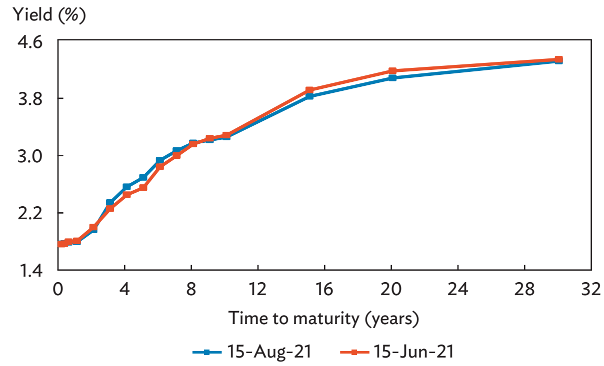
Malaysia

Yield Movements

Movements in Malaysia's local currency (LCY) government bond yields were mixed between 15 June and 15 August (**Figure 1**). Yields for the 1-month and 3-month tenors barely moved, increasing 0.3 basis points (bps) and 0.1 bps, respectively. At the shorter-end of the curve, the 6-month tenor and 1-year tenor declined 1 bp each, while the 2-year yield decreased 4 bps. Yields on tenors of 3 years to 7 years jumped an average of 10 bps, with the 5-year yield rising the most among all tenors with a 14-bps gain during the review period. The longer-end of the yield curve (9 years to 30 years) recorded declines, with the 20-year yield declining the most at 10 bps. During the review period, the yield spread between 2-year and 10-year government bonds slightly increased from 128 bps to 129 bps.

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



Source: Based on data from Bloomberg LP.

The mixed movement in yields reflected investors' cautious view of the economy as Malaysia and its neighboring economies continued to reel from the effects of the COVID-19 pandemic, with the spread of the delta variant and an increasing number of COVID-19 cases remaining a threat to the domestic and global economic recovery. Uncertainty in Malaysia's political landscape also affected Malaysia's financial markets, and the selling pressure in the belly of the yield curve may be attributed to risk-off sentiment among investors. On the other hand, the low long-term yields may be ascribed to the low-interest-rate environment as Bank Negara Malaysia (BNM) kept the overnight policy rate at 1.75% in July.

Aggravated by political uncertainty, the Malaysian ringgit weakened 2.8% against the United States (US) dollar during the review period to close at MYR4.2375 per USD1.0 dollar on 15 August.

On 8 July, the monetary policy committee of BNM maintained its policy rate at 1.75%. The decision came as the global economy continued to recover from the COVID-19 pandemic. On the domestic front, Malaysia's economic growth in the first quarter (Q1) of 2021 was better than expected, although this growth was slightly dampened in the second quarter (Q2) of 2021 as the economy was placed under another Movement Control Order to curb the spread of COVID-19 infections. Malaysia's stimulus packages and strong external position are helping to support economic growth.

Malaysia's economy grew 16.1% year-on-year (y-o-y) on Q2 2021, reversing 4 straight quarters of contraction. Gross domestic product (GDP) growth was supported by expansions in the manufacturing and services sectors. At the same time, the significant growth in Q2 2021 was buoyed by a low base effect from Q2 2020 when GDP growth plunged owing to the first Movement Control Order implemented in March 2020 to curb the spread of COVID-19. On a quarter-on-quarter (q-o-q) basis, economic growth fell 2.0% during the quarter. In Q2 2021, the value of Malaysia's GDP remained lower than its pre-pandemic level in the fourth quarter of 2019. In August, BNM revised its expected full-year 2021 economic growth to 3.0%–4.0% from 6.0%–7.5%, mainly due to the effects of COVID-19 containment measures.

Consumer price inflation followed a downtrend, though remained elevated, during Q2 2021. From 4.7% y-o-y in April, prices of basic goods and services increased at a slower pace in May and June, recording inflation of 4.4% y-o-y and 3.4% y-o-y, respectively. Prices in April and May were elevated as increased demand from consumers coincided with Muslim festivities. The elevated inflation rates were also due to a low base effect from low retail fuel prices in 2020 and a lag in the effects of the government's tiered rebate of the electricity tariff implemented from April to December 2020. By July, inflation fell to 2.2% y-o-y. Malaysia's central bank expects consumer price inflation will fall between 2.5% and 4.0% for full-year 2021.

