UST, MGS Yields Trend Higher on Hawkish Fed Expectations

May-26 Fixed Income Review



Author
MBSB Research
research@mbsb.com

Economic Review

- The US Treasury (UST) yield curve shifted higher in May-26. The yield curve shifted mostly at the short to medium term of the curve, with the 10-year yield increasing by +7bps to 4.44%. The UST10Y yield increased to the highest level of the month at 4.66% but eased lower towards the end of the month.
- MGS yield curve generally closed higher in May-26, across all tenors. The MGS10Y yield curve closed the month higher by +14bps at 4.44% (end-Apr-26: 4.37%). The yield curve experienced gradual upward pressure during the month and closed higher across the yield curve, tracking the movement in the UST yields.
- Foreign funds registered outflows in May-26 with foreign holdings of Malaysian bonds declining by -RM4.2b to RM304.9b (Apr-26: RM309.2b). The size of foreign holdings shrank but still above the RM300b level last month.

US TREASURY & MALAYSIAN GOVERNMENT BONDS

UST shifted higher last month amid a hawkish bias turnaround

The US Treasury (UST) yield curve shifted higher in May-26. the yield curve shifted mostly at the short to medium term of the curve, with the 10-year yield increasing by +7bps to 4.44%. The UST10Y yield increased to the highest level of the month at 4.66% but eased lower towards the end of the month. Market volatility spiked last month, driven by shifting geopolitical tensions in the Middle East and evolving expectations for the federal funds rate (FFR) trajectory. Early in the month, the yield curve shifted higher as sticky US inflation expectations prompted investors to price in a potential rate hike by year-end. However, UST yields retreated as expectations of further rate hikes eased after both headline and core PCE inflation came in lower than market expectations on a monthly basis. Meanwhile, some news supported the market as the US and Iran are potentially nearing a ceasefire deal, but President Donald Trump is seen to be delaying the signing. The ongoing uncertainty from the Middle East conflict continues to weigh on investor sentiment amid limited progress towards lasting peace deal and the continued blockade of the Strait of Hormuz.

To remain cautious even on the longer-term prospect

At this juncture, we foresee upside pressures on the UST yield to continue given elevated inflation and shift in market expectations, which priced in higher probability for a rate hike towards the end of the year. Despite maintaining its slightly dovish stance at the latest FOMC meeting, we expect the Fed to be more focused towards addressing inflation, with recent releases indicating continued resilience in the US job market. In addition, investors would continue to be cautious with the long-term prospects of the US fiscal sustainability, in view of the projected 134% debt-to-GDP ratio by 2035 and a looming surge in defence expenditures, which are expected to reach USD1.5tn by 2027.

MGS10Y rose tracking the UST in May-26

MGS yield curve generally closed higher in May-26, across all tenors. The MGS10Y yield curve closed the month higher by +14bps at 4.44% (end-Apr-26: 4.37%). The yield curve experienced gradual upward pressure during the month and closed higher across the yield curve, tracking the movement in the UST yields. The MGS10Y yield traded between the range 3.46% to 3.62% last month, while the UST10Y was trading at a wider range of 4.35% to 4.66%.

The MGS3Y yield also increased last month, closing at 3.22% (end-Apr-26: 3.20%). In the first week of the month, we saw strong inflows into the debt market for both government and corporate debt; However, there were two consecutive weeks of outflows during the month, which were cumulatively higher compared to the inflows during the first week. Conversely, given the recent development in the US market, investors' expectations for the FFR are currently on a more hawkish trajectory for the year, given a possible hike scenario towards the end of the 4QCY26. However, towards the end of the month, Investors' hawkish stance eased lower, causing both MGS and UST to ease lower. Therefore, the MGS yields may mirror the movement of the UST yields in the short to medium-term, depending on the inflationary risk and the development in the Middle East.

