

MALAYSIAN RATING CORPORATION BERHAD
01480101

JULY 2014

Monthly Bond Market & Rating Snapshot

FINANCIAL VARIABLE	JUN-14	JUL-14	MoM CHNG
Overnight Policy Rate (%)	3.00	3.25	25 bps
3-year Benchmark MGS (%)	3.50	3.50	-1 bps
10-year Benchmark MGS (%)	4.03	3.89	-14 bps
3-year IRS (%)	3.85	3.87	3 bps
10-year IRS (%)	4.31	4.39	9 bps
Ringgit 3-year AAA (%)	3.90	3.91	2 bps
Ringgit 3-year AA (%)	4.29	4.31	2 bps
Ringgit 3-year A (%)	6.27	6.28	2 bps
10-year US Treasury (%)	2.53	2.56	3 bps
2-year US Treasury (%)	0.46	0.53	7 bps
MYR/USD	3.2110	3.1957	-0.5%
KLCI Index	1,882.71	1,871.36	-0.6%
S&P 500 Index	1,960.23	1,930.67	-1.5%

Source: Bloomberg, MARC Fixed Income Research

**Global Markets**

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The benchmark 10-year US Treasuries (UST) yield jumped 10 bps on 30 July, after second quarter GDP data from the US beat economists' projection by growing 4.0%. The release of the FOMC statement which showed that the Fed is on track to taper its monthly bond purchases by another USD10 billion to USD25 billion and policymakers viewed "the likelihood of inflation running persistently below 2 percent has diminished somewhat" also added selling pressure to UST.

Ringgit Bonds

2

The local bond market reacted positively to BNM's decision to raised overnight policy rate to 3.25% from 3.00%, with the benchmark Malaysian Government Securities (MGS) 10- and 20-year yields dipping lower as investors expected BNM's decision to be able to contain inflationary pressure in the near term. Heightened geopolitical risk following conflicts in the Middle East and Ukraine and the downing of the Malaysian Airlines aircraft also lent support to the government bond market as investors increased demand towards safe haven asset classes.

Currency

2

The ringgit posted a third consecutive month of gains against the USD, lifted by BNM's interest rate hike decision. Nonetheless, the ringgit pared its gains as stronger-than-expected US GDP growth in the second quarter and signs of a strengthening job market renewed investors' concerns that the Fed would raise the interest rate sooner than expected.

Topic of the Month – No Hurry in Further Tightening

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Market Review

Global Markets

Before the conclusion of the FOMC meeting on 30 July, strong buying interest towards the longer-end of the UST curve was seen with the benchmark 10- and 30-year UST yields falling to the lowest level since June last year, due to a rally in European bonds that enticed investors to add duration to their portfolio. The right wing of the curve also gained ground after reports showed that US consumer prices have continued to stay muted (June: +0.3%; May: +0.4%) and the International Monetary Fund (IMF) cut the country's growth forecast for 2014 to 1.7% from the 2.0% predicted earlier. Investors were also seeking refuge in safe haven asset classes following the anxiety over geopolitical developments in the Middle East and Ukraine. However, good economic news is bad news for the bond market. The benchmark UST 10-year yield jumped 10 bps on 30 July, the biggest increase since May 2013 and reversing its earlier gains, after second quarter GDP data from the US beat economists' projection by growing 4.0%. The release of the FOMC statement which showed that the Fed is on track to taper its monthly bond purchases by another USD10 billion to USD25 billion and policymakers viewed *"the likelihood of inflation running persistently below 2 percent has diminished somewhat"* also added selling pressure as investors worried that the economic landscape is good enough for the central bank to hike its interest rate before the first quarter of next year.

In the euro zone, the bond market extended its upward trajectory to close higher for the seventh consecutive month with the Bloomberg Eurozone Sovereign Bond Index closing near its highest level on record. This is amid investors' speculation that the European Central Bank (ECB) would need to implement further stimulus as slower growth in consumer prices (July: +0.4%; June: +0.5%) and a stubbornly high unemployment rate (June: 11.5%; May: 11.6%) have led many to believe that the central bank's recent stimulus measures are not sufficient to revive the region's economy. The benchmark sovereign 10-year yields across Germany and Italy dropped to record-low levels on 29 July before increasing slightly due to profit-taking activities.

