Deputy Governor's Closing Keynote Address at 2021 Malaysian Banking and Finance Summit

Speaker: Datuk Abdul Rasheed Ghaffour / Venue: - / Language: English / Speech/Interview Date: 21 Sep 2021 /

Thank you for inviting me to deliver the closing remarks at the 2021 Malaysian Banking and Finance Summit. While most of us would have liked to gather in person today, I am grateful that we are still able to connect virtually. Congratulations to the organisers for a successful event.

Since early 2020, the COVID-19 pandemic has impacted our lives in unprecedented and profound ways. We have had to learn to live with disruption, and to find new ways to work and interact with each other.

The financial industry has also experienced other forms of disruptions, especially over the past five years. This includes the increasing pace of digitalisation, new business models, and evolving consumer preferences. Like the uncertainty brought upon by COVID-19, the path ahead for the financial sector will also have new and unpredictable challenges. The key point is that; we must be prepared for a world where change is the norm.

Against the backdrop of a public health and economic crisis of this scale, the financial sector, is now presented with a once-in-a-generation opportunity to mould the future of finance. As history illustrates, this opportunity is no different from what we have seen in the past.

About a century ago, the West emerged from the rubble of World War I and the Spanish flu to a decade of exhilarating economic expansion – a period known in America as the “Roaring Twenties”.

The renowned economist, John Kenneth Galbraith, described the stock market boom in the 1920s as fuelled by activities in financial markets and innovations in new financial products. With lacklustre financial regulation in America at the time, these developments left the economy vulnerable to adverse shocks. Indeed, the ensuing Great Depression saw real Gross Domestic Product (GDP) falling an unprecedented 30 per cent, sending the unemployment rate soaring above 20 per cent at its highest point[1]. The Great Depression was the longest and most widespread economic crisis of the 20th century.

A century on and with the benefit of hindsight, the financial sector can, and must surely do better in balancing development and risk. Banks – who have been a source of stability and support during this COVID-19 pandemic – now have a unique chance to rethink financial services. **We must ensure that progress and transformation is inclusive and sustainable, while not posing undue risk to financial or economic stability**.

Today, I would like to share how the financial sector may strengthen its role now and, in the future, in a responsible and sustainable manner. In his opening keynote address, YB Minister of Finance spoke about the “3Rs”, which are the focus of the Budget 2022. I would also like to reference the same themes. This demonstrates the importance of a coordinated approach towards ensuring progress in our economy and society at large.

The first is “**Resilience**”: Here, we consider how the sector can support the economy and the *Rakyat* during the most challenging times; and

This is followed by “**Recovery”:** how banks can play a role in safeguarding the ‘healing process’ amid an environment of risks and uncertainties; and

Third, is “**Reform**”: Going beyond immediate priorities, we turn to longer-term strategies that the industry can undertake to accelerate digital adoption in financial services while funding a sustainable and inclusive future.

Resilience: Supporting the economy during the most challenging times

Our financial sector has been proven to be **Resilient** in this crisis.

Like other countries, Malaysia was adversely impacted by the COVID-19 pandemic. Malaysia's economy contracted by 5.6 per cent in 2020[2], the weakest performance since the Asian financial crisis. The unemployment rate reached a high of 5.3 per cent in May 2020, a level not recorded since the late 1980s[3].

However, a strong fiscal, monetary, and financial policy response cushioned this economic shock. Despite the re-imposition of stricter nationwide containment measures in the middle of this year, the economy continued its recovery path, driven by improvements in domestic demand and continued robust exports performance[4]. For 2021, the economy is expected to record a growth of between 3.0 per cent and 4.0 per cent.

A key success factor is the coordinated and consistent policy response by the Government and the banking industry, particularly in offering relief facilities and loan repayment assistance to affected individuals and Small and Medium Enterprises (SMEs). In April 2020, Malaysia was one of the first few countries to implement an automatic moratorium for all bank loans for a six-month period. Recognising the ongoing challenges faced by borrowers, from July 2021, the banking industry has continued to make available the six-month loan moratorium to assist all individuals, microenterprises, and affected SMEs. As of August 2021, the total individual and SME loans eligible for the automatic loan moratoriums account for close to RM1.4 trillion, or around 73 per cent of total banking system loans in the country[5], benefitting more than 2.6 million borrowers in Malaysia between 1 June and 20 August 2021[6]. In terms of scale and scope, the measures introduced in the last one and a half years have been the among the most extensive offered by any country[7]**.** With the high level of strength and stability of our financial sector at the onset of the pandemic, the banking industry has been able to step up when we needed it the most.