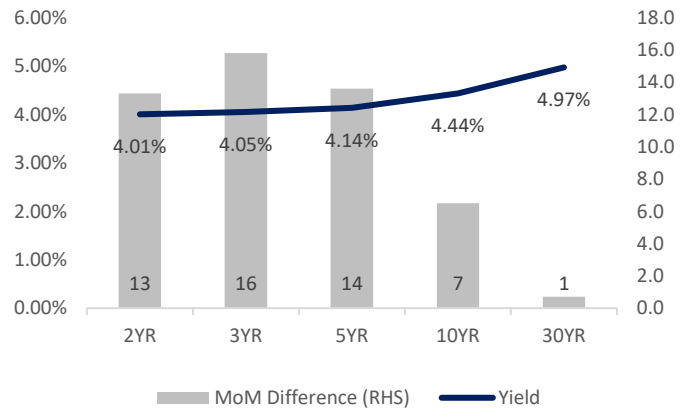
Auction demand last month was slightly weaker

Gross issuance of MGS/GII was higher at RM13.0b in May-26 (Apr-26: RM9.5b), and RM2.0b of additional issuance last month. Auction demand was relatively weaker, with the auctioned garnering an average BTC of 2.58x (Apr-26: 2.84x). However, demand for the 10-year MGS issuance was stronger than the previous 10-year auction at 2.87x (BTC: 1.60x). Meanwhile, the outstanding government bonds were lower at RM121.5t at the end of May-26 (Apr-26: 127.6t).

Maintain our view; 10-year MGS to end the year around 3.50%, with an upside bias

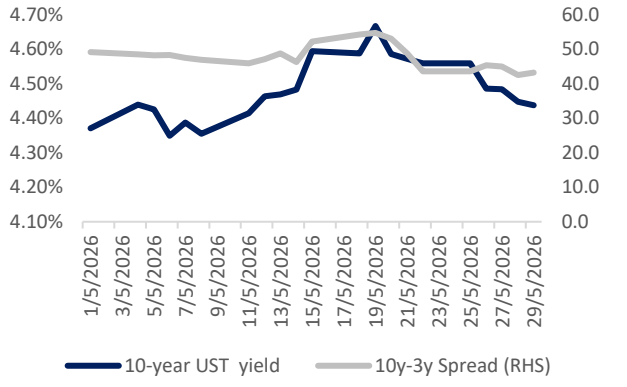
We expect the +50bps OPR spread to act as a firm floor for yield compression through the end of 2026. While MGS yields may briefly follow UST yields higher, a weakening historical correlation points to a decoupling. This shift should cap domestic yield spikes and keep the upward trajectory moderate. This suggests that domestic yields have entered a period of relative decoupling, driven more by local liquidity and fiscal fundamentals than by trends in the US interest rates. In the near term, however, the fed funds rate is projected to remain steady but with an upside bias. This could further widen the interest rate differential between the FFR and BNM's OPR, driving increased demand toward US-denominated assets, given the supply shock in the energy market. On a positive note, the MGS market should remain resilient due to a stable domestic macro environment. Proactive fiscal reforms, namely SST expansion and subsidy rationalisation, are key catalysts for sustained investor confidence. This fiscal discipline, coupled with a healthy current account surplus, maintains a compelling risk-reward profile for MGS investors. However, the short-term risk of elevated inflation may still pose a challenge to the domestic economic outlook.

