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

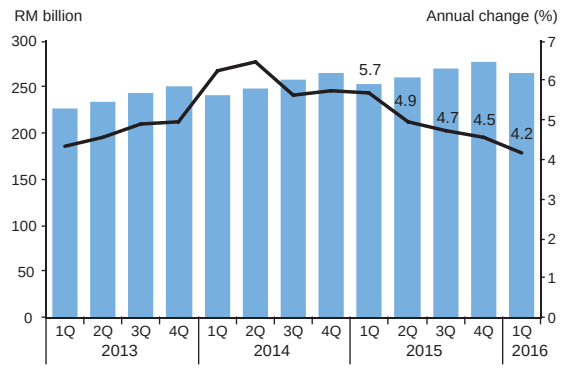
OVERVIEW

In the first quarter of 2016, the global economy expanded moderately against a backdrop of high financial market volatility. The advanced economies continued to register modest improvements, as the pace of growth remained constrained by crisis-related legacies, including high indebtedness and labour market slack. In Asia, economic activity expanded at a more moderate pace due in part to the weakness in exports. Amid these developments, several economies adopted more stimulus to support growth.

The Malaysian economy grew by 4.2% in the first quarter of 2016

The Malaysian economy expanded by 4.2% in the first quarter of 2016 (4Q 2015: 4.5%). The slight moderation in growth mainly reflected external shocks to the economy and cautious spending by the private sector. On the supply side, growth continued to be driven by the major economic sectors. On a quarter-on-quarter seasonally-adjusted basis, the economy recorded a growth of 1.0% (4Q 2015: 1.2%).

The economy expanded by 4.2% in the first quarter (at constant 2010 prices)



Source: Department of Statistics, Malaysia

Private sector activity remained the key driver of growth, although the pace of expansion moderated amid on-going adjustments in the economy. Private consumption expanded by 5.3% (4Q 2015: 4.9%), supported by continued wage and employment growth. Private investment grew at a slower rate of 2.2% (4Q 2015: 4.9%). This was mainly attributable to the cautious business sentiments and lower investments in the upstream mining sector. Growth of public consumption improved to 3.8% in the first quarter (4Q 2015: 3.3%) due to higher spending on emoluments. On the other hand, public investment declined by 4.5% (4Q 2015: 0.4%), due to lower spending on fixed assets by the public corporations.

On the supply side, the major economic sectors registered a moderate growth performance. The services sector recorded a sustained growth on account of the continued expansion in domestic demand. In the manufacturing sector, growth was supported by the continued expansion in both export- and domestic-oriented industries, although at a slower pace. The agriculture sector registered a contraction, as adverse weather conditions led to lower production of palm oil. The mining sector turned around to record a marginally positive growth following an improvement in the production of natural gas.

Inflation, as measured by the annual change in the Consumer Price Index (CPI), was higher at 3.4% in the first quarter of 2016 due to the reduction in electricity tariff rebates in January 2016 and the base effect from the larger decline in domestic fuel prices in the first quarter of 2015.

The trade surplus amounted to RM23.9 billion in the first quarter of 2016 (4Q 2015: RM30.6 billion). Gross exports continued to increase (1.0%; 4Q 2015: 8.1%), supported mainly by the continued expansion in manufactured exports, despite a larger contraction in commodity exports. Meanwhile, gross imports contracted marginally by 0.4% (4Q 2015: 3.5%), reflecting mainly the lower imports of capital and intermediate goods.

The international reserves of BNM amounted to RM381.6 billion (equivalent to USD97.0 billion) as at 31 March 2016.This reserves level has taken into account the quarterly adjustment for foreign exchange revaluation changes. As at 29 April 2016, the reserves position amounted to RM381.4 billion (equivalent to USD97.0 billion). The international reserves remain ample to facilitate international transactions. It is sufficient to finance 7.9 months of retained imports, significantly higher than the 3-month international threshold. The reserves level is also adequate to meet external obligations with the reserves to short-term external debt coverage of 1.2 times. It is important to note that not all short-term external debt creates an immediate claim on reserves given the external assets and export earnings of borrowers.

Interest rates remained stable

The Monetary Policy Committee (MPC) maintained the Overnight Policy Rate (OPR) at 3.25% during the first quarter of 2016. At the prevailing level of the OPR, monetary conditions remained supportive of economic activity. Interbank rates of longer maturities continued to be elevated in January, reflecting continued competition for stable funding and the uneven distribution of liquidity among banks. The reduction in the Statutory Reserve Requirement (SRR) effective 1 February 2016 provided a broad-based increase in the level of liquidity in the banking system. This resulted in greater interbank lending activity in the money market and reduced some of the pressure on the Kuala Lumpur Interbank Offered Rates (KLIBOR). The average base rate (BR) of banks at the end of the quarter increased slightly, reflecting the upward revision to the BR following the higher KLIBOR at the end of 2015.

M3, or broad money, increased by RM9.8 billion on a quarter-on-quarter basis to grow at an annual rate of 0.9% as at end-March (end-December 2015: 2.6%). The slower increase in M3 mainly reflected the moderation in credit extended to the private sector by the banking system. The level of surplus liquidity placed with BNM remained ample and was relatively stable during the quarter.

During the quarter, total gross financing raised by the private sector through the banking system and the capital market amounted to RM286.6 billion (4Q 2015: RM331.4 billion). On a net basis, outstanding banking system loans and PDS expanded by 7.6% as at end-March (end-December 2015: 8.6%). Outstanding business loans grew at a slower annual pace of 5.2% as at end-March (end-December 2015: 8.0%) due to the stronger growth in loan repayments relative to disbursements. The level of loans disbursed to businesses grew by 1.1% on an annual basis to RM191 billion during the quarter (4Q 2015: RM189 billion). Outstanding household loans growth moderated to 6.4% as at end-March (end-December 2015: 7.7%), reflecting mainly the moderation in loans *for the purchase of securities, purchase of non-residential property* and *credit card facility*. Net funds raised in the capital market moderated to RM25.4 billion in the first quarter (4Q 2015: RM51.4 billion), as higher public sector issuances were offset by lower private sector financing in both the debt and equity markets.

The ringgit and other regional currencies appreciated against the US dollar during the quarter, due to weaker-than-expected economic performance in the US, resulting in expectations of a slower pace of interest rate normalisation by the Federal Reserve. The ringgit, however, appreciated significantly more compared to other major and regional currencies. This is attributable to the release of positive domestic economic data, the recovery of Brent crude oil prices and the 2016 Budget Recalibration announcement. These factors lifted investor sentiments on the Malaysian economy and led to increased demand for ringgit financial assets.

Overall, the ringgit appreciated by 9.4% against the US dollar during the quarter. The ringgit also appreciated against the pound sterling (13.1%), the euro (5.7%), the Australian dollar (4.4%), and the Japanese yen (2.2%). Against all regional currencies, the ringgit also appreciated by between 4.6% and 9.0%.

Domestic financial stability continued to be preserved

The Malaysian financial system remained resilient against potential risks related to spillovers from the weaker global growth and continued volatility in the international financial and commodity markets. Domestic risks more broadly have continued to moderate. However, more challenging business conditions and rising costs will likely weigh on the revenue and loan performance of financial institutions in the period ahead, requiring higher vigilance. The sound underwriting practices observed by financial institutions will continue to lend firm support to domestic financial intermediation. Ample liquidity in the banking system has continued to support credit growth and orderly market conditions. Debt servicing capacity of most borrowers remained intact, with net impaired loans remaining steady at 1.2% of total bank loans.

The capitalisation of financial institutions remained strong and is sufficient to absorb potential losses from adverse developments in financial and economic conditions. For banks, the common equity tier-1 capital, tier-1 capital and total capital ratios of banks were sustained well above the minimum regulatory levels at 13.0%, 13.9% and 16.5%, respectively. The capital adequacy ratio for the insurance and takaful sectors remained healthy at 242.6% (4Q 2015: 245.4%). Financial institutions are well-positioned to withstand any adverse macroeconomic and financial shocks, with combined capital buffers of RM170.4 billion as at end first quarter of 2016 (banks: RM121.9 billion; insurers and takaful operators: RM48.5 billion).

Domestic demand will remain the key driver of growth

Overall, downside risks to the global economy remain elevated. Cyclical and structural economic weaknesses continue to weigh on growth in the major economies, in addition to uncertainty in the direction of energy prices and rising geopolitical risks. Looking ahead, although the global economy is projected to improve, the pace of expansion is expected to be moderate and uneven. In most of Asia, growth will be underpinned by domestic demand with continued policy support.

Going forward, the Malaysian economy is expected to remain on a sustained growth path of 4-4.5%, despite the challenging economic environment globally and domestically. Domestic demand will continue to be the principal driver of growth, sustained primarily by private sector spending. However, domestic consumption is expected to grow at a moderate pace as households continue to adjust to the higher cost of living. Overall investment is also expected to grow at a slower pace but will remain supported by the implementation of infrastructure development projects and capital spending in the manufacturing and services sectors. Uncertainties in the external environment and the on-going adjustments in the domestic economy pose downside risks to growth.

DEVELOPMENTS IN THE FIRST QUARTER OF 2016

INTERNATIONAL ECONOMIC ENVIRONMENT

Moderate global growth

In the first quarter of 2016, the global economy expanded moderately against a backdrop of high financial market volatility. The advanced economies continued to register modest improvements, as the pace of growth remained constrained by crisis-related legacies, including high indebtedness and labour market slack. In Asia, economic activity expanded at a more moderate pace due in part to the weakness in exports. Amid these developments, several economies adopted more stimulus to support growth.

Global financial conditions were volatile during the quarter, particularly at the start of the year, from a confluence of factors. The unexpected adjustments in PR China's currency and equities, amid weaker Chinese economic data, led to heightened concerns over the health of the Chinese economy and the potential spillovers to the rest of the world. Additionally, the decline of the Brent crude oil prices to a 12-year low (USD28 per barrel) also dampened investor sentiments. In the euro area, financial markets were affected by concerns that the introduction of negative interest rates and weak global growth would undermine the health of Europe's banking sector. The adoption of negative interest rates policy by the Bank of Japan also contributed to an increase in market volatility. As a result, credit spreads widened and equity markets fell across major and regional financial markets. Nevertheless, equity markets in the major and regional economies rose in the second half of the quarter, which offset earlier declines in several economies. The improvement was supported by a modest rebound in oil prices and Chinese policymakers' comments on more accommodative policy and exchange rate stability. The Federal Reserve's announcement of more gradual monetary policy adjustments on 16 March 2016 also contributed to the improvement in market sentiments. Against this backdrop, most major and regional currencies ended the quarter higher against the US dollar.

Brent crude oil prices declined to an average of USD35 per barrel in the first quarter of 2016 (4Q 2015: USD45 per barrel) as excess supply and elevated inventory build-up continued. In January, sentiments in the markets were weighed down by worsening oversupply in the oil market following the lifting of international sanctions on Iran on 16 January 2016. Financial market volatility in PR China was also a key factor in causing prices to hit a 12-year low of USD 28 per barrel on 20 January 2016. However, the oil market recovered slightly towards the end of the quarter due to improved sentiments following the news of an agreement by OPEC and Russia to meet in Doha, Qatar on 17 April 2016 to discuss a plan to freeze oil output from both parties. In addition, the continued fall in oil rig count in the US and news of project deferments and job cuts in the US shale oil industry reinforced expectations of lower US oil production that could support prices in the coming months. Brent crude oil prices reached a 4-month high of USD42 per barrel on 22 March 2016, eventually ending the quarter at USD 40 per barrel.

In the US, economic activity was sustained at 2.0% in the first quarter, supported by private consumption and government spending. However, on a seasonally adjusted annualised basis, the overall growth momentum slowed to 0.5% (4Q 2015: 1.4%). The moderation in growth was observed in all major components of growth except government spending. While private consumption remained a key contributor to growth, demand was weighed down by durable goods, which turned negative due mainly to motor vehicles and parts. The slower momentum in fixed investment was attributable mainly to weaker capital spending in structures and equipment. Net exports were a larger drag on growth as exports recorded negative growth for the second consecutive quarter (-2.6%) while imports grew by 0.2%. During the quarter, headline inflation moved closer to the target rate of 2.0% with a 1.1% increase (4Q 2015: 0.5%), due mainly to the rise in the cost of medical care and transportation services.

The euro area economy expanded by 1.6%, according to preliminary estimates. On a seasonally-adjusted quarter-on-quarter basis, growth improved to 0.6%, from 0.3% in the

fourth quarter 2015. Economic activity was underpinned by growth in household consumption and gradual improvements in the labour market. Overall business sentiments were weaker but remained positive, with the manufacturing PMI declining slightly to 51.8 (4Q 2015: 52.8). On the external front, exports contracted marginally (Jan. - Feb. 2016 average: -0.4%, 4Q 2015: 3.4%), following lower shipments of raw materials and manufactured products. Deflationary pressures increased during the quarter as headline inflation declined to 0% (4Q 2015: 0.2%) while core inflation remained low at 1.0%. following a broad-based moderation across industries.

The UK economy expanded at a sustained pace of 2.1% in the first quarter. The services sector continued to be the key contributor to growth, particularly the business services and finance sub-sectors. Labour market conditions remained favourable, as employment continued to grow at a strong pace, while the unemployment rate remained low. Headline inflation rose slightly to 0.3% (4Q 2015: 0.1%), as a result of higher prices for housing and household expenditures.

