Promoting a Progressive and Inclusive Financial System

The Bank is committed to promoting a progressive and inclusive financial system that best serves the needs of the Malaysian economy.

In 2020, we continued to advance the development of the financial sector despite challenges in managing and responding to the pandemic. Efforts were geared towards accelerating the digitalisation of financial services, deepening financial markets, enhancing access to finance and financial inclusion, and building financial resilience.

Accelerating the digitalisation of financial services

For individuals and businesses alike, digitalisation would contribute to easier, faster and cheaper ways to access services and manage their finances. Recognising this, the Bank strives to ensure that our regulations are responsive to digital innovations that aim to better serve communities, while ensuring that financial institutions are effectively managing the associated risks.

Arising from the pandemic, there was an accelerated shift towards online financial services. In 2020, online banking transactions grew by 49% while e-wallet[1] transactions increased by 131% compared to the same period last year (see more trends in the chapter on "Promoting Safe and Efficient Payment and Remittance System"). To further support the uptake of online financial services, the electronic Know-Your-Customer (e-KYC) Policy Document was issued in June 2020, enabling the opening of accounts digitally for customers to occur anytime and anywhere. As a gateway towards digitalisation, e-KYC is expected to pave the way for greater innovation and provision of end-to-end digital financial services. Several financial institutions, including banks, e-money issuers and remittance service providers have adopted e-KYC solutions, with more expected to follow in 2021.

The Bank issued the Policy Document on Licensing Framework for Digital Banks on 31 December 2020. The licensing of new players with innovative business models is expected to serve the economy and contribute to the well-being of Malaysians. Through the use of agile technology platforms and data analytics, digital banks are expected to widen the offering of banking products and services that are more targeted towards solving Malaysian consumer pain points, particularly for the unserved and underserved consumer segments. The Bank will adopt a proportionate regulatory framework as well as require digital banks to observe limits on aggregate asset exposures during the initial years of operations. These measures are intended to reduce barriers to entry, whilst allowing the Bank to observe attendant risks. With the publication of the Policy Document, the Bank has begun accepting licence applications until 30 June 2021. Up to five licences may be issued to qualified applicants by the first quarter of 2022. Successful applicants will have to be able to demonstrate a strong value proposition focused on the unserved and underserved segments and the ability to meet regulatory requirements to safeguard the stability of the financial system.

In recent years, we have observed notable progress in the use of technology in the financial markets. Our aim is to improve efficiency and transparency in the intermediation and price discovery process. In 2020, digitalisation in the onshore financial market advanced further in the area of foreign exchange trading. Following the publication of

[1] Network-based e-money which are accessible via the internet, mobile phones or other devices.

the Framework for Electronic Trading Platforms (ETP) in 2019, the Bank in 2020, approved three global ETP operators to provide their services as intermediaries in the Malaysian financial market. This contributed to the digitalisation of the financial market, which also served to support increased remote working arrangements during the pandemic. Trades through ETPs accounted for nearly 19% of the total onshore foreign exchange turnover following the commencement of operations by the approved ETP operators.

The Fintech Regulatory Sandbox (Sandbox) continued to play an important role in encouraging innovation in the financial sector. Most notable has been the growing interest from applicants providing Insurtech solutions such as end-to-end digital insurance, digital insurance broker and financial aggregation business. This development resonates closely with the Bank's agenda to increase insurance penetration, thus further deepening financial inclusion in Malaysia. For 2020, one takaful operator has received approval to live test its peer-to-peer (P2P) family takaful product in the Sandbox. Meanwhile, four fintech companies have advanced to the preparation stage[2] for subsequent live testing of their solutions. However, quite a large number of the applications during the year were either withdrawn by the participants or did not meet criteria for admission to the Sandbox, typically because the proposed innovative solutions did not face any regulatory hindrance to warrant testing in the Sandbox or there was a lack of operational readiness for live testing.

