BANK NEGARA MALAYSIA
CENTRAL BANK OF MALAYSIA

FINANCIAL SECTOR BLUEPRINT 2011–2020

strengthening our future

STRONG

STABLE

SUSTAINABLE

This 10-year Blueprint is a strategic plan that charts the future direction of the financial system as Malaysia transitions towards becoming a high value-added, high-income economy


Savings
e-banking


A
PLAN
STRATEGY
SUCCESS

contents

Introduction

efficient

effective

foreword by the Prime Minister and Minister of Finance

A strong, comprehensive and progressive financial system underpins Malaysia's vision to become a developed nation by 2020, and for the private sector to assume a key role in realising this vision. Well-functioning and efficient financial institutions and markets, with sufficient flexibility to adapt to market needs and opportunities are central to the optimal allocation of capital to new areas of growth. With the nation's solid foundations established in this recent decade, Malaysia's financial sector has every potential to meet the imperatives of the new economic model which is built on the core tenets of high value-added entrepreneurship, creativity and innovation.

The Financial Sector Blueprint for the next ten years reinforces the Government's initiatives to drive Malaysia to become a fully developed nation. The financial system will have a key role in spurring new areas of growth, and facilitating our economic transformation. In charting a clear path that will further broaden and deepen Malaysia's financial system to achieve these objectives, it is paramount that careful attention be accorded to the stability of the financial system given the considerably more complex and challenging environment.

Malaysia's growth potential will also be intrinsically linked to the intensification of regional economic and financial integration. The financial sector in facilitating this will also expand its opportunities for risk diversification. The Blueprint also positions Malaysia to reap the full benefits of this development. It further cements Malaysia's leadership in Islamic finance to develop Malaysia as an international Islamic financial centre.

The Blueprint accords importance for Malaysia's development and growth agenda to be inclusive and sustainable. Critical to this outcome includes the deepening of our talent pool and enhancing financial education to increase the participation of all segments of society in the financial system. These important priorities will require close coordination and cooperation between the different parts of Government and the industry.

I would like to take this opportunity to express my appreciation to Bank Negara Malaysia and all those who contributed towards the formulation of this Financial Sector Blueprint. The Government is fully committed to this agenda, and with great clarity and commitment to a shared vision for a world-class financial system that will benefit all Malaysians, I have every confidence that Malaysia will realise the full benefits of the recommendations contained in the Blueprint to be implemented during the course of this decade.

Dato' Sri Mohd Najib

21 December 2011

message from the Governor

The Malaysian financial system has transformed significantly over this recent decade. Going forward, as Malaysia transitions towards becoming a high value-added, high-income economy, a new trajectory of transformation and growth is now envisioned for the financial system. This will also take into account the forces of change that are shaping the international and regional economic and financial landscape, including the new sources of risks to financial stability.

Over the course of the implementation of the first Financial Sector Masterplan from 2001 to 2011, the sector expanded by an annual growth of 7.3%. During this period, the Malaysian financial system has become increasingly more diversified, competitive and resilient. Institutional capacity building, financial infrastructure development, regulatory reforms and greater use of technology has yielded a financial system that is able to offer the range of financial products and services to consumers and businesses with more efficient delivery channels. The foundations for financial stability have also been significantly strengthened, while progressive liberalisation of the domestic financial sector has contributed to the further diversification of the financial system and its competitiveness. These developments have supported the effective and efficient functioning of the financial system without disruption even in the most challenging of times.

The next phase of transformation will build on these achievements to evolve a financial ecosystem that will further enhance the competitiveness and dynamism of the financial sector. This will be reinforced by strategies that will continue to promote inclusive access to financial services; encourage the development of the range of financial institutions, products and markets that will facilitate and drive the development of new domestic sources of growth; and accelerate Malaysia's regional and international connectivity.

This regional and international integration will deepen cross-border trade and investment activities and will allow for more effective intermediation of cross-border financial flows. An important part of this will be the internationalisation of Islamic finance and the development of Malaysia as an international Islamic financial centre.

Deep, liquid, and efficient financial markets, effective regulation and supervision, and a high degree of market transparency will continue to underpin the financial ecosystem. This will include the development of new instruments for risk management by businesses and households, more efficient clearing and settlements of cross-border trade and investment, in addition to a strengthened consumer protection framework. In this new environment, technology will continue to have a significant role in the offering of a broader range of financial products and services, and enhancing the efficiency of financial transactions through electronic means of payments and delivery channels.

In this Blueprint, the growth of the financial sector will be firmly anchored to the growth of the real economy. Equally important is that the quality of growth is balanced, inclusive and sustainable. The Blueprint also accords priority to the development of talent for the financial industry, a key enabler for the vision for the financial sector to be realised.

In finalising the Blueprint, Bank Negara Malaysia has benefitted from engagements with the industry, consumer groups, Government Ministries and agencies in addition to private corporations. The recommendations in the Blueprint reflect their collective input under an integrated approach to the development of our financial system that is focused on shared goals, and that leverages on the comparative strengths of the different components of Malaysia's financial system. The opportunity is taken here to record the Bank's gratitude to the Minister of Finance and the Prime Minister, YAB Dato' Sri Mohd Najib Tun Abdul Razak for the continued support given to Bank Negara Malaysia in the formulation and development of this Blueprint.

As with our first Financial Sector Masterplan, effective implementation will be key to realising the goals in this Blueprint. The Bank counts on the collective efforts of the industry, and other regulatory and public agencies in the implementation of the recommendations in this Blueprint and thus support Malaysia's transition towards becoming a developed nation with a comprehensive, resilient and progressive financial system.

Zeti Akhtar Aziz
21 December 2011

1 Overview

stable

strong

The Malaysian financial system

has played an important catalytic role in facilitating the economic transformation and growth of the Malaysian economy through the various phases of economic development. This strategic role of the Malaysian financial sector will increase in importance in the years ahead as Malaysia becomes even more integrated with the international financial system and the global economy. The rapid changes in the global economic and financial environment will also contribute towards transforming the operating landscape of the Malaysian financial system. At the same time, a more integrated and globalised environment, greater regionalisation, and the more sophisticated and diverse investment and financing needs of the domestic economy will require a financial system that is more progressive and dynamic to advance the nation's vision towards the attainment of a high value-added, high-income economy.

This 10-year Blueprint is a strategic plan that charts the future direction of the financial system as Malaysia transitions towards becoming a high value-added, high-income economy. To achieve this and to leverage on the opportunities going forward, consideration is made on the global trends and domestic economic forces of change that will affect the operating environment. The progress made in the financial system over the recent decade provides a foundation for the future growth and development of the financial system in the next ten years. This chapter discusses the global and domestic landscape that is likely to evolve over this decade and the financial system that will be developed during the course of the decade to 2020, as the Malaysian financial sector matures and advances to become more effective in performing its intermediation function in tandem with Malaysia becoming a developed economy.

1.1

global and domestic landscape

The Global Landscape

A fundamental transformation of the global economic and financial landscape is currently unfolding. Following the 2008 global crisis, uneven global growth with divergent growth prospects has resulted in the growing importance of the emerging economies. With the rise of growth centres in Asia, the Middle East, Latin America and Africa, the share of global economic output by the emerging economies has now exceeded that of the advanced economies, and is projected to account for about 60% of total world output by 2030 (OECD: Perspectives on Global Development 2010 – Shifting Wealth).

The growing role of the emerging economies in the global landscape is also having significant implications on global and regional trade and finance, the nature and direction of capital flows, and global governance in the areas of finance and economics.

In the global economy, Asia is leading the recovery process today, and is expected to remain as the world's fastest growing region over this decade. The region is expected to generate one third of world output by 2015 (IMF: World Economic Outlook September 2011). The rapid transformation of the region over this decade will contribute to increasing its financial and economic potential.

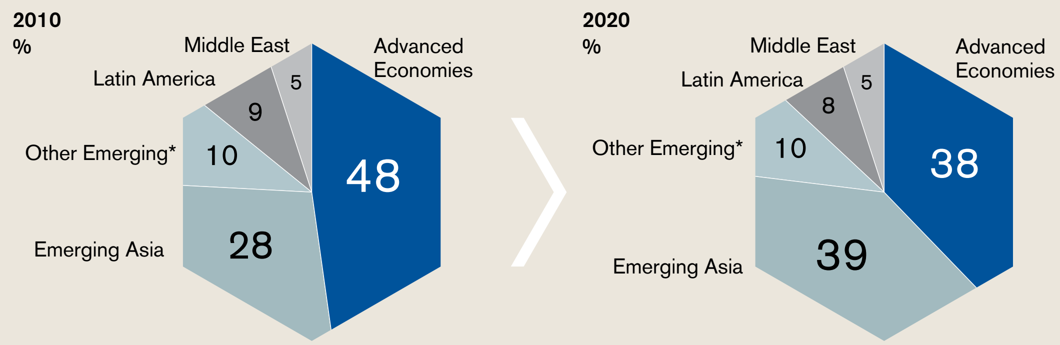
Two key structural trends are already unfolding. First is the strengthening of domestic sources of growth, led mainly by the private sector. The global middle class is expected to increase to 3.2 billion people by 2020 from 1.8 billion in 2009, and Asia is expected to contribute 85% of this increase to become the home to more than 50% of the global middle class. This imminent rise of a sizeable and increasingly more affluent middle class population will not only

The growing role of the emerging economies in the global landscape is having significant implications on global and regional trade and finance, and global governance

support greater domestic consumption in the region, but the region's large cumulative market will also make Asia an increasingly important global consumer. The rising final demand in Asia will also accelerate regional economic integration in Asia. The intensification of economic integration will allow the region to further optimise the complementarities arising from its diversity and the different comparative advantages that exist in the region. The international linkages with the other emerging economies and traditional growth centres across the world are also expected to strengthen.

The concurrent rise of the emerging economies is fundamentally changing the global landscape

Evolution in the share of the global economy



Factors contributing to the growth of the emerging economies

A Large & growing middle class	Emerging economies to add 125 million people into the global middle class annually, doubling the global middle class population to 3.2 billion by 2020
B Young population with higher propensity to consume	Emerging economies to contribute to more than half of global consumption by 2020, with Asia alone accounting for more than 40% of global consumption
C Greater regional integration	Higher trade & investment within and across the various regions of emerging economies will further strengthen regional economic & financial integration

* Includes Sub-Saharan Africa, Central & Eastern Europe and the Commonwealth of Independent States
Source: International Monetary Fund (IMF), Organisation for Economic Co-operation and Development (OECD) and Bank Negara Malaysia estimates

The second trend is the strengthening of financial linkages in the region. Asia, as a region with a high savings rate and rising investment requirements for capacity expansion and in infrastructure development, would benefit from more effective and efficient intermediation of Asia's sizeable surplus funds towards the vast investment opportunities in the region. The gains from greater financial integration will be far-reaching – it will not only enhance growth, but also act as a catalyst for deeper regional economic integration.

Within Asia, the Association of Southeast Asian Nations (ASEAN) region is in a strategic position to leverage on the increasing opportunities emanating from the Asia-Pacific region. The integration of ASEAN as a single market will enhance the region's growth and dynamism. The sizeable population of about 600 million people in ASEAN presents a large and fast-expanding market. The region's focus on greater financial integration will further enhance regional economic growth and promote greater financial stability. Initiatives are already underway to strengthen financial integration within the broader Asian region.

Meanwhile, the ongoing international financial regulatory reforms will also redefine the global financial landscape, with broader implications for competition, innovation and overall economic activity. A clear consensus has been reached in several areas, including the need for more responsive regulatory frameworks to risks, the strengthening of risk management capabilities in financial institutions, and enhancing supervisory oversight of financial institutions. However, there remains substantial debate in other areas, such as on the degree of balance of regulation and the design of institutional frameworks for financial stability. Whilst the degree of consensus on the spectrum of recommended reforms has been mixed, the end goal of greater financial stability in the region remains a shared vision.

Another key development is the greater role and relevance of Islamic finance in contributing to global financial stability and in supporting overall global economic growth. The internationalisation of Islamic finance can be expected to significantly increase following the strengthening of Islamic finance as a viable and competitive component of the international

Financial regulatory changes

More extensive & intrusive regulation
- Capital, liquidity, incentive system, governance, consumer, accounting
- Enhanced scope of regulation for systemic institutions

Strengthened institutional arrangements
- To avoid gaps and clarify accountability
- More formalised arrangements for coordination & cooperation

International financial architecture
- Reforms of international institutions to reflect enhanced role, broader representation and diversity

Implications:

1. ↓ **Expected return on equity**
   - ↑ Capital requirements and other regulation-imposed costs
   - ↓ Real economic returns
   - ↓ Growth due to lower leverage
2. ↑ **Cost of intermediation**
3. ↑ **Financial stability**
   - ↑ Macroprudential stability
   - ↑ Confidence
   - ↑ Efficient markets

financial system in the recent decade. The strengthening of trade and investment ties between Asia and the Middle East has also prompted greater financial linkages in the more recent period. This will also serve to further reinforce the rising importance and prominence of Islamic finance. Given the more challenging international environment, emphasis will increasingly be placed on enhancing the resilience of Islamic finance, including in liquidity and crisis management, to complement the ongoing efforts in strengthening the relevant regulatory and legal framework for Islamic finance and in promoting greater harmonisation in Shariah interpretations.

The rapid and simultaneous rise of numerous growth centres, especially with several large emerging economies, will intensify global competition for investment and human capital. The flow of capital across economies and regions will also increase in magnitude and frequency, with heightened volatilities in financial markets, asset prices and financial risks amidst an increasingly inter-connected world. These trends will require greater global and regional coordination and cooperation, in particular to manage systemic cross-border contagion risks which can be expected to increase. Strengthened collaboration will be key in managing the heightened cross-border risks arising from greater financial inter-connectedness across countries and regions. It is within this more challenging global environment that the emerging economies, including Asia, will need to fundamentally strengthen domestic demand and meaningfully enhance productivity, in order to sustain their continued growth and development over the next ten years.

The Malaysian Economy over the Next Ten Years

Against this rapidly changing global landscape, Malaysia aspires to transform into a developed and more competitive economy by 2020. This transformation will rely largely on the private sector to drive greater productivity and innovation to move up to higher value-added activities that will underpin and sustain strong economic growth. The Government's commitment to comprehensive long-term structural reforms will provide the enabling environment for the economic transformation to succeed. The target is to double income per capita to RM48,000 (approximately equivalent to USD16,000) by 2020. An equally important consideration is that the growth and development will be more inclusive and sustainable.

Malaysia's economic transformation will rely largely on the private sector to drive greater productivity and innovation to move to higher value-added activities

Characteristics of Malaysia as a high value-added, high-income economy

Malaysia in 2020

1. **Demography**
   More mature and urbanised population

Greater balance of domestic & external demand

2. **Consumption**
   Higher consumption with rising incomes and a larger middle class
3. **Investment**
   Higher and enhanced quality of private investment

High value-added activity across all sectors

4. **Manufacturing**
   More innovation-driven industries
5. **Services**
   Growth of knowledge-driven sub-sectors
6. **Government**
   Efficient facilitator of growth
7. **Infrastructure**
   Extensive & efficient infrastructures
8. **Innovation**
   Strong technological & innovation culture
9. **Competition**
   Competitive & efficient private sector-driven markets
10. **International integration**
    International & regional linkages extend from trade to financial and talent flows

1. Knowledge- and innovation-intensive economic activity

The transformation of the economy will be characterised by economic sectors moving to higher value-added economic activities, where knowledge, innovation and productivity are central to value creation. For Malaysia, given the existing strong manufacturing and services base, movement towards higher value-added activity will be driven by the existing and new industries migrating up the value chain, such as in the areas of advanced electronics as well as green and resource-based industries. This will be strongly complemented by the development of knowledge-intensive services, including computing, information and communication technology (ICT), research and development (R&D), health and education, as well as manufacturing-related support services such as logistics, marketing and branding. Of significance, while multinational and large domestic corporations will remain important, small and medium enterprises (SMEs) will be central to the economy. A broad base of highly dynamic, innovative and competitive SMEs will be a critical and prominent feature of a high value-added, high-income Malaysian economy.

Economic activities will be increasingly driven by knowledge & innovation

Movement to higher value-added activities across all economic sectors
Value creation will be underpinned by knowledge, innovation & productivity improvements

Manufacturing
High value-added, innovation-driven industries
- Existing and new industries to increasingly move up the value chain, such as in advanced electronics and downstream resource-based activities
- Greater sophistication and specialisation as firms compete using niche strategies

Services
Growth of knowledge-driven services
- Growth of knowledge-intensive services, such as computing & ICT, R&D, health and education
- Manufacturing-related support services to provide strong support for industrial growth, including logistics, marketing and branding

Strong base of dynamic, innovative & competitive SMEs
A large base of competitive and innovative SMEs will be central to the economy, providing critical support to the large domestic and multinational corporations

Towards achieving this, the Government has launched comprehensive initiatives to facilitate the growth of key economic sectors. In particular, under the Economic Transformation Programme (ETP), strong emphasis is being placed on several key growth engines: namely, the 12 National Key Economic Areas (NKEAs). These NKEAs are expected to contribute substantially to Malaysia's economic performance, complemented by the prioritisation of public investment and policy support towards these activities. It is envisaged that these NKEAs will generate RM1.4 trillion (approximately equivalent to USD466 billion) of investment activities over the next ten years. 92% of the investment is expected to be undertaken by the private sector and 32% contributed by Government-linked companies.

2. Competition-driven private sector-led economy

Malaysia's transition towards a high value-added, high-income economy will be led by the private sector in an increasingly more competitive environment. Competition will contribute to a more efficient allocation of resources and the creation of greater economic vibrancy and dynamism. For markets to function effectively and efficiently, the removal of market distortions, particularly those that affect price signals, is a necessary precondition. Such market distortions include broad-based producer and consumer subsidies and restrictive regulatory constraints. Also important is the further strengthening of institutional arrangements to address and minimise the potential risks of market failure and to promote a more competitive and fair business environment.

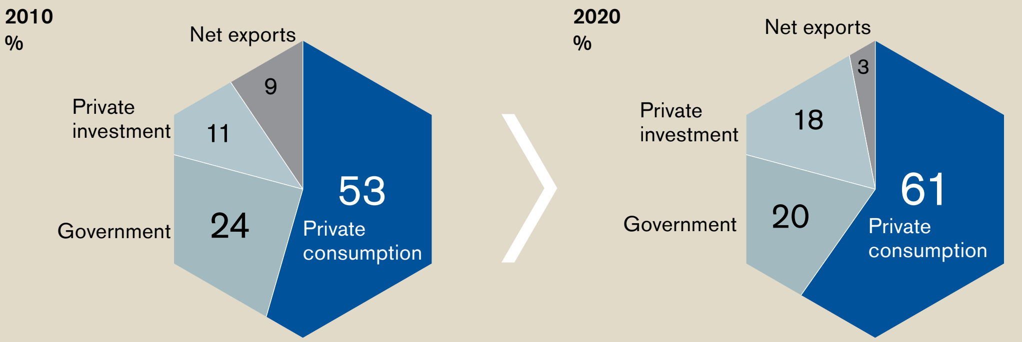
As the private sector takes the lead, the role of the Government will shift to that of a facilitator of growth. The focus of the Government will be on providing the necessary preconditions and on continuously nurturing a competitive environment for the efficient functioning of the market that will generate the appropriate incentives for private sector initiatives. This will primarily involve the investments into human capital, good governance and the creation of other enabling institutional arrangements and infrastructures.

3. Greater balance between domestic and external demand

Consistent with the trend since the Asian financial crisis, the sources of growth in the Malaysian economy will increasingly be more balanced, with growth driven by both the external and domestic sectors. Whilst Malaysia's competitive advantage in the external sector will remain key, the domestic sector will assume a greater role in contributing to overall growth. First, a larger and more affluent middle income population will support higher and more broad-based private consumption. It is estimated that approximately a quarter of the more mature population will belong to the middle income group in 2020 (2007: 19%). The middle 60% of the population (20th to 80th percentile) is projected to earn a higher real annual income (after adjusting for inflation) of RM36,000 (2007: RM20,400). This is expected to provide key support to the continued growth in private consumption over this decade, raising the share of private consumption to about 60% of GDP by the year 2020 (2010: 53%). Second, an increase in the quality of private investment will contribute to a more sustainable growth of high value-added, high-income employment. Private investment will increasingly shift towards advanced automation and R&D to facilitate the movement up the value chain and support innovation. The share of private investment to GDP is projected to rise to about 18% by the year 2020 (2010: 11%), with the increased contribution anchored by domestic direct investment and supported by continued inflows of foreign direct investment.

Greater balance between domestic and external demand as sources of economic growth, driven by higher private domestic demand

Evolution in the share of the Malaysian economy*



A. Higher private consumption, supported by rising incomes and a larger & richer middle income population

- Share of private consumption to increase to about 60% of GDP by 2020 (2010: 53%)
- Approximately a quarter of the population will belong to the middle-income group in 2020 (2007: 19%)
- 60% of the population to earn a higher real annual income (after adjusting for inflation) of RM36,000 in 2020 (2007: RM20,400)
- Improvements in income distribution

Demographic profile in 2020

- Lower population growth of 1.5% in 2011-2020 (2000-2010: 2.1%)
- Higher median age of 30 years (2010: 26 years)
- Longer life expectancy of 76 years (2010: 74 years)
- Larger mature population, with lower support ratio of ten people (2010: 14 people)
- Increase in rate of urbanisation to 79% (2010: 72%)

% of population	2010	2015	2020
Age 0-14	29.1	27.2	25.3
Age 15-64	66.1	67.0	67.6
Age > 65	4.8	5.8	7.1
Total population	28 mil	30 mil	32 mil

B. Higher & enhanced quality of private investment that will transition towards higher value-added economic activities

- Share of private investment to rise to about 18% of GDP by 2020 (2010: 11%)
- More investments from stronger & innovative SMEs
- More investments in areas such as R&D, ICT, automation and energy efficiency

Background: ETP

- 12 NKEAs to generate RM1.4 trillion (approximately equivalent to USD466 billion) of investment activities in 2011-2020
- 92% of investments expected to be undertaken by the private sector, requiring about RM120 billion of investment annually
- 32% of investments to be contributed by Government-linked companies
- Domestic direct investment to account for 73% of total private investment, with 27% from foreign direct investment

Source: Department of Statistics Malaysia (DOSM), Economic Planning Unit (EPU), National Economic Advisory Council (NEAC), Performance Management and Delivery Unit (PEMANDU), World Bank, International Labour Organisation (ILO) and Bank Negara Malaysia estimates

* Figures exclude change in stocks & do not sum to 100%

4. Greater global and regional economic integration

Given that the domestic market in Malaysia is relatively small, the growth of firms – in terms of both size and strength – will increasingly depend on their ability to integrate with the region and the rest of the world for greater access to larger markets. For Malaysia, further integration with the region and the broader global economy will be a key characteristic of the transition towards becoming a high value-added, high-income economy. In particular, the recent rising trend of investment abroad by Malaysian companies can be expected to continue. Over the medium term, this will bring increased benefits in terms of new opportunities and markets. Indeed, Malaysia is expected to have an increasingly important role in intensifying regional economic integration within Asia and across other emerging economies.

The Malaysian economy is currently positioned at an important juncture of its development, and the progress forward can be expected to be confronted with many challenges. Throughout Malaysia's development across the span of more than 50 years, the economy has demonstrated the ability and flexibility to continually evolve into new areas of comparative advantage and growth. Going forward, with the prevailing sound economic fundamentals and resilient financial sector, Malaysia is well positioned with the necessary foundations to take advantage of the emerging opportunities from the rapidly changing regional and global trends. The financial sector in this Blueprint is envisaged to not only make progress in tandem with developments shaping the economy, but also to have a greater role in facilitating and catalysing the transformation of Malaysia into a high value-added, high-income economy by 2020.

1.2

evolution of the Malaysian financial sector

The transformation of the Malaysian financial sector over this recent decade provides an important platform that will support the future growth and development of the financial services industry. Much of the transformation has been guided by the implementation of the Financial Sector Masterplan (FSMP), introduced in 2001.

The FSMP outlined a 10-year plan for the orderly development of the financial sector, beginning with building the institutional capacity of the domestic intermediaries and developing the domestic financial infrastructure. This was followed by the introduction of an increasingly competitive environment as the financial sector shifted to become more deregulated and market oriented. This culminated in greater liberalisation and international integration. To date, all of the FSMP recommendations have been implemented or are being implemented on an ongoing basis.

The robust and resilient state of the Malaysian financial system today, with its enhanced strength and stability has enabled the financial system to effectively and efficiently perform its intermediation function even amid the challenging conditions during the global financial crisis. It has also reinforced its role as a key contributor of growth in the Malaysian economy. Since 2001, the financial sector has expanded at an average annual rate of 7.3%, to account for 11.7% of real GDP in 2010 (2001: 9.7%).

The development of the Malaysian financial sector has not only provided support to the changing requirements of the Malaysian economy and significantly strengthened Malaysia's foundations for financial stability, but has also better positioned the financial sector to withstand the effects during destabilising episodes of increased volatility and stress in global financial markets. The focus of reforms has been accorded to three key efforts:

Evolution of the Malaysian financial sector

1997 → **2010**

Pre-Asian Financial Crisis

- Fragmented banking system with 77 domestic banking institutions
- Less developed bond market
- Over-reliance by corporations on the banking system for financing
- More rigid & prescriptive rules-based regulation & supervision
- Limited prominence of Islamic finance
- Rigid price mechanisms
- Gaps in access to financing

FSMP

Key Achievements

- Consolidation & rationalisation of the banking industry
- Diversified financial sector with a deep & liquid debt securities market
- Strengthened corporate governance & risk management practices
- Strategic alliances with foreign institutions
- Efficient delivery channels for financial products & services
- Robust surveillance, regulatory & supervisory framework
- Comprehensive consumer protection framework
- Malaysia as an international Islamic financial hub
- Enhanced access to financing especially for SMEs & micro-enterprises
- Greater market orientation
- Strengthened financial & economic linkages

1. Strengthening the resilience of financial institutions

Domestic financial institutions in Malaysia underwent restructuring, consolidation and rationalisation. Having greater scale, there was increased investment in technology and talent. The institutions have now accumulated strong capital and loan loss buffers, with improvements in underwriting and risk management practices, as well as strengthened governance structures and discipline. The institutional development and capacity building initiatives have generated highly competitive domestic financial intermediaries.

Improved performance indicators

Commercial Banks	Domestic 2000	Domestic 2010	Foreign 2000	Foreign 2010
Capitalisation				
RWCR (%)	11.7	14.2	14.0	14.6
Asset Quality				
Net NPL Ratio (%)	9.2	2.6	5.7	1.2
Profitability				
ROA (%)	1.1	1.6	2.1	1.6
ROE (%)	13.3	16.7	26.4	19.6

To date, all of the FSMP recommendations have been implemented or are being implemented on an ongoing basis

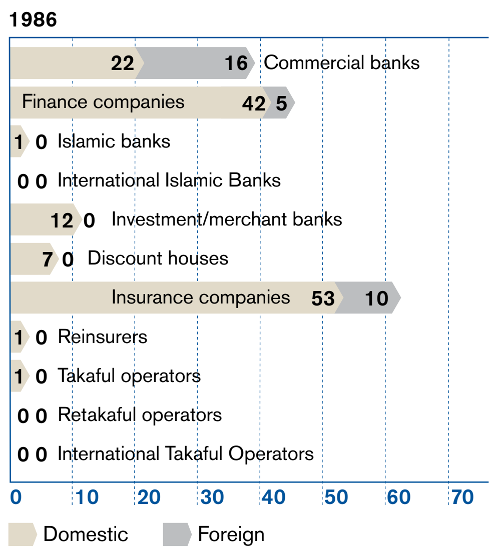
Structure of the Malaysian financial system has evolved to become less fragmented through consolidation & rationalisation

1980s — 1990s — 2011

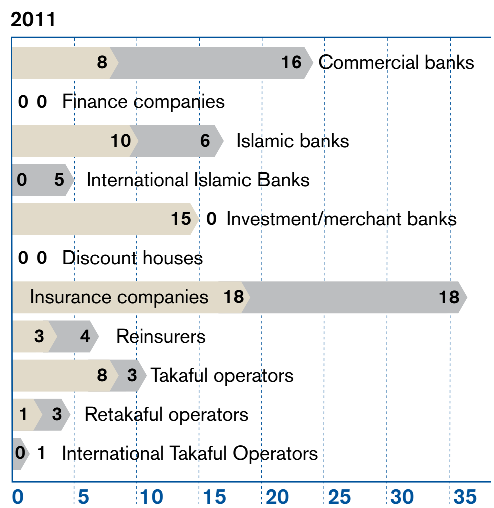
77 domestic banking institutions
55 domestic insurance companies

34 domestic banking institutions
37 domestic insurance companies

Number of financial institutions in Malaysia



Number of financial institutions in Malaysia



2. Establishing the domestic financial infrastructure

The establishment of key financial market infrastructure, including the development of the domestic debt securities market and robust payment and settlement systems, has been vital in the development and functioning of the intermediation function of the financial system. During this period, the new interest rate framework was introduced, resulting in a more market-oriented financial system; and foreign exchange administration rules were liberalised, creating the preconditions to move to a flexible exchange rate regime. Several steps were taken during this period to develop the debt securities market, which has now become a vibrant market both for raising financing and for investments. These initiatives include developing the market infrastructure, including enhancing the clearing and settlement mechanism; ensuring availability of timely market information; publishing the auction calendar and the indicative yield to maturity of both public and private debt issuances; enhancing the mortgage corporation, Cagamas; and establishing a credit enhancement agency, Danajamin. The functioning of the market was also elevated with a more conducive environment to facilitate transactions, including greater hedging mechanisms,

Development of the debt securities market has contributed towards more diversified sources of long-term financing and has positioned Malaysia's debt securities market as the largest in Southeast Asia

an enhanced regulatory framework and increasing liberalisation of foreign exchange policies for non-resident participation in the market. The development of the domestic debt securities market has since contributed significantly towards financial stability by dispersing the concentration of risk in the financial system through diversifying the sources of financing in the country and enhancing the intermediation of investment and capital flows. The size of the debt securities market has expanded significantly from an outstanding value of RM306.8 billion in 2001 to RM867 billion or 105% of GDP in 2011. This has positioned Malaysia's debt securities market as the largest in Southeast Asia. The vibrancy of the market is marked by the proliferation of new types of instruments with varying tenures and a wide group of issuers and investors including foreign corporations.

