# *Monthly Perspective – May 2019*

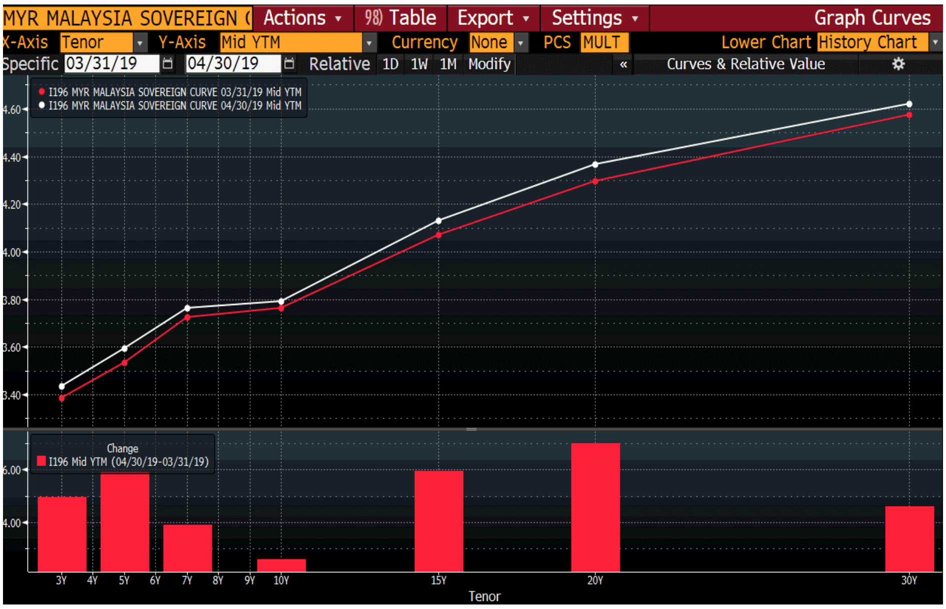
## *MYR Bond Market*

## *Recapping the month of April*

***US Treasuries (UST's)*** *strengthened on safe-haven bids whilst bucking the trend displayed by most other countries. UST yields ended higher albeit between 1-11bps as the curve steepened and moved higher; with the insignificant inversion still appearing on the front-end. The improvement in US payrolls for April and strong 1Q GDP growth was partly offset by weak inflation outlook which sagged below policy-makers' 2.0%. The front-end UST 2Y yield edged 1bps higher MOM at 2.27% levels whilst the 10Y, which depicts as a benchmark for US mortgage rates and also inflation indicator, saw lesser volatility in April; ranging between a low of 2.41% and a high of 2.59% levels and closed 9bps sharply higher MOM at 2.50%. The US Dollar meanwhile ended stronger against all G10 currencies, pushing the Dollar Index higher to 97.5 levels. The steeper UST yield curve continued to see the non-threatening inversion on the front-end whilst the 2s10s spread widened another 9bps to about 23bps.*

*On the local front,* ***MYR bonds*** *saw sharp reversal of foreign holdings in April amid still robust secondary trade volume of RM90.9b (March:RM101.4b) due to concerns emanating from knee-jerk reactions on potential bond allocation changes by the Norwegian Sovereign Fund and FTSE Russell Index despite earlier dovish comments from BNM. The foreign holdings of total Malaysian debt securities dropped by RM8.8b MOM to RM180.1b; reversing the earlier two (2) months of inflows of RM7.5b. The percentage of foreign holdings of MYR government bonds (MGS + GII +SPK) fell to 21.9% or RM162.3b of total outstanding issuance. (March: RM169.4b or 22.8%). Overall benchmark MGS/GII bonds yields ended higher as bonds rallied between 2-6bps. The 5Y MGS 4/23 moved 6bps higher at 3.59% whilst the much-watched 10Y MGS 8/29 edged 2bps higher from 3.77% to 3.79% levels. (The 10Y saw a low-high range of 3.73-90% levels). Corporate Bonds/Sukuk similarly saw a drop of RM1.52b in the levels of foreign holdings at RM11.9b. Local institutional investors were still net buyers causing yields to grind lower on solid demand on sustained volume of RM16.0b versus RM16.6b prior month.*

