

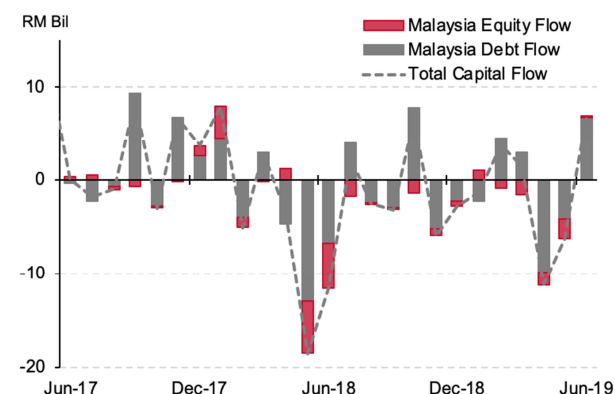
# Malaysia Bond Flows Update

Net foreign debt flows rebound at the fastest rate in eight months

## OVERVIEW

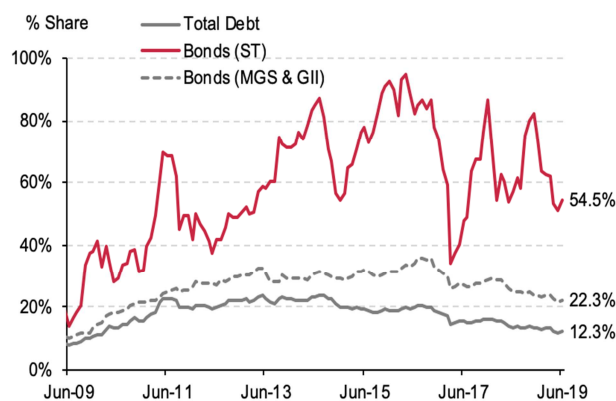
- Foreign investors turned net buyers of Malaysia's debt securities in June**, as total foreign holdings increased by RM6.6b (May: -RM4.2b) or 3.8% MoM (May: -2.3%) to RM182.6b (May: RM175.9b), recording the largest inflow in eight months, after declining for the past two successive months. Consequently, the share of total foreign holdings of Malaysia's debt inched higher to 12.3% (May: 11.9%). Similarly, **foreign investors shifted to become net buyers in the equity market in June**, charting a net inflow of RM0.1b (May: -RM2.1b), after pulling out funds for the previous four straight months. Collectively, **the capital market experienced its largest net inflow of foreign funds in 17 months** (RM6.8b; May: -RM6.3b), supported by strengthening of the Ringgit, amid growing indication of an imminent rate cut by the US Federal Reserve, as well as hopes of a trade war truce at the G20 summit.
- June's improvement was largely attributable to a net increase of Malaysian Government Securities (MGS) (RM5.8b; May: -RM3.8b) and short-term notes (ST) (RM0.9b; May: -RM0.01b).** Consequently, the foreign holdings share of total MGS and ST tilted up to 36.9% (May: 35.8%) and 54.5% (May: 51.1%), respectively. These have more than offset declines in Malaysian Government Investment Issues (GII) by RM 0.01b (May: -RM0.5b) and Private Debt Securities (PDS) by RM0.1b (May: +RM0.1b), marginally squeezing the foreign holdings share of total GII and PDS to 4.4% (May: 4.5%) and 1.68% (May: 1.69%), respectively.
- While there is a possibility for the trend to reverse into a net-outflow amidst the looming uncertainty surrounding the US-China trade dispute and rising growth moderation in major economies, **we foresee that the pull-out of funds by foreign investors would be less compared to the previous year.** This is premised on the pivot towards a dovish monetary policy stance by the US Fed and the European Central Bank, leading to highly probable benchmark rate cuts and liquidity injections. Against this development, the US 10-year Treasury note average yield extended its fall, dropping by 31 basis points (bps) to 2.06% in June, while the benchmark Malaysian 10-year MGS average yield decreased by 13 bps to 3.67%, widening the average yield spread in June to 161 bps (May: +143 bps).
- Overall, **we expect Bank Negara Malaysia (BNM) to hold the OPR steady at 3.00% in 2019** following a rate cut of 25 bps in May. However, we opine that BNM has scope and space to lower the OPR, in case of a steeper deterioration of the economy and should the Fed decide to cut rates more than once this year. On the Ringgit outlook, **we maintain our USDMYR year-end forecast of 4.10 (2018: RM4.13)**, as we foresee an imminent US Fed rate cut to trigger a "risk on" sentiment, lifting demand for higher yielding emerging market assets.

Graph 1: Foreign Holdings of Bonds and Equities



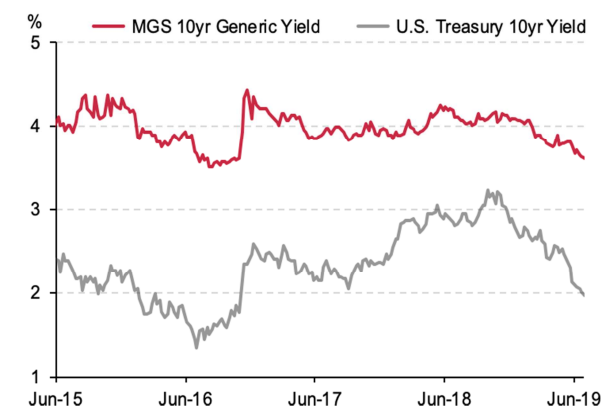
Source: BNM, Kenanga Research

Graph 2: Foreign Holdings of Malaysian Debt



Source: Dept. of Statistics, Kenanga Research

Graph 3: 10-Year US Treasury Yield Vs 10-Year MGS Yield



Source: Bloomberg, Kenanga Research

**Table 1: Foreign Holdings of Malaysian Bonds**

		Jan-19	Feb-19	Mar-19	Apr-19	May-19	Jun-19
<b>MGS</b>	Value (MYR billion)	144.4	149.3	150.7	147.1	143.4	149.1
	% of Total MGS	37.6%	38.3%	38.7%	37.1%	35.8%	36.9%
<b>GII</b>	Value (MYR billion)	16.6	17.4	18.7	15.2	14.7	14.7
	% of Total GII	5.3%	5.5%	5.8%	4.8%	4.5%	4.4%
<b>BNM bills</b>	Value (MYR billion)	5.0	5.0	5.0	5.0	5.0	5.0
	% of Total BNM bills	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
<b>PDS</b>	Value (MYR billion)	13.8	13.5	13.5	11.9	12.0	12.0
	% of Total PDS	2.1%	2.0%	2.0%	1.7%	1.7%	1.7%
<b>Total Foreign Debt Holdings</b>	Value (MYR billion)	182.5	187.0	190.0	180.1	175.9	182.6
	% of Total Securities	12.9%	13.1%	13.3%	12.5%	11.9%	12.3%

Source: BNM, Kenanga Research

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