Other institutions established include the Malaysia Deposit Insurance Corporation (PIDM) as a vital infrastructure in the Malaysian financial system, and the Cooperative Commission Malaysia to provide oversight to the credit cooperatives.

The Bank has further strengthened its financial stability framework and governance arrangements in the management of financial stability

3. Enhancing Bank Negara Malaysia's financial stability framework

The Bank has further strengthened its financial stability framework and governance arrangements in the management of financial stability over the 10-year period. The regulation and supervision of financial institutions during this decade has become more risk-focused and pre-emptive to reflect the nature, size and complexity of different institutions. This has been accompanied by a significantly more pronounced focus for the effective oversight of financial institutions by boards and senior management. The management of system-wide risks to financial stability has also been strengthened, with improved data and information, enhanced tools and methodologies, closer inter-agency and regional cooperation, and expanded financial stability powers. Within the Bank, clear accountability and decision-making structures, including the Financial Stability Committee have also been put in place since 2004. Particular focus has been given to improving the rigour of stress tests performed by the supervisors and financial institutions. This has ensured that the financial institutions build and maintain sufficient financial buffers in good times that can be drawn on under conditions of stress. As a result, confidence in the financial system has strengthened and continues to be preserved.

Throughout this recent decade, the sustained soundness and efficient functioning of the Malaysian financial system has contributed towards meeting the increasing and differentiated demands of the economy. Continued credit flows to Malaysian households and businesses have been accompanied by enhanced access to a wider spectrum of financial products, services and delivery channels, improved customer service quality, and more pervasive use of technology. In particular, the growth and development of small and medium enterprises (SMEs), a key engine of growth in the Malaysian economy, continues to draw strong support from the financial sector in meeting their financial demands. The improved environment for SME financing followed the development of a comprehensive institutional framework, enhanced loan approval and disbursement processes, and provision of advisory services and redress mechanisms.

The Bank's financial sector development policies have also taken into account the need to achieve balanced growth by according attention to financial inclusion. This commitment to financial inclusion is now embedded in the Central Bank of Malaysia Act 2009, which specifies as one of the functions of the Bank, the promotion of a sound, progressive and inclusive financial system. The Bank's financial inclusion agenda has achieved significant advancements in extending financial access to all segments of the Malaysian population, with the improved outreach of financial services nationwide, particularly in remote and non-urban locations. The development of the *Pembiayaan Mikro* framework, and the availability of basic banking services that empower consumers through financial information, education and assistance have continued to yield positive results. A comprehensive consumer education and protection framework is now in place, reinforced by assistance platforms such as the Credit Counselling and Debt Management Agency (AKPK), Financial Mediation Bureau, and the Bank's Integrated Contact Centre. The financial services industry also provides advisory services to promote well-informed and responsible financial decisions for consumers and businesses.

Given that the quality and productivity of the workforce represents an essential element in the development of a modern and dynamic financial system, wide-ranging initiatives in human capital development and talent have also been implemented during this period. The comprehensive education and learning programmes introduced have resulted in the establishment of differentiated platforms to meet the diverse needs of financial services professionals at varying stages

Spearheading initiatives for talent development

1960

2001

2003 **International Centre for Leadership in Finance (ICLIF)**
Training for senior management in strategic & leadership management

2006 **International Centre for Education in Islamic Finance (INCEIF)**
Build talent & skills in Islamic finance

2007 **Financial Sector Talent Enrichment Programme (FSTEP)**
Training for top graduates to provide foundation in the financial services industry

2008 **Financial Institutions Directors' Education Programme (FIDE)**
Promote high impact boards in financial institutions in corporate governance, risk management and strategic issues

International Shariah Research Academy for Islamic Finance (ISRA)
Promote applied research in Shariah & Islamic finance

2010 **ICLIF Leadership & Governance Centre**
FIDE Programme fully managed and delivered by ICLIF

1968

Malaysian Insurance Institute (MII)
Provides education and training programmes for professionals in the insurance and insurance-related industries

1977

The Institute of Bankers Malaysia (IBBM)
The key enabler of transfer of knowledge and skills for banking and finance professionals

2008

Asian Institute of Finance (AIF)
Coordinated & collaborative approach towards human capital development

2001

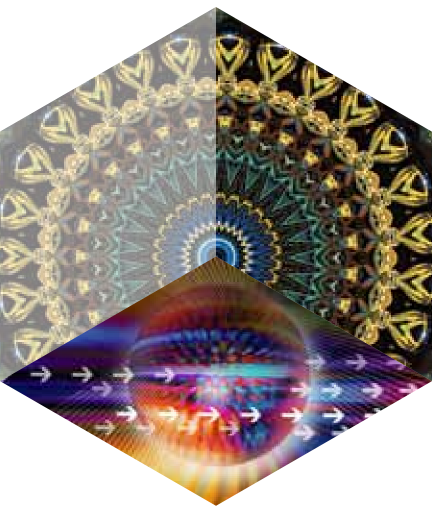
Islamic Banking & Finance Institute Malaysia (IBFIM)
One-stop Islamic finance reference centre for the industry & academia

Securities Industry Development Corporation (SIDC)
The leading capital markets education, training and information resource provider in ASEAN

The Bank has undertaken wide-ranging initiatives in human capital development and talent enrichment

of their career. These include the Financial Sector Talent Enrichment Programme (FSTEP) for entry-level graduates, the Asian Institute of Finance (AIF) for continuous training and skills development of professionals in the banking, insurance, securities and Islamic financial services industries, and the ICLIF Leadership and Governance Centre for senior management and board of directors of financial institutions. In the field of Islamic finance, its development is further supported by the International Centre for Education in Islamic Finance (INCEIF), Malaysia's global university of Islamic finance, and the International Shariah Research Academy for Islamic Finance (ISRA), which promotes applied research in Shariah and Islamic finance.

The commitment to the gradual and progressive liberalisation of the financial sector over the years has enhanced Malaysia's international linkages with the global economy. The Malaysian financial sector now has a sizeable presence of global players, accounting for approximately 20% market share of the banking sector, and two-thirds market share in the insurance and takaful sector. This has facilitated international trade and investment flows, supported the development of new economic growth areas, created employment opportunities for Malaysians, and contributed to the growth and diversified nature of the financial system. It has also facilitated the transfer of expertise and technology, and cultivated a more competitive environment, providing the impetus for enhancing efficiency, driving product innovation, and improving customer service quality, to the benefit of all Malaysians.



Stronger global presence of domestic banking groups

Overseas Contribution	2002	2010
Total Assets	RM3.3 bil	RM240.2 bil
Pre-tax Profit	(RM108.9 mil)	RM2.3 bil

With stronger foundations, Malaysian financial institutions have also actively participated in business opportunities in the regional markets. In the more recent years, Malaysian financial institutions have actively pursued initiatives, including the establishment of financial conglomerates, investment banks, insurance and reinsurance companies, and takaful operators, to enlarge their regional footprint through the acquisition or the establishment of subsidiaries, branches, or joint ventures as part of longer-term growth strategies to diversify their sources of income and tap the region's growth prospects. Malaysian financial institutions have now successfully emerged as leading regional players with an important role in contributing to the overall economic development of the region. In parallel with these developments, the Bank has also been proactive in the development of strong regional frameworks for cooperation in the areas of surveillance, supervision, policy, and crisis prevention and management.

In the area of Islamic finance, this recent decade has witnessed significant strides in its development. The Islamic banking industry has expanded from 6% to 22% of the overall banking sector while the sukuk market now accounts for 55% of the debt securities market. With increased liberalisation of the Islamic financial system, Malaysia has now also emerged as a leading international hub for Islamic finance. With the world's largest sukuk market, and as a leading centre for Islamic equity, Islamic fund management, Islamic banking and takaful, Malaysia is home to most of the key international financial groups that offer Islamic financial products and services. Malaysia has also focused on promoting global dialogue to facilitate international convergence of Shariah rulings and standards. In addition, Malaysia has participated actively in the formation of international institutions, namely the Islamic Financial

Labuan IBFC has seen steady expansion in terms of the number of players, diverse financial product offering and volume of activity

Services Board (IFSB) and the International Islamic Liquidity Management Corporation (IILM) as part of the internationally collative efforts to promote financial stability in the Islamic financial system.

Also an important part of the Malaysian financial system is the financial centre in Labuan, which has been transformed into an International Business and Financial Centre (IBFC). Over the recent decade, the Labuan IBFC has seen steady expansion in terms of the number of players, the diverse financial product offering and the volume of activity. As at end-2010, Labuan IBFC has more than 8,000 companies and 400 international financial institutions, including the top international banks and reinsurance companies that originate from more than 100 countries.

In the area of Islamic finance, the development of key sectors such as retakaful and Islamic structured finance has been strengthened with the enactment of the Labuan Islamic Services and Securities Act 2010. In providing the full range of financial services, Labuan offers total financial solutions, both in conventional and Islamic finance. This includes the introduction of new financial products and services such as Labuan foundations, limited liability partnerships, protected cell companies and shipping operations, thus providing investors with greater choices to maximise their investment potential. Labuan IBFC's international competitiveness has also been complemented with modern communication links, and the business and education amenities to support Labuan's aspiration as an international business and financial centre. In 2007, the Labuan International Airport was enhanced further and an open sky policy has been adopted to facilitate greater access to the island. Improvements have also been made to the deep harbour facilities.

A key success factor to the sustained growth of Labuan IBFC is a robust regulatory framework that safeguards stability and integrity which are crucial for an international business and financial centre. In this regard, the regulatory and supervisory approach of the Labuan Financial Services Authority (Labuan FSA) has evolved over the years in line with the changing business environment. From the outset, Labuan FSA has implemented an entry policy that is catered to the establishment of strong and sound financial institutions and trust companies, as well as for capital market activities. Labuan IBFC's regulatory framework has been duly recognised by its categorisation as a low-risk jurisdiction for money laundering by the Asia/Pacific Group on Money Laundering. To further enhance the regulatory and supervisory regime, a new legislative framework was introduced and this has raised the supervisory standards in line with international regulatory practices. These encompassed areas such as registration and revocation of licences, director statutory duties and obligations, audit and accounts requirements, supervisory enforcement powers, and provisions that allow for effective sharing of information between supervisors.
The Labuan IBFC complements the domestic financial system in Malaysia as Malaysia increases its international economic and financial integration with the global economy and international financial system.

1.3

vision for the financial sector

Building on the progress achieved in this recent decade and the current position of strength, the financial sector is today well positioned to advance into its next phase of development and to take advantage of the opportunities of a more competitive and integrated environment, while serving the more varied and complex needs of the domestic economy. As the country transitions towards a high value-added, high-income economy and becomes regionally and internationally more integrated, the financial sector will need to enhance its role in increasing the potential capacity of the economy to grow and become more developed.

Broad characteristics of a financial sector that best serves Malaysia moving forward

Necessary characteristics for a well-functioning financial sector	
Robust	Robust surveillance, regulatory & supervisory framework
Stable	Strong corporate governance & risk management practices
Sound	Comprehensive crisis management framework and ability to withstand systemic shocks

Requisite characteristics for a financial sector that best serves Malaysia	
Competitive	Optimal allocation of resources in line with economic needs Enhanced financial sector productivity & efficiency
Dynamic	Innovative products, services & delivery channels Pervasive adoption of new technology in business operations
Inclusive	Meets financial needs across all segments of society Fair & equitable practices with empowered & educated consumers
Diversified	Wide range of intermediaries & markets Wide range of instruments Wide range of investors
Integrated	Financial institutions with extensive regional presence & global outreach Engaged in significant volume of cross-border activity

The transition towards a high value-added, high-income economy will demand the development of a wider spectrum of financial products and services to support the functioning of the economy and its transformation. It will place increasing emphasis on innovation-driven economic activities that will support new areas of growth and drive new areas of competitive advantage. It is also anticipated that a significant number of new frontier industries will be spearheaded by innovative small and medium enterprises (SMEs). This will however require financial solutions that support the start-up of such businesses. To facilitate this, a more diversified, vibrant and sustainable funding ecosystem that can catalyse growth of higher value-added economic activities will be essential. This will require a vibrant risk capital ecosystem and greater business financing avenues beyond traditional bank financing.

The private sector, envisioned to be the key driver of the country's economic growth, will need the requisite investment financing and financial products and services to grow the broad range of industries and service-related activities. To effectively engage and optimise private sector participation, of paramount importance is the efficient intermediation of funds from surplus to deficit agents through a complete range of intermediaries, markets and instruments. There will also need to be the provision of large and long-term project financing for the infrastructure

Key roles of the Malaysian financial sector

Enabler

Facilitate the transformation of Malaysia into a high value-added, high-income economy

Businesses

- Financing new areas of growth
- Financing innovation & entrepreneurship
- Financing modern infrastructure
- Financing firm internationalisation

Households

- Providing more high-quality & innovative retail financial services
- Providing greater sophistication in wealth management
- Financing retirement & healthcare

Roles of the Financial Sector

Driver

Generate higher contribution to gross domestic product

- As an international financial centre for Islamic finance
- Harnessing revenue from overseas operations
- Diversifying into higher value-added activities

Catalyst

Accelerate growth of supporting & ancillary services sectors

- Growth of new niche sectors

development for a developed economy. This will be critical to increase the potential capacity for economic growth. This will include the development of intermediaries, financial markets and the supporting legal and financial infrastructure to facilitate the matching of long-term savings and investments and to further enhance the public-private partnership framework.

As the country shifts towards a higher-income status, it is envisaged that the financial needs of consumers will become more varied and sophisticated, leading to increased demands for more high-quality and innovative retail financial services. To spur greater innovation and raise the level of financial service quality, greater competition will be encouraged through the progressive liberalisation of delivery channels and a more facilitative regulatory environment. To cater to the rising affluence, the enabling environment for wealth management will be enhanced to support the provision of more comprehensive and sophisticated wealth management financial product offerings.

Changes in the demographic structure will be accompanied by changes in the financial products and services required. As the population becomes more mature, financial solutions for retirement and healthcare will become increasingly important. Efforts will be aimed at developing a more sustainable pension system for retirement that protects

A holistic ecosystem of support and strategic partnerships between domestic and regional financial institutions will be promoted

against old-age poverty, and that will support a sufficient standard of living in retirement. Institutional capacities will need to be enhanced to offer the range of medical and health insurance products and services, including long-term care and other forms of disability insurance, as well as products to encourage individual savings for long-term medical care. This will serve to complement the medical benefits that will be provided to all Malaysians when the proposed national health insurance scheme is implemented by the Government.

A continued agenda in this more dynamic and competitive environment is the sustained emphasis on ensuring that all Malaysians have continued access to high-quality, affordable and essential financial services to facilitate balanced growth. This will entail having in place convenient, effective and efficient access points as well as a comprehensive range of products and services for the underserved. In reaffirming the Bank's commitment that financial services are made available to all segments of society, economic activities and geographical locations in the country, this Blueprint includes a comprehensive set of desired outcomes for the aspirations of the financial inclusion agenda.

Beyond Malaysia's borders, the continued growth and prosperity of the Asian region offers new opportunities for the provision of financial services to facilitate intra-Asian trade and investment flows. This will result in businesses in the region engaging in increased regional trade and investment activities in addition to meeting the needs of the domestic economy. To facilitate this, a holistic ecosystem of support and strategic partnerships between domestic and regional financial institutions will be promoted. In the process, the presence and activities of Malaysian financial institutions abroad is expected to become more significant, while the increasing presence of regional and international financial institutions in our domestic financial system will also further connect Malaysian households and businesses to regional and global trade and investment opportunities. Following from the Financial Sector Masterplan, Malaysia's approach to further liberalisation of the financial sector will continue, accompanied by appropriate prudential safeguards to ensure that the nation's best interests and financial stability are preserved. This includes, among others, ensuring the continued presence of a core group of strong and competitive domestically-owned financial institutions.

The increased regional linkages is not only to meet the new consumer demands arising from a growing middle class population in Asia, but also the significant infrastructure needs of the region, and the growing intra-regional private sector investment activities. Financial intermediaries and markets in Asia will have a key role in intermediating capital flows in the region through increased connectivity and deepening financial integration. Moving forward, efforts will also be directed towards developing the domestic financial markets and to enhance its connectivity to other financial markets in emerging economies in particular. Corresponding to this development is the need for enhancing risk management avenues and instruments to manage risks emanating from cross-border transactions as well as the greater use of regional currencies to reduce transaction costs and risks in regional cross-border trade and investment. Central to this will be the further development of the domestic foreign exchange market to support a wider range of products and services with more active market players. A further enabling element to facilitate transactions in the retail market is the integration of the retail payment systems. This will also enable and facilitate increased intra-regional tourism and labour mobility.

A key pillar of financial sector development for this decade is the strengthening of Malaysia's position as an international Islamic financial centre. Malaysia already has a strong brand affirmed by the growing prominence of a more diverse foreign presence and the higher level of foreign participation in the domestic Islamic financial markets, particularly in the sukuk market. Building from this position of strength, initiatives will be put in place to further accelerate the internationalisation of Islamic finance moving forward, thereby

establishing a more significant role for the financial system in the intermediation of international financial flows. This will involve the introduction of more innovative Islamic financial products and services that will meet the more diverse global demands for Shariah-compliant financial solutions. The enabling environment in Malaysia will also need to continue to be strengthened with a wider range of ancillary services, more efficient delivery channels, adequate supply of high-quality talent and having in place a strong regulatory regime to promote the soundness and stability for the growth and development of Islamic finance.

With a more dynamic and competitive financial sector going forward, the foundations for financial stability will be further strengthened through a more robust regulatory and supervisory regime. The regulation and supervision of the financial sector will take into account the ongoing global regulatory reforms, but contextualised to the evolving financial system that is integral to Malaysia's economic transformation. The overarching objective remains the stability of the overall financial system with priority accorded to further enhancing the resilience of financial institutions through policies that maintain a clear focus on sound risk management practices, supported by sufficient capital and liquidity buffers in times of stress. The scope of the Bank's surveillance and supervisory activities will be further broadened to take into account the greater significance of cross-border operations and new forms of credit intermediation.

As demand for financial services increases in scale and sophistication, the regulatory environment will provide greater flexibility for the participation of strong institutions in the financial sector, while preserving the ability of financial groups to undertake a broad range of financial activities with strengthened prudential safeguards to protect core utility banking services. Financial integrity and consumer protection will also be further emphasised with enhanced arrangements for the investigation of financial crimes, regulation of all consumer credit activities and coordination of financial capability initiatives.

The financial sector also needs to be supported by several key enablers to facilitate its growth and development. This comprises an efficient payment system infrastructure, effective consumer education and protection, and an adequate supply of highly-skilled talent.

For the payment systems, the infrastructure will be enhanced to provide the requisite reliability and efficiency levels while offering convenience to consumers and businesses.

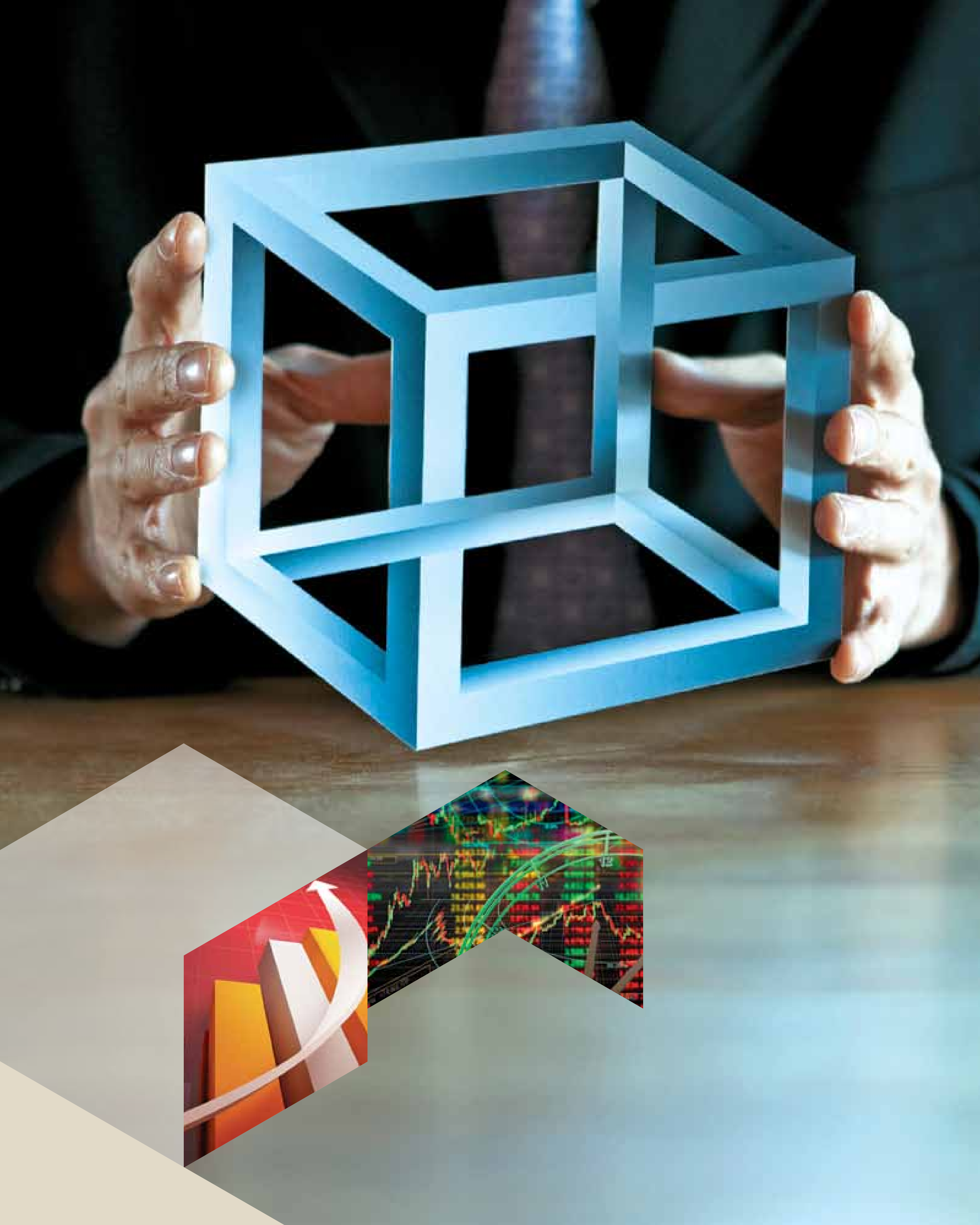
Electronic payments will be promoted as the preferred medium for all economic transactions with the enabling infrastructure and regulatory support put in place to facilitate and encourage greater utilisation. At the same time, intensive efforts will also be undertaken to inculcate greater technology literacy, awareness and confidence to drive the desired payment behaviour during this phase of development of the financial sector.

Underpinning the more competitive and dynamic financial sector is an overall culture of responsibility with financially-educated consumers that are served by financial service providers operating responsibly and with integrity. Towards achieving this objective, a comprehensive approach to consumer protection and education will be put in place. This includes initiatives aimed at ensuring all segments of society have the knowledge and capacity to manage and protect their personal wealth, and the development of a holistic institutional arrangement for financial consumer education and protection.

For consumer protection, the focus will be on building a culture of fair and equitable dealings embedded within the core values of financial service providers and ensuring the availability of effective and efficient mechanisms for dispute resolution for financial products and services.

A further critical success factor to achieve the vision for the financial sector is the supply of highly-skilled talent. The changing demographics consisting of a multi-generational workforce and the increasing international mobility of labour will further intensify the global war for talent. Going forward, the Bank will continue to support and complement industry initiatives aimed at ensuring the supply of a deep pool of highly-skilled talent to drive the financial services sector. Efforts will also be put in place to create an enabling environment that will promote Malaysia as a centre of excellence for financial sector education.

The initiatives in the Blueprint will be implemented progressively over the short to medium term and longer term, with several initiatives being implemented on an ongoing basis. While the implementation timeline is guided by the initiatives outlined in the respective chapters, the overall approach towards implementation will be cohesive and comprehensive. Overall, the initiatives that provide the enabling environment to support the further development of the financial sector, particularly talent development and financial inclusion, will be approached as critical success factors in the strategy for the implementation of the initiatives in the Blueprint. At the same time, initiatives relating to greater liberalisation of the financial sector will be implemented once the required safeguards are in place to ensure the efficient functioning of the financial system and the preservation of financial stability at all times. For the sustainable growth and orderly development of the financial sector, the initiatives in the Blueprint will also be implemented with an effective regulatory and supervisory regime in place that will preserve the stability of the financial system and soundness of individual financial institutions.



1.4

structure of the financial sector in 2020

The recommendations in this Blueprint aim to build a financial sector in 2020 that will benefit a high value-added, high-income Malaysian economy, and generate a growth that is founded on productivity gains and innovation, that is inclusive, balanced and sustainable, while also having an increasingly important role in meeting the growing financial needs of emerging Asia.

It is envisioned that in the next ten years, the Malaysian financial sector will increasingly be intermediating domestic, regional and international financial resources and contributing to the efficient allocation of resources not only in the domestic economy but also across borders.

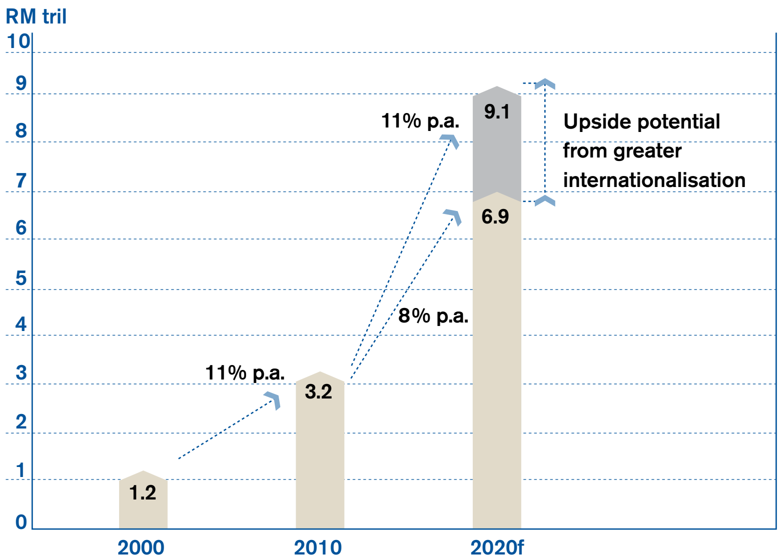
Within this decade, the financial system[1] is expected to grow at an annual rate of 8-11%, increasing the depth[2] of the financial system to six times of gross domestic product (GDP) in 2020 (2010: 4.3 times of GDP). Correspondingly, the financial sector contribution to nominal GDP in 2020 is expected to increase to 10-12% (2010: 8.6%). The contribution of financial institutions is also expected to strengthen, with assets of the banking sector rising to almost three times of GDP[3] by 2020 (2010: 2.4 times of GDP).

[1] The size of the financial system is proxied by the sum of loans outstanding, stock market capitalisation and bonds outstanding.

[2] Financial system depth is the sum of loans outstanding, stock market capitalisation and bonds outstanding, relative to GDP. It reflects the extent of financing activity through financial intermediaries and markets.

[3] This includes assets of overseas operations of Malaysian banks. In advanced economies with large banking systems, bank assets (for domestic operations only) relative to GDP was on average eight times the size of GDP in 2007.