Meanwhile, overall economic activity in Japan remained weak. Business sentiments were weaker, as indicated by the Tankan survey index for large manufacturers (6.0%, 4Q 2015: 12.0%) while industrial production declined (-3.3%, 4Q 2015: -1.1%). In terms of external demand, exports contracted further, mainly due to slower demand growth in most of its key trading partners. Nevertheless, consumer spending experienced a slight improvement as real wages recorded a positive growth of 1.6% in the first quarter, after a contraction in 2015. Headline inflation (excluding fresh food) declined slightly to -0.1% (4Q 2015: 0%) while core inflation (excluding food and energy) was sustained at 0.7%.

Advanced Economies: Real GDP Growth

	2015			2016
	1Q	4Q	Year	1Q
UK	2.6	2.1	2.3	2.1[p]
US	2.9	2.0	2.4	2.0[a]
Euro area	1.3	1.6[r]	1.6[r]	1.6[p]

[a] Advance estimate
[p] Preliminary estimate
[r] Revised

Source: National authorities

Monetary policy in the advanced economies remained highly accommodative during the quarter, with most central banks in the advanced economies conducting further easing. The European Central Bank (ECB) lowered interest rates on the main refinancing operations and the marginal lending facility by 5 basis points to 0.00% and 0.25% respectively. The ECB also further reduced the deposit rate by 10 basis points to -0.4% and started increasing asset purchases by EUR20 billion to EUR80 billion per month as well as extending the period of the asset purchases to at least March 2017. A new series of four targeted long-term loans to banks (TLTRO II) was also announced. Additionally, beginning June 2016, the ECB will start the corporate sector purchase programme (CSPP), an expansion to the type of assets purchased under its current programme. Under the CSPP, the ECB will purchase investment-grade euro-denominated bonds issued by euro area's non-bank corporations. It is intended to further strengthen the effectiveness of its asset purchases programme. Meanwhile, in an unanticipated move, the Bank of Japan (BOJ) introduced "Quantitative and Qualitative Monetary Easing (QQE) with a Negative Interest Rate" on 29 January 2016. Of significance, the interest rate on deposits that financial institutions hold at the BOJ was reduced from 0.1% to -0.1%. Likewise, the Swedish Riksbank and Reserve Bank of New Zealand lowered their key policy rates by 15 basis points to -0.5% (official cash rate) and by 25 basis points to 2.25% (main repo rate), respectively. In the other advanced economies, central banks in the US, Australia and Canada reiterated their commitment to maintain accommodative monetary conditions and kept their policy rates unchanged during the quarter. In particular, the Federal Reserve in March projected a more gradual pace of normalisation, with an estimated 50 basis points increase in the interest rate by the end of the year (Dec. 2015: 100 basis points).

The Chinese economy grew at a moderate pace of 6.7% in the first quarter (4Q 2015: 6.8%). Economic activity continued to be affected by the unwinding of excess capacity in key industries and the weakness in external demand. In view of rising downside risks to growth, the Chinese Government implemented

a series of wide-ranging policy measures. These included the easing of house purchase restrictions and higher infrastructure investment. The People's Bank of China (PBOC) also eased monetary policy through liquidity injections into the interbank market and lowered the reserve requirement ratio to support liquidity conditions. Meanwhile, inflation increased to 2.1% (4Q 2015: 1.5%) due to higher prices in the food and healthcare sub-sectors.

In several other Asian economies, economic activity moderated amid continued weakness in external demand. In Indonesia, growth was slightly lower at 4.9% (4Q 2015: 5.0%) due to more moderate investment activity. The Korean economy expanded at a slower pace of 2.7% (4Q 2015: 3.1%), as growth was weighed down by a moderation in private consumption, investment and exports. Growth in Singapore remained modest at 1.8% (4Q 2015: 1.8%). An improvement in construction activity was offset by a moderation in growth in the manufacturing and services sectors. Meanwhile, growth in Chinese Taipei recorded a sharper contraction of 0.8% (4Q 2015: -0.5%), as investment and exports declined at a faster pace, offsetting the improvement in private consumption.

Regional Countries: Real GDP Growth

	2015			2016
	1Q	4Q	Year	1Q
	Annual change (%)			
PR China	7.0	6.8	6.9	6.7
Indonesia	4.7	5.0	4.8	4.9
Korea	2.4	3.1	2.6	2.7[a]
Singapore	2.7	1.8	2.0	1.8[a]
Chinese Taipei	4.0	-0.5	0.7	-0.8[a]

[a] Advance estimate

Source: National authorities

Inflation increased in several Asian economies. Food prices grew at a faster pace due to lower supply caused by colder weather conditions and higher seasonal demand during the Lunar New Year festival period. In addition, inflation rose in Chinese Taipei as the effect from the electricity rate refund plan which was implemented for households in 2015 diminished, leading to higher growth in the cost of utilities. However, Singapore and Thailand remained in deflation, reflecting mainly the lower cost of housing and transportation.

In this environment, the monetary policy stance remained accommodative across the regional economies, with a few central banks lowering their key policy rates during the quarter. Bank Indonesia lowered its key policy rate by a cumulative 75 basis points from 7.50% to 6.75% to support economic activity, as domestic inflationary pressures eased. In March, the Central Bank of the Republic of China (Taiwan) lowered its key policy rate by 12.5 basis points to 1.50% from 1.625%, noting that the modest economic recovery faced headwinds from the external environment. In contrast, to deter offshore speculation of the renminbi, the People's Bank of China tightened offshore renminbi liquidity by implementing a reserve requirement ratio of 17.5% on banks' offshore renminbi deposits.

Overall, downside risks to the global economy remain elevated. Cyclical and structural economic weaknesses continue to weigh on growth in the major economies, in addition to volatility of energy prices and rising geopolitical risks. Looking ahead, although the global economy is projected to improve, the pace of expansion is expected to be moderate and uneven. In most of Asia, domestic demand will continue to drive growth amid policy support.

DEVELOPMENTS IN THE MALAYSIAN ECONOMY

The Malaysian economy grew by 4.2% in the first quarter

The Malaysian economy expanded by 4.2% in the first quarter of 2016 (4Q 2015: 4.5%). The slight moderation in growth mainly reflected external shocks to the economy and cautious spending by the private sector. Nevertheless, private sector expenditure remained the key driver of growth (4.5%; 4Q 2015: 4.9%). Net exports contributed negatively to growth during the quarter following a decline in real exports of goods and services (-0.5%; 4Q 2015: +4.0%) amid continued positive growth in real imports (1.3%; 4Q 2015: 4.0%). On a quarter-on-quarter seasonally-adjusted basis, the economy recorded a growth of 1.0% (4Q 2015: 1.2%).

Slower expansion in domestic demand

Domestic demand grew by 3.6% in the first quarter of the year (4Q 2015: 4.0%), with private sector expenditure expanding at a slower pace of 4.5% (4Q 2015: 4.9%). **Private consumption** growth expanded by 5.3% (4Q 2015: 4.9%), supported by continued wage and employment growth. **Private investment** registered a slower growth of 2.2% in the first quarter (4Q 2015: 4.9%). The cautious business sentiments and lower commodity prices continued to weigh down on investments in the upstream mining sector. Nevertheless, there was continued investment in the manufacturing and services sectors.

Public consumption growth improved to 3.8% (4Q 2015: 3.3%), as a result of higher spending on emoluments. On the other hand, **public investment** declined by 4.5% (4Q 2015: 0.4%), due to lower spending on fixed assets by public corporations, particularly in the oil and gas and transportation sectors, which more than offset higher investment by the Federal Government.

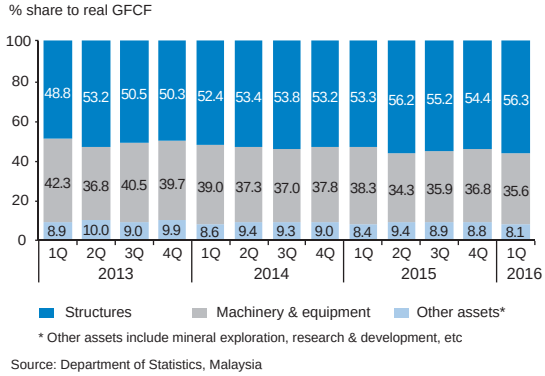
GDP by Expenditure Components
(at constant 2010 prices)

	Share 2015 (%)	2015			2016
		1Q	4Q	Year	1Q
		Annual change (%)			
Aggregate Domestic Demand (excluding stocks)	91.6	8.0	4.0	5.1	3.6
Private Sector	69.2	9.6	4.9	6.1	4.5
Consumption	*52.4*	*9.0*	*4.9*	*6.0*	*5.3*
Investment	*16.9*	*11.6*	*4.9*	*6.4*	*2.2*
Public Sector	22.4	2.6	2.1	2.1	0.4
Consumption	*13.5*	*4.1*	*3.3*	*4.4*	*3.8*
Investment	*8.9*	*0.6*	*0.4*	*-1.0*	*-4.5*
Net Exports	8.6	-10.1	4.3	-3.8	-12.4
Exports of Goods and Services	*72.9*	*-0.6*	*4.0*	*0.6*	*-0.5*
Imports of Goods and Services	*64.3*	*0.9*	*4.0*	*1.2*	*1.3*
GDP	**100.0**	**5.7**	**4.5**	**5.0**	**4.2**
GDP (q-o-q growth, seasonally adjusted)	**-**	**1.4**	**1.2**	**-**	**1.0**

Source: Department of Statistics, Malaysia

In terms of total investment, **gross fixed capital formation (GFCF)** growth moderated to 0.1% (4Q 2015: 2.7%), following a slower growth in private investment and a decline in public investment. By type of assets, the lower growth in GFCF was due to a larger contraction of investment in machinery and equipment (-7.1%; 4Q 2015: -0.1%), which more than offset the improvement in structures investment (5.7%; 4Q 2015: 5.0%).

GFCF by Type of Assets



* Other assets include mineral exploration, research & development, etc

Source: Department of Statistics, Malaysia

Moderate growth in major economic sectors

On the supply side, the major economic sectors registered a moderate growth during the first quarter. The services sector recorded a sustained growth, supported by the continued expansion in domestic demand. In the manufacturing sector, growth was supported by both export- and domestic-oriented industries, albeit at a slower pace. Growth in the agriculture sector contracted, as adverse weather conditions led to a lower production of palm oil. The growth in construction remained strong, driven mainly by the civil engineering sub-sector. The mining sector turned around to record a marginally positive growth, following an improvement in the production of natural gas.

The **services sector** registered a sustained growth of 5.1% in the first quarter of 2016 (4Q 2015: 5.0%), supported by domestic demand. The wholesale and retail trade sub-sector grew by 5.2% (4Q 2015: 6.4%), in tandem with continued growth in household spending. Growth of the information and communication sub-sector remained robust (8.5%; 4Q 2015: 9.2%), benefitting from sustained demand for data communication services. The utilities sub-sector recorded stronger growth of 6.7% (4Q 2015: 3.2%), following higher consumption of electricity during the quarter. The real estate and business services sub-sector expanded by 6.4% (4Q 2015: 6.1%), supported mainly by the business services segment. The transport and storage sub-sector grew by 5.8% (4Q 2015: 6.0%) in line with the continued expansion in trade-related activities. The finance and insurance sub-sector registered a positive growth of 0.1% (4Q 2015: -1.5%), due mainly to improvements in net interest income and fee income.

GDP by Economic Activity (at constant 2010 prices)

	Share 2015 (%)	2015			2016
		1Q	4Q	Year	1Q
		Annual change (%)			
Services	53.5	6.4	5.0	5.1	5.1
Manufacturing	23.0	5.6	5.0	4.9	4.5
Mining	9.0	9.7	-1.3	4.7	0.3
Agriculture	8.9	-4.1	1.5	1.2	-3.8
Construction	4.4	9.6	7.4	8.2	7.9
Real GDP	**100.0[1]**	**5.7**	**4.5**	**5.0**	**4.2**
Real GDP (q-o-q seasonally adjusted)	**-**	**1.4**	**1.2**	**-**	**1.0**

[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 2015 (%)	2015			2016
		1Q	4Q	Year	1Q
		Annual change (%)			
Intermediate Services	**38.2**	**5.7**	**4.1**	**4.6**	**4.7**
Finance & insurance	12.9	1.9	-1.5	-0.7	0.1
Real estate & business services	8.0	7.5	6.1	6.6	6.4
Transport & storage	6.6	5.7	6.0	5.7	5.8
Information & communication	10.6	9.6	9.2	9.4	8.5
Final Services	**61.8**	**6.8**	**5.4**	**5.5**	**5.3**
Wholesale & retail trade	27.4	9.8	6.4	6.9	5.2
Food & beverages and accommodation	5.2	7.3	5.8	6.4	6.1
Utilities	4.8	3.7	3.2	3.5	6.7
Government services	16.3	3.8	4.7	4.0	5.3
Other services	8.2	4.6	4.6	4.7	4.6
Total Services	**100.0[1]**	**6.4**	**5.0**	**5.1**	**5.1**

[1] Numbers do not add up due to rounding

Source: Department of Statistics, Malaysia

Selected Quarterly Indicators in the Services Sector

	2015			2016
	1Q	4Q	Year	1Q
	Index			
MIER Consumer Sentiments Index	72.6	63.8	69.6	72.9
MIER Retail Trade Index	85.4	77.9	83.4	65.9
MIER Tourism Market Index	100.7	89.8	97.9	93.0
	Annual change (%)			
Tourist arrivals	-8.6	-2.3	-6.3	n.a
Total passenger traffic at all airports	-0.8	-3.0	0.9	5.9[1]
Total consumption credit outstanding	3.5	3.1	3.1	1.9
Total loans outstanding	9.2	7.9	7.9	6.4
Loans outstanding to the wholesale & retail trade, hotels & restaurants	9.3	8.2	8.2	7.0
Imports of consumption goods	4.4	38.3	24.1	24.6
Total sales of motor vehicles	5.3	4.1	0.0	-22.0
Container cargo handled (Port Klang and PTP)	12.9	5.4	7.9	6.7[1]

[1] Jan-Feb 2016

Source: Various sources

The **manufacturing sector** continued to expand during the quarter (4.5%; 4Q 2015: 5.0%), supported by both domestic- and export-oriented industries. Growth in the domestic-oriented industries was driven by stronger production in the consumer-related cluster, particularly food-related products, as well as firm demand for construction-related materials. Meanwhile, the export-oriented industries were supported by the better performance in the primary-related cluster amid continued expansion in the electrical and electronics (E&E) cluster.

