

Bond Market Development in Malaysia

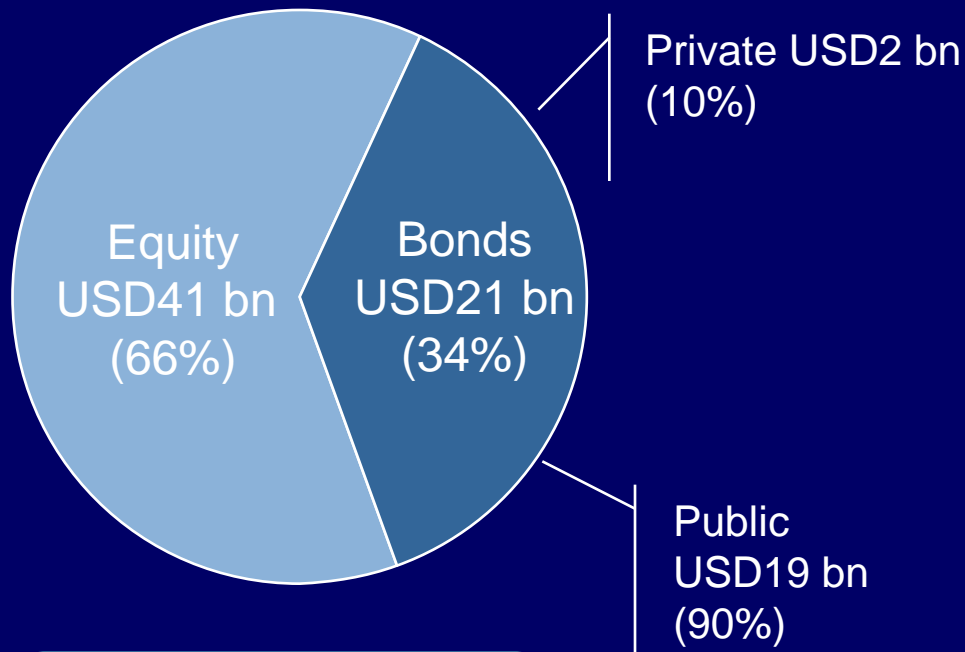
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- Background
- Bond Market Developmental Initiatives Post Financial Crisis
- Current State of the Malaysian Bond Market
- Continuous Enhancement of Regulatory Environment

Malaysia's capital market in the 1990s was not well diversified...

