

## ECONOMIC AND FINANCIAL DEVELOPMENTS IN MALAYSIA IN THE FOURTH QUARTER OF 2010

### OVERVIEW

#### The Malaysian economy recorded a growth of 4.8% in the fourth quarter of 2010

The Malaysian economy registered a growth of 4.8% in the fourth quarter of 2010. Higher private and public sector spending contributed to the expansion in domestic demand. The slower growth in the global economy, however, had led to weaker growth in external demand. On the supply side, all economic sectors, with the exception of the primary sectors, continued to expand further during the quarter. For the year as a whole, the Malaysian economy registered a growth of 7.2% (2009:-1.7%).

Domestic demand strengthened by 5.7% in the fourth quarter (3Q 10: 5%), due mostly to the strong expansion in private consumption and capital spending. Private consumption increased by 6.5% (3Q 10: 7.1%) supported by favourable labour market conditions, positive consumer confidence and higher income levels. Public consumption, on the other hand, declined by 0.3% (3Q 10: -10.2%), arising from lower expenditure on supplies and services. Gross fixed capital formation increased by 9.2% (3Q 10: 9.8%) driven by both public and private capital spending. Private sector capital spending was led by the expansion in the production of domestic-oriented industries amid high levels of capacity utilisation. Public sector capital investment rose as a result of higher development expenditure mainly in the education and transportation sectors.

On the supply side, all economic sectors, with the exception of the primary sectors, continued to expand further in the fourth quarter. Growth in the services sector was higher at 6.2% (3Q 10: 5.4%) with expansion in all sub-sectors,

supported mainly by domestic economic activity. The construction sector also registered higher growth of 5.6% (3Q 10: 2.8%), reflecting expansion in the non-residential and civil engineering sub-sectors. The manufacturing sector expanded at a more moderate pace of 6.2% (3Q 10: 7.5%) mostly on account of the weaker external demand. The agriculture sector, however, registered a contraction of 4.3% (3Q 10: 2.7%) attributed to the decrease in palm oil output. The mining sector contracted further (-1.3%; 3Q 10: -1%) due to continued decline in production of crude oil.

The headline inflation rate, as measured by the change in the Consumer Price Index (CPI), increased by 2% on an annual basis in the fourth quarter (3Q 10: 1.9%). The increase in inflation was attributable mainly to higher price of *food and non-alcoholic beverages* which rose by 2.9% and *transport* (4Q 10: 2.5%, 3Q 10: 2.1%) reflecting the further removal of fuel subsidies by the Government which resulted in an upward adjustment of 5 sen/litre for RON95 petrol and diesel prices.

In the external sector, the trade surplus widened to RM25.5 billion in the fourth quarter (3Q 10: RM22.3 billion). Both gross exports and imports increased at a more moderate pace of 3.7% and 10.1% respectively (3Q 10: 10.4% and 16.5% respectively), in line with the moderation of the global economy. The slower growth in exports was due mainly to the lower exports of manufactured products, reflecting the softening global demand for electronics. The moderation in gross imports reflected mainly lower intermediate imports while imports of capital and consumption goods were sustained amidst strengthening domestic demand.

On a cash basis, gross inflows of foreign direct investment (FDI)\* were higher at RM11.8 billion in the fourth quarter (3Q 10: +RM8.5 billion), reflecting mainly larger inflows of equity capital. After adjusting for gross outflows due to repayment of inter-company loans, net FDI increased to RM8.3 billion (3Q 10: +RM4.4 billion). FDI was channelled mainly into the services, manufacturing and mining sectors. Investments in the services sector were primarily undertaken by companies in the finance, insurance and business services, as well as wholesale and retail trade sub-sectors. In the manufacturing sector, the FDI was channelled into the electrical and electronics as well as petroleum-related industries. Direct investment abroad (DIA)\* by Malaysian companies recorded a lower net outflow of RM3.2 billion in the fourth quarter (3Q 10: -RM5.4 billion) due to lower net extensions of inter-company loans to subsidiaries abroad. These investments were undertaken by the services sector, particularly in the finance, insurance and business services, and wholesale and retail trade sub-sectors. There were also sizeable investments in the oil and gas and the agriculture sectors. Portfolio investment registered a smaller net inflow of RM2.8 billion in the fourth quarter (3Q 10: +RM9.8 billion), due partly to net foreign liquidation of debt securities in November as investors reacted to the sovereign debt concerns in the eurozone. Nevertheless, steady growth in the domestic economy has continued to attract inflows of foreign funds into the domestic equity and bond markets.

The international reserves of Bank Negara Malaysia amounted to RM328.6 billion (equivalent to USD106.5 billion) as at 31 December 2010. This level of reserves has taken into account the quarterly adjustment for foreign exchange revaluation gain, following the strengthening of most major currencies against the ringgit during the quarter. As at 31 January 2011, the reserves position amounted to RM333.5 billion (equivalent to

USD108.1 billion), sufficient to finance 8.7 months of retained imports and is 4.2 times the short-term external debt.

### Monetary policy is supportive of economic activity

The Overnight Policy Rate (OPR) was left unchanged at 2.75% in the fourth quarter of 2010 and also at the MPC meeting held on 27 January 2011. At the prevailing level, the OPR remains accommodative and is considered to be appropriate and consistent with the assessment of growth and inflation prospects.

Reflecting the unchanged OPR, the average overnight interbank rate was stable. In terms of the commercial banks' lending rates, the average lending rate edged lower following a foreign currency loan issued at a lower lending rate by a foreign banking institution. The average fixed deposit (FD) rates were unchanged.

Financing conditions remained supportive of economic activity. The demand for financing from both the public and private sectors was supported by continued access to financing, the reasonably low cost of borrowing and ample liquidity in the financial system. Total gross financing raised by the private sector through the banking system and capital market increased to RM220.9 billion in the fourth quarter (3Q 10: RM189.4 billion). On a net basis, banking system loans and PDS outstanding rose by an annual rate of 11.4% as at end-December (3Q 10: 10.9%). Major loan indicators remained strong in the fourth quarter.

Net funds raised in the capital market by both the public and private sectors amounted to RM30.5 billion (3Q 10: RM16.8 billion). In the private sector, fund raising activity was mainly from the bond market. In the public sector, funds were raised through issuances of Malaysian Government Securities (MGS) and Government Investment Issues (GI).

\* The statistics for FDI and DIA on a cash basis does not include retained earnings.

Monetary aggregates continued to grow at a sustained pace in the fourth quarter. M3, or broad money, expanded at an annual growth rate of 7% as at end-December 2010 (3Q 10: 8.5%).

During the quarter, the ringgit appreciated marginally (+0.1%) against the US dollar. The appreciation of the ringgit towards the end of the year following renewed optimism on the growth outlook for Asia roughly offset its earlier depreciation in October and November amid higher risk aversion following concerns over the European sovereign debt problems and tensions in the Korean Peninsula. The ringgit also appreciated against the euro (+2.9%), pound sterling (+2.2%) but depreciated against the Japanese yen (-2.4%). Against regional currencies, the ringgit broadly depreciated in the range -0.1% to -1.7% as country specific factors led to the strengthening of these currencies against the ringgit. The ringgit, however, strengthened by 0.7% against the Indonesian rupiah.

### Financial stability preserved

Financial stability was maintained throughout the fourth quarter, supported by sound financial institutions and orderly financial markets which provided continued support for financial intermediation in the domestic economy.

On 3 November 2010, the Bank introduced the maximum limit on loan-to-value (LTV) ratio of 70% for the third house financing facility taken by a borrower. The implementation of the LTV ratio is aimed at promoting a stable and sustainable property market, and ensuring the continued affordability of homes for the general public.

The banking sector remained financially resilient, with strong capital buffers of more than RM60 billion. Profitability was sustained amidst continued growth in lending activity with average returns on assets and equity at 1.5% and 16.5% respectively. Financing was broad-based, with financing to households and SME's accounting for about 70% of

total outstanding financing. Capitalisation was strong with risk-weighted capital ratio of 14.6% and core capital ratio of 12.8%. Meanwhile, the level of net non-performing loans (including impaired financing) improved slightly to account for 2% of total loans. The loan loss coverage strengthened further to 99.5% providing additional buffer to the banking sector.

The capital adequacy ratio for the insurance industry was 225.7% (3Q 10: 222.7%). For the year as a whole, profits of insurance and takaful operators improved to RM16.3 billion (2009: RM14.6 billion) due mainly to improved investment performance, more favourable claims experience in the general business segment and continued business expansion.

### Recovery to remain uneven across different regions

Going forward, the global economic recovery is expected to remain uneven across the different regions. While short-term prospects for the advanced economies have improved recently, uncertainties remain over weak fiscal positions, high unemployment and constrained lending conditions. In contrast, the growth outlook for Asia remains favourable, supported by robust domestic demand. The regional economies are, however, confronted with the challenges of rising inflationary pressures, particularly from high commodity and fuel prices, and the large and volatile capital flows.

The pace of growth of the Malaysian economy will be affected by the environment of moderating external demand. Growth will, nevertheless, be supported by continued firm expansion in domestic demand. Private consumption spending will continue to benefit from the favourable labour market conditions, firm commodity prices and access to financing. The roll-out of construction and infrastructure activities and the implementation of the economic transformation programme by the Government are likely to provide significant support to the growth momentum in private investment.

## DEVELOPMENTS IN THE FOURTH QUARTER OF 2010

### INTERNATIONAL ECONOMIC ENVIRONMENT

#### Uneven recovery in the global economy amid renewed sovereign debt crisis in the euro area

The global economic recovery continued to be uneven in the fourth quarter. Growth in the advanced economies remained moderate as these economies continued to face headwinds in terms of persistent high unemployment, sluggish lending activity and growing concerns over fiscal sustainability. Although its economic fundamentals remained weak, US growth strengthened in the fourth quarter due to better-than-expected private consumption. In Asia, growth remained strong, as resilient domestic demand continued to provide support to economic activity. The expansion, however, was at a more moderate pace compared to the strong performance in the first half of the year in part due to the slower pace of improvement in external demand. Conditions in the international financial markets deteriorated during the quarter, particularly in November, following uncertainty over Ireland's fiscal position. This eventually led to a €85 billion EU-IMF bailout package for Ireland on 28 November which was aimed at restructuring the Irish banking system and safeguarding its public finances. In view of the divergence between further accommodative monetary stance in the advanced economies and policy normalisation in the emerging economies, particularly Asia, capital flows into the Asian region continued to remain large. In response, authorities in several Asian countries further introduced wide-ranging measures to mitigate the impact of capital flows on macroeconomic and financial stability.

In the **US**, real GDP grew faster by 3.2% on an annualised basis, (3Q 10: 2.6%) due to a stronger expansion in private consumption towards the latter part of the quarter. Private consumption increased as households drew down their savings following a slower pace of deleveraging and the better prospects for a turnaround in the employment outlook as monthly job creation averaged 128,000 during the quarter (3Q 10: -30,000). However, consumer sentiment remained soft relative to

historical norms, reflecting concerns over the persistently high unemployment rate which had remain above 9% since May 2009. Growth was also contributed by net exports due to a sharp decrease in imports following a rapid deceleration in inventory restocking. Fixed investment, in particular for equipment and software, remained supportive of growth, albeit at lower rates compared to the earlier period of the economic recovery. On the inflation front, headline CPI rose by 1.3% during the quarter (3Q 10: 1.2%), due to higher energy prices. On 3 November, the **Federal Reserve** (Fed) introduced a second round of quantitative easing amounting to USD600 billion to support the fragile economic recovery and address concerns over rising deflationary pressures. The measures are aimed at bolstering private sector demand, particularly consumption of households, through the lowering of long-term yields for residential mortgage payments and higher wealth effect from rising equity prices. Households received a further boost from the unveiling of a USD858 billion tax relief package (5.9% of GDP) in December, which included the extension of Bush era tax cuts and unemployment benefits.

In the **euro area**, growth on a quarter-on-quarter basis was sustained at 0.3% in the fourth quarter (3Q 10: 0.3%). On an annual basis, the economy grew by 2% in the fourth quarter (3Q: 1.9%). Growth was supported by an improvement in both exports and domestic demand for the core economies, in particular in Germany, while economic activity remained weak in the peripheral economies. On the inflation front, consumer prices rose by 2% (3Q 10: 1.7%), due to higher energy and food prices. The Irish crisis eventually led to a €85 billion EU-IMF package for Ireland's banking restructuring and public sector finance restoration on 28 November. During the quarter, the **European Central Bank** (ECB) utilised the Securities Market Programme which was introduced earlier in May as it purchased government bonds of the affected euro area economies to stabilise their respective borrowing costs.

### Advanced Economies: Real GDP Growth

	2009		2010			Key contributing factors for 4Q growth
	4Q	Year	3Q	4Q	Year	
	Annual change (%)					
US <sup>1</sup>	5.0	-2.6	2.6 <sup>r</sup>	3.2 <sup>a</sup>	2.9	Growth contributed by private consumption, net exports and investment in equipment and software.
Japan <sup>1</sup>	7.3	-6.3	3.3 <sup>r</sup>	-1.1 <sup>p</sup>	3.9	Contraction due to slower improvement in external demand and decline in private consumption following expiry of government subsidies.
Euro area	-2.0	-4.1	1.9	2.0 <sup>p</sup>	1.7	Growth supported by an improvement in both external and domestic demand in the core economies.
UK	-2.8	-4.9	2.7 <sup>r</sup>	1.7 <sup>p</sup>	1.4	Moderation due mainly to decline in the construction and services sectors.

<sup>1</sup> Annualised basis

<sup>r</sup> Revised

<sup>a</sup> Advance estimate

<sup>p</sup> Preliminary

Source: National authorities

The **UK** economy experienced a quarter-on-quarter contraction of 0.5% (3Q 10: 0.7%) in the fourth quarter. On an annual basis, growth moderated to 1.7% (3Q 10: 2.7%). The unexpected weaker growth was attributed mainly to a decline in the construction and services sectors, as economic activity was significantly affected by bad weather conditions. The economy, however, continued to be supported by an improvement in both production and exports. On the domestic demand side, private consumption weakened as indicated by slower retail sales and continued decline in consumer confidence following the prospects of further fiscal austerity measures. Meanwhile, inflation grew at a faster rate of 3.3% during the quarter (3Q 10: 3.1%) driven mainly by higher commodity prices. In balancing the weaker growth prospects and the risk of stronger inflation, the Bank of England (BOE) decided to leave its policy rate unchanged at 0.5% and maintained the size of its asset purchase programme at £200 billion.

The **Japanese** economy contracted by 1.1% on an annualised basis (3Q 10: 3.3%) in the fourth quarter, due to slowing external demand and renewed weakness in domestic demand upon the expiry of government subsidies. On an annual basis, the economy grew at a slower rate of 2.2% (3Q 10: 4.9%). Exports moderated sharply to 10% y-o-y (3Q 10: 17.8%) due to weaker external demand and to some extent, the impact of strong yen. Meanwhile, household spending declined by 1.4% (3Q 10: 0.9%) upon the expiry of government stimulus while the unemployment rate remained elevated at 5% (3Q 10: 5.1%). Deflationary

pressures persisted as core consumer prices (excluding fresh food) continued to decline by 0.5% (3Q 10: -1.1%). In response to the weaker economy amid strong yen and deflation, the **Bank of Japan** (BoJ) reduced the overnight call rate to a range of 0 - 0.1% in October and further established a ¥5 trillion (USD60 billion) asset purchase programme to acquire government and corporate bonds.

In the **Asian** region, economic activities in most economies remained strong in the fourth quarter as growth continued to be supported by resilient domestic demand, particularly private consumption, in light of improving labour market conditions and a strong growth in bank lending. However, the rate of expansion moderated from the first half of the year, reflecting a more modest improvement in external demand and slower inventory restocking activity. Growth in **PR China** expanded by 9.8% due to robust domestic demand in spite of a series of tightening measures during the quarter. **Singapore's** economy recorded a strong growth of 12.0% (3Q 10: 10.5%), driven mainly by the volatile biomedical manufacturing cluster. In **Korea**, the economy grew by 4.8% (3Q 10: 4.4%), supported by strong exports activity while the **Philippines'** economy expanded by 7.1% (3Q 10: 6.3%), led by strong household consumption and accelerated investments, particularly in durable equipment investments. In **Indonesia**, the economy grew by 6.9% (3Q 10: 5.8%), supported by strong investment activities and public spending. Meanwhile, the **Chinese Taipei** economy expanded by 6.9% (3Q: 10.7%) due mainly to a moderation in exports.

Amid favourable growth and rising inflationary pressures associated with higher commodity and fuel prices, several central banks in the region continued to normalise their policy interest rates to a level consistent with the prevailing economic conditions. In response to rising inflationary pressures where inflation peaked at a 28-month high in November, the **People's Bank of China (PBOC)** raised its one-year deposit and lending rates twice by 25 basis points each to 2.75% and 5.81% in October and December, as well as increasing reserve requirement ratio three times during the quarter by 50 basis points each, to 18.5% for the major banks. In January 2011, the central bank further raised the reserve requirement ratio to 19%. The **Central Bank of the Republic of China (Taiwan)** increased its discount rate by 12.5 basis points to 1.625% in December while the **Bank of Thailand** and the **Bank of Korea** hiked their policy rates by 25 basis points to 2.25% and 2.75% respectively in January 2011. In addition, several monetary authorities in the region also took further steps to manage capital inflows by imposing levies or taxes on foreign inflows (Korea and Thailand) and utilising macroprudential measures in

limiting foreign currency exposure of the banking system (Chinese Taipei, Korea and Indonesia). Several authorities such as in Hong Kong, Singapore and Thailand also introduced administrative measures to discourage speculative activities in the domestic real estate sector.

Prices of **crude oil**<sup>1</sup> generally trended upwards in the fourth quarter, averaging USD85 per barrel (3Q: USD76 per barrel). Oil prices rose to USD88 per barrel on 11 November following the announcement of a second round of quantitative easing by the Fed. This trend subsequently reversed, with oil prices touching a low of USD80 per barrel on 17 November as market sentiments were tempered by anticipation of further policy tightening by PR China, the second largest oil consumer, and renewed concerns over the sovereign debt problem in the euro area. Nevertheless, oil prices resumed its upward trend in December ahead of rising winter demand and tighter inventory conditions in the US. At the end of the year, crude oil traded at USD91 per barrel, representing a 27-month high as well as an increase of 15% from the level at the end of 2009.

