SECTION 4

# Debt Management

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## Overview

The formulation of effective debt management strategies together with the development of domestic market continue to be the main priorities for debt managers. The debt burden has been rising across countries for the last decade and further compounded by the impact of COVID-19 pandemic as governments need to provide fiscal stimulus and assistance packages that require additional financing to keep the economy afloat. Debt levels and vulnerabilities are expected to remain elevated due to large financing needs and high cost of borrowing coupled with global monetary tightening. Amid rising vulnerabilities and a more complex debt profiles, the challenge remains in balancing between the optimal level of financing and its impact to government debt accumulation. Thus, effective debt management is crucial in reducing debt level and vulnerabilities through strong macroeconomic policies and prudent fiscal measures for nation-building.

During the period from 2020 to 2022, the Federal Government was able to tap more than RM280 billion, among others, to finance pandemic response measures. The unprecedented large borrowing to finance the deficit sourced entirely from domestic market at an acceptable cost demonstrates a well-functioning and resilient capital market that supports a strong debt management strategy amid challenging external environment. Therefore, the Government will continue its prudent debt management strategies while adhering to the debt rules. Moving ahead, the Government's crisis-related extraordinary borrowings will be reduced to conform to fiscal consolidation efforts as the economy recovers post-pandemic.

In this regard, the ringgit-denominated issuance will be given priority to further support the domestic capital market and minimise the foreign exchange risk. The issuances will be focused on medium- and long-tenured securities to smoothen the debt maturity profiles. Furthermore, the Government will continue to uphold transparency and ensure a well-functioning and high liquidity domestic market through an open bidding issuance which will attract diverse investors, thus encouraging competitive pricing.

## Financing

The Federal Government's effective borrowing programme is needed to finance fiscal deficit and refinance maturing debts. Total gross borrowings for 2023 are estimated to record RM228.5 billion or 12.4% of GDP with RM93.2 billion for deficit financing, while RM135.3 billion for principal repayments. The principal repayments consist of maturing Malaysian Government Securities (MGS) at RM38.3 billion, Malaysian Government Investment Issues (MGII) at RM39 billion, treasury bills at RM54 billion, Government Housing Sukuk (SPK) at RM3.6 billion and offshore borrowings at RM0.3 billion.

Sufficient liquidity in the domestic market enables the Government to raise its entire borrowings in 2023 through ringgit-denominated instruments. The total issuances of MGS and MGII are expected to amount to RM91 billion and RM95 billion or 39.8% and 41.6% of total gross borrowings, respectively, while the remaining 18.6% or RM42.5 billion will be financed through the issuances of treasury bills. As at end-August 2023, the

Government has raised RM166.5 billion or 72.8% of total gross borrowings through 26 issuances of both MGS and MGII amounted to RM129.5 billion as well as 16 issuances of treasury bills at RM37 billion. Of the total, principal repayments stood at RM99.5 billion while the balance of RM67 billion was for deficit financing and prefunding the maturing debts in the upcoming months.

**TABLE 4.1.** *Federal Government Financing, 2022 – 2023*

| | RM MILLION | | SHARE (%) | |
|---|---|---|---|---|
| | 2022 | 2023[2] | 2022 | 2023[2] |
| **Gross borrowings** | **230,949** | **228,500** | ***100.0*** | ***100.0*** |
| **Domestic** | **230,949** | **228,500** | ***100.0*** | ***100.0*** |
| MGS | 86,500 | 91,000 | *37.5* | *39.8* |
| MGII | 85,000 | 95,000 | *36.8* | *41.6* |
| Treasury bills | 59,449 | 42,500 | *25.7* | *18.6* |
| **Offshore** | **-** | **-** | **-** | **-** |
| Market loans | - | - | - | - |
| Project loans | - | - | - | - |
| **Repayments** | **131,528** | **135,220** | ***100.0*** | ***100.0*** |
| Domestic | 131,262 | 134,920 | *99.8* | *99.8* |
| Offshore | 266 | 300 | *0.2* | *0.2* |
| **Net borrowings** | **99,421** | **93,280** | **-** | **-** |
| Domestic | 99,687 | 93,580 | - | - |
| Offshore | -266 | -300 | - | - |
| **Change in assets[1]** | **61** | **-40** | **-** | **-** |
| **Total deficit financing** | **99,482** | **93,240** | **-** | **-** |

[1] (+) indicates drawdown of assets; (-) indicates accumulation of assets
[2] Estimate
Source: Ministry of Finance, Malaysia

Based on the overwhelming demand for the Sustainability MGII issuance in 2022, the Government has reopened the paper on 28 February 2023 amounting to RM5.5 billion to further reiterate its commitment towards the 2030 Sustainable Development Agenda. The issuance received strong demand from local financial institutions, institutional investors as well as insurance companies and was oversubscribed by two times. To date, the issuance has achieved its target of RM10 billion, as announced in the Budget 2022.

The Government's fund raising activities for 2023 are conducted mainly through auctions, constituting 87% of total gross borrowings in view of the market's ability to absorb the high supply, while the balance are issued via private placement to support longer tenured issuances. In addition, the Government is projected to reopen 33 out of 37 issuances of medium- and long-tenured papers in its continuous efforts to consolidate the number of outstanding papers in line with the investors' demand, while the balance were new issuances. All borrowing operations are conducted through Fully Automated System for Issuing/Tendering (FAST) to ensure fairness and market transparency.

The Government issues a wide range of instruments with maturities ranging from 3-month to 30-year to smoothen debt maturity profile while meeting investors' demand. As part of the borrowing strategy, the Government aims to manage refinancing risk by reducing the issuance of short-term papers and increasing the issuance of medium- and long-term instruments as the pricing spread between the maturities narrowed. Thus, the composition of short-term papers (less than a year) is estimated at 18.6% of total gross borrowings and medium-term papers (3- to 7-year) at 37.2%. Meanwhile, long-term papers (10-year and above) are expected to be higher at 44.2%. Overall, the weighted average time to maturity for 2023 issuances is expected to remain favourable around 10.3 years (2022: 9.3 years). This is in accordance to the debt management strategy in minimising rollover risks to ensure a well-spread maturity profile.

Between March 2022 until August 2023, the US Federal Reserve has aggressively raised the Federal Funds Rates (FFR) by a cumulative of 525 basis points (bps) to the range of 5.25% and 5.50% to record the highest level over two decades. Meanwhile, the Monetary Policy Committee of BNM has moderately increased the OPR by 125 bps cumulatively from 1.75% to 3.00% during the same period in line with global monetary tightening and outlook of domestic inflation and growth. The moderate adjustment, however, does not distort the demand from foreign investors on Government papers which remained strong as risk appetite and market sentiment improved. Hence, total foreign flow of the Federal Government instruments in the first eight months registered a net inflow of RM27.9 billion (end-August 2022: RM0.27 billion). In addition, foreign investors were more attracted to longer tenured instruments which offers competitive returns largely on the expectations that there will be no further hike in the FFR.

Meanwhile, the MGS yields were relatively stable despite a broad increase in the US Treasury and other global bond yields during the first eight months of 2023. The MGS yield has declined by an average of 25 bps, with benchmark yield on 3-, 5-, 7- and 10-year recorded at 3.450%, 3.590%, 3.740% and 3.840%, respectively. Similarly, MGS yield on instruments with maturity beyond 10 years trended downwards mainly driven by improved investor risk appetite and better overall market conditions. However, the Government's weighted average cost of borrowing has increased from 3.765% in 2022 to 4.047% as at end-August 2023 as a result of higher coupon rate of short-term papers amid global financial tightening and liquidity challenges.

The MGS and MGII auctions received a total bid of RM228.3 billion for market issuances of RM106 billion during the first eight months of 2023. The Government has received a favourable bidding with a bid-to-cover (BTC) ratio of 2.15 times, reflecting a strong demand from the investors supported by the deep and liquid domestic market. From the tenure perspective, the demand for both medium- and long-term papers recorded BTC ratios of 2.12 times and 2.20 times, respectively. Overall, the steady BTC ratios reflect investors' confidence towards Malaysia's economic performance and growth prospects.