Performance of the Manufacturing Sector

	2015			2016
	1Q	4Q	Year	1Q
	Annual Change (%)			
Value Added (at constant 2010 prices)	**5.6**	**5.0**	**4.9**	**4.5**
Export-oriented industries	7.0	5.4	5.6	4.5
Domestic-oriented industries	2.9	4.1	3.7	4.6
Overall Manufacturing Production[1]	**5.7**	**4.8**	**4.8**	**4.3**
Export-oriented industries	**5.1**	**4.7**	**4.8**	**4.2**
Electronics and electrical products cluster	**10.7**	**10.7**	**9.2**	**5.9**
Of which:				
Electronics	-0.2	5.7	0.7	6.0
Electrical products	40.5	24.7	32.1	6.4
Primary-related cluster	**2.2**	**1.5**	**2.5**	**3.2**
Of which:				
Chemicals and chemical products	9.9	1.9	4.6	3.3
Petroleum products	2.1	-0.2	1.2	1.2
Rubber products	-1.3	7.0	5.1	6.9
Off-estate processing	-20.2	-1.9	-3.5	2.7
Domestic-oriented industries	**7.6**	**5.0**	**4.7**	**4.6**
Construction-related cluster	**6.9**	**4.8**	**4.5**	**4.9**
Of which:				
Construction-related products	8.1	3.7	4.5	4.7
Fabricated metal products	4.7	6.9	4.6	5.4
Consumer-related cluster	**8.3**	**5.1**	**4.8**	**4.2**
Of which:				
Transport equipment	9.2	3.7	5.2	2.0
Food, beverage & tobacco products	7.5	7.4	4.8	7.3

[1] Industrial Production Index (2010=100)

Source: Department of Statistics, Malaysia

The **construction sector** grew by 7.9% in the first quarter (4Q 2015: 7.4%), underpinned by the civil engineering sub-sector. The expansion of the civil engineering sub-sector was driven by petrochemical, utility and transport-related projects. Growth in the specialised construction activities sub-sector improved during the quarter, reflecting increased early-work activities such as demolition, piling and earthworks. In the non-residential sub-sector, the pace of expansion was subdued due to slower construction activity for industrial and commercial buildings. In the residential sub-sector, growth remained supported by the construction of properties in both the mass- and high-end markets.

Indicators for the Construction Sector

	2015			2016
	1Q	4Q	Year	1Q
	Annual change (%)			
Value of construction work done	15.1	11.2	12.1	11.1
Residential	19.5	8.7	10.9	8.4
Non-residential	24.3	3.6	13.9	3.8
Civil engineering	4.2	23.3	11.9	21.3
Special trade[1]	4.2	4.4	8.0	17.3
Housing approvals	-24.2	-18.5	-25.3	-22.1
Production[2] of construction-related materials				
Hydraulic cement	20.2	11.9	14.8	-7.9
Other articles of concrete, cement and plaster n.e.c	20.9	-15.3	3.4	-8.9
Other porcelain and ceramic products	31.2	12.2	20.0	0.7
Prefabricated structural components for building or civil engineering of cement, concrete or artificial stone	-13.3	21.1	-2.2	21.7
Capital imports (excluding lumpy items)	11.3	3.1	4.8	-8.1
Loans for the construction sector				
Approval	21.4	-5.5	3.8	0.4
Disbursement	3.2	-13.4	-0.6	-2.8

[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

Growth in the agriculture sector contracted by 3.8% (4Q 2015: 1.5%), reflecting mainly lower production of palm oil as the El Niño weather phenomenon affected crop yields. Meanwhile, growth in the **mining sector** turned around to record a marginally positive growth of 0.3% (4Q 2015: -1.3%) following an improvement in the production of natural gas.

Performance of the Agriculture Sector

	Share in 2015 (%)	2015			2016
		1Q	4Q	Year	1Q
		Annual change (%)			
Value Added (at constant 2010 prices)	**100**	**-4.1**	**1.5**	**1.2**	**-3.8**
Industrial Crops	**61.0**	**-9.3**	**1.7**	**0.7**	**-9.2**
Of which:					
Oil palm	46.9	-11.7	1.2	1.3	-10.0
Rubber	7.2	4.8	26.9	8.1	-13.0
Food Crops	**39.0**	**4.0**	**1.2**	**2.0**	**3.5**
Of which:					
Fishing	10.7	4.4	2.4	0.6	-2.1
Livestock	10.7	4.3	0.4	2.4	5.0

Source: Department of Statistics, Malaysia

Performance of the Mining Sector

	2015			2016
	1Q	4Q	Year	1Q
	Annual change (%)			
Value Added (at constant 2010 prices)	**9.7**	**-1.3**	**4.7**	**0.3**
Production				
Of which:				
Crude oil and condensates	20.3	0.2	10.1	-0.3
Natural gas	-1.3	-5.0	-1.8	0.0
Other mining and support services	14.3	14.4	13.7	6.5

Source: Department of Statistics, Malaysia

Headline inflation increased in first quarter 2016

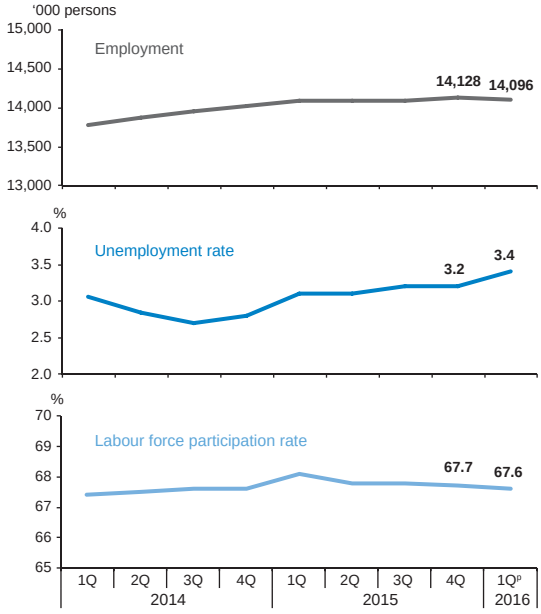
Inflation, as measured by the annual change in the Consumer Price Index (CPI), was higher at 3.4% in the first quarter of 2016 (4Q 2015: 2.6%). Inflation in the *housing, water, electricity, gas and other fuels* category increased to 3.0% in first quarter of 2016 (4Q 2015: 2.5%) following the reduction in electricity tariff rebates from 2.25 sen per kWh to 1.52 sen per kWh in January 2016. The higher inflation during the quarter was also attributable to the smaller negative inflation in the *transport* category (-1.6%; 4Q 2015: -5.7%) due to the base effect from the larger decline in domestic fuel prices in the first quarter of 2015.

The Producer Price Index (PPI) declined in the first quarter of 2016 by 4.4% (4Q 2015: -4.5%). The decline was driven mainly by lower prices of intermediate materials, particularly in the *processed fuel and lubricants* category, reflecting the low global energy and commodity prices during the quarter.

Softer but stable labour market

Labour market conditions were softer but broadly stable during the first quarter of 2016[1], as the unemployment rate increased slightly (3.4% of labour force; 4Q 2015: 3.2%), while labour force participation remained sustained (67.6% of the labour force; 4Q 2015: 67.7%). Demand for new hires was also sustained in the first quarter, as proxied by the high number of new positions posted by employers, mostly from the manufacturing and services sectors on Jobstreet.com (61,378; 4Q 2015: 54,569).

Labour Market Indicators*



* The Labour Force Survey (LFS) figures for 1Q 2015 onwards reflect new current population estimates by the Department of Statistics, Malaysia

[p] Preliminary

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

Consumer Price Index

Category	Weights (%) (2010=100)	4Q 2015	1Q 2016
		Annual change, %	
Total	**100.0**	**2.6**	**3.4**
Food and non-alcoholic beverages	30.2	4.5	4.6
Housing, water, electricity, gas and other fuels	23.8	2.5	3.0
Transport	13.7	-5.7	-1.6
Others	32.3	5.0	4.8

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

[1] Based on preliminary data

Aggregate wages in the manufacturing sector continued to record robust growth (6.9%; 4Q 2015: 7.4%) supported by continued growth in export performance, particularly in the electrical and electronics cluster. Nevertheless, employment growth in the manufacturing sector remained weak (-0.5%; 4Q 2015: -0.4%) indicating that employers continued to remain cautious about expanding their workforce during the quarter. In the distributive trade services sub-sector[2], wage growth was sustained at 4.7% (4Q 2015: 4.6%). Employment in this sub-sector expanded at a rate of 2.5% (4Q 2015: 2.6%).

External position remained resilient in the first quarter

The **current account** recorded a smaller surplus of RM5.0 billion, equivalent to 1.8% of GNI in the first quarter of 2016 (4Q 2015: RM10.5 billion or 3.6% of GNI), due mainly to a lower goods surplus and a larger services deficit, despite smaller deficits in the income accounts.

Balance of Payments[1]

	2015			2016
	1Q	4Q	Year	1Q
Current Account	**11.3**	**10.5**	**34.7**	**5.0**
(% of GNI)	*4.2*	*3.6*	*3.1*	*1.8*
Goods	27.7	31.1	109.6	23.5
Services	-3.5	-6.4	-21.0	-6.8
Primary income	-7.7	-9.1	-32.0	-6.7
Secondary income	-5.1	-5.0	-21.9	-4.9
Financial Account	**-29.8**	**3.9**	**-50.9**	**5.8**
Direct investment	-1.4	5.8	4.8	3.7
Assets	*-10.0*	*-2.9*	*-37.2*	*-11.2*
Liabilities	*8.5*	*8.6*	*41.9*	*14.9*
Portfolio investment	-7.9	15.9	-28.2	13.1
Assets	*-7.4*	*5.6*	*-9.1*	*-5.9*
Liabilities	*-0.5*	*10.3*	*-19.1*	*19.0*
Financial derivatives	0.0	-0.1	-0.7	0.5
Other investment	-20.5	-17.6	-26.8	-11.5
Errors & omissions[2]	2.8	-20.4	21.1	-38.4
Overall Balance	**-15.7**	**-6.0**	**3.8**	**-27.6**

Assets: (-) denotes outflows due to the acquisition of assets abroad by residents
Liabilities: (+) denotes inflows due to the incurrence of liabilities in Malaysia by non-residents
[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 2015 (%)	2015			2016
		1Q	4Q	Year	1Q
		Annual change (%)			
Gross Exports	**100.0**	**-2.5**	**8.1**	**1.9**	**1.0**
Manufactured	80.2	0.2	12.5	6.5	6.4
E&E	*35.6*	*6.8*	*9.6*	*8.5*	*3.6*
Non-E&E	*44.6*	*-4.7*	*14.9*	*5.0*	*8.7*
Resource based	*22.3*	*-12.2*	*2.7*	*-3.9*	*1.6*
Non-resource based	*22.3*	*4.7*	*29.5*	*15.7*	16.2
Commodities	19.2	-10.6	-7.3	-13.4	-18.3
Minerals	*10.6*	*-7.2*	*-14.5*	*-20.6*	*-32.5*
Agriculture	*8.6*	*-15.9*	*3.8*	*-2.7*	*6.5*
Gross Imports	**100.0**	**0.2**	**3.5**	**0.4**	**-0.4**
Intermediate goods	58.2	3.0	-1.7	-2.3	-3.1
Capital goods	14.0	8.7	0.5	0.0	-12.9
Consumption goods	9.1	4.4	38.3	24.1	24.6
Re-exports and dual-use goods	18.7	-15.0	9.0	-0.3	8.7
Trade balance (RM billion)	**-**	**21.3**	**30.6**	**94.6**	**23.9**

Source: MATRADE and Department of Statistics, Malaysia

In the first quarter of 2016, gross exports continued to increase, albeit at a slower rate of 1.0% (4Q 2015: 8.1%), due mainly to a larger decline in commodities exports amid the continued expansion of manufactured exports. Gross imports contracted slightly by 0.4% (4Q 2015: 3.5%), reflecting mainly the lower imports of capital and intermediate goods. As a result, the trade surplus was lower at RM23.9 billion (4Q 2015: RM30.6 billion).