***MYR sovereign curve (MGS)***




*Source : Bloomberg*

### *April NFP data solid but "transitory" inflation is ongoing despite strong economic figures; no rate hike expected…*

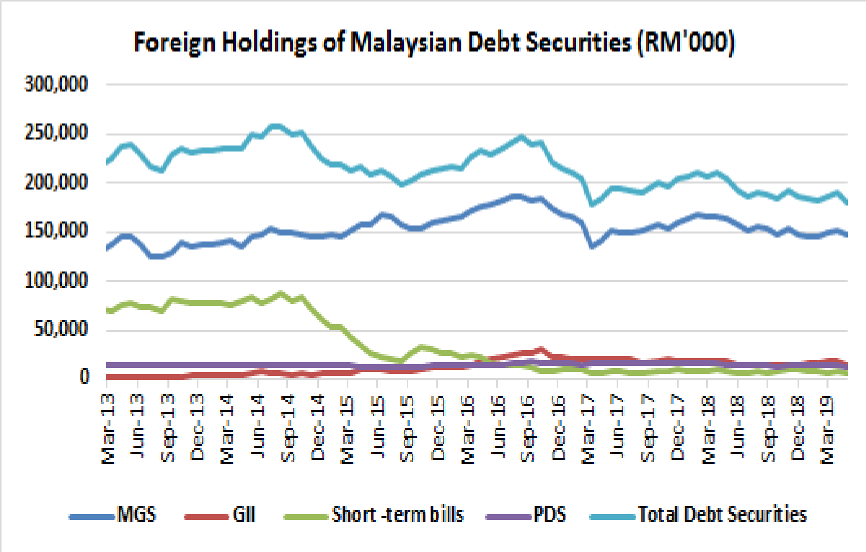
**April Non-Farm Payrolls ("NFP")** surprised on the upside with the printing of 263k compared to market consensus of 190k (March: revised upwards slightly to 189k) pointing to a strong labor market continuing the prior month's strong hiring. The pace of hiring confirmed that it had recovered from its February "blip" and is more than enough to keep the unemployment rate falling yet further to a low of 3.6%. That is believed to be largely attributable to slight declining participation rate of 62.8% from 63% previously. However the continued soft print on hourly wages MOM i.e. 0.2% (previous: +0.2%) did not dent the euphoria and indicated a robust economy that isn't pressuring up inflation; hence a "goldilocks" report that vindicates Fed's patience on interest rate outlook.

The US central bank left rates unchanged at 2.25-2.50% as widely expected and its **May FOMC** statement stated that economic growth has slowed from its solid rate whilst signaling that rates may stay pat this year with a potential rate hike only in 2020. The current Fed's dot plot still reflects the present case for no interest rate movement i.e. neither increases nor reduction (note that the Fed was projecting two rate hikes during early-part of 2019) with the next FOMC meet on 19th June. The Fed's patience is lauded but it may even take a dovish stance as global risks weigh on the economic outlook amid muted inflation outlook. Meanwhile there has been no change in the balance sheet tapering/roll-off which is scheduled to be halted end-September. Its preferred inflation measure for February i.e. the core PCE was lower at 1.6% YOY compared to 1.8% seen prior month.

### *Foreign holdings of overall MYR bonds nosedived in April on potential foreign portfolio and index adjustments*

Foreign holdings of MYR bonds slipped in April by RM8.8b or 4.6% to RM180.1b following two (2) earlier consecutive increases in the months of February and March. The non-resident holdings of MGS was substantially lower by RM3.5b to RM147.1b (representing 37.1% of total outstanding) whereas total MYR Government bonds (i.e. MGS+GII+SPK) holdings similarly saw a drop of RM7.1b to RM162.3b (representing 21.9% of total outstanding) despite slightly higher issuances of ~RM500m for the month; a 10-month high.