Malaysia continues to spearhead the Islamic capital market with a share of 38.8% of total global sukuk issued as at end-July 2023. The Government continues to support the development of Malaysia's Islamic capital market with substantial issuances of Shariah-compliant papers. In this regard, the issuance of MGII and Malaysian Islamic Treasury Bills (MITB) in 2023 is expected to reach 60% of total gross borrowings. From the pricing perspective, spread between the MGS and MGII yields have been on a narrowing trend. As at end-August 2023, the spread has declined to an average of 3 bps, particularly the 3-year paper which narrowed by 8 bps while 10-year by 2 bps. Furthermore, bidding interest of the MGII for the first eight months of 2023 was oversubscribed by 2.18 times from the total issuance of RM65 billion contributed by a steady acceptance and larger portfolio investment allocation for Shariah-compliant instruments. The oversubscribed issuances reflected strong demand for Islamic papers supported by the enabling environment in the domestic market.

## Federal Government Debt

The unprecedented additional borrowings incurred during the pandemic resulted in the increase of Federal Government debt level and still impacting the public finance. Therefore, due to the elevated debt-to-GDP ratio and the financing requirement under the Twelfth Malaysia Plan, 2021-2025 (Twelfth Plan), the Government maintained the statutory debt limit at 65% of GDP under the Loan (Local) (Statutory Ceiling for Borrowing) and Government Funding (Statutory Ceiling of Moneys Received) Order 2022 [*P.U. (A) 399/2022*] which came into effect on 1 January 2023. As at end-August 2023, the Federal Government statutory debt which comprises MGS, MGII and MITB recorded 59.9% of GDP, below the stipulated debt ceiling.

Meanwhile, the statutory debt limit for offshore borrowings and Malaysia Treasury Bill (MTB) as governed under the External Loans Act 1963 [*Act 403*] and Treasury Bills (Local) Act 1946 [*Act 188*] remained at RM35 billion and RM10 billion, respectively. In this regard, offshore borrowings as at end-August 2023 amounted to RM30 billion while MTB stood at RM3.5 billion, of which these instruments' outstanding are still within the stipulated thresholds.

**TABLE 4.2.** *Debt Legislative*

| ACT | STATUTORY LIMIT | END-AUGUST 2023 |
|---|---|---|
| **Loan (Local) Act 1959 [*Act 637*][1]**<br>**Government Funding Act 1983 [*Act 275*][2]** | Outstanding MGS, MGII and MITB not exceeding 65% of GDP | **59.9% of GDP** |
| **External Loans Act 1963 [*Act 403*]** | Offshore borrowings not exceeding RM35 billion | **RM30 billion** |
| **Treasury Bills (Local) Act 1946 [*Act 188*]** | MTB not exceeding RM10 billion | **RM3.5 billion** |

[1] Instrument issued under Act 637 is MGS
[2] Instruments issued under Act 275 are MGII and MITB
Source: Ministry of Finance, Malaysia

As at end-August 2023, the total Federal Government debt stood at RM1,147.1 billion or 62% of GDP, largely denominated in ringgit with a share of 97.4% of the total debt, while the remaining 2.6% was in foreign currencies. Out of the total debt, Shariah-compliant instruments constituted RM569.2 billion or 49.6%, signifying Government continuous support for development of the Islamic capital market. The large composition of these instruments at 96.5% were denominated in ringgit while the remaining were in US dollar.

Domestic debt is diversified across various maturities and type of instruments. Short-term domestic debt with less than 12-month maturities are MTB amounted to RM3.5 billion and MITB at RM31 billion, while medium- and long-term domestic debt with maturities ranging from 3- to 30-year comprise MGS amounted to RM564.3 billion and MGII at RM512.8 billion. Another component is SPK which registered RM5.5 billion and will be fully redeemed in 2024. Meanwhile, Malaysia's exposure to foreign exchange risk is minimal

**TABLE 4.3.** *Federal Government Debt by Instrument, 2022 – 2023*

| COMPONENT | RM MILLION | | SHARE (%) | | SHARE OF GDP (%) | |
|---|---|---|---|---|---|---|
| | 2022 | 2023[1] | 2022 | 2023[1] | 2022 | 2023[1] |
| **Domestic debt** | **1,050,078** | **1,117,158** | ***97.3*** | ***97.4*** | ***58.6*** | ***60.4*** |
| MGS | 538,178 | 564,358 | *49.9* | *49.2* | *30.0* | *30.5* |
| MGII | 471,300 | 512,800 | *43.7* | *44.7* | *26.3* | *27.7* |
| SPK | 9,100 | 5,500 | *0.8* | *0.5* | *0.5* | *0.3* |
| Treasury bills | 31,500 | 34,500 | *2.9* | *3.0* | *1.8* | *1.9* |
| **Offshore borrowings** | **29,513** | **29,974** | ***2.7*** | ***2.6*** | ***1.7*** | ***1.6*** |
| Market loans | 25,543 | 26,298 | *2.3* | *2.3* | *1.5* | *1.4* |
| Project loans | 3,970 | 3,676 | *0.4* | *0.3* | *0.2* | *0.2* |
| **Total** | **1,079,591** | **1,147,132** | ***100.0*** | ***100.0*** | ***60.3*** | ***62.0*** |
| *Memorandum item:*<br>Non-resident holdings of ringgit-denominated debt securities | 233,208 | 261,081 | *22.2* | *23.4* | *13.0* | *14.1* |

[1] End-August 2023
Source: Ministry of Finance, Malaysia

due to a small share of offshore borrowings which registered RM30 billion. The offshore borrowings consist of market loans totalling RM26.3 billion which denominated in US dollar (75.8%) and yen (24.2%), while project loans amounted to RM3.7 billion were primarily in yen (97.6%) and the balance were in other currencies.

Resident holdings of the Federal Government debt as at end-June 2023 amounted to RM863.4 billion, representing 75.4% of the total debt. Resident holders are comprised of various entities with banking institutions held the largest share at 30.5% followed by the Employees Provident Fund at 24.8%. In addition, insurance companies held 4.9%, BNM (4.4%), Retirement Fund (Incorporated) (3%), development financial institutions (2.2%) and others (5.6%).

Meanwhile, non-resident holdings registered RM281.6 billion or 24.6% of the total debt. Foreign long-term institutions collectively held 10.8%, namely central bank and sovereigns (5.8%), pension funds (4.2%) and insurance companies (0.8%). The balance was held by fund managers (8.3%), banking institutions (5%) and others (0.5%).

**TABLE 4.4.** *Federal Government Debt by Holder, 2022 – 2023*

| COMPONENT | RM MILLION | | SHARE (%) | | SHARE OF GDP (%) | |
|---|---|---|---|---|---|---|
| | 2022 | 2023[3] | 2022 | 2023[3] | 2022 | 2023[3] |
| **Resident** | **821,370** | **863,431** | ***76.1*** | ***75.4*** | ***45.9*** | ***46.7*** |
| Employees Provident Fund | 265,685 | 284,129 | *24.6* | *24.8* | *14.8* | *15.4* |
| Retirement Fund (Incorporated) | 29,748 | 33,806 | *2.8* | *3.0* | *1.7* | *1.8* |
| Insurance companies | 52,547 | 56,522 | *4.9* | *4.9* | *2.9* | *3.1* |
| Bank Negara Malaysia | 68,525 | 50,841 | *6.3* | *4.4* | *3.8* | *2.7* |
| Banking institutions | 322,459 | 349,507 | *29.9* | *30.5* | *18.0* | *18.9* |
| Development financial institutions | 22,129 | 24,514 | *2.0* | *2.2* | *1.3* | *1.3* |
| Others[1] | 60,277 | 64,112 | *5.6* | *5.6* | *3.4* | *3.5* |
| **Non-resident** | **258,221** | **281,587** | ***23.9*** | ***24.6*** | ***14.4*** | ***15.2*** |
| Fund manager | 86,014 | 94,656 | *8.0* | *8.3* | *4.8* | *5.1* |
| Central bank and sovereigns | 73,709 | 67,046 | *6.8* | *5.8* | *4.1* | *3.6* |
| Banking institutions | 36,773 | 57,161 | *3.4* | *5.0* | *2.1* | *3.1* |
| Pension funds | 47,887 | 47,877 | *4.4* | *4.2* | *2.7* | *2.6* |
| Insurance companies | 7,946 | 9,135 | *0.7* | *0.8* | *0.4* | *0.5* |
| Others[2] | 5,892 | 5,712 | *0.6* | *0.5* | *0.3* | *0.3* |
| **Total** | **1,079,591** | **1,145,018** | ***100.0*** | ***100.0*** | ***60.3*** | ***61.9*** |

