**Financial Markets Committee (FMC) Meeting**
**13 April 2023**
**Bank Negara Malaysia**


## Summary

The meeting discussed recent financial market developments and reviewed progress updates and proposals on development initiatives, including those by the Bond Market Subcommittee and Islamic Financial Market Subcommittee.


## 1 Market developments and outlook

1.1 The meeting discussed the impact of rapid monetary policy tightening in advanced economies over the past year and the recent US and Swiss banking crises. Domestic financial market volatility has subsided from a peak near the end of 2022 in line with a slowdown in tightening while the banking crises have not had a significant impact on the domestic market, with confidence in Malaysian banks remaining high given healthy levels of capital and ample liquidity buffers.

1.2 On the Additional Tier 1 (AT1) bond market, the meeting noted that the domestic reaction to the Credit Suisse wipeout was not immediately apparent given minimal trading post incident, though a drastic impact on prices was not expected. Members also highlighted that the elevated Kuala Lumpur Interbank Offered Rate (KLIBOR) has been driven by various factors, including rates competition and focus on regulatory ratios, though pressures have recently gradually receded.

1.3 The meeting discussed the overall status of the onshore financial market and affirmed the healthy growth and accessibility of the FX market. Additional efforts are required to develop onshore bond market liquidity commensurate with the growing size of the market and overcome structural challenges such as a sizeable institutional investor base with buy and hold strategies.

1.4 Although a repeat of 2022's volatility is not expected, the meeting acknowledged that several downside risks to the outlook remain, including renewed inflationary pressures from energy price volatility and geopolitical tensions, as well as a significant increase in global financial market volatility and tightening of financial conditions.

## 2 Bond Market Subcommittee

2.1 The meeting was briefed on the growing size of the bond market over the years as evidenced by rising daily average trading volume, including repo and short-selling transactions. Regionally, Malaysia's bond market position remains

strong and continues to be among the largest markets by absolute size and as a percentage of GDP with robust interest from non-resident investors (YTD foreign net inflows: RM11.4 bil). The meeting discussed matters surrounding the bond market and deliberated on efforts to further deepen the market, including improving the overall bond turnover ratio and tightening bid-offer spreads.

2.2 The meeting discussed plans to further improve efficiency and liquidity by promoting greater use of collateralized transactions and securities borrowing and lending (SBL) to a wider base of market players such as insurance companies and assets managers. The meeting also supported efforts to promote standardisation through the issuance and adoption of recommended market conventions in the repo market.

2.3 Members were updated on the Bond Market Subcommittee's deliberations on Electronic Trading Platforms (ETPs). The Subcommittee proposed for the use of an ETP for the trading of government bonds among Principal Dealers (PDs) to be considered to improve bond market liquidity and enhance price transparency on a real-time basis. The meeting also endorsed the formation of a PD Working Group (PDWG) as a platform to discuss PD-related matters, which includes identifying the appropriate inter-PD ETP, deepening the PDs' core market-making capacity, assessing the current state of the MGS futures market and driving repo market development initiatives.

## 3 Islamic Financial Market Subcommittee

3.1 Islamic Financial Market Subcommittee (IFMC) updated on the progress of the Islamic Financial Market Report which aims to highlight the current state of the Malaysian Islamic financial market, challenges, prevailing gaps and the way forward for further development and progress. Members noted that a preliminary report was prepared by the IFMC and shared during the roundtable discussion at Global Islamic Finance Forum (GIFF) 2022 where the report was then further refined taking into consideration valuable feedback from the roundtable participants and committee members. FMC members agreed on the endorsement of the Islamic Financial Market Report and its publication on BNM's website.

3.2 Members discussed future areas of development for the Islamic market with reference to the potential development areas identified and highlighted in the report such as:

a. Sustainability-linked Treasury products
b. Increase non-residents' participation in the sukuk market

c. New intermediaries to provide liquidity or market making for sukuk i.e. non-bank dealers
d. Market making or trading of regional sukuk securities

3.3 Members were updated on Islamic development initiatives including:
a. Feasibility study on anticipatory hedging to increase usage of Islamic derivatives and hedging instruments, including a proposal to arrange for a consultation with the members of the Shariah Advisory Council (SAC)
b. Development of Islamic repo market via multiple initiatives which would provide better visibility and price discovery for improved trading volume
c. Availability of ESG debt securities data as proposed by market participants during GIFF to improve transparency and support informed decision-making

## 4 Updates on Local Currency Settlement Framework (LCSF)

4.1 The meeting was updated on the progress of local currency (LCY) settlement initiatives with China, Thailand and Indonesia. The renminbi initiatives between China and Malaysia saw the share of RMB settlement with China increasing from 6.4% in 2013 to 17.2% in 2022. Similar positive growth was also observed in the share of trade and direct investment LCY settlement with Thailand (2022: 16.1%) and Indonesia (2022: 16.6%) especially since the establishment of LCSF.

4.2 Members highlighted that the special non-resident account flexibility offered via LCSF provided an added advantage to LCY settlement in addition to other existing flexibilities that are already being offered via the Appointed Overseas Office (AOO) channel. Members also discussed strategies to improve the LCSF which includes simplifying the LCSF reporting requirement process through system enhancements.

## 5 Updates on Malaysia Overnight Rate (MYOR) and KLIBOR

5.1 The meeting was updated on the conclusion of KLIBOR review in 2H 2022. Malaysia remains on a multiple-rate approach with KLIBOR co-existing alongside MYOR, allowing market participants to choose the rate that best suits their needs.

5.2 Members acknowledged the incremental progress to support trading of MYOR derivatives, including the recent inclusion of MYOR in the ISDA Interest Rate Derivatives Definitions and the Financial Market Association Malaysia (FMAM)'s circulation of recommended conventions for three types of MYOR derivatives (MYOR IRS, MYOR-KLIBOR basis and SOFR-MYOR currency basis). Members noted the issuance of the first floating-rate bond priced

against MYOR by Cagamas in July 2022 and discussed potential areas for further MYOR development, including MYOR-based money market products.