

Monetary and Financial Developments

HIGHLIGHTS

- The ringgit appreciated while bond and equity markets improved.
- Interest rates declined further following the reduction in the OPR.
- Financing expansion was supported by household loans.

Continued improvement in domestic financial market conditions as global risk appetite increased

Chart 19: Performance of Regional Currencies Against the US Dollar

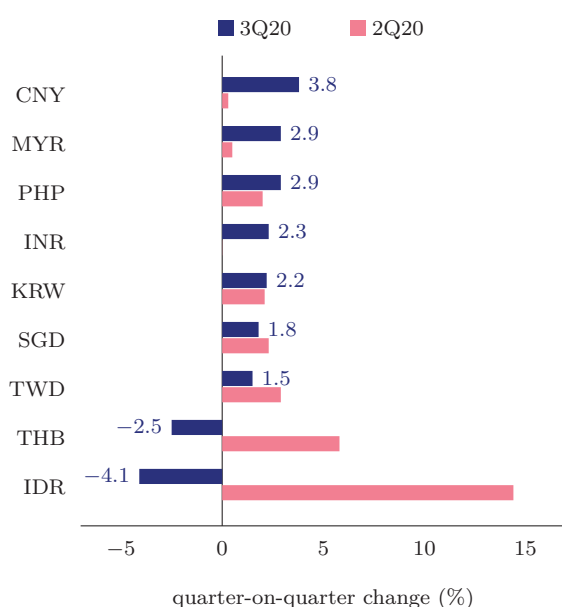
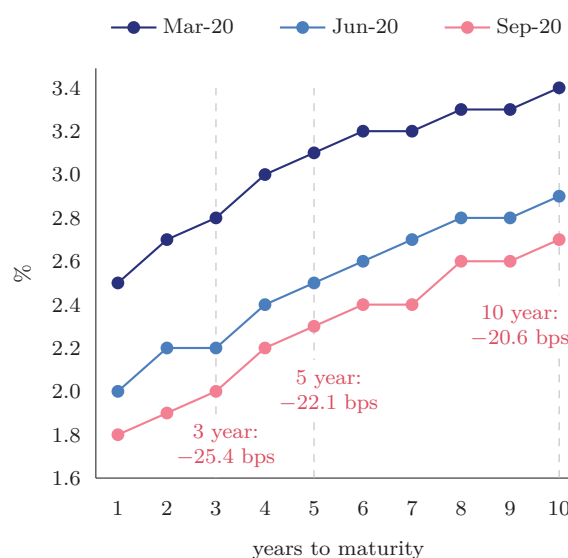


Chart 20: Trend in MGS Yields

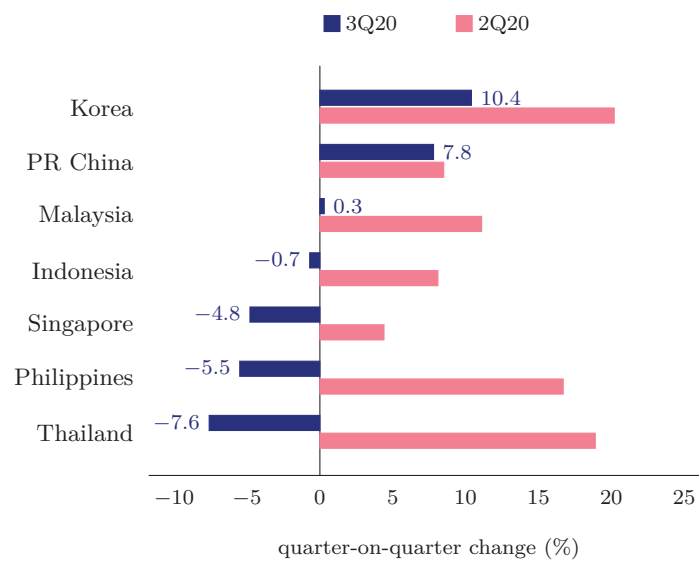


Source: Bank Negara Malaysia

Domestic financial market conditions continued to improve during the third quarter of 2020, driven by positive investor sentiments following signs of recovery in global economic activity as countries eased movement restrictions and progressively restarted their

economies. Improvements in investor risk appetite were also supported by the US Federal Reserve's changes to its monetary policy framework, which suggests that US monetary policy could remain accommodative for a longer period.

