Better business sentiment amid robust SME financing growth

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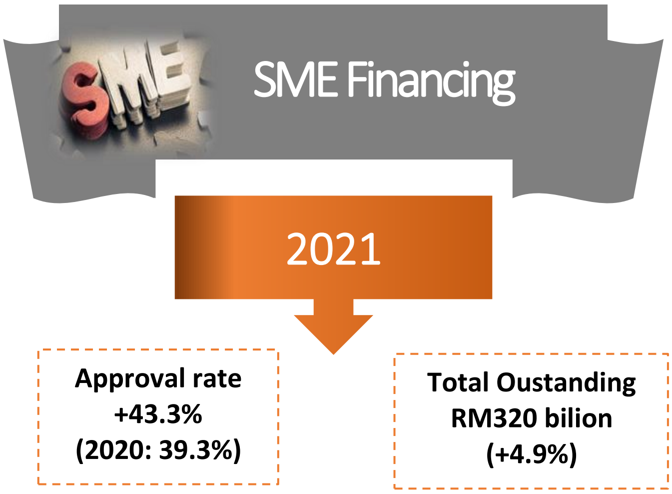
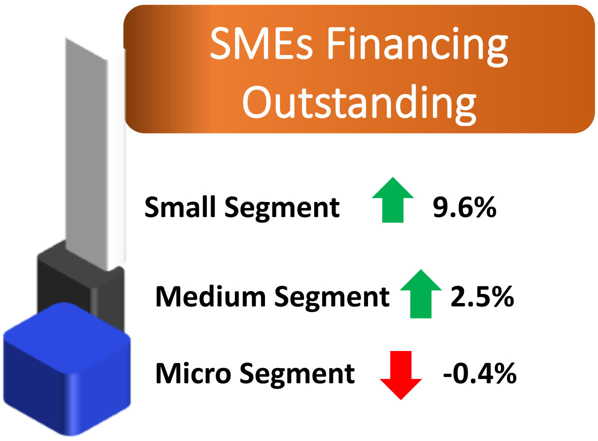
Gradual resumption of economic activities had taken place in 2021. With the accelerated rate of vaccination – 78.5% as at 1st January 2022 vs 3.4% as at 1st June 2021, the government has eased restrictions and more businesses were allowed to operate. Continued fiscal policy and accommodative financial measures has provided support to economic activity. GDP performance in 4Q 2021 was buoyed by strong private consumption due to pent-up demand.