We also took active steps to facilitate a wider range of innovation beyond fintech solutions. To this end, the Financial Technology Enabler Group (FTEG), a cross-functional internal working group established in June 2016 to support the Bank in regulatory policies and development strategies for the adoption of technological innovations in the Malaysian financial services industry was renamed the Financial Technology and Innovation Group (FinTIG). Recognising the continuously evolving scope of financial innovation, the change reflects the expanded mandate of FinTIG to include non-technology driven innovations, such as changes in business models, channels of distribution and product design that may not involve the use of new technology. In line with this, the Sandbox is also being reviewed to accommodate non-technologically driven innovation. The Bank's Financial Development and Innovation Department (FDI) acts as the primary contact point (fintech@bnm.gov.my) for the Bank on fintech matters. FDI, as the secretariat of FinTIG works closely with members of FinTIG toward facilitating innovation.

To support the overall development of a dynamic fintech ecosystem in Malaysia, we collaborated with the Malaysia Digital Economy Corporation (MDEC) to launch the Fintech Booster programme in August 2020 (Diagram 1). Positioned as a platform to connect fintech companies with other actors and stakeholders in the ecosystem, the programme aims to provide fintech companies with capacity building tools and support on legal and compliance matters, business development and access to technology resources in order to enhance prospects for viable and successful financial innovations. The Bank is supporting the programme through the Legal and Compliance vertical, whilst the Business Model and Technology verticals are overseen by MDEC with the support from its partners.

Deepening financial markets

The Bank continued in 2020 with ongoing developmental initiatives aimed at further improving market access and liquidity in the domestic financial markets. First, we pursued measures to enhance Malaysia's position as an attractive investment destination for global investors. Global market players were continuously engaged, albeit virtually, during the pandemic. Second, in collaboration with domestic market stakeholders, we pursued initiatives to deepen liquidity in the government bond and interest rate swap markets, which contributed to more efficient market pricing and greater flexibility in risk management. In addition, there were refinements to the Foreign Exchange Policy (FEP) to improve hedging conditions for both corporates and investors. Taken together, these measures have further strengthened the resilience and attractiveness of the domestic financial market.

[2] Upon obtaining the Bank's approval to participate in the Sandbox, an applicant is considered to have advanced to Stage 2 (preparation stage) where the applicant will work with the Bank on details (e.g. testing parameters, exit strategy and transition plan) in preparation for subsequent live testing stage.

Diagram 1: Fintech Booster Programme

FINTECH BOOSTER PROGRAMME

Provide capacity building programmes for fintech companies to develop meaningful products and solutions

A centralised hub to provide the necessary tools and support for fintech companies

Legal & Compliance*

ACTIVATED

Support for companies to enhance legal and regulatory understanding on gatekeeping regimes, compliance and risk management

- ✓ Financial Policies & Risk Management
- ✓ IT Compliance & Cybersecurity
- ✓ Legal Advisory in Business Set Up

*Supported by BNM & MDEC

Business Model**

UPCOMING

Support on companies' business plan and market assistance

- ✓ Business Plan
- ✓ Market Assistance
- ✓ Training & Infrastructure
- ✓ Collaboration

**Supported by MDEC

Technology**

UPCOMING

Access to technology ecosystem, infrastructure resources and services

- ✓ Service and Mentorship
- ✓ Technology Infrastructure

**Supported by MDEC

318 Registered members

Public programme — **10** Public programmes organised on regulations, taxation, data protection, Shariah, risk, etc

Private programme — **24** Completed one-on-one legal consultations

Source: Malaysia Digital Economy Corporation (MDEC)

Diagram 2 : Deepening Financial Market

Enhanced access to the Malaysian financial markets

Formalisation of the Primary Market Maker (PMM) Framework in April 2020

- ✓ PMM banks are accorded with market-making flexibilities and now publish continuous reference USD/MYR quotes on international platforms
- ✓ Total of USD3.3 billion worth of foreign exchange (FX) transactions has been facilitated by PMM banks after KL trading hours in 2020 with competitive bid-ask spreads

Listing of Malaysian government bonds under Bursa Malaysia's Exempt Regime

- ✓ Increased visibility and transparency of domestic bond market to attract long-term investors, while enhancing market profiling of MGS/MGII issuances

Continuous engagement with participants from global financial markets

- ✓ Effective investor engagement by FMAM -BNM via video conference with global portfolio managers, traders and custodians
- ✓ Continuous engagement with foreign investors and bond index providers to provide clarity on documentation, third party FX and pre-funding requirements

