Monthly Fixed Income Perspective –

Jan’ 20 review & Feb’ 20 outlook

US Bond market

- **US Treasuries (UST’s)** ended strong in January as sentiment was tilted more towards a risk-off mode arising mainly from the unprecedented Covid-19 viral outbreak which outweighed the positive US-China trade tariff developments and stronger economic data out of the US. Benchmark **UST yields closed between 21-39bps lower across a slightly flatter curve.** The UST 2Y declined by 21bps at 1.35% whilst the much-watched 10Y rallied pushing yields down the most by 39bps, at 1.53%. The yield curve saw inversion return again with the 2y10y halving from +34 to +18bps whilst the 3m10y reverted form +36 to -4bps. The US Dollar meanwhile ended stronger against most G10 currencies save for the Swiss franc and the Japanese yen with the Dollar Index up at 97.39 levels.

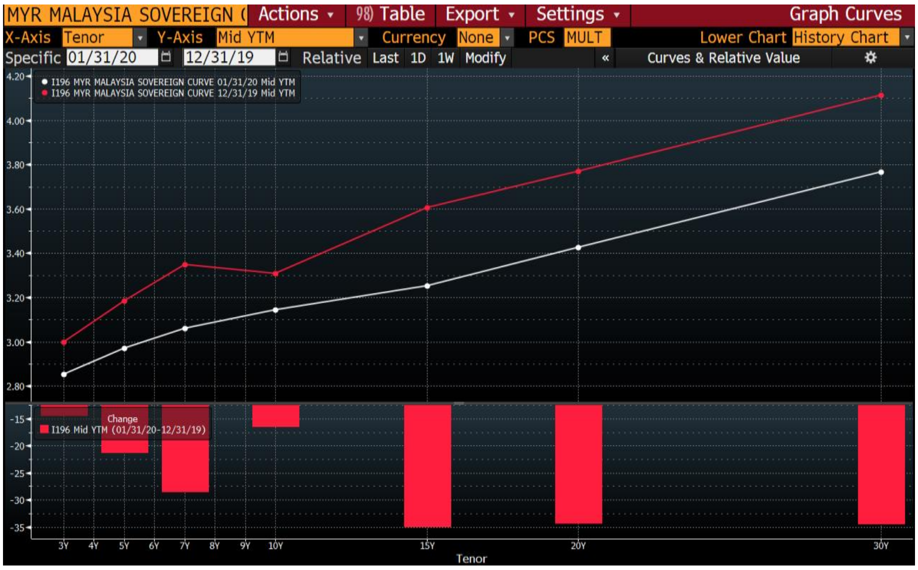
- **For Feb**, we expect the US economy to maintain momentum with jobs data sustaining strong numbers and inflation under check. The further improvement of US-China trade matters is expected to provide for a risk-on appetite. However we foresee these may be on the back-burner for now in view of the seriousness of the coronavirus outbreak which may impact trade, corporate profits and the economy as a whole. **Expect UST 10Y to see mild sell-off and range higher between 1.60-1.90% levels with potential to drift higher with resistance pegged at the 1.90% levels** whilst the Corporate Bond IG space is expected to be well-bid in sectors involving health-care and chemicals. We prefer to avoid the HY sector due to its vulnerable balance sheets.

MYR Bond Market

- MYR govvies saw benchmark **MGS bonds bull-flatten and shift lower; closing between 15-33bps lower as the longer-ends ended richer (GII bond yields ended lower albeit by lesser margins i.e. 3-10bps).** The 5Y MGS 6/24 rallied pushing yields 20bps lower at 2.95% whilst the 10Y MGS 8/29 yields declined 17bps at 3.13% levels. Foreign holdings of MYR government bonds (MGS + GII + SPK) spiked again for the 3rd month in a row in January to 24.4% or RM188.2b of total outstanding issuance due to large net maturities. The three (3) auctions involving 3Y, 7Y and 15Y MGS/GII saw strong BTC ratios above the 2.0x handle; denoting sizeable appetite.

