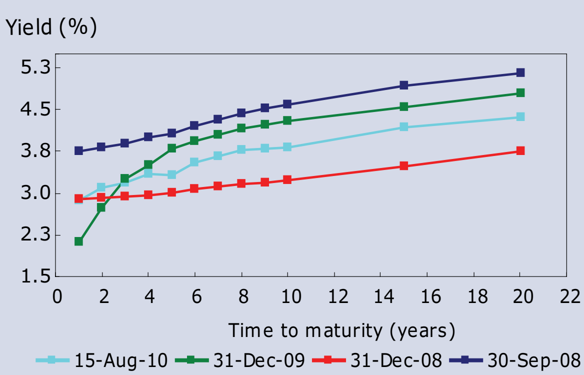
Malaysia—Update

Yield Movements

An increase in the overnight policy rate (OPR), an uptick in consumer price inflation, and robust growth in the first half of the year resulted in the flattening of Malaysia's government bond yield curve. Between end-2009 and mid-August, yields rose at the short-end and dropped in the belly and at the long-end of the curve **(Figure 1)**. Bank Negara Malaysia (BNM) has already raised its key rate three times this year, increasing the OPR by a total of 75 basis points to 2.75%. Before an initial increase in February, the OPR had been kept at a historic low of 2.0% since February 2009.

Driven by sustained growth in domestic and external demand, Malaysia's economy expanded 8.9% year-on-year (y-o-y) in 2Q10, which brought the country's gross domestic product (GDP) growth to 9.5% in the first half of the year. Domestic demand grew 9.0% y-o-y in 2Q10, higher than growth of 5.3% recorded in 1Q10, mainly due to higher levels of private consumption as well as increased business and public sector spending. Relatively low inflation coupled with favorable labor market conditions and improved consumer confidence led to 7.9% y-o-y growth in private consumption. Meanwhile, public sector spending increased 6.9% y-o-y in 2Q10 and gross fixed capital formation grew 9.4% y-o-y.

Figure 1: Malaysia's Benchmark Yield Curve–LCY Government Bonds



LCY = local currency.
Source: Bloomberg LP.

Prices in Malaysia continued to rise as domestic demand and public sector spending fueled economic growth. In July, consumer price inflation rose slightly to 1.9% y-o-y from 1.7% in June and 1.6% in May. For January–July, consumer price inflation was reported at 1.5% y-o-y.

Size and Composition

At the end of June, total outstanding local currency (LCY) bonds in Malaysia stood at MYR695.9 billion, up 14.0% y-o-y. Outstanding government LCY bonds expanded 18.3% y-o-y to MYR401.2 billion. Excluding central bank bills, outstanding government LCY bonds rose 12.5% y-o-y **(Table1)**.

Issuance of government LCY bonds (excluding central bank bills) was lower in 1H10 compared with 1H09, as the government had issued more bonds in 2009 to fund its MYR60.0 billion stimulus program. The government issued a total of MYR21.0 billion of Malaysian Government Securities (MGS) in the first 6 months of 2010 compared with MYR32.0 billion in the same period last year. Issuance of Government Investment Issues (GII) likewise fell, from MYR16.5 billion in 1H09 to MYR12.0 billion in 1H10.

The issuance of central bank bills increased as the central bank mopped up excess liquidity in the market amid rising consumer price inflation. Issuance of central bank bills reached MYR68.2 billion in 2Q10 from MYR35.5 billion in 1Q09.

In 2Q10, total corporate LCY bonds outstanding grew 8.6% y-o-y, and 3.1% on a quarter-on-quarter (q-o-q) basis, to reach MYR294.7 billion.

After a slow start in 1Q10, the issuance of corporate LCY bonds picked up in 2Q10.

Table 1: Size and Composition of the LCY Bond Market in Malaysia

	Amount (billion)								Growth Rate (%)						
	Mar-10		Apr-10		May-10		Jun-10		Mar-10		Apr-10	May-10	Jun-10		
	MYR	USD	MYR	USD	MYR	USD	MYR	USD	y-o-y	q-o-q	m-o-m	m-o-m	y-o-y	q-o-q	m-o-m
Total	648.0	198.6	674.3	211.8	686.2	210.3	695.9	215.7	11.0	(98.4)	4.1	1.8	14.0	7.4	1.4
Government	362.2	111.1	381.7	119.9	392.8	120.4	401.2	124.4	12.7	4.4	5.4	2.9	18.3	10.8	2.1
Central Government Bonds	328.1	100.6	322.7	101.3	322.7	98.9	331.2	102.7	22.2	5.0	(1.6)	—	15.0	0.9	2.6
Central Bank Bills	32.5	9.9	57.6	18.1	69.2	21.2	69.1	21.4	(27.1)	8.2	77.3	20.2	58.0	112.8	(0.1)
Others	1.7	0.5	1.5	0.5	1.0	0.3	1.0	0.3	(79.9)	(60.1)	(14.4)	(34.2)	(87.1)	(43.7)	—
Corporate	285.7	87.6	292.6	91.9	293.4	89.9	294.7	91.4	9.0	(0.9)	2.4	0.3	8.6	3.1	0.4

