



# The Anatomy of Local Bond Markets in Emerging Market Economies - Sharing Malaysia's Experience



**Rahamat Bivi Yusoff**  
**Under Secretary**  
**Ministry of Finance, Malaysia**  
**9 May 2007**

# Agenda

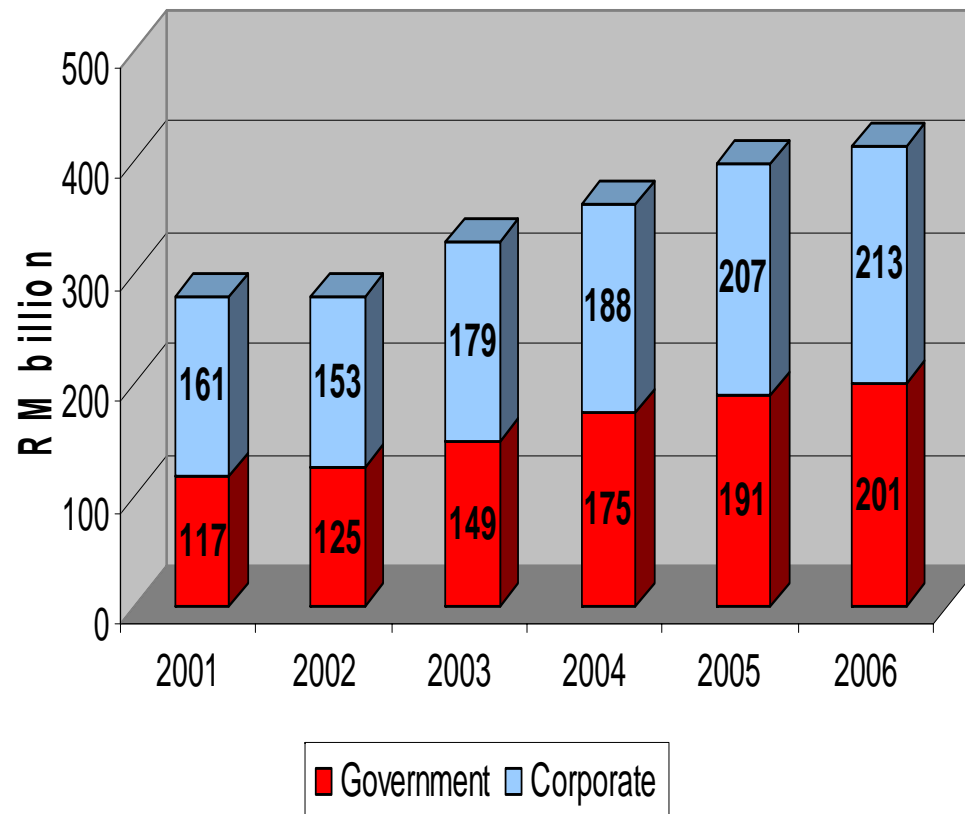


- **Overview of Malaysian Bond Market**
- Policy Direction Post-Financial Crisis
- Recent Initiatives
- Future Challenges

