Part 5

Capital Market Review and Outlook

OVERVIEW

The Malaysian economy continued to be resilient in 2019, upheld by sustained strength in domestic private sector activities amidst a challenging external environment. Against this backdrop, the Malaysian capital market continued to play a vital role in financing the domestic economy with notable improvement in fundraising activities across all market segments. In terms of performance, the domestic bond market registered positive returns while the equity market experienced a positive shift in sentiments towards small and mid-cap companies, especially in the energy, construction and technology sectors. Going forward into 2020, the Malaysian economy is expected to remain on a steady growth path. Although the domestic capital market continues to be influenced by key external developments, it is expected to remain resilient and orderly, underpinned by Malaysia's strong macroeconomic fundamentals, ample domestic liquidity and supportive capital market infrastructure.

GLOBAL DEVELOPMENTS IN 2019

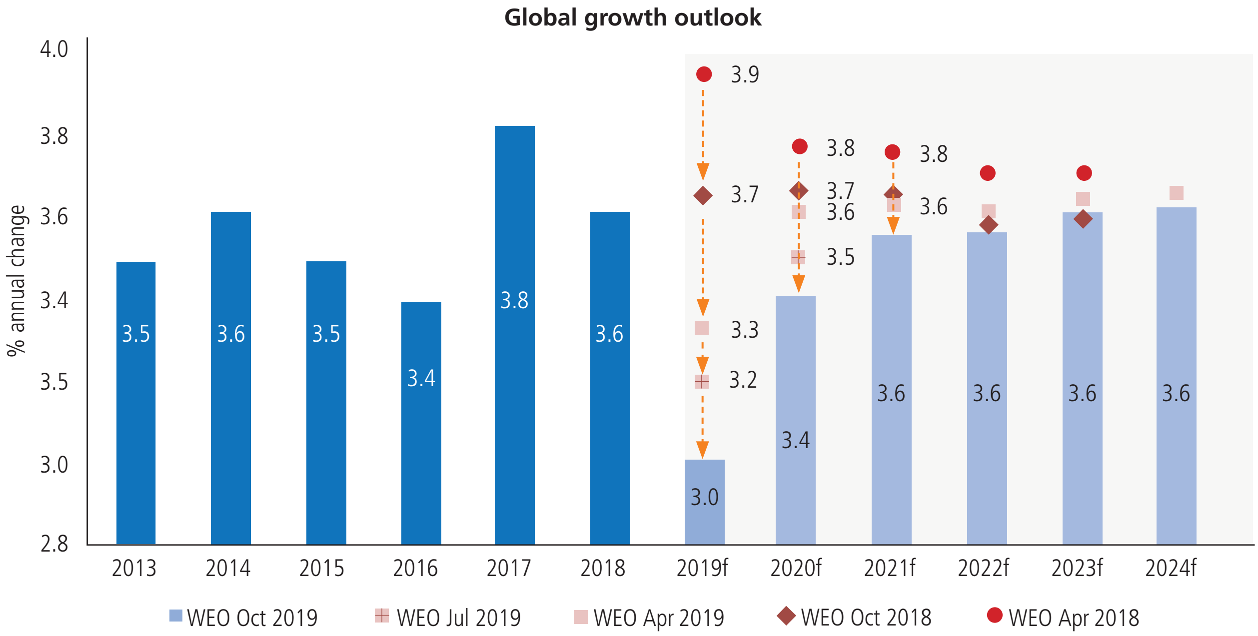
Growth of the global economy continued to soften in 2019, characterised by a synchronised slowdown across most economies in the developed and emerging world. This was driven primarily by significant weakness in global manufacturing and trade activities amidst the ongoing trade tensions and geopolitical uncertainties throughout the year. The slowdown in the global economy led the International Monetary Fund (IMF) to continue to downgrade its global growth projections (Chart 1). In October 2019, the IMF lowered its global growth forecast for the fifth consecutive time since April 2018 to 3.0% in 2019 – the weakest since the Global Financial Crisis (GFC). However, in contrast to the manufacturing sector, the services sector remained relatively resilient across the globe, particularly in Advanced Economies (AEs) on the back of positive labour market conditions and continued growth in consumer spending.

Global policy uncertainty continued to significantly affect the performance of the global economy and shape the performance of the global financial market during the year. This was reflected by measures of policy uncertainty which reached new highs in 2019 (Chart 2). In particular, the World Trade Uncertainty Index – a measure of global trade policy uncertainty – rose nearly ten-fold in Q4 2019 compared to a year earlier. The year 2019 commenced with a temporary US-China trade truce since December 2018, but experienced sharp escalations in tariff war between May and August 2019. Apart from tariffs, the US had also imposed business restriction on China's technology companies via its entity list in May and declared China as a currency manipulator in August. In September 2019, trade negotiation between the two nations took a positive turn. While overall global policy uncertainty remained high, this set the stage for a shift in investor sentiments for the remainder of the year, with the US and China officially agreeing to a phase-one trade deal in mid-December[1]. However, trade tensions were not isolated only to the US and China but also between the US and its other major trading partners in Europe and Latin America, as well as among other countries such as between Japan and South Korea.

[1] On 13 December 2019, the US agreed to halve the 15% duties on US$120 billion of Chinese products but maintained a 25% levy on US$250 billion of goods. US also agreed to avert new duties on US$160 billion of Chinese goods. China meanwhile pledged to increase total purchases of US goods by at least US$200 billion over the next two years and as much as US$50 billion of US farm products annually, and make commitments on currency and intellectual property enforcement.

Chart 1

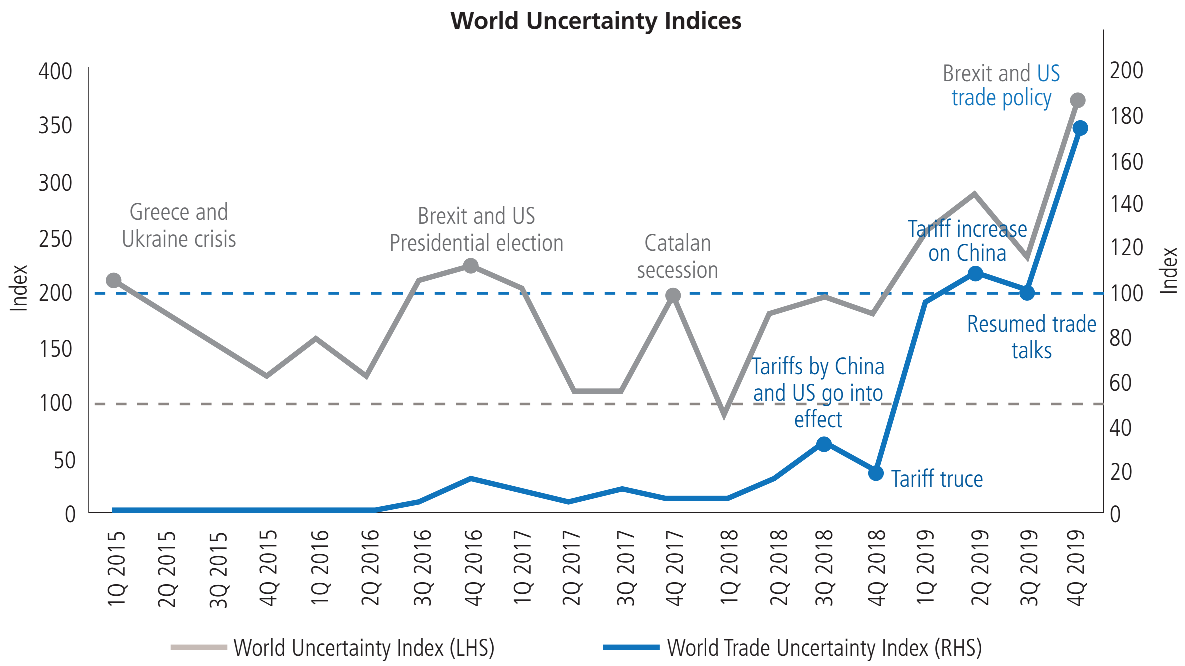
Global economy experienced synchronised slowdown, leading to downward revisions in global growth projection by the IMF



Source: IMF World Economic Outlook (WEO) Databases

Chart 2

Measures of economic uncertainty were at an all-time high, due mainly to rising trade and geopolitical tensions



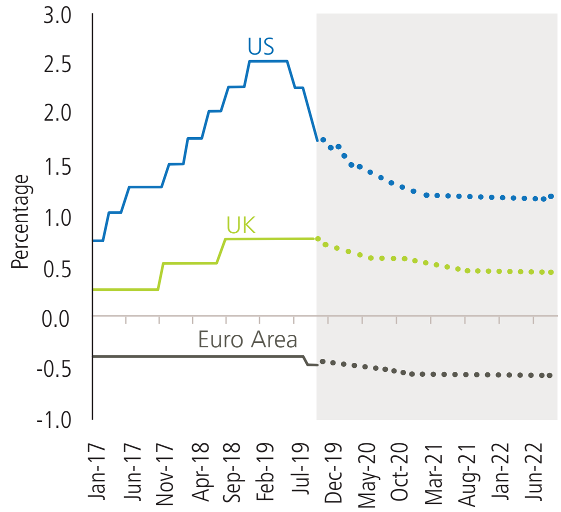
Source: Ahir, H, N Bloom, and D Furceri (2018), "World Uncertainty Index", Stanford mimeo

Amidst slower global growth and higher policy uncertainty, global monetary policy turned towards greater easing. This marked a turning point in the global monetary cycle and a shift in expectations of global liquidity after a period of normalisation in some economies. More than half of the economies globally adopted a more accommodative monetary stance in 2019. Notably, after increasing the benchmark federal funds rate to 2.5% in December 2018, the US Federal Reserve (Fed) lowered the benchmark rate by a cumulative 75 basis points (bps) to 1.75% in three separate moves in 2019. The more accommodative shift in monetary policy was also mirrored by other major central banks in AEs. Similarly, about two-thirds of emerging market economies' (EMEs) central banks eased their respective monetary policies (Chart 3).

