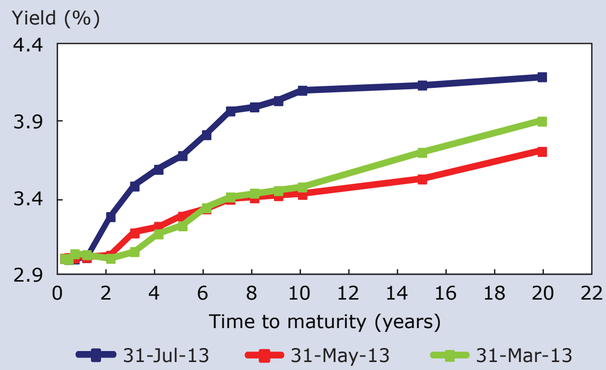
Malaysia

Yield Movements

Malaysia's local currency (LCY) government bond yield curve slightly flattened between end-March and end-May, as yields dropped across the length of the curve, with the exception of tenors between 2 years and 5 years. Yields of longer-dated tenors (maturities more than 6 years) slumped the most, falling between 17 basis points (bps) and 20 bps.

By end-July, however, the yield curve steepened between the shorter-end, where yields continued to slide, and the belly through the longer-end, where yields continued their upward trend. Yields for tenors of 2 years and longer rallied—by as much as 68 bps for 10-year Malaysian Government Securities (MGSs). In contrast to the rest of the curve, yields fell for short-term instruments with maturities of 1 year or less, with decreases ranging from 0.1 bps for the 1-year tenor to 1.1 bps for the 3-month tenor. The yield spread between 2- and 10-year tenors widened to 43 bps at end-July from 1 bp at end-June **(Figure 1)**.

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



LCY = local currency.
Source: Bloomberg LP.

Yields surged on concerns that the United States (US) Federal Reserve might taper its asset purchase program and that inflation might be accelerating. Consumer price inflation in Malaysia rose to 2.0% year-on-year (y-o-y) in July, following 1.8% in both June and May. The increase reflected higher food and housing costs, which inched up 3.9% and 1.9% y-o-y. On a month-on-month (m-o-m) basis, Malaysia's inflation increased 0.2% in July.

In its Monetary Policy Committee meeting on 11 July, Bank Negara Malaysia (BNM) decided to keep its overnight policy rate unchanged at 3.0%. BNM has kept its benchmark rate at the same level since May 2011. The central bank expects private consumption to remain steady, underpinned by income growth and stable labor market conditions, although sustained weakness in the external sector may affect the overall growth momentum. BNM also expects capital spending in domestic-oriented industries and the ongoing implementation of infrastructure projects to support investment activity.

Malaysia's economic growth has slowed but still remains robust in 2013, supported by buoyant domestic demand amid weakness in the external sector. Real gross domestic product (GDP) growth picked up slightly in 2Q13, rising to 4.3% y-o-y from 4.1% in 1Q13. Government consumption, which rose 11.1% y-o-y in 2Q13, cushioned the moderation in private consumption, which slowed to 7.2% in 2Q13 from 7.5% in the previous quarter. Total exports of goods and services, on the other hand, fell 5.2% y-o-y in 2Q13. On a quarter-on-quarter (q-o-q) and seasonally adjusted basis, the economy recorded growth of 1.4% in 2Q13. With continued weaknesses in the external economy, BNM has revised downward its 2013 GDP growth forecast to 4.5%–5.0% from 5.0%–6.0%.

Size and Composition

Total LCY bonds outstanding in Malaysia rose 6.4% y-o-y to MYR993.5 billion (US$314.4 billion) at end-June; LCY government bonds increased 5.1% and LCY corporate bonds grew 8.2%. On a quarter-on-quarter (q-o-q) basis, however, total

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

	Outstanding Amount (billion)						**Growth Rate** (%)			
	2Q12		**1Q13**		**2Q13**		**2Q12**		**2Q13**	
	MYR	**US$**	**MYR**	**US$**	**MYR**	**US$**	**q-o-q**	**y-o-y**	**q-o-q**	**y-o-y**
Total	934	294	996	322	994	314	2.3	15.0	(0.2)	6.4
Government	559	176	589	190	588	186	1.6	15.3	(0.2)	5.1
Central Government Bonds and Bills	417	131	446	144	459	145	2.3	10.9	2.8	10.0
Central Bank Bills	142	45	136	44	123	39	(0.3)	31.0	(10.1)	(13.7)
Sukuk Perumahan Kerajaan	0	0	6	2	6	2	–	–	0.0	–
Corporate	375	118	407	132	406	128	3.2	14.6	(0.3)	8.2

( ) = negative, – = not applicable, 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.
Sources: Bank Negara Malaysia Fully Automated System for Issuing/Tendering (FAST) and Bloomberg LP.