- **For February, we anticipate yields to decline further momentarily due to another potential rate cut of 25bps following tepid 4Q2019 GDP data and imminent economic fallout from the Covid-19 viral outbreak. Kinks within the govvies curve reveal decent values for both the 6-8Y MGS and 20Y GII bonds.** The high supply of negative-yielding global debt which initially provided the impetus for yield-seeking investors is being supported by safe-haven bids arising from concerns over the coronavirus-led flu contagion. **MYR Corporate Bonds/Sukuk transactions are expected to be vibrant with investor preference along the GG and AAA segment which still appear decent at 20-24bps5 and 44-48bps spreads respectively. The 5-10Y tenures may attract attention.**

MYR sovereign curve (MGS)



Source : Bloomberg

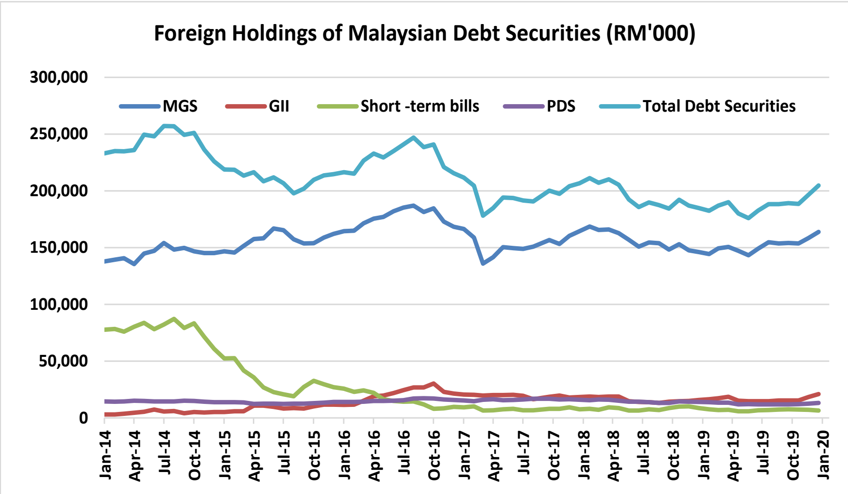
Higher NFP data for January showed US companies increased job positions as the mild weather spurred a surge in construction employment and health care….

January Non-Farm Payrolls ("NFP") of 225k was above consensus of 160k (Nov and Dec: revised up by 7k) due to delayed seasonal layoffs in the construction sector stemming from mild January weather. The average job gain over the past three (3) months of 211k was higher compared to 195k during the similar period one (1) year back. We note that the unemployment rate notched a tad higher at 3.6%; away from the record 50-year low of 3.5% the previous two (2) months; due to the higher participation rate of 63.4%. The better print on average hourly wages of +0.2% MOM (previous month: +0.1%) was equally seen in the YOY gain of +3.1% (previous month: +3.0% revised), pointing to a tighter labor market. These figures have cemented the Fed's description of a solid job market

The Fed (which carried out three rate cuts totaling 75bps to 1.50-1.75% last year) stayed pat in its last FOMC meeting on the 30th of January. The core components of the latest economic data were reasonably strong to footprint the Fed's call for no further action for now as the 4Q 2019 GDP growth was in line with its estimates. The Fed's **preferred inflation measure** for December i.e. the personal consumption expenditure (PCE) core index which the Fed officially targets for 2% was a tad higher MOM at 0.2% gain but maintained at 1.6% YOY. (This core index strips out the volatile food and energy costs and is reputed to be a better gauge of underlying price trends). The initial conclusion of Trump's 17-month trade war with China via phase one (1) US-China trade deal may revive higher domestic and global growth. Nevertheless the sudden coronavirus outbreak in January may derail the positive trade development mentioned above. The **Fed's dot plot currently reflects a pause** mainly on interest rate for 2020 with **market odds (via readings from the Fed Fund Futures)** of rate cuts between 25-50bps post-NFP last month easing to 8% **in March and also to 19% in April**. The recent inversion of the yield curve may reflect more of a global uncertainty phenomenon rather than the mere outlook on the US economy.