Pilot flexibility on interest rate swaps (IRS) in November 2020

- ✓ Non-resident banks can enter into IRS without firm commitment directly with selected licensed onshore banks or via their Appointed Overseas Office (AOO) on pilot basis
- ✓ Based on the positive feedback during the pilot, the Bank announced the liberalisation of the onshore IRS market where all onshore banks and their AOOs may trade IRS with non-resident banks without firm commitment effective 15 March 2021

Measures to deepen liquidity have led to increased market vibrancy

Revised settlement methodology for the 5-year Malaysian Government Securities (MGS) Futures Contract

- ✓ Elevated MGS futures as an alternative hedging instrument through collaboration with Bursa Malaysia, Securities Commission Malaysia and key market makers to revise settlement methodology from cash delivery to physical delivery

Government bond auctions designed to feature increased re-openings

- ✓ Enlarged individual bond issuances in the market for better bond market liquidity
- ✓ Increased ease of index tracking by global passive bond investors

Improved hedging environment for corporates and investors

- ✓ Exporters have better natural hedge as export proceeds below RM200,000 are exempted from conversion
- ✓ Residents may hedge foreign currency obligations up to underlying tenure and are given flexibility to cancel their hedging positions in response to changing market conditions

Enhancing access to finance and financial inclusion

Financial inclusion is essential for a more equitable society. The pandemic further underscored the need to support and protect the underserved segments of society, especially those who are disproportionately affected. In line with this, the Bank continued to take active steps to advance financial inclusion.

An important focus during the year was ensuring continued access to finance for SMEs under highly challenging business conditions. SMEs have a sizable contribution to the Malaysian economy of close to 39%[3] of GDP and make up almost 50% of total employment. However, their relatively low cash buffers and narrower profit margins, worsened by the pandemic, have made them more susceptible to cashflow and financing constraints. To help SMEs to weather the pandemic, we significantly increased the allocation of financing assistance under BNM's Fund for SMEs (BNM's Fund) from RM9.1 billion to RM23.1 billion. Facilities[4] under BNM's Fund, channelled through the financial institutions, aimed to provide immediate cash relief to adversely affected SMEs, support recovery of hard-hit economic sectors and enhance innovative capacity of high-tech SMEs. BNM's Fund complements the much larger provision of SME financing by the financial institutions, which disbursed a total of RM256.8 billion in loans/financing to SMEs in 2020, with more accounts approved compared to the previous year (2020: 145,993 accounts; 2019: 115,498 accounts). BNM's Fund has helped to sustain businesses and safeguard jobs, with about RM6.0 billion worth of funds still available for new applications by SMEs as at mid-March 2021. Key facts of BNM's Fund are provided in Diagram 3. Beyond the provision of funds, the Bank also supported the availability of credit guarantee schemes to encourage continued bank lending in the heightened risk environment.

Funds by the Bank benefitted more than 32,000 SMEs and supported around 596,600 jobs.

As the environment will continue to be challenging, we strive to ensure that the Bank's funds for SMEs are responsive to the immediate challenges facing SMEs, while supporting their ability to transform and adapt to new norms that will further enhance Malaysia's future growth potential. We continue to take active measures to raise awareness and address SMEs' concerns on facilities with relatively low demand, such as the PENJANA Tourism Financing (PTF) which has been mired by the weak business outlook in the sector. The slower take-up, nonetheless, allows us the flexibility to reallocate resources towards other pressing needs of the SMEs. This is reflected in the recent upsizing of the SME Automation and Digitalisation Facility (ADF) announced in March 2021 from RM300 million to RM1 billion, to encourage SMEs across all sectors to automate processes and digitalise operations that can better support their recovery and productivity in the post-pandemic environment.