Ringgit Bonds

Moving to the local market, the focus of the month was BNM's Monetary Policy Committee (MPC) meeting on 10 July. As predicted by most economists, the central bank decided to raise the OPR to 3.25% from 3.00% after the meeting. The floor and ceiling rates of the corridor for the OPR have been correspondingly raised to 3.00% and 3.50% respectively. The decision came amid (1) sustainable growth prospects; (2) inflation remaining above its long-run average; and (3) a build-up of economic and financial imbalances. Somewhat surprisingly, the local bond market reacted positively to the news with the benchmark MGS 10- and 20-year yields dipping lower as investors expected BNM's decision to be able to contain inflationary pressure in the near term. Heightened geopolitical risk following conflicts in the Middle East and Ukraine and the downing of the Malaysian Airlines aircraft also lent support to the government bond market as investors increased demand towards safe haven asset classes.

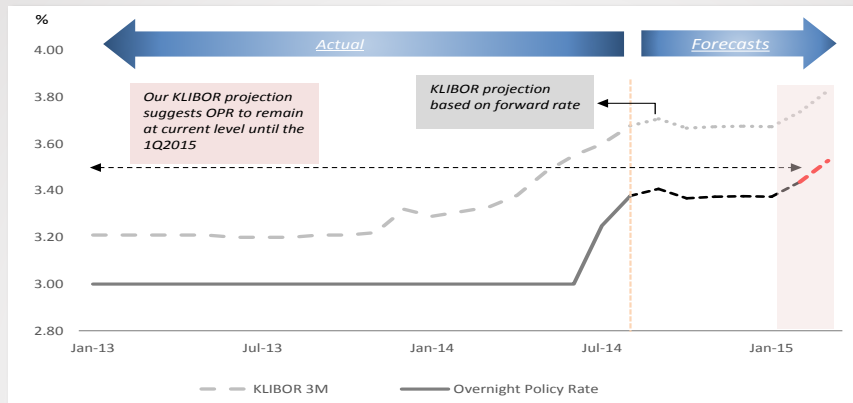
On the domestic front, Malaysia's consumer price index (CPI) has continued to grow, rising by 3.3% in June from a year ago as a result of higher food prices. For 1H2014, the CPI increased by 3.4% from the corresponding period last year. Meanwhile, the country's industrial production expanded by an annualised 6.0% in May, lifted by growth in all the indices including manufacturing (+7.8%), electricity (+4.6%) and mining (+1.4%).

In the primary market, the government's offering of the RM1.5 billion 15-year re-opening of Government Investment Issue (GII) garnered decent demand with a bid-to-cover ratio of 3.81x, the highest demand year-to-date, partly due to its rather small issuance amount. Another offering last month was the five-year re-opening of MGS worth RM3.0 billion, attracting a bid-to-cover ratio of 2.18x with an average yield of 3.70%.

Currency

The ringgit posted a third consecutive month of gains against the dollar, lifted by BNM's interest rate hike decision. As a result, some investors bet that the central bank may raise its OPR again in future meetings. Nonetheless, the ringgit pared its gains as stronger-than-expected US GDP growth in the second quarter and signs of a strengthening job market renewed investors' concerns that the Fed would raise the interest rate sooner than expected. The local currency appreciated 0.48% m-o-m to settle at 3.1957 against the greenback. Meanwhile, the dollar registered gains against most of its major counterparties with the Bloomberg Dollar Spot Index closing 2.11% higher to 81.46, the highest level in more than eleven months, on signs of sustainable economic recovery. On a monthly basis, the euro depreciated 2.21% to 1.3390 against the dollar, incurring the biggest loss since March last year.

No Hurry in Further Tightening



Source: Bloomberg, MARC Fixed Income Research

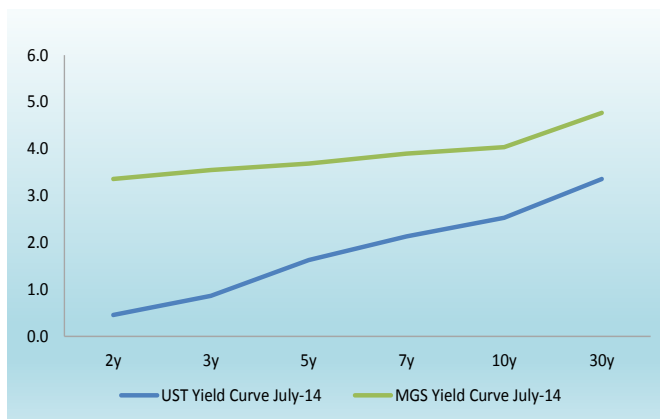
As widely predicted, BNM finally raised its OPR after the MPC meeting on 10th July in response to upside surprises in economic growth and stronger inflationary pressures. While BNM concluded the June statement with “Further review of the degree of monetary accommodation will depend on the MPC’s assessment of the balance of risks surrounding the outlook for domestic growth and inflation”, we are of the view that the central bank’s tone has become less hawkish and more data-dependent compared with its strongly-worded May statement.

