

# DBS Flash

## Malaysian Bonds: Fiscal concerns easing

DBS Group Research

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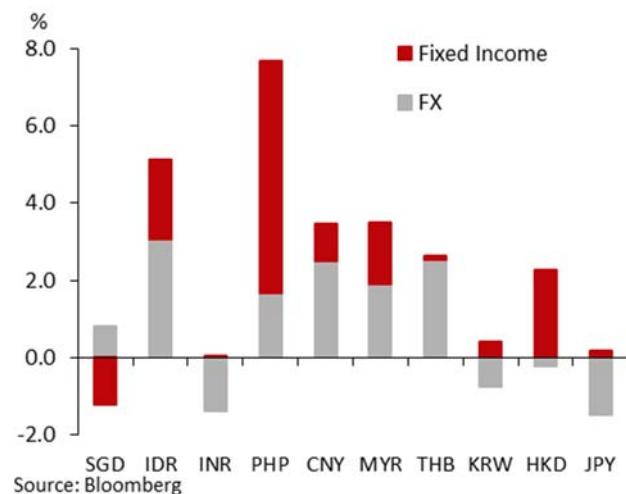
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- MGS have rallied but are not overvalued yet.
- Foreign buying is expected to pick up into light positioning.
- Fiscal concerns are easing on higher oil prices and ratings affirmation by Moody's and Fitch.
- MGS are attractive assets to carry in the current environment.
- Expect MGS to continue to outperform.

On Malaysian Government Securities (MGS), we wrote in January that valuations are cheap, technicals appear supportive and fundamentals (weaker due to deterioration of fiscal position) could improve ahead. We continue to hold that bullish view. **MGS have rallied since then but are by no means overvalued.** The technical picture remains quite positive. Year-to-date, fund flows into EM have been robust. With Malaysia holding decent weights in EM bond benchmarks, **foreign buying would be picking up into light positioning** (from 2018's outflows).

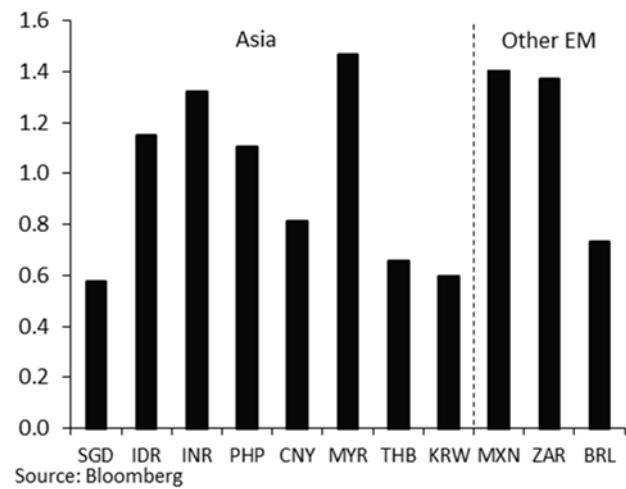
Most importantly, **fiscal concerns are easing.** Oil's rally to USD66 per barrel has increased confidence that the government can meet its 2019 fiscal deficit target of 3.4% of GDP (Budget assumed USD70 per barrel). The risk of rating downgrade has also declined with both Moody's and Fitch affirming Malaysia's rating at A3 and A- respectively and both keeping outlook stable. In our view, **MGS could continue to outperform** (currently 3rd-best within Asia, behind Philippine and Indonesia bonds).

### 10Y Local Government Bond - YTD Total Return



In the current carry-conducive environment where investors are reaching for yields, **MGS are an attractive asset to carry (yield-to-volatility ratios are low)**. MGS are also **not exposed to election-related risks**, unlike bonds in India, Indonesia and Philippines.

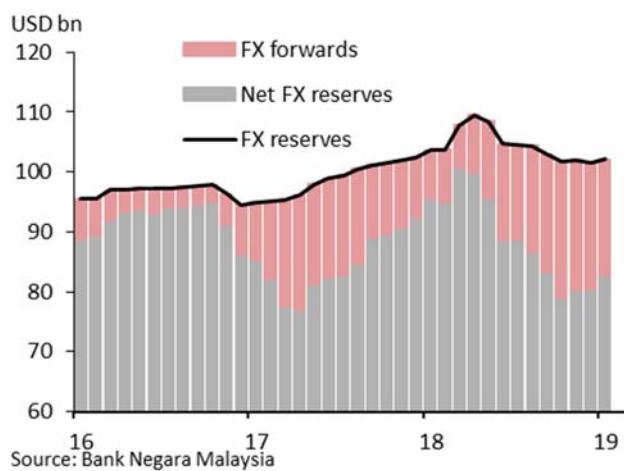
### Bond Carry (10Y Yield / 3M Historical Price Volatility)



Malaysia's **low FX reserves** (coupled with high short-term external debt) appears to be a **key worry amongst investors and is likely weighing on the MYR**. In the event of risk aversion towards EM assets, the MYR can be expected to underperform (MGS's fixed income returns should hold up better due to support from onshore banks and domestic social security funds). For now though, the

Fed remains on pause and risk appetite has been holding up. Furthermore, there could be some relief on the horizon. **Petronas's RM30bn special dividend payment to the Malaysian government (sizable relative to 2018's current account of RM34bn) could underpin the MYR if Petronas has to repatriate some of its overseas assets or convert some of its foreign currency funds.**

**Net of short positions in FX forwards, reserves have declined to USD83bn.**



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**Sources:** Data for all charts and tables are from CEIC, Bloomberg and DBS Group Research (forecasts and transformations).

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