Taklimat
Laporan Tahunan 2016 dan
Laporan Kestabilan Kewangan
dan Sistem Pembayaran 2016

Gabenor Bank Negara Malaysia
23 Mac 2017
Taklimat
Laporan Tahunan 2016 dan
Laporan Kestabilan Kewangan
dan Sistem Pembayaran 2016

Gabenor Bank Negara Malaysia
23 Mac 2017
In 2016, the Malaysian economy continued to expand despite multiple external shocks and domestic adjustments amid a period of adjustment to various challenges.

Real GDP growth of selected countries

- Volatile global commodity prices
- Weak global demand
- Depreciation of the ringgit
- Lingering impact of GST implementation
- Domestic price adjustments

Note: PH= Philippines, ID= Indonesia, MY= Malaysia, TH= Thailand, KR= South Korea, SG= Singapore

Source: National authorities, Department of Statistics, Malaysia
Private domestic demand remained the key growth driver

- **Sustained private consumption:**
  - Supported by continued wage and employment growth, with additional impetus from Government measures

- **Private investment continued to expand:**
  - Supported by implementation of new and ongoing projects in the manufacturing and services sectors

- **Smaller negative contribution from net exports:**
  - Import growth moderated at a faster pace than exports

**Real GDP Growth**

- Contribution to growth (ppt.)
- **6.0%**
- **5.0%**
- **4.2%**
- **1.2%**
- **1.1%**
- **0.6**
- **0.6**
- **1.8**
- **1.1**
- **0.6**
- **-0.5**
- **-0.4**
- **-0.2**

Source: Department of Statistics, Malaysia
2017 will be characterised by several developments

- Improvement in global growth
- Higher commodity prices
- Volatile financial markets
- Socio- and geopolitical developments
- Policy adjustments in advanced economies
Malaysia is positioned to benefit from positive developments and to withstand negative shocks

- **Diversified economic and trade structure**
  Structural transition towards high-value added sectors with varied export products and markets

- **Well-developed and resilient financial system**
  Strong capital and liquidity buffers with continued access to financing

- **Adequate reserves and manageable external debt**
  Ample international reserves and increased foreign asset holdings act as buffer against external shocks

- **Policy space and flexibility**
  Flexible exchange rate and monetary policy space
Recent indicators point to an improvement in global growth

Higher global manufacturing and industrial production data signal better global growth prospects

Exports in Asia has been recovering

Global Manufacturing Indicators

Export Value Growth in Selected Asian Economies

*Data available as at 2016
** January 2017 data for Malaysia and Thailand

Source: Bloomberg, Haver, BNM
Global growth and trade projected to expand in 2017

Broad-based expansion in growth across regions

World trade to world GDP ratio to improve after reaching the lowest ratio since 2001

GDP Growth By Region

World Trade Growth and Trade to GDP Ratio

% yoy

0 2 4 6 8 10 12


Global
Adv. economies
Asia
Other EMEs

% yoy

0 2 4 6 8 10 12 14


World Trade Growth
World Trade to World GDP Ratio (RHS)

Source: International Monetary Fund (IMF)
The Malaysian economy to expand by 4.3 – 4.8% in 2017

Growth to remain anchored by private domestic demand, with support from external sector

Real GDP Growth
Annual change (%)

Private Consumption
Annual change (%)

Private Investment
Annual change (%)

Net Exports
Annual change (%)

Source: Department of Statistics, Malaysia, Bank Negara Malaysia
Domestic demand to remain a key driver, with support from improvement in net exports

