

# The Malaysian Economy: Drawing resilience from underlying strength

Presentation for “Malaysia: A New Dawn” Conference

9 October 2018



# Presentation outline

**Part I: Positive outlook amidst challenging environment**

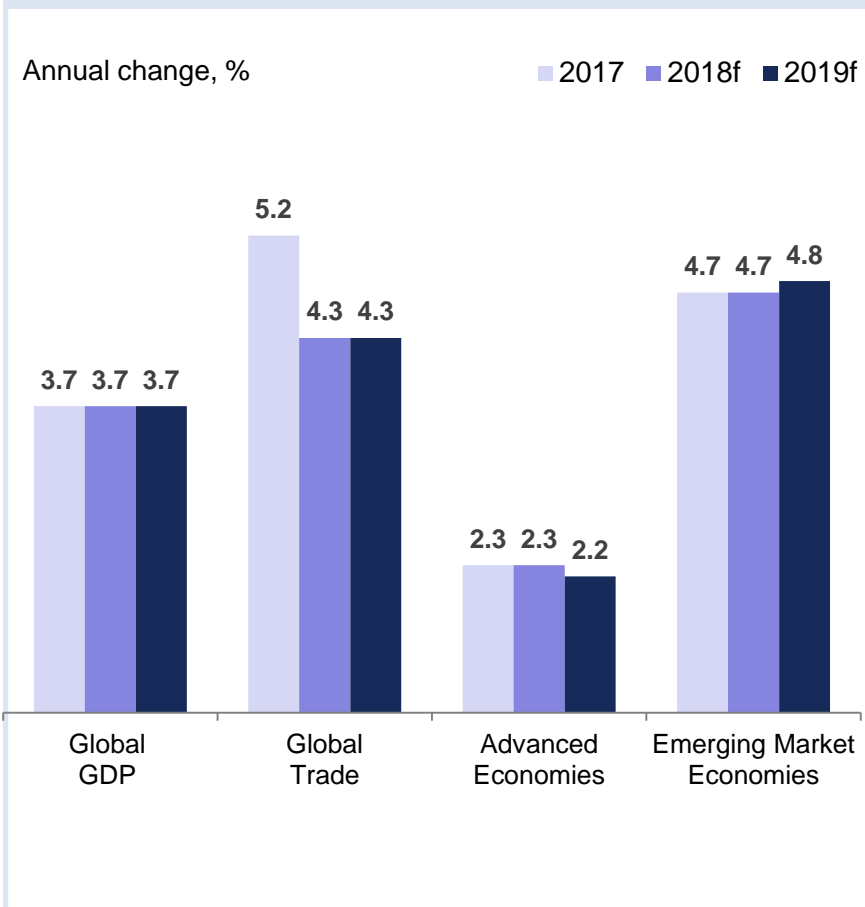
Part II: Strong fundamentals fortifying Malaysia's resilience

Part III: Underlying strength the key defence against potential headwinds



# Global economic momentum, although still strong, is showing some signs of moderation amid emerging downside risks

Global growth and trade to moderate but remains supportive of economic prospects in 2018 and 2019



Source: IMF (WEO Oct 2018)

Balance of global risks has shifted to the downside amid emerging headwinds



**Faster-than-expected monetary policy normalisation path in the US**



**Rising trade protectionism**

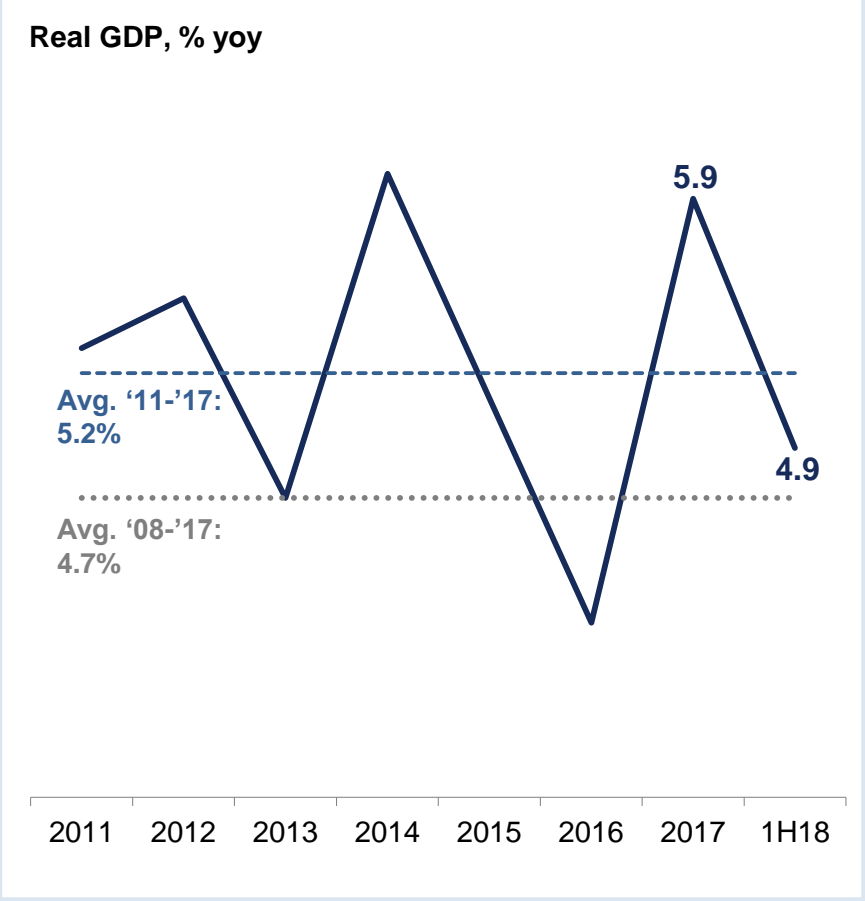


**Re-emergence of financial market volatility amid sharp capital outflows from EMEs**



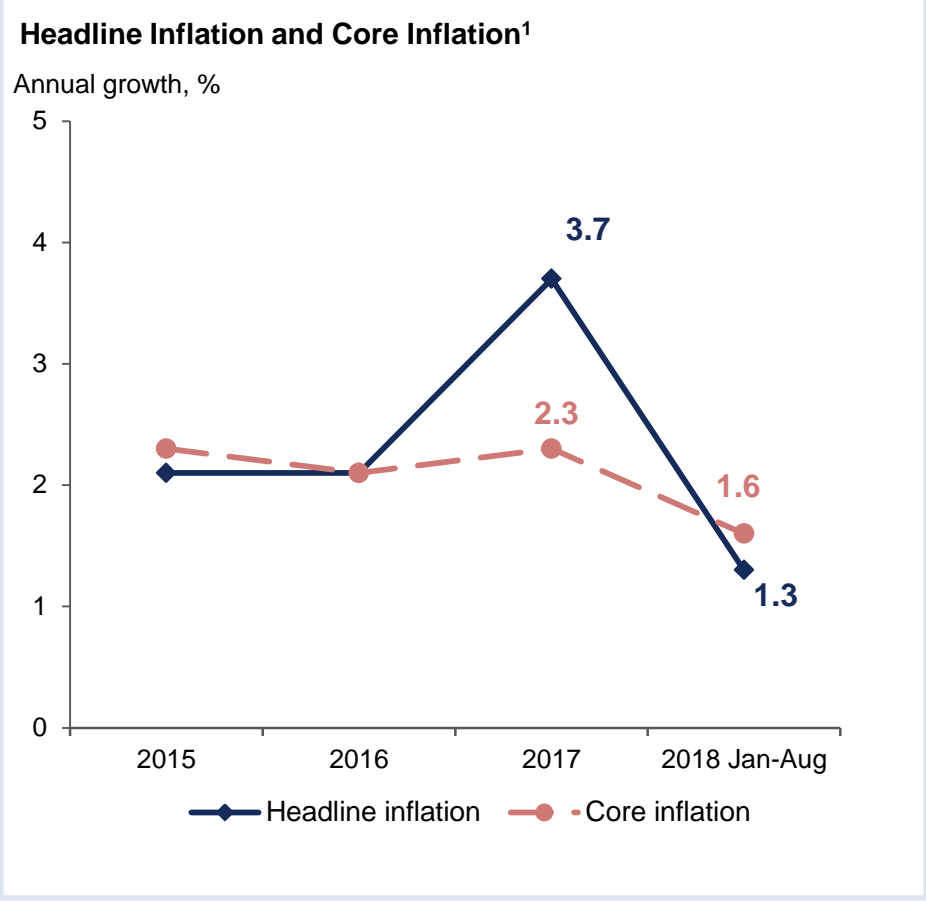
# Despite the headwinds, domestic economy is on a steady growth path with moderate inflation

