

# Promoting a Progressive and Inclusive Financial System

In 2022, our strategies focused on promoting a financial system that supports a more digitalised, diversified, inclusive, and climate resilient economy. We are guided by the objectives and desired outcomes of the Financial Sector Blueprint 2022-2026.

## Advancing the Digitalisation of Financial Services

During the year, we continued efforts to establish a conducive ecosystem that spurs greater innovation, competition and dynamism. A key part of this is facilitating the entry of new digital-first players into the financial sector. Digital banks offer banking services online without a physical branch network, allowing them to overcome geographical barriers. Digital banks apply innovative technologies, which can include personalised solutions backed by data analytics, without the constraint of legacy systems. Their attention on user experience should also bring more convenience to consumers. Digital banks are expected to focus on underserved and unserved segments, which will advance the financial inclusion agenda and enhance society's participation in the economy. In April 2022, the Minister of Finance granted conditional approval to five digital bank applicants. The digital banks are currently undergoing operational readiness checks and may begin operations by the second quarter of 2024. During the year, digital banks have started appointing their management and Board members, instituting key policies and control procedures, and finalising their digital infrastructure. Digital banks have also engaged independent external parties to

objectively review their state of readiness. The Bank will also conduct an operational readiness review before the digital banks commence operations.

In the same vein as digital banks, new digital insurers and takaful operators (DITOs) may soon enter Malaysia's financial landscape to deliver greater inclusion, market competition, and efficiency, primarily through digital means (Diagram 1). DITOs are expected to achieve this via driving new types of business models and offering wider product choices. In November 2022, the Bank issued an Exposure Draft on the Licensing and Regulatory Framework for DITOs. We sought to introduce licensing requirements that are proportionate to the complexity of DITOs during their initial stage of operations. Similar to digital banks, the newly licensed DITOs will be required to observe a foundational phase and comply with sound risk management and consumer protection requirements. During this period, they would be subject to simplified requirements such as a lower minimum number of Shariah committee members and a lower minimum paid-up capital. The Bank aims to finalise the policy document and invite applications for up to five DITO licences in 2023.

Diagram 1: Value Propositions of DITOs



Source: Bank Negara Malaysia Exposure Draft on the Licensing and Regulatory Framework for DITOs

### The Bank maintains focus on sound risk management and consumer protection for DITO applicants.

We have also revised our policies to better support digitalised business models and solutions. The Exposure Draft on Electronic Know-Your-Customer (e-KYC) was issued in February 2023. It expands on the existing e-KYC requirements to include digital account openings for businesses and individuals. It also aims to help financial institutions (FIs) in adopting the latest technological advancements in e-KYC, while preserving the integrity of the financial system.

The Financial Technology Regulatory Sandbox (Sandbox) remains an important avenue for the financial industry to experiment with new ideas. In 2022, nine solutions were facilitated under the Sandbox. Of this, four new initiatives have been tested, encompassing insurtech and Buy-Now-Pay-Later solutions. Building on these experiences, the Bank will introduce enhancements to the Sandbox framework with an exposure draft expected to be

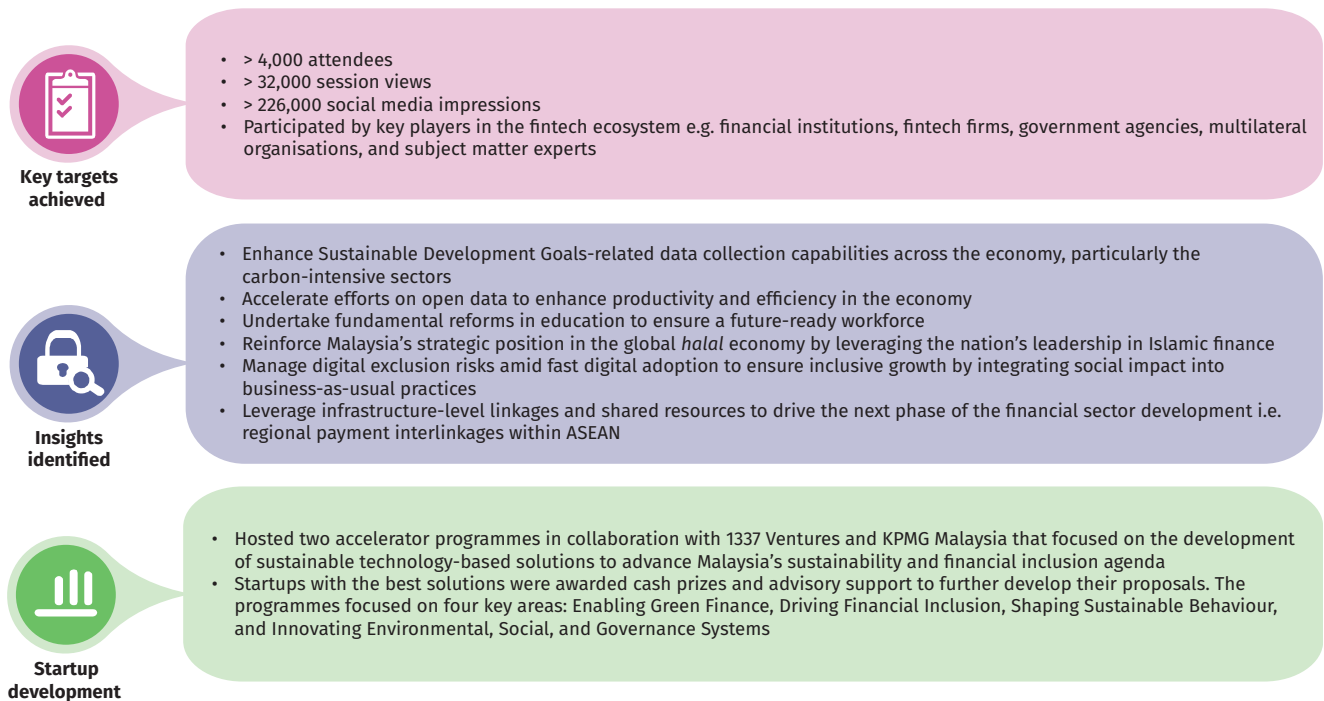
issued in the first quarter of 2023. This will include two key enhancements: (i) accelerating the turnaround time to realise innovations for FIs with strong risk management capabilities; and (ii) simplifying the eligibility assessment for the Sandbox.

We continue to intensify our engagements with the industry and other stakeholders to advance the digital agenda. In January 2022, we hosted the second edition of MyFintech Week. The week-long online event saw over 4,000 participants and speakers participate in opportunities to drive digitalisation for recovery, sustainability and inclusion in Malaysia. Key highlights from the event are further detailed in Diagram 2.

