BANK NEGARA MALAYSIA
CENTRAL BANK OF MALAYSIA

## Statutory Requirements

In accordance with section 48 of the Central Bank of Malaysia Act 1958, Bank Negara Malaysia hereby publishes and has transmitted to the Minister of Finance a copy of this Annual Report together with a copy of its Financial Statements for the year ended 31 December 2008, which have been examined and certified by the Auditor-General. The Financial Statements will also be published in the Gazette.

For the purposes of section 115 of the Development Financial Institutions Act 2002, the annual report on the administration of the Development Financial Institutions Act 2002 and other related matters for the year ended 2008 is incorporated in Bank Negara Malaysia's Financial Stability and Payment Systems Report 2008 which forms an integral part of this Annual Report 2008.

Zeti Akhtar Aziz
Chairman
Board of Directors

25 March 2009

# Board of Directors

**Tan Sri Dato' Sri Dr. Zeti Akhtar Aziz**
D.K. (Johor), P.S.M., S.S.A.P., D.P.M.J., S.U.M.W.
Governor and Chairman

**Dato' Ooi Sang Kuang**
D.M.P.N.
Deputy Governor

**Dato' Zamani bin Abdul Ghani**
D.P.S.K., D.M.S.M., D.S.M., K.M.N.
Deputy Governor

**Dato' Mohd Razif bin Abd Kadir**
D.P.M.S., D.I.M.P., D.P.M.P.
Deputy Governor

**Tan Sri Dato' Sri Dr. Wan Abdul Aziz bin Wan Abdullah**
P.S.M., S.P.S.K., S.S.A.P., D.P.S.K., A.M.N.

**Datuk Oh Siew Nam**
P.J.N.

**Tan Sri Datuk Amar Haji Bujang bin Mohd. Nor**
P.S.M., D.A., P.N.B.S., J.S.M., J.B.S., A.M.N., P.B.J., P.P.D.(Emas)

**Dato' N. Sadasivan**
D.P.M.P., J.S.M., K.M.N.

**Tan Sri Dato' Seri Mohd Hassan Marican**
P.S.M., S.S.D.K., S.P.M.T., D.S.M.T., P.N.B.S., S.U.M.W., A.M.K.

Datuk Oh Siew Nam, Tan Sri Datuk Amar Haji Bujang bin Mohd. Nor and Dato' N. Sadasivan were reappointed as members of the Board of Directors effective 1 March 2009.

| | |
|---|---|
| Governor | Tan Sri Dr. Zeti Akhtar Aziz |
| Deputy Governor | Dato' Ooi Sang Kuang |
| Deputy Governor | Dato' Zamani bin Abdul Ghani |
| Deputy Governor | Dato' Mohd Razif bin Abd. Kadir |
| Secretary to the Board | Dato' Mohd Nor bin Mashor |
| Assistant Governor | Dato' Mohamad Daud bin Hj. Dol Moin |
| Assistant Governor | Dato' Muhammad bin Ibrahim |
| Assistant Governor | Nor Shamsiah binti Mohd Yunus |
| Assistant Governor | Dato' Mohd Nor bin Mashor |
| Assistant Governor | Lillian Leong Bee Lian |
| Assistant Governor | Gopala Krishnan Sundaram |
| Assistant Governor | Dr. Sukhdave Singh |
| Director | |
| Governor's Office | Suhaimi bin Ali |
| Corporate Communications | Abu Hassan Alshari bin Yahaya |
| Statistical Services | Chew Siew Kheam |
| Special Investigation | Sani bin Ab. Hamid |
| Internal Audit | Tan Nyat Chuan |
| Financial Intelligence | Wan Mohd Nazri bin Wan Osman @ Wan Abdullah |
| *Economics* | |
| Monetary Assessment and Strategy | Fraziali bin Ismail |
| Economics | Marzunisham bin Omar |
| International | Ismail bin Alowi |
| *Regulation* | |
| Islamic Banking and Takaful | Ahmad Hizzad bin Baharuddin |
| Financial Sector Development | S. Abd. Rasheed bin S. Abd Ghafur |
| Development Finance and Enterprise | Kamari Zaman bin Juhari |
| MIFC Promotion Unit | Shariffuddin bin Khalid |
| Prudential Financial Policy | Jessica Chew Cheng Lian |
| Financial Surveillance | Madelena binti Mohamed |
| Consumer and Market Conduct | Koid Swee Lian |
| *Supervision* | |
| Banking Supervision | Chung Chee Leong |
| Financial Conglomerates Supervision | Che Zakiah binti Che Din |
| Insurance and Takaful Supervision | Yap Lai Kuen |
| Payment Systems Policy | Cheah Kim Ling |
| DFI Supervision | Mahdi bin Mohd. Ariffin |
| *Investment and Operations* | |
| Investment Operations and Financial Market | Norzila binti Abdul Aziz |
| Currency Management and Operation | Ramli bin Saad |
| Foreign Exchange Administration | Wan Hanisah binti Wan Ibrahim |
| *Organisation Services* | |
| Human Resource Management | Mohd. Adhari bin Belal Din |
| Legal | Jeremy Lee Eng Huat |
| Human Capital Development Centre | Arlina binti Ariff |
| Corporate Services | Dato' Mohd Nor bin Mashor |
| Strategic Management | Donald Joshua Jaganathan |
| Central Banking Services | V. Vijayaledchumy |
| Finance | Abdul Aziz bin Abdul Manaf |
| IT Services | Alizah binti Ali |
| Property and Services | Zulkifli bin Abd Rahman |
| Security | Mior Mohd Zain bin Mior Mohd Tahir |
| Risk Management | Santhini a/p Chandrapal |
| Sasana and Lanai Kijang Management Office | Lim Foo Thai |
| *Head of Unit* | |
| Regulation and Supervision Administration | Siti Ramlah binti Ahmad |
| *Chief Representative* | |
| London Representative Office | Azman bin Mat Ali |
| New York Representative Office | Mohamad Ali Iqbal bin Abdul Khalid |
| *Branch Manager* | |
| Johor Bahru | Kamalullail bin Ramli |
| Kuching | Ishak bin Musa |
| Shah Alam | Mohd. Khir bin Hashim |
| Kuala Terengganu | Azizan bin Mohd Ali |
| Kota Kinabalu | Ahmad bin Abd Rahim |
| Pulau Pinang | Rosnani binti Mahamad Zain |

# Governor's Statement

BANK NEGARA MALAYSIA
CENTRAL BANK OF MALAYSIA

The global economic and financial environment in 2008 became increasingly difficult as the conditions of increased inflationary pressures arising from the sharp escalation of global fuel and commodity prices in the first half-year shifted to a rapidly deteriorating slowdown of the global economy in the second half of the year. Despite recording declines in exports and industrial production in the latter part of the year, Malaysia registered an economic growth of 4.6% in 2008 following strong growth in the first half of the year.

The global economy is expected to continue to weaken significantly in 2009, with all advanced economies experiencing sharp economic contraction. There is, at this stage, no visible sign that the global financial crisis has abated. Delays in addressing the financial sector problems in several of the advanced economies have increased the prospect of a more protracted and deeper economic downturn. The experience from the Asian financial crisis more than a decade ago suggests that the financial sector resolution measures would need to be comprehensive to restore financial system stability. The restoration of the financial intermediation process and a resumption in lending activity are vital elements for economic recovery. While a number of stimulus measures are being undertaken across the globe to counter the effects of the economic downturn, the full impact of these measures will require time to take effect.

The significant deterioration in the advanced economies, particularly the collapse in private sector activity, has contributed to a substantial weakening of global trade and investment flows. Asia, with its strong international trade and investment linkages, has been adversely affected. A number of economies in Asia are already in recession, while others are experiencing a sharp moderation in growth. The relatively strong financial systems and the extensive monetary and fiscal policy responses instituted by the regional economies are, however, expected to contribute towards partially mitigating the impact of the global economic slowdown on this part of the world.

The year 2009 will be a highly challenging year for the Malaysian economy. While the domestic economy has been affected by the adverse global developments since the second half of 2008, it is expected that the Malaysian economy will experience the full impact of the global recession in 2009. Taking into account the full implementation of the measures to support domestic demand, the GDP performance in 2009 in real terms is projected to be between -1% to 1%. This outlook is dependent on stability being restored in the crisis-affected economies in the second half of the year. It will essentially depend on the effective implementation of the announced resolution and stimulus measures. Should the financial sector problems globally remain unresolved, conditions can be expected to continue to deteriorate.

For the domestic economy, the increased capacity for domestic demand, which has been built up over several years, has the potential to remain positive going forward. In addition, the high degree of economic diversification, in terms of exports and markets, and in the increased range of domestic-oriented activities, is another key element that will contribute towards growth. These trends need to be developed and further reinforced, including our trade with the other emerging economies especially in Asia. Under these circumstances, the strategy is to provide support to domestic demand in order to mitigate the severity of the economic downturn. Two factors are important in supporting domestic demand. Firstly, to ensure that the monetary and financing conditions are supportive of domestic demand. Secondly, is the role of fiscal policy to support domestic demand and to place Malaysia in the position to resume growth once conditions in the global economy stabilise.

The monetary policy response has been forward-looking in this environment of shifting challenges. An accommodative monetary environment was already maintained in the first part of 2008 despite the rise in supply-driven inflationary pressures. The balance of risks to both growth and inflation had become more acute and elevated when inflation surged due to the significant adjustment to fuel prices in June 2008, resulting in a deflationary shock to the economy. It was assessed, however, that in the latter part of 2008 the balance of risks would shift from higher inflation to slower growth. Indeed, headline inflation has continued to moderate, from the peak of 8.5% in July 2008 to less than 4% by the beginning of 2009. This downward trend is expected to continue, with inflation now projected to slow significantly to an average of less than 2% in 2009. With the risk that growth would decelerate more significantly with the deteriorating global environment, monetary policy action was frontloaded. Since November 2008, the Overnight Policy Rate (OPR) has been lowered by 150 basis points to 2% and the Statutory Reserve Requirement was lowered by 3 percentage points to reduce further the cost of intermediation.

Moving forward, the focus of attention will be to ensure the continued access to financing. The strong domestic banking system, with its ample liquidity, has been important in ensuring that the access to financing remains uninterrupted. Several measures have been introduced to further enhance access to financing for all economic sectors. These include the establishment of special funds, financing guarantee facilities for businesses, adequate liquidity including the availability of US dollars for trade financing, and the establishment of the Financial Guarantee Institution to provide credit enhancement to companies for fund-raising in the domestic bond market.

In a highly uncertain global economic environment and volatile international financial markets, the flexible exchange rate regime has enabled Malaysia to adjust to and absorb these international developments, while according broad stability against our main trading partners. The exchange rate represents an important price in a highly open economy such as Malaysia. An excessively volatile exchange rate would have significant disruptive impact on international trade and investment. The policy of the Bank would be to continue to maintain orderly conditions in the ringgit foreign exchange market to facilitate international trade and investment. While the exchange rate in the current environment has been largely influenced by capital flows, it is well supported by a strong external position.

The current crisis has highlighted the benefits and importance of raising the level of regional cooperation, particularly in undertaking joint-surveillance of the developments in the region and putting in place mechanisms for crisis management among central banks in the region. Such collaborative efforts have been extensive. The establishment of an integrated regional monitoring mechanism, undertaking vigilant risk management functions, and the setting up of an integrated crisis management and crisis resolution mechanism under the aegis of the Executives' Meeting of East Asia Pacific Central Banks (EMEAP) Monetary and Financial Stability

Committee, are important developments that have taken place. Steps are also being taken to enhance the liquidity support mechanism in the Chiang Mai Initiative by moving towards multilateralisation that would enable an effective pooling and utilisation of liquidity support among member countries. In addition, bilateral arrangements have taken place within the region. Bank Negara Malaysia and the People's Bank of China entered into a bilateral currency swap arrangement to promote bilateral trade and investment early this year.

Bank Negara Malaysia marks 50 years of central banking this year. We can look back with pride at our contribution to maintaining monetary and financial stability and to the development of a comprehensive financial system in the nation. This has also involved the modernisation of the Bank to ensure that we remain effective in a rapidly changing environment. In 2008, continuous efforts were directed towards transforming the Bank into a more strategy-focussed and performance-based organisation. This year saw the development of a 3-year Business Plan encapsulating the Bank's key priorities, strategic results to be achieved and the effective alignment of our resources for this purpose. In the area of talent management, focus continues to be given to the development of the talent pipeline for leadership succession and to the management of performance.

As part of the modernisation of the Bank, a new Central Bank of Malaysia Act will be tabled to the Parliament this year. The proposed Act involves a comprehensive review of the Bank's mandate, governance, accountability and the legislative framework to ensure that the Bank remains effective in performing its functions. The proposed Act aims to provide greater clarity to the existing roles and functions of the Bank and will entrust the Bank with the necessary powers and instruments to perform the Bank's roles and functions effectively. The proposed Act will further institutionalise many of the practices that have been introduced in this recent decade. In addition, the governance framework of the Bank would be strengthened through the proposed Act to enhance accountability, professionalism and transparency.

The experience over 50 years in preserving monetary and financial stability and in supporting the sustainability of economic development has seen many challenges, with many lessons learnt. The year 2009 presents another highly challenging year that would place greater demands on the readiness, capacity and capabilities of the Bank to sustain the welfare of the nation through these difficult times. In the tradition of the strength of our resolve, the Bank will remain focussed in the pursuit of these goals.

**Zeti Akhtar Aziz**
**Governor**

25 March 2009

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## Economic Developments in 2008

# Economic Developments in 2008

## THE INTERNATIONAL ECONOMIC ENVIRONMENT IN 2008

The global economy was characterised by two distinct periods in 2008. In the first half year, economies across the world were facing intense inflationary pressures amidst sharp increases in prices of oil, food and other commodities. This, however, gave way to concerns over the intensification and spread of turmoil in the international financial markets and their contractionary impact on economic growth. The global economy sustained its growth in the first half of 2008, largely due to the strong performance of the emerging economies, while the advanced economies, particularly the United States (US), experienced a moderation in growth. The emerging and developing economies continued to sustain the global growth momentum in the first half, led by PR China and India. The deterioration of the financial problems in the advanced economies initially caused investment funds to shift out of mortgage securities and equities to commodities, contributing to record high prices of oil and other commodities by the middle of the year. This subsequently resulted in increased cost-push inflationary pressures globally.

**The global economy experienced a reversal from inflationary concerns in the first half of 2008 to the sharp deterioration in growth in the second half following an intensification of the global financial crisis**

Global economic conditions, however, experienced a major reversal in the second half of 2008, as the financial crisis developed into a systemic failure of the financial system. Concerns over inflationary pressures that prevailed in the first half shifted rapidly towards the threat of economic contraction as the intensification of the global financial turmoil and the ensuing credit crunch led the advanced economies into a synchronised recession. The spillover effects on the emerging economies were evident towards the end of the year. The more open economies in Asia experienced export-led recessions, while growth in the other economies moderated sharply. The sharp deterioration in global financial and economic conditions precipitated a rapid correction in commodity prices, and together with rapidly contracting demand conditions, resulted in large reduction in inflationary pressures sweeping across the global economy.

**Table 1.1**
**World Economy: Key Economic Indicators**

| | Real GDP Growth (%) | | Inflation (%) | |
|---|---|---|---|---|
| | 2007 | 2008e | 2007 | 2008e |
| **World Growth** | **5.2** | **3.4** | – | – |
| **World Trade** | **7.2** | **4.1** | – | – |
| **Major Advanced Economies** | | | | |
| United States | 2.0 | 1.1 | 2.9 | 3.8 |
| Japan | 2.4 | -0.6 | 0.0 | 1.4 |
| Euro Area | 2.4 | 0.8 | 2.1 | 3.3 |
| United Kingdom | 3.0 | 0.7 | 2.3 | 3.6 |
| **East Asia** | **10.0** | **6.5** | **4.1** | **6.0** |
| **Asian NIEs[1]** | **5.6** | **1.7** | **2.2** | **4.5** |
| Korea | 5.0 | 2.5 | 2.5 | 4.7 |
| Chinese Taipei | 5.7 | 0.1 | 1.8 | 3.5 |
| Singapore | 7.8 | 1.1 | 2.1 | 6.5 |
| Hong Kong SAR[2] | 6.4 | 2.5 | 2.0 | 4.3 |
| **The People's Republic of China** | **13.0** | **9.0** | **4.8** | **5.9** |
| **ASEAN[3]** | **6.2** | **4.4** | **3.8** | **7.9** |
| Malaysia | 6.3 | 4.6 | 2.0 | 5.4 |
| Thailand | 4.9 | 2.6 | 2.3 | 5.5 |
| Indonesia | 6.3 | 6.1 | 6.3 | 10.2 |
| Philippines | 7.2 | 4.6 | 2.8 | 9.3 |
| India[4,5] | 9.1 | 7.0 | 4.6 | 3.0 |

1 Newly Industrialised Asian Economies
2 Inflation refers to composite price index
3 Includes Singapore
4 Real GDP growth refers to fiscal year
5 Inflation refers to wholesale price index
e Estimate

Source: International Monetary Fund, National Authorities & BNM estimates

The financial problems of US financial institutions arising from deteriorating sub-prime assets as the housing bubble burst in mid-2007, escalated into a major and severe international systemic financial crisis by late 2008. What started as a problem in the US financial system rapidly developed into a global financial crisis as it spread swiftly across all segments of financial markets in the advanced economies and rapidly to the emerging economies. In the early stages of the crisis, the primary focus of the authorities in the large advanced economies was to address liquidity problems in the financial system. However, the failure of a number of systemically large US financial institutions in September 2008 triggered widespread loss of confidence across the global financial markets leading to the breakdown and dysfunctioning of the interbank and credit markets in the advanced economies. Credit spreads increased to abnormal levels and liquidity dried up across most markets in the financial system, resulting in funding difficulties and the rapid collapse in values of financial assets. This threatened the solvency of many large financial institutions. In response, governments in the advanced economies intervened to inject massive quantities of liquidity and capital to strengthen the balance sheets of the large financial institutions. At the same time, major efforts were made to restore the functioning of credit markets through aggressive direct purchase of a range of financial papers and guarantee schemes. At the international level, massive currency swap arrangements between the Federal Reserve and a number of major central banks in the world were undertaken to ease the tightening global US dollar liquidity.

Despite the unprecedented large and aggressive financial measures taken by the authorities to address the financial meltdown, financial markets remained highly volatile and the credit markets dysfunctional. The deepening crisis in the financial markets has subsequently spilled over into the real economy, as the credit crunch and declining asset values contributed to the rapid and sharp contraction in real economic activities. The global stock market capitalisation has declined by 45% to USD29 trillion in 2008 (end-2007: USD53 trillion). The huge wealth destruction, equivalent to 44% of the world's GDP, has severely undermined consumer spending and the ability of the corporate sector to raise capital or refinance their existing borrowings. Consumer and business confidence in the advanced economies deteriorated rapidly following the weakening economic prospects, impaired balance sheets and difficulties in obtaining access to financing. This has exerted further pressure on the balance sheets of financial institutions as non-performing loans increased. To contain the sharp contraction in economic activity and the negative feedback loop between the financial system and the real economy, the authorities in several countries responded with large fiscal stimulus packages and aggressive monetary easing and quantitative injections of liquidity directly into illiquid financial markets.

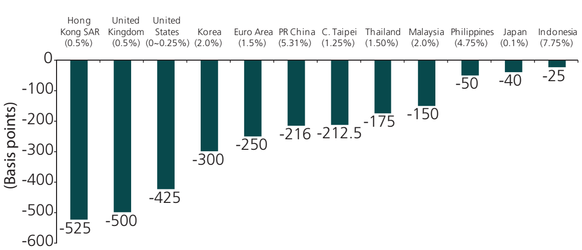
In the **US**, despite the emerging negative impact from the financial sector problems, real GDP recorded a better-than-expected growth of 2.3% in the first half of the year, lifted by the temporary boost from the USD168 billion fiscal stimulus introduced in February 2008. Nevertheless, there were increasing signs of rising stress in the US financial system, leading to a major US investment bank to fail in March. The Federal Reserve (the Fed) moved aggressively to ease the federal funds rate to 2% by April, and at the same time introduced deposit and lending facilities to manage the growing erosion of confidence in the financial system. However, in the second half of the year, as the financial turmoil intensified and spread, the contractionary impact on the real economy accelerated in magnitude, leading growth in real GDP to be flat in the second half of the year, bringing the overall growth to 1.1% for 2008. Consumer sentiment was severely affected by deteriorating housing and equity prices as well as large job losses of 3.1 million. Sharp declines in house prices, together with declining equity markets, led to an estimated wealth loss of about USD11.2 trillion for households, resulting in further cuts in household borrowings and spending. The decline in investment, initially in residential investment, accelerated in the second half of the year as non-residential investment also suffered its first decline due to falling demand and profits, and tight financing conditions. In response, the Fed cut its federal funds rate aggressively by another 175 to 200 basis points to 0 – 0.25% by December. The Fed also resorted to quantitative easing in an attempt to revive the credit markets. In addition, the US Treasury introduced the USD700 billion Troubled Asset Relief Program (TARP) to recapitalise troubled financial institutions and provide liquidity support to revive the markets for a number of important financial instruments.

In the other advanced economies, economic growth moderated in the first half of 2008 after expanding above potential for two years. However, the other advanced economies followed the US into a synchronised recession in the second half as the financial turmoil escalated further. Growth in the **euro area** also moderated in the first half, reflecting the impact of slower exports on the German economy and the negative influence arising from the bursting of the housing bubble in other euro area economies such as Spain and Ireland. Inflation, which averaged 3.5% in the first half, was a major reason underpinning the European Central Bank's (ECB) decision to raise its policy rate by 25 basis points to 4.25% in July as commodity prices continued to rise. However, the euro area experienced its third consecutive quarter-on-quarter decline in the fourth quarter, confirming that the region was in recession despite registering anaemic growth of 0.8% for the year as a whole. The European banking institutions were also adversely affected by their exposure to sub-prime credit and derivative products. With significantly weaker balance sheets, there was a pullback in credit to the real economy, thus impacting domestic demand. In response, the ECB cut its key rate to 2.5% by December and took measures to restore the functioning of the interbank market. The four largest euro area member countries, Germany, France, Italy and Spain, also introduced fiscal stimulus, ranging from 1.3% to 5.2% of GDP, to support the real economy.

Meanwhile, in the **United Kingdom** (UK), real GDP slowed in the first half following weakness in the construction as well as the business and financial services sectors. Despite inflation edging upwards on higher commodity prices, the Bank of England (BOE) eased its base lending rate gradually from February 2008 in response to the emerging weakness in the financial sector as financial institutions were hit by the rising mortgage defaults from the burst of the bubble in the housing market. In the second half, real GDP declined by 0.8% as the housing bust and credit crunch led to the failure of one of the largest mortgage lenders in September 2008 and the freezing of credit channels by the banking system. The credit crisis led to a weaker domestic demand as households and firms had difficulties in securing financing. In response, the BOE reduced its key rate to 2% by end-2008, its lowest level since 1951, while the Government implemented two bank rescue packages to resuscitate the vulnerable financial system. In addition, the Government announced a fiscal stimulus package amounting to 1.6% of GDP to mitigate the impact on the real economy.

In the first half of 2008, positive contribution from net exports and private consumption, supported **Japan's** growth of 1%. The Bank of Japan (BOJ) maintained its overnight call rate at 0.5% even as inflation reached its highest rate of 2.3% in a decade. However, real GDP contracted in the second half, bringing growth for the year to -0.6% as the economy entered into a recession following the sharp deterioration in exports. The BOJ responded by

**Chart 1.1**
**Cumulative Movements of Policy Rates since 2008**




Note: Current policy rates in parentheses, as at mid-March 2009

Source: National Authorities

**Table 1.2**
**Fiscal Stimulus in Selected Economies**

| | Amount (USD bn) | % of GDP |
|---|---|---|
| **Advanced Economies** | | |
| United States | 787 | 5.5 |
| Euro Area[1] | 271 | 2.3 |
| United Kingdom | 31 | 1.6 |
| Japan | 116 | 2.4 |
| **Regional Economies** | | |
| The People's Republic of China | 586 | 13.3 |
| Singapore | 13.7 | 8.0 |
| Chinese Taipei | 24.3 | 6.2 |
| Philippines | 6.3 | 4.0 |
| Thailand | 10.0 | 3.3 |
| Indonesia | 6.1 | 1.5 |
| Korea | 15.0 | 2.3 |
| Malaysia | 18.1 | 9.5 |
| Hong Kong SAR | 1.4 | 0.7 |

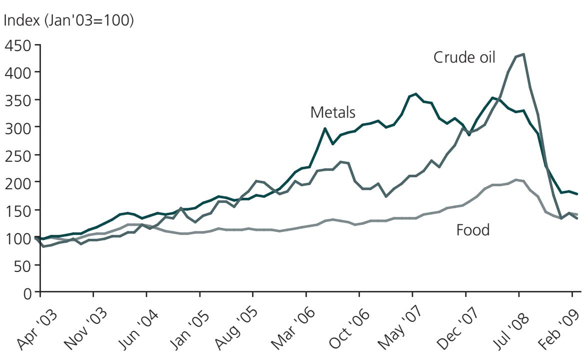
[1] Refers to Germany, France, Italy & Spain

Note: As at mid-March 2009

Source: National Authorities, Bank Negara Malaysia estimates reducing its key rate to 0.1% while the Government unveiled a series of fiscal and financial packages to stabilise the financial sector and mitigate the impact on the real sector.

In the **Asian region**, growth remained strong in the first half, supported by resilient domestic demand and continued favourable export performance, particularly to the non-US markets and growth of intra-regional trade. Notably, **PR China** continued to expand strongly by 10.4% during the first half of the year following robust domestic demand and export performance. Commodity-exporting economies benefited significantly from the substantial improvement in terms-of-trade as a result of higher commodity prices. In response to the rising domestic headline inflation, a number of authorities in the region tightened monetary policy while introducing fiscal measures, including increasing subsidies, tax rebates as well as reducing utility bills and import tariffs, to mitigate the impact of increasing food and fuel prices on the public. As the financial and economic conditions in the advanced economies deteriorated sharply in the second half of 2008, the spillover effects began to be felt by the Asian economies. Exports of the regional economies experienced sharp contractions and industrial production declined towards the end of the year. The commodity-exporting economies were also affected by the sharp declines in commodity prices. While the region's banking system remains healthy, the global deleveraging process and deepening recession in the advanced countries led to declines in the regional equity markets, large outflows of portfolio capital and a weakening of the regional currencies against the US dollar. Foreign direct investment also slowed considerably. Under these circumstances, the region's overall growth moderated sharply in the second half of the year. The newly-industrialised Asian economies (NIEs) as a group entered into recession, while PR China recorded its lowest quarterly growth since 2001 in the fourth quarter of 2008.

**Chart 1.2**
**Key Commodity Prices**




Source: International Monetary Fund

**Global inflation** was on an uptrend in the first half of 2008, driven by sharp increases in prices of food, oil and a broad spectrum of commodities. Between January and July, the price of crude oil increased by about 50% to a record high of USD147 per barrel. The rise in commodity prices was largely due to the buying by institutional funds, reinforced by the underlying strong robust demand from the large emerging economies. Supply constraints, including the diversion of certain food crops towards bio-fuel production added to the uptrend in prices. However, in the second half, the deepening financial crisis which resulted in a shift of funds out of the commodity markets as well as the adverse economic developments in the advanced economies, led to a rapid and sharp correction of commodity prices. Notably, crude oil price dropped by about 70% from its peak to USD44 at the end of 2008. Similarly, prices of other commodities and food items also declined by varying degrees, in tandem with the decline in oil prices. As demand conditions weakened and commodity prices declined, inflationary pressures eased significantly across countries towards the end of 2008.

In the **foreign exchange markets**, the US dollar started the year on a weaker note, depreciating against most currencies, influenced mainly by prospects of a greater economic slowdown in the US and interest rate cuts by the Fed. The US dollar was relatively stable from April to July on anticipation that the aggressive monetary easing in the US would support the recovery process. However, from July onwards, the US dollar began to appreciate sharply against most currencies with the exception of the yen, amidst broad-based global deleveraging by financial institutions and investors, leading to large liquidations of their exposure in Asian equities and bonds, and from high-yielding markets such as in Australia and New Zealand. Both the pound sterling and the euro weakened against the US dollar as the financial turmoil in the US spread to Europe, leading to expectations of aggressive monetary easing in Europe. Similarly, the regional currencies depreciated against the US dollar from July onwards as the deleveraging activities in the US caused large outflows of portfolio capital from the region.

## THE MALAYSIAN ECONOMY IN 2008

The Malaysian economy registered a growth of 4.6% in 2008, amidst the international financial turmoil and sharp deterioration in global economic environment. Robust domestic demand, in particular sustained private consumption and strong public spending, supported growth during the year. While external demand was strong in the first half of 2008, the sharp and rapid deterioration in the global economic conditions as well as major correction in commodity prices in the second half led to a contraction in Malaysia's export performance in the latter part of the second half year. Given the high degree of openness of the Malaysian economy, the contraction in exports adversely affected income and domestic demand. Private investment activities and private consumption moderated significantly in the fourth quarter of 2008.

## The Malaysian economy registered a growth of 4.6% in 2008 amidst the international financial turmoil and rapid deterioration in global economic conditions

The economy grew strongly by 7.1% in the first half of 2008 supported by robust domestic and external demand. Domestic demand was led by continued strong expansion in private consumption, supported by a steady increase in disposable income, positive labour market conditions and favourable financing environment. External demand was supported by very high commodity prices and strong export volume. Demand from the regional countries was also strong. When the global downturn intensified in the second half of 2008, with several major advanced economies slipping into recession and growth in a number of regional economies moderating rapidly, net external demand declined significantly. Nevertheless, real GDP growth remained positive in the second half-year, expanding modestly by 2.4%, supported by strong public consumption and continued expansion in private consumption. Bonus for the civil servants, payment of cash rebates for fuel subsidy and continued access to financing supported private consumption amidst weakening employment conditions which had some dampening influence on consumer sentiments. The deteriorating global economic environment also led to a decline in private investment activities in the second half of the year.

On the supply side, growth in the first half-year was driven by robust performance of the services sector as a result of the strong domestic demand conditions, and the expansion in trade and tourism activities. Further support came from the manufacturing sector due to robust external demand from the non-US markets and higher exports of resource-based products which also benefited from the rising commodity prices. The agriculture sector also expanded at a stronger pace due mainly to the strong expansion in crude palm oil production. However, the manufacturing sector, particularly the export-oriented industries, weakened in the second half of the year in line with the deterioration in global demand and the sharp correction in commodity prices. The services sector continued to support the economy in the second half-year, although growth moderated due to the slowdown in the services sub-sectors that were dependent on trade and capital-market related activities.

In line with the strong economic activities in the first half of 2008, labour market conditions strengthened during the period. Nevertheless, labour market conditions began to soften in the second half of the year as businesses, particularly in the manufacturing sector, turned cautious amidst deterioration in external demand. As a result, the unemployment rate increased to 3.7% in 2008, as total employment expanded at a slower pace compared to the increase in the labour force. Despite the rising inflationary pressure in the first half of the year, there was no evidence of excessive wage increases in response to the higher prices. The Malaysian Employers Federation Survey indicated that average salary in the private sector increased by 5.9% in 2008 in line with historical trends. Meanwhile, labour productivity improved further in 2008, thus supporting increases in salary and wage growth.

Headline inflation was already on an uptrend in the first five months of 2008 following the

**Table 1.3: Malaysia - Key Economic Indicators**

| | 2006 | 2007 | 2008*p* | 2009*f* |
|---|---|---|---|---|
| Population (million persons) | 26.6 | 27.2 | 27.7 | 28.3 |
| Labour force (million persons) | 11.5 | 11.8 | 12.0 | 12.1 |
| Employment (million persons) | 11.2 | 11.4 | 11.5 | 11.5 |
| Unemployment (as % of labour force) | 3.3 | 3.2 | 3.7 | 4.5 |
| Per Capita Income (RM) | 20,885 | 23,115 | 25,796 | 24,541 |
| (USD) | 5,694 | 6,724 | 7,738 | 6,812[7] |
| **NATIONAL PRODUCT (% change)** | | | | |
| Real GDP at 2000 prices[1] | 5.8 | 6.3 | 4.6 | -1.0 ~ 1.0 |
| (RM billion) | 475.2 | 505.4 | 528.8 | 528.9 |
| Agriculture, forestry and fishery | 5.4 | 2.2 | 3.8 | -2.0 |
| Mining and quarrying | -2.7 | 3.3 | -0.8 | -0.4 |
| Manufacturing | 7.1 | 3.1 | 1.3 | -8.0 |
| Construction | -0.5 | 4.6 | 2.1 | 3.0 |
| Services | 7.3 | 9.7 | 7.3 | 4.5 |
| Nominal GNI | 11.6 | 12.9 | 13.9 | -2.9 |
| (RM billion) | 556.4 | 628.1 | 715.3 | 694.8 |
| Real GNI | 7.1 | 6.1 | 2.9 | 1.8 |
| (RM billion) | 454.6 | 482.2 | 496.1 | 504.9 |
| Real aggregate demand[2] | 6.6 | 9.8 | 6.9 | 2.9 |
| Private expenditure[2] | 6.7 | 10.6 | 7.1 | -0.3 |
| Consumption | 6.5 | 10.8 | 8.4 | 3.5 |
| Investment | 7.5 | 9.8 | 1.5 | -17.7 |
| Public expenditure[2] | 6.5 | 7.9 | 6.5 | 11.4 |
| Consumption | 4.9 | 6.6 | 11.6 | 7.3 |
| Investment | 8.4 | 9.3 | 0.7 | 16.6 |
| Gross national savings (as % of GNI) | 38.4 | 38.4 | 37.9 | 32.2 |
| **BALANCE OF PAYMENTS (RM billion)** | | | | |
| Goods balance | 134.6 | 127.7 | 170.1 | 108.1 |
| Exports (f.o.b.) | 589.7 | 605.9 | 664.2 | 495.8 |
| Imports (f.o.b.) | 455.2 | 478.2 | 494.1 | 387.6 |
| Services balance | -6.9 | 2.4 | 1.7 | -0.9 |
| (as % of GNI) | -1.2 | 0.4 | 0.2 | -0.1 |
| Income, net | -17.3 | -13.9 | -25.4 | -10.6 |
| (as % of GNI) | -3.1 | -2.2 | -3.6 | -1.5 |
| Current transfers, net | -16.9 | -15.7 | -17.0 | -16.6 |
| Current account balance[3] | 93.5 | 100.4 | 129.4 | 80.0 |
| (as % of GNI) | 16.8 | 16.0 | 18.1 | 11.5 |
| Bank Negara Malaysia international reserves, net[4] | 290.4 | 335.7 | 317.4 | - |
| (in months of retained imports) | 7.8 | 8.4 | 7.6 | - |
| **PRICES (% change)** | | | | |
| CPI (2005=100)[5] | 3.6 | 2.0 | 5.4 | 1.5 ~ 2.0 |
| PPI (2000=100)[6] | 5.1 | 6.7 | 8.2 | - |
| Real wage per employee in the manufacturing sector | -1.4 | 2.2 | -0.9 | - |

[1] Beginning 2007, real GDP has been rebased to 2000 prices, from 1987 prices previously
[2] Exclude stocks
[3] Figures for the year 2008 are estimates
[4] All assets and liabilities in foreign currencies have been revalued into ringgit at rates of exchange ruling on the balance sheet date and the gain/loss has been reflected accordingly in the Bank's account
[5] Effective from 2006, the Consumer Price Index has been revised to the new base year 2005=100, from 2000=100 previously
[6] Effective from 2006, the Producer Price Index has been revised to the new base year 2000=100, from 1989=100 previously
[7] Based on average USD exchange rate for the period of January-February 2009
*p* Preliminary
*f* Forecast

Note: Numbers may not necessarily add up due to rounding

**Table 1.4 Malaysia - Financial and Monetary Indicators**

| **FEDERAL GOVERNMENT FINANCE (RM billion)** | **2006** | | **2007** | | **2008*p*** | |
|---|---|---|---|---|---|---|
| Revenue | 123.5 | | 139.9 | | 159.8 | |
| Operating expenditure | 107.7 | | 123.1 | | 153.5 | |
| Net development expenditure | 35.0 | | 37.5 | | 41.9 | |
| Overall balance | -19.1 | | -20.7 | | -35.6 | |
| Overall balance (% of GDP) | -3.3 | | -3.2 | | -4.8 | |
| Public sector net development expenditure | 86.5 | | 95.1 | | 106.7 | |
| Public sector overall balance (% of GDP) | -0.3 | | 1.7 | | -3.3 | |
| **EXTERNAL DEBT**[1] | | | | | | |
| Total debt (RM billion) | 184.5 | | 187.4 | | 235.6 | |
| Medium- and long-term debt | 141.7 | | 133.0 | | 155.6 | |
| Short-term debt[2] | 42.8 | | 54.5 | | 80.0 | |
| Debt service ratio (% of exports of goods and services) | | | | | | |
| Total debt | 4.8 | | 3.8 | | 2.7 | |
| Medium- and long-term debt | 4.5 | | 3.4 | | 2.5 | |
| **MONEY AND BANKING** | **Change in 2006** | | **Change in 2007** | | **Change in 2008** | |
| | **RM billion** | **%** | **RM billion** | **%** | **RM billion** | **%** |
| Money Supply M1 | 17.0 | 13.7 | 27.6 | 19.6 | 14.0 | 8.3 |
| M3 | 87.5 | 13.0 | 72.4 | 9.5 | 99.0 | 11.9 |
| Banking system deposits | 119.3 | 17.2 | 56.5 | 7.0 | 103.6 | 11.9 |
| Banking system loans[3] | 34.9 | 6.3 | 57.2 | 8.6 | 82.3 | 12.8 |
| Loan-deposit ratio (end of year) | 70.5 | | 72.2 | | 73.5 | |
| Financing-deposit ratio[4] | 79.0 | | 80.7 | | 81.1 | |
| | **2006** | | **2007** | | **2008** | |
| **INTEREST RATES (AVERAGE RATES AS AT END-YEAR)** | **%** | | **%** | | **%** | |
| Overnight Policy Rate (OPR) | 3.50 | | 3.50 | | 3.25 | |
| Interbank rates | | | | | | |
| 1-month | 3.58 | | 3.56 | | 3.30 | |
| Commercial banks | | | | | | |
| Fixed Deposit 3-month | 3.19 | | 3.15 | | 3.04 | |
| 12-month | 3.73 | | 3.70 | | 3.50 | |
| Savings deposit | 1.48 | | 1.44 | | 1.40 | |
| Base lending rate (BLR) | 6.72 | | 6.72 | | 6.48 | |
| Treasury bill (3-month) | 3.43 | | 3.39 | | 2.94 | |
| Government securities (1-year) | 3.55 | | 3.53 | | 2.89 | |
| Government securities (5-year) | 3.70 | | 3.78 | | 3.00 | |
| | **2006** | | **2007** | | **2008** | |
| **EXCHANGE RATES** | **%** | | **%** | | **%** | |
| Movement of Ringgit (end-period) | | | | | | |
| Change against SDR | 1.8 | | 1.7 | | -2.7 | |
| Change against USD[5] | 7.0 | | 6.8 | | -4.5 | |

[1] Effective from the first quarter of 2008, the external debt data of Malaysia has been redefined to treat entities in Labuan International Business and Financial Centre (Labuan IBFC) as residents
[2] Excludes currency and deposits held by non-residents with resident banking institutions
[3] Includes loans sold to Cagamas
[4] Adjusted to include holdings of private debt securities
[5] Ringgit was pegged at RM3.80=USD1 on 2 September 1998 and shifted to a managed float against a basket of currencies on 21 July 2005
*p* Preliminary

steady increase in global food and fuel prices that breached unprecedented new highs at mid-year. The inflation rate, however, rose sharply in the third quarter following the 40.4% adjustment to retail fuel prices in June. The increase in the headline inflation peaked at 8.5% in July. The easing of global food prices and bursting of the commodity bubble led to the sharp and rapid correction in the global commodity prices across the board. This led to the decline in prices of domestic food and fuel prices in the fourth quarter. For the year as a whole, headline inflation averaged at 5.4%.

The external position remained strong in the first half of 2008, due mainly to the large current account surplus. The current account was supported by a significantly larger trade surplus following the stronger growth in both commodities and resource-based manufacturing exports amidst high commodity prices. The services account continued to record a surplus, due to higher receipts from tourism. The financial account also recorded a large surplus in the first half of 2008 due to strong inflows of foreign direct investment and other investment. The large surplus in the current account was sustained in the second half of 2008 as the moderation in exports was mitigated by a decline in imports. Nevertheless, the overall balance of payments position in the second half of 2008 recorded a net deficit as the large net outflows in the financial account more than offset the surplus in the current account. The net outflow in the financial account was due mainly to the large reversal of portfolio investment flows due to the deleveraging activities by foreign financial institutions following the intensification of the global financial crisis.

The Malaysian economy faced the global financial crisis from a position of strength. This is largely due to the strengthened financial system after the Asian financial crisis a decade ago and the more balanced and diversified economic structure. The country's external position is also resilient, with low external debt, a sustained current account surplus and high level of foreign reserves. The financial sector is sound, with strong liquidity and capital buffers. Given the continued uncertainty in the external environment, the policy response has focused on supporting domestic demand, by ensuring that there will be continued expansion in private consumption and public spending, and preventing widespread unemployment.

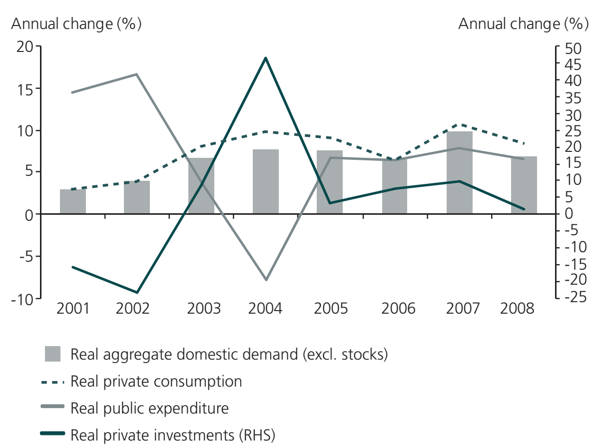
**DOMESTIC DEMAND CONDITIONS IN 2008**

In the first half of 2008, the economy expanded strongly on the strength of domestic demand, which grew by 9.4% driven mainly by strong growth in private consumption spending. The resilient consumer spending was supported by a steady increase in disposable income, stable labour market conditions and favourable financing environment. However, as the global financial crisis worsened in the second half of 2008, the global downturn intensified further, leading to sharp decline in external demand and correction in commodity prices.

## Domestic demand, which grew strongly in the first half, moderated towards end-2008 as the global economic downturn intensified

The impact was felt in economic sectors with high trade exposure, subsequently affecting domestic demand. As a result, growth in domestic demand moderated to 4.7% in the second half-year, bringing the overall growth in aggregate **domestic demand** for the year to 6.9% (2007: 9.8%). Private consumption growth slowed down towards end-2008 following the weaker outlook in the job market. Private investment moderated, particularly in the second half of 2008, as the global economic

**Chart 1.3**
**Real Domestic Demand Aggregates**

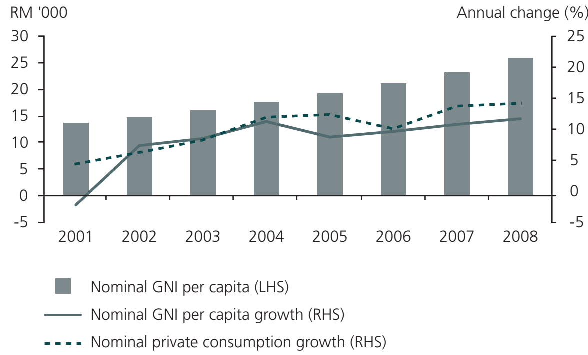


slowdown started to affect capital spending activities, especially within the export-oriented manufacturing sector. The public sector, meanwhile, continued to be supportive of overall economic growth.

**Private consumption** remained resilient in 2008, increasing by 8.4% (2007: 10.8%) despite concerns over the higher general level of prices following the hike in fuel and electricity prices in June 2008. The performance of major consumption indicators such as imports of consumption goods, credit card spending, loans approved and disbursed to households, as well as passenger car sales remained strong. Household spending was supported by the steady increase in disposable income arising from the high commodity prices and stable labour market conditions, particularly during the first half of the year. Although commodity prices moderated significantly in the second half, prices were on average at favourable levels relative to historical trends. The expansionary impact from the civil servants' salary adjustment in second half of 2007 also carried over into the first half of 2008, providing support for higher consumer spending. Meanwhile, the bonus to the civil servants, which was paid in September and December 2008, offered an additional lift to consumption. Furthermore, labour market conditions remained largely stable throughout the year. Towards the year-end, however, the impact of the deepening and broader global economic slowdown has resulted in weaker job prospects, with companies mainly in the export-oriented industries taking cost-cutting measures through temporary lay-offs and shorter working hours; hence, leading to a moderation in consumption spending, especially in the fourth quarter of 2008.

While consumer spending was still expanding, consumer sentiments were undermined by a number of factors as the year progressed. Reflecting consumers' concerns over rising prices and subsequently worsening global conditions, the Malaysian Institute of Economic Research (MIER)'s Consumer Sentiment Index fell below the 100-point threshold from the second quarter of 2008 onwards. Consumers were initially concerned with the impact of the 78-sen hike in retail fuel prices on their disposable income. However, this was mitigated by the rebates and subsidies provided to selected motorists and car owners. The Government subsequently reduced

**Chart 1.4**
**GNI per Capita**




the fuel prices in line with the decline in global crude oil prices. Towards end-2008, consumer sentiments shifted from concerns of higher cost of living to conditions in the job market and income prospects as the global recessionary conditions deepened.

During the year, consumer spending was also supported by favourable financing conditions. Interest rates remained low and accommodative, while consumers continued to enjoy access to credit. Against this backdrop, household credit expanded further with outstanding household loans increasing by 9.7% in 2008 (2007: 7.7%), driven mainly by loans for purchase of residential property, consumer durables and passenger cars. On the whole however, household balance sheets remained sound, with household debt to financial asset ratio remaining low at 41.9% (2007: 36.8%), while the non-performing loan (NPL) ratios for household loans and residential property declined further to 4.1% and 5.6% respectively (2007: 5.3% and 7.0% respectively) at end-2008.

**Private investment**, however, moderated to 1.5% in 2008 (2007: 9.8%). While private investment was strong in the early part of 2008, capital expansion activities slowed towards the year-end as businesses deferred or cancelled investment decisions following the sharp global economic downturn. Various investment indicators showed weakening investment activities in the later part of 2008. Imports of capital goods, which showed strong positive growth of 9.6% in the first half, declined by 7.9% in the second half. Loans disbursed to businesses, and private debt securities issued for new activities also indicated

## Patterns of Investment in Countries at Different Stages of Development

### Introduction

Investment plays an important role in the economic development process, as it expands a country's productive capacity of physical and human capital. Total investment comprises capital spending by both the private and public sectors, with the public sector's role being mainly to focus on providing basic and necessary infrastructure to support private sector economic activities. As an economy develops, patterns of investment spending tend to expand to involve more diverse types of economic activities.

This article analyses the patterns of total investment as a percentage of gross domestic product (GDP) in countries at different stages of economic development. By analysing the investment patterns of different groups of countries, the article assesses whether different stages of economic development, as measured by nominal income per capita, correspond to particular levels of investment relative to GDP. The second part of the article discusses the reasons for the steady decline of the investment-to-GDP ratio as a country becomes more developed. The final part of the article assesses whether there is a distinctive, overall trend in the investment–to-GDP ratio as a country progresses from a low to a high income economy.

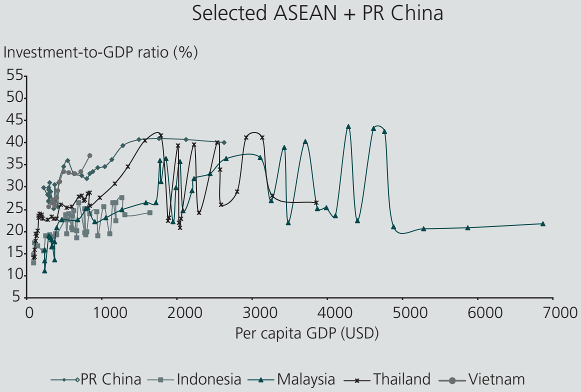
### Do stages of development influence investment levels?

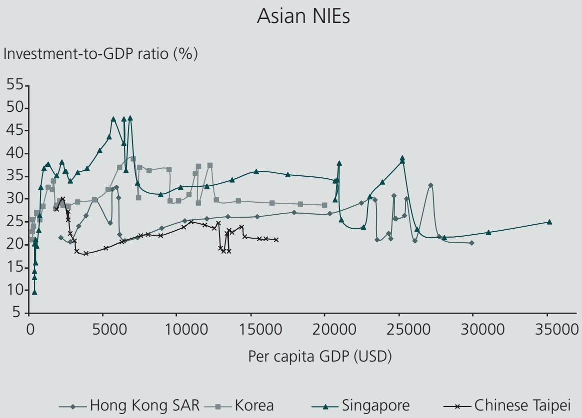
Analysing the investment-to-GDP ratios of the 14 economies in Chart 1 in relation to income per capita shows that there is no common investment level associated with any particular stage of development. Countries have different investment expenditure as a percentage of GDP even at similar stages of development. For example, at the same USD1,000 income per capita, Malaysia's share of investment to GDP was nearly 22%, Thailand 28%, while PR China is even higher at 35%. In certain cases, a country's investment-to-GDP ratio is twice the level of another country although both have relatively similar incomes per capita. For instance, Singapore's investment-to-GDP ratio is 40% at a per capita income of USD6,000, roughly double Chinese Taipei's investment-to-GDP ratio which has a similar income per capita.

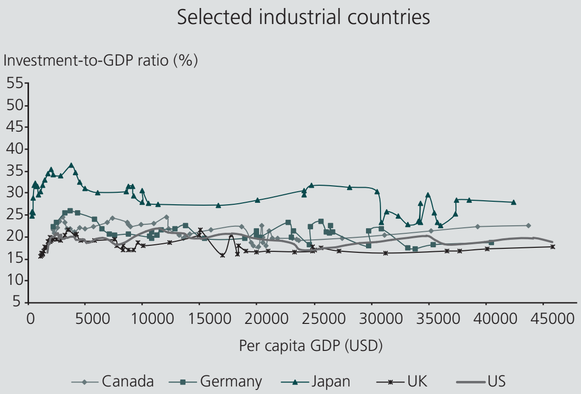
This suggests that there are other factors that influence a country's investment expenditure as a percentage of its GDP. Three factors are particularly important. The first factor is the growth strategies that countries pursue. For example, countries that adopt aggressive export-oriented industrialisation strategies, which often involve promotion of inflows of foreign direct investment (FDI), tend to have higher investment ratios. The industrialisation process is generally driven by rapid expansion of the manufacturing sector, which is more capital-intensive since it requires the private sector to invest heavily on machinery and equipment. In addition, as the industrialisation process intensifies and contributes to a higher level of income per capita, the level of investment also increases as the country moves up to higher value-added manufacturing activities. In the case of countries relying on FDI, the high investment ratios may persist if foreign firms continue to expand the initial investment and reinvest their earnings in the host economies.

The second factor relates to the role of the public sector in the economy at the different stages of economic development. The experience of ASEAN, Asian NIEs and PR China show that investment undertaken by the public sector is high at the early stages of the development, in particular in the areas of transportation infrastructure, utilities and education, which is necessary to create a conducive environment to support private sector activity as well as in attracting FDI.

**Chart 1**
**Selected Economies Pattern of Investment**




The third factor that may influence the investment-to-GDP ratio is whether the countries have natural resources. Countries which lack natural resources or land, such as Singapore and Japan, have higher incentives to attract and nurture strong, diverse and capital-intensive industries. Resource-rich countries, on the other hand, may have lower investment ratios as they seek to exploit their natural advantage, which tend to involve lower capital input. This is especially true if countries do not expend much effort to generate higher value added from these natural resources, particularly in developing downstream activities.

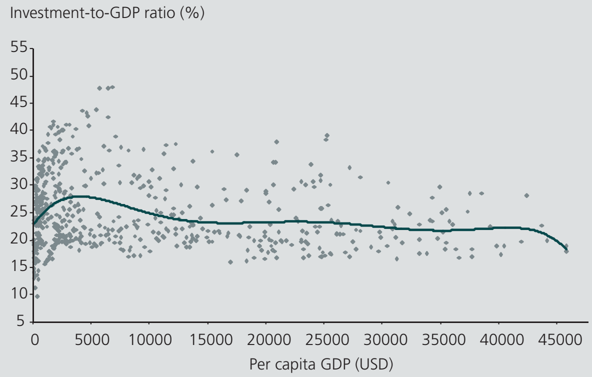
**Why does the investment ratio decline steadily as an economy becomes developed?**

As shown in Chart 1, industrial countries tend to have lower and more stable investment ratios, with the ratios converging within a smaller band of between 15-25% of GDP, except for Japan (20-35%). This may be the outcome of the rise of the services sector as the largest economic sector as an economy becomes more developed. The services sector, by its nature, is less capital-intensive, but has a higher value-added relative to the manufacturing sector. Unlike the export-oriented manufacturing sector, the services sector is more related to and has higher reliance on private consumption spending. Indeed, private consumption is higher in advanced economies, mainly in line with their high level of income, which is one of the major determinants of private consumption expenditure.

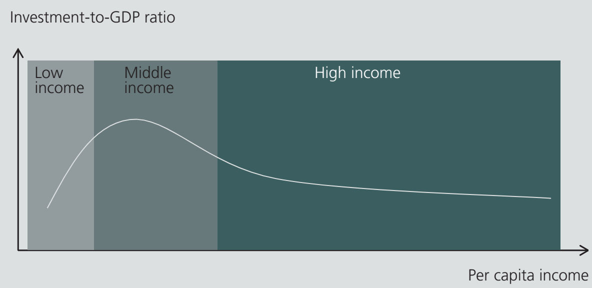
The investment ratios of the Asian developing countries tend to lie within a relatively wider band of 10-45% of GDP. In addition, the investment ratios are also more volatile compared with the industrial countries. This may be due to the diverse characteristics of the countries, in terms of the degree of openness, production structure, investment policies, and the mix of capital and labour in the economy. For instance, a more open economy is often associated with a higher investment ratio at any given income per capita, but may be more susceptible to external demand volatility.

**Chart 2**
**Pattern of Investment as Countries Move Across Stages of Development**

Scatter plot




Possible investment path across development stages




**Is there a distinctive trend for the investment-to-GDP ratio across the different development stages?**

Despite considerable heterogeneity across countries as outlined above, there seems to be a broad common trend in investment-to-GDP ratio as countries move from one stage of economic development to another, as suggested in Chart 2[1].

First, low income countries tend to have a rapid increase in their investment-to-GDP ratios. During the early development stage, nations need to build up basic and necessary infrastructure in order to get the major factor markets connected and functioning properly, for example, through building road and transportation networks. This would require high initial investment. In addition, economic activity is typically concentrated in labour-intensive commodity production and basic assembly operations. Hence, although the amount of investment involved may be smaller, the growth of its share to GDP is more significant. Also, the increase in investment-to-GDP ratio is a reflection of the cost of acquiring the latest technologies from foreign companies in the more advanced countries. The technology acquisition approach represents a quicker way to moving up the development ladder.