In June, the Government of Malaysia unveiled the National Recovery Plan, an exit strategy from the COVID-19 crisis. The plan consists of four phases. Movement from one phase to another is based on three thresholds: (i) number of daily COVID-19 infections, (ii) bed utilization rates in intensive care unit wards, and (iii) the percentage of the population that is fully vaccinated. Various restrictions on economic and social activities will be implemented during each phase, relaxing as the economy moves to latter phases. Malaysia was in Phase 1, the strictest phase, in June as a full Movement Control Order was implemented to curb rising COVID-19 cases. As of 4 August, seven states remained in Phase 1, while six states were in Phase 2, and three states had moved to Phase 3. By the end of October, 60% of Malaysia's population is expected to be fully vaccinated through the National COVID-19 Immunization Programme.

Size and Composition

The LCY bond market of Malaysia expanded 2.7% q-o-q in Q2 2021 to reach a size of MYR1,693.3 billion (USD408.1 billion) at the end of June, up from MYR1,648.9 billion at the end of Q1 2021 (**Table 1**). The Q2 2021 expansion was slightly slower than the 2.8% q-o-q growth recorded in Q1 2021. On an annual basis, the LCY bond market grew 8.9% y-o-y in Q2 2021, which was faster than the 7.9% y-o-y growth posted in the prior quarter. The growth may be attributed to expansions in both LCY government and corporate bonds, which accounted for 54.6% and 45.4%, respectively, of total LCY bonds outstanding at the end of June. At the end of the review period, total outstanding *sukuk* (Islamic bonds) reached MYR1,065.1 billion on growth of 2.3% q-o-q that was supported by increased stocks of government and corporate *sukuk*.

Issuance of LCY bonds in Q2 2021 increased 1.0% q-o-q to MYR101.2 billion from MYR100.2 billion in Q1 2021, driven by increased corporate bond issuance. The growth was partially offset by a decline in issuance of government bonds.

Government bonds. The LCY government bond market grew 3.9% q-o-q to a size of MYR924.1 billion at the end of Q2 2021 from MYR889.6 billion at the end of March. The Q2 2021 expansion was slower than the growth of 4.3% q-o-q in the previous quarter. The increase was due to the increase of 4.1% q-o-q in outstanding central government bonds, which comprised 97.4% of total outstanding LCY government bonds at the end of June, spurred by the increased stock of government bonds and Treasury bills. There were no outstanding central bank bills at the end of June, while the amount of outstanding

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

	Outstanding Amount (billion)						Growth Rate (%)			
	Q2 2020		Q1 2021		Q2 2021		Q2 2020		Q2 2021	
	MYR	USD	MYR	USD	MYR	USD	q-o-q	y-o-y	q-o-q	y-o-y
Total	**1,555**	**363**	**1,649**	**398**	**1,693**	**408**	**1.8**	**4.5**	**2.7**	**8.9**
Government	829	193	890	215	924	223	3.2	6.4	3.9	11.5
Central Government Bonds	797	186	865	209	900	217	4.0	7.4	4.1	12.9
of which: *Sukuk*	367	86	403	97	415	100	1.5	10.1	2.9	12.9
Central Bank Bills	5	1	1	0	0	0	(50.0)	(45.7)	(100.0)	(100.0)
of which: *Sukuk*	0	0	0	0	0	0	(100.0)	(100.0)	–	–
Sukuk Perumahan Kerajaan	27	6	24	6	24	6	0.0	(3.9)	0.0	(10.1)
Corporate	726	169	759	183	769	185	0.2	2.4	1.3	6.0
of which: *Sukuk*	582	136	614	148	626	151	0.9	5.0	2.0	7.6

( ) = negative, – = not applicable, MYR = Malaysian ringgit, q-o-q = quarter-on-quarter, Q1 = first quarter, Q2 = second 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* refers to Islamic bonds.
5. 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.

Sukuk Perumahan Kerajaan, which comprised 2.6% of total outstanding LCY government bonds at the end of Q2 2021, was unchanged from Q1 2021.

LCY government bond issuance in Q2 2021 declined 1.8% q-o-q to MYR56.0 billion from MYR57.0 billion in Q1 2021. The reduced issuance was due to slightly lower issuances of government bonds and Treasury bills.

The total issuance of Malaysian Government Securities (conventional bonds) and Government Investment Issues (Islamic bonds) during the first half of 2021 increased compared to the first half of 2020 as Movement Control Orders restricted economic activities, and fiscal support was needed in response.

Corporate bonds. Outstanding LCY corporate bonds outstanding grew 1.3% q-o-q to MYR769.2 billion at the end of June from MYR759.3 billion at the end of March. Growth in Q2 2021 was faster than the 1.0% q-o-q growth logged in Q1 2021. The amount of outstanding corporate *sukuk* grew 2.0% q-o-q to MYR626.4 billion in Q2 2021 from MYR614.4 billion in Q1 2021, with growth also accelerating from 0.9% q-o-q in the previous quarter.

