

Malaysia—Update

Yield Movements

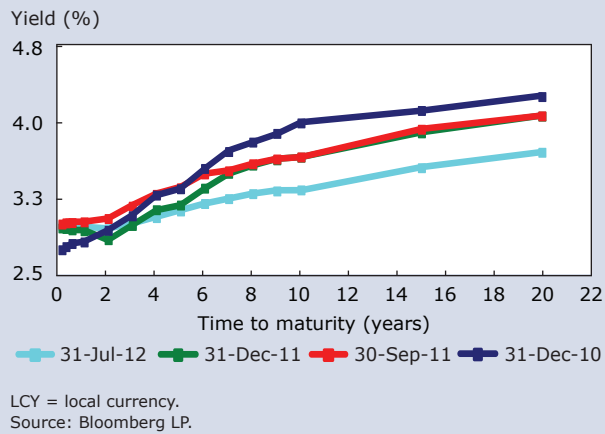
The yield curve for Malaysian local currency (LCY) government bonds flattened in the first half of the year, as yields rose at the shorter-end and fell at the belly and longer-end of the curve (**Figure 1**). Moderated by easing inflation amid concerns over the impact of the European debt crisis, yields at the shorter-end rose between 2 basis points (bps) and 11 bps between end-December 2011 and end-July 2012. On the other hand, yields for 4- and 5-year maturities fell 8 bps and 6 bps, respectively, while yields between the 6- and 20-year maturities posted double digit declines of 15 bps–35 bps. The yield spread between the 2- and 10-year maturities narrowed to 39 bps at end-July from 82 bps at end-December.

Bank Negara Malaysia (BNM) decided to keep its overnight policy rate steady at 3.0% at its Monetary Policy Committee meeting on 5 July. BNM has kept its rate at this level since May 2011. According to BNM, Malaysia's domestic consumption and investment activity remain resilient, while inflation is expected to remain moderate during the remainder of the year. BNM forecasts inflation to average 2%–3% for the full-year 2012.

Malaysia's consumer price inflation eased to 1.6% year-on-year (y-o-y) in June from 1.7% in May and 2.2% in April. Inflation during the first half of the year was 2.0% y-o-y, compared with 3.0% in the same period in 2011.

Malaysia's economy has remained resilient in 2012, supported largely by domestic demand. Growth in Malaysia's real gross domestic product (GDP) slowed to 4.7% y-o-y in 1Q12 from a revised 5.2% growth rate in 4Q11. Domestic demand growth remained firm at 9.6% y-o-y in 1Q12, supported by an increase in private consumption of 7.4%, which was up slightly from 7.3% growth in 4Q11. Meanwhile, public consumption grew 5.9% y-o-y in 1Q12, after registering 22.9% growth in 4Q11. Growth in gross fixed capital formation accelerated

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



to 16.1% y-o-y in 1Q12 versus 8.4% in the previous quarter.

On the supply side, the agriculture and manufacturing sectors posted lower growth rates of 2.1% and 4.2% y-o-y, respectively, in 1Q12, compared with growth of 6.9% and 5.2% in the previous quarter. The services sector grew 5.0% in 1Q12, compared with 6.6% in 4Q11. The mining sector grew 0.3% in 1Q12 in a reversal of the 3.8% decline in 4Q11, and the construction sector posted robust 15.5% growth following an expansion of 7.5% in the previous quarter.

Size and Composition

Malaysia's bond market continues to post double digit growth rates, with total LCY bonds outstanding rising 15.0% y-o-y to MYR934.2 billion (US\$294.0 billion) at end-June after posting 18.7% growth at end-March (**Table 1**). LCY government and corporate bonds both posted strong growth at 15.3% and 14.6% y-o-y, respectively, in 2Q12. On a quarter-on-quarter (q-o-q) basis, total LCY bonds outstanding grew 9.1% in 1Q12 and 2.3% in 2Q12.

Growth in LCY government bonds eased slightly to 15.3% y-o-y in 2Q12 after posting a 20.0%

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

	Amount (billion)						Growth Rate (%)										
	Mar-12		Apr-12		May-12		Jun-12		Mar-12		Apr-12		May-12		Jun-12		
	MYR	US\$	MYR	US\$	MYR	US\$	MYR	US\$	Y-o-y	q-o-q	Y-o-y	q-o-q	Y-o-y	q-o-q	Y-o-y	q-o-q	
Total	913	298	916	302	929	293	934	294	18.7	9.1	0.2	1.5	15.0	2.3	0.6		
Government	550	179	553	183	565	178	559	176	20.0	9.6	0.5	2.1	15.3	1.6	(1.0)		
Central Government Bonds and Bills	408	133	413	136	420	132	417	131	13.5	6.0	1.2	1.8	10.9	2.3	(0.7)		
Central Bank Bills	142	46	140	46	145	46	142	45	44.4	21.5	(1.5)	3.1	31.2	(0.3)	(1.7)		
Corporate	363	119	363	120	364	115	375	118	16.9	8.5	(0.2)	0.4	14.6	3.2	3.0		

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. All government bonds, previously under the category "Others," have matured as of end-February 2012. "Others" refers to Khazanah Bonds issued by Khazanah Nasional Bhd. and Cagamas Bonds and Notes, Bithaman Aji Islamic Securities, Sanadat ABBA Cagamas, and Sanadat Mudharabah Cagamas issued by Cagamas Bhd.

