

# CREDIT RISK

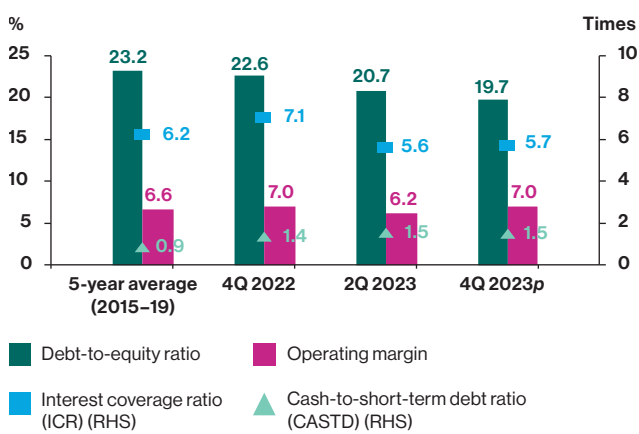
## Businesses remained resilient against persistent challenges

Businesses remained resilient in the second half of 2023, although operating conditions remained challenging amid ongoing headwinds. The recovery and performance of businesses continued to be uneven. Businesses in the services sector benefitted from the improvements in consumer spending and tourism. Businesses in the non-E&E manufacturing sector also experienced some uplift as external regional demand improved slightly towards the end of the year. While demand remained forthcoming, cost pressures continued to weigh on profit margins. Despite some easing throughout the year, input costs remained elevated relative to pre-pandemic levels with the median cost of goods sold ratio<sup>12</sup> at 78.8% (June 2023: 77.6%; 2015–19 average: 75.9%). The cost pressures were more prominent within the construction and manufacturing sectors, where the moderation observed in input prices has yet to have a discernible effect on costs due to pre-existing contractual obligations. Labour costs also remained elevated amid strong competition for skilled labour. In the commercial real estate segment, oversupply conditions continued to persist despite higher market activity. Additional incoming supply coupled with a shift in customer preferences towards newer and ‘green-certified’ commercial spaces continue to weigh on occupancy and rental rates.

Despite ongoing cost pressures, aggregate business operating margins improved in the latter half of the year as revenue growth of firms continued to be supported by resilient domestic demand (Chart 1.4). Business leverage continued to be on a downward trend, while cash buffers remained significantly above pre-pandemic levels. This supported the overall debt-servicing ability of businesses, with the median interest coverage ratio comfortably sustained above the prudent threshold of two times at 5.7 times. The overall share of firms-at-risk<sup>13</sup> also improved to 26.2%, although it still remained above its pre-pandemic average (Chart 1.5). Some businesses continued to face challenges, reflecting the uneven recovery. While the recovery of tourist arrivals

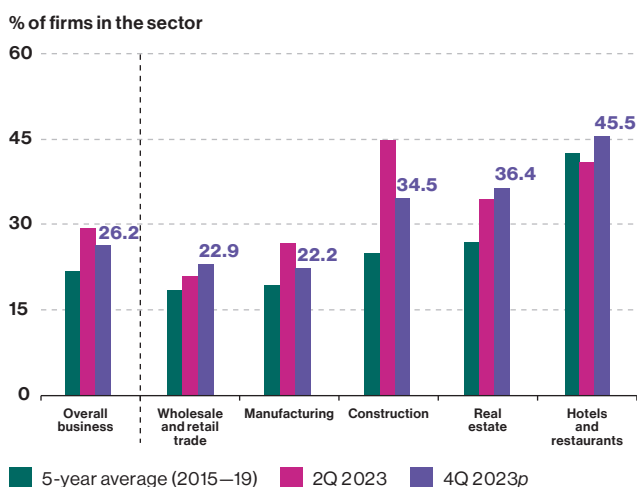
provided support to tourism-related sectors, total tourist expenditure has yet to recover to pre-pandemic levels. Firms in the food and beverages and accommodation sub-sectors have been affected by changes in consumer preferences and behaviour, as some consumers prioritised spending on necessities amid the higher cost of living. In the construction and manufacturing sectors, although business costs remained high, some firms in the sector began to see a turnaround in financial performance in the second half of the year after previously recognising significant losses. This improvement was primarily due to an expansion in construction activities, which also benefitted manufacturers of building materials.

