ECONOMIC AND FINANCIAL DEVELOPMENTS IN MALAYSIA IN THE FOURTH QUARTER OF 2016

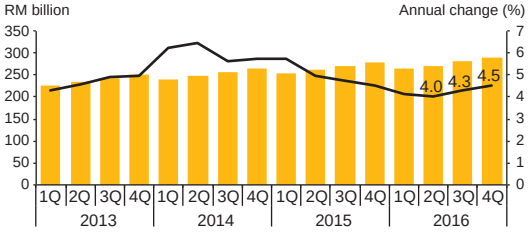
OVERVIEW

Global economic activity continued to expand in the fourth quarter of 2016. The advanced economies experienced divergent growth trends, in part, driven by differences in the strength of private consumption amid cyclical and structural weaknesses. In Asia, economic activity was supported mainly by domestic demand. Of importance, the external sector provided a small lift to growth in several economies, following consecutive quarters of negative growth. Financial market volatility increased due to concerns over major issues in the advanced economies, such as policy and political uncertainties following the outcome of the presidential election in the US and the UK's vote to exit the EU. Overall, global monetary conditions remained very accommodative, against a backdrop of continued growth concerns with rising, but still low inflation.

The Malaysian economy expanded by 4.5% in the fourth quarter of 2016

The Malaysian economy grew by 4.5% in the fourth quarter of 2016 (3Q 2016: 4.3%), underpinned by continued expansion in private sector expenditure. On the supply side, growth continues to be driven by the manufacturing and services sectors. On a quarter-on-quarter seasonally-adjusted basis, the economy recorded a sustained growth of 1.4% (3Q 2016: 1.4%).

The Economy Expanded by 4.5% in the Fourth Quarter (at constant 2010 prices)



Source: Department of Statistics, Malaysia

Overall, domestic demand expanded at a more moderate pace, as the sustained growth in private sector expenditure was partly offset by the decline in public expenditure. In the fourth quarter, private consumption grew by 6.2% (3Q 2016: 6.4%), supported by continued wage and employment growth. Private investment registered a growth of 4.9% (3Q 2016: 4.7%), following continued capital spending in the services and manufacturing sectors. Growth of public investment improved mainly on account of higher spending on fixed assets by public corporations, but nevertheless, remained in contraction during the quarter. Public consumption also declined by 4.2% (3Q 2016: +2.2%) arising from the rationalisation of spending on supplies and services and a moderation in the growth of spending on emoluments. On the external front, net exports contributed positively to growth as real exports expanded at a faster rate than real imports.

On the supply side, growth in the manufacturing, mining and agriculture sectors improved. The manufacturing sector expanded at a faster pace owing to higher growth in both domestic and export-oriented industries. The mining sector recorded an improvement due to the increase of natural gas production during the quarter. In the agriculture sector, economic activity contracted at a slower pace, reflecting the diminishing impact of El Niño on crude palm oil yields. Growth in the services sector continued to expand, albeit at a more moderate pace, supported mainly by consumption-related services. In the construction sector, growth remained driven by the civil engineering sub-sector.

Inflation, as measured by the annual change in the Consumer Price Index (CPI), increased to 1.7% in the fourth quarter of 2016 (3Q 2016: 1.3%), driven mainly by upward adjustments to domestic fuel prices during the quarter. Inflation in the *transport* category registered a smaller negative inflation of 2.6% during the quarter

(3Q 2016: -7.4%). The inflationary impact was, however, mitigated by the lower inflation in the *alcoholic beverages and tobacco* category (6.6%; 3Q 2016: 19.7%) due to the lapse in the impact of the upward revision in cigarette prices in the base period of 4Q 2015. For the year as a whole, inflation averaged 2.1% (2015: 2.1%).

In 4Q 2016, the current account surplus widened, due mainly to a higher trade surplus and narrower deficits in the income accounts.

As at 31 January 2017, the reserves position amounted to USD95.0 billion (equivalent to RM426.0 billion). The international reserves remain ample to facilitate international transactions. They are sufficient to finance 8.6 months of retained imports, significantly higher than the 3-month international threshold. The reserves level is also adequate to meet external obligations given the reserves to short-term external debt coverage of 1.1 times. It is important to note that not all short-term external debt creates a claim on reserves given the availability of external assets and export earnings of borrowers.

Monetary conditions remain supportive of economic activity, with continued growth in financing to the private sector

The Monetary Policy Committee (MPC) maintained the Overnight Policy Rate (OPR) at 3.00% during the fourth quarter of 2016. At the prevailing level of the OPR, monetary conditions remained supportive of economic activity. Reflecting the unchanged OPR, interbank rates and the 3-month KLIBOR were relatively stable during the quarter. Correspondingly, retail lending rates were also stable. The weighted average base rate (BR) of commercial banks remained unchanged at 3.61% while the weighted average lending rate (ALR) on outstanding loans declined by five basis points from end-September to end-December.

M3, or broad money, increased by RM25.0 billion on a quarter-on-quarter basis to record an annual growth rate of 3% as at end-December (end-September: 2.2%). The increase in M3 during the quarter was driven mainly by the continued expansion of credit extended to the private sector by the banking system.

Total gross financing raised by the private sector through the banking system, development financial institutions (DFIs), and the capital market amounted to RM316.2 billion (3Q 2016: RM293.8 billion). On a net basis, the growth of loans extended by the banking system and DFIs, and the outstanding issuances of corporate bonds, moderated to 5.5% in 4Q 2016 (3Q 2016: 6.5%) due mainly to the lower growth in outstanding corporate bonds. On an annual basis, outstanding business loans extended by the banking system and DFIs grew by 4.8% in the fourth quarter (3Q 2016: 2.0%). The growth of outstanding household loans of the banking system and DFIs moderated to 5.5% in 4Q 2016 (3Q 2016: 5.8%), reflecting mainly the moderation in outstanding loans for the purchase of passenger cars and the *purchase of residential property*. Net funds raised in the capital market moderated to RM2.1 billion in the fourth quarter of 2016 (3Q 2016: RM13.5 billion). The decline was due mainly to lower net funds raised by the private sector.

The ringgit and all major and regional currencies depreciated against the US dollar during the quarter. The depreciation was driven mainly by portfolio investment outflows from emerging economies amid uncertainties arising from the outcome of the US Presidential Elections. Expectations of an interest rate increase, the actual increase in the US Federal Reserve's policy rate in December 2016, and the anticipation of a faster pace of US interest rate normalisation in 2017, exacerbated portfolio outflows and exerted further downward pressure on most major and regional currencies. The ringgit also faced additional adjustments during the quarter following speculative activity in the non-deliverable forward (NDF) market. The ringgit, along with regional currencies, however, began to stabilise towards the end of the quarter amidst higher stability in the global financial markets. The implementation of measures to develop, deepen, and address the rising imbalances in the domestic foreign exchange market, and the firmer global crude oil prices also lent stability to the domestic foreign exchange market towards the end of the quarter.

Overall, the ringgit depreciated by 7.6% against the US dollar during the quarter. The ringgit also depreciated against the euro (-1.6%), the pound sterling (-2.4%) and the Australian dollar (-2.5%), but appreciated against the Japanese yen (6.3%). The ringgit also depreciated against all regional currencies, with the exception of the Korean won, by between 2.1% and 5.6%.

Domestic financial system remains resilient

The Malaysian financial system remains resilient despite global uncertainties over policy adjustments in the major economies. The domestic banking system remains well-capitalised, with ample liquidity to support the financing needs of businesses and households. As businesses and households continue to adjust to the challenging economic outlook and higher cost of living, these financial buffers will support the resilience of the financial institutions. Going forward, external events will continue to weigh heavily on the volatility in domestic financial markets. These include increased uncertainty over political developments and growth in the major economies as well as volatile commodity prices. Domestic financial system stability is nonetheless expected to be preserved given the loss absorption capacity of financial institutions supported by strong capital and liquidity buffers.

Financial institutions remained well-capitalised. The combined capital buffers of banks, insurers and takaful operators stood at RM172.5 billion. Banks maintained a high level and quality of capitalisation. This is reflected in the high common equity tier-1, tier-1 and total capital ratios of banks which stood at 13.1%, 14.0% and 16.5%, respectively (3Q 2016: 13.3%, 14.2% and 16.7%, respectively). Similarly, the capital adequacy ratio for the insurance and takaful sectors remained high at 243.8% (3Q 2016: 226.3%).

Domestic demand will remain the key driver of growth

Going forward, the global economy is expected to improve but remain on a moderate growth path. While there are indications of more sustained growth in the major economies in 2017, downside risks to global growth continue to prevail, arising from the volatility in commodity prices, policy uncertainties and growth prospects of the major developed economies, heightened risk aversions in the global financial markets as well as geopolitical developments.

While the external environment may continue to remain challenging, the Malaysian economy will experience sustained growth with the primary driver being domestic demand. Private consumption is anticipated to remain supported by wage and employment growth, with additional impetus coming from announced Government measures to support disposable income of households. Investment activity will continue to be anchored by the on-going implementation of infrastructure projects and capital spending in the manufacturing and services sectors.

DEVELOPMENTS IN THE FOURTH QUARTER OF 2016

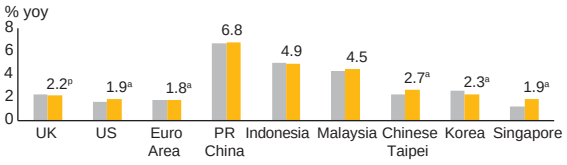
INTERNATIONAL ECONOMIC ENVIRONMENT

Global economic activity continued to expand in the fourth quarter of 2016. The advanced economies experienced divergent growth trends, in part, driven by differences in the strength of private consumption amid cyclical and structural weaknesses. In Asia, economic activity was supported mainly by domestic demand. Of importance, the external sector provided a small lift to growth in several economies, following consecutive quarters of negative growth. Financial market volatility increased following concerns over major issues in the advanced economies, such as the policy and political uncertainties in the US and the UK, arising from the outcome of the presidential election in the US and the UK's vote to exit the EU. Overall, global monetary conditions remained very accommodative, against a backdrop of continued growth concerns with rising, but still low inflation.

Continued expansion in the global economy

The advanced economies experienced a divergence in growth performance, with improvement in the US and sustained growth in the UK and euro area. The US economy expanded at a faster pace in 4Q 2016, mainly reflecting a turnaround in fixed investment growth. Of significance, higher capital spending by the public sector on highways, education and recreation-related constructions supported investment activity. Growth in the UK was broadly sustained, being anchored primarily by private consumption. Firms remained cautious regarding the prospects of the economy amid lingering uncertainties surrounding the new framework of UK-EU relations. In the euro area, growth was mainly driven by domestic demand. However, labour market conditions remained subdued with weak wage growth and high unemployment rates. In addition, business conditions continued to be weighed down by uncertainties from upcoming national elections in some key economies and a potentially lengthy UK-EU exit negotiation process, especially with rising euroscepticism across the region.

Global Real GDP Growth (Annual Change, %)



a Advance
p Preliminary

Source: National authorities

Economic activity was sustained in emerging Asia against a backdrop of gradual improvement in external demand. The Chinese economy registered a marginal improvement in economic growth. While the primary and secondary industries expanded at a slower pace, this was more than offset by higher growth in the services industry (8.2%, 3Q 2016: 7.5%), in particular, in consumer services such as media, education, scientific research, and social services. In the ASEAN economies, growth continued to be underpinned by domestic demand amid some policy support.

Global financial market volatility increased during the quarter

In the second half of the quarter, global financial conditions were more volatile, dominated by shifts in sentiments surrounding events in the advanced economies. In the US, equity markets and the US dollar rose after the presidential election outcome on expectations of pro-growth policies under the new administration and a faster pace of monetary policy normalisation by the Federal Reserve. Financial markets in most other advanced economies improved, supported by tentative signs of strength from PR China, and an extension of the ECB's bond-buying programme. The weakening of the yen against the US dollar also contributed to the rally in Japanese markets, as prospects for exports improved. In contrast, most regional equity and bond markets were adversely affected by concerns that these events could accelerate capital outflows from emerging markets. As a

result, currencies in the region declined broadly from early-November, and ended the quarter lower against the US dollar.

The Brent crude oil prices trended higher, averaging USD51 per barrel (3Q 2016: USD47). During most of the quarter, expectations for an OPEC oil output cut agreement supported a marked improvement in market sentiments. The upward trend was disrupted in the middle of the quarter on account of post-US election uncertainties. The decline was exacerbated by a re-emergence of oversupply concerns as oil inventories in the US increased and uncertainty rose over OPEC's ability to finalise its agreement. Subsequently, however, the eventual agreement among OPEC and non-OPEC countries to reduce oil output resulted in an increase in Brent crude oil price to the highest level since mid-2015, ending the year at USD57 per barrel.

Marginally higher inflation in the advanced and Asian economies

Headline inflation in the advanced economies increased during the quarter, albeit still remaining below central bank targets in most economies. Of significance, the uptrend in headline inflation partly reflected the increase in crude oil prices in the fourth quarter of the year, contributing towards higher fuel and heating oil prices, consequently reducing the drag from energy prices on domestic price pressures. Core inflation was relatively stable in the advanced economies.

Similarly, inflation rose in most Asian economies. Food prices in the region continued to grow at a faster pace due to supply shortages caused by adverse weather conditions. Additionally, the increase in oil prices had eased downward price pressures across the region. Of significance, following a period of negative inflation since 4Q 2014, Singapore recorded its first quarterly increase in inflation, as the modest recovery in global oil prices reduced the drag from transportation costs. However, Hong Kong SAR experienced a moderation in inflation, as government measures to curb escalating private housing prices began to take effect.