As the world gradually reopens and vaccination rates accelerate, there is reason to be cautiously optimistic. Yet, the battle against COVID-19 and its variants is not over. The banking industry will need to be proactive and ensure that it continues to build the capacity required to extend support to borrowers who need help in a timely and efficient manner. This includes extending new financing to support the economic recovery as more businesses are allowed to resume operations.

Since the structural reforms of the post-Asian Financial Crisis era, banks have been a source of stability and strength to the country. This must continue, even as banks contend with the long-lasting effects of the pandemic, including the potential 'double whammy' of reduced income and higher loan defaults by individuals and businesses.

Recovery: Safeguarding the 'healing process' amid ongoing risks and uncertainties

Many of us have come to terms with the realisation that COVID-19 is here to stay. Instead of aspiring for a future where the virus is completely eradicated, we should begin to adapt our activities and behaviours to turn COVID-19 into a manageable risk. From both the economic and public health perspective, the risks of not doing so are too costly.

There are encouraging signs where this adaptation is taking place. For example, fully vaccinated individuals are now able to participate in a wider range of activities, subject to compliance with strict Standard Operating Procedures (SOP), bringing about much-needed relief to businesses. Further arrangements are being explored, including cross-border travel bubbles within ASEAN and collaboration on mutual recognition of vaccination certificate documents between regional countries[8].

This progress is certainly encouraging. And I believe that the financial sector will play a pivotal role to safeguard Malaysia's ongoing healing process amid the complex challenges ahead. While there may be several paths to **Recovery** – let me share three ways forward.

First, the banking sector should **continue to ensure access to financing to those who deserves it**. As I mentioned earlier, banks have responded to this call admirably. At end of the second quarter of 2021, outstanding loans to both the business and household segments increased by 1.3 per cent and 5.3 per cent respectively, as compared to the same period last year[9]. But the job is definitely not done. Banks must continue to strengthen their countercyclical role to support the economy by continuing to finance viable but distressed borrowers. Bank Negara, will continue to assist the industry by providing support in various areas, including through dedicated funds that offer financing at concessionary rates for banks to on-lend to consumers.

Second, the financial industry should **seize this opportunity to contribute to the recovery process and broader reform agendas of the nation**. The pandemic has underscored and exacerbated some of the deep structural issues in the economy, especially in the labour market, where more vulnerable workers groups have been affected.

As the economy moves into the recovery period, policies should shift from job preservation to job creation. Banks can contribute through the provision of financing, and also support through other ways. A key reform area, for example, is the implementation of active labour market policies by the Government to improve the overall social protection framework. This is aimed at enhancing the employability and income potential of workers. In many countries, these are primarily market-financed. Banks can seek out opportunities to support these policies, which would alleviate the fiscal pressure on the Government. In addition, banks can lead by training and investing in upskilling and development to prepare a workforce that is ready for the future.

Third, banks must **focus on sustainability as part of efforts to promote economic recovery** – in line with the global focus to achieve a balance of economic, social, and environmental progress. Bank Negara, in partnership with Securities Commission and the industry, has continued to lead collective climate actions through the Joint Committee on Climate Change (JC3). I am pleased to note the progress made by the JC3 so far, notably on the establishment of the Climate Change and Principle-Based Taxonomy (CCPT) Implementation Group to ensure a successful implementation of the taxonomy, the plans to support climate-related disclosures by financial institutions, and the collaboration between key public and private sector partners to address critical data gaps for climate risk management[10].

Banks have a core role to play in the transition to a greener economy. For example, inclusive circular economy solutions and business models – seen as a critical piece for sustainable development – are still considered a high-risk venture for financiers[11]. This is an opportunity for the banking sector to work closely with relevant stakeholders, including policymakers, to develop new and innovative financial instruments that de-risk circular economy investments while ensuring that the right incentives are in place for better public-private partnerships. An example of such an instrument is blended finance, which is emerging as a promising approach to unlocking commercial finance consistent with desired development goals, that is, to build circular economy innovations and businesses at scale.

Reform: Accelerating digital adoption in financial services while funding a sustainable and inclusive future

Let me now move to our final 'R' – **Reform**. I would like to focus on two major trends relevant for the banking sector: the first is on Digitalisation and the second is on Funding the Future Economy.

Digitalisation

Today, increasing digitalisation and emerging new business models are reshaping the very identity of the financial sector – as shown by changing consumer behaviour, the blurring of boundaries within and beyond the financial sector, and even in the way we interact with finance. The rapidly evolving landscape brings with it a host of opportunities, including lower costs for financial services, more tailored and convenient financial offerings, and a greater ability to reach underserved and unserved segments.