**Chart 1.4: Business Sector – Key Financial Performance Indicators**



p Preliminary  
 Note: Prudent thresholds for ICR and CASTD are two times and one time respectively.  
 Source: S&P Capital IQ and Bank Negara Malaysia estimates

**Chart 1.5: Business Sector – Firms-at-risk for Selected Sectors**



p Preliminary  
 Source: S&P Capital IQ and Bank Negara Malaysia estimates

<sup>12</sup> Cost of goods sold (COGS) ratio is calculated by taking a firm’s COGS divided by its revenue. A higher ratio indicates that COGS makes up a higher proportion of revenue.

<sup>13</sup> Firms-at-risk refers to firms with interest coverage ratio below the prudent threshold of two times.

Business loans expanded by 3.6% (June 2023: 0.6%) in the second half of 2023. Loan growth was driven mainly by small and medium enterprise (SME) loans, primarily for working capital purposes. This was complemented by the continued availability of facilities under BNM's Fund for SMEs.<sup>14</sup> Meanwhile, a smaller contraction in loan growth was observed among larger firms, in line with a more positive business outlook (December 2023: -0.5%; June 2023: -4.6%). Large corporates also tapped the corporate bond market amid favourable funding conditions, given the narrowing bond spreads for high quality issuers. This resulted in an annual growth of outstanding corporate bonds of 4.3% (June 2023: 5.2%).

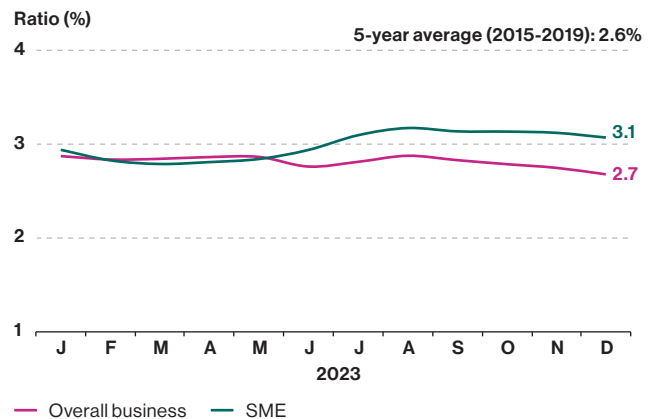
While the overall credit quality of business loans remained sound, some SMEs are showing emerging signs of financial vulnerabilities. The share of SMEs missing repayments<sup>15</sup> increased to 2.1% (June 2023: 1.6%) of total SME loans. The bulk of the increase was driven by SMEs with a history of missing repayments. Insights from banks indicate that these SME borrowers continue to make occasional or partial repayments to manage their cashflows while avoiding a default on their debt obligations. SME impairments also remained elevated at 3.1% of total SME loans (Chart 1.6). Some SMEs that are facing challenges have been proactive in reaching out to banks and the Credit Counselling and Debt Management Agency (AKPK) for repayment assistance. The number of repayment assistance applications from SMEs to AKPK in the second half of 2023 doubled compared to the corresponding period in 2022 – partly owing to greater awareness of AKPK's services – but it remains small at 0.6% of total SME loans (Chart 1.7). Similarly, new enrolments into repayment assistance offered by banks<sup>16</sup> also increased from low levels (December 2023: 0.2% of total SME loans; June 2023: 0.1%). On balance, these risk drivers continue to be offset by the sustained repayments of the vast majority of SMEs that have exited repayment assistance programmes introduced during the pandemic. SME loans under repayment assistance continued to decline to 5.4% of total SME loans (June 2023: 5.5%), or 0.9% of total banking system and development financial institution (DFI) loans. Almost all (94%) SMEs that exited repayment assistance programmes have been able to resume and sustain prompt repayment of their loans.

<sup>14</sup> About RM7.9 billion from a total allocation of RM32.4 billion remained available as at end-December 2023.

<sup>15</sup> Refers to loans with one or two months in arrears, or between 30 and 90 days past due.