[1] Include other non-bank financial institutions, statutory bodies, nominees and trustee companies, co-operatives, securities placed by institutional investors at the central bank and unclassified items
[2] Include individuals, non-financial corporations, multilateral and bilateral institutions as well as unidentified sectors
[3] End-June 2023
Source: Ministry of Finance, Malaysia

In 2023, the Federal Government allocated RM46.1 billion or 15.2% of revenue (2022: RM41.3 billion; 14%) for debt service charges (DSC). The DSC-to-revenue ratio stood higher than last year as a result of the elevated debt level. The DSC is primarily for domestic issuance estimated at RM45.3 billion, while the remaining RM0.8 billion is for offshore borrowings. In this regard, the weighted average cost of borrowing for outstanding domestic debt as at end-August 2023 recorded at 4.095% (2022: 4.031%).

The weighted average time to maturity for outstanding debt securities is estimated to lengthen at 9.5 years (2022: 9.0 years) as a result of a notable shift in the composition of the medium- and long-term papers with remaining maturities of six years and above, constituting 58.3% in 2023 higher than 2022 (56.3%). Conversely, the proportion of securities with remaining maturities of five years and below is reduced to 41.7% from the previous year (43.7%). This signifies a strategic move in managing refinancing risk towards a well-spread maturity profile.

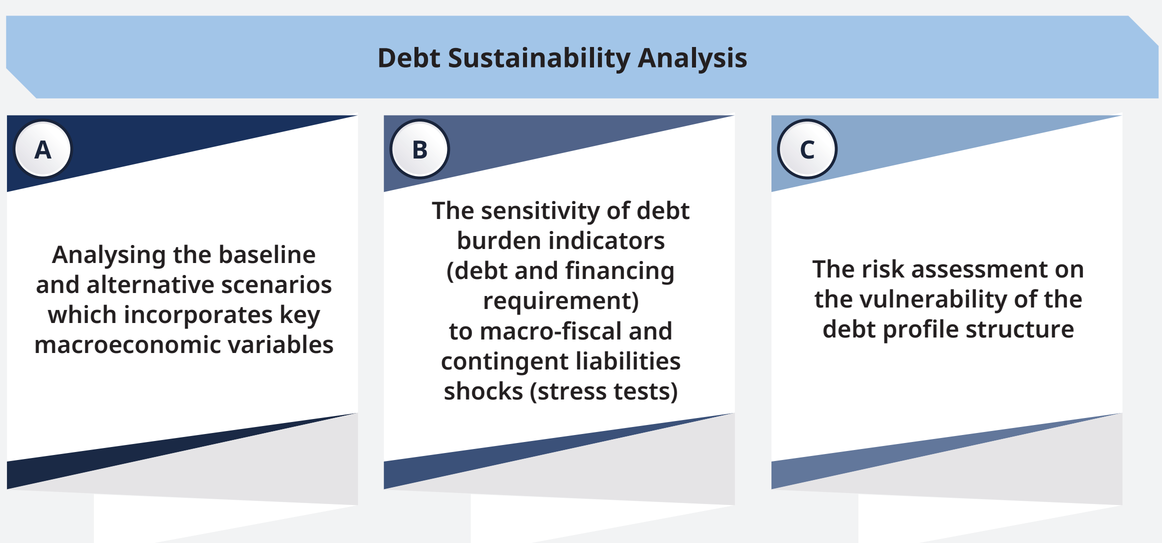
FEATURE ARTICLE

## Malaysia's Debt Sustainability Analysis 2023

### Introduction

The Federal Government of Malaysia has applied the Debt Sustainability Analysis (DSA) framework developed by the IMF and the World Bank as a risk assessment tool since 2019. The DSA assessment is imperative to guide the government's fiscal conduct as well as borrowing and debt strategy, to enable the country absorb any shocks in the medium- and long-term, and avoid payment difficulties. A country's debt sustainability is determined by the government's ability to serve all its current and future payment obligations without requiring exceptional financial assistance or experiencing default. Furthermore, the reporting of DSA also provides greater insight to the creditors and investors on potential debt-related shocks such as economic downturn, monetary policy tightening, depreciation in exchange rate and higher deficit. The report will also assist in investment portfolio planning and financing terms customisation. Figure 1 highlights the reporting of DSA for the Federal Government debt.

**FIGURE 1.** *DSA's Main Highlights*




Source: Ministry of Finance, Malaysia and IMF

The DSA outcomes are translated into debt and gross financing needs (GFN) projections as a percentage to GDP. In addition, the outcomes also highlight and summarise the shock exposures to the debt levels and borrowing requirements. Under the DSA framework, the threshold of debt burden for emerging markets are set at a level of 70% for debt-to-GDP ratio and 15% for GFN-to-GDP ratio. In June 2022, the IMF and the World Bank have initiated a gradual adoption of the Sovereign Risk and Debt Sustainability Framework (SRDSF) which will eventually replace the DSA. Consequently, Malaysia plans to apply the SRDSF as an internal assessment once it is fully ready and rolled out by the IMF.

### Analyses

### A. Scenario Analyses

#### i. Baseline Scenario

This DSA covers the projection period from 2023 to 2028. The main underlying macro-fiscal assumptions used in the DSA are in line with the Federal Government's Medium-Term Fiscal Framework as shown in Table 1.

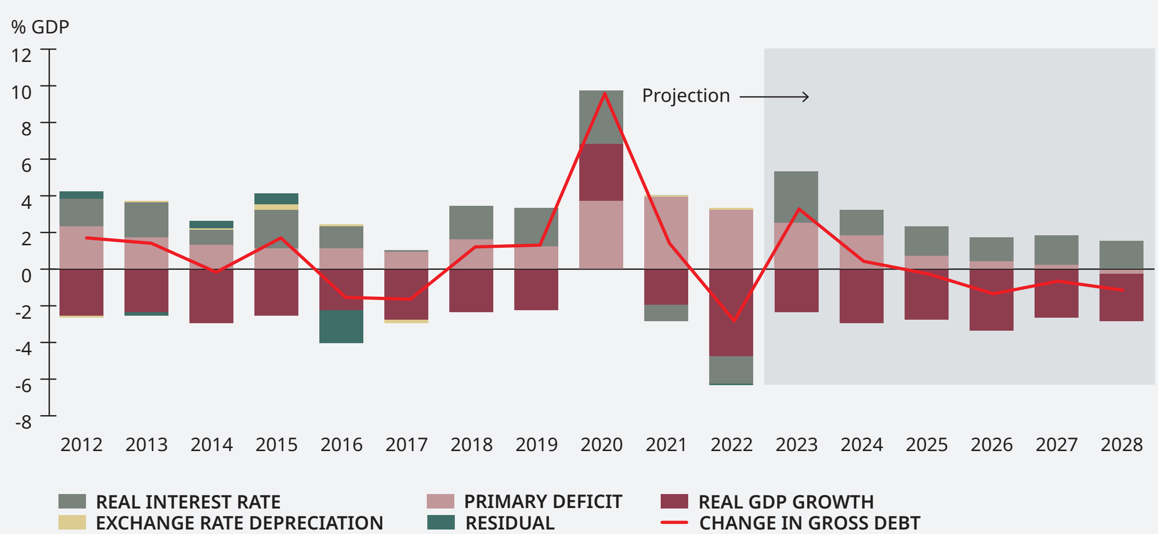
**TABLE 1.** *DSA 2023 Macro-Fiscal Indicators*

| MACRO-FISCAL INDICATORS | AVERAGE 2023 – 2028 (% PER ANNUM) |
|---|---|
| Real GDP growth | 4.5 |
| Revenue growth | 4.3 |
| Non-interest expenditure growth | 1.0 |
| Interest rate[1] | 4.2 |

Source: Ministry of Finance, Malaysia

For 2012 – 2022, primary deficit and real interest rate are the two major factors that contributed to the increase in debt-to-GDP ratio. In contrast, real GDP growth has lessened the debt-to-GDP ratio, except in 2020, and is projected to continue in a similar trend for the next five years as shown in Figure 2. Nevertheless, the debt ratio will further improve attributed to gradual reduction in the size of primary deficit as a result of fiscal consolidation efforts.

