Economic Research

MARC Research | 2 April 2021

Malaysian Rating Corporation Berhad
199501035601 (364803-V)

BNM Annual Report 2020

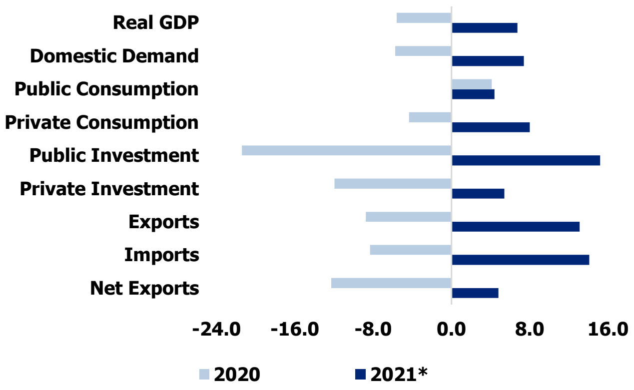
Firdaos Rosli
+603-2717 2936
firdaos@marc.com.my

Quah Boon Huat
+603-2717 2931
boonhuat@marc.com.my

Lee Si Xin
+603-2717 2942
sixin@marc.com.my

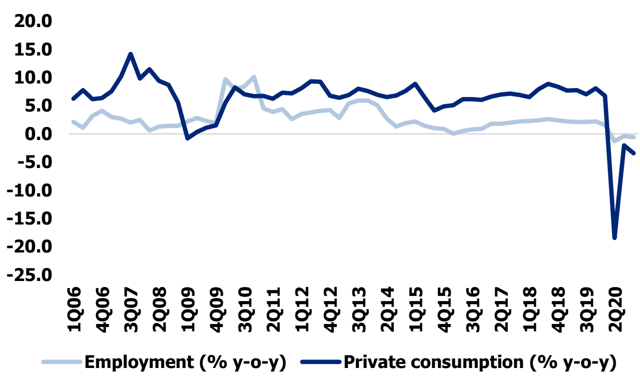
Nor Lyana Zainal Abidin
+603-2717 2912
norlyana@marc.com.my

Chart 1: GDP components: 2020 vs 2021 (%)



** BNM forecast*
Source: BNM

Chart 2: Private consumption vs employment



Sources: CEIC, MARC Research

GDP to recover to pre-COVID-19 levels by mid-2021

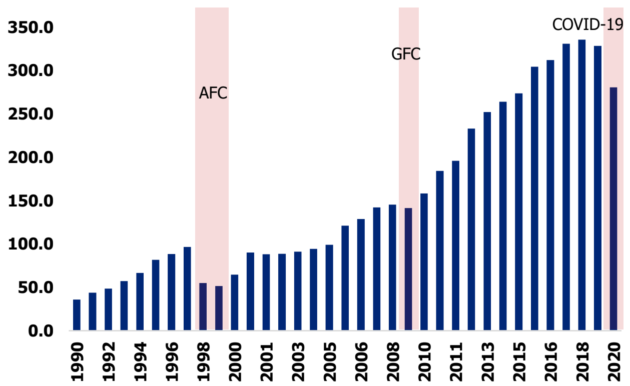
- **BNM expects the economy to expand by between 6.0% and 7.5% in 2021 (2020: -5.6%) and recover to pre-COVID-19 levels by mid-2021.** It sees support coming from improving external demand amid the technology upcycle, and on the domestic demand side, less stringent containment measures and the rollout of vaccines, gradual improvement in labour market conditions, and continued policy support. Further impetus to growth, it says, will come from the continuation of public infrastructure projects.

- **Domestic private consumption, according to BNM, will anchor GDP growth in 2021.** It is expected to expand by 8.0% on the back of less stringent movement restrictions and gradually improving sentiment on the back of the rollout of vaccines and income growth, as well as increasing economic activity. Private and public investment – driven by better demand conditions and government initiatives – are both expected to rebound. Meanwhile, the central bank observes encouraging signs of continued hiring activity, which should improve employment.

