chapter one

executive summary

Introduction

Changing economic and business environment as well as rapid technological advances over the last decade have had significant impact on the development of the financial system, domestically and globally.

Global forces at work and advances in technology have redefined the rules of the game and transformed the operational environment within which financial institutions operate. Indeed, the ability to reap the benefits arising from greater competition depends largely on the capability and capacity of financial institutions to adapt swiftly and to embrace the changes.

Similarly, the rapid pace of economic development and transformation that creates new demands as well as opportunities for businesses have called for a more effective and efficient provision of financial services. In moving ahead, a well-defined strategy will need to be formulated for the financial sector if it were to prosper in the new environment and play a meaningful role in the nation's future economic development.

Vision and Objectives of the Financial Sector

The objective of the FSMP is therefore 'to develop a more resilient, competitive and dynamic financial system with best practices, that supports and contributes positively to the growth of the economy throughout the economic cycle, and has a core of strong and forward looking domestic financial institutions that are more technology driven and ready to face the challenges of liberalisation and globalisation'. The development of domestic institutions that form the core of an efficient, effective and stable financial sector is an important part of this process.

- It is envisaged that Malaysia's real economy will continue to expand significantly during the decade, becoming more internationally integrated and more dynamic (with more high-tech services, with greater reliance on small and medium-sized industries [SMIs] and with increasingly rapid rate of innovation), and with more differentiated and demanding consumers.
- To serve this dynamic economy efficiently and effectively, and to ensure that domestic institutions will have a leading role within it, the financial sector, particularly its domestic institutions will need to be more focused, efficient and innovative.
- The regulatory framework within which the financial industry operates will be based on a supervised market approach. The regulations will allow product innovations and market activism, while being strongly supervised by standards and prudential requirements.
- The financial landscape at the end of the 10-year period will consist of a more diversified range of 'brick and mortar' financial service providers, from large one-stop financial centres to niche providers, of specialist services - competing with 'virtual' providers across most product areas. In addition, the capital market will have a relatively more important role in the allocation of resources and risks.

Key Challenges that Need to be Addressed

As changes in the global financial industry continue to evolve and accelerate in the new millennium, the Malaysian financial system, particularly domestic banking institutions and insurance companies will face mounting pressure to become more efficient and competitive, innovative, technology-driven, and strategically more focused. The financial infrastructure will have to be developed accordingly to facilitate and support this development. In so doing, the industry will face the following key challenges:

- The need for domestic institutions to improve their efficiency and effectiveness to be at par with the best international players; and
- The need to ensure that performance gaps do not widen, as technology continues to drive global trends in financial services. In order to compete in the new environment, financial institutions in leading markets are leveraging on new technology, as well as:

- Becoming increasingly global and specialised;
- Using new organisation structures and more aggressive compensation models;
- Relying much more on alliances and third party relationships; and
- Investing more in technology.

Recommendations to Achieve Objectives

In order to bring in greater innovation, flexibility and dynamism into the Malaysian financial system, the FSMP has made a number of recommendations to be implemented over the plan period. Measures to identify and remove impediments to progress will be implemented, beginning with improvements in infrastructure and increasing the intensity of domestic competition, so as to allow best institutions to flourish.

Given the important roles played by domestic financial institutions in ensuring the stability of the financial system and supporting the economy, steps will need to be taken to:

- Develop the best domestic institutions by:
  - Building the capabilities of domestic institutions; and
  - Increasing the incentives for domestic institutions to drive performance.
- Maintain stability of the financial system through an efficient infrastructure, more resilient institutions as well as strong prudential regulations and supervision;
- Meet the socioeconomic objectives of Malaysia that will result in the least possible distortion and to minimise the burden on the institutions; and
- Promote a more market driven consumer protection infrastructure.

Approach to Implementation

The change programme will be implemented over the next 8-10 years in three phases, subject to achieving specified milestones and safeguards. The first phase is on building the domestic capacity, the second phase in which domestic competition increases and the third phase in which the pace for the integration with the international market is increased.

While measures to increase domestic capacity would be implemented during the first phase, these measures will continue to be strengthened during the second and third phases to ensure orderly adjustment to a more competitive and increasingly deregulated and liberalised market. The order in which specific recommendations are made in this FSMP will not necessarily indicate the sequence of implementation. Implementation of the recommendations will be done in a practical manner such that the desired outcomes are achieved without any destabilising impacts to the financial sector.