### Deepening Financial Markets

In 2022, we undertook several initiatives to further advance the domestic financial market. These were aimed at improving market access, liquidity, and governance arrangements. The Bank established sub-committees within the Financial Markets Committee<sup>1</sup> (FMC) dedicated to the development of the domestic bond financial markets and Islamic financial markets.

Diagram 2: MyFintech Week 2022



Source: Bank Negara Malaysia, adapted from a publication by EY

<sup>1</sup> The Financial Markets Committee was established in 2016 to engage with the financial market industry and to review and formulate comprehensive strategies for the wholesale financial markets.

Malaysia continues to adopt a multiple-rate approach, with the Kuala Lumpur Interbank Offered Rate (KLIBOR) and Malaysia Overnight Rate running in parallel. As such, we have maintained the publication of one-, three-, and six-month KLIBOR tenors to provide market participants the flexibility to price financial products based on an active underlying market. The Bank also re-appointed 11 KLIBOR submitters for 2023-2024. Guided by the KLIBOR Rate Setting Policy Document issued in September 2021, these submitters will ensure KLIBOR remains robust and representative of conditions in the underlying market.

Principal Dealers (PDs) are critical in ensuring the stability and development of the financial markets. PDs help to build a stable and dependable source of demand for securities. They provide liquidity in the secondary market by devoting capital resources to absorb an occasional shortfall in liquidity. They also build distribution channels and provide market information which includes prices, volumes, and spreads between bids and offers. In 2022, the Bank reviewed the Principal Dealership Framework to ensure its relevance. Key enhancements to the Principal Dealership Framework include a greater focus on financial market development, increased incentives for contributing to market liquidity and transparency, and the promotion of healthy competition.

## Enhancing Access to Financial Products and Services

### **Enhancing financial access points**

Agent banks are an important element in achieving our financial inclusion goals. They provide convenient access to essential financial services, particularly for remote communities. These services include cash deposits and withdrawals, fund transfers, bill payments, and prepaid top-up transactions. In June 2022, the Bank revised its Agent Banking Policy Document to expand the scope of financial services offered by agent banks. Agent banks can now facilitate the opening of banking accounts via e-KYC protocols, undertake money services business, distribute microinsurance and microtakaful products, and conduct e-money cash-in and cash-out activities. The expanded scope of agent banks is expected to have sizable positive effects on financial inclusion in Malaysia (Diagram 3).

Agent banks are now available in almost all *mukim* (sub-districts) in Malaysia.

In addition to existing agent banks, the Bank collaborated with the industry to introduce the Bank Bergerak Initiative. Mobile banks (*bank bergerak*)<sup>2</sup> have helped to widen access to essential banking services in underserved areas, including providing advisory services<sup>3</sup> and catalysing the adoption of digital financial services. As at end-2022, a total of 19 mobile banks have been deployed, covering 39 underserved *mukim* in seven states in Malaysia. Mobile banks facilitated the opening of more than 3,182 new banking accounts and over 31,970 transactions valued at RM29.5 million.

### **Ensuring continuous access to finance for businesses and entrepreneurs**

Malaysian FIs continue to support the recovery of small and medium enterprises (SMEs) by providing needed financing. This helps SMEs manage cashflow needs and make capital investments to expand their businesses. As at end-2022, outstanding loans and financing from the banking system to SMEs expanded by 5.0% (2021: 5.7%)<sup>4</sup>. More than RM154 billion in financing was approved for about 230,000 SME accounts (2021: RM131 billion to about 196,000 accounts). Disbursement activity recorded double-digit expansion, with a total of RM505 billion channelled to SMEs (2021: RM399 billion).

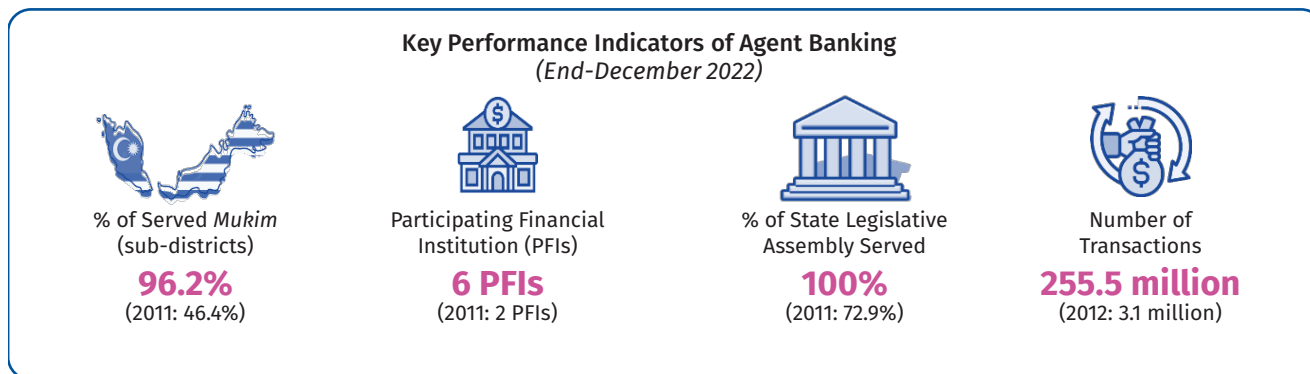
To support SMEs impacted by nationwide floods during the year, the Bank activated the Disaster Relief Facility 2022 (DRF 2022). The DRF 2022 provided urgent financing for SMEs to mitigate the fallout from the floods. Such financing was used for repairs and replacement of damaged assets, such as plants and machinery, and any additional working capital. As at end-December 2022, participating FIs approved over RM200 million under DRF 2022 in financing to support more than 500 SMEs and microenterprises.

<sup>2</sup> In June 2021, the Government announced an RM18 million allocation for the Bank Bergerak Initiative under Pakej Perlindungan Rakyat dan Pemulihan Ekonomi (PEMULIH). The objective was to enhance access to basic banking services in underserved areas with limited financial access points across Peninsular Malaysia, Sabah, and Sarawak.

<sup>3</sup> The financial advisory services provided by mobile banks include raising awareness of digital financial services and financial scams, on-boarding to digital financial services by downloading FIs' mobile banking app, and explaining the benefits of various financial products, including insurance/takaful, particularly Perlindungan Tenang, etc.

<sup>4</sup> All loan/financing data from the banking system and development financial institutions are based on updated statistical reporting requirements and may not be directly comparable to the data reported in previous publications.

Diagram 3: Agent Banking Services in Malaysia



Source: Bank Negara Malaysia

BNM’s Fund for SMEs (BNM’s Fund) further complements the banks’ effort to support SMEs’ financing needs. We also aim to incentivise and crowd-in private financing into identified new growth areas. During the year, BNM’s Fund underwent changes to more firmly support SMEs’ recovery and future growth. In February 2022, we introduced two new funds. The Business Recapitalisation Facility assists SMEs in restructuring or increasing their working capital funding, while the Low Carbon Transition Facility supports SMEs in transitioning to low carbon and sustainable operations. The High Tech Facility – National Investment Aspirations was also enhanced and rebranded as the High Tech and Green Facility. This is aimed to support eligible SMEs to make investments that can help spur economic growth, particularly in areas such as digital technology, green technology, and biotechnology.

