MANAGING RISKS TO FINANCIAL STABILITY

Financial stability continued to be preserved

Financial stability was maintained throughout the first quarter of the year. This was underpinned by sound financial institutions and orderly financial market conditions. The continued effective functioning of financial intermediation has provided a supportive environment for economic activity. Confidence in the financial system was also preserved.

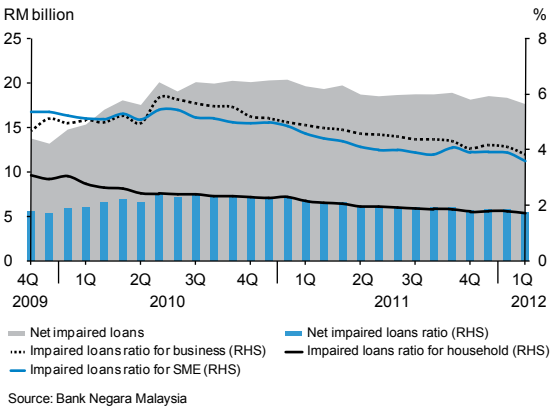
The overall quality of credit exposures of the financial sector remained manageable, further supported by the sound economic fundamentals. Both impaired loans and loans-in-arrears (for duration of one to less than three months) improved in terms of value and ratio. As at end-March 2012, loan impairment and loans-in-arrears ratios were at 1.7% of net loans (4Q 11: 1.8%), or 3.5% of gross loans (4Q 11: 3.6%) respectively. Credit risk exposures of the insurance industry, emanating mainly from holdings of private debt securities, were similarly maintained at a manageable level with exposures at 3.4% of insurers' total capital (4Q 11: 3.2% of total capital).

Growth in household indebtedness continued to moderate to 0.4% during the quarter (4Q 11: 3.2%). Financing for the purchase of residential properties grew by 3.4% (4Q 11: 3.2%), whilst outstanding credit card balances declined during the quarter. The household sector continued to exhibit the ability to meet its debt obligations, with the overall impaired loans ratio for the household sector improving marginally to 1.7% during the quarter (4Q 11: 1.8%).

Credit extended to businesses expanded by 0.9% during the quarter, with broad-based expansion in financing across business sectors. Credit risk for this portfolio remained manageable with the risk of delinquency, as measured by the expected default frequency, improving further to 0.53% (4Q 11: 0.68%), supported by the sustained debt servicing capacity of businesses. During the quarter, the level of loan impairment for the business segment improved to 3.8% of gross business loans (4Q 11: 4.1%).

The overall level of global financial market volatility improved during the first quarter as significant actions taken by the European policymakers led to some improvement in global market sentiments. On the domestic front, the financial markets remained orderly and exhibited ample capacity to intermediate the portfolio flows. Trading liquidity in the debt and equity markets remained intact, as reflected in higher turnover ratios and relatively stable bid-ask spreads. Interest rate risk exposures remained stable at 4.9% of capital base for the banking system while that of the insurance sector accounted for 3.1% of capital base (4Q 11: 3.8%). The banking system exposures to equity risk remained well-contained at 0.9% of capital base (4Q 11: 0.9%), while exposures of insurers increased slightly to 7.0% (4Q 11: 6.8%) of capital base following higher investments in equity amounting to RM31.3 billion (4Q 11: RM29 billion).

