

Malaysia—Update

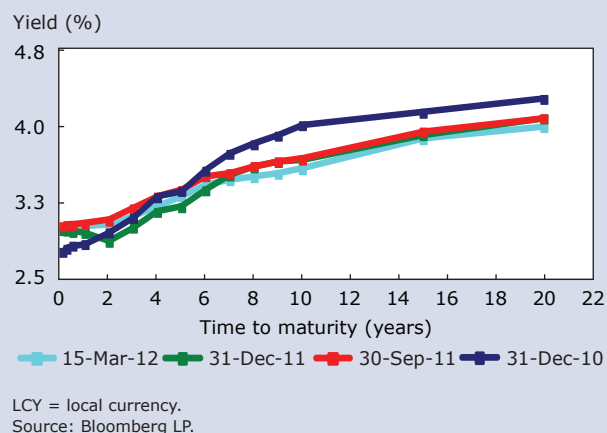
Yield Movements

The yield curve for Malaysian local currency (LCY) government bonds fell across all maturities between end-September and end-December 2011. The yield curve then flattened between end-December and 15 March as yields rose at the short-end and the belly of the curve, but dropped at the long-end (**Figure 1**). Yields at the very short-end rose between 2 basis points (bps) and 4 bps, while 2- and 3-year maturities rose 17 bps and 12 bps, respectively. Yields for the 5-year maturity rose 11 bps, while yields for 4- and 6-year maturities both increased by 6 bps. On the other hand, yields between the 7- and 20-year maturities fell 5 bps–12 bps. The yield spread between 2- and 10-year maturities narrowed to 92 bps in mid-March from 106 bps at end-December.

Bank Negara Malaysia (BNM) decided to keep its overnight policy rate steady at 3.0% after its Monetary Policy Committee meeting on 9 March. BNM has kept its rate at this level since May last year. Consumer price inflation averaged 3.2% in 2011 and is expected to moderate in 2012 as cost-push inflation eases amid a slowdown in global economic activity. Malaysia's consumer price inflation slowed to 2.2% year-on-year (y-o-y) in February from 2.7% in January. Index for food and non-alcoholic beverages increased 2.9% y-o-y in February, significantly lower than the 4.8% y-o-y increase posted in January. Meanwhile, index for non-food increased 1.8% y-o-y in February, slightly higher than January's 1.7%.

Malaysia's gross domestic product (GDP) expanded 5.2% y-o-y in 4Q11, down slightly from the 5.8% growth posted in 3Q11. Growth in 4Q11 was supported by sustained domestic demand that increased 10.5% y-o-y, compared with 9.0% in 3Q11, and was driven by higher growth in public sector consumption and gross fixed capital formation. On the other hand, net exports dropped 25.7% y-o-y in 4Q11 in a reversal from the 18.1% increase posted in

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



the previous quarter. For the full-year 2011, Malaysia's GDP increased 5.1%.

Size and Composition

Total LCY bonds outstanding reached MYR833.8 billion (US\$263.2 billion) at the end of 2011, up 10.4% y-o-y but flat on a quarter-on-quarter (q-o-q) basis (**Table 1**). Growth in LCY government bonds eased to 12.0% y-o-y in 4Q11—for a total of MYR499.0 billion (US\$157.5 billion)—after posting a 19.8% increase in 3Q11. Central government bills and bonds rose 13.0% y-o-y at end-December versus 10.9% at end-September. However, central bank bills growth slowed to 9.3% y-o-y at end-December from 58.0% at end-September. On a q-o-q basis, total LCY government bonds outstanding fell 1.2% in 4Q11.

Issuance of government bonds—Malaysian Government Securities (MGSs) and Government Investment Issues (GIIs)—increased 92.8% y-o-y to MYR20.2 billion in 4Q11. Total government bond issuance increased 60.6% in 2011 to reach MYR93.3 billion, up from MYR58.1 billion in 2010. A total of MYR48.1 billion worth of government bonds matured in 2011, which brought net issuance to MYR45.2 billion.

