

Malaysia

Yield Movements

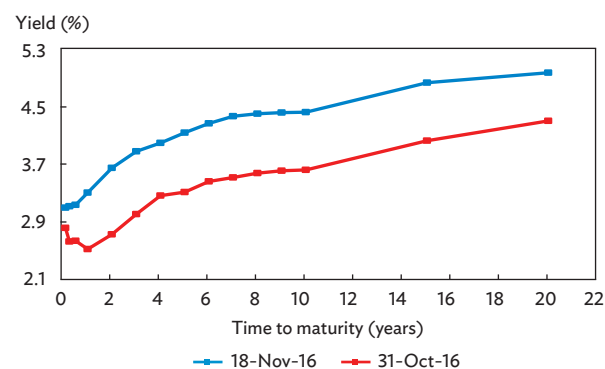
Between 31 October and 18 November, local currency (LCY) government bond yields rose for all tenors. Yields for tenors of less than 1 year rose 42 basis points (bps) on average (**Figure 1**). Yields for tenors of 1 year to 20 years rose 81 bps on average, ranging between 67 bps and 92 bps. The spread between the 2-year and 10-year yields narrowed to 77 bps on 18 November from 89 bps on 31 October.

Yields have been on the rise since September due to volatile oil prices and, particularly, after the October release of the minutes of the United States (US) Federal Reserve meeting, which strengthened the case for the likelihood of a federal funds rate hike in December. Yields soared in November as the market reacted to the unexpected outcome of the US presidential election, reflecting uncertainty over the economic policies of the next administration. Markets foresee increased inflationary pressures in the US as the new administration intends to focus on fiscal expansion, prompting speculation that the Federal Reserve may raise rates more quickly than previously expected. This has led to a sell-off in bonds in the region. Malaysia, along with Indonesia, saw the highest rise in yields as more than a third of its LCY central government bonds are held by foreign investors.

The depreciation of the Malaysian ringgit reflected these developments. As of 18 November, the currency had dropped 8.3% against the US dollar since 1 September and 5.2% since the US presidential election on 8 November. In an effort to mitigate market volatility, Bank Negara Malaysia (BNM) announced on 13 November the reinforcement of existing restrictions on the facilitation of ringgit nondeliverable forward contracts, which the BNM considers speculative.

Foreign holdings of central government bonds remained high in the third quarter (Q3) of 2016. However, September saw the first net capital outflows for the year, with foreign holdings of central government bonds declining to MYR212 billion at end-September from a high of MYR218 billion in August, partly due to maturing Malaysian Government Securities (MGSSs). Foreign investors returned to the market in October due to new

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



Source: Based on data from Bloomberg LP.

issuances of central government bonds, resulting in a rebound of foreign holdings to MYR218 billion. However, recent news in November noted outflows following market uncertainty which resulted after the US election.

At its 7 September Monetary Policy Committee meeting, BNM decided to keep its overnight policy rate at 3.00%. The central bank stated that while volatility in global financial markets has subsided, downside risks remain. The committee expects Malaysia's economy to grow in 2016 in line with prior expectations of continued support from domestic demand.

Malaysia's economic growth inched up to 4.3% y-o-y in Q3 2016 from 4.0% y-o-y in the second quarter (Q2) of 2016, mainly due the accelerated increase in private consumption. Inflation remained subdued in Q3 2016, averaging 1.4% y-o-y over the 3-month period.

Size and Composition

The Malaysian LCY bond market barely changed in size in Q3 2016, with a minimal increase in bonds outstanding of 0.4% quarter-on-quarter (q-o-q) to reach MYR1,168 billion (USD282 billion) at the end of September (**Table 1**). A decline in the government bond sector was compensated for by growth in the corporate bond market. Total government bonds outstanding summed to MYR632 billion, while corporate bonds amounted to MYR537 billion. *Sukuk* (Islamic bonds)