Total size of capital market
1990 – USD62 bn

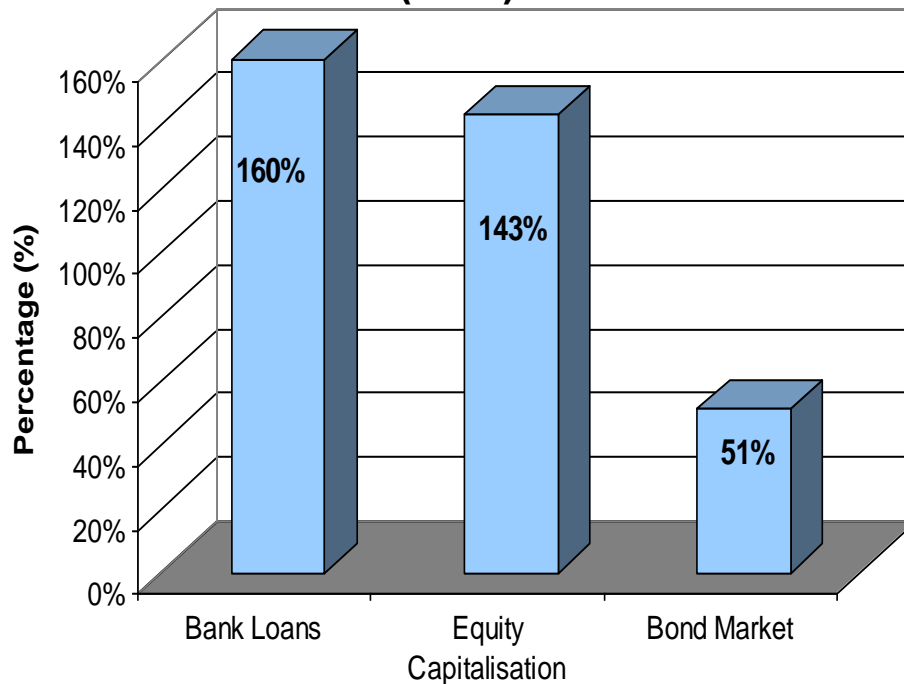


Banking sector assets:
USD36 billion

- From mid-1992, heavy speculative inflows in search of Ringgit assets - well in excess of supply and resulted in asset price inflation
- High liquidity with bank loans growing rapidly
- Availability of external financing which corporates tapped into for infrastructure projects
- Current account turned into deficit

...and was exposed to vulnerabilities

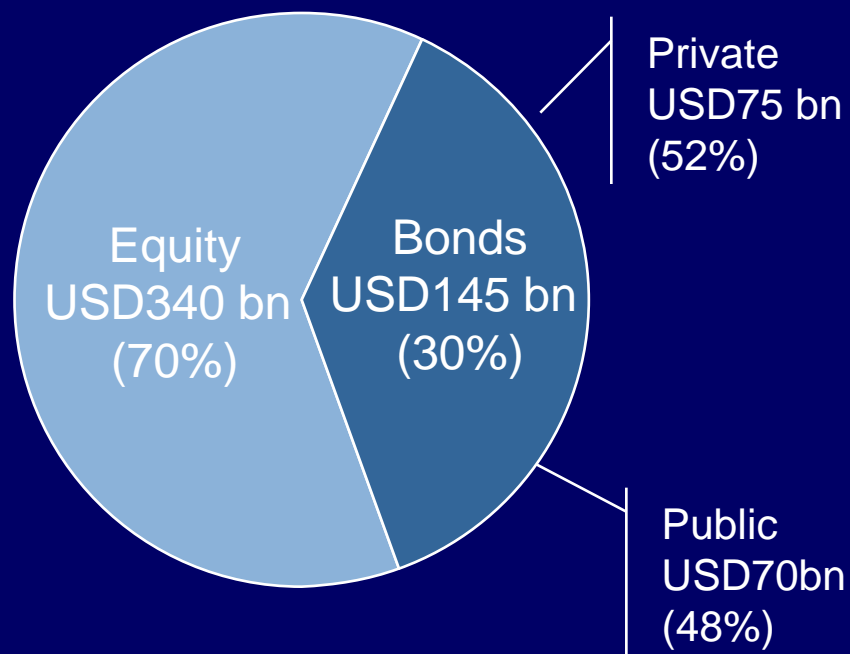
**Outstanding amounts as a % of GDP
(1997)**



- An under-developed bond market meant a lack of an alternative avenue to obtain funding
- Overdependence on bank financing led to maturity mismatches
- Capital market became vulnerable to sudden outflow of funds
- Combination of the above led to the onset of the 1997 financial crisis

Today strong foundations are in place

Total size of capital market
Dec 2007 – USD485 billion



Banking sector assets:
USD202 billion

- Holistic approach to develop capital market through the Capital Market MasterPlan (CMP) – implemented 85% of 152 recommendations
- Strengthen corporate governance and investor protection
- Consolidation of financial institutions, strengthening of balance sheets, prudential and compliance systems
- Diversification in sources of financing
- Bond market has emerged as a viable and cost efficient source of funding
- Development of investment management industry

The Asian financial crisis provided an impetus for urgent efforts to develop the bond market

National Economic Recovery Plan (August 1998)

