9 Developments in the Financial System

Monetary Policy

The overall objective of monetary policy in 1996 is to ensure price stability as it is only in an environment of price stability that the growth process will continue. An important element of policy is also to ensure stability in the domestic money and foreign exchange markets so as to create a predictable and stable economic environment for the private sector. This would also allow the transmission mechanism for monetary policy measures to be given the opportunity to achieve the medium- and longer-term objectives. In this endeavour, the thrust of monetary policy in the first eight months of 1996 continued to be directed at the management of excess liquidity in order to ensure that inflationary pressures arising from excess demand did not become a source of instability that could derail the growth process.

In formulating the strategy for monetary policy during the period, consideration was given to several issues, particularly the strong credit and monetary expansion, in the face of rising inflationary pressures. In the first four months of 1996, monetary growth remained high, with the annual growth of the broader monetary aggregate, M3, accelerating to 27% at the end of April from 22.3% at the end of 1995. The higher M3 was caused mainly by increased lending to the private sector. The annual growth in total loans extended by the banking system continued to rise to peak at 30.1% at the end of April (28.6% at the end of 1995). Of the increase in loans, more than half was channelled to the less productive sectors of the economy, namely the broad property and finance, insurance and business services sectors and for consumption purposes. The trend, if left unchecked, would fuel asset price inflation, in particular in the property sector, build up excess demand which would intensify inflationary pressures and undermine the future growth process as less funds would be available for productive sectors. Given this development as well as Bank Negara Malaysia's (BNM) commitment to achieving price stability, monetary policy was tightened further in the first quarter of 1996 and again in the second quarter, resulting in higher interest rates. In addition, banking institutions were discouraged from lending excessively for less productive activities.

BNM actively managed the liquidity situation through a combination of direct and indirect instruments. Instruments included accepting deposits in the interbank market, centralising the excess funds of the Government and the Employees Provident Fund with BNM and the statutory reserve requirement (SRR). During the period under review, the SRR of the banking institutions was raised on two occasions by one percentage point each, from 11.5% to 12.5% effective 1 February and to 13.5% from 1 June, reflecting the continuing commitment of BNM in containing the rate of credit and monetary expansion, and hence, inflationary pressures. The SRR increases absorbed a total of RM5.4 billion.

Complementing the liquidity operations of BNM was the upward adjustment in interest rates in the first eight months of 1996 consequent to monetary tightening. The higher interest rates were evident from the three-month interbank rate, which rose from 6.76% at the end of December 1995 to 7.33% at the end of August 1996. Similarly, deposit and lending rates offered by the banking institutions edged upwards. The higher deposit rates helped to promote savings and ensure that the trend of a high rate of savings in the country was sustained. In the foreign exchange market, the ringgit exchange rate was left to adjust to market forces, with intervention operations essentially undertaken to eliminate destabilising influences and achieve a stability in trend. As such, the exchange rate reflected the underlying economic fundamentals. In the first eight months, the ringgit strengthened against all the major currencies. The ringgit strengthened by 7.3% against the Japanese yen, 1.8% against the US dollar and 1.3% against the Singapore dollar.

The above monetary measures, together with the credit measures implemented in October 1995 on hire-purchase financing and credit to the property sector helped to moderate somewhat the growth in credit and in money supply. The annual growth of loans extended by the banking system moderated from 30.1% at the end of April to 27.5% at the end of August, while the annual growth of M3 slowed down from 27% to 21.8% during the same period. However, in view of the risks for demand pressures for the rest of 1996, the present stance of monetary restraint will be maintained. Monetary policy will continue to accord priority to the management of the prevailing excess liquidity situation in order to ensure that excess demand does not worsen inflationary pressures. BNM will monitor closely developments in credit and monetary growth, particularly lending for less productive activities. While ensuring that funds are utilised effectively, policy will concomitantly be aimed at the effective mobilisation of savings. Also of significance is the development of the financial infrastructure as part of the commitment of BNM to deepen and broaden the financial sector as well as to enhance the effectiveness of the transmission of monetary policy.

It is, however, recognised that monetary policy can only address inflationary pressures arising from excess demand. Hence, monetary policy will be reinforced with other macroeconomic policies to deal with inflationary pressures arising from supply shortages and imperfections in the distribution system. In this respect, supply-side policies, together with policies to enhance efficiency, will be implemented and coordinated.

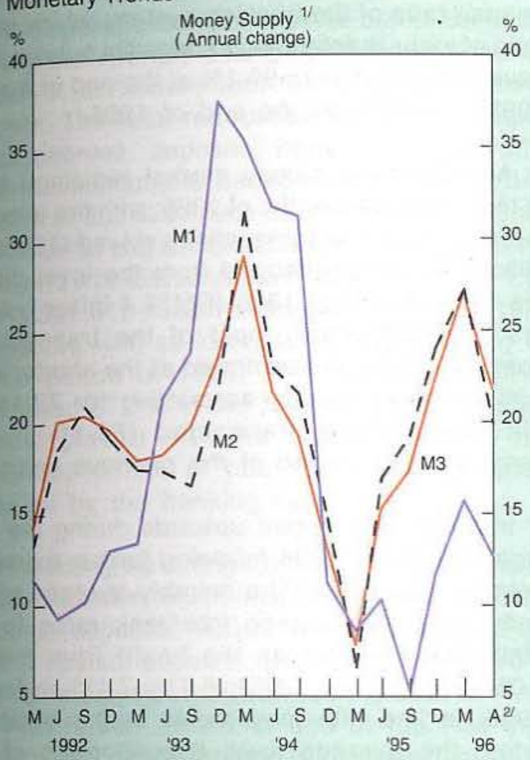
Money Supply

Growth in money supply during the first eight months of 1996 reflected the effects of further monetary tightening by BNM. After accelerating in the first four months of 1996, the annual growth of all the key monetary aggregates, that is M1, M2 and M3, slowed down in the following months. By the end of August, the annual growth rates of M1 and M3 were at about the levels prevailing at the end of 1995, while M2 growth was below that at the end of 1995. The expansion was underpinned mainly by increased lending to the private sector.

Narrow money, M1, which is defined to include currency in circulation and demand deposits of the private sector recorded a higher growth of 7% in the first eight months (6.1% during the corresponding period of 1995). The higher M1 reflected the continued demand for transactional balances, of both demand deposits and currency in circulation, consistent with sustained economic activities. While demand deposits rose by 7.3%, at the same rate as in the corresponding period of 1995, currency in circulation rose by 6.3% (an increase of 3.7% during the same period of 1995). On an annual basis, the growth of M1 accelerated from 11.7% at the end of 1995 to 17% at the end of April 1996, before moderating to 12.7% at the end of August.

The growth of broad money, M2, which consists of M1 and narrow quasi money (comprising private sector holdings of fixed and savings deposits with the commercial banks and BNM, net negotiable instruments of deposit (NIDs) and repurchase agreements (repos)), slowed down to increase by 10.5% (14.3% during the corresponding period of 1995). The slowdown was largely due to the relatively slower growth in quasi money of 11.7% (January-August 1995: 17.6%), reflecting mainly the substantially smaller increase in NIDs and repos of RM1.2 billion or 4.3% (RM4.4 billion or 22.6% in the same period of 1995). Growth in savings deposits was higher at 4.4% whereas fixed deposits grew at a slower pace of 15.6% (2.1% and 20.9% respectively during the corresponding period in 1995). Despite the slower rate of increase, fixed deposits remained the leading contributor to the rise in quasi money (87.2%), followed by repos (10.6%) and savings deposits (6%). There was a net repayment of NIDs (-3.8%). On an annual basis, after accelerating to 27.9% at the end of April 1996 (end-1995: 24%), M2 growth slowed down to 19.9% at the end of August.

Chart 9.1
Monetary Trends



1/ End of March, June , September and December including Repurchase Agreements (Repos)
2/ As at end of August 1996

During the first eight months of 1996, the broader monetary aggregate, M3, which comprises M2 and private sector deposits (including repos) placed with other banking institutions, namely, finance companies, merchant banks, discount houses and Bank Islam, but excluding the placements of funds among these institutions, increased at a slower pace of 12.6% (13.1% during the corresponding period of 1995). Compared with the corresponding period in 1995, the growth of private sector deposits placed with other banking institutions excluding interplacements almost doubled, rising by 18.2% (January-August 1995: 9.9%). Of particular significance was the rapid expansion in fixed deposits, which was more than double that of the corresponding period in 1995, attributable to the more attractive rates of returns offered, when compared with the commercial banks. On an annual basis, M3 grew strongly in the first four months of 1996 to peak at 27% at the end of April, before slowing down to 21.8% at the end of August (22.3% at the end of 1995).

The growth of M3 during the first eight months of 1996 emanated mainly from **lending to the private sector,** which rose by RM47 billion (RM39 billion during the corresponding period of 1995). A notable development was increased lending by the banking system for less productive activities (58% of the increase in total loans; 48.2% in the corresponding period of 1995), with loans channelled to the broad property and finance, insurance and business services sectors and for consumption purposes amounting to RM9.8 billion, RM8.4 billion and RM5.3 billion respectively. The manufacturing sector, in the meantime, received RM5.3 billion worth of credit. In line with the momentum of the stock market, loans extended to individuals for the purchase of shares and units of unit trusts grew by RM1.1 billion during the first eight months of 1996.

The growth in monetary aggregates was also supported, although to a smaller extent, by **Government budgetary operations**, which were expansionary by RM2 billion in the first eight months of 1996 (-RM2.7 billion in the corresponding period of 1995). This was mainly accounted for by higher Government borrowings (RM3 billion), which more than offset the increase in its deposits (RM1 billion).

Bank Liquidity and Money Market

During the first eight months of 1996, liquidity in the banking system continued to remain ample. As a result, monetary policy was directed at the management of excess liquidity so as to contain excess aggregate demand and inflationary pressures and, thereby, ensure a sustainable pace of growth. Managing excess liquidity was also crucial in order to reduce the potential for credit expansion as lending was the major determinant fuelling the growth of money supply during the period.

To effectively manage liquidity, BNM conducted its liquidity operations by using a combination of traditional and market-based instruments. BNM was most active in its liquidity operations through direct borrowing from the money market as a means to fine-tune liquidity. In addition, BNM rolled over most of its Bank Negara Bills (BNBs) which matured during the period. BNM also raised the SRR of the banking institutions twice by one percentage point in February, from 11.5% to 12.5%, and then again to 13.5% in June 1996, as a more permanent measure to absorb the excess liquidity. Other measures included the continued centralisation of vostro accounts and the excess funds of the Government and the Employees Provident Fund with BNM. Reflecting the impact of these measures, domestic interest rates firmed, thereby helping to restrain credit and monetary growth.

The ample liquidity situation in the banking system was reflected in the growth of the monetary aggregates, loan-deposit surplus of the banking system and holding of excess liquid assets by the banking system (holdings in excess of the mandatory requirement of 17% for commercial banks and 10% to 12.5% for finance companies and merchant banks). Monetary growth, which had accelerated in the first quarter, slowed down subsequently, although it remained strong. By the end of August, the growth of M1, M2 and M3 were 12.7%, 19.9% and 21.8% respectively. In addition, the banking system experienced a loan-deposit surplus of RM1 billion in the first eight months, compared with a resource gap of RM2.3 billion over the same period in 1995. There was also an inflow of funds from abroad as investors sought higher rates of return. Reflective of this, the net external liabilities of the banking system increased by RM8 billion during the first eight months (RM1.2 billion in the corresponding period of 1995). Meanwhile, the excess liquid assets of the banking system rose from RM1.5 billion at the end of 1995 to RM2 billion at the end of August 1996.

During the first eight months of 1996, total loans and advances of the banking system increased markedly by RM40.5 billion (16.1%) to RM292.3 billion at the end of August 1996 (January-August 1995: RM33.4 billion or 17.1%). The bulk of the increase in loans was mainly extended to the broad property and the finance, insurance and business services sectors and for consumption purposes, as well as to the manufacturing sector. Total deposits (including repos) of the banking system concomitantly recorded strong growth, rising by RM41.4 billion (14.7%) from the end of 1995 to RM324.3 billion at the end of August 1996 (RM31.1 billion or 13.4% in the corresponding period of 1995). The bulk of the increase in deposits was mobilised by the commercial banks (55.1%) and finance companies (34.8%). By type, fixed deposits accounted for the largest portion (70.3%) of the increase in total deposits. As deposits grew faster than loans, the banking system experienced a loan-deposit surplus of RM1 billion. The loan-deposit ratio of the banking system, which is the ratio of loans outstanding to deposits outstanding, nevertheless, rose to 90.1% at the end of August 1996 from 89% at the end of 1995.

Activity in the money market remained brisk in the first eight months of 1996, with the average monthly volume of transactions valued at RM69.8 billion, almost unchanged from the level during the same period in 1995 (RM71.4 billion). As in the previous years, most of the transactions continued to be concentrated at the shorter-end, with overnight money accounting for 73.1% of the total volume transacted (60.1% in the corresponding period of the previous year).

Interest rates edged upwards during the first eight months of 1996 following further monetary tightening by BNM. The monthly average of the daily weighted average interbank rates for all maturities rose across the board from 6.47%-7.05% in December 1995 to 6.61%-7.43% in August 1996. In line with movements in the interbank rates, the average fixed deposit rates of the commercial banks and finance companies across the maturity spectrum were higher by 37-64 and 40-60 basis points, ranging between 7.15%-7.26% and 7.25%-7.38% at the end of August. Reflecting the higher cost of funds, the average base lending rates (BLR) trended upwards. The average BLR of the commercial banks increased from 8.03% at end of 1995 to 9.25% at the end of August 1996, while that of the finance companies rose from 9.38% to 10.62% over the same period.

Meanwhile, **external sector operations** contributed a contractionary influence on M3. Reflecting the improved external balance, the net international reserves of BNM recorded an increase of RM3.7 billion during the first eight months, amounting to RM67.5 billion at the end of August. The net external liabilities of the banking system, on the other hand, increased by RM6.4 billion during the period. Consequently, the external operations of the non-bank private sector were contractionary by RM2.7 billion (-RM3.2 billion during the same period of 1995). 'Other influences', representing residual factors, were contractionary by RM12.1 billion during the first eight months of 1996, mainly due to higher paid-up capital and reserves, undistributed profits and acceptances payable of the banking institutions.

