

Monetary Policy and Financial Sector Developments

In the first eight months of 1999, monetary policy was eased to complement fiscal policy in supporting the economic recovery process in addition to promoting a stronger financial system. The priority of monetary policy was to provide a conducive environment for economic growth without generating inflation. Given the benign outlook for inflation over the short-term, Bank Negara Malaysia (BNM) was able to ease monetary policy to ensure that there was ample liquidity in the banking system to support the economic recovery process and to ensure that depositors continued to earn a positive real rate of return.

Monetary growth picked up by RM18.9 billion or 4.7% in the first eight months of 1999. The strong performance of the external sector, the improvement in economic and stock market activity as well as the continued easing of monetary policy have contributed to the expansion in money supply. During the first quarter of 1999, the annualised growth of the main monetary aggregates M1, M2 and M3 improved to -3.8%, 4.6% and 3.9% respectively at the end of March (end 1998: -14.6%, 1.5% and 2.7% respectively). The improvement registered in the period reflected mainly the increase in private sector liquidity, brought about primarily by a stronger external trade performance which contributed to a surplus in the current account of the balance of payments and a resultant increase in external reserves. However, loan growth remained subdued, with annualised growth declining to -4.7% during the first quarter reflecting primarily high loan repayments and the sale of Non-Performing Loans (NPLs) to Danaharta (RM10.3 billion) amidst a generally weak business environment.

The build-up in liquidity in the first quarter led to a further expansion in the resource surplus of the banking system which translated into continued easing of interbank money market liquidity. Consequently, the average 3-month interbank rates softened from 6.46% at end-1998 to 5.70% as at end-March 1999. The BNM intervention rate, however, remained unchanged at 7%. However, the average base lending rates (BLR) of commercial banks and finance companies remained unchanged throughout the first quarter at 8.04% and 9.50% respectively. Meanwhile, the average fixed deposit rates of commercial banks declined to between 5.39%-5.44% by end March while the average rates of finance companies declined to between 5.69%-5.90%. Despite the relative easing in interest rates, loans of the banking system continued to decline resulting in a decline in the loan deposit ratio from 91.4% at end 1998 to 88.3% at the end of March.

The expansion in monetary growth registered in the first quarter continued into the second quarter of 1999, with the annual growth in M3 increasing to 7.7% as at end-June. The external sector continued to exert an expansionary impact on money supply given the continued strong performance of exports, inflows of private capital and external borrowings by the Government. This in turn exerted an expansionary impact on the net external assets of BNM. Loans extended to the private sector continued, however, to decline by RM1.4 billion in the second quarter reflecting essentially high loan repayments and the sale of NPLs to Danaharta during the period of RM4.4 billion.

The moderating trend of inflation enabled a further easing of the BNM 3-month intervention rate from 7.00% to 6.50% on 5 April and again to 6.00% on 3 May. The reductions in the policy

rate were aimed at lowering interest rates to support the momentum of economic recovery in an environment of moderating price pressures. However, the 100 basis point reduction in the BNM 3-month intervention rate during the quarter was translated into a significant 240 basis point reduction in the 3-month interbank rate from 5.7% at end-March to 3.30% at end-June given the continued increase in liquidity in the banking system. Following the reductions in the intervention rate, the average BLR of commercial banks and finance companies declined from 8.04% and 9.50% at end-March to 7.24% and 8.50% respectively at end-June. Similarly, the average fixed deposit rates of commercial banks declined from 5.39% - 5.44% to between 3.75% - 3.80% by end-June, while that of finance companies declined from 5.69% - 5.90% to 3.78%-3.97%. Reflecting a pick-up in economic activities and improved market sentiments, total deposits of the banking system increased by 4.7%. However, total loans outstanding (including loans sold to Cagamas and Danaharta) declined 5.0% in the period resulting in a decline in the loan-deposit ratio to 86.8% at the end of June. Despite ample liquidity in the banking system, loan growth remained moderate due to high repayments as a substantial portion of the loans were short-term and self-liquidating trade and capital related facilities. Loan approvals as well as disbursements, lead indicators of recovery, were, however, higher at RM25 billion and RM78.1 billion in the second quarter compared to RM20.5 billion and RM77.5 billion respectively in the first quarter.

The monetary situation continued to improve in July and August reflecting the favourable developments in both the external sector as well as improved domestic economic conditions. M3 continued its growth trend with the annual growth rate increasing further to 8.5% at end August reflecting mainly the large trade surplus in the external account and its impact on the net international reserves of BNM and government activities. In line with the need to further strengthen the economic recovery by easing lending rates, the 3-month intervention rate was reduced by another 50 basis points to 5.50% on 9 August. This led to a decline in the average BLRs of the commercial banks and finance companies to 6.79% and 7.95% respectively by end-August from the end-July levels of 7.24% and 8.50% respectively. At these levels, BLRs are at the lowest historical level.

BNM continued to introduce new measures to promote the economic recovery in the first eight months of 1999. Effective 4 January 1999, guidelines on financing for the property sector were reviewed to help clear the existing backlog of properties. Banking institutions were not allowed to finance the development of new residential properties and shop houses exceeding RM250,000 each. The financing restriction also includes the development of hotels, resorts, office buildings, golf courses, clubs and shopping complexes. However, the end-financing for the purchase of completed residential and non-residential properties as well as those under construction were not affected. Banking institutions were also encouraged to extend end-financing to help clear the existing stock of properties, thus, stimulating new economic activities. In regard to the loan growth target of 8% by year end, with NPLs stabilising and the risk-weighted capital ratio (RWCR) increasing above the minimum requirement, the ability of banking institutions to lend is expected to be further enhanced. Together with the increasing loan approvals and good economic prospects in the latter half of the year, loan growth is expected to pick up. In addition, as part of efforts to stimulate domestic demand to strengthen the economic recovery, effective 28 July 1999, the minimum annual income eligibility criteria for credit cards was reduced from RM24,000 to RM18,000.

In the first eight months of 1999, further progress was made in the restructuring of both the banking and corporate sectors. By end-August 1999, Danaharta had acquired and managed loans amounting to RM39.3 billion from the financial system, comprising a total of 2,272 loan accounts. From the banking system, Danaharta had acquired and managed NPLs amounting to RM30 billion or 34% of total NPLs in the banking system. The resultant impact was a moderation of the net NPL ratio on a 6-month classification to 7.9% as at end-July 1999 as compared to 7.5% registered as at end-1998. Taking into account loans removed by Danaharta, the average monthly rate of increase in NPLs had moderated to 1.5% in the first seven months of 1999 from an average increase of 10.1% per month in 1998. As at end-August, Danaharta had used RM7.6 billion of the RM15 billion allocated to it for the purpose of NPL acquisitions. In addition, Danaharta has also expanded its activities in loan and asset management, as well as begun to dispose of some of the assets acquired from financial

institutions. On asset disposal, Danaharta conducted a restricted tender on 5 July 1999 to dispose a portion of its foreign loan assets with principal value of US\$142.82 million. At the close of its tender on 9 August, two principal bidders and 12 marketable bidders participated in this tender exercise. The recovery rate was 55.3%.

Danamodal has, since its inception, injected capital into 10 banking institutions in the form of Exchangeable Subordinated Capital Loans totalling RM6.4 billion. As at end-August 1999, Danamodal's capital injection amounted to RM5.692 billion given the repayment of capital by some banking institutions. With the capital injection, the RWCR of these 10 banking institutions strengthened to 12.5% at end August 1999 from 9.9% as at end September 1998, when the banking institutions were recapitalised.

As part of the continuing measures to create a strong and competitive banking system, a consolidation and rationalisation exercise for the domestic banking institutions was announced on 29 July 1999. With the consolidation exercise, the domestic banking groups will be better positioned to meet the future challenges from globalisation and liberalisation as well as contribute more effectively towards meeting the demands of a changing domestic economy.

In regard to corporate restructuring, the Corporate Debt Restructuring Committee (CDRC) has also made considerable progress. As at 21 September 1999, CDRC had received 63 applications with debts totalling RM35.02 billion. Of this total, 12 restructuring schemes involving debts of RM11.4 billion have been completed or are in the process of being implemented while another 2 cases with debts worth RM1 billion have been referred to Danaharta. In the meantime, 13 cases involving debts of RM3.1 billion have been rejected, while the debt restructuring schemes for 36 cases involving debts of RM19.6 billion are being worked out.

Money Supply

Monetary expansion continued to improve in the first eight months of 1999. This is attributed to the increased momentum in economic activities as well as large monthly trade surpluses and consequential increase in external reserves, which

contributed to the expansion in liquidity. Reflective of this expansion, growth of the broader monetary aggregate, M3, accelerated to 8.5% by end of August 1999 from 2.7% as at end of 1998.

Narrow money, M1, which is defined to include currency in circulation and demand deposits of the private sector, expanded at a significantly higher annual rate of 21.5% as at the end of August 1999, compared with a decline 14.6% as at end of 1998. The growth in M1 reflected the increased demand for demand deposits as a result of the pick up in economic activities especially in the second quarter. Demand deposits increased at a higher annual rate of 19.2% during the first eight months of 1999, as compared with a decline of 28.0% for the corresponding period of 1998, reflecting the recovery in the real economy and improved market sentiment. Meanwhile, currency in circulation recorded a positive growth of 0.9%, as compared with a decline of 6% for the corresponding period in 1998.

Broad money, M2, comprising M1 and narrow quasi money (constituting private sector holdings of fixed deposits, savings deposits and foreign exchange deposits with commercial banks and BNM, net negotiable instruments of deposit (NIDs) and repurchase agreements (repos) registered an annual growth of 11.3% as at the end of August 1999 (1.5% as at end-1998). This increment was largely due to the relatively faster growth in narrow quasi-money of 5.9% during the first eight months of 1999 (January-August 1998: 2.8%). This was due mainly to a larger expansion in both fixed and savings deposits by individuals, statutory authorities (including local government) and business enterprises, reflecting improvement in their financial and liquidity positions.

Growth of 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 placement of funds among these institutions, accelerated from an annual rate of 2.7% as at end 1998 to 8.5% as at end-August 1999. This was due to faster growth of savings and demand deposits. Savings and demand deposits grew from an annual rate of 4% and -13.6%, at the end of 1998 to 40.5% and 43%

institutions. On asset disposal, Danaharta conducted a restricted tender on 5 July 1999 to dispose a portion of its foreign loan assets with principal value of US\$142.82 million. At the close of its tender on 9 August, two principal bidders and 12 marketable bidders participated in this tender exercise. The recovery rate was 55.3%.

Danamodal has, since its inception, injected capital into 10 banking institutions in the form of Exchangeable Subordinated Capital Loans totalling RM6.4 billion. As at end-August 1999, Danamodal's capital injection amounted to RM5.692 billion given the repayment of capital by some banking institutions. With the capital injection, the RWCR of these 10 banking institutions strengthened to 12.5% at end August 1999 from 9.9% as at end September 1998, when the banking institutions were recapitalised.

As part of the continuing measures to create a strong and competitive banking system, a consolidation and rationalisation exercise for the domestic banking institutions was announced on 29 July 1999. With the consolidation exercise, the domestic banking groups will be better positioned to meet the future challenges from globalisation and liberalisation as well as contribute more effectively towards meeting the demands of a changing domestic economy.

In regard to corporate restructuring, the Corporate Debt Restructuring Committee (CDRC) has also made considerable progress. As at 21 September 1999, CDRC had received 63 applications with debts totalling RM35.02 billion. Of this total, 12 restructuring schemes involving debts of RM11.4 billion have been completed or are in the process of being implemented while another 2 cases with debts worth RM1 billion have been referred to Danaharta. In the meantime, 13 cases involving debts of RM3.1 billion have been rejected, while the debt restructuring schemes for 36 cases involving debts of RM19.6 billion are being worked out.

Money Supply

Monetary expansion continued to improve in the first eight months of 1999. This is attributed to the increased momentum in economic activities as well as large monthly trade surpluses and consequential increase in external reserves, which

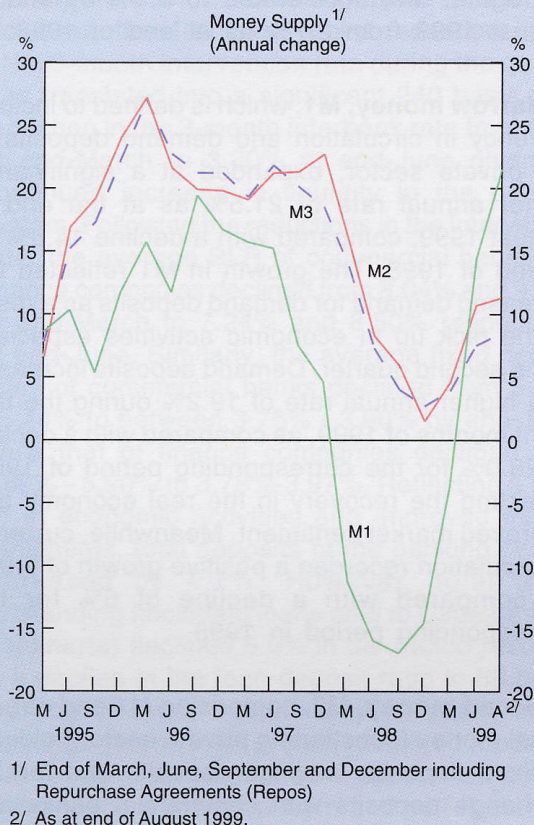
contributed to the expansion in liquidity. Reflective of this expansion, growth of the broader monetary aggregate, M3, accelerated to 8.5% by end of August 1999 from 2.7% as at end of 1998.