The recent reports on the Norwegian Sovereign Fund and FTSE Russell index's intention to underweight MYR bonds saw a sell-off in MYR govvies. This coupled with Moody's statement of credit impact on government's assistance on FELDA reversed inflows seen in earlier months. YTD overall, MYR bonds saw a net decrease in foreign holdings of RM4.7b in the first four (4) months of 2019 while equities saw a further net outflow of RM2.8b. On the currency side, the MYR weakened by 1.3% at 4.1347 levels as at end-April and also against most Asian currencies save for the Korean Won. At the time of writing, USDMYR is trading at 4.1643 post OPR cut of 25bps.




*Source: BNM, HLB Research*

### *MPC cuts OPR from 3.25% to 3.00% on global & domestic concerns*

BNM cut the OPR from 3.25% to 3.20% at the 3rd MPC meeting of the year on 7th of May citing downside risks to growth from heightened uncertainties in both global and domestic environment, trade tensions and extended weakness in commodity-related sectors. (The last policy move was a 25bps hike in January 2018 whilst the last rate cut was in July 2016). Despite the rebound in inflation i.e. both headline and core to 0.2% and 1.6% respectively from two (2) earlier consecutive months of deflation in February and January, the central bank had acknowledged that inflation is expected to be low mainly due to policy measures; including the price ceiling on domestic fuel prices until the middle of this year. Lower rates would allow existing portfolio investors to potentially reap gains but also diminish the yield appeal of MYR bonds by fresh investors. We opine that the government is not taking any chances on US tariff threats to global demand and would like to preserve the degree of monetary accommodativeness. Hence the tone has turned neutral suggesting no immediate plans for further rate cuts for the year.

### *MYR government bond auctions saw decent demand in April for 15Y MGS and 5Y GII*

The three (3) government bond tenders concluded for the month of April 2019 under the auction calendar included the reopening of the 15Y MGS 11/33 which we briefly mentioned in our previous monthly report (solid BTC ratio of 2.792x; averaging 4.065%), new issuance of 5Y GII 10/24 and also the reopening of 7Y MGS 7/26. Overall weighted average BTC for the month tapered off to 2.14x mainly due to the weak final auction for the later at a mere 1.51x. (Compare this with both the entire 33 auctions for 2018 which notched a BTC ratio of 2.29x). Tenders for the month received decent bids from mainly local followed by institutional investors. The subsequent auction in early-May at the time of writing include the new issuance of 30Y GII 11/49 that will gauge investors and inter-bank players interest in Malaysia's long bond.

