MARKET COMMENTARY

Fixed income market review and outlook

January 2025

Review

- The Federal Reserve ("**Fed**") kept the fed fund rate steady at the 4.25%-4.5% range during its January 2025 meeting, following three consecutive cuts since September 2024. This decision comes amidst steady economic activity, a stable labour market and a slight easing of inflationary pressures. In December 2024, the U.S. economy added 256k jobs, surpassing the market forecast of 160k. November 2024's job gains were revised down to 212k jobs. The unemployment rate unexpectedly improved to 4.1% (Nov: 4.2%), continue to signal a strong and stable labour market. The U.S. PCE Price index edged up to 2.6% (Nov: 2.4%), whereas the core PCE price index steadied at 2.8% (Nov: 2.8%) in December. The University of Michigan Consumer Sentiment index fell to 71.1 in January 2025 from 74.0 in December. The S&P Global U.S. Composite Purchasing Managers Index ("**PMI**") came in at 52.7 (Dec: 55.4) in January 2025. Manufacturing PMI edged up to 51.2 (Dec: 49.4) suggesting a modest recovery, while the service PMI marked the softest expansion at 52.9 (Dec: 56.8).

- The Bank of England ("**BOE**") cut its bank rate by 25 basis points (bps) to 4.5% from 4.75% in February 2025 decision. The BOE reiterated its position that the monetary easing is anticipated to be gradual in 2025 as growing concerns about economic growth are influenced by persistent underlying services inflation. The U.K.'s inflation rate unexpectedly edged lower to 2.5% in December (Nov: 2.6%). In January, the S&P Global UK Composite PMI rose to 50.6 (Dec: 50.4), reflecting a slower contraction in the Manufacturing PMI, which rose to 48.3 from 47.0, while the Services PMI showed growth at 50.8, slightly down from 51.1.

- The European Central Bank ("**ECB**") lowered its key interest rates by 25 bps in January 2025, reducing the interest rates on its deposit facility rate, main refinancing operations and marginal lending facility to 2.75%, 2.90% and 3.15%, respectively. The move aligns with the ECB's revised inflation outlook, with price pressures easing in accordance with expectations. In January 2025, Eurozone's inflation rate increased to 2.5% (Dec: 2.4%), influenced by a significant surge in energy prices (1.8% vs 0.1% in December. Its core inflation rate remained unchanged at 2.7%. In January, the Eurozone Composite PMI rose to 50.2 (Dec: 49.6), supported by a second consecutive expansion in Services PMI (51.3 vs 51.6) and a slower contraction in the manufacturing PMI (46.6 vs 45.1).

- In Asia, Bank of Indonesia unexpectedly cut its interest rate by 25% to 5.75% during its January 2025 meeting to maintain its inflation target of 2.5±1% for 2025 and 2026, stabilise the currency and support economic growth amid global uncertainties. Whereas the Bank of Japan raised its short-term interest rate by 25 bps to 0.5% to reflect wage hike momentum and steady progress in inflation. Both Bank Negara Malaysia ("**BNM**") and Bank of Korea kept their interest rate unchanged at 3.00% in January 2025. Meanwhile, Central Bank of Philippines and Bank of Thailand did not hold any monetary policy committee meeting in January 2025.

- The People's Bank of China **("PBoC")** maintained its key lending rates at January 2025 fixing. The 1-year and 5-year loan prime rates were held at 3.1% and 3.6%, respectively. The decision was made against the backdrop of increased pressure on yuan, which restricted PBoC's capacity to implement further monetary easing, and the rising concerns about potential policy changes in the U.S. under the incoming Trump administration. In December, China's imports rose by 1.0% YoY in USD terms (Nov: -3.9%) amid improving demand and the prospects of upcoming US restrictions on chip exports, and its exports surged by 10.7% (Nov: 6.7%) as some manufacturers front-loaded orders in anticipation of further tariffs from the US. Retail sales rose by 3.7% YoY (Nov: 3.0%) and industrial production grew by 6.2% YoY (Nov: 5.4%) in December. China's fixed asset investment rose by 3.2% YoY from January to December 2024.