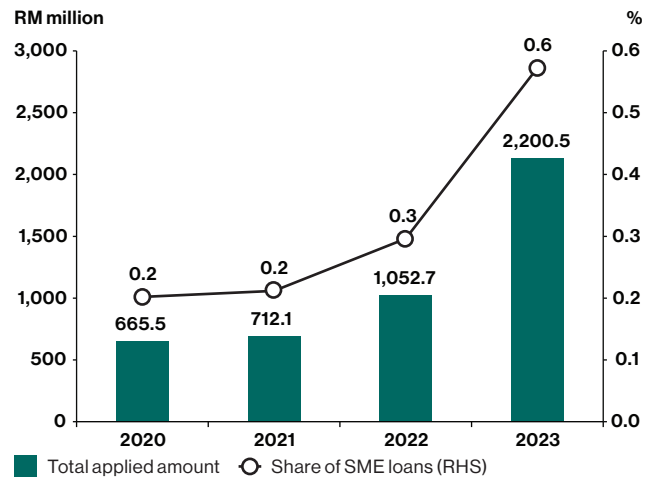
<sup>16</sup> Refers to rescheduling and restructuring (R&R) programmes.

Chart 1.6: Business Sector – Gross Impaired Loans



Source: Bank Negara Malaysia

Chart 1.7: Business Sector – SME Applications for AKPK Repayment Assistance



Source: Bank Negara Malaysia

In contrast, the quality of borrowings of large corporates has improved in line with general improvements in the financial strength of these firms. Some banks have started to write-back provisions on their large corporate exposures, reflecting sustained improvements in the recovery of business activities and a more positive outlook for specific firms. Movements in the ringgit in the latter half of 2023 were in focus for corporates with external debt obligations. Risks from non-financial corporate external debt, however, are assessed to be manageable as most of the exposures from large resident corporates are naturally or financially hedged against currency mismatches. Only a small number of companies with unhedged external borrowings may be susceptible to exchange rate volatility (22% of all resident-controlled corporates' external borrowings, equivalent to only 1.8% of total business debt). However, these borrowers have minimal domestic borrowings



## Key Developments in the Second Half of 2023

(less than 0.5% of total domestic banking loans), thus limiting contagion risks to domestic financial stability. Some corporates prudently prepaid their USD borrowings to manage the elevated USD borrowing costs in a high interest rate environment. A large share of the corporate external debt exposures (71%) were with maturities of above one year, further mitigating rollover risk. These exposures also remained adequately covered by assets, with corporate external assets at 1.1 times of corporate external debt.

Stress tests conducted by BNM confirmed that banks have adequate capital buffers to withstand a potential increase in credit losses from the business sector in adverse stress scenarios (refer to section on 'Assessing the Resilience of Financial Institutions' for more details). In addition, debt resolution mechanisms such as the Small Debt Resolution Scheme (SDRS), Corporate Debt Restructuring Committee (CDRC) and court-sanctioned corporate rescue mechanisms provide restructuring options for distressed but viable firms.<sup>17</sup> The recent legislative enhancements to the Companies Act 2016

will widen the coverage of firms that will benefit from these rescue mechanisms while embedding sufficient safeguards against potential abuse.<sup>18</sup>

Looking ahead, the anticipated recovery of the global technology cycle and ongoing progress in the implementation of domestic investment and infrastructure ventures will provide support to businesses' earnings. Against this, the implementation of subsidy rationalisation, tax adjustments and wage policies, while necessary, will have a bearing on the near term financial outlook for businesses. Ongoing geopolitical conflicts, China's economic trajectory and financial market volatility present further challenges, alongside an increased focus on climate-related risks and opportunities. Banks are well-buffered against potential downside risks, backed by conservative provisions and strong capital levels. A widespread deterioration in credit quality is not expected, as indicated by the improving Stage 2 ratio (December 2023: 12.4% of business loans; June 2023: 13.8%), which reflects an improving growth outlook for the Malaysian economy.

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<sup>17</sup> Refer to the Information Box on 'Debt Resolution Mechanisms for Viable Businesses Facing Temporary Financial Distress' in the BNM Financial Stability Review for Second Half 2020 for further details.

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<sup>18</sup> The Companies (Amendment) Bill 2023, which aims to strengthen the corporate rehabilitation framework and enhance corporate transparency in the Companies Act 2016, was tabled and passed at the Parliament in December 2023. It is expected to be gazetted into law in 2024.