Malaysia has consistently demonstrated dynamism and resilience



Source: Department of Statistics, Malaysia

Impact from SST on headline inflation will be transitory; Core inflation to remain relatively stable



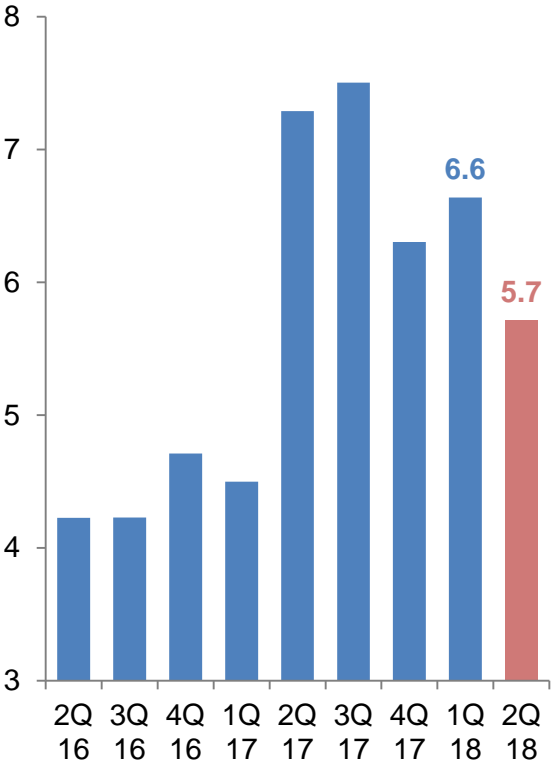
<sup>1</sup>Core inflation is computed by excluding the estimated direct impact of GST  
Source: DOSM and BNM estimates

# Favourable labour market conditions and improving sentiments ensuring environment is supportive of growth and private sector expenditure