Malaysia's top 30 corporate bond issuers accounted for MYR456.4 billion of outstanding corporate bonds at the end of Q2 2021, representing 59.3% of the total LCY corporate bond market (**Table 2**). Government-owned Danainfra Nasional led all issuers with LCY corporate bonds outstanding amounting to MYR76.0 billion. Financial institutions had the largest sectoral share (52.9%) among all sectors represented in the top 30 list with MYR241.2 billion in LCY corporate bonds outstanding at the end of the review period.

LCY corporate bonds issued in Q2 2021 jumped 4.7% q-o-q to MYR45.2 billion from MYR43.2 billion in Q1 2021. The growth in Q2 2021 was a reversal from the decline of 25.8% q-o-q posted in the prior quarter. The expansion may be attributed to companies taking advantage of the low-interest-rate environment as BNM kept its overnight policy rate at 1.75% in July 2021 and the economy is expected to recover during the second half of the year.

In April, Infracap Resources, a special purpose vehicle of the Sarawak state government, issued a total of MYR5.8 billion of *sukuk murabahah*, an Islamic bond in which bondholders are entitled to a share of the revenues generated by the assets (**Table 3**). The issuance had 11 tranches with tenors ranging from 1 year to 15 years. Proceeds from the issuance will be used by the company to fund various Shariah-compliant purposes. Cagamas, the national mortgage corporation of Malaysia, issued three 2-year conventional medium-term notes during the quarter. A dual-tranche bond, both tranches with a coupon rate of 2.5%, was issued in May and its proceeds will be used in funding purchases from the financial system of housing loans. Cagamas' various Islamic medium-term notes were issued under its Medium-Term Note Programme. In May, Danainfra Nasional, which funds projects of the Government of Malaysia, issued five tranches of *sukuk murabahah* totaling MYR2.0 billion and with tenors ranging from 7 years to 30 years. Proceeds from this issuance will be used to fund Shariah-compliant expenses related to the Klang Valley Mass Rapid Transit Project.

Investor Profile

Foreign holdings of LCY government bonds in the Malaysian market rose throughout Q2 2021, with foreign investors holding MYR231.4 billion worth of LCY government bonds in April, MYR233.4 billion in May, and MYR233.8 billion in June (**Figure 2**). Net capital inflows into the bond market in April were MYR6.6 billion, declining to MYR2.0 billion and MYR0.4 billion in the succeeding 2 months. The tapered pace of buying from foreign investors may be attributed to investors' risk aversion due to the resurgence of COVID-19 infections in Malaysia and neighboring economies, which in turn lead the Government of Malaysia to institute again a nationwide Movement Control Order in June. Economic and political uncertainties contributed to foreigners' tepid enthusiasm for Malaysian government bonds. As a share of LCY government bonds, foreign holdings increased from 26.0% at the end of March to 26.6% at the end of April before gradually easing to 26.0% at the end of June.

At the end of March, investors in LCY government bonds were led by financial and social security institutions, holding 34.0% and 27.2% of the total, respectively (**Figure 3**). The holdings of financial institutions increased while those of social security institutions declined compared to the same month in 2020. The share of foreign holders increased to 25.6% during the review period from 21.8% a year prior. The holdings of insurance companies and BNM increased to 4.8% and 1.9% from 4.2% and 1.6%, respectively, between March 2020 and March 2021.

