

MONETARY AND FINANCIAL DEVELOPMENTS

Overview

Monetary policy and financial conditions continue to support growth...

Monetary policy in 2006 continues to emphasise economic growth with price stability. With the economy on track to register steady growth on the back of strong domestic demand and favourable external conditions, the main challenge for monetary policy is the management of inflation. On the international front, inflationary pressures remain a concern due to persistently high crude oil prices. Similarly, domestic inflation has increased following the adjustment in retail prices of petroleum and electricity tariffs, arising from higher global energy prices.

The overnight policy rate (OPR) was raised twice during the first half of 2006 to align monetary conditions to the current economic environment. Notwithstanding the increase, the OPR remains below the neutral level, reflecting a supportive monetary stance. The rise in interest rates has been gradual and from historically low levels. The current interest rates continue to support economic activity and growth, reflected by the steady growth in bank lending, especially to the small and medium enterprises (SMEs) and households.

The shift in the ringgit exchange rate regime to a managed float since 21 July 2005 has been positive for the economy, as it enables Malaysia to respond better to structural changes in the regional and international environment. To date, the ringgit has strengthened against the greenback, supported by Malaysia's strong trade performance, sustained capital flows and positive growth prospects.

The financial landscape has been progressively transformed following the rationalisation of existing institutions as well as the introduction of new institutions and foreign competition. The consolidation of finance companies and commercial banks into single entities was successfully completed by January 2006, resulting in enhanced efficiency, capacity and capability to meet the increasingly sophisticated demands of consumers. The current mergers of merchant banks, stockbroking companies and discount houses will see the emergence of investment banks by year-end. The financial system is also witnessing greater regional and international integration, following the approval of three foreign Islamic financial institutions in Malaysia, of which one has commenced operations. In addition, increased foreign participation of up to 49% is allowed in Islamic subsidiaries, *takaful* operators and investment banks. Flexibility has also been given to the

locally incorporated foreign banking institutions (LIFBs) to establish an additional four branches. Meanwhile, Malaysian financial institutions have also increased market penetration in some regional and international markets.

Malaysia is also an internationally recognised Islamic capital market, being among the world's most active issuers of Islamic bonds as well as its success in attracting supranational agencies to raise syariah-compliant ringgit-denominated bonds in the domestic capital market. Recent initiatives to enhance Malaysia as an international Islamic finance centre include the establishment of the International Centre for Education in Islamic Finance (INCEIF) in March 2006 to develop human capital in Islamic finance. New financial instruments continue to be introduced as part of ongoing efforts to broaden and deepen the Islamic capital market.

The capital market remains an important source of funding for economic activities, amounting to RM1,161 billion as at end-June 2006, of which the debt market accounted for RM439 billion or 80% of Gross Domestic Product (GDP) and the equity market RM722 billion or 131.7% of GDP. Measures continue to be taken towards building an efficient, resilient, dynamic and competitive capital market to support the economy, particularly through the Capital Market Masterplan (CMP).

Recent initiatives to further develop the capital market include allowing foreign firms to be listed on Bursa Malaysia and Main Board Malaysian companies to seek secondary listings abroad. Single stock futures (SSF) was launched in April this year to provide an additional risk management tool for investors. The introduction of the new FTSE Bursa Malaysia Index Series in June 2006 is expected to raise the visibility of the Malaysian capital market among both local and global investors. There has also been enhanced competition and international integration in the domestic capital market, with the presence of five foreign stockbrokers and one foreign fund manager in Malaysia since the end of 2005.

Monetary Policy

Monetary policy remains supportive of growth...

Monetary policy in 2006 continues to emphasise economic growth in an environment of price stability. Growth prospects for the economy remain bright supported by strong domestic demand and a favourable external sector. However, inflationary pressures remain arising from the increased costs on transport and food, following the adjustment on retail fuel prices in February 2006. The Consumer Price Index (CPI) rose by 4.8% in March 2006, following the 30 sen per litre increase in petrol pump prices on 28 February, marking the highest inflation level in seven years. However the CPI has since moderated to average 3.9% during the first seven months of 2006 (January-July 2005: 2.8%). Against the background of sustained domestic growth prospects amidst higher inflation, the key policy interest rate was raised twice to align interest rates with the current economic conditions. The OPR was increased by 25 basis points (bps) from 3.00% to 3.25% on 22 February 2006 and by another 25 bps to 3.50% on 26 April 2006. Notwithstanding the increase, the monetary stance remains supportive of economic activity and growth, with the OPR at below the neutral level.

On the international front, there has been bias towards tightening of monetary stance to mitigate inflationary pressures from persistent high and volatile crude oil prices, as shown in *Table 5.1*. The United States (US) raised interest rate four times in the first six months of 2006, bringing the federal funds rate from 4.25% to 5.25%. The interest rate hike in June 2006 marked the 17th consecutive increase of 25 bps since June 2004. With the latest upward adjustment, the nominal interest rate differential vis-à-vis Malaysia's policy interest rate has widened to 175 bps in favour of the US. Japan removed its policy of quantitative easing in March this year and raised its overnight call rate to 0.25% in July, the first increase in six years. The European Central Bank (ECB) has thrice raised

TABLE 5.1

Key Interest Rates of Selected Countries

Country	End-2005 (%)	15 Aug 2006 (%)	Change (basis points)	Effective Date
Australia (Cash rate target)	5.50	5.75	+25	3 May 2006
		6.00	+25	2 Aug 2006
Euro area (Refinancing rate)	2.25	2.50	+25	8 Mar 2006
		2.75	+25	8 June 2006
		3.00	+25	3 Aug 2006
Japan (Official discount rate)	0.00	0.25	+25	14 July 2006
UK (Repo rate)	4.50	4.75	+25	3 Aug 2006
US (Federal funds rate)	4.25	4.50	+25	31 Jan 2006
		4.75	+25	27 Mar 2006
		5.00	+25	11 May 2006
		5.25	+25	30 June 2006
China (Lending rate)	5.58	5.85	+27	27 Apr 2006
		6.12	+27	18 Aug 2006
Indonesia (1-month discount rate)	12.75	12.50	-25	9 May 2006
		12.25	-25	6 July 2006
		11.75	-50	8 Aug 2006
Republic of Korea (Key rate)	3.75	4.00	+25	9 Feb 2006
		4.25	+25	8 June 2006
		4.50	+25	9 Aug 2006
Philippines (Overnight call rate)	7.50	7.50	0	20 Oct 2005
Malaysia (Overnight policy rate)	3.00	3.25	+25	22 Feb 2006
		3.50	+25	26 Apr 2006
Thailand (14-day repurchase rate)	4.00	4.25	+25	18 Jan 2006
		4.50	+25	8 Mar 2006
		4.75	+25	10 Apr 2006
		5.00	+25	7 June 2006

Source: Central Banks and Bloomberg.

its refinancing rate by 25 bps, bringing it from 2.25% to 3.00% in August 2006. Similarly, regional economies including the Republic of Korea, Thailand, China and India have also raised key interest rates to curb inflationary pressures.

The transition to the managed float exchange rate regime since 21 July 2005 has been orderly and positive for the economy. Under the present regime, the exchange rate of the ringgit is determined by market conditions and economic fundamentals. More importantly, the managed float regime enables Malaysia to respond better to structural changes in the regional and international environment. The primary objective of the exchange rate policy remains focussed on promoting stability, important for the open and trade-reliant Malaysian economy.

Monetary Developments

Sustained expansion of money supply and private sector financing...

Monetary aggregates expanded moderately in line with sustained economic expansion during the first half of 2006. **Narrow money or M1** grew by 10.1% in June 2006 (end-2005: 8.5%), reflecting steady demand for transaction balances from households and businesses, as shown in *Chart 5.1*. **Broad money or M3** rose by 6.4% in June 2006 (end-2005: 8%). The more moderate expansion of money supply was due to the slower increase in net external operations, while claims on the private sector remained expansionary, as shown in *Table 5.2*. However, this was partly offset by lower net claims on the Government.

TABLE 5.2

Determinants of M3 January-June

	Change (RM million)	
	2005	2006
M3	34,633.6	26,536.6
Net claims on Government	-13,755.3	-8,026.9
Claims on private sector	15,382.6	19,433.0
Loans	20,631.9	19,133.6
Securities	-5,249.3	299.4
Net external operations	31,290.5	24,653.2
Bank Negara Malaysia	32,476.2	24,010.6
Banking system	-1,185.7	642.6
Other influences	1,715.8	-9,522.7

M1: Currency in circulation + Demand deposits

M2: M1 + Narrow quasi-money

M3: M2 + Deposits placed with other banking institutions

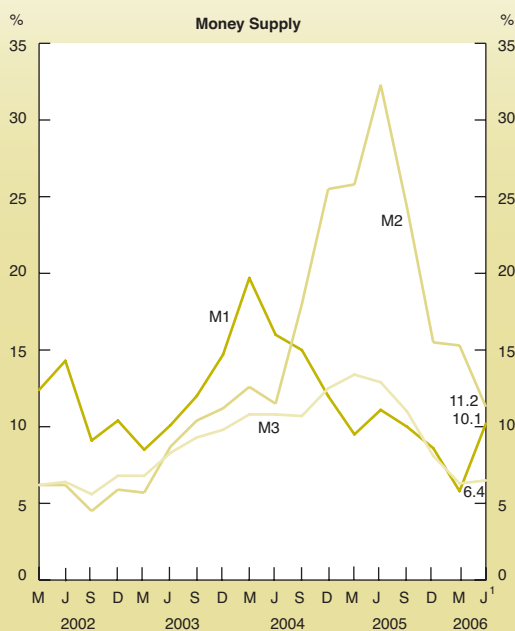
Source: Bank Negara Malaysia.

Interest rates of the banking system rose in tandem with the adjustment in the OPR. The base lending rate (BLR) of commercial banks increased to 6.34% at end-February 2006 (end-2005: 6.20%) following the hike in the OPR on 22 February. The BLR edged up to 6.72% at end-May 2006, following the second increase in the OPR on 26 April and remained unchanged at end-June 2006, as shown in *Table 5.3*. Similarly, the average lending rate of commercial banks was also adjusted upwards. However, the adjustment in interest rates on savings deposits and 1 to 12-month fixed deposits was less than the adjustment on lending rates. Due to the higher inflation rate, the real return on deposits remained negative.

Gross private sector financing through loan disbursements of the banking system as well as private debt securities (PDS) and equity raised in the capital market increased, albeit more moderately, by 2.5% to RM279.7 billion

CHART 5.1

Monetary Aggregates (annual change)

¹ As at end-June 2006.

Source: Bank Negara Malaysia.

