

CHAPTER 4

Monetary and Financial Developments

119 OVERVIEW

119 MONETARY DEVELOPMENTS

120 PERFORMANCE OF RINGGIT

120 BANKING SECTOR PERFORMANCE

Feature Article 4.1 – Digital Banks in Malaysia

126 CAPITAL MARKET PERFORMANCE

Information Box 4.1 – Key Capital Market Measures

131 ISLAMIC BANKING AND CAPITAL MARKET PERFORMANCE

132 CONCLUSION

133 REFERENCES

Vibrant Monetary Operations & Sound Financial System

Vibrant Money & Foreign Exchange Markets

and intermediation activities supported monetary operations



Resilient Monetary & Financial Conditions

throughout COVID-19 pandemic period supported economic recovery



Monetary Developments

Monetary policy cushioned the adverse effects of measures implemented to contain the spread of COVID-19 virus on the economy.

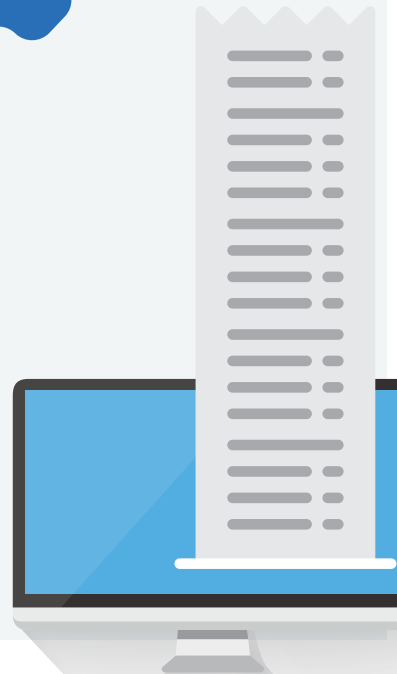
The Overnight Policy Rate (OPR) was reduced successively by 125 basis points (bps) during the first seven months of 2020 to a historic low of 1.75%.

Banking institutions were also given the flexibility to use Malaysian Government Securities (MGS) and Malaysian Government Investment Issues (MGII) to fully meet SRR compliance.



Monetary policy also provided additional stimulus to sustain the pace of economic recovery.

The Statutory Reserve Requirement (SRR) was reduced by 100 bps from 3.00% to 2.00%.



Risks to Capital and Financial Market Performance



Pace of global economic recovery



Prolonged US-China trade tensions



Weak commodity prices



Volatile global financial markets

Performance of Ringgit



JANUARY



In January 2020, the ringgit appreciated against the US dollar mainly due to non-resident portfolio inflows. This was supported by improved investors' risk sentiment attributed to positive development in the US-China trade negotiation.

FEBRUARY



In February and March, the local note, along with regional currencies, faced significant depreciation against the US dollar. The downward trend of the ringgit was contributed by geopolitical uncertainties, declining commodity prices and rapid escalation of the COVID-19 pandemic.

Robust & Orderly Banking Sector

ample liquidity & strong capital buffers



Resilient Capital Market

well-developed infrastructure & instruments



Banking Sector Performance



Capitalisation of banking sector remained strong, supported by the accumulation of high-quality loss-absorbing instruments.

As at end-July 2020, excess total capital buffer remained high at RM121.6 billion.

Islamic Banking & Capital Market Performance



Islamic banking industry expanded with total assets valued at RM1,038.2 billion and market share at 33% as at end-July 2020. Total Islamic financing outstanding increased further by 10% to RM787.8 billion.

Islamic financing is expected to expand further supported by the recovery in economic activity and continuous promotion of Shariah-compliant products.

The demand for Shariah-compliant products is expected to be stronger in the future, supported by its appeal to a broader group of investors.

Ongoing promotion of Shariah-compliant products and digitalisation of services will provide the impetus for the country to position itself as a prominent international centre for Islamic financial services.

The growth is primarily contributed by household sector financing, which increased by 8.7% to RM490.9 billion, mainly for the purchase of residential properties.

The Islamic Capital Market (ICM) continues to thrive with Malaysia being among the largest issuer of sukuk and Islamic equity in the world. As at end-July 2020, the domestic size of ICM was valued at RM2.2 trillion, accounting for 66.2% of RM3.3 trillion of Malaysia's total capital market size.

Sukuk issuances amounted to RM130.8 billion or 60.2% of total bonds issuances. Sukuk outstanding was valued at RM986.9 billion or 62.6% of total bonds outstanding.

Despite the challenging economic climate, the prospect for ICM remains promising.

SECOND QUARTER



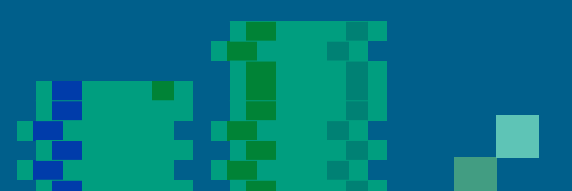
From the second quarter onwards, recovery in global investor sentiments amid monetary and fiscal stimulus measures deployed to combat the pandemic led the ringgit to appreciate by 3.5% against the US dollar, in line with the appreciation of regional currencies. As at end-September, the ringgit recorded a depreciation of 1.6% against the US dollar.

END-SEPTEMBER



Going forward, the expected recovery in the global and domestic economy will provide some support for the ringgit.

GOING FORWARD



CHAPTER 4

Monetary and Financial Developments

Overview

The financial sector remains sound

Monetary and financial conditions have been resilient throughout the COVID-19 pandemic period and supportive of economic recovery. Monetary operations will be supported by vibrant money and foreign exchange markets as well as intermediation activities. The banking sector is expected to remain robust and orderly, underpinned by ample liquidity and strong capital buffers. The capital market will continue to be resilient, driven by well-developed infrastructure and instruments. Nevertheless, concerns over the momentum of global economic recovery due to the pandemic, continued US-China trade tensions, weak commodity prices, and volatile global financial markets may affect financial and capital market performance.

Monetary Developments

Monetary policy mitigates the impact of the pandemic

Monetary policy cushioned the adverse effects of measures implemented to contain the spread of COVID-19 virus on the economy. The policy also provided additional stimulus to sustain the pace of economic recovery. The Overnight Policy Rate (OPR) was reduced successively by 125 basis points (bps) during the first seven months of 2020 to a historic low of 1.75%. Similarly, the Statutory Reserve Requirement (SRR) was reduced by 100 bps from 3.00% to 2.00%. Banking institutions were also given the flexibility to use Malaysian Government Securities (MGS) and Malaysian Government Investment Issues (MGII) to fully meet SRR compliance. The measures were implemented to ensure sufficient liquidity and to support the orderly functioning of the domestic financial market.

The interest rate in the banking system was lowered in line with the OPR adjustment since January 2020. In the first seven months of 2020, the average lending rate and weighted base rate of commercial banks were reduced consecutively to 3.70% and 2.43%, respectively. During the same period, the average interest rate on savings deposit of commercial banks was lowered to 0.48% while fixed deposits of 1-month to 12-month maturities moderated to between 1.53% and 1.79%.

