



BANK NEGARA MALAYSIA
CENTRAL BANK OF MALAYSIA

FINANCIAL
SECTOR
BLUEPRINT

20²²₂₆



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Foreword by the Minister of Finance

Malaysia is at an inflection point. As we exit and recover from the COVID-19 pandemic, it is hard to look back and ignore the scars it has left on the lives and livelihoods of many. Yet, it is important for us to look forward and not lose sight as to what is ahead of us, as we continue to push forward towards becoming a high value-added, high-income nation.

The pandemic has accelerated the digital revolution, which has profoundly changed the way we work, play and interact with each other. Meanwhile, the implications of climate change, biodiversity loss, and demographic change are no longer academic, but real and pressing. While these shifts pose new risks – especially to the most vulnerable in our society – they also present opportunities to build back better and transform the country's development trajectory.

In this regard, the launch of the Financial Sector Blueprint 2022-2026 is timely. In realising the nation's aspirations, the financial sector has always played an important role – be it supporting families to grow and protect their wealth, or helping businesses venture into new territories. In the next five years, the strategies expressed in this Blueprint will be critical for the financial sector to navigate the oncoming challenges and capture new opportunities. To that end, I call upon the financial sector to continue to be the catalyst for reform, drive sustainability and contribute to our collective aspiration of a "Prosperous, Inclusive and Sustainable Malaysia".

With this, allow me to express my congratulations and appreciation to everyone involved in formulating the Blueprint, particularly Bank Negara Malaysia.

A handwritten signature in black ink, consisting of several fluid, overlapping strokes.

YB Senator Tengku Datuk Seri Utama Zafrul Tengku Abdul Aziz

24 January 2022



Message from the Governor

Through the years, the financial sector has grown and evolved to help improve the lives and livelihoods of many in Malaysia. While the financial sector has come a long way, we have not stopped thinking about how finance can be further propelled to more effectively serve the economy, and in particular, to help support the nation in transitioning to its next stage of development.

In the world of finance, new applications of technology, broader shifts to digital channels and the emergence of new business models have opened up exciting possibilities for better financial services. At the same time, these developments raise fundamental questions about finance itself and how it should be regulated. Similarly, demographic shifts in Malaysia would require fresh ideas to facilitate savings, investments, and effective social safety nets for a soon-ageing population, even as other persistent socioeconomic gaps remain. The economic effects of climate change are also beginning to manifest. Along with this, there has been a growing appreciation for the risks to the financial sector, as well as the potential role of finance in the transition towards a greener, more climate-resilient economy.

Further shaping the path ahead for the financial sector is the pandemic. We are reminded that the health and fortunes of the financial sector are closely intertwined with the wider economy, as well as the natural environment. During the pandemic, the financial sector played a key role in supporting millions of Malaysian individuals and businesses during the lockdowns, as well as in helping jumpstart the economy as it reopened. This has been possible due to the resilience of the financial system, underpinned by the prudent management and build-up of buffers by financial institutions over the years.

As the nation navigates the extraordinarily uncertain times ahead, my hope is that the financial sector will continue to serve the Malaysian economy from a position of strength. This Blueprint sets out our vision for the next steps for that journey, alongside financial sector strategies to advance desired outcomes from 2022 to 2026. Beyond supporting the economic recovery, the financial sector will play a key role in helping Malaysia make the most out of this unique moment in history to realise a more dynamic, inclusive and sustainable development path.

Developing this Blueprint was no small task. I would like to express my heartfelt gratitude to all who worked to grapple with the big questions explored here. Special thanks goes to those from outside the Bank, whose suggestions and insights have been crucial in informing our strategies.

Nor Shamsiah Yunus
24 January 2022

Executive summary

Overview of the Blueprint

Key megatrends shaping the landscape ahead



Economic conditions

Uneven global economic recovery, alongside other uncertainties (e.g. virus path, global supply chain shifts)



Demographics

Risks of financial exclusion amid ageing population and other persistent gaps (e.g. socioeconomic disparities, financial literacy)



Technology

Promise of better financial services but with new regulatory challenges amid shorter innovation cycles, new skillsets required and blurred boundaries



Climate and environment

Need for a just and orderly transition to greener, more climate-resilient economy and financial sector

Desired outcomes and targets for 2026



Three broad themes

Finance for all

- ◆ Diverse choices for customers, including 'digital first' solutions
- ◆ Strengthened financial safety nets
- ◆ Confident and capable financial consumers



Finance for transformation

- ◆ Growth in alternative finance
- ◆ Deeper global integration, with continued leadership as an international gateway for Islamic finance
- ◆ Vibrant and dynamic financial landscape



Finance for sustainability

- ◆ Wider adoption of value-based intermediation (VBI) to serve the economy, community and environment
- ◆ Steady progress in greening finance and financing green

Key targets and milestones¹

- ◆ Narrowing of gap between Malaysia's **OECD/ INFE² financial literacy scores** and the average score of OECD members
- ◆ Increase in **e-payment per capita** at CAGR³ of higher than 15%
- ◆ **Insurance/takaful penetration** rate of 4.8-5.0% (as % of GDP⁴)
- ◆ Doubling of number of individuals subscribed to **microinsurance/microtakaful**
- ◆ Enactment of **consumer credit law and oversight body**
- ◆ Single **licensing regime** for financial advisors and financial planners
- ◆ Steady growth in **alternative finance** channelled to new, innovative enterprises
- ◆ Faster, cheaper, more accessible **cross-border payments**
- ◆ More than 50% of new financing is for **green and transitioning activities**
- ◆ Steady growth in **VBI-aligned assets**

¹ Selected areas, not representative of the Blueprint as a whole

² OECD International Network on Financial Education

³ Compounded annual growth rate

⁴ Gross domestic product

Our regulatory focus for financial development



Foster market dynamism while supporting sustainable development objectives ...

- ♦ Address undue barriers to market entry, while ensuring orderly exit
- ♦ Promote 'co-opetition' for critical ecosystem enablers
- ♦ Strengthen conditions for market discipline, focusing on more empowered consumers
- ♦ Build on VBI to advance greater inclusion, climate resilience and environmental sustainability

... anchored on monetary and stability mandates

- ♦ Continued monetary policy efficacy amid changing landscape
- ♦ Safeguard system-wide resilience and financial integrity

Five strategic thrusts for 2022-2026



Fund Malaysia's economic transformation

a. Sustain a strong economic recovery

e.g. supportive credit guarantee ecosystem, higher usage of forward-looking and alternative data, stronger countercyclical roles of DFIs⁵

b. Facilitate transformation to a high-income nation

e.g. supportive regulatory and taxation framework for alternative finance, stronger regulatory collaboration to both develop and oversee risks from non-debt finance ecosystem

c. Ensure post-pandemic resilience of financial intermediation role

e.g. increased collateralised transactions and developed derivatives markets for more vibrant onshore financial market, greater usage of insurance and takaful to support financing to firms, especially to high-risk industries

⁵ Development financial institutions



Elevate the financial well-being of households and businesses

- a. **Enhance financial capability and access, as well as effective usage of financial services towards greater financial inclusion**
e.g. financial education initiatives and impact monitoring through FEN⁶, strengthened role of agent banks and Mobile Banks (Bank Bergerak), wider adoption of financial inclusion KPI⁷ disclosures
- b. **Strengthen protection for households and businesses to build financial resilience**
e.g. public-private partnerships for risk protection against high-risk large-scale perils, microinsurance and microtakaful development, further liberalisation of motor and fire tariffs, sustainable MHIT⁸ cover
- c. **Shape a financial system that upholds fair and responsible dealings with financial consumers**
e.g. enhanced professionalism and incentive frameworks of intermediaries, guidance on conduct risk identification and ethical use of technology, consumer protection reforms (e.g. CCA and CCOB⁹, single licensing framework for financial advisors and financial planners)

⁶ Financial Education Network

⁷ Key performance indicators

⁸ Medical and health insurance/takaful

⁹ Consumer Credit Act and Consumer Credit Oversight Board



Advance digitalisation of the financial sector

- a. **Futureproof key digital infrastructures**
e.g. CBDC¹⁰ proof-of-concepts, non-bank access to RENTAS¹¹, high-impact open data use cases, shared infrastructures for fully digitalised motor claims
- b. **Support a vibrant digital financial services landscape**
e.g. simplified tracks for Regulatory Sandbox, licensing of digital insurers/takaful operators, digital payments, enhanced regulatory guidance for critical digital enablers such as cloud and AI/ML¹²
- c. **Strengthen cyber security readiness and responsiveness**
e.g. intensified focus on third party service providers, sharing of actionable cyber security intelligence through cyber contagion maps, standards for cyber security and cyber resilience terminology, cyber security training and certification
- d. **Support greater use of technology for regulation and supervision**
e.g. greater adoption of technology for regulation and supervision, reforms to the Bank's data gathering infrastructure and methods

¹⁰ Central Bank Digital Currencies

¹¹ Real-Time Electronic Transfer of Funds and Securities System

¹² Artificial intelligence/machine learning



4
Position the financial system to facilitate an orderly transition to a greener economy

- a. Integrate climate-related and environmental risks in prudential regulation and supervision**
e.g. effective implementation of taxonomy, greater alignment with VBIAF¹³ and its sectoral guides, strengthened supervisory expectations and prudential framework on managing climate and environmental risks, mandatory disclosure of climate risks
- b. Support orderly transition to a low-carbon economy**
e.g. intensified focus on bridging data gaps, expanded specialised funding and risk mitigation mechanisms, synergy between national policies and financial sector initiatives, accelerated capacity building initiatives on global platforms
- c. Integrate climate risks in the Bank’s internal functions and operations**
e.g. climate risk stress test for the financial industry, climate and environmental risk considerations in the Bank’s portfolio management activities, greater adoption of sustainability in the Bank’s physical operations

¹³ VBI Financing and Investment Impact Assessment Framework



5
Advance value-based finance through Islamic finance leadership

- a. Sharpen Malaysia’s proposition as an international gateway for Islamic finance**
e.g. strengthened gateway-critical capabilities (particularly on distributional capabilities, innovation, competitiveness), deepening of Islamic financial and capital markets, mechanisms for greater industry leadership
- b. Strengthen policy enablers of value-based finance for greater impact**
e.g. alignment of Shariah contracts’ application with the underlying wisdom (hikmah), broader application of ta’awun (mutual assistance) in takaful, enhance impact-based disclosures
- c. Mainstream social finance**
e.g. blended finance and funding escalator models, multi-stakeholder efforts to promote shared infrastructures



Malaysia's Financial Development Context

10 Key trends and developments

What success looks like in 2026

20 Our regulatory focus for financial development

Box Article:

Futureproofing the financial sector workforce

Box Article:

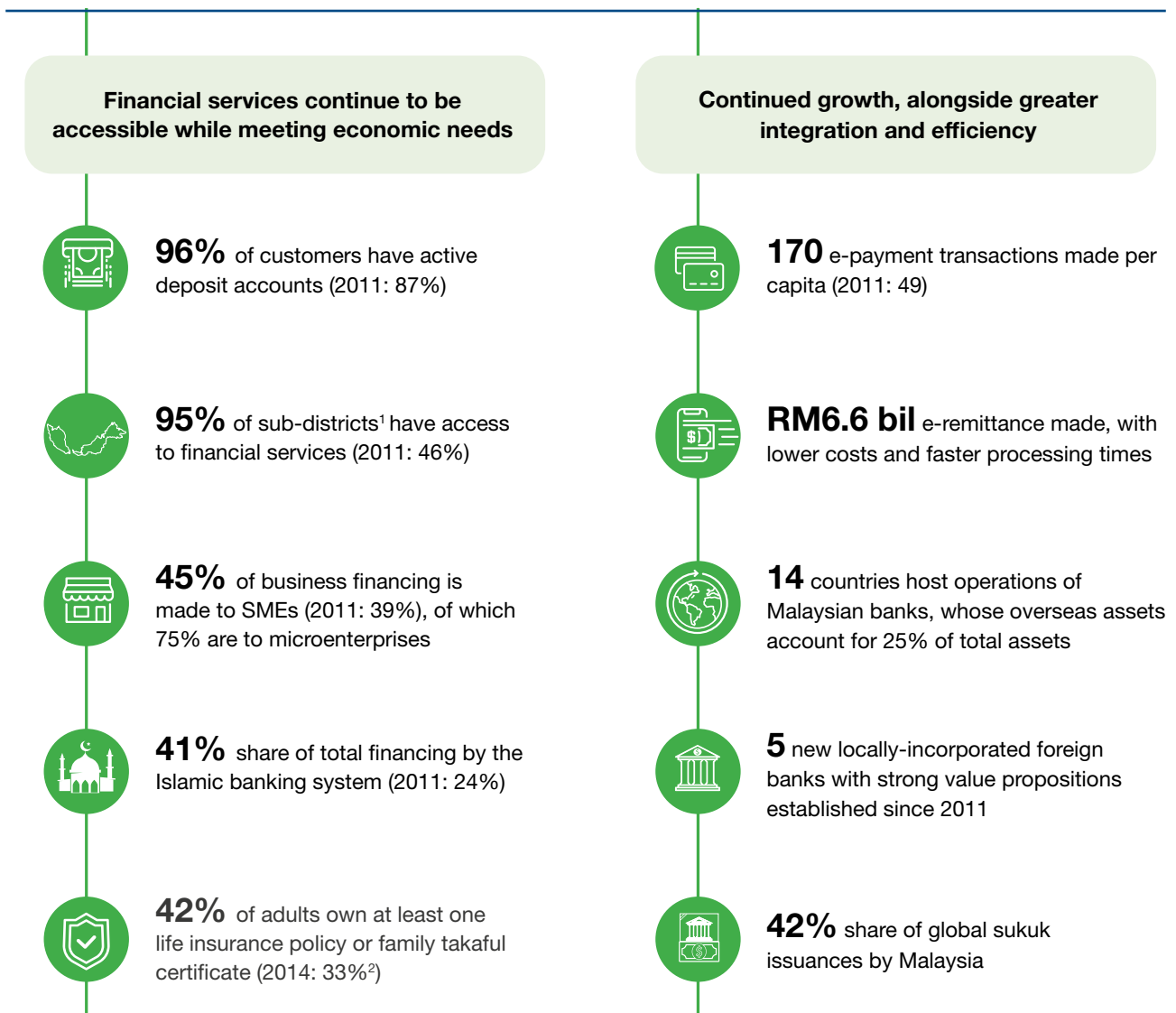
Medium-term priorities for the prudential framework and anti-money laundering and countering financing of terrorism (AML/CFT)

Key trends and developments

The financial sector has served the Malaysian economy well

It is vital that the financial sector is anchored on the real economy. This means that financial services should ultimately improve lives and livelihoods – helping individuals or businesses grow their wealth, make payments, own a home, grow their enterprise, manage financial risks and adverse events, create high quality jobs, and other economic outcomes. To that end, Malaysia's financial sector development has made good progress over the years (Diagram 1).

Diagram 1:
Malaysia's financial development progress at a glance



¹ With population of at least 2,000 people

² Earliest data available, after accounting for multiple policies per individual

Source: Bank Negara Malaysia, data as of end-2020 unless specified otherwise.

Malaysia's financial system today is the outcome of continued efforts and reforms over decades. Initiatives pursued under the Financial Sector Masterplan 2001 and the Financial Sector Blueprint 2011-2020 have fostered an environment conducive for the financial sector to keep pace with emerging developments and capitalise on new opportunities – thereby supporting Malaysia's economic development.

Along the way, core building blocks were established – many of which placed Malaysia's financial sector on a stronger footing, not only to withstand the shocks of the recent pandemic, but also to become a source of strength to cushion the economy:

- **Modernisation of the laws governing the financial sector**, particularly with the enactment of the Central Bank of Malaysia Act 2009 (CBA), Financial Services Act 2013 (FSA), and Islamic Financial Services Act 2013 (IFSA). These reforms enabled us to be more responsive to risks to monetary and financial stability in an environment when the financial system was becoming more interconnected. Enhanced legal powers paved the way for more effective oversight of more complex structures that were emerging then, which are increasingly relevant today (e.g. financial groups, non-bank financial institutions). Our commitment to other key financial regulatory objectives – such as conduct regulation, financial inclusion, and managing risks from non-bank financial institutions – were also cemented in these laws.

- **Regulatory reforms to create a strong, stable and progressive financial system**. Building on lessons all the way from the 1997 Asian Financial Crisis (AFC), corporate governance and risk management practices of financial institutions have been significantly strengthened. In the wake of the 2007/08 global financial crisis, we also advanced the adoption of key international standards (e.g. Basel III capital and liquidity reforms) – a crucial enabler as Malaysia's financial system was becoming more integrated with the global financial system (e.g. greater overseas presence, capital-raising activities in international financial markets).

More importantly, these reforms placed the financial system in a position of strength to be a shock absorber during economic downturns and play a countercyclical role to support economic recovery. Reflecting this, the range of financial sector assistance during the pandemic – be it debt restructuring for affected borrowers, or new financing to help businesses recover and rebuild – were possible only on account of the large buffers built up during good times.

Malaysia's financial system today is the outcome of decades of continued efforts and reforms

- **Key initiatives to empower and protect consumers**. These include the introduction of responsible financing guidelines in 2012. Against more competitive conditions, the guidelines ensured that lenders remained prudent in assessing whether borrowers could afford financing products over the lifetime of the financing – thereby promoting a more sustainable credit market and sound credit culture. The guidelines also encourage sound borrowing decisions by consumers, with clear expectations set for financial institutions to ensure that consumers are treated fairly in the sales, marketing and administration of financing facilities. In the area of insurance and takaful intermediaries, the Balanced Scorecard Framework was also introduced in 2018 – aligning remuneration structures of insurance and takaful intermediaries with better quality sales and policy servicing. More broadly, the recently introduced policy on Fair Treatment of Financial Consumers has placed expectations on financial institutions' boards and management to promote a culture of fair dealings with financial consumers.

Complementing these efforts is our continued collaboration with the Government and other stakeholders in the area of financial education, thereby supporting more well-informed decisions by consumers. Notably, the Financial Education Network (FEN) was established in 2016 to coordinate and drive a national financial education strategy in Malaysia. Meanwhile, advisory and redress mechanisms have also been put in place to support individuals and businesses facing financial distress. These include the Credit Counselling and Debt Management Agency (AKPK), Small Debt Resolution Scheme (SDRS), Corporate Debt Restructuring Committee (CDRC), and Ombudsman for Financial Services (OFS) – all of which are established by the Bank.

- Reforms to support Islamic finance development.** The CBA reinforced the role of the Shariah Advisory Council, thereby accorded it the status of the sole authoritative body on Shariah matters pertaining to Islamic finance. Enhancements to the regulatory framework following the enactment of the IFSA have strengthened foundations for end-to-end Shariah governance and compliance in the Islamic finance sector. This has allowed Islamic financial institutions to make full use of the diverse spectrum of Shariah contracts in financial transactions to design products that better meet customer needs, while being assured of the sanctity and validity of such transactions in the eyes of Shariah. With this groundwork, the focus has since turned to efforts to give full effect to the underlying principles of Shariah. An important step in this journey was the introduction of VBI, which calls on Islamic financial institutions to engineer solutions and adopt practices that have a more positive impact on the economy, community, and environment.

Meanwhile, as part of concerted efforts with the Government, financial regulators and industry players under the Malaysia International Islamic

Financial Centre (MIFC) agenda, key initiatives have also been advanced over the years to strengthen Malaysia's global standing for Islamic finance – including to develop global infrastructures such as the Islamic Financial Services Board (IFSB) and International Islamic Liquidity Management Corporation (IILM).

- Growing adoption of electronic payments (e-payments), alongside modernising of key infrastructures.** The use and acceptance of e-payment methods by businesses have accelerated over the past decade. Through concerted efforts with industry players, we have lowered the cost of e-payments to make it more affordable. For instance, this was achieved by addressing price distortions such as those existing between cash and cheques against e-payments. Key infrastructure enhancements were also rolled out – most notably, the Real-time Retail Payments Platform (RPP), which serves to support instant and seamless payments – not only between bank accounts, but also with e-wallets. Together with efforts to raise public awareness and confidence in the use of e-payments, these initiatives have made it easier for Malaysians and businesses to make and receive payments, be it in the physical or online world. These developments were vital in helping Malaysians manage the shock of the pandemic – which called for more contactless and digital transactions.

- Enhancements to the financing ecosystem for small and medium enterprises (SMEs), including microenterprises.** While credit decisions are commercial decisions for banks to make, we have worked with industry players to establish various mechanisms to bridge financing gaps. These include Credit Guarantee Corporation Malaysia Berhad's (CGC) imSME platform. Introduced in 2018, the platform enables SMEs to get fast access to a diverse array of financing products offered by various lenders. Meanwhile, SMEs facing difficulty with their financing applications may seek the assistance of *Khidmat Nasihat Pembiayaan* (MyKNP) to discuss challenges associated with their applications. The SDRS also helps financially distressed SME borrowers restructure or reschedule their financing. This was important during the pandemic in complementing repayment assistance programmes offered by lenders. Collectively, these mechanisms support an ecosystem that aims to ensure that the financing needs of SMEs are well supported, be it in good times or bad. This is particularly important given the sizeable role and importance of SMEs to the Malaysian economy and the distinct challenges they face in getting access to financing as compared to larger businesses.



A new landscape places new demands on the financial sector

As we continue to build on these foundations, it is crucial that the Malaysian financial system keeps pace with emerging developments. Looking ahead, various megatrends are expected to shape the future economic and financial landscape (see Diagram 2 for an overview). The pandemic has accelerated certain developments – accentuating some pre-existing vulnerabilities while also giving rise to opportunities for reforms that are long overdue.

Diagram 2
Key megatrends shaping the economic and financial landscape



Economic conditions

Uneven global economic recovery, alongside other uncertainties (e.g. virus path, global supply chain shifts)



Demographics

Risks of financial exclusion amid ageing population and other persistent gaps (e.g. socioeconomic disparities, financial literacy)



Technology

Promise of better financial services but with new regulatory challenges amid shorter innovation cycles, new skillsets required and blurred boundaries



Climate and environment

Need for a just and orderly transition to greener, more climate-resilient economy and financial sector

Macroeconomic trends amid an uneven global economic recovery

The shocks from the pandemic have led to the world economy's deepest recession since the Great Depression, where global gross domestic product (GDP) contracted by 3.1% in 2020. Since then, an unprecedented fiscal and monetary response at the global level has been crucial in charting the global economic recovery. Growth prospects have also improved with the progress in the rollout of vaccines across many countries.

Against this backdrop, the global economy is expected to rebound. According to the International Monetary Fund (IMF), the global economy is forecast to grow by 4.9% in 2022. The path to recovery, however, is likely to be uneven across countries, depending on differences in – and efficacy of – fiscal and monetary stimulus, as well as vaccination programmes.

As a small and open economy, Malaysia's opportunities and risks will continue to be shaped by developments and uncertainties beyond our shores. Prolonged effects on global trade are also possible, amid social and geopolitical tensions in an increasingly multi-polar world order. There are also pressures towards deglobalisation, alongside rising protectionist sentiments and potential shifts in global supply chains. On the public health front, the evolutionary path of the virus is another uncertainty – and may trigger new threats. This can lead to containment measures that affect economic activity. Among others, these trends will weigh on the strength and speed of global growth.

Structural reforms are needed to lay foundations for innovation-led growth and mitigate scarring effects from the pandemic

In navigating the challenges ahead, Malaysia must remain committed to executing structural reforms. Beyond the immediate focus of protecting lives and livelihoods, the broader objective should be to mitigate longer-term scarring effects from the crisis, while laying the foundations for a more innovation-led growth model to remain competitive at an international level and sustain our economic progress¹. Key areas of reform should include investment policy and incentives, labour markets, as well as digitalisation.

This includes helping key segments, such as SMEs, to pivot to a higher productivity growth path. Notably, SMEs have benefited from continued access to finance (45% share of total business financing in 2020), but there is still considerable room to translate that into higher economic output (38% contribution to GDP in 2020) to be on par with regional economies – e.g. Indonesia (61%), China (60%), and Singapore (47%)².

Rapid technological change

The transformative forces of digitalisation are fuelled by rapid technological advancements such as artificial intelligence (AI) and machine learning (ML), distributed ledger technology, and potential future applications from quantum computing. These will affect the delivery of finance in a multitude of ways.

As the wave of digitalisation sweeps across other sectors in the economy, the demand for financing will change as well. The Twelfth Malaysia Plan (RMK12) expects new innovative and technology-intensive industries, particularly the aerospace, biomass energy, electrical and electronics (E&E), halal, creative and smart agriculture industries to drive economic growth. Finance will need to support these new and emerging industries, which are critical for Malaysia's economic transformation.

The financial sector is expected to play an important role in supporting economic transformation.

Traditional modes of finance will remain important. Complementing efforts to reform the economy, the financial sector will need to meet new and more complex financing demands – such as for high-tech firms and other enterprises in highly innovative ventures.

In paving the way for the future of finance, it is vital to ensure that the financial sector absorbs, rather than amplifies, shocks and vulnerabilities in the economy. Avoiding an excessive reliance on debt will be key to that outcome. Apart from the recent pandemic, history has rich lessons to offer – particularly the experiences of “lost decades”, where markets with rapid expansion of debt outpacing economic growth suffered prolonged economic downturns and adverse effects on productivity in the wake of financial crises.

At the same time, “too much finance” may diminish benefits to economic growth – with potentially detrimental effects (e.g. more frequent booms and busts of an economy, diverting human capital away from productive sectors)³. Alternative finance – including non-debt-based solutions such as blended finance, venture capital (VC), private equity (PE), equity crowdfunding (ECF) – can complement traditional finance, providing new and potentially more resilient ways to fund the economy.

Digitalisation will also continue to shift consumer and business behaviour. Following the pandemic, the ‘low-touch’ economy has become much more pervasive. Customers have become much more familiar with digital and remote access amid public health concerns and movement controls. Although physical channels will likely remain relevant, this behavioural shift could be permanent for certain segments, especially among digital natives. Customers will increasingly demand an experience that is more frictionless, affordable, and customised, whether in the broader economy or financial services specifically. Governments, regulators, and industry players alike will need to have clear digitalisation strategies – not only to remain relevant, but to ensure that transformation efforts do not inadvertently heighten risks, such as to operational resilience, cyber security, and inclusion.

¹ For further details, please refer to the Box Article titled “Innovation Malaysia: Towards Higher Quality Growth in a Post-pandemic Future” in Bank Negara Malaysia's Economic and Monetary Review 2020, accessible at https://www.bnm.gov.my/documents/20124/3026377/emr2020_en_box2_innovation.pdf.

² Source: Data compilation from Statistics Indonesia, Singapore Department of Statistics and China's Ministry of Industry and Information Technology.

³ Source: Arcand, Berkes and Panizza (2012), “Too Much Finance?”, IMF Working Paper 12/61; Philippon and Reshef (2013), “An International Look at the Growth of Modern Finance”, Journal of Economic Perspectives.

In the digital world, the heightened focus on the customer comes with an intensified focus on data, often described as the new ‘oil’. Increasingly, financial institutions are making use of AI and ML to better understand consumer behaviour and spending patterns. This can support better risk management practices, more accessible financial services, and more customer-centric innovation. There is also a growing recognition of the criticality of key financial infrastructures that store, share, or synthesise these data. These include payment and settlement systems, as well as credit information systems. Combined with the Government’s initiatives – notably the National Data Sharing Policy (NDSP) to expand data accessibility – we expect more room for data-driven innovations moving forward. The regulatory landscape for financial services will also need to evolve in tandem, particularly to promote responsible and ethical use of data.

Rise of digital ecosystems demand policy responses that unlock benefits while managing regulatory arbitrage, potential spill-over risks and a growing reliance on third party service providers

Digitalisation is also profoundly reshaping the dynamics of the financial sector. A major development is the blurring of the lines between financial and non-financial services, as players seek to build ecosystems. Commercial enterprises – including Bigtechs – are making inroads into financial services, leveraging their existing networks of customers and merchants. Meanwhile, incumbent financial service providers (FSPs) are entering into an array of strategic partnerships, such as with fintechs and other firms, to better serve their customers. In parallel, emerging innovations – such as those in the decentralised finance (DeFi) space – are also introducing novel ways to store and mobilise funds, with potentially greater control by end-users.

Collectively, these trends intensify competition and collaboration – introducing new business models, as well as the promise of more efficient and innovative financial services. But these trends will also raise questions about how to keep these services inclusive and secure, while preserving market vibrancy. Safeguarding cyber security, including to manage ‘weakest link’ risks – amidst growing relationships between financial institutions and third party service providers (TPSPs) – will be critical.



Demographic shifts and challenges

Malaysia is expected to become an ageing nation by 2030⁴. Coupled with slower population growth, there will be new opportunities and challenges for the financial system. Visible coverage gaps remain among retirement savings schemes in Malaysia. For instance, the Employees Provident Fund (EPF) estimates that two out of three active EPF contributors may have insufficient retirement savings to meet a minimum pension of RM1,000 per month⁵. Meanwhile, private retirement schemes may be insufficient, with less than 3% of Malaysia's workforce having a Private Retirement Scheme (PRS) account⁶.

These gaps need to be addressed at the national scale, and the financial sector can play a role – in particular, to support greater household wealth accumulation for retirement and individuals to manage longevity risks. It will also be critical to ensure sufficient diversity in financial products and services that are linked to health and income protection – as well as to raise awareness of available products in the market.

Attracting quality investments is important to rebuild buffers that were eroded during the crisis, such as retirement savings

The future of work also presents positive prospects and challenges for jobs, such as the growing gig economy. However, social insurance coverage gaps remain for workers in the informal sector and the self-employed, arising both from the absence of an Employment Insurance System (EIS) equivalent cover and undersubscription to Self-Employment Social Security Scheme (SESS) for employment injury protection. The pandemic surfaced some of these gaps, with workers in these segments being hit particularly hard – amplified by typically lower savings.

As the economy recovers, it will be important to put in place measures to gradually rebuild financial buffers that were affected during the crisis, such as retirement savings and longer-term investments. Meanwhile, priority must continue to be accorded to expand the coverage of social insurance schemes, with private financial sector solutions complementing protection cover needed by this growing segment to build resilience against future economic and financial shocks.

Other socioeconomic factors are also relevant in shaping financial development. Socioeconomic disparities, such as income and wealth inequality – alongside rising cost of living – are relevant considerations. It will be important to ensure that developments in the financial sector continuously strive to be more inclusive, particularly in meeting the needs of individuals and businesses that are unserved and underserved. Financial services will need to remain affordable and accessible, so that it addresses the societal needs of various segments.

Financial literacy gaps will also remain relevant in determining financial development priorities ahead. A recent study found that Malaysians scored below average in financial knowledge, reflecting gaps in financial decision making⁷. Delivery of products and services, in particular innovations, must be supplemented with safeguards. These should aim to preserve sound consumer outcomes, while empowering individuals to make well-informed financial decisions based on their circumstances.

More broadly, the financial sector can play a role in supporting greater social resilience and upward mobility, such as by combining financial services with other services for the customer (e.g. advisory, financial education, capacity-building) and offering more innovative products to help customers grow and secure their wealth. At the very least, the financial sector should avoid further deepening existing disparities, such as through greater household indebtedness for non-productive activities. Competition will continue to be key in advancing these outcomes, especially through the entry of players that target existing market gaps or segments that may be served better.

⁴ Population aged 60 years and over surpassing 15% of the total population.

⁵ Source: EPF (2018), "Social Protection Insight 2018".

⁶ Source: Manulife Investment Management (2019), "A Zoom into Asia's Pension Reform Journey: Different Perspectives of a Multi-pillar Approach".

⁷ Source: OECD, International Network on Financial Education (2020), "International Survey of Adult Financial Literacy".

Climate change and the broader sustainability agenda

The implications of climate change are also becoming more evident. Climate-related events – such as storms, flooding, droughts – have been intensifying in severity and frequency. The knock-on effects can go beyond nature and affect livelihoods, food security, and businesses. There can be further risks to financial stability as the health and resilience of the financial sector are linked to the broader economy.



Efforts to reinvigorate the economy must aim for a greener model of growth. Tackling this challenge requires making bold policy decisions including adopting carbon pricing, ensuring energy security as a key priority, and formulating a stronger international cooperation framework. As a signatory to the Paris Agreement, Malaysia has committed to reduce greenhouse gas (GHG) emissions by 45% by 2030, and a further 60% in 2035 compared to 2005 levels. As the central bank, we are equally committed to foster a climate-resilient financial sector that also supports an orderly transition to a low-carbon economy, in line with the Paris goals and the Government's longer-term commitment to become a net zero nation.

Malaysia's efforts will also contribute to the growing global movement towards promoting greater environmental sustainability. Climate change – and its associated raft of reforms – can be expected to alter the course of economic development. Malaysia's active efforts on this front will preserve the nation's economic competitiveness, especially as more countries introduce climate change legislation, carbon management programmes, and other climate-related initiatives.

Beyond climate change, it will also be timely to advance efforts towards a more sustainable development model. Other issues of environmental well-being, such as those relating to the circular economy and biodiversity, are equally important.

The need for a ‘whole-of-nation’ approach

All crises – including the recent pandemic – come with a unique window of opportunity for reform. Malaysia should seize it. Going forward, Malaysia’s growth must be innovation-led. This will call for reforms that can improve our economic complexity – that is, productivity reflected by the diversity and sophistication of Malaysia’s goods and services. To this end, the National Investment Aspirations (NIA) are important signposts⁸ that aim to attract and promote quality investments, build innovation capacity, and increase both productivity and growth.

Making these things happen will require a concerted, collaborative effort by all stakeholders, be it the public or private sector – a ‘whole-of-government’ and ‘whole-of-nation’ approach. To this end, the RMK12 has set out a range of aspirations and initiatives – among others, to achieve a strong economic recovery, accelerated productivity, higher household incomes, widespread connectivity, improved well-being, and a greener economy. Advancing these goals will be key moving forward.

Complementing these broader strategies, the Bank is committed to ensure that the financial sector continues to provide a conducive environment for sustainable economic growth. This Blueprint will set out how we plan to do this over the next five years. This is further supported by our envisioned outcomes and targets for the financial sector in 2026, as set out in “What success looks like in 2026”.



⁸ The NIAs refer to overarching strategic developmental objectives to increase economic complexity, create high-value jobs, extend domestic industry linkages, and develop new and existing clusters. For further details, please refer to the Box Article titled “Securing Future Growth through Quality Investments” in Bank Negara Malaysia’s Economic and Monetary Review 2019, accessible at https://www.bnm.gov.my/documents/20124/2722983/emr2019_en_box1.pdf

What success looks like in 2026

What success looks like in 2026

Finance for all



Diverse choices for customers, with most preferring digital solutions

- ♦ 'Digital first' solutions available (e.g. invisible payments, digitalised motor claims, smart contracts)
- ♦ High level of trust in reliability and security of online services
- ♦ Accelerated digital payments adoption, with e-payment per capita increasing at a CAGR¹ of higher than 15%

Strengthened financial safety nets, especially for the most vulnerable

- ♦ Insurance/takaful penetration rate at between 4.8% to 5%²
- ♦ Significant increase in take-up of insurance/takaful, with doubling of number of individuals subscribed to microinsurance/microtakaful
- ♦ Growth in social finance solutions and other value-added services (e.g. upskilling)

Confident and capable financial consumers taking charge of their financial futures

- ♦ Improved financial literacy, with narrowing gap between Malaysia's OECD International Network on Financial Education (OECD/INFE) financial literacy scores, and the average score of OECD members
- ♦ Consumer protection reforms (e.g. CCA³ and CCOB⁴, single regulatory regime for financial advisors and financial planners)

Finance for transformation



Significant growth in alternative finance, supporting innovative ventures

- ♦ Steady growth in alternative finance channelled to new, innovative enterprises (e.g. early-stage, asset-light, technology intensive)
- ♦ Greater use of alternative data alongside traditional metrics for more differentiated pricing and inclusion

Deeper global integration, including in Islamic finance

- ♦ Faster, cheaper, more accessible and transparent cross-border payments in line with the Group of Twenty (G20) roadmap
- ♦ Malaysia continues to be recognised as global leader in Islamic finance

Vibrant and dynamic financial landscape

- ♦ Healthy competition driving continuous innovation to better serve customers
- ♦ Regulatory environment recognised as conducive for digital financial innovation
- ♦ Open and interoperable infrastructures (e.g. payment systems, technical standards for data sharing)

Finance for sustainability



Wider adoption of VBI to serve the economy, community and environment

- ♦ Steady growth in VBI-aligned assets, with a growing share by conventional banks and insurers
- ♦ Better quality disclosures to support market incentives for more responsible and ethical finance

Steady progress in greening finance and financing green

- ♦ Strengthened practices to assess, measure, disclose and manage climate risk
- ♦ Increasing share of financial flows towards climate supporting and transitioning activities – by 2026, more than 50% of new financing classified as C1, C2 and C3 under the CCPT⁵
- ♦ Financial institutions provide meaningful support to help customers transition

¹ Compounded annual growth rate

² As a percentage of GDP

³ Consumer Credit Act

⁴ Consumer Credit Oversight Board

⁵ Climate Change and Principle-based

Taxonomy, where C1, C2 and C3 represent economic activities that are classified as "climate supporting" or "transitioning" in terms of their contribution towards climate and environmental objectives



... underpinned by stable and resilient foundations
anchored on the Bank's mandates to promote monetary and financial stability

Our regulatory focus for financial development

Broadly, our regulatory focus will be to:

- Foster market dynamism;
- Support sustainable development objectives; and
- Remain anchored on our mandate to promote monetary and financial stability conducive for sustainable economic growth.

These underpin the strategies set out in the Blueprint and are further articulated in the remainder of this chapter.

Fostering market dynamism

With various major forces of change at play, the next stage of Malaysia's financial development journey takes place in a landscape that is extraordinarily uncertain. At the same time, Malaysia's financial sector is now more well-developed. Unlike the decades before, gaps that demand strong regulatory involvement may be less obvious.

In such an environment, fostering greater market dynamism is critical for the financial sector to adapt effectively to a wide range of scenarios.

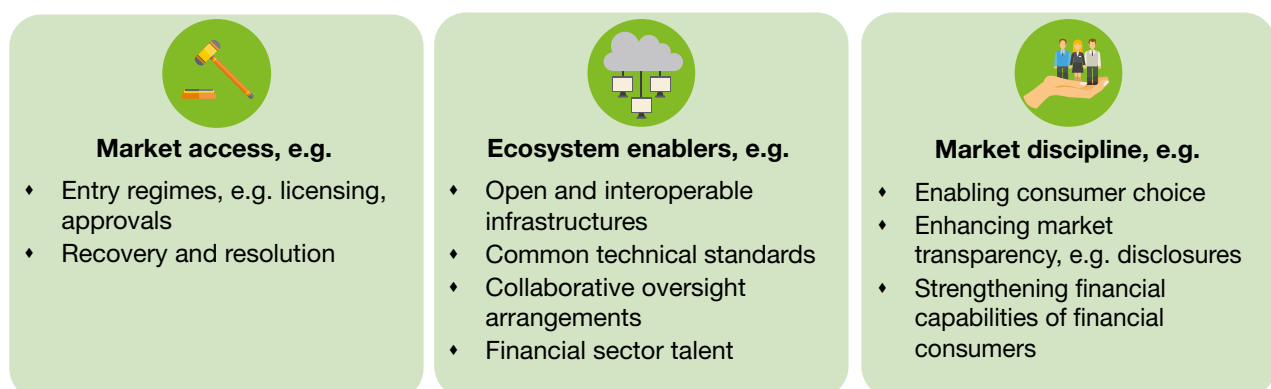
Regulatory efforts will aim to foster the right conditions for these outcomes, through targeted interventions to remove undue barriers to competition and innovation, as well as to address market failures. Priority will be given to ensure the well-functioning of three key market mechanisms – namely, market access, ecosystem enablers, and market discipline (Diagram 1).

In relation to these market mechanisms, our focus will be to:

- Address undue barriers to market entry, while ensuring orderly exit;
- Promote 'co-opetition' efforts for critical ecosystem enablers; and
- Strengthen conditions for market discipline focusing on more empowered consumers.

We will aim to foster the right conditions for a highly adaptive financial sector

Diagram 1:
Key elements of market dynamism



Address undue barriers to market entry, while ensuring orderly exit

Entry regimes will be designed based on principles of parity and proportionality. This means that the same types of risks will be regulated the same way ('parity'), with the intensity of regulatory requirements calibrated in a way that is commensurate with the level of risk ('proportionality').

This may entail graduated entry pathways – where a new entrant is gradually transitioned into the existing regulatory framework for incumbents – to better reflect the risk profile and stage of development of a new entrant. An example of this is the foundational phase in our licensing framework for digital banks.

A more managed approach to market entry will continue to be adopted. In determining the number of new licences, we will seek to avoid excessive fragmentation in the financial sector – which creates inefficiencies and vulnerabilities that can jeopardise public interests and financial stability. Our aim will be

We are keen to ensure that new players contribute towards addressing prevailing gaps

to facilitate the entry of new players that contribute towards addressing prevailing gaps – such as in advancing greater financial inclusion.