Commercial Banks

The operations of commercial banks continued to expand strongly during the first eight months of 1996, consistent with the pace of economic growth. The **total resources** (inclusive of capital and reserves, deposits, borrowings from other financial institutions, bankers' acceptances (BAs) and other liabilities such as interest-in-suspense, provision for bad and doubtful debts and borrowings from and bills discounted with BNM) rose by 11.9% to RM327,015 million at the end of August 1996, compared with an increase of 13.7% during the same period of 1995. The commercial banks mobilised 67.7% of the total deposits (including repos) placed with the banking system and extended 68.9% of total loans and advances granted by the banking system.

Reflecting the strong expansion in the economy, **total deposits**, which includes current, fixed and savings deposits, NIDs, New Investment Fund (NIF), special deposits and repos, mobilised by the commercial banks recorded a growth of 11.6% to RM219,689 million at end of the first eight months of 1996, compared with a growth of 14.0% during the corresponding period of 1995, as indicated in Table 9.1. The growth in total deposits reflects the firming of the interest rates during the period under review. A major proportion of new deposits was placed by other customers (which accounted for RM11,757 million or 51.5% of the total new deposits), followed by business enterprises (RM6,883 million or 30.1%) and the Government and statutory authorities (RM4,371 million or 19.1%). However, there was a significant decline (RM1,920 million) in deposits placed by the financial institutions.

The strong demand for credit by the private sector saw sustained growth in total **loans and advances** (excluding housing loans sold to Cagamas Berhad) of commercial banks which increased by 15.1% during the first eight months of 1996 to RM201,483 million at the end of August 1996, compared with 19.8% during the same period of 1995, as indicated by Table 9.2. During this period, a substantial proportion of new loans (48.3% or RM12,778 million) was channelled to the less productive sectors of the economy, with RM6,296 million or 23.8% of the total new loans and advances being extended to the broad property sector, RM5,643 million or 21.3% to the finance, insurance and business services sectors and

Table 9.1

Commercial Banks: Deposits

	Change During Period				As at end of August 1996
	1995 January-August		*1996 January-August*		
	RM million	*%*	*RM million*	*%*	*RM million*
Demand deposits	2,889	9.1	2,813	7.8	39,114
Savings deposits	452	2.1	1,040	4.4	24,522
Fixed deposits	16,009	20.6	16,043	15.7	118,253
NIDs[1]	2,034	10.5	1,180	4.8	25,721
Repos	999	10.9	1,748	18.1	11,360
Others[2]	97	20.7	14	2.0	719
TOTAL	22,480	14.0	22,838	11.6	219,689

[1] Negotiable instruments of deposit.
[2] Include New Investment Fund and special deposits.

Source: BNM.

Table 9.2

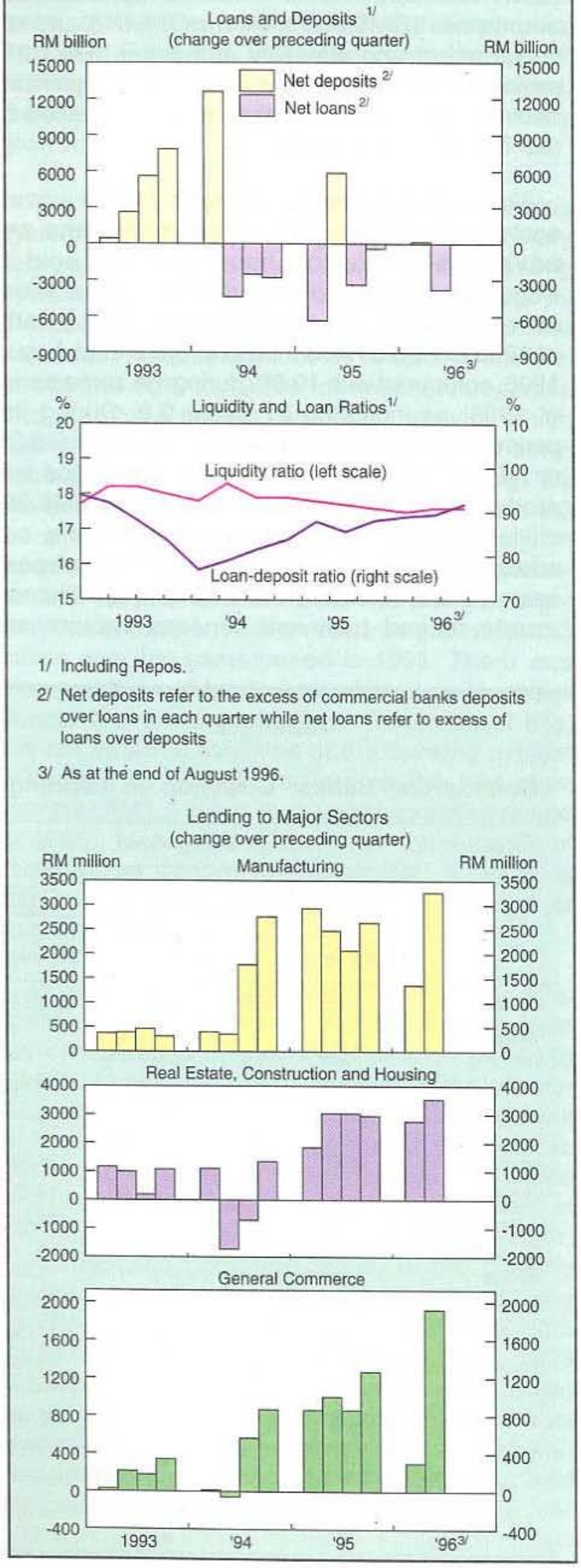
Commercial Banks: Direction of Lending

	Change During Period				As at end of August 1996
	1995 January-August		*1996 January-August*		
	RM million	*%*	*RM million*	*%*	*RM million*
Agriculture	32	0.9	413	10.8	4,273
Mining and quarrying	398	76.4	-229	-25.8	657
Manufacturing	7,723	23.9	4,619	10.9	46,963
Finance, insurance and business services	3,331	19.6	5,643	23.8	29,350
Construction	2,090	20.1	3,172	22.7	17,167
General commerce	3,204	21.3	2,218	11.6	21,261
Transport and storage	258	10.6	512	17.2	3,498
Real estate	3,143	29.1	2,782	18.1	18,145
Housing[1]	1,528	10.8	342	2.0	17,083
Miscellaneous	4,790	17.3	7,004	19.4	43,086
TOTAL	26,497	19.8	26,476	15.1	201,483

[1] Excluding loans sold to Cagamas Berhad.

Source: BNM.

Chart 9.2
Commercial Banks



RM839 million or 3.2% for consumption credit. Meanwhile, total loans extended to the manufacturing sector increased by 10.9% during the first eight months of 1996 to RM46,963 million as at end August 1996, compared with 23.9% during the same period of 1995. Loans extended for the purchase of stocks/shares increased significantly by 18.3% from the end of 1995 to RM9,505 million at the end of August 1996 (a decline of 0.02% during the same period of 1995), reflecting the number of new issues in the equity market.

Reflecting the faster growth in loans and advances (15.1%) compared with the growth in deposits (11.6%), commercial banks recorded a lower loan-deposit gap of RM3,638 million during the first eight months of 1996, compared with RM4,017 million during the corresponding period of 1995. As a result, the **loan-deposit ratio** of the commercial banks increased from 88.9% at the end of 1995 to 91.7% at the end of August 1996.

The commercial banks continued to extend credit to the **priority sectors** of the economy, namely the Bumiputera business community, purchases of houses each costing RM100,000 and below and to small-scale enterprises (SSEs) under the New Principal Guarantee Scheme (NPGS) of the Credit Guarantee Corporation (CGC). In March 1996, the 1996 Lending Guidelines were issued by way of an extension to the previous Guidelines which expired on 31 March 1996. Under the new Guidelines, commercial banks were required to secure at least RM1 billion (RM350 million, previously) guarantee cover from CGC on loans below RM500,000 each, of which at least one-half of the allocated quota has to be extended to Bumiputera borrowers. In respect of lending to Bumiputera community, the quota was increased from 20% of the loan base to 30%, with effect from 31 March 1996. Commercial banks are also required to finance the purchase of at least 100,000 units (75,000 units, previously) of houses each costing RM100,000 and below. The compliance date for the above Guidelines is 31 March 1998, with one-half of the minimum requirement to be complied with by 31 March 1997.

During the first eight months of 1996, loans extended to the **Bumiputera community** increased by 14.9% or RM7,353 million, compared with 13.3% during the corresponding period of 1995. Total loans extended to the Bumiputera community amounted to RM56,849 million or 31.2% of the loan base (31 December 1995) as at end of August 1996. The loans were extended mainly to the broad property sector (RM17,435 million), finance, insurance and business sectors (RM12,140 million) and for the purchase of stocks/shares (RM6,835 million). Commercial banks also made firm commitments in financing the purchase of 19,199 units of houses each costing RM100,000 and below or 19.2% of the target (100,000 units of such houses). Total loans extended by the commercial banks to the SSEs under the NPGS of the CGC increased to RM400 million at the end of August 1996 (RM228 million at the end of August 1995), while loans approved under the Loan Fund for Hawkers and Petty Traders (LFHPT) increased by 54.0% to RM115.5 million (of this, RM63.2 million were granted to Bumiputera borrowers).

Reflecting the tight monetary policy pursued by BNM, the mode interest rate of commercial banks' fixed deposits exhibited an upward trend registering an increase of 0.20 to 0.60 percentage point during the first eight months of 1996. The mode fixed deposits rates for one-month and three-month maturities increased from 6.50% and 6.60% per annum, respectively at the end of 1995 to 7.10% and 7.15% per annum, respectively at the end of August 1996. Similarly, the six-month rate increased to a range of 7.15% to 7.30% per annum at the end of August 1996 from 6.70% per annum at the end of 1995, while the twelve-month rate increased to 7.20% per annum from 7.00% per annum at the end of 1995. The mode savings deposits rate increased by 0.25 percentage point to 3.50% per annum at the end of August 1996 from 3.25% per annum at the end of 1995. In the interbank money market, the increase in the daily weighted average interbank rates for all maturities ranged between 6.61% to 7.43% per annum at the end of August 1996 from a range of 6.47% to 7.05% per annum at the end of 1995. In consonance with the increase in the interbank money market rates, the average cost of funds rose by 1.20 percentage points to 5.87% per annum at the end of August 1996 from 4.67% per annum at the end of 1995. Similarly, the average lending rate increased from 9.28% per annum at the end of 1995 to 10.17% per annum at the end of August 1996.

As the average cost of funds grew faster relative to the growth in the average lending rate, the gross interest margin narrowed by 0.31 percentage point from 4.61% per annum at the end of 1995 to 4.30% per annum at the end of August 1996. The mode BLR of the commercial banks rose to 9.35% per annum at the end of August 1996 from 8.20% per annum at the end of 1995, reflecting the upward trend in the cost of funds.

The **Export Credit Refinancing (ECR)** scheme was launched in 1977 to promote the export of manufactured goods and selected commodities. BNM provides financing at a preferential rate of interest to eligible direct and indirect exporters via commercial banks. Total ECR financing declined significantly by 30.2% during the first eight months of 1996 to RM8,060 million at the end of August 1996, compared with an increase of 25.0% during the corresponding period of 1995. Of this, RM4,148 million was for post-shipment and RM3,912 million for pre-shipment. The bulk of credit was for palm oil (RM2,425 million or 30.1% of the total new credit), mechanical and electrical products (RM1,825 million or 22.6%) and rubber products (RM1,179 million or 14.6%). Reflecting the upward trend of interest rates in the local money market, particularly the BAs rates, the rate of ECR financing was increased from 7.25% per annum to 7.70% per annum, effective from 1 April 1996.

As at end of August 1996, the number of commercial banks operating in the country remained at 37, of which 23 were domestic banks and 14 were foreign-controlled banks. The total number of branch offices of domestic banks increased from 1,362 at the end of August 1995 to 1,500 at the end of August 1996, while that of foreign-controlled banks remained unchanged at 144. As at end of August 1996, 11 commercial banks had been accorded Tier-I status. As Tier-1 commercial banks, they are allowed to undertake the following activities subject to prudential limits and conditions determined by BNM, effective from 26 July 1996:

(i) issue NIDs up to five times of their capital funds;

(ii) participate in equity derivatives;

(iii) undertake securities borrowing and lending activities but subject to Securities Commission approval; and

(iv) expand their operations through setting up of branch offices, representative offices, subsidiaries or on joint venture basis.

Islamic Banking

Islamic banking experienced yet another year of strong growth with an increasing number of financial institutions offering Islamic banking services under the Interest-free Banking Scheme (IBS). At the end of July 1996, apart from Bank Islam Malaysia Berhad (BIMB), a total of 46 financial institutions (24 commercial banks, 19 finance companies and three merchant banks) were offering Islamic banking services under the IBS compared with 21 commercial banks, 15 finance companies and three merchant banks operating the IBS at end of July 1995. Total assets of the Islamic banking system (IBS and BIMB) increased by 19.0% during the first seven months of 1996 to RM6,604 million at the end of July 1996 (July 1995: RM5,970 million). Total deposits mobilised by the Islamic banking system surged 14.6% from end of 1995 to RM5,644 million at the end of July 1996, while total financing gained 50.8% to RM5,155 million. The bulk of the new deposits emanated from general investment deposits (28.6%) and specific investment deposits (9.7%), amounting to RM2,801 million and RM500 million, respectively. At the same time, savings deposits and demand deposits increased significantly by 25.6% and 21.3%, respectively. In terms of sectoral breakdown, 26.4% of the new financing was extended to the construction and real estate sectors (RM458 million), while 15.0% was extended to the housing sector (RM261 million) and 7.5% to the transport and storage sector (RM131 million). Transactions in the Islamic Interbank Money Market (IIMM) recorded an increase of RM27,071 million during the period. The transactions of Islamic BAs amounted to RM2,460 million at the end of July 1996, while Green BAs amounted to RM9,513 million. In order to further increase the transactions of IIMM, BNM introduced four more measures with effect from 2 February 1996. These measures are:

(i) **Minimum benchmark for the Mudharabah Interbank Investment (MII)**

IIMM participants were required to peg their rates to a minimum benchmark prescribed by BNM. At present, the minimum benchmark is the Malaysian Government Investment Issues plus a spread of 0.5%.

(ii) **Central Bank intervention via MII**

BNM may conduct its money market operations via MII as and when the situation warrants in order to provide liquidity in the market as well as to influence the overall liquidity situation in the banking system.

(iii) **Trading practices in the MII**

The money brokers were required to carry out the function as intermediaries to match the requirements of the surplus unit ("lender") and the deficit unit ("borrower") of the MII. These brokers were expected to facilitate active trading in the MII by providing a structured profit-sharing ratio mechanism, whereby both the deficit and surplus units of the MII will be required to place their bid and offer through the money brokers.