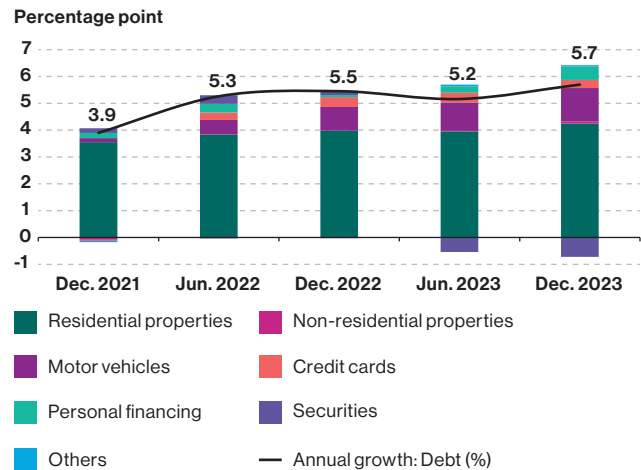
## Overall credit risk from the household sector remained contained, supported by continued improvement in income and employment

In the second half of 2023, household debt<sup>19</sup> grew at a faster pace amidst sustained improvements in the labour market and economic activity (Chart 1.8). The overall debt growth continued to be driven largely by housing and car loans, which collectively make up almost three-quarters (73.7%) of total household debt (Chart 1.9). The growth in housing loans reflects general improvements in residential property market activity, further supported by the continued availability of stamp duty exemptions or remissions for first-time home buyers. Meanwhile, car loans remained on an upward trend on the back of higher car sales following promotional campaigns and new model launches, including electric vehicles, during the period.

Households continued to take on more personal and credit card debt during the period. Such unsecured debt as a share of overall household debt has, however, remained broadly unchanged (15.5% of total household debt). A closer look at new personal financing and credit card debt also indicates that risks remained manageable. New personal financing approvals by banks in 2023 across borrowers from all income segments were primarily associated with debt consolidation, which helps to preserve household resilience. Growth in outstanding credit card debt has also been consistent with the ongoing recovery in consumer spending. Furthermore, prudential requirements remain in place to ensure that new credit card applications are subject to affordability assessments and appropriate credit limits. In line with these observations, credit card cash advance transactions remained low at 1.3% of total card transactions (June 2023: 1.3%; 2015–19 average: 2.2%). Revolving balances, as a proportion of outstanding credit card balances, also continued to trend lower to 47.9% (June 2023: 50.9%; 2015–19 average: 60.6%). Loans for the purchase of securities continued to decline (-13.8%; June 2023: -10.2%). This was driven primarily by lower Amanah Saham Bumiputera (ASB) financing as the narrowing spread between financing and dividend rates led to higher redemptions and lower new demand for such loans.

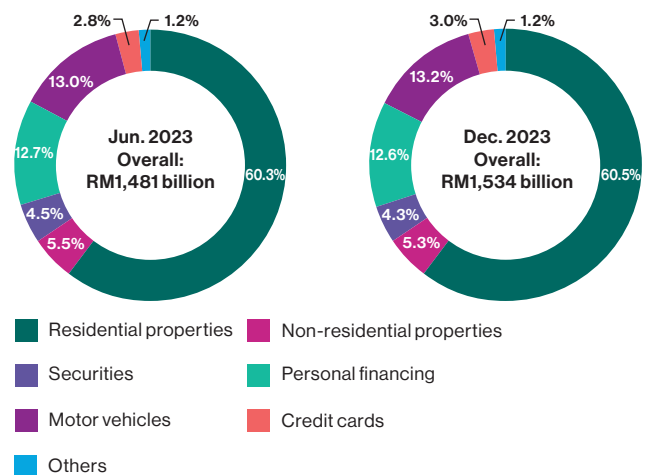
<sup>19</sup> Extended by both banks and non-bank financial institutions.

Chart 1.8: Household Sector – Annual Growth of Debt



Source: Bank Negara Malaysia

Chart 1.9: Household Sector – Composition of Debt by Purpose

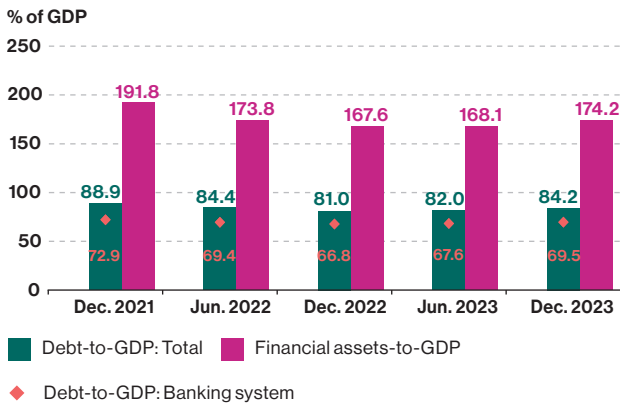


Note: Figures may not add up due to rounding.