#### Regional Countries: Real GDP Growth

	2009		2010			Key contributing factors for 4Q growth
	4Q	Year	3Q	4Q	Year	
	Annual change (%)					
Singapore	4.6 <sup>r</sup>	-0.8 <sup>r</sup>	10.5 <sup>r</sup>	12.0	14.5	Underpinned by strong expansion in the manufacturing sector, led by the biomedical manufacturing cluster.
PR China	10.7	9.2	9.6	9.8	10.3	Supported largely by robust domestic demand.
Philippines	6.0	1.1	6.3	7.1	7.3	Growth led by strong household consumption and investment.
Indonesia	5.4	4.5	5.8	6.9	6.1	Supported by strong investment activities and public sector spending.
Chinese Taipei	9.2	-1.9	10.7	6.9 <sup>p</sup>	10.8	Due mainly to a moderation in export performance while domestic demand remained resilient.
Korea	6.0	0.2	4.4 <sup>r</sup>	4.8 <sup>p</sup>	6.1	Driven by stronger export performance and sustained expansion in private consumption.

<sup>r</sup> Revised  
<sup>p</sup> Preliminary

Source: National authorities

<sup>1</sup> Refers to West Texas Intermediate one-month futures on NYMEX

In the **foreign exchange markets**, the US dollar weakened against most currencies but strengthened against the euro and the pound sterling. The US dollar broad weakness was largely attributable to the anticipation of further quantitative easing by the Fed in November. Both the euro and pound sterling weakened against the dollar following renewed sovereign debt concerns arising from the Irish debt crisis, further rating downgrades and concerns over the impact of fiscal austerity measures on the recovery process. On the other hand, the yen continued to strengthen against the US dollar, to reach a 15-year high of ¥80 in October, benefiting from its role as a safe haven currency amid heightened investor risk aversion in the global financial market. Most regional currencies also strengthened against the US dollar in the fourth quarter following continued capital flows into the region amid optimism over the region's favourable growth prospects. On 4 November,

the Singapore dollar traded at a record high of S\$1.2824 per US dollar but weakened subsequently during the month due to rising geopolitical tension in the Korean peninsula and the escalation of sovereign debt crisis in Ireland. The Chinese yuan ended the quarter at a 17-year high of 6.5897 per US dollar.

Going forward, the global economic recovery is expected to remain uneven across the different regions. While short-term prospects for the advanced economies have improved recently, uncertainties remain over weak fiscal positions, high unemployment and constrained lending conditions. In contrast, the growth outlook for Asia remains favourable, supported by robust domestic demand. The regional economies are, however confronted with the challenges of both rising inflationary pressures, particularly from high commodity and fuel prices, and the large and volatile capital flows.

## DEVELOPMENTS IN THE MALAYSIAN ECONOMY

### Growth moderated in the fourth quarter

The Malaysian economy registered a growth of 4.8% in the fourth quarter, driven by stronger domestic demand amid weaker external demand. The stronger expansion in domestic demand was supported by both private and public sector spending. The slower growth in the global economy, however, had led to the weaker growth in external demand. On the supply side, all economic sectors, with the exception of the primary sectors, continued to expand during the quarter. Rounding up for the year, the Malaysian economy expanded by 7.2% (2009: -1.7%).

### Domestic demand increased further

**Domestic demand** expanded by 5.7% in the fourth quarter (3Q 10: 5%), due mostly to the expansion in private consumption and capital spending.

**Private consumption** grew by 6.5% in the fourth quarter (3Q 10: 7.1%), supported by favourable labour market conditions, positive consumer sentiments and higher income levels. Consumer spending was also encouraged by the sales promotions held during the festive period as well as the long school holidays in December. Major consumption indicators such as credit card spending, sales of passenger cars and bank lending for consumption recorded a strong performance, pointing to robust consumption activity during the quarter. The fourth quarter MIER Consumer Sentiments Index increased to 117.2 points (3Q 10: 115.8 points), reflecting positive consumer confidence.

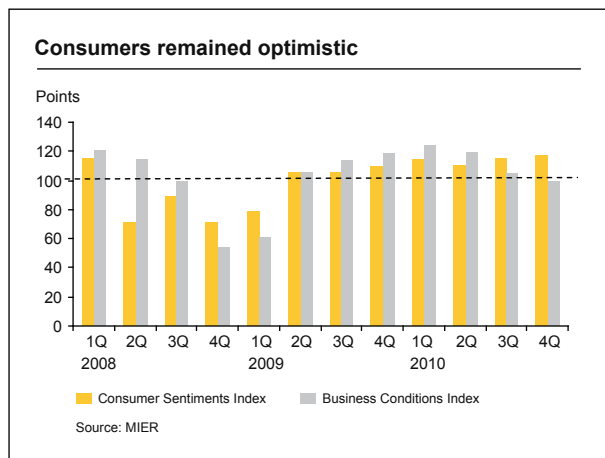
### GDP by Expenditure Components (at constant 2000 prices)

	2009		2010		
	4Q	Year	3Q	4Q	Year
	Annual change (%)				
Aggregate Domestic Demand (excluding stocks)	2.8	-0.5	5.0	5.7	6.3
Consumption	1.4	1.2	3.5	4.7	5.3
<i>Private sector</i>	1.6	0.7	7.1	6.5	6.6
<i>Public sector</i>	0.7	3.1	-10.2	-0.3	0.1
Gross Fixed Capital Formation	8.2	-5.6	9.8	9.2	9.4
Net Exports	-4.7	5.0	-31.7	-18.3	-24.2
<i>Exports of Goods and Services</i>	6.0	-10.4	6.6	1.5	9.8
<i>Imports of Goods and Services</i>	7.0	-12.3	11.0	3.3	14.7
<b>GDP</b>	<b>4.4</b>	<b>-1.7</b>	<b>5.3</b>	<b>4.8</b>	<b>7.2</b>

Source: Department of Statistics, Malaysia

**Public consumption** declined by 0.3% (3Q 10: -10.2%), due to lower expenditure on supplies and services.

**Gross fixed capital formation** increased by 9.2% (3Q 10: 9.8%) driven by expansion in both private and public capital spending. Private sector investment benefited from expansion in production of domestic-oriented industries amid the high levels of capacity utilisation. Major investment indicators such as imports of capital goods and sales of commercial vehicles pointed to continued expansion in investment activity. Public sector investment accelerated during the quarter, providing additional impetus to domestic economic activity. Major components of development expenditure in the fourth quarter include spending for education and transportation sectors.



**GDP by Economic Activity (at constant 2000 prices)**

	2009		2010		
	4Q	Year	3Q	4Q	Year
	Annual change (%)				
Agriculture	5.9	0.4	2.7	-4.3	1.7
Mining	-2.8	-3.8	-1.0	-1.3	0.2
Manufacturing	5.0	-9.4	7.5	6.2	11.4
Construction	9.3	5.8	2.8	5.6	5.2
Services	5.2	2.6	5.4	6.2	6.8
<b>Real GDP (Annual Change)</b>	<b>4.4</b>	<b>-1.7</b>	<b>5.3</b>	<b>4.8</b>	<b>7.2</b>
<b>Real GDP (Preceding Change)</b>	<b>2.0</b>	<b>-1.7</b>	<b>2.5</b>	<b>1.5</b>	<b>7.2</b>

Source: Department of Statistics, Malaysia

## Continued growth across most sectors

On the supply side, most economic sectors, registered further growth in the fourth quarter. Growth in the **services sector** was higher with broad-based expansion in all sub-sectors, supported by favourable domestic demand conditions amid positive consumer sentiments. The **construction sector** also improved, supported mainly by the non-residential and civil engineering sub-sectors. The **manufacturing sector** continued to expand, but at a more moderate pace amid weaker external demand. The **agriculture sector** declined during the quarter as a result of the decrease in crude palm oil output. The **mining sector** contracted further due to continued decline in crude oil production.

## Continued improvement in domestic-oriented industries

Value-added in the manufacturing sector grew at a more moderate pace of 6.2% in the fourth quarter (3Q 10: 7.5%), as continued improvements in the domestic-oriented industries were more than offset by slower growth in the export-oriented industries.

Growth in the **export-oriented industry** moderated to 4.5% (3Q 10: 6.4%) despite improved performance in the primary-related cluster as growth in the E&E cluster slowed further following declines in the production of computers and parts, and semiconductors.

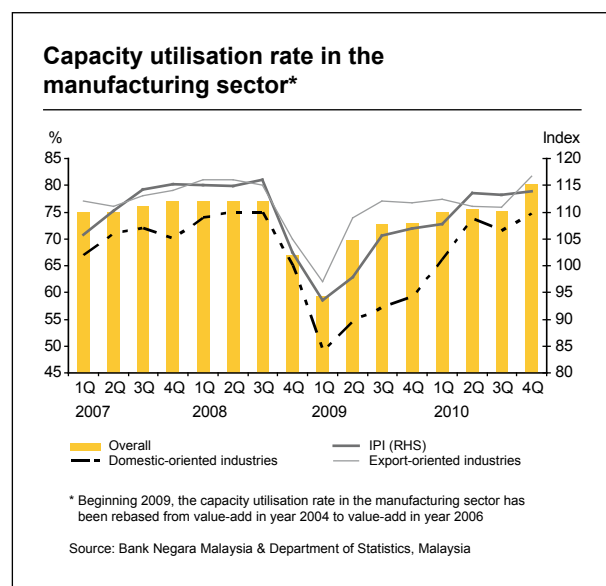
On the other hand, the **domestic-oriented industry** grew stronger by 13.3% (3Q 10: 9.8%), driven mainly by the continued robust expansion in the construction-related cluster. The consumer-related cluster also registered positive growth, supported by expansions in the transport and beverages segments.

**Performance in the Manufacturing Sector**

	2009		2010		
	4Q	Year	3Q	4Q	Year
	Annual Change (%)				
<b>Value Added (at constant 2000 prices)</b>	<b>5.0</b>	<b>-9.4</b>	<b>7.5</b>	<b>6.2</b>	<b>11.4</b>
<b>Overall Production<sup>1</sup></b>	<b>4.4</b>	<b>-10.0</b>	<b>7.2</b>	<b>6.4</b>	<b>11.0</b>
<b>Export-oriented industries</b>	<b>4.1</b>	<b>-11.1</b>	<b>6.4</b>	<b>4.5</b>	<b>9.7</b>
<b>Electronics and electrical products cluster</b>	<b>1.8</b>	<b>-22.8</b>	<b>9.6</b>	<b>0.2</b>	<b>17.4</b>
<i>Of which:</i>					
Electronics	0.8	-24.6	-7.4	-16.4	3.2
Electrical products	4.0	-18.8	44.4	34.8	47.4
<b>Primary-related industry cluster</b>	<b>5.5</b>	<b>-3.5</b>	<b>4.7</b>	<b>7.0</b>	<b>5.7</b>
<i>Of which:</i>					
Chemicals and chemical products	19.5	-1.7	8.0	4.1	11.3
Petroleum products	-6.9	-0.8	0.2	16.3	-2.4
Rubber products	16.2	-3.0	17.5	12.7	20.8
Off-estate processing	8.5	-2.1	2.9	-14.1	-2.3
<b>Domestic-oriented industries</b>	<b>5.5</b>	<b>-5.7</b>	<b>9.8</b>	<b>13.3</b>	<b>15.6</b>
<b>Construction-related cluster</b>	<b>2.5</b>	<b>-11.4</b>	<b>9.3</b>	<b>22.0</b>	<b>18.8</b>
<i>Of which:</i>					
Construction-related materials	-2.5	-18.1	14.8	19.9	21.8
Fabricated metal products	10.1	-1.1	2.5	24.8	15.0
<b>Consumer-related cluster</b>	<b>7.8</b>	<b>-1.2</b>	<b>10.1</b>	<b>7.4</b>	<b>13.3</b>
<i>Of which:</i>					
Transport equipment	-8.3	-12.4	20.7	21.0	29.8
Food, beverage & tobacco products	12.0	1.5	11.1	8.7	8.7

<sup>1</sup> Industrial Production Index (2005=100)  
Source: Department of Statistics, Malaysia

Overall capacity utilisation rate in the manufacturing sector increased to 80% in the fourth quarter (3Q 10: 75%), reflecting sustained production in the sector. Export- and domestic-oriented industries were operating at 82% and 75% of total capacity respectively (3Q 10: 76% and 71% respectively).



### Better performance in the services sector

The **services sector** recorded a higher growth of 6.2% during the quarter (3Q 10: 5.4%), supported mainly by the continued expansion in domestic economic activity. The sector remained the largest contributor to growth, contributing 3.6 percentage points to the overall GDP growth. Growth was driven mainly by the wholesale and retail trade; real estate and business services; and communication sub-sectors.

The **wholesale & retail trade** sub-sector registered a growth of 8.2% (3Q 10: 5.7%), in tandem with continued growth in private consumption, and reflective of the positive consumer sentiments and year-end sales. The communication sub-sector continued its robust expansion to grow by 9.8% (3Q 10: 9.1%) as demand for broadband and mobile data services remained high. The real estate and business services sub-sector registered a higher growth of 8.7% (3Q 10: 6.2%), following the improvement in capital market activity.

### Performance of the Services Sector (value added at constant 2000 prices)

	Share 2009 (%)	2009		2010		
		4Q	Year	3Q	4Q	Year
		Annual change (%)				
<b>Intermediate Services</b>	<b>43.6</b>	<b>8.0</b>	<b>3.4</b>	<b>6.7</b>	<b>5.8</b>	<b>7.0</b>
Finance & insurance	20.4	10.5	5.1	6.4	3.4	6.1
Real estate & business services	9.4	7.2	2.4	6.2	8.7	7.8
Transport & storage	6.6	2.6	-2.8	5.5	5.1	6.9
Communication	7.2	7.1	6.0	9.1	9.8	8.5
<b>Final Services</b>	<b>56.4</b>	<b>3.3</b>	<b>2.0</b>	<b>4.4</b>	<b>6.4</b>	<b>6.6</b>
Wholesale & retail trade	23.2	3.6	1.2	5.7	8.2	7.9
Accommodation & restaurant	4.3	2.2	2.8	5.1	3.4	5.0
Utilities	5.2	9.1	0.4	4.0	4.3	8.2
Government services	13.2	0.4	2.0	2.7	6.9	6.5
Other services	10.5	4.2	4.4	3.7	3.9	4.0
<b>Total Services</b>	<b>100.0</b>	<b>5.2</b>	<b>2.6</b>	<b>5.4</b>	<b>6.2</b>	<b>6.8</b>

Source: Department of Statistics, Malaysia

### Selected Quarterly Indicators in the Services Sector

	2009	2010			
	4Q	1Q	2Q	3Q	4Q
	<b>Index</b>				
MIER Consumer Sentiments Index	109.6	114.2	110.4	115.8	117.2
MIER Retail Trade Index	111.0	106.9	134.1	140.0	132.0
MIER Tourism Market Index	114.1	120.5	118.2	118.8	124.6
	<b>Annual change (%)</b>				
Tourist arrivals	9.5	5.3	3.9	5.6	1.2
Total passenger traffic at all airports	15.8	20.3	14.1	10.0	6.3
Total consumption credit outstanding	7.6	9.5	10.6	10.7	9.9
Loans outstanding to the wholesale & retail trade, hotels & restaurants	-1.0	4.5	8.6	7.3	7.5
Imports of consumption goods	6.3	18.5	13.3	3.2	6.9
Total sales of motor vehicles	17.6	22.7	17.4	3.7	9.3
Container cargo handled (Port Klang and PTP)	11.8	22.5	21.3	10.9	9.6

Source: Various sources

The **finance and insurance** sub-sector expanded by 3.4% (3Q 10: 6.4%) supported mainly by the finance segment due to favourable loan growth during the quarter. Meanwhile, growth in the transport and storage sub-sector moderated due mainly to the lower growth in cargo-related transport services arising from the moderation in trade activities.

### Performance of the Agriculture Sector

	2009		2010		
	4Q	Year	3Q	4Q	Year
	<b>Annual change (%)</b>				
<b>Value Added (at constant 2000 prices)</b>	<b>5.9</b>	<b>0.4</b>	<b>2.7</b>	<b>-4.3</b>	<b>1.7</b>
Industrial Crops	5.4	-4.6	-2.2	-10.4	-2.6
Food Crops	6.6	7.2	8.4	4.0	7.0
<b>Production</b>					
<i>Of which:</i>					
Crude palm oil	6.4	-1.0	3.1	-15.1	-3.3
Rubber	19.6	-20.1	0.3	6.1	9.6
Fish	7.9	12.2	6.1	2.4	2.7
Livestock	13.0	7.6	2.6	-2.2	2.4

Source: Malaysian Palm Oil Board (MPOB)  
Malaysian Rubber Board (MRB)  
Fisheries Department, Malaysia  
Department of Veterinary Services, Malaysia  
Department of Statistics, Malaysia

### Performance of the Mining Sector

	2009		2010		
	4Q	Year	3Q	4Q	Year
	<b>Annual change (%)</b>				
<b>Value Added (at constant 2000 prices)</b>	<b>-2.8</b>	<b>-3.8</b>	<b>-1.0</b>	<b>-1.3</b>	<b>0.2</b>
<b>Production</b>					
<i>Of which:</i>					
Crude oil and condensates	-4.1	-4.5	-6.1	-3.4	-3.5
Natural gas	0.6	-1.6	7.2	2.0	4.4

Source: PETRONAS  
Department of Statistics, Malaysia

### Weaker performance in the commodities sector

Value-added in the **agriculture sector** contracted by 4.3% in the fourth quarter (3Q 10: 2.7%), reflecting a decline in crude palm oil output as above average rainfall curbed harvesting. Production of food crops also moderated during the quarter. The mining sector contracted by 1.3% (3Q 10: -1.0%), reflecting continued decline in the production of crude oil amid moderation in natural gas production.