Commodity exports registered a larger decline in the first quarter of 2016, attributable to lower demand for all major commodities during the quarter, with the exception of crude palm oil. The sharp decline in LNG and rubber prices weighed further on commodities exports. Nevertheless, the continued expansion in manufactured exports (6.4%) remained supportive of gross export growth, driven by both non-resource based and resource-based manufactured products, particularly machinery, equipment and parts, metal products, as well as chemicals and chemical products. Electrical and electronic (E&E) exports also grew, supported mainly by demand for electrical machinery and parts and telecommunication equipment.

[2] The distributive trade services sub-sector consist of wholesale and retail trade, and motor vehicles sub-sectors.

In terms of destination, exports remained supported by demand from key trading partners, particularly the US, EU and the ASEAN region. Exports to the US and ASEAN region were supported mainly by E&E products. Exports to the EU were driven mainly by machinery, equipment and parts, as well as palm oil. Exports to PR China continued to expand during the quarter, supported largely by exports of manufactured metal and metal ores.

Gross imports contracted marginally during the quarter (-0.4%). Capital imports were lower in tandem with the more modest expansion in investment activity. Imports of intermediate goods also recorded a slightly larger contraction, weighed down largely by the decline in fuel-related inputs in line with the lower crude oil prices. Nevertheless, growth of consumption imports remained strong with continued demand for imported food and beverages, as well as higher imports of semi-durable consumer goods, particularly garments and footwear. Imports for re-export, particularly metal and E&E products, also contributed to gross import growth.

Malaysia: Direction of Exports

	Share 2015 (%)	2015			2016
		1Q	4Q	Year	1Q
		Annual change (%)			
United States	**9.4**	**14.9**	**18.4**	**14.4**	**13.1**
European Union (EU)	**10.1**	**1.7**	**13.0**	**8.4**	**8.0**
Japan	**9.5**	**-2.8**	**-6.7**	**-10.7**	**-20.6**
Selected ASEAN countries[1]	**27.6**	**-2.3**	**7.7**	**2.6**	**5.7**
North East Asia	**24.0**	**-7.1**	**7.1**	**3.0**	**-4.3**
People's Republic China	*13.0*	*-12.3*	*10.8*	*10.0*	*1.3*
Hong Kong SAR	*4.7*	*7.2*	*1.0*	*-0.5*	*-3.2*
Korea	*3.2*	*-9.5*	*-10.0*	*-9.7*	*-13.7*
Chinese Taipei	*3.0*	*-3.6*	*25.0*	*-3.5*	*-15.1*
West Asia[2]	**2.8**	**-8.0**	**-3.3**	**-4.1**	**5.2**
India	**4.1**	**12.1**	**7.8**	**-0.7**	**3.0**
Total exports	**100.0**	**-2.5**	**8.1**	**1.9**	**1.0**

[1]Singapore, Thailand, Indonesia, Philippines, Brunei Darussalam and Vietnam
[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 RM6.8 billion in the first quarter of 2016 (4Q 2015: a deficit of RM6.4 billion) attributable mainly to higher net payments for other services, particularly for construction and telecommunication services, as well as usage charges for intellectual properties. This was partially offset by smaller net transportation payments amid more modest trade activities, and slightly higher travel surplus following lower outbound travel by residents.

The deficit in the **primary income** account narrowed to RM6.7 billion in the first quarter of 2016 (4Q 2015: a deficit of RM9.1 billion), reflecting mainly lower income accrued to foreign direct investors, particularly in the mining and manufacturing sectors. This more than offset the lower direct investment income accrued to Malaysian companies investing abroad in the mining sector following persistent weakness in oil prices and higher operating costs. The net payments in the **secondary income** account were lower at RM4.9 billion in the first quarter of 2016 (4Q 2015: net payment of RM5.0 billion), due mainly to lower outward remittances.

The **financial account** recorded a net inflow of RM5.8 billion (4Q 2015: net inflow of RM3.9 billion), due particularly to direct investment and portfolio investment inflows.

Direct investment account registered a net inflow of RM3.7 billion (4Q 2015: net inflow of RM5.8 billion), as the incurrence of direct investment liabilities continued to offset the accumulation of direct investment assets. On the assets side, outward direct investment increased to RM11.2 billion (4Q 2015: net outflow of RM2.9 billion). Of these, Direct Investment Abroad (DIA) by Malaysian companies increased to RM11.3 billion (4Q 2015: net outflow of RM6.4 billion), mainly on account of higher injection of equity capital to subsidiaries abroad and sizeable earnings retained for reinvestment purposes. The bulk of DIA was channelled into the mining sector, followed by the services sector, particularly in the finance and insurance as well as information and communications (ICT) sub-sectors. On the liabilities side, inward direct investment rose to RM14.9 billion (4Q 2015: net inflow of RM8.6 billion). Of these, Foreign Direct Investment (FDI) amounted to RM15.0 billion (4Q 2015: net inflow of RM12.2 billion), largely in the form of equity capital and continued reinvestments sourced from retained earnings. The bulk of FDI inflows were channelled into the services sector, mainly reflecting the acquisition of domestic power generation assets by a foreign entity and continued investments in the finance and insurance and ICT sub-sectors. FDI into the mining and construction sector also remained sizeable.

The **portfolio investment** account continued to record net inflows amounting to RM13.1 billion (4Q 2015: net inflow of RM15.9 billion). Net portfolio investments by non-residents rose to RM19.0 billion (4Q 2015: net inflow of RM10.3 billion), on account of continued purchases of debt securities, particularly for Malaysian Government Securities (MGS), and a resumption of net purchases of equities. While global financial markets remained volatile, investor sentiments improved in the latter part of the quarter, supported by a modest rebound in oil prices and signals by the Fed for a more gradual pace in US monetary policy adjustments. On the other hand, portfolio investment by residents recorded a net outflow of RM5.9 billion (4Q 2015: net inflow of RM5.6 billion), due mainly to a resumption in net acquisition of foreign financial assets by domestic banks and institutional investors.

Other investment account recorded lower outflows of RM11.5 billion (4Q 2015: net outflow of RM17.6 billion), due mainly to lower net outflows by both the banks and non-bank private sector. The net outflows were attributed mainly to the placements of funds by Malaysian banks in foreign financial institutions, as well as the net extension of trade credits by Malaysian exporters. At the same time, the public sector also recorded a lower net outflow, attributed mainly to the lower repayment of long-term loans by public enterprises.

Following these developments, the overall balance of payments registered a deficit of RM27.6 billion in the first quarter (4Q 2015: a deficit of RM6.0 billion). Errors and omissions amounted to –RM38.4 billion or -11.1% of total trade, mostly reflecting the foreign exchange revaluation changes in international reserves arising from the strengthening of the ringgit against major currencies during the quarter.

Manageable external debt

Malaysia's external debt stood at RM809.1 billion, equivalent to USD203.7 billion or 65.8% of GDP as at end-March 2016 (end-December 2015: RM833.8 billion or USD192.3 billion, equivalent to 72.1% of GDP). The lower external debt was attributed mainly to the valuation effects following the strengthening of ringgit against most currencies. This was partially offset by the higher non-resident holdings of domestic debt securities.

The strengthening of the ringgit affected mainly the outstanding amount of offshore borrowing, which declined to RM439.0 billion as at end-March 2016 (end-December 2015: RM463.6 billion). It also resulted in lower non-resident deposits and other external debt liabilities, which declined to RM78.8 billion and RM67.5 billion, respectively (end-December 2015: RM81.6 billion and RM77.2 billion, respectively).

During the quarter, there was a net repayment of offshore borrowing by the public sector, mainly on account of the net repayment by public corporations reflecting, in particular, the redemption of an international bond. Nevertheless, these were partly offset by the net drawdown of intercompany loans by foreign multinational corporations with direct investments in the country.

During the quarter, non-resident holdings of domestic debt securities increased by RM12.5 billion to RM223.9 billion, reflecting continued improvement in investor sentiments (end-December 2015: RM211.3 billion). The acquisitions were concentrated mainly in Government domestic debt securities, namely MGS and Government Investment Issues. The non-resident holdings of Bank Negara Monetary Notes, meanwhile, declined to RM21.1 billion as at end-March 2016 (end-December 2015: RM23.7 billion).

Overall, Malaysia's external debt remains manageable, with medium- to long-term external debt comprising more than half of the outstanding position (59.4%). The impact of foreign exchange fluctuations is also fairly contained, as about 40% of the total external debt is denominated in ringgit. The remaining external debt are mostly hedged, either naturally through foreign currency earnings, or through the use of financial instruments. The short-term external debt was lower during the quarter and accounted for only 40.6% of the total external debt. The international reserves were adequate to cover the short-term external debt by 1.2 times. Given the foreign currency earnings and high external assets of banks and corporations, not all of the short-term external debt will create claims on international reserves.

Outstanding External Debt

	2015		2016
	end-Mar	end-Dec	end-Mar
	RM billion		
Offshore borrowing[1]	408.6	463.6	439.0
USD billion equivalent	*109.1*	*106.9*	*110.5*
Medium- and long-term	*241.7*	*285.9*	*271.8*
Public sector	117.3	128.3	117.0
Private sector	124.3	157.6	154.8
Short-term	*166.9*	*177.7*	*167.1*
NR holdings of dom. debt securities	210.7	211.3	223.9
Medium- and long-term	*168.8*	*184.1*	*197.8*
Short-term	*41.9*	*27.2*	*26.1*
NR deposits	81.4	81.6	78.8
Others[2]	66.5	77.2	67.5
Medium- and long-term	*10.9*	*11.9*	*11.4*
Short-term	*55.6*	*65.3*	*56.1*
Total external debt	**767.1**	**833.8**	**809.1**
USD billion equivalent	*204.9*	*192.3*	*203.7*
External debt (Redefined)			
Total debt/GDP (%)	66.3	72.1	65.8
Short-term debt[3]/Total debt (%)	45.1	42.2	40.6
Reserves/Short-term debt[3] (times)	1.1	1.2	1.2[5]
External debt (Previous definition)			
Total debt/GDP (%)	35.3	40.1	35.7
Short-term debt[4]/Total debt (%)	40.8	38.3	38.1
Reserves/Short-term debt[4] (times)	2.3	2.3	2.3[5]

[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] Equivalent to short-term offshore borrowing.
[5] Based on international reserves as at 29 April 2016.

Note: NR refers to non-resident

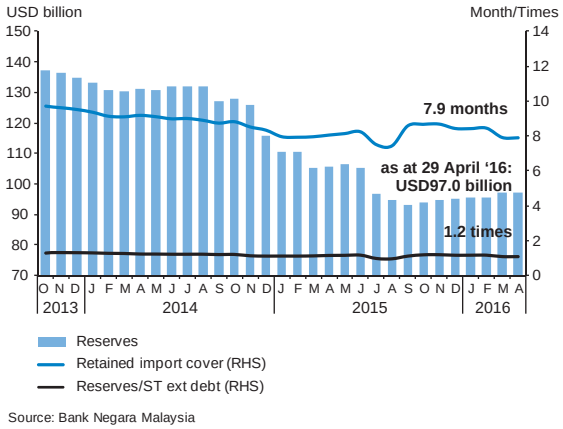
Source: Ministry of Finance, Malaysia and Bank Negara Malaysia

International reserves remain ample to facilitate international transactions

The international reserves of BNM amounted to RM381.6 billion (equivalent to USD97.0 billion) as at 31 March 2016. On account of the quarterly adjustment for foreign exchange revaluation changes, the reserves level in ringgit terms has declined due to the strengthening of ringgit against various currencies. However, underscoring the diversified composition of foreign currency reserve assets, the reserves level in USD terms had correspondingly increased, amid the weakening of USD against most major and regional currencies during the quarter.

As at 29 April 2016, the reserves position amounted to RM381.4 billion (equivalent to USD97.0 billion). The international reserves remain ample to facilitate international transactions. They are sufficient to finance 7.9 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 1.2 times. It is important to note that not all short-term external debt creates claim on reserves given the external assets and export earnings of borrowers.

Net International Reserves (as at end period)

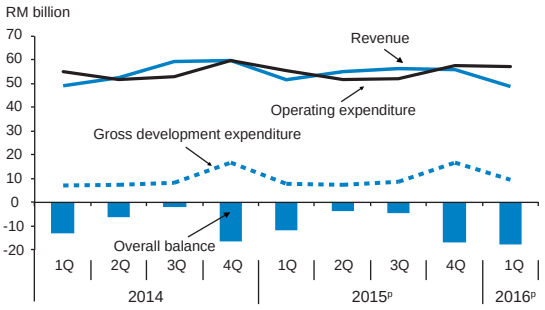


Source: Bank Negara Malaysia

Government spending increased

Federal Government expenditure increased by 5.1% (4Q 2015: -4.2%), due to higher operating and development expenditure. Operating expenditure increased on account of higher spending on *supplies and services* and *pension and gratuities*. Development expenditure rose reflecting higher disbursements for housing projects, roads and bridges under the *social services* and *transportation* sectors, respectively. Government revenue declined by 5.3% (4Q 2015: -6.0%), due mainly to lower oil-related and corporate tax collections. Overall, the Federal Government recorded a deficit of 6.1% of GDP (4Q 2015: -5.6% of GDP) during the quarter. As at end-March 2016, total outstanding debt of the Federal Government amounted to RM626.9 billion or 51.0% of the estimated 2016 GDP.