# Robust Growth in Malaysian Bond Market



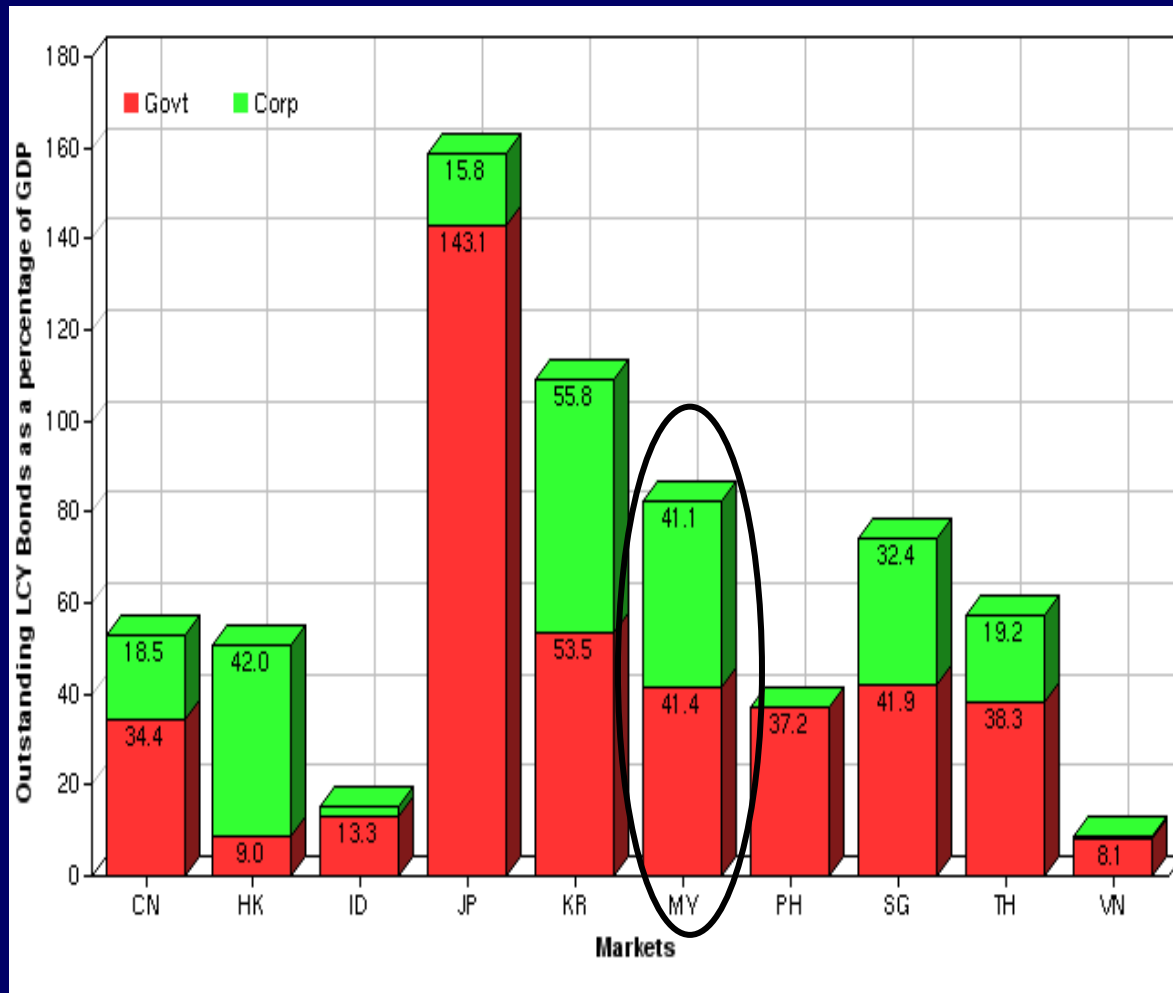
Total bonds outstanding



As at end December 2006,

- Outstanding size of bond market increased to RM416 bln (USD122 bln) from RM157 bln at end-1998
- Local currency corporate bond market is currently 3rd largest in Asia (ex. Japan)
- Corporate bonds comprised more than half of total bonds outstanding

