الوكالة الإسلامية الدولية للتصنيف
Islamic International Rating Agency

IIRA Reaffirms Sovereign Ratings of Malaysia

Manama, April 13, 2021–The Islamic International Rating Agency (IIRA) has maintained the long term and short term foreign currency ratings of Malaysia (or 'the Country') at 'A / A1' (Single A / A One) and local currency ratings at 'A+/ A1' (Single A Plus/ A One), on the international scale, and 'AAA (my)/ A1+ (my)' (Triple A/ A One Plus) on the national scale, with 'Stable' outlook.

Ratings assigned to Malaysia (or 'the country') are strengthened by a sustained, positive current account balance, continued strong growth potential and a stable investment climate supported by a well-developed physical and social infrastructure. A healthy financial sector provides overall economic stability to the country. As a member nation of the Association of Southeast Asian Nations (ASEAN), Malaysia maintains strong trade and diplomatic relations with regional and global economies.

In the aftermath of COVID–19 and as the global economy contracted, Malaysia registered contraction of 5.6% in GDP with a drop in both domestic and external demand. A Movement Control Order (MCO) was imposed in March 2020, which was extended several times, impeding economic activity. Another MCO in the beginning of 2021, may have set back earlier expectations for the pace of recovery in the current year; IIRA expects the economy to rebound at a rate of 5.5% in 2021. The vaccination drive has picked pace in recent weeks with 80% of the population targeted to be inoculated by December 2021. A faster than expected recovery, as a result of effective measures, could provide upward impetus to growth.

In an almost universal response to the economic slowdown, central banks globally cut interest rates; Bank Negara Malaysia (BNM) cut the interest rate to 1.75% in July 2020 from 3.0% in January of the same year. Headline inflation fell in negative territory at -1.2% in 2020, with core inflation also lower at 1.1%. Inflation is likely to be higher in 2021, as commodity prices have recovered in recent months. While BNM still has some margin to support the economy through further monetary policy easing, expectation regarding inflationary environment and growth globally, are likely to drive interest rates gradually upwards. International funds flow is likely to remain subdued with momentum to potentially return in the latter half of the current year.

Led by a boost in semi-conductor led Electrical & Electronic (E&E) exports in H2'20, higher than prior year current account surplus was recorded, helped also by lower deficits in primary and secondary income accounts, and providing much needed space to the economy. Supported by a strong goods balance, the current account position is expected to remain robust in the current year, although likely checked by continued expected depression in tourism receipts.

The government has exhibited commitment to provide ongoing support to the economy. A series of stimuli were announced in 2020, to support businesses and individuals, with direct fiscal support from the establishment of a COVID-19 fund. Excluding COVID-19 fund outlays, fiscal deficit stood at -3.5% of GDP in 2020, remaining just below IIRA's rating trigger of 3.8% as indicated in our last assessment on

March 20, 2020. Overall fiscal deficit registered at -6.2% of GDP, with 2021 budget also seeing a deficit of -5.4% of GDP, later revised to 6.0%.

Federal government debt rose sharply, as a result of the increased funding requirement, to 62.2% of GDP at year-end. Debt levels are likely to continue to rise through 2021, with the pace of increase moderating in 2022, as the fiscal position begins to improve and the economy achieves relative normalcy. On the other hand, external debt has remained largely steady over the last few years and is covered by adequate international reserves which have increased further by end 2020. Debt coverage ratio at 51.6% in 2020 is slightly higher YoY (2019: 50.1%) and is deemed commensurate with ratings assigned.

Indicators for Future Change in Ratings

Given the temporary nature of the stimulus and related transitory impact on fiscal position and federal government debt, IIRA has reaffirmed the ratings with a 'Stable' outlook. Ratings are also supported by growth in exports and positive reflection on the current account balance and largely stable coverage of external debt.

Ratings may be reassessed for improvement in case of faster than expected economic recovery in the backdrop of an efficient vaccine rollout and even distribution across the population.

Ratings may be viewed to be under downward pressure in case of:

- Fiscal deficit varying by more than 20% of the targeted balance in 2021 and/ or a delayed fiscal recovery,
- External debt position deteriorating either through increase in gross external debt or significant decline in buffers comprising international foreign exchange reserves and current account surplus,
- Material deterioration in banking sector indicators, in terms of capitalization and asset quality.

For further information on this rating announcement, please contact IIRA at iira@iirating.com.