TABLE 5.3

Interest Rates of Commercial Banks

	Interest Rates (%)			
	End-1998	End-2005	End-June 2006	Change End-June 2006 vs End-2005
Base lending rate	8.04	6.20	6.72	0.52
Average lending rate	9.72	6.12	6.55	0.43
Savings deposit	3.87	1.41	1.47	0.06
Fixed deposit				
1-month	5.82	3.01	3.11	0.10
3-month	5.83	3.02	3.18	0.16
6-month	5.76	3.04	3.32	0.28
9-month	5.74	3.08	3.45	0.37
12-month	5.74	3.70	3.75	0.05

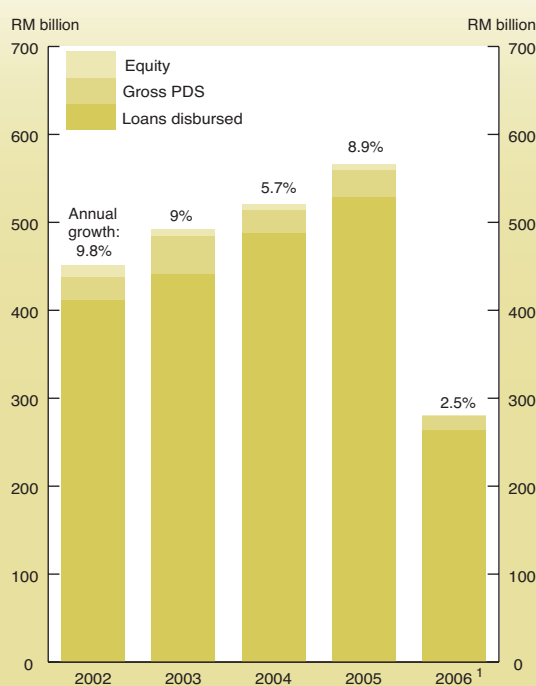
Source: Bank Negara Malaysia.

in the first six months of 2006 (January-June 2005: 10.6%; RM272.7 billion), as shown in *Chart 5.2*. Loan disbursements of the banking system grew moderately by 3.1% to RM264.2 billion (January-June 2005: 9.1%; RM256.2 billion), as shown in *Table 5.4*. This was, however, partly offset by the strong increase in PDS raised by the corporate sector. Total PDS expanded by 29.5% to RM15.7 billion during the first six months of 2006 (January-June 2005: 30.4%; RM12.1 billion). Over the years, the corporate sector has increasingly turned to the PDS market for funding. Total PDS outstanding stood at RM220 billion and accounted for 40.1% of GDP at end-June 2006 compared to 16.5% at end-1998.

Loan applications of the banking system, however, decreased by 4.6% to RM142.4 billion during the first six months of 2006 (January-June 2005: 15.7%; RM149.3 billion), mainly due to

CHART 5.2

Gross Private Sector Financing Through Banking System Loans and Capital Market



¹ As at end-June 2006.

Source: Bank Negara Malaysia.

TABLE 5.4

Banking System: Loan Indicators January-June

Indicators	RM billion		Annual growth (%)	
	2005	2006	2005	2006
Total				
Loan applications	149.3	142.4	15.7	-4.6
Loan approvals	90.2	94.0	7.7	4.3
Loan disbursements	256.2	264.2	9.1	3.1
Loans outstanding ¹	533.6	579.3	8.3	8.6
of which:				
Business sector				
Loan applications	78.7	68.8	15.0	-12.6
Loan approvals	41.8	41.7	2.5	-0.2
Loan disbursements ²	86.9	101.4	11.1	16.6
Loans outstanding ¹	221.6	230.7	2.8	4.1
SMEs				
Loan applications	29.5	29.0	17.7	-1.8
Loan approvals	17.2	17.4	21.4	1.5
Loan disbursements	53.0	65.6	124.1	23.6
Loans outstanding ¹	91.4	102.4	9.1	12.0
Households				
Loan applications	68.4	68.4	15.0	0.0
Loan approvals	47.4	46.2	12.6	-2.5
Loan disbursements ²	69.5	72.3	11.7	3.9
Loans outstanding ¹	282.4	320.0	14.6	13.3

¹ End period.

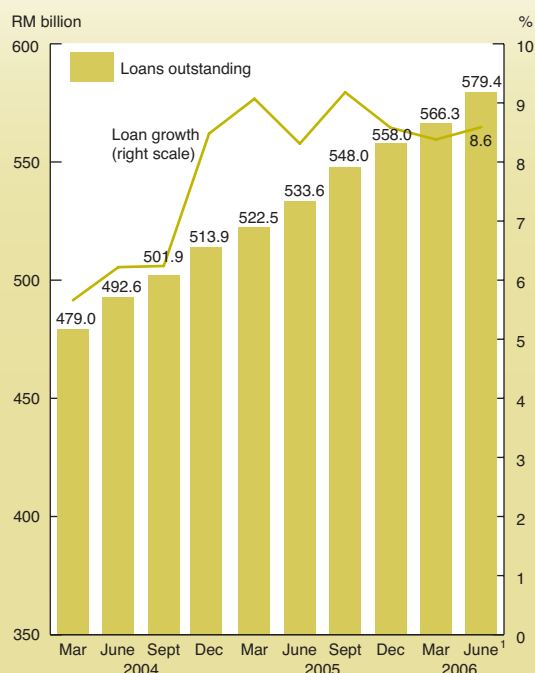
² Data for April till June 2006 is subject to revision, arising from change in lending indicators classification.

Source: Bank Negara Malaysia.

the decline in loan demand from the business sector. Household demand for financing remained resilient with loan applications maintained at the previous year's level. Nonetheless, growth in loans outstanding of the banking system was sustained at 8.6% at end-June 2006 (end-2005: 8.6%), as shown in *Chart 5.3* and *Table 5.5*. Loan disbursements to businesses continued to be mainly channelled to the manufacturing sector, totalling RM59.9 billion or 22.7% of total loan disbursements, followed by the wholesale and retail trade, hotels and restaurants sector (RM47.4 billion; 17.9%) and the finance, insurance and business services (RM20.3 billion; 7.7%), as shown in *Chart 5.4*.

CHART 5.3

Banking System: Loans Outstanding and Growth



¹ As at end-June 2006.

Source: Bank Negara Malaysia.

Ongoing efforts continue to be taken to strengthen the development of SMEs, in line with the objective to enhance their contribution to the economy. Recent initiatives to further improve SME access to financing include the introduction of new trade financing products, the establishment of an SME portal to provide comprehensive information on access to financing, as well as an increase in allocation of RM2.5 billion to two specialised funds.

The banking system also continues to support the financing needs of SMEs, with lending to SMEs continuing to drive loan growth to the business sector. Loans outstanding to SMEs increased by 12% to RM102.4 billion at end-June 2006 (end-2005: 8.7%; RM96 billion). Loans outstanding to SMEs were mainly extended to the wholesale and retail trade, hotels and restaurants, accounting for 27.4% of total outstanding loans, manufacturing (23.7%) and construction (14.1%) sectors.

Bank lending to the household sector remained firm, supported by favourable financing conditions, rising incomes and a stable labour market.

TABLE 5.5

Banking System: Direction of Lending¹

Sectors	Amount (RM million)		%	
	December 2005	End-June 2006	Annual Growth	Share End-June 2005
Agriculture, hunting, forestry and fishing	10,978.9	12,038.4	7.8	2.1
Mining and quarrying	810.5	1,410.4	55.8	0.2
Manufacturing	60,731.9	66,165.3	5.5	11.4
Electricity, gas and water	4,628.8	5,339.9	6.1	0.9
Wholesale and retail trade, hotels and restaurants	47,041.9	49,631.9	9.0	8.6
Broad property sector	228,959.4	241,692.4	11.0	41.7
Construction	29,991.9	31,560.5	4.7	5.4
Residential property	149,198.5	156,000.6	10.8	26.9
Non-residential property	35,123.3	37,097.6	13.4	6.4
Real estate	14,645.8	17,033.7	20.6	2.9
Transport, storage and communication	11,356.4	10,826.9	10.7	1.9
Finance, insurance and business services	30,143.5	36,720.4	19.8	6.3
Consumption credit, of which:	123,365.9	127,214.8	13.8	22.0
Credit cards	16,692.9	17,318.5	15.3	3.0
Purchase of passenger cars	86,481.0	90,249.8	15.2	15.6
Purchase of securities	20,904.4	19,646.5	1.3	3.4
Purchase of transport vehicles	2,855.6	2,124.2	-16.6	0.4
Community, social and personal services	5,726.9	4,496.9	-25.4	0.8
Others	10,561.6	2,040.6	-80.5	0.4
Total loans outstanding²	558,065.6	579,348.7	8.6	100.0

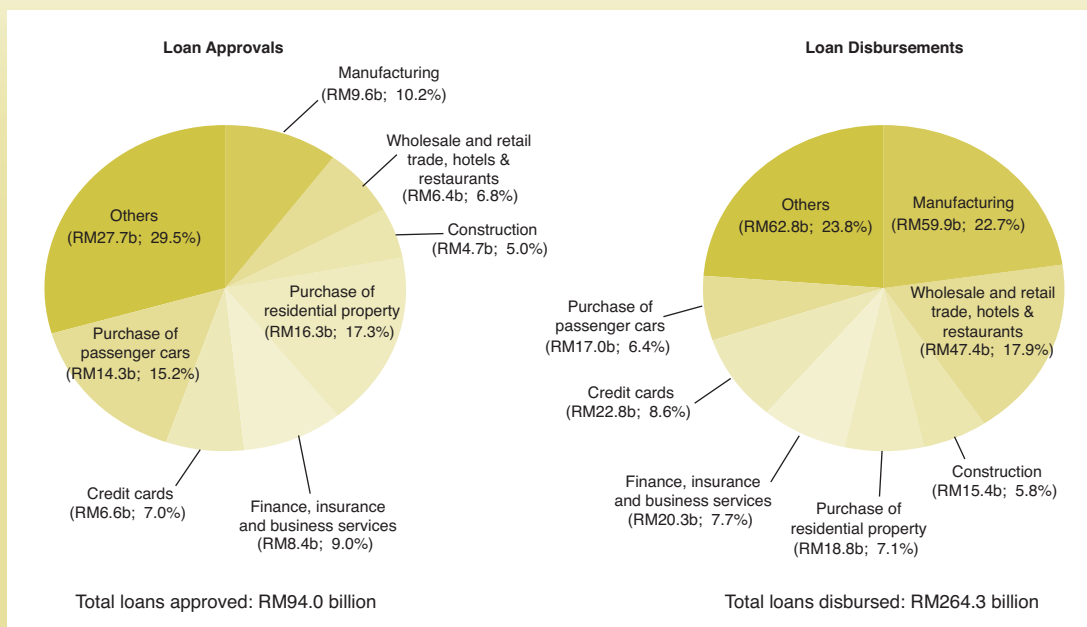
¹ Including Islamic banks.

² Including loans sold to Cagamas.

Source: Bank Negara Malaysia.

CHART 5.4

Loan Approvals and Disbursements By Sector: Value and Share January - June 2006



Source: Bank Negara Malaysia.

Loans outstanding to households continued to post double-digit growth rates, increasing by 13.3% to RM320 billion at end-June 2006 (end-2005: 15.1%; RM304.4 billion). Loan disbursements were predominantly for credit card spending, accounting for 31.5% of total household loan disbursements and purchase of residential properties (25.9%). Credit card usage continued to rise, driven by the growth in private consumption and aggressive promotion of credit cards.

The **performance of the ringgit** was mixed against the major currencies during the period from end-2005 to 15 August 2006, as shown in *Chart 5.5 and Table 5.6*. The ringgit strengthened against the US dollar but depreciated against the euro and pound sterling. The ringgit was supported by the strong trade performance and sustained capital flows, as well as favourable growth prospects. Against regional currencies, the ringgit recorded a mixed performance. Several regional

currencies had appreciated on the back of interest rate hikes to curb inflation arising from higher crude oil prices. Since the removal of the ringgit peg to 15 August 2006, the ringgit gained 5% against the US dollar and 9.1% against the yen.

