FINANCIAL SECTOR MASTERPLAN

The Financial Sector Masterplan (FSMP) which was launched in March 2001 sets out the broad strategies for the development of the financial sector over a ten year period. The end objective is to evolve the financial system into one which is competitive, resilient and dynamic. Efforts that were undertaken during the initial stage of the implementation of the FSMP were predominantly directed towards enhancing the capacity and capability of domestic financial institutions in order to enhance their level of effectiveness and competitiveness, strengthening the regulatory and supervisory framework, promoting a safe and efficient payments system as well as developing the framework on consumer education and protection.

During the first three years of the implementation of the FSMP, a total of 31 out of the 119 recommendations have been fully implemented, with an additional 24 recommendations are being implemented on a continuous basis. Details of the recommendations which have been fully implemented are as listed in the accompanying table.

Completed Recommendations

Banking Sector	
R3.4	Liberalise restrictions on salaries and staff mobility in the banking industry to enable the industry to attract the best talent and reward them accordingly
R3.5	Uplift restriction on employment of expatriates to attract the best international talents to meet the demand for expertise in specific areas of banking
R3.6	Establishment of board committees, namely Nominating, Compensation and Risk Management Committees to further enhance corporate governance standards
R3.7	Allow group rationalisation through cross-selling of products and consolidation of back-office processes as well as facilitate the merger of commercial banks and finance companies to further enhance efficiency and competitiveness
R3.12	Encourage outsourcing of non-core functions to gain greater strategic focus and efficiency
R3.14	Encourage the development of new delivery channels to increase the range of products and services to further enhance competitiveness
R3.15.1 and R3.15.2	Introduction of a simpler product notification process to provide incentive for development of new and innovative products, and outline clear set of guidelines providing criteria for product notification and specific product approval requirements
R3.21	Issuance of examination manuals for implementation of risk-based supervision with supervisory focus on high risk areas and greater attention on weak institutions
R3.28	Allow market forces to shape developments in the payments system to allow greater competition and increase innovation in payments system
Insurance Sector	
R4.1	Remove restrictions on outsourcing to enable insurers to further develop core competencies and effective business strategies
R4.2	Allow eligible insurers to use the internet as a distribution channel to enhance competitiveness and efficiency of the insurance industry
R4.6	Relax the restrictions on employment of expatriates to accelerate the development of skills and expertise in the industry
R4.16	Increase the statutory minimum paid-up capital of insurers to enhance their financial resilience and to accelerate the consolidation of the industry in order for domestic insurers to capture the size and scale needed to compete effectively in a more deregulated and liberalised market
R4.18	Establish board committees with specific responsibilities and enhance disclosure of compensations to directors and senior management to ensure they act in a manner that will increase shareholder value

R4.19 Raise the entry requirements for the agency force to ensure the recruitment of more qualified and competent agency force
R4.20 Introduce additional compulsory exams as part of continuing education programmes for agents to upgrade their knowledge and skills
R4.21 Further strengthen performance-based supervision to maintain stability under more deregulated and competitive market conditions
R4.26 Introduce 'best advice' regulations to enhance consumer protection and professionalism in the sale of life insurance products by insurance intermediaries
R4.27 Strengthen regulations on unfair trade practices to ensure sound business practices and fair treatment of consumers
R4.29 Allow financial and non-financial institutions to acquire interests in direct insurers to create business synergies

Islamic Banking and Takaful

R5.3 Build strong management through the establishment of board committees, benchmarking and employment of experienced and qualified staff
R5.6 Increase the number of takaful operators to accelerate the expansion of takaful industry

Development Financial Institutions (DFIs)

R6.4 Introduce a systematic framework for sourcing funds to ensure the appropriate and adequate funding for the operations of DFIs.
R6.7 Establish a legislative framework to provide for the regulation and supervision of DFIs to ensure that DFIs' policies and objective are consistent with the national policy objectives