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

	Amount (billion)						Growth Rate (%)										
	Sep-11		Oct-11		Nov-11		Dec-11		Sep-11		Oct-11		Nov-11		Dec-11		
	MYR	US\$	MYR	US\$	MYR	US\$	MYR	US\$	Y-o-y	Q-o-Q	M-o-M	Y-o-y	Q-o-Q	M-o-M	Y-o-y	Q-o-Q	M-o-M
Total	840.0	263.4	839.7	273.9	843.7	265.5	833.8	263.2	16.5	3.4	(0.03)	0.5	10.4	(0.7)	10.4	(0.7)	(1.2)
Government	505.0	158.4	504.1	164.4	502.1	158.0	499.0	157.5	19.8	4.1	(0.2)	(0.4)	12.0	(1.2)	12.0	(1.2)	(0.6)
Central Government Bonds	376.8	118.2	383.0	124.9	389.0	122.4	392.0	123.7	10.9	0.2	1.6	1.6	13.0	4.0	13.0	4.0	0.8
Central Bank Bills	127.7	40.0	120.6	39.3	112.6	35.4	106.7	33.7	58.0	17.8	(5.6)	(6.6)	9.3	(16.4)	9.3	(16.4)	(5.2)
Others	0.5	0.1	0.5	0.2	0.5	0.1	0.2	0.1	(52.1)	-	-	-	(75.0)	(47.8)	(75.0)	(47.8)	(47.8)
Corporate	335.0	105.0	335.6	109.5	341.6	107.5	334.8	105.7	11.8	2.3	0.2	1.8	8.1	(0.05)	8.1	(0.05)	(2.0)

- = not applicable, 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 LP end-of-period LCY-US\$ rate is used.
 3. Growth rates are calculated from LCY base and do not include currency effects.
 4. "Others" refers 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, Fully Automated System for Issuing/Tendering (FAST); and Bloomberg LP.

Outstanding LCY corporate bonds rose 8.1% y-o-y as of end-2011. However, on a q-o-q basis, total LCY corporate bonds outstanding were unchanged in 4Q11. LCY corporate bonds outstanding have been steadily increasing since 2005, largely driven by the surge in *sukuk* (Islamic bonds). At the end of 2011, LCY corporate *sukuk* outstanding stood at MYR206.1 billion, more than double the level from 2006 and more than 5 times the amount in 2001. On the other hand, outstanding conventional LCY corporate bonds were unchanged in 2011 (Figure 2).

Despite the drop in the stock of more traditional Islamic bonds issued by corporations (IBONDS) and Islamic corporate paper, Islamic-based LCY corporate bonds outstanding were up 14.1% y-o-y at end-2011 due to an increase in Islamic Medium-Term Notes (IMTNs) outstanding, which surged 49.9% to MYR101.5 billion in 2010 and 29.0% to MYR130.8 billion in 2011 (Table 2). The large issuers of IMTNs in 2011 included water asset management company Pengurusan Air (MYR9.9 billion), Tenaga Nasional's special purpose vehicle Manjung Island Energy (MYR4.9 billion), and national infrastructure company Prasarana (MYR3.1 billion). State-owned GovCo Holdings and state electricity provider Sarawak Energy each sold MYR3.0 billion worth of IMTNs in 2011, while road toll operator Anih Bhd. issued MYR2.5 billion of IMTNs.

Figure 2: Outstanding LCY Corporate Bonds, 2001–2011 (MYR billion)



LCY = local currency.
Source: Bank Negara Malaysia.

Table 2: Outstanding Islamic Corporate LCY Bonds, 2001-2011 (MYR billion)

Year	IABS/ ABS-IMTN	IBONDS	ICP	IMTN
2001	–	18.33	4.48	1.12
2002	–	33.29	4.46	1.75
2003	–	46.11	4.69	2.57
2004	0.99	52.09	6.21	5.43
2005	0.60	55.09	3.62	9.97
2006	3.25	62.88	4.49	16.75
2007	3.21	65.05	5.89	26.96
2008	5.55	70.99	6.46	55.07
2009	6.17	71.95	5.89	67.67
2010	5.12	68.79	5.28	101.45
2011	5.10	67.05	3.18	130.82

– = data not available, ABS-IMTN = asset-backed securities-Islamic medium-term notes, IABS = Islamic asset-backed securities, IBONDS = Islamic bonds, ICP = Islamic corporate paper, IMTN = Islamic medium-term notes.

