MALAYSIAN BOND MARKET: PROBLEMS AND PROSPECTS

By

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Dedicated to Awa Yombeh

ABSTRACT

This study looks at the historical quarterly returns of the various categories of bonds in Malaysia. Beginning from January 1987 to September 1995, the quarterly returns on long-term Malaysian Government Securities, convertible bonds, non-convertible bonds, all-bonds and the Kuala Lumpur Stock Exchange Composite Index are computed and compared. The relationship between the various categories of bonds and the stock market index is also determined.

The study finds out that in Malaysia, as in all other markets, higher investment returns can only be achieved by assuming higher risk and that non-convertible bonds have a higher return for the risk level involved, or, a low risk for the returns offered. The study also finds that all other categories of bonds and the stock index offer returns commensurate with their risk level. Since the correlation between non-convertible bonds and stocks is found to be 0.36, the study shows that the prudent financial manager can improve investment

performance by allocating investment funds between these two types of securities. The correlation between convertible and non-convertible bonds is also low (0.25) and allocation of funds between these categories of bonds is also found to be beneficial. However, the correlation between all-bonds and the stock market is high (0.51) and gains from diversification become smaller. The correlation between convertibles and the stock index is almost equal to 1. Generally convertibles offer higher returns, followed by all-bonds, then the stock index, then non-convertibles and finally Malaysian Government Securities. The risk levels of the above securities follow the same pattern.

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TABLE OF CONTENTS

LIST OF TABLES

LIST OF FIGURES