Chart 1: UST Yields and MoM Difference (bps) end May-26



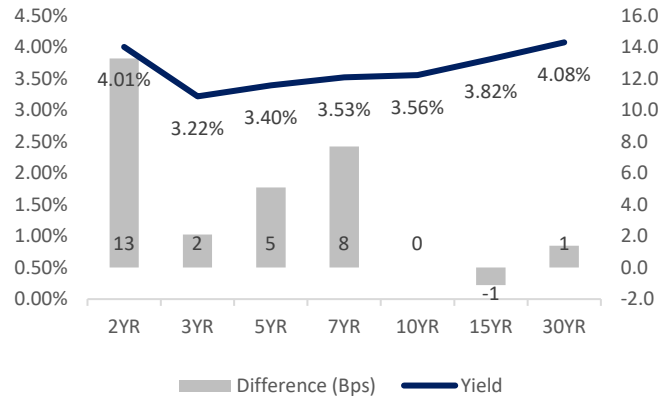
Source: Macrobond, MBSBR

Chart 2: 10y UST Yield vs 10y-3y Yield Spread (bps) in May-26



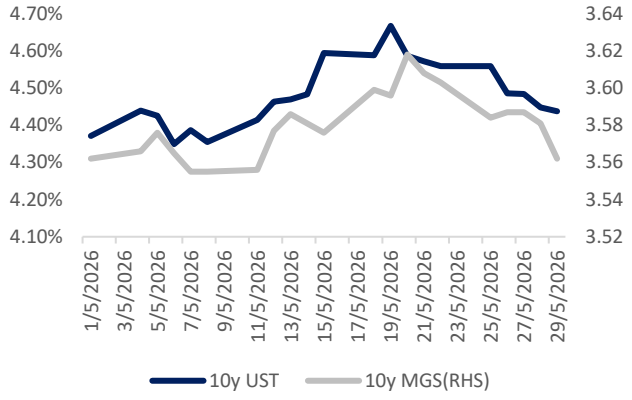
Source: Macrobond, MBSBR

Chart 3: MGS Yield Curve and MoM Difference (bps) as at end-May-26



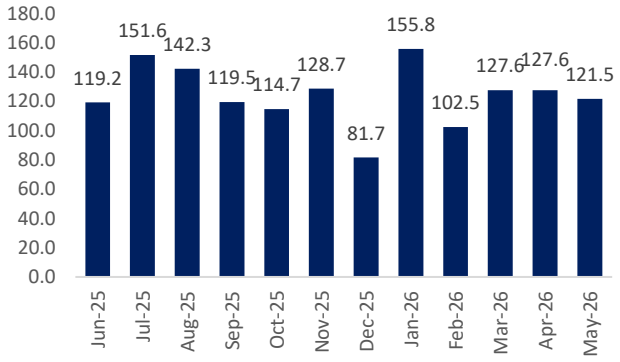
Source: Bloomberg, MBSBR

Chart 4: 10y MGS vs 10y UST Yields (%) in May-26



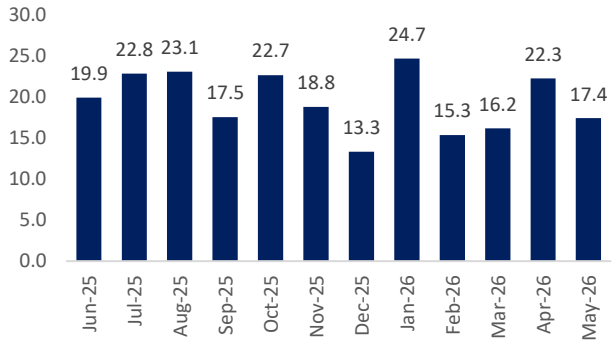
Source: Bloomberg, MBSBR

Chart 5: Outstanding Malaysia Government Bonds (RM t)



Source: Bondstream, MBSBR

Chart 6: MGS Volume of Government Bonds Traded (RM b)



Source: Bondstream, MBSBR

Table 1: Quarterly Forecast for MYR and MGS 10-year yield

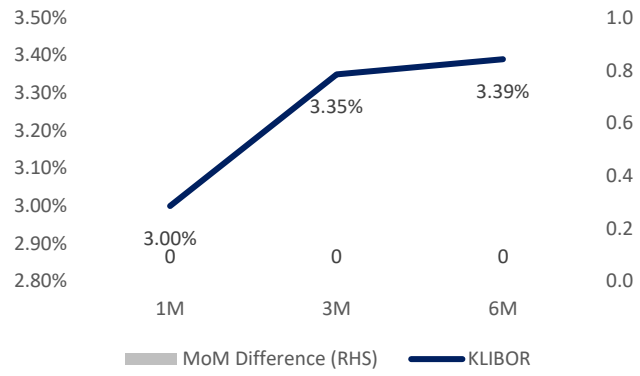
	1Q26f	2Q26f	3Q26f	4Q26f
Exchange Rate, vs USD (average)	3.96	3.95	3.91	3.87
Exchange Rate, vs USD (end-period)	4.01	3.92	3.92	3.85
10Y Government Bond Yield (average)	3.54	3.51	3.47	3.51
10Y Government Bond Yield (end-period)	3.52	3.50	3.46	3.50