<table>
<thead>
<tr>
<th>Real GDP by Expenditure (Annual change, %)</th>
<th>Share(^2) 2016 (%)</th>
<th>2016(^p)</th>
<th>2017(^f)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Domestic demand(^1)</td>
<td>91.8</td>
<td>4.4</td>
<td>4.4</td>
</tr>
<tr>
<td>Private expenditure</td>
<td>70.2</td>
<td>5.7</td>
<td>5.6</td>
</tr>
<tr>
<td>Consumption</td>
<td>53.3</td>
<td>6.1</td>
<td>6.0</td>
</tr>
<tr>
<td>Investment</td>
<td>16.9</td>
<td>4.4</td>
<td>4.1</td>
</tr>
<tr>
<td>Public expenditure</td>
<td>21.6</td>
<td>0.4</td>
<td>0.5</td>
</tr>
<tr>
<td>Consumption</td>
<td>13.1</td>
<td>1.0</td>
<td>-0.2</td>
</tr>
<tr>
<td>Investment</td>
<td>8.5</td>
<td>-0.5</td>
<td>1.5</td>
</tr>
<tr>
<td>Net exports</td>
<td>8.1</td>
<td>-1.8</td>
<td>5.3</td>
</tr>
<tr>
<td>Exports</td>
<td>70.0</td>
<td>0.1</td>
<td>2.2</td>
</tr>
<tr>
<td>Imports</td>
<td>61.9</td>
<td>0.4</td>
<td>1.8</td>
</tr>
<tr>
<td>Real GDP</td>
<td>100.0</td>
<td>4.2</td>
<td>4.3 – 4.8</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Real GDP by Economic Activity (Annual change, %)</th>
<th>Share(^2) 2016 (%)</th>
<th>2016(^p)</th>
<th>2017(^f)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Services</td>
<td>54.2</td>
<td>5.6</td>
<td>4.9</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>23.0</td>
<td>4.4</td>
<td>4.3</td>
</tr>
<tr>
<td>Mining &amp; Quarrying</td>
<td>8.8</td>
<td>2.7</td>
<td>2.7</td>
</tr>
<tr>
<td>Agriculture</td>
<td>8.1</td>
<td>-5.1</td>
<td>4.0</td>
</tr>
<tr>
<td>Construction</td>
<td>4.5</td>
<td>7.4</td>
<td>8.0</td>
</tr>
<tr>
<td>Real GDP</td>
<td>100.0</td>
<td>4.2</td>
<td>4.3 – 4.8</td>
</tr>
</tbody>
</table>

\(^1\) Excluding stocks, \(^2\) Numbers may not add up due to rounding and exclusion of import duties

Source: Department of Statistics, Malaysia and Bank Negara Malaysia
Private consumption to remain supported by continued employment and income growth

Sustained household spending…

Real private consumption

Annual change (%)

…supported by continued employment growth…

Employment

Million Persons

… and wage growth

Wage growth in the manufacturing and major services sectors

Annual change (%)

<table>
<thead>
<tr>
<th>Year</th>
<th>Real private consumption</th>
<th>Employment</th>
<th>Wage growth</th>
</tr>
</thead>
<tbody>
<tr>
<td>2013</td>
<td>6.1%</td>
<td>13.6%</td>
<td>5.3%</td>
</tr>
<tr>
<td>2014</td>
<td>6.0%</td>
<td>13.9%</td>
<td>4.9%</td>
</tr>
<tr>
<td>2015</td>
<td>6.1%</td>
<td>14.1%</td>
<td>4.2%</td>
</tr>
<tr>
<td>2016p</td>
<td>N/A</td>
<td>+112k jobs</td>
<td>N/A</td>
</tr>
<tr>
<td>2017f</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
</tr>
</tbody>
</table>

Source: Department of Statistics, Malaysia
Households have the capacity and resilience to support expenditure

Continued expansion in income, the primary driver of private consumption

Determinants of Private Consumption (% share)

- Disposable income (MEF salary increment in 2017: 5.4%; 2016: 5.5%)
- Housing wealth
- Financial wealth
- Others

On aggregate, households have ample liquid financial assets to cover debt

HH Liquid Financial Assets and Debt (RM trillion)

- HH Debt
- HH Liquid Financial Assets

1Q'05 - 4Q'13

Source: Bank Negara Working Papers (WP7/2015), Department of Statistics, Malaysia, Bank Negara Malaysia, Malaysian Employers Federation
Private investment to register modest growth

Private investment activity to grow at 4.1%

Malaysia continues to attract FDI, but in lower amounts

Business sentiments remain soft

Real Private Investment Growth

Annual change (%)

25
20
15
10
5
0

2011 2013 2015 2017f

6.4 4.4 4.1

Foreign Direct Investment

Share to Nominal Private Investment (%)

30
20
10
0


Avg. Annual FDI: RM36.6 bn

FDI: RM43.4 bn

FDI: RM41.2 bn

23% 22% 19%

Business Condition Index

Points

110
100
90
80
70

1Q 15 2Q 15 3Q 15 4Q 15 1Q 16 2Q 16 3Q 16 4Q 16

81.2

p preliminary, f forecast

Source: Department of Statistics, Malaysia, Bank Negara Malaysia, MIER
Private investment will be supported by the ongoing projects in the services and manufacturing sectors

Services and manufacturing sectors account for 75% of private investment activity

Key quality projects to increase efficiency, productive capacity and employment

**Services**
- Transport and storage: Oil and gas storage terminals, seaports and aircrafts
- Telecommunication: 4G/LTE network expansion

**Manufacturing**
- Electrical and electronics (E&E)
- Resource-based industries

Source: Department of Statistics, Malaysia, Bank Negara Malaysia
External trade performance to improve

Higher export and import growth, lifted by positive global factors amid sustained domestic demand