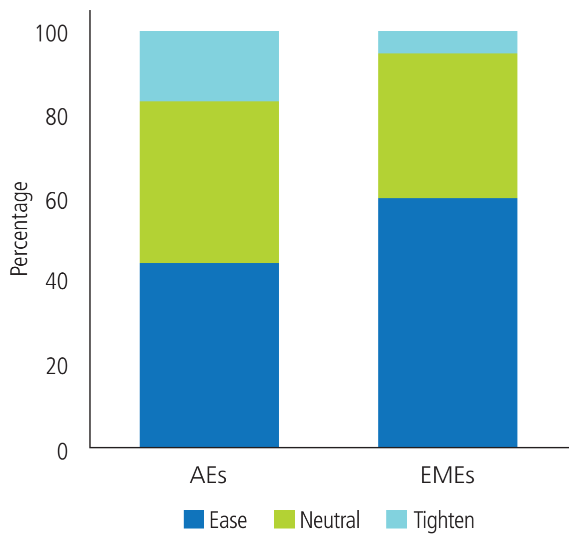
Chart 3

Global monetary policy broadly shifted towards a greater easing bias, with more than half of the economies globally adopting easier monetary policies

Actual and expected policy rates[1]



Proportion of central banks' actions in AEs and EMEs[2]



Notes:

1 Expectation of policy rates are based on the federal funds rate futures for the US, the sterling overnight interbank average rate for the UK, and the euro interbank offered forward rate for the Euro Area.

2 Based on Bloomberg Global Central Bank Monitor, which comprised 18 AEs and 35 EMEs.

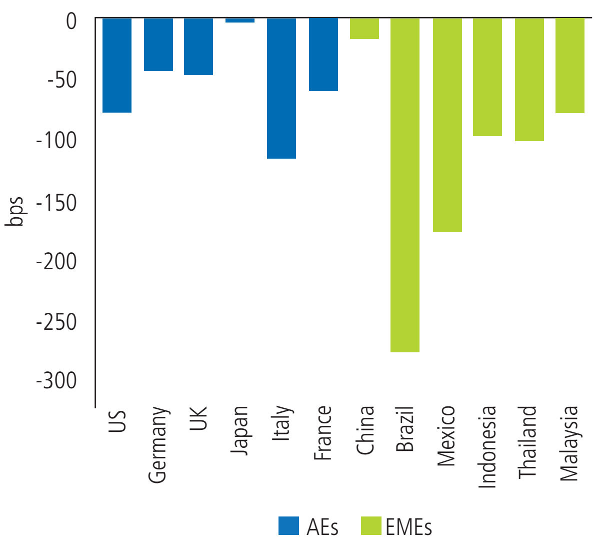
Source: Bloomberg, IMF, SC's calculations

The shift in global monetary policy direction had contributed to the improvement in global financial conditions and shaped the overall global capital market's performance during the year. In line with the increase in overall risk aversion amidst fears of possible global recession, global bond yields declined to reach unprecedented lows. This resulted in a flattening trend of the global bond yield curve and even temporary inversions in some AEs, where longer-tenured notes yielded lower than those with shorter-dated maturities. Notably, the spread between 10-year US Treasury (UST) and three-month Treasury bills turned negative between May and August 2019 following the sharp escalation of US-China trade tensions during the period. Overall, the amount of sub-zero yield debt securities surged to an all-time high of US$17 trillion in August to account for more than 30% of total global bonds (Chart 4).

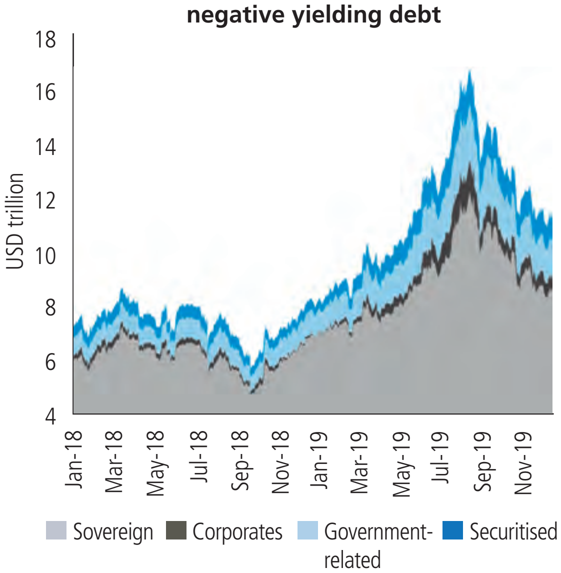
Chart 4

Global bond yields declined across the board, accompanied by a surge in negative yielding debt

Change in 10-year government bonds



Bloomberg Barclays global aggregate negative yielding debt



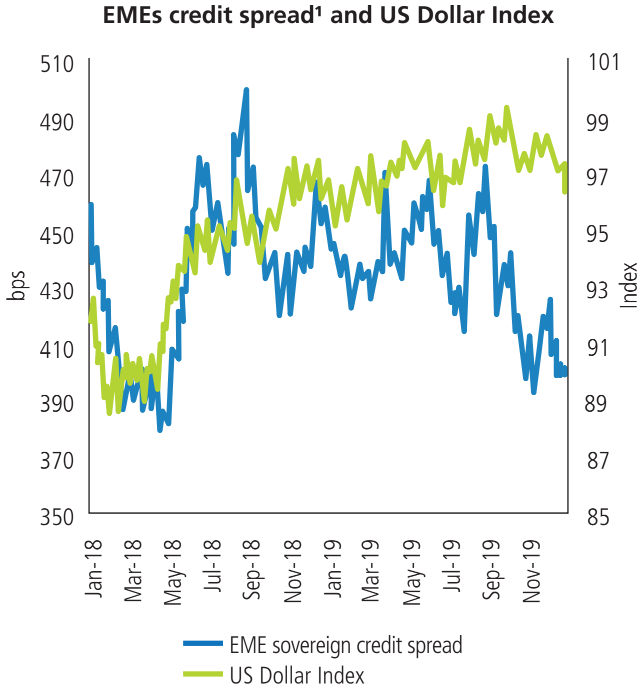
Source: Bloomberg, SC's calculations

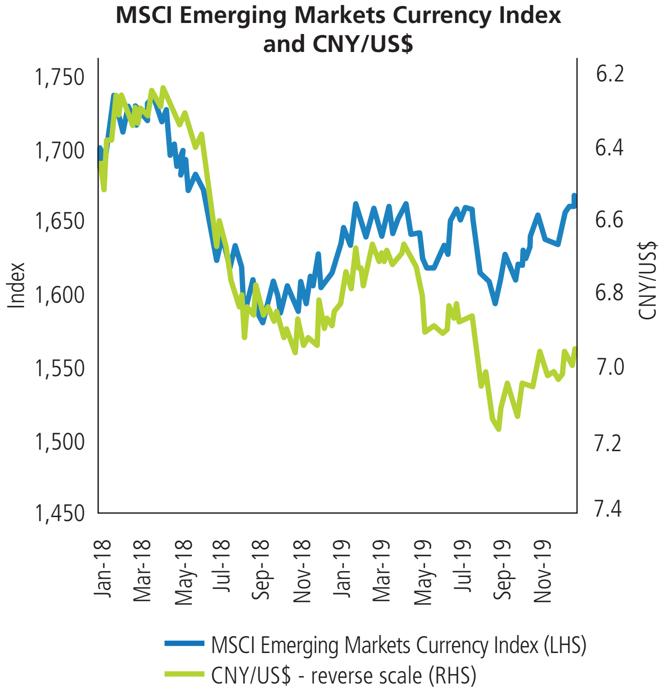
The improvement in global financial conditions, aided by the shift in AE's monetary policy direction, supported the rebound in portfolio flows in EMEs. This is especially visible in the bond market as higher yielding dollar-denominated debt became more attractive than that of AEs'. Although the EMEs' sovereign bond yields largely mirrored the performance of those in AEs, the spread between EMEs sovereign bond and UST yields narrowed in the second half of the year (Chart 5 – left panel).

