

Malaysia

Yield Movements

Between 1 March and 15 May, Malaysian local currency (LCY) government bond yields fell for most tenors, particularly at the short-end of the curve, amid market expectations that the United States (US) Federal Reserve would delay further increases in its policy rate (**Figure 1**). Yields for tenors between 1 month and 6 months fell between 13 basis points (bps) and 16 bps, and yields for tenors between 1 year and 5 years fell 4–22 bps. Yields for bonds with tenors of between 9 years and 20 years fell 2–16 bps. The 2-year versus 10-year spread rose from 73 bps to 90 bps.

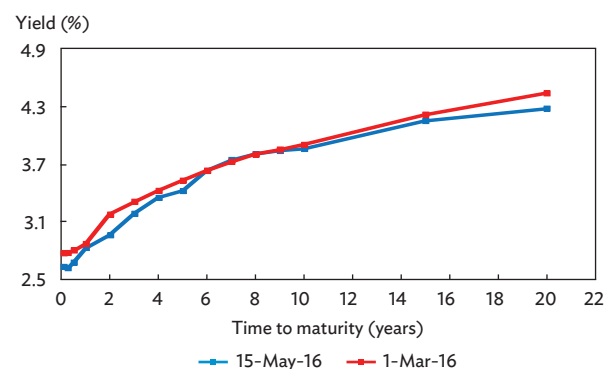
Declining yields were also reflective of renewed investor confidence in the Malaysian local bond market and the Malaysian ringgit. The rebound in oil prices since the start of the year provided support to the domestic bond market and the local currency. However, the fall in yields and the appreciation of the Malaysian ringgit were capped during the latter part of April amid reports of 1Malaysia Development Berhad's (1MDB) nonpayment of interest due to bondholders.

The Malaysian ringgit appreciated 6.1% year-to-date through 15 May, reaching a high of MYR3.87–USD1 on 20 April, after depreciating 22.8% in full-year 2015. Data from Bank Negara Malaysia (BNM) also showed a surge in foreign holdings of central government debt securities in the first 4 months of the year to MYR199 billion in April from MYR179 billion in January.

Inflation inched up in the first 2 months of the year to 4.2% year-on-year (y-o-y) in February, before easing to 2.6% y-o-y in March and further to 2.1% y-o-y in April. Benign inflation allowed BNM to maintain the overnight policy rate at 3.25% at its 19 May policy meeting. Inflation is projected to trend lower in 2016 due to low energy and commodity prices. The central bank also expects Malaysia's economy to grow 4.0%–4.5% y-o-y in 2016 and will continue to be supported by strong domestic demand.

Malaysia's gross domestic product growth slowed to 4.2% y-o-y in the first quarter (Q1) of 2016 from 4.5% y-o-y in the fourth quarter (Q4) of 2015. The

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



Source: Based on data from Bloomberg LP.

slower rate of expansion was due to weaker growth in gross fixed capital formation of 0.1% y-o-y in Q1 2016 compared with 2.7% y-o-y in the previous quarter. Exports also contracted 0.5% y-o-y in Q1 2016, while imports increased 1.3% y-o-y. Government spending and private final consumption expenditure both posted higher annual increases in Q1 2016 compared with the previous quarter. By sector, all industries posted annual increases except for agriculture, which contracted 3.8% y-o-y in Q1 2016 following growth of 1.5% y-o-y in Q4 2015.

Size and Composition

The Malaysian LCY bond market expanded 1.9% quarter-on-quarter (q-o-q) to MYR1,141 billion (USD293 billion) at the end of March, led by growth in the government bond sector (**Table 1**). On a y-o-y basis, the LCY bond market rose 6.3% in Q1 2016. Government bonds outstanding totalled MYR628 billion at the end of March, while corporate bonds summed to MYR512 billion. *Sukuk* (Islamic bonds) continued to comprise the majority of the LCY bond market, with a share of 54% of total bonds outstanding at the end of March.

Government Bonds. LCY government bonds outstanding rose 2.7% on both a q-o-q and y-o-y basis to close at MYR628 billion at the end of March. The rise was solely the result of an increase in the outstanding stock of central government bonds, particularly Malaysian

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

	Outstanding Amount (billion)						Growth Rate (%)			
	Q1 2015		Q4 2015		Q1 2016		Q1 2015		Q1 2016	
	MYR	USD	MYR	USD	MYR	USD	q-o-q	y-o-y	q-o-q	y-o-y
Total	1,073	290	1,119	261	1,141	293	(2.7)	2.1	1.9	6.3
Government	612	165	612	142	628	161	(5.4)	(0.3)	2.7	2.7
Central Government Bonds	531	143	559	130	579	148	2.2	5.7	3.5	9.0
of which: <i>Sukuk</i>	193	52	214	50	221	57	4.0	8.4	3.0	14.2
Central Bank Bills	57	15	25	6	22	6	(46.8)	(42.3)	(12.2)	(62.3)
of which: <i>Sukuk</i>	19	5	1	0.1	0	0	(54.4)	(52.1)	(100.0)	(100.0)
Sukuk Perumahan Kerajaan	24	7	28	7	28	7	19.6	89.1	0.0	16.4
Corporate	461	125	507	118	512	131	1.0	5.4	1.0	11.1
of which: <i>Sukuk</i>	328	89	361	84	366	94	1.6	10.4	1.4	11.5