<table>
<thead>
<tr>
<th>Annual change (%)</th>
<th>% share (2016)</th>
<th>2016&lt;sup&gt;p&lt;/sup&gt;</th>
<th>2017&lt;sup&gt;f&lt;/sup&gt;</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Gross exports</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Manufactured</td>
<td>82.2</td>
<td>3.2</td>
<td>3.7</td>
</tr>
<tr>
<td>E&amp;E</td>
<td>36.6</td>
<td>3.5</td>
<td>4.2</td>
</tr>
<tr>
<td>Non-E&amp;E</td>
<td>45.5</td>
<td>3.0</td>
<td>3.3</td>
</tr>
<tr>
<td>Commodities</td>
<td>17.1</td>
<td>-8.6</td>
<td>14.8</td>
</tr>
<tr>
<td><strong>Gross imports</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Intermediate goods</td>
<td>57.1</td>
<td>-0.1</td>
<td>5.4</td>
</tr>
<tr>
<td>Capital goods</td>
<td>14.3</td>
<td>4.9</td>
<td>7.9</td>
</tr>
<tr>
<td>Consumption goods</td>
<td>9.6</td>
<td>7.3</td>
<td>9.9</td>
</tr>
<tr>
<td><strong>Trade balance (RM billion)</strong></td>
<td>-</td>
<td>87.3</td>
<td>86.4</td>
</tr>
</tbody>
</table>

*p preliminary, f forecast

Note: G3 refers to the US, EU and Japan, NIEs refers to Hong Kong, Korea and Chinese Taipei, ROW refers to rest of the world

Source: Department of Statistics, Malaysia and Bank Negara Malaysia
Current account balance to narrow but remain in surplus

Smaller CA surplus reflect global conditions and domestic structural transformation

Higher domestic investments and moderating savings

Lower private sector surplus, due partly to higher investment

Source: Department of Statistics, Malaysia, Bank Negara Malaysia
The ringgit exchange rate has stabilised in 2017, in line with most major and regional currencies.

The ringgit followed two distinct phases in 2016, with most of the depreciation occurring after the US election. The ringgit has, however, recovered slightly in 2017, in line with most major and regional currencies.

Performance of Selected Currencies against the US dollar (USD)

<table>
<thead>
<tr>
<th>Currency</th>
<th>2016</th>
<th>2017 YTD</th>
</tr>
</thead>
<tbody>
<tr>
<td>KRW</td>
<td>-2.5</td>
<td>7.9</td>
</tr>
<tr>
<td>AUD</td>
<td>-1.0</td>
<td>6.6</td>
</tr>
<tr>
<td>TWD</td>
<td>2.0</td>
<td>5.9</td>
</tr>
<tr>
<td>JPY</td>
<td>3.2</td>
<td>3.5</td>
</tr>
<tr>
<td>SGD</td>
<td>0.4</td>
<td>3.4</td>
</tr>
<tr>
<td>THB</td>
<td>3.1</td>
<td>3.1</td>
</tr>
<tr>
<td>EUR</td>
<td>-3.7</td>
<td>2.1</td>
</tr>
<tr>
<td>MYR</td>
<td>-4.3</td>
<td>1.3</td>
</tr>
<tr>
<td>IDR</td>
<td>2.8</td>
<td>2.8</td>
</tr>
<tr>
<td>GBP</td>
<td>-17.1</td>
<td>0.9</td>
</tr>
<tr>
<td>CNY</td>
<td>-6.6</td>
<td>0.7</td>
</tr>
<tr>
<td>PHP</td>
<td>-5.3</td>
<td>-1.3</td>
</tr>
</tbody>
</table>

1 Regional currencies: Chinese renminbi, Indonesian rupiah, Korean won, Philippine peso, Singapore dollar, New Taiwan dollar and Thai baht. Each currency carries equal weight.

Source: Bank Negara Malaysia
The FMC measures have lent stability to the ringgit and domestic foreign exchange market

- Daily turnover remained stable
- Ringgit volatility declined
- Offshore-onshore gap narrowed
- Bid-ask spread narrowed
- FX conversion increased post-measures
- 5Y CDS spread narrowed

Note: Volatility refers to the difference between MYR/USD interbank intraday highest and lowest rate. Offshore rate refers to the NDF 3-month rate while onshore rate refers to the spot rate.

Source: Bloomberg, Bank Negara Malaysia
Non-resident holdings of Malaysian government bonds remained broadly stable as at end-2016

Non-resident holdings of Malaysian Government bonds stabilised towards the end of the year

Majority of non-residents holdings are by long-term investors

Distribution of Non-resident Holdings in Government Bonds as at end-Dec’16

Non-resident holdings of Malaysian government bonds stabilised towards the end of the year. Majority of non-residents holdings are by long-term investors. The distribution of non-resident holdings in government bonds as at end-Dec’16 shows that the majority of holdings are by long-term investors, with the largest share held by Asset Management (42%), followed by Central Bank/Government (30%).