However, capital market performance in EMEs continued to be volatile, driven largely by the unexpected turns in the US-China trade dispute and overall weakening in economic growth. Growth outlook had gradually shifted downward, weighed down by deteriorating global growth prospects and a slower than expected growth in China. China's economic growth slowed further to a multi-decade low of 6.2% in the first three quarters of 2019 with the renminbi weakening to 7.0 per US dollar in August – its lowest level since the GFC. Reflecting these developments, overall EMEs' currencies also weakened in tandem with the renminbi (Chart 5 – right panel).

Chart 5

EMEs' sovereign credit spread narrowed in the second half of the year, while EMEs' currencies weakened in tandem with the renminbi



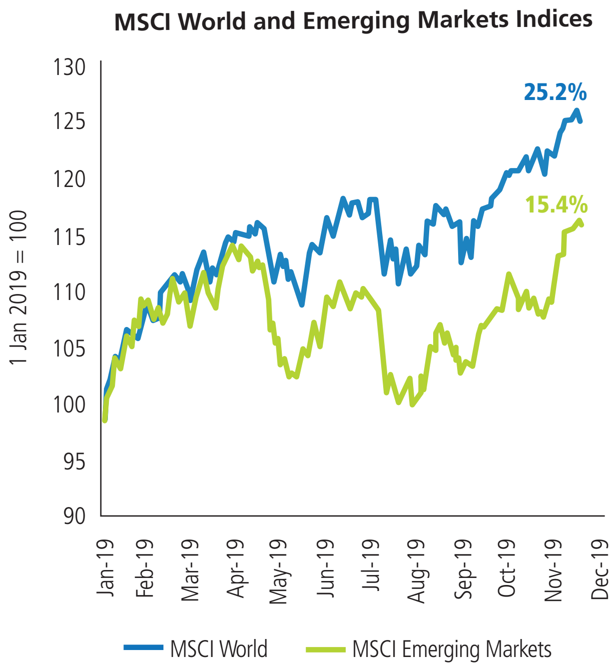


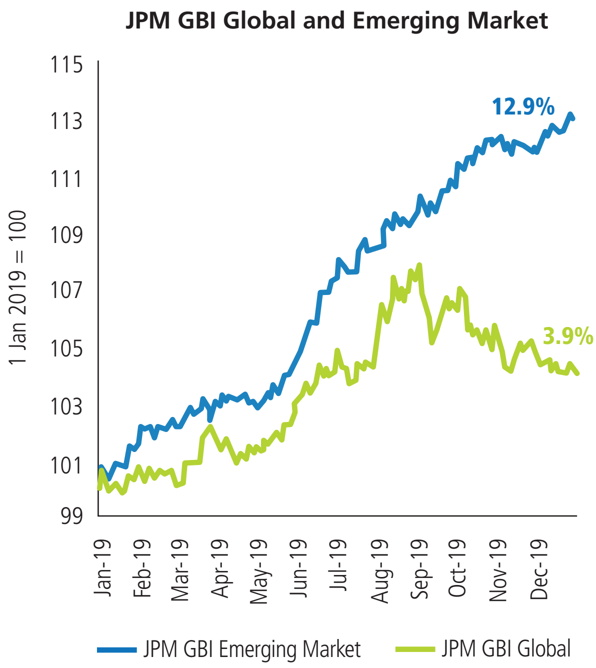
Note:
[1] JPMorgan Government Bond Index (JPM GBI) Emerging Market spread over 10-year UST.

Source: Bloomberg, Thomson Reuters Datastream, SC's calculations

Chart 6

Global equities and bonds rebounded to register positive returns in 2019 despite continued volatility throughout the year





Source: Thomson Reuters Datastream, SC's calculations

Overall, despite continued volatility throughout the year, the global capital market ended the year on a positive note, aided by relatively accommodative global financial conditions. In the equity market, the MSCI World Index ended the year 25.2% higher (2018: -10.4%) while the MSCI Emerging Markets Index rose 15.4% (2018: -16.6%). Likewise, the global bond market registered positive returns throughout the year as lower global interest rates and stronger risk aversion drove bond yields to touch multi-year lows. The JPMorgan Government Bond Index (JPM GBI) Global rose 3.9% in 2019 (2018: -1.2%) while the JPM GBI Emerging Market gained 12.9% (2018: 4.9%) (Chart 6).

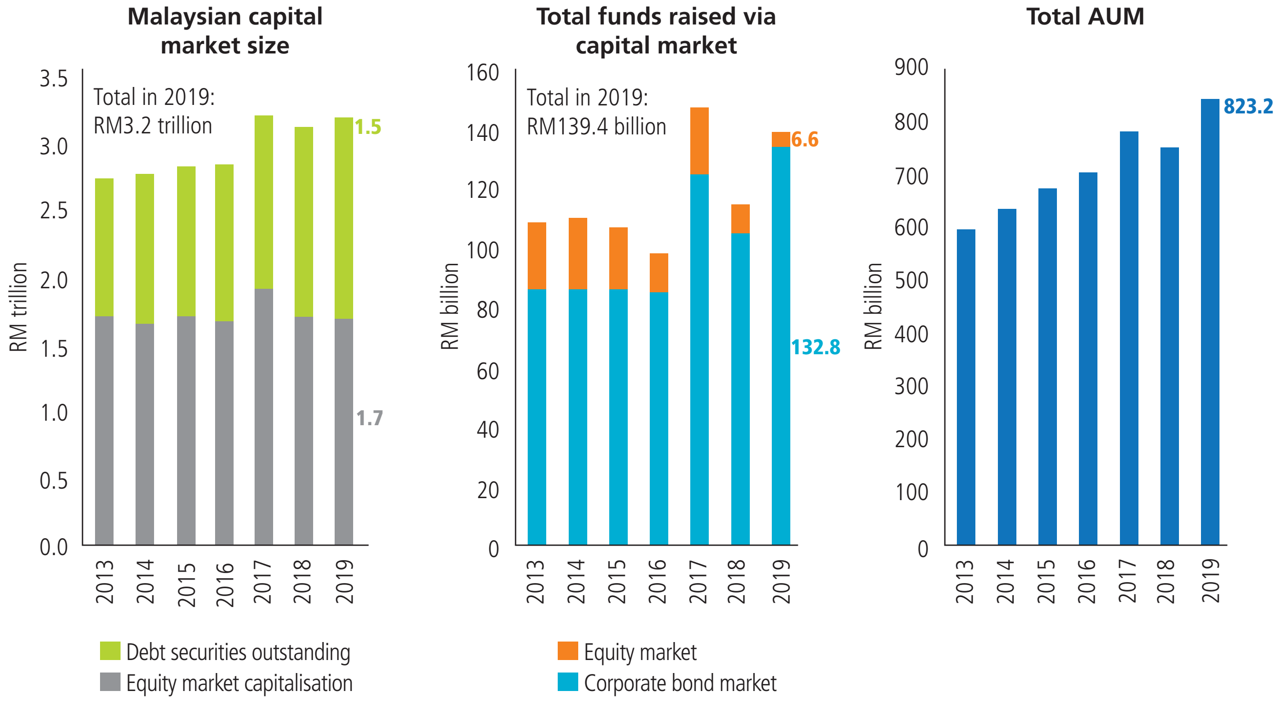
MALAYSIAN CAPITAL MARKET DEVELOPMENTS IN 2019

Despite the challenging global environment, the Malaysian economy remained on a steady growth path in 2019, underpinned by sustained resilience in domestic private sector activities. The economy grew 4.3% in 2019 (2018: 4.7%), driven primarily by robust growth in private consumption amidst continued positive labour market conditions and steady income growth. On the supply side, the economy continued to be supported by expansion in key sectors, led by manufacturing and services.

Over the year, the domestic capital market continued to play an important role in financing

Chart 7

The Malaysian capital market continued to play a vital role in financing the domestic economy and mobilising savings



Source: SC, BNM, Bursa Malaysia

the Malaysian economy. The total size of the capital market expanded to RM3.2 trillion in 2019 from RM3.1 trillion the year before (Chart 7), with debt securities outstanding and equity market capitalisation of RM1.5 trillion and RM1.7 trillion respectively (2018: RM1.4 trillion and RM1.7 trillion respectively).

Notwithstanding the challenging global backdrop and ongoing domestic policy reforms, the Malaysian capital market witnessed a higher level of fundraising activities during the year, with total funds raised in the bond and equity market amounting to RM139.4 billion in 2019 compared to RM114.6 billion in 2018. Alternative fundraising avenues have also continued to gain traction, especially in ECF and P2P financing, with total funds raised more than doubled to RM443.8 million (2018: RM195.9 million)[2].