**FIGURE 2.** *Debt-Creating Flow*




Source: Ministry of Finance, Malaysia and IMF

[1] The interest rate refers to the coupon/profit rate of the Federal Government debt instruments.

Under the baseline scenario, the debt-to-GDP ratio is estimated to record about 63% in 2023 and trend down to slightly below 60% in 2028. Likewise, the annual gross borrowing size reflects the fiscal consolidation trajectory with GFN-to-GDP ratio forecast to gradually reduce to 5.6% in 2028 compared with 12.3% in 2023.

### ii. Alternative Scenarios

The alternative scenarios reveal potential changes in the country's debt outlook if the current fiscal policy remains unchanged. These scenarios assess the debt and borrowing projections for the medium-term, using the underlying assumption of a constant primary balance and historical performance data, individually.

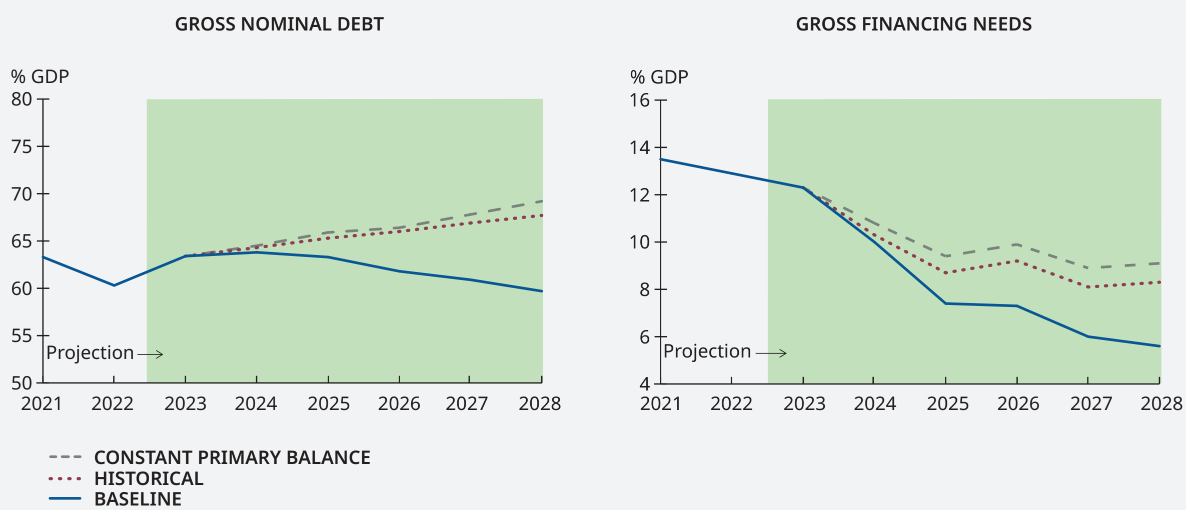
#### (a) Constant Primary Balance Scenario

Assuming a constant primary deficit of 2.5% of GDP throughout the projection period of five years, the debt-to-GDP is projected to almost reach the DSA threshold of 70% in 2028. This level is alarming as it will surpasses the Federal Government statutory debt limit of 65% starting 2025. Moreover, the GFN for the period is anticipated to average around 10% of GDP annually. Thus, a higher amount of borrowings is required in the absence of consolidation measures.

#### (b) Historical Scenario

By imputing an average of ten years historical data (2013 – 2022) of primary deficit-to-GDP (2%), economic growth (4.2%) and interest rate (4.0%), the debt-to-GDP ratio will increase to 67.7% in 2028. Although this ratio is slightly below the DSA benchmark, it will exceeds the Federal Government statutory debt limit starting 2025. Meanwhile, the amount of GFN is estimated at 8.3% of GDP in 2028. These scenarios are depicted as in Figure 3.

**FIGURE 3.** *Baseline and Alternative Scenarios*




Source: Ministry of Finance, Malaysia and IMF

## B. Sensitivity Analyses

Conducting sensitivity analyses or stress tests enable governments to evaluate potential impacts of various macro-fiscal shocks on the level of indebtedness. Consequently, appropriate policy measures can be tailored and implemented ahead in order to mitigate the effects if such circumstances arise.

### i. Primary Balance Shock Scenario

Assuming another pandemic crisis occurs in 2024 and 2025, and similar fiscal measures were to be introduced which led the primary deficit to surge to 3.8% of GDP, the debt-to-GDP ratio is projected to peak at 68.5% in 2025 and slightly decline to 67.3% in 2028. Similarly, GFN is expected to remain elevated at 12% of GDP in 2024 and moderate to 7.4% in 2028. While the debt-to-GDP ratio remains within the DSA threshold, the ratio exceeds the statutory debt limit of 65% throughout the projection period. The analysis demonstrates that accumulated high borrowings during crisis years to finance additional fiscal measures will result in a prolonged debt-scarring effect.

### ii. Real GDP Growth Shock Scenario

Assuming real GDP contracts by 5.5% in 2024, rebounds to 3.3% in 2025 and thereafter averages at 4.8% for the rest of the projection period, the debt-to-GDP ratio is forecast to increase and peak at 77.8% in 2025 and gradually decline to 73.5% in 2028. Similarly, the GFN-to-GDP ratio trends upward to 13.6% in 2024 and gradually declines to 6.9% in 2028. The debt-to-GDP ratio under this shock exceeds both the DSA threshold and the Federal Government statutory debt limit. The contraction in real GDP will increase the debt-to-GDP ratio as most of the macroeconomic indicators deteriorated and affect the primary deficit and borrowing cost.

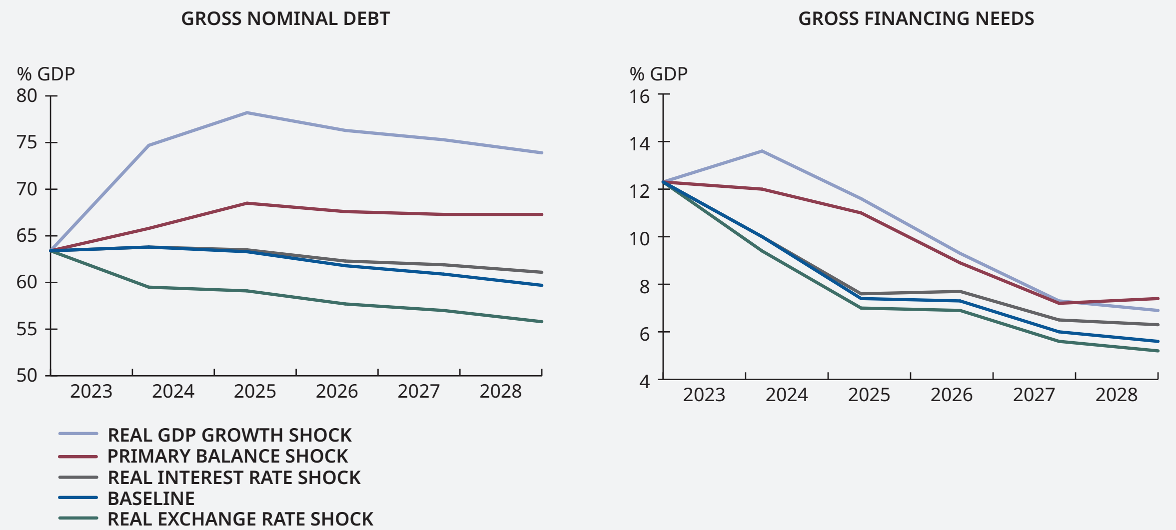
### iii. Real Interest Rate Shock Scenario

With the assumption that the interest rate rises by almost 230 basis points annually, the simulation does not significantly deviate the debt-to-GDP and GFN-to-GDP ratio trajectories for 2024 – 2028 from the baseline projections. The widest gap between this shock and baseline scenario is in 2028 of which the debt-to-GDP ratio is estimated at 61.1% (baseline: 59.7%), while GFN-to-GDP ratio is at 6.3% (baseline: 5.6%). The slight increase in the debt-to-GDP projection ratio is attributed to the increase in cost of borrowings. This scenario shows that the debt and financing projection does not breach the DSA thresholds and the Federal Government statutory debt limit.