Alternative Modes of Financing

R7.2 Establish a RM500 million Venture Capital Fund to increase the availability of Venture Capital financing and stimulate new ventures
R7.3 Introduce further tax incentives for the Venture Capital industry to promote the growth of Venture Capital
R7.4 Liberalise the MESDAQ listing requirements to facilitate the exit of Venture Capital companies from their investments

Labuan International Offshore Financial Centre

R8.3 Adopt a consultative and market driven approach to create a conducive tax and business environment to enhance the competitiveness and attractiveness of Labuan
R8.6 Strengthen Islamic banking and finance as well as takaful to develop Labuan with a strategic focus on Islamic products and services
R8.7 Enhance Labuan International Financial Exchange (LFX) to be a one stop financial exchange for residents and global companies

The recommendations implemented and the various initiatives undertaken during the first three years of implementation have contributed towards enhancing capacity and capabilities of domestic financial institutions, as well as providing a robust infrastructure to ensure overall stability of the financial sector.

BANKING SECTOR

Initiatives that were undertaken during Phase 1 of the implementation of the FSMP were primarily focused on building the capacity and capabilities of domestic banking institutions to enhance their competitiveness and building the infrastructure within which the banking institutions operate to promote the development of a more robust banking system. Attention was also accorded towards creating the necessary infrastructure for a more market-based consumer protection framework.

One of the key milestones for Phase 1 of the FSMP is to drive performance improvement. The industry-wide benchmarking programme which was initiated in 2002 provided banking institutions with a tool to enable more effective strategic focus and business planning and provided the relative ranking of each institution in all areas of performance. The benchmarking exercise also enabled Bank Negara Malaysia to assess the progress of the industry, particularly the performance improvements recorded by the domestic financial institutions thereby determining the speed of transition and progress.

The domestic banking institutions have steadily recorded improvements over the past three years yielding desirable results. The consolidation programme has resulted in larger and better capitalised domestic banking institutions. The average total assets and shareholders' funds per domestic commercial banks have more than doubled from RM18.1 billion as at end-1999 to RM44.9 billion as at end-2003 and from RM1.4 billion as at end-1999 to RM3.8 billion as at end-2003 respectively. The profitability levels have increased over the past three years. Return on average assets and return on average equity of the domestic banks have increased from 0.7% and 8.4% in 2001 to 1.2% and 13.4% in 2003 respectively. Pre-tax profit per employee had also increased significantly from RM50,196 in 2001 to RM108,728 in 2003. The cost to income ratio also declined from 41.2% in 2001 to 40.1% in 2003. Improved management of the operating costs had stabilised the operating expenses as a percentage of average assets at RM1.42 per every RM100 of assets over the same time period.

The banking institutions in Malaysia operate in an open environment. Both the domestic and foreign controlled banking institutions are governed by the same set of legislations and regulations, with the only remaining restriction on foreign banks being in the area of branching. Foreign controlled banking institutions nevertheless have a strong presence in the market, accounting for 26%, 27% and 25% of the commercial banking assets, loans and deposits markets respectively.

Competition has resulted in the narrowing of gross interest margins of commercial banks from 4.14 percentage points in 2001 to 3.69 percentage points in 2003. In this more competitive environment, the domestic banking institutions have been able to sustain their market share at 80%. The foreign banking institutions have expanded their loan market share mainly in housing loans. The domestic banking institutions continue to be the main provider of financing for businesses, particularly for the small and medium enterprises, where 83% of the loans to this sector were extended by the domestic banking institutions. The domestic commercial banks have also expanded their market share in the credit card business, which was previously the domain of the foreign controlled commercial banks to 47% of the market (2000: 43%).