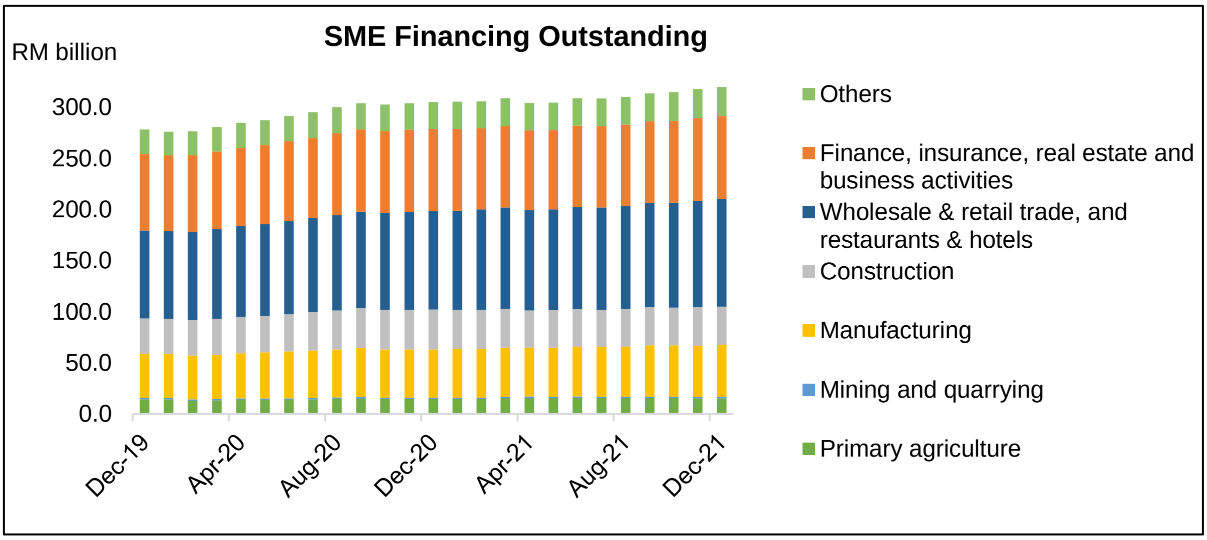


The financial industry approved more than a quarter of SME financing in 2021, with approval rates advancing to 43.3% (2020: 39.3%). The total outstanding SME financing grew 4.9% y-o-y to RM320 bil as at end-Dec 2021, the largest amount ever recorded since 2014. The rebound in economic activities in 2021 has led to **increased demand for financing related to working capital (+4%) and the purchase of landed property (+3.1%),** which collectively add to around 80% of total SME financing. Additionally, various relief funds offered by the government and Bank Negara Malaysia (BNM), about 4% of GDP in 2021, also contributed to the strong financing growth.



The **small enterprise segment** made up **close to half** of the total SME's financing outstanding and **grew by the fastest rate at 9.6%** y-o-y in December 2021. Financing extended to the medium segment increased 2.5% while the micro segment dipped 0.4%.

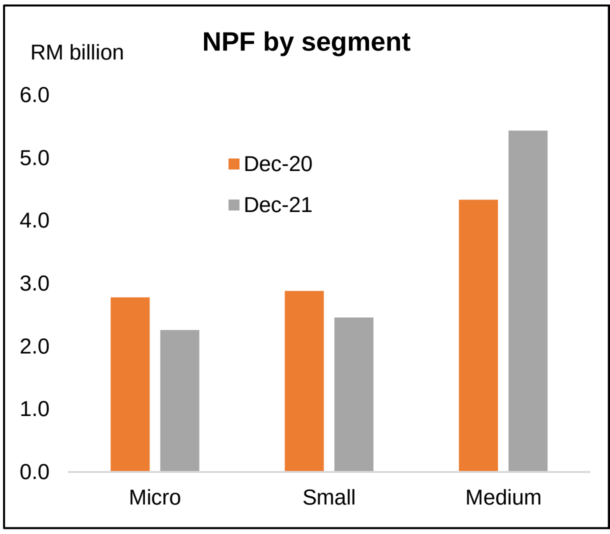
By sector, the lion's share of SME financing (67% of total) was concentrated in the Services sector, which contributed 62% to SMEs GDP. In particular, the Wholesale & Retail Trade and Finance & Insurance took the lead under the services sub-sector. This is followed by the Manufacturing (15.8%), Agriculture (4.8%) and Construction (11.8%) sectors.

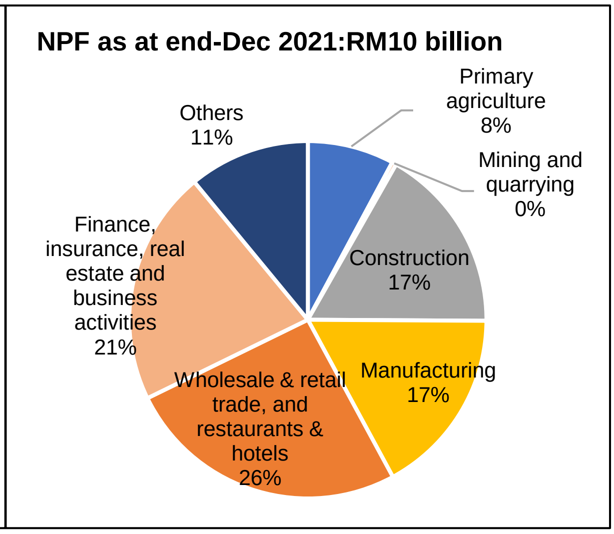


Source: BNM

In terms of SME financing application, it was up 8% m-o-m and 14.6% y-o-y in December 2021, chiefly contributed by sectors such as Finance & Insurance (+12.1% y-o-y), Wholesale & Retail trade (+13.7%), Construction (+27.1%) and Manufacturing (12.6%), reflecting SMEs' sturdier confidence towards business environment.

The SME **non-performing financing (NPF) has been steadily trending downwards since 2H 2019, before the Covid-19 pandemic**. The NPF ratio hovered within the range of 3.0%-3.5% over the last 2 years, thanks to loan moratorium programmes. Although the **medium enterprise segment** only account for **a quarter of outstanding financing**, this segment registered the **highest amount of NPF** at RM 5.4 bil as at end-December 2021 (42% of the NPF), which **suggests higher vulnerabilities** of medium sized enterprises. It is not surprising that the bulk of the industry wide SME NPF stem from the wholesale & retail and restaurant & hotels sub-sector as at the same date. Impairments may inch up following the end of moratoriums and relief assistance programmes if businesses are unable to adapt.

