DEVELOPMENTS IN THE BANKING SYSTEM

The banking system maintained its strength and resilience in the second quarter of 2003, as reflected in the strong financial indicators with no signs of vulnerabilities both at the system and institution levels. Of significance was the continued improvement in the quality of loan portfolio and high levels of capitalisation.

Capitalisation sustained at high levels

The capital position of the banking system remained strong with both the risk-weighted capital ratio (RWCR) and core-capital ratio sustained above 13% and 10%, respectively throughout the second quarter. The RWCR stood at 13.1% at end-June 2003. The strong capital position enhanced the capacity of the banking system to extend new loans. Meanwhile, Tier-1 capital declined by RM1.1 billion or 1.8% resulting from a merger between two commercial banks. Consequently, core capital ratio declined marginally to 10.6% at end-June 2003.

Capitalisation of the Banking System

	2002			2003	
	Jun.	Sep.	Dec.	Mar.	Jun.
Capital					
Core-capital ratio (%)	10.9	11.0	11.1	11.0	10.6
RWCR (%)	13.2	13.3	13.2	13.2	13.1

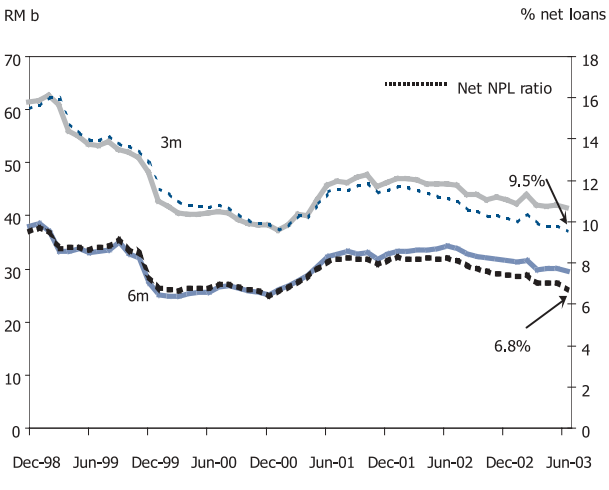
Banking operations remained profitable amidst intense competition

The banking system registered gross operating profits of RM2.9 billion in the second quarter, similar to the level achieved in the preceding quarter. Increased competition in the loan market, particularly in lending to the household sector, resulted in a flat growth in net interest income. In addition, the higher income of RM0.9 billion from fee-based activities (increase of RM0.5 billion) offset the increase in administrative expenses. However, the increased recoveries of RM2.4 billion (increase of RM1.4 billion) and trading and investment income of RM1.5 billion (increase of RM0.5 billion) contributed to increase in the profit before tax of the banking system by 16% to RM2.8 billion.

NPLs trending downwards

The level of non-performing loans (NPLs) of the system in the second quarter of 2003 improved further as a result of higher loan write-offs and implementation of debt restructuring schemes. Net NPLs on a six-month classification declined to RM29.6 billion or 6.8% of net total loans from 7% as at end-March 2003 (three-month classification: declined to 9.5% from 9.9% as at end-March 2003). During the quarter, a total of RM2.5 billion of loans

Banking System: Non-performing Loans



were written off whilst recoveries amounted to RM2.4 billion. Loans classified as NPLs during the quarter amounted to RM5.6 billion, a decline of 9.4% compared with RM6.2 billion in the previous quarter. The loan loss coverage ratio remained comfortable at 61.1%.

In terms of economic sector, the level of NPLs for the business sector declined by RM1.8 billion to account for 16.4% of total business loans primarily due to conversions of manufacturing and construction-related loans into bonds as part of debt restructuring exercises. Meanwhile, NPLs for the household sector increased only moderately by RM0.2 billion to RM17.1 billion with NPLs for the purchase of residential properties grew by RM0.3 billion to RM9.6 billion. The increase in incidence of default in the household sector remained manageable, with NPLs for household sector accounting for 8.5% of total household sector loans.