More broadly, we remain guided by our continuing objectives to promote market participation in a way that serves the best interest of Malaysia, as set out in the FSA and IFSA. Maintaining a strong core of resilient and competitive domestic institutions will continue to be an important consideration – particularly for stability-critical areas (e.g. systemically important infrastructures). This reflects the important role of domestic institutions as a countercyclical force during times of unanticipated shocks, volatilities or uncertainties, as shown in past crises.

In any competitive market, the possible exit of individual players must also be expected. We see this as an important part of the creative destruction process, which creates more dynamic and adaptive players. This in turn makes Malaysia's financial ecosystem stronger and more resilient in the longer-term. In this regard, we do not aim for 'zero failures'. Instead, we focus on reducing the risks and impact when failures happen, such as by requiring financial institutions to have clear exit plans for winding up business operations in a way that is not disruptive.

Promote 'co-opetition' and public-private partnerships for critical ecosystem enablers

We will promote collaboration and coordination among relevant stakeholders to address ecosystem-wide issues. These include developing shared infrastructures, technical standards, and other protocols to increase efficiency and encourage innovation – which are preconditions for market dynamism.

This is consistent with the principle of 'co-opetition' – where industry players pool resources to develop ecosystem enablers, such as shared infrastructures – which we have long promoted. The resultant efficiency gains will deliver more affordable services to end-users, such as consumers and businesses. Meanwhile, competition would be intensified at the product level, with industry players aiming to differentiate themselves through value-added features that better serve end-users.

We expect industry players to ultimately take the lead in making these collective decisions to promote more sustainable outcomes that advance common interests, while taking into account longer-term commercial implications for industry players. Industry associations, as well as public-private partnerships, can play a vital role in this regard. A key success factor to greater industry leadership will be financial sector talent (refer to the box article "Futureproofing the financial sector workforce").

We will facilitate industry efforts to collaborate effectively on ecosystem enablers, such as infrastructures and technical standards

On our part as the central bank, we will aim to facilitate collective actions among industry players, complementing our stability mandates. In doing so, we will seek to preserve and encourage healthy competition among industry players. We will focus our interventions on situations where there are clear red flags of market failures or risks to the system. This may be where desirable collective efforts – namely, those that advance public interests – are not forthcoming due to overly dominant short-term or competing commercial interests. Fear of first-mover disadvantage, or the desire to shut out competition, are some of these red flags.

Strengthen conditions for market discipline focusing on more empowered financial consumers

We will seek to promote better informed decisions by financial consumers. Combined with competition, consumer choice provides strong incentives for financial institutions to address pain points faced by their customers, or to innovate to attract new ones.

To this end, our longstanding efforts to help consumers make well-informed decisions continue to be essential. This includes ensuring that consumers have access to the right information, and in a way that is easy to navigate and understand.

Another relevant factor is for financial consumers – upon being better informed – to be able to seamlessly act on their preferences. In this regard, we will continue to collaborate with other stakeholders to explore ways to make it easier for consumers to change their FSPs – namely, lowering ‘switching costs’. This will take into account the need for minimum protections to safeguard consumers against fraud and abuse, as well as the implications to the overall resilience of the financial system.

We will also aim to promote open and interoperable design principles for key financial infrastructures, such as to futureproof access to payment and settlement systems and to promote open data initiatives. We see this as a natural evolution of the financial sector, as business models become more diverse and to some extent, less bank-centric. In these efforts, our key focus on preserving the overall resilience of these infrastructures will remain.

In parallel with efforts to empower consumers further, we will also continue to strengthen standards of conduct applied to financial institutions to deliver fair consumer outcomes. This will be reinforced by the use of our supervisory and enforcement levers to give effect to these outcomes. Continued financial education efforts will therefore also be critical to progressively elevate the financial capability of Malaysians.

In addition, we will advance our current collaboration with the Ministry of Finance (MOF) and the Securities Commission (SC) to pursue reforms to Malaysia’s legal and regulatory architecture for conduct oversight. These aim to provide stronger and more consistent protection for financial consumers across FSPs that are currently subject to different levels of formal oversight – aiming to better align expectations on business conduct and fair treatment of financial consumers across the industry.

Reforms to Malaysia’s legal and regulatory architecture for conduct oversight will be advanced together with the MOF and the SC



BANK NEGARA MALAYSIA

Support sustainable development objectives

As the financial sector navigates development opportunities, it will be important to ensure that we move towards a more sustainable, inclusive, and responsible future. We remain committed to this outcome, which will contribute towards supporting the United Nations Sustainable Development Goals (SDGs).

Diagram 2:
Focus areas for sustainable development



Efforts to promote sustainable development objectives will aim to:

- Mainstream VBI;
- Address needs of the unserved and underserved; and
- Support greater climate resilience and a more environmentally sustainable growth model.

Signposts in the financial development journey ahead will be important to ensure a more sustainable, inclusive, and responsible future

Mainstream VBI

VBI will continue to be a key framework to guide our financial development initiatives. Introduced in 2017, VBI emphasises the need for financial services to have a clear and distinct focus on generating a positive impact on the economy, community, and environment.

While the earlier stages saw a major role by Islamic financial institutions, the objectives and principles of VBI are universal. We envision these considerations to be gradually mainstreamed moving forward, with more financial institutions committing to the VBI agenda.

Address needs of the unserved and underserved

Our continued work to support inclusive financial services will be a major thrust of that broader vision. As we look at enabling new business models and other innovations, we will seek to prioritise those that can better address the needs of the unserved and underserved. We emphasised this when we introduced the digital banking licensing framework for Malaysia. Within the funding ecosystem, we will also implement initiatives and accelerate institutional reforms – working with the relevant stakeholders – to ensure key segments in the economy (e.g. SMEs) have continued access to finance, including alternative finance solutions. Other areas that we will be paying greater attention to in the next few years will include more inclusive models for insurance/takaful, as well as social finance.

Support greater climate resilience and a more environmentally sustainable growth model

Environment-related initiatives will also be a major area of focus. Our priority here is to ensure that Malaysia's financial sector effectively evaluates and mitigates risks arising from climate change. We will seek to enhance prudential frameworks in this regard, as well as our broader surveillance capabilities to better assess the complex implications of climate risk on the financial sector. We will also actively consider opportunities for finance to play a catalytic role in supporting the transition to a low-carbon economy.



Across these efforts, we are committed to work together with various other stakeholders – from the Government, businesses and civil society – to support Malaysia's broader efforts to combat climate change.

Promoting monetary and financial stability

Our efforts to promote greater market dynamism and sustainable development outcomes will continue to be firmly anchored on our monetary and financial stability mandates. To this end, the Blueprint clarifies outcomes and principles for financial development in ways that are aligned with our core mandates – including what is clearly beyond our appetite, given major implications to public interests.

Diagram 3: Monetary and financial stability priorities



Ensure continued monetary policy efficacy

We will continue to ensure our monetary policy framework, strategies and tools remain effective in a changing financial landscape



Intensify efforts to safeguard resilience and integrity of the broader financial ecosystem

Regulations and supervision must remain effective against emerging risks (e.g. operational resilience, cyber risks, money laundering and terrorism financing (ML/TF)), avoid procyclicality, and minimise regulatory arbitrage – with strengthened collaborative oversight arrangements as different activities (including beyond the financial sector) become more interlinked

Ensure continued monetary policy efficacy

We will seek to preserve monetary policy efficacy amid the changing environment. The megatrends we outlined in the previous chapter – relating to macroeconomic conditions, technological change, demographics, and climate change – may have important implications for the conduct of monetary policy.

The emergence of digital assets and currencies will likely have an impact on the effectiveness of monetary policy transmission, while the linkages between climate risk and the broader macroeconomic conditions may give rise to new considerations for the conduct of

monetary policy. In addition, the diversification into non-debt based finance, including the increasing use of alternative finance instruments, will likely affect the relative importance of the traditional interest rate channel in the transmission of monetary policy.

To this end, we will assess our monetary policy framework, strategies, and tools to ensure that these remain fit-for-purpose in the years to come. This is to ensure that we are well-positioned to continue to achieve our core mandate of monetary stability and orderly market conditions in this changing landscape.

Intensify efforts to safeguard resilience and integrity of the broader financial ecosystem

We will aim to ensure that financial development efforts – whether by us or the industry – do not erode system-wide resilience and financial integrity. To this end, we remain committed to continuously enhance our regulatory frameworks in line with international standards – such as those set out by the Basel Committee on Banking Supervision (BCBS), International Association for Insurance Supervisors (IAIS), IFSB, and Financial Action Task Force (FATF) – where appropriate and relevant.

A crucial consideration moving forward will be the blurring boundaries in the landscape – be it across financial services, or between financial and non-financial sectors. Public interest objectives that were previously clearly demarcated are also becoming more interconnected. Issues relating to stability, competition, conduct, inclusion, and privacy – for example – are increasingly intertwined in the sphere of digital financial services.

Against this backdrop, it is vital to ensure the continued effectiveness of oversight arrangements and coordination at the ecosystem level – including to address the build-up of financial imbalances within the system (e.g. unsustainable levels of leverage or asset bubbles), as well as in fighting financial crime across the financial value chain.

Vital to ensure effective oversight at the ecosystem level, given blurring of boundaries in the financial landscape

To that end, we will review – and where appropriate, strengthen – current oversight arrangements for non-banks, be it for smaller entrants or larger non-bank financial institutions. This considers the potentially heightened risks of regulatory arbitrage, and deepened interlinkages beyond the financial sector, such as with third party service providers (TPSPs) and other partners of financial institutions. This is particularly relevant for risks to operational resilience, including those from cyber threats, and Anti-Money Laundering and Countering Financing of Terrorism (AML/CFT) concerns where the ecosystem may be only as strong as the weakest link.

Efforts will also be undertaken to advance shared priorities among the financial regulatory community. This will be supported by continued efforts to strengthen inter-agency coordination to ensure existing laws and regulations are administered effectively in a more complex landscape. We will also work with other regulatory authorities to identify areas for enhancement. These may include streamlining of regulatory processes, or longer-term measures that may call for new or enhanced legislation.

Five strategic thrusts for 2022-2026

In giving effect to our regulatory focus for financial development, we are driven by five strategic thrusts that are set out in the following chapters:

1. Fund Malaysia's economic transformation
2. Elevate the financial well-being of households and businesses
3. Advance digitalisation of the financial sector
4. Position the financial system to facilitate an orderly transition to a greener economy
5. Advance value-based finance through Islamic finance leadership

Box Article

Futureproofing the financial sector workforce

Introduction

A competent and highly skilled workforce is critical for the financial system to function effectively. Over the past decade, the size of Malaysia's financial sector¹ workforce grew by 16% (2020: 166,360), driven by a larger proportion of higher skilled workers. Employment conditions in the sector remained resilient amid challenging times throughout the pandemic. The financial sector has continued to be a net creator of jobs, led by the banking sector. Net jobs gained after layoffs and discharges remained robust, averaging above 4,000 jobs per year over the past three years².

As the financial sector continues to evolve, jobs and skills will transform in tandem. The next stage of Malaysia's financial development journey will require a more adaptive workforce that is agile and equipped with skillsets of the future to effectively perform their role.



¹ Unless otherwise specified, "financial sector" in this box article comprises banking institutions (includes development financial institutions), insurers and takaful operators.

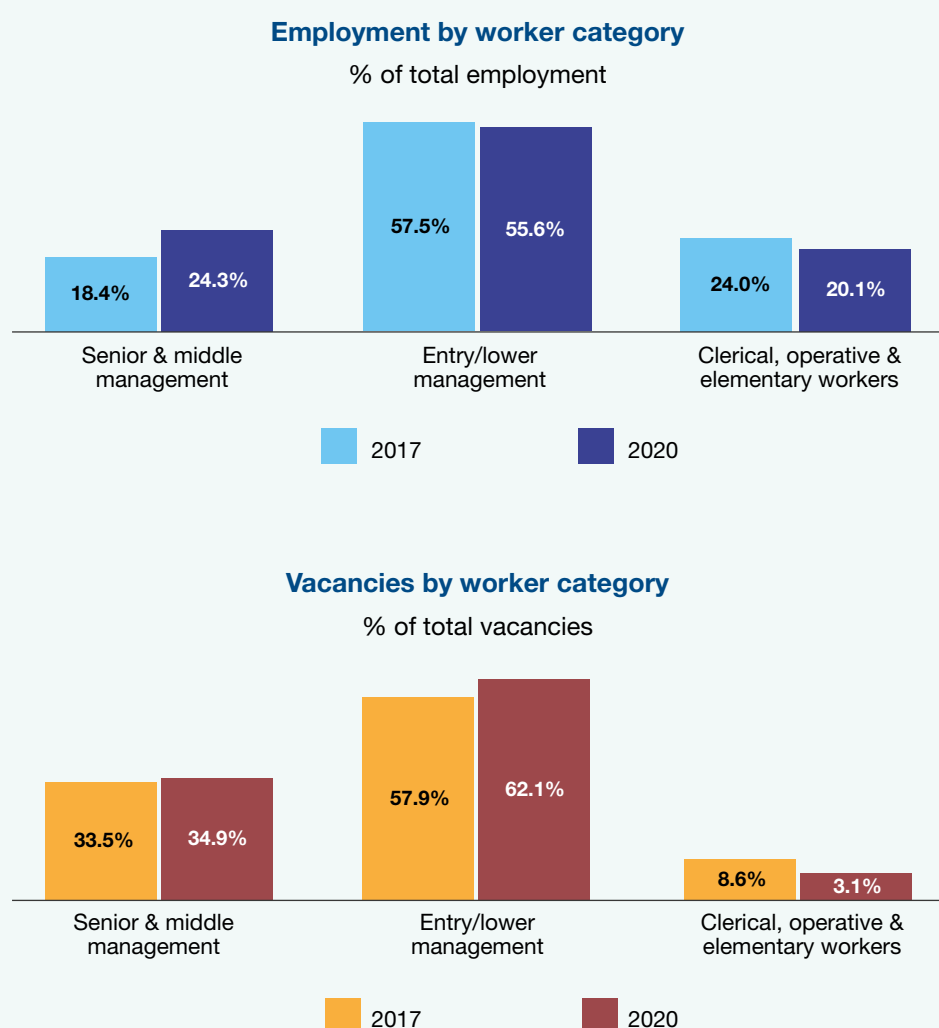
² Data on net jobs gained after layoffs and discharges is collected from 2016 onwards through the Bank's Labour Market Statistics Survey for Financial Services.

Key trends and developments shaping the future workforce

Continued demand and job opportunities for higher skilled talent

The financial sector continues to observe healthy demand for senior and middle management level talent³ (Chart 1). Job vacancies for senior, middle and entry/lower-level management⁴ increased over the last few years, indicating that job opportunities in these categories remain healthy amidst sizeable unmet demand. In contrast, demand for lower skilled and routine-based roles in the financial sector weakened – the proportion of job vacancies for clerical, operative and elementary⁵ workers over total vacancies fell by 5.5%, alongside a decline in the proportion of employment for this segment.

Chart 1:
Employment and job vacancies by worker category in the financial sector (2017-2020)



Note: Figures may not necessarily add up due to rounding
Source: Bank Negara Malaysia

³ Equivalent to managers and professionals categorised as Major Group 1 and Major Group 2 respectively under the Malaysia Standard Classification of Occupations (MASCO) 2020.

⁴ Equivalent to technicians and associate professionals categorised as Major Group 3 under MASCO 2020.

⁵ Categorised as Major Group 4 and 9 under MASCO 2020. Primarily performs simple, routine and non-systematic tasks, such as compilation and maintenance of financial transaction records and other information of business activities as well as general and miscellaneous functions.

Growing need for a workforce with strong digital skills and acumen

As Malaysia's digital economy continues to expand, we expect to see an acceleration of digital transformation in the financial sector. This reinforces the need for talent who are able to learn, apply, and deploy emerging business models as well as new technologies. It also demands a workforce that is more digitally savvy as a whole – with the ability to innovate and integrate business concepts with technology and data (see Diagram 1 for further details). Globally, there is an urgent need to fill in the digital skills gap for readily available talent, with skills shortage in local labour markets perceived as the largest barrier for organisations to harness the growth potential from new technologies⁶.

The future of work and skills required is multifaceted

The transformation of work in the financial sector will be felt across various dimensions. The most significant transformation will be in terms of how we work, skills, and people management. Flexible work arrangements and acceptance of part-time or gig workers into the workforce is anticipated to be more widely adopted, enabled through greater use of data, strengthened cyber resilience and governance arrangements. Automation of routine-based tasks will see existing jobs evolve to require higher levels of human creativity, judgement, and interpersonal skills. For instance, with greater adoption of AI, individuals staffing call centres will take on an added level of complexity in their roles that requires them to contextualise, apply empathy, and exercise judgement in assisting consumers to solve problems.

Emerging consumer and business priorities continuously reshape what it takes to remain effective in job roles

Financial services providers with innovative product designs and personalised financial solutions that cater to the needs of discerning consumers will have a competitive edge. This however will require talent equipped with up-to-date knowledge of consumer or business-specific needs, that would enable financial institutions to innovate and capitalise on these opportunities. It will also be important for the workforce to keep abreast with emerging developments and priorities – such as SDGs, climate risks, value-based finance and social finance – to continuously deliver value to consumers.

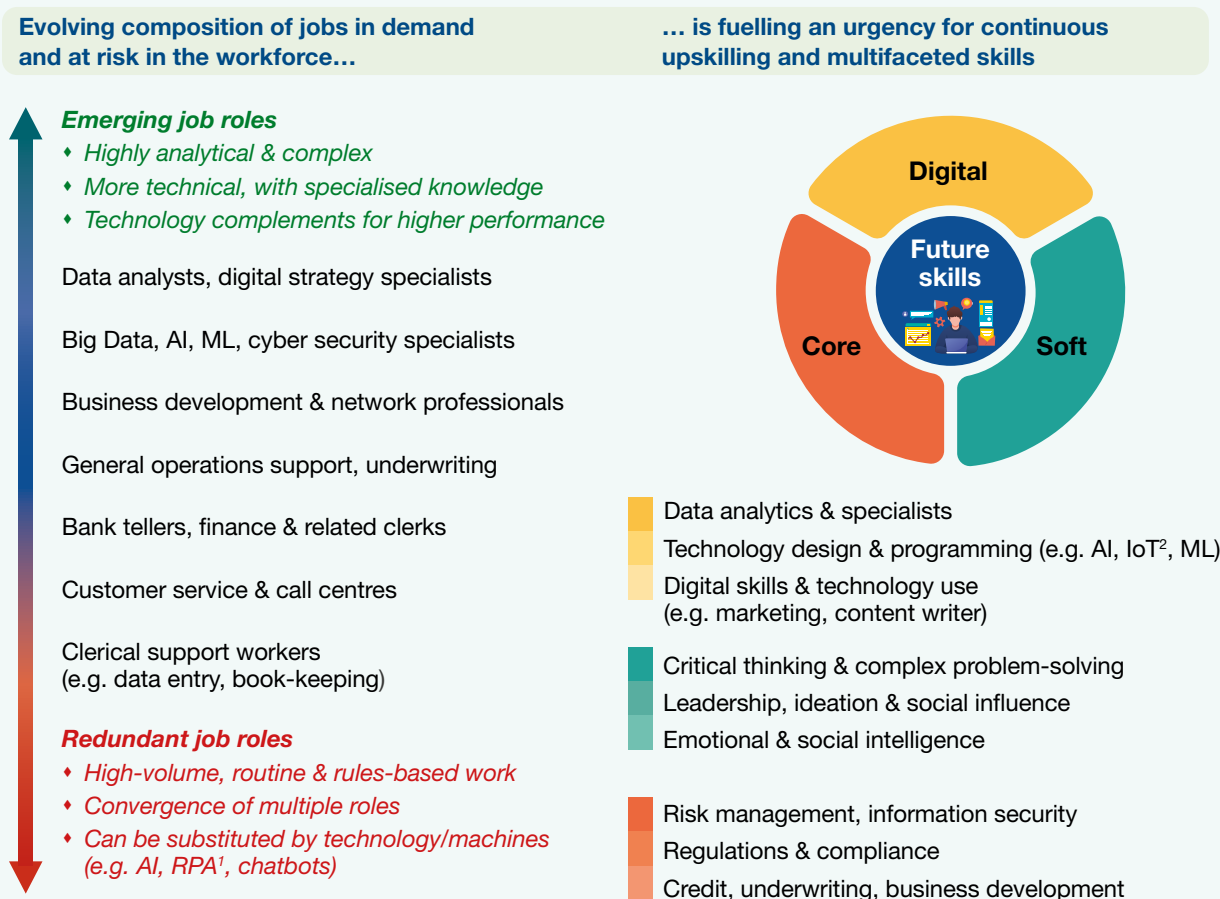
Shorter shelf-life of skills demands constant reskilling and upskilling

With various forces of change at play going into the future, the ability to quickly adapt to the new operating environment will be critical. Financial sector talent must continuously learn new skills to remain relevant and be ready to grasp new opportunities. This needs to be supported by access to comprehensive upskilling and learning infrastructures made available for the workforce, both at an industry-wide and organisation level.

⁶ This finding is consistent across 20 of the 26 advanced and developing economies (including Malaysia) surveyed in *The Future of Jobs Report 2020* by the World Economic Forum.

Collectively, these trends are expected to drive the evolution of jobs and skills – both in terms of jobs creation and jobs at risk of displacement. Certain capabilities and skillsets will become more pronounced, while certain roles will be re-engineered to complement business transformation (Diagram 1).

Diagram 1:
Anticipated evolution of jobs and skills of the financial sector workforce



¹ Robotic process automation (RPA)

² Internet of Things (IoT)

Source: World Economic Forum, Bank Negara Malaysia

Preparing the workforce for the future: priorities moving forward

As we move ahead, financial institutions must intensify the focus on their people. The challenge faced by financial institutions to upskill and reskill their workforce is significant – for most institutions, bridging the skills gap is a challenge that cannot be solved alone. A dynamic and sustainable talent ecosystem is thus crucial to continuously enhance talent capabilities and support the transition of the financial sector workforce.

This is an area where we see a continued need for the industry to come together to take collective action. Over the last decade, notable progress was made to raise the professionalism of the workforce and strengthen institutional infrastructures for talent development. Enhancements to the quality and diversity of training programmes facilitated upskilling – a greater proportion of the workforce today is equipped with accredited professional certifications from a wide range of programmes covering leadership development, ethics modules, and specialised certification tracks in key functions. Importantly, Malaysia also continues to be globally recognised as a leader in Islamic finance talent development.

Going forward, strong industry-led initiatives to further develop the talent ecosystem will remain crucial to effectively prepare the workforce for the future. We envision this outcome to be holistically driven by various stakeholders and leaders in the financial sector – industry associations, FSPs, training providers, professional bodies, institutions of higher learning, and union groups all play important roles to identify key skills needs and training gaps for the workforce.

To this end, two key priorities that will pave the way towards a more dynamic and sustainable industry-led talent ecosystem – including for Islamic finance talent – will be pursued in the immediate horizon.

First, develop and implement a Future Skills Framework for the financial sector

Given the multifaceted skills needs of financial services, a primary focus for the sector will be to establish an industry-led framework that identifies skills required, job expectations as well as career development pathways for individuals currently working in or aspiring to work in financial services. Over the long-term, this is envisioned to support several key outcomes for the financial services workforce – it identifies roles with an acute skills shortage, matches skills to jobs available, facilitates talent mobility across different roles, enables training providers to respond to training needs, and supports individuals to chart their own professional development paths. To complement this, continuous efforts to raise the professionalism of the workforce through higher standards of professional programmes and qualifications for various career pathways – from risk specialists to loss adjusters – will also be important. The framework should be designed to benefit multiple stakeholders across the financial sector talent ecosystem, enabling each actor to make better informed decisions and play its role effectively (Diagram 2).

Early job impact identification and mitigation plans are important to enable recalibration of the workforce towards new roles – and something we expect all financial institutions to drive. Nonetheless, we recognise that some job losses may be inevitable. A whole-of-industry approach is thus important to ensure appropriate supporting mechanisms are in place to minimise the impact of job displacement on livelihoods and support an orderly transition of the affected workforce to jobs in other organisations or economic sectors. Such support may include, among others, appropriate compensation, financial support to reskill and outplacement assistance.

The impact of new business models and technological advancement on the evolution of jobs and skills is ubiquitous – its effects will be felt not only by the financial services sector, but Malaysia's workforce as a whole. A coordinated effort to reduce fragmentation and advance the implementation of a holistic future skills framework for Malaysia at a national level would complement the Financial Sector Skills Framework to unlock greater benefits and synergies in cross-sector talent mobility.



Diagram 2:
Envisioned outcomes and benefits of a Future Skills Framework for the financial sector



Second, align existing requirements on training and development applicable to financial institutions

We will undertake a holistic review of requirements on staff training and development applicable to financial institutions, with a view to uplift the Staff Training Expenditure (STE) policy in 2022 and Staff Training Fund (STF) policy by end-2026. We will also engage with the financial industry to explore opportunities for more effective coordination, synergies, and collaboration across the financial sector talent ecosystem – particularly where it will serve to deepen the talent pool for the financial industry and encourage talent growth and mobility.

Box Article

Medium-term priorities for the prudential framework and anti-money laundering and countering financing of terrorism (AML/CFT)

The recent pandemic has underscored the importance of prudent risk-taking and building up buffers in good times – so that the financial system can cushion unexpected shocks during a crisis and be an effective countercyclical force to support economic recovery. We will continue to ensure the continued effectiveness of Bank Negara Malaysia's prudential framework for financial institutions, with the focus areas outlined below for the next five years.

Basel III capital requirements

Introduced in the wake of the 2008 Global Financial Crisis, the Basel III reforms have been integral in promoting the resilience of the global banking system. Over the years, Malaysia has implemented most of the key elements of this reform package – particularly the minimum capital requirements, leverage ratio, and liquidity standards.

Our priority ahead will be to review and implement Basel III reforms related to the computation of risk-weighted assets – with a focus on credit risk, operational risk, counterparty credit risk, securitisation, and exposures to central counterparties. We will also review the Single Counterparty Exposure Limit (SCEL) policy to take into account developments in international standards on large exposures where relevant. This will include potential refinements to the limit, scope of eligible collateral, and treatment of specific exposures (e.g. to sovereigns, central counterparties and intragroup entities).

As with existing practice, in the adoption of international standards, we will carefully consider relevant applications in the Malaysian context, as well as the expanding footprint of Malaysian financial institutions abroad. Where relevant, we will also continue to ensure that regulatory standards are proportionate to the risks at hand, while taking into account the industry's operational readiness and the need for transition arrangements.



Risk-Based Capital Framework for Insurers and Takaful Operators (RBC/T)

Since the implementation of the RBC/T in 2009 for insurers and 2014 for takaful operators, market conditions have evolved alongside greater product innovation and the introduction of new takaful models and Shariah contracts. New global regulatory measures such as the Risk-based Global Insurance Capital Standards (ICS) developed by the IAIS have also paved the way for greater convergence on international capital adequacy standards.

In line with these developments, we have commenced a holistic review of the RBC/T to ensure its continued effectiveness to respond to new and emerging risks, as well as to align measurement practices across the insurance and takaful industry. This should enable the insurers and takaful operators (ITOs) to align their business strategies and remain competitive. We intend to broadly align our RBC/T with the ICS, both in terms of the framework design and timeline. In the years ahead, we will also seek to build upon the industry feedback on proposed enhancements to the RBC/T, particularly on the appropriateness of broad design elements to the different business models.

The review will also consider Shariah principles to facilitate greater fungibility of capital between takaful funds, which is currently restricted to reflect different ownership of individual funds. These considerations will include *ta'awun* (mutual assistance) for surpluses in a particular takaful fund – in excess of capital requirements at the fund level – to be used to support another takaful fund.

AML/CFT measures

As the competent authority under the Anti-Money Laundering, Anti-Terrorism Financing and Proceeds of Unlawful Activities Act 2001 (AMLA), we remain committed to drive a robust national AML/CFT regime. In doing so, we have led efforts to establish the necessary mechanisms and initiatives for effective prevention, investigation, and prosecution of financial crimes, in collaboration with the domestic law enforcement agencies (LEAs), reporting institutions, foreign financial intelligence units, regional and international groups, as well as other relevant stakeholders.

In this regard, our medium-term priorities for preserving the integrity of the financial system will continue to build on the established collaboration mechanisms, while targeting mitigation of the ML/TF risks identified in the recently concluded National Risk Assessment 2020 (NRA 2020)¹. Overall, our strategies will be anchored on three key thrusts.

First, we will explore integrated efforts to improve coordination to better prevent, detect, disrupt and dismantle financial crimes at the earliest opportunity, prioritising highest-risk crime, namely fraud and crimes with elements of organised criminal syndicates. This includes the development of an information sharing platform between participating financial institutions and relevant LEAs to minimise the dissipation of scammed funds and leveraging on the National Anti-Financial Crime Centre (NFCC) to conduct joint intelligence and investigation focusing on organised criminal groups.

¹ The NRA 2020 had identified that the banking system, remittance services and designated payment instruments continue to be abused to facilitate top five high risk crimes – fraud, corruption, smuggling, illicit drug trafficking and organised crimes. This is further aggravated by increasing digitalisation in the financial sector and the swift nature of domestic and cross-border transactions.

Second, we will continue to further our understanding of the emerging and higher ML/TF risk areas, involving financial and non-financial sectors, to provide responsive mitigating policies and guidance to reporting institutions. Among others, we will focus on assessing the key ML/TF risk drivers identified in the NRA 2020, such as the growing use of virtual assets and technology to facilitate financial crimes and the exposure emanating from digitalisation of financial services or digital banking. Emphasis will also be placed on other high-risk areas, such as the abuse of shell and shelf companies, or professional services.

Third, consistent with regional and global developments, we will encourage industry-led collaborative initiatives to drive more efficient practices and strengthen the compliance culture in the industry. These initiatives include the issuance of sector-driven AML/CFT guidance or best practices to streamline the implementation of specific measures, development of professionally qualified or certified subject matter experts through accreditation or train-the-trainer programmes, as well as development of shared infrastructure or solutions for effective monitoring and information sharing on ML/TF risks.

Responsibility mapping

We will finalise the Responsibility Mapping Framework, which was proposed at end-2019 before the onset of the pandemic. Reflecting the importance of the tone-from-the-top, the framework aims to ensure that responsibilities for key functions, including those prescribed by laws and regulations, are clearly allocated to individuals at senior levels.

By enabling greater clarity and transparency in the governance and accountability of individuals in the financial institutions, the framework supports several important outcomes. These include facilitating meaningful regulatory engagements with the board of directors of financial institutions on the operations and decision-making process of the financial institution, driving better decisions through strengthened incentives for good conduct and culture, and allowing institutions to address barriers that may prevent key individuals from carrying out their duties effectively. In the longer term, these internal transformations will be key to bolster the industry's long-term financial soundness – and in turn, their continued ability to fulfil their obligations and meet the customers' needs.



Risk Management in Technology (RMiT)

The rapid pace of change in the digital landscape means that regulatory expectations must evolve in tandem to remain effective. We will prioritise fine-tuning the RMiT policy, which is a central piece of the regulatory framework for technology risk management. Efforts on the RMiT in particular will be guided by four thrusts.

First, we will ensure greater supervisory focus on how financial institutions manage risks from TPSPs. Our supervisory activities will focus on financial institutions' overall governance, due diligence, continuous monitoring, and data protection – and whether safeguards are commensurate with the scope of services provided and criticality of information being processed by TPSPs. The goal will be to ensure that TPSPs do not become the 'weakest link' in the supply chain. Complementing this, we will also explore supporting broader initiatives to develop common standards for TPSPs in relation to governance and risk management, in line with the interest among TPSPs to bolster confidence on the robustness of their services. This may entail leveraging the RMiT as a baseline for TPSPs to develop such standards.

Importantly, heightened supervisory focus in this area complements the broader digitalisation strategies in the Blueprint – particularly on regulatory oversight and cyber security (refer to the chapter "Advancing digitalisation of the financial sector"), which emphasise the need to consider the broadening perimeter of risks, including those arising from greater partnerships with TPSPs.

Second, we will enhance our guidance to the industry on cloud service management. We will consider various possible models for future oversight arrangements, with the desired outcome of establishing assurance that cloud service providers (CSPs) are mitigating risks effectively. To this end, it will be important for industry players to strengthen their capacity in understanding these operations, particularly the resultant risks to financial institutions – rather than solely relying on the CSPs or appointed TPSPs for knowledge and expertise on cloud-related arrangements. We will look to financial institutions to have a clear roadmap in building internal capabilities in this regard.

Third, we will heighten our scrutiny on the implementation of 'high availability' infrastructures. Such infrastructures include online financial services, for which there is a reasonable expectation for minimal disruptions or continued service availability by customers and counterparties. Maintaining a high level of uptime is therefore crucial, particularly to preserve confidence in the financial sector. As industry players are making encouraging progress in this regard, we will remain open to different approaches by respective financial institutions to build greater operational resilience into their 'high availability' infrastructures.

Fourth, the Bank will explore allowing financial institutions to rely on their internal risk function in conducting risk assessment, as the industry's infrastructure and practices mature. Currently, the use of external service providers for independent assessment is required in the RMiT. We expect financial institutions to leverage these external assurance arrangements to build internal capacity for technology risk management.

Recovery and resolution planning

In recent years, we have collaborated with Malaysia Deposit Insurance Corporation (PIDM) to establish a policy framework to implement recovery and resolution planning (RRP) for financial institutions in Malaysia – guided by the Financial Stability Board's (FSB) Key Attributes of Effective Resolution Regimes for Financial Institutions. This framework serves to ensure continued resilience of the financial system in times of distress and avert episodes of financial institution failure that could threaten financial stability.

With the release of the Recovery Planning policy in July 2021, the recovery plans in Malaysia will be implemented on a phased approach. Our immediate focus will be on financial institutions under the first phase of the roll-out plan, with first submissions from banks on their recovery plans expected in 2023. These recovery plans will serve as an important starting point to support PIDM's resolvability assessments and resolution plans.



Strategic Thrusts

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Strategic Thrust 1

Fund Malaysia's economic transformation

As Malaysia continues its transformation to become a high-income, high value-added economy, a vibrant and resilient funding ecosystem will be key. The immediate focus will be for the financial sector to provide continued support in the path to a sustainable recovery. Alongside this, the financing and investment landscape must evolve to support a dynamic model of economic growth – one that is innovation-led, with highly productive and internationally competitive firms.

With this in mind, we will advance three strategies (Diagram 1).

Diagram 1:
Fund Malaysia's economic transformation



A

Sustain a strong economic recovery

- ◆ Strengthen counter-cyclical measures for continued access to financing
- ◆ Support measures for distressed borrowers to manage debt burden
- ◆ Facilitate 'second chances' for non-viable borrowers



B

Facilitate transformation to a high-income nation

- ◆ Sustain and grow alternative finance and its supporting infrastructure
- ◆ Strengthen the regulatory framework and collaboration to promote development of the non-debt finance ecosystem
- ◆ Reinforce the finance ecosystem for microenterprises for sustainable and inclusive growth



C

Ensure post-pandemic resilience of financial intermediation role

- ◆ Preserve funding capacity in the long-term
- ◆ Strengthen vibrancy and resilience of financial markets to act as an absorber of risk

Strategy 1A **Sustain a strong economic recovery**

A swift and robust recovery from the pandemic is paramount. Even as economic conditions improve, progress may be uneven, with possible challenges remaining for the lives and livelihoods of Malaysians.

The financial sector has the capacity to continue supporting the broader economic recovery, and in particular, affected households and businesses. The focus of our strategies is to ensure viable borrowers continue to have access to finance, while at the same time assist non-viable borrowers towards orderly resolution arrangements. In considering these strategies, we will also uphold value-based finance principles – that is, combining the dual objectives of profit and social responsibility, to create a positive impact on the economy, society, and environment.

To this end, we will seek to advance the following:

- i. Strengthen counter-cyclical measures for continued access to financing;
- ii. Support measures for distressed borrowers to manage debt burden; and
- iii. Facilitate 'second chances' for non-viable borrowers.



i Strengthen counter-cyclical measures for continued access to financing

- We will review the **credit guarantee ecosystem**, where necessary, to ensure that it supports financing. The pandemic has underscored the importance of guarantee facilities in ensuring continued lending in a time of uncertainty. We will work with the industry and Government to expand the capacity of guarantee providers, including the CGC and *Syarikat Jaminan Pembiayaan Perniagaan* (SJPP), to support the evolving financing needs of underserved segments. This includes supporting mid-sized corporates to undertake investments that increase productive capacity, as well as providing credit enhancement for new-to-bank customers and innovative firms in high-growth sectors. Next, we will consider streamlining the respective mandates, risk appetites, and product features of the guarantee providers vis-à-vis their target segments. This is to address any redundancies and overlaps in the guarantee ecosystem.
- We will aim to address the industry's need for **forward-looking and alternative data** to improve financing to target segments, especially to those with limited credit records. The exceptional conditions and policy support measures during the pandemic had substantially affected the reliability of historical credit and non-credit information in providing a risk outlook. In addition, a sole focus on historical data also makes it harder for borrowers with no prior credit history to obtain finance. To address this, we will facilitate banks' access to a **wider range of data sources on borrowers**, such as real-time payment information and analytical tools, to allow for richer and more predictive insights on the credit capacity and quality of borrowers. Beyond harnessing transactional information, we will also work with the industry to explore broader application of behavioural models and tools, such as psychometric assessments, to complement credit underwriting. To drive all these efforts, we will facilitate the implementation of common standards to enable data exchange within and beyond the financial sector. We will also strengthen the digital data governance framework to ensure responsible and ethical use of data, including through appropriate safeguards such as consent frameworks.
- We will strengthen the role of development financial institutions (DFIs) to **bridge financing gaps** to strategic economic sectors and underserved segments through the following measures:
 - First, we will work closely with the Government to successfully complete the **restructuring of the DFI industry**. The multi-year reform, which was announced in 2019, will see a consolidation of the industry, driven by two key outcomes. One, the reforms will introduce a robust and strong governance structure to strengthen the accountability and transparency of DFIs as public institutions and ensure effective delivery of their respective mandates. The restructuring also aims to establish DFIs with larger economies of scale and greater diversification of portfolios to better manage risk. This will allow a more efficient allocation of capital and resources to finance key target segments and align with national development priorities, including growth areas identified under the RMK12.
 - Second, we will continue to build on the implementation of the **performance measurement framework** for DFIs initiated by the Bank in 2018, whereby key result indicators that are development-oriented form part of the Bank's supervisory assessments to better reflect the socioeconomic impact of DFIs' operations. Examples of such indicators include the financing amount approved to first-time borrowers, new jobs created through financed projects, and funds crowd-in from the private sector for underserved or new growth segments. Importantly, these key result indicators are intended to be dynamic and are expected to change over time to reflect the prevailing economic priorities and the focus areas for DFIs. As public institutions, it is important for DFIs to continue to improve on how they report their contribution to the economy, as part of an ongoing commitment to increase transparency and accountability in serving their mandates. This would encourage greater market efficiency in the allocation of economic resources to optimise Malaysia's growth potential.

ii Support measures for distressed borrowers to manage debt burden

- We will facilitate the provision of **targeted support to vulnerable segments** that require additional time to recover from cash flow difficulties. This will be important to minimise permanent scarring from the pandemic. We acknowledge that certain vulnerable segments, both individuals and businesses, may require longer-term repayment assistance to meet their financing obligations. To support these groups, we will work with AKPK and banks to ensure an effective roll-out of repayment relief measures under the Financial Management and Resilience Programme (URUS) and the Financial Resilience Support Scheme (FIRST). Under these programmes, eligible borrowers affected by the pandemic from the vulnerable B50 segment¹, including individuals and microenterprises, are able to apply for further repayment assistance. For URUS, banks have collectively set aside RM1 billion to fund the cost of the reduction in interest/profit for the programme's implementation. At the same time, we will continue to collaborate with the financial industry and AKPK to further strengthen the financing ecosystem for vulnerable SMEs. In this regard, we will ensure continuous access to effective avenues to seek information, financial advisory and redress. We will also increase outreach efforts and engagements to address the needs as well as improve the overall financial health of vulnerable businesses.
- We will promote the offering of **blended finance solutions** to further catalyse the recovery of businesses. Blended finance instruments combine different sources of funds – such as philanthropic funds and traditional bank financing – to lower financing costs for firms and reduce leverage. We are pleased to note that some banks have already partnered with equity finance providers to pilot blended finance schemes. Looking ahead, we will work with the financial industry and other stakeholders to further scale the offering of these solutions. The Bank will also provide dedicated concessionary funding for banks to tap into to increase the offering of blended finance solutions.

iii Facilitate 'second chances' for non-viable borrowers

Supporting a holistic economic recovery is not limited to helping viable borrowers survive, but includes implementing policies to help non-viable borrowers with efficient and orderly exit strategies, whilst ensuring their rights are reasonably protected

- We will work closely with the banking industry, AKPK, the Malaysian Department of Insolvency and the Companies Commission of Malaysia (SSM) to support efforts to simplify the **insolvency regime for SMEs**, especially microenterprises. This targeted approach reflects a key observation during the pandemic, where microenterprises account for most business closures in Malaysia². Enhancements to the current insolvency framework are required to reduce the total time and cost to complete insolvency proceedings, which may disproportionately impact microenterprises. As part of the process, we will promote conditions for entrepreneurship by making it easier and less costly for SMEs to exit and restart business ventures. This will also enable creditors to accelerate efforts to redeploy and reinvest remaining funds of the businesses – such as through liquidation of remaining assets – into new ventures and projects.
- We will enhance the regulatory framework that governs the **disposal and purchase of impaired financing**. We will seek to remove the existing foreign equity limit requirement for buyers to attract greater participation, particularly from established international players, into the market. With a more diverse buyer market, banks will be able to manage impaired financing in a more efficient manner. This will continue to be subject to safeguards that reasonably protect the rights of impaired borrowers and preserve fair opportunities for them to resolve their debt. Non-bank buyers of impaired financing will be required to meet certain eligibility criteria, for example, a proven track record of fair debt recovery practices. All buyers must also observe strict conduct requirements upon purchase of the impaired financing.