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	76.0	18.3	Yes	No	Finance
2.	Prasarana	37.0	8.9	Yes	No	Transport, Storage, and Communications
3.	Lembaga Pembiayaan Perumahan Sektor Awam	34.2	8.2	Yes	No	Property and Real Estate
4.	Cagamas	30.3	7.3	Yes	No	Finance
5.	Project Lebuhraya Usahasama	28.9	7.0	No	No	Transport, Storage, and Communications
6.	Urusharta Jamaah	27.3	6.6	Yes	No	Finance
7.	Perbadanan Tabung Pendidikan Tinggi Nasional	24.3	5.9	Yes	No	Finance
8.	Pengurusan Air	18.3	4.4	Yes	No	Energy, Gas, and Water
9.	CIMB Bank	13.4	3.2	Yes	No	Finance
10.	Maybank Islamic	13.0	3.1	No	Yes	Banking
11.	Malayan Banking	12.1	2.9	No	Yes	Banking
12.	Sarawak Energy	12.0	2.9	Yes	No	Energy, Gas, and Water
13.	Khazanah	11.9	2.9	Yes	No	Finance
14.	CIMB Group Holdings	11.6	2.8	Yes	No	Finance
15.	Tenaga Nasional	10.3	2.5	No	Yes	Energy, Gas, and Water
16.	Danga Capital	10.0	2.4	Yes	No	Finance
17.	Jimah East Power	8.9	2.2	Yes	No	Energy, Gas, and Water
18.	Danum Capital	8.4	2.0	No	No	Finance
19.	Public Bank	6.9	1.7	No	No	Banking
20.	Bank Pembangunan Malaysia	6.8	1.6	Yes	No	Banking
21.	Sapura TMC	6.4	1.5	No	No	Finance
22.	YTL Power International	6.1	1.5	No	Yes	Energy, Gas, and Water
23.	Bakun Hydro Power Generation	5.9	1.4	No	No	Energy, Gas, and Water
24.	Infracap Resources	5.8	1.4	Yes	No	Finance
25.	GOVCO Holdings	5.7	1.4	Yes	No	Finance
26.	Turus Pesawat	5.3	1.3	Yes	No	Transport, Storage, and Communications
27.	GENM Capital	5.3	1.3	No	No	Finance
28.	EDRA Energy	5.1	1.2	No	Yes	Energy, Gas, and Water
29.	1Malaysia Development	5.0	1.2	Yes	No	Finance
30.	Kuala Lumpur Kepong	4.6	1.1	No	Yes	Energy, Gas, and Water
Total Top 30 LCY Corporate Issuers		**456.4**	**110.0**			
Total LCY Corporate Bonds		**769.2**	**185.4**			
Top 30 as % of Total LCY Corporate Bonds		**59.3%**	**59.3%**			

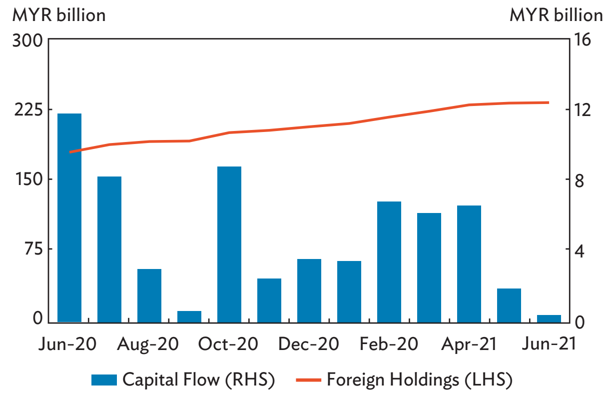
LCY = local currency, MYR = Malaysian ringgit, USD = United States dollar.
Notes:
1. Data as of 30 June 2021.
2. State-owned firms are defined as those in which the government has more than a 50% ownership stake.
Source: *AsianBondsOnline* calculations based on Bank Negara Malaysia Fully Automated System for Issuing/Tendering data.

Table 3: Notable Local Currency Corporate Bond Issuances in the Second Quarter of 2021

Corporate Issuers	Coupon Rate (%)	Issued Amount (MYR million)
Infracap Resources		
1-year *sukuk murabahah*	2.83	900
3-year *sukuk murabahah*	3.11	350
5-year *sukuk murabahah*	3.69	450
7-year *sukuk murabahah*	4.12	500
8-year *sukuk murabahah*	4.23	400
10-year *sukuk murabahah*	4.40	600
11-year *sukuk murabahah*	4.50	300
12-year *sukuk murabahah*	4.60	400
13-year *sukuk murabahah*	4.70	300
14-year *sukuk murabahah*	4.80	450
15-year *sukuk murabahah*	4.90	1,100
Cagamas		
2-year Islamic MTN	2.48	600
2-year Islamic MTN	2.41	200
2-year MTN	2.50	700
2-year MTN	2.50	800
2-year MTN	2.41	700
3-year Islamic MTN	2.78	400
5-year Islamic MTN	3.15	350
Danainfra Nasional		
7-year *sukuk murabahah*	3.25	300
15-year *sukuk murabahah*	4.10	400
20-year *sukuk murabahah*	4.47	400
25-year *sukuk murabahah*	4.56	400
30-year *sukuk murabahah*	4.64	500

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. Multiple issuances of the same tenor indicates issuance on different dates.
Source: Bank Negara Malaysia Bond Info Hub.