Size of the financial system*



*Proxied by loans outstanding, equity market capitalisation & bonds outstanding
Source: Capital Market Masterplan 2 & Bank Negara Malaysia

Malaysian financial sector envisaged to serve domestic, regional & international needs

International

Evolving into an international Islamic financial hub with strong connectivity, diversity of players & instruments, and specialisation in areas with strong competitive advantage

Asian & Emerging Economies

Stronger financial linkages to facilitate trade & investment and support effective intra-regional intermediation

ASEAN

Integrated ASEAN financial markets driven by the ASEAN Economic Community

Malaysia

Strong, stable, competitive & inclusive financial system that supports effective & efficient intermediation of funds, the development of vibrant financial markets and contributes towards meeting the financing needs of the economy

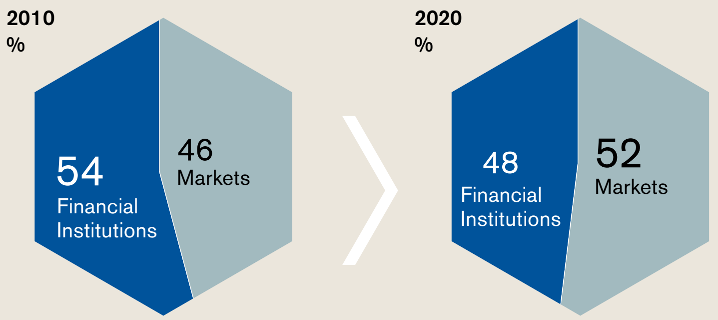
Supported by a robust surveillance, regulatory & supervisory framework and robust cross-border arrangements to ensure preservation of financial stability

The financial sector contribution to nominal GDP is expected to increase to 10-12% in 2020

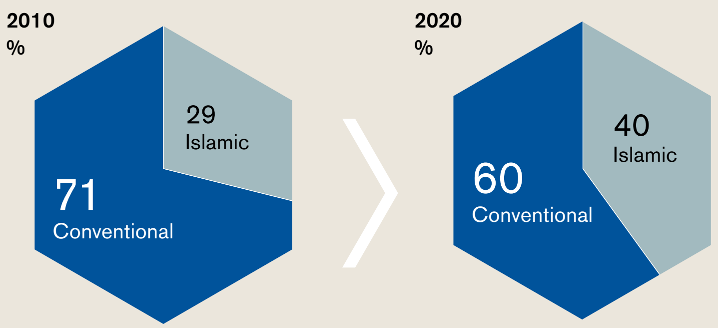
Meeting the Needs of the Malaysian Economy

The sources and uses of funds in the financial sector will evolve to meet the growing and changing needs of the Malaysian economy. In terms of the sources of funds, the traditionally strong bank deposit base will increasingly be complemented by higher direct participation of savers and investors in the financial markets through the growing suite of investment-related savings accounts and products, such as provident and pension funds, insurance and takaful, as well as retail bonds. The broader funding base will allow better matching between financial assets and liabilities, and hence enable financial institutions to further expand their scope beyond debt financing and offer more diverse financing products and services that will better meet the new and differentiated financing needs of the economy.

Financing activity will transition further towards being more market-based



Share of Islamic finance of total domestic financing to grow further



These developments will in turn unlock new potential for the financial system and drive the progression towards a system which is characterised by greater equity participation and more diversified domestic markets that are also regional in terms of participants and offer broader types of instruments, as well as a wider range of maturities. Consequently, this decade will see a shift towards more market-based financing. By 2020, more than half of total financing is expected to be raised through financial markets (2010: 46%). Meanwhile, financing based on Islamic principles would also grow to account for 40% of total financing in 2020 (2010: 29%). It is envisioned that the pace of growth of the domestic Islamic finance industry would be sustained in this decade, underpinned by greater reach and product innovation.

Greater Asian Financial Integration

It is envisioned that Malaysia will be a significant part of the Asian regional financial integration both in terms of the increased presence of Malaysia's intermediaries in the region and Malaysia's participation in regional financial markets. Similarly, greater liberalisation would result in greater foreign presence and participation in Malaysia's financial system. In addition to serving the needs of the Malaysian economy, the financial system will be a long-term growth partner for the ASEAN and Asian region by mobilising funds from regional and global savers and investors, and allocating capital to key centres of economic activity in Asia as regional economic integration deepens and gathers momentum. Focus will, in particular, be given towards channelling funds to productive uses across Asia. Malaysia's strength will lie in being the window for investment in Asia, as a centre for reducing information asymmetries and quantifying risks for Asian-bound investments.

Evolving Malaysia as an International Centre for Islamic Finance

The internationalisation of the Malaysian Islamic financial system will not only contribute to enhancing Malaysia's trade and investment linkages with other emerging economies, especially the Middle East, Asia and Africa, but it will also contribute to intermediating a part of the sizeable savings and investments within these regions, as well as from and to other parts of the world. With a highly developed and comprehensive Islamic financial system, supported by a robust regulatory and supervisory regime and the spectrum of ancillary services, increased liberalisation will intensify this internationalisation process. This will be reinforced by the more developed Islamic financial markets and financial infrastructure.

The Landscape of the Financial System in 2020

The reorientation and expansion of the financial system will alter the landscape of the financial system significantly. While commercial banks performing traditional lending activities will continue to expand and facilitate economic growth, the new landscape will be redefined by the increased importance of existing institutions and the emergence of new financial institutions including those with a greater regional and international focus. Together they will form a complete, competitive and yet mutually complementary and reinforcing financial ecosystem. Correspondingly, the scope of both the conventional and Islamic financial activity will expand at a faster pace. The financial landscape will be characterised by:

- Offerings of a wider range of financial products and services to meet the more advanced and differentiated needs of Malaysian businesses and households.
- Wider access to the formal financial system that enables all members of society to participate in and benefit from economic progress, underpinned by a high degree of financial literacy.
- Enhanced and more meaningful participation by qualified international financial institutions in the domestic financial sector that can contribute towards Malaysia's economic growth and transformation and financial stability.
- Wider operational breadth and scope of institutional investors with the introduction of infrastructure funds, private pension funds and funds of funds, as well as the rejuvenation of the venture capital and private equity industries.
- Insurers and takaful operators having an enhanced role in providing comprehensive protection and investment plans for the entire lifecycle of consumers, as well as offering greater avenues for risk mitigation to reduce the cost of doing business in Malaysia.
- Stronger and more prominent specialised financial institutions such as development financial institutions and cooperatives having a leading role in providing financial services and nurturing the growth of targeted sectors, as well as contributing to financial stability.
- Growth of the domestic debt securities market and Malaysia's role as a centre for debt securities origination and fund-raising activities.
- Liquid and broad range of product offerings in the domestic foreign exchange and money markets.
- The increased presence of Asian banks and the greater regional presence of Malaysian banks. These institutions will catalyse intra-regional trade and investment activities and strengthen Malaysia's linkages within Asia.
- Expanded dimension of Islamic financial activity with greater emphasis on the management of Islamic funds in Malaysia through the advent of Islamic investment banks, fund managers and wealth advisory service providers with global reach and stature.

The financial landscape will be redefined by the increased importance of existing institutions and the emergence of a new range of financial institutions including those with a greater regional and international focus

- Enhanced role of the Labuan International Business and Financial Centre as a premier integrated business and financial centre in key sectors such as oil and gas and shipping, with financial institutions focused on wealth management, captive insurance, reinsurance, and leasing business.

Crucial to the growth of the financial system are institutions that perform a supplementary role to ensure efficient and effective intermediation. The Malaysia Deposit Insurance Corporation (PIDM) and the Central Credit Reference Information System (CCRIS) will continue to be key elements in safeguarding financial stability, while Cagamas Berhad and the Credit Guarantee Corporation Malaysia Berhad would continue to play a role in financial market and economic development. Among the key additions to the landscape to support international Islamic finance are the emergence of a single reference body for Shariah matters, as well as Shariah advisories and consultancies. New entities will also emerge to perform the crucial function of reducing information asymmetries and quantifying of risks associated with new and highly innovative ventures.

Key to supporting the growth and advancement of the financial industry is a steady stream of competent and dynamic talent. It is estimated that the financial sector would need an additional workforce of 56,000 by 2020 (2010: 144,000) to fulfil the talent demands in critical areas such as risk management, wealth management, Islamic finance and investment advisory services. While existing programmes and institutions such as the Asian Institute of Finance, the Institute of Bankers Malaysia, Financial Sector Talent Enrichment Programme and ICLIF Leadership and Governance Centre would continue to provide high-quality training to meet the growing needs of the financial industry, a Financial Sector Talent Council will be established to provide strategic direction for the holistic talent development in the financial sector.

2

The financial sector that best serves the Malaysian economy

innovative

inclusive


SOLUTIONS

2.1

effective intermediation

for a high value-added and high-income economy

The Malaysian financial system's ability to allocate financial resources effectively and efficiently will be crucial to support Malaysia's transformation to become a high value-added, high-income economy. Amid greater regional economic and financial integration, the financial sector will also have a more prominent role in intermediating funds in the region and other emerging economies. A more diversified, efficient, competitive and stable financial system is therefore a necessary precondition for Malaysia's economic transformation.

The financial system must be able to mobilise savings effectively from domestic and cross-border sources, towards meeting the large and diverse financing and investment needs of the domestic economy and across borders, particularly in the Asian region and other emerging economies.

The financial sector today is well positioned to advance and benefit from the opportunities emanating from a more competitive and integrated environment. In the recent decade, the Malaysian financial system has performed its intermediation function without disruption even during the height of the recent global financial crisis. This achievement reflects the resilience of the financial system during periods of increased volatility and turmoil or economic downturn. The significance of the bond market has also increased with a broader spectrum of financial instruments to meet the long-term funding needs of large businesses and projects with long gestation periods. Reliance on the capital market by the Malaysian corporate sector for funding has therefore increased, with the corporate debt securities and sukuk market now accounting for 58.5% of total corporate financing as at end-2010, compared with 46.4% in 2001. In this regard, financing activity for the corporate sector has transitioned towards becoming more market-based from being predominantly bank-based in the early 2000s.

The lending structure of the banking sector has hence evolved from predominantly corporate loans towards more retail-based loans to household consumers, and business loans to small and medium enterprises (SMEs). The share of outstanding loans to the household sector has increased from 34.4% of total outstanding loans as at end-2000 to 55.4% as at end-2010, while SME financing has increased from 31.1% to 38.5% of total outstanding business financing during the same period. The enhanced financing environment for SMEs followed the implementation of a comprehensive set of initiatives to support the financial requirements of SMEs, improve processes and procedures within financial institutions, and facilitate the availability of advisory services, including redress mechanisms, by the industry and other agencies such as those provided by the Bank and SME Corporation Malaysia established in 2009. Overall, the strengthening of risk management processes and corporate governance in the financial industry has enabled financial institutions to perform their intermediation function more prudently and effectively.

Moving forward, a number of key broad economic trends will affect the intermediation function performed by the financial sector:

- Increased diversification in Malaysia's economic structure, where the manufacturing and services sectors will increasingly advance up the value chain towards higher value-added activities. Economic growth will be increasingly driven by knowledge-intensive and more innovative industries, and a larger pool of more advanced SMEs, with improved processes, product innovation and market outreach.
- Development of more advanced and extensive infrastructure in the domestic economy, as well as in the region. In Malaysia alone, an estimated RM1.3 trillion of investments in knowledge-intensive as well as large and long-term infrastructure projects is required under the Economic Transformation Programme over the course of the next ten years. Of significance, 92% of this funding requirement is expected to be sourced from the domestic financial system. Meanwhile, the financing requirements to support the massive infrastructure development needed in the Asia Pacific region are also expected to be sizeable, estimated to be at USD8 trillion over the next decade (Asian Development Bank: Infrastructure for a Seamless Asia – 2010).
- Greater international and regional economic and financial integration will provide new opportunities and markets for the Malaysian corporate and financial sectors.
- Changing demography in Malaysia, with a larger pool of more affluent middle-income consumers, a more mature population, and more financially-savvy consumers.

The financial sector today is well positioned to advance and benefit from the opportunities emanating from a more competitive and integrated environment

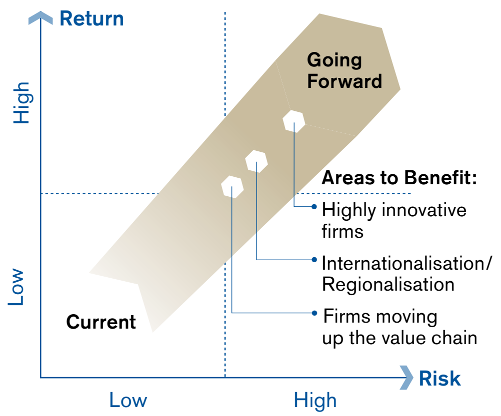
To support a more diverse range of enhanced demands for financial services, the financial sector will need to improve and expand its role to effectively and efficiently mobilise larger volumes of funds from a broad range of sources – from households in the form of traditional retail deposits and insurance premiums, to more sophisticated sources such as pension funds and institutional investors – within Malaysia and also the region. There will therefore need to be more effective matching of sources of funds with the diverse financing needs of the economy. The financial markets are also expected to grow in significance, functioning as an important intermediary for fund-raising and for investors seeking market returns for wealth creation, accumulation and preservation. To respond to these expected trends, financial institutions will need to strengthen their capacity and capability to offer a wider range of financial products and services that can cater for the whole spectrum of risk, liquidity and maturity preferences of borrowers and investors. This trend will gain greater significance as regional financial integration intensifies. The Malaysian financial system, which includes the presence of foreign financial institutions and a more developed financial market, is well positioned to effectively mobilise regional savings to be channeled to regional investment activities. This would also involve the effective and efficient intermediation in multiple currencies. In terms of financing, it is envisaged that commercial banks and development financial institutions (DFIs) will continue to be the main providers of traditional forms of financing to households and SMEs. Investment banks will also be key players in arranging financing and other financial solutions for firms, with a greater focus on large investment activities across borders and in multiple currencies. To support the demands of innovation-driven economic activities and start-up ventures, a vibrant risk capital ecosystem will be required to provide financing avenues beyond traditional bank financing. In tandem with the larger pool of funds mobilised from investment-related products, opportunities exist for financial institutions to expand their scope of financing beyond traditional financing, towards more equity-based and risk capital funding. Towards this end, there will be a greater shift towards a more balanced risk-taking culture among

Widening the risk spectrum of the financial system to support economic transformation

1. Moving Up the Risk-Return Profile

Prerequisites:

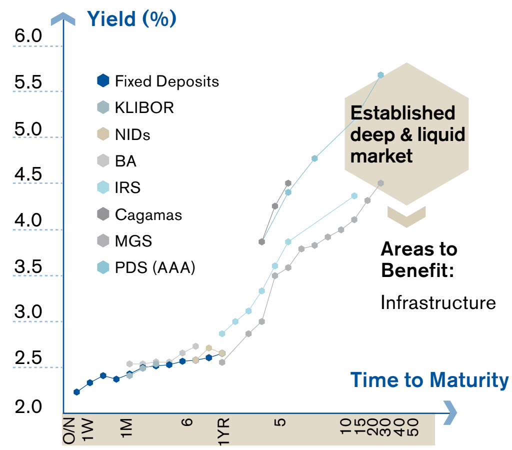
- Effective & transparent flow of information
- Innovative supporting environment: legal & regulatory framework, appropriate culture/mindset and strong governance



2. Lengthening the Maturity Profile

Prerequisites:

- Established benchmark yield curve for pricing, including for long durations
- Deep & liquid markets for long-term securities



Legend			
O/N	Overnight	**M**	Month
W	Week	**YR**	Year

financiers that will facilitate new ventures by entrepreneurs while recognising the possibility of bona fide failures among new start-ups. In support of this development, the enabling infrastructures will be developed to reduce information asymmetries and increase the volume of information flow which is critical to facilitate better credit assessments and to promote the more efficient pricing of risks. Going forward, the financial markets are also expected to have a more meaningful role in financial intermediation, expanding the breadth and depth of financial instruments to facilitate the better matching of long-term savings and investments. This will be complemented by creating an enabling environment to support large-scale financing

To support the demands of innovation-driven economic activities and start-up ventures, a vibrant risk capital ecosystem will be required to provide financing avenues beyond traditional bank financing for projects with long gestation periods, in particular for infrastructure financing.

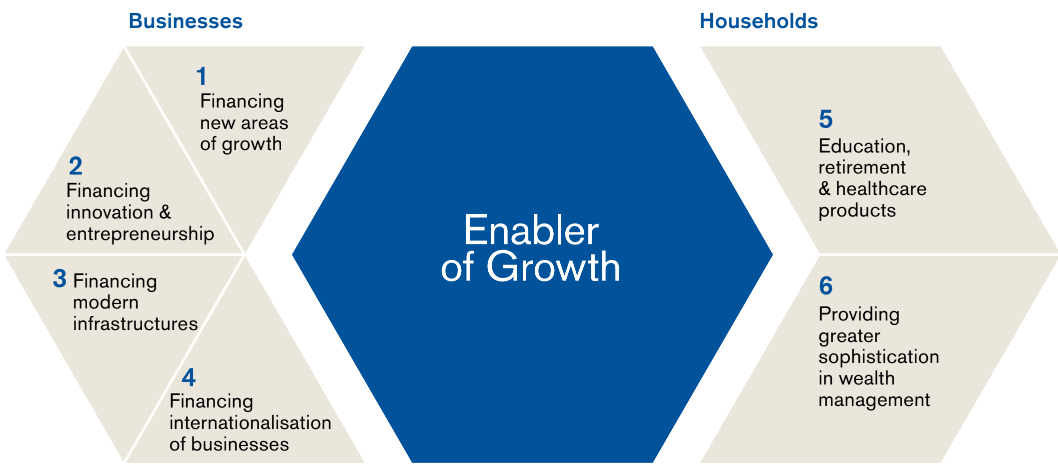
As Malaysia enhances its trade and investment linkages with the region and other parts of the world, the financial sector has a crucial role in supporting the expansion of Malaysian corporations, intermediating surplus funds from the region to productive investments, and facilitating cross-border capital flows. Increasing consumer demand from a larger middle-income population in the region will also be a key impetus for a more sophisticated and comprehensive range of financial services. The presence of Malaysian banks in the region is expected to continue to expand and become more entrenched, while the financial markets is expected to deepen with expanded international outreach, especially in Islamic finance. In the process, the mobilisation of cross-border funds to meet the financing and investment needs of domestic, regional and international businesses will contribute significantly to the deepening of the financial system in Malaysia.

The aim is therefore to develop a vibrant and sustainable financial system that will facilitate economic activities moving up the value chain, meet domestic and regional financing needs of all firms across the risk-reward spectrum, and support financing of large and long-term projects. The capacity of the financial system will also be enhanced to better support the

The financial sector as an enabler of growth

Enabler of Growth

The financial sector should effectively & efficiently allocate resources to the relevant activities that facilitate the transformation of Malaysia towards a high value-added, high-income economy



internationalisation of Malaysian businesses as well as provide a comprehensive range of solutions for mitigation of business and financial risks.

In terms of the provision of financial products and services to households, as Malaysia transitions to become a high-income economy, the expansion of the middle class and rising income levels will require more diversified and differentiated risk-return savings and investment products, and financing options for education, wealth creation, accumulation and preservation, and financial planning. Consumers will also demand for a more diverse range of high-quality financial products and services that are cost-effective and reliable, and offered through more accessible, convenient and cost-effective delivery channels.

In tandem with the gradually maturing population, greater emphasis will also be accorded to develop products and services that cater for retirement and long-term medical demands of consumers. The development of a robust and efficient pension framework will also contribute as an important source of long-term funding for large major projects required to facilitate the economic transformation process.

The mobilisation of cross-border funds to meet the financing and investment needs of domestic, regional and international businesses will contribute significantly to the deepening of the financial system in Malaysia

Going forward, the vision is for the financial sector to serve as the foundation from which Malaysia's transformation into a high value-added, high-income economy can be achieved through effective and efficient domestic and regional financial intermediation that will comprehensively mobilise diverse savings towards a wide spectrum of investment activities in Malaysia and across borders. The financial sector will be able to channel funds from surplus to deficit entities, through a complete range of intermediaries, markets and instruments, and perform the intermediation function to the highest value creation at a competitive cost. This process will be driven primarily by productive competition and sustainable practices, thereby contributing towards the preservation of financial stability. This will be achieved by having the following:

- A vibrant and sustainable ecosystem comprising diversified, strong and competitive financial institutions and diversified financial markets, supported by effective and efficient financial infrastructure, as well as a conducive operating environment;
- An appropriate balance between regulatory and market-based mechanisms to ensure the continued development of the financial sector in providing financial products and services that meet the demands of businesses and individuals; and
- Greater regionalisation and internationalisation of the Malaysian financial system.

Recommendation 2.1.1

Enhance the financial sector's capability to support high value-added activities. This includes supporting the financial needs of innovative enterprises throughout the lifecycle, which will encompass the transition to the growth and expansion stages, and facilitating efficient exit for early stage investors, by:

i. Enhancing the role of financial institutions in developing profit- and risk-sharing investment and financing facilities, such as equity- and quasi-equity-based financing. This will be complemented by sufficient safeguards to ensure that such activities are not funded by retail deposits in these financial institutions.

ii. Promoting the offering of factoring and leasing by financial institutions and DFIs to meet the needs of small businesses and start-ups. This would also include international factoring to finance exporters, given Malaysia's high trade openness.

iii. Promoting the full range of financing by DFIs to targeted strategic sectors, particularly in the agriculture, cooperative and SME sectors.

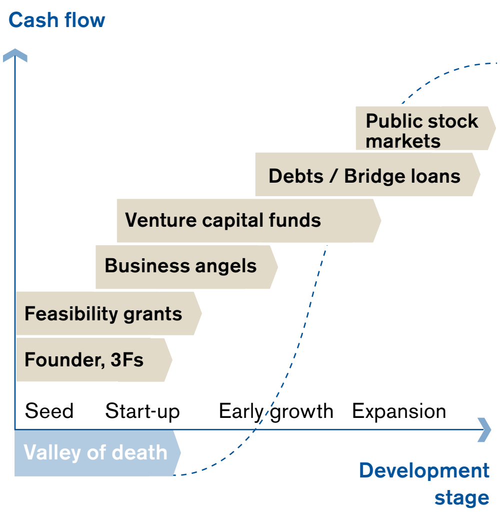
iv. Promoting market-based alternatives, such as a receivables exchange which allows

Financing innovation and entrepreneurship

A financial system that efficiently provides financing to support innovation & entrepreneurship

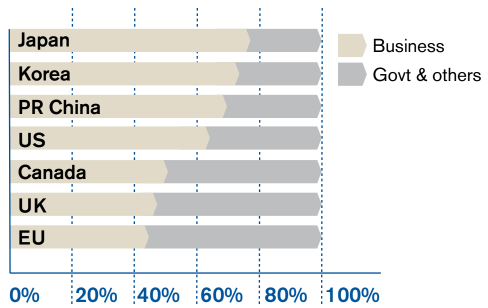
1. Growth of innovative firms & entrepreneurship at all stages of development requires different sources of financing

Different stages of innovative firms require different forms of financing



R&D relies mainly on internal financing

R&D by sources of funding



EU: Business sources of funding for R&D

Own financing	Bank borrowings	Market financing	
		Equity	Bond
81.4%	5.0%	1.1%	0.3%

Source: Science and Engineering Indicators 2010, Financing of Innovative Technology Survey, France 2000, UN Economic Commission for Europe, Policy Options and Instruments for Financing Innovation businesses to sell receivables to institutional investors in a real-time auction, for more effective access to funding.

v. Promote the development of expertise to support new growth areas such as green technology and the adoption of socially and environmentally sustainable financing practices which are consistent with international standards.

Recommendation 2.1.2

Increase the supply of a broad range of private risk capital funding across all stages of financing by collaborating with the Government and other agencies to:

i. Promote the establishment of funds of funds that invest in the venture capital industry both domestically and regionally, and provide incentives for investments in innovative local start-ups. The sources of financing could potentially originate from domestic and foreign business angels, private equity and venture capital funds, as well as institutional investors.

ii. Facilitate the establishment of new institutions with specialised expertise to provide risk capital financing, complementing the private equity and venture capital industries. The capacity and capability of DFIs to have a greater role in providing risk capital financing to support targeted strategic sectors will also be enhanced.

Recommendation 2.1.3

Enhance the capacity of the financial sector to support the financing needs of domestic and regional large-scale projects with long gestation periods, including infrastructure development. The provision of products with longer maturities will meet the longer-term investment demand of insurance companies and institutional investors, including pension funds. Towards this end, the following measures will be pursued:

i. Encourage strategic partnerships between domestic financial institutions and foreign financial institutions specialising in long-term project financing to strengthen domestic capabilities.

ii. Promote the regionalisation of Malaysian financial institutions to participate in the effective mobilisation and allocation of regional capital in addition to domestic savings, towards both local and regional projects.

iii. Support the establishment of new institutions with specialised expertise in structuring large and long-term financing, in particular infrastructure funds to capitalise on economies of scale by pooling funds from a diverse range of investors, as well as mobilise regional savings to be invested in domestic and regional projects.

iv. Strengthen the risk assessment and management capabilities of insurance companies and institutional investors, including pension funds, to better ascertain the prospects and financial viability of long-term projects, instead of relying solely on the credit ratings of such instruments.

Recommendation 2.1.4

Support the regionalisation and internationalisation of Malaysian businesses by strengthening Malaysian financial institutions' knowledge of the different markets to overcome the key challenge of information asymmetries. This includes:

i. Establishing strategic partnerships with foreign counterparts to facilitate greater information exchange, counterparty risk assessments and market information.

ii. Collaborating with Government agencies, industry specialists, DFIs, financiers, and industry and business associations to establish a common platform for information exchange on financial products and services and other relevant information. International linkages will be established with global entities such as foreign financial institutions, foreign trade promotion agencies and multinationals to facilitate greater synergies.

iii. Facilitating more significant presence and participation of qualified Malaysian financial institutions abroad, supported by cross-border coordination and cooperation in financial regulation, supervision, surveillance, and crisis prevention and resolution mechanisms to preserve financial stability.

Financing for greater internationalisation of businesses

A financial system that effectively facilitates the internationalisation of Malaysian firms

1. Expansion of firms abroad requires a myriad of financial services
2. Private financial institutions to meet financing needs that support the internationalisation of firms

Necessary financial services for successful internationalised firms

- Increasing need for cross-border financing as overseas business opportunities for companies expand
- Particularly, funding will be required for three major purposes:

Trade Finance	International Finance	Project Finance	
• Trade finance for exports & imports • Credit insurance to mitigate default risk	• Funding of overseas plants & operations • Includes small, shorter tenure loans as working capital	• Large, long tenure loans with limited recourse to the project sponsor • Requires credit assessment capability to guarantee against risks	**To be complemented by additional end-to-end advisory services**

- Structural limitations potentially inhibit the local market's capacity to lend

〉

- **Need for specialist financial institutions (e.g. export credit agencies & export-import banks) to complement private financial institutions**
- **Market-based solutions**

Recommendation 2.1.5

Promote a conducive environment for financial institutions to develop more products and enhance services for businesses to better manage business risks, by:

i. Promoting the development and offering of a wide range of foreign currency products and services to meet the demands of businesses for foreign currency financing, hedging of foreign currency receipts and payments, as well as other foreign currency exposures.
ii. Promoting the development and offering of political risk insurance to ensure adequate protection for Malaysian businesses that expand abroad.
iii. According greater flexibility for qualified insurers and takaful operators to underwrite surety bonds and provide credit guarantee insurance. This will provide businesses with greater diversity of products that mitigate risks such as non-performance of contracts and non-payment by debtors. Existing caps on these insurance businesses will be gradually removed, subject to compliance with prudential requirements as well as the institutional capacity and financial soundness of the insurers and takaful operators.
iv. Facilitating greater injection of foreign expertise in the insurance and takaful broking and loss adjusting industries to better support insurance and takaful business, especially for the risk mitigation needs of firms engaged in high value-added activities.

Recommendation 2.1.6

Improve access to information to reduce information asymmetries and enhance the effectiveness and efficiency of financial intermediation. This includes:

i. Strengthening the credit information framework to facilitate more comprehensive financial assessments of borrowers, taking into account their repayment track records on other obligations which are not currently captured by the Central Credit Reference Information System (CCRIS).

ii. Establishing a technology advisory facility that pools the expertise of domestic and regional practitioners and academicians to strengthen the capability of financial institutions in assessing knowledge- and technology-based proposals. The feasibility and prospects of businesses will be assessed through a rating system. Such assessments should be available upon request by financial institutions or directly by the businesses.
iii. Collaborating with the Government to set up an integrated platform to allow both domestic and foreign investors to network with entrepreneurs for the purpose of exploring investment opportunities. This is also aimed to provide a one-stop centre for entrepreneurs to advertise business ideas and empower them with appropriate business and financial skills.