Another subsequent monthly jump in foreign holdings of MYR bonds in January amid steady MYR….

Foreign holdings of MYR bonds saw another spike (albeit smaller one) in January by RM3.6b or 1.7% to RM208.2b. Non-resident holdings of MGS jumped by RM3.3b from RM163.9b to RM167.2b (representing 41.7% of total outstanding) whereas total MYR Government bonds (i.e. MGS+GII+SPK) holdings similarly saw net inflows of RM3.2b to RM188.2b (representing 24.4% of total outstanding) amid net issuances of RM10.0b for last month (Dec net issuances of RM3.0b). The jump in foreign holdings for January was mainly due to safe-haven bids and also testimony of investor confidence in the local govvies market at least until March 2020 when FTSE Russell re-evaluates Malaysia's weightage in the WGBI. Malaysia continues to be in the US Treasury Department's Semi-Annual Currency's latest report/list but this is not expected to pose threat to foreign investor interest and ultimately the MYR bond asset class as a whole. **Overall MYR bonds saw a cumulative 12-month foreign inflows of RM25.8b versus net equity outflows of RM12.2b.** On the currency side, the MYR ended slightly weaker at 4.0980 levels as at end-January and closed mostly mixed against most Asian currencies between -1.72% to +3.67%. (At the time of writing, USDMYR is trading weaker at 4.1403 amid a risk-off mode for EM Asia due to fears over coronavirus outbreak from China.



Source: BNM, HLB Research

Our house view is for OPR to reduce further by 25bps in 1H2020 now as BNM maintains a pro-active policy stance following the surprised January cut….

BNM's monetary policy committee cut the OPR from 3.00% to 2.75% at the 1st MPC meeting of the year on 22nd of January and surprised investors and traders alike. In what was seen as a tactical move; BNM's policy decision is seen as a pre-emptive measure to secure improving growth trajectory amid price stability. The central bank noted that downside risks to growth remained, including those emanating from domestic factors such as "weakness in commodity-related sectors and delays in the implementation of projects. BNM continues to expect a moderate growth in 2020; supported by household spending and export performance. MOF has been forecasting a rather optimistic economic growth forecast for this year at 4.8%, compared to the just-released 4Q219 GDP growth of a mere 3.6% and 4.3% overall for 2019. The stance of monetary policy is expected to remain accommodative and growth is expected to find support from the overall 50bps cuts in total within the last eight (8) months and expansionary fiscal measures by the government. Expect MPC to continue to assess the risks to growth from the coronavirus outbreak which may stunt growth in 1H 2020; but a classic rebound in confidence, trade and financial assets upon cure and resolve cannot be discounted thereon. **Our full year estimate for 2020 GDP growth has been tweaked lower to 4.0% from 4.3% given imminent adverse impact from the Covid-19 viral outbreak following a bigger-than-expected pullback in 4Q2019 growth of a mere 3.6%** (1Q2019: 4.5%; 2Q2019: 4.9%; 3Q1019: 4.4%) Eradication of the virus outbreak from new drug or treatments, further inking of mutual agreements on US-China trade matters, improving global growth and non-presence of geopolitical tensions could however cushion the downside risks to overall growth outlook.

MYR government bond auctions saw strong bidding metrics for the reopening of 7Y MGS 5/27 and 15Y GII 11/34 in January…..

The three (3) government bond tenders concluded for the month of Jan 2020 under the auction calendar saw average BTC ratio at 2.64x (Dec 2019 BTC ratio: mere 1.64x; Nov BTC ratio: 2.24x) with the 15Y GII 11/34 seeing the largest bids totaling RM8.5b; the largest since Aug 2019 on strong bidding metrics resulting in BTC ratio of 3.40x. Auction appetite in January was strong in a continuation from December's secondary market rally.