(iv) **Lender of last resort**

BNM will take the role as the lender of last resort on the basis of Al-Mudharabah. A flat rate penalty of RM2,000 will be imposed if the IIMM participants borrow funds from BNM more than three times in a week. In addition, the profit sharing ratio has been increased from 70:30 to 95:5 (95% for the provider of funds).

To further boost Islamic banking, BNM has set in motion the establishment of a central 'syariah' advisory council by end of this year. The council will act as a central coordinating secretariat and reference centre on 'syariah' issues relating to Islamic banking and finance. The council which is to be based in BNM will be the reference centre as well as the regulatory body for 'syariah' matters. A major impetus to the development of Islamic banking was the launching of the first published Islamic index in the Asian region on 10 May 1996. The index, called RHB Islamic Index, is based on 'syariah' principles and comprises 179 'syariah' approved counters. The Kuala Lumpur Stock Exchange (KLSE) is also preparing an Islamic index comprising Islamic companies as classified by the Securities Commission.

Finance Companies

The performance of finance companies continues to improve, reflecting the strong demand for financial services in an expanding economy. **Total resources** (comprising mainly capital and reserves, deposits and borrowings from other financial institutions) mobilised by finance companies increased by 18.6% from the end of 1995 to RM108,964 million at the end of August 1996, compared with 13.5% during the corresponding period of 1995. **Total deposits** (including repos) mobilised by finance companies also rose by 20.6% to RM84,383 million at the end of August 1996 (January-August 1995: 12.3%), as indicated in Table 9.3, mainly due to the higher interest rates offered for deposits. Similarly, **total loans** extended by finance companies increased by 18.4% to RM74,293 million at the end of August 1996, compared with a growth of 13.2% during the same period of 1995.

Table 9.3

Finance Companies: Deposits

	Change During Period				*As at end of August 1996*
	1995 January-August		*1996 January-August*		
	RM million	*%*	*RM million*	*%*	*RM million*
Savings deposits	–459	–8.3	–196	–4.0	4,703
Fixed deposits	4,960	11.0	10,779	19.8	65,193
Special deposits	5	14.6	3	4.3	72
NIDs[1]	1,642	29.9	3,733	42.9	12,444
Repos	875	80.2	101	5.4	1,971
TOTAL	7,023	12.3	14,420	20.6	84,383

[1] Negotiable instruments of deposit.

Source: BNM.

During the first eight months of 1996, total new deposits mobilised by finance companies increased by RM14,420 million, compared with an increase of RM7,023 million during the corresponding period of 1995. In terms of deposits by holders, the major depositors were other customers (41.8% of total outstanding deposits), financial institutions (23.8%), business enterprises (21.1%) and the Government and statutory authorities (11.0%). The bulk of the new deposits was in the form of fixed deposits, which increased by RM10,779 million during the first eight months of 1996 to RM65,193 million at the end of August 1996 (an increase of RM4,960 million during the same period of 1995), reflecting the higher interest rates offered for such deposits. However, savings deposits registered a smaller decline of 4.0% from the end of 1995 to RM4,703 million at the end of August 1996, compared with a decline of 8.3% during the same period of 1995. NIDs issued by finance companies rose significantly by 42.9% during the period, compared with an increase of 29.9% during the corresponding period of 1995, bringing the total NIDs to RM12,444 million as at the end of August 1996. Total outstanding deposits of the finance companies amounted to RM84,383 million as at the end of August 1996, representing 23.4% of total resources of the banking system. The bulk of the deposits was in the form of fixed deposits (77.3% of the total outstanding deposits as at the end of August 1996), followed by NIDs (14.7%) and savings deposits (5.6%).

Lending activities of the finance companies expanded further, reflecting the increase in demand for financing by the private sector. Total new loans and advances of the finance companies increased by RM11,541 million during the first eight months of 1996 to RM74,293 million at the end of August 1996, compared with an increase of RM6,627 million during the corresponding period of 1995, as indicated in Table 9.4. Lending to private individuals increased by 13.8% (RM4,837 million) to RM39,848 million at the end of August 1996. Of this, 19.4% (RM7,726 million) was extended for the purchase of houses and 69.2% (RM27,561 million) for consumption purposes. Meanwhile, loans extended to the construction, real estate and manufacturing sectors increased by 28.6%, 26.5% and 13.1%, respectively during the first eight months of 1996 (–2.6%, 11.0% and 21.3%, respectively during the same period of 1995). Reflecting the faster growth in deposits (20.6%) compared to growth in loans (18.4%), the loan-deposit ratio of the finance companies decreased from 89.7% at the end of 1995 to 88.0% at the end of August 1996.

Reflecting the tight monetary stance adopted by BNM, the mode fixed deposits rates of finance companies for all maturities increased during the first eight months of 1996. The one-month and three-month rates increased from 6.65% and 6.80% per annum, respectively at the end of 1995 to 7.25% and 7.30% per annum, respectively at the

Table 9.4

Finance Companies: Direction of Lending

	Change During Period				As at end of August 1996
	1995 January-August		1996 January-August		
	RM million	%	RM million	%	RM million
Agriculture	91	11.9	151	15.8	1,104
Mining and quarrying	44	26.4	5	2.0	250
Manufacturing	628	21.3	526	13.1	4,531
Construction	–103	–2.6	1,251	28.6	5,622
Real estate	306	11.0	895	26.5	4,272
Private individuals of which:	3,652	13.1	4,837	13.8	39,848
Consumption credit	3,162	17.8	4,439	19.2	27,561
Purchase of stocks/shares	149	4.0	–6	–0.1	4,561
Housing*	341	5.3	404	5.5	7,726
General commerce	60	4.3	310	20.1	1,855
Miscellaneous	1,949	19.3	3,566	26.9	16,811
TOTAL	6,627	13.2	11,541	18.4	74,293

* Excluding loans sold to Cagamas Berhad.

Source: BNM.

end of August 1996. Similarly, the six-month and twelve-month rates rose to 7.35% and 7.40% per annum, respectively at the end of August 1996 from 6.85% and 7.00% per annum, respectively at the end of 1995. The mode savings deposits rate, however, remained stable from a range of 4.50% to 5.50% per annum at the end of 1995 to 5.50% per annum at the end of August 1996.

The **average cost of deposits** of finance companies increased from 6.31% per annum at the end of 1995 to 7.00% per annum at the end of August 1996, reflecting the increase in fixed deposits rates. Similarly, the average lending rate increased by 0.32 percentage point to 11.86% per annum at the end of August 1996 from 11.54% per annum at the end of 1995. With the more rapid increase in the average cost of deposits compared with the average lending rate, the gross interest margin narrowed by 0.37 percentage point to 4.86% per annum at the end of August 1996, from 5.23% per annum at the end of 1995. Reflecting the increasing trend in the average cost of deposits, the mode **BLR** of finance companies increased from 9.20% per annum at the end of 1995 to 10.60% per annum at the end of August 1996.

Lending Guidelines pertaining to **priority sectors** was issued on 27 March 1996 by way of an extension to the previous Guidelines governing finance companies. Under the new Guidelines, lending to the Bumiputera community was increased from 20% of the loan base to 30% of the loan base. In respect of lending for the purchase of houses, finance companies were required to make firm commitments to finance the purchase of at least 40,000 units of houses costing RM100,000 and below each (25,000 units, previously). Finance companies were also required to secure at least RM240 million (RM60 million, previously) guarantee cover from CGC on loans below RM500,000 each, of which at least one-half of the allocated quota was to be extended to Bumiputera borrowers. The compliance date for the targets outlined in the Guidelines is 31 March 1998, with the stipulation that one-half of the minimum requirement was to be complied with by 31 March 1997. As at the end of August 1996, lending to the Bumiputera community totalled RM24,795 million or 38.3% of the loan base (31 December 1995), while finance companies, as a group, had made firm commitments in financing the purchase of 8,916 units of houses costing RM100,000 and below each or achieved 22.3% of the target.

The two-tier regulatory system which was introduced for the commercial banks (December 1994) and merchant banks (January 1996) was extended to finance companies. To be classified under the Tier-1 group, finance companies must have a minimum shareholders' funds of RM300 million. In addition, finance companies were also required to increase their shareholders' funds to RM600 million by end of 1998 and achieve a minimum paid-up capital of RM600 million by the end of 2000. Subject to prudential limits and conditions imposed by BNM, Tier-I finance companies are allowed to undertake a wider range of activities as follows:

(i) provide factoring services;

(ii) provide remittance services within Malaysia, including bankers cheques, demand drafts, payment order and telegraphic transfer. However, a finance company is only allowed to use the cheques of the commercial bank belonging to the same Group, or the cheques of Tier-I commercial banks;

(iii) participate in special funds established by BNM (such as Fund for Food, Special Fund for Tourism, New Entrepreneurs Fund and Bumiputera Industrial Fund);

(iv) grant unsecured business loans up to a maximum of RM500,000 except for personal loans which will continue to be subject to the existing limit of RM10,000;

(v) participate in venture capital (VC) financing through a subsidiary company, or in the case of a finance company of a Group with a VC subsidiary company, the Group's VC subsidiary; and

(vi) issue NIDs up to five times of their capital funds.

The SRR of finance companies was raised twice by one percentage points from 11.5% to 12.5% of their eligible liabilities (with effect from 1 February 1996) and then from 12.5% to 13.5% of their eligible liabilities (with effect from 1 June 1996).

The number of finance companies operating in the country as at the end of August 1996 remained at 40, of which 12 were wholly-owned subsidiaries of domestic commercial banks and four were subsidiaries of locally-incorporated foreign commercial banks. During the period, finance companies established another 63 new branches, thus bringing the total to 1,051 branches at the end of August 1996.

Merchant Banks

The overall performance of merchant banks improved during the first eight months of 1996 underpinned by the strength of the nation's economic growth and concomitant increase in the demand for financial intermediation. Total resources mobilised by merchant banks from **fund-based activities** increased by 10.1% during the first eight months of 1996 to RM29,796 million, compared with an increase of 2.5% during the corresponding period of 1995. The new resources were mainly sourced from placements by corporations and NIDs issued by the merchant banks. During the review period, total **new deposits** mobilised by merchant banks increased by RM4,178 million to RM20,271 million (January-August 1995: RM1,646 million), as indicated in Table 9.5. This was mainly due to the firming of deposits rates. New deposits (including repos) placed by financial institutions increased by RM3,100 million during the first eight months of 1996 to RM8,573 million, compared with RM700 million during the same period of 1995. Financial institutions were the largest contributor, accounting for 42.3% of the total outstanding deposits placed with merchant banks at the end of August 1996. The bulk (88.5%) of the total outstanding fixed deposits remained concentrated in short-term maturity periods of up to six months. During the first eight months of 1996, **total deposits** (including repos) mobilised by merchant banks rose by 26.0% to RM20,271 million, compared with an increase of 11.3% during the corresponding period of 1995. As at the end of August 1996, the share of deposits mobilised by merchant banks to the total outstanding deposits of the banking system increased marginally to 6.2% from 5.7% at the end of 1995.

Lending operations of the merchant banks increased by 23.9% from the end of 1995 to RM16,531 million at the end of August 1996, compared with a growth of 2.8% during the same period of 1995. This was mainly due to the increased lending to the private sector (100.2%). However, lending to the public sector recorded a decline of 0.7%. Loans to the private sector accounted for 98.6% of the total outstanding loans extended by merchant banks as at end of August 1996. The bulk of the loans was in the form of term loans, amounting to RM9,033 million or 54.6% of the total outstanding loans of merchant banks at the end of August 1996. The bulk of new credit was channelled to the finance, insurance and business sectors (RM1,424 million or 44.7% of total new loans), followed by the broad property sector (RM1,037 million or 32.5%) and the manufacturing sector (RM274 million or 8.6%).

As the growth in deposits outpaced the growth in loans, the **loan-deposit ratio** of merchant banks decreased from 87.9% at the end of 1995 to

Table 9.5

Merchant Banks: Deposits And Lending

	Change During Period				As at end of August 1996
	1995 January-August		1996 January-August		
	RM million	%	RM million	%	RM million
Deposits					
Fixed deposits	963.5	9.8	1,999.6	19.9	12,033.3
Commercial banks	–134.4	–28.2	361.8	63.8	928.8
Finance companies	228.9	88.7	–44.8	–14.4	267.0
Corporations	37.3	0.5	689.8	9.7	7,815.2
Others[1]	831.7	42.7	992.8	48.9	3,022.3
NIF	7.3	123.7	332.8	2,233.6	347.7
Repos	492.8	24.1	–355.7	–13.4	2,308.3
NIDs	182.0	6.7	2,201.2	65.1	5,581.9
TOTAL	1,645.6	11.3	4,177.9	26.0	20,271.2
Loan					
Term loans	116.9	1.9	1,930.2	27.2	9,032.7
Federal and state governments	–11.8	–35.1	–6.7	–11.9	49.5
Statutory authorities and local governments	2.4	5.2	–8.6	–19.5	35.6
NFPEs[2]	–34.0	–21.8	17.1	14.6	134.1
Bumiputera individuals	–73.6	–3.4	780.1	34.1	3,068.7
Domestic	231.1	5.9	1,148.3	25.1	5,718.2
Foreign	2.8	37.9	–0.0	–0.0	26.6
Trade bills (including BAs)	88.8	15.2	–104.1	–14.2	629.2
Others	119.0	2.5	1,363.3	24.8	6,869.1
TOTAL	324.7	2.8	3,189.4	23.9	16,531.0

[1] Includes merchant banks and other financial institutions.

[2] Non-Financial Public Enterprises.

Source: BNM.

81.5% at the end of August 1996. The **average liquidity ratio** of merchant banks increased from 15.3% at the end of 1995 to 15.6% at the end of August 1996. The average cost of deposits of merchant banks increased by 0.85 percentage point to 7.19% at the end of August 1996 from 6.34% at the end of 1995, reflecting the increase in fixed deposits rates. Similarly, the average lending rate increased from 9.50% at the end of 1995 to 10.95% at the end of August 1996 and consequently, the gross interest margin widened by 0.60 percentage point to 3.76% from 3.16%.

