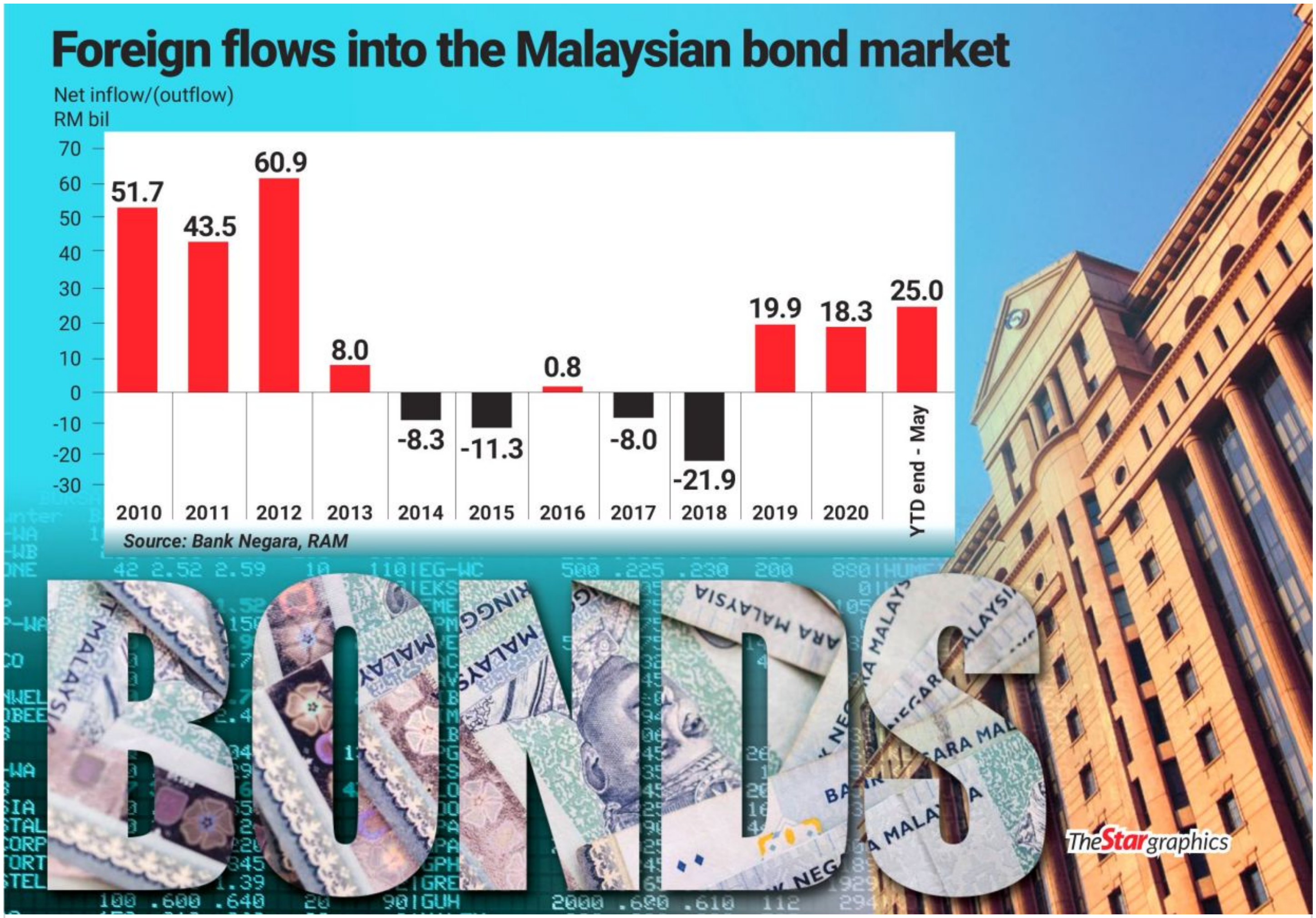
Foreign inflows into bonds set to remain positive

By DALJIT DHESI

MARKETS

Monday, 14 Jun 2021

Bond Pricing Agency Malaysia (BPAM) CEO Meor Amri Meor Ayob (file pic) said there is a possibility that foreign inflows may slow down in the coming months if the Fed turns hawkish by tapering the quantitative easing programme later this year due to mounting inflationary pressure on the US soil.



CLICK TO ENLARGE

PETALING JAYA: The Malaysian bond market, which registered the 13th straight month of positive net foreign inflows in May, will likely see lesser foreign inflows in the coming months as inflationary pressure in the US builds up.

This may result in the US Federal Reserve (Fed) tapering its quantitative easing (QE) exercise, according to economists and bond analysts.

QE refers to the buying of longer-term bonds or securities by the Fed to increase money supply and spur lending and investment.

But this may cause higher inflation. By the Fed cutting back or tapering on its bond buying, it can result in higher treasury yields in the US, hence luring foreign investors in emerging markets, including Malaysia, to seek higher yields or returns in the US. Bond price and yields are inversely related.

Malaysian Rating Corp Bhd (MARC) head of economic research Firdaos Rosli (pic below) said the local bond market is likely to record a net foreign inflow this year, albeit at a smaller magnitude compared to last year.

Moderation in foreign inflow in the coming months would likely be driven by the potential increase in US treasury (UST) yields driven by Fed tapering expectations and heightened inflation expectations diminishing real returns for foreign investors.

“Positive progress in the country’s vaccination drive and FTSE Russell’s decision to retain Malaysia in the World Government Bond Index (WGBI) would continue to attract foreign interest in local bonds.

“Simply put, there will be outflow but not strong enough to offset the inflow in the first half of the year.”