Narrow money, M1, which is defined to include currency in circulation and demand deposits of the private sector, expanded at a significantly higher annual rate of 21.5% as at the end of August 1999, compared with a decline 14.6% as at end of 1998. The growth in M1 reflected the increased demand for demand deposits as a result of the pick up in economic activities especially in the second quarter. Demand deposits increased at a higher annual rate of 19.2% during the first eight months of 1999, as compared with a decline of 28.0% for the corresponding period of 1998, reflecting the recovery in the real economy and improved market sentiment. Meanwhile, currency in circulation recorded a positive growth of 0.9%, as compared with a decline of 6% for the corresponding period in 1998.

Broad money, M2, comprising M1 and narrow quasi money (constituting private sector holdings of fixed deposits, savings deposits and foreign exchange deposits with commercial banks and BNM, net negotiable instruments of deposit (NIDs) and repurchase agreements (repos) registered an annual growth of 11.3% as at the end of August 1999 (1.5% as at end-1998). This increment was largely due to the relatively faster growth in narrow quasi-money of 5.9% during the first eight months of 1999 (January-August 1998: 2.8%). This was due mainly to a larger expansion in both fixed and savings deposits by individuals, statutory authorities (including local government) and business enterprises, reflecting improvement in their financial and liquidity positions.

Growth of 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 placement of funds among these institutions, accelerated from an annual rate of 2.7% as at end 1998 to 8.5% as at end-August 1999. This was due to faster growth of savings and demand deposits. Savings and demand deposits grew from an annual rate of 4% and -13.6%, at the end of 1998 to 40.5% and 43%

Chart 8.1
Monetary Trends



RM1.1 billion). However, new deposits by financial institutions declined by RM4.2 billion. The annual growth in total deposits of the banking system increased by 4.2% at the end of August 1999, compared with a decline of 0.5% at the end of 1998.

During the first eight months of 1999, the banking system's **total loans and advances** (including NPLs sold to Danaharta) declined RM2.4 billion or 0.6%, compared with an increase of RM0.8 billion or 0.2% during the corresponding period of 1998. However, given the recovery in domestic economic activities, total loans outstanding turned around to increase in the second quarter. As at end-August 1999, a large proportion of the outstanding credit (excluding NPLs sold to Danaharta) was channeled to finance the broad property sector (36.4%), manufacturing (15.5%) and consumption credit (12.2%). On an annual basis, however, total loan growth (including NPLs sold to Danaharta) was 0.5% at the end of August 1999 (August 1998:7.5%). The banking system experienced a resource surplus of RM25.9 billion during the first eight months of 1999, compared to a resource gap of RM11.3 billion during the corresponding period of 1998, resulting in the loan-deposit ratio easing from 91.4% at the end of 1998 to 85.7% at the end of August 1999. The net NPL of the banking system increased slightly from 7.5% (6 months net basis) of total loans at end-1998 to 7.9% at end of July 1999. The RWCR of the banking system which stood at 12.8% at end-August 1999 continued to be above the minimum international standard of 8% and the position at end-1998 (11.8%).

The **interbank money market** was active in the first eight months of 1999, although transactions were lower compared to the corresponding period in 1998. A monthly average volume of RM116.9 billion was transacted in the market during the first eight months of 1999, compared with an average of about RM164.1 billion during the corresponding period in 1998. Short-term funds constituted the major proportion of funds transacted, with the volume of overnight transactions averaging RM65.6 billion in the first eight months of 1999.

Interbank rates declined progressively in the first eight months of 1999, a continuation of trends established in the second half of 1998. The average

interbank rate for the 7-day to 6-month maturities in August 1999 ranged from 2.65% - 3.40% (5.85% - 6.45% in December 1998). The average 3-month interbank interest rates which declined from 11.07% in June 1998 to 6.48% in December 1998, declined further to 3.19% in August 1999, reflecting the easing of liquidity during the period. The overnight rates also decreased progressively, from 10.59% in April 1998 to 5.41% at end 1998 to a low of 2.54% in August 1999. In tandem with movements in the interbank rates, the average fixed deposit rates for both the commercial banks and finance companies fell to 3.75%-3.79% and 3.78%-4.04% respectively by the end of August 1999, compared to 5.74%-5.83% and 6.35%-6.57% respectively at the end of 1998. Similarly, the average savings deposit rate for the commercial banks and finance companies declined marginally by 129 and 156 basis points to 2.89% and 3.62% respectively at the end of August 1999. As at end-August 1999, the average BLR had declined to 6.79% and 7.95% for the commercial banks and finance companies respectively, compared to 10.61% and 12.65% at the end of 1998, reflecting the lower cost of funds.

Commercial Banks

During the first eight months of 1999, the commercial banks' **total resources** constituting 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, expanded by 5.4% or RM24.6 billion, compared with a decline of 5.3% or RM25.4 billion during the corresponding period of 1998. The increase in total resources was due mainly to the increase in deposits.

During the first eight months of 1999, **total deposits** mobilised by the commercial banks, including NIDs, New Investment Fund (NIF), special deposits and repos expanded by 6.1% or RM18.8 billion (January-August 1998: -1.7%) following the expansion in activities in the real economy as well as increases in disposable incomes, as indicated in Table 8.1. Deposits placed with the commercial banks accounted for 74.0% of the total deposits placed with the banking system.

Table 8.1

Commercial Banks: Deposits

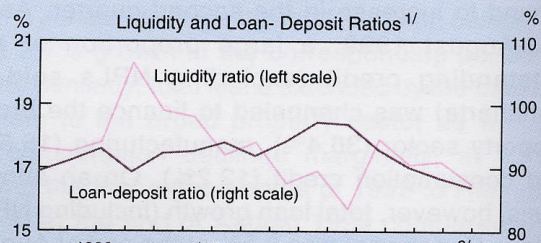
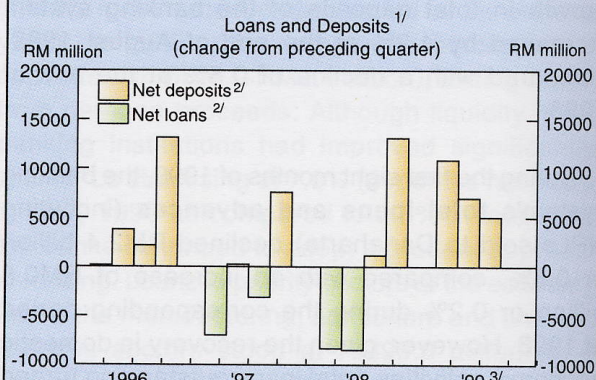
	Change During Period				As at End of August 1999
	1998		1999		
	January–August		January–August		
	RM million	%	RM million	%	RM million
Demand deposits	–12,040.0	–27.5	6,396.0	17.4	43,189.6
Savings deposits	–2,641.5	–10.2	5,459.0	20.4	32,258.7
Fixed deposits	14,859.2	9.0	24,106.2	13.7	199,768.7
NIDs ¹	–4,430.3	–11.2	–21,366.0	–58.0	15,492.4
Repos	–2,480.4	–16.5	–2,008.7	–12.8	13,624.8
Others ²	1,627.8	14.8	6,194.8	39.5	21,886.7
TOTAL	–5,105.2	–1.7	18,781.3	6.1	326,220.9

¹ Negotiable instruments of deposit.

² Include New Investment Fund and special deposits.

Source: Bank Negara Malaysia

The major proportion of commercial banks' resources (59.4%) was utilised for the financing of loans during the first eight months of 1999. Reflecting the banks' continuing concern about NPLs, **total loans and advances** extended by commercial banks contracted by 0.6% to RM283.8 billion (excluding loans sold to Cagamas Bhd) as at end of August 1999, compared with a growth of 4.2% to RM287.9 billion as at end of August 1998. This was primarily due to loans which were sold or managed by Danaharta, valued at RM11.3 billion for the period under review. If disposed loans were included, total new loans and advances extended by commercial banks would register an expansion of 3.3% or RM9,498.5 million. The decline in new loans and advances was primarily due to the decline in loans extended for the purchase of securities (-15.2%), the finance, insurance and business sectors (-12.7%) and the manufacturing sector (-1.6%) given that the bulk of the loans to these sectors had been disposed to Danaharta. This was, however, compensated by the expansion in loans for purchase of residential property (including loans sold to Cagamas Bhd) and credit cards which registered an increase of 7.1% and 18% respectively, following the launch of the house ownership campaign early in the year and the relaxation of requirements in regard to credit cards. Loans extended by the commercial banks accounted for 74.6% of the total loans granted by the banking system as at end-August of 1999.

Chart 8.2
Commercial Banks

1/ Including Repos

2/ Net deposits refer to the excess of commercial bank deposits over loans in each quarter while net loans refer to excess of loans over deposits

3/ As at the end of August 1999

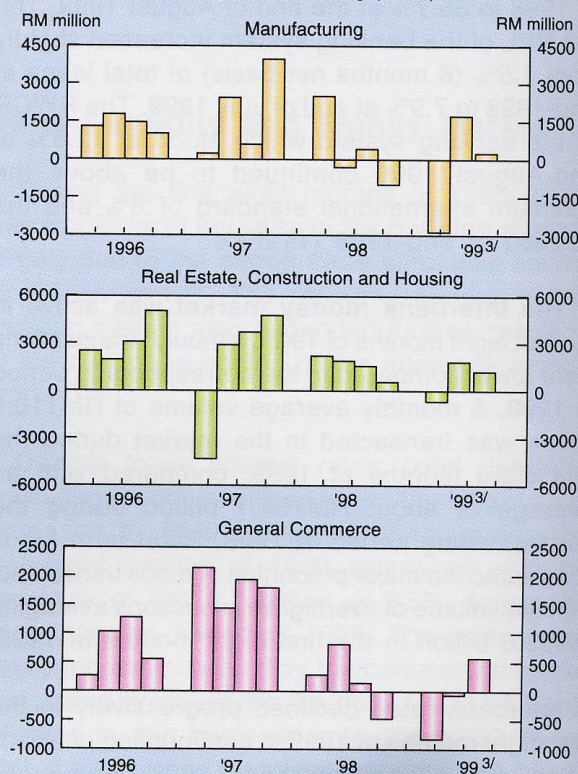
Lending to Major Sectors
(change from preceding quarter)

Table 8.2

Commercial Banks: Direction of Lending

	Change During Period				As at End of August 1999
	1998 January–August		1999 January–August		
	RM million	%	RM million	%	RM million
Agriculture	241.8	4.1	259.0	4.2	6,437.4
Mining and quarrying	441.7	56.1	−87.5	−7.3	1,112.7
Manufacturing	2,833.9	5.2	−899.3	−1.6	55,632.2
Finance, insurance and Business services	1,361.9	4.8	−3,848.4	−12.7	26,421.3
Construction	2,313.3	7.9	−1,022.9	−3.3	29,550.1
General commerce	1,474.3	5.0	−307.1	−1.0	29,955.6
Transport, storage and communication	1,109.8	12.9	139.4	1.2	11,559.2
Real estate	−373.4	−3.0	320.5	2.7	12,060.2
Housing ¹	4,230.0	11.1	3,090.2	7.1	46,457.6
Miscellaneous	−1,484.3	−1.8	−1,793.1	−2.3	75,810.7
TOTAL	12,149.0	4.2	−4,149.2	−1.4	294,997.0

¹ Including loans sold to Cagamas Berhad.

Source: Bank Negara Malaysia.

Loans provided by the commercial banks included those extended to the **priority sectors**, namely the Bumiputera Community, housing and small and medium-scale enterprises. During the first seven months of 1999, lending to Bumiputera

borrowers declined by 4.8% or RM3.2 billion, compared with an increase of 0.5% in the corresponding period of 1998. As at end of July 1999, total loans extended to the Bumiputera community amounted to RM80.5 billion or 33.7% of the loan base (loan amount outstanding as at end-1996), below the target requirement of 30% set out by the BNM 1998 Lending Guidelines. Of these loans, 17.5% was extended for construction, with 12.1% and 10.9% extended to the residential property and manufacturing sectors respectively. As at end-March 1999, commercial banks financed the purchase of 64,898 units of houses costing RM100,000 and below or 65% of the target (at least 100,000 units of such houses). In terms of new loans of RM500,000 and below, approved and disbursed to the small and medium-sized enterprises under the BNM 1998 Lending Guidelines, the commercial banks as a whole extended loans amounting to RM2.0 billion as at end-June 1999.

Bank Negara Malaysia introduced “The 1999 Lending Guidelines on Loans to the Small and Medium-Scale Enterprises” to replace “The 1998 Lending Guidelines on Loans of RM500,000 and below to the Small and Medium-Scale Enterprises”. Under the new guidelines, the commercial banks are required to extend loans of RM1,043 million to small and medium-scale enterprises by 31 December 2000. The main differences between the two guidelines are as follows:

Qualifying Criteria	The 1998 Lending Guidelines on Loans of RM500,000 and below to the Small and Medium-Scale Enterprises	The 1999 Lending Guidelines on Loans to the Small and Medium-Scale Enterprises
Size of loan	RM500,000 and below	RM5 million and below
Size of the small and medium-scale enterprises	Shareholders' funds not exceeding RM2.5 million for companies and net assets not exceeding RM2.5 million for registered businesses	Shareholders' funds not exceeding RM10 million for companies and net assets not exceeding RM10 million for registered businesses

The average interest rate of commercial banks' fixed deposits registered a decline of between 98 to 208 basis points during the first eight months of 1999, reflecting the prevailing liquidity conditions. The average fixed deposit rates for 1-month decreased from 5.82% per annum to 3.75% per annum. Similarly, the average fixed deposit rates for 3-month, 6-month and 12-month also declined from 5.83%, 5.76% and 5.74% per annum as at end-1998 to 3.75%, 3.76% and 3.79% per annum as at end-August 1999 respectively. The average savings deposit rate declined to 2.89% per annum in August 1999 from 3.87% per annum at the end of 1998. The daily weighted average interbank money market rates for most maturities dipped from a range of 5.41% to 6.48% per annum at the end of 1998 to a range of 2.91% to 3.82% per annum at the end of August 1999. The **average cost of funds** declined by 243 basis points to 3.74% per annum at the end of August 1999 in line with the decline in interbank money market rates (end of 1998: 6.17% per annum). Reflecting the cost of funds, the average lending rate declined to 8.00% per annum at the end of August 1999 from 9.72% per annum at the end of 1998. As the average lending rate declined at a relatively lower rate than the average cost of funds, the gross interest margin widened by 71 basis points from 3.55% at the end of 1998 to 4.26% at the end of August 1999.