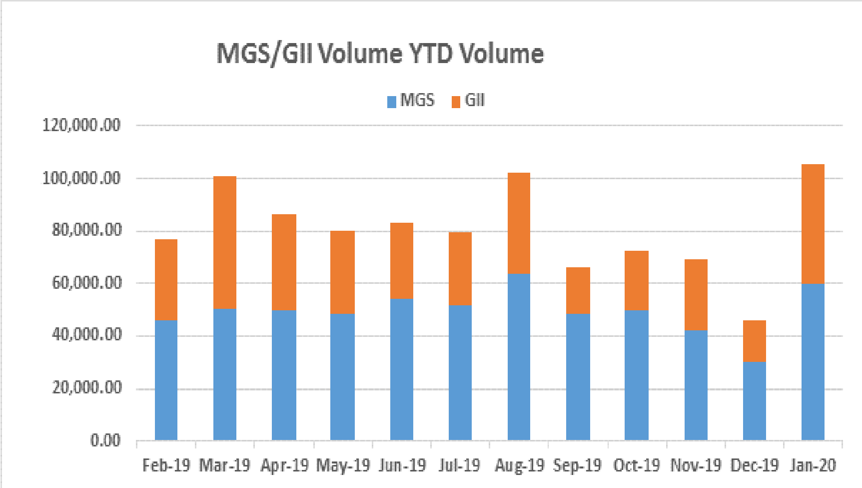
MGS/GII issuance pipeline in 2020

No	Stock	Tenure (yrs)	Tender Month	Quarter	Tender Date	Projected Issuance Size (RM mil)	Actual Auction Issuance (RM mil)	Private Placement X	Auction Amt Issued YTD	BTC (times)	Low	Average	High	Cut-off
1	7-yr reopening of MGS (Mat on 05/27)	7	Jan	Q1	8/1/2020	4,000	3,500		3,500	2.498	3.259	3.281	3.288	57.1%
2	15-yr Reopening of GII (Mat on 11/34)	15	Jan	Q1	14/1/2020	4,000	2,500	1,000	6,000	3.396	3.500	3.507	3.513	42.9%
3	3-yr Reopening of MGS (Mat on 3/23)	3	Jan	Q1	23/1/2020	3,000	3,000		9,000	2.183	2.837	2.858	2.875	80.0%
4	30-yr Reopening of GII (Mat on 11/49)	30	Feb	Q1	4/2/2020	3,000	2,500	1,500	11,500	2.328	3.747	3.780	3.792	66.7%
5	10-yr Reopening of MGS (Mat on 08/29)	10	Feb	Q1	13/2/2020	3,000	4,000		15,500	2.036	2.860	2.888	2.898	80.0%
6	5-yr Reopening of GII (Mat on 10/24)	5	Feb	Q1		3,000								
7	15-yr Reopening of MGS (Mat on 07/34)	15	Mar	Q1		4,000		X						
8	20-yr Reopening of GII (Mat on 09/39)	20	Mar	Q1		4,000		X						
9	5-yr Reopening of MGS (Mat on 09/25)	5	Mar	Q1		3,000								
10	7.5-yr New Issue of GII (Mat on 09/27)	7	Mar	Q1		4,000		X						
11	20-yr Reopening of MGS (Mat on 05/40)	20	Apr	Q2		4,000		X						
12	10.5-yr New Issue of GII (Mat on 10/30)	10	Apr	Q2		4,000		X						
13	7-yr Reopening of MGS (Mat on 05/27)	7	Apr	Q2		3,500								
14	15-yr Reopening of GII (Mat on 11/34)	15	May	Q2		3,500		X						