Note:
- Malaysian Government Bonds includes Malaysian Government Securities (MGS), Malaysian Government Investment Issues (MGII), and Sukuk Perumahan Kerajaan (SPK).
- ‘Others’ include individuals, non-financial corporations and unidentified sectors.
- Data may vary pending further classification by reporting entities.

Source: Bank Negara Malaysia
Malaysia’s external debt remains manageable given its currency, maturity and balance sheet profiles

Foreign currency-denominated debt remains low relative to Asian Financial Crisis

Breakdown by Currency (% of GDP)

- Ringgit-denominated debt
- Foreign currency-denominated debt

59% of total external debt is in medium- to long-term tenures

Breakdown by Maturity (% of total share)

- Limited rollover risks
- Medium- to Long-term 58.6%
- Short-term 41.4%

Short-term external debt partly covered by short-term external assets

Breakdown by Maturity (% of total share)

- Limited rollover risks
- Medium- to Long-term 58.6%
- Short-term 41.4%

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

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*Based on previous definition of external debt

*Debt instruments only

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BANK NEGARA MALAYSIA
CENTRAL BANK OF MALAYSIA

20
Going forward, Malaysia is well-positioned to intermediate volatile capital flows

Short-term capital flows were driven by prevailing conditions in the global financial markets

- Going forward, large and volatile shifts in global liquidity will continue to shape capital flow movements
- Malaysia will be able to withstand these external shocks, drawing on its diversified economic structure, financial buffers and prevailing robust policy framework
- Well-developed and resilient financial system accord Malaysia the capacity to intermediate large and volatile flows

Source: Department of Statistics, Malaysia
Ample international reserves and increased foreign asset holdings act as buffer against external shocks

Reserves position remains at about four-times the level during the Asian Financial Crisis

Increased holdings of foreign assets by banks and corporations

Malaysia’s External Assets

Increased holdings of foreign assets by banks and corporations

Net International Reserves

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

*Lower ratio since 2009 following redefinition of external debt

1 Based on the International Investment Position
For 2017, headline inflation to average 3 – 4% reflecting primarily the pass-through impact of the increase in global oil prices on domestic retail fuel prices.

Headline inflation would be relatively high in 1H 2017 before moderating thereafter.

The cost-driven inflation is not expected to have significant spillovers given the moderate domestic demand conditions.

- Core inflation to increase only modestly.

Source: Department of Statistics, Malaysia and Bank Negara Malaysia.
Headline inflation outlook is subject to uncertainty in global oil prices

- Trajectory of domestic headline inflation will be dependent on the future trend in global oil prices which remain highly uncertain.

- The uncertainties in global oil prices arises mainly from:
  - Possible extension of OPEC's agreement on the cut in crude oil production.
  - Recovery in the global growth.
  - Geo-political tensions.

Source: Bloomberg and Bank Negara Malaysia
Monetary policy will focus on supporting the sustainable growth of the economy while maintaining price stability

- OPR of 3.00% is currently consistent with steady growth and stable inflation
- The MPC will continue to assess balance of risks on outlook of domestic growth and inflation

**GDP growth**

- **Baseline:** Sustained domestic demand supported by more positive contribution from external sector
- **Risk factors:** Threats of protectionism, geopolitical developments, cautious sentiments, financial disruptions

**Inflation**

- **Baseline:** Cost-driven inflation primarily due to pass-through impact of higher global oil prices on domestic fuel prices
- Core inflation to increase modestly
- **Risk factors:** Developments in global oil prices and higher spillovers from cost-push inflation
Financing to the private sector remained healthy with relatively stable borrowing costs

Broad-based loan disbursed across all economic sectors for both businesses and households

<table>
<thead>
<tr>
<th>Year</th>
<th>Gross Financing* (RM bn)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2010</td>
<td>842</td>
</tr>
<tr>
<td>2011</td>
<td>926</td>
</tr>
<tr>
<td>2012</td>
<td>1,124</td>
</tr>
<tr>
<td>2013</td>
<td>1,084</td>
</tr>
<tr>
<td>2014</td>
<td>1,209</td>
</tr>
<tr>
<td>2015</td>
<td>1,225</td>
</tr>
<tr>
<td>2016</td>
<td>1,194</td>
</tr>
</tbody>
</table>