The **liquidity position** of commercial banks fluctuated during the first eight months of 1999. However, the commercial banks' liquidity position remained higher than the required minimum level of 15%, with the highest level this year at 17.5% in April. The liquidity ratio of commercial banks stood at 16.5% the end of August 1999 compared with 17.9% at the end of 1998. The commercial banks registered a loan deposit surplus of RM42.4 billion during the first eight months of 1999 (January-August 1998: -RM21.8 billion), given the 6.1% increase in deposits placed with the commercial banks, compared to the 0.6% decline in loan growth. This resulted in the **loan-deposit ratio** of commercial banks declining 87.0% at the end of August 1999, against 92.9% registered at the end of 1998.

As at end-August 1999, 34 commercial banks were operating in the country, comprising 21 domestic banks and 13 foreign-controlled banks. Domestic banks operated a total of 1,586 branch offices at the end of July 1999, an increase from

1,557 at the end of July 1998, while branches of foreign-controlled banks remained unchanged at 144.

Islamic Banking

Islamic Banking operations expanded in line with the economic turnaround experienced this year. As at end-July 1999, in addition to Bank Islam Malaysia Berhad (BIMB), 54 other financial institutions (24 commercial banks, 18 finance companies, 5 merchant banks and 7 discount houses) offered Islamic Banking services under the Islamic Banking Scheme (IBS). **Total assets** of the Islamic banking system (IBS and BIMB) increased by 47.3% during the first seven months of 1999 to RM31.9 billion at end-July 1999 (July 1998: RM13.5 billion). Mobilisation of **total deposits** by the Islamic banking system increased by 48.3% in the same period to RM24.4 billion at end-July 1999, while **total financing** registered a decline of 8.0% to RM11.8 billion. Most of the new deposits were from investment deposits which registered an increase of 72.3% to RM17.1 billion at end-July 1999. During the first seven months of 1999, savings and current deposits increased by 19.9% to RM2.5 billion and 37.5% to RM4.2 billion respectively.

In terms of sectoral breakdown, a major portion of the financing was channeled to the housing sector (24.8% or RM2.9 billion), with 22.1% (RM2.6 billion) being extended to the construction and real estate sectors and the manufacturing sector accounting for 12.4% (RM1.5 billion). During the first seven months of 1999, the value of transactions recorded in the Islamic Interbank Money Market was RM281.6 billion, compared to RM115.4 billion transacted during the corresponding period of 1998. The value of Islamic Accepted Bills transactions recorded, inclusive of Green Bankers Acceptances, was RM 8.6 billion as at end-July 1999.

New measures were introduced as part of the continuous efforts to strengthen the development of the Islamic banking system. These measures include the following:

- (i) Effective 1 December 1998, the term "Interest-free Banking" was replaced by "Islamic Banking" and banking institutions were required to use this new term in all their Islamic banking operations, transactions and correspondence;

- (ii) From 2 January 1999, all banking institutions participating in the Islamic Banking Scheme are required to upgrade their Islamic Banking Unit to Islamic Banking Division, which are required to offer all aspects of Islamic Banking, including banking services and administration;
- (iii) Effective from 2 January 1999, the minimum funds of Islamic Banking was raised from RM1 million to:
 - (a) RM5 million for commercial banks, which will be gradually increased to RM20 million by 31 December 2000;
 - (b) RM5 million for finance companies, which will be gradually increased to RM10 million by 31 December 2000; and
 - (c) RM3 million for merchant banks, which will be gradually increased to RM6 million by 31 December 2000.
- (iv) From 4 January 1999, discount houses are permitted to participate in the Islamic Banking Scheme;
- (v) From 12 November 1998, IBS banking institutions were allowed to accept funds of less than one-month maturity from non-interbank customers. However, the funds received through the repos were to be utilised solely for Islamic banking purposes. Previously, only principal dealers were granted this privilege.
- (vi) On 8 December 1998, BNM introduced the Guidelines on Islamic Negotiable Instruments for two new deposit-taking products based on Islamic principles, namely Negotiable Islamic Debt Certificate based on the concept of Bai 'Bithman Ajil and Islamic Negotiable Instruments of Deposits based on the concept of Al-Mudharabah. The product provided an additional avenue for the Islamic bank and banking institutions participating in the IBS to mobilise domestic savings from the public. At the same time, it would promote the development of the Islamic money market with marketable and liquid instruments.

Finance Companies

In the first eight months of 1999, the **total resources** (mainly comprising capital and reserves, deposits and borrowings from other financial institutions) mobilised by finance companies declined by 8.4% to RM113.2 billion, compared with a decline of 12.5% during the corresponding period of 1998. The decline in total resources was partly the consequence of the absorption and mergers of 14 finance companies under the merger program for finance companies. This has also resulted in a large decline of 8.8% to RM89.1 billion in **total deposits** of finance companies at the end of August 1999, compared with a decline of 3.8% in the corresponding period of 1998. In tandem with the decline in resources, the **lending operations** of finance companies also contracted during the first eight months of 1999, with the **total loans** extended to the various sectors of the economy declining by 13.7% to RM74.7 billion at the end of August 1999 compared with a decline of 10.4% during corresponding period of 1998. The decline in total loans was also partly due to the sale RM3.6 billion loans to Danaharta since October 1998.

New deposits mobilised by finance companies declined by 8.8% to RM89.1 billion during the first eight months of 1999, compared with a decline of RM4.0 billion during the corresponding period of 1998. The major depositors were 'individuals' (52.7%), financial institutions (21.4%), business enterprises (14.1%) and the Government and statutory authorities (11.6%). In terms of different types of new deposits mobilised, increases registered during the period were for savings deposits (27.2% or RM1.0 billion), IBS deposits (63% or RM1.6 billion) and other deposits (278.4% or RM0.13 billion); while fixed deposits (6.3% or RM4.8 billion), NIDs issued (32.3% or RM4.2 billion) and repos (79.7% or RM2.3 billion) registered declines. Total outstanding deposits of finance companies as at end of August 1999 amounted to RM89.1 billion, representing 20.2% of total deposits of the banking system. As a percentage of total outstanding deposits, 79.6% was in the form of fixed deposits, while NIDs and savings deposits represented 9.8% and 5.3% respectively of the total outstanding deposits at the end of August 1999.

Table 8.3

Finance Companies: Deposits

	Change During Period				As at End of August 1999
	1998		1999		
	January–August		January–August		
	RM million	%	RM million	%	RM million
Savings deposits	–521.6	–14.5	1,002.6	27.2	4,689.8
Fixed deposits	4,340.2	5.8	–4,799.0	–6.3	70,903.1
IBS deposits ¹	496.2	40.2	1,554.4	63.0	4,022.9
NIDs ²	–4,226.0	–22.5	–4,154.8	–32.3	8,693.6
Repos	–4,093.5	–52.0	–2,303.5	–79.7	587.7
Others	–34.3	–15.5	125.3	278.4	170.3
TOTAL	–4,039.0	–3.8	–8,575.0	–8.8	89,067.4

¹ Islamic Banking Scheme² Negotiable Instruments of Deposit

Source: Bank Negara Malaysia

Lending activities of finance companies continued to contract during the first eight months of 1999 mainly due to the RM2.6 billion NPLs disposed to Danaharta and the direct effect of the absorption of finance companies by their respective holding commercial banks. This resulted in a 11.8% decline in total new loans and advances to RM81.3 billion during the first eight months of 1999, compared with a decline of 10.1% during the same period of 1998. Loans extended for housing increased by 5.4%, loans to general commerce decreased by 3% and real estate by 49.3%. Finance companies recorded a resource surplus of RM14.4 billion at the end of August 1999 (1998: RM6.5 billion) as the decline in loans extended was larger than the contraction in deposits for the January to August 1999 period. The **loan-deposit ratio** consequently declined from 88.6% at end-1998 to 83.8% at the end of August 1999.

The average fixed deposit rates of finance companies for all maturities declined during the eight months of 1999, following the lower interest rate environment. The average rate of fixed deposits for all maturities declined to between 253-262 basis points to 3.78%–4.04% per annum for the period January to August 1999 (end-1998: between 6.35%–6.57% for all maturities). Similarly, the average savings deposit rate also declined to 3.62% per annum at the end of August 1999 from 5.01% per annum at the end of 1998.

Table 8.4

Finance Companies: Direction of Lending

	Change During Period				As at End of August 1999
	1998		1999		
	January–August		January–August		
	RM million	%	RM million	%	RM million
Agriculture	-212.8	-16.2	-144.7	-15.6	783.0
Mining and quarrying	-64.5	-14.0	-64.7	-19.8	262.3
Manufacturing	-765.3	-13.7	-872.8	-21.7	3,153.9
Construction	-463.3	-5.5	-574.2	-7.5	7,047.8
Real estate	-53.8	-1.4	-1,595.9	-49.3	1,642.2
Consumption credit	-6,545.0	-16.5	-2,612.1	-8.1	29,537.6
Purchase of stocks/shares	-1,889.0	-18.1	-2,043.5	-22.5	7,028.4
Housing ¹	71.2	0.6	691.3	5.4	13,599.4
General commerce	-30.2	-0.8	-109.6	-3.0	3,494.0
Miscellaneous	-964.0	-4.4	-3,569.8	-19.5	14,737.5
TOTAL ¹	-10,916.7	-10.1	-10,896.0	-11.8	81,286.1

¹ Including loans sold to Cagamas Berhad.

Source: Bank Negara Malaysia.

The **average cost of deposits** of finance companies declined from 7.74% per annum in December 1998 to 5.00% per annum at the end of August 1999, in line with the decline in fixed deposit rates. Similarly, the average lending rate declined marginally by 21 basis points from 11.76% per annum in December 1998 to 11.55% per annum at the end of August 1999. With the average cost of deposits declining at a faster rate than the average lending rate, the gross interest margin had widened from 4.02% at end of December 1998 to 6.63% at the end of August 1999. In tandem with the declining average cost of deposits, the average BLR of finance companies stood at 7.95% per annum at the end of August 1999 from 9.50% per annum at end of 1998.

The **liquidity ratio** of finance companies fluctuated in the first half of 1999 with the liquidity ratio higher than the minimum requirement of 10.0% (12.5% for finance companies that issue negotiable instruments of deposit). The highest liquidity ratio of 19.4% was recorded in July, higher than the liquidity ratio of 14.0% recorded at end-1998. The liquidity ratio of finance companies stood at 18.9% in August 1999.

In terms of financing to the **priority sectors** as prescribed by the Central Bank's Lending Guidelines, lending to the Bumiputera community totalled RM29.7 billion or 38.8% of the total outstanding loans as at end of July 1999. As for lending to individuals for the purchase of houses priced at RM100,000 and less, the finance companies had extended financing for the purchase of a cumulative total of 25,081 units of such houses, exceeding the minimum requirement of financing at least one-half of 40,000 units by the end of March 1999. In terms of new loans of RM500,000 and below approved and disbursed to the small and medium-sized enterprises under the BNM 1998 Lending Guidelines, finance companies extended loans amounting to RM0.3 billion as at end-June 1999. With the introduction of the new 1999 Lending Guidelines, finance companies are required to extend loans of RM0.2 billion to small and medium-scale enterprises by 31 December 2000.

There are a total of 25 domestic finance companies with 1,005 branches in operation in the country as at end-July 1999.

Merchant Banks

The financial intermediation activities of merchant banks slowed down marginally in the first eight months of 1999. Total resources mobilised by merchant banks from **fund-based activities** declined by RM2.1 billion to RM37.1 billion at end of August 1999, compared with a decline of RM6.9 billion during the corresponding period of 1998 mainly due to a decline in loan portfolio and tradeable securities holdings. The new resources generated were mostly from repos. **Deposits** placed by financial institutions declined by 8.9% or RM0.5 billion to RM5.2 billion as at end of August 1999, compared with a substantial increase of 42% or RM1.8 billion in the corresponding period of 1998. The bulk of the total deposits continued to be concentrated in short-term fixed deposits of maturity period of up to six months. **Total deposits** (including repos) mobilised by the merchant banks declined by 3.8% from the end of 1998 to RM25.3 billion as at the end of August 1999. The share of deposits mobilised by merchant banks to the total outstanding deposits of the banking system declined marginally from 6.1% at the end of 1998 to 5.7% as at the end of August 1999.

During the first eight months of 1999, **total loans** extended by merchant banks declined 13.4% or RM3.0 billion compared with a decline of 1.7% during the same period of 1998. This was mainly due to a decline in lending to both the private and public sectors, by RM3.0 billion and RM0.1 billion respectively. The decline in lending to the private sector was due to RM1.6 billion loans being taken over by Danaharta in the period January to August 1999. Taking into account these loans, lending by merchant banks would have declined only by 5.2%. The dip in lending was caused mainly by lower lending to the finance, insurance and business sectors, purchase of securities and the construction sector. However, this was compensated in part by the increase in lending for real estate, purchase of passenger cars and others. As at end of July 1999, merchant banks extended 96.6% of total loans to the private sector while loans to the public sector accounted for 0.5%, with the balance being loans to foreign customers. At the end of August 1999, term loans constituted the bulk of the loans, amounting to RM9.8 billion or 51% of total outstanding loans of the merchant banks.

