

BANK NEGARA MALAYSIA
CENTRAL BANK OF MALAYSIA

The BNM Quarterly Bulletin presents a quarterly review of Malaysia's economic, monetary and financial developments. It includes the Bank's latest assessments on the direction of the economy going forward. The Bulletin also provides insights on current economic and financial issues, including highlights of policy initiatives undertaken by Bank Negara Malaysia in pursuit of its mandates.

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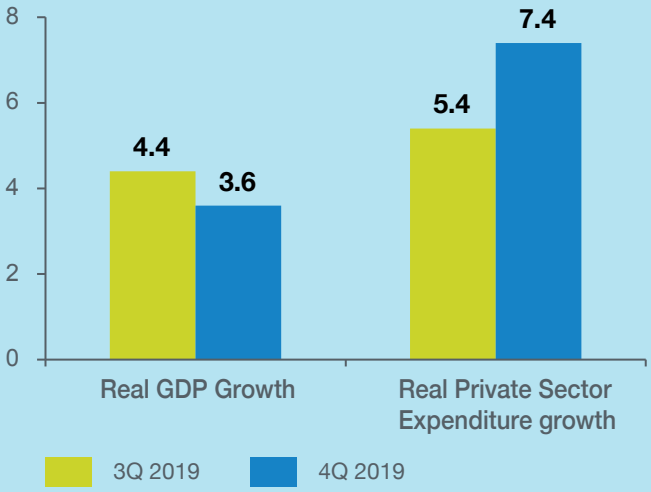
Key Highlights on

# Economic and Financial Developments in 4Q 2019

## The Malaysian economy grew by 3.6% in the fourth quarter

**Growth was underpinned by stronger private sector expenditure, amid supply disruptions in the commodities sector**

Annual change (%)




Continued income and employment growth anchored household spending

Private investment improved to 4.2% (3Q'19: 0.3%)

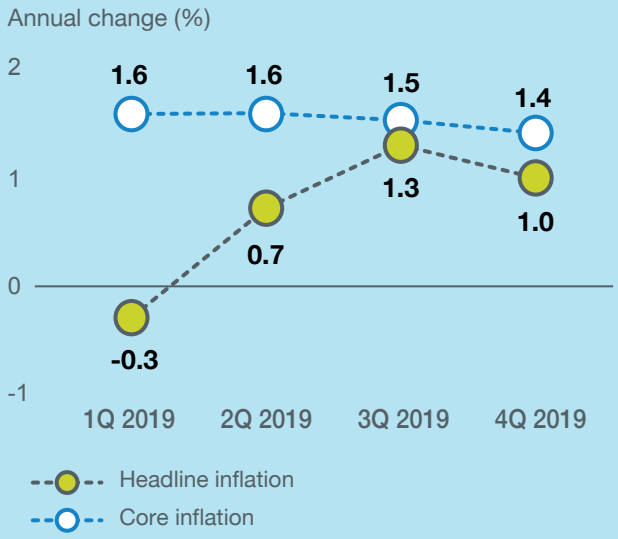
Commodities sector affected by supply disruptions

- Agriculture contracted by 5.7% (3Q'19: +3.7%)
- Mining remained in contraction (-2.5%, 3Q'19: -4.3%)

## Headline inflation averaged lower in the fourth quarter

**Lower headline inflation as the impact of the SST implementation lapsed**

Headline and Core Inflation[1]




[1] Core inflation is computed by excluding price-volatile and price-administered items. It also excludes the estimated direct impact of consumption tax policy changes.

Lapse in the impact of the SST implementation

Fuel inflation continued to exert downward pressure as domestic retail fuel price ceilings were maintained

Core inflation was stable amid the absence of strong demand pressures and moderate expansion in private sector wages

Source: Department of Statistics Malaysia, Bank Negara Malaysia unless stated otherwise
For more information, visit www.bnm.gov.my

# International Economic Environment

## HIGHLIGHTS

- Global growth remained weak in the fourth quarter of 2019.
- Exports in regional economies showed signs of soft recovery.
- Financial market volatility receded as the trade dispute de-escalated.

### Global economic activity remained weak

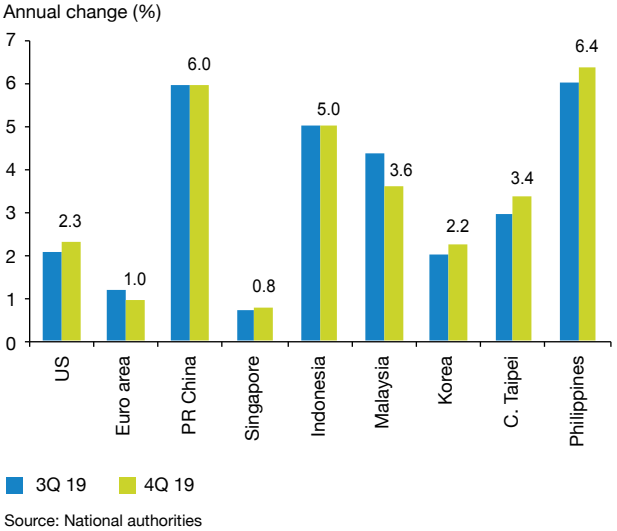
The global economy expanded at a moderate pace in the fourth quarter of 2019.

Growth in the US improved, driven by higher public spending and lower imports. These more than offset the moderation in private investment, which was affected by slower manufacturing activity and poor business sentiments. Meanwhile, private consumption was sustained on the back of supportive labour market conditions.

Growth in most regional economies improved marginally, with early signs of recovery in exports and sustained domestic demand. Growth in PR China was sustained at 6.0% in the fourth quarter, supported mainly by stronger investments amid a pickup in production activity. In Singapore, growth recorded a marginal uptick, due to improving exports, especially to the region and the US.

Modest growth in most economies in 4Q 2019

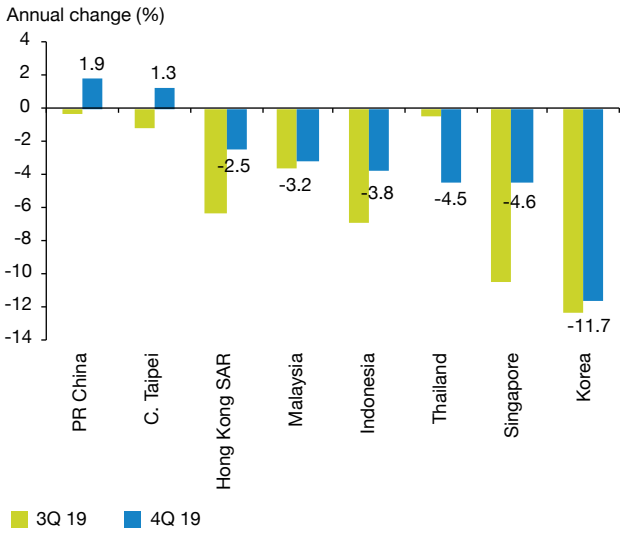
Chart 1: GDP Growth of Selected Economies