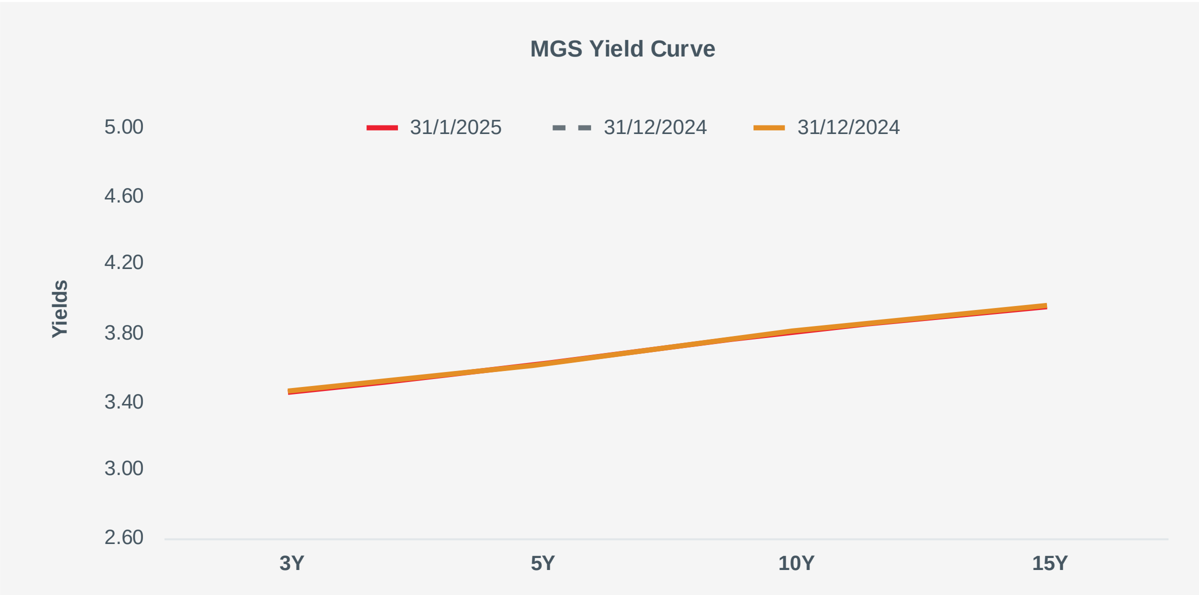
- In December, Malaysia's headline and core CPI declined to 1.7% YoY (Nov: 1.8%) and 1.6% YoY (Nov: 1.8%), respectively, bringing both headline and core inflation averaging at 1.8% in 2024. Unemployment rate remained unchanged at 3.2% in November (Oct: 3.2%). BNM international reserves amounted to US$115.5bn as at 15 January 2025 (13 Dec Nov: US$118.1bn). The reserves position is sufficient to finance 4.9 months of imports and is 1.0x of the total short-term external debt. The Ringgit gained 1.1% against the USD, closing at 4.42 in January 2025 (Dec: 4.47), benefiting from a weaker USD that was pressured by Trump's remarks downplaying the likelihood of tariffs on China.

- Three auctions were held in January 2025, the reopening of 7Y MGS 07/32, new issuance of 15.5Y MGII 07/40 and reopening of 3Y MGII 07/28. The auctions received an average bid-to-cover ratio of 3.24x.
  - RM5.0b re-opening 7-year MGS averaging yield of 3.799% at a bid-to-cover ratio of 2.808x;
  - RM4.0b (including RM1.0b of private placement) new issuance 15.5-year MGII averaging yield of 3.974% at a bid-to-cover ratio of 4.289x; and
  - RM5.5b re-opening 3-year MGII averaging yield of 3.561% at a bid-to-cover ratio of 2.623x.

- In January, Malaysia's MGS and GII yields saw minor movements except for 3Y MGII yields which increased significantly by 10 bps to 3.52%. The 10Y UST ended the month unchanged at 4.58%, after rising above 4.8% in the week before Trump's January 20 inauguration. During the month, the local bond market experienced a positive net foreign fund flow of RM1.15 billion, following a negative net flow of RM1.39 billion in December 2024.

Benchmark	Dec 2024 Yield	Dec 2024 Yield	Jan 2025 Yield	MOM Change	YTD Change
3-year MGS	3.47%	3.47%	3.45%	-2 bps	-2 bps
5-year MGS	3.62%	3.62%	3.62%	0 bp	0 bp
10-year MGS	3.82%	3.82%	3.81%	-1 bp	-1 bp
15-year MGS	3.97%	3.97%	3.97%	0 bp	0 bp

