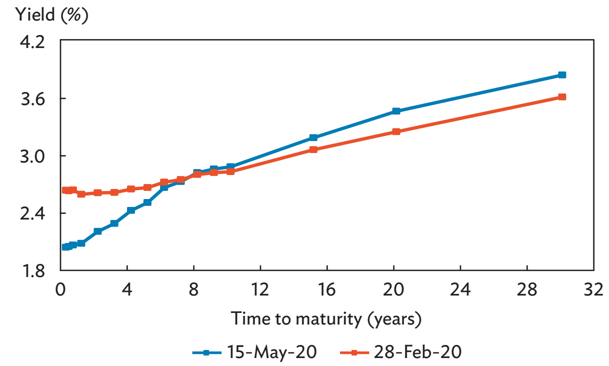
Malaysia

Yield Movements

Between 28 February and 15 May, movements in Malaysia's local currency (LCY) government bond yields were mixed (**Figure 1**). Yield of bonds with 1-month to 7-year tenor declined an average of 34 basis points (bps). Yields of longer-term tenors (from 8 years to 30 years) increased an average of 11 bps. The yield spread between 2-year and 10-year government bonds expanded from 22 bps to 67 bps during the review period.

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



Source: Based on data from Bloomberg LP.

The movement at the shorter-end of the yield curve in Malaysia was driven by Bank Negara Malaysia's (BNM) decision to cut its overnight policy rate by a total of 75 bps during its monetary policy committee meetings held on 3 March and 5 May. To enhance liquidity amid the economic fallout from the coronavirus disease (COVID-19) pandemic, BNM also announced in March that banks may use Malaysian Government Securities and Government Investment Issues to fulfill their statutory reserve requirements. The decline in demand for longer-term tenors reflects investors' flight to safety amid an uncertain economic outlook. In March, Malaysia's 10-year yield spiked as a substantial decline in global oil prices hampered sentiments in global financial markets, with investors demanding a higher risk premium. Investors turned wary of the possible effects of oil-related revenues on Malaysia's fiscal balance. The 10-year yield has since fallen as global oil prices rebounded.

On 5 May, the monetary policy committee of BNM decided to lower the overnight policy rate by 50 bps to 2.00%, the third time in 2020 that it has reduced the policy rate. The committee decreased the overnight policy rate by 25 bps during its 22 January and 3 March meetings. The series of reductions were meant to ensure price stability and a stable growth trajectory for Malaysia's economy. But with the COVID-19 pandemic disrupting economic activities worldwide, the decision was viewed as enabling conditions for a sustainable economic recovery.

Prices of basic goods and services in Malaysia declined 0.2% year-on-year (y-o-y) in March, dragged down by the transport industry. This came after consumer price inflation of 1.6% y-o-y and 1.3% y-o-y in January and February, respectively. In May, BNM announced that it expects inflation for full-year 2020 to be negative due to falling global oil and other commodity prices.

Malaysia's economic growth slowed to 0.7% y-o-y in the first quarter (Q1) of 2020 from 4.4% y-o-y and 3.6% y-o-y in the third quarter and fourth quarter (Q4) of 2019, respectively. In April, BNM's economic growth forecast for full-year 2020 was between –2.0% and –0.5% due to weak global demand that has led to declining oil prices and commodity supply disruptions. During the second half of March, the Government of Malaysia implemented a Movement Control Order to contain the spread of COVID-19. This is expected to lead to limited domestic demand. BNM expects the Malaysian economy to contract in the second quarter of 2020.