The **fee-based income** of merchant banks, which accounted for 56.4% of the merchant banks' total income amounted to RM243 million during the first six months of 1996, compared with RM185 million during the same period of 1995. The merchant banks underwrote 80 issues of new stocks and shares as well as private debt securities (PDS), amounting to RM3,070 million, compared with a value of RM1,790 million during the same period of 1995. Of this, 14 were public issues and 28 were rights issues. During the first six months of 1996, 12 merchant banks acted as corporate advisers on acquisitions, take-overs, mergers and undertook feasibility studies for a total of 184 corporate clients. The portfolio funds managed by the merchant banks increased by 5.2% to RM3,787 million during the period (January-June 1995: 14.6%). Total fees derived from portfolio management activities undertaken by merchant banks, constituting 2.4% of the total income amounted to RM10.2 million during the first half of 1996, compared with RM10.8 during the same period of 1995. The bulk of portfolio funds managed by merchant banks belonged to institutions (65.1%), while the remaining funds belonged to corporations (18.1%), others (15.0%) and individuals (1.8%).

There were 12 merchant banks with eight branch offices operating in the country as at end of August 1996. **Total assets** of the merchant banks increased by 10.1% from the end of 1995 to RM29,796 million at the end of August 1996, compared with 2.5% during the same period of 1995.

The two-tier regulatory system introduced for commercial banks in December 1994 was extended to merchant banks, with effect from January 1996. Merchant banks which satisfy the criteria of ratings in terms of capital, assets, management, earnings and liquidity (CAMEL), having a minimum shareholders' funds of RM250 million and actively participate in fee-based activities would be classified as Tier-1 merchant banks. The Tier-1 merchant banks are allowed to undertake the following activities subject to prudential guidelines issued by BNM:

(i) foreign exchange activities for their own accounts and to offer foreign exchange services to eligible customers;

(ii) participate in the domestic and global derivatives markets;

(iii) invest in all non-trustee shares listed on the Kuala Lumpur Stock Exchange (KLSE) and other exchanges in the ASEAN countries subject to prescribed limit;

(iv) accept fixed deposits from individuals subject to a minimum amount of RM1 million;

(v) issue NIDs up to five times of their capital funds; and

(vi) expand their operations regionally through the establishment of a branch, a subsidiary company or a joint-venture.

As at end of August 1996, four merchant banks have been accorded Tier-1 status.

Discount Houses

During the first seven months of 1996, the operations of discount houses expanded markedly in line with the strong expansion of economic activities. **Total resources** of discount houses increased by 20.9% from the end of 1995 to RM15,504 million at the end of July 1996, compared with a growth of 19.2% during the same period of 1995. This was mainly due to the increase in **deposits** (including repos) mobilised by discount houses which increased by RM2,559 million during the first seven months of 1996 to RM14,770 million at the end of July 1996 (January-July 1995 : RM1,661 million). The new deposits were placed by commercial banks (RM1,669 million or 65.2% of total new deposits) and business enterprises (RM866 million or 33.8%), while statutory authorities and other financial institutions recorded a marginal increase of RM62 million and RM9 million, respectively during the period.

Total investment of discount houses rose significantly by 30.4% from the end of 1995 to RM14,838 million at the end of July 1996, compared with an increase of 16.5% during the corresponding period of 1995. In terms of components, investment in PDS increased markedly by 78.1% to RM7,816 million (January-July 1995 : RM556 million), while investment in BAs rose by 3.1% to RM5,261 million (January-July 1995 : RM917million). However, investment in Malaysian Government Securities (MGS) continued to decline by 6.9% due to a shift in investment to higher yielding papers such as PDS and BAs (a decline of 51.1% during the same period of 1995). On the other hand, investment in NIDs and Cagamas bonds increased significantly by 19.3% and 29.1%, respectively to RM340 million and RM590 million, respectively compared with a decline of 20.3% and 32.1% during the corresponding period of 1995.

The volume of secondary transactions registered by discount houses in various type of papers increased significantly to RM78,930 million, compared with RM54,307 million during the corresponding period of 1995. Total purchases and sales of PDS and BAs increased markedly to RM30,794 million and RM26,146 million, respectively, while that of MGS rose to RM7,082 million. Similarly, total transactions in BNBs (including certificates) increased marginally to RM8,320 million, compared with RM8,008 million during the same period of 1995. However, the value of total transactions in both Cagamas bonds and Treasury bills declined by RM4,072 million and RM2,116 million, respectively to RM1,931 million and RM4,196 million (RM6,003 million and RM6,312 million, respectively during the corresponding period of 1995).

To promote a more dynamic and performance-based dealer system, BNM reviewed the existing Principal Dealer system and in January 1996 accorded principal dealer status to only three discount houses compared to all seven discount houses previously. In 1996, BNM also granted approval for discount houses to participate in the futures market.

Development Finance Institutions

The five principal development finance institutions (DFIs) set up by the Government to specialise in the provision of medium - and long-term loans to finance capital investment in new industries as well as entrepreneurs in the industrial sector are the Malaysian Industrial Development Finance Berhad (MIDF), Bank Industri Malaysia Berhad (Bank Industri), Bank Pembangunan Malaysia Berhad (Bank Pembangunan), Sabah Development Bank (SDB) and Bank Pertanian Malaysia (Bank Pertanian). The Export-Import Bank of Malaysia Berhad, yet another industrial finance institution, was established in August 1995 with the objectives of financing and promoting international trade and facilitating the export of goods and services by means of export credit, financing of capital investment and provision of business information and services. Total resources of the DFIs increased by 5.7% during the first six months of 1996 to RM10,708 million compared with 13.5% during the corresponding period of 1995.

The DFIs as a group registered a mixed performance in terms of total resources. Reflecting the significant increase in total deposits (136.5%), total resources of the SDB increased by 23.9% during the first six months of 1996 to RM1,255 million, as indicated in Table 9.6 (January-June 1995: 22.9%). Total resources of the MIDF and Bank Industri rose by 20.0% and 10.2%, respectively to RM2,006 million and RM1,627 million, respectively at the end of June 1996, compared with a growth of 2.2% and 4.5%, respectively during the corresponding period of 1995. Similarly, total resources of Bank Pertanian increased marginally by 0.9% from the end of 1995 to RM4,013 million at the end of June 1996 (an increase of 33.3% during the corresponding period of 1995). However, total resources of Bank Pembangunan declined further by 9.4% to RM1,807 million, compared with 7.4% during the same period of 1995.

Total new loans extended by the DFIs declined by 13.7% to RM1,922 million during the first six months of 1996 as against RM2,227 million during the corresponding period of 1995, as indicated in Table 9.7. In terms of lending by sector, the agriculture sector registered a significant increase of 27.3% to RM527 million from RM414 million during the same period of 1995. However, the mining and quarrying sector recorded a decline of 33.3% to RM12 million as against RM18 million during the corresponding period of 1995, while other sectors (including trade credit and miscellaneous) declined by 28.6% to RM439 million

Table 9.6

Development Finance Institutions
(as at end of period)

Institution	*1995*	*June 1996*
Total Resources[1] (RM million)		
Bank Pertanian Malaysia	3,976	4,013
Bank Pembangunan Malaysia Bhd.	1,994	1,807
Malaysian Industrial Development Finance Bhd.	1,672	2,006
Bank Industri Malaysia Bhd.	1,476	1,627
Sabah Development Bank Bhd.	1,013	1,255
Average Interest Rates (%)		
Bank Pertanian Malaysia		
Concessional rate	4.00	4.00
Commercial rate	0-4 above BLR[2]	0-4 above BLR[2]
Bank Pembangunan Malaysia Bhd.	6.55	6.89
Malaysian Industrial Development Finance Bhd.	8.15	8.30
Bank Industri Malaysia Bhd.		
Ship repairing	6.00	6.00
Ship building	7.75-9.00	7.75-9.00
Dockyard infrastructure	9.00	9.00
Export Credit Refinancing Scheme	5.00-9.00	5.00-9.00
Sabah Development Bank Bhd.	above 9.00	above 9.00

[1] Include shareholders' funds, short and long-term borrowings and deposits mobilised.

[2] Base Lending Rate

Sources: Bank Pertanian Malaysia, Bank Pembangunan Malaysia Berhad, Malaysian Industrial Development Finance Berhad, Bank Industri Malaysia Berhad and Sabah Development Bank Berhad.

(January-June 1995: RM615 million). Similarly, the real estate and construction sectors registered a decline of 23.8% to RM240 million (first half of 1995: RM315 million), while the manufacturing sector and the shipping industries declined by 23.6% and 6.1%, respectively to RM472 million and RM232 million, respectively (January-June 1995: RM618 million and RM247 million, respectively). The bulk of the new loans was

Table 9.7

Direction of Lending by DFIs

	1995	1996[p]	Change During Period
	(January-June) RM million		%
Manufacturing	618	472	–23.6
Shipping	247	232	–6.1
Agriculture	414	527	27.3
Real estate and construction	315	240	–23.8
Mining and Quarrying	18	12	–33.3
Others	615	439	–28.6
Total	2,227	1,922	–13.7

[p] Preliminary data

Source: Bank Pertanian Malaysia, Bank Pembangunan Malaysia Berhad, Malaysian Industrial Development Finance Berhad, Bank Industri Malaysia Berhad and Sabah Development Bank Berhad.

extended to the agriculture sector (27.4%) with Bank Pertanian and the SDB accounting for 94.3% and 5.7%, respectively while 24.6% was extended to the manufacturing sector and 22.8% to the other sectors.

As in previous years, the lending activities of individual DFIs varied. New loans approved by Bank Pertanian increased by 25.5% to RM496.9 million during the first six months of 1996 (January-June 1995: RM395.8 million), while credit approved by the SDB rose by 19.6% to RM410.5 million (January-June 1995: RM 343.2 million). However, loans approved by the MIDF declined significantly by 40.5% to RM334.1 million from RM561.4 million during the same period of 1995. Similarly, total lending by Bank Industri declined by 37.3% to RM261.6 million (January-June 1995: RM417.2 million), while new loans approved by Bank Pembangunan declined by 17.9% to RM418.0 million (January-June 1995: RM509.1 million). Consequently, total outstanding loans of the DFIs stood at RM6,123.3 million at the end of June 1996, compared with RM5,367.8 million at the end of 1995. The average interest rates charged by the individuals DFIs varied within a range of 4.00% to 10.00% per annum, as indicated in Table 9.6.

The DFIs continued to play the role of implementing agencies for the various specialised assistance schemes such as the **Industrial Adjustment Fund (IAF)**, the **Enterprises Rehabilitation Fund (ERF)** and the **ASEAN-Japan Development Fund (AJDF)**. The IAF which was launched on 5 February 1991 with a total allocation of RM500 million is aimed at rationalising and restructuring companies existing before 31 December 1990 in three selected industries, namely machinery and engineering, wood-based and textile industries through mergers, takeovers, relocations and diversification. As no new applications were approved during the first seven months of 1996, the total number of approved applications at the end of July 1996 remained unchanged at the end-1995 level (18 applications with an aggregate value of RM66.0 million). Meanwhile, a total of RM53.8 million had been disbursed as at 31 July 1996.

The ERF which was set up in 1988 is aimed at providing financial assistance to ailing but viable Bumiputera enterprises facing financial difficulties due to the recession in 1985/86. Although total applications approved declined by three applications, the total amount approved increased by RM60,519 during the first seven months of 1996 (one application amounting to RM2.4 million was approved during the corresponding period of 1995). Thus, as at end of July 1996, 236 applications with a total value of RM642.9 million was approved, while drawdowns totalled RM589.7 million. The bulk of the loans was extended to finance the housing sector (RM417.7 million), followed by the construction sector (RM92.3 million), the property sector (RM77.6 million) and the manufacturing sector (RM39.4 million).

The AJDF established with the aim of assisting the development of small and medium-scale industries remains under the administration of Bank Pertanian, Bank Industri, Bank Pembangunan and MIDF. This revolving fund was launched in January 1989 with the initial funding allocated by the Overseas Economic Cooperation Fund (OECF) and the Export-Import Bank of Japan (EXIM). The implementing DFIs approved a total of RM158.5 million during the first six months of 1996, despite a decline in total applications approved by 254 (January-June 1995: 78 applications with a total value of RM143 million was approved). As at 30 June 1996, total loans approved amounted to RM1,706.3 million for 4,097 projects. Of this, RM1,329.4 million (77.9%) was derived from OECF's allocation, while the remaining balance (RM376.9 million) came out of EXIM's allocation.

Other funds implemented jointly by commercial banks, merchant banks and the DFIs also continued to provide for specialised assistance funds set up by the Government and administered by BNM. The RM120 million **Special Fund for Tourism (SFT)** set up in March 1990 with the aim of financing the development of tourist-related projects was raised to RM200 million and converted to a revolving fund due to overwhelming response, effective from 16 November 1993. This enabled the Fund to be fully utilised during the period under review. During the first seven months of 1996, six applications with a total value of RM8.0 million was approved, compared with 17 applications amounting to RM85.5 million approved during the same period of 1995. This brings the total number of applications approved to 188, valued at RM213.5 million as at end of July 1996, with RM157.6 million having been disbursed. The bulk (88.7%) of the approvals was extended for the construction and renovation of budget hotels and chalets.

The RM250 million **New Entrepreneurs Fund (NEF)** launched in December 1989, to encourage more small - and medium-scale Bumiputera entrepreneurs to participate actively in various fields of business was raised to RM750 million and converted to a revolving fund. The implementing agencies of the Fund include Bank Pembangunan, Bank Industri, MIDF and 11 other commercial banks. During the first seven months of 1996, the Fund was fully utilised with a total number of 124 new applications approved, valued at RM86.9 million (January-July 1995: 147 applications approved, amounting to RM89.1 million). As at end of July 1996, a total number of 1,963 applications valued at RM919.0 million was approved, of which RM806.9 million had been disbursed.

Under the **Fund for Food** scheme, a total number of 360 applications, amounting to RM31.4 million was approved during the first seven months of 1996, compared with 229 applications valued at RM56.3 million approved during the same period of 1995. This brings the number of applications approved at end of July 1996 to 1,020 with a total value of RM290.4 million, of which RM240.5 million had been disbursed. The bulk of approvals was for animal husbandry (RM162.0 million), followed by cultivation of fruits and vegetables (RM52.6 million) and food processing (RM32.1 million). Recently, the Government announced the approval of an additional allocation of RM300 million to the existing RM300 million under the Fund.

Other Financial Institutions

National Savings Bank

Total resources of the **National Savings Bank (NSB)** expand further in line with the further expansion of its activities. During the first six months of 1996, total resources of the NSB increased by 8.4% or RM512 million to RM 6,584 million compared with a growth of 4.7% during the corresponding period of 1995. This was mainly due to the increase in deposits, especially both the long - and short-term deposits, which grew significantly by 70.6% during the period to RM974 million (January-June 1995: 7.2%).