With these additional and enhanced financing facilities, the total financing available through BNM’s Fund increased to RM31.1 billion in 2022 from RM9.1 billion in 2019. In 2022, RM22.6 billion (2021: RM19.4 billion) of financing was approved for more than 65,000 (2021: 53,000) SMEs, with disbursements amounting to RM20.1 billion (2021: RM16.4 billion). See Diagram 4 for further details on the type of facilities available under BNM’s Fund.

Social finance is envisioned to be a key driver of social development in Malaysia. It complements public sector finance and commercially driven financial solutions to promote greater social resilience. One example is iTEKAD<sup>5</sup>. Since its pilot

phase in 2020, the number of participants and business sectors has steadily grown. In 2022, the iTEKAD programme expanded to include nine participating banks, up from three in the previous year. Together with their implementation partners, these banks have committed to onboard more than 4,000 new iTEKAD participants and mobilise almost RM40 million of diverse social finance funds (including donations, zakat, and social impact investment) in 2023. iTEKAD has delivered tangible benefits to its participants. This includes improvements in business growth, sustained employment, financial resilience, and digital adoption. (See Diagram 5)

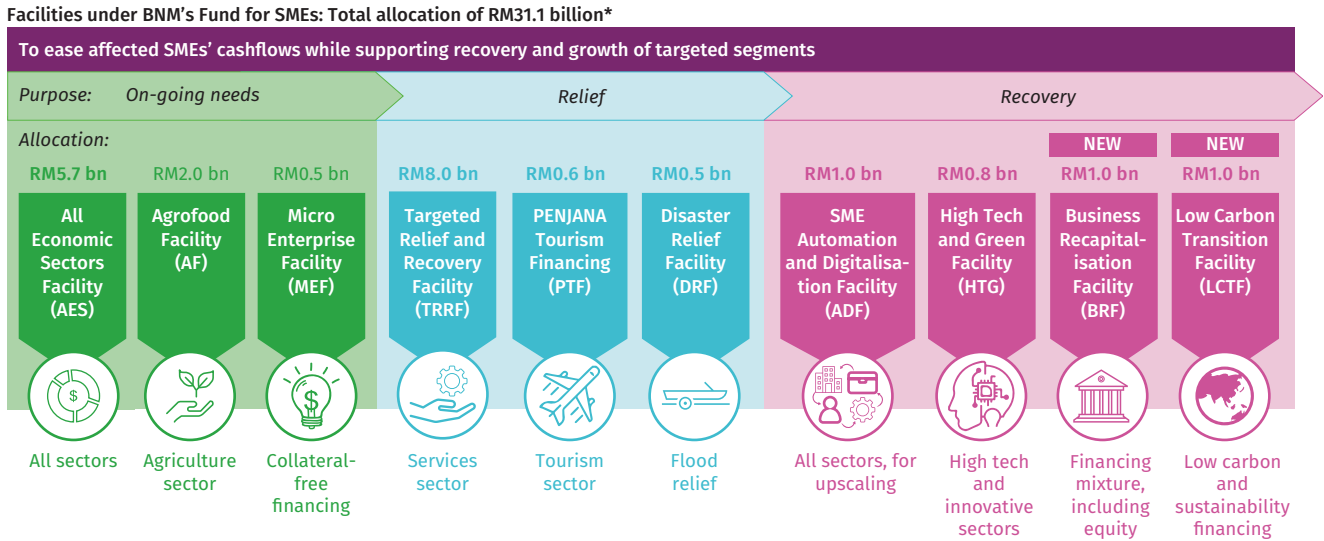
The launch of iTEKAD has provided the Bank and FIs with many valuable insights. Given the increasingly important role of social finance, FIs will need to deploy comprehensive strategies along the social finance value chain, from onboarding participants, upskilling participants, funding, and impact monitoring to realise its full potential (Diagram 6). The Bank, on its part, will continue to play an active role in supporting the industry to broaden the outreach and success of social finance programmes like iTEKAD.

**Promoting inclusive financial product offerings**

Insurance and takaful protection can provide valuable support in times of need, especially for households or individuals with insufficient savings and financial buffers. Perlindungan Tenang (PT) products provide protection against unexpected financial losses and adverse life events. It meets the

<sup>5</sup> iTEKAD is a blended social finance programme which provides seed capital, structured training and microfinancing. iTEKAD targets low-income segment of aspiring and existing microentrepreneurs.

Diagram 4: List of Facilities Under BNM’s Fund for SMEs



\*RM10 billion allocated for Special Relief Facility has been fully utilised and closed for application

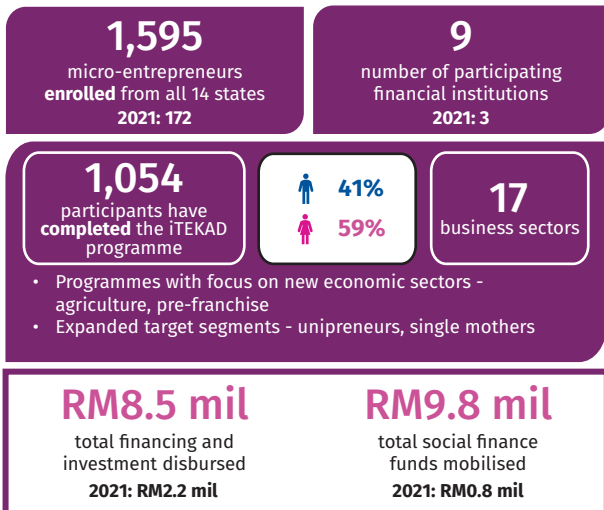
Source: Bank Negara Malaysia

Diagram 5: Key Performance Indicators of iTEKAD

## ACHIEVEMENTS IN 2022

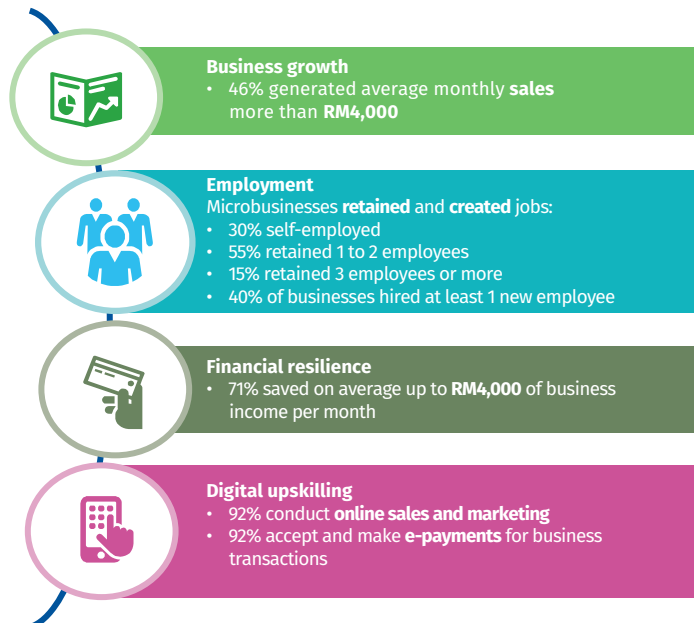
### Key Performance Indicators of iTEKAD