Recommendation 2.1.7

Develop a vibrant private pension industry to enhance Malaysians' financial preparedness for retirement and old age. The voluntary private pension industry would effectively complement mandatory retirement saving schemes and old-age welfare safety nets. The private pension industry will also support the core objectives of the Government's pension reform initiative, which includes protection against the risk of old-age poverty and consumption-smoothing in order to maintain reasonable living standards from work-life into retirement. The development of the pension industry is also expected to enhance the role of pension funds as a key source of funding, particularly for the longer-term and risk-based financing needs of the economy. Efforts will be focused on positioning insurance companies and banking institutions as significant intermediaries in the private pension industry to drive the outreach of retirement products by leveraging on their extensive distribution networks, as well as on enhancing consumer awareness by promoting the overall confidence of consumers in pension products and safeguarding the funds for retirement. This includes:

i. Developing a supporting infrastructure and regulatory framework for the development and offering of diversified and innovative pension products, such as annuities that mitigate longevity and inflation risks, "locked-in" savings that minimise pre-retirement

The development of the pension industry is also expected to enhance the role of pension funds as a key source of funding, particularly for the longer-term and risk-based financing needs of the economy

Financing old age & retirement and wealth management

A financial system that facilitates the adequate provision of retirement income including serving more affluent & sophisticated households

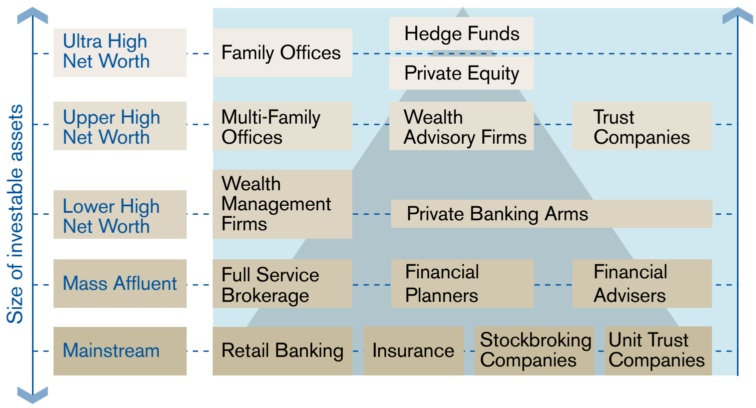
1. A well-developed financial sector can have an important role in retirement income provision that is financially sustainable, equitable from an inter-generational perspective and that provides adequate pension & social security benefits
2. Affluent and more sophisticated households would require and demand a wider range of financial services for more optimal wealth management
3. Facilitates the smoothening of household consumption patterns

Development of Pillar 3 is important for comprehensive retirement income provision

Pillars	Characteristics
Pillar 0	Social assistance to provide a minimum level of protection
Pillar 1	Mandatory public pension plan (may be partially funded)
Pillar 2	Mandatory occupational / personal pension plan (fully funded)
Pillar 3	Voluntary occupational / personal pension plan (typically market-driven)
Pillar 4	Informal support (including family), other formal social programmes (including healthcare), other individual financial & non-financial assets (including home ownership)

Source: Holzmann, Hinz and Dorfman (2008), "Pension Systems and Reform Conceptual Framework", World Bank

Wealth management landscape in Malaysia



As the pool of mass affluent grows in Malaysia as well as across the region, there will be greater demand for innovative and customised financial solutions to meet the varying demands of individuals leakages and financial solutions for retirees such as reverse mortgages.

ii. Collaborating with the Government to develop incentives to spur the development of the private pension industry by the insurance companies and banking institutions.
iii. Promoting greater consumer education and the adoption of simple and comprehensible product disclosure and transparency standards.
iv. Strengthening the financial safety net for pension products to promote confidence and predictability of the expected retirement income levels.
v. Implementing appropriate regulatory parameters applicable to pension products to safeguard their ability to fulfill the financial needs at retirement.

Recommendation 2.1.8

Enhance the provision of wealth management products and services to better cater to the demands of the growing affluent segment of the community. As the pool of the affluent grows in Malaysia as well as across the region, there will be greater demand for innovative and customised financial solutions to meet the varying demands of individuals. Financial advisory services will become increasingly crucial in the planning and arrangement of the financial affairs of the affluent, ranging from estate management, asset allocation, tax planning to retirement planning.

Moving forward, the institutional set-up and infrastructure to support a more effective provision of wealth management products and services will encompass the following measures:

i. Streamlining the current dual licensing regime for financial advisers and financial planners, including potential harmonisation and convergence of regulatory and operating requirements for financial planners and advisers.
ii. Encouraging the establishment of family offices to better accommodate the demands of ultra high net worth individuals and families, which will also contribute towards Malaysia's aspirations to become a global centre for Islamic wealth management.
iii. Promoting Islamic fund and wealth management activities through the offering of innovative financial solutions to meet the more sophisticated investment demands of the increasingly affluent population, including households in Asia.
iv. Enhancing the development of important ancillary services that support the wealth management industry, such as legal services and real estate planning, in collaboration with relevant regulatory agencies and industry associations.
v. Facilitating the internationally-established financial institutions present in the Labuan International Business and Financial Centre (Labuan IBFC) to offer services through foundations and private trust companies to institutional investors and high net worth individuals.

Recommendation 2.1.9

Enhance the capacity and capability of the insurance and takaful industry to provide higher value-added medical and health insurance. This includes:

i. Encouraging insurers and takaful operators to offer higher-end and more sophisticated insurance and takaful products, complementing the basic protection to be provided under the oncoming national health financing scheme. This includes the provision of long-term care benefits, such as assisted-living and hospice care.
ii. Encouraging greater strategic alliances between domestic insurance companies and foreign financial institutions with specialised expertise in medical and health insurance and takaful.

Recommendation 2.1.10

Introduction of greater operational flexibility for financial institutions to introduce new products, expand the distribution network and widen their outreach to consumers subject to appropriate safeguards and meeting prudential requirements. Innovation in delivery channels over the years, particularly in the retail segment, has been catalysed by the advent of new technology and the drive by financial institutions to reduce costs, enhance revenues, increase customer satisfaction and widen outreach nationwide. Among the key initiatives that will be introduced under this broad strategy include:

i. Gradually removing restrictions for locally-incorporated foreign banking institutions to establish non-branch delivery channels, such as off-site electronic terminals and kiosks. This is in line with the objective to promote electronic means as a key delivery channel for financial services to accelerate the migration towards electronic payments (refer to the chapter Electronic Payments for Greater Economic Efficiency). Banking institutions are expected to leverage on this flexibility to introduce more cost-effective delivery channels for financial services to consumers.
ii. According greater flexibility for locally-incorporated foreign banking institutions to establish more physical branches in the medium term, with the aim of promoting greater outreach of financial services. These flexibilities will also be balanced with safeguards to ensure that banking institutions continue to fulfill their role in meeting the financial inclusion objectives (refer to the chapter Strengthening Regional and International Financial Integration).
iii. Encouraging insurers and takaful operators to enhance the offering of insurance and takaful products through non-branch delivery channels. This aims to expand the outreach of insurance and takaful services through more cost-effective means and contribute towards enhancing the insurance and takaful penetration rate in the country.

iv. Allowing locally-incorporated foreign banking institutions to conduct hire purchase business. This will be facilitated through appropriate legislative amendments.

Recommendation 2.1.11

Enhance service quality in the provision of financial services and the conduct of business by financial institutions through:

i. Collaborating with industry associations and training institutes to develop market-based mechanisms and training programmes aimed towards enhancing the level of service quality in the financial sector.
ii. Enhancing fair dealing in financial services through transparent service quality measurements.

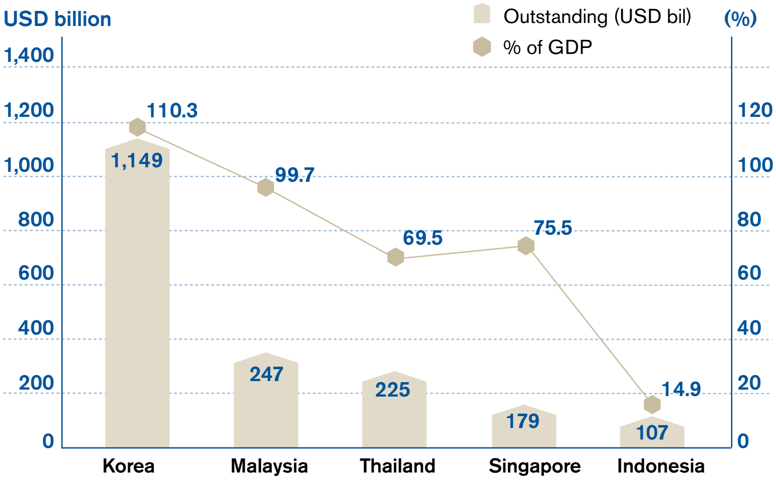
The implementation of the initiatives identified in this chapter will commence immediately, with a particular focus on strategies to reinforce the financial infrastructure and create a conducive ecosystem for more effective intermediation of funds in the short to medium term. These include initiatives such as enhancing the credit information framework and establishing a technology advisory facility to support assessments of knowledge and technology-based proposals. Efforts to enhance the institutional structures will be made on an ongoing basis to continuously promote greater efficiency in the intermediation process, such as encouraging financial institutions to develop alternative forms of financing and promoting the offering of new financial products and services to meet demands of the changing demography.

2.2

developing deep and dynamic financial markets

Financial markets have an important role in the productive mobilisation of savings and allocation of capital. Efficient financial markets also support the effective transfer of risks and management of liquidity.
As Malaysia transitions towards a high value-added, high-income economy, vibrant, competitive and resilient financial markets are necessary to meet the diverse and more complex demands of a more developed and internationally integrated economy.

Bond market size as at Dec 2010



Source: Asian Bonds Online; Bank Negara Malaysia

Vibrant, competitive and resilient financial markets are necessary to meet the diverse and more complex demands of a more developed and internationally integrated economy

Currently, the Malaysian financial markets are among the more developed markets in Asia. The size of the debt securities market has grown to RM867 billion or 105% of GDP in 2011, making it one of the larger debt securities markets in emerging Asia. The debt securities market has continued to develop with a growing presence of international issuers and investors.

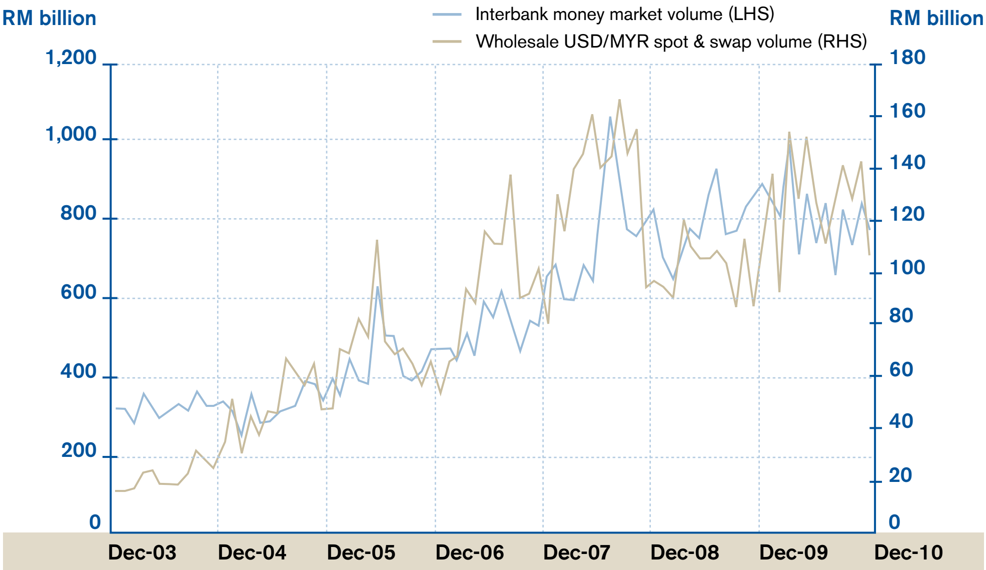
The Islamic capital markets have also expanded both in terms of ringgit and foreign currency issuances and the range of new financial instruments. Issuers have responded to the demand for more innovative Islamic financial products and services. The progress has also culminated with the launchings of ringgit and foreign currency sukuk indices, developed in collaboration with the Association of Islamic Banking Institutions Malaysia, Bloomberg and Bank Negara Malaysia. These indices mark another significant milestone achieved in the internationalisation of Islamic finance in Malaysia.

The money market and the foreign exchange market have grown in depth and liquidity. The daily average volume traded in the money and foreign exchange markets in 2010 reached RM39 billion and USD7.3 billion respectively. Turnover in the foreign exchange market has increased significantly to 3.32 times the volume of trade in goods and services, higher than the 1.64 times registered in 2005. The size of the equity market has also expanded, with market capitalisation increasing from RM444 billion in 2000 to RM1.2 trillion in 2010.

Meanwhile, direct investment and portfolio capital flows have increased in both directions, with a rising trend of foreign and portfolio investment abroad by Malaysian corporations and institutions. These flows, and the continued expansion of regional and international trade, will cement the direction for greater integration of Malaysian financial markets with the international financial markets, in particular, those in Asia.

Much of the progress in the financial markets reflects the combined result of the Bank's initiatives with other regulators and market players. The progressive liberalisation of the capital account and the opening up of the financial system and markets to a larger group of foreign institutions were also important contributing factors. In addition, the regulatory environment have facilitated financial market and real sector economic activities.

Wholesale foreign exchange & interbank money market monthly volume



Source: Bank Negara Malaysia

Moving forward, the Blueprint envisions that the Malaysian financial markets will grow in breadth and maturity, and become an important gateway to the ASEAN markets. In Islamic finance, it is envisaged that Malaysia will become a leading international Islamic financial centre. To fulfil these objectives, domestic financial markets will be geared to perform the following roles:

- Competitively meet the funding requirements of corporations, financial institutions and investors across the maturity spectrum and diversity of funding requirements;
- Address investment needs across a variety of institutional and retail investors through marketable or customised solutions in terms of choices of instruments and asset classes;
- Offer a variety of risk management solutions to meet the diverse demands of portfolio investors, financial institutions and corporations in investments, financing, and trade activities; and
- Intermediate competitively across domestic and regional markets and facilitate investment, financing, trade payment and settlement in the region.

The Malaysian financial markets will grow in breadth and maturity, and become an important gateway to the ASEAN markets; while in Islamic finance, Malaysia will position itself as the leading international Islamic financial centre

Enabling Conditions

Vibrant financial markets rely on a holistic development of the money, foreign exchange, bond, equity and derivatives markets as well as the supporting infrastructures. Institutional capacity building and prudential safeguards that were put in place thus far have strengthened financial players' capabilities and resilience and have better positioned the industry in a more integrated and competitive environment. Strong and highly rated financial institutions supported by globally integrated settlement and payment system will further increase the ability of the markets to provide competitive offerings and conduct cross-border financial activities. This includes leveraging on the strong and large international financial institutions in the Labuan International Business and Financial Centre (IBFC) to contribute to the vibrancy of the markets. Reinforced by a supportive regulatory framework, which will allow Malaysia to become a netting friendly jurisdiction, the costs in undertaking financial market transactions in Malaysia will be reduced considerably.

Progressive liberalisation of foreign exchange administration together with commitments to support financial market developments will further enhance the country's regional and international linkages. With the preconditions in place, it paves the way for the full 'internationalisation' of the ringgit, where access to the ringgit market by non-residents for purposes beyond settlement of trade and investment will be fully liberalised. While such a move would further increase the efficiency in undertaking financial transactions in the ringgit market, it would also be accompanied by the risk of potentially destabilising speculative foreign exchange activities.

Preconditions therefore need to be met including having deep and vibrant domestic foreign exchange and money markets as well as ensuring sound risk management and corporate governance practices by financial market players. These preconditions will facilitate increasing two-way flows and the development of avenues and tools to manage risks. The surveillance framework and prudential safeguards will also need to be enhanced to mitigate or manage such risks, in particular to prevent excessive speculative activities that would undermine the overall macroeconomic and financial stability.

The recommendations in the Blueprint will focus on the money, foreign exchange and government securities markets. The recommendations outlined below will form the core of the Bank's initiatives to develop these markets.

Recommendation 2.2.1

Promote an efficient and competitive money market with greater depth and liquidity by offering a wide range of liquid ringgit and multi-currency money market instruments, with participation by a wide variety of players. This includes:

i. Reducing counterparty risks and enhancing liquidity in money market transactions by promoting greater volume of securities and collateralised transactions. This will involve further development of the repurchase agreement (repo) market for domestic and cross-border transactions. The Bank aims to achieve a target of 70% of wholesale money market transactions to be in conventional and Islamic repo or any other form of collateralised transactions by promoting repo transactions for ringgit and foreign currencies funding including the use of cross-border collateral denominated in foreign currencies. In addition, it will be facilitated by conducting monetary operations with greater reliance on securities and collateralised transactions including accepting highly rated corporate short-term papers and qualified foreign currency securities.
ii. Widening participation in the wholesale money market to include qualified corporations to enhance liquidity. This includes allowing corporations that meet the qualifying criteria to participate directly in the wholesale money market and expanding the intermediary roles of money market brokers to provide services to the qualified corporations.
iii. Promoting deep and liquid interest rate derivatives for cost-effective hedging by financial institutions and corporations through the liberalisation of non-residents' participation in the onshore interest rate derivatives market to enhance market liquidity and to raise the level of knowledge and skills to encourage greater use of interest rate derivatives by corporations, pension funds and insurers and takaful operators.
iv. Enlarging the size and range of Islamic money market instruments to cater for different market needs through innovative Shariah-compliant solutions by promoting equity-based (including hybrid) instruments. This would be achieved by using these instruments in the Bank's market operations, and to collaborate with market participants to establish a mechanism/platform for Islamic banks to hedge their risk exposures.

Recommendation 2.2.2

Deepen liquidity in the government debt securities and sukuk markets by enhancing the benchmark yield curve, increasing product offerings and introducing government debt securities derivatives products. A liquid government debt securities market would contribute to minimising the cost and risk of financing to the Government and provide a reflective benchmark yield curve that facilitates market participants to appropriately price private debt securities. It will also enable the Government to better manage its public debt and for the private sector to more efficiently raise funding to finance long-term initiatives. Towards this end, the recommendations include:

i. Collaborating with the Government, to increase the issuance frequency of government benchmark securities across the yield curve and ensuring the issuance sizes are sufficient to support liquidity and benchmarking by the financial markets.
ii. Facilitating active buy-back or conversion of the off-the-run government securities to support liquidity and more transparent pricing of the entire yield curve.
iii. Enlarging the issuance size of government treasury bills to enhance the Government's financial management and debt operation.
iv. Increasing the product dimension in the government securities market to create benchmark pricing for these instruments by introducing long-term and index-linked securities, promoting innovative Shariah-compliant government securities using equity and hybrid contracts and issuing securities in regional currencies to enhance the product offerings for the foreign currency debt securities and sukuk market in Malaysia. This may also include issuance of securities in regional currencies out of the Labuan IBFC.

Recommendation 2.2.3

Broaden the investor base for the government securities market, by:

i. Exploring cost-effective investment and distribution channels for direct retail participation in the debt securities and sukuk markets, especially in the government securities market.

Efforts will be concentrated on improving liquidity, depth and participation in the money, foreign exchange and government securities markets, and the foreign exchange administration rules will be progressively liberalised to further raise efficiency in financial market transactions

ii. Collaborating with regional countries to develop a regional principal dealers' framework to be the market makers for cross-border dealings of government securities.

Recommendation 2.2.4

Enhance avenues for risk management and instruments to manage risk exposures. Derivatives and other risk management instruments can be used to protect the value of investments, hedge liabilities and also enhance secondary market liquidity, through:

i. Providing further flexibilities to Principal Dealers in undertaking short-selling activities.
ii. Broadening the scope of Guidelines on Securities Borrowing and Lending Programme to allow non-Principal Dealers to borrow and lend securities.
iii. Enhancing the mechanism and infrastructure that facilitate securities-driven repo transactions such as central clearing for repo transactions.
iv. Structuring government securities issuances to support the design and specification of government securities futures contract.

Recommendation 2.2.5

Developments in the foreign exchange market in Malaysia have so far focused on meeting the growing needs of the real sector for trade and direct investment. As corporations expand their businesses overseas and more Malaysians invest internationally, there is a need to offer diversified products and services to meet such foreign currency financing for long-term investments, hedging of receipts and payment and for other risk management purposes. In this regard, the recommendation places emphasis on enhancing access and improving liquidity in the foreign exchange market and encouraging financial institutions to offer a wider range of foreign currency products and services. The recommendation is therefore to broaden the participation in the onshore foreign exchange market by:

i. Allowing corporations to actively manage foreign currency exposures arising from their overseas operations.
ii. Permitting institutional funds and retail investors to trade in foreign currencies, including margin trading, as a new investment class and avenue, subject to suitable safeguards.
iii. Allowing financial institutions to offer internet and electronic trading platforms for corporations and retail investors, subject to full disclosure of risks, and in compliance with prudential safeguards and investor protection requirements.
iv. Permitting participation by non-residents in the onshore foreign exchange derivatives market without underlying trades or investments, subject to prudential limits on funding and size of open positions.

Recommendation 2.2.6

Support the use of regional currencies for trade settlement and direct investment activities to reduce transaction costs and risks in regional cross-border transactions. This would lead to the creation of new asset classes in the Malaysian market, characterised by a broad range of investment products denominated in regional currencies, by:

i. Encouraging financial institutions to provide direct foreign exchange cross quotations with both onshore and offshore counterparties. The Bank will provide foreign currency liquidity in designated regional currencies to facilitate trade settlement.
ii. Allowing financial institutions to quote ringgit crosses to residents and non-residents with appropriate safeguards to enhance intermediation linkages.
iii. Promoting Malaysia as a centre for regional treasury operations for home-grown resident multinational companies and foreign multinational corporations.

Recommendation 2.2.7

Develop infrastructure and institutional arrangements that will support efficient and cost-effective foreign currency trading, payments and settlements onshore. This includes:

i. Promoting a common network infrastructure that includes establishing linkages between Real-time Electronic Transfer of Funds and Securities system and international securities depositories.
ii. Creating an electronic trading platform for regional currencies, to complement cost-effective offering of cross-border financial products and services.
iii. Collaborating with the financial market industry to establish a Self Regulatory Organisation to elevate professionalism in the foreign exchange market.

The implementation of the initiatives will commence immediately with a focus on widening product variety and access to financial markets and enhancing integration with the regional and global markets. Over the medium term, the implementation of the strategies will focus on strengthening the financial institutions' capacity and widening access to financial markets for a larger number of participants. This will improve market liquidity and create more business opportunities as well as promote market activities. Concurrently, the market infrastructure will be enhanced to support the efficiency of financial transactions. In the medium to long-term, integration of the financial markets with the regional and global markets will be further enhanced by allowing greater access to non-residents. As the Malaysian financial markets develops with strengthened risk management capabilities and the necessary prudential safeguards and investor protection mechanism in place, Malaysia will become significantly internationally-integrated with strong linkages to other emerging economies and the traditional financial centres.

2.3

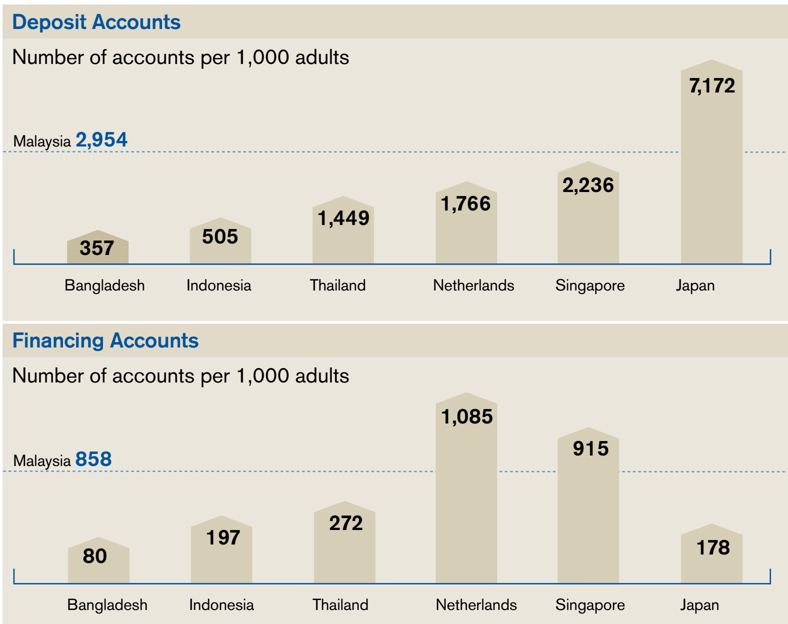
financial inclusion

for greater shared prosperity

Pursuing the financial inclusion agenda, where all members of society have the opportunity to participate in the formal financial system, will continue to be a key component of Malaysia's inclusive growth strategy. Financial inclusion will enable all citizens, including the low-income and rural residents, to have the opportunity to undertake financial transactions, generate income, accumulate assets and protect themselves financially against unexpected adverse events, thereby enabling them to benefit from economic progress. This will in turn contribute to balanced and sustainable economic growth and development.

Many initiatives implemented over this recent decade have significantly improved financial inclusion in Malaysia. These include the introduction of new financial products and services that meet the diverse requirements of all segments. This has been reinforced with the development of a consumer education and protection framework, as well as the strengthening of the enabling financial infrastructure. In addition, the role and capacity of development financial institutions (DFIs) have also been enhanced. As a result of these initiatives, the take-up of deposits has increased from 1,975 deposit accounts per 1,000 adults in 2000 to 2,954 deposit accounts per 1,000 adults in 2010. Meanwhile, the take-up of financing has increased from 310 financing accounts per 1,000 adults in 2000 to 858 financing accounts per 1,000 adults in 2010. These achievements have elevated Malaysia's position in various global financial inclusion rankings. This includes Malaysia's number one ranking since 2007 for "Getting Credit" in the "Ease of Doing Business" index by the World Bank and number eight out of 142 countries in 2011 for "Ease of Access to Loans" by the World Economic Forum.

Cross country comparison of selected financial inclusion indicators



Source: Consultative Group to Assist the Poor (CGAP) and Bank Negara Malaysia

Moving forward, in an increasingly market-driven and more competitive economy, greater efforts are required to achieve the vision of an inclusive financial system that best serves all members of society, including the underserved, to have access to and usage of quality, affordable essential financial services to satisfy their needs, towards greater shared prosperity. The successful achievement of the financial inclusion agenda will be characterised by the following outcomes:

- Increased convenient access to financial services, including in rural areas;
- More effective usage of financial services by all citizens, including the underserved, through an expanded range of products and services that meets their needs; and
- Enhanced quality of financial services that satisfies the financial needs of all citizens, including the underserved.

Recommendation 2.3.1

Adopt innovative channels to enhance the outreach of quality and affordable financial services in a more cost-efficient manner. This includes:

i. Supporting the development of agent banking by developing a comprehensive agent banking framework to enable outreach of financial services at lower costs. Agent banking is the use of non-bank retail outlets (for example, post offices, petrol stations and other retail chains) by financial institutions to deliver financial services. By leveraging on technology, agent banking also contributes to the electronic payments agenda by facilitating an increase in the number of debit cards, point-of-sale terminals and mobile banking services.

ii. Accelerating the roll-out of innovative delivery channels, including mobile banking, by leveraging on technological advancements and strengthening collaboration

Greater efforts are required to achieve the vision of an inclusive financial system that best serves all members of society, including the underserved, to have access to and usage of quality, affordable essential financial services to satisfy their needs, towards greater shared prosperity amongst relevant stakeholders, including telecommunication companies. This will provide users with the convenience to perform financial transactions at all times without the need to visit a physical access point.

A comprehensive agent banking framework will be developed to enable outreach of financial services at lower costs

Recommendation 2.3.2

Expand the range of products and services that will meet the distinct financial needs of all citizens, including the underserved. This includes:

i. Encouraging flexible micro financing products that enable prompt drawdown of financing in times of need and prepayment of financing during good times, to meet the needs of micro enterprises which have irregular or seasonal income streams.
ii. Enhancing provision of long-term contractual micro-savings products with low committed periodical savings and favourable returns to enable low-income households to inculcate the savings habit and fulfill long term goals such as starting a business, home ownership, education and to have a secure retirement.
iii. Facilitating the insurance and takaful industry to develop microinsurance and microtakaful products, which provide the underserved with adequate financial protection against unexpected adverse events in a cost-effective, accessible and easy-to-understand manner through a facilitative regulatory environment, strengthened delivery capacity, increased market awareness and enhanced consumer literacy.

Recommendation 2.3.3

Strengthen the institutional arrangements to provide financial services to all citizens, including the underserved and build capacity of practitioners in an effective and sustainable manner. This includes:

i. Strengthening the financial inclusion role of specialised DFIs which mobilise savings of small Malaysian savers and enhance micro financing to micro enterprises. This is achieved by having appropriate key performance indicators for financial inclusion, adequate representation on the board with expertise in financial inclusion, as well as improved potential for innovative product development.
ii. Encouraging financial training providers to offer structured and cost-effective financial inclusion training for professionals from financial institutions, cooperatives, microfinance institutions and

non-governmental organisations (NGOs) in Malaysia, which can be extended to the region to draw on the sharing of experience from different jurisdictions.