## Continued private sector wage growth

### Private Sector Wage Growth

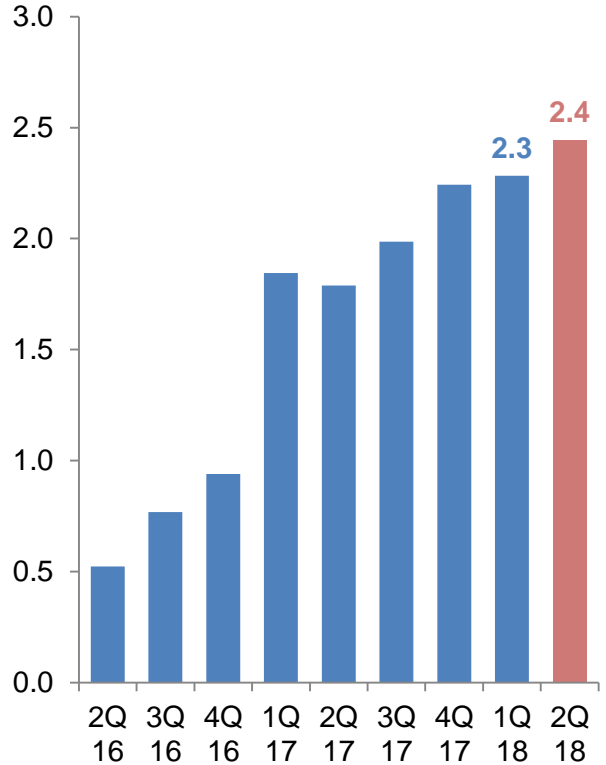
Annual change, %



## Improvements in overall employment growth

### Employment Growth

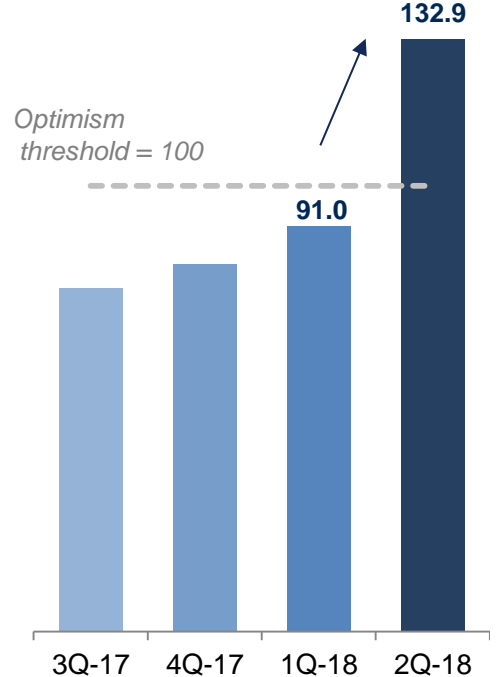
Annual change, %



## Consumer sentiments highest in two decades

### MIER Consumer Sentiments Index

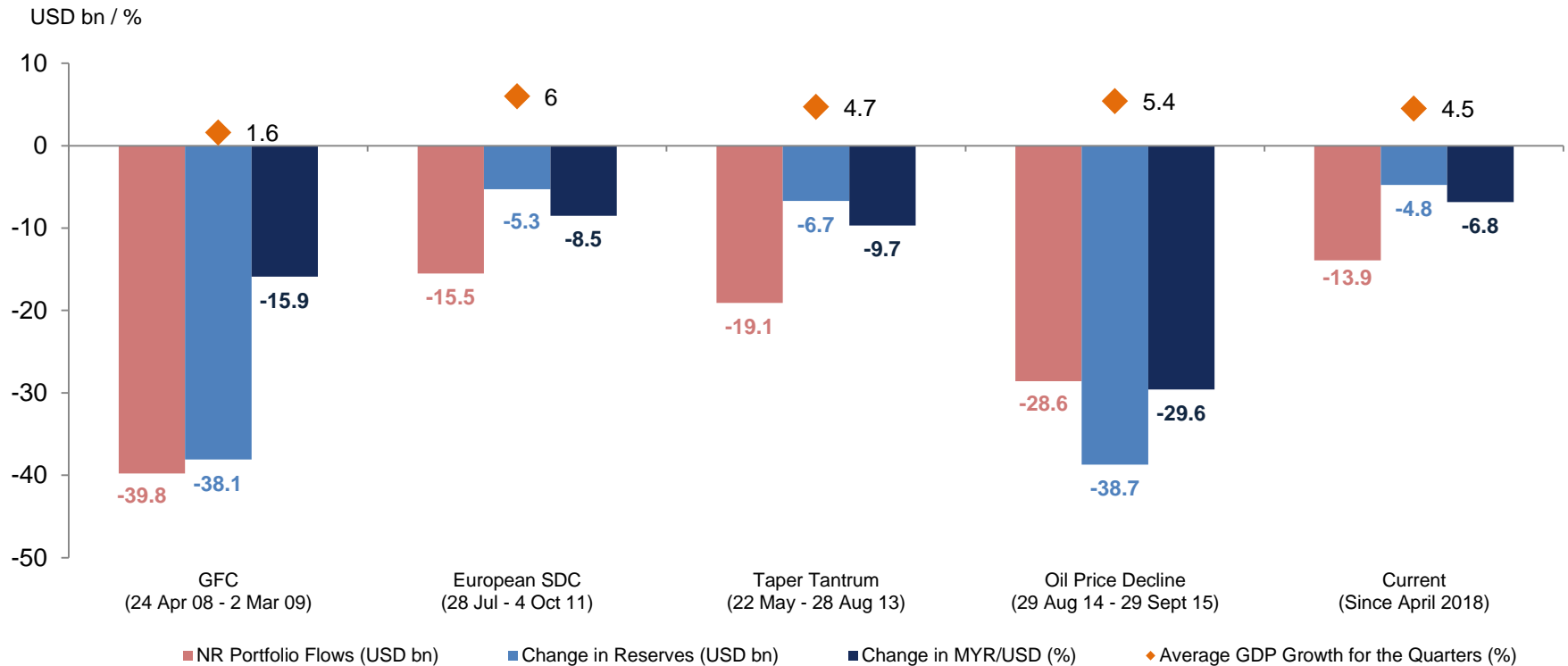
Points



# Policy flexibility and deep financial markets have allowed Malaysia to weather episodes of stress and ensure growth is preserved

Ringgit flexibility, FX intervention and financial market development initiatives are integral in Malaysia's ability to withstand external shocks

NR Portfolio Flows, Reserves, Ringgit Performance, and GDP Growth during Outflow Periods



Note: Current data for reserves is as at end-Sept 2018; MYR/USD and NR portfolio flows as at 5 October 2018

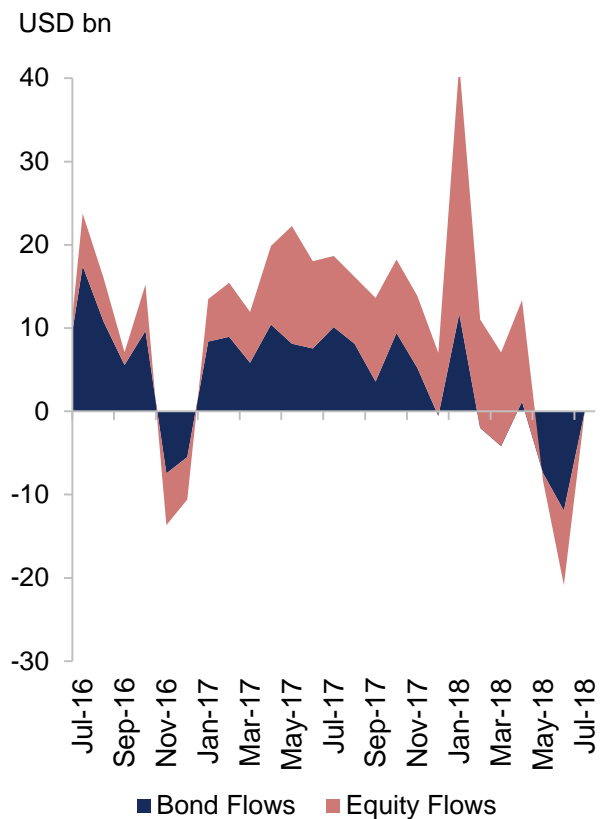
Source: Bank Negara Malaysia, Bloomberg and DOSM



# While the ringgit has depreciated against the USD along with most EM currencies amid global developments...

Significant capital outflows from the EMEs, particularly since 2Q18 have resulted in currency depreciation among EM currencies

## Emerging Market Economies: Net Monthly Capital Flows



## Performance of Selected EM/Regional Currencies against the USD



1 Capital outflows were driven mainly by external factors, as reflected by similar trends in other EMEs

2 The ringgit has been relatively resilient compared to other EM and regional currencies

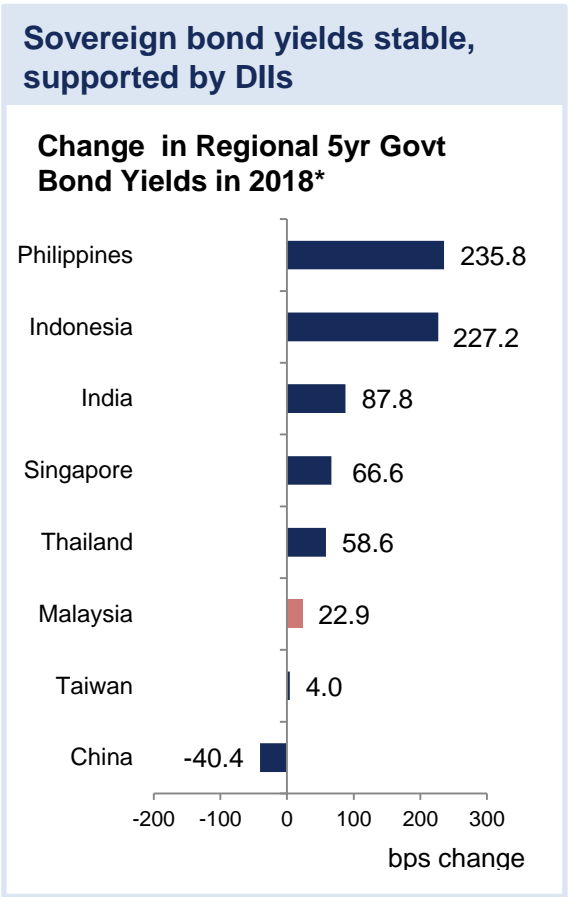
Note: EPFR data is based on a survey of global fund managers, and may not be reflective of national balance of payments data

Source: EPFR; Bank Negara Malaysia and Bloomberg



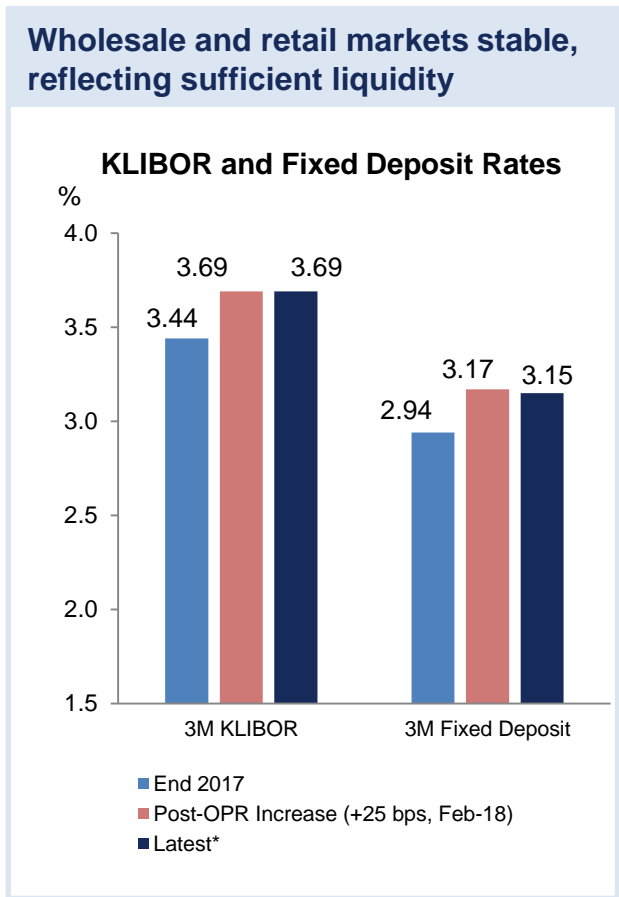
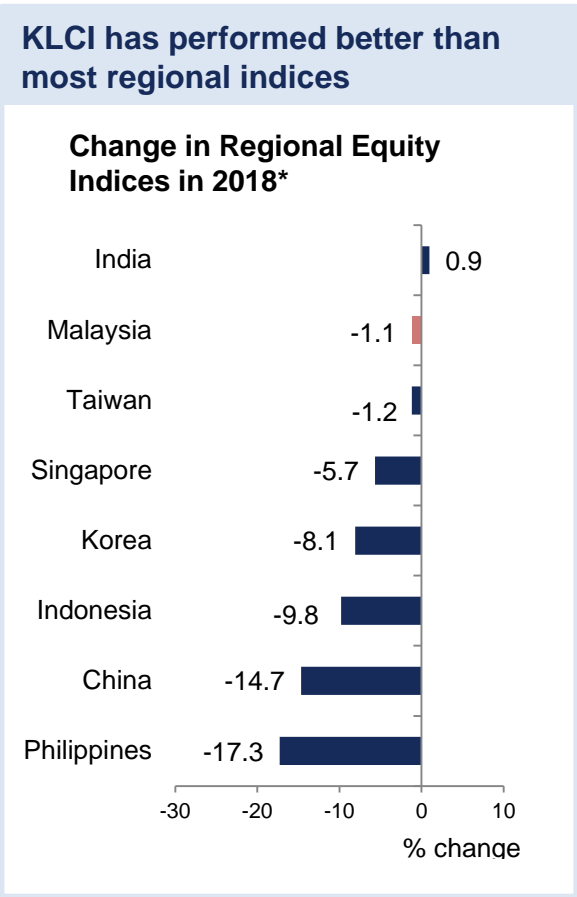
# ...domestic financial conditions have remained stable