# In Line with Regional Development



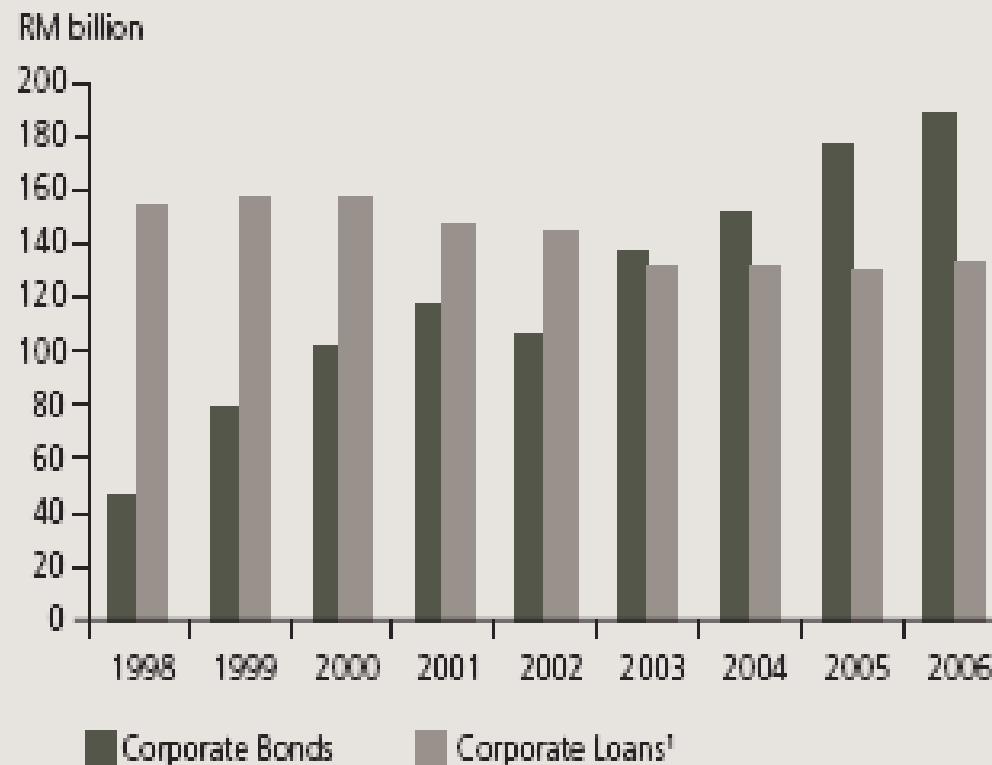
Source : ADB

- Asia's bond market has reached USD\$2.8 trillion in 2006
- Ex-Japan, bond markets in Asia constituted 60% of GDP
- Corporate bond markets are significant relative to government bond markets

# Sustainable Corporate Bond Issues



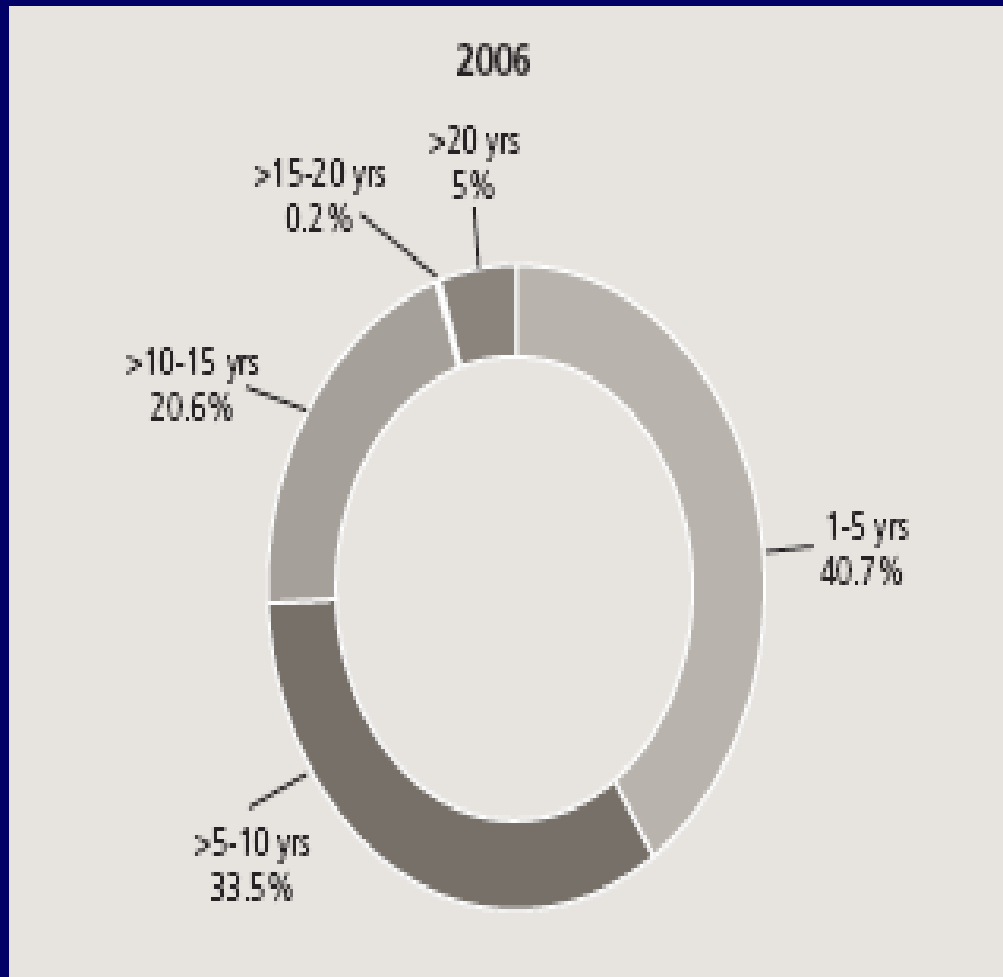
Size of Corporate Bonds Market against Corporate Loans<sup>1</sup>