New deposits (including premium savings certificates) mobilised by the NSB increased by RM2,268 million to RM11,134 million, compared with RM8,866 million during the same period of 1995. On the other hand, total withdrawals also registered an increase of RM2,014 million to RM10,811 million (January-June 1995: RM8,797 million). Thus, net deposits increased to RM323 million (RM69 million during the same period of 1995), reflecting the firming of deposits rates during this period which attracted more deposits.

The **GIRO** savings scheme remained the core product of the NSB, mobilising a total value of RM9,870 million or 88.6% of the total new deposits mobilised by the NSB during the first half of 1996 (January-June 1995: RM7,791 million). This was mainly due to the introduction of several facilities, such as standing instructions, bill payments, money transfers, salary credits and Automated Teller Machines (ATMs) facilities. Similarly, total withdrawals also grew significantly by RM9,704 million compared with RM7,718 million during the same period of 1995. Consequently, total net deposits mobilised by the NSB under the scheme was relatively higher at RM166 million, compared with RM73 million during the corresponding period of 1995. The Guaranteed Giro Order (GGOs) facility which works similarly as a Cashier's Order introduced in 1993 for the purchase of new public share offerings was also extended to the second issuing house, Malaysia Issuing House. During the first half of 1996, a total of 144,574 GGOs were issued with a total value of RM453 million (January-June 1995: 89,627 GGOs valued at RM303 million).

Reflecting comparable interest rates offered by the NSB to depositors, new deposits mobilised under the fixed deposits scheme increased by RM70 million to RM312 million during the first half of 1996 from RM242 million during the corresponding period of 1995. At the same time, withdrawals amounted to RM217 million compared with RM263 million during the same period of 1995. As such, the fixed deposits scheme registered a net inflow of RM94 million, compared with a net outflow of RM21 million during the corresponding period of 1995. Similarly, total **savings deposits** recorded an increase of RM20 million to RM753 million (6.8% of the total new deposits) during the first half of 1996 from RM733 million during the same period of 1995, while withdrawals increased by 6.5% to RM783 million (January-June 1995: RM735 million). Thus, the savings deposits scheme registered a larger net outflow of RM30 million compared with a net outflow of RM2 million during the corresponding period of 1995. Meanwhile, the Save-As-You-Earn scheme continued to record net withdrawals of RM0.8 million (January-June 1995: RM0.7 million) as deposits lagged behind withdrawals at RM8.2 million and RM9 million, respectively. However, the premium savings certificates scheme registered a larger net inflow of RM93 million (January-June 1995: RM20 million) as purchases of premium certificates rose by RM191 million as compared with the increase in withdrawals of RM98 million during the first half of 1996.

In line with the growth in total resources of NSB, **investments** rose by 2.1% during the first half of 1996 to RM3,864 million compared with an increase 1.7% during the same period of 1995. This was mainly due to further investments in Federal Government securities (comprising MGS, Cagamas bonds and Treasury bills) which increased by 2.1% from the end of 1995 to RM2,572 million at the end of June 1996 (January-June 1995: 5.2%). MGS accounted for 80.3% of the total outstanding investments. The short and long-term deposits placed with the banking system increased significantly by 70.6% during the first half of 1996 to RM974 million, while NSB's investments in stocks and shares increased by 2.1% to RM1,291 million (a decline of 8.3% during the same period of 1995).

The **lending activities** of the NSB registered a smaller increase of RM104 million (9.5%) during the first six months of 1996 to RM1,200 million as at end of June 1996, compared with of RM122 million during the corresponding period of 1995. However, loans granted to individuals declined by RM66 million as some of the loans were either

Table 9.8

National Savings Bank
(as at end of period)

	1995	*1996p*
Deposits[1] (RM million)		
Savings	1,734	1,704
Fixed	914	1,008
Save-As-You-Earn	22	22
GIRO	2,134	2,300
Premium Savings Certificates	356	449
Investments at book value (RM million)		
MGS	2,109	2,066
Stocks and shares[2]	1,265	1,291
Others[3]	571	974
Loans (RM million)	1,096	1,200
Individuals	742	676
Corporate	150	160
Visa Cards	11	17
Hire-Purchase	193	347
Number of NSB branches[4]	479	479
Number of post offices with NSB facilities	606	611
Number of depositors ('000)	9,305	9,706
Savings	4,090	4,117
Fixed	79	90
Save-As-You-Earn	22	22
GIRO	5,114	5,477

[1] Includes interest credited.
[2] Includes trustee and non-trustee shares, private debt securities and warrants.
[3] Includes long and short-term deposits.
[4] Includes mini and sub-branches.
[p] Preliminary data.

Source: National Savings Bank.

prepaid or matured during the period. In contrast, credit granted to Visa Cards and for hire-purchase increased significantly by 54.5% and 79.8%, respectively while loans extended to the corporate sector rose by 6.7%.

As part of its expansion programme, the NSB established another seven more mini-branches and installed four ATMs. As at the end of June 1996, the bank had a total of 479 branches with 588 ATMs. In line with its objective of providing better and more varied products, the NSB is expected to venture into the stockbroking business by the end of 1996 following the granting of a new licence by BNM recently.

Provident and Pension Funds

The four principal provident and pension funds, namely the Employees Provident Fund (EPF), the Social Security Organisation (SOCSO), the Armed Forces Fund (AFF) and the Pensions Trust Fund (PTF) continue to expand their activities and provide the largest source of long-term financing for development projects initiated by the public sector. During the first half of 1996, total resources of these four funds increased by 8.2% from RM112.5 billion to RM121.7 billion (January-June 1995: 8.3%), as indicated in Table 9.9.

The EPF remains the largest provident and pension fund in the country. Total resources of the EPF increased by 7.7% during the first half of 1996 to RM106.3 billion (January-June 1995: 7.7%), reflecting mainly the increase in the number of contributors as well as higher returns from its various investments. The total membership of the EPF rose by 166,524 persons to 7,922,785 contributors at the end of June 1996 from 7,756,261 contributors at the end of 1995. Reflecting the increase in membership, gross contributions to EPF increased by RM6.3 billion during the first half of 1996, compared with RM5.2 billion registered during the same period of 1995. At the same time, total withdrawals amounted to RM1.8 billion (January-June 1995: RM1.6 billion). Consequently, net contributions to the EPF increased by 25.0% to RM4.5 billion, compared with an increase of RM3.6 billion during the same period of 1995. The total outstanding balance of contributor's accounts (including interest credited) increased by 4.6% from RM97.5 billion at the end of 1995 to RM102.1 billion at the end of June 1996 (January-June 1995: 4.2%).

Table 9.9

Provident And Pension Funds
(as at end of period)

	Total Resources (RM million)		*Malaysian Government Securities (RM million)*		*Number of Members ('000)*	
	1995	*June 1996*[p]	*1995*	*June 1996*[p]	*1995*	*June 1996*[p]
EPF	98,715	106,314	39,150	38,977	7,756	7,923
SOCSO	4,478	4,741	2,310	2,330	7,422	7,589
AFF	3,520	3,587	10	10	99	99
PTF	5,805	7,059	0	0	—	—
TOTAL	112,518	121,701	41,470	41,317	15,277	15,611

[p] Preliminary data.

Source: Employees Provident Fund, Social Security Organisation, Armed Forces Fund and Pensions Trust Fund.

In consonance with the increase in total resources (RM7.6 billion), total investments of the EPF expanded by 7.4% from the end of 1995 to RM103.8 billion as at end of June 1996 (January-June 1995: 7.7%), accounting for 97.6% of the total outstanding resources. The EPF's holdings of MGS declined further by 0.4% to RM39.0 billion at the end of June 1996, compared with a decline of 0.7% during the corresponding period of 1995. Thus, investments in MGS constitute a share of only 37.6% of the total outstanding investments of the EPF compared with a share of 41.0% at end of 1995, below the mandatory requirement of the cumulative investments in MGS of 50% (70% in 1994). This was mainly due to shortages in Government papers resulting from the decline in Government borrowings in view of its strong overall financial position. Investments by the EPF in loans and debentures (including promissory notes), however, increased by 10.0% from RM7.5 billion as at the end of 1995 to RM8.2 billion at the end of June 1996 (January-June 1995: 13.5%). Similarly, investments in corporate securities increased by 21.3% to RM25.7 billion in the same period (first half of 1995: 18.9%), in line with the EPF's objective of reducing its dependence on interest income by diversifying into higher revenue-earning investments. In line with this, investments in NIDs, fixed deposits and short-term deposits slowed down substantially by 15.9% to RM25.9 billion at the end of June 1996 compared with an increase of 41.3% during the same period of 1995.

On 5 February 1996, the EPF was allowed to participate in the construction of low - and medium-cost houses through its subsidiary, Malaysian Building Society Berhad to alleviate general shortages in the supply of low-cost houses and to curb price increases for such houses. The Minister of Finance also announced that EPF contributors will be permitted to invest up to 20% of their funds in unit trusts beginning from 1997. This investment scheme is available to contributors below 55 years with more than RM50,000 under Account One, which constitutes a share of 60% of their total contributions. In addition, the programme would not involve the transfer of cash as the EPF will disburse contributors' funds directly to the managers of the selected unit trusts.

The **PTF** was established on 1 June 1991 under the Pensions Trust Fund Act 1991, with the objective of setting up a self-financing fund to take over the Government's obligations to meet the cost of payment of pensions, gratuity and other pension benefits to retired public servants. The primary source of funds will be annual contributions by the Government, initially set at 5% of the annual civil service emolument bill. Funds are also derived from the monthly contributions made by employers under the Statutory and Local Authorities Pensions Act 1980, refund of the employers' contribution to the EPF and other approved funds established for retired public officials, income from investments and other sources approved by the Ministry of Finance. During the first six months of 1996, total resources of the PTF increased by 21.6% to RM7,059 million (January-June 1995: 25.2%). The bulk (70.0%) of the total outstanding resources was channelled to investments while the balance (30.0%) comprising cash and balances was placed in the banking system (including BNM).

SOCSO was established in 1971 under the Employees Social Security Act 1969 to provide social security benefits to workers through the Employment Injury Insurance Scheme and Invalidity Pension Scheme. Total resources of SOCSO increased by 5.9% during the first six months of 1995 to RM4,741 million (January-June 1995: 5.8%), in line with the expansion in its investments as well as net contributions. The bulk or 49.2% of the total outstanding resources was invested in MGS, while 35.4% was placed with the banking system and 9.6% was invested in corporate securities. As at 30 June 1996, the number of registered employees stood at 7,589,288 persons, an increase of 167,097 persons from the end of 1995 (December 1995: 7,422,191 persons).

The **AFF** was established in 1973 to provide superannuation benefits to to servicemen in the armed forces. Total resources of the AFF increased marginally by RM66.6 million during the first half of 1996 to RM3,587 million (January-June 1995: RM106.8 million).This was mainly due to the marginal growth in returns from its investments and a decline in contributors' outstanding balances (including interest credited). As the membership of the AFF declined marginally by 0.1% during the period, the contributors' balances declined by 2.4% from RM2,907 million to RM2,836 million.

As retirees outnumbered recruits, the membership of the AFF declined from 99,300 persons to 99,250 persons. The AFF invested 81.9% of its total outstanding resources in corporate securities (RM2,938 million), while 14.6% was placed in the banking system (RM523 million). However, investments in MGS remained unchanged at RM10 million as at end of June 1996.

Insurance Companies

In consonance with the nations' economic performance, the **insurance industry** continued to record impressive growth in 1995. Total premium income of both the life and general insurance increased at the same rate of 22.0% as in 1994 to RM7.9 billion as at the end of 1995. Premium income of the industry as a percentage of nominal Gross National Product (GNP) increased further to 3.9% in 1995, compared with 3.7% in 1994. Total benefits and net claims paid out by the industry increased by 14.0% in 1995 to RM2.2 billion at the end of 1995 (1994: 10.1%), constituting 28.3% of the premium income (1994: 30.3%). The industry's insurance fund assets rose by 19.7% in 1995 to RM25.0 billion as at the end of 1995 (1994: RM20.9 billion) to account for 3.4% of the total assets of the financial system (1994: 3.3%).

Business of the **life insurance** sector expanded, albeit at a more moderate pace, in 1995. The number of new policies issued increased by 9.0% to 1,029,459 units in 1995 (1994: 17.1%), thus bringing the total number of policies in force to 5,363,584 units. Consequently, new premiums increased by 23.4% to RM1,491.9 million (1994: 28.0%), while new sums insured grew by 19.6% to RM75,300.8 million (1994: 38.1%), as indicated in Table 9.10. Total assets of the life insurers increased further by 17.0% to RM17,383.8 million (1994:22.6%), constituting a share of 69.5% of the total assets of the insurance funds in the industry and 2.4% of the total assets of the financial system (1994: 2.4%). In terms of investment, the life insurance funds were invested in Government securities and Government-guaranteed loans (26.9%), corporate securities (23.8%), loans (20.4%) and cash and deposits (20.1%), as indicated in Table 9.11.

Reflecting the momentum of economic activities, the performance of the **general insurance** improved in 1995. Total written premiums rose by 17.8% to RM4,641.7 million in 1995 from RM3,940.7 million recorded in 1994. A total of RM1,222.0 million was ceded overseas, thus

Table 9.10

Life and General Insurance Business

	1994	*1995p*
Life Insurance (RM million)		
New Business:		
Number of policies ('000 units)	944.7	1,029.5
Sums insured	62,937.0	75,300.8
Total premiums	1,208.7	1,491.9
Business in Force:		
Number of policies ('000 units)	4,331.6	4,950.4
Sums insured	197,268.4	242,728.8
Annual premiums	3,697.1	4,574.1
Premium Income	3,653.7	4,512.0
Benefit Payments:		
Total	915.8	1,068.5
Maturity	330.4	379.6
Death and disability	347.1	419.4
Surrender	176.0	191.5
Cash bonuses	62.1	77.7
Annuity	0.2	0.3
General Insurance (RM million)		
Premium Income:		
Written	3,940.7	4,641.7
Net	2,847.3	3,419.7
Reinsurance Placed Outside Malaysia	1,093.4	1,222.0
Retention Ratio (%)	72.3	73.7
Number of Insurance Companies		
Direct:		
Life	5	5
General	40	40
Composite	13	13
Reinsurers	3	4

p Preliminary data.

Source: Director General of Insurance.