### Indicators for the Construction Sector

	2009		2010		
	4Q	Year	3Q	4Q	Year
	Annual change (%)				
New sales and advertising permits	100.8	12.3	8.6	13.0	16.0
Housing approvals	111.6	4.2	43.1	31.7	23.6
Production <sup>1</sup> of construction-related materials	2.5	-11.4	9.3	22.0	18.8
Loans approved for construction	14.6	-19.1	77.0	49.7	53.6
Imports of construction materials and mineral products	10.5	-3.1	13.7	34.8 <sup>2</sup>	30.7 <sup>3</sup>

<sup>1</sup> Industrial Production Index (2005=100)

<sup>2</sup> Oct-Nov 2010

<sup>3</sup> Jan-Nov 2010

Source: Ministry of Housing and Local Government, Department of Statistics, Malaysia and Bank Negara Malaysia

### Higher growth in the construction sector

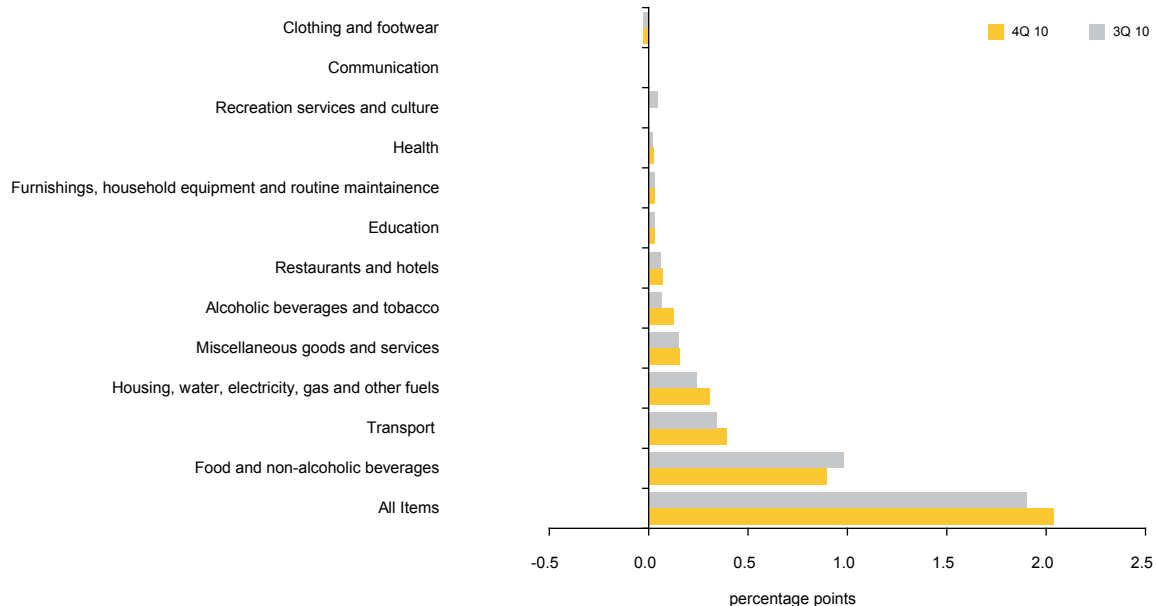
The **construction sector** registered a higher growth during the quarter (5.6%; 3Q 10: 2.8%), reflecting broad improvement in overall construction activity. The expansion in the non-residential sub-sector was due mainly to the construction of office and retail spaces, while growth in the civil engineering sub-sector was supported by the further progress in the implementation of infrastructure projects. The residential sub-sector turned around to record a positive growth in the fourth quarter.

### Inflation edged higher in the fourth quarter

The headline inflation rate, as measured by the change in the Consumer Price Index (CPI), increased by 2.0% on an annual basis in the fourth quarter (3Q 10: 1.9%). Prices in the *transport* category registered an increase of 2.5% (3Q 10: 2.1%) following the Government's subsidy rationalisation programme which saw upward adjustment in retail fuel price of 5 sen/litre for RON95 petrol and diesel. In addition, prices of RON97 have also been adjusted by a total increase of 20 sen/litre for petrol. Inflation in the *food and non-alcoholic beverages* category was unchanged at 2.9% (3Q 10: 2.9%). Within the food sub-category, higher food prices were experienced in the *sugar, jam, honey, chocolate and confectionery* sub-category as a result of the 20 sen/kg upward adjustment in the retail price of sugar while the *vegetables* sub-category recorded smaller price increases following Government efforts to ensure sufficient supply during the festive season in December. These price increases, however, were partially mitigated by declining prices in the *clothing and footwear* and *communication* categories.

The Producer Price Index (PPI) increased at a slower rate of 4.8% on a yearly basis in the

### Contribution to Consumer Price Inflation



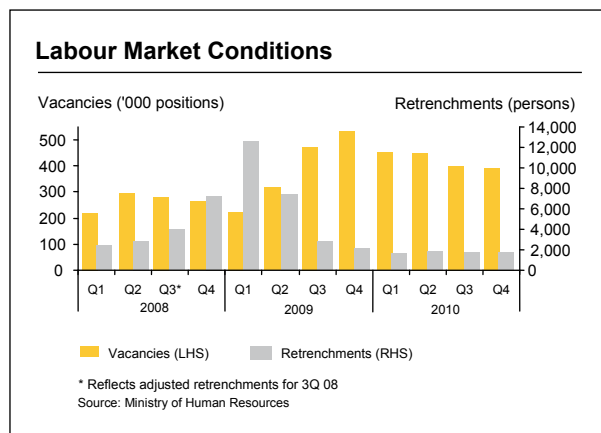
Source: Bank Negara Malaysia

fourth quarter of 2010 (3Q 10: 5.1%). Prices in the non commodity-related components of the PPI increased at a slower rate of 1.1% (3Q 10: 1.6%). Similarly, the increase in prices of commodity-related components moderated to 13.0% (3Q 10: 13.4%).

In terms of composition, prices in the imported component of the PPI were unchanged at 1.1% (3Q 10: 1.1%). Meanwhile, prices in the local component of the PPI increased at a slower rate of 6.6% (3Q 10: 7.1%) due to a moderation in the *mineral, fuels lubricants etc.* category (4Q 10: 3.4%, 3Q 10: 15.0%).

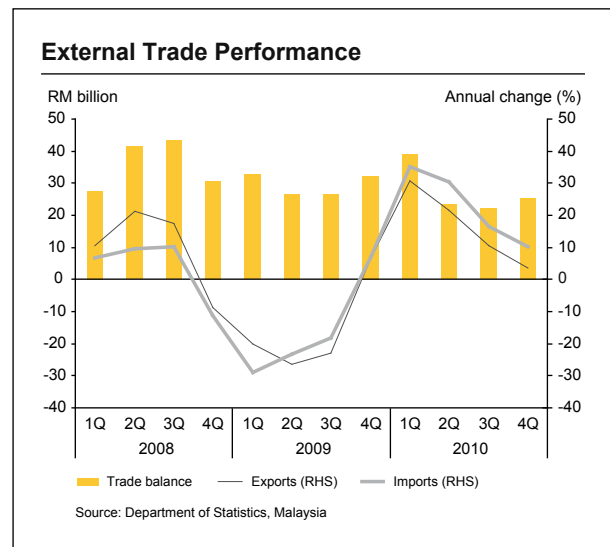
### Labour market conditions remained favourable

Conditions in the labour market continued to remain favourable. The number of retrenchments remained low and the unemployment rate declined further. Total retrenchments amounted to 1,761 persons (3Q: 1,751 persons), with the services sector accounting for a larger share of total retrenchments. Employment in the manufacturing sector remained resilient despite the moderation in external demand in the second half year. During the quarter, there was a notable decline in the number of layoffs in the manufacturing sector, particularly in the E&E sub-sector. For the first two months of the quarter, the unemployment rate eased further to 3% (3Q 10: 3.2%), due to the strong employment



growth (2.7%), which continued to outpace the growth in labour force (2.2%). The real wage per worker in the manufacturing sector grew more moderately by 0.5% (3Q 10: 1.6%).

However, during the quarter, total vacancies posted on JobsMalaysia Portal were marginally lower (393,408 positions; 3Q 10: 401,778 positions), reflecting the softer labour demand following the moderation in economic activity in the second half year. Lower number of job openings was evident across the manufacturing, services and construction sectors.



#### Trade Account

	2009		2010		
	4Q	Year	3Q	4Q	Year
	Annual change (%)				
<b>Gross Exports</b>	<b>6.6</b>	<b>-16.5</b>	<b>10.4</b>	<b>3.7</b>	<b>15.6</b>
Manufactured	11.3	-11.4	5.2	-0.6	12.0
E&E	18.4	-10.8	3.9	-8.0	9.7
Non-E&E	2.9	-12.2	6.8	9.5	15.0
Commodities	-10.0	-28.8	28.2	16.9	26.8
Agriculture	5.4	-22.7	19.3	33.1	29.5
Minerals	-17.7	-32.5	34.9	6.5	25.0
<b>Gross Imports</b>	<b>6.9</b>	<b>-16.3</b>	<b>16.5</b>	<b>10.1</b>	<b>21.7</b>
Capital goods	17.4	-5.9	21.1	9.4	16.2
Intermediate goods	0.1	-21.6	15.6	10.5	22.1
Consumption goods	6.3	-2.7	3.2	6.9	10.1
<b>Trade balance (RM billion)</b>	<b>32.4</b>	<b>118.4</b>	<b>22.3</b>	<b>25.5</b>	<b>110.2</b>

Source: MATRADE and Department of Statistics, Malaysia

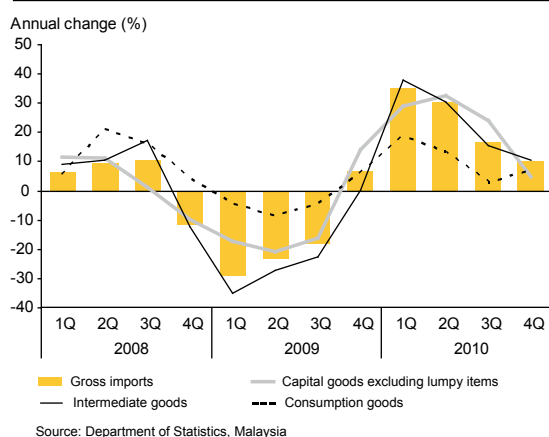
### Malaysia: Direction of Exports

	2009		2010			2009		2010		
	4Q	Year	3Q	4Q	Year	4Q	Year	3Q	4Q	Year
	Annual change (%)					Share of total exports (%)				
<b>United States</b>	-7.4	-26.7	-0.6	-10.8	0.6	10.6	10.9	9.6	9.1	9.5
<b>European Union (EU)</b>	1.0	-19.8	11.1	0.4	14.5	11.1	10.8	10.8	10.8	10.7
<b>Selected ASEAN countries<sup>1</sup></b>	13.6	-16.4	4.5	1.7	13.9	25.7	25.5	24.1	25.3	25.1
<b>North East Asia</b>	40.1	-2.8	9.8	2.5	19.7	24.6	23.8	24.7	24.3	24.6
<i>People's Republic of China</i>	60.5	6.0	3.4	0.1	19.9	12.8	12.2	12.5	12.4	12.6
<i>Hong Kong SAR</i>	38.3	2.3	-0.3	-0.4	12.8	5.2	5.2	5.1	5.0	5.1
<i>Chinese Taipei</i>	21.1	-14.4	28.8	32.6	39.9	2.6	2.6	3.4	3.3	3.2
<i>Korea</i>	8.3	-21.7	39.9	-5.6	14.7	4.0	3.8	3.6	3.6	3.8
<b>West Asia</b>	-10.2	-18.0	-15.7	11.0	1.9	3.4	3.9	3.1	3.7	3.4
<b>India</b>	-27.5	-31.3	35.2	21.9	23.3	2.8	3.1	3.5	3.3	3.3
<b>Total exports</b>	6.6	-16.5	10.4	3.7	15.6	100.0	100.0	100.0	100.0	100.0

<sup>1</sup> Singapore, Thailand, Indonesia, Philippines, Brunei Darussalam and Vietnam

Source: Department of Statistics, Malaysia

### Import Growth



### Moderation in trade activity

The **trade surplus** amounted to RM25.5 billion in the final quarter of 2010 (3Q 2010: RM22.3 billion), where both gross exports and imports moderated. Gross exports expanded at a more modest pace, following weaker external demand for electronics. Likewise, the moderation in gross imports reflected lower intermediate imports, while imports of capital and consumption goods were sustained by favourable domestic demand.

The modest growth in **gross exports** of 3.7% reflected mainly the marginal decline in **manufactured exports** (-0.6%; 3Q 10: 5.2%), which were weighed down primarily by weaker

external demand for electronics. Meanwhile, exports of non-E&E products were sustained, driven by firm regional demand for chemicals as well as optical and scientific equipment. **Commodity exports** remained robust, expanding by 16.9% (3Q 10: 28.2%), supported by higher prices and continued demand from the region.

**Gross imports** expanded at a more moderate pace due to slower growth of intermediate imports, reflecting the weaker manufactured exports. Imports of capital and consumption goods continued to register positive growth, amidst continued strengthening of domestic demand.

### Higher FDI amidst continued inflows of portfolio investment

On a cash basis, gross inflows of **foreign direct investment (FDI)\*** increased to RM11.8 billion in the fourth quarter (3Q 10: +RM8.5 billion), reflecting larger inflows of equity capital. After adjusting for gross outflows due mainly to repayment of inter-company loans, net FDI was also higher at RM8.3 billion (3Q 10: +RM4.4 billion). During the quarter, FDI was channelled mainly into the services, manufacturing and mining sectors. FDI in the services sector was mainly undertaken by companies in the finance, insurance and business services as well as wholesale and retail trade sub-sectors. In the manufacturing sector, the bulk of the inflows went to electrical and electronics (E&E) as well as petroleum-related industries. FDI in the oil and gas sub-sector remained sizeable.

\* The statistics for FDI and DIA on a cash basis does not include retained earnings.

**Direct investment abroad (DIA)\*** by Malaysian companies recorded a smaller net outflow of RM3.2 billion in the fourth quarter (3Q 10: -RM5.4 billion), reflecting mainly both lower equity capital flows and net extensions of inter-company loans to subsidiaries abroad. These investments were largely undertaken by companies in the services sector, particularly those in the finance, insurance and business services, and wholesale and retail trade sub-sectors. There were also sizeable investments in the oil and gas as well as the agriculture sectors.

Net inflows of **portfolio investment** amounted to RM2.8 billion in the fourth quarter (3Q 10: +RM9.8 billion). The smaller inflows reflected partly net foreign liquidation of debt securities in November due to the renewed global concerns over sovereign debt in the eurozone. Nevertheless, steady growth in the domestic economy continued to attract inflows of foreign funds into the domestic equity and bond markets.

### External debt declined

Malaysia's **total external debt** declined to RM226.3 billion or USD72.6 billion as at end-December 2010 (end-Sept 2010: RM227.6 billion or USD73 billion), equivalent to 30.2% of GNI.

The **medium- and long-term external debt** remained stable at RM146.9 billion (end-Sept 2010: RM146.8 billion), as the net repayment position in the public sector was offset by a

slight increase in the external debt following the strengthening of major currencies against the ringgit during the quarter. The net repayment position in the public sector was due mainly to the repayment of several large borrowings by the NFPEs. The Federal Government, however, recorded a small net drawdown. Meanwhile, external debt of the private sector registered a marginal increase during the quarter reflecting mainly higher non-bank private sector borrowings to finance their capital investment.

As at end-December 2010, the **short-term external debt** declined to RM79.4 billion or USD25.7 billion (end-Sept 2010: RM80.8 billion), due mainly to lower borrowings by the banking sector. Short-term external debt accounted for 35.1% of total external debt. The latest international reserves position as at 31 January 2011 is able to cover 4.2 times the short-term external debt.

#### External Debt Outstanding

	2009	2010	
	end-Dec	end-Sept	end-Dec <sup>P</sup>
	RM billion		
Medium- and long-term debt	155.4	146.8	146.9
Public sector	85.4	84.1	83.3
Private sector	70.0	62.7	63.6
Short-term debt <sup>1</sup>	77.8	80.8	79.4
Total external debt	233.1	227.6	226.3
USD billion equivalent	67.4	73.0	72.6
External debt/GNI (%)	35.1	30.3	30.2
Reserves/Short-term external debt (times)	4.3	3.8	4.2 <sup>2</sup>

<sup>1</sup> Excludes currency and deposits held by non-residents with resident banking institutions

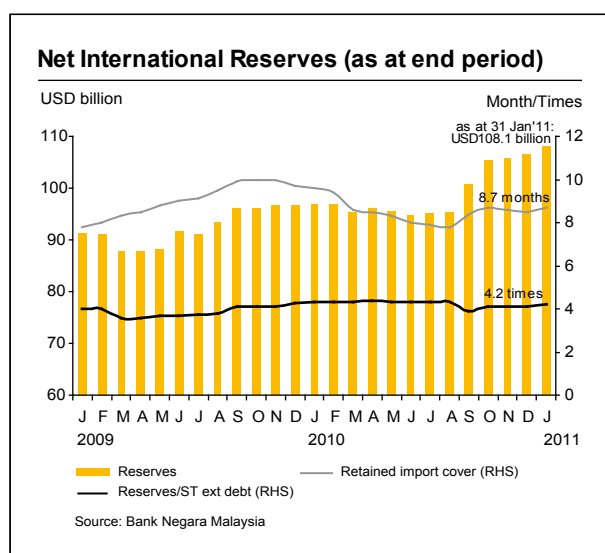
<sup>2</sup> International Reserves as at 31 January 2011

<sup>P</sup> Preliminary

Source: Ministry of Finance, Malaysia and Bank Negara Malaysia

## International reserves remained high

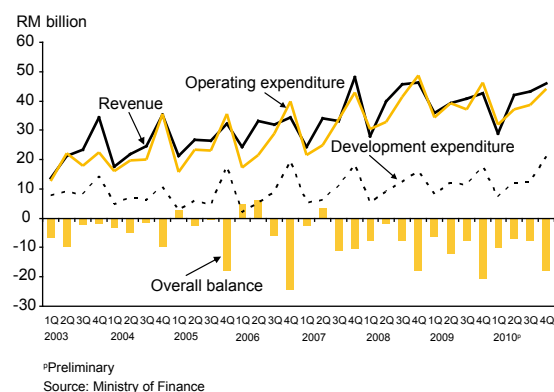
The international reserves of Bank Negara Malaysia amounted to RM328.6 billion (equivalent to USD106.5 billion) as at 31 December 2010. The reserves level as at 31 December 2010 has taken into account the quarterly adjustment of the foreign exchange revaluation gain, following the strengthening of most major currencies against the ringgit during the quarter. As at 31 January 2011, the reserves position amounted to RM333.5 billion (equivalent to USD108.1 billion), sufficient to finance 8.7 months of retained imports and is 4.2 times the short-term external debt.