“The National Economic Recovery Plan has identified that the over-dependence on the banking sector for much of the long-term funding needs for corporate growth and expansion has been a contributory factor to the 1997 crisis. Therefore, it becomes crucial that the Ringgit corporate bond market be developed in order to be able to cater to the financing needs of the private sector”

National Bond Market Committee (June 1999)

- Provided overall policy direction for orderly development of corporate bond market
- Studied developmental issues
- Identified and recommended appropriate developmental strategies to be implemented
- Public and private sector collaboration crucial factor in effecting implementation of strategies

Securities Commission: (July 2000)

- Sole regulator of the capital market including sole approving authority for corporate bonds
- Formulates regulatory framework governing corporate bond market
- Supervises secondary bond market trading activities
- Supervises bond market intermediaries

5 key pillars were identified for further development...

The 5 Pillars

1.

Establish
reliable and
efficient
benchmark
yield curve

2.

Introduce
efficient &
facilitative
issuance
process for
corporate
bonds

3.

Widen
issuers and
investors
base

4.

Improve
liquidity in the
secondary
market

5.

Facilitate
introduction of
risk management
instruments

Priority actions

1. Enhance use of Malaysian Government Securities as benchmark
2. Broadening the issuer and investor base
3. Tax incentives to spur growth of bond market

Capital Market Master Plan (CMP)

152 capital market recommendations

- The CMP advocates 17 recommendations for the bond market
- ***15 recommendations have been implemented***
- Recommendations for the bond market that have been implemented include:
 - Framework for ABS market
 - Framework to encourage MDBs, MFIs and MNCs to issue Ringgit bonds
 - Full disclosure based framework
 - Facilitating retail participation in the bond market via bond funds
 - Strengthened the tax framework to encourage issuance and investment in bonds

Phase 1
(2001-2003)

Strengthen domestic capacity

Phase 2
(2004-2005)

Gradual liberalisation of market
access

Phase 3
(2006-2010)

Enhance international
positioning

A facilitative approval process for corporate bonds is now in place

- Disclosure based corporate bond submissions
- Facilitative approval timeframe: 14 and 28 working days for corporate bonds and ABS issues respectively
- Rating required, but no minimum investment grade imposed for bond approval
- Adequate disclosure required such as stringent due diligence for investor protection

With easy access to bond market information for investors

- Availability of bond issuer documentation on SC's website for investors to make informed investment decisions:
 - Principal terms and conditions;
 - Information memorandum; and
 - Trust deed
- Promote continuous post-issuance disclosure by issuers, advisers, credit rating agencies and trustees
- Availability of fair value prices of all Ringgit bonds provided by bond pricing agency

A recognition system for credit rating agencies

- Practice Note on Recognition of CRAs by the SC for the Purpose of Rating Bond Issues (January 2006)
 - Recognition criteria are in line with the principles set out in the IOSCO CRA Code
- The recognition system seeks to ensure that CRAs:
 - Exercise high standards of professionalism and due diligence in rating and monitoring corporate bonds
 - Provide adequate and timely dissemination of rating information

A registration system for bond trustees and bond pricing agencies

Bond Trustees:

- Practice Note on Registration by the SC for the Purpose of Acting as a Bond Trustee (October 2006)
- The registration system seeks to ensure that bond trustees:
 - Exercise high standards of professionalism that translates into greater protection for investors
 - Maintain their independence and avoid of conflicts of interest

Bond Pricing Agencies:

- Guidelines on the Registration of BPA (January 2006)
 - Registration criteria: independence, adequate expertise, fit and proper requirements for directors and management
- A BPA contributes to market liquidity by:
 - Providing independent and objective fair value for bonds
 - Facilitating mark-to-market valuation of bond portfolios

Intermediary supervision

- Supervise credit rating agencies, bond trustees and bond pricing agencies to ensure compliance with relevant guidelines, registration criteria etc.
- Supervisory functions are conducted on-site and off-site

Market surveillance

- Detect market abuses and deter misconduct in the primary and secondary bond market activities, leading to:
 - ✓ Increased investor protection;
 - ✓ Increased market integrity;
 - ✓ Higher investor confidence; and
 - ✓ Higher standards of professionalism among market participants.