To provide SMEs with one-stop access to specialised and comprehensive debt restructuring assistance, financial education and advisory services, the Small Debt Resolution Scheme (SDRS) function was transferred to the Credit Counselling and Debt Management Agency (*Agensi Kaunseling dan Pengurusan Kredit*, AKPK) on 1 September 2020. With AKPK's wide online presence and 12 branches nationwide, the transfer will offer SMEs more convenient access to debt restructuring services and strengthens the SDRS' capacity to manage SMEs in need of debt resolution assistance. Further, the dedicated micro business helpdesk[5] set up at AKPK in November 2020 provides an additional avenue for micro enterprises to obtain targeted repayment assistance and free financial advice. Notably, following the transfer as well as the end of the automatic moratorium in September 2020, the number of SMEs assisted by AKPK's Repayment Assistance to SMEs[6] (RAS) increased by 48% in September – December 2020, compared with the first 8 months of the year.

Development financial institutions (DFIs) remained important in broadening access to finance. DFIs played a counter-cyclical role during the pandemic to bridge financing gaps in strategic economic sectors and to the underserved. In 2020, total loans/financing outstanding by DFIs registered a growth of 7.7% to RM153.7 billion (end-2019: -0.3% to RM142.7 billion), underpinned by demand from the household, agriculture and general commerce sectors.

[3] Source: Department of Statistics, Malaysia (DOSM).
[4] Facilities under BNM's Fund include the Special Relief Facility (SRF), Agrofood Facility (AF), SME Automation and Digitalisation Facility (ADF), All Economic Sectors (AES) Facility, Micro Enterprises Facility (MEF), PENJANA Tourism Financing (PTF), Targeted Relief and Recovery Facility (TRRF) and High Tech Facility – National Investment Aspirations (HTF-NIA). For further details, refer to www.bnm.gov.my/covid19/
[5] The micro business helpdesk can be accessed via www.akpk.org.my/microhelpdesk
[6] Consists of the SDRS and Debt Management Program (DMP) for sole proprietors.

Diagram 3: BNM's Fund for SMEs in numbers - Key facts of selected facilities in 2020

Targeted funds met SME financing needs amid the COVID-19 pandemic

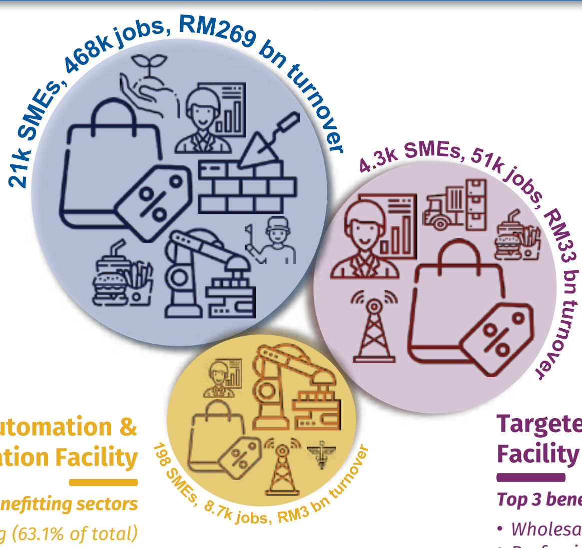
Key facts of selected facilities[1]

	Special Relief Facility (SRF)	Agrofood Facility (AF)	SME Automation & Digitalisation Facility[2] (ADF)	PENJANA Tourism Financing (PTF)	Targeted Relief & Recovery Facility (TRRF)	High Tech Facility - National Investment Aspirations (HTF-NIA)
PURPOSE	EASE CASH-FLOW CONSTRAINTS	INCREASE FOOD PRODUCTION AND EXPORTS	INCENTIVISE AUTOMATION AND DIGITALISATION	AID THE TOURISM SECTOR	SUPPORT RELIEF AND RECOVERY OF SERVICE SECTOR	SUPPORT HIGH-TECH AND INNOVATIVE SECTORS
DATE ANNOUNCED	27 FEB 2020	27 FEB 2020[3]	27 FEB 2020	30 JUL 2020	06 NOV 2020	15 DEC 2020
TOTAL ALLOCATION	RM 10.0 BILLION[4]	RM 1.5 BILLION	RM 1.0 BILLION[5]	RM 0.6 BILLION[6]	RM 4.0 BILLION[7]	RM 0.8 BILLION[8]
AVAILABLE BALANCE	FULLY UTILISED	RM 0.2 BILLION	RM 0.8 BILLION	RM 0.5 BILLION	RM 2.7 BILLION	RM 0.8 BILLION
APPROVAL RATE	78%	91%	83%	64%	88%	100%