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

| | Outstanding Amount (billion) | | | | | | Growth Rate (%) | | | |
|--------------------------|------------------------------|------------|--------------|------------|--------------|------------|-----------------|--------------|------------|------------|
| | Q3 2015 | | Q2 2016 | | Q3 2016 | | Q3 2015 | | Q3 2016 | |
| | MYR | USD | MYR | USD | MYR | USD | q-o-q | y-o-y | q-o-q | y-o-y |
| Total | 1,076 | 245 | 1,163 | 289 | 1,168 | 282 | (0.01) | (0.3) | 0.4 | 8.6 |
| Government | 602 | 137 | 644 | 160 | 632 | 153 | (1.0) | (4.9) | (1.9) | 4.9 |
| Central Government Bonds | 549 | 125 | 600 | 149 | 592 | 143 | (1.5) | 8.0 | (1.3) | 8.0 |
| of which: <i>Sukuk</i> | 206 | 47 | 232 | 57 | 236 | 57 | (1.4) | 10.4 | 1.9 | 14.6 |
| Central Bank Bills | 25 | 6 | 15 | 4 | 11 | 3 | 6.4 | (77.0) | (29.5) | (56.7) |
| of which: <i>Sukuk</i> | 2 | 0 | 0 | 0 | 0 | 0 | (59.5) | (96.0) | – | (100.0) |
| Sukuk Perumahan Kerajaan | 28 | 6 | 28 | 7 | 28 | 7 | 1.8 | 67.1 | 0.0 | 0.0 |
| Corporate | 474 | 108 | 519 | 129 | 537 | 130 | 1.3 | 6.1 | 3.3 | 13.3 |
| of which: <i>Sukuk</i> | 340 | 77 | 375 | 93 | 393 | 95 | 1.0 | 8.5 | 4.9 | 15.5 |

(-) = negative, – = not applicable, MYR = Malaysian ringgit, q-o-q = quarter-on-quarter, Q2 = second quarter, Q3 = third 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.

continued to account for most of Malaysia's LCY bond market with a share of 56.3% at the end of September. On a y-o-y basis, Malaysia's LCY bond market expanded 8.6%.

Government Bonds. LCY government bonds outstanding fell 1.9% q-o-q to MYR632 billion at the end of September due to maturing MGSs and declining issuances in Q3 2016. The outstanding stock of central bank bills continued to decline, while Government Investment Issues increased in Q3 2016. On a y-o-y basis, government bonds outstanding rose 4.9%.

Issuance of government bonds fell in Q3 2016 due to smaller bond auction programs for MGSs and Government Investment Issues. On the other hand, issuance of Treasury bills and central bank bills rose in Q3 2016, albeit by smaller amounts.

Corporate Bonds. LCY corporate bonds rose 3.3% q-o-q to MYR537 billion at the end of September. Malaysia's LCY corporate bond market continued to be dominated by *sukuk* in Q3 2016, with their share of the total inching up to 73.3% at the end of September from 72.2% at the end of June.

Table 2 presents the top 30 LCY corporate bond issuers in Malaysia at the end of September. The top 30 issuers comprised 54.7% of the total LCY corporate bond

market, with aggregate bonds outstanding amounting to MYR293.5 billion. Financial firms, including banks, continued to account for a majority of the top 30 largest debt issuers, with total bonds outstanding worth MYR158.8 billion. Other firms in the list include those involved in transportation and communications, utilities, construction, and real estate. Approximately two-thirds of those on the list are also state-owned firms. Highway operator Project Lebuhraya Usahasama remained the largest issuer with MYR30.6 billion of outstanding bonds. State-owned mortgage firm Cagamas was second with MYR27.0 billion.

Corporate bond issuance picked up in Q3 2016 to MYR39.9 billion from MYR34.1 billion in the previous quarter. *Sukuk* dominated corporate bond issuance in Q3 2016, with a share rising to 69.9% from 58.9% in the previous quarter. By type of instrument, Islamic medium-term notes (MTNs) continued to account for the single-highest share of total issuance at 53.5%, while conventional commercial paper was next with a share of 16.8%. **Table 3** lists notable corporate bond issuances in Q3 2016.

Government-owned entities were some of the largest bond issuers in Q3 2016, led by Sarawak Hidro, developer of Malaysia's largest hydropower project, which issued MYR5.5 billion worth of multitranches Islamic MTNs. Malaysia's Lembaga Pembiayaan Perumahan Sektor