MGS/GII issuance pipeline in 2019

| No | Stock | Tenure (yrs) | Tender Month | Quarter | Tender Date | Projected Issuance Size (RM mil) | Actual Auction Issuance (RM mil) | Private Placement | Amt Issued YTD | BTC (times) | Low | Average | High | Cut-off |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 1 | 10.5-yr New Issue of GII (Mat on 07/29) | 10 | Jan | Q1 | 8/1/2019 | 4,000 | 3,500 | 1,500 | 3,500 | 4.067 | 4.110 | 4.130 | 4.135 | 86.1% |
| 2 | 7.5-yr New Issue of MGS (Mat on 07/26) | 7 | Jan | Q1 | 14/1/2019 | 4,000 | 3,500 | 500 | 7,000 | 2.216 | 3.890 | 3.906 | 3.914 | 8.2% |
| 3 | 5-yr Reopening of GII (Mat on 11/23) | 5 | Jan | Q1 | 30/1/2019 | 3,500 | 4,000 | | 11,000 | 1.974 | 3.845 | 3.862 | 3.873 | 19.0% |
| 4 | 10.5-yr New Issue of MGS (Mat on 08/29) | 10 | Feb | Q1 | 14/2/2019 | 4,000 | 4,000 | 1,000 | 15,000 | 2.536 | 3.867 | 3.885 | 3.893 | 31.6% |
| 5 | 15-yr Reopening of GII (Mat on 06/33) | 15 | Feb | Q1 | 27/2/2019 | 3,000 | 2,000 | 1,000 | 17,000 | 3.906 | 4.360 | 4.370 | 4.375 | 33.9% |
| 6 | 3-yr Reopening of MGS (Mat on 03/22) | 3 | Mar | Q1 | 7/3/2019 | 3,500 | 3,000 | | 20,000 | 3.132 | 3.470 | 3.483 | 3.487 | 70.0% |
| 7 | 20.5-yr New Issue of GII (Mat on 09/39) | 20 | Mar | Q1 | 14/3/2019 | 4,000 | 2,500 | 2,000 | 22,500 | 2.758 | 4.445 | 4.467 | 4.480 | 14.5% |
| 8 | 30-yr Reopening of MGS (Mat on 07/48) | 30 | Mar | Q1 | 21/3/2019 | 3,500 | 2,000 | 2,000 | 24,500 | 1.718 | 4.550 | 4.591 | 4.629 | 25.0% |
| 9 | 7-yr New Issue of GII (Mat on 03/26) | 7 | Mar | Q1 | 28/3/2019 | 4,000 | 4,000 | | 28,500 | 2.330 | 3.699 | 3.726 | 3.745 | 21.2% |
| 10 | 15-yr Reopening of MGS (Mat on 11/33) | 15 | Apr | Q2 | 5/4/2019 | 4,000 | 2,500 | 1,000 | 31,000 | 2.792 | 4.058 | 4.065 | 4.071 | 40.0% |
| 11 | 5.5-yr New Issue of GII (Mat on 10/24) | 5 | Apr | Q2 | 12/4/2019 | 4,000 | 3,500 | | 34,500 | 2.313 | 3.627 | 3.655 | 3.669 | 64.7% |
| 12 | 7-yr Reopening of MGS (Mat on 07/26) | 7 | Apr | Q2 | 29/4/2019 | 3,000 | 3,500 | 500 | 38,000 | 1.510 | 3.735 | 3.757 | 3.777 | 75.0% |
| 13 | 30.5-yr New Issue of GII (Mat on 11/49) | 30 | May | Q2 | | 3,000 | | | | | | | | |
| 14 | 10-yr Reopening of MGS (Mat on 08/29) | 10 | May | Q2 | | 3,500 | | | | | | | | |
| 15 | 15.5-yr New Issue of GII (Mat on 11/34) | 15 | May | Q2 | | 4,000 | | | | | | | | |
| 16 | 5-yr New Issue of MGS (Mat on 06/34) | 5 | Jun | Q2 | | 4,000 | | | | | | | | |
| 17 | 20-yr Reopening of GII (Mat on 09/39) | 20 | Jun | Q2 | | 3,000 | | | | | | | | |
| 18 | 15-yr New Issue of MGS (Mat on 07/34) | 15 | Jul | Q3 | | 4,000 | | | | | | | | |
| 19 | 7-yr Reopening of GII (Mat on 3/26) | 7 | Jul | Q3 | | 3,000 | | | | | | | | |
| 20 | 30-yr Reopening of MGS (Mat on 07/48) | 30 | Jul | Q3 | | 2,500 | | | | | | | | |
| 21 | 5-yr Reopening of GII (Mat on 10/24) | 5 | Aug | Q3 | | 3,500 | | | | | | | | |
| 22 | 20-yr Reopening of MGS (Mat on 06/38) | 20 | Aug | Q3 | | 3,000 | | | | | | | | |
| 23 | 10-yr Reopening of GII (Mat on 7/29) | 10 | Aug | Q3 | | 3,500 | | | | | | | | |
| 24 | 7-yr Reopening of MGS (Mat on 07/26) | 7 | Sep | Q3 | | 3,500 | | | | | | | | |
| 25 | 15-yr Reopening of GII (Mat on 11/34) | 15 | Sep | Q3 | | 3,000 | | | | | | | | |
| 26 | 10-yr Reopening of MGS (Mat on 08/29) | 10 | Oct | Q4 | | 3,000 | | | | | | | | |
| 27 | 20-yr Reopening of GII (Mat on 09/39) | 20 | Oct | Q4 | | 2,500 | | | | | | | | |
| 28 | 5-yr Reopening of MGS (Mat on 06/24) | 5 | Oct | Q4 | | 3,500 | | | | | | | | |
| 29 | 3.5-yr New Issue of GII (Mat on 05/23) | 3 | Nov | Q4 | | 4,000 | | | | | | | | |
| 30 | 20.5-yr New Issue of MGS (Mat on 05/40) | 20 | Nov | Q4 | | 4,000 | | | | | | | | |
| 31 | 10-yr Reopening of GII (Mat on 07/29) | 10 | Nov | Q4 | | 3,000 | | | | | | | | |
| 32 | 15-yr Reopening of MGS (Mat on 07/34) | 15 | Dec | Q4 | | 3,000 | | | | | | | | |
| | Gross MGS/GII supply in 2019 | | | | | 104,000 | | 9,500 | | | | | | |