15	10-yr Reopening of MGS (Mat on 08/29)	10	May	Q2		3,500								
16	3-yr Reopening of GII (Mat on 05/23)	3	Jun	Q2		3,000								
17	30-yr New Issue of MGS (Mat on 06/50)	30	Jun	Q2		3,500		X						
18	20-yr Reopening GII (Mat on 09/39)	20	Jun	Q2		3,500		X						
19	3-yr Reopening of MGS (Mat on 03/23)	3	Jul	Q3		3,500								
20	10-yr Reopening of GII (Mat on 10/30)	10	Jul	Q3		3,500								
21	15-yr Reopening of MGS (Mat on 07/34)	15	Jul	Q3		3,000								
22	7-yr Reopening of GII (Mat on 09/27)	7	Aug	Q3		3,500								
23	20-yr Reopening of MGS (Mat on 05/40)	20	Aug	Q3		4,000		X						
24	15-yr Reopening of GII (Mat on 11/34)	15	Aug	Q3		3,500		X						
25	7-yr Reopening of MGS (Mat on 05/27)	7	Sep	Q3		3,000								
26	30-yr Reopening of GII (Mat on 11/49)	30	Sep	Q3		3,000		X						
27	5-yr Reopening of MGS (Mat on 09/25)	5	Sep	Q3		3,000								
28	3-yr Reopening of GII (Mat on 05/23)	3	Oct	Q4		3,000								
29	10.5-yr New Issue of MGS (Mat on 04/31)	10	Oct	Q4		4,000								
30	5-yr Reopening of GII (Mat on 03/26)	5	Oct	Q4		4,000								
31	30-yr Reopening of MGS (Mat on 06/50)	30	Nov	Q4		3,000		X						
32	7-yr Reopening of GII (Mat on 09/27)	7	Nov	Q4		3,500								
33	15-yr Reopening of MGS (Mat on 07/34)	15	Nov	Q4		3,000								
34	10-yr Reopening of GII (Mat on 10/30)	10	Dec	Q4		3,400		X						
	Gross MGS/GII supply in 2020					117,400		2,500						

