eastspring investments

A Prudential plc company

MARKET COMMENTARY

Fixed income market review and outlook

March 2024

Review

- U.S. February data continued to point to the resilience of its economy. Headline U.S. Personal Consumption Expenditure ("**PCE**") price index increased to 2.5% YoY, while the U.S. core PCE was flattish at 2.8% YoY in February (January: 2.4%; 2.8%). The University of Michigan Consumer Sentiment index for March recorded an increase to 79.4 from the downward revised 76.9 in the prior month. The Non Farm Payroll data showed that the U.S. economy added 275,000 jobs in February compared to the revised 229,000 jobs in the prior month although unemployment rate increased to 3.9% in February compared to 3.7% in the previous month. The U.S. Composite Purchasing Managers' Index ("**PMI**") remained expansionary despite a marginal decline to 52.2 in March from the upwardly revised 52.5 in February, as both Services and Manufacturing PMI recorded a decline to 51.7 and 51.9 respectively in March from the revised 52.3 and 52.2 respectively the previous month. Meanwhile, the Federal Open Market Committee ("**FOMC**") voted unanimously to keep the Fed funds rates unchanged at 5.25%-5.50%.

- In March, the Bank of England ("**BOE**") in its Monetary Policy Committee ("**MPC**") meeting again kept its bank rate unchanged at 5.25%. Both the U.K.'s headline and core inflation rate fell sharply to 3.4% and 4.5% YoY respectively in February (January: 4.0%; 5.1%), while its composite PMI continued to remain expansionary at 52.9 in March (February revised: 53.0) as Manufacturing PMI turned expansionary to 50.3 from the revised 47.5, while Services PMI declined to 53.4 compared to the revised February data of 53.8.

- The European Central Bank ("**ECB**") decided to keep its three key interest rates on the main refinancing operations, marginal lending facility and the deposit facility unchanged at 4.50%, 4.75% and 4.00% respectively. ECB's inflation forecast for 2024 was revised down to 2.3% due to lower contribution from energy prices, while 2024 growth projection was also revised lower to 0.6%. Eurozone's composite PMI Flash increased to 49.9 in March from the revised 49.2 in the previous month, as services PMI rose to 51.1 while manufacturing PMI declined to 45.7 (February revised: 50.2, 46.5). Eurozone's inflation and core inflation rates for February declined further to 2.6% and 3.1% respectively compared to 2.8% and 3.3% recorded in the prior month.

- In March, Swiss National Bank became the first central bank among the developed countries to cut its policy rate by 25bps to 1.50%. On the other hand, Bank of Japan ("**BoJ**") raised its policy rate to a range of 0.0 to +0.1% (previous: -0.1%), ending its long period of negative interest rates. The Reserve Bank of Australia ("**RBA**") decided to keep its cash rate unchanged at 4.35%. In Asia, Bank Indonesia and Bank Negara Malaysia ("**BNM**") decided to maintain their policy interest rates at 6.00% and 3.00% respectively. Meanwhile, the central banks of the Philippines and Thailand did not hold any monetary policy committee meeting in March.

- The People's Bank of China ("**PBoC**") maintained its key lending rate, 1-year and 5-year loan prime rate ("LPR") unchanged at 3.45% and 3.95% respectively in March. Economic activity data from China showed some improvement compared to the past few months, although its economic recovery is perceived to still be fragile. China's imports in the first two months of 2024 grew by 3.5% YoY in USD terms, while its exports increased strongly by 7.1% YoY (December 2023: 0.2%; 2.3%). Its retail sales expanded by 5.5% YoY in January-February 2024 (December: 7.4%), while the industrial production growth was recorded at 7.0% YoY over the same period (December: 6.8%). China's fixed asset investments recorded 4.2% YoY growth for 2M2024.