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 | 7.4 | No | No | Transport, Storage, and Communications |
| 2. | Cagamas | 27.0 | 6.5 | Yes | No | Finance |
| 3. | Danainfra Nasional | 25.2 | 6.1 | Yes | No | Finance |
| 4. | Prasarana | 20.6 | 5.0 | Yes | No | Transport, Storage, and Communications |
| 5. | Khazanah | 20.0 | 4.8 | Yes | No | Finance |
| 6. | Perbadanan Tabung Pendidikan Tinggi Nasional | 14.5 | 3.5 | Yes | No | Finance |
| 7. | Pengurusan Air | 13.8 | 3.3 | Yes | No | Energy, Gas, and Water |
| 8. | Maybank | 13.7 | 3.3 | No | Yes | Banking |
| 9. | CIMB Bank | 10.1 | 2.4 | No | No | Banking |
| 10. | Sarawak Energy | 9.5 | 2.3 | Yes | No | Energy, Gas, and Water |
| 11. | Jimah East Power | 9.0 | 2.2 | Yes | No | Energy, Gas, and Water |
| 12. | Public Bank | 8.6 | 2.1 | No | No | Banking |
| 13. | Sarawak Hidro | 6.5 | 1.6 | Yes | No | Energy, Gas, and Water |
| 14. | Aman Sukuk | 6.3 | 1.5 | Yes | No | Construction |
| 15. | Rantau Abang Capital | 6.0 | 1.4 | Yes | No | Finance |
| 16. | RHB Bank | 5.4 | 1.3 | No | No | Banking |
| 17. | Turus Pesawat | 5.3 | 1.3 | Yes | No | Transport, Storage, and Communications |
| 18. | CIMB Group Holdings | 5.2 | 1.3 | Yes | No | Finance |
| 19. | BGSM Management | 5.1 | 1.2 | No | No | Transport, Storage, and Communications |
| 20. | 1Malaysia Development | 5.0 | 1.2 | Yes | No | Finance |
| 21. | Danga Capital | 5.0 | 1.2 | Yes | No | Finance |
| 22. | Putrajaya Holdings | 4.9 | 1.2 | Yes | No | Property and Real Estate |
| 23. | Manjung Island Energy | 4.9 | 1.2 | No | No | Energy, Gas, and Water |
| 24. | YTL Power International | 4.8 | 1.2 | No | Yes | Energy, Gas, and Water |
| 25. | GOVCO Holdings | 4.6 | 1.1 | Yes | No | Finance |
| 26. | Jambatan Kedua | 4.6 | 1.1 | Yes | No | Transport, Storage, and Communications |
| 27. | Celcom Networks | 4.5 | 1.1 | No | No | Transport, Storage, and Communications |
| 28. | Malakoff Power | 4.4 | 1.1 | No | No | Energy, Gas, and Water |
| 29. | Bank Pembangunan Malaysia | 4.4 | 1.1 | Yes | No | Banking |
| 30. | AM Bank | 4.2 | 1.0 | No | Yes | Banking |
| Total Top 30 LCY Corporate Issuers | | 293.5 | 70.9 | | | |
| Total LCY Corporate Bonds | | 536.6 | 129.7 | | | |
| Top 30 as % of Total LCY Corporate Bonds | | 54.7% | 54.7% | | | |

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

Notes:

1. Data as of end-September 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 Q3 2016

| Corporate Issuers | Coupon Rate (%) | Issued Amount (MYR million) |
|---|-----------------|-----------------------------|
| Sarawak Hidro | | |
| 3-year Islamic MTN | 4.11 | 245 |
| 4-year Islamic MTN | 4.16 | 360 |
| 5-year Islamic MTN | 4.21 | 410 |
| 6-year Islamic MTN | 4.25 | 425 |
| 7-year Islamic MTN | 4.29 | 450 |
| 8-year Islamic MTN | 4.34 | 470 |
| 9-year Islamic MTN | 4.38 | 470 |
| 10-year Islamic MTN | 4.43 | 480 |
| 11-year Islamic MTN | 4.47 | 470 |
| 13-year Islamic MTN | 4.56 | 510 |
| 14-year Islamic MTN | 4.61 | 625 |
| 15-year Islamic MTN | 4.67 | 625 |
| Lembaga Pembiayaan Perumahan Sektor Awam | | |
| 3-year Islamic MTN | 3.50 | 300 |
| 5-year Islamic MTN | 3.60 | 600 |
| 7-year Islamic MTN | 3.83 | 700 |
| 10-year Islamic MTN | 4.05 | 700 |
| 20-year Islamic MTN | 4.62 | 900 |
| 30-year Islamic MTN | 4.90 | 800 |

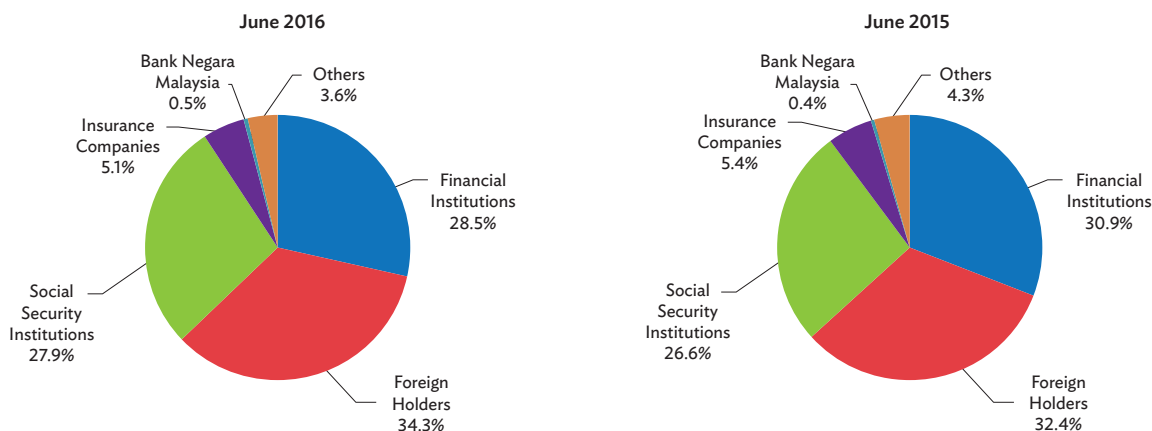
MTN = medium-term note, MYR = Malaysian ringgit, Q3 = third quarter.
Source: Bank Negara Malaysia Bond Info Hub.