<sup>1</sup> Excludes loans to small and medium enterprises

- **Corporate bonds as percentage of total corporate financing increased from 21.2% in 1998 to 57.8% in 2006**
- **Represents a significant source of long-term financing for private sector**
- **Contributed to addressing maturity mismatches in private sector financing**

# Deepening in Corporate Bond Market



- **More than 50% of total corporate bond issuances had maturities of more than 5 years**
- **26% of corporate bond issues with more than 10-year tenor mostly to finance infrastructure and utilities projects**

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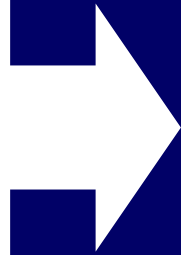


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# Policy Direction after 1997 Crisis



NEAC :  
Develop  
Corporate  
Bond  
Market



**National Bond Market Committee**  
(1999)

**Bond market-specific  
mandate to focus  
attention & effort:**

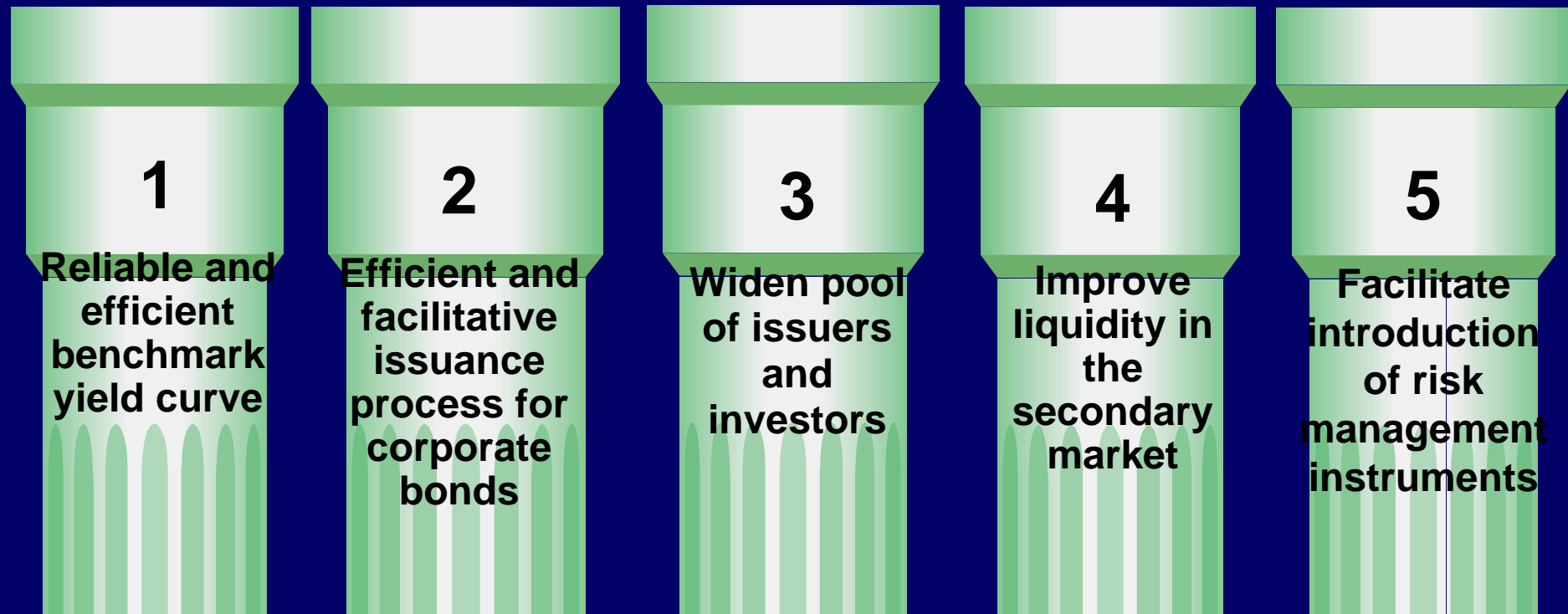
1. Overall policy direction for orderly development
2. Study development issues
3. Identify and recommend implementation strategies

