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Media Release

Yield hunt boosts appetite for Malaysian government bonds

Foreign buying of MGS/GII is likely to continue following the recent change in the US Federal Reserve (Fed)'s policy framework, which indicates a strong commitment to maintaining a dovish stance. The domestic bond market achieved its fourth consecutive month of net foreign inflows in August (RM3.0 bil), spurred by investors' continued hunt for yields and the increasing weight of Malaysian government bonds in the JPMorgan Government Bond Index-Emerging Market (GBI-EM).

The Fed recently changed its approach to inflation, from a fixed target of 2% to a flexible average target of 2%. With inflation mostly undershooting the targeted rate in recent past, this policy change means that interest rates will only normalise much further down the road. The latest dot plot released in mid-September shows that Federal Open Market Committee members envisage rates to stay at near zero through 2023.

Low interest rates are expected to persist in the advanced economies while rates may normalise earlier in emerging markets like Malaysia. This will provide sustainably favourable yield differentials that may drive foreign inflows into the domestic market. Nonetheless, Malaysia's watchlist status on FTSE Russell's World Government Bond Index (WGBI) may impede such inflows. That said, positive engagement between FTSE Russell and the regulatory authorities to improve foreign investors' access diminishes the likelihood of Malaysia's removal from the WGBI. At worst, it may just remain on the watchlist.

In August, long-term yields were mainly trending upwards, with the 10-year MGS rising 7.5 bps m-o-m. This is attributable to heightened supply risk stemming from the lifting of Malaysia's statutory debt limit from 55% to 60% of GDP. The heightened supply concerns and, in turn, softer investor appetite led to markedly weaker bid-to-cover (BTC) ratios for MGS/GII tendered last month. The 15-year GII and 20-year MGS only attained respective BTC ratios of 1.42 and 1.47 times, instead of the usual average of around 2.4 times in past tenders.

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