Federal Government Finance



p Preliminary

Source: Ministry of Finance, Malaysia

Federal Government Finance[p]

	2015			2016
	1Q	4Q	Year	1Q
	RM billion			
Revenue	51.5	56.0	219.1	48.8
% annual growth	*4.8*	*-6.0*	*-0.7*	*-5.3*
Operating expenditure	55.4	57.5	217.0	57.4
% annual growth	*0.4*	*-3.8*	*-1.2*	*3.5*
Current account	**-3.9**	**-1.4**	**2.1**	**-8.6**
% of GDP	***-1.4***	***-0.5***	***0.2***	***-2.9***
Net development expenditure	7.9	15.5	39.3	9.2
% annual growth	*13.2*	*-5.7*	*2.2*	*16.1*
Overall balance	**-11.8**	**-16.9**	**-37.2**	**-17.7**
% of GDP	***-4.2***	***-5.6***	***-3.2***	***-6.1***
Memo item:				
Total net expenditure	63.3	72.9	256.3	66.5
% annual growth	*1.8*	*-4.2*	*-0.7*	*5.1*
Total Federal Government debt (as at end-period)	596.8	630.5	630.5	626.9[1]
% of GDP	*51.6*	*54.5*	*54.5*	*51.0*
Domestic debt	418.9	433.1	433.1	416.7
% of GDP	*36.2*	*37.4*	*37.4*	*33.9*
External debt	177.9	197.4	197.4	210.2
% of GDP	*15.4*	*17.1*	*17.1*	*17.1*
Non-resident holdings of RM-denominated Federal Government debt	*160.2*	*176.0*	*176.0*	*190.2*
% of GDP	*13.8*	*15.2*	*15.2*	*15.5*
Offshore borrowing	*17.6*	*21.5*	*21.5*	*19.9*
% of GDP	*1.5*	*1.9*	*1.9*	*1.6*

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 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 3.25% during the first quarter of 2016. At the prevailing level of the OPR, monetary conditions remained supportive of economic activity.

Reflecting the unchanged OPR, the average overnight interbank rate was relatively stable, trading within a range of 3.01% and 3.24% during the quarter. Interbank rates of longer maturities remained elevated in January, reflecting continued competition for stable funding and the uneven distribution of liquidity among banks. The reduction in the Statutory Reserve Requirement (SRR) effective 1 February 2016 resulted in a broad-based release of liquidity into the banking system. Following this, higher interbank lending activity was observed, which improved the distribution of liquidity in the banking system and alleviated pressure on the Kuala Lumpur Interbank Offered Rates (KLIBOR). For the quarter as a whole, the 3-month KLIBOR decreased from 3.84% to 3.71%. Interest rate swaps continued to trend lower during the quarter, reflecting the lower Malaysian Government Securities (MGS) yields.

Throughout the quarter, the average base rate (BR) of commercial banks increased marginally from 3.86% to 3.89%, reflecting the earlier increase in the KLIBOR towards the end of 2015.

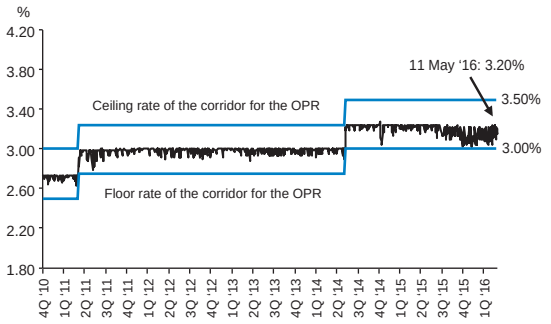
During the quarter as a whole, the weighted average lending rate (ALR) on outstanding loans remained stable (end-March: 5.41%; end-December 2015: 5.40%).

Interest Rates

	2015		2016
	1Q	4Q	1Q
	At end-period (%)		
Overnight Policy Rate (OPR)	3.25	3.25	3.25
Interbank rates			
Overnight	3.24	3.05	3.04
1-month	3.28	3.45	3.25
Base lending rate (BLR)			
Commercial banks	6.79	6.79	6.80
Base rate (BR)			
Commercial banks	3.90	3.86	3.89
Weighted average lending rate			
Commercial banks	5.48	5.40	5.41
Fixed deposit rates			
Commercial banks			
1-month	3.08	3.08	3.08
12-month	3.31	3.31	3.31

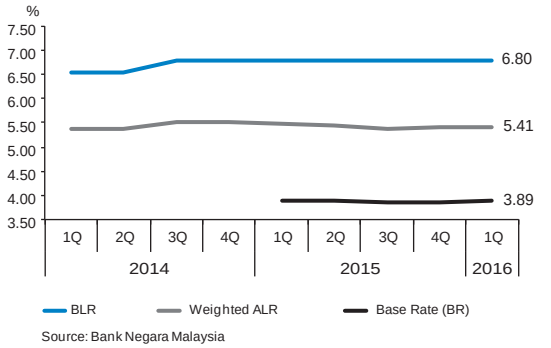
Source: Bank Negara Malaysia

Daily Weighted Average Overnight Interbank Rate



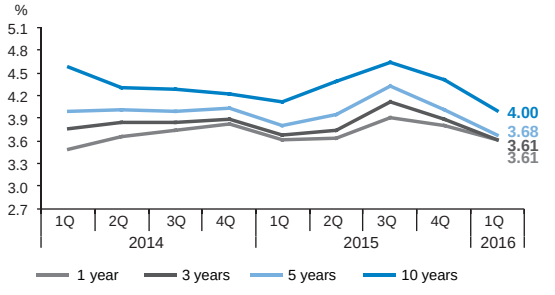
Source: Bank Negara Malaysia

Lending Rates of Commercial Banks (At end-period)



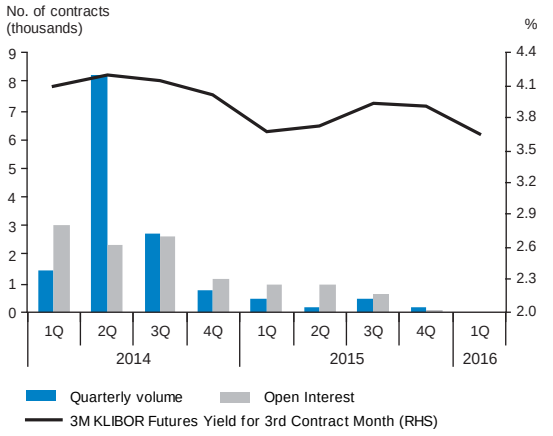
Source: Bank Negara Malaysia

Interest Rate Swap: Rates



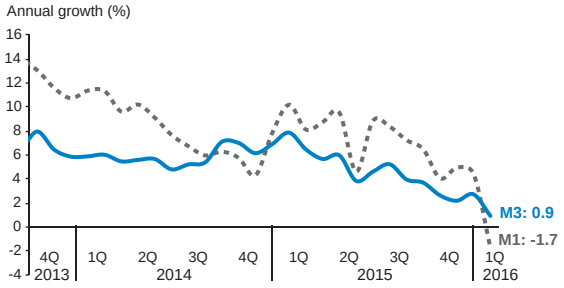
Source: Bloomberg

3 Month KLIBOR Futures



Source: Bursa Malaysia

Monetary Aggregates



Source: Bank Negara Malaysia

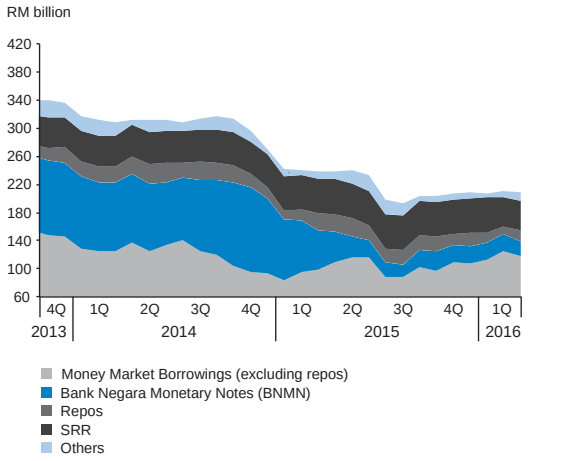
M3 expanded during the quarter

M1, or narrow money, decreased by RM6.3 billion during the quarter. On an annual basis, M1 contracted by -1.7% at end-March (end-December 2015: 4.1%). The contraction in M1 mainly reflected the drawdown of demand deposits for a large one-off loan repayment by domestic businesses. M3, or broad money, increased by RM9.8 billion on a quarter-on-quarter basis to record an annual growth rate of 0.9% as at end-March (end-December 2015: 2.6%).

The slower increase in M3 during the quarter mainly reflected the moderation in credit extended to the private sector by the banking system. On an annual basis, the moderation in broad money growth also reflected the lower net foreign assets due to external sector outflows.

In the banking system, liquidity conditions remained ample at both the institutional and system-wide levels. The level of surplus liquidity placed with BNM was relatively stable during the quarter. The reduction in the statutory reserve requirement (SRR) ratio from 4.00% to 3.50% which took effect from 1 February 2016 resulted in a broad-based release of liquidity into the banking system. Following this, greater interbank lending activity was observed and this partially relieved the demand for BNM's reverse repo operations.

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
	1Q	4Q	Year	1Q
	RM billion			
M3	**35.9**	**12.1**	**40.8**	**9.8**
Net claims on Government	-4.6	5.2	-8.8	-1.0
Claims on private sector	28.3	31.6	120.1	11.0
Loans	*25.2*	*25.7*	*106.1*	*10.6*
Securities	*3.1*	*5.9*	*14.0*	*0.3*
Net foreign assets[1]	-3.4	13.5	-35.6	11.2
BNM	*-26.6*	*8.6*	*-56.3*	*3.0*
Banking System	*23.2*	*5.0*	*20.7*	*8.2*
Other influences	15.6	-38.2	-35.0	-11.4

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

Source: Bank Negara Malaysia

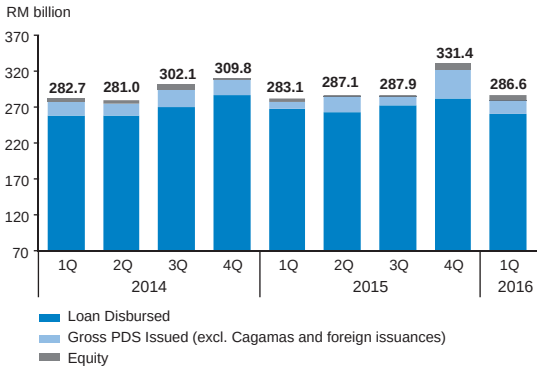
Private sector financing moderated in the first quarter

In the first quarter, total gross financing raised by the private sector through the banking system and the capital market amounted to RM286.6 billion (4Q 2015: RM331.4 billion). On a net basis, outstanding banking system loans and PDS expanded by 7.6% as at end-March (end-December 2015: 8.6%).

Net lending to businesses by the banking system was lower by RM3.6 billion during the quarter (4Q 2015: RM4.9 billion). On an annual basis, outstanding business loans also grew at a slower pace of 5.2% as at end-March (end-December 2015: 8.0%) due to the stronger growth in loan repayments relative to disbursements. The level of loans disbursed to overall businesses grew by 1.1% on an annual basis to RM191 billion during the quarter (1Q 2015: RM189 billion). Nevertheless, loans disbursed to large corporations increased to RM130 billion (1Q 2015: RM123 billion).

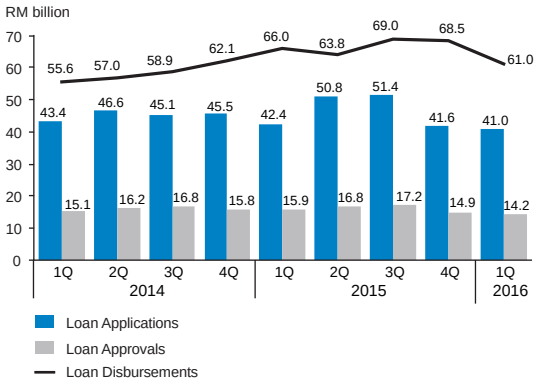
Net financing to the household sector expanded by RM7.1 billion during the quarter (4Q 2015: RM16.9 billion). On an annual basis, outstanding household loans growth moderated to 6.4% as at end-March (end-December 2015: 7.7%), reflecting mainly the moderation in loans for the *purchase of securities, purchase of non-residential property and credit card spending*.

