MARKET COMMENTARY

Fixed income market review and outlook

December 2024

Review

- At the Federal Open Market Committee (FOMC) meeting in December 2024, the Federal Reserve ("**Fed**") announced a further 25 basis points (bps) rate cut, marking the third consecutive cut this year and bringing borrowing costs to 4.25% to 4.5%, as expected. It reflects the Fed's continued commitment to achieving its dual goals of maximum employment and price stability. The U.S. economy added 227,000 jobs in November 2024, a strong rebound from October's upwardly revised gain of 36,000, which was heavily impacted by Boeing strikes and disruption caused by hurricanes in Southeastern states. The unemployment rate in the US went up to 4.2% in November (Oct: 4.1%). The U.S. PCE Price index accelerated to 2.4% (Oct: 2.3%), whereas the core PCE price index steadied at 2.8% (Oct: 2.8%) in November. The University of Michigan Consumer Sentiment index continued its fifth-month trend of steady increases, rising from to 74.0 in December compared to 71.8 in November. The S&P Global U.S. Composite Purchasing Managers Index ("**PMI**") rose to 55.4 in December (Nov: 54.9), driven by robust expansion in Services PMI at 56.8 (Nov: 56.1), which offset a contraction in Manufacturing PMI at 49.4 (Nov: 49.7).

- The Bank of England kept its bank rate stable at 4.75% in December, aligning with market expectations. This decision comes as wage growth and some indicators of inflation expectations have risen, heightening the risk of persistent inflation. The U.K.'s inflation rate edged up for a second month to 2.6% in November (Oct: 2.3%). In December, the S&P Global UK Composite PMI slipped to 50.4 (Nov: 50.5), amid lower output by factories and decline in news orders in Manufacturing PMI (47.0 vs 48.0) despite better business activity in Services PMI (51.1 vs 50.8).

- The European Central Bank ("**ECB**") has decided to cut its key interest by 25 bps in its final meeting of 2024, indicating a more positive inflation outlook and improvements in monetary policy transmission. Specifically, the interest rates on its deposit facility rate, main refinancing operations and marginal lending facility have all been decreased by 25 bps, bringing them to 3.00% (from 3.25%), 3.15% (from 3.40%) and 3.40% (from 3.65%), respectively. Eurozone's inflation rate accelerated for a third straight month to 2.4% in December (Nov: 2.2%), while its core inflation rate stayed at 2.7%. Inflation is projected to gradually decline, with forecast of 2.4% in 2024, 2.1% in 2025 and 1.9% in 2026. In December, the Eurozone Composite PMI rose to 49.6 (Nov: 48.3). The manufacturing sector remained weak with PMI at 45.1 (Nov: 45.2), but the services sector rebounded into expansion territory with PMI at 51.6 (Nov: 49.5).

- The Reserve Bank of Australia and Bank of Japan maintained their interest rate at 4.35% and 0.25% during their final meeting of 2024, respectively. In Asia, the Central Bank of Philippines lowered its interest rate by 25 bps to 5.75% during its December 2024 policy meeting, marking the third consecutive rate cut. The Bank of Indonesia and Bank of Thailand kept their interest rate unchanged at 6.00% and 2.25%, respectively in December 2024. Meanwhile, Bank of Korea and Bank Negara Malaysia ("**BNM**") did not hold any monetary policy committee meeting in December.

- The People's Bank of China **("PBoC")** maintained its key lending rates at December fixing, following a commitment from Chinese leaders in early December to raise the 2025 budget deficit to 4% of GDP to spur an economic turnaround and boost consumer spending. The 1-year and 5-year loan prime rates were held at 3.1% and 3.6%, respectively. In November, China's imports dropped by 3.9% YoY in USD terms (Oct: -2.3%) amid weak domestic demand and the potential ripple effect of tariff threats from the US, while its exports grew by 6.7% (Oct: 12.7%) as some manufacturers front-loaded orders in anticipation of further tariffs from the US. Retail sales rose 3.0% YoY (Oct: 4.8%) and industrial production expanded by 5.4% YoY (Oct: 5.3%) in November. China's fixed asset investment rose by 3.3% YoY in January to November 2024.

- In November, Malaysia's headline CPI declined to 1.8% YoY (Oct: 1.9%), while core inflation remained stable at 1.8% YoY (Oct: 1.8%). Unemployment rate improved to 3.2% in October (Sept: 3.4%). BNM international reserves amounted to US$118.1bn as at 13 December 2024 (15 Nov: US$118.0bn). The reserves position is sufficient to finance 4.6 months of imports and is 0.9x of the total short-term external debt. The Ringgit closed slightly weaker at 4.4718 against the USD, at 0.6% m-o-m. In 2024, the Ringgit appreciated over 2.73% against the US dollar, outperforming other major Asian currencies which either declined or stagnated, supported by the coordinated efforts between the government and BNM, Malaysia's promising economic prospects, and ongoing structural reforms.