Private sector continue to benefit from stable financing costs

Interest Rates on New Loans to the Private Sector

<table>
<thead>
<tr>
<th>Sector</th>
<th>Long-run average** (%)</th>
<th>Jan-17 (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Overall private sector</td>
<td>6.0</td>
<td>5.5</td>
</tr>
<tr>
<td>Households</td>
<td>5.5</td>
<td>5.0</td>
</tr>
<tr>
<td>Overall businesses</td>
<td>6.0</td>
<td>5.5</td>
</tr>
<tr>
<td>SMEs</td>
<td>5.5</td>
<td>5.0</td>
</tr>
<tr>
<td>Large Corporate (5y AAA PDS)</td>
<td>4.5</td>
<td>4.0</td>
</tr>
</tbody>
</table>

*Comprises gross loans from the banking system and DFIs, and gross funds raised from the capital markets

**Average (Jan 2002 – Dec 2016)

Source: Bank Negara Malaysia
Malaysia’s macroeconomic fundamentals remain supportive of growth

Diversified sources of growth
Malaysia GDP by Economic Sectors (2016)
% share of GDP

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>% share</td>
<td>54</td>
<td>23</td>
<td>9</td>
<td>8</td>
<td>5</td>
</tr>
</tbody>
</table>

Conducive investment destination for foreign investors

FDI Inflows by Source Country (2016)
% share of total FDI inflows

<table>
<thead>
<tr>
<th>Country</th>
<th>HK</th>
<th>SG</th>
<th>JP</th>
<th>CN</th>
<th>US</th>
<th>NL</th>
<th>UK</th>
<th>KR</th>
<th>CH</th>
</tr>
</thead>
<tbody>
<tr>
<td>% share</td>
<td>36</td>
<td>16</td>
<td>9</td>
<td>9</td>
<td>8</td>
<td>5</td>
<td>5</td>
<td>4</td>
<td>3</td>
</tr>
</tbody>
</table>

Diversified export market and product

<table>
<thead>
<tr>
<th>Product</th>
<th>% share of exports</th>
</tr>
</thead>
<tbody>
<tr>
<td>E&amp;E</td>
<td>17</td>
</tr>
<tr>
<td>Non-E&amp;E</td>
<td>46</td>
</tr>
<tr>
<td>Commodity</td>
<td>20</td>
</tr>
</tbody>
</table>

Current account balance reflects strong investment

Current Account Balance
% of GNI

- 2015: 10.4
- 2016p: 2.1

Stable labour market conditions

Employment (million)

- 2015: 14.1
- 2016p: 14.2

Wage Growth (%)

- 2015: 4.9
- 2016p: 4.2

Deeper markets and strong financial buffers

Size of Bond Market and Banking Capital Ratio

- 1998: 55.5
- 2016p: 95.3

* Capital ratio in '98 refers to the risk-weighted capital ratio; Ratio in 2016 refers to total capital ratio, reported based on Basel III Capital Adequacy Framework adopted since January 2013;
Note: HK= Hong Kong, SG= Singapore, JP=Japan, CN=China, US=United States, NL=Netherlands, UK= United Kingdom, KR=South Korea, CH= Switzerland

Source: Department of Statistics, Malaysia and Bank Negara Malaysia
The economy remains resilient with the ability to manage potential downside risks to growth

1. The Malaysian economy to expand by 4.3 – 4.8% in 2017, driven by domestic demand

2. While headline inflation to range between 3.0 – 4.0%, underlying inflation is expected to increase only slightly

3. Risks to growth emanating from global and domestic fronts
   - **Upside:** Positive spillovers from expansionary policies by major economies
   - **Downside:** Slower global growth emanating from global policy uncertainties, volatility in capital flows and exchange rates, and weaker consumer and business sentiments

4. Malaysia’s strong fundamentals to provide resilience in confronting these risks
   - Diversified economic, trade and FDI structures
   - Stable labour market conditions
   - Current account surplus and ample international reserves
   - Strong financial buffers with well-capitalised banking system and developed capital markets
   - Policy flexibility
Financial position remained strong in 2016:

- Total assets of BNM amounted to RM450.98 billion with International Reserves of RM423.9 billion (USD 94.5 billion)
- Net profit of RM6.48 billion
- Dividend of RM2.5 billion to the Government
Income Statement (Year ended 31 December 2016)

<table>
<thead>
<tr>
<th>Description</th>
<th>RM billion</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Income</td>
<td>9.02</td>
</tr>
<tr>
<td>Less:</td>
<td></td>
</tr>
<tr>
<td>Recurring Expenditure</td>
<td>1.12</td>
</tr>
<tr>
<td>Development Expenditure</td>
<td>1.37</td>
</tr>
<tr>
<td>Taxation</td>
<td>0.05</td>
</tr>
<tr>
<td>Total Expenditure</td>
<td>2.54</td>
</tr>
<tr>
<td>Net Profit</td>
<td>6.48</td>
</tr>
</tbody>
</table>
Laporan Kestabilan Kewangan dan Sistem Pembayaran 2016
Laporan Kestabilan Kewangan
dan Sistem Pembayaran 2016
### Financial stability was sustained in 2016