Source: National authorities

Improvements in regional export growth in 4Q 2019

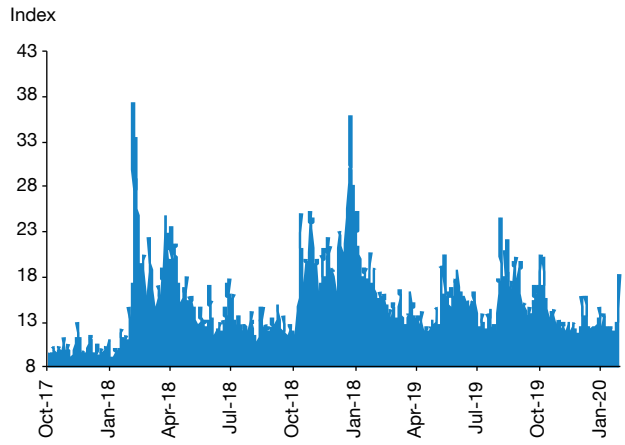
Chart 2: Export Growth of Selected Economies (in USD terms)




Source: National authorities

Global financial market volatility subsided in 4Q 2019

Chart 3: Chicago Board Options Exchange (CBOE) Volatility Index (VIX)




Source: Bloomberg

## Marginal recovery in regional exports growth

Exports showed signs of recovery in several regional economies in the fourth quarter. Exports of goods from PR China rebounded to 1.9%, from a marginal contraction of 0.3%. This was supported by increased demand from the ASEAN economies and the EU. In C. Taipei, goods exports similarly turned around, driven by a broad-based improvement across product segments. Exports from Korea, Indonesia and Singapore remained in contraction, albeit less than the previous quarter.

## Lower volatility in the financial market

Global financial market volatility was lower during the quarter. Positive sentiments, driven by improving trade-related data releases, led to price rallies across major economies. Towards the end of the quarter, expectations on the Phase One trade deal between the US and PR China and its finalisation on 15 January 2020 further contributed to the market rally.

However, there was a marginal spike in volatility prior to the general elections in the UK, attributable to uncertainties surrounding the election results and the subsequent policy direction influencing Brexit outcomes.

Brent crude oil price remained steady at USD62 per barrel in the fourth quarter of 2019, as the extension of voluntary output cuts by OPEC+ and heightened geopolitical tensions in the Middle East more than offset the moderating global oil demand conditions.

# Developments in the Malaysian Economy

## HIGHLIGHTS

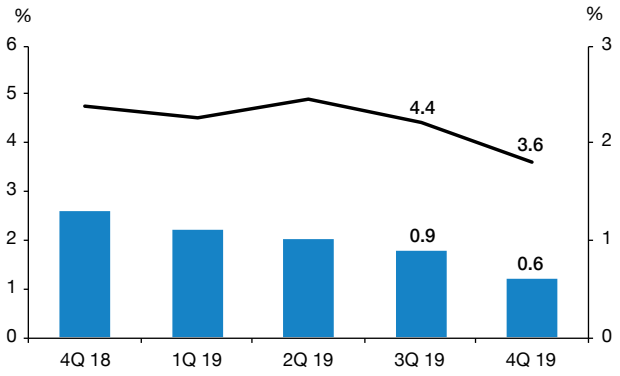
- The Malaysian economy expanded by 3.6% in the fourth quarter of 2019.
- Headline inflation declined in the fourth quarter while core inflation remained stable.
- Current account surplus narrowed to RM7.6 billion (2.0% of GNI).

### The Malaysian economy grew by 3.6% in the fourth quarter of 2019

The Malaysian economy expanded by 3.6% in the fourth quarter of 2019 (3Q 2019: 4.4%), supported by higher private sector spending (7.4%; 3Q 2019: 5.4%). However, growth was affected by a decline in net exports. On the supply side, higher growth in the services and construction sectors was weighed down by supply disruptions in the commodities sector. On a quarter-on-quarter seasonally-adjusted basis, the economy grew by 0.6% (3Q 2019: 0.9%). For 2019 as a whole, the economy expanded by 4.3% (2018: 4.7%).

Continued growth in 4Q 2019

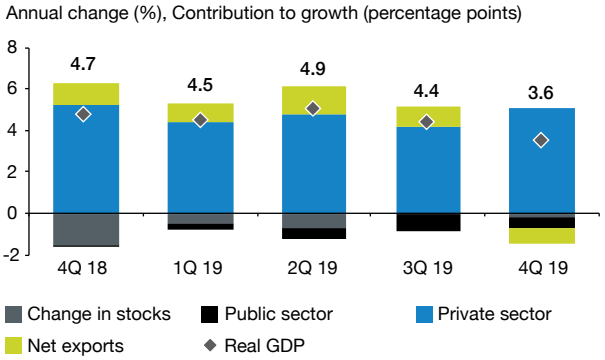
Chart 4: Real GDP Growth




Source: Department of Statistics, Malaysia

**Private sector activity remained the key driver of growth**

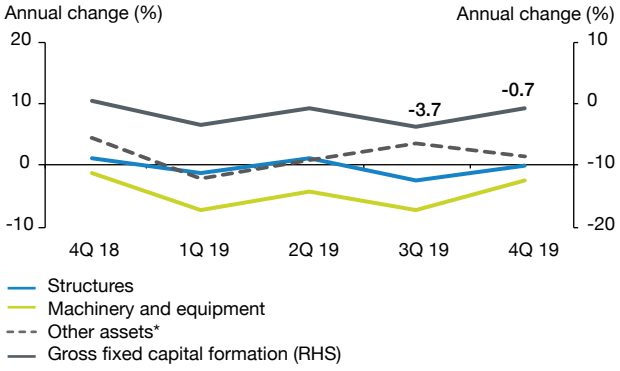
Chart 5: Contribution of Expenditure Components to Real GDP Growth




Source: Department of Statistics, Malaysia

**Smaller contraction in gross fixed capital formation**

Chart 6: GFCF Growth by Type of Assets




*Other assets include mineral exploration, research & development and capitalised planting.

Source: Department of Statistics, Malaysia

## Growth underpinned by domestic demand

Growth was anchored by domestic demand, amid weak net exports. Domestic demand expanded by 4.9% (3Q 2019: 3.5%), driven by higher private sector activity.

Private consumption growth increased to 8.1% (3Q 2019: 7.0%), anchored by positive income and employment growth. This was supported by sustained spending on necessities, such as food and transportation, and leisure-related expenditure, such as restaurants and hotels, and recreational services.

Public consumption expanded by 1.3% (3Q 2019: 1.0%), supported by higher growth in emoluments. Government spending on supplies and services continued to decline, albeit at a smaller pace.

Gross fixed capital formation (GFCF) registered a smaller contraction of 0.7% (3Q 2019: -3.7%). This was mainly underpinned by higher capital spending by the private sector. By type of assets, investment in structures as well as machinery and equipment (M&E) improved, with growth of 0.1% (3Q 2019: -2.4%) and -2.6% (3Q 2019: -7.4%), respectively. Structures investment was supported by implementation of civil engineering projects and the turnaround in the residential segment.

Private investment registered a higher growth of 4.2% (3Q 2019: 0.3%), mainly driven by continued investments in the services and manufacturing sectors. In particular, higher capital expenditure in transport services and construction-related manufacturing had contributed to the growth performance.

Public investment recorded a smaller decline of 7.7% (3Q 2019: -14.1%). This was due to a smaller contraction in capital spending by public corporations amid weak investment by the General Government.

## Higher growth in the services and construction sectors, weighed down by supply disruptions in the commodities sector

The services sector grew at a faster rate (6.1%; 3Q 2019: 5.9%). Growth was mainly driven by firm consumer-related spending, particularly in the food and beverages and accommodation sub-sector, as well as motor vehicles. The finance and insurance sub-sector registered higher growth mainly due to higher fee-based income. Continued demand for data communication services contributed to growth in the information and communication sub-sector, while sustained growth in the transport and storage sub-sector was largely supported by air passenger traffic and port-related activities.