1 As at 17 March 2021
2 Under the All Economic Sector (AES) Facility
3 Refers to the date when the allocation was increased for the AF, which is an existing facility
4 The SRF was upsized in March 2020 (from RM2 billion to RM5 billion) and May 2020 (from RM5 billion to RM10 billion)
5 The ADF was upsized in March 2021 (from RM0.3 billion to RM1 billion)
6 From the initial RM1 billion, RM200 million was reallocated to the Disaster Relief Facility (DRF) in February 2021 and RM200 million to the ADF in March 2021
7 The TRRF was upsized in February 2021 (from RM2 billion to RM4 billion)
8 From the initial RM1 billion, RM200 million was reallocated to the ADF in March 2021

. . . preserving businesses and jobs that helped stabilise the economy

Profile of accounts approved[1, 2]



Special Relief Facility (SRF)

Top 3 benefitting sectors
- Wholesale and Retail Trade (47.2% of total)
- Manufacturing (15.2%)
- Construction (9.0%)

SME Automation & Digitalisation Facility

Top 3 benefitting sectors
- Manufacturing (63.1% of total)
- Wholesale and Retail Trade (13.8%)
- Information and Communications (5.6%)

Targeted Relief and Rectovery Facility (TRRF)

Top 3 benefitting sectors
- Wholesale and Retail Trade (66.5% of total)
- Professional, Scientific and Technical Activities (6.9%)
- Transportation and Storage (5.3%)

1 As at 24 February 2021
2 SMEs' sales turnover is as reported in application for the facilities

Source: Bank Negara Malaysia

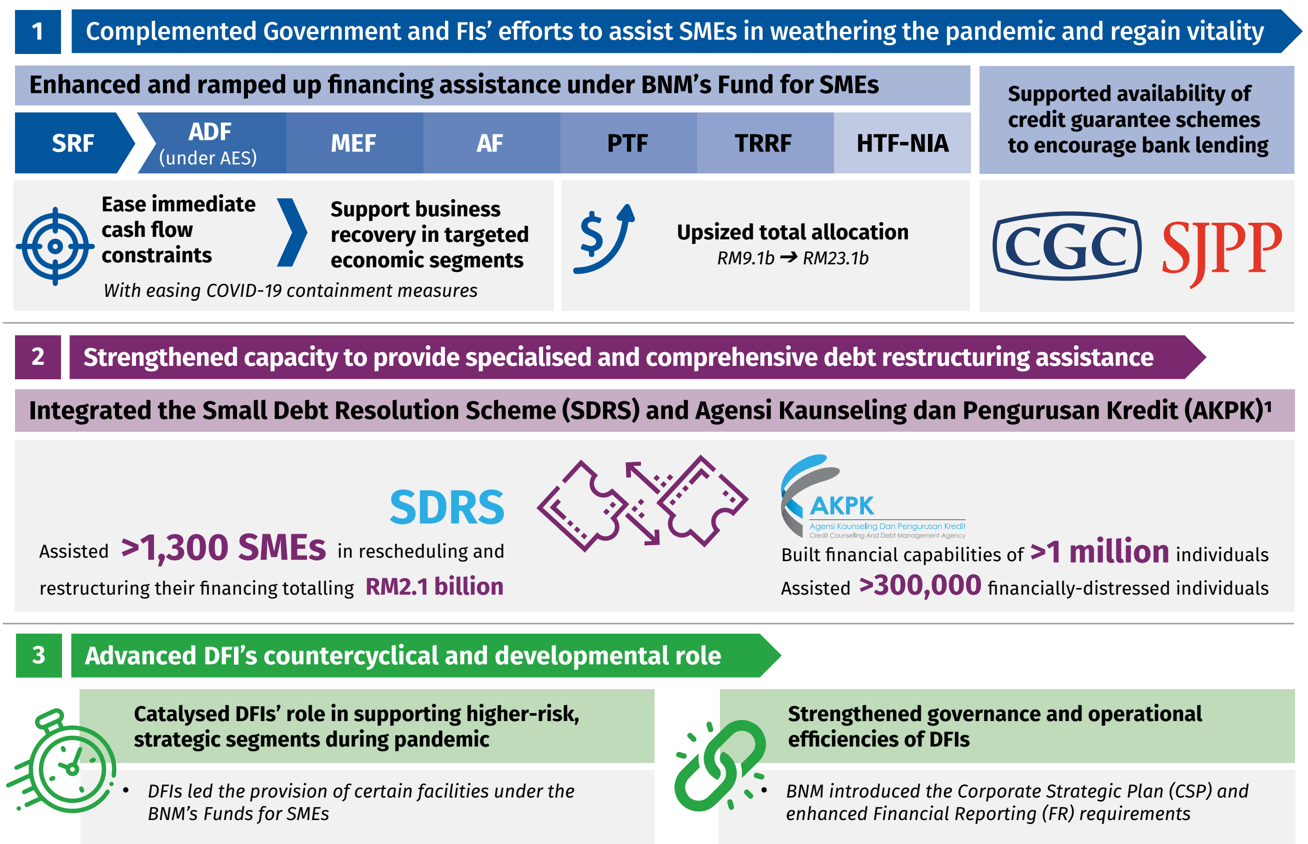
DFIs also provided support and assistance to higher risk segments not typically served by commercial banks, and who were badly affected by the pandemic. This includes financial assistance for agrofood businesses, tourism providers, money services businesses and homestays. Moreover, DFIs were involved as key administrators of various financing schemes introduced by the Government and the Bank under the PRIHATIN, PENJANA, PERMAI and recently announced PEMERKASA stimulus packages, aimed at sustaining the business operations of small businesses and microenterprises. As at end-2020, DFIs provided financing amounting to RM833.7 million to 30,905 microenterprises under the PRIHATIN and PENJANA schemes. In addition to financing, more than 68,900 businesses and 1,625,000 individuals were granted a 6-month moratorium on financing repayments by DFIs. This provided timely support to vulnerable households and SMEs in key economic sectors during the challenging year.