### iv. Exchange Rate Shock Scenario

Assuming the ringgit depreciates unexpectedly around 30% annually against the baseline without any policy intervention, this scenario leads to higher prices resulting in higher nominal GDP. Thus, the debt-to-GDP and GFN-to-GDP ratios are projected to improve to record 55.8% and 5.2%, respectively, in 2028. This is attributed to the low share of foreign currency denominated debt which constitutes less than 3% of the total Federal Government debt.

**FIGURE 4.** *Macro-Fiscal Stress Tests*




Source: Ministry of Finance, Malaysia and IMF

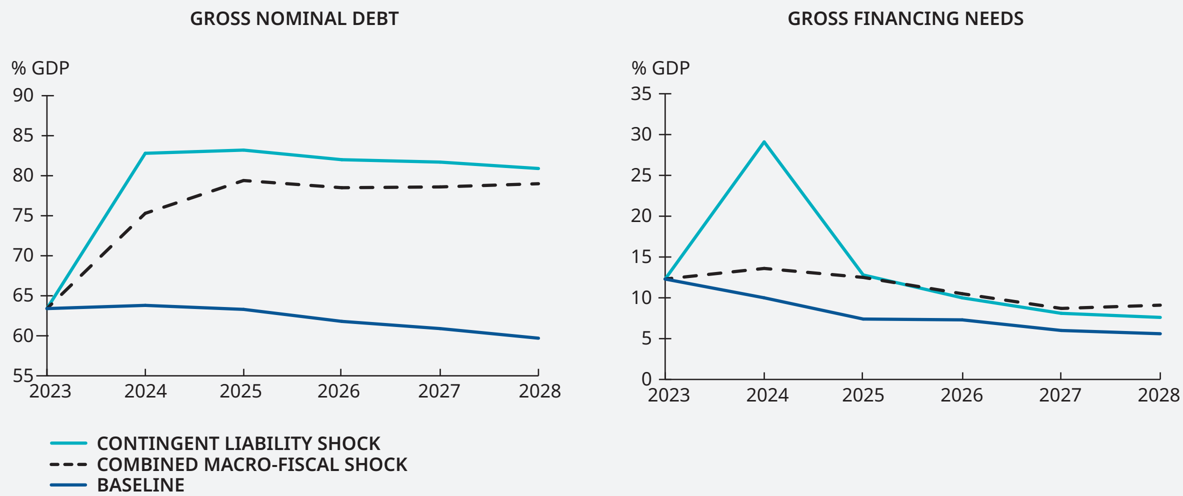
v. **Combined Macro-Fiscal Shock Scenario**

Assuming all macro-fiscal shocks materialise concurrently, the debt and GFN trajectories reveal substantial increases during the projection period. The debt-to-GDP ratio exceeds the DSA threshold from as early as 2024 at 75.3%, then continues to elevate in 2025 and hovers around 79% from 2026 onwards. However, the GFN-to-GDP ratio declines from 13.6% in 2024 to 9.1% in 2028. Under this scenario, the debt level surpasses both the DSA threshold and the statutory debt limit throughout the projection period. This scenario reflects the increase in financial and macroeconomic burden during a major crisis, which lead to the exponential increase in debt level. This unfavourable trajectory poses risks to the country should no specific mitigating measures are undertaken.

vi. **Contingent Liability Shock Scenario**

Assuming the Government is required to fulfil all its contingent liabilities, which constitute approximately 12% of GDP in 2024, the debt-to-GDP ratio is expected to surge to 82.8% in 2024 and gradually reduce to 80.9% in 2028. The GFN-to-GDP ratio will escalate exponentially to 29.1% in 2024 and averages around 10% during 2025 – 2028. This is the worst-case scenario among all shocks due to the debt-scarring effect resulting from additional debt burden incurred by the Federal Government in financing the committed liabilities. This leads to a continuous increase in the debt trajectory, exceeding both the DSA threshold and the statutory debt ceiling. Furthermore, this is the only scenario of which the GFN ratio surpasses the DSA threshold. The debt-to-GDP and GFN-to-GDP trajectories for all scenarios are shown in Figure 4 and Figure 5.

**FIGURE 5.** *Additional Stress Tests*




Source: Ministry of Finance, Malaysia and IMF

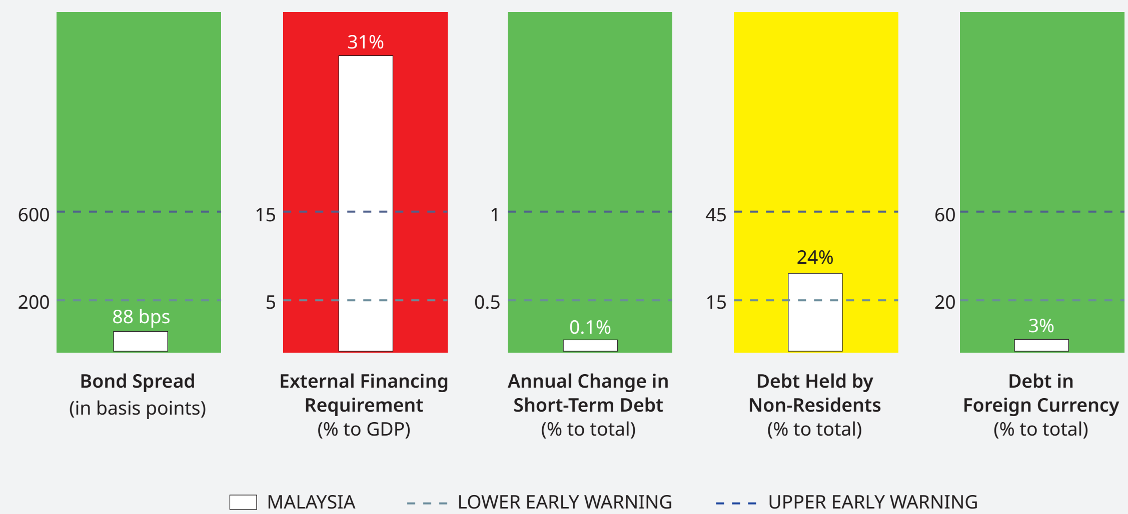
## C. Risk Assessment

### i. Debt Profile Risk

In addition to the macro-fiscal and contingent liabilities stress tests, the DSA also provides a comprehensive risk assessment in evaluating the current debt profile of a country. Under this assessment[2], the external debt financing requirement[3] is categorised as high risk since it surpasses the upper early warning threshold which increases the Government exposure to foreign exchange risk. Meanwhile, the Federal Government debt instruments held by non-residents poses a moderate risk as it surpasses the lower early warning threshold. In the event of capital flight, this could result in an oversupply of the Government papers in the domestic market. However, currently these risks are mitigated by the availability of sufficient private sector external assets and operation of deep and liquid domestic capital market. Furthermore, the Government continues to monitor the orderly functioning of the financial market. Lower and upper risk assessment for each debt profile parameter is illustrated in Figure 6.

[2] Based on 2022 data.
[3] External financing requirement in this assessment also include private sector's external debt.