[1] Excluding the last few observations in the scatter plot related to those with highest income per capita, the trend line in the scatter plot can almost exactly replicate the path projected in the second chart.

Next, the investment pattern stabilises in the middle-income stage. As economic activity becomes more sophisticated, and as countries move towards higher value-added activities in the supply chain, they need to improve and upgrade their infrastructure. This includes, for example, more advanced ports with higher capacity, telecommunications, and utilities infrastructure. Furthermore, their industrial structures may also entail high investment. Moving from simple assembly operations to wafer production for instance, requires high investment since the new process needs different and almost certainly higher cost machinery and inputs.

Finally, advanced countries tend to have lower investment ratios, generally due to their shift towards services and greater consumption spending, which leads to a larger consumption-to-GDP ratio. They also have bigger and more efficient services sectors that serve their domestic economies. Since the services sector tends to be less capital-intensive, the overall share of investment to GDP is lower. Another contributing factor is the relocation of the major economies' lower value-added production activities abroad as a means to remain viable through lower costs. Firms still retain part of the production supply chain in the developed economies especially the higher value-added activities, as the developed economies tend to be driven more by innovation and knowledge-based activities. Investment expenditure then focuses more on improving learning and fostering innovation, rather than spending on heavy machineries and physical capital inputs.

In the case of Malaysia, during the early stages of development, major economic activities were concentrated on exploiting the rich natural resources. During the early stage of development, Malaysia was heavily dependent on the resource-based sector through production and exports of major commodities such as rubber, tin and later, palm oil and crude oil. Investment expenditure was mainly concentrated in developing and improving higher-yielding agricultural crops as well as the provision of basic infrastructure by the public sector. The global economic crisis in the early 1980s prompted the Government to diversify the sources of growth and pursue an export-oriented industrialisation strategy. The active promotion of a capital-intensive manufacturing sector led to rising private investment particularly through high FDI inflows, which resulted in a higher share of the manufacturing sector in the economy. Public investment was also sustained as the Government, through its privatisation exercise, embarked on improving further and upgrading infrastructure such as roads, ports, airports, telecommunications and utilities. Investment peaked at 43.6% of GDP in 1995. After the Asian Financial Crisis of 1997/98, however, the investment-to-GDP ratio declined and stabilised at lower levels as the less capital-intensive services sector became more prominent, while large-scale public sector infrastructure projects, which were mainly started prior to the crisis, were completed.

**Conclusion**

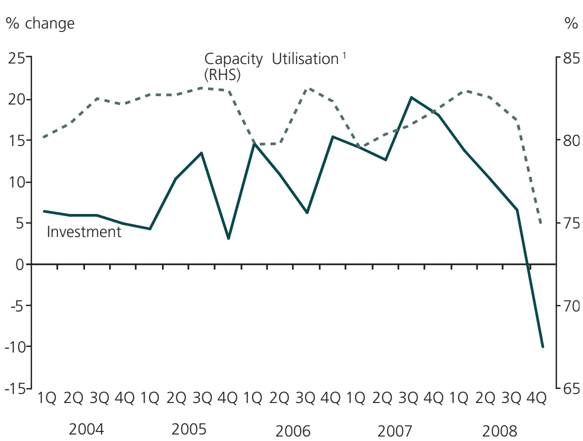
In summary, this article analyses patterns of investment in countries at different stages of economic development rather than across time. A few observations could be drawn from this analysis. First, there is a wide range of investment-to-GDP ratios among countries, even within the same income band. This suggests that there are factors other than the level of income that influence investment ratios. The development and industrialisation strategies, role of the public sector as well as the existence of natural resources are important determinants. Secondly, investment ratios for more advanced economies tend to stabilise at a relatively lower rate. This largely reflects the shift towards higher value-added but less capital-intensive and services-related activities. Finally, there is a broad pattern of investment–to-GDP ratio as countries evolve through the different development stages as measured by level of per capita income – a rapid rise in investment at the initial stage of development, followed by a stable investment ratio as it reaches the middle income stage, before converging to a lower investment ratio as a more advanced stage of development is achieved.

slower investment activities towards the year-end. Although gross FDI inflows remained high at RM51 billion (2007: RM46.2 billion), the worsening global economic environment affected inflows in the second half of 2008. Reflecting the weaker investor sentiments, MIER's third quarter Business Conditions Index (BCI) dipped below the 100-point confidence threshold, and ended the year at a low 53.8 points in the final quarter.

Investment in the manufacturing sector was the most severely affected by the deteriorating global economic conditions. As demand for manufactured exports declined, so did production activities which led to lower capacity utilisation rates. MIER's capacity utilisation rates dropped from 83% in the first quarter of 2008 to 74.4% in the fourth quarter, thereby reducing the need for firms to undertake new capacity expansion exercises. While ongoing projects were continued, the global economic downturn has led to some postponements of new projects. Trends in indicators such as imports of machineries and loans disbursed to the manufacturing sector confirmed the declining investment trend.

However, investment in other sectors remained positive. In the mining sector, capital expenditure in the oil and gas sector remained high. Rising crude oil prices, particularly in the first half of 2008, supported exploration activities especially into deepwater oil fields. Investment

**Chart 1.5**
**Total Nominal Investment and Manufacturing Sector Capacity Utilisation**




[1] Source: Malaysian Institute of Economic Research (MIER)

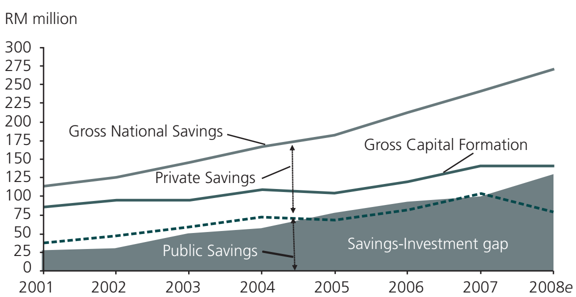
in the services sector expanded mainly in the transportation sub-sector, attributable to expansion in the rail and air transport, as well as in port facilities. Meanwhile, ongoing network upgrading exercises by current and new mobile operators supported investment in the communications sub-sector. In the wholesale and retail trade sub-sector, there were ongoing expansion projects for new outlets.

**Public investment** grew at a slower pace of 0.7% in 2008 (2007: 9.3%). Large development expenditure continued to be channelled into projects to further improve the economic and social services sectors of the economy, in line with the Government's role to provide support for growth. In the economic sector, expenditure was mainly targeted to improve and upgrade industrial and public utilities infrastructure, enhance transportation system and increase efficiency in agriculture production. Meanwhile, spending in the social services sector continued to focus on essential services including education, healthcare and housing.

Capital spending by the non-financial public enterprises (NFPEs) was sustained. Investment by PETRONAS expanded further, channelled mainly into exploration and development activities in the upstream oil and gas sub-sector, as well as shipping fleet expansion. Further capital spending by the NFPEs was to improve the utilities, transportation and communication systems. Tenaga Nasional Berhad continued to undertake capital spending to upgrade and improve its power generation, transmission and distribution systems. Meanwhile, capacity improvement in the communications sector was mainly to enhance the broadband infrastructure facilities in order to provide for wider and better communication services.

**Public consumption** expanded strongly by 11.6% in 2008 (2007: 6.6%) due mainly to higher expenditure on emoluments, defence as well as supplies and services. The increase in emoluments expenditure reflected the Government's commitment to enhance human resource development in the public sector. Meanwhile, the higher expenditure for supplies and services during the year was mainly for maintenance of buildings and fixtures as well as to improve administrative machinery and delivery system of the public sector.

**Chart 1.6**
**Gross National Savings and Savings-Investment Gap**




*e* Estimate

Despite the strong growth in private consumption, private sector savings increased significantly to RM190.5 billion or 26.6% of GNI in 2008 (2007: 21.8%), broadly reflecting households' sound financial position. Banking sector deposits held by individuals rose further to RM366 billion during the year (2007: RM330.6 billion). However, public sector savings declined to RM80.4 billion or 11.2% of GNI (2007: 16.6%). In total, **gross national savings (GNS)** increased by 12.3% to RM270.9 billion, which in turn led to a larger savings-investment surplus of RM129.4 billion or 18.1% of GNI in 2008. This high rate of savings enabled Malaysia to finance its growth mainly from domestic sources.

## SECTORAL REVIEW

The Malaysian economy entered 2008 with favourable growth across all major sectors, amidst strong domestic demand and supportive external demand conditions from regional economies and rising prices of commodities. Growth in the first half-year was driven by robust performance of the services sector with further support coming from the manufacturing and agriculture sectors. However, the sharp deterioration in the global economic conditions in the second half of 2008 led to a pronounced deceleration in external demand. This led to weakened performance of sectors most directly exposed to global demand, particularly the electronics and electrical industry. In addition, the external sector was also affected by the bursting of the commodity price bubble. The economy, however, continued to be supported by the expansion of the services sector.

### Services Sector

In 2008, the **services sector** expanded by 7.3% compared with 9.7% in 2007. The sector contributed 3.9 percentage points to the overall GDP growth whilst its share to GDP increased to 55% (2007: 53.6%). In the first half of the

**Table 1.5**
**Services Sector Performance at Constant 2000 prices**

| | 2007 | 2008*p* | 2007 | 2008*p* |
|---|---|---|---|---|
| | Annual change (%) | | Share to GDP (%) | |
| **Services** | **9.7** | **7.3** | **53.6** | **55.0** |
| Intermediate services | 11.7 | 6.0 | 23.4 | 23.7 |
| Finance and insurance | 11.1 | 7.7 | 10.7 | 11.0 |
| Real estate and business services | 18.2 | 1.5 | 5.3 | 5.1 |
| Transport and storage | 10.0 | 6.1 | 3.7 | 3.8 |
| Communication | 7.0 | 7.3 | 3.7 | 3.8 |
| Final services | 8.1 | 8.4 | 30.2 | 31.2 |
| Wholesale and retail trade | 12.5 | 9.8 | 12.2 | 12.8 |
| Accommodation and restaurant | 10.8 | 7.3 | 2.4 | 2.4 |
| Utilities | 3.9 | 2.1 | 3.0 | 2.9 |
| Government services | 4.5 | 11.9 | 6.9 | 7.4 |
| Other services | 5.0 | 4.9 | 5.7 | 5.7 |

*p* Preliminary
Note: Numbers may not necessarily add up due to rounding
Source: Department of Statistics, Malaysia

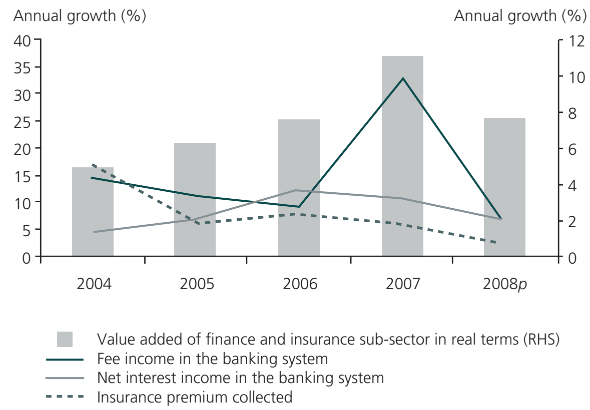
year, the sector posted a strong performance due to the robust domestic demand conditions, and expansion in trade and tourism activities. In contrast with other sectors that were affected by the global economic slowdown, growth in the services sector registered a commendable growth of 6.4% in the second half of the year (1H 2008: 8.4%). Growth in the second half year was affected by the moderation in the services sub-sectors that were dependent on trade and capital market-related activities.

## Despite moderating in the second half of the year, growth of the services sector continued to remain strong in 2008

The **wholesale & retail trade** sub-sector expanded by 9.8% compared with 12.5% in 2007. The sub-sector registered a strong growth in the first half year, in line with robust domestic demand. The continued expansion in hypermarkets and retail outlets coupled with the extension of Visit Malaysia Year and Malaysian Mega Sale events helped boost retail spending. In addition, the motor vehicle segment grew significantly during the first nine months, following the launch of new models. However, growth moderated in the second half year, affected by high inflation and weak consumer sentiments. As a result, consumer purchases were mainly confined to food and beverages, and essential household items.

The **finance and insurance** sub-sector recorded a growth of 7.7% (2007:11.1%) to account for 11% of GDP at end-2008. In the finance segment, financial intermediation continued to support economic activity in an environment of ample liquidity and continued access to financing. Total loans outstanding of the banking system increased by 12.8% (2007: 8.6%) with strong loan growth to all sectors of the economy. Nevertheless, the net interest income of the banking system recorded a lower growth of 8% (2007: 10.8%) partly as a result of narrowing interest rate spreads following greater competition. Meanwhile, fee-based income moderated due mainly to the slowdown in the capital market activities in the second half of the year. Islamic finance continued to expand during the year, with six new Islamic

**Chart 1.7**
**Performance of the Finance and Insurance Sub-sector vis-à-vis Related Indicators**




*p* Preliminary
Source: Department of Statistics, Malaysia; Bank Negara Malaysia

banks commencing operations, resulting in a total of 17 Islamic banks in operation as at end-2008. Meanwhile, the insurance services industry recorded a moderate growth due mainly to lower activities in the life insurance segment.

In the **communication** sub-sector, increased competition in the telecommunications market and the roll-out of new broadband services, particularly WiMax, provided impetus for strong demand in both the cellular and broadband segments. By August, four WiMax operators were offering high speed broadband services to key urban areas. This development acted as a catalyst in enhancing broadband accessibility throughout the country. Meanwhile, the cellular segment continued to remain vibrant with the entrance of a new player, aggressive promotions of post-paid business and the implementation of mobile number portability. As at end-2008, penetration rate of broadband increased to 21.1% of household (end-2007: 14.4%), while that of cellular segment rose to 96.8% of population, compared to 85.1% as at end-2007. These developments contributed favourably towards a higher growth of 7.3% in the communication sub-sector (2007: 7%).

Meanwhile, the **transport and storage** sub-sector expanded at a moderate pace of 6.1% (2007: 10%). The cargo-related segment performed favourably in the first half of the year,

**Table 1.6**
**Selected Indicators for the Services Sector**

| | 2007 | 2008*p* |
|---|---|---|
| | Annual change (%) | |
| **Utilities** | | |
| Electricity production index | 3.9 | 1.2 |
| **Wholesale & Retail Trade and Accommodation & Restaurant** | | |
| Consumption credit disbursed | 9.5 | 10.8 |
| Tourist arrivals | 19.5 | 5.1 |
| Total sales of motor vehicles | -0.7 | 12.5 |
| **Finance & Insurance and Real Estate & Business Services** | | |
| Loans outstanding in the banking system | 8.6 | 12.8 |
| Insurance premiums | 6.1 | 2.7 |
| Bursa Malaysia turnover (volume) | 94.1 | -59.8 |
| **Transport & Storage and Communication** | | |
| Total container handled at Port Klang and PTP (TEUs) | 13.6 | 7.7 |
| Airport passenger traffic | 6.2 | 5.9 |
| Air cargo handled | -5.5 | -6.7 |
| SMS traffic | 70.6 | 28.7 |
| | % | |
| Penetration rate: | | |
| - Broadband[1] | 14.4 | 21.1 |
| - Cellular phone[2] | 85.1 | 96.8 |
| - Fixed line | 47.8 | 44.9 |

[1] of household
[2] of population
*p* Preliminary

Source: Department of Statistics, Malaysia; Malaysia Tourism Promotion Board; Malaysian Automotive Association; Bursa Malaysia Berhad; Port Klang Authority; PTP; Malaysia Airports Holdings Berhad; Senai Airport Terminal Services Sdn Bhd; Malaysian Communications and Multimedia Commission; and Bank Negara Malaysia.

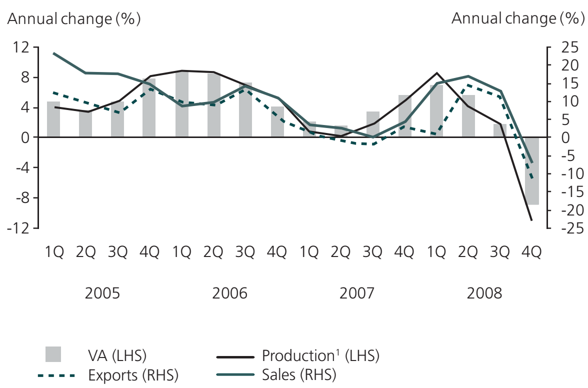
supported by favourable trade and manufacturing activities. However, in the second half of the year, the global economic downturn adversely affected the manufacturing sector, which in turn, translated into lower demand for air cargo, shipping, ports and other related services. Nevertheless, the passenger-related segment continued to be resilient. In particular, air passenger traffic at all airports sustained its momentum from the previous year, primarily on strong domestic and regional travel, as budget airlines continued to prosper in the region. Furthermore, the year also saw a significant milestone in the airline industry following the partial liberalisation of the Kuala Lumpur-Singapore air route to budget airlines in February and full liberalisation in December.

In the **other services** sub-sector, growth was sustained at 4.9% (2007: 5%). The sub-sector benefited from continued demand for private education services, healthcare services and entertainment-related services. However, the **accommodation & restaurant** sub-sector recorded a more moderate growth in 2008, having registered a double-digit growth in 2007, as the sub-sector was affected by the weaker consumer sentiments in the latter part of the year. Similarly, the **real estate & business services** sub-sector registered a lower growth of 1.5% in 2008, following a robust growth of 18.2% in 2007. The moderation in growth was mainly due to weak capital market-related activity and the moderation in property transactions that was particularly evident in the second half of the year.

### Manufacturing Sector

**Manufacturing sector** expanded, albeit at a much slower pace in 2008 (1.3%; 2007: 3.1%), driven mainly by domestic-oriented industries. In the first half of the year, growth was strong and broad based with robust external demand for both electronics and electrical (E&E) products, emanating largely from non-US markets, and primary-related products which benefited from the rising commodity prices.

**Chart 1.8**
**Manufacturing Sector: Value-added, Production, Exports and Sales**




[1] Data from 2008 onwards are based on the new Industrial Production Index (2005=100)
Source: Department of Statistics, Malaysia

**Table 1.7**
**Performance of the Manufacturing Sector**

| | 2007 | 2008 |
|---|---|---|
| | Annual change % | |
| **Value-added (RM million at 2000 prices)** | **3.1** | **1.3** |
| **Overall Production**[1] | **2.2** | **0.7** |
| **Export-oriented industries** | **1.0** | **-1.2** |
| **Electronics & electrical cluster** | **-1.5** | **-3.5** |
| *of which:* | | |
| Electronics | 3.0 | -5.4 |
| Electrical | -10.8 | 1.1 |
| **Primary-related cluster** | **2.7** | **0.4** |
| *of which:* | | |
| Chemicals and chemical products | 3.6 | -3.5 |
| Petroleum products | 2.5 | 5.9 |
| Rubber products | 8.6 | 4.7 |
| Off-estate processing | -8.9 | 9.4 |
| **Domestic-oriented industries** | **7.6** | **8.0** |
| **Consumer-related cluster** | **5.6** | **11.0** |
| *of which:* | | |
| Transport equipment | -1.1 | 23.4 |
| Food, beverage & tobacco products | 9.1 | 7.4 |
| **Construction-related cluster** | **10.0** | **4.3** |
| *of which:* | | |
| Construction-related products | 8.5 | 3.2 |
| Fabricated metal products | 12.5 | 6.1 |
| **Exports** | **0.3** | **3.6** |

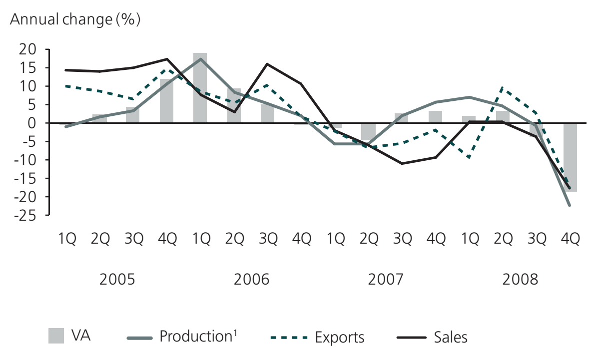
[1] Production data are based on the new Industrial Production Index (2005=100)
Source: Department of Statistics, Malaysia

This was further reinforced by the firm performance in domestic-oriented industries owing to strong domestic demand. In the second half of the year, the manufacturing sector began to weaken in line with the rapid deterioration in global demand and the sharp correction in commodity prices. Export-oriented industries were severely affected, particularly towards the end of the year as global demand decelerated sharply. This weakness also affected the performance of the domestic-oriented industries, but the strong expansion in the consumer-related products partly cushioned the overall decline in the manufacturing sector. Nevertheless, manufacturing sector continued to be the second largest contributor to the economy with its share of GDP of 29.2% (2007: 30.1%).

## Manufacturing sector growth was driven by domestic-oriented industries as the performance of export-oriented industries weakened significantly towards year-end

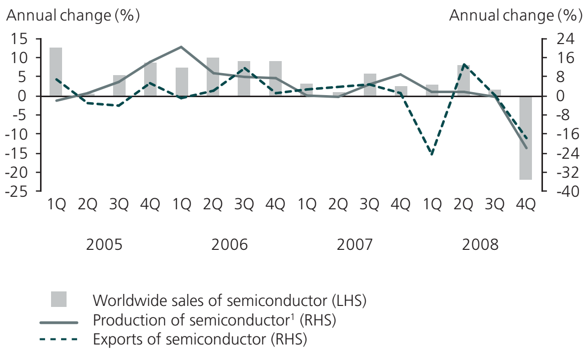
**Export-oriented industries** contracted by 1.2% (2007: 1.0%) as the declines in the E&E cluster of industries outweighed the growth of the primary-related cluster. **E&E** industry continued to weaken in 2008, affected by the global downturn in the second half of the year, which more than offset the robust external demand from emerging economies in the early part of the year. During the first half of the year, production of computers and parts recorded a strong performance attributable to the surge in external demand from the non-US markets. Meanwhile, output of semiconductors increased as there was strong demand for end-products such

**Chart 1.9**
**E&E Cluster: Value-added, Production, Exports and Sales**




[1] Data from 2008 onwards are based on the new Industrial Production Index (2005=100)
Source: Department of Statistics, Malaysia

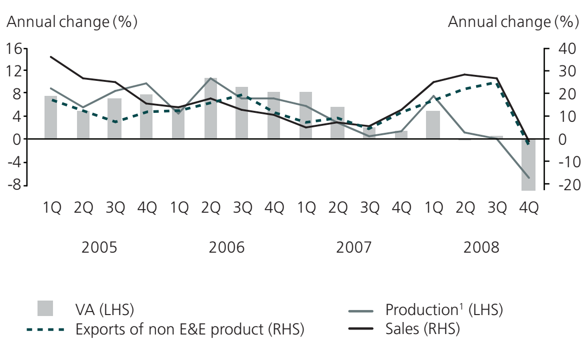
**Chart 1.10**
**Production and Exports of Semiconductors**




[1] Data from 2008 onwards are based on the new Industrial Production Index (2005=100)
Source: Department of Statistics, Malaysia
Semiconductor Industry Association (SIA)

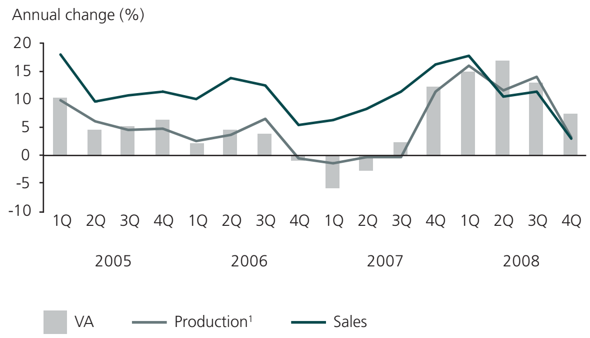
as computers, consumer electronics and telecommunications, mainly from PR China, Hong Kong and India. Similarly, strong demand for new electrical products such as Blu-ray disc players and HD LCD televisions, mainly from Australia and Middle-East, contributed significantly, reversing the decline in production of electrical goods in the previous year. However, these trends reversed sharply in the second half of the year as the downturn in the global economy precipitated declines in E&E production.

**Chart 1.11**
**Primary-related Cluster: Value-added, Production, Exports and Sales**




[1] Data from 2008 onwards are based on the new Industrial Production Index (2005= 100)
Source: Department of Statistics, Malaysia

**Chart 1.12**
**Consumer-related Cluster: Value-added, Production and Sales**

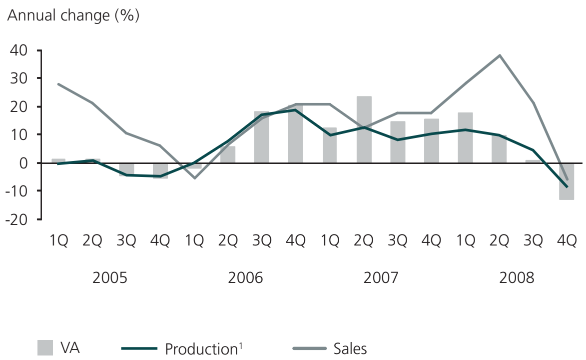



[1] Data from 2008 onwards are based on the new Industrial Production Index (2005=100)
Source: Department of Statistics, Malaysia

Manufacturers in the E&E industry also faced price attrition in their products amidst intense competition not only locally but also among major global players.

Output in the **primary-related** products industry expanded, albeit marginally, supported mainly by the off-estate, chemicals and rubber products. During the first half of the year, the strong growth in the off-estate processing segment was due mainly to the high commodity prices that encouraged more harvesting and processing, while rubber products were mainly sustained by continued growth in the transportation industry and the strong external demand for rubber gloves. In addition, the sustained growth of the E&E and transportation sub-sectors lent support to the plastic industry in the chemicals and chemical products segment. In the second half of the year, primary-related products were affected by both the global economic slowdown and the commodity price correction. Production of the off-estate processing registered a sharp decline. The decline in production of rubber tires due to slower growth in the transportation segment was cushioned by the more resilient demand for rubber gloves which supported the overall rubber products segment. The growth of the chemicals and chemical products was mainly affected by the tapering off in demand for E&E products as well as other consumer and industrial goods.

**Chart 1.13**
**Construction-related Cluster:**
**Value-added, Production and Sales**




[1] Data from 2008 onwards are based on the new Industrial Production Index (2005=100)

Source: Department of Statistics, Malaysia

**Domestic-oriented industries** registered a stronger growth of 8% (2007: 7.6%), supported mainly by strong domestic demand. Output of **consumer-related products** such as food, beverages and tobacco increased by double digits, attributable to the robust private consumption during the year. Meanwhile, transport equipment saw a robust performance in the first half year in line with the high car sales. Car sales reached its four-year cyclical peak, owing to the positive consumer sentiment given continuous income growth, availability of competitive financing rates as well as aggressive promotions on new car models. However, in the second half year, the performance of auto industry moderated as consumers turned cautious due to the weakening economic outlook.

Strong growth in production of **construction-related** materials in the first half of the year was supported by both the domestic construction sector and robust external demand from the region. The removal of the price ceiling on steel bars and billets as well as the reduction in import duty on cement provided a further boost. Slower growth in the second half of the year was due mainly to weak local demand and decline in prices, but cushioned somewhat by external demand especially for iron and steel products.

**Table 1.8**
**Agriculture Sector:**
**Value Added and Production**

| | 2007 | 2008*p* |
|---|---|---|
| | Annual change (%) | |
| **Value added** | **2.2** | **3.8** |
| **Industrial crops** | **0.1** | **3.2** |
| *Production of which:* | | |
| Crude palm oil | -0.4 | 12.1 |
| Rubber | -6.6 | -10.1 |
| Saw logs | 0.7 | -16.3 |
| Cocoa beans | 10.2 | -20.5 |
| **Food crops** | **5.3** | **4.7** |
| *Production of which:* | | |
| Fish | 0.2 | 5.2 |
| Livestock [1] | 9.9 | 4.3 |
| Vegetables | 8.6 | 11.9 |
| Fruits | -2.8 | 3.2 |

[1] Refers to Peninsular Malaysia only
*p* Preliminary

Source: Department of Statistics, Malaysia
Malaysian Palm Oil Board
Malaysian Rubber Board
Forestry Departments (Peninsular Malaysia, Sabah and Sarawak)
Malaysian Cocoa Board
Fisheries Department, Malaysia
Veterinary Services Department, Malaysia
Department of Agriculture, Malaysia

**Agriculture Sector**
The agriculture, forestry and fishing **(agriculture) sector** expanded at a faster pace of 3.8% in 2008, driven mainly by stronger palm oil production, which accounted for about 30% of value add in the agriculture sector. Growth during the year was also supported by higher output of key food-related activities such as fisheries and livestock.

**Crude palm oil** production rose strongly by 12.1% to 17.7 million tonnes in 2008, driven by favourable weather conditions and in part by strong increase in crude palm oil prices of 16.3% to an average of RM2,875 per tonne.

## The expansion in agriculture sector was driven mainly by stronger palm oil production

Strong outperformance was attributable to the more widespread application of fertilizer that contributed to higher yields in Peninsular Malaysia which recorded total output of 10.1 million tonnes

## Impact of Developments in Commodity Prices

Commodity prices were characterised by exceptional volatilities in 2008, with prices moving in large magnitudes on the upswing and downswing within the short period of a year. Commodity prices increased sharply in the first half of the year due in part to the strong underlying demand and the expectations of stronger demand from the large emerging economies and also due to the increase in demand from funds as commodities became a new investment asset class. In addition, food prices were also driven by the increasing use of food crops for the production of alternative fuels and production shortfalls due to adverse weather conditions. Prices of several commodities reached all time highs. However, as the global financial turmoil intensified in the second half of the year, the large unwinding of long positions by funds and the pull back of financing by financial institutions caused commodity prices to correct sharply, with prices of several commodities declining significantly from their peaks in the first half of 2008. As the year progressed, the decline in demand also contributed to the softening in prices of commodities.

**Chart 1**
**BNM Commodity Price Index - Level**

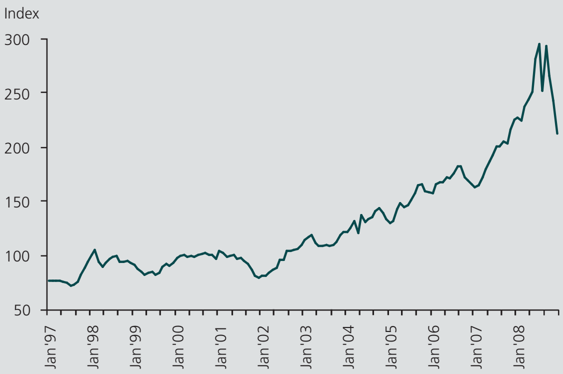
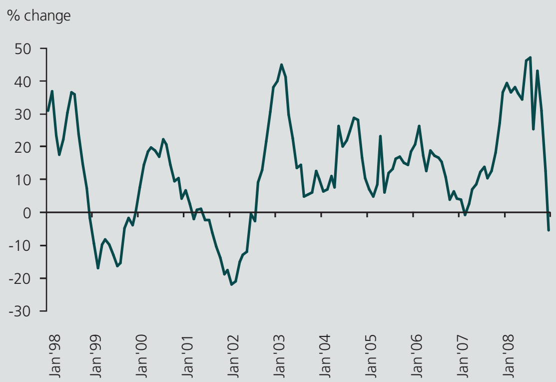



**Chart 2**
**BNM Commodity Price Index: Annual Growth**



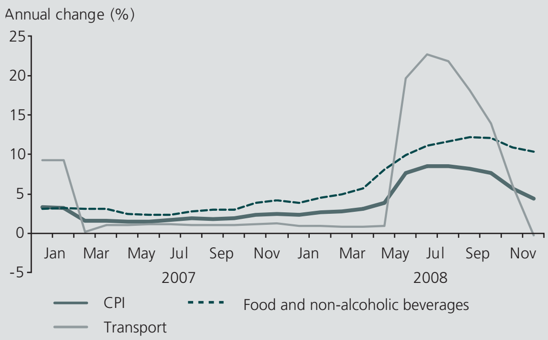

Prior to 2008, commodity prices had already been exhibiting an upward trend as seen in a gradual increase in the BNM Commodity Price Index[1] (Chart 1) since 2003, in tandem with a prolonged period of high global growth accompanied by the rapid industrialisation in several large emerging economies. Nevertheless, commodity prices accelerated sharply in unparalleled magnitudes in the first half of 2008, with the Index increasing sharply by 23.5% (Chart 2). Crude oil prices (NYMEX West Texas Intermediate) reached an all-time high of USD145 per barrel in July, 63.6% higher than in January 2008. Palm oil prices peaked at RM4,180 per tonne in March, doubling in value from a year earlier. Similarly, steel prices also doubled to over RM4,000 per tonne over the same period. However, the second half of 2008 saw a rapid reversal, with prices of most commodities declining sharply. NYMEX crude oil prices ended the year at USD44.60 per barrel, the lowest level since January 2005, while palm oil prices declined to RM1,630, the lowest level since October 2006. Accordingly, the BNM Commodity Price Index declined by 27.9% during this period.

Malaysia, as a major producer and exporter of several commodities such as palm oil, crude oil, natural gas and rubber, has been affected by this sharp increase and subsequent reversal in commodity prices. Changes in commodity prices have a heterogeneous impact on the economy – benefiting some segments while exerting negative impact on others. Key economic variables that have been affected are price levels, external trade, incomes of businesses and individuals involved in the agriculture and mining sectors, and the fiscal position of the Government.

[1] BNM Commodity Price Index is an export-weighted index (2000 = 100) of prices of major Malaysia's export commodities, namely palm oil, palm kernel oil, crude oil, natural gas, saw logs, sawn timber, cocoa, rubber and tin.

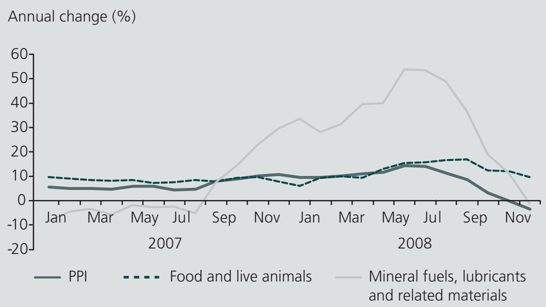
The rapid increase in global commodity and food prices exerted strong pressure on domestic price levels, both the Consumer Price Index (CPI) and Producer Price Index (PPI). While CPI inflation had already been increasing gradually in the first five months of 2008, the fuel subsidy restructuring exercise undertaken by the Government in June caused fuel prices to increase by 40.4%, resulting in a sharp increase in the headline inflation rate, which peaked at 8.5% in July. Subsequently, domestic fuel and food prices declined with the Government's downward fuel price adjustments in line with the global prices, contributing to the moderation in inflation rate to 4.4% by December. Overall, inflation averaged 5.4% in 2008, higher than the country's average long-term inflation rate of 3.0%. Reflecting the effect of commodity prices on domestic inflation, the food and non-alcoholic beverages and transport categories together accounted for 77.1% of the overall rise in domestic prices during the year. The impact of global prices of commodities was more evident in the PPI, which peaked at 14.4% in June, before declining in the second half of the year. In particular, the commodity component of the PPI reached a high of 42.5% in June before declining rapidly to -10.4% by the end of the year. To mitigate the impact of high food and fuel prices on the public, particularly the low income group, the Government introduced several measures, including subsidising prices of domestically-produced rice, subsidising fuel prices for fishermen and public transport operators, as well as providing fuel cash rebates for motorists.

**Chart 3**
**Consumer Price Index (CPI)**




Source: Department of Statistics, Malaysia

**Chart 4**
**Producer Price Index (PPI)**

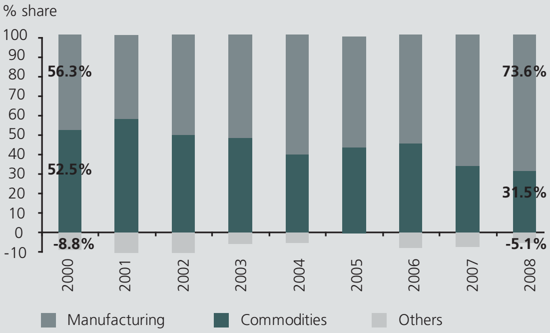



Source: Department of Statistics, Malaysia

Malaysia has over the years undertaken measures to diversify the country's export base, with manufacturing exports becoming the main export earner. Nevertheless, as a major net commodity exporter, the sharp increases in commodity prices have raised the contribution of commodities to Malaysia's exports earnings significantly. Commodity exports' share of total exports doubled to 23.5% in 2008, from 13.3% in 2000. In addition, as commodity exports have relatively low import content compared to the manufactured exports, the contribution of commodity exports to total trade balance has also increased significantly. In 2008, 73.6% of Malaysia's trade surplus of RM142 billion was contributed by exports of commodities, compared with 56.3% in 2000. The large reversal in commodity prices seen in the second half of 2008 has thus led to a significant decline in the value of gross exports of commodities.

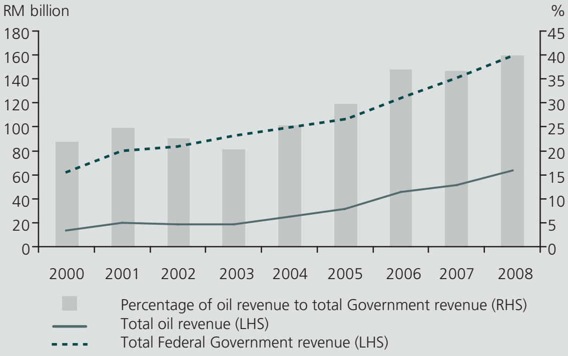
The impact of commodity prices on income levels is also substantial, with participants in both agriculture and mining sectors, including smallholders as well as plantation and oil companies, experiencing strong income growth in line with the rise in prices. Most of the major plantation companies recorded significant growth in profitability, as high as 80% on a year-to-year basis in the second quarter of 2008. Similarly, higher commodity prices, particularly palm oil and rubber, have benefited almost 270,000 smallholders involved in these activities. The average income of the Federal Land Development Authority (FELDA) settlers increased to RM3,014 per month for rubber and RM3,489 per month for palm oil in 2008 compared to the income levels of RM2,353 per month for rubber and RM1,930 per month for palm oil in 2007. However,

**Chart 5**
**Net Contribution to Trade Surplus**




Source: MATRADE

**Chart 6**
**Oil revenue contribution to Federal Government revenue**




Source: Accountant General Department

with the decline in commodity prices towards the end of 2008, profits of the plantation and mining companies were adversely affected, while incomes of the smallholders have retreated substantially, to about RM600 per month for rubber and RM750 per month for palm oil as at end-2008.

Another consequence of the sharp increase in commodity prices was the consequential rise in prices of most input materials as well as cost of investment in the mining and agriculture sectors. Oil and gas companies experienced a sharp increase in costs of rigs of about 100% in the first half of the year, as well as steel which rose by 75% during the same period. Meanwhile, the price of fertilizer increased by almost 100% in 2008. While the decline in commodity prices towards the end of 2008 has eased somewhat the cost pressures on these input materials, the concurrent decline in revenue and the reduction in margins served to limit the ability of plantation and oil companies to increase investment expenditure, with several reporting a reduction in capital spending.

The rise in oil prices also contributed significantly to the increase in Government revenue. The revenue to the Government is in the forms of petroleum income taxes, oil and gas royalties, petroleum export duties, sales taxes and dividends paid by PETRONAS. The oil revenue increased from RM13.6 billion in 2000 to RM51.2 billion in 2007. In tandem with the sharp increase in oil prices in 2008, the oil revenue amounted to RM63.7 billion in 2008 to account for 39.9% of the overall Government revenue. These higher oil-based revenue has, over the years, allowed the Government to undertake development spending on infrastructure, education and healthcare, thus contributing further to enhancing the country's long-term productive capacity. However, the large contribution of oil revenues has also increased sensitivity of fiscal revenue to movements in oil prices.

Going forward, commodity prices are expected to remain subdued in 2009, given the significant weakness in global financial and economic conditions. Malaysia, as a major commodity-exporter economy, will be affected. While lower commodity prices will continue to exert downward pressure on inflation, the lower incomes of smallholders, as well as businesses in the agriculture and mining sectors could also affect private consumption and investment expenditure. While a current account surplus is still being projected, the contribution of commodities to Malaysia's trade balance will also be affected.

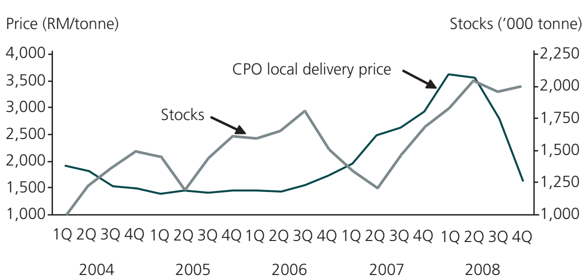
**Chart 1.14**
**Oil Palm: Area, Production and Yield**


*p* Preliminary
Source: Malaysian Palm Oil Board (MPOB)

and increased by 17.4%. Production in Sabah increased at a more moderate pace of 3.2% due to a smaller increase in acreage and no growth in FFB yields. Overall, FFB yields increased by 6% to 20.18 tonnes per hectare in 2008. With the increase in production, palm oil stocks rose substantially as well, reaching an all-time high of 2.27 million tonnes in November 2008, before ending the year at 1.99 million tonnes.

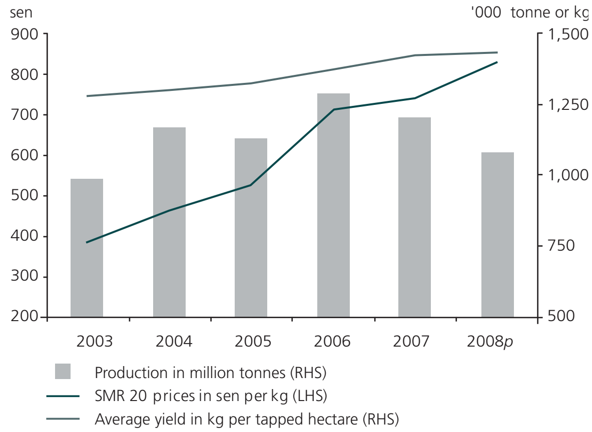
Production of **natural rubber** contracted by 10.1% to 1.08 million tonnes in 2008 due to weather-related factors in the first half of the year, as well as the sharp decline in prices in the second half of the year. In the first half of the year, there were frequent instances of heavy rainfall, particularly in the key producing region of northern Peninsular Malaysia, which disrupted tapping activities. As a result, output

**Chart 1.15**
**Palm Oil Price and Stocks**




Source: Malaysian Palm Oil Board (MPOB)

**Chart 1.16**
**Natural Rubber: Production, Prices and Yield**




*p* Preliminary
Source: Malaysian Rubber Board (MRB) and Department of Statistics, Malaysia

during this period declined by 4.7%. Rubber output declined further by 15.4% in the second half, as sharp decline in prices led to smallholders, which produced 95% of total output, to cut their production. Rubber prices declined sharply from a high of 1,053 sen per kilogramme in early July 2008 to a low of 400 sen per kilogramme in December 2008.

The **food crops** sub-sector continued to perform favourably in 2008, with fisheries and livestock sub-sectors growing by 5.2% and 4.3% respectively. Growth in the fisheries sub-sector was driven mainly by growth in aquaculture, while livestock was led by higher output of poultry. In the **forestry** sub-sector, logging activities declined further in 2008, with output of logs contracting by 16.3%, in line with the sustainable forest management policy as set by the International Tropical Timber Organisation. Meanwhile, output of **cocoa** declined by 20.5% due to a significant reduction in cultivation area in Sabah, as well as intensive replanting activities in some areas.

### Mining Sector

The value-added of the **mining sector** declined marginally by 0.8% in 2008 due to lower output of natural gas, while crude oil production registered a small increase.

Production of **crude oil (including condensates)** averaged 694,141 barrels per day (bpd) in 2008, representing an increase of 2%. The higher production was driven entirely by the doubling in

**Table 1.9**
**Mining Sector: Value Added and Production**

| | 2007 | 2008*p* |
|---|---|---|
| | Annual change (%) | |
| **Value added** | **3.3** | **-0.8** |
| **Production** | | |
| *of which:* | | |
| Crude oil and condensates | 2.4 | 2.0 |
| Natural gas | 1.9 | -4.9 |

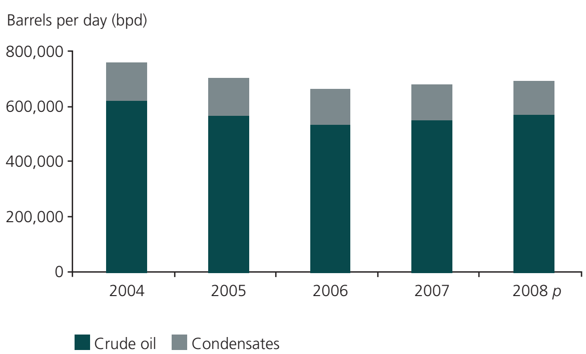
*p* Preliminary
Source: PETRONAS
Department of Statistics, Malaysia

crude oil output in Sabah to 150,792 barrels per day (bpd) (2007: 74,800 bpd). Sabah now accounts for 21.7% of total oil output. In keeping with the production limits set by the National Depletion Policy, production in Peninsular Malaysia declined by 8.9% to 337,369 bpd, to account for 49% of total output of crude oil of the country. Meanwhile, condensates continued to contribute significantly, accounting for 17.5% of the total oil production, at 121,511 bpd.

## The mining sector declined marginally due to lower natural gas output

Output of **natural gas** contracted by 4.9% to 5,579 million standard cubic feet per day due mainly to lower external demand for liquefied

**Chart 1.17**
**Production of Crude Oil and Condensates**




*p* Preliminary
Source: PETRONAS

**Table 1.10**
**Malaysia: Crude Oil and Natural Gas Reserves[1]**

| | As at 1 January | |
|---|---|---|
| | 2007 | 2008*p* |
| **Crude oil (including condensates)** | | |
| Reserves (billion barrels) | 5.36 | 5.46 |
| Reserve/Production (year) | 22 | 22 |
| **Natural gas** | | |
| Reserves (billions of barrels oil equivalent) | 14.82 | 14.67 |
| Reserve/Production (year) | 39 | 36 |

[1] The National Depletion Policy was introduced in 1980 to safeguard the exploitation of the national oil reserves by postponing the development and control the production of major oil fields (with reserves of 400 million barrels or more).
*p* Preliminary
Source: PETRONAS

natural gas (LNG). In addition, production was also affected by unplanned maintenance shutdowns at several gas fields in Peninsular Malaysia. Oil reserves in the country increased to 5.46 billion barrels or 22 years of lifespan as at 1 January 2008, suppor ted by the rising reserves from the deepwater discoveries in offshore Sabah. Meanwhile, natural gas reserves is at 14.67 billions of barrels oil equivalent (boe), sufficient to cover 36 years of gas output at current production levels.

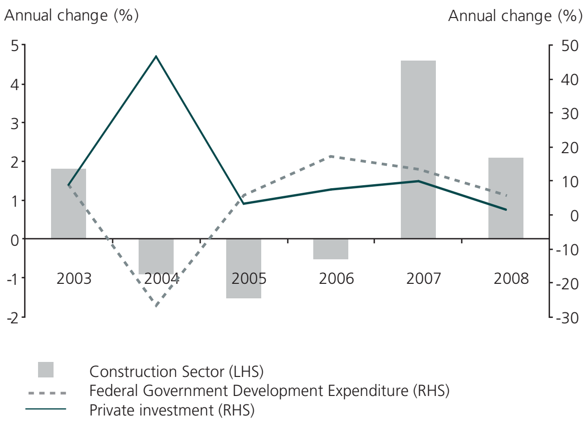
### Construction Sector

The **construction sector** recorded a positive growth rate for the second successive year, registering a growth of 2.1%. The growth was supported by higher activities across the three sub-sectors. In the **civil engineering** sub-sector, strong growth was recorded in the first half year following the implementation of projects under the Ninth Malaysia Plan (9MP) as well as those in the oil and gas industry. The Federal Government development expenditure increased by 23.5% in the first half year of 2008, mainly to finance construction of new projects and upgrading of existing infrastructure facilities. The oil and gas industry continued to experience higher activity, especially in building rigs, platforms and storage terminals.

## The construction sector growth remained positive in 2008

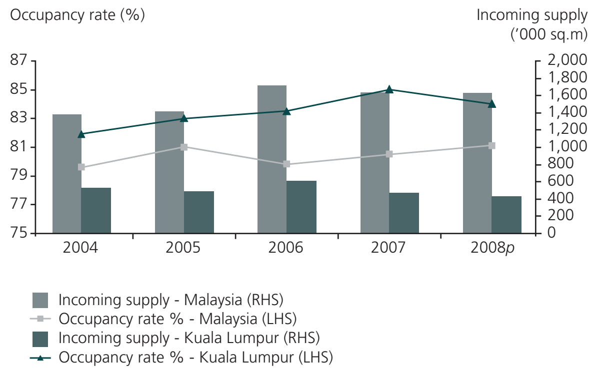
In the second half of the year, the civil engineering sub-sector was affected by the sharp increase in prices of construction materials, particularly steel

**Chart 1.18**
**Value-add Growth in Construction Sector versus Growth in Federal Government Development Expenditure and Private Investment**




Source: Department of Statistics, Malaysia and Accountant General's Department

**Chart 1.19**
**Incoming Supply and Occupancy Rate of Retail Space in Malaysia and Kuala Lumpur (as at end period)**



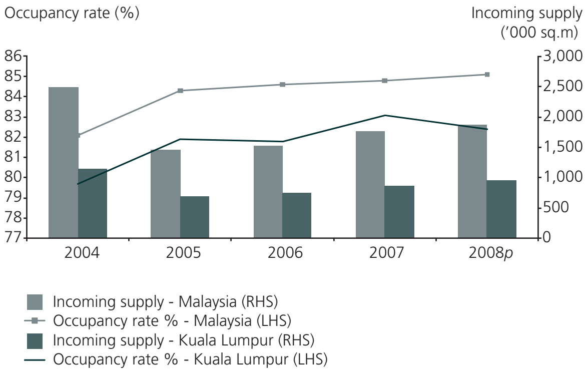

*p* Preliminary
Source: National Property Information Centre (NAPIC), Valuation and Property Services Department

and cement. Following sharp increases in global prices of building materials, the Government decided to liberalise the pricing structure of both steel and cement in May and June 2008, resulting in a sharp rise in the prices of these materials. As a result, many existing projects experienced a slowdown in construction while companies were reluctant to bid for new projects due to fluctuating costs. To ensure that the implementation of Government projects was completed as planned, the Government issued an update to the Variation of Price (VoP) clause

**Table 1.11**
**Measures Introduced in the Construction Sector in 2008**

| Announcement Date | Measures |
|---|---|
| Liberalisation in steel industry<br>12 May 2008 | • Abolishment of ceiling prices on steel bars and billets<br>• Allow import of long steel products without the requirement of an AP (Approval Permit) and abolishment of import duty for steel bars under the HS Code 7214.10 910 and 7214.20 910 |
| Liberalisation in cement industry<br>5 June 2008 | • Abolishment on ceiling price of cement<br>• Import duty reduced to 10% from 50% in non-Asean countries<br>• The liberalisation is effective on the following cement only:<br>- HS 2523 29 900 (ordinary Portland cement); and<br>- HS 2523 90 000 (hydraulic cement).<br>• Cement importers in Sabah and Sarawak are excluded from obtaining license (Approval Permit) to import |
| Adjustment to the Variation of Price (VOP) Clause Specifications<br>August 2008 | • Expanded to include design and build projects on 50:50 cost sharing basis<br>• The materials that come under VOP scheme can be categorised under:<br>1) Civil Works - 11 items from the previous 5 items<br>2) Building Works - 15 items<br>3) Mechanical and Electrical Works - 7 items<br>• The ruling is applicable for Government projects implemented after 1 January 2008, including design and build projects on 50:50 cost sharing basis |
| First Stimulus Package<br>4 November 2008 | • 10% import duty on cement abolished<br>• Import duty of another 54 HS Codes for long steel products abolished<br>• All imports must comply with Malaysian Standards (MS) or recognised International Standards if MS is not available |

**Chart 1.20**
**Incoming Supply and Occupancy Rate of Purpose-Built Office Space in Malaysia and Kuala Lumpur (as at end period)**




*p* Preliminary
Source: National Property Information Centre (NAPIC), Valuation and Property Services Department

for these projects in August 2008. This initiative, along with the moderation in steel prices towards the end of the year, revived somewhat the confidence in the construction industry.

Growth in the **non-residential** sub-sector was robust, driven primarily by the office segment. Strong business activities at the beginning of the year provided businesses with the room to expand, resulting in higher demand for prime grade office buildings in the Klang Valley. Occupancy rate was higher at 85.1% in 2008 (2007: 84.8%) while rental rates increased to a high of RM10 to RM12 per square feet. A total of 24 new office buildings were completed, while incoming supply was at 1.9 million square metres as at end- 2008. Resilient private consumption contributed to a sustainable retail market. In total, 29 new shopping complexes

**Table 1.12**
**Demand and Supply Indicators of the Residential Property Market**

| | 1H '07 | 2H '07 | 1H '08 | 2H '08 |
|---|---|---|---|---|
| Annual change (%) | | | | |
| Demand indicators | | | | |
| **Residential property transactions** | | | | |
| Value (RM million) | 10.5 | 35.9 | 35.5 | -3.0 |
| Volume | 1.7 | 16.3 | 20.7 | -1.2 |
| **Finance for purchase of residential property** | | | | |
| Loan applications | 38.4 | 57.2 | 43.9 | 12.2 |
| Loan approvals | 27.8 | 65.3 | 43.1 | 7.3 |
| Supply indicators | | | | |
| **New launches** | **8.2** | **62.6** | **25.0** | **-33.7** |
| **New sales and advertising permits** | **0.4** | **3.6** | **2.0** | **-38.6** |
| **Housing approvals** | **-17.5** | **-5.3** | **19.0** | **-52.6** |
| **Loans for construction** | | | | |
| Loan applications | 67.5 | 35.7 | 22.2 | -30.0 |
| Loan approvals | 94.8 | 32.6 | 20.5 | -19.8 |

Source: Bank Negara Malaysia, National Property Information Centre (NAPIC), Valuation and Property Services Department, Ministry of Housing and Local Government.

**Table 1.13**
**Overhang of Residential Property in Malaysia by Price Range**

| **Residential Price Range** | Units | Share (%) | Units | Share (%) |
|---|---|---|---|---|
| | As at end-2007 | | As at end-2008*p* | |
| RM50,000 or less | 3,356 | 14.0 | 3,602 | 13.8 |
| RM50,001 - RM100,000 | 7,151 | 29.8 | 7,491 | 28.8 |
| RM100,001 - RM150,000 | 4,284 | 17.9 | 4,045 | 15.5 |
| RM150,001 - RM200,000 | 3,639 | 15.2 | 3,786 | 14.6 |
| RM200,001 - RM250,000 | 1,778 | 7.4 | 2,119 | 8.1 |
| RM250,001 - RM500,000 | 2,920 | 12.2 | 3,888 | 14.9 |
| RM500,001 - RM1,000,000 | 776 | 3.2 | 993 | 3.8 |
| More than RM1,000,000 | 93 | 0.4 | 105 | 0.4 |
| **Total** | **23,997** | **100** | **26,029** | **100** |

*p* Preliminary

Source: National Property Information Centre (NAPIC), Valuation and Property Services Department were completed increasing the stock level to 9.2 million square metres as at end- 2008 (2007: 8.6 million square metres). Rentals were relatively stable, while tenants had several options in terms of location and type of properties. Occupancy rate increased slightly to 81.1% in 2008 (2007: 80.5%).

