

MARKET COMMENTARY

FIXED INCOME MARKET REVIEW AND OUTLOOK

June 2020



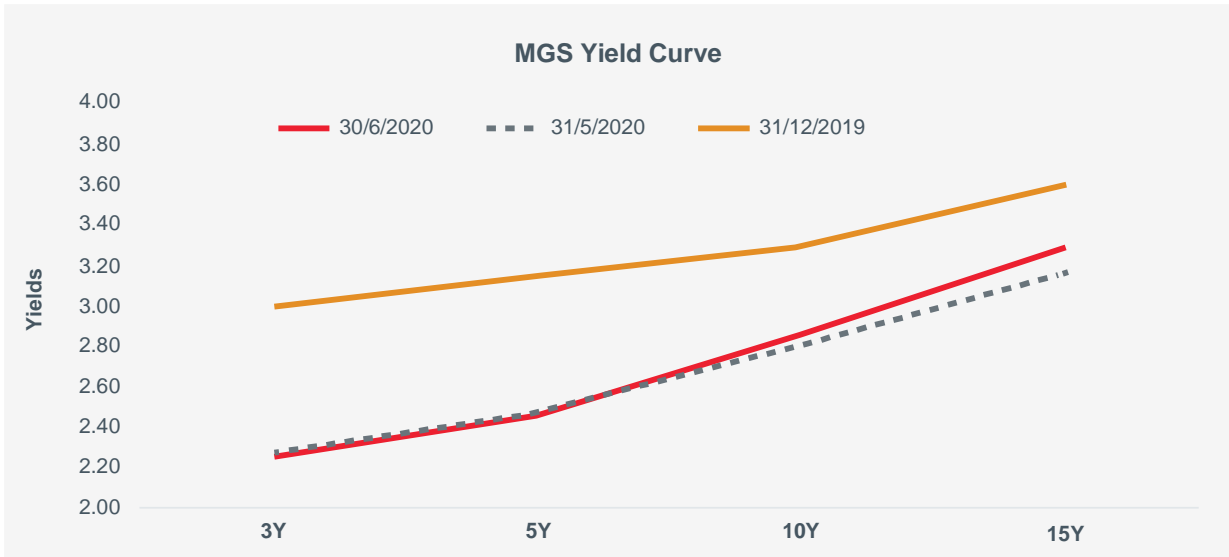


REVIEW

- ▶ The Government recently announced its third stimulus package - short-term economic recovery plan (“PENJANA”), worth around RM 35b, targeting wage subsidies, subsidizing consumer spending and extending financing to SMEs. The direct fiscal impact of PENJANA is expected to be around RM18b or 1.2% of GDP. The total of 3 stimulus packages announced to date, is expected to bring the 2020 fiscal deficit to 5.8% - 6.0% of GDP against the 3.2% of GDP deficit target at the start of the year.
- ▶ May 2020’s headline inflation declined by 2.9% YoY, the same as April 2020’s reading of -2.9% YoY and slightly lower than consensus expectations of -2.7 YoY, primarily due to a price deflation in the Transport category, -20.8% YoY (Apr: -21.5%). Meanwhile, core inflation was lower at 1.1% YoY (Apr: 1.3% YoY).
- ▶ Malaysia’s sovereign bond yield curve steepened in June 2020 as 3-, 5-, 10- and 15-years MGS yields moved -2bps, -1bps, +6bps and +12bps to close at 2.25%, 2.46%, 2.86% and 3.29% respectively. The market movement generally reflected the concern on bond supply risk amid funding need from the PENJANA stimulus package, in which the supply is expected to come from the longer-term government bonds, while shorter tenors were supported by some investors positioning for a speculated rate cut in July. Similarly, MGII yield curve steepened during the month, as 3-, 5-, 10- and 15-year GII yields closed -1bps, +6bps, +17bps and +17bps at 2.31%, 2.53%, 2.87% and 3.41%, respectively.
- ▶ There were 3 government bond auctions in June:
 - ▶ RM4.5b re-opening of the 3-year GII averaging 2.306% at a bid-to-cover ratio of 2.502x.
 - ▶ RM3.0b new issuance of the 30-year MGS averaging 4.065% at bid-to-cover ratio of 2.167x.
 - ▶ RM3.5b re-opening of the 20-year GII averaging 3.761% at a bid-to-cover ratio of 2.055x.