Depth and breadth of Malaysia's financial system, supported by mature and sophisticated domestic players, helped intermediate the large outflows



\*Data as at 5 October 2018

Source: Bloomberg



\*Latest refer to 5 October 2018 for 3M KLIBOR and August 2018 for 3M Fixed Deposit

Source: Bank Negara Malaysia





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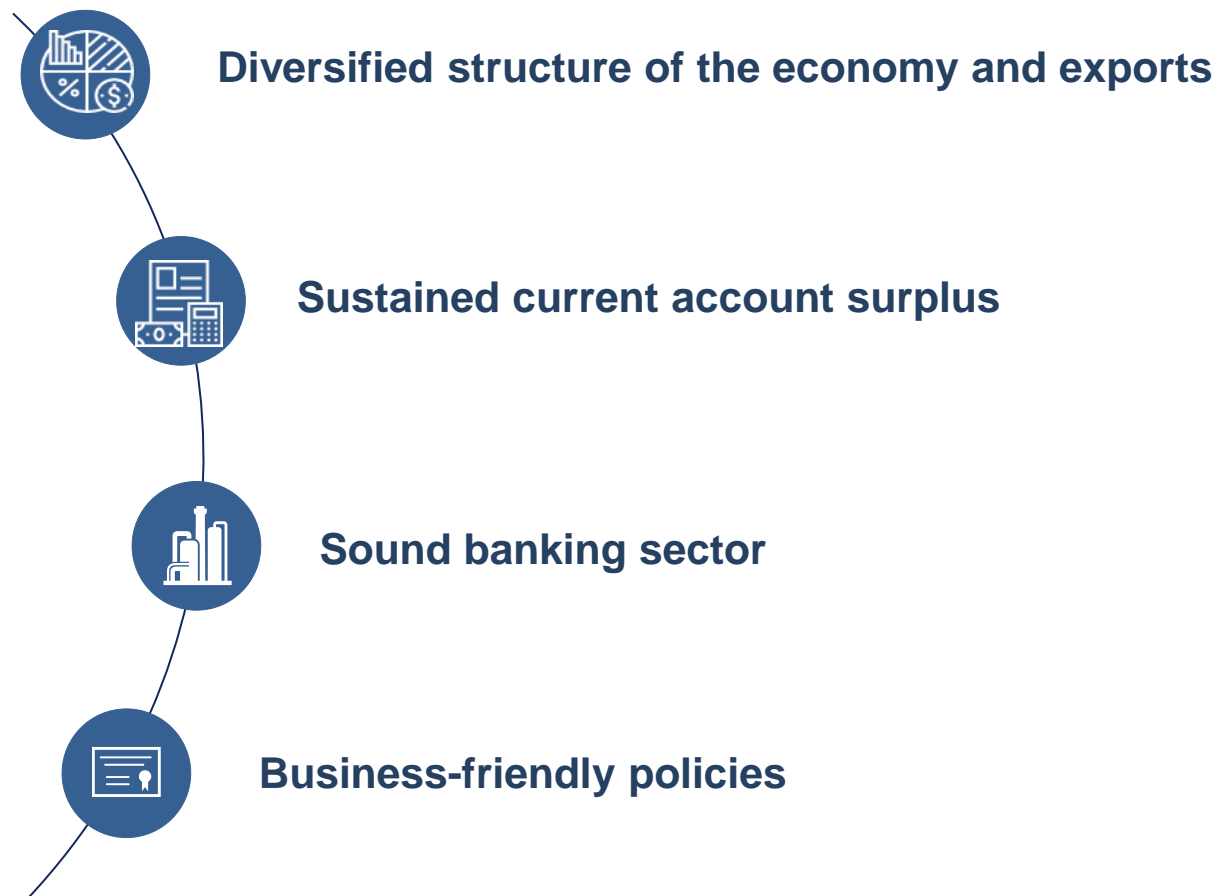
Part I: Positive outlook amidst challenging environment

**Part II: Strong fundamentals fortifying Malaysia's resilience**

Part III: Underlying strength the key defence against potential headwinds



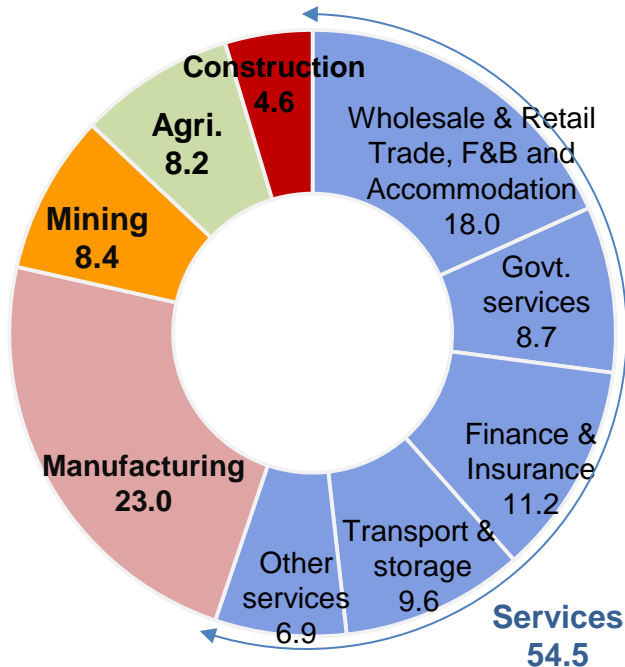
# Malaysia's strengths are anchored by solid economic fundamentals



# The well-diversified structure of the economy accords Malaysia the resilience to face global and domestic headwinds

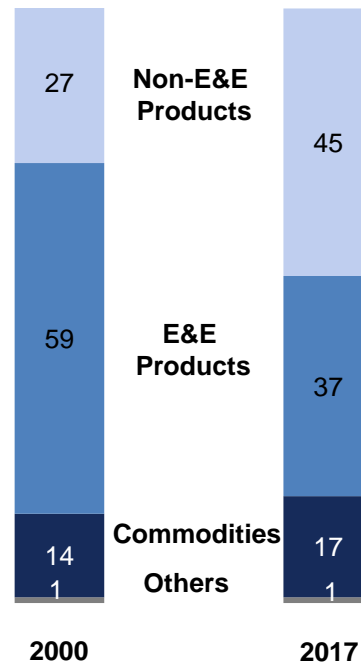
Structural reforms have resulted in a more diversified economic structure