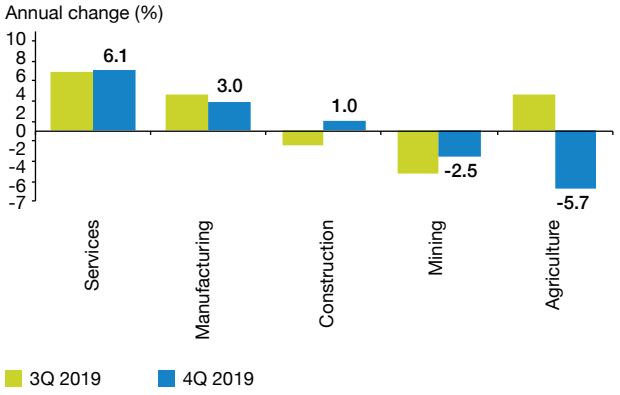
Growth in the manufacturing sector moderated (3.0%; 3Q 2019: 3.6%). E&E production was affected by continued weakness in the global demand for semiconductors. Production disruptions in the commodities sector also had a negative impact on downstream manufacturing activities. Growth in the consumer-related cluster was weaker mainly due to a contraction in oil palm production. In the primary-related cluster, growth moderated following closures of major downstream oil refineries and lower gas liquefaction activities. However, the pace of moderation was cushioned by the operationalisation of large oil refinery and petrochemical facilities in Johor.

Having registered positive growth in the first three quarters of the year, the agriculture sector contracted during the quarter (-5.7%, 3Q 2019: 3.7%). This was due to the decline in oil palm output, which was affected by severe dry weather conditions and cutbacks in fertilizer application during the early part of 2019.

Mining sector growth declined at a slower pace (-2.5%; 3Q 2019: -4.3%), reflecting a smaller decline in oil production as output gradually recovered from major maintenance work that was done in the previous quarter. Growth in natural gas output contracted, as production was affected by temporary facility closures.

### Most sectors expanded, while mining and agriculture sectors contracted

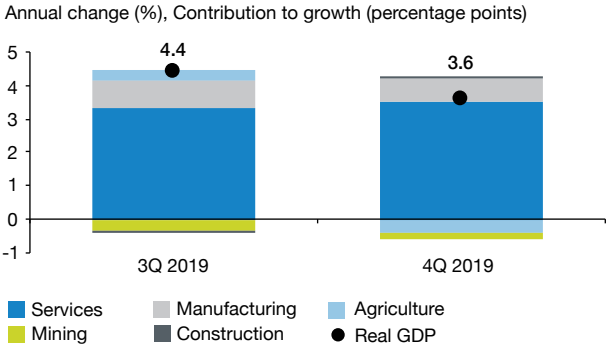
Chart 7: Growth by Sector




Source: Department of Statistics, Malaysia

### Services and manufacturing sectors remained the key drivers of growth

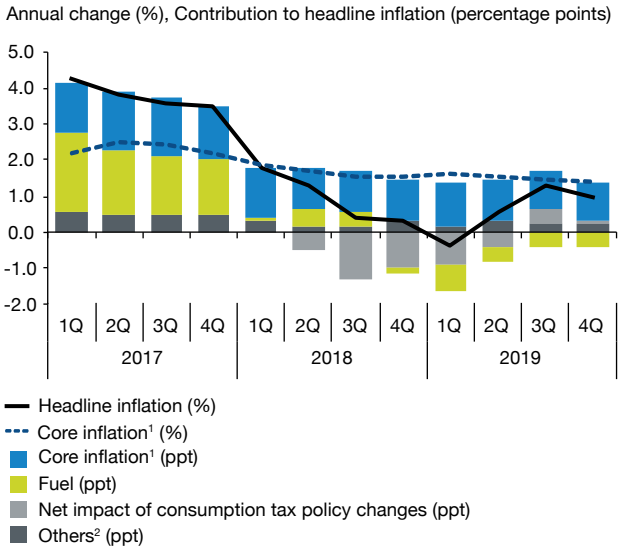
Chart 8: Contributions to Real GDP by Economic Sector




Source: Department of Statistic, Malaysia

**Lower headline inflation as the impact of the SST implementation lapsed**

Chart 9: Contribution to Headline Inflation by Components




[1] Core inflation is computed by excluding price-volatile and price-administered items. It also excludes the estimated direct impact of consumption tax policy changes.

[2] Others include price-volatile items and other price-administered items

Source: Department of Statistics, Malaysia and Bank Negara Malaysia estimates

Growth in the construction sector recovered (1.0%; 3Q 2019: -1.5%) during the quarter. The recovery was mainly attributable to the turnaround in the residential sub-sector, supported by affordable housing activities. Civil engineering activities were also higher, supported by large transportation projects. In addition, higher growth in special trade sub-sector was due mainly to the ongoing solar projects and higher installation and finishing works from the completion of petrochemical and mixed development projects. The non-residential sub-sector however remained in contraction, amid ongoing oversupply of commercial properties.

## Headline inflation declined as the impact of the SST implementation lapsed

Headline inflation, as measured by the annual percentage change in the Consumer Price Index (CPI), decreased to 1.0% in 4Q 2019 (3Q 2019: 1.3%). The lower inflation outcome mainly reflected the lapse in the impact of the SST implementation. Fuel inflation continued to have a negative contribution to inflation, as domestic retail fuel price ceilings were maintained.

Core inflation was stable at 1.4%, reflecting the absence of strong demand pressures in the economy, amid moderate expansion in private sector wages.

## Improved labour market conditions

During the fourth quarter, labour market conditions improved. Employment growth was higher (2.2%; 3Q 2019: 2.1%), while the unemployment rate was lower at 3.2% (3Q 2019: 3.3%) as employment growth outpaced labour force growth during the quarter.

Private sector wage growth was marginally higher at 3.9% (3Q 2019: 3.8%), driven by firm wage growth in both the services and manufacturing sectors. Private services wages grew by 4.2% (3Q 2019: 4.1%), supported by wage growth in the wholesale and retail trade (3.7%; 3Q 2019: 3.6%) and transportation and storage (2.8%; 3Q 2019: 2.6%) sub-sectors. In the manufacturing sector, wages expanded by 3.3% (3Q 2019: 3.2%). This was due mainly to higher wages in the domestic-oriented industries, particularly in the food, beverages and tobacco (3.9%; 3Q 2019: 2.4%) as well as the non-metallic mineral and metal products (3.0%; 3Q 2019: 1.9%). Wages in the electrical and electronics industry, however, moderated (3.8%; 3Q 2019: 4.1%) due to continued weakness in demand for E&E products.

