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Markit Commentary

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Indonesian and Malaysian credit lift from lows

The commodities slowdown has seen Indonesian and Malaysian credit come under increasing pressure, but the recent monetary easing from their biggest trading partner China has seen this trend reverse.

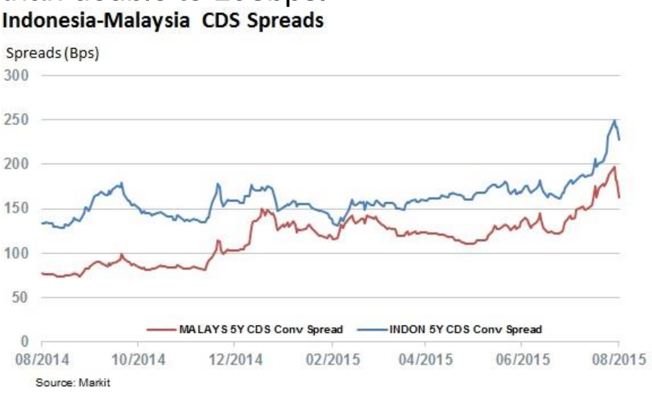
- Malaysian and Indonesian CDS spreads are both 10% off their highs seen on Monday
- Bond yields yet to reflect this trend with 10 year bonds in both countries at yearly highs
- Dollar denominated corporate bonds in both countries are now in negative territory for 2015

Indonesia and Malaysia were two of the worst impacted countries in the wake of the Chinese and wider emerging market slowdown. Both their currencies retreated to multi year lows against the dollar as their export driven economic models came under strain from the commodities slump.

This pressure saw the credit market turn increasingly bearish with both countries seeing CDS spreads and bond yields hit recent highs in the last couple of weeks.

CDS spreads surge only to retreat

The recent developments saw credit investors treat both Indonesian and Malaysian bonds with a greater degree of bearishness, demonstrated by the fact that 5 year CDS spreads for both Malaysian and Indonesian sovereign bonds surged to new recent highs earlier this week. At the crux of Monday's selloff, Indonesian CDS spreads were 70% higher than the level seen a year ago, while Malaysian bonds saw their spreads more than double to 198bps.



Both Indonesia and Malaysia have seen their CDS spreads come down over the last couple of days. This move coincides with the recent loosening of Chinese monetary policy which saw the country lower both its reserve requirement and benchmark interest rates in order to prop up its economy. This move saw Malaysian CDS spreads tighten by 34bps to 163bps. Indonesian CDS spreads also moved in the same direction with a 21bps tightening to 228bps. Despite the recent tightening, CDS investors are still much more bearish on both countries than 12 months ago.

Government bonds at lows

Sovereign bonds in both countries have also come under pressure in recent weeks with the both Indonesia and Singapore seeing their 10 year bonds surge to recent highs in the last couple of weeks. 10 year locally denominated Malaysian bonds are now yielding 4.5%; over 50bps more than the yearly seen in early April.

Indonesian bonds have proven even more volatile with 10 year yields touching 9% on Tuesday, over 200bps higher than the levels seen in early March.

Unlike the CDS spreads, both countries have yet to reflect the recent shift in Chinese monetary policy as both yields are at or near the yearly highs.

Corporate bonds also under stress

The volatile situation has also seen total returns delivered by dollar denominated bonds issued by Indonesian and Malaysian companies head negative for the year. Total returns for Malaysian corporate bonds as represented by the Markit iBoxx USD Corporates Malaysia Index are now -0.2% for the year having been as high as 3% in early April. Indonesian bonds have been even more volatile as the -1.86% total returns which the Markit iBoxx USD Corporates Indonesia Index has delivered is now over 8% off the highs seen in April.

Bonds in both countries are now underperforming their regional peers as the Markit iBoxx USD Emerging Markets Corporates Asia Index is still sitting on a relatively healthy 1.28% total return for the year.

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