Malaysia: Economy by Sector (2017, % of GDP)

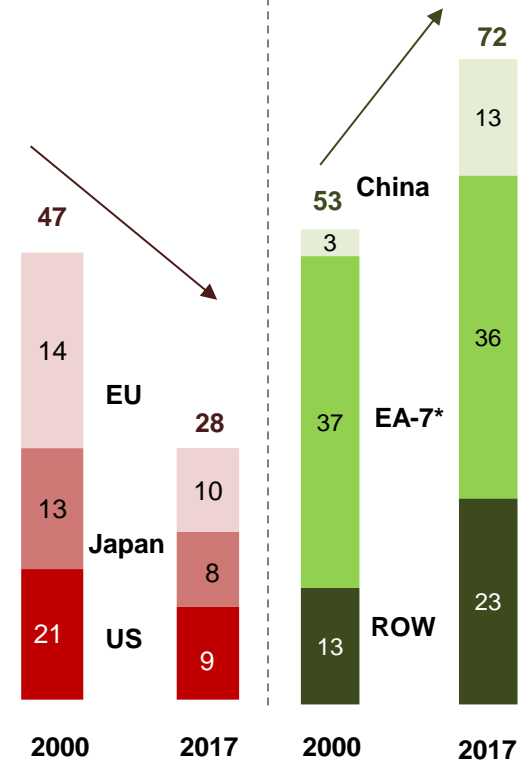


Highly diversified export products and markets

Malaysia's Exports by Products  
% share of gross exports



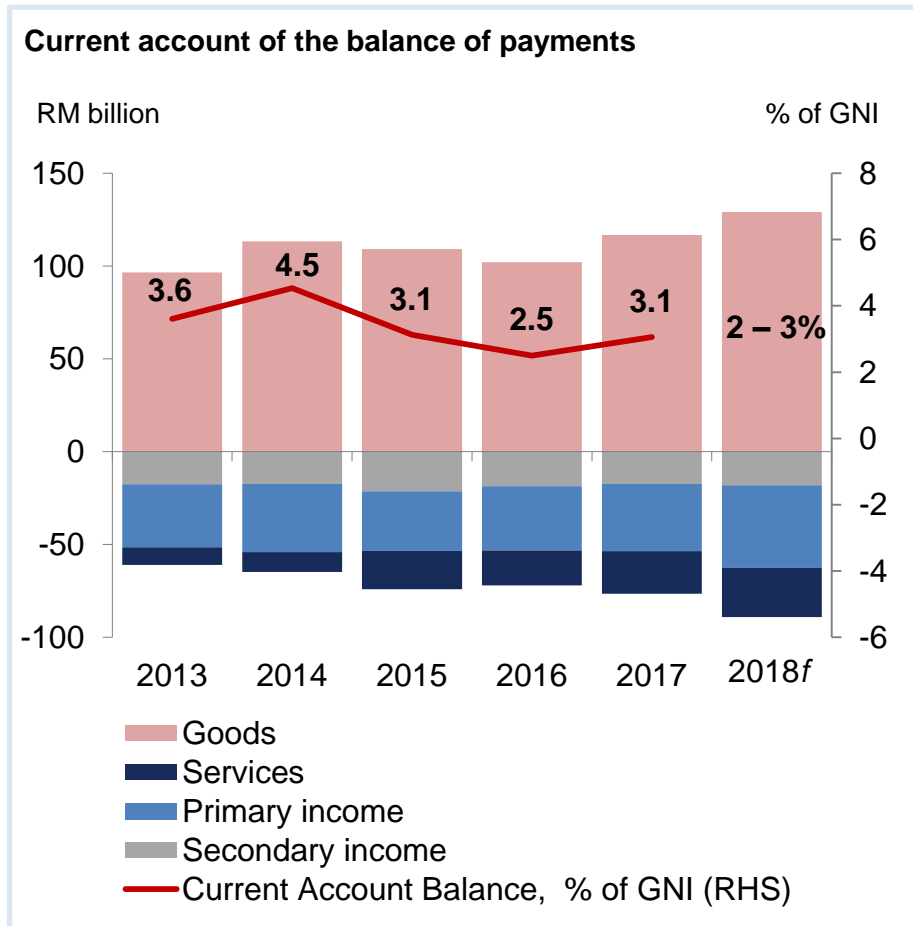
Malaysia's Exports by Markets  
% share of gross exports



\* Refers to Singapore, Thailand, Indonesia, Philippines, Korea, Hong Kong SAR and Chinese Taipei (Note: Numbers may not add up due to rounding)  
Source: Department of Statistics, Malaysia

# The current account has continued to register a healthy surplus

Healthy goods surplus supported by continued demand from key trade partners, expansion in global technology cycle and firm commodity prices



**Continued demand from major trade partners**

*(United States, regional economies)*



**Expansion in global demand for electronics**

*(e.g. Internet of things, Automotive)*



**Higher production capacity**

*(E&E and primary-related manufacturing)*



**Firm commodity prices**

*(e.g. Crude oil and LNG)*

Source: Department of Statistics, Malaysia and Bank Negara Malaysia



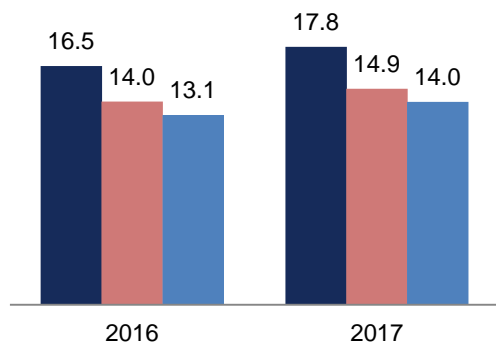
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# Sound banking sector, with strong financial buffers

Banks are well-capitalised, with sufficient liquidity to support financial intermediation

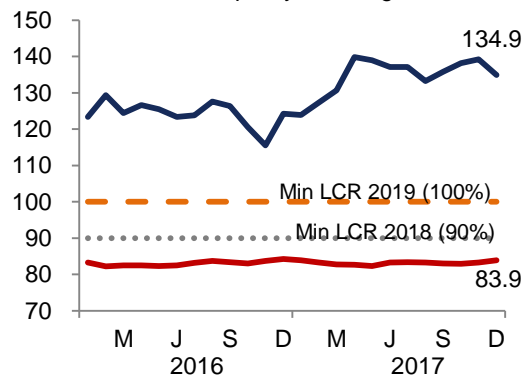
## Capital Ratios (% of RWA)

■ Total Capital Ratio ■ Tier 1 Capital Ratio  
■ CET1 Capital Ratio



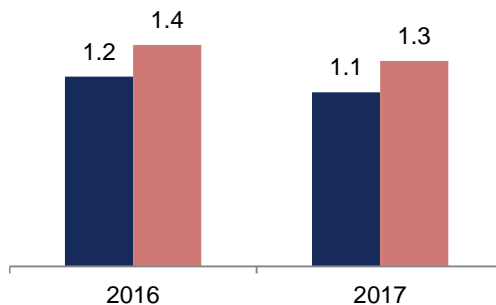
## Liquidity Ratios (%)