With accommodative monetary policy, monetary aggregates expanded rapidly during the first seven months of 2020. M1 rose by 15.7% to RM497.2 billion, supported by higher currency in circulation and demand deposits which increased by 18.5% and 14.9%, respectively. Similarly, M3 expanded by 6.1% to RM2,029.7 billion, mainly due to higher net

FIGURE 4.1. Monetary Aggregates (% change)



¹ End-July 2020
Source: Bank Negara Malaysia

claims on the Government and extension of credit to the private sector, primarily through securities. The money supply is expected to expand further backed by higher demand for loans and securities by the private sector.

TABLE 4.1. Factors Affecting M3, January – July 2019 and 2020

	CHANGE (RM BILLION)	
	2019	2020
M3	18.8	68.1
Net claims on Government	-10.9	62.8
Claims on Government	18.3	81.9
Less: Government deposits	29.2	19.1
Claims on private sector	37.6	39.3
Loans	26.7	29.4
Securities	10.9	9.9
Net foreign assets ¹	11.2	35.9
Bank Negara Malaysia	10.8	22.0
Banking system	0.4	13.9
Other influences	-19.1	-69.9

¹ Includes exchange rate revaluation losses/gains
 Note: Total may not add up due to rounding
 Source: Bank Negara Malaysia

Performance of Ringgit

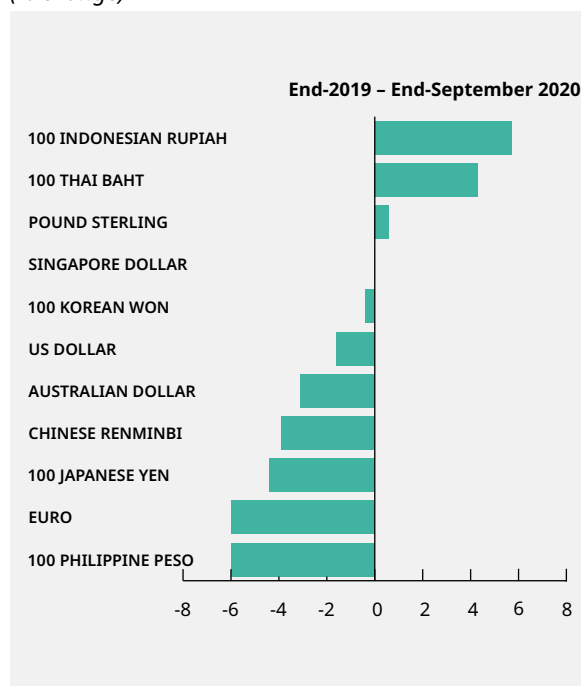
Periods of volatility in the exchange rate

In January 2020, the ringgit appreciated against the US dollar mainly due to non-resident portfolio inflows. This was supported by improved investors’ risk sentiment attributed to positive development in the US-China trade negotiation. However, in February and March, the local note, along with regional currencies, faced significant depreciation against the US dollar. The downward trend of the ringgit was contributed by geopolitical uncertainties, declining commodity prices and rapid escalation of the COVID-19 pandemic.

From the second quarter onwards, recovery in global investor sentiments amid monetary and fiscal stimulus measures deployed to combat the pandemic led the ringgit to appreciate by

3.5% against the US dollar, in line with the appreciation of regional currencies. As at end-September, the ringgit recorded a depreciation of 1.6% against the US dollar. Going forward, the expected recovery in the global and domestic economy will provide some support for the ringgit. However, lingering uncertainties over the COVID-19 pandemic, global political and policy environment could lead to periods of heightened exchange rate volatility.

FIGURE 4.2. Performance of Ringgit against Selected Currencies (% change)



Source: Bank Negara Malaysia

Banking Sector Performance

Resilient banking sector

The capitalisation of the banking sector remained strong, supported by the accumulation of high-quality loss-absorbing instruments. As at end-July 2020, excess total capital buffer¹ remained high at RM121.6 billion. The banking sector remained well-capitalised with Common Equity Tier 1 Capital, Tier 1 Capital and Total Capital Ratios at 14.6%,

¹ Excess total capital buffer refers to the total capital above the banks’ regulatory minima, which also includes the capital conservation buffer (2.5% of risk-weighted assets) and bank-specific higher minimum requirements.

15.1% and 18.3%, respectively. The ratios are well above the Basel III minimum regulatory levels of 4.5%, 6% and 8%, of risk-weighted assets.

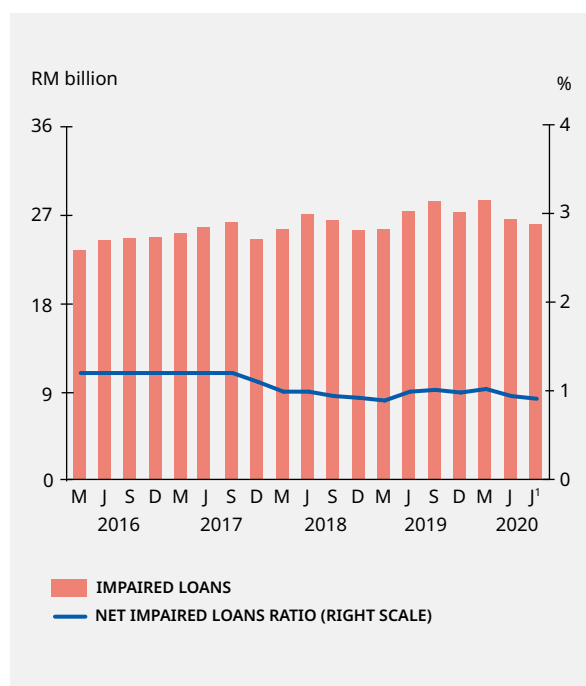
The pre-tax profit of the banking sector fell by 11.7% to RM20.5 billion in the first seven months of 2020. Despite the challenging environment, domestic banks remain strong, supported by orderly financial markets and sustained confidence in the banking sector. As a result, returns on assets and equity continued to be stable at 1.2% and 10.5%, respectively.

The loan quality and liquidity of the banking sector also remain sound. As at end-July 2020, the net impaired loans ratio and loan loss coverage ratio (including regulatory reserves) remained healthy at 0.91% and 121%, respectively. Similarly, the Liquidity Coverage Ratio was at 152%, well above the 100% minimum requirement. Notwithstanding uncertainties and heightened risks from global

financial markets following the fallout from the COVID-19 pandemic and ongoing geopolitical tensions, the banking sector liquidity remains sufficient and stable in the near term.

Lending activities slowed down, reflecting cautious sentiment on the global and domestic growth outlook. In the first seven months of 2020, loan approvals and disbursements fell by 22% and 7.3% to RM185.5 billion and RM657.1 billion, respectively. This was mainly due to financial institutions taking precautionary measures to approve new loans following restricted economic activities. However, total loans outstanding expanded by 4.5% to RM1,806.1 billion as at end-July 2020.