Gross Private Sector Financing through the Banking System and Capital Market



Source: Bank Negara Malaysia

Bank Lending to SMEs



Source: Bank Negara Malaysia

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

	During the period (RM billion)				Annual growth (%)			
	2015			2016	2015			2016
	1Q	4Q	Year	1Q	1Q	4Q	Year	1Q
Gross total financing	**283.1**	**331.4**	**1,189.5**	**286.6**	**0.2**	**6.9**	**1.2**	**1.2**
Loans disbursed	267.4	283.3	1,088.1	262.0	3.5	-1.5	1.3	-2.0
Gross PDS[1]	11.0	40.6	83.5	17.9	-45.2	91.4	1.1	63.0
Equity	4.7	7.5	17.9	6.7	11.3	681.5	-6.5	42.8
Net total financing (A)+(B)	**26.0**	**53.3**	**152.8**	**11.3**	**8.3**	**8.6**	**8.6**	**7.6**
Banking system	23.7	24.0	113.4	5.6	9.2	7.9	7.9	6.5
*Loans outstanding (A)**	*22.2*	*21.1*	*105.4*	*4.3*	*9.2*	*7.9*	*7.9*	*6.4*
Holding of PDS	*1.5*	*2.9*	*8.0*	*1.3*	*8.2*	*8.0*	*8.0*	*7.7*
PDS outstanding (B)	3.8	32.2	47.4	7.0	5.4	10.7	10.7	11.4
Memorandum item								
Gross PDS[2]	11.4	40.6	85.6	40.6	-44.3	87.9	0.2	60.5

* Banking systems loans 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
	1Q	4Q	Year	1Q	1Q	4Q	Year	1Q
Total								
Loan applications	178.5	215.6	827.2	187.7	-3.9	2.6	0.6	5.1
Loan approvals	94.0	100.2	393.2	76.7	3.1	-5.8	-2.0	-18.4
Loan disbursements	267.4	283.3	1,088.1	262.0	3.5	-1.5	1.3	-2.0
Loan repayments	255.6	266.9	1,021.1	264.7	4.0	3.2	2.5	3.6
Change in loans outstanding*	22.2	21.1	105.4	4.3	9.2	7.9	7.9	6.4
Of which:								
Business enterprises[1,2]								
Loan applications	78.4	107.6	396.8	87.8	-9.1	7.2	2.7	11.9
Loan approvals	39.9	49.0	179.9	35.7	14.5	6.2	12.4	-10.4
Loan disbursements	189.0	206.5	787.2	191.0	2.7	-1.6	2.2	1.1
Loan repayments	187.8	201.1	757.5	194.9	4.6	4.6	3.0	3.8
Change in loans outstanding*	9.8	4.9	39.6	-3.6	8.9	8.0	8.0	5.2
SMEs[1]								
Loan applications	42.4	41.6	186.2	41.0	-2.4	-8.6	3.0	-3.3
Loan approvals	15.9	14.9	64.8	14.2	5.5	-5.6	1.6	-10.9
Loan disbursements	66.0	68.5	267.4	61.0	18.9	10.2	14.4	-7.6
Loan repayments	60.3	66.4	254.1	60.8	14.4	15.4	14.2	0.8
Change in loans outstanding*	14.5	5.7	33.8	2.4	17.2	15.0	15.0	9.0
Large corporations[2]								
Loan applications	36.1	66.0	210.6	46.8	-15.8	20.3	2.5	29.8
Loan approvals	24.0	34.1	115.0	21.6	21.3	12.3	19.6	-10.0
Loan disbursements	123.0	138.1	519.9	130.0	-4.2	-6.6	-3.1	5.7
Loan repayments	127.5	134.7	503.4	134.1	0.6	-0.1	-1.9	5.2
Change in loans outstanding*	-4.7	-0.8	5.8	-6.0	2.3	2.2	2.2	1.7
Households								
Loan applications	100.1	108.0	430.4	99.9	0.7	-1.5	-1.3	-0.2
Loan approvals	54.1	51.2	213.4	41.0	-3.9	-15.0	-11.6	-24.3
Loan disbursements	78.4	76.8	300.9	70.9	5.4	-1.3	-0.9	-9.6
Loan repayments	67.8	65.8	263.7	69.8	2.2	-0.6	1.0	3.0
Change in loans outstanding*	16.3	16.9	59.0	7.1	9.8	7.7	7.7	6.4

* The annual growth is for end-period.
[1] Include loans to individual businesses.
[2] Include domestic financial institutions, government, domestic other entities and foreign entities, except for loan outstanding which refers to businesses only.
Note: Numbers do not add up due to rounding

Source: Bank Negara Malaysia

Loans by Sector

	Loans disbursed					Loans out-standing
	During the period (RM billion)				Share of total (%)	Share of total (%)
	1Q 2015	4Q 2015	2015	1Q 2016		
Business enterprises[1,*]	**189.0**	**206.5**	**787.2**	**191.0**	**72.9**	**42.9**
Large corporations[1]	*123.0*	*138.1*	*519.9*	*130.0*	*49.6*	*24.8*
*SMEs**	*66.0*	*68.5*	*267.4*	*61.0*	*23.3*	*18.1*
Selected sectors[1]						
Agriculture, hunting, forestry and fishing	8.8	10.2	39.9	11.2	4.3	2.5
Mining and quarrying	7.0	5.9	20.4	1.8	0.7	0.9
Manufacturing	50.4	53.4	209.9	48.9	18.7	6.9
Construction	17.4	16.7	65.1	16.9	6.4	4.4
Real estate	13.3	13.3	53.3	12.6	4.8	7.0
Electricity, gas and water supply	1.8	2.7	8.9	2.3	0.9	0.6
Wholesale and retail trade, restaurants and hotels	47.0	52.7	199.4	47.4	18.1	7.4
Transport, storage and communication	6.1	4.0	22.5	5.4	2.1	2.3
Finance, insurance and business services	24.9	31.6	104.1	28.3	10.8	6.9
Households	**78.4**	**76.8**	**300.9**	**70.9**	**27.1**	**57.1**
Purchase of residential properties	21.0	21.7	84.7	20.1	7.7	28.9
Consumption credit	44.4	44.9	172.5	41.1	15.7	16.8
Of which:						
Credit cards	*26.3*	*27.2*	*102.4*	*26.0*	*9.9*	*2.4*
Purchase of passenger cars	*10.8*	*10.1*	*40.4*	*8.5*	*3.3*	*10.0*
Others	13.0	10.1	43.7	9.7	3.7	11.5
Total	**267.4**	**283.3**	**1,088.1**	**262.0**	**100.0**	**100.0**

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

Source: Bank Negara Malaysia

Lower net funds raised in the capital market

Net funds raised in the capital market moderated to RM25.4 billion in the first quarter of 2016 (4Q 2015: RM51.4 billion). While fundraising activity was mainly supported by higher public sector issuances, the increase was mostly offset by lower private sector financing in both the debt and equity markets.

In the public sector, net funds raised by the public sector increased to RM18.7 billion during the first quarter (4Q 2015: RM13.5 billion). Gross issuances were higher at RM25.7 billion (4Q 2015: RM21.7 billion), with funds mainly raised through new issuances of 5-year, 7-year and 10-year Malaysian Government Investment Issue (MGII), as well as the re-opening of a 3-year and 15-year Malaysian Government Security (MGS) and 20-year MGII. Government debt redemptions were also lower at RM7.0 billion (4Q 2015: RM8.2 billion) during the period, contributing further to the increase of net funds raised by the public sector.

In the private sector, net financing in the capital market moderated largely due to lower gross issuances and higher redemptions in the private debt securities (PDS) market. Following the significantly larger PDS issuances in the previous quarter, gross funds raised in the PDS market were lower in the first quarter of 2016, amounting to RM18.4 billion (4Q 2015: RM40.6 billion). Funds raised in the PDS market were primarily from the *Finance, Insurance, Real Estate and Business Services* sector and were mainly used for the purpose of working capital.

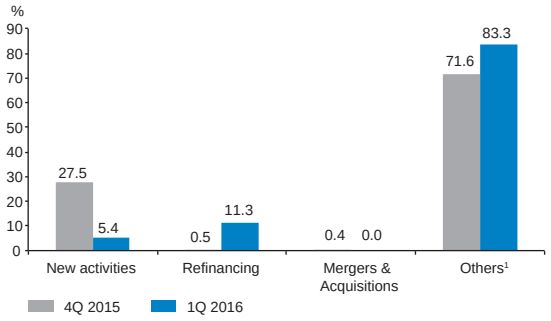
Net Funds Raised in the Capital Market

	2015			2016
	1Q	4Q	Year	1Q
	RM billion			
By Public Sector	**13.2**	**13.5**	**46.8**	**18.7**
Government securities, Gross	27.0	21.7	100.4	25.7
Malaysian Government Securities	13.5	10.9	51.3	12.1
Government Investment Issues	9.5	10.9	41.1	13.6
Sukuk Pinjaman Perumahan Kerajaan	4.0	-	8.0	-
Less: Redemptions	13.8	8.2	53.6	7.0
Malaysian Government Securities	11.8	8.2	41.1	-
Government Investment Issues	2.0	-	12.5	7.0
Sukuk Pinjaman Perumahan Kerajaan	-	-	-	-
By Private Sector	**8.3**	**37.9**	**62.8**	**6.7**
Shares	4.7	7.5	17.9	1.1
Private Debt Securities, Net	3.6	30.5	44.9	5.6
Private Debt Securities, Gross	*11.4*	*40.6*	*85.6*	*18.4*
Less: Redemptions	*7.8*	*10.1*	*40.8*	*12.7*
Total	**21.5**	**51.4**	**109.6**	**25.4**

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

Source: Bank Negara Malaysia and Bursa Malaysia

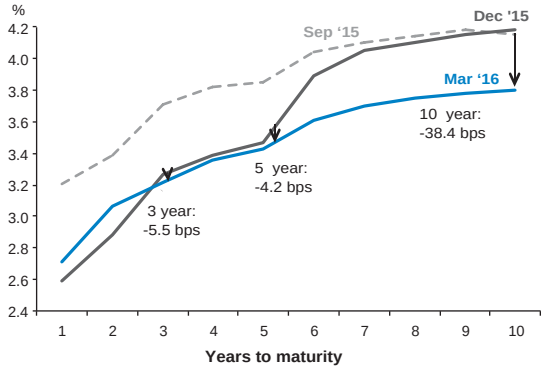
Private Debt Securities Issued by Purpose (% of total)



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

Source: Bank Negara Malaysia

Trend in MGS Yields

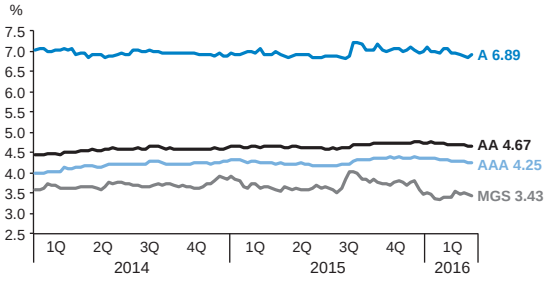


Source: Bank Negara Malaysia

Bond yields declined, especially at the longer end of the yield curve

MGS yields continued to decline in the first quarter of 2016, reflecting sustained non-resident demand for Malaysian sovereign bonds. Non-resident investors increased MGS holdings by RM9.4 billion during the quarter, of which RM5.7 billion was allocated towards papers with tenures longer than 5 years. As a result, yields on the 3-year, 5-year and 10-year declined by 5.5, 4.2 and 38.4 basis points, respectively. In the PDS market, yields remained stable on account of sustained demand by domestic investors.

5 year MGS and 5 year PDS Yields

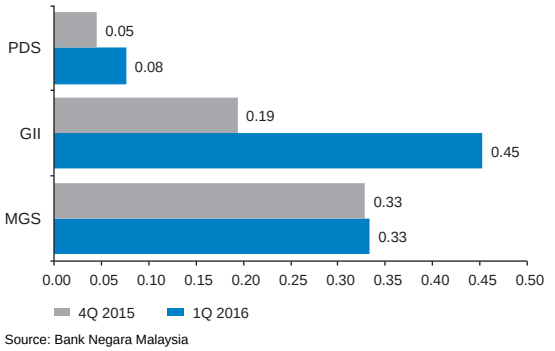


Source: Bank Negara Malaysia

Higher trading in the bond market

Total trading in the secondary market was higher at RM254.1 billion during the quarter (4Q 2015: RM173.9 billion) reflecting more active trading activity between non-residents and financial institutions. In particular, trading liquidity in the MGII market more than doubled to 0.45 (4Q 2015: 0.19), reflecting stronger investor demand for the new issuances during the quarter. The liquidity ratios in the MGS and PDS markets were, however, relatively unchanged at 0.33 and 0.08, respectively (4Q 2015: 0.33, 0.05).

Liquidity Ratio: Value of Bonds Traded / Outstanding



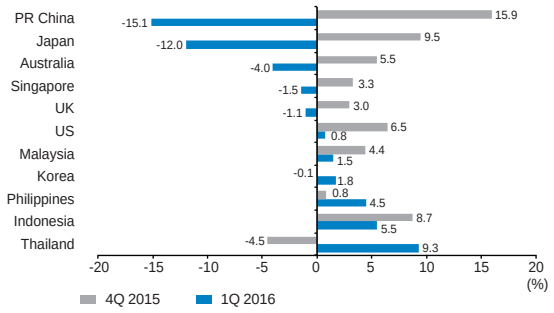
Source: Bank Negara Malaysia

Further increase in FBM KLCI

During the first quarter of 2016, the FBM (FTSE Bursa Malaysia) KLCI increased by 1.5% to close at 1,717.6 points at end-March (end-December 2015: 1,692.5 points).

The increase was in line with trends observed in regional equity markets amid increased risk appetite among global investors for emerging market financial assets. The improvement in global investor sentiments was attributable to expectations of a slower pace of interest rate normalisation in the US and the recovery in Brent crude oil prices. The announcement of the 2016 Budget Recalibration and positive domestic economic data also provided support to the domestic stock market during the quarter.

