



The Malaysian Debt Market and Derivates – What next?

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Section 1

Introduction to the Malaysian Islamic Capital Market

Introduction

The Malaysian capital market has experienced substantial progress over the past decade, particularly in key areas such as:

- growth in fund-raising capacity;
- expansion of capital market products and services;
- adoption of many internationally benchmarked practices;
- and the development of a robust regulatory framework supporting the capital market.

The combination of these factors, coupled with the country's strong economic fundamentals, comprehensive supporting infrastructure, presence of a pool of educated and talented professionals, and cost-competitive operational resources have all combined to create an attractive investment environment for investors.

Despite the setbacks in the growth path experienced during the financial crisis of 1997–98, these strengths are still very present in Malaysia and represent cogent factors in favor of the future development of the capital market.

Malaysian Experience – Islamic Capital Market

- Malaysia's first Shariah compliant savings institution was formed in 1963 serving the Malay Muslims outside the conventional market.
- The Islamic Banking Act was enacted in 1983 and the Takaful Act in 1984 which immediately after that, the country's first Islamic Bank and Takaful company was established
- Ten years later, the Islamic Banking Window Scheme or "Skim Perbankan Tanpa Faedah" was introduced which allowed all conventional banks to offer Islamic financial products and services. Resulting from this initiative the Islamic banking and finance share of market grew from a mere 1% over the last 10 years to about 6% nearly overnight.
- Over the course of the last 6 years, Islamic banking asset in Malaysia has grown to more than 150%.
- As at 2009, Malaysia's Islamic financial market is to a degree complete comprising the banking sector, the inter-bank money market, the debt and equity market, asset management, takaful, other non-banking financial institutions and the derivatives market.

Malaysian Experience – Islamic Capital Market

Islamic Capital Market rides on the vast potential of Sukuk development:

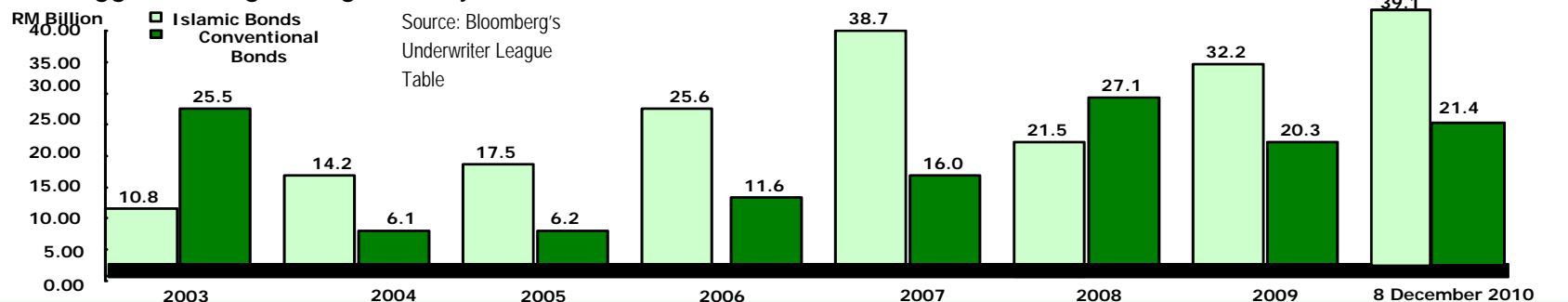
- The more recent development in Islamic finance is the growing significance of the Sukuk market to become an increasingly important component of the Islamic financial system.
- The development of the Sukuk market will provide opportunities for the corporate sector, the government agencies, multinational corporations (MNCs) and multinational development institutions to raise funds through the issuance of Sukuk to meet their financing requirements.
- The Sukuk market also serves as an important platform, complementing the conventional bond market in enhancing the effectiveness and efficiency for the mobilization and allocation of funds within the domestic financial system, as well as in the international financial system.