Performance in the **residential** segment was relatively mixed during the year. In the first half of 2008, demand for properties was strong, with property transactions increasing by 35.5%. Nevertheless, demand for properties began to soften in the second half year as consumer sentiment started to decline, first as a result of rising inflationary pressures and later, the deteriorating global economic conditions. Demand for properties in the high-end segment of the market was especially affected. As a result, property transactions reversed and registered a decline of 3% in value terms in the second half. The moderation in demand was also observed in terms of property overhang. Overall overhang level increased by 8.5% in 2008, with property overhang of prices above RM200,000 experiencing a sharp increase of 27.6% to 7,105 units (2007:5,567 units). Property developers reacted cautiously to the softening demand by reducing the number of launches of new developments which led to lower housing approvals and demand for bridging loans. In addition, property developers were affected by increases in construction cost following the liberalisation in prices of cement and steel, which led to some delays in the implementation of existing and new projects.

## EXTERNAL SECTOR

### Balance of Payments

Malaysia's external position remained resilient in 2008, despite a weak external environment in the second half of the year. The current account recorded another large surplus, while the reversal

**Table 1.14**
**Balance of Payments**

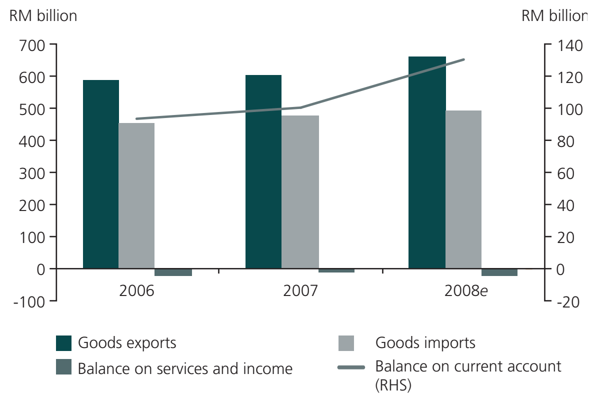
| Item | 2007 | | | 2008e | | |
|---|---|---|---|---|---|---|
| | + | - | Net | + | - | Net |
| | RM billion | | | | | |
| Goods | 605.9 | 478.2 | 127.7 | 664.2 | 494.1 | 170.1 |
| *Trade account* | *605.2* | *504.8* | *100.3* | *663.5* | *521.6* | *141.9* |
| Services | 101.2 | 98.9 | 2.4 | 102.2 | 100.5 | 1.7 |
| **Balance on goods and services** | **707.2** | **577.1** | **130.0** | **766.4** | **594.5** | **171.8** |
| Income | 38.8 | 52.7 | -13.9 | 39.1 | 64.5 | -25.4 |
| Current transfers | 1.4 | 17.2 | -15.7 | 1.4 | 18.5 | -17.0 |
| **Balance on current account** | **747.4** | **647.0** | **100.4** | **806.9** | **677.5** | **129.4** |
| **% of GNI** | | | **16.0** | | | **18.1** |
| Capital account | | | -0.1 | | | 0.6 |
| Financial account | | | -37.7 | | | -123.9 |
| Direct investment | | | -9.1 | | | -20.5 |
| Portfolio investment | | | 18.4 | | | -92.4 |
| Other investment | | | -46.9 | | | -11.0 |
| **Balance on capital and financial accounts** | | | **-37.8** | | | **-123.3** |
| Errors and omissions | | | -17.3 | | | -24.3 |
| *of which:* | | | | | | |
| *Foreign exchange revaluation gain (+) or loss (-)* | | | *-5.6* | | | *-5.8* |
| **Overall balance** | | | **45.3** | | | **-18.2** |
| **Bank Negara Malaysia international reserves, net** | | | **335.7** | | | **317.4** |
| **USD billion equivalent** | | | **101.3** | | | **91.5** |

e Estimate
Note: Numbers may not necessarily add up due to rounding
Source: Department of Statistics, Malaysia and Bank Negara Malaysia

of short-term capital flows in the second half of the year resulted in a net outflow in the financial account. The **overall balance of payments** recorded a deficit as the higher net outflow in the financial account more than offset the larger surplus in the current account.

The larger current account surplus of RM129.4 billion or 18.1% of GNI was due to a higher trade surplus and sustained surplus in the services account. The income account, however, recorded a larger deficit following higher profits and dividends accruing to the MNCs operating in Malaysia.

**Chart 1.21**
**Current Account**




*e* Estimate
Source: Department of Statistics, Malaysia and Bank Negara Malaysia

## Malaysia's external position remained resilient in 2008, despite a weak external environment in the second half of the year

The financial account recorded a larger net outflow due to the significant liquidation of portfolio investment by foreign investors, particularly in the second half of 2008, following deleveraging activities as the global financial turmoil intensified. During the year, net direct investment abroad by Malaysian companies increased, mainly through acquisition of interests and expansion of existing operations abroad. Meanwhile, the net inflows of foreign direct investment (FDI) moderated, particularly in the second half-year, in tandem with the deterioration in the global economic and financial conditions. After adjusting for errors and omissions, which include the foreign exchange revaluation loss arising from the revaluation of the international reserves due to the strengthening of the ringgit against some major currencies, the net international reserves declined by RM18.2 billion to RM317.4 billion or equivalent to USD91.5 billion as at 31 December 2008. As at 27 February 2009, the reserves remained at a comfortably high level of RM315.9 billion (equivalent to USD91.1 billion), adequate to finance 7.6 months of retained imports and cover 3.9 times of the short-term external debt. Malaysia's reserves remain usable and unencumbered.

### Current Account

The **current account** recorded a larger surplus of RM129.4 billion or 18.1% of GNI (2007: RM100.4 billion or 16% of GNI), supported by a significantly higher trade surplus and sustained surplus in the services account. Stronger growth in both commodities and resource-based manufacturing exports, particularly in the first half of 2008 due to high commodity prices, contributed to a larger trade surplus. The services account surplus was due mainly to higher tourism receipts from 22.1 million visitors. The larger deficit in the income account reflected mainly higher profits and dividends accruing to the MNCs operating in Malaysia, particularly in the manufacturing, oil and gas, and services sectors.

## The larger current account surplus was underpinned by strong exports of commodities and resource-based manufacturing products as well as higher tourism receipts

**Gross exports** increased by 9.6% in 2008 (2007: 2.7%), led by the expansion in both commodities and resource-based manufacturing exports. In the first half of 2008, **manufactured exports** grew by 7.8%, supported mainly by regional demand for resource-based manufacturing exports. However, in the second half-year, the ensuing weakness in global demand and easing of commodity prices led to a marginal decline in manufactured exports

**Table 1.15**
**Gross Exports**

| | 2007 | 2008p |
|---|---|---|
| | Annual change (%) | |
| **Gross exports** | **2.7** | **9.6** |
| **Manufactures** | **0.3** | **3.6** |
| *of which:* | | |
| *Electronics* | *-3.5* | *-8.2* |
| *Semiconductors* | *3.2* | *-6.9* |
| *Electronic equipment and parts* | *-8.4* | *-9.3* |
| *Electrical products* | *-5.9* | *8.6* |
| *Resource-based products*[1] | *9.7* | *20.2* |
| **Commodities** | **14.7** | **37.1** |
| **Agriculture** | **24.4** | **30.0** |
| *of which:* | | |
| *Palm oil* | *47.8* | *43.7* |
| *Rubber* | *-10.9* | *10.6* |
| **Minerals** | **7.5** | **43.2** |
| *of which:* | | |
| *Crude oil and condensates* | *3.5* | *35.0* |
| *LNG* | *12.3* | *55.7* |

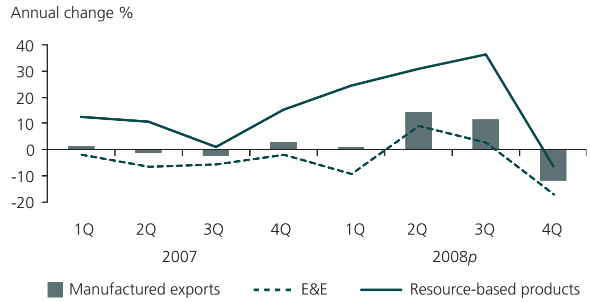
[1] Refers to food, beverages and tobacco products, wood products, furniture and parts, rubber products, petroleum products, chemicals and chemical products and non-metallic mineral products
*p* Preliminary

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

of 0.2%. For the year as a whole, exports of **electronics and electrical (E&E)** products contracted by 3.8%, as the decline in exports of electronics more than offset the strong recovery in exports of electrical products. The exports of semiconductors were affected by weak demand for electronic equipment and parts from the advanced economies, particularly in the second half of the year, as well as lower prices. Electrical exports, however, expanded strongly by 8.6%, driven by consumer electrical goods as well as industrial and commercial electrical products. Product innovation which led to a shift to higher value-added products, as well as penetration to new export markets, notably the United Arab Emirates, Saudi Arabia, India and Australia, contributed towards the expansion in electrical exports.

Exports of **non-E&E** products strengthened by 15.2%, in line with higher input prices of commodities and sustained demand from regional countries. In the first half-year, exports of non-E&E

**Chart 1.22**
**Export Performance of Electronics & Electrical (E&E) and Resource-Based Industries**



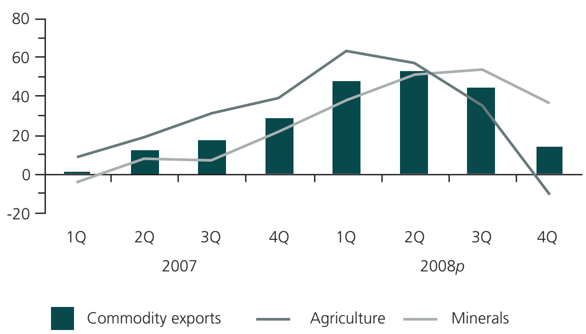

*p* Preliminary
Source: Department of Statistics, Malaysia and Bank Negara Malaysia

products, particularly resource-based products such as rubber, petroleum, and chemicals and chemical products, increased by 20%. Growth was also supported by exports of construction-related products, such as manufactures of metal amidst booming construction activity in PR China, Vietnam and Singapore. In the second half-year, growth in exports of non-E&E products moderated to 10.8%, following the decline in commodity prices.

Exports of **primary commodities** expanded strongly by 37.1% and accounted for a higher share of gross exports of 23.5% (2007: 18.8%). In the first half of the year, commodity exports expanded strongly by 50.2%, driven mainly by significantly higher prices of palm oil, rubber, crude oil and LNG. Despite a marked softening of commodity prices in the second half of 2008, the growth in commodity exports remained strong at 26.9%, supported mainly by LNG exports.

**Agriculture exports** strengthened by 30%, led mainly by strong exports of palm oil and rubber. In the first half of 2008, export earnings from palm oil surged by 90.9%, underpinned by sharply higher prices (+53% to an average of RM3,140 per tonne) and exports volume (+24.8%). Exports of rubber expanded by 26.2%, attributable mainly to higher prices (+20.9% to an average of 846 sen per kilogramme), amidst low global stocks in major producing regions and rising demand. In the second half of 2008, the growth of agriculture exports moderated to 10%, as prices of major agricultural commodities eased significantly.

**Chart 1.23**
**Commodity Export Performance**




*p* Preliminary
Source: Department of Statistics, Malaysia

**Mineral exports** recorded a robust growth of 43.2% in 2008, reflecting mainly higher prices and export volume of crude oil, particularly in the first half-year. Higher price of LNG as well as the continued demand by Korea and Japan mitigated the moderate growth of crude oil exports in the second half-year.

**Gross imports** increased by 3.3% (2007: 5%) due mainly to higher imports of inputs for manufactured exports and consumption goods. Imports of **intermediate goods**, which account for 72.7% of gross imports, expanded by 5.7%. Strong demand by resource-based industries led to an increase in imports of fuel and lubricants as well as chemicals. Consistent with strong domestic consumption, imports of food and beverages for industry expanded. Increased activity in the construction sector, underpinned the imports of industrial supplies, particularly metals. In tandem with the lower global demand for E&E products, imports of parts and accessories of capital goods declined.

Imports of **capital goods** were broadly unchanged (2007: 7.2%), with imports of transportation equipment contracting. Excluding lumpy items, capital imports expanded by 4.3% in 2008. In the first half-year, capital imports expanded strongly by 9.6%, mainly for the oil and gas, manufacturing, and telecommunication sectors. Increased exploration and development activities in the oil and gas industry amidst high crude oil prices resulted in higher imports of construction and mining equipment. In the manufacturing sector, higher imports of machinery were in tandem with continued expansion in capacity. Investments for upgrading in new technologies led to growth in imports of telecommunication equipment. Capital imports, however, declined in the second half of the year as the deterioration in the global economic conditions led to the postponement of capacity

**Table 1.16**
**Imports by End-Use**

| | 2007 | 2008*p* |
|---|---|---|
| | Annual change (%) | |
| **Capital goods** | **7.2** | **...** |
| Capital goods (except transport equipment) | 5.6 | 2.2 |
| Transport equipment | 17.8 | -13.6 |
| **Intermediate goods** | **6.9** | **5.7** |
| Food and beverages, mainly for industry | 21.0 | 30.0 |
| Industrial supplies, n.e.s. | 17.0 | 9.7 |
| Fuel and lubricants | 2.0 | 32.0 |
| Parts and accessories of capital goods (except transport equipment) | 0.4 | -5.0 |
| **Consumption goods** | **3.6** | **11.8** |
| Food and beverages, mainly for household consumption | 6.8 | 21.4 |
| Consumer goods, n.e.s. | 1.8 | 5.5 |
| **Re-exports** | **-22.4** | **-14.6** |
| **Gross Imports** | **5.0** | **3.3** |

n.e.s. Not elsewhere specified
*p* Preliminary
... Negligible

Source: Department of Statistics, Malaysia

**Table 1.17**
**Direction of External Trade**

| | 2008*p* | | | | |
|---|---|---|---|---|---|
| | Exports | | Imports | | Trade balance |
| | RM billion | Annual change (%) | RM billion | Annual change (%) | RM billion |
| **Total** | **663.5** | **9.6** | **521.6** | **3.3** | **141.9** |
| *of which:* | | | | | |
| **United States** | **82.5** | **-12.7** | **56.5** | **3.2** | **26.1** |
| **European Union (EU)** | **74.9** | **-3.8** | **61.7** | **2.9** | **13.2** |
| **Selected ASEAN countries**[1] | **169.6** | **9.9** | **125.8** | **2.5** | **43.8** |
| **Selected North East Asia countries** | **133.6** | **10.9** | **129.9** | **-2.5** | **3.8** |
| *The People's Republic of China* | *63.2* | *19.2* | *66.9* | *3.0* | *-3.7* |
| *Hong Kong SAR* | *28.3* | *1.2* | *13.7* | *-6.9* | *14.7* |
| *Chinese Taipei* | *16.2* | *-1.4* | *25.1* | *-12.6* | *-8.9* |
| *Korea* | *25.9* | *12.4* | *24.2* | *-2.8* | *1.7* |
| **West Asia** | **26.1** | **38.0** | **25.1** | **44.4** | **1.0** |
| **Japan** | **71.8** | **30.0** | **65.1** | **-0.6** | **6.7** |
| **India** | **24.7** | **22.4** | **10.3** | **45.8** | **14.4** |

*p* Preliminary
[1] Singapore, Thailand, Indonesia, Philippines, Brunei Darussalam and Vietnam
Note: Numbers may not necessarily add up due to rounding
Source: Department of Statistics, Malaysia

expansion in the manufacturing, transportation, and oil and gas sectors.

Imports for **consumption goods** expanded by 11.8% in tandem with continued growth in private consumption. The growth in consumption imports reflected largely demand for imports of food and beverages. Imports of consumer goods, particularly clothing and footwear, household furnishing and medicines, were also higher.

In 2008, trade with major trading partners, namely the US, EU and Japan accounted for a lower share of Malaysia's total trade (34.8%; 2007: 36.7%). In contrast, trade links with North East Asia (excluding Japan), West Asia, India, Australia and New Zealand had strengthened substantially. Trade with North East Asia (excluding Japan) was underpinned by growth in exports of E&E components and commodities, particularly to PR China and Korea. Of significance, exports to West Asia, comprising mainly consumer electrical products, palm oil, jewellery and processed food, recorded a robust growth of 38%. Exports to India also registered a strong growth, supported largely by demand for crude petroleum, chemicals and chemical products, as well as palm oil. Exports to Australia and New Zealand consisted largely of crude oil and electrical products.

Trade with ASEAN countries remained robust, with total trade expanding by 6.6% in 2008, driven mainly by demand for energy, food and inputs for the manufacturing industry. Exports to the ASEAN countries increased by 9.9% and accounted for 25.6% of Malaysia's total exports. Exports to Indonesia and Philippines expanded strongly by 16.8% and 11.7% respectively, supported by exports of crude petroleum, chemicals and chemical products, as well as palm oil.

In 2008, the **services account** registered its second consecutive year of surplus of RM1.7 billion or 0.2% of GNI. This reflected a sustained large surplus from travel account and an improvement in other services deficit, which more than offset a higher deficit in the transportation account.

Despite greater competition in the tourism industry in the region and higher costs of travel, particularly in the first half of 2008, tourist arrivals increased to a record level of 22.1 million

**Table 1.18**
**Services and Income Accounts**

| | 2007 | 2008e | | |
|---|---|---|---|---|
| | RM billion | | | |
| | Net | + | - | Net |
| **Services Account** | **2.4** | **102.2** | **100.5** | **1.7** |
| *% of GNI* | *0.4* | | | *0.2* |
| Transportation | -13.2 | 23.0 | 37.6 | -14.6 |
| Travel | 29.1 | 50.7 | 22.5 | 28.2 |
| Other services | -13.2 | 28.3 | 39.6 | -11.3 |
| Government transactions n.i.e. | -0.4 | 0.1 | 0.7 | -0.6 |
| **Income Account** | **-13.9** | **39.1** | **64.5** | **-25.4** |
| *% of GNI* | *-2.2* | | | *-3.6* |
| Compensation of employees | -0.6 | 4.4 | 5.2 | -0.7 |
| Investment income | -13.3 | 34.7 | 59.4 | -24.7 |

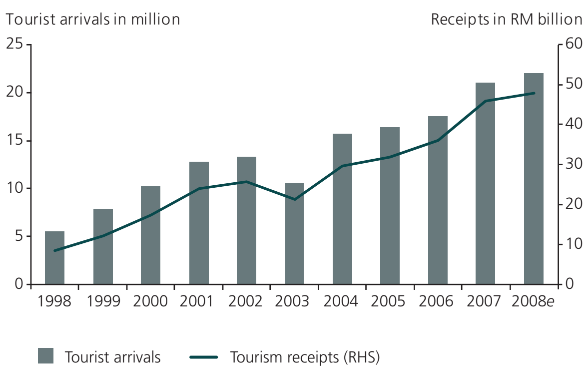
n.i.e. Not included elsewhere
*e* Estimate
Note: Numbers may not necessarily add up due to rounding
Source: Department of Statistics, Malaysia and Bank Negara Malaysia

visitors in 2008. While tourist arrivals continued to be largely from the region, particularly ASEAN, PR China, Japan and India, long-haul tourists from the Western and Northern Europe have also increased. Extension of the Visit Malaysia Year 2007 campaign until August 2008 and concerted promotional efforts to diversify from traditional markets led to higher tourist arrivals. Promotion was aimed at new and emerging niche segments such as homestay, student travel, wellness tourism and eco-tourism. Increased air service connectivity, particularly by low cost carriers, facilitated travel in the region.

The other services account recorded a lower deficit of RM11.3 billion, stemming mainly from lower net outflows for royalties and licence fees, construction and communication services, as well as improvement in net inflows from IT services. During the year, the lower net outflows for royalties and licence fees reflected sustained payments for acquisition and usage of intellectual property rights which was offset partially by higher receipts due to royalties from oil exploration projects. Meanwhile, net outflows for construction services declined, following lower demand for imported construction services, and in line with the downsizing of deep sea oil and gas exploration projects amidst higher cost of building materials. The improvement in receipts from IT services was attributed mainly to shared services and outsourcing activities in Malaysia. Lower reliance on services and facilities provided by foreign telecommunication operators, following continuous capacity expansion in domestic broadband networks, led to a smaller deficit in communication services. Payments for professional services were larger due mainly to imports of project consultancy services by the oil and gas sector, and construction sub-sector.

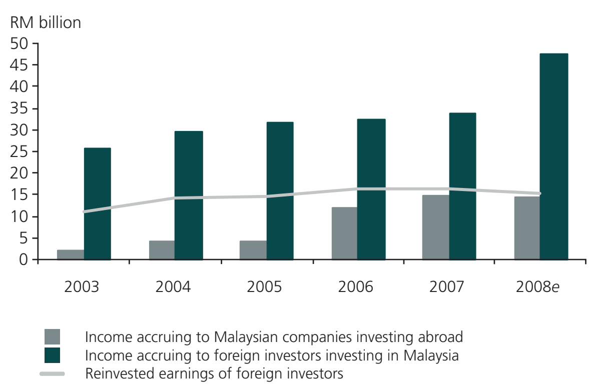
The sustained surplus in the travel account and improvement in the other services account were partially offset by a higher deficit in the transportation account of RM14.6 billion. The larger deficit in transportation account was due to lower earnings from passenger fares while payments for freight charges increased following higher fuel prices.

**Chart 1.24**
**Tourist Arrivals and Tourism Receipts**




*e* Estimate
Source: Malaysia Tourism Promotion Board and Department of Statistics, Malaysia

**Chart 1.25**
**Direct Investment Income**




*e* Estimate
Source: Department of Statistics, Malaysia and Bank Negara Malaysia

The **income account** deficit widened to RM25.4 billion or 3.6% of GNI, reflecting mainly higher profits and dividends accruing to foreign direct investors in Malaysia. This was contributed by the strong performance of the manufacturing, oil and gas, and services sectors, particularly in the first half of 2008. Profits and dividends accruing to Malaysian companies investing abroad were sustained while returns on holdings of international reserves improved moderately, despite deterioration in the global economic and financial conditions in the second half-year. The bulk of the profits and dividends accruing to Malaysian companies were from investments in the oil and gas sector, and financial services sub-sector.

**Table 1.19**
**Balance of Payments: Financial Account**

| | 2007 | 2008e |
|---|---|---|
| | RM billion | |
| **Financial Account** | **-37.7** | **-123.9** |
| **Direct Investment** | **-9.1** | **-20.5** |
| Abroad | -38.2 | -47.1 |
| In Malaysia | 29.1 | 26.7 |
| **Portfolio Investment** | **18.4** | **-92.4** |
| **Other Investment** | **-46.9** | **-11.0** |
| Official sector[1] | -5.8 | -2.7 |
| *Federal Government* | *-2.3* | *-0.5* |
| *NFPEs* | *-3.5* | *-2.2* |
| Private sector | -41.1 | -8.3 |

[1] Excludes bonds and notes raised abroad by the Federal Government and NFPEs
*e* Estimate
Note: Numbers may not necessarily add up due to rounding
Source: Department of Statistics, Malaysia and Bank Negara Malaysia

## Financial Account

In 2008, the **financial account** recorded a larger net outflow of RM123.9 billion, due mainly to the reversal of portfolio funds which were received in 2007 and the early part of 2008. The large capital reversal, particularly in the second half of 2008, was due to the deleveraging activities by foreign financial institutions as the global financial crisis worsened. There was also higher direct investment abroad by Malaysian companies, in particular in the finance and insurance sub-sector following expansion of operations in the Asian region, as well as in the utilities sub-sector and oil and gas sector. Meanwhile, net inflows of foreign direct investment (FDI) moderated, particularly in the second half-year, following the deterioration in the global economic and financial conditions.

### The larger net outflow in the financial account was due mainly to the reversal of portfolio funds which were received in 2007 and the early part of 2008

For the year as a whole, **portfolio investment** registered a large net outflow of RM92.4 billion, attributed mainly to the liquidation of portfolio investment due to deleveraging activities by foreign financial institutions following the deepening global financial crisis. In the first quarter, there was a net inflow of foreign portfolio funds amounting to RM21.1 billion, mainly for investment in the debt securities market which more than offset the net outflows from the equity market. The subsequent intensification of the global financial crisis in the second and third quarters triggered wide scale global deleveraging activity. This resulted in a significant liquidation of portfolio investment from the Asia-Pacific markets, including Malaysia. The reversal of short-term capital flows, particularly in the third quarter was well absorbed with limited disruption to the domestic financial markets and the real sector of the economy. In the fourth quarter, net outflow of portfolio investment moderated as the global deleveraging activities, which peaked in October, subsided towards the end of the year.

Gross inflows of **FDI** increased to RM51 billion (or 7.1% of GNI) during the year. While strong inflows of FDI were recorded in the first half of 2008, the deterioration in the global economic and financial conditions moderated FDI inflows in the second half of the year. FDI continued to be broad-based, and channeled largely into the manufacturing (45% share), services (27%) and oil and gas (26%) sectors. After taking into account the adjustments for outflows due largely to loan repayments to parent companies, net inflows of FDI moderated to RM26.7 billion or 3.7% of GNI (2007: RM29.1 billion).

In the *manufacturing sector*, inflows of FDI in the first half-year increased and were funded mainly by retained earnings as well as new inflows of equity capital. The bulk of FDI was channeled into the E&E industry, undertaken largely by existing companies for the purpose of upgrading of equipment and

**External Resilience: An International Balance Sheet Perspective**

**Introduction**

One of the key strengths of Malaysia's economy lies in its strong external position. Despite the on-going global financial turmoil and the consequent deleveraging activities which had caused an outflow of capital from emerging economies, the external position of Malaysia remains resilient. This is reflected in a sustained sizeable current account surplus, a relatively low level of external debt and a high level of international reserves.

**Assessment from the international balance sheet perspective**

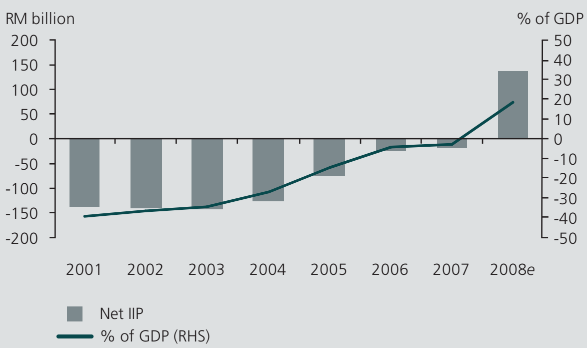
In addition to the traditional flow-based analysis of the balance of payments, the strength of the external sector could be analysed from the international balance sheet perspective. The international balance sheet is generally represented by the international investment position (IIP), which measures the stocks of the external financial assets and liabilities of a country. Analysis of the size and composition of the IIP facilitates identification of possible sources of vulnerability in the country's external financial position in the event of a shock.

During the period 2001-2008, Malaysia's external position has improved substantially (Chart 1). The net IIP of Malaysia strengthened from a large net liabilities position of RM137.6 billion as at end-2001 to a small net liabilities position of RM18.2 billion as at end-2007. This position improved further to a net assets position of RM138.3 billion as at end-2008. The improvement in the external position was due to faster accumulation of external financial assets relative to the build up in the external financial liabilities.

Since 2001, the **total external financial assets** of Malaysia more than tripled to RM778.4 billion as at end-2008 (Chart 2). The large increase was due mainly to:

i. the higher direct investment abroad by Malaysians, at RM240.3 billion (or 32.4% of GDP) and accounted for 30.9% of the total external financial assets as at end-2008, reflecting the diversification and expansion of Malaysian companies abroad. These investments have yielded positive results as shown by the rising profits and dividends accruing to the Malaysian companies from their operations abroad (2008: +RM14.4 billion; 2001: -RM0.2 billion); and

**Chart 1**
**Net International Investment Position (IIP)**




*e* Estimate
Source: Department of Statistics, Malaysia and Bank Negara Malaysia

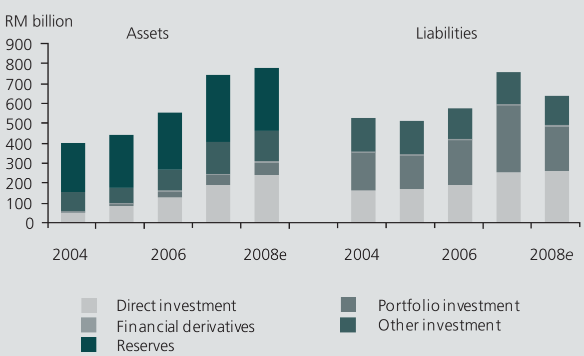
ii. the large build up in international reserves to RM317.4 billion as at end-2008, which accounted for 40.8% of the total external financial assets. The accumulation of reserves since 2001 was attributed largely to the favourable current account surplus and steady inflows of foreign direct investment (FDI). The increase in reserves was also contributed by large inflows of portfolio funds, particularly in 2007 and early part of 2008. Nevertheless, these inflows were subsequently reversed in the second half of 2008 due to the deleveraging activities following the intensification of the global financial turmoil.

Meanwhile, the **total external financial liabilities** almost doubled during the period 2001-2008, to RM640.1 billion as at end-2008. The increase reflected mainly inflow of long-term capital as well as foreign investment in the domestic capital market. During this period, Malaysia received a net inflow of FDI at an average of 3.1% of GDP, and the stock of FDI increased from RM129.1 billion to RM262 billion (or 35.4% of GDP) as at end-2008, reflecting Malaysia as an attractive destination for FDI. The external debt of the economy continues to be low, at 31.8% of GDP as at end-2008, with the debt profile remaining skewed towards a longer maturity structure. Following the recent large reversal of capital flows, a significant proportion of the remaining foreign investment in the domestic capital markets reflect the strategic long-term holdings by foreign investors.

The assessment of the external position indicates limited risks arising from maturity, currency and capital structure mismatches.

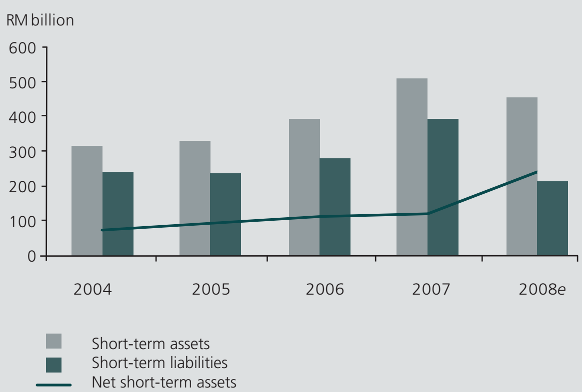
- The sustained net short-term assets position indicates minimum risks of maturity mismatch (Chart 3). The larger short-term assets relative to liabilities demonstrates the strong ability of the economy to service its maturing short-term external obligations, and thus, is unlikely to face liquidity constraints.
- The total foreign currency assets of the economy far outweigh the total foreign currency liabilities (Chart 4). This indicates a low risk of currency mismatch, and therefore, reduced vulnerability to exchange rate shocks.
- From the capital structure perspective, external financing in the form of debt is smaller than that of equity (Chart 5). The increase in the debt-to-equity ratio in 2008 was due mainly to large liquidation of non-strategic equity holdings by foreign investors following the global deleveraging activities in the second half of 2008. The relatively higher external financing through equity reduces solvency risk as equity obligations, in the form of profits and dividends, are not mandatory. In contrast, debt obligations, in terms of the debt servicing and repayment schedule, remain generally unchanged even under adverse economic conditions.

**Chart 2**
**International Investment Position by Broad Components**




*e* Estimate
Source: Department of Statistics, Malaysia and Bank Negara Malaysia

**Chart 3**
**Short-term Assets and Liabilities**



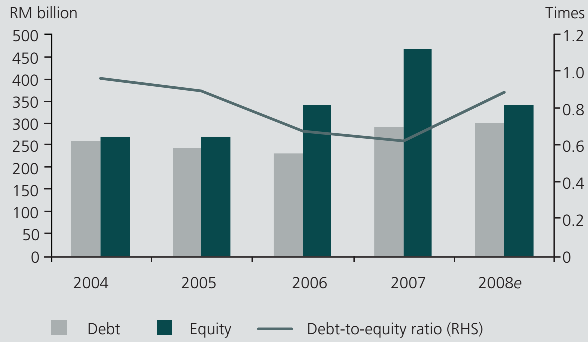

*e* Estimate
Source: Department of Statistics, Malaysia and Bank Negara Malaysia

**Chart 4**
**Foreign-currency Assets and Liabilities**


*e* Estimate

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

**Chart 5**
**Capital Structure of External Liabilities**




*e* Estimate

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

**Role of policy in strengthening the external position**

The increasing resilience of Malaysia's external sector could be attributed to the policies and strategies adopted, in particular, the further liberalisation of the capital account. The liberalisation has been undertaken on a gradual and sequential basis, taking into consideration the state of the domestic economy, the level of development of the domestic financial system, the strength of the balance of payments position and global developments. Prudential rules are in place to ensure sound external debt management, particularly to reduce risks associated with large external obligations, servicing ability and uncovered positions. While the business and investment climate is continuously being improved to attract FDIs, local companies are also encouraged to invest abroad to expand business opportunities available in the regional and international markets, establish market presence globally and provide greater synergy to domestic businesses. With the increase in international reserves and complexity of asset classes and instruments amidst the challenging operating environment, the reserves management strategy and practices have progressively been enhanced to improve risk adjusted returns while maintaining the traditional objectives of capital and liquidity preservation.

**Conclusion**

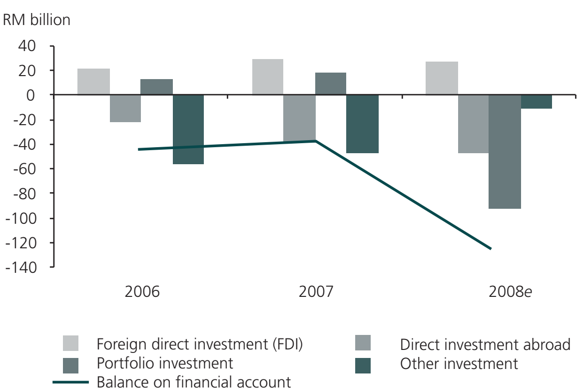
The strong external position is one of the key strengths of Malaysia's economy, particularly during this period of heightened uncertainty in global financial and economic conditions. It is recognised that the openness of the Malaysian economy renders the country more susceptible to vulnerabilities arising from external developments. Thus, it is important to ensure that appropriate policy measures are taken continuously to further enhance the resilience of the external position. In addition, close surveillance and monitoring of global economic and financial conditions as well as strong co-operation and regular engagement with the regional economies are critical for early detection of risks and vulnerabilities in the external position.

technology as well as establishing new product lines. There were also sizeable inflows of FDI into the niche and higher value-added activities, particularly in the production of solar cells, modules and panels as well as testing and measurement instruments. However, as the global economic downturn intensified in the later part of 2008, the amount of earnings retained for reinvestment declined significantly, as a greater focus was accorded on capital preservation due to liquidity constraints faced by their parent companies.

During the year, FDI in the *services sector* was channeled mainly into the finance and insurance sub-sector, followed by the communication, and real estate and business services sub-sectors. FDI inflows into the finance and insurance sub-sector was reflected in the sizeable acquistion of interests in two domestic banking institutions by foreign banks as well as the commencement of operations by a new foreign takaful company. In the communication sub-sector, the FDI inflows reflected mainly the participation of two foreign companies in a newly established mobile operator. Meanwhile, there was continued investment in the real estate and business services sub-sectors, as evidenced by the establishment of 36 new wholly foreign-owned shared services and outsourcing (SSO) companies with Multimedia Super Corridor (MSC) status during the year.

Investment in the *oil and gas sector* was supported by strong crude oil prices and firm global demand in the first half of the year. The investments, ranging from exploration and extraction operations to production and development activities, were mostly undertaken by MNCs in joint venture with PETRONAS through production sharing contracts.

**Chart 1.26**
**Financial Account**




*e* Estimate
Source: Department of Statistics, Malaysia and Bank Negara Malaysia

Net **direct investment abroad** by Malaysian companies increased to RM47.1 billion in 2008. Overseas investments were led by companies in the *services sector*, mainly in the finance and insurance, communication, and electricity, gas and water sub-sectors. These investments were effected largely through the acquisition of interests or expanding participation in existing operations abroad, particularly in the finance and insurance sub-sector following expansion in activities in the Asian region. In the communication sub-sector, the national telecommunication company has strengthened its presence in India by merging two of its strategically-owned mobile operators. The investment in the electricity, gas and water sub-sector reflected mainly the expansion of activities by a domestic utility company abroad.

Investment abroad in *oil and gas sector* remained significant as PETRONAS continued to conduct exploration, extraction and downstream processing activities in Africa, Central Asia and Vietnam. Meanwhile, investment in the *manufacturing sector* reflected mainly the acquisition of two process equipment manufacturers in Germany and Belgium to acquire new technology and gain a foothold in the European market. There were also some investments in the E&E and cement industries overseas.

The **other investment** account recorded a lower net outflow of RM11 billion, attributed to both lower net external debt repayment by the official sector and net outflows by the private sector. The lower external debt repayment by the **official sector** reflected normal scheduled repayment of term loans by both the Federal Government and NFPEs. Meanwhile, the other investment by the **private sector**, which comprises mainly of banking sector's borrowing and lending as well as placement and withdrawal of deposits, and transactions between the non-bank private sector and unrelated counterparties, recorded a significantly lower net outflow. The improvement was due largely to liquidation of short-term assets placed abroad, resulting in a reversal of the banking sector position to register a net inflow during the year. These inflows were more than offset by higher outflow by the non-bank private sector, due mainly to higher extension of trade credits by Malaysian exporters as well as larger repayment of trade credits by Malaysian importers.

### External Debt

The global credit crisis and the deterioration of the global financial landscape in 2008 demonstrate the importance of prudent and pragmatic external debt management. During the year, Malaysia continued to adopt a prudent external debt management strategy, while ensuring that the ability of the private sector to borrow from foreign sources to meet their financing requirements is not impinged. In this regard, the rules on foreign currency borrowing were further liberalised to allow resident corporations to source foreign currency borrowing within the same corporate group, onshore and offshore, without restrictions. This is in line with the overall objective of the Bank of creating a facilitative business environment that enhances the competitiveness of the economy. In addition, the external debt management strategies are also important in safeguarding monetary and financial stability. A comprehensive and robust surveillance and debt monitoring system enabled early detection of possible risks arising from the country's overall external debt exposure of both the public and private sectors.

**Table 1.20**
**Outstanding External Debt**

| | 2007[2] | 2008*p* | 2007[2] | 2008*p* |
|---|---|---|---|---|
| | RM billion | RM billion | USD billion | USD billion |
| **Total debt** | **211.2** | **235.6** | **63.1** | **67.2** |
| Medium- and long-term | 134.0 | 155.6 | 40.0 | 44.4 |
| Short-term[1] | 77.2 | 80.0 | 23.1 | 22.8 |
| *As % of total debt* | *36.6* | *34.0* | *36.6* | *34.0* |
| *As % of net international reserves* | *23.0* | *25.2* | *23.0* | *25.2* |
| **As % of GNI** | | | | |
| Total debt | 33.6 | 32.9 | | |
| Medium- and long-term debt | 21.3 | 21.8 | | |
| **As % of exports of goods and services** | | | | |
| Total debt | 29.9 | 30.7 | | |
| Medium- and long-term debt | 18.9 | 20.3 | | |
| **Debt service ratio (%)** | **3.8** | **2.7** | | |

[1] Excludes currency and deposits held by non-residents with resident banking institutions
[2] End-2007 data has been adjusted to be in line with the redefined external debt data of Malaysia, except for the debt service ratio
*p* Preliminary

Source: Ministry of Finance, Malaysia and Bank Negara Malaysia

## Malaysia's external debt remained low at RM235.6 billion or 32.9% of GNI

To facilitate a strengthened risk assessment for the economy as well as to be consistent with the international standards and best practices on the treatment of offshore entities in external data compilation, the external debt data of Malaysia has been redefined to treat entities in Labuan International Business and Financial Centre (IBFC) as residents with effect from the beginning of 2008. Under this new definition, debt exposure of these offshore entities vis-à-vis the rest of the world is included in Malaysia's external debt while debt exposure of residents with offshore entities in Labuan IBFC is excluded. The shift to the new definition in the compilation of external debt has resulted in a higher level of external debt (end-2007: RM211.2 billion; old definition: RM187.4 billion). This was attributed mainly to the debt exposure of offshore financial entities in Labuan IBFC, arising from their inter-bank borrowings.

As at end-2008, Malaysia's total external debt remained low at RM235.6 billion (or USD67.2 billion), or equivalent to 32.9% of GNI. During the year, the **medium- and long-term external debt** increased, reflecting mainly higher external debt by both the non-financial public enterprises (NFPEs) and non-bank private sector. The depreciation of the ringgit against the US dollar and Japanese yen also contributed to the increase in the external debt. The higher external debt by the **NFPEs** was due mainly to loan drawdown by companies in the finance and insurance sub-sector, particularly to finance capital expenditure, as well as the electricity, gas and water sub-sector for capacity expansion. Meanwhile, repayment of external debt, comprising mainly repayment and prepayment of term loans, was lower. During the year, the **Federal Government** sourced its funding requirements mainly from the non-inflationary domestic sources. For the fifth consecutive year, no market loan was raised from the international capital market. The drawdown of external loan was entirely from project loans committed earlier from official bilateral sources and multilateral development banks.

In 2008, the **private sector** registered another net drawdown of external debt, amounting to RM9.8 billion. The loan drawdown was effected mainly by companies in the services sector, particularly the finance and insurance and communication sub-sectors, as well as agriculture and manufacturing sectors, largely to finance capital expenditure. Meanwhile, the repayment was attributed largely to companies in the manufacturing and oil and gas sectors as well as communication sub-sector. The private sector debt accounted for about half of the total medium- and long-term debt, and about two third of these debt are inter-company loans that have flexible terms and concessionary interest rate.

During the year, the **short-term external debt** outstanding increased marginally to RM80 billion, attributed primarily to the inter-bank borrowings arising from treasury operations. The short-term external debt accounted for only 11.2% of GNI, 25.2% of international reserves and 10.4% of exports of goods and services. The bulk of the short-term debt was held by the banking sector (90.2%). Meanwhile, short-term external debt of the non-bank private sector, comprising mainly of revolving credits and overdraft facilities, remained low.

### International Reserves

The international reserves held by Bank Negara Malaysia consist of gold and foreign exchange holdings, the reserve position with the IMF and holdings of Special Drawing Rights (SDR). In 2008, the net international reserves moderated by RM18.2 billion to RM317.4 billion (equivalent to USD91.5 billion) as at 31 December 2008.

During the year, the movement in the international reserves was characterised by two distinct periods. In the first six months of the year, the reserves increased by RM75.2 billion to RM410.9 billion (equivalent to USD125.8 billion) as at end-June, due mainly to higher repatriation of export earnings supported by strong commodity exports, and significantly larger inflows of portfolio capital as well as foreign direct investment. However, the reversal of the portfolio capital flows due to the deleveraging activities by international foreign financial institutions following the deepening of the global financial crisis led to a decline in reserves in the second half of the year to RM317.4 billion (equivalent to USD91.5 billion) as at end-December 2008. The high level of reserves has acted as a sound buffer during such periods of large reversals in short-term flows, without undermining the functioning of domestic financial markets and the financing of real sector of the economy. The increased payments for imports of goods and services, larger repatriation of profits and dividends accruing to foreign companies operating in Malaysia as well as higher overseas investment by Malaysian companies also contributed to the outflows. Meanwhile, the cumulative foreign exchange revaluation loss amounting to RM5.8 billion reflected the strengthening of the ringgit against a number of the major currencies, particularly in the first and fourth quarters of 2008.

**Table 1.21**
**Net International Reserves**

| | As at end | | | Change |
|---|---|---|---|---|
| | 2006 | 2007 | 2008 | 2008 |
| | RM million | | | |
| SDR holdings | 756.9 | 760.9 | 786.4 | 25.5 |
| IMF reserve position | 793.4 | 617.5 | 1,127.1 | 509.6 |
| Gold and foreign exchange[1] | 288,871.2 | 334,338.6 | 315,554.3 | -18,784.3 |
| **Gross International Reserves** | **290,421.5** | **335,717.0** | **317,467.7** | **-18,249.3** |
| *Less* Bank Negara Malaysia external liabilities | 22.9 | 22.2 | 22.5 | 0.3 |
| **Net International Reserves** | **290,398.6** | **335,694.8** | **317,445.3** | **-18,249.5** |
| **USD million equivalent** | **82,450.8** | **101,338.1** | **91,529.5** | **-9,808.6** |
| Months of retained imports | 7.8 | 8.4 | 7.6 | |
| Reserves/Short-term external debt[2] (times) | 6.9 | 6.2 | 4.0 | |

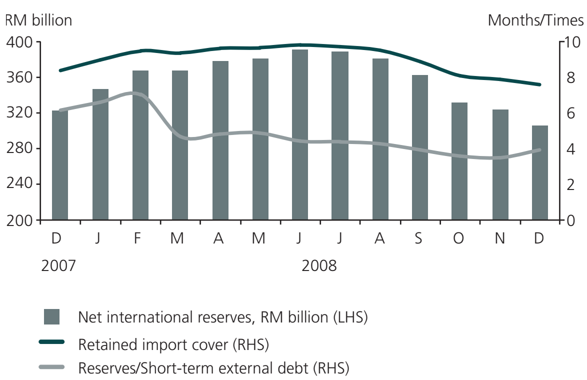
[1] 'Other Foreign Currency Claims on Residents' is reclassified from 'Gold and Foreign Exchange' to 'Other Assets' of Bank Negara Malaysia
[2] With effect from end-March 2008, the short-term external debt refers to the external debt under the new definition, with offshore entities in Labuan IBFC being treated as residents
Note : Numbers may not necessarily add up due to rounding

Source: Bank Negara Malaysia

The tumultuous period for international financial markets in the second half of 2008 heightened the challenge in the management of the reserves. As the global financial turmoil gathered momentum, volatility rose sharply while liquidity evaporated in many of the non-sovereign bond markets. Many large global financial institutions were also under severe stress from sharply rising costs of borrowings in the interbank market, credit ratings downgrades and a general loss of confidence in counter-party risks and in the financial markets of a broad range of instruments. Furthermore, the turmoil also led to significant outflows from the regional markets, including Malaysia. In dealing with these events, the Bank's reserve management strategy was adapted accordingly. During the second half of 2008, increasing emphasis was placed on sovereign or sovereign risk related investments and maintaining sufficient liquidity to meet the outflows as well as ensuring orderly market conditions. Reserve diversification was also reviewed as the correlations between markets increased sharply during the crisis. Oversight and risk management practices were also enhanced, particularly during the heightened volatility period of October.

Malaysia remains a participating member in the Financial Transactions Plan of the IMF which makes resources available to member countries facing short-term balance of payments difficulties. The increase in **reserve position with the IMF** in 2008 reflected mainly net purchases of currencies by various member countries under the Financial Transactions Plan. Meanwhile, the increase in international reserves held in the form of **SDRs** was attributed mainly to the exchange revaluation gains on holding of SDR and receipt of remuneration arising from Malaysia's net creditor position with the IMF.

**Chart 1.27**
**Net International Reserves (end-month)**




Note: With effect from end-March 2008, the short-term external debt refers to the external debt under the new definition, with offshore entities in Labuan IBFC being treated as residents
Source: Bank Negara Malaysia

## The international reserves remained high at RM315.9 billion as at 27 February 2009, adequate to finance 7.6 months of retained imports and cover 3.9 times of the short-term external debt

As at 27 February 2009, the reserves remained at a comfortably high level of RM315.9 billion (equivalent to USD91.1 billion), adequate to finance 7.6 months of retained imports and is 3.9 times the short-term external debt. The international reserves held by the Bank are usable and unencumbered. There are no foreign currency loans with embedded options; and no undrawn, unconditional credit lines provided by or to other central banks, international organisations, banks and other financial institutions. Bank Negara Malaysia also does not engage in options-related activity in the foreign currency markets with regard to the ringgit.

### LABOUR MARKET DEVELOPMENTS

The strong labour market conditions in 2007 continued into the first half of 2008 as reflected in the higher vacancies, lower retrenchments and continued gains in employment. Nevertheless, labour market conditions began to soften in the second half of the year as businesses turned cautious amidst rising cost pressures and declining external demand as a result of the deepening global financial and economic crisis.

## Labour market conditions weakened towards the end of the year

Accordingly, for the year as a whole, the unemployment rate increased to 3.7% in 2008 (2007: 3.2%), as total employment expanded at a slower pace of 1.1% compared to the labour

**Table 1.22**
**Selected Labour Market Indicators**

| | 2004 | 2005 | 2006 | 2007 | 2008*e* |
|---|---|---|---|---|---|
| Employment[1] ('000 persons) | 10,463.7 | 10,892.8 | 11,159.0 | 11,398.0 | 11,524.7 |
| Annual change (%) | 4.1 | 4.1 | 2.4 | 2.1 | 1.1 |
| Labour force[1] ('000 persons) | 10,846.0 | 11,290.5 | 11,544.5 | 11,775.1 | 11,967.5 |
| Annual change (%) | 4.0 | 4.1 | 2.2 | 2.0 | 1.6 |
| Retrenchments | 19,956 | 16,109 | 15,360 | 14,035 | 16,469* |
| Annual change (%) | -5.9 | -19.3 | -4.6 | -8.6 | 17.3 |
| Unemployment rate[1] (% of labour force) | 3.5 | 3.5 | 3.3 | 3.2 | 3.7 |
| Real labour productivity growth[2] (%) | 2.5 | 1.2 | 3.3 | 4.1 | 3.5 |

[1] Based on estimates by Economic Planning Unit
[2] Based on estimates by Bank Negara Malaysia
* Excludes 7,564 retrenched workers from a company that was taken over, and rehired immediately by the new owner
*e* Estimate

Source: Bank Negara Malaysia
Economic Planning Unit
Ministry of Human Resources

force (1.6%). Meanwhile, labour cost increased at a slightly slower pace of 5.9% (2007: 6%), as employers' ability to increase wages was affected by the rising cost and softening economic activity towards the end of the year.

The slower economic activity, particularly in the manufacturing sector, was reflected in the rising number of **retrenchments**. In the first half of 2008, when domestic and external demand was strong, total retrenchments was only 5,218 persons (1H 2007: 8,382 persons). Nevertheless, the sharp deceleration in global demand towards the end-year affected businesses, especially in the export-oriented industries, and prompted companies to adopt various cost-cutting measures, including retrenchment. A total of 11,251[1] persons were retrenched in the second half-year, resulting in the total retrenchments in 2008 rising to 16,469 workers. Most of the retrenchments were in the manufacturing sector (67% share), in particular those involving the electronic and electrical (E&E) industries (29% share of total retrenchments), while the distributive trade, hotels and restaurants sub-sector accounted for another 12%.

Similarly, the demand for workers was also strong in the first half-year. Total **vacancies** increased by 35% during the January-June period, with higher number of vacancies across most sectors. Vacancies in the second half-year continued to increase, but at a slower pace (23%). To some extent, vacancies in the fourth quarter were supported by the active promotion of the employment portal of the Ministry of Human Resources. For the year as a whole, total vacancies increased by 28% to about 1.06 million positions (2007: 0.8 million positions), with the services and manufacturing sectors accounting for 33% and 31% share of total vacancies respectively.

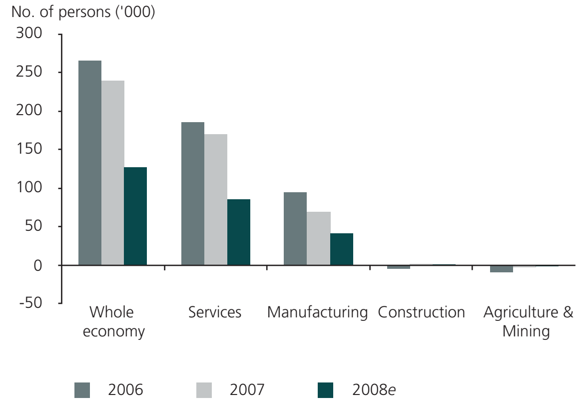
Despite the higher vacancies, many jobseekers found it difficult to secure jobs, as reflected by the decline in MIER Employment Index and Jobstreet Employee Confidence Index to 55.8 points and 47.3 points respectively (2007: 113.1 and 49.6 points, respectively). Apart from cost-cutting measures such as retrenchments, companies were increasingly more selective in their hiring activities. As a result, total **employment** grew at a slower rate in 2008 (1.1%; 2007: 2.1%), reflecting mainly the slower employment growth in the manufacturing and services sectors. The manufacturing sector, which is the second largest employer, had begun to reduce the number of workers since mid-year as a result of the deterioration in global demand which had affected both the E&E and domestic-oriented industries. Employment in the

[1] Excludes 7,564 retrenched workers from a company that was taken over in the second half-year, and rehired immediately by the new owner

**Chart 1.28**
**Output and Employment**


e Estimate
Source: Economic Planning Unit
Department of Statistics, Malaysia

**Chart 1.30**
**Additions to Employment by Sector**

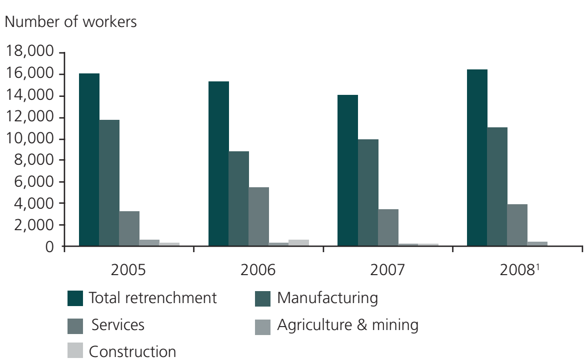



e Estimate
Source: Economic Planning Unit

services sector also grew at a slower pace, as some companies became more selective while others postponed their recruitment plans and trimmed headcounts as business conditions became progressively weaker during the course of the year. Meanwhile, employment in the construction sector was supported by higher activity in the sector. Employment growth in the agriculture sector continued on its long-term downward trend reflecting primarily workers' preference to be engaged in other sectors, while hiring in the mining sector was affected by the slower activity in the sector.

In 2008, total registered **foreign workers** (including foreign expatriates) in Malaysia increased by 0.9% to 2.10 million workers. Foreign workers accounted for 18% of total employment in Malaysia. The increase in migrant workers was at a slower pace of 0.9% to 2.06 million workers (2007: 9.4%) as companies reduced intake of new workers given the weakening economic conditions towards the end of the year. Foreign expatriates employed in the country increased marginally by 0.7% to 36,794.