Continued accommodative global monetary policy stance

The monetary policy stance in the advanced economies remained highly accommodative. Most central banks maintained their key policy rates except the US Federal Reserve (Fed). The Fed raised the federal funds rate for the first time since December 2015 by 25 basis points to 0.50 – 0.75%. The Fed assessed that the US economic recovery has been expanding at a moderate pace, with significant improvements in the labour market. Of significance, the FOMC expected a faster pace of monetary policy normalisation in 2017. In the euro area, the European Central Bank (ECB) decided to maintain its key policy rate and continue the asset purchase programme (APP) at a rate of EUR80 billion per month until the end of March 2017 and subsequently reduce it to EUR60 billion until December 2017, or beyond, dependent upon the adjustment in the path of inflation. Other central banks in the advanced economies such as the Bank of Japan, Bank of England and the Reserve Bank of Australia kept their key policy rates unchanged over the last quarter.

In Asia, a few central banks reduced their key policy rates during the quarter. Bank Indonesia (BI) cut its key policy rate, the seven-day reverse repo rate, from 5.00% to 4.75% in October as domestic inflationary pressures eased. Subsequently, BI maintained its key interest rates, indicating its caution in response to increasingly uncertain global financial markets. The Reserve Bank of India also reduced its key policy rate from 6.50% to 6.25% in October, citing a marked slowdown in global growth. This was the first decision by the recently appointed monetary policy committee, which pushed policy rates to a five-year low. All other central banks across the region maintained their key policy rates.

Global growth prospects continue to be surrounded by uncertainties

Going forward, the global economy is expected to improve but remain on a moderate growth path. While there are indications of more sustained growth in the major economies in 2017, downside risks to global growth continue to prevail, arising from the volatility in commodity prices, policy uncertainties and growth prospects of the major developed economies, heightened risk aversions in the global financial markets as well as geopolitical developments.

DEVELOPMENTS IN THE MALAYSIAN ECONOMY

The Malaysian economy grew by 4.5% in the fourth quarter

The Malaysian economy expanded by 4.5% in the fourth quarter of 2016 (3Q 2016: 4.3%). Private sector expenditure remained the key driver of growth and contributed towards the continued expansion in domestic demand. However, public sector spending declined and partly offset the sustained growth in private sector activity. As a result, growth in domestic demand moderated. On the external front, net exports contributed positively to growth as real exports expanded at a faster rate than real imports. On a quarter-on-quarter seasonally-adjusted basis, the economy recorded a sustained growth of 1.4% (3Q 2016: 1.4%).

Slower expansion in domestic demand

Domestic demand grew by 3.3% in the fourth quarter of the year (3Q 2016: 4.6%), as the sustained growth in private sector expenditure was partly offset by the contraction in public sector expenditure. **Private consumption** expanded by 6.2% (3Q 2016: 6.4%), supported by continued wage and employment growth. **Private investment** registered a growth of 4.9% (3Q 2016: 4.7%), following continued capital spending in the services and manufacturing sectors. Businesses remained cautious in undertaking capacity expansion given headwinds from both external and domestic fronts.

Public investment recorded a smaller contraction of 0.3% (3Q 2016: -3.8%), supported by higher spending on fixed assets by public corporations. Public consumption growth also contracted during the quarter by 4.2% (3Q 2016: +2.2%) arising from lower spending on supplies and services, particularly on discretionary items such as travel, and professional and consultancy services.

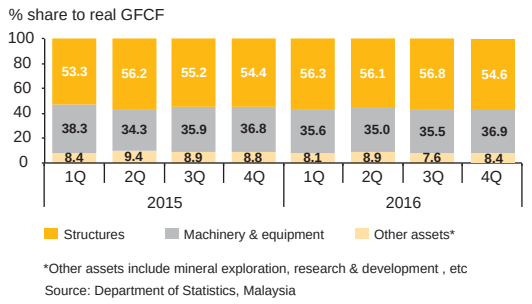
GDP by Expenditure Components
(at constant 2010 prices)

	Share 2016 (%)	2015		2016		
		4Q	Year	3Q	4Q	Year
		Annual change (%)				
Aggregate Domestic Demand (excluding stocks)	91.8	4.0	5.1	4.6	3.3	4.4
Private Sector	70.2	4.9	6.1	6.0	6.0	5.7
Consumption	*53.3*	*4.9*	*6.0*	*6.4*	*6.2*	*6.1*
Investment	*16.9*	*4.9*	*6.4*	*4.7*	*4.9*	*4.4*
Public Sector	21.6	2.1	2.1	-0.2	-2.6	0.4
Consumption	*13.1*	*3.3*	*4.4*	*2.2*	*-4.2*	*1.0*
Investment	*8.5*	*0.4*	*-1.0*	*-3.8*	*-0.3*	*-0.5*
Net Exports	8.1	4.3	-3.8	5.9	5.8	-1.8
Exports of Goods and Services	*70.0*	*4.0*	*0.6*	*-1.3*	*1.3*	*0.1*
Imports of Goods and Services	*61.9*	*4.0*	*1.2*	*-2.3*	*0.7*	*0.4*
GDP[1]	**100.0[1]**	**4.5**	**5.0**	**4.3**	**4.5**	**4.2**
GDP (q-o-q growth, seasonally adjusted)	**-**	**1.2**	**-**	**1.4**	**1.4**	**-**

[1] Numbers do not add up due to rounding and exclusion of stocks
Source: Department of Statistics, Malaysia

Gross fixed capital formation (GFCF) expanded at a slightly faster pace of 2.4% (3Q 2016: 2.0%), due to an improvement in public and private investment growth. The marginally stronger growth in total investment was on account of higher capital spending in machinery and equipment (2.9%; 3Q 2016: 0.9%) amid a moderate expansion in structures investment (2.8%; 3Q 2016: 5.0%) and a smaller contraction in other type of assets investment (-2.1%; 3Q 2016: -12.5%).

GFCF by Type of Assets



*Other assets include mineral exploration, research & development , etc
Source: Department of Statistics, Malaysia

Major economic sectors continued to expand

On the supply side, growth across most major economic sectors improved in the fourth quarter.

The **services sector** expanded at a more moderate pace of 5.5% in the fourth quarter (3Q 2016: 6.1%). The wholesale and retail trade sub-sector registered a slower growth, as the improvement in retail trade and motor vehicles segment was offset by slower growth in the wholesale sub-sector. Growth in the finance and insurance sub-sector also moderated, reflecting the slower expansion in life insurance segment. The transport and storage sub-sector recorded a higher growth, benefitting from the improvement in trade activity and passenger travel during the quarter. In the information and communication sub-sector, growth remained robust, supported by continued demand for data communication services.

GDP by Economic Activity (at constant 2010 prices)

	Share 2016 (%)	2015		2016		
		4Q	Year	3Q	4Q	Year
		Annual change (%)				
Services	54.2	5.0	5.1	6.1	5.5	5.6
Manufacturing	23.0	5.0	4.9	4.2	4.8	4.4
Mining	8.8	-1.3	4.7	3.0[r]	4.9	2.7
Agriculture	8.1	1.5	1.2	-6.1[r]	-2.4	-5.1
Construction	4.5	7.4	8.2	7.9	5.1	7.4
Real GDP	**100.0[1]**	**4.5**	**5.0**	**4.3**	**4.5**	**4.2**
Real GDP (q-o-q seasonally adjusted)	**-**	**1.2**	**-**	**1.4**	**1.4**	**-**

[r] Revised
[1] Numbers do not add up due to rounding and exclusion of import duties component

Source: Department of Statistics, Malaysia

Performance of the Services Sector (value added at constant 2010 prices)

	Share 2016 (%)	2015		2016		
		4Q	Year	3Q	4Q	Year
		Annual change (%)				
Intermediate Services	**38.2**	**4.1**	**4.6**	**6.2**	**5.7**	**5.5**
Finance & insurance	12.5	-1.5	-0.7	5.0	3.2	2.5
Real estate & business services	8.1	6.1	6.6	7.0	7.2	6.9
Transport & storage	6.6	6.0	5.7	5.2	5.5	5.6
Information & communication	10.9	9.2	9.4	7.6	7.7	8.2
Final Services	**61.9**	**5.4**	**5.5**	**6.1**	**5.5**	**5.7**
Wholesale & retail trade	27.5	6.4	6.9	6.7	6.2	6.2
Food & beverages and accommodation	5.2	5.8	6.4	7.4	7.7	7.1
Utilities	4.8	3.2	3.5	5.0	4.5	5.4
Government services	16.2	4.7	4.0	5.5	4.1	4.9
Other services	8.1	4.6	4.7	5.1	5.2	4.8
Total Services	**100.0[1]**	**5.0**	**5.1**	**6.1**	**5.5**	**5.6**

[1] Numbers do not add up due to rounding

Source: Department of Statistics, Malaysia

Selected Quarterly Indicators in the Services Sector

	2015		2016		
	4Q	Year	3Q	4Q	Year
	Index				
MIER Consumer Sentiments Index	63.8	69.6	73.6	69.8	73.7
MIER Retail Trade Index	77.9	83.4	111.6	91.4	93.5
MIER Tourism Market Index	89.8	97.9	112.1	101.4	101.5
	Annual change (%)				
Total passenger traffic at all airports	-3.0	0.9	9.9	11.8[1]	6.0[2]
Total consumption credit outstanding	3.1	3.1	1.2	0.9	0.9
Total loans outstanding	7.9	7.9	4.2	5.3	5.3
Loans outstanding to the wholesale & retail trade, hotels & restaurants	8.2	8.2	3.1	5.5	5.5
Imports of consumption goods	38.1	24.1	-0.8	0.1	7.4
Total sales of motor vehicles	4.1	0.0	-12.5	-10.8	-13.0
Container cargo handled (Port Klang and PTP)	5.4	7.9	-4.0	1.5	2.1

[1] Oct-Nov 2016
[2] Jan-Nov 2016

Source: Various sources

The **manufacturing sector** registered a higher growth of 4.8% (3Q 2016: 4.2%), driven by both export- and domestic-oriented industries. The better performance of the export-oriented industries was driven mainly by stronger growth in the E&E segment, with double-digit expansion in semiconductors, which was in line with the continued uptick in global demand for semiconductors. Manufacturing activity was also supported by improvements in the primary-related cluster following higher production of petrochemicals as a result of sustained regional demand. Growth of domestic-oriented industries was supported by sustained construction-related activity and food-related production, despite being weighed down by continued weakness in the transport equipment segment, as car production growth remained contractionary.

Performance of the Manufacturing Sector

	Share in 2015 (%)	2015		2016		
		4Q	Year	3Q	4Q	Year
		Annual Change (%)				
Overall Value Added (at constant 2010 prices)	**100.0**	**5.0**	**4.9**	**4.2**	**4.8**	**4.4**
Export-oriented industries	63.6	5.4	5.6	5.6	6.1	5.8
Domestic-oriented industries	36.4	4.1	3.7	1.7	2.4	1.9
Overall Manufacturing Production[1]	**100.0**	**4.8**	**4.8**	**4.0**	**4.9**	**4.3**
Export-oriented industries	**77.6**	**4.7**	**4.8**	**4.1**	**6.0**	**4.7**
Electronics and electrical products cluster	**25.0**	**10.7**	**9.2**	**6.2**	**7.4**	**7.0**
Of which:						
Electronics	15.3	5.7	0.7	8.9	10.6	8.9
Electrical products	7.6	24.7	32.0	2.2	2.4	4.6
Primary-related cluster	**52.6**	**1.5**	**2.5**	**2.9**	**5.2**	**3.3**
Of which:						
Chemicals and chemical products	14.3	1.9	4.6	5.7	7.0	5.2
Petroleum products	21.0	-0.2	1.2	3.1	3.1	3.1
Rubber products	2.5	7.0	5.1	2.9	1.4	3.9
Off-estate processing	6.4	-1.9	-3.5	-7.2	9.5	-5.0
Domestic-oriented industries	**22.4**	**5.0**	**4.7**	**3.3**	**1.6**	**3.0**
Construction-related cluster	**11.3**	**4.8**	**4.5**	**4.0**	**3.9**	**4.4**
Of which:						
Construction-related products	8.2	3.7	4.5	3.3	3.9	4.1
Fabricated metal products	3.1	6.9	4.6	5.2	3.9	5.1
Consumer-related cluster	**11.1**	**5.1**	**4.8**	**2.7**	**-0.5**	**1.7**
Of which:						
Transport equipment	5.5	3.7	5.2	-2.0	-4.0	-3.1
Food, beverage & tobacco products	5.4	7.4	4.8	8.3	3.8	8.0

[1] Industrial Production Index (2010=100)

Source: Department of Statistics, Malaysia

The **construction sector** grew by 5.1% in the fourth quarter (3Q 2016: 7.9%), underpinned mainly by activity in the civil engineering sub-sector following progress in various projects in the petrochemical, transportation and utilities segments. Although still affected by oversupply issues in the commercial segment, growth in the non-residential sub-segment improved marginally, benefitting from the low base from the previous year. Activity in the residential sub-sector moderated, reflecting the subdued property market, while growth in the special trade sub-sector was supported by both early- and end-work activity.

Growth in the **agriculture sector** contracted at a slower pace (-2.4%; 3Q 2016[r]: -6.1%), supported by an improvement in crude palm oil yields as the negative impact of El Niño gradually waned. Of significance, in December, fresh fruit bunch (FFB) yields recorded its first positive growth in 2016, growing by 1.5% compared to the same period last year. In the **mining sector**, growth improved (4.9%, 3Q 2016[r]: 3.0%), due mainly to higher natural gas production, underpinned particularly by output increases in Sarawak and Sabah.

