

## **Zeti Akhtar Aziz: The development of the Malaysian bond market**

Remarks by Dr Zeti Akhtar Aziz, Governor of the Central Bank of Malaysia, at the Launch of the Electronic Trading Platform by Bursa Malaysia, Kuala Lumpur, 29 April 2008.

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Let me first of all thank Bursa Malaysia for inviting me to say a few words on this occasion of the launch of the Electronic Trading Platform. This initiative marks another important advancement in the development of the Malaysian bond market. The Electronic Trading Platform will take over the function that was previously performed by the Bond Information and Dissemination System (BIDS). Bank Negara established BIDS ten years ago, in 1997 to provide market information on domestic debt securities. BIDS was developed as a centralized database that provided information on the terms of the issue, details of trade done and the relevant information on the various debt securities, to facilitate increased transparency and efficiency in the bond market. BIDS therefore aided the price discovery process thereby promoting secondary and primary activities in the bond market. BIDS was revolutionary in its time as authorities in other jurisdictions subsequently launched similar initiatives in their respective markets.

This Electronic Trading Platform is a significant enhancement to the mechanism in the development of a more vibrant bond market. Indeed, this development is timely because the Malaysian bond market is now at the threshold of its next stage of development. Several factors have brought the development of the bond market to this threshold. Firstly, large investment projects of long-term gestation by the private sector can now source financing mainly from the bond market as opposed to only relying on the banking system. As a consequence, the expansion of the private debt securities market has now exceeded the public debt securities market. With the recovery of private investment since 2003 and its increased momentum there has been growing expansion of the bond market.

Secondly, the liberalisation of the bond market to allow non-residents to raise funds from our domestic bond market has also contributed further to the growth of the market. Thirdly, an important development of Islamic finance in Malaysia is the development of the sukuk market. In 2007, the sukuk issuance has exceeded the issuance of conventional bonds. This has increased the diversity of asset classes and instruments in the Malaysian bond market.

Fourthly, there has been a major structural enhancement in the capital market intermediaries with the introduction of investment banking in 2006. With the permitted foreign interest in investment banking raised to forty-nine percent, foreign participation is encouraged. In addition, Islamic banking institutions, including Islamic subsidiaries may conduct investment banking activities. These capital market intermediaries are also reinforced by the strengthening of the institutional investors and the fund management industry. The growing sophistication of investors has resulted in increasing diversification of portfolios with growing interest in the bond market. Foreign holdings of debt securities outstanding have also increased from less than 1% in 2000 to 15% in 2007. And finally, these developments have been continuously reinforced by the strengthening of the financial infrastructure, the settlement system, the legal and regulatory framework to ensure the robustness and vibrancy of the bond market.

Malaysia has benefited immensely from the development of the bond markets. As an important source of financing, it contributes to the economic growth process. It also allows for more efficient mobilization and allocation of financial resources. With greater efficiency in the intermediation process, it reduces the cost of financing. It also allows for the increased diversification of risks both for issuers and investors. In addition, it enhances financial stability through potential diversification, increased transparency and greater market discipline. The development of the bond market also enhances the transmission mechanism

of monetary policy. Finally, and most importantly, the more developed bond market has enhanced our resilience to the implications of increased volatility in the international financial markets.

The Malaysian bond market has several distinguishing features. Firstly, it comprises both the conventional and Islamic bond market. Secondly, the secondary and repo market is now growing in significance. Turnover volume in the secondary market has been steadily increasing over the years marking the active participation in the bond market by investors. In 2007, total annual turnover volume increased by 46% to RM777 million.

There is also an increased diversity of instruments being issued ranging from asset-backed bonds, bonds bearing features such as stepped-up coupons and "floaters" and pass-through ABS. Malaysia is also a leader in the development of sukuks and its pioneering efforts have seen the introduction of innovative structures such as the exchangeable sukuk musharakah, exchangeable sukuk as well as sukuk based on *istisna'* and *ijarah*. This is reinforced by the diversified tenures of the issues. Malaysia's strong financial links to the traditional and non-traditional markets such as in the Middle East also allows issuers to diversify their investor base. Malaysia therefore continues to remain an important destination for international financial flows that are traded on the New Silk Road.

In concluding my remarks, I wish to congratulate all those involved in crystallizing the Electronic Trading Platform that is being launched today. This is a further step to create a more vibrant bond market. The growing role of the bond market in mobilizing and allocating funds not only in the domestic financial system but also across borders, to and from other parts of the world, has demonstrated the maturity of the Malaysian bond market. This has not only strengthened international financial inter-linkages but has increased the potential for greater economic integration and shared prosperity.