INTERBANK MONEY MARKET

IRS shifted higher in May-26

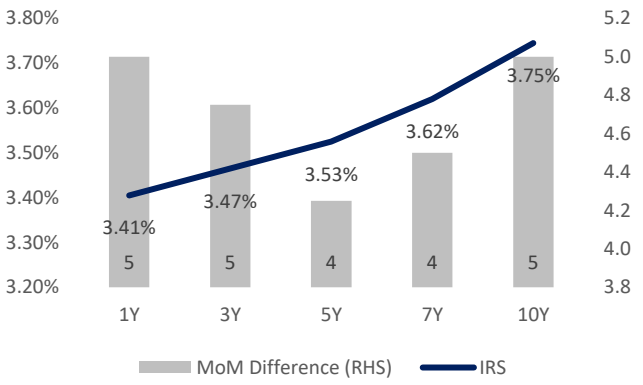
KLIBOR interbank rates were stable and unchanged across the 1M, 3M, and 6M tenures last month at 3.0%, 3.35%, and 3.39%, respectively. However, the IRS market saw a broad-based increase in May-26, as the 1Y, 3Y, 5Y, 7Y, and 10Y tenure moved higher by +5bps, +5bps, +4bps, +4bps, and +5bps to 3.41%, 3.47%, 3.53%, 3.62%, and 3.75%, respectively. With most of the IRS tenors trended higher last month, this suggests the movement also tracked increases in the MGS yields.

Chart 7: KLIBOR and MOM Difference (bps)



Source: Macrobond, MBSBR

Chart 8: IRS and MOM Difference (bps)



Source: Macrobond, MBSBR

CORPORATE BONDS

Monthly corporate bond volume declined

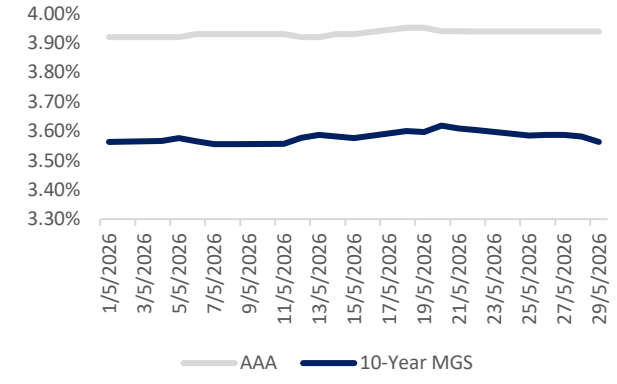
The volume of the traded corporate bond declined RM17.4b in May-26 (Apr-26: RM22.3b), being the third highest for the year. The corporate bond yield mostly increased across the yield curve, with the AA1 space, the increases were in the medium to longer end of the curve. Within the non-rated securities, the yield curve increased between the 5Y to 10Y tenor, while it was mixed at the shorter end.

