The Changing Pattern of Financing of the Economy

Introduction

With the strengthening of the banking system, growth in bank lending has become more robust in providing the necessary financing to support economic growth. Since 2000, a significant shift in the pattern of bank lending has also occurred in line with the changing economic structure and sources of economic growth.

Increased bank lending to support domestic economic activity

Amidst ample liquidity conditions and low interest rates, bank lending has resumed since the 1998 crisis to support the higher level of economic activities. In value terms, loan applications and approvals in 2002 recorded the highest level in five years. Loans disbursed in 2002 were higher than the level recorded in 1997. In the first six months of 2003, loan applications and approvals have improved further to record a monthly average of RM18.2 billion and RM12.2 billion respectively (RM18.1 billion and RM11.5 billion respectively in 2002). Notwithstanding the uncertainties arising from the geopolitical tension and SARS outbreak, loan disbursements remained high at a monthly average of RM34.2 billion (RM34.3 billion in 2002). While growth in lending activity is reflected in the higher loan applications, approvals and disbursements, the growth in outstanding loans also reflects the high level of repayments. The significant repayments followed the restructuring and refinancing exercise, which resulted in either loans written off by the banking institutions or refinanced through the bond market or converted into equity.

As part of the effort to promote endogenous sources of growth, efforts were undertaken to enhance SME contribution to growth in the domestic economy. Private domestic consumption was also being promoted to further support domestic growth. The banking system has responded positively to the policy shift with bank lending shifting towards higher lending to the consumers and the small and medium enterprises (SMEs). In terms of maturity structure of

Banking System: Loan Indicators

	Monthly average							Annual growth	
	1997	1998	1999	2000	2001	2002	J-Jun 03	2002	Jun-03
	RM billion							%	
Total									
Loan applications	20.9	7.4	10.7	17.4	15.9	18.1	18.2	14.1	14.5
Loan approvals	17.7	5.5	8.7	11.2	10.5	11.5	12.2	9.7	24.5
Loan disbursements	28.2	20.9	26.5	30.1	31.1	34.3	34.2	10.3	8.5
Loan repayments	22.3	22.5	27.7	28.9	30.4	33.6	32.9	10.3	-3.9
Change in outstanding loans	7.4	0.4	0.1	2.0	1.4	1.7	2.0	4.2	3.9
Of which									
Businesses									
Loan applications	n.a.	n.a.	n.a.	n.a.	n.a.	11.3	10.3	n.a.	10.2
Loan approvals	13.4	3.9	5.1	6.6	5.3	5.7	6.3	7.9	45.8
Loan disbursements	23.2	17.6	21.4	22.5	22.5	23.5	23.3	4.3	6.5
Loan repayments	18.5	19.0	22.4	22.4	23.1	23.0	22.6	-0.3	-7.0
Change in outstanding loans	4.2	0.2	0.5	0.3	-0.5	-0.3	-0.1	-2.1	-1.7
Households									
Loan applications	n.a.	n.a.	n.a.	n.a.	n.a.	6.8	7.5	n.a.	14.9
Loan approvals	3.6	1.4	3.3	4.4	4.9	5.6	5.7	13.5	6.6
Loan disbursements	3.9	2.6	4.1	6.3	7.2	8.8	8.9	21.1	14.3
Loan repayments	3.0	2.8	4.2	5.4	6.0	7.0	7.3	17.3	12.1
Change in outstanding loans	2.7	-0.4	0.3	1.4	1.9	2.2	1.8	14.8	12.7

Loans of the Banking System[1] by Customers, 2001 - June 2003 Outstanding as at end-period, RM billion

	2000	% share	2002	% share	Average Annual Growth rate 2001-2002	June 2003	% share	Annual Growth Rate as at end-Jun 03
Loans extended to:								
Household sector	157.4	34.7	206.8	42.2	14.6	217.9	43.4	12.7
Business sector	260.7	57.4	252.1	51.4	-1.6	251.4	50.1	-1.7
Small and medium enterprises	70.5	15.5	74.6	15.2	2.8	78.0	15.5	4.9
Others	190.1	41.9	177.6	36.2	-3.4	173.4	34.5	-4.4
Others [2]	36.0	7.9	31.3	6.4	-6.7	32.7	6.5	-4.6
TOTAL [3]	454.0	100.0	490.3	100.0	3.9	502.0	100.0	3.9

[1] Include Islamic banks
[2] Others refer to Government, financial institutions, other domestic entities and foreign entities.
[3] Include loans sold to Cagamas and Danaharta

loans, the lending pattern has also changed, becoming more skewed towards shorter-term loans for working capital as large corporations with longer-term financing requirements issue more private debt securities (PDS) to meet their financing needs. Overall, this changing pattern has led to higher share of consumer and SMEs loans to total bank lending.