Chart 21: Performance of Regional Equity Markets



Source: Bloomberg

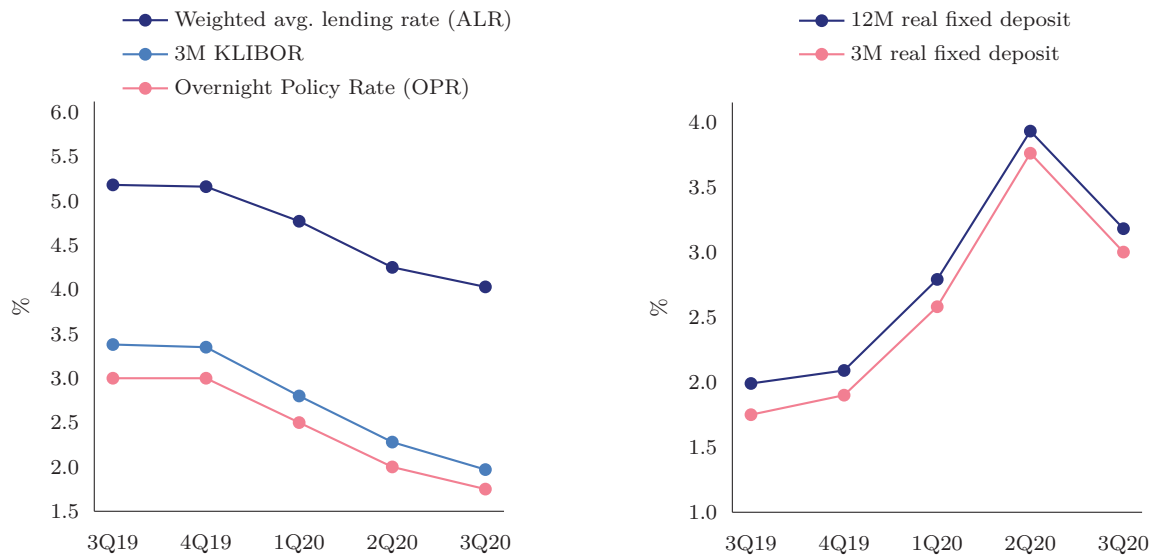
Consequently, regional financial markets including Malaysia exhibited broad-based improvements across asset markets. During the third quarter, the domestic bond market continued to experience non-resident portfolio inflows, which led to an appreciation of the ringgit against the US dollar by 2.9%, in line with most regional currencies. These inflows partly contributed to the decline of the 3-year, 5-year and 10-year MGS yields by 25.4, 22.1 and 20.6 basis points, respectively. The lower yields also reflected the further reduction in the Overnight Policy Rate (OPR) in July 2020 by 25 basis points.

The performance of domestic equity markets, however, only improved marginally during the quarter. While

the better-than-expected releases of economic data, mainly from the US and PR China, supported the increase in regional stock indices earlier in the quarter, the global equity market correction in September affected regional equity indices and reversed the earlier gains. The correction was triggered by concerns on the potential materialisation of risk events, which included the implementation of another round of movement restrictions in Europe and the failure to pass a new US fiscal stimulus bill amid the ongoing political gridlock. Domestically, announcements of subdued second quarter corporate earnings by selected large companies in the main board also affected domestic equity markets. As at end-September, the FBM KLCI increased by 0.3% to close at 1,504.8 points (end-June: 1,501.0 points).

Interest rates declined further following the reduction in the OPR in July 2020

Chart 22: Interest Rates (at end-period)



Source: Bank Negara Malaysia, Bloomberg

Interest rates in the wholesale and retail markets declined during the quarter following the reduction in the OPR by 25 basis points in July 2020. There was strong and immediate pass-through of the OPR reduction to interbank rates across all tenures, with the KLIBOR declining by 25 basis points across tenures within one day of the OPR adjustment. During the rest of the quarter, nominal interest rates in the wholesale market declined marginally. In particular, the 3-month KLIBOR declined by another 6 basis points to 1.97% (2Q 2020: 2.28%).

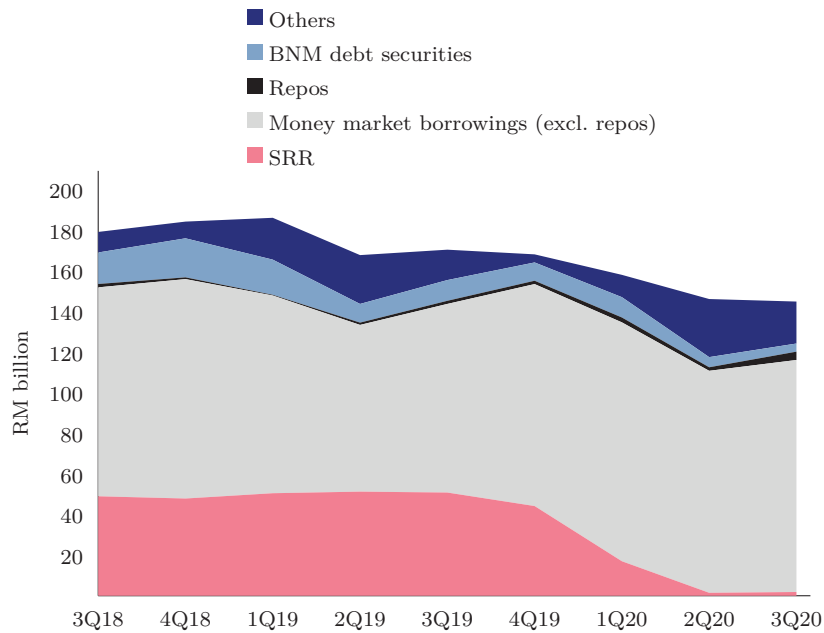
The transmission of OPR to base rate (BR) was also strong, with all banks revising their BRs downwards