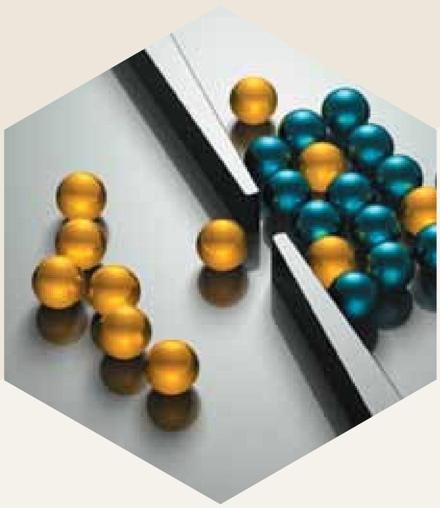
iii. Enhancing the monitoring framework for the outcomes of financial inclusion initiatives, which are to achieve convenient outreach, high take-up, responsible usage and high consumer satisfaction, and a financial inclusion index to facilitate the tracking of the overall financial inclusion progress in Malaysia.

Recommendation 2.3.4

Enhance the knowledge and capacity of the underserved to utilise financial services responsibly. This includes:

i. Improving the provision of advisory services to increase the income generating capability of micro enterprises through greater participation of NGOs that have the capability to provide effective handholding and have strong relationships with the micro enterprise communities, to build skills and confidence of micro entrepreneurs.
ii. Enhancing the role and outreach of Mobile LINK (coach and mobile counter services) and the collaboration with consumer associations.

The implementation of all the initiatives will be conducted in phases over the immediate and medium term. In the first phase, efforts will be focused on adopting innovative channels to expand outreach of existing financial services to the underserved. In the second phase, the range and features of financial products and services will be further expanded to meet the diverse and distinct needs of the underserved. Finally, the capacity of financial service providers and the underserved are enhanced to intermediate funds more effectively.



3 Enhancing regional and international financial linkages

interlinked

integrated

3.1

strengthening regional and international financial integration

Strengthened ties with regional and international economies are key foundations in Malaysia's transition towards becoming a high value-added, high-income economy. Stronger cross-border linkages will serve to enhance trade and investment opportunities by expanding the market for final demand, increasing capital accumulation and improving factor productivity. Such cross-border linkages will also enhance opportunities for Malaysia and the region to capitalise on the diverse comparative advantages in the region.

Malaysia to be more regionally & internationally integrated
• Creation of an ASEAN Economic Community (AEC) by 2015
• Closer regional trade integration, through ASEAN & other bilateral or regional free trade agreements
• Malaysian corporations venturing abroad to expand business opportunities
• Labour & specialised talent increasingly more mobile
• Greater spill overs from dynamism of Asian economies

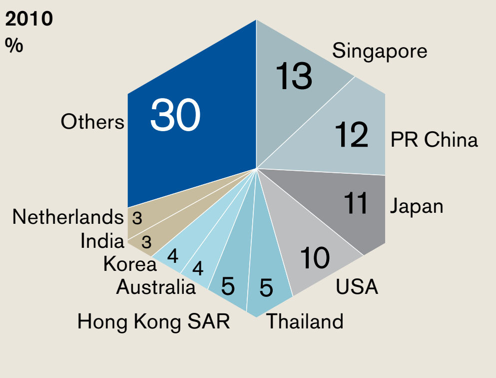
The Malaysian financial sector has made significant strides in facilitating the country's cross-border linkages with other economies. The overseas expansion of Malaysian financial institutions over this recent decade has supported the increasing trend in investments abroad by Malaysian corporations pursuing new opportunities and markets, particularly in the energy, construction, plantation and services sectors. The financial services provided by Malaysian financial institutions through their regional network have helped the growth and consolidation of the operations of Malaysian businesses in the region and other parts of the world.

To date, six out of eight domestic banking groups have an established presence in 19 countries worldwide, with substantial overseas operations centred in Southeast Asia. The significance of these operations has grown considerably. As at end-2010, the total overseas assets and contribution of overseas pre-tax profit of Malaysian banking groups were RM240.2 billion and 13.6% respectively, compared to RM3.3 billion and -4.3% respectively in 2002.

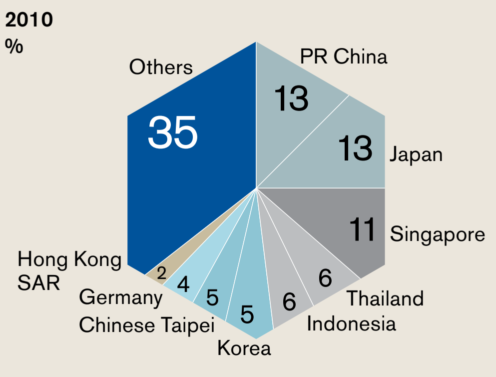
The international character of the Malaysian financial system has also been enhanced with the gradual liberalisation of the financial sector in this recent decade

Significant trade & investment between Malaysia and Asia

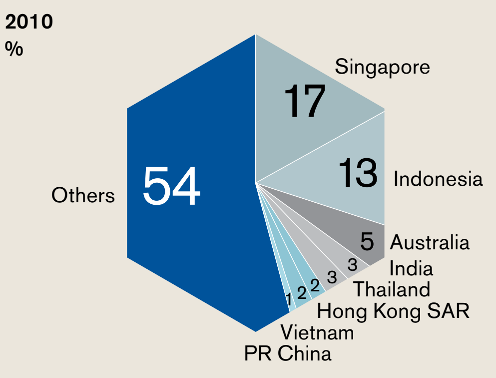
Malaysian exports by destination



Malaysian imports by source



Outstanding direct investment abroad



Source: Department of Statistics, Malaysia

The international character of the Malaysian financial system has also been enhanced with the gradual liberalisation of the financial sector during this period. 27 foreign banks from 14 countries have a presence in Malaysia. With the strengthening of domestic financial institutions, greater operational flexibilities have been accorded to incumbent foreign institutions, thus enhancing their potential to contribute to the economy and to balanced growth. More meaningful foreign participation in the financial system was also facilitated through the entry of new institutions to serve Malaysia's new growth areas, as well as higher foreign equity limits in domestic financial institutions. The progressive approach towards liberalisation of the financial sector has contributed to the further development of domestic financial institutions in a more competitive market, and prepared the foundations for an enhanced role of the Malaysian financial system in facilitating regional and international economic activity, while preserving the stability of the overall financial system.

Regional economic & financial integration to gather momentum

Intensification of intra-regional trade & investment

Trade Integration	Financial Integration
• Increasingly liberalised trade & investment environment • Bilateral or regional free trade agreements to intensify	• Recycling of Asia's surplus savings to the region especially for infrastructure investments • Asian Development Bank: Asia needs to invest about USD8 trillion from 2010 to 2020 (USD750 billion a year)

As Asia contributes more significantly to global growth and engages in even greater intra-regional trade and investment activities, a larger number of Asian financial institutions that can effectively intermediate the region's surplus funds to productive investments, facilitate cross-border capital flows and support the regional expansion of Asian corporations on a larger scale, will emerge. In addition, as economic and financial integration in Asia intensifies, cost considerations will accelerate the use of local and regional currencies for payments and settlements.

Beyond Asia, emerging economies in other regions will also gain greater prominence in the global economy. Malaysia will pursue initiatives to enhance financial sector linkages with other emerging economies to support mutually-reinforcing growth. Meanwhile, Malaysia's international linkages will also be strengthened through the continued growth of Malaysia International Islamic Financial Centre (MIFC) and the Labuan International Business and Financial Centre (Labuan IBFC). These efforts will also be complemented by the ongoing and progressive liberalisation of Malaysia's foreign exchange administration rules, which will be accompanied by appropriate safeguards to preserve financial stability.

It is envisioned that the Malaysian financial sector will evolve to be regional in orientation and internationally connected to increasingly intermediate regional and cross-border financial flows. In the Islamic financial system, this will extend beyond the region to other parts of the world. Malaysian financial institutions will have enhanced capacity to adequately serve the needs of Malaysian corporations going abroad. The Malaysian financial sector will also be well positioned to provide a full suite of products and services to support the financial requirements of international and regional corporations that invest and expand their businesses in Malaysia.

Liberalisation will create new opportunities in the Malaysian financial sector and contribute towards enhancing Malaysia's trade and investment linkages with other parts of the world. Going forward, policies on foreign investment in the financial sector through the issuance of new licences or the acquisition of significant equity interests in Malaysian financial institutions will be guided by two key considerations. The first relates to the prudential criteria and the second is for the investment to be in the best interest of Malaysia. Prudential criteria will include the consideration of the financial strength, business record, experience, character and integrity of the foreign investor; the soundness and feasibility of the business plans for the institution in Malaysia; the transparency and complexity of the group structure so as not to impede effective regulation and supervision by the Bank; and the nature and extent of supervision of the foreign investor in its home country.

In ensuring that the best interest of Malaysia is met, the following considerations will be taken into account:

- The effect of the foreign investment on economic activity in Malaysia, having particular regard to the contribution of the foreign investment in promoting and catalysing new high value-added economic activities, addressing demand for financial services in areas where there are gaps, and providing high-skilled employment opportunities.

The Malaysian financial sector will evolve to be regional in orientation and internationally connected to increasingly intermediate regional and cross-border financial flows

Also important is the contribution to enhancing productivity, efficiency and the quality of financial services.

- The extent to which the foreign investor will contribute towards enhancing international trade and investment linkages between Malaysia and other parts of the world.
- Contribution towards the internationalisation of Islamic finance and support for Malaysia's evolution as an international hub for Islamic finance.
- The impact the investment will have on financial stability, including on the level of competition in a specific market and on market behaviours that could result in a risk to financial stability.

A further consideration in assessing the best interest of Malaysia is the degree and significance of participation of Malaysians in domestic financial institutions. Similar to developed markets with strong and stable financial sectors, the continued presence of strong and well-managed domestic banking groups that mobilise more than a 50% share of resident deposits is important for the orderly growth and development of the financial sector. In this regard, the control of a certain significant share of domestic banking groups should continue to reside with Malaysians to promote and secure the best interests of Malaysia through the economic cycles and progressive stages of Malaysia's development.

The vision is for the Malaysian financial sector to be well developed and well connected to efficiently intermediate domestic and cross-border financial flows. This will be achieved through:

- A more open, competitive and diversified financial sector that will strengthen Malaysia's role in the effective and efficient intermediation of cross-border transactions and financial flows;
- The deepening of cross-border coordination and cooperation in financial regulation, supervision, surveillance, crisis prevention, and mechanisms for resolution; and
- Greater connectivity within the region to be supported by well-developed financial infrastructure and efficient information flows.

Recommendation 3.1.1

Promote greater foreign participation in the financial sector under a strategic and managed approach to evolve a financial sector that is more diversified and integrated with regional and international financial markets. The aim is to enhance the presence of regional and international financial institutions in Malaysia, whilst increasing the presence and significance of the activities of Malaysian financial institutions abroad. Financial institutions in Malaysia will have a greater role in intermediating and allocating capital across borders. Towards realising this potential, the Bank will pursue liberalisation measures while ensuring effective prudential safeguards to preserve financial stability. Key initiatives under this broad strategy include:

i. Issuing new licences to financial institutions with specialised expertise to support Malaysia's high value-added economic activities, serve new areas of growth, promote financial market development, and contribute towards enhancing the development of skilled talent in Malaysia.

ii. According more flexible foreign equity participation in financial institutions to boost the level of productive innovation, quality of financial services and risk management practices, and that serves the best interests of Malaysia.

iii. Providing greater flexibility for onshore financial institutions to establish new delivery channels, while promoting greater financial inclusion and wider adoption of electronic payments. The expanded outreach of foreign banking institutions through this flexibility will therefore be implemented together with measures that will accelerate the development of alternative delivery channels and maintain a balanced distribution of branch locations to support the needs of underserved areas.

iv. Advancing collective initiatives that support regional economic integration under the ASEAN Economic Community. This would involve granting greater flexibilities on a mutually advantageous basis that will provide the environment for qualifying ASEAN financial institutions to assume more dynamic roles in driving regional financial and economic integration.
v. Establishing a financial sector investor relations platform that will serve as a comprehensive and efficient single point of interface to provide advisory services and information on Malaysia's financial regulatory environment and policy initiatives.

Recommendation 3.1.2

Deepen cross-border coordination and cooperation among regulators to promote the orderly provision of financial services in the region. This will ensure financial stability is preserved while realising efficiency gains from increased activities of Malaysian financial institutions abroad as well as regional and international financial conglomerates in Malaysia. Towards this end, the Bank will undertake the following:

i. Pursue cross-border arrangements with other regulatory authorities with a view to achieve mutual recognition or to promote consistency of prudential and market conduct standards.
ii. Establish regional supervisory networks for home-host cooperation in supervision and crisis prevention, management and resolution.

These strategies are further elaborated in the chapter Regulation and Greater Regional and International Integration.

The more significant presence and activities of Malaysian financial institutions abroad and greater presence of regional and international financial conglomerates in Malaysia require closer cross-border cooperation in financial surveillance, regulation and supervision, and the development of regional financial infrastructure

Recommendation 3.1.3

Establish well-developed financial infrastructure to facilitate increased cross-border financial intermediation, particularly in the area of payments and settlements for cross-border capital flows, trade and retail payments. This includes supporting initiatives at the ASEAN level to accelerate the adoption of a common set of standards on cross-border payments, benchmarked against international best practices and standards, and formulating a common guiding framework for implementation. This will serve to accelerate the integration of payments and settlements systems linkages for the cross-border intermediation of both wholesale and retail funds in the region. Efforts will be focussed on developing the regional infrastructure to reduce the cost of doing business, and enhancing the linkages among regional retail payment networks so as to expand region-wide services, such as cash withdrawals and cross-border electronic funds transfers and payments, to benefit the increasing levels of intra-regional tourism and movement of skilled labour. The initiatives will include:

i. Further expanding the use of local and regional currency payment arrangements on a bilateral basis with strategic regional trading partners.
ii. Developing infrastructure to support the issuance, trading and settlement of securities in international currencies.
iii. Collaborating with regulators in the region to effectively support the private sector in leading regional initiatives, particularly those under the Asian Payment Network.

iv. Intensifying efforts under ASEAN to promote the use of more cost-efficient channels for money remittances while ensuring sufficient safeguards to preserve the integrity of such remittances.

Recommendation 3.1.4

Enhance the position of the Labuan IBFC as a cost-effective and attractive regional operational hub for global corporations and investors to conduct their business in the region. This will involve:

i. Developing the role of the Labuan IBFC to support international trade and investments in specific business niches. This includes:
   - Positioning Labuan IBFC as a centre for captive insurance business by enhancing the Labuan IBFC as a preferred domicile for captives in the Asia-Pacific region.
   - Promoting more international trading and investment holding companies to establish operations in the Labuan IBFC.
   - Encouraging local conglomerates to use Labuan as a platform for outward investments in the region.
   - Promoting the leasing industry in Labuan.
   - Further developing the insurance industry in Labuan, including reinsurance and retakaful.

ii. Improving the ability of businesses in the Labuan IBFC to compete effectively through the creation of a more conducive and facilitative business environment. Initiatives are targeted to harness the business and financial eco-system in Labuan in line with its vision to be Asia's most connected, convenient and cost-efficient international business and financial centre. The initiatives will involve the following:

- Allowing the co-location of Labuan entities to have their physical presence in other parts of Malaysia.
- Strengthen the capabilities of service providers such as insurance managers and trust companies to ensure the highest standards of ancillary services.
- Transform the Labuan International Financial Exchange into an efficient and effective exchange that provides a viable non-ringgit listing and trading platform for financial instruments.
- Promote further business growth in shipping through collaboration with the relevant authorities to encourage ship owners to incorporate their companies in Labuan and to obtain financing and insurance from Labuan-based companies. This is also aimed at boosting the development of the maritime industry in Malaysia by leveraging on the status of Labuan as the sole port of registry for the Malaysia International Ship Registry.
- Enhance incentives accorded to Labuan companies, including those involved in the oil and gas sector, to attract greater investments and in the process, further promote Labuan as a trading, financing and insurance hub.

The liberalisation measures for new foreign participation in the Malaysian financial sector will be implemented when the preconditions are in place to ensure an orderly transition to a more liberalised environment. Meanwhile, efforts to enhance the framework for the effective regulation and supervision of regional financial activities, as well as the financial infrastructure for regional payments and settlements will be undertaken concurrently on an ongoing basis in cooperation with other regulatory authorities in the region.

3.2

internationalisation of
Islamic finance

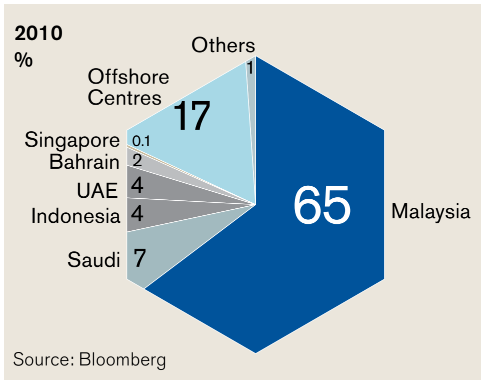
The development of the domestic financial sector moving forward and the strengthening of its international dimension will not only contribute to Malaysia's overall economic growth but also enhance its economic and financial linkages with other emerging economies and the international financial centres. Building on the progress achieved during the Financial Sector Masterplan 2001, Malaysia has developed a progressive and comprehensive Islamic financial system that contributes to the overall effectiveness and efficiency of the Malaysian financial sector.

Several important initiatives implemented to develop the requisite financial infrastructure, regulatory framework and incentive structure, while gradually liberalising the operating environment, have strengthened the Islamic financial system to become increasingly more competitive.

The progressive development of the Islamic financial system in the initial years has led to the launch of the national agenda to position Malaysia as an international Islamic financial centre (MIFC) in 2006. There has been increased interest by the global community in Islamic finance given its close linkage to economic activities and its key pillars of fairness, transparency, risk sharing, and prohibition of excesses and speculation. The MIFC agenda has provided the platform for Malaysia to extend the outreach of Islamic financial services beyond the domestic and regional markets. It has opened the doors for financial institutions to expand their Islamic financial activities by leveraging on the presence of a comprehensive Islamic financial system and supportive environment in Malaysia. Initiatives introduced were in five focus areas, namely sukuk origination and trading, Islamic fund and wealth management, international Islamic banking, international takaful and human capital development.

As a result of the wide ranging initiatives to develop the Islamic financial system in Malaysia, this recent decade has seen the contribution of Islamic finance to the Malaysian economy growing significantly. The Islamic finance value-added to gross domestic product (GDP) has advanced by an average rate of 32% per annum, and contributing a 2.1% share to Malaysia's GDP in 2009, compared to only 0.3% in 2000. This has also translated into greater job creation where employment in Islamic finance contributed 11% of total employment in the financial system. On the international front, Malaysia has evolved to become an international Islamic financial centre. Malaysia ranks highly in various global indices relating to Islamic finance, being the largest sukuk (Islamic bond) market in the world with 65% share (at USD96 billion in 2010) and among the top investment destinations for Islamic funds. In the global takaful sector, Malaysia is the second largest takaful market with 26% share of global takaful assets in 2009 (PricewaterhouseCoopers Gateway to Asia: Malaysia, International Islamic Finance Hub - 2010). As at the end of 2010, Malaysia's takaful market recorded total assets of RM14.7 billion. Foreign participation in the domestic Islamic banking and takaful industry and the Islamic capital market has also been on an increasing trend.

Global sukuk outstanding by country



Malaysia has also supported international efforts towards strengthening the international Islamic financial landscape, encompassing development of international standards and regulatory framework through the Islamic Financial Services Board (IFSB), and talent development through the establishment of a global university, the International Centre for Education in Islamic Finance (INCEIF). A recent important development in the international Islamic financial system was the establishment of the International Islamic Liquidity Management Corporation (IILM) in 2010, to facilitate efficient management of liquidity by Islamic financial institutions in the international financial system. The launch of the Bloomberg-AIBIM-Bursa Malaysia Sovereign Shariah Index (BMSSI) in early 2011 marked another significant milestone in the development of the global sukuk market. This was followed by the launch of the Thomson Reuters IdealRatings Islamic Indices in June 2011 as the first Islamic benchmark

Islamic finance in Malaysia will continue to expand reinforced by the global expansion where creation, preservation and distribution of wealth are effectively undertaken by market participants in a manner that promotes the universal values of Shariah

that offers research-based Shariah screening based on globally accepted standards to investors, money managers and analysts across a range of Islamic instruments.

On the international front, the attention given to Islamic finance by the financial community has increased following the global financial crisis, with particular interest in the prospects, potential role and relevance of Islamic finance in contributing towards global financial stability and more sustainable economic growth. Its adoption of universal ethical values of fairness, transparency and risk sharing has enforced this trend. The demand for Islamic finance is expected to emanate not only from the Muslim population but also from those with affinity for socially responsible objectives and those seeking ethical financial solutions where the central theme is a more equitable model that would foster sustainable growth, whilst preserving the environment and improving the overall socio-economic landscape. This is spurred by the growing significance of global ethical consumer movement where Socially Responsible Investment (SRI) is expected to be an important mainstream asset class by 2015. With this development, Islamic finance has an enhanced growth prospect given its close synergy with ethical finance.

In addition, while Islamic finance has been highly dynamic and innovative in focusing on the provision of financial solutions to the new requirements of the changing economic landscape in the domestic and international economy, it also focuses on the financial inclusion agenda. In this recent period, as its international dimension intensifies, Islamic finance will have a greater role in the intermediation and distribution of wealth across borders particularly among the emerging economies.

Key spectrums of an effective international Islamic financial centre

1. International financial activities

- Breadth & depth of cross-border foreign currency business in banking and retakaful
- High degree of investment mobility
- Wide range of Islamic financial products and services

2. Business enablers

- Business-friendly regulatory environment
- Business facilitation tools (for example standard agreements)
- Accessibility to skilled talent
- Well-informed market

Optimum

3. Diverse & dynamic market participants

- Full range of financial providers
- Strong financial institutions with global presence
- Supporting professional services

4. International financial platforms

- Effective intermediation of liquidity
- Active international exchanges & indices
- Internationally connected clearing system

Moving forward, building from Malaysia's position of strength and the global potential for Islamic finance, it is envisaged that Islamic finance in Malaysia will continue to expand, reinforced by the global expansion where creation, preservation and distribution of wealth are effectively undertaken by market participants in a manner that promotes the universal values of Shariah. This growth and development of Islamic finance will be supported by a dynamic Islamic financial ecosystem that will be conducive for the mobilisation of the increasing volumes of international Islamic financial flows.

To achieve this vision, the Islamic finance industry in Malaysia needs to:

- Effectively and efficiently intermediate cross-border financial flows, through a comprehensive range of innovative Islamic financial instruments offered by a diverse range of players;
- Competitively meet international business demands through the provision of cost-effective foreign currency funding arrangements supported by liquid Islamic financial markets and increased market connectivity;
- Be recognised as a reference centre for Islamic finance with Malaysia as the location of choice for knowledge development and talent management in Islamic finance; and
- Strategically enhance its international profile.

The recommendations outlined in this Blueprint to achieve the above goals will build upon the initiatives currently being implemented. The approach towards greater liberalisation in the Islamic finance industry will also continue to be undertaken to support Malaysia's international Islamic finance agenda while ensuring the overall financial system stability is maintained at all times.

In sustaining its competitive position, Malaysia must continue to provide a conducive environment for the market players, including Islamic financial institutions as well as professional ancilliary service providers in Islamic finance, to conduct their business. Elements such as a conducive tax environment, liberal foreign exchange administration policies, comprehensive infrastructure and strong economic fundamentals will be continuously enhanced.

In this endeavour, the Bank will continue to foster international cooperation as well as collaborate with the relevant ministries and Government agencies, financial regulators, market players in the Malaysian Islamic finance industry, as well as other multilateral agencies and national regulatory authorities to ensure the successful implementation and achievement of the vision for the Islamic finance industry and its increased internationalisation.

Malaysia to continue providing a conducive environment for the market players, including Islamic financial institutions as well as professional ancillary service providers in Islamic finance to conduct their business

Recommendation 3.2.1

Increase the diversity of players in the domestic Islamic finance industry to support a wider range of Islamic financial products and services that serves the best interest of Malaysia, by facilitating greater cross-border financial business and meeting the increasing demands of a wider and greater spectrum of investors and customer base. The ability to tap into growth areas will be enhanced by enabling the presence of new niche players and widen the scope of businesses of existing players. This includes:

i. Issuing new Islamic banking licences to institutions with specialised expertise to support the growth of cross-border wholesale and investment banking activities that will be able to provide a wider range of innovative Islamic financial services.
ii. Expanding the business scope of qualified International Islamic Banks in enhancing their roles to offer a wider range of financial solutions to businesses and contribute towards reducing the cost of cross-border trade and investment transactions.
iii. Issuing new takaful licences to institutions with specialised expertise to provide coverage to serve higher value-added economic activities and widen the provision of protection, in particular for large and specialised risks.

Recommendation 3.2.2

Support the growth of Islamic fund and wealth management industry that can offer innovative financial solutions to meet the more sophisticated investment demands of the increasingly affluent population particularly in Asia and the Middle East, thus positioning Malaysia as a regional and international centre for Islamic fund and wealth management. Efforts in this direction, in collaboration with relevant authorities, include:

i. Supporting international Islamic fund managers to attract greater participation and relocation of talent into the domestic fund management industry.
ii. Providing a conducive environment with appropriate prudential safeguards for Islamic banking players that venture into the following high value-added financial services:
   - asset management and private banking businesses;
   - global fund and administrator services;
   - global cash management business; and
   - trust business.
iii. Supporting the establishment of relevant vehicles for asset and wealth management such as asset managers, trust companies, family offices and foundations in Malaysia, including in the Labuan International Business and Financial Centre (IBFC).
iv. Promoting the wider integration of socially responsible investment principles through Islamic financial institutions.

Enhance liquidity in Islamic financial markets in facilitating more effective and efficient intermediation of cross-border Islamic financial flows

v. Facilitating the establishment of professional ancillary service providers in Malaysia to provide a comprehensive range of services to meet the growing demand in the Islamic finance industry in areas such as wealth advisory, Shariah advisory, legal, taxation and auditing.

Recommendation 3.2.3

Enhance liquidity in Islamic financial markets to facilitate more effective and efficient intermediation of cross-border Islamic financial flows by developing a comprehensive range of innovative Islamic financial instruments that meets the requirements for international liquidity risk management, as well as by enhancing market infrastructure and practices.

This involves enhancing the dynamics of the Islamic money, foreign exchange and capital markets through the development of more innovative Shariah-compliant instruments, which includes:

i. Developing new products to facilitate Islamic repo transactions and unlock captive instruments, thereby re-invigorating activities in the wholesale money market (refer to the chapter Developing Deep and Dynamic Financial Markets).
ii. Expanding the range of globally-accepted Islamic hedging instruments to mitigate market risks and cross-border exposures.
iii. Supporting further the development of real estate investment trusts (REITs) and exchange traded funds (ETFs) for the Islamic capital market.
iv. Encouraging Malaysian issuers to offer foreign currency Islamic capital market investment products by providing attractive tax package for establishing and listing these products in Malaysia.

Recommendation 3.2.4

Increase market efficiency by facilitating the use of standard documents and agreements among financial market players. Such efforts include:

i. Promoting wide adoption of standardised product documentation and practices such as Wakalah Agreement and Commodity Murabahah Master Agreement through bilateral and multilateral agreements between local and foreign financial institutions.
ii. Developing a new set of facilitative standard agreements for financial market instruments based on specific underlying Shariah contracts, for example, Collateralised Murabahah Agreement, to enhance market linkages and efficient transactional activities between financial institutions and corporate sectors, domestically and internationally.

Recommendation 3.2.5

Promote active participation in issuance and trading of sukuk to create an efficient market with well-established information infrastructure and improved liquidity.
This includes:

i. Facilitating regular sukuk issuance by the Government and government-linked companies that will improve the development of a benchmark yield curve as well as enlarge issuers' base in the financial markets.
ii. Issuing equity participation notes by the Government and government-linked companies for project funding which can be subscribed by a wider range of investors.
iii. Promoting larger Islamic investment mandates by Government and government-linked companies, particularly in the foreign currency sukuk issued out of Malaysia.

Recommendation 3.2.6

Enhance the depth and vibrancy of the Islamic financial markets by providing a conducive regulatory and tax environment for onshore issuance of short-term and long-term tradable foreign currency instruments such as Negotiable Islamic Debt Certificates (NIDCs), Islamic Negotiable Instruments of Deposits (INIDs), Islamic Accepted Bills (IABs),

medium-term notes and long-term sukuk by both residents and non-residents. Efforts in this direction include:

i. Recognising qualified foreign currency instruments as liquid assets and eligible collateral to obtain liquidity support from the Bank, subject to identified parameters.
ii. Continuously providing an enabling environment for the issuance of foreign currency Islamic securities.