Source: BNM, HLB Research

Trading volume for MGS/GII spiked sharply in January…

Trading volume for MYR govvies i.e. MGS + GII bonds more than doubled to ~RM101.7b in January compared to prior month's RM46.4b. Interest was seen mainly across the short-end of the bellies with substantial and frequent trades done in the off-the-run 20-21's (RM15.8b for these tenures forming ~16% of overall volume; higher than the RM13.2b for the previous month). This was followed by an uptick in interest for the benchmark 10Y benchmarks which churned a massive secondary market volume of RM11.4b for the month whilst the longer-ends saw strong demand as per our earlier recommendation for the 33's and/also 15Y tenures which accounted for RM5.2b (5.1%) and RM6.71b (6.6%) of total volume respectively. In short, investors were seen generally long on the ultra-short-end and also the 10-15Y duration; as demand surfaced arising from kinks on certain parts of the curve. This was somewhat similar to the previous month with investors consisting of both foreign, local institutional investors and also inter-bank participants. This further leads us to believe that the projected weaker external environment arising from the coronavirus flu-related contagion engulfing the greater Asian region has overshadowed the FTSE Russell WGBI concerns which are on the back-burner at least until the coming March 2020.

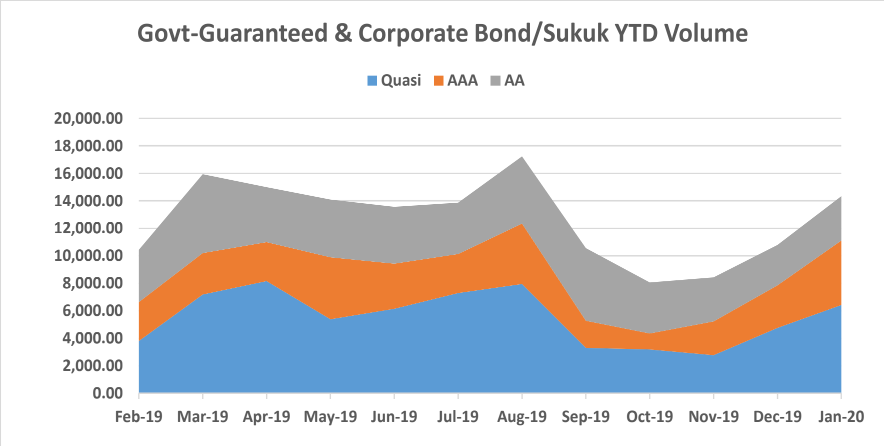


Source : BPAM, Bloomberg, HLB Research

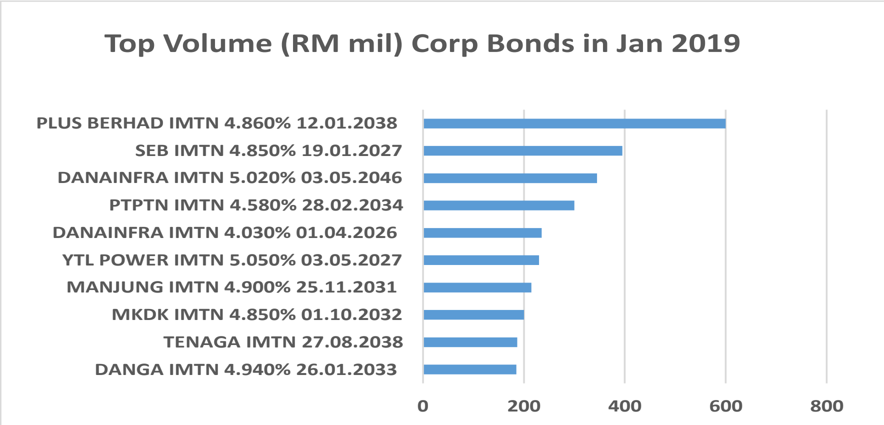
Corporate Bonds/Sukuk sees continued traction for 4th month running…

In the secondary market, Corporate Bonds/Sukuk (including Govt-Guaranteed bonds) saw higher secondary market trading volume on higher momentum as volume notched ~ RM15.4b in January (a 33% rise compared to RM11.6b in Dec). Market activity was upbeat as portfolio fund managers chased yields as safe-haven bids continue to pour into MYR sovereigns. Liquidity improved as credit spreads relative to MGS narrowed for the month under review with yields closing mostly lower between 2-5bps with the initial US-China trade issues out of the way and initial spreads widening due to sovereign yields grinding lower as fears over the coronavirus outbreak surfaced. Nevertheless, Corporate Bonds/Sukuk saw foreign holdings ease slightly to RM13.1b; off-the recent high in December 2019. Total transactions for GG bonds eased by 9% for the month compared to AAA and AA-rated papers; whilst still forming a steady yet impressive 45% of overall volume. Bulk of investor interest was mainly centered on DANAINFRA, PRASARANA followed by LPPSA bonds. The largest drop was seen in the AA-segment with interest tapering off from 27% to 23% of overall trades. (AA-rated bonds last lead with 38% market share in November last year). Bonds that garnered top volume for the month were PLUS 1/38 which moved 15bps lower at 3.66% and AA-rated SEB 1/27 which rallied 24bps higher at 3.44%. This was followed by GG-related DANA 5/46 which declined 31bps at 3.91%. The banking sector saw the Bank Pembangunan 2022-2032 again top monthly investor favorites; closing sharply lower between 4-90bps compared to previous-done levels.

