

Strengthening Stability in Malaysia's Financial Landscape Through Resolution Readiness

Oct 17, 2024

Dear editor,

September is a time of reflection for those in the financial industry mainly due to the Asian Financial Crisis (AFC) of 1997 and the Global Financial Crisis (GFC) of 2008. For Perbadanan Insurans Deposit Malaysia (PIDM), September is equally significant to us – it commemorates the month we were established in 2005. This year, 16 years after the GFC and in conjunction with PIDM's 19th anniversary, we revisit the reasons for our establishment and the role we continue to play in today's financial landscape.

In the aftermath of the AFC, Malaysia recognised the need for a robust financial protection system. This realisation led to the establishment of PIDM on 5 September 2005, as part of a comprehensive strategy under Bank Negara Malaysia's (BNM) Financial Sector Master Plan 2001-2010 to strengthen Malaysia's financial sector and promote financial system stability. In its early years, PIDM focused on developing internal readiness and the necessary foundational frameworks for financial consumer protection and resolution. Over time, PIDM has since evolved into focusing on building collaborative readiness in an age where risks and unpredictability have become the norm, maintaining the trust and confidence of financial consumers amidst uncertainty.

Steady Hands on the Tiller: Building Confidence and How PIDM Protects and Resolve

PIDM plays a pivotal role with its dual mandate. As a deposit insurer, PIDM protects deposits and takaful and insurance benefits, ensuring financial safety, if a member institution fails. As a resolution authority, PIDM aims to resolve a failing institution in a prompt and orderly manner while minimising potential disruption to the financial system. PIDM works closely with other financial safety net players, including BNM and the Ministry of Finance, in achieving its mandate to promote the country's financial stability.

Fore-reaching through the Storm: PIDM's Commitment to Depositor Protection During Crisis

The GFC and the collapse of Lehman Brothers in 2008 had countries worldwide implementing measures to preserve public confidence. In Malaysia, as a response to the GFC, the Government implemented the Government Deposit Guarantee (GDG) in October 2008 to provide full protection for all deposits, with PIDM entrusted to administer this critical safety net. The GDG covered all ringgit and foreign currency deposits in Malaysia. The GDG proved as a successful collaboration between PIDM, BNM and the Malaysian Government in protecting depositors and preserving public confidence during a time of global financial turmoil.

Batten Down the Hatches: Establishing Effective Resolution Regime & Resolution Planning Requirements as a Post-Crisis Imperative

Crises typically lead to the introduction of regulatory reforms by global standard-setting bodies, aimed at strengthening further the resilience of the global financial system. In particular post the GFC, there was an urgent need to address how financial institutions deemed “too big to fail” would be managed when they fail. This led to the development of frameworks and tools to ensure orderly resolution without severely impacting the financial system and needing to resort to taxpayer-funded bailouts.

In 2011, the Financial Stability Board published the Key Attributes of Effective Resolution Regimes for Financial Institutions (FSB's Key Attributes), setting the global benchmark. The FSB's Key Attributes outline the essential components of a robust resolution framework – clear legal mandates for authorities, resolution tools such as bail-in to absorb losses and cross-border cooperation between authorities during the resolution process. A significant aspect of the FSB's Key Attributes is resolution planning, which requires systemically important financial institutions to develop resolution plans (also known as “living wills”) which detail how they could be resolved during a failure.

Responding to global developments, in Malaysia, BNM and PIDM jointly developed policy frameworks for Recovery and Resolution Planning (RRP) to strengthen the crisis preparedness and resilience of Malaysian financial institutions. Recovery planning, led by BNM, ensures that banks can respond effectively to financial distress and are capable of restoring viability during times of severe stress. Resolution planning, led by PIDM, ensures that banks can be resolved in a prompt and orderly manner without severe disruption to the financial system. In September 2023, PIDM issued resolution planning requirements to its

member banks. This initiative will be implemented in phases, guided by the principle of proportionality, depending on the bank's size and complexity.

“Steady as She Goes” – Living with Readiness and Building Collaborative Resolvability

More recently, the failures of Silicon Valley Bank (SVB) and Credit Suisse (CS) in 2023 are stark reminders of the unpredictability of financial crises and the significant risks they pose, even to seemingly stable banks. (Read PIDM's Annual Report 2023 article on the Spring 2023 bank failures here: https://pidm.gov.my/pidm2022/media/assets/annualreport/Article-from-AR2023_ENG.pdf)

These events reiterate the importance of resolution planning for PIDM member banks:

1. Resolution planning means preparing in advance for a failure, minimising hurdles that may present themselves in a crisis when time is of the essence. Options are provided, giving PIDM the flexibility to deal with a failing bank promptly and in an orderly manner.
2. Resolution planning also aims to ensure banks are more resolvable in a failure through building of capabilities in good times to support an effective resolution.
3. In the case of SVB and CS, the banks or parts of them were consequently transferred to third-party purchasers. In Malaysia, resolution planning will ensure that PIDM member banks are “transfer ready”. As part of the resolution planning process, a plan will be drawn up to ensure that a failing bank can be seamlessly transferred to a credible purchaser, minimising disruptions to banking services and the broader financial system.

To achieve this, PIDM will work closely with member institutions and relevant stakeholders to foster an ecosystem where all parties are prepared to participate actively in resolution and promote a shared understanding of roles and responsibilities during a crisis. The focus will be on adopting a principle of “living with readiness,” ensuring that PIDM member institutions and stakeholders maintain continuous preparedness to deal with a crisis.

Anchors Aweigh: Sail, Not Drift

The evolution of PIDM in Malaysia, particularly with its focus on resolution planning, highlights the intentional and adaptive strategies to maintain financial stability. Since its inception, PIDM has developed and continued to enhance its crisis preparedness

framework, ensuring it remains robust, current and relevant for effective resolution and crisis response. As the Malaysian financial system continues to evolve, PIDM's proactive "just-in-case" approach will remain essential in navigating emerging challenges. In doing so, it lays a strong foundation for enduring trust in the financial system, even in times of crisis. As the saying goes, "The wind and the waves are always on the side of the ablest navigator".

Contributed by Perbadanan Insurans Deposit Malaysia.

Sent on 10 September 2024.