**Inter-agency  
membership to ease  
implementation:**

- MOF
- BNM
- SC
- Economic Planning Unit
- Bursa M'sia
- EPF
- Private sector

***Critical factors  
for successful  
implementation***

# Establishing Robust & Efficient Market



**Priority** : Centralise regulation of corporate bond market

**Action** : Securities Commission as sole regulator w.e.f. 1 July 2000

# Proactive Role of Government & Regulatory Bodies



## Ministry of Finance



- Co-ordinate developmental efforts of Government agencies (under the National Bond Market Committee)
- Grant tax incentives – stamp duty exemption for primary and secondary market transactions, withholding tax for non-residents, real property gains tax for asset-backed securities and etc

## Bank Negara Malaysia



- Manage public debt and MGS issuance
- Own and operate FAST, RENTAS and BIDS

## Securities Commission



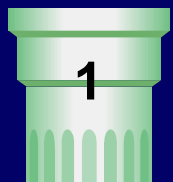
- **Sole approving authority for corporate bond issuance**
- **Regulates secondary bond market activities**

# Proper Sequencing of Developmental Initiatives



- Malaysian bond market is supported by sound infrastructure and institutions established prior to 1997:
  - National mortgage corporation (Cagamas)
  - Domestic rating agencies
  - Primary dealer system
  - Institutional investors (e.g. insurance companies, unit trust and fund managers)
  - Funds transfer and scripless book-entry system (RENTAS)
  - Electronic tendering system (FAST)
  - Bond information and dissemination system (BIDS)

# Significant Progress has been made

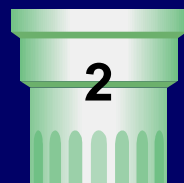


## Benchmark yield curve

Introduction of auction calendar for Malaysian Government Securities (MGS)

Review of principal dealers system

Introduction of MGS15 and MGS20



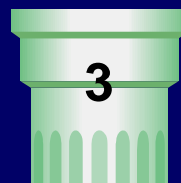
## Issuance process

PDS and ABS Guidelines (revised July 2004)

Shelf regulation scheme (issued July 2000)

Structured Products Guidelines (issued Dec 2003)

Islamic Securities Guidelines (issued July 2004)



## Issuers & investors

Broadening of investors base for OTC market since July 2000

Facilitative framework for ringgit bonds issued by MDBs, MFIs, foreign govts, and quasi-govt agencies



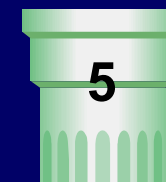
## Liquidity

Non-FIs allowed to conduct repo

Guidelines on Securities Borrowing and Lending Programme

Introduction of on-line Institutional Securities Custodian Program (ISCAP)