Performance of the Agriculture Sector

	Share in 2016 (%)	2015		2016		
		4Q	Year	3Q	4Q	Year
		Annual change (%)				
Value Added (at constant 2010 prices)	**100.0**	**1.5**	**1.2**	**-6.1[r]**	**-2.4**	**-5.1**
Industrial Crops	**57.3**	**1.7**	**0.7**	**-12.3[r]**	**-5.4**	**-10.8**
Of which:						
Oil palm	43.1	1.2	1.3	-13.8	-7.2	-12.7
Rubber	7.1	26.9	8.1	-8.1[r]	1.1	-6.3
Food Crops	**42.7**	**1.2**	**2.0**	**3.9**	**2.6**	**3.8**
Of which:						
Fishing	11.5	2.4	0.6	3.2	1.1	2.2
Livestock	11.7	0.4	2.4	4.2	0.8	3.7

[r] Revised

Source: Department of Statistics, Malaysia

Performance of the Mining Sector

	2015		2016		
	4Q	Year	3Q	4Q	Year
	Annual change (%)				
Value Added (at constant 2010 prices)	**-1.3**	**4.7**	**3.0[r]**	**4.9**	**2.7**
Production					
Of which:					
Crude oil and condensates	0.2	10.1	6.3[r]	0.2	1.6
Natural gas	-5.0	-1.8	-1.1[r]	10.1	3.3
Other mining and support services	14.4	13.7	6.9[r]	5.7	6.9

[r] Revised

Source: Department of Statistics, Malaysia

Indicators for the Construction Sector

	Share 2016 (%)	2015		2016		
		4Q	Year	3Q	4Q	Year
		Annual change (%)				
Value of construction work done	100.0	11.2	12.1	10.7	8.1	10.3
Residential buildings	26.1	8.7	10.9	16.4	9.8	11.7
Non-residential buildings	26.3	3.6	13.9	-1.4	2.5	1.7
Civil engineering	29.0	23.3	11.9	19.3	12.5	18.4
Special Trade[1]	18.5	4.4	8.0	4.2	3.7	9.6
Housing approvals		-18.5	-25.3	26.6	-18.5	-17.7
Production[2] of construction-related materials		4.8	4.5	4.0	3.9	4.4
Hydraulic cement		11.9	14.7	-8.3	-6.3	-7.6
Other porcelain and ceramic products		12.2	20.0	10.7	-0.8	4.4
Prefabricated structural components for building or civil engineering of cement, concrete or artificial stone		21.1	-2.2	26.2	6.8	18.3
Capital imports (excluding lumpy items)		2.7	4.3	0.1	4.9	0.3
Loans for the construction sector						
Approval		-5.5	3.8	34.4	2.9	5.1
Disbursement		-13.4	-0.6	7.7	4.5	3.5

[1] Works such as site preparation, electrical installation and painting
[2] Industrial Production Index (2010=100)

Source: Department of Statistics, Malaysia, Ministry of Urban Wellbeing, Housing and Local Government and Bank Negara Malaysia

Headline inflation was higher in the fourth quarter 2016

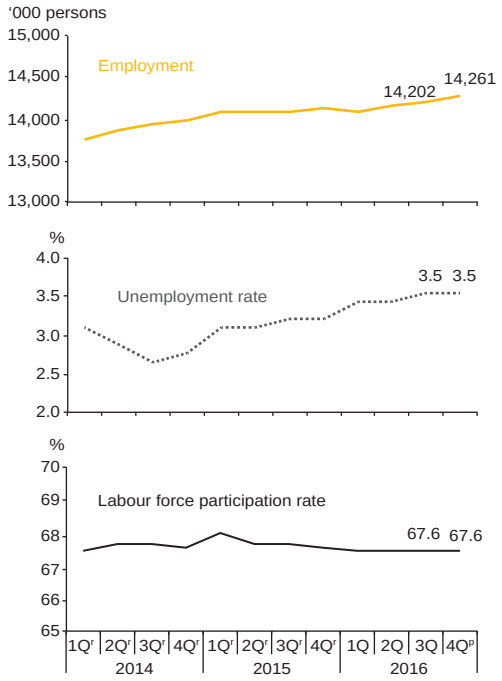
Inflation, as measured by the annual change in the Consumer Price Index (CPI), increased to 1.7% in the fourth quarter of 2016 (3Q 2016: 1.3%). The higher inflation was driven mainly by upward adjustments to domestic fuel prices during the quarter. Average prices of RON95 petrol, RON97 petrol and diesel increased by 15 sen, 15 sen and 17 sen, respectively, leading to a smaller negative inflation in the *transport* category (-2.6%; 3Q 2016: -7.4%). The inflationary impact was mitigated by the lower inflation in the *alcoholic beverages and tobacco* category (6.6%; 3Q 2016: 19.7%) due to the lapse in the impact of the upward revision in cigarette prices in the base period of 4Q 2015. For the year as a whole, inflation averaged 2.1% (2015: 2.1%).

The Producer Price Index (PPI) turned around to increase by 2.9% (3Q 2016: -0.6%) in the fourth quarter of 2016. The increase in PPI was due mainly to higher prices of *crude materials for further processing* and *intermediate materials, supplies and components*, reflecting higher prices of crude palm oil-related materials and global oil price during the quarter. Crude palm oil price rose significantly during the quarter amid the seasonal decline in production and low inventory levels. Global oil price was also higher following the OPEC agreement to reduce output.

Softer labour market

Labour market conditions remained stable. While total employment was higher during the quarter, registering a higher net gain of 58,600 jobs (3Q 2016: 40,500 jobs), the unemployment rate was unchanged, at 3.5% of the labour force (3Q 2016: 3.5%). The job gains in the fourth quarter were attributable mainly to the services sector, particularly the wholesale and retail, and accommodation and food services; and the finance and insurance sub-sectors. Labour force participation was sustained at 67.6% of total working-age population (3Q 2016: 67.6%), while new job postings on JobStreet.com moderated to an average of 17,738 positions per month in the fourth quarter (3Q 2016: 20,229), following continued conservative hiring by businesses.

Labour Market Indicators*



*The Labour Force Survey (LFS) figures for 1Q 2014 onwards reflect new current population estimates by DOSM

[p] Preliminary [r] Revision

Source: Department of Statistics, Malaysia

Consumer Price Index

Category	Weights (%) (2010=100)	3Q 2016	4Q 2016
		Annual change, %	
Total	**100**	**1.3**	**1.7**
Food and non-alcoholic beverages	30.2	3.4	3.3
Housing, water, electricity, gas and other fuels	23.8	2.2	2.1
Transport	13.7	-7.4	-2.6
Alcoholic beverages and tobacco	2.9	19.7	6.6
Others	29.4	1.1	1.1

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

Private sector wage growth was sustained, supported by the increase in the minimum wage, which took effect in July 2016. In the major services sub-sectors[1], wage growth was slightly higher at 3.3% (3Q 2016: 3.1%). Manufacturing sector wages continued to expand, albeit at a more moderate pace of 5.9% (3Q 2016: 6.9%), supported by export-oriented sectors, particularly the petrochemicals and resource-related clusters. In the public sector, aggregate wage growth remained strong in the fourth quarter, following the civil servants' salary adjustment, which was implemented in July 2016 (7.1%; 3Q 2016: 11.7%).

External position remained resilient in the fourth quarter

In 4Q 2016, the current account surplus widened, due mainly to a higher trade surplus and narrower deficits in the income accounts.

Balance of Payments[1]

	2015		2016		
	4Q	Year	3Q	4Q	Year
	RM billion				
Current Account	**10.5**	**34.7**	**6.0**	**12.2**	**25.2**
(% of GNI)	*3.6*	*3.1*	*2.0*	*3.8*	*2.1*
Goods	31.1	109.6	26.5	31.4	101.2
Services	-6.4	-21.0	-5.1	-6.0	-22.6
Primary income	-9.1	-32.0	-10.8	-9.0	-34.7
Secondary income	-5.0	-21.9	-4.6	-4.1	-18.7
Financial Account	**3.9**	**-50.9**	**-6.3**	**-13.2**	**-4.2**
Direct investment	5.8	4.8	3.0	5.9	17.9
Assets	*-2.9*	*-37.2*	*-11.3*	*-7.9*	*-34.3*
Liabilities	*8.6*	*41.9*	*14.3*	*13.8*	*52.2*
Portfolio investment	15.9	-28.2	-10.6	-22.3	-19.7
Assets	*5.6*	*-9.1*	*-7.1*	*2.8*	*-15.0*
Liabilities	*10.3*	*-19.1*	*-3.5*	*-25.1*	*-4.7*
Financial derivatives	-0.1	-0.7	-0.1	-1.2	-0.8
Other investment	-17.6	-26.8	1.4	4.4	-1.7
Errors & omissions[2]	-20.4	21.1	14.9	20.1	-6.0
Overall Balance	**-6.0**	**3.8**	**14.6**	**19.2**	**15.0**

Assets: (-) denotes outflows due to the acquisition of assets abroad by residents
Liabilities: (+) denotes inflows due to the incurrence of foreign liabilities
[1] In accordance with the Sixth Edition of The Balance of Payments and International Investment Position Manual (BPM6) by the International Monetary Fund (IMF)
[2] Includes unrealised foreign exchange revaluation gains/losses on international reserves

Source: Department of Statistics, Malaysia

Trade Account

	Share 2016 (%)	2015		2016		
		4Q	Year	3Q	4Q	Year
		Annual change (%)				
Gross Exports	**100.0**	**8.0**	**1.6**	**-2.3**	**2.8**	**1.1**
Manufactured	82.2	12.5	6.5	-1.1	3.4	3.2
E&E	*36.6*	*9.6*	*8.5*	*-0.6*	*7.6*	*3.5*
Non-E&E	*45.5*	*14.9*	*5.0*	*-1.6*	*0.1*	*3.0*
Resource based	*22.9*	*2.7*	*-3.9*	*-0.5*	*5.6*	*3.3*
Non-resource based	*22.7*	*29.5*	*15.7*	*-2.7*	*-5.2*	*2.7*
Commodities	17.1	-7.7	-14.9	-8.2	-0.9	-8.6
Minerals	*8.2*	*-15.1*	*-22.9*	*-17.7*	*-12.8*	*-19.8*
Agriculture	*9.0*	*3.8*	*-2.8*	*1.2*	*14.1*	*4.7*
Gross Imports	**100.0**	**3.4**	**0.4**	**-0.1**	**5.0**	**1.9**
Intermediate goods	57.1	-1.7	-2.1	-0.3	3.8	-0.1
Capital goods	14.3	0.2	-0.3	15.7	6.5	4.9
Consumption goods	9.6	38.1	24.1	-0.8	0.1	7.4
Others (including re-exports and dual-use goods)	18.9	8.9	-0.2	-9.5	10.4	3.2
Trade balance (RM billion)	**–**	**30.6**	**91.6**	**18.0**	**27.5**	**87.3**

Source: MATRADE and Department of Statistics, Malaysia

Gross exports turned around to register a positive growth of 2.8% in 4Q 2016, (3Q 2016: -2.3%). The expansion was underpinned by higher manufactured exports and improvement in commodity exports. Gross imports also recorded a positive growth of 5% (3Q 2016: -0.1%). The faster growth was due to a higher growth in all import categories, except capital imports. As a result, the trade surplus widened to RM27.5 billion (3Q 2016: RM18.0 billion). For 2016 as a whole, exports and imports recorded a growth of 1.1% and 1.9%, respectively (2015: 1.6% and 0.4%, respectively), contributing an accumulated trade surplus of RM87.3 billion (2015: RM91.6 billion).

Manufactured exports recorded a positive turnaround in the fourth quarter, attributed mainly to the improvement in exports of semiconductor devices. The higher E&E exports more than offset the decline in exports of non-resource based products such as manufactures of metal, and machinery, equipment and parts. Commodity exports continued to improve, supported by broad-based improvement in prices.

[1] Major services sector consists of wholesale and retail trade and food and beverages, accommodations; information and communications, transportation and storage; health, education and arts, entertainment and recreation; and professional and real estate services sub-sectors.

By destination, exports to major trading partners, particularly P.R. China and Hong Kong, experienced a sharp turnaround to register positive growth due mainly to higher demand for E&E and agriculture exports. Exports to the EU also recorded an improvement, largely underpinned by higher E&E exports and commodity exports. Export growth to Japan continued to decline, while exports to the US moderated, reflecting lower exports of LNG and manufactured goods, respectively.

Gross imports expanded by 5% during the quarter (3Q 2016: -0.1%), supported by higher import growth in intermediate and consumption goods. The recovery in intermediate imports was due mainly to a higher demand for fuel and lubricants, and industrial supplies, in line with higher commodity prices and manufactured export growth. Higher imports of consumption goods, particularly food and beverages, durable and non-durable goods, also supported gross import growth. The expansion in imports for re-exports reflects the improvement in global demand and a pick-up in trade activity. Capital import growth however, moderated due primarily to lower imports of telecommunications equipment and metal containers.

Malaysia: Direction of Exports

	Share 2016 (%)	2015		2016		
		4Q	Year	3Q	4Q	Year
		Annual change (%)				
European Union (EU)	**10.2**	**12.9**	**8.4**	**-3.5**	**1.0**	**1.2**
Japan	**8.1**	**-6.9**	**-12.0**	**-13.0**	**-13.2**	**-12.9**
United States	**10.2**	**18.4**	**14.4**	**4.8**	**2.3**	**8.9**
ASEAN[1]	**29.4**	**8.5**	**2.7**	**3.3**	**6.1**	**5.4**
North East Asia	**22.9**	**6.9**	**2.3**	**-7.7**	**5.6**	**-3.2**
People's Republic of China	*12.5*	*10.9*	*10.0*	*-8.3*	*12.3*	*-2.9*
Hong Kong SAR	*4.8*	*1.0*	*-0.5*	*-1.4*	*10.4*	*2.1*
Korea	*2.9*	*-9.8*	*-11.7*	*-16.2*	*-7.8*	*-7.6*
Chinese Taipei	*2.7*	*22.6*	*-6.5*	*-6.1*	*-13.5*	*-8.0*
West Asia[2]	**2.9**	**-3.3**	**-4.1**	**-9.4**	**11.8**	**3.1**
India	**4.1**	**7.8**	**-0.7**	**1.4**	**1.1**	**1.1**
Total exports	**100.0**	**8.0**	**1.6**	**-2.3**	**2.8**	**1.1**

[1] Singapore, Thailand, Indonesia, Philippines, Brunei Darussalam, Vietnam, Cambodia, Myanmar and Laos
[2] United Arab Emirates, Saudi Arabia, Oman, Iraq, Qatar, Kuwait, Jordan, Lebanon, Bahrain, Syria, Palestine, Yemen and Iran

Source: Department of Statistics, Malaysia

The deficit in the **services** account was larger at RM6.0 billion in the fourth quarter of 2016 (3Q 2016: a deficit of RM5.1 billion), attributable mainly to higher net transportation payments amid better trade activities and higher net payments for other services, particularly for construction; and usage charges for intellectual properties. In addition, lower net receipts from travel services arising from the rise of outbound tourists posed a drag to the services account.