FIGURE 4.3. Banking System: Impaired Loans and Net Impaired Loans Ratio (End-period)



¹ End-July 2020
Source: Bank Negara Malaysia

TABLE 4.2. Banking System: Loan Indicators, January – July 2019 and 2020

	RM BILLION		CHANGE (%)	
	2019	2020	2019	2020
Total¹				
Loans applications	501.3	447.9	-1.7	-10.6
Loans approvals	237.9	185.5	5.8	-22.0
Loans disbursements	709.0	657.1	3.2	-7.3
Loans outstanding ^{2,3}	1,728.8	1,806.1	3.9	4.5
<i>of which:</i>				
Businesses				
Loans applications	203.8	200.9	-0.6	-1.4
Loans approvals	92.2	80.7	2.7	-12.5
Loans disbursements	450.2	430.7	1.0	-4.3
Loans outstanding ³	609.2	633.3	2.6	4.0
Households				
Loans applications	276.3	225.9	-1.6	-18.2
Loans approvals	127.0	88.9	4.1	-30.0
Loans disbursements	197.4	165.3	1.6	-16.3
Loans outstanding ³	981.1	1,024.0	4.8	4.4

¹ Includes foreign entities, other domestic entities, Government and others

² Includes loans sold to Cagamas

³ As at end-period

Note: Total may not add up due to rounding
Source: Bank Negara Malaysia

Loan approvals to businesses decreased by 12.5% to RM80.7 billion as at end-July 2020. Total disbursements to businesses fell by 4.3% to RM430.7 billion, representing 65.5% of total loans disbursed. The bulk of loans were channelled into manufacturing (22.2% of total loans), wholesale and retail trade, restaurants and hotels (19.4%) as well as construction (6.6%) sectors. At the same time, total loans outstanding to the business sector increased by 4% to RM633.3 billion, accounting for 35.2% of total loans outstanding.

Household borrowings slowed down with loan approvals declining by 30% to RM88.9 billion. Loans disbursed to households also declined by 16.3% to RM165.3 billion, mainly for consumption credit (13.1% of total loans), purchase of residential properties (6.3%) and securities (2.7%). As at end-July 2020, total household loans outstanding rose by 4.4% amounting to RM1,024 billion, which accounts for 56.8% of total loans outstanding in the banking sector.

The overall household debt increased by 4% to RM1,265.9 billion, accounting for 87.5% of Gross Domestic Product (GDP) as at end-June 2020. The increase was mainly due to the sharp contraction in GDP during the first half of the year. The bulk of the debt comprises of loans for the purchase of residential properties (55.9%), followed by personal use (14.2%) and passenger cars (12.3%). Total household assets were valued at RM2,751.9 billion with growth in household financial assets continuing to outpace that of debt. Although household debt has risen, it is expected to remain manageable, supported by programmes to rein in the debt level and measures enacted to cushion the impact of the COVID-19 pandemic on the economy.

TABLE 4.3. Banking System: Loans Outstanding by Sector, End-July 2019 and 2020

	RM BILLION		SHARE (%)	
	2019	2020	2019	2020
Businesses	609.2	633.3	35.3	35.2
Non-SMEs ¹	326.9	351.5	19.0	19.5
SMEs	282.3	281.8	16.4	15.6
<i>Selected sectors</i>				
Primary agriculture	34.4	34.7	2.0	1.9
Mining and quarrying	7.9	9.0	0.5	0.5
Manufacturing ²	115.0	122.3	6.7	6.8
Electricity, gas and water supply	13.0	14.7	0.8	0.8
Wholesale and retail trade, restaurants and hotels	127.6	134.4	7.4	7.5
Construction	91.9	91.6	5.3	5.1
Real estate	117.1	119.0	6.8	6.6
Transport, storage and communication	37.2	39.8	2.2	2.2
Finance, insurance and business activities	42.2	43.8	2.4	2.4
Households	981.1	1,024.0	56.9	56.8
<i>of which:</i>				
Purchase of residential properties	551.6	594.4	32.0	33.0
Purchase of non-residential properties	80.4	80.5	4.7	4.5
Purchase of passenger cars	145.1	146.2	8.4	8.1
Consumption credit	133.5	135.4	7.7	7.5
<i>of which:</i>				
Credit cards	38.3	35.3	2.2	2.0
Personal use	95.2	100.1	5.5	5.6
Purchase of securities	68.9	66.1	4.0	3.7
Others	0.4	0.4	0.0	0.0
Other sectors	134.2	144.1	7.8	8.0
Total³	1,724.4	1,801.4	100.0	100.0

¹ Non-SMEs refers to large corporations, including foreign entities, other domestic entities, Government and others

² Including agro-based

³ Total = Businesses + Households + Other sectors

Note: Total may not add up due to rounding

Source: Bank Negara Malaysia

FEATURE ARTICLE 4.1

Digital Banks in Malaysia

Introduction

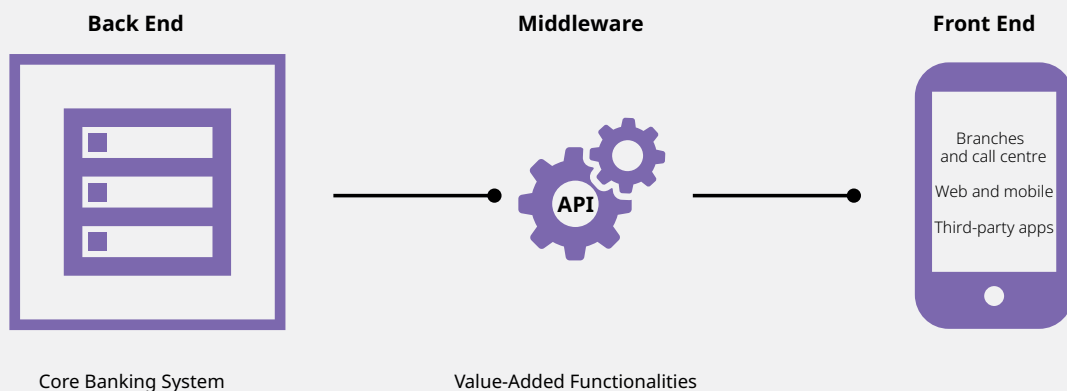
The banking industry has experienced multiple transformations to suit customer demands and keep up with technological advancements, such as secure digital ledger transactions and artificial intelligence (AI). Moreover, the COVID-19 pandemic has forced societies to favour cashless transactions, all of which enable a faster shift towards the establishment of digital banks. A digital bank is essentially a virtual bank, which operates in a digital environment and is devoid of brick-and-mortar presence of a traditional bank. However, digital banks offer similar services to that of traditional banks, such as savings and current accounts, withdrawals and transfers. As such, digital banks are expected to revolutionise the financial landscape by offering financial services through digital and automated platforms (Deloitte, 2020).

Currently, Australia, Brazil, Canada, China, Germany, Hong Kong SAR, Republic of Korea, South Africa, Taiwan, the Philippines, the UK and the US have established their own digital banks (PricewaterhouseCoopers, 2020). Singapore is expected to issue its digital bank licences in 2020. Meanwhile, Bank Negara Malaysia (BNM) is at the stage of finalising the updated Exposure Draft on Licensing Framework for Digital Banks issued on 3 March 2020. With this development, Malaysia looks forward to establishing several digital banks in the near future, paving the way for a more vibrant financial services landscape.

How Does Digital Bank Work?