Source: Bank Negara Malaysia Fully Automated System for Issuing/Tendering (FAST) and Bloomberg LP.

increase in 1Q12. Total LCY government bonds outstanding stood at MYR559 billion at end-June. Central government bills and bonds rose 10.9% y-o-y at end-June, slightly lower than the 13.5% growth recorded at end-March. Meanwhile, outstanding central bank bill growth increased 31.2% y-o-y in 2Q12 after surging 44.4% in 1Q12. On a q-o-q basis, total LCY government bonds outstanding rose 1.6% in 2Q12.

Total LCY government bond issuance increased 8.4% during the first half of 2012 to reach MYR235 billion, up from MYR216.7 billion in the same period last year. Issuance of government bonds—Malaysian Government Securities (MGSs) and Government Investment Issues (GIIs)—rose 1.0% and 1.9% y-o-y in 1Q12 and 2Q12, respectively. Meanwhile, issuance of central bank bills rose 29.0% y-o-y in 1Q12, but fell 8.5% y-o-y in 2Q12.

Outstanding LCY corporate bonds rose 14.6% y-o-y at end-March and 17.4% y-o-y at end-June. On a q-o-q basis, total LCY corporate bonds outstanding rose 8.5% and 3.2% in 1Q12 and 2Q12, respectively. The first half of 2012 saw a surge in issuance of corporate bonds, particularly *sukuk* (Islamic bonds). Issuance of Islamic medium-term notes (IMTNs) reached MYR50.6 billion during the first 6 months of 2012, up from the MYR40.4 billion of IMTN issuance in all of 2011. Issuance of IMTNs has been rapidly increasing since 2005 (Table 2).

Among the notable *sukuk* issues during the first half of 2012 was toll expressway operator Projek Lebuhraya Utara Selatan Bhd.'s (PLUS) MYR30.6 billion worth of IMTNs, the world's largest *sukuk* issuance to date (Table 3). In addition, Sarawak Energy raised a total of MYR2.5 billion from the sale of 10- and 15-year *sukuk* in recent months, telecommunications company Maxis Bhd. sold MYR2.5 billion worth of 10-year *sukuk* in February, and electricity producer Tanjung Bin Energy Bhd. raised MYR3.3 billion from the multi-tranche sale of *sukuk* in March. More recently, Encorp Systembilt raised MYR1.6 billion from the sale of multi-tranche *sukuk* in May.

Table 2: Issuance of Corporate LCY Bonds, 2005–1H12
(MYR billion)

Year	BONDS	IBONDS	MTNs	IMTNs
2005	1.88	7.04	2.18	4.81
2006	8.16	6.80	4.56	12.12
2007	5.60	13.13	11.70	29.24
2008	18.57	9.40	11.57	13.98
2009	9.65	5.96	16.58	26.33
2010	5.25	3.67	15.24	26.47
2011	9.99	4.67	14.07	40.43
1H12	4.33	3.43	7.39	50.57

BONDS = conventional corporate bonds, IBONDS = Islamic bonds, IMTNs = Islamic medium-term notes, MTNs = medium-term notes.
Source: Bank Negara Malaysia.

Malaysian Airlines sold an initial tranche—worth MYR1 billion—of its perpetual junior *sukuk*, the world's first perpetual *sukuk*, to Kumpulan Wang Persaraan Retirement Fund Inc.

Several state-owned companies also issued *sukuk* during the first 6 months of the year. In April, construction company Pembinaan BLT, which is owned by the Ministry of Finance, issued MYR1.4 billion in a multi-tranche sale. The *sukuk*, issued through a special purpose vehicle, Aman Sukuk Bhd., are part of the construction company's MYR10 billion IMTN Programme under the *musharakah* (joint venture) concept. Johor Corp. raised MYR3 billion from the sale of IMTNs issued under the *wakalah billsthitmar* (investment through agent) principle. These *sukuk* are irrevocable and unconditionally guaranteed by the Malaysian government. Finally, Perbadanan Tabung Pendidikan Tinggi Nasional (Malaysia's National Higher Education Corporation) issued MYR2.5 billion worth of 10-year *sukuk* under the principle of *murahaba* (cost-plus financing).