¹ Borrowers with a gross household income of RM5,880 or lower, based on the definition by the Department of Statistics of Malaysia.

² According to the Ministry of Entrepreneur Development and Cooperatives in September 2021, over 37,000 Malaysian businesses have closed since the implementation of the Movement Control Order in 2020, in which over 26,000 or close to 70% comprised of microenterprises.

Strategy 1B

Facilitate transformation to a high-income nation

For Malaysia to achieve a high-income nation status, it is essential to have a vibrant and innovative private sector that can respond to challenges and seize new growth opportunities. It is therefore critical for the nation to nurture firms that are more knowledge-, innovation- and technology-based. At the national level, progress has been made to advance bold and comprehensive reforms on this front, as seen by the adoption of the NIA policy in 2021.

The NIA, which now forms the basis of Malaysia's investment policies, is expected to drive long-term growth by building innovation capacity and attracting quality and sustainable investments into new growth areas. This in turn promotes the creation of high value-added jobs and strengthens domestic linkages.

In general, traditional debt-based financing funded from bank deposits better suits firms with regular repayments and risks that are well-understood. However, reliance on this type of financing alone may not be sufficient to meet the diverse needs across a growth firm's funding lifecycle. This is particularly true for firms that are innovative and that are engaged in new growth ventures or business transformation exercises. For example, such firms may operate in emerging industries and may lack established credit histories or predictable revenue streams. Increasingly, the profile of such firms is often 'asset-light', investing more in intellectual property (IP) and software, compared to tangible assets, which are often traditionally used as collateral for financing from banks.

We also remain cognisant of the longer-term risks to the financial system that may materialise from an underdeveloped alternative finance ecosystem – namely increased reliance and concentration of financing in the banking system. This could lead to unsustainable corporate leverage and even excessive risk taking by banks – which could have systemic implications.

Going forward, greater access to a more diverse range of funding instruments will be key to support the growth of such firms and promote longer-term financial stability. Alternative finance solutions, which include debt and equity-based instruments, will play a critical role in complementing bank-led debt financing to fund the economy, given their relevance across the business lifecycle of firms. These instruments include quasi-equity structures, asset-based finance, expanded applications of trade-based financing solutions, ECF and peer-to-peer (P2P) lending, VC financing, and equity investment via angel investors.

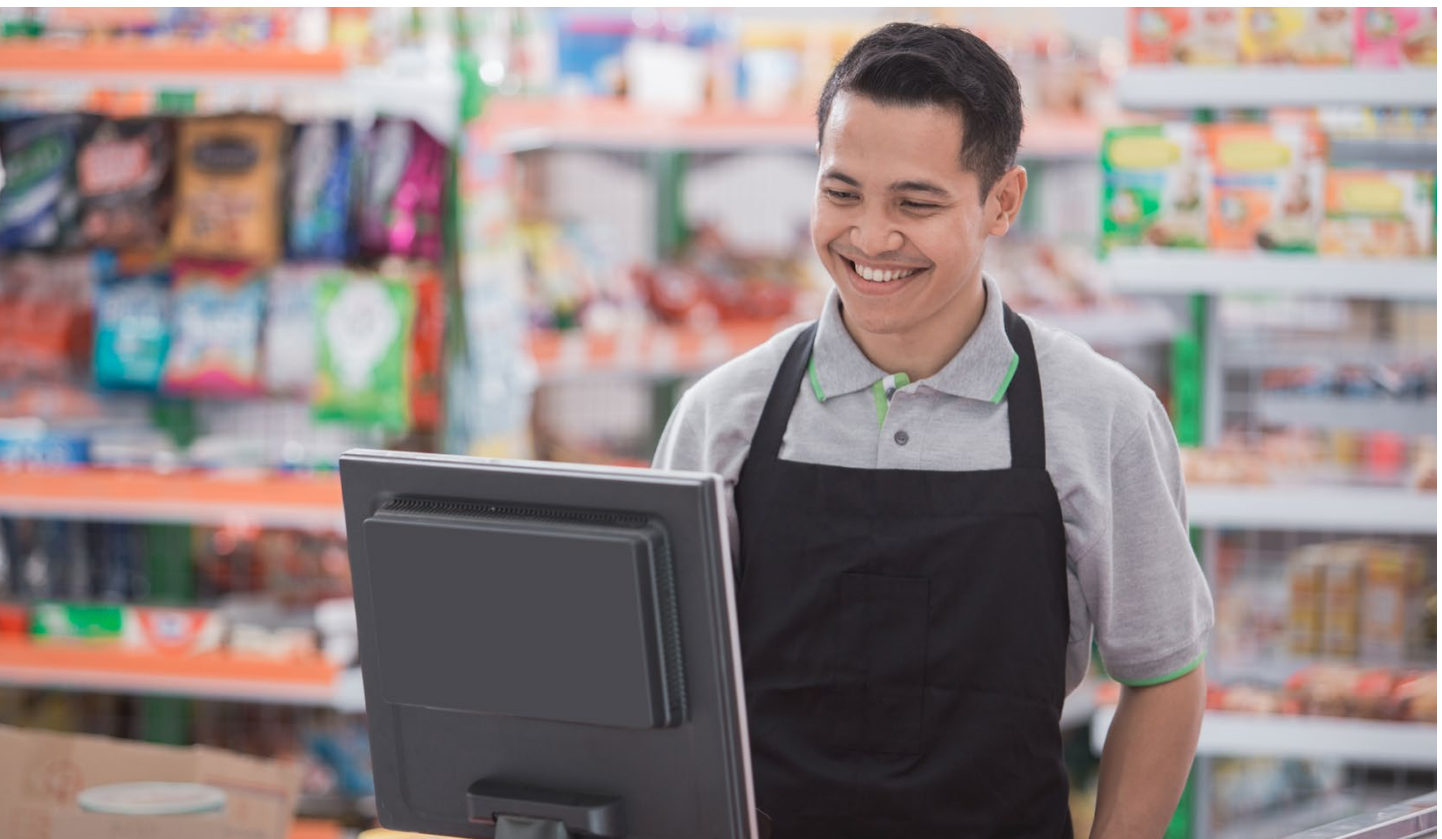
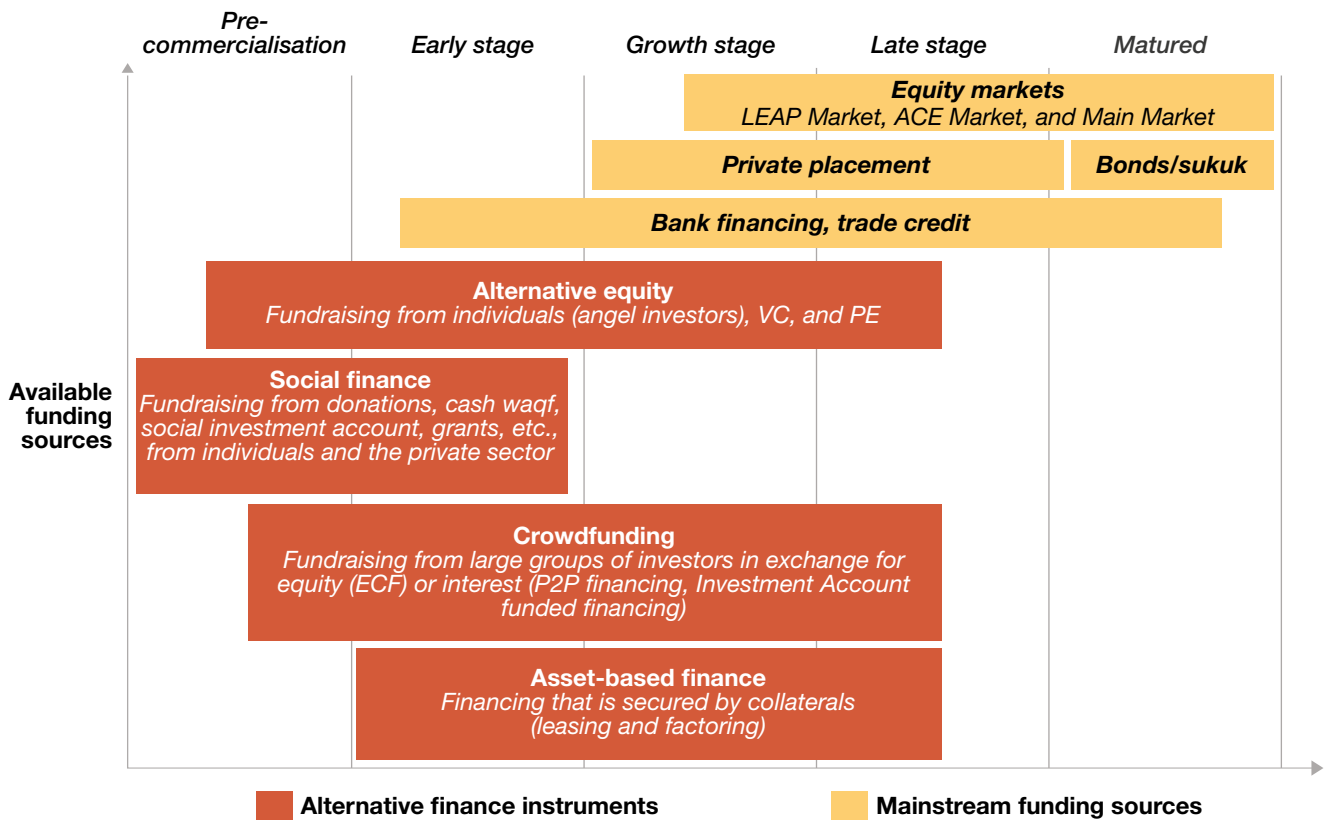
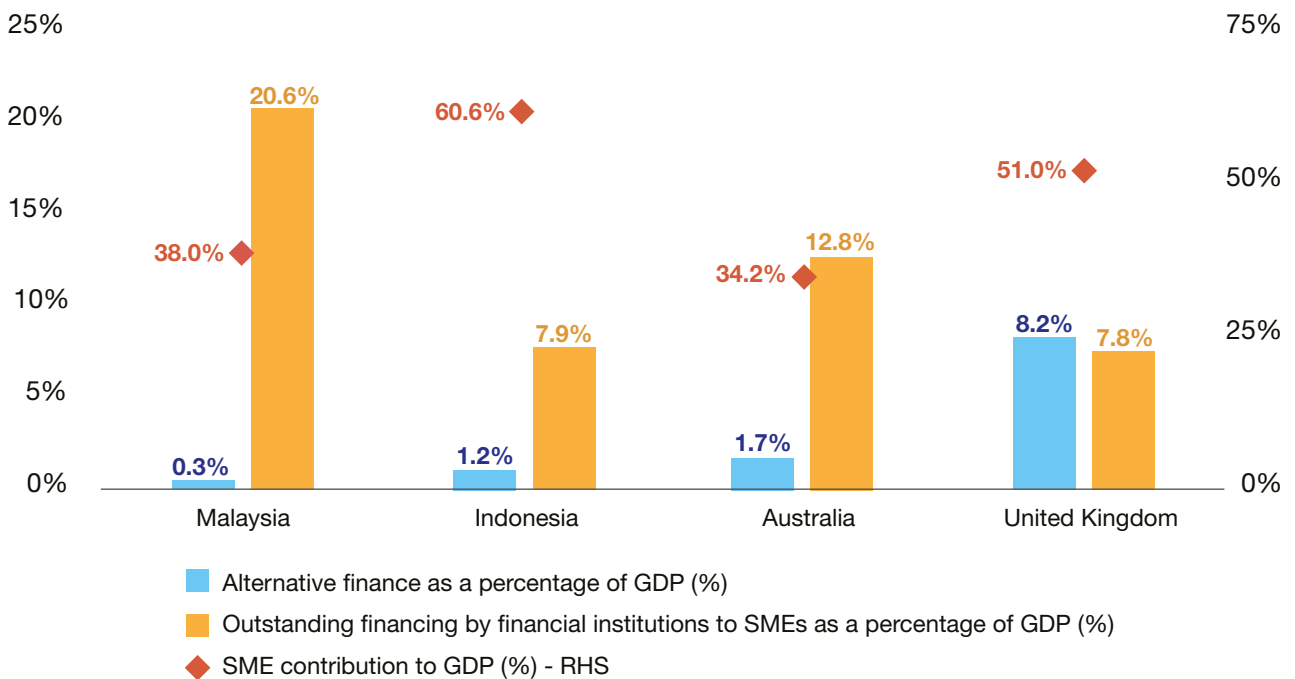


Diagram 2:
Available funding sources for businesses by stage of development



Source: Bank Negara Malaysia, the Securities Commission

Chart 1:
Malaysia's alternative finance¹ market remains small, compared to regional peer and developed markets



Data is from 2018

¹ Alternative finance in this chart includes leasing and factoring finance provided by banks and non-banks, VC, PE, P2P lending and ECF

Source: Bank Negara Malaysia, the Securities Commission, Organisation for Economic Co-operation and Development

As growing the alternative finance ecosystem will require close collaboration and commitment across relevant stakeholders, we will continue to actively cooperate with the SC and other relevant ecosystem partners, as well as industry players.

We will also review the microfinance landscape to better assist smaller firms to sustain their recovery from the pandemic through greater income generation opportunities.

To this end, we will seek to advance the following:

- i. Sustain and grow the alternative finance ecosystem and its supporting infrastructure;
- ii. Strengthen the regulatory framework and collaboration to promote the development of non-debt finance; and
- iii. Reinforce the finance ecosystem for microenterprises for sustainable and inclusive growth.



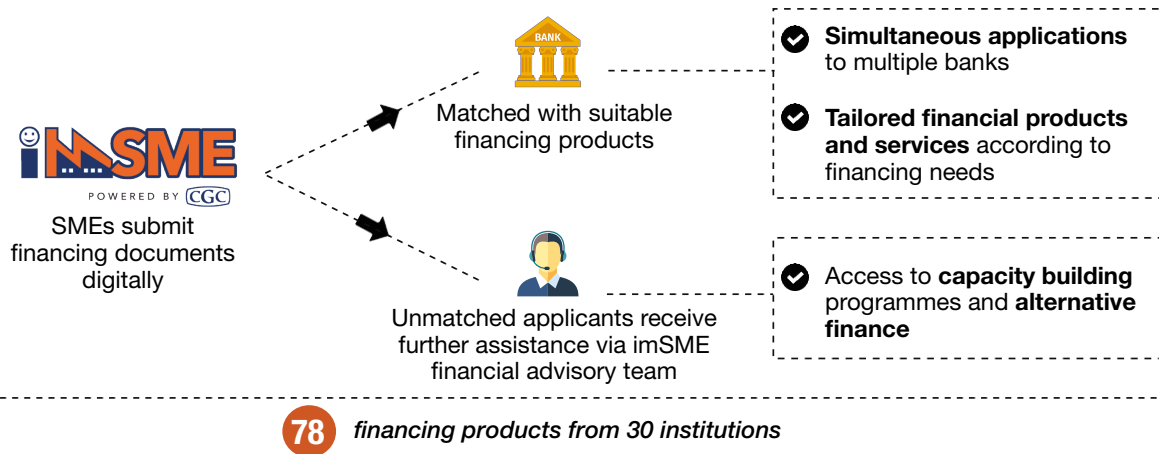
i Sustain and grow the alternative finance ecosystem and its supporting infrastructure

- We will encourage financial institutions' exploration of **social finance** within their business models. Social finance refers to financial business that is focused on social outcomes and uses recognised instruments, such as donations and cash *waqf*, to deliver financial products and services, while generating sustainable income to recipients. Social finance is envisioned to improve societal resilience through affordable and accessible provision of funds and financial protection. In recent years, social finance has been introduced into the market by blending philanthropic capital with other sources of funds. This allows the creation of financial products with features such as lower financing costs and flexible repayment terms to improve access to financing and protection for microentrepreneurs and households. Building on the progress so far, we will aim to broaden the adoption of such solutions to address other socioeconomic needs, such as affordable housing and healthcare. In this regard, we will continue to calibrate the regulatory framework to meet financial stability objectives, whilst still encouraging innovative and socially responsible finance.
- We will support and enhance new and existing **infrastructure** that provides the necessary foundation to accelerate the growth of the alternative finance ecosystem:
 - First, we will continue to work closely with relevant agencies, including SSM, to support efforts to expand the collateral base for SME financing, including via the establishment of a **centralised collateral registry**. This registry is envisioned to allow one-stop registration of all secured interest in assets – including moveable properties and IP – to be pledged as collateral, which in turn, supports more reliable credit appraisals. With greater transparency, finance providers will be able to screen for potential competing security interests on a particular asset before granting financing, which lowers the incidences of disputes over rights to property. With more credible and reliable access to collateral, SMEs will benefit as they can maximise the value of their tangible and intangible assets to obtain additional financing.

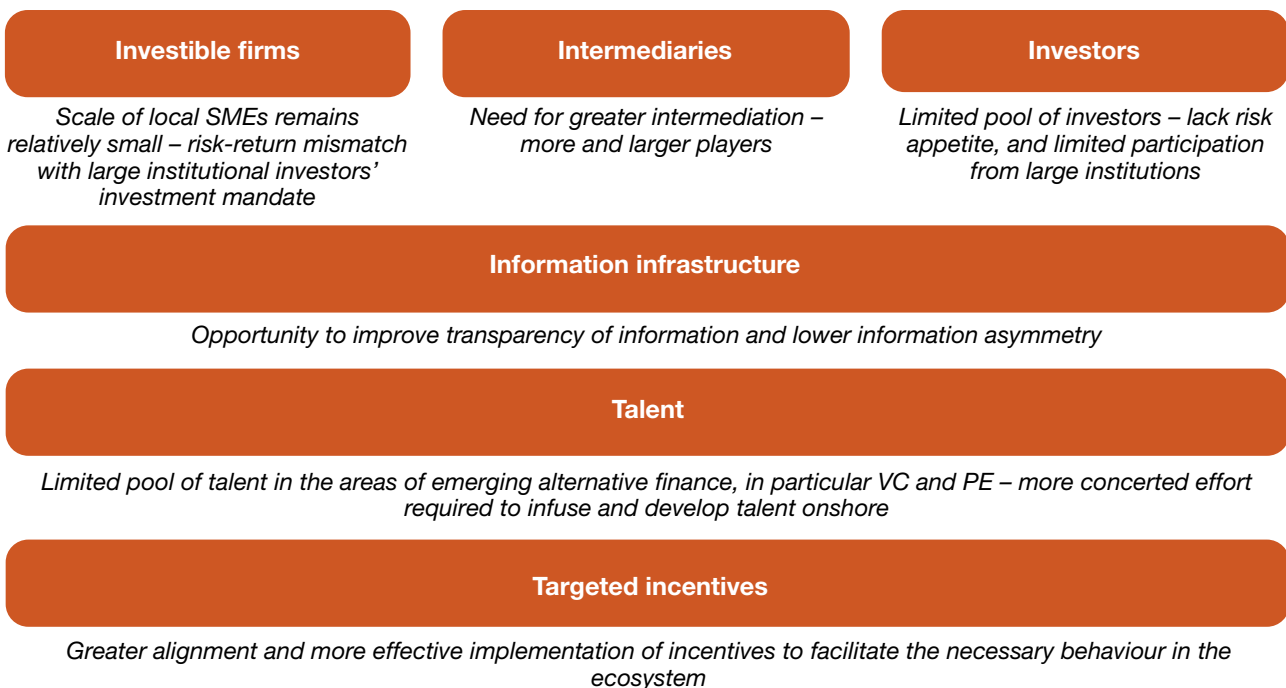
- Second, we will work with CGC to further increase the coverage and efficacy of **referrals to alternative finance on the imSME platform**. The imSME platform is an online SME financing and loan referral platform that matches SMEs to finance providers, including alternative finance lenders. The platform has seen increased participation in recent years from a wide range of alternative finance players, including factoring providers, VC funds, ECF and P2P firms. To further enhance the breadth and depth of finance providers on the imSME platform, we will mandate referrals of SMEs who do not qualify for bank financing to alternative financiers. With this, we envision that awareness and adoption of alternative finance among SMEs will gain faster traction.
- We will continue to perform our role in **advising and informing Government policies** to advance alternative finance development, including in the following areas:
 - Review of the **taxation framework** for alternative finance instruments. We will collaborate with relevant agencies and stakeholders to study the impact of existing corporate tax policy design on debt and equity-based instrument offerings. Through this study, we aim to move towards a more equitable tax regime for debt and equity finance that will encourage the growth of alternative finance. We view that such a study is timely, given that the current inclination towards debt finance due to the existing tax framework may lead to further risks to macroeconomic stability. At the same time, the bias towards debt finance may unfavourably discriminate against innovative firms that may be better suited for equity financing.

Additionally, we will also advance a more conducive tax regime for leasing providers. Under existing regulations, leasing activities
 - are treated as a distinct and separate business source, resulting in a higher tax burden on leasing companies, which impedes the growth of the market. Through relevant amendments to the existing legislation, this tax burden could be lowered. This will in turn promote the uptake of leasing among SMEs, especially for the acquisition of machinery and equipment.
 - Support **government-linked investment companies (GLICs) and DFIs** in accelerating the holistic development of the alternative finance ecosystem. There are opportunities for GLICs, in particular, to complement bank financing by enhancing their focus on developmental and catalytic investments, either directly via holdings in domestic PE, or indirectly via investments in equity or P2P platforms. In addition, studies³ have shown that the participation of institutional investors, such as GLICs, plays a key role in the growth of the alternative finance sector to achieve critical mass. Going forward, we will advocate for policies that facilitate the GLICs' and DFIs' involvement in alternative finance, while allowing them to continue to meet their existing investment and financing mandates.
 - Greater adoption of trade-based financing instruments, including **supply chain financing programmes**, as an alternative form of financing for eligible large corporate buyers and their vendors. Such programmes allow these vendors, who are often SMEs, to receive immediate payment for goods and services rendered to buyers, via the sale of invoices to financial institutions. With a more effective cashflow management process, small vendors can strengthen their resilience and growth prospects. We will also support efforts by corporates to collaborate with the financial sector to promote the design and offering of supply chain finance solutions to their vendors.

³ Source: Cambridge Centre for Alternative Finance (2021), "The 2nd Global Alternative Finance Market Benchmarking Report".

Diagram 3:**Seamless financing application process via the imSME online platform with a wide range of finance providers**

Source: Bank Negara Malaysia

Diagram 4:**Ecosystem requirements to grow alternative finance**

Source: Bank Negara Malaysia



As the finance ecosystem increasingly expands beyond debt-based solutions, we will work closely with financial institutions to ensure that they can participate and offer non-debt instruments

ii Strengthen the regulatory framework and collaboration to promote development of non-debt finance

■ We will explore measures to make it easier for banks to offer **non-debt-based finance solutions**, including via the provision of equity-based solutions and through partnerships with other non-debt-based finance providers. We welcome the interest of the industry to offer such solutions and will work closely with the industry and relevant stakeholders to address two existing challenges for banks:

- First, we will ensure that our **regulatory framework** does not pose undue barriers for banks' participation in non-debt finance. On this, we will review relevant aspects of the regulatory framework to support productive and meaningful participation of banks that remain consistent with financial stability outcomes.
- Second, we will support the banking industry to actively **partner with industry players within the start-up ecosystem**, through formal funding and expansion of incubation and accelerator programmes. With closer collaboration with industry players, banks will be able to deepen their understanding of new growth areas and

facilitate a more accurate evaluation of the risk profile of firms in these sectors. For example, in the United States of America (USA), European Union and Singapore, banks have partnered with institutional investors to provide venture debt solutions for firms as a way for founder entrepreneurs to raise funds, without diluting share equity.

- We will work closely with the SC to enhance efforts to develop a **comprehensive domestic funding ecosystem**. As non-debt-based finance offerings often involve both financial institutions and capital market intermediaries, we are committed to ensure strategic alignment in the efforts of the Bank and the SC in this area. To achieve this, we will establish a dedicated inter-agency platform, together with industry players, to coordinate and spearhead the development of the alternative finance market.

We will work closely with other regulators and industry players to ensure holistic development of the alternative finance market

iii Reinforce the finance ecosystem for microenterprises for sustainable and inclusive growth

- We will review and improve the microfinancing ecosystem, including the **Skim Pembiayaan Mikro (SPM)**. SPM is a scheme that enables fast and convenient access to business financing of up to RM50,000 without collateral from participating banks. Since the introduction of the SPM in 2006, the microfinance landscape has evolved rapidly. Prior to 2006, only *Amanah Ikhtiar Malaysia (AIM)* and *Tabung Ekonomi Kumpulan Usahawan Niaga (TEKUN)* provided microfinance. As at 2021, a total of 11 banks offer microfinance via the SPM. The market is also now more competitive with the entrance of new players – such as digital money lenders – that can offer compelling value propositions to microenterprises. In view of these developments, we will initiate a holistic review of the SPM to ensure it remains a relevant and effective financing tool. This would include an assessment on existing features of the SPM and access gaps, such as for informal and gig workers. At the same time, collaboration with CGC and SJPP will also be strengthened to further enhance access to finance for microentrepreneurs, including through the establishment of a simplified portfolio guarantee scheme.
- We will also support **programmes that go beyond finance** to assist microenterprises to further move up the value chain. Focus areas would be on increasing business formalisation through simple, facilitative, and seamless on-boarding procedures, facilitating business matching via supply and demand platforms, building microenterprises' resilience, and subsequently graduating microbusinesses to become bigger enterprises that are able to tap wide ranging products offered in the financial system. These programmes will be pioneered through the establishment of financial education modules and structured capacity building programmes, such as mentoring and business advisory support, by AKPK and the FEN.



Strategy 1C

Ensure post-pandemic resilience of financial intermediation role

The sound foundation of our financial institutions and markets has served as a “shock absorber” to the economy, by ensuring businesses and households continue to have access to finance despite the challenging economic conditions.

Our strategies will aim to ensure that the financial intermediation function continues to be resilient and effective moving forward. In pursuing this, we will build on the lessons learnt in managing past crises. Additionally, we will also promote better utilisation of insurance and takaful products, as well as enhance supervisory arrangements over key entities that provide finance.

As conditions in the financial markets are expected to remain challenging going forward, we will continue to ensure sufficient liquidity and orderly conditions in the foreign exchange and money markets. We also aim to ensure that financial markets do not increase financial stability risks, by improving the governance and accountability framework for market players.

To this end, we will seek to advance the following:

- i. Preserve funding capacity in the long-term; and
- ii. Strengthen vibrancy and resilience of financial markets to act as an absorber of risk.



i Preserve funding capacity in the long-term

- We will continue to work closely with the financial industry to improve our **crisis management responses** to better assist those in need. Drawing on the experience from the AFC, Malaysia has put in place well-established debt restructuring mechanisms for businesses. These include both court-sanctioned rescue mechanisms for businesses under the Companies Act 2016, and out-of-court platforms such as the CDRC and SDRS. Since the AFC, banks have also significantly improved their capacity in managing and resolving debt, even for multi-lender debt. Moving forward, we will continue to strengthen and advocate for more holistic debt restructuring arrangements. This includes the infusion of equity or equity-like investments to assist viable businesses that are highly leveraged. As most policy responses have been focused on providing credit, distressed businesses facing income shortages are burdened with additional debt – increasing the risk of insolvency. The debt-to-equity conversion would assist to moderate these businesses’ gearing level and provide a ‘second chance’ for viable businesses to recover.

■ We will promote greater offering of **insurance and takaful solutions** to mitigate risks incurred by finance providers and firms. The insurance and takaful industry, including reinsurers and retakaful providers, can contribute to economic growth and effective financial intermediation through the transfer of risk and mobilisation of funds. Therefore, we will work with the industry to further diversify and increase risk protection solutions in the following areas:

- First, we will facilitate the offering of **trade credit protection** solutions. As we look to enhance trade-based financial instruments in the market, we acknowledge the risks that firms, especially SMEs, are exposed to from non-payment of goods and services. These risks can often lead to financial losses or even insolvency. We believe that insurers and takaful operators can lower these risks through the offering of trade credit protection products, and in turn, facilitate these firms to better manage their operations and investments to secure growth. In this regard, we will work with the industry and relevant government agencies to address key bottlenecks to trade credit protection growth, such as the high cost, low underwriting technical capacity and low market awareness associated with such products.
- Second, we will encourage the offering of **specialised insurance and takaful products** by building domestic expertise and capacity to manage risks in emerging growth areas, such as in renewable energy projects. These protection solutions are expected to assist firms to increase their exposure to these areas

by mitigating downside risks. In the case of renewable energy projects, this includes protection to firms against engineering deficiencies and for the transportation of power-generating equipment. These solutions will help to drive more investments into key areas and projects, and ultimately support the economic transformation aspirations of the country.

- Third, we will work with the **reinsurance and retakaful industry** so that it supports the risk diversification needs of the domestic insurance and takaful market. In this regard, we will seek to promote sufficient reinsurance and retakaful capacity, especially in critical protection areas that promote economic growth as well as household and business resilience. We believe that these efforts will also in turn support Malaysia's aspirations to become a regional reinsurance and retakaful hub.
- We will also enhance surveillance and promote stronger **oversight arrangements for non-bank players**, in particular pension and provident funds and deposit-taking-like entities that are systemically important. As the financial intermediary landscape continues to diversify beyond the banking sector to include non-bank players with different business models and risk profiles, an agile and holistic approach to risk management is needed to mitigate any adverse shocks that could impact the integrity and effective functioning of financial intermediation. In this regard, we will work closely with key stakeholders, such as the SC, to enhance the oversight over these non-bank players, so that preventive and corrective actions can be taken in a timely manner to address any risk events.

ii Strengthen vibrancy and resilience of financial markets to act as an absorber of risk

To mitigate excessive volatility in the global financial system, we will continue to enhance the risk mitigation role of the domestic financial markets by improving market liquidity and resilience to shocks

■ We will promote a **liquid and vibrant onshore financial market**, focusing on strategies that enhance the market's countercyclical role, address real sector needs, and improve capacity for effective risk management. To this extent, we will advance three key strategies:

- First, we will enhance the **breadth and depth of our financial market** to improve its ability to manage external shocks and to cater to domestic and international economic needs.

We will continue to promote greater adoption of **collateralised transactions** within the domestic money market, particularly to deepen the domestic repurchase agreement (repo) market. Repo transactions not only diversify financing accessibility for participants across the system, but also allow for more robust and efficient allocation of funds across tenors in the money market. To this end, we will pursue greater diversity of investors in the repo and securities borrowing and lending markets to include more non-banking participants, such as insurance companies and large corporations.

As another area of focus, we will intensify efforts to develop the **onshore derivatives market**, including interest rate derivative products, to increase market liquidity and volume of transactions. These measures are expected to promote the development and application of a transaction-based alternative reference rate for Malaysia, in line with global financial benchmark reform initiatives.

We will also enhance our usage of technology to improve **liquidity and pricing transparency** in the onshore market. To this end, we envision that a wider adoption of electronic trading platforms by onshore market participants will further improve price discovery and provide efficient execution. We will also adopt relevant technology to enhance the efficiency of regulatory reporting in the foreign exchange (FX), bond and money markets to enable effective assessment, monitoring, as well as dissemination of information surrounding risk build-ups in the financial markets.

Additionally, we will advocate for greater **risk management practices** among resident businesses, as well as participation by a broader set of investors in the derivatives market. This will be supported by continuous assessment and enhancement to our policies to facilitate flexibilities for businesses as well as to encourage utilisation of FX forward hedging amongst corporates and domestic portfolio institutional investors. Initiatives to further enhance the investment climate and business efficiency aim to further strengthen the attractiveness of Malaysia's position in the global supply chain, besides fostering a conducive environment for foreign direct investment (FDI).

To further strengthen Malaysia's financial market's resilience to withstand future shocks, we will **expand safety nets arrangements**. To achieve this, we will continue to pursue strategic bilateral swap arrangements with regional central banks, as well as enhance existing bilateral and multilateral safety net arrangements.

Next, we will continue to promote liquidity in the domestic **environmental, social and governance (ESG) bond and sukuk market**, ensuring alignment with national sustainable development aspirations as well as meeting international investor demand for ESG-linked financial products. On a broader level, this measure is also expected to be a catalyst for a deep and robust ESG investment ecosystem.

- Second, we seek to preserve Malaysia's **leadership in Islamic finance**, through initiatives to deepen the Islamic money and capital markets.
- Third, we will further strengthen **integrity and professionalism** in our financial market by upholding the highest standards and practices. To this end, we will advocate for a more active role by market participants in shaping the financial market's **conduct and best practices**. In this regard, the wholesale market code of conduct, which sets out principles and standards to be observed by market participants in the money and foreign exchange markets, will be continuously reviewed and updated, in line with global standards.
- We will also continue to enhance the integrity and reliability of our **domestic financial market benchmarks**, in line with the FSB's recommendations. This includes undertaking periodic reviews to ensure that the financial benchmark rates remain robust and reflective of an active underlying market.

Strategic Thrust 2

Elevate the financial well-being of households and businesses

Financial well-being refers to an individual's ability to meet ongoing financial obligations, stay resilient to income shocks, achieve future financial goals, and make financial decisions to improve one's overall quality of life. In a similar vein, businesses should be in good financial health to withstand unanticipated financial setbacks and capitalise on emerging opportunities to upscale and secure future growth.

The pandemic has surfaced, and in some respects, exacerbated significant vulnerabilities impacting the financial well-being of households and businesses. Addressing these vulnerabilities requires important economic reforms to raise the standards of living of households through employment and income-generating activities, with the financial sector playing a key role to serve the financial intermediation needs

of all. Ongoing reforms to the social protection framework¹ and business ecosystem² will be fundamental to secure future resilience.

Measures to elevate financial well-being go beyond ensuring access. The desired outcome is for individuals and businesses to meaningfully benefit from their participation in the financial system by equipping households and businesses with suitable and affordable solutions, as well as empowering them with the financial capability to make sound financial judgments. Alongside these, it is also important to ensure financial consumers continue to be treated fairly to inspire positive user experience and consumer outcomes.

With this in mind, we will advance three key strategies (Diagram 1).

Diagram 1:
Elevate financial well-being



A

Enhance financial capability and access, as well as effective usage of financial services towards greater financial inclusion

- ◆ Equip consumers with improved financial capabilities
- ◆ Address remaining inclusion gaps, focusing on take-up and meaningful usage of financial services, especially for the unserved and underserved segments



B

Strengthen protection for households and businesses to build financial resilience

- ◆ Expand market capacity to meet household and business protection needs against future risks
- ◆ Strengthen efforts to address pre-conditions for a sustainable protection landscape for key risks



C

Shape a financial system that upholds fair and responsible dealings with financial consumers

- ◆ Strengthen professional standards, incentive frameworks and disclosure practices
- ◆ Promote an enabling conduct environment for innovation and efficiency
- ◆ Pursue regulatory reforms to strengthen the oversight of non-bank consumer credit providers and promote consistent consumer protection

¹ This is broadly categorised into social safety nets, social insurance and active labour market policies. For further details, please refer to the Box Article titled "A Vision for Social Protection in Malaysia" in Bank Negara Malaysia's Economic and Monetary Review 2020, accessible at https://www.bnm.gov.my/documents/20124/3026377/emr2020_en_box1_socialprotection.pdf

² Measures to support businesses include debt resolution schemes for the purpose of business rehabilitation, financing guarantee and insurance for microenterprises and informal businesses.

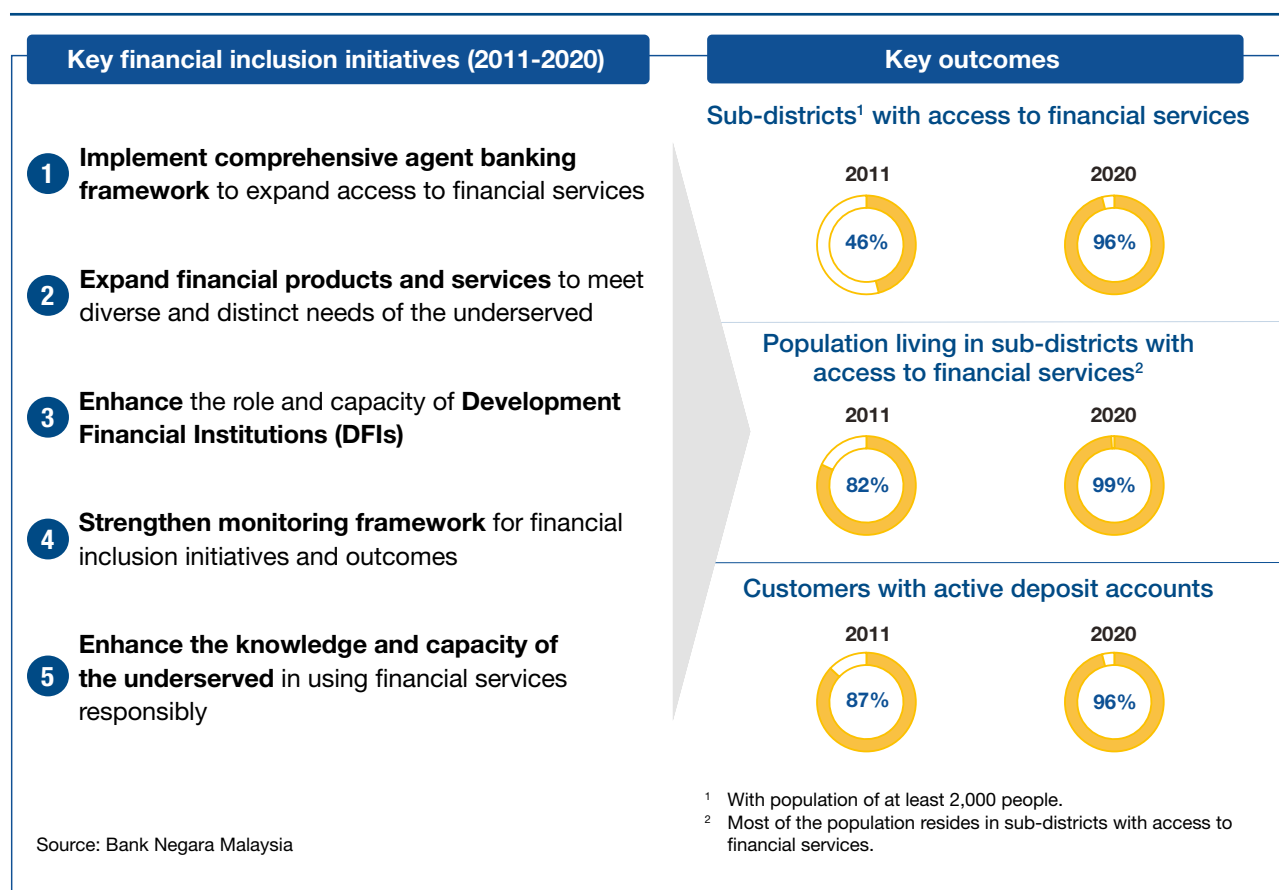
Strategy 2A

Enhance financial capability and access, as well as effective usage of financial services towards greater financial inclusion

Over the past decade, Malaysia has made significant progress in advancing financial inclusion and introduced nationwide financial education initiatives to elevate financial capability³. The Financial Education Network (FEN) was established in 2016 as a cohesive inter-agency platform to lead such efforts, while the National Strategy for Financial Literacy (2019-2023) outlines strategic priorities to elevate financial literacy and promote responsible financial behaviour of consumers across all life stages. Through our collaboration with the Ministry of Education (MOE), financial education modules have also been successfully integrated into all levels of the formal education system and as elective programmes of higher learning and teacher training institutes – with the Financial Literacy Core Competency Framework for adults serving as a key reference to effect lasting behavioural change.