A digital bank works differently from mobile or online platforms as it requires full digitalisation of banking services. The bank makes use of high-end technology called middleware solution to connect the nodes between front- and back-end processes. The middleware solution bridges the operating systems or databases with other applications while adopting other technologies in its processes (Figure 4.1.1.). Digital banks demand high-end technologies such as Application Programming Interface (APIs), AI Machine Learning, Cloud Computing, Big Data, Cybersecurity, Data Visualisation, User Interface (UI) – User Experience (UX) Design and Blockchain. These technologies allow multilayer processes to be conducted simultaneously across all its delivery channels (Figure 4.1.2.).

FIGURE 4.1.1. *Process Workflow of a Digital Bank*



Source: ATKearney

FIGURE 4.1.2. Key Aspects of a Digital Bank



Cybersecurity

State of being protected against criminal or unauthorised use of electronic data.



Big Data

Extremely large data sets that are analysed computationally to reveal patterns, trends, and associations, especially relating to human behaviour and interactions.



Cloud Computing

Practice of using a network of remote servers hosted on the Internet to store, manage and process data.



Data Visualisation

Describes any effort to help people understand the significance of data by placing it in a visual context.



UI/UX Design

Human-computer interaction, user interface.



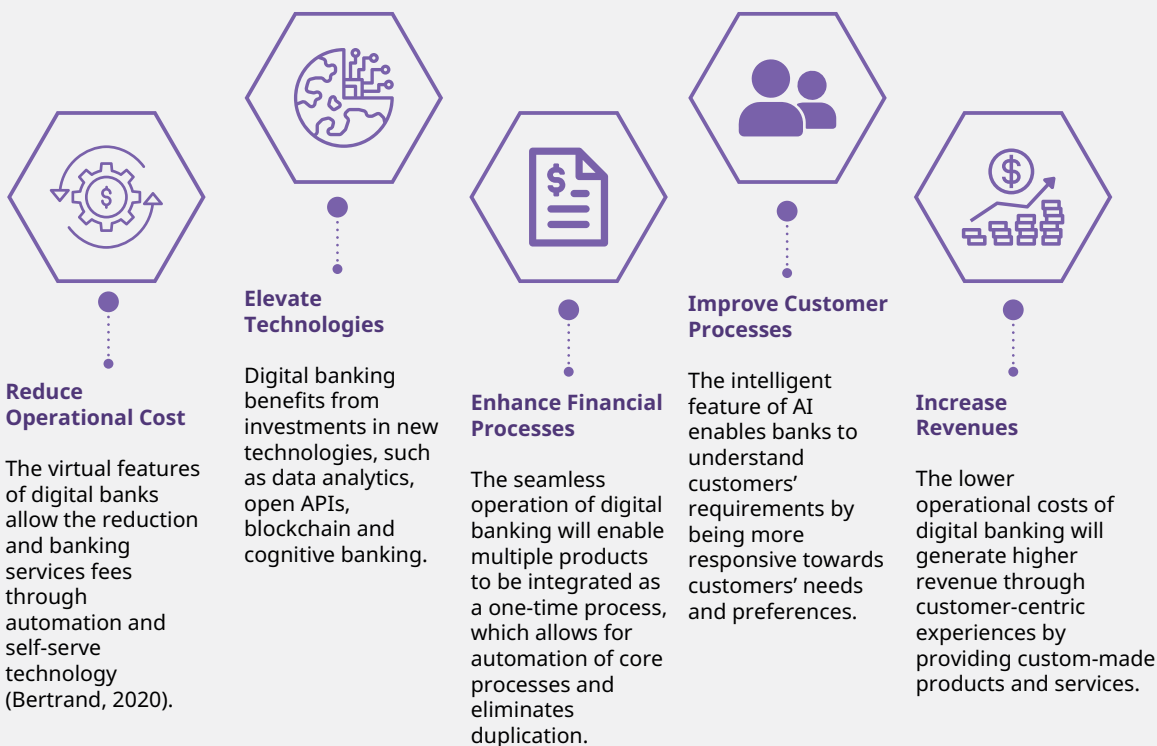
AI Machine Learning

The theory and development of computer systems able to perform tasks normally requiring human intelligence.

Source: Fintalent

FIGURE 4.1.3. Advantages and Disadvantages of Digital Banks

Advantages of Digital Banks



Disadvantages of Digital Banks

Data Protection and Security Issues

- The complete dependency on online services will expose customers with issues such as breach of confidential data as well as cybersecurity threats (Chauhan, 2018).
- Nevertheless, technologies to solve these threats include cloud-based digital banking platforms which have a built-in functionality for constant security upgrades will provide data security for customers.

Workforce related Challenges

- In line with increasing digitalisation within the financial sector, the automation feature of digital banking will reduce the need for human intervention since some of its essential procedures are conducted digitally.
- While some roles may become obsolete in the future, the real concerns would be on tackling the change management, particularly on talent availability issue, which requires a small yet succinct team force with technical knowledge (TM & Akamia Netalliance, 2020).
- According to Comfort (2019), approximately 77,780 jobs were cut by 50 financial regulators globally in 2019 to accommodate for the transition to digital banks. It is also estimated that another 200,000 positions will be displaced in the next decade based on the global trend (Zujev, 2020).

The Future of Digital Banks in Malaysia

Digital bank holds a promising future in Malaysia. The journey towards establishing digital banks will become a reality with digital transformation in the Malaysian financial landscape subjected to three key elements:

Effective Regulatory Ecosystem

The establishment of an effective regulatory ecosystem for digital banks in Malaysia is still in progress. The updated draft by BNM on 3 March 2020 has proposed a balanced approach to enable the admission of digital banks with strong value propositions while safeguarding the integrity and stability of the financial system (BNM, 2020).¹ Through the framework, up to five licences may be issued, subject to applicants' ability to meet the requirements of the Financial Services Act 2013 and the Islamic Financial Services Act 2013.

Strong Technology Backup

Digital banks should adopt and innovate the latest technologies, which leverage cloud systems, APIs, automation and AI Machine Learning. Malaysia is not far off when it comes to digital maturity, as most traditional banks are now adopting the digital approach as part of their business models (TM & Akamia Netalliance, 2020). According to a survey by Finder.com conducted in March 2020, there will be a rise in digital bank adoption in Malaysia with an estimated 8.4 million people likely to open up a digital bank account by 2025 (Cruz, 2020). Similarly, a study conducted by PricewaterhouseCoopers in November 2019 indicated that 74% of Malaysian respondents are interested in becoming a digital bank customer (PricewaterhouseCoopers, 2019).² The move towards complete digitalisation in the financial sector is supported by the National Fiberisation Connectivity Plan. This is also in line with the Communications and Multimedia Blueprint (2018 – 2025) to accelerate the development of a digital economy.

¹ New applicants for digital banks are referred to as challenger banks or entrants (PricewaterhouseCoopers, 2020).

² 1,517 respondents from Malaysia were surveyed for the study (PricewaterhouseCoopers, 2019).

