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MARKET COMMENTARY

FIXED INCOME MARKET REVIEW AND OUTLOOK

December 2021

REVIEW

- The Federal Reserve (the **"Fed")** kept its federal funds rate unchanged at 0%-0.25% at its Dec 2021 meeting but removed the word "transitory" from its inflation narrative and acknowledged that high inflation may be more persistent. It announced the doubling in pace of its tapering, seeking to wrap it up by Mar 2022 instead of the previously expected mid-2022 finish. In addition, the central bank's revised dot plot showed that the majority of officials now expect three rate hikes in 2022 and three more hikes in 2023. It is also worth noting that the Fed discussed about shrinking its balance sheet at the Dec 2021 meeting although no decision was made. Meanwhile, the Fed lowered its 2021 economic growth and unemployment forecasts to 5.4% and 4.3% respectively but increased its PCE and core PCE forecasts to 5.3% and 4.4% from 4.2% and 3.7% previously.

- Following the Fed's more hawkish stance, a range of central banks also signalled tighter monetary policy going forward. Of note, Bank of England surprised the market with a 15bps rate hike to 0.25% in Dec 2021 despite the uncertainty surrounding the Omicron variant. The central bank expects inflation to hit 5% in the spring of 2022 before moderating to around 2% in late-2023. Meanwhile, the European Central Bank also announced that its Pandemic Emergency Purchase Programme will be reduced gradually and discontinued in Mar 2022 although its net purchases under the Asset Purchase Programme will continue to avoid a quantitative easing cliff edge.

- The US' 3Q2021 real GDP grew 2.3% on an annualized rate. The 0.2% upward revision was driven mainly by higher personal consumption, particularly for services, business fixed investment and changes in inventories. Meanwhile, the passing of the larger USD1.75tr social spending package is still in doubt after news emerged that Senator Manchin would not support the bill on concerns over inflation and long-term debt impact. However, it is reported that efforts to revise the package are ongoing although the bill is unlikely to be ready for floor action in the near future. Separately, the US averted a looming government shutdown after the Senate reached an agreement that would allow Democrat to raise the debt ceiling on their own.

- China's Nov 2021 PPI eased slightly to 12.9% YoY (Oct 2021: +13.9% YoY) on softer coal and industrial metal prices while headline CPI rose further to 2.3% YoY (Oct 2021: 1.5% YoY) attributable mainly to higher food and transport fuel prices. Meanwhile, China's exports again topped market expectation for four consecutive months in Nov 2021, registering a strong growth of 22.0% YoY as external demand remained resilient heading into the holiday season. As risks to growth remain, there have been increasing signs of pro-growth policy support with "economic stability" now being China's 2022 priority objective.

- In Malaysia, all states have transitioned to the final phase of the national recovery plan effective 3 Jan 2022. Finance Minister Tengku Zafrul has reiterated that Malaysia is on track to achieve the targeted growth of 3%-4% in 2021 despite the emergence of Omicron. Meanwhile, various measures have been undertaken to keep prices of essential goods in check. On a separate note, the Regional Comprehensive Economic Partnership agreement has come into force on 1 Jan 2022 for 10 participating countries, namely, Australia, Brunei, Cambodia, China, Japan, Laos, New Zealand, Singapore, Thailand and Vietnam. Malaysia is amongst the remaining five countries that have yet to ratify the agreement.

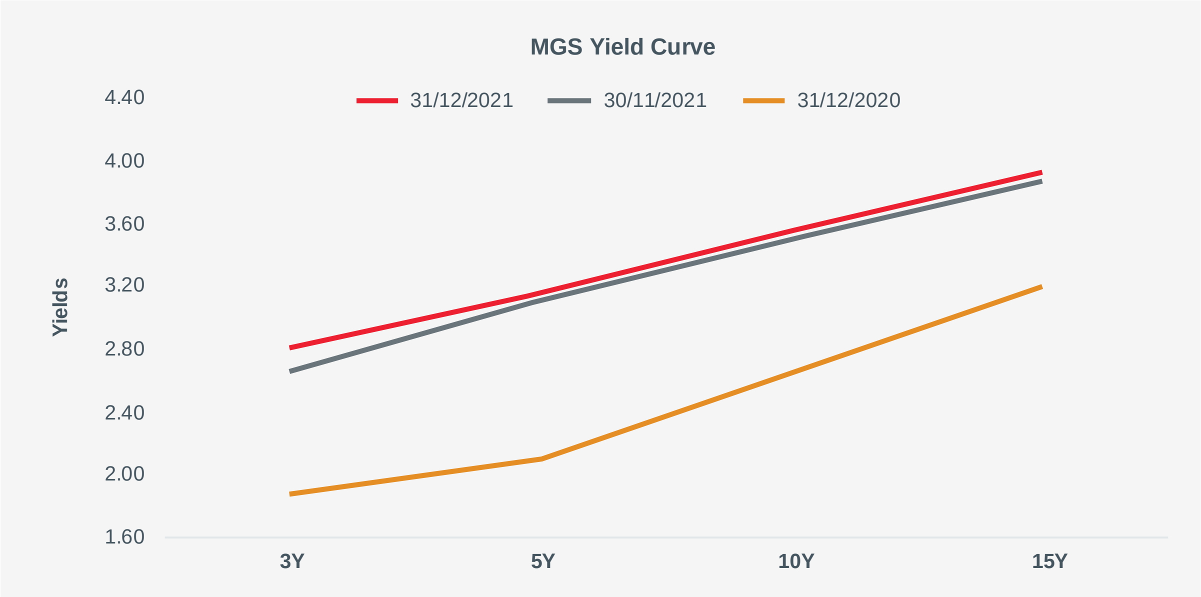
- Malaysia's agreement with Singapore to allow quarantine-free air and land travels via the Vaccinated Travel Lane scheme suffered a setback after the countries agreed to temporarily suspend the bus and air tickets sales from 23 Dec 2021 to 20 Jan 2022 due to an increase of imported Covid-19 cases in Singapore.