Assuming that the three-month KLIBOR will stabilise at 30 bps above the OPR, the historical statistical relationship between the three-year MGS yield and the KLIBOR shows that an increase in the OPR to 3.5% is consistent with a three-year MGS yield of 3.6%, a level last seen before the launch of Quantitative Easing 1 in late-2008. Given the country’s high household indebtedness and in order not to hurt the economy’s growth trajectory, we opine BNM will not raise the OPR again for the rest of the year as the recent 25 bps hike is enough to dampen inflation expectation, evidenced by a fall in the 10-year MGS yield after the rate hike announcement. In addition, we believe most people, particularly low-income earners, have already felt the impact of the rate hike on their consumption behavior and debt-servicing ability. Last but not least, we believe the central bank will not hurry to increase the rate again until more data indicates that inflation is demand-pull driven, which will probably occur in the 1Q2015 prior to implementation of the Goods and Services Tax.

Notwithstanding these developments, we expect anxieties over a further rate hike will continue to exert selling pressure towards the shorter-tenure bonds and BNM’s data-dependent monetary direction will cause these bonds react sensitively to incoming economic data. As such, we maintain our earlier forecast of an upside bias in MGS yield with a bearishly flattening yield curve.

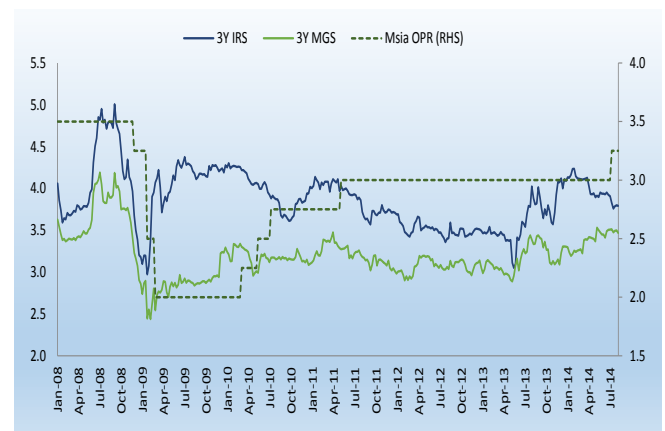
Yield Curve, IRS and OPR

UST and MGS Yield Curve (%)



Source: Bloomberg, MARC Fixed Income Research

IRS, MGS and OPR (%)



Source: Bloomberg, MARC Fixed Income Research

Summary of Corporate Bond Issuance and Outstanding

Historical Trend of Bond Issuance by Category (RM billion)

Year	MGS	Unrated Corporate Bonds	Rated Corporate Bonds	Unrated Government Guaranteed	Cagamas	Total Corporate Bonds
2008	60.0	3.52	40.38	6.80	5.05	55.74
2009	88.5	7.49	31.39	13.85	8.31	61.03
2010	58.1	6.03	35.99	4.73	6.33	53.07
2011	93.3	5.20	47.63	15.02	2.80	70.63
2012	96.2	13.44	76.55	30.38	3.42	123.79
2013	92.5	12.33	52.38	13.56	7.90	86.17
2014 YTD	50.0	2.61	31.41	14.01	1.06	49.09

Source: BPAM, MARC Fixed Income Research

Gross issuance of local corporate bonds rose for the second consecutive month in July to RM9.0 billion, up a significant 50% from the RM6.0 billion raised in June, lifted by increased issuances of quasi-government bonds (July: RM2.5 billion; June: RM0.6 billion). For the period from January through July, total gross issuance was also higher at RM31.4 billion, compared to RM24.8 billion raised during the corresponding period in 2013.

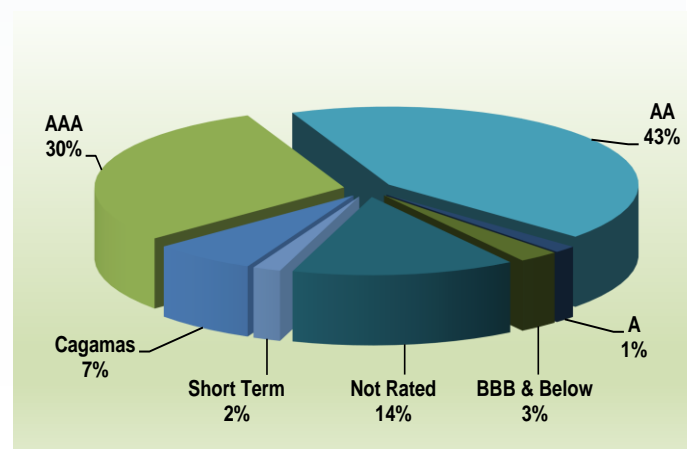
In the rated segment, a total of RM5.9 billion was issued in the month of July from the RM4.4 billion issued in June. The increase was mainly attributed to higher issuances in the financial services sector (July: RM3.2 billion; June: RM2.2 billion) and a notable increase in the infrastructure & utilities sector (July: RM2.0 billion; June: RM0.3 billion).