Cultural Adaptation

The road towards digital bank requires digital transformation, mastering new skills, adopting new processes, and changing the way business is being done. Thus, all interested parties need to reform their business models and culture and emphasise on innovation as well as greater adoption of big data analytics to create a customer-centric orientation. The transition to digital banks may not be straightforward, and it could disrupt financial services (Sharko et al., 2017). Traditional banks may also form new ventures and apply for a digital bank licence as part of efforts to reform their business model. The models must also cater to the underserved and unserved segments of society, such as low-income individuals, early income millennials, start-ups as well as small and medium enterprises (SMEs).³

Conclusion

The journey towards the establishment of digital banks is an expected progression in the Malaysian financial market as the country evolves into a digital economy. For the transformation to materialise, a whole new wave of digital products and solutions must be in place. This has to be supported by a robust regulatory ecosystem, innovative technology and cultural adaptation to accelerating economic growth and financial inclusion in Malaysia. Furthermore, the COVID-19 pandemic, which accelerated remote and contactless transactions, provides the impetus for the establishment of digital banks.

³ Refers to groups such as the bottom 40% of household income group (B40) as well as micro enterprises and SMEs, including those in rural and remote areas (Raj, 2020). They are typically underserved due to high servicing cost and low revenue potential.

Capital Market Performance

Fundraising activities to recover

Gross funds raised in the capital market declined by 14.4% to RM143.7 billion during the first seven months of 2020. The lacklustre performance was due to lower fundraising activity in the private sector, which fell significantly by 48.6% to RM45.8 billion. Gross funds raised by the private sector through the domestic equity market declined from RM5 billion to RM0.3 billion. The sharp decline was due to cautious investors' sentiment during the lockdown period.

During the same period, funds raised through new corporate bond issuances also fell by 45.9% to RM45.6 billion. The bulk of issuances were medium-term notes, accounting for 92.1% of total corporate bonds. The majority of funds were raised by finance, insurance, real estate, and business services sector, accounting for 72% of new corporate bond issuances. The funds were mainly allocated for infrastructure

projects, working capital and business activities. On the back of global economic uncertainties and rising geopolitical risks, fundraising in the domestic capital market remains promising buoyed by ongoing and resumption of strategic projects.

Gross funds raised by the public sector increased further by 24.5% to RM97.9 billion during the first seven months of 2020. The expansion was contributed by strong demand for Government papers to support the various stimulus packages. The issuance of MGS rose to RM50 billion, while MGII expanded to RM47.9 billion. During the same period, foreign holdings of MGS and MGII stood at 38.2% and 5.8%, respectively. The holding portfolios indicate that Malaysia's debt market remains attractive to institutional and foreign investors, attributed to its deep, liquid and investor-friendly nature.

During the first seven months of 2020, MGS and corporate bond yields were broadly on a declining trend across all tenures. The lower MGS yields were influenced by the easing of domestic monetary stance given the slower-

than-expected economic growth. Yields on MGS 1-year, 3-year, 5-year, and 10-year declined within the range of 76 and 119 bps. Yields for the corporate bond on the 5-year AAA-rated, AA-rated and A-rated securities also fell between 75 and 77 bps.

TABLE 4.4. Funds Raised in the Capital Market, January – July 2019 and 2020

	RM MILLION	
	2019	2020
Public Sector		
Government securities		
Malaysian Government Securities	38,797.1	49,969.9
Malaysian Government Investment Issues	39,853.7	47,916.4
New issues of debt securities	78,650.8	97,886.3
Less: Redemptions	26,093.4	38,000.0
Net funds raised by the public sector	52,557.3	59,886.3
Private Sector		
Shares¹/Warrants		
Initial Public Offers	1,570.0	292.1
Rights Issues	3,466.7	-
Warrants	-	-
New issues of shares/warrants	5,036.8	292.1
Debt securities²		
Straight bonds	3,090.0	386.5
Convertible bonds	-	-
Islamic bonds	2,944.3	3,200.0
Medium-term notes	78,137.8	41,966.7
New issues of debt securities	84,172.1	45,553.2
Less: Redemptions	41,630.0	29,073.9
Net issues of debt securities	42,542.1	16,479.2
Net funds raised by the private sector	47,578.9	16,771.3
Total net funds raised	100,136.2	76,657.6

¹ Excludes funds raised by the exercise of Employee Share Option Scheme, Transferable Subscription Rights, Warrants and Irredeemable Convertible Unsecured Loan Stocks

² Excludes short-term papers in conventional and Islamic principles

Note: Total may not add up due to rounding

Source: Bank Negara Malaysia

TABLE 4.5. New Issuance of Corporate Bonds by Sector, January – July 2019 and 2020

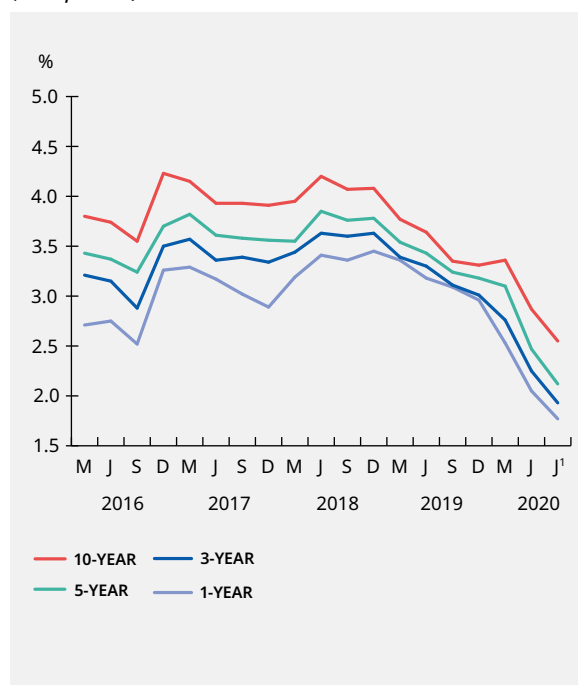
	RM MILLION		SHARE (%)	
	2019	2020	2019	2020
Agriculture, forestry and fishing	50.0	-	0.1	-
Manufacturing	670.0	306.0	0.8	0.7
Construction	1,724.3	4,639.5	2.0	10.2
Electricity, gas and water	4,600.0	3,185.0	5.5	7.0
Transport, storage and communication	32.0	1,120.0	0.0	2.5
Finance, insurance, real estate and business services	70,263.5	32,791.7	83.5	72.0
Government and other services	5,354.9	3,301.0	6.4	7.2
Wholesale and retail trade, restaurant and hotels	1,477.5	210.0	1.8	0.5
Total	84,172.1	45,553.2	100.0	100.0

Note: Includes corporate bonds issued by Cagamas and non-resident corporations

Total may not add up due to rounding

Source: Bank Negara Malaysia

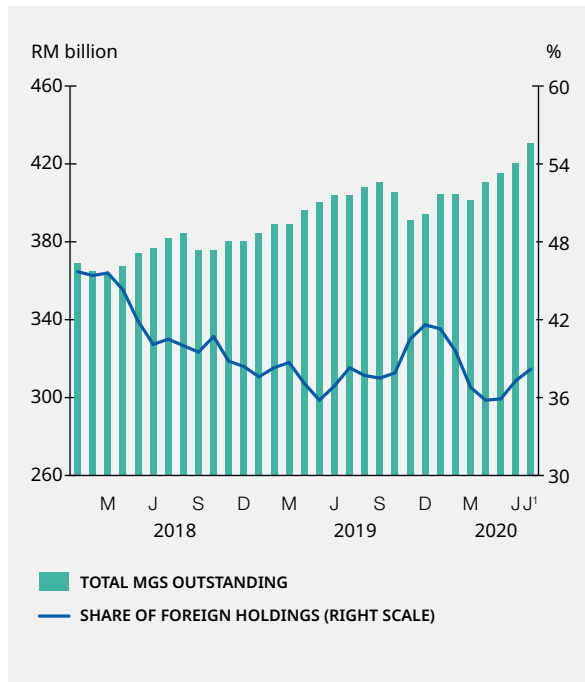
FIGURE 4.4. Malaysian Government Securities (MGS) Indicative Yields (End-period)



