

# The Bank's Policy Considerations

## Highlights

- The Monetary Policy Committee (MPC) maintained the OPR at 1.75% at the May and July 2021 MPC meetings, considering the stance of monetary policy to be appropriate and accommodative.
- Fiscal and financial measures will also continue to cushion the economic impact on businesses and households and provide support to economic activity. The Bank remains committed to utilise its policy levers as appropriate to foster enabling conditions for a sustainable economic recovery.

### Monetary policy remains accommodative

At the May and July 2021 Monetary Policy Committee (MPC) meetings, the MPC maintained the Overnight Policy Rate (OPR) at 1.75%.

The MPC assessed that the global economic recovery has strengthened further, supported by improvements in manufacturing and services activity. The pace of recovery, however, varies across countries. Economies making better progress in their vaccination programmes have been able to ease containment measures, enabling a swift recovery in domestic activity. Sizeable fiscal and monetary measures in several advanced economies are also supporting a stronger recovery momentum, although tighter containment measures to curb COVID-19 resurgences have disrupted activities in some economies. Financial conditions remain supportive of growth. Overall, the balance of risks to the growth outlook remains tilted to the downside, due mainly to uncertainty over the path of the pandemic as well as potential risks of heightened financial market volatility.

For the Malaysian economy, better-than-expected economic activity in the first quarter of 2021 continued into April, particularly in exports, retail spending and labour market conditions. The re-imposition of nation-wide containment measures to curb the resurgence in COVID-19 cases, however, will dampen the growth momentum. The degree of impact to the economy is highly dependent on the stringency and duration of containment measures. Nevertheless, the impact of restrictions will be partly mitigated by the continued allowances for essential economic sectors to operate, albeit at a reduced capacity, and higher adaptability to remote work, automation and digitalisation. The various policy support packages will alleviate some

of the financial pressures on households and businesses. Favourable external demand conditions will continue to provide a lift to growth. Going forward, the gradual relaxation of containment measures, alongside the rapid progress of the domestic vaccination programme and continued strength in external demand will provide support for the growth recovery into 2022. The growth outlook, however, remains subject to significant downside risks, due mainly to factors that could lead to a delay in the easing of containment measures or imposition of tighter containment measures, and a weaker-than-expected global growth recovery.

As expected, headline inflation spiked recently due mainly to the base effect from low fuel prices in the second quarter of last year. This spike is transitory and headline inflation is projected to moderate in the near term as this base effect dissipates. For 2021 as a whole, headline inflation is projected to average closer to the lower

bound of the earlier communicated forecast range.<sup>11</sup> Underlying inflation, as measured by core inflation, is expected to remain subdued, averaging between 0.5% and 1.5% for the year, amid continued spare capacity in the economy. The outlook, however, is subject to global commodity price developments.

The MPC considers the stance of monetary policy to be appropriate and accommodative. In addition, fiscal and financial measures will continue to cushion the economic impact on businesses and households and provide support to economic activity. Given the uncertainties surrounding the pandemic, the stance of monetary policy will continue to be determined by new data and information and their implications on the overall outlook for inflation and domestic growth. The Bank remains committed to utilise its policy levers as appropriate to foster enabling conditions for a sustainable economic recovery.

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<sup>11</sup> Headline inflation in 2021 was projected to average between 2.5% to 4.0%, as published in the BNM Economic & Monetary Review 2020 publication.