Reflecting on these opportunities, the reality is that the lines between technology and finance are increasingly vague, with market-place innovations leading the way. For example, new financial players such as Big Tech firms have been able to enter financial services and scale up rapidly by harnessing their users' data and leveraging network effects. A similar scaling up can be observed in the adoption of stablecoins, with The Economist[12] estimating that the market capitalisation of stablecoins has increased by more than seven times in just a year, from about USD14 billion in August 2020 to over USD100 billion in August 2021. And in a more esoteric corner of finance, the emerging trend of non-fungible tokens (NFT) since late 2020 has led to a democratisation of finance of sorts, that may have implications on traditional finance intermediaries.

When we take a step back, these technology-driven developments – including the broader trend of global stablecoins and Decentralised Finance (DeFi) platforms[13] – may seem relatively nascent in the context of the existing financial sector. But, these developments will have profound implications for regulators and more broadly, for the financial sector.

Central banks, including Bank Negara, are **mindful of these complex challenges, even as we anticipate the opportunities that lie ahead**. On 2 September 2021[14], Bank Negara announced that we will join forces with the BIS Innovation Hub, the Reserve Bank of Australia, Monetary Authority of Singapore, and South African Reserve Bank to test the use of central bank digital currencies (CBDC) for international settlements through Project Dunbar. This proof-of-concept is a key part of our journey to build internal capacity and understanding on emerging technologies, to facilitate the future-proofing of our key payment infrastructures, whilst addressing existing gaps in cross-border payments.

At the same time, Bank Negara is committed to **foster an enabling environment for data-sharing in the financial sector**. We will focus on developing common standards for high-impact use cases and strengthening the digital data governance framework to ensure the protection and fair treatment of financial consumers. We are also actively collaborating with other stakeholders, including the Government and industry players, to enhance accessibility to public data under the Government's open data initiatives and to contribute to the development of a robust data protection legal framework.

The Ministry of Health's recent launch of COVIDNOW, a one-stop portal for COVID-19 data, is a good example of moving towards data-driven policy decisions. Importantly, the initiative, which has received encouraging feedback so far, demonstrates that public-private partnerships are possible and, in fact, much needed.

Similarly, the banking sector **should make the most of the progress in the data ecosystem** to further advance financial inclusion, to empower consumers to make informed financial decisions, and to develop innovative financial solutions that benefit the *Rakyat* as a whole.

Funding the future economy

Equally important for a sustainable **Reform** is to **ensure quality investment and innovation-led growth**. Some promising steps have already been taken, notably in the development of the National Investment Aspirations (NIA), a forward-looking growth framework, that serves as a basis for Malaysia's investment priorities. The NIA is expected to propel longer-term growth for Malaysia through the sustainable quality investment in new and complex growth areas. At Bank Negara, we have established the RM1 billion High Tech Facility-National Investment Aspirations (HTF-NIA) under the BNM Funds for SMEs program for businesses affected by the pandemic, to preserve Malaysia's competitive positioning in the global value chain while at the same time safeguarding high-skilled jobs.

While the unprecedented policy response by the Government has been key to limit the economic fallout of the pandemic, an overreliance on a debt-based recovery will lead to significant financial stability risks[15]. Therefore, banks should **seize this moment to offer new forms of financing and to improve understanding of new growth areas**, including those aligned with the NIAs. Innovative alternative financial instruments – whether based on debt, equity, or even invoice-based financing – will be critical in meeting the needs of high-growth businesses across various phases of the firm lifecycle. I would strongly encourage banks to continue to work closely with the ecosystem players, including market-based financing entities, industry players and regulators, in this journey together.

Closing remarks

Let me conclude with the words of Søren Kierkegaard, a Danish philosopher and theologian – "Life can only be understood backwards, but it must be lived forwards."

Turning back the pages of time is necessary to understand and learn from mistakes. Yet, even as we seek to move forward, we are confronted with the reality of a complex and rapidly evolving world.

Looking ahead, I am pleased to share that we are in the advanced stages of developing the upcoming Financial Sector Blueprint, that will set the vision for the financial sector for 2022 – 2026, which will be launched early next year. The Blueprint will also emphasise the importance of market-led development. Given the increased level of maturity and development of the financial sector, at Bank Negara, we believe that it is an opportune time for industry to be at the forefront and to play a bigger role in defining the future of the financial sector.

Before I end my remarks, let me emphasise – I am excited for the future of the financial sector. It is now, more than ever, that the financial sector should turn crises into new opportunities with the '3R' strategy, to build a more inclusive, resilient, and sustainable future for Malaysia.

With that, thank you very much.

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