¹ End-July 2020

Source: Bank Negara Malaysia

FIGURE 4.5. Share of Foreign Holdings in Total MGS Outstanding (End-period)



¹ End-July 2020
Source: Bank Negara Malaysia

At the beginning of the year, the FTSE Bursa Malaysia Kuala Lumpur Composite Index (FBM KLCI) and other regional indices fell into bearish territory. The local bourse was dragged down below 1,600 points in the second week of January 2020, following the rising geopolitical tensions between the US and Iran. Despite the improvement in the US and China trade deal on 15 January 2020, the FBM KLCI along with major and regional bourses remained on a softer note.

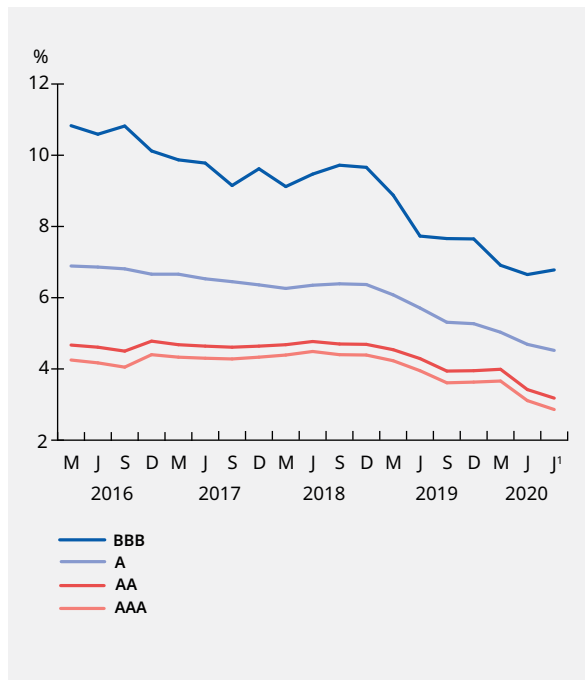
The FBM KLCI was subdued on the back of global economic uncertainties, rising geopolitical tensions, low commodity prices and the spread of the COVID-19 pandemic, which dampened investors' risk appetite. Furthermore, the enforcement of the Movement Control Order (MCO) beginning 18 March 2020 led to panic selling in the equities market. The MCO tapered investors' risk appetite, resulting in the local bourse to hit its decade-low of 1,219.72 points on 19 March 2020.

Nevertheless, the subsequent relaxation of lockdown measures and gradual resumption of economic activities supported the recovery of the local bourse. The FBM KLCI rebounded to 1,575.27 points on 10 June 2020 in tandem with regional markets' optimism amid the upward performance of the Wall Street. In addition, the improvement of the local index was also attributed to the launching of the various stimulus packages announced by the Government to mitigate the impact of COVID-19 pandemic on the economy.

The FBM KLCI started to decline again to 1,488.14 points on 26 June 2020. This was due to the announcements by the Fed, IMF and World Bank on downside risks to global and domestic growth following mounting concerns over the second wave of COVID-19 pandemic. However, the local bourse elevated to reach 1,504.82 points at end-September 2020 upon investors' positive sentiment towards the Government's effort to contain the pandemic despite fresh lockdowns by several countries.

There has been a significant improvement in trading activities in the first nine months of 2020. Total volume and total market transacted value rose by 162.2% to 1,272 billion units and 90% to RM749 billion, respectively. Market velocity was sustained at 62.4%, while market

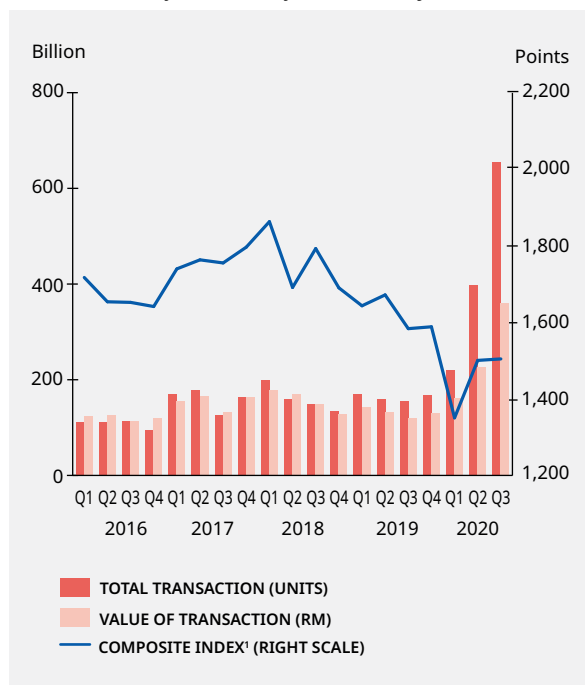
FIGURE 4.6. 5-Year Corporate Bond Yields (End-period)



¹ End-July 2020
Source: Bank Negara Malaysia

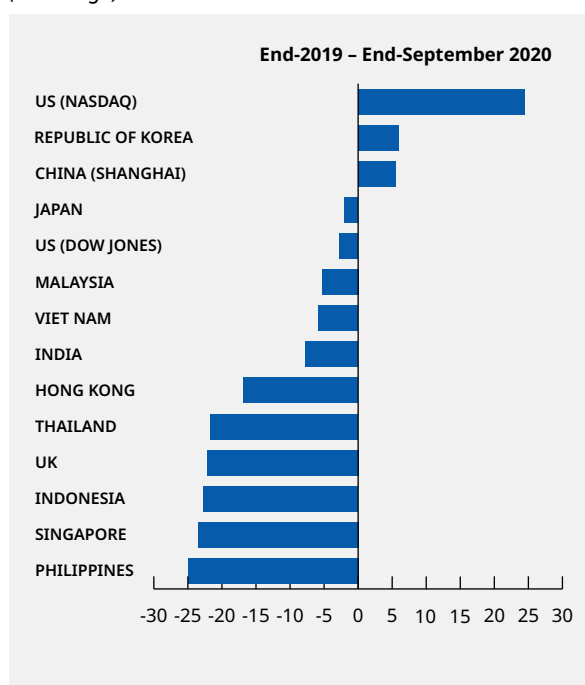
volatility at 36.3%. Foreign holdings based on market capitalisation in the local bourse remained stable at 12.6% as at end-September

FIGURE 4.7. Performance of Bursa Malaysia



¹ As at end-period
Source: Bursa Malaysia

FIGURE 4.8. Performance of Selected Stock Markets (% change)



Source: Bloomberg

2020. Nevertheless, the market capitalisation declined by 2.1% to RM1,638.7 billion as at end-September 2020. The domestic equity market is expected to regain traction following investors' optimistic outlook on the pace of global market recovery and domestic economic growth supported by various strategic projects.