Table 2: Corporate Bond Yield and MOM Yield Change as at End-May-26

	1Y	2Y	3Y	5Y	7Y	10Y
AAA	3.441	3.538	3.623	3.728	3.831	3.938
AA1	3.476	3.568	3.653	3.757	3.861	3.974
A1	3.896	4.033	4.161	4.369	4.558	4.8
BBB1	5.37	5.883	6.306	6.943	7.511	8.27
Non-rated	5.763	5.867	5.484	5.144	5.22	5.96
MOM Difference (bps)						
AAA	+0	+1	+2	+2	+3	+2
AA1	-0	+0	+2	+2	+3	+1
A1	+0	+1	+0	+1	+1	+1
BBB1	+0	+0	+0	+1	+0	-0
Non-rated	+2	-3	-0	+4	+4	+2

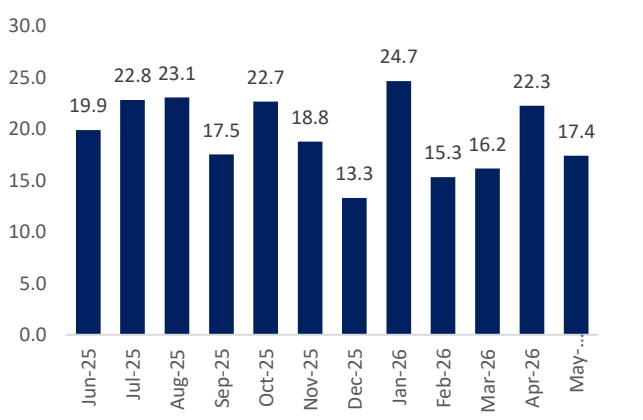
Source: Bondstream, MBSBR

Chart 9: 10-Year AAA vs 10-Year MGS Yields (%)



Source: Macrobond, MBSBR

Chart 10: Volume of Corporate Bond Traded (RM b)



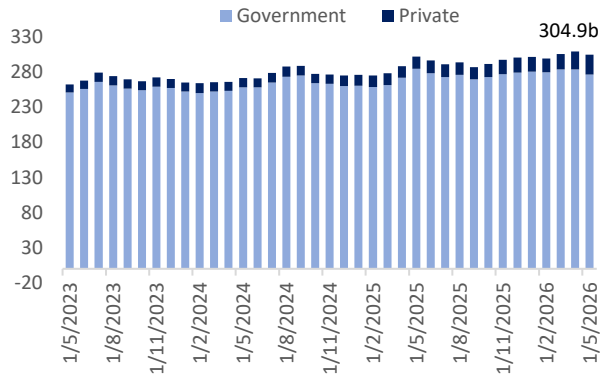
Source: Macrobond, MBSBR

FOREIGN HOLDINGS OF MALAYSIAN BONDS

Foreign holdings of Malaysian bonds declined in Jun-26

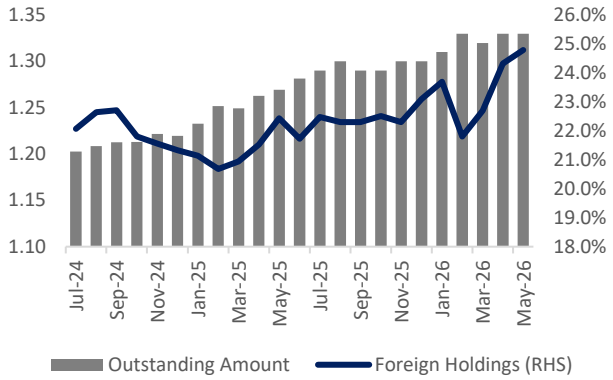
Foreign funds registered outflows in May-26 with foreign holdings of Malaysian bonds declining by -RM4.2b to RM304.9b (Apr-26: RM309.2b). The size of foreign holdings tracked lower but still above the RM300b level last month. We estimate that the ratio of foreign holdings out of the total outstanding government bonds, including the MGS and sukuk was slightly higher at 24.8% (Apr-26: 24.3%)

Chart 11: Foreign Holdings of Malaysian Bonds (RM b)