Section 2

Growth of Islamic Debt Capital Markets

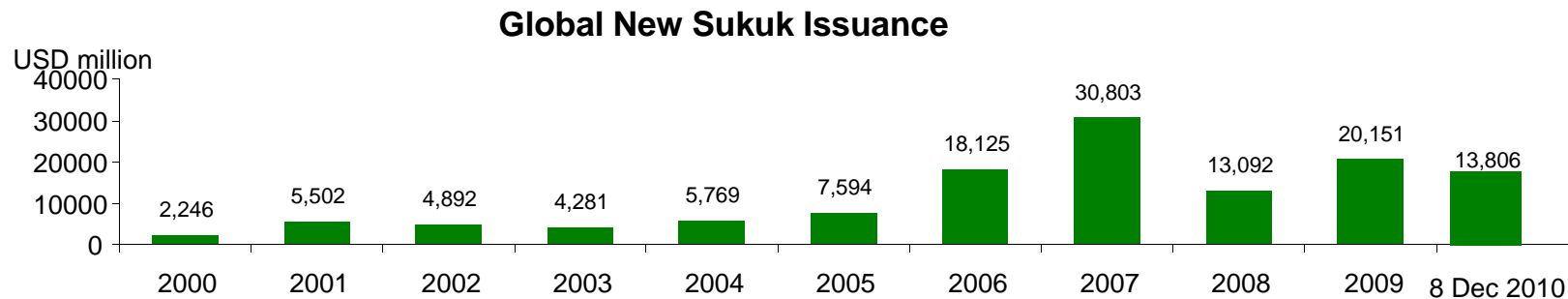
Malaysia: Sukuk Market

- The **first Sukuk issue** in Malaysia was the Shell MDS Sdn Bhd Bai' Bithaman Ajil (BBA) in 1990 and since then, Sukuk has evolved in depth and sophistication. Investors can now choose between RM and non-RM denominated Sukuk, as well as the types of securities, tenures, asset classes, structures, issuers and risk profiles that suit their needs.
- Malaysia also kick-started the international Sukuk market which began in 2001 by Kumpulan Guthrie Berhad's issuance of USD 150 million First Global sukuk. Subsequently, in 2002 the Government of Malaysia issued a USD600 million issuance– It has been growing in size ever since with more issuance of Islamic Eurobonds in the international Sukuk market.
- 17 years later, the Malaysian Sukuk market is the world's largest Islamic Sukuk market, **representing about two thirds of the USD66 billion in outstanding Sukuk globally**. In addition, the Securities Commission of Malaysia has approved a total of 42 bond issues amounting to RM52.40 billion of which 15 issues were Sukuk, valued at RM32.1 billion. The value represented 61.3% of total new bond issues approved as of 2009. The reduce percentage as compared to previous years is mainly due to proposed issuance by issuers from the conventional financial services sector.
- The announcement on tax neutrality was done in 2004 where the issuances of sukuk have increased for the following years.
- The Ringgit Sukuk grew significantly since 2003, versus conventional bonds, as illustrated below:



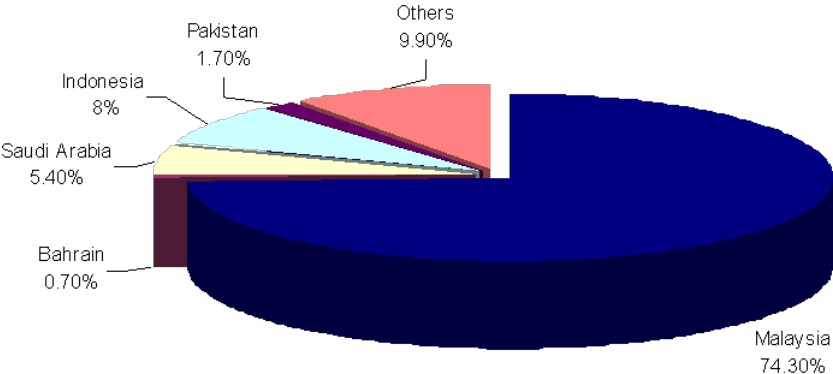
Global: Growth of the Islamic Debt Capital Markets (Cont'd)

- The global Sukuk market has experienced a boom in recent years, spurred by the advantages offered by Sukuk (as highlighted in the previous slides) over conventional bonds.
- Sukuk issues globally have grown exponentially in the last 4 years, from USD 5.7 billion in 2004 to USD 30.8 billion in 2007. There was a decline in Sukuk issuance of more than 50% in 2008, due to bleak economic conditions. As of Year 2009, the Sukuk market has started picking up with over USD20 billion new sukuk issuance entering the market.