LCY bonds outstanding declined 0.2% in 2Q13 **(Table 1)**.

Government Bonds. LCY government bonds outstanding stood at MYR587.5 billion at end-June, rising 5.1% y-o-y. About 63% of total government bonds outstanding were conventional bonds, while 37% were *sukuk* (Islamic bonds). Growth in the government bond market was driven by central government bonds, specifically Government Investment Issues (GIIs) and *Sukuk Perumahan Kerajaan* (SPK). Central government bonds and bills, which accounted for 77.3% of the total government bonds, grew 10.1% y-o-y to MYR458.8 billion. Outstanding SPK amounted to MYR6.2 billion. In contrast, total central bank bills outstanding slumped 13.7% y-o-y and 10.1% q-o-q due to a decline in monetary note issuance by BNM.

Government bond issuance fell 3.1% q-o-q to MYR101.1 billion in 2Q13, as issuance volumes declined for central government bills and central bank bills. On a y-o-y basis, the issuance of government bonds also saw negative growth of 0.2% due to a drop in central government bond issuance, particularly MGSs.

Corporate Bonds. Malaysia's LCY corporate bonds outstanding expanded 8.2% y-o-y to MYR406 billion (US$128.5 billion) at end-June, but edged slightly lower by 0.3% on a q-o-q basis. Some 67% of the total LCY corporate bonds were *sukuk*, while conventional bonds accounted for 33%. Medium-term notes (MTNs) accounted for 74.0% of total *sukuk* and 49.5% of total corporate bonds outstanding.

Corporate issuance declined in 2Q13, continuing a trend in place since 4Q12. Total LCY corporate bond issuance dropped to MYR20.6 billion, down 29.1% y-o-y and 29.3% q-o-q, due to a decline in *sukuk* issuance, particularly Islamic commercial paper and MTNs. Of the total issuance during the quarter, conventional bonds accounted for 58.3% of the total, while *sukuk* registered 41.7%.

Bond issuance from corporate entities was heavily concentrated among a handful of corporates, as the top 30 issuers accounted for 93.0% of the total issuance for the quarter. **Table 2** lists some notable corporate bonds issued during 2Q13.

The largest corporate issuer in 2Q13 was TNB Northern Energy (TNB NE), a wholly owned subsidiary of state-owned Tenaga Nasional. TNB NE sold MYR1.63 billion worth of *sukuk* consisting of 39 series with tenures ranging from 4 years to 23 years. The proceeds from the bond sale will be used to finance construction, delivery,

Table 2: Notable LCY Corporate Bond Issuance in 2Q13

Corporate Issuers	Coupon Rate (%)	Issued Amount (MYR million)	Corporate Issuers	Coupon Rate (%)	Issued Amount (MYR million)
TNB Northern Energy			17-year *sukuk*	4.42	50
4-year *sukuk*	3.55	30	17.5-year *sukuk*	4.46	50
4.5-year *sukuk*	3.59	30	18-year *sukuk*	4.48	50
5-year *sukuk*	3.63	30	18.5-year *sukuk*	4.52	55
5.5-year *sukuk*	3.67	30	19-year *sukuk*	4.55	50
6-year *sukuk*	3.71	30	19.5-year *sukuk*	4.59	55
6.5-year *sukuk*	3.75	30	20-year *sukuk*	4.62	55
7-year *sukuk*	3.79	30	20.5-year *sukuk*	4.66	55
7.5-year *sukuk*	3.83	35	21-year *sukuk*	4.69	50
8-year *sukuk*	3.87	30	21.5-year *sukuk*	4.73	55
8.5-year *sukuk*	3.91	30	22-year *sukuk*	4.76	50
9-year *sukuk*	3.95	30	22.5-year *sukuk*	4.80	55
9.5-year *sukuk*	3.99	35	23-year *sukuk*	4.83	55
10-year *sukuk*	4.03	35	Cagamas		
10.5-year *sukuk*	4.06	35	3-month Islamic commercial paper	3.21	500
11-year *sukuk*	4.08	35	1-year Islamic MTNs	3.23	50
11.5-year *sukuk*	4.11	35	1-year medium term notes	3.30	70
12-year *sukuk*	4.13	35	2-year Islamic MTNs	3.40	80
12.5-year *sukuk*	4.16	35	3-year Islamic MTNs	3.40	450
13-year *sukuk*	4.18	35	Perbadanan Tabung Pendidikan Tinggi Nasional		
13.5-year *sukuk*	4.21	45	10-year Islamic MTNs	3.80	100
14-year *sukuk*	4.23	40	15-year Islamic MTNs	4.19	100
14.5-year *sukuk*	4.26	45	15-year Islamic MTNs	4.19	500
15-year *sukuk*	4.28	45	Telekom Malaysia		
15.5-year *sukuk*	4.32	50	10-year Islamic MTNs	3.93	250
16-year *sukuk*	4.35	50	10-year Islamic MTNs	3.95	400
16.5-year *sukuk*	4.39	50			