Recommendation 3.2.7

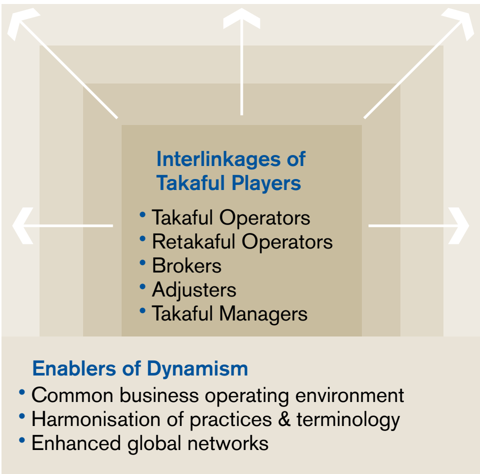
Strengthen the framework for effective and efficient flow of cross-border Islamic financial activities in view of increased cooperation and coordination towards achieving greater market connectivity in Islamic finance globally.

This will include positioning Malaysia, including Labuan IBFC, as an international retakaful centre, with significant presence of takaful and retakaful operators supported by active takaful intermediaries to meet the domestic and global growth in takaful business. Efforts in this direction include:

Strengthen the framework for effective and efficient flow of cross-border Islamic financial activities and heighten global cooperation and coordination

i. Encouraging international players with strong capacity, rating and technical expertise to establish retakaful operations in Malaysia as well as attracting brokers with international linkages to serve the takaful sector.
ii. Encouraging greater involvement of takaful brokers in broadening the range of takaful product offerings and outreach by extending MIFC incentives to such takaful brokerage business activities.
iii. Promoting the use of takaful as a risk management tool in Islamic financial transactions, for instance in Islamic trade finance transactions and sukuk issuances.

Towards enhancing dynamism of takaful interlinkages



Recommendation 3.2.8

Continue to enhance financial linkages between different jurisdictions by undertaking efforts to:

i. Foster and enhance strategic alliances with other jurisdictions through bilateral and multilateral agreements in business and developmental areas of Islamic finance in promoting greater breadth and depth of the Islamic finance industry at the international level.
ii. Encourage greater participation by Islamic banking institutions in offering trade finance facilities to expand cross-border Islamic financial transactions.
iii. Encourage Islamic financial institutions to increase international correspondent banking arrangements to facilitate capital flows in multi-currencies, and better support economic and financial integration in the region.
iv. Support and encourage a regional presence of strong Islamic financial institutions offering basic Islamic financial needs in retail financing and takaful.
v. Leverage on Labuan business structures and institutions to raise funds in multi-currencies in accordance with Shariah principles.

Recommendation 3.2.9

Optimise the potential of existing Islamic financial market platforms to increase cross-border Islamic financial activities. The efforts include:

i. Supporting the International Islamic Liquidity Management Corporation (IILM) and the Bursa Suq Al-Sila' as key infrastructure for liquidity management by providing facilitative business and operating environment to strengthen their value propositions in meeting the demand of global financial community.
ii. Enhancing the visibility of the Malaysian sukuk market amongst the international investors by promoting the inclusion of sukuk on established international indices.
iii. Supporting the development of market indices as a reference and for price quotations of the various classes of Islamic financial assets.
iv. Establishing links with commodity exchanges in other jurisdictions and explore the use of different types of commodities as underlying assets for new Islamic liquidity instruments.
v. Developing Malaysia as an international platform for the listing and trading of a full spectrum of Shariah-compliant asset classes in collaboration with other regulatory agencies.

Recommendation 3.2.10

Develop Malaysia as a reference centre for Islamic financial transactions. To enable this, Malaysia needs to build on the development of human capital in Islamic finance and the establishment of the Shariah, legal, regulatory and supervisory frameworks. This includes:

i. Establishing a single legislated body as the apex authority on Shariah matters for institutions offering Islamic financial services in Malaysia. This is aimed at paving the way to meet the developments in the international Islamic financial markets.
ii. Strengthening the International Shariah Research Academy for Islamic Finance (ISRA) to become a premier international research agency on Islamic finance and Shariah to promote greater harmonisation or mutual recognition of Shariah views on Islamic finance, to support innovation of Islamic financial products and services, and to conduct applied research in areas such as developing a reference benchmark pricing for Islamic financial transactions.
iii. Developing Shariah Parameters to serve as the reference point across jurisdictions for the development of Islamic financial products and services by clarifying the principles and basis of the underlying Shariah contracts for the various Islamic financial transactions.

Develop Malaysia as a reference centre for Islamic financial transactions and reaffirm the country's position in Islamic finance education and training

iv. Gaining international recognition for the Association of Shariah Advisors (ASAS) as the body responsible for enhancing qualification and professionalism of Shariah advisors, locally and internationally.

v. Developing the Malaysian legal system to be recognised for international Islamic financial transactions by strengthening the legal framework to ensure effective enforceability of Islamic financial transactions and activities. This includes efforts to:

- Review the existing laws applicable to Islamic financial transactions by the recently established Law Harmonisation Committee (LHC) and, where necessary, amendments will be proposed to strengthen legal support to Islamic financial transactions.
- Enhance the capacity of the Kuala Lumpur Regional Centre for Arbitration (KLRCA) to effectively and efficiently arbitrate both domestic and international Islamic finance disputes.

vi. Strengthening the regulatory and supervisory framework for international Islamic finance by continuing to have an active role in supporting the efforts undertaken by international Islamic finance organisations such as the Islamic Financial Services Board (IFSB), IILM, the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), International Islamic Financial Market (IIFM) and the Islamic Development Bank (IDB) in the development of Islamic finance.

Recommendation 3.2.11

Enhance Islamic finance knowledge propositions to further strengthen Malaysia's position in Islamic finance education and training. This will also be supported by a comprehensive talent development programme catering to the various segments to meet the growing demand for Islamic finance professionals that are critical to research and innovation efforts especially in the areas of Shariah and product development. The initiatives include:

i. Promoting standards and the accreditation of Islamic finance programmes by the Islamic finance industry (refer to the chapter Talent Development to Support a More Dynamic Financial Sector).

ii. Supporting the introduction of structured training programmes for relevant stakeholders, for example, the judges and lawyers, through the industry's collaborative efforts with the relevant authorities in facilitating understanding of the specificities of Islamic finance.

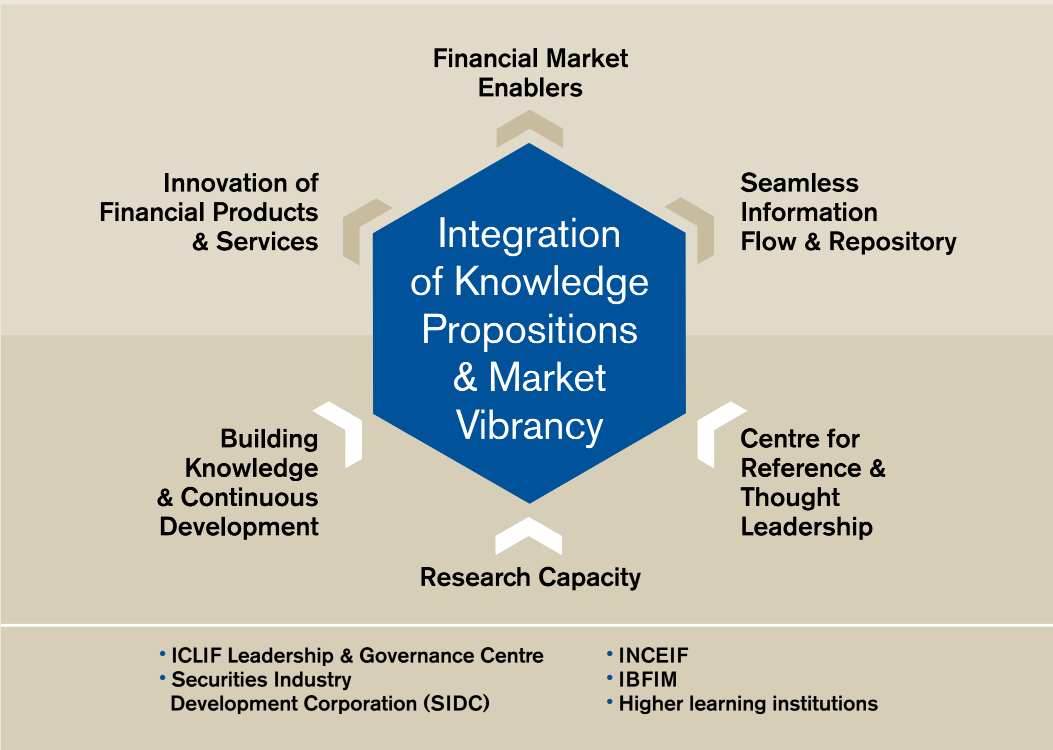
iii. Introducing dedicated training programmes to prepare Shariah graduates for careers in the Islamic finance industry. This will be pursued as a joint effort between the industry, training institutions and regulators.

Recommendation 3.2.12

Promote greater global engagement and alliances in the development of the Islamic finance industry to increase Malaysia's business connection and collaboration with other financial centres towards enhancing our financial and economic linkages with other parts of the world. This includes efforts to:

i. Establish information flows in Islamic finance to build greater regional and global connectivity by continuing to collaborate with the private sectors in organising meetings and

Synergistic impact of knowledge propositions & market vibrancy



conferences, intellectual discourse and debates to create understanding and awareness on Islamic finance and other opportunities to support seamless cross-border information flows.

ii. Encourage public-private sector collaboration and intensify networking between Malaysia and other financial centres for business opportunity matching.

The recommendations collectively promote enhancing varying value propositions of Islamic finance and Malaysia as an international Islamic financial centre. In the immediate to medium term, the implementation of the recommendations will focus on enhancing the capacity of financial institutions, improving market liquidity and connectivity, thus stimulating cross-border market activities. Incumbent Islamic financial institutions are expected to have greater business focus and increased financial resilience to bring the industry to a new level and to meet new competition. In the medium to longer term, issuance of specialised licences will be introduced to allow new entrants into the Islamic finance industry to address gaps in certain Islamic banking and takaful business segments. Ongoing efforts throughout the Blueprint period will be accorded towards developing thought leadership in Shariah matters and in talent development for the industry to drive the internationalisation agenda and thus strengthen the international financial and economic linkages, in particular among the emerging economies and with the traditional international financial centres.

4

Safeguarding the stability of the financial system

responsive

responsible

A regulatory and supervisory regime

that effectively maintains the stability of the financial system and soundness of financial institutions is necessary for sustainable growth and the orderly development of the financial sector.

Significant attention has been directed over the recent decade towards strengthening the effectiveness of the regulatory regime, in line with leading standards and practices, and providing an enhanced focus on governance practices and risk management. The implementation of the Basel II capital adequacy rules for banking institutions in 2008 and the Risk-Based Capital Framework for insurers in 2009 have aligned regulatory requirements to the specific risk profiles and circumstances of individual financial institutions.

Strengthened corporate governance, risk management and disclosure standards have engendered prudent risk taking, while a risk-based approach to supervision and a pre-emptive intervention framework have supported comprehensive risk assessments and mitigation of risks to ensure the soundness and stability of financial institutions and the financial system. Pre-emptive responses to address risks in the financial system have ensured continued confidence and have minimised any disruption to the financial intermediation process during the recent global financial crisis. The enactment of the Central Bank of Malaysia Act 2009 has further reinforced the foundations for financial stability in Malaysia by enabling the Bank to respond more effectively to potential threats to the stability of the financial system.

Going forward, the regulatory and supervisory regime will continue to focus on safeguarding the stability of the overall financial system, including key market infrastructure; further strengthening the resilience of individual financial intermediaries; sustaining the Bank's ability to effectively regulate and supervise financial institutions on an ongoing basis; and promoting responsible and fair dealings towards financial consumers with due regard to financial stability. In doing so, key trends affecting the financial landscape will need to be taken into consideration, including:

- The increasing size and complexity of financial institutions, with higher levels of financial innovation;
- Continued evolution of financial institutions towards financial conglomeration;
- A more competitive and vibrant operating environment;
- A greater role of development financial institutions (DFIs) in financial inclusion;

- The growing significance of Islamic finance and its trend toward greater internationalisation; and
- The greater diversity of players in the Malaysian financial system, with cross-border linkages, a significant overseas presence of Malaysian financial institutions and greater participation of foreign financial institutions in Malaysia.

The recommendations will therefore focus on ensuring the continued effectiveness of the regulatory and supervisory regime that includes:

- Ensuring that potential risks to financial stability in the new financial landscape continue to be addressed through timely and appropriate policy measures;
- Raising the standards of corporate governance, risk management and control functions; and
- Establishing a regulatory and supervisory environment appropriate for a more regionally- and internationally-connected financial sector.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'09
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'11

4.1

the regulatory and supervisory regime

The regulatory and supervisory regime, including institutional arrangements, will be further developed to address potential risks to financial stability that may emerge from the evolving financial landscape. This will involve enhancing the legislative framework to promote a consistent approach to regulation and supervision across the financial sector; support a more risk-based approach to regulation and supervision; strengthen the Bank's capacity to manage risks associated with financial intermediation activities that occur outside the banking system (such as non-bank credit and financial intermediation activities); and provide enhanced powers for the Bank to take timely intervention actions to deal effectively with vulnerable institutions in the interest of depositors, insurance policyholders and takaful participants.

Recommendation 4.1.1

Enact a comprehensive legislative framework for the conventional and Islamic financial systems respectively. The proposed legislation will reinforce a sound, transparent, and accountable system for effective regulation and supervision that is consolidated across the banking, insurance, takaful, financial intermediary and payment system services sectors.

Recommendation 4.1.2

Review regulations on the ownership structures of licensed financial institutions to encourage the participation and long-term commitment of strong institutional shareholders while preserving appropriate safeguards to promote the safety and soundness of financial institutions. This includes:

i. Allowing greater flexibility on the maximum permitted shareholdings by institutions and cross-shareholdings in financial institutions, with a view of allowing greater flexibility for shareholders that meet suitability requirements which are appropriate with the level of interest held in the financial institution. Such flexibility in shareholding structures should not unduly amplify the inter-connectedness within the Malaysian financial system, create excessive industry concentration, or undermine competition in the financial sector.

ii. Strengthening and enhancing the transparency of suitability criteria for significant controlling interests in financial institutions. This will include factors such as the ability of prospective shareholders to provide continuing financial support to the financial institution; their character, integrity, business record and experience; and whether their group structures or activities impede effective supervision and undermine financial stability. In addition, controllers will also be expected to demonstrate the soundness of their plans for the financial institution's business. To ensure the suitability of all persons exercising material influence over financial institutions, including those that may not necessarily hold direct equity positions, the notions of "interest" and "control" will also be further clarified and enhanced.

Recommendation 4.1.3

Strengthen the supervisory oversight over financial holding companies to avert risks to the safety and soundness of licensed financial institutions that may emanate from other entities within financial groups. Accordingly, financial holding companies will be subject to appropriate prudential regulations with a greater level of supervisory oversight. This will be achieved mainly through:

i. The formal authorisation of financial holding companies, which will include requirements for financial holding companies to meet relevant suitability criteria and demonstrate capabilities for ensuring prudent management over financial groups.
ii. More transparent group structures and appropriate limits on the nature and scope of non-financially-related activities to ensure that depositors, insurance policyholders and takaful participants are not exposed to excessive risk and leverage.
iii. Requirements for financial groups to comply with prudential standards, including on corporate governance, risk management, capital and liquidity to ensure effective risk management and soundness of operations of groups.
iv. Appropriate powers for the Bank to examine, request information and implement supervisory interventions in financial groups.

A comprehensive legislative framework will be enacted to reinforce a sound, transparent and accountable system for effective regulation and supervision

Recommendation 4.1.4

Strengthen the institutional structure of financial institutions to provide adequate safeguards for depositors, insurance policyholders and takaful participants against contagion risks and excessive leverage. This will be achieved through:

i. Implementing measures to ensure that retail deposits are not excessively leveraged by banking institutions in high-risk and complex activities. This includes requirements for high-risk activities to be conducted out of investment banking or specialised entities, along with other safeguards to maintain effective ring-fencing of retail deposits such as limitations or prudential requirements governing intra-group transactions and the sharing of operational infrastructure.
ii. Requiring life and general businesses of insurers, and family and general business of takaful operators to be carried out under separate entities due to the different risk characteristics and nature of these businesses. Transition arrangements will be put in place to allow for an orderly segregation of businesses by existing composite insurers and takaful operators.

Recommendation 4.1.5

Promote the long-term sustainability and enhanced capacity of DFIs in support of their mandates. This will include:

i. Enhancing the risk-sharing and accountability arrangements between the DFIs and the Government.
ii. Introducing specific measures to further strengthen the corporate governance and risk management of DFIs so as to secure their self-sufficiency in funding and capital.

Recommendation 4.1.6

Implement the Basel III reform package to promote a more resilient Malaysian banking system. The standards will be implemented in Malaysia in phases, beginning 2013 until 2019, in line with the globally-agreed implementation timeline. This will include:

i. Raising the quality of capital held by banking institutions, while also creating incentives for banking institutions to build up capital buffers that can be drawn down in times of stress. The enhancements to the capital standards will also consider the risk profile of banking institutions and the nature of their operations including cross-border activities and investments, as well as the offering or trading of exotic products.
ii. Strengthening the liquidity standards of banking institutions by enhancing the existing liquidity framework in Malaysia, while also introducing incentives for banking institutions to tap stable long-term funding.

Implementation of the global standards will also carefully consider the operating environment in order to avoid unintended consequences. This will also include addressing structural issues such as the dominant role of institutional funds in mobilising household savings and the limited availability of high-quality liquid assets, particularly those which are Shariah-compliant. In overcoming these implementation challenges, the Bank will also encourage the development of solutions by the industry and cooperate with other agencies to formulate an appropriate regulatory framework for new instruments that will support banking institutions' compliance with the new standards.

Recommendation 4.1.7

Strengthen the regulatory and supervisory framework of the Labuan International Business and Financial Centre (IBFC) in line with international standards and best practices. This includes:

i. Enhancing the capital standards for Labuan financial institutions in tandem with their growing sophistication and the development of other established financial centres. A risk-based capital model will be implemented for Labuan banking, and insurance and takaful sectors. The minimum statutory and paid-up capital of Labuan financial institutions will also be progressively increased.
ii. Strengthening corporate governance and risk management practices of Labuan financial

institutions and other service providers with a focus on strengthening the oversight functions of financial institutions, and promoting sound management of credit, market, operational, liquidity and other risks.

Recommendation 4.1.8

Develop a framework for monitoring and managing risks arising from entities and activities taking place outside the directly supervised financial system. This will include:

i. Enhancing data collection and surveillance of such entities and activities, particularly those of systemic importance.
ii. Implementing appropriate regulatory responses to pre-emptively manage emerging risks. Where relevant, these will be employed in coordination with other authorities.

Recommendation 4.1.9

Enhance the institutional arrangements for effective and orderly resolution of distressed financial institutions through enhancing the role of the Malaysia Deposit Insurance Corporation (PIDM) as a resolution authority for dealing in an orderly manner with large, non-viable financial institutions in Malaysia that can affect financial stability. Recognising the expertise and capabilities being developed within PIDM to undertake the resolution of member institutions, PIDM is well positioned to facilitate the resolution of a wider range of financial institutions in Malaysia including non-member institutions. This will be supported by appropriate accountability and financial arrangements to ensure the effective coordination between the Bank and PIDM as well as with other relevant authorities within and outside Malaysia.

Recommendation 4.1.10

Enhance the framework for financial crime prevention and investigation to preserve the integrity of the financial system. This takes into consideration the increasing sophistication of the nature and methods for perpetrating financial crimes, which necessitates more coordinated mechanisms for effective prevention, investigation and prosecution of financial crimes. In the near term, existing inter-agency coordination mechanisms will be enhanced with a view to consider more fundamental reforms to the institutional and legal framework to address financial crimes in the future. Given the more regionally- and internationally-connected financial sector moving forward, particular focus will also be directed at strengthening arrangements for cross-border collaboration in financial crime investigation.


Value
markets
market
innovation
reach
relative

4.2

raising the standards of governance and risk management

The increased size and complexity of the financial services industry in the emerging landscape will require standards of governance and risk management in financial institutions, as well as the role of market discipline, to be further strengthened to ensure effective oversight and prudent management of risks.

Recommendation 4.2.1

Strengthen the corporate governance of financial institutions and the role of market discipline in ensuring effective oversight over financial institutions. Specific measures that will be pursued include:

i. Requiring disclosures of periodic audits of corporate governance and Shariah governance so that shareholders and other stakeholders better understand whether disclosed governance policies and procedures are reflected in actual practice.
ii. Codifying in law the functions of boards and responsibilities of individual directors, with emphasis on the need for directors to give due regard to the interest of depositors, insurance policyholders and takaful participants.
iii. Supporting the development of a pool of independent directors to facilitate board succession and renewal. The pool, which will be established under the Financial Institutions Directors' Education (FIDE) Programme within the ICLIF Leadership and Governance Centre, will be developed through a systematic process of identifying, training and profiling potential candidates for new appointments in financial institutions.
iv. Elevating the role of company secretaries that support the effective functioning of boards, including improving board interactions with management. For this purpose, the roles and responsibilities of company secretaries in financial institutions will be more clearly defined, and suitability criteria introduced to ensure that company secretaries have the necessary skills, competencies and experience to perform their duties and responsibilities effectively.
v. Continue developing a suitable complement of education programmes for directors of financial institutions under the FIDE initiative.

Recommendation 4.2.2

Raise the standards of risk management and internal control functions across the financial sector in line with developments in the financial services industry. This will include:

i. Enhancing risk management standards to address new and potential risks which may emerge from evolving industry practices and changes in the operating environment, including the expansion of market-based financial activities and instruments; the greater interdependencies arising from shared functions and services within financial groups; the more dynamic pricing of insurance and takaful products and more liberalised rules on expense management for insurers.
ii. Requiring insurers and takaful operators to be served by independent and dedicated heads of risk and observe higher standards for risk management systems and processes, in line with their growing significance and importance in the financial sector. The role of actuaries and their interactions with key control functions will also be reviewed, with further clarification on the roles of actuaries in life insurers and family takaful operators, and a more prominent role for actuaries in general insurers and general takaful operators.
iii. Introducing specific risk management standards for microlenders to ensure sustainable practices and that institutional safety and soundness is maintained, while also avoiding the emergence of predatory lending practices as financial inclusion further deepens in Malaysia.

Corporate governance of financial institutions and the role of market discipline will be further strengthened to ensure effective oversight of financial institutions and prudent management of risks

Recommendation 4.2.3

Strengthen the foundations for a sound risk culture in the financial sector. A strong risk culture that promotes prudent risk taking and the long-term viability of financial institutions will become more important in the future financial landscape which is expected to be more diverse and competitive. This will be advanced through:

i. Implementing measures to promote more risk-aligned executive compensation.
ii. Developing codes and practices, and training programmes that support a sound risk culture.

4.3

regulation and greater regional and international integration

The integration of the Malaysian financial system with the global financial system will further intensify as it plays a greater role in the intermediation of cross-border funds. Accordingly, the promotion of a regulatory and supervisory environment that is appropriate for a more regionally-and internationally-connected financial sector will be a key priority moving forward.

Home-host coordination arrangements, particularly with central banks and supervisory authorities within the region, will be strengthened to ensure the orderly expansion of Malaysian financial institutions overseas, and the entry of new foreign financial institutions in the domestic financial sector, as well as in the Labuan IBFC. These will seek to ensure that cross-border financial linkages foster regional growth in a manner that does not propagate systemic risk across borders.

Recommendation 4.3.1

Collaborate with other central banks and supervisory authorities to safeguard the stability of a regionally- and internationally-connected financial sector. This will include:

i. Achieving greater consistency in the principles of regulation and supervision across jurisdictions within the region. Strategic collaboration and cooperation initiatives will be pursued to build capacity and support the raising of standards across jurisdictions, with the view of promoting greater harmonisation of principles and mutual recognition of standards in the long run.
ii. Establishing channels for the timely exchange of information between supervisory authorities to support the effective supervision of cross-border institutions, financial system surveillance, and crisis prevention, management and resolution. This includes the establishment and more active role of supervisory colleges for the supervision of regionally- and internationally-active financial institutions.
iii. Strengthening liquidity safety nets to support more efficient cross-border provision of liquidity to markets and institutions in times of stress through bilateral and multilateral arrangements, which include the implementation of cross-border collateral and currency swap arrangements with other central banks within the region.

Recommendation 4.3.2

Participate in greater cross-border arrangements and supervisory cooperation to support the orderly development of an international Islamic finance industry. This will include:

i. Accelerating the development of a more robust infrastructure to support more efficient liquidity management.
ii. Implementing prudential standards, risk management and Shariah governance practices.

These efforts will be pursued by leveraging on existing bilateral and multilateral initiatives within the region, including ASEAN, ASEAN+3 and the Executives' Meeting of East Asia-Pacific (EMEAP) Central Banks, as well as through international Islamic financial organisations such as the Islamic Financial Services Board (IFSB).

The Bank will seek to promote a regulatory and supervisory environment that ensures the orderly expansion of Malaysian financial institutions overseas and the entry of new foreign financial institutions into Malaysia

The immediate to medium term focus will be on efforts to reinforce the foundations for effective regulation and supervision, particularly with respect to strengthening the preconditions and creating an enabling environment to support the implementation of various recommendations under the Blueprint. This will include making necessary enhancements to the legislative framework, strengthening supervisory capacity, as well as enhancing coordination arrangements with other supervisory authorities within and outside Malaysia. Meanwhile, more fundamental reforms and enhancements that will be necessary to safeguard financial stability in response to the evolving financial landscape will be implemented in the medium to longer term. Attention will also be directed at continuously raising the standards of corporate governance, risk management and control functions.

5

Key enablers for the development of the financial system

proactive

productive


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e-banking

5.1

electronic payments

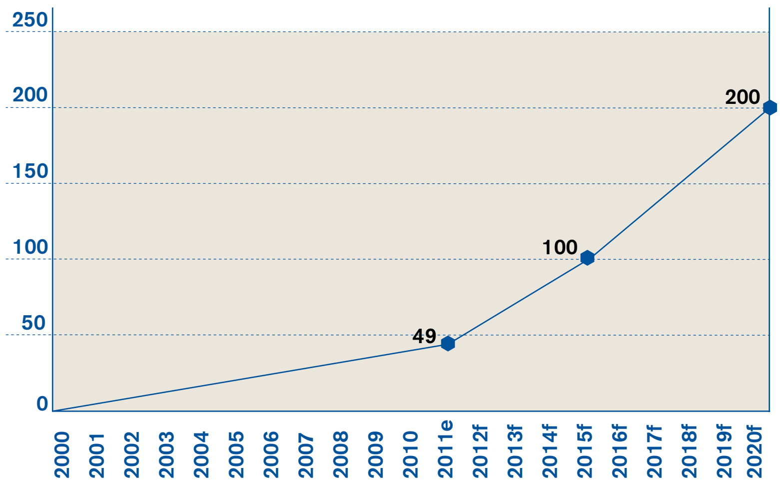
for greater economic efficiency

The payment system is a critical component of the economic and financial infrastructure of a country. It has a pivotal role in facilitating the circulation of money in the economy, and enabling the conduct of trade, commerce and other economic activities. Having a payment system that facilitates the efficient movement of funds is therefore highly important for financial development and the growth of the economy.

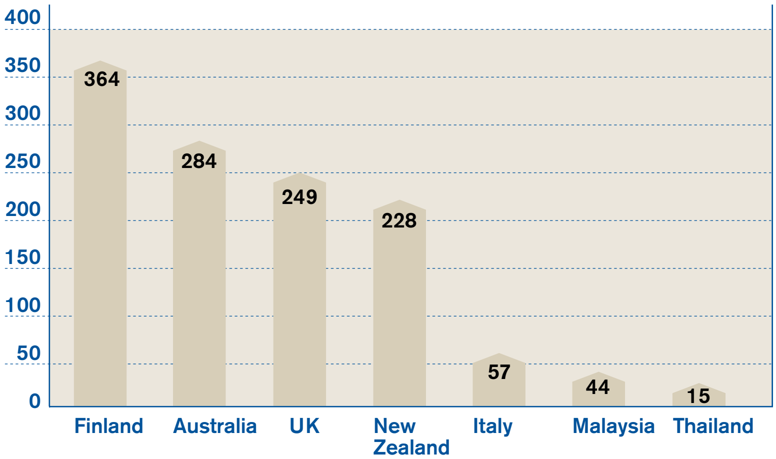
Electronic payments (e-payments), which offers a more expedient, secure and cost-effective means of moving funds over paper-based payments, is one of the strategic tools for achieving greater economic efficiency, productivity and growth as Malaysia transitions towards a high value-added, high-income economy. Increasing the offering and adoption of e-payments would allow businesses and society at large to enjoy greater convenience and higher operational efficiency from expedient payments and receipts of funds. This in turn contributes towards improving the competitiveness of the economy and the quality of life of its citizens. The benefits of migrating to e-payments are not only limited to financial efficiency gains as it also promotes a more eco-friendly environment.