<table>
<thead>
<tr>
<th>Banking Sector (%)</th>
<th>2015</th>
<th>Jan 2017</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Capitalisation</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Common equity tier 1 ratio</td>
<td>13.3</td>
<td>13.1</td>
</tr>
<tr>
<td>Total capital ratio</td>
<td>16.6</td>
<td>16.9</td>
</tr>
<tr>
<td>Excess capital buffer (RM bn)</td>
<td>124.3</td>
<td>131.0</td>
</tr>
<tr>
<td><strong>Profitability</strong></td>
<td>1.3</td>
<td>1.3</td>
</tr>
<tr>
<td>Return on assets</td>
<td>12.3</td>
<td>11.6</td>
</tr>
<tr>
<td><strong>Asset Quality</strong></td>
<td>1.2</td>
<td>1.2</td>
</tr>
<tr>
<td>Net impaired loans ratio</td>
<td>2.2</td>
<td>2.2</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Insurance/Takaful Sector (%)</th>
<th>2015</th>
<th>2016</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Capitalisation</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital adequacy ratio</td>
<td>251.6</td>
<td>248.5</td>
</tr>
<tr>
<td>Insurance</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital adequacy ratio</td>
<td>191.6</td>
<td>205.3</td>
</tr>
<tr>
<td>Takaful</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital buffer (RM bn)</td>
<td>45.9</td>
<td>47.9</td>
</tr>
<tr>
<td><strong>Profitability</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Profit (RM bn)</td>
<td>14.7</td>
<td>16.6</td>
</tr>
<tr>
<td>Claims ratio</td>
<td>60.2</td>
<td>56.0</td>
</tr>
</tbody>
</table>

1. **Domestic financial stability was sustained in 2016 amid heightened financial market volatility**
   - Sound financial institutions and orderly financial market conditions preserved

2. **Stable outlook for financial stability in 2017**
   - Financial institutions remain resilient to any severe macroeconomic and financial shocks, supported by strong financial buffers

Source: Bank Negara Malaysia
Healthy banking system liquidity positions, supported by diversified funding sources

Sufficient liquidity buffer to withstand potential shocks

Increased contribution of equity and long term debt instruments to support asset growth

Source: Bank Negara Malaysia
Household debt accumulation more in line with asset and income growth

Growth in debt converged towards financial assets and income growth

Financial assets: 5.4%
Income: 5.5%
Debt: 5.4%

Lower share of debt to vulnerable borrowers

Source: Bank Negara Malaysia and Malaysia Employers Federation
Continued access to house financing, especially for first time home buyers

Growth in financing mainly driven by sustained demand for affordable housing

72% of housing loan borrowers are first time home buyers of houses priced <RM500K

Source: Bank Negara Malaysia
Housing affordability remains low, amid slow pace of new supply in affordable segment

Houses are unaffordable in major urban centres

Higher-priced property forms most of new launches

Most unsold* houses are in the higher-priced segments

*Includes unsold properties that were completed and under construction

Source: NAPIC, DOSM and BNM estimates. For details, refer to 2016 AR Box Article “Demystifying the Affordable Housing Issue in Malaysia”
Measures to encourage prudent financial discipline remain important, as signs of risk are emerging.

Increase in impairment and delinquency in recent period, particularly for housing

Existing measures still needed but more can be done

1. Raise productivity and income
2. Reduce unproductive debt through debt rationalisation and consolidation
3. Accelerate supply of affordable housing and rental schemes
4. Ensure efficient allocation of affordable housing units to eligible target buyers

Note: Delinquent loans refer to loan-in-arrears of between one and three months

Source: Bank Negara Malaysia
Corporate sector borrowings continue to support domestic economic activities

Financing activities broadly in line with domestic economic activities

Source: Bank Negara Malaysia
Debt servicing capacity of businesses remained sound

Low leverage, with debt servicing capacity and liquidity sustained above prudent thresholds

Debt-to-equity ratio
Interest coverage ratio (RHS)
Cash-to-short-term debt (RHS)

Debt-at-risk within manageable levels

Impaired and delinquent loans broadly low and stable

*For 2016, data as at first nine months

^Debt-at-risk is measured as the share of debt borne by firms with an interest coverage ratio (ICR) of less than two times

ICR= Earnings before interest expense, taxes, depreciation and amortisation / interest expense

Source: Bank Negara Malaysia, International Monetary Fund
Overseas operations of domestic banks remain financially sound amid continued regional expansion

Net external liabilities largely driven by LIFBs, while DBGs continue to maintain net external assets