LCY = local currency, MTNs = medium-term notes.
Source: Bank Negara Malaysia Bond Info Hub.

and working capital requirements for a 1,071.43 megawatt gas-fired power plant in Prai, Penang. The bond was rated AAAIS by Malaysian Rating Corp Berhad.

Other notable issuances in 2Q13 came from state-owned companies such as national mortgage corporation Cagamas, which issued MYR1.15 billion worth of conventional bonds and *sukuk*, and Perbadanan Tabung Pendidikan Tinggi Nasional (National Higher Education Fund Corporation), which raised a total of MYR700 million from IMTNs carrying 10- and 15-year maturities. Meanwhile, publicly-listed Telekom Malaysia also issued MYR650 million worth of AAA-rated 10-year *sukuk*.

Table 3 provides a breakdown of the top 30 LCY corporate bond issuers as of end-June. The amount of LCY bonds outstanding of the top 30 corporate bond issuers in Malaysia stood at MYR223.2 billion, representing 55.0% of total corporate bonds outstanding. Financial firms comprised 14 of the 30 largest corporate

Table 3: Top 30 Issuers of LCY Corporate Bonds in Malaysia

Issuers	Outstanding Amount		State-Owned	Listed Company	Type of Industry
	LCY Bonds (MYR billion)	LCY Bonds (US$ billion)			
1. Project Lebuhraya Usahasama.	30.60	9.68	No	Yes	Transport, Storage, and Communications
2. Cagamas	20.65	6.53	Yes	No	Finance
3. Khazanah	18.70	5.92	Yes	No	Quasi-Govt.
4. Pengurusan Air	11.28	3.57	Yes	No	Energy, Gas, and Water
5. Prasarana	9.91	3.14	Yes	No	Finance
6. Binariang GSM	9.89	3.13	No	No	Transport, Storage, and Communications
7. Maybank	9.70	3.07	No	Yes	Finance
8. CIMB Bank	7.00	2.21	No	No	Finance
9. Cagamas MBS	6.03	1.91	No	No	Finance
10. Senai Desaru Expressway	5.57	1.76	No	No	Construction
11. Sarawak Energy	5.50	1.74	Yes	No	Energy, Gas, and Water
12. Perbadanan Tabung Pendidikan Tinggi Nasional	5.40	1.71	Yes	No	Quasi-Govt.
13. Turus Pesawat	5.31	1.68	Yes	No	Quasi-Govt.
14. Malakoff Power	5.10	1.61	No	No	Finance
15. Public Bank	5.07	1.61	No	Yes	Finance
16. Aman Sukuk	5.03	1.59	Yes	No	Construction
17. Celcom Networks	5.00	1.58	No	No	Transport, Storage, and Communications
18. 1Malaysia Development	5.00	1.58	Yes	No	Finance
19. Hong Leong Bank	4.86	1.54	No	Yes	Finance
20. KL International Airport	4.86	1.54	Yes	No	Transport, Storage, and Communications
21. Manjung Island Energy	4.85	1.53	No	No	Energy, Gas, and Water
22. Putrajaya Holdings	4.76	1.51	No	No	Finance
23. AM Bank	4.71	1.49	No	No	Finance
24. RHB Bank	4.60	1.46	No	No	Finance
25. YTL Power International	4.32	1.37	No	Yes	Energy, Gas, and Water
26. Tanjung Bin Power	4.20	1.33	No	No	Energy, Gas, and Water
27. Jimah Energy Ventures	4.03	1.28	No	No	Energy, Gas, and Water
28. Danainfra Nasional	3.90	1.23	Yes	No	Finance
29. Rantau Abang Capital	3.80	1.20	No	No	Quasi-Govt.
30. Danga Capital	3.60	1.14	No	No	Finance
Total Top 30 LCY Corporate Issuers	**223.21**	**70.63**			
Total LCY Corporate Bonds	**406.04**	**128.48**			
Top 30 as % of Total LCY Corporate Bonds	**55.0%**	**55.0%**			

LCY = local currency.
Notes:
1. Data as of end-June 2013.
2. State-owned firms are defined as those in which the government has more than a 50% ownership stake.
Source: *AsianBondsOnline* calculations based on Bank Negara Malaysia Fully Automated System for Issuing/Tendering (FAST) data.

bond issuers, with bonds outstanding worth MYR94.9 billion.