- **Contrasting with BNM's optimistic GDP forecast, MARC's forecast comes in lower at 5.6%.** We believe that the current rebound will not take GDP back to pre-COVID-19 levels by mid-2021. After all, the economic damage remains, and the recovery has not been broad-based. It is telling that the majority of businesses in a recent survey by the Associated Chinese Chambers of Commerce and Industry of Malaysia indicated that they cannot sustain beyond six months due to cash flow problems. In the absence of full economic resumption, we think any potential upsides to the central bank's forecast due to the so-called pent-up demand will be muted.

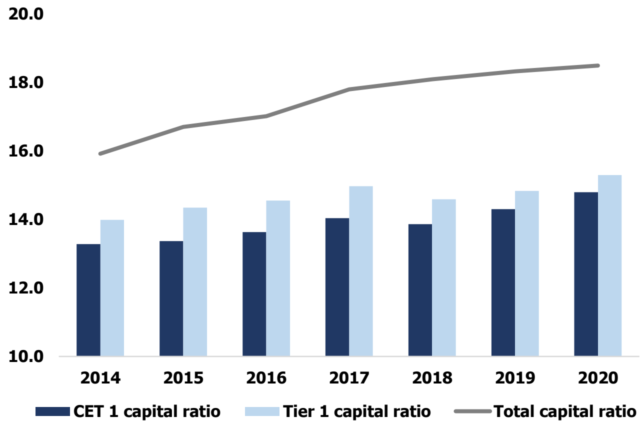
- **It is important to note that the strength of the recovery remains heavily dependent on the persistence of the economic scarring.** Also important is the effectiveness of policy responses and the ability of businesses to adapt. For example, while the pandemic may have spurred increased digitalisation and innovation, some businesses may not have the resources to adapt to the new normal. In any case, it is likely that the scarring to high-contact service sectors, which have borne the brunt of the pandemic, will be slower to heal.

Chart 3: Investment (RM billion)



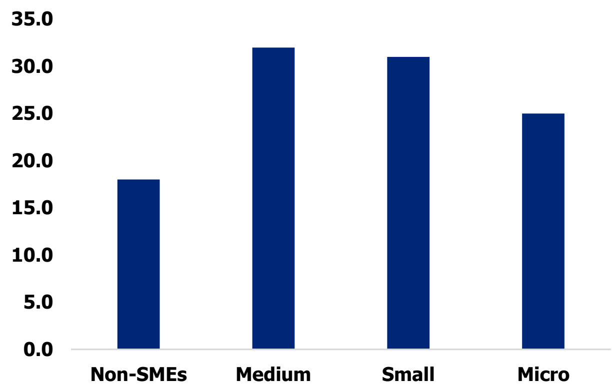
Sources: CEIC, MARC Research

Chart 4: Capital ratios of the banking system (%)



Source: BNM

Chart 5: Share of firms reporting increase in financing gap (%; 2H2020)



Source: BNM Survey on Firms' Access to Financing 2020

- **We agree with BNM that risk to 2021 growth, primarily due to pandemic-related factors, remains tilted to the downside.** The possibility of a broad-based lockdown to curb infection or slower-than-expected rollout of vaccines – if not here, then perhaps in major trading countries – is very real. Note that infections in, for example, the US continue to spike despite the rollout of vaccines and the Centers for Disease Control and Prevention director has warned of "impending doom." Having said that, we laud the Malaysian government's commitment to steer clear from deploying a blanket Movement Control Order (MCO) to combat the pandemic.

- **Expectation: Regarding the official growth estimates, we believe that the government will soon lift the ban on interstate travel soon.** As the virus has already infiltrated the community, we think a stronger enforcement of SOPs rather than the imposition of harsh mobility restrictions is a more appropriate policy response. This is because it will minimise further economic scarring.