**FIGURE 6.** *Debt Profile Vulnerabilities*

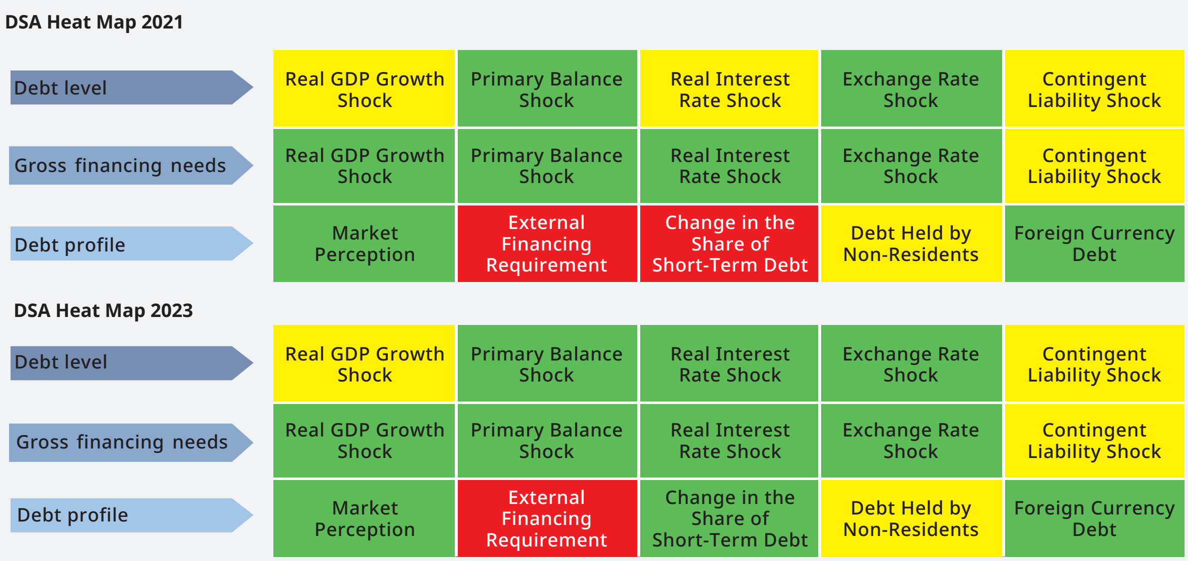



Source: Ministry of Finance, Malaysia and IMF

## Finding - Heat Map

The heat map illustrates an overview on the severity of risk of the country's debt level and GFN from the various shock scenarios and the debt profile. This assessment aims to compare the heat map of DSA 2023 with DSA 2021[4] as shown in Figure 7a and the risks indicators as shown in Figure 7b.

**FIGURE 7a.** *Simulation of DSA Heat Map for Malaysia (2021 vs 2023)*




Source: Ministry of Finance, Malaysia and IMF

[4] The DSA 2021 report can be referred in Fiscal Outlook and Federal Government Revenue Estimates 2022.

**FIGURE 7b.** *Risk Indicators for Debt Level, GFN and Debt Profile*

| Heat Map | Debt Level | Gross Financing Needs | Debt Profile |
|---|---|---|---|
| Low Risk | If the debt level does not exceed the 70% of GDP threshold under baseline or specific shock scenarios | If the gross financing needs do not exceed the 15% of GDP threshold under baseline or specific shock scenarios | If the country's value is less than the lower early warning parameters |
| Moderate Risk | If the debt level exceeds the 70% of GDP threshold under the specific shock scenarios but not baseline | If the gross financing needs exceed the 15% of GDP threshold under the specific shock scenarios but not baseline | If the country's value is in between the lower and upper early warning parameters |
| High Risk | If the debt level exceeds the 70% of GDP threshold under baseline | If the gross financing needs exceed the 15% of GDP threshold under baseline | If the country's value exceeds the upper early warning parameters |

Source: Ministry of Finance, Malaysia and IMF

Improvements were observed for Malaysia's debt level and debt profile in the DSA 2023 heat map compared with 2021. In the DSA 2023 debt level, real interest rate shock carries low risk to the Government. This implies a lower borrowing requirement as a result of fiscal consolidation efforts. In terms of debt profile vulnerabilities, the share of short-term debt has significantly improved in 2023 as compared to 2021 and no longer poses a high risk to the country. This is due to the high repayment of treasury bills which leads to a reduction in the outstanding of short-term financing instruments.

Even though the external debt financing requirement remains at high risk, the possibility of defaulting in the offshore borrowing is unlikely. This is due to the sizeable asset availability and good creditworthiness among external debt issuers. Furthermore, prudential requirement on liquidity and funding risk management imposed by the regulator also support to alleviate the risk.

However, the real GDP growth shock remains at moderate risk level despite the country transitioning from the COVID-19 pandemic to endemic phase. Debt held by non-residents also stays at moderate risk of which the composition has remained stagnant around 24% of total debt since 2019. Above all, the contingent liabilities shock would pose a major concern to the Government in the event it materialises which require immediate mitigation measures to contain the surge of the debt level and manage financing needs accordingly.

Overall, the identified risks are manageable given the implementation of fiscal measures. Continuous effort should be taken in order to rebuild wider fiscal buffers, thus ensuring all shocks are within the low-risk parameters.

**Conclusion**

The DSA illustrates that higher economic growth and fiscal surplus are the two main determinants which could swiftly reduce the Federal Government debt-to-GDP ratio. In this regard, expediting the implementation of planned fiscal reforms and enhancing debt management strategies are pertinent. The adoption of the proposed Public Finance and Fiscal Responsibility Act is aspired to further improve debt sustainability, complemented by the rollout of the Medium-Term Revenue Strategy and expenditure reviews to propel the fiscal consolidation path. These initiatives contribute towards improving fiscal soundness, ensuring debt sustainability and alleviating vulnerabilities of the country in the medium- and long-term.

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## Malaysia's External Debt

As at end-June 2023, external debt[1] increased by 6% to RM1,213.1 billion or 65.6% of GDP mainly attributed to higher offshore borrowings, non-resident holdings of ringgit-denominated debt securities and non-resident deposits. Offshore borrowings have increased to RM646.2 billion and remained the largest component, representing 53.3% of total external debt. The increase in offshore borrowings was mainly contributed by higher net foreign currency loans from the private sector and valuation effects following the appreciation of the US dollar. Similarly, non-resident holdings of ringgit-denominated debt securities and deposits increased to RM267.9 billion and RM134.3 billion, respectively. Larger holdings of the non-resident in ringgit-denominated debt securities were attributed to improved investors demand for Government papers, while higher non-resident deposits were driven by increased deposits in the domestic banking system. Furthermore, other external debt increased to RM164.7 billion following higher trade credits. Overall, the country's external debt remained manageable given its favourable maturity profile, with medium- and long-term debt constituting a higher share at 58.2% compared to short-term debt (41.8%). Nonetheless, a sufficient balance of international reserves at 1.0 times of short-term external debt mitigates the refinancing risk.

**TABLE 4.5.** *External Debt, 2022 – 2023*

| COMPONENT | RM MILLION | | SHARE (%) | | SHARE OF GDP (%) | |
|---|---|---|---|---|---|---|
| | 2022 | 2023[3] | 2022 | 2023[3] | 2022 | 2023[3] |
| **Offshore borrowings** | **625,712** | **646,213** | ***54.7*** | ***53.3*** | ***34.9*** | ***34.9*** |
| Medium- and long-term debt | 382,895 | 401,540 | *33.5* | *33.1* | *21.3* | *21.7* |
| Public sector | 145,823 | 144,614 | *12.8* | *11.9* | *8.1* | *7.8* |
| Federal Government | 25,013 | 25,557 | *2.2* | *2.1* | *1.4* | *1.4* |
| Public corporations | 120,810 | 119,057 | *10.6* | *9.8* | *6.7* | *6.4* |
| Private sector | 237,072 | 256,926 | *20.7* | *21.2* | *13.2* | *13.9* |
| Short-term debt | 242,817 | 244,672 | *21.2* | *20.2* | *13.6* | *13.2* |
| **Non-resident holdings of ringgit-denominated debt securities** | **246,565** | **267,899** | ***21.5*** | ***22.1*** | ***13.8*** | ***14.5*** |
| Medium- and long-term debt | 238,158 | 258,937 | *20.8* | *21.4* | *13.3* | *14.0* |
| Federal Government | 226,078 | 248,589 | *19.7* | *20.5* | *12.6* | *13.4* |
| Others[1] | 12,080 | 10,348 | *1.1* | *0.9* | *0.7* | *0.6* |
| Short-term debt | 8,408 | 8,961 | *0.7* | *0.7* | *0.5* | *0.5* |
| **Non-resident deposits** | **111,572** | **134,310** | ***9.8*** | ***11.0*** | ***6.2*** | ***7.3*** |
| **Others[2]** | **160,814** | **164,681** | ***14.0*** | ***13.6*** | ***9.0*** | ***8.9*** |
| **Total** | **1,144,663** | **1,213,102** | ***100.0*** | ***100.0*** | ***63.9*** | ***65.6*** |