Table 8.5

Merchant Banks: Deposits and Lending

	Change During Period				As at End of August 1999
	1998 January–August		1999 January–August		
	RM million	%	RM million	%	RM million
Deposits					
Fixed deposits	338.6	2.2	–1,241.6	–7.7	14,823.4
IBS deposits ¹	15.5	5.6	–67.4	–18.0	307.2
Repos	–1,636.2	–41.6	668.5	20.4	3,952.4
NIDs	–309.8	–4.7	–23.2	–0.4	6,219.0
Others ²	5.1	1.4	–345.9	–93.2	25.4
TOTAL	–1,586.8	–6.0	–1,009.6	–3.8	25,327.4
Loans					
Term Loans	137.4	1.3	–1,026.7	–9.5	9,802.1
Revolving credit facilities	–390.0	–3.7	–1,860.5	–18.9	7,977.5
Others	–149.7	–8.4	–76.5	–5.0	1,455.0
TOTAL ¹	–402.3	–1.7	–2,963.7	–13.4	19,234.6

¹ Islamic Banking Scheme

² Includes merchant banks and other financial institutions

Source: Bank Negara Malaysia.

The merchant banks recorded a resource surplus of RM6.1 billion in the first eight months of 1999 (1998: -RM2.1 billion) due to the slower decrease in deposits (-3.8%) as compared with the decline in loans (-13.4%). This resulted in the merchant banks' **loan-deposit ratio** increasing to 75.9% at end-August 1999 as compared with the end-1998 position of 84.3%. With the decrease in fixed deposits rates, the average cost of deposits of merchant banks declined significantly from 7.45% at the end of 1998 to 4.15% at the end of August 1999, while the average lending rate fell from 10.71% at the end of 1998 to 8.14% at the end of August 1999. Thus, the gross interest margin widened marginally by 73 basis point to 3.99% at the end of August 1999 from 3.26% at the end of 1998.

The merchant banks' **liquidity** fluctuated in the eight months of 1999. However, the liquidity of merchant banks recorded was higher than the required minimum of 10% (12.5% for merchant banks that issue negotiable instruments of deposit). As at August 1999, the liquidity ratio of merchant banks stood at 19.4%, marginally lower than the 20.3% recorded as at end-1998.

Total income from fee-based activities for the first half of 1999 was RM0.18 billion, or 5.8% of total income of merchant banks, representing an increase of 61.6%, against a decline of RM0.11 billion or 53.8% during the corresponding period of 1998. The bulk of the fee-based income was generated mainly from activities in corporate advisory services (33.0%), underwriting (19.0%) and the syndication of consortium loans (15.0%).

Twelve merchant banks with 24 branch offices were operating in the country as end of July 1999. **Total assets** of the merchant bank decreased marginally by 5.3% from the end of 1998 to RM37.1 billion at the end of August 1999, compared with a decline of 15.6% during the same period of 1998.

Discount Houses

Overall performance of the discount houses declined in the first seven months of 1999 as reflected in the 7.5% decline in total deposits (including repos) mobilised by discount houses to 16.85 billion, compared with the decline of 11.7% during the corresponding period of 1998.

27.0% of the total deposits was placed by the commercial banks, with the balance being placed by the other financial institutions.

Discount houses registered a 9.6% decline in **total investment** from the end of 1998 to RM16.68 billion at the end of July 1999 (January-July 1998: -1%). Investment in Cagamas bonds, increased significantly by 241.7% to RM843 million in the period, compared with a decline of 18% registered during the corresponding period of 1998. However, investment in Private Debt Securities (PDS) posted a 5.4% decline to RM12.84 billion (January-July 1998: +0.1%) while investment in BAs declined by 26.0% to RM3.17 billion (January-July 1998: -44.7%). Investment in MGS and NIDS declined by 37.5% and 40.8% respectively during this period, compared with an increase of 26.1% and 40.6% during the corresponding period of 1998.

Development Finance Institutions

Development Finance Institutions (DFIs) are institutions established for the main purpose of promoting development in the agriculture and manufacturing sectors as well as exports and international trade. Total resources mobilised by the DFIs increased 18.9% to RM18.16 billion at end-June 1999 from RM15.28 billion at end-June 1998. As DFIs are not licensed to take deposits from the public, the major source of funding for the DFIs continued to be borrowings. Borrowings by the DFIs increased by 8.4% from RM7.20 billion at end-June 1998 to RM7.81 billion at end-June 1999 to account for 43% of the total source of funds for DFIs. Capital funds, which represented another primary source of funding for the DFIs, increased to RM2.22 billion at end-June 1999 (end-June 1998: RM1.31 billion).

In tandem with the recovery of the economy, lending activities of the DFIs also accelerated. **New loans** approved by the DFIs increased significantly by more than 500% to RM5.26 billion at end-June 1999 from RM0.87 billion at end-June 1998. The increase in lending activities was mainly by Bank Pembangunan and Infrastruktur, which recorded RM4.69 billion in loan approvals (end-June 1998: RM0.21 billion). The surge in loan approvals of Bank Pembangunan and Infrastruktur was mainly due to the substantially higher provision of loans in financing infrastructure

projects, as part of efforts to revive the economy. The infrastructure projects financed included the construction of the rail system from Kuala Lumpur Sentral to the Kuala Lumpur International Airport, the Central Station in Brickfields, Cyberjaya project, Port Klang West Port, as well as the Automatic Light Rail Transit Joint Venture, Light Rail Transit System and Shahpadu Highway Project.

Consequently, loans to the real estate and construction sector rose to RM4.55 billion to account for 86% of total loans approved at end-June 1999 (end-June 1998: RM0.02 billion or 2%). However, loans to the manufacturing and shipping sectors declined by 19.4% and 42% respectively to RM0.44 billion and RM0.10 billion at end-June 1999 (end-June 1998: RM0.54 billion and RM0.17 billion respectively).

DFIs continued to implement a number of specialised assistance schemes. Among the schemes implemented is the **Fund for Food** scheme, which was launched in early 1993 with an initial allocation of RM0.30 billion, which was subsequently increased to RM0.70 billion in 1997. In May 1999, the allocation was increased by another RM0.30 billion to RM 1 billion. The new allocation of RM0.30 billion managed by Bank Pertanian Malaysia will be allocated to the Farmers Association for distribution to their members. The

maximum lending rate under this Fund remained at 4% per annum. A total of 613 applications amounting to RM0.12 billion was approved in the first nine months of 1999 (January – September 1998: 388 applications amounting to RM0.11 billion). The number of applications approved as at 30 September 1999 totalled 2,302 applications with a value of RM0.62 billion. Meanwhile, the value of disbursements increased to RM0.50 billion as at 30 September, 1999.

Subsequent to the 1985/86 recession, the **Enterprises Rehabilitation Fund (ERF)** was established in 1988 to provide financial assistance to ailing but viable Bumiputera enterprises. The total amount approved was increased by RM0.01 billion during the first seven months of 1999 to total RM0.66 billion at end of July 1999, compared with an increase of RM0.03 billion during the corresponding period of 1998. In the same period, drawdowns amounted to RM0.61 billion. In terms of sectoral distribution, a major proportion of these loans was extended to housing (RM0.39 billion), property (RM0.06 billion), "Skim Rundingan Terus" (RM0.05 billion) and the construction (RM0.04 billion) sectors.

The **ASEAN - Japan Development Fund (AJDF)**, a revolving fund set up in January 1989 with an initial funding allocation by the Overseas Economic Cooperation Fund (OECF) and the Export - Import Bank of Japan (EXIM), is administered by Bank Pertanian, Bank Industri, Bank Pembangunan and MIDF. The Fund is aimed at assisting the development of small and medium-scale industries. During the first seven months of 1999, the implementing DFIs approved a total of 2 applications amounting to RM300 million, compared to 4 applications (RM660 million) during the corresponding period of 1998. Thus, as at 31 July 1999, total loans approved amounted to RM1.92 billion for 4,361 projects. Of this, RM1.53 billion was provided by OECF's allocation, while the balance was from EXIM's allocation.

The **New Entrepreneurs Fund (NEF)**, yet another assistance scheme aimed at encouraging more small and medium-scale Bumiputera entrepreneurs to venture into business, was launched in December 1989, with an allocation of RM0.75 billion. Given that the NEF is a revolving fund and insufficient to meet demands as it involved long repayment periods, the NEF allocation was increased by another RM0.5 billion on 15 July,

Table 8.6

Direction of Lending by DFIs
(RM million)

	June 1998	% share	June 1999 ^a	% share
Manufacturing	543.22	62.5	437.61	8.3
Shipping	169.93	19.6	98.40	1.9
Agriculture	63.44	7.3	132.12	2.5
Real estate & Construction	17.14	2.0	4,550.23	86.5
Mining and Quarrying	0.75	—	1.25	—
Others	74.43	8.6	42.35	0.8
TOTAL	868.91	100.0	5,261.96	100.0

^a Preliminary data.

Source: Bank Pertanian Malaysia, Bank Pembangunan & Infrastruktur Malaysia Berhad, Malaysian Industrial Development Finance Bhd., Bank Industri Malaysia Bhd., Export-Import Bank of Malaysia Bhd, Sabah Development Bank Bhd., Perbadanan Pinjaman Sabah and Borneo Development Corporation (Sabah) Sdn. Bhd.

1998 to stand at the current RM1.25 billion. On 3 May 1999, the rate of interest for all loans under NEF was reduced from 8% per annum to 6% per annum, following the reduction of the 3-month intervention rate from 6.5% to 6.0% on the same day. The implementing agencies of the Fund include MIDF, Bank Pembangunan, Bank Industri and 9 other commercial banks. A total number of 257 applications totalling RM0.12 billion was approved during the first nine months of 1999 (January – September 1998: 53 applications valued at RM0.06 billion). This brings the total number of applications approved to 2,443, valued at RM1.18 billion, with disbursements at RM1.05 billion as at end of September 1999.

The **Bumiputera Industrial Fund (BIF)** was established on 4 January 1993 with a total allocation of RM0.1 billion to encourage the vendor development programme among the small and medium-scale Bumiputera entrepreneurs. As at 30 September, participating financial institutions had approved 99 applications totalling RM0.10 billion of which RM0.09 billion had been disbursed. As the fund allocation under the fund had almost been fully utilised, the scheme would be absorbed under the NEF since BIF and NEF had the same target group.

The **Industrial Adjustment Fund (IAF)** launched in 1991, with an initial allocation of RM0.5 billion, was 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, relocation and diversification. As at end-September 1999, the number of approved applications received stood at 27, with an aggregate value of RM0.11 billion (1998: RM0.11 billion), while drawdowns amounted to RM0.095 million (1998: RM0.09 billion). The IAF was terminated effective 4 August 1999. The unutilised portion of the IAF would be reallocated to the Fund for Small and Medium-Industries.

The Government set up the **Special Fund for Tourism (SFT)** in March 1990 with an allocation of RM0.2 billion, aimed at financing the development of tourism-related projects. As no new application has been approved since 31 December 1997, this revolving fund has been terminated. As at end of September 1999, the number of applications stood at 200 with a value

of RM0.22 billion, while disbursements amounted to RM0.20 billion.

Other funds administered by DFIs and other participating finance institutions (PFI) included the **Fund For Small and Medium Industries (FSMI)**. The FSMI was launched in January 1998 with a total allocation of RM1.5 billion to promote new productive capacity as well as utilisation of existing capacity in the manufacturing, agro-based and services sectors. To enhance the effectiveness of the FSMI and in addressing the problems faced by the small and medium scale industries (SMIs) which have been affected by the economic slowdown, the Government had on 8 May 1998 relaxed some of FSMI Operational Guidelines as follows:

- (i) All activities of SMIs under the manufacturing, agro-based and services sectors are eligible for loans under the scheme. Previously, only SMIs involved in the export-oriented industries or having linkages with export or import substitution were eligible;
- (ii) The minimum loan amount was lowered from RM250,000 to RM50,000 per customer;
- (iii) The maximum loan amount was increased from RM2 million (RM3 million in special cases) to RM5 million per customer;
- (iv) The restriction that only 20% of the loan can be used as working capital has been lifted;
- (v) The shareholders' funds limit of the SMIs has been increased from RM5 million to RM10 million; and
- (vi) The RM50 million sales turnover limit has been withdrawn.

To speed up the channelling of loans to the SMIs, the list of PFIs under the FSMI had been extended to 50 institutions since 5 October 1998 to include all commercial banks, 10 finance companies, Bank Islam Malaysia Berhad and 4 DFIs. The maximum lending rate under the FSMI had been reduced twice since its implementation on 2 January 1998 to ensure the SMI companies benefit from the increased liquidity in the banking system, on 5 December 1998 from 10% per annum to 8.5% per annum and again on 3 May 1999 to 6.5% per annum.

Consequent to the various measures undertaken by the Government to improve the scheme, the number of loan approvals increased from 78 as at 8 May 1998 to 3,345 as at 30 September 1999 totalling RM0.11 billion and RM2.36 billion respectively. Meanwhile, RM1.16 billion has been disbursed. Due to the encouraging response from the SMIs, the allocation under the FSMI was increased to RM1.85 billion with effect from 4 August 1999.

Recognising the problems faced by the SMIs especially those that had been affected by the economic downturn, the Government had on 23 November 1998 established the **Rehabilitation Fund For Small and Medium Industries (RFSMI)**, primarily aimed at providing financial assistance to viable SMIs facing NPLs and temporary cash flow problems. Basically, the features of the loans under RFSMI are similar to that of FSMI except the following:

- (i) Lower lending and funding rates (at 5.0% per annum and 1.0% per annum respectively compared to 6.5% and 4.0% under FSMI);
- (ii) Wider margin for the lending institutions as they bear higher credit risks under the scheme (4.0% points compared with 2.5% points under FSMI); and
- (iii) 30% of the total approved limit can be utilised to refinance and restructure the existing NPLs which is not allowed under the FSMI.

Previously there were 50 PFIs under the RFSMI. Like FSMI, the list of PFIs had been extended to 56 institutions to speed up the channeling of funds to the SMIs. The extended list of PFIs had included all commercial banks, 17 finance companies, Bank Islam Malaysia Berhad and 4 DFIs. As at 30 September 1999, the participating banking institutions had approved 254 applications under the RFSMI amounting to RM0.21 billion, of which RM0.11 billion had been disbursed to the borrowers. To ensure effective utilisation of resources, the Government had reduced the allocation for RFSMI from RM0.75 billion to RM0.50 billion with effect from 4 August 1999.