To enhance the level of operating efficiency and allow greater strategic focus on business operations, banking institutions can now outsource non-core operations to third party service providers. They are also permitted to rationalise common internal operations such as treasury function and human resource management. A number of banking institutions also cross-sell products and services within the same banking group. Strategic alliances between banks and other banking institutions as well as non-banking institutions have also taken place to further enhance competition and innovation. One example is in the area of bancassurance and the sale of unit trusts. In addition, domestic banking institutions have also introduced new services such as wealth management and structured deposit products.

To enhance the delivery of products and services to customers, banking institutions have embraced innovative technology-based delivery channels such as internet and mobile banking. This widens the accessibility of banking services and facilitates seamless connectivity in the delivery of financial products and services to customers through the operation of one-stop financial centres. Efficiency of the banking sector has also improved, with the average time taken by commercial banks to process housing loan applications having declined from 4 days in March 2002 to 3.1 days and from 11 days to 9.5 days for new credit card applications. With greater emphasis on customer relationship, the percentage of customer complaints that are resolved within 14 days have improved from 82.1% in March 2002 to 87.6% in December 2003.

As a result of the significant progress made by the domestic banking institutions, liberalisation of the system has been brought forward in several areas. While the domestic banking institutions were allowed to offer full internet banking services beginning 1 June 2000, the locally-incorporated foreign banks were permitted to offer such services beginning 1 January 2002, earlier than was announced. The requirement for a non-resident controlled company to source at least 50% of its financing requirements from domestic banking institutions was also uplifted with effect from 1 April 2003.

A smooth functioning payments system which is efficient and effective is also important. As the payments technology and the structure of the financial services industry change rapidly, it is necessary to have a payments system which responds to this new environment. To encourage greater innovation and competition, Bank Negara Malaysia has shifted its role from being directly involved in the development process to a more facilitative role, particularly in the retail payments system. Bank Negara Malaysia will however, continue to ensure that minimum security standards are applied when any new systems are introduced. The Payment Systems Act 2003 was enacted to facilitate the development of payments system and to ensure that it is secure and efficient.

An important aspect of stability in the financial system relates to the ability of the system to undergo the transition to deregulation and increasing competition with no disruption in the level or reliability of services to customers. The customers also play an important role to drive performance improvement of the financial institutions. Crucial to this is active consumerism, which can only be attained with the public having the necessary information and understanding of financial products and services. Towards this, a 10-year consumer education programme was launched to disseminate information to consumers including information on consumer rights and responsibilities. In addition, efforts have also been put in place to encourage consumers to pursue formal administrative and legal redress for their grievances. Banking institutions are required to set up dedicated complaint units to manage complaints received from customers.

The banking system remains the largest provider of funds to the private sector, providing support to the various sectors of the economy. In line with the objective to develop a well-diversified financial system with well-functioning, deep and liquid markets, Bank Negara Malaysia continued to take an active role in the development of the bond market to meet the changing needs of the Malaysian economy. As a result, the bond market experienced a rapid growth since the Asian financial crisis. As at end-2003, the size of the bond market was equivalent to 87.6% of GDP, compared with 46.9% in 1996. The private debt securities (PDS) market has emerged as an important source of financing for the private sector since 1998. PDS outstanding represented 34.3% of GDP at end-2003.

To enhance the liquidity in the secondary bond market, the Guidelines on Securities Borrowing and Lending (SBL) Programme under the Real Time Electronic Transfer of Funds and Securities System were issued to support trading strategies for principal dealers and enhance the return on bond portfolio investment for investors. Through SBL, principal dealers (PDs) can now participate as both borrower and lender, which allow PDs to quote two-way prices more effectively and at the same time able to meet commitments of their treasury activities. In addressing the captive bond market issue and to promote the secondary trading, greater investment flexibility was accorded for insurance companies to invest in Malaysian Government Securities and PDS.

To increase the availability of risk management tools for market participants, more players were allowed to undertake repo transactions with the licensed financial institutions. The Prudential Standards on Asset Backed Securities Transactions by Licensed Institutions issued by Bank Negara Malaysia in 2003 helped in creating greater awareness and participation in securitisation transactions. Universal brokers have been allowed to participate in fixed income market and thus engage the services of money-brokers. A broader investor base is an important factor in contributing to liquidity in the secondary market.