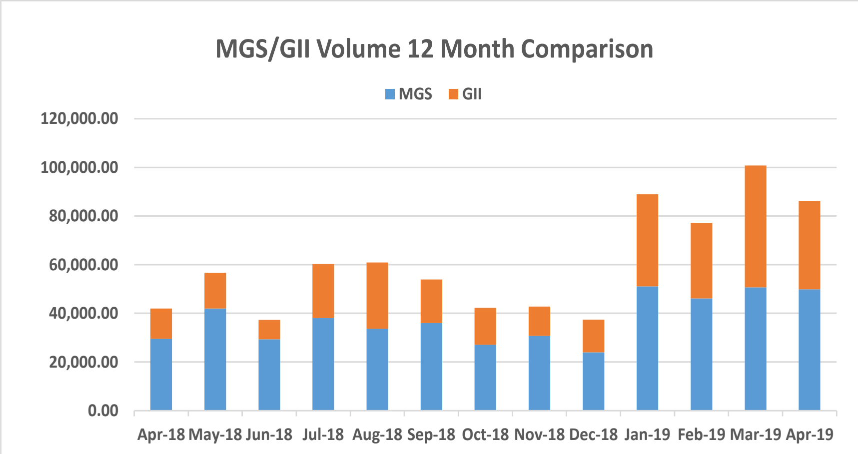
*Source: BNM, HLB Research*

### *Trading volume for MGS/GII retracts slightly in April…*

Trading volume for MYR govvies pulled back almost by 10% from RM90.9b in April compared to prior month's RM101.4b. Strong traction was still seen across the curve with substantial frequency of trades and nominal amounts done in the short off-the-run 19-20's (ended largely lower between 1-3bps), 23's and 28's (these ex-5Y and 10Y benchmarks ended largely higher instead between 6-10bps). Both MGS and GII 7Y and 10Y benchmarks (ended about 2-5bps higher as well) also saw active trades. The 19's and 20's MGS/GII bonds alone formed almost 15% of total volume for the month under review. It is believed that off-shore investors were net sellers instead for MYR govvies in April due to risk-off sentiments and the sudden turnaround in foreign holdings of local bonds was due to a knee-jerk reaction towards announcements by:

- Norway's US$1.0 billion Sovereign Wealth Fund (SWF) which plans to omit emerging market (EM) bonds from its fixed-income benchmark; and
- FTSE Russell that placed Malaysia on the watch list for potential exclusion from the World Government Bond Index (WGBI).

The month under review saw Malaysian bonds reverse and head south unlike February-March rally as investors await local regulatory moves on deepening and providing stronger liquidity in both bond and Ringgit market.