The **Ship Financing Facility (SFF)** was established on 30 October 1992 with a total allocation of RM600 million to increase shipping capacity to carry Malaysia's cargo, as a measure

to overcome the problem of deficit in the services account of Malaysia's balance of payments. As at 30 September 1999, Bank Industri Malaysia Berhad, the sole PFI, had approved 33 applications amounting to RM0.55 billion of which RM0.52 billion had been disbursed to the borrowers.

In May 1998, the **Special Scheme For Low and Medium-Cost Houses (SLMCH)** was launched with a total allocation of RM1 billion to finance the eligible developers to construct low and medium-cost houses costing RM150,000 and below per unit. The granting of the bridging finance under the scheme was for a maximum of 3 years or up to the date of completion of the housing project, whichever is earlier. As at 30 September 1999, the banking institutions had approved 139 applications amounting to RM0.94 billion of which RM0.22 billion had been disbursed. Due to the slow rate of loan approvals and disbursement, the Government had decided to terminate the scheme with effect from 4 August 1999. The unutilised allocation under the scheme has been transferred to FSMI.

Other Financial Institutions

National Savings Bank

Total resources of the National Savings Bank (NSB) increased by 15.6% to RM8.9 billion at end-June 1999 (end-June 1998: RM7.7 billion). The increase was attributed to an 11.1% rise in **deposits** mobilised by NSB to RM7.0 billion (end-June 1998: RM6.3 billion). Fixed deposits rose 36.8% to RM2.6 billion to account for 37.6% of total deposits (end-June 1998: RM1.9 billion). Deposits mobilised through the GIRO scheme increased slightly by 3.5% to RM2.4 billion to account for 34.4% of total deposits, while other types of deposits declined.

In tandem with the increase in total resources, investments rose 20.4% to RM5.9 billion at end-June 1999 (end-June 1998: RM4.9 billion). The bulk of NSB's resources was invested in long and short-term deposits as well as in subsidiaries and associated companies, amounting to RM2.4 billion or 40.7% of total investments. Investments in MGS amounted to RM2.1 billion to account for 36.4% of total investments, followed by investments in stocks and shares which accounted for 22.9% of total investments.

Reflecting the recovery in economic activities, lending activities of NSB also picked up. **Loans** provided by NSB increased by RM76 million or 4.8% to RM2.2 billion (end-June 1998: RM2.1 billion). The bulk of the loans continued to be extended to individuals, recording an increase of 15.1% to account for RM1.2 billion or 53.5% of total loans. Loans granted for hire-purchase financing declined by 24.5% to RM660 million or 30.3% of total loans at end-June 1999 (end-June 1998: RM874 million). Loans extended to the corporate sector rose sharply by 77.7% to RM275.5 million (end-June 1998: RM155.0 million). In consonance with the easing of the minimum monthly repayment on credit cards, loans extended through credit cards rose 20.2% to RM31.8 million (end-June 1998: RM26.5 million).

The total number of NSB branches and sub-branches declined to 445 in June 1999 from 458

in June 1998 due to the merging of some branches. At the same time, 625 post offices also provided NSB facilities.

Provident and Pension Funds

The provident and pensions funds (PPFs) continued to be the largest source of long-term domestic financing for the public sector. Total resources mobilised by the nine PPFs, comprising the Employees Provident Fund, the Social Security Organisation, the Armed Forces Fund and the Pensions Trust Fund and five other private provident and pension funds, increased by 13.7% to RM184.2 billion at end June 1999 (end-June 1998: RM162 billion). Total contributions to the PPFs were marginally lower at end-June 1999, amounting to RM11.9 billion compared to RM12.1 billion at end-June 1998. However, net contributions were higher at RM7.9 billion at end-June 1999, an increase of 11.3% from RM7.1 billion at end-June 1998. This was due to the lower withdrawal of RM4.0 billion at end-June 1999 compared to RM4.9 billion at end-June 1998.

The Employees Provident Fund (EPF) remained the largest provident and pension fund in the country, accounting for RM158 billion or 85.8% of total resources of PPFs. Total resources of EPF rose 13.6% to RM158 billion at end-June 1999 from RM139 billion at end-June 1998, mainly due to increased returns from investments. Income from investments increased 9.8% to RM5.3 billion (end-June 1998: RM4.8 billion). EPF membership increased by 978,683 contributors or 11.7% to 9,368,153 contributors (end-June 1998: 8,389,470 contributors), reflecting the more favourable labour market due to the recovery of the economy. Investment in MGS increased by 23.9% to RM47 billion during the period under review, accounting for 30.4% of total investments. Investment in deposits placed with BNM increased significantly by 202% to RM10.4 billion to account for 6.7% of total investments (end-June 1998: RM490 million or 3.6% of total investments). Similarly, investment in loans and debentures rose significantly by 72.4% to RM40.5 billion, representing 26.3% of total investments (end-June 1998: RM23.5 billion or 17.4% of total investments). However, EPF investment in corporate securities and in the money market declined by 30.3% and 15.2% respectively to RM27.4 billion and RM28.5 billion at end-June 1999, mainly due to the less favourable equity

Table 8.7

National Savings Bank (as at end of period)

	June 1998	June 1999 ^P
Deposits ¹ (RM million)		
Savings	1,478.0	1,403.4
Fixed	1,896.4	2,635.1
Save-As-You-Earn	18.6	15.2
GIRO	2,329.0	2,411.0
Premium Savings Certificates	544.7	543.4
Investments at book value (RM million)		
MGS	2,106.2	2,142.7
Stocks and shares ²	1,345.4	1,351.5
Others ³	1,452.8	2,398.5
Loans (RM million)		
Individuals	1,012.8	1,165.8
Corporate	155.0	275.5
Credit Cards	26.5	31.8
Hire Purchase	874.4	660.4
Number of NSB Branches ⁴	458	445
Number of post offices with NSB facilities	624	625
Number of depositors ('000)	8,760	8,170
Savings	3,053	2,580
Fixed ⁵	123	—
Save-As-You-Earn	17	14
GIRO	5,567	5,576

¹ Includes interest credited.

² Includes trustee and non-trustee shares and warrants.

³ Includes long and short-term deposits.

⁵ Fixed savings scheme converted to certificates from 9 August 1998.

⁴ Includes mini and sub-branches.

^P Preliminary data

Source: National Savings Bank

market which has yet to recover to pre-crisis levels and the low interest rate regime.

The **Social Security Organisation (SOCSO)**, which was established under the Employees Social Security Act 1969 to provide security benefits to workers through the Employment Injury Scheme and Invalidity Pension Scheme, mobilised total resources amounting to RM7 billion at end-June 1999, an increase of 12.9% compared to RM6.2 billion at end-June 1998. Most of SOCSO's resources was invested in deposits and the money market (50%), followed by MGS (35.4%) and corporate securities (8.3%).

The **Armed Forces Fund (AFF)** was established to provide superannuation benefits to servicemen in the armed forces. Total resources mobilised by the AFF rose slightly by 4.4% to RM4.7 billion at end-June 1999 (end-June 1998: RM4.5 billion). However, net contributions to the AFF remained negative due to higher net withdrawals. This was

attributed to the lower increase in recruits compared to the number of retirees, as well as withdrawals for housing and payments made under the death and disability schemes. The bulk of AFF's investments was in corporate securities (RM3.8 billion or 81% of total investments), while RM756 million (16.1%) was invested in deposits and the money market. Investment in MGS remained unchanged at RM5 million, while RM7.1 million was invested in government-guaranteed loans.

The **Pensions Trust Fund (PTF)** was established under the Pensions Trust Fund Act 1991 to assume the government's obligations in meeting the cost of payments of pension, gratuity and other pension benefits of the public sector. Total resources mobilised by the PTF rose 20.4% to RM13.6 billion at end-June 1999 from RM11.3 billion at end-June 1998. The increase in total resources was mainly due to a 8.5% increase in the funds contributed by the federal and state governments, as well as statutory and local

Table 8.8

**Provident and Pension Funds
(as at end of period)**

	<i>Total Resources (RM million)</i>		<i>Malaysian Government Securities (RM million)</i>		<i>Net Contributions (RM million)</i>	
	<i>June 1998</i>	<i>June 1999^P</i>	<i>June 1998</i>	<i>June 1999^P</i>	<i>June 1998</i>	<i>June 1999^P</i>
EPF	139,131	158,054	37,922	46,987	3,413	3,868
SOCSCO	6,184	7,034	2,759	2,489	241	233
AFF	4,547	4,683	5	5	(78)	(109)
PTF	11,338	13,563	0	0	3,622	3,956
Private PPFs	762	863	244	223	(39)	(17)
TOTAL	161,962	184,197	40,930	49,704	7,159	7,931

^P Preliminary data.

Figures in parentheses indicate net withdrawals.

Source: Employees Provident Fund, Social Security Organisation, Armed Forces Fund, Pensions Trust Fund and five other private provident and pension funds (Malaysian Estates Staff Provident Fund, MAS Malaysia Provident Fund, SESCO Employees' Provident Fund, Petronas Retirement Benefit Scheme and Jendarata-Bernam Provident Fund).

authorities and a 9.7% increase in refunds of employers' contribution to the EPF and other approved funds. The bulk of PTF's resources was invested in deposits and the money market (56.8%), followed by investment in equity and trust funds (31.6%), as well as loans and corporate bonds (11.6%).

Total resources mobilised by the five private PPFs rose by 13.2% to RM863 million at end-June 1999 from RM762 million at end-June 1998. In terms of investments, the bulk of it was placed in corporate securities (38.3%), followed by deposits and the money market (34.6%) and in MGS (26.2%). Net contributions of the five private PPFs continued to remain negative due to higher net withdrawals.

Insurance Companies

The performance of the insurance industry was adversely affected by the financial crisis. The combined premium income of the life and general insurance sectors contracted by 2.3% (1997: +14.4%) to RM10.9 billion in 1998, with more than half of the premium income (57.1%) being derived from life business. Total premium income as a percentage of nominal Gross National Product was 4.2% in 1998. The growth in assets of the industry's insurance funds moderated, registering an increase of 10.9% (1997: 13%) to RM38.7 billion. Total benefits and net claims paid out by the industry increased by 22.3% (1997: 28.2%) to RM4.5 billion, representing 41% (1997: 32.8%) of premium income.

After almost a decade of positive growth, the life insurance industry experienced a contraction in 1998 due to the economic slowdown. New business premiums recorded a decline of 10.2% (1997: +11.1%), while total new sums insured contracted by 2.8% in 1998 (1997: +18.2%). All categories of policies recorded negative growth in new premiums.

Given the prevailing economic difficulties, sums insured which were forfeited increased by 27.2% (1997: 17.5%) to RM15.4 billion in 1998. In consonance with this, total annual premiums terminated by forfeiture grew by 34.3% to RM0.5 billion. At the same time, total sums insured terminated through surrenders also increased by

49.1% to RM6 billion in 1998 (1997: 7.7%) due to the higher incidence of cashing out by policyholders.

With the slowdown in new business which led to the deterioration in termination, the growth of annual premiums in force and sums insured in force slowed down to 4.2% (1997: 13.3%) and 4.6% (1997: 13.9%) to RM6.2 billion and RM336.8 billion respectively in 1998. In terms of distribution of business in force, whole life policies remained the most dominant class of life insurance with a share of 36.4% of total sums insured in force, followed by temporary insurance which accounted for 33.6% of the total business in force.

Aggregate income of the life insurance industry recorded a slower growth of 4.3% (1997: 11.6%) to RM8 billion in 1998. The lower growth was mostly due to the decline in profits on sale of assets by 94.2% (1997: -33.2%) to RM17 million in 1998, reflecting the bearish stock market conditions in 1998. At the same time, the growth of premium income also slowed down significantly from 14.2% in 1997 to 4.2% in 1998. The net investment income grew by 19.4% (1997: 20.8%) to RM1.6 billion in 1998. In terms of investment yield, the net rate of interest of the insurance funds, excluding capital gains or losses, improved by 0.6 percentage points to 7.8% in 1998. However, the investment yield including capital losses deteriorated to only 3.1% (1997: 7%) due to losses on realisation of securities.

Total outgo of the industry declined by 15.9% (1997: +53.7%) to RM4.3 billion in 1998, mainly due to the reduction in acquisition costs which declined by 15.2% (1997: -0.9%) to RM1.3 billion, following the implementation of the operating cost guidelines. Significant write backs of provisions for diminution in value of investments and bad and doubtful debts in the second half of 1998 due to the recovery of the stock prices also contributed to the improvements shown in total industry outgo. Consequently, the excess of income over outgo of the industry grew by 44% (1997: -27.5%) to RM3.7 billion in 1998.

Total assets of life funds grew by 12.5% to RM26.2 billion as at end 1998. Corporate securities remained the largest component, accounting for 30.5% (1997: 29.4%) of total life funds, followed by cash and deposits with 22.4% (1997: 22.9%) of total assets. This reflected the more cautious

and liquid investment policies adopted by insurers due to the uncertain investment conditions. Meanwhile, policy loans continued to grow significantly by 32.2% (1997: 24.1%) to RM2.6 billion as more policy owners took advantage of premium loans provided by the insurers. The proportion of life fund assets invested in Government securities and Government guaranteed loans continued to decline in 1998 to account for 13.5% (1997: 15%) of total assets due to the lower statutory requirement on the holding of Government securities.