Source: Bank Negara Malaysia.

Issuance of LCY corporate bonds fell 9.2% y-o-y to MYR23.2 billion in 4Q11, but total corporate LCY bond issuance increased 12.4% to MYR92.3 billion in full-year 2011.

As of end-2011, the top 30 issuers in Malaysia accounted for 56% of total LCY corporate bonds outstanding. Cagamas Bhd., Khazanah Nasional, and Binariang GSM remained the biggest issuers of LCY corporate bonds, with outstanding amounts of MYR20.0 billion, MYR13.2 billion, and MYR11.3 billion, respectively (**Table 3**).

Investor Profile

As of end-December, financial institutions were the largest holders of MGSs and GIIs, with 42% of total outstanding government bonds, followed by social security institutions, which held 24%. Insurance companies comprised 6% of the total (**Figure 3**). The share of government bonds held by foreign investors continued to rise to 26% at end-December, up from a 25% share at end-September and 22% at end-December 2010.

Domestic commercial and Islamic banks were the largest holders of LCY corporate bonds, with an estimated share of 45% at end-December 2010. Life insurance companies and the Employment

Provident Fund followed with shares of 30% and 13%, respectively (**Figure 4**).

Ratings Change

In January, Moody's affirmed Malaysia's A3 long-term LCY and foreign currency (FCY) rating and gave it a stable outlook (**Table 4**). According to Moody's, Malaysia's A3 sovereign rating was based on its economic resiliency, backed by a highly open, medium-sized economy, and a well-diversified external sector. While Malaysia's credit metrics have weakened due to the global financial crisis, the stable outlook reflects prospects for the effective implementation of countercyclical fiscal policy and gradual reforms to help cushion the impact of external shocks.

Policy, Institutional, and Regulatory Developments

BNM Announces a Renminbi Settlement Service

BNM announced that Renminbi Settlement Services (RSS) were to be included in its Real-Time Electronic Transfer of Funds and Settlement System (RENTAS) beginning 21 March. Bank of China (Malaysia) Bhd. has been appointed as the onshore settlement institution for RSS, which will provide greater efficiency and competitiveness in trade settlement, facilitate bilateral trade between Malaysia and the People's Republic of China (PRC), and provide a natural hedge against the fluctuations and volatility of other currencies while eliminating settlement risk for renminbi transactions.

HKMA, BNM, and Euroclear Unveil Pilot Program for Cross-Border Bond Transactions

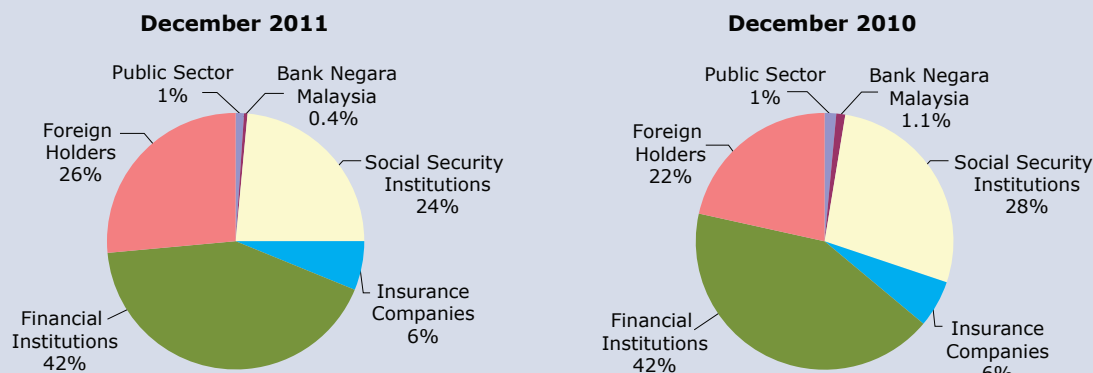
The Hong Kong Monetary Authority (HKMA), BNM, and Euroclear Bank announced the launch of a pilot platform in March. The platform, which became operational on 30 March, allows investors in Hong Kong, China and Malaysia to buy and hold foreign debt securities, and settle cross-border transactions on a delivery-