Frequency and volume of trades in the pure credit space were seen within a range of bonds namely conglomerates (i.e. DRB HICOM 22-29, DANUM 23-24 and GENTING-related 23-34) and infrastructure-related names including sub-sectors such as construction/property (i.e. IJM-related bonds 20-perps, AMAN 21-30, DANGA 20-33), energy (i.e. AAA-rated TENAGA 33-38, MANJUNG 22-31, AA-rated BGSM 21-26, EDRA 29-33, JEP 27-32, SARAWAK HIDRO 20-27, SEB 22-36, TBEI 26-30, SOUTHERN POWER 24-31, YTL Power 23-27). We also note the continued interest in odd-lot denominated trades involving unrated YNH PROPERTIES Berhad.



Source : BPAM, Bloomberg, HLB Research



Source : BPAM, Bloomberg, HLB Research

Primary issuance print in January boosted by following names:

Notable issuances in Jan-19	Rating	Amount Issued (RM mil)
Eternal Icon Sdn Berhad	NR	18
Khazanah Nasional Berhad	GG	2,900
Kedah Cement Sdn Berhad (fka Lafarge Cement Sdn Bhd)	A1	180
Liziz Standaco Sdn Berhad	NR	27
OCR Land Holdings Sdn Berhad	NR	15
OSK I CM Sdn Berhad	NR	100
Perbadanan Kemajuan Negeri Selangor	A3	100
Setia Fontaines Sdn Berhad (fka Setia Recreation Sdn Berhad)	NR	3
TTDI KL Metropolis Sdn Berhad	NR	20
Toyota Capital Malaysia Sdn Berhad	AAA	200
United Malayan Land Berhad	NR	500
		4,062

Source : BPAM, Bloomberg, HLB Research

Total fresh issuances for all ratings of Corp Bonds/Sukuk dropped by 65% to ~RM4.1b (Dec: R11.9b) with govt-related KHAZANAH issuances making up the bulk. The prominent bond issuances consist of unrated KHAZANAH Nasional Berhad's 20Y bond totaling RM2.1b with coupon of 4.137% and AAA-rated TOYOTA Capital Malaysia Sdn Berhad's 3Y and 5Y bonds totaling RM200m with coupons ranging from 3.7-3.8%. This was followed by AA3-rated PKNS's issuance of 3Y papers amounting to about RM100m with coupons of 3.765%.

Outlook for February 20

Investors to take advantage of mild sell-offs (if any) whilst seeking values in the curve as trading activity is expected to be robust with intermittent profit-taking activities…..

The MYR bond market which notched solid bidding metrics (BTC ratio: 2.64x) for January 2020 due to comparative worldwide sovereign yields and also save-haven bids on concerns over the coronavirus-led flu contagion. BNM's decision to cut the OPR by 25bps at its recent January MPC meeting will be followed closely by market participants with the next meeting scheduled on 3rd March 2020 with our revised house view of another 25bps rate cut in the 1H2020. Separately, the Finance Ministry together with the government will announce a stimulus package on the 27th of February to counter the economic impact of the coronavirus outbreak. The USDMYR pair has weakened to 4.1390 levels at the time of writing as a result of both USD strength coupled with risk-off bids for EM Asia**.** The FTSE-Russell-related risk of outflows of up to US$4 billion by passive funds and an additional US$2-4 billion by active funds is at the back-burner for now at least until March 2020. Nevertheless, Malaysian regulators continue to engage with officials of the Index provider to provide a deeper and more liquid bond market. The extension of Repo/Reverse Repo transactions from 365 days to 5 years along with measures such as the engagement of Principal Dealers to facilitate quotes for off-the-run-bonds, ease of FX Forward transactions and the establishment of Appointed Overseas Offices (AOO) to improve MYR accessibility and hedging opportunities are expected to benefit credentials of the MYR bond market.