Size and Composition

Malaysia's LCY bond market expanded 2.9% quarter-on-quarter (q-o-q) in Q1 2020 to reach a size of MYR1,527.8 billion (USD353.7 billion), up from MYR1,485.4 billion at the end of Q4 2019 (**Table 1**). The growth corresponds to a 6.0% y-o-y jump from MYR1,440.8 billion at the end of Q1 2019. The growth in the LCY bond market in Q1 2020 was supported by expansions in both LCY government and corporate bonds, which accounted for 52.6% and 47.4%, respectively, of total LCY bonds outstanding at the end of March. Total outstanding *sukuk* (Islamic bonds) at the

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

	Outstanding Amount (billion)						Growth Rate (%)			
	Q1 2019		Q4 2019		Q1 2020		Q1 2019		Q1 2020	
	MYR	USD	MYR	USD	MYR	USD	q-o-q	y-o-y	q-o-q	y-o-y
Total	**1,441**	**353**	**1,485**	**363**	**1,528**	**354**	**2.9**	**7.6**	**2.9**	**6.0**
Government	766	188	773	189	804	186	3.6	8.7	3.9	4.9
Central Government Bonds	720	176	737	180	767	177	4.2	9.8	4.0	6.4
of which: *Sukuk*	327	80	341	83	362	84	6.7	14.1	5.9	10.6
Central Bank Bills	17	4	9	2	10	2	(9.9)	(13.9)	11.1	(42.2)
of which: *Sukuk*	5	1.3	1	0.2	2	0.3	40.5	420.0	50.0	(71.2)
Sukuk Perumahan Kerajaan	28	7	27	7	27	6	(1.8)	(1.8)	0.0	(3.9)
Corporate	675	165	712	174	724	168	2.0	6.4	1.7	7.3
of which: *Sukuk*	520	127	569	139	577	134	3.0	8.3	1.5	11.0

( ) = 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 rates are 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 and Bloomberg LP.

end of the review period stood at MYR966.7 billion on growth of 3.1% q-o-q from MYR937.7 billion at the end of the previous quarter, spurred by increased stocks of government and corporate *sukuk*.

Issuance of LCY bonds in Q1 2020 increased 10.7% q-o-q to MYR92.6 billion from MYR83.7 billion in Q4 2019, driven by increased government bond issuance.

Government bonds. The LCY government bond market grew 3.9% q-o-q to MYR803.5 billion in Q1 2020, up from MYR773.2 billion in the previous quarter. The growth was due to the 4.0% q-o-q increase in outstanding central government bonds, which comprised 95.4% of total outstanding LCY government bonds, and the 11.1% q-o-q expansion of outstanding central bank bills, which comprised a 1.2% share of total LCY government bonds outstanding. The outstanding stock of Sukuk Perumahan Kerajaan (3.3% of total outstanding LCY government bonds) remained unchanged from the previous quarter.

LCY government bonds issued in Q1 2020 surged 42.9%, spurred by robust issuance of government bonds and Treasury bills. These were more than enough to offset the decline in BNM bills. Issuance of Malaysian Government Securities and Government Investment Issues jumped compared to the previous quarter.

Corporate bonds. LCY corporate bonds outstanding expanded 1.7% q-o-q to MYR724.3 billion in Q1 2020 from MYR712.2 billion in Q4 2019. Outstanding corporate *sukuk* rose 1.5% q-o-q to MYR576.8 billion at the end of March from MYR568.6 billion in the prior quarter.

The top 30 corporate bond issuers in Malaysia accounted for an aggregate MYR432.9 billion of corporate bonds outstanding at the end of Q1 2020, or 59.8% of the total corporate bond market (**Table 2**). Government institutions Danainfra Nasional, Prasarana, and Cagamas continued to dominate all issuers with outstanding LCY corporate bonds amounting to MYR63.8 billion (8.8% of total LCY corporate bonds outstanding), MYR34.5 billion (4.8%), and MYR32.9 billion (4.5%), respectively. By industry, finance comprised the largest share (53.4%) of the top 30 issuers with MYR231.1 billion in outstanding LCY corporate bonds at the end of March. This was followed by the transport, storage, and communications industry with MYR69.2 billion, which represented 16.0% of total LCY corporate bonds outstanding at the end Q1 2020.

Issuance of LCY corporate bonds declined 14.1% q-o-q in Q1 2020 due to the slow pace of issuance in January.

