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`Move to issue bonds timely'

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MALAYSIA has made the right move in issuing sovereign bonds now as the economic climate is reasonably healthy and the political situation is stable, bond traders say.

They added that the move is timely because the bonds risk being seen by investors as expensive if the second quarter gross domestic product (GDP) figures, expected to be released anytime this month, are unfavourable.

"It will be quite risky if the Government waits until the GDP figures for the second quarter are released.

"If the GDP growth is low, the bonds will be more expensive," a local trader told Business Times in Kuala Lumpur.

Malaysia's first quarter GDP grew by 3.2 per cent, down from 6.3 per cent in the previous quarter.

Prime Minister Datuk Seri Dr Mahathir Mohamad said the April-June GDP would be similar to the January-March period, but some analysts are predicting lower figures.

Traders said that if the second quarter GDP shows zero or negative growth, investors may not form a positive outlook on Malaysia's economy.

Subsequently, the bonds may be downgraded, such as in 1998 when rating agencies downgraded everybody's in Asia, the traders said.

"This would affect the spread and despite low US interest rates, the cost of raising US dollars would be more expensive," they added.

Some US\$750 million (US\$1 = RM3.80) of Malaysian bonds are being marketed by JP Morgan Chase & Co and Salomon Smith Barney Inc to fund the country's fiscal stimulus measures to boost the slowing economy.

The 10-year bonds are expected to yield about 235 basis points more than US Treasuries, which are 25 basis points more than existing Malaysian bonds maturing in 2009.

The Government could sell up to US\$1 billion of bonds, depending on demand.

The Finance Ministry, in a statement released last week, said the bonds will be rated BBB by Standard & Poor's and Baa2 by Moody's Investors Service Inc.

The ministry said proceeds from the offering will be used for the Government's general funding purposes.

When asked about the new bonds last week, Dr Mahathir, who is also the Finance Minister, said the Government could not respond to a downturn purely by reducing interest rates.

"We have to think of other ways and means to prop up the economy," he said.

Malaysia's existing US\$1.5 billion of 10-year bonds, which pay interest of 8.75 per cent and mature in 2009, recently yielded about 210 basis points more than US Treasuries of similar maturity.

Traders and analysts believe that Malaysian new bonds would be attractive in the international market, given the low US interest rates which have been reduced for the sixth time this year. This brought the federal funds rate - a benchmark for short-term rates - to 3.75 per cent, the lowest in more than seven years.

An analyst said Malaysia would not have difficulties in marketing its bonds due to the stability of the domestic economy.

He said Malaysia's trade surplus and external reserves, which are sufficient to finance three months retained import and low inflation, are

factors which indicate that the country would not default on payments for its bonds.

However, another bond trader said that foreign investors are also monitoring Malaysia's political development and the country's reserves.

"Investors are quite worried about the reserves. They are concerned whether it will drop below three months' import," he said, adding that investor confidence will strengthen if Malaysia's international reserves grow to a level adequate to finance four months of retained import.

As of May 31 this year, Bank Negara Malaysia's international reserves stood at RM98.6 billion, sufficient to finance about 3.8 months of retained import and 5.5 times the short-term external debt.

Investors' concerns may arise as the central bank's reserves position is low, not only by Malaysia's own standard of six to seven months previously; but also in comparison with Singapore's 12.3 months, Taiwan's 9.6, Indonesia's 6.1 and Thailand's 5.7.

The bond trader also noted that foreign investors are waiting for the appointment of a new finance minister by the Prime Minister after former Finance Minister Tun Daim Zainuddin resigned on June 1.

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