Bond Pricing Agency Malaysia (BPAM) CEO Meor Amri Meor Ayob said there is a possibility that foreign inflows may slow down in the coming months if the Fed turns hawkish by tapering the quantitative easing programme later this year due to mounting inflationary pressure on the US soil.

“The growth and hurdle factors currently hinge upon how well the Covid-19 pandemic is managed in Malaysia. If the pandemic curve is flattened soon and the vaccination programme ramps up, this will boost the confidence of bond investors.

“As demonstrated by the US, once the pandemic is contained and vaccination rate increases, economic growth will ensue, ” he said.Meor Amri said a failure to flatten the pandemic curve as soon as possible and any delays in the domestic vaccination plans would dampen economic outlook as well as investors’ sentiment in the bond market.

RAM Rating Services Bhd economist Nadia Mazlan (pic below) expects foreign inflows into Malaysian bonds to largely remain.

This is due to the still-favourable yield differentials (between 10-year UST and 10-year Malaysia

"As we do not expect normalisation of policy rates to commence this year, the continued global hunt for yields will likely support foreign inflows into MGS through the rest of 2021, " she said.

That said, she said there could be sporadic episodes of foreign outflows due to specific risks including the recent imposition of MCO 3.0 and full lockdown that may impact economic growth more than projected.

"As long as the impact of such risks is not assessed to cause permanent impairment, by and large, investors will still prioritise yield, which will lend support to MGS over the longer term, " Nadia noted.

The local bond market sustained positive net foreign inflows for the 13th straight month in May. Net foreign inflow in May was lower at RM1.9bil compared with RM6.4bil in April. Foreign holdings of MGS rose to RM191.7bil compared with RM189.3bil in April.

Maybank Kim Eng head of fixed income research Winson Phoon (pic below) said economic vibrancy and the growing breadth and depth of domestic capital markets are key to support the expansion of Malaysian bond market.

For corporate bonds or the private debt securities (PDS) market, he said a hurdle is a lack of diversity in terms of issuers and investors that entail a wider spectrum of risk appetite.

"We need more issuances in the single-A credit sector, and match them with investors having such a risk appetite, " he noted.

Phoon expects a moderate increase in MGS yields on expectations that the Covid-19 situation i
Malaysia would eventually come under control as vaccine rollout switches to a higher gear, as w
upward repricing in US rates in the second half of the year as a US-led global economic recovery gains

Firdaos, however, said faster-than-expected monetary policy normalisation would have a negative impact on local bonds.

This would occur if interest rates in Malaysia remain unchanged while other jurisdictions see higher rates, thus leading to foreign outflows.

The threat of uncontrolled inflation due to rising commodity prices would keep local bond investors on the edge.

In addition, he added that the local bond market is also vulnerable to capital flight due to the high concentration of foreign holdings.

He said there are several risks which may cast doubt and lead to capital flight from the developing economies, including Malaysia.

“Rising politicisation of Covid-19 vaccines that restricts global supply and geopolitical tensions with China may prolong the economic suffering.

“These factors may cause risk-off sentiment to reappear, causing capital flight from developing economies as investors seek safe-haven assets. There is also the threat of domestic political instability as the emergency is slated to end in August, ” Firdaos noted.

Upholding a bullish view, Nadia said attractive yield differentials, positive economic prospects and political stability are some factors that have attracted global investors to MGS.

As long as the country’s outlook remains stable and prospects for recovery remain viable despite the current rising pandemic caseload, the Malaysian bond market would continue to attract investors looking for yield.

“The yield differential between 10-year MGS and 10-year UST has risen steadily since April 2021, on account of the larger issuances to fund the additional rounds of fiscal stimulus packages.

The higher yields vis-à-vis historic low global rates will continue to drive foreign uptake of MGS going forward, ” she said.

Phoon said in the absence of an idiosyncratic event that could weigh on foreign investors’ risk appetite on ringgit bonds, he expects the 10-year MGS-UST spread to remain stable in the 150-200 basis points range.

He said: “ Rating risk from global rating agency S&P remains an ongoing concern given its negative outlook on Malaysia, but we don’t expect it to have a significant impact on bond yields even if a r rating action materialises eventually.”

For MGS and government investment issues (GII) the rating agency projects RM155bil-RM165bil issuance in 2021 (2020: RM151.9bil) driven by the government's heftier deficit financing needs amid the slew of stimulus measures to tackle the pandemic.

MARC forecast for gross issuance for MGS/GII for this year is estimated to be between RM160bil and RM170bil.

Meanwhile, it foresees the gross issuance of corporate bonds to rebound to between RM100bil and RM110bil in 2021 similar to 2018.

TAGS / KEYWORDS:

Bonds , Inflows , MARC , Firdos Rosli , Bond Pricing Agency , Meor Amri , Maybank Kim Eng ,

TOPIC:

Markets Corporate News

Making sense of the complexities of media and communications

MALAYSIA 18h ago

Malaysian airlines give good ground service at vaccination centres

NATION 15h ago

With case numbers climbing, Negri govt appeals for more Covid-19 vaccine supply

NATION 16h ago

PwD vaccine recipients given special treatment at UMK PPV

NATION 19h ago

Khairy: Over 700 journalists have received Covid-19 vaccine appointments

NATION 11h ago

Kelantan to conduct house-to-house Covid-19 vaccination

NATION 18h ago

Khairy: Over 30,000 doses of Covid-19 vaccines to be sent to Labuan in coming week

METRO NEWS 8h ago

Early target for herd immunity

THAILAND 14h ago

Bangkok hospitals postpone Covid-19 shots, citing vaccine shortages

Vietnam's Covid-19 vaccine fund receives over US$211mil in cash donations

NATION 19h ago

Khairy: Approximately 4.5mil people have registered for Covid-19 vaccination's second...

Load More