Concerted efforts were also made to develop the Islamic financial markets to meet the demands of institutional investors such as the issuance of Islamic based Government investment issues and the development of a risk-free benchmark Islamic yield curve to help in the pricing and trading of Islamic securities. To further develop the Islamic capital market, the Government had provided incentives such as tax exemption for expenses incurred on the issuance of Islamic PDS. As a result of these efforts, the Islamic PDS market has grown significantly. Total outstanding of Islamic PDS stood at RM69.1 billion, or 46% of total PDS outstanding as at end-2003.

Measures that have been put in place over the past three years were implemented to ensure that the banking system will continue to support sustainable economic growth and to prepare the Malaysian banking sector for a more liberalised and global operating environment. The strategy for the banking system on the latter has been one of gradualism. A managed and sequenced deregulation and liberalisation process is adopted to ensure that financial reforms will be effectively implemented without destabilising implications on the system.

INSURANCE SECTOR

The recommendations implemented in the first phase of the FSMP are aimed at building the capabilities of domestic insurers to compete more effectively, strengthening the consumer protection framework and raising corporate governance standards to further enhance the protection of policyholders and shareholders value.

The capacity-building initiatives and measures implemented under Phase 1 of the FSMP have brought about positive developments in the industry over the last three years. Significant progress was achieved in the consolidation of the industry, particularly in the more fragmented general insurance sector, following the increase in the minimum paid-up capital requirement for insurers from RM50 million to RM100 million in 2001. A total of 15 mergers and acquisitions involving a total of 28 general insurers (including four composite insurers) have been successfully completed since 1999. As a result, the average capitalisation of general insurers strengthened by 54.4% from RM92.2 million in 2000 to RM142.3 million in 2003, improving the competitive position, and therefore better able to take advantage of the opportunities presented in the more open market environment.

Domestic insurers continued to maintain their dominant position in the general insurance sector, while also achieving productivity and profitability gains. As at end-2003, domestic insurers accounted for 73.3% of gross general insurance premiums, with the top five domestic insurers collectively controlling 31.8% of the total gross premiums in the industry. Employee productivity rose from RM498,857 in 2000 to RM797,923 in 2003. Overall profitability, as measured by gross premiums generated per employee, also improved, with domestic insurers sustaining a higher return on equity over foreign insurers (24.7% as against 20.4% by foreign insurers for the year 2003).

In the life insurance sector, significant attention was directed at developing new growth opportunities to increase the market penetration, and hence economies of scale. In this respect, domestic insurers secured a dominant position in bancassurance business, accounting for 76.6% of the total new insurance premiums generated through banking institutions in 2003. The commitment of domestic insurers to the development of bancassurance was supported by the encouraging sales of non-credit related products. Domestic insurers accounted for more than 80% of total non-credit related bancassurance business in 2003.

As at end-2003, a total of 12 life insurers had been given approval to enter into bancassurance arrangements with banking institutions. Business generated through this alternative distribution channel has quadrapled since 2000 to reach RM1,859 million in 2003. Two domestic insurers have successfully leveraged on the banking distribution network to become market leaders in bancassurance, with a combined market share of 36% of total bancassurance premiums generated in 2003. Bancassurance currently accounts for more than 38% of total new life business premiums in the market and has been a major factor contributing to the higher penetration of life insurance business in Malaysia which increased from 31.5% in 2000 to 36.4% in 2003.

Domestic life insurers succeeded in making further inroads in investment-linked business, which has emerged as a new growth area. The market share of investment-linked business attributed to domestic insurers has increased progressively from 16% in 2001 to 27.9% in 2003, contributing to a higher overall new business growth rate of 31.5% achieved by domestic life insurers in 2003, compared with 19.4% registered by foreign insurers.