The deficit in the **primary income** account narrowed to RM9.0 billion in the fourth quarter of 2016 (3Q 2016: a deficit of RM10.8 billion), reflecting mainly higher direct investment income accrued to Malaysian companies investing abroad in the mining sector as a result of higher commodity prices. Income accrued to foreign direct investors, particularly in the mining and manufacturing sectors, was broadly unchanged. The net payments in the **secondary income** account were lower at RM4.1 billion in the fourth quarter of 2016 (3Q 2016: net payment of RM4.6 billion), due mainly to higher inward remittances.

In the fourth quarter of 2016, the **financial account** recorded a net outflow of RM13.2 billion (3Q 2016: net outflow of RM6.3 billion), as the larger net outflows in the portfolio investment account had more than offset the higher net inflows in both the direct and other investment accounts.

Portfolio investment recorded a significant net outflow of RM22.3 billion (3Q 2016: net outflow of RM 10.6 billion). Portfolio investment by non-residents recorded a net outflow of RM25.1 billion (3Q 2016: net outflow of RM3.5 billion), mainly on account of lower foreign holdings of Malaysian Government Securities (MGS) and Government Investment Issues (GII) as well as higher liquidation of equity securities. During the period, volatility in the global financial markets intensified as investor sentiments were affected by the outcome of the US presidential election, and the expectation of a faster pace of monetary policy normalisation by the Federal Reserve. Portfolio investment by residents registered a net inflow of RM2.8 billion (3Q 2016: net outflow of RM7.1 billion), due mainly to the maturity of foreign currency debt securities held by domestic financial institutions, which more than offset the continued purchases of foreign equity securities.

Direct investment account recorded a higher net inflow of RM5.9 billion (3Q 2016: net inflow of RM3.0 billion), as the incurrence of direct investment liabilities continued to outpace the moderating accumulation of direct investment assets.

On the liabilities side, inward direct investment amounted to a net inflow of RM13.8 billion (3Q 2016: net inflow of RM14.3 billion). Of these, **Foreign Direct Investment (FDI)** rose to RM10.8 billion (3Q 2016: net inflow of RM6.5 billion), due mainly to a higher injection of equity capital and a net extension of loans by parent companies to their subsidiaries in Malaysia. FDI inflows were largely channelled into the manufacturing sector, particularly the E&E and petrochemical industries. This is followed by investments in the services sector, mainly in the finance and insurance as well as the wholesale and retail trade sub-sectors.

On the assets side, outward direct investment amounted to a net outflow of RM7.9 billion (3Q 2016: net outflow of RM11.3 billion). Of these, **Direct Investment Abroad (DIA)** by Malaysian companies increased to RM4.9 billion (3Q 2016: net outflow of RM3.6 billion), due mainly to a higher reinvestment of earnings and sustained equity capital injections to subsidiaries abroad. The bulk of DIA was undertaken by companies in the mining sector, followed by the services sector, particularly the telecommunication and wholesale and retail trade sub-sectors.

Other investment account registered a larger net inflow of RM4.4 billion (3Q 2016: net inflow of RM 1.4 billion), attributed mainly to a net placement of interbank deposits by foreign financial institutions in Malaysian banks as well as a repayment of trade credits which were previously extended by Malaysian exporters.

Following these developments, the overall balance of payments registered a surplus of RM19.2 billion in the fourth quarter (3Q 2016: surplus of RM 14.6 billion). Errors and omissions amounted to RM20.1 billion or 4.9% of total trade, mostly reflecting the foreign exchange revaluation changes in international reserves arising from the strengthening of major currencies against the ringgit during the quarter.

Manageable external debt

Malaysia's external debt increased by RM43.4 billion or 5.0% to RM908.7 billion, equivalent to USD200.6 billion or 73.9% of GDP as at end-December 2016 (end-September 2016: RM865.3 billion or USD206.6 billion, equivalent to 70.4% of GDP). The increase was mainly attributed to valuation effects following the weakening of the ringgit against most currencies during the quarter. About 82% of the foreign exchange valuation changes were recorded in offshore borrowing. Nonetheless, the offshore borrowing remained low at 42.7% of GDP as at end-December compared to 60% of GDP during the Asian Financial Crisis (AFC) in 1997-98. Also, the Federal Government only accounts for 4.0% of total offshore borrowing as at end-December 2016.

In aggregate, the impact of foreign exchange fluctuations was mostly contained, as one-third of total external debt was denominated in ringgit. The remaining portion denominated in foreign currency was largely hedged, either naturally through foreign currency earnings, or through the use of financial instruments.

Excluding valuation effects, Malaysia's external debt position would have increased by only 0.7% from the previous quarter. The increase reflected a net increase in interbank borrowing and intercompany loans, on top of a slightly higher placement of deposits in the domestic banking system by non-residents. This was partly offset by some liquidation of non-resident holdings of domestic debt securities, especially MGS and Government Investment Issues.

Overall, Malaysia's external debt remains manageable, with medium- to long-term external debt accounting for more than half of the outstanding position (58.6%). The share of short-term external debt increased slightly to account for 41.4% of the total external debt (end-September 2016: 38.6%) during the quarter. The international reserves were adequate to cover the short-term external debt by 1.1 times. About two-thirds of the short-term external debt is held by the banking sector, not all of which poses a claim on the international reserves given that this debt is partly covered by the banks' corresponding external assets. The bulk of the remaining short-term external debt is accounted for by trade credits and intercompany loans. The former are largely backed by export earnings, while the latter are generally on flexible and concessionary terms, such as having no fixed repayment schedule and zero or low interest rate.

Outstanding External Debt

	2015	2016	
	end-Dec	end-Sep	end-Dec
	RM billion		
Offshore borrowing[1]	463.6	472.1	524.3
USD billion equivalent	*106.9*	*112.7*	*115.8*
Medium- and long-term	*285.9*	*295.8*	*316.4*
Public sector	128.3	120.4	130.6
Private sector	157.6	175.4	185.9
Short-term	*177.7*	*176.3*	*207.9*
NR holdings of dom. debt securities	211.3	237.1	214.2
Medium- and long-term	*184.1*	*223.5*	*203.3*
Short-term	*27.2*	*13.6*	*10.9*
NR deposits	81.6	82.6	86.2
Others[2]	77.2	73.5	84.0
Medium- and long-term	*11.9*	*11.8*	*12.4*
Short-term	*65.3*	*61.7*	*71.6*
Total external debt	**833.8**	**865.3**	**908.7**
USD billion equivalent	*192.3*	*206.6*	*200.6*
Total debt/GDP (%)	72.1	70.4	73.9
Short-term debt[3]/Total debt (%)	42.2	38.6	41.4
Reserves/Short-term debt[3] (times)	1.2	1.2	1.1[4]

[1] Equivalent to the external debt as previously defined, comprised mainly foreign currency loans raised, and bonds and notes issued offshore.
[2] Comprise trade credits, IMF allocation of SDRs and miscellaneous.
[3] Short-term offshore borrowing, NR holdings of short-term domestic debt securities, NR deposits, short-term trade credits and miscellaneous.
[4] Based on international reserves as at 31 January 2017.

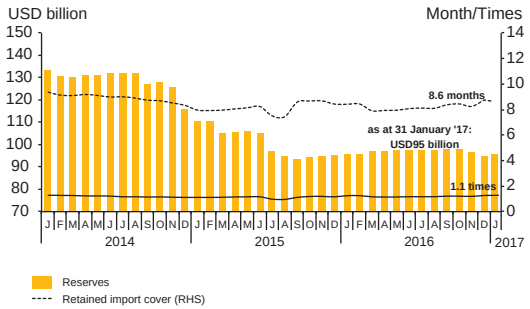
Note: NR refers to non-resident

Source: Ministry of Finance, Malaysia and Bank Negara Malaysia

International reserves remain ample to facilitate international transactions

As at 31 January 2017, the reserves position amounted to USD95.0 billion (equivalent to RM426.0 billion). The international reserves remain ample to facilitate international transactions. They are sufficient to finance 8.6 months of retained imports, significantly higher than the 3-month international threshold. The reserves level is also adequate to meet external obligations given the reserves to short-term external debt coverage of 1.1 times. It is important to note that not all short-term external debt creates a claim on reserves given the availability of external assets and export earnings of borrowers.

Net International Reserves (as at end period)

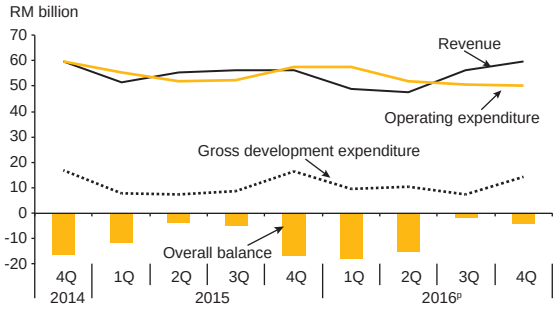


Source: Bank Negara Malaysia

Lower fiscal deficit of 3.1% of GDP in 2016

In the fourth quarter, the Federal Government recorded a fiscal deficit of 1.3% of GDP (3Q 2016: -0.6% of GDP), due to higher growth in revenue and a decline in total expenditure. Revenue increased by 6.8% on an annual basis (3Q 2016: 0.1%) driven by higher collections of Goods and Services Tax (GST). Operating expenditure declined by 13.0% on an annual basis (3Q 2016: -3.0%) due mainly to lower expenditure on supplies and services, and subsidies. Development expenditure similarly recorded a decline on an annual basis. The bulk of the expenditure during the quarter was disbursed primarily to the health sector, and agriculture and rural development. For the year as a whole, the Federal Government achieved a fiscal deficit target of 3.1% of GDP (2015: 3.2% of GDP). Total outstanding debt of the Federal Government stood at RM648.5 billion or 52.7% of GDP as at end-2016.

Federal Government Finance



p Preliminary

Source: Ministry of Finance, Malaysia

Federal Government Finance

	2015		2016p		
	4Q	Year	3Q	4Q	Year
	RM billion				
Revenue	56.0	219.1	56.3	59.8	212.4
% annual growth	*-6.0*	*-0.7*	*0.1*	*6.8*	*-3.0*
Operating expenditure	57.5	217.0	50.7	50.0	210.2
% annual growth	*-3.8*	*-1.2*	*-3.0*	*-13.0*	*-3.1*
Current account	**-1.4**	**2.1**	**5.6**	**9.8**	**2.2**
% of GDP	***-0.5***	***0.2***	***1.8***	***3.0***	***0.2***
Net development expenditure	15.5	39.3	7.4	13.9	40.9
% annual growth	*-5.7*	*2.2*	*-15.1*	*-9.8*	*4.2*
Overall balance	**-16.9**	**-37.2**	**-1.8**	**-4.1**	**-38.7**
% of GDP	***-5.6***	***-3.2***	***-0.6***	***-1.3***	***-3.1***
Memo item:					
Total net expenditure	72.9	256.3	58.1	64.0	251.1
% annual growth	*-4.2*	*-0.7*	*-4.7*	*-12.3*	*-2.0*
Total Federal Government debt[1]					
(as at end-period)	630.5	630.5	643.6	648.5	648.5
% of GDP	*54.5*	*54.5*	*52.4*	*52.7*	*52.7*
Domestic debt	433.1	433.1	411.4	435.6	435.6
% of GDP	*37.4*	*37.4*	*33.5*	*35.4*	*35.4*
External debt	197.4	197.4	232.2	212.9	212.9
% of GDP	*17.1*	*17.1*	*18.9*	*17.3*	*17.3*
Non-resident holdings of RM-denominated Federal Government debt	*176.0*	*176.0*	*211.8*	*191.8*	*191.8*
% of GDP	*15.2*	*15.2*	*17.2*	*15.6*	*15.6*
Offshore borrowing	*21.5*	*21.5*	*20.4*	*21.1*	*21.1*
% of GDP	*1.9*	*1.9*	*1.7*	*1.7*	*1.7*

p Preliminary
[1] A portion of the Housing Loan Fund debt amounting to RM21.9 billion (1.8% of estimated 2016 GDP) has been transferred to the new statutory body for civil servant housing loans (Public Sector Home Financing Board, LPPSA) beginning 2016

Note: Beginning first quarter of 2015, GDP has been rebased from base year 2005 to base year 2010

Source: Ministry of Finance, Malaysia and Bank Negara Malaysia

MONETARY AND FINANCIAL DEVELOPMENTS

Interest rates remained stable

The Monetary Policy Committee (MPC) maintained the Overnight Policy Rate (OPR) at 3.00% during the fourth quarter of 2016. At the prevailing level of the OPR, monetary conditions remained supportive of economic activity.