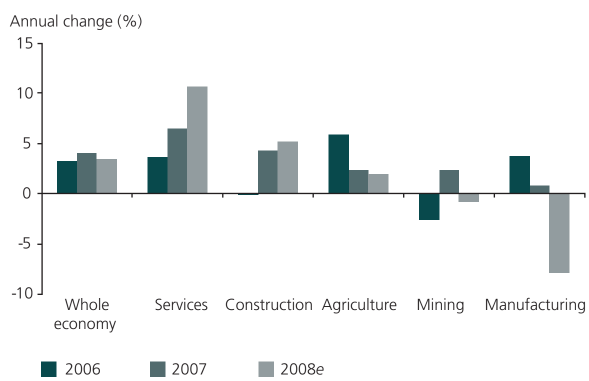
**Chart 1.29**
**Retrenchment by Sectors**




[1] Excludes 7,564 retrenched workers from a company that was taken over, and rehired immediately by the new owner

Source: Ministry of Human Resources

**Chart 1.31**
**Labour Productivity Trends**




e Estimate
Source: Bank Negara Malaysia
Department of Statistics, Malaysia

**Labour productivity**, as measured by real value added per worker, grew at a slower pace of 3.5% (2007: 4.1%), due mainly to the deterioration in manufacturing productivity growth (-7.8%). Nevertheless, this was offset to some extent by improvements in the services productivity growth (10.7%). Gains in productivity were supported by the continued growth in capital investment, increased training and the participation of more educated workforce in the labour market. The increase in labour productivity continued to support increases in salary and wage growth. An issue of concern in the earlier part of the year was that rising inflationary pressure would lead to higher wage increases. Bank Negara Malaysia paid close attention to assess if second-round effects emerged, which would result in inflation being persistent. Nevertheless, evidence indicated no signs of excessive wage increases in response to the higher prices. In addition, competitive pressures also reduced the possibility of a wage-price spiral. The second-round effects became less of a concern as inflationary pressures diminished in the latter part of the year amidst weaker global economic conditions and a significant decline in commodity prices. According to the survey conducted by the Malaysian Employers Federations (MEF), average **salary** in the private sector increased by 5.9% in 2008 (2007: 6%), with executives receiving an average increment of 6.1%, while non-executives, a 5.7% increase (2007: 6.3% and 5.8% respectively).

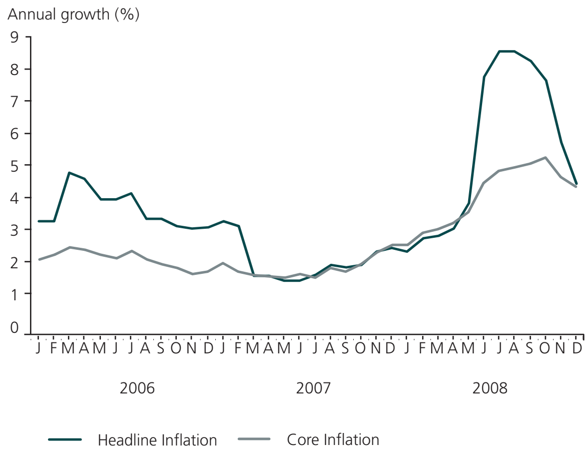
## PRICE DEVELOPMENTS

### Consumer Prices

Headline inflation, as measured by the annual percentage change in the Consumer Price Index (CPI), averaged 5.4% in 2008 (2007: 2.0%). This is significantly higher than the country's long-term inflation average of 3.0%. Core inflation, which is a measure of demand-driven pressure on prices, also rose and averaged 4.0% in 2008 (2007: 1.8%).

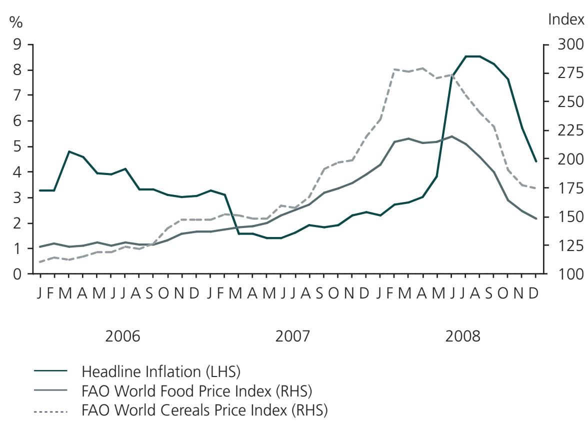
In the first five months of the year, headline inflation had continued its modest uptrend from 2007 as global food and fuel prices rose steadily due to supply-related factors. Most of the rise in inflation during the year, however, occurred in the third quarter when the inflation rate rose sharply following the 40.4% adjustment to retail fuel prices in June – which was the largest adjustment since 1990, as global fuel prices

**Chart 1.32**
**Consumer Price Inflation**



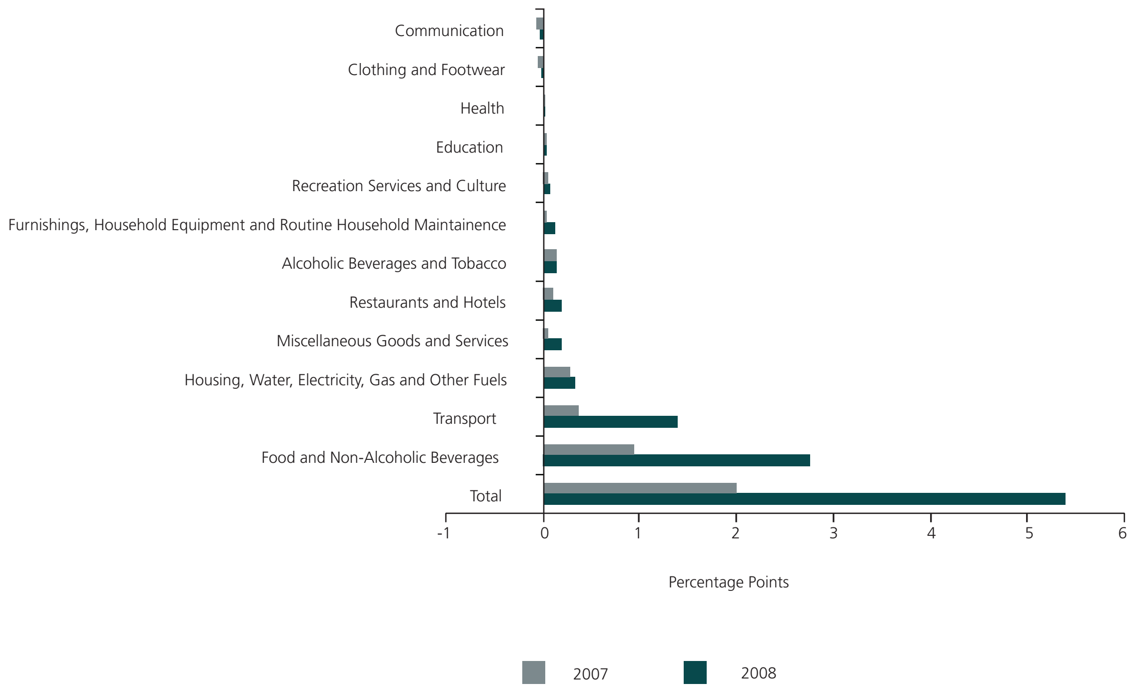

reached historical levels. The benchmark price of West Texas Intermediate (WTI) crude oil trading on the NYMEX rose to a new record level of USD147.27 per barrel on July 11, 2008. As a result, inflation peaked at 8.5% in July. However, the global financial turmoil and higher inflation had a negative impact on the real economy by dampening consumption and investment activities. The contraction in global demand combined with the unwinding of positions taken

**Chart 1.33**
**Headline Inflation and World Food Prices**




Note: 1. FAO stands for Food and Agricultural Organisation of the United Nations
2. The FAO Food Price Index consists of a weighted average of 55 food commodities considered by FAO specialists as representing the international prices of food.
3. The FAO Cereals Price Index consists of a weighted average of the International Grains Council (ICG) wheat price index and the average price of 16 different rice price quotations.

**Chart 1.34**
**Contribution to Inflation**




in the commodity markets led to a rapid decline of commodity prices and allowed domestic fuel and food prices to decline, with domestic inflation moderating to 4.4% by December.

By category, the main contributors to inflation in 2008 were the *food and non-alcoholic beverages* and *transport* categories which together comprised 79.7% of the overall rise in domestic prices during the year. Inflation in the *food and non-alcoholic beverages* category averaged 8.8% in 2008 (2007: 3.0%), and contributed 52.2% to overall inflation in 2008. The increase in food prices was universal, with all food sub-components recording a faster rate of price increase compared to the year before. As in the previous year, the increase in domestic food inflation was mainly due to higher global food prices, especially grain prices. On average, the domestic price of rice rose by 25.3% in 2008 as poor harvests caused supply shortages in major rice-exporting countries, and prompted major stockpiling activities to ensure food security. Overall, the extent of the pass-through from global prices to domestic food prices was moderated by the existence of Government price controls. For food items not subject to price controls, the increase in prices reflected the direct pass-through from higher production costs and global prices to consumers. The uptrend in domestic food prices began in August 2007 and rose to a peak of 12.3% in September 2008. Since then, food-price inflation has been on a moderating trend.

Inflation in the *transport* category averaged 8.8% in 2008 (2007: 2.3%), and contributed 25.9% to domestic inflation. Despite the surge in global fuel prices, inflation in the *transport* category remained relatively modest in the first half of the year as domestic retail fuel prices remained unchanged due to Government subsidies. However, the adjustment to domestic retail fuel prices in June by an average of 40.4% led to inflation in the *transport* category accelerating sharply to 19.6% (May 08: 0.9%). The impact on headline inflation was immediate, with headline inflation rising to 7.7% in June (May 08: 3.8%). Nevertheless, in line with the fall in global fuel prices, the Government revised retail fuel prices down seven times between August and December to end the year at fuel prices that were lower than their pre-June adjustment levels.

Other notable factors affecting headline inflation during the year were the rise in electricity tariffs by 19.4% in July 2008 and the imposition of a

**Chart 1.35**
**Headline Inflation and Retail Petrol Price**


Note: Retail petrol price refers to the price of RON 97

20% rise in excise duties on cigarettes in August. Consequently, prices in the *housing, water, electricity, gas and other fuels* category increased at a faster rate of 1.6% in 2008 (2007: 1.3%). Despite the increase in excise taxes on cigarettes, the *alcoholic beverages and tobacco* category still registered a lower inflation rate of 7.3% in 2008 (2007: 7.8%), due to the fact that the increase in excise duties in 2008 were lower than the increase in 2007. As with the previous years, the increase in overall prices was partly mitigated by the decline in prices in the *communication* and *clothing and footwear* categories. Prices in the communication category have been on a declining trend since 2005, while prices in the *clothing and footwear* category have been falling since 1999.

In view of the burden faced by the general public as a result of the sharp increase in food and energy prices in 2008, the Government introduced a number of measures focusing on ensuring an adequate supply of essential goods at affordable prices and on limiting the burden of higher costs on businesses, as well as on consumers, in particular, those in the lower-income groups. To mitigate the impact of high food prices, price controls were expanded to include other types of domestically-produced rice (previously only the Super Tempatan 15% rice was controlled), freeing the movement of paddy between states and initiating a price reduction campaign amongst major hypermarkets and retailers. To mitigate the effect of high fuel prices, the Government provided a targeted cash rebate for owners of vehicles below a certain engine capacity and raised the eligibility criteria for welfare assistance, from a monthly household income of RM400 to RM720 for Peninsula Malaysia, RM830 for Sarawak and RM960 for Sabah.

In addition, the Government also introduced a number of measures aimed at ensuring long-term food security. This included the stockpiling of essential food items such as palm-based cooking oil, allocating more land for agricultural purposes and allocating funds under Budget 2009 for improving the food distribution system. An investment of RM35 billion over 5 years was allocated under Budget 2009 for improving the existing public transportation system in the country.

**Producer Prices**

The effect of global commodity prices was most evident in the Producer Price Index (PPI). Producer price inflation, as measured by the PPI rose to 8.2% in 2008 (2007: 6.6%). In the first half of the year, PPI inflation escalated and peaked at 14.4% in June. Since then, PPI inflation has been on a rapid decline, mirroring the turnaround in global commodity prices. This development was especially evident in the commodities component of the PPI. For the first eight months of 2008, the commodities component of the PPI recorded high double-digit inflation rates, peaking at 42.5% in June before declining rapidly to -10.4% by the end of the year. For the year as a whole, inflation in the commodities component of the PPI averaged 25.8% (2007: 12.5%). Excluding commodities, PPI inflation declined to 1.9% in 2008 (2007: 4.6%).

In terms of composition, inflation in the local component of the PPI increased to 10.3% in 2008 (2007: 7.6%). This was primarily due to price increases in the *mineral, fuels, lubricants and related materials, chemicals and related products not elsewhere specified* and *manufactured goods classified chiefly by materials* categories. These price increases were attributable mainly to the high prices of petroleum, which then led to higher input costs for petroleum-derived products such as plastics, polymers, fertilizers and soap. Meanwhile, inflation in the imported component of the PPI moderated to 4.2% (2007: 4.8%). This was due to the smaller share of commodities in the imported component of the PPI – commodities made up only 7.2% in the imported component of the PPI compared with 26.8% in the local component of the PPI.

## Development of Small and Medium Enterprises

A dynamic small and medium enterprise (SME) sector will contribute to development objectives, including towards more efficient allocation of resources, employment, the development of indigenous entrepreneurship, equitable growth and poverty eradication. The economic potential of the SME sector thus makes SME development an important Government agenda. During the year, further measures were taken to develop a strong and dynamic SME sector by strengthening the enabling infrastructure for SME development, building capacity and capabilities, and improving access to financing by SMEs.

**Profile of SMEs**

The Baseline Census of Establishments and Enterprises conducted in 2005 (Census 2005) provided important data on the profile and performance of SMEs to facilitate the formulation of effective policies and strategies to support SME development. Based on a large sample response of 552,804 business enterprises, SMEs formed 99.2% or 548,267 of the business establishments in Malaysia, of which almost 80% or about 435,300 were micro enterprises. The findings also revealed that 87% of SMEs were in the services sector, followed by 7.2% in the manufacturing sector and 6.2% in the agriculture sector.

**Key Initiatives and Achievements for SME Development in 2008**

Several key initiatives were implemented in 2008, reflecting the strong commitment towards SME development:

**(i) SME Central Coordinating Agency - Assuming the Secretariat Function of National SME Development Council**

In August 2004, the National SME Development Council[1] (Council) was set up as the highest policy-making body for SME development. The Council is chaired by the Prime Minister and BNM was the Secretariat. Its functions included coordinating and formulating SME policies across all sectors, as well as monitoring and evaluating the implementation and effectiveness of SME programmes by the Ministries and Agencies. The Secretariat also acts as a single point of reference for the Government and SMEs on information relating to the development of SMEs.

During its time as Secretariat to the Council, the following initiatives were implemented to support SME development:

**(a) Improved policy formulation, monitoring and assessment**

- Preparation of the SME Development Blueprint, an annual action plan and assessment of public sector programmes for the development of SMEs; and
- Establishment of macro targets for SME development 2006 – 2010.

**(b) Strengthened capacity and capability building for SMEs**

- Appointment of Pembangunan Sumber Manusia Berhad (PSMB) and establishment of the SME Marketing Committee to coordinate training and marketing efforts for SMEs; and
- Strengthened financial advisory services through the establishment of BNM's Laman Informasi Nasihat Khidmat, SME Bank Advisory Centre and financial advisory services provided by the commercial banks.

**(c) Enhanced access to financing for SMEs**

Strengthened financial service providers through:

- Establishment of SME Bank;
- Transformation of Credit Guarantee Corporation to expand credit guarantee facilities to assist SMEs in obtaining financing;

[1] Consists of 15 Ministers, the Chief Secretary to the Government and three Heads of Agencies

- Transformation of Bank Pertanian Malaysia to enhance its capacity to lend to agriculture and agro-based industries;

Developed new financial products for SMEs:
- Rolled out microfinance for micro enterprises;
- Introduced new trade finance products;
- Launched RM300 million venture capital funds for agriculture businesses; and
- Introduced RM1 billion Overseas Project Financing facilities.

**(d) Improved statistical information**
- Developed standard SME definitions;
- Initiated the Census of Establishments and Enterprises 2005; and
- Established the National SME Database.

**(e) Disseminated comprehensive information**
- Published the SME Annual Reports on the status and performance of SMEs as well as key programmes on SME development;
- Establishment of SMEinfo portal to provide a one-stop information centre for SMEs; and
- Establishment of Human Resource Development (HRD) training portal to provide training information for SMEs.

In July 2008, the secretariat function held by Bank Negara Malaysia was successfully transferred to the Small and Medium Industries Development Corporation (SMIDEC), which will be transformed to become the new SME Corporation Malaysia, a dedicated Government agency to spearhead SME development in Malaysia. This dedicated Agency will coordinate SME policy formulation and programme implementation across all sectors and Government Agencies. The Agency will also serve as the central point of information, reference and advisory services for SMEs across all sectors and acts as the Secretariat to the National SME Development Council. SME Corporation Malaysia is targeted to be fully operationalised in 2009. This marks a turning point for the development of a more dynamic, competitive and resilient SME sector.

**(ii) National SME Development Blueprint 2008**

The National SME Development Blueprint 2008 which was endorsed by the Council on 2 June 2008, provided an assessment of the SME programmes implemented in 2007 and identified programmes that will be implemented in 2008.

In 2007, more than 286,000 SMEs were assisted through the implementation of 189 key programmes, involving a total expenditure of RM4.9 billion. SMEs assisted in 2007 include a total of 135,000 women entrepreneurs and students who benefited from entrepreneurship and technical training programmes, while more than 4,750 SMEs were provided with business premises and factories.

In 2008, 198 key programmes were targeted to be implemented with a financial commitment of RM3.2 billion to assist SMEs across all sectors, in the areas of infrastructure support, capacity building and in improving access to financing. The main focus of programmes in 2008 was towards promoting SMEs in the services and agriculture and agro-based sectors, in line with the strategies formulated in the Ninth Malaysia Plan (9MP) and Industrial Master Plan 3 (IMP3).

As part of the initiatives to address gaps in SME development programmes, focus group discussions were conducted with the trade associations and business chambers representing SMEs. Arising from the sessions conducted, feedback from SMEs were evaluated and SMEs' views and suggestions were highlighted to the relevant Ministries/Agencies to facilitate future planning and implementation.

The adoption of the SME Blueprint Management Framework by the Council in 2005 has shown benefits after only three years of implementation. The structured approach of the Blueprint has resulted in the strong commitment of Ministries and Agencies to implement focused SME development programmes as well as in meeting the targets set. Inter-Ministry/Agency collaboration and coordination remain the priority of the Blueprint to ensure effectiveness of programmes and greater outreach to SMEs.

**(iii) SME Annual Report 2007**

On 24 July 2008, the Council released the SME Annual Report 2007. The Report is an important initiative to disseminate information on the strategies and programmes that have been implemented by the Government to support the growth of the SME sector. The report also showcased success stories of several SMEs who have benefited from Government programmes.

### Enhancing Access to Financing for SMEs

**Comprehensive and Diversified Financing Landscape for SMEs**

**SMEs have 651,563 accounts[1] with financing value of RM138.9b as at end-2008**

**Banking Institutions**
- **54** banks with **4,149** branches
- **RM124.8 billion** financing outstanding to **550, 716** SME accounts at end-2008
- 2008: **RM54.4 billion** financing approved to **117,524** SME accounts

**Development Financial Institutions (DFIs)**
- **6** DFIs with **682** branches
- **RM14.1 billion** financing outstanding to **100,847** SME accounts at end-2008
- 2008: **RM4.8 billion** financing approved to **31,220** SME accounts

**Financing by Banking Institutions and Development Financial Institutions include:**

**5 Bank Negara Malaysia Special Funds**
- Approved **RM18.1 billion** financing to **37,438** SME accounts
- **RM7.6 billion** outstanding at end-2008
- 2008: **RM2.1 billion** approved to **3,758** SME accounts

**2 Financing Schemes with Guarantee Facilities**
- August-December 2008: **RM1.1 billion** approved to **4,923** SME accounts

**114 Goverment Funds and Schemes[2]**
- Approved **RM100.3 billion** to **1.5 million** SME accounts at end-2008
- **RM9.7 billion** financing outstanding at end-2008
- 2008: **RM14.7 billion** approved to **267,929** SME accounts

**Small Debt Resolution Scheme**
- Since establishment, restructured NPLs of **627** SMEs amounting to **RM373 million**
- 2008: Restructured NPLs of **62** SMEs amounting to **RM49 million**

**Credit Guarantee Corporation Malaysia Berhad**
- Guaranteed **RM42.1 billion** financing to **384,033** SME accounts since 1972
- Outstanding guaranteed financing of **RM15.6 billion** to **94,354** SME accounts at end-2008
- 2008: Guaranteed **RM3.0 billion** financing to **10,368** SME accounts

**Venture Capital (VC)[3]**
- **56** VC companies
- Outstanding **RM1.9 billion** investment in **450** companies at end-2008
- 2008: **RM477 million** invested

**Leasing and Factoring**
- **RM1.8 billion** financing outstanding at end-2008
- 2008: **RM556 million** approved

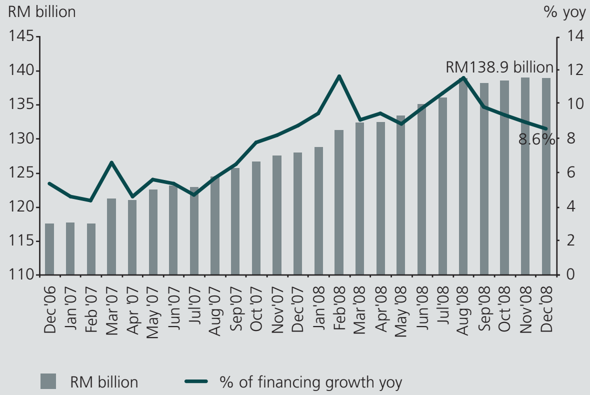
Note 1: Consist of accounts maintained with banking institutions and development financial institutions

Note 2: Only part of the Goverment's funds and schemes are disbursed through development financial institutions. Source from SMIDEC

Note 3: Source from Securities Commission

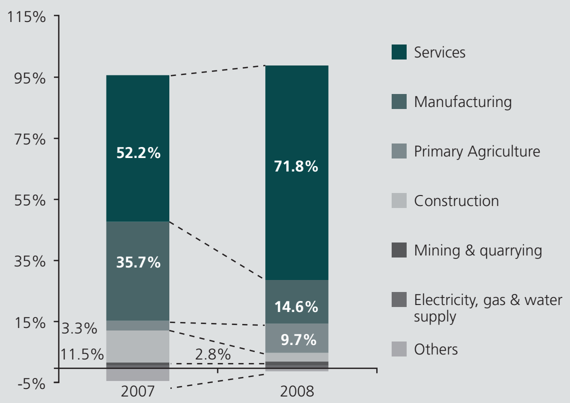
There are various sources of financing available for SMEs. These include financing from banking institutions, development financial institutions, leasing and factoring companies, as well as venture capital companies. In addition, many SME financing schemes have been set up by the Government. Banking institutions remain the largest source of financing for SMEs, accounting for 90% of the SME financing outstanding of the financial institutions[2] at end-2008.

**SME Financing Outstanding of Financial Institutions**

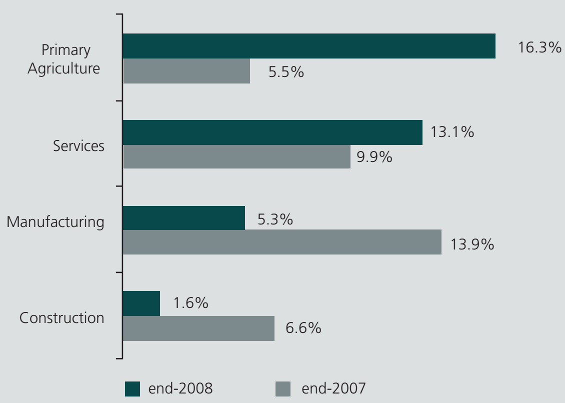



Financial institutions continued to support the financing needs of SMEs in 2008. Despite the challenging economic environment, SME financing outstanding of the financial institutions expanded by 8.6% to RM138.9 billion at end-2008 (end-2007: 8.8%; RM128 billion). Financing to SMEs accounted for 42.3% of total business financing of the financial institutions at end-2008 (end-2007: 44%).

**Sector Contribution to the Increase in SME Financing Outstanding**




**Financing Outstanding by Major Sectors (%yoy change)**




On a sectoral basis, the services sector continues to drive financing growth in 2008, contributing 72% to the total increase in the SME financing outstanding in 2008. The strength in the services and agriculture sectors offset the lower contribution from the manufacturing and construction sectors. Financing to the primary agriculture sector grew strongly in 2008, expanding by 16.3% (2007: 5.5%). Financing to the

[2] Refers to banking institutions and development financial institutions (DFIs).

manufacturing and construction sectors moderated, reflecting the reduced demand for financing from these sectors.

**Progress of Major Initiatives to Improve Access to Financing for SMEs**
Efforts to enhance access to financing for SMEs continued to focus on four broad areas: (i) strengthening the financial infrastructure for SMEs; (ii) enhancing and developing financing incentives and schemes for SMEs; (iii) strengthening financial service providers; and (iv) strengthening the provision of advisory services for SMEs. The objective is to ensure that SMEs at various stages of growth are able to have adequate access to financing.

**(i) Strengthening the Financial Infrastructure**

**(a) Development of a Vibrant and Sustainable Microfinance Industry**
The findings of the Census 2005 indicated that about 80% of SMEs in Malaysia are micro enterprises, and that most relied on internal sources for financing. Recognising this, the Council in 2006 approved a comprehensive microfinance institutional framework, comprising banking institutions, development financial institutions and credit cooperatives, to develop a sustainable microfinance industry.

To create greater public awareness on the availability and benefits of microfinance, the national Pembiayaan Mikro (microfinance) logo was launched in September 2007. Participating financial institutions have displayed the logo and a microfinance client charter to signify commitment in providing easy, fast and convenient microfinance services. At end-2008, more than 1,500 microfinance access points are displaying the logo. Microfinance clients who obtained microfinance were also encouraged to display the logo at their business premises. Bank Negara Malaysia had also embarked on a microfinance television commercial initiative in November 2008. In addition, microfinance information flyers were distributed at various strategic locations.

As a result of the efforts to promote the growth of the microfinance industry, nine financial institutions are now offering microfinance products under the Pembiayaan Mikro (microfinance) scheme. These provide micro enterprises with access to micro financing for business activities. At end-2008, the amount of outstanding micro financing by the nine Pembiayaan Mikro financial institutions amounted to RM478 million (annual growth rate of 113%), benefiting 45,179 microfinance customers (annual growth rate of 98%).

**(b) The SME Credit Bureau**
The Census 2005 highlighted that among the main problems faced by SMEs to obtain financing was the lack of financial track records. To address these issues, an SME Credit Bureau was established through a strategic partnership between CGC and Dun and Bradstreet, a premier global provider of credit information on SMEs.

The Bureau, which commenced operations in July 2008, serves as a credit databank by providing financial institutions and trade creditors data on SMEs. This comprise data acquired from Suruhanjaya Syarikat Malaysia (SSM), the Central Credit Reference Information System (CCRIS), Dishonoured Cheque Information System (DCHEQS) and SME trade data. Through its operations, the Bureau will assist SMEs to build good credit track records and hence, credibility. This increases SMEs' prospects of obtaining financing from financial institutions. The Bureau also provides credit ratings for SMEs which will inculcate prudent and sound financial management practices amongst SMEs. The ratings will identify and highlight areas of weaknesses for SMEs to improve their operations. Financial institutions will also be able to have timely and efficient access to credit information on SMEs, leading to faster and accurate decisions on loan applications.

Within five months of operations, the Bureau has managed to secure membership from 37 financial institutions and nearly 18,000 SMEs with more than 3,400 reports generated during the period. The Bureau is currently operated by SME Credit Bureau (M) Sdn. Bhd and SMEs can register as members of the Bureau at www.smecreditbureau.com.my.

**(c) The Small Debt Resolution Scheme (SDRS)**
Bank Negara Malaysia had established the Small Debt Resolution Scheme in 2003 to facilitate the restructuring and rescheduling of non-performing loans (NPLs) and non-performing financing (NPFs) of SMEs with on-going businesses. As at end 2008, 808 applications with total NPLs/NPFs of RM563 million had been facilitated. Of these, 627 applications involving NPLs/NPFs of RM373 million were approved for either restructuring or rescheduling, while RM18 million in new financing were approved to 37 SMEs. Restructuring and rescheduling of NPLs/NPFs will continue to be an important aspect in supporting the viability and sustainability of financially distressed SMEs. To provide a wider coverage for debt resolution, Bank Negara Malaysia in January 2008 had expanded the range of participating financial institutions to include Bank Kerjasama Rakyat Malaysia Berhad, Bank Pertanian Malaysia Berhad and Export-Import Bank of Malaysia Berhad.

**(ii) Enhancing and developing financing incentives and schemes for SMEs**
Given that 99.2% of business establishments in Malaysia are SMEs, adequate access to financing is critical to enable SMEs to contribute to the economic development of the nation. Bank Negara Malaysia has developed several initiatives in the past year to address financing gaps and ensure that viable SMEs continue to have adequate access to financing. Among the initiatives taken are:

**(a) The SME Assistance Facility and the SME Modernisation Facility**
In August 2008, Bank Negara Malaysia introduced two financing facilities amounting to RM1.2 billion: the SME Assistance Facility and the SME Modernisation Facility. The SME Assistance Facility was established to assist viable SMEs that were facing temporary cashflow problems due to rising costs in the third quarter of 2008. Eligible SMEs would be able to enjoy interest rates as low as 4% per annum, thus providing SMEs with more flexibility in managing their finances during the challenging period. Likewise, the SME Modernisation Facility was established to incentivise SMEs to modernise their operations, in particular to purchase or upgrade machinery and equipment, including energy saving equipment, which would reduce operational costs in the long run. The performance and demand for the facilities have been encouraging. As at end 2008, 4,923 applications amounting to RM1.1 billion have been approved by the participating financial institutions.

**(b) Micro Enterprise Fund (MEF)**
In November 2008, Bank Negara Malaysia established a RM200 million Micro Enterprise Fund (MEF) to ensure viable micro enterprises have continuous access to financing during the current challenging business environment. The fund is accessible through the nine financial institutions participating in the Pembiayaan Mikro scheme. Participating financial institutions will determine the lending or financing rate to be charged and applications are subject to the normal credit approval process of the participating financial institutions. This fund is available for micro enterprises with viable businesses from 5 November 2008 to 31 December 2009. At end-2008, RM4.2 million were approved to 241 micro enterprises under the MEF. It is expected that many more micro enterprises will benefit from creation of this fund.

**(c) SME Assistance Guarantee Scheme (SME AGS)**

Bank Negara Malaysia established a RM2 billion SME Assistance Guarantee Scheme in January 2009, to ensure that viable SMEs adversely impacted by the current economic slowdown, continue to have adequate access to financing. With the guarantee cover, access to financing can be given at a lower cost to viable SMEs.

Eligible SMEs can obtain financing of up to RM500,000, and with tenures of up to five years. CGC will provide an 80% guarantee cover for financing approved under this Scheme. The guarantee cover will be provided free of charge and the cost of the guarantee will be fully borne by Bank Negara Malaysia. This Scheme is accessible at all commercial and Islamic banks, SME Bank, Agrobank, Bank Rakyat, EXIM Bank and Bank Simpanan Nasional. Participating financial institutions will determine the lending or financing rates and applications are subject to the normal credit approval process of the participating financial institutions. This Scheme is available from 3rd February 2009 till 31st December 2009, or when the financing limit of RM2 billion has been fully utilised.

**(d) Rationalisation of Government SME Funds**

To enhance the effectiveness of the 111 Government funds for SME, the National SME Development Council has agreed that the Economic Planning Unit (EPU) to conduct a study to analyse the effectiveness of the funds. Among the specific objectives of the study are to provide recommendations to rationalise the funds where appropriate; and to propose a new methodology and mechanism to channel Government funds for SMEs. The guiding principles of this process is to enhance the efficiency of the mechanism to channel financing to SMEs, while ensuring that SMEs eligible to obtain funding under the current mechanisms are not worse-off. In addition, lending to the SMEs by the Government should not be at the expense of good credit practice.

A special committee headed by the Director General of EPU and comprising representatives from the relevant Ministries and Agencies was established to oversee the study and present the recommendations to the Government.

**(iii) Strengthening Financial Service Providers**

**(a) Transformation of Credit Guarantee Corporation (CGC)**

To better serve the growth and development of competitive SMEs, CGC embarked on a transformation exercise in 2005. A three year plan was put in place to transform CGC from a traditional credit guarantee provider into a more effective and financially sustainable institution that can better serve the current and evolving needs of SMEs through the provision of a wider range of products and services.

In 2008, CGC focused on putting in place the necessary infrastructure to reduce its dependency on financial assistance from the Government and thus achieve financial sustainability. CGC has turned to the capital market to raise funds, introduced more dynamic investment strategies and enhanced loan quality management. CGC has also established a new business model that would be implemented in the second half of 2009.

Since its establishment in 1972, CGC has guaranteed more than RM40 billion worth of financing to more than 385,000 SMEs with insufficient collateral.

**(b) Transformation of Bank Pertanian Malaysia**

In 2008, Bank Pertanian Malaysia has been re-branded and renamed as Agrobank to widen its appeal to its core customer base. The corporatised Agrobank, now with a strengthened capital position, has been operational since April 2008. With strengthened institutional and financial capabilities, Agrobank is positioned to be effective and instrumental in supporting and promoting the development of the agriculture and agro-based sector, by providing a broader range and more innovative financial and non-financial products and services to meet the financing and developmental needs of the sector. Agrobank is currently embarking on a series of enhancement measures to strengthen its capacity and capability, particularly in the areas of product development, risk management and information technology systems enhancement.

**(iv) Strengthening the Provision of Financial Advisory Services**

Initiatives have also been taken to ensure that a comprehensive financial advisory services infrastructure is in place to help SMEs. SMEs can utilise the various avenues made available to channel queries, complaints and seek assistance to rehabilitate problematic businesses. Bank Negara Malaysia provides these services through the following:

**(a) BNMLINK**

Bank Negara Malaysia's Laman Informasi Nasihat dan Khidmat (BNMLINK) continues to provide financial advisory services to the SMEs in the following areas:

- Information on various sources of financing available to SMEs;
- Assistance in facilitation of the loan application process; and
- Advice on SME financial requirements and problems.

As at end-2008, the number of enquiries and assistance sought by SMEs totaled 12,880 reflecting continued awareness among SMEs of the availability of such services in Bank Negara Malaysia. Of these, 83% were mainly enquiries on special funds provided by the Government and advice on loan matters, while the remaining were requests for assistance, mainly on loan restructuring and loan rejections.

**(b) BNMTELELINK**

To complement the walk-in counter services offered by BNMLINK, the BNMTELELINK, Bank Negara Malaysia's dedicated Contact Centre was launched in 2007. BNMTELELINK facilitates members of public including SMEs, to bring their queries and complaints to the Bank via telephone, or in writing via the fax, email or post. BNMTELELINK can be contacted at:

Tel.: 1300 88 5465
Fax: 03 – 2174 1515 / 03 – 2174 1616
Email: bnmtelelink@bnm.gov.my

In addition to the above services by Bank Negara Malaysia, financial advisory services are also being provided to SMEs by all commercial banks through the respective SME Units; the SME Bank through its Advisory Centre (SAC); and the Credit Guarantee Corporation Malaysia Berhad (CGC) through its Business Advisory Services Entity (BASE) panel consultants. The Association of Banks Malaysia (ABM) has also taken steps to enhance communications with business associations, chambers of commerce and members of the public to increase awareness on access to and management of financial products and services. ABM launched a toll-free service at 1300-88-9980 to receive queries and complaints on issues relating to the banking industry and general concerns about credit.

# Monetary and Financial Conditions

# Monetary and Financial Conditions

## OVERVIEW

The direct impact of the global financial crisis on the Malaysian financial conditions in early 2008 was relatively modest as domestic financial institutions and markets had negligible exposures to structured credit products. In addition, domestic financial institutions had strengthened and built significant buffers during the decade after the Asian financial crisis. Nevertheless, capital flows driven by the deleveraging by international financial institutions created increased volatility in the domestic financial markets. The deepening financial crisis and worsening global economic outlook, particularly during the fourth quarter of 2008, had affected sentiments in the financial markets.

While the domestic monetary and financial conditions in 2008 were affected by the short-term capital inflows during the first half of the year and reversals in the second half of the year arising from deleveraging activities by international financial institutions, the credit market was well supported by a strong banking sector and liquidity remained ample. During the year, interest rates remained supportive of financing the economy. Critically, while the developed economies experienced a severe credit crunch due to dysfunctional financial institutions and markets, the credit situation in Malaysia remained resilient. Domestic financial institutions and markets continued their intermediation function effectively.

## INTERNATIONAL MONETARY AND FINANCIAL CONDITIONS

In 2008, the international financial markets were mainly characterised by the two-fold concern of rising global inflation in the first half of the year and the sharp deterioration in the health of the global financial system in the second half of the year.

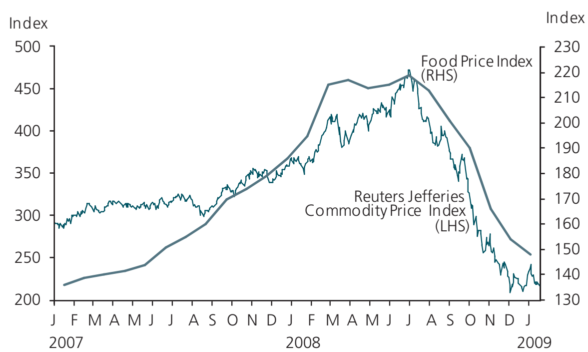
In the first half of the year, inflation rates globally rose significantly due mainly to the sharp rise in the prices of a wide range of commodities. The increase resulted from strong demand from emerging economies, short-term supply constraints and the shift of funds to commodities as an asset class. Global oil prices rose to unprecedented levels, breaking the USD100 per barrel mark for the first time in history. Concurrently, global food prices also rose to record levels. Notably, rising biofuel production which fueled the demand for corn and rapeseeds oil, spilled over to other foods through demand and crop substitution effects. The sharp surge in oil prices could not be entirely explained by fundamentals alone. The combination of the depreciating US dollar in the first half of 2008, rising credit risk in advanced economies and investors' search for a hedge in oil futures had increased the attractiveness of oil and other storable commodities as alternative assets.

## Stress in the global financial system intensified in 2008, exacerbating the deleveraging process

The impact of high food and fuel prices on inflation was especially felt in emerging market economies, owing to the higher share of food and fuel in the consumption baskets. In addition, the removal of subsidies to contain the fiscal burden also contributed to the significant rise in the headline inflation in several of these economies.

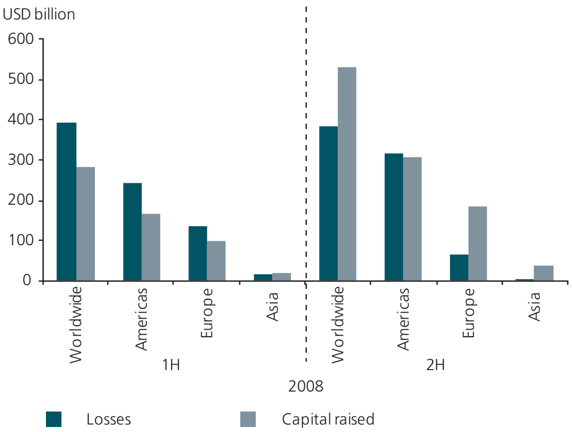
Against the backdrop of inflation concerns, international financial markets continued to experience significant disruptions throughout the year. The global financial turmoil that began with the collapse of the US sub-prime mortgage market in mid-2007, and the end of the housing market

**Chart 2.1**
**Food and Commodity Price Indices**



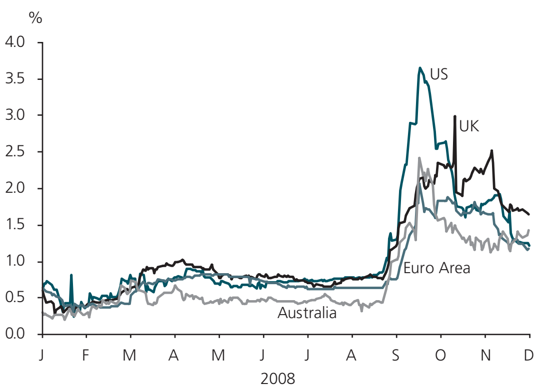

Source: Bloomberg, Food And Agriculture Association (FAO)

**Chart 2.2**
**Financial Institutions Losses and Capital Raised**




Source: Bloomberg

**Chart 2.3**
**Money Market Spreads[1]**




[1] 3 month LIBOR less 3 month Overnight Index Swaps (OIS)
Source: Bloomberg

boom, spread to other financial markets. The rise in delinquencies in the US sub-prime market complicated the valuation of asset-backed securities that used the sub-prime mortgages as their underlying assets. Price discovery for all structured products became problematic, resulting in bouts of panic and tightening liquidity conditions. The health of the financial sector worsened as many major financial institutions posted large write-downs and losses. With the erosion of the capital base and inability to raise sufficient funds to meet regulatory requirements, the US banking sector began to show signs of severe distress.

The liquidity crisis turned into a full-fledged solvency and confidence crisis in the second half of the year. The bankruptcy of a US investment bank, Lehman Brothers, in September 2008 triggered a freeze in the interbank money markets as confidence in counterparties faded. Corporate debt spreads widened sharply to reflect the heightened default risk as well as concerns of possible further failures of financial institutions. At the same time, banks' reluctance to lend to one another globally resulted in acute shortages in dollar liquidity, driving short-term US dollar rates upwards.

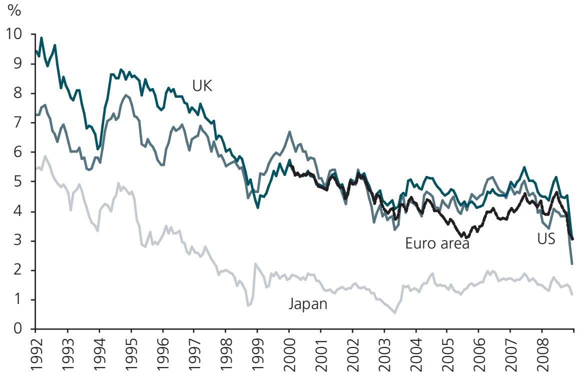
The global deleveraging process accelerated as financial institutions addressed the need to reduce their debts and repair their balance sheets. This led to the large sell-off in the global equity markets. The yen also appreciated sharply against all currencies as carry trades were unwound and funds were repatriated back to Japan beginning September 2008. Meanwhile, investors sought safe-haven assets, such as US Treasury bond, and drove long term yields down by around 150 basis points in the fourth quarter to near all-time lows.

As bank losses escalated, there was a heightened concern of a global credit crunch. The combination of sustained uncertainty in global financial markets and significantly weaker financial institutions weighed heavily on financing conditions. Banks in the major economies also tightened their supply of credit due to the less favorable economic outlook, the reduced tolerance for risk and the decline in customers' creditworthiness.

**Chart 2.4**
**MSCI Equity Market Indices**

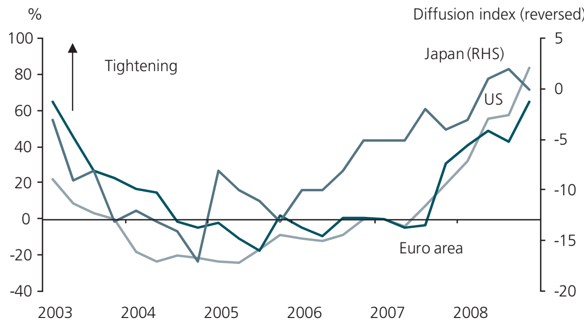

Source: Bloomberg

**Chart 2.5**
**Developed Markets 10-year Sovereign Yields**



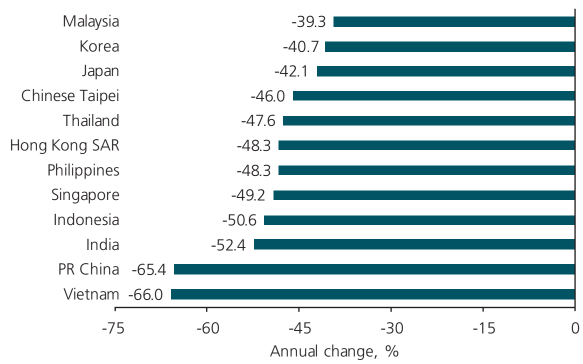

Source: Bloomberg

**Chart 2.6**
**Bank Lending Conditions[1] for Business**




[1] Based on Senior Loan Officer Survey conducted in selected countries
Source: Central Banks' Websites

**Chart 2.7**
**Performance of Asian Equity Indices in 2008**




Source: Bloomberg

During the year, the major central banks and governments responded to the challenging financial environment by aggressively reducing policy rates and expanding the range of their liquidity facilities. Further measures were then deployed to recapitalise weakened financial institutions through direct cash injections and the purchase of equity stakes in these institutions.

Inevitably, emerging markets were affected by the global financial crisis due to the increased financial linkages with the major economies. Several countries in the former Eastern Bloc such as Ukraine and Hungary were significantly affected given their substantial exposure to the financial markets of the advanced economies, high domestic credit growth and weak external positions. The initial financial effects of the crisis, however, were largely averted in most Asian economies due to their limited direct exposure to the US credit derivatives markets. Nevertheless, pressures on the emerging economies intensified as concerns that a protracted global credit crunch and the sharp deterioration in global growth outlook would severely affect regional economic activity. The combination of the global deleveraging process as well as the downward revision on earnings expectations had large ramifications on the region. As a result, equity markets in the Asian region declined by 30-70% in 2008. Capital outflows from the region increased during the year as funds were repatriated to the United States.

The escalating crisis led emerging Asian economies to take decisive actions to sustain confidence. Some of the measures included providing deposit guarantees and the injection of liquidity into the financial markets. Collaborative efforts with major economies through the introduction of foreign currency swap lines helped to ease tensions in the money markets. Monetary policy was also eased to address mounting concerns on the growth prospects. In addition, governments implemented large fiscal stimulus packages to mitigate the risk of a deep and protracted slowdown in their respective domestic economies. Nevertheless, ongoing concerns on tightening external financing conditions, volatile capital flows and the uncertain growth outlook, continued to weigh on emerging markets.

## DOMESTIC MONETARY AND FINANCIAL CONDITIONS

### Exchange rate

The broad appreciating trend of the ringgit in 2007 continued into the early part of 2008. Underlying demand for the ringgit was driven by the positive net trade balance, as high commodity prices continued to support Malaysia's export performance. The ringgit demand was also augmented by significant inflows of portfolio funds given Malaysia's limited direct exposure to the global financial crisis and a sound financial system, as well as the relatively resilient prospects for economic growth. The increased expectations for a weaker economic growth in the US had also led to the broad weakness of the US currency against regional currencies, including the ringgit. The ringgit appreciated by 10.6% from end-2007 to RM3.1315 against the US dollar on 23 April 2008. This is the strongest level against the US currency since the move to the managed float exchange rate regime in July 2005.

## Ringgit adjusted with the global financial market developments

This trend reversed towards the end of April due to a reversal in these investment flows. The failure of Bear Stearns and other financial institutions in the developed economies significantly increased counterparty risk and raised concerns over the possibility of broader systemic failures. The collapse of Lehman Brothers in September further intensified the unwinding of investments in emerging economies as the international financial institutions commenced to deleverage.

Despite the strong underlying demand for the ringgit due to the positive net trade balance, the ringgit was significantly affected by these global developments. Between May and December 2008, the ringgit oscillated around a broad depreciating trend similar with other regional currencies following rapid change in sentiments in the financial and the currency markets. While the ringgit weakened to RM3.6375 on 5 December 2008, the ringgit ended the year at the US dollar exchange rate of 3.4640, or 4.5% lower compared to the end of 2007.

**Chart 2.8**
**Exchange Rate of the Malaysian Ringgit (RM) Against Major Currencies**

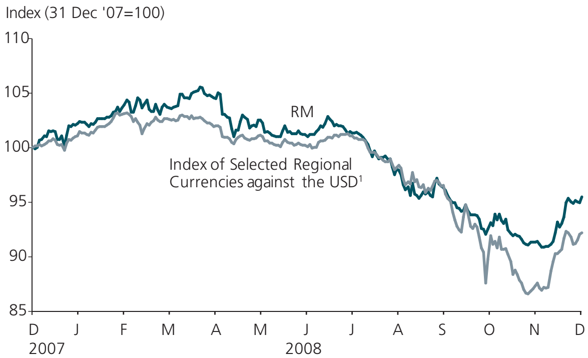

Note: An increase in the index indicates an appreciation of ringgit against the currency
Source: Bank Negara Malaysia

The ringgit also ended the year weaker against the Japanese yen as the large unwinding of yen carry trades increased the demand for the Japanese currency. The ringgit, however, ended the year stronger against the pound sterling, and was relatively unchanged against the euro. The pound sterling was adversely affected by the deterioration of the British economy and concerns surrounding the UK financial system.

Ringgit performance against the regional currencies was mixed. Although other regional currencies were similarly affected by the trend in major currencies, intra-regional exchange rate performance was differentiated by country specific factors. In particular, the Korean won and the Indonesian rupiah weakened significantly against most currencies. Both currencies had experienced a significant degree of market overshooting as their earlier rapid appreciation quickly turned into sharp depreciation.

In a more volatile and uncertain global environment, the managed float regime has provided the requisite flexibility for the ringgit to adjust to global economic and financial developments. At the same time, the current regime has also accorded a degree of exchange rate stability against the country's main trading partners. While there were concerns that the ringgit depreciation against the US dollar and the Japanese yen had increased the cost of

**Chart 2.9**
**Exchange Rate of the Malaysian Ringgit (RM) and Selected Regional Currencies Against the US Dollar**

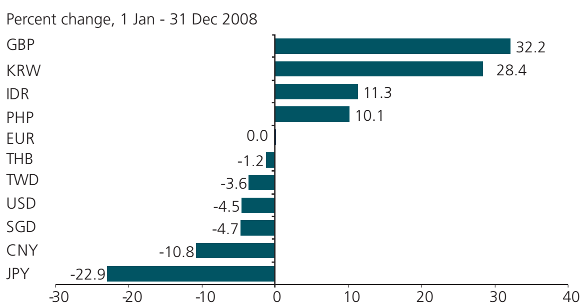



[1] Regional currencies: Chinese renminbi, Indonesian rupiah, Korean won, Philippine peso, Singapore dollar, New Taiwanese dollar and Thai baht. Each currency is of equal weight

Note: An increase in the index represents an appreciation of the ringgit or selected regional currencies against the US dollar

Source: Bank Negara Malaysia

**Chart 2.10**
**Summary of Malaysian Ringgit (RM) Performance Against Major and Regional Currencies in 2008**




Note: (+) indicates an appreciation of the ringgit against foreign currency
Source: Bank Negara Malaysia

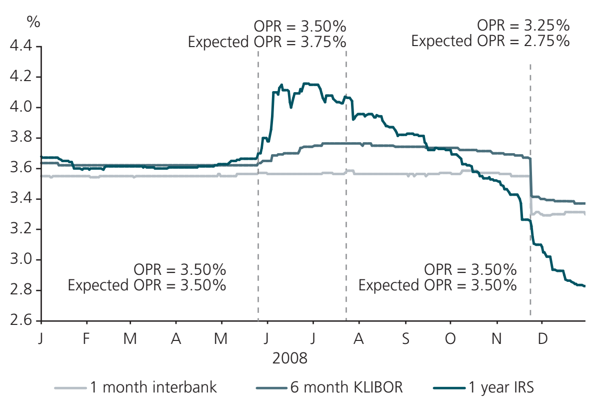
imports, especially productive inputs, only 24% of Malaysia's imports are sourced from the US and Japan. During the year, the average price increases of consumer goods and services in the US and Japan were lower than the price increase in Malaysia, which partially offsets the impact of ringgit depreciation against these currencies. A better measure for Malaysia's international purchasing power is the real effective exchange rate (REER). The REER is the weighted average of the ringgit against the currencies of our major trading partners and is adjusted for differences in price changes. By this measure, the REER for the ringgit depreciated by only about 1.5% during the year.

**Interest rates, bond yields and equity prices**
During the year, interest rates were low and stable to support the financing needs of the economy. Domestic interest rates reflected Bank Negara Malaysia's monetary policy stance, which in turn was driven by the Bank's assessment of the relative risks to growth and price stability. The thrust of monetary policy is to promote price stability in an environment of sustainable economic growth over the medium term.

## Interest rates were strongly supportive of the economy

The overnight, one-week and one-month interbank rates were relatively stable in the first eleven months of the year, trading closely to the overnight policy rate (OPR). Medium term money market rates, however, were influenced by expectations of OPR movements. After remaining stable for the first six months, KLIBOR and interest rate swap (IRS) rates rose as markets anticipated a monetary policy response to rising inflation. The OPR was however left unchanged and the rates were subsequently pared down. Towards year-end, interbank rates adjusted downward following the 25 basis points reduction in OPR on 24 November.

**Chart 2.11**
**Money Market Rates**

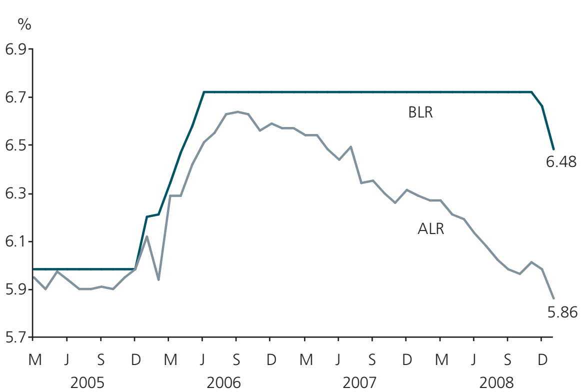



Note: Expected OPR compiled from analyst consensus at Bloomberg
Source: Bank Negara Malaysia and Bloomberg

Retail lending rates were near historic lows throughout 2008. Borrowers in both the household and business sectors continued to benefit from low interest rates. Low lending rates were underpinned by two factors. First, the low cost of funds as a result of the accommodative monetary policy stance and ample banking system liquidity. Second, the intense competition between banks kept the margins charged on loans low. Notwithstanding these factors, some upward pressures emerged in the money market during the middle of the year following expectations for monetary policy tightening as inflation rose significantly. Consequently, hire purchase loans were re-priced upwards in tandem with the rising cost of hedging fixed-rate loans through the interest rate swaps market. Such uptrend in interest rates proved to be temporary as market expectations for an OPR adjustment receded as the global and domestic growth outlook began to soften. After Bank Negara Malaysia reduced the OPR in November, lending rates to businesses and households declined. Consequently, the average lending rate (ALR) on loans outstanding ended the year at a new historic low of 5.86%.