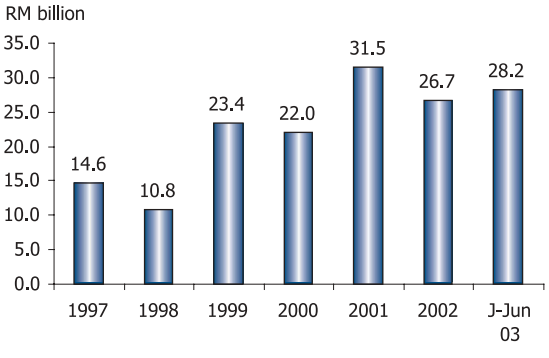
More diversified sources of financing

While the banking sector remains the most important source of financing, large corporations have increasingly raised funds from the bond market for longer-term capital requirements. During the period 1997 to June 2003, the significant debt restructuring has also resulted in refinancing of existing debt by the issue of private debt securities. PDS issued have therefore increased at an average annual growth of 12.8% in the period 1998-2002 with PDS outstanding to GDP increasing from 16.5% in 1997 to 32.2% as at end-June 2003. Amidst the low interest rate environment, large corporations have issued PDS to lock in long-term funds at low cost. Issuance of PDS also ensures that longer gestation projects are being financed by longer-term funds, thus reducing the risks of maturity mismatch for corporations. This has improved the risk management of both corporations and banking system. Total issuance of PDS from January 2001 to June 2003 amounted to RM86.4 billion, 53.7% increase from the issuance of RM56.2 billion recorded during the period 1998-2000. Issuance in the first half of 2003 has exceeded the total issuance for the whole year of 2002.

Banking institutions continue to extend indirect financing to the business sector through significant holding of PDS issued by the private sector. Taking into account this indirect financing,

Large corporations are increasingly raising funds from the bond market. Issuance in the first half of 2003 have exceeded total issuance for the whole of 2002

Gross PDS issuance



Financing through Banking System[1] and PDS, 2001-June 2003 Outstanding as at end-period, RM billion

	2000	2002	Average Annual Growth Rate 2001-2002	Jun-03	Annual Growth Rate as at end-Jun 03
Financing by the banking system	**472.1**	**518.4**	**4.8**	**532.4**	**5.1**
Loans Outstanding[2](A)	454.0	490.3	3.9	502.0	3.9
Holdings of PDS	18.1	28.1	24.8	30.4	31.9
PDS Outstanding[3](B)	**100.5**	**104.0**	**1.7**	**123.1**	**27.2**
Total (A) + (B)	**554.5**	**594.2**	**3.5**	**625.1**	**7.8**

1 Include Islamic banks
2 Include loans sold to Cagamas and Danaharta
3 Refers to total PDS issued by the private sector with original maturity period of more than one year. Exclude debt securities issued by banking institutions, Khazanah, BNM, Cagamas, Danaharta and Danamodal.

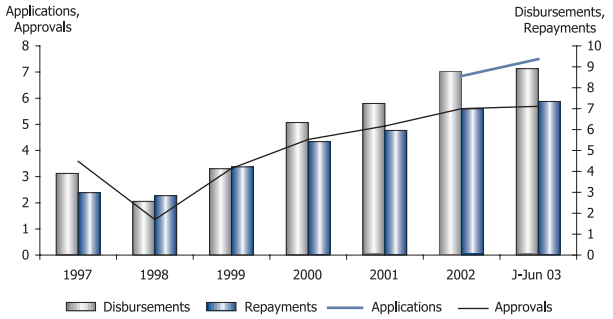
total financing of the private sector by the banking system expanded at an average annual rate of 4.8% during 2001-2002 and 5.2% as at end-June 2003. Consequently, the loan-deposit ratio, including holdings of private debt securities by the banking system, stood at 93.8% as at end-June 2003 (92% as at end-2000). After taking into account redemptions, net financing raised through the banking system and the PDS market rose by 3.5% during 2001-2002 and at a higher rate of 7.8% as at end-June 2003.