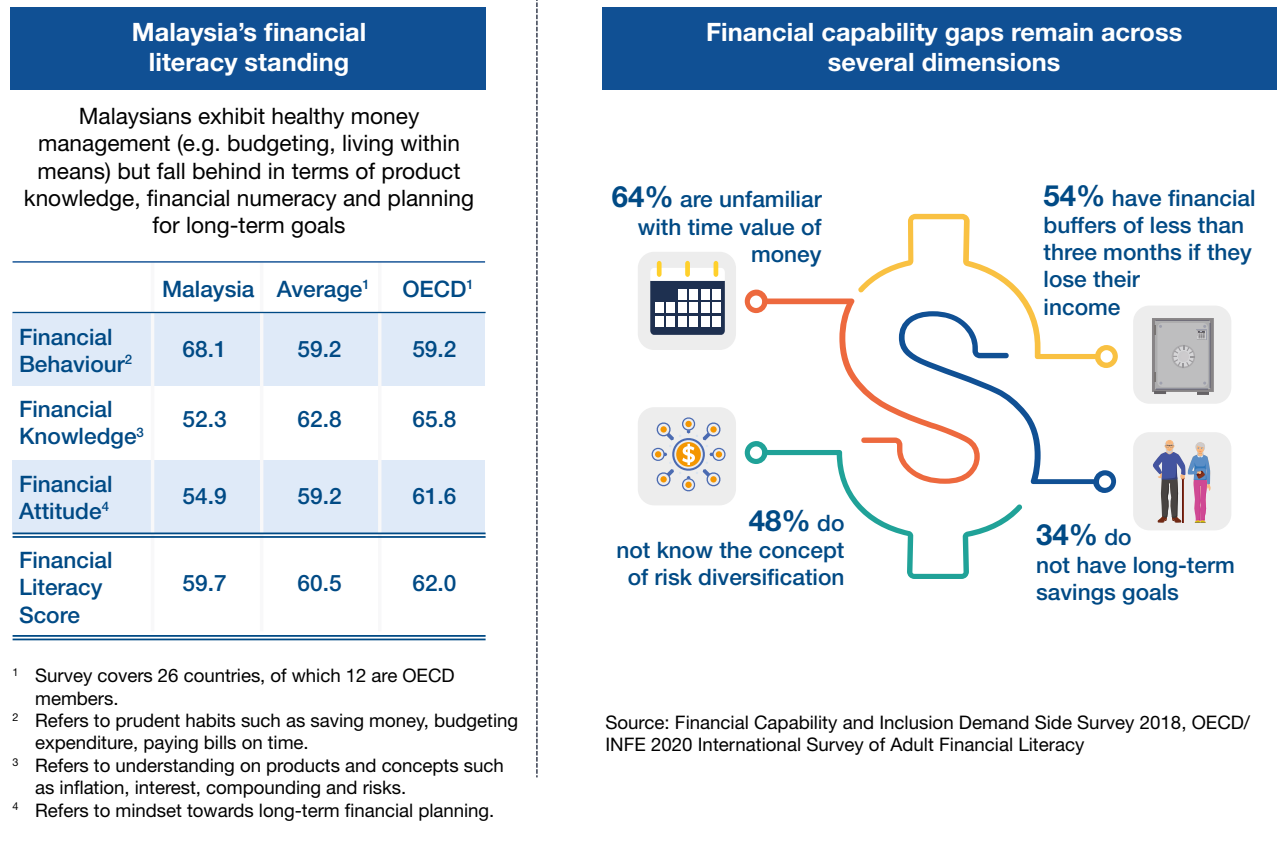
In advancing financial inclusion, a range of measures have been undertaken since 2011, thereby expanding access to and provision of financial services (see Diagram 2). Nonetheless, some financial capability gaps remain to be addressed (see Diagram 3).

Diagram 2:
Key financial inclusion initiatives and outcomes between 2011-2020



³ Financial capability is the combination of attitude, knowledge, skills, and self-efficacy needed to make and exercise money management decisions. (Source: Center for Financial Inclusion)

Diagram 3:
Remaining financial capability gaps in Malaysia



Moving forward, our strategies in enhancing financial inclusion will target initiatives to advance the following:

- i. Equip consumers with improved financial capabilities; and
- ii. Address remaining inclusion gaps, focusing on take-up and meaningful usage of financial services, especially for the unserved and underserved segments.

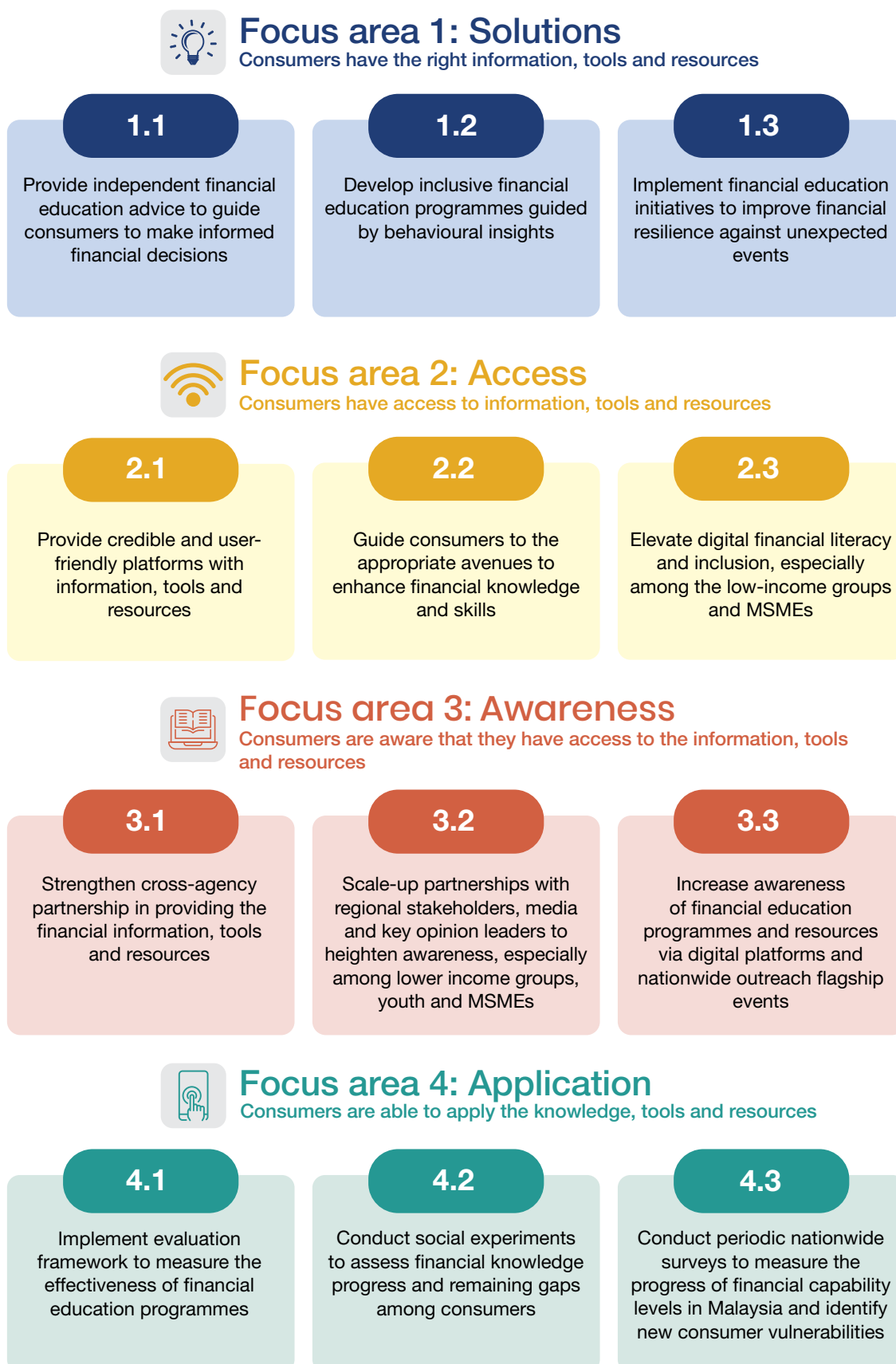
i Equip consumers with improved financial capabilities

- We will **advance national collaboration on financial education initiatives through the FEN** by expanding strategic partnerships, accelerating awareness via digital platforms, and building a research ecosystem. We will build on the FEN Programmatic Roadmap – with a focus on Solutions, Access, Awareness and Applications (see Diagram 4) – to elevate the financial capability of consumers.

We will seek to cultivate sound financial decisions⁴ among consumers and businesses through targeted financial literacy initiatives

⁴ Ability to make rational financial choices through the understanding of financial concepts and take precautions against financial scams as well as behavioural biases (e.g. herd behaviour).

Diagram 4 :
Focus areas and initiatives under FEN Programmatic Roadmap



- We will **scale up targeted consumer engagement measures to elevate financial literacy and inclusion** by leveraging innovative channels and digital touchpoints. These measures will help consumers learn to use financial management tools for financial planning, budgeting, and product comparison. Importantly, we envision consumers having greater knowledge of available financial solutions in the market, as well as being able to develop a habit of saving, investing, and planning for retirement at an early age. We will emphasise cultivating sound financial judgement – including to guard against behavioural biases such as herd behaviour and susceptibility to financial scams. Given the increasing digitalisation of financial services, we will also intensify efforts to enhance digital financial literacy.
- **Annual Key Performance Indicators (KPIs) will be identified** under the four focus areas of the FEN Programmatic Roadmap to measure and track the impact of financial capability initiatives more effectively. These annual KPIs will be evaluated alongside improvements in the levels of knowledge, behaviour, and attitude of consumers in Malaysia on financial matters as measured under the Financial Capability and Inclusion (FCI) Demand Side Survey, which is conducted on a triennial basis.

At a broader level, we will also ensure our assessment and monitoring tools – such as the FCI – are aligned to international best practices and remain relevant so that financial capability and inclusion gaps can be addressed in a timely manner. A financial education measurement and impact assessment framework will be developed to systematically assess the effectiveness of financial education initiatives targeting all segments of the population – from students to adults. Findings from the assessment will be used to continuously improve financial education initiatives.

With better capabilities to accurately identify remaining gaps, we can enhance the efficacy of our inclusion strategies and help achieve other development goals under the 2030 SDGs. For instance, we will account for emerging financial services channels by building in digital take-up, quality of digital services, and digital literacy.

Together, these measures will augment efforts by the Bank and FEN members towards more evidence-based policymaking – to prioritise critical financial capability and inclusion initiatives and design targeted interventions.

ii Address remaining inclusion gaps, focusing on take-up and effective usage of financial services, especially for the unserved and underserved segments

Moving forward, financial inclusion efforts will go beyond improving access, with an aim towards driving sustained and responsible usage of financial products and services. We will strive to enable more meaningful financial participation by all in Malaysia so that they are able to save, invest, and build long-term financial buffers. At the same time, we will continue to find innovative ways to address financial barriers, particularly for the unserved and underserved communities.

Financial inclusion initiatives will go beyond improving access – we will seek to drive sustained, responsible and meaningful usage of financial solutions

- We will continue to **strengthen the role of agent banks and Mobile Banks (*Bank Bergerak*)** to enable wider access to financial services through existing networks and facilitate the digital on-boarding of consumers in unserved and underserved areas. This includes the following:
 - **Preserve physical financial touchpoints** to help low-income, elderly, and non-urban communities – at least for the medium term – until the necessary levels of connectivity (i.e. internet and devices) and digital literacy are achieved in these segments to support the transition to digital financial channels.
 - **Expand the range of services of agent banks**, including to facilitate a simplified onboarding process for customers. We will focus on rural and underserved areas that lack bank branches to carry out customer due diligence.

□ **Explore greater interoperability⁵ between banks.** This aims to facilitate access to a wider range of financial services and service providers, including withdrawals and deposits, as well as digital payments through all agent banks, digital banks, and Mobile Banks.

■ **We will improve outreach to the “last mile” unbanked population.** On this front, our priority will be to strengthen the roles and capabilities of financial institutions to serve financial inclusion objectives. To this end, we will accord focus to:

□ **Increase the impact of DFIs in delivering their developmental mandates** towards the financial inclusion agenda (refer to Strategy 1A(i) of the chapter “Fund Malaysia’s economic transformation” for more details).

□ **Ensure that digital banks address remaining market gaps** among the unserved and underserved segments. Performance of the digital banks will be monitored against the respective institutions’ financial inclusion commitments, which form an essential component of the value proposition for the granting of digital bank licences.

□ **Liberalise the policy on the establishment of physical branches** for locally-incorporated foreign banks (LIFBs), aimed at enhancing the role of LIFBs in contributing to the needs of the domestic economy and furthering financial inclusion objectives.

□ **Facilitate industry efforts to pilot and expand the use of behavioural analytics to engage out-of-reach communities** more effectively. This is expected to encourage the development of more targeted, needs-based products and to effectively nudge consumers towards better-informed financial decisions – through applications ranging from credit assessments, identification of protection needs, predictive modelling, product design, and marketing.

■ **We will promote wider adoption of financial inclusion KPI disclosures** by financial institutions to encourage greater alignment with inclusive finance goals. We will improve guidance on how financial institutions should define the financially unserved and underserved, and consider standardised reporting on KPIs – to enable financial institutions to express their commitment as socially responsible institutions in a systematic manner. Such disclosures will serve to demonstrate how financial institutions support the broader ESG goals and SDG agendas.

■ **We will promote more seamless data sharing** across the financial sector to further unlock new financial inclusion opportunities through common standards for data sharing (as referenced in Strategy 3A(ii) of the chapter “Advance digitalisation of the financial sector”). Our immediate focus will be to enable improved access to data on the profiles, needs, usage and behaviour of unserved or underserved segments by enabling data sharing pipelines with other partner institutions such as microfinance institutions and key government agencies. In prioritising datasets for sharing with the industry, we will accord greater priority to high-impact, innovative use cases that can address remaining financial inclusion gaps. For example:

□ **Access and needs-based solutions.** Facilitate the development of alternative credit scoring models by sharing pooled information on “thin file” consumers with financial providers. Similarly, more granular data points on consumer protection needs will also enable better targeted and affordable microinsurance/microtakaful product designs for key consumer groups (e.g. B40 group).

□ **Consumer choice and financial management.** While existing financial aggregators predominantly feature products by financial institutions, this should be expanded to more offerings by other financial providers such as fintech companies, so consumers can compare the price and suitability of more diverse financial products. In this regard, we will facilitate the integration of product comparison features with additional value-add services (e.g. financial management tools and financial advisory), taking into account the benefits and risks of such arrangements.

⁵ Financial services where the issuer and the acquirer are not the same financial institution.

Strategy 2B

Strengthen protection for households and businesses to build financial resilience

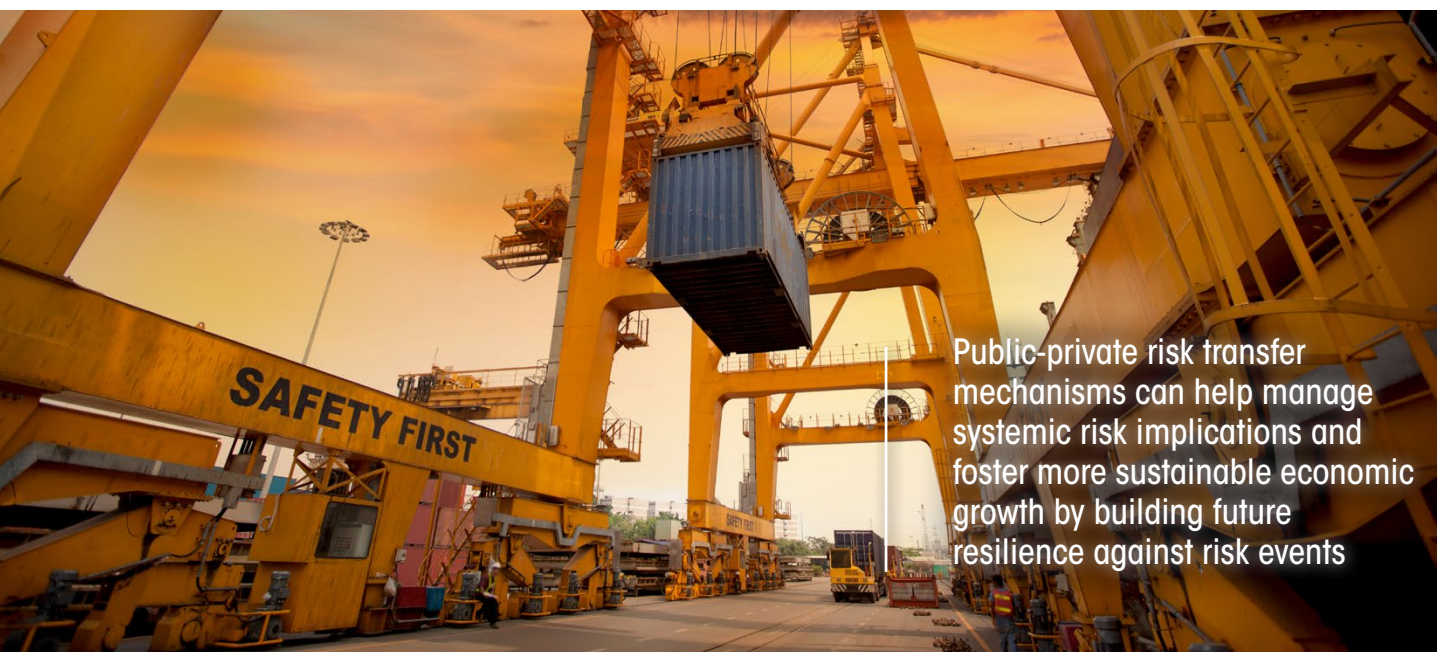
Malaysia's next stage of economic transformation stands to significantly benefit from a rich and diversified range of mechanisms that can protect financial consumers. The financial needs of households and businesses are expected to evolve in several important ways amid wider demographic shifts and technological change. Individuals will be more discerning and are likely to seek more specific, affordable, and needs-based protection. Meanwhile, businesses would need solutions that support future resilience against emerging risks. The pandemic – which underscored the value of financial security in a time of uncertainty and distress – has also generated greater appreciation and demand for insurance and takaful solutions.

The insurance and takaful landscape must therefore be positioned to support the new demands and play an effective risk transfer role. This requires a protection landscape that is competitive, efficient, and inclusive. These three outcomes will shape our strategic priorities in the coming years. We will also leverage the universal principles under the Value-based Intermediation for Takaful (VBIT) framework, which supports value creation for stakeholders – consumers, society, and the environment (further details in the chapter “Advance value-based finance through Islamic finance leadership”). We also see digitalisation as a catalyst for innovation and competition, including through the use of shared digital infrastructures to address structural gaps in the ecosystem (further details in the chapter “Advance digitalisation of the financial sector”).

Financial resilience must be supported by a diverse range of factors: sufficiency of income above the living wage, savings buffers, social protection, diverse wealth accumulation solutions and protection against unanticipated events. Efforts to support this outcome require a whole-of-government approach. In addition to protection solutions, our efforts to develop a vibrant funding and financial markets landscape (see the chapter “Fund Malaysia's economic transformation”) will also support improved financial resilience of households and businesses. At a broader level, we will continue to work with other regulatory authorities and relevant agencies – particularly the SC – to holistically develop a diverse ecosystem of wealth and risk management solutions that will cater to various life and business stages. This includes solutions for wealth accumulation and preservation (e.g. fixed deposits, unit trusts, exchange-traded funds), decumulation (e.g. reverse mortgage, deferred annuity), and for the management of risks (e.g. insurance protection, hedging instruments).

To this end, our efforts here aim to:

- i. Expand market capacity to meet household and business protection needs against future risks; and
- ii. Strengthen efforts to address pre-conditions for a sustainable protection landscape for key risks.



Public-private risk transfer mechanisms can help manage systemic risk implications and foster more sustainable economic growth by building future resilience against risk events

i Expand market capacity to meet household and business protection needs against future risks

- We will **explore public-private partnerships to develop business risk transfer protection schemes against high-risk, large-scale perils** – serving as safety nets that can be quickly activated in times of crisis. This builds on lessons learned during the pandemic and floods, which revealed a significant protection gap in business interruption risks. The absence of suitable coverage and low take-up have left MSMEs vulnerable to weather these risk events given their limited financial buffers, and places increased fiscal demands on the Government to provide relief measures.

A key success factor will be the ability of public-private risk pools to cover a wide range of risks, given the systemic nature of such events. These risk pools should capture not only risks arising from pandemics, but also other emerging ones such as cyber risks, as well as climate-related and environmental risks. Challenges due to adverse selection⁶ and a small domestic consumer pool limit the ability of the private sector market to expand and provide cover for systemic risks, which is observed globally to be particularly evident for natural disaster perils such as flood risk. To manage this, larger public-private national insurance pools are typically explored as a more sustainable and inclusive solution. Doing so will in turn enable the private sector to be the first line of defence to provide protection through risk pooling in the event of such shocks. Meanwhile, the public sector can redeploy financial resources for longer-term outcomes, such as to provide financial backing – including through initial capacity development and backstop guarantee for excess losses. Importantly, given the systemic nature of these risks, such support by the public sector will provide greater certainty for insurance and takaful players to design and price the right risk coverage.

- We will continue to **support the growth of a diverse microinsurance and microtakaful market** which delivers products that provide good protection value, are accessible, affordable, simple to purchase, and make claims against. The *Perlindungan Tenang* initiative was first introduced in 2017 to spur greater awareness as well as the development of microinsurance and microtakaful products. While the increased take-up has been encouraging, some challenges remain to hinder the initiative from achieving its potential in benefitting unserved and underserved consumers. Building on

our experience over the last four years, we will take a three-pronged strategy to catalyse further growth in this market segment:

- **Promote greater innovation through flexibilities under the *Perlindungan Tenang* framework.** ITOs can leverage the flexibilities granted in the framework in serving the underserved segments (e.g. offering more diverse products, expanding distribution channels, and introducing innovation through product bundling). We will continue to enhance the framework to ensure that it remains relevant and fit-for-purpose.
- Further **develop and provide access to more granular demand-side information** to enable the industry to better identify protection coverage gaps, risks and behaviours of the unserved and underserved segments, such as the B40 group. This will help facilitate more informed and targeted policies, and the expansion of product offerings by the industry.
- **Advance financial literacy initiatives** to improve consumer awareness and understanding of microinsurance and microtakaful protection, as well as benefits of the *Perlindungan Tenang* initiative among segments that need it the most, through our role in the FEN.

While we are committed to delivering the above strategies, private sector supply-side measures alone would be insufficient. Government support (e.g. purchase vouchers and stamp duty exemptions for *Perlindungan Tenang* products first announced in the 2021 Budget) and the social safety net system should serve as a key foundation to widen protection coverage. Moving forward, we will continue to work with relevant government agencies to advance alternative means of developing and funding protection instruments that take into account economic dependencies (e.g. income levels, size of household, age) of target groups.

⁶ Occurs when only those facing higher risk purchase insurance, and those less at risk do not.

ii Strengthen efforts to address pre-conditions for a sustainable protection landscape for key risks

We will adopt a whole-of-ecosystem approach in addressing structural challenges for key risks in the insurance and takaful landscape

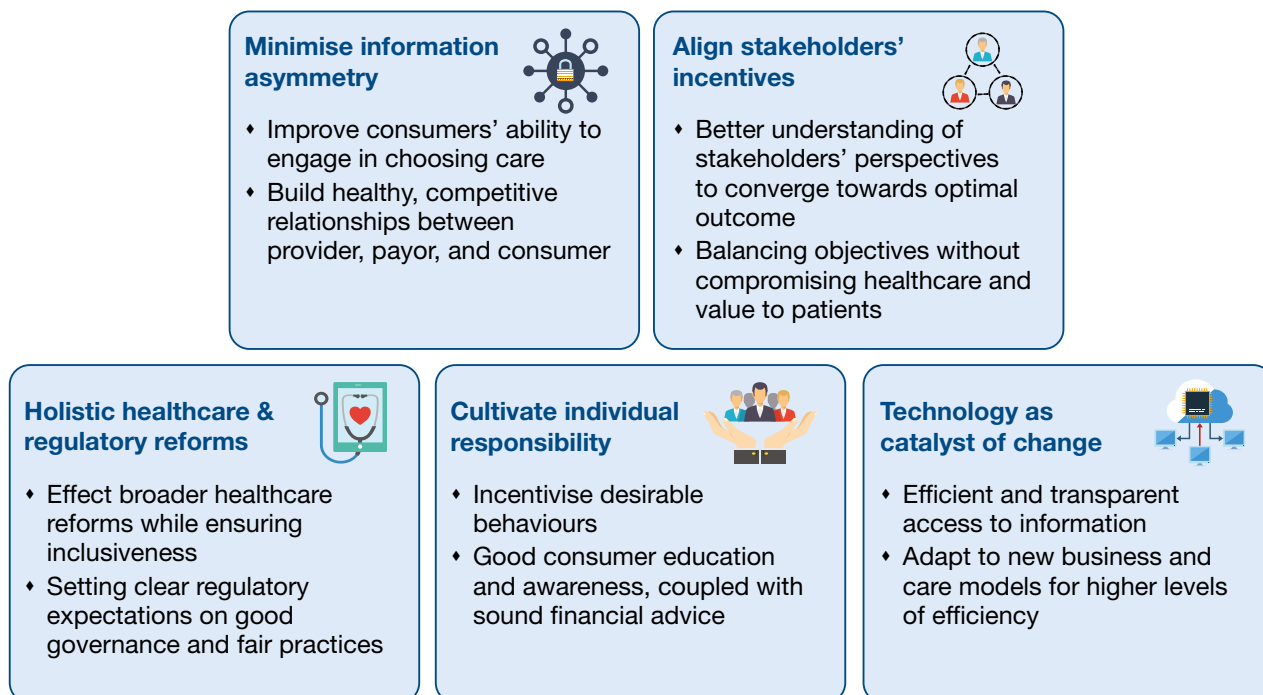
- We will **advocate and support comprehensive social protection reforms** by the Government to strengthen the financial resilience of society. In doing this, we will continue to play an active role in existing policy platforms such as the Malaysia Social Protection Council (MySPC) and Economic Action Council (EAC) to recommend best practices for Malaysia.
 - We will **advocate for a social protection floor** to ensure that all vulnerable groups are adequately protected. For comprehensive protection, it is key to draw on the three complementing pillars of social protection reforms: (i) social safety nets; (ii) social insurance; and (iii) active labour market policies. Together, these policies will mitigate existing vulnerabilities and ensure long-term resilience as well as economic security.
 - We will **assist the Government's policy development efforts through an ongoing gap assessment** on Malaysia's social protection framework. For example, we will help to identify the right private sector solutions as the nation progresses further towards voluntary contribution schemes of social insurance (e.g. private retirement schemes).
 - We will **support and work with the Government to adopt a comprehensive and unified social protection database**, with the goal of minimising inclusion and exclusion errors⁷. In achieving this, the application of technology, inter-agency collaboration, and continuous capacity building will be key.
- We will continue to **pursue further liberalisation of the motor and fire tariffs** to support an orderly transition to a more market-based pricing approach. Further liberalisation will serve as an impetus for ITOs to innovate in products and elevate the quality of services, thereby bringing better benefits and cost savings for consumers. Even as we do so, we will ensure basic motor protection cover remains accessible to all consumer segments. Our priorities on this front in the next five years will seek to complement broader efforts to support the transformation of the motor claims ecosystem into the desired end state. Digital transformation across the value chain will be key in achieving this (see further details of Strategy 3A(ii) of the chapter "Advance digitalisation of the financial sector").
- We will focus on measures to **address the long-term sustainability and affordability of private medical and health insurance/takaful (MHIT) cover**. Since 2016, the growth of medical claims (11.6% per year) has outpaced that of medical premiums/contributions (9.5% per year), with 2020 being the sole exception. Coupled with the rising cost of private medical care in Malaysia – reported to be among the highest in Southeast Asia⁸ – there is likely to be more pressure on the pricing and sustainability of hospital and surgical insurance/takaful (HSIT) covers.

With MHIT players having to frequently reprice their products to keep up with these rising costs, there can be significant knock-on effects on the costs of premium/contributions to existing policy and certificate holders – thereby making it increasingly unaffordable. These developments highlight the urgency for early intervention and structural reforms to stem the rise in medical claims inflation. From our global benchmark findings and assessments, we have identified five key success factors to sustainably manage medical costs and claims inflation (see Diagram 5).

⁷ Inclusion errors refer to aid provision to the non-targeted groups who do not require aid, whereas exclusion errors refer to undercoverage or failure to aid the targeted groups.

⁸ Willis Towers Watson (2021), "2022 Global Medical Trends Survey Report".

Diagram 5 :
Key success factors to sustainably manage medical costs and claims inflation



With these findings in mind, we will aim to advance efforts to help address these issues, anchored on three intended outcomes:

- First, we will **explore measures that can steer positive change in behaviour** among actors in the private medical healthcare ecosystem so that covers remain inclusive and sustainable for policy and certificate holders, and financially viable for insurance and takaful providers.

We will work with relevant stakeholders to explore measures that can promote more responsible usage among consumers, including the feasibility of introducing more meaningful cost-share⁹ features in HSIT covers. Based on our observation, cost-sharing features implemented in other countries have effectively nudged positive consumption behaviour by reducing “buffet syndrome”¹⁰ among policy and certificate holders, and thereby moderate excessive utilisation of medical services that can lead to higher claims inflation. In Malaysia itself, based on a sample group of HSIT¹¹, we have observed how cost-sharing features have reduced premiums/contributions by 19% to 68%.

To complement cost-share features, we will also explore the viability of other mechanisms to encourage active savings and mobilise funds for medical-related expenditures. Such savings mechanisms would enable better management of longevity risks – funds can be used to fund top-up premiums/contributions, rises in future medical costs, and out-of-pocket expenses for services not covered under medical covers. As such, we will explore and assess the suitability of establishing a national-level plan with relevant agencies and stakeholders vis-à-vis planned healthcare reforms by the Government.

⁹ Cost-sharing refers to the portion of costs for healthcare services that is shared between the patient and their insurer/takaful operator.

¹⁰ A phenomenon where policy and certificate holders seek to maximise the value premiums/contributions paid, thereby consuming medical services without considering the reasonability or necessity of associated costs. This invariably leads to over-consumption of medical services.

¹¹ Based on a range of products with deductibles between RM300 – RM50,000.

- Second, we aim to **support better cost control management and transparency** of the MHIT cover by leveraging digital solutions. This will be pursued in phases, with the first phase focusing on setting up data protocols among ITOs. Ideally, this can also be expanded to standardise data protocols among hospitals in collaboration with the relevant stakeholders in the future.

As a start, the Bank will facilitate the collection and standardisation of MHIT claims data across the industry via a centralised data exchange platform. This aims to enable greater industry-wide analysis of medical claims data and pave the way for both the publication of cost of common medical procedures and implementation of minimum cost-sharing levels. We will steer the industry to establish an open data architecture for the platform to lay the foundation for ITOs to transmit and analyse the data in a more efficient as well as systematic way, as part of the broader vision to digitalise MHIT data.

We will also advocate for greater transparency for consumers to make informed healthcare decisions on their preferred medical provider and the reasonableness of costs incurred – this includes working with the Ministry of Health (MOH) to provide relevant information to the public on the cost of common medical procedures. Similar efforts have been observed to be effective in Singapore, Australia, and the USA.

- Third, we will **institute higher standards on business conduct and sales practices**, including but not limited to: (i) enhancing product disclosure sheet requirements to improve understanding by consumers and encourage informed actions; (ii) strengthening needs-based sales requirements for MHIT products to reduce the risk of mis-selling; and (iii) providing additional guidance on repricing practices to promote a more objective, structured and consistent repricing approach for the industry moving forward.

Managing the long-term affordability and sustainability of medical reimbursement cover in Malaysia requires coordination and collaboration by all stakeholders in the ecosystem from payors, healthcare providers, managed care organisations, the Government and regulators, to consumers. Wider structural reforms and coordinated efforts led by the MOH will be necessary to ensure healthcare services remain inclusive and affordable for all. To this end, the Bank is committed to working with MOH and other relevant stakeholders to advance the above measures together with the industry and support wider ecosystem reforms.

- We will **support early financial planning and access to diverse financial solutions that meet the retirement needs** of individuals. We will facilitate the development of new business models and solutions in the retirement planning ecosystem that will address coverage gaps, as well as complement this with our literacy efforts on financial planning for retirement under the FEN. Importantly, immediate efforts to rebuild retirement funds depleted by early withdrawals and relief measures, together with broader reforms through the three pillars of social protection, will be key to strengthen financial resilience for retirement (refer to ‘comprehensive social protection reforms’ in the earlier part of this section).

Strategy 2C

Shape a financial system that upholds fair and responsible dealings with financial consumers

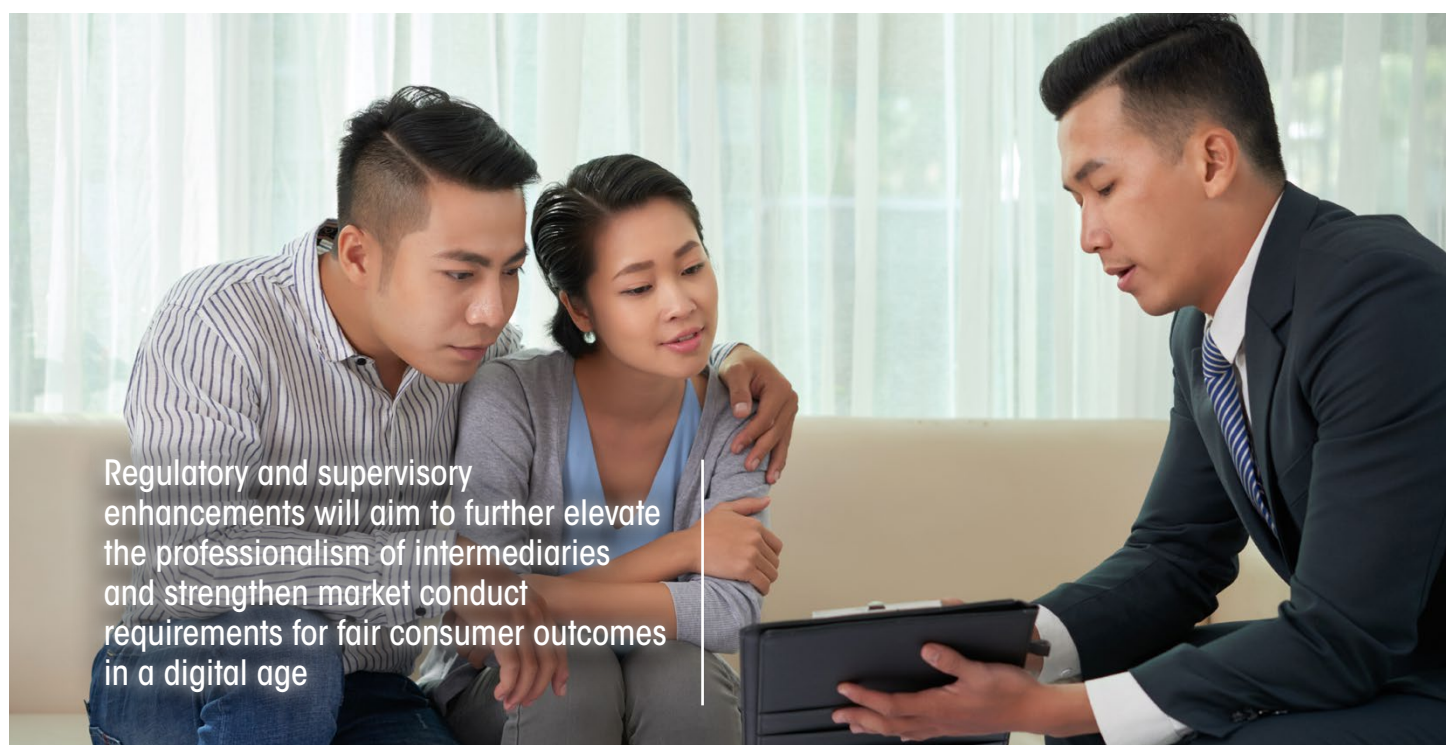
An effective consumer protection framework is critical for an inclusive and enabling financial services landscape – it creates trust, inspires confidence, and empowers consumers with knowledge of their rights and responsibilities. This in turn supports more active and productive use of financial solutions by consumers. The acceleration of digital finance presents tremendous opportunities to enhance the consumer empowerment journey by providing consumers with more needs-based, personalised solutions and innovative tools to make informed financial decisions. However, it also introduces new risks that can undermine consumer trust – such as digital fraud, misuse of personal data, and financial exclusion associated with machine learning biases – which must be actively mitigated.

Emerging financial service applications enabled by AI/ML such as robo-advisory platforms, aggregator services, and personal financial management are already gaining market acceptance. In some cases, these platforms displace the role of agents, in particular those who do not upskill to deliver more value to their customers with specific, needs-based, and cost-efficient advisory services. This places greater urgency for brick-and-mortar intermediaries – particularly insurance and takaful agents – to consider how their business practices must evolve to remain relevant, be it through digital transformation, adoption of higher standards of professionalism, or both.

In navigating the environment ahead, we will foster an enabling regulatory environment that continues to deliver fair and sound consumer outcomes by addressing undue regulatory frictions, and further empowering consumers. At the same time, we will also enhance existing consumer protection and market conduct frameworks by addressing emerging consumer concerns and placing greater accountability on FSPs to safeguard the interests of consumers. This will be underpinned by our overarching principles in regulating innovation (see Strategy 3B(iii) of the chapter “Advance digitalisation of the financial sector”).

To this end, we will seek to advance the following:

- i. Strengthen professional standards, incentive frameworks and disclosure practices;
- ii. Promote an enabling conduct environment for innovation and efficiency; and
- iii. Pursue regulatory reforms to strengthen the oversight of non-bank consumer credit providers and promote consistent consumer protection.



Regulatory and supervisory enhancements will aim to further elevate the professionalism of intermediaries and strengthen market conduct requirements for fair consumer outcomes in a digital age

i Strengthen professional standards, incentive frameworks and disclosure practices

- We will **ensure a responsive regulatory framework for conduct regulation** of new and existing intermediaries, particularly in the insurance and takaful business.
 - We will **review existing regulatory requirements on the conduct of intermediaries** to accommodate new digital business models and the expansion of solutions offered by existing intermediaries – such as insurance/takaful agents, brokers and financial advisers (FAs). This will also promote the entry of credible new digital intermediaries that can offer innovative solutions to minimise critical protection gaps among underserved segments by leveraging the outreach potential of their platforms.
 - We will **enhance the bancassurance/bancatakaful policy framework** to strengthen consumer safeguards and ensure the fair and responsible promotion of insurance/takaful products through the bancassurance channel. As bancassurance/bancatakaful evolves as a key distribution channel – particularly for life insurance and family takaful products – we see room to better align the conduct and sales practices of bancassurance agents with consumer needs. Policy refinements include reinforcing internal governance requirements and requiring effective consumer needs-based identification, targeting, and marketing to be conducted moving forward. This aims to ensure that the bancassurance channel continues to grow in a sustainable and responsible manner, with due regard to the interests and needs of financial consumers.
- We will **elevate the professionalism and integrity of intermediaries** in dispensing their roles to better support informed financial decisions by consumers.
 - We will **enhance professional qualification and employee screening requirements** to bolster public confidence in the agency workforce as a fair and trusted distribution channel. The agency workforce remains a key bridge between ITOs and consumers, with 41% of business transacted in life insurance/family takaful business facilitated by the workforce in 2020¹². To better equip life insurance/family takaful agents with the necessary skills to conduct a financial needs analysis and explain product risks, we will enhance existing entry-level qualification requirements. We will also impose more robust standards on ITOs with regard to employee screening and procedures to ensure agents' compliance with fit and proper requirements.
 - The Bank and the SC will **conduct a joint review towards rationalising the regulation of insurance/takaful and capital market intermediaries** who provide advisory services to financial consumers and investors into an integrated licensing framework. FAs and financial planners (FPs) play an important role in providing quality financial and investment advice to facilitate informed decisions by consumers. At present, FAs which are approved to advise on insurance/takaful products are regulated by the Bank, while FPs licensed to advise on capital market products fall under the SC's purview. However, most FAs also apply for FP licenses with the SC to offer a full range of advisory services to their customers. Recognising this, the rationalisation aims to reduce regulatory costs from the dual licensing regime of FAs and FPs and enable greater efficiency through the offering of a wider range of financial advisory and planning services.
 - We will **review and strengthen the incentive frameworks for insurance and takaful intermediaries** to ensure alignment with the delivery of good consumer outcomes and experiences. As financial solutions increase in diversity and complexity, consumers place higher trust and reliance on intermediaries to have their best interests in mind when recommending products. Our measures will aim to promote greater transparency and align incentive frameworks with these expectations. We will begin by exploring the viability of transitioning from a commission-based to a fee-based remuneration structure and further improving disclosures to consumers on the amount, type, and source of remuneration received by intermediaries.

¹² Source: Bank Negara Malaysia.