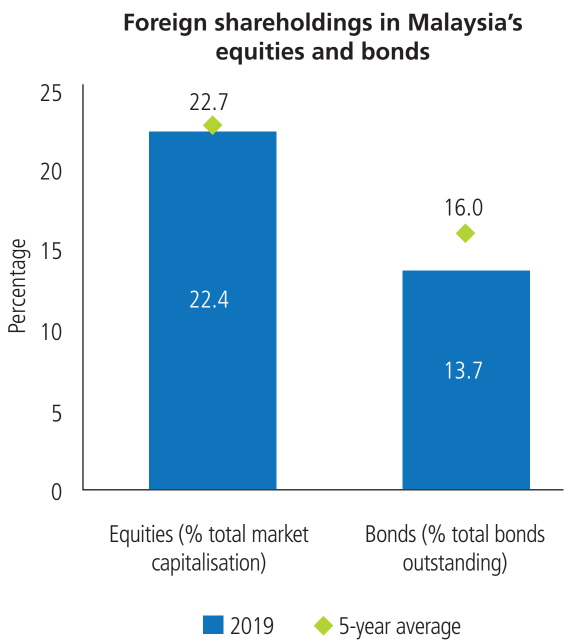
A total of RM132.8 billion was raised in the corporate bond and sukuk market[3] compared to RM105.4 billion in 2018, with issuances mainly in utilities and financial services. Sukuk made up 77.1% of total bond issuances in 2019. Meanwhile, RM6.6 billion was raised via the equity market (2018: RM9.2 billion), of which RM2.0 billion was through new equity listings with a total of 30 IPOs and RM4.6 billion raised via secondary fundraising. In 2019, four companies were listed on the Main Market, 11 companies on the ACE Market, and the

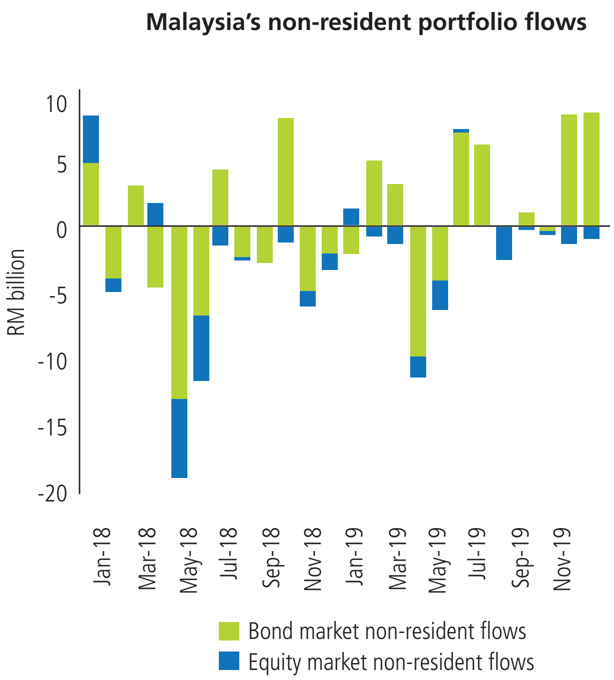
[2] Further information on ECF and P2P financing are provided in *Part 1 (Enhancing Access to the Capital Market)* and *Part 6 (Venture Capital and Private Equity) of this Annual Report.*

[3] Including sukuk issuance worth RM27.6 billion by *Urusharta Jemaah Sdn Bhd* as part of *Lembaga Tabung Haji's* (Malaysian Hajj Pilgrims Fund Board) restructuring plan in May 2019.

Chart 8

Foreign shareholdings were broadly stable while non-residents remained net-buyers of Malaysia's financial assets





Source: BNM, CEIC, SC's calculations

remaining on the LEAP Market. Notably, the size of issuances via the LEAP Market grew by 60.6% y-o-y to RM92.2 million in 2019 (2018: RM57.4 million).

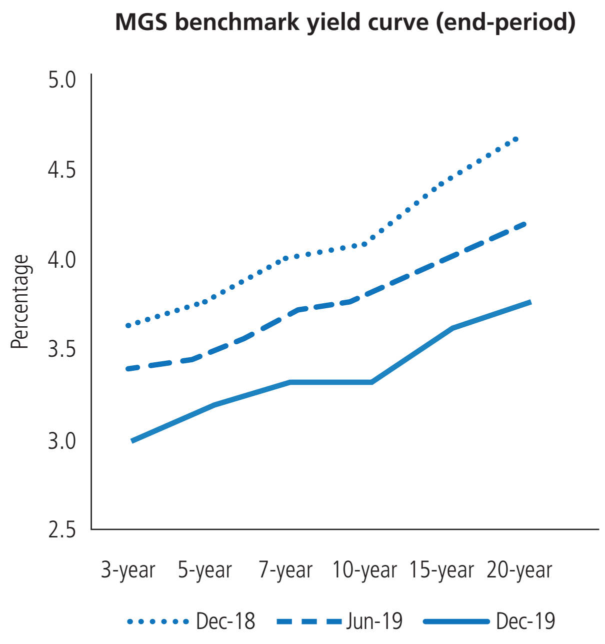
In the fund management industry, total AUM rose to RM823.2 billion (2018: RM743.6 billion) amidst an increase in market value, driven by robust performance of small and mid-cap equities and higher net injection from dividend reinvestment. Total net sales for the unit trust segment amounted to RM30.5 billion in 2019, a decrease of -19.5% y-o-y (2018: RM37.9 billion).

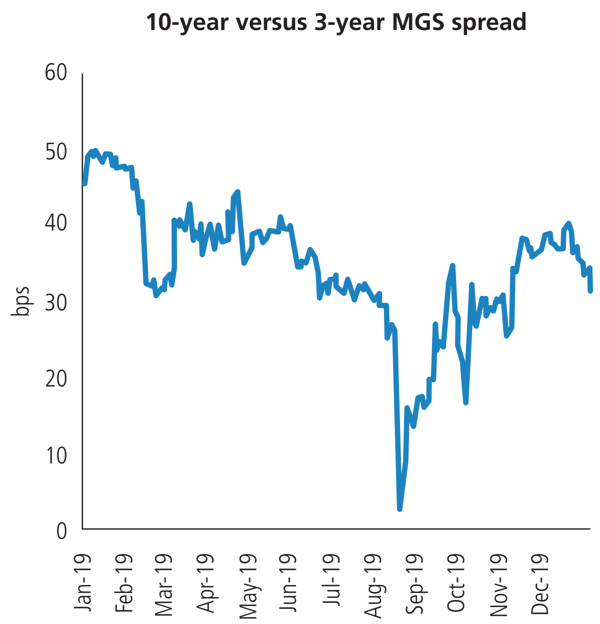
In terms of portfolio flows, total non-resident inflows amounted to RM8.7 billion in 2019 (2018: portfolio outflows of -RM33.6 billion), mirroring regional trends. The bond market recorded total inflows of RM19.9 billion (2018: outflows of -RM21.9 billion) while the equity market recorded total outflows of -RM11.1 billion (2018: outflows of -RM11.7 billion). In the bond market, non-residents accounted for 13.7% of total outstanding ringgit bonds as at end December (end-2018: 13.1%) – most of which were Malaysian Government Securities (MGS) at 80.1% of total foreign holdings (end-2018: 79.1%). In the equity market, foreign holdings remained stable at 22.4% of total market capitalisation in 2019, in line with its five-year average (Chart 8). The high level of domestic liquidity in the capital market continued to allow for orderly market adjustments of fund flows between non-residents and local investors.

The Malaysian bond market grew 7.1% from RM1.4 trillion in 2018 to RM1.5 trillion as at end 2019. This was supported by higher levels of debt fundraising, sustained demand by domestic

Chart 9

MGS yields faced downward pressure across tenures in 2019





Source: Bloomberg, SC's calculations

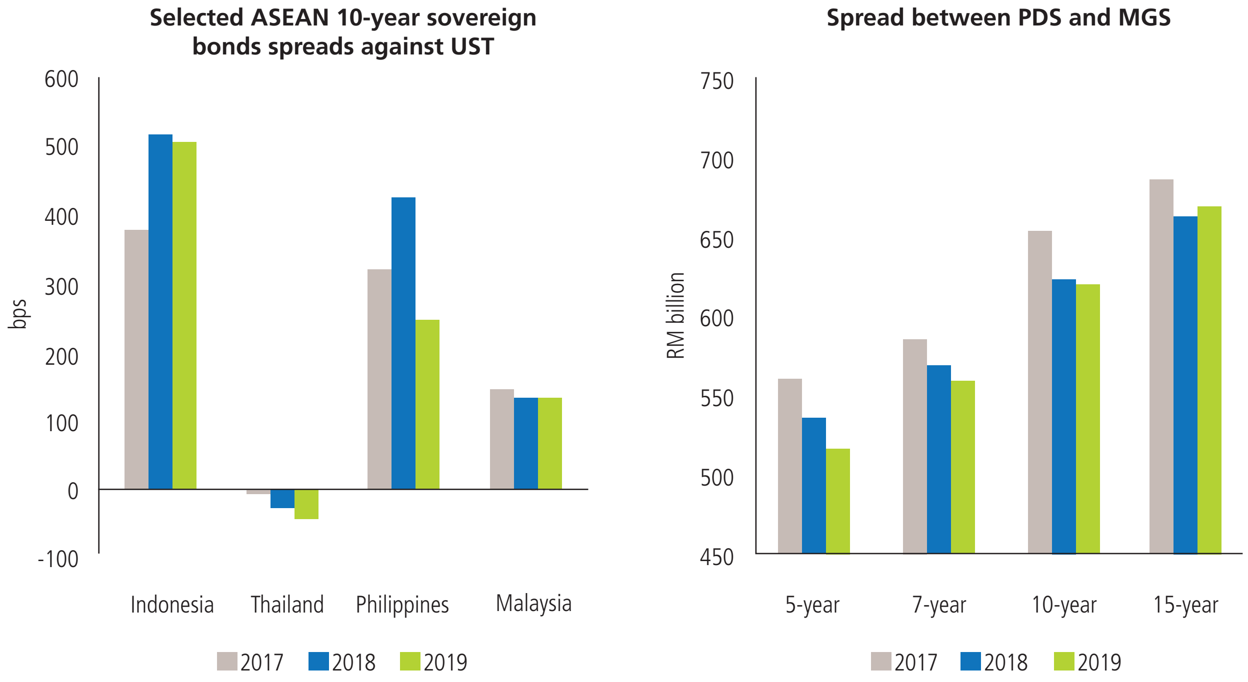
institutional investors, and favourable domestic macroeconomic conditions. Despite the challenging environment, Malaysia was also among the emerging East Asian economies that saw local currency bond markets expand in 2019. In 2019, as a percentage of GDP, Malaysia remained the third largest local currency bond market in Asia after Japan and South Korea. However, ongoing trade tensions, the shift in global monetary policy expectations, and general concern over slower global growth continued to drive volatility in the bond market throughout the year.