Source: Macrobond, MBSBR

Chart 12: Share of Foreign Holdings of MGS/GII



Source: Macrobond, MBSBR

APPENDICES

Table 4: MGS/GII Auctions Calendar

Tender Date	Issues	Quarter	Month	Issue Date	Issuance (RM mil)	Private Placement (RM million)	BTC (Times)
08/04/2025	15-year Reopening of MGII 07/40	2QCY25	April	08/04/2025	3,000.00	1,000.00	2.89
15/04/2025	3-year Reopening of MGS 04/28	2QCY25	April	15/04/2025	5,000.00	-	3.46
30/04/2025	10-year New Issue of MGII 05/30	2QCY25	April	30/04/2025	5,000.00	-	2.00
14/05/2025	5-year New issue of MGS 04/35	2QCY25	May	15/05/2025	5,000.00		2.13
23/05/2025	20-year New issue of MGII 05/45	2QCY25	May	30/05/2025	3,000.00	2,000.00	3.32
10/06/2025	15-year Reopening of MGS 04/39	2QCY25	June	10/06/2025	3,000.00		2.86
16/06/2025	30-year Reopening of MGII 03/54	3QCY25	June	16/06/2025	3,000.00	2,000.00	3.30
30/06/2025	10-year New Issue of MGS 07/35	3QCY25	June	30/06/2025	5,000.00		3.01
04/07/2025	7-year Reopening of MGII 10/31	3QCY25	July	04/07/2025	5,000.00		2.92
15/07/2025	30-year New Issue of MGS 07/55	3QCY25	July	15/07/2025	3,000.00	2,000.00	2.00
22/07/2025	10-year Reopening of MGS 04/35	3QCY25	July	22/07/2025	5,000.00		2.73
08/08/2025	20-year Reopening of MGS 05/44	3QCY25	August	08/08/2025	2,500.00	2,000.00	2.73
15/08/2025	15-year Reopening of MGII 07/40	3QCY25	August	15/08/2025	3,000.00	1,000.00	2.85
22/08/2025	5-year Reopening of MGS 05/40	3QCY25	August	22/08/2025	5,000.00		1.87
29/08/2025	20-year Reopening of MGII 05/45	3QCY25	August	29/06/2025	3,000.00	2,000.00	1.84
09/09/2025	3-year Reopening of MGS 04/28	3QCY25	Sep	09/09/2025	5,000.00		1.93
17/09/2025	30-year Reopening of MGII 03/54	3QCY25	Sep	17/09/2025	3,00000	2,000.00	1.93
23/09/2025	15-year Reopening of MGS 04/39	3QCY25	Sep	23/09/2025	3, 500.00	1,000.00	1.52
30/09/2025	3-year Reopening of MGII 07/28	3QCY25	Sep	30/09/2025	5, 000.00		2.88
07/10/2025	30-year Reopening of MGS 07/55	4QCY25	October	07/10/2025	3,000.00	2,000.00	1.38
15/10/2025	5-year Reopening of MGII 08/30	4QCY25	October	15/10/2025	5,000.00		2.81
22/10/2025	20-year Reopening of MGS 05/44	4QCY25	October	22/10/2025	2,500.00	2,000.00	1.70
12/11/2025	10-year Reopening of MGII 04/35	4QCY25	Nov	12/11/2025	5,000.00		2.57
19/11/2025	7-year Reopening of MGS 07/32	4QCY25	Nov	19/11/2025	4,000.00		1.91
26/11/2025	20-year Reopening of MGII 05/45	4QCY25	Nov	26/11/2025	3,000.00		2.72
15/12/2025	10-year Reopening of MGS 07/35	4QCY25	Dec	15/12/2025	3,000.00		1.92
07/01/2026	5-year Reopening of MGII 08/30	1QCY26	Jan	08/01/2026	5,000.00		2.30
14/01/2026	15-year New Issue of MGS 01/41	1QCY26	Jan	15/01/2026	3,500.00	1,500.00	1.94
29/01/2026	30-year New Issue of MGII 01/56	1QCY26	Jan	31/01/2026	3,000.00	2,000.00	2.07
05/02/2026	10-year Reopening of MGII 07/35	1QCY26	Feb	02/07/2026	5,000.00		1.60
16/02/2026	20-year Reopening of MGII 05/45	1QCY26	Feb	16/02/2026	3,000.00	2,000.00	3.04
27/02/2026	5-year Reopening of MGS 06/31	1QCY26	Feb	27/02/2026	5,000.00		2.90
10/03/2026	15-year New Issue of MGII 07/40	1QCY26	Mar	10/03/2026	3,500.00	1,500.00	2.30
16/03/2026	3-year New Issue of MGS 03/29	1QCY26	Mar	16/03/2026	5,000.00		2.22
31/03/2026	7-year New Issue of MGII 03/33	1QCY26	Mar	31/03/2026	5,000.00		1.69
08/04/2026	30-year Reopening of MGS 07/55	2QCY26	Apr	08/04/2026	3,000.00	2,000.00	2.86
15/04/2026	3.5-year New Issue of MGII 10/29	2QCY26	Apr	08/04/2026	5,000.00		2.92
23/04/2026	20-year New Issue of MGS 04/46	2QCY26	Apr	23/04/2026	3,5000.00	1,500.00	3.56
15/05/2026	10-year Reopening of MGII 04/35	2QCY26	May	15/05/2026	5,000.00		2.87
22/05/2026	7-year Reopening of MGS 04/33	2QCY26	May	22/05/2026	5,000.00		2.59
29/05/2026	30-year Reopening of MGS 01/56	2QCY26	May	29/05/2026	3,000.00	2,000.00	2.29
05/06/2026	3-year Reopening of MGS 03/29	2QCY26	June	05/06/2026	5,000.00		

