05 January 2026

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YIELD DIVERGENCE AMID FED POLICY UNCERTAINTY

Fed Minutes Reveal Deep Divisions Over December Rate Cut Amid Inflation Fears. Minutes from the Federal Reserve's (Fed's) December 9–10 meeting reveal a central bank deeply fractured over the path of monetary policy, despite ultimately approving a quarter-point rate cut to a range of 3.5%–3.75%. Although the 9–3 vote was the most lopsided in terms of dissents since 2019, the minutes clarify that the decision was even more precarious than the tally suggests, with several supporters describing the choice as finely balanced and nearly opting to hold rates steady. This internal friction stems from a difficult tug-of-war between a cooling labor market and inflation progress that many officials believe stalled in 2025. While the committee's dot plot points toward a neutral rate of 3.00% by 2027, policymakers expressed growing anxiety over upside inflation risks—specifically citing the temporary but significant impact of President Trump's tariffs—against the backdrop of a domestic economy that saw GDP soar at a 4.3% annualized pace in the third quarter. The path forward is further obscured by a data vacuum resulting from the recent government shutdown, leaving officials wary of making aggressive moves based on incomplete official reports. Amid this uncertainty, the Fed took the significant step of resuming its bond-buying program, committing to purchase USD40 billion in Treasury bills monthly to prevent bank reserves from dipping below ample levels. With four notably more hawkish regional presidents set to rotate into voting roles and a general consensus to proceed with caution, the markets are now bracing for a period of inactivity. As the Federal Open Market Committee (FOMC) waits for clearer economic signals to emerge from the post-shutdown fog, the focus has shifted from aggressive easing to a "wait-and-see" approach intended to ensure inflation sustainably returns to the 2.0% target without triggering a sharper downturn in employment.

Trump Intensifies Venezuela Campaign with New Sanctions and Coastal Strikes. On December 31, 2025, the Trump administration intensified its economic and military pressure on Venezuela by sanctioning four companies—Zhejiang-based Corniola Ltd and Hong Kong-based Aries Global Investment Ltd, Krape Myrtle Co, and Winky International Ltd—along with four oil tankers (Della, Nord Star, Rosalind, and Valiant) for their involvement in Maduro's shadow fleet. This rare move against Chinese entities serves as a strategic warning to Beijing, Venezuela's primary oil customer, to distance itself from the regime. This escalation coincided with a significant expansion of U.S. military operations under Operation Southern Spear; on December 29, the CIA conducted a drone strike on a Venezuelan loading dock, marking the first direct strike on Venezuelan soil. Additionally, U.S. Southern Command reported sinking multiple suspected narco-trafficking vessels in late December and early January, resulting in at least eight deaths. While China has condemned these actions as unilateral bullying and a violation of international law, the U.S. continues to justify the campaign as a necessary measure to dismantle narco-terrorist networks.

Upcoming Events: Key Economic Data Release

Monday	Indonesia CPI (December), Singapore Retail Sales (November)
Tuesday	S&P Global PMI (December)
Wednesday	Euro Area Inflation (December)
Thursday	Euro Area Unemployment Rate
Friday	China Inflation (December), U.S. Jobs Data (December)

Weekly Changes, basis points (bps)

UST	Yields (%) 19-Dec-25	Yields (%) 26-Dec-25	Change (bps)	Yields (%) 2-Jan-26	Change (bps)
3-Y UST	3.53	3.54	1	3.55	1
5-Y UST	3.70	3.68	-2	3.74	6
7-Y UST	3.91	3.89	-2	3.95	6
10-Y UST	4.16	4.14	-2	4.19	5
MGS	Yields (%) 19-Dec-25	Yields (%) 26-Dec-25	Change (bps)	Yields (%) 2-Jan-26	Change (bps)
3-Y MGS	3.02	3.01	-2	3.00	-1
5-Y MGS	3.27	3.25	-2	3.25	0
7-Y MGS	3.45	3.41	-4	3.37	-4
10-Y MGS	3.56	3.54	-2	3.50	-4
GII	Yields (%) 19-Dec-25	Yields (%) 26-Dec-25	Change (bps)	Yields (%) 2-Jan-26	Change (bps)
3-Y GII	3.12	3.10	-2	3.09	-1
5-Y GII	3.28	3.25	-2	3.25	0
7-Y GII	3.36	3.35	-1	3.34	-1
10-Y GII	3.56	3.55	-2	3.52	-3