Expansion of iTEKAD through collaboration between participating financial institutions and implementation partners resulted in:



### Key Impact Indicators from iTEKAD microentrepreneurs

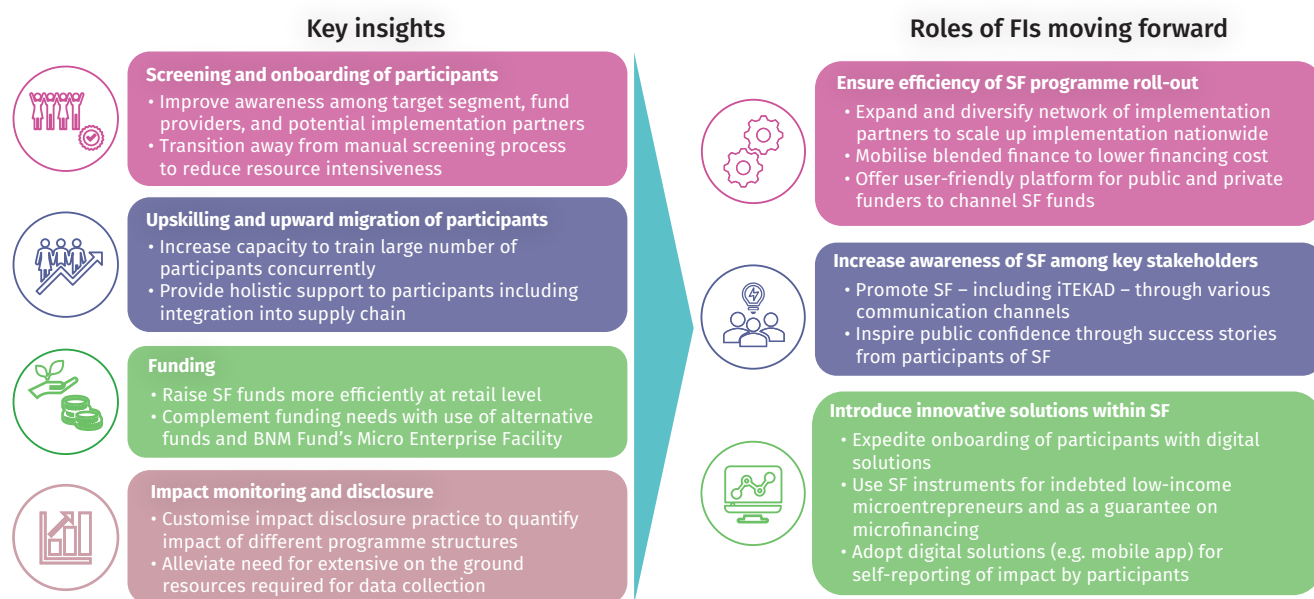
Impact among iTEKAD participants are tracked through four key dimensions:



Note: Figures are derived from sample of iTEKAD participants.

Source: Bank Negara Malaysia, participating financial institutions of iTEKAD

Diagram 6: Opportunities for Optimisation Along the Social Finance (SF) Value Chain



Source: Bank Negara Malaysia

principles of being affordable, accessible, provides good value, and is easy to understand, buy, and claim. In 2022, the PT initiative grew significantly (Diagram 7) with 4.9 million insurance policies/takaful certificates purchased (2021: 1.7 million) and RM12.4 million in claims paid (2021: RM10.2 million). This was enabled through a fit-for-purpose regulatory framework and the Government's Perlindungan Tenang Voucher (PTV) programme<sup>6</sup> introduced since 2021. The PT regulatory framework encouraged insurers and takaful operators (ITOs) to diversify both their product offerings to encourage general products, and distribution channels to include non-traditional channels. This improved consumer choice and accessibility to PT products. The Government's PTV programme encouraged vulnerable groups to purchase and experience insurance and takaful protection, which they otherwise might not have been interested in.

The PTV programme has highlighted the importance of good sales practices, particularly by intermediaries. Some ITOs had gaps in their oversight over distribution partners who interfaced with PTV recipients. This has resulted in complaints on unauthorised voucher redemptions from consumers. These ITOs were required to undertake remedial actions and conduct more robust due diligence of their PT partners prior to appointment. They were also required to ensure more effective

monitoring and quality checks on sales practices, customer onboarding, and disclosure processes of their PT partners.

A demand-side study to support the future growth of a sustainable microinsurance and microtakaful market was completed in 2022. Jointly commissioned by the Bank and the insurance and takaful industry, the study provided greater insights on the protection needs and consumption behaviours of three emerging segments in Malaysia – gig workers, young millennial families, and sales and services workers (Diagram 8). To complement the demand-side study, macro data on the mySalam<sup>7</sup> scheme's experience with hospitalisation and critical illness claims were shared with ITOs. This provided ITOs with a better understanding of claims behaviour amongst the typical target segments of the microinsurance and microtakaful market. Such information will facilitate ITOs in designing and introducing more needs-based microinsurance and microtakaful products. It will also help ITOs to develop suitable consumer education programmes to sustain future demand.