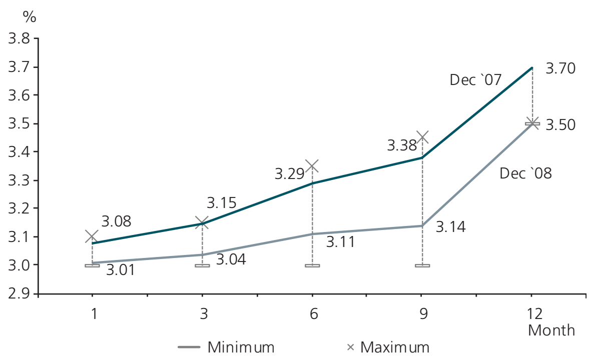
Meanwhile, deposit rates were stable in the first eleven months of the year. The downward pressure on deposit rates was mitigated by the interest rate floor imposed by the Bank on fixed deposit (FD). In contrast to the stable nominal interest rates, real interest rates declined and turned negative in May following the sharp increase in inflation.

**Chart 2.12**
**Commercial Banks' Lending Rates (at end-period)**




Source: Bank Negara Malaysia

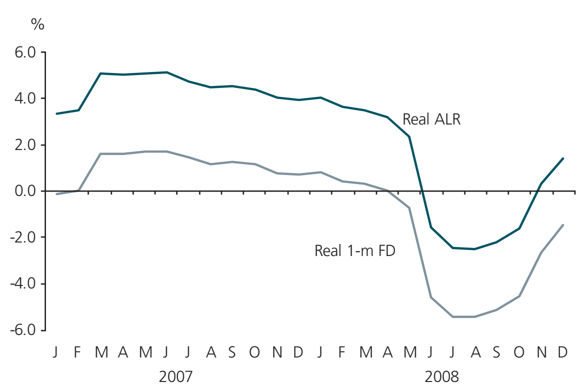
**Chart 2.13**
**Commercial Banks' Fixed Deposit Rates**




Source: Bank Negara Malaysia

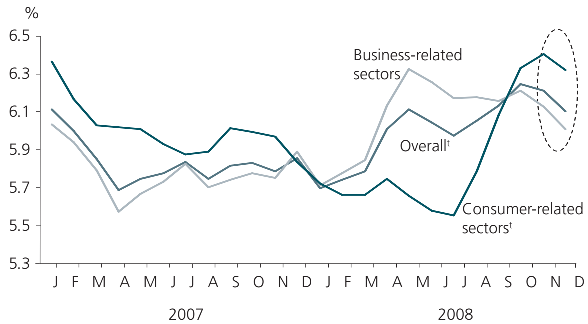
The reduction in the OPR in November was rapidly transmitted to retail lending rates. Twenty banks reduced their base lending rate within two weeks of the OPR cut. In addition, the magnitude of the pass-through was sizeable, as banks passed on the interest rate reductions to their customers. The average BLR of the commercial banks fell from 6.72% in October to 6.48% in December. Consequently, rates on loans approved to businesses and households fell by 26 and 25 basis points respectively in the following month, fully reflecting the 25 basis points reduction in the OPR. Deposit rates also fell as the reduction in the OPR was accompanied by a downward revision of the floor on FD rates.

**Chart 2.14**
**Real Deposit and Lending Rates**



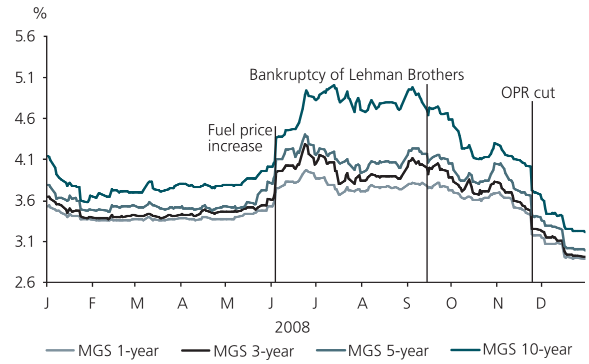

Source: Bank Negara Malaysia

**Chart 2.15**
**Commercial Banks' ALR on New Loans Approved (3-month moving average)**




[t] Excludes loans for the purchase of residential property and credit cards.
Source: Bank Negara Malaysia

**Chart 2.16**
**MGS Yields**




Source: Bank Negara Malaysia

In 2008, sovereign bond yields were mainly influenced by inflation expectations and concerns over the growth outlook. In the first half of the year, expectations of higher domestic inflation led yields to gradually trend upwards, especially in the longer-tenures. The rise, however, was mitigated by the large inflows of capital into the equity and bond markets, as investors rebuilt their portfolio in the beginning of the year. The expectations of a further strengthening of the ringgit on account of the resilient performance of the economy also kept yields low and stable.

## Sovereign yields reflected the changing outlook for growth and inflation

Inflationary expectations intensified in June following the increase in retail fuel and electricity prices. This, in turn, heightened expectations of a monetary policy tightening and raised MGS yields considerably. As investors weighed the higher interest rates outlook going forward, yields for the 10-year and 3-year MGS rose sharply by 84 and 50 basis points respectively in June. The maturity spread between the 10-year and shorter-term MGS also widened, resulting in the steepening of the slope of the yield curve. Furthermore, yields remained high as foreign investors unwound their portfolio investments as the global financial crisis intensified further.

By September, however, yields began to fall as inflation expectations eased. In addition, the deepening global financial crisis resulted in extreme risk aversion among investors. Investors increased the demand for risk-free and lower risk assets and shifted their investments from the equity to the government securities markets, driving yields further downwards.

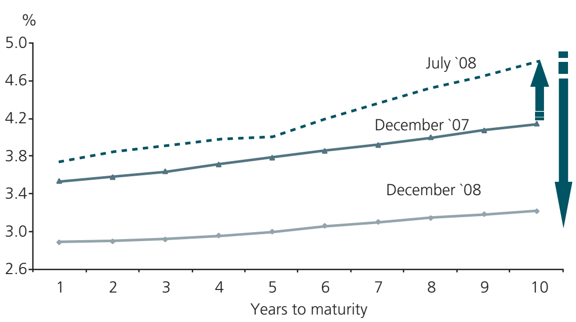
With pronounced indications of dissipating domestic inflationary pressures and mounting concerns over the economic slowdown, expectations of a reduction in OPR surfaced towards year-end. The reduction in OPR on 24 November was therefore, immediately and fully transmitted in the sovereign bond market, as reflected by the decline in yields across all maturities. In December, long-term MGS yields continued to decline to levels that were below the OPR as investors priced-in further policy interest rate cuts following the release of weak economic data. The bond-swap spreads for short to medium-term securities remained negative reflecting such expectations.

The movements of private debt securities (PDS) yields broadly mirrored those of the MGS in the first half of the year. In June, however, uncertainties with regard to debt issuers' viability arising from the imposition of windfall tax on Independent Power Producers (IPPs) and palm-oil plantation companies led to the deterioration in investor sentiments. As a result, liquidity in the PDS market declined significantly, raising yields sharply upwards.

**Chart 2.17**
**MGS Maturity Spread**


Source: Bank Negara Malaysia

**Chart 2.18**
**MGS Benchmark Yield Curve**




Source: Bank Negara Malaysia

Investors' sentiments were further undermined by concerns about creditworthiness arising from prospects of lower earnings in the second half-year.

## PDS yields affected by rising risk premiums

PDS yields, therefore, remained at elevated levels due to the higher risk premiums. The rebalancing of portfolio allocations by investors from the more risky PDS to sovereign papers also contributed to the increase in yields. These culminated into a significant widening of the spread between MGS and

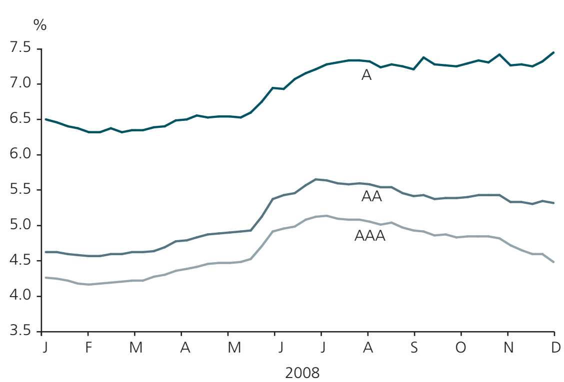
**Chart 2.19**
**Bond-Swap Spread[1]**


[1] Interest Rate Swap minus MGS yields
Source: Bank Negara Malaysia

PDS yields. Credit spreads began rising sharply in November as the magnitude of the decline in MGS yields exceeded that of the PDS. Notably, larger spreads were recorded for the lower-rated securities. Although PDS yields had not fallen as much as MGS yields, issuances of higher-rated PDS remained relatively healthy during the period.

Equity prices were volatile due to domestic and external developments during the year. The Kuala Lumpur Composite Index, KLCI, was subjected to significant volatility because of its large exposure to the resource-based sectors that were affected by the substantial

**Chart 2.20**
**PDS Yields (5-year)**

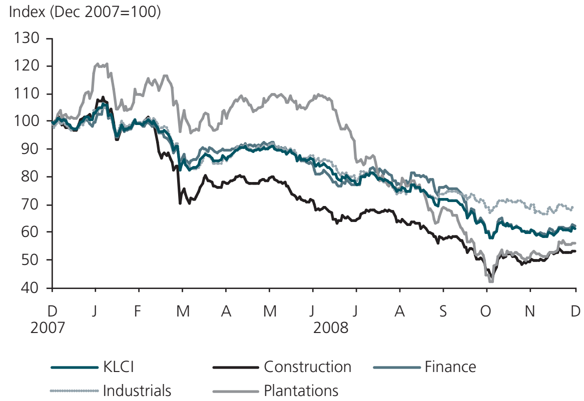



Source: Bank Negara Malaysia

**Chart 2.21**
**Corporate Yield Spread Against MGS (5-year)**


Source: Bank Negara Malaysia

**Chart 2.23**
**KLCI and Bursa Malaysia Sectoral Indices**



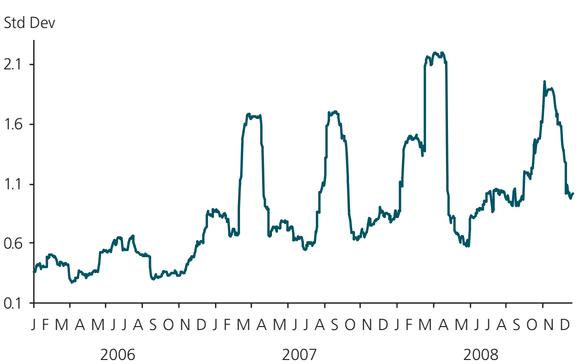

Source: Bloomberg

fluctuations in commodity prices. The KLCI volatility was further augmented by outflows of funds driven by the worsening of sentiments in the financial markets and deleveraging activities by foreign investors. Widespread expectations of deteriorating earnings also influenced domestic sentiments and further amplified market volatility.

## Share prices were volatile and on downward trend

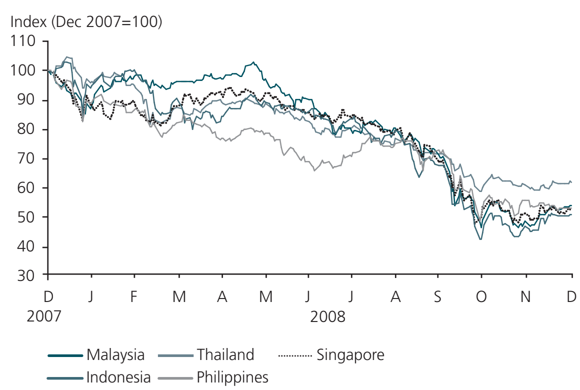
Uncertainties with regard to the US financial turmoil and the outcome of the general election in March led to weak market sentiments in the first half-year. Despite these uncertainties, the index remained buoyant, supported by gains in plantation-related stocks that benefited from rising commodity prices. In the second half of the year, however, a further deterioration in global and domestic sentiments exerted downward pressure on equity prices. The high cost of raw materials and increases in utilities charges, amid slower economic growth prospects, adversely impacted firms' earnings, and consequently, companies' valuations. Towards year-end, falling commodity prices, extreme risk aversion and deleveraging activities brought share prices further down. For the year as a whole, the KLCI fell by 39.3% to 876.8. The decline in the KLCI was broadly similar to that experienced in other regional markets.

**Chart 2.22**
**Volatility of Returns on the KLCI[1]**




[1] Refers to 30-day rolling standard deviation of daily returns
Source: Bloomberg

**Chart 2.24**
**Regional Indices**




Source: Bloomberg

**Liquidity**
Liquidity conditions were ample throughout 2008. Malaysia's deep integration with the world economy through trade and financial links, however, meant that domestic liquidity was affected by global developments. As such, domestic liquidity, as measured by broad money, or M3, exhibited two distinct phases in 2008.

## Domestic liquidity affected by foreign deleveraging but remained ample

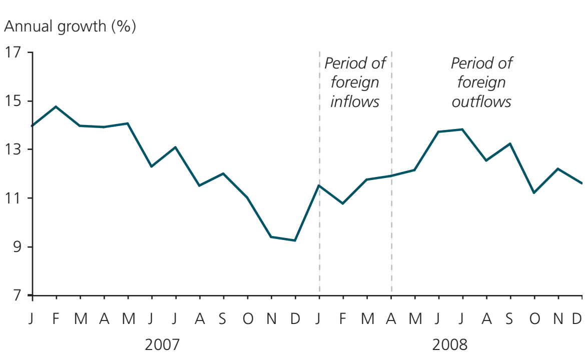
In the first half of the year, broad money increased at a faster pace. The increase was underpinned by both external and domestic factors. On the external side, foreign inflows rose substantially on account of Malaysia's trade surplus and portfolio inflows. Credit growth to the private sector also increased, as banks continued to provide financing in line with the faster pace of economic activity. Broad money growth peaked in July, with an annual growth rate of 14.1% (end-December 2007: 9.5%).

In the second half of the year, the deleveraging process among international financial institutions created a strong demand for US dollars, causing sudden and large outflows from Malaysia. These exerted a contractionary impact on broad money. The effect of the outflows on broad money, however, was partially offset by the sustained pace of lending by the domestic banking sector. In addition, broad money growth was also supported by higher Government spending, which was financed through the issuances of government securities, some of which were taken up by the banking sector. Accordingly, monetary aggregates continued to grow, albeit at a slower pace, in the second half of 2008. Broad money, or M3, ended the year with a growth rate of 11.9% in December.

Bank Negara Malaysia conducted operations in the money market to ensure that the level of liquidity was sufficient to meet the financing needs of the economy. In the first half of 2008, the Bank mopped up a higher amount of excess liquidity in order to prevent over expansionary liquidity conditions. This was achieved through the utilisation of a wide range of monetary instruments in the Bank's sterilisation operations, including direct borrowing, repos and the issuance of Bank Negara Monetary Notes (BNMNs). Accordingly, excess liquidity remained modest.

Large outflows of liquidity following foreign selling of domestic assets were compensated by the

**Chart 2.25**
**Broad Money, M3**




Source: Bank Negara Malaysia

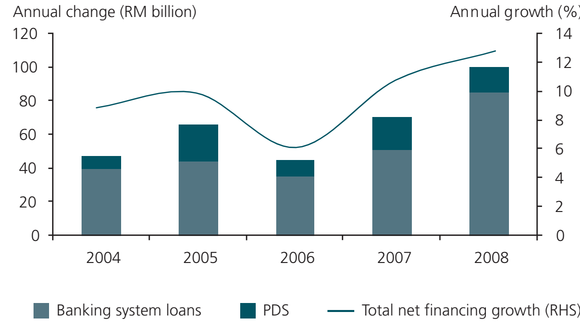
**Table 2.1**
**Broad Money, M3**

| | Change (RM billion) | |
|---|---|---|
| | 2008 | |
| | 1H | 2H |
| **M3** | **66.4** | **32.7** |
| Currency in circulation | 2.9 | 1.3 |
| Demand Deposits | 5.3 | 5.8 |
| Broad Quasi-Money | 58.3 | 25.6 |
| *Fixed deposits* | *14.8* | *13.2* |
| *Savings deposits* | *4.0* | *3.8* |
| *NIDs* | *-0.3* | *0.4* |
| *Repos* | *1.1* | *-4.1* |
| *FX deposits* | *11.5* | *5.1* |
| *Other deposits* | *27.2* | *7.1* |
| **Determinants of M3** | | |
| Net claims on Government | -4.1 | 37.6 |
| Claims on the private sector | 43.3 | 51.7 |
| *Loans* | *40.2* | *36.5* |
| *Securities* | *3.1* | *15.2* |
| Net foreign assets* | 48.7 | -95.4 |
| *Bank Negara Malaysia** | *68.4* | *-80.9* |
| *Banking system* | *-19.7* | *-14.6* |
| Other influences | -21.5 | 38.8 |

* Pre-revaluation of the international reserves

release of liquidity kept with the Bank. The large net interbank placements with the Bank acted as a liquidity buffer for the banking system. While the size of the surplus liquidity was reduced by outflows, liquidity in the banking system, nonetheless, remained in surplus. This was evident by the loan-deposit ratio remaining at modest levels, ranging between 72.5 in July to 73.5 in December. At the institution level, 49 out of 54 banking institutions operated from a position of surplus liquidity with net placement of funds with the Bank. The large number of institutions with a surplus of liquidity supported the domestic banking system's resilience by limiting over reliance on wholesale funding. The Bank also ensured adequate US dollar liquidity to prevent any shortage in foreign currency for trade activities.

**Chart 2.26**
**Net Financing to the Private Sector through Banking System Loans and PDS**




Source: Bank Negara Malaysia

### FINANCING OF THE ECONOMY

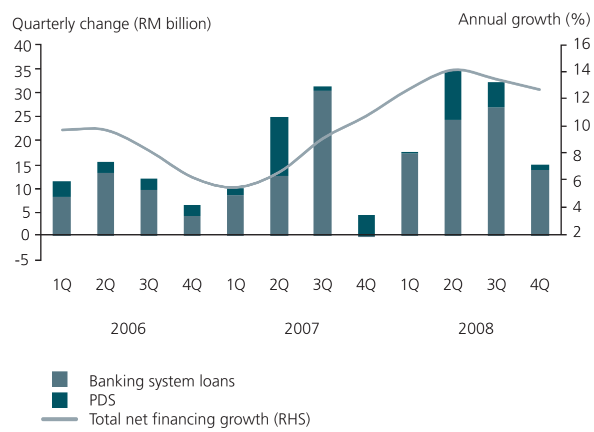
In 2008, the domestic credit situation remained conducive to sustainable growth. While inflationary pressures in the first three quarters of 2008 reflected the impact of the commodity price shock, credit expansion was broadly in line with the underlying economic conditions, and this helped to limit the potential for second-round effects of inflation.

## Banking sector and capital markets continued to support demand for financing

Of importance, while the developed countries faced severe credit crunch conditions, especially in the fourth quarter of the year, domestic credit conditions continued to remain favourable. Banking institutions and the financial markets continued to support the demand for financing of the economy. Total net financing[1] channeled to both the public and private sectors increased at a sustained rate of 11.5% (2007: 9.2%). There continued to be robust demand for financing from both households and businesses during the year. Towards year-end, however, the demand for financing slowed down somewhat due to the moderation in economic growth and the more cautious sentiments of the private sector.

Net financing to the private sector through banking system loans and PDS outstanding expanded at a faster annual pace of 12.7% in 2008 (2007: 11.3%). In the first three quarters of the year, robust private consumption underpinned by the continued resilience of the domestic economy, contributed towards the steady demand for financing. Additionally, the higher prices of raw materials, fuel and electricity resulted in a higher cost of operations and thus, raised the demand for financing working capital

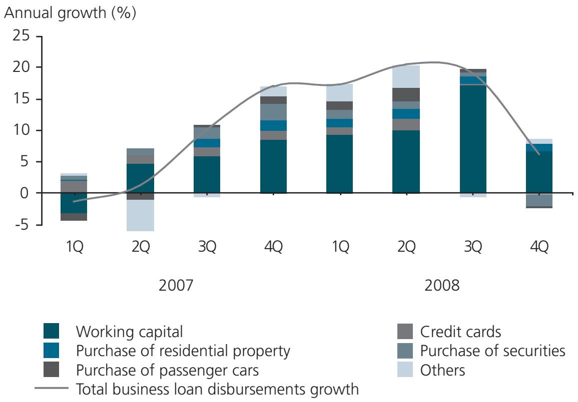
**Chart 2.27**
**Net Financing to the Private Sector through Banking System Loans and PDS**




Source: Bank Negara Malaysia

[1] Comprised financing provided by the banking system, capital market, development financial institutions (DFIs), insurance companies, leasing and factoring companies, housing credit institutions, Employee Provident Fund (EPF), Treasury Housing Loan Division and external sources.

**Chart 2.28**
**Loan Disbursements to Businesses: Total Growth and Contribution by Purpose**

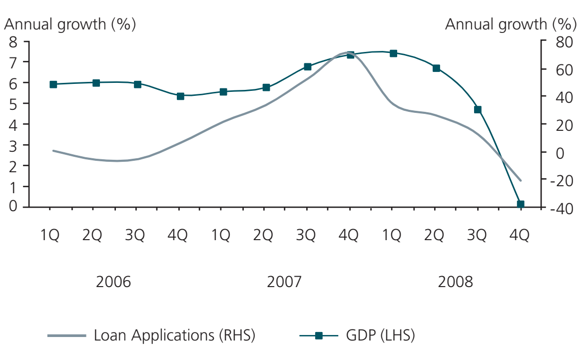



Note: Data excludes one large loan extended in 2007 for a privatisation activity
Source: Bank Negara Malaysia

by businesses. Loans disbursed for the purpose of working capital rose significantly at an annual rate of 22.1% in the first nine months of 2008 compared to 4.3% for the corresponding period in 2007. In particular, loan applications from the food and beverages industry increased by 87.1% during January to September 2008 compared to 1.2% for the corresponding period in 2007.

Banking system loan applications and approvals increased by 22.8% and 20.7% respectively in the first nine months of the year (2007: 36.7%; 37.5%)[2]. The absence of demand for financing of merger and acquisition activities, however, meant

**Chart 2.29**
**Loan Applications and GDP**




Data excludes one large loan extended in 2007 for a privatisation activity
Source: Bank Negara Malaysia

**Chart 2.30**
**Gross PDS Issued**


Note: Data excludes Cagamas bonds and issuances by non-residents
Source: Bank Negara Malaysia

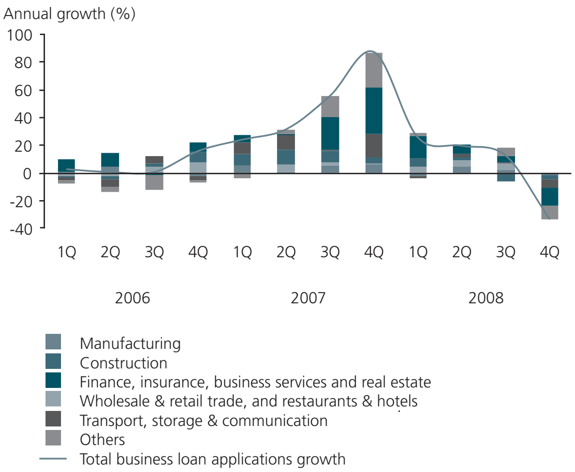
that growth in loan applications and approvals were smaller compared to the corresponding period in 2007. Despite bouts of weak market sentiment, PDS financing during the period was robust. Expectations of higher yields due to anticipated OPR increases, prompted businesses to secure financing ahead of the expected increase. In fact, the highest amount of issuance was recorded in June, prior to the July MPC meeting.

The demand for financing by households was supported mainly by the robust sales in residential properties and passenger cars. In part, the demand for mortgage financing was attributable to the various incentives introduced by the Government for the property sector in 2007, which included the flexibility to withdraw funds from the EPF Account II on a monthly basis for repayment of mortgages. The increase in commodity prices provided additional income to the rural population and these contributed to the demand for passenger cars and pick-up trucks. Higher prices of food, fuel and electricity by mid-year, however, raised the cost of living and reduced households' disposable income. Households became more cautious in their spending, as reflected by the decline in their discretionary expenditure. Consequently, by the third quarter, the growth of hire purchase loans, credit cards and mortgage financing moderated.

The effects of the sharper deterioration of the global economy began to have its impact on the

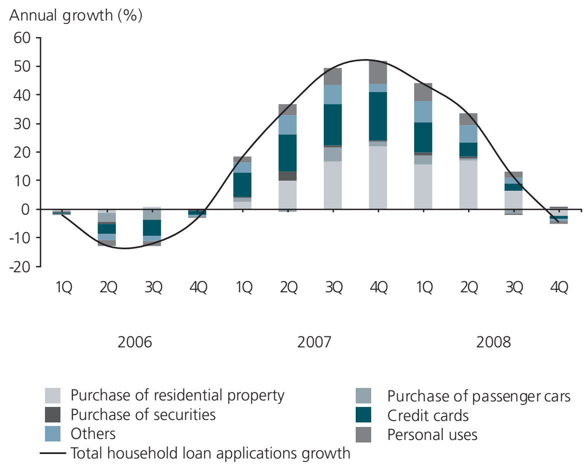
[2] The analysis on loan developments excluded one large loan extended in 2007 for a privatisation activity.

**Chart 2.31**
**Loan Applications by Businesses: Total Growth and Contribution by Sectors**




Note: Data excludes one large loan extended in 2007 for a privatisation activity
Source: Bank Negara Malaysia

**Chart 2.32**
**Loan Applications by Households: Total Growth and Contribution by Purpose**




Source: Bank Negara Malaysia

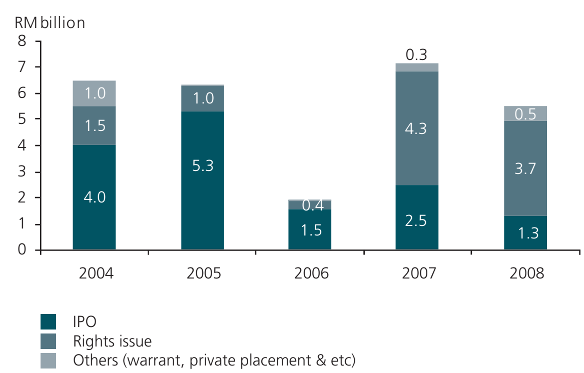
domestic economy in the fourth quarter of 2008. The decline in external demand led to a sharp and rapid contraction in exports and a slowdown in the pace of private investment, which in turn, affected labour market conditions. Coupled with weak sentiments in the financial markets, the demand for financing from both businesses and households moderated during the quarter. Loan applications by businesses declined across all economic sectors in the fourth quarter, with the exception of the wholesale, retail trade, restaurants and hotels sector. Loan applications by households, namely for housing, credit cards and personal loans, also contracted during the period. In the PDS market, the higher risk premiums demanded by investors made it more costly for firms to raise funds. Some issuers also chose to postpone their bond issuances in anticipation of lower yields in the future. Thus, despite a continued flow of approvals for issuances of PDS, actual issuances moderated as firms delayed their bond issuances. Funds raised through the equity market also declined to RM5.5 billion (2007: RM7.1 billion). Reflecting weak market sentiments, funds raised were mostly through right issues rather than initial public offerings (IPOs).

### Sources of financing

As the domestic financial institutions and markets continue to function efficiently, the private sector benefited from having the flexibility to choose the most effective sources of financing for its activities. In 2008, the banking system remained the largest provider of financing for the economy, with bank loans accounting for 42% of total financing. Meanwhile, financing through PDS issuances accounted for 15%, the third largest source after foreign direct investment. Reliance on external financing remained small at 5% due to ample domestic liquidity.

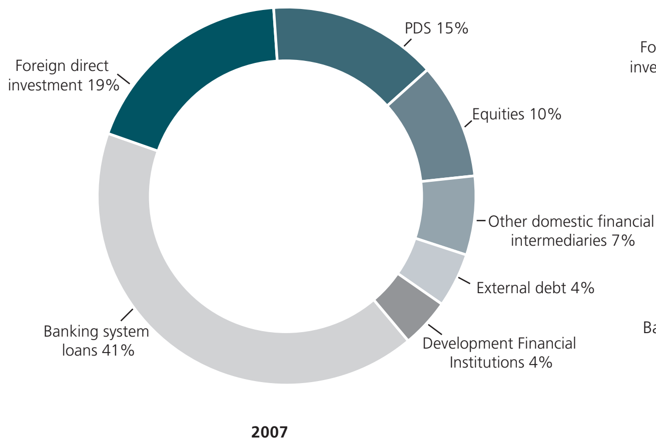
The choice of the sources of financing for the business sector primarily hinges on the purpose

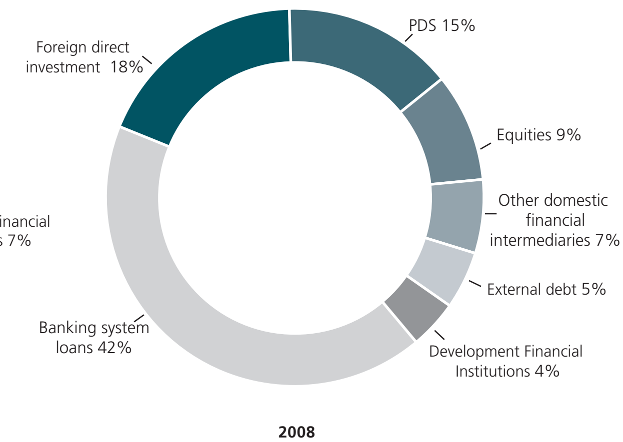
**Chart 2.33**
**Total Financing Raised via the Equity Market**




Source: Bursa Malaysia, Bank Negara Malaysia estimates

**Chart 2.34**
**Sources of Financing for the Private Sector**




Source: Bank Negara Malaysia

**Table 2.2**
**Special Funds for SMEs Administered by Bank Negara Malaysia**

| | RM million | | | | % |
|---|---|---|---|---|---|
| | Allocations | Approvals | Disbursements | Loans Outstanding | Utilisation Rate[1] |
| | As at end-2008 | | | | |
| **Special Funds** | | | | | |
| Fund For Food[2] | 1,300.0 | 1,730.4 | 1,707.0 | 255.7 | 78.3[3] |
| New Entrepreneurs Fund 2 | 2,850.0 | 3,544.6 | 3,351.4 | 2,261.9 | 90.0 |
| Fund for Small and Medium Industries 2 | 6,750.0 | 11,933.8 | 10,893.7 | 4,972.2 | 94.2 |
| Bumiputera Entrepreneurs Project Fund | 300.0 | 899.9 | 814.2 | 79.5 | 87.0 |
| Micro Enterprise Fund | 200.0 | 4.2 | 2.4 | 2.4 | 2.1 |
| **Total** | **11,400.0** | **18,112.8** | **16,768.8** | **7,571.7** | **90.3** |
| **SME Financial Assistance Schemes** | | | | | |
| SME Assistance Facility | 700.0 | 1,013.0 | 234.1 | 4.6 | |
| SME Modernisation Facility | 500.0 | 83.3 | 6.9 | 211.2 | |
| **Total** | **1,200.0** | **1,096.3** | **241.0** | **215.8** | |
| | Change during the year | | | | |
| **Special Funds** | | | | | |
| Fund For Food[2] | - | - | 0.5 | -84.5 | |
| New Entrepreneurs Fund 2 | - | 107.9 | 148.4 | -134.1 | |
| Fund for Small and Medium Industries 2 | - | 1,815.9 | 2,117.4 | 177.4 | |
| Bumiputera Entrepreneurs Project Fund | - | 139.6 | 158.0 | 8.2 | |
| Micro Enterprise Fund | 200.0 | 4.2 | 2.4 | 2.4 | |
| **Total** | **200.0** | **2,067.6** | **2,426.7** | **-30.6** | |
| **SME Financial Assistance Schemes** | | | | | |
| SME Assistance Facility | 700.0 | 1,013.0 | 234.1 | 4.6 | |
| SME Modernisation Facility | 500.0 | 83.3 | 6.9 | 211.2 | |
| **Total** | **1,200.0** | **1,096.3** | **241.0** | **215.8** | |

[1] Ratio of approvals over allocations and repayments.
[2] Exclude funds allocated by the Government under the Ninth Malaysia Plan.
[3] Exclude repayments of RM541 million that has been converted into Agrobank's equity.

Source: Bank Negara Malaysia

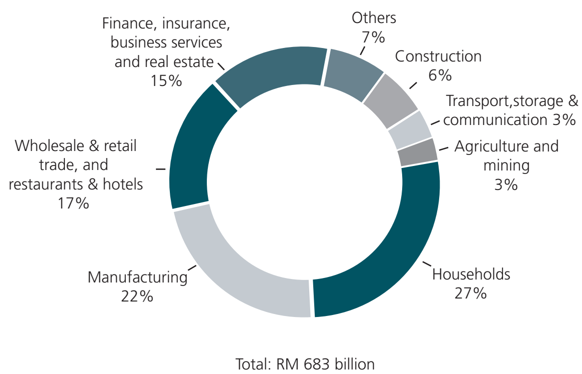
for which financing is being sought. In particular, firms issued PDS to finance larger and longer-term projects, and turned to the banking system for shorter-term financing needs such as for working capital. For the small and medium enterprises (SMEs) and micro enterprises, financing was primarily sourced from banking institutions and development financial institutions (DFIs). These were augmented by special funds established by Bank Negara Malaysia from time to time to achieve specific purposes. There has been in total, 21 funds set up by Bank Negara Malaysia since 1988. Currently, there are seven funds. The utilisation rate of the funds, excluding the guarantee facilities, stood at 90.3% in 2008. The household sector's credit requirements have been mostly met by the banking institutions. The availability of financing from the DFIs and insurance companies also widened the range of financing instruments and avenues for households and enhanced competition in the consumer credit segment.

**Direction of lending**

The steady flow of financing during the year was channeled across all the economic sectors and borrowers. Gross financing raised from the banking system and PDS market were extended mostly to the business sector, with the manufacturing, wholesale and retail trade, as well as finance, insurance, business services and real estate sectors, accounting for more than 50% of total gross financing. Amidst weakening external demand, financing to the manufacturing sector, which accounted for 22% of total gross financing, were mainly directed to the domestic oriented industries[3]. Financing to the household sector remained stable at 27% of total gross financing (2007: 28%).

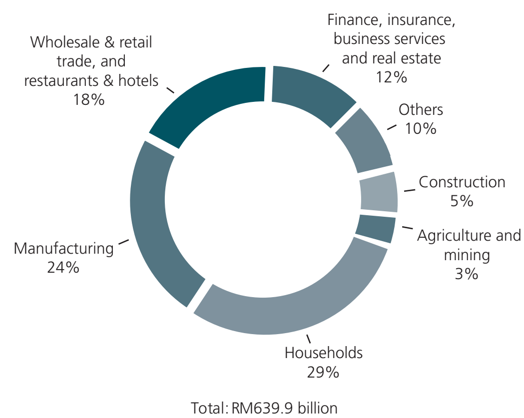
In the banking system, loans to the business sector were mainly disbursed to finance working capital. Disbursements of loans to the business sector were primarily channeled to the manufacturing, wholesale and retail trade, restaurants and hotels, and finance, insurance, business services and real estate sectors. Increased disbursement of loans to the business sector led to further expansion in outstanding business loans by 13.2% at end-2008 (2007: +10.3%). In the PDS market, funds were mostly raised to finance new investment activities. Of the total gross PDS issued in 2008, 60.6% was raised by firms from the finance, insurance,

**Chart 2.35**
**Gross Private Sector Financing in 2008**




Source: Bank Negara Malaysia

**Chart 2.36**
**Loan Disbursements by Sector in 2008**



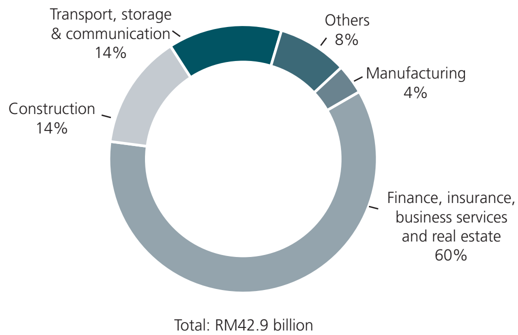

Source: Bank Negara Malaysia

business services and real estate sector. Of this amount, 21.7% was issued by the domestic banking institutions. Meanwhile, the transport, storage and communication, and construction sectors each accounted for 14% of total gross funds raised in 2008.

Loans extended to the SMEs accounted for 17.2% of total loans outstanding. Banking system loans to the SMEs rose by 9.4% at end-2008, after increasing by 13.2% in August 2008 (2007: 9.1%). The demand for financing by SMEs expanded at a more

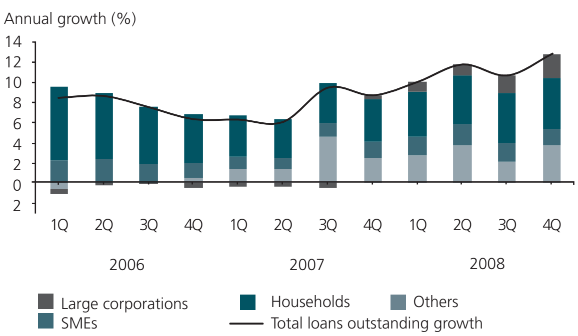
[3] Refers to food, beverages, transport-equipment, paper, tobacco and construction related industries.

**Chart 2.37**
**Gross PDS Issued by Sector in 2008**




Note: Data excludes Cagamas bonds and issuances by non-residents
Source: Bank Negara Malaysia

**Chart 2.38**
**Loans Outstanding:**
**Total Growth and Contribution by Customers**

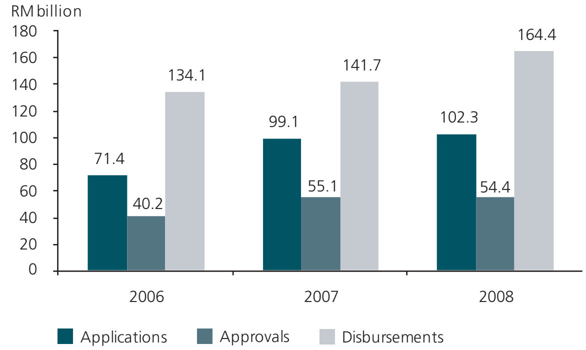



Data excludes one large loan extended in 2007 for a privatisation activity
Source: Bank Negara Malaysia

moderate pace during the year, with loan applications registering a slower growth of 3.3% (2007: 38.8%). The moderation was observed across all the economic sectors. Notwithstanding the slowdown in demand, loans disbursed to the SMEs in 2008 increased by 16% (2007: 5.6%), mainly to meet working capital requirements. Disbursements remained broad based with the manufacturing and wholesale and retail trade sectors accounting for 31% and 29% of total loan disbursements, respectively.

In July 2008, Bank Negara Malaysia introduced two financial assistance programs, the SME Assistance Facility and

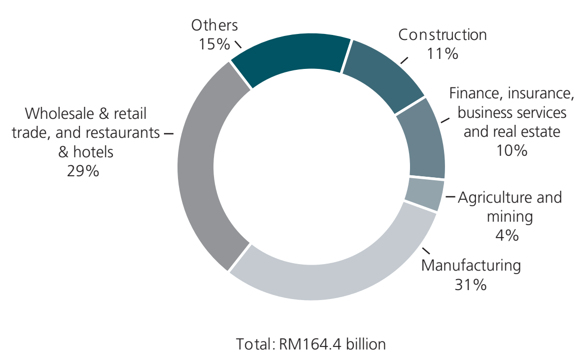
**Chart 2.39**
**Loan Indicators for the SMEs**




Source: Bank Negara Malaysia

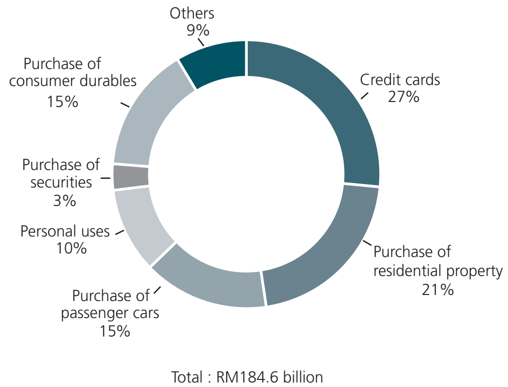
SME Modernisation Facility, totaling RM1.2 billion. These facilities were introduced to assist SMEs to overcome temporary cash flow problems arising from the higher cost of doing business as well as to promote higher efficiency and productivity through modernisation and upgrading of machinery, equipment and operations. In November, Bank Negara Malaysia launched the RM200 million Micro Enterprise Fund to broaden the access to financing for micro enterprises with viable businesses. In January 2009, Bank Negara Malaysia established a RM2 billion SME Assistance Guarantee Scheme (SAGS). The micro financing and guarantee scheme are aimed at ensuring that viable SMEs

**Chart 2.40**
**Loan Disbursements to SMEs by Sector in 2008**




Source: Bank Negara Malaysia

**Chart 2.41**
**Loan Disbursements to Households by Purpose in 2008**




Source: Bank Negara Malaysia

and micro enterprises which are facing temporary difficulties because of weakening demand, continue to have access to adequate financing.

In the household sector, loan disbursements increased at an annual rate of 8.9% (2007: 12.8%), and were primarily channeled to finance the purchase of residential properties and passenger cars. Consumption credit expanded at a slower pace. Growth in credit card spending fell markedly to 2.1% compared with 20.6% in 2007. Credit cards continued to be used largely as a mean of payment rather than as a mode of financing, as evident by the high repayment ratio[4] of 61.2%. With sustained disbursements of housing and car loans, loans outstanding to the household sector expanded at a faster pace of 9.1% (2007: 7.4%), accounting for 53.4% of the total increase in bank loans.

[4] Repayment ratio = [(total spending + cash advance) – outstanding balance] / (total spending + cash advance)

# Monetary Policy in 2008

# Monetary Policy in 2008

## OVERVIEW

Monetary policy in 2008 operated in a complex environment with rapidly changing inflation, economic and financial conditions. Monetary policy in the first half of the year was confronted with heightened risks of elevated inflation arising from supply-driven factors, and the risk that domestic demand could be affected by adverse external developments. The balance of risks to growth and inflation shifted rapidly during the course of the year. Inflation rose significantly to multi-year highs following high food and commodity prices and the Government's adjustment to domestic fuel prices. Notwithstanding the significant rise in headline and core inflation, price pressures were expected to moderate in 2009, as higher prices began to erode the purchasing power of households. In addition, the global financial turmoil was expected to have an adverse impact on the performance of the export sector.

**Monetary policy in 2008 operated in a complex environment emanating from supply-driven inflationary shocks, financial market contagion and decelerating global growth**

By the end of the third quarter, although headline inflation was still elevated in many countries including Malaysia, the evidence of its deflationary impact on growth had already become evident. By then, the financial turmoil had become more widespread and had begun to substantially undermine global growth. Concerns over the growth prospects began to take precedence over concerns about inflation. By the fourth quarter, the balance of evidence became strongly skewed towards the risks to growth, with the global growth and trade outlook deteriorating considerably and inflation in many countries starting to abate amidst rising slack capacity and retreating commodity prices.

## MONETARY POLICY IN 2008

At the beginning of the year, the risks of rising inflation and the uncertainties surrounding the growth outlook were about balanced. There were significant concerns regarding inflation. The prognosis earlier during the year was for headline and core inflation to continue trending upwards, reflecting the pass-through of the higher global food and commodity prices onto the domestic economy. On the growth front, domestic demand was strong during this period, though with a slight moderation compared to 2007.

While global food and commodity prices were expected to remain elevated, the upward pressures on domestic inflation were assessed to be fairly contained for several reasons. The presence of Government subsidies on fuel and certain food items mitigated the pass-through of higher global prices into domestic prices. In addition, labour costs were expected to rise at a pace commensurate with improvements in labour productivity. Furthermore, the weaker global economic outlook was expected to contain further increases in global commodity prices, thereby easing the domestic inflationary pressures emanating from food and commodity prices. The expectation therefore was that headline and core inflation would be higher. Overall, inflation was forecast to be 2.5% - 3.0%, with a gradual declining trajectory towards the end of the year.

On the growth front, economic activity remained resilient, underpinned by strong private consumption and investment. As a commodity producer, the economy received an additional boost from higher trade receipts, especially from the sale of crude palm oil, petroleum and rubber. The forecast was for the economy to expand by 5% - 6% in 2008, a rate that is close to its estimated potential output. Notwithstanding the relatively healthy outlook for GDP growth, there were considerable uncertainties with respect to economic prospects going forward. Rising inflation, especially of food prices, which comprise 31.4% of the average expenditure of the Malaysian consumer, had affected disposable incomes and threatened to reduce the discretionary spending of a large segment of Malaysian households. Profits of businesses were also affected by rising costs. Growth prospects were also bounded by moderating global growth which was gradually being weighed down by the financial turmoil in the major financial markets.

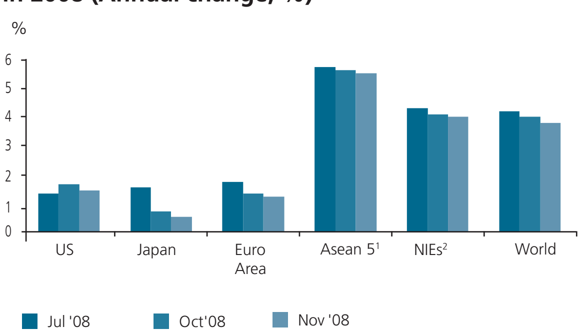
As a highly open economy, the most visible threat to Malaysia would be from the trade channel. While a large share of Malaysia's trade was with Asia, there were concerns that a rapid and significant decline in the final demand in the advanced economies, and an escalation in bearish consumer and business sentiments, could create significant risks to the external sector. There was also the risk of contagion, given the high integration of the Malaysian financial markets with the rest of the world. To Malaysia's advantage, Malaysian banks had minimal exposure to the problems in mortgage related products and markets of the advanced economies.

From the monetary policy perspective, the risks to growth and inflation in the first half of the year were therefore relatively balanced. As the risks of higher inflation and moderating growth became more evident as the year progressed, monetary policy was left unchanged. Monetary policy surveillance was focused on assessing the risks of second-round effects on inflation from the higher commodity prices. Indicators suggested that while inflationary expectations had increased, monetary conditions remained stable, and wage demands continued to be moderate and were largely compensated by productivity growth. Recognising the limited role of monetary policy in dealing with the first-round effects of supply-driven shocks on inflation, there was a greater focus by the Government on measures to improve and increase production as well as reduce costs. In relation to this, the movement of rice across state borders was freed in stages to increase competitiveness and lower domestic prices, and rice buffer stocks were raised through increased imports from Thailand.

## The monetary policy dilemma intensified significantly when inflation surged following the significant fuel price adjustment in June with growth prospects being negatively affected by the ensuing deflationary effect on the economy

The monetary policy dilemma however became more intense by the middle of the year. The gap between domestic and international fuel prices widened to unprecedented levels as global oil prices reached historical highs. As the fiscal costs of fuel subsidies became unsustainable,

**Chart 3.1**
**Changing Outlook for Real GDP Growth in 2008 (Annual change, %)**




[1] Indonesia, Malaysia, Philippines, Thailand and Vietnam
[2] Newly Industrialised Economies

Source: IMF, WEO July, October and November 2008

**Chart 3.2**
**Contribution to Headline Inflation**

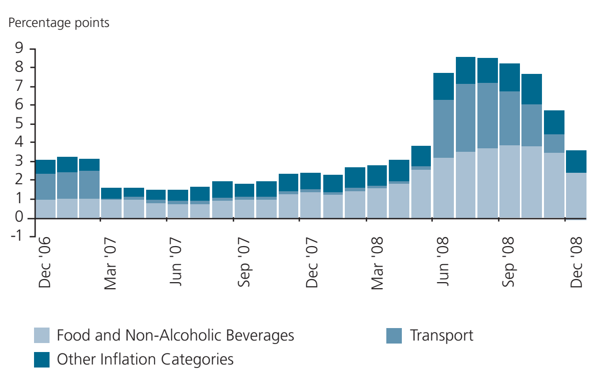
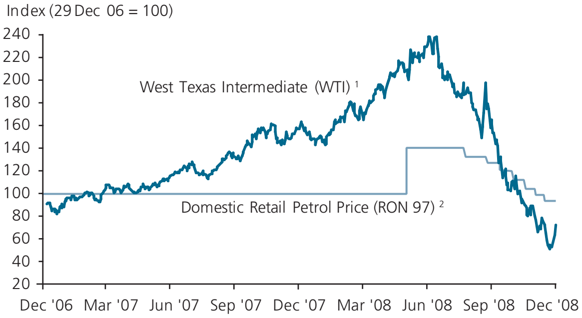


**Chart 3.3**
**Global Oil Prices and Domestic Retail Petrol Price (RON97)**




[1] Source: Bloomberg
[2] Source: Ministry of Domestic Trade and Consumer Affairs

the Government raised domestic fuel prices by up to 40.4% on 4 June, which was the largest adjustment since 1990. Headline inflation, which was already experiencing upward pressure from rising food and commodity prices, accelerated to 7.7% in June from 3.8% in May. Inflation increased further to 8.5% in July and August. The inflation forecast for 2008 was revised upwards to 5.5% – 6.0% at the July MPC meeting.

Given the magnitude of the increase in fuel prices, the first-round effects on the prices of goods and services were expected to be large. While there were limitations to what monetary policy could do under these circumstances, there was however the concern that this might fuel inflationary expectations. A monetary policy response might have been warranted had there been indications of wages increasing disproportionately or evidence of second-round effects on inflation. Evidence from monetary policy surveillance however indicated that the sharp increase in prices had eroded the purchasing power of consumers and had led to cutbacks in discretionary spending, which would in turn result in slower economic growth. Without evidence of a strong wage response, the high inflation would not be sustained. Surveys and industry consultations by the Bank showed that wage demands remained moderate. Monetary and credit conditions showed relatively moderate growth rates. It was also becoming more evident that the ongoing financial turmoil in the advanced economies had become more acute and had begun to negatively affect global economic activity, and thereby was expected to become a significant downside risk to the performance of Malaysia's external sector. Thus, notwithstanding the rise in inflation, the downside risks to growth had also become significantly elevated. In light of these considerations, the decision therefore was for monetary policy to remain unchanged.

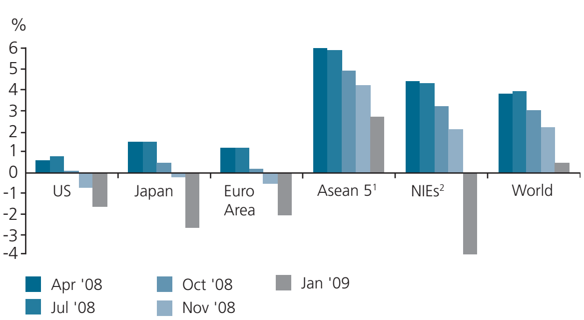
It was recognised that such a decision would be highly contentious given the evidence of high inflation. The combination of the spike in inflation and the then relatively imperceptible signs of slower global and domestic growth raised expectations for an increase in the OPR during this period. There were concerns that inflationary expectations would become unhinged, which would in turn complicate further the conduct of monetary policy. The decision to maintain the OPR at 3.5% created the perception that the monetary policy strategy undertaken by the Bank was 'behind the curve'. The Bank enhanced its communications to explain the issues to the public. Specifically, the Bank elucidated its views on the unfolding economic and financial developments and the consequential impact that these developments would have on the medium-term domestic growth and inflation trends. It explained that the surge in inflation would be temporary and that inflation would moderate in 2009. The Monetary Policy Statement (MPS) was further augmented by additional statements and communication sessions with the industry and the public (Note: Box Article on Monetary Policy Communication in Malaysia).

By the end of the third quarter, there were clear signs that the global market turmoil had become a full blown crisis that had spread to other markets, with a greater number of asset classes being affected and involving more countries. The global growth outlook deteriorated considerably. Headline inflation in many countries, including Malaysia, although remaining at elevated levels showed signs that it had peaked. Concerns over growth prospects began to take a higher precedence over inflation.

In spite of the greater volatility, weaker sentiments and heightened uncertainty, the Malaysian financial markets continued to function normally. Global deleveraging meant that the local equity and bond markets were affected by the offloading of ringgit assets by non-resident investors. The ringgit, along with other currencies in the Asia Pacific region experienced a weakening trend since the second quarter of the year, amidst outflows of funds from domestic markets as the deleveraging in the crisis-affected economies intensified. Nevertheless, the ringgit adjustment was orderly, and the money market also continued to function efficiently. A more significant challenge came from the spillover effects of the economic contraction occuring in the advanced economies, which was expected to have a significant impact on Malaysia's export sector. Domestic demand, while supportive of growth, was also moderating amidst the more cautious consumer sentiment, softening labour market conditions and a more challenging business environment. An increasing number of inflation indicators suggested a moderation of inflationary pressures in the economy. The Bank had left monetary policy unchanged at a level considered to be sufficiently low to support economic activity.

The severity of the global financial crisis in the fourth quarter however necessitated measures to avoid contagion to the domestic financial system. Hence, as a pre-emptive measure, the Ministry of Finance and the Bank jointly announced on 16 October 2008 a full guarantee of all ringgit and foreign currency deposits at commercial, Islamic and investment banks, as well as deposit-taking development financial institutions regulated by the Bank. The guarantee was provided by the Government through Perbadanan Insurans Deposit Malaysia (PIDM), which is the deposit insurance corporation, until December 2010. The guarantee is extended to all domestic and locally incorporated foreign banking institutions.

**Chart 3.4**
**Outlook for Real GDP Growth in 2009 (Annual change, %)**




[1] Indonesia, Malaysia, Philippines, Thailand and Vietnam
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Source: IMF, WEO April, July, October, November 2008 and January 2009

## The OPR was lowered as inflation moderated and growth prospects became significantly affected as the global financial turmoil turned into a widespread economic crisis

Global conditions deteriorated markedly and rapidly towards the end of the year, with global growth prospects worsening beyond what was earlier anticipated. Several major advanced economies were by then in a recession amidst continued severe stress in their financial systems. The sharp slowdown in global demand, the significant fall in commodity prices and the widespread contagion effect across financial markets exerted a greater downward pressure on the growth prospects of regional economies. The Malaysian economy was negatively impacted by these adverse developments, as reflected in the rapid slowdown in export performance and industrial production. Although domestic demand remained resilient, there were clear indications of slower private sector activity. The GDP growth forecast for 2008 was revised to 5.0% - 5.5%. For the year 2009, GDP growth was estimated by the Government to decelerate to 3.5%. As inflation pressures abated, the policy focus quickly turned to mitigating the severity of the domestic economic slowdown. The OPR was reduced by 25 basis points to 3.25% on 24 November 2008. To reduce the cost of intermediation, the Statutory Reserve Requirement (SRR) was reduced by 50 basis points to 3.5% with effect from 1 December 2008.

Apart from lowering the OPR, the policy focus was on ensuring that the monetary easing was transmitted to the economy. The worsening outlook had prompted several banking institutions to exercise greater caution in granting credit to their customers. To ensure adequate and ready access to credit, the Bank conducted dialogues with the banking institutions and businesses. There continued to be sufficient credit to support consumption and investment activity, as indicated by the continued increase in lending by banking instituitions. Depositors were however affected by lower returns. Nevertheless, real interest rates were expected to trend higher as inflation moderated. To support depositors who were particularly dependent on income from deposits, the Bank issued the Merdeka Savings Bond in March 2009 amounting to RM2 billion as an additional savings instrument.