## Fiscal deficit of 5.6% of GDP in 2010

The Federal Government's total expenditure in the fourth quarter was higher resulting in an overall fiscal deficit of 5.6% of GDP for the year as a whole. In particular, higher development expenditure was recorded as a result of increased spending in the education and commerce & industry sectors. Meanwhile, revenue remained favourable on account of higher collections from individual tax and indirect tax. The fiscal deficit was financed from domestic borrowings. As at end-2010, total outstanding debt of the Federal Government amounted to RM407.1 billion or 53.1% of GDP.

## Federal Government Finance



## Federal Government Finance

	2009		2010 <sup>p</sup>		
	4Q	Year	3Q	4Q	Year
	RM billion				
Revenue	42.6	158.6	43.1	45.8	159.7
% growth	-8.0	-0.7	5.7	7.6	0.6
Operating expenditure	46.2	157.1	38.6	44.1	151.6
% growth	-5.4	2.3	3.9	-4.6	-3.5
<b>Current account</b>	<b>-3.6</b>	<b>1.6</b>	<b>4.6</b>	<b>1.7</b>	<b>8.0</b>
% of GDP	<b>-2.0</b>	<b>0.2</b>	<b>2.4</b>	<b>0.8</b>	<b>1.0</b>
Gross development expenditure	17.6	49.5	12.5	20.8	52.8
% growth	9.5	15.6	8.0	18.6	6.6
<b>Overall balance</b>	<b>-20.9</b>	<b>-47.4</b>	<b>-7.8</b>	<b>-18.2</b>	<b>-43.3</b>
% of GDP	<b>-11.3</b>	<b>-7.0</b>	<b>-4.0</b>	<b>-8.9</b>	<b>-5.6</b>
<b>Memo item:</b>					
Total gross expenditure	63.8	206.6	51.1	64.9	204.4
% growth	-1.7	5.2	4.9	1.8	-1.0
Total Federal Government debt (as at end-period)	362.4	362.4	397.8	407.1	407.1
% of GDP	53.3	53.3	51.9	53.1	53.1
Domestic debt	348.6	348.6	381.4	390.4	390.4
% of GDP	51.3	51.3	49.8	51.0	51.0
External debt	13.8	13.8	16.4	16.7	16.7
% of GDP	2.0	2.0	2.1	2.2	2.2

<sup>p</sup> Preliminary

Source: Ministry of Finance

## MONETARY AND FINANCIAL DEVELOPMENTS

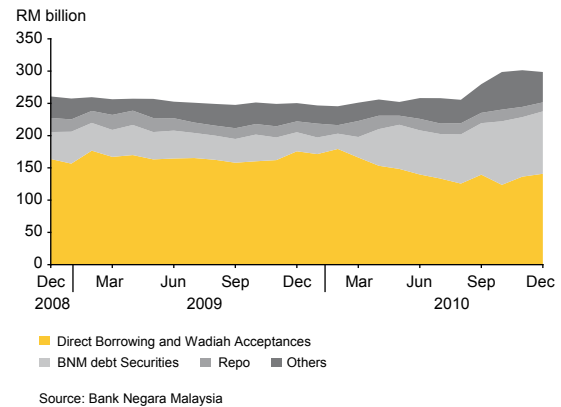
### Interest rates remained stable

The OPR was left unchanged at 2.75% in the fourth quarter of 2010 and also at the MPC meeting held on 27 January 2011. At the prevailing level, the OPR remains accommodative and is considered to be appropriate and consistent with the assessment of growth and inflation prospects.

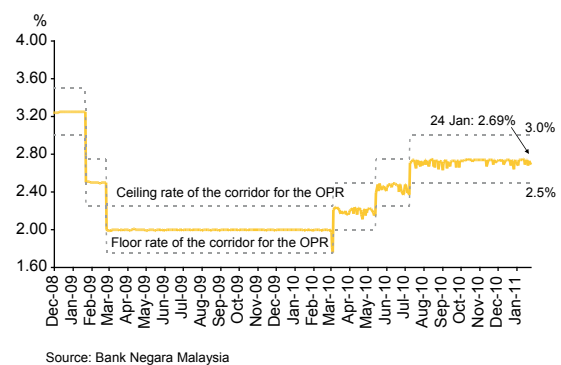
Reflecting the unchanged OPR, the average overnight interbank rate was stable, moving within a range of 2.67% to 2.75% during the period 1 October – 31 December 2010. Similarly, interbank rates of other maturities were also stable.

In terms of retail deposit rates, the average quoted fixed deposit (FD) rates of commercial banks (CBs) were relatively unchanged. As at end-December, the average quoted FD rates for tenures between 1 to 12 months ranged between 2.71% to 2.97% respectively. In terms of retail lending rates, the average base lending rate (BLR) of CBs was unchanged at 6.27%. The average lending rate (ALR) on loans outstanding, however, moderated to 5.05% (end-September: 5.19%). This was mainly due to a foreign currency loan issued at a lower lending rate by a foreign banking institution. Notably, retail lending rates remained below their pre-crisis levels.

**Outstanding Liquidity Placed with Bank Negara Malaysia (At end-period, RM billion)**



**Daily Weighted Average Overnight Interbank Rate**

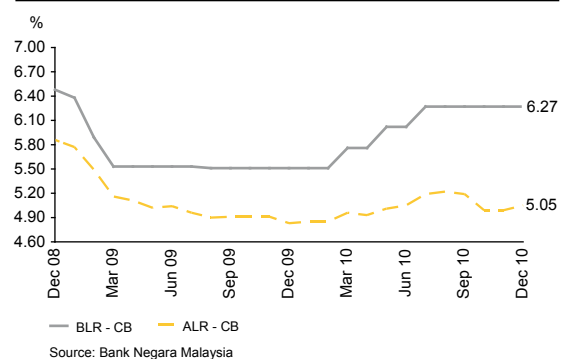


### Interest Rates

	2009		2010	
	4Q	3Q	4Q	
	At end-period (%)			
Overnight Policy Rate (OPR)	2.00	2.75	2.75	
Interbank rates				
Overnight	1.99	2.73	2.72	
1-month	2.07	2.81	2.83	
Base lending rates (BLR)				
Commercial banks	5.51	6.27	6.27	
Average lending rates (ALR)				
Commercial banks	4.83	5.19	5.05	
Fixed deposit rates				
Commercial banks				
3-month	2.03	2.73	2.74	
12-month	2.50	2.95	2.97	

Source: Bank Negara Malaysia

**Lending Rates of Commercial Banks (Average for the period)**



## Moderation in money supply growth

The monetary aggregates continued to grow at a sustained pace in the fourth quarter. M1, or narrow money increased by RM10.9 billion during the quarter. On an annual basis, M1 expanded by 11.7% as at end-December 2010 (end-September: 11.5%). M3, or broad money, expanded at an annual growth rate of 7.0% as at end-December (end-September: 8.5%). On a quarter-on-quarter basis, M3 increased by RM30.4 billion.

The main impetus for the increase in broad money was higher credit extension to the private sector by the banking system. This was accounted for by an increase in loans of RM28.9 billion and higher holdings of private debt securities by the banks. In addition, broad money also expanded due to net foreign inflows. These inflows were sterilized by the issuance of securities by BNM. Thus, deposits were withdrawn for the purchases of those securities. This was reflected by the

moderation in “net other influences” which subsequently exerted a contractionary impact on money supply.

## Private sector financing activity strengthened in the fourth quarter

In the fourth quarter, financing conditions remained supportive of economic activity. The demand for financing from both the public and private sectors were supported by continued access to financing, reasonably low cost of borrowing and ample liquidity in the financial system. Total gross financing raised by the private sector through the banking system and the capital market increased to RM220.9 billion in the fourth quarter (3Q 10: RM189.4 billion). The higher financing reflected increased loan disbursements as well as higher private debt securities (PDS) issuances and initial public offerings (IPOs) during the quarter. On a net basis, banking system loans and PDS outstanding rose by an annual rate of 11.4% as at end-December (3Q 10: 10.9%).

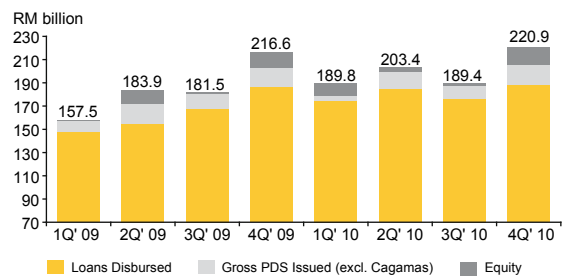
### Determinants of Broad Money, M3

	Change during the period				
	2009		2010		
	4Q	Year	3Q	4Q	Year
	RM billion				
<b>M3</b>	<b>41.5</b>	<b>85.4</b>	<b>23.9</b>	<b>30.4</b>	<b>71.5</b>
Net claims on Govt	13.5	25.8	2.7	-3.5	-8.3
Claims on private sector	19.3	51.0	22.5	29.4	96.5
Loans	14.7	46.5	17.2	28.9	92.3
Securities	4.6	4.5	5.3	0.5	4.2
Net foreign assets <sup>1</sup>	6.6	11.8	19.0	14.8	50.2
BNM	1.7	-3.4	5.9	17.1	30.8
Banking System	4.8	15.1	13.0	-2.3	19.5
Other influences	2.1	-3.1	-20.2	-10.4	-67.0

<sup>1</sup>Pre-revaluation

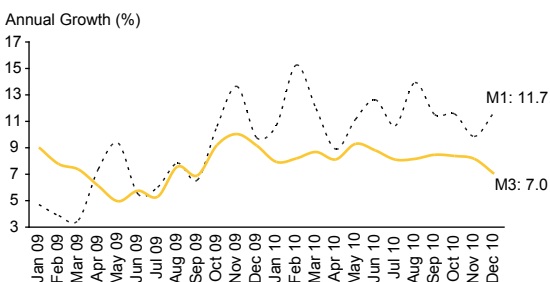
Source: Bank Negara Malaysia

### Gross Private Sector Financing through Banking System and Capital Market



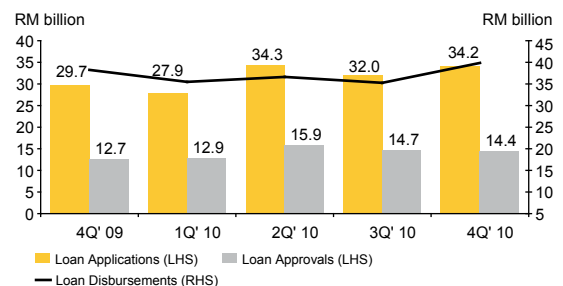
Source: Bank Negara Malaysia

### Monetary Aggregates



Source: Bank Negara Malaysia

### Bank Lending to SMEs



Source: Bank Negara Malaysia

### Financing of the Private Sector through Banking System and Capital Market

	During the period (RM billion)				Annual growth (%)		
	2009	4Q 09	3Q 10	4Q 10	2009	3Q 10	4Q 10
<b>Gross total financing</b>	<b>739.4</b>	<b>216.6</b>	<b>189.4</b>	<b>220.9</b>	<b>7.4</b>	<b>4.4</b>	<b>2.0</b>
Loans disbursed*	657.2	187.0	176.1	188.8	2.7	5.1	1.0
Gross PDS (excl. Cagamas and issuances by non-residents)	56.1	16.4	11.2	17.4	30.9	-11.3	5.9
Equity	26.0	13.2	2.1	14.7	375.5	73.6	12.0
<b>Net total financing (A)+(B)</b>	<b>82.4</b>	<b>30.1</b>	<b>25.0</b>	<b>38.2</b>	<b>8.4</b>	<b>10.9</b>	<b>11.4</b>
<b>Banking system</b>	<b>57.2</b>	<b>19.8</b>	<b>22.9</b>	<b>29.9</b>	<b>7.3</b>	<b>11.0</b>	<b>12.0</b>
Loans outstanding (A)	57.0	19.8	19.2	29.5	7.8	11.8	12.8
Holding of PDS	0.2	0.0	3.7	0.4	0.3	1.3	2.0
PDS outstanding (B)	25.5	10.3	5.8	8.7	10.0	8.3	7.4
<b>Memorandum item</b>							
Gross PDS (incl. Cagamas and issuances by non-residents)	58.6	16.4	14.4	18.3	18.0	6.5	11.4

\*Banking system loans include loans sold to Cagamas

Source: Bank Negara Malaysia

### Loan Indicators

	During the period (RM billion)				Annual growth (%)			
	2009	4Q 09	3Q 10	4Q 10	2009	4Q 09	3Q 10	4Q 10
<b>Total</b>								
Loan applications	521.3	141.2	176.3	173.5	9.8	39.0	30.1	22.9
Loan approvals	286.9	80.4	91.2	91.8	-1.4	32.1	25.5	14.1
Loan disbursements	657.2	187.0	176.1	188.8	2.7	18.4	5.1	1.0
Loan repayments	595.1	162.4	165.2	168.1	4.7	13.2	13.4	3.5
Change in loans outstanding*	57.0	19.8	19.2	29.5	7.8	7.8	11.8	12.8
<b>Of which:</b>								
<b>Business enterprises**</b>								
Loan applications	237.8	61.2	84.7	82.1	-2.7	19.2	40.6	34.1
Loan approvals	127.7	37.1	43.7	43.4	-13.7	25.8	47.5	17.0
Loan disbursements	440.0	126.1	116.5	124.5	-3.4	12.0	5.9	-1.3
Loan repayments	407.3	112.8	113.6	113.2	1.0	10.7	15.7	0.4
Change in loans outstanding*	8.9	5.9	2.1	13.4	3.0	3.0	7.1	9.4
<b>SMEs**</b>								
Loan applications	104.6	29.7	32.0	34.2	4.2	49.4	12.2	14.9
Loan approvals	45.3	12.7	14.7	14.4	-16.3	10.3	18.3	13.5
Loan disbursements	143.2	38.3	35.3	39.9	-12.1	-3.3	-1.3	4.2
Loan repayments	132.1	34.9	33.9	37.5	-9.1	-3.4	3.2	7.6
Change in loans outstanding*	0.6	5.9	2.8	3.7	0.5	0.5	4.5	2.6
<b>Large corporations</b>								
Loan applications	133.2	31.5	52.8	47.9	-7.5	0.1	66.0	52.3
Loan approvals	82.4	24.4	29.0	29.0	-12.2	35.7	68.5	18.8
Loan disbursements	296.8	87.8	81.3	84.6	1.4	20.2	9.3	-3.6
Loan repayments	275.2	77.9	79.7	75.7	6.7	18.5	22.0	-2.9
Change in loans outstanding*	8.3	0.0	-9.0	18.0	4.9	4.9	4.1	14.1
<b>Households</b>								
Loan applications	283.5	80.0	91.6	91.4	23.1	59.3	21.6	14.3
Loan approvals	159.2	43.3	47.5	48.3	11.3	38.0	10.3	11.6
Loan disbursements	217.2	60.9	59.6	64.3	17.7	34.3	3.5	5.6
Loan repayments	187.8	49.6	51.6	54.9	13.9	19.4	8.5	10.7
Change in loans outstanding*	38.6	12.1	14.8	14.2	9.8	9.8	13.3	13.4

\* The annual growth is for end-period.

\*\* Include loans to individual businesses.

Source: Bank Negara Malaysia

The major loan indicators remained strong in the fourth quarter. In the business sector, higher loan disbursements reflected mainly the drawdown of funds to finance working capital for the *finance, insurance and business services; electricity, gas and water supply; and manufacturing sectors*. Demand for new financing was sustained at high

levels with higher applications from the *transport, storage and communication; wholesale and retail, restaurants and hotels; electricity, gas and water supply and construction sectors*. On an annual basis, business loans outstanding expanded by 9.4% as at end-December (3Q 10: 7.1%).

## Loans by Sector

	Loans disbursed				Loans out-standing	
	During the period			Share of total	Share of total	
	2009	4Q 09	3Q 10	4Q 10		
	(RM billion)			(%)		
<b>Business enterprises</b>	<b>440.0</b>	<b>128.1</b>	<b>116.5</b>	<b>124.5</b>	<b>65.9</b>	<b>44.6</b>
<i>Large corporations</i>	296.8	87.8	81.3	84.6	44.8	30.1
<i>SMEs*</i>	143.2	38.3	35.3	39.9	21.1	14.5
<i>Selected sectors</i>						
Agriculture, hunting, forestry and fishing	20.9	7.1	4.8	5.3	2.8	2.3
Mining and quarrying	2.3	0.5	0.9	1.2	0.7	0.4
Manufacturing	128.5	34.9	36.1	36.8	19.5	9.4
Construction	40.6	12.2	11.3	11.9	6.3	4.4
Real estate	20.7	6.5	6.9	7.5	4.0	4.4
Electricity, gas and water supply	8.0	2.6	0.9	2.6	1.4	1.3
Wholesale, retail, restaurants and hotels	105.5	28.4	30.6	30.9	16.4	7.4
Transport, storage and communication	22.6	6.8	4.2	4.3	2.3	2.9
Finance, insurance and business services	45.3	12.8	13.0	17.8	9.4	7.1
<b>Households</b>	<b>217.2</b>	<b>60.9</b>	<b>59.6</b>	<b>64.3</b>	<b>34.1</b>	<b>55.4</b>
Purchase of residential properties	55.6	16.8	13.7	15.1	8.0	25.6
Consumption credit	132.6	36.2	38.2	39.9	21.1	20.6
Of which:						
<i>Credit cards</i>	70.5	19.5	21.3	23.4	12.4	3.4
<i>Purchase of passenger cars</i>	32.8	8.2	9.4	9.1	4.8	12.5
Others	29.0	8.0	7.7	9.3	4.9	9.1
<b>Total</b>	<b>657.2</b>	<b>187.0</b>	<b>176.1</b>	<b>188.8</b>	<b>100.0</b>	<b>100.0</b>

\*Include loans to individual businesses.