The growth of general business in 1998 was affected by the economic slowdown with written premiums declining by 10.6% to RM5.4 billion, compared with an increase of 7.1% in 1997. Despite slower premium growth, the net retention ratio improved slightly from 85% in 1997 to 85.8% in 1998. Increased domestic reinsurance capacity arising from higher capitalisation of a number of insurers as well as the role played by foreign professional reinsurers operating in the country led to a reduction in the outflow of premiums. Insurance premiums ceded overseas fell by 15.5% from RM912.6 million in 1997 to RM770.7 million in 1998. During the year, all sectors registered increases in claims, resulting in the overall claims ratio deteriorating to 62.6%, compared with 58% in 1997.

Reflecting the slower growth in premium income, total assets of general insurance funds grew at a slower rate of 7.7% to RM12.6 billion in 1998 (1997: 14.3%). Cash and deposits continued to be the largest component of the insurance fund assets in 1998, accounting for 42.3% share of total assets, followed by corporate securities, which totalled RM2.3 billion or a share of 18.6%.

During the first half of 1999, the combined premium income grew by 3.1% to RM5.3 billion, compared with an increase of 3.7% in the corresponding period in 1998. The growth was dampened by the continued decrease in net premium income of general business. The combined assets of both life and general insurance funds registered a higher growth of 15.8% (January-June 1998: 8.9%) to RM42.2 billion at the end of the first half of 1999.

The growth rate of premium income of life insurance business increased by 8.6% during the first half of 1999, compared with 12.8% in the

first half of 1998. Both new business premiums and new sums insured increased by 5.2% and 6.8% respectively during the same period. All categories of policies registered positive growth in new business premiums, except whole life with new business premiums contracting by 2.8%.

Total income of the life insurance industry recorded a higher growth of 20.7% (January-June 1998: 8.8%) to RM4.5 billion, while total outgo decreased by 15.2% (January-June 1998: +25.1%) to RM1.8 billion. The decrease in total outgo was caused by the reduction in loss on disposal of assets. The assets of life funds increased by 18.0% to reach RM28.7 billion at end-June 1999. Corporate securities continued to be the largest component of the life funds accounting for 36.1% of total funds.

During the first half of 1999, total written premiums of the general insurance sector further declined by 5.6% to RM2.6 billion (January-June 1998: decline of 8.2%). The total assets of the general insurance industry increased by 7.1% to RM13.5 billion at end-June 1999 (December 1998: RM12.6 billion).

As at end-September 1999, there were 68 insurers, comprising seven life insurers, 11 composite, 40 general insurers, nine general reinsurers and one life reinsurer. Of the total, 58 were Malaysian-incorporated and the remaining foreign incorporated. As at the same date, there were 37 licensed brokers and 42 licensed loss adjusters.

Takaful Business

The Malaysian takaful industry comprises two takaful operators namely, Syarikat Takaful Malaysia Berhad (STMB) and Takaful Nasional Sdn. Berhad (TNSB). Based on unaudited data for the financial year 1999, the takaful industry continued its growth momentum with the main business indicators recording double-digit growth rates. Combined assets of takaful funds and shareholders' funds increased by 41.1% to reach RM967.4 million at the end of the 1999 financial year compared with a growth of 21.2% in 1998, largely attributable to the favourable growth in the family takaful business. Assets of the family takaful funds accounted for 61.5% of the total assets, while general takaful funds accounted for another 23.2%

Table 8.9**Life and General Insurance Business**

	1998 ¹	1999 ²
Life Insurance (RM million)		
New Business:		
Number of policies ('000 units)	1,143.0	517.0
Sums insured	87,429.2	47,562.8
Total premiums	1,420.4	714.8
Business in force:		
Number of policies ('000 units)	6,289.3	6,448.3
Sums insured	336,795.7	34,041.4
Annual premiums	6,208.3	6,356.9
Premium Income	6,198.0	3,123.4
Benefit Payments		
Total	1,925.9	967.8
Maturity	529.4	248.7
Death & disability	661.5	324.4
Surrender	478.9	253.3
Cash bonuses	255.9	141.3
Annuity	0.2	0.1
General Insurance (RM million)		
Premium Income:		
Written Premium	5,429.7	2,615.2
Net Premium	4,659.0	2,222.0
Reinsurance Placed Outside Malaysia		
	770.7	393.2
Retention Ratio (%)	85.8	85.0
Number of Insurance Companies		
Direct:		
Life	7	7
General	40	40
Composite	11	11
Reinsurance:		
Life	1	1
General	9	9
Number of Takaful Operators	2	2

¹ As at calendar year end² As at 30 June 1999

Source: Bank Negara Malaysia

with the balance of 15.3% being assets of shareholders' funds. Investment in Malaysian Government Investment Certificates and Government guaranteed bonds amounted to RM144.1 million or 14.9% of total assets, while investment in Bank Islam Malaysia Berhad was RM30.4 million or 3.1 % of total assets.

New takaful business grew steadily in 1999 with a total of 88,286 new certificates sold under family takaful business, an increase of 57.3% with total participation of RM4,299.4 million. Total contributions received on new certificates increased by 23.6% to RM147.5 million in 1999. Business in force continued to expand in tandem with the steady pace of growth of new business in 1999 with the number of certificates in force increasing by 48.4% to reach 238,837 units (1998: 160,944). Total contributions and total participation in force rose by 48.8% and 41.6% to reach RM376.4 million and RM17,410.4 million respectively (1998: RM253 million and RM12,291.7 million respectively) at the end of the 1999 financial year.

General takaful business, comprising marine, motor, fire, group personal accident and engineering coverages continued to record a double-digit growth rate of 16.2% in gross contribution to RM142.5 million in 1999, after registering a strong growth rate of 33.1% in 1998. The lower growth could be attributed to the downturn in the economy. Total net claims paid during the year increased by 44.6% from RM17.5 million to RM25.2 million compared with a marginal increase of 8.7% in 1998. This was mainly due to an increase in claims from the motor sector and continuing bad claims experience in the mandatory group personal accident takaful scheme for students.

The strong growth of takaful business, contributed largely by the family takaful business was partly due to the expansion of the distribution network arising from the opening of more branch offices and takaful desks throughout the country to promote the sale of takaful products nationwide. As at 30 June 1999, there were 61 takaful desks and 52 takaful branch offices throughout the country compared to 59 and 36 respectively at end-June 1998. The sustained growth of takaful business over the past few years, despite the economic slowdown, reflects the increasing awareness of the general public about the benefits of takaful.

Table 8.10

Life and General Insurance Funds

	Life Insurance (RM million)			General Insurance (RM million)		
	1997	1998 ¹	1999 ²	1997	1998 ¹	1999 ²
Fixed assets	177.5	337.7	266.8	420.2	550.7	557.1
Loans	5,269.9	5,826.7	5,727.2	564.7	549.1	470.2
Government securities*	3,367.6	3,408.3	3,976.3	2,183.0	2,108.9	2,253.4
Government guaranteed loans	122.3	129.5	78.4	20.0	38.9	69.7
Corporate securities	6,854.6	7,997.1	10,360.5	1,985.0	2,337.8	2,617.1
Investment properties	1,127.3	1,302.0	1,523.7	166.2	208.4	332.1
Cash and deposits	5,334.4	5,864.3	5,528.2	4,768.4	5,311.8	5,614.0
Other assets	1,037.5	1,326.7	1,238.4	1,544.3	1,445.6	1,596.5
TOTAL	23,291.1	26,192.3	28,699.5	11,651.8	12,551.2	13,510.1

* Includes Treasury bills and government securities issued abroad.

¹ As at calendar year end.

² As at 30 June 1999.

Source: Bank Negara Malaysia

Capital Market

In the first eight months of 1999, net funds raised in the capital market were higher by 33.3% at RM2.8 billion (RM2.1 billion raised in the corresponding period of 1998). Higher net funds were raised by the public sector, consistent with the fiscal stimulus undertaken by the Government to revive the economy. The public sector raised RM3.2 billion in the first eight months of 1999, compared with a net redemption of RM546 million in the corresponding period of 1998. However, the private sector recorded a net redemption of RM436.8 million, as compared with RM2.6 billion raised in the corresponding period of 1998. This was largely due to a surge of 102.3% in the redemption of securities, amounting to RM8.7 billion (1998: RM4.3 billion). The importance of the capital market as a source of financing is reflected in the net funds raised of RM2.8 billion compared

with the decline in outstanding loans of the banking system of RM1 billion.

A total of RM9.4 billion was raised by the public sector through the issuance of MGS worth RM6.0 billion, Khazanah bonds valued at RM1.4 billion and Government Investment Issues worth RM2.0 billion. In the same period, total redemptions amounted to RM6.2 billion, involving RM4.2 billion redemption in MGS, RM2.0 billion in government investment issues and RM1.8 million in Malaysia Saving Bonds. MGS continued to account for the bulk (63.9%) of the gross issuance of debt instruments, followed by Government Investment Issues (21.3%) and Khazanah bonds (14.8%).

Despite the recovery in the equity market, the corporate sector was cautious in raising funds from new equity issues after the experience in 1998, when several initial public offers (IPOs)

Table 8.11**Family and General Takaful Business**

	<i>Financial Year 1997</i>	<i>Financial Year 1998</i>	<i>Financial Year 1999^u</i>
Assets ¹ (RM million)	565.7	685.4	967.4
Malaysian Investment Certificates	99.5	113.9	144.1
Investment in Bank Islam Malaysia Bhd.	76.1	11.9	30.4
Others ²	390.1	559.6	792.9
Family Takaful Business			
New Business:			
Total contribution (RM million)	79.2	119.3	147.5
Sums participated (RM million)	2,317.8	5,606.6	4,299.4
Number of certificates	50,005	56,126	88,286
Business in Force:			
Total contribution (RM million)	162.3	253.0	376.4
Sums participated (RM million)	7,892.2	12,291.7	17,410.4
Number of certificates	112,605	160,944	238,837
General Takaful Business			
Gross contributions (RM million)	92.1	122.6	142.5
Net claims paid (RM million)	16.1	17.5	25.2

^u Unaudited data¹ Assets of family takaful funds, general takaful funds and shareholders' funds² Includes shares, cash and other assets

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

PDS. Funds raised through PDS increased by 23.2% to RM6.9 billion (January – August 1998: RM5.6 billion). The increase was consistent with the prevailing low interest rates and inflation rate in the country. The low interest rate environment encouraged investors to seek higher yields through bonds, with AAA rated bonds carrying a yield of over 7.0% and over 10.0% for BBB rated bonds. In addition, the low inflation rate placed less pressure for interest rates to rise, which could lower the prices of bonds. The bulk of PDS was issued through Cagamas bonds (RM4.1 billion or 59.7% of total PDS), Islamic bonds (RM1 billion or 15.3%), straight bonds (RM660 million or 9.6%), convertible bonds (RM556 million or 8.1%) and bonds with warrants (RM500 million or 7.3%). After taking into account the redemption of maturing issues of PDS, valued at RM8.7 billion, the private sector recorded a net redemption of RM437 million in the first eight months of 1999.

During the first nine months of 1999, **Cagamas Berhad**, the national mortgage corporation, mobilised a total of RM19.7 billion, comprising RM15.6 billion notes from 18 issues and RM4.1 billion bonds from 11 issues. This represented a 25.5% increase from RM15.7 billion raised during the corresponding period in 1998, involving RM12.8 billion notes from 16 issues and RM2.9 billion bonds, including RM70 million Islamic bonds from 8 issues. A total of RM4.2 billion in housing loans was purchased by Cagamas during January – September 1999. A major proportion of housing loans (86.1%), valued at RM3.6 billion, was purchased from the financial institutions, with the remaining RM0.5 billion (12.3%) purchased from the Housing Loans Division of the Ministry of Finance and RM67 million (1.6%) from corporations.

The performance of Cagamas is expected to improve during 1999 in tandem with the recovery of the economy. The securitisation of housing loans and leases by financial institutions to Cagamas is envisaged to increase as the sales of residential property picks up.

The number of ratings completed on proposed bond issues increased significantly during the first eight months of 1999, following improved investor sentiments consistent with the recovery in economic activities and a return in stability in the financial market. Other factors contributing to the sharp increase in bond financing were the larger number of corporate debt restructuring exercises being

closed lower than their offer prices and were undersubscribed. Consequently, funds raised from IPOs were lower by 85.5% at RM95.5 million (January – August 1998: RM656.7 million). However, funds raised through rights issues rose significantly by 152.6% to RM1.0 billion (1998: RM424 million) to account for the bulk (75.2%) of funds raised in the equity market, followed by special issues valued at RM200.5 million (14.1%).

In tandem with the recovery of the economy and expectations of improved corporate performance, the private sector was able to mobilise higher gross funds from the issuance of

Table 8.12

Funds Raised in the Capital Market

	1998 Jan – Aug (RM million)	1999 ^p Jan – Aug (RM million)
By Public Sector		
Debt Securities	5,827.8	9,392.6
Malaysian Government Securities	4,500.0	6,000.0
Khazanah Bonds	1,327.8	1,392.6
Government Investment Issues	–	2,000.0
Less: Redemptions	6,374.0	6,151.8
Malaysian Government Securities	4,700.0	4,150.0
Government Investment Issues	750.0	2,000.0
Malaysia Saving Bonds	924.0	1.8
Net funds raised	-546.2	3,240.8
By Private Sector		
Shares ¹	1,398.0	1,423.3
Public issues	656.7	95.5
Rights issues	423.9	1,070.8
Special issues	–	200.5
Private placements	317.4	56.5
Debt Securities ² (gross)	5,582.3	6,870.8
Straight bonds	2,033.5	660.0
Convertible bonds	83.8	555.8
Islamic bonds	345.0	1,050.0
Bond with warrants	150.0	500.0
Cagamas bonds	2,970.0	4,105.0
Less: redemptions	4,325.2	8,730.9
Net issues of debt securities	1,257.1	-1,860.1
Net funds raised	2,665.1	-436.8
TOTAL	2,108.9	2,804.0

^p Preliminary data.

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

² Refers to securities with maturities of more than one year. Excludes debt securities issued by banking institutions.