Figure 2: Foreign Holdings and Capital Flows in the Malaysian Local Currency Government Bond Market



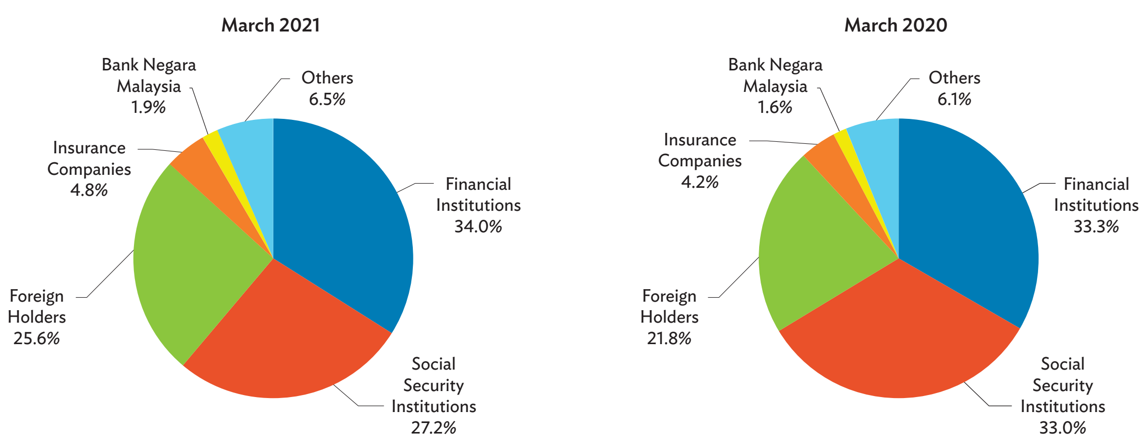
LHS = left-hand side, MYR = Malaysian ringgit, RHS = right-hand side.
Notes:
1. Figures exclude foreign holdings of Bank Negara Malaysia bills.
2. Month-on-month changes in foreign holdings of local currency government bonds were used as a proxy for bond flows.
Source: Based on data from Bloomberg LP.

Ratings Update

Rating and Investment Information Affirms Malaysia's Credit Rating with Stable Outlook

On 2 June, Rating and Investment Information affirmed Malaysia's A+ foreign and local currency issuer ratings with a stable outlook for both ratings. The affirmation came as the rating agency expects Malaysia's economy to recover this year supported by

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.

its relatively advanced diversified industries. R&I also viewed Malaysia's government debt ratio as manageable albeit at an elevated level. Finally, R&I affirmed the credit ratings due to the economy's external stability as evidenced by current account surpluses and ample international reserves.

S&P Global Ratings Affirms Malaysia's Credit Rating with Negative Outlook

On 22 June, S&P Global Ratings affirmed the foreign currency long-term issuer rating of A– for Malaysia with a negative outlook. The affirmation of the rating was attributed to Malaysia's strong external position, flexible monetary policy, and the government's track record of having the ability to sustain economic growth and demonstrating resiliency during economic downturns. The rating agency attributes the negative outlook to Malaysia's high fiscal deficit and debt ratio. A slow economic recovery and political uncertainties are seen to prevent the government's ability to consolidate its finances.

Fitch Ratings Affirms Malaysia's Credit Rating with Stable Outlook

On 18 July, Fitch Ratings affirmed the long-term foreign currency issuer default rating of Malaysia at BBB+, maintaining its stable outlook. The affirmation came as the rating agency sees the economy recovering in 2021 from the contraction recorded in 2020. Despite increased government debt due to expenses related to the COVID-19 response, Malaysia's debt ratio is expected to decline starting in 2022. Fitch Ratings also sees a gradual reduction in the fiscal deficit. Supporting the affirmation are Malaysia's consistent annual current account surplus and the central bank's monetary policy, which the rating agency views as supportive of economic activities.

Policy, Institutional, and Regulatory Developments

Bank Negara Malaysia and Bank Indonesia Expand Local Currency Settlement Framework

On 2 August, BNM and Bank Indonesia expanded their LCY settlement framework. The framework aims to encourage investors to use Malaysian ringgit and Indonesian rupiah in settlements of financial transactions between the two economies. Aside from trade settlement, the expanded framework included in its list of eligible transactions direct investments, income, and transfer settlements. Individuals were included in the expanded framework's eligible users. Its foreign exchange policy has also been streamlined to attract more investors. With the expanded framework, the central banks of Malaysia and Indonesia included in their list more qualified banks that are allowed to execute the framework.

Bank Negara Malaysia Revises Reference Rate Framework

On 11 August, BNM released its revised Reference Rate Framework, effective 1 August 2022. In the revised version, all financial institutions will use a common rate, the standardized base rate, as the reference rate for new issuances of floating-rate notes and refinancing of existing loans in Malaysia. This replaces the current use of a base rate that differs across financial institutions. Furthermore, the standardized base rate will be linked to the overnight policy rate. The revision allows consumers to understand better the changes in their loan repayments. This will also facilitate the transmission of the policy rate to the broader economy.