## Other policy highlights in the second quarter of 2021

| Policy highlight  | Salient details   |
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| <p>Discussion Paper (DP) on Risk-Based Capital Framework for Insurers and Takaful Operators (Framework Design)</p>  | <ul style="list-style-type: none"> <li>• Issued on 30 June 2021, the DP outlines proposed enhancements to the design of the capital adequacy framework for licensed insurers and licensed takaful operators (ITOs). This forms part of the Bank’s multi-phase review of the overall solvency framework.</li> <li>• The proposed enhancements aim to ensure that the framework remains effective under changing market conditions and facilitates consistent and comparable capital adequacy measurements across ITOs.</li> <li>• The key areas addressed in the DP are – <ul style="list-style-type: none"> <li>o recognition of the loss absorbing capacity of management actions under Total Capital Available;</li> <li>o appropriate target risk level for calibration of capital charges;</li> <li>o measurement approach for the risk components under Total Capital Required; and</li> <li>o feasibility of a single formula to calculate the Capital Adequacy Ratio for ITOs, taking into consideration the uniqueness of the insurance and takaful business models.</li> </ul> </li> <li>• The DP is open for feedback until 30 September 2021.</li> </ul> |
| <p>Policy Document (PD) on Anti-Money Laundering, Countering Financing of Terrorism and Targeted Financial Sanctions for Financial Institutions (AML/CFT and TFS for FIs) (Supplementary Document No. 1) - Money Services Business Sector</p> | <ul style="list-style-type: none"> <li>• The PD was issued on 30 June 2021.</li> <li>• The PD sets out the minimum requirements that an approved money services business (MSB) licensed under the MSB Act 2011 must observe in implementing a non-face-to-face verification process when on-boarding corporate customers.</li> <li>• This is to ensure effective and robust Anti-Money Laundering and Counter Financing of Terrorism control measures and systems are in place to safeguard the integrity of money services.</li> </ul>   |
| <p>Exposure Draft (ED) on Electronic Money (E-Money)</p>  | <ul style="list-style-type: none"> <li>• Issued on 11 June 2021, the ED sets out proposed enhancements to the regulatory requirements for approved e-money issuers (EMIs).</li> <li>• The proposed requirements aim to ensure the safety and reliability of e-money issued by EMIs, which in turn will preserve customers’ and merchants’ confidence in accepting e-money for the payment of goods and services.</li> <li>• The key areas addressed in the ED include – <ul style="list-style-type: none"> <li>o proportionate application of minimum capital funds requirements on EMIs in line with the significance of their operations;</li> <li>o proposed exemptions from authorisation requirements for limited purpose EMI;</li> <li>o strengthened requirements on safeguarding of customer funds; and</li> <li>o enhancements to prudential requirements such as governance and management of operational risks.</li> </ul> </li> <li>• The ED was open for consultation until 31 July 2021.</li> </ul>   |
| <p>PD on Corporate Strategic Plan for DFIs</p>  | <ul style="list-style-type: none"> <li>• The PD sets out expectations for development financial institutions (DFIs) to develop holistic and integrated corporate strategy plans that encapsulate their business plans and funding requirements.</li> <li>• The strategic plans aim to strengthen the focus of DFIs on their developmental outcomes and mandates, supported by the clear identification and measurement of ‘additionalities’ (defined as positive impacts attributable to DFIs beyond what is delivered under a solely profit-driven environment).</li> <li>• The PD was issued on 27 May 2021.</li> </ul>   |

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| <p>DP on Alternative Reference Rate and Strategic Direction on KLIBOR and KLIRR for the Malaysian Financial Markets</p> | <ul style="list-style-type: none"> <li>• This DP was issued on 19 May 2021 to seek feedback on the framework, design and features pertaining to the development of an Alternative Reference Rate (ARR), potential enhancements to the Kuala Lumpur Interbank Offered Rate (KLIBOR) as well as a review of the Kuala Lumpur Islamic Reference Rate (KLIRR).</li> <li>• The DP outlines the features of the proposed transaction-based ARR, proposals to refine KLIBOR and its fallback plans, and the future direction for KLIRR.</li> <li>• The DP, which was issued in consultation with the Financial Markets Committee, was open for feedback until 18 June 2021.</li> </ul>  |
| <p>Climate Change and Principle-based Taxonomy</p>  | <ul style="list-style-type: none"> <li>• Developed in collaboration with the Joint Committee on Climate Change (JC3) Risk Management Sub-committee, this document introduces a principle-based taxonomy for assessing and categorising economic activities according to the extent to which the activities meet climate objectives and promote the transition to a low-carbon economy, as well as the extent of their associated impact on the broader environment. The taxonomy facilitates the standardised classification and reporting of climate-related exposures by financial institutions to support risk assessments, climate risk-related financial disclosures and financial flows towards supporting climate objectives.</li> <li>• The standardised classification categorises economic activities into 3 broad groups based on 5 guiding principles that encapsulate climate change mitigation, adaptation, no harm to the environment, remedial measures to transition and prohibited activities: <ul style="list-style-type: none"> <li>o Climate Supporting – Activities with positive impacts on climate change, and that do not cause significant harm to the environment;</li> <li>o Transitioning – Activities that cause significant harm to the environment, but with remedial measures taken to reduce the harm; and</li> <li>o Watchlist – Activities that cause significant harm to the environment and there are no remedial measures taken to reduce the harm.</li> </ul> </li> <li>• The principle-based approach recognises the diverse state of transition towards sustainable practices across businesses, and encourages efforts to achieve an orderly transition of the economy in meeting the climate objectives.</li> <li>• The final document was issued on 30 April 2021.</li> </ul> |