Source: Bank Negara Malaysia

undertaken in the period, as well as the lower interest rate environment. Consequently, the number of new ratings completed by **Rating Agency Malaysia (RAM)** on proposed bond issues rose sharply to 26 proposed issues valued at RM28.0 billion during the first eight months of 1999, compared with 4 proposed issues valued at RM0.6 billion during the corresponding period in 1998. In addition to PDS rating, RAM also completed one claims paying ability rating and one senior debt rating. The bonds rated were from the infrastructure and utilities, industrial products, financial services, construction and engineering, diversified holdings, mining and petroleum, trading and services as well as the property and real estate sectors.

The second rating agency, the **Malaysian Rating Corporation (MARC)**, completed six ratings, comprising five corporate debts and one insurance rating, valued at RM4.38 billion during the first eight months of 1999 (January-August 1998: 9 ratings valued at RM0.9 billion). The bonds rated were from the construction, property, consumer credit and utilities sectors. Of the five corporate debts, four were Islamic private debt securities.

In terms of maturity profile of the proposed issues, there was a preference for medium to long-term papers as market participants sought to lock in the low cost of funding amid signs that interest rates may be bottoming out in line with the economic recovery. In terms of guarantee, only one of the bond issues was bank-guaranteed, while another issue was corporate guaranteed with a combined value of RM290 million.

The Kuala Lumpur Stock Exchange

The improved performance of the Kuala Lumpur Stock Exchange (KLSE) in the first nine months of 1999 reflected the growing confidence that investors had in the recovery and growth prospects of the Malaysian economy. Beginning the year on a softer note, a carry over from the bearish sentiments prevailing in 1998, the benchmark Kuala Lumpur Composite Index (KLCI) closed at 591.43 points at end-January 1999. In February, the KLCI declined to 542.23 points due to the selling pressure evoked on the days ahead of implementation of the graduated exit levy. The downward trend continued into March, with the KLCI closing at

502.82 points, influenced by expectations of poor 1998 corporate results, the Central Limit Order Book issue and anxieties associated with the outcome of the Sabah state elections.

However, the market made a turnaround in April, triggered by news of improved perceptions of Malaysia by foreign rating agencies. Standard and Poor's revised its rating on Malaysia from negative to stable for the nation's debt, while Morgan Stanley recommended an overweight on Malaysian assets. This was followed by Moody's upgrading of Malaysia's long-term foreign currency country ceiling from negative to stable, Fitch IBCA's restoration of Malaysia's investment grade from BB to BBB-. Meanwhile, the reduction of BNM's intervention rate from 7% to 6.5% on 5 April added more liquidity to the equity market. In addition, the release of improved economic indicators further strengthened market confidence. The Securities Commission's (SC) decision to allow the issuance and listing of new warrants to replace existing warrants, also led to increased participation by retail investors. The KLCI breached the 600-level to close at 674.96 points at end-April.

Bullish sentiments continued to prevail in May, with the KLCI crossing the 700 point psychological level to 743.04 points at end-May. The upward trend in the market was influenced by factors, which included a further reduction in BNM's intervention rate from 6.5% to 6% on 3 May, stock market rallies in regional bourses, a rise in the Dow Jones Industrial Average Index, success of the global bond issue by Malaysia, as well as renewed confidence in the sustainability of the country's economic recovery. The bullish trend continued into June, aided by factors such as growing investor confidence, lower interest rates and expectations of an early election, which spurred buying interest. This led the benchmark KLCI to breach the 800-level to close at 811.10 points at end-June.

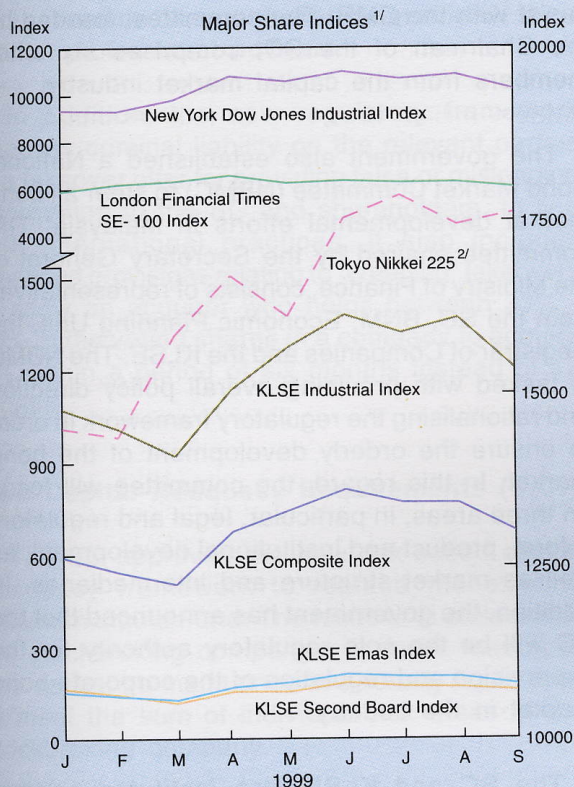
The uptrend in the KLSE, however, witnessed a reversal in the third quarter of 1999, beginning from the middle of July, due mainly to externally generated adverse factors. The factors included the decline in price indices of regional stock markets, concerns over the China-Taiwan political tension, fears of a possible increase in U.S. interest rates, concerns over the sustainability of the Japanese economic recovery due to the

strengthening of the yen, as well as the imposition of trading restrictions by selective stockbroking companies. Subsequently, the KLCI closed lower at 768.69 points at end-July. The downward trend continued into August. However, news on the proposed reinstatement of Malaysia into the Morgan Stanley Capital International indices from February 2000 saw the KLCI advance by 40.46 points and 43.92 points respectively to close at 728.96 points on 12 August and 772.88 points on 13 August. The market, however, could not sustain this surge due to fears of a massive withdrawal of foreign funds in September 1999 when the one-year moratorium on portfolio capital was lifted. Consequently, the market closed at 767.06 points at end-August.

The anticipated huge outflow of portfolio funds in early September was a non-event and the outflow was insignificant. Meanwhile, the replacement of the two-tier levy system with a flat 10% levy on the repatriation of profits on portfolio investment on 21 September saw the KLCI rising by 29.27 points or 4.1% to end at 739.30 points on the same day. However, market sentiments remained weak in September in tandem with regional market sentiments, concerns over the strengthening yen and its consequent impact on the Japanese economy, as well as nagging fears of the U.S. increasing its interest rates. Consequently, the market closed at 675.45 points at end-September. However, this level was still 80.8% higher compared to 373.52 points at end-September 1998. Similarly, market capitalisation was also higher by 83.7% at RM457.6 billion, compared with RM249.1 billion at end-September 1998. This was equivalent to 152.6% of GDP in 1999, compared to 87.6% of GDP in 1998. In terms of ranking of market capitalisation in US\$, the KLSE was in eighth position in the Asia-Pacific region and second in Asean as at end-August 1999.

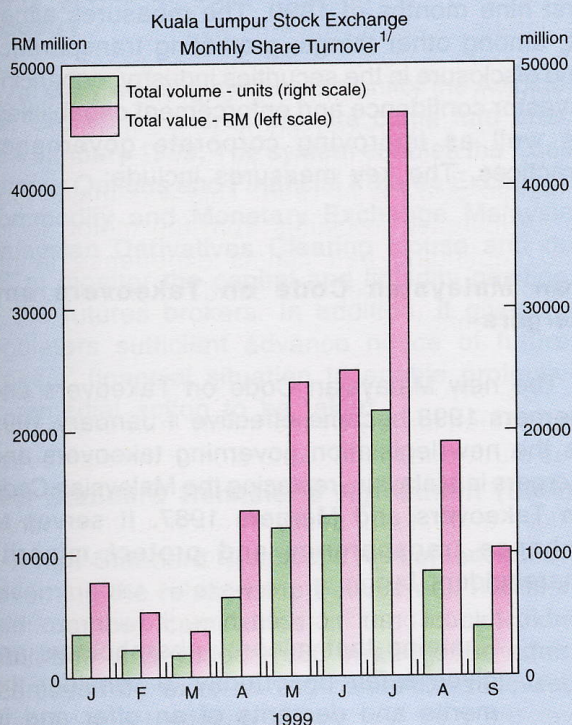
In October, the KLCI reversed its trend, aided by factors such as speculations of a pre-election rally, expectation of an increase in the number of anchor banks and the release of data on improved trade surplus and industrial production index for August, as well as the strong Wall Street performance following the decision to maintain interest rates. This led the KLCI to breach the 700-point level to finish at 721.18 points on 15 October 1999.

Chart 8.3
Share Markets



1/ End of period closing indices

2/ Right scale



1/ Refers to the Main Board and Second Board of the Kuala Lumpur Stock Exchange

In line with the improvement of the KLCI, trading volume on the KLSE was higher by 83.2% during the first nine months of 1999, amounting to 72.9 billion units (January - September 1998: 39.8 billion units). Average daily volume registered 394.2 million units during the same period in 1999 (January - September 1998: 247.0 million units). Underpinned by higher stock prices and the increase in volume traded, total turnover value was significantly higher by 83.4% at RM153.7 billion (January - September 1998: RM83.8 billion). In terms of sectoral performance, the leading sector was trading and services with 25.4% of total trading volume, followed by loans (16.6%) and the finance sector (12.9%). The Main Board accounted for 94.0% of total shares traded (January - September 1998: 91.0%), while the Second Board accounted for 6.0% (January - September 1998: 9.0%). Reflecting the higher trading volume, market liquidity as measured by the ratio of trading volume to the number of securities listed, increased to 44.4% during the first nine months of 1999, compared with 25.4% during the corresponding period in 1998.

In tandem with the recovery of the region in the aftermath of the financial crisis, other regional bourses also made positive gains in 1999. Up to end-September 1999 compared with end-September 1998, the KLCI registered an increase of 80.8%, against the gains made by the Jakarta composite index (98.4%), all-Singapore index (92.8%), the Philippine composite index (66.4%) and the Thailand index (53.5%). However, in East Asia, the Korea Composite Index performed better, registering a 169.5% gain.

During the first nine months of 1999, a total of 9 companies with a combined nominal capital of RM349 million were newly listed on the KLSE, compared with 26 companies with a combined nominal capital of RM1.3 billion during the corresponding period in 1998. With the new listings, the total number of companies listed on the KLSE was 745, with 461 companies listed on the Main Board and 284 companies on the Second Board at end-September 1999 (end-September 1998: 734 with 452 companies listed on the Main Board and 282 companies on the Second Board).

The year saw several key developments in relation to the capital market in Malaysia. In July 1999, the government approved the SC initiative to develop a Capital Market Master Plan (CMP)

Table 8.13**Kuala Lumpur Stock Exchange : Selected Indicators**

	<i>Jan–Sept 1998</i>	<i>Jan–Sept 1999</i>
Price Indices ¹		
Composite	373.52	675.45
Emas	99.34	174.81
Second Board	92.69	153.60
Total Turnover ²		
Volume (billion units)	39.77	72.93
Value (RM billion)	83.75	153.74
Average Daily Turnover ²		
Volume (billion units)	246.99	394.20
Value (RM million)	520.18	831.01
Market Capitalisation ¹ (RM billion)	249.13	457.55
Market Capitalisation ¹ /GDP (%)	87.6	152.6
Total No. of Companies Listed ¹	734	745
Main Board	452	461
Second Board	282	284
Market Liquidity ¹		
Turnover Value/Market Capitalisation	33.6	33.6
Turnover Volume/No. of Listed Securities (%)	25.4	44.4
Market Concentration ¹		
10 Most Highly Capitalised Stocks/Market Capitalisation (%)	32.0	33.0
Average Paid-up Capital of Stockbroking Firms ¹ (RM million)	82.61	84.82

¹ As at end of period² Market transactions only

Source: Kuala Lumpur Stock Exchange

to assist in the creation of a resilient and competitive capital market. Subsequently, a Capital Market Strategic Committee (CMSC) was appointed to assist with the CMP. The committee, headed by the Chairman of the SC, comprises six other members from the capital market industry.

The government also established a National Bond Market Committee (NBMC) to steer all bond market developmental efforts in Malaysia. The committee chaired by the Secretary General of the Ministry of Finance, consists of representatives from the SC, BNM, Economic Planning Unit, the Registrar of Companies and the KLSE. The NBMC is tasked with providing overall policy direction and rationalising the regulatory framework in order to ensure the orderly development of the bond market. In this regard, the committee will focus on three areas, in particular, legal and regulatory reform, product and institutional development, as well as market structure and intermediaries. In addition, the government has announced that the SC will be the sole regulatory authority for the supervision and regulation of the corporate bond market in the country.

The SC and KLSE also instituted several regulatory and legislative measures during the first nine months of 1999. The measures aimed at, among other things, promoting transparency and disclosure in the securities industry, enhancing investor confidence and enforcement capabilities, as well as improving corporate governance practices. The key measures include:

New Malaysian Code on Takeovers and Mergers

The new Malaysian Code on Takeovers and Mergers 1998 became effective 1 January 1999 as the new legislation governing takeovers and mergers in Malaysia, replacing the Malaysian Code on Takeovers and Mergers 1987. It serves to enhance transparency and protect minority shareholders by:

- Ensuring that minority shareholders are given a fair opportunity to consider the merits and demerits of an offer and to enable them to decide whether they should retain or dispose of their shares; and

to prioritise immediate needs of the Malaysian capital market and to chart its future direction and long-term growth. Amongst other things, the CMP aims to address weaknesses in the capital market which were highlighted during the crisis, provide a strategic road map for the industry to facilitate future business development, as well as

- Requiring offer documents, board of directors' circulars and independent advice circulars to include all relevant information required by shareholders and their professional advisers.

In addition, the new regulatory framework imposes criminal liability on the relevant parties in a takeover offer for providing false or misleading information to the SC and shareholders. In line with international practices, it also includes amended provisions relating to "creeping" takeovers to allow an acquirer who holds between 33% - 50% of the voting shares in a company to acquire 2% within a period of six months instead of 12 months.