### Higher employment growth

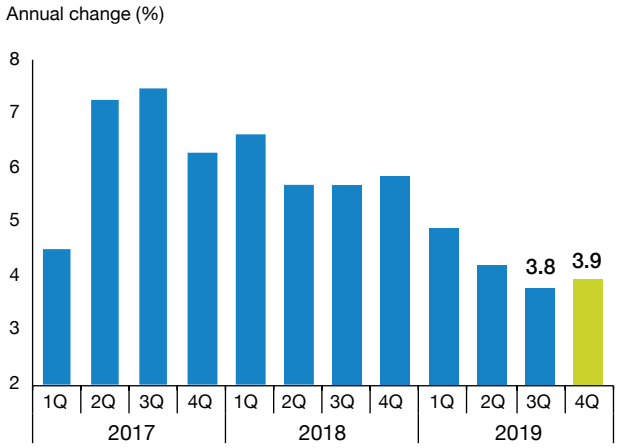
Chart 10: Employment Growth




Source: Department of Statistics, Malaysia

### Marginally higher private sector wages

Chart 11: Private Sector Wages*



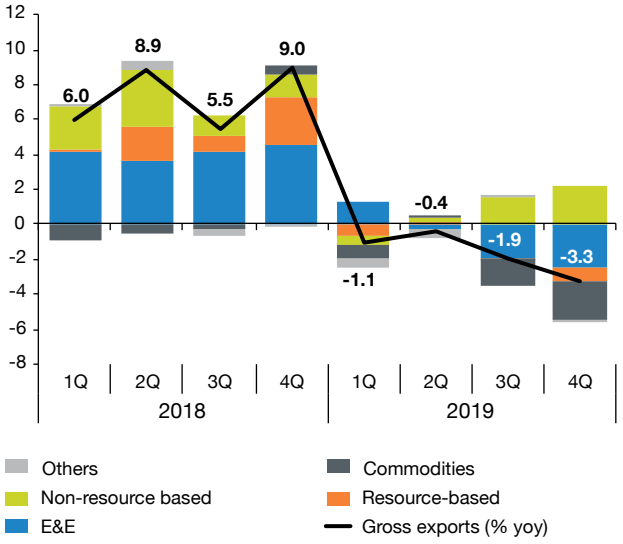

* Private sector wages are derived from the salaries and wages data published in the Monthly Manufacturing Statistics and Quarterly Services Statistics by the Department of Statistics, Malaysia. They cover 62.9% of total employment.

Source: Department of Statistics, Malaysia and Bank Negara Malaysia estimates

### Sharper decline in manufactured and commodities exports

Chart 12: Gross Exports by Products

Annual change (%), Contribution to growth (percentage points)

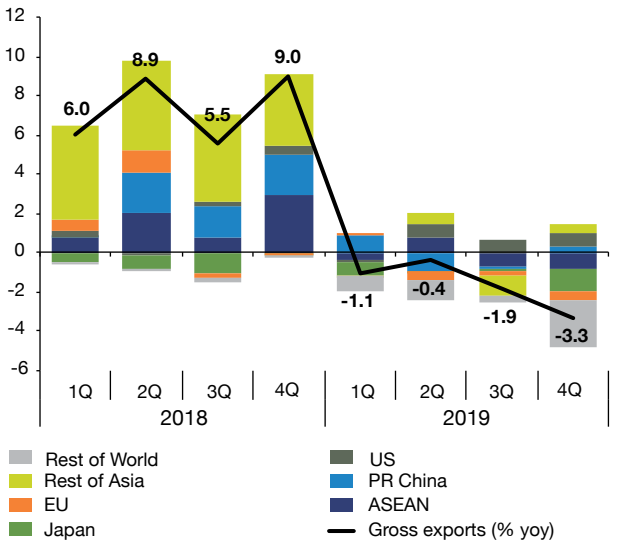



Source: Department of Statistics, Malaysia

### Slowing demand from regional economies

Chart 13: Gross Exports by Markets

Annual change (%), Contribution to growth (percentage points)




Source: Department of Statistics, Malaysia

## Sharper decline in exports while imports registered a smaller contraction

In the fourth quarter of 2019, gross exports contracted by 3.3% (3Q 2019: -1.9%), weighed by declines in both manufactured and commodities exports. Gross imports declined at a slower pace of 4.0% (3Q 2019: -5.8%), due mainly to a positive turnaround in intermediate imports and a smaller contraction in capital imports. The trade surplus[1] increased to RM36.5 billion (3Q 2019: RM33.5 billion).

Manufactured exports contracted by 1.2% (3Q 2019: -0.6%), due mainly to the decline in E&E exports (-6.5%; 3Q 2019: -4.9%) amid lower exports to the US, PR China and regional economies. This partly reflected the slowdown in global semiconductor sales. By contrast, non-E&E exports continued to expand at a sustained pace. Exports of commodities recorded a larger decline (-14.3%; 3Q 2019: -10.0%) due to a sharp contraction in liquefied natural gas exports (-25.2%; 3Q 2019: 4.1%), following temporary facility closures and lower prices.

Intermediate import growth turned positive during the quarter (0.9%; 3Q 2019: -3.0%), due to higher imports of industrial supplies, such as metals and metal products, and parts and accessories of capital goods. Capital imports recorded a smaller decline (-8.9%; 3Q 2019: -15.5%), supported by higher demand for maritime ships, aircrafts and office equipment.

[1] The difference between the goods surplus and trade surplus arises from the exclusion of goods for processing, storage and distribution in the goods accounts as per the 6th Edition of the Balance of Payments and International Investment Position Manual (BPM6) by the IMF.

## Narrower current account surplus

The current account surplus of the balance of payments amounted to RM7.6 billion or 2.0% of GNI in the fourth quarter of 2019 (3Q 2019: RM11.5 billion or 3.1% of GNI). The higher goods surplus was offset by larger income and services deficits.

As the decline in imports outpaced exports, the goods surplus widened to RM32.8 billion (3Q 2019: RM30.8 billion).

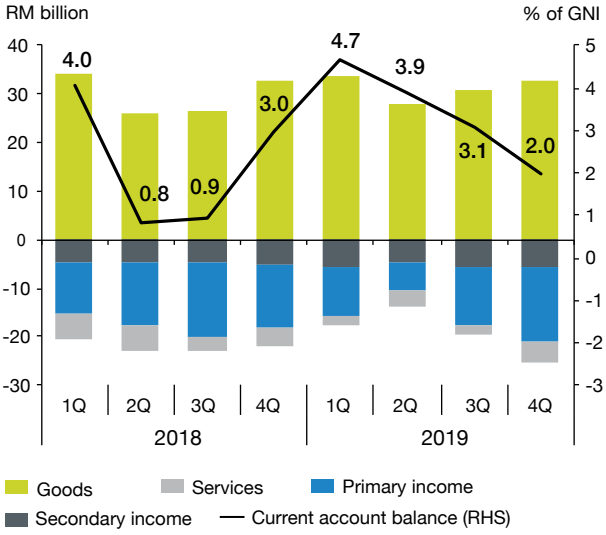
In the services account, the deficit widened to RM4.0 billion (3Q 2019: -RM1.6 billion) during the quarter. This was due primarily to a decline in the travel account surplus (RM6.4 billion; 3Q 2019: RM9.5 billion) following lower tourist arrivals.

The primary income account registered a larger deficit of RM15.7 billion (3Q 2019: -RM12.2 billion). This mainly reflected higher investment income accrued to foreign investors in Malaysia.

The deficit in the secondary income account amounted to RM5.5 billion (3Q 2019: -RM5.5 billion), reflecting continued outward remittances by foreign workers.