Significant growth in bank lending to households reflects policy to promote domestic consumption

The policy to stimulate consumption spending through monetary and fiscal measures has contributed to significant increase in consumption spending. In line with stronger growth in private consumption, financing extended to households by the banking system has increased at a significant average annual rate of 14.6% in the period 2001-2002 and by 12.7% as at end-June 2003. This rapid growth in household loans raised the share of household loans to 43.4% of total loans outstanding as at end-June 2003, from 34.7% as at end-2000. Of the total loans disbursed to the household sector during this period, 31.8% was for purchase of houses, 26.4% for financing of cars and 41.8% for consumption credit. The higher lending to

Lending to households has been on an upward trend, supporting the strong growth in private consumption

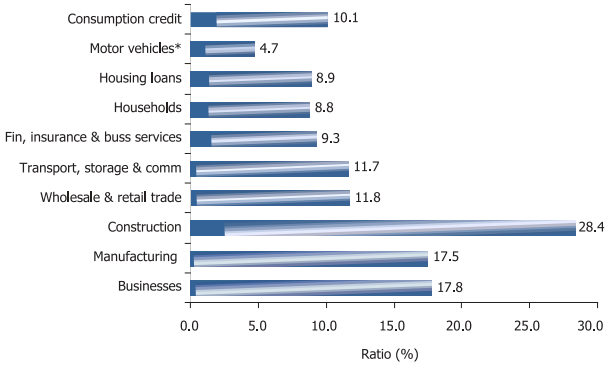
Lending to Household Sector (Monthly averages, RM billion)



household sector has not created increased risks given the high savings rate of the Malaysian households. The risk of household loans turning non-performing has remained at 8.8%, the lowest rate compared with NPLs for other categories. The banking institutions also have the capacity to monitor loan exposure through the Centre for Credit Reference Information System (CCRIS) to ensure that exposure of households remain within prudential limits.

Default rate of household loans has been low at 8.8%

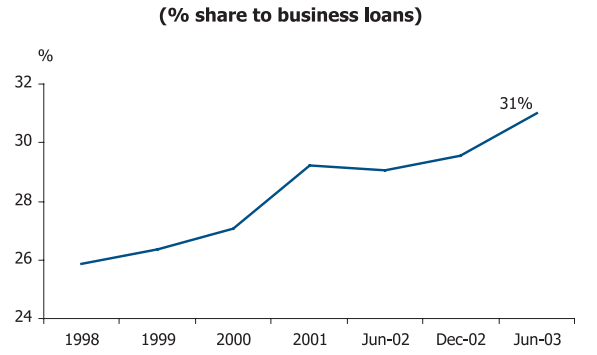
Non-Performing Loans of the Banking System Ratio against outstanding loans as at end-June 2003



* Include passenger cars

Lending to SMEs has increasingly gained importance as evident by the rising share to total business portfolio of the banks

Loans Outstanding to SMEs



Lending by the Banking System[1] to Small and Medium Enterprises (SMEs), 2002-Jun 2003

	2002	Jan-Jun 2003	Total	% share to total loans	% share to business loans
(During the period, RM billion)					
Amount of loans approved	30.7	12.0	42.7	20.2	40.2
Amount of loans disbursed	49.5	40.2	89.7	14.5	21.3
(During the period, Unit)					
No of loans approved	74,233	37,648	111,881	3.5	n.a.

[1] Include Islamic banks

Strong growth in lending to SMEs

Another significant development is the increased bank lending to SMEs. Outstanding loans to SMEs increased at an average annual rate of 2.8% in 2001-2002 and at a higher annual rate of 4.9% as at end-June 2003. Data available for 2002 and the first half of 2003 showed that a total of RM42.7 billion of loans were approved to 111,881 SMEs. Total loans disbursed were higher, amounting to RM89.7 billion, reflecting the higher turnover of loans. For the first half of 2003 alone, RM12 billion was approved to more than 37,000 SMEs whilst disbursements amounted to RM40.2 billion compared RM49.5 billion for the whole of 2002. As at end-June 2003, SMEs loans to total business loans outstanding accounted for 31% compared with 26.4% as at end-1999.