New Capital Adequacy Requirements (CAR)

The SC approved the new risk-based capital adequacy framework to replace the existing Minimum Liquid Fund. The focus is to ensure that the stockbroking company's financial resources and capital be maintained in a readily liquid form to meet the sum of individual risk areas of the stockbroking company.

Early Warning System for the Derivatives Industry

An early warning system to monitor the Adjusted Net Capital of futures brokers came into effect on 4 January 1999. The system enables the Kuala Lumpur Options and Financial Futures Exchange, Commodity and Monetary Exchange Malaysia, Malaysian Derivatives Clearing House and the SC to monitor the capital and liquidity positions of the futures brokers. In addition, it gives the regulators sufficient advance notice of futures brokers' financial situation to enable protective or remedial action to be taken.

New Standard Remisier's Agreement (SRA)

A new Standard Remisier's Agreement (SRA), governing the relationship between all remisiers and member companies in the stockbroking industry, was introduced. Among the areas addressed by the new SRA were the following:

- The remisier shall now be regarded as an agent of the stockbroking company to trade

securities in the name of the company. This was not made explicit in previous arrangements; and

- Remisiers' security deposit in the form of cash must be placed in trust accounts with banks licensed under the Banking and Financial Institutions Act 1984 or Islamic Banking Act 1983;
- Explicit clauses were introduced to ensure the rights of both remisiers and the stockbroking company; and
- Remisiers may take home their commission earned, RM1,000 and below, subject to other charges, expenses and levies incurred.

Quarterly Reporting of Financial Statements by Public Listed Companies and Limits on Directorships

Compulsory quarterly reporting of financial statements and limits on the number of directorships were implemented, aimed at enhancing corporate disclosure and governance respectively. Public listed companies (PLCs) are now required to file financial statements, comprising income statement, balance sheet and explanatory notes on a quarterly basis, with KLSE for public release, and to issue their audited annual accounts within 4 months from the end of a financial year. The move is to make available timely, adequate and accurate information to aid investors in making informed decisions, thereby reducing investment risk for investors, as well as increasing accountability of PLCs.

In addition, directors of PLCs are now barred from holding more than 10 directorships in PLCs and more than 15 directorships in non-listed companies. This will enhance corporate governance by enabling directors of PLCs to focus more time and energy on a smaller number of companies. It will also minimise and eliminate the practice of directors sitting on numerous boards of PLCs merely to lend their name and reputation to the PLC without the accountability of effective involvement in the PLC.

Report on Corporate Governance

The Finance Committee on Corporate Governance released its Report on Corporate

Governance in March 1999. The report included recommendations to:

- Strengthen the statutory and regulatory framework for good governance;
- Enhance the self-regulatory mechanisms that promote good governance; and
- Identify training and education programmes to ensure that the framework recommended is supported by the necessary human and institutional capital.

An Implementation Project Team, comprising members from the SC, the Registrar of Companies, KLSE and the Federation of Public Listed Companies, was established on 29 January 1999 to lead and oversee the implementation of the recommendations of the Report.

Revised “Policies and Guidelines on Issue/ Offer of Securities” (Issues Guidelines) and Flexibility in the Issue of Replacement Warrants

A number of requirements in regard to listing, reverse takeovers and backdoor listings were raised in order to increase the free float and liquidity of listed companies, aimed at ensuring that listing standards remain appropriate and competitive, as well as to enhance the confidence of investors. Some of the major changes include the following:

- Increasing the minimum issued and paid-up capital of companies seeking listing on the Second Board and the Main Board and removing the maximum limit imposed on those seeking listing on the Second Board;
- Tightening the profit track requirements for companies seeking listing on both the Main Board and the Second Board, for both initial public offerings and reverse takeovers/backdoor listings;
- Removing the requirement that future profits should reflect an increasing trend and replacing it with a new requirement. Companies applying for listing, whether on the Main Board or Second Board, should, subsequent to listing, be in a position to sustain their earnings at a reasonable level commensurate with their enlarged share capital base;

- Tightening the criteria for listings of property development companies only on the Main Board, in terms of profit records and assets; and
- Allowing the listing of construction and trading/retailing companies only on the Main Board, subject to strict criteria.

In addition, the SC also allowed companies listed on the KLSE to issue and list new equity warrants to replace the existing equity warrants issued by such companies as many warrants listed on the KLSE were rendered ‘out-of-the-money’ by the economic downturn.

KLSE Compensation Fund

The compensation fund now stands at RM20 million and will be further expanded with contributions from the SC and KLSE. In addition, member companies of KLSE are required to increase their annual contributions into the fund from RM10,000 to RM50,000 in 1999, and from RM50,000 to RM100,000 thereafter. The fund was expanded to ensure that investors’ assets were protected, in light of the financial difficulties faced by the stockbroking industry recently, and also to minimise systemic risk arising from a potential “run” on a stockbroking company.

Creation of SCANS Standby Facility

A standby facility of RM500 million was established for SCANS, the stock exchange’s clearing house, to be used in the event that KLSE member companies vis-à-vis clearing members of SCANS are unable to meet their obligations to the clearing house in respect of their settlement obligations.

Enhancement of Transparency and Accountability

Rule 16A of the KLSE Rules Relating To Member Companies became effective 1 July 1999. It imposes minimum standards for the ‘treatment of interest on non-performing accounts and standardised provisions for bad and doubtful debts in stockbroking companies’ financial statements. The purpose is to increase transparency in the

treatment of stockbroking companies' accounts, thus enhancing the accountability of stockbroking companies towards prudent management of their business. In light of the new rule, the Ministry of Finance has approved tax relief for stockbroking companies during 1999 and 2000 on a proportion of interest income until it is collected. In addition, stockbroking companies have also been given a transition period for full compliance with Rule 16A.

Institutional Settlement Services (ISS)

The ISS was launched by the KLSE on 15 July 1999 via the Exchange's clearing house, SCANS for the settlement of all on-market institutional trades. With the ISS, delivery-versus-payment, to the extent that there is same-day movement of funds and securities, will be achieved for all trades on the KLSE. The key feature of ISS, which is an optional service, is that membership in SCANS is now extended to non-broker institutions, including custodian banks, benefiting amongst others, foreign institutional clients who trade in Malaysian securities, while facilitating increased institutional participation in the KLSE.

Amendments to Listing Requirements and New Practice Notes

The new **Policy on Suspension** is aimed at ensuring continuous trading of listed securities and proper functioning of the market and addressing the following:

- Any listed company requesting a suspension must substantiate and justify its request; and
- The period of suspension ranges from one market day up to a maximum of three market days.

Sponsorship of **American Depositary Receipts (ADRs)** or **Global Depositary Receipts (GDRs)**

Sponsorship of ADR or GDR programmes by listed companies is allowed subject to certain conditions. This is aimed at enhancing foreign interest in Malaysian securities.

Flexibilities for Variations to Profit Guarantee

The SC allowed flexibility for variations to profit guarantee agreements after reviewing requirements

on variations to profit guarantees. These flexibilities relate to applications submitted after the close of the financial year and applications involving the variation of the first year's profit guarantee obligation. Such applications are now allowed if the guarantors can demonstrate that they do not have the financial capability to fulfil the profit guarantee obligation.

Measures were also concurrently introduced to ensure that investors' interests are upheld in light of these flexibilities being allowed. In this respect, guarantors who opt to vary the tenure of the profit guarantee period or the guaranteed sum must provide a security margin equivalent to at least 120% of the original guaranteed annual maintainable profit as stated in the prospectus of the company.

Securities Industry (Compliance with Approved Accounting Standards) Regulations 1999

The Securities Industry (Compliance with Approved Accounting Standards) Regulations 1999 became effective June 1999, empowering the SC to ensure that the quality of information disclosed by listed companies in financial statements is of a high standard and strictly comply with the accounting standards issued by the Malaysian Accounting Standards Board.

The **Malaysian Exchange of Securities Dealing and Automated Quotation (MESDAQ)** which was established in October 1997 started trading on 30 April 1999. As at end-August 1999, only one company, Supercomal Technologies Bhd. was listed on MESDAQ. However, another four companies are expected to be listed on the exchange in the fourth quarter of 1999. In terms of membership, the exchange has 13 members, 3 advisers, 5 sponsors and 7 market movers as well as 1,989 registered dealers representatives. Trading volume amounted to 3.9 million units valued at RM12.8 million as at end-August 1999. Several measures continued to be taken by MESDAQ to promote its exchange, including organising roadshows, seminars, presentations and dialogues, as well as publicity through interviews, the mass media and its web page. MESDAQ has also published a book "Going Public on MESDAQ" as a guide for companies seeking listing on the exchange, as well as brochures for investors.

Trading of the Kuala Lumpur Stock Exchange Composite Index Futures (FKLI) on the **Kuala Lumpur Options and Financial Futures Exchange (KLOFFE)** declined by 47.1% to 371,147 contracts during the first nine months of 1999 (January - September 1998: 701,267 contracts). Similarly, average daily turnover contracted by 47.9% to 2,006 contracts (January - September 1998: 3,853 contracts), while the month end open interest declined by 79.7% to 2,903 contracts (January - August 1998: 14,293 contracts). The Derivative Liquidity Ratio, which measures the value of futures contracts traded against the total value of the 100 underlying component stocks, also declined by 64.6% in August 1999. The decline in the performance of the FKLI contracts was due mainly to the lack of foreign and domestic participation. Foreign institutions, which contributed 47% of market share during 1998, declined to 11% of market share during the first four months of 1999.

However, monthly volume during the first nine months of 1999 has recovered to a monthly average of 41,238 contracts from a low of 16,893 contracts in October 1998. During the period under review, the trading volume of FKLI was highest in May with 58,378 contracts and a daily average volume of 2,780 contracts. At end-September 1999, KLOFFE had 59 local members, 40 trading members, of which 28 are licensed, as well as 632 futures broker representatives.

A significant development which affected KLOFFE was its acquisition by the KLSE in January 1999, paving the way for greater consolidation in the areas of business development and system requirements between the two exchanges, as well as enhancing investor confidence in the Malaysian financial market. Efforts undertaken by KLOFFE to promote the exchange include holding roundtable discussions with foreign and local investors, organising seminars to educate investors on the futures market, as well as increasing publicity on KLOFFE's activities through the mass media.

The trading volume of the 3-month Kuala Lumpur Interbank Offered Rate (KLIBOR) futures contracts on the **Commodity and Monetary Exchange Malaysia (COMMEMEX)**, the merged entity between the Malaysian Monetary Exchange and the Kuala Lumpur Commodity Exchange, declined by 9.2%

to 19,827 contracts in the first nine months of 1999 (January - September 1998: 21,824 contracts). The lower trading volume was mainly attributable to the lack of foreign participation.

However, open positions at end-September 1999 were 5,660 contracts, compared with 2,459 contracts at end-September 1998. The 130.2% increase in the open positions was due to active but sporadic hedging activities by over-the-counter (OTC) providers, such as Commerce International Merchant Bankers, BSN Commercial Bank, Arab Malaysian Merchant Bankers and Standard Chartered Bank Malaysia. The pegging of the ringgit also resulted in KLIBOR being the reference rate for interest rate swap prices rather than the foreign exchange swap. As such, swap providers preferred the 3-month KLIBOR futures contract as the hedging instrument to hedge their swap books. As at end-September 1999, COMMEMEX had registered 8 general broker members, 7 financial broker members, 10 financial non-broker members and 47 locals as trade members for the 3-month KLIBOR futures market.

In regard to trading in crude palm oil (CPO) futures, 7.65 million tonnes or 306,121 lots of CPO futures were traded during the first nine months of 1999. This represented an increase of 3.7% over the same period in 1998 (295,133 lots). On average 1,664 lots daily were traded (January - September 1998: 1,615 lots). Meanwhile, total open positions improved from 4,906 lots in January 1999 to 7,167 lots in September 1999, representing a significant increase of 41.6%. Palm oil prices have been on a downward trend since the beginning of 1999. While it has been traded at a premium vis-à-vis its major competitors such as soyabean oil over an unusually long period of 15 months since March 1998, palm oil prices have recently softened and are now traded at a discount to soyabean oil. This price development can be attributed to the significantly higher palm oil production and export availability in South East Asia. Among major palm oil producers, Malaysia's production has recovered more rapidly than expected from the preceding drought stress. As at end-September 1999, COMMEMEX had registered 13 broker members and 36 non-broker commodity members for the CPO futures market.

Table 8.14

Unit Trust Industry: Selected Indicators

	1998 ¹			1999 (End of August)		
	Government Supported Funds	Private Funds	Total	Government Supported Funds	Private Funds	Total
Number of Unit Trust Management Companies	10	22	32	10	22	32
Number of Unit Trust Funds ²	28	61	89	29	69	98
Units in Distribution (billion)	35.512	11.026	46.538	34.167	13.999	48.166
Number of Accounts (million)	7.745	0.843	8.588	7.865	0.930	8.812
Net Asset Value (NAV) (RM billion)	32.325	6.403	38.728	30.433	9.602	39.775
NAV/KLSE Market Value (%)	8.63	1.71	10.34	5.90	1.87	7.74

¹ End of period² Refers to funds already launched.

Source: Securities Commission

In line with the recovery of the equity market, the **unit trust industry** continued to expand in 1999 with the launching of nine new unit trust funds in the first eight months of 1999, (also nine for the whole of 1998), bringing the total number of unit trusts in operation to 98, with 69 private and 29 government supported funds. Units in circulation rose by 1.63 billion units to 48.17 billion

units at end-August 1999 from 46.54 billion units at end-1998. Net asset value (NAV) of the unit trust industry grew by 2.8% to RM39.8 billion at end-August 1999 from RM38.7 billion at end-1998 (end-1997: RM33.6 billion). However, the ratio of the industry's NAV to the market capitalisation of the KLSE declined from 10.3% at end-1998 to 7.7% at end-August 1999.