Table 9.11

Life and General Insurance Funds
(as at end of period)

	Life Insurance (RM million)		General Insurance (RM million)	
	1994	1995p	1994	1995p
Fixed assets	92.7	109.1	236.4	269.4
Loans	2,807.2	3,537.0	103.9	155.9
Government securities[1]	3,986.7	4,345.3	1,664.4	2,074.7
Government guaranteed loans	409.0	338.6	72.0	59.5
Corporate securities	3,114.0	4,139.3	885.8	1,129.6
Investment properties	683.5	800.7	39.8	38.2
Cash and deposits	3,271.3	3,496.3	2,256.8	3,027.0
Other assets	497.8	617.5	783.8	880.5
TOTAL	14,862.2	17,383.8	6,042.9	7,634.8

p Preliminary data.

[1] Includes Treasury bills and Government securities issued abroad.

Source: Director General of Insurance.

Table 9.12

Family and General Takaful Business

	Financial Year 1995	Financial Year 1996p
Assets (RM million)		
Malaysian Investment Certificates	69.5	80.8
Investment in Bank Islam Malaysia Bhd.	62.9	49.2
Others[1]	83.4	234.3
Family Takaful		
New Business:		
Total contribution (RM million)	26.1	66.7
Sums participated: (RM million)	1,433.6	1,920.2
Number of certificates	30,952	41,170
Business in Force:		
Total contribution (RM million)	37.0	93.9
Sums participated (RM million)	2,788.1	4,280.9
Number of certificates	55,035	76,452
General Takaful Business		
Gross contributions	58.4	67.9
Net claims paid	27.4	15.4

p Preliminary data.

[1] Includes shares, cash and balances and other assets.

Source: Syarikat Takaful Malaysia Berhad and MNI Takaful Sdn. Berhad.

resulting in a net retention ratio of 73.7% (1994:72.3%). The total assets of the general insurance funds rose by 26.3% to RM7,634.8 million at the end of 1995 from RM6,042.9 million at the end of 1994. Cash and deposits remained the largest item on the investment portfolio of the industry (RM3,027.0 million), followed by investments in Government securities and corporate securities which amounted to RM2,074.7 million and RM1,129.6 million, respectively.

The insurance industry is expected to maintain its pace of growth in 1996. Preliminary data for the first half of 1996 indicate that the combined premium income of the industry rose by 19.0% to RM4,176.7 million, compared with 20.4% during the corresponding period of 1995. Similarly, total assets of the life and general insurance sectors increased by 10.9% to RM27,344.8 million in the period (December 1995: RM25,018.6 million).

However, the life insurance industry is expected to record lower new business growth in 1996, partly attributable to the adjustments in the industry following the implementation of BNM's Guidelines on Operating Cost of Life Insurance Business. Annual premium in force of the life insurance sector increased by 20.1% to RM4,771.9 million as at the end of June 1996 (January-June 1995: 23.8%). The total written premiums of the general insurance sector increased by 18.2% during the period to RM2,554.3 million, compared with 14.0% during the corresponding period of 1995. The total assets of the general insurance industry increased by 12.2% to RM8,569.1 million in the period (end-1995: RM7,634.8 million).

Takaful or Islamic insurance is provided by two takaful operators, namely Syarikat Takaful Malaysia Berhad (STMB) and MNI Takaful Sendirian Berhad (MNIT). With two takaful operators in the market, the business has expanded significantly in 1996 with the main performance indicators registering double digit growth rates, as indicated in Table 9.12. Total assets of the takaful operators rose by 68.8% to RM364.3 million as at the end of the financial year (FY) on 30 June 1996, compared with a growth of 43.5% in the previous FY. Assets of the general takaful funds accounted for 30.4% of the total assets, while that of family takaful funds accounted for another 44.8%. The balance of 24.8% comprised assets of shareholders funds. Investment in Malaysian Investment Certificates accounted for 22.2% of total assets, while 13.5% was placed in investment accounts with BIMB. During the FY under review, a total of 41,170 (1995: 30,952) new certificates were issued under the family takaful business amounting to RM1,920.2 million (1995: RM1,433.6 million). Contributions totalled RM66.7 million, compared with RM26.1 million in 1995. Total gross contributions under the general takaful business continued to increase, albeit at a moderate rate, by 16.3% to RM67.9 million in 1996, compared with an increase of 51.7% in 1995. However, total net claims paid out declined by 43.8% to RM15.4 million in 1996 from RM27.4 million in 1995.

Reflecting the development of the insurance industry in the country, the number of insurance companies and insurance-related agents operating in Malaysia has increased. As at end June 1996, there were 65 insurers comprising of five life insurers, 13 composite insurers, 40 general insurers and seven general reinsurers. Of this, 51 were incorporated domestically, while the remaining 14 were foreign-incorporated companies. There were 38 licensed brokers and 43 licensed loss adjusters operating in the country at end of June 1996.

Capital Market

The capital market continues to be a major conduit in the mobilisation of savings for the purpose of financing capital formation for economic growth and development in 1996. Underpinned by the additional financing requirements of the corporate sector, coupled with the introduction of new and innovative products as well as the commitment by Government to promote Kuala Lumpur as a regional financial centre, activities in the Malaysian capital market expanded further during the first eight months of 1996. Total funds raised by both the public and private sectors through the capital market increased significantly by 64.2% to RM20,434 million compared with RM12,445 million mobilised during the corresponding period of 1995, as indicated in Table 9.13. The private sector accounted for 104.1% of the net funds raised in the capital market in the period. Gross funds raised by the private sector recorded a strong growth of 45.7% to reach RM23,408 million (RM16,070 million in the corresponding period of 1995). After adjusting for redemptions, net funds raised in the period rose to RM21,263 million (62.7% higher than the net funds of RM13,071 million raised in the corresponding period of 1995). The public sector, on the other hand, registered a higher net repayment of RM829 million in the review period compared with a net repayment of RM626 million in the corresponding period of 1995.

During the first eight months of 1996, the Government floated one issue of MGS valued at RM2,000 million (there were no issues of MGS during the same period of 1995). The issuance of MGS in the period reflects the need to maintain sufficient papers in the market to provide a benchmark yield for the bond market rather than the need to borrow as the Federal Government's overall financial position remains strong. A total of RM1,909 million of MGS and RM20 million worth of Malaysia Savings Bond were redeemed by holders during the period under review. Although no new Government Investment Issues were raised in the period, a total of RM900 million was redeemed.

The 62.7% increase in the net funds raised by the **private sector** during the first eight months of 1996 were largely through the issuance of private debt securities (PDS). Total gross funds raised from the PDS market increased significantly by 54.5% to RM12,210 million, compared with RM7,905 million raised during the same period of 1995. This was issued mainly by companies undertaking large infrastructure and privatised entities. These funds were raised through 78 issues of conventional bonds (RM5,797 million), 19 issues of convertible bonds (RM698 million) and two issues of Islamic papers (RM2,350 million). After adjusting for redemptions of RM2,145 million, net

Table 9.13

Funds Raised in the Capital Market

	1995 January-August RM million	1996p January-August RM million
By Public Sector		
Government Securities[1], gross	0	2,000
Less: Redemptions	850	1,909
Equals: Net issues	–850	91
Less: Government holdings	0	0
Equals: Net Federal receipts	–850	91
Malaysia Savings Bond, net	–26	–20
Investment certificates, net	250	–900
Net funds raised	–626	–829
By Private Sector		
Equity market		
Shares[2]	8,165	11,198
Public issues	3,598	1,692
Rights issues	3,316	4,435
Special issues[3]	483	1,878
Private placements[4]	645	3,193
Warrants	123	0
Debt Securities[5] (gross)		
Conventional bonds	4,825	5,797
Convertible bonds	708	698
Islamic notes	800	2,350
Cagamas bonds	1,572	3,365
Less: redemptions	2,999	2,145
Net issues of debt securities	4,906	10,065
Net funds raised	13,071	21,263
TOTAL	12,445	20,434

p Preliminary data.
1 Refers to Federal Government securities, excluding Treasury bills.
2 Refers to corporate shares issues by companies listed on the Kuala Lumpur Stock Exchange.
3 Includes special issues to Bumiputera and selected investors.
4 Includes restricted offer for sales.
5 Refers to securities with maturity of more than one year.

Source: BNM.

funds mobilised through debt securities was RM10,065 million during the period. This represented a significant increase of 105.2% in the net funds raised in the PDS market when compared to the same period of 1995 (RM4,906 million) and accounted for 47.3% of the total net funds raised by the private sector in the capital market (January-August 1995: 37.5%). This reflects the growing importance of the PDS market in financing private sector activities.

Similarly, total gross funds raised by the private sector through the equity market increased significantly by 37.1% to RM11,198 million during the first eight months of 1996 (January-August 1995: RM8,165 million). Of this, a total of RM1,692 million was raised from 71 public issues, RM4,435 million from 31 rights issues, RM1,878 million from 14 special issues and RM3,193 million from private placements. There were no new issues of call warrants during the period (January-August 1995: RM123 million).

The national mortgage corporation, **Cagamas Berhad**, was fairly active in the capital market, raising a total of RM6,470 million from 20 issues of Cagamas notes during the first eight months of 1996 (January-August 1995: RM3,332 million from 9 issues of Cagamas notes). The notes with maturities ranging from three to nine months were issued mainly to meet short-term funding needs. Meanwhile, Cagamas Berhad purchased a total of RM4,282 million of housing loans during the period, compared with RM2,970 million during the corresponding period of 1995. Of this, 99.3% or RM4,252 million was purchased from the financial institutions, while 0.7% or RM30 million from Bank Islam Malaysia Berhad (BIMB).

During the first eight months of 1996, the **Rating Agency Malaysia Berhad (RAM)** completed 58 corporate debt rating exercises of both long - and short-term PDS worth RM9.5 billion (January-August 1995: 57 issues valued at RM8.8 billion). This brought the total number of issues rated by RAM to 326 corporate ratings amounting to RM47.8 billion since its inception in 1990, reflecting the increasing attractiveness of PDS as an avenue for financing investment and the continued growth of private sector financing activities. There were 33 bank-guaranteed issues amounting to RM4.0 billion during the first eight months of 1996, compared with 36 issues amounting to RM4.6 billion during the corresponding period of 1995.

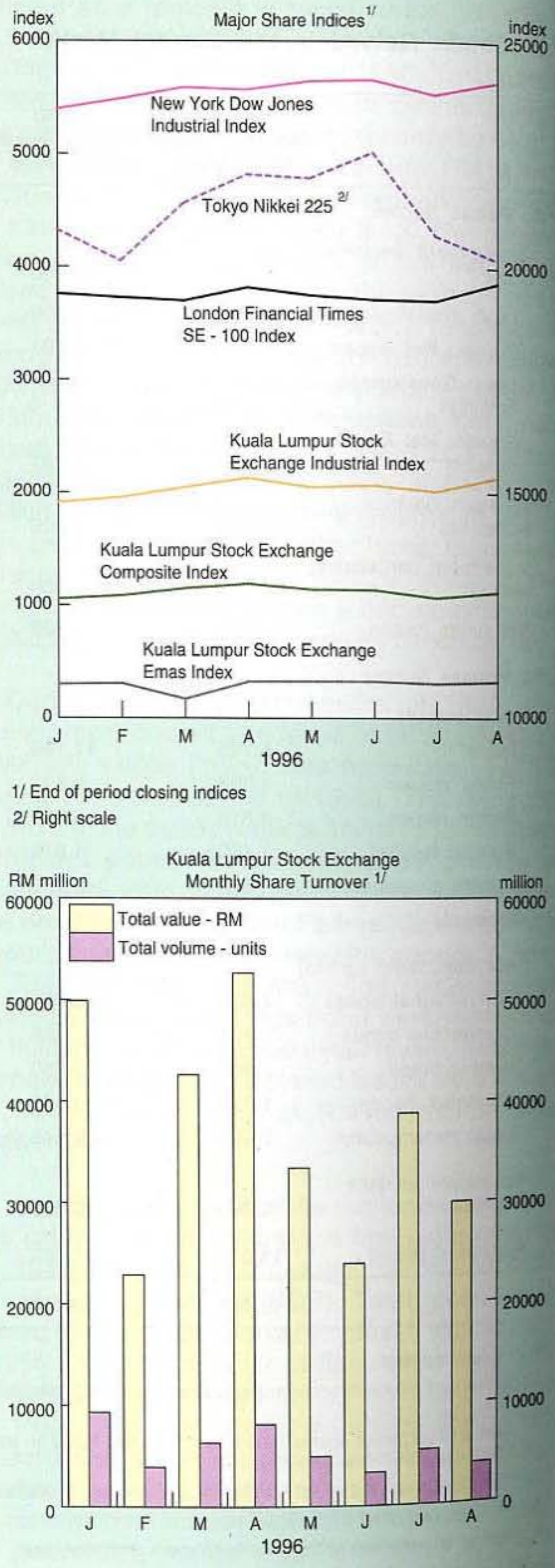
RAM has to date rated 34 financial institutions comprising 19 commercial banks, 10 merchant banks, three finance companies and two DFIs that have provided guarantees for various issues of PDS. In line with the country's aspiration of becoming a regional capital market, a second rating agency, the Malaysian Rating Corporation Berhad (MARC), was launched by the Minister of Finance on 5 September 1996. In addition to rating bonds, MARC will also undertake financial strength ratings as well as providing research and rating information services and related publications to issuers and investors.

The Kuala Lumpur Stock Exchange

Sentiments on the Malaysian stock market generally improved during 1996 with the market barometer, the Kuala Lumpur Composite Index (KLCI) remaining above the 1,000 psychological level throughout the first eight months of the year. Domestic macroeconomic and international developments continued to influence sentiments during the year. On the domestic front, the market was affected by concerns over developments on the current account of the balance of payments, interest rate movements and inflation, while international concerns centred on developments in other major overseas bourses, uncertainties in currency markets and other adverse political developments. Interest in the market centred not only on existing counters but also on initial public offerings which continued to attract substantial subscriptions from the investing public. The first eight months therefore, saw the total volume of trade expanding 89.0% compared with the same period last year and the KLCI touching 1,118.6 at the end of August 1996.

The stock market entered 1996 on a bullish note. The KLCI was lifted from below 1,000 to 1,055.4 in January 1996 before moving to a high of 1,149.1 at the end of the first quarter. Interest on the Kuala Lumpur Stock Exchange (KLSE) was centred on quality issues and situational stocks and the Second Board. Market sentiments were also buoyed by inflows of foreign funds amidst interest rate cuts in the US and other major industrial countries. However, the subsequent release of improved US employment data indicating that interest rate cuts were not likely as well as

Chart 9.3
Share Markets



1/ Refers to the Main Board and Second Board of the Kuala Lumpur Stock Exchange the mounting tensions between China and Taiwan forced the KLCI to retreat to 1,083.0 on 11 March 1996. The second half of March 1996, however, saw sentiments improving on the KLSE and the KLCI was lifted to 1,164.5 on 26 March 1996. The improved sentiments was mainly due to healthy corporate results on the domestic front and international developments such as the easing of both US interest rates and political tensions between China and Taiwan. In addition, interest in the Second Board continued unabated and the Second Board Index was lifted to an all-time high of 515.7 points on 19 April 1996 (298.7 points at the end of 1995). As overall buying interest was also sustained on the Main Board, the KLCI touched its highest level for the first half of 1996 at 1,189.5 points on 30 April 1996.