MGS yields experienced downward pressure across tenures (Chart 9), tracking global trends, on the back of major central banks' shift in monetary policy stance and overall higher global risk aversion. It also reflected the lower domestic growth and inflation expectations alongside the Overnight Policy Rate (OPR) cut by BNM in May 2019. As such, yields reduced across the board while the overall curve was relatively flatter for the year.

Reflecting regional trends, the 10-year UST/MGS spread remained relatively tight at 140.6 bps as at end 2019 from 140.4 bps as at end 2018 (Chart 10 – left panel). The decline in bond yields was broad-based across the ASEAN region, with the spread between the 10-year UST and 10-year local currency sovereign bonds mostly narrowing, reflecting improved global demand on regional assets. Meanwhile, spread between private debt securities (PDS) and MGS tightened throughout the year across shorter tenures, reflecting higher demand for PDS, partly driven by higher issuances on the back of a more favourable interest rate environment (Chart 10 – right panel).

Chart 10

ASEAN-UST bond spread mostly narrowed, while sentiment towards MGS and PDS remained positive



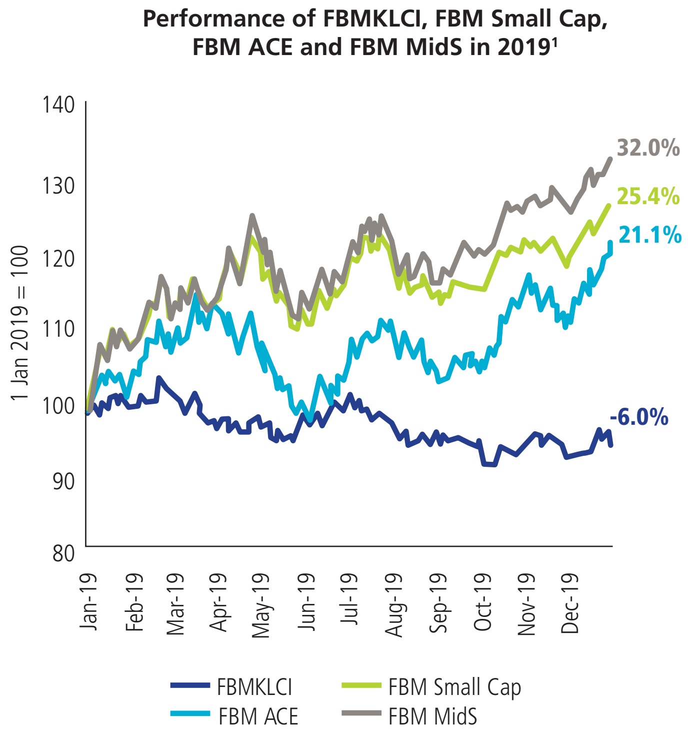
Source: Bloomberg, Thomson Reuters Datastream, BNM, BPAM, SC's calculations

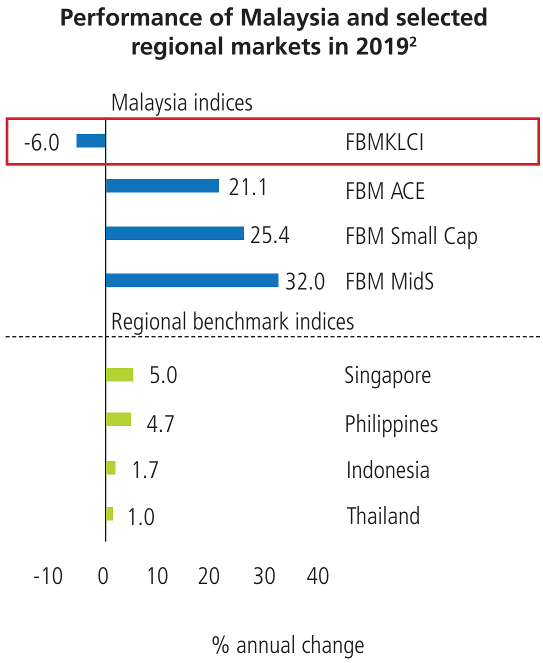
For the Malaysian equity market, overall market capitalisation ended the year marginally higher by 0.7% to RM1.71 trillion in 2019 from RM1.70 trillion in 2018. This was despite the challenging external environment with heightened headwinds mainly from the ongoing US-China trade tensions and weaker global growth. Overall, while the FBMKLCI moderated in 2019, some segments in the broader domestic equity market gained significant traction, partly reflecting a shift in investors' preference. This occurred as sentiments swayed in favour of constituents with better valuation and corporate earnings prospects, particularly in the small and mid-cap segment.

The FBMKLCI declined by -6.0% y-o-y to close the year at 1,588.76 points (2018: -5.9% y-o-y to 1,690.58 points), influenced by a year of event-driven volatility in sentiments as well as subdued corporate earnings, which continued to be a pressure point on the benchmark index. Additionally, the FBMKLCI was also weighed down by major counters subjected to key policy adjustments in 2019, aimed at longer-term improvement. Nevertheless, the non-FBMKLCI components in the Malaysian equity market performed favourably in 2019. It registered higher growth despite the challenging external headwinds, as improved earnings outlook garnered investor interest into this segment. The FBM MidS, FBM Small Cap and FBM ACE indices increased at robust double-digit rates of 32.0% y-o-y, 25.4% y-o-y, and 21.1% y-o-y respectively in 2019 (Chart 11).

Chart 11

The domestic equity market experienced positive shift in sentiment towards small and mid-cap companies





Notes:

1 FBMKLCI consists of the largest 30 companies ranked by full market capitalisation in the FTSE Bursa Malaysia EMAS Index; FBM Small Cap consists of all constituents of the FTSE Bursa Malaysia EMAS Index that are not constituents of the FTSE Bursa Malaysia Top 100 Index; FBM MidS comprises constituents from the FTSE Bursa Malaysia EMAS Index with a full market capitalisation range of RM200 million to RM2 billion; FBM ACE comprises all companies listed on the ACE Market.