Source: Bank Negara Malaysia

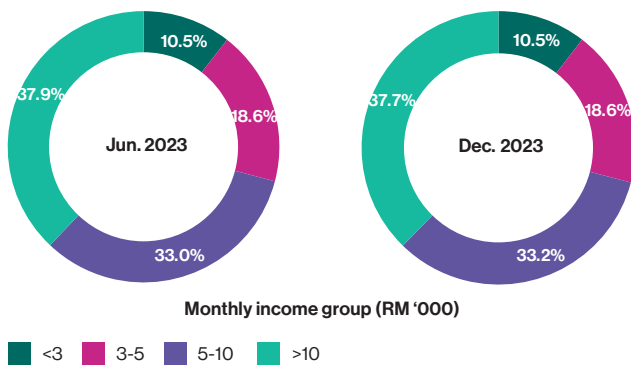
As at December 2023, the ratio of household debt-to-GDP and the ratio of banking system household debt-to-GDP remained elevated at 84.2% and 69.5% respectively (Chart 1.10). Despite this, households remain generally resilient. About 70.9% of household banking system debt is held by middle- and higher-income borrowers with a monthly income of RM5,000 and above (Chart 1.11). The overall median debt-to-income ratio was stable at 1.4 times (June 2023: 1.4 times) as banks maintained sound lending standards (Chart 1.12). Other measures also point to sustained debt-servicing capacity. In the second half of 2023, debt service ratios (DSRs) of newly approved and outstanding household loans stood at 41% and 35% respectively

**Chart 1.10: Household Sector – Key Ratios**



Source: Bank Negara Malaysia, Bursa Malaysia, Department of Statistics, Malaysia, Employees Provident Fund and Securities Commission Malaysia

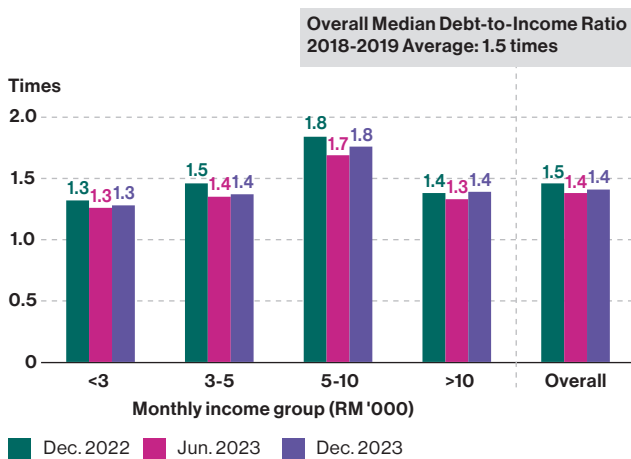
**Chart 1.11: Household Sector – Composition of Banking System Debt by Income Group**



Note: 1. Figures exclude loan accounts with incomplete income information. 2. Figures may not add up due to rounding.

Source: Bank Negara Malaysia

**Chart 1.12: Household Sector – Median Debt-to-Income Ratios by Income Group**

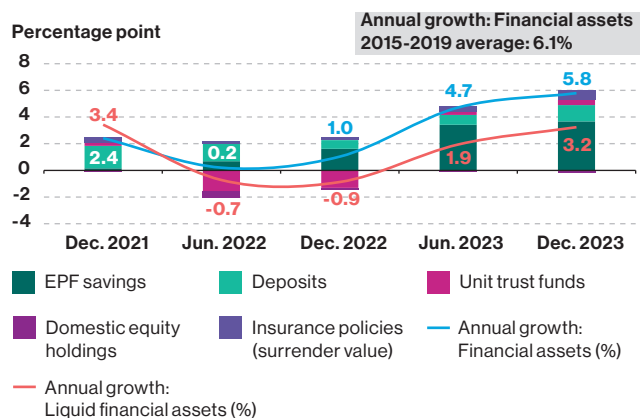


Source: Bank Negara Malaysia

(June 2023: 41% and 35%), providing healthy buffers for households to meet their loan obligations. Meanwhile, the share of borrowers with DSR exceeding 60% remained broadly unchanged at about a quarter of total household borrowers. More than two-thirds (69%) of high-DSR debt is held by middle- and high-income borrowers who typically have larger financial buffers to sustain loan repayments in the event of financial shocks. This is reflected in the low and stable level of impairment ratio among high-DSR borrowers (1.2%; June 2023: 1.3%).