— Loan-to-Funds Ratio  
— Basel III Liquidity Coverage Ratio



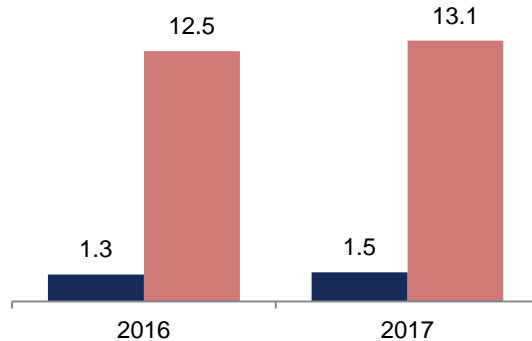
## Asset Quality (%)

■ Net Impaired Loans Ratio  
■ Total Provisions to Total Loans Ratio



## Returns on Asset and Equity (%)

■ Return on assets ■ Return on equity



1 Financial sector has undergone significant structural and regulatory reforms over the years to enhance resilience

2 Stress tests affirm financial institutions' resilience to withstand severe shocks under adverse macroeconomic and financial conditions

➤ Banks' total capital ratio estimated to remain above 10% under the stress scenarios

Source: Bank Negara Malaysia



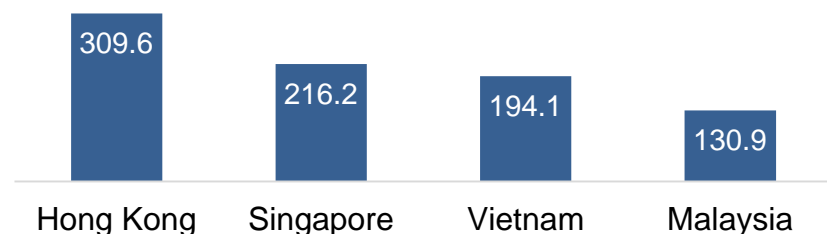
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# Business-friendly policies and attractive investment environment facilitate Malaysia's long-standing trade and financial openness

Malaysia is one of the most open economies in the world and consistently offers great values to investors

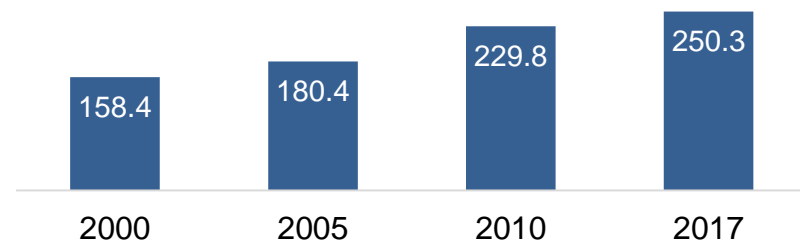
## Malaysia is the fourth most open economy in East Asia

Trade, % of GDP (2017)



## Malaysia continues to show progress in financial openness

External assets and liabilities, % of GDP



Source: Haver Analytics and Bank Negara Malaysia

1 Malaysia consistently scores high in the World Bank's Ease of Doing Business Index

2 The current level of FDI stock has quadrupled, from USD34 billion (2001) to USD144 billion in 2Q 2018

3 Malaysian Investment Development Authority (MIDA) has approved foreign investments worth USD 39 billion in 2013-2017



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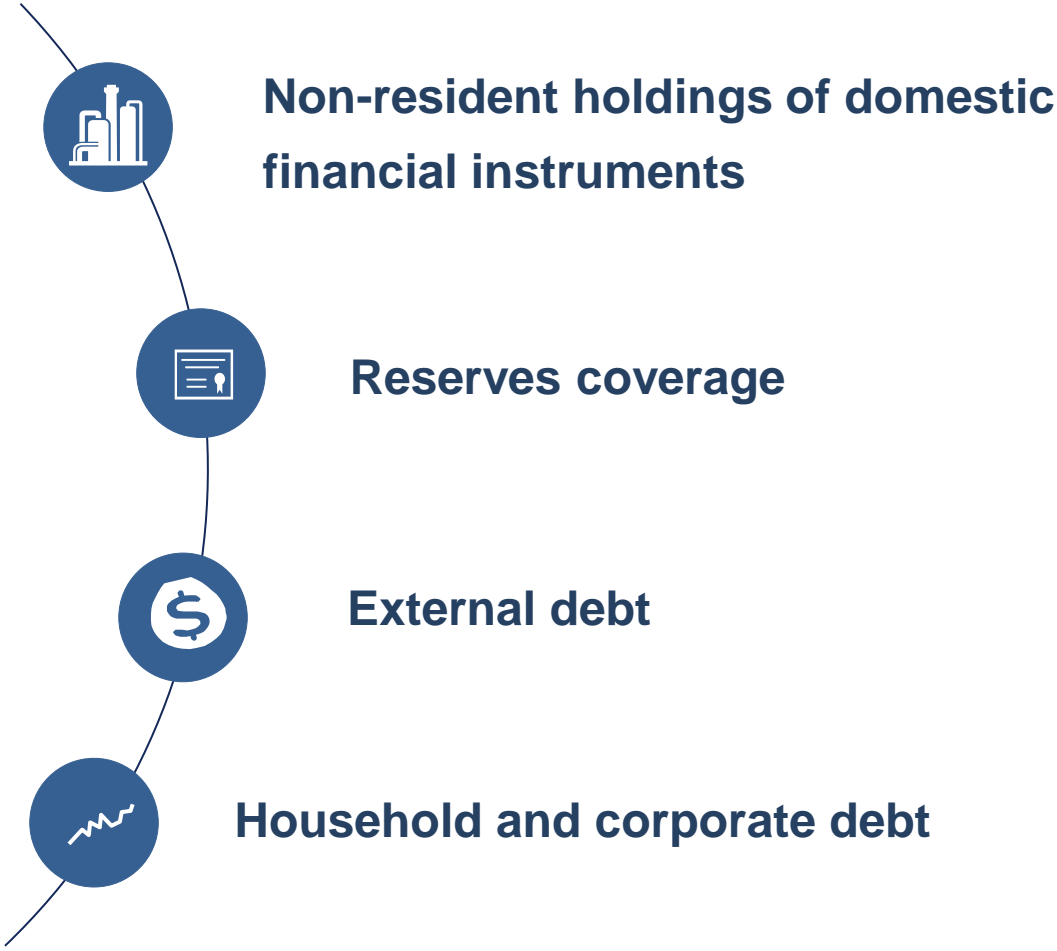
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# Malaysia's underlying strength is the key line of defence against potential headwinds but it is important to look beyond the headline numbers

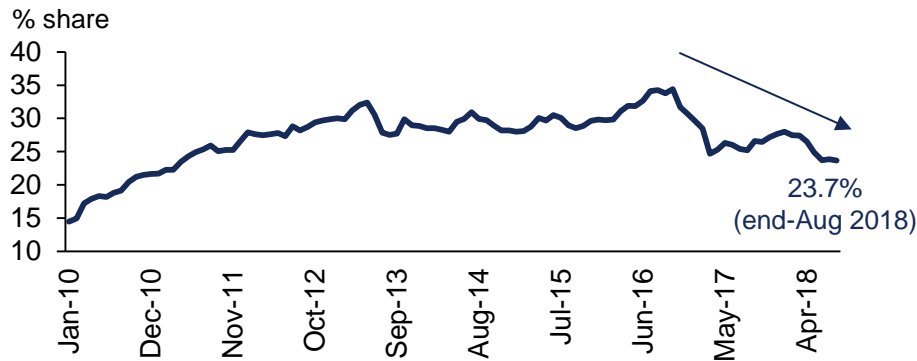




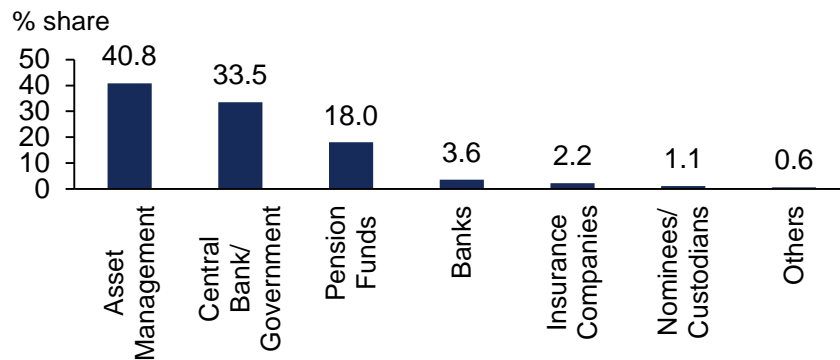
# Non-resident holdings in the domestic financial market have moderated