2 Referenced composite indices: Philippines – PCOMP, Singapore – STI, Thailand – SET, Indonesia – JCI.

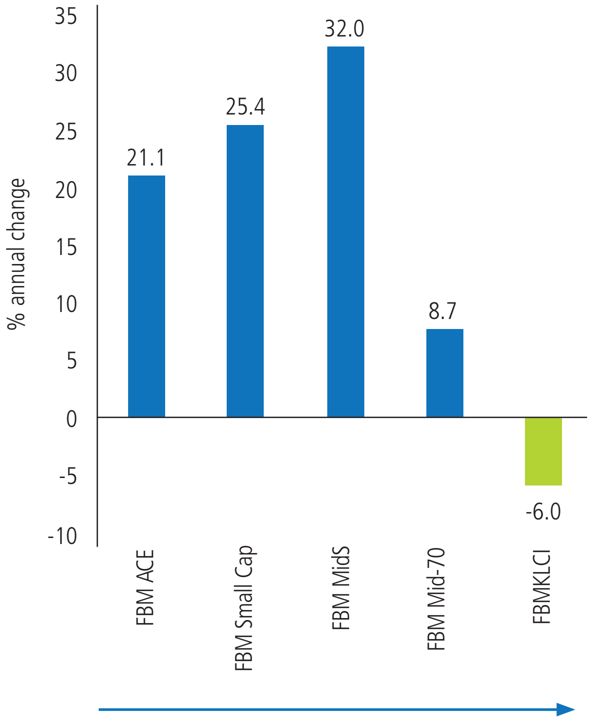
Source: Bloomberg, SC's calculations

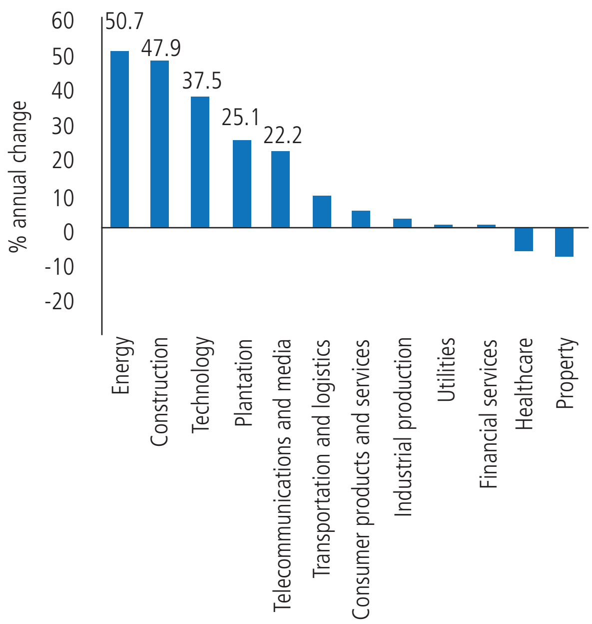
The significant growth in small and mid-cap indices was mainly driven by the energy, construction, and technology sectors, which benefitted from stronger fundamentals and better valuation prospects of their key companies during the year. Excluding the FBMKLCI components, the energy sector specifically recorded the largest increase, rising by 50.7% y-o-y (2018: -17.3% y-o-y[4]), while the construction sector increased by 47.9% y-o-y (2018: -46.0% y-o-y), owing partly to the revival of public projects by the government. The technology sector, in turn, rose by 37.5% y-o-y (2018: -9.32% y-o-y), benefitting from the 5G network rollout, higher global smartphone shipments, and potential trade diversion stemming from the ongoing US-China trade war (Chart 12).

4 Percentage change from September to December 2018, due to Bursa Malaysia's updated sectoral classification for the energy sector.

Chart 12

Energy, construction and technology sectors spearheaded the domestic equity market's performance





Notes:

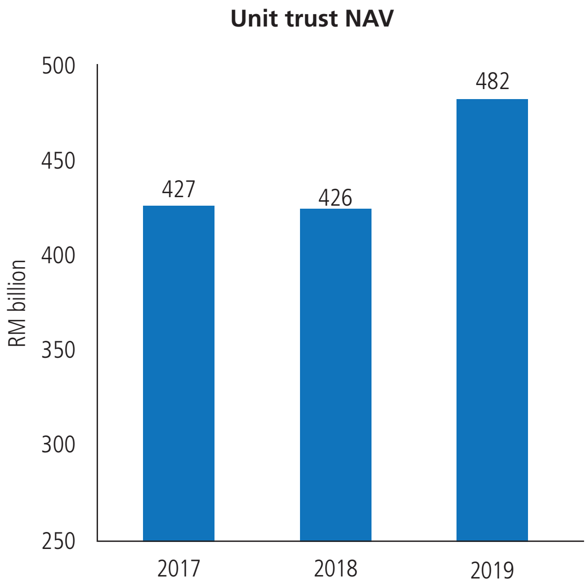
[1] FBM ACE comprises all companies listed on the ACE Market; FBM Small Cap consists of all constituents of the FTSE Bursa Malaysia EMAS Index that are not constituents of the FTSE Bursa Malaysia Top 100 Index; FBM MidS comprises constituents from the FTSE Bursa Malaysia EMAS Index with a full market capitalisation range of RM200 million to RM2 billion; FBMKLCI consists of the largest 30 companies r anked by full market capitalisation in the FTSE Bursa Malaysia EMAS Index; FBM Mid-70 consists of the next 70 companies ranked by full market capitalisation in the FTSE Bursa Malaysia EMAS Index.

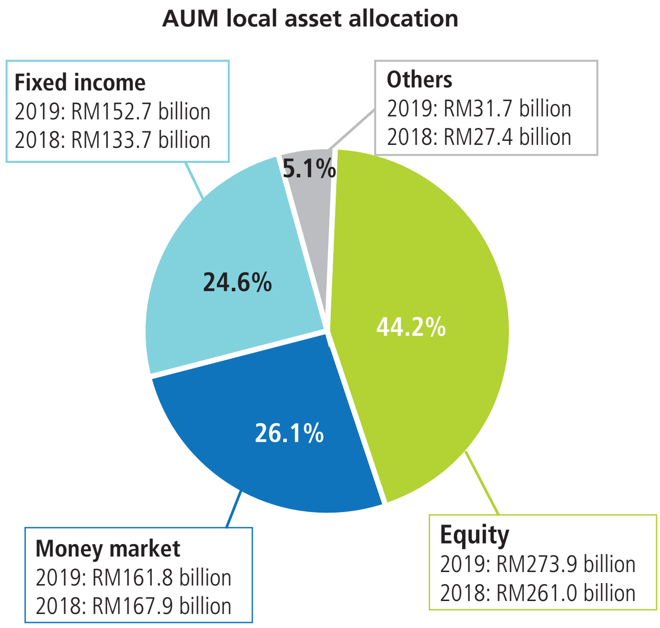
[2] Annual percentage change in market capitalisation based on sectoral classification by Bursa Malaysia as of 2019, excluding KLCI and REITs.

Source: Bursa Malaysia, Bloomberg, SC's calculations

Chart 13

Unit trust remained the largest source of funds under management, with a higher portion invested locally in 2019, mostly in local equities and fixed income assets





Source: SC's calculations

Meanwhile, in the fund management industry, the unit trust segment remained the largest source of funds towards the AUM, with net asset value (NAV) amounting to RM482.1 billion in 2019 (2018: RM426.2 billion). Overall, 75.3% of the fund management industry's AUM was invested locally, of which 44.2% was in domestic equities, followed by 26.1% in money market placements, and 24.6% in fixed income (Chart 13). Compared to 2018, investment in local equities and fixed income rose in value by RM12.9 billion and RM19.0 billion respectively, while the domestic money market placements decreased by RM6.1 billion.

Financial Development: Catalysing Economic Development in Malaysia

Economic development often entails a structural transformation of the economy from the production of low value-added goods and services towards higher value-added economic activities. An important enabler for such transformation is financial development. A well-developed financial sector provides greater opportunities for high-growth potential projects to receive financing, laying the foundation for new sources of growth in the economy to take root, develop, and scale up. Given that financial development exerts a strong influence on overall economic development, Malaysia's financial development is a key dimension to focus on in the pursuit to transform Malaysia into an advanced economy.

This box article will first explore the existing body of research studying the nexus between financial development and economic development, highlighting key insights and stylised facts or features from studies on the general impact and consequences of financial development. The article will then look into Malaysia's relative positioning in the world in terms of its financial development and contextualise Malaysia's potential as the country progresses towards advanced economy status.

Financial Development – Economic Development Nexus

The financial system is integral to the proper functioning of today's modern economy. Without such system, it would be impossible to save, invest, borrow, transact, and trade. However, its importance extends far beyond this. The financial system, by virtue of directing the flow of funds among various agents in the economy, implicitly steers the direction of economic activities and sets the trajectory of future economic potential of the country. This is reflected in two primary functions that the financial system carries out:

- **Resource allocation.** The financial system performs an intermediary role by linking funds from savers and investors with agents – households, firms, or governments – that require capital. The search for productive uses of capital dictate where these funds are ultimately channelled to, and which in turn is enabled by the financial sector via their services such as information collection, profitability assessment, as well as writing and enforcing contracts.

- **Risk and resource management.** The financial system allows agents in the economy to tailor their financial positions to suit their respective risk and investment preferences. This is performed through portfolio diversification, minimising specific or concentrated risk exposure, investment monitoring, overseeing firm behaviour as creditors or shareholders, as well as exercising corporate governance to improve the likelihood of positive outcomes from the investment.

As a country's banking system and capital market become more developed, the financial sector's capacity to allocate and manage resources also evolves, expanding the types of projects and activities that the economy is able to undertake. The interplay between the evolution of the financial sector and the types of economic activities it enables, ties together the extent of a country's financial development with the economic potential unlocked by its financial sector. From the body of research written on the nexus between financial development and economic development, three general stylised facts of this nexus emerge:

- **Stylised fact 1: Financial development fuels economic growth up to a point**
  For a developing country, financial development matters, given the important role of investment in driving economic growth (Estrada et al., 2010). However, this relationship is not linear. As financial development continues past the advanced economy stages, it could have a lower or even negative impact to growth. Factors such as rising prevalence of household credit relative to enterprise credit (Beck et al., 2012) as well as talent drain from economically productive sectors towards the financial services industry could hamper a country's economic potential (Cecchetti and Kharroubi, 2015).

- **Stylised fact 2: Financial structure shapes the nature of economic development**
  Financial structure, which is the mixture of capital market and banks operating in an economy, has an impact on the nature of economic development as it determines the way resources are channelled into investments (Xu, 2015). Banks are better at reducing market frictions related to financing standardised, lower risk, and well-collateralised projects, whereas capital markets are generally suited to finance more innovative and higher-risk projects that rely more on intangible inputs such as human capital and intellectual property. The specific blend of these two intermediation channels would funnel resources into economic activities that are best suited to the risk-reward profile of the prevalent financial structure, which in turn would help steer the trajectory of the country's economic development.

