

22/10/2001

Shift in budget process to benefit bond market

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THE bond market, an important source of financing for the Government in the coming year, could be a prime beneficiary of the administration's move to plan its finances two years ahead beginning next year.

The Government's shift to a two-year budget process is expected to improve its ability to plan its expenditure and raise financing easily when it needs to.

Bond market players hope this move will help Bank Negara Malaysia and the Treasury plan ahead for issues of government bonds and avoid surprising the bond market with unexpectedly large issues which can swing bond prices.

"It is important that we know how much the Government intends to borrow each time so that we can plan our own strategies," said a bank treasury dealer.

Since last year, the central bank has published a calendar giving the dates it intends to issue government bonds, particularly the Malaysian Government Securities (MGS), and their tenure.

However, the size of the issues is still missing from the bond auction calendar, making it difficult for traders to plan their investment strategies.

"We hope that this extra planning will be helpful in formulating a more precise bond calendar this year. Currently, the bond calendar only has the schedule for the months and tenures of MGS without the amounts," a trader said.

"It would be very helpful if the forward planning would make it possible for the 2002 bond calendar to incorporate the amounts of each MGS, which would help us to plan our investment cashflow," a treasury head said.

Last week, the Government said it will determine its expenditure two years ahead from now on, instead of annually, in a move to improve the quality and efficiency of budget allocations.

Detailed examinations and reviews of ministries' proposals will be conducted once every two years from next year, a change which is hoped it will reduce the time and resources poured into preparing the budget every year.

"In setting the budget two years ahead, ministries and agencies are able to plan and implement programmes and projects with greater certainty, discipline and transparency.

"Government borrowing programmes and requirements can be more accurately determined in advance to minimise either over- or under-borrowing," it said.

Meanwhile, conditions are expected to remain conducive in the medium term for the Government to finance its RM18.6 billion budget deficit through the local debt market.

The general sentiments for the local bond market is that it will continue to play a major role in fund-raising not only for the Government but also for the private sector.

As such, the Government should be able to issue the MGS to raise funds at a relatively cheap cost at current low interest rates.

Raising funds through sovereign US-denominated bonds would also be relatively cheap as the US short-term interest rates remain low at 2.5 per cent, with further expectations that it is likely to fall another 50 basis points to 2 per cent in the near future.

Malaysia's budget deficit for 2002 is 5 per cent of gross domestic product (GDP) compared with RM22.4 billion this year representing 6.5 per cent of GDP.

The economic uncertainties, heightened by the September 11 terrorist attacks on the US, have increased investors' interests in higher rated corporate bonds and almost-zero-risk MGS.

As such, the success pick-up rate for MGS and sovereign bonds remains favourable.

Last Friday in the budget address, Prime Minister Datuk Seri Dr Mahathir Mohamad said Malaysia would not issue any more sovereign bonds this year, but he did not rule out such a sale next year.

At the end of June, Malaysia issued US\$1 billion (US\$1 = RM3.80) in 10-year sovereign bonds.

International ratings agency Standard & Poor's is expected to maintain its BBB long-term foreign currency rating with a stable outlook on Malaysia at the present.

The country's rating is at the lower end of investment grade, and a couple of notches above speculative grade.

For the first nine months of this year, the issuance of MGS increased by 16.2 per cent, amounting to RM11.26 billion to account for almost 83 per cent of gross funds raised by the public sector.

The increase reflects the Government's higher financing needs and commitment to establish a benchmark yield for the bond market through the regular issues of MGS.

Fund raised through the issuance of Khazanah bonds, however, declined to RM583 million.

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