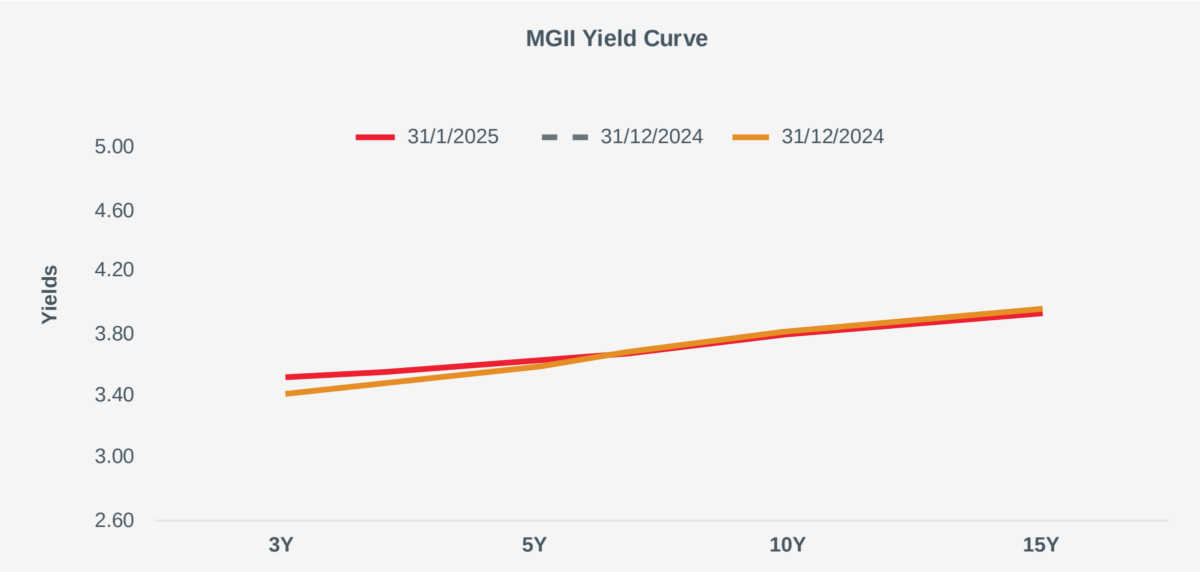
Source: Bloomberg



Source: Bloomberg

Benchmark	Dec 2024 Yield	Dec 2024 Yield	Jan 2025 Yield	MOM Change	YTD Change
3-year MGII	3.42%*	3.42%*	3.52%*	+10 bps	+10 bps
5-year MGII	3.62%	3.62%	3.62%	0 bp	0 bp
10-year MGII	3.83%	3.83%	3.82%	-1 bp	-1 bp
15-year MGII	3.98%	3.98%	3.95%	-3 bps	-3 bps

Source: Bloomberg. *MGII3Y Index



Source: Bloomberg

Outlook

- The Fed decided to keep the interest rates unchanged during its first FOMC meeting of 2025. Chair Powell emphasized that the Fed is not rushing to lower interest rates and has opted to pause cuts, adopting a “wait-and-see” approach to gain more clarity on the potential impact of the upcoming policies under the Trump administration, while offering no guidance on future rate cuts. The Fed noted that the unemployment rate steady at a low level in the recent months, while inflation continues to be somewhat elevated. Additionally, there is ongoing uncertainty surrounding the economic outlook, prompting the Fed to stay vigilant about risks related to both aspects of its dual mandate. According to CME Group data, markets are anticipating interest rate of approximately 3.9% by the end of 2025, reflecting a 61% probability of two quarter-point rate cuts in 2025. Continued heightened geopolitical risks and new 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. The tensions will worsen if Canada, Mexico, China and other countries retaliate with protectionist measures.

- 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.

- Four auctions are expected in the month of February 2025, with the re-opening of 30Y MGS 03/53, re-opening of 7Y of MGII 10/31, re-opening of 20Y MGS 05/44 and new issuance of 5.5Y MGII 08/30. 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 2: Indicative Bond Yields (%)

	3yr	5yr	7yr	10yr	15yr
MGS	3.52	3.66	3.76	3.82	3.98
GII	3.51	3.66	3.79	3.83	3.93
Swap rate*	3.48	3.48	3.48	3.70	3.92
AAA	3.82	3.90	3.95	4.00	4.09
AA1	3.90	4.00	4.05	4.12	4.27
AA2	3.97	4.08	4.14	4.24	4.43
AA3	4.05	4.16	4.23	4.34	4.58
A1	4.97	5.06	5.28	5.59	6.01
A2	5.43	5.82	6.13	6.54	7.08
A3	6.05	6.57	6.97	7.48	8.15

Source: Bloomberg*/Bondstream

Disclaimer