[1] Include private sector and public corporations
[2] Comprise trade credits, IMF allocation of Special Drawing Rights and miscellaneous
[3] End-June 2023
Note: Total may not add up due to rounding
Source: Bank Negara Malaysia

[1] The nation's external debt constitutes the public and private sector offshore borrowings, non-resident holdings of ringgit-denominated debt securities, non-resident deposits as well as other external debt

# Public Sector Debt

The public sector debt as at end-June 2023 increased by 4.2% to RM1,541.9 billion or 83.3% of GDP on account of higher Federal Government debt which constituted 74.3% of the total debt. In contrast, statutory bodies guaranteed debt decreased marginally to record RM94.6 billion attributed to the principal repayment by Public Sector Home Financing Board (LPPSA) and Perbadanan Tabung Pendidikan Tinggi Nasional (PTPTN). The non-financial public corporations (NFPCs) debt also reduced to RM302.2 billion or 19.6%, primarily contributed by the principal repayments of maturing debt among the NFPCs.

**TABLE 4.6.** *Public Sector Debt, 2022 – 2023*

| COMPONENT | RM MILLION | | SHARE (%) | | SHARE OF GDP (%) | |
|---|---|---|---|---|---|---|
| | 2022 | 2023[1] | 2022 | 2023[1] | 2022 | 2023[1] |
| **Federal Government** | **1,079,591** | **1,145,018** | ***73.0*** | ***74.3*** | ***60.3*** | ***61.9*** |
| Domestic | 1,050,078 | 1,114,658 | *71.0* | *72.3* | *58.6* | *60.3* |
| Offshore | 29,513 | 30,360 | *2.0* | *2.0* | *1.7* | *1.6* |
| **Statutory bodies** | **95,418** | **94,648** | ***6.4*** | ***6.1*** | ***5.3*** | ***5.1*** |
| Domestic | 95,418 | 94,648 | *6.4* | *6.1* | *5.3* | *5.1* |
| *of which:* Guaranteed | 95,418 | 94,648 | *6.4* | *6.1* | *5.3* | *5.1* |
| Offshore | - | - | - | - | - | - |
| **Non-financial public corporations** | **304,499** | **302,189** | ***20.6*** | ***19.6*** | ***17.0*** | ***16.3*** |
| Domestic | 188,310 | 187,129 | *12.7* | *12.1* | *10.5* | *10.1* |
| *of which:* Guaranteed | 188,310 | 187,129 | *12.7* | *12.1* | *10.5* | *10.1* |
| Offshore | 116,189 | 115,060 | *7.9* | *7.5* | *6.5* | *6.2* |
| *of which:* Guaranteed | 29,089 | 31,756 | *2.0* | *2.1* | *1.6* | *1.7* |
| **Total** | **1,479,508** | **1,541,855** | ***100.0*** | ***100.0*** | ***82.6*** | ***83.3*** |

[1] End-June 2023
Source: Ministry of Finance, Malaysia

# Outlook for 2024

In line with Ekonomi MADANI framework, the Government aims to restructure the economy and rebuild the country's fiscal resiliency and capacity. The Government is also committed to prudent debt management in reducing debt and liabilities exposures as well as the need for a robust financing strategy.

As a result, the Federal Government gross borrowings are estimated to be lower around 10% of GDP. Given the sufficient liquidity and resiliency of domestic debt capital market, funding will be raised entirely onshore. Furthermore, efforts will be focused on ensuring a well-spread debt maturity profile by reducing the issuance of the short-term instruments and its outstanding in managing the refinancing risk.

The Federal Government debt is projected to be around 64% of GDP as at end-2024, mainly for financing strategic development projects under the Twelfth Plan, among others, flood mitigation programme, Central Spine Road (CSR), Pan Borneo Sabah and Sarawak highways, Rapid Transit System Link (RTS Link) Project between Johor Bahru and Singapore as well as National Fiberisation and Connectivity Plan or currently known as Pelan Jalinan Digital Negara (JENDELA). In navigating the challenges ahead, the Government is committed towards fiscal consolidation through bold fiscal reform initiatives, hence, the debt-to-GDP ratio is expected to reduce over the medium-term.

## Conclusion

The Government continues to ensure fiscal and debt sustainability while protecting the well-being of the rakyat. Amid persistent global economic headwinds and challenges, the Government remains committed to reduce debt-to-GDP ratio by upholding to the Medium-Term Fiscal Framework strategies accompanied by the proposed Public Finance and Fiscal Responsibility Act. In addition, debt management continues to be guided by several principles, among others, adhering to stipulated debt rules and giving priority to domestic-sourced financing with the ultimate goals of reducing Government indebtedness level and widening fiscal space.