Outstanding Size of Sovereign, Cagamas and Corporate Bonds as of June 2014 (RM billion)

Asset Class	Conventional	Islamic	Total
Sovereign	318.53	205.00	523.53
Cagamas	10.88	12.74	23.62
PDS	127.87	198.59	326.46
Corporate	40.90	152.97	193.88
Corporate Guaranteed	13.90	28.06	41.95
Financial	63.48	13.39	76.86
ABS	9.59	4.17	13.77

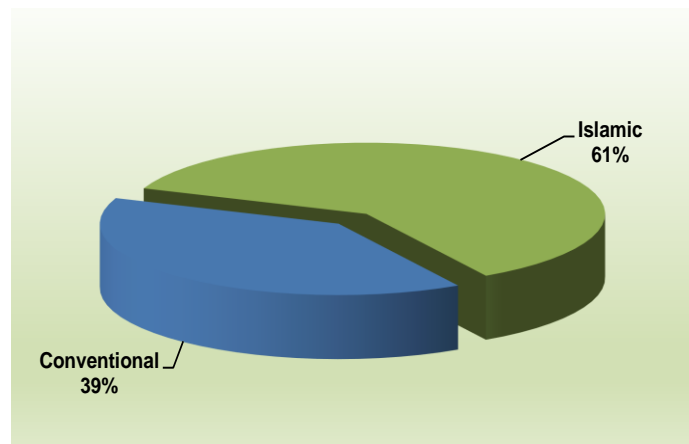
Source: BPAM, MARC Fixed Income Research

PDS outstanding: Distribution by Rating Type



Source: BPAM, MARC Fixed Income Research

PDS outstanding: Conventional & Islamic



Source: BPAM, MARC Fixed Income Research

Secondary Market Activities

Secondary Market Volume (RM billion)

Asset Class	Jun-14	Jul-14	MoM Chng
MGS/GII	32.7	46.0	13.3
Cagamas	0.3	0.6	0.2
FI Corporate	2.1	2.4	0.3
Non FI-Corporate	4.9	6.6	1.7

Source: BPAM, MARC Fixed Income Research

Non-FI Corporate Traded by Rating Type (RM billion)

Rating Type	Jun-14	Jul-14	MoM Chng
AAA	1.7	3.3	1.6
AA	3.1	3.2	0.0
A	0.0	0.0	0.0
BBB and below	0.0	0.0	0.0
Short term	0.0	0.2	0.1