Continued earnings resilience and sustained asset quality of DBGs’ overseas operations

LIFBs: Locally incorporated foreign banks; DBGs: Domestic banking groups

Source: Bank Negara Malaysia
Continued regional expansion expected under ASEAN Banking Integration Framework

1. Presence in 15 countries worldwide

2. Bilateral arrangements with Indonesia and other ASEAN countries pave the way for further regional integration

Source: Bank Negara Malaysia
Insurance and takaful sector continued to record positive growth

New life/family takaful premiums driven by growth in endowment and group term policies

In the general sector, growth in fire premiums offset slower growth in motor & MAT premiums

Insurance and takaful assets expanded, with a shift to higher yielding corporate bonds and equity

Source: Bank Negara Malaysia
Greater focus on strengthening domestic underwriting capacity and reducing the protection gap

1. Domestic underwriting capacity for more complex & non-traditional risks remains underdeveloped, mainly in the MAT sector

2. Insurance penetration plateaued, with significant protection gap
   - Only 35% of the population have at least 1 life insurance/family takaful policy, with average sum assured of RM61k per capita
   - Initiatives being pursued to expand the provision of simple & affordable products, leveraging on technology & alternative channels to enhance access

Source: Bank Negara Malaysia
Sustained demand for Islamic financial services, with encouraging growth in investment intermediation

Increasing share of investment accounts as a new source of funding for Islamic banks, facilitated by:

- **Investment Account Framework and Implementation Guide**
  - regulatory expectations on product structuring, operational management & business conduct
  - protection of investors
  - recognition of distinct risk characteristics compared to Islamic deposits

- **Investment Account Platform (IAP)**
  - Operationalised in April 2016 by a consortium of 6 Islamic banking institutions
  - Raised RM20 million in new funding to date
  - Combines *wakalah* or *mudarabah* with debt based contracts (e.g. *tawarruq*)

Source: Bank Negara Malaysia
Islamic finance poised to assume a larger role in value-based intermediation

Diversifying measures of effective intermediation in realising socio-economic impact of Islamic finance

- Financial Deepening
- Contribution to GDP
- Growth
- Institutional Strength
- Delivery Channels
- Range of Products & Services
- Profitability
- Cost Efficiency
- Sustainability
- Institutional Quality
- Inclusivity and Diversity
- Efficiency

1. Development of Corporate Value Intent framework and value-based scorecard
   - Promote high quality disclosures on intent, strategy and performance of business
   - Broader dimensions of performance measurement to accelerate value creation for the economy, shareholders and wider community

2. Waqf and sadaqah applications in financial products to deliver positive socio-economic impact
   - Cash waqf arrangements
   - Debit card with waqf features
   - Banking charity accounts
Regulatory measures taken to further strengthen financial system resilience and integrity

- Greater emphasis on sound risk culture and risk-aligned compensation
- Strengthened requirements for independent boards
- Enhanced operational and credit risk management standards
- Improvements to stress testing practices

Corporate governance and risk management

- Smooth transition to higher Liquidity Coverage Ratio
- Implementation of ICAAP for takaful operators

Capital and liquidity

- Proposed enactment of Consumer Credit Law
- Financial Education Network established to drive the national financial education strategy
- Operationalisation of the Ombudsman for Financial Services

Consumer protection and financial literacy

- Strengthened compliance with international AML/CFT standards
- Enhanced cooperation to combat terrorism financing threats

AML/CFT

Supported by supervisory and enforcement actions
Stable outlook for financial stability in 2017

- Stable labour market conditions, continued economic growth and sound lending and risk management practices expected to support asset quality
- Ample domestic liquidity to remain supportive of financial intermediation
- Banks and insurance companies are well positioned to manage transition to strengthened regulatory standards and more competitive environment
- Effects from measures to deepen and broaden domestic foreign exchange market will contribute to orderly market conditions

Source: Bank Negara Malaysia
Implementation of the Financial Sector Blueprint is on track with further priorities identified

Key Initiatives Implemented

- Strengthened and new legislation (i.e. FSA 2013, IFSA 2013 and DFIA 2002)
- Implementation of Payment Card Reform Framework
- Financial Ombudsman Scheme
- Agent Banking Framework
- ASEAN Banking Integration Framework
- Reforms under the motor and LIFE Framework

New/Expanded Priorities

1. Evolving a vibrant FinTech ecosystem
2. Developing more market-based funding solutions
3. Developing deep and liquid financial markets to manage risk exposures
4. Enhancing the role of development financial institutions
5. Expanding insurance and takaful to address protection gaps
Development of alternative finance to meet diverse financing needs of new economy

SMEs Using Alternative Financing

- Leasing
- Pawnbroker/Ar-Rahnu
- Cooperatives
- Factoring
- Licensed money lenders
- Venture capital
- Angel investors
- Investment Account Platform
- Crowdfunding

% of SMEs

1Q 2016
3Q 2016

Policy priorities moving forward

- Strengthen institutional arrangements
- Improve data on alternative finance and the innovative economy
- Establish a unified collateral registry
- Promote the development of open Application Programme Interfaces
- Raise SMEs’ awareness on alternative financing avenues.