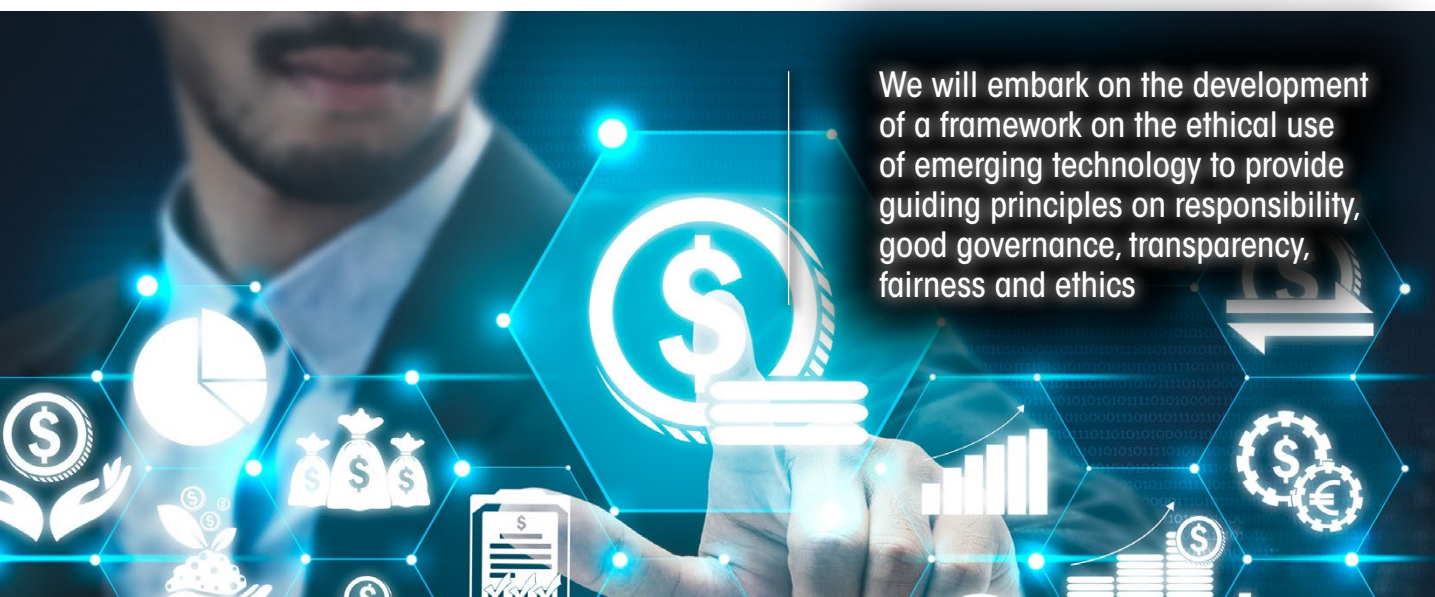
- We will **enhance the effectiveness of product transparency and disclosure requirements** by improving accessibility to key product information and leveraging behavioural insights to facilitate informed financial decisions. To this end, we will:
 - **Double down on the use of plain language** with better navigation (e.g. sign-posting with bite-sized guides, diagrams) to aid consumers in distilling the benefits, risks as well as key terms and conditions behind the products offered.
 - **Ensure that disclosure requirements** continue to reflect the changing needs and experiences of consumers (e.g. disclosures via digital channels for consumers who access financial services through mobile devices).
 - **Make greater use of behavioural insights** to nudge consumers towards responsible and optimal financial choices. For example, interactive designs and mobile-friendly layouts have been shown to encourage reading by consumers who are less inclined to review digital disclosure documents.
- We will incorporate **conduct risk assessments as a key component of supervisory engagements with financial institutions under the annual Composite Risk Rating (CRR)¹³ review process**. This adds another dimension beyond safety and soundness criteria, which form the current focus of the CRR communication. FSPs will be assessed on their conduct and business practices, as well as the extent to which these practices may cause harm to consumers and pose material financial or reputational risks to FSPs. We may also issue public reprimand as part of our enforcement, with the aim to reinforce a strong conduct risk culture within FSPs. As FSPs strengthen accountability for and management of conduct risks moving forward, this is envisioned to further pave the way for the Bank to adopt a more principles-based approach to the regulation of conduct risk.



¹³ Represents the FSP's overall risk profile, level of monitoring and type of supervisory intervention required by the Bank. This in turn determines the category of deposit protection premium the FSP falls under.

ii Promote an enabling conduct environment for innovation and efficiency

- We will **outline minimum parameters for conduct risk identification and mitigation** for new business models and innovations by the industry. For example, the use of technology to capture, store, and analyse data must be complemented by safeguards to prevent the misuse of customer data and exposure to cyber security risks. As the landscape continues to evolve with greater complexity from innovation, FSPs must also regularly enhance their business continuity and resolution framework through clear contingency planning, recovery and exit resolutions to minimise disruption to financial services delivery and safeguard consumer interests in the event of market exits.
- We will **outline guiding principles and regulatory expectations on the ethical use of emerging technology**, in particular AI. Applications of AI can offer a significant leap in process efficiency and enrich the customer experience, such as through automated credit assessments enabled by algorithms and non-traditional indicators such as social media postings and online purchase transactions. However, AI algorithms are also subject to biases that can lead to unfair outcomes or unintended financial exclusion of certain consumer segments that are otherwise creditworthy borrowers. Proper AI governance is important to mitigate these instances. Consistent with global regulatory developments, our framework will therefore aim to emphasise the importance of fair and ethical use of such technologies, underpinned by robust and transparent AI governance.
- We aim to **facilitate greater ease of product comparison, portability and innovative product offerings by FSPs**. In doing so, we will focus our efforts towards identifying structural reforms that will promote greater market transparency and competition in order to benefit consumers.
 - First, we will **ensure the effective implementation of the enhanced Reference Rate Framework (RRF)¹⁴ for a more competitive loan market**. The framework which takes effect in August 2022 will introduce the Standardised Base Rate (SBR) as a common reference rate for all FSPs in pricing new retail financing facilities, where the price of the facility offered to consumers will be quoted as “SBR + spread”. This change aims to make it easier for consumers to identify the FSPs offering the most competitive rates. We will also pursue parallel efforts to enable a more efficient and competitive loan market, by exploring measures to minimise switching costs for consumers.
 - Second, we will **facilitate broader efforts towards open and secure data sharing** that will support ease of product comparison and switching by consumers (refer to Strategy 2A(ii) in this chapter and Strategy 3A(ii) of the chapter “Advance digitalisation of the financial sector” for further details). To this end, we will first focus on establishing data infrastructures and a robust data governance framework.



We will embark on the development of a framework on the ethical use of emerging technology to provide guiding principles on responsibility, good governance, transparency, fairness and ethics

¹⁴ The Policy Document on ‘Reference Rate Framework’ was issued on 11 August 2021 and will be effective from 1 August 2022. Further details are accessible at <https://www.bnm.gov.my/documents/20124/938039/Reference+Rate+Framework.pdf>.

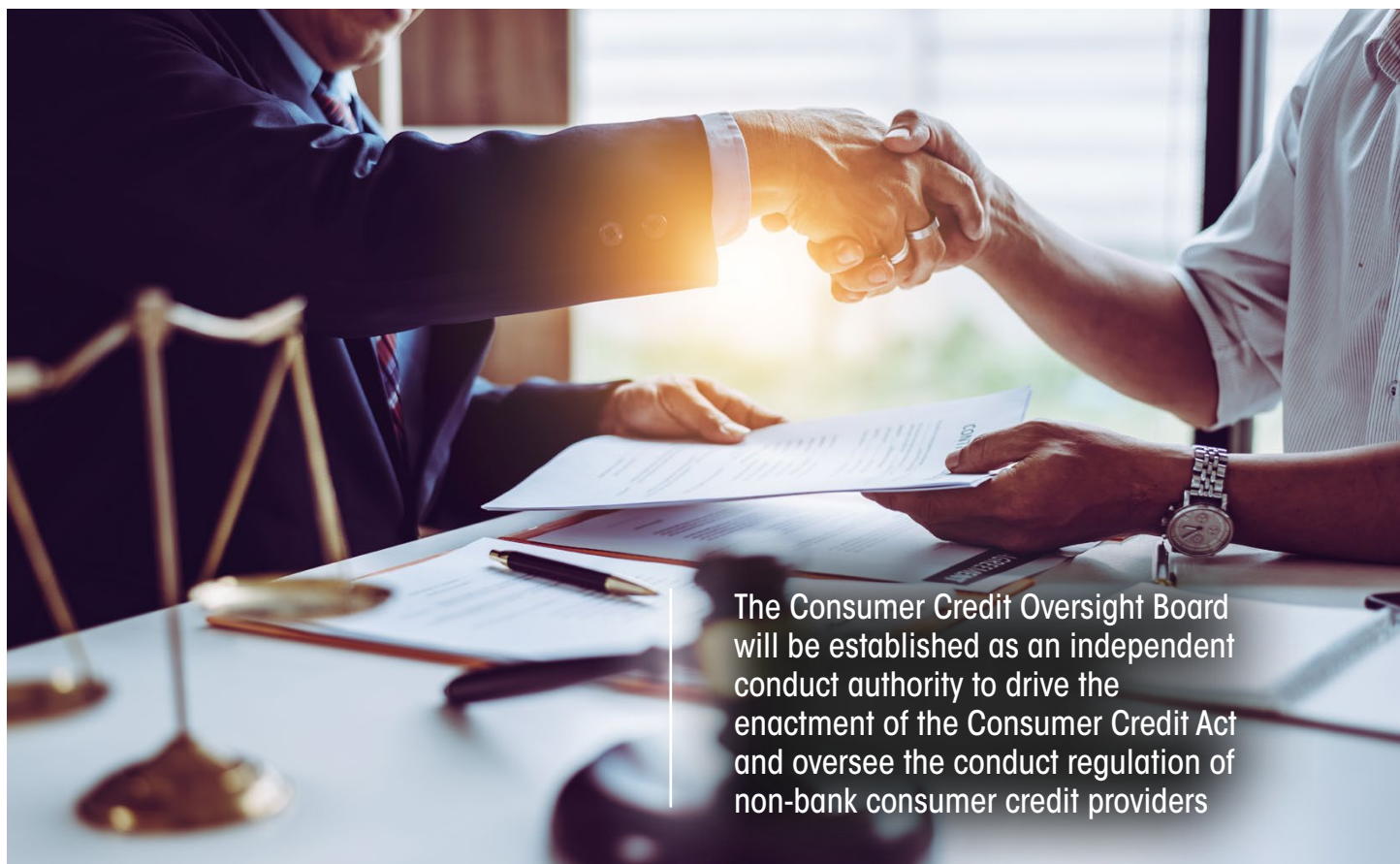
iii Pursue regulatory reforms to strengthen the oversight of non-bank consumer credit providers and promote consistent consumer protection

■ We will work closely with the MOF and the SC to **reform the conduct regulatory architecture** to strengthen regulation of non-bank consumer credit providers. This will be achieved through the following:

□ First, the **enactment of the proposed Consumer Credit Act (CCA)**. Overlaps in responsibilities between regulatory authorities and coverage gaps in the supervision of consumer credit providers have led to inconsistencies in the level of protection accorded to consumers. Recognising this, the Bank and the SC, with the support of the MOF, are leading reforms to close these gaps through the enactment of the CCA. Under the proposed CCA, the Consumer Credit Oversight Board (CCOB) will be established to serve as an independent conduct authority to oversee consumer credit providers which are not currently subject to conduct regulation¹⁵. Over the longer term, these functions are expected to expand to include other non-bank credit

providers that are currently under the purview of various Ministries and agencies, with a view to ultimately transition to an integrated structure for the regulation of financial conduct in Malaysia.

□ Second, the **OFS and the Securities Industry Dispute Resolution Center (SIDREC) will be consolidated** into an integrated dispute resolution scheme. An independent dispute resolution framework is important in our effort to ensure effective redress arrangements are available to financial consumers. The OFS was established to provide dispute resolution related to entities regulated by the Bank, while SIDREC under the SC provides dispute resolution services to investors dealing with capital market products, services, and institutions. Consolidation of the OFS-SIDREC aims to enhance operational synergies of dispute resolution schemes given the increasing complexity of financial solutions and blurring of lines between financial and capital market activities conducted by FSPs.



The Consumer Credit Oversight Board will be established as an independent conduct authority to drive the enactment of the Consumer Credit Act and oversee the conduct regulation of non-bank consumer credit providers

¹⁵ Leasing companies, factoring companies, debt collectors, non-bank impaired loan buyers, entities offering Buy Now Pay Later schemes.

Strategic Thrust 3

Advance digitalisation of the financial sector

Digitalisation continues to have widespread implications for financial services. Customers are expecting faster, more frictionless, and more customised services, with growing awareness about the importance of data privacy and security. Digital business models are also becoming more ecosystem-driven, whether through a platform or a network of partnerships. Alongside this, the risk landscape is also being reshaped. Boundaries are blurring, with new and more complex interlinkages within and beyond the financial sector. The key will be for Malaysia's financial industry to take advantage of the upsides of digitalisation, while managing the associated risks – especially those that may threaten system-wide stability, consumer outcomes, and confidence in the financial sector.

To this end, we will advance four key strategies (Diagram 1).

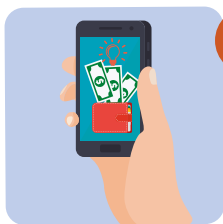
Diagram 1:
Advance digitalisation of the financial sector



A

Futureproof key digital infrastructures

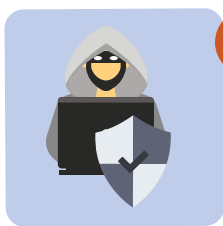
- ◆ Leverage key financial infrastructures for Malaysia's broader digital ecosystem
- ◆ Advance development of an open data ecosystem that is fair and fit for the future



B

Support a more vibrant digital financial services landscape

- ◆ Enhance pathways for digital innovations to test, scale and exit
- ◆ Support industry-led strategies for digital payments adoption
- ◆ Preserve effective oversight of digital business models



C

Strengthen cyber security readiness and responsiveness

- ◆ Strengthen system-wide cyber security oversight and capabilities
- ◆ Strengthen domestic and global collaborative efforts on cyber security



D

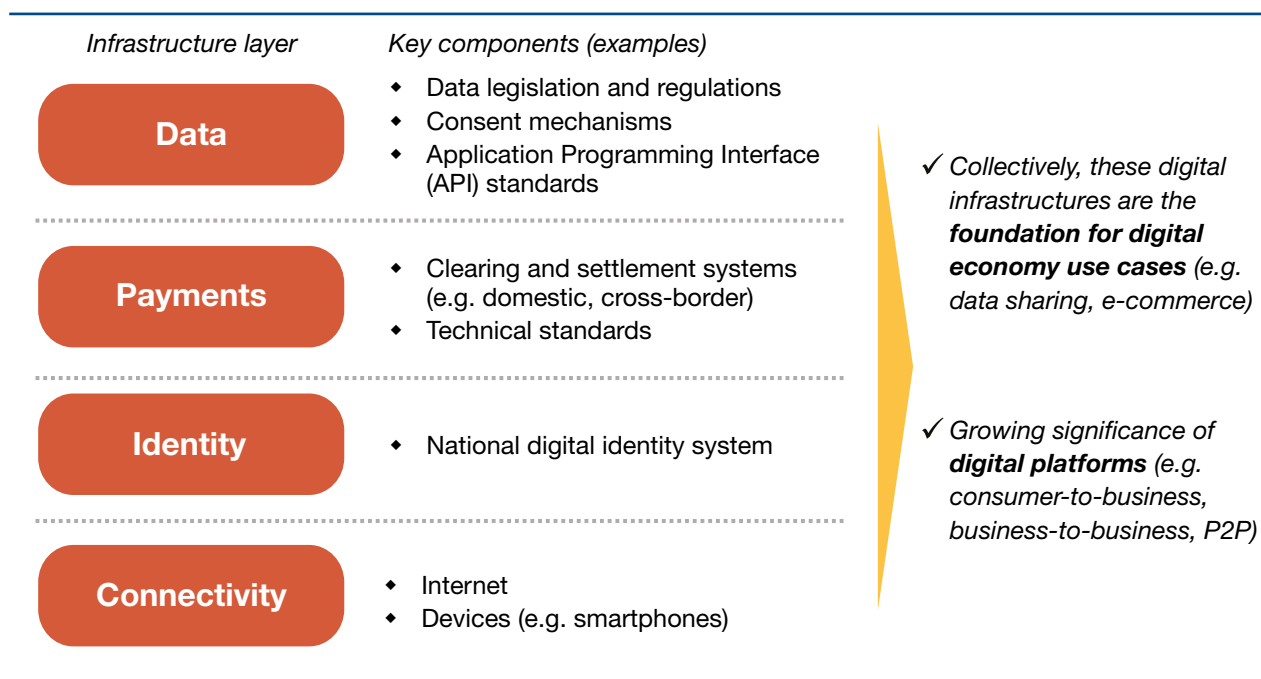
Support greater use of technology for regulation and supervision

- ◆ Leverage technology to further strengthen the Bank's regulation and supervision of the financial industry
- ◆ Futureproof the Bank's data strategy

Strategy 3A Futureproof key digital infrastructures

A digital economy is built upon a combination of technological infrastructures (Diagram 2). Financial infrastructures are a vital part of that. Payment and settlement systems, for example, enable day-to-day economic activities of households and businesses. As more transactions move to the digital sphere, so does data – and the vast potential and risks that come with it.

Diagram 2:
Key infrastructure layers in the digital economy



Our strategies to futureproof key financial infrastructures will be anchored on several desired outcomes. First, these infrastructures should be resilient, particularly to enable a secure ecosystem and preserve the continuity of critical services in adverse situations. Second, these infrastructures should be inclusive – designed to promote openness and interoperability, reflecting the increasingly diverse profile of stakeholders in the financial landscape, without compromising the safety of the system. Third, these infrastructures should be adaptable to emerging developments, including new technologies and operating models.

Broader digital infrastructures, including non-financial ones, are also equally important for financial development objectives. Similar outcomes like resilience, inclusivity, and adaptability should also guide the development of these infrastructures. Connectivity and digital identity are some key examples that support greater innovation and adoption of digital financial services. It will also be important to leverage emerging digital platforms to unlock major upsides for the financial sector and broader economy.

For the data ecosystem, we will look to advance efforts that can better serve financial consumers. These include policies and safeguards that support responsible and ethical usage of data, as well as facilitate fair and reciprocal data sharing initiatives among participants in Malaysia’s data ecosystem. These efforts will be reinforced by collaborative initiatives with the Government to accelerate the roll-out and enhancements of these broader infrastructures.

To this end, we will:

- i. Leverage key financial infrastructures for Malaysia’s broader digital ecosystem; and
- ii. Advance the development of an open data ecosystem that is fit for the future.

i Leverage key financial infrastructures for Malaysia's broader digital ecosystem

- We will aim to **futureproof Malaysia's payment systems – particularly real-time payment infrastructures**, including real-time gross settlement systems and retail payment systems, focusing on three areas:

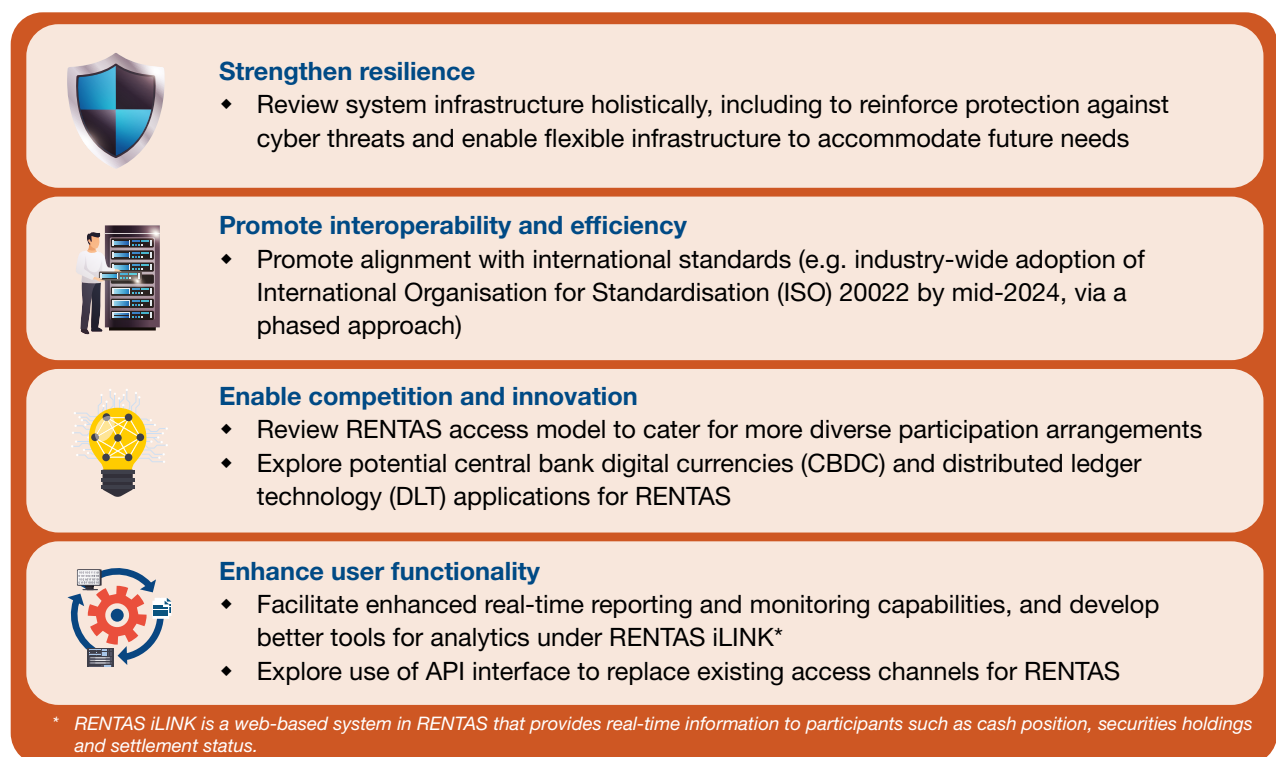
- **A multi-year modernisation exercise for the Real-Time Electronic Transfer of Funds and Securities Settlement (RENTAS)**. As part of this exercise, we will review the RENTAS access model to cater for more diverse participation – including by non-bank payment service providers (PSPs), without compromising the operational and cyber resilience of RENTAS. Besides levelling the playing field between banks and non-bank PSPs, this would expand the range of transactions settled using central bank money – in turn, potentially lowering settlement risk in the ecosystem. The modernisation exercise will also include initiatives to strengthen the end-to-end risk management in RENTAS, promote interoperability and efficiency, facilitate competition and innovation, as well as to enhance user functionalities (see Diagram 3 for summary).

We will review the RENTAS access model to cater for more diverse participation, including by non-bank payment service providers

- Enabling **shared payment infrastructures** in Malaysia's payments ecosystem, including the RPP. These infrastructures allow industry players to pool resources and share costs, while competing at the product level to better serve end-users, such as consumers and merchants. A key priority will be to preserve and ensure effective implementation of open and risk-based access regimes for banks and non-bank PSPs – whether through direct or indirect participation regimes¹.

Other areas of focus include facilitating the adoption of common technical standards (e.g. ISO 20022, DuitNow QR), and exploring opportunities to leverage on shared payment infrastructures for more use cases (e.g. welfare payments, tax refunds, fraud analytics, trade finance).

Diagram 3:
Key objectives of RENTAS modernisation exercise



¹ Indirect participation regimes are where a non-bank payment service provider relies on an intermediary (also known as a 'sponsor institution') to indirectly join the network of a shared payment infrastructure. Some PSPs may prefer the indirect participation regime due to specific commercial or operational needs.

- **Intensifying efforts to enhance cross-border payments efficiency.** We will work with industry players to address challenges associated with cross-border payments, such as high costs, low speed, limited access, and insufficient transparency. This includes linking up the RPP with other real-time payment systems in the Association of Southeast Asian Nations (ASEAN) region and beyond, focusing on countries with strong economic linkages with Malaysia. We will build on the recently established QR payment linkages with Thailand and Indonesia and the ongoing work with Singapore and the Philippines. The goal will be to expand the scope of use cases to P2P fund transfers as well as to establish similar linkages with other countries in the region and beyond. Beyond this region, we are also working on a proof-of-concept (POC) with the Bank for International Settlements (BIS) Innovation Hub and other partners in Project Nexus to develop a multilateral and scalable mode, which aims to connect all real-time payment systems globally to facilitate fast and seamless cross-border payments.

In addition to real-time payment linkages, we will **explore emerging payment innovations for cross-border payments**, such as the use of multi-CBDC arrangements. Unlike existing correspondent banking arrangements, the use of CBDC could shorten the transaction chain and free up liquidity that is 'trapped' in correspondent banking accounts – thus resulting in faster and cheaper cross-border payments. We will be embarking on collaborative initiatives in this regard. This includes building on findings from our participation in Project Dunbar, where we have partnered with the BIS Innovation Hub and other central banks – namely, Reserve Bank of Australia, Monetary Authority of Singapore, and South African Reserve Bank – to test the

use of multiple CBDC and DLT for cross-border settlements.

- We will **intensify research and experimentation on the use of central bank digital currencies** for Malaysia's monetary and financial infrastructures – with the initial focus on wholesale payments – as part of broader efforts to respond to digital currency developments (refer to the box article "Digital currencies: A new frontier").
- The effective delivery of digital financial services also hinges on the **availability of common, non-financial digital infrastructures that support all sectors of the economy**. To this end, there are three key areas that we will continue to pursue in cooperation with the Government and relevant agencies:
 - **The establishment of a national digital identity**, which requires a coordinated collaboration between different government agencies and the private sector. We will continue to advocate for speedy and effective implementation, to cater to both existing and future needs (particularly in relation to the choice of technology for authentication).
 - Legislative and regulatory reforms to facilitate end-to-end digitalisation of business processes, such as **the use of digital and electronic signatures** by the both private and public sectors.
 - Speed, quality, and affordability of **internet connectivity** across the country and segments of society. This in turn will facilitate greater accessibility and usage of digital financial services, especially among the underserved and unserved segments as well as those in the rural areas.





ii Advance the development of an open data ecosystem that is fit for the future

- We will continue to **facilitate efforts to develop common standards for data sharing in the financial sector, particularly for high-impact use cases**. Therefore, we aim to focus efforts on use cases that:

- **Promote greater financial inclusion.** These include facilitating new data sharing arrangements, such as on “thin file” consumers – namely, those with little or no credit history – to enable the development of alternative credit scoring models. This aims to make use of alternative forms of data such as payments or utilities data, which can help enrich the creditworthiness assessment.
- Support consumers to make **better informed financial decisions**, such as through financial planning. These include personal financial management solutions, providing better quality information to consumers, and nudging consumers towards better financial behaviour (such as encouraging habits in relation to savings and investments).

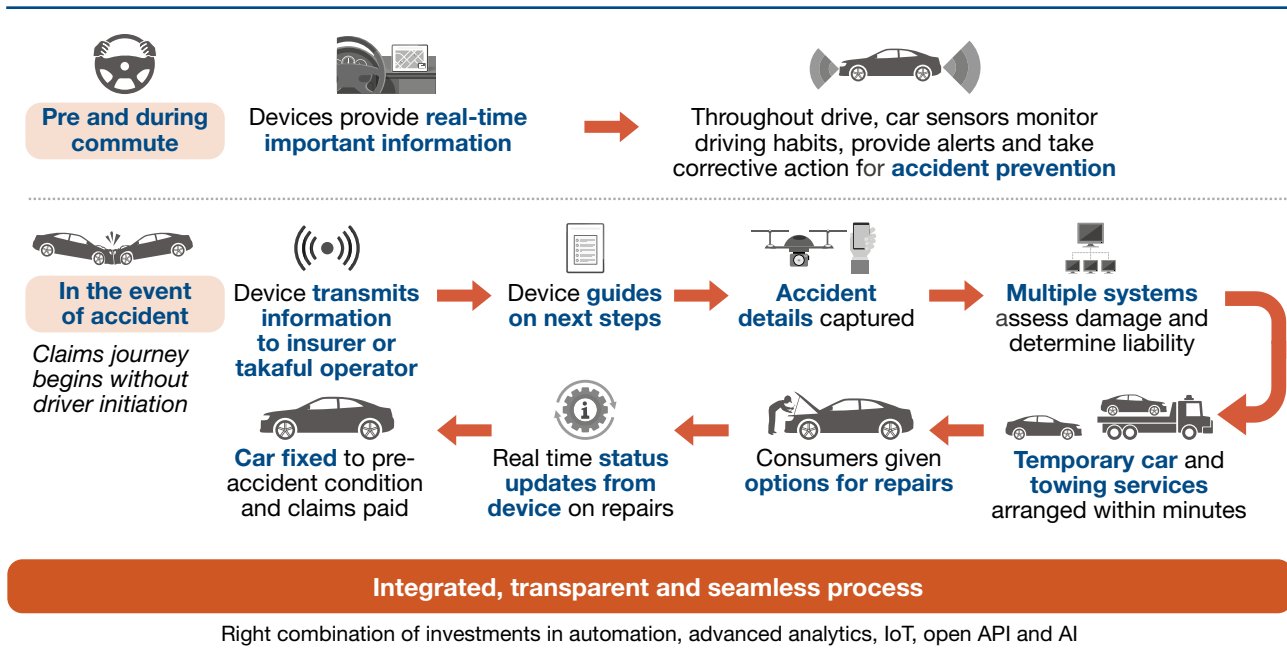
Where specific use cases have been identified by the industry, we will work closely with the relevant stakeholders on the development of common data standards and suitable data sharing arrangements – with the view to provide guidance on policy and regulation, where appropriate. A market-led approach will generally be preferred to provide industry players with sufficient space to test and iterate, before converging on standards that are fit-for-purpose. However, we may consider

establishing mandates to accelerate progress, where warranted, to serve the broader public interest in line with the Bank’s regulatory objectives.

- We will **support efforts to establish shared data infrastructures for the financial sector and its broader value chain**. This would include emerging digital platforms that enable more seamless and efficient connections among various users. As with other key digital infrastructures, our priority will be to promote the adoption of open and interoperable design principles. Examples of these infrastructures include trade finance infrastructures (e.g. for detection of duplicate invoicing), a medical claims data exchange (e.g. for costs of common medical procedures) that is accessible by industry players, as well as modernised systems that enable an end-to-end digital experience for motor claims.

For insurance and takaful services in particular, digitalisation is a key game changer that will bring the current level of services to new heights – especially to create a hassle-free experience for consumers making motor claims, and address prevailing pain points in the process. To this end, we will intensify efforts to pave the way for insurers and takaful operators to advance digital transformation efforts that will deliver more integrated, transparent, and seamless processes (see Diagram 4 for desired outcomes for the motor ecosystem). This includes establishing and improving existing infrastructure to support the adoption of digital technologies across the claims process. This is a necessary precondition for the full liberalisation of motor tariffs.

Diagram 4:
Digitalisation - A game changer for consumers' claims experience



■ We will **continuously review the data governance framework for the financial sector**, in tandem with legal developments and technological applications to ensure the protection and fair treatment of financial consumers. This includes potential enhancements to customer consent mechanisms and requirements around the ethical and responsible usage of data – which are key elements in building a trusted data regime. We expect FSPs to collect, process, and share personal consumer data in a lawful and secure manner such that individuals know how their data will be used and give consent to such usage. Data must also be used in ways that do not result in the unfair treatment of consumers.

■ Beyond the financial industry, we will continue to collaborate with industry players and other stakeholders to **enable broader arrangements for more open and secure data sharing, focused on three priorities:**

□ **Improving accessibility to public data** under the Government's open data initiatives. These initiatives, such as the Malaysian Administrative Modernisation and Management Planning Unit's (MAMPU) Open Data platform, provide the potential for various stakeholders – including the financial sector – to leverage datasets residing in other agencies to build data-driven innovations to better serve the public. To make data sharing more seamless, it will be important

to synchronise key reforms discussed in flagship policy documents (e.g. RMK12, MyDigital) and develop a uniform approach to data governance. This in turn will provide the necessary foundations for the adoption of interoperable standards and formats across sectors.

□ **Supporting national efforts to develop a data protection legal framework.** Primarily, we will do this through our membership in national-level committees. We will also collaborate with government agencies in relation to key laws and policies, such as on the drafting of NDSP and amendments to the Personal Data Protection Act 2010 (PDPA). The implementation of both NDSP and amended PDPA will strengthen the confidence and trust of data users to facilitate greater data sharing in the digital economy as a whole.

□ **Supporting regional level data sharing initiatives.** To this end, we will continue to collaborate with government agencies and industry players to advance best practices with respect to cross-border data flows that are aligned with global standards and policies. Key focus areas include managing cross-border fraud and money laundering, support risk management practices of internationally active financial institutions, as well as promote trade activities, including within the ASEAN region.

Strategy 3B

Support a more vibrant digital financial services landscape

Technological changes have taken place at an unprecedented pace in recent years, enabling new applications in financial services. The pandemic has only accelerated this, as customers sought to access 'low-touch' or completely digital channels – in turn, shaping behavioural norms for financial services.

New technologies can redefine the landscape, pushing the boundaries of what is technically and operationally possible. Efforts need to be centred on keeping pace and responding effectively to technology.

Our strategies on this front will aim to foster an enabling environment for innovation, while preserving broader financial system stability. We will also prioritise strengthening institutional arrangements to facilitate greater collaboration – among industry players, regulators, and other agencies.

To this end, we will seek to advance the following:

- i. Enhance pathways for digital innovations to test, scale, and exit;
- ii. Support industry-led strategies for digital payments adoption; and
- iii. Preserve effective oversight of evolving digital business models.

i Enhance pathways for digital innovations to test, scale and exit

- We will enhance testing mechanisms for financial innovation in two key ways.

First, we will **refresh our Regulatory Sandbox**. The Sandbox has played an important role in advancing digital innovation so far, paving the way for critical use cases such as electronic Know-Your-Customer (e-KYC) and new business models such as digital insurers, P2P family takaful and digital remittance. The Sandbox will continue to support industry players in bringing financial innovations safely to the market, across different stages of the innovation cycle.

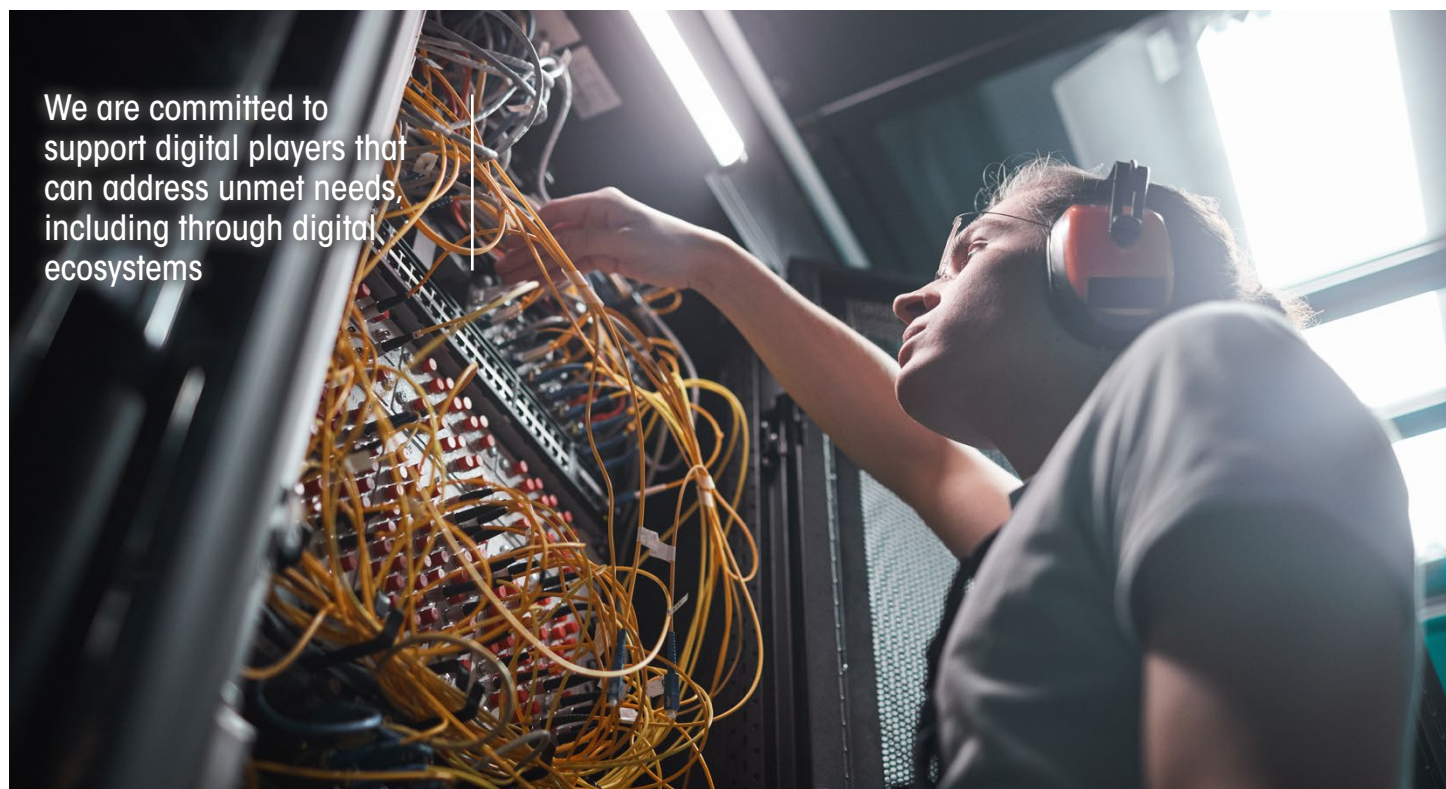
Enhancements moving forward will aim to accelerate time-to-live testing under the Sandbox. For late-stage or more mature innovative solutions, this may include accelerated tracks for lower-risk activities or simplified testing parameters for players who can demonstrate robust governance and risk management practices. In particular, for financial institutions that we already regulate, we will simplify and reduce the Sandbox's gatekeeping processes to test new value propositions and address regulatory implications. This will aim to allow financial institutions to test their innovations more quickly and flexibly, supplemented with principles-based testing parameters.

Drawing from our experience with a specialised e-KYC testing track, we will also consider similar accelerated tracks for other relevant use cases. This would cover activities where the risks are low or can be managed within standardised and pre-determined boundaries, or where development of relevant policies is already underway. Such activities include insurance and takaful aggregation activities.

Second, we will look to **advance 'collaborative pilot' mechanisms** for areas where digital transformation is needed at the industry or national level. This is relevant for financial innovations that are multi-stakeholder in nature – whereby testing and iteration across the value chain is needed to pave the way towards viable business models and arrangements for the industry. These include efforts to establish shared utilities or platforms, promoting common standards, or piloting new industry use cases.

Previously, we have adopted a collaborative approach in promoting common open API standards and developing Project Spyder² a DLT-based trade finance solution. In addition to continuing such efforts, we will also seek to advance efforts towards establishing shared digital infrastructures for insurance and takaful solutions, as set out in Strategy 3A(ii) of this chapter.

² Project Spyder is a proof-of-concept developed in 2019 between the Bank and an industry consortium of leading Malaysian banks to detect duplication of invoice financing and to enable interbank sharing of invoice information in a secure manner. The testing phase of Project Spyder concluded in November 2019, in which more than 1,700 duplicate invoices were detected from over 290,000 invoices submitted from participating banks.



We are committed to support digital players that can address unmet needs, including through digital ecosystems

- We will **facilitate greater digitalisation of business models in financial services**, prioritising those that can advance greater financial inclusion by better meeting the needs of the unserved and underserved (refer to the chapter “Elevate the financial well-being of households and businesses”).

A key priority will be the **smooth implementation of the digital banking framework**. We are committed to ensure that the policy environment remains relevant, as digital banks and incumbents continue to evolve their business models (e.g. through greater partnerships with other FSPs or third parties) to create an ecosystem that will better address underserved and unserved segments, without jeopardising system-wide stability and consumer outcomes. A key consideration will be to foster an appropriate regulatory environment for all players engaged in banking services – be it through traditional or digital channels, consistent with the principles of parity, proportionality and neutrality (refer to Strategy 3B(iii) in this chapter).

Additionally, we will **finalise a regulatory framework for digital insurers and digital takaful operators in 2022**, with the view to significantly elevate the dynamism of the sector. We aim to license new digital players in 2023 that can leverage technologies to deliver value propositions on three fronts. First, inclusion – to enhance the financial resilience of customers whose protection needs are not adequately served. Second, competition – to transform the existing market structure of insurance/takaful through innovative solutions. Third, efficiency – to deliver a more frictionless consumer experience and protection at lower costs.

- We will continue to **advocate and support the growth potential of Malaysia’s broader fintech ecosystem**. In addition to broader digital infrastructures (refer to Strategy 3A in this chapter), we will also aim to seamlessly integrate our frameworks – such as the Sandbox – with other initiatives, both at industry and national level. This will aim to establish an extensive network of key stakeholders that can connect fintech start-ups to a comprehensive suite of support facilities, ranging from capacity-building resources to market access opportunities. This will build on various existing initiatives available, including those under the Malaysia Digital Economy Corporation (MDEC) and the newly formed Malaysian Research Accelerator for Technology and Innovation (MRANTI).