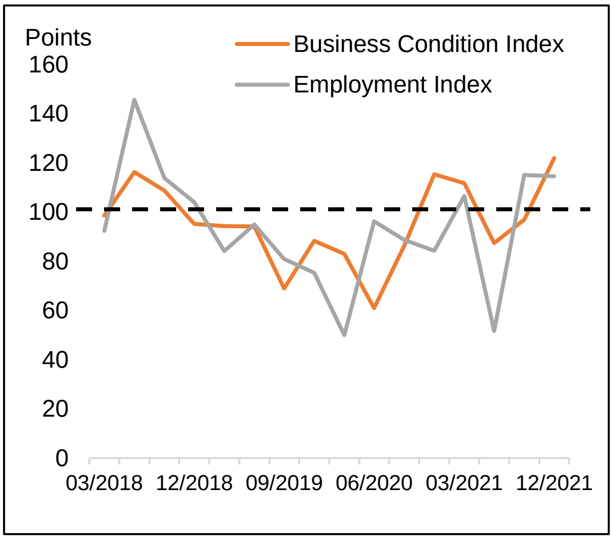


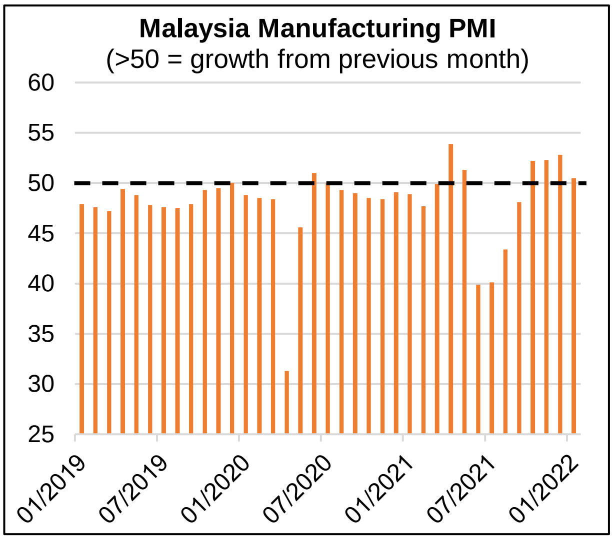


Source: BNM

Currently, a 6-month flood relief programme until mid-2022 and a 2-year Financial Management and Resilience Programme (URUS) for B50 group are still ongoing. We deem the **risk of asset quality deterioration among Malaysian banks to remain manageable** as creditors **had amassed enough provisions** to shoulder potential bad debts. Total provisions currently stand at 1.9% of total banking system loans and 130.5% of impaired loans. According to BNM's Financial Stability Review Report, the system's loan loss coverage ratio (including regulatory reserves) stood at a commendable level of 129.2% as at June 2021.

The upbeat financing data largely points towards **improvement in business sentiment on the ground**. According to the Business Confidence Index (BCI) by Malaysian Institute of Economic Research, the index rose 25 points to hit 122 points in 4Q 2021. Points above the 100-point threshold suggests that manufacturers view the economic outlook positively. In December 2021, capacity utilisation rate also reached a historical high of 88.6% (2020: 80%) as more labour force return to workplace. Lower unemployment rate and tighter labour market conditions mirror that of the global trend.





Source: *MIER, IHS Markit and SME Bank SCEA*

The uptick in the BCI was in tandem with the Purchasing Managers' Index (PMI) for the Manufacturing sector. The PMI has been clocking in above the 50-point level since Oct last year. As the global economy fully removes restrictions imposed to contain the spread of Covid-19 virus, the nation's manufacturing output is anticipated to increase this year due to strong demand, which augurs well for export-oriented companies. On the services front, recovery in tourism related industries is poised to gain traction on account of the reopening of borders to foreign tourists by May 2022 as announced.

SME Bank will launch our very own SME Sentiment Index this year. Unlike the BCI and PMI that targets solely the Manufacturing sector, our SME-centric index captures respondents that mainly span across the Services sector, with the aim to compile the SMEs' views on the business outlook. We believe it will be able to act as a forward-looking indicator to gauge the health of the economy, given that SMEs represented 97.2% of total business establishments in 2020 and 85% of which were concentrated in the services sector.

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