Significant progress has been made

1

Benchmark yield curve

Introduction of auction calendar for Malaysian Government Securities (MGS)

Review of principal dealers system

Introduction of MGS15 and MGS20

2

Issuance process

PDS and ABS Guidelines

Islamic Securities Guidelines

Structured Products Guidelines

3

Issuers & investors

Broadening of investors base for OTC market since July 2000

Facilitative framework for Ringgit & foreign currency denominated bonds issued by MDBs, MFIs, foreign govts, quasi-govt agencies & MNCs

4

Liquidity

Non-FIs allowed to conduct repo

Guidelines on Securities Borrowing and Lending Programme

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

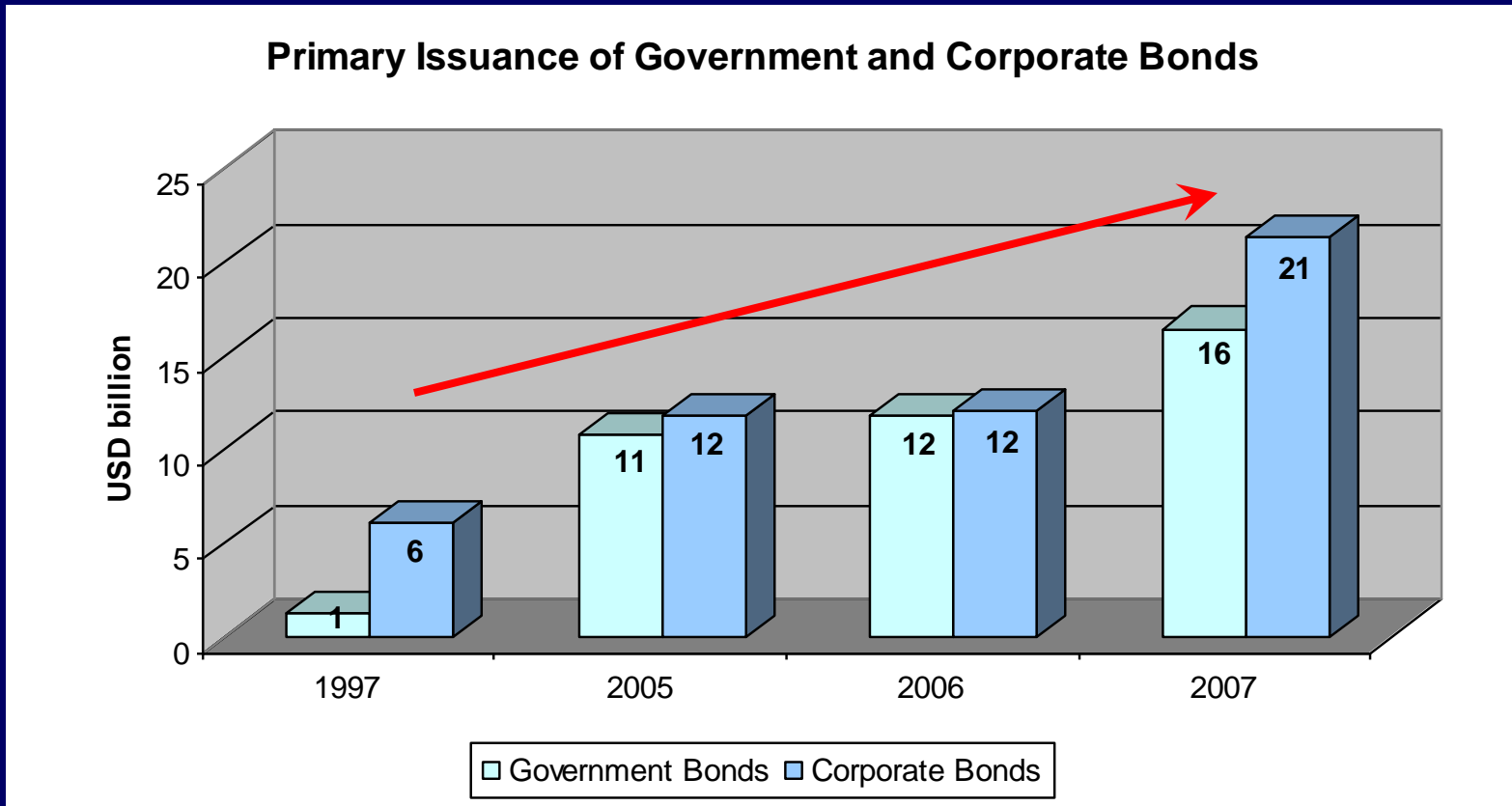
Withholding tax exemption & other tax incentives