Table 3: Top 30 Issuers of LCY Corporate Bonds in Malaysia (as of end-December 2011)

Issuers	Outstanding Amount (MYR billion)					State- Owned	Privately- Owned	Listed Company	Type of Industry
	BONDS	IBONDS	MTN	IMTN	TOTAL				
1. Cagamas			9.77	10.22	19.99	Yes	No	No	Finance
2. Khazanah		13.20			13.20	Yes	No	No	Quasi-Govt. and Other
3. Binariang GSM		3.02		8.28	11.30	No	Yes	No	Transport, Storage, and Comm.
4. Pengurusan Air Bhd.				11.08	11.08	Yes	No	No	Energy, Gas, and Water
5. Maybank	9.10	1.50			10.60	No	Yes	Yes	Finance
6. Project Lebuhraya		5.62		3.68	9.30	No	Yes	Yes	Transport, Storage, and Comm.
7. Prasarana	2.91	2.00		4.00	8.91	Yes	No	No	Finance
8. Malakoff Corp.		1.70		5.60	7.30	No	Yes	No	Finance
9. CIMB Bank	7.00				7.00	No	Yes	No	Finance
10. Public Bank	1.20		4.87		6.07	No	Yes	Yes	Finance
11. KL International Airport	1.60	4.26			5.86	Yes	No	No	Transport, Storage, and Comm.
12. Rantau Abang Capital Bhd.				5.80	5.80	No	Yes	No	Quasi-Govt. and Other
13. Senai Desaru Expressway Bhd.				5.58	5.58	No	Yes	No	Construction
14. 1Malaysia Development Bhd.				5.00	5.00	Yes	No	No	Finance
15. AM Bank	0.49		4.48		4.96	No	Yes	Yes	Finance
16. Manjung Island Energy Bhd.				4.85	4.85	Yes	No	No	Energy, Gas, and Water
17. Jimah Energy Ventures				4.43	4.43	No	Yes	No	Energy, Gas, and Water,
18. Putrajaya Holdings		0.57		3.78	4.35	Yes	No	No	Finance
19. Celcom Transmission				4.20	4.20	No	Yes	No	Transport, Storage, and Comm.
20. Bank Pembangunan Malaysia	0.90		2.40	0.90	4.20	Yes	No	No	Finance
21. RHB Bank	0.60		3.25		3.85	No	Yes	No	Finance
22. Tanjung Bin				3.73	3.73	No	Yes	No	Energy, Gas, and Water
23. Danga Capital				3.60	3.60	Yes	No	No	Finance
24. YTL Power International			3.53		3.53	No	Yes	Yes	Energy, Gas, and Water
25. Cepak Mentari	3.50				3.50	No	Yes	Yes	Finance
26. Hong Leong Bank	2.20		1.16		3.36	No	Yes	Yes	Finance
27. Anih Bhd.	0.62			2.50	3.12	No	Yes	No	Finance
28. GOVCO Holdings				3.00	3.00	Yes	No	No	Quasi-Govt. and Other
29. Sarawak Energy				3.00	3.00	Yes	No	Yes	Energy, Gas, and Water
30. CIMB Group	2.13		0.50	0.35	2.98	No	Yes	Yes	Finance
Total Top 30 LCY Corporate Issuers	32.25	31.87	29.96	93.57	187.65				
Total LCY Corporate Bonds	59.06	67.05	56.41	130.82	334.81				
Top 30 as % of Total LCY Corporate Bonds	54.6%	47.5%	53.1%	71.5%	56.0%				