Reflecting the unchanged OPR, the overnight interbank rate was relatively stable during the quarter, moving within a range of 2.90%-3.00%. Interbank rates for tenures one month and shorter were also relatively stable. The 3-month interbank rate, while relatively steady, increased by four basis points from end-September to end-December given competition for stable funding amid net external outflows. Reflecting the steady interbank rates, the 3-month KLIBOR was stable during the quarter, increasing marginally by one basis point to 3.41%.

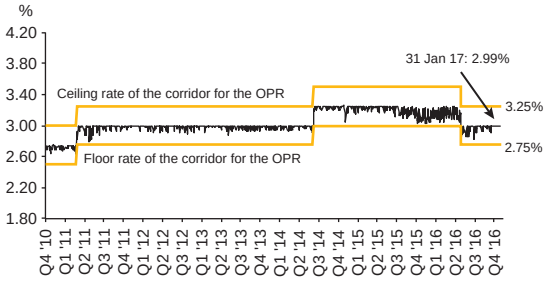
Correspondingly, retail lending rates were stable during this quarter. The weighted average base rate (BR) of commercial banks was unchanged at 3.61%. The weighted average lending rate (ALR) on outstanding loans was also relatively stable, declining by five basis points from end-September to end-December[2]. On average, fixed deposit (FD) rates remained unchanged for tenures of up to 1-year.

Interest Rates

	2015	2016	
	4Q	3Q	4Q
	At end-period (%)		
Overnight Policy Rate (OPR)	3.25	3.00	3.00
Interbank rates			
Overnight	3.05	2.99	3.00
1-month	3.45	3.08	3.10
Base lending rate (BLR)			
Commercial banks	6.79	6.65	6.65
Weighted average base rate (BR)			
Commercial banks	3.77	3.61	3.61
Weighted average lending rate (ALR)			
Commercial banks	5.40	5.27	5.21
Fixed deposit rates			
Commercial banks			
1-month	3.08	2.87	2.86
12-month	3.31	3.07	3.06

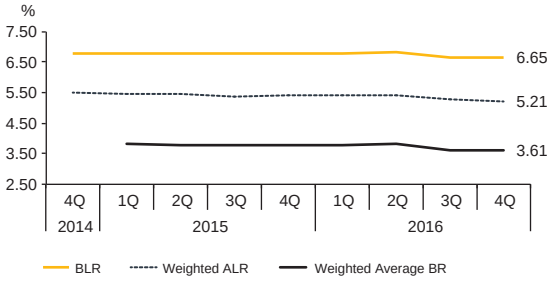
Source: Bank Negara Malaysia

Daily Weighted Average Overnight Interbank Rate



Source: Bank Negara Malaysia

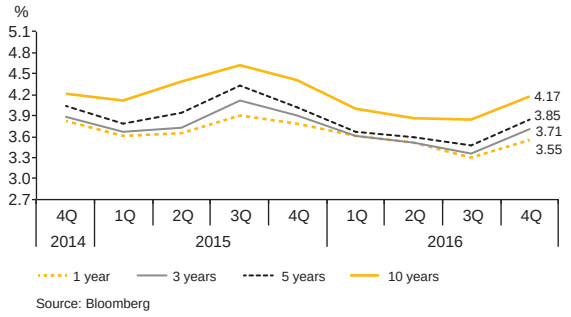
Lending Rates of Commercial Banks (At end-period)



Source: Bank Negara Malaysia

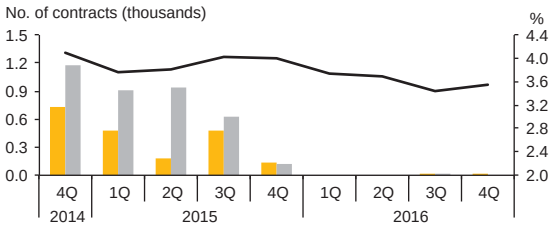
[2] In comparison, the weighted ALR declined by 16 basis points in the third quarter.

Interest Rate Swap: Rates



Source: Bloomberg

3 Month KLIBOR Futures



Source: Bursa Malaysia

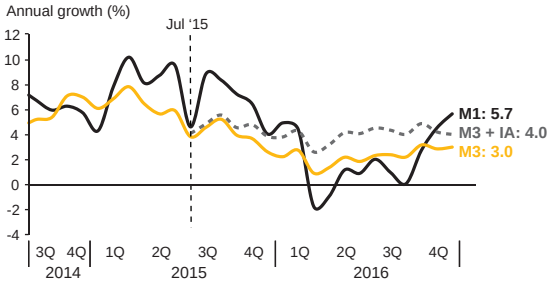
M3 expanded during the quarter

M1, or narrow money, decreased by RM22.6 billion during the quarter. On an annual basis, M1 recorded a growth rate of 5.7% as at end-December (end-September: 0.1%). M3, or broad money, increased by RM25.0 billion on a quarter-on-quarter basis to record an annual growth rate of 3% as at end-December (end-September: 2.2%).

The increase in M3 during the quarter was driven mainly by the continued expansion of credit extended to the private sector by the banking system. The expansion, however, was partially offset by *other influences*, reflecting foreign exchange revaluation effects and the continued growth of Islamic Investment Accounts.

In the banking system, liquidity conditions remained ample at both the institutional and system-wide levels. The level of surplus liquidity placed with BNM remained relatively stable during the quarter.

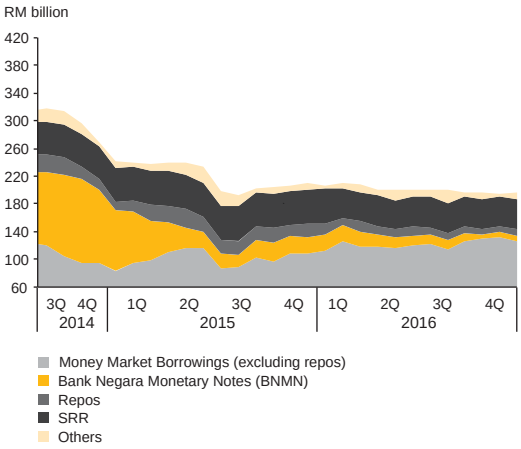
Monetary Aggregates



Note: From July 2015 onwards, the compilation of M3 is adjusted to exclude Islamic Investment Accounts (IA) due to a data reclassification exercise. This is reflected as a negative contribution through *'other influences'*. The dotted line represents M3 growth had this reclassification not taken place

Source: Bank Negara Malaysia

Outstanding Liquidity Placed with Bank Negara Malaysia (At end-period, RM billion)



Source: Bank Negara Malaysia

Determinants of Broad Money, M3

	Change during the period				
	2015		2016		
	4Q	Year	3Q	4Q	Year
	RM billion				
M3	**12.1**	**40.8**	**6.4**	**25.0**	**47.9**
Net claims on Government	5.1	-8.9	2.0	18.9	18.1
Claims on private sector	31.6	120.3	23.5	31.6	88.7
Loans	*25.7*	*106.1*	*18.7*	*37.2*	*83.5*
Securities	*5.9*	*14.1*	*4.8*	*-5.6*	*5.2*
Net foreign assets[1]	-0.2	22.0	1.3	10.1	-5.8
BNM	*-5.7*	*1.0*	*14.4*	*18.8*	*14.9*
Banking System	*5.5*	*21.0*	*-13.1*	*-8.8*	*-20.7*
Other influences	-24.4	-92.6	-20.4	-35.5	-53.1

[1] Post-revaluation
Note: Numbers may not add up due to rounding

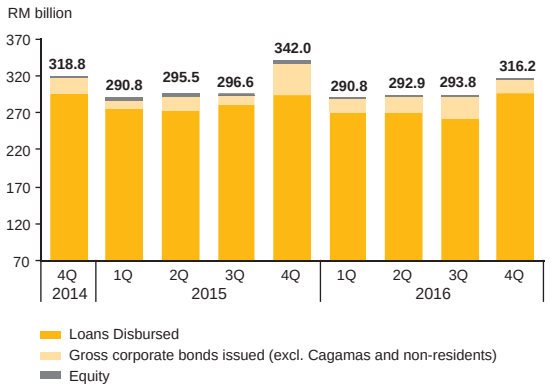
Source: Bank Negara Malaysia

Private sector financing was sustained in the fourth quarter

In the fourth quarter of 2016, total gross financing raised by the private sector through the banking system, development financial institutions (DFIs), and the capital market amounted to RM316.2 billion (3Q 2016: RM293.8 billion). On a net basis, the growth of outstanding banking system loans, DFIs, and corporate bonds moderated to 5.5% in the fourth quarter (3Q 2016: 6.5%), reflecting mainly the moderation in the growth of net outstanding corporate bonds amid higher growth of loans extended by the banking system and development financial institutions (DFIs) during the quarter. The moderation in the growth of outstanding corporate bonds was mainly due to the higher base recorded in December 2015 given large one-off issuances by a few companies.

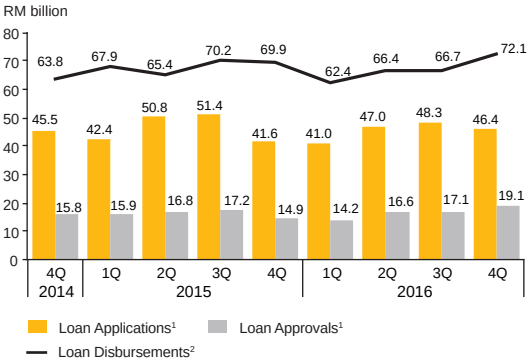
Net lending to businesses by the banking system and DFIs expanded by RM21.8 billion during the quarter (3Q 2016: RM7.8 billion). On an annual basis, outstanding business loans extended by the banking system and DFIs also grew strongly at 4.8% (3Q 2016: 2%). In addition, the amount of loans disbursed to businesses increased during the quarter with a higher level of credit extended mainly to the *finance, insurance, and business services; transport, storage and communication* and *real estate* sectors. Financing provided to SMEs also remained high, with outstanding SME loans recording an annual growth rate of 9% in 4Q 2016 (3Q 2016: 8.2%).

Gross Private Sector Financing through the Banking System, Development Financial Institutions (DFIs) and Capital Market



Source: Bank Negara Malaysia

Lending to SMEs



[1] Banking system only
[2] Banking system and DFIs

Source: Bank Negara Malaysia

Financing of the Private Sector through the Banking System, DFIs and Capital Market

	2015		2016			2015		2016		
	4Q	Year	3Q	4Q	Year	4Q	Year	3Q	4Q	Year
	During the period (RM billion)					Annual growth (%)				
Gross total financing	**342.0**	**1,224.8**	**293.8**	**316.2**	**1,193.7**	**7.3**	**1.3**	**-0.9**	**-7.5**	**-2.5**
Loans disbursed	293.9	1,123.4	263.6	296.2	1,102.3	-0.9	1.5	-6.6	0.8	-1.9
Gross Corporate bond (CB)[1]	40.6	83.5	27.0	19.2	84.3	91.4	1.2	128.0	-52.5	1.0
Equity	7.5	17.9	3.2	0.8	7.1	681.5	-6.5	28.0	-89.5	-60.4
Net total financing	**55.2**	**159.9**	**39.9**	**37.7**	**114.0**	**8.4**	**8.4**	**6.5**	**5.5**	**5.5**
Outstanding loans (Banking system* and Development Financial Institution (DFIs))	23.0	112.6	21.9	40.4	84.1	7.7	7.7	4.3	5.3	5.3
Outstanding CB	32.2	47.4	17.9	-2.7	29.9	10.7	10.7	14.2	6.1	6.1
Memorandum item										
Gross CB[2]	40.6	85.6	27.6	19.2	85.3	87.9	0.2	109.8	-52.5	-0.4

* Include loans sold to Cagamas
[1] Excluding Cagamas and foreign issuances
[2] Including Cagamas and foreign issuances
Note: Numbers may not add up due to rounding

Source: Bank Negara Malaysia

Loan Indicators

	During the period (RM billion)					Annual growth (%)				
	2015		2016			2015		2016		
	4Q	Year	3Q	4Q	Year	4Q	Year	3Q	4Q	Year
Total										
Loan applications[1]	215.6	827.2	204.0	198.6	802.8	2.6	0.6	-9.3	-7.9	-3.0
Loan approvals[1]	100.2	393.2	87.6	93.1	346.9	-5.8	-2.0	-9.2	-7.1	-11.8
Loan disbursements[2]	293.9	1,123.4	263.6	296.2	1,102.3	-0.9	1.5	-6.6	0.8	-1.9
Loan repayments[2]	276.6	1,060.2	257.9	279.2	1,078.4	3.4	3.1	-2.6	0.9	1.7
Change in outstanding loans*.[2]	23.0	112.6	21.9	40.4	84.1	7.7	7.7	4.3	5.3	5.3
Of which:										
Business enterprises[3]										
Loan applications	107.6	396.8	93.9	92.4	376.8	7.2	2.7	-16.9	-14.1	-5.0
Loan approvals	49.0	179.9	40.0	46.4	165.9	6.2	12.4	-9.1	-5.3	-7.8
Loan disbursements	212.1	804.8	187.1	217.8	796.0	-1.2	2.2	-8.9	2.7	-1.1
Loan repayments	205.7	777.9	185.2	206.7	786.2	4.4	3.5	-5.1	0.4	1.1
Change in outstanding loans*	5.4	41.9	7.8	21.8	28.0	7.7	7.7	2.0	4.8	4.8
SMEs										
Loan applications	41.6	186.2	48.3	46.4	182.7	-8.6	3.0	-5.9	11.5	-1.9
Loan approvals	14.9	64.8	17.1	19.1	66.9	-5.6	1.6	-0.9	28.0	3.1
Loan disbursements	69.9	273.3	66.7	72.1	267.6	9.6	14.4	-4.9	3.2	-2.1
Loan repayments	67.6	258.2	67.4	69.2	265.9	14.8	13.7	0.6	2.5	3.0
Change in outstanding loans*	5.9	35.0	4.9	8.6	24.6	14.6	14.6	8.2	9.0	9.0
Non-SMEs[3]										
Loan applications	66.0	210.6	45.5	46.1	194.1	20.3	2.5	-26.0	-30.2	-7.8
Loan approvals	34.1	115.0	22.9	27.3	99.1	12.3	19.6	-14.4	-19.8	-13.9
Loan disbursements	142.2	531.5	120.4	145.7	528.4	-5.7	-3.1	-10.9	2.4	-0.6
Loan repayments	138.2	519.7	117.8	137.4	520.3	0.0	-0.9	-8.1	-0.5	0.1
Change in outstanding loans*	-0.5	7.0	2.9	13.2	3.4	2.3	2.3	-3.3	1.1	1.1
Households										
Loan applications	108.0	430.4	110.1	106.2	426.0	-1.5	-1.3	-1.6	-1.7	-1.0
Loan approvals	51.2	213.4	47.6	46.7	181.0	-15.0	-11.6	-9.3	-8.9	-15.2
Loan disbursements	81.8	318.6	76.5	78.3	306.4	-0.3	-0.4	-0.5	-4.2	-3.8
Loan repayments	70.8	282.3	72.7	72.5	292.2	0.6	1.9	4.4	2.4	3.5
Change in outstanding loans*	18.4	63.8	12.1	16.1	49.2	7.6	7.6	5.8	5.5	5.5