5

Hedging instruments

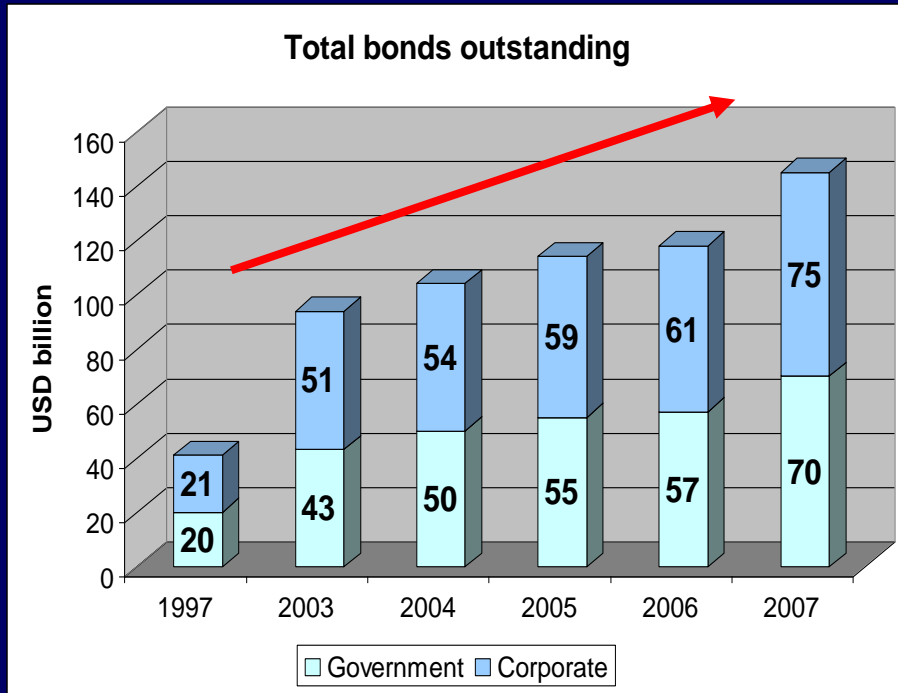
Introduction of 3, 5 and 10 years MGS Futures

Remarkable growth in bond issuances ...