In this recent decade, the Bank's efforts reinforced by developments in technology and innovation have led the transformation of the payments landscape towards greater offerings and the adoption of e-payment products and services. The Bank has been a driver for the greater adoption of e-payments and has coordinated efforts in Malaysia to achieve this agenda. This includes engaging with several economic sectors and the Government to facilitate their transition to e-payments. The Bank had also collaborated with several central banks in the region

E-payment transactions per capita



E-payment transactions per capita in 2010



to improve the efficiency of retail payments and facilitate linkages between the Malaysian Electronic Payment System Sdn. Bhd. (MEPS) shared Automated Teller Machine (ATM) network with shared ATM networks in Singapore, Indonesia, Thailand, Korea and the People's Republic of China. The growth in e-payments has been encouraging since embarking on this agenda, with notable growth registered across all e-payment methods. E-payments usage per capita doubled from 22 in 2005 to 44 in 2010, with substantial growth in the usage of debit cards which increased by 8.2 times, Internet banking by 6.3 times and Interbank GIRO by 4.5 times.

In the next 10 years, the Bank aims to increase the number of e-payment transactions per capita from 44 transactions in 2010 to 200 transactions by the end of 2020, which is comparable to the e-payment transactions per capita of the more developed countries. The vision is to make e-payments the preferred medium for economic transactions in Malaysia. The achievement of this vision will be through the creation of a vibrant and conducive environment which provides the incentives for greater usage and provision of e-payment products and services. This will require new and bold measures and the commitment by all stakeholders to transform the Malaysian payments system to one that is highly efficient in terms of speed, security, convenience and cost.

In the next 10 years, the Bank aims to increase the number of e-payment transactions per capita from 44 transactions in 2010 to 200 transactions by the end of 2020

The cost and inefficiencies associated with manual paper-based payments should be significantly reduced. As markets become more open and integrated, the need to allocate and utilise resources more efficiently and reduce costs is crucial in order to remain internationally competitive. A highly resilient and efficient national payments system is a major impetus towards a high value-added, high-income economy.

Moving forward, the Bank's payment subsidiary, Malaysian Electronic Clearing Corporation Sdn. Bhd. (MyClear), which was established to spearhead the e-payments agenda, will take a leading role in elevating the migration to e-payments agenda to the next level. The Bank will continue to provide the necessary regulatory environment to drive the migration to e-payments agenda, enhance efficiency including initiatives that will derive cost savings for the country as a whole and contribute to the payment system stability. One of the initiatives that is currently being implemented is the local switching, clearing and settlement of domestic payment card transactions. Efforts to accelerate the migration to e-payments, however, also require a high level of collaboration and cooperation among all payment system stakeholders including payment service providers, corporate users, consumers, the Government and other regulators to improve the entire payment process and drive changes in payment behaviour.

The Bank will promote a fair and healthy level of competition in the retail payments space. The adoption of international standards will improve interoperability, security and operational efficiency of the payment infrastructure. At the same time, the Bank recognises that achieving economies of scale in certain payment sectors is important to generate the desired cost efficiency. This has been demonstrated in several countries where it is more cost efficient and effective for just one player or a small number of players to co-exist in certain sectors, for example in the transportation sector. Often, these are sectors where a massive capital outlay is required to build the necessary infrastructure. Limited competition would avoid such duplication of systems and resources. It would:

- Result in a more efficient allocation of resources and contribute towards increasing the efficiency and productivity in the overall economy; and
- Lead to greater convenience for consumers and bring other social benefits to the economy.

The limited competition would be subject to a competitive and transparent process. Close oversight and regulatory prescriptions would also ensure that there is no anti-competitive behaviour which could be to the detriment of consumers or the public at large. Of paramount importance would be to ensure the safety, security and reliability of the payment services are maintained and the business model is sustainable, efficient and fair, particularly in terms of pricing and access.

In addition, the focus of priorities in the next ten years would include improving cross-border payments and settlements. Linkages between large value payment systems and retail payment systems would be developed and enhanced in support of ASEAN financial integration.

Recommendation 5.1.1

Enhance the e-payments infrastructure by introducing improvements and new services that will significantly improve user convenience and access to payment services to further facilitate the adoption of e-payments. This includes:

i. Widening access to the Real-time Electronic Transfer of Funds and Securities (RENTAS) system via electronic channels (e-channels) such as Internet banking to promote the use of e-payments for large value transactions.
ii. Adopting international messaging standards for the RENTAS system that would facilitate Malaysian banks and corporates to achieve greater straight-through-processing and lower infrastructure cost by streamlining treasury processing for domestic and regional operations.

iii. Facilitating efficient reconciliation of electronic transactions by providing adequate payment information to beneficiaries.
iv. Providing a mechanism to facilitate payment assurance and timely information of rejections for unsuccessful electronic transactions.
v. Introduce rules in collaboration with financial institutions for faster and more standardised crediting of funds for e-payments. This will benefit merchants through reduced risks and improved cash flow.
vi. Facilitating higher transaction limits via e-channels by leveraging on initiatives such as mobile public key infrastructure (mPKI). This will promote the use of e-channels as a more viable payment alternative to cheques.

Recommendation 5.1.2

Enhance the mobile banking channel by driving the adoption of the mobile phone as a simple and convenient channel to conduct banking and payment transactions, by encouraging greater participation of financial service providers and merchants in the mobile banking and payments ecosystem[1]. Efforts would be taken to ensure payments can be made and received easily and at affordable charges. Other features and new value-added services will be introduced to promote the safety of the mobile channel and enhance user convenience as follows:

i. Implementation of a strong and secure authentication method that is simple and cost-effective, such as mPKI to instill user confidence in mobile banking and payments.
ii. Introduction of the Electronic Bills Payment Portal to offer consumers and billers the efficiency and convenience of having one portal to pay all their bills from various channels.
iii. Leveraging on Near Field Communication (NFC) technology to offer convenient mobile payment services.

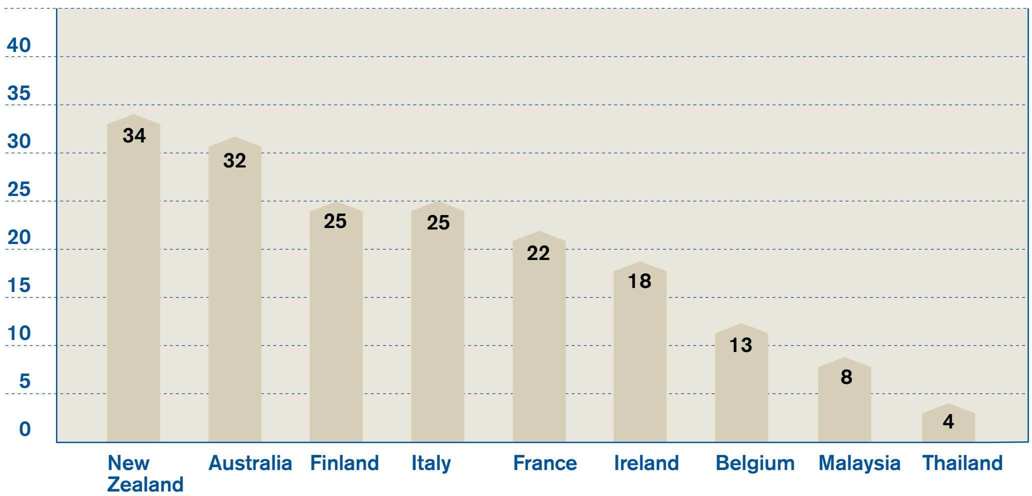
[1] Mobile banking and payments ecosystem is a multi-bank and mobile network operator neutral ecosystem that offers a standard mobile banking application and a common security standard.

Recommendation 5.1.3

Widen the payment card infrastructure with the aim of increasing the use of debit cards from 0.6 transactions per capita in 2010 to 30 transactions per capita by 2020. Initiatives will include:

i. Increasing the number of point-of-sale (POS) terminals that accept payment cards from 8 terminals per 1,000 inhabitants in 2010 to 25 terminals per 1,000 inhabitants by 2020 by accelerating the deployment of POS terminals, including at smaller merchants. In countries with high e-payments per capita, the widely available POS terminals contributed to the high usage of payment cards and the reduction in the use of cash.
ii. Instituting an incentive structure that would encourage the use of debit cards.
iii. Facilitating the deployment of standalone POS terminals at smaller merchants.
iv. Widening the acceptance of the domestic PIN-based debit card or e-Debit among merchants.

Number of EFTPOS terminals per 1,000 inhabitants in 2010



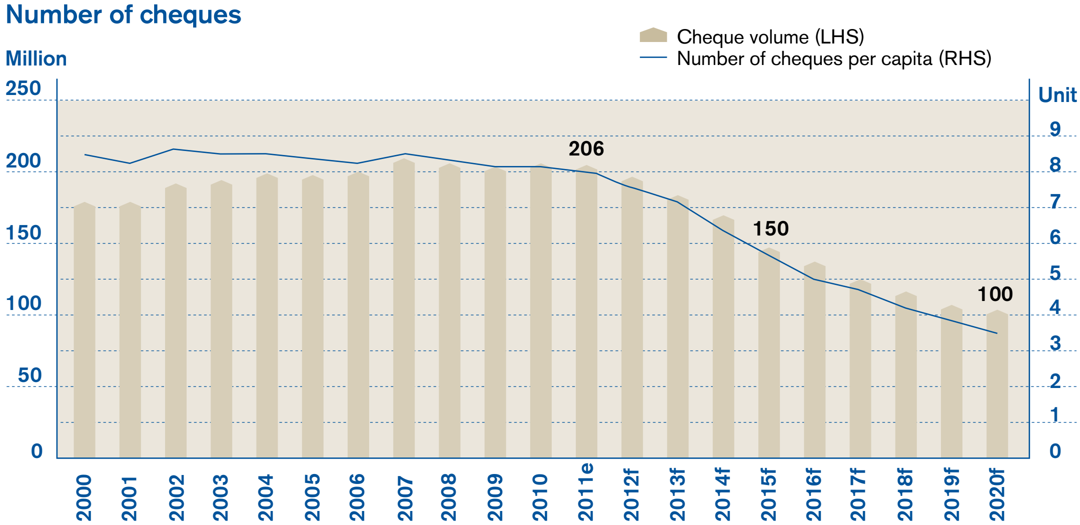
Recommendation 5.1.4

Promote a conducive pricing structure for payment services that facilitates the use of more cost effective payment methods and undertake appropriate measures to reduce the use of cheques from 207 million in 2010 to 100 million by 2020.

Various international studies have shown that e-payment transactions cost between one-third to one-half that of paper-based instruments. The cost savings that a country can potentially gain is about 1% of its GDP annually by switching fully from paper-based payments to e-payments. The survey amongst banks in Malaysia on the cost of paper-based payments and e-payments yielded similar results. The cost savings and efficiency gains from the migration to e-payments would enhance the nation's competitiveness. The current price distortion that

The cost savings that a country can potentially gain is about 1% of its GDP annually by switching fully from paper-based payments to e-payments

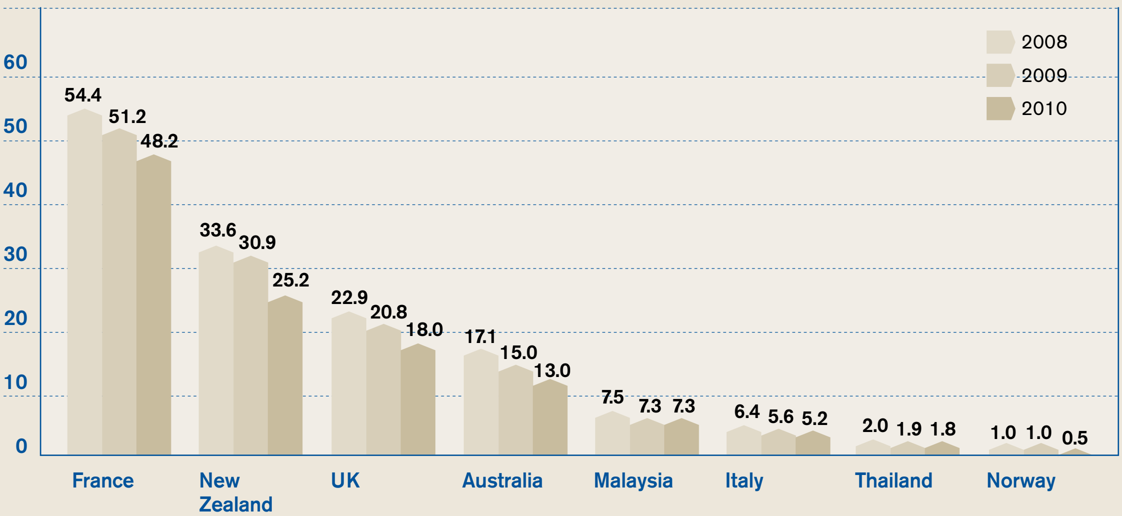
Number of cheques



exists between e-payments and paper-based payment instruments therefore has to be removed. Payment service providers need to provide the right price signals to encourage users to switch from the more expensive payment methods to lower cost alternatives. The following initiatives will be undertaken to promote the migration from the use of cheques to the more cost-effective payment methods:

i. Allow charges to be imposed on cheques to reflect its higher cost, while lowering the price of e-payments. Charges imposed on cheques should however not be prohibitive while e-payment services must be enhanced to ensure they are readily accessible, convenient and not costly to use.
ii. Banking institutions to introduce cost-efficient banking products that promote the use of e-payments and discourage the use of cheques.
iii. Support efforts by the Government and private corporations to reduce the use and acceptance of cheques.
iv. Explore the introduction of tax incentives to encourage the desired behavioral changes and complement the new pricing structure for payment services.

Number of cheques per capita in 2010



Recommendation 5.1.5

Enhance awareness and promote user confidence in using e-payments to encourage higher usage of e-payments, as awareness and confidence are very crucial components to ensure the success of the e-payment agenda. This will be undertaken through:

i. Establishing a one-stop information portal dedicated to promote e-payments that provides useful information for consumers as well as businesses such as e-payment mechanisms available, the benefits of e-payments and tips to ensure the safety of transactions.
ii. Increasing promotional campaigns such as road shows and exhibitions in collaboration with industry and trade associations.

Implementation of the initiatives for the migration to e-payments will be conducted in stages. In the immediate to medium term, efforts will be focused more on enhancing and expanding the existing e-payments infrastructure to provide alternatives to paper-based payment instruments. The next stage will involve reviewing the incentive structure for e-payments by rolling out more aggressive pricing strategies and promotional campaigns to achieve the vision of e-payments becoming the preferred medium for economic transactions. Measures will also be introduced throughout the ten year period to build awareness and influence behavioral change and to build public confidence in e-payments and thus accelerate the migration to e-payments.

Payment service providers need to provide the right price signals to encourage users to switch from the more expensive payment methods to lower cost alternatives

5.2

empowering consumers

In an environment of greater globalisation, advances in technology coupled with the intensification of competition in the financial sector, and the changes taking place in consumers' behaviour, a comprehensive and holistic approach towards consumer protection and education is essential. Over the recent decade, financial consumer protection and education has received greater recognition as having an important role in contributing towards a sound, stable and competitive financial sector.

International reform efforts which have focused on strengthening the institutional framework and infrastructure for consumer protection and enhancing financial literacy have gained significant momentum.

On the domestic front, a multi-pronged approach has been adopted to ensure that the continued growth of the financial sector is underpinned by fair and responsible market practices and conduct, and that consumers are better equipped with the necessary financial knowledge to make informed decisions. Several consumer protection initiatives have been undertaken to this effect such as the strengthening of business conduct regulations applicable to financial service providers and the establishment of comprehensive institutional arrangements for dealing with consumer enquiries, complaints and redress. This includes requiring the setting up of customer contact centres at the financial service providers in addition to the Bank Negara Malaysia Laman Informasi Nasihat dan Khidmat (BNMLINK), the Financial Mediation Bureau (FMB) and the Agensi Kaunseling Dan Pengurusan Kredit (AKPK). These initiatives are complemented by a comprehensive financial literacy programme set to enhance the financial capability of consumers.

Over the recent decade, financial consumer protection and education has received greater recognition as having an important role in contributing towards a sound, stable and competitive financial sector

As Malaysia transitions towards a high value-added, high-income economy, the financial sector will become more competitive with a greater diversity of intermediaries and delivery channels. In addition, there will be increased innovative and complex financial products and services being offered to meet the different consumer demands and profiles. In this environment, strengthening the financial capability of

consumers will continue to be an important priority so as to support well informed, effective and responsible financial decisions. This will be pursued in parallel with equal attention to ensuring that the financial service providers conduct their business with integrity. The effective collaboration and continued commitment and support of relevant stakeholders such as Government agencies, regulatory agencies, consumer groups and non-governmental organisations will also become increasingly important.

Promoting a culture of mutual responsibility by consumers and financial service providers will entail the following:

- Consumers who are empowered with knowledge, skills and tools to build, manage and protect their personal wealth;
- Financial service providers which embrace a culture of fair and responsible dealings in the conduct of their business;

The effective collaboration and continued commitment and support of relevant stakeholders such as Government agencies, regulatory agencies, consumer groups and non-governmental organisations will also become increasingly important

- Enabling infrastructures to ensure sustainable and effective implementation of financial education initiatives;
- Effective and efficient redress mechanisms for financial products and services;
- Enhanced credit information infrastructure to promote a responsible credit culture amongst borrowers and lenders; and
- Effective and holistic institutional and legal framework for consumer protection and financial literacy.

The recommendations in this Blueprint for greater empowerment to consumers in the financial sector aim to strengthen the framework for financial consumer protection and financial literacy at the national level to better align and coordinate initiatives for consumer protection and financial literacy among key stakeholders in a more holistic manner.

Recommendation 5.2.1

Promote financial capability as an essential life skill from an early age through the integration of financial education into the formal curriculum at schools and higher learning institutions. The priority areas include:

i. Integrating important aspects of financial education in selected key subjects in the curriculum covering basic money management, spending and savings, credit and debts, e-payments, financial risk management and consumer responsibilities.

ii. Enhancing the knowledge and skills of teachers in the formal school system to effectively deliver financial education to students of different ages.

iii. Developing a programme to encourage the opening of deposit accounts with the aim of inculcating a savings culture at an early age and providing basic money management skills.

Recommendation 5.2.2

Adopt a life events approach to the development and delivery of programmes and encourage greater collaboration among stakeholders in delivering financial education. This includes:

i. Implementing targeted financial capability programmes focusing on specific life events that influence the lifestyle and behaviour of consumers, which would also alter their financial commitments. Key events include the pursuit of education, purchasing a first car or home, starting a first job, getting married, raising a family and retirement. This will supplement the Pengurusan Wang Ringgit Anda (POWER!) Programme developed for first-time borrowers and aims collectively to reach out to consumers with information that is tailored to their specific circumstances.

ii. Leveraging on strategic partnerships with Government agencies, non-governmental organisations, religious authorities, local councils and employers in providing financial education to expand the outreach to all segments of society. This envisages the intensification of training of trainers programmes to deliver effective financial education to identified target groups.

iii. Increasing the use of technology to enhance the reach, flexibility and effectiveness in the delivery of financial education. This will also enable the development of new and improved toolkits for financial planning and management.

iv. Enhancing the roles of financial service providers and industry associations in supporting the financial literacy initiatives by pooling resources and coordinating activities more optimally.

AKPK will have an important role as the lead agency in spearheading financial education initiatives that target adult consumers.

Recommendation 5.2.3

Introduce a cohesive regulatory regime that addresses regulatory gaps and is consistently enforced with the establishment of a committee of relevant authorities to formulate and operationalise a new consumer credit law. While consumer credit activities in Malaysia are currently subjected to a number of legislation including the Banking and Financial Institutions Act 1989, the Hire-Purchase Act 1967, the Pawnbrokers Act 1972 and the Moneylenders Act 1951,

Agensi Kaunseling Dan Pengurusan Kredit will have an important role as the lead agency in spearheading financial education initiatives that target adult consumers there are pockets of credit activity which are currently not subject to any legislative requirement. The consumer credit law to be enacted in Malaysia would provide for a comprehensive and consistent supervision and regulation of credit activities by the respective authorities. The consumer credit law should be flexible and responsive to challenges confronting consumers and will provide greater clarity in consumer protection and market oversight in the consumer credit market.

Recommendation 5.2.4

Establish the Financial Ombudsman Services (FOS) Scheme with expanded powers to promote the effective and fair handling of disputes with financial service providers. This includes:

i. Transforming the existing FMB into the FOS that will be backed by legislation.
ii. Expanding the scope of the FMB to cover a wider range of disputes against financial service providers.
iii. Collaborating with other regulatory agencies to facilitate the move towards an integrated dispute resolution scheme for the resolution of disputes with all financial service providers.

Recommendation 5.2.5

Promote the wider utilisation of credit reports to encourage a more responsible credit and repayment culture. The credit reports will source credit-related information from various sources that will provide an overall assessment on the consumer's financial health and credit behaviour to avoid over-indebtedness. Efforts will therefore be undertaken as follows:

i. Facilitating the sharing of financial and credit information between the Central Credit Reference Information System (CCRIS) and other approved credit reporting agencies to produce credit reports which comprehensively reflect the consumers' repayment capability.

ii. Broadening the range of information collected by authorised credit reporting agencies to include credit information from non-bank financial institutions, telecommunication companies and utilities and other relevant sources which could enhance the assessment of individual consumers' financial health and their repayment potential.
iii. Promoting convenient and efficient access to timely, informative and user-friendly credit reports by financial service providers and financial consumers.

Recommendation 5.2.6

Strengthen the enabling infrastructure by providing comprehensive access to financial education information and introducing a mechanism to gauge the financial capability of consumers and enhancing the effectiveness of the implementation of financial education initiatives. In this regard, the following initiatives will be undertaken:

i. Introduce a single interface to facilitate access by the public to financial education information, consumer alerts, tips for achieving a healthy financial lifestyle, financial tools, learning modules and resources, research, articles and news provided by different agencies. This single interface will display financial education content from the relevant agencies' websites into one portal and hence, reduce the need for financial consumers to perform multi-point navigation for financial advice and information.
ii. Establish an assessment framework to regularly monitor and measure the financial capability of consumers. This entails undertaking a baseline evaluation to be followed by periodic assessments to track progress in the level of awareness, knowledge, skill, attitude and behaviour of consumers in making sound financial decisions. Results of the assessment will also support the development and implementation of the financial literacy initiatives.

Recommendation 5.2.7

Promote and reinforce fair and responsible practices among financial service providers through appropriate regulation and enhanced transparency. Greater emphasis will be placed on transparency as well as strengthening the governance and internal controls of the financial service providers to ensure responsible practices in their dealings with consumers. In particular, greater expectations will be placed on the Board and senior management of such financial service providers in setting the right culture, policies and incentive systems that are aligned with and support fair and responsible business practices. All this will enhance the image of financial service providers as being fair and responsible institutions and as consumers become more knowledgeable and empowered, financial service providers that embrace fair dealings will be in a better position to build confidence and trust to meet consumers' demands and remain competitive. In this regard, the efforts will include:

Greater emphasis will be placed on transparency as well as strengthening the governance and internal controls of the financial service providers to ensure responsible practices in their dealings with consumers

i. Promoting the publication of customer charters by all financial service providers and implement processes for measuring performance against the published charters. These measures are expected to generate long-term benefits for consumers who can exercise their right of choice among the service providers. The increased competition will also raise the bar for transparent and responsible business conduct, and enhance the quality in the provision of financial solutions.
ii. Intensify supervisory reviews of practices by financial service providers to reinforce fair dealings towards consumers.
iii. Review current barriers to the portability of financial products and services, and the extent to which they have or may potentially harm consumers.

These efforts will be supported with the further strengthening of regulatory laws in respect of the regulation and supervision of the business conduct of financial service providers. The framework will provide explicit requirements with regard to business conduct, including prohibition on misleading or deceptive conduct, false or misleading representation and undue harassment, as well as enhancing the enforcement powers.

The implementation of the recommendations will be guided by two broad phases. The first phase will be implemented in the immediate to medium term and will focus on engaging with the stakeholders to develop a coordinated national strategy for consumer protection and financial literacy. Concurrently, steps will also be undertaken to strengthen the enabling arrangements for financial education. Measures to promote greater transparency and fair dealings among financial service providers will also be pursued during the first phase of the implementation. The second phase will involve the implementation of the initiatives outlined in the national strategy.


INNOVATION
PLAN
SUCCESS

5.3

talent development to support a more dynamic financial sector

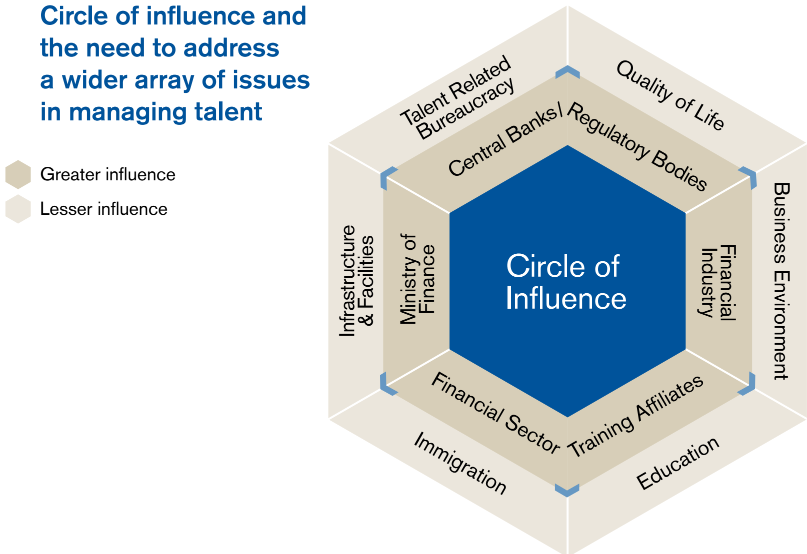
The successful implementation of the initiatives outlined in the Blueprint hinges on the availability of a pool of skilled talent that are able to drive the development of the financial sector in the next decade. With the growth of the financial sector anticipated to be between 8-11% annually leading to an increased contribution of the financial sector to about 10-12% of nominal GDP in 2020 (2010: 8.6%), and given the envisioned transformation of the financial sector, there will be an even greater demand for high-quality talent by the financial sector.

It is anticipated that over the next ten years, the financial sector will require a workforce of about 200,000, which is an increase of 56,000 from the current 144,000 employees. This increase will be underpinned by strong demand across the financial sector, including for specialised skills in high growth and niche areas such as risk capital financing, wealth management, Shariah advisory, corporate finance and investment advisory services. With greater regional financial integration, the skill sets needed for the financial sector will also need to correspond with developments in the region. For instance, the increasing role and prominence of the regional foreign exchange market will require specialised skill sets in managing foreign exchange and multi-currency transactions. Similarly for the Labuan International Business and Financial Centre (Labuan IBFC), talent is needed in financial advisory, insurance management and underwriting, and specialised lending for the transport and oil and gas industries. Equally important is the talent for the ancillary services needed to support the financial sector.

Going forward, efforts to develop talent for the financial industry will therefore need to be comprehensive and holistic taking into account ongoing and future trends. This includes the challenges of a multi-generational workforce and increasing mobility of labour both across borders and industries. At the same time, given that there is a wider range of issues in talent development which is outside the scope of the financial sector, it will require greater collaboration and coordination with relevant agencies in particular between the industry, the regulators, the Government and academia (refer to chart on the circle of influence). Financial sector talent development therefore

Over the next ten years, the financial sector will require a workforce of about 200,000, which is an increase of 56,000 from the current 144,000 employees will need to focus on developing talent for the entry level, promoting continuous learning of the existing human capital in the industry, attracting talent from abroad and fostering a cohesive collaborative arrangement to further advance the domestic talent development agenda.

Circle of influence and the need to address a wider array of issues in managing talent



The talent development initiatives for the next decade can build on the existing comprehensive steps that have been taken in this recent decade to develop financial services professionals across the various levels, from the entry level for graduates to the leadership level for senior management and board of directors. These initiatives as summarised in the chart on established institutions for talent development, provide an enabling platform from which further institutional and infrastructure arrangements for the development of human capital in the industry can be made moving forward. Taking into account the extensive institutional infrastructure that has been put in place and the future needs of the financial sector, the vision moving forward is to ensure a steady stream of competent and capable talent pool for a dynamic and innovative financial sector.

Established institutions for talent development agenda within the financial sector

Different development platforms at different stages of talent development

Entry Level

Financial Sector Talent Enrichment Programme

- Training for top graduates to provide foundation of the financial services industry

Asian Institute of Finance

- Enhance human capital development in the financial sector

Institute of Bankers Malaysia

- Training provider for banking institutions

Malaysian Insurance Institute

- Education & training provider in areas of insurance & financial services

Islamic Banking and Finance Institute Malaysia

- One-stop Islamic finance reference centre for the industry & academia

International Centre for Education in Islamic Finance

- Build talent & skills in Islamic finance for practitioners & graduate programmes

International Shariah Research Academy

- Promote applied research in Shariah & Islamic finance

Securities Industry Development Corporation

- Capital markets education, training & information resource provider in ASEAN

Leadership

ICLIF Leadership & Governance Centre

- Training for senior management in strategic & leadership management
- Financial Institutions Directors' Education Program

Recommendation 5.3.1

Produce more industry-ready entry-level graduates through enhanced collaboration and coordination between the financial industry and institutions of higher learning to ensure seamless transition of graduates into the financial industry workforce.
Initiatives include:

i. Establishing formal working arrangements between the industry and institutions of higher learning in developing structured programmes for graduates to develop and enhance their skills required for employment in the financial industry.
ii. Embedding the contents of the Financial Sector Talent Enrichment Programme (FSTEP), that has been designed to prepare graduates for the financial industry, into the curriculum and syllabus in institutions of higher learning so as to better equip graduates to become industry-ready upon graduation. FSTEP will be gradually phased out once efforts to produce industry-ready graduates are achieved.