- **Stylised fact 3: Capital market development can stimulate resource allocation towards high-growth potential industries**
  As an economy advances, capital market-based development becomes even more important for economic growth (Gambacorta et al., 2014). Indeed, growth in advanced economies are generally anchored on activities that are driven by innovation and geared for export-orientation – activities that are riskier but entail higher rewards. Such activities induce structural upgrading of the economy, turning it into a knowledge-based economy that relies on high quality human capital to drive economic growth. Developments in capital markets are therefore better suited to spur these types of projects, either through direct fundraising via the capital market (Manova, 2008) or avenues for PE or VC firms to generate value (Hall and Lerner, 2010). This would unlock new forms of higher value creation potential to power future economic growth.

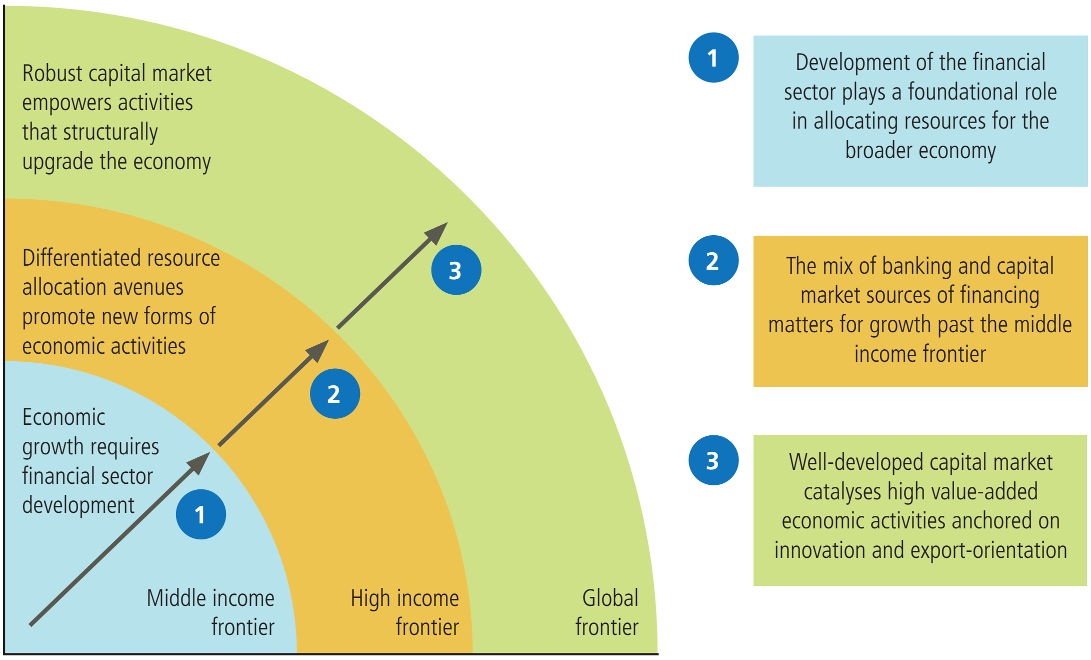
When combined, the three features illustrate how financial development induces economic development. The production possibility frontier (Figure 1) shows how different stages of financial development stimulates different forms of economic development.

Financial Development: Catalysing Economic Development in Malaysia

(Continued)

Figure 1

How financial development contributes towards a country's economic development



Visualisation based on synthesising the stylised facts from existing research exploring the financial development – economic development nexus.

Where Malaysia Stands: Contextualising the Country's Financial Development

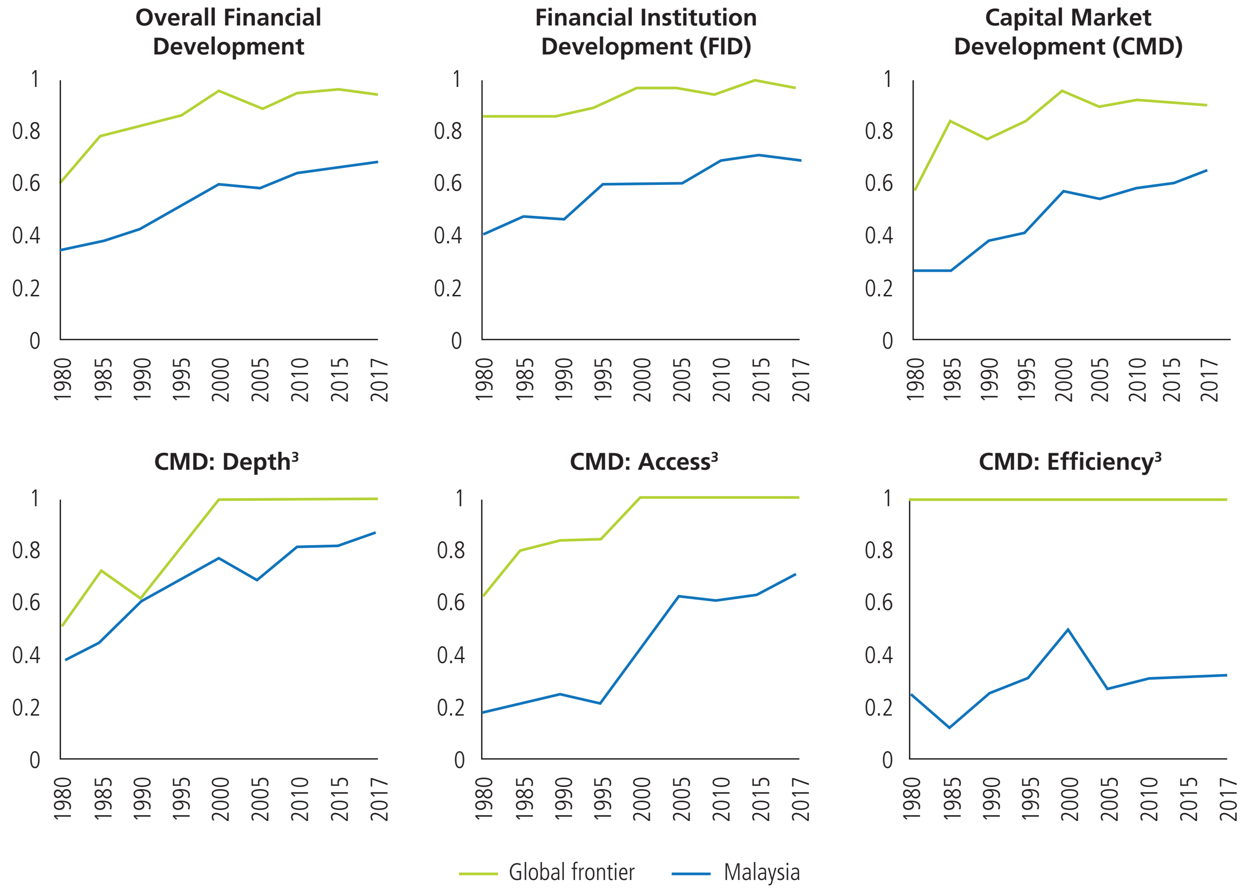
To measure a country's financial system's development, the depth, access, and efficiency of the financial system serve as important markers. Recognising the multidimensional nature of financial development, the IMF has developed indices of financial development (Svirydzenka, 2016) aimed at distilling diverse concepts and data into a composite indicator that captures the extent of the country's financial development along the three dimensions. The result is a broad-based index that illustrates how the system is structured and how well it performs its designated functions.

Cross-country comparisons of financial development between Malaysia and advanced economies provide useful insights into our positioning today *vis-à-vis* the global frontier. The financial development index measurements (Chart 1) show that Malaysia's overall financial sector development has by and large improved significantly since 1980, gradually converging with the financial development of the global frontier.

Moving forward, Malaysia stands to gain as it converges towards the frontier of capital market development. Enhancements that increase the efficiency of the capital market – such as widening the pool of investors and investible projects, developing tools that facilitate efficient price discovery for growth segments of the market, or expanding international intermediation capabilities – can improve the market's vibrancy and ability to uncover new sources of value creation in the economy. In turn, this would expand the avenues for high-growth potential economic activities such as high-tech manufacturing or modern services to receive the financing needed to develop and scale. Continuous development and improvements to Malaysia's capital market would bring about positive structural transformation for the country and unlock Malaysia's full economic potential.

Chart 1

From a long-term perspective, Malaysia's capital market (CM)[1] development is largely converging towards the global frontier[2]



Notes:
1 IMF uses the term 'Financial Market', which comprises bond and equity markets, to designate the capital market (CM). For consistency, Financial Market is referred to as CM in this article.
2 Global frontier refers to the highest ranked country for each year for any given financial development index and sub-index. All six charts plot the financial development index and sub-indices for the global frontier and Malaysia in five-year intervals.
3 The indices summarise how developed a CM is in terms of (a) depth (measures of size and liquidity of markets relative to gross domestic product (GDP)), (b) access (percent of market capitalisation outside of top 10 largest companies and total number of debt issuers), and (c) efficiency (stock market turnover ratio), all of which contribute towards the overall level of a country's financial development.