Withholding tax exemption for non-residents



## Hedging instruments

Introduction of 3, 5 and 10 years MGS Futures

# Agenda



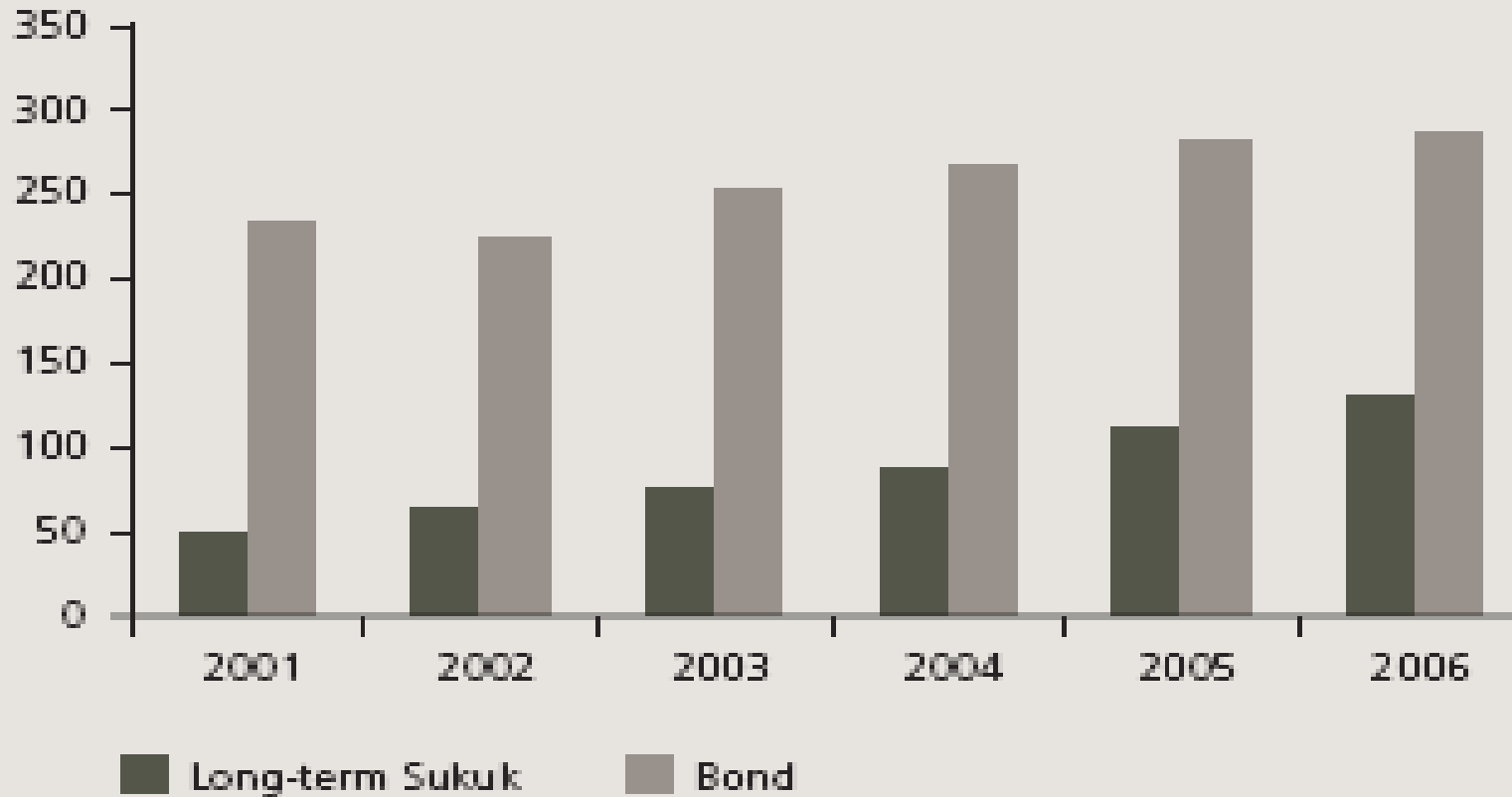
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# Rapid Growth in Sukuk (Islamic Bonds) Issuance



## Outstanding Long-term Sukuk vs. Bond

RM billion



# Features of Sukuk



- Structured under approved Syariah principles
- Profit rate (interest prohibited)
- Utilisation of proceeds for halal purposes
- Hybrid structures possible (profit and risk sharing)
- Syariah adviser

# Key Developmental Objective



## **Malaysian bond market to comprise of both Islamic & conventional bonds**

- Widen range of products in bond market
- Enlarge pool of investors, including participation of international investors

# Promoting Sukuk



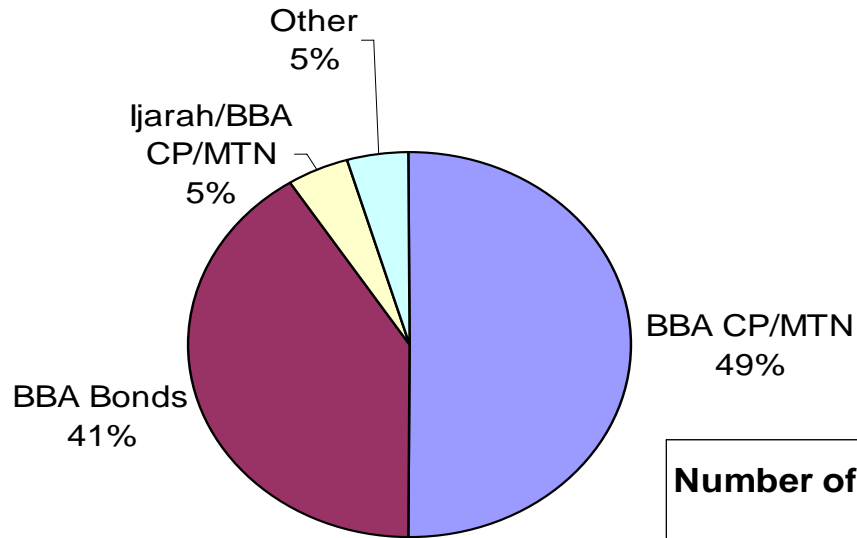
## **Government commitment**

- Part of wider government initiative to develop Malaysia as international hub of Islamic financing
- Tax incentives for issuer
- Tax incentives for specific products
- Malaysian sovereign sukuk