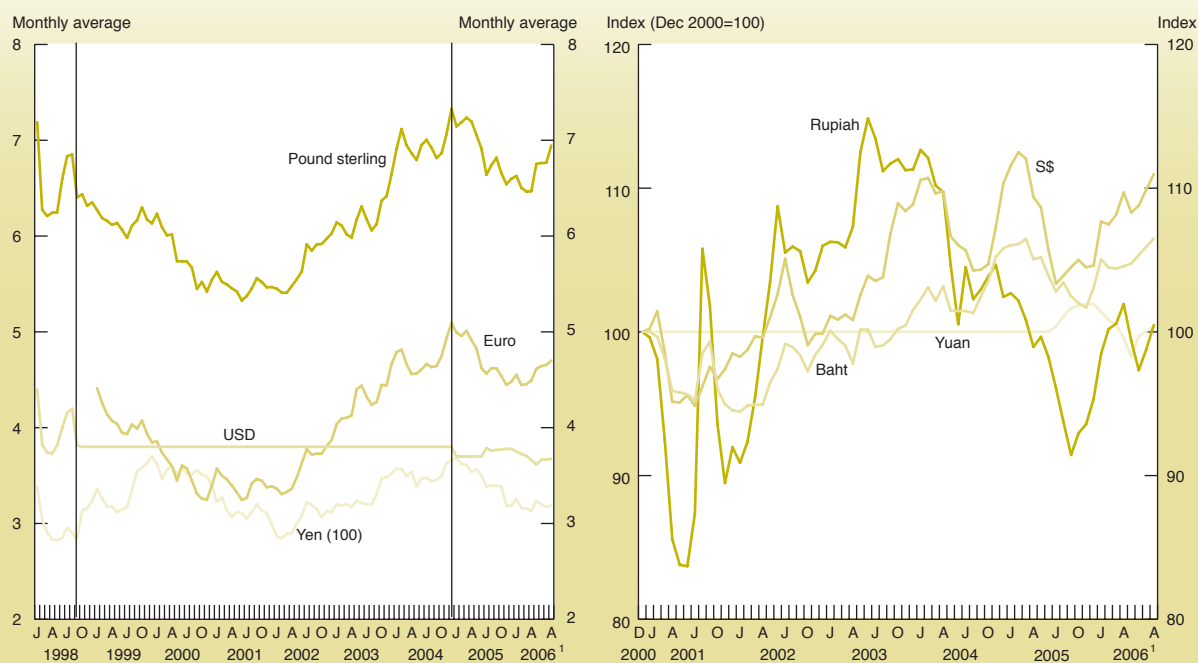
Health of the Banking System

Banking system remains robust...

The banking system remained robust with strong capitalisation and profitability and further improvement in asset quality in the first six months of 2006, amid favourable macroeconomic conditions. The risk-weighted capital ratio (RWCR) and core capital ratio (CCR) of the banking system were sustained at 12.9% and 10.1%, respectively at end-June 2006 (end-2005: 13.6%; 10.7%), continuing to exceed the Basel minimum requirements of 8% and

CHART 5.5

Performance of Ringgit Against Selected Currencies



¹ As at 15 August 2006.

Source: Bank Negara Malaysia and Bloomberg.

TABLE 5.6

Performance of Ringgit Against Selected Currencies

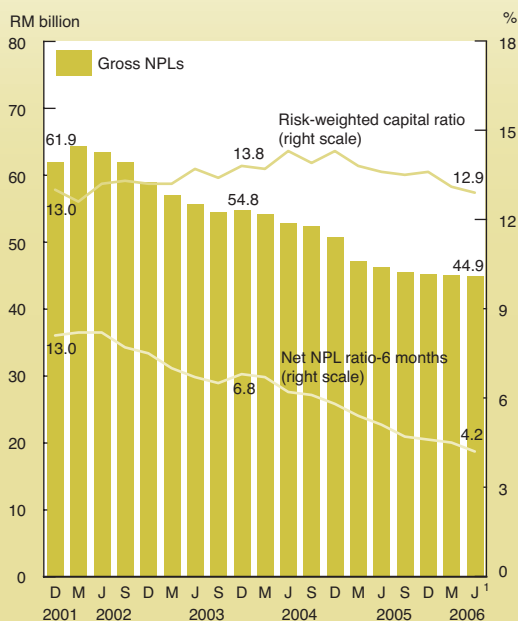
Currency	RM per foreign currency ¹			Change (%)	
	21 July 2005	End-2005	15 August 2006	21 July 2005	End-2005
US dollar	3.8000	3.7800	3.6185	5.0	4.5
Pound sterling	6.6270	6.5226	6.9579	-4.3	-6.3
Euro	4.6212	4.4867	4.6867	-1.3	-4.3
Japanese yen (100)	3.3745	3.2229	3.1589	9.1	2.0
Singapore dollar	2.2570	2.2714	2.3283	-1.2	-2.4
Thailand baht (100)	9.0681	9.2049	9.8502	-6.5	-6.6
Philippine peso (100)	6.8131	7.1254	7.1597	-4.9	-0.5
Indonesian rupiah (100)	0.0386	0.0385	0.0404	-4.0	-4.7
Korean won (100)	0.3665	0.3739	0.3812	-2.1	-1.9
Chinese yuan	0.4686	0.4686	0.4606	1.7	1.7

¹ Interbank rates at 12.00 noon in Kuala Lumpur are an average of the highest buying and lowest selling quotes.

Source: Bank Negara Malaysia.

CHART 5.6

**Banking System:
Gross Non-Performing Loans (NPLs),
Net NPL Ratio and Risk-Weighted
Capital Ratio**



¹ As at end-June 2006.

Source: Bank Negara Malaysia.

4%, respectively. The banking system recorded pre-tax profits totalling RM6.1 billion during the first six months of 2006 on account of higher net interest and fee-based income.

Asset quality of the banking system continued to improve with the net non-performing loans (NPLs) ratio based on 6-months declining to 4.2% at end-June 2006 (end-2005: 4.6%), the lowest level since the Asian financial crisis, as shown in *Chart 5.6*. The net NPL ratio based on 3-months also improved to 5.5% (end-2005: 5.8%).

Transformation of the Financial Landscape

Emergence of investment banks...

The financial landscape continues to be progressively transformed following the rationalisation among existing financial institutions, leading to the phasing out of

Progress of Investment Banks as at End-June 2006

- Significant progress has been achieved in the rationalisation process of capital market intermediaries into investment banks. All banking groups have obtained the requisite approvals from the Minister of Finance to transform the merchant banks, stockbroking firms and discount houses within the group into investment banks.
- Banking groups are now in the implementation process of their rationalisation programme. Pending the completion of this process, merchant banks, stockbroking firms and discount houses within banking groups shall continue to operate as separate legal entities. Stand-alone discount houses are also given the same flexibility to complete their transformation process into investment banks. The transformation process into investment banks is expected to be completed by 31 December 2006.
- With regard to universal brokers, BNM and the Securities Commission (SC) have completed the due diligence exercises on these entities. The universal brokers are now in the process of submitting their applications to become investment banks to BNM and the SC. However, they are given the flexibility in determining the timeframe required for them to transform into investment banks.

Credit Cards in Malaysia – Some Highlights

Credit Cards in Circulation

The expansion of credit cards in Malaysia has been significant, with growth continuing to register double-digit rates. During the period 2001-2005, credit cards recorded an average annual growth of 22.7%. Intense competition as well as aggressive promotional efforts of banking institutions have resulted in a higher number of Malaysians owning credit cards. The number of credit cards in circulation has risen to 8.4 million as at June 2006.

Numbers of Credit Cards in Circulation (million)

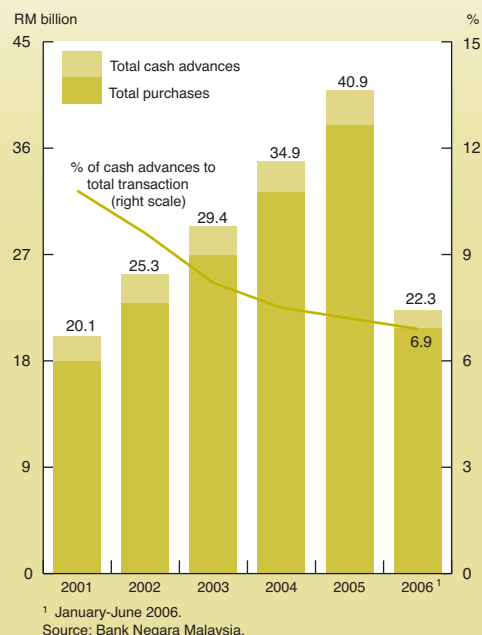
Year (End-period)	Principal Cards	Supplementary Cards	Total	Annual Growth (%)
2001	2.84	0.59	3.84	21.6
2002	3.63	0.73	4.36	27.1
2003	4.22	0.88	5.10	17.0
2004	5.37	1.21	6.58	29.0
2005	6.62	1.20	7.82	18.8
June 2006	7.35	1.05	8.40	17.8

Source: Bank Negara Malaysia.

Credit Card Transactions vis-à-vis Cash Advances

Credit card transactions have risen in tandem with the increase in the number of cardholders and the strong growth in private consumption. Credit card transactions grew by 17.3% to nearly RM41 billion in 2005 (2004: 18.8%; RM34.9 billion). The bulk of credit card transactions continued to be mainly for purchases of goods and services. Consumers have been encouraged to use credit cards for purchases, following the vigorous promotion by banking institutions,

Credit Card Transactions by Malaysian Cardholders



including the introduction of reward incentives and easier payment terms for the purchase of consumer durables.

With credit cards largely used for purchase transactions, cash advances as a share of total credit card transactions reflected a declining trend. In June 2006, cash advances accounted for 6.9% of total credit card transactions, down from 7.2% in 2005 and 7.5% in 2004.

Non-Performing Loans Due to Credit Cards

Despite the significant increase in the number of credit cardholders and transactions through credit cards, the NPLs on credit cards accounted for only 1.4% of total NPLs in the banking system as at end-2005. Furthermore, BNM data also indicates that 60% of card users serviced their credit card loans in full.

Non-Performing Loans of Credit Cards

Year (End-period)	(RM million)		% Share
	NPLs of Credit Cards	Total NPLs of Banking System	
2001	409.4	67,828.3	0.6
2002	434.3	63,676.4	0.7
2003	578.6	58,271.5	1.0
2004	663.9	55,064.7	1.2
2005	743.7	52,151.0	1.4
June 2006	597.2	52,069.8	1.1

Source: Bank Negara Malaysia.

Credit Card Bankruptcies (million)

Year	Credit Card Bankruptcies	Amount Involved (RM million)	Total Bankruptcies	% of Credit Card Bankruptcies to Total
2001	952	23.3	11,685	8.1
2002	1,117	28.2	12,268	9.1
2003	1,152	33.0	12,351	9.3
2004	1,397	38.7	16,251	8.6
2005	1,479	44.4	15,868	9.3
Total	6,884	183.9	78,141	8.8

Note: Refers to individuals declared bankrupt.

Source: Bank Negara Malaysia.

Credit Card Bankruptcies

Notwithstanding the increase in the number of credit card bankruptcies, the percentage of credit card bankruptcies continued to account for less than 10% of total bankruptcies. During the period 2001 to 2005, bankruptcies due to credit card debts totalled less than 7,000 vis-à-vis total bankruptcies at 78,141.

Key Consumer Initiatives

Measures have been taken to address the potential credit issues that could be faced by overstretched households and individuals. This includes BNM's website on BankingInfo, which aims to educate consumers regarding personal finance. Among others, BankingInfo incorporates information on charges applicable on credit cards, as well as tips on how to shop for credit

cards, minimise credit card charges and how to avoid being trapped as a borrower. Credit card issuers are also required to undertake prudent credit assessment and verification of credit worthiness of card applicants through BNM's Central Credit Reference Information System (CCRIS). In addition, the Credit Counselling and Debt Management Agency (CCDMA), which began operations in April 2006, provides free counselling and assistance to individuals on financial management and education, as well as debt restructuring.

Notwithstanding the measures in place, ultimately it is the consumers' financial discipline that matters with regard to credit card spending. Consumers should bear in mind that credit cards are to be used as a convenient mode of payment and to exercise prudence in spending.

traditional players such as finance companies and discount houses. The consolidation of commercial banks and finance companies into single entities was completed by January 2006, while the merger of merchant banks, stockbroking companies and discount houses is currently ongoing. The transformation process into investment banks is expected to be completed by year-end. The rationalisation is aimed at further enhancing the capacity and capability of the financial system to meet the changing and differentiated needs of the economy. The banking system also reported one merger exercise involving two domestic banking groups during the first six months of 2006.