- In Dec 2021, Malaysia's sovereign yield curve ended flatter. The yields of the 3-, 5-, 10- and 15-year MGS rose 14bp, 4bps, 5bps and 8bps respectively to close the month at 2.81%, 3.16%, 3.56% and 3.94% respectively. Similarly, the MGII curve also closed flatter as yields of the 3-, 5-, and 10-year MGII increased 14bps, 11bps and 6bps respectively to end the month at 2.90%, 3.21% and 3.62% respectively while the 15-year MGII fell 6bps to close at 3.93%.

- Two auctions were held in the month of Dec 2021, the re-opening of the 7-year MGII 08/28 and the re-opening of the 3-year MGS 06/24. The auctions received an average bid-to-cover ratio of 1.703x.
  - RM3.5b re-opening of 7-year MGII averaging 3.481% at a bid-to-cover ratio of 2.247x; and
  - RM4.5b re-opening of 3-year MGS averaging 2.881% at a bid-to-cover ratio of 1.158x

BENCHMARK	Dec 2020 Yield	Nov 2021 Yield	Dec 2021 Yield	MOM Change	YTD Change
3-year MGS	1.88%	2.67%	2.81%	+ 14 bps	+ 93 bps
5-year MGS	2.10%	3.12%	3.16%	+ 4 bps	+ 106 bps
10-year MGS	2.65%	3.51%	3.56%	+ 5 bps	+ 91 bps
15-year MGS	3.19%	3.86%	3.94%	+ 8 bp	+ 75 bps

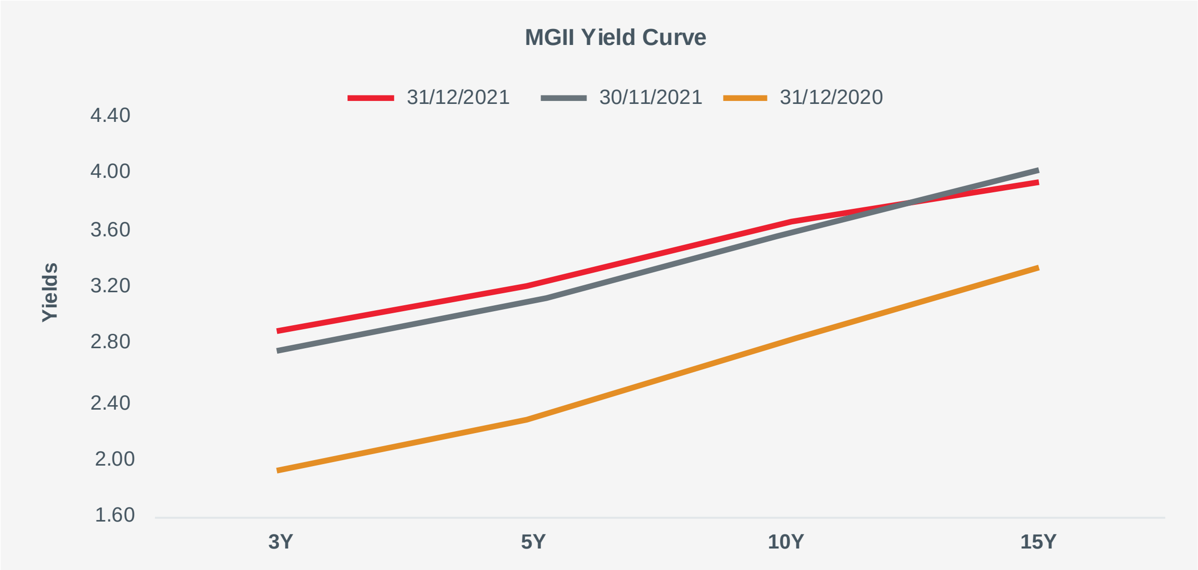
Source: Bloomberg



Source: Bloomberg

BENCHMARK	Dec 2020 Yield	Nov 2021 Yield	Dec 2021 Yield	MOM Change	YTD Change
3-year MGII	1.92%	2.76%	2.90%	+ 14 bps	+ 98 bps
5-year MGII	2.26%	3.10%	3.21%	+ 11 bps	+ 95 bps
10-year MGII	2.81%	3.56%	3.62%	+ 6 bps	+ 81 bps
15-year MGII	3.32%	3.99%	3.93%	- 6 bps	+ 61 bps