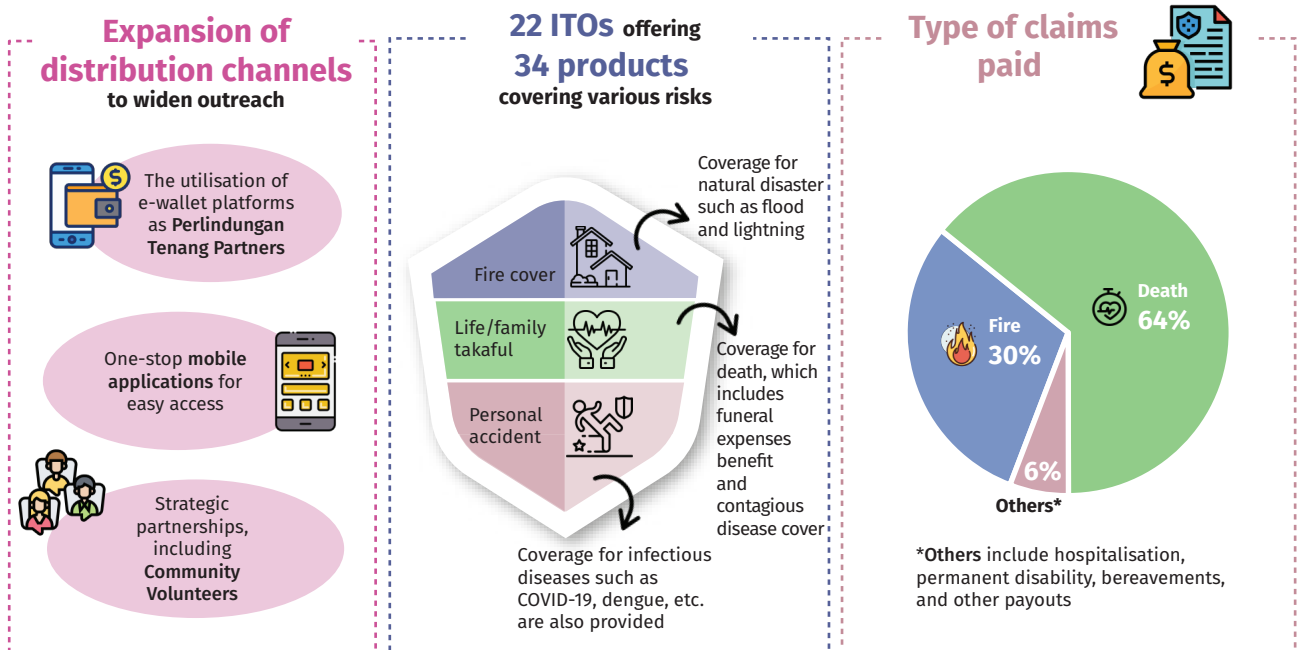
**Development financial institutions (DFIs) as key enablers to enhance inclusivity and access to financing**

In 2022, outstanding DFI financing grew by 1.1% to RM163.4 billion (2021: 3.6% to RM161.6 billion), mainly in the household, construction, and manufacturing

<sup>6</sup> PTV programme provides eligible Bantuan Keluarga Malaysia recipients with a RM50 voucher in 2021 and RM75 voucher in 2022 to purchase or renew PT products.

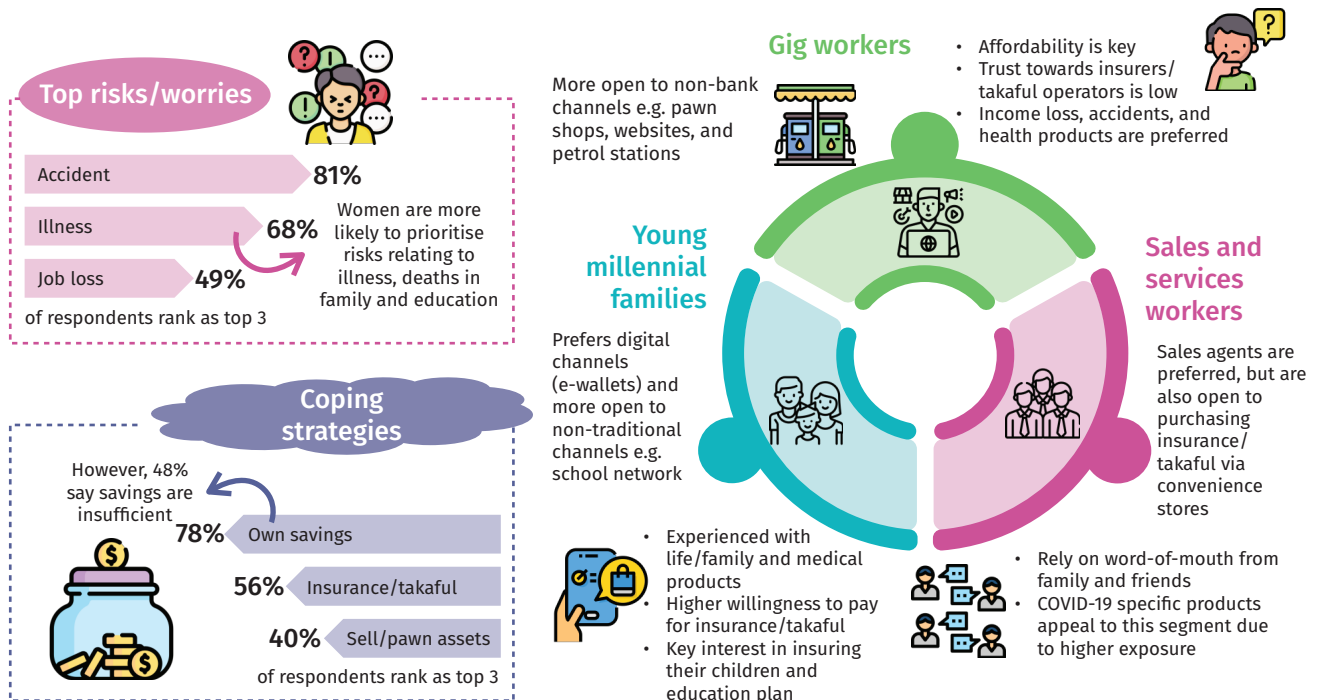
<sup>7</sup> mySalam is a free takaful income assistance scheme by the Government which provides takaful protection for eligible individuals, including individuals who receive special government assistance payments.

Diagram 7: Performance of Perlindungan Tenang



Source: Insurance Services Malaysia

Diagram 8: Key Outcomes from a Demand-side Study Jointly Commissioned by the Insurance/Takaful Industry and the Bank