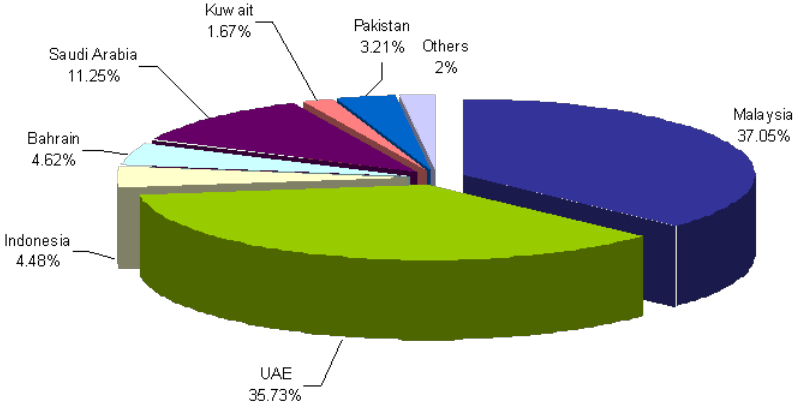


Source: Bloomberg

Sukuk Issuance By Country



Data as of 8 December 2010. Source: Bloomberg



Data as of December 2008. Source: Bloomberg

Section 3

Malaysia Islamic Debt Capital Market

Malaysia: Our Strengths

The commitment and combined efforts of the Malaysian government and regulators. There is a clear articulation of the vision and policies to drive the local Islamic capital market. This is reinforced by the implementation of a strong legal, regulatory and tax framework.

Key development contributors:

- 1. Jurisdiction & Regulations:** Bank Negara Malaysia and the Securities Commission have worked closely on a sequence of vital blueprints:
 - 10-year Financial Sector Master Plan,
 - 10-year Capital Market Master Plan and the Islamic securities guidelines.
 - The government has reaffirmed all these plans and initiatives with the announcement of a range of tax measures in the 2006 budget.
- 2. Islamic Financial Centers:** MIFC, Bank Negara Malaysia & ICM, Securities Malaysia
- 3. Development institutions:** Development of the other key components of the Islamic financial system, the money market, banking, and takaful sectors. The various components are able to meet the different requirements of the economy including the differentiated tenor for which the funds are required. This includes providing stable long-term funds for large investments and development projects. These would allow for a balanced allocation of financial and economic resources within the economy, diversifying the risks through the Islamic financial system, and enhancing its flexibilities to adjust, thus strengthening its resilience.

Weaknesses (Challenges)

While much has been achieved, much remain to be done. Among key issues that need to be adhere by practitioners of Islamic Capital Market in Malaysia:

1. Continuous supply of Islamic papers and instruments that would promote the secondary trading of instruments and add greater depth to the market.

2. Shariah experts

Full understanding of the mechanics of Islamic Capital Market, are key to ensuring its proper governance. And shariah decisions, when made, should be transparent and disclosed. This will allow others to appreciate the juristic reasoning, which in turn should lead to wider acceptance of shariah decisions, particularly if they have implications on cross-border transactions. In relation to this, a guide for issuers and investors to refer with regards to shariah decisions would facilitate the development of the market.

Opportunities

Five major trends are having a significant bearing on the future development of the Sukuk market.

1. The bond market is now becoming **key to meeting the funding requirements** for both the public and private sectors in emerging market economies. This is particularly the case for the Middle East and Asia, which are among the fastest-growing regions in the global economy.
2. **Demand for Sukuk significantly exceeds the supply**, spurred by growing interest by corporations, sovereigns and MNCs. Today, the global Sukuk market, denominated in international currencies, is estimated to exceed US\$50 billion. Although the size of the market is modest by global standards, the Sukuk market is experiencing remarkable growth, increasing at an average rate of growth of 40% a year. The significant demand for Sukuk has also been spurred by the high levels of surplus savings and reserves in Asia and in the Middle East.
3. There are a **great number of global players** such as investment banks, Islamic banks and securities firms that are involved in the issuance of Sukuk in the international financial markets. A large number of western banks are also providing Islamic financial services taking advantage of the opportunities and to provide customized products and services to their customers.
4. The **established international financial centers** have also shown interest in promoting the development of the Sukuk market including enacting the appropriate legislative provisions. These developments would augur well for the development of Islamic Capital Market.