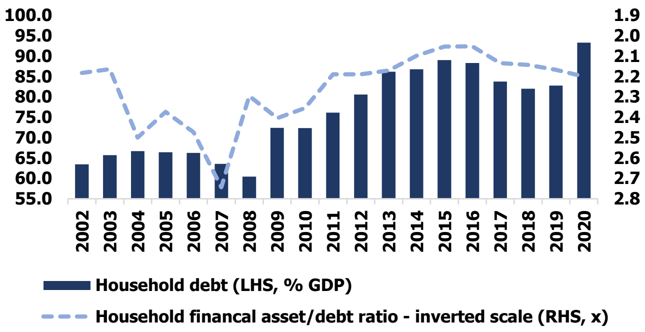
Financial system remains resilient

- **Banks, according to BNM, remained well-positioned to support economic recovery despite the challenging credit risk outlook.** Capital ratios, for example, continued to surpass the regulatory minimum. In 2H2020, the total capital ratio rose to 18.5% from 18.3% previously. The Common Equity Tier 1 capital ratio also improved to 14.8% from 14.6%. Meanwhile, excess capital buffers stood at RM126.7 billion, up from RM122.0 billion. It is notable that banks' healthy liquidity position remains supported by stable funding conditions. While BNM expects credit risk to rise, it will be buffered by higher provisions.

- **Financial intermediation has remained supportive of the economy.** This is buoyed by a plethora of measures that support financing activities, including SST exemption, the Home Ownership Campaign, guarantee schemes, and BNM funds to complement banks' financing to SMEs. Financial market stress has, as a result, receded from levels seen at the onset of the pandemic with orderly market conditions preserved.

- **Most households, thanks to existing financial buffers and relief measures, have been able to sustain their debt-servicing capacity.** According to BNM, aggregate financial buffers have remained broadly intact. For example, the financial assets-to-debt ratio had stood unchanged from six months ago at 2.2 times in 2H2020 and the liquid financial assets-to-debt ratio has improved to 1.5 times from 1.4 times. It is notable that most households were able to resume their loan repayments after the automatic moratorium ended.

Chart 6: Household debt vs financial asset



Source: BNM

- **The outlook for certain business segments remains challenging, though the latest available business sector indicators – at least for 3Q2020 – showed that overall financials were sustained even as earnings performance weakened.** While the operating margin fell to 4.7% from 5.0% six months earlier, there were improvements in debt-to-equity (23.4%), cash-to-short-term debt (1.1 times) and interest coverage ratios (4.1 times). Notwithstanding this, firms-at-risk remained elevated with more businesses in pandemic-affected sectors seeking repayment assistance.

- **Latest stress tests under two hypothetical adverse scenarios affirm the resilience of the financial system.** The simulation indicated that post-shock, the banking and insurance sectors will be able to maintain their capital levels at well above the regulatory minimum. Banks have ample capital buffer to take on unexpected shocks.

- **We think that the worst of the crisis is over. However, with the ongoing pandemic and given the uneven sectoral recovery, we agree with BNM that the credit risk outlook for selected sectors remains challenging.** It is thus important that there continues to be support for viable businesses, which consequently should help maintain the stability of the financial system.

- **Expectation: If the present mobility restrictions persist until 2H2021, we believe that some, if not all, of these initiatives will continue to lend support to private consumption growth in the latter half of the year.**

Table 1: Malaysia's GDP performance and forecast

Growth (% y-o-y)	2015	2016	2017	2018	2019	2020	2021F	
							MARC	BNM
GDP	5.1	4.4	5.7	4.7	4.3	-5.6	5.6	6.0 - 7.5
Domestic Demand	5.1	4.3	6.5	5.5	4.3	-5.7	5.8	7.4
Private Consumption	6.0	5.9	6.9	8.0	7.6	-4.3	6.2	8.0
Public Consumption	4.5	1.1	5.5	3.3	2.0	4.1	3.3	4.4
Private Investment	6.3	4.5	9.0	4.3	1.5	-11.9	5.8	5.4
Public Investment	-1.1	-1.0	0.3	-5.0	-10.8	-21.4	8.3	15.2
Real Exports	0.3	1.3	8.7	2.2	-1.1	-8.8	5.6	13.1
Real Imports	0.8	1.4	10.2	1.3	-2.3	-8.3	5.3	14.1

Sources: DOSM, BNM, MARC Research

Published and Printed by:

Malaysian Rating Corporation Berhad 199501035601 (364803-V)
19-07, Level 19, Q Sentral, 2A Jalan Stesen Sentral 2, Kuala Lumpur Sentral, 50470 KUALA LUMPUR
Tel.: +603 2717 2900 Fax: +603 2717 2920 Email: marc@marc.com.my
Website: www.marc.com.my