As the year progressed into the second half of 1996, price erosion was interspersed with sporadic buying activities which left prices somewhat higher. Market concerns in the period centred on speculation about domestic interest rates, adjustments to the SRR, the dismal performance of other regional bourses and the absence of foreign funds in the KLSE.

At the end of August 1996, however, the KLCI closed substantially higher (12.4%) by 123.4 points at 1,118.6 points compared with 995.2 points at the end of 1995, while the broader based Emas Index gained 15.2% to 321.9 points, as indicated in Table 9.14. The Second Board Index registered an impressive 79.8% increase to 537.1 points at the end of the period. On a sectoral basis, the rise in share prices was the highest for the mining counters (47.9%), followed by consumer products (31.5%), industrial products (20.9%), finance (15.9%), plantation (14.4%), construction (12.6%), properties (12.3%) and the trading and services sector (8.5%).

Total market capitalisation of the KLSE increased by 27.2% to RM719.5 billion at the end of August 1996 from RM565.6 billion at the end of 1995. Total trade as measured by the total turnover volume increased significantly by 89.1% to 45.3 billion units, compared with a decline of 60.1% during the same period of 1995. Similarly, in terms of value of turnover, a growth of 128.5% was registered to RM294.3 billion (January-August 1995: RM128.8 billion). Thus, market liquidity as measured by the turnover value to market capitalisation increased significantly to 40.9% at the end of the period from 23.2% at the end of August 1995.

Table 9.14

Kuala Lumpur Stock Exchange: Key Indicators

	1995	*1996 August*
Price Indices[1]		
Composite	995.17	1,118.57
Emas	279.47	321.86
Second Board	298.66	537.08
Industrial	1,822.75	2,137.04
Finance	7,561.95	8,766.90
Property	2,103.72	2,362.70
Plantation	2,446.93	2,798.42
Mining	386.49	571.63
Price Earning Ratio[1]	24.48	26.77
Market capitalisation[1] (RM billion)	565.63	719.48
Number of listed companies[1]	529	583
Turnover[2]		
Volume (million units)	23,973	45,322
Value (RM million)	128,793	294,261

[1] As at end of period.

[2] For January-August only.

Source: Kuala Lumpur Stock Exchange.

During the first eight months of 1996, another 54 new companies involving a total nominal capital of RM3.04 billion were listed on KLSE (January-August 1995: 32 companies), thus bringing the total number of listed companies to 583 at end of August 1996. Of this, 394 companies were listed on the Main Board, while 189 companies were listed on the Second Board.

FEATURE ARTICLE 6

The Collective Investment Industry in Malaysia

Introduction

The promotion of savings is an important element in the development agenda of the nation in consonance with the need to mobilise national resources for financing economic development and maintaining sustainable growth. An increasingly important conduit in the mobilisation of savings for financing investment is collective investment which has been and continues to be promoted not only as a vehicle for mobilising funds but also as a strategy towards broadening and deepening the domestic capital market as well as improving the nation's financial infrastructure. The mobilisation of savings for collective investment in Malaysia is undertaken through corporate schemes, which include provident funds and Government schemes such as the Employees Provident Fund (EPF) and the Social Security Organisation (SOCSO) as well as private retail unit trusts and client management schemes offered by professional managers.

Funds mobilised by collective investments have expanded rapidly, especially in the past eight years, underpinned by the rapid expansion of the economy, a steady increase in disposable incomes and household savings as well as more diversified avenues for channelling savings into productive investment. While the EPF and unit trusts under the Amanah Saham Nasional (ASN) and Amanah Saham Bumiputra (ASB) are expected to continue to grow and maintain their importance, private professionally - managed funds will expand more rapidly given the encouragement by Government to develop a vibrant and dynamic fund management industry. Institutions involved in the management of collective investment not only assist in mobilising savings for capital formation but also provide the services sector with an opportunity to play a more catalytic role in economic growth and development and, at the same time, build the expertise for fund management.

Overview of the Collective Investment Industry

The collective investment framework in Malaysia is made up largely of pension and provident funds, life and general insurance funds, unit trust and investment portfolio funds managed by merchant banks and asset management companies. These institutional funds had until the 1970s been concentrated mainly in the provident, pension and insurance funds. However, the last five years have

Table 1

Collective Investments

	1991		1992		1993		1994		1995	
	RM million	*% share*	*RM million*	*% share*	*RM million*	*% share*	*RM million*	*% share*	*RM million*	*% share*
Provident and Pension Funds	58,911	68.7	70,222	69.3	83,663	63.9	97,204	61.9	113,379	61.0
(of which EPF)	(53,272)		(62,169)		(72,674)		(84,485)		(98,133)	
Life and General Insurance Funds	11,432	13.3	13,605	13.4	16,309	12.5	20,905	13.3	24,831	13.4
Value of Investment Portfolio Funds Managed by Merchant banks	1,742	2.0	1,802	1.8	2,868	2.2	3,323	2.1	3,600	1.9
Unit Trusts	13,700	16.0	15,721	15.5	28,134	21.8	35,716	22.7	44,134	23.7
(of which ASN and ASB	(12,357)		(14,971)		(25,512)		(29,170)		(34,842)	
Total	85,785		101,350		130,974		157,148		185,944	

Source: BNM, Securities Commission, ASN, ASB and EPF

Table 2

Provident and Pension Funds (RM million)

	1991	1992	1993	1994	1995
EPF	53,272	62,169	72,674	84,485	98,133
SOCSO	2,344	2,740	3,281	3,866	4,469
AFF	2,282	2,614	2,779	3,099	3,528
PTF	—	1,637	3,694	4,437	5,916
TPF	206	203	207	206	191
MESF	282	283	308	322	314
Others	525	576	720	789	828
TOTAL	58,911	70,222	83,663	97,204	113,379

Source: Employees Provident Fund (EPF), Social Security Organisation (SOCSO), Armed Forces Fund (AFF), Pensions Trust Fund (PTF), Teachers Provident Fund (TPF) and Malaysian Estates Staff Provident Fund (MESF)

seen the emergence of private funds managed by merchant banks, unit trust funds and asset management companies as more individuals opt to diversify their enlarged savings increasingly into professionally-managed schemes.

At the end of 1995, total funds in collective investment are estimated at RM 186 billion (see Table 1). These funds are dominated by the provident and pension funds with assets totalling RM113 billion, contributing to an estimated three-quarters of the funds mobilised as collective investments. Another 23.7% is accounted for by unit trust funds, both private and Government-backed, with ASN and ASB providing a major proportion of the unit trust funds (78.9%). The market share of insurance funds was 13.4% while the funds managed by merchant banks and asset management companies remained relatively small in comparison.

In terms of growth however, the unit trusts had expanded significantly, with 26 companies (excluding ASN and ASB) in operation, and growth averaging 29.0% annually during the period 1991-95. The performance of privately-owned unit trusts is even more impressive, expanding at 108% annually, with 17 companies managing RM5.6 billion in 1995. The growth of funds managed by merchant banks also gained momentum in recent years, registering a growth rate of 22.1% per annum in the same period. The funds managed by licensed asset management companies, however were not significant, estimated at RM1,740 million as at end of 1995. The growth of provident and pension funds continued to be strong, expanding at an average rate of 17% per annum during the period with the EPF providing a major proportion of the funds mobilised. The insurance industry, meanwhile, registered an average growth of 21.9% per annum during the same period.

Taken collectively, the provident and pension funds invested a substantial proportion of their funds in Malaysian Government Securities (MGS). Notwithstanding this, however, the proportion invested in government securities has decreased from 66.8% in 1991 to 36.5% or RM41.4 billion in 1995 due mainly to the declining importance of government securities in the investment portfolio of the EPF as new issues of Government securities have declined. This is on account of improvements in Government's financial position as well as the Government's decision to liberalise EPF's investment. Through the mobilisation of savings in Government securities, the provident and pension funds have played a major role in providing an important source of non-inflationary financing for national development. As privatisation progresses and with the overall financial position of Government recording surpluses since 1993, this role has been reduced in favour of direct financing of development, as is already evident from increasing investment in several development projects and participation in corporate securities by these funds. Participation in equities has risen from 6% of total investment in 1991 to 20.3% in 1995. The channelling of funds into potentially higher-yielding investment is expected to continue with the growing sophistication and range of capital market instruments.

The **EPF** is the largest contributor to provident and pension funds, accounting for 82% of total funds mobilised. Its assets have almost doubled, from an estimated RM53 billion as at end of 1991 to RM98 billion as at end of 1995, with growth averaging 16% per annum. The EPF, which has been in existence since 1952, has 7,756,261 contributors. However, 68.5% of its members have credit balances of less than RM10,000. It is a leading financier of the nation's development process, with its role undergoing significant transformation in recent years. In the first 25 years of its existence, the EPF's role in development was essentially passive, investing about 90% of its funds in MGS. The proportion invested in MGS has since been reduced to about 40% of member's contributions although, in absolute terms, the investment in MGS stood at a significant RM39 billion at the end of 1995. This reflects, in part, the liberalisation of provisions of the EPF Act 1991 which permits the EPF to channel up to 50% of its funds in non-government securities.

In recent years, the role of the EPF has evolved to directly financing or part financing private sector initiatives in major development projects, particularly infrastructure and utilities. It has also participated in the construction of low and medium-cost houses in 1996 in line with the Government's efforts to alleviate supply shortages of this category of houses by increasing the supply and thereby availability of such houses at more affordable prices. Its investment in corporate securities has also increased from a share of 5.2% in 1991 to 16.0% in 1995 while the share of investment in money market instruments declined from 34.1% to 29.6% in the same period. The increased investment in corporate securities reflects EPF's strategy to reduce its dependence on interest income by investing in the secondary market as well as purchasing shares of unlisted companies with potential, thereby optimising returns.

The **Pensions Trust Fund (PTF)**, which was established in June 1991 as a self-financing fund to take over the Government obligations to meet the costs of payments of pension, gratuity and other benefits, has grown with increases in the civil service emolument bill, as 5% of emoluments are contributed to the PTF. Income is also derived from monthly contributions of employees under the Statutory and Local Authorities Pension Act, 1990 at the rate of 17.5% of the salary of pensionable officers. Starting with an initial allocation of RM500 million, PTF's total resources have expanded to RM5.9 billion in 1995. The resources have been mainly invested in corporate securities (55%) and term deposits (39%).

The **SOCSO**, which was set up to provide social security benefits to workers, has grown from RM2.3 billion as at end 1991 to RM4.5 billion as at end of 1995, an average growth rate of 17.3% per annum. SOCSO invests the bulk of its resources in MGS (38%), placements with the banking system (31%) and investment in corporate securities (28%). In the case of the **Armed Forces Fund (AFF),** it has expanded at an annual average rate of 11.1% from RM2.3 billion to RM3.5 billion during the same period. A substantial proportion of AFF's funds was invested in corporate securities (76%), while the rest of the funds were placed with the banking system (19%) or invested in fixed assets and Government securities in 1995. Other provident and pension funds, including the **Malaysian Estates Staff Provident Fund (MESF), Teachers Provident Fund (TPF)** and other statutory and privately-managed provident and pension funds, including the **PETRONAS** fund have also expanded, at an average annual rate of 7.2% during the period. Approximately one-quarter of these funds resources were invested in Government securities, 38-45% in corporate securities, with the rest in the form of deposits with the banking system and investment in fixed assets in 1995.

For the **life and general insurance industry,** however, cash and deposits continues to be the largest item in its investment portfolio, accounting for 25.5% of the total assets as at end of 1995, while investment in Government securities has remained at about 25%. Corporate securities were the third most important class of assets in 1995 with a share of 22.1% and the balance of funds was invested in loans, properties and other assets. In absolute terms, the amount of funds mobilised by the life and general insurance industry has increased from RM2.8 billion as at the end of 1991 to RM6.2 billion as at the end of 1995.

The **unit trust industry** managed a total fund of RM44 billion as at end 1995. The major funds in the industry are ASN and ASB (78.9% of unit trust funds), private unit trusts (12.8%) and other government-backed unit trusts (8.3%). ASN and ASB invested 85.2% of its funds in equities in 1995, with the remaining in money market instruments. In August, 1996 the Amanah Saham Wawasan 2020 was launched. This fund, managed by Pengurusan Amanah Saham Nasional Berhad, is offered for sale to all Malaysians aged 12 to 29 years old. Another fairly recent development is the establishment of unit trust funds based on Islamic principles. As at the end of 1995, six-Islamic based funds including Amanah Saham Darul Iman, Amanah Saham Kedah and Amanah Saham Bank Islam Tabung Pertama had been launched with a total net asset value of RM833,910. Another collective investment scheme catering especially for Muslims is the Lembaga Urusan dan Tabung Haji which mobilises savings of Muslims for the purpose of performing their pilgrimage. As at end of 1995, total resources of the Board stood at RM3.4 billion. Of this, some 44% was invested in corporate securities with the rest invested as placements with the banking system.

The steady growth of collective investment augers well for Malaysia as it will help to mobilise resources for financing growth while providing investors with the opportunity to invest in professionally-managed and diversified portfolio investment funds with a potentially higher rate of return than that offered by the banking system on deposits. In addition, private funding of privatised infrastructure projects, through funds mobilised for collective investment, promotes a more liquid and sophisticated capital market and allows individuals to participate in and directly benefit from such projects, while enhancing the contribution of the industry in developing the financial services sector. The growth of collective investment has also provided a broader base for Malaysia to promote itself as a regional capital market, capable of harnessing not only domestic but regional funds. Consequently, the Government has encouraged the development of private provident funds while allowing the EPF to diversify its investments. Aside from creating a supportive environment for fund management activities, the Government has also directed its efforts at streamlining the regulatory framework governing such activities, with a view to promoting a more efficient industry.

Prospects and Challenges

The collective investment industry will play an increasingly prominent role in the mobilisation of savings for financing capital formation. Collective investment activities will also continue to receive the encouragement of Government as it will assist in encouraging national savings and reducing the nation's resource gap while promoting Malaysia as a regional fund management centre. In this connection, a National Fund Management Policy has been proposed by the Securities Commission to address various aspects relevant to the development of an efficient fund management industry. It includes aspects relating to the mobilisation of both existing and new savings, efficient channelling of these funds into the capital market, enhancing the skills, capabilities and professionalism of local fund managers, providing incentives and streamlining the regulatory framework.