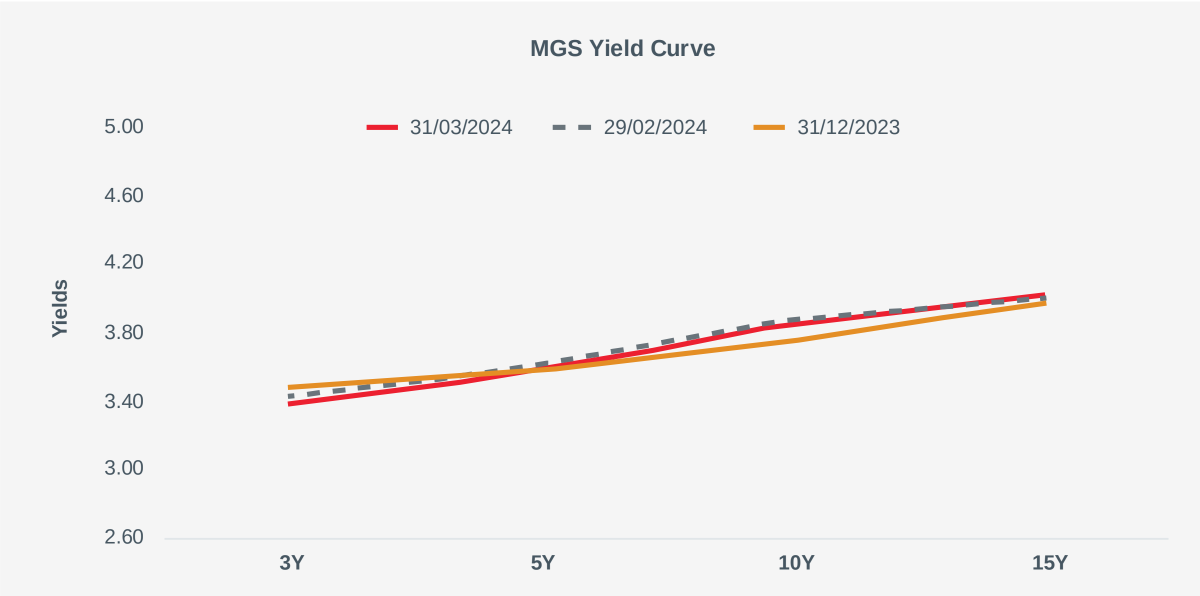
- Malaysia's headline CPI and core CPI both halted the easing trend and stood at 1.8% YoY in February (December: 1.5%; 1.8%), while unemployment rate remained stable at 3.3% in January. BNM international reserves decreased to US$113.4bn as of mid-March (mid-February: US$115.4bn). The reserves position is sufficient to finance 5.4 months of imports and is 1.0x of the total short-term external debt.

- Three auctions were held in March, the re-opening 10Y MGS 11/33, the new issue of 30Y MGII 03/54 and the re-opening of 5Y MGS 08/29. The auctions received an average bid-to-cover ratio of 2.343x.
  - RM5.0b re-opening 10-year MGS averaging 3.854% at a bid-to-cover ratio of 2.046x;
  - RM3.0b new issue 30-year MGII averaging 4.280% at a bid-to-cover ratio of 3.187x; and
  - RM5.0b re-opening 5-year MGS averaging 3.681% at a bid-to-cover ratio of 1.797x.

- Malaysia's MGS curve movement was mixed in the month of March. The yields of the 3- and 5-year MGS declined by 4 bps and 1bp respectively, 10-year MGS yield remained unchanged, while 15-year MGS yield increased by 2 bps to close the month at 3.39%, 3.59%, 3.85% and 4.01% respectively. The yield curve of MGII on the other hand shifted downwards, with the 3-, 5-, 10- and 15-year MGII yields falling by 3 bps, 2 bps, 1 bp and 3 bps to end the month at 3.44%, 3.60%, 3.85% and 3.96% respectively.

BENCHMARK	Dec 2023 Yield	Feb 2024 Yield	Mar 2024 Yield	MOM Change	YTD Change
3-year MGS	3.48%	3.43%	3.39%	-4 bps	-9 bps
5-year MGS	3.58%	3.60%	3.59%	-1 bp	0 bp
10-year MGS	3.74%	3.86%	3.85%	0 bp	+12 bps
15-year MGS	3.97%	3.99%	4.01%	+2 bps	+4 bps