Highway-operator Project Lebuhraya Usahasama. (PLUS) remained the largest issuer with outstanding bonds valued at MYR30.6 billion. Among the top 30 issuers, 19 were privately-owned companies, five of which were listed on Bursa Malaysia.

Investor Profile

Financial institutions remained the largest holder of MGSs and GIIs, accounting for 42.3% of total government debt outstanding at end-March **(Figure 2)**, which was down slightly from 43.3% in March 2012 and 44.1% in June 2012. In absolute terms, the holdings of financial institutions stood at MYR187 billion at end-March, up from MYR174.7 billion a year earlier.

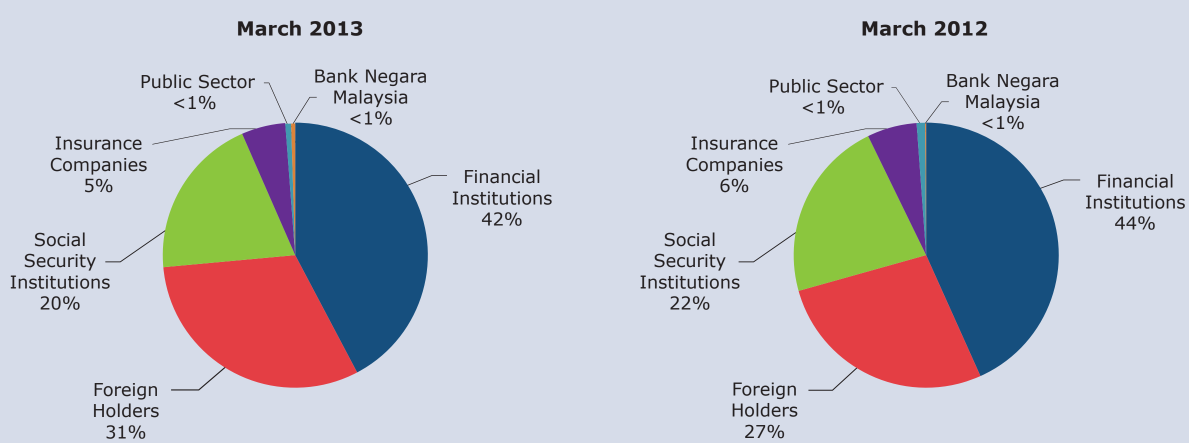
Foreign investors comprised the second-largest investor group with 31.2% of total government bonds outstanding. This number has steadily risen from 10% in March 2009 as a result of the appreciation of the ringgit versus the US dollar. Meanwhile, the holdings of social security institutions fell to 19.9% at end-March from 22.2% a year earlier due to a decrease in the Employees Provident Fund's holdings.

Domestic commercial and Islamic banks increased their already dominant share of the Malaysian corporate bond market at the end of 2012 to 48% from 44% at the end of 2011 **(Figure 3)**. Holdings of insurance companies remained at 30% of the total corporate bonds in 2012, while holdings of corporate bonds by the Employees Provident Fund fell to 10% from 13% of the total in 2011. Holdings of corporate bonds by insurance companies have more than doubled since 2006 **(Table 4)** and continued to rise in 2012 in nominal terms, but holdings of corporate bonds by Employees Provident Fund have risen much more slowly over the last 7 years and even declined in 2012.