As the year drew to a close, the global economic and financial conditions continued to deteriorate. There remained considerable uncertainty with regard to the severity and duration of the global downturn. A sustained economic recovery would require the financial sector's functionality to be restored. Authorities in the advanced and regional economies intensified their fiscal and financial sector resolution measures while recognising that these measures would take time to be fully effective. For Malaysia, the external position remains strong and the high external reserves allow for a greater cushion to offset capital outflows. In addition, inflationary expectations have become more subdued, while the deeper financial markets have facilitated financial adjustments to be taken in an orderly manner. The banking system is also operating with strong capital buffers that facilitate the intermediation process. Nevertheless, the severity of the global shocks calls for macroeconomic policies to support domestic demand until conditions in the global economy showed signs of normalisation.

## MONETARY OPERATIONS IN 2008

Conditions in the domestic money market were generally stable despite the heightened volatility in global financial markets. The Malaysian money market continued to operate under a surplus liquidity environment. Volatility in the domestic financial market was also contained by the Malaysian banks' significantly lower cross-border credit exposures and smaller derivatives and foreign-currency denominated business.

The first half of the year saw a steady growth of domestic liquidity. As an indicator of the surplus liquidity level, total domestic liquidity as at 30 June 2008 was RM408 billion, which was RM63 billion or 18.3% higher than the RM345 billion level as at end-December 2007. The increase in surplus liquidity was mainly accounted for by portfolio inflows driven primarily by expectations of an appreciation of the ringgit against the US dollar. Weakness in the US dollar globally arising from the sub-prime crisis in United States caused investors to seek alternative investment destinations, including ringgit assets, which prompted the expectations of an appreciating trend in the ringgit exchange rate.

The liquidity and exchange rate trends reversed in the second half of the year. Although liquidity conditions remained ample, the surplus liquidity in the domestic money market began to moderate due to portfolio outflows, driven by the weakening global economic conditions and the deleveraging by foreign financial institutions. Domestic liquidity declined to RM258 billion as at end-December 2008. Requirements for liquidity were met by the maturity of previous money market borrowing operations.

**Chart 3.5**
**Outstanding Liquidity Placed with Bank Negara Malaysia**

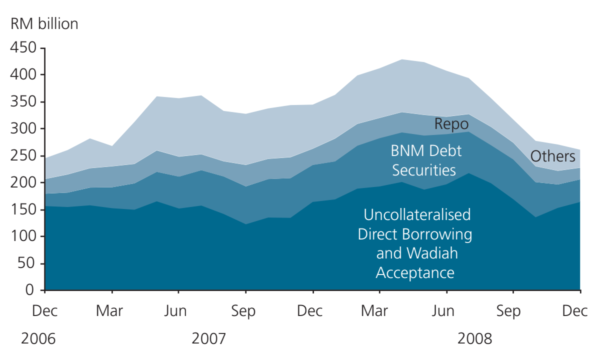
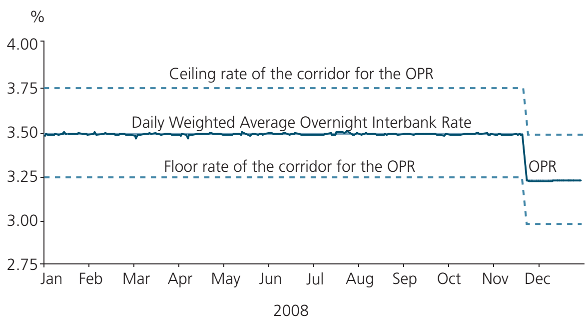


**Chart 3.6**
**Overnight Policy Rate (OPR) and Daily Weighted Average Overnight Interbank Rate**




Throughout the year, the Bank's discretionary money market operations continued to maintain liquidity conditions that ensured that the overnight interbank interest rate traded within the +/- 25 basis point corridor around the OPR. During the year, the average overnight interbank money market rate traded within the range of 3 basis points below and 1 basis point above the OPR. Apart from the overnight rate, the other longer-term interbank rates continued to be primarily market determined, reflecting overall demand and supply conditions as well as prevailing interest rate expectations in the financial markets.

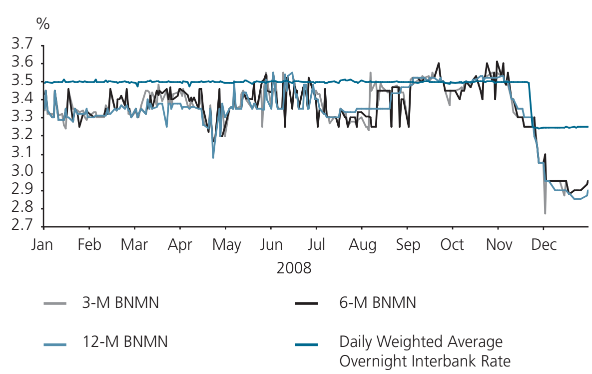
All interbank participants remained net lenders in the interbank money market throughout the year. For that reason, the Bank's standing facility was only utilised 14 times throughout the year, of which only two were for providing funds to facilitate short-term transitory liquidity shortages that were solely due to operational factors.

In terms of the types of monetary instruments, for the whole of 2008, uncollateralised direct borrowings and Wadiah acceptances continued to be relied upon as the primary instruments, accounting for 62% (uncollateralised direct borrowings at 47% and Wadiah acceptances at 15%) of surplus liquidity sterilised as at end-2008. Repurchase transaction (repo) operations, as well as net issuances of Bank Negara Monetary Notes (BNMNs) and the shariah compliant Bank Negara Monetary Notes-i (BNMN-i) accounted for 8% and 16% of total outstanding instruments, respectively.

During periods of strong portfolio inflows and to a lesser extent, trade-related inflows in the first half of the year, BNMNs were used aggressively as compared to uncollateralised direct borrowings and Wadiah acceptances to absorb surplus liquidity, as there was a strong investor preference for short-term debt securities, particularly amongst non-resident investors. With the strong demand, the issuance yields for BNMNs were 11 to 27 basis points lower than the OPR, hence providing a cost effective means of mopping up the surplus liquidity. Accordingly, non-resident holdings of BNMNs also increased to a high of 61% or RM56.7 billion as at end-April 2008. With the increasing amounts of surplus liquidity, the Bank also issued a total of RM2.5 billion 1-year floating rate BNMNs via four competitive variable-rate uniform price auctions, mainly to lock in the surplus liquidity for a longer period without undertaking corresponding longer-term interest rate risks.

During the second half of the year, longer-term interbank money market rates exhibited some volatility following market expectations for changes in monetary policy, firstly due to rising inflation in the middle of the year and subsequently, slowing economic conditions. The heightened uncertainties in the global financial system following the increased impairment

**Chart 3.7**
**3-month, 6-month, 12-month BNMNs and Daily Weighted Average Overnight Interbank Rate**



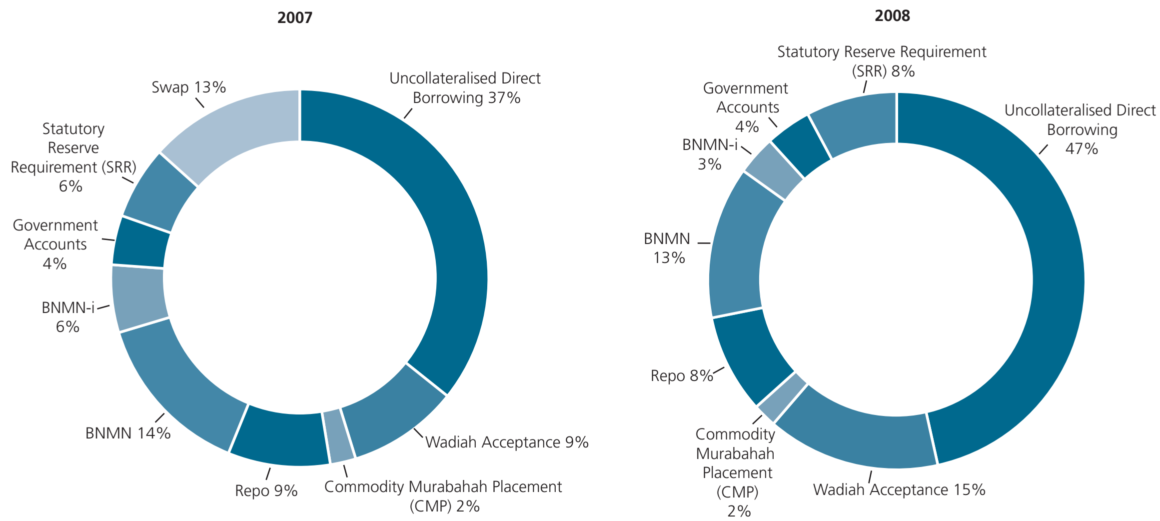
of financial institutions in the crisis-affected countries led to the deleveraging process that in turn resulted in reversals in portfolio flows.

Monetary operations were then focused on shortening the average maturity of sterilisation operations so that the daily maturity of previous operations would offset any potential liquidity outflows. The maturity term for uncollateralised borrowings was reduced from 2 months to mainly below 45 days, while the maturity terms for both BNMNs and BNMN-i were shortened from 6 months to an average of slightly below 3 months. The average maturity for all monetary instruments employed in the monetary policy implementation process declined from 39 days in April 2008 to 19 days by end-December 2008. The short maturity strategy and the subsequent maturity of previous operations in the second half of the year enabled the Malaysian domestic money market to be well-insulated against excessive volatility due to portfolio outflows. The capital outflows were sufficiently met by the unwinding and non-rollover of previous operations, without any liquidity stress that otherwise would have required liquidity injections by the Bank.

Repo transactions, where possible, were also used extensively, representing 8% of total surplus liquidity absorbed by the Bank. Funds-driven repo rates remained at a negative spread to unsecured interbank rates at approximately 25 basis points below interbank rates of equivalent maturities. This was due to the high demand for the underlying general collateral for short-term investment as well as compliance to prudential regulations. Lending of benchmark Malaysian Government Securities (MGS) through repo transactions was also in high demand. MGS benchmark securities were well sought after by banking institutions for market making purposes as well as for the short-covering of regulated short sales, which contributed to rates being consistently below the interbank borrowing rate of corresponding maturities by an average of 210 bps throughout the year.

Several developmental initiatives were implemented to increase operational efficiency. On 28 November 2008, the Bank introduced a competitive variable-rate multiple price auction process for commodity murabahah transactions, whereby participating Islamic financial institutions submitted profit-rate bids, which replaced a bilateral reverse inquiry process initially used for such transactions. This new development served as another mechanism for the price discovery process in Malaysian Islamic money market.

**Chart 3.8**
**Outstanding Monetary Policy Instruments**



In addition, on 5 November 2008, as part of pre-emptive measures to maintain stability of the financial system, the Bank made available its liquidity facility to insurance companies and takaful operators regulated and supervised by the Bank. Nevertheless, the facility was not utilised by any insurers or takaful operators as a significant portion of their assets were already in the form of liquid assets that were more than enough to meet their liquidity requirements should the need have arisen. Furthermore, the nature of the insurance business posed substantially lower liquidity risks compared to the banking system.

In conclusion, the Bank, through its monetary operations in 2008, was able to successfully manage liquidity as well as contain volatility in the domestic money market through the use of a diverse and effective set of monetary instruments. In addition, the Bank's operational flexibility will enable the effective management of the challenges arising from the continued volatility in global financial markets and capital flows.

## Core Inflation: Measurements and Evaluation

### Introduction

Inflation is generally defined as a persistent increase in the price of goods and services over a certain time period. High inflation and expectations about the future course of inflation influence the aggregate spending of households and firms in a way that leads to inefficient allocations of real and financial resources. Such an environment normally results in a sub-optimal growth potential. Hence, price stability, a situation where inflation is relatively low and stable and does not distort economic agents' spending and investment plans, is central to achieving sustainable economic growth. The importance of anchoring inflation expectations and lags in the monetary policy transmission process point to the need for Bank Negara Malaysia to ensure policies on inflation are forward looking. For this reason, in fulfilling its policy mandate to maintain price stability, the Bank looks at different measures and indicators of headline inflation and core inflation. This box article describes the concept of core inflation and discusses how it is being used by the Bank as part of its information set in assessing current and future inflationary trends.

### Rationale for Using Core Inflation Measures

In theory, movements in prices are the result of interactions between demand and supply conditions. However, factors that drive demand and supply conditions could differ. In particular, cyclical changes in demand conditions are generally persistent in nature. A change in the price level caused by a variation in demand conditions is most likely to remain for an extended period and represents a permanent change in the underlying inflation trend. By contrast, supply shocks, such as adverse weather conditions or disruptions to global oil production, are usually short-lived and often result in only a temporary deviation of inflation from its underlying trend.

Often, prices of goods and services are determined by the dynamic interaction between demand and supply conditions, which are at times hard to distinguish. An additional challenge to policy analysis is the fact that demand pressures are not directly observable. Measures of core inflation attempt to identify movements in prices that are actuated by demand shocks. To increase the degree of confidence, the Bank employs several methods to compute core inflation. These range from an exclusion-based method to one that is based on statistical techniques. All these methods seek to isolate the persistent component of inflation from transitory price movements. This allows for a better identification of the sources of price pressures.

### Measures of Core Inflation

An important measure of core inflation used by the Bank is based on the **exclusion method,** which permanently excludes from the CPI basket, items whose price fluctuations are considered transitory in nature and do not have a lasting impact on the underlying trend in inflation. These include price volatile items such as fresh vegetables and seafood, price administered goods and those that are affected by government price controls. The exclusion-based core inflation series is relatively easy to understand and frequently used by the Bank in assessing the direction of inflation.

While the exclusion-based measure is an important methodology used to estimate core inflation, this is supplemented by other measures such as the **trimmed mean** and **weighted median** methods. Both techniques are based on the distribution of price changes. They place greater emphasis on the general price movements. Small or zero weights are assigned to large price changes that are considered as outliers.

Another method employed by the Bank to estimate core inflation is using the **exponential smoothing technique.** This method derives core inflation by exponentially smoothening current and past aggregate price data. The **double weighted measure,** meanwhile, involves assigning lower weights to highly volatile CPI items and higher weights to items that are less volatile. Instead of removing volatile items, this method seeks to minimise their effects. Yet another alternative way to computing core inflation is by using the **Kalman Filter technique.** It involves extracting a common signal from movements in CPI component. Finally, core inflation could also be derived using **principal**

**Table 1**
**Measures of Core Inflation**

| Core Inflation Measures | Brief Descriptions | Advantages | Disadvantages |
|---|---|---|---|
| 1. Exclusion-based | • Exclude price-volatile energy and food items from the CPI basket<br>• Most commonly used measure among central banks | • Easy to construct and compute<br>• Easy to communicate | • Critics argued that the excluded items may also contain important signals about underlying inflation<br>• Excludes items that could represent a large share of the CPI basket (especially if food and energy account for a large share of CPI) |
| 2. Trimmed mean | • Items are arranged according to the magnitude of their price change during the month<br>• Trims an equal amount (15% for Malaysia) from each end of the distribution of price changes | • Easy to construct and compute | • The exact percentage that is excluded is still subject to debate |
| 3. Weighted median | • Items are arranged according to the magnitude of their price change during the month<br>• Core inflation is selected from the 50th percentile inflation rate at which half of the components in the CPI basket have higher inflation and the other half, less | • Easy to construct and compute<br>• Easy to communicate | • Item with large weights may dominate the median<br>• Median can sometimes differ significantly from the mean |
| 4. Principal component analysis | • Derives core inflation from the common price trends embedded in the various components of the CPI | • Uses disaggregated data from the CPI basket | • The technical nature of the technique reduces its usefulness in communications |
| 5. Exponential smoothing | • Exponential smoothening of current and past CPI data | • Remove seasonality from the data | • Works with some lags<br>• The technical nature of the technique reduces its usefulness in communications |
| 6. Double-weighted measure | • Assigns larger weights to less volatile items and lower weights to the more volatile items | • Easy to construct and understand | • May minimise important price signals from price volatile items |
| 7. Kalman Filter | • Extracts the common price signal that drives price movements in individual CPI components | • Optimal use of the disaggregated CPI data | • The technical nature of the technique reduces its usefulness in communications |

**component analysis** (PCA). Basically, this method identifies patterns in the CPI's main components and expresses them in a way that highlights their similarities.

Each measure of core inflation has its strengths and weaknesses in its success in isolating price changes that are driven by demand-related factors, as opposed to supply-related factors. Table 1 summarises these strengths and weaknesses for the various measures of core inflation.

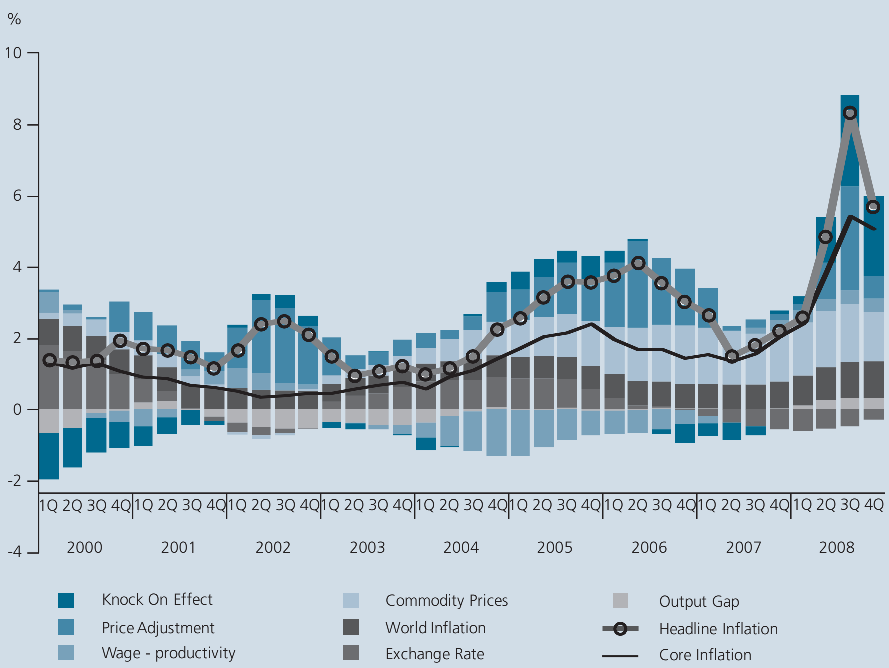
**Uses for Core Inflation**

From the policymaker's perspectives, core inflation provides important information not only about current inflation, but also about the future path of headline inflation. Therefore, core inflation analysis is a useful component of the information set used by the Monetary Policy Committee in setting the stance of monetary policy when balancing the risks to price stability and growth. The following two episodes of elevated headline inflation elucidate this point.

*February 2006 - March 2007*

During this period, headline inflation rose sharply, to average 3.4%, while average core inflation was only 2%. A disaggregation analysis of headline inflation (*see Chart 1*) reveals the increase was mainly the outcome of higher prices for fuel items in the *transport* category of the CPI, following the 30 sen per litre increase in retail fuel prices in February of 2006. The absence of second round effects and subdued core inflation implied that the increase in inflation was almost entirely due to the supply shock and was unlikely to be sustained beyond the near term. As shown in Chart 2, headline inflation did ease off as the supply-side effects began to wane in the second half of 2006.

**Chart 1**
**Disaggregation of factors contributing to Headline Inflation**

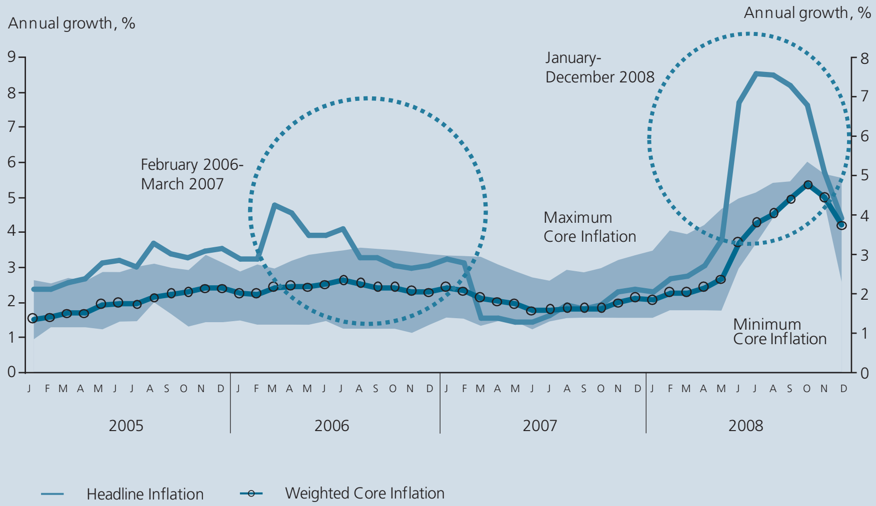



Note: The disaggregation of factors contributing to inflation is derived from an econometric model for exclusion based core inflation. Price adjustment refers to items excluded from core inflation.

*January 2008 – August 2008*

During this period, domestic prices, especially for food and energy, rose sharply in response to the higher global prices for crude oil and food commodities. To mitigate the impact of ballooning fuel subsidies on the Government's fiscal position, prices of domestic retail petroleum products were increased significantly in June 2008. While this led to a sharp increase in price administered items in the CPI basket, it also gave rise to a large "knock-on" effect through the supply-chain to other domestic goods and services (*see Chart 1*). Consequently, the underlying inflation rose sharply during the period. In that sense, the rise in core inflation was not reflective of demand pressures but rather the first-round transmission of the fuel price shock across a wide variety of goods and services throughout the economy. With the subsequent reversals of global commodity prices and the downward revisions in domestic retail petroleum products, core inflation began to moderate in the fourth quarter of 2008.

**Chart 2**
**Headline and Weighted Core Inflation**




Note: Weights are assigned to the weighted core inflation based on the relative measure of core inflation root mean squared error (RMSE) performance. This technique requires one to regress headline inflation on different core inflation measures at various time horizons. From each regression, one has to calculate the RMSE for the in-sample forecast of the model. The closer the value of the RMSE to 0, the higher weight is assigned to the respective core inflation measure.

## Conclusion

The various types of core inflation measures are useful components of the group of indicators used by the Bank to access the incipient risks to price stability. It must, however, be emphasised that no single indicator forms the basis of policy decision. As with all indicators, the interpretation of the core measures has to be within the overall context of the current and expected economic environment.

## Monetary Policy Communication in Malaysia

### The Importance of Communication in Conducting Monetary Policy

Central banks can perform their roles and fulfill their goals more effectively when their policy actions and decisions are better understood by the public and financial markets. This has resulted in growing emphasis by central banks around the world to provide greater transparency to the public by expanding the modes of communication and increasing the frequency, amount and quality of information shared with external stakeholders. In this regard, Bank Negara Malaysia has in the recent years published more information and provided more detailed explanations on the Bank's role, policy objectives, as well as the assessment and rationale underlying its monetary policy decisions.

One of the key reasons for the importance of monetary policy communication is the recognition of the need to effectively manage expectations. By managing expectations about the future course of economic activity and inflation, central banks can influence aggregate demand in the immediate future given the forward looking nature of economic agents. Importantly, expectations of future prices are a key factor in determining actual inflation. When people expect prices to rise rapidly in the future, they react by bringing forward purchases of goods and services, which lead to the increase in the prices for these goods and services, or demand higher wages, thereby creating the very inflation they had earlier expected. Communications on the Bank's commitment and strategies to ensure price stability is therefore important for promoting greater public understanding and confidence that long-term inflation would remain low, and hence encourage agents to react accordingly. While good communication is not a substitute for good policy making, central banks need to ensure good policy decisions are supported by strategic communication efforts, which are also reinforced by a track record of consistent policy decisions to ensure the predictability, credibility and effectiveness of monetary policy.

Clear communication is also important for the efficient transmission of monetary policy to the economy, for example through the interest rate channel. Under the New Interest Rate Framework adopted in April 2004, the Bank seeks to influence the overnight market interest rate to be at the desired level of the Overnight Policy Rate (OPR). Adjustments to the OPR alone may not be sufficient for monetary policy to be effective in influencing aggregate domestic demand given the long and variable lags between the time the policy rate is changed and when it actually affects spending and investment decisions by economic agents. Rather, it is important for the market to respond to the signals of the Bank's current and expected monetary policy stance through the OPR, and appropriately adjust the prices of relevant financial assets, which in turn affect spending and investment decisions by economic agents. In the money market, this involves adjustments to other maturities and instruments such as interest rate swaps that influence the cost of funds, which subsequently form the basis of the retail lending rates charged to bank borrowers. In the bond market, expectations of the future path of interest rates affect the cost of raising funds to firms. Effective communication therefore also facilitates a more rapid transmission of the policy rate into the pricing of credit and longer-term rates, thereby enhancing the overall efficiency of the monetary transmission mechanism.

Given the significant impact of policy actions by the central bank on the economy through its influence on aggregate domestic demand, central banks find it necessary to provide an explanation of their decisions and the rationale underlying these decisions. Greater transparency by central banks thus enables a more objective assessment of the central bank's performance by external stakeholders. Furthermore, public discourse on policy matters can lead to improvements in internal deliberations and promote the formulation of more effective policies. Through greater engagement, the Bank also aims to receive feedback from the industry, economic sectors, the market and the public, and provide an enhanced understanding of the central bank's reasoning, strategies and objectives.

There continues to be divergent views and differing practices on the appropriate degree of transparency and what constitutes an ``optimal˝ communication strategy. This can mainly be attributed to, among others, the differences in the decision-making structures, policy frameworks, as well as the institutional environment in which a central bank operates. For example, an inflation targeting central bank would tailor its monetary policy communication strategy with respect to an explicit numerical target for inflation. In the case of Bank Negara Malaysia, while price stability is a primary objective, promoting sustainable growth and financial stability are also important policy objectives. For a central bank with multiple mandates, the pursuit of monetary policy which is consistent with the other mandates places greater emphasis on elucidating the assessment on the balance of risks to both growth and inflation whenever a policy decision is made. By fostering a better understanding among its stakeholders on the Bank's assessments of economic and financial developments and the policy initiatives, effective communication facilitates the successful transmission and acceptance of the Bank's policies. Accordingly, the Bank employs several channels for its communication.

**Channels for Monetary Policy Communication**

The Monetary Policy Statement (MPS) is the main channel for monetary policy communication for the Bank. The MPS not only states the monetary policy decision, but also provides the Bank's assessment of the performance of the economy, inflation and the policy issues. The first MPS was issued on 27 August 2003 and was initially released only on a quarterly basis to coincide with the announcement of the GDP growth figures. Since 2006, the MPS is issued after each Monetary Policy Committee meeting. The publication of more regular and timely information on monetary policy decisions is part of the Bank's on-going initiative to enhance a greater understanding of the country's economic and financial conditions, and that has become a factor affecting the formation of market and public expectations. The Bank also releases in advance the schedule of MPC meetings for the following year[1]. The transparency of procedures and the clarity of monetary policy decisions to market participants have contributed towards facilitating orderly market adjustments following monetary policy announcements.

Bank Negara Malaysia also publishes regular reports that are readily available and widely disseminated to the public. In March each year, the Bank publishes its Annual Report. In addition to being an account of economic developments that took place during the previous year, the Annual Report includes the Bank's forecast for economic growth and inflation, as well as the monetary policy outlook, in order to provide the public with a comprehensive assessment on the balance of risks to economic growth and price stability for the year. The forecasts are subject to rigorous assessments within the Bank prior to publication, and are subsequently assessed regularly in light of new developments. Any revision to these forecasts will most likely be communicated either through the MPS or during the quarterly press conferences held in conjunction with the release of the quarterly GDP growth figures.

The Quarterly Bulletin provides a quarterly record of economic and financial developments, while the Monthly Statistical Bulletin provides timely and comprehensive statistics on the economy and financial system. To reduce the time lag of data releases and to increase the accessibility of information, the dissemination of these reports also takes place electronically through the Bank's website (URL: http://www.bnm.gov.my).

[1]The advance schedule is normally released in conjunction with the final MPS in the preceding year.

Other important communication channels include public comments by the Governor through media interviews and speeches at public forums, which are accessible on the Bank's website. Press conferences during the release of the Annual Report and Quarterly Bulletins, as well as briefings to investors, analysts and economists, are also key communication channels for the Bank to engage with the public and participants of the financial market. In addition, the Bank conducts regular meetings, briefings and consultations with financial market participants, industry and business associations in order to engage them on economic and financial issues and policies.

**Challenges in the Communication of Monetary Policy**

For it to be effective, the communication of monetary policy matters needs to strike a balance between comprehensiveness, relevance and timeliness. The fact that the monetary policy horizons extend to the medium term means central banks need to undertake an array of quantitative and qualitative analyses to form their assessment about the growth and inflation outlook as well as the risks involved. As with any prediction about the future, such assessments are often wrought with uncertainty, and hinge crucially on the underlying assumptions regarding a range of factors. For example, forecasting the global price of oil in 2007 and 2008 amid a rapidly changing global financial and economic environment was a highly challenging exercise. In such a volatile environment, it would be necessary to update the forecasts more frequently. It is also important to explain to the public that any inflation forecast is not a monetary policy target, but that it could potentially involve a change in monetary policy.

While monetary data and indicators are widely available and extensively analysed by market participants and analysts, it is nevertheless still important for the central bank to provide market participants with its perspective on the latest developments. In some circumstances, such communication would confirm market beliefs, while at others, the central banks' perspective provides market participants with further assessments of the more recent developments.

The communication challenges clearly manifested themselves in the volatile environment during 2007 and 2008, evidenced by the keen debates on whether monetary policy in Malaysia ought to be tightened in response to high and rising inflation. On both occasions, the Bank explained in great length its rationale for not raising the OPR, which was contrary to the expectations of several market participants. Specifically, in the first half of 2008, the upward inflationary pressures on global economies, including Malaysia, were caused by supply-driven factors, namely the higher global food and commodity prices. In communicating the decision for the Bank's monetary policy stance to remain unchanged, emphasis was placed on explaining the diagnosis of the situation and why a monetary response was not required. It was explained that, first, as a demand management tool, the role of monetary policy in a supply-driven shock was fairly limited. Secondly, the assessment was for the pressure on inflation to be temporary since the factors that could create second-round effects of price increases were absent or weak. Third, the Bank highlighted the high possibility of an oncoming weakness of the economy that would exert a moderating impact on inflation going forward. Although the prognosis turned out to be correct, for several weeks, policy communication faced considerable challenges. It was only when actual signs of weakness in the global and domestic economies began to appear that there was a convergence of market views with that of the Bank.

Communication on monetary policy decisions and related issues is an on-going challenge. Effective central bank communication, nevertheless, would remain an integral part of the Bank's role in conducting monetary policy. Going forward, the Bank will continue its focus on improving its channels of communication, and on enhancing the availability of relevant information on the monetary policy decision-making process and outcomes.

# Outlook and Policy

# Outlook and Policy

**INTERNATIONAL ECONOMIC OUTLOOK IN 2009**

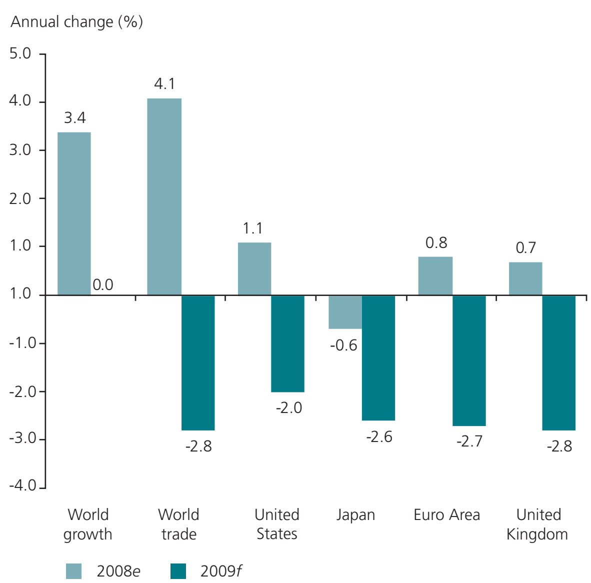
The global economy is not expected to record any growth in 2009, with a large number of economies experiencing a synchronised recession. Global financial markets will remain under stress in 2009 in spite of the extensive measures that have been unveiled, reflecting the ongoing need to repair and restructure the severely damaged balance sheets of a large number of systemically important financial institutions in several advanced economies. The weakened financial position of the financial sector in these economies is also expected to be further undermined as the deterioration in economic activities contributes to further writedowns and losses and dilution in the capital base of the financial institutions. The expected losses of US-originated credit assets held by banks and other financial institutions could increase to USD2.2 trillion[1]. Financial intermediation and confidence in the advanced economies are expected to take some time to normalise. Spreads in the funding markets are expected to remain elevated with lending standards remaining relatively tight. Market conditions in the international financial system will likely to remain challenging and are expected to stabilise when the announced policy measures are effectively implemented to restore confidence in the financial sector.

## The global economy is not expected to record any growth in 2009 with a large number of economies experiencing a synchronised recession

The recession in the advanced economies is expected to be protracted. Alongside the continued impact of the credit crunch on domestic demand, private consumption will also face pressures from job losses and declining asset prices, while private investment will be constrained by the significantly weaker demand and higher unutilised capacity. These developments in the advanced economies will adversely affect the growth of the Asian regional economies given the contraction in trade and investment flows. The newly industrialised Asian economies (NIEs) as well as the ASEAN economies are expected to record anaemic to no growth, while PR China is expected to record sub-par growth due to the weaker exports and investment outlook.

In the **US**, the prospect is for further declines in real economic activity. Private consumption is expected to remain depressed in view of the persistent weaknesses in both the labour and housing markets. Since 2008, job losses in the US have increased to 4.4 million, while households have experienced wealth destruction of more than USD11.2 trillion due to the sharp declines in house and equity prices. This will require adjustments in household consumption which was significantly financed by accumulation of debt over several years, thereby accelerating the deleveraging trend that has taken place since 2008. In addition, the decline in investment is expected to be more broad-based, extending beyond residential

**Chart 4.1**
**World Growth, World Trade and Growth in Major Advanced Economies (2008-2009)**




*e* Estimate
*f* Forecast

Source: International Monetary Fund and National Authorities

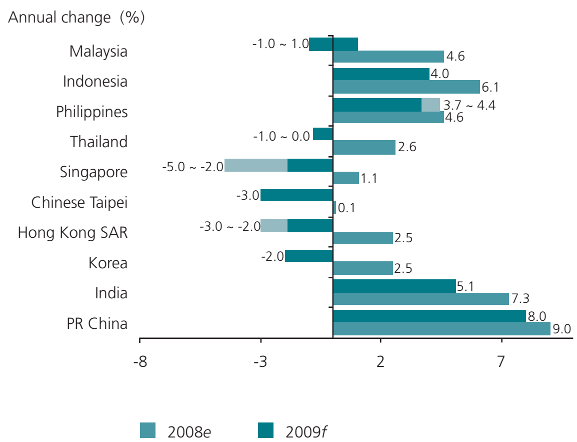
[1] IMF World Economic Outlook Update, January 2009

investment to non-residential investment following the depressed demand outlook, falling industrial production and rising inventory levels. The aggressive monetary and quantitative easing together with the USD787 billion fiscal stimulus package are, however, expected to provide support to the economy. A key policy priority is the successful implementation of the measures to resolve the financial sector problems, which is necessary to support the resumption in growth of economic activity.

The recession in the **euro area** is expected to deepen due to a combination of the housing slump in several economies such as Spain, Ireland, Denmark and Netherlands, as well as the impact of the financial turmoil in the region. The largest euro area economy, Germany, is undergoing an export-led recession, leading to a sharp fall in intra-regional trade that would also have an impact on domestic demand in the other euro area economies. The credit crunch in Europe is also expected to intensify due to the exposure of the Western European banks to the Central and Eastern European economies, which are affected by the current international financial turmoil. Meanwhile, in the **UK**, there are further signs of a deepening contraction in the economy due to the persistent credit crunch amidst the housing recession. **Japan**, being a more export-dependent economy, is expected to face further deterioration in its export sector and investment activities, which will prolong the recession that started in the second half of 2008.

With the advanced economies expected to experience a prolonged recession, **global trade** is expected to contract further during the year. This contraction is expected to have repercussions on the emerging economies with greater trade openness. The decline in global trade will also be accompanied by a decline in global foreign direct investment, as multinational companies scale down their investments amidst increasing capacity while global financial institutions cut back on financing.
As a region that is highly integrated with the global economy, the **Asian economies** will experience significant downside risks to growth in 2009. This will arise from the sharp contraction in external demand, low commodity prices and reduction in FDI inflows. These influences will, in turn, affect domestic private sector demand. Indicators show that domestic

**Chart 4.2**
**Regional Economies: Real GDP Growth**




*e* Estimate
*f* Forecast
Source: International Monetary Fund and National Authorities

demand has begun to moderate sharply since late 2008 due to weaker private sector sentiments, rising unemployment and large declines in production. The NIEs are anticipated to remain in recession in 2009, while the other regional economies are expected to face a sharp moderation in growth in 2009. The countercyclical fiscal measures that have been introduced by most economies in the region would also provide some support to growth in 2009. PR China is expected to register a lower growth, with support to growth coming from the implementation of the large fiscal stimulus of 13% of GDP over a two-year period.

**Global inflation** is expected to decelerate further in 2009 due to sluggish real economic activity and the sharp declines in commodity prices. Oil prices are expected to remain subdued as the decline in global demand is likely to outweigh the cuts in production initiated by the Organisation of Petroleum Exporting Countries (OPEC). Similar trends are expected to be observed in other commodities, including agriculture and base metals, reflecting the broad-based decline in global demand. The reversal of the trend in commodity prices and the significantly weaker demand conditions is expected to exert large deflationary pressures on headline inflation in most economies, with the possibility of deflation surfacing in some economies. Headline inflation in advanced economies is expected to decline to a record low of 0.3% in 2009. Meanwhile, inflation in emerging and developing economies is expected to moderate to 5.8% in 2009 from 9.2% in 2008[2]. Against this backdrop, monetary policy actions are expected to remain expansionary with additional quantitative easing in some cases, to address sector-specific issues in the financial markets.

Several **downside risks** remain on the global and regional outlook. The recession in the advanced economies could be prolonged by longer-than-expected structural adjustments in the household sector, particularly in the US, as households increase savings and reduce their overleveraged position. The financial sector resolution could also take longer than expected to be implemented effectively. In addition, support for the economy depends critically on the effectiveness of fiscal spending. The effectiveness of a combination of fiscal and monetary policy responses and large-scale global coordination in restoring the functioning of the financial system and markets are critical factors in determining the timing of economic stability in the respective economies. While the risks to the growth outlook in the advanced economies would have significant implications on the Asian regional economies, the region as a whole entered the current downturn from a position of strength, in terms of strong fundamentals and sound macroeconomic policies. This would, therefore, allow for greater policy flexibility in managing these downside risks. Moreover, the countercyclical measures that are being undertaken will also provide support to the real economy during this period of uncertainty.

## MALAYSIAN ECONOMY IN 2009

Global economic and financial conditions, which deteriorated sharply in the fourth quarter of 2008, are expected to weaken further in 2009. Being a highly open economy, Malaysia has already been impacted by the adverse global environment with exports and industrial production declining, in particular, steeply since December 2008. The rapid deterioration in external demand also dampened private investment and consumption and has led to weaker labour market conditions, which contributed to the significant moderation in domestic demand in the fourth quarter of 2008. The Malaysian economy is expected to experience the full impact of the global downturn in 2009.

**Taking into account the prospect for a deepening global downturn and the support to the economy provided by the policy measures, real GDP performance in 2009 is projected to be between -1% to 1%**

In response, several policy measures have been put in place with a primary focus on supporting domestic demand, as well as mitigating the impact of the global slowdown on the affected segments of the economy. On 4 November 2008, the Government announced the first economic stimulus package amounting to RM7 billion. The funds would be allocated to projects which have a high and immediate multiplier impact on the economy. In addition, several measures to directly support private consumption were also introduced, such as a reduction of EPF contributions from 11% to 8% and higher vehicle loan eligibility for civil servants. As the global economic conditions deteriorated further in the fourth quarter of 2008 and in the early part of 2009, a second economic stimulus package of RM60 billion or almost 9% of GDP was announced on 10 March 2009. The package will be implemented over 2009 and 2010, and will involve spending on training, job creation, improving public infrastructure, school facilities and basic amenities, as well as establishing guarantee facilities.

Meanwhile, with the risk of inflation receding rapidly, the easing of the monetary policy has been front-loaded and directed towards supporting domestic economic activity by reducing the cost of intermediation. Bank Negara Malaysia has reduced the Overnight Policy Rate (OPR) by 150 basis points since November 2008 to 2.0%, while the Statutory Reserve Requirement

[2] IMF World Economic Outlook Update, January 2009

(SRR) has been reduced by 300 basis points to 1.0%. In addition, several measures have also been introduced to ensure continued access to credit as well as to minimise the impact of the economic downturn on specific affected groups. These include the setting up of four new financing facilities to facilitate access to financing by the small and medium enterprises and micro enterprises as well as measures by the financial institutions to lessen the burden on the affected groups through loan restructuring. Under the second economic stimulus package, two loan guarantee facilities, namely the Working Capital Guarantee Scheme and Industry Restructuring Loan Guarantee Scheme were established, to provide working capital and to encourage investment by businesses respectively. In addition, the Financial Guarantee Institution will also be established to provide credit enhancement to companies that raise funds from the bond market.

Taking into account the expectation of a deepening global downturn as well as the support provided by the policy measures, real GDP performance in 2009 is projected to be between -1% to 1%. Domestic demand is expected to provide the main support to the economy and is projected to record a positive growth, with public sector expenditure and private consumption as the main anchors. Public sector expenditure is projected to increase substantially following the implementation of the Government's stimulus measures, thus providing major support to the overall economic growth in 2009. The policy responses will provide important support to household consumption given the anticipated weakness in the labour market and relatively lower commodity prices. Private investment is expected to slow in an environment of a more broad-based slowing of economic growth.

On the supply side, sectors that are directly exposed to the external demand will be significantly affected in 2009. Output in the manufacturing sector is expected to decline due to the contraction in the export-oriented industries as well as weaker support from the domestic-oriented industries. The services sector is expected to still contribute positively to growth with continued expansion, albeit moderately, given the weaker performance in the trade-related industries. The agriculture and mining sectors will register negative growth due mainly to lower production of palm oil, rubber, and crude oil, in part discouraged by lower prices. Meanwhile, the construction sector is expected to record a stronger growth, benefiting from the implementation of projects under the two economic stimulus packages.

Labour market conditions are expected to weaken further, with the unemployment rate projected to increase to 4.5% in 2009. Businesses that are affected by the sharp deterioration in external demand are likely to continue to implement cost-cutting measures, including temporary layoffs and retrenchments. While employment in the public sector is expected to increase in 2009, this will not be able to fully offset the weak employment prospects in the private sector.

Headline inflation is expected to average between 1.5 – 2% in 2009. This reflects the sharp reversal of global commodity prices from their peaks in 2008 and slowing global inflation. The impact of downward adjustments to administered prices by the Government and the expected slowdown of domestic economic activity will also dampen price pressures.

On the external front, the current account surplus is projected to moderate, but remain sizeable at 11.5% of GNI in 2009. Although gross exports are expected to contract substantially due to the significant weakness in external demand and lower commodity prices, the trade surplus will remain sizeable as export contraction will largely be offset by import compression. The services account is expected to record a deficit in 2009 due to the moderation in the travel account. On the financial account, gross inflows of foreign direct investment are anticipated to continue to moderate in 2009, as multinational corporations postpone their investment plans until clearer signs of a recovery in demand emerged.

The projected economic performance of -1% to 1% for Malaysia in 2009 is based on the weaker global conditions expected during the year, that will be partially offset by the implementation of policy measures to support domestic demand. The timely implementation of the economic stimulus is, therefore, critical in ensuring that the outcome will be at the higher end of the projected range. There remains, however, significant uncertainties regarding the

## Potential Output of the Malaysian Economy

Potential output is the level of output that is consistent with the aggregate productive capacity of the economy. It provides an indication of the sustainable pace of economic growth, given the available productive inputs. The growth in potential output is determined by the expansion and non-inflationary utilisation of physical capital and labour, as well as growth of total factor productivity (TFP), which captures productivity gains from improvements in factor inputs as well as overall economic efficiency.

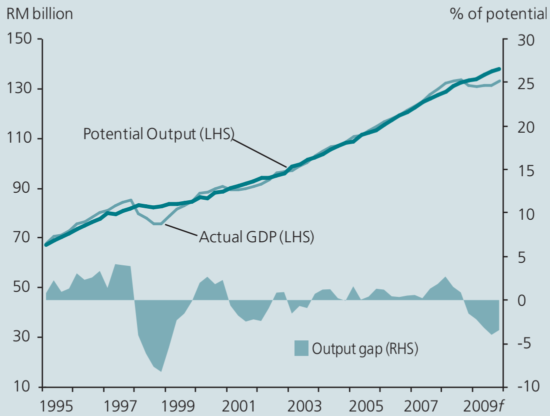
The latest estimate indicates that the potential output of the Malaysian economy was close to 5.1% in 2008, with the output gap[1] of positive 0.5% of potential output. The small positive output gap suggests that the Malaysian economy was performing close to its potential with minimal demand-driven inflationary pressure. Overall, since the year 2000, the Malaysian economy has been experiencing this trend of relatively balanced growth as shown by the output gap, which was on average less than ±1% of potential output.

**Table 1**
**Actual GDP and Potential Output**

| Period | Actual GDP | Potential Output | Investment | Labour | Output Gap |
|---|---|---|---|---|---|
| | Annual change (%) | | | | (% of potential output) |
| 1993-1999 | 6.5 | 6.6 | 4.3 | 3.2 | 0.0 |
| 2000 | 8.9 | 4.0 | 26.0 | 4.3 | 2.2 |
| 2001 | 0.5 | 4.6 | -2.1 | 1.6 | -1.8 |
| 2002 | 5.3 | 3.9 | 0.6 | 3.5 | -0.4 |
| 2003 | 5.8 | 6.0 | 2.8 | 3.6 | -0.6 |
| 2004 | 6.8 | 5.5 | 3.6 | 4.0 | 0.6 |
| 2005 | 5.3 | 5.1 | 5.0 | 4.1 | 0.8 |
| 2006 | 5.8 | 6.0 | 7.9 | 2.2 | 0.6 |
| 2007 | 6.3 | 6.0 | 9.6 | 2.0 | 0.9 |
| 2008e | 4.6 | 5.1 | 1.1 | 1.2 | 0.5 |

e Estimate

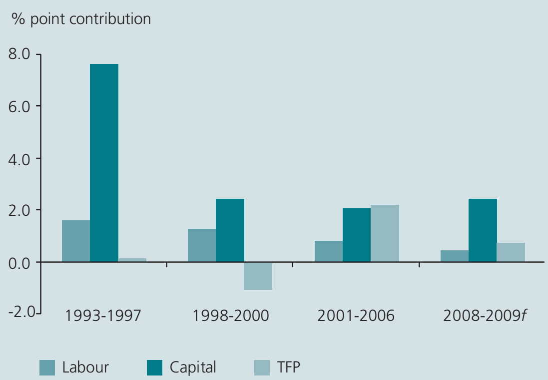
**Chart 1**
**Actual and Potential GDP**




*f* Forecast

As a small open economy, Malaysia is being affected by the severe global financial and economic crisis. Under this environment, potential output is therefore projected to moderate in 2009 due to an expected decline in overall productivity (TFP) and labour force participation as well as stagnation in capital stock growth, consistent with the experience during previous periods of slowdown. However, the output gap is projected to be negative in 2009 given the larger expected moderation of actual output.

**Chart 2**
**Factor contributions and TFP growth**




*f* Forecast

[1] The output gap is the difference between the levels of actual and potential output and the gap is measured as a percentage of potential output. A positive output gap indicates that actual output is above potential output, while a negative output gap indicates the reverse.

global economic outlook. First, the turmoil in the international financial markets may be more protracted and extend beyond this year, with problems in the financial sectors in a number of countries remaining unresolved, thereby further exerting downward contractionary influence on the global economy. Second, the large stimulus measures that are being implemented by several countries would take some time to take effect. Thirdly, there is the risk of trade and financial protectionism. These factors will influence the depth and length of the recession in the advanced economies and the overall direction of the global economy. Nevertheless, the strengths of the Malaysian economy, in terms of a strong banking sector, a healthy external position, high savings as well as relatively low indebtedness among individuals, businesses and the Government, provide flexibility for the economy to better weather this challenging period and recover once the global economic and financial conditions stabilised.

**Table 4.1**
**Real GDP by Expenditure (2000=100)**

| | 2008*p* | 2009*f* | 2008*p* | 2009*f* |
|---|---|---|---|---|
| | Annual change (%) | | Contribution to real GDP growth (percentage point) | |
| **Domestic Demand[1]** | **6.9** | **2.9** | **6.0** | **2.6** |
| Private sector expenditure | 7.1 | -0.3 | 4.4 | -0.2 |
| Consumption | 8.4 | 3.5 | 4.3 | 1.8 |
| Investment | 1.5 | -17.7 | 0.2 | -2.0 |
| Public sector expenditure | 6.5 | 11.4 | 1.6 | 2.8 |
| Consumption | 11.6 | 7.3 | 1.5 | 1.0 |
| Investment | 0.7 | 16.6 | 0.1 | 1.8 |
| **Change in stocks** | | | **-0.8** | **1.4** |
| **Net exports of goods and services** | **-3.8** | **-29.7** | **-0.5** | **-4.0** |
| Exports | 1.5 | -16.6 | 1.8 | -19.7 |
| Imports | 2.2 | -14.9 | 2.4 | -15.7 |
| **Real Gross Domestic Product (GDP)** | **4.6** | **-1.0~1.0** | **4.6** | **-1.0~1.0** |

Note: Figures may not necessarily add up due to rounding
[1] Excluding stocks
*p* Preliminary
*f* Forecast
Source: Department of Statistics, Malaysia and Bank Negara Malaysia

### Domestic Demand Conditions

Domestic demand is projected to experience a moderate growth of 2.9% in 2009, reflecting mainly the adverse spill over effects of the deepening global downturn on private sector activity. Household consumption is projected to moderate while capital spending by businesses is expected to contract further during the year.

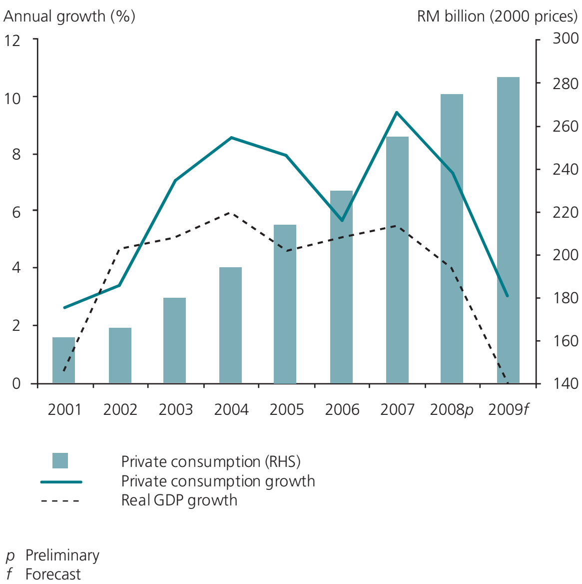
## Domestic demand to moderate in 2009 as a deeper global downturn affects household consumption and business spending. The public sector will be the main impetus of domestic demand

Nevertheless, domestic demand will be supported by higher Government spending. The public sector will be the main impetus of domestic demand, in particular following the implementation of two economic stimulus packages in 2009. With the prospect of inflation receding significantly, a substantial easing of monetary policy is aimed at supporting domestic economic activities. In addition, the domestic financial system has the capacity to continue to meet the financing needs of both households and businesses.

Growth in **private consumption** expenditure is expected to moderate but register a positive growth of 3.5% in 2009. The slower expansion in consumer spending will be affected largely by the weaker domestic labour market conditions with higher retrenchments and less favourable employment prospects. Labour demand in various sectors is envisaged to be weaker, with decline in the manufacturing sector being a major cause for the weaknesses. In view of this, the average increase in private sector salary is expected to moderate to 2.7% while the unemployment rate is projected to increase to 4.5% of the labour force. At the same time, affected companies have embarked on cost-cutting measures, including salary reductions, shorter work-week, unpaid leave and temporary layoffs. In addition, significant declines in commodity prices since the fourth quarter of 2008 have substantially affected incomes of smallholders.

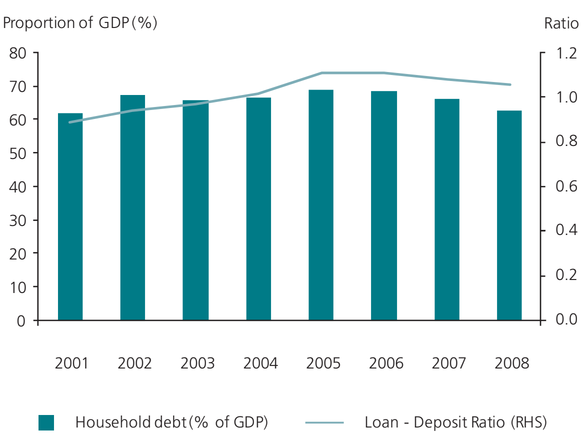
While consumer confidence is affected by the weakening trend in employment and economic

**Chart 4.3**
**Real GDP and Private Consumption**




activity, policy responses, including the substantial easing of monetary policy and the continued access to credit, will provide some support to private consumption. In addition, several measures in the economic stimulus packages are expected to lessen the impact of the economic slowdown on the households. These include the reduction of EPF contributions from 11% to 8%, an increase in vehicle loan eligibility for civil servants, and several measures to increase employment and training

**Chart 4.4**
**Household Debt Indicators**




opportunities contained in the second economic stimulus package.

**Private investment** is projected to decline by 17.7% in 2009 as capital spending activities will be affected by falling demand and negative business sentiments due to the worsening global economic conditions. While this trend of declining private investment has taken place in the fourth quarter of 2008, the impact of the slower economic growth is expected to be more widespread, affecting most economic sectors in 2009. Investment activities in the manufacturing sector will experience the largest decline, as external demand contracts further and domestic demand moderates. Although a high level of total investment was approved in the manufacturing sector in 2008, firms are expected to postpone some investment plans until there are clearer signs of recovery in demand. Furthermore, capacity utilisation rates are expected to fall during the year, which will discourage further capacity expansion.

In the services sector, consumer-oriented business segments such as transportation and communications are expected to continue to undertake investments, mainly to improve the provision of services. Businesses in the wholesale and retail trade sub-sector are also expected to expand their operations, though more selectively and at strategically located new outlets. In the mining sector, capital spending will moderate and be channelled towards maintaining existing production facilities and exploration activities in view of long-term commitment to ensure sustainable reserves. In addition, capital expenditure in the construction sector will benefit from the implementation of projects identified in the stimulus packages as well as the Ninth Malaysia Plan (9MP).

**Public consumption** is expected to increase by 7.3% in 2009, due mainly to higher expenditures on emoluments and supplies and services. Of importance, the higher allocation for supplies and services is to ensure the effective delivery of Government services to support the private sector and cushion the impact of the external downturn on affected segments.