Government-owned public transport company Prasarana issued the most tranches of Islamic medium-term notes (MTN), issuing five tranches with tenors ranging from 7 years to 30 years, proceeds from which will be used for various Shari'ah-compliant activities of the company (**Table 3**). Prasarana also issued a MYR0.7 billion 20-year

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.	Danainfra Nasional	63.8	14.8	Yes	No	Finance
2.	Prasarana	34.5	8.0	Yes	No	Transport, Storage, and Communications
3.	Cagamas	32.9	7.6	Yes	No	Finance
4.	Project Lebuhraya Usahasama	29.4	6.8	No	No	Transport, Storage, and Communications
5.	Urusharta Jamaah	27.6	6.4	Yes	No	Finance
6.	Lembaga Pembiayaan Perumahan Sektor Awam	24.7	5.7	Yes	No	Property and Real Estate
7.	Perbadanan Tabung Pendidikan Tinggi Nasional	21.6	5.0	Yes	No	Finance
8.	Pengurusan Air	18.0	4.2	Yes	No	Energy, Gas, and Water
9.	Khazanah	14.2	3.3	Yes	No	Finance
10.	CIMB Bank	14.1	3.3	Yes	No	Finance
11.	Maybank Islamic	13.0	3.0	No	Yes	Banking
12.	Maybank	11.4	2.6	No	Yes	Banking
13.	CIMB Group Holdings	11.2	2.6	Yes	No	Finance
14.	Sarawak Energy	11.1	2.6	Yes	No	Energy, Gas, and Water
15.	Danga Capital	10.0	2.3	Yes	No	Finance
16.	Jimah East Power	9.0	2.1	Yes	No	Energy, Gas, and Water
17.	Public Bank	7.9	1.8	No	No	Banking
18.	GENM Capital	7.6	1.8	No	No	Finance
19.	Bank Pembangunan Malaysia	7.2	1.7	Yes	No	Banking
20.	GOVCO Holdings	7.2	1.7	Yes	No	Finance
21.	Tenaga Nasional	7.0	1.6	No	Yes	Energy, Gas, and Water
22.	Bakun Hydro Power Generation	6.3	1.5	No	No	Energy, Gas, and Water
23.	YTL Power International	6.1	1.4	No	Yes	Energy, Gas, and Water
24.	Telekom Malaysia	5.8	1.3	No	Yes	Telecommunications
25.	Rantau Abang Capital	5.5	1.3	Yes	No	Finance
26.	Danum Capital	5.5	1.3	No	No	Finance
27.	Turus Pesawat	5.3	1.2	Yes	No	Transport, Storage, and Communications
28.	EDRA Energy	5.1	1.2	No	Yes	Energy, Gas, and Water
29.	1Malaysia Development	5.0	1.2	Yes	No	Finance
30.	Sunway Treasury Sukuk	4.9	1.1	No	No	Finance
Total Top 30 LCY Corporate Issuers		**432.9**	**100.2**			
Total LCY Corporate Bonds		**724.3**	**167.7**			
Top 30 as % of Total LCY Corporate Bonds		**59.8%**	**59.8%**			

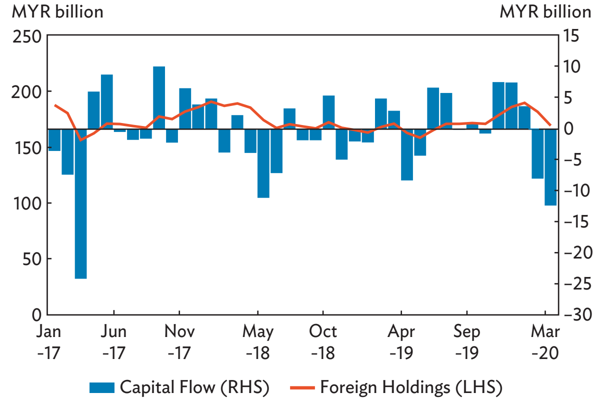
LCY = local currency, MYR = Malaysian ringgit, USD = United States dollar.
Notes:
1. Data as of 31 March 2020.
2. State-owned firms are defined as those in which the government has more than a 50% ownership stake.
Source: *AsianBondsOnline* calculations based on Bank Negara Malaysia Fully Automated System for Issuing/Tendering data.