In 2020, we introduced and enhanced several policy requirements to better align and enhance DFIs' developmental outcomes with the principles set out by the Performance Measurement Framework (PMF). These requirements, centred around DFIs' corporate strategic planning and financial reporting, were aimed at institutionalising developmental objectives and mandates within the DFIs' business strategies and activities, and further aligning the DFIs' achievements with national development priorities.

To ensure continued access to financing during movement restrictions, the Bank worked closely with State Governments and DFIs to ensure operational continuity of agent banks. In addition, we worked with the relevant financial institutions to set-up ATM machines and mobile counters in rural and remote communities to facilitate the distribution of Government aid. Beyond the existing Mobile Banks (*Bank Bergerak*) offered by financial institutions, we also worked to establish new alternative channels such as mobile ATMs to further improve the delivery of basic financial services nationwide.

Agent banking continued to serve as an important channel for providing convenient access to financial

Diagram 4: Key areas in enhancing the financing ecosystem for SMEs and individuals amid the COVID-19 pandemic



[1] Data cited refers to cumulative data since the establishment of SDRS in 2003 and AKPK in 2006

services in remote areas with limited connectivity, generating positive spillover effects to the wider community. In the first nine months of 2020, 17.1 million transactions of basic financial services valued at RM1.6 billion were transacted at agent banks (January – September 2019: 20.8 million transactions, amounting to RM1.9 billion). Since the introduction of the agent banking initiative in 2012, agent banks have facilitated 212 million transactions, amounting to RM17.9 billion as at end-September 2020. In terms of accessibility, 95% of sub-districts or State Legislative Assemblies (*Dewan Undangan Negeri*, DUN) now have access to basic financial services (2011: 46%).

Building resilience through inclusive financial product offerings

In 2020, we also worked to further develop Malaysia's microinsurance and microtakaful landscape. A key initiative on this front was the review of the *Perlindungan Tenang* framework, launched in 2017, to encourage the provision and take-up of meaningful insurance and takaful solutions for the underserved. Key principles and the progress of the *Perlindungan Tenang* initiatives are highlighted in Diagram 5.