Banking System: Asset quality

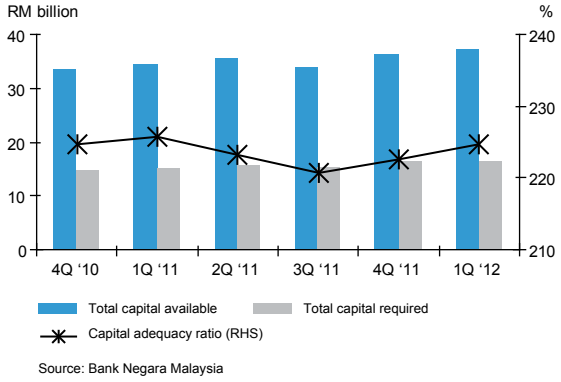


Source: Bank Negara Malaysia

The financial sector remained resilient

The financial sector continued to be well-capitalised with strong financial buffers to withstand potential losses from possible adverse financial and economic conditions. Core capital ratio and risk-weighted capital ratio of the banking system remained firm at 13.0% (4Q 11: 13.6%) and 14.7% (4Q 11: 15.6%) respectively. Approximately 88.7% of total capital is made up of high quality Tier-1 capital, comprising paid-up capital and reserves. Capital in excess of the minimum 8% regulatory requirement remained high at RM71.6 billion. Similarly, the insurance sector also maintained a sound capital adequacy ratio of 224.8% (4Q 11: 222.5%) and excess capital buffer of RM20.8 billion.

Insurance Sector: Capitalisation

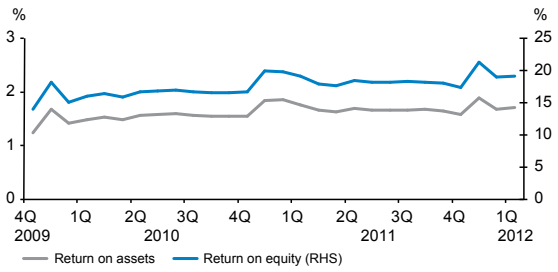


Source: Bank Negara Malaysia

The banking system recorded pre-tax profit totalling RM7.7 billion for the quarter (4Q 11: RM5.9 billion), attributable mainly to the higher income from financing activities and fee-based income, which partly offset the increase in overhead costs. Returns on assets and equity were 1.7% (4Q 11: 1.6%) and 19.1% (4Q 11: 17.4%) respectively.

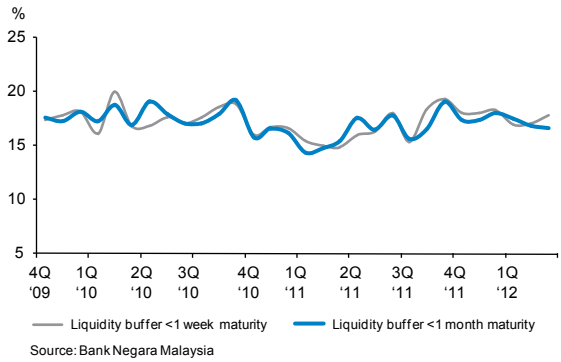
The life insurance and family takaful businesses recorded an excess of income over outgo of RM4 billion (4Q 11: RM4.3 billion). The lower amount of net premiums for ordinary life and investment-linked products was partly offset by higher capital gains arising from improved financial market conditions. The general insurers and general takaful operators registered a higher level of underwriting and operating profit totalling RM317.9 million and RM653 million respectively (4Q 11: underwriting loss of RM242 million and operating profit of RM143.2 million, respectively) following moderation in claims. The claims ratio for the Motor 'Act' cover (mandatory insurance cover required under the Road Transport Act 1987) improved to 182.7% (4Q 11: 321.4%).

Banking System: Profitability



Source: Bank Negara Malaysia

Banking System: Liquidity Buffer to Total Deposit Ratio



Source: Bank Negara Malaysia

Banking sector resilience was further reinforced by the sustained availability of ample liquidity to meet demands for deposit withdrawals and other liquidity obligations. Liquidity buffer accounted for 18% of total deposits for liquidity needs maturing within one month. The foreign currency liquidity mismatch of banks remained manageable, recording a small negative position in the less than one month bucket of RM11.5 billion, in tandem with some easing in on-shore USD liquidity.

Insurance and Takaful Sectors: Indicators

	2011			2012	2011			2012
	1Q	4Q	Year	1Q	1Q	4Q	Year	1Q
	RM million				Annual Change (%)			
Life insurance & family takaful								
Excess of income over outgo	3,238.5	4,342.9	12,662.2	3,964.2	11.4	37.8	-9.4	22.4
General insurance & general takaful								
Operating profit	553.9	143.2	1,776.9	653.0	5.6	-74.6	-20.9	17.9
Claims ratio (%)	61.5	66.7	66.7	60.5	-1.3	4.6	4.6	-1.0

Source: Bank Negara Malaysia