**Public investment** is expected to increase strongly in 2009, as the Government implements counter-cyclical measures to mitigate the impact of the externally-induced slowdown on the economy. Federal Government spending will be higher, mainly channelled towards improving the economic and social sectors of the economy. In addition to projects under the 9MP, the Government is expected to accelerate the implementation of various projects identified in the two stimulus packages. In the social services sector, a major part of the allocation will be utilised to improve the Government's provision of essential services such as education and health, the development of infrastructure in the rural areas and the building of affordable houses. Capital spending by the non-financial public enterprises (NFPEs) is expected to moderate due to slower economic activity. This will be reflected in the slower capacity expansion in the oil and gas as well as utilities sub-sectors. Investments by the NFPEs in the communications and utility sub-sectors will focus on enhancing broadband network and improving power supply respectively.

### Sectoral Outlook

On the supply side, the year 2009 will be a challenging year for most sectors in the economy, particularly industries directly exposed to the external demand. The contraction in global demand is expected to continue to adversely affect the manufacturing sector as well as trade- and tourism-related industries in the services sector. In addition, the spillover of weaknesses in external demand and the generally cautious economic environment will lead to moderating private sector activities in domestic dependent sectors, in line with the slower pace of growth in domestic demand. Nonetheless, the domestic-oriented sectors will be partially supported by expansionary fiscal and accommodative monetary policies. In particular, the construction sector is expected to benefit from higher Government spending and register stronger growth in 2009.

## The year 2009 will be challenging for most sectors in the economy, particularly industries directly exposed to the external demand

Amidst slower overall economic activity, growth in the **services** sector is expected to moderate to 4.5% in 2009. However, as the sector is more domestically driven, the slower but continued growth in domestic demand, together with supportive fiscal and monetary policies, will provide some support against the weaker performance of trade- and tourism-related activities that are expected to prevail in 2009. As a whole, the services sector will remain the key growth sector of the economy in 2009, contributing 2.5 percentage points to the overall GDP growth.

The **finance and insurance** sub-sector will continue to grow in 2009, albeit at a slower pace. In line with slower private sector activity, both lending activity and the insurance business are expected to moderate. Fee-based income is also expected to reflect the subdued activity in the capital markets. The lower demand for financing will, however, be partially offset by an accommodative monetary environment and new measures introduced by the Government and Bank Negara Malaysia to enhance access to financing for viable businesses, such as the RM2 billion SME Assistance Guarantee Scheme, the RM5 billion Working Capital Guarantee Scheme and the RM5 billion Industry Restructuring Loan Guarantee Scheme.

**Table 4.2**
**Real GDP by Sector (2000=100)**

| | 2008*p* | 2009*f* |
|---|---|---|
| | Annual change (%) | |
| Agriculture | 3.8 | -2.0 |
| Mining & quarrying | -0.8 | -0.4 |
| Manufacturing | 1.3 | -8.0 |
| Construction | 2.1 | 3.0 |
| Services | 7.3 | 4.5 |
| **Real Gross Domestic Product (GDP)** | **4.6** | **-1.0~1.0** |

*p* Preliminary
*f* Forecast

Source: Department of Statistics, Malaysia
Bank Negara Malaysia

Meanwhile, growth in the sub-sectors that are largely dependent on domestic consumption, such as wholesale and retail trade, and communications sub-sectors, will be sustained at a more moderate pace. The **wholesale and retail trade**, and **accommodation and restaurant** sub-sectors are projected to grow at lower rates compared to 2008. Growth in both sub-sectors will continue to be supported by domestic demand, amidst easing inflationary pressures. Nevertheless, the projected decline in new motor vehicle sales will have a negative impact on the automotive segment of the wholesale and retail trade sub-sector, despite some support from the Government's auto-scrapping scheme. Furthermore, consumers are expected to be cautious in their spending due to the uncertainty in the economic environment, while the expected decline in tourist arrivals will also have some impact on both sub-sectors. The **communication** sub-sector is expected to continue to register favourable growth in 2009, supported by sustained demand for mobile communication and broadband services. In particular, expansion of broadband coverage following further investment in the high speed broadband project and WiMax services will provide impetus for growth in the sub-sector.

Moderation in growth is expected to be more pronounced in trade- and business-related services due to the weakening external demand. Growth in the **transport and storage** sub-sector is expected to slow, as the anticipated lower trade and manufacturing activity will adversely affect demand for shipping and other cargo-related transportation services. Similarly, the passenger segment is expected to be affected by lower global demand for air travel. However, the impact will be cushioned by the extensive promotion of low air fares and the implementation of the ASEAN Open Skies Policy on 1 January 2009. Meanwhile, growth in the **utilities** sub-sector will be affected by the moderation in demand for electricity, particularly from the industrial sector.

The **manufacturing** sector is projected to decline sharply in 2009 (-8%; 2008: 1.3%), to be led by steep contractions in export-oriented industries and weaker support from domestic-oriented industries. In particular, the E&E industry is expected to be the worst affected by the sharp deterioration in global conditions affecting the final demand for all E&E products. Similarly, weak external demand and declining commodity prices will affect the performance of the primary commodities related industries. Nonetheless, demand for hygiene and medical rubber gloves will continue to provide support to the rubber industry. The consumer-related industry is expected to grow at a slower pace due to the expected decline in demand for motor vehicles which will affect the manufacturing of transport equipment. However, performance in this industry will be supported by sustained growth in the food and beverages industries given moderate but continued growth in domestic demand. Construction-related industries are expected to move in tandem with the broad construction sector and resume a more favourable growth path in the second half of the year as the economic stimulus measures take effect.

The **agriculture** sector is expected to register a decline of 2.0%, due mainly to lower production of both palm oil and rubber as the expected lower prices of both commodities will reduce the incentive for marginal producers to maintain the output growth trend seen in recent years. However, this decline will be partially mitigated by positive growth in the food crops sub-sector, particularly livestock, fisheries and vegetables.

The **mining** sector is projected to decline marginally by 0.4%, as the decline of 2.2% in crude oil output to 675,000 barrels per day will be offset to some extent by a 2.9% increase in natural gas output due to LNG demand from a new buyer, PR China, which is expected to commence in the second half of 2009.

The **construction** sector is expected to expand by 3% in 2009, supported by the civil engineering segment due to the implementation of projects under the two economic stimulus packages. Meanwhile the residential sub-sector is expected to moderate as weakening consumer sentiments lead developers to reduce launches of new housing developments, thereby keeping the overhang at manageable levels. Nevertheless, the measure to provide tax relief on interest paid for housing loans will provide some support to demand for houses.

**Balance of Payments**

On the external front, the deepening of the global economic downturn and persistent uncertainty in the international financial markets are expected to continue to impact trade and capital flows in 2009. In tandem with the significantly weaker external demand and lower commodity prices, gross exports are expected to decline substantially. Nevertheless, the trade surplus is projected to remain sizeable as export contraction would largely be offset by import compression. The weaker export and slower domestic economic activity are expected to significantly reduce imports of intermediate goods as well as imports of capital and consumption goods. Meanwhile, the services, income and current transfers accounts are expected to record deficits. Taking all these into consideration, **the current account surplus** is thus projected to moderate but remain sizeable at RM80 billion or 11.5% of GNI in 2009.

Meanwhile, capital flows will remain subdued reflecting the weaker external environment.

**Gross exports** are expected to decline sharply by 25.3% in 2009, as exports will be simultaneously affected by the manufacturing and commodity downturns. The contraction in manufactured exports is projected to be most pronounced in the E&E industry, due to the combined effects of declining global demand as well as falling prices. Meanwhile, the decline in the value of primary commodities and resource-based manufactured exports reflects largely the price effect, arising from the large corrections in commodity prices already seen in the second half of 2008, with prices expected to remain subdued in 2009. Agriculture exports are projected to decline due to lower prices and reduced demand for crude palm oil and rubber, while mineral exports will contract due to lower prices of crude oil and LNG.

## With the weaker global economic outlook, export growth and capital flows are expected to be impacted further in 2009. Nevertheless, the current account surplus will remain sizeable as export contraction would be largely offset by import compression

In line with the weaker demand for manufactured exports and slower domestic economic activity, **gross imports** are expected to decline by 21.2%. Intermediate imports, which account for 70% of gross imports, are projected to decline as manufacturers reduce their production in line with the declining export orders. Imports of capital goods are also anticipated to decline sharply following the expected slowdown in the implementation of existing private sector investment projects and the postponement of new investment commitments. Meanwhile, imports of consumer goods are expected to decline marginally in line with more cautious consumer spending in the domestic economy.

The **services account** is projected to record a deficit of RM0.9 billion in 2009, as deficits in the transportation and other services accounts are

**Table 4.3**
**Balance of Payments**

| | 2008*e* | 2009*f* |
|---|---|---|
| | RM billion | |
| Goods | 170.1 | 108.1 |
| Trade account | 141.9 | 84.9 |
| *Exports (% annual change)* | *9.6* | *-25.3* |
| *Imports (% annual change)* | *3.3* | *-21.2* |
| Services | 1.7 | -0.9 |
| **Balance on goods and services** | **171.8** | **107.2** |
| Income | -25.4 | -10.6 |
| Current transfers | -17.0 | -16.6 |
| **Balance on current account** | **129.4** | **80.0** |
| **% of GNI** | **18.1** | **11.5** |
| Capital account | 0.6 | |
| Financial account | -123.9 | |
| **Balance on capital and financial accounts** | **-123.3** | |
| Errors and omissions | -24.3 | |
| *of which:* | | |
| *Foreign exchange revaluation loss* | *-5.8* | |
| **Overall balance** | **-18.2** | |

Note: Numbers may not necessarily add up due to rounding
*e* Estimate
*f* Forecast

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

expected to more than offset the surplus in the travel account. The travel surplus will moderate due to lower projected tourist arrivals as the weaker global economic outlook will affect travel by both corporates and households. With the anticipated further weakening of global trade and the travel industry, transportation earnings by domestic shipping and airline companies are expected to be lower. The deficit in other services account is expected to persist, reflecting continued payments, albeit lower, for imports of construction, communication and professional services.

The **income account** deficit is projected to be lower at 1.5% of GNI, reflecting mainly lower profits and dividends accruing to MNCs operating in Malaysia. The lower income projection is in line with the expected weaker export performance of the E&E industry as well as the oil and gas sector. Meanwhile, profits and dividends accruing to Malaysian companies investing abroad are also expected to be lower, particularly in the oil and gas, construction and services sectors.

**Table 4.4**
**External Trade**

| | 2008*p* | | 2009*f* | |
|---|---|---|---|---|
| | RM billion | Annual change (%) | RM billion | Annual change (%) |
| **Gross exports** | **663.5** | **9.6** | **495.7** | **-25.3** |
| *of which:* | | | | |
| Manufactured | 491.9 | 3.6 | 389.2 | -20.9 |
| Agriculture | 68.1 | 30.0 | 35.7 | -47.6 |
| Minerals | 87.5 | 43.2 | 54.7 | -37.5 |
| **Gross imports** | **521.6** | **3.3** | **410.8** | **-21.2** |
| *of which:* | | | | |
| Capital goods | 69.9 | ... | 57.2 | -18.2 |
| Intermediate goods | 379.1 | 5.7 | 286.5 | -24.4 |
| Consumption goods | 32.3 | 11.8 | 31.4 | -2.8 |
| **Trade balance** | **141.9** | **41.4** | **84.9** | **-40.2** |

... Negligible
*p* Preliminary
*f* Forecast

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

On the **financial account**, gross inflows of **foreign direct investment** (FDI) are anticipated to decline in 2009. The moderation, which began in the second half-year of 2008, is expected to continue into 2009 as business confidence worldwide remains weak and MNCs operating in Malaysia become increasingly focused on capital preservation in an environment of very weak global demand. Foreign investment in the manufacturing sector, in particular the E&E industry which are funded mainly by retained earnings, are anticipated to decline as MNCs are expected to continue to repatriate a larger share of their income back to their parent companies. Despite the higher levels of foreign manufacturing projects approved in 2007 and 2008, the implementation of these projects will likely be affected by the curtailment and postponement of investment plans given the weaker global demand conditions. In addition, rising excess capacity amidst the falling demand is expected to further discourage investment activity in the manufacturing sector. Meanwhile, FDI in the oil and gas sector is also expected to moderate given the falling prices and demand for crude oil. FDI in the services sector is also expected to be lower due mainly to declining merger and acquisition activity by foreign investors in an environment of falling global FDI flows.

Similarly, **direct investment abroad by Malaysian companies** is anticipated to be lower in 2009, with investments channeled mainly into the regional and other emerging economies. During the year, outflows for acquisitions of strategic interests in the services sector, which were committed towards end-2008, are expected to continue, particularly in the utilities and transportation sub-sectors. Meanwhile, overseas investments in the oil and gas, and construction sectors are expected to moderate, following the projected subdued performance of the oil and gas sector as well as a slowdown in the implementation of infrastructure and development projects, particularly in the Middle East and South Asia.

### Labour Market Outlook

The labour market is expected to further weaken in tandem with the slowdown in economic activity. Following the sharp deterioration in external demand since late 2008, businesses, particularly in those sectors that are exposed to external trade, are likely to continue to implement cost-cutting initiatives, including shorter work-week, voluntary separation schemes, temporary layoffs and retrenchments. The cautious sentiment amongst employers is indicated in the 2008-2009 Survey by Bank Negara Malaysia on employment outlook in the manufacturing, services and construction sectors, where about 24% of companies stated that they would reduce the number of jobs in 2009.

## Weaker labour market conditions in 2009

In contrast, the public sector is expected to step up its employment drive with the aim of employing 63,000 people in 2009-2010. In addition, the Government has also unveiled several measures to provide training opportunities to Malaysians affected by the economic slowdown as well as to incentivise employers to recruit retrenched workers. It is expected that 100,000 training opportunities will be created through these

**Table 4.5**
**BNM Survey on Salary Outlook in 2009**

| | 2008*e* | 2009*f* |
|---|---|---|
| **Average - all sectors** | **5.9** | **2.7** |
| Construction | 6.3 | 3.1 |
| Services | 5.1 | 2.7 |
| Manufacturing | 6.3 | 2.2 |

*e* Estimate
*f* Forecast
Source: BNM Survey, 2008/2009

initiatives. Nonetheless, these measures would not be able to fully offset the overall weak prospects in the labour market. Consequently, the **unemployment rate** is expected to increase from 3.7% in 2008 to 4.5% in 2009, while the average private sector **salary** increase is expected to moderate to 2.7% (2008: 5.9%).

### Inflation Outlook

Headline inflation is expected to slow significantly to average between 1.5% and 2.0% in 2009. This reflects the continued moderation in global energy and food prices and slowing global inflation precipitated in part by the reversal in commodity prices caused by the global financial deleveraging and the contraction in global economic activity. As a small and highly open economy, the decline in global commodity prices and recessionary influences will have a material impact on price developments in Malaysia. Domestically, the impact of downward adjustments to administered prices by the Government and the expected slowdown of economic activity will also restrain price pressures.

Global commodity prices are expected to continue to fall in 2009 in line with the slowdown in global economic activity. Crude oil prices as reflected in the West Texas Intermediate futures front-month have averaged USD40.59 per barrel in January-February 2009, representing a 72.1% decline since the peak in July 2008 and a 59.2% decline from the average of 2008. The sharp increase in world cereal production (comprising wheat, rice and coarse grains) in 2008 will facilitate a rebalancing of the global cereal supply and demand in 2009. Data from the February 2009 edition of the Food and Agriculture Organization of the United Nations' (FAO) *Crop Prospects and Food Situation* indicates that the ratio of cereal production relative to utilization has increased from 0.97 in 2006/07, to 1 in 2007/08, and to 1.03 in 2008/09. This development has exerted downward pressure on international cereal prices.

The prevailing global economic and financial crisis has significantly weakened the outlook for demand across both developed and emerging economies. The weak demand conditions are likely to depress prices in the affected countries. Consequently, inflation in the countries that are Malaysia's major sources of imports is expected to nearly halve to 2.6% in 2009 from 5.1% in 2008. This will allow greater flexibility for local importers and users of imported inputs to align prices with domestic demand conditions.

Similarly, the weaker external environment has begun to affect domestic economic activity. Faltering export demand has adversely affected the manufacturing and resource-based sectors, as well as the service sector that is dependent on them. The general deterioration in consumer and investor sentiments is expected to culminate in a broader fall in demand. The expected rise in unemployment and the corresponding moderation in disposable incomes, as well as the larger output gap are likely to keep demand-driven price pressures contained.

The series of adjustments to administered prices by the Government will have a noticeable impact in reducing inflation. The lapse of the impact from the adjustments to retail fuel prices in 2008 is expected to exert a significant downward impact on inflation in the second half of 2009. The reduction of electricity tariffs and gas prices announced in February 2009 will further ease consumer price inflation both directly, and indirectly through lower costs of productive inputs. Any further reductions in administered prices during the year will have a similar effect on inflation. In the current challenging economic environment, the downward adjustments to prices by the Government will significantly help to alleviate the burden of households and businesses by keeping prices and production costs low.

In terms of the countervailing upward pressures on inflation, the depreciation of the ringgit's nominal effective exchange rate since the beginning of 2008 has been relatively small, and is unlikely to result in higher imported prices. There may also be a temporary loss of productivity as the economy adjusts to the lower demand. However, the impact of this on inflation is expected to be more than offset by the strong forces behind the moderation in economic activity as wage and input costs are reduced. Consequently, inflation will remain low in 2009, especially in the second-half of the year.

**MONETARY POLICY IN 2009**

The world economy will continue to face significant challenges in 2009. The advanced economies, representing more than 60% of the world economy, are expected to be in recession. Likewise, the export driven economies in Asia face the prospect of a severe slowdown in economic activity. As one of the most open economies in the region, Malaysia is already affected by the deteriorating external environment.

With the risk of inflation abating considerably, the balance of risk has shifted from inflation to growth. Headline inflation decelerated to 3.9% in January 2009 from the July 2008 peak of 8.5%. There are strong indications that this downward trend is likely to continue during 2009. The weakening global demand has brought down global food and energy prices and is expected to continue to exert downward pressure on domestic inflation. Wage demands will be muted. Conversely, the risk to economic growth has intensified. Manufacturing production and exports have declined since September 2008 and October 2008 respectively, particularly in the electronics and electrical sector. The deepening of the global economic downturn is likely to affect domestic economic activity and employment prospects as the year progresses.

As a pre-emptive measure, the Monetary Policy Committee reduced the OPR by 25 basis points in November 2008, followed by further reductions of 75 and 50 basis points in January and February 2009 respectively to provide a more supportive monetary environment for the domestic economy. Lower interest rates are expected to provide support for domestic demand through the availability of credit at lower costs and by increasing disposable income through lower debt servicing costs. Lower interest rates also increase the affordability of loans and reduce the cost of capital.

Given the downside risk to growth, it is important that the financial system continues to function effectively and that the flow of credit is not impeded. At the first instance, reductions in the OPR need to be translated into lower retail borrowing costs speedily. To this end, the reductions in the OPR were accompanied by reductions in the Statutory Reserve Requirement (SRR) and the floor on deposit rates. This move softens the narrowing of bank margins, and thereby promotes the downward adjustments of interest rates. The demand for loans must also be matched by supply. The capacity of banks to provide credit will depend on the quality and strength of their balance sheets. Prudent policies and the substantial progress in developing and strengthening the domestic financial system since the Asian Financial Crisis have contributed to its resilience. As a consequence, the banking institutions' capacity to perform the intermediation function remains strong.

The reduction in deposit rates does not detract from the longstanding emphasis on ensuring a positive real rate of return to savers. With inflation trending down, the real rate of return on 12-month deposits is expected to average approximately above 0.5% this year. The Bank also announced the issuance of the Merdeka Savings Bond amounting to RM2 billion on 28 January as an additional savings instrument for Malaysian citizens aged 56 and above. Meanwhile, the Government has also announced the issuance of syariah-compliant Savings Bonds amounting to RM5 billion for citizens above 21 years old. With a nominal return of 5% per annum, the real return on these bonds are expected to average above 3% in 2009.

Going forward, the Bank will continuously assess the appropriateness of the OPR and its monetary policy stance. As monetary policy works with a lag, the Bank has frontloaded the cumulative 150 basis points OPR reduction in view of the significant moderation in the prospects for growth and inflation. In the next few months, the Bank will continuously assess whether all these measures are having their intended effects in sustaining domestic credit expansion and economic activity.

The current environment is exceptional both in terms of its gravity and scope. It will require a concerted policy response at both the national and international level. Globally, while central banks are easing monetary policy, governments are undertaking fiscal stimulus on a scale that are creating large fiscal deficits unseen in recent years. Such complementarity of policies is necessary. Monetary policy, as a demand management tool, has limits on the magnitude of reflation it can achieve in the current environment. Fiscal policy has an important role in compensating for the fall in private demand through an increase in public spending. In addition to the stimulus package of RM7 billion announced in November 2008, the Malaysian Government has announced an additional stimulus package worth RM60 billion on 10 March 2009 to mitigate the adverse developments in the external sector. The collective impact of monetary and fiscal policies should limit the effect of the global economic downturn on domestic economic activity and provide a firm base for the economy to return to its medium-term growth path once global economic and financial conditions normalise.

The collective impact of monetary and fiscal policies should limit the effect of the global economic downturn on domestic economic activity and provide a firm base for the economy to return to its medium-term growth path once global economic and financial conditions normalise

**FISCAL POLICY IN 2009**

The severity of the global economic downturn and uncertainties on the length of the downturn is likely to lead to a general weakness in domestic confidence. Both monetary and fiscal policies are needed to mitigate the impact on the domestic economy and support domestic demand. While monetary policy has significantly lowered interest rates and provided ample liquidity to support financing activity, an expansionary fiscal policy is needed to directly support economic growth by increasing public spending, compensating for the declines in the external and domestic demand. It would also stimulate private sector demand by providing incentives for private consumption and investment.

The Federal Government's 2009 Budget announced in August 2008 was initially formulated with the principal objective of further strengthening the nation's economic resilience in the face of the two-fold challenges of rising inflation and increased uncertainties. Of importance was the greater focus on measures to ensure that the well being of Malaysians especially those in the lower and middle income groups is protected in an environment of volatile prices. Towards this end, a broad range of measures were introduced, including an increase in the eligibility criteria for welfare assistance from a monthly income of RM400 to RM720, a one-month bonus for civil servants and a reduction of import duties for several consumer products. In addition, personal income tax rates were reduced from 28% to 27% for those in the top income tax bracket and from 13% to 12% for the RM35,000 - RM50,000 tax bracket. Government spending also continued to be focused on enhancing the efficiency of public transport, improving health care and education, and providing housing incentives for Malaysians.

As the financial crisis deepened and the global economic situation worsened in the fourth quarter of 2008, fiscal policy was then geared to undertake a counter-cyclical role. Towards this end, the Government announced a RM7 billion Economic Stabilisation Plan on 4 November 2008. The plan, financed by the savings from the lower fuel subsidies expenses, represents a combination of public spending to compensate for the fall in private sector demand and measures to reinvigorate private spending. Of the total RM7 billion, RM4.7 billion is allocated for small-scale construction and development projects including the building of low- and medium-cost houses. The rest is channeled for upgrades and maintenance of social infrastructure and public amenities such as roads in rural areas, schools, hospitals, police stations and army quarters. In order to boost private consumption, the Government announced several other measures including the option to reduce employee's contribution to the Employees Provident Fund

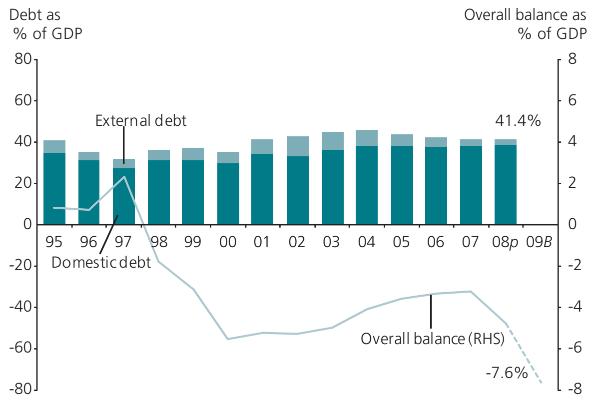
**Table 4.6**
**Federal Government Finance**

| | RM billion | | % change | |
|---|---|---|---|---|
| | 2008*p* | 2009*B* | 2008*p* | 2009*B* |
| Revenue | 159.8 | 160.8 | 14.2 | 0.7 |
| Total expenditure | 196.3 | 215.9 | 20.0 | 10.0 |
| *Operating expenditure* | *153.5* | *159.2* | *24.7* | *3.7* |
| *Gross development expenditure* | *42.8* | *56.7* | *5.6* | *32.4* |
| Loan recoveries | 1.0 | 1.2 | | |
| **Overall balance** | **-35.6** | **-53.8** | | |
| **% of GDP** | **-4.8** | **-7.6** | | |
| *Sources of financing:* | | | | |
| Net domestic borrowing | 35.7 | - | | |
| Net external borrowing | -0.5 | - | | |
| Realisable assets [1] and adjustments | 0.4 | - | | |

[1] A positive (+) sign indicates a drawdown in the accumulated realisable assets
*p* Preliminary
*B* Revised budget
Note: Numbers may not add up due to rounding

Source: Ministry of Finance

**Chart 4.5**
**Federal Government Fiscal Balance and Debt**




*p* Preliminary
*B* Revised budget

Source: Ministry of Finance

(EPF) from 11% to 8% for two years, extension of the repayment period for civil servants' housing loans and an increase in the limit for civil servants' car loans.

On 10 March 2009, the Government announced an additional stimulus package to mitigate the impact of a more pronounced global economic slowdown. The broad thrusts of the economic stimulus programme are to reduce unemployment and increase employment opportunities, assist and ease the burden of both households and businesses and build long-term capacity of the economy. The announced package amounting to RM60 billion or almost 9% of GDP, will be implemented over 2009 and 2010. Of the total, RM15 billion would be in the form of fiscal injection, RM25 billion for Guarantee Funds, RM10 billion for equity investments, RM7 billion for private finance initiative and RM3 billion in the form of tax incentives.

As a result of the large stimulus package, the Federal Government's fiscal deficit is estimated to widen from 4.8% of GDP in 2008 to 7.6% of GDP in 2009. The Government continues to finance the fiscal deficit from non-inflationary domestic sources, mainly through the issuances of Malaysian Government Securities (MGS) and Government Investment Issues (GII). In addition, the Government would issue a retail bond, the Government Savings Bond, amounting to RM5 billion. This, in part, provides an alternative savings instrument for savers. Importantly, with ample liquidity and high domestic savings in the domestic financial sector, public sector spending would not crowd out the availability of financial resources to the private sector.

### Foreign Exchange Administration of Malaysia

While the protracted global financial crisis has yet to be resolved, many new lessons have been learnt. In this context, the implications for the pace of capital account liberalisation need to continuously be assessed. Malaysia has continuously reviewed the relevance of the remaining foreign exchange administration (FEA) rules to achieve greater efficiency in the conduct of international financial transactions. Issues for consideration is to ensure that there will be no disruption to the financing of international trade and investment in an environment of short US dollar liquidity, highly volatile capital flows, capital markets are more risk averse and heightened counterparty risks for settlement and payments.

During the height of the Asian financial crisis, the FEA rules assumed a significant role and were implemented as part of a comprehensive Economic Recovery Plan to expedite reforms, restore stability and promote growth in the domestic economy. With the stabilisation of the economy following the implementation of the Economic Recovery Plan, the rules have been removed in a series of sequenced and progressive liberalisation initiatives. The liberalisation has extended beyond removing these rules. This has been in line with the overall philosophy of creating a conducive business environment to facilitate private sector expansion and enhance overall competitiveness of the economy. The country's improved economic fundamentals, a strong and resilient domestic financial sector as well as the development of a more effective and comprehensive surveillance framework have permitted a more rapid pace of liberalisation of the FEA rules since 2003. Major and significant liberalisations were made in 2005 and 2007 on rules affecting the flexibility of capital flows to enhance business efficiency and promote foreign direct investments.

In 2008, the FEA rules were further liberalised, aimed at enhancing Malaysia's competitiveness by facilitating greater flexibility and accessibility to financing by businesses and reducing the cost of doing business in Malaysia. A resident corporation is free to borrow any amount of foreign currency from licensed onshore banks, non-resident non-bank parent company and other resident companies within the same corporate group in Malaysia. The resident corporation is also free to refinance any outstanding approved foreign currency borrowing.

To provide additional flexibility of financing for real sector activities in Malaysia, a resident corporation is free to borrow any amount of ringgit from its non-resident non-bank parent company for such purposes. A non-resident non-bank company or individual is also allowed to borrow any amount in ringgit from resident corporations as well as the licensed onshore banks to finance the real sector activities in Malaysia.

To promote Malaysia as an International Islamic Financial Hub, International Islamic Banks, International Takaful Operators and International Currency Business Units of licensed onshore banks, takaful operators or retakaful operators may make payments in foreign currency to resident intermediaries for the settlement of financial services rendered. In addition, to support the development of domestic financial markets, residents are free to invest in US dollar denominated crude palm oil futures contracts on Bursa Malaysia.

The remaining existing FEA rules are mainly for prudential safeguards to support monetary and financial stability and can be categorised as supporting the following broad objectives-

(i) Facilitating the effective use of domestic financial resources;
(ii) Sustaining manageable level of external debt;
(iii) Safeguarding against speculation on the domestic currency; and
(iv) Facilitating overseas investments by Malaysian corporations.

The deterioration of the global financial landscape in 2008 has underscored the need for prudent and pragmatic external debt management policies that are consistent with the country's long-term economic growth, extension of the domestic economic frontier and the nation's strategic economic agenda. In safeguarding against speculation on the ringgit, the non-internationalisation of the ringgit restricts the access to financing speculative activity on the ringgit by non-residents.

**The administration of FEA rules – going forward**

While the FEA rules are still relevant and would continue to serve as a prudential safeguard in supporting and complementing the broad macro-economic policy framework to maintain the country's economic and financial stability against external shocks, Malaysia remains committed to progressively liberalise the FEA rules. This is particularly important as Malaysia is a small and open economy with its domestic financial system highly integrated with the international financial markets.

The liberalisations going forward, will be conducted within a holistic framework and will be undertaken in an orderly and progressive approach with careful and comprehensive assessment to ensure the following guiding principles are met:

**(i) The benefits of the liberalisations outweigh the costs and risks**
The country has a strong track record of policy pragmatism and maintains the objective of ensuring that policies liberalised will be able to meet its goal of sustaining and enhancing competitiveness during periods of high and sustained economic growth as well as able to withstand periods of vulnerabilities and shocks that confront the domestic economy. The liberalisations undertaken thus far have yielded economic benefits to the country outweighing the trade-offs of the increased risks that may be associated with the liberalisations.

**(ii) The liberalisations be supported by "readiness" of the economic and financial system**
Consideration for liberalisation of the FEA rules will be based on comprehensive evaluation of the domestic and global economic and financial conditions to ascertain the state of readiness of the economy. Important preconditions include sound macroeconomic fundamentals supported by a sufficiently robust regulatory framework. This would be achieved through continuous environmental scanning, the establishment of an effective and a comprehensive surveillance system for early detection of possible vulnerabilities and emerging risks.

**Conclusion**

The country's strong trade and financial inter-linkages with the regional and global economies merit continuous review of the rules in order to continue to be supportive in facilitating the nation's economic transformation taking into account the new regional and global challenges. Malaysia will also continue to pursue a comprehensive strategy in administering the FEA rules to harness the full potential of the Malaysian economy while promoting a sound and stable financial system as well as a resilient and competitive economy. This comprehensive approach is key in the efforts towards achieving balanced and sustainable growth with stability.

# Governance, Communications and Organisational Development

# Governance, Communications and Organisational Development

## OVERVIEW

The governance, communications and organisational development initiatives in 2008 continued to emphasise on transforming the Bank into a more strategy-focused and performance-based organisation. Operating in an increasingly uncertain and difficult financial and economic environment, the challenge is to ensure that the Bank continues to remain effective and efficient in delivering its mandate. During the year, continuous enhancements were made in the areas of strategic management, governance, communications, risk management and talent management to further strengthen the organisational capability and capacity of the Bank. There was also a reinforcement of the strong knowledge-based and performance-driven culture to enhance the agility of the Bank in responding to the new challenges that were emerging.

The communications function of the Bank has also assumed greater significance with heightened engagement with stakeholders that have resulted in the improved understanding of the economic and financial developments. Greater two-way flow of information and engagement between the Bank and its stakeholders has enabled better management of stakeholders' expectations, thus promoting confidence in the Bank's policy measures and actions.

The enhanced strategic management process implemented in 2008 which involved enterprise level mid-term business planning, had facilitated a more effective and robust process of setting, implementing and reviewing organisation-wide priorities, resource allocations, and accomplishments. The initiatives improved the management and tracking of the key business strategies and programmes in meeting the desired outcomes. The strategic focus and priorities of the Bank are now reflected in the Bank's Business Plan using a 3-year rolling period. The Plan serves to provide clarity in the Bank's objectives, enhances focus in the Bank's organisational development efforts, facilitates the evaluation of performance of the various initiatives, and enables a more optimal utilisation and alignment of resources within the organisation.

The adoption of the revised Enterprise Risk Management (ERM) framework during 2008 has made risk management more entrenched in the Bank's decision-making process. This has allowed for better identification and management of key risks at the organisation level, while providing reasonable assurance to the Management and Board that ex-ante risk mitigation measures are in place in achieving the Bank's objectives. The enhancement in structures and processes within the existing ERM framework led to reinforcement of roles, accountability, focus through specialisation, and increase in effectiveness and efficiency of risk management process without corresponding increase in resources directed at managing risks.

In ensuring the Bank's talent needs are fulfilled on a sustainable basis, the focus of talent management was on developing a healthy talent pipeline for executive readiness and leadership succession. To complement this, efforts on talent sourcing and retention as well as aligning human capital development with business strategies were also strengthened during the year. In the area of learning and knowledge management, efforts were directed towards better alignment of the initiatives with the Bank's business needs, as evidenced by greater customisation of learning, made possible through closer collaboration with line departments. The Bank also continued to place emphasis on self-directed learning through the introduction of the core central banking curriculum to augment its training and learning strategies. In addition, the increased leverage on technology facilitated improvements in knowledge sharing and accessibility as well as learning efficiency, particularly through the Bank's enhanced intranet and the newly launched Learning & Knowledge Portal, provided wider outreach and easy access to information and learning services for staff.

Meanwhile, ICT management remained focused on providing leading-edge and on-demand technology solutions to support the various business functions of the Bank. In line with the intensified regional integration and cooperation, the Bank's capacity to manage technical cooperation with external agencies was strengthened further, which resulted in more technical assistance programmes to a larger number of recipients.

**GOVERNANCE**

In 2008, the Bank continued to advance its governance framework and practices which are built upon three important pillars, namely, maintaining the Bank's **independence** based on the given roles and need for operational autonomy; instituting strong **accountability** based on the need for operational effectiveness and efficiency as well as monitoring performance and managing the associated risks; and the demonstration of **transparency** through clarity of its actions as they impact the Bank's multiple stakeholders. Independence also demands greater accountability and transparency in the conduct of the Bank's activities and mandates.

The accountability and independence of the Bank are accorded by the Central Bank of Malaysia Act 1958 (CBA). The Board of Directors which functions as an oversight board, comprises the Governor, three Deputy Governors, the Secretary General to the Treasury and four other professional members with diverse knowledge and corporate experience. Providing oversight to the operations, the Board is entrusted with the responsibility for the general policy, administration and business of the Bank. The Governor chairs the Board while the Board Audit Committee is chaired by an independent director.

The Management Committee, which is the highest executive body within the Bank and chaired by the Governor, meets weekly to deliberate on policy matters pertaining to the financial system, the economy and the general operations of the Bank. The Management Committee is supported by other policy committees, which are also chaired by the Governor. These committees include, the Reserve Management Committee, Monetary Policy Committee, Financial Sector Policy Committee and Risk Management Committee. These policy committees provide the forum for balanced deliberation, formulation and implementation of decisions on a wide range of issues. The collective skills, depth and breadth of experience and knowledge of the Management Committee, the extensive use of cross-functional committees and combined with the legal framework under the CBA, have contributed significantly to the Bank's capacity for effective policy formulation and implementation.

Against the backdrop of significant changes in the domestic and global economic and financial landscape, and the evolving nature and role of central banking, a comprehensive review of the CBA was undertaken in 2008. The new CBA proposes to institutionalise many of the Bank's existing governance practices. Additional provisions will be incorporated with a clear orientation towards central bank modernisation as well as to equip the Bank with the necessary powers and policy instruments moving forward. In addition, efforts were initiated towards consolidating the various existing legislations concerning the Bank's multiple financial supervisory roles and functions into one omnibus law.

As a regulatory and supervisory authority operating in a interconnected financial system, the Bank also has in place Memorandum of Understanding with the various financial authorities such as the Securities Commission and the Malaysia Deposit Insurance Corporation for purposes of coordinating policy formulation and execution relating to the supervision and regulation of the financial system. At the regional and international levels, the Bank is actively involved in fora such as those under the umbrella of Executive Meeting of East Asia and Pacific Central Banks (EMEAP), International Monetary Fund, International Association of Insurance Supervisors, Bank for International Settlements, Asia Pacific Economic Cooperation Financial Regulatory and Advisory Groups, all of which are aimed at promoting international and regional financial stability through coordinated development initiatives, standard setting, financial surveillance and risk management.

In carrying out the Bank's broad mandate, some of the Bank's senior officers participate actively in various forums, such as committees, outside the Bank. However, in keeping with the Bank's strategic focus and priorities, a review of such involvement in external committees was conducted during 2008 to assess the need to continue such roles and engagements, and where appropriate, to exit from these committees. The review was also undertaken to pre-empt possible conflict of interest situations which could be detrimental to the Bank's independence and accountability.

As part of on-going organisational development, the Bank's internal audit functions and processes were reviewed to strengthen the controls towards compliance with financial and non-financial requirements and to adopt a risk-based internal audit framework in 2009. In addition, the internal governance concerning financial controls continues to be strictly adhered to. Further enhancement was introduced during the year in the Bank's formal budgeting process. Initiatives to enforce the culture of cost consciousness were continued, and further progress was also recorded in the policies and practices to make the operational spending and procurement processes more effective and rigorous.

The Bank keeps the Minister of Finance informed of the monetary and banking policies and other policies that fall within the Bank's jurisdiction. In respect of transparency, the Bank has moved well beyond fulfilling the statutory disclosures.

## COMMUNICATIONS

### Communications an integral role in Bank Negara Malaysia

In recent years, the communications function of the Bank has assumed growing significance by playing an integral role in the Bank's operations. Greater engagement with stakeholders are undertaken with the ultimate objective of providing more clarity on the Bank's policies and measures. Amidst the more challenging external and domestic environment in 2008, the Bank has stepped up its communications efforts, through pro-active and timely communications with key stakeholders, including Government officials, industry groups, analysts, media and members of the public. These have elevated the understanding on the Bank's policies and initiatives, enhanced channels of receiving quality feedback, thereby contributing to an improved process for making informed decisions.

### Greater and timely engagement with key external stakeholders

To promote greater understanding of monetary policy decisions among stakeholders in the financial markets, monetary policy communications has been enhanced significantly. These include the continued advance release of the schedule of Monetary Policy Committee meetings, initiated in December 2005 and the same day release of Monetary Policy Statements. As the year progressed, the Bank's communications function was put to severe test, in view of the challenges faced. The Malaysian economy was facing rising inflationary pressures in the first half of the year, following the higher global food and commodity prices. When the market views turned out to be different from the Bank's stance on interest rates during this period, it was for monetary policy communications to explain the basis for the policy decisions. The Bank has clearly signalled in its communications that the weaker growth prospects in the subsequent months would have a moderating impact on inflationary pressures. Ultimately, the Bank's decision was accepted by the market, as the events unfolded. (For more details on monetary policy communications, please refer to Box Article of Chapter 3).

In this highly uncertain economic environment, greater interaction with stakeholders becomes even more essential. For 2008, in addition to scheduled official meetings, the Bank also continuously engaged with the financial institutions, analysts/economists, business leaders, specific industry groups, including Small Medium Enterprises (SMEs) and the public at large. These regular engagement sessions enabled the Bank to provide up-to-date assessments on the changing economic and financial conditions and the issues arising. These efforts, beside enabling the stakeholders to be better prepared in facing the challenges, also provided a channel for the Bank to address specific issues, including reinforcing the importance of responsible lending behavior on the part of financial institutions and to ensure that viable and well-run businesses, including SMEs, will continue to have access to financing. Financial institutions were also encouraged to be pro-active in dealing with customers, including in rescheduling and restructuring of credit facilities of borrowers facing difficulties due to the current economic downturn. These efforts provided the Bank with a critical source of information on the real issues faced by the stakeholders, which served as valuable inputs for policy formulation.

The Bank also continued with its annual series of communications sessions with various stakeholders during the release of the Bank's Annual Report and Financial Stability and Payment Systems Report. These sessions provide a platform for the Bank to communicate the assessment on key issues relating to economic and financial developments as well as the prospects going forward. The end-results were the improved understanding on various economic and financial policy issues and a two-way flow of information and engagement between the Bank and its stakeholders.

The Bank further reinforced its working relationship with the media as a key platform for mass information dissemination to members of the public. The Bank has established networks with the local, regional, print and electronic media by organising regular meetings, informal discussions and information-sharing sessions, scheduling exclusive interviews on key issues with senior officers of the Bank, and conducting background briefings on technical issues related to the Bank. This has resulted in more accurate and balanced reporting on the issues relating to the Bank's policies and initiatives to the public at large.

**Strategic Communications on key initiatives**

For 2008, the Bank had also implemented several strategic communications programmes to support a number of key initiatives. In 2008, Malaysia as an International Islamic Financial Centre (MIFC) global awareness campaign was launched. The communications campaign highlighted the opportunities and offerings in Malaysia for investors, issuers, industries in the economic sectors and for professionals and practitioners with interest in the Islamic financial services industry. It has also strengthened Malaysia's connectivity with the rest of the world. A dedicated MIFC Promotions Unit was established in 2008 to provide greater focus in the Bank's efforts to promote and market Malaysia as a hub for Islamic finance.

As one of the key drivers of SME development in Malaysia, the Bank has developed and implemented communication programmes which offer SMEs greater access to information on financing, business opportunities and the SME sector as well as SME financial advisory and mediation services provided by the Bank. This was achieved through the multi-lingual SMEinfo Portal, the SME Annual Report and various other communication channels. There was also increased communication activities to promote micro financing, namely the display of the microfinance logo by microfinance providers and through the mass media. All these are part of efforts in enhancing the SME development agenda towards the formation of competitive and resilient SMEs as well as acting as a catalyst in unlocking the potential of micro entrepreneurs to participate in the mainstream economy.

**Reaching out to the general public on financial matters**

In taking the public understanding of financial matters to the next level, the Bank has adopted a one-stop centre for public interface, the Integrated Contact Centre (ICC). Under this set-up, all public queries and complaints on banking and insurance matters is put under one roof, thereby facilitating effective resolution of disputes. It also acts as a channel for feedback from public on the Bank's policies, guidelines and practices to the line departments. The Bank's walk-in service centre, 'Laman Informasi Nasihat dan Khidmat' (BNMLINK), serves as a platform for visitors' enquiries and complaints in matters under the purview of the Bank. This has been expanded to the Bank's branches in Johor Bahru and Pulau Pinang as BNM MINI LINK to cater for outstation customers. This was further complemented by BNMTELELINK which manages enquiries via telephone calls, facsimiles, letters and e-mails and the Complaint Management and Advisory (CMA). The CMA facilitates resolution of public, including SMEs, complaints against institutions under the purview of the Bank and also provides financial advisory services to SMEs.

Since its establishment in 2005 until end of 2008, the BNMLINK has seen an increase of about 71% in the number of monthly average customers who have sought its services (about 2,960 in 2005 to 5,070 for 2008). This shows the continuous increase in the Bank's interface with the public. BNMTELELINK also reported close to 80% increase in the monthly average queries to more than 6,320 in 2008 (2007 : 3,560). Meanwhile, the monthly average number of cases handled by CMA was sustained at about 690, despite the coming into operations of BNMTELELINK as an additional channel to handle public queries on financial matters.

**Enhancing employee communications and knowledge sharing**

The Bank is already in the path of transforming to a Knowledge Based Organisation with its consequent benefits of improved productivity and performance. The year 2008 saw the Bank's intranet, Kijang.net, evolving into becoming the Bank's Enterprise Portal (EP) to accelerate this transformation. Among the EP's enhanced features were improved and timely information access across the organisation and delivery of the right content and services through an electronic collaborative work environment. This in turn has fostered innovation and business process transformation. The EP has enabled the effective alignment of the entire organisation to deliver the Bank's desired outcomes through the sharing of its business objectives, strategies, views and vision with staff. It has also facilitated the bottom-up process through the provision of an avenue for staff to share their opinions and discuss on the developments in the Bank.

In summary, with the added features and innovation, the employees have become more informed and connected. The Kijang.net has become the knowledge and communications hub for staff, driving employee engagement across the Bank to higher levels and promoting the Bank's values and work culture.

Moving forward, there will also be more opportunities for communications in an informal environment between staff and management on key issues and developments. These will ultimately contribute towards improving the Bank's productivity and capacity to deal with challenges through instilling a culture that keeps staff learning, thinking and acting positively.

## ORGANISATIONAL DEVELOPMENT

**Strategic and Performance Management**

In 2008, the Bank continued its focus on becoming a performance-driven organisation. The Bank made deliberate attempts and managerial interventions to make the organisation highly strategy-focused, which translated into greater organisation-wide clarity and understanding of the Bank's objectives and goals, and alignment of resources, processes, structure, people and leadership towards the achievement of those objectives and goals. The focus on performance also means that the Bank as an entity is progressing to become more results-oriented, while its people and leaders are more role-based in their orientation, in order to improve collective organisational performance.

The year 2008 saw the Bank put in place a more robust strategic management structure and processes. In line with this, the Bank developed the Medium Term Business Plan (2009-2011) that documents the key priorities and desired strategic results, business strategies as well as action plans to guide the organisation in achieving its objectives. During the year, the alignment and linkages between strategic management and financial or operational planning were further reinforced through better management of process flows, sequencing of tasks and activities, and vigorous assessment of requests from line departments for financial allocations, based on a decision matrix which is strategy-linked and outcome-driven.

The new, more structured strategic management process was designed to facilitate cross-functional conversations on business issues and strategies, thus fostering greater collaboration across sectors and departments, leading towards better appreciation of the critical inter-linkages and dependencies among functional units. It served to provide a feedback loop and platform for the management and business units to deliberate and review the effectiveness of strategies, as well as performance issues that could have implications on the Bank's efforts in achieving its objectives. The processes would allow the Bank to assess the adequacy of talents, learning, knowledge, technology, infrastructure and leadership, and whether or not these elements are appropriately aligned to support the Bank's strategic focus.

**Talent Management**

One of the most important objectives of talent management in the Bank is to ensure that the talent needs of the Bank are met in the most effective and efficient manner, towards the achievement of the Bank's goals and objectives. The Integrated Human Capital Management (IHCM) provides a holistic approach in institutionalising critical orientations and policies in talent management, and in integrating processes relating to talent demand, talent supply, performance management, staff development as well as rewards management. The IHCM blueprint requires a greater collaboration and effective inclusion of stakeholders in managing talent issues. This would ensure alignment of talent management policies and practices with business needs, and that talent management directly contributes towards the achievement of desired strategic results.

Implementation of the IHCM had seen the introduction of performance differentiated rewards, broad banded job and salary structure, and a new competency model. In addition, the processes include constant assessment of performance of talents in the Bank, to correspond with the dynamics of the Bank's operating environment, stakeholders' expectation, role realignment, rising performance benchmark, and overall aspirations of the Bank.

The focus of talent management in 2008 was on developing a healthy talent pipeline for leadership succession for the next five years. The process involved the assessment of potential talents for executive readiness and job fit, supplemented with formal and informal development interventions. The Leadership Profiling Centre in the Human Resource Management Department provides a consistent, robust and transparent platform to enable the identification and assessment of talents for mission critical positions in the Bank.

As the strength of the succession pool is dependent on the quality of the overall talent pool, efforts had also been focused on attracting top talents into the Bank, retaining, developing and motivating them. The Bank had been more innovative in sourcing for talents through multi-pronged efforts, including collaboration with local and foreign higher learning institutions with good track records in producing high quality talents, early identification and engagement with prospective talents, and hiring of experienced specialists and professionals to meet immediate needs in mission critical positions.

The Bank's scholarship programme continued to be an important source of the Bank's long term talent pool. In 2008, a total of 81 selected high potential students were awarded scholarships to pursue pre-university programmes at local colleges and first degree programmes at local and foreign universities, in disciplines relevant to central banking. In a continuous effort to develop and enhance capabilities of staff within the Bank, 42 staff at various levels were awarded scholarships to pursue first degree and post-graduate education at local and foreign institutions.

As part of its nation-building initiatives, the Bank awarded 10 scholarships under the Kijang Emas Scholarship Award to students with outstanding results in the 2007 Sijil Pelajaran Malaysia examination. Recipients of this special award were free to enroll in any field of studies of their choice and upon completion of studies are required to return to Malaysia, in line with the Bank's aspiration of developing top talents in the country. In addition, the Bank introduced the Scholarship Award for Secondary Schools, awarded to 20 students with excellent performance in the Penilaian Menengah Rendah examinations. This programme is aimed at the early identification of potentials for the Bank's talent pool and to provide financial assistance to students from lower income families.

In a continuous effort to promote greater clarity on roles and alignment with the strategic objectives of the Bank, several departments in the Bank reassessed their structure, talent and capability needs, and manpower numbers, guided by a more role-based approach in managing processes and delivering their strategic results. The exercise led to constructive changes in departmental structures, new profiling of talents, knowledge and learning requirements, realignment of roles, rationalisation of functions, greater reliance on technology to improve efficiency and effectiveness and greater horizontal and vertical collaboration within and across departments.

The total staff strength of the Bank increased by one percent to 2,616 as at end-2008, as compared to end of 2007, while the attrition rate due to retirement and resignations remained at four percent. The ratio of executive to non-executive staff remained at 3:2, with continued focus on strengthening of the professional and executive pool.

**Learning and Knowledge Management**
During 2008, the Human Capital Development Centre (HCDC – formerly referred to as Human Resource Development Centre, or HRDC)

adopted a new organisational structure to meet the new challenges in learning and talent development. The new structure transformed HCDC from a functional-based unit to a value-based and role-based learning and knowledge management centre. The structural changes facilitated further integration of learning and knowledge management processes, improvement of the competencies of HCDC staff in delivering learning solutions, as well as in leveraging on technology for greater effectiveness and operational efficiency.

To meet the demands for learning solutions that meet the learning needs of knowledge workers and which focus on positive impact on performance of business units, efforts were directed towards increasing the availability of customised learning solutions. Learning and knowledge management solutions were designed specifically to meet the business needs of the specific stakeholders, incorporating blended learning architectures that integrate a variety of the delivery channels to achieve both individual and organisational learning goals. Greater emphasis was placed on the transfer of learning at the workplace, and the measurement of the impact of learning on performance. Overall, the average learning investment per employee for 2008 was RM8,200, which represented 11% of staff salary, with an average of 10 training man-days per employee.

To further promote the culture of self-managed, self-directed learning, the Bank developed a competency-based core central banking curriculum during the year. Through the integration of the new curriculum with the Bank's Learning Management System, and supplemented by the information on role profiling and career development options, employees would now be able to determine their own learning needs, the appropriate learning solutions that they could have access to, and the preferred learning progression paths that they wish to pursue based on their performance targets and career aspirations.

Staying focused on the objective of leveraging effectively on collective knowledge for performance, the Bank continued to enhance its knowledge infrastructure and nurture a knowledge-rich environment conducive for knowledge-sharing and knowledge re-use in achieving business objectives. In enhancing its knowledge infrastructure, efforts were made to enhance learning and knowledge management systems and improve content delivery to stakeholders.

The Learning Management System provided online learning opportunities for employees and enhanced operational efficiency through online registration to learning solutions. E-learning courses ranging from the FSI Connect suite of central banking technical subjects, to those of management and ICT, provided employees with a broad selection of courses for on-demand learning, and facilitated blended learning in the design of customised learning solutions.

As a common gateway to knowledge repositories in the Bank, the Kijang.net has significantly improved knowledge visibility, accessibility, and ultimately, knowledge sharing. New capabilities were introduced in Kijang.net, such as the enterprise search, personalisation and collaborative tools, all of which enhance the prospects for further improvement in knowledge management practices in the Bank. The Kijang.net also facilitates collaborative work among users, Bank's ability to reach and interact with stakeholders, linkages to external knowledge repositories, and process flow management.

Following the rollout of the Kijang.net, the next stage of enterprise portal development would focus on content management, with the ultimate objective of putting in place a robust decision-making and learning support system. The Bank had adopted a comprehensive Content Management Policy that, among others, mandates departments to contribute contents to the Bank's Knowledge Hub. The policies and practices are aimed at developing systematic identification, capture, sharing and storage of Bank's knowledge assets, to allow greater degrees of knowledge re-use for decision-making, and collaborative learning. Archival policies and processes were revamped to effectively build up knowledge repositories and encourage re-use of the Bank's knowledge assets.

The Knowledge Management Centre (KMC) continued to provide comprehensive and relevant resources in the form of physical collections and online information resources. The KMC also offered value-added services such as information scanning, information alerting and repackaging of information to meet specific needs of stakeholders, thus significantly reducing time-to-knowledge. Easy access to these information resources was made available via the Learning & Knowledge Portal within Kijang.net which was also launched in April 2008, as a one-stop access to information and learning services. The KMC also continued to enhance its product and service offerings in preparation to transform itself to a premier regional resource centre in central banking and Islamic finance.

To sustain performance in a dynamic and challenging environment, the Bank has long nurtured a culture of knowledge-sharing. Structurally, committee-based and team-based working groups in the Bank promotes knowledge sharing and collaborative learning. Specific effort is made to draw on the tacit knowledge of senior and experienced staff or subject matter experts from across the Bank by the establishment of a pool of resource persons in the Bank who actively participate in the Bank's learning programmes. By engaging leaders as teachers, promoting the use of collaborative or group-work technologies, and encouraging individuals' contribution to the Bank's Knowledge Hub, the knowledge sharing initiatives in the Bank demonstrated significant achievements during the year. To reinforce the learning and knowledge-sharing culture, the Bank also leveraged on new ideas and innovations in the design for physical space for learning and collaboration. High demand for innovative spaces at the KMC indicated a change of mindset towards informal learning, networking and collaboration in the Bank. Specially designed according to adult learning principles, these spaces function as places for group discussions, generation of ideas and personal research or reflection.