Larger income and services deficit

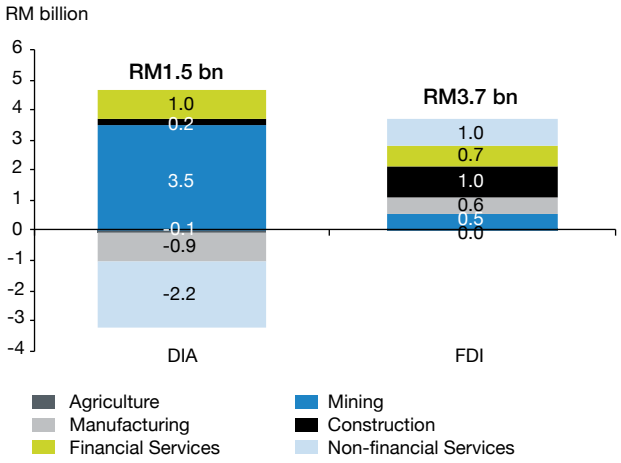
Chart 14: Current account balance




Source: Department of Statistics, Malaysia

### Net inflow in the direct investment account

Chart 15: Net Direct Investment Flows by Sector

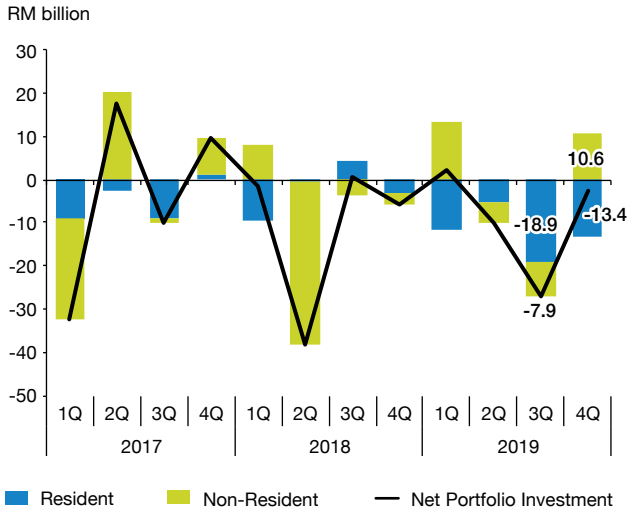



Note: For DIA, positive values refer to net outflows while negative values refer to net inflows. Figures may not add up due to rounding.

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

### Net outflow in portfolio investment account attributable to resident investors

Chart 16: Portfolio Investments




Source: Department of Statistics, Malaysia and Bank Negara Malaysia

## Financial account registered a smaller net outflow

The financial account registered a smaller net outflow of RM0.6 billion (3Q 2019: -RM1.3 billion), due to lower net outflow of portfolio investments amid net inflow in the direct investment account.

The direct investment account turned around to register a net inflow of RM2.2 billion (3Q 2019: net outflow of RM0.8 billion), reflecting higher foreign direct investment (FDI) and a smaller outflow of direct investment abroad (DIA). During the quarter, FDI registered a higher net inflow of RM3.7 billion (3Q 2019: +RM2.9 billion) and was channelled mainly into the construction and non-financial services sectors, particularly the wholesale and retail trade sub-sector. DIA by Malaysian companies registered a smaller net outflow of RM1.5 billion (3Q 2019: -RM3.7 billion). The outflows were mainly channelled into the mining and financial services sectors.

The portfolio investment account registered a smaller net outflow of RM2.8 billion (3Q 2019: -RM26.8 billion), following more moderate outflows from resident investors and a return of non-resident portfolio investments. Residents' portfolio investments abroad recorded a smaller net outflow (RM13.4 billion; 3Q 2019: -RM18.9 billion). Domestic institutional investors continued to purchase equity securities abroad, while liquidating some holdings of foreign debt securities. For non-residents, improved investor sentiments amid positive developments in trade negotiations led to a net inflow of RM10.6 billion into domestic debt securities (3Q 2019: -RM7.9 billion).

The other investment account recorded a marginal net inflow of RM0.6 billion (3Q 2019: RM25.3 billion). This reflected a drawdown of loans to the private sector, which were almost entirely offset by net interbank placements abroad by resident banks. Net errors and omissions amounted to -RM9.4 billion during the quarter, or -2.0% of total trade.

## Manageable external debt

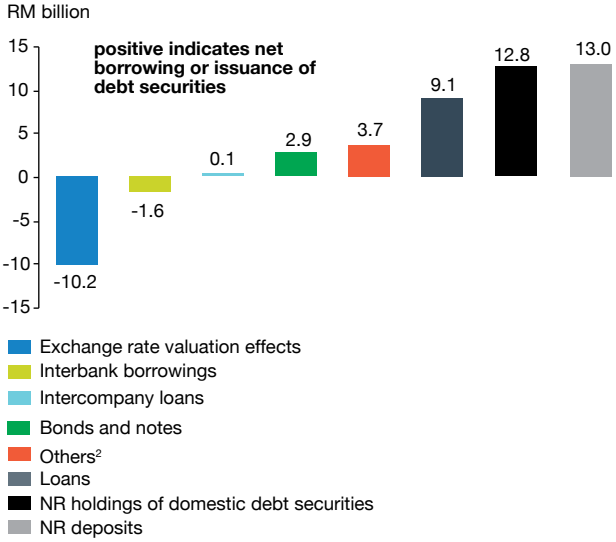
Malaysia's external debt increased to RM946.3 billion, or 62.6% of GDP as at end-December 2019 (end-September 2019: RM916.4 billion or 60.7% of GDP). The higher external debt reflects mainly the increase in non-resident (NR) deposits and purchases of Malaysian Government Securities, and higher external borrowings by resident corporations. This was partially offset by valuation effects following the stronger ringgit against selected major and regional foreign currencies during the period.

The country's external debt remains manageable, given its currency and maturity profiles. Close to one-third of external debt was denominated in ringgit (32.8%; end-September 2019: 32.0%), mainly in NR holdings of domestic debt securities (64.8% share of ringgit-denominated external debt) and NR ringgit deposits (17.9% share) in domestic banking institutions. These liabilities are not subject to valuation changes that may arise from fluctuations in the ringgit exchange rate.

The remaining external debt (RM635.9 billion or 67.2% of total external debt) was denominated in foreign currency (FCY). The corporate sector accounted for close to half of FCY-denominated external debt and are largely subject to prudential and hedging requirements so that such borrowings do not pose a material macroeconomic risk. Long-term bonds and notes issued offshore, accounting for 24.5% of total FCY-denominated external debt, stood at RM155.5 billion as at end-December 2019. These were mainly by non-financial corporations and channelled primarily to finance asset acquisitions abroad. Intercompany loans, amounting to RM89.8 billion or 14.1% of FCY-denominated external debt, are typically on flexible and concessionary terms.

### Higher external debt in 4Q 2019

Chart 17: Changes in External Debt
Net change[1]: +RM29.9 billion

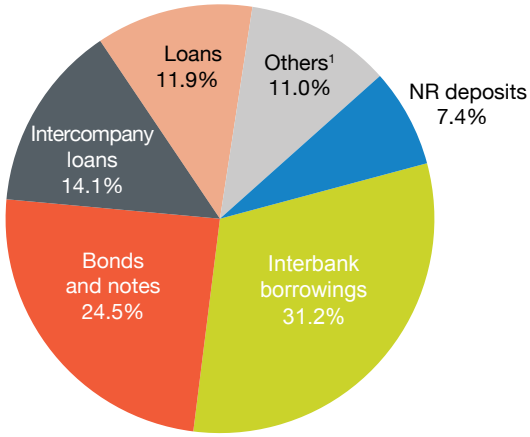



[1] Changes in individual debt instruments exclude exchange rate valuation effects
[2] Comprises trade credits, IMF allocation of SDRs and other debt liabilities
Note: NR refers to non-residents
Figures may not add up due to rounding

Source: Ministry of Finance, Malaysia and Bank Negara Malaysia

### FCY-denominated debt subject to prudent liquidity management practices and hedging requirements

Chart 18: Breakdown of Foreign Currency-Denominated External Debt (% share)




[1]Includes trade credits and miscellaneous, such as insurance claims yet to be disbursed and interest payables on bonds and notes

Source: Ministry of Finance, Malaysia and Bank Negara Malaysia

Interbank borrowings and FCY deposits in the domestic banking system accounted for 38.6% (or RM245.3 billion) of FCY-denominated external debt. About three quarters of the interbank borrowings were in the form of largely stable intragroup borrowings, including from parent banks, regional offices and subsidiaries. This reflects banks' centralised liquidity and funding management practices. Foreign-currency risk, measured in terms of the net open position of FCY-denominated exposures[2], remained low at 4.4% of banks' total capital.