* The annual growth is for end-period
[1] Loan applications and approvals for all segments include only banking system loans
[2] Loan disbursements, repayments and change in outstanding loan for all segments includes banking system and development financial institutions (DFIs)
[3] Includes domestic non-bank financial institutions, domestic financial institutions, government, domestic other entities and foreign entities
Note: Numbers do not add up due to rounding

Source: Bank Negara Malaysia

Loans by Sector (Banking System and DFIs)

	Loans disbursed						Outstanding Loans
	During the period (RM billion)					Share of total	Share of total
						(%)	
	4Q 2015	Year	3Q 2016	4Q 2016	Year		
Business enterprises[1,*]	**212.1**	**804.8**	**187.1**	**217.8**	**796.0**	**72.2**	**42.9**
Non-SMEs[1]	*142.2*	*531.5*	*120.4*	*145.7*	*528.4*	*47.9*	*25.0*
*SMEs**	*69.9*	*273.3*	*66.7*	*72.1*	*267.6*	*24.3*	*18.0*
Selected sectors[1]							
Agriculture, hunting, forestry and fishing	11.4	43.6	12.4	12.0	48.8	4.4	2.7
Mining and quarrying	6.2	21.3	2.2	2.3	8.4	0.8	0.8
Manufacturing	54.4	212.5	51.9	54.4	206.2	18.7	6.4
Construction	17.1	66.7	17.5	18.5	69.8	6.3	4.6
Real estate	13.3	53.4	13.4	16.2	56.9	5.2	6.6
Electricity, gas and water supply	2.8	9.8	2.0	2.3	9.3	0.8	0.8
Wholesale, retail, restaurants and hotels	54.0	203.6	50.7	53.2	204.2	18.5	7.0
Transport, storage and communication	4.4	23.7	5.6	10.3	29.8	2.7	2.7
Finance, insurance and business services	32.0	105.1	21.7	34.0	111.0	10.1	3.3
Households	**81.8**	**318.6**	**76.5**	**78.3**	**306.4**	**27.8**	**57.1**
Purchase of residential properties	21.9	85.3	18.8	20.1	78.9	7.2	27.7
Consumption credit	49.8	189.6	48.7	48.8	190.2	17.3	19.4
Of which:							
Credit cards	*27.5*	*103.7*	*27.2*	*28.3*	*108.0*	*9.8*	*2.2*
Purchase of passenger cars	*10.2*	*41.0*	*9.2*	*9.1*	*35.6*	*3.2*	*8.8*
Others	10.1	43.7	9.0	9.5	37.3	3.4	10.0
Total	**293.9**	**1,123.4**	**263.6**	**296.2**	**1,102.3**	**100.0**	**100.0**

* Include loans to individual businesses.
[1] Include domestic non-bank financial institutions, domestic financial institutions, government, domestic other entities and foreign entities.
Note: Numbers do not add up due to rounding

Source: Bank Negara Malaysia

Net financing to the household sector by the banking system and DFIs expanded by RM16.1 billion during the quarter (3Q 2016: RM12.1 billion). On an annual basis, the growth in outstanding household loans extended by the banking system and DFIs moderated to 5.5% in 4Q 2016 (3Q 2016: 5.8%), reflecting mainly the moderation in loans for the *purchase of passenger cars* and the *purchase of residential property*. Borrowers with the capacity to service their loans continued to have access to financing during the quarter.

Lower net financing from the capital market

Net funds raised in the capital market moderated to RM2.1 billion in the fourth quarter of 2016 (3Q 2016: RM13.5 billion). The decline was due mainly to lower net funds raised by the private sector.

In the private sector, gross corporate bond issuances were lower at RM19.2 billion (3Q 2016: RM27.6 billion) amid heightened market uncertainty and volatility during the fourth quarter. In addition, large redemptions amounting to RM22.1 billion (3Q 2016: RM10.0 billion), offset the issuances and resulted in net redemptions of RM2.8 billion

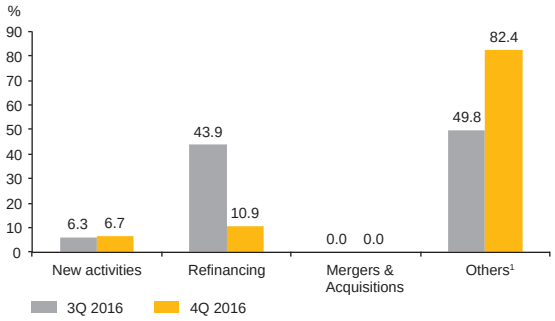
Net Funds Raised in the Capital Market

	2015		2016		
	4Q	Year	3Q	4Q	Year
	RM billion				
By Public Sector	**13.5**	**46.8**	**(7.2)**	**4.1**	**39.2**
Government securities, Gross	21.7	100.4	20.8	15.1	87.4
Malaysian Government Securities	10.9	51.3	11.9	3.9	44.1
Government Investment Issues	10.9	41.1	8.9	11.2	43.2
Sukuk Perumahan Kerajaan	-	8.0	-	-	-
Less: Redemptions	8.2	53.6	28.0	11.0	48.1
Malaysian Government Securities	8.2	41.1	24.0	-	26.1
Government Investment Issues	-	12.5	4.0	11.0	22.0
Sukuk Perumahan Kerajaan	-	-	-	-	-
By Private Sector	**37.9**	**62.8**	**20.7**	**(2.0)**	**35.2**
Shares	7.5	17.9	3.2	0.8	7.1
Corporate bonds, Net	30.5	44.9	17.5	(2.8)	28.1
Corporate bonds, Gross	*40.6*	*85.6*	*27.6*	*19.2*	*85.3*
Less: Redemptions	*10.1*	*40.8*	*10.0*	*22.1*	*57.2*
Total	**51.4**	**109.6**	**13.5**	**2.1**	**74.4**

Note: Numbers may not add up to total due to rounding

Source: Bank Negara Malaysia and Bursa Malaysia

Corporate Bond Issued by Purpose (% of total)



[1] Includes issuance for the purpose of capital expenditure, working capital and general business activities as well as issuance by non-residents and Cagamas

Source: Bank Negara Malaysia

in the fourth quarter (net funds raised in the 3Q 2016: RM17.5 billion). Funds raised in the private bond market were primarily from the *Finance, Insurance, Real Estate and Business Services* and were mainly used for the purpose of financing infrastructure projects, working capital and general business activities.

In the public sector, net funds raised were higher at RM4.1 billion during the fourth quarter (net funds raised in the 3Q 2016: -RM7.2 billion). The funds were raised through new issuances of 3-year Government Investment Issues (GII) as well as re-opening of 10-year and 20-year Malaysian Government Securities (MGS) and 7-year, 10-year, and 20-year GII. Government debt redemptions were lower at RM11 billion (3Q 2016: RM28 billion) during the quarter, contributing to the increase in net funds raised by the public sector.

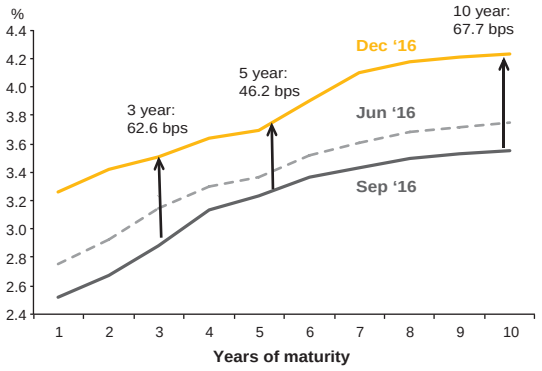
Bond yields increased in the fourth quarter

MGS yields trended upward in the fourth quarter of 2016, in line with global bond yields. This was driven by the redistribution of portfolio investments in favour of US dollar assets, especially equities, following the outcome of the US Presidential Elections. Expectations of an interest rate increase, the actual increase in the US Federal Reserve's policy rate in December 2016, and the anticipation of a faster pace of US interest rate normalisation in 2017 also led to spillover effects on bond yields globally, including the MGS yields. Non-resident investors reduced MGS holdings by RM12.9 billion during the quarter. As a result, the 3-year, 5-year and 10-year MGS yields increased by 62.6, 46.2 and 67.7 basis points, respectively. In the corporate bond market, the increase in yields was relatively contained amid low and stable non-resident holdings of corporate bonds and sustained demand by domestic investors.

Lower trading in the bond market

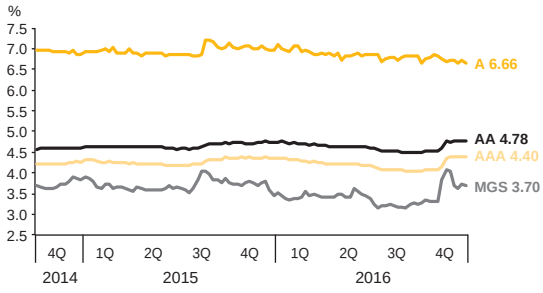
Total trading in the secondary market was lower at RM223.5 billion during the quarter (3Q 2016: RM269.1 billion) amid uncertainties arising from the outcome of US elections and as investors positioned for a higher probability of an increase in US interest rates. Correspondingly, all segments recorded lower liquidity ratios compared to previous quarter. The MGS, GII and corporate bond segments registered liquidity ratios of 0.36, 0.26 and 0.06, respectively.

Trend in MGS Yields



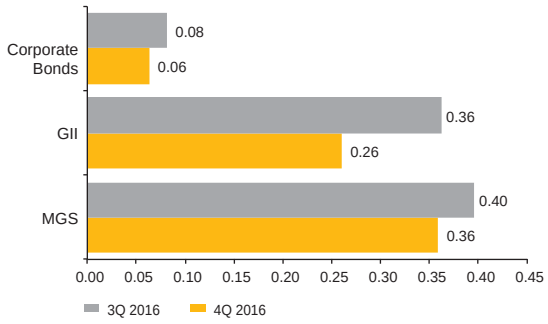
Source: Bank Negara Malaysia

5-year MGS and 5-year Corporate Bond Yields



Source: Bank Negara Malaysia

Liquidity Ratio: Value of Bonds Traded / Outstanding



Source: Bank Negara Malaysia

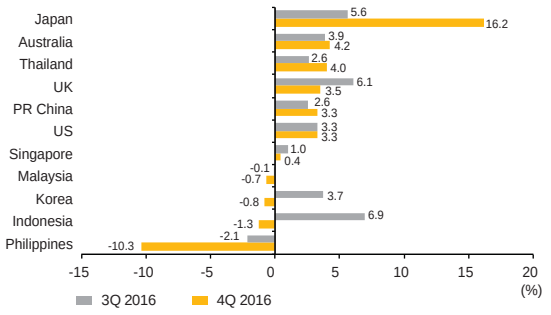
FBM KLCI declined during the quarter

During the fourth quarter of 2016, the FBM (FTSE Bursa Malaysia) KLCI declined by 0.7% to close at 1,641.7 points at end-December (end-September 2016: 1,652.6 points). During the quarter, the equity market was affected by market expectations of a tighter path for US interest rate normalisation. In addition, the uncertainties arising from the outcome of the US Presidential Election led to portfolio rebalancing by global investors, resulting in reduced holdings of Malaysian equity. The decline, however, was mitigated by improved market sentiments towards the end of the year amid gains in global oil prices following OPEC's agreement to cut output. Domestically, the index was also supported by positive sentiments created by the 2017 budget announcements and active buying of selected blue-chip stocks as investors consolidated their investment positions towards the end of the year.

Overall, market capitalisation decreased to RM1.67 trillion as at end-December 2016 (end-September 2016: RM1.69 trillion) while the daily average turnover decreased to 1.54 billion units (3Q 2016: 1.87 billion units) during the quarter.

On 14 February 2017, the KLCI ended higher at 1708.9 points (since end-December 2016: +4.1%), with a market capitalisation of RM1.75 trillion (since end-December 2016: +4.9%).