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



Source: Bloomberg and Bank Negara Malaysia calculations

Consequently, non-resident inflows into the domestic equity market amounted to RM5.5 billion during the quarter.

Overall, market capitalisation was sustained at RM1.71 trillion as at end-March 2016 (end-December 2015: RM1.70 trillion) while the daily average turnover moderated to 1.88 billion units (4Q 2015: 2.23 billion units) during the quarter.

On 11 May 2016, the KLCI ended lower at 1644.6 points (since end-March 2016: -4.3%), with a market capitalisation of RM1.65 trillion (since end-March 2016: -3.1%).

Bursa Malaysia: Selected Market Indicators

	2015			2016
	As at end			
	Mar	Dec	Year	Mar
Price Indices				
Composite	1,830.8	1,692.5	1,692.5	1,717.6
FBMEMAS[1]	12,563.4	11,793.7	11,793.7	11,920.8
ACE Market[2]	7,120.2	6,389.2	6,389.2	5,637.0
Market capitalisation (RM billion)	1,737.5	1,695.2	1,695.2	1,707.4
No. of companies listed	903	903	903	904
	During the period			
	1Q	4Q	Year	1Q
Average daily turnover				
Volume (million units)	2,107.4	2,234.0	2,038.3	1,875.8
Value (RM million)	2,177.4	2,149.7	2,082.2	2,052.2

[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	
	1Q		4Q		Year		1Q	
	Billion units	RM billion	Billion units	RM billion	Billion units	RM billion	Billion units	RM billion
Turnover	124.3	128.5	138.5	133.3	501.4	512.2	112.5	124.1
Of which:								
Main Board	75.8	117.7	82.5	121.4	299.1	464.6	76.3	117.0
Of which								
Consumer Products	7.4	6.4	7.0	6.8	26.9	25.6	8.8	7.3
Industrial Products	12.8	11.1	19.1	21.8	59.0	60.0	14.6	19.3
Construction	3.7	5.9	3.9	4.6	16.5	22.9	4.1	5.3
Trading/Services	32.7	55.4	32.4	51.3	124.7	204.3	30.7	48.0
Finance	3.5	21.3	2.9	17.7	12.8	79.6	3.1	20.1
Properties	5.4	4.8	7.5	5.0	23.7	18.9	6.4	3.4
Plantations	1.0	3.5	1.7	5.0	5.0	15.6	1.6	5.9
Infrastructure	1.0	4.4	1.0	4.3	4.2	18.8	0.8	3.2
ACE Market[1]	41.2	8.7	36.7	8.3	139.2	32.2	20.5	4.1

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

Source: Bursa Malaysia

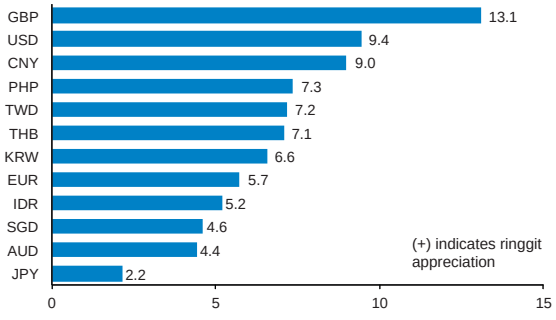
Ringgit strength driven by both domestic and external factors

The ringgit and other regional currencies appreciated against the US dollar during the quarter, due to weaker-than-expected economic performance in the US, resulting in expectations of a slower pace of interest rate normalisation by the Federal Reserve. The ringgit, however, appreciated significantly more compared to other major and regional currencies. This is attributable to the release of positive domestic economic data, the recovery of Brent crude oil prices and the 2016 Budget Recalibration announcement. These factors lifted investor sentiments on the Malaysian economy and led to increased demand for ringgit financial assets.

Overall, the ringgit appreciated by 9.4% against the US dollar during the quarter. The ringgit also appreciated against the pound sterling (13.1%), the euro (5.7%), the Australian dollar (4.4%), and the Japanese yen (2.2%). Against all regional currencies, the ringgit also appreciated by between 4.6% and 9.0%.

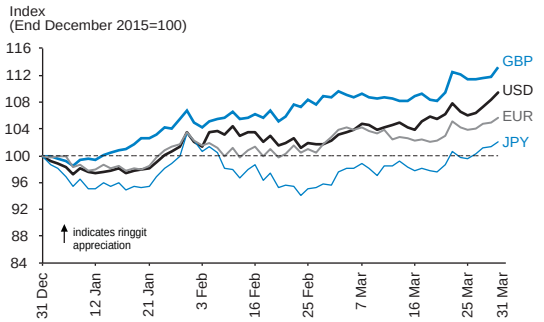
Between 1 April and 11 May 2016, the ringgit depreciated against the US dollar (-3.3%). The ringgit also depreciated against the euro (-3.9%), the pound sterling (-4.0%), and the Japanese yen (-6.4%). The ringgit, however, appreciated against the Australian dollar (0.7%). The ringgit depreciated against regional currencies.

Summary of Ringgit Performance against Selected Currencies Percent Change (1 January - 31 March 2016)



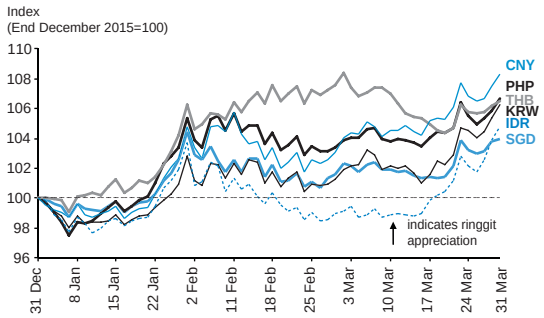
Source: Bank Negara Malaysia

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*	
	1Q 2015	4Q 2015	1Q 2016	1Q 2015	4Q 2015
US dollar	3.7165	4.2920	3.9220	-5.2	9.4
Euro	4.0153	4.6918	4.4377	-9.5	5.7
Pound sterling	5.4935	6.3607	5.6234	-2.3	13.1
Australian dollar	2.8329	3.1338	3.0009	-5.6	4.4
100 Japanese yen	3.0903	3.5645	3.4892	-11.4	2.2
Singapore dollar	2.6997	3.0356	2.9023	-7.0	4.6
100 Thai baht	11.423	11.922	11.134	2.6	7.1
100 Philippine peso	8.3111	9.1494	8.5233	-2.5	7.3
100 Indonesian rupiah	0.0284	0.0311	0.0295	-3.9	5.2
100 Korean won	0.3342	0.3651	0.3427	-2.5	6.6
100 New Taiwan dollar	11.874	13.056	12.180	-2.5	7.2
Chinese renminbi	0.5993	0.6610	0.6064	-1.2	9.0

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

Source: Bank Negara Malaysia

Activity in the foreign exchange derivatives market was subdued as market volatility stabilised

In the first quarter of 2016, the foreign exchange derivatives market recorded a lower volume of USD240.9 billion (4Q 2015: USD268.6 billion) consistent with the decline in the foreign exchange spot market. Swap transactions, which account for 84% of total derivatives market activities, declined by 13.0% as non-residents who were the most active participants have less domestic exposure and hedging needs following last year's capital outflows. Residents on the other hand, continued to be active in managing their foreign currency exposure in anticipation of a stronger ringgit via outright forwards, which increased by USD3.8 billion or 18.4% in terms of y-o-y growth.

As at end first quarter of 2016, the cost of borrowing US dollars through cross-currency swap market was 73 bps, which was in the range of previous quarter closing levels (75 bps). In February 2016, the cost was temporarily lowered to 65 bps following improvement in domestic US dollar liquidity from net capital inflows during that period, before stabilizing above 70 bps in March 2016.

MANAGING RISKS TO FINANCIAL STABILITY

Domestic financial system remains resilient

The Malaysian financial system remained resilient against potential risks related to spillovers from the weaker global growth prospects and continued volatility in the international financial and commodity markets. Domestic risks more broadly have continued to moderate. However, more challenging business conditions and rising costs will likely weigh on the revenue and loan performance of financial institutions in the period ahead, requiring close vigilance. Any adverse developments are expected to remain well within the loss absorption capacity of financial institutions given the healthy capital buffers which strengthened further since end-2015. This, along with sound underwriting practices observed by financial institutions, will continue to lend firm support to domestic financial intermediation. Ample domestic liquidity has also remained supportive of credit growth and orderly market conditions.

Manageable credit risk exposures amid sustained debt servicing capacity

Credit risk exposures of banks remained manageable, underpinned by the sustained debt servicing capacity of borrowers. Loan impairments and delinquencies as a share of total bank loans were largely unchanged at 1.2% and 2.1% respectively. The overall loan loss coverage for the banking sector, while slightly lower, remained above 90%. This was supported by measures to shore up provisions over the last two years, including measures taken in response to the Bank's call for banking institutions to maintain loan loss reserves at a minimum level of at least 1.2% of bank loans. In the insurance and takaful industry, credit exposures (mainly from holdings of highly-rated private debt securities and Malaysian Government Securities) rose slightly to 4.3% of total capital available (4Q 2015: 4.2%).

Growth in household borrowings continued to moderate in the first quarter of the year (1Q 2016: +6.5%; 4Q 2015: +7.3%; 1Q 2015: +9.1%). House financing remained robust, expanding by 10.7% (4Q 2015: +11%; 1Q 2015: +12%) amid sustained strong demand for affordable housing. Growth in personal financing picked up slightly to 5.4% (4Q 2015: +4.6%), likely reflecting adjustments to higher costs of living by households. Generally, prudent debt service ratios continued to be observed by both banks and non-banks for new household lending. This has led to improved quality of new financing to households, and preserved overall household resilience. The average debt service ratio (against net income) for new household loans remained below 60%. About half of new financing approved for the period were to borrowers with a debt service ratio below 40%.

The ratio of impaired household loans edged slightly higher to 1.7% (4Q 2015: 1.6%) of total household loans by banks and non-banks amid emerging signs of weaker repayment capacity observed for borrowers that are more reliant on cyclical income sources such as commission-based jobs. Risks of a broader deterioration in the performance of household loans appear contained as overall household delinquencies improved to 1.4% of total household borrowings (4Q 2015: 1.5%). The banking system also continued to record improvements in the retail lending portfolio during the quarter, with impairments and delinquencies accounting for 1.0% and 1.4% of bank lending to households respectively as at end first quarter of 2016. The overall debt servicing capacity of households is also supported by the net accumulation of financial assets over debt which increased further by RM27.4 billion during the quarter.

Risks from banks' exposures to the business sector remain contained. The aggregate leverage of Malaysian businesses[3], as measured by the median debt-to-equity ratio, improved to 44.5% in the fourth quarter of 2015 (3Q 2015: 46.8%). Business sector borrowings expanded at a slower pace of 8.8% as at end first quarter of 2016 (4Q 2015: +13.2%) in line with the moderation in domestic economic activity. Bank financing to businesses expanded by 4.9% (4Q 2015: +8%), with financing to small and

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

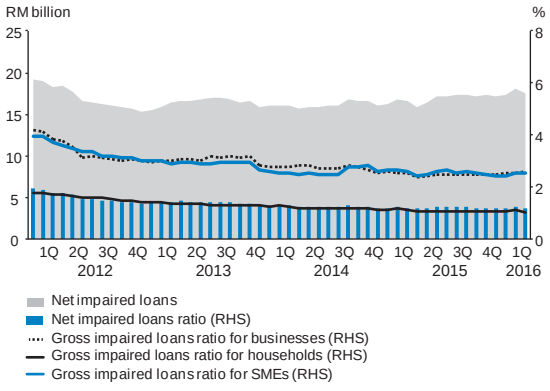
medium enterprises remaining a key driver of business loan growth (+9.0%). Outstanding external borrowings by businesses amounted to RM287.4 billion, lower than in the previous quarter (RM296.5 billion), on account of sustained healthy repayments and the strengthened ringgit as at end fourth quarter of 2015. More than 40% of total external borrowings remained in the form of inter-company obligations by multinational corporations with operations in Malaysia, which continue to present limited potential rollover and funding risks.

The effects of weak commodity prices and softer external demand on the financial health of overall businesses in the export-oriented sectors have generally been contained. In the domestic-oriented sectors, weaker consumer sentiment, higher import costs and increased competition continued to pose a drag on corporate earnings. Reflecting these conditions, the median interest coverage ratio (ICR) was lower at 4.4 times in the fourth quarter (3Q 2015: 5.0 times). This measure of the ability to service debt remains comfortably above the level of two times which is generally considered to be prudent. The aggregate liquidity buffers of businesses to meet short-term debt obligations also remained intact, with the median current ratio (current assets-to-current liabilities) and cash-to-short-term debt ratio (CASTD) unchanged at 1.7 times and 1.2 times respectively in the final quarter of 2015.