Meanwhile, a number of conventional bonds were issued by banks and financial institutions in the first half of the year. Malayan Bank (Maybank) raised MYR2.1 billion from the issuance of 12-year subordinated debt, while Hong Leong Bank raised MYR1.5 billion from the sale of 12-year senior subordinated notes. Genting Capital raised

Table 3: Notable Corporate Issues in 1H12

Corporate Issuer	Instrument	Amount (MYR billion)
Projek Lebuhraya Utara Selatan (PLUS) Bhd.	IMTNs	30.60
Tanjung Bin Energy	IMTNs	3.29
Johor Corp	IMTNs	3.00
Sarawak Energy	IMTNs	2.50
Perbadanan Tabung Pendidikan Tinggi Nasional (PTPTN)	IMTNs	2.50
Maxis Bhd.	IMTNs	2.45
Maybank	BONDS	2.10
Genting Capital	MTNs	2.00
Encorp Systembilt	IBONDS	1.58
Hong Leong Bank	BONDS	1.50
Pembinaan BLT (Aman Sukuk)	IMTNs	1.35
Malaysian Airlines	IBONDS	1.00

BONDS = conventional corporate bonds, IBONDS = Islamic bonds, IMTNs = Islamic medium-term notes, MTNs = medium-term notes.
Source: Bank Negara Malaysia.

MYR2 billion from the sale of 10- and 5-year medium-term notes (MTNs). The issue is covered by an irrevocable and fully unconditional guarantee of the parent company.

As of end-June, the top 30 issuers in Malaysia accounted for 56.9% of total LCY corporate bonds outstanding. With the issuance of its MYR30.6 billion multi-tranche *sukuk*, PLUS became the largest issuer of LCY corporate bonds, followed by Cagamas Bhd., Khazanah Nasional, and Binariang GSM, with outstanding amounts of MYR19.2 billion, MYR13.2 billion, and MYR11.3 billion, respectively (**Table 4**).

Investor Profile

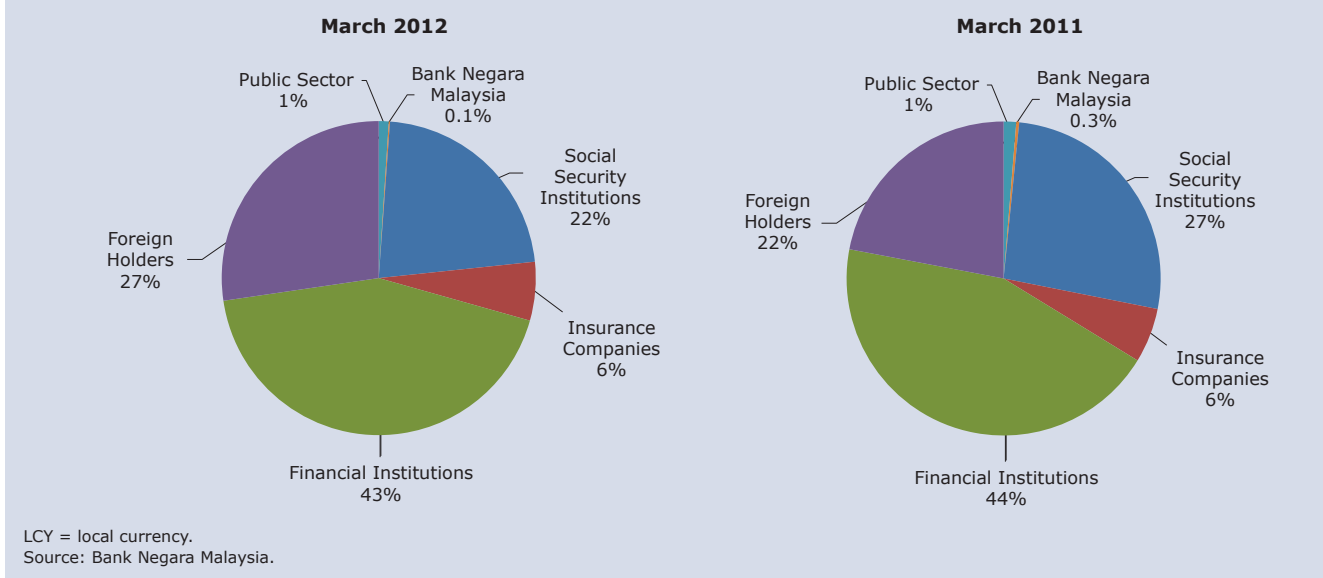
As of end-March, financial institutions were the largest holders of MGSs and GIIs, with 43% of total outstanding government bonds, followed by foreign investors and social security institutions, which held 27 and 22%, respectively (**Figure 2**). Insurance companies comprised 6% of the total. The share of government bonds held by foreign investors continued its gradual rise to 27% at end-March, up from 26% at end-December 2011 and 25% at end-September 2011.