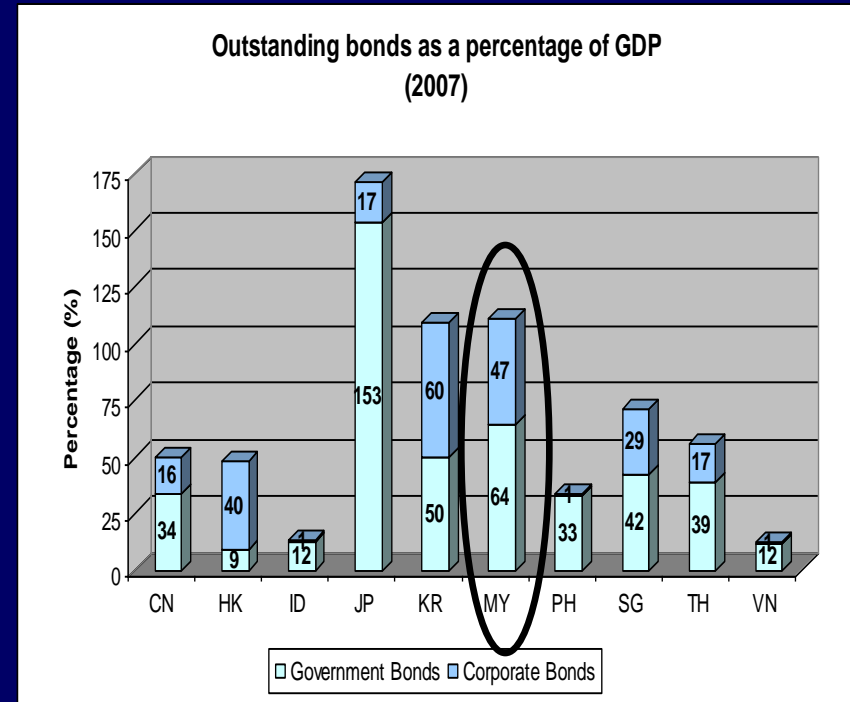


- Record year in 2007 for new issuance of corporate bonds
- Bond market is increasingly becoming a very important source of funding for corporate sector

... leading to a strong growth of the bond market



Source: BNM



Source: ADB

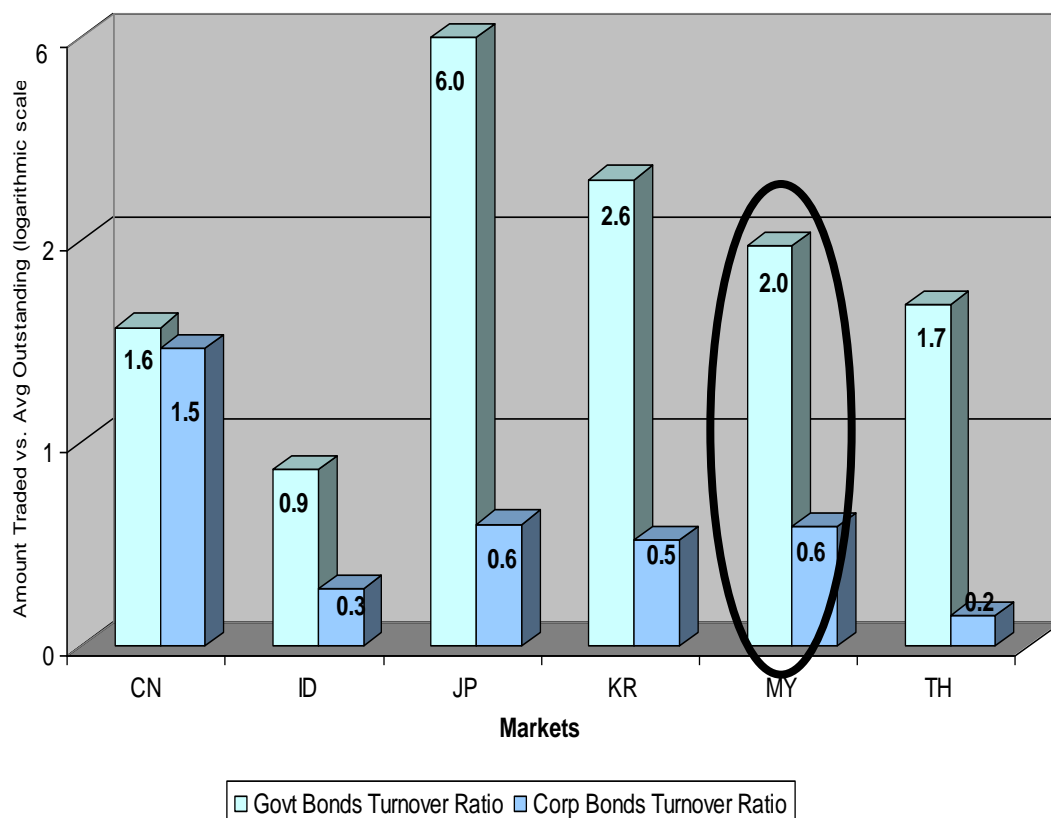
- Outstanding bonds reached USD145 billion as at end-2007
- 52% of outstanding bonds are corporate bonds while 48% are government issues
- Islamic bonds (Sukuk) accounted for 36% and 56% of total outstanding bonds and corporate bonds respectively