There has also been progressive liberalisation of the financial sector. The LIFBs operating in Malaysia have been allowed to establish up to four additional branches within a one-year period effective 1 January 2006. This operational flexibility will permit LIFBs to participate more effectively in the domestic economy.

Meanwhile, the implementation of the **Financial Sector Master Plan (FSMP)** is well on track, with the end of 2005 marking the halfway point of the 10-year plan (2001–2010). As at 30 June 2006, 49 recommendations with milestones have been completed, while 29 recommendations are being implemented on a continuous basis. Capacity building initiatives will continue to be intensified during the remaining Phase 2 of the FSMP period to prepare the domestic financial sector for further global integration as it moves to the third phase of the FSMP.

Developments in Islamic Finance

Further initiatives to position Malaysia as a premier international Islamic financial centre...

Further initiatives were taken to position Malaysia as a premier international Islamic financial centre. A key initiative was the establishment of INCEIF, which commenced operations in March 2006. INCEIF will serve as an international centre of educational excellence in Islamic finance

by developing professionals and specialists in Islamic finance to meet the needs of the industry. In addition, the uptake of foreign equity in Islamic financial institutions of up to 49% will also help push Malaysia to the forefront of Islamic finance. Meanwhile, new Islamic financial products continued to be introduced as part of ongoing efforts to broaden and deepen the domestic Islamic capital market. The BNM *Sukuk Ijarah*, which was introduced in February 2006, will add to the diversity of instruments in managing liquidity in the Islamic money market, as well as serve as a benchmark for the issuance of other Islamic bonds.

In tandem with the progressive liberalisation of the Islamic banking industry, strategic moves were undertaken to further strengthen the institutional capacity and financial resilience of the domestic Islamic banking institutions. In this regard, seven domestic banking groups were approved to transform the “Islamic window” institutional structure into an Islamic subsidiary within their respective banking groups to carry out Islamic banking business. Six domestic banking groups have since commenced operations in 2006. Meanwhile, one foreign Islamic bank has been operational since August 2005, following the approval to three foreign Islamic financial institutions to operate in Malaysia. BNM also approved four new *takaful* licences to consortiums and joint ventures between domestic and foreign financial institutions in 2006. The new *takaful* operators will help to contribute towards the development of the *takaful* industry, as well as complement efforts in establishing Malaysia as a premier international Islamic financial centre.

An online submission of new Islamic financial products has also been successfully automated, following the implementation of the Product Approval and Repository System (PARS) in February 2006 to expedite the processing of new products for approval and maintenance of a repository of Islamic banking products. In February 2006, the Islamic Financial Services Board (IFSB) issued two standards, namely the Capital Adequacy Standard (CAS) and the Guiding Principles of Risk Management (Guiding Principles) for institutions offering

Islamic financial services. The CAS and the Guiding Principles are the first international standards that govern the prudential regulatory and supervisory framework for Islamic banking institutions issued by the IFSB.

Malaysia International Islamic Financial Centre (MIFC) Initiative

Another significant milestone was the launching of Malaysia International Islamic Financial Centre (MIFC) initiative in August 2006. The MIFC initiative will introduce measures and incentives to promote the centre in the offering of Islamic financial products and services by a diversified range of financial institutions in international currencies to the international and domestic financial community. Among the key measures include the following:

- i. Setting up of an International Currency Business Unit within Malaysian Islamic banks and *takaful* operators to offer Islamic financial services in international currencies. This division may enjoy tax incentives that will be introduced;
- ii. Issuance of new conditional licences under the Islamic Banking Act 1983 and conditional registrations under the *Takaful* Act 1984 to qualified foreign and Malaysian financial institutions to conduct the full range of Islamic banking and *takaful* business in international currencies and enjoy similar tax incentives as those accorded to the International Currency Business Units;
- iii. Greater flexibility for Labuan offshore Islamic banks and Islamic divisions of offshore banks as well as offshore *takaful* operators to open operational offices anywhere in Malaysia; and
- iv. Establishment of an MIFC Executive Committee as a single coordinating committee to efficiently and effectively act collectively in the implementation of the initiatives.

Performance of Islamic Banking Industry

Islamic banking expanded further...

The Islamic banking industry continued to expand in 2006. Islamic banking assets increased by 5% to RM117,393 million while deposits grew by 2.8% to RM86,216 million during the first six months of 2006, as shown in *Table 5.7*. Financing by Islamic banking institutions rose by 3.6% to RM69,820 million as at end-June 2006 (end-2005: RM67,365 million), mainly attributable to the increase in financing for the purchase of transport vehicles amounting to RM945 million. In terms of market share, Islamic banking assets accounted for 11.8% of total assets in the banking sector at end-June 2006 (end-2005: 11.6%). Meanwhile, the market share of Islamic financing and deposits stood at 15.6% and 11.6%, respectively of total loans and deposits of the banking system as at end-June 2006 (end-2005: 15.5%; 11.7%). In terms of financing by purpose, the purchase of transport vehicles accounted for the largest share at RM21,784 million or 31.2% of total Islamic financing at end-June 2006, as shown in *Table 5.8*.

TABLE 5.7

Islamic Banking: Key Indicators

	RM million		Change
	End-2005	End-June 2006	(%)
Assets	111,823.5	117,393.2	5.0
Deposits	83,874.8	86,216.5	2.8
of which:			
Investment	44,579.3	43,836.2	-1.7
Savings	9,504.5	10,096.0	6.2
Demand	14,785.6	15,994.0	8.2
Others	15,005.4	16,290.3	8.6
Financing	67,364.6	69,820.4	3.6
of which:			
SMEs	8,608.0	8,908.0	3.5
Large corporations	16,983.1	17,926.9	5.6
Households	41,773.5	42,985.5	2.9

Source: Bank Negara Malaysia.

TABLE 5.8

Islamic Banking System: Direction of Financing

Purpose	End-June 2006 (RM million)	Share (%)
Construction	1,132.20	1.6
Landed property	19,364.70	27.7
Personal uses	4,605.30	6.6
Credit cards	494.10	0.7
Purchase of consumer durables	41.30	0.1
Purchase of securities	842.50	1.2
Purchase of transport vehicles	21,784.40	31.2
Purchase of fixed assets	577.10	0.8
Merger and acquisition	2.00	0.0
Working capital	14,319.90	20.5
Other purpose	6,656.90	9.5
Total	69,820.40	100.0

Source: Bank Negara Malaysia.

The asset quality of the Islamic banking sector improved significantly with the net non-performing financing ratio declining from 4.8% in 2005 to 3.8% as at end-June 2006. The Islamic banking sector also remained well capitalised, with the total capital base increasing to RM11.4 billion as at end-June 2006, mainly due to new capital injection following the establishment of three new Islamic subsidiaries. As at end-June 2006, the Islamic banking sector recorded a strong RWCR and CCR of 15% and 12%, respectively (end-2005: 14.1%; 11.3%).

Development Financial Institutions

DFIs continued to finance development of strategic economic sectors...

The **development financial institutions (DFIs)** continue to provide financing to support development of the targeted sectors, including agriculture, high technology and capital-intensive industries, infrastructure and SMEs as well as exports. Total loans outstanding extended

TABLE 5.9

Development Financial Institutions: Direction of Lending

Sector	RM million		% share	
	End-2005	End-June 2006	End-2005	End-June 2006
Manufacturing	4,633.4	4,627.2	9.8	8.9
Agriculture	3,359.2	3,443.7	7.1	6.6
Electricity, gas and water supply	2,253.0	2,687.0	4.7	5.2
Broad property	12,267.5	14,244.2	25.8	27.4
of which:				
Construction	5,120.5	5,994.1	10.8	11.5
Residential property	5,465.1	6,225.3	11.5	12.0
Consumption credit	14,045.1	15,939.3	29.6	30.7
Transport and communication	6,539.4	6,497.1	13.8	12.5
Finance, insurance and business services	864.1	990.7	1.8	1.9
Others	3,557.7	3,571.4	7.5	6.9
Total	47,519.4	52,000.6	100.0	100.0

¹ Refers to Bank Pembangunan Malaysia Bhd, Bank Perusahaan Kecil dan Sederhana Malaysia Berhad (SME Bank), Bank Kerjasama Rakyat Malaysia Bhd, Bank Simpanan Nasional Bhd, Export-Import Bank of Malaysia Bhd, Bank Pertanian Malaysia, Malaysia Industrial Development Finance Bhd, Credit Guarantee Corporation Malaysia Bhd, Lembaga Tabung Haji, Sabah Development Bank Bhd, Sabah Credit Corporation, Borneo Development Corporation (Sabah) Sdn Bhd and Borneo Development Corporation (Sarawak) Sdn Bhd.

² Before 1 October 2005, data included Bank Industri & Teknologi Malaysia Bhd and Malaysia Export Credit Insurance Bhd and excluded SME Bank.

Source: Bank Negara Malaysia.

by the DFIs rose by 9.4% to RM52 billion as at end-June 2006 (end-2005: 25.8%; RM47.5 billion), as shown in *Table 5.9*. Of the total financing, 24.8% or RM12.9 billion were loans to SMEs, particularly in the construction as well as transport and communication sectors. More than three quarters of the SME loans were for *Bumiputera* entrepreneurs.

The increase in lending during the first half of 2006 was due mainly to higher financing for infrastructure projects, consumption credit and purchase of residential properties. Infrastructure loans extended by Bank Pembangunan Malaysia Bhd (BPMB) grew by 9.5% to account for 28% of total loans outstanding of the DFIs, mainly to finance activities in the construction and utilities sectors. Meanwhile, consumption credit increased further by 13.5%, reflecting sustained demand for personal loans of Bank Kerjasama Rakyat Malaysia Bhd and Bank Simpanan Nasional Bhd (BSN). Growth in housing loans also remained high at 13.9%, amidst the competitive interest rate environment. Both consumption credit and housing loans constituted 30.7% and 12%, respectively of total loans outstanding of the DFIs. Loans extended by Bank Pertanian Malaysia to the agriculture sector increased by 2.9% or RM90.4 million to RM3.3 billion as at end-June 2006 (end-2005: RM3.2 billion), mainly to the fisheries, crops and livestock sectors.

Total resources of DFIs increased by 3.9% to RM103 billion as at end-June 2006 (end-2005: RM99.2 billion), as shown in *Table 5.10*. The increase was mainly due to the expansion in shareholders' funds to RM15 billion (end-2005: RM12.7 billion), following capital injection by the Government into BSN, BPMB, Bank Perusahaan Kecil dan Sederhana Malaysia Bhd (SME Bank) and Export-Import Bank of Malaysia (EXIM Bank). Deposits mobilised by the deposit-taking DFIs and borrowings from the Government remained the major funding components to support activities of the DFIs, accounting for 52.6% and 14.7%, respectively of total resources.

TABLE 5.10

Development Financial Institutions: Sources and Uses of Funds (RM million)

	End-2005	End-June 2006
Sources		
Shareholders' funds	12,756.8	15,004.7
Paid-up capital	8,563.5	10,219.9
Reserves	2,244.8	2,245.7
Retained earnings	607.9	1,721.4
Current profit/(loss)	1,340.6	817.7
Deposits accepted	54,251.3	54,233.0
Borrowings	20,523.0	20,937.9
Government	14,828.8	15,156.1
International/foreign/ multilateral agencies	4,300.8	4,422.3
Others	1,393.4	1,359.5
Others	11,629.1	12,845.2
Total	99,160.2	103,020.8
Uses		
Deposits placed	14,162.6	15,294.1
Investment securities	22,984.2	21,465.5
of which:		
Securities	10,616.4	10,359.6
Quoted shares	6,850.2	6,873.1
Unquoted shares	314.4	313.1
Loans and advances	47,519.4	52,000.6
Fixed assets	3,910.2	3,945.6
Others	10,583.8	10,315.0
Total	99,160.2	103,020.8
Contingencies		
Guarantees	6,335.9	7,263.6
Export credit insurance	743.8	812.3
Total	7,079.7	8,075.9

¹ Refers to Bank Pembangunan Malaysia Bhd, Bank Perusahaan Kecil dan Sederhana Malaysia Berhad (SME Bank), Bank Kerjasama Rakyat Malaysia Bhd, Bank Simpanan Nasional Bhd, Export-Import Bank of Malaysia Bhd, Bank Pertanian Malaysia, Malaysia Industrial Development Finance Bhd, Credit Guarantee Corporation Malaysia Bhd, Lembaga Tabung Haji, Sabah Development Bank Bhd, Sabah Credit Corporation, Borneo Development Corporation (Sabah) Sdn Bhd and Borneo Development Corporation (Sarawak) Sdn Bhd.