Performance of Selected Global and Regional Equity Markets in 2016 (% growth QoQ)



Source: Bloomberg and Bank Negara Malaysia calculations

Bursa Malaysia: Selected Market Indicators

	2015		2016		
	As at end				
	Dec	Year	Sep	Dec	Year
Price Indices					
Composite	1,692.5	1,692.5	1,652.6	1,641.7	1,641.7
FBMEMAS[1]	11,793.7	11,793.7	11,687.6	11,466.5	11,466.5
ACE Market[2]	6,389.2	6,389.2	5,219.9	4,780.7	4,780.7
Market capitalisation (RM billion)	1,695.2	1,695.2	1,686.2	1,667.4	1,667.4
No. of companies listed	903	903	905	904	904
	During the period				
	4Q	Year	3Q	4Q	Year
Average daily turnover					
Volume (million units)	2,234.0	2,038.3	1,870.0	1,540.5	1,762.9
Value (RM million)	2,149.7	2,082.2	1,876.7	1,931.0	1,963.8

[1] FBMEMAS stands for FTSE Bursa Malaysia EMAS Index
[2] From 3 August 2009, MESDAQ market was replaced with ACE Market

Source: Bursa Malaysia

Bursa Malaysia: Market Turnover

	2015				2016					
	4Q		Year		3Q		4Q		Year	
	Billion units	RM billion	Billion units	RM billion	Billion units	RM billion	Billion units	RM billion	Billion units	RM billion
Turnover	138.5	133.3	501.4	512.2	114.1	114.5	95.5	119.7	433.7	484.1
Of which:										
Main Board	82.5	121.4	299.1	464.6	73.2	107.8	65.0	114.2	289.8	457.9
Of which										
Consumer Products	7.0	6.8	26.9	25.6	4.9	6.1	4.4	5.9	26.2	26.3
Industrial Products	19.1	21.8	59.0	60.0	14.2	14.1	14.1	15.9	57.1	65.1
Construction	3.9	4.6	16.5	22.9	3.4	4.7	4.4	6.0	15.8	21.3
Trading/Services	32.4	51.3	124.7	204.3	31.9	47.4	25.7	47.8	119.3	194.7
Finance	2.9	17.7	12.8	79.6	4.1	18.2	4.0	21.9	14.8	83.7
Properties	7.5	5.0	23.7	18.9	4.6	4.9	3.4	3.4	19.9	15.0
Plantations	1.7	5.0	5.0	15.6	1.7	5.7	1.8	6.2	6.5	23.5
Infrastructure	1.0	4.3	4.2	18.8	0.7	2.5	0.7	2.6	2.9	11.0
ACE Market[1]	36.7	8.3	139.2	32.2	19.2	3.4	14.8	2.1	77.8	14.1

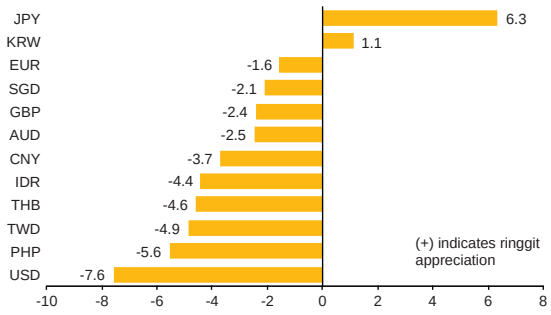
[1] From 3 August 2009, MESDAQ market was replaced with ACE Market

Source: Bursa Malaysia

Ringgit weakness driven primarily by external factors

The ringgit and all major and regional currencies depreciated against the US dollar during the quarter. The depreciation was driven mainly by portfolio investment outflows from emerging economies amid uncertainties arising from the outcome of the US Presidential Elections. Expectations of an interest rate increase, the actual increase in the US Federal Reserve's policy rate in December 2016, and the anticipation of a faster pace of US interest rate normalisation in 2017, exacerbated portfolio outflows and exerted further downward pressure on most major and regional currencies. The ringgit also faced additional adjustments during the quarter due to speculative activity in the non-deliverable forward (NDF) market. The ringgit, along with regional currencies, however, began to stabilise towards the end of the quarter amidst higher stability in the global financial markets. The implementation of measures to develop, deepen, and address the rising imbalances in the domestic foreign exchange market, and the firmer global crude oil prices also lent stability to the domestic foreign exchange market towards the end of the quarter.

Summary of Ringgit Performance against Selected Currencies
Percent Change (1 October - 30 December 2016)

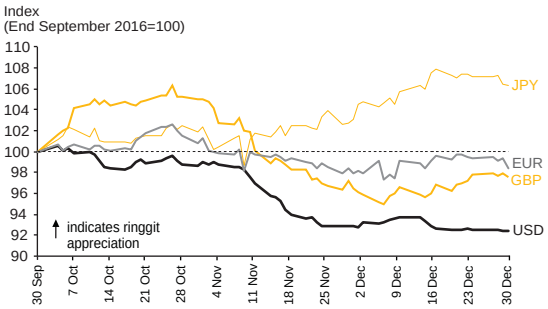


Source: Bank Negara Malaysia

Overall, the ringgit depreciated by 7.6% against the US dollar during the quarter. The ringgit also depreciated against the euro (-1.6%), the pound sterling (-2.4%) and the Australian dollar (-2.5%), but appreciated against the Japanese yen (6.3%). The ringgit also depreciated against all regional currencies, with the exception of the Korean won, by between 2.1% and 5.6%.

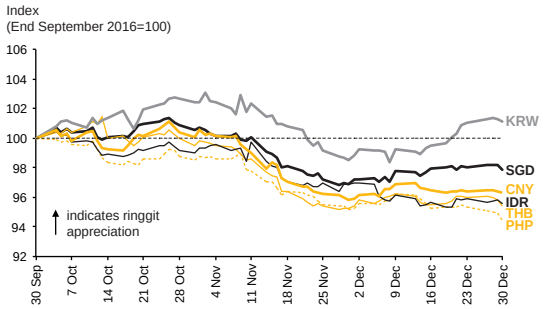
Between 1 January and 14 February 2017, the ringgit appreciated against the US dollar (0.8%). The ringgit also appreciated against the euro (0.1%), but depreciated against the pound sterling (-1.2%), the Japanese yen (-1.9%) and the Australian dollar (-5.0%). The ringgit depreciated against most regional currencies during the period.

Ringgit Performance against Major Currencies



Source: Bank Negara Malaysia

Ringgit Performance against Regional Currencies



Source: Bank Negara Malaysia

Performance of Ringgit against Selected Currencies

RM per foreign currency	As at end			% change since*	
	4Q 2015	3Q 2016	4Q 2016	4Q 2015	3Q 2016
US dollar	4.2920	4.1455	4.4860	-4.3	-7.6
Euro	4.6918	4.6500	4.7238	-0.7	-1.6
Pound sterling	6.3607	5.3775	5.5108	15.4	-2.4
Australian dollar	3.1338	3.1632	3.2436	-3.4	-2.5
100 Japanese yen	3.5645	4.0881	3.8442	-7.3	6.3
Singapore dollar	3.0356	3.0359	3.1016	-2.1	-2.1
100 Thai baht	11.922	11.943	12.517	-4.7	-4.6
100 Philippine peso	9.1494	8.5492	9.0516	1.1	-5.6
100 Indonesian rupiah	0.0311	0.0319	0.0334	-6.9	-4.4
100 Korean won	0.3651	0.3762	0.3720	-1.8	1.1
100 New Taiwan dollar	13.056	13.236	13.915	-6.2	-4.9
Chinese renminbi	0.6610	0.6215	0.6455	2.4	-3.7

* (+) indicates appreciation of ringgit against respective currency and (-) indicates depreciation.

Source: Bank Negara Malaysia

Foreign exchange derivatives activities were higher in the fourth quarter of 2016 as volatility in the financial market increased post US-Presidential election results mid-November

Foreign exchange derivatives volume was higher by 9.9% (3Q 2016: -11.1%) during the quarter compared to the same period in the previous year, contributed by higher volume of interbank FX swap (13.3%) and cross-currency interest rate swap (2.5%) transactions. The increase in interbank FX swap volumes was mainly attributed to the increase in demand for dollar following non-resident portfolio adjustments post-US Presidential results, interest rate hike by US Federal Reserve in December and year-end dollar liquidity requirements. The interbank FX swap activities also recorded 12% growth in 4Q 2016 from 3Q 2016 while volume of forward transactions was lower by 1% from the previous quarter.

The 5-year USD/MYR cross-currency interest rate swap widened to 68 bps from the previous quarter's closing of 55 bps. This was attributed to the high demand for US dollar liquidity in the domestic market, amidst expectation of the hike in the US interest rate.

MANAGING RISKS TO FINANCIAL STABILITY

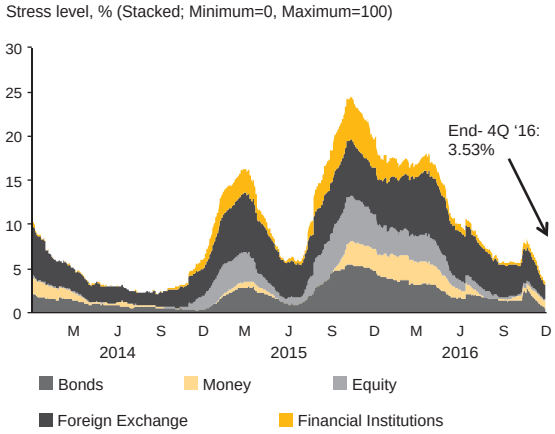
Domestic financial system remains resilient

The Malaysian financial system remains resilient despite global uncertainties over policy adjustments in the major economies. The domestic banking system remains well-capitalised, with ample liquidity to support the financing needs of businesses and households. As businesses and households continue to adjust to the challenging economic outlook and higher cost of living, these financial buffers will support the resilience of the financial institutions. Going forward, external events will continue to weigh heavily on the volatility in domestic financial markets. These include increased uncertainty over political developments and growth in the major economies as well as volatile commodity prices. Domestic financial system stability is nonetheless expected to be preserved given the loss absorption capacity of financial institutions supported by strong capital and liquidity buffers.

Domestic financial market conditions remained orderly

Global uncertainties emanating from the US presidential elections outcome, the timing and frequency of the US Federal Reserve interest rate normalisation and on-going volatility in the commodities market heavily influenced investor sentiments and behaviour throughout the quarter, particularly in November. Average volatility in the domestic financial markets was, nevertheless, lower in the final quarter, despite the slight uptick in the Financial Market Stress Index. In the MGS market however, average volatility for the 10-year yields edged higher (4Q 2016: 14.0%; 3Q 2016: 10.3%) following global re-pricing of sovereign bond yields after the US presidential elections.

Financial Market: Financial Market Stress Index (FMSI)



Note:
1. The FMSI is a risk monitoring tool for financial markets, developed based on the European Central Bank's (ECB's) Composite Indicators of Stress Index (CISS). It is constructed from indicators of volatility in five components of domestic financial markets - bonds, money, equity, foreign exchange and financial institutions.
2. The FMSI at a specific date is expressed as a value between 0 and 100, which signifies the lowest to highest stress level.

Source: Bloomberg and internal computation

Portfolio investments recorded a net outflow position of RM22.3 billion (3Q 2016: net outflow of RM 10.6 billion), driven mainly by non-resident outflows from the bond market. This reduced non-resident holdings to 32.1% (3Q 2016: 35.4%) of total outstanding MGS and GII at end of the year, with about 63% (3Q 2016: 58%) of the holdings maturing within the next five years. The 3-, 5- and 10-year MGS yields increased to 3.50%, 3.70% and 4.23%, respectively (3Q 2016: 2.88%, 3.24% and 3.55%, respectively) following an upward shift in the global bond yields. The FBM KLCI ended the quarter lower at 1641.73 points (3Q 2016: 1652.55 points), with non-resident holdings declining slightly to 22.3% (3Q 2016: 22.8%) of total market capitalisation.

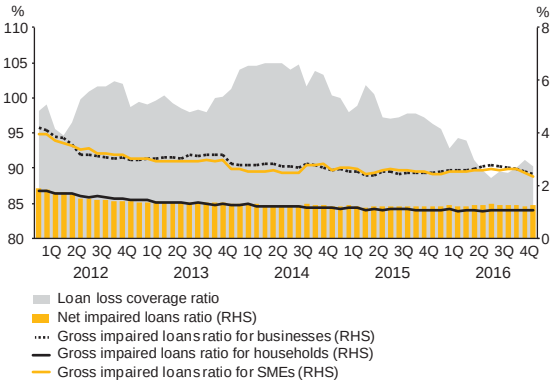
Trading liquidity in the markets were generally sustained with the monthly turnover ratio for MGS declining slightly to 11.8% (3Q 2016: 12.4%), while the equities market turnover ratio for FBM KLCI edged higher to 1.9% (3Q 2016: 1.7%). The bid-ask spreads were unchanged at 0.4% of mid-price for FBM KLCI, but increased slightly to 0.2% of mid-price for MGS.

In the currency market, pricing of the ringgit in the onshore market was influenced by the spillover from speculative activities in the offshore ringgit non-deliverable forward (NDF) market. This exacerbated adjustment in ringgit post the US presidential election, which saw the ringgit depreciating against the US dollar by 5.9% to RM 4.4680 by 1 December 2016. As-at 4Q 2016, the 5-year cross-currency basis swap spread had widened to 68 bps (3Q 2016: 55 bps), while the 5-year sovereign credit default swap spread had widened to 137.5 bps (3Q 2016: 122.4 bps). In November 2016, the Bank reinforced the existing rules on non-recognition of the ringgit NDF market to limit the spillover effects from the offshore market on the domestic foreign exchange (FX) market. In addition, several measures were introduced on 2 December 2016 to stabilise conditions in the financial markets. These include measures to promote the onshore hedging market and improve the depth and liquidity of the domestic FX market. While these measures will take some time to yield the desired effects, average volatility in the onshore ringgit market has eased (November 2016, December 2016 and January 2017: 7.5%, 6.4% and 5.4%, respectively). The ringgit further depreciated only by 0.4% to end the quarter at RM 4.4860 per US dollar (3Q 2016: RM4.1455). The 5-year cross-currency basis swap and sovereign credit default swap spread both eased to 58 bps and 131 bps, respectively, as at end-January.