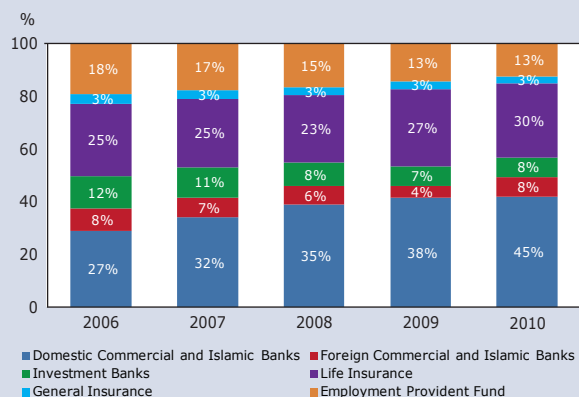
IBONDS = Islamic bonds, IMTN = Islamic medium-term notes, LCY = local currency, MTN = medium-term notes.
Source: Bank Negara Malaysia Fully Automated System for Issuing/Tendering (FAST).

Figure 3: LCY Government Bonds Investor Profile



LCY = local currency.
Source: Bank Negara Malaysia.

Figure 4: Malaysian LCY Corporate Bonds Investor Profile, 2006–2010



LCY = local currency.
Source: Bank Negara Malaysia.

Table 4: Selected Sovereign Ratings and Outlook for Malaysia

	Moody's	S&P	Fitch	R&I
Sovereign FCY LT Ratings	A3	A-	A-	A
Outlook	Stable	Stable	Stable	Stable

FCY = foreign currency, LT = long term.
Source: Rating agencies.

database maintained by Euroclear Bank. The new infrastructure is expected to strengthen cross-border issuance of local bonds in Hong Kong, China and Malaysia, and the rollout of the platform will provide investors and market intermediaries with efficient and cost effective cross-border access to the Hong Kong, China and Malaysian bond markets.

BNM and MAS Sign MOU to Enhance Domestic Liquidity

In January, BNM and the Monetary Authority of Singapore (MAS) signed a memorandum of understanding (MOU) to strengthen their cooperation in carrying out domestic liquidity management and enhance the liquidity of financial institutions in both countries. The cross-border collateral agreement allows eligible financial institutions in Singapore to pledge ringgit or MYR-denominated government and central bank securities to obtain Singapore dollar liquidity

versus-payment (DVP) basis. According to BNM and HKMA's joint press release, the platform is intended to facilitate the harmonization of market practices and standardization of the issuance and settlement of debt securities in order to deepen Asian bond market liquidity, attract investment, and increase operational efficiency. The pilot platform will optimize existing system links between HKMA's Central Moneymarkets Units (CMUs), BNM's RENTAS, and Euroclear Bank, as well as strengthen the connections between local central securities depositories and foreign current real-time gross settlement systems. It will also contain a comprehensive Asian debt securities

from MAS. Likewise, eligible financial institutions in Malaysia may pledge Singapore dollars or SGD-denominated government securities to obtain ringgit liquidity from BNM.

BNM Issues New Liberalization Measures

In February, BNM issued new liberalization measures to enhance competitiveness and develop domestic financial markets. The new measures (i) permit licensed onshore banks to trade one FCY against another with a resident, (ii) allow licensed onshore banks to offer MYR-denominated interest rate derivatives to a non-bank non-resident; and (iii) permit residents to convert a MYR- or FCY-denominated debt obligation into a debt obligation of another FCY.

These new measures are designed to increase liquidity, depth, and participation in domestic financial markets.

PBOC and BNM Enter Into Currency Swap Agreement

The People's Bank of China (PBOC) and BNM signed a currency swap agreement in February to exchange CNY180 billion–MYR90 billion over a period of 3 years. The swap value was increased to CNY180 billion–MYR90 billion from CNY80 billion–MYR40 billion, which had previously been agreed to in February 2009. The PBOC said that the swap agreement will facilitate bilateral trade between the People's Republic of China and Malaysia, and maintain regional financial stability.