From a maturity perspective, 58.6% of the total external debt was skewed to medium- to long-term tenure (end-September 2019: 57.0%), suggesting limited rollover risks. Short-term external debt accounted for the remaining 41.4% of external debt. Close to half of the short-term external debt were intragroup borrowings among banks and corporations, which are generally stable and on concessionary terms, while another 12.2% were accounted by trade credits, largely backed by export earnings. As at 31 January 2020, international reserves stood at USD104.2 billion, sufficient to finance 7.5 months of retained imports, and is 1.1 times the short-term external debt.

[2] Refers to the aggregated sum of the net short or long foreign currency positions for all currencies across banks.

# Monetary and Financial Developments

## HIGHLIGHTS

- The ringgit appreciated amidst a resumption in non-resident portfolio inflows following positive global developments.
- The recovery in investor sentiments led to improved performance of domestic bond and equity markets.

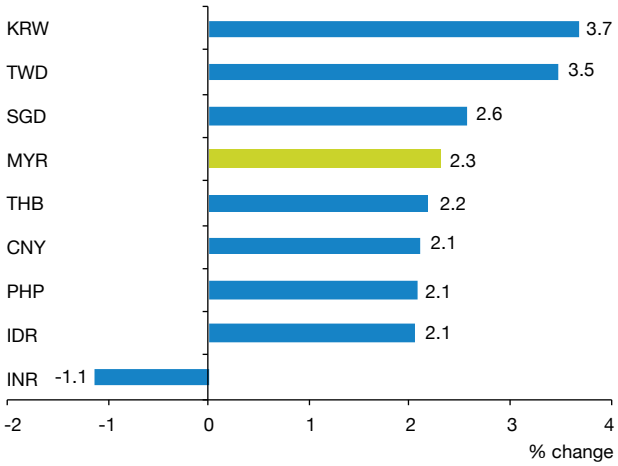
### The performance of domestic financial markets improved during the fourth quarter

Conditions in domestic financial markets improved during the quarter contributed mainly by the resumption in non-resident portfolio inflows. This was largely driven by positive developments in global trade negotiations and global monetary policy easing, which led to improved investor sentiments.

While domestic financial markets were affected by intermittent periods of uncertainty on trade tensions during the quarter, investor sentiments were lifted following the announcement of a Phase One trade deal between the US and PR China in December, which was signed on 15 January 2020. Synchronised policy rate cuts by several major central banks during the quarter, including the US, also contributed to the improvement in global investor risk appetite.

Ringgit appreciated against the US dollar in line with most regional currencies

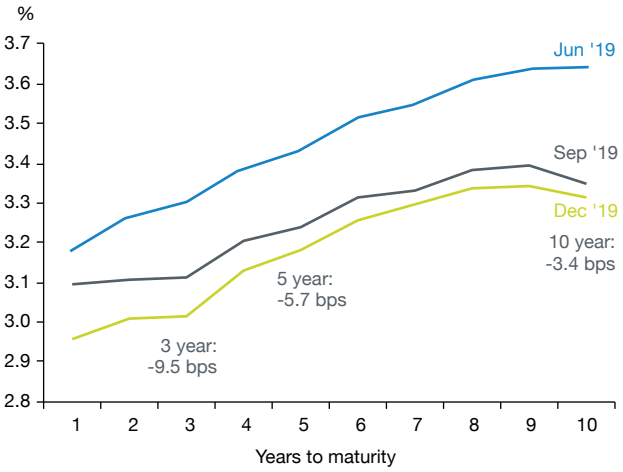
Chart 19: Performance of Regional Currencies Against the US Dollar (1 October - 31 December 2019)




Source: Bank Negara Malaysia

### MGS yield curve shifted downwards driven by non-resident portfolio inflows

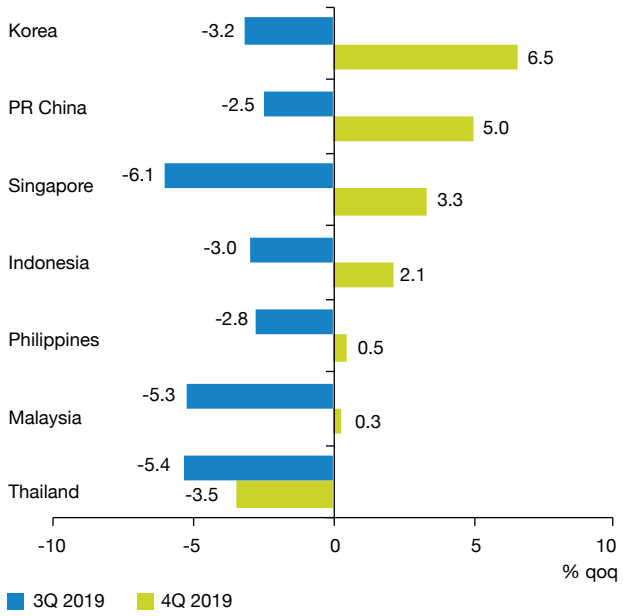
Chart 20: Trend in MGS Yields




Source: Bank Negara Malaysia

### Domestic equity market performance improved in line with regional trend

Chart 21: Performance of Regional Equity Markets




Source: Bloomberg

This confluence of risk-on sentiments and lower global interest rates contributed to portfolio inflows to the domestic bond market. As a result, the 3-year, 5-year, and 10-year MGS yields declined by 9.5, 5.7 and 3.4 basis points, respectively.

The domestic equity market also benefitted from the improved investor risk appetite, with the KLCI increasing by 0.3% to close at 1,589 points as at end-December (end-September: 1,584 points).

Consequently, the ringgit also appreciated by 2.3% against the US dollar during the quarter, in line with most regional currencies.

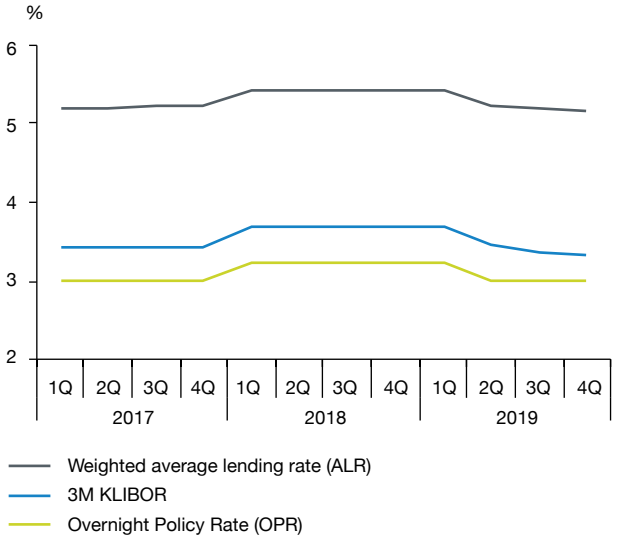
## Interest rates remained stable during the quarter

Nominal interbank interest rates were broadly stable in the fourth quarter. The 3-month KLIBOR, however, declined slightly after the announcement of the reduction in the Statutory Reserve Requirement (SRR) ratio in November 2019 and ended the quarter at 3.35% (3Q 2019: 3.38%). In addition, retail lending rates remained stable, with the weighted average base rate (BR) and the weighted average lending rate (ALR) on outstanding loans at 3.68% (3Q 2019: 3.68%) and 5.16% (3Q 2019: 5.18%), respectively.