Awam (Public Sector Housing Financing Agency) also issued multitranches Islamic MTN worth MYR4.0 billion. Lebuhraya Duke Fasa 3, established by private company Ekovest Berhad to undertake the Duke Phase 3 expressway under a concession agreement with the Government of Malaysia, issued MYR3.6 billion worth of multitranches Islamic MTNs.

Investor Profile

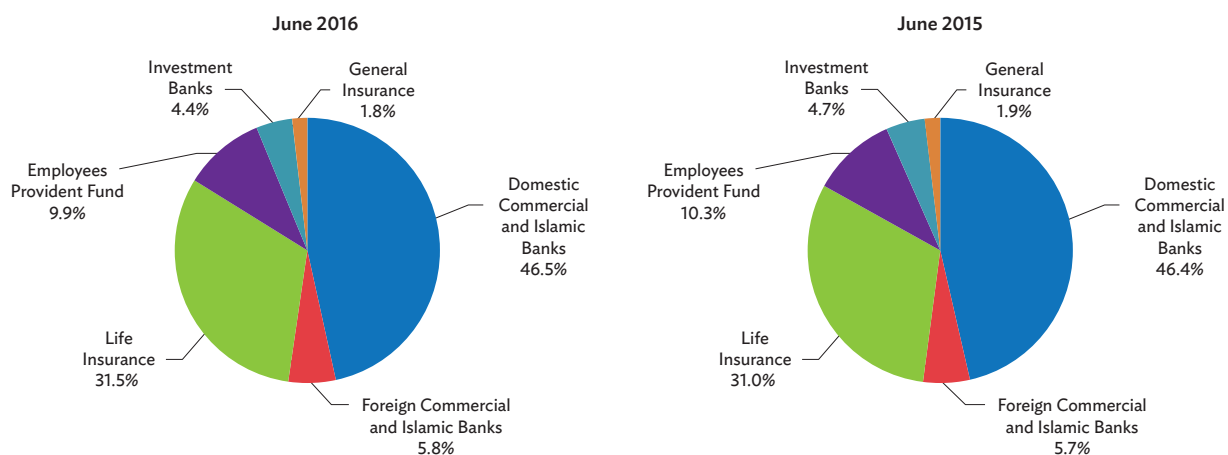
Foreign investors continued to account for the largest holdings of LCY government bonds at the end of June with a 34.3% share of the total, up from 32.4% a year earlier (**Figure 2**). Financial institutions remained the second-largest investor group of LCY government bonds with a share of 28.5% at the end of June, down from 30.9% in June 2015. The share of social security institutions' government bond holdings inched up to 27.9% from 26.6% during the review period.

The investor profile of Malaysia's corporate bond market was barely changed at the end of June compared with a year earlier (**Figure 3**). Domestic banks, both commercial and Islamic, remained the largest investor group with a share of 46.5%. Life insurance companies remained the second-largest holders of corporate bonds with a share of 31.5%.

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 are as of end-December 2015.
Sources: Bank Negara Malaysia and the Employees Provident Fund.

Policy, Institutional, and Regulatory Developments

Prime Minister Announces 2017 Federal Budget

On 21 October, the Prime Minister announced the release of Malaysia's 2017 federal budget with a total allocation of MYR260.8 billion for a 3.4% increase from the 2016 revised budget. The government also announced a fiscal deficit target of MYR40.3 billion, or

3.0% of gross domestic product, down from the 2016 target of 3.1%. Federal government revenue collection is expected to increase 3.0% y-o-y to MYR219.7 billion. The Prime Minister noted the decline in revenues due to the continued fall in oil prices, with an estimated loss of MYR30 billion. Collections from the implementation of the Goods and Services Tax, which was launched in 2015, had reached MYR30 billion as of 19 October 2016. The economy is expected to grow 4.0%–5.0% in 2017, while annual inflation is forecasted at 2.0%–3.0%.