Table 5: Top Traded Government Bonds

Stock Name	Traded amount (RM m)
MGS 1/2019 3.906% 15.07.2026	2,173.40
GII MURABAHAH 3/2016 4.070% 30.09.2026	1,788.53
GII MURABAHAH 3/2016 4.070% 30.09.2026	1,526.20
GII MURABAHAH 3/2025 3.612% 30.04.2035	1,473.00
GII MURABAHAH 1/2023 3.599% 31.07.2028	1,445.68
MGS 3/2016 3.900% 30.11.2026	1,416.12
MGS 1/2019 3.906% 15.07.2026	1,386.47
GII MURABAHAH 3/2016 4.070% 30.09.2026	1,376.70
MGS 2/2020 2.632% 15.04.2031	1,298.00
MGS 2/2023 3.519% 20.04.2028	1,283.83
Total	15,167.93

MBSB RESEARCH (formerly known as MIDF Research) is part of
MBSB Investment Bank Berhad (formerly known as MIDF Amanah Investment Bank)
(Bank Pelaburan) (A Participating Organisation of Bursa Malaysia Securities Berhad)

DISCLOSURES AND DISCLAIMER

This report has been prepared by MBSB INVESTMENT BANK BERHAD (formerly known as MIDF Amanah Investment Bank Berhad) 197501002077 (24878-X).

It is for distribution only under such circumstances as may be permitted by applicable law.

Readers should be fully aware that this report is for information purposes only. The opinions contained in this report are based on information obtained or derived from sources that we believe are reliable. MBSB INVESTMENT BANK BERHAD (formerly known as MIDF AMANAH INVESTMENT BANK BERHAD) makes no representation or warranty, expressed or implied, as to the accuracy, completeness or reliability of the information contained therein and it should not be relied upon as such.

This report is not, and should not be construed as, an offer to buy or sell any securities or other financial instruments. The analysis contained herein is based on numerous assumptions. Different assumptions could result in materially different results. All opinions and estimates are subject to change without notice. The research analysts will initiate, update and cease coverage solely at the discretion of MBSB INVESTMENT BANK BERHAD (formerly known as MIDF AMANAH INVESTMENT BANK BERHAD).

The directors, employees and representatives of MBSB INVESTMENT BANK BERHAD (formerly known as MIDF AMANAH INVESTMENT BANK BERHAD) may have an interest in any of the securities mentioned and may benefit from the information herein. Members of the MBSB Group and their affiliates may provide services to any company and affiliates of such companies whose securities are mentioned herein This document may not be reproduced, distributed or published in any form or for any purpose.