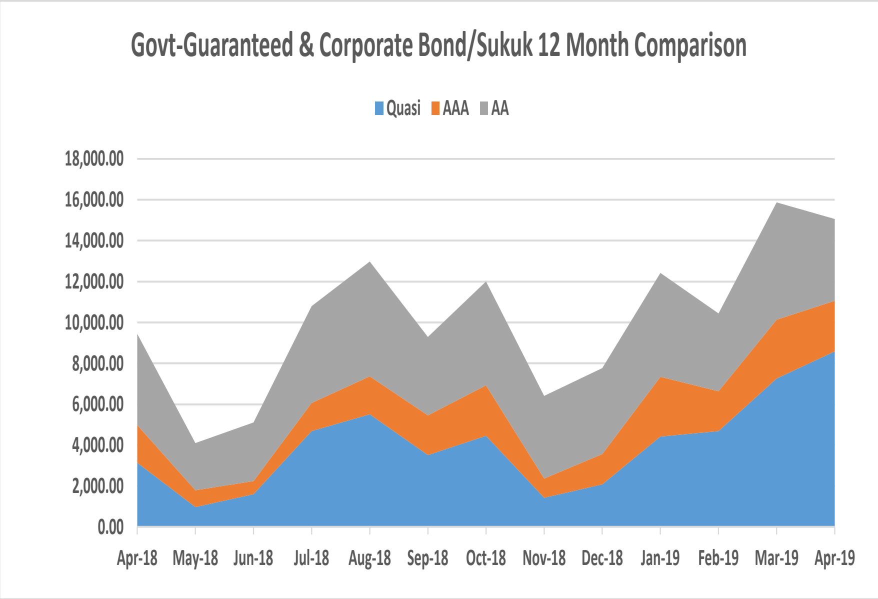

*Source : BPAM, Bloomberg, HLB Research*

## *Corporate bonds/Sukuk continue to register solid demand…*

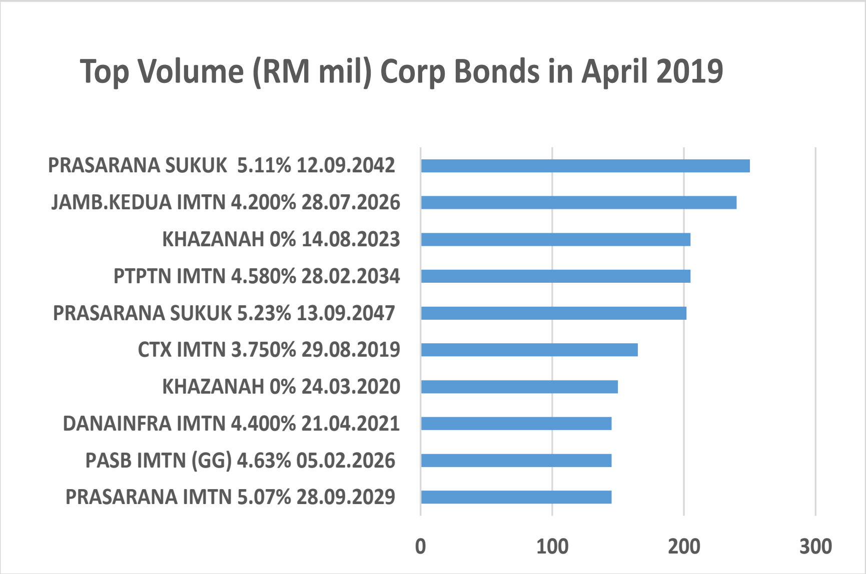
In the secondary market, Corporate bonds/Sukuk (including Govt-Guaranteed bonds) saw secondary market trading volume almost maintain its momentum from RM16.6b in March to RM16.0b in April. Fund managers/portfolio investors continued to actively bid in the secondary market in the hunt for yield coupled with liquidity on various credits (Govt-guaranteed bonds i.e. GG papers have been grouped together for ease of reference). The rate pause outlook in the US by the Fed and dovish-tone by BNM generally spurred a risk-on demand for EM assets in April.

Investor appetite for GG maintained traction MOM; increasing to 57% in April (March: 46%) whilst AA-rated bonds saw a dip to 26% of overall of transactions (March: 36%). The fresh supply of GG bond issuances was fully-taken up by investors with almost RM7.1b of DANAINFRA, LPPSA and SME bonds issued for the month. AAA-rated PLUS 29 and Govt-guaranteed DANAINFRA 4/26 topped the monthly volume; closing 4bps lower and 4bps higher respectively at 4.23% and 3.91% for the month respectively compared to previous-done levels. This was followed by both PLUS 23 and DANAINFRA 5/31 which also rallied between 1-30bps to close at 4.02% and 4.12% respectively.