- Ringgit bond market is the 2nd largest in Asia* relative to its size of GDP at end-2007
- In terms of size, Ringgit bond market is the 4th largest in Asia

*Includes securities with maturities of less than one year

Liquidity in secondary market is healthy

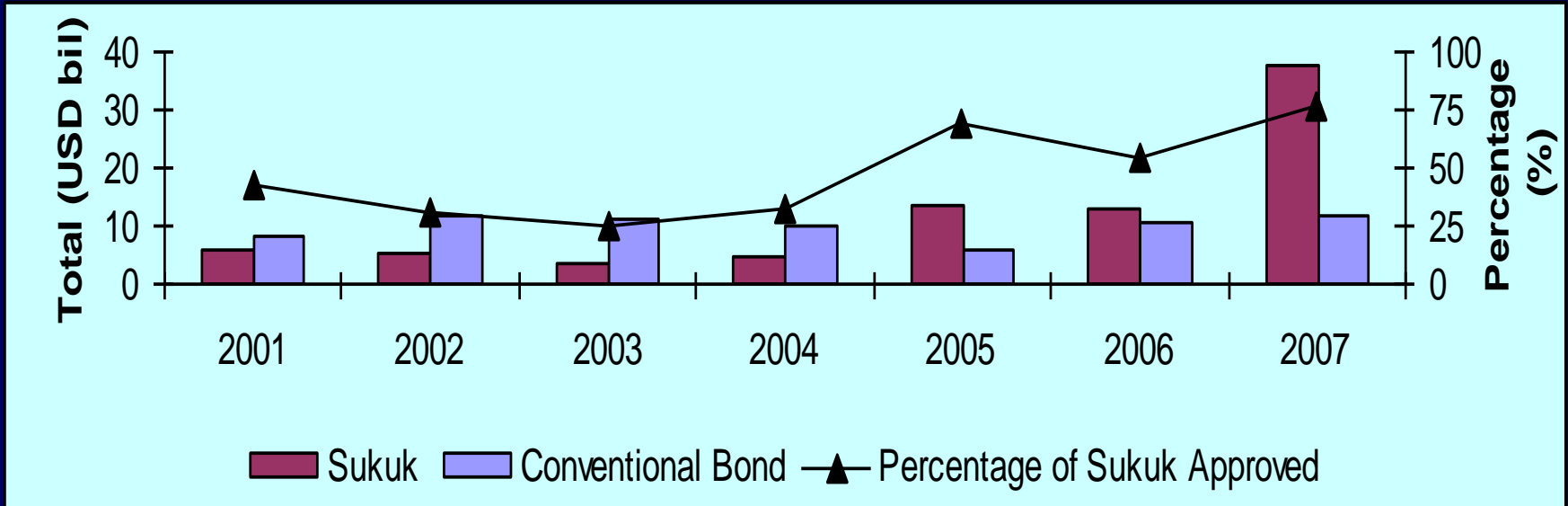
Liquidity in selected ASEAN + 3 nations
(2007)



- Liquidity relatively high by regional standards
- Significant increase in foreign shareholdings
- Inclusion in major bond indices (e.g. Citibank World Government Bond Index) has contributed to increased liquidity