LCY = local currency, m-o-m = month-on-month, q-o-q = quarter-on-quarter, y-o-y = year-on-year.
Notes:
1. Calculated using data from national sources.
2. Bloomberg end-of-period LCY–USD rate is used.
3. Growth rates are calculated from LCY base and do not include currency effects.
4. "Others" refer to Khazanah Bonds issued by Khazanah Nasional Berhad and Cagamas, Bonds and Notes, Bithaman Ajil Islamic Securities, Sanadat ABBA Cagamas and Sanadat Mudharabah Cagamas issued by Cagamas Berhad.
Source: Bank Negara Malaysia and Bloomberg LP.

Malaysia's corporate LCY bond issuance totaled MYR22.9 billion in 2Q10, 90.4% higher than the MYR12.0 billion posted in 1Q10, but 18.0% lower compared with the MYR28.0 billion issued in 2Q09. Among the biggest issuances during the period were Bank Pembangunan Malaysia (MYR2.5 billion), Khazanah Nasional subsidiary Danga Capital (MYR2.0 billion), national mortgage corporation Cagamas Berhad (MYR1.8 billion), AmBank (MYR1.3 billion), RHB Bank (MYR1.0 billion), and CIMB Group (MYR750 million).

The top 20 corporate issuers in Malaysia comprised 48.3% of total corporate bonds outstanding in 2Q10 **(Table 2)**. Cagamas Berhad remained the top issuer of corporate bonds with MYR18.2 billion outstanding in conventional and Islamic *(sukuk)* medium-term notes, followed by the government's investment holding arm, Khazanah Nasional, and the investment holding company, Binariang GSM, with MYR13.2 billion and MYR11.5 billion, respectively.

Investor Profile

At the end of June, financial institutions were the largest holders of government bonds, with 43.7% of total outstanding MGS and GII, followed by social security institutions, which held 30.2%. Foreign holders and insurance companies held 18.1% and 6.0%, respectively, of total outstanding MGS and GII **(Figure 2)**.

Meanwhile, foreign holdings of MGS increased from 16.9% at end-December to 23.4% at end-June **(Figure 3)**.With the relaxation of foreign exchange rules (see Policy, Institutional, and Regulatory Developments), the Malaysian ringgit gained against the US dollar in 2Q10 and government bonds rallied on expectations of the ringgit's further appreciation, which has already gained 9.4% against the US dollar since the beginning of the year.

Turnover Ratio

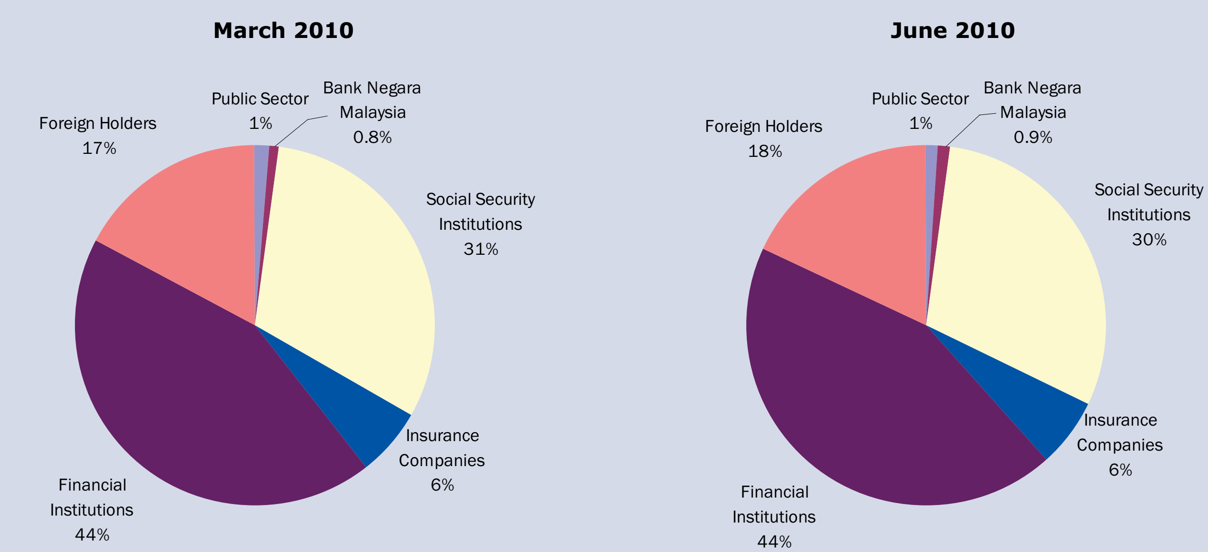
Monthly data showed government bond trading volume rose to MYR71.5 billion in January

