Diversification to spur bond market

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MARKETS

Monday, 02 Dec 2024

BPAM chief executive officer Meor Amri Meor Ayob

PETALING JAYA: The Malaysian bond market is set to get a boost and attract more foreign investor participation in the debt market, thanks to Bank Negara's move to allow multilateral development banks (MDBs) and foreign development financial institutions (DFIs) to issue ringgit-denominated bonds.

Experts agree that this move would further spur foreign investors participation and liquidity into the local bond market.

Bond Pricing Agency Malaysia chief executive officer Meor Amri Meor Ayob told StarBiz allowing MDBs and foreign DFIs to issue ringgit-denominated bonds introduces high-quality issuers into the domestic bond market.

This will improve liquidity and broaden the investor base of the ringgit bond market, he noted.

"For international investors, the inclusion of MDB and foreign DFI bonds offers a new class of high-grade securities, potentially reducing reliance on government bonds or local corporate issuances. This diversification could enhance portfolio returns and risk management.

"Besides, when global institutions like MDBs and foreign DFIs participate in the ringgit bond market, it signals confidence in the domestic financial system as well as the Malaysian ringgit.

"Ultimately, the ringgit financing provided by MDBs and foreign DFIs to resident corporates could be channelled into high-value investment projects, such as the electrical and electronics industry, technology adoption, data centres and sustainable development projects.

"These key growth areas often require affordable financing, which MDBs and DFIs are well-suited to provide," he said.

Furthermore, Meor Amri said the move by the central bank to allow MDBs and foreign DFIs to issue ringgit-denominated debt securities is likely to spur foreign participation in the local bond market, especially in the Malaysian Government Securities (MGS) segment.

Any increased participation from MDBs and foreign DFIs could signal confidence in Malaysia's financial system and capital market, indirectly benefiting MGS, he said.

RAM Rating Services Bhd economist Nadia Mazlan

Apart from spurring foreign participation in the local bond market, RAM Rating Services Bhd economist Nadia Mazlan said issuances from these new entrants (MDBs and foreign DFIs) should help broaden the range of high-quality issuers, in turn contributing to an improvement in market depth and liquidity while also enhancing supply diversity.

“The presence of MDBs and foreign DFIs may elevate investor confidence and increase the appeal of the Malaysian bond market to a broader spectrum of issuers and investors.

“Over time, this liberalisation could foster a more vibrant and diversified financial ecosystem, which in turn, will further increase the attraction of the local market to foreign investors,” Nadia noted.

As the MDBs and non-resident DFIs would issue corporate bonds, she expects to see more foreign participation in this segment.

However, she said this market liberalisation could generate some spillover interest in MGS as the more dynamic market and heightened awareness of investment opportunities in Malaysia may spur foreign investor interest in a diversified range of instruments.

The preference for long-dated or short-dated bonds would likely depend on investors’ risk appetites and portfolio strategies, Nadia said.

OCBC Bank (M) Bhd head of global markets Stantley Tan

OCBC Bank (M) Bhd head of global markets Stantley Tan thinks that the impact to the local bond market would more likely be on an indirect basis, as the funding raised by MDBs and foreign DFIs via ringgit bond issuances are to be channelled to real economic activities only.

“However, a more diverse and distributed lender base may free up local lenders’ balance sheets enabling greater appetite and participation in the fixed income market.

“This effect may benefit the longer duration securities more than shorter ones, as the front end of the yield curve is relatively more sensitive to policy rates and an uncertain inflationary outlook,” he said.

MARC Ratings Bhd chief economist Ray Choy

MARC Ratings Bhd chief economist Ray Choy said for now, foreign participation would be focused on government bonds, with opportunities in the corporate bond market contingent on achieving substantial improvements in market liquidity over time.

As at October 2024, foreign holdings in government bonds stood at 21.7% (2023: 23%), below the pre-Covid-19 pandemic average of 29.2%. Although foreign holdings in MGS remain significantly lower than the peak of 39.4% in 2014, they are still among the highest in Asean, reflecting strong foreign interest in Malaysia's government bond market.

Foreign participation in corporate bonds also presents significant growth potential, with foreign holdings currently at 1.5% (2023: 1.5%), below the pre-pandemic average of 2.5%.

Choy said further efforts through such policies like allowing MDBs and foreign DFIs to issue ringgit-denominated bonds should be taken to strengthen links with global capital markets, and Malaysia has opportunities to further leverage on proximity to global financial centres such as Hong Kong and Singapore.

On the outlook of the ringgit bond market, Choy said: "The ringgit bond market remained resilient in 2024, with yields holding steady despite global market volatility, and bond issuance aligning with expectations. The outlook for 2025 appears positive, supported by strong economic fundamentals and stable inflation.

"The expected reduction in the fiscal deficit over the next few years will ease elevated debt levels, helping to maintain low yields.

"Additionally, while external risks such as United States trade policy can cause ringgit volatility, global interest rates are on their way down, even if the magnitude may be less than initially expected," he added.

MGS issuance is expected to record RM173bil in 2024 and decline to RM167bil in 2025, reflecting a lower budget deficit, he said. Corporate bond issuance is projected to increase from RM129bil in 2024 to RM133bil in 2025, in tandem with rising gross domestic product growth, the ongoing investment upcycle and stable credit market environment, Choy said.

Tan said the bank has a constructive outlook on the ringgit bond market for 2025. The global hiking cycle is behind us, removing a major headwind for bond markets in general, he said.

More importantly, he said the government seems highly committed to continue fiscal consolidation within their mandated term, which should bode well for MGS.

"Headwinds to watch out for going into 2025 are mainly inflation risks – on the domestic front, fiscal policies may lead to price pressures, while externally, there remain uncertainties on president-elect Donald Trump's policies when he takes office, which could drive a fresh round of global inflationary pressure," Tan noted.

Nadia said bond market activity has been robust this year. MGS and government investment issues (GII) totalled RM165.2bil as of October 2024 and is expected to clock in closer to the upper end of the rating agency's forecast range of RM170bil to RM180bil by year-end (2023: 190.9bil), according to RAM Ratings.

"For 2025, we project a slightly lower issuance range of RM155bil to RM165bil in MGS and GII issuance. This takes into account the narrower fiscal deficit which is in line with the government's commitment to fiscal consolidation and more moderate refinancing needs next year.

"For corporate bond issuance, we expect some of this year's strength to spillover into next year, with corporate bond issuance likely to remain in the range of RM110bil to RM120bil in 2025. Additionally, infrastructure financing and businesses' funding needs should underpin steady corporate bond issuance activity, Nadia said.

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