² Before 1 October 2005, data included Bank Industri & Teknologi Malaysia Bhd and Malaysia Export Credit Insurance Bhd and excluded SME Bank.

Source: Bank Negara Malaysia.

Performance of Insurance Industry

Slower growth of insurance industry...

The **insurance industry's** combined premium income of both life and general business increased at a lower rate of 2.4% to RM11,825 million in the first half of 2006 (January-June 2005: 8.7%; RM11,549 million), as shown in *Table 5.11*. The moderate increase was mainly due to the slower growth recorded in the life insurance sector, which constituted 67% of the industry's premium income.

The lower premium income for the **life insurance sector** was mainly caused by a decline in new business premiums, but was, however, mitigated by strong annual premium contributions of in force business. During the first half of 2006, new business premiums contracted by 11.4% to RM3,217 million (January-June 2005: 14.3%; RM3,630 million), primarily due to the scaling back of sales of single premium capital-guaranteed endowment products. However, investment-linked business rebounded to register a positive growth of 55.9% to RM1,277 million (January-June 2005: -31%; RM819 million). Investment-linked and ordinary life endowment policies accounted for RM1,957 million or 60.8% of total new life business premiums, reflecting sustained consumer interest in life insurance to meet short to medium-term investment objectives. Meanwhile, market penetration as measured in terms of the total number of policies in force to total population, increased to 38.7% as at end-June 2006 (end-June 2005: 38.1%).

In the **general insurance sector**, premiums underwritten expanded by 4.5% to RM5,071 million (January-June 2005: 10%; RM4,852 million). Fire insurance business recorded a marginal growth of 0.8% to RM946 million due to the softening of premium rates, especially for large industrial risks. Similarly, motor insurance business, which constituted 43% of general business, also recorded a nominal growth of 0.8% (January-June 2005: 15.7%). The slower

TABLE 5.11

Life and General Insurance Business

	End-2005	End-June 2006 ¹
Life Insurance Business (RM million)		
New business:		
Number of policies ('000 units)	1,365	603
Sums insured	181,156.5	98,379.6
Total premiums	6,701.4	3,217.3
Business in force		
Number of policies ('000 units)	10,145	10,317
Sums insured	644,295.5	662,551.9
Annual premiums	12,308.1	12,656.9
Premium income	16,002.1	7,903.0
Benefit payments	6,268.7	3,208.6
Death and disability	772.1	387.4
Maturity/Vesting	1,504.7	683.1
Surrender/Net cancellation of units	1,808.0	1,015.7
Cash bonuses	816.9	327.4
Medical	704.6	428.4
Others	662.4	366.6
General insurance (RM million)		
Premium income:		
Gross direct premiums	9,388.2	5,071.4
Net premiums	7,551.7	3,922.1
Reinsurance placed outside Malaysia	966.9	584.4
Retention ratio ² (%)	88.7	87.0
Number of insurance companies		
Direct:		
Life	7	8
General	26	26
Composite	9	8
Reinsurance:		
Life	1	1
General	5	4
Composite	1	1

¹ Preliminary data.

² Net premiums to gross direct and reinsurance accepted premiums less reinsurance within Malaysia.

Source: Bank Negara Malaysia.

TABLE 5.12

Assets of Life and General Insurance Funds
 (RM million)

	Life Insurance		General Insurance	
	End-2005	End-June 2006 ¹	End-2005	End-June 2006 ¹
Property, plant and equipment	432.6	446.4	720.9	733.7
Loans	9,725.1	10,228.5	244.8	247.4
Government securities	12,746.3	12,756.9	2,661.3	2,924.4
Government guaranteed loans	-	-	10.0	10.0
Corporate and debt securities	42,076.5	43,455.7	6,224.6	6,260.0
Investment properties	3,007.0	3,111.6	428.3	388.5
Cash and deposits	8,278.2	10,101.0	5,562.6	5,634.1
Other assets ²	2,396.9	3,001.6	2,123.2	2,744.3
Total	78,662.6	83,101.7	17,975.7	18,675.4

¹ Preliminary data.

² Includes other investments and foreign assets.

Source: Bank Negara Malaysia.

growth was mainly due to the decline in motor vehicle sales, resulting from a combination of factors, such as weaker demand, adjustments to motor vehicle tariffs under the National Automotive Policy (NAP), depressed used car value, tighter consumer credit and higher petrol prices.

Total benefits and claims paid by the insurance industry increased by 13.2% to RM5,293 million in the first half of 2006 (January-June 2005: RM4,675 million). Payment on net policy benefits of the life insurance sector continued to account for the bulk (61%) of total benefits and claims paid. Notwithstanding the slower growth in premiums and a higher payout in benefits and claims, the profitability of the insurance industry remained healthy on the back of a more favourable investment climate, which led to the write-back of provisions for diminution in the value of investments and profit from investments during the period. During the first half of 2006, excess of income over outgo for the life insurance sector improved by 1.5% to RM5,254 million while operating profit for the general insurance sector improved by 7% to RM740 million.

Total assets of the insurance industry increased further by 5.3% to RM101,777 million as at end-June 2006 (end-2005: RM96,638 million), as shown in *Table 5.12*. Life insurance business continued to account for a significant portion of the industry's total assets with a share of 82% or RM83,102 million (end-2005: 81.4%; RM78,663 million). In terms of composition of assets, corporate and debt securities remained the largest asset class, accounting for 48.8% of total assets (end-2005: 50%). Despite the three-fold increase of investments in foreign assets to RM696 million, the share of foreign assets remained small at less than 1% of total assets.

Performance of *Takaful* Industry

Takaful industry expanded further...

The *takaful* industry expanded further during the first six months of 2006, with major key indicators of the industry showing positive growth. New *takaful* business slowed down during the period with total new contributions

declining by 8.3% to RM359 million (January-June 2005: 18.3%; RM392 million), as shown in *Table 5.13*. However, new *takaful* business is expected to rise in the second half of the year with the entrance of new *takaful* operators and existing *takaful* operators intensifying their efforts in promoting family *takaful* products.

Business in force also continued to show positive results with the number of certificates and annual contributions increasing at double-digit rates of 17.2% and 29.9%, respectively. This was mainly contributed by the marginal increase in termination rate. Market penetration of the *takaful* industry, as measured by the number of certificates in force divided by total population, rose to 6.1% as at end-June 2006 (end-2005: 5.6%).

TABLE 5.13

Family and General *Takaful* Business

	Financial Year 2005	End-June 2006
Assets¹ (RM million)	5,878.4	6,510.5
Government Investment Issues	662.2	692.0
Investment deposits	1,470.7	1,817.3
Islamic PDS and equities	2,997.7	3,087.1
Cash and bank balances	161.6	204.2
Financing	62.3	58.9
Fixed assets	230.6	235.6
Others	293.3	415.4
Family <i>Takaful</i> Business		
New Business:		
Total contributions (RM million)	725.5	359.0
Sums participated (RM million)	36,281.0	19,615.7
Number of certificates	356,623	174,844
Business in Force:		
Total contributions (RM million)	576.1	674.0
Sums participated (RM million)	111,342.5	107,809.9
Number of certificates	1,499,691	1,629,624
General <i>Takaful</i> Business		
Gross contributions (RM million)	553.8	392.3
Net claims paid (RM million)	133.8	100.7

¹ Combined assets of family *takaful* and general *takaful* funds.
Source: Bank Negara Malaysia.

Gross contributions of the general *takaful* business rose by 29.3% to RM392.3 million during the first six months of 2006 (end-June 2005: RM303.5 million). Motor insurance business recorded stronger growth, accounting for 37% of the total gross contributions, followed by fire insurance business with 33.9%.

Total assets of the *takaful* industry expanded by 10.8% to RM6,511 million at end-June 2006 (end-2005: RM5,878 million) and accounted for 5.9% of the total assets in the insurance sector. In terms of asset allocation, Islamic PDS and equities constituted the largest asset class amounting to RM3,087 million or 47.4% of total assets of the *takaful* industry.

Capital Market

Higher PDS raised by the private sector...

Gross funds raised in the capital market grew by 4.8% to RM36,543 million in the first six months of 2006 (January-June 2005: -21.2%; RM34,864 million), as shown in *Table 5.14*. Of significance, funds raised by the private sector through the debt and equity markets accounted for a larger share at RM20,038 million or 58% of total funds, in consonance with the role of the private sector as the driver of economic growth. Issuance of Government securities declined by 15.3% to RM14,506 million (January-June 2005: -39.2%; RM17,135 million), as the Government continued on its consolidation efforts. In contrast, new PDS issued by the private sector expanded significantly by 60.5% to RM21,357 million (January-June 2005: -1.7%; RM13,309 million). Despite accounting for higher redemption, net PDS raised totalled RM8,175 million, substantially larger than the RM5,019 million in the corresponding period of 2005. Meanwhile, funds raised in the equity market during the first half of 2006 were significantly lower at RM680 million (January-June 2005: RM4,421 million). This was due to the lower number of initial public offerings (IPOs) during the period. The IPOs were also predominantly from the smaller capitalised companies.

In terms of PDS issuance by sector, companies in the finance, real estate and business services sector were the main issuers, accounting for

TABLE 5.14

**Funds Raised in the Capital Market
January-June**
(RM million)

	2005	2006 ¹
By Public Sector		
Government Securities		
Malaysian Government Securities	13,543.1	11,005.6
Khazanah bonds	833.2	0.0
Government Investment Issues	2,001.1	3,500.0
Merdeka Savings Bonds	758.0	0.0
New Government securities	17,134.3	14,505.5
Less: Redemptions	8,522.9	4,502.9
Net funds raised	8,611.4	10,002.6
By Private Sector		
Shares²		
Initial public offerings	3,867.2	598.0
Rights issues	536.2	66.5
Private placements	0.0	0.0
Special issues	0.0	0.0
Warrants	17.4	15.8
New share issues	4,421.2	680.3
Debt Securities³ (gross)		
Straight bonds	1,310.3	3,306.0
Convertible bonds	2,708.7	0.0
Islamic bonds	2,668.4	3,360.0
Asset-backed bonds	497.3	745.9
Bonds with warrants	0.0	0.0
Medium-term notes ⁴	4,944.2	8,295.5
Cagamas bonds	1,180.0	5,650.0
New debt securities	13,308.9	21,357.1
Less: Redemptions	8,290.1	13,182.6
Net issues of debt securities	5,018.9	8,174.5
Net funds raised	9,440.0	8,854.7
Total net funds raised	18,051.4	18,857.3

¹ Preliminary data.

² Excludes funds raised by the exercise of Employees Share Option Scheme, Transferable Subscription Rights and Irredeemable Convertible Unsecured Loan Stocks.

³ Includes bonds issued by banking institutions since July 2000.

⁴ Classified as instrument of PDS since January 2004.

Source: Bank Negara Malaysia.

RM4,666 million or 29.7% of total PDS issuance during the period (January-June 2005: RM4,043 million; 33.3%), as shown in *Table 5.15*. More than 60% of the PDS proceeds were used for financing new activity (January-June 2005: 39.3%), reflecting the continuing growth in private investment activity, as shown in *Chart 5.7*.