The capacity building initiatives under Phase 1 of the FSMP also introduced a more flexible operating regime aimed at enabling domestic insurers to innovate, develop expertise and enhance efficiency levels. In this respect, the transfer of expertise to domestic insurers was facilitated by a more flexible policy on the appointment of expatriates. As at end-2003, a total of 42 expatriates were employed in the insurance industry to provide technical support in the areas of information technology, underwriting, actuarial and agency development. In the more flexible operating environment, an increasing number of insurers also leveraged on effective outsourcing strategies to lower costs while delivering higher service quality to their customers.

As at end-2003, more than 30 insurers were engaged in outsourcing arrangements, primarily in back-end support functions related to management information systems, data processing and customer service support. Consumer access to insurance was also made more convenient with approval given to 18 insurers to provide insurance over the internet, including eight insurers which are now able to offer motor insurance policies on-line through an interactive website. The process improvements enabled by these developments resulted in an overall improvement in the efficiency levels of domestic insurers. Domestic life insurers registered a lower expense rate of 34.2% in 2003 (2000: 36.8%), while the combined management expense ratio of domestic general insures improved to 24% in 2003 (2000: 24.4%).

Notwithstanding the positive developments in the industry, domestic players with significant overall market share have yet to emerge in the life insurance sector. In the transition to the second phase of the FSMP which envisages a level playing field between domestic and foreign players, the focus of policy will continue to be directed at developing domestic insurers, in particular life insurers, to consolidate domestic strengths in the penetration of alternative distribution channels, promote further innovation and facilitate strategic alliances.

The implementation of specific measures under Phase 1 of the FSMP to promote greater market discipline and strengthen corporate governance will support further performance improvements by domestic insurers. Enhanced disclosure requirements and the implementation of a comprehensive consumer education programme will empower consumers to make informed decisions on their choice of financial products and services which in turn, will serve as a strong incentive for improved product and service offerings by insurers. The strengthened corporate governance framework underpinning these initiatives will also serve to ensure that the board of directors posses the appropriate qualifications and experience to enable them to provide effective strategic direction to insurers in the more challenging environment. These measures supplement the changes being made to the regulatory framework and constitute important elements of a comprehensive approach to develop a robust, stable and dynamic insurance sector.

ISLAMIC BANKING AND TAKAFUL

The Islamic banking and takaful sector strengthened and expanded significantly during the first phase of the FSMP. The Islamic banking market share increased to account for 9.7% (2000: 6.9%) of total assets, 10.4% (2000: 7.4%) of total deposits and 10.3% (2000: 5.3%) of total financing of the banking system.

The takaful sector also expanded rapidly to constitute 5.7% (2000: 3.9%) of total assets and 6.0% (2000: 3.9%) of total contributions of the insurance industry. Phase 1 also witnessed significant progress being achieved in the development of the financial infrastructure for Islamic banking and takaful to function efficiently and effectively in parallel with conventional banking and insurance.

A significant milestone was achieved in the legal infrastructure development with the assignment of a dedicated High Court in 2003 to adjudicate all Islamic banking and finance cases. This development, reinforced by the formation of the Law Review Committee to undertake a holistic review of the present common law-based legislations will serve to establish an effective legal structure to cater for the unique nature of transactions in Islamic banking and finance. To complement these initiatives, a preliminary review of the Islamic Banking Act 1983 and Takaful Act 1984 was also undertaken.

The Shariah advisory structure was also strengthened with the amendment of the Central Bank of Malaysia Act 1958 which conferred a legal stature to the Shariah Advisory Council at Bank Negara Malaysia as the sole authority to decide on Shariah matters on Islamic banking and finance that fall under the purview of Bank Negara Malaysia. Guidelines will be issued to strengthen the structure of the Shariah Committees at the Islamic banking institutions and takaful operators and to define the composition, roles and responsibilities of these Shariah Committees. With the guidelines in place, the overall effectiveness of Shariah governance framework will be significantly enhanced.