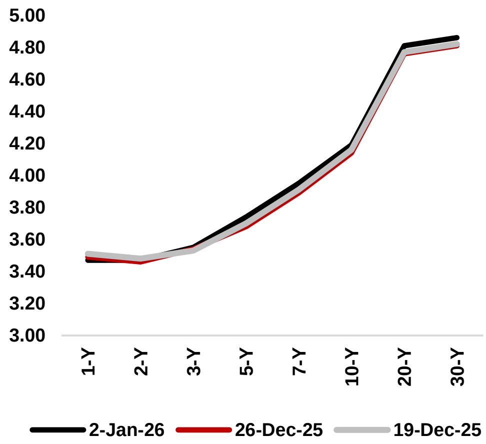
Sources: Federal Reserve Board, BNM, Bank Islam

Commentaries

UST Yields The U.S. Treasury (UST) yields edged higher in the range of 1bp to 6bps w-o-w for the week ending January 2 (December 26: -4bps to +1bp). An increase in long-term yields led to a modest bear steepening of the yield curve, driven by hawkish undertones in the FOMC minutes that revealed significant internal disagreements regarding the economic outlook. This upward pressure was further intensified by lower-than-expected jobless claims. The U.S. jobless claims unexpectedly plunged to 199K for the week ending December 27, well below the anticipated 220K. Despite the usual year-end volatility, this marks the strongest reading for the labor market since early 2025, excluding a three-year low reached in late November.

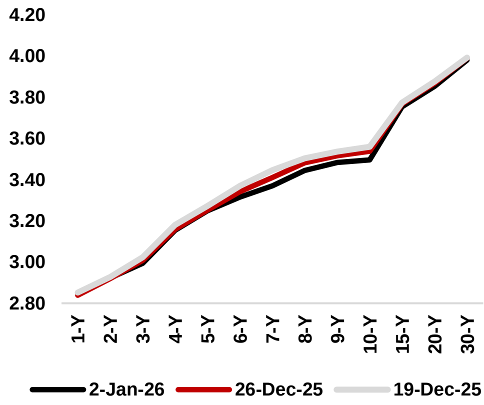
Short-term outlook: UST yields could drift lower next week as investors prepare for a series of high-impact economic indicators. The primary focus will be on labor market data—including ADP employment, JOLTS, non-farm payrolls, and the unemployment rate—to shape interest rate expectations. Despite a mixed consensus, emerging signs of a cooling labor market may exert downward pressure on yields, though any reports of robust economic activity could act as a floor, limiting the extent of the decline.

UST Yield Curves, %



Sources: Federal Reserve Board, Bank Islam

MGS Yield Curves, %



Sources: BNM, Bank Islam

MGS/GII Yields Malaysian Government Securities (MGS) and Government Investment Issues (GII) yields mostly declined, moving downwards within a narrow range of 1bp to 4bps for the week ending January 2 (December 26: -1bp to -4bps). Meanwhile, 5-Y MGS and GII yields plateaued at 3.25%.

Domestic yields moved lower as a resilient macroeconomic story and consistent investor interest supported the market. This positive sentiment was further bolstered by Malaysia's external trade strength, Malaysia's trade performance remains on a record-breaking trajectory, with total trade reaching RM2.77 trillion and exports hitting RM1.45 trillion during the first 11 months of 2025. According to MATRADE, this performance marks the fifth consecutive year that Malaysia has surpassed the trillion-ringgit milestone, positioning the nation to finish the year with a new all-time high.

Key growth metrics from January to November show a 6.1% increase in exports, a 5.8% rise in total trade, and a 5.6% uptick in imports compared to the same period last year. Furthermore, the trade surplus widened significantly, growing by 10.7% to RM132.5 billion, underscoring the resilience and strength of Malaysia's external trade sector.

Short-term Outlook: Local yields are expected to remain range-bound with a slight downward bias as the market processes a heavy data schedule. The steady December PMI reading of 50.1 points has established a stable baseline, while upcoming releases—including November industrial production (IPI), retail sales, and labor market figures due on January 9—are expected to anchor investor sentiment and encourage continued inflows into the domestic debt market. Externally, the focus remains on U.S. labor data; a softer employment report would likely cement expectations for Federal Reserve easing, providing further tailwinds for a decline in local yields.

Auction Calendar 2026

The 2026 Auction Calendar released on the FAST BNM portal outlines a total of 37 scheduled issuances, reflecting a balanced approach to fiscal financing. The government maintains a near-equal distribution between conventional and Shariah-compliant papers, supporting Malaysia's dual financial system. Government Investment Issues (MGII): 19 issuances (51.4%). Malaysian Government Securities (MGS): 18 issuances (48.6%).