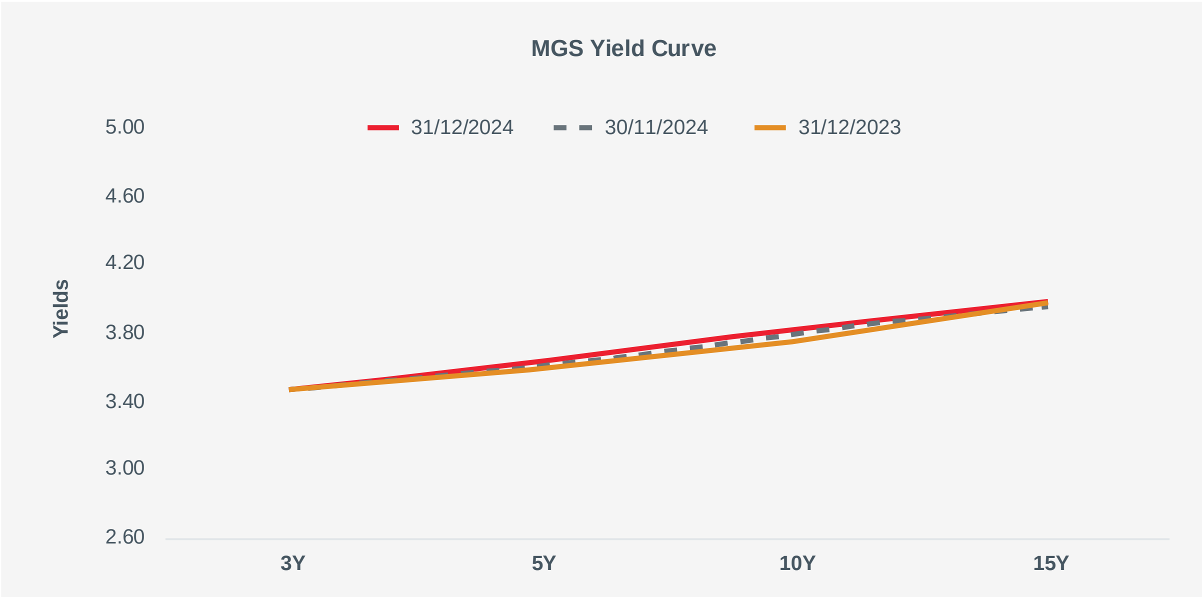
- Foreign fund outflows in the local bond market widened to RM1.39 billion in December (Nov: RM1.14 billion). This decline was driven by heightened global uncertainty which led to a reduced appetite for local bonds. Nevertheless, December YTD figures remained positive with a cumulative net inflow of RM4.78 billion (Nov YTD: RM6.17 billion).

- In December, only one auction was held for the reopening of 10Y MGS 07/34, which received a moderate bid-to-cover ratio of 2.015 times, with an auction size of RM2 billion. The 3Y MGII 09/27 auction has been removed from the calendar on BNM which was previously set for December 2024, "to reflect the latest funding requirements of the Government".

- In December, Malaysia's MGS and GII yields ended mixed. The 10Y UST ended the month at 4.58%, reflecting an increase of 41bps. The 3-year MGS yields remained relatively steady, whereas the 5-, 10- and 15-year MGS yields increased by 3ps, 1bp and 3bps to 3.62%, 3.82% and 3.97%, respectively. The 3-year MGII yields decreased by 2 bps to 3.33%, whereas 5-, 10- and 15-year MGII yields increased by 1bp, 2bps and 2bps to 3.62%, 3.83% and 3.98%, respectively.

Benchmark	Dec 2023 Yield	Nov 2024 Yield	Dec 2024 Yield	MOM Change	YTD Change
3-year MGS	3.48%	3.46%	3.47%	0 bp	-1 bp
5-year MGS	3.58%	3.58%	3.62%	+3 bps	+3 bps
10-year MGS	3.74%	3.81%	3.82%	+1 bp	+8 bps
15-year MGS	3.97%	3.94%	3.97%	+3 bps	0 bp