Further initiatives continue to be taken towards developing Malaysia into a world-class capital market. Initiatives in the pipeline include the consolidation of the securities and futures laws and a one-stop processing of visas and work permits for foreigners in the financial sector, which will be centralised at BNM and the SC.

Cagamas, the National Mortgage Corporation, remained an active issuer of PDS with Cagamas outstanding bonds amounting to RM26,225 million or 12.2% of total outstanding PDS at end-June 2006 (end-2005: RM24,357 million; 11.8%). During the first six months of 2006, Cagamas raised 22 new PDS issues with a total

TABLE 5.15

New Issues of PDS by Sector¹
(January-June)

Sector	2005		2006 ²	
	RM million	Share (%)	RM million	Share (%)
Agriculture	155.5	1.3	285.0	1.8
Manufacturing	1,127.1	9.3	270.8	1.7
Electricity, gas and water supply	3,433.9	28.3	3,242.1	20.6
Wholesale & retail trade, hotels and restaurants	122.0	1.0	5.4	0.0
Construction	1,032.2	8.5	3,278.0	20.9
Transport, storage and communication	1,088.7	9.0	140.0	0.9
Finance, insurance, real estate and business services	4,042.8	33.3	4,665.9	29.7
Government and others	1,126.7	9.3	3,820.0	24.3
Total	12,128.9	100.0	15,707.2	100.0

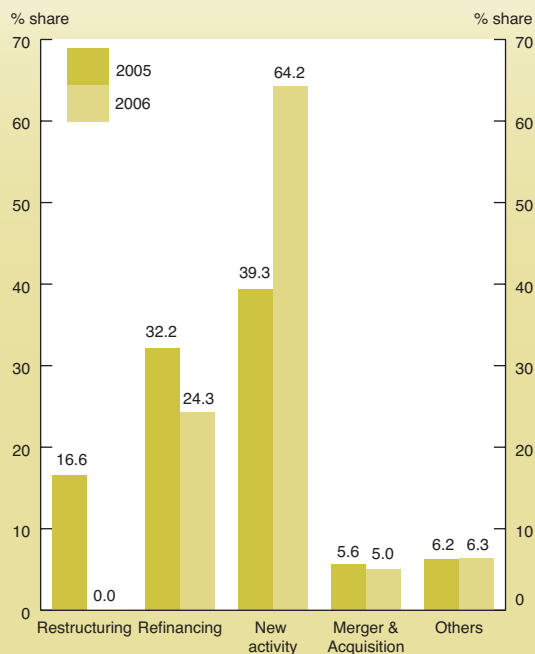
¹ Excluding Cagamas bonds.

² Preliminary.

Source: Bank Negara Malaysia.

CHART 5.7

New Issues of PDS by Purpose January-June



Source: Bank Negara Malaysia.

nominal value of RM5,650 million, accounting for 26.5% of the PDS market (January-June 2005: 9 issues; RM1,180 million). However, the volume of secondary trading declined substantially by 52.2% to RM5,697 million from RM11,922 million over the same period, due to market uncertainty regarding future interest rate direction.

New PDS issuances continued to be dominated by fixed notes involving RM3,150 million, accounting for half of Cagamas bonds, followed by *Bithaman Ajil* Securities with RM2,500 million (40.5% share). The purchase of loans and debts increased by three-fold to RM4,538 million (January-June 2005: RM1,399 million), as financial institutions were prompted to lock in their sales with Cagamas to hedge against rising interest rates, following two increases in the OPR during the first six months of 2006. As at end-June 2006, Cagamas bonds continued to be predominantly held by banking institutions, accounting for 50.6% of total Cagamas bonds, followed by provident and pension funds with 33%.

Since the mandate in 2004 to undertake the securitisation of the Government staff housing loans, Cagamas, through its subsidiary Cagamas MBS Bhd, had launched three issues of residential mortgage-backed securities (RMBS) totalling RM6,046 million. Of the three RMBS issued, one was an Islamic RMBS involving RM2,050 million.

During the first six months of 2006, both **Rating Agency Malaysia Bhd (RAM)** and **Malaysian Rating Corporation Bhd (MARC)** completed ratings on 74 issues (January-June 2005: 74 issues). Although the value of proposed issues was higher at RM27,649 million (January-June 2005: RM25,007 million), the bond market was somewhat affected by expectations of interest rate increases. The bulk of ratings continued to be concentrated on Islamic PDS, reflecting strong interest in Islamic papers and in line with ongoing efforts to promote the domestic Islamic capital market. Ratings were completed on 35 Islamic issues valued at RM17,143 million and accounted for 47.3% of the total number of PDS ratings (January-June 2005: 58 issues; RM20,207 million; 78.4%). In terms of rating category, most of the PDS rated were in the AAA, AA and A categories, indicating market preference for highly rated debt securities. The higher proposed value of PDS issues was largely contributed by Khazanah, the Government investment arm, followed by proposed issues in the financial services, infrastructure and utilities as well as the property sectors.

Bursa Malaysia

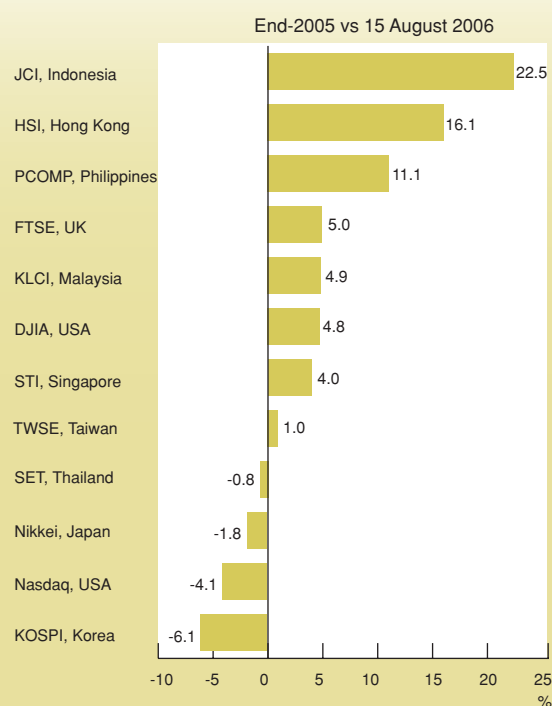
Improved performance despite concerns of rising inflation and higher interest rates...

Bursa Malaysia began 2006 on a positive note on improved investor sentiment amidst favourable economic prospects and continued foreign portfolio inflows. The benchmark Kuala Lumpur Composite Index (KLCI) gained 26.84 points or 3% to close at 926.63 points at end-March 2006 (end-2005: 899.79 points). Market capitalisation was also higher at RM732.9 billion (end-2005: RM695.3 billion). Average

daily turnover rose more than two-fold to 779.5 million units during the first quarter (Q4 2005: 303.9 million units). The KLCI hit a six-year high of 966.88 points on 9 May 2006 before concerns over rising US interest rates and global inflationary pressures began to affect major and regional markets. The decline was further aggravated by a sharp correction in the prices of global commodities. The KLCI closed lower at 914.69 points with market capitalisation at RM721.8 billion as at end-June 2006. In July, the performance of global and regional bourses was affected by the escalation of tensions in the Middle East as well as higher crude oil prices, which breached USD78 per barrel. Despite the adverse developments, the KLCI closed higher at 935.85 points as at end-July 2006 compared to the previous month. In terms of year-to-date performance to 15 August 2006, the KLCI has risen by 44.15 points or 4.9% to 943.94 points, as shown in *Chart 5.8*.

CHART 5.8

Performance of Selected Stock Market Indices



Trading on Bursa Malaysia was more active with total turnover surging by 83.3% to 120.6 billion units in the first seven months of 2006 (January-July 2005: 65.8 billion units), as shown in *Table 5.16* and *Chart 5.9*. The market continued to attract foreign participation, which accounted for 34.7% of trading activity during the period (January-July 2005: 34.4%). On a

TABLE 5.16

Bursa Malaysia: Selected Indicators (January-July)

	2005	2006
Price Indices¹		
Composite	937.39	935.85
EMAS ²	213.88	n.a
Second Board	91.90	90.24
MESDAQ Market	95.09	118.97
Total Turnover³		
Volume (million units)	65,794.8	120,601.1
Value (RM million)	112,972.2	141,631.3
Average Daily Turnover³		
Volume (million units)	463.3	849.3
Value (RM million)	795.6	997.4
Market Capitalisation ¹ (RM million)	724,971.6	727,792.4
Market Capitalisation ¹ /GDP (%)	146.4	132.7
Total No. of Companies Listed¹		
	997	1,029
Main Board	642	649
Second Board	269	258
MESDAQ Market	86	122
Market Liquidity¹		
Turnover Value/ Market Capitalisation (%)	15.6	19.5
Turnover Volume/ No. of Listed Securities (%)	20.8	36.7
Market Concentration¹		
10 Most Highly Capitalised Stocks/Market Capitalisation (%)	36.1	35.4
Average Paid-up Capital of Stockbroking Firms ¹ (RM million)	170.6	155.4

¹ End period.

² EMAS Index was replaced by FBMEMAS Index on 26 June 2006.

³ Based on market transactions only during period.

Source: Bursa Malaysia.

sectoral basis, the MESDAQ market was the best performer during the first seven months of 2006, following its sharp correction in 2005 and supported by the upturn in the electronics cycle, as shown in *Table 5.17*. The MESDAQ market index rose by 36.6% to 118.97 points at end-July 2006 (end-2005: -29.1%; 87.09 points).

The equity market remained an important source of capital for the corporate sector, with a total of 26 IPOs during the first seven months of 2006. The bulk of the IPOs came from small to medium-capitalised companies, with the MESDAQ market attracting 16 IPOs, the Second Board six and the Main Board four, bringing the total number of listed companies on Bursa Malaysia to 1,029 as at end-July 2006 (January-July 2005: 47 IPOs; 997 listed companies). Funds mobilised through the equity market amounted to RM1,439.8 million during the period (January-July 2005: RM5,615 million).