Source: IMF Financial Development Index database, 2019

Financial Development: Catalysing Economic Development in Malaysia

(Continued)

Alternative means of fundraising via private markets such as VC and PE and new digital platforms such as ECF and P2P financing solutions, also add value to the country's financial development. It supplements traditional fundraising avenues by attracting a wider pool of potential investors, expanding the universe of investible projects, and diversifying the types of activities that could receive funding. The development of these alternative investment sources also ensures that the capital market caters not only to large and established companies, but to the young and rising businesses as well. The role that the SC plays in facilitating the development of these markets is designed to foster a healthy and holistic capital market ecosystem that provides the groundwork for positive structural transformation of the Malaysian economy.

Through continuous development of the wider capital market ecosystem, the economy gains a powerful platform to cultivate firms with the potential to structurally upgrade the economy. The capital market catalyses precisely these types of investments that spur new growth opportunities for the country – ones that are capable of materialising Malaysia's potential of becoming a knowledge-based, export-driven, and high-income nation.

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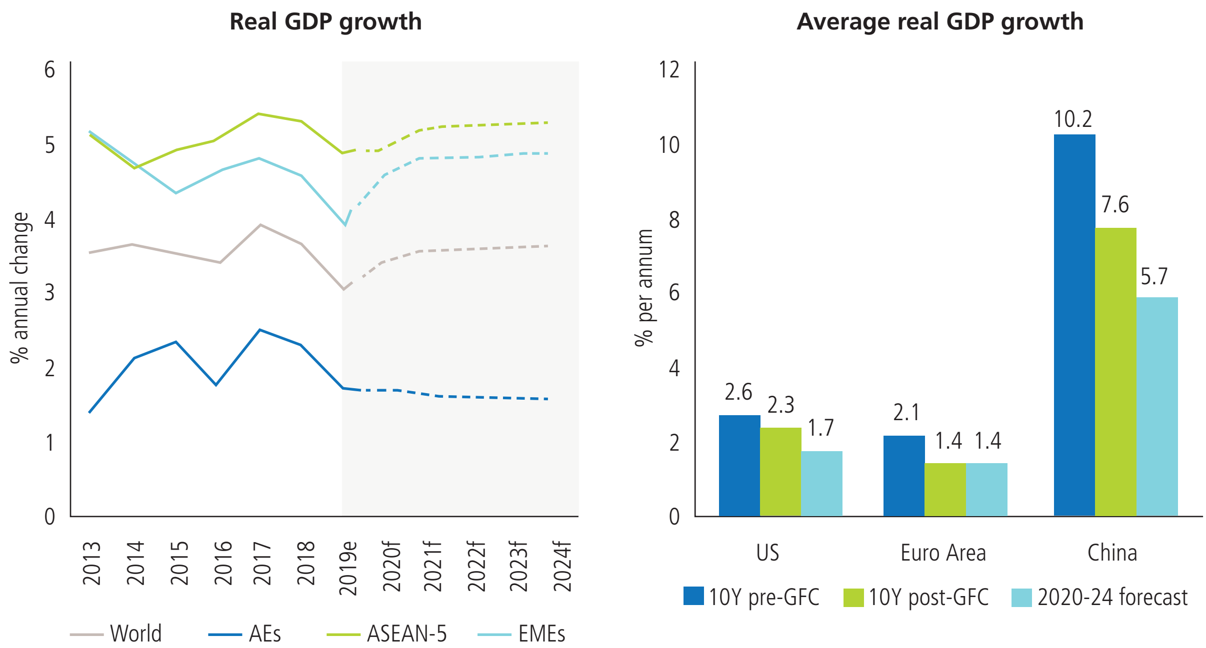
OUTLOOK FOR 2020

Growth of the global economy is projected to improve to 3.4% in 2020 from an estimated 3.0% growth in 2019[5]. This outlook, however, will continue to remain uncertain, subject to sustained de-escalation of global trade tensions following the finalisation of the phase one trade deal between US and China, as well as the expected stabilisation and rebound in activities in some EMEs. In addition, geopolitical tensions remain key risks to the outlook. Given its strong interconnectivity with the global economy, the growth outlook of the ASEAN region will be subject to downside risks, arising from prevalent global trade and policy uncertainties. Nonetheless, ASEAN is expected to remain the world's fastest growing region, underpinned by strong macroeconomic fundamentals and a supportive policy environment. In addition, deeper economic integration within the ASEAN region will continue to provide underlying support for economic growth.

Activities in the global capital market will continue to be shaped by developments in the global economy and the relatively easy global financial conditions, aided by the prospect of continued accommodative global monetary policies. Volatility, however, will likely persist, given heightened downside risks to growth. The prospect of global equities is expected to remain generally positive, underpinned by continued commitment from global policymakers to support growth.

Chart 14

Global growth to be sustained by continued expansion across major economies while ASEAN economies will remain the fastest growing region



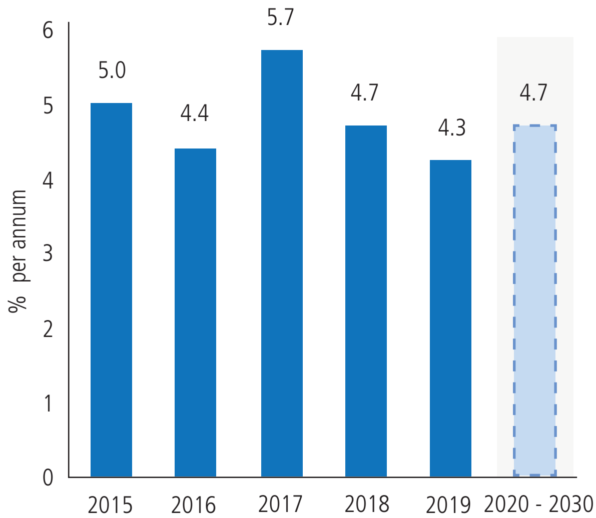
Source: IMF World Economic Outlook Database, October 2019

5 IMF World Economic Outlook, October 2019.

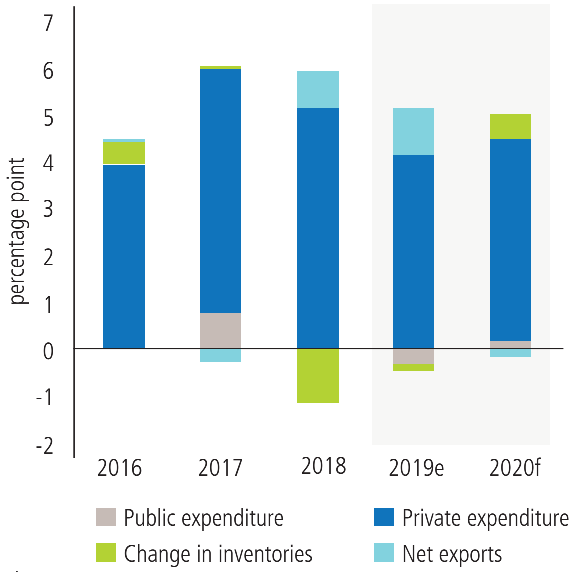
Chart 15

The Malaysian economy is expected to be driven by continued growth in private sector activities going forward

Malaysia's real GDP long-term projection[1]



Contribution to real GDP by demand components



Note:

[1] Growth in 2020-2030 is based on Malaysia's Shared Prosperity Vision 2030 projection.

Source: DOSM, Ministry of Economic Affairs, SC's calculations

Nevertheless, a prolonged period of a low-interest rate environment will likely intensify yield-seeking trends, further contributing to already stretched valuations in some equity markets. In the global bond market, performance will continue to be reflective of the overall trends in global risk aversion, with the shape of the yield curve anticipated to remain relatively flat. Meanwhile, credit spreads between EMEs and AEs are projected to remain relatively contained, given the more favourable growth outlook in the former. However, the overall performance on EMEs will be differentiated, favouring those with stronger macroeconomic fundamentals.

The Malaysian economy is expected to remain on a steady growth path, backed by firm domestic private sector activities (Chart 15). Growth will be underpinned by sustained manufacturing activities and further supported by resilient services sector expansion, especially in the wholesale and retail trade sub-sector. On the demand side, a stable labour market amidst relatively subdued inflation will continue to drive private consumption expansion, while the resumption of strategic public projects is expected to provide impetus to investment growth.

The outlook for the domestic capital market in 2020 will continue to be influenced by key global developments, with volatility driven primarily by the direction and pace of global economic growth and global monetary policy stance, and the uncertainty in relation to the ongoing trade and geopolitical tensions. In addition, the performance will also be influenced by greater clarity in ongoing domestic policy reforms. Nevertheless, the Malaysian capital market will continue to support economic growth through the financing of business expansion and infrastructure.

Overall, the domestic capital market is expected to remain resilient and orderly, underpinned by Malaysia's strong macroeconomic fundamentals, ample domestic liquidity, and supportive capital market infrastructure, which will continue to support the growth of the Malaysian economy in 2020.