Stable foreign holders profile and Malaysia's strong financial and banking system reduce the risks of non-resident outflows

### Non-resident Holdings of Government Bonds



### Distribution of Non-resident Holdings in Government Bonds as at June 2018



Source: Bank Negara Malaysia

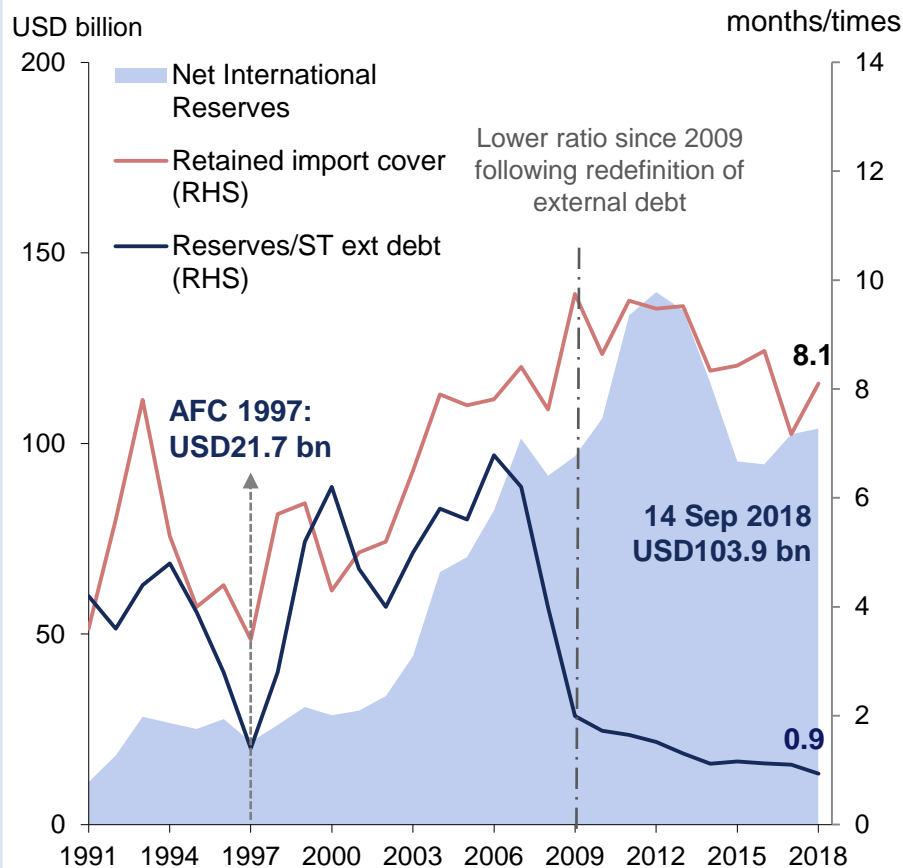
- 1 Non-resident holdings of ringgit-denominated debt securities have moderated
- 2 The majority of foreign holders of Government bonds are long-term stable investors
- 3 Malaysia's deep financial market, participation of domestic institutional investors as well as a highly-capitalised and liquid banking system would mitigate potential non-resident outflows



# International reserves remain adequate and are not the only means to meet external obligations

International reserves have thus far provided sufficient buffers against external shocks and capital outflows

## International reserves (USD billion)



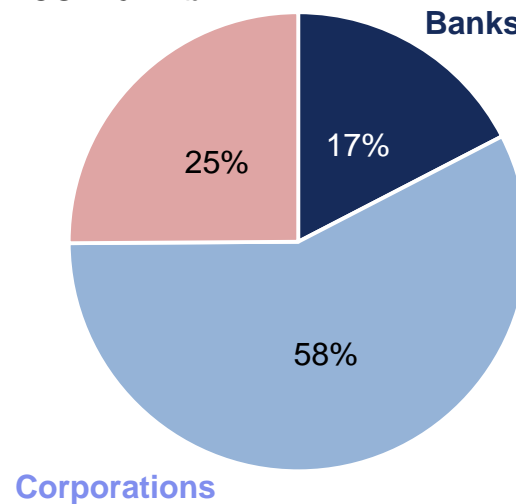
Source: Bank Negara Malaysia

External assets held by banks and corporations can be drawn upon to meet external debt obligations

## External assets (as at end-2Q 2018)

### International Reserves

USD104.7 bn



External assets held by banks and corporations

USD307.2 bn

# Manageable external debt, with favourable debt profile

External debt is skewed towards longer-term, while foreign-currency exposure is manageable

Total external debt as at 2Q 2018: USD229.2 billion (64.7% of GDP)

By Tenure



Medium- to long-term

Short term

*"No immediate repayment requirements"*

By Currency

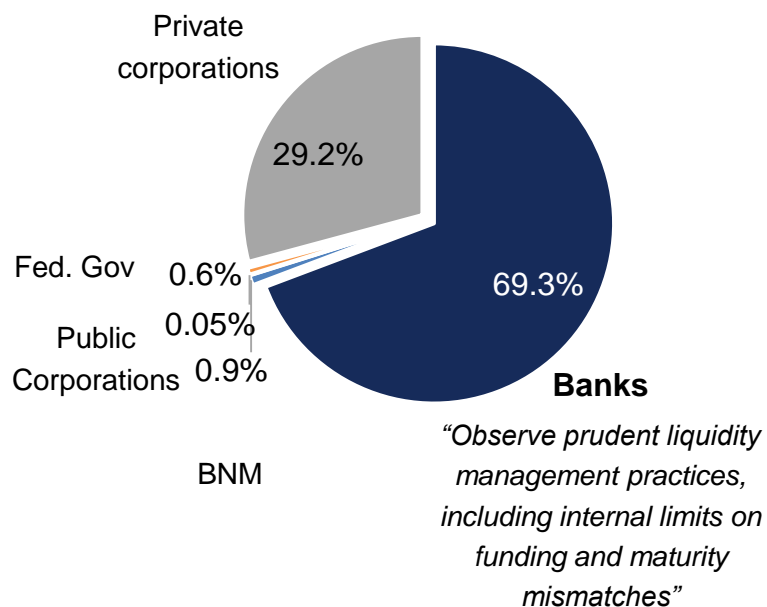


Ringgit

Foreign currency

*"Not affected by valuation"*

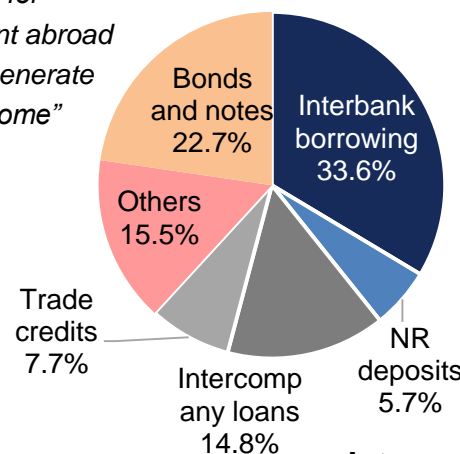
Short-term External Debt by Institutions