We will continue to accord priority to preserving and further strengthening confidence in digital payments

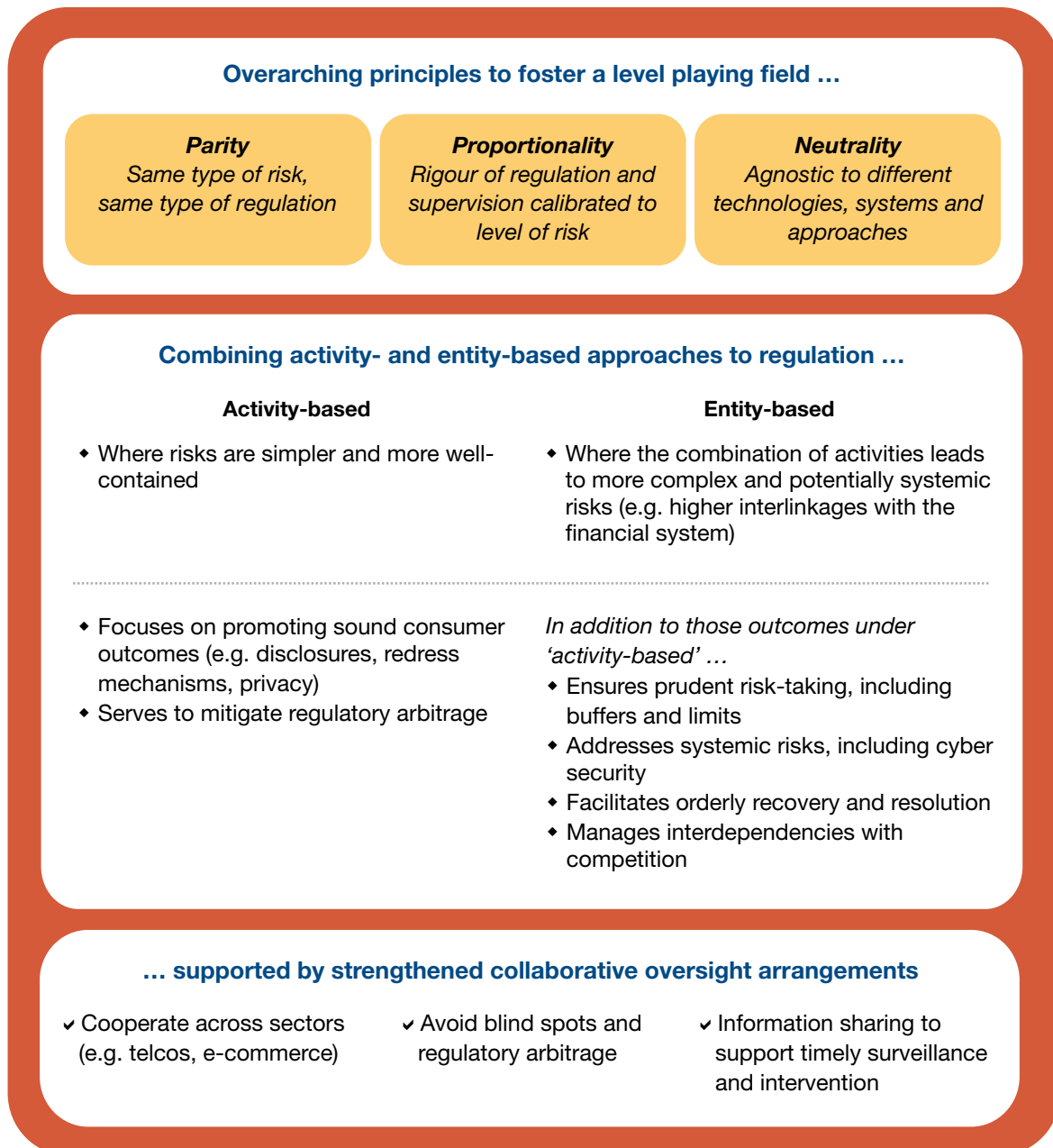
ii Support industry-led strategies for digital payments adoption

- Considering the trajectory of Malaysia's retail payment services landscape, we will **advance an industry-led approach to digital payments development**. Digital payments adoption has risen significantly in Malaysia, accelerated further by the recent pandemic. While regulatory efforts over the past decade have helped catalyse the progress so far, the retail payments industry is also maturing. In more recent years, we have observed the industry becoming highly competitive – especially with the entry of new players – resulting in cheaper and more innovative services to merchants, including SMEs. New consumer-facing technologies, such as biometrics and wearables, have also made digital payments more convenient. Against this backdrop, we expect industry efforts to sustain the momentum of digital payments adoption, as we play an enabling role.
 - As Malaysia's broader economy becomes more digitalised, the importance of payment system operators (PSOs), such as the Payments Network Sdn. Bhd. (PayNet), Visa and Mastercard, to system-wide stability will also intensify – along with growing commercial interest to be PSOs in Malaysia. Given this, we will **advance regulations for PSOs**, which will clarify and align expectations in areas such as governance, risk management, operational resilience, and transparency.
 - We will also **review existing regulatory policies on digital payments**, to ensure their continued relevance. These include the e-Payment Incentive Fund Framework (ePIF), Payment Card Reform Framework (PCRF), and the Interoperable Credit Transfer Framework (ICTF).
 - Efforts will also be made to **pave the way for greater industry leadership and market dynamism in relation to the shareholding of PayNet**. Consistent with PayNet's role as a shared payment infrastructure operator, its shareholding composition will be enhanced to be more reflective of the growing diversity in Malaysia's payments landscape – with the Bank progressively divesting its share in PayNet over time.
- We are **supportive of the broader national aspirations for digital payments under MyDigital**. We expect the commitment by federal and state agencies to adopt cashless payments to play a pivotal role in creating behavioural shifts towards greater digital payments adoption. We are committed to supporting these national aspirations and will intensify our awareness-building strategies to that end.

iii Preserve effective oversight of evolving digital business models

- We will **continuously refine and adapt financial sector policies on digital business models** to ensure that risks are managed effectively. Digital innovation is constantly evolving, shaped by technological change and commercial breakthroughs. In overseeing such a landscape, we will be guided by a set of key considerations to determine the way we regulate digital financial services (Diagram 5):

Diagram 5:
Our approach to regulating innovation



- We aim to **preserve parity, proportionality, and neutrality**. This means that same types of risks will be regulated the same way ('parity') – but with its rigour and intensity calibrated in a way that is commensurate with the level of risk ('proportionality').

In implementing proportionate regulations, we will consider the nature of risks and public interests. For example, in the area of cyber security, especially where it concerns critical financial services, the same rigour of requirements may be warranted for all players to address 'weakest link' risks in the financial value chain – such as where activities are connected to one another across firms or infrastructures (refer to Strategy 3C in this chapter). Similarly, universal consumer redress mechanisms for financial services will continue to be preserved for all financial consumers, irrespective of the size or complexity of the FSP.

We are agnostic to different technologies, systems and approaches ('neutrality'). However, we expect industry players to demonstrate that risks associated with a particular technology or innovation are well-understood, and adequately managed.

Collectively, we expect these to foster a level playing field, while ensuring that digital innovations are supported by sound risk management.

- We will **continue to adopt a combination of activity- and entity-based regulations**³. A purely activity-based approach can be suitable for circumstances where the risks are simpler and relatively insulated. That is, where frictions from adverse events – such as a business failure or temporary service interruption – will not have significant spill-over effects on the financial system or economy. We will adopt activity-based regulations with two key priorities. First, to ensure reasonable protection of sound consumer outcomes, such as through clear disclosures, dispute resolution and redress mechanisms. Second, to mitigate regulatory arbitrage, such that different businesses carrying out the same services are subject to the same rules.

Entity-based regulations are appropriate where certain activities – when combined as part of a business model – can give rise to a more complex risk profile, as well as interdependencies that can amplify market-wide disruptions. This can arise in business models that combine a range of different activities that build an existing ecosystem or platform – sometimes described as 'embedded finance'. In these circumstances, entities may be subject to a comprehensive set of prudential expectations, including those on governance, risk management, financial capacity to absorb losses, and disclosures. Entities that pose systemic risks to the financial system may also be required to develop actionable recovery and resolution plans to protect critical financial services. Our licensing approach for digital banks reflects an entity-based approach, guided by our assessment of the underlying risks of the banking business.

We will also **intensify our focus on business continuity and resolution frameworks**. A more competitive and innovative market can mean dealing with greater unknowns and more dynamic changes in the financial landscape – which may include a higher turnover of entities within the financial services industry. Our objective will be to ensure that financial services activities can be unwound in an orderly fashion without adversely affecting system-wide stability, while safeguarding consumer outcomes. At the same time, we will also focus on strengthening the credibility of financial institutions' business continuity plans to ensure that they adequately reflect changing operational configurations as well as increasing interdependencies on third parties and shared infrastructures.

- We will **continuously develop and refine our regulatory guidance on critical digital enablers** – such as the use of cloud, AI and ML. The focus will be to better align expectations among industry players to ensure the sound management of risks and fair treatment of consumers. We will also seek to address undue regulatory frictions or inefficiencies, if any – including in our supervisory processes – to support greater agility by financial institutions in adopting these technologies (refer to the box article "Medium-term priorities for the prudential framework and AML/CFT").

³ Activity-based rules consist of requirements to be met by any institution offering a given service (e.g. lending, payment services). Entity-based rules consist of requirements imposed on institutions with a specific licence or charter, which in turn sets out the activities those entities are allowed to undertake.



We will also seek to address undue regulatory frictions relating to the use of critical digital enablers, such as cloud technologies and AI/ML

- We will **enhance inter-agency cooperation to better oversee emerging non-bank business models**, focusing on two areas:
 - Economic sectors that are increasingly linked to financial services (such as telecommunications and e-commerce); and
 - Regulatory mandates that are closely intertwined with monetary and financial stability within the sphere of digital finance – particularly competition, data protection, and privacy.

This approach reflects the growing prevalence of digital financial ecosystems (e.g. emergence of digital lenders, cross-selling of financial products by e-wallet operators, potential partnerships between banks or insurers with other technology-based service providers).

In enhancing these arrangements, our priorities will be to support the timely identification, monitoring, and mitigation of risks in the overall financial value chain to financial stability and consumer outcomes. Given the potentially rapid pace at which digital models may scale, we will also work closely with the relevant authorities on timely information-sharing and intervention arrangements.

Strategy 3C

Strengthen cyber security readiness and responsiveness

Malaysia's financial sector is increasingly part of a broader network of digital relationships – with third party service providers (TPSPs), other financial institutions, and devices. As cross-border and global supply chain linkages deepen, so will new interdependencies and potential blind spots. In these networks, each of the nodes is a possible target. Unlike most operational risks, cyber security breaches in one node can quickly propagate to others in a short period. The cyber security strength of any single 'node' or institution is therefore only as strong as the weakest link in that network.

With the continued digitalisation of financial services in Malaysia, cyber security is arguably one of the biggest risks. The same digital ecosystems that accelerate innovation – and all its upsides to consumers and businesses – also bring risks and vulnerabilities for the financial sector. These include operational disruptions, data breaches, fraud, and financial losses. If not managed well, these can have severe consequences for financial and monetary stability, as well as the broader economy.

Importantly, the cyber security threat landscape is highly complex, shaped by a range of factors (see Diagram 6). The tools of cyber criminals are also constantly evolving, becoming easier and more inexpensive by the day. The threat is borderless, and

increasingly more coordinated and sophisticated. Such factors compound the challenge of putting in place reliable safeguards.

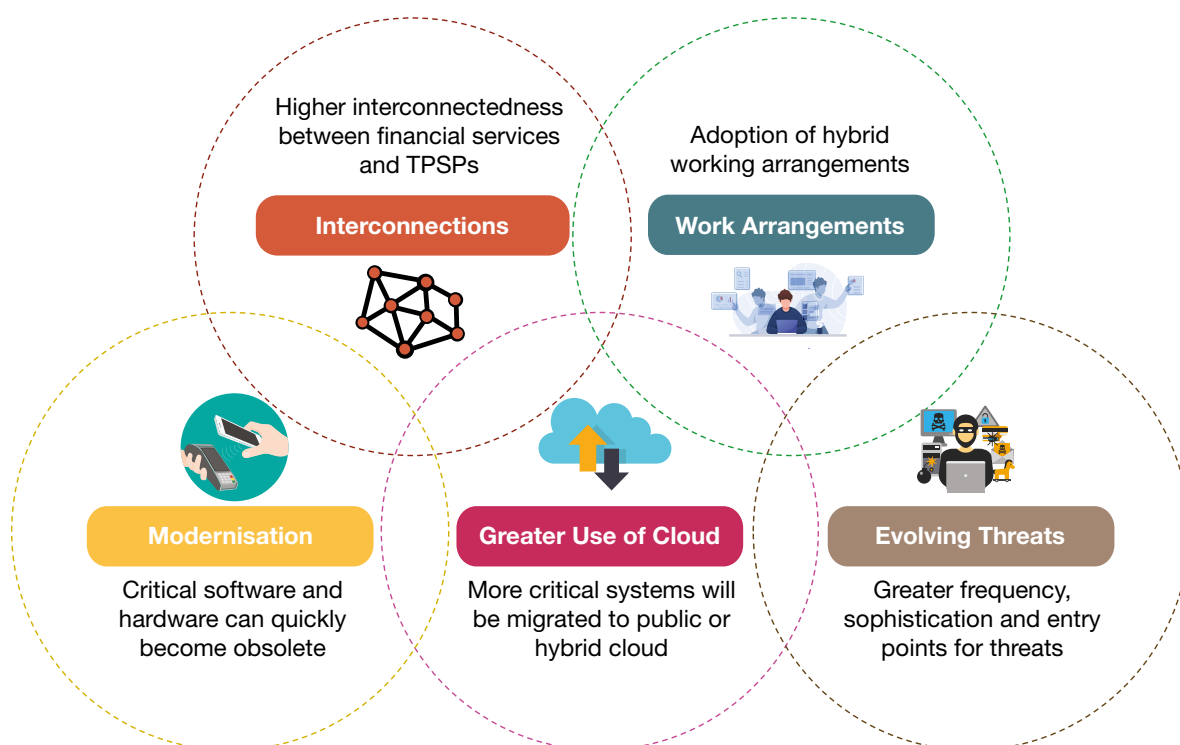
Against this backdrop, a financial system with strong cyber security fundamentals will continue to be a critical priority of the Bank, in turn providing a solid foundation for innovation to thrive.

Given the characteristics of cyber risk, our strategies are centred around readiness and responsiveness. While reducing the probability of cyber attacks remains an important objective, we will intensify efforts to mitigate the impact of such attacks. We will also strengthen collaborative arrangements – among authorities and industry players, domestically and internationally. These efforts will aim to develop holistic defences against cyber security risks to the financial sector, including those from telecommunications infrastructure and potentially critical TPSPs such as cloud operators.

We will seek to advance the following strategies:

- i. Strengthen system-wide cyber security oversight and capabilities; and
- ii. Strengthen domestic and global collaborative efforts on cyber security.

Diagram 6:
Key factors shaping the cyber security landscape



i Strengthen system-wide cyber security oversight and capabilities

- We will **continuously strengthen our oversight of cyber security risks, with an increased focus on the broader financial ecosystem**. This entails:

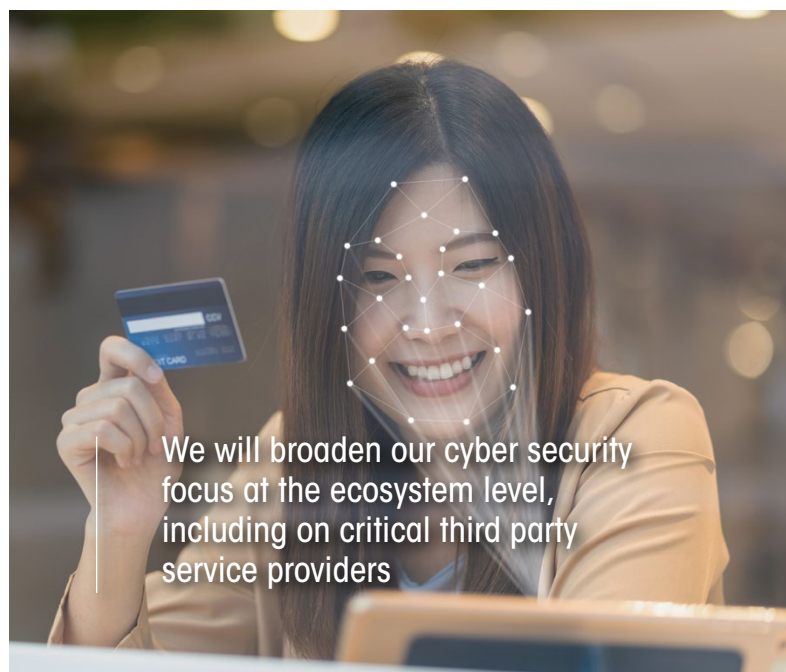
- **Ensuring that the financial industry adheres to a strong set of minimum standards** on cyber risk governance and management.
- **Intensifying our focus on cyber security issues arising from critical TPSPs**. This will entail assessing the adequacy of existing policies in managing TPSP risks and where necessary, developing additional frameworks to better protect the financial ecosystem throughout its entire value chain.

Further, we will consider the need for strengthened oversight arrangements to take into account interactions between the financial sector and TPSPs that can give rise to systemic risks. These include expanding the regulatory perimeter given the increasing interdependence with TPSPs. We will consult with key industry players, including critical TPSPs to develop possible approaches for securing the financial system's technology linkages with third party providers.

We will also consider integrating TPSPs as part of intelligence-sharing arrangements established in the financial sector (as set out below).

- We will **intensify sharing of actionable cyber security intelligence** by:

- Further **developing our capacity to construct and maintain comprehensive cyber contagion maps of the financial industry**. The aim will be to identify, on a continuing basis, vulnerable points, potential concentration risks and interconnections in the financial sector arising from technological infrastructures and services that are being used by financial institutions. These contagion maps are expected to provide a more granular view of how the shock from a cyber incident could spread throughout the financial ecosystem, including its magnitude and impact.



We will broaden our cyber security focus at the ecosystem level, including on critical third party service providers

This will in turn guide our supervisory assessments of financial institutions, support better informed business decisions by the financial sector to manage potential risk concentration of TPSPs or related services, as well as focus our efforts at the national level to better safeguard critical infrastructures.

- **Expanding the scope and coverage of ongoing resilience measures**. This includes the implementation of the cyber resilience maturity assessment (CRMA) framework, cyber drill exercises with other stakeholders and the Government, and the recently established Financial Sector Cyber Threat Intelligence Platform (FinTIP). Across these initiatives, we will aim to involve a greater range of stakeholders and industry players in the financial sector value chain. These initiatives are expected to enrich our collective understanding and improve the ecosystem-wide ability to proactively mitigate cyber risks.



Cyber security is a shared responsibility

ii Strengthen domestic and global collaborative efforts on cyber security

- We will continue to **support nationwide efforts in strengthening digital literacy and cyber hygiene practices** of financial consumers. With wider adoption of digital financial services, basic cyber hygiene practices will be crucial to protect consumers from threats such as online scams, financial fraud and identity theft. To this end, we will support and work with industry associations, law enforcement agencies and relevant government agencies to increase cyber security awareness among consumers so that they can effectively protect their data and digital devices.
 - We will **advocate for greater standardisation in cyber security and cyber resilience terminology** at the national level. With a common language among all relevant stakeholders, ecosystem-wide efforts to safeguard and strengthen cyber security – whether to share information or to coordinate interventions – can be pursued more effectively.
- In our advocacy efforts, we will aim to leverage on widely accepted practices. This would consider global efforts such as those of the FSB’s Cyber Lexicon, ISO, as well as domestic policies of various agencies such as National Cyber Security Agency Malaysia (NACSA), CyberSecurity Malaysia (CSM), Malaysian Communications and Multimedia Commission (MCMC), National Institute of Standards and Technology (NIST) and others.
- We will **facilitate initiatives to deliver specialised cyber security training and certification** that promote skills development and competencies in the financial industry. In doing so, we will work together with relevant government agencies and industry associations – such as MDEC, CSM, NACSA, and *Persatuan Penguji Keselamatan Siber (PPKS)* – to collect, compare, and assess data to design a clear roadmap to deepen Malaysia’s cyber security talent pool.

Strategy 3D

Support greater use of technology for regulation and supervision

We are also committed to ensure that we leverage digital technologies to continuously improve our effectiveness and efficiency – particularly, as a financial regulator and supervisor. This will complement the financial industry’s shift towards greater digitalisation.

A key consideration in our way forward would be to enhance how we create, collect, capture, synthesise and share data – aiming to improve the efficiency, integrity, and security of the ecosystem. This reflects the growing importance of data for a range of functions, from the surveillance of risks and vulnerabilities to facilitating efficient ways to comply with regulatory policies and requirements. As future enhancements will affect existing infrastructures, systems, and processes, we will ensure that the path forward is collaboratively mapped out, together with industry players and other regulatory authorities.

As part of this effort, we will seek to advance the following:

- i. Leverage technology to further strengthen the Bank’s regulation and supervision of the financial industry; and
- ii. Futureproof the Bank’s data strategy.

i Leverage technology to further strengthen the Bank's regulation and supervision of the financial industry

- We will aim to continuously strengthen our application of technologies – such as AI, ML, natural language processing, and automation – to deliver **process improvements** in our regulatory and supervisory functions. This will include:
 - Greater **integration of our risk analytics engines** to support more holistic surveillance across different datasets – and with it, explore further enhancements in the way we conduct our oversight activities. In particular, this is expected to enhance risk-based supervision, by providing richer insights in identifying and sizing up risks to financial institutions – and in turn, enabling more timely and targeted interventions.
 - **Streamlining and facilitating more efficient regulatory and compliance processes.** This includes providing a single, technology-supported applications and submissions interface, with monitoring capabilities, for all authorised financial institutions with the Bank.

ii Futureproof the Bank's data strategy

We aim to reform our data arrangements, including through the use of APIs and Open Data initiatives




- We will initiate a **comprehensive industry review on the financial data ecosystem**, which includes the submission, processing and usage of regulatory reporting and statistical submissions to the Bank. In the next five to ten years, we will focus on improving the timeliness, quality, granularity, and transparency of the data that we collect from the industry. This will be done through the implementation of a new data collection and sharing arrangement between the Bank, the financial industry and other partner institutions.
 - **Quality and timeliness.** We will work with the industry to gradually phase out manual or semi-automated data submissions and quality control processes, and explore the use of APIs to improve the overall data preparation and submission processes. This will reduce compliance costs for financial institutions and improve the Bank's regulatory and supervisory efficiency.
 - **Granularity.** We will increasingly leverage the use of geospatial and other technologies to continuously enhance the granularity of data – and in turn, drive better insights for our analysis and decision-making. This will build on efforts so far, such as pilot initiatives that we have pursued since the onset of the pandemic – where we collect more granular payments and financial inclusion data from selected financial institutions, on a near real-time basis. We will continue to expand the scope of such pilots to include other data sets, such as household and business data, climate-related exposures, and green financing data.
 - **Transparency.** We will continue to enhance public access and portability of the Bank's various financial and economic data sets that do not reveal any commercially sensitive information. This can play a role in catalysing the broader data community – such as through Open Data initiatives – to develop new insights and identify collaboration opportunities, including with the Bank. Where possible, we will also explore the development of dashboarding capabilities, leveraging on industry data reported to the Bank, for financial institutions to anonymously benchmark their risk profiles and practices relative to peers.

Box Article

Digital currencies: A new frontier

Over the past decade, rapid technological innovation and the increasing pace of digitalisation have transformed the payment landscape in Malaysia. Digital payment adoption has accelerated, alongside a more diverse landscape of payment service providers. More recently, digital currencies are gaining traction – typically leveraging on tokenisation and DLT to facilitate P2P transfers without the need for intermediaries (Diagram 1). Central banks are also experimenting with central bank digital currencies (CBDC) – a new form of central bank money that represents a direct liability of the central bank.

Diagram 1:
Comparison of CBDC, stablecoins and non-backed digital assets

	Issued by a sovereign body	Issued by private entities	
	 <p>Central Bank Digital Currencies (CBDC)</p> <ol style="list-style-type: none"> Wholesale CBDC: issued to facilitate settlement between financial institutions Retail CBDC: issued for use by the general public (households and businesses) to facilitate day-to-day transactions 	 <p>Stablecoins (digital assets with value stabilisation mechanism)</p> <ol style="list-style-type: none"> Fiat-backed: value is backed by fiat currency (e.g. Tether) Asset-backed: value is backed by assets such as commodities or crypto-assets (e.g. Dai) Algorithm-based: value is supported by protocols that adjust supply in response to changes in demand (e.g. Terra) 	 <p>Non-backed Digital Assets</p> <ol style="list-style-type: none"> Exchange tokens: used as a means of exchange or for investment (e.g. Bitcoin, Ethereum) Security tokens: may provide rights (e.g. ownership, repayment of a sum of money, or entitlement to future profits) Utility tokens: can be redeemed for access to a specific product or service
Store of value	Value is backed by a sovereign body (e.g. Government, central bank)	Value is backed by assets or is stabilised by controlling the market supply of the stablecoin	No formal backing for its value i.e. subject to market forces
Medium of exchange	Likely to be widely used as a means of payment given that it is a digital representation of fiat currency	May potentially be used as a means of payment subject to effectiveness of value stabilisation mechanism	Not likely to be widely used as a means of payment due to various limitations (e.g. price volatility)
Unit of account	Denominated in fiat currency	May be denominated in fiat currency (for stablecoin backed by fiat currency)	Has its own unit of account

Developments in this space can spur greater efficiency, inclusion, and vibrancy in the payments and financial landscape. Increased competition in the retail payment space may result in lower cost, wider access, and better services. Applications of emerging technologies – such as CBDC, stablecoins, and the broader DLT infrastructure – may also help address longstanding pain points, particularly those in cross-border payments (e.g. high costs, low speed, limited access, and insufficient transparency)¹.

¹ Source: Financial Stability Board (2020), “Enhancing Cross-Border Payments: Stage 1 Assessment Report to the G20”.

CBDC in particular can also serve as a tool to achieve public policy goals, including by advancing financial inclusion, strengthening monetary policy transmission² as well as promoting innovation in payment services. Leveraging its programmable features³, CBDC may also spur other innovations in the way financial transactions are conducted through the use of smart contracts.

While these developments may offer some opportunities to Malaysia, there are attendant risks that need to be managed. Depending on the way it is designed, CBDC issuance may impact monetary policy operations, and amplify operational and cyber risks to the Bank. It may also trigger financial stability risks if there is a significant shift of bank deposits to CBDC.

Likewise, cross-border usage of foreign-currency denominated CBDC (foreign CBDC) and stablecoins may have spillover effects to Malaysia. For instance, widespread adoption of foreign CBDC and stablecoins for payments in Malaysia may heighten currency substitution risk, which may in turn undermine monetary stability. In addition, foreign CBDC and stablecoins may amplify capital flow volatility risk. In times of stress, there may be financial stability implications if there is a flight to foreign CBDC and stablecoins, which may be perceived as a safer alternative store of value. Such risks may materialise if foreign CBDC and stablecoins bypass traditional intermediaries and controls through which foreign exchange measures and other regulatory requirements are typically enforced.

As emerging payment technologies evolve, it is vital for us to be in a state of readiness to capitalise on the opportunities, while mitigating the associated risks. Among others, this includes promoting interoperability between CBDC platforms and existing payment infrastructures to facilitate seamless payment flows, ensuring parity and proportionality to support innovation, and establishing the necessary safeguards, where required.

Keeping in mind these trade-offs, we will adopt a two-pronged strategy:

One, focus on building internal capacity to support informed decisions on CBDC issuance

At the time of this Blueprint's publication, we do not have any immediate plans to issue CBDC. In Malaysia, the financial system continues to support the functioning of the economy, while the existing monetary and financial policy tools continue to be effective in safeguarding monetary and financial stability. Moreover, domestic payment systems – including the RPP – continue to be safe and highly efficient to support the needs of individuals and businesses, and facilitate migration to digital payments.

Nevertheless, we recognise the importance to be proactive in scaling up our internal understanding and capacity on CBDC. This would have two key benefits:

- Greater clarity on the use cases that offer higher upsides for Malaysia, the potential risks and implications to monetary and financial stability arising from CBDC issuance, as well as the appropriate CBDC design and controls to ensure the risks are adequately mitigated; and
- Adequate technical understanding and capacity to build and operate a CBDC platform, should the need to implement one arise in the future.

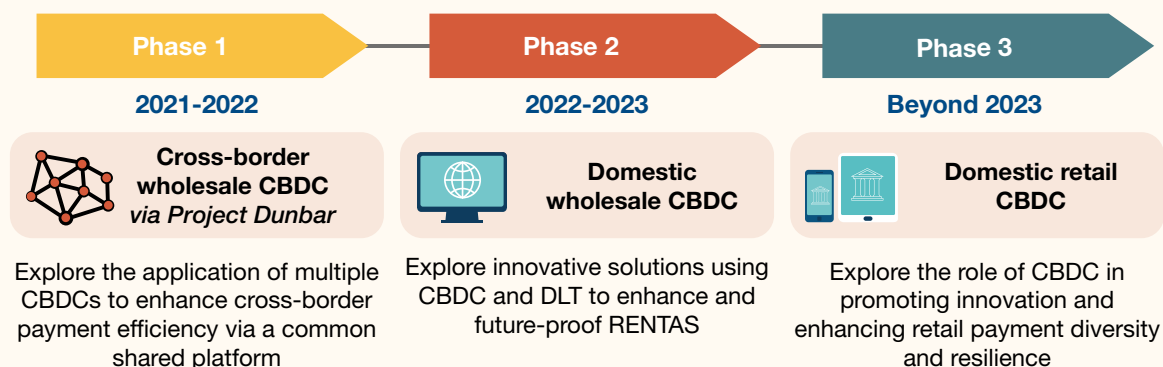
To this end, we have commenced a multi-year CBDC exploration through a POC with three phases (Diagram 2). The POC aims to explore the potential of CBDC to address key problem statements by prioritising use cases that would offer the higher upsides for Malaysia. This will be done collaboratively with the relevant stakeholders, including to facilitate interested industry players to participate in the POC.

² For example, an interest-bearing CBDC may strengthen the monetary policy transmission mechanism.

³ CBDC may be programmed with business logic (e.g. by allowing it to be spent upon fulfilment of certain conditions).

Diagram 2: Malaysia's CBDC proof-of-concept roadmap

A multi-year exploration to assess the potential of CBDC to address gaps in the financial sector and achieve public policy objectives



- Phase 1 (Cross-border wholesale CBDC):** We see the potential of CBDC in addressing the longstanding frictions in cross-border payment arrangements such as low speed, high cost, limited access, and insufficient transparency. By enabling instant settlement, CBDC has the potential to reduce the number of intermediaries and mitigate the need to pre-fund multiple correspondent banking accounts, thus resulting in faster and cheaper cross-border payments. As a highly open economy with trade-to-GDP ratio averaging over 130% since 2010⁴, any improvement in the efficiency of cross-border payments has the potential to create substantial cost savings and productivity gains, thereby strengthening Malaysia's trade competitiveness. In this regard, we have collaborated with the BIS Innovation Hub, Reserve Bank of Australia, Monetary Authority of Singapore, and South African Reserve Bank to test the use of wholesale CBDC for international settlements via a shared platform through Project Dunbar (Diagram 3). The POC, which commenced in September 2021, is envisaged to be completed by March 2022. The interim findings of Project Dunbar have been published on the BIS portal.

Diagram 3: Overview of Project Dunbar



⁴ Source: World Bank

- **Phase 2 (Domestic wholesale CBDC):** This POC will provide us with an opportunity to reimagine and future-proof our domestic wholesale payment system, RENTAS. While RENTAS has been operating at high levels of availability, efficiency and resilience, the application of wholesale CBDC and DLT has the potential to elevate the domestic wholesale payment system to the next level. Some of the potential benefits include reducing the single point of failure risk, enhancing the efficiency of liquidity management, simplifying compliance processes, and enabling new use cases such as the settlement of tokenised assets.
- **Phase 3 (Domestic retail CBDC):** Although we already have an efficient real-time retail payment system – namely, the RPP – we see the potential of retail CBDC in complementing the RPP and serving as a catalyst to spur greater innovation in the financial sector. Besides enhancing payment diversity and resilience, CBDC may introduce a smarter version of central bank money which could support new use cases through its programmable features. By designing it with public interests in mind, an open and flexible CBDC platform may serve as a shared infrastructure upon which private sector innovation may flourish. For instance, CBDC can be programmed to streamline compliance processes and facilitate automatic payment to beneficiaries upon meeting certain pre-defined conditions. Some examples include automated coupon payment upon bond maturity, automatic routing of tax payments to the authorities at point of sale⁵ and automated settlement of vehicle or real estate purchase upon confirmation of the transfer of legal title. Besides lowering transaction costs, this has the potential to mitigate counterparty risk and thereby enhancing financial stability.

Two, evaluate implications of the broader digital currency ecosystem to monetary and financial stability and develop appropriate policy responses

Irrespective of our decision on the issuance of CBDC, the developments in the broader digital currency space, particularly foreign CBDC, stablecoins, and other digital assets, may pose other challenges and risks – some of which were highlighted at the onset of this article.

Beyond assessing the opportunities and risks associated with CBDC issuance by the Bank via the CBDC POC, we will also undertake a holistic assessment of the implications of foreign CBDC, stablecoins, and other digital assets to monetary and financial stability, with the aim to develop appropriate policy responses and strategies. This may include:

- Assessment on implications to monetary policy transmission, financial intermediation, capital flow management, and financial integrity;
- Development of an effective surveillance framework; and
- Strengthening regulatory and supervisory frameworks to mitigate risks without stifling innovation. This may include developing the appropriate regulatory approach to stablecoins and establishing the prudential treatment for digital assets in the financial sector.

Through our involvement in various international fora, we will continue to advocate for international collaboration in developing relevant rules and standards to facilitate interoperability, enhance cooperative oversight, and promote responsible innovation in the digital currency space to mitigate any negative spillovers.

⁵ Source: Bank for International Settlements (2021), “Central Bank Digital Currencies: User Needs and Adoption”.

Being prepared together

In the next five years, we believe that digital currencies will continue to shape the landscape of payment infrastructures. In particular, CBDC – which would be built with public interests in mind – could have the potential to serve as an important infrastructure upon which private sector players may innovate to promote a more efficient, inclusive, and vibrant financial landscape.

While the reach and magnitude of digital currencies' impact remain to be seen, early exploratory efforts will be key to ensure that the financial sector can adapt effectively. We are committed to advancing these efforts for Malaysia, as set out in our two-pronged approach above. Given the complexity and pace of these developments, we welcome and will continue to support broader collaborative efforts in our journey. This includes international cooperation efforts to advance the principles of responsible innovation in the digital currency space, as well as strong public-private collaboration to ensure CBDC infrastructures are well-designed in addressing current pain points and meeting the emerging needs of the economy.



Strategic Thrust 4

Position the financial system to facilitate an orderly transition to a greener economy

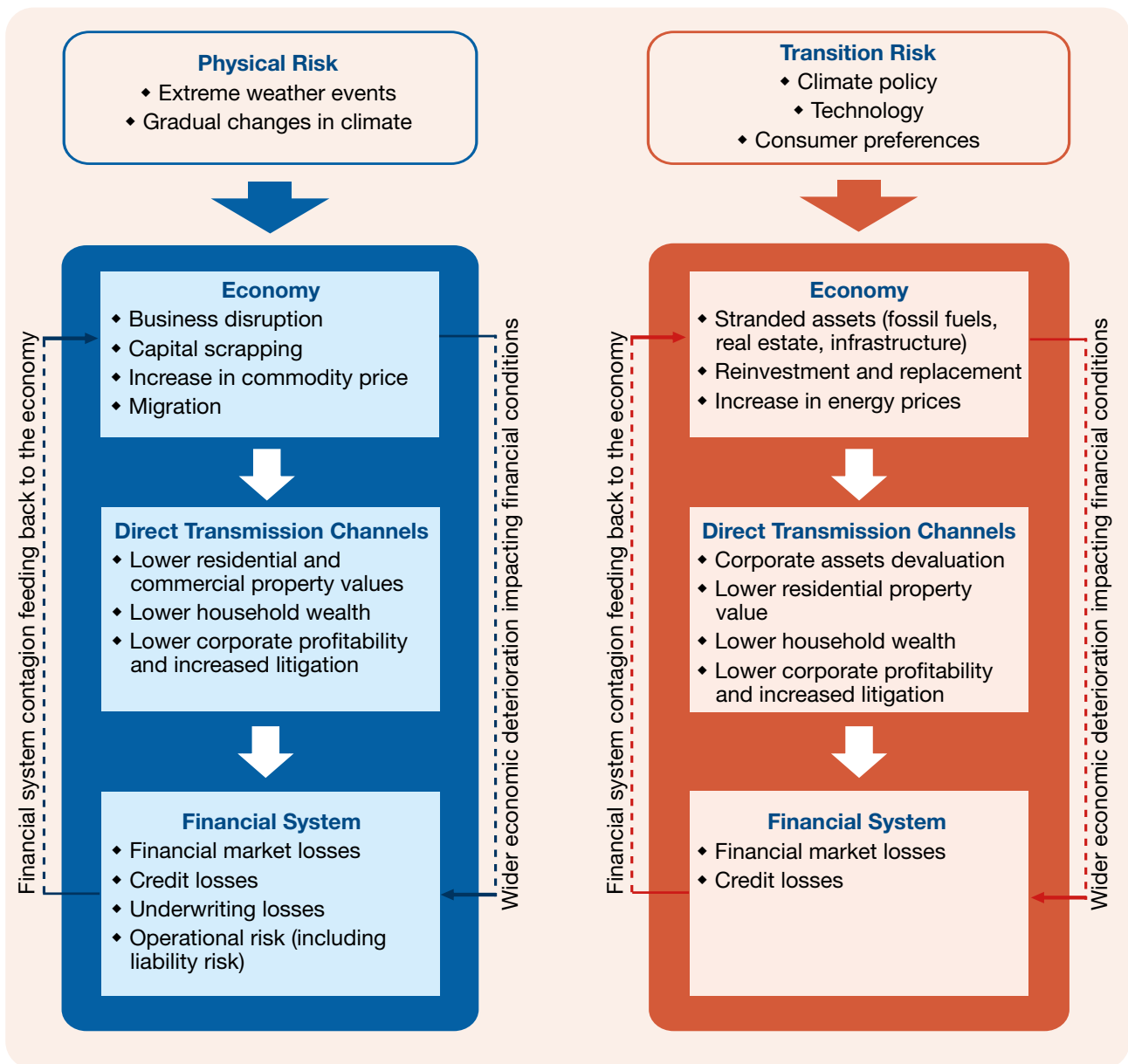
Climate change and environmental degradation pose unprecedented challenges and opportunities that will reshape the economic and financial landscape. These include:

- **Physical risk.** Extreme weather events and gradual shifts in the climate can damage property and disrupt business activity. Beyond putting livelihoods – and in extreme cases, lives – at risk, such developments also increase financial risk to financial institutions as the creditworthiness of materially affected borrowers deteriorate. In addition, this would lead to a higher cost of financial protection or the potential reduction in insurance and takaful capacity. Physical risk also impacts investment and collateral values, where assets can be destroyed or significantly damaged by climate or environment events.
- **Transition risk.** The adjustment to a low-carbon economy may entail changes to public policies, legislative and regulatory frameworks, technologies or societal responses – with possible consequences on the economy and financial sector. Globally, the pace of such adjustments is intensifying, with a growing list of nations and large organisations that have made carbon neutral or net-zero emissions commitments. Policies to promote a circular economy¹ are also gaining momentum, further contributing to changes aligned with environmental outcomes and longer-term socioeconomic prosperity. Shifts in consumer and investor expectations, regulatory pressure as well as technological advancements present risks to businesses. As an export-oriented economy, Malaysia will be directly affected by the transition efforts by major trading partners. A late or abrupt transition to these new trends could leave exposed businesses with stranded assets that experience an unexpected drop in value due to diminishing demand or regulatory restrictions. For financial institutions exposed to such businesses, these changes may translate into financial and reputational risks that could negatively impact their balance sheets and bottom lines.
- **Fiscal spillovers.** Beyond the losses to the economy and private finance, the materialisation of physical and transition risks will also have cascading effects to public finances. In addition to the Government's direct exposures, there is also the risk of spillovers such as through reduced tax revenue, higher sovereign spreads and substantial fiscal spending in the aftermath of a natural disaster.
- **Liability risk.** Governments, corporations as well as company directors and officers may also face higher prospects of legal action for failures to adequately address climate-related and environmental risks. Other than the cost of liability from successful lawsuits, such litigation can have a significant reputational impact on affected stakeholders. These risks may affect financial institutions that have extended liability protection, financing or investment to affected companies.



¹ A circular economy is an industrial system that is restorative or regenerative by intention and design. The idea is to gradually decouple economic activity from the unsustainable consumption of finite resources – and in turn, shift to systems designed to remove waste and pollution, keep products and materials in use and regenerate natural systems. Source: World Economic Forum (2014), "Towards the Circular Economy: Accelerating the Scale-up Across Global Supply Chains"; Ellen MacArthur Foundation (2020), "Financing the Circular Economy: Capturing the Opportunity".

Diagram 1:
Transmission of climate risk to the economy and financial system



Source: Network for Greening the Financial System (2020), "Guide for Supervisors: Integrating Climate-related and Environmental Risks into Prudential Supervision".