BENCHMARK	31/12/2019 Yield	29/5/2020 Yield	30/6/2020 Yield	MOM Change	YTD Change
3-year MGS	2.98%	2.27%	2.25%	-2 bps	- 73 bps
5-year MGS	3.15%	2.47%	2.46%	- 1 bps	- 69 bps
10-year MGS	3.30%	2.80%	2.86%	+6 bps	- 44 bps
15-year MGS	3.60%	3.17%	3.29%	+ 12 bps	- 31 bps

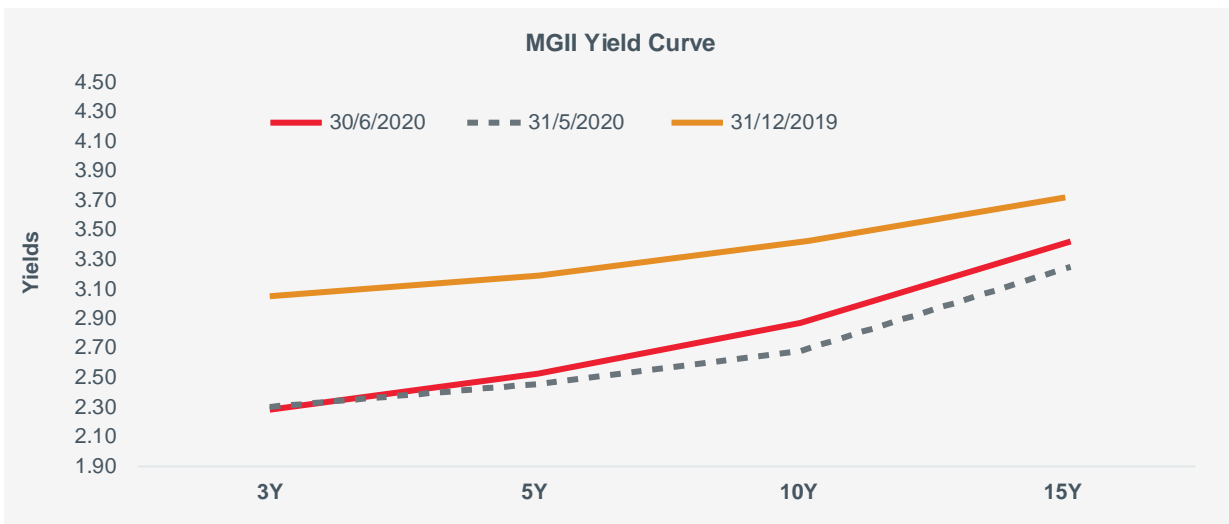
Source: Bloomberg



Source: Bloomberg

BENCHMARK	31/12/2019 Yield	29/5/2020 Yield	30/6/2020 Yield	MOM Change	YTD Change
3-year MGII	3.06%	2.32%	2.31%	- 1 bps	- 75 bps
5-year MGII	3.19%	2.47%	2.53%	+ 6bps	- 66 bps
10-year MGII	3.42%	2.70%	2.87%	+17 bps	- 55 bps
15-year MGII	3.72%	3.24%	3.41%	+ 17 bps	- 31 bps

