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Govt expected to issue second Sukuk in Q3 (HL)

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MALAYSIA is expected to issue the country's second Islamic bond, most likely euro-denominated, in the third quarter of this year to take advantage of the attractive global interest rate environment, said industry sources.

Three banks are believed to be the main contenders to arrange the global issue. Malaysia launched the first-ever rated Islamic sovereign bonds, known as Sukuk, when it came out with a RM600 million issue in June 2002.

Sources said the front runners are HSBC Global, which is teaming up with Commerce International Merchant Bankers Bhd for the deal, and the Citibank Bhd. A total of 10 banks are in the running.

Yesterday, Second Finance Minister Datuk Dr Jamaludin Jarjis said Malaysia was planning to launch another tranche of sovereign bonds in the second half of this year for benchmarking purposes.

"Now it is already the middle of the year. The Government will have to go to the market, at least for benchmarking. We do not need it for our cash flow," he told reporters at a briefing after the launching of the 2003 RHB Investment Forum in Putrajaya.

Jamaludin said the Government has not decided on the size and the denomination of the bonds, or whether the issue will be Islamic or conventional, "but we are mindful there is a need to replicate the success of the Islamic instrument (last year)".

Earlier this month, Jamaludin said Malaysia might opt to sell global euro-denominated bonds to wean the country away from its dependency on the US dollar.

Industry sources said the second global Sukuk should hit the market in September or October this year. A road show to West Asia and Europe will be conducted a month before the launch.

"The HSBC-CIMB partnership looks to be the favourite to clinch the deal right now, as the former had successfully structured the first Sukuk," a source said.

The first sovereign Sukuk, an award-winning issue of five-year global Islamic Floating Rates Notes based on the Islamic principle of Sukuk Al-Hijarah, was twice oversubscribed, a big hit considering its novelty.

Prior to that, Islamic debt securities issued in Malaysia were not considered fully Syariah-compliant by West Asian investors due to the conflicting Syariah interpretations and legal systems. More than anything, analysts said the paper had effectively achieved the international Islamic community's endorsement that its underlying principle was within the

definition of "halal".

The first Sukuk, launched two days after Prime Minister Datuk Seri Dr Mahathir Mohamad's surprise retirement announcement, was rated "BAA2" by Moody's Investors Service and "BBB" by Standard & Poor's.

It is listed both on the Luxembourg Stock Exchange and the Labuan International Financial Exchange. Demand for a second global Sukuk is expected to be strong, partly riding on the success of its predecessor.

Meanwhile, industry sources said Malaysia's second global Sukuk may also be issued in a combination of dollar and euro denominations, with a larger proportion in the latter.

An official from one of the main contending banks confirmed yesterday that they had been asked by the central bank to make a presentation on a possible euro-denominated Sukuk issue.

Assuming the appreciation of the euro is nearing its peak, a euro-denominated Sukuk will allow the Government to benefit from significant translation gains in the future should the currency depreciate in the medium to longer term. It will be cheaper to service the debt in euros in terms of ringgit value, as less ringgit will be needed to repay the debt.

An euro Sukuk will be in line with the central bank's strategy to diversify its basket of currencies in its international reserves.

Although the exact make-up of Bank Negara Malaysia's reserves is not disclosed, they are estimated to be 60 to 80 per cent in US dollars. The euro and the yen account for only 5 to 10 per cent each.

The issue should also work hand-in-hand with the Government's recent go-euro stance.

"If we keep our assets in US dollars, it will depreciate in value. The debt side can remain in dollars, but for those incoming revenue it should be euro. This is basically mitigating business risk. We are advising our corporations to take note of this, especially those that we own," said Jamaludin.

He also said the country would relook the ringgit peg only if Malaysia's products were losing competitiveness. "For now, there is no such requirement," he said.