TABLE 4.6. Bursa Malaysia: Selected Indicators, End-September 2019 and 2020

	2019	2020
Indices		
FBM KLCI	1,583.91	1,504.82
FBM EMAS	11,203.71	10,831.56
FBM 100	11,037.83	10,660.70
FBM SCAP	12,978.08	12,835.21
FBM ACE	4,495.12	9,914.01
Total turnover¹		
Volume (million units)	485,046.82	1,271,710.10
Value (RM million)	394,266.47	749,007.22
Average daily turnover¹		
Volume (million units)	2,694.70	6,911.47
Value (RM million)	2,190.37	4,070.69
Market capitalisation (RM billion)	1,673.53	1,638.72
Total number of listed companies		
Main Market	773	765
ACE Market	127	133
LEAP Market	25	34
Market liquidity		
Turnover value/market capitalisation (%)	23.6	45.7
Market concentration		
10 highest capitalised stocks/market capitalisation (%)	33.8	32.0

¹ Based on market transactions and direct business transactions between January and September
Source: Bursa Malaysia

INFORMATION BOX 4.1

Key Capital Market Measures

Several measures were undertaken in the first eight months of 2020 to enhance liquidity and efficiency in the capital market. The measures include:



Islamic Banking and Capital Market Performance

Islamic banking and capital market to persevere

The Islamic banking industry expanded with total assets valued at RM1,038.2 billion² and market share at 33% as at end-July 2020. Meanwhile, the total Islamic financing outstanding increased further by 10% to RM787.8 billion. The growth is primarily contributed by household sector financing, which increased by 8.7% to RM490.9 billion, mainly for the purchase of residential properties. Islamic financing is expected to expand further supported by the recovery in economic activity and continuous promotion of Shariah-compliant products.

The Islamic Capital Market (ICM) continues to thrive with Malaysia being among the largest issuer of sukuk and Islamic equity in the world. As at end-July 2020, the domestic size of ICM was valued at RM2.2 trillion, accounting for 66.2% of RM3.3 trillion of Malaysia's total capital market size. Meanwhile, sukuk issuances amounted to RM130.8 billion or 60.2% of total bonds issuances. Sukuk outstanding was valued at RM986.9 billion or 62.6% of total bonds outstanding. While Malaysia continued to account for the largest share of global sukuk outstanding at 45.6% as at end-June 2020, the turmoil in the global market has affected the performance of the ICM. This was reflected in the subdued performance of corporate sukuk issuances during the initial MCO period. Nevertheless, the reopening of almost all economic sectors in the middle of the year led to the improvement in corporate sukuk performance.

Bursa Malaysia continued to promote Shariah-compliant securities products. As at end-July 2020, a total of 716 or 76.8% of the 932 listed companies was Shariah-compliant. The market

TABLE 4.7. *Islamic Banking: Key Indicators¹, End-July 2019 and 2020*

	RM BILLION		CHANGE (%)	
	2019	2020	2019	2020
Assets	806.5	857.6	11.1	6.3
Financing	594.8	650.3	8.2	9.3
Primary agriculture	16.3	18.6	7.6	13.8
Mining and quarrying	3.7	4.2	-28.1	15.4
Manufacturing ²	27.5	30.3	19.4	10.2
Electricity, gas and water supply	3.4	5.4	26.3	61.5
Wholesale and retail trade, restaurants and hotels	28.0	32.0	18.0	14.2
Construction	35.2	35.3	3.8	0.3
Real estate	28.8	31.6	8.7	9.5
Transport, storage and communication	17.4	20.0	6.5	15.2
Finance, insurance and business activities	31.9	33.8	-10.3	6.0
Education, health and others	20.2	33.7	-4.6	66.8
Households	367.3	399.6	10.7	8.8
Others	15.1	5.7	1.6	-62.1
Liabilities	748.6	794.0	11.2	6.1
Deposits and Investment Account	610.3	633.1	13.6	3.7
Investment	0.7	0.6	-16.1	-19.7
Savings	44.2	58.1	8.1	31.4
Demand	82.7	99.7	11.2	20.5
Investment account	80.6	97.1	6.0	20.5
Others	482.6	474.7	14.6	-1.6

¹ Excluding DFIs

² Including agro-based

Note: Total may not add up due to rounding

Source: Bank Negara Malaysia

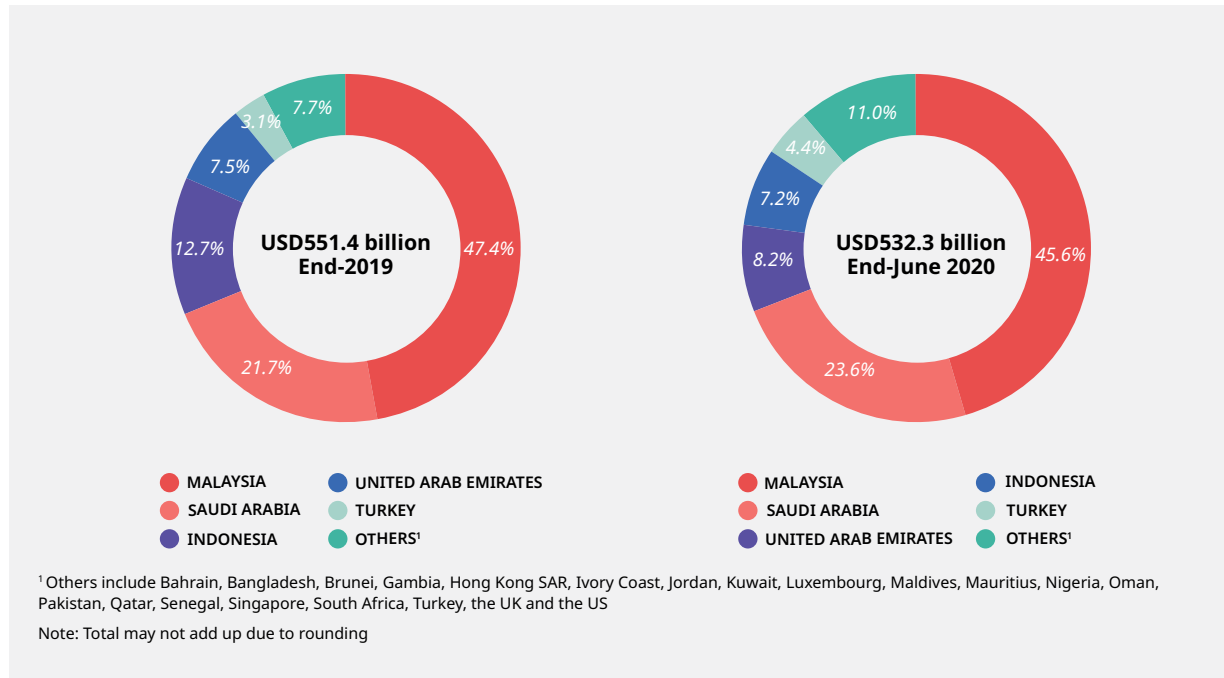
capitalisation of Shariah-compliant securities stood at RM1.18 trillion or 69.5% of the total market capitalisation.

² Includes Development Financial Institutions (DFIs).