(-) = negative, MYR = Malaysian ringgit, q-o-q = quarter-on-quarter, Q1 = first quarter, Q4 = fourth quarter, USD = United States dollar, y-o-y = year-on-year.

Notes:

1. Calculated using data from national sources.
2. Bloomberg LP end-of-period local currency-USD rate is used.
3. Growth rates are calculated from local currency base and do not include currency effects.
4. Sukuk Perumahan Kerajaan are Islamic bonds issued by the Government of Malaysia to refinance funding for housing loans to government employees and to extend new housing loans.

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

Government Securities and Government Investment Issues.

Total government bond issuance, however, fell 23.3% q-o-q to MYR29 billion in Q1 2016 from MYR37 billion in Q4 2015, as BNM did not issue any central bank bills in the most recent quarter. There was also less issuance of Malaysian Government Securities in Q1 2016 compared with the previous quarter. Issuance of Government Investment Issues and Treasury bills, on the other hand, was up in Q1 2016.

Corporate Bonds. Total outstanding LCY corporate bonds increased 1.0% q-o-q in Q1 2016 to MYR512 billion at the end of March. The ratio of corporate *sukuk* to total corporate bonds outstanding remained steady at 71%.

Table 2 provides a breakdown of the top 30 LCY corporate bond issuers in Malaysia, whose total LCY bonds outstanding stood at MYR281.5 billion at the end of March, representing 54.9% of the LCY corporate bond market. Financial firms, including banks, comprised 16 of the 30 largest corporate bond issuers, with bonds outstanding worth MYR154.7 billion. Highway operator Project Lebuhraya Usahasama remained the largest issuer with outstanding bonds valued at MYR30.6 billion.

Issuance of corporate bonds started the year at a moderate pace as total issuance fell to MYR34 billion

in Q1 2016 from MYR57 billion in Q4 2015. *Sukuk* accounted for 55.4% of total issuance, while conventional bonds registered a share of 44.6%. By type of instrument, Islamic medium-term notes had the highest share of total issuance at 34.9%, followed by conventional commercial paper with a share of 31.6%. **Table 3** lists notable corporate bond issuances in Q1 2016.

The largest corporate issuers in Q1 2016 were from government-owned entities in the financial, utilities, and transport sectors. Prasarana Malaysia Berhad, which owns the largest public transportation company in Malaysia, issued MYR3.05 billion worth of *sukuk* in five tranches with maturities ranging from 7 years to 25 years. Sime Darby, with major holdings in palm oil plantations, issued MYR2.2 billion worth of perpetual *sukuk* with a non-call option of 10 years and a profit rate of 5.65%. Pengurusan Air SPV, a water services company, issued *sukuk* comprising a MYR1 billion 7-year tranche and a MYR750 million 10-year tranche with coupon rates of 4.43% and 4.63%, respectively.

Foreign Currency Bonds. In April, the Government of Malaysia issued USD1.5 billion worth of dual-tranche US dollar *sukuk* via a special purpose vehicle, Malaysia *Sukuk* Global Berhad. The issue comprised a USD1 billion 10-year tranche and a USD500 million 30-year tranche. The 10-year and 30-year *sukuk* were priced at 3.18% and 4.08%, respectively.