Source: Bank Negara Malaysia

Financing to the household sector remained steady. Demand for loans was mainly for the *purchase of residential and non-residential properties, and passenger cars*. Loan disbursements to households also increased during the quarter. Accordingly, household loans outstanding expanded by RM14.2 billion during the quarter to increase at an annual growth rate of 13.4% as at end-December (3Q 10: 13.3%).

## Stronger fund raising activity in the capital market

Net funds raised in the capital market increased to RM30.5 billion (3Q 10: RM16.8 billion) during the quarter, driven by stronger fund raising activity by the private sector. Gross funds raised through PDS issuances rose to RM18.3 billion (3Q 10: RM14.4 billion). The funds were mainly used for refinancing (48.4% of total funds raised) and working capital. As with the previous quarter, the bulk of issuances came from firms in the finance sector. Funds raised from the equity market rose substantially to RM14.7 billion, due to a large IPO amounting to RM12.5 billion by a firm in the industrial products sector.

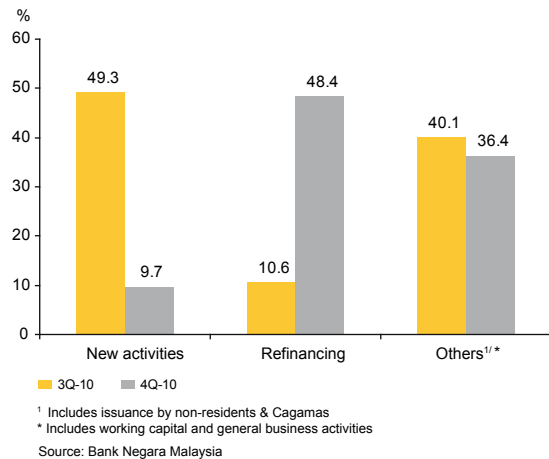
In the public sector, gross funds of RM9.6 billion were raised through issuances of the 10-year Government Investment Issues (GII) and the re-opening of the 3-year and 7-year MGS. After adjusting for redemptions, net funds raised by the public sector in the fourth quarter amounted to RM7.1 billion (3Q 10: RM8.9 billion).

## Net Funds Raised in the Capital Market

	2009		2010		
	4Q	Year	3Q	4Q	Year
RM billion					
<b>By Public Sector</b>	<b>5.6</b>	<b>57.8</b>	<b>8.9</b>	<b>7.1</b>	<b>37.0</b>
Government securities, <i>net</i>	5.7	53.3	9.0	7.1	34.9
<i>Malaysian Government Securities</i>	13.5	61.3	9.9	6.6	37.7
<i>Government Investment Issues</i>	3.5	28.5	6.0	3.0	21.0
<i>Less: Redemptions</i>	11.4	36.5	7.0	2.5	23.9
Khazanah Bonds, <i>net</i>	-	(2.4)	-	-	-
Savings Bonds, <i>net</i>	(0.1)	6.9	(0.1)	(0.1)	2.2
<b>By Private Sector</b>	<b>24.0</b>	<b>52.6</b>	<b>7.9</b>	<b>23.4</b>	<b>50.5</b>
Shares	13.2	26.0	2.1	14.7	32.1
Debt securities, <i>net</i>	10.8	26.5	5.8	8.7	18.4
<i>Private Debt Securities</i>	16.4	58.6	14.4	18.3	52.1
<i>Less: Redemptions</i>	5.6	32.0	8.6	9.6	33.8
<b>Total</b>	<b>29.6</b>	<b>110.3</b>	<b>16.8</b>	<b>30.5</b>	<b>87.5</b>

Source: Bank Negara Malaysia and Bursa Malaysia

### Private Debt Securities Issued by Purpose (% of total)



In the PDS market, the 5-year corporate bond yields remained stable despite the increase in the benchmark 5-year MGS yields. The AAA-rated papers recorded a slight increase of 1 basis point, while the A-rated papers recorded a slight decline of 5 basis points. Yields on the AA-rated papers were unchanged during the quarter.

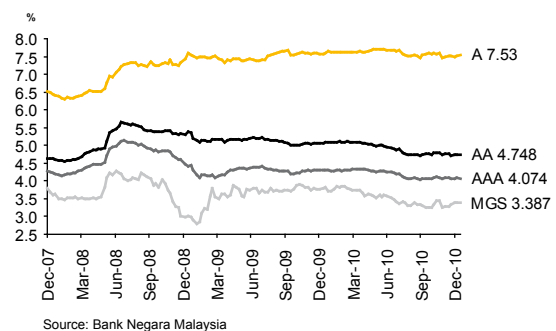
### Secondary trading

Total trading in the secondary bond market declined to RM158 billion during the quarter (3Q 10: RM179 billion). As a result, liquidity ratios across all segments fell, with the MGS, GII and PDS segments registering liquidity ratios of 0.43, 0.30 and 0.07 respectively.

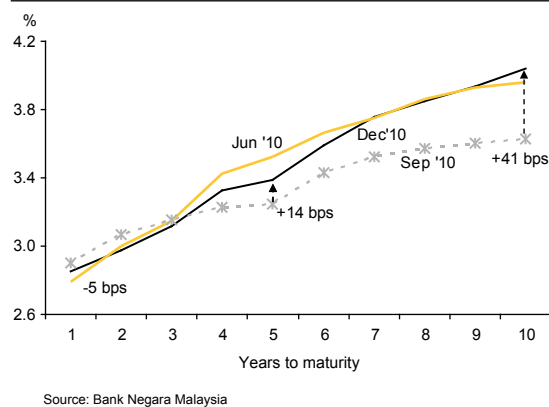
### Long-term yields increased

Following the Budget 2011 announcement on 15 October, MGS yields of longer maturities increased during the last quarter of 2010 on expectations of larger debt issuances in 2011 and the positive economic outlook. The 5-year and 10-year MGS yields recorded an increase of 14 and 41 basis points respectively. However, short-term yields were largely unaffected. Yields on the 1-year MGS and 3-year MGS recorded a slight decline of 5 and 4 basis points respectively. As a result, the benchmark MGS yield curve was steeper in the fourth quarter.

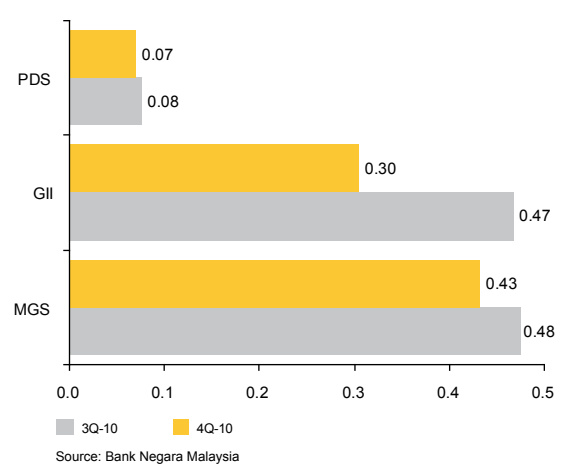
### 5-year MGS and 5-year Corporate Bond Yield



### Trend in MGS Yields

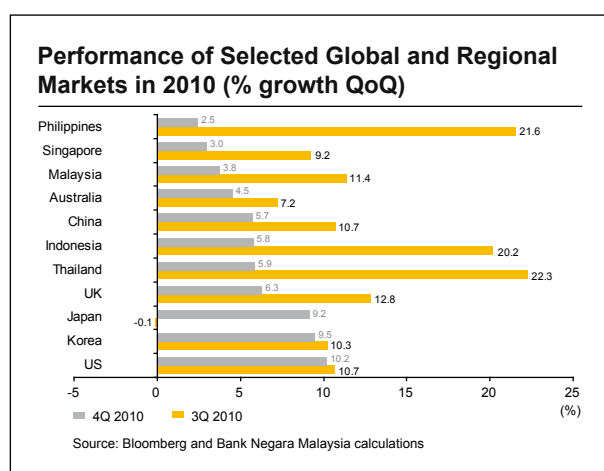


### Liquidity Ratio: Turnover / Outstanding



## KLCI continued to rise in the fourth quarter

The FBM KLCI ended the fourth quarter higher at 1,518.91 (since 3Q 10: 3.8%), supported by investor optimism following the Government's announcement of key projects in the Economic Transformation Programme (ETP). The domestic equity market was also supported by gains in the plantation sector due to rising crude palm oil prices. Regional equity markets, including Malaysia's, were lifted by expectations and the eventual implementation of a second round of quantitative easing by the US Federal Reserve. Market capitalisation



increased to RM1.28 trillion at end-Dec 2010 (3Q 10: RM1.15 trillion), while the daily average turnover was higher at 1.28 billion units (3Q 10: 0.92 billion units) during the quarter.

On 18 January 2011, the KLCI closed higher at 1,570.04 points (since end-2010: +3.37%) with market capitalisation of RM1.33 trillion (since end-2010: +4.01%).

### Bursa Malaysia: Selected Market Indicators

	2009		2010		
	As at end				
	Dec	Year	Sep	Dec	Year
Price Indices					
Composite	1,272.8	1,272.8	1,463.5	1,518.9	1,518.9
FBMEMAS <sup>1</sup>	8,507.6	8,507.6	9,811.6	10,375.0	10,375.0
FTSE Second Board <sup>2</sup>	-	-	-	-	-
ACE Market <sup>3</sup>	4,299.6	4,299.6	3,877.0	4,347.6	4,347.6
Market capitalisation (RM billion)	999.5	999.5	1,150.1	1,275.3	1,275.3
No. of companies listed	960	960	958	957	957
	During the quarter				
	4Q	Year	S3	S4	Year
Average daily turnover					
Volume (million units)	915.2	1,000.2	920.9	1,276.5	1,021.2
Value (RM million)	1,210.3	1,220.9	1,481.7	2,002.5	1,573.9

<sup>1</sup>FBMEMAS stands for FTSE Bursa Malaysia EMAS Index

<sup>2</sup>From 3 August 2009, FTSE Second Board was merged with the Main board and renamed as Main Market

<sup>3</sup>From 3 August 2009, Mesdaq market was replaced with ACE Market

Source: Bursa Malaysia

### Bursa Malaysia: Market Turnover

	2009				2010					
	4Q		Year		3Q		4Q		Year	
	Billion units	RM billion	Billion units	RM billion	Billion units	RM billion	Billion units	RM billion	Billion units	RM Billion
Turnover	57.7	76.2	248.1	302.8	58.0	93.4	79.1	124.2	268.0	413.0
Of which:										
Main Board	48.3	73.7	210.4	292.7	49.3	91.7	65.7	121.1	225.5	403.3
Of which										
Consumer Products	3.8	3.8	11.3	14.5	4.2	5.0	3.6	5.5	15.3	19.3
Industrial Products	10.1	9.5	44.5	36.0	8.9	9.9	15.4	22.7	47.6	58.9
Construction	2.5	4.7	15.7	22.4	4.5	8.5	4.5	8.7	16.4	29.0
Trading/Services	15.4	27.7	70.5	105.6	15.1	34.5	19.3	40.0	68.2	140.2
Finance	4.2	15.1	17.1	56.6	3.5	18.7	4.6	22.7	17.7	86.2
Properties	4.6	3.5	29.3	19.4	6.7	4.6	11.5	8.8	33.1	21.6
Plantations	1.1	4.4	5.9	21.6	1.0	5.1	2.3	7.9	6.1	25.5
Infrastructure	1.6	1.8	5.7	10.3	1.8	2.2	1.7	2.4	5.8	8.9
Second Board <sup>1</sup>	-	-	10.8	4.0	-	-	-	-	-	-
Mesdaq <sup>2</sup>	5.6	1.4	16.7	3.4	4.1	0.6	5.6	1.3	20.3	3.9

<sup>1</sup>From 3 August 2009, FTSE Second Board was merged with the Main board and renamed as Main Market

<sup>2</sup>From 3 August 2009, Mesdaq market was replaced with ACE Market

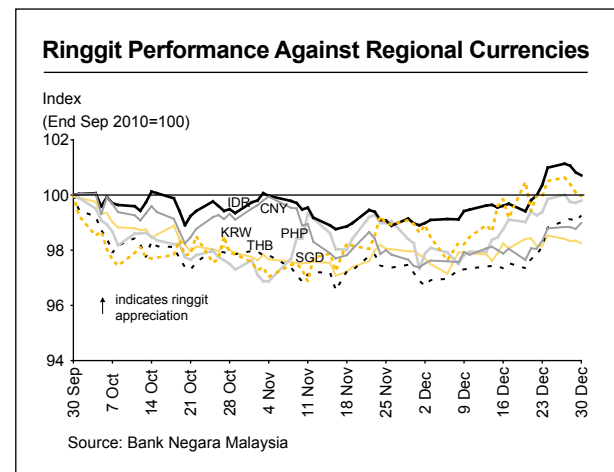
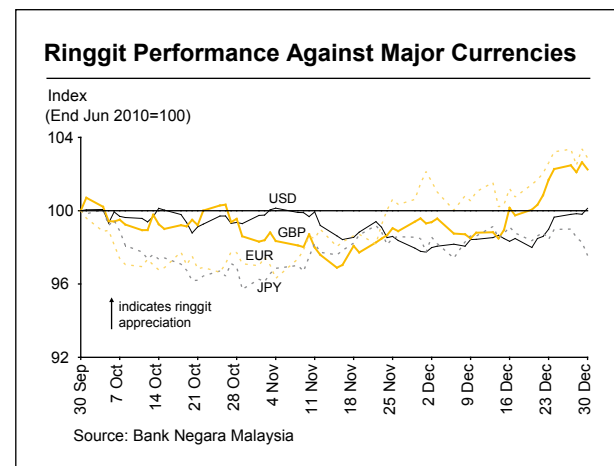
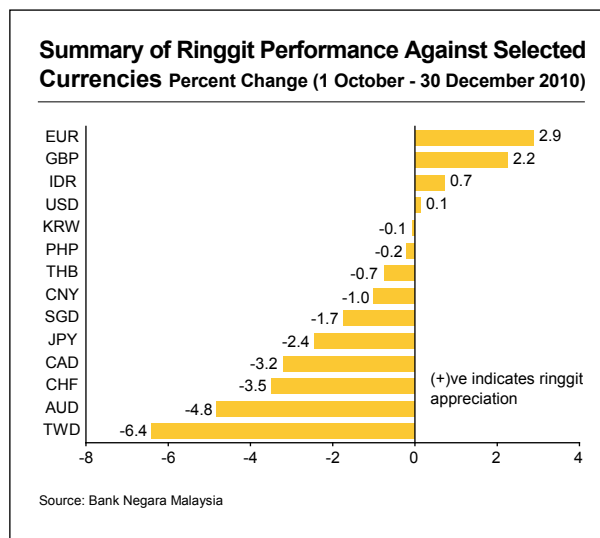
Source: Bursa Malaysia

### Mixed performance of the ringgit during the quarter

For the fourth quarter, the ringgit appreciated marginally (+0.1%) against the US dollar as the appreciation and depreciation during the interim months roughly offset each other. The ringgit broadly depreciated in October and November amid higher risk-aversion following lingering concerns over the European sovereign debt problems and tensions in the Korean Peninsula. The ringgit, however, ended the year stronger as it strengthened against the US dollar and currencies of major trade partners following optimism in the growth outlook for Asia, which boosted investor sentiments towards regional financial markets. Against other major currencies, ringgit appreciated against the euro (2.9%) and pound sterling (2.2%) but depreciated against the Japanese yen (-2.4%). Against regional currencies, the ringgit broadly depreciated in the range of -0.1% to -1.7% as country specific factors led to a strengthening of these currencies against the ringgit. The ringgit,

however, appreciated by 0.7% against the Indonesian rupiah.

During the period between 1 January to 14 February 2011, the ringgit appreciated against the U.S dollar (1%) and the Japanese yen (3.3%), but depreciated against the pound sterling (-2.5%) and the euro (-1.2%). The ringgit appreciated against regional currencies in the range of 0.1% to 3.1%, with the exception of the Korean won, against which the ringgit depreciated by 0.4%.



**Performance of Ringgit Against Selected Currencies**

RM per foreign currency	As at end				% change since*		
	21 Jul 05	4Q 09	3Q 10	4Q 10	21 Jul 05	4Q 09	3Q 10
US dollar	3.8000	3.4245	3.0875	3.0835	23.2	11.1	0.1
Euro	4.6212	4.9191	4.1979	4.0804	13.3	20.6	2.9
Pound sterling	6.6270	5.5001	4.8892	4.7817	38.6	15.0	2.2
100 Japanese yen	3.3745	3.7076	3.6943	3.7869	-10.9	-2.1	-2.4
Singapore dollar	2.2570	2.4401	2.3442	2.3859	-5.4	2.3	-1.7
100 Thai baht	9.0681	10.271	10.151	10.227	-11.3	0.4	-0.7
100 Philippine peso	6.8131	7.4196	7.0254	7.0400	-3.2	5.4	-0.2
100 Indonesian rupiah	0.0386	0.0364	0.0346	0.0344	12.4	6.0	0.7
100 Korean won	0.3665	0.2937	0.2706	0.2707	35.4	8.5	-0.1
Chinese renminbi	0.4591	0.5016	0.4615	0.4662	-1.5	7.6	-1.0

\* (+) indicates appreciation of ringgit against respective currency and (-) indicates depreciation.

Source: Bank Negara Malaysia

## DEVELOPMENTS IN THE BANKING AND INSURANCE SECTORS

Financial stability was maintained throughout the fourth quarter, supported by sound financial institutions and orderly financial markets which provided continued support for financial intermediation in the domestic economy.

On 3 November 2010, the Bank announced the implementation of a maximum loan-to-value (LTV) ratio of 70% for the third house financing facility taken by a borrower. The targeted implementation of the LTV ratio is aimed to support a stable and sustainable property market, and promote the continued affordability of homes for the general public.