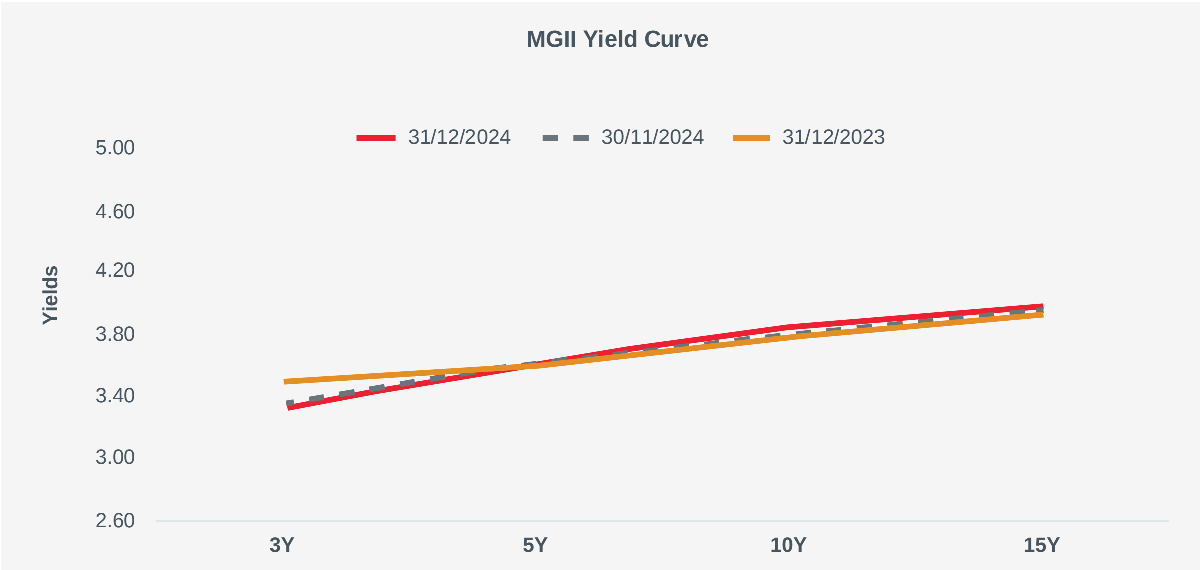
Source: Bloomberg



Source: Bloomberg

Benchmark	Dec 2023 Yield	Nov 2024 Yield	Decr 2024 Yield	MOM Change	YTD Change
3-year MGII	3.49%	3.35%	3.33%	-2 bps	-16 bps
5-year MGII	3.61%	3.61%	3.62%	+1 bp	+1 bp
10-year MGII	3.78%	3.81%	3.83%	+2 bps	+6 bps
15-year MGII	3.93%	3.96%	3.98%	+2 bps	+5 bps

Source: Bloomberg



Source: Bloomberg

Outlook

- During the post-FOMC press conference, Powell emphasized that the December rate cut was considered the best decision to support the Fed's dual mandate of price stability and maximum employment. He highlighted the need for further progress on inflation and labor market as the Fed contemplates additional rate cuts. Additionally, the Fed is evaluating President-elect Donald Trump's proposals on trade, taxation and immigration but has yet to incorporate them into decisions due to uncertainty surrounding the policies. Overall, the market anticipates two to three cuts in 2025 from the FOMC, albeit at a relatively slow pace. Nevertheless, the FOMC emphasizes that interest rate decisions will be data-dependent, with close monitoring of unemployment and inflation.

- Looking forward, we expect Fed to gradually reduce its target range for the Fed funds rate towards a neutral stance over time, with the size and timing of the cuts depending on incoming data, the evolving outlook and the balance of risks on both sides of the dual mandates. We believe the Fed will be cautious and proceed gradually as it nears the neutral rate. Continued heightened geopolitical risks with the Israel-Hamas war in the Middle East, on top of the ongoing Russia-Ukraine war and trade tensions between U.S. and its trading partners, i.e., Canada, Mexico and China, are expected to generate uncertainties and influence the trajectory of the global markets.

- BNM is expected to maintain OPR at 3.0% in 2025 as the current monetary policy continues to support the economy and aligns with the prevailing outlook for inflation and growth. It is noted that the upside risk to inflation would be dependent on the extent of spillover effects of domestic policy measures, such as the RON95 petrol subsidy rationalisation and higher labour costs under Budget 2025, expanded sales and services tax scope, an expected increase in electricity tariffs as well as global commodity prices and financial market developments. Malaysia's economy is expected to grow by 4.5%-5.5% in 2025, driven by strong domestic demand and export recovery. Inflation is projected to increase moderately to 2.0%-3.5%. The government plans to cut the deficit from 4.3% in 2024 to 3.8% in 2025, aiming for 3% by 2026.

- Three auctions are expected in the month of January 2025, with the re-opening of 7Y MGS 07/32, new issuance of 15.5Y MGII 07/40 and re-opening of 3Y MGII 07/28. 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 amidst the significant compression in credit spreads.

Table 1: Indicative Rates (%)	
	31-Dec-24
MBB O/N*	1.30
MBB 1-Week*	1.40
MBB 1-Mth FD*	2.30
MBB 6-Mth FD*	2.50
MBB 1-Year FD*	2.50
1-mth BNM MN	3.13
3-mth BNM MN	3.17
3-mth KLIBOR	3.73
CP	
1-mth (P1)	3.77
3-mth (P1)	3.95

Source: Bloomberg/Bondstream
* Maybank2u.com.my

Table 2: Indicative Bond Yields (%)					
	3yr	**5yr**	**7yr**	**10yr**	**15yr**
MGS	3.53	3.65	3.78	3.84	3.98
GII	3.47	3.67	3.75	3.84	4.00
Swap rate*	3.50	3.55	3.63	3.73	3.89
AAA	3.83	3.95	3.99	4.04	4.13
AA1	3.90	4.02	4.07	4.12	4.28
AA2	3.97	4.08	4.17	4.24	4.44
AA3	4.04	4.15	4.25	4.34	4.60
A1	4.78	5.05	5.26	5.57	6.00
A2	5.43	5.82	6.12	6.53	7.07
A3	6.05	6.57	6.96	7.47	8.14

Source: Bloomberg*/Bondstream