Against this backdrop, our primary focus will be to **promote financial system resilience** by continuing our efforts to improve climate-related and environmental risk management in the financial sector.

We will also seek to foster a **conducive market environment** for green financing and investment. Significant and concrete action is required to support an orderly transition by Malaysian households and businesses, and capitalise on opportunities from shifts to a low-carbon and sustainable economy. At this point, efforts needed to address climate-related and environmental risks – such as reskilling, the application of new technology, infrastructure upgrades, and the preservation of natural ecosystems – remain underfunded. In this regard, we will work to align legal and regulatory frameworks where appropriate², and

support mechanisms to mobilise mainstream finance in supporting the country's transition to a greener economy.

Given its central role in allocating and deploying economic resources, the financial sector can be the catalyst in encouraging players in the Malaysian economy to adopt more sustainable practices. At the same time, this should promote a **just and orderly transition** – that is, one which reinforces early and sustained actions to address climate change and environmental concerns, while adequately supporting affected communities to make the adjustments needed and ameliorate short-term impacts.

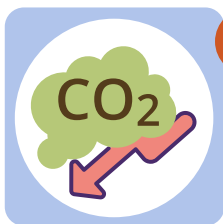
To achieve these goals, we will advance the following strategies (see Diagram 2 for an overview).

Diagram 2:
Position the financial system to facilitate an orderly transition to a greener economy



A Integrate climate-related and environmental risks in prudential regulation and supervision

- ◆ Ensure effective implementation of the Climate Change and Principle-based Taxonomy (CCPT) to facilitate the assessment of climate-related risks and encourage financial flows towards environmentally sustainable economic activities
- ◆ Align the prudential and supervisory framework to incorporate climate and environmental risk considerations
- ◆ Strengthen practices in the disclosure of climate risk by financial institutions



B Support orderly transition to a low-carbon economy

- ◆ Improve availability, access, and use of data for tackling climate change and environmental degradation
- ◆ Scale up green finance for a more sustainable Malaysia
- ◆ Collaborate with government agencies to align the financial sector's response with the national strategy towards achieving carbon neutral and net-zero targets
- ◆ Represent emerging market perspectives on sustainable finance developments and challenges



C Integrate climate risks in the Bank's internal functions and operations

- ◆ Enrich the scope of our macroeconomic and financial stability assessments to include climate and sustainability effects
- ◆ Manage our financial assets with greater consideration to climate and environmental risk
- ◆ Run our physical operations more sustainably

² Consistent with the Bank's mandate to promote a sound, progressive and inclusive financial system under section 5 of the Central Bank of Malaysia Act 2009.

Strategy 4A

Integrate climate-related and environmental risks in prudential regulation and supervision

Our efforts will be centred on aligning the financial sector regulatory and supervisory framework to account for climate-related as well as environmental physical and transition risks. This will build on a common framework for identifying and capturing climate-related and environmental risks across the financial sector to support risk assessments and disclosures.

To this end, we will continue the work of the Joint Committee on Climate Change (JC3)³ to advance the following outcomes for the financial sector:

- i. Ensure effective implementation of the Climate Change and Principle-based Taxonomy (CCPT)⁴ to facilitate the assessment of climate-related risks and encourage financial flows towards environmentally sustainable economic activities;
- ii. Align the prudential and supervisory framework to incorporate climate and environmental risk considerations; and
- iii. Strengthen practices in the disclosure of climate risk by financial institutions.



i Ensure effective implementation of the CCPT to facilitate the assessment of climate-related risks and encourage financial flows towards environmentally sustainable economic activities

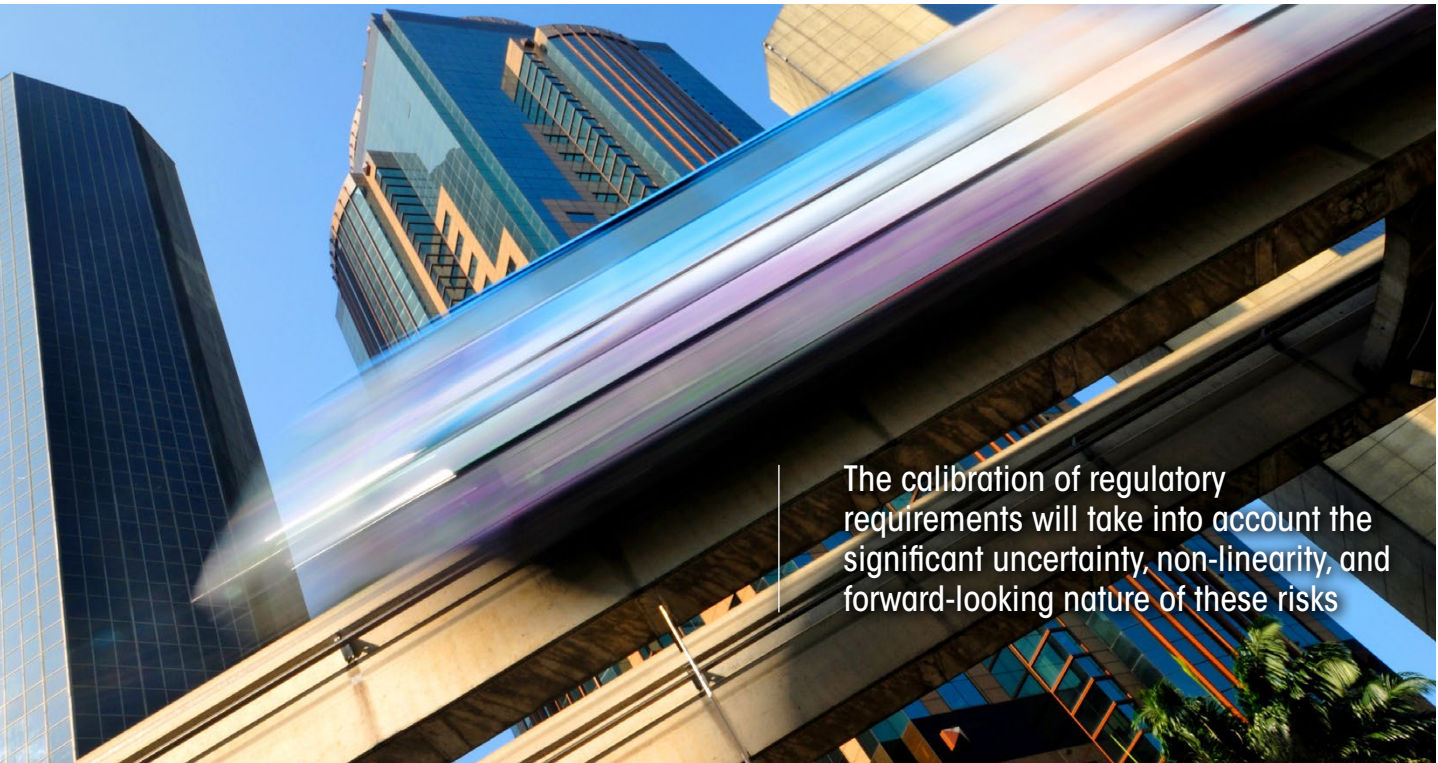
- With the issuance of the CCPT in April 2021, our focus will be to work with the industry through the CCPT Implementation Group under the JC3 to **ensure that the taxonomy is implemented in a consistent and credible manner**. This would include enriching the repository of use cases to guide financial institutions in applying the CCPT.
- In addition to identifying and addressing implementation issues, we will work to **promote further integration and alignment with the Value-based Intermediation Assessment Framework (VBIAF) and its sectoral guides**, which provide

sector-specific⁵ toolkits for financial institutions to incorporate environmental, social and governance (ESG) risk considerations in their financing and investment decisions. Beyond this, we will also actively pursue broader efforts to promote comparability, alignment and interoperability with ESG-related taxonomies over time – such as the SC’s Sustainable and Responsible Investment taxonomy, the ASEAN Taxonomy for Sustainable Finance and others adopted at the global level, where appropriate. This will be important to spur external financing and foreign investments in mitigation and adaptation efforts.

³ The JC3 is a platform to pursue collaborative action for building climate resilience within the Malaysian financial sector. It is co-chaired by the Bank and the SC, with members comprising senior leaders from Bursa Malaysia, the financial industry and relevant subject matter experts. The JC3 comprises five sub-committees: Risk Management; Governance and Disclosure; Product and Innovation; Engagement and Capacity Building; and Bridging Data Gaps.

⁴ The CCPT guidance document was issued on 30 April 2021 to provide a common language for financial institutions to classify and report on climate-related exposures. Further details are accessible at <https://www.bnm.gov.my/documents/20124/938039/Climate+Change+and+Principle-based+Taxonomy.pdf>

⁵ To date, sectoral guides have been issued for the following six activities/sectors: Palm Oil; Renewable Energy; Energy Efficiency; Oil and Gas; Construction and Infrastructure; and Manufacturing.



The calibration of regulatory requirements will take into account the significant uncertainty, non-linearity, and forward-looking nature of these risks

ii Align the prudential and supervisory framework to incorporate climate and environmental risk considerations

- We will **strengthen our supervisory expectations for financial institutions to identify, measure, monitor, and manage exposures to climate-related and environmental risks**. This will include setting expectations for financial institutions to align business and risk strategies, with their sustainability commitments (such as net-zero milestones and green financing targets) and properly oversee transition plans.
- We will **review the existing prudential framework to align expectations for financial institutions to increase their resilience to climate and environmental risks**. This will include the consideration of relevant adjustments to prudential requirements (e.g. capital risk weights, the internal capital adequacy assessment process, counterparty exposure limits, and the treatment of collateral), where appropriate.

We will work with the industry and wider stakeholders to collect data and conduct research to inform any adjustments to the prudential framework. The calibration of regulatory requirements will consider the unique characteristics of such risks, including their significant uncertainty, non-linearity, and forward-looking nature. Supervisory judgment will therefore play an important role.
- We will also pay close attention to ensure that safeguards are in place to mitigate against greenwashing. Additionally, the regulatory framework will reflect the critical role and expectations for financial institutions to support transition activities. To this end, we will seek to ensure that financial institutions consider the needs of customers most vulnerable to physical and transition risks and support their efforts to adapt.
- We will also **continue to support industry efforts to expand the availability of intermediate and advanced technical programmes on climate-related risks** to strengthen the capabilities of financial sector professionals in the area of climate and environmental risk management. This includes partnering with subject matter experts from professional bodies and academic institutes, including International Centre for Education in Islamic Finance (INCEIF), Islamic Banking and Finance Institute Malaysia (IBFIM), the Asian Institute of Chartered Bankers (AICB), and the Asia School of Business (ASB), to develop structured training solutions relevant to the Malaysian context.





iii Strengthen practices in the disclosure of climate-related risks by financial institutions

■ We will **strengthen practices in the disclosure of climate-related risk exposures by financial institutions**. A clear roadmap will be announced for all financial institutions regulated by the Bank to make mandatory climate-related risk disclosures aligned with recommendations by the Task Force on Climate-related Financial Disclosures (TCFD). This aims to provide greater transparency to markets, sustain financial institutions' risk and business strategies that are aligned with climate considerations, and encourage cascading effects to also improve disclosures by the businesses that

they finance and invest in. Better quality disclosures will in turn facilitate financial flows to activities that support a more sustainable future.

The disclosure of climate-related risks is a critical step to address climate data gaps and accelerate the path to a net-zero emissions economy

Diagram 3:
Overview of the Task Force on Climate-related Financial Disclosures (TCFD)

Thematic areas	Recommended disclosures	Principles for effective disclosure
 Governance	<ul style="list-style-type: none"> Board's oversight of climate risks and opportunities Management's role in assessing and managing climate risks and opportunities 	<ul style="list-style-type: none"> Represent relevant information Specific and complete Clear, balanced and understandable Consistent over time Comparable among companies within a sector industry Reliable, verifiable and objective Provided on a timely basis
 Strategy	<ul style="list-style-type: none"> Impact of climate risks and opportunities on the organisation's businesses, strategy and financial planning Resilience of the organisation's strategy, taking into consideration different climate-related scenarios 	
 Risk management	<ul style="list-style-type: none"> Organisation's processes for identifying, assessing and managing climate risks Integration of climate risks into the overall risk management 	
 Metrics and targets	<ul style="list-style-type: none"> Metrics used to assess climate risks and opportunities in line with strategy and risk management processes Greenhouse gas emissions Targets used to manage climate risks and opportunities, and performance against targets 	

Source: TCFD (2017), "Final Report: Recommendations of the Task Force on Climate-related Financial Disclosures".

Strategy 4B

Support orderly transition to a low-carbon economy

Environmental challenges – including climate change – are highly complex. Addressing them effectively requires concerted efforts across a wide range of stakeholders, often beyond national borders, and on a sustained basis.

The financial sector has a significant role to play in this regard. The pathway to carbon neutral and ultimately net zero will require significant green investments and transition finance to be channelled towards initiatives that reduce Malaysia's carbon footprint (e.g. renewable energy solutions, rethinking transport, low-carbon cities), and improve climate resilience (e.g. safeguards against rising sea levels, extreme weather). Businesses will also need funding to pivot to new business models, recalibrate existing practices, and adopt new technology. In Malaysia, demand for green investment funds is expected to grow to RM76.2 billion by 2030⁶, and much more investment will be needed over the coming years to fund Malaysia's journey to net-zero emissions and broader sustainability transition. It is thus crucial that financial institutions urgently step up and mobilise capital to support the increasing demand for green and transition funds in the period ahead.

Meeting this need calls for a significant scaling up of both public and private sources of funding in a manner that takes full advantage of the growing global demand for meaningful and measurable green investment opportunities. In this regard, the implementation of the CCPT by financial institutions will play an important role to help channel funds to investible green projects.

To complement the role of financial institutions, strategies to enhance the landscape (set out in chapter "Fund Malaysia's economic transformation") will also give specific focus to addressing funding gaps for high priority green projects, where the risks – or opportunities – posed by climate change are particularly prominent for the Malaysian economy. This includes utilising a diverse array of financing instruments, such as alternative finance, to meet the various needs of green finance priorities.

Government policies will also need to work in tandem, to remove barriers or incentivise more sustainable economic models. A clear national policy will provide the foundations for a cohesive reform agenda by public sector agencies, regulators, businesses, civil society, and consumers alike. This will also need to be supported by capacity-building efforts to expand access to the necessary skills, knowledge, technologies and data to advance climate- and environment-related reforms.

We are committed to play our role as a central bank and financial regulator within this broader 'whole-of-government' and 'whole-of-society' endeavour. In particular, we will seek to advance the following:

- i. Improve availability, access, and use of data for tackling climate change and environmental degradation;
- ii. Scale up green finance for a more sustainable Malaysia;
- iii. Collaborate with government agencies to align the financial sector's response with the national strategy towards achieving carbon neutral and net-zero targets; and
- iv. Represent emerging market perspectives on sustainable finance developments and challenges.

⁶ Source: Ministry of Energy, Green Technology and Water Malaysia (2017), "Green Technology Master Plan Malaysia 2017-2030".

i Improve availability, access, and use of data for tackling climate change and environmental degradation

The availability and transparency of climate-related data in Malaysia is a prerequisite for effective risk management in the financial sector

■ We will **facilitate the application of advanced digital tools to address the needs of the financial sector for accurate, granular and location-specific data** to support climate risk mitigation and adaptation use cases. For instance, such a broad range of data can help:

- Anticipate physical risk incidents (e.g. droughts, floods) and resulting economic losses, and thus inform and reward adaptation efforts through lower insurance premiums / takaful contributions;

- Increase the speed of insurance and takaful claims, by tying pay-outs to predefined climate-related triggers (e.g. flooding exceeding a certain threshold) without the need to assess actual loss or damage to physical assets;
- Reliably track emissions to validate sustainability practices and address risks of greenwashing; and
- Remotely measure and verify carbon capture in rainforests to provide efficient assurance for voluntary carbon markets and emissions trading schemes.

■ We will work through the JC3 Sub-committee on Bridging Data Gaps to collaborate with government agencies, academic institutes, technology firms and other relevant players to **identify critical data needs and create open access to relevant data sources** to continuously improve the availability of data crucial to climate risk and business strategies.



We will develop specialised funding mechanisms for green finance and support efforts to develop carbon markets

ii Scale up green finance for a more sustainable Malaysian economy

■ We will **work with industry players such as Cagamas Berhad, CGC and the development financial institutions to further develop and expand specialised funding and risk mitigation mechanisms**, such as the Low Carbon Transition Facility (LCTF) and Green Technology Financing Scheme (GTFS). This will aim to encourage the scaling up of green finance, particularly for SMEs, through targeted credit enhancements and

protection, and access to lower-cost funding for climate supporting and transition activities. We will also support efforts to involve the financial sector in developing carbon markets – such as the domestic emissions trading scheme and voluntary carbon market – in order to promote better pricing of emissions externalities and increase capital flows to nature-based solutions such as rainforest conservation.

We will actively pursue collaborative strategies to align our sustainability agenda with the Government's policy and initiatives



iii Collaborate with government agencies to align the financial sector's response with the national strategy towards achieving carbon neutral and net-zero targets

- We will **continue to align our efforts with Malaysia's broader objective to advance sustainability, as outlined in the RMK12 and in accordance with the national strategy set by the Malaysia Climate Action Council (MyCAC).** Financial sector policies and initiatives, including those set out above to build financial sector resilience and foster a conducive environment for green financing and investment, will take into account the nation's commitments under the Paris Agreement and the introduction of climate change legislation that will formalise the nation's climate targets and timeline to achieve net-zero greenhouse gas emissions.
- To **promote synergy between national-level policies and financial sector initiatives**, we will also work closely with relevant stakeholders to encourage timely and coordinated action in high priority areas under the forthcoming Malaysia sustainable finance roadmap. Particular focus will be given to securing an orderly transition, strengthening physical risk adaptation, as well as promoting areas of competitive advantage.

iv Represent emerging market perspectives on sustainable finance developments and challenges

It is critical for global efforts to deliver equitable outcomes

- An inclusive global approach to fighting climate change is crucial to deliver equitable outcomes for all. With this in view, we will **continue to participate in international efforts to advance emerging market and ASEAN perspectives on sustainable finance.** Support for emerging economies to manage transition spillovers from the growing international momentum toward net zero (e.g. reduced market access and job losses due to changes in demand and regulations) will be particularly important, with many emerging economies also challenged by severe physical risks and striving to lift a significant portion of its population out of poverty. At the same time, many are home to highly valuable but under-priced natural capital with potential as global carbon sinks and biodiversity banks.
- Through the Bank's membership in the Network for Greening the Financial System (NGFS) and involvement in other international standard setting bodies and platforms, we will seek to **encourage meaningful cooperation to accelerate capacity building initiatives and inform global strategies and standards on climate risks and sustainable finance.**
- Within the region, we will **continue to work closely with the South East Asian Central Banks (SEACEN), the ASEAN Finance Ministers and Central Bank Governors, as well as other partners to tackle common issues faced in climate and environmental risk management.** This includes addressing data limitations across the region to support better risk surveillance and cooperating to further strengthen the regulatory and supervisory framework. We will also support broader efforts in the development of an ASEAN Green Map to promote a comprehensive and unified approach to addressing sustainability issues across banking, insurance, and capital markets in the region.

Strategy 4C

Integrate climate risks in the Bank’s internal functions and operations

Within our organisation, we are taking a holistic approach to integrate climate risk and sustainability considerations in delivering our mandate.

To this end, we will seek to advance the following:

- i. Enrich the scope of our macroeconomic and financial stability assessments to include climate and sustainability effects;
- ii. Manage our financial assets with greater consideration to climate and environmental risks; and
- iii. Run our physical operations more sustainably.

i Enrich the scope of our macroeconomic and financial stability assessments to include climate and sustainability effects

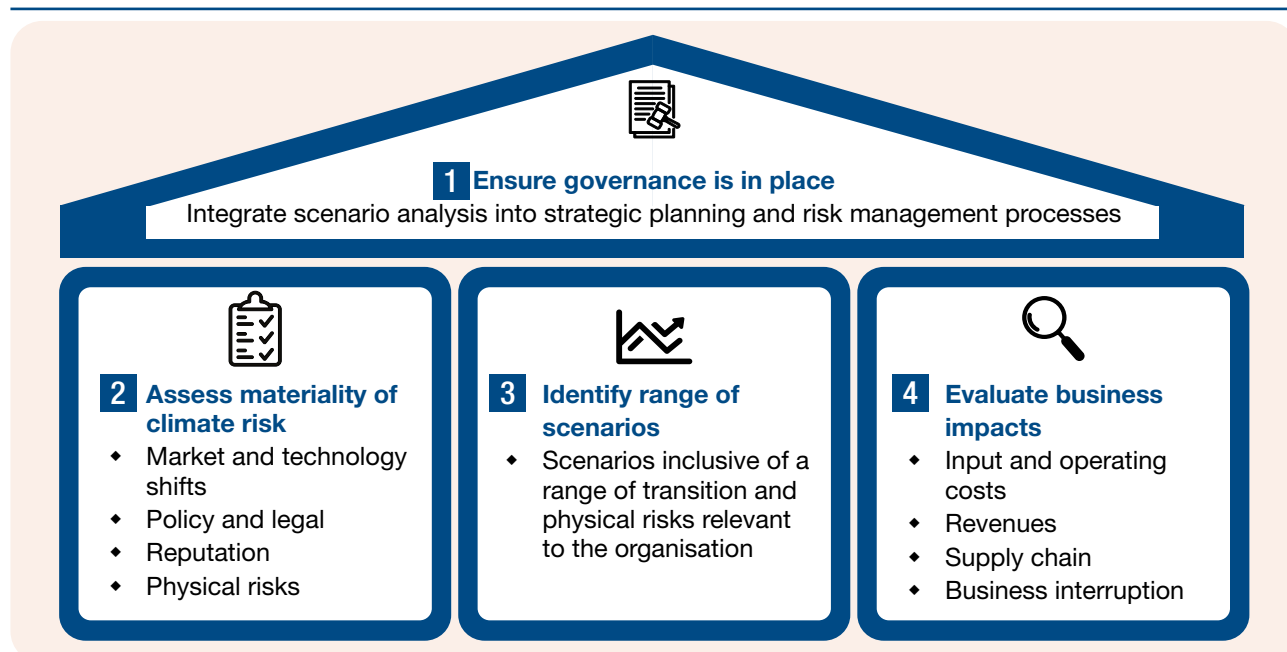
We will commit to manage climate risk across our policy functions and reduce emissions from our physical operations

- We aim to **conduct climate risk stress tests for the financial industry by 2024**. These stress tests will assess the impact of climate change on the balance sheets of financial institutions over the next 30 years and estimate the potential financial losses that may result. This will be supplemented by efforts to model the macroeconomic and financial system impact of climate shocks based on various climate

scenarios, building on the scenarios developed by the NGFS.

- We will **enhance our surveillance and forecasting work to better understand the possible effects of climate change on key macroeconomic variables**. This will include engaging business leaders and other relevant stakeholders to better understand the transmission of physical and transition risks to the real sector, including the knock-on effects throughout the supply chain. We will also seek to better understand the implications of these changes on the conduct of monetary policy.

Diagram 4:
Overview of scenario analysis process



Source: TCFD (2017), “Technical Supplement: The Use of Scenario Analysis in Disclosure of Climate-related Risks and Opportunities”.

ii Manage our financial assets with greater consideration to climate and environmental risks

- We will **adopt the recommendations of the TCFD and continue to enhance our climate-related financial disclosures, building on disclosures made since 2020.** Efforts will be directed at expanding disclosures to include risk management, metrics and targets relevant to the Bank's operations.
- We will **incorporate climate and environmental risk considerations into our portfolio management activities.** This aims to manage our own exposure to climate and environmental risks, as well as contribute to the transition towards reduced emissions, in a manner that is consistent with our investment objectives. Our investment strategies will take into account ESG factors and principles of Sustainable and Responsible Investment (SRI) as we consciously manage the environmental impact of our portfolio in line with sustainable financial returns.

iii Run our physical operations more sustainably

- In the management of our facilities, we will seek to **improve energy efficiency and move toward principles of circularity in waste management.**
- On currency management, we will **continue to promote the issuance and usage of longer-lifespan polymer banknotes** that will reduce banknote disposal volumes over time. We will also explore more sustainable ways to dispose shredded banknotes while doubling-down on efforts to accelerate the adoption of e-payments, which will also promote the broader digitalisation agenda.



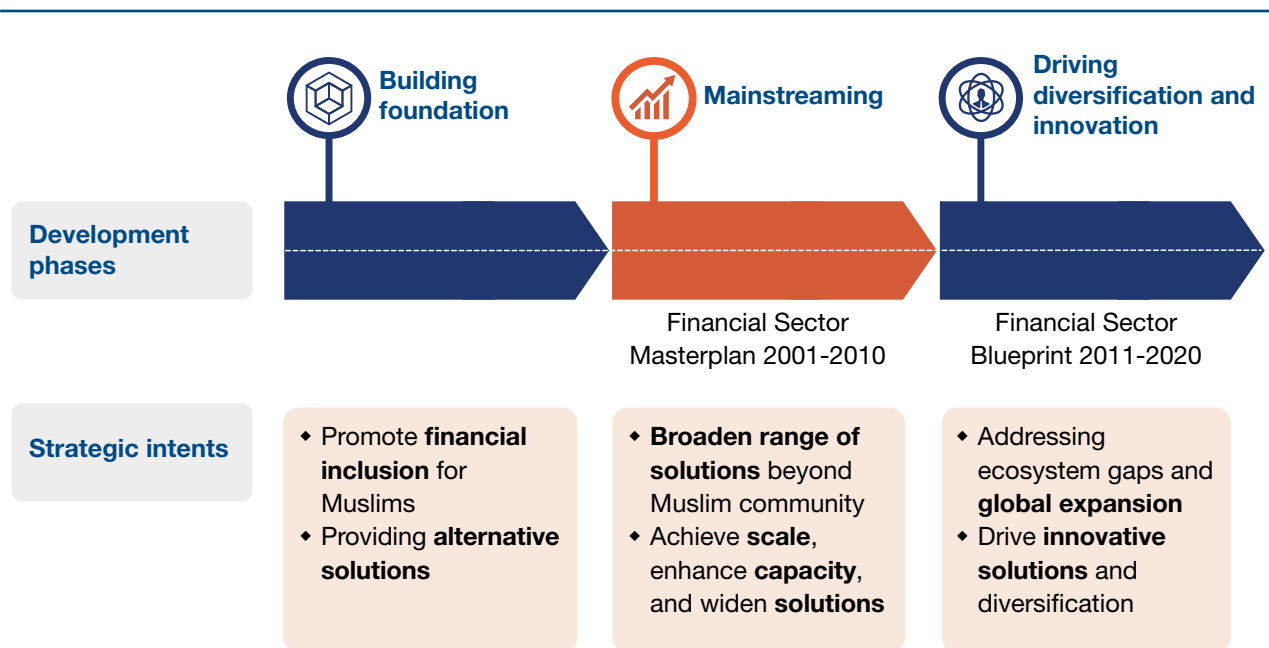


Strategic Thrust 5

Advance value-based finance through Islamic finance leadership

Islamic finance in Malaysia has undergone three broad phases of development over the last four decades – foundation-building, mainstreaming, as well as driving diversification and innovation (Diagram 1).

Diagram 1:
Phases of development over the last four decades



Malaysia's global leadership in Islamic finance is the result of concerted efforts by the Government, financial regulators, and industry players. Over the years, a wide range of initiatives have been advanced – including providing the overall enabling legal and regulatory environment, rolling out structural reforms to align strategies, addressing market frictions and incentives, as well as building long-term capacity. The country has also contributed to the development of global infrastructures to promote Islamic finance development, such as the setting up of the Islamic Financial Services Board (IFSB) and the International Islamic Liquidity Management Corporation (IILM), which are both headquartered in Malaysia.

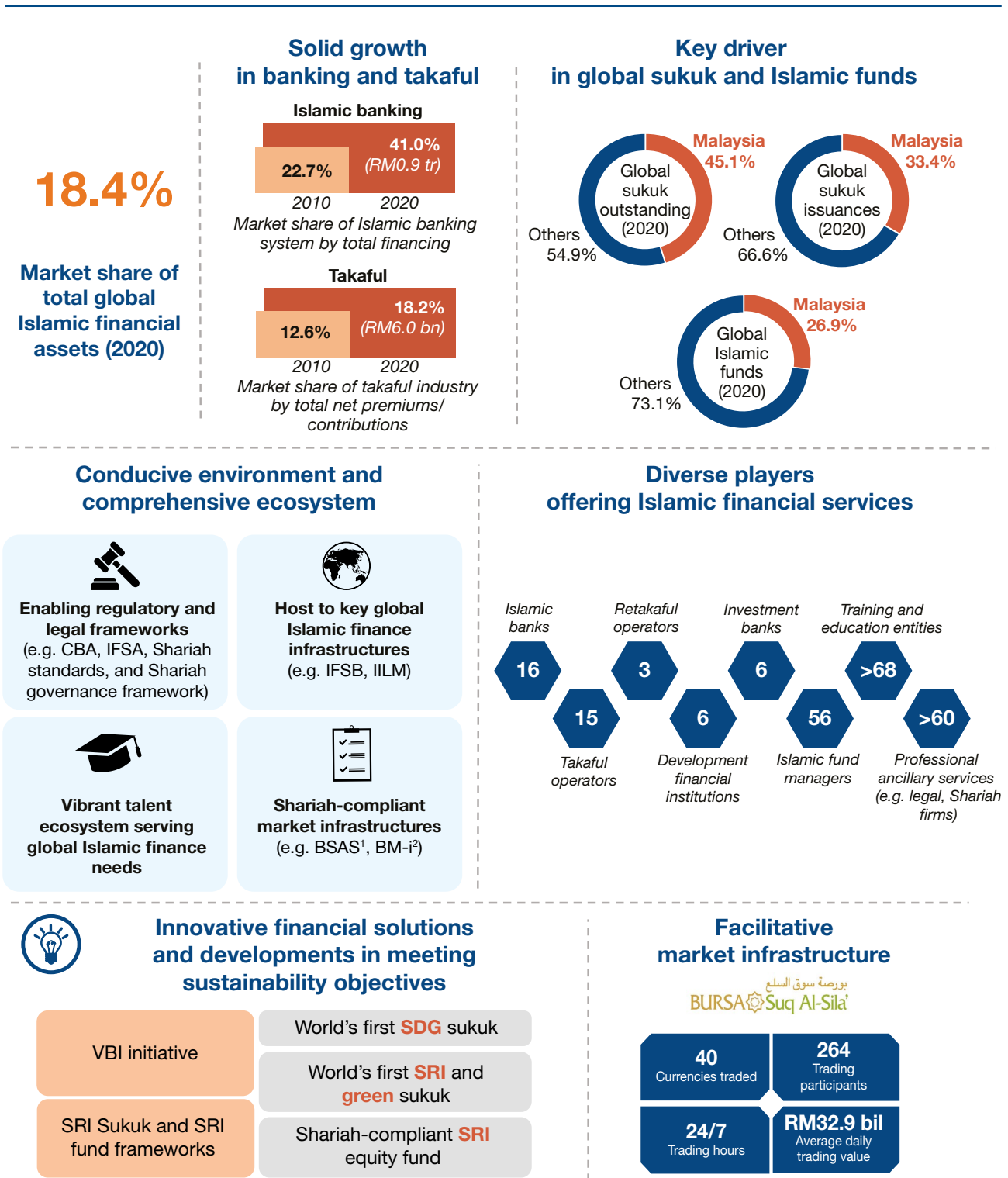
Today, Malaysia enjoys a mature Islamic finance ecosystem with dynamic and resilient players, diverse products, and comprehensive enabling infrastructures (see Diagram 2 for an overview).

As Malaysia's Islamic finance ecosystem continuously adapts to the fast evolving economic and social needs, efforts remain anchored on Shariah principles – aimed at realising a vision of economic growth that is balanced, progressive, sustainable and inclusive (Diagram 3).

Building on these achievements, the strategies for the next five years will seek to leverage Malaysia's well-developed Islamic finance ecosystem, particularly to:

- Sharpen Malaysia's proposition as an international gateway for Islamic finance;
- Strengthen policy enablers of value-based finance for greater impact; and
- Mainstream social finance.

Diagram 2:
Highlights of Malaysia's Islamic finance ecosystem



¹ Bursa Suq Al-Sila' (BSAS) is a commodity trading platform specifically dedicated to facilitate Islamic liquidity management and financing by Islamic financial institutions.

² Bursa Malaysia-i (BM-i) is a fully integrated Islamic securities exchange platform with a comprehensive range of exchange related facilities, that incorporate Shariah-compliant features.

Source: Bank Negara Malaysia, MIFC data estimates, Bursa Malaysia, Malaysian Qualifications Agency, the Securities Commission, Refinitiv

Diagram 3:
Shariah principles underpinning Islamic finance development efforts

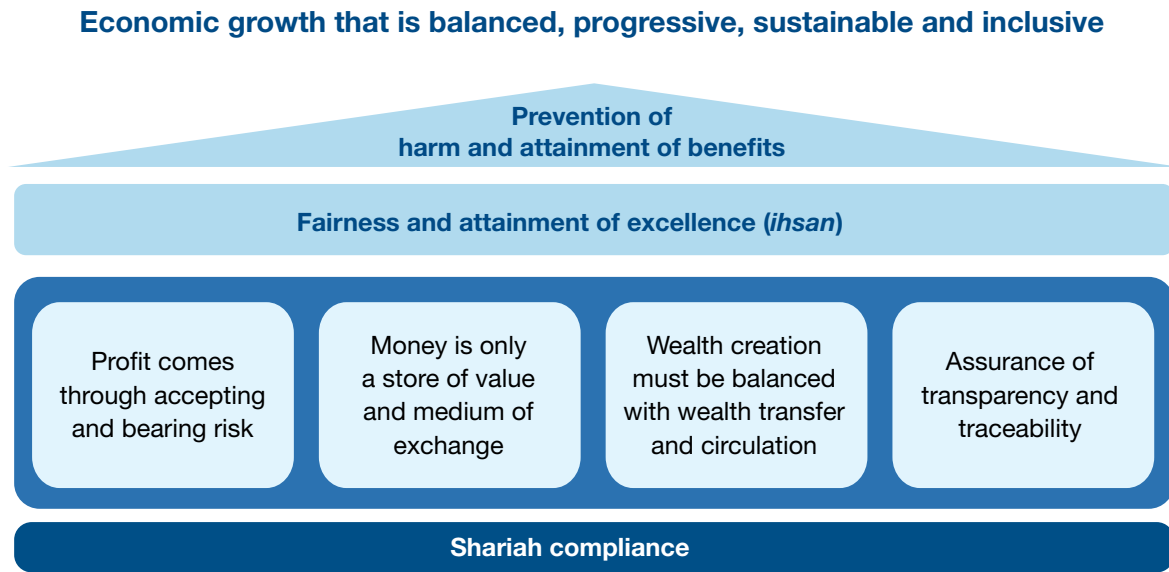


Diagram 4:
Advance value-based finance through Islamic finance leadership

**A**

Sharpen Malaysia's proposition as an international gateway for Islamic finance

- ◆ Strengthen gateway-critical capabilities in Malaysia's Islamic financial industry
- ◆ Promote greater industry leadership
- ◆ Facilitate further deepening of Malaysia's Islamic financial and capital markets

**B**

Strengthen policy enablers of value-based finance for greater impact

- ◆ Develop a more conducive regulatory environment to facilitate the application of diverse Shariah contracts
- ◆ Support the industry's innovation efforts in developing new value-based business models, solutions, and practices
- ◆ Facilitate greater stakeholder activism through higher quality disclosures

**C**

Mainstream social finance

- ◆ Elevate social finance as an integral part of the Islamic finance ecosystem

Strategy 5A

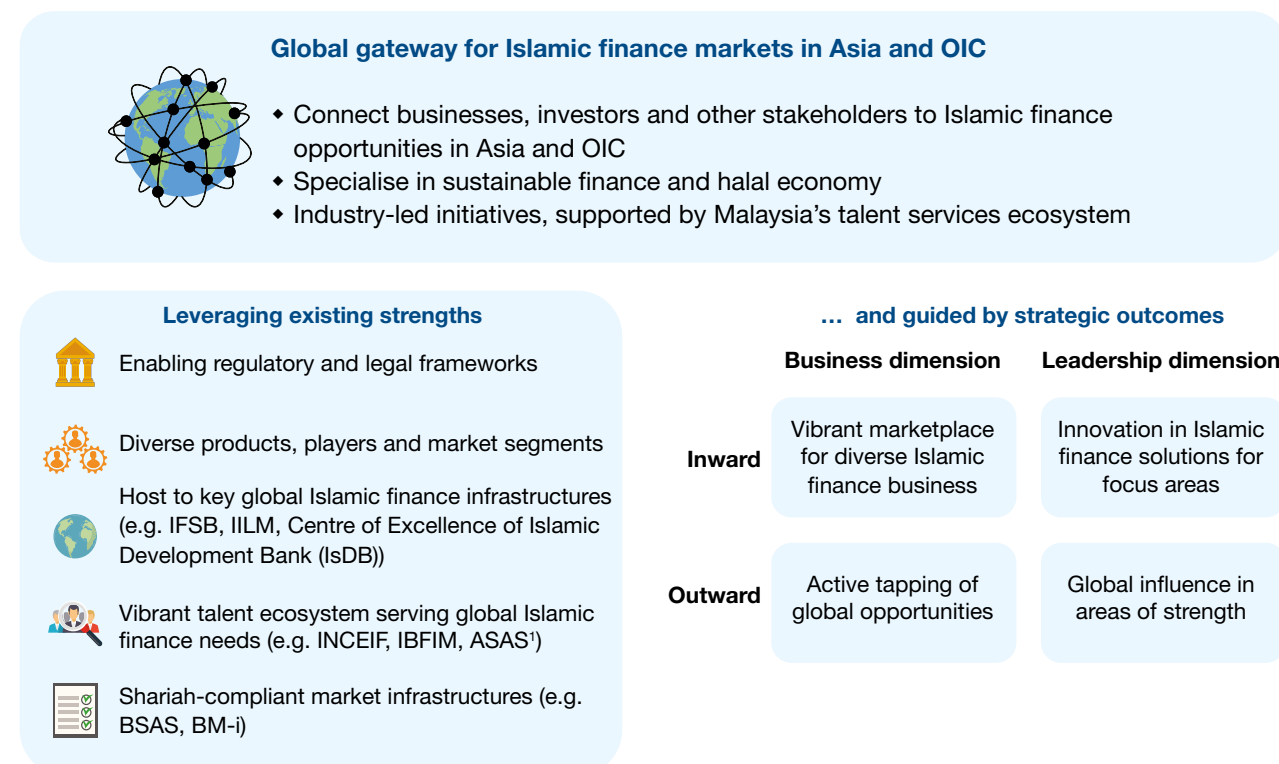
Sharpen Malaysia's proposition as an international gateway for Islamic finance

The global Islamic finance landscape has evolved significantly. Compared to a decade ago, Islamic finance has gained greater prominence in the global financial landscape. Global Islamic financial assets have grown from USD1.6 trillion in 2012 to USD2.7 trillion in 2020¹. Prospects for further growth remain significant, particularly within Asia and Organisation of Islamic Cooperation (OIC) countries. These may arise from untapped market segments, the growing halal business, and demand for more sustainable investments. Alongside the broader digitalisation of financial services, Islamic fintech opportunities are also growing, particularly in developing countries with Muslim-majority populations.

The Islamic finance space is thus expected to become more vibrant globally. Increasingly, more countries are looking to develop domestic markets and expand their footprint overseas. This environment creates new opportunities to Islamic finance – such as new cross-border partnerships to realise synergies, including through ‘collaborative competition’ (co-opetition) among established and emerging Islamic financial centres.

Against this backdrop, the Malaysia International Islamic Financial Centre (MIFC) vision and strategy continues to evolve in response to global trends and shifts in real economic needs (Diagram 5).

Diagram 5:
MIFC vision moving forward



¹ Association of Shariah Advisors in Islamic Finance (ASAS).

¹ Source: IFSB (2013, 2021), “Islamic Finance Services Industry (IFSI) Stability Report”.

Our strategies aim to sharpen Malaysia's proposition – specifically, to be a **global gateway for Islamic finance markets in Asia and OIC**. This envisions Malaysia connecting Islamic finance opportunities in Asia and OIC markets with businesses, investors, and other stakeholders across the globe – including partnerships with other jurisdictions to advance areas of mutual interest. We will intensify efforts to facilitate industry-led initiatives that leverage Malaysia's Islamic finance ecosystem, including its infrastructure, instruments, expertise, and players. This includes efforts to preserve Malaysia's strengths as a destination of choice for Islamic fundraising and investment activities, as well as a retakaful hub.