Source: BPAM, MARC Fixed Income Research

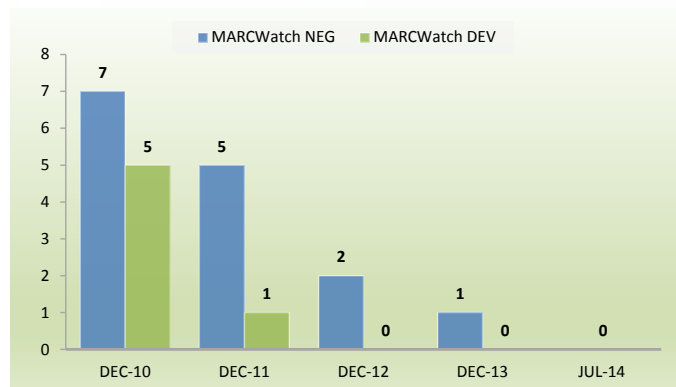
MARC Rating Activities in 2014 YTD

List of Rating Migration in 2014 YTD

Principle	Main Sector	Issuer	Date Announced	Rating Action	Rating Outlook	Long-Term Rating		Short-Term Rating		Issue Size (MYR mil)
						Before	After	Before	After	
Conventional	Trading/Services	Tesco Stores (M) Sdn Bhd	15-Jan-14	DOWNGRADED	STA	AAA	AA+	MARC-1	MARC-1	3500
Islamic	Industrial Products	Kinsteel Bhd	11-Mar-14	DOWNGRADED		C	D			100
Islamic	Industrial Products	Kinsteel Bhd	11-Mar-14	DEFAULT		C	D			100
Conventional	Property	Special Coral Sdn Bhd	21-Mar-14	UPGRADED	STA	AA	AA+			40
Conventional	Property	Special Coral Sdn Bhd	21-Mar-14	UPGRADED	STA	A	AA-			35
Conventional	Property	Special Coral Sdn Bhd	21-Mar-14	UPGRADED	STA	B	BB-			30
Conventional	Property	Special Coral Sdn Bhd	21-Mar-14	UPGRADED	STA	BBB	A-			25
Conventional	Property	Special Coral Sdn Bhd	21-Mar-14	UPGRADED	STA	BB	BBB-			10

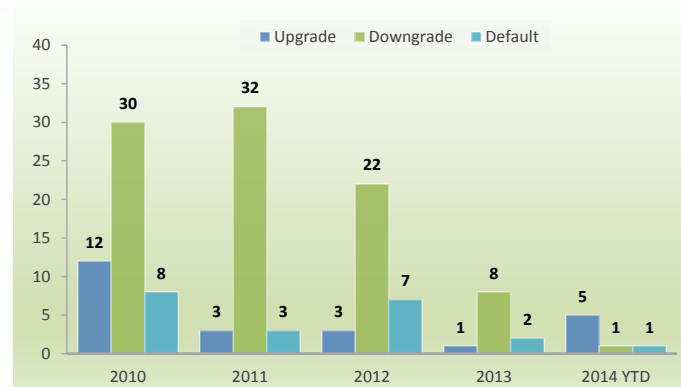
Source: MARC Fixed Income Research

MARCWatch Placements, by Issue Count



Source: MARC Fixed Income Research

Upgrades, Downgrades and Default, by Issue Count



Source: MARC Fixed Income Research

List of Rating Actions in the month of July 2014

Principle	Main Sector	Issuer	Date Announced	Rating Action	Rating Outlook	Long-Term Rating		Short-Term Rating		Issue Size (MYR mil)	Credit Enhancement
						Before	After	Before	After		
Islamic	Infrastructure & Utilities	Kapar Energy Ventures Sdn Bhd	3-Jul-14	WITHDRAWN		AA+	AA+			3402	
Conventional	Industrial Products	Press Metal Berhad	3-Jul-14	AFFIRMED	NEG	BBB	BBB			323.7	
Islamic	Property	Putrajaya Holdings Sdn Bhd	4-Jul-14	WITHDRAWN		AAA	AAA			1500	
Conventional	Finance	Hong Leong Financial Group Bhd	9-Jul-14	AFFIRMED	STA	AA	AA	MARC-1	MARC-1	1800	
Conventional	Property	MRCB Sentral Properties Sdn Bhd	9-Jul-14	AFFIRMED	STA	AAA	AAA	MARC-1	MARC-1	400	fg
Islamic	Infrastructure & Utilities	Ranhill Group Sdn Bhd	9-Jul-14	AFFIRMED	STA	AAA	AAA			300	bg
Islamic	Infrastructure & Utilities	Ranhill Group Sdn Bhd	9-Jul-14	AFFIRMED	STA	AAA	AAA			500	fg
Unspecified	Finance	Hong Leong Investment Bank Berhad (fka MIMB)	10-Jul-14	AFFIRMED	STA	AA-	AA-	MARC-1	MARC-1	0	
Unspecified	Finance	Hong Leong Investment Bank Berhad (fka MIMB)	10-Jul-14	AFFIRMED	STA	AA-	AA-	MARC-1	MARC-1	0	
Islamic	Infrastructure & Utilities	Ranhill Powertron II Sdn Bhd	17-Jul-14	AFFIRMED	STA	AA	AA			360	
Islamic	Infrastructure & Utilities	Ranhill Powertron II Sdn Bhd	17-Jul-14	AFFIRMED	STA	AAA	AAA			350	fg
Islamic	Infrastructure & Utilities	Alloy Properties Sdn Bhd (f.k.a Haluan Gigih Sdn Bhd)	22-Jul-14	WITHDRAWN		AA	AA			240	
Unspecified	Country	Indonesia	23-Jul-14	INITIAL	STA	AA-	AA-			0	
Conventional	Construction	Special Port Vehicle Bhd	25-Jul-14	AFFIRMED	NEG	AAA	AAA			1310	
Islamic	Technology	Serrisa Sinar Bhd	31-Jul-14	WITHDRAWN		AA	AA	MARC-1	MARC-1	200	

Source: BPAM, MARC Fixed Income Research

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