The share of households that reported facing difficulties affording essential monthly expenditures with their current income increased slightly in 2023, notably among lower-income groups.<sup>20</sup> Most households, however, appear to be able to sustain consumption patterns and savings. Household spending on both necessities and discretionary expenditure items continued to expand, lending support to private consumption which grew by 4.4% in the second half of 2023. This has been accompanied by a sustained strong growth in the value of debit card spending of 13.5%. Similarly, the value of credit card spending expanded by 9.2%, with the share of revolving balances continuing to trend lower as earlier noted. Household financial assets also recorded healthy growth (5.8%; June 2023: 4.7%; 2015-19: 6.1%) (Chart 1.13), with higher savings held in bank deposits and contributions to the Employee Provident Fund (EPF), in line with the improvements in labour market conditions. Correspondingly, households continued to hold financial

**Chart 1.13: Household Sector – Annual Growth of Financial Assets**



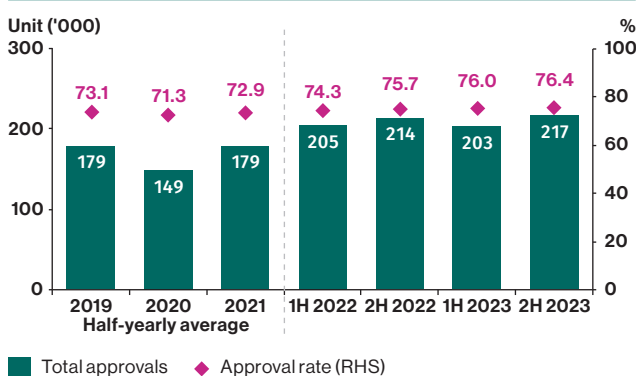
Source: Bank Negara Malaysia, Bursa Malaysia, Employees Provident Fund and Securities Commission Malaysia

<sup>20</sup> Based on BNM's monthly Consumer Sentiment Survey. The survey aims to gauge general economic and financial sentiments and expectations of the Malaysian consumers on a variety of topics such as household financial positions, labour market developments and cost of living. The survey is based on a representative sample of households across all income levels nationwide.

assets in excess of debt, with the aggregate value of financial assets remaining steady at 2.1 times of total household debt (June 2023: 2.1 times; December 2022: 2.1 times).

House financing continues to account for the bulk of household debt (60.5% of total household debt). Financing activity for the purchase of residential properties remained forthcoming in the second half of 2023, with loan applications and approvals picking up amid improved labour market conditions (Chart 1.14). Average lending rates on new house financing were below levels observed in the second half of 2019 (2H 2023 average: 4.2%; 2H 2019 average: 4.4%) when the OPR was last at 3.00%, reflecting strong competition among financial institutions (Chart 1.15). This has helped support access to financing for new home buyers. Owner-occupiers<sup>21</sup> continued to drive overall housing loan growth, accounting for more than two-thirds of the increase in overall housing loans. These borrowers

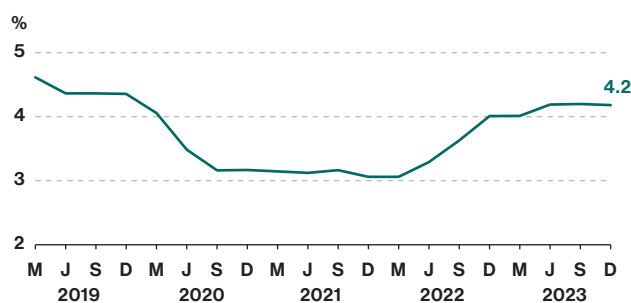
**Chart 1.14: Property Market – Volume of Approvals and Approval Rate for Housing Loans**



Note: Approval rate calculated based on volume of approvals.

Source: Bank Negara Malaysia

**Chart 1.15: Property Market – Average Lending Rate on New Housing Loans**



Source: Bank Negara Malaysia

<sup>21</sup> Proxied by individual borrowers with one housing loan, including first-time home buyers.

typically have higher incentives to service their loans. The median loan-to-value (LTV) ratio of outstanding housing loans remained prudent (66.6%; June 2023: 65.9%). This provides comfortable buffers for banks and borrowers against a correction in house prices, although risks of this materialising have receded amid improving activities in the housing market (see Information Box on 'Developments in the Residential Property Market').

Risks from credit-fuelled property investments have remained low. Outstanding housing loan growth for individual property investors<sup>22</sup> grew at a relatively moderate pace in the second half of 2023 (4.5%; June 2023: 4.4%), well below the growth rate for loans by owner-occupiers (9.2%; June 2023: 8.6%). The median LTV ratio of outstanding housing loans of individual property investors has also been relatively stable at 62.9% (June 2023: 62.4%). The bulk of these investors have no more than two property loans. Insights from banks, consistent with the historical loan performance, point to strong incentives generally observed among these investors to service loans, comparable to owner-occupiers (December 2023 impairment ratio for individuals with only two outstanding property loans: 1%; owner-occupiers: 1.4%). This is partly attributed to investors' longer-term intentions for holding properties (e.g. purchased for children or as a source of retirement income). The share of such exposures that are in a negative equity position also remains small (1.1%).

## Overall household resilience remains intact amid favourable labour market conditions, but vulnerabilities persist within certain segments

The overall quality of household borrowings has remained relatively sound (Chart 1.16). The share of household loans classified as Stage 2 (identified as having higher credit risk) edged higher (4.8%; June 2023: 4.3%). This remains within banks' expectations and is about 40% lower in value terms than that at the height of the pandemic. However, new signs of stress have been muted. The overall share of household borrowings under repayment assistance remained largely stable (1.6%; June 2023: 1.8% of total banking system and DFI loans), with a lower flow of new loans-in-arrears

<sup>22</sup> An individual property investor refers to an individual borrower with more than one housing loan.

**Chart 1.16: Household Sector – Loan Impairment and Delinquency Ratios in the Banking System**



Source: Bank Negara Malaysia

during the period. Newly restructured or rescheduled household loans also remained small at RM4.6 billion, equivalent to 0.2% of total banking system and DFI loans. Of this, newly-distressed exposures (exposures with no prior history of repayment assistance) only amounted to RM1.6 billion (or 0.1% of total banking system and DFI loans), indicating limited signs of emerging pocket of vulnerabilities.

Households facing repayment difficulties remain contained to a small segment of borrowers with pre-existing financial vulnerabilities. These include (i) lower-income borrowers, (ii) borrowers who were previously under repayment assistance programmes,

and (iii) borrowers whose income levels have yet to fully recover since the pandemic. Financial and debt management assistance remains in place through the Credit Counselling and Debt Management Agency (AKPK) to help these segments of borrowers attain a firmer financial footing. Enrolments into AKPK’s Debt Management Programme (DMP) for 2023 increased to 52,057 cases (2022: 34,670 cases; 2019: 48,581 cases) as more borrowers sought help to manage their debt amid cost of living pressures. Greater awareness of support available also contributed to the increase in enrolments. The overall share of household debt under DMP remained small (0.54% of total banking system and DFI loans; June 2023: 0.49%; December 2019: 0.49%).

Favourable labour market conditions, the continued availability of loan repayment assistance for viable borrowers, as well as government support measures for vulnerable households are expected to continue to lend support to overall household debt-servicing capacity. Nevertheless, banks remain firmly resilient to potential stress from the household sector in the unlikely event that ongoing challenges faced by some borrowers become more widespread. The latest stress test conducted by BNM shows that up to 4.8% of total banking system loans could be at risk of default by end-2026 if household borrowers experience severe labour market shocks with the unemployment rate reaching as high as 6.0%. This would continue to remain comfortably within banks’ excess capital buffers (refer to the section on ‘Assessing the Resilience of Financial Institutions’ for more details).

## Developments in the Residential Property Market

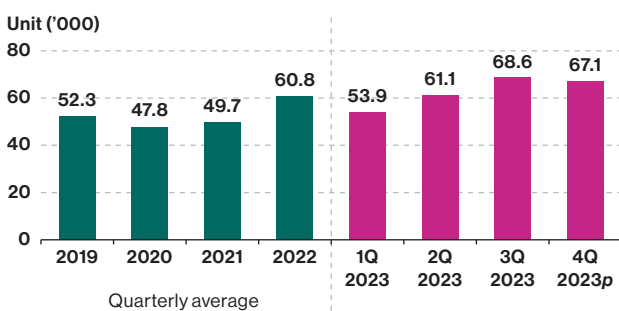
Malaysia's residential property market continued its recovery momentum in the second half of 2023, with further improvements in market activity. Against the backdrop of improving income and employment conditions, demand for housing remained forthcoming. Total residential property transactions picked up further in the second half of 2023 to above pre-pandemic levels (Chart 1.17). More than three-quarters of these transactions were for the purchase of properties in the more affordable mass-market segment (i.e. houses priced RM500,000 and below).<sup>23</sup> Demand for housing was also supported by measures to promote homeownership,<sup>24</sup> as well as competitive financing conditions. The volume of housing loan applications and approvals correspondingly increased during the period.

While transactions have trended higher across all key states,<sup>25</sup> market activity was particularly pronounced in Johor. This was spurred by improved sentiments surrounding projects like the Special Economic Zone and Johor Bahru–Singapore Rapid Transit System Link, as well as favourable demand from Malaysians who are working in Singapore. Importantly, signs of speculative activities remained limited, as most of these purchases were made by first- and second-time home buyers.

House prices<sup>26</sup> expanded by 3.3% in the third quarter of 2023 (Chart 1.18). The growth was largely driven by higher prices for landed properties, reflecting a persistent supply-demand mismatch for affordable housing amid stronger demand for new landed homes compared to high-rise units. Key states continued to drive overall house price growth, with Johor in particular recording strong growth.

Improvements in the housing market have reduced risks to household borrowers and lenders from a sudden and significant decline in house prices. The volume of unsold housing units has also continued to decline to 128,315 units (June 2023: 141,855 units; 2015–19 average: 130,210 units) further mitigating downside risks to house prices. Looking ahead, risks are expected to remain low. This is supported by (i) sustained income and population growth, supporting demand for housing, and (ii) low risk of widespread household defaults and foreclosures that would negatively impact house prices. Housing affordability issues are however expected to persist in the near term given elevated construction costs, which are likely to be passed on by developers to home buyers, and fewer launches relative to the pre-pandemic years constraining supply, particularly in the affordable housing segment.

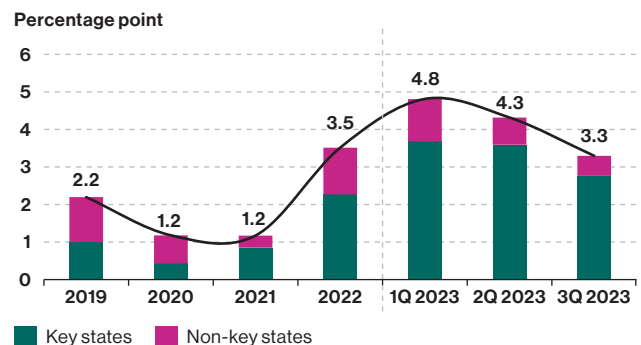
**Chart 1.17: Property Market – Housing Transaction Volume**



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Source: National Property Information Centre (NAPIC)

**Chart 1.18: Property Market – Malaysian House Price Index (MHPI) Growth by State**



Key states Non-key states

Source: National Property Information Centre (NAPIC)

<sup>23</sup> Housing affordability, while remaining within the 'seriously unaffordable' range, has remained broadly steady amid income growth that outpaced that of house prices. The median house price-to-income ratio stood at 4.3 in 2022.

<sup>24</sup> Refers to Malaysian Home Ownership Initiative (i-Miliki) which provides (i) 100% stamp duty exemption for first-time home buyers purchasing residential properties valued at RM500,000 or below until end-2025 and (ii) 75% stamp duty exemption for properties priced between RM500,000 and RM1 million until end-2023.

<sup>25</sup> Key states include Johor, Kuala Lumpur, Pulau Pinang and Selangor.

<sup>26</sup> As measured by the Malaysian House Price Index by National Property Information Centre (NAPIC).