Manageable credit risk exposures amid sustained debt servicing capacity

Credit risk exposures and asset quality of financial institutions remain intact, underpinned by sustained debt servicing capacity of borrowers. Loan delinquencies, measured by loans-in-arrears of between one and three months remained stable at 2.1% of total bank loans. Impairment ratio, net of individual impairment provisions, improved to 1.2% of net loans. Banks' loan loss coverage ratio[3] was ample at about 90.2% (3Q 2016: 89.4%). In addition, banks have also set aside regulatory reserves as buffers for potential credit losses on loans and financing portfolio. Credit exposures for insurance and takaful industry were largely unchanged at 4.1% (3Q 2016: 4%) of total capital available.

Banking System: Loan Quality



Source: Bank Negara Malaysia

Household debt continued to grow more moderately on an annual basis at 5.4% (3Q 2016: +5.8%; 4Q 2015: +7.3%) in the final quarter of the year. House financing, which grew by 9.1% (3Q 2016: +9.6%), remains the key driver of the increase in household debt amid sustained demand for affordable housing. The annual expansion in outstanding financing for personal use grew by 4.8% (3Q 2016: +5%). The debt repayment capacity of households remains supported by generally stable income and employment conditions, coupled with strengthened affordability assessments by lenders. About 74% of borrowers with newly approved loans have debt service ratios (computed based on income net of statutory deductions) of less than 60%. The share of total household debt borne by vulnerable borrowers[4] declined further to 22.2% (2015: 22.8%; 2014: 24.3%) of total bank and non-bank lending to households. For banks, the share is lower at 19.1% (2015: 19.6%; 2014: 20.9%).

The overall quality of lending to households by both banks and non-banks was generally sustained. Both aggregate impaired and delinquent loans ratios remained unchanged at 1.6% and 1.5%, respectively. The level of impairment for personal use increased, but remained low and stable at 2% (3Q 2016: 2%) of total personal financing. Higher delinquencies were due mainly to financial difficulties faced by borrowers who were affected by lower variable income and retrenchment by specific firms. However, the potential risks to domestic financial

[3] Refers to ratio of individual plus collective impairment provisions to total impaired loans.
[4] Defined as borrowers with a monthly income of less than RM3,000.

stability, particularly from vulnerable borrowers, remains mitigated amid the ample excess capital buffers of banks.

Credit conditions remained conducive with limited evidence of broad-based tightening in the supply of financing to businesses. Total borrowings grew annually by 6.2% (3Q 2016: +6%) for the fourth quarter of 2016. This increase was mainly contributed by fund raising from the bond and sukuk markets (+RM25 billion or +7.3%) and external borrowing (+RM15.5 billion or +5.2%). Outstanding bank financing to businesses expanded by 4.9% (3Q 2016: +2%) driven by higher disbursements to the transportation, real estate and manufacturing sectors. Financing to SMEs also sustained a robust growth of +9.2% (3Q 2016: +8.5%).

Financial health of firms remained intact despite the more challenging business climate. The aggregate leverage of Malaysian businesses[5], as measured by the median debt-to-equity ratio increased slightly to 44.2% (2Q 2016: 42.8%) as at end of the third quarter of 2016. This was supported by satisfactory debt servicing capacity and liquidity positions. The median interest coverage ratio (ICR) remained above prudent thresholds of two times, albeit moderating to 4.1 times (2Q 2016: 5.5 times). The moderation was driven by weaker profitability of firms in the food and beverage manufacturing and automotive industries. On aggregate, firms continued to maintain sufficient liquidity buffers to meet short-term obligations - the cash-to-short-term debt ratio (CASTD) has remained stable at 1.1 times. As expected, higher impairment and delinquencies were observed in the oil & gas (O&G), water transport, wholesale and retail, and infrastructure sectors. Overall, the ratio of impaired loans remained low at 2.4% (3Q 2016: 2.7%), while the ratio of delinquent loans increased slightly to 0.4% (3Q 2016: 0.3%) of total bank lending to businesses.

The outlook for the O&G and automotive sectors remained weak given expectations of persistent low levels of global crude oil prices and soft consumer spending. The overall median ICR of the O&G sector was sustained in 3Q 2016 at 1.2 times while CASTD declined to 0.7 times (2Q 2016: 0.9 times). Similarly, the debt servicing capacity and liquidity position for the automotive industry also weakened, with ICR and CASTD of 4.4 times and 1.1 times, respectively (2Q 2016: 9.3 times and 1.5 times, respectively). The impairment and delinquency ratios for the O&G sector were higher at 4.1% and 0.32%, respectively (3Q 2016: 1.8% and 0.01%, respectively). In the automotive industry, impaired and delinquent loans remained low and fairly stable at 0.4% and 0.01% of total bank lending to businesses. In terms of concentration risks, banks' exposures to the O&G-related and automotive sectors remain small at 3.1% and 0.8% of total exposures to businesses, respectively. Banks have gradually been increasing the level of provisions and regulatory reserves for collective impairment since 2015 to strengthen buffers against potential loss events.

The average annual growth of the Malaysian House Price Index (MHPI) for the first nine months of 2016 was lower at 6.4% compared to an average of 9.5% during 2010-2015. Primary and secondary housing markets remained soft across major states and house type amid cautious consumer sentiments. Against this backdrop, housing transactions in terms of volume and value declined by 13.9% to 49,640 units (2Q 2016: -12.5% to 52,487 units) and 12% to RM15.6 billion (2Q 2016: -9.7% to RM16.7 billion), respectively. Notwithstanding this, demand for affordable housing remains strong, supported by stable loan approval rates. Speculative activity in the housing market was subdued as the growth in the number of borrowers with three or more outstanding housing loans remained low and stable at 1.4% (3Q 2016: 1.6%).

Market risk exposures supported by risk management and hedging strategies

Banks' exposures to market risks were mainly in the form of FX risk. At end-December, FX net open position of banks declined to 6.2% (3Q 2016: 6.7%) of total capital, as banks continued to actively manage FX exposures amid ringgit

[5] Based on 160 companies listed on Bursa Malaysia with market capitalisation of 80% (excluding financial institutions) covering 10 key economic sectors.

volatility. Exposures to both interest rate risk in the trading book and equity risk remained low and accounted for only 1.1% and 0.8% of total capital, respectively (3Q 2016: 1.2% and 1.0%, respectively). For the insurance and takaful industry, market risk exposures were lower at 13.3% (3Q 2016: 14.4%) of total capital available, driven by improvement in interest rate risk. Equity risk, which forms the bulk of insurers' market risk exposures, rose slightly to 7.7% (3Q 2016: 7.6%) of total capital available.

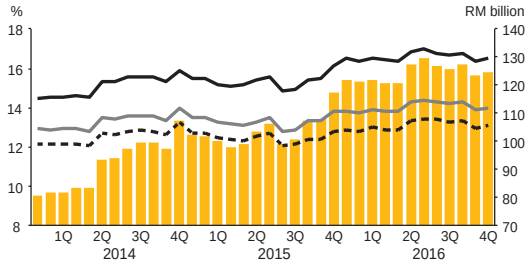
Sustained strength and resilience of financial institutions

Financial institutions remained well-capitalised. The combined capital buffers of banks, insurers and takaful operators stood at RM172.5 billion. Banks maintained a high level and quality of capitalisation. This is reflected in the high common equity tier-1, tier-1 and total capital ratios of banks which stood at 13.1%, 14.0% and 16.5%, respectively (3Q 2016: 13.3%, 14.2% and 16.7%, respectively). Similarly, the capital adequacy ratio for the insurance and takaful sectors remained high at 243.8% (3Q 2016: 226.3%).

Pre-tax profit of the banking system amounted to RM7.7 billion in the fourth quarter (3Q 2016: RM7.9 billion), with the growth in fee-based income partially offsetting the lower dividend income from subsidiaries, and trading and investment activities. Notwithstanding this, financing (including interest) margin net of operating costs and loss provisions improved to 0.6 percentage points (ppts) (3Q 2016: 0.58 ppts).

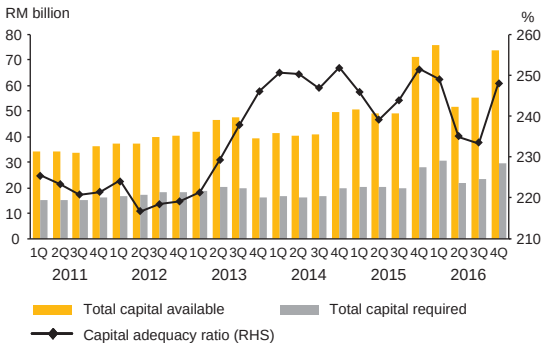
In the insurance and takaful sector, general insurers and takaful operators recorded higher operating profit of RM891.4 million in the fourth quarter of 2016 (3Q 2016: RM885.4 million), on account of higher investment income. Unlike the previous quarter where higher valuation in the bond market benefitted the life insurers and family takaful operators, the situation reversed in the fourth quarter due to the increase in bond yield. This explained the significant decrease of excess income over outgo to RM0.7 billion (3Q 2016: RM5.3 billion).

Banking System: Basel III Capitalisation



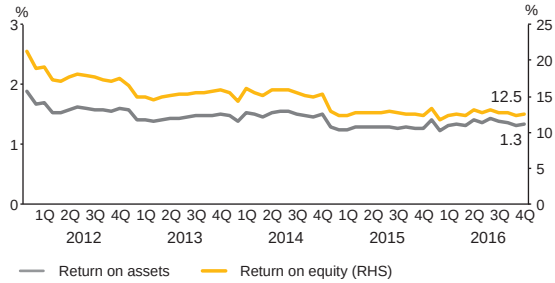
Source: Bank Negara Malaysia

Insurance Sector: Capitalisation



Source: Bank Negara Malaysia

Banking System: Profitability



Source: Bank Negara Malaysia

Insurance and Takaful Sectors: Indicators

	2015		2016		
	4Q	Year	3Q	4Q	Year
	RM million				
Life insurance & family takaful					
Excess of income over outgo	5,257	12,020	5,348	651	13,253
General insurance & general takaful					
Operating profit	679	2,698	885	891	3,406
Claims ratio (%)	60.6	60.2	56.4	56.9	56.0
	Annual change (%)				
Life insurance & family takaful					
Excess of income over outgo	148.2	-12.6	1,382.0	-87.6	10.3
General insurance & general takaful					
Operating profit	-10.6	-15.1	59.3	31.2	26.3
Claims ratio (percentage points)	1.1	2.7	-9.1	-3.7	-4.2

Source: Bank Negara Malaysia

Liquidity in the banking system remains ample to support intermediation activities. Total banking system placements, reverse repos and statutory reserves with Bank Negara Malaysia which can be unwound to meet liquidity needs, stood at RM179.9 billion. The banking system Basel III Liquidity Coverage Ratio (LCR)[6] stood at 124.8% as at end-December 2016, well above the current transitional minimum regulatory requirement of 70% (3Q 2016: 127%). About 80% of banks recorded LCR levels above 100%.

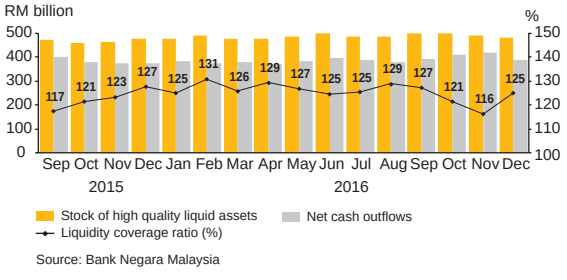
Domestic funding conditions remained stable during the quarter. Average cost of deposits for banks and the 3-month KLIBOR was stable at 2.6% and 3.4%, respectively. Banks' funding structure remained stable and predominantly deposit-based (69.4% of total funding) and in local currency. On aggregate, banking system deposits recorded a positive growth of 1.5% (3Q 2016: 0.8%). Household deposits continued to grow at a rate of 5.1% (3Q 2016: +4.6%), offsetting the decline in deposits from businesses (4Q 2016: -2.3%; 3Q 2016: -4.7%).

While the bulk of banks' funding remained in the form of deposits, banks continued to diversify their funding structure through the issuance of medium-term ringgit and foreign currency denominated funding instruments. The total net issuance of debt securities for 4Q 2016 amounted to RM4.8 billion (3Q 2016: RM0.3 billion). This contributed towards further reducing maturity and currency mismatches in the banks' funding structures.

Taking into account the broadened funding structure, the loan-to-funds ratio[7] (LTF) stood at 84.3% (3Q 2016: 83.4%) at the end of the quarter.

Net external liabilities of Malaysian banks stood at RM157 billion (2Q 2016: RM146 billion) as at end-3Q 2016, amid continued centralised liquidity management practices among Malaysian banks with related overseas entities. Some smaller locally incorporated foreign banks' (LIFB) have been gradually reducing intra-group placements with overseas parents to comply with the Single Counterparty Limit[8] (SCEL) requirement which comes into effect on 1 January 2017. The SCEL requirement on exposures with related banking entities has a two-year transition period to allow a gradual adjustment and to minimise the impact on the LIFBs' operations. Notwithstanding this, the structure of external exposures of Malaysian banking system has remained largely unchanged.

Banking System: Basel III Liquidity Coverage Ratio



Source: Bank Negara Malaysia

[6] The Basel III LCR has been phased in since June 2015, with initial compliance set at 60% and progressive increments of 10% each year until 100% with effect from 2019. As of 1 January 2017, the minimum requirement is set at 80%.

[7] Fund comprises deposits and all debt instruments (including subordinated debt, debt certificates/ sukuk issued, commercial papers and structured notes).

[8] The SCEL requirement limits exposures of a banking institution to a counterparty which is a related banking entity to 50% of the banking institution's total capital (subject to obtaining prior approval from the Bank).