Table 2: Top 30 Issuers of Local Currency Corporate Bonds in Malaysia

	Issuers	Outstanding Amount		State-Owned	Listed Company	Type of Industry
		LCY Bonds (MYR billion)	LCY Bonds (USD billion)			
1.	Project Lebuhraya Usahasama	30.6	7.8	No	No	Transport, Storage, and Communications
2.	Cagamas	26.1	6.7	Yes	No	Finance
3.	Danainfra Nasional	20.7	5.3	Yes	No	Finance
4.	Prasarana	20.6	5.3	Yes	No	Transport, Storage, and Communications
5.	Khazanah	20.0	5.1	Yes	No	Finance
6.	Maybank	14.9	3.8	No	Yes	Banking
7.	Pengurusan Air	14.2	3.7	Yes	No	Energy, Gas, and Water
8.	Perbadanan Tabung Pendidikan Tinggi Nasional	11.0	2.8	Yes	No	Finance
9.	CIMB Bank	9.1	2.3	No	No	Banking
10.	Jimah East Power	9.0	2.3	Yes	No	Energy, Gas, and Water
11.	Public Bank	8.6	2.2	No	No	Banking
12.	Sarawak Energy	8.5	2.2	Yes	No	Energy, Gas, and Water
13.	Aman Sukuk	6.3	1.6	Yes	No	Construction
14.	Rantau Abang Capital	6.0	1.5	Yes	No	Finance
15.	Danga Capital	5.5	1.4	Yes	No	Finance
16.	RHB Bank	5.4	1.4	No	No	Banking
17.	Turus Pesawat	5.3	1.4	Yes	No	Transport, Storage, and Communications
18.	BGSM Management	5.1	1.3	No	No	Transport, Storage, and Communications
19.	1Malaysia Development	5.0	1.3	Yes	No	Finance
20.	Manjung Island Energy	4.9	1.2	No	No	Energy, Gas, and Water
21.	CIMB Group Holdings	4.8	1.2	Yes	No	Finance
22.	Bank Pembangunan Malaysia	4.8	1.2	Yes	No	Banking
23.	YTL Power International	4.8	1.2	No	Yes	Energy, Gas, and Water
24.	AM Bank	4.5	1.2	No	Yes	Banking
25.	Putrajaya Holdings	4.5	1.2	Yes	No	Property and Real Estate
26.	Celcom Networks	4.5	1.2	No	No	Transport, Storage, and Communications
27.	Malakoff Power	4.4	1.1	No	No	Energy, Gas, and Water
28.	Cagamas MBS	4.2	1.1	Yes	No	Finance
29.	Sime Darby	4.2	1.1	Yes	Yes	Finance
30.	Tanjung Bin Power	4.0	1.0	No	No	Energy, Gas, and Water
Total Top 30 LCY Corporate Issuers		281.5	72.2			
Total LCY Corporate Bonds		512.3	131.4			
Top 30 as % of Total LCY Corporate Bonds		54.9%	54.9%			

LCY = local currency, MYR = Malaysian ringgit, USD = United States dollar.

Notes:

1. Data as of end-March 2016.

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.

Table 3 : Notable Local Currency Corporate Bond Issuance in Q1 2016

Corporate Issuers	Coupon Rate (%)	Issued Amount (MYR million)
Prasarana		
7-year Islamic MTN	4.29	500
10-year Islamic MTN	4.47	500
15-year Islamic MTN	4.75	700
20-year Islamic MTN	4.97	600
25-year Islamic MTN	5.07	755
Sime Darby		
10-year Islamic MTN	5.65	2,200
Pengurusan Air		
7-year Islamic MTN	4.43	1,000
10-year Islamic MTN	4.63	750
Danga Capital		
10-year Islamic MTN	4.60	1,500
Cagamas		
3-year MTN	4.10	1,120
Maybank Islamic		
10-year bond	4.65	1,000

MTN = medium-term note, MYR = Malaysian ringgit, Q1 = first quarter.
Source: Bank Negara Malaysia Bond Info Hub.

Investor Profile

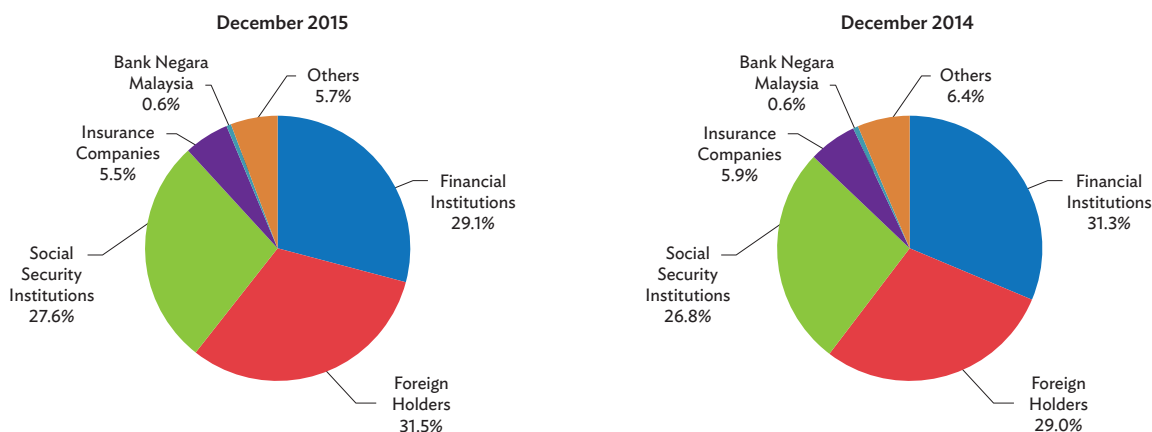
At the end of December, foreign investors comprised the largest share of the government bond market at 31.5%, surpassing financial institutions—including

banks, development financial institutions, and nonbank financial institutions—whose share declined to 29.1% from 31.3% at the end of December 2014 (**Figure 2**). Social security institutions remained the third largest holders of government bonds with a share of 27.6%, which was slightly higher than their share of 26.8% a year earlier. Meanwhile, the share of insurance companies' government bond holdings fell to 5.5% from 5.9% a year earlier.