Source: Bank Negara Malaysia

## Promoting a Progressive and Inclusive Financial System

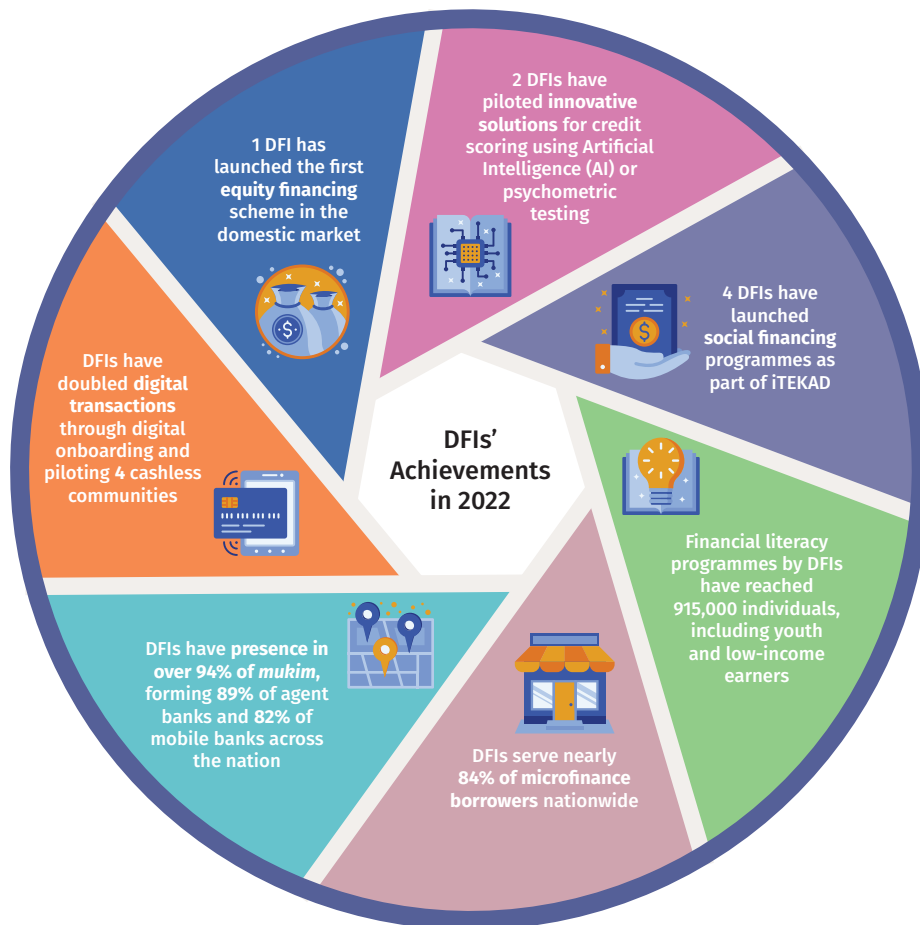
sectors. New financing approved by DFIs grew markedly by 16.3% (2021: -2.4%), which reached 630,000 low-income borrowers and 31,000 SMEs, including start-ups and first-time borrowers. DFIs also remain as the main credit provider for microenterprises, constituting 84% of total microfinance accounts. Supported by financing from DFIs, over 10,000 businesses achieved higher turnover and about 3,700 businesses upscaled its operations, creating and retaining an estimated 131,000 jobs in the economy in 2022. Other key achievements of DFIs are summarised in Diagram 9 below.

During the year, the Bank supported DFIs in their efforts to innovate products and develop solutions that bridge gaps in financial inclusion. We facilitated regular engagements between DFIs and fintech companies. This was to encourage exploration of solutions to instil a savings habit, provide equity financing, and enhance credit assessment methods for “thin-file” customers using Artificial Intelligence/ Machine Learning or other credit scoring methods

(e.g. psychometric analysis). We also facilitated DFIs in launching social finance programmes through iTEKAD to extend reach to underserved segments.

To improve the impact and effectiveness of DFIs in promoting financial inclusion, we focused on the implementation and enforcement of the Performance Measurement Framework (PMF) introduced in 2018 (Diagram 10). We worked closely with DFIs to refine their PMF-related governance, systems, and resources. This resulted in improved reporting of baseline impact indicators by DFIs and more meaningful application of PMF to track long-term developmental outcomes. This enabled the Bank to provide more holistic interventions where needed. The PMF also prompted DFIs to take proactive action to enhance its outreach and crowd-in private sector financing for underserved industries (e.g. new growth areas, microenterprises, social enterprises, green financing) and borrower segments (e.g. vulnerable segments, “thin-file” customers).

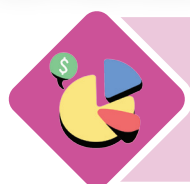
**Diagram 9: Snapshot of Development Financial Institutions (DFIs) Achievements in 2022**



Source: Bank Negara Malaysia

## Diagram 10: Four Additionalities Monitored Under the Performance Measurement Framework (PMF)

One of the core result areas of the PMF is additionality creation, which is the increase in social value that would not have occurred under a fully commercial environment.



### Financial additionality

DFIs' contribution towards closing financing gaps, providing countercyclical financing, and other support to strategic sectors and underserved segments, e.g. increase in the value of financing approved to first-time borrowers.



### Demonstration additionality

DFIs' contribution in building private sector capability by demonstrating the growth potential of target segments to attract private sector investments, e.g. increase in value of financing crowded-in through guarantees or syndicated loans.



### Design additionality

DFIs' contribution towards socio-economic development and building customer resilience using impactful design features, e.g. increase in the number of customers that have improved their business resilience.



### Policy additionality

DFIs' contribution towards public policy design and public sector capabilities, e.g. proposal for state governments to develop the digital infrastructure in an unserved area to enable the delivery of financial services to the local community.

Source: Bank Negara Malaysia

### Catalysing structural reforms

During the year, the Bank worked closely with the financial industry and other stakeholders to introduce key reforms for the Malaysian insurance and takaful sector. These reforms are designed to promote positive consumer outcomes. The commitment of diverse stakeholders is required to ensure these reforms are implemented successfully and are effective in delivering a better consumer experience.

The general ITOs have committed to the vision of establishing an end-to-end digital motor insurance and takaful claims settlement system by end-2026. Almost all general ITOs are committed to implement the first phase of reforms, namely to have digital roadside assistance solutions by end-2023. Information on the Bank's motor reforms journey is featured in the article "Driving into the Future-A Digital Motor Claims Journey". These reforms will enhance customer experience and confidence, reduce claims leakages and fraud, as well as pave the way for the continued liberalisation of motor and fire tariffs.

The Bank is steadfast in pursuing structural reforms within the medical and health insurance and

takaful (MHIT) industry. This is in tandem with the Minister of Health's efforts to pursue broader reforms that will improve Malaysia's healthcare system. Our objective is to ensure MHIT protection remains accessible and sustainable in the long run. To this end, we issued an Exposure Draft on MHIT Business in December 2022. The Exposure Draft sets out prevailing expectations for ITOs to observe fair and responsible business conduct practices towards consumers. The Exposure Draft also proposes for ITOs to develop MHIT products with cost-sharing element to counter rising claims inflation and maintain affordability of premiums. The Exposure Draft recommends ITOs to enhance the collection and standardisation of MHIT claims data to support better cost control management and transparency of MHIT cover. This is further supported by digital solutions such as a MHIT claims data exchange platform to be developed and piloted by the industry in 2023. The platform will enable greater industry-wide claims analysis and pave the way forward for the future publication of healthcare costs, which can enable consumers to make easier cost comparisons and informed choices.

## Going Forward

In 2023, the Bank will continue to ensure that the Malaysian financial sector remains progressive in responding to emerging market developments and inclusive in serving the existing needs of the nation. Our initiatives will be consistent with developmental and regulatory priorities outlined in the Financial Sector Blueprint 2022-2026.

The digitalisation of financial services will accelerate as technological advancements continue to grow. The Malaysian financial sector must continue to meet milestones in its ongoing digital transformation journey. In support of this, the Bank will be finalising the licensing framework for DITOs and preparing for the commencement of operations of the country's first five digital banks.