Source: Bloomberg



Source: Bloomberg

OUTLOOK

- The confirmed Covid-19 cases continue to rise across the world, surpassing 290m with approximately 5.4m fatalities. While the surge in new Omicron cases has prompted a new wave of restrictions in certain European countries, the fears are easing after studies across the world suggested that the variant may be less severe and current vaccines, especially with boosters, are effective against the variant. Further mitigating the concern are the increasing vaccination rate and the swift response from vaccine producers. Globally, the daily vaccinate rate now stands at 37.8m doses and it will take another 3 months to have 75% of the population receiving at least one dose at this pace. In addition, we believe major economies are now better prepared to deal with a resurgence. That said, the rapid spread of the virus is likely to result in changes in consumer and business behaviours as well as exert pressure on health systems although we believe the “Living with Covid-19” policy that has been adopted by many countries including Malaysia will not be significantly affected.

- Malaysia’s headline inflation rate surged further to 3.3% YoY in Nov 2021 (Oct: 2.9% YoY), the highest level in five months, attributable mainly to increases in costs of Transport (+12.7% YoY), Food & Non-Alcoholic Beverages (+2.7% YoY) as well as Housing, Water, Electricity, Gas and Other Fuels (+3.4% YoY). Year-to-date, inflation growth averaged 2.3% while core CPI remained subdued at 0.7% YoY, an indication that domestic demand has yet to fully recover. Full year inflation rate is expected to come in within Bank Negara Malaysia’s (“BNM”) forecast of 2.0% to 3.0%.

- The 2022 Auction Calendar released by BNM shows that there will be a total of 36 auctions against 37 in 2021. Meanwhile, the number of auctions with private placement will come in lower at 14 compared to 18 in the previous year although the number of auctions with tenure of 10 years and above total 21 against 2021’s 20. We expect another record year of gross MGS/MGII supply of RM160-165b in 2022 (2021: RM160b), after taking into consideration total MGS/MGII maturity amount of RM65.3b and 2022’s budget deficit of RM97.5b.

- There will be three auctions in the month of Jan 2022, the re-opening of the 5Y MGS 11/26, the new 10.5Y MGS 07/32 and the re-opening of the 15Y MGII 07/36. While there is still ample liquidity in the system, the outcome of these auctions is likely to be influenced by prevailing market sentiment. On the corporate front, we expect mixed demand for corporate bonds as investors continue to be selective in their investments.

- In 2021, Malaysia’s sovereign yield curve has moved much higher since early of the year, underpinned by the narrative of a recovering economy and higher inflationary pressure. For 2022, we believe the main themes surrounding the Malaysian bond market are the still evolving pandemic situation, Malaysia’s economic growth, monetary policy normalization, potential general elections and the supply-demand dynamics. On balance, we still see bonds facing some headwinds in the medium-term on the back of expected sustainable economic recovery, still unfavourable demand-supply dynamics and inflationary pressures. Going forward, we believe the performance of the bond market will continue to be dictated by economic data, effectiveness of vaccines as well as global risk sentiment.

Table 1: Indicative Rates (%)	
	31-Dec-21
MBB O/N*	0.25
MBB1-Week*	0.35
MBB 1-Mth FD*	1.50
MBB 6-Mth FD*	1.80
MBB 1-Year FD*	1.85
1-mth BNM MN	1.78
3-mth BNM MN	1.80
3-mth KLIBOR	2.05
CP	
1-mth (P1)	2.24
3-mth (P1)	2.45

Source: Bloomberg/Bondstream
* Maybank2u.com.my

Table 2: Indicative Bond Yields (%)					
	3yr	5yr	7yr	10yr	15yr
MGS	2.97	3.18	3.44	3.63	3.98
GII	3.00	3.28	3.46	3.68	3.93
Swap rate*	2.74	2.94	3.19	3.38	3.66
AAA	3.25	3.60	3.94	4.10	4.35
AA1	3.36	3.74	4.07	4.23	4.52
AA2	3.47	3.87	4.20	4.36	4.68
AA3	3.58	4.00	4.33	4.49	4.83
A1	4.46	4.84	5.19	5.48	5.96
A2	5.17	5.67	6.11	6.58	7.19
A3	5.88	6.51	7.04	7.69	8.41

Source: Bloomberg*/Bondstream

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