Domestic banks (commercial and Islamic) remained the largest investor group in LCY corporate bonds at the end of March 2016 with a share of 46.5% (**Figure 3**). Compared with March 2015, the share of domestic banks increased 1.7 percentage points, while that of foreign banks decreased 2.2 percentage points to 5.7%. Life insurance companies remained the second largest holders of LCY corporate bonds with a share of 31.8%, up from 30.6% a year earlier.

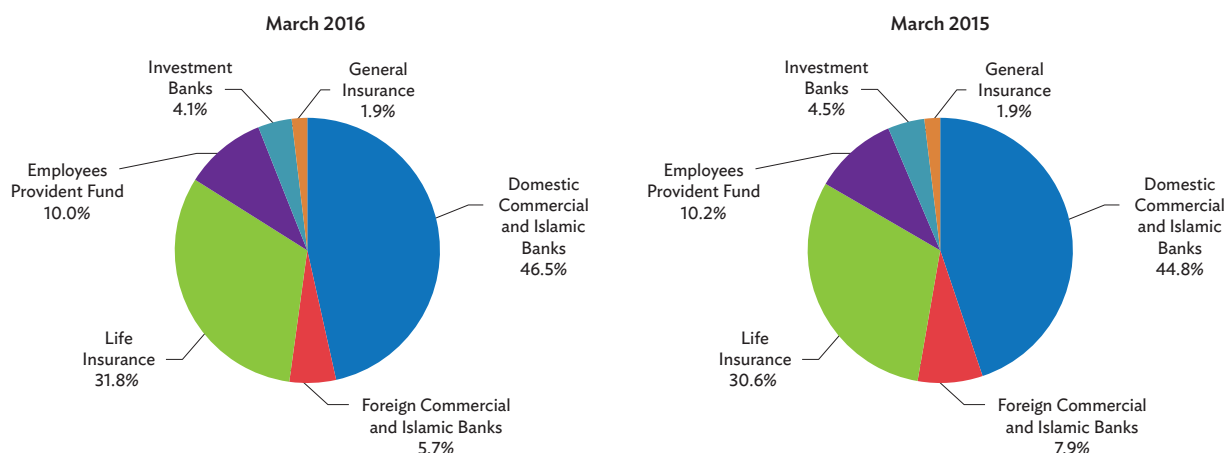
Ratings Update

In February, Fitch Ratings (Fitch) affirmed its long-term foreign currency issuer default rating of A– and long-term local currency issuer default rating of A for Malaysia, with a stable outlook for both ratings. Fitch cited as reasons for its decision Malaysia's commitment to fiscal consolidation, the stabilization of the Malaysian ringgit and foreign reserves, and strong (despite slower) economic growth relative to its A-rated peers.

Figure 2: Local Currency Government Bonds Investor Profile

Note: "Others" include statutory bodies, nominees and trustee companies, and cooperatives and unclassified items.
Source: Bank Negara Malaysia.

Figure 3: Local Currency Corporate Bonds Investor Profile



Note: The Employees Provident Fund's bond holdings data is as of end-December 2015.
Source: Bank Negara Malaysia and Employees Provident Fund.

In March, S&P Global Ratings (S&P) affirmed its A-/A-2 foreign currency and A/A-1 local currency sovereign credit ratings for Malaysia. S&P also maintained a stable outlook on both ratings. S&P cited Malaysia's strong external position and monetary flexibility as reasons for its decision. S&P expects the Government of Malaysia to continue its policies to achieve balanced economic growth despite ongoing issues concerning 1MDB.

Policy, Institutional, and Regulatory Developments

Bank Negara Malaysia and Bank of Thailand Launch Local Currency Settlement Framework

In March, BNM and the Bank of Thailand announced the launch of a local currency settlement framework intended to promote bilateral trade between the two economies. The framework will allow Malaysian and Thai

businesses greater access to local currency and other financial services in appointed banks in both markets. The framework follows a memorandum of understanding signed between the two central banks in August 2015.

Securities Commission Malaysia Introduces Regulatory Framework for Peer-to-Peer Financing Program

In April, the Securities Commission Malaysia introduced the regulatory framework for a peer-to-peer financing (P2P) program, including requirements for the registration of a P2P platform. The P2P electronic platform facilitates access to market-based financing for eligible private and unlisted companies. The framework also outlines the duties and responsibilities of a P2P operator, as well as the types of issuers and investors who can participate in the platform.