The strength of the national digital infrastructure sets the foundation for the digitalisation of financial services. Hence, advancing the development of the digital infrastructure in Malaysia will have cross-

sectoral and nationwide benefits. This includes efficiency gains to both financial consumers and businesses alike who utilise digital financial services. We will carry on working with FIs and relevant government agencies to pilot more open data use cases. At the same time, we will also continue to advocate the implementation of a National Digital Identity framework.

An inclusive financial sector helps to foster financially strong and resilient households, communities, and economy. It is therefore critical to set out a clear vision for advancing financial inclusion strategies. Efforts are ongoing to engage stakeholders for feedback on the Discussion Paper on the Financial Inclusion Framework 2023-2026 (FIF). Following this, we plan to finalise the second edition of FIF later this year. The FIF outlines medium-term initiatives to elevate the financial well-being and standard of living of Malaysians. This includes clarifying ways to ensure public access to affordable financial solutions and empower consumers to make sound financial decisions.

## Driving into the Future - A Digital Motor Claims Journey

In 2022, the Bank continued to call on general insurers and takaful operators (ITOs) to improve customers' claims experience and outcomes by going digital. This is in line with aspirations set out in the Bank's Financial Sector Blueprint 2022-2026.

### Why go digital?

There are various pain points in the motor insurance and takaful claims process in Malaysia. At the scene of an accident or vehicle breakdown, consumers may be exposed to harmful practices. Unsolicited parties who show up at an accident scene often take advantage of accident victims by pressuring them to allow their vehicles to be towed away without notifying the relevant ITOs, or deal with unknown parties to handle aspects of the claim. Victims may be made to pay fees for these actions. Damaged vehicles towed to workshops of unknown reputation also raise safety concerns from the use of non-genuine parts or sub-standard repairs. These unhealthy practices will ultimately contribute to greater risks of insurance fraud and exaggerated claims due to inflated costs of repairs and parts. Additionally, manual claims processes have often led to long turnaround times to approve and settle claims. Digital solutions like web or mobile apps can address many of these issues. By linking each party within the claims process, digitalisation can provide consumers a more efficient and seamless experience.

### Towards a transformative customer experience

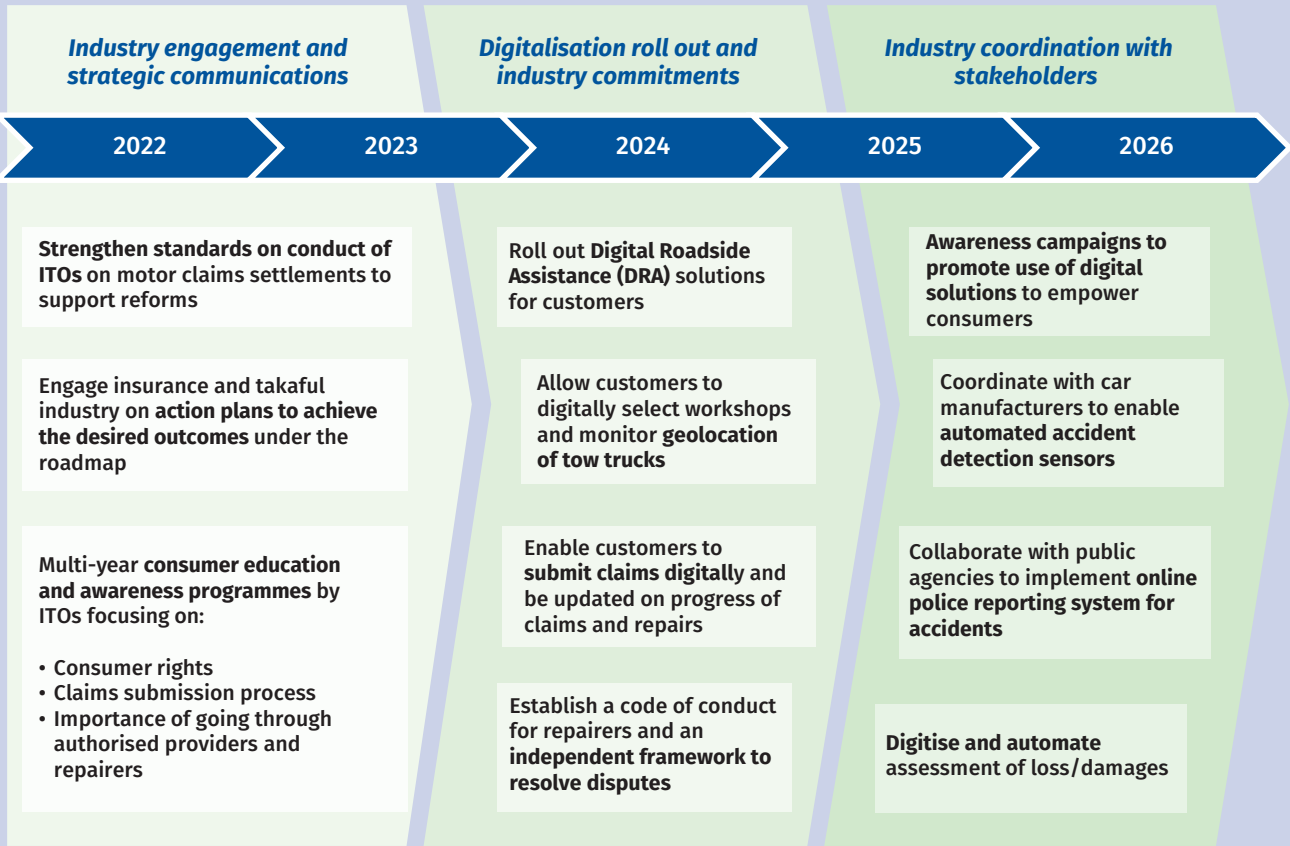
Collaboration both across ITOs and with key parties in the claims value chain is crucial to reshape an end-to-end digital motor claims journey. The desired outcome is a faster, more transparent and better claims experience for customers. To this end, a five-year digitalisation roadmap (2022-2026, Diagram 1) has been rolled out for the insurance and takaful industry to complement efforts to transform the motor claims ecosystem. The Bank continues to engage and work collaboratively with stakeholders, including insurtechs<sup>1</sup>, relevant government agencies and authorities, consumer groups and service providers, in pursuing the key initiatives outlined under the roadmap.

### What can consumers expect?

ITOs are anticipated to deliver more innovative value propositions to their customers. Between 2023 and 2024, most ITOs are expected to deploy Digital Roadside Assistance (DRA) solutions via the web and mobile apps. This will enable consumers to conveniently manage all aspects of their claims journey (Diagram 2) digitally – from notifying an ITO of the accident to receiving the repaired vehicle. Amongst ITOs, greater use of technology such as telematics, data analytics and process automation will further improve the speed, efficiency and accuracy of claims processes, while better controlling fraud. For instance, telematics can notify ITOs automatically when an accident occurs and help initiate the claims process for the consumer. Efforts by ITOs to educate consumers on DRA and encourage its usage will also be ramped up to improve customers' awareness and capability in managing claims processes.