Rating Changes

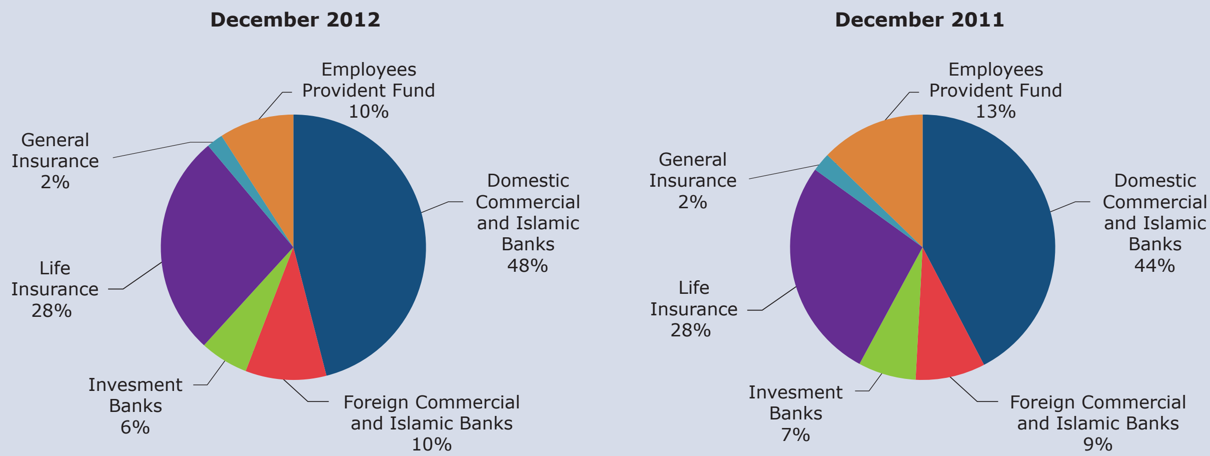
In July, Standard & Poor's Ratings Services (S&P) affirmed Malaysia's long-term foreign currency (FCY) and LCY ratings at A– and A, respectively. S&P also maintained its long-term rating outlook at stable on account of the country's strong external

Figure 2: LCY Government Bonds Investor Profile



LCY = local currency.
Source: Bank Negara Malaysia.

Figure 3: LCY Corporate Bonds Investor Profile



LCY = local currency.
Source: Bank Negara Malaysia.

Table 4: Corporate Bonds Held By Insurance Companies and the Employees Provident Fund in Malaysia (MYR billion)

	2006	2007	2008	2009	2010	2011	2012
Malaysia Total	**88.0**	**102.2**	**106.2**	**122.8**	**141.7**	**147.5**	**160.3**
Insurance	54.4	63.4	67.3	85.3	100.5	102.8	122.1
Employees Provident Fund	33.6	38.8	39.0	37.5	41.1	44.7	38.2
as % of Total Corporate Bonds	**46%**	**44%**	**40%**	**43%**	**46%**	**44%**	**40%**

Source: Bank Negara Malaysia and Employees Provident Fund.

position and monetary flexibility, and in spite of its weak fiscal performance. The rating agency expects government reform efforts to continue along with other economic reform policies.

In the same month, Fitch Ratings (Fitch) downgraded Malaysia's credit outlook to negative from stable, with the long-term FCY and LCY issuer default ratings affirmed at A– and A, respectively. Fitch cited Malaysia's public finances as its key rating weakness with worsening prospects for budgetary reform and fiscal consolidation. The rating agency believes that it will be difficult for the government to achieve its interim 3% federal budget deficit target in 2015 without additional consolidation measures.

In August, Moody's Investors Service (Moody's) maintained a stable outlook for Malaysia and an A3 rating for LCY and FCY government bonds based on its assessment of moderate economic resiliency that is supported by a highly open, medium-sized economy and a well-diversified external sector. Moody's said the high degree of government financial strength is underpinned by the country's strong external position and high savings rate compared with its peers. It added that Malaysia has strong and well-managed corporate and banking sectors, and that its state-owned enterprises were undergoing needed reform. Moody's noted, however, that Malaysia's economic growth has been relatively dependent on public sector expenditure.

Policy, Institutional, and Regulatory Developments

Malaysia Enacts Financial Services Act and Islamic Financial Services Act

Malaysia enacted a new single legislative framework for conventional and Islamic financial services effective 30 June. The Financial Services Act 2013 (FSA) and the Islamic Financial Services Act 2013 (IFSA) repealed and consolidated the provisions included in several previous laws: the Banking and Financial Institutions Act 1989, Islamic Banking Act 1983, Insurance Act 1996, Takaful Act 1984, Payment Systems Act 2003, and Exchange Control Act 1953.

The new legislation provides clearly defined regulatory objectives and establishes accountability for BNM in pursuing its principal objective of safeguarding financial stability. It sets forth transparent assessment criteria for authorizing institutions to engage in regulated financial transactions. The acts include provisions to regulate financial holding companies and non-regulated entities in order to take account of systemic risks that can emerge from the interaction between regulated and unregulated institutions, activities, and markets. The IFSA provides a comprehensive legal framework that is fully consistent with *sharia'h* (Islamic law) in all aspects of regulation and supervision, from licensing to the winding-up of an institution.

BNM Implements Measures to Mitigate Household Debt Risks

BNM implemented measures to limit risks stemming from rising household debt. The measures set limits for mortgages and personal loans—including a maximum tenure of 10 years for personal financing and 35 years for financing for residential and non-residential properties—and prohibit the offering of pre-approved personal financing products.