### Developments in the banking sector

The banking sector remained resilient, with strong capital buffers, sustained profitability, stable loan quality and ample liquidity. The financing portfolio was broad-based, with financing extended to households and small and medium-sized enterprises comprising 55.4% and 14.5% of total outstanding financing respectively.

Banking System				
	2009		2010	
	4Q	3Q	4Q	
<b>Capital position</b>				
Risk-weighted assets (RM billion)	928.5	993.3	1,017.9	
Capital base (RM billion)	142.6	146.5	148.3	
Risk-weighted capital ratio (%)	15.4	14.7	14.6	
Core capital ratio (%)	13.8	13.2	12.8	
<b>Profit before tax (RM million)</b>				
Annualised return on equity (%)	14.0	16.6	16.5	
Annualised return on assets (%)	1.2	1.6	1.5	

Source: Bank Negara Malaysia

Capitalisation was strong with the risk-weighted capital ratio (RWCR) and core capital ratio (CCR) at 14.6% and 12.8% respectively. Approximately 78% of total capital comprised high quality Tier-1 capital mainly in the form of paid-up capital and reserves. Capital in excess of the minimum 8% requirement stood above RM60 billion.

The banking sector recorded a pre-tax profit (PBT) of RM5.7 billion during the quarter (3Q 2010: RM 5.9 billion). This was supported by sustained revenue from financing-related activities. Average returns on assets and equity

stood at 1.5% (3Q 2010: 1.6%) and 16.5% (3Q 2010: 16.6%) respectively.

Loan quality remained stable with fewer new incidences of impairment and prudent write-offs observed during the quarter. Consequently, the level of net NPLs (including impaired financing) improved marginally to account for 2% of total loans. In addition, the level of loans-in-arrears for less than 3 months improved slightly to account for 4.2% of total loans. The loan loss coverage correspondingly strengthened further to 99.5% (3Q 2010: 97%).

Liquidity in the banking system remained ample during the quarter. The liquidity buffers for the maturity buckets of up to one week and one month were at 16.6% and 16% of total deposits respectively (3Q 2010: 18.8% and 19.2%). These were sufficient to meet demand for deposit withdrawals and other liquidity obligations. The loan-to-deposit ratio was stable at 81.4% (3Q 2010: 81.2%).

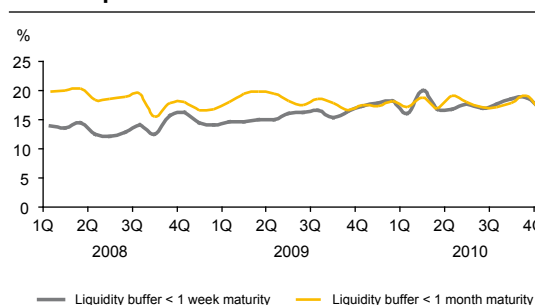
### Banking System: Non-Performing Loans (NPL)<sup>1</sup>

	2009		2010	
	4Q	3Q	4Q	
Net NPL (RM million)	13,787.9	17,425.7	17,231.2	
	%			
Net NPL ratio	1.8	2.1	2.0	
Gross NPL ratio	3.7	3.3	3.1	
Large businesses	4.2	4.8	4.4	
Small & medium enterprises	5.4	4.9	4.5	
Households	3.1	2.4	2.3	

<sup>1</sup> Beginning January 2010, loans are reported based on Financial Reporting Standards (FRS) 139. The adoption of FRS 139 requirement is based on the financial year of the banks. For banks that have adopted FRS 139, the level of NPLs reflects impaired loans.

Source: Bank Negara Malaysia

### Banking System: Liquidity Buffer to Total Deposit Ratio



Source: Bank Negara Malaysia

### Developments in the insurance and takaful sector

The insurance and takaful sector remained resilient with a strong Capital Adequacy Ratio of 225.7% (3Q 2010: 222.7%) and excess capital of RM18.5 billion. The excess of income over outgo for life and family takaful business profits recorded a slight moderation in the fourth quarter to RM3.1 billion (3Q 2010: RM5 billion) due to lower capital gains recorded amidst higher net policy benefits. However, year-on-year, total profits recorded an improvement of 12.6% to RM14.1 billion (2009: RM12.5 billion) on account of improved capital gains and higher net premium income. New business premium contributions grew by 12.5% to RM2.7 billion (3Q 2010: RM2.4 billion) due to the continued growth in investment-linked business.

Similarly, the general insurance and takaful industry also recorded an improvement in

profitability to RM0.56 billion (3Q 2010: RM0.51 billion). This was supported by higher revenue from motor and personal accident businesses. The overall claims ratio stood at 62.8%, with the dominant motor segment which account for about 50% of total premium revenue, continuing to exhibit a significantly higher loss ratio of 79.6% (relative to overall claims). This is attributed mainly to third party motor insurance.

#### Insurance and Takaful Sector: Profitability<sup>p</sup>

	2009		2010		
	4Q	Year	3Q	4Q	Year
	RM million				
<b>Life insurance &amp; family takaful business</b>					
Excess of income over outgo	3,165.8	12,522.7	5,064.1	3,140.8	14,095.0
<b>General insurance &amp; general takaful business</b>					
Operating profit	826.4	2,097.4	514.4	557.7	514.4

<sup>p</sup> Preliminary

Source: Bank Negara Malaysia

**2010 Institute of International Finance (IIF) Annual Membership Meeting:  
“South East Asia: Potential and Perspectives in the New Asia”  
Washington D.C, 8 October 2010**

Luncheon Address by

**Tan Sri Dato' Sri Dr. Zeti Akhtar Aziz**  
Governor, Bank Negara Malaysia

Generating growth and a long lasting recovery is the primary priority for the global economy in this aftermath of the recent crisis. The massive life support that was provided to avert a deep recession was to be temporary - to provide the opportunity to address the weakness in the system and to rebuild the capacity for a self-sustaining recovery. Recent indications are that this prospect has not been realised. The emerging world has however performed well with the potential to generate such a sustained recovery. These developments have drawn significant interest to the Asian emerging economies and on their changing role in the global economy and in the international financial system.

It is my honour and great pleasure to speak at this 2010 Institute of International Finance Annual Membership Meeting. My remarks today will focus on the challenges in managing such a sustained recovery with specific focus on the potential for emerging Asia to rise to these challenges in this new global economic and financial environment. The final part of my remarks will be on the changes taking place in the international financial environment from the perspective of emerging Asia.

As growth in the developed world slows, weighed down by structural factors, will the global environment of increasing interdependence then dampen the prospects for the Asian emerging economies? Asia comprises highly diverse economies. South East Asia, with a population of more than 500 million people is strategically located south of China and east of India, has been since the 13th century an important trading hub connecting Asia to the West. Being the most open economies in Asia, and perhaps in the world, we, therefore stand to be the most vulnerable to global developments.

While economic stimulus is vital for crisis containment, it will not, however, be sufficient to produce a self-sustaining recovery. The challenge is essentially the economic restructuring and transformation, the reform and rebuilding of the institutional capacity so as to remain effective in the new environment and to be well positioned to manage future shocks.

As emerging economies in Asia transition into this post crisis era, three important structural shifts are transforming the region. The first is the economic restructuring and the strategy to pursue more balanced sources of growth. This has involved significant shifts to new areas of comparative advantage and new areas of growth, and the greater emphasis on domestic demand as a driver of growth. While the export sector continues to be important, the pattern of trade has changed significantly with the growing importance of trade with emerging economies, in general, and with Asia, in particular.

Perhaps the most important factor that has for several decades sustained the economic success of the emerging Asian economies is its economic flexibility to adjust to the changing conditions in the global environment. This economic flexibility is supported by the high degree of labour and capital mobility within the national economies and the significant investment accorded to education and to infrastructure development. The region has also adopted a pragmatic approach to policy that is not constrained by rigid ideology. In this more recent decade, institutional development, extensive financial reforms, and the adoption of new business models have been an important part of this transformation process.

Several of the economies in emerging Asia's have transformed their production capacity in the manufacturing and services sector to meet

the changing demands of the global economy and the growing consumer market in Asia. Given the different stages of development and endowment of natural resources in the region, the emerging economies in Asia have also leveraged on their respective distinct comparative advantages. This has resulted in intra-regional division of labour and specialisation, and the capacity to undertake the entire spectrum of the supply chain for a wide range of products and services.

Part of the economic restructuring has also involved the greater emphasis on domestic demand as an important source of growth. This has involved significant increases in domestic private consumption and investment activities. Rising income levels and the presence of a young demographic structure with a high propensity to consume has resulted in a huge consumer market and the development of an extensive modern retail sector across the region. The potential sustainability of this trend is supported by the absence of inflationary trends, of large scale unemployment, or of high levels of indebtedness.

The second fundamental trend is the intensification of regional economic and financial integration. This has been facilitated by the ability to leverage on complementarities in the region arising from diversity and differences in comparative advantage. Intra-regional trade has been a major contributor to the recent recovery in Asia. Intra-regional investment flows have also gained momentum. Businesses in the region are increasingly leveraging on regional complementarities and taking advantage of the growing markets in the region through regional trade agreements to achieve the aspiration for ASEAN to become an Economic Community by 2015.

As high saving economies, it is recognized that there is an important need for a more efficient intermediation of the surplus funds in the region. This is to not only effectively channel these funds into productive investment opportunities in the region, but also to finance the massive development of infrastructure required by the region. As part of the increased regional financial integration, there is now increased regional presence and participation

in the domestic financial systems of the region. This phenomenon has been supported by the progressive financial liberalisation, the development of domestic financial markets, the greater use of domestic currency to facilitate bilateral trade activities and the development of the payments and settlement systems.

The economic and financial regional integration has also been reinforced by a higher level of regional cooperation. Earlier regional cooperation had focused mainly on trade, investment and development. This decade has seen the cooperation shift to efforts to address financial stability issues, including in surveillance, crisis management, liquidity support arrangements, financial supervision and financial market development.

The approach in forging greater financial integration in Asia will be different from that adopted by Europe. The region does not have centralised institutions to coordinate financial integration but has leveraged on the existing intra-regional groupings and networks to forge greater cooperation and collaboration in areas of common interest. The region has its own monetary and financial stability committee that is supported by arrangements for regional surveillance to identify risks and vulnerabilities to the region. Also in place is an integrated crisis management framework that will be operationalised in the event of an imminent financial crisis in the region. Recently the region successfully organised two schemes for reserve pooling, the Asian Bond Fund and the ASEAN+3 Chiang Mai Multilateralised Swap arrangement as a liquidity support facility.

As economic and financial systems in Asia continue to transform and as the region becomes more integrated and cohesive, this has not only enhanced the potential for the region to contribute to global growth but also enhanced the resilience of the region and thus its role in contributing to global financial stability. These trends support the global efforts by the various international groupings and multilateral agencies in the search for solutions to achieve global financial stability and sustainable growth.

The transition from G7 to G20 is recognised as a positive step forward that extends its

reach beyond the developed world. But the representation in G20 is by virtue of the size of the economy and not by representation of specific groups of countries. Its outreach and inclusiveness is therefore limited, and small and medium sized emerging economies are not part of this process. The G20 is, nevertheless, an important global forum for considering global issues and will have an important role in setting the direction for global policies. Earlier, the cohesiveness, the sense of purpose and urgency of the G20 did indeed contribute to restoring confidence in the global financial system and the coordinated policy stimulus was an important catalyst for the economic recovery. In recent months, however, the momentum for this coordinated actions have dissipated and there have been differing positions on several important issues. At the same time, a number of the major crisis affected countries have implemented their own financial reform plans. In view of the far reaching implications of any reform agenda, it is an important global responsibility to ensure that the reforms achieve their intended results and that this new phase of globalisation will result in a more inclusive international financial system that will allow for the effective participation in the global economy and international financial system regardless of size or stage of developments.

On the specific regulatory reforms to address the issues and problems that caused the crisis, of importance, is that the goal of such regulatory reform should not be overlooked - promoting financial stability is a means to an end and the ultimate goal is to achieve sustainable growth and development. Many have already highlighted the potential increased regulatory costs on intermediation and hence on economic activity. This is even more relevant in Asia where there is greater reliance on the banking sector for financing. The efforts undertaken to comprehensively assess the macroeconomic impact including by the IIF is highly relevant and will be important to the reform process.

A further concern and one that is less discussed is on the implementation of the regulatory reform. With greater capital mobility across borders, the stricter regulations could result in the migration of financial business to less regulated market segments, institutions or

financial centres. Important to this is the need for the development of the framework for cross border policy coordination and resolution. In Asia, efforts are underway to address these specific issues recognising that in this interconnected environment, the execution of remedial and containment measures will be highly complex and challenging. Focus is also being given to having enhanced surveillance and oversight that is complemented by a robust framework for governance, transparency and accountability.

Given the strong presence of international institutions in the Asian region, we have strong interest in the establishment of an effective cross border resolution mechanism so that any failure of such large and systemically important institutions with cross border representations can be dealt with effectively in an orderly manner. This will require cooperation and coordination across countries, taking into consideration their differing regulatory and legal systems.

A further priority in emerging Asia is the promotion of responsible market practices and consumer protection given the stage of development and level of financial literacy. There is significant scope for creating greater global momentum for improvements in regulatory standards on market practices.

Much work still remains ahead and would require resolve and commitment in this reform agenda. The more inclusive global process is critical to this effort and should be further deepened to truly reflect the global dimension of the financial system in this 21st century.

On the recent increasingly intense debate on the role of the exchange rate as the solution to the global imbalances, it needs to be recognised that the foreign exchange market is not like any other markets. With a daily transaction amounting up to USD4 trillion, it is the most liquid and dynamic market in the world. It is a market that is prone to excessive movements and overshooting. Any effort to engineer a significant exchange rate adjustment within a short period of time carries the risk of highly destabilising consequences. Global imbalances that have been built up

over several years need to be unwound by a combination of adjustments in demand, prices and exchange rates. Over reliance on the exchange rate to do the adjustment may not only not produce the desired result, but it also risks becoming a trigger factor to causing instability and future crisis.

The final development that I wish to say something on is the global development of Islamic finance and its increasing role in enhancing global economic and financial linkages particularly among emerging economies. Islamic finance is all about basic banking that is always supported by underlying economic activity. Its profit sharing feature provides for risk sharing and thus the necessary due diligence, disclosure and transparency, risk management and governance. The industry is also well supported by the regulatory and supervisory standards issued by the Islamic Financial Services Board (IFSB). While the focus

has been on keeping the regulation abreast with the developments in the financial system, emphasis is also given on the supervisory oversight, capacity building, and institutional and financial infrastructure development as part of the efforts to ensure financial stability. The most recent significant development was the establishment of the International Islamic Liquidity Management Corporation (IILM) that will issue highly rated short-term Islamic instruments to facilitate more efficient liquidity management of cross border investments.

The global challenges call for a collaborative approach to strengthen the prospects for a global recovery. The way forward is also to recognise the relative strengths of different parts of the world and the potential to leverage on these strengths. The transformation of Asia in this new environment offers the prospects for a greater shared responsibility towards a greater shared prosperity in the world.

**IMF-World Bank Annual Meetings:  
“Islamic Finance: An Agenda for Balanced Growth and Development”  
Washington D.C, 10 October 2010**

Luncheon Address by

**Tan Sri Dato’ Sri Dr. Zeti Akhtar Aziz**  
Governor, Bank Negara Malaysia

The growth and development agenda is now the primary priority for the world economy. In the advanced economies, the efforts to generate a long lasting recovery in the aftermath of this recent unprecedented global financial crisis is heavily weighed down by the need to address several structural challenges which will affect the strength of this recovery. In this new phase of globalisation, of greater economic and financial interdependence, the growth and development agenda for the emerging and developing world has therefore become even more challenging.

The global crisis has in fact demonstrated the pivotal role of an efficient functioning financial system towards achieving such a self-sustaining economic recovery. This has prompted an intensive collaborative effort by the international community to undertake wide ranging and far reaching financial reforms. This commitment is for a solution that will evolve a financial system that will best serve the real economy, a financial system that is sound and resilient and that is less vulnerable to financial crisis.

Islamic finance, as a rapidly growing form of financial intermediation, has demonstrated its resilience during the global financial crisis and has every potential to advance the growth and development agenda. It is my very great honour to be invited to speak at the Islamic Development Bank Group’s luncheon held in conjunction with the 2010 IMF-World Bank Annual Meetings here in Washington D.C. My remarks this afternoon will discuss the recent developments in the Islamic financial system and its role as an effective and competitive form of financial intermediation in the growth and development agenda. I will also discuss on the increasingly more important role of Islamic finance in strengthening international economic and financial linkages in the global economy,

particularly among the emerging and developing world thereby increasing the potential for achieving a greater shared progress and prosperity.

As a form of financial intermediation, Islamic finance incorporates several elements that guide the process of the mobilisation and allocation of funds to generate productive economic activity and inclusive development. Fundamental to Islamic finance is the requirement that financial transactions be accompanied by an underlying productive economic activity that will generate legitimate income and wealth. There is therefore, a close link between financial transactions and productive flows. Thus, the growth in Islamic financial assets is generally accompanied with growth of underlying activities that have economic value.

These important elements in Islamic finance enhance its ability to contribute to the growth and development agenda. Firstly, Islamic finance has been able to be dynamic to respond to the differentiated and requirements of consumers and business. In the early stage of its development, Islamic finance focused on meeting the demands for trade financing. Today, it offers the range of financial products and services from a highly diversified financial system that include the provision of innovative and high quality financial products and services such as consumer financing, wealth management and wide ranging products from the Takaful industry and the Islamic capital markets. It also has the capacity to promote project financing and long term structured products for the financing of large scale project and infrastructure development.

The second factor that has ensured the sustainability of Islamic finance is its ability to

remain a competitive form of financing. The competitiveness of Islamic finance is vital to enhance its role in the growth and development agenda and is derived from a number of fundamental reasons. Given that the Islamic financial instruments reflect the underlying economic activities and that such instruments inherently have the potential to provide tangible returns to the investors, it has therefore created significant demand on Shariah compliant financial products. In the current environment of great uncertainty, both investors and issuers are in search of financial products and services that require greater transparency and explicit risk management. Shariah principles, in this respect, prohibit excessive leverage and speculative financial activities and discourage excessive risks exposures.