**FIGURE 4.1.** *Issuance by Maturity*

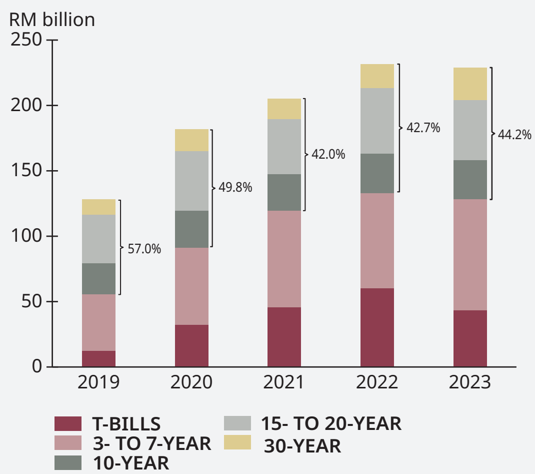



**FIGURE 4.2.** *BTC Ratios of MGS and MGII Issuances*

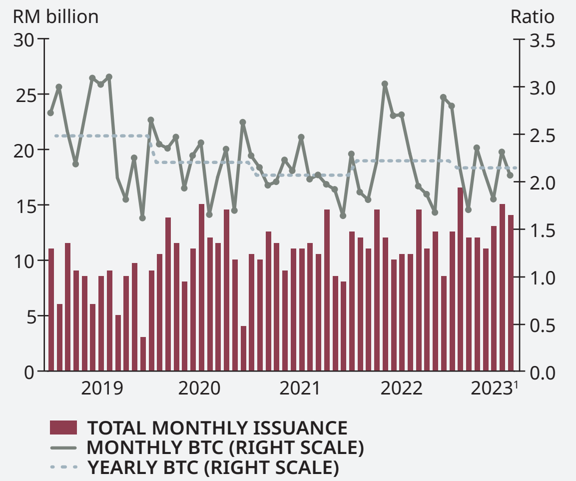



**FIGURE 4.3.** *MGS Benchmark Yield Curve*

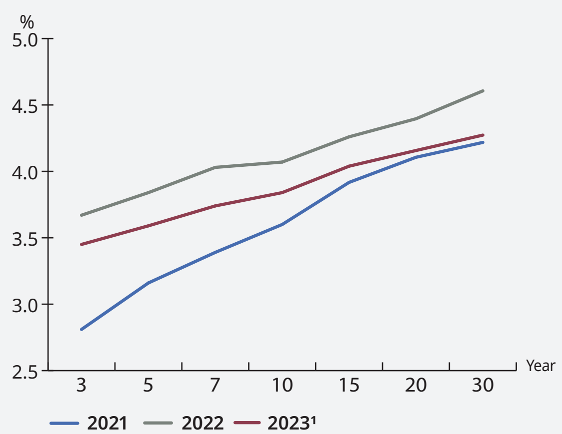
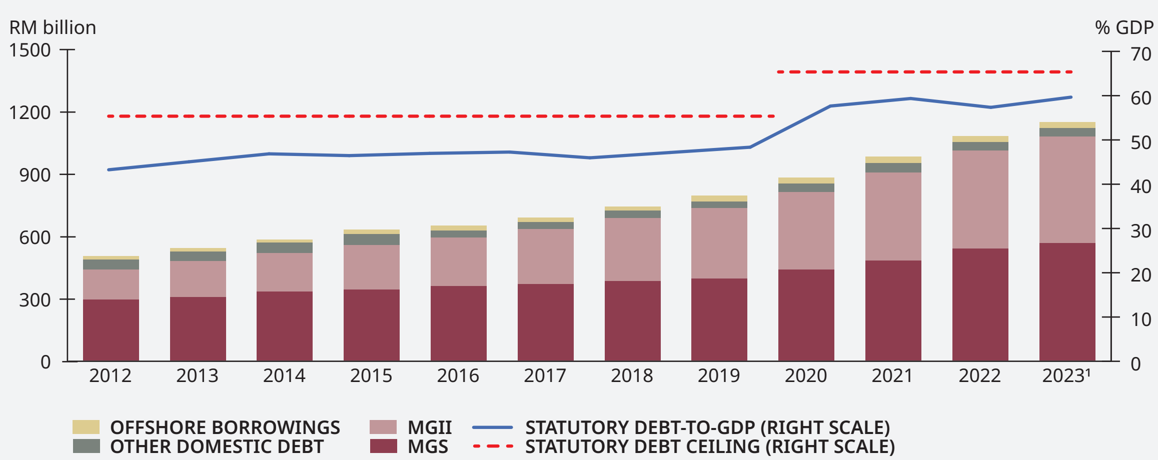



**FIGURE 4.4.** *MGS Indicative Yields*


**FIGURE 4.5.** *Federal Government Debt Composition*




[1] End-August 2023
Source: Ministry of Finance, Malaysia, Bank Negara Malaysia and Bloomberg

**FIGURE 4.6.** *Federal Government Debt by Holder*

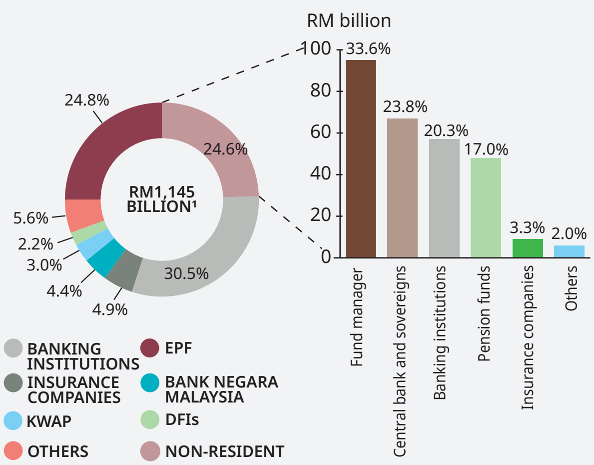



**FIGURE 4.7.** *Non-Resident Holdings of Ringgit-Denominated Debt Securities*

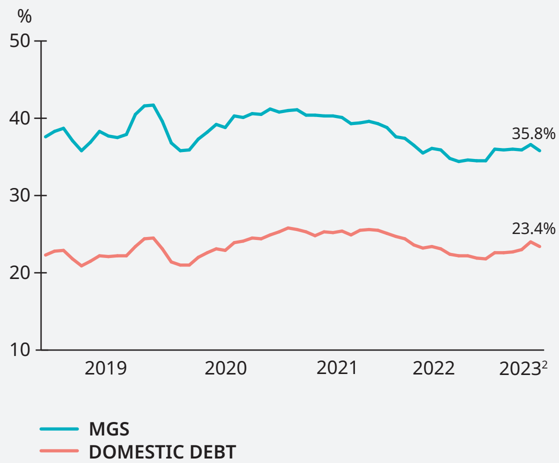



**FIGURE 4.8.** *Federal Government Debt by Remaining Maturity*

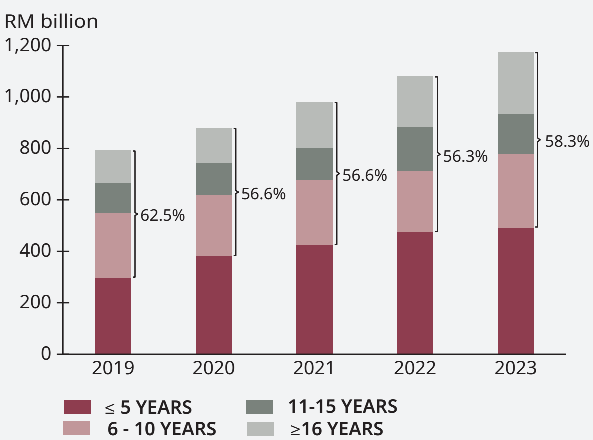



**FIGURE 4.9.** *Debt Service Charges*

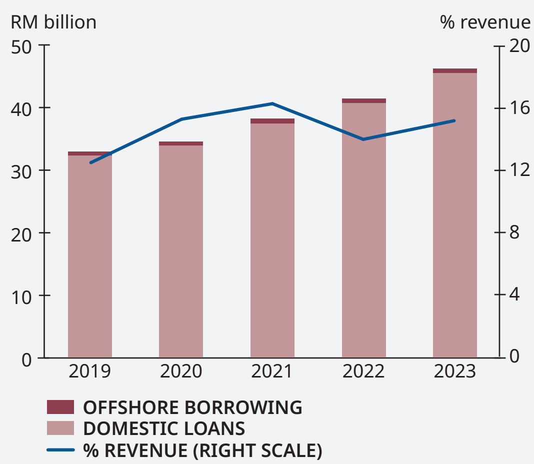
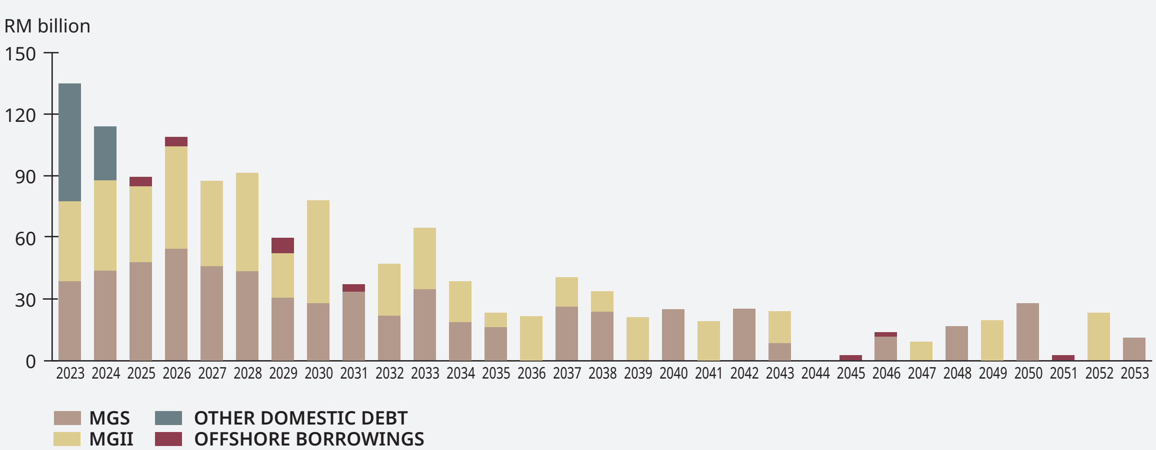



**FIGURE 4.10.** *Debt Maturity Profile*




[1] End-June 2023
[2] End-August 2023
Source: Ministry of Finance, Malaysia