We anticipate yields to continue its decline initially; similar to December-January period in line with the relatively good performance of the bond market for the last quarter**. Slight kinks within the govvies curve make the 6-8Y MGS and 20Y GII bonds look more compelling other maturities.** We note that there are nil maturities for the first two (2) months of the year with no requirements for rollovers. Nevertheless the 20-21's continue to see tremendous investor/trader interest. The increasing supply of negative-yielding global debt may provide impetus for yield-seeking investors that buy into **Ringgit Corporate Bonds/Sukuk with preference along the GG segment which still look decent at 20-24bps spreads** compared to November-January period. **The 5-10Y tenures look particularly attractive** as yields have yet to be chased down amid the lack of supply last month. Expect continued spillover down the credit spectrum especially **into the AAA bonds followed by improving interest in non-rated bonds on yield-enhancement requirements. Liquid names in conglomerates, utilities, and infrastructure sub-sectors i.e. energy and toll may continue to attract bidding interest.**

Markets are concerned over coronavirus outbreak and may re-consider pricing in a Fed rate cut this year…

The UST movements in January saw the curve turn flatter with the much-watched UST 10Y declining 39bps to 1.53% levels; having been through a much more volatile trading range of 39bps (December: 21bps) as the bond market continued to see massive gains across the curve. Several other bond markets including Germany, China and UK rallied equally despite the Fed being neutral on its interest rate outlook. While average 2019 monthly job gains of 174k are slightly less stellar compared to the average 223k in 2018, the monthly job creation of at least 100k to keep up with growth in the working-age population is being frequently met. This, along with the low unemployment rate of 3.6% reinforces the steady growth outlook arising from steady

ISM and PMI manufacturing data in January. Both the Fed and investors will continue to monitor key economic indicators including inflation, jobs data, US-China trade progress and most of all the ongoing impact of the coronavirus outbreak on Asia and eventual global economy. With the successful conclusion of the US-China phase one (1) trade pact, market are now awaiting the continued removal of further tariffs in another trade agreement in the coming months. Elsewhere, the uncertain impact of BREXIT on UK and potential geo-political tensions are not to be discounted and may reduce risk appetite for assets like equities. The yield curve (reputed to be a reliable recession predictor) which was on the cusp of inverting again is a distant troubling sign and the Fed is watching intently for warning signs despite the current policy accommodation.

We continue to opine the case for no rate cut based on continued moderate global outlook arising from the full impact of three (3) earlier cuts and most recently the vast potential for improvement in US-China trade matters. The recent signing of US-China trade phase one (1) and a further negotiation on tariff reductions is expected to remove additional uncertainty on US-China global trade issues. However the emergence of the coronavirus-led flu contagion and the repercussions from this virus will put a temporary damper on global growth just when a trade truce between the U.S. and China was expected to ease business uncertainty and stimulate new investments. **Hence, we note that the shorter-end has turned rich since our last call due to rate-cut expectations. Any immediate sell-off in the medium-to-longer tenure now represents an opportunity to extend duration in February. The 10Y is expected to range between 1.60-1.90% whilst finding support at 1.90% levels whilst taking cognizance of the $27b that the US Treasury will auction in Feb.**

In the Credit/Corporate space, Investment grade (IG) debt may remain to be well sought after with healthcare and chemicals expected to outperform as the current backdrop of low yields are still seen to outperform at 100bps spreads (reference is made to the Bloomberg Barclays US Aggregate Index for Investment-Grade Corporate Bonds). We have altered our earlier stance of adopting a negative duration as we opine that the virus outbreak may stunt global trade and growth. Boosting the credit quality of portfolio is recommended to minimize risk and consequently **prefer to keep credit quality high and duration at between 3-7Y tenures.** We continue to prefer avoiding the HY sector due to vulnerability of balance sheets being challenged as corporate revenue and profits fall. **Investors may still find value in IG issuances especially in chemicals and health-care sectors.**

Hong Leong Bank Berhad
Fixed Income & Economic Research, Global Markets
Level 8, Hong Leong Tower
6, Jalan Damanlela
Bukit Damansara
50490 Kuala Lumpur
Tel: 603-2081 1221
Fax: 603-2081 8936
Email: HLMarkets@hlbb.hongleong.com.my