In positioning Malaysia's Islamic finance gateway, we will pursue two areas of specialisation:

- First, a greater focus on opportunities in **sustainable finance**. This builds on Malaysia's pioneering work in VBI, which sets out the frameworks and implementation guidance for a holistic approach to financial intermediation. There are also synergies with our efforts on climate and environmental risks – a key piece of the sustainable finance agenda (refer to the chapter “Position the financial system to facilitate an orderly transition to a greener economy”).
- Second, greater integration of Islamic finance with the **halal industry**, particularly in financing halal trade and investment. This supports a more

complete solution for the halal value chain. Notably, the global halal trade has enormous prospects (estimated to be worth USD2.4 trillion in 2024²). In realising this potential, the MIFC community can play a role to support halal trade and supply chain activities (e.g. halal certification and logistics). Further, financial institutions may also help nurture local halal businesses into global or regional players.

In supporting these developments, we will continue to provide an enabling policy environment. Realising this vision will require Malaysia's Islamic financial institutions to be agile and in a state of readiness to capitalise on evolving opportunities. Greater industry leadership, as well as targeted public-private partnerships, will thus be crucial. This includes initiatives in the Islamic finance talent ecosystem – which will remain vital to drive expertise development for the gateway's key focus areas, as well as to export Malaysia's education and training services abroad.

In advancing the sharpened vision for MIFC, our strategies aim to:

- i. Strengthen gateway-critical capabilities in Malaysia's Islamic financial industry;
- ii. Promote greater industry leadership; and
- iii. Facilitate further deepening of Malaysia's Islamic financial and capital markets.

i Strengthen gateway-critical capabilities in Malaysia's Islamic financial industry

We are committed to the MIFC agenda and will continue to lead on regulatory and Shariah fronts, as well as facilitate market access for financial institutions

- We will **support efforts to improve the Islamic financial industry's global distribution capabilities** to better tap opportunities outside of Malaysia. These include facilitating Islamic finance activities in other markets by businesses that prefer to use Islamic finance, as well as enabling business matching of halal exports with potential clients abroad (see Diagram 6). To this end, we will enhance Malaysia's connectivity with potential Islamic finance markets to strengthen or realise the distribution potential of financial institutions. These include collaborative efforts to:

- **Facilitate Malaysian financial institutions in expanding their footprint in Islamic finance business** in other markets – among others by engaging with other financial regulators and authorities, either bilaterally or multilaterally, to enable the wider provision of Islamic financial offerings;
- **Promote greater alignment of Islamic finance-related standards and practices**, including through global standard-setting bodies such as the IFSB and bilateral engagements. We will also continue to promote mutual recognition of Shariah and regulatory requirements globally. This includes enhancing the role and structure of the Centralised Shariah Advisory Authorities (CSAA) as the platform to pursue mutual recognition of Shariah application across jurisdictions; and

² Amount projected based on Muslim spending on halal products and services (Source: Dinar Standard Report (2020), “State of the Global Islamic Economy Report 2020/21: Thriving in Uncertainty”).

- **Facilitate greater visibility of Malaysia's professional services** (e.g. Shariah advisory) and **talent development** institutions (e.g. INCEIF, International Shari'ah Research Academy for Islamic Finance (ISRA), IBFIM). This aims to further export Malaysia's Islamic finance expertise through cooperative efforts with industry players and the relevant government agencies, such as the Malaysia External Trade Development Corporation (MATRADE) and Halal Development Corporation (HDC).
- We will **facilitate nascent Islamic financial innovations, including to accelerate the scaling up of new products and services**. Our efforts will focus on trade-related solutions, alternative finance models (e.g. blended finance), and sustainable finance. These include repurposing existing seed funding provided by the Bank to Islamic fund management companies (IFMCs) to focus on sustainability and innovative-driven mandates. Meanwhile, the growing market for Islamic fintech will be supported by broader initiatives to foster a vibrant digital financial services landscape – including a conducive environment to test and scale digital innovations (refer to Strategy 3B(i) of “Advance digitalisation of the financial sector”).
- Complementing this, we will continue to **strengthen global partnerships to advance Islamic financial innovations** beyond Malaysia's borders. These include joint initiatives with other international financial centres and multilateral organisations (e.g. the World Bank, United Nations Development Programme (UNDP) and IsDB). Such initiatives can provide critical insights for innovations in Malaysia's Islamic finance ecosystem. Where possible, we will build on these arrangements to identify areas where Malaysia can act as a testbed for innovation to better meet global Islamic finance needs.
- We remain committed to **refine measures towards strengthening Malaysia's global competitiveness as an Islamic finance gateway**. A key outcome will be to support Malaysia as the preferred Islamic finance partner for halal industry growth. To this end, we will explore collaboration with the relevant agencies (e.g. MOF, Malaysian Investment Development Authority (MIDA) and HDC) to create stronger links between Islamic financial services and Malaysia's economic propositions as a leading halal hub, particularly in supporting high value-added sectors and initiatives under the NIA. We will also continue to work alongside other financial regulators such as the SC Malaysia, Bursa Malaysia, and the Labuan Financial Services Authority on complementary strategies that advance the MIFC agenda.



Greater industry leadership
to take MIFC forward

ii Promote greater industry leadership

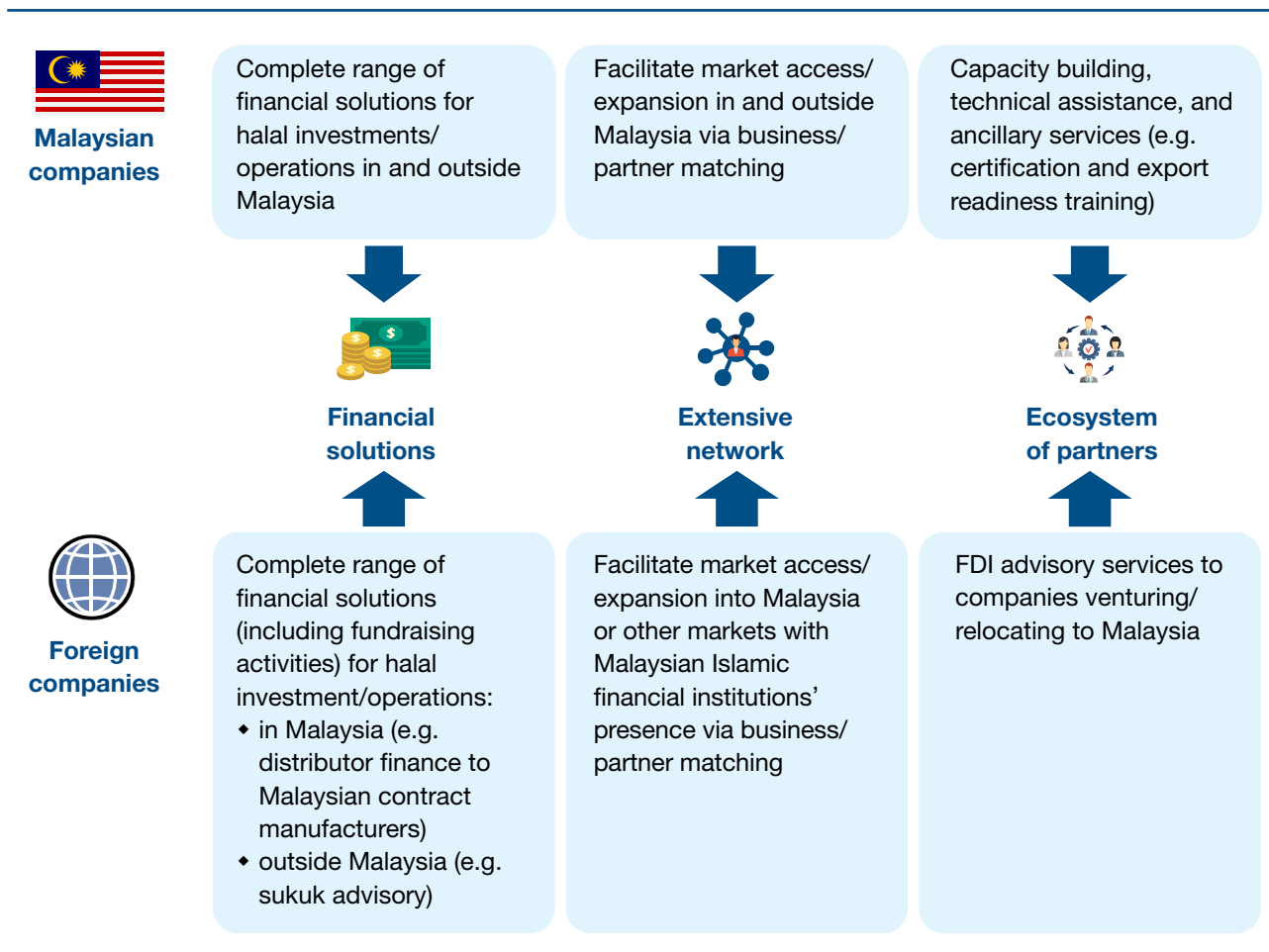
- We will **enhance mechanisms for greater industry leadership**. This includes the review of the MIFC Executive Committee (EXCO) and MIFC communication strategies. In the earlier years of the MIFC agenda, a strong regulatory role – together with the contribution of the MIFC EXCO and industry players – formed the key building blocks for a conducive and vibrant Islamic finance ecosystem.

With the more mature Islamic financial industry and the rapidly evolving landscape of global opportunities, greater industry stewardship is needed going forward. In sharpening Malaysia's proposition as an Islamic finance gateway, we see our role as focusing more on being a facilitator or partner in broader industry-wide efforts.

In the near term, we will work with the industry to **reform existing mechanisms and platforms** to be more agile, and to better position industry champions to drive critical agendas for MIFC. These include efforts to further:

- Enhance Malaysia's position as an **Islamic fundraising and investment destination**;
- Strengthen **distributional capabilities** and expand **market access** for players to provide Islamic finance solutions;
- Enhance the role of Islamic finance to **support Malaysia's national halal agenda** (see Diagram 6); and
- Encourage cohesive efforts by education and training providers in sustaining Malaysia's position as a **leading a knowledge centre for Islamic finance globally**.

Diagram 6:
Examples of possible Islamic finance offerings as a gateway to the halal economy



iii Facilitate further deepening of Malaysia's Islamic financial and capital markets³

Efforts to improve Malaysia's Islamic financial and capital markets will be continuously pursued

- We will continue to **promote Malaysia as the centre for origination, issuance, and trading for sukuk**. This will leverage our comparative advantage in sukuk advisory, particularly in structuring and innovation, to tap into the growing sukuk trends, including sustainable sukuk in line with MIFC's focus areas. This will also be achieved through the continued deepening of the domestic hedging market and strengthening of domestic players' global distribution capabilities to further enhance Malaysia's ability to attract a larger and broader foreign investor base. Such efforts will further improve Malaysia's propositions as the preferred destination for Shariah-compliant fundraising and investment, complemented by a facilitative framework for the issuance and subscription of ringgit and foreign currency-denominated sukuk in Malaysia.
- We will continue to **enhance best practices and standards in the Islamic money and capital markets**, in line with international standards. To this end, we will continue to promote collateralised Islamic transactions and support the implementation of collateral management practices. As part of these efforts, we will work towards the recognition of additional Islamic instruments for close-out netting (e.g. collateralised commodity *murabahah*) and greater adoption of Islamic derivatives agreements (*tahawwut*) among interbank players⁴.
- We will continue to **review and improve the structure of Islamic instruments** to promote greater Shariah acceptance and to leverage the diversity of Shariah contracts. This includes efforts to promote a wider range of Islamic risk management tools, including derivatives, to investors. We envision that this measure will lead to increased vibrancy in the Islamic derivatives market, and subsequently contribute to the expansion of Islamic finance and share of Islamic financing in the onshore financial market.

Strategy 5B

Strengthen policy enablers of value-based finance for greater impact

As we advance SDGs in financial development, the Islamic financial sector can play a key role. Islamic finance is uniquely aligned to the growing calls for a responsible and ethical model for financial services, given the fundamental values of Shariah to prevent harm and promote the attainment of benefits – including to improve well-being through wealth preservation, wealth circulation, and justice.

Building on this, we introduced key frameworks in recent years – namely, VBI in 2017 and VBIT in 2021. Complemented by implementation guidance, these frameworks outline how Islamic finance solutions and practices can support a more positive impact on the economy, community, and environment.

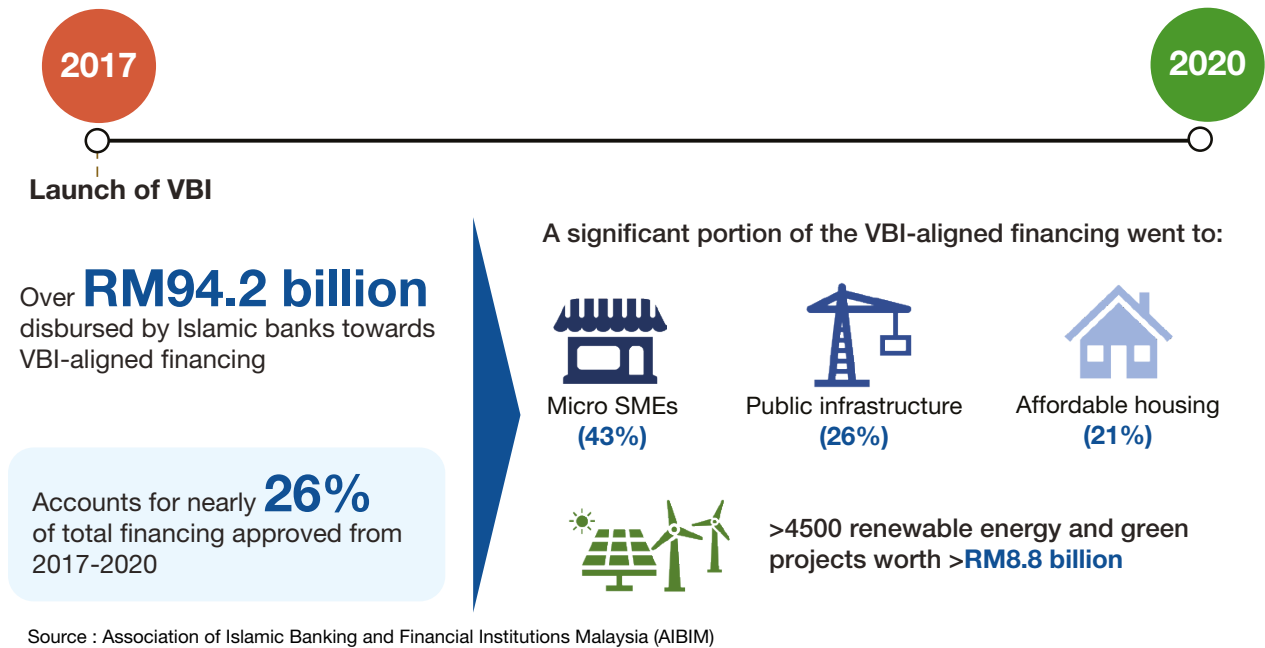
Islamic financial institutions have made steady progress since then, delivering value-based finance solutions to a growing number of individuals and businesses in recent years (see Diagram 7). The impact of VBI is also evident in the halal industry. Halal businesses have benefited from the comprehensive suite of financial solutions in expanding their operations beyond the domestic market, complemented by the provision of business advisory and ancillary services.

In the coming years, we envision Islamic financial institutions leading efforts to widen the adoption of value-based finance across the financial sector. These efforts include developing innovative solutions and refining business practices towards greater social, economic, and environmental resilience – underpinned by more refined measures of value and impact.

³ These efforts will be pursued in collaboration with the Securities Commission, consistent with the Capital Market Masterplan 3 (CMP3).

⁴ Initiatives will be geared towards greater adoption of *tahawwut* agreements by interbank participants and consequentially expanding the adoption to other markets and players.

Diagram 7:
Overview of VBI-aligned financing (2017 - 2020)



To advance these goals, we will prioritise these strategies:

- Develop a more conducive regulatory environment to facilitate the application of diverse Shariah contracts;
- Support the industry's innovation efforts in developing new value-based business models, solutions, and practices; and
- Facilitate greater stakeholder activism through higher quality disclosures.

We will continue to provide the appropriate regulatory facilitation for value-based finance implementation



i Develop a more conducive regulatory environment to facilitate the application of diverse Shariah contracts

- We will **strengthen the Shariah regulatory framework** by aligning the application of Shariah contracts with their underlying wisdom (*hikmah*). This includes setting out clear considerations for financial institutions in adopting certain arrangements in exceptional circumstances (e.g. ceding takaful risk to conventional insurers or reinsurers due to capacity constraints), in line with the *hajah* principle⁵.

Another desired outcome is for financial institutions to use more diverse Shariah contracts, thereby enabling value-based finance to serve a wider range of economic and social needs. This may call for a reconsideration of the use of *tawarruq*, which is presently a dominant Shariah contract for Islamic finance products in Malaysia's Islamic finance landscape.

- We will **explore the potential recalibration of existing regulatory requirements to cater to the broader application of *ta'awun***⁶ in takaful, guided by clear Shariah parameters. Current regulations restrict the transferability of distributable surplus across takaful funds in meeting the capital requirements, due to separate fund ownership for takaful. An expanded application of *ta'awun* may allow distributable surplus in a takaful fund that is sufficiently capitalised to support shortfalls in another takaful fund.

Similarly, a broader application of *ta'awun* can facilitate greater wealth circulation within the wider society. For example, the utilisation of distributable surplus in takaful funds may potentially be channelled to provide takaful coverage to lower-income households, thereby improving their financial resilience. In exploring the expansion of *ta'awun* application, key considerations would be to promote benefits to the wider society while preserving the interest of takaful participants.

ii Support the industry's innovation efforts in developing new value-based business models, solutions, and practices

Innovation, particularly through the application of diverse Shariah contracts, is an important enabler of value-based finance

- We will leverage enhancements to our existing Regulatory Sandbox to **better support innovations in value-based finance**, such as novel applications of Shariah contracts. These may arise from enhancements to the scope of *hajah* application, as well as from the exploration of new takaful business and operating models that support value-based protection (refer to Strategy 3B(i) of Chapter 3 – “Advance digitalisation in the financial sector”).

- We will **support further diversification of Investment Account (IA) offerings by Islamic banks** to mobilise new sources of funds for value-based financing, particularly initiatives to develop **impact-driven investment instruments**. This will align with broader efforts to facilitate banks' participation in non-debt finance solutions (refer to Strategy 1B(ii) of Chapter 1 – “Fund Malaysia's economic transformation”). IA offerings will need to evolve in tandem with heightened competition in the retail investment space, such as from equity crowdfunding and P2P financing. To widen the appeal of IA offerings among eligible investors, there is a need to expand the underlying assets beyond traditional financing. This may include mezzanine financing and venture capital that can also support VBI-aligned outcomes. We will continue to support industry efforts on that front where appropriate, including addressing regulatory frictions and facilitating the development of enabling infrastructure as necessary.

⁵ *Hajah* is defined as a situation of exigent circumstances that will cause or is likely to cause a detrimental impact to the safety and soundness of the Islamic financial institution, thus necessitating a temporary exception of a Shariah ruling. Further details are accessible in Bank Negara Malaysia's “Discussion Paper on Hajah” (2021) at https://www.bnm.gov.my/documents/20124/938039/Discussion_Paper_on_Hajah.pdf.

⁶ *Ta'awun* refers to the cooperation among a group of individuals in a takaful fund to mutually aid each other to meet certain needs, as collectively agreed in a takaful contract. Further details are accessible in Bank Negara Malaysia's “Shariah Resolution in Islamic Finance” (2010) at https://www.bnm.gov.my/documents/20124/761709/shariah_resolutions_2nd_edition.pdf/3844f55b-8c0f-23ea-5a2a-9874dc416a04?t=1593546461329.

iii Facilitate greater stakeholder activism through higher quality disclosures

With meaningful disclosures on impact, stakeholders can engage with financial institutions to address gaps and accelerate impact creation

- We will **facilitate improvements in the quality and usefulness of impact-based disclosures**. Our priority here is to foster a more conducive environment for effective stakeholder activism.

As it stands, Islamic financial institutions do provide impact-based disclosures under VBI. However, there is room to further enhance the information published – including to ensure the continued integrity of such disclosures, and better align them with international practices. This can foster greater confidence among

key stakeholders (e.g. investors and financial consumers) to evaluate, compare, and differentiate practices in VBI, thereby nudging the industry to continuously improve – while supporting greater visibility of VBI initiatives beyond national borders.

In collaboration with the VBI Community of Practitioners and VBIT Steering Committee, we will provide **guidance on reporting metrics that improve comparability and quality of disclosures**. A major focus will be to mitigate the risks of ‘impact washing’⁷ in these disclosures, which may include reducing the subjectivity or discretion accorded to certain parameters. The guidance will also be aligned to the phases of individual financial institutions’ VBI implementation which vary across the industry⁸, and complement the existing principles of sustainability reporting and initiatives on climate risk disclosures.

Strategy 5C

Mainstream social finance

Social finance refers to financial structures or business models that aim to deliver tangible social outcomes by mobilising philanthropic capital. Such capital includes Islamic social finance instruments such as *sadaqah* (donation), *waqf* (endowment) and *zakat* (alms). In recent years, we have worked closely with the industry and other stakeholders to encourage greater integration of social finance in the Islamic finance ecosystem.

Moving forward, social finance is envisioned to play a greater role, with Islamic finance leading the way – complementing public sector finance,

commercially-driven financial solutions, and corporate social responsibility (CSR) activities of the financial institutions to promote greater social resilience. To unlock the potential of social finance, our strategies will aim to elevate social finance as an integral part of the Islamic finance ecosystem.

The box article on “Social finance as an enabler of social development in Malaysia” provides further details on the social finance landscape as well as recommendations for other social finance actors on unlocking the potential and amplifying the impact of social finance.



We will adopt a nurturing approach to support financial institutions’ explorations to better integrate social finance within their businesses

⁷ Impact washing refers to a process in which impact-focused initiatives claim to be aligned with and contribute to development objectives without providing meaningful supporting evidence (Source: OECD (2021), “OECD-UNDP Impact Standards for Financing Sustainable Development”).

⁸ There are four phases towards the full implementation of VBI, namely Initiating, Emerging, Engaged, and Established (Source: Bank Negara Malaysia (2018), “VBI Implementation Guide”).

i Elevate social finance as an integral part of the Islamic finance ecosystem

- We will **support a range of finance models that promote impactful social outcomes**. This reflects how the optimal models can vary based on individual player's risk appetite, capacity, operational readiness, business strategy, and the evolving needs of financial consumers. Generally, we will **facilitate both blended finance and funding escalator models** (refer to Diagram 1 under the box article, "Social finance as an enabler of social development in Malaysia") to address financing, investment, and protection gaps in the market. This may include providing funding for specific financing facilities and facilitating collaboration between actors from the private and public sectors. Blended finance models refer to the combination of commercial funding (e.g. microfinancing) and philanthropic capital (e.g. *zakat* or *sadaqah*) to fund beneficiaries based on adjusted risk acceptance criteria. Funding escalator models, on the other hand, refer to the incubation of beneficiaries using social finance funds as they develop their creditworthiness and business track record, upon which they graduate to source for commercially-driven funding. Social finance funds are also mobilised to extend financial protection to low-income households as a form of safety net in the event of calamity.
- We will **enable a conducive regulatory environment for diverse business models**, recognising that social finance solutions could be delivered by a range of players. This builds on emerging interest among industry players to enter this space – be it as part of their existing mandates (e.g. DFIs), CSR initiatives by incumbents, or as a primary business strategy (e.g. digital players with a social finance focus). As part of these efforts, we will **facilitate the roll-out of more impactful pilot programmes for social finance**. These programmes will guide efforts to enhance regulations to remain fit-for-purpose, particularly to scale tried-and-tested social finance solutions. For example, these may include tailoring capital and liquidity rules to better reflect the risk profile of such activities (e.g. proportionate credit risk requirements for group-based lending using concessional funds and simplified liquidity requirements for ring-fenced donations).
- We will collaborate with the industry to **develop better measures of value and impact** in promoting more transparent disclosures of social finance. This strategy will be pursued together with impact-based disclosures for value-based finance, as outlined under strategy 5B(iii).



Box Article

Social finance as an enabler of social development in Malaysia

Social finance has the potential to narrow remaining inclusion gaps

Social finance is envisioned to play a greater role in Malaysia's financial landscape, with Islamic finance leading the way – complementing public sector finance and commercially-driven financial solutions to promote greater social resilience. Importantly, social finance has three unique qualities that can advance financial inclusion in a way that is transformative and addresses constraints typically associated with traditional finance.

First, social finance instruments can be designed for greater flexibility, thereby increasing the level of risk absorbency (in contrast with traditional debt-based finance). These range from allowing more flexible repayment terms that accommodate irregular income streams and not imposing repayment obligations on beneficiaries (e.g. financing funded by *zakat* funds). For donation-sourced financing, there is usually minimal or no financing cost attached (e.g. beneficiaries are only required to repay the benevolent financing provided). Social finance can thus improve access to funding for segments that face challenges in accessing commercially-driven finance. The use of more flexible, innovative financial structures can also avoid deepening existing financial vulnerabilities (e.g. indebtedness) faced by such individuals or businesses.

Second, implementation partners generally supplement funding with structured programmes that upskill beneficiaries in financial management, business acumen, and other key areas (e.g. digital capabilities). These enhance their financial literacy, foster entrepreneurial behaviour, and empower the beneficiaries to generate a more sustainable income and improve their quality of life.

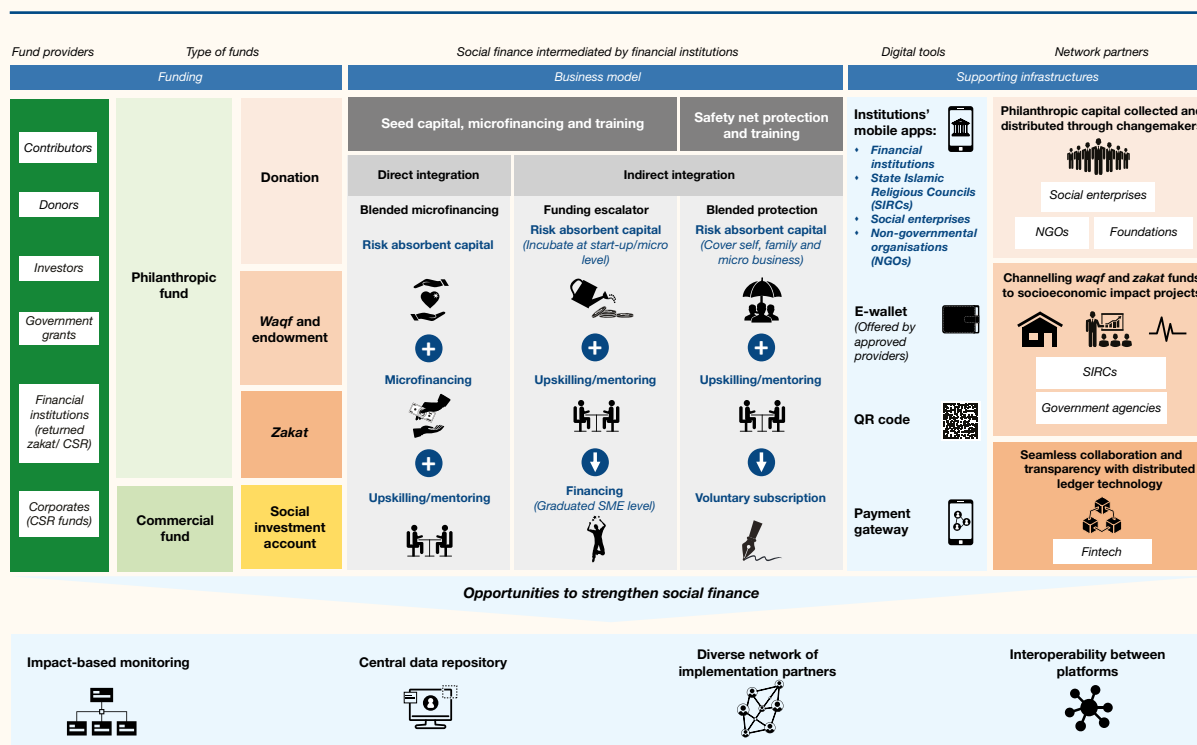
Third, social finance initiatives are often supported by impact monitoring and “pay-it-forward” mechanisms. Effective implementation of these mechanisms can build trust among the fund providers and target groups, as well as foster a virtuous cycle that encourages past beneficiaries to be part of efforts to support future ones – potentially creating a valuable network of support, thereby strengthening the upsides of social finance solutions.

The landscape of social finance solutions is becoming more vibrant and diverse

Over the past decade, several financial institutions have been exploring different ways to deliver social finance, refining their offerings over time (Diagram 1). While most ventures have been pursued as part of CSR initiatives, some players are developing social finance as a viable business proposition. Encouragingly, VBI-aligned financial institutions have begun to adopt a blended finance approach in social finance offerings, thus improving the target segments' access to capital and protection.

There is also greater collaboration among the diverse stakeholders and implementation partners. These partnerships can optimise the strengths of various actors in the ecosystem (e.g. collection/distribution agents, platform providers, payment facilitators, fund managers, and underwriters), thereby improving efficiency and outreach, augmented by the increased adoption of digital tools.

Diagram 1:
Common characteristics of social finance offerings in Malaysia



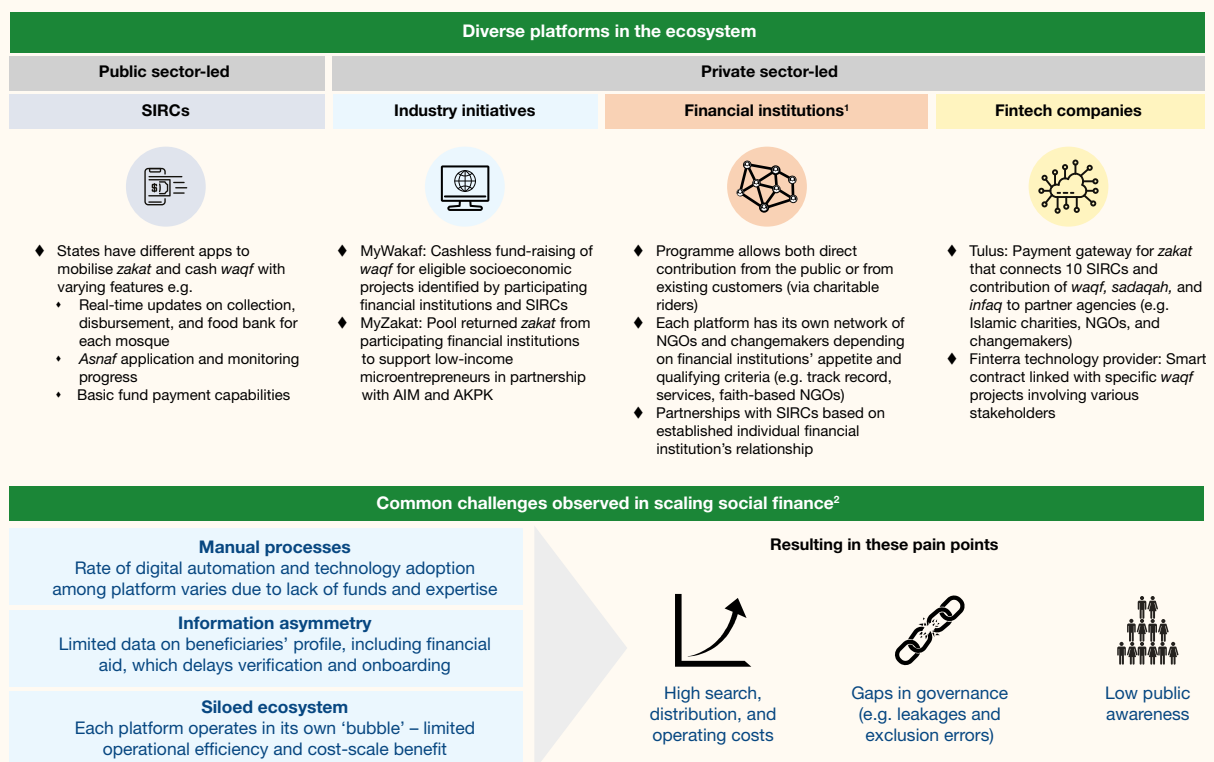
In 2020, iTEKAD was launched – a social finance pilot programme that blends financial and non-financial components. The first phase of the pilot has provided useful insights for participating banks to design more flexible offerings, as well as for diverse implementation partners to support training, business mentorship, and impact monitoring. Since then, we have seen the launch of more social finance solutions that are consistent with iTEKAD components to support pandemic affected micro-SMEs. These offerings combine philanthropic funds (such as grants, donations, and *zakat*¹) with low-cost or benevolent microfinance, supplemented with structured financial and business training. Ultimately, we are working towards nationwide expansion of iTEKAD and similar social finance offerings by various financial institutions. These programmes require close collaboration with diverse range of implementation partners and stakeholders such as government agencies, SIRCs, fintech companies, NGOs, social enterprises, and foundations.

Moving forward, multi-stakeholder efforts are key – including to promote shared infrastructures and to support national developmental priorities

As social finance gains traction, multi-stakeholder coordination and collaboration are critical to lower search and distribution costs, as well as to promote greater public confidence in the disbursement and governance of funds (refer to Diagram 2).

¹ Financial institutions as *zakat* payers may apply to participating SIRC to distribute a portion of the *zakat* paid (returned *zakat*) or partner directly with SIRC to distribute a certain portion to eligible recipients on behalf of the SIRC, subject to predefined criteria.

Diagram 2:
Overview of the diverse social finance platforms available



¹ The examples cited are social finance platforms established by financial institutions under the direct integration model.

² These challenges are not in relation to any specific platform and are based on observations across the social finance ecosystem.

These efforts include developing shared infrastructures – or making better use of existing ones, such as by making them interoperable – to reduce barriers to social finance offerings. Examples of such infrastructures include:

- A shared data repository of target groups for social finance programmes, which can support better risk-informed profiling of beneficiaries and the channelling of funds to unmet groups.
- A network of credible implementation partners – that are vested in social outcomes and have strong relationships with 'at-risk'² communities – can act as support system to build trust and encourage participation in the financial system.
- An integrated dashboard optimising mobile-based interfaces that facilitates real-time funding updates and impact disclosures. This can address key information gaps on the social finance landscape, including on readily available opportunities for willing stakeholders to contribute funds or volunteer other resources.

Another important thrust is to align social finance initiatives to national priorities, thereby amplifying the impact of social finance. These priorities include improving income generation potential for entrepreneurs as well as providing funding support for the provision of cost-effective education, healthcare services and facilities for common non-communicable diseases. Suitable financing and protection solutions can be designed to support these sectors in line with Malaysia's long-term focus on sustainable economic growth and entrepreneurial drive towards a high-income society and shared prosperity for all.

² These target groups, among others, are budding entrepreneurs and community groups with the ability to generate productive income when supported by small financing and protection value.



References

Acronyms and abbreviations

AFC	Asian Financial Crisis	CRR	composite risk rating
AI	artificial intelligence	CSAA	Centralised Shariah Advisory Authorities
AICB	Asian Institute of Chartered Bankers	CSM	CyberSecurity Malaysia
AIM	Amanah Ikhtiar Malaysia	CSPs	cloud service providers
AKPK	Credit Counselling and Debt Management Agency	CSR	corporate social responsibility
AML/CFT	Anti-Money Laundering and Countering Financing of Terrorism	DeFi	decentralised finance
AMLA	Anti-Money Laundering, Anti-Terrorism Financing and Proceeds of Unlawful Activities Act 2001	DFI	Development Financial Institution
API	application programming interface	DLT	distributed ledger technology
ASB	Asia School of Business	EAC	Economic Action Council
ASEAN	Association of Southeast Asian Nations	ECF	equity crowdfunding
BCBS	Basel Committee on Banking Supervision	EIS	Employment Insurance Scheme
BIS	Bank for International Settlements	e-KYC	electronic Know-Your-Customer
CAGR	compounded annual growth rate	EPF	Employees Provident Fund
CBA	Central Bank of Malaysia Act 2009	ePIF	e-Payment Incentive Fund Framework
CBDC	central bank digital currencies	ESG	environmental, social and governance
CCA	Consumer Credit Act	FA	financial adviser
CCOB	Consumer Credit Oversight Board	FATF	Financial Action Task Force
CCPT	Climate Change and Principle-based Taxonomy	FCI	Financial Capability and Inclusion Demand Side Survey
CDRC	Corporate Debt Restructuring Committee	FDI	foreign direct investment
CGC	Credit Guarantee Corporation Malaysia Berhad	FEN	Financial Education Network
CRMA	Certification in Risk Management Assurance	FinTIP	Financial Sector Cyber Threat Intelligence Platform
		FIRST	Financial Resilience Support Scheme

FP	financial planner	INCEIF	International Centre for Education in Islamic Finance
FSA	Financial Services Act 2013	IoT	internet of things
FSB	Financial Stability Board	IP	intellectual property
FSP	financial service provider	IsDB	Islamic Development Bank
FX	foreign exchange	ISO	International Organisation for Standardisation
G20	Group of Twenty	ISRA	International Shari'ah Research Academy for Islamic Finance
GDP	gross domestic product	ITOs	insurers and takaful operators
GHG	greenhouse gas	JC3	Joint Committee on Climate Change
GLICs	government-linked investment companies	KPI	key performance indicator
GTFS	Green Technology Financing Scheme	LCTF	Low Carbon Transition Facility
HDC	Halal Development Corporation	LEAs	law enforcement agencies
HSIT	hospital and surgical insurance/ takaful	LIFBs	locally-incorporated foreign banks
IA	Investment Account	MAMPU	Malaysia Administrative Modernisation and Management Planning Unit
IAIS	International Association of Insurance Supervisors	MASCO	Malaysia Standard Classification of Occupations
IBFIM	Islamic Banking and Finance Institute Malaysia	MATRADE	Malaysia External Trade Development Corporation
ICS	Risk-based Global Insurance Capital Standards	MCMC	Malaysian Communications and Multimedia Commission
ICTF	Interoperable Credit Transfer Framework	MDEC	Malaysia Digital Economy Corporation
IFMCs	Islamic fund management companies	MHIT	medical and health insurance/takaful
IFSA	Islamic Financial Services Act 2013	MIDA	Malaysian Investment Development Authority
IFSB	Islamic Financial Services Board	MIFC	Malaysia International Islamic Financial Centre
IILM	International Islamic Liquidity Management Corporation	ML	machine learning
IMF	International Monetary Fund	ML/TF	money laundering and terrorism financing

MOE	Ministry of Education	PIDM	Malaysia Deposit Insurance Corporation
MOF	Ministry of Finance	POC	proof-of-concept
MOH	Ministry of Health	PPKS	Persatuan Penguji Keselamatan Siber
MRANTI	Malaysian Research Accelerator for Technology and Innovation	PRS	Private Retirement Scheme
MyCAC	Malaysia Climate Action Council	PSOs	payment service operators
MyKNP	Khidmat Nasihat Pembiayaan	PSPs	payment service providers
MySPC	Malaysia Social Protection Council	RBC/T	Risk-Based Capital Framework for Insurers and Takaful Operators
NACSA	National Cyber Security Agency Malaysia	RENTAS	Real-Time Electronic Transfer of Funds and Securities System
NDSP	National Data Sharing Policy	repo	repurchase agreement
NFCC	National Anti-Financial Crime Centre	RMIT	Risk Management in Technology
NGFS	Network for Greening the Financial System	RMK12	Twelfth Malaysia Plan
NGOs	non-governmental organisations	RPA	robotic process automation
NIA	National Investment Aspirations	RPP	Real-time Retail Payments Platform
NIST	National Institute of Standards and Technology	RRF	Reference Rate Framework
NRA 2020	National Risk Assessment 2020	RRP	recovery and resolution planning
OECD/INFE	Organisation for Economic Co-operation and Development / International Network on Financial Education	SBR	Standardised Base Rate
OFS	Ombudsman for Financial Services	SC	Securities Commission
OIC	Organisation of Islamic Cooperation	SCEL	Single Counterparty Exposure Limit
P2P	peer-to-peer	SDGs	Sustainable Development Goals
PayNet	Payments Network Sdn. Bhd.	SDRS	Small Debt Resolution Scheme
PCRF	Payment Card Reform Framework	SEACEN	South East Asian Central Banks
PDPA	Personal Data Protection Act 2010	SESS	self-employed social security
PE	private equity	SIDREC	Securities Industry Dispute Resolution Center
		SIRC	State Islamic Religious Councils

Acronyms and abbreviations

SJPP	Syarikat Jaminan Pembiayaan Perniagaan	TPSPs	third party service providers
SMEs	small and medium enterprises	UNDP	United Nations Development Programme
SPM	Skim Pembiayaan Mikro	URUS	Financial Management and Resilience Programme
SRI	sustainable and responsible investment	USA	United States of America
SSM	Companies Commission of Malaysia	VBI	Value-based Intermediation
STE	Staff Training Expenditure	VBIAF	Value-based Intermediation Assessment Framework
STF	Staff Training Fund	VBIT	Value-based Intermediation for Takaful
TCFD	Task Force on Climate-related Financial Disclosures	VC	venture capital
TEKUN	Tabung Ekonomi Kumpulan Usahawan Niaga		

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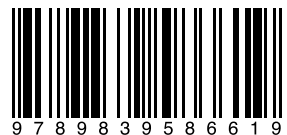
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