by 25 basis points, resulting in the current weighted average of 2.43% (2Q 2020: 2.68%). Correspondingly, the weighted average lending rate (ALR) on outstanding loans declined by 22 basis points to 4.03% in September (2Q 2020: 4.25%).

Similarly, nominal fixed deposit (FD) rates also decreased during the quarter, across tenures of 1 to 12 months, following the OPR reduction. Real FD rates decreased given the decline in nominal rates and the less negative inflation in September.

Banking system liquidity remained sufficient to facilitate financial intermediation

Chart 23: Outstanding Ringgit Liquidity placed with BNM (at end-period)



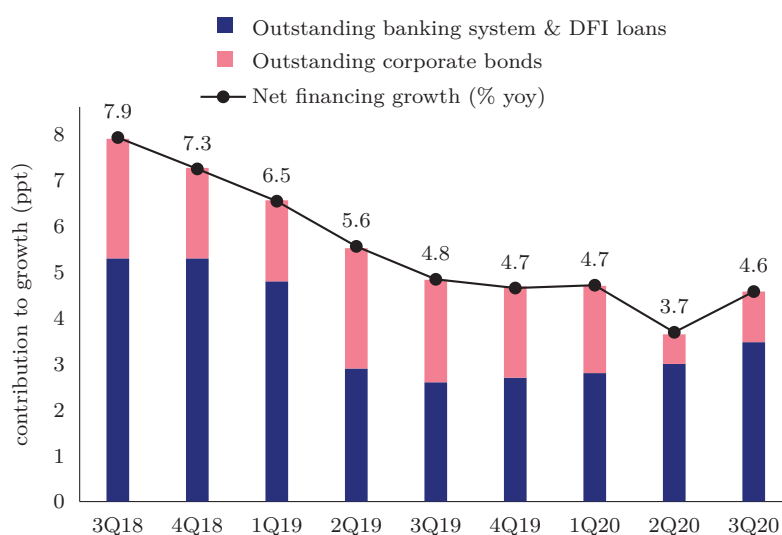
Source: Bank Negara Malaysia

The volume of surplus liquidity placed with the Bank remained broadly stable during the quarter. Total banking system liquidity remained sufficient to facilitate

financial intermediation. At the institutional level, almost all banks continued to maintain surplus liquidity positions with the Bank.

Financing expansion supported by household loans

Chart 24: Contribution to Net Financing Growth



Source: Bank Negara Malaysia

In the third quarter of 2020, net financing expanded by 4.6% on an annual basis (2Q 2020: 3.7%). Outstanding loan⁵ growth increased during the quarter (4.7%; 2Q 2020: 4.1%), supported mainly by household loans. Outstanding corporate bond⁶ growth (4.3%; 2Q 2020: 2.5%) also increased during the quarter due to large issuances from Government-related entities.

Growth in outstanding household loans increased (5.6%; 2Q 2020: 3.7%), driven by higher loans for the purchase of passenger cars and personal use. Disbursements of household loans rebounded strongly during the quarter (RM99.1 bn; 2Q 2020: RM57.3 bn), with broad-based improvements across all loan purposes as loan demand rose amid the economic stimulus measures, and recovery in economic conditions under the RMCO. The new loans disbursed translated to some pick-up in loan repayments during the quarter, together

with a gradual resumption in instalment payments by more borrowers voluntarily opting out of the automatic moratorium. This has resulted in the repayment level in September reaching 72%⁷ of the level in March.

Meanwhile, outstanding business loans registered modest growth (2.9%, 2Q 2020: 3.9%), due to slower loans disbursed for working capital purposes⁸. As business activities resumed under RMCO, improving cash flow conditions led to lower demand⁹ for working capital loans. However, loan disbursements for investment-related purposes saw a recovery during the quarter, supported particularly by loans for the purchase of non-residential properties and large-value loans for the purchase of fixed assets. Loan repayments normalised from the subdued level in the previous quarter, but remained below historical trend.

⁵ Loans from the banking system and development financial institutions (DFIs).

⁶ Excludes issuances by Cagamas and non-residents.

⁷ Excludes credit cards.

⁸ Classification of business loans by purpose is only available for the banking system, which makes up 92% of total outstanding loans extended to businesses.

⁹ Indicated by loan applications to the banking system.