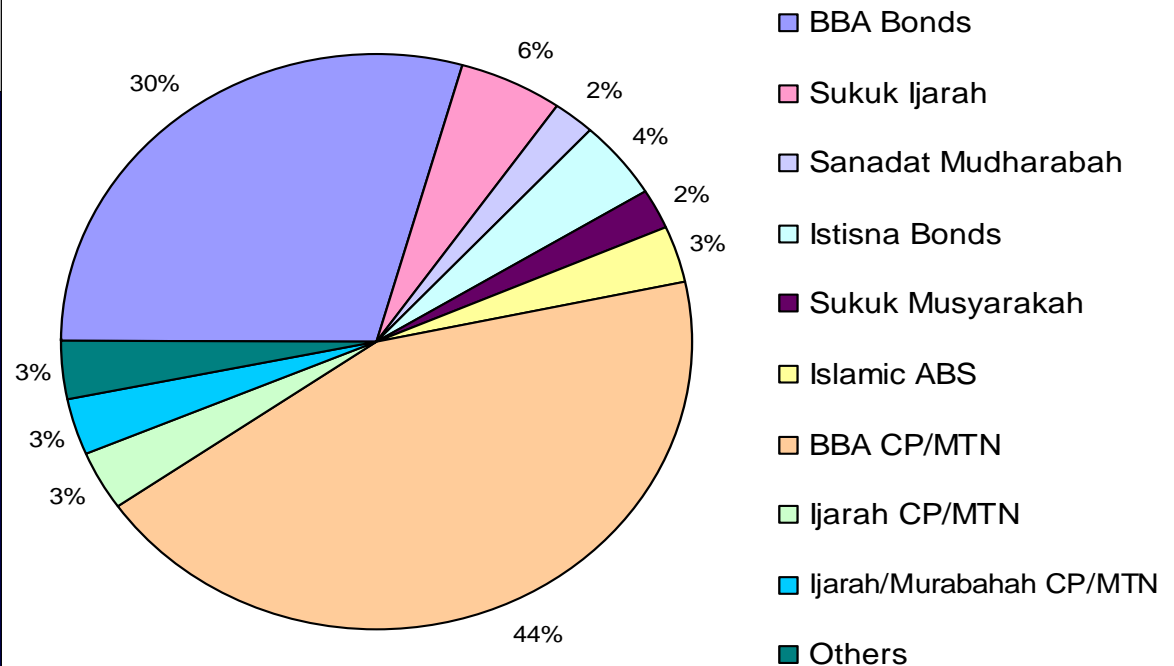
**Sets pace for market growth  
& product innovation**

# Product Innovation in Sukuk Issuances

**Number of Islamic securities issued (by %)  
Jan '03 - June '04**



**Number of Islamic securities issued (by %)  
July '04 - Dec '05**



Marked increase in range of Islamic bonds issued after Islamic Securities Guidelines released in July 2004.

# Facilitating Entry of International Issuers



MDB	ADB	IFC	IBRD	ADB	KfW
Issue date	10 Nov 04	10 Dec 04	12 May 05	25 Apr 06	11 May 06 24 Jan 07
Size	RM400 m	RM500 m	RM760 m	RM3.8 b	RM2.5 b
Type	<b>Fixed Rate Bonds</b>	<b>Islamic Bonds</b>	<b>Islamic Bonds</b>	<b>Medium Term Notes</b>	<b>Fixed Rate /MTN</b>
Tenor	5 yrs	3 yrs	5 yrs	15 yrs (programme)	7 yrs / 10-yr programme
Rating	AAA	AAA	AAA	AAA	AAA

Six RM-denominated bond issues/programmes with a total value of RM7.6 billion have been launched to date