Source : ADB

Preference for Islamic issues to tap wider investor base



Year	Sukuk (USD bil)	Conventional Bond (USD bil)	% of Sukuk Approved by SC
2001	5.8	8.2	42%
2002	5.4	11.8	31%
2003	3.7	10.9	25%
2004	4.7	10.1	32%
2005	13.4	6.0	69%
2006	13.0	10.4	55%
2007	37.5	11.6	76%

- Malaysia is a leader in sukuk issuance...
 - Malaysia accounts for more than 60% of global outstanding sukuk
 - Issued the world's first global sukuk worth US\$150 million in 2001 (Guthrie Berhad)
 - Issued the world's first global sovereign sukuk worth US\$600 million in 2002 (Government of Malaysia)
 - Issued the world's first exchangeable sukuk worth US\$750 million in 2006 (Khazanah Nasional Berhad)
 - Issued the world's largest sukuk in 2007 worth US\$4.7 billion (Binariang GSM Sdn Bhd)
- Increase preference for sukuk due to strong investor demand
 - As at end-2007, 36% and 56% of total outstanding government and corporate bonds respectively are Shariah-compliant

With an established domestic issuer/investor base, greater diversity is now being pursued

- Facilitative approval process for issuance of Ringgit denominated bonds:
 - Deemed approval granted to sovereigns, quasi-sovereigns, MDBs & MFIs rated “AAA”
 - 14 working days for foreign MNCs and foreign corporations
- Facilitative approval process for issuance of foreign currency denominated bonds:
 - Deemed approval granted to sovereigns, quasi-sovereigns, MDBs, MFIs and foreign MNCs rated “A-” on foreign rating scale
 - Governing laws of Malaysia, England or United States may be used for bond documentation

Issuance of Ringgit Bonds /Sukuk by Foreign Entities in Malaysia to Date:

Issuer	Summary of Issuances			
	Size of Issuance (equivalent in USD)	Subscription Rate	Allocation	Date of Issuance
Asian Development Bank (ADB)	USD123 million bonds	6.5 x	Non-resident: 34% Resident : 66%	10 Nov 2004
International Finance Corporation (IFC)	USD154 million Islamic bonds	4.3 x	Non-resident : 30% Resident : 70%	13 Dec 2004
International Bank for Reconstruction & Development (IBRD)	USD235 million Islamic bonds	1.9 x	Non-resident : 6.5% Resident : 93.5%	12 May 2005
ADB	USD154 million MTNs	2.15 x	Non-resident : 16% Resident : 84%	25 April 2006
KfW Bankengruppe of Germany (KfW)	USD154 million bonds	1.2 x	Non-resident : 15% Resident : 85%	11 May 2006
KfW	USD185 million MTNs	Private placement	Resident : 100%	24 Jan 2007
ADB	USD154 million MTNs	Private placement	Resident : 100%	8 Feb 2007
Gulf Investment Corporation	USD185 million bonds	3.7x	Non-resident: 10% Resident: 90%	5 Feb 2008
	USD123 million bonds	1.3x		
Total	USD1,467 million			

Note: 1USD = RM3.24

- (1) Further liberalisation measures planned for Ringgit and foreign currency denominated bond issuance:
 - ✓ To further liberalise issuer eligibility criteria for Ringgit and foreign currency denominated bond issuance

- (2) Introduction of electronic information dissemination and trading system in 2008
 - ✓ Real time dissemination of pre and post trade information
 - ✓ Improve price transparency and discovery
 - ✓ Facilitate bond market surveillance

For further information on the Malaysian Bond Market ...

Please visit the following websites:

<http://www.sc.com.my> (Securities Commission Malaysia)

<http://www.bnm.gov.my> (Bank Negara Malaysia)

<https://fast.bnm.gov.my/fastweb> (Fully Automated System for Issuing/Tendering)

<http://rmbond.bnm.gov.my> (Ringgit Bond Market)