The regulatory framework has been enhanced to address the characteristics of Islamic banking and takaful as well as to strengthen institutional capacity and financial resilience of Islamic banking and takaful players. The introduction of the standard framework for the computation of the rate of return in Islamic banking operations in 2001 provided greater transparency in the derivation of the rate of return to ensure a more equitable distribution of income between the bank and its depositors. The framework enhanced the capability of Islamic banking institutions to manage volatility in the rate of return more effectively and to remain competitive relative to the conventional banking institutions. The issuance of the Guidelines on the Specimen Reports and Financial Statements for Licensed Islamic Banks (GP8-i) in 2003 further increased financial disclosure to promote a more effective role of market discipline.

The capital position and financial resilience of the Islamic banking system strengthened significantly as a result of the regulatory requirement for conventional banking institutions participating in the Islamic Banking Scheme (IBS banks) to observe the minimum risk-weighted capital ratio for their Islamic banking portfolios. The minimum capital requirement of takaful operators would be raised from RM35 million to RM100 million with effect from 31 December 2004 to position takaful operators at par with conventional insurers.

The benchmarking programme for performance measurement has also been put in place to enhance the ability of Islamic banking institutions and takaful operators to assess their relative efficiency and formulate strategies to improve operational efficiency and to be at par with international best practices. In the area of corporate governance, the issuance of guidelines on the establishment of board committees, minimum qualifications and training requirements for directors, as well as the roles and responsibilities of independent directors in 2003 aim to strengthen the management of Islamic banking institutions and takaful operators as shareholders play a more active role in overseeing the effectiveness of the board of directors and management.

The issuance of the Guidelines on the Sell and Buy Back Agreement in 2002 enhanced the capacity of Islamic banking institutions to better meet their liquidity requirements as part of the efforts to develop a deep Islamic financial market structure. The variable rate financing mechanism introduced in 2003 provided a competitive tool for Islamic banking players in pricing product offerings to sustain their competitive position in a dual banking environment and concurrently assist Islamic banking institutions to effectively manage risks in pricing arising from asset and liability mismatches. The detail implementation framework for *mudharabah* (profit-sharing) and *musyarakah* (profit and loss sharing) financing is in the final stage of completion and is expected to further promote greater diversity in the mode of financing as the Islamic banking system advances into Phase 2 of FSMP.

The establishment of the Islamic Banking and Finance Institute Malaysia (IBFIM) in 2002 as an industry-owned training and research institute was another important progress achieved. IBFIM will spearhead the development of a pool of knowledgeable and competent Islamic bankers and takaful operators to meet the requirements of the Islamic financial industry. The organisation of the Islamic Banking and Takaful Week in 2001 and 2003 as well as the launching of the Consumer Education Programme have also played an important role in enhancing the level of public literacy in Islamic banking and takaful. Consumers are now more aware of the characteristics of Islamic banking and takaful, its underlying Shariah principles and concepts as well as the range of products and services offered by Islamic banking institutions and takaful operators.

Progress has also been achieved in the development of the institutional infrastructure. Two additional takaful operators have been licensed. In Islamic banking, a review of the existing "window" institutional structure of the IBS banks is being undertaken to prepare an enabling structure that can assimilate these developments and thus strengthen the prudential regulatory and supervisory regime.

As the progress of development has exceeded initial expectations in Phase 1, Bank Negara Malaysia has brought forward the liberalisation for the Islamic banking sector from Phase 3 to Phase 2, three years earlier than envisaged by the FSMP. The liberalisation of the Islamic banking sector will further hasten the pace of development and strengthen global integration to prepare the enabling environment for Malaysia to evolve as a regional centre for Islamic banking and finance.

DEVELOPMENT FINANCIAL INSTITUTIONS

In tandem with the strategic directions outlined in the FSMP, efforts undertaken during Phase 1 of the FSMP were focused on fostering a pool of efficient and effective DFIs to complement banking institutions in providing financing to identified priority and strategic sectors in the economy.