Real fixed deposit (FD) rates increased in the fourth quarter amid lower headline inflation. In particular, the real 3-month and 12-month FD rates increased to 1.90% (3Q 2019: 1.75%) and 2.09% (3Q 2019: 1.99%), respectively.

**Broadly stable interest rates in the interbank and retail markets**

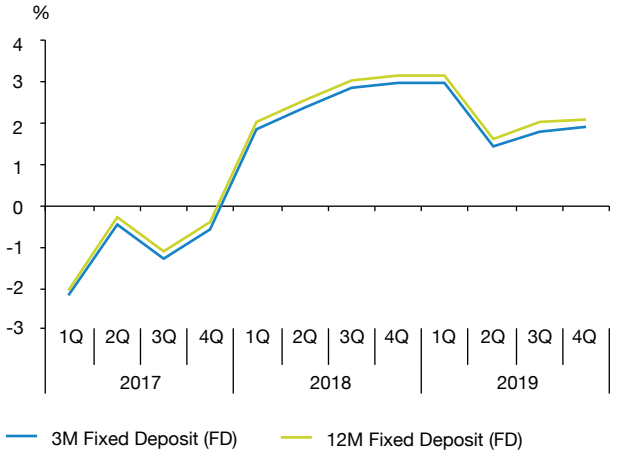
Chart 22: Policy, Interbank and Lending Rates (at end-period)




Source: Bank Negara Malaysia and Bloomberg

**Real deposit rates increased, reflecting lower inflation during the quarter**

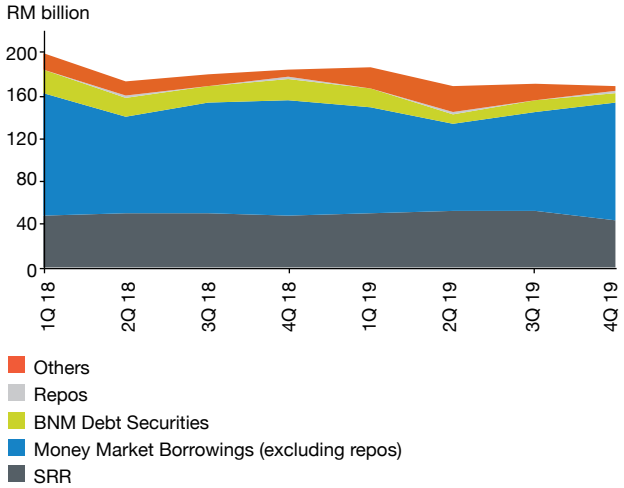
Chart 23: Real Fixed Deposit Rates by Maturity (at end-period)




Source: Bank Negara Malaysia

**Outstanding surplus ringgit liquidity placed with the Bank remained stable**

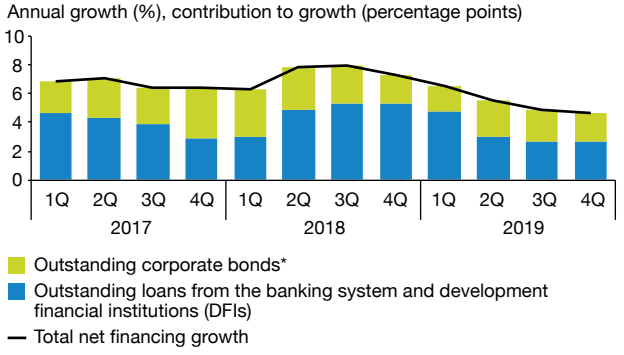
Chart 24: Outstanding Ringgit Liquidity Placed with Bank Negara Malaysia (at end-period)




Source: Bank Negara Malaysia

**Sustained expansion of net financing, supported by sustained growth in loans**

Chart 25: Contribution to Net Financing Growth




* Excludes issuances by Cagamas and non-residents

Source: Bank Negara Malaysia

## Banking system liquidity remained sufficient to facilitate financial intermediation

The level of surplus liquidity placed with the Bank remained relatively stable, reflecting the marginal net inflows during the quarter. At the institutional level, most banks continued to maintain surplus liquidity positions with the Bank.

The reduction in the SRR ratio has led to higher liquidity available to banks, providing greater flexibility for banks in their liquidity management. This was reflected in the higher level of money market placements with the Bank by the end of the fourth quarter.

## Sustained expansion of net financing

In the fourth quarter, net financing expanded by 4.7% on an annual basis (3Q 2019: 4.8%), supported by sustained growth in outstanding loans[3] (3Q 2019: 3.5%, 4Q 2019: 3.5%). Nonetheless, growth in outstanding corporate bonds[4] moderated slightly to 8.0% during the quarter (3Q 2019: 9.0%) amid higher redemptions. Corporate bond issuances, however, were higher across most sectors. Growth in outstanding business loans improved to 2.4% (3Q 2019: 1.6%), driven by higher loan growth in the manufacturing sector and improvements across most sectors. For the household segment, growth in outstanding loans was stable at 4.7% during the same period (3Q 2019: 4.6%), with higher loans disbursed for purchase of residential property, credit card and personal use. Demand for both business and household loans, as indicated by loan applications[5], was broadly stable.

[3] Loans from the banking system and development financial institutions (DFIs).
[4] Excludes issuances by Cagamas and non-residents.
[5] Loan applications in the banking system only.

# The Bank's Policy Considerations

## HIGHLIGHTS

- **The MPC reduced the Overnight Policy Rate by 25 basis points to 2.75% at the January 2020 MPC meeting. The adjustment was a pre-emptive measure to sustain growth amid price stability.**

### The OPR remained accommodative

The Monetary Policy Committee (MPC) maintained the Overnight Policy Rate (OPR) at 3.00% at the November 2019 meeting. More recently, at the January 2020 MPC meeting, the MPC reduced the OPR by 25 basis points to 2.75%. The ceiling and floor rates of the corridor for the OPR were correspondingly reduced to 3.00% and 2.50%, respectively. The adjustment to the OPR was a pre-emptive measure to sustain growth amid price stability.

In the MPC's assessment, the global economy was expected to continue expanding at a moderate pace. Latest indicators and the recent dissipation of trade tensions pointed to improving global trade activity. Monetary easing across major economies in the second half of 2019 helped ease financial conditions, and was expected to continue to support economic activity. However, downside risks remained due to geopolitical tensions and policy uncertainties in a number of countries. This could cause a resurgence of financial market volatility and weigh on the global growth outlook.

Growth of the Malaysian economy in 2020 was expected by the MPC to continue to be supported by private sector spending. However, downside risks to growth remained. These included uncertainty from various trade negotiations, geopolitical risks, weaker-than-expected growth of major trade partners, heightened volatility in financial markets, and domestic factors that included weakness in the commodities sector and delays in the implementation of projects.