Table 2: Top 20 Corporate Issuers, June 2010 (MYR billion)

Issuer	Industry	Conventional Bonds	Islamic Bonds	Conventional MTN	Islamic MTN	Total
Cagamas	Finance	—	—	9.30	8.85	18.15
Khazanah	Quasi-Govt. and Other	—	13.20	—	—	13.20
Binariang GSM	Transport, Storage & Comm.	—	3.17	—	8.28	11.45
Project Lebuhraya	Transport, Storage & Comm.	—	6.57	—	3.68	10.25
Prasarana	Finance	5.11	2.00	—	2.00	9.11
Maybank	Finance	6.10	2.50	—		8.60
Rantau Abang Capital Bhd	Quasi-Govt. and Other	—	—	—	8.00	8.00
Malakoff Corp	Finance	—	1.70	—	5.60	7.30
KL International Airport	Transport, Storage & Comm.	1.60	4.76	—	—	6.36
AM Bank	Finance	1.60	—	4.33	—	5.93
Value Cap	Finance	5.10	—	—	—	5.10
1 Malaysia Development Bhd.	Finance	—	—	—	5.00	5.00
Jimah Energy Ventures	Utilities	—	—	—	4.77	4.77
Tanjung Bin	Utilities	—	—	—	4.59	4.59
Bank Pembangunan Malaysia	Finance	1.00	—	2.60	0.90	4.50
Putrajaya Holdings	Finance	—	1.70	—	3.65	5.35
YTL Power International	Utilities	2.20	—	1.70	—	3.90
Tenaga Nasional	Utilities	1.50	2.15	—	—	3.65
Danga Capital	Finance	—	—	—	3.60	3.60
RHB Bank	Finance	0.60	—	3.00	—	3.60
Total		**24.81**	**37.75**	**20.93**	**58.91**	**142.40**
Total Outstanding		**63.48**	**70.47**	**45.48**	**89.40**	**294.65**
Top 20 as % of Outstanding		**39.1%**	**53.6%**	**46.0%**	**65.9%**	**48.3%**

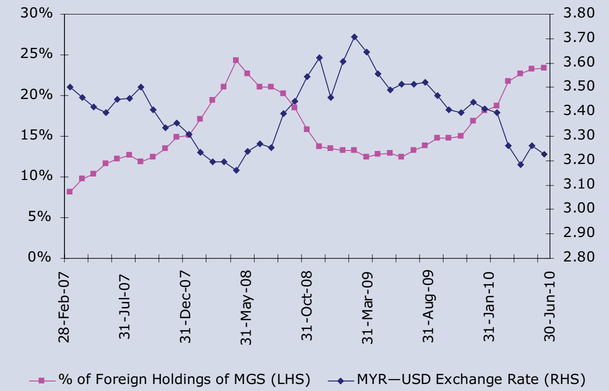
— = not applicable, MTN = medium-term notes.
Source: Bank Negara Malaysia Fully Automated System for Issuing/Tendering (FAST).

Figure 2. LCY Government Bonds Investor Profile



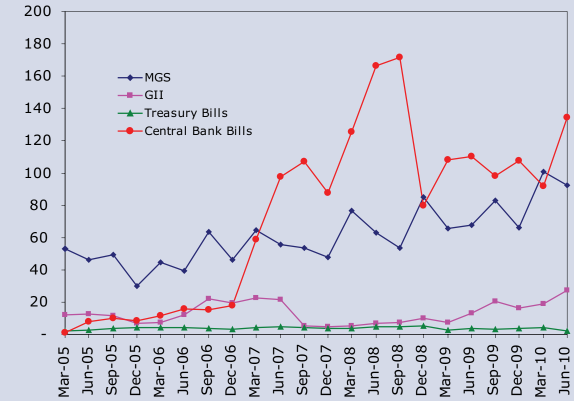
LCY = local currency.
Source: Bank Negara Malaysia.

