How Cagamas benefits from secondary market liquidity enhancement

By Chito Santiago

Malaysia's national mortgage corporation, Cagamas, is ramping up its issuance of both conventional bonds and *sukuks* in 2017, and remains committed to enhancing its secondary market liquidity. The offerings already represent about one-third of its projected total issuance size of 10.5 billion ringgit (US$2.40 billion) for the year, having raised the equivalent of 3.4 billion ringgit (US$770 million) as of April 12.

"The increased issuances this year have much to do, firstly, with the implementation of Basel III because banks need high quality liquid assets to better manage their liquidity and capital structure," says Cagamas CEO Chung Chee Leong. "At the same time, the market is still flushed with liquidity."

Chung Chee Leong, CEO, Cagamas.

Cagamas on April 12 announced the pricing of its latest transaction – a dual currency, multi-tranche offering totaling 417 million ringgit (US$95 million) equivalent. The deal comprised of a one-year 70 million-ringgit and a one-and-a-half-year 30 million-ringgit conventional medium-term note issued under Cagamas' existing 40 billion-ringgit (US$9.1 billion) medium-term note programme, and a one-year S$100 million (US$71.43 million) issue through its wholly-owned subsidiary Cagamas Global PLC.

The one-year deal was competitively priced at 3.80% and the one-and-a-half-year at 3.90%, representing 47bp and 51bp, respectively, over the corresponding Malaysian government securities (MGS). The Singapore dollar tranche was priced at 1.64%, representing 35bp above the corresponding Singapore offer rate curve. This was Cagamas' second Singapore dollar issuance in 2017 drawn from the company's US$5 billion multi-currency medium-term note programme.

Earlier on March 22, Cagamas priced a three-month Islamic commercial paper (ICP) amounting to 500 million ringgit (US$113.5 million) issued under the commodity *murabaha* structure. On the back of strong demand the company was able to tighten the pricing by 3bp from the high end of the initial price guidance and secured a commendable bid-to-cover (BTC) ratio of 1.9x.

"The issuance of ICP underscores the company's relevance in its continuous support towards the development of the bond market through the issuance of various types of bonds/*sukuks* to meet the diversified investor needs," says Chung.

Since the start of 2017, Cagamas has managed to issue a variety of bonds with the first issuance being a one-year floating rate note amounting to 300 million ringgit (US$68 million) via private placement with the proceeds to be used to fund the purchase of mortgage loans from the financial system.

In 2016, Cagamas undertook a number of re-opening initiatives as part of its strategic resolutions to enhance the total outstanding amount per stock, which is vital to reduce new issue premium through value tracking assistance and continuous proactive engagement with investors.

"A lot of investors, particularly from overseas, say they are not keen to go into the corporate bond space simply because of the liquidity issue," explains Chung. "That is why we put efforts to enhance the secondary liquidity of Cagamas' papers."

It kick-started the initiatives with a 400 million-ringgit re-opening of its three-year *sukuk*, taking a strategic decision to tap a low duration stock bearing a high coupon rate of 5.28% as it has a low sensitivity to interest rate movement. The deal was priced competitively with a new issue concession of 7bp. "The re-opening increased the size of the outstanding issuances so that they can be qualified and be included in some of the highly influential bond indices," Chung points out.

The second *sukuk* re-opening amounting to 375 million ringgit, also for three years, attracted a robust demand from both local and foreign investors as evidenced by 5.4x BTC with orders from 30 different accounts, including foreign bids among various market segments. It improved the secondary trading of the re-opened stock from zero to 180 million ringgit post issuance, representing 48% of the re-opened stock. It was priced at 19bp below the comparable AAA curve and achieved lower cost of funding as illustrated by a reduction in spread of 12bp against the three-year government benchmark curve compared with the first re-opening in February.

As part of Cagamas' initiatives to promote secondary liquidity for its debt securities, it launched in April 2016 its Bloomberg pricing platform – the first and only pricing page created by a corporate entity in collaboration with Bloomberg. It was created to promote an efficient and robust price discovery for the establishment of a reliable *sukuk* yield curve based on continuously traded prices. It likewise increased the visibility of Cagamas' *sukuk* pricing especially among the foreign market players, which in turn attracts more participation from foreign investors and bank traders in local *sukuk* papers with the increased secondary market liquidity.

The company had the highest secondary trading volume in the local corporate bond and *sukuk* market, which was the second-highest traded paper after the government of Malaysia.

In 2016, Cagamas achieved the highest secondary market volume among the AAA-rated papers as well as the whole domestic corporate bond and *sukuk* secondary market with a total volume of 17.1 billion ringgit (US$3.86 billion), exceeding the 5.3 billion ringgit (US$1.2 billion) achieved in 2015.

As Cagamas ramps up its bond/*sukuk* issuance this year, Chung says the company will explore public issuances as one of its key performance indices in 2017 after relying on private placement offerings in which it managed to obtain better pricing.

"The past two years have been challenging for Malaysia, but things have settled down," says Chung. "It is a good time to look again at public issuance and we will explore it if it makes commercial sense. We are not afraid to compete in the market as we are different and provides investors with scarcity value."

In terms of foreign holdings of Cagamas papers in the ringgit space, Chung says they have increased from 0.5% in September 2015 to almost 8% in September 2016 as foreign investors became aware of the credit due to its foreign currency issuances. It has since fallen to about 6% at present as banks exited the credit.

This journey to attract foreign investors started in November 2013 when it was assigned a first-time international rating of A3 from Moody's Investors Services and put in place two euro medium-term note programmes. It has since tapped the CNH, Hong Kong dollar, US dollar and Singapore dollar markets.

"Also, as the yield and exchange rate moved against the ringgit in the past two years, foreign investors found it cheaper to invest in ringgit paper, which is why we see the influx of these foreign investors into Cagamas' credit," adds Chung.

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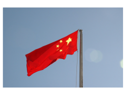

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