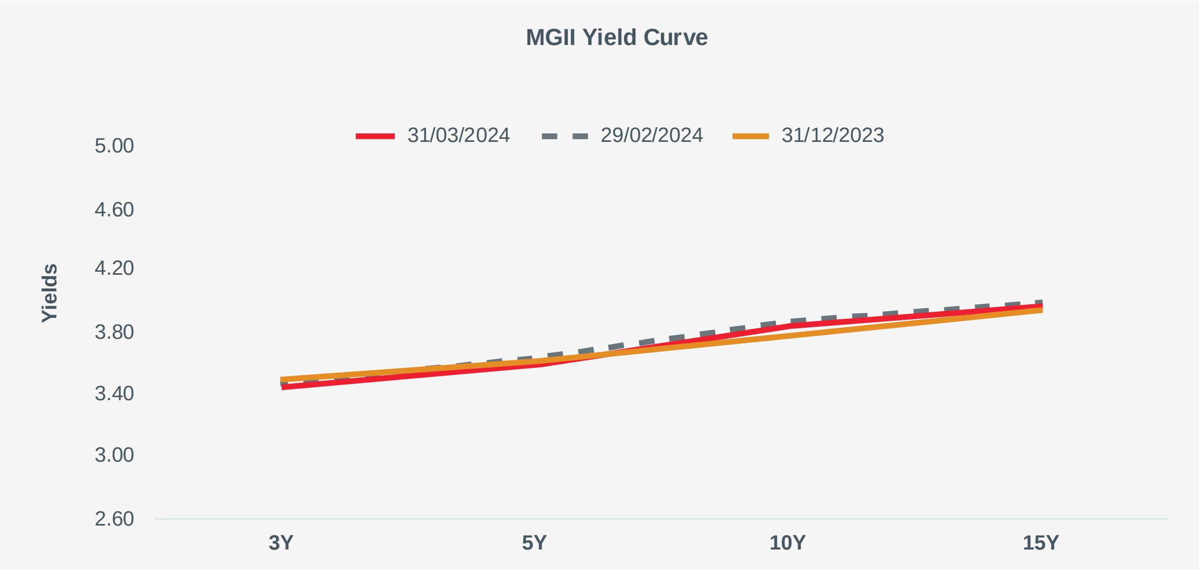
Source: Bloomberg



Source: Bloomberg

BENCHMARK	Dec 2023 Yield	Feb 2024 Yield	Mar 2024 Yield	MOM Change	YTD Change
3-year MGII	3.49%	3.47%	3.44%	-3 bps	-5 bps
5-year MGII	3.61%	3.62%	3.60%	-2 bps	-1 bp
10-year MGII	3.78%	3.86%	3.85%	-1 bp	+7 bps
15-year MGII	3.93%	3.99%	3.96%	-3 bps	+3 bps

Source: Bloomberg



Source: Bloomberg

Outlook

- After months of aggressive interest rate hikes by the central banks in developed countries, the market and investors are expecting these central banks to cut policy rates this year. In December 2023, futures traders were expecting the Federal Reserve ("**Fed**") to cut its policy rates six times of 25 bps each for the year 2024 and this expectation had been lowered to only three cuts of 25 bps each, which is now inline with Fed's guidance. We expect future monetary decisions to be dependent on economic data. Inflation rates seemed to have peaked in the U.S., U.K. and the Eurozone, and are declining albeit not in a straight line Heightened geopolitical risks continues with the Israel-Hamas war, on top of the ongoing Russia-Ukraine war and the tensions between U.S. and China. The U.S. presidential election towards the end of the year will also add to the uncertainty. Meanwhile, China's economic growth is expected to be slower in 2024, due to its real estate slump and weaker demand for exports.

- For Malaysia, BNM's decision on the Overnight Policy Rate ("**OPR**") will also be data dependent as the central bank assesses the sustainability of the domestic growth momentum, upside risks to inflation with potential subsidy rationalisation, global economic growth in developed economies and China, as well as the performance of the Ringgit. With the roll out of the targeted subsidy programme for RON95 petrol expected in the second half of 2024, inflation is expected to come in higher in 2024. Malaysia's growth momentum in the next few years will depend on the execution of the policy blueprints such as MADANI Economy, National Energy Transition Roadmap ("**NETR**") and New Industrial Master Plan ("**NIMP**").

- Three auctions are expected in the month of April, with the new issue of 7.5Y MGII 10/31, the new issue of 15Y MGS 04/39 and the re-opening of 3Y MGII 09/26. While there is ample liquidity in the system, the outcome of these auctions is likely to be influenced by prevailing market sentiment both from local and foreign investors. On the corporate front, we expect mixed demand for corporate bonds as investors continue to be selective in their investments.

Table 1: Indicative Rates (%)	
	31-Mar-24
MBB O/N*	1.30%
MBB 1-Week*	1.40%
MBB 1-Mth FD*	2.70%
MBB 6-Mth FD*	3.05%
MBB 1-Year FD*	3.10%
1-mth BNM MN	3.18%
3-mth BNM MN	3.23%
3-mth KLIBOR	3.59%
CP	
1-mth (P1)	3.80%
3-mth (P1)	3.97%

Source: Bloomberg/Bondstream
* Maybank2u.com.my

Table 2: Indicative Bond Yields (%)					
	3yr	**5yr**	**7yr**	**10yr**	**15yr**
MGS	3.48	3.66	3.78	3.88	4.00
GII	3.49	3.65	3.78	3.86	3.92
Swap rate*	3.58	3.65	3.76	3.88	4.08
AAA	3.72	3.83	3.96	4.06	4.16
AA1	3.83	3.94	4.04	4.16	4.30
AA2	3.90	4.01	4.11	4.27	4.47
AA3	4.00	4.10	4.20	4.37	4.66
A1	4.79	5.11	5.38	5.66	6.02
A2	5.41	5.82	6.17	6.60	7.08
A3	6.02	6.54	6.97	7.53	8.14

Source: Bloomberg*/Bondstream

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