Figure 3. Foreign Holdings of MGS vs. the MYR—USD Exchange Rate



LHS = left hand side, RHS = right hand side, MGS = Malaysian Government Securities.
Source: Bank Negara Malaysia.

Figure 4. Quarterly Trading Volume for LCY Government Bonds (MYR billion)



LCY = local currency, MGS = Malaysian Government Securities, GII = Government Investment Issues.
Source: Bank Negara Malaysia.

after having fallen in 4Q09, when trading volume averaged MYR65.5 billion per month. Trading volume fell again to MYR54.9 billion in February before rising to MYR89.4 billion in March **(Figure 4)**. The quarterly turnover ratio was 0.61 in 1Q10, compared with 0.56 in 4Q09.

In April, government bond trading volume surged to MYR104.0 billion due to an increase in trading of central bank bills, which reached MYR53.6 billion as their issuance was increased to mop up excess liquidity. Government bond trading volume fell to MYR80.5 billion and MYR71.9 billion in May and June, respectively. The turnover ratio for government bonds stood at 0.67 in 2Q10.

For January–June, the bulk of the trading of government bonds and central bank bills were interbank transactions **(Table 3)**. Of the MYR232.8 billion in government bonds traded in 1H10, MYR184.0 billion of these bonds were traded in the interbank market. About 70% of the trading volume of central bank bills was in the interbank market.

Corporate bond trading volume reached MYR19.2 billion in 1Q10 from MYR16.2 billion in 4Q09. The trading volume increased further in 2Q10 to MYR28.3 billion. As a result, the turnover

Table 3: Securities Turnover by Participant for January–June 2010 (MYR million)

	Interbank	Non-Interbank	Total
Government Bonds	184,018	48,812	232,830
MGS	143,279	45,594	188,872
GII	40,740	3,218	43,958
Treasury Bills	4,311	2,342	6,653
Central Bank Bills	156,150	65,388	221,538

MGS = Malaysian Government Securities, GII = Government Investment Issues.
Note:
Interbank—both buyers and sellers are financial institutions.
Non-Interbank—either the buyer or seller is a financial institution.
Source: Bank Negara Malaysia.

ratio for corporate bonds increased to 0.10 in 2Q10 from 0.06 and 0.07 in 4Q09 and 1Q10, respectively.

Policy, Institutional, and Regulatory Developments

Corporate Debt Restructuring Committee Revises Eligibility Criteria

The Corporate Debt Restructuring Committee (CDRC) has revised its eligibility criteria to allow more companies to seek assistance from the CDRC in restructuring their debt obligations.

Under the revised eligibility criteria, companies seeking to resolve their debt obligations under the CDRC must fulfill the following:

(i) aggregate indebtedness of MYR30 million or more;

(ii) at least two financial creditors;

(iii) not in receivership or liquidation, except in cases where receivers have been appointed over certain specified assets and the directors remain in control over the companies' overall operations; and

(iv) difficulties in servicing debt obligations, which may not include having already defaulted, provided criteria (i) and (ii) are met.

The revised criteria extends eligibility to any company listed on Bursa Malaysia that has been classified as either PN17 (Main Market—the merged main board and second board of Bursa Malaysia) or GN3 (ACE market—the revamp of the Malaysian Exchange Securities Dealing and Automated Quotation [MESDAQ]), irrespective of the amount of debt outstanding.

BNM Further Liberalizes FX Rules

In August, BNM announced the further liberalization of foreign exchange (FX) administrative rules to promote efficiency in trade. The new rules provide for the following:

(i) the use of the ringgit as a settlement currency for the international trade of goods and services between residents and non-residents;

(ii) the borrowing of any amount of foreign currency by a resident company from its respective non-resident, non-bank related company (thus abolishing all limits on cross-border foreign currency inter-company borrowings); and

(iii) the lifting of the limit on residents' anticipatory hedging of current account transactions with licensed onshore banks.

To promote bilateral trade between the People's Republic of China (PRC) and Malaysia, the China Foreign Exchange Trading System (CFETS) has issued a separate statement that allows trading of the PRC yuan against the ringgit. Aside from the ringgit, other currencies that are traded on the CFETS are the US dollar, euro, pound sterling, yen, and Hong Kong dollar.