TABLE 5.17

Bursa Malaysia: Performance of Selected Indices

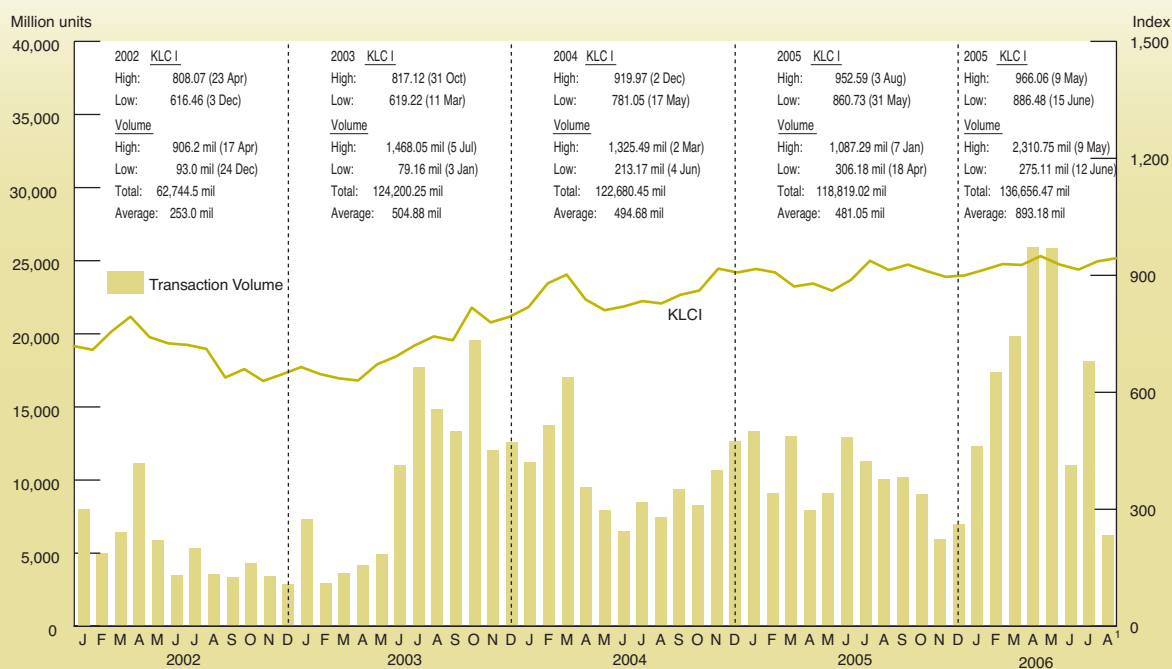
Index	End-Dec 2005	End-July 2006	Change (%)
Composite	899.79	935.85	4.0
EMAS	203.85	—	—
Second Board	80.44	90.24	12.2
MESDAQ Market	87.09	118.97	36.6
Syariah	127.12	135.09	6.3
FBM100 ¹	—	6,044.78	—
FBM30 ¹	—	6,055.80	—
FBM70 ¹	—	6,001.67	—
FBMSCAP ¹	—	6,266.21	—
FBMEMAS ¹	—	6,073.08	—
FBMFLG ¹	—	6,194.17	—
Construction	127.00	155.99	22.8
Consumer Products	220.66	241.12	9.3
Finance	7,204.35	7,472.50	3.7
Industrial	2,040.95	1,945.34	-4.7
Industrial Products	74.65	77.88	4.3
Mining	314.98	376.65	19.6
Plantation	2,798.71	3,506.35	25.3
Property	524.64	584.21	11.4
Technology	26.81	27.29	1.8
Trading/Services	129.67	130.50	0.6

¹ The FTSE Bursa Malaysia Index series was launched on 26 June 2006.

Source: Bursa Malaysia.

CHART 5.9

Bursa Malaysia: KLCI and Trading Volume



As part of efforts to boost the domestic stock exchange among global investors, Bursa Malaysia launched Phase 1 of the new FTSE Bursa Malaysia Index Series on 26 June 2006. The new FTSE Bursa Malaysia Index is expected to enhance the visibility of the Malaysian stock market and help spur the creation of new investment products, such as exchange traded funds, new derivatives and over-the-counter products. The best performing index in the new FTSE Bursa Malaysia Index series was FTSE-Bursa Malaysia Large 30 Index, which increased by 4.3% to 6,105.30 points as at 15 August 2006 (26 June 2006: 5,855.10 points).

Performance of Unit Trust Industry

Unit trust industry expanded moderately...

The **unit trust industry** expanded moderately in the first six months of 2006. A total of 33 new funds were launched during the period (2005: 51 funds), bringing the total number of funds to 356 as at end-June 2006 (end-2005: 323 funds) as shown in *Table 5.18*. Units in circulation increased by 6.4% to 148.34 billion units as at end-June 2006 (end-2005: 17.5%; 139.39 billion units). Meanwhile, investments abroad amounted to RM4.02 billion as at end-May 2006 (end-2005: RM3.48 billion), following the increase in the threshold for investment abroad from 10% to 30% of the total net asset value (NAV) of resident funds, effective 1 April 2005.

As of end-May 2006, 24 global funds with total fund size of RM18.49 billion have been approved by the SC. The NAV of the unit trust industry grew by 6.9% to RM105,294 million at end-June 2006 (end-2005: 12.7%; RM98,485 million). The Islamic unit trust segment expanded further, with nine new Islamic unit trust funds launched during the period, bringing the total to 88 funds as at end-June 2006 (end-2005: 79 Islamic trust funds). However, the NAV of Islamic funds increased slower by 3.1% and accounted for 8.3% of total NAV of the unit trust industry at end-June 2006 (end-2005: 25.5%; 8.6%). In July 2006, the first Islamic

TABLE 5.18

Unit Trust Industry: Selected Indicators

	End-2005	End-June 2006
Number of Unit Trust Management Cos.	36	36
Number of Unit Trust Funds ¹	323	356
Conventional	244	268
Islamic	79	88
Units in Circulation (million)	139,386	148,336
Number of Accounts (million)	10.9	11.1
Net Asset Value (NAV) (RM million)	98,485	105,294
Conventional	89,988	96,544
Islamic	8,487	8,750
NAV/Bursa Malaysia Market Value (%)	14.2	14.6

¹ Refers to funds already launched.

Source: Securities Commission.

Real Estate Investment Trusts (REITs) was launched, in line with ongoing efforts to promote the Islamic capital market.

Investor response has been positive to the introduction of REITs as an additional investment instrument, with total turnover chalking up RM311 million in the first half of 2006 compared with RM342 million in 2005. The recent move in July 2006 to allow the REITs industry to borrow up to 50% of their total asset value from 35% previously, is expected to further spur investor interest in REITs. The higher gearing limit also enhances the competitiveness of Malaysian REITs vis-à-vis REITs of regional countries.

Derivatives Market

Higher trading of derivatives...

Trading on **Bursa Malaysia Derivatives** was higher at over two million contracts during the first seven months of 2006 (January-July 2005: 1.4 million contracts). The Crude Palm Oil (CPO) futures market was the best performer and accounted for 45.4% of total derivatives

volume. Turnover of CPO futures rose by 30% to 918,805 contracts during the period (January-July 2005: 708,628 contracts). The benchmark 3-month CPO futures prices averaged RM1,468 per tonne during the period (January-July 2005: RM1,405 per tonne). Trading in the CPO futures market was significantly higher in July, with an increase of 85.7% over June 2006, spurred mainly by the potential increase in demand from palm oil-based biodiesel plants.

The KLCI futures market remained active with a 45.7% increase in volume to 904,573 contracts (January-July 2005: 620,877 contracts), accounting for 44.7% of total derivatives traded. The financial futures market improved significantly, with turnover of the 3-month Kuala Lumpur Interbank Offered Rate (KLIBOR) futures increasing by close to 70% to 174,972 contracts (January-July 2005: 103,147 contracts). The higher volume was attributed to market expectations of domestic interest rate hikes. Total turnover of Malaysian Government Securities (MGS) futures more than doubled to 24,610 contracts (January-July 2005: 10,512 contracts). The 5-Year MGS futures with 22,991 contracts contributed significantly to the higher volume due to the concentration of the underlying market activity in the 5-year tenure.

The first tranche of SSF, introduced in April on 10 Main Board stocks, registered 948 contracts up to July 2006. The lacklustre performance of SSF was attributed to lack of market intermediaries as well as lack of investor knowledge and understanding of the new derivatives product.

Progress of the Capital Market Masterplan

CMP reaches midway point in 2006, with 66% of total recommendations completed...

The **CMP** has reached the midway milestone in 2006 and enters Phase 3 covering the period 2006-2010. As at end-June 2006, a total of 101 recommendations or 66% of the CMP have been completed, with the remaining 51

recommendations still in progress. Phase 2 of the CMP (2004-2005) focussed on strengthening key sectors and gradual liberalisation of market access. Phase 3 of the CMP will focus on measures to further strengthen market processes and infrastructure towards becoming a fully developed capital market, as well as enhance the international positioning of the domestic capital market in areas of comparative advantage. Among others, initiatives in 2006 will continue to emphasise on creating a more facilitative regulatory environment and further enhancing the quality of companies.

Outlook 2007

Monetary policy to ensure growth with price stability, supported by a robust financial market...

Monetary policy in 2007 will continue to emphasise economic growth in an environment of price stability. With the growth momentum expected to be sustained in 2007, the main challenge for monetary policy would be to ensure that inflation expectations are well contained, while financing conditions remain supportive of investment activity. Surveillance by BNM has revealed limited evidence of second-round effects on the general price level and lack of indications of demand-induced inflationary pressures. Nonetheless, monetary policy will continue to be vigilant against inflationary risks. The course of monetary policy will be determined based on the assessment of the implications of new developments and information for the medium-term prospects of both price stability and sustainable economic growth.

Meanwhile, the stronger and more resilient financial sector is well positioned to meet the growing financing needs of the economy, as well as coping with rising competition, following measures taken over the years to strengthen the sector. Continuous efforts will also be taken towards promoting greater vibrancy of the financial sector whilst further enhancing its competitiveness. Malaysia will also continue to leverage on its strengths in Islamic finance to advance the nation as a premier international Islamic financial centre.

UNIT TRUST INDUSTRY IN MALAYSIA

Introduction

Unit trust is an investment instrument that allows individuals to pool their funds to be invested in a portfolio of securities or other assets. A professional fund manager then manages and invests the pooled funds on behalf of the individuals. There is a wide array of unit trust funds for investors to choose, from equities, fixed income, money market to real estate investment trusts (REITs).

Since the establishment of the first unit trust way back in 1959, the Malaysian unit trust industry has grown significantly, supported by the strong growth of the economy and high level of savings. The unit trust industry has expanded from only five unit trust management companies and 18 funds during the period 1959 to 1979, to comprise 36 unit trust management companies, 340 unit trust funds and funds managed totalling RM98.5 billion as at end-2005.

Number of Management Companies, Approved Funds, Total Approved Fund Size and Units in Circulation



¹ Including funds approved but not yet launched.
Source: Securities Commission.

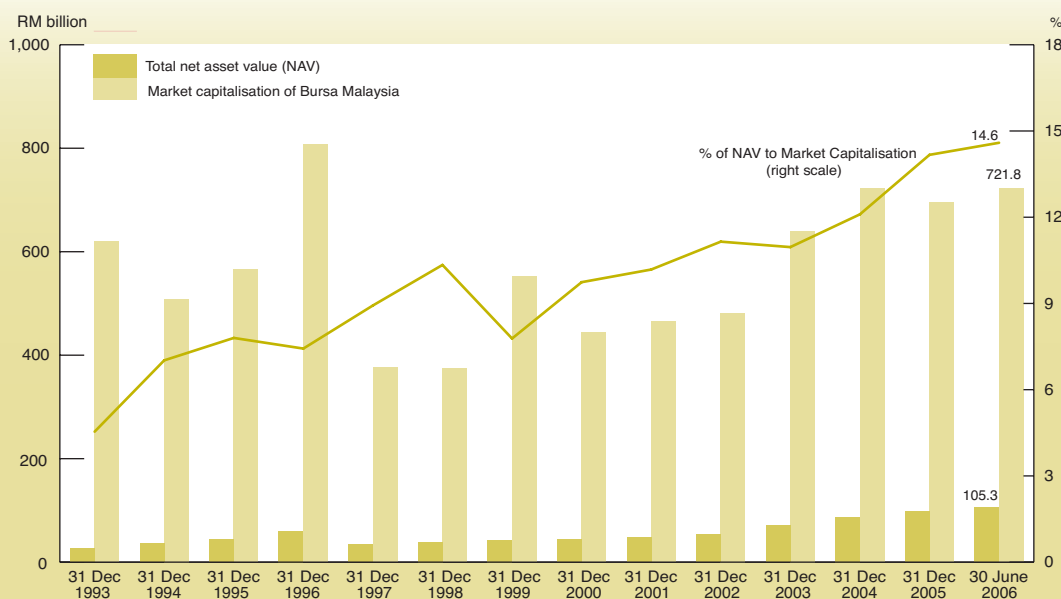
Growth of Unit Trust Industry

The unit trust industry experienced vibrant growth during the period 1993 to 2005. The number of funds approved rose more than seven-fold from 44 at end-1993 to 340 funds at end-2005. The size of the industry in terms of the net asset value (NAV) expanded by 250% from 1993 to RM98.49 billion at end-2005. Investment in equities by unit trust funds constituted the largest portion with RM67.2 billion or 68.2% of total NAV at end-2005, while investments in fixed income amounted to RM10.3 billion or 10.5% of total NAV. The penetration level, as measured by the ratio of NAV of the unit trust industry to equity market capitalisation, improved to 14.2% in 2005 from 4.5% in 1993. However, given the national high savings rate of 37.1% of Gross National Product (GNP), as well as the significant pool of investible assets in excess of RM750 billion

at end-2005, there is huge potential to promote unit trusts as an investment tool. Moreover, a substantial amount of individual savings is deposited with the banking institutions.