Foreign Currency External Debt by Instruments

## Bonds and notes

*"Primarily for investment abroad that will generate future income"*



## Interbank borrowing and non-resident deposits

*"Subject to prudent liquidity management practices, including internal limits on funding and maturity mismatches"*

## Trade credits

*"Backed by exports earnings"*

## Intercompany loans

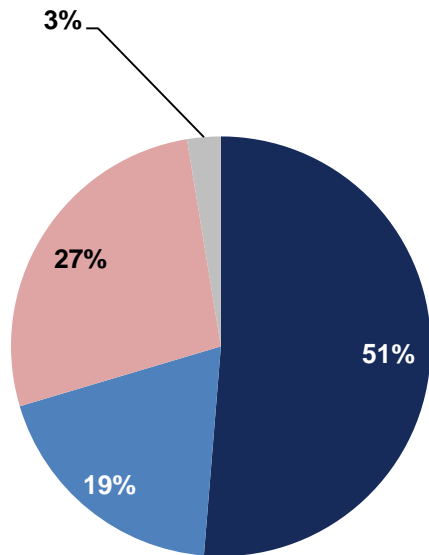
*"Subject to flexible and concessionary terms"*



# Risks associated with banks' external debt are manageable

About half of banks' short-term external debt are stable intragroup placements, thus less susceptible to sudden withdrawal shocks

Banks' Short-term External Debt by Instruments (%)



■ Interbank borrowings (intragroup) ■ Interbank borrowings (unrelated)  
■ NR deposits & vostro ■ Other short-term debt

Banks hold substantial liquid FCY assets to meet external obligations

↓ Liquidity risk exposure



Sizable liquid FCY assets<sup>1</sup> of **RM90.2 bil**

↓ Market risk exposure



Low and stable FX net open position at **5.2%** of total capital

<sup>1</sup> Comprise cash and cash equivalents, short-term interbank placements and debt securities

Source: Bank Negara Malaysia



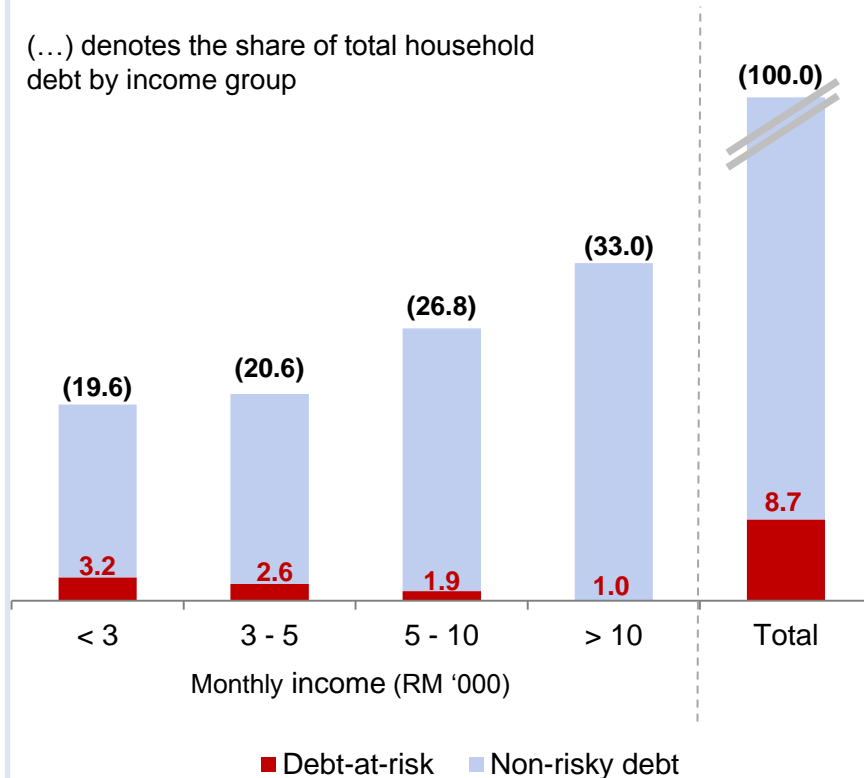
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# Household and corporate sectors' debt are manageable, with debt-at-risk (DAR) well-contained

DAR for borrowers with negative financial margin\* is estimated at only 8.7% of household debt

% share

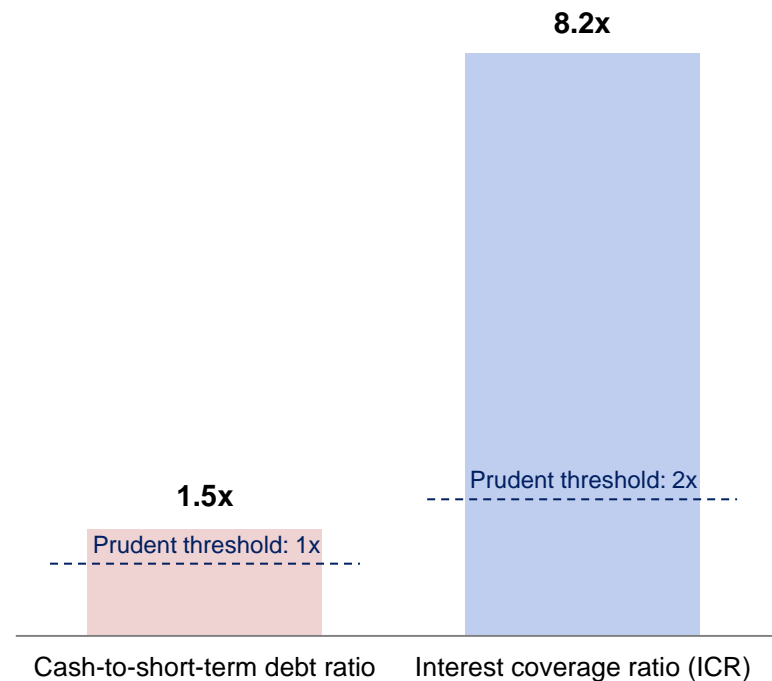
(...) denotes the share of total household debt by income group



\*The balance of borrower's monthly income and liquid financial assets, after deducting debt repayments and expenditure on basic necessities

Source: BNM estimates

Corporate DAR at 7.7% as liquidity position and debt servicing capacity of Malaysian corporations remained intact



Note:

1. Debt-at-risk is defined as the debt borne by firms with ICR<2 times.
2. Based on financial data of 120 companies that are listed on Bursa Malaysia, covering major economic sectors and about 85% of market capitalisation (excluding financial institutions).

Source: Bloomberg and BNM estimates



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# Stress tests further affirm banks' resilience to household, property and corporate sectors

Losses from individuals earning <RM5K per month account for 19.1% of excess capital

## Simulated shocks



**4 times**

increase in default rates from baseline levels



up to **95%**

Loss given default (LGD) for unsecured financing

Losses from large borrower groups account for one-third of excess capital

## Cumulative shocks



**30%**

Depreciation in ringgit



**50%**

Decline in operating profit



**50 bps**

Increase in cost of RM borrowings



**200 bps**

Increase in cost of FCY borrowings

Losses from property-related exposures amount to 3.2 ppt decline in capital ratios

## Simulated shocks



Increase in impairments up to **historical worst** default experience (1997-2001)



**50%** decline in property prices (reversal of 5-year cumulative price growth)

Source: Bank Negara Malaysia



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# Key Takeaways

- 1 **Malaysia's economic outlook remains positive amid a challenging external environment**
- 2 **Monetary policy consistent with intended policy stance amid sustained growth prospects and stable inflation environment**
- 3 **Malaysia's underlying resilience and competitive environment provide attractive investment opportunities**
- 4 **Perceived risks of Malaysia should not be taken at face value given the unique features of the Malaysian economy and financial system**



# Q & A