Month	Issue / Tenor	Private Placement	Estimated Amount (RM Mil)
Jan	5-yr Reopening of MGII 8/30 3.635%	No	5,000
	15-yr New Issue of MGS (Mat on 01/41)	*Yes*	*5,000*
	30-yr New Issue of MGII (Mat on 01/56)	*Yes*	*5,000*
Feb	10-yr Reopening of MGS 7/35 3.476%	No	5,000
	20-yr Reopening of MGII 5/45 3.775%	Yes	5,000
	5-yr Reopening of MGS 6/31 4.232%	No	5,000
Mar	15-yr Reopening of MGII 7/40 3.974%	Yes	5,000
	3-yr New Issue of MGS (Mat on 03/29)	*No*	*5,000*
	7-yr New Issue of MGII (Mat on 03/33)	*No*	*5,000*
Apr	30-yr Reopening of MGS 7/55 3.917%	Yes	5,000
	3.5-yr New Issue of MGII (Mat on 10/29)	*No*	*5,000*
	20-yr New Issue of MGS (Mat on 04/46)	*Yes*	*5,000*
May	*10-yr Reopening of MGII 4/35 3.612%*	No	*5,000*
	7-yr Reopening of MGS 4/33 3.844%	No	5,000
	30-yr Reopening of MGII 1/56	Yes	5,000

Jun	3-yr Reopening of MGS 3/29	No	5,000
	15-yr Reopening of MGII 7/40 3.974%	Yes	5,000
	5-yr Reopening of MGS 6/31 4.232%	No	5,000
	20-yr Reopening of MGII 5/45 3.775%	Yes	5,000
Jul	10-yr Reopening of MGS 7/35 3.476%	No	5,000
	3.5-yr Reopening of MGII 10/29	No	5,000
	15-yr Reopening of MGS 1/41	Yes	5,000
Aug	5-yr Reopening of MGII 10/31 3.804%	No	5,000
	30-yr Reopening of MGS 7/55 3.917%	Yes	5,000
	7-yr Reopening of MGII 3/33	No	5,000
	20-yr Reopening of MGS 4/46	Yes	5,000
Sep	10-yr Reopening of MGII 7/36 3.447%	No	5,000
	7-yr Reopening of MGS 4/33 3.844%	No	5,000
	30-yr Reopening of MGII 1/56	Yes	5,000
Oct	3.5-yr Reopening of MGII 10/29	No	5,000
	15-yr Reopening of MGS 1/41	Yes	5,000
	20-yr Reopening of MGII 5/45 3.775%	*Yes*	*5,000*
	10-yr New Issue of MGS (Mat on 10/36)	*No*	*5,000*
Nov	15-yr Reopening of MGII 7/40 3.974%	Yes	5,000
	3-yr Reopening of MGS 3/29	No	5,000
	10-yr Reopening of MGII 7/36 3.447%	No	5,000
Dec	30-yr Reopening of MGS 7/55 3.917%	Yes	4,000
		Total	184,000

Source: FAST BNM

Maturity and Duration Profile

The calendar shows a pronounced concentration in long-dated papers, which suggests an intent to lock in funding for longer durations and cater to the demand from pension funds and insurers.

Tenor Bucket	Number of Auctions	%
Short-Term (3Y – 3.5Y)	6	16.2
Medium-Term (5Y – 7Y)	8	21.6
Benchmark (10Y)	6	16.2
Long-End (15Y, 20Y, 30Y)	17	46.0
Total	**37**	**100**

Quarterly Supply Dynamics

Issuance activity is slightly front-to-mid-loaded, with the highest concentration of auctions occurring in the second and third quarters.

1Q2026: 9 issuances (Average of 3 per month).

2Q2026: 10 issuances.

3Q2026: 10 issuances.

4Q2026: 8 issuances (Tapering off toward year-end).

Estimated 2026 Auction Amounts

The Federal Government's financing needs are driven by two main factors:

1. *Net Borrowing (The Deficit)*: RM74.6 billion (as per Budget 2026).
2. *Refinancing (Maturities)*: RM108.7 billion in MGS and MGII are maturing in 2026.

2026 Government Bond Maturities

Maturity date	Stock	RM billion
31-Mar-26	MGS 1/2018 3.882% 14.03.2025	25.5
15-Apr-26	MGS 3/2005 4.837% 15.07.2025	8.4
15-Jul-26	GII MURABAHAH 1/2018 4.128% 15.08.2025	20.0
15-Sep-26	MGS 1/2015 3.955% 15.09.2025	2.3
30-Sep-26	GII MURABAHAH 4/2015 3.990% 15.10.2025	29.5
30-Nov-26	MGS 1/2015 3.955% 15.09.2025	23.0
	Total Maturity	**108.7**

Source: Bloomberg

This brings the total Gross Issuance Requirement to approximately RM183.3 billion. Spread across 37 auctions, the average issuance size is roughly RM4.95 billion per auction.