Source: SME Corporation Malaysia
Providing a conducive regulatory environment for fintech innovation

Solutions applied through Regulatory Sandbox

1. The Regulatory Sandbox Framework allows innovative fintech solutions to be tested safely in a live environment.

2. Further initiatives planned to facilitate open banking models, common KYC utilities, distributed ledger applications and cloud computing.

- **Product Aggregator**
  - Comparison of insurance product

- **Currency Exchange**
  - Peer-to-peer currency exchange model

- **Remittance**
  - e-money transfer to parties across countries

- **Artificial Intelligence**
  - Digital identification verification & Chatbot
Motor insurance reform on track

From 1 July 2016

New products and add-on covers introduced by insurers

- Flexibility for insurers to introduce new motor products at market-based pricing
- Additional options for consumers e.g. Guaranteed Asset Protection product

From 1 April 2017

Nation-wide awareness campaign to inform and empower consumers

- Important information will be disseminated via print and social media, online, agents and customer support channels
- Empowering consumers to compare products, understand policy options and be aware of price drivers
- Public encouraged to visit www.bnm.gov.my; www.piam.org.my; or www.malaysiantakaful.com.my for more information

From 1 July 2017

Pricing of motor comprehensive and third party fire & theft products will be liberalised to reflect risks

- More equitable and competitive pricing based on risk
- Improved incentives for safe driving and prevention of vehicle theft
Increasing momentum in migration to e-payments

Sustained decline in cheques with increasing use of electronic fund transfers

Transaction Volume for Cheques, IBG and Instant Transfer

<table>
<thead>
<tr>
<th>Month</th>
<th>Cheques</th>
<th>IBG</th>
<th>Instant Transfer</th>
</tr>
</thead>
<tbody>
<tr>
<td>M 2013</td>
<td>10</td>
<td>15</td>
<td>5</td>
</tr>
<tr>
<td>J 2013</td>
<td>15</td>
<td>20</td>
<td>10</td>
</tr>
<tr>
<td>S 2013</td>
<td>20</td>
<td>25</td>
<td>15</td>
</tr>
<tr>
<td>D 2013</td>
<td>25</td>
<td>30</td>
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</tr>
<tr>
<td>M 2014</td>
<td>30</td>
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</tr>
<tr>
<td>J 2014</td>
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<td>S 2014</td>
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<td>D 2014</td>
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<td>M 2015</td>
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<tr>
<td>J 2015</td>
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<td>S 2015</td>
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</tr>
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<td>D 2015</td>
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<td>70</td>
<td>60</td>
</tr>
<tr>
<td>M 2016</td>
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<td>75</td>
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</tr>
<tr>
<td>J 2016</td>
<td>75</td>
<td>80</td>
<td>70</td>
</tr>
<tr>
<td>S 2016</td>
<td>80</td>
<td>85</td>
<td>75</td>
</tr>
<tr>
<td>D 2016</td>
<td>85</td>
<td>90</td>
<td>80</td>
</tr>
</tbody>
</table>

Average growth: 6.5% p.a.

Accelerated expansion of payment card acceptance points

Number of Point-Of-Sale (POS) terminals

<table>
<thead>
<tr>
<th>Year</th>
<th>Number ('000)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2011</td>
<td>100</td>
</tr>
<tr>
<td>2012</td>
<td>150</td>
</tr>
<tr>
<td>2013</td>
<td>200</td>
</tr>
<tr>
<td>2014</td>
<td>250</td>
</tr>
<tr>
<td>2015</td>
<td>300</td>
</tr>
<tr>
<td>2016</td>
<td>350</td>
</tr>
</tbody>
</table>

Average growth: 18.6% p.a.

Source: Bank Negara Malaysia
Fostering stronger payment card security

Migration to PIN-based transactions

- **Enhancement of payment card infrastructure**: Migration from signature to PIN verification for payment card transactions at POS terminals.
- **Transition period**: 6-month period to adapt to the usage of PIN at POS terminals.
- **Mandatory PIN verification**: All payment card transactions at POS terminals must be completed with PIN.

*Cardholders and merchants are urged to adopt the use of PIN today, before PIN is made mandatory for all payment card transactions effective 1 July 2017.*
End of Presentation
End of Presentation