The third aspect of the sustainability of Islamic finance is its resilience. The global financial crisis, unprecedented in modern history has brought to the forefront the wide ranging issues concerning soundness and stability of financial system. The regulatory reform and the reform of the international financial architecture is part of the efforts by the international community to address the many weaknesses that caused the crisis. In any reform exercise, however, of great importance is the clarity of the objectives to be achieved. It is recognised that financial stability is critical to ensure the sustainability of the intermediation function. The debate however has raised the issue on whether such stringent regulation might increase the costs of financial regulation and in turn affect the growth and development agenda.

In Islamic finance, financial stability has been addressed on three fronts. Firstly, Islamic finance has its own inherent inbuilt checks and balances. Its value proposition of profit and risk sharing requires the appropriate due diligence, disclosure and transparency. The features inherent in Islamic finance, therefore, emphasises the dimensions of governance and risk management. The role of the Shariah Board is to ensure all aspects of the business operations of Islamic institutions are in accordance with the Shariah principles. This therefore adds another level of oversight which inherently safeguards against irresponsible practices. This is particularly important in

ensuring that the rapid pace of innovation in the current environment contributes towards the real economy and the society.

The second factor that contributes towards strengthening the soundness of the Islamic financial system is the establishment of the Islamic Financial Services Board (IFSB) in 2002. This is an important international institution that sets the prudential standards for Islamic finance. This includes the standards for capital adequacy, risk management and corporate governance taking into account the specific risks inherent in Islamic finance. While the regulatory regime is keeping abreast with dramatic changes that have transformed the international economic and financial landscape, key for the Islamic financial service industry to thrive in this new environment is that its level of resilience has to be strengthened further.

Early this year, the IFSB Governing Board endorsed an independent report initiated by the IDB and IFSB which has proposed eight recommendations of which two of these recommendations are being implemented. The first is the establishment of the Islamic Financial Stability Forum (IFSF) as a platform to achieve the primary objective of building cross-border dialogue among regulators in efforts to promote financial stability, in the Islamic financial system. The objective of IFSF will be to facilitate better understanding of emerging developments in the Islamic financial system and their implications for national and global financial stability. The second is the development of a liquidity management infrastructure to facilitate cross border financial flows. This is a major breakthrough for Islamic finance. Not only does it address the issue of more efficient management of liquidity across borders but also it enhances competitiveness and addresses the issue of liquidity management in achieving financial stability.

The remaining recommendations involve strengthening further the institutional arrangements and financial infrastructure for Islamic finance. This includes extending the parameters for prudential standards to other segments of the industry to avoid migration to less regulated sectors. The IFSB is also now mandated to set the prudential standards for Takaful and capital markets.

The second remaining recommendation is strengthening of the safety net mechanisms which are compatible with Shariah principles, such as lender of the last resort facilities and emergency financing mechanism and deposit insurance. In the current regulatory reform by the international community, there is yet to be a consensus on the resolution framework. For Islamic finance, the efforts will be in parallel not only for resolutions of problem institutions within jurisdictions but also across borders.

The third relates to the accounting, auditing and disclosure standards to enhance financial reporting and allow for effective monitoring and assessment of Islamic financial institutions. The fourth relates to macro prudential surveillance framework to support prudential regulation which cannot always effectively deal with system wide stress. The fifth relates to strengthening the rating process and finally the sixth, relates to the capacity building and talent development so that the industry and the regulators are well equipped to deal with the issues and challenges in the new environment.

In the search for permanent solutions to put the financial system on a solid foundation, an issue that has been frequently highlighted is that this may result in higher financial intermediation costs that will have a disproportionate impact on economic activity. This is particularly relevant to emerging and developing economies. For Islamic finance, to avoid the over reliance on regulation to achieve financial stability, the strategy has been for the regulatory framework to be complemented with building the institutional capacity, relying on other policies including macro prudential measures, strengthening surveillance and an enhanced effectiveness of supervisory oversight.

Another more recent important development in Islamic finance is the increased significance of its international dimension driven by extensive interest and demand from different parts of the world, the internationalization of Islamic finance is shaping new global patterns of financial and trade flows. It is also facilitated by progressive liberalization of emerging economies in this recent decade. There is now increased presence of Islamic financial institutions beyond their domestic borders

and increased foreign participation in Islamic domestic financial markets. Correspondingly, the internationalisation process reflects the more inclusive global financial integration as it facilitates financing of international trade and cross border investment activities among the emerging and developing world. The wave of internationalisation in Islamic finance which continued unabated despite the recent global crisis has contributed to stronger investment and financial flows between Asia and the Middle East, generating mutually reinforcing growth prospects for both regions. This has in particular contributed to the deepening of financial and economic ties between Asia and the Middle East, which harnesses the complementarities in these dynamic growth regions to promote trade, direct investment and finance.

It has therefore becoming an important channel for fostering international financial linkages and in so doing is contributing to more balanced growth and development. The internationalization of Islamic finance has therefore not only allowed for further diversification of risks, it has also contributed to more efficient allocation of funds across borders from centres with surplus funds to regions with investment opportunities.

The importance of Islamic finance in strengthening financial linkages is evident in particular with the emergence of sukuk instruments to prominence as an attractive new asset class for investors and a competitive form of financing for businesses. The global sukuk market currently stands at almost US\$130 billion, with an average growth rate of about 40 percent annually. Having now become the most vibrant segment in Islamic finance, the sukuk market has evolved into a truly international market, generating significant cross-border flows as funds are being raised from beyond domestic financial markets.

As observed from the Malaysian experience, whilst sukuk has now become the preferred financing and capital raising option for the government and local corporations, our market has also seen a significant amount of participation and continued rising interest from foreign companies and multilateral institutions. Our sukuk market has also attracted investors

from across the globe. The recent issuance of Malaysia's USD1.25 billion sovereign sukuk in May this year was 6 times oversubscribed with a wide investor base from Asia, the Middle East, Europe, and the U.S, despite the prevailing volatile market conditions.

### Conclusion

Let me now conclude. As we pursue with stronger vigour the agenda of balanced growth

and development, we have the potential to leverage on the increased role of Islamic finance in contributing to the global growth and global financial stability agenda. In addition, it can also be leveraged upon to foster greater financial flows across borders to contribute towards our agenda of enhancing a mutually reinforcing growth and the development agenda to achieve global aspiration of a self-sustaining, balanced and long lasting economic progress and development.

**World Congress of Accountants (WCOA):  
“Islamic Finance: Strengthening the Global Financial Market”  
Kuala Lumpur, 10 November 2010**

Keynote Address by

**Tan Sri Dato’ Sri Dr. Zeti Akhtar Aziz**  
Governor, Bank Negara Malaysia

Restoring stability in financial markets, resuming the efficient functioning of financial systems and reigniting a sustainable economic recovery are the pressing priorities in the current global environment. As financial markets across jurisdictions become more connected, and as economies become more inter-linked, the resulting increased interdependence has however rendered the search for solutions to be even more challenging.

While the extensive international response involving massive stimulus measures have contained the extent of the global crisis, it has however, not been sufficient to produce a self-sustaining long lasting economic growth. Over and above the regulatory reforms are the required restructuring, resolution and the other financial and economic reforms to address the crisis related and structural issues that are still confronting the world economy. These prevailing conditions can therefore be expected to result in an extended period of increased uncertainty.

In such a period of extraordinary challenges and uncertainties, Islamic finance has continued its global expansion and development. In addition, this recent decade has seen the increased internationalisation of Islamic finance. It is my great pleasure to join you today at this World Congress of Accountants to speak at this session on Islamic Finance and its introduction in the global financial markets. My remarks this morning will discuss the potential role of Islamic finance in the international financial system as it becomes increasingly internationalised and its role in strengthening international financial and economic linkages in the global economy. Of importance to this trend are both the inherent features of Islamic finance and the financial infrastructure development that have

contributed to its resilience and sustainability and thus its positive role in the international financial system.

### **The Islamic finance model**

As a form of financial intermediation, Islamic finance incorporates several elements that guide the process of the mobilisation and allocation of funds. The Shariah injunctions fundamentally require that the financial transactions in Islamic finance be accompanied by an underlying productive economic activity that will generate legitimate income and wealth. This gives rise to a close link between financial transactions and productive flows. Therefore, the growth in Islamic financial assets is generally accompanied with growth of underlying activities that have economic value.

Islamic finance also has its own inherent inbuilt checks and balances that address the issues in financial stability. Its value proposition of profit and risk sharing requires the appropriate due diligence, disclosure and transparency. The features inherent in Islamic finance, thus, emphasise the importance of governance and risk management. The contracts entered into therefore demands high standards of disclosure and transparency, which in turn, reinforces market discipline and minimises informational asymmetries. A further layer of oversight that acts as a safeguard against irresponsible practices is the Shariah board in the respective individual financial institutions that has an important role in ensuring that the business operations of Islamic financial institutions are in accordance with the Shariah principles. Thus, Islamic finance, embraced in its entirety, supports responsible and sustainable innovation that contributes towards the real economy and to society.

These important elements in Islamic finance provide the foundations on which it contributes to growth and development and towards preserving financial stability. Despite the turmoil and uncertainties in the global financial system, Islamic finance has demonstrated its resilience and its continued global expansion during this period. Expanding at an average annual rate of 20%, Islamic finance represents one of the fastest growing segments in the financial industry. The Islamic financial services industry is now approximated to be worth more than US\$1 trillion.

Of importance is that Islamic finance has also been able to respond to the changing demands of consumers and businesses by providing the range of differentiated products and services. Today, Islamic finance offers an extensive spectrum of innovative and high quality financial products and services that include consumer financing, asset and wealth management and products from the Islamic insurance industry and capital markets. Islamic finance has also demonstrated its capacity to undertake project financing with the sukuk market becoming a highly competitive fundraising option for large scale projects and infrastructure development.

Today, in Malaysia, we have developed a comprehensive Islamic financial system that operates in parallel with the conventional financial system. The Islamic banking system in Malaysia currently accounts for 20 percent of our banking system while the sukuk market accounts for more than 50 percent of the bond market that is now 98% of GDP. Following the liberalisation initiatives in this decade, there is greater foreign institutional presence and substantial foreign participation in Malaysia's Islamic financial system. Of significance is that the participation from multinational corporations and international financial institutions from both the Muslim and non-Muslim countries. The Islamic financial system in Malaysia is also well supported by a robust regulatory and supervisory regime, legal and Shariah framework, and payment and settlement systems that are also important in supporting its sustainability.

### **Islamic finance: Strengthening international economic and financial linkages**

The internationalisation of Islamic finance has in a large part been facilitated by increased liberalisation initiated in this decade and by the further development of the international Islamic financial infrastructure. This trend has prompted Islamic financial institutions to venture beyond their domestic borders. Today, there are more than 600 Islamic financial institutions that operate in more than 75 countries. Similarly, the liberalisation of the Islamic financial markets has resulted in increased foreign participation to raise funds in these markets. This participation also includes institutional investors that have surplus funds for investment. This wave of internationalisation of Islamic finance has continued unabated despite the challenging global economic environment. In financing trade and investment activities, it has influenced new global patterns of trade and financial flows. In particular, it has strengthened financial and economic ties between Asia and the Middle East. In strengthening international financial linkages between nations, it reflects its potential for the diversification of risks and for the efficient allocation of resources across borders.

The fastest growing segment of the Islamic financial system is the sukuk market which has become a significant platform upon which international financial and economic inter-linkages are being fostered. Sukuk instruments are fast emerging as an attractive new asset class for investors while becoming a preferred financing and capital raising option for issuers. Growing at an average annual rate of about 40 percent, the global sukuk market has demonstrated its ability to effectively intermediate funds across borders, allocating surplus funds from one part of the world to productive investment opportunities in other parts of the world. Today, the sukuk market has become a truly global product, generating significant cross-border financial flows.

In tandem with the rapid internationalisation of Islamic finance, this decade has also seen the increased emphasis that has been given to the development of the international Islamic financial infrastructure relating to financial stability. The Islamic Financial Services Board (IFSB) was established in 2002 as the international prudential standard setting body for the Islamic finance industry. With only nine regulators as members when it was established, the IFSB now has membership of more than fifty regulators from both Muslim and non-Muslim countries. In considering risks that are specific to Islamic finance, the IFSB has introduced standards for capital adequacy, risk management and corporate governance as part of the regulatory regime to strengthen the resilience of Islamic financial institutions. The work of the IFSB has not only contributed to the orderly global expansion of Islamic finance, but has also contributed towards achieving a cohesive cross-border regulatory framework and international best practices for the Islamic financial system.

During this year, two new initiatives have been introduced to further strengthen the international financial infrastructure in Islamic finance and to promote the sound and efficient functioning of its financial markets. The first is the establishment of the Islamic Financial Stability Forum (IFSF) that serves as a platform for cross-border engagement among regulators to discuss efforts to achieve financial stability in the Islamic financial system. The forum aims to promote better understanding of the developments in the Islamic financial system and their implications for national and global financial stability.

The second major breakthrough for Islamic finance is the establishment of the International Islamic Liquidity Management Corporation (IILM) in October this year - a liquidity management infrastructure for Islamic financial institutions. It represents a concrete collaboration and commitment by twelve regulatory authorities to establish a mechanism for more efficient management of liquidity across borders, and to address the issue of liquidity management in achieving financial stability. Cumulatively, these efforts serve to contribute towards the continued resilience of the global Islamic financial system.

### **Addressing the financial reporting issues in Islamic finance**

As the Islamic finance industry continues to grow and expand beyond domestic boundaries, the role and support of the accounting profession and standards setters will become more important. Applying the existing accounting frameworks and conventions to Islamic financial institutions may prove to be more challenging given the unique features of Islamic financial transactions such as the equity based and profit sharing contracts. In addition, given the risk sharing features of these contracts, it may raise the case for a higher level of transparency for users to better understand and be better positioned to assess the underlying risks and their likely financial impact.

More broadly, there are the questions on whether the current international accounting framework adequately addresses the different Islamic financial transactions, structures and business models which are continuing to evolve as the industry develops and matures. There are differences in views on how conventional accounting concepts, such as reporting based on substance over form, and cash flow discounting principles, can be applied to Islamic financial transactions. There is therefore a need for greater understanding on these issues to further evolve solutions that would improve the value of the financial reporting.

### **Harmonisation of financial reporting standards in Islamic finance**

An important development that has accompanied the internationalisation of Islamic finance is the effort to enhance the cross-border comparability of Islamic financial transactions. In this area, the Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI) has made contributions towards improving the measurement approaches for Islamic transactions and the overall quality of financial statements. There has also been greater cooperation at the regional level through the recently formed Asian-Oceanian Standard-setters Group (OSG) to examine the technical issues in financial reporting of Islamic finance. The efforts by AAOIFI and OSG represent important contributions to current efforts to evolve

an accounting framework that is appropriate and that will support further the global development of Islamic finance. It is important that the standards setting bodies such as the IASB is engaged in this process to complement, and to leverage on the current global efforts to converge international accounting frameworks.

### Conclusion

Allow me to now conclude. The internationalisation of Islamic finance pushes forward the new frontier that brings with it tremendous potential to become a further means by which cross border financial flows are intermediated between economies from different parts of the world. Islamic finance, as an increasingly important component of the international financial system can be leveraged upon to facilitate surplus funds to be

intermediated to economies that present new opportunities. As Islamic finance continues to gain global acceptance, strengthening the accounting reporting, auditing and disclosure standards are very much a vital part of this process.

As we enter this new phase of globalisation in which Islamic finance is very much a part of, the cumulative efforts of the standard setters, the regulators and the industry will raise the potential to address the many challenges before us. We need to leverage on the respective areas of strengths and address the weaknesses with unrelenting perseverance. While a more connected world may bring with it new vulnerabilities, I do believe it also brings with it new prospects for new opportunities, new relationships and new hope for a greater shared prosperity.

**Svein Gjedrem Colloquium -  
“Role of Central Banks in Emerging Economies”  
Norway 18 November 2010**

by

**Tan Sri Dato’ Sri Dr. Zeti Akhtar Aziz**  
Governor, Bank Negara Malaysia

## **Introduction**

Central Banks continue to be challenged with changing demands as the environment before us is rapidly being transformed. These fundamental and pronounced changes have prompted calls for a review of the role of Central Banks in the financial system and in the economy. Frequently, such calls have been precipitated during a financial crisis, as was the case during the Asian financial crisis and more recently during this current global financial crisis. However, such institutional reforms undertaken in periods of exceptional conditions risks influencing the nature and direction of the reforms. While the reforms following a crisis may address the immediate term demands, of equal importance is the medium and the longer term implications of the reforms. Perhaps, an important lesson for Central Banks is that such reinvention and modernisation should be undertaken during the good times so that we will not be subjected to such changes during the worst of times. In essence, in such a dynamic environment, Central Banks need to continue to adjust and evolve to remain relevant and, thus, useful.

It is my great honour to be invited to speak at the Norges Bank Colloquium held in honour of Governor Svein Gjedrem. Let me take this opportunity to congratulate Governor Gjedrem for the achievements of the Bank under this leadership during his twelve year terms in office. My remarks today will focus on the role of Central Banks from the perspective of emerging economies and more specifically in the context of Central Banking in Asia as we confront the challenges in this rapidly changing global economic and financial environment.

## **Central Bank Mandates**

While there is no unique blueprint for the design of the institutional arrangements for a Central Bank, of importance is that it needs to be relevant to our own circumstances. But of importance is that there is clarity on the mandate, the governance framework and the areas of accountability of the Central Bank. And that needs to be supported by the empowering legislation to ensure that the Central Bank has at its disposal the capabilities to deliver the mandate.

Central Banks in emerging economies generally have a broader mandate beyond the traditional mandates of monetary and financial stability. Even within these traditional mandates, the role of Central Banks have varied considerably. In the mandate of monetary stability, it has ranged from having the narrow mandate of price stability to the mandate where price stability is the primary role of the Central Bank while due consideration is also given to economic and employment objectives. While for some the mandates are clearly hierarchical, for others, the multiple mandates involve assessments of the trade-offs.