The future direction and growth of the collective investment industry will, to a large extent, depend on how the industry overcomes some of the challenges that it currently faces. While growth in the pension and insurance funds and the Government-backed unit trust funds, notably ASN and ASB, is expected to continue to dominate the collective investment industry in the coming years, the expansion of privately-owned unit trust funds, merchant banks and asset management companies will be influenced by their capacity to generate competitive returns for the investors. Several measures have been undertaken by the Government to promote the industry. These measures include the decentralisation of management of EPF funds, whereby the EPF could invest up to 15% of its funds in the equity market and contributors with more than RM50,000 in their retirement account are allowed to withdraw up to 20% of the balance for investment in approved funds and fund management institutions. Other measures that have been introduced to enhance savings and thereby collective investment include the launching of the Wawasan 2020 Fund, the provision of incentives to the corporate sector for the establishment of private pension funds as well as allowing qualified stockbroking companies to operate unit trusts and foreign fund management companies to operate and tap local institutional funds if they set up joint-ventures with a maximum foreign-equity share of 70%. Closed-end funds, a new collective investment vehicle to complement the unit trust industry, is also being promoted to further mobilise retail funds.

The emergence of new collective investment vehicles, particularly those that are privately managed, has made it necessary for the Government to continually review the regulatory environment to ensure that investors in these schemes are protected. In this regard, the Securities Commission has issued a number of guidelines on unit trusts, property trusts, closed-end funds and foreign fund management companies. Regulatory authorities aim at creating a sound market place, inculcating high standards of disclosure and accountability and emphasizing due diligence and professional responsibility, at the same time taking into account commercial practicalities.

It is recognised that the growth of the collective investment industry needs to be matched by adequate investment in training, resources and expertise by the industry if a high level of professionalism is to prevail. Currently, there still exists a lack of expertise in the industry as skilled and experienced fund managers are lacking and opportunities for training are limited. The moves by the Government to liberalise the capital market and promote the fund management industry will provide domestic fund managers with opportunities to gain experience through the management of a larger volume of funds. In addition, the presence of foreign fund managers will also assist in the development of professional skills which remain paramount to the further growth of the collective investment industry.

Another equally challenging task ahead for the Government and the industry is educating the investing public. The lack of adequate knowledge about alternative investment possibilities of these funds has hampered the further development of fund management activities. While the Government recognises the need to enhance knowledge about the industry, the task of educating the investing public can also be shared by industry participants and the mass media. Presently, the Securities Industry Development Centre of the SC facilitates the further development of the capital market through both research and training and acts as an information resource centre. However, more knowledge and greater transparency about the industry and the easy availability of comparative data on the performance of fund managers and rates of investment returns would help boost investors confidence, enhance knowledge and ensure competition among fund management companies. Competition will lead to investors' funds being rechannelled to managers providing better returns to investors, hence creating an environment that will encourage both professionalism in the industry and better returns for investors.

With the continued efforts of the Government to further develop the capital market, including the diversification and enlargement of the collective investment industry, in particular fund management activities, the future of the industry remains good. The further development of the industry will allow funds to be more professionally managed, mobilise additional resources for financing economic growth and reduce the Government's burden of providing retirement and social benefits. The enhancement of the industry will also allow Malaysia to build domestic expertise and attract foreign funds. At the same time, the domestic market will also be made more efficient, liquid and sophisticated in terms of investment instruments, given a broader variety of product choice which can include life policies, personal pension and retirement plans and the like. The emphasis on collective investment and fund management activities is also timely, given the expected liberalisation of the domestic financial services sector consistent with the nation's commitments under the General Agreement on Trade in Services.

Several regulatory and legislative measures were instituted during the first eight months of 1996 in line with efforts to further deepen and broaden the activities of the capital market. These include:

(i) **Listing of Infrastructure Project Companies (IPC)**

To encourage greater participation of the capital market in helping to meet the financing needs of large infrastructure projects, Malaysian-incorporated or joint-venture infrastructure companies with concessions or licences with a minimum of 18 years are effective from 19 September 1995, eligible to seek listing on KLSE without the need to meet the normal listing track-record requirements. Powertek Bhd. was the first such company to be approved by the Securities Commission (SC) and listed on KLSE under the IPC listing guidelines.

(ii) **Securities Borrowing and Lending and Regulated Short Selling**

To improve the settlement efficiency of the securities market and to facilitate the development of the financial derivative market, guidelines have been issued by the SC on Securities Borrowing and Lending. In line with this, the KLSE has introduced Rule 22 for short selling which has been approved by the SC and will be implemented through KLSE rules, effective from 30 September 1996.

(iii) **Code on Electronic Client-Ordering System**

The KLSE has issued a Code on Electronic Client-Ordering System for member companies in November 1995. Any member company intending to offer the electronic client ordering facility to the general public needs to obtain approval from the Exchange. The Code is aimed at protecting the interest of all parties with the objective of ensuring that stockbroking companies understand fully and comply with the requirements prior to the introduction of such a system.

(iv) **Listing of Closed-end Funds**

Guidelines for listing of Closed-end Funds, a new collective investment vehicle to complement the unit trust industry, were issued by the SC in October 1995. The listing of investment companies is aimed at further increasing investor participation in the local bourse through collective investment vehicles.

(v) **Amendments to the Listing Requirements**

In an effort to improve the transparency of the market and improve the regulatory framework, the following amendments to KLSE Listing Requirements were made:

(a) Substantial shareholders of companies seeking listing (on a selective basis) can choose to abide by the terms of a moratorium on their shares or to issue a profit guarantee instead;

(b) With effect from 1 January 1996, the paid-up capital requirements were revised as follows:

(i) Main Board Companies - minimum of RM40 million (previously RM20 million);

(ii) Second Board Companies - minimum of RM10 million but less than RM40 million (previously RM5 million but less than RM20 million).

(vi) **A Move From Merit-Based to Disclosure-Based Regulations for Initial Public Offerings (IPOs)**

The SC has made known its intention to move from a merit-based system to a disclosure-based system of regulation under a three-phase approach over a period of five years. The move is aimed at fostering a more competitive and transparent market as well as inculcating higher standards of disclosure, due diligince, corporate governance and accountability by companies. The move would also enable Malaysian investors to take a more professional stance in making their investment decisions in addition to ensuring that financial intermediaries such as merchant banks and underwriters take on an even more effective role in ensuring fair play in the marketplace. The first phase of the move towards disclosure-based regulation commenced in January 1996 with flexibilities given by the SC for issuers and underwriters to decide on their own IPO pricing as opposed to intervention by the SC in the past.

The Central Depository System (CDS) entered its fourth year of operation in 1996. As at end of August 1996, a total of 531 companies involving 42.3 billion units of shares had been mobilised into the CDS. During the period, a total of 339,218 new CDS accounts were opened, thus bringing the total number of accounts as at end of August 1996 to 1,410,100. The number of participants in the CDS increased to 92 at the end of August 1996, comprising 61 Authorised Depository Agents and 31 Authorised Depository Members.

Another significant development in the Malaysian capital market during the period under review was the commencement of operations of the Malaysia Monetary Exchange (MME) and the launching of the three-month Kuala Lumpur Interbank Offered Rate (KLIBOR) futures contract on 28 May 1996. The MME also plans to introduce a second financial instrument, bond futures, based on a liquid default-risk free paper by the first quarter of 1997. The Kuala Lumpur Options and Financial Futures Exchange (KLOFFE) which commenced operations on 15 December 1995, provides an avenue for both domestic and international investors to manage their risk exposures in an efficient and cost-effective manner. The innovative products offered by both the MME and KLOFFE reflect the increasing maturity of the financial market and the need for hedging mechanisms to add depth to the capital market.

In a further move to develop the capital market and position Kuala Lumpur as a regional financial centre, the Minister of Finance announced on 8 August 1996 the approval of the listing of foreign companies on KLSE. In the first phase of the exercise, foreign companies with substantial assets or operations and which are owned or controlled by Malaysians will be permitted to list on the Main Board. In addition, the listing of these companies must be through primary listings or these companies are listed elsewhere but intend to shift their primary listings to KLSE. The shares will be listed and traded in ringgit. In line with plans to gradually liberalise the market, the scope of foreign companies qualified to be listed on the KLSE would be widened, at an appropriate time, beyond those allowed under the first phase.

To encourage more Bumiputera-controlled companies to be listed on KLSE, the SC has on 27 August 1996 decided to allow flexibilities in its listing requirements for applications based on proforma accounts for Bumiputera-controlled companies which have pooled together for listing on KLSE. With the flexibilities, a group of Bumiputera-controlled companies applying for listing based on the strength of the group's proforma accounts would only have to comply with the criterion of being involved in the same or complementary business activities and not the other two criteria of having common directors and common controlling shareholders. However, such Bumiputera companies must fulfill the following conditions:-

(i) The group must have a genuine pooled arrangement;

(ii) The company which represents a significant contributor to profits within the proforma group should have been incorporated and have been in business operation for at least five years prior to making submissions to the SC;

(iii) Each company to be pooled together must have had more than 50% of Bumiputera equity ownership and must have been under the same Bumiputera shareholders with controlling shareholding for at least three years prior to making submission to the SC (or throughout the duration of the company if the company has been incorporated for less than three years); and

(iv) The company used as the listing vehicle must upon listing be a majority Bumiputera-controlled company wherein more than 50% of its equity is owned by Bumiputera-controlled company.

Notwithstanding the flexibilities given, other normal quantitative and qualitative requirements for listing would have to be complied with.

The **unit trust industry** grew rapidly during the first eight months of 1996 in line with the launching of another nine new unit trust funds with a total approved fund size of 4.6 billion units (January-August 1995: six unit trust funds, 2.4 billion units). In addition, approval was given to two existing unit trust funds [excluding Amanah Saham Nasional (ASN) and Amanah Saham Bumiputera(ASB)] to increase the fund size to a combined total of 1.12 billion units from 1.03 billion units. Among the new funds launched during the period were the Kuala Lumpur Bond Fund (KLMF Berhad), DCB-RHB Mudharabah International Fund (DCB-RHB Unit Trust Management Berhad), TA Balanced Fund (TA Unit Trust Management Berhad) and Mayban Income Trust Fund (Mayban Management Berhad). The Amanah Saham Wawasan (ASW) 2020 managed by Pengurusan Amanah Saham Nasional Berhad was launched on 28 August 1996 with the primary objective of inculcating the savings habit and improving the standard of living of the younger generation in the future. The Minister of Finance has also announced the setting up of a Cabinet Committee on the Promotion of Savings on 15 August 1996 aimed at further promoting national savings.

The Kuala Lumpur Commodity Exchange

On the Kuala Lumpur Commodity Exchange, crude palm oil (CPO) futures contract continues to remain the only active contract. During the first eight months of 1996, there was hardly any trading in Crude Palm Kernel Oil (CPKO), Cocoa and Tin, reflecting lack of liquidity . CPO futures contract, however, remained actively traded during the period.

Trading in CPO futures in the first eight months of 1996 declined by 14.9%, with a total turnover of 321,569 lots of 25 tonnes each, compared with 377,753 lots in the corresponding period of 1995. Translated into total tonnes traded, this is equivalent to 8.0 million tonnes of crude palm oil, which is higher than the level of Malaysia's crude palm oil production of 5.2 million tonnes for the first eight months of 1996. Similarly, the average daily turnover in the period dropped to 2,022 lots or 50,550 tonnes in 1996, compared with 2,311 lots or 57,775 tonnes attained in 1995.

Trading activity of CPO contract fluctuated from month to month. In January, trading was active, with 60,222 lots traded and daily turnover averaging 2,737 lots. Average prices for Spot Month January was RM1,279 per tonne, reflecting the strong demand for processed palm oil from Pakistan, Republic of China, Europe, Turkey, Egypt and Japan. Average physical prices for January was RM1,245 per tonne. As for February, turnover declined by 28,511 lots to 31,711 lots due to the higher number of public holidays during that month. Average price for Spot Month February was RM1,211 per tonne while the average price for Cash Market was RM1,221 per tonne. Compared to February, turnover for March and April improved to 33,024 lots and 39,188 lots, respectively. In May, however, turnover dropped to 24,733 lots, with the average Cash price recorded at RM1,281 per tonne and for futures at RM1,276 per tonne. For the months of June and July, the turnover increased to 44,064 lots and 53,826 lots, respectively. The average prices for both Cash and futures were RM1,160 per tonne and RM1,143 per tonne, respectively for the month of June while, for the month of July the average price were RM1,066 per tonne for Cash market and RM1,031 per tonne for futures market. However, turnover for August declined to 34,801 tonnes, with price for the cash market averaging at RM1,126 per tonne and the futures market at RM1,063 per tonne.

Table 9.15

KLCE: Trading Volume
(January-August)

Futures Contract[1]	*Total Turnover*				
	1995		*1996*		
	Lots	*Tonnes*	*Lots*	*Tonnes*	*% change*
Crude palm oil (CPO)	377,753	9,443,825	321,569	8,039,225	–14.9
Crude palm kernel oil (CPKO)	—	—	—	—	—
Cocoa	—	—	—	—	—
Tin	—	—	—	—	—

[1] One lot of CPO Futures contract comprises 25 tonnes, CPKO futures contract comprises 15 tonnes, cocoa futures comprised 10 tonnes.

Following the softening of the CPO prices in the physical market, the average monthly price for CPO futures in the KLCE declined to RM1,176 per tonne in the first eight months of 1996 compared with RM1,507 per tonne in the corresponding period of 1995. The highest monthly average price recorded was RM1,447 per tonne in January while the lowest was RM1,013 per tonne in August.

In efforts to increase liquidity in the CPO futures market, the KLCE had organised a Road Show in the country as well as overseas to attract entrepreneurs or "locals" on the KLCE. However, considering that crude palm oil is the only active commodity futures being traded on the KLCE, measures are being taken to instil greater interest in the commodities futures market. Towards this end, KLCE proposes to launch new futures contracts such as for pepper, lauric oil and sawn timber. To date, 55 entrepreneurs are registered with the KLCE. To enhance and expand the money market, KLCE had established a subsidiary namely Malaysia Monetary Exchange (MME). The first contract of MME was the three-month Kuala Lumpur Interbank Offered Rate (KLIBOR). The highest volume traded was on May 28, 1996, the opening day, when 1,134 lots were transacted. Up to the end of August 1996, the volume traded has averaged 314 lots per day.