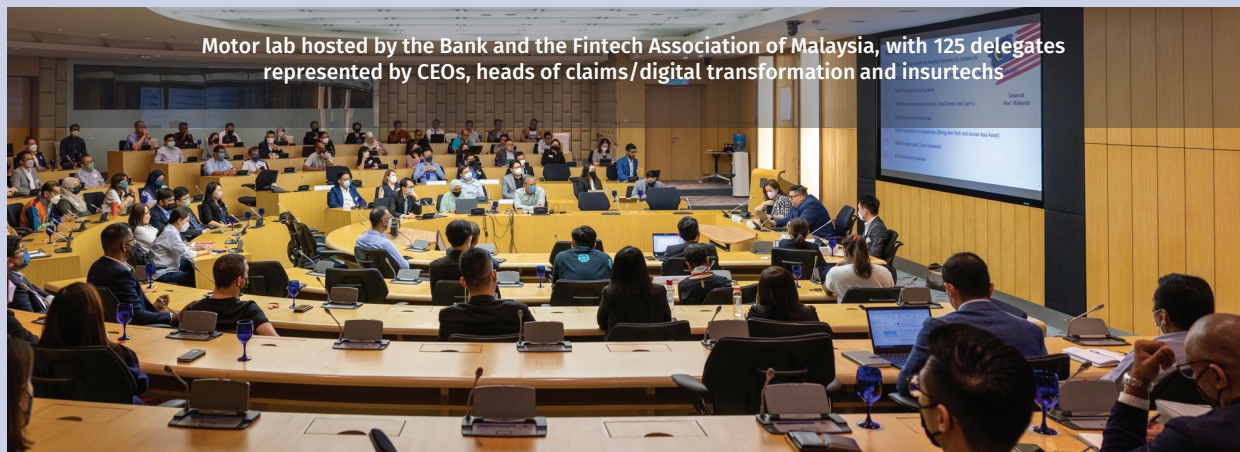
<sup>1</sup> Insurtech is a combination of the word "insurance" and "technology". It refers to the innovative use of technology to improve business processes, efficiency and customer experience in the current insurance and takaful business model including administration, underwriting, distribution and claims.

Diagram 1: A 5-year Roadmap for the Motor Insurance and Takaful Claims Ecosystem



**Desired outcomes**

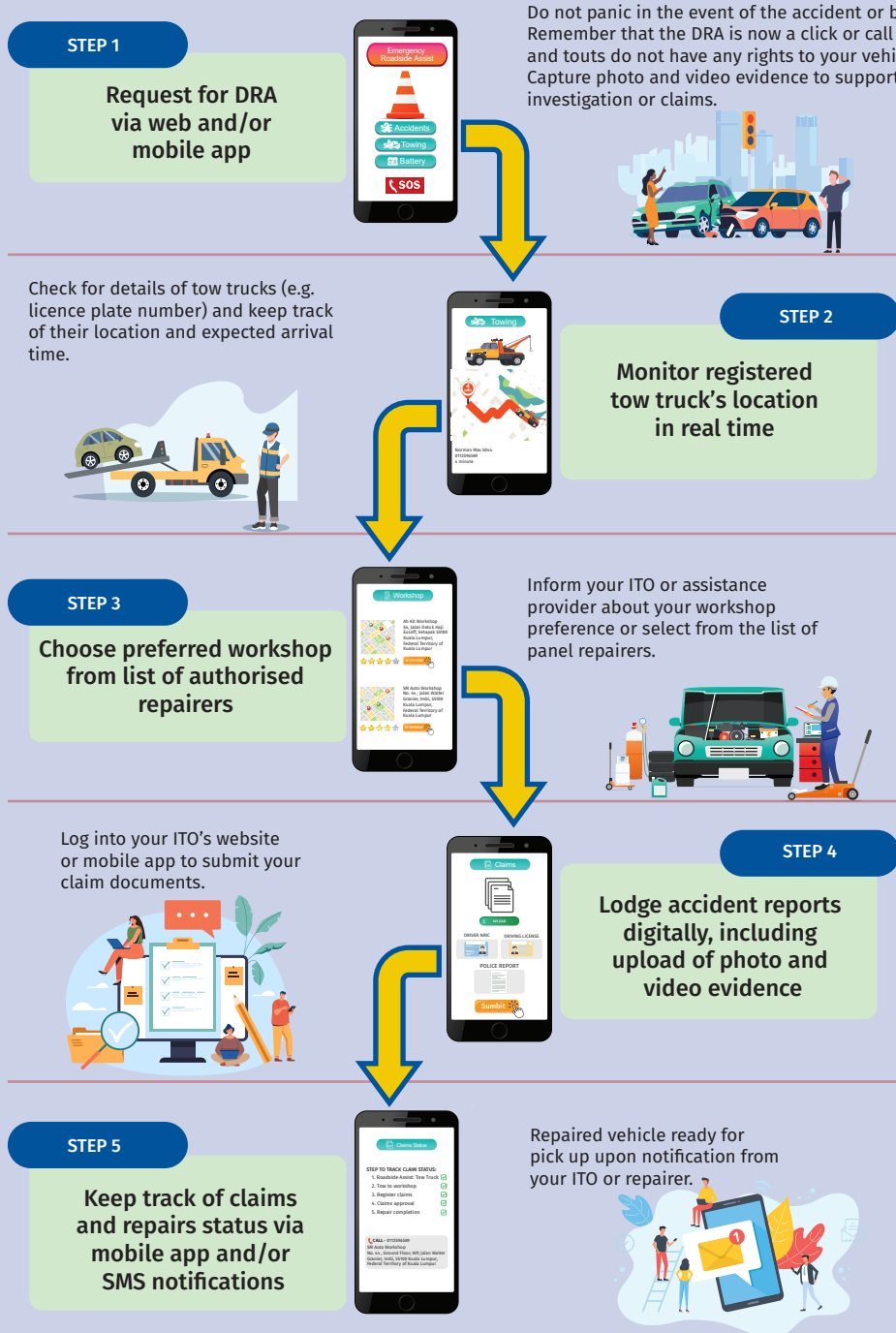
<p><b>Timeliness</b></p>	<p><b>Transparency</b></p>	<p><b>Transformative Customer Experience</b></p>
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Motor lab hosted by the Bank and the Fintech Association of Malaysia, with 125 delegates represented by CEOs, heads of claims/digital transformation and insurtechs

Source: Bank Negara Malaysia

Diagram 2: Customer Journey for an End-to-end Digital Motor Claims Process via a Mobile App



Note: The above diagram is for illustration only. The actual user interface may vary across participating ITOs.

Source: Bank Negara Malaysia