# Origination of Foreign Currency-Denominated Bonds in Malaysia



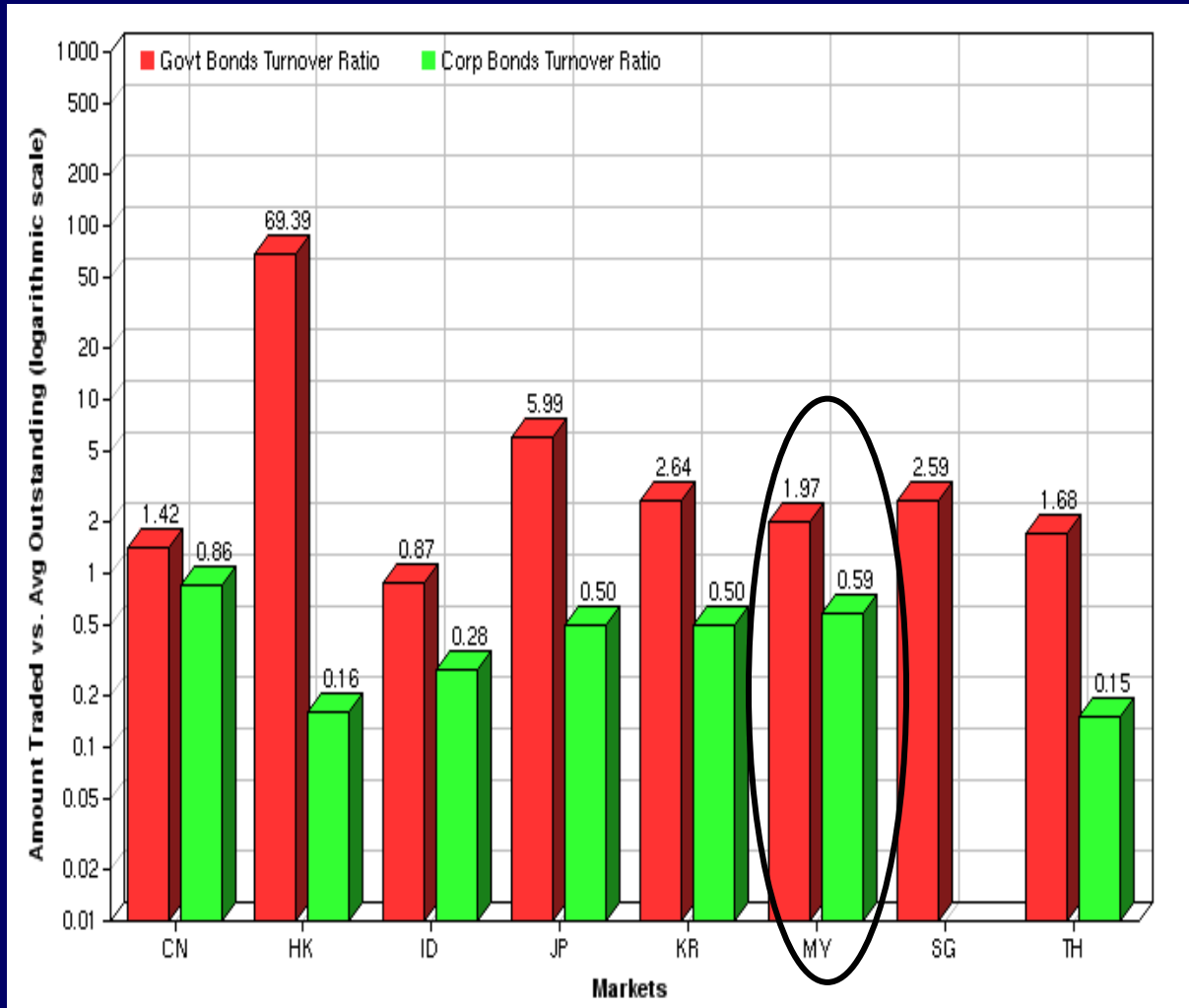
- Eligible Issuers:
  - Multilaterals
  - Sovereigns
  - Quasi-sovereigns
  - MNCs (including domestic MNCs that have natural hedge on currency exposures)
- International documentation acceptable
- Deemed approval for min A-rated issues
- Withholding tax exemption if structured as sukuk issue

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# Liquidity in Secondary Markets



Source : ADB

- Liquidity is relatively low due to (i) buy-and-hold strategy among domestic investors and (ii) size of each issue remains small by international standards
- Trading of corporate bonds is rather active by regional standards
- Government efforts to enhance investors base, including withholding tax exemption to attract foreign investment

# Future of Malaysian Bond Market



- Challenge for bond market to constantly evolving with new products:
  - Sukuk
  - Bond issuances by multilateral development banks, foreign governments, agencies of foreign governments and MNCs
  - Foreign currency-denominated bonds and sukuk
  
- Recent foreign exchange liberalisation will lead to more open and competitive market place:
  - Promote robust participation by issuers and investors in non-RM bonds
  - Facilitate integration of Asian bond markets as envisaged under the Asian Bond Markets Initiative (ABMI)
  - Position Malaysia as an attractive and competitive investment destination for sukuk and foreign currency-denominated bonds



The End