During Phase 1 of FSMP, strategies undertaken were centred mainly on strengthening the regulatory framework and capacity building of the DFIs. These strategies and initiatives include the legal infrastructure and policy development to support an orderly and sound development of effective DFIs.

A comprehensive regulatory and supervisory framework to facilitate the overall policy development of DFIs, especially in strengthening the financial and operational soundness of the DFIs was completed with the enactment of the Development Financial Institutions Act 2002 (the Act) in February 2002. The Act provides comprehensive mechanisms to ensure DFIs perform their mandated socio-economic functions. Following the enactment of the Act, six DFIs were subjected to the regulatory and supervisory framework embedded in the Act.

The major policy framework on building the capacity of DFIs aimed to ensure that as specialised development institutions, the institutions would have an effective role in supporting developmental needs of the nation. The DFIs are required to prepare and submit statement of corporate intent which highlight the planned business activities, implementation strategies and performance target within the mandated roles and Government's development objectives to ensure that DFIs remained focused on their mandated roles.

Prudential measures, namely, the classification of impaired loans and loan loss provisioning requirement have been introduced to ensure that the impaired loans and potential losses are identified and recognised in a timely manner, and loan assets and income are fairly and prudently stated. The maintenance of minimum liquidity has been introduced to enhance the financial soundness of DFIs. The policy on minimum capital requirement has been initiated to ensure DFIs have the financial capacity to sustain their operations. During Phase 1, regular on-site examinations of the six DFIs were conducted to assess the DFIs' performance in meeting the mandated roles.

To further equip DFIs as specialised development institutions, measures were undertaken to enhance their role in providing non-financial services. A joint project with the Japan International Cooperation Agency and selected DFIs was initiated to enhance the provision of advisory services of these DFIs to SMEs. The project will formulate action and implementation plans to enhance the institutional capability, including human resource skills.

To strengthen corporate governance, guidelines were issued to assist the DFIs and their stakeholders in instituting effective governance structure and oversight of Board of Directors. The main areas addressed in the guideline are duties and responsibilities of the board of directors, minimum requirements and rules governing the appointment of directors and chief executive officers as well as the establishment of board committees.

Moving forward, measures implemented will continue to be focussed on providing the enabling environment for the DFIs to operate efficiently and effectively. Strategies in the near term will focus on institutional development of the DFIs in the areas of risk management and the advisory and consultancy capability for other targeted customers, besides the SMEs. At the same time, efforts to promote institutional efficiency of the DFIs through the formulation of performance indicators will also be intensified to strengthen their financial and operational conditions.

MOVING FORWARD

The measures that have been implemented thus far were aimed towards providing a strong foundation on which the financial sector will be developed in the future. In addition to the measures that were implemented in the banking, insurance, Islamic banking and takaful, and development financial institutions sectors, significant strides have also been recorded in introducing alternative modes of financing in the domestic financial system. Significant progress has also been made in the development of Labuan as an international offshore financial centre. On the former, the Government has been in the forefront in the development of the venture capital (VC) industry, a key step towards transforming Malaysia into a knowledge-based economy. Initiatives such as the establishment of a one-stop centre for the VC industry, tax incentives and VC fund will continue to spur development in the industry. With the rapid recognition and growing demand for Islamic finance, Labuan has strategically promoted itself as an Islamic financial centre. Supported by the strong onshore Islamic financial sector, Labuan is well positioned to participate in the growing global Islamic financial market.

As we move forward, further efforts in institutional development will be undertaken, in particular, for the domestic financial institutions. This will be accompanied by gradual liberalisation, with the balance being made to ensure that the benefits will be maximised while any destabilising implications minimised. In addition, a more diversified financial services landscape will emerge with the capital market, insurance and venture capital having a significant role in the financial sector.