Revisions to the *Perlindungan Tenang* framework included fit-for-purpose flexibilities to promote innovation and address supply-side challenges. For example, more entities will be allowed to distribute *Perlindungan Tenang* products. Further, distributors will be granted additional operational flexibilities and *Perlindungan Tenang* products can be combined with other financial products where it can be demonstrated that doing so will encourage higher take-up for the benefit of the targeted segments without materially increasing risks. At the same time, insurers and takaful operators (ITOs) are also required to observe parameters in the design of products which serve to ensure the *Perlindungan Tenang* products provide good value-for-money coverage and benefits to safeguard consumers' interests.

Recognising its importance, the Malaysian Government also announced incentives in the Budget 2021 to promote *Perlindungan Tenang* products. This includes a RM50 voucher for eligible recipients and extension of stamp duty exemption for *Perlindungan Tenang* products for another five years. These measures are expected to further increase the take-up of *Perlindungan Tenang* products and widen the financial safety net for the *rakyat*.

Diagram 5: Key principles and progress of *Perlindungan Tenang*

Launched in 2017, this initiative aims to encourage insurers and takaful operators to offer products that are suitable for the unserved and underserved segments that meet the following principles:

PERLINDUNGAN tenang MAMPU & MUDAH

Affordable • Premium/contribution must consider circumstances of the target market i.e. disposable income, occupation, etc.	• Premium/contribution for *Perlindungan Tenang* products ranges from RM1 to RM20 per month
Accessible • Products and services should be made available at convenient access points	• Products can be purchased online, from physical counters nationwide (e.g. postal offices) or through mobile network operator
Good Value • Protection provided corresponds to key needs • Proportion of premium/contribution allocated to the benefits is maximised	• Products offer additional benefits including *Badal Hajj*, donation to charity, cover for funeral expenses and hospitalisation cash reimbursement
Easy to understand • Product benefits, terms and conditions should be self-explanatory to consumers	• Product design and descriptions are simple and available in multiple languages
Easy to buy and claim • Customer journey from purchase to claims should be frictionless	• Products have minimal underwriting questions and claims are paid within 5 working days upon complete submission of documentation

Progress (as at end-2020)

Participation from
14 insurers and takaful operators

offering
14 Life insurance/family takaful products
2 General products

which cover
✓ Death
✓ Total permanent disability
✓ Personal accident
✓ Fire and flood

172,648 Persons covered[1] with
RM8.2 million Premium/contribution collected

1,706 claims paid out amounting to
RM5.6 million

[1] Include individual and group policies/certificates

The Bank embarked on communication and education efforts to increase awareness and understanding of insurance and takaful protection among Malaysians. Through the Financial Education Network (FEN), we collaborated with the insurance and takaful industry to host an education and awareness programme in conjunction with Financial Literacy Month in October 2020. The webinar attracted more than 27,000 views.

Beyond the insurance/takaful space, the Bank also facilitated industry efforts to develop innovative ecosystems for more inclusive financial services. These include new business models involving partnerships between payment service providers and fund management firms to enable micro-investments, thereby broadening access to wealth management products. In these areas, we worked closely with relevant regulatory authorities to enhance and refine existing regulations to facilitate such partnerships, subject to safeguards for financial stability and consumer protection.

In strengthening financial and social resilience, the Bank also continued to support the advancement and integration of social finance in Islamic financial services, particularly for the underserved segments. Further details on the Bank's initiatives to advance social finance are in the chapter on "Promoting a Progressive and Inclusive Islamic Financial System".

Going forward

For 2021, the Bank's priority would be to set out the critical developmental and regulatory priorities for the next five years (2022 – 2026) under a new blueprint for the financial sector (Blueprint 3.0). These priorities will focus on enabling technology and data-driven innovation, enhancing the competitiveness of the financial sector, expanding access and responsible usage of financial solutions, and ensuring financial intermediation remains effective to support the future needs of the economy. Blueprint 3.0 will also emphasise the catalytic role of the financial sector in advancing the sustainability agenda, in particular climate-related risks to support an orderly transition towards a greener economy.