Despite the challenging economic climate, the prospect for ICM remains promising. The demand for Shariah-compliant products is expected to be stronger in the future, supported by its appeal to a broader group of investors. The ongoing promotion of

Shariah-compliant products and digitalisation of services will provide the impetus for the country to position itself as a prominent international centre for Islamic financial services.

FIGURE 4.9. Global Sukuk Outstanding by Country (% share)



Source: Malaysia International Islamic Financial Centre

Conclusion

Monetary policy will continue to support economic recovery. The economy is anticipated to improve during the second half of the year and register a sharp turn-around in 2021. The positive outlook will be backed by favourable global growth projection along with a revival in domestic economic activities. In turn, this will bode well for financial market performance. However, the resurgence of

COVID-19 cases, geopolitical tensions and weak commodity prices may pose downside risks to the encouraging outlook. In this regard, various initiatives are being undertaken to ensure the financial market continues to be resilient. These initiatives include promoting green financing instruments, supporting financial platforms driven by digital technology, enhancing knowledge and awareness among investors, and fostering greater collaboration with market players at domestic and international levels.

References

- AT Kearney. (2015). *Going Digital: The Banking Transformation Road Map*. Retrieved from <https://tinyurl.com/y23dwvad>
- Bank Negara Malaysia. (2020). *Annual Report 2019*. Kuala Lumpur. Retrieved from <https://www.bnm.gov.my>
- Bank Negara Malaysia. (2020). *Exposure Draft on Licensing Framework for Digital Banks*. Retrieved from <https://tinyurl.com/y47krph4>
- Bank Negara Malaysia. (2020). *Economic and Financial Developments in the Malaysian Economy in the Second Quarter of 2020*. Retrieved from <https://www.bnm.gov.my>
- Bank Negara Malaysia. (2020). *Economic and Financial Developments in the Malaysian Economy in the First Quarter of 2020*. Retrieved from <https://www.bnm.gov.my>
- Bank Negara Malaysia. (2020). *Financial Stability and Payment Systems Report 2019*. Kuala Lumpur. Retrieved from <https://www.bnm.gov.my>
- Bank Negara Malaysia. (2020). *Monthly Highlights and Statistics July 2020*. Retrieved from <https://www.bnm.gov.my>
- Bank Negara Malaysia. (2020). *Monthly Highlights and Statistics June 2020*. Retrieved from <https://www.bnm.gov.my>
- Bank Negara Malaysia. (2020). *Monthly Highlights and Statistics May 2020*. Retrieved from <https://www.bnm.gov.my>
- Bank Negara Malaysia. (2020). *Monthly Highlights and Statistics April 2020*. Retrieved from <https://www.bnm.gov.my>
- Bank Negara Malaysia. (2020). *Monthly Highlights and Statistics March 2020*. Retrieved from <https://www.bnm.gov.my>
- Bank Negara Malaysia. (2020). *Monthly Highlights and Statistics February 2020*. Retrieved from <https://www.bnm.gov.my>
- Bank Negara Malaysia. (2020). *Monthly Highlights and Statistics January 2020*. Retrieved from <https://www.bnm.gov.my>
- Bertrand, M. (2020). *The Impact of COVID-19 on Malaysia's Looming Digital Banking Revolution*. Retrieved from <https://tinyurl.com/y49jzbqh>
- Bursa Malaysia. (2020). *Bursa Malaysia Amends Main and ACE Market Listing Requirements to Facilitate Application of Specified Corporate Exercises via Electronic Means*. Retrieved from <https://tinyurl.com/y23u764k>
- Bursa Malaysia. (2020). *Bursa Malaysia Amends Main Market and ACE Market Listing Requirements in Relation to New Issues of Securities and other Areas*. Retrieved from <https://tinyurl.com/y48u9zcv>
- Bursa Malaysia. (2020). *Bursa Malaysia Introduces World's First Options Contract on US Dollar Denominated Palm Olein Futures*. Retrieved from <https://tinyurl.com/y2yqc317>
- Bursa Malaysia. (2020). *Bursa Malaysia Launches Bursa Academy for a Unique Experience in Elevating Financial Literacy and Investor Education*. Retrieved from <https://tinyurl.com/y4tjttga>
- Bursa Malaysia. (2020). *Bursa Malaysia Successfully Implements ISO 20022 Messaging Standards for Corporate Announcements*. Retrieved from <https://tinyurl.com/y29qocm9>
- Bursa Malaysia. (2020). *Collaboration between Bursa Malaysia and Shenzhen Stock Exchange to Broaden Opportunities in Investment*. Retrieved from <https://tinyurl.com/y5sg2ubc>
- Bursa Malaysia. (2020). *SC and Bursa Malaysia Implement Temporary Revisions to Market Management and Control Mechanisms*. Retrieved from <https://tinyurl.com/y38qf4yf>
- Bursa Malaysia. (2020). *Taiwan Futures Exchange and Bursa Malaysia Derivatives Berhad Sign Memorandum of Understanding*. Retrieved from <https://tinyurl.com/y22dn6su>

- Chauhan, Y. (2018). *How Important is Digital Banking?* Retrieved from <https://tinyurl.com/y2nk7n5o>
- Comfort, N. (2019). *Banks Set for Biggest Job Cull Since 2015 as Morgan Stanley Cuts*. Retrieved from <https://tinyurl.com/wjj9n88>
- Cruz, P. (2020). *The Rise of Digital Banks*. Retrieved from <https://tinyurl.com/yx8oow79>
- Deloitte. (2020). *Banking on Digital*. Retrieved from <https://tinyurl.com/y5p2us2c>
- Fintalent. (2020). *Future-Enabled Digital Banking Skill Sets You Need to Have*. Retrieved from <https://tinyurl.com/y445vc3d>
- PricewaterhouseCoopers. (2020). *Digital Banking: Malaysian Banks at a Crossroads*. Retrieved from <https://tinyurl.com/y3ousv2z>
- PricewaterhouseCoopers. (2019). *Virtual Banking: Malaysian Customers Take Charge*. Retrieved from <https://tinyurl.com/yywa9398>
- Raj, A. P. (2020). *Is Focus on Underserved Worthwhile for Digital Banks?* Retrieved from <https://tinyurl.com/y2p9uujl>
- Securities Commission Malaysia. (2020). *Annual Report 2019*. Kuala Lumpur. Retrieved from <https://www.sc.com.my>
- Securities Commission Malaysia. (2020). *SC Introduces Enhanced IPO Framework for Main Market*. Retrieved from <https://tinyurl.com/y5xprmoy>
- Securities Commission Malaysia. (2020). *SC Liberalises Regulation on Private Retirement Schemes (PRS) to Enhance Competitiveness of the Industry*. Retrieved from <https://tinyurl.com/y3et5zob>
- Sharko, A. D., Meka, E., Sharko, G. and Baholli, I. (2017). *Digital Banking the Wave of the Future. International Conference Proceedings, ISTI-2016*.
- TM and Akamai Netalliance. (2020). *Transforming Digital Banking in Malaysia: More than a Channel Strategy*. Retrieved from <https://tinyurl.com/y26aupp6>
- Zujev, A. (2020). *The Road to True Digital Bank*. Retrieved from <https://tinyurl.com/y6qhpmlj>