The ratio of impaired and delinquent business loans remained stable during the quarter at 2.6% and 0.3% of total bank lending to businesses respectively (4Q 2015: 2.5% and 0.3% respectively). Delinquencies were slightly higher in the construction and real estate sectors, reflecting softer operating conditions for businesses in these segments. Correspondingly, the overall expected default frequency for businesses increased to 0.69% (4Q 2015: 0.61%), suggesting a slight weakening in the credit risk outlook for sectors that are more exposed to uncertainties in global demand, and movements in exchange rate and commodity prices. Notwithstanding this, risks to the banking system are limited. Banks' exposures to the crude palm oil and oil and gas sectors remained small at 3.8% and 2.2% of total credit exposures to businesses respectively. Exposures to large business borrowers with weak financials (ICR below 1.5 times and CASTD below one time) remained limited at 6.7% of total bank credit exposures to corporations. Furthermore, exposures to large borrower groups with a higher concentration of foreign currency denominated borrowings (i.e. more than 30% of total borrowings) and weak financials represented less than 2% of total bank credit exposures to businesses.

In the third quarter of 2015, the annual growth of the Malaysian House Price Index moderated marginally to 7.4% (2Q 2015: +7.5%). Across states, average house price increases ranged between 3% - 8.9% (2Q 2015: 0.2% - 8.7%). Housing transactions, particularly in the higher-priced segments, remained soft in both the primary and secondary markets. On an annual basis, the total transaction volume and value declined by 3.1% to 58,859 units (3Q 2015: -9.4% to 57,662 units) and 4.1% to RM19.3 billion (3Q 2015: -18.1% to RM17.7 billion) respectively as at end fourth quarter of 2015. In contrast, the volume and value of transactions in the affordable segment (houses priced below RM250,000) continued to register positive growth of 7.5% and 14.6% respectively (3Q 2015: +5% and +10.2% respectively). Credit-induced speculative purchases of residential properties remained subdued. The number of borrowers with at least three outstanding housing loans (a proxy used for speculative house purchases) expanded at a slower annual rate of 2.9% in the first quarter of 2016 (4Q 2015: 3.2%).

Banking System: Loan Quality



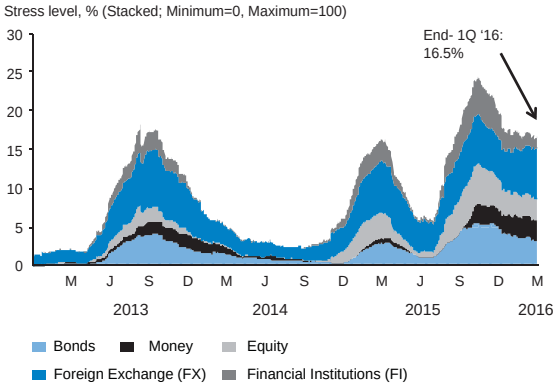
Source: Bank Negara Malaysia

Domestic financial market conditions remained orderly

Orderly conditions in the domestic financial markets were preserved as volatility in the bond and equity markets eased during the quarter. Average volatility of the 10-year MGS yield and FBM KLCI declined to 13.5% and 11.7% respectively (4Q 2015: 17.2% and 14.5% respectively). Improved investor sentiment broadly reflected some recovery in commodity prices and the prospects of further US policy rate increases being deferred. This attracted foreign capital inflows and renewed participation in the domestic asset markets. Portfolio investments recorded a larger net inflow of RM13.1 billion (4Q 2015: net inflows of RM15.9 billion) on the back of sustained strong interest by non-residents in the MGS and equity markets.

Non-residents' holdings of MGS rose to 48.7% (4Q 2015: 47.7%) of total outstanding MGS, of which 62.6% comprised holdings of short- to medium-term MGS with maturities up to 5 years. Yields on the 3, 5 and 10-year MGS eased to 3.21%, 3.43% and 3.80% respectively (4Q 2015: 3.27%, 3.47% and 4.19% respectively). The FBM KLCI ended the quarter higher at 1,717.6 points (4Q 2015: 1,692.5 points) in line with most regional markets. Equity holdings by non-residents stood at 22.9% of total market capitalisation (4Q 2015: 22.3%). The price-to-earnings (PE) ratio of FBM KLCI rose to 19 times against a long-term average PE ratio of 17 times following the more subdued corporate earnings in the first quarter. Trading liquidity, both in terms of price and volume, remained intact. The bid-ask spreads for MGS and FBM KLCI remained tight at 0.1% and 0.4% of the mid-price respectively. The monthly turnover ratio for the MGS and FBM KLCI also held firm at 11.9% and 2.0% respectively as at end first quarter of 2016 (4Q 2015: 10.5% and 2.1% respectively). The ringgit strengthened against the US dollar, appreciating by 9.4% to end the quarter at RM3.9220 per US dollar (4Q 2015: RM4.2920), in line with the performance of the domestic bond and equity markets. Investors' perception of Malaysia's sovereign credit risk and onshore US dollar liquidity conditions improved further during the quarter. The 5-year sovereign credit default swap spread eased to 153.9 basis points (4Q 2015: 180.2 basis points, 3Q 2015: 238.9 basis points), while the 5-year cross-currency basis swap spread was almost unchanged at 73 basis points (4Q 2015: 75 basis points, 3Q 2015: 115 basis points).

Financial Market: Financial Market Stress Index (FMSI)



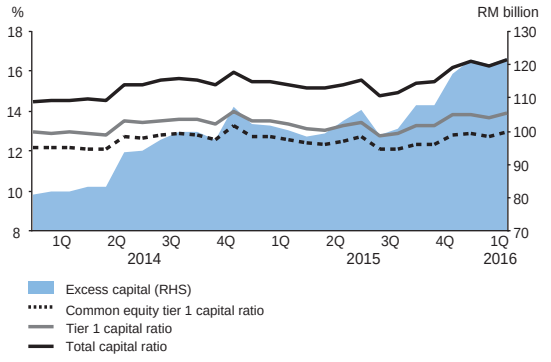
Note: The FMSI is constructed from indicators of volatility in the five components of the domestic financial markets - the foreign exchange (FX), equity, bond, money markets and financial institutions (FIs). The stress level at a specific date is expressed as a value between 0 and 100, which signifies the lowest to highest stress level.

Source: Bloomberg and internal computation

Sustained strength and resilience of financial institutions

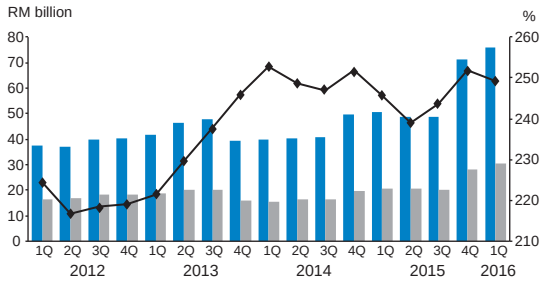
Malaysian banks, insurers and takaful operators continued to maintain a high level and quality of capitalisation, of which more than 90% is in the form of retained earnings, paid-up capital and reserves. At end first quarter of 2016, the common equity tier-1 capital, tier-1 capital and total capital ratios of banks were sustained well above the minimum regulatory levels at 13.0%, 13.9% and 16.5%, respectively. The capital adequacy ratio for the insurance and takaful sectors stood healthy at 242.6% (4Q 2015: 245.4%). Financial institutions are well-positioned to withstand potential adverse macroeconomic and financial shocks, with combined capital buffers of RM170.4 billion as at end first quarter of 2016 (banks: RM121.9 billion; insurers and takaful operators: RM48.5 billion).

Banking System: Basel III Capitalisation



Source: Bank Negara Malaysia

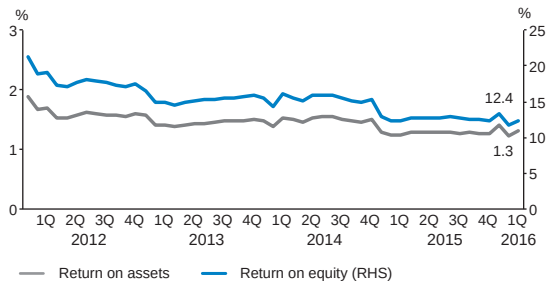
Insurance Sector: Capitalisation



Source: Bank Negara Malaysia

Bank earnings remained resilient during the quarter in spite of a more challenging operating environment. The pre-tax profit of the banking system increased to RM7.7 billion as at end first quarter of 2016 (4Q 2015: RM7.2 billion) following improved revenue from treasury related activities and lower operating expenses. Returns on assets and equity were unchanged at 1.3% and 12.4% respectively (4Q 2015: 1.3% and 12.4% respectively). General insurers and takaful operators recorded higher operating profits of RM730.2 million for the quarter (4Q 2015: RM679.5 million), on account of more favourable claims experience with the claims ratio improving to 54.1% (4Q 2015: 60.6%). In contrast, life insurers and family takaful operators recorded a lower excess income over outgo of RM4.7 billion (4Q 2015: RM5.2 billion). This was mainly due to the lower net capital gains of RM1.5 billion (4Q 2015: RM2.0 billion), reflecting the weaker equity performance in the first two months of the quarter.

Banking System: Profitability



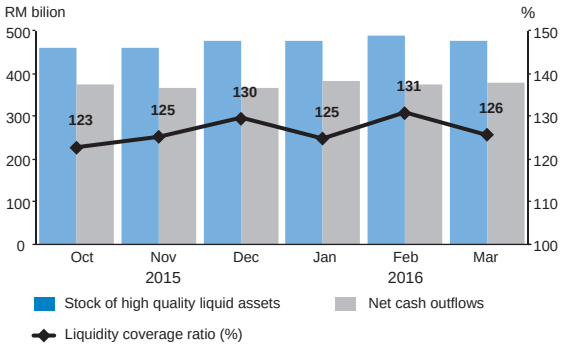
Source: Bank Negara Malaysia

Market risk exposures remained well-contained within the risk appetite and internal limits of financial institutions, supported by active risk management and hedging strategies. Bank exposures to interest rate risk in the trading book and equity risk remained low at 1.1% and 0.8% of total capital respectively (4Q 2015: 1.2% and 0.7% respectively). The foreign exchange net open position of banks rose slightly to 6.5% of total capital (4Q 2015: 6.1%). Market risk exposures of the insurance and takaful industry were broadly unchanged at 13.1% (4Q 2015: 12.9%) of total capital available, while equity risks, which forms the bulk of insurers' market risk exposures, edged lower to account for 7.3% (4Q 2015: 7.5%) of total capital available.

Ample liquidity in the banking system has continued to support financing activities. As at end-1Q 2016, banking system placements and reverse repos with Bank Negara Malaysia which can be unwound to meet liquidity needs, increased to RM135 billion (4Q 2015: RM127 billion), preserving comfortable buffers against unexpected cash outflows or adverse liquidity shocks. Under the Basel III Liquidity Coverage Ratio (LCR) standards which have been phased in since June 2015[4], the banking system LCR stood at 126% as at end first quarter of 2016 (4Q 2015: 130%). All banks maintained LCR levels that are above the current minimum regulatory requirement of 70%, with 38 banks recording LCR levels above 100%.

Domestic funding conditions improved during the quarter. The average cost of deposits[5] was stable at 2.54% (4Q 2015: 2.53%, 2014: 2.38%) while the 3-month KLIBOR eased to 3.71% (4Q 2015: 3.84%) following some easing in competition for corporate deposit placements since January 2016. The quoted 1-month fixed deposit rates for large corporate depositors fell between 15 basis points and 85 basis points during the quarter. Similarly, quoted 3-month fixed deposit rates declined between 50 basis points and 65 basis points during the same period. Household deposits continued to register a healthy growth of 5% (4Q 2015: +5.3%). However, overall deposits in the banking system declined by 0.9% (4Q 2015: +1.8%) as the outstanding deposits accepted from businesses fell by 4.2%. This was partly attributed to an isolated withdrawal by a large corporate depositor. Notwithstanding this, deposits and investment accounts accepted by banks expanded by 2.4% (4Q 2015: +4.7%) as at end first quarter of 2016. Banks continued to diversify their funding structure through the issuance of medium-term ringgit and foreign currency denominated funding instruments, which grew annually by 13% to RM102 billion (4Q 2015: +24%) as at end first quarter of 2016. This has contributed towards further reducing maturity and currency mismatches in bank funding structures. Taking into account the broadened funding base of banks, the loan-to-funds ratio[6] (LTF) improved to 82.4% during the quarter, while the loan-to-deposit ratio[7] was lower at 87.7% (4Q 2015: 83.0% and 88.7% respectively).

Banking System: Basel III Liquidity Coverage Ratio



Source: Bank Negara Malaysia

Insurance and Takaful Sectors: Indicators

	2015			2016
	1Q	4Q	Year	1Q
	RM million			
Life insurance & family takaful				
Excess of income over outgo	5,336	5,246	12,009	4,689
General insurance & general takaful				
Operating profit	781	679	2,698	730
Claims ratio (%)	50.3	60.6	60.2	54.1
	Annual Change (%)			
Life insurance & family takaful				
Excess of income over outgo	66.2	147.4	-12.7	-12.1
General insurance & general takaful				
Operating profit	-5.2	-10.6	-15.1	-6.5
Claims ratio (percentage points)	-4.7	1.1	2.7	3.7

Source: Bank Negara Malaysia

[4] In the first phase, compliance is set at 60% with progressive increments of 10% each year until 100% with effect from 2019. The current minimum requirement is set at 70%.
[5] Revision in the computation of the average cost of deposits (calculated as the interest expense on deposits as a percentage of total deposits accepted).
[6] Fund comprises deposits and all debt instruments (including subordinated debt, debt certificates/ sukuk issued, commercial papers and structured notes).
[7] Beginning July 2015, loans exclude financing funded by Islamic investment accounts.