The higher lending to SMEs has followed the concerted efforts to enhance access to financing to this group (details in the next article). Measures have focused on building the infrastructure to support increased access to financing by SMEs. Banking institutions have now established special units for SME financing, Loan Rehabilitation Units and Bumiputera Development Units. The Credit Guarantee Corporation and ERF Sdn Bhd have also been enhanced. At Bank Negara Malaysia, an SME Special Unit has been established. Other measures include the strengthening of the effectiveness of

Status of Special Fund under the Administration of Bank Negara Malaysia, 2000 - Jun 2003

	Total allocation at end Jun-03	Loan approvals				Utilisation Rate at end Jun-03	Loan disbursements			
		Total as end		Change (2001-June 2003)			Total as end-		Change (2001-June 2003)	
		2000	June 2003				2000	June 2003		
	RM million				%	%	RM million			%
Fund for Food	1,300	854	1,386	532	62.3	106.6	740 0	1,216	476	64.4
New Entreprenuer Fund 2	900	0	802	802	-	89.1		591	591	-
Fund for SMIs 2	1,250	99	1,506	1,406	1,416.7	120.5	43	1,077	1,035	2,424.9
Bumiputra Entreprenuer Projecy Fund	300	0	407	407	-	135.8	0	324	324	-
Rehabilitation Fund for SMIs	500	288	326	38	13.2	65.2	235	297	62	26.5
Entreprenuer Rehabilitation & Development Fund	500	0	3	3	-	0.6	0	1	1	-
Total	**4,750**	**1,241**	**4,430**	**3,189**	**256.9**	**93.3**	**1,017**	**3,506**	**2,489**	**244.7**

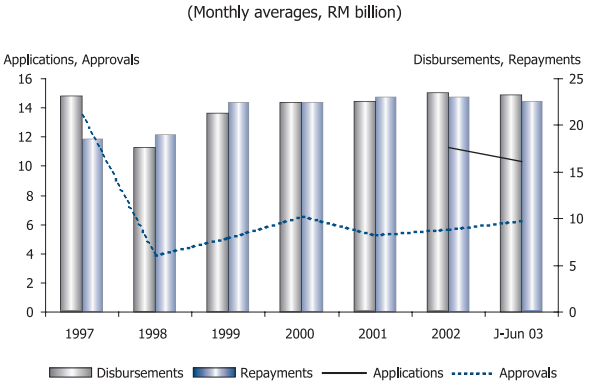
special funds by expanding the scope and size of special funds, liberalising the eligibility criteria of selected special funds, establishing new funds as well as lowering the cost of borrowing. To date, a total of RM4.8 billion has been allocated for special funds. The utilisation rates of these funds were high. A total of RM4.4 billion has been approved and a total of RM3.5 billion has been disbursed as at end-June 2003.

Lending by banks to businesses is now more skewed towards shorter-term financing

The pattern of maturity structure of loans has also changed reflecting the shift in the sources of economic growth to a more domestic driven growth and from an investment-led to increased consumption and the increased reliance of larger corporations on PDS market for longer-term funds. This has resulted in increased demand for shorter-term borrowing. Large corporations seek revolving credit and overdrafts facilities from the banking system to finance short-term working capital. As a result, long-term loans with the maturity of more than one-year extended to the business sector accounted for only 26.3% of total loans as at end-June 2003, down from 30% as at end-1997. For the households, consumption credit is mainly with short-term maturity while housing and car loans have maturity of more than one year. With the rapid growth in consumer loans, the share of housing and car loans have increased from 20.6% of total loans as at end-1997 to 35.7% as at end-June 2003.

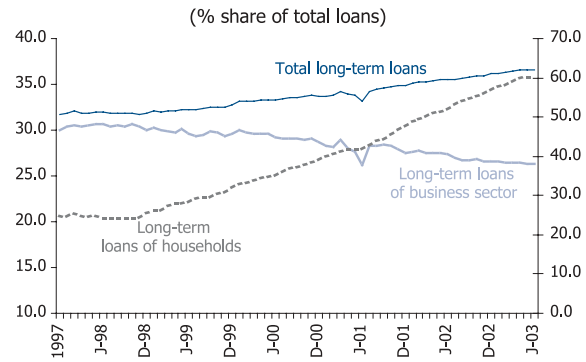
Large corporations continued to raise short-term financing from the banks. This was reflected in the high disbursements and high repayments of loans

Lending to Business Sector



Increase in long-term loans due mainly to long-term loans of households

Long-term Loans of the Banking System



The recourse for more shorter-term funds by the business sector has resulted in higher disbursements, which were being matched by equally high repayments. Consequently, while loans disbursed to the large corporations accounted for 48.5% of the total loans disbursed, the share of this group declined to 34.5% of total loans outstanding as at end-June 2003, from 41.9% as at end-2000. Thus, while this more robust financing activity is not reflected in the outstanding loans, the higher rate of disbursements and its multiplier effects on the economy have been important in supporting the economic growth.