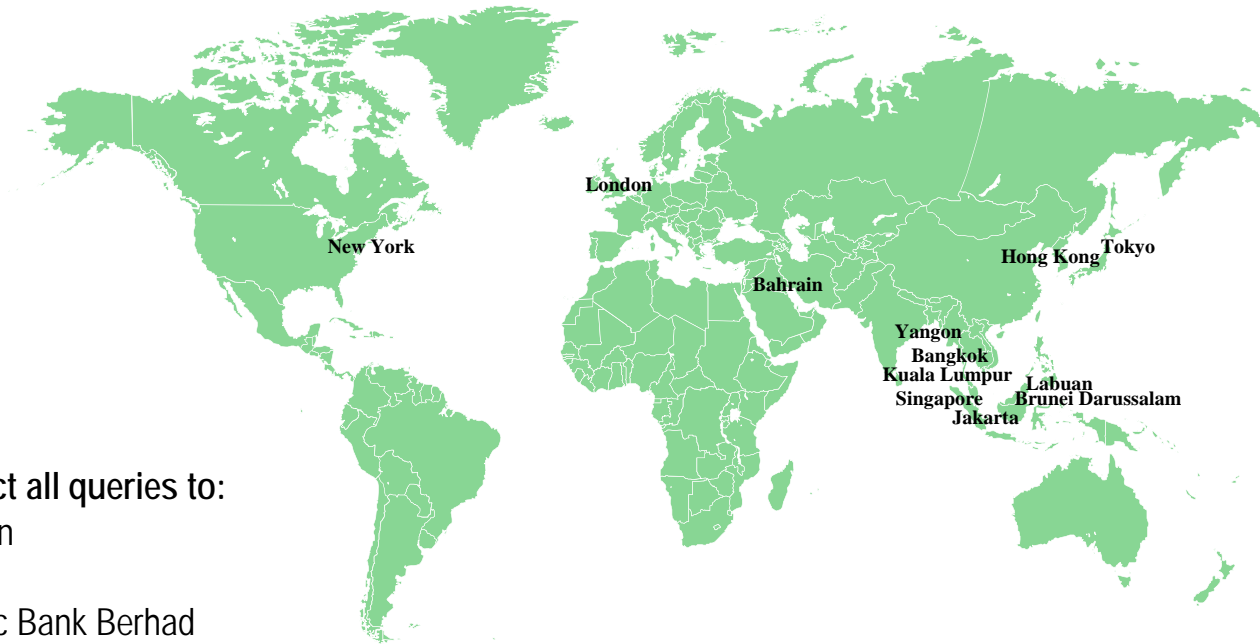
Section 4 Conclusion

Conclusion

- **Continuous product innovation** -Clearly, our ICM is not only built on a strong and well established Shariah foundation, our products and services are also offered within Malaysia's robust regulatory framework for the capital market
- **Liberalization** -Rules that limit or inhibit the market from flourishing have been removed or are being reviewed. For instance, measures allowing non-residents, in particular, multinational corporations and multilateral agencies to issue ringgit denominated bonds in Malaysia have led the International Finance Corporation and the World Bank to issue their first ever Sukuk in Malaysia.
- **Investors protection** – establishment of Shariah Advisory Council (SAC) at the SC soon after SC's own establishment in 1993
- **Increase connectivity** - connectivity of Malaysia's ICM to a global ICM network with the signing of a mutual recognition agreement between the SC and the Dubai Financial Services Authority (DFSA) and recently with Qatar Financial Markets Authority.
- **High quality intermediation services** - investment banks, local and foreign Islamic banks, brokers and fund managers, played a big role into the dramatically expansion in recent years.

THANK YOU

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