Meanwhile, ongoing efforts to promote the development of the Islamic capital market have resulted in the rapid growth of Islamic funds. As at end-2005, there were 83 Islamic funds (2000: 17 Islamic funds) approved by the Securities Commission (SC). The NAV of Islamic funds has also risen to account for 8.6% of total NAV of the unit trust industry as at end-2005 (2000: 3.9%).

Total NAV vs Market Capitalisation



Source: Securities Commission.

Key Initiatives in Promoting the Unit Trust Industry

The centralisation of regulations relating to the unit trust industry with the SC since 1993 has been instrumental in the rapid growth of the industry in Malaysia. Several measures have been taken to promote the development of the unit trust industry. These measures were in relation to the introduction of new products, further liberalisation, widening market participation, improving time-to-market and enhancing investor protection. In January 2005, the previous Guidelines on Property Trust Funds were revised and renamed as the Guidelines on REITs, with the objective to further accelerate the growth of a vibrant and competitive REITs industry in Malaysia. The issuance of the revised REITs guidelines together with tax incentives have spurred interest among industry players and investors in property investments. As at 15 August 2006, eight REITs have been listed on Bursa Malaysia. Total turnover of REITs also rose significantly to RM341.6 million in 2005 from RM11.8 million in 2004. The Guidelines for Islamic REITs were also issued to promote the listing of Islamic REITs. The Guidelines on Exchange Traded Funds also released in 2005 provided a framework for the introduction of a new asset class known as exchange traded funds (ETFs). An ETF is an index tracking unit trust fund listed on Bursa Malaysia. Following the release of the guidelines, the ABF Malaysia Bond Index Fund (ABFM) was introduced as the first ETF in Malaysia.

Further flexibilities were granted for unit trusts to invest abroad, with the threshold raised from 10% to 30% of the total NAV of resident funds effective 1 April 2005. There has been growing interest in offshore investments, following the accord of greater flexibility for unit trust management companies to diversify their portfolios. As at end-May 2006, 24 global funds with total fund size of RM18.49 billion were approved by the SC, with RM4.02 billion invested abroad. Besides global funds, existing unit trust funds have also started to increase their investments in foreign markets.

Recognising the synergies and benefits from enhanced international integration, the Government has allowed five foreign stockbrokers and five global fund managers to operate in Malaysia. To date, five foreign stockbroking companies and one foreign fund management company have commenced operations in Malaysia. The presence of foreign players in the domestic capital market is expected to spur product innovation and enhance competition as well as attract foreign capital. Foreign equity in unit trust management companies was also raised to 49% from 30% to promote greater foreign participation in the industry.

Other key measures include the introduction of a uniform regulatory framework to streamline the licensing rules of the investment management industry, as well as promotion of online transactions and activities of unit trusts. An online unit trust database has also been introduced to help promote investor education and support capital market research. The range of industry players allowed to offer unit trusts was also widened to include licensed fund managers, universal brokers and investment advisers. The time-to-market of unit trust products to investors was further improved in 2005, with SC registering a prospectus for unit trust funds 14 days after receipt of prospectus, which will then be post-vetted. Previously, the prospectus for unit trust funds was pre-vetted and the process could take up to a month to register. The SC also introduced compliance guidelines for fund managers to further strengthen investor protection, which required fund managers to adhere to best practices with regard to trading and portfolio management, safeguarding of clients' assets and compliance with the Anti-Money Laundering Act 2001.

Spurring Further Growth of the Unit Trust Industry

Notwithstanding the tremendous growth of the unit trust industry achieved over the years, there is potential to further grow unit trusts as a viable investment instrument, in view of Malaysia's low penetration level vis-à-vis developed countries, as well as the substantial pool of investible assets that remains locked in individual savings with the banking institutions. In this respect, the unit trust industry should undertake continuous efforts to spur investor interest in unit trusts as a choice investment alternative. The unit trust industry must continue to offer innovative and competitive products to encourage investors to shift funds into unit trusts. Unit trust management companies should adopt and practise high standards of professionalism, particularly of their sales personnel to instil investor confidence in the industry. They must provide efficient and cost-effective services and always strive to ensure maximum returns on clients' investments within the context of appropriate prudential standards and practices. The Government, on its part, will continue to focus on efforts to ensure the growth of the unit trust industry within a well-regulated environment with emphasis on investor protection.

Conclusion

The unit trust industry has expanded significantly on the back of growing interest in unit trusts as a viable investment instrument. There is tremendous potential to further grow the unit trust industry, given the substantial untapped pool of individual savings. While the Government will continue to facilitate the orderly development and growth of the unit trust industry, the industry itself must continually enhance its capacity and capabilities to seize the huge growth opportunities to encourage investors to place their money in unit trusts.

Key Capital Market Measures

Measures focussed on further strengthening the capital market...

Capital market measures introduced in the first six months of 2006 were aimed at further strengthening the capital market and enhancing international competitiveness. The key measures include the following:

Enhancing Price Transparency and Professional Standards in the Bond Market

- On 25 January, the SC issued the Guidelines on the Registration of Bond Pricing Agencies (BPA) to facilitate the introduction of bond pricing agencies. Under the guidelines, a BPA must be registered with the SC to provide independent and objective fair value prices on a daily basis for all ringgit-denominated bonds traded in the over-the-counter (OTC) bond market. This measure will provide reliable and independent fair value prices to fund managers and institutional investors to mark-to-market their bond portfolios on a daily basis.
- On 25 January, a Practice Note on Recognition of Credit Rating Agencies for the Purpose of Rating Bond issues was also released. The practice note provides a set of recognition criteria to ensure that credit rating agencies exercise high standards of professionalism and due diligence in rating and monitoring corporate bonds and Islamic securities, as well as provide adequate and timely dissemination of rating information to the investing public.
- On 24 April, SC released a Practice Note applying the Guidelines on the Offering of PDS to an issuance of commercial papers or a combination of commercial papers and medium-term notes.

Enhancing Quality of Listed Companies

- On 5 May, Bursa Malaysia made several amendments to its listing requirements in relation to the financial condition and level of operations of listed companies. With the amendments, the criteria for classification as a PN17 company have been made more stringent. The amendments are also aimed at expediting the restructuring of financially distressed listed companies and those with inadequate level of operations. The key objectives of the amendments are to enhance the quality of listed issuers and further strengthen investor protection and promote investor confidence.
- On 8 May, Bursa Malaysia issued the revamped MESDAQ Market Listing Requirements (MMLR) to further strengthen and enhance the MESDAQ market. Among others, the key changes under the revamped MMLR include enhanced requirements in relation to corporate disclosure, transparency, corporate governance, post-listing obligations to deter dissipation of assets and maintain capital requirements, as well as quality of MESDAQ companies and related party transactions.
- On 22 June, the SC released a Guidance Note to enhance the listing requirements for domestic companies under the market capitalisation test. Under the new requirements, domestic companies must have market capitalisation of at least RM500 million and after-tax profit of RM30 million for the latest financial year to seek listing on the Main Board.

Enhancing Malaysia's Competitive Positioning Through Further Liberalisation

- On 23 March, SC issued a Practice Note to clarify the application of the Guidelines on the Offering of PDS in relation to the issuance of ringgit-denominated debt securities in Malaysia by a foreign government or agency or organisation of a foreign government. Likewise, a Practice Note to clarify the application of the Guidelines on the Offering of Islamic PDS was issued.
- On 22 June, the SC issued Guidance Notes to facilitate the listing on Bursa Malaysia of foreign-owned corporations having operations abroad as well as secondary listings on foreign stock exchanges of Main Board listed Malaysian companies. The liberalisation would enhance diversity of offerings and promote cross-border linkages. The liberalisation is also expected to heighten the integration of the Malaysian capital market internationally and expand the range of investment opportunities for investors.

Widening the Range of Islamic Capital Market Products

- On 26 June, the SC Syariah Advisory Council approved SSF as a syariah-compliant instrument. SSF was introduced by Bursa Malaysia in April 2006 as a tool for managing share price risk, as well as to facilitate entry to the stock market at a cheaper cost. The SSF provides investors with another Islamic investment alternative.

Accelerating Growth of the Investment Management Industry

- On 7 April, SC released the Guidelines on Restricted Investment Schemes to set out the requirements for fund managers in relation to restricted investment schemes, where funds with a common investment objective are pooled for the purpose of investment. Such arrangements will fall under the ambit of unit trust schemes and require the approval of the SC.
- On 17 May, SC issued a Guidance Note to the Guidelines on Unit Trust Funds to specify provisions with regard to unit trust investments in warrants and options. Among others, the provisions include conditions for investments in options traded OTC, disclosures regarding risk management measures in relation to investments in warrants and options and limits of holdings of unit trust funds in warrants and options. A Guidance Note to the Guidelines on Unit Trust Funds was also issued in relation to unit trust investments in structured products.
- On 25 May, SC introduced an online unit trust database, which includes prospectuses, trust deeds, annual reports, financial statements and directors' reports of all Malaysian unit trust funds issued from 1996 to the present. The online database would help promote investor education as well as support capital market research.
- On 29 May, the SC clarified that fund management companies need not obtain SC's approval for investments in foreign exchanges deemed as "approved foreign markets" by the SC (stock exchanges recognised by Bursa Malaysia Securities Bhd and future exchanges specified under the Futures Industry Act 1993). However, the management company is required to submit a notification on the foreign exchanges that the fund is going to invest in.

Enhancing Liquidity in the Equity Market

- On 26 June, Bursa Malaysia and FTSE group launched Phase 1 of the new FTSE Bursa Malaysia Index Series comprising six indices (FTSE Bursa Malaysia EMAS Index, FTSE Bursa Malaysia Large 30 Index, FTSE Bursa Malaysia Mid 70 Index, FTSE Bursa Malaysia 100 Index, FTSE Bursa Malaysia Small Cap Index and FTSE Bursa Malaysia Fledgling Index). The new index series, which was established using the benchmarks of developed markets, will help enhance the investability and transparency of the domestic equity market.

Enhancing Liquidity in the Derivatives Market

- On 28 April, the first tranche of SSF was launched. The introduction of SSF is significant as it facilitates price discovery, provides an additional risk management tool for investors and also gives investors a lower cost of entering the market. To encourage market uptake of SSF, Bursa Malaysia has waived exchange and clearing fees for the initial three months from the initial launch date as well as waived data feed fees for information vendors for the first 12 months from the launch date.

Increasing the Use of ICT Across Market Segments

- On 6 January, SC released the Guidelines on the Registration of an Electronic Broking System. The guidelines specify the regulatory requirements and procedures to be met by a licensed money broker with regard to an electronic broking system.

Enhancing Shareholder and Investor Protection

- On 26 April, SC issued a set of enhanced guidelines for placements of securities. The guidelines are aimed at promoting greater protection for shareholders and investors as part of continuous efforts to further develop a facilitative regulatory framework for fund raising.
- On 29 May, Bursa Malaysia announced amendments to the Listing Requirements and MMLR in relation to bonus issues. Under the amendments, public listed companies (PLCs) are disallowed from undertaking a bonus issue where the PLCs' accumulated losses exceed the reserves to be capitalised for the bonus issue.
- On 1 July, a RM100 million Clearing Guarantee Fund (CGF) established by Bursa Malaysia became operational. The purpose of the CGF is to deal with potentially large credit or liquidity risks that may arise through the payment or delivery default of its trading clearing participants.