Table 3: Notable Local Currency Corporate Bond Issuance in the First Quarter of 2020

Corporate Issuers	Coupon Rate (%)	Issued Amount (MYR billion)
Prasarana		
7-year Islamic MTN	3.02	0.4
10-year Islamic MTN	3.09	0.6
15-year Islamic MTN	3.28	0.5
20-year Islamic MTN	3.44	1.0
20-year *sukuk murabahah*	3.75	0.7
25-year Islamic MTN	3.90	0.7
30-year Islamic MTN	3.80	1.0
Khazanah		
20-year MTN	4.14	2.9
Aeon Credit Service		
7-year *sukuk wakalah*	3.80	0.3
8-year *sukuk wakalah*	3.85	0.2
10-year *sukuk wakalah*	3.95	0.2

MTN = medium-term note, MYR = Malaysian ringgit.
Notes:
1. *Sukuk murabahah* are Islamic bonds in which bondholders are entitled to a share of the revenues generated by the assets.
2. *Sukuk wakalah* are Islamic bonds backed by an agreement between an investor and an agent. The bondholders are entitled to profits as agreed upon by the two parties.
Source: Bank Negara Malaysia Bond Info Hub.

Figure 2: Foreign Holdings and Capital Flows of Local Currency Central Government Bonds in Malaysia



LHS = left-hand side, MYR = Malaysian ringgit, RHS = right-hand side.
Notes:
1. Figures exclude foreign holdings of Bank Negara Malaysia bills.
2. Month-on-month changes in foreign holdings of local currency government bonds were used as a proxy for bond flows.
Source: Bank Negara Malaysia Monthly Statistical Bulletin.

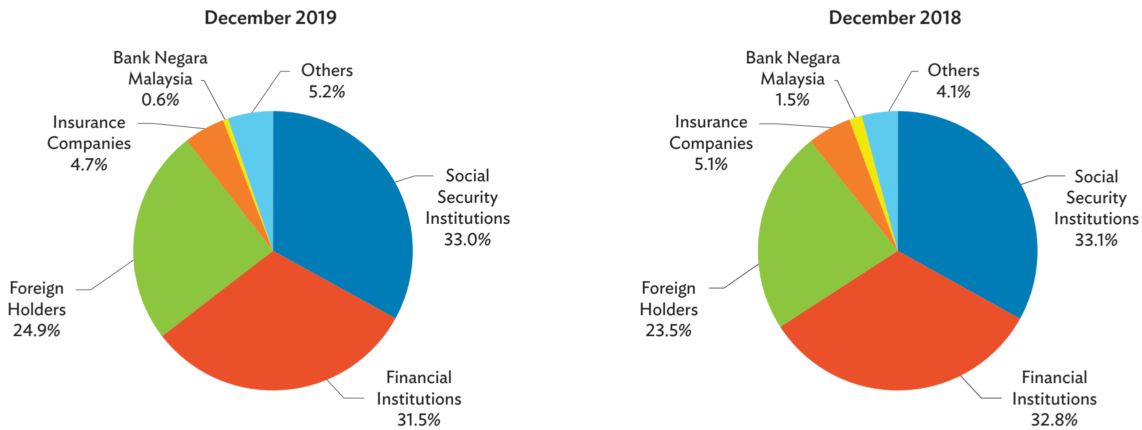
sukuk murabahah (an Islamic bond in which bondholders are entitled to a share of the revenues generated by the assets) with a coupon rate of 3.75%. The *sukuk* was issued under the company's Sukuk Murabahah Programme, and its proceeds will be used to finance Shari'ah-compliant activities related to the LRT3 project. Prasarana issued a 25-year Islamic MTN worth MYR0.7 billion and with a coupon rate 3.90%. Proceeds from the issuance will be used for Shari'ah-compliant capital expenditure and general working capital requirements. Khazanah had the single-largest issuance, which also carried the largest coupon, during the quarter with a MYR2.9 billion 20-year MTN and a 4.14% coupon rate. The sovereign wealth fund of the Government of Malaysia will utilize the proceeds to fund general investments and refinance borrowing. Aeon Credit Service issued two tranches of *sukuk* with tenors of 7 years and 8 years. It also sold a MYR0.2 billion 10-year *sukuk* with a 3.95% coupon rate. The financial institution will use the proceeds from the issuances to finance disbursements to its customers and refinance existing obligations.