**Experience Sharing and Collaboration Programmes with External Agencies**

During 2008, the Bank expanded its efforts towards greater regional and international cooperation by establishing a new business unit known as Central Banking Services. The purpose is to more effectively manage and coordinate requests for experience sharing with other central banks. The Bank's initiatives in international technical cooperation aim to complement the on-going process of regional integration. The Bank received some 80 requests for technical assistance during the year, and had engagement with central bankers from Asia, Central Asia, the African continent and the Middle-East who visited the Bank to discuss a broad range of topics such as different aspects of monetary and financial system stability, Islamic finance, currency management, talent management and central bank modernisation. In achieving the Bank's aspirations as a regional centre of excellence in learning and knowledge management in central banking and financial services, the Bank had offered a series of International Learning Programmes which drew participation from central banks and supervisory agencies of 15 participating countries under the auspices of the Malaysian Government-sponsored Malaysian Technical Cooperation Programme (MTCP).

Two major programmes conducted during 2008 were the Banking Supervision Foundation Course and the Intermediate Central Banking Course. Apart from programmes offered under the umbrella of the MTCP and the ad-hoc training courses, the Bank also ran two Islamic Finance courses in collaboration with the Islamic Development Bank. The courses provided opportunities for international participants to observe opportunities in business and training available in Malaysia as an International Islamic Financial Centre. In addition, it also provided a learning platform for central bankers, Ministry of Finance officials and Securities Commission regulators to enhance their knowledge and skills in Islamic finance operations, Shariah and regulatory framework for an effective implementation of a resilient Islamic financial system.

**ICT Management**

Information and Communications Technology (ICT) continued to function as a key enabler to achieve the Bank's strategic outcomes. During 2008, the Bank embarked on initiatives to implement reliable ICT infrastructure that has the capacity to cater for future expansion while ensuring continuous operational excellence. These initiatives strategically position the Bank higher up in the external value chain, paving the way for a standard platform that allows for nationwide data exchange between the Bank and its stakeholders in the financial sector and the related government agencies. An important milestone in the Bank's technology roadmap was the successful implementation of the New Wide Area Network Infrastructure (NWI). NWI is a secure, high-capacity communication network between the Bank and its stakeholders. This network serves as the enabling infrastructure for many industry-wide ICT systems. The first business process to successfully leverage on this infrastructure is Sistem Penjelasan Imej Cek Kebangsaan Secara Electronik (eSPICK), implemented in June 2008. eSPICK eliminates the handling of physical cheques, resulting in a fully automated, efficient and timely clearing process. Other key ICT systems that leverage on NWI include statistical submission systems, bond issuance system, securities custodian system, funds transfer system, depository system and regulatory services system.

In promoting the development of the capital market, the Bank, in collaboration with Bursa Malaysia, established a link between the Bank's bond issuance system (FAST) with Bursa's Electronic Trading Platform (ETP). This link allows for exchange of primary and secondary market information in real-time to facilitate primary bond issuance at the Bank and secondary bond market trading at Bursa. The Bank had also successfully implemented changes to the Electronic Scripless Securities Trading System (eSSTS) to facilitate the issuance of Bon Simpanan Merdeka (BSM) 2008. This implementation had enabled the first scripless BSM issuance, replacing the bond certificates used in previous issuance. In addition, a link to Jabatan Pendaftaran Negara's (JPN) identity card validation system was leveraged to ensure the correctness and integrity of bond applications from senior citizens. The Bank's public delivery system was enhanced with the deployment of the Integrated Contact Centre (ICC) system that improves the responsiveness to enquiries and complaints by members of the public. This system provides the Bank with a single view of all enquiries and complaints made by the individual, associations and private sector organisations, hence enabling end-to-end process of managing the enquiries and resolving complaints.

To ensure sustained excellence in providing ICT facilities and services, the construction work for a new Data Centre had begun in 2008. The operationalisation of the Data Centre will take place in the year 2009, with the objective of providing the Bank with a scaleable, resilient and secure ICT environment that supports a high-performance workplace.

**Risk Management**

Risk management remains one of the Bank's strategic priorities to support better decision-making by providing greater insight into the nature of risks that may impede the Bank's overall strategies and objectives. Sound risk management leads to the development of effective strategies to manage performance and results, reinforces transparency and accountability and provides reasonable assurance to Management and Board on the achievement of the Bank's objectives.

In 2008, the Bank introduced significant changes to its existing Enterprise Risk Management (ERM) system. The main objective of ERM is to embed risk management in all areas of strategic initiatives, policy-making and operations of the Bank. The implementation of ERM establishes more robust oversight, controls and disciplines to drive continuous improvement in the Bank's risk management capabilities.

The Risk Management function of the Bank is primarily driven by the Risk Management Committee (RMC) chaired by the Governor, which oversees and ensures the effective management of risks in the Bank. It is the leading forum for focused and regular deliberation of organisational risks. The RMC provides direction and value-added input to enable early identification of risks and prompt remedial actions as well as to ensure that appropriate risk management practices are embedded in the Bank's strategic initiatives, policy formulation and operations. The RMC is further supported by two sub-committees, namely the Financial Risk Management Committee (FRMC) and the Operational Risk Management Committee (ORMC) each headed by a designated Deputy Governor. The two sub-committees provided important platforms to assist the RMC in identifying and converging risk issues associated to financial and operational areas and in providing adequate support through in-depth analysis and forward-looking recommendations.

The Risk Management Unit (RMU) is responsible to manage and maintain the ERM framework which encapsulates the development of policies and processes, tools and methodologies as well as promoting risk management best practices. The RMU oversees the operationalisation of the framework and ensures all elements in the framework are functioning as intended. In addition, RMU facilitates line departments in identifying, assessing, measuring and interpreting their risk exposures. It gives an independent view of high and significant risks from the Bank's perspective and provides reasonable assurance to the management that these risks are being managed accordingly.

The RMC in 2008 approved a revised ERM framework to enhance the governance structure, create more robust risk management processes and provide greater clarity in roles and responsibilities. The risk taxonomy was also further refined to ensure consistent usage of common risk language across the Bank and to facilitate better risk categorisation and treatment for Bank-wide risk consolidation. To inculcate good risk management culture, collaboration with line departments in dealing with risk management was further enhanced to create better awareness of best practices. Greater appreciation of risk management was achieved through the validation of the risk issues with line departments and regular communication with line departments on the decisions made by oversight committees on key risk issues. In addition to communication of critical information essential for effective decision-making, these collaboration efforts promoted sharing of lessons learnt across the Bank.

Reputation risk, as in all central banks, is an important risk that the Bank has to manage. It is defined as risk that is associated with real or perceived loss of stature, credibility and effectiveness as a result of negative publicity arising from failure to comply with applicable laws or in managing risk, lack of fulfillment of roles and objectives or other external events. Ensuring adequate oversight of the Bank's reputation risk would also ensure better management of organisational risks. In 2008, sector based discussions, with technical support and facilitations by RMU, were used to identify key sources of reputation risk which were used as input to permit dynamic discussions and monitoring at the highest level, the RMC. The discussions on reputation risk was a valuable tool for top-down assessments and with the greater commitment and cross consultations shown through the increased participation of senior management from relevant sectors, these sessions have become increasingly important to highlight, identify and effectively address key organisational risks.

Another vital component of Risk Management is the self-assessment process which not only establishes accountability but is a bottom-up assessment which enables a more detailed risk profile, integrating business area and process perspectives. To improve the self-assessment process further in the Bank, a bank-wide survey was conducted to gauge the level of effectiveness of the risk management tools, and in particular the Risk Control Self Assessment (RCSA). Taking into account the feedback received from the RCSA survey, the Bank strengthened its risk management process by conducting facilitated risk management workshops with line departments to ensure continuity and follow-through in the process. The risk assessment of what risks remain since the last declaration in 2007 was also used to ensure a more focused discussion on areas of concern and as a foundation to develop the 2008 Bank-wide risk profile. This was also done to alleviate undue administrative burden from the administrating of the RCSA. Results of the bottom-up assessment will be used as another building block for a top-down assessment to seek senior management's perspectives in ascertaining the risk level as well as the inter-linkages across the Bank. In developing a periodic consolidated and robust corporate risk profile of the organisation, the risks identified from the top-down and bottom-up assessment will be aggregated, linked to the organisational objectives and performance and subsequently used to formulate an enterprise-wide risk strategy.

Throughout the years, one key observation reflecting positive and encouraging progress in relation to organisation risk awareness is the increased regularity of references made to risk management in strategic dialogues, decision-making forums across the Bank and better usage of self-assessment tools. In 2008, the increased level of commitment to risk management was apparent through the full cooperation and active participation of departments in the facilitated self-assessment workshops. The submission of departments' risk assessment were completed in a more comprehensive and timely manner. The requirement for upward reporting to respective Assistant Governors remained unchanged in providing direction for addressing risk issues as well as to enable continued intermediation in managing potential risks facing the Bank. In managing risks for various projects and initiatives throughout the Bank, regular consultations by departments were held to seek independent views and technical assistance. Greater executive sponsorship in setting the right tone through continuous promotion of risk management culture and integration of risk management in the decision-making process had also contributed to the raised level of risk awareness in the Bank.

Another category of risks is strategic risks, which are risks associated with the formulation and execution of business plans and strategies and non-achievement of strategic aims and objectives of the Bank. The integration of risk management with the strategic planning framework remained an important priority to ensure that the Bank's strategic results are achieved. Thus, strategic risk was placed as one of the specific areas under the purview of the RMC. Other governance structures such as Management Committees, and Steering Committees chaired by Senior Management are also in place to encourage active management of strategic risks and initiatives undertaken by the Bank.

The core functions of the Bank are in formulating and implementing policies to promote monetary and financial stability in the country. The resources, processes and activities directed at achieving these objectives give rise to policy risks, which mostly relate to policy contents as well as policy execution. To ensure the robustness of the policy-making mechanism in the Bank, a policy risk and implementation framework was put in place. This framework covers the end-to-end process for discussion and deliberation of all issues related to policy development and implementation. The high level committees that preside over policy-making in the Bank are the Monetary Policy Committee, the Financial Stability Committee and Management Committee. Chaired by the Governor, the objectives of these committees are to provide a platform for high level cross functional deliberation to ensure sound and efficacious policies. In supporting the high level committees, the Policy Working Groups chaired by Assistant Governors represent the working level deliberations on policy issues which ensure that all information and expertise are tapped in the design and formulation of policies.

The management of financial risk in the Bank has been enhanced in the year with the establishment of the FRMC. The Committee focused on the monitoring and reporting of the sustainability of income to support the Bank's operations, the management of financial exposures and commitments to external parties and provided an oversight function on key financial risk management processes.

An independent section (Treasury Risk Management) in the Investment Operations and Financial Market Department is responsible to assess the treasury risk of the Bank and to enforce the Bank's treasury risk management policy with direct reporting to the Deputy Governor. The treasury risk management policy defines the risk parameters for market risk exposures and provides effective risk control by quantifying the risk limits under which the Bank should conduct its investment activities. In line with market best practice and advancement in IT, the Bank continues to upgrade and update its risk methodology and framework to ensure robust risk coverage on all investment of the foreign reserves. During the course of 2008, a more efficient risk management system was implemented which enabled more up-to-date and comprehensive risk information to be escalated to the Management, thus enabling more responsive investment decisions in an increasingly challenging market environment. In addition, abilities to perform stress-testing and multiple scenario analyses with minimum effort, were developed.

The credit risk exposures from treasury operations of the Bank remained low throughout the year. These exposures are confined to risk on deposits with international financial institutions and counterparty exposure in execution of investment transactions. Stringent credit risk controls are in place and will continue to be implemented through rigorous credit assessment utilising credit scoring models and external ratings assessment, as well as a range of credit limits encompassing all aspects of potential and actual exposure.

In its day-to-day operations, robust management of the Bank's operational risk is imperative to manage losses arising from inadequate systems, lapses in internal controls and procedures, human errors and external events. In ensuring operational risks are well managed and amalgamated in the day-to-day operations, efforts were directed by departments towards developing detailed procedure manuals and ensuring amongst others, that dual control systems, clear roles and responsibilities and separation of incompatible duties, are in place and embedded in departmental processes. Key measures at an organisational level to address operational risks include effective budgetary controls, a sound procurement framework and a robust internal audit function, which plays a crucial role in monitoring operational risk. In an effort to continuously enhance risk management and internal controls in the Bank, the ORMC was established to oversee the operational risk issues in the Bank. In 2008, ORMC deliberated on significant risk issues affecting controls, efficiency and effectiveness of the Bank's operations with specific focus on areas with high financial impact, high rate of incidence and new processes which may give rise to new risks. Operational risk management also remained an important focus for treasury operations given the reserve size and expanded asset classes as well as activities in a more complex financial market. A newly implemented online operational incident logging system was used to identify and monitor key risk indicators for treasury activities.

In 2008, the Bank continued to strengthen the readiness and response capabilities of departments to business disruptions. The Bank's business continuity management (BCM) framework is aimed at containing any threats of disruptions to monetary and financial system stability whether through physical disruptions (e.g. systems breakdown) or non-physical disruptions (e.g. financial crisis) and providing for safety of Bank's staff and protection of Bank's assets. The RMC which also governs the Bank's BCM activities, policies and practices, approved the formation of the Financial Stability Disruption Crisis Management Committee in addition to the existing Crisis Management Team. The Financial Stability Disruption Crisis Management Committee is responsible for the management of financial crisis with potential systemic implications while the existing Crisis Management Team is responsible for managing operational disruptions which have implications to the Bank's services and physical infrastructure comprising buildings, people and systems.

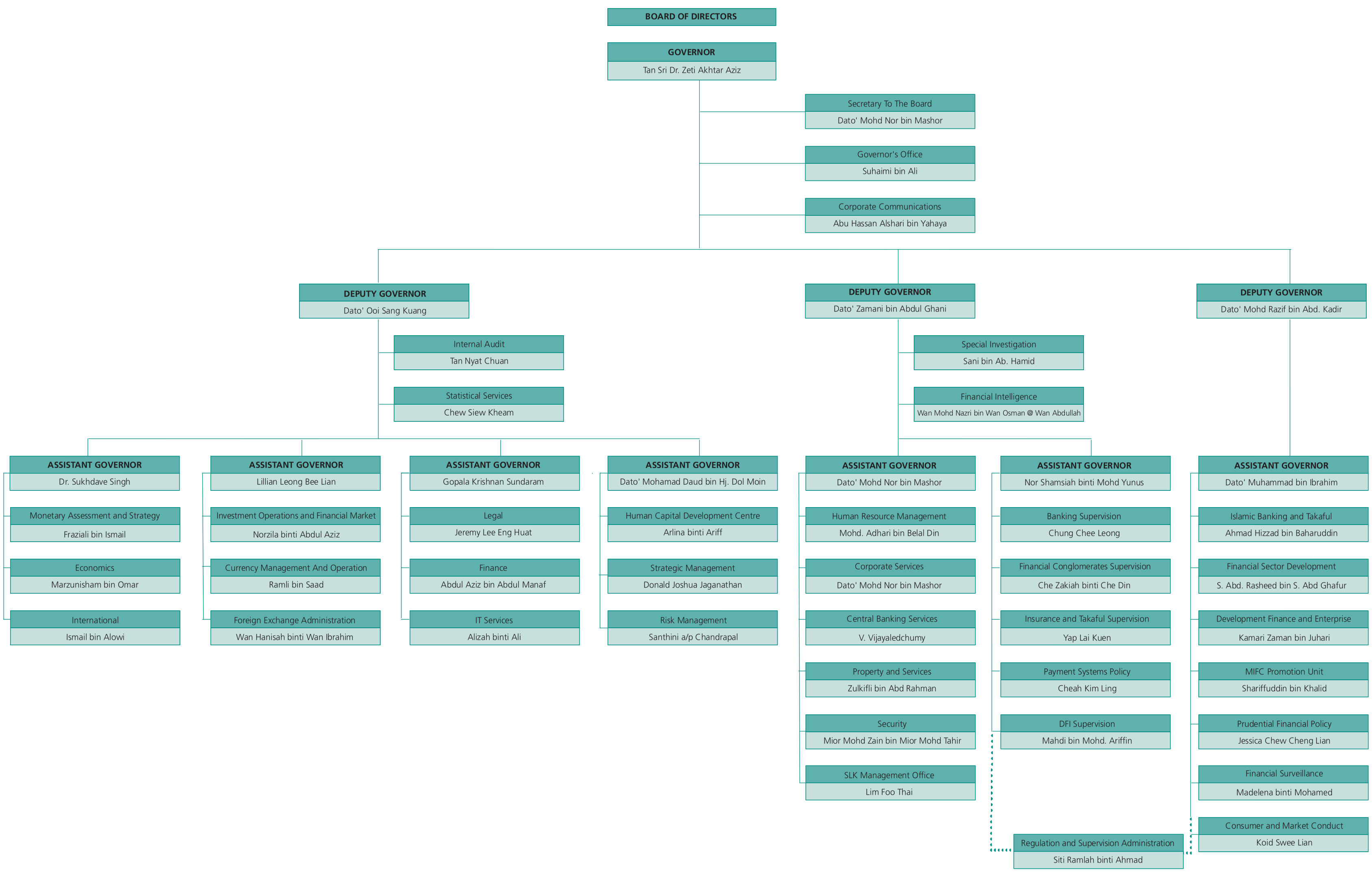
In the light of the crisis and disruptions arising in other parts of the globe throughout 2008, the urgent need for a heightened state of preparedness in dealing with and managing crisis, was recognised. To assess the readiness of departments to accordingly respond to and manage crisis, a desktop simulation exercise was conducted in September 2008 for the Crisis Management Team members, all heads of departments and BCM coordinators. The objectives of the simulation exercise were to enhance awareness as well as identify gaps in the recovery plan. During the desktop simulation, several possible scenarios of major disruptions were identified to ensure that departments are well prepared in responding to and managing different crisis conditions. Pursuant to the exercise, departments reviewed their Business Continuity Plan to ensure comprehensiveness and relevancy of their plan.

As in previous years, periodic assessments on the Recovery Centre's capability were conducted through the quarterly live run exercises. Assessments were conducted to evaluate system readiness and ability of the staff involved to respond accordingly to crisis situations. Several initiatives were introduced to enhance the live run process including implementation of severity ranking in evaluating incidences during the exercise. In ensuring that the live run exercises achieved its objectives, pre-engagement with all critical departments were carried out and results of the exercises were communicated to the Crisis Management Team and departments.

Another significant development in the year was the upgrading of the Bank's Recovery Centre which is aimed at enhancing the existing infrastructure towards a full fledged Business Recovery Centre. A study was undertaken to upgrade the Bank's back-up facility which includes reviews of the space requirement in any crisis situation to accommodate all departments in the Recovery Centre. The business impact analysis, formed the basis for reviewing the existing recovery centre infrastructure to ensure adequate investment is made to upgrade the recovery centre in terms of logistics and technology arrangements.

In an effort to streamline the understanding of the departments on BCM methodology and principles, a generic guide for operational crisis was developed which summarised all the salient requirements and pertinent information from the Bank's BCM Plan. This generic guide serves to provide easy reference on BCM and promote greater cooperation for coordinated bank-wide arrangements in handling and managing future crisis.

## BANK NEGARA MALAYSIA
## Organisation Structure



# Annual Financial Statements

# CERTIFICATE OF THE AUDITOR GENERAL ON THE FINANCIAL STATEMENTS OF BANK NEGARA MALAYSIA FOR THE YEAR ENDED 31 DECEMBER 2008

I have audited the financial statements of Bank Negara Malaysia for the year ended 31 December 2008. These financial statements are the responsibility of the management. My responsibility is to express an opinion on these financial statements based on my audit.

2. The audit has been conducted in accordance with the Audit Act 1957 and in conformity with approved auditing standards. Those standards require the audit be planned and performed to obtain reasonable assurance whether the financial statements are free of material misstatement. This audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. Evaluation is also made on the accounting principles used and the overall financial statements presentation.

3. In my opinion, the financial statements give a true and fair view of the financial position of Bank Negara Malaysia as at 31 December 2008 and of the results of its operations for the year then ended in accordance with approved accounting standards.

**(TAN SRI DATO' SETIA HAJI AMBRIN BIN BUANG)**
AUDITOR GENERAL
MALAYSIA

PUTRAJAYA
10 MARCH 2009

# STATEMENT BY CHAIRMAN AND ONE OF THE DIRECTORS

We, Zeti Akhtar Aziz and Oh Siew Nam, being the Chairman and one of the Directors of Bank Negara Malaysia, do hereby state that in the opinion of the Board, the financial statements are drawn up so as to give a true and fair view of the state of affairs of Bank Negara Malaysia as at 31 December 2008 and of the results of operations for the year ended on that date.

On behalf of the Board,

**ZETI AKHTAR AZIZ**
CHAIRMAN

6 MARCH 2009
KUALA LUMPUR

On behalf of the Board,

**OH SIEW NAM**
DIRECTOR

6 MARCH 2009
KUALA LUMPUR

# DECLARATION BY THE OFFICER PRIMARILY RESPONSIBLE FOR THE FINANCIAL MANAGEMENT OF BANK NEGARA MALAYSIA

I, Abdul Aziz Abdul Manaf being the officer primarily responsible for the financial management of Bank Negara Malaysia, do solemnly and sincerely declare that the financial statements, are to the best of my knowledge and belief, correct and I make this solemn declaration conscientiously believing the same to be true and by virtue of the provisions of the Statutory Declarations Act, 1960.

Subscribed and solemnly declared )
by the abovenamed at Kuala Lumpur )
this 6 March 2009. )

PESURUHJAYA SUMPAH
No: W 027
Nama : NG LEONG HUAT
MALAYSIA

Before me,

LEE HISHAMMUDDIN ALLEN & GLEDHILL
Level 16, Menara TM Asia Life
189, Jalan Tun Razak
50400 Kuala Lumpur
Tel : 603-2161 2330
Fax : 603-2161 3933

## Bank Negara Malaysia

**Balance Sheet as at 31 December 2008**

| | Note | 2008 RM | 2007 RM |
|---|---|---|---|
| **ASSETS** | | | |
| Gold and Foreign Exchange | 3 | 315,554,271,994 | 334,338,606,394 |
| International Monetary Fund Reserve Position | | 1,127,065,750 | 617,472,897 |
| Holdings of Special Drawing Rights | | 786,401,257 | 760,950,672 |
| Malaysian Government Papers | 4 | 2,525,239,300 | 2,468,203,632 |
| Deposits with Financial Institutions | 5 | 4,507,787,500 | 62,470,044,391 |
| Loans and Advances | 6 | 12,516,545,727 | 12,288,159,901 |
| Other Assets | 7 | 7,505,008,921 | 11,937,972,319 |
| **Total Assets** | | **344,522,320,449** | **424,881,410,206** |
| **LIABILITIES AND CAPITAL** | | | |
| Currency in Circulation | | 48,042,855,068 | 42,192,729,256 |
| Deposits by: Financial Institutions | | 184,136,298,017 | 231,591,665,147 |
| Federal Government | | 11,155,942,757 | 14,274,462,010 |
| Others | 8 | 373,848,344 | 2,819,726,945 |
| Bank Negara Papers | | 43,710,213,247 | 69,009,960,464 |
| Allocation of Special Drawing Rights | 9 | 742,639,517 | 726,822,946 |
| Other Liabilities | 10 | 24,604,565,308 | 34,518,924,334 |
| Total Liabilities | | 312,766,362,258 | 395,134,291,102 |
| Authorised Capital RM200,000,000 | | | |
| Paid-up Capital | 11 | 100,000,000 | 100,000,000 |
| General Reserve Fund | 12 | 11,976,653,686 | 10,799,678,929 |
| Other Reserves | 13 | 19,679,304,505 | 18,847,440,175 |
| Total Capital | | 31,755,958,191 | 29,747,119,104 |
| **Total Liabilities and Capital** | | **344,522,320,449** | **424,881,410,206** |

*Notes on the following pages form part of these financial statements.*

# Bank Negara Malaysia

## Income Statement for the Year Ended 31 December 2008

| | Note | 2008 RM | 2007 RM |
|---|---|---|---|
| **Total Income** | 14 | **8,158,398,385** | **8,489,814,550** |
| Less: | | | |
| Recurring Expenditure | 15 | 939,599,724 | 834,185,691 |
| Development Expenditure | 16 | 709,518,486 | 994,993,036 |
| **Total Expenditure** | | **1,649,118,210** | **1,829,178,727** |
| **Net Profit** | | **6,509,280,175** | **6,660,635,823** |

## Profit and Loss Appropriation Statement for the Year Ended 31 December 2008

| | | 2008 RM | 2007 RM |
|---|---|---|---|
| **Net Profit** | | **6,509,280,175** | **6,660,635,823** |
| Transfer to Other Reserves | 17 | 3,832,305,418 | 3,723,507,115 |
| Transfer to General Reserve Fund | | 1,176,974,757 | 1,437,128,708 |
| Amount Payable to Federal Government | | 1,500,000,000 | 1,500,000,000 |
| | | **6,509,280,175** | **6,660,635,823** |

*Notes on the following pages form part of these financial statements.*

# Notes to the Financial Statements - 31 December 2008

1. **Principal Activities of the Bank**

The Bank's principal roles and responsibilities are as follows:
(a) to achieve monetary stability;
(b) to promote a stable financial system;
(c) to ensure an efficient payment system;
(d) to issue currency in Malaysia; and
(e) to act as a banker and a financial adviser to the Federal Government.

2. **Accounting Policies**

The principal accounting policies applied in the preparation of these financial statements are set out below. These accounting policies are consistently applied to both of the financial years presented, unless otherwise stated.

2.1 **Basis of Preparation of Financial Statements**

(a) These financial statements have been prepared in accordance with the Central Bank of Malaysia Act 1958 (Revised 1994) and applicable Malaysian Financial Reporting Standards (FRS) in as far as it is considered appropriate to the roles and responsibilities of the Bank. The Bank, having considered its responsibilities for the formulation and conduct of effective monetary policy, is of the opinion that, it is appropriate to differ, in some aspects, from the Malaysian FRS.

(b) The preparation of the financial statements in conformity with the requirements of the Malaysian FRS requires management to use certain estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of income and expenses during the financial year. Although these estimates are based on the management's best knowledge of current events and actions, the actual results could differ from those estimates.

2.2 **Measurement Base and Accrual Accounting**

The financial statements have been prepared on the historical cost basis of accounting, with the revaluation of financial instruments that are held at fair value through profit and loss and on an accrual basis.

2.3 **Foreign Currency Translation**

(a) The financial statements have been prepared using Ringgit Malaysia, the currency of the primary economic environment in which the Bank operates.

(b) Assets and liabilities in foreign currencies have been revalued into Ringgit Malaysia at rates of exchange prevailing on the balance sheet date. Transactions in foreign currencies during the year have been translated into Ringgit Malaysia at rates of exchange prevailing on the value dates.

(c) The International Reserves comprising Gold and Foreign Exchange, International Monetary Fund Reserve Position and Holdings of Special Drawing Rights as at 31 December 2008 was RM317,467.7 million equivalent to USD91,536 million.

2.4 **Gold, Securities and Investments**
Gold, securities and investments are stated mainly at cost and provisions have been made for diminution in value as at 31 December 2008.

2.5 **Repurchase and Reverse-Repurchase Agreements**
The amount borrowed under repurchase agreements is reported under `Other Liabilities´. The amount lent under reverse-repurchase agreements is reported under `Other Assets´. The difference between the amount received and amount paid under repurchase and reverse-repurchase agreements is recognised as interest expense and interest income on a straight-line basis, respectively.

2.6 **Net Profit**
The net profit of the Bank has been appropriated in accordance with section 7 of the Central Bank of Malaysia Act 1958 and only realised gains are made available for dividend distribution.

3. **Gold and Foreign Exchange**

| | **2008** | **2007** |
|---|---|---|
| | **RM** | **RM** |
| Foreign Securities | 282,566,246,554 | 239,672,351,872 |
| Foreign Deposits | 10,860,543,730 | 68,159,741,976 |
| Balances with Other Central Banks, Bank for International Settlements (BIS) and International Monetary Fund (IMF) | 3,592,893,233 | 6,603,359,274 |
| Others | 18,534,588,477 | 19,903,153,272 |
| | 315,554,271,994 | 334,338,606,394 |

4. **Malaysian Government Papers**

| | **2008** | **2007** |
|---|---|---|
| | **RM** | **RM** |
| Malaysian Government Securities | 2,525,239,300 | 2,468,203,632 |

5. **Deposits with Financial Institutions**
Deposits with Financial Institutions comprise deposits placed by the Bank with financial institutions under section 30(1)(nn) and section 31B of the Central Bank of Malaysia Act 1958.

6. **Loans and Advances**
Loans and advances comprise mainly advances extended by the Bank to the participating institutions under section 30(1) of the Central Bank of Malaysia Act 1958.

7. **Other Assets**
Other assets include investments in shares and bonds of RM7,107,102,191 acquired under section 30(1)(j) and section 30(1)(oo)(i) of the Central Bank of Malaysia Act 1958.

8. **Deposits by Others**
A substantial part of these deposits comprises deposits from Federal Statutory Authorities.

9. **Allocation of Special Drawing Rights**
IMF member countries are allocated Special Drawing Rights (SDR) in proportion to their subscription to the IMF. The allocation represents a dormant liability of the Bank to the IMF, against which assets are received in SDR from the IMF. The net cumulation of the allocation was RM742,639,517 equivalent to SDR139,048,000.

10. **Other Liabilities**
Other liabilities include mainly placements by financial institutions under the repurchase agreements.

11. **Paid-up Capital**
The entire issued and paid-up capital of RM100 million is owned by the Government of Malaysia.

12. **General Reserve Fund**

| | **2008** | **2007** |
|---|---|---|
| | **RM** | **RM** |
| As at 1 January | 10,799,678,929 | 9,362,550,221 |
| Transfer from Net Profit | 1,176,974,757 | 1,437,128,708 |
| As at 31 December | 11,976,653,686 | 10,799,678,929 |

13. **Other Reserves**
Other reserves comprise the Exchange Rate Fluctuation Reserve, Revaluation Reserve and the Contingency Reserve.

14. **Total Income**
Total income comprises revenue from foreign reserve management which includes interest and dividends, non-treasury income and is stated at net of amortisation/accretion of premiums/discounts and the monetary policy cost.

15. **Recurring Expenditure**
Recurring expenditure are expenses incurred in the management and administration of the day-to-day operations of the Bank.

16. **Development Expenditure**
Development expenditure are expenses incurred mainly to finance developmental and long term projects undertaken by the Bank that are in line with its principal roles and responsibilities.

17. **Transfer to Other Reserves**
This transfer is made in accordance with section 7(2) of the Central Bank of Malaysia Act 1958 and note 2.6.

18. **Contingent Liabilities**

Total contingent liabilities as at 31 December 2008 amounted to RM6,944,979,130. These comprise:

(a) an amount of RM6,880,487,932 which represents the obligation of the Bank to pay in full, in SDR or other convertible currencies, the amount of Malaysia's quota in the IMF under the Articles of Agreement; and

(b) an amount of RM64,491,198 which represents the uncalled portion of the 3,220 units of shares held by the Bank in Bank for International Settlements. The amount is based on the nominal value (SDR5,000) of the uncalled portion and SDR rate as at the balance sheet date.

19. **Income Tax**

The Bank is exempted from payment of income tax and supplementary income tax as set out in the Income Tax (Exemption) (No. 7) Order 1989.

# Annex

# Contents

# Foreign Exchange Administration Policies

Malaysia continues to maintain a liberal foreign exchange administration policy. The remaining foreign exchange administration rules are mainly prudential safeguards to support the overall macroeconomic objective of maintaining financial and economic stability.

## I. DEFINITIONS

**Non-residents:**
- Overseas branches, subsidiaries, regional offices, sales offices and representative offices of resident companies;
- Embassies, Consulates, High Commissions, supranational or international organisations recognised by the Government of Malaysia; or
- Malaysian citizens who have obtained permanent resident status of a territory outside Malaysia and are residing outside Malaysia.

**Residents:**
- Citizens of Malaysia (excluding persons who have obtained permanent resident status of a territory outside Malaysia and are residing abroad);
- Non-citizens who have obtained permanent resident status in Malaysia and are residing permanently in Malaysia; or
- Persons, whether body corporate or unincorporated, registered or approved by any authority in Malaysia.

**Ringgit assets** include:
- Ringgit-denominated securities including bills of exchange, private debt securities, Cagamas bonds or notes, Malaysian Government Securities, Treasury Bills, shares and warrants;
- Derivatives traded on Bursa Malaysia and OTC derivatives (excluding OTC derivatives and structured products which tantamount to lending or borrowing of ringgit between residents and non-residents);
- Fixed deposits and negotiable instruments of deposits denominated in ringgit;
- Immovable properties in Malaysia; and
- Other fixed assets in Malaysia.

**Foreign currency assets** include:
- Equity/portfolio investment abroad;
- Loans to non-residents;
- Foreign currency deposits onshore and offshore; and
- Investment in approved foreign currency products marketed by licensed onshore banks, licensed International Islamic Banks (licensed IIBs) and any residents permitted by the Controller of Foreign Exchange (the Controller).

**Domestic ringgit borrowings** refer to any ringgit advances, loans, trade financing facilities, hire purchase, factoring facilities with recourse, financial leasing facilities, guarantee for payment of goods, redeemable preference shares or similar facilities in whatever name or form, except:
- Trade credit terms extended by suppliers for all types of goods and services;
- Forward foreign exchange contracts entered into with licensed onshore banks;
- Performance guarantees and financial guarantees;
- One personal housing loan and one vehicle loan obtained from residents;
- Credit card and charge card facilities;
- Operational leasing facilities;
- Factoring facilities without recourse; and
- Inter-company borrowings within a corporate group in Malaysia.

## II. Foreign Exchange Administration Rules Applicable to NON-RESIDENTS

| FOREIGN DIRECT AND PORTFOLIO INVESTMENTS BY NON-RESIDENTS | |
|---|---|
| The foreign exchange administration rules support and facilitate non-residents' investments into Malaysia | |
| • Purchase of ringgit assets | • Free to purchase any ringgit assets including ringgit-denominated bonds/ sukuk issued by non-residents in Malaysia |
| • Sourcing ringgit for settlement of ringgit assets | • Ringgit for settlement of the investment can be sourced from:<br>✓ non-residents' own External Accounts[1];<br>✓ sale of foreign currency on spot or forward basis, with licensed onshore banks[2] or overseas branches appointed by licensed onshore banks; or<br>✓ onshore borrowing |
| • Onshore borrowing | • Free to borrow any amount in foreign currency from licensed onshore banks and licensed IIBs<br>• Free to borrow in ringgit of any amount from licensed onshore banks, resident companies[3] and individuals[4] to finance activities in the real sector in Malaysia, including financing the purchase of ringgit assets<br>• Free to borrow any amount for margin financing from resident stockbroking companies |
| • Divestment/ income from investment | • Free to repatriate funds from divestment of ringgit assets or profits/ dividends arising from the investments<br>• Repatriation, however, must be made in foreign currency other than the currency of Israel |
| • Hedging | • Free to hedge the exposure arising from investment in ringgit assets made on or after 1 April 2005 with licensed onshore banks or overseas branches appointed by the licensed onshore banks |
| **INVESTMENT IN IMMOVABLE PROPERTIES BY NON-RESIDENTS** | |
| • Purchase of immovable property | • Free to purchase residential and commercial properties in Malaysia<br>• Such purchase need only to comply with guidelines[5] issued by the Foreign Investment Committee of Malaysia. The details can be obtained at http://www.epu.jpm.my |
| • Onshore borrowing | • Free to borrow any amount to finance or refinance the purchase of residential and commercial properties in Malaysia, except for purchase of land only |
| **LENDING IN RINGGIT AND FOREIGN CURRENCY BY NON-RESIDENTS TO RESIDENTS** | |
| • Ringgit lending<br>✓ By non-resident non-bank parent companies[6] | • Free to lend any amount of ringgit to resident subsidiaries to finance activities in the real sector in Malaysia |

1 External Accounts are ringgit accounts maintained with licensed onshore banks by or for non-residents.
2 Licensed onshore banks refer to licensed commercial banks, licensed Islamic banks and licensed investment banks.
3 Resident companies include limited partnerships and entities other than companies such as co-operatives and charitable organisations.
4 Resident individuals include sole proprietorships, general partnerships and partnerships with general and limited partners.
5 (a) FIC's approval is not required for non-residents purchasing residential property exceeding RM250,000; and
(b) Non-residents under the "Malaysia My Second Home" Programme are exempted from any approval requirement.
6 A non-resident non-bank parent company refers to -
(a) a non-resident company with more than 50% shareholding in a resident company; or
(b) the ultimate non-resident parent company of the resident company, which is not a bank, an investment holding company owned by a bank or a stockbroking company.

<table>
<tr>
<td>✓ By other non-resident non-bank companies or individuals<br><br>• Foreign currency lending<br><br>✓ By non-resident non-bank parent companies<br><br>✓ By other non-resident non-bank companies or individuals</td>
<td>• Free to lend up to RM1 million in aggregate to resident companies and individuals for use in Malaysia<br><br>• Free to lend any amount in foreign currency to resident subsidiaries in Malaysia<br><br>• Free to lend in foreign currency to a resident provided the resident borrower’s total foreign currency borrowing does not exceed the following limits:
<table>
<tr><td>✓ Resident individual</td><td>RM10 million equivalent in aggregate</td></tr>
<tr><td>✓ Resident company</td><td>RM100 million equivalent in aggregate on a corporate group basis</td></tr>
</table>
• The onus is on the resident borrower to obtain the prior permission of the Controller for borrowing exceeding the limits</td>
</tr>
<tr>
<td colspan="2">BORROWING BY NON-RESIDENTS FROM RESIDENTS</td>
</tr>
<tr>
<td>• Foreign currency borrowing from licensed onshore banks and licensed IIBs<br><br>• Foreign currency borrowing from resident non-bank companies or individuals</td>
<td>• Free to borrow any amount of foreign currency from licensed onshore banks and licensed IIBs<br><br>• Free to obtain foreign currency borrowing from resident non-bank companies and individuals as follows:
<table>
<tr><th>Resident lender</th><th>Amount</th></tr>
<tr><td>A resident with no domestic ringgit borrowing</td><td>No limit</td></tr>
<tr><td>A resident, with or without domestic ringgit borrowing, using own foreign currency funds maintained onshore or offshore</td><td>No limit</td></tr>
<tr><td>A resident with domestic ringgit borrowing*:<br><br>✓ Resident individual<br><br>✓ Resident company</td><td>Through conversion of ringgit up to:<br><br>✓ RM1 million in aggregate per calendar year<br>✓ RM50 million in aggregate per calendar year on a corporate group basis</td></tr>
</table>
* Provided the resident lender’s total investment in foreign currency assets, including lending in foreign currency, does not exceed the limit.</td>
</tr>
</table>

| | |
|---|---|
| • Ringgit borrowing from licensed onshore banks, resident non-bank companies and individuals | • Free to obtain ringgit borrowing from licensed onshore banks, resident non-bank companies and individuals as follows:<br>✓ By non-resident (other than stockbrocking companies and banks) from licensed onshore banks, resident non-bank companies individuals to:<br>➢ finance activities in the real sector in Malaysia; and<br>➢ finance or refinance the purchase of residential and commercial properties in Malaysia<br>✓ By non-resident stockbrocking companies banks and banks from licensed onshore banks for settlement of ringgit securities on Bursa Malaysia and RENTAS due to inadvertent delays on the receipt of funds<br>✓ By non-resident (other than stockbrocking companies banks) from licensed onshore banks and resident stockbrocking companies for margin financing<br>✓ By non-resident individuals from resident insurance companies up to the cash surrender value of the insurance policies purchased by the non-residents |
| **ISSUANCE OF RINGGIT AND FOREIGN CURRENCY DENOMINATED BONDS/SUKUK IN MALAYSIA BY NON-RESIDENTS** | |
| • Issuance of ringgit or foreign currency denominated bonds/ sukuk | • Multilateral Development Banks, Multilateral Financial Institutions, foreign sovereign, foreign quasi-sovereign agencies and foreign multinational companies may issue ringgit or foreign currency denominated bonds/sukuk in Malaysia |
| • Utilisation of bond/sukuk proceeds | • Proceeds from the issuance of bonds/sukuk are allowed to be used onshore or offshore<br>• Ringgit-denominated bond/sukuk proceeds to be used offshore have to be converted into foreign currency with licensed onshore banks |
| • Hedging | • Issuers are free to hedge exchange rate and interest/profit rate exposure arising from the issuance of ringgit-denominated bonds/sukuk and any subsequent interest/profit and coupon payments with licensed onshore banks<br>• Non-resident investors of the bonds/sukuk are also free to hedge exchange rate and interest/profit rate exposure with licensed onshore banks |
| • Guidelines for issuance | • Specific details on guidelines as well as incentives for issuance of ringgit and foreign currency denominated bonds/sukuk in Malaysia can be obtained at any of the following website addresses:<br>✓ http://www.mifc.com<br>✓ http://www.bnm.gov.my/fxadmin<br>✓ http://www.sc.com.my |
| **HEDGING BY NON-RESIDENTS** | |
| • Hedging of ringgit assets | • Free to hedge with licensed onshore banks, exchange rate and interest rate exposures arising from investments in ringgit assets purchased on or after 1 April 2005 as well as ringgit-denominated bonds/sukuk issued in Malaysia by non-residents |

| OPENING OF RINGGIT AND FOREIGN CURRENCY ACCOUNTS IN MALAYSIA BY NON-RESIDENTS | |
|---|---|
| • Opening of ringgit and foreign currency accounts | • Free to open:<br>✓Ringgit accounts with licensed onshore banks; and<br>✓ Foreign currency accounts with licensed onshore banks and licensed IIBs<br>• The ringgit accounts maintained by non-residents with licensed onshore banks in Malaysia are termed as "External Accounts" |
| • Repatriation/utilisation of funds from the ringgit or foreign currency accounts | • **External Accounts**<br>✓Free to convert with licensed onshore banks for repatriation abroad<br>✓Free to pay a resident for any purpose, except for the following:<br>➢Payment for the import of goods and services;<br>➢Lending in ringgit to residents other than as permitted by the Controller; and<br>➢Payment on behalf of a third party<br>✓Free to pay in to another non-resident's External Account for settlement of purchase of ringgit assets<br><br>• **Foreign currency accounts**<br>✓Free to repatriate<br>✓Free to pay a resident for any purpose including for settlement of goods and services |
| **IMPORT AND EXPORT OF RINGGIT AND FOREIGN CURRENCY NOTES BY NON-RESIDENT TRAVELLERS** | |
| • Import and export of ringgit notes | • Allowed to import or export ringgit notes up to RM1,000 |
| • Import of foreign currency notes and traveller's cheques | • No limit |
| • Export of foreign currency notes and traveller's cheques | • Up to the amount brought into Malaysia or USD10,000, whichever is higher |
| • Declaration for import and export of foreign currency | • To declare to Immigration officer, if the total amount of foreign currency notes and traveller's cheques exceeds USD10,000, upon arrival at or departure from Malaysia |
| • Import and export of ringgit and foreign currency exceeding permitted limits | • Application can be made online, using Form 13 which can be obtained at http://www.bnm.gov.my/fxadmin, or submitted via written application to Foreign Exchange Administration Department, Bank Negara Malaysia<br>• Response is given within one day from receipt of application with complete information |

### III. Foreign Exchange Administration Rules Applicable to RESIDENTS

<table>
<tr><th colspan="2">INVESTMENTS IN FOREIGN CURRENCY ASSETS BY RESIDENTS</th></tr>
<tr><td colspan="2">The current limits for investment in foreign currency assets are applicable only to residents that have domestic ringgit borrowing and are converting ringgit into foreign currency to invest in foreign currency assets</td></tr>
<tr><td>• Investment in foreign currency assets</td><td>• No limit for residents without domestic ringgit borrowing<br>• Residents with domestic ringgit borrowing are allowed to invest as follows:
<table>
<tr><td>✓ Resident individuals[7]</td><td>• No limit if funded by own foreign currency funds retained onshore or offshore;<br>• Up to full amount of approved foreign currency borrowing; and<br>• Up to RM1 million in aggregate per calendar year if from conversion of ringgit</td></tr>
<tr><td>✓ Resident companies[8]</td><td>• No limit if funded with own foreign currency funds retained onshore or offshore;<br>• No limit if funded from proceeds of listing through initial public offering on:<br>- the Main Board of Bursa Malaysia; or<br>- foreign stock exchanges<br>• Up to RM50 million equivalent in aggregate on a corporate group basis per calendar year if from conversion of ringgit; and<br>• Up to the full amount of approved foreign currency borrowing</td></tr>
</table></td></tr>
<tr><td>• Investment in foreign currency assets by resident institutional investors<br>✓ Unit trust management companies<br>✓ Fund management companies<br>✓ Insurers and takaful operators</td><td>• Unit trust mangement companies:<br>✓ Investment of Islamic funds<br>➢No limit<br>✓ Investment of conventional funds<br>Foreign currency-denominated funds<br>➢100% of the net asset value (NAV)<br>Ringgit-denominated funds<br>➢100% of NAV attributed to non-residents and residents without domestic ringgit borrowing; and<br>➢50% of NAV attributed to residents with domestic ringgit borrowing<br>• Fund management companies:<br>✓ Funds mandated to be invested in Shariah-compliant assets<br>➢No limit</td></tr>
</table>

[7] Resident individuals include sole proprietorships, general partnerships and partnerships with general and limited partners.
[8] Resident companies include limited partnerships and entities other than companies such as co-operatives and charitable organisations.

| | |
|---|---|
| | ✓ Funds mandated to be invested in non Shariah-compliant assets<br>**Foreign currency-denominated funds**<br>➢ No limit<br>**Ringgit-denominated funds**<br>➢ 100% of total funds managed for non-residents and residents without domestic ringgit borrowing; and<br>➢ 50% of total funds managed for residents with domestic ringgit borrowing<br>• Insurers and takaful operators, including international currency business unit of takaful operators and international takaful operators:<br>**Foreign currency-denominated funds**<br>➢ 100% of NAV of foreign currency investment-linked funds marketed to residents and non-residents<br>**Ringgit-denominated funds**<br>➢ 100% of NAV of investment-linked funds marketed to non-residents and residents without domestic ringgit borrowing;<br>➢ 50% of NAV of investment-linked funds marketed to residents with domestic ringgit borrowing;<br>➢ 10% of margin of solvency for insurers; and<br>➢ 5% of total assets for takaful operators |
| • Payment for purchase of foreign currency assets | • Offshore foreign currency assets<br>✓ Payment must be made in foreign currency other than the currency of Israel<br>✓ The foreign currency may be sourced from conversion of ringgit with licensed onshore banks[9], or own foreign currency funds<br>• Onshore foreign currency assets offered by licensed onshore banks, licensed IIBs or entities[10] approved by the Controller:<br>✓ Payment may be in foreign currency or ringgit |
| • Divestment/income from investment in foreign currency assets | • Free to repatriate and convert divestment proceeds or income from investment in foreign currency assets into ringgit<br>• Free to retain the proceeds in foreign currency accounts |
| • Hedging | • Free to hedge with licensed onshore banks and licensed IIBs for investment in foreign currency assets based on firm underlying commitment<br>• Hedging involving ringgit shall only be undertaken with licensed onshore banks |
| **BORROWING IN FOREIGN CURRENCY AND RINGGIT BY RESIDENTS** | |
| • Foreign currency borrowing by: | |
| ✓ Resident individuals | • Free to borrow in foreign currency up to the equivalent of RM10 million in aggregate from:<br>✓ Licensed onshore banks;<br>✓ Licensed IIBs; and<br>✓ Non-residents<br>• Trade financing involving export shall only be obtained from licensed onshore banks<br>• Allowed to refinance outstanding approved foreign currency borrowing (principal and accrued interest) |

[9] Licensed onshore banks refer to licensed commercial banks, licensed Islamic banks and licensed investment banks.
[10] Example: (a) Unit trust companies offering foreign currency unit trust funds.
(b) Bursa Malaysia for trading of foreign currency derivative products such as CPO futures.

| | |
|---|---|
| ✓ Resident companies | • Free to borrow any amount in foreign currency from:<br>✓ Non-resident non-bank parent companies[11];<br>✓ Other resident companies within the same corporate group[12] in Malaysia;<br>✓ Licensed onshore banks; and<br>✓ Licensed IIBs<br>• Free to borrow in foreign currency up to the equivalent of RM100 million in aggregate on a corporate group basis:<br>✓ From other non-residents (other than non-resident non-bank parent companies); and<br>✓ Through the issuance of foreign currency denominated bonds onshore and offshore<br>• Free to borrow any amount of foreign currency supplier's credit for capital goods from non-resident suppliers<br>• Allowed to refinance outstanding approved foreign currency borrowing (principal and accrued interest) |
| • Proceeds from offshore listing | • Free to borrow from other resident companies within the same corporate group in Malaysia, the foreign currency proceeds from the listing on foreign stock exchanges |
| • Foreign currency trade financing facilities | • Free to obtain foreign currency trade financing facilities from licensed onshore banks and licensed IIBs<br>• Allowed to obtain foreign currency trade financing facilities from offshore up to the equivalent of RM5 million in aggregate. The trade financing facilities are part of the RM100 million limit on foreign currency borrowing from non-residents<br>• Trade financing facilities for export of goods are to be obtained from licensed onshore banks only |
| • Repayment and prepayment | • Free to repay and prepay approved foreign currency borrowing |
| • Hedging | • Free to hedge drawdown and repayment of foreign currency borrowing with licensed onshore banks and licensed IIBs<br>• Hedging involving ringgit shall only be undertaken with licensed onshore banks |
| • Ringgit borrowing from non-residents by: | |
| ✓ Resident individuals | • Free to borrow up to RM1 million in aggregate from non-resident non-bank companies or individuals for use in Malaysia |
| ✓ Resident companies | • Free to borrow any amount in ringgit from their non-resident non-bank parent companies to finance activities in the real sector in Malaysia<br>• Free to borrow up to RM1 million in aggregate from other non-resident non-bank companies or individuals for use in Malaysia |

[11] Non-resident non-bank parent company refers to -
(a) a non-resident company with more than 50% shareholding in a resident company; or
(b) the ultimate parent company of the resident company, which is not a bank, an investment holding company owned by a bank or a stockbroking company.

[12] Corporate group refers to a group of companies with parent-subsidiary relationship in Malaysia.

| LENDING IN RINGGIT BY RESIDENTS | |
|---|---|
| • Ringgit lending by: | |
| ✓ Resident non-bank companies and individuals | • Free to lend any amount in ringgit to non-resident non-bank companies and individuals to:<br>✓ finance activities in the real sector in Malaysia; and<br>✓ finance or refinance the purchase of residential and commercial properties in Malaysia |
| ✓ Licensed onshore banks | • Free to lend any amount in ringgit to:<br>✓ non-resident non-bank companies and individuals (other than stockbroking companies and banks):<br>➢ to finance activities in the real sector in Malaysia;<br>➢ for margin financing; and<br>➢ to finance or refinance the purchase of residential and commercial properties in Malaysia<br>✓ non-resident stockbroking companies and banks for settlement of ringgit securities on Bursa Malaysia and RENTAS due to inadvertent delays on the receipt of funds |
| ✓ Resident stockbroking companies | • Free to provide margin financing of any amount in ringgit to non-resident non-bank companies and individuals for purchase of shares listed on Bursa Malaysia |
| ✓ Resident insurance companies | • Free to lend to non-resident individuals in ringgit up to the cash surrender value of the insurance policies purchased by the non-residents |
| **ISSUANCE OF RINGGIT AND FOREIGN CURRENCY DENOMINATED SECURITIES BY RESIDENTS** | |
| • Issuance of securities to non-residents | • Free to issue the following ringgit securities registered in Malaysia to non-residents:<br>✓ Ordinary shares, including bonus and rights issues;<br>✓ Irredeemable preference shares; and<br>✓ Private debt securities<br>• Prior permission is required for issuance of securities to non-residents other than as stated above |
| • Issuance of bonds/sukuk: | |
| ✓ Ringgit-denominated bonds/sukuk | • Free to issue in Malaysia |
| ✓ Foreign currency-denominated bonds/sukuk | • Allowed as long as total foreign currency borrowing, including the bonds/sukuk does not exceed RM100 million equivalent |

| | |
|---|---|
| • Utilisation of bond/sukuk proceeds: | |
| ✓ Ringgit-denominated bonds/sukuk | • Free to use onshore<br>• Free to use for investment in foreign currency assets provided the issuer's total investment does not exceed RM50 million equivalent in aggregate per calendar year |
| ✓ Foreign currency-denominated bonds/ sukuk | • Free to use onshore and offshore |
| • Guidelines for issuance | • Guidelines for issuance can be obtained at:<br>✓ http://www.mifc.com<br>✓ http://www.bnm.gov.my/fxadmin<br>✓ http://www.sc.com.my |
| **EXPORT AND IMPORT OF GOODS AND SERVICES BY RESIDENTS** | |
| • Currency for payment of import and export | • Payment must be made in foreign currency other than the currency of Israel |
| • Repatriation of export proceeds | • Must be repatriated to Malaysia in full as per the sales contract and not exceeding six months from the date of export<br>• Prior permission is required for residents to:<br>✓ Offset export proceeds against other payables due to non-residents; or<br>✓ Receive the export proceeds exceeding six months from date of export |
| • Retention of export proceeds | • Free to retain in foreign currency accounts and ringgit accounts with licensed onshore banks<br>• Prior permission is required to retain export proceeds in foreign currency accounts maintained with licensed IIBs or offshore banks |
| • Hedging | • Free to hedge with licensed onshore banks and licensed IIBs, payments or receipts for the import or export of goods and services:<br>✓ Based on firm underlying commitment; or<br>✓ On anticipatory basis up to the actual total amount paid or received in the preceding 12 months<br>• Hedging involving ringgit shall only be undertaken with licensed onshore banks |
| **OPENING OF FOREIGN CURRENCY ACCOUNTS (FCA) BY RESIDENTS** | |
| • Opening of FCA | • Free to open FCA with licensed onshore banks, licensed IIBs, licensed offshore banks in Labuan and overseas banks |
| • Sources of funds | • The FCA can be credited with foreign currency funds sourced:<br>✓ From conversion of ringgit with licensed onshore banks:<br>➢ No limit for residents without domestic ringgit borrowing;<br>➢ For residents with domestic ringgit borrowing, up to permitted limits for investment in foreign currency assets. Additional limits for overseas education and employment purposes:<br>- Up to USD150,000 with licensed onshore banks and licensed IIBs; |

| | |
|---|---|
| | - Up to USD150,000 with licensed offshore banks in Labuan; and<br>- Up to USD50,000 with overseas banks<br>✓ From other residents for permitted purposes; and<br>✓ From non-residents. Export proceeds, however, may be retained with licensed onshore banks only |
| • Opening of joint FCA | • Resident individuals are free to open joint foreign currency accounts for any purpose with other resident individuals<br>• Resident companies, however, require prior permission to open joint foreign currency accounts |
| **PAYMENT BETWEEN RESIDENTS** | |
| • Payment in ringgit | • No restriction |
| • Payment in foreign currency | • Resident companies with export earnings are free to pay other resident companies in foreign currency for settlement of goods and services |
| **HEDGING BY RESIDENTS** | |
| • Hedging of current account transactions | • Free to hedge with licensed onshore banks and licensed IIBs for payments and receipts for import and export of goods and services:<br>✓ Based on firm underlying commitment; or<br>✓ On anticipatory basis provided the amount hedged does not exceed the total amount paid or received in the preceding 12 months<br>• Hedging involving ringgit shall only be undertaken with licensed onshore banks |
| • Hedging of capital account transactions | • Free to hedