

Overview

Global financial markets continued to experience heightened volatility through the second and third quarters of 2024 from shifting investor expectations as major central banks begin to ease monetary policy. Financial market volatility peaked in early August, amid fears of a 'hard landing' triggered by the release of weaker-than-expected US labour market data. Market expectations for earlier and more substantial rate cuts by the US Federal Reserve Board subsequently led to improved investor appetite for emerging market assets, including Malaysia. Domestic financial markets remained orderly with uninterrupted two-way flows in the bond and equity markets. Funding conditions remained favourable, supported by healthy liquidity in the government bond market and stable corporate bond credit spreads. In the domestic foreign exchange (FX) market, the ringgit continued to be primarily driven by external developments. Since the beginning of the year, the ringgit has appreciated by 11.4% against the US dollar.¹ Positive economic prospects and domestic structural reforms, complemented by ongoing initiatives to encourage foreign exchange flows, will continue to provide enduring support to the ringgit.

Business activities improved in the first half of 2024 in line with the recovery in both global and domestic economic conditions. Some business sectors continue to face challenges arising from continuing cost pressures and slower recovery in consumer demand in some product sub-segments. Businesses have remained generally resilient against these challenges. Measures of overall debt-servicing capacity of businesses remained healthy while the overall share of firms-at-risk has continued to decline to 23.4%. The overall credit quality of business loans remained sound with the impairment ratio remaining low at 2.6%. Banks remain vigilant over the loan performance of small and medium enterprises (SMEs) and continue to maintain prudent buffers against potential losses. So far, risks continue to be well contained. The share of SMEs with delinquent loans

has declined. SMEs that have exited repayment assistance programmes have also been able to sustain prompt loan repayments. Going forward, overall business resilience is expected to improve further in the second half of the year amid a sustained expansion in economic activity.

Household resilience continued to be supported by favourable economic and labour market conditions. The ratio of household debt-to-GDP stood at 83.8%, broadly unchanged since December 2023 as household debt grew in line with the pace of economic activity. Risks from buy now pay later (BNPL) schemes continue to be limited, with outstanding exposures remaining small at just over 0.1% of overall household debt. Further, banks' prudent lending standards continue to play an important role in keeping household debt accumulation in check and in line with debt-servicing capacity. During the period, household financial assets expanded at a faster pace and remained adequate to cover more than two times of overall household debt. Household borrowings that may be at higher risk of default decreased to 4.4% of total household loans (December 2023: 4.8%). Looking ahead, favourable economic and labour market conditions as well as sound lending standards will continue to underpin household resilience.

The banking system remained strong and well-positioned to withstand shocks and support financial intermediation. Banks continue to be well-capitalised, with the aggregate total capital ratio at 18.4% and excess capital buffers of RM136.1 billion as at end-June 2024. Funding and liquidity positions also remained sound as evidenced by the healthy Liquidity Coverage Ratio (155.1%) and Net Stable Funding Ratio (115.5%). Banks' profitability continued to be supported by sustained interest income amid stronger loan growth and higher trading and investment income. Improved operational efficiency further bolstered profitability and has helped cushion the impact of compressed net interest margins as well as supported banks' significant ongoing investments in

¹ Data as of 30 September 2024.

strengthening technology and cyber resilience. While asset quality has remained sound, banks continued to be cautious in releasing provisioning buffers built up during the pandemic. This has kept annualised credit costs broadly stable around pre-pandemic historical averages. Stress tests conducted by Bank Negara Malaysia (BNM) affirmed that banks remained resilient under adverse stress scenarios and are able to continue to meet the financing needs of the economy.

The insurance and takaful sector also maintained its resilience with an aggregate capital adequacy ratio of 227% and excess capital buffers of RM37.4 billion. Profitability improved due to higher net unrealised gains from the strong equity market performance and sustained investment income. New business premium growth provided further support. However, elevated medical benefit payouts continue to weigh on underwriting performance in the life and family takaful segment. General insurance and takaful operating profits were broadly sustained despite higher motor claims provisions, in line with robust business growth. Nevertheless,

exposure to climate events could see increased volatility in the performance of general insurers and takaful operators going forward.

Technology and cyber-related risks will continue to pose challenges to the management of operational risks within the financial system. Continuous efforts by financial institutions, including payment service providers, to reinforce their technology and cyber defences, and strengthen fraud controls, remain paramount to support the financial system's operational resilience. While financial losses from operational risks reported by financial institutions remained low, moderate disruptions to online banking services have called for stronger measures to ensure more robust incident response plans and closer monitoring of risks arising from a growing reliance on third-party service providers. BNM continues to raise standards expected of financial institutions in response to new and emerging threats. These include enhanced expectations on managing third-party risks, fraud countermeasures and information technology (IT) stress testing.