Investor Profile

Foreign holdings of LCY government bonds in Q1 2020 jumped to MYR542.2 billion from MYR536.9 billion in Q4 2019, although monthly holdings showed a declining trend (**Figure 2**). A total of MYR16.7 billion in net capital outflows were recorded in Q1 2020, with the largest outflows recorded in March amid recession concerns as global investors became increasingly wary of the economic impact of the COVID-19 pandemic. This reversed the capital inflows of MYR14.4 billion recorded in the previous quarter. As a share of LCY government bonds, foreign holdings of LCY government bonds decreased to 22.2% at the end of Q1 2020 from 25.3% at the end of Q4 2019.

At the end of Q4 2019, social security institutions and financial institutions led all investors in LCY government bond holdings with 33.0% and 31.5% of the total, respectively, both of which were down from a year earlier (**Figure 3**). Foreign holders increased their share of total holdings to 24.9% from 23.5% in Q4 2018. The shares of insurance companies and BNM fell to 4.7% and 0.6%, respectively, from 5.1% and 1.5% during the review period.

Figure 3: Local Currency Government Bonds Investor Profile



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

Ratings Update

On 27 March, S&P Global affirmed Malaysia's A-/A-2 foreign currency and A/A-1 local currency ratings with a stable outlook for both. Despite falling oil prices and the sudden change in government, the rating agency hailed the economy's strong position in the international market, monetary stance flexibility, and well-established institutions. It also expects the new government to continue the reforms started by the previous administration. On the other hand, increasing net general government debt and rising political risk are placing downward pressure on the economy's ratings.

On 9 April, Fitch Ratings affirmed Malaysia's long-term foreign currency issuer default rating at A– but revised its outlook to negative from stable. Declining economic activities due to the lockdown imposed to fight the COVID-19 pandemic have weakened growth prospects for Malaysia. The uncertainty of the duration of the pandemic contributed to the weak projections for the economy. Fitch Ratings is also wary of political risks hampering improvements in governance for the past 2 years as the new government's plans have yet to be laid out.

Policy, Institutional, and Regulatory Developments

Bank Negara Malaysia Decreases Statutory Reserve Requirement

On 19 March, BNM decreased the statutory reserve requirement ratio from 3.0% to 2.0%. Principal dealers can now include up to a total of MYR1.0 billion worth of Malaysian Government Securities and Government Investment Issues in the computation of their reserves. On 5 May, the central bank allowed all banking institutions to do the same, although no cap on the total amount was mentioned. The measures are expected to release MYR46.0 billion worth of liquidity into Malaysia's banking system to support financial activities in the market.

FTSE Russell Keeps Malaysia on Its Watchlist

On 2 April, FTSE Russell decided to keep Malaysia on its watchlist during its interim March review, saying it would continue to monitor Malaysia for a possible downgrade. To avoid being removed from the FTSE Russell World Government Bond Index, Malaysia has been given 6 months to improve its market conditions. Since its placement on the watchlist last year, Malaysia has implemented regulations to improve bond and foreign exchange liquidity conditions. The decision on whether or not to exclude Malaysia from the benchmark index is expected during FTSE Russell's annual review in September.