Source: Bloomberg



Source: Bloomberg



OUTLOOK

- ▶ White House trade advisor Peter Navarro caused a minor storm when he stated that the US-China trade deal was “over” before President Trump tweeted that the trade was fully intact. Despite the survival of the trade deal for now, US-China tensions continue as the US Congress approved The Hong Kong Autonomy Act against Chinese and Hong Kong authorities in response to China passing a new national security law for Hong Kong. The Act imposes sanctions on banks that do business with Chinese officials who are involved in cracking down on pro-democracy protesters in Hong Kong. As this is an election year in the US, both Republicans and Democrats wish to appear as being tough on China, therefore there is likely to be no rapprochement between the two countries in the near term. Global market sentiment is expected to remain cautious on this geopolitical risk.
- ▶ The US Federal Reserve (“Fed”) held rates steady at 0-0.25% during its June FOMC meeting. In the FOMC minutes, Fed officials noted that “the current stance of monetary policy remained appropriate” and the need for a “highly accommodative monetary policy for some time”. Fed officials also noted the need for more forward guidance, a policy where the Fed states and commits to the direction of future interest rates and asset purchases. The US Treasury yield curve steepened slightly in June where 2y fell 1bps to 0.15% and 10y rose 1bps to 0.68%. In the near term, we expect yield movement to be driven by risk sentiment, especially on the back of the concerns of a second wave of Covid-19 pandemic and US-China tension.
- ▶ In June, S&P revised Malaysia’s sovereign rating outlook from stable to negative driven by the negative impact of the Covid-19 pandemic on the country’s economic growth and fiscal position. Nonetheless, we only saw short-lived selling sentiment and the bond market was well-supported by local investors as the rating outlook revision was not unexpected. Going forward the government’s long-term commitment to fiscal discipline, political stability and economic growth will be key rating factors to monitor.
- ▶ Ex-Prime Minister Mahathir Mohammad withdrew from the contest to be Pakatan Harapan’s prime minister candidate and in an unexpected move, mooted for Sabah chief Minister Shafie Apdal to be Pakatan’s Prime Minister candidate. Mahathir’s no-confidence motion against the new government in set to be tabled in the upcoming Parliament sitting scheduled from 13 July to 27 Aug 2020. Should the current government lose a vote of confidence in parliament, a snap election may ensue – a development that will likely lead to volatilities in the domestic bond market.
- ▶ Stimulus packages announced by the Government is expected to increase net government bond supply up to RM 100b in 2020 compared to RM 52b at the start of the year. Nonetheless the additional supply is expected to be partly absorbed by BNM’s earlier cut of SRR by 100 bps to 2.00% and allowance for financial institutions to recognize MGS and GII as part of their reserve requirements which will release around RM46b of liquidity into the banking system.
- ▶ BNM reduced the overnight policy rate (OPR) by 25 bps on 7 July to provide additional stimulus to accelerate the pace of economic recovery following the sharp contraction in 2Q2020. BNM stated “that the Bank will continue to utilize its policy levers as appropriate to create enabling conditions for a sustainable economic recovery”, indicating that it will ease monetary policy further if circumstances require it.
- ▶ There are re-openings of 3y MGS, 10y GII and 15y MGS (expected total RM 15bn) in July against RM 8bn in government bond maturity. We expect the issuances to be well supported given the ample domestic liquidity and dovish policy outlook. On the corporate bond front, we expect demand for corporate bonds to be mixed, with a preference for higher quality names. Corporate issuances have slowed in recent months as corporates assess their funding needs on the back of low economic activity.



Table 1: Indicative Rates

	30-Jun-20
MBB O/N*	0.50%
MBB1-Week*	0.60%
MBB 1-Mth FD*	1.90%
MBB 6-Mth FD*	2.05%
MBB 1-Year FD*	2.10%
1-mth BNM MN	2.02%
3-mth BNM MN	2.03%
3-mth KLIBOR	2.28%
CP	
1-mth (P1)	2.66%
3-mth (P1)	2.83%

Source: Bloomberg/Bondstream

* Maybank2u.com.my

Table 2: Indicative Bond Yields (%)

	3yr	5yr	7yr	10yr	15yr
MGS	2.27	2.44	2.68	2.94	3.36
GII	2.33	2.57	2.73	2.84	3.48
Swap rate*	2.11	2.31	2.53	2.69	3.01
AAA	2.91	3.07	3.22	3.41	3.72
AA1	3.08	3.25	3.40	3.60	3.93
AA2	3.22	3.40	3.55	3.76	4.13
AA3	3.35	3.55	3.71	3.94	4.32
A1	4.21	4.50	4.77	5.13	5.68
A2	5.01	5.42	5.81	6.28	7.02
A3	5.81	6.37	6.83	7.46	8.30

Source: Bloomberg*/Bondstream



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