The MPC assessed that headline inflation in 2020 was expected to average higher but remain modest. The trajectory of headline inflation would be dependent on global oil and commodity price developments and the timing of the lifting of the domestic retail fuel price ceilings. Underlying inflation was expected to remain broadly stable, reflecting the continued expansion in economic activity and the absence of strong demand pressures.

The impact of the coronavirus outbreak on economic performance would depend on its severity and duration and is an evolving development that requires continuous monitoring.

**Other policy highlights in the fourth quarter of 2019**

| Policy highlights | Salient requirements |
|---|---|
| **Electronic Know-Your-Customer (e-KYC) – Exposure Draft (ED)** | • The ED was issued on 16 December 2019, setting out the proposed requirements in implementing e-KYC for onboarding of customers.<br>• The proposed requirements aim to promote-<br>o Safe and secure on-boarding of customers digitally;<br>o Lower on-boarding costs for both users and providers; and<br>o Greater innovation and complete end-to-end offering of digital financial services for consumers.<br>• The final policy document is expected to be issued in 2020. |
| **Fair Treatment of Financial Consumers – Policy Document (PD)** | • The PD was issued on 6 November 2019 to promote fair dealing and professional conduct amongst financial service providers (FSPs).<br>• The PD stipulates expectations on financial institutions to treat their customers fairly by ensuring, amongst others, that they-<br>o are not subject to unfair contract terms;<br>o are provided with clear, relevant and timely information, and suitable advice to facilitate decision-making; and<br>o have their complaints and claims handled in a prompt, fair and effective manner.<br>• The PD will come into force on 6 May 2020, except for the requirements on fair contract terms, which will take effect from 6 November 2020. |
| **Licensing Framework for Digital Banks – Exposure Draft (ED)** | • The ED was issued on 27 December 2019 for public consultation until end-February 2020.<br>• The ED aims to enable admission of digital banks that are able to contribute to economic development by addressing market gaps in unserved and underserved segments.<br>• Digital banks will be required to operate in a managed environment in their first three to five years of operations, functioning as a "foundational phase" for them to demonstrate sound and viable operations, and for the Bank to observe performance and attendant risks. During this phase, digital banks will be subject to-<br>o a minimum capital funds requirement of RM100 million unimpaired by losses;<br>o an asset threshold of RM2 billion; and<br>o simplified capital, liquidity, stress test and public disclosure requirements. |
| **Responsibility Mapping – Exposure Draft (ED)** | • The ED was issued on 27 December 2019, setting out the Bank's proposals to clarify the roles, responsibilities and accountability of individuals holding leadership positions in financial institutions.<br>• The ED aims to–<br>o ensure responsibilities for key functions of a financial institution are allocated to individuals at an appropriate senior level within the financial institution;<br>o clarify and strengthen the accountability of individuals to whom key responsibilities are allocated; and<br>o encourage a financial institution to carefully consider whether the allocation of responsibilities to individuals within senior management is compatible with effective risk management practices, taking into account the size, scale and complexity of the financial institution's operations. |
| **Valuation of Insurance and Takaful Liabilities – Exposure Draft (ED)** | • The ED was issued for public consultation on 24 December 2019, setting out proposed enhancements to the requirements on valuation of insurance and takaful liabilities.<br>• The ED, which is one of the building blocks of the solvency framework, aims to ensure that the measurement of insurance and takaful liabilities accurately reflects the underlying cash flow obligations of the insurance and takaful contracts, and is consistent and comparable across different types of products and licensed persons. |

# Macroeconomic Outlook

## HIGHLIGHTS

- Global economic activity to register a marginal improvement in 2020.
- The Malaysian economy will remain supported by private sector activity in 2020.
- Headline inflation in 2020 is projected to average higher but remain modest.

### Global growth to register a mild improvement in 2020

After its weakest performance since the Global Financial Crisis at 2.9% in 2019, global growth is expected to improve marginally in 2020. Trade activity will be supported by the Phase One agreement between the US and PR China.

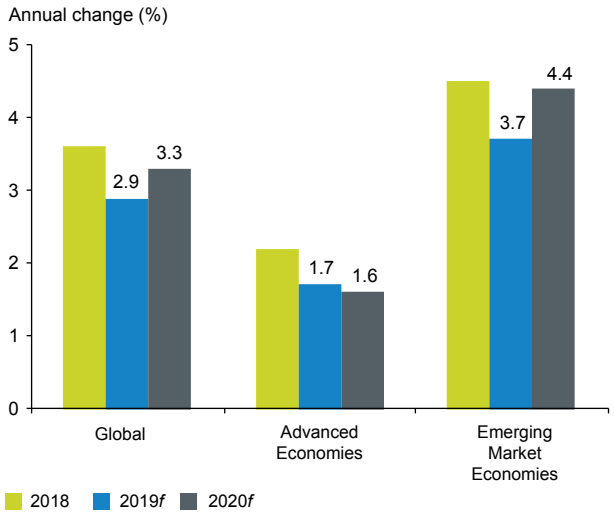
Growth in the advanced economies is projected to be stagnant. The US economy is expected to moderate as labour market conditions soften, with continued weakness in investment and production activity. In the euro area, recovery from previous disruptions in the manufacturing sector will support growth prospects.

PR China and the regional economies are expected to benefit from an improved trade outlook from the Phase One agreement. However, near-term growth prospects will be weighed by the ongoing coronavirus outbreak. Domestic and international travel restrictions, as well as an extension to the Lunar New Year holiday for many businesses in the manufacturing sector, will suppress private sector activity, particularly in the first quarter of the year.

On balance, risks to the global outlook are tilted to the downside, emanating mainly from geopolitical risks, a re-escalation of lingering trade tensions and the severity and duration of the coronavirus outbreak. Such episodes could also cause a resurgence of financial market volatility and further weigh on global growth prospects.

**Global growth to marginally improve in 2020**

Chart 26: GDP Growth




*f* Forecast

Source: IMF World Economic Outlook (January 2020)

## The Malaysian economy is expected to remain supported by private sector activity in 2020

The Malaysian economy expanded by 4.3% in 2019. Going into 2020, growth, particularly in the first quarter of the year, will be affected by the coronavirus outbreak. The impact will be felt largely in tourism-related sectors, and to a certain extent, in the manufacturing sector through disruptions within the global supply chain and the expected slowdown in PR China. The overall impact on the Malaysian economy will, however, depend on the duration and spread of the outbreak as well as policy responses by authorities.

For the year as a whole, growth will be supported by household spending, underpinned by continued income and employment growth amid modest price pressures. Investment is projected to record a modest recovery, supported by the realisation of approved private investment projects in recent periods, and higher public sector capital spending, particularly in the transport-related segment. Meanwhile, the external sector is expected to benefit from the gradual recovery in global growth and trade.

The growth momentum is subject to high near-term downside risks. The most significant would be the prolonged impact of the coronavirus. In addition, uncertainties remain in global economic and financial conditions. On the domestic front, risks emanate mainly from weakness in the commodities sector and delays in projects implementation.

## Headline inflation is expected to be higher but remain modest in 2020

The annual average headline inflation is projected to be higher but remain modest in 2020. The trajectory of headline inflation will be dependent on global oil and commodity price developments and the timing of the lifting of the domestic retail fuel price ceilings.

Underlying inflation is expected to be broadly stable, reflecting the continued expansion in economic activity and the absence of strong demand pressures.