Appetite in the credit space was mainly seen in a wide range of bonds namely infrastructure-related bonds including telecommunication, toll and energy sub-sectors of the economy. AAA-rated TELEKOM 23-28, MANJUNG 21-31, PLUS 20-31 together with AA-rated SEB 22-36, EDRA Energy 23-37, Southern Power 26-33, DUKE 35-37 and also YTL Power 23-28 were actives an saw tremendous interest for the month. In the banking space high frequency of trades were noticed for both SABAHDEV and SDBB bonds for the 2020-2026 tranches followed by Affin Islamic Bank papers. (We have excluded single-A rated and non-rated papers in the illustration below).




*Source : BPAM, Bloomberg, HLB Research*




*Source : Bloomberg, BPAM, HLB Research*

***Primary issuance print in April boosted by the following names:***

| Notable issuances in Apr-19 | Rating | Amount Issued (RM mil) |
|---|---|---|
| Alam Maritim Resources Berhad | NR | 2 |
| DanaInfra Nasional Berhad | GG | 3,800 |
| IJM Corporation Berhad | AA3 | 250 |
| Lembaga Pembiayaan Perumahan Sektor Awam | GG | 3,000 |
| Maybank Islamic Berhad | AA1 | 1,000 |
| Malaysia Debt Ventures Berhad | GG | 270 |
| Perbadanan Kemajuan Negeri Selangor | AA3 | 50 |
| Perdana ParkCity Sdn Berhad | NR | 30 |
| Sabah Development Bank Berhad | AA1 | 1,150 |
| SunREIT Unrated Bond Berhad | NR | 600 |
| SUNREIT Perpetual Bond Berhad | NR | 340 |
| Touch Mobile Sdn Berhad | NR | 40 |
| Midciti Sukuk Berhad | AAA | 500 |
| Pavilion REIT Bond Capital Berhad | NR | 75 |
| Tiger Synergy Berhad | NR | 2 |
| Touch Mobile Sdn Berhad | NR | 40 |
| RH Consortium Sdn Berhad | NR | 16 |
| | | 11,165 |

*Source : BPAM, Bloomberg, HLB Research*

Total fresh issuances of all ratings of Corp Bonds/Sukuk also increased to ~RM11.2b; (similar to March's RM11.2b) with GG issuances forming a higher 60% of total issuances. The largest issuance involved the MRT operator i.e. DANAINFRA Nasional Berhad with a massive RM3.8b issuance consisting of 7-25Y bonds.

## *Outlook for May*

### *Investors may side-line due to re-rating matters and potentially seek emerging values which are not compelling at this juncture*

The weighted average BTC for the three (3) auctions in April tapered off to 2.14x mainly due to the weak final auction for the later at a mere 1.51x. (Compare this with both the entire 33 auctions for 2018 which notched a BTC ratio of 2.29x and also the previous month i.e. March's BTC solid ratio of 2.5x) as the bond market eased similar to most EM markets. Nevertheless BNM's dovish-like comments which resulted in the recent **OPR cut** is seen to somewhat provide some relief and support to the local bond market. The USDMYR pair which has weakened to 4.1600 levels is reflective of current market conditions and may weaken further, depending also on trade talk headlines.

The challenges for Malaysia's bond market in 2019 come mainly from external noises. The Norwegian sovereign wealth fund's pullout from emerging market bonds is expected to be gradual as the exposure level is low. The fund's exposure to Malaysian govvies is US$1.96 billion (RM8 billion), representing 5.4% of total foreign holdings in Malaysian Government Securities (MGS) of RM147.1 billion as at end-April 2019. Norway's sovereign wealth fund will streamline its US$300 billion (RM1.23 trillion) fixed-income portfolio by cutting emerging market bonds from the benchmark index it tracks. Currently worth US$1.05 trillion (RM4.31 trillion), Norway's Government Pension Fund Global has invested around 30% into fixed income with the balance 70% invested in equities. In terms of size, Malaysia is the third largest country with exposure to the fund after South Korea and Thailand.