The Central Bank mandate of financial stability is less clearly defined particularly in circumstances in which the supervisory function does not reside in the Central Bank. The majority of Central Banks in emerging economies in Asia, however, has the responsibility of the supervisory function although for three of the region’s major economies - Japan, China and Korea, this function resides in a separate agency. Even for Central Banks that has the responsibility of the supervisory function, the specific outcomes to be achieved are less clearly defined compared

to the mandate for price stability. In Malaysia, our new Central Bank Act of 2009 has defined this mandate in terms of the risks to financial stability - that is, the risk of the disruption to financial intermediation, the risk of disruption to the orderly functioning of financial markets and the risk of loss of confidence in the financial system.

Common to most Central Banks in emerging economies is the mandate to develop the financial system. Given the stage of development of financial systems in emerging economies, this is an important mandate not only to enhance the financial intermediation process in the economy but also for the purposes of facilitating the mandate of monetary and financial stability. This mandate has involved institutional building, financial market development and the strengthening of the financial infrastructure including that of the payment systems and the legislative framework.

The decade of financial reforms and financial sector development that followed the Asia financial crisis have resulted in more developed and resilient financial systems that is now better able to intermediate the more volatile financial flows and to withstand shocks to the system. During the recent global financial crisis, most emerging economies in Asia did not experience any disruptions to the financial intermediation process and credit flows continued uninterrupted providing important support to economic activity. It also allowed the financial markets to facilitate the transmission of policies to support the economic recovery.

This developmental role is also significant in contributing towards preserving financial stability. The development of the domestic financial markets and the development of a more diversified financial system has reduced the risk of over concentration on the banking system, a feature that was prevalent during the Asian financial crisis. The introduction of new institutional arrangements has also been aimed at keeping abreast with innovation, the advancement in technology and the intensification of globalisation. It has also allowed for the adoption of a more balanced approach towards regulation in which it is complemented by the newly developed

mechanisms for surveillance including across borders, strengthened supervisory oversight and institutional arrangements for resolution.

## Central Banks and Financial Markets

A more recently much discussed mandate is the role of the Central Bank in ensuring the orderly functioning of financial markets. Orderly functioning financial markets are vital not only for the efficient allocation of financial resources in the economy but it is also essential for the transmission of the monetary policy and for preserving financial stability. While competitive forces are expected to result in efficient and optimal outcomes, Central Banks in emerging economies have had the important role of balancing between the market forces and intervention with the objective of ensuring the orderly functioning of the financial markets. It needs to be recognised that several important preconditions need to be in place to generate equilibrium prices that reflect the underlying fundamentals. This includes the institutional and market infrastructure, the incentive structure, the rules of the game and the level of financial literacy that recognise and understand the market signals. When these elements are still yet to be fully developed in many emerging economies, it increases the risk to instability. Thus, as a result of the stage of development of such markets, or its size or prevailing market imperfections, emerging economies have tended to be more vulnerable to greater volatility and circumstances in which markets do not self-equilibrate. The recent global financial crisis has shown that such dislocations have occurred even in developed financial systems. Institutional structures and rules that become deficient and less relevant heighten the risk for such unstable market conditions. Experience has also shown that such market dislocations have severe and far reaching adverse implications on the overall economy.

For the effectiveness of such interventions, however, there needs to be clarity in the objectives to be achieved by such Central Bank presence and the results that are expected to be delivered. Of importance, there needs to be the recognition of the temporary nature of such interventions and the challenge of efficiently unwinding such presence when the objectives

are achieved. There is also the need to manage the risks of unintended consequences of such direct Central Bank interventions. Such risks could include the potential for circumvention, or the gravitation to other markets not protected by such intervention. There could also be potential costs associated with such interventions, not only the current costs, but also the cost to future generations.

While the pace of deregulation and liberalisation may differ across emerging economies, there is a discernable distinct shift to greater market orientation in this recent decade. These reform efforts have been reinforced by efforts to develop the financial markets and financial infrastructure. Within this framework, the nature of intervention has been in the form of direct presence in the financial markets, the setting of rules and regulation, and in the resolution of problem financial institutions. Such interventions were evident during the Asian financial crisis in the late 1990s to restore stability in the financial markets. This in turn created conditions for the resumption of the financial intermediation process. While the efficient functioning of the financial system was vital for the economic recovery in Asia, more important was the comprehensive set of policies that produced the recovery. Within a year of the introduction of the pro-growth measures, most of the crisis affected economies experienced a strong recovery.

More recently, the global financial crisis has seen several rounds of wide ranging direct market interventions to restore the smooth functioning of these markets. Described as actions taken in the most extraordinary and exceptional circumstances, it demonstrates that this phenomenon of severe market dislocations has the potential to occur even in the most developed of the financial systems. As these massive interventions continue, primarily in the public and private securities markets, the concern is on its potential consequences on other parts of the world, in particular, to the emerging world. In the now more interconnected and interdependent world, these actions are already creating significant shifts in capital flows. Important for

the emerging world is the ability to intermediate such surges in capital flows and to manage the risks associated with such liquidity inflows and its potential to undermine the current recovery.

A further element that has frequently been underestimated is the role of behaviour which has had a major influence on the dynamics of the financial markets. Extreme forms of such behaviour are evident in asset and foreign exchange markets. While the former is prone to boom and bust, the latter is prone to overshooting. While several emerging economies have successfully relied on macro prudential measures to contain the formation of such asset bubbles, the foreign exchange market is not like any other market. With a daily transaction amounting to USD4 trillion, it is the most liquid and dynamic market in the world. The role of sentiment and expectations has resulted in a market that is frequently prone to excessive movements and overshooting. As highly open economies, disruptions and disequilibrium in the foreign exchange market have far reaching consequences in the real economy. Intervention operations to maintain orderly market conditions reinforced by sterilisation operations have aimed at ensuring liquidity in the market and at ensuring that the market conditions reflect the underlying economic fundamentals. Similar to the presence in other financial markets, this is to ensure the sustainability of the efficient functioning of the market.

### **Central Banks and Crisis Containment and Management**

The world going forward is likely to continue to be affected by financial crisis. History has shown that there have been more than a hundred distinct banking crises in this recent two decades. The prospect of surviving such a crisis is not only about building resilience but also having the capacity to manage it. Central Banks have a critical role in crisis containment and management, in particular, to provide liquidity, to restore the efficient functioning of financial markets, to lead resolution programmes and to restore confidence to the financial system.

Given that the Central Bank is the lender of the last resort, the Central Bank is in the front line of actions to restore stability. Regardless of the institutional arrangements for the supervision function, - of whether it is based on an integrated model or a model that is organised along sectoral lines, effective coordination is vital to effectively safeguard financial stability. Established arrangement for coordination avoids a piecemeal approach by any individual agency in the system and ensures a comprehensive response to the crisis. Greater coordination across agencies also allows for prompt actions to be taken.

Elements for crisis management have largely been put in place in several of the emerging economies in Asia. This has included a framework for rigorous surveillance for the early detection of risks and vulnerabilities, the range of policy instruments to address the build-up of risks, the governance and accountability framework as well as the coordination framework. Regardless of whether the supervisory responsibility resides at the Central Bank, the role of the Central Bank in surveillance for macro-economic management, and its direct contact with the financial markets in its money market and reserve management operations can be leveraged upon to support the financial stability mandate. This allows for a more comprehensive response in containing and managing the crisis.

In Asia, as regional financial integration intensifies, there has been greater regional cooperation and collaboration. During the Asian financial crisis, the management of the crisis was by the individual economies. As the challenges become more complex, standalone actions may not achieve the desired outcomes. Moreover, the perceived best solution for one country may have unintended consequences for collective stability. Asia has, thus, come together collectively to conduct regional surveillance with concrete steps to establish financial support networks, to develop regional financial markets and payment systems. Such collaboration also provides a collective voice and representation and the potential to be heard in the sphere of global policy formulation.

## Modernisation of the Central Bank

As central banks advance forward into the future of great uncertainty, the challenge of the new environment demands new institutional capability for the central banks to remain effective in delivering our mandates. Central Banks also need to undertake its own transformation and modernization. Such institutional capability enhancement may involve changes in the institutional arrangements, organizational and governance structures and practices, the empowering legislation and the talent required. Such organisational development would thus require continual reinvention to adjust to the new realities of the changing environment.

In most emerging economies, the largest concentration of talent resides in the Central Bank. In this new environment, this talent needs to have new capabilities to deal with complex issues from different perspectives that are no longer based on functional boundaries. While this involves horizontal collaboration across the organization, it also requires management of relationships including with the government while retaining the independence of the organization. This would require institutionalizing the channels for information flows, governance structures and clarity of accountabilities as well as the mechanisms for dealing with disputes. Cumulatively, this would provide for a constructive relationship while preserving the independence of the Central Bank.

An essential element in Central Banking that is paramount in an environment of great uncertainty is having a well-developed communication strategy. Unlike the mature evolution of communication strategy in the conduct of monetary policy, Central Banks' communication with respect to financial stability is still very much in its early stage of development. Indeed, the recent crisis has clearly surfaced the need for Central Banks and policy makers to design communication strategy that balances the objective of providing information to the market and the public, while achieving an optimal outcome of enhanced financial stability.

## Conclusion

Allow me to conclude. The rapidly changing global economic and financial environment will continue to exert much demands on the Central Banks. While extensive modernization and transformation of Central Banks can be implemented at the national level, the increasingly interconnected and interdependent

world demands a greater emphasis on global perspectives and considerations. The greater interface at the international level has involved enhanced engagement to concrete collaborative actions. The common objective is surely for an inclusive participation in the international financial system that will facilitate the common agenda for a self-sustaining global growth and development. Thank you for your attention.

## CALENDAR OF EVENTS July – September 2010

### 7 Oct 2010

The Bank and Bank of Mauritius signed a Memorandum of Understanding (MoU) to establish a collaborative framework aimed at enhancing mutual co-operation on capacity building and human capital development in the financial services industry, including in the area of Islamic financial services sector. In recognition of the growth potential of Islamic finance and Malaysia's leading role as the centre for Islamic finance, the MoU will pave the way for both countries to strengthen co-operation in the development of talent, expertise, business linkages and infrastructure support in Islamic finance.

On another occasion on 10 October 2010, the Bank and Banque de France signed an MoU to promote greater cooperation in the area of financial services. The signing also reflected the commitment of both parties to cooperate towards the advancement of the Islamic finance industry in the respective countries. The MoU aimed to foster long-term strategic developments in conventional and Islamic finance between France and Malaysia, focussing on three key areas; namely, capacity building and talent development; strengthening financial market infrastructure; and enhancing cross-border financial activities.

### 8 Oct 2010

In her luncheon address at the 2010 Institute of International Finance (IIF) Annual Membership Meeting in Washington D.C., Governor Dr. Zeti said that generating growth and a long lasting recovery was the primary priority for the global economy in the aftermath of the recent crisis. She noted that while economic stimulus is vital for crisis containment, it will not be sufficient to produce a self-sustaining recovery. The challenge then is essentially that of economic restructuring and transformation, reform and rebuilding of the institutional capacity to remain effective in the new environment and be well positioned to manage future shocks. Governor also highlighted the potential for emerging Asia to rise to these challenges in the new global economic and financial environment.

### 10 Oct 2010

In her luncheon address at the IMF-World Bank Annual Meetings in Washington D.C., Governor highlighted the importance of Islamic finance in strengthening financial linkages as evident with the emergence of sukuk as an attractive new asset class for investors and a competitive form of financing for business. She added that the sukuk market, being the most vibrant segment in Islamic finance, has evolved into a truly international market, generating significant cross-border flows as funds are raised from beyond domestic financial markets. Governor also reiterated that Islamic finance can be leveraged upon to foster greater financial flows across borders to contribute towards the agenda of enhancing a mutually reinforcing growth and to achieve global aspiration of a self-sustaining, balanced and long lasting economic progress and development.

### 22 Oct 2010

The Bank as the Malaysia International Islamic Finance Centre (MIFC) Secretariat announced the successful closing of an Emas U.S. dollar sukuk issuance by the Islamic Development Bank, the first U.S. dollar sukuk issuance by a multilateral development institution in Malaysia. The sukuk issuance followed a series of foreign currency Emas Islamic financing instruments issued under the MIFC initiative and reflected Malaysia's evolution into a multi-currency platform for sukuk issuances.

## 25 Oct 2010

The Bank hosted the Global Islamic Finance Forum (GIFF) 2010 with the theme “Islamic Finance: Opportunities for Tomorrow”. The event was held in Kuala Lumpur from 25th to 28th October 2010. A key international event in the calendar of Islamic finance, the GIFF 2010 brought together regulators, scholars and financial industry players to discuss and exchange insights on the growth potential and opportunities in the internationalisation of Islamic finance. On the same day, eleven central banks and two multilateral organisations signed the Articles of Agreement for the establishment of the International Islamic Liquidity Management Corporation (IILM), an initiative aimed to assist institutions offering Islamic financial services in addressing their liquidity management in an efficient and effective manner. The IILM will issue high quality Shariah-compliant financial instruments at both the national level and across borders, thereby facilitating liquidity management in the Islamic financial systems. The signatories of the IILM Articles of Agreement are Governors and their representatives from the central banks or monetary agencies of Indonesia, Iran, Luxembourg, Malaysia, Mauritius, Nigeria, Qatar, Saudi Arabia, Sudan, Turkey and the United Arab Emirates. The Islamic Development Bank and the Islamic Corporation for the Development of the Private Sector are the multilateral organisations participating in the initiative. Subsequently on 13 December, the IILM has appointed Governor Dr. Zeti as the first Chairperson of its Governing Board.

## 26 Oct 2010

In conjunction with GIFF 2010, the Bank announced that the Royal Award for Islamic Finance has been awarded to Shaikh Saleh Abdullah Kamel for his visionary drive, extraordinary leadership and personal commitment in spurring the global accessibility of Islamic finance. Spearheaded by the Malaysia International Islamic Financial Centre (MIFC) initiative, the award is regarded as a global benchmark in identifying exceptional individuals who have inspired the development of Islamic finance worldwide. The award focuses on the individuals’ record of achievement and outstanding contribution towards the development and advancement of Islamic finance globally.

On the same day the Bank also announced the release of Shariah Resolutions in Islamic Finance (Second Edition) book, a compilation of all Shariah resolutions made by the Bank’s Shariah Advisory Council between 1997 and 2009. It is a continuation of the Bank’s efforts to deepen the understanding on Shariah interpretations and increasing the transparency level on juristic reasoning for the rulings in Islamic finance, and thus, increasing the appreciation and acceptance of Shariah decisions.

## 2 Nov 2010

The Bank announced the new members of the Shariah Advisory Council (SAC) for a period of three years, effective 1 November 2010. The SAC is the highest authority in the determination of Shariah in Islamic finance and it plays a pivotal role in ensuring the sanctity of Shariah rulings referred by Islamic financial institutions as well as the court and arbitrator. The SAC consists of qualified Shariah scholars, jurists and market practitioners who have vast experience in banking, finance, economics, laws and application of Shariah, particularly in the areas of Islamic economics and finance.

### 3 Nov 2010

The Bank announced the implementation of a maximum loan-to-value (LTV) ratio of 70%, applicable to the third house financing facility taken out by a borrower, with immediate effect. Financing for purchase of the first and second homes are not affected and borrowers will continue to be able to obtain financing at the existing prevailing LTV level applied by banks based on their internal credit policies. The measure aims to support a stable and sustainable property market, and promote the continued affordability of homes for the general public.

On the same day the Bank also announced the introduction of the Financial Capability Programme as part of the Bank's continuous efforts to raise the level of financial literacy and to promote sound financial and debt management by Malaysians. The Programme will be offered by Agensi Kaunseling dan Pengurusan Kredit (AKPK) through its establishments nationwide and will equip individuals with important knowledge for responsible financial decisions by gaining practical understanding and skills in money and debt management.

### 10 Nov 2010

In her speech at the World Congress of Accountants (WCOA) in Kuala Lumpur, Governor said that the internationalisation of Islamic finance offers potential for it to become a further means by which cross border financial flows are intermediated between economies worldwide. She added that Islamic finance, as an increasingly important component of the international financial system, can be leveraged upon to facilitate surplus funds to be intermediated to economies that present new opportunities.

### 12 Nov 2010

At its final meeting for 2010, the Bank's Monetary Policy Committee (MPC) decided to maintain the Overnight Policy Rate (OPR) at 2.75%. The MPC considered the current level of OPR as appropriate and consistent with its latest assessment of economic growth and inflation prospects. The stance of monetary policy continued to remain accommodative and supportive of economic growth. The committee also approved the schedule of MPC meetings for 2011.

### 15 Nov 2010

The Bank announced the appointment of Puan Nor Shamsiah Mohd Yunus as Deputy Governor for a three year tenure effective 16 November 2010. Deputy Governor Puan Nor Shamsiah joined the Bank in 1987 and has extensive experience in the development of prudential regulation, legislation, policies and guidelines for the financial sector. Prior to this appointment, she was the Assistant Governor responsible for the supervision of financial institutions under the purview of the Bank as well as overseeing the Bank's Risk Management Department.

### 18 Nov 2010

In her speech at the Svein Gjedrem Colloquium – "Role of Central Banks in Emerging Economies" – in Oslo, Norway, Governor highlighted that Central Banks have a critical role in crisis containment and management, in particular, to provide liquidity, to restore the efficient functioning of financial markets, to lead resolution programmes and to restore confidence to the financial system. She said as Central Banks move forward into the future of great uncertainty, the challenge of the new environment demanded new institutional capability for them to remain effective in delivering their mandates.

### **22 Nov 2010**

The Bank announced that the Malaysian economy registered a growth of 5.3% in the third quarter of 2010, driven by domestic demand amid slowing external demand. The expansion in domestic demand was supported by private sector spending while the slowdown in the global economy has led to the moderation in external demand. On the supply side, all major economic sectors, except mining, continued to expand during the quarter at a more moderate pace.

### **21 Dec 2010**

Governor Dr. Zeti was honoured with the 'Lifetime Achievement Award' at the Annual Islamic Business & Finance Awards held in Dubai. The Islamic Business and Finance Awards is considered one of the most prominent events in the finance industry throughout the Gulf region. The annual ceremony is designed to highlight, encourage and reward the exceptional performance and growth of Islamic business and the finance community. The awards are also widely considered a benchmark of excellence in the industry.