Table 4: Top 30 Issuers of LCY Corporate Bonds in Malaysia (as of end-June 2012)

Issuers	Outstanding Amount (MYR billion)					State- Owned	Privately- Owned	Listed Company	Type of Industry
	BONDS	IBONDS	MTNs	IMTNs	TOTAL				
1. Project Lebuhraya				30.60	30.60	No	Yes	Yes	Transport, Storage, and Comm.
2. Cagamas			9.52	9.65	19.17	Yes	No	No	Finance
3. Khazanah		13.20			13.20	Yes	No	No	Quasi-Govt. and Other
4. Binariang GSM		3.02		8.28	11.30	No	Yes	No	Transport, Storage, and Comm.
5. Maybank	9.70	1.50			11.20	No	Yes	Yes	Finance
6. Pengurusan Air Bhd.				11.08	11.08	Yes	No	No	Energy, Gas, and Water
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. Senai Desaru Expressway Bhd.				5.58	5.58	No	Yes	No	Construction
12. Sarawak Energy				5.50	5.50	Yes	No	Yes	Energy, Gas, and Water
13. KL International Airport	1.60	3.76			5.36	Yes	No	No	Transport, Storage, and Comm.
14. Johor Corp		2.15		3.00	5.15	Yes	No	No	Quasi-Govt. and Other
15. 1Malaysia Development Bhd.				5.00	5.00	Yes	No	No	Finance
16. Hong Leong Bank	3.70		1.16		4.86	No	Yes	Yes	Finance
17. Manjung Island Energy Bhd.				4.85	4.85	No	Yes	No	Energy, Gas, and Water
18. AM Bank	0.49		4.28		4.77	No	Yes	Yes	Finance
19. RHB Bank	0.60		4.00		4.60	No	Yes	No	Finance
20. Putrajaya Holdings		0.50		3.88	4.38	No	Yes	No	Finance
21. Jimah Energy Ventures				4.32	4.32	No	Yes	No	Energy, Gas, and Water
22. Celcom Transmission				4.20	4.20	No	Yes	No	Transport, Storage, and Comm.
23. Bank Pembangunan Malaysia	0.90		2.40	0.90	4.20	Yes	No	No	Finance
24. Rantau Abang Capital Bhd.				3.80	3.80	No	Yes	No	Quasi-Govt. and Other
25. Aman Sukuk Bhd.				3.62	3.62	Yes	No	No	Construction
26. Danga Capital				3.60	3.60	Yes	No	No	Finance
27. YTL Power International			3.54		3.54	No	Yes	Yes	Energy, Gas, and Water
28. Tanjung Bin				3.53	3.53	No	Yes	No	Energy, Gas, and Water
29. Cepak Mentari	3.50				3.50	No	Yes	Yes	Finance
30. Tanjung Bin Energy				3.29	3.29	No	Yes	No	Energy, Gas, and Water
Total Top 30 LCY Corporate Issuers	31.60	27.82	29.77	124.26	213.46				
Total LCY Corporate Bonds	61.52	60.58	59.75	172.10	375.21				
Top 30 as % of Total LCY Corporate Bonds	51.4%	45.9%	49.8%	72.2%	56.9%				

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

Figure 2: Malaysian LCY Government Bonds Investor Profile



Rating Changes

In August, international credit rating agency Standard & Poor’s (S&P) affirmed Malaysia’s A-/A-2 foreign currency (FCY) credit rating and A/A-1 LCY credit rating, citing the country’s strong external liquidity position, competitive middle-income economy, and high savings rate (**Table 5**).

Fitch Ratings also affirmed Malaysia’s long-term FCY and LCY issuer default ratings at A- and A, respectively, with a stable outlook for both ratings. According to Fitch, the affirmation of the ratings and stable outlooks reflect Malaysia’s macroeconomic stability and strong net external creditor position. However, Fitch also cited the deterioration of public debt ratios and structural weaknesses in Malaysia’s public finances as weighing on its credit profile.

Table 5: 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.

Policy, Institutional, and Regulatory Developments

BNM Announces Renminbi Settlement Services

BNM announced that Renminbi Settlement Services (RSS) would be included in its Real-Time Electronic Transfer of Funds and Settlement System (RENTAS), effective 21 March. Bank of China (Malaysia) Bhd. has been appointed as the onshore settlement institution for the RSS, which is expected to 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 to eliminate settlement risk for renminbi transactions.

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

BNM, Euroclear Bank, and the Hong Kong Monetary Authority (HKMA) 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-versus-payment 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 Unit (CMU), BNM's RENTAS, and Euroclear, as well as strengthen the connections between local central securities depositories and FCY real-time gross settlement systems. It will also contain a comprehensive Asian debt securities database maintained by Euroclear. 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.