Recommendation 5.3.2

Upgrading the skills and competencies of the existing workforce to ensure they are able to meet the changing needs of the financial industry as it undertakes higher value-added services moving forward and to enable them to perform in a more competitive and globalised environment. This includes:

i. Developing certification of the skills level or competencies required for the key functions and positions within the financial sector.
ii. Providing wider opportunities for and easy access to distance learning and self-learning programmes. To successfully implement this, it is proposed that strong collaborative arrangements be put in place to bring together training providers, institutions of higher learning and professional bodies.
iii. Enhancing the overall content and quality of training programmes offered by training providers, including by Institute of Bankers Malaysia (IBBM), the Malaysian Insurance Institute and the Islamic Banking and Finance Institute Malaysia, by:
   - Leveraging on the expertise and experience of industry practitioners, particularly leading financial institutions to contribute towards enhancing the training programmes.
   - Ensuring the oversight of the quality of the training and learning being conducted for the industry.
iv. Ensuring accreditation of programmes offered by the training institute affiliates of the Asian Institute of Finance (AIF) to meet the standards and requirements stipulated in AIF's Learning Programme Assessment and Accreditation Framework.

v. Setting standards for professional programmes and qualifications in Islamic finance that meet the standards set by the Association of Chartered Islamic Finance Professionals (ACIFP), a professional body responsible for global quality standards for Islamic finance professionals.
vi. Ensuring sufficient funding of education for educators for the financial sector.

Recommendation 5.3.3

Attract regional and international talent by facilitating entry into the domestic financial sector workforce. Initiatives include:

i. Effectively communicating the recruitment opportunities in the Malaysian financial sector through the launch of a web portal to profile Malaysia's financial sector as a destination for international and regional talent. The website will provide information on career opportunities in the Malaysian financial sector and other relevant information such as immigration procedures, work permits, housing information, and international schools.
ii. Simplifying of procedures for temporary or permanent international skilled migration to the financial sector.
iii. Instituting collaborative arrangements with TalentCorp to leverage on existing incentive programmes for skilled professionals entering the financial sector.
iv. Fostering partnerships with internationally renowned training providers and universities in advancing the education agenda for the financial sector in Malaysia.
v. Promoting collaborative financial sector research on issues important for the industry.

Recommendation 5.3.4

Foster greater strategic focus, coordination and collaboration to achieve a comprehensive approach to talent development for the financial sector by adopting policies, strategies and oversight to address the issues relating to raising the standards and supply of talent for the financial sector. It is recommended that a Financial Services Talent Council (FSTC) be established to drive, oversee and coordinate the financial sector talent development agenda and further outline its developmental strategies. Members of the Council will be from the industry, regulatory agencies, tertiary academic institutions, government ministries, and thought leaders. The FSTC will coordinate the sector's efforts relating to its talent development requirements and collaborate with the relevant agencies and authorities to advance talent development in a continuous and sustainable manner. The roles of the Council will include:

- Fostering and driving collaboration and coordination among industry players, regulators, educators and the Government in identifying ways to ensure the availability of high quality and experienced talent for the Malaysian financial sector;
- Formulating broad policies and strategies to facilitate the overall development of talent in the financial sector;
- Driving and overseeing implementation of approved policies and strategies; and
- Commissioning comprehensive periodic studies and assessments of talent needs and gaps in the Malaysian financial sector.

Recognising the importance of having a continuous supply of skilled talent to drive the development of the financial sector moving forward, the implementation of the talent development initiatives will commence immediately and concurrently. In the immediate term, the focus will be on establishing the FSTC and its secretariat. Initiatives to produce industry-ready entry-level graduates, upgrading the skills and competencies of the existing workforce and drawing talent from abroad will all need to be pursued concurrently. Transformation of the education opportunities for the financial sector will need to be aggressively pursued during the early part of the plan period.

A Financial Services Talent Council (FSTC) will be established to drive, oversee and coordinate the financial sector talent development agenda

List of recommendations

decisive

definitive

2.1 Effective intermediation for a high value-added and high-income economy

2.2 Developing deep and dynamic financial markets

2.3 Financial inclusion for greater shared prosperity

3.1 Strengthening regional and international financial integration

3.2 Internationalisation of Islamic finance

4.1 The regulatory and supervisory regime

4.2 Raising the standards of governance and risk management

4.3 Regulation and greater regional and international integration

5.1 Electronic payments for greater economic efficiency

5.2 Empowering consumers

5.3 Talent development to support a more dynamic financial sector

2.1 Effective intermediation for a high value-added and high-income economy

2.1.1 Enhance the financial sector's capability to support high value-added activities, including the financial needs of innovative enterprises throughout the lifecycle

i. Enhance the role of financial institutions in developing profit- and risk-sharing investment and financing facilities subject to safeguards
ii. Promote the offering of factoring and leasing by financial institutions and development financial institutions
iii. Promote the full range of financing by development financial institutions to targeted strategic sectors
iv. Promote market-based alternatives for more effective access to funding
v. Promote the development of expertise to support new growth areas such as green technology and the adoption of sustainable financing practices

2.1.2 Increase the supply of a broad range of private risk capital funding across all stages of financing by collaborating with the Government and other agencies

i. Promote the establishment of funds of funds that invest in the venture capital industry and incentivise investments in innovative start-ups
ii. Facilitate the establishment of new institutions with specialised expertise to provide risk capital financing

2.1.3 Enhance the capacity of the financial sector to support the financing needs of large-scale projects with long gestation periods

i. Encourage strategic partnerships between domestic and foreign financial institutions specialising in long-term project financing
ii. Promote the regionalisation of qualified Malaysian financial institutions to participate in the effective mobilisation and allocation of regional capital
iii. Support the establishment of new institutions with specialised expertise in structuring large and long-term financing
iv. Strengthen risk assessment and management capabilities of insurers and institutional investors to assess viability of long-term projects

2.1.4 Strengthen financial institutions' knowledge of different markets to support internationalisation of Malaysian businesses

i. Establish strategic partnerships with foreign counterparts to facilitate greater information exchange
ii. Establish a platform for information exchange on financial products and services and other relevant information
iii. Facilitate more significant presence and participation of qualified Malaysian financial institutions abroad

2.1.5 Promote a conducive environment for financial institutions to develop more products and enhance services for businesses to better manage business risks

i. Promote the development and offering of foreign currency products and services to meet the demands of businesses
ii. Promote the development and offering of political risk insurance to ensure adequate protection for Malaysian businesses that expand abroad
iii. Accord greater flexibility for qualified insurance companies to underwrite surety bonds and provide credit guarantee insurance
iv. Facilitate greater injection of foreign expertise in the insurance and takaful broking and loss adjusting industries to better support insurance and takaful business

2.1.6 Improve access to information to reduce information asymmetries and enhance the effectiveness and efficiency of financial intermediation

i. Strengthen the credit information framework to facilitate more comprehensive financial assessments of borrowers
ii. Establish a technology advisory facility to strengthen assessment of knowledge- and technology-based proposals by financial institutions
iii. Set up an integrated platform to allow investors to network with entrepreneurs and explore investment opportunities

2.1.7 Develop a vibrant private pension industry to enhance Malaysians' financial preparedness for retirement and old age

i. Develop a supporting infrastructure and regulatory framework for the development and offering of pension products by insurers and banks
ii. Develop incentives to spur the development of the private pension industry by insurers and banks in collaboration with the Government
iii. Promote greater consumer education and the adoption of simple and comprehensible product disclosure and transparency standards for pension products
iv. Strengthen the financial safety net for pension products to promote confidence and predictability of the expected retirement income levels
v. Implement appropriate regulatory parameters applicable to pension products to safeguard their ability to fulfill financial needs at retirement

2.1.8 Enhance the provision of wealth management products and services to cater to the demands of the growing affluent segment of the community in collaboration with relevant regulatory agencies

i. Streamline the dual licensing regime for financial advisers and financial planners
ii. Encourage the establishment of family offices to accommodate the demands of ultra high net worth individuals and families
iii. Promote Islamic fund and wealth management activities through the offering of innovative financial solutions
iv. Enhance the development of important ancillary services that support the wealth management industry
v. Facilitate internationally-established financial institutions in the Labuan IBFC to offer services through foundations and private trust companies

2.1.9 Enhance the capacity and capability of the insurance and takaful industry to provide higher value-added medical and health insurance

i. Encourage insurers and takaful operators to offer higher-end insurance products to complement the national health financing scheme
ii. Encourage strategic alliances between domestic and foreign financial institutions with specialised expertise in medical and health insurance

2.1.10 Introduce greater operational flexibility for financial institutions subject to appropriate safeguards

i. Gradually remove restrictions for locally-incorporated foreign banking institutions to establish non-branch delivery channels
ii. Accord greater flexibility for locally-incorporated foreign banking institutions to establish physical branches subject to meeting stipulated criteria
iii. Encourage insurers and takaful operators to enhance offering of insurance products through alternative delivery channels
iv. Allow locally-incorporated foreign banking institutions to conduct hire purchase business

2.1.11 Enhance service quality in the provision of financial services and the conduct of business by financial institutions

i. Develop market-based mechanisms and training programmes to enhance service quality in the financial sector
ii. Implement transparent service quality measurements

2.2 Developing deep and dynamic financial markets

2.2.1 Promote an efficient and competitive money market with greater depth and liquidity

i. Promote greater volume of securities, collateralised transactions and repo transactions
ii. Allow qualified corporations to directly participate in the wholesale money market and expand the intermediary roles of money market brokers
iii. Liberalise non-resident participation in the onshore interest rate derivatives market and encourage greater use of interest rate derivatives by market players
iv. Promote equity based (including hybrid) instruments and establish a hedging mechanism/platform for Islamic banks

2.2.2 Deepen liquidity in the government debt securities and sukuk markets

i. Increase the issuance frequency of government benchmark securities across the yield curve
ii. Facilitate active buy-back or conversion of the off-the-run government securities
iii. Enlarge the issuance size of government treasury bills
iv. Introduce long-term and index-linked securities, promote innovative Shariah compliant securities and issue securities in regional currencies

2.2.3 Broaden the investor base for the government securities market

i. Explore cost-effective investment and distribution channels for direct retail participation
ii. Collaborate with regional countries to develop a regional principal dealers' framework

2.2.4 Enhance avenues for risk management and instruments to manage risk exposures

i. Provide further flexibilities to Principal Dealers in undertaking short-selling activities
ii. Broaden the scope of Guidelines on Securities Borrowing and Lending Programme to allow non Principal Dealers to borrow and lend securities
iii. Enhance the mechanism and infrastructure that facilitate securities-driven repo transactions
iv. Structure government securities issuances to support the design and specification of government securities futures contracts

2.2.5 Enhance access and improve liquidity in the foreign exchange market

i. Allow corporations to actively manage foreign currency exposures arising from their overseas operations
ii. Permit institutional funds and retail investors to trade in foreign currencies subject to suitable safeguards
iii. Allow financial institutions to offer internet and electronic trading platform for corporations and retail investors
iv. Permit participation by non-residents in the onshore foreign exchange derivatives market without underlying trades or investments, subject to safeguards

2.2.6 Support the use of regional currencies for trade settlement and direct investment activities

i. Encourage financial institutions to provide direct foreign exchange cross quotations with both onshore and offshore counterparties
ii. Allow financial institutions to quote ringgit crosses to residents and non-residents
iii. Promote Malaysia as a centre for regional treasury operations for home-grown resident and foreign multinational corporations

2.2.7 Develop infrastructure and arrangements for efficient and cost effective foreign currency trading, payments and settlements onshore

i. Promote a common network infrastructure
ii. Create an e-trading platform for regional currencies for cost-effective offering of cross-border financial products and services
iii. Appoint a Self Regulatory Organisation to elevate professionalism in the foreign exchange market

2.3 Financial inclusion for greater shared prosperity

2.3.1 Adopt innovative channels to enhance the outreach of quality and affordable financial services in a more cost-efficient manner

i. Develop a comprehensive agent banking framework to enable outreach of financial services at lower costs
ii. Accelerate the roll-out of innovative delivery channels, including mobile banking

2.3.2 Expand the range of products and services that will meet the distinct financial needs of all citizens, including the underserved

i. Encourage flexible micro financing products that enable prompt drawdown of financing in times of need and prepayment of financing during good times
ii. Enhance provision of long-term contractual micro-savings products with low committed periodical savings and favourable returns
iii. Facilitate the insurance/takaful industry to develop affordable microinsurance/microtakaful products for protection against unexpected adverse events

2.3.3 Strengthen institutional arrangements to provide financial services to the underserved and build capacity of practitioners to support this in an effective and sustainable manner

i. Strengthen the financial inclusion role of specialised development financial institutions
ii. Encourage financial training providers to offer structured financial inclusion training
iii. Enhance monitoring framework for the outcomes of financial inclusion initiatives

2.3.4 Enhance the knowledge and capacity of the underserved to utilise financial services responsibly

i. Improve the provision of advisory services to increase the income generating capability of micro enterprises
ii. Enhance the role and outreach of Mobile LINK and the collaboration with consumer associations

3.1 Strengthening regional and international financial integration

3.1.1 Promote greater foreign participation in the financial sector under a strategic and managed approach that serves the best interest of Malaysia

i. Issue new licences to financial institutions with specialised expertise
ii. Accord more flexible foreign equity participation in financial institutions
iii. Provide greater flexibility for onshore financial institutions to establish new delivery channels
iv. Advance collective initiatives that support regional economic integration under the ASEAN Economic Community
v. Establish a financial sector investor relations platform that will serve as a comprehensive and efficient single point of interface

3.1.2 Deepen cross-border coordination and cooperation among regulators to promote orderly provision of financial services in the region

i. Pursue cross-border arrangements with regulators for mutual recognition or to promote consistency of prudential and market conduct standards
ii. Establish regional supervisory networks for home-host cooperation in supervision and crisis prevention, management and resolution

3.1.3 Establish well-developed financial infrastructure to facilitate increased cross-border financial intermediation

i. Expand the use of local and regional currency payment arrangements on a bilateral basis with strategic regional trading partners
ii. Develop infrastructure to support the issuance, trading and settlement of securities in international currencies
iii. Collaborate with regulators to support the private sector in leading regional initiatives particularly under the Asian Payment Network
iv. Intensify efforts under ASEAN to promote the use of more cost-efficient channels for money remittances

3.1.4 Enhance the position of Labuan IBFC as a cost-effective and attractive regional operational hub for global corporations and investors

i. Develop the role of Labuan IBFC to support international trade and investments in specific business niches
ii. Improve the competitive ability of businesses in Labuan IBFC through the creation of a more conducive and facilitative business environment

3.2 Internationalisation of Islamic finance

3.2.1 Increase the diversity of players in the domestic Islamic financial industry to support a wider range of financial products and services that serves the best interest of Malaysia

i. Issue new Islamic banking licences to institutions with specialised expertise
ii. Expand the business scope of qualified International Islamic Banks
iii. Issue new takaful licences to institutions with specialised expertise

3.2.2 Support the growth of the Islamic fund and wealth management industry in collaboration with relevant authorities

i. Support international Islamic fund managers to attract greater participation and relocation of talent into the domestic industry
ii. Provide a conducive environment with appropriate prudential safeguards for Islamic banking players that venture into high value-added financial services
iii. Support the establishment of relevant vehicles for asset and wealth management
iv. Promote the wider integration of socially responsible investment principles through Islamic financial institutions
v. Facilitate the establishment of professional ancillary service providers in Malaysia to provide a comprehensive range of services

3.2.3 Enhance the dynamics of the Islamic money, foreign exchange and capital markets

i. Develop new products to facilitate Islamic repo transactions and unlock captive instruments
ii. Expand the range of globally-accepted Islamic hedging instruments
iii. Support the development of real estate investment trusts (REITs) and exchange traded funds (ETFs)
iv. Encourage Malaysian issuers to offer foreign currency Islamic capital market investment products

3.2.4 Increase market efficiency by facilitating the use of standard documents and agreements among financial market players

i. Promote wide adoption of standardised product documentation and practices
ii. Develop a new set of facilitative standard agreements for financial market instruments

3.2.5 Promote active participation in issuance and trading of sukuk

i. Facilitate regular sukuk issuance by the Government and government-linked companies
ii. Issue equity participation notes by the Government and government-linked companies for project funding
iii. Promote larger Islamic investment mandates by Government and government-linked companies

3.2.6 Enhance the depth and vibrancy of the Islamic financial markets by providing a conducive regulatory and tax environment

i. Recognise qualified foreign currency instruments as liquid assets and eligible collateral for liquidity support
ii. Continue to provide the enabling environment for the issuance of foreign currency Islamic securities

3.2.7 Position Malaysia including Labuan IBFC as an international retakaful centre

i. Encourage international players to establish retakaful operations in Malaysia and brokers with international linkages to serve the takaful sector
ii. Encourage greater involvement of takaful brokers to broaden the range of takaful product offerings and outreach by extending MIFC incentives
iii. Promote the use of takaful as a risk management tool in Islamic financial transactions

3.2.8 Continue to enhance financial linkages between different jurisdictions

i. Foster and enhance strategic alliances with other jurisdictions
ii. Encourage greater participation by Islamic banking institutions in offering trade finance facilities
iii. Encourage Islamic financial institutions to increase international correspondent banking arrangements
iv. Support and encourage a regional presence of strong Islamic financial institutions
v. Leverage on Labuan business structures and institutions to raise funds in multi-currencies

3.2.9 Optimise the potential of existing Islamic financial market platforms

i. Support IILM and Bursa Suq Al-Sila' as key infrastructure for liquidity management
ii. Promote the inclusion of sukuk on established international indices
iii. Support the development of market indices as a reference and for price quotations of the various classes of Islamic financial assets
iv. Establish links with commodity exchanges in other jurisdictions and explore the use of different types of commodities as underlying assets
v. Develop Malaysia as an international platform for the listing and trading of Shariah-compliant asset classes in collaboration with other regulatory agencies

3.2.10 Develop Malaysia as a reference centre for Islamic financial transactions

i. Establish a single legislated body as the apex authority on Shariah matters
ii. Strengthen ISRA to become a premier international research agency on Islamic finance and Shariah
iii. Develop Shariah Parameters to serve as the reference point across jurisdictions for the development of Islamic financial products and services
iv. Gain international recognition for the Association of Shariah Advisors
v. Develop the Malaysian legal system to be recognised for international Islamic finance transactions
vi. Strengthen the regulatory and supervisory framework for international Islamic finance

3.2.11 Enhance Islamic finance knowledge propositions supported by a comprehensive talent development programme

i. Promote standards and the accreditation of Islamic finance programmes for the Islamic financial industry
ii. Support the introduction of structured training programmes to facilitate the understanding of the specificities of Islamic finance
iii. Introduce dedicated training programmes to prepare Shariah graduates for careers in Islamic finance

3.2.12 Promote greater global engagement and alliances in the development of the Islamic finance industry

i. Establish information flows in Islamic finance to build greater regional and global connectivity
ii. Encourage public-private sector collaboration and intensify networking between Malaysia and other financial centres

4.1 The regulatory and supervisory regime

4.1.1 Enactment of a comprehensive legislative framework for the conventional and Islamic financial systems

4.1.2 Review regulations on the ownership structures of licensed financial institutions

i. Allow greater flexibility on the maximum permitted shareholdings by institutions and cross-shareholdings in financial institutions
ii. Strengthen and enhance transparency of suitability criteria for significant controlling interests in financial institutions

4.1.3 Strengthen the supervisory oversight over financial holding companies

i. Introduce formal authorisation of financial holding companies
ii. Enhance transparency of group structures with appropriate limits on the nature and scope of non-financial-related activities
iii. Strengthen requirements for financial groups to comply with prudential standards
iv. Enhance powers of the Bank to examine, request information and implement supervisory interventions for financial groups

4.1.4 Strengthen the institutional structure of financial institutions to provide adequate safeguards against contagion risk and excessive leverage

i. Enhance safeguards for retail customers of banking institutions against risks associated with increasingly complex activities
ii. Require life and general businesses of insurers, and family and general businesses of takaful operators to be carried out under separate entities

4.1.5 Promote the long-term sustainability and enhanced capacity of DFIs in support of their mandates

i. Enhance risk-sharing and accountability arrangements between DFIs and the Government
ii. Strengthen the corporate governance and risk management of DFIs

4.1.6 Implement the Basel III reform package to strengthen the capital and liquidity buffers held by banking institutions

4.1.7 Strengthen the regulatory and supervisory framework of the Labuan IBFC

i. Enhance the capital standards for Labuan financial institutions
ii. Strengthen corporate governance and risk management practices of Labuan financial institutions and other service providers

4.1.8 Develop a framework for monitoring and managing risks arising from non-regulated entities and activities

i. Enhance data collection and surveillance of entities and activities outside the supervised financial system
ii. Implement appropriate regulatory responses to pre-emptively manage emerging risks

4.1.9 Enhance the role of PIDM as a resolution authority in the financial system

4.1.10 Enhance the framework for financial crime prevention and investigation

4.2 Raising the standards of governance and risk management

4.2.1 Strengthen the corporate governance of financial institutions and the role of market discipline

i. Require disclosures of periodic audits of corporate governance and Shariah governance
ii. Codify in law the functions of boards and responsibilities of individual directors
iii. Support the development of a pool of independent directors to facilitate board succession and renewal
iv. Elevate the role of company secretaries that support the effective functioning of boards
v. Develop a suitable complement of education programmes for directors under the Financial Institution Directors' Education initiative

4.2.2 Raise the standards of risk management and internal control functions across the financial sector

i. Enhance risk management standards to address new potential risks
ii. Require insurers and takaful operators to be served by independent and dedicated heads of risk
iii. Introduce risk management standards for microlenders

4.2.3 Strengthen the foundations for a sound risk culture in the financial sector

i. Implement measures for more risk-aligned executive compensation
ii. Develop codes and practices, and training programmes

4.3 Regulation and greater regional and international integration

4.3.1 Collaborate with other central banks and supervisory authorities to safeguard stability of a regionally- and internationally-connected financial sector

i. Achieve greater consistency in the principles of regulation and supervision across jurisdictions
ii. Establish channels for the timely exchange of information between supervisory authorities
iii. Strengthen liquidity safety nets to support more efficient cross-border provision of liquidity

4.3.2 Participate in greater cross-border arrangements and supervisory cooperation to support the orderly development of an international Islamic finance industry

i. Develop a robust infrastructure to support efficient liquidity management
ii. Implement prudential standards, risk management and Shariah governance practices

5.1 Electronic payments for greater economic efficiency

5.1.1 Enhance the e-payments infrastructure through improvements and new services to further facilitate the adoption of e-payments

i. Widen access to the Real Time Electronic Transfer of Funds and Securities (RENTAS) system via electronic channels such as Internet banking
ii. Adopt international messaging standards for the RENTAS system
iii. Facilitate efficient reconciliation of electronic transactions by providing adequate payment information to beneficiaries
iv. Provide mechanism to facilitate payment assurance and timely information of rejections for unsuccessful electronic transactions
v. Introduce rules in collaboration with financial institutions for faster and more standardised crediting of funds for e-payments
vi. Facilitate higher transaction limits via electronic channels

5.1.2 Enhance mobile banking and payments by driving the adoption of the mobile phone for banking and payment transactions

i. Implement a secure, simple and cost-effective authentication method such as mPKI to instill user confidence in mobile banking and payments
ii. Introduce an Electronic Bills Payment Portal for consumers and billers
iii. Leverage on Near Field Communication (NFC) technology to offer convenient mobile payment services

5.1.3 Widen the payment card infrastructure with the aim of increasing the use of debit cards

i. Increase the number of point-of-sale (POS) terminals that accept payment cards to 25 terminals per 1,000 inhabitants by 2020
ii. Institute an incentive structure that would encourage the use of debit cards
iii. Facilitate the deployment of standalone POS terminals at smaller merchants
iv. Widen the acceptance of the domestic PIN-based debit card or e-Debit among merchants

5.1.4 Promote a conducive pricing structure for payment services that facilitates the use of more cost effective payment methods

i. Allow charges to be imposed on cheques to reflect its higher cost, while having lower charges for e-payments
ii. Encourage banking institutions to introduce more cost-efficient products that promote the use of e-payments and discourage the use of cheques
iii. Support efforts by the Government and private corporations to reduce the use and acceptance of cheques
iv. Explore the introduction of tax incentives to encourage adoption of e-payments

5.1.5 Enhance awareness and user confidence in using e-payments to encourage higher usage of e-payments

i. Establish a one-stop information portal dedicated to promoting e-payments
ii. Intensify promotional campaigns, including road shows and exhibitions, in collaboration with the industry and trade associations

5.2 Empowering consumers

5.2.1 Promote financial capability as an essential life skill through the integration of financial education into the formal school and higher learning curriculum

i. Integrate important aspects of financial education in key subjects
ii. Enhance the knowledge and skills of teachers in the formal school system to effectively deliver financial education to students
iii. Encourage opening of deposit accounts to inculcate a savings culture and basic money management skills at an early age

5.2.2 Adopt a life events approach to the development and delivery of programmes and encourage greater collaboration among stakeholders in delivering financial education

i. Implement targeted financial capability programmes focusing on specific life events that influence the lifestyle and behaviour of consumers
ii. Leverage on strategic partnerships with the Government, NGOs, religious authorities, local councils and employers in providing financial education
iii. Increase the use of technology to enhance the reach, flexibility and effectiveness in the delivery of financial education
iv. Enhance roles of financial service providers and industry associations to support financial literacy initiatives by pooling resources and coordinating activities

5.2.3 Introduce a cohesive regulatory regime that addresses regulatory gaps and is consistently enforced with the establishment of a committee of relevant authorities to formulate and operationalise a new consumer credit law

5.2.4 Establish the Financial Ombudsman Services (FOS) Scheme with expanded powers to promote the effective and fair handling of disputes with financial service providers

i. Transform the existing Financial Mediation Bureau (FMB) into the FOS
ii. Expand the scope of the FMB to cover a wider range of disputes against financial service providers
iii. Collaborate with other regulatory agencies to facilitate an integrated dispute resolution regime

5.2.5 Promote the wider utilisation of credit reports to encourage a more responsible credit and repayment culture

i. Facilitate the sharing of financial and credit information between the Central Credit Reference Information System (CCRIS) and other approved credit reporting agencies
ii. Broaden the range of information collected by authorised credit reporting agencies
iii. Promote convenient and efficient access to credit reports by financial service providers and financial consumers

5.2.6 Strengthen the enabling infrastructure for access to financial education information and assessment of the effectiveness of financial education initiatives

i. Introduce a single interface to facilitate access to comprehensive financial education information provided by different agencies
ii. Establish an assessment framework to regularly monitor and measure the financial capability of consumers

5.2.7 Promote and reinforce fair and responsible practices among financial service providers through appropriate regulation and enhanced transparency

i. Promote publication of customer charters by all financial service providers and implement processes for measuring performance against the charters
ii. Intensify supervisory reviews of practices by financial service providers to reinforce fair dealings towards consumers
iii. Review current barriers to the portability of financial products and services

5.3 Talent development to support a more dynamic financial sector

5.3.1 Produce more industry-ready entry-level graduates through enhanced collaboration and coordination between the financial industry and institutions of higher learning

i. Establish formal working arrangements between the industry and tertiary education institutions
ii. Embed contents of the Financial Sector Talent Enrichment Programme (FSTEP) into the curriculum and syllabus of institutions of higher learning

5.3.2 Upgrade the skills and competencies of the existing workforce to enable them to perform in a more competitive and globalised environment

i. Develop a certification programme for competencies required in the key functions and positions within the financial sector
ii. Provide wider opportunities for and easy access to distance learning and self-learning programmes
iii. Enhance the overall content and quality of training programmes offered by training providers
iv. Ensure accreditation of programmes offered by training affiliates of the Asian Institute of Finance (AIF) to maintain high standards in quality education for the financial industry
v. Set standards for professional programmes and qualifications in Islamic finance
vi. Ensure sufficient funding of education for the financial sector

5.3.3 Attract regional and international talent by facilitating entry into the domestic financial sector workforce

i. Launch a web portal to profile Malaysia's financial sector as a destination for international and regional talent
ii. Simplify procedures for temporary or permanent international skilled migration to the financial sector
iii. Institute collaborative arrangements with Talent Corp to leverage on existing incentive programmes for skilled professionals entering the financial sector
iv. Foster partnerships with internationally renowned training providers and universities in advancing the education agenda for the industry
v. Promote collaborative financial sector research

5.3.4 Foster greater strategic focus, coordination and collaboration to achieve a comprehensive approach to talent development for the financial sector with the establishment of a Financial Services Talent Council to drive, oversee and coordinate the financial sector talent development agenda

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