Malaysia could also face an outflow risk of about US$4 billion by passive funds and an additional US$2-4 billion by active funds, should FTSE Russell drop Malaysian bonds from the World Government Bond Index (WGBI). If FTSE Russell decides to remove Malaysia from the WGBI, foreign selling will likely concentrate in MGS (Malaysian Government Securities), as currently the WGBI index excludes GII (Government Investment Issue), although the GII curve will inevitably be affected if foreign selloffs weigh on the MGS curve.

This means a potential outflow risk of US$6-8 billion, or about RM24-33 billion. We expect a quiet month in May with intermittent profit-taking and portfolio readjustment weighing on the curve and bond levels. Participation (if any) is expected to be initiated mainly by large local GLIC's and financial institutions as investors await regulatory authorities to deepen and provide consistent liquidity. There are no maturities for MYR govvies in May as opposed to prior months RM10b.

**Despite levels being "grid-locked" following the recent OPR cut, some parts of the curve exhibit values. The 4-5Y GII followed by MGS bonds along with 15Y MGS bonds are seeing values emerge whilst investors are reminded to take notice of the rather rich valuations in the 10Y part-of-the curve. Demand for Ringgit Corporate Bonds/Sukuk along the GG segment will continue to be strong even with the return of GG issuances that provide tighter 15-25bps spreads relative to MGS/GII bonds. Nevertheless the AAA and AA-rated space encompassing infrastructure, toll and energy-related related bonds may provide liquidity plus yield-carry due to the inelasticity of yield movements compared to Govvies and also due to captive market by local portfolio managers.**

## *Fed dot plot denotes a pause in earlier rate hike for 2019; however bond traders expecting rate cut going forward…*

The UST rally in April saw the curve shift lower with the UST 10Y saw a tighter range of only 18bps (March: 36bps) as markets were seen "confused" by the Fed's initial dovish outlook on muted core inflation which was later deemed to be "transitory"; causing market participants to potentially downplay a rate cut. Hence, latest revisions for interest rate outlook in 2019 reveal a pause with a tilt to a rate cut instead of the previous expectations of up to two (2) rate hikes. This has allowed UST's to find strong support at the moment. The Fed will be looking at growth, job creation, wages and inflation whilst keeping an eye on China, Europe and other events like BREXIT Bond investors that bought put options on UST's and Bunds, betting that trade tensions will abate to send global yields rising again are now seen reversing that decision. The demand for the contracts, particularly among Asia-based traders, was earlier seen coming from those who expect the latest escalation in the U.S.-China trade conflict to be short-lived.

**The US yield curve which has continued to display its inverted stance on the front-end whilst both the 3m10y and 2y10y spreads have flirted dangerously narrow again following a brief inversion in late-March. These supposedly accurate recession predictors may continue to cause concerns**. The dovish-like situation may now be a "new normal" for 2019 on the back of muted inflation and softer global growth which will see continuing and fresh debacles arising from last Friday's imposition of 25% tariffs on $200b of Chinese goods**. The short-medium term maturities potentially offer better risk-reward stance i.e. 2-5Y sectors may still be favorable as shorter UST's now offer much yield comparable to the 10Y but on lesser duration risk**. The 10Y is expected to drift higher on strong jobs data and other decent economic data whilst finding support at 2.60% levels. However, risks to the above assumptions remain if US-China global trade matters become uglier as safe-haven bids will emerge strongly. Geo-political tensions are not expected to surface under current global landscape.

**In the Credit/Corporate space, investors may still find Investment Grade issuances to undergo less stress** at ~180-200bps spreads instead of High Yield names, as these corporates are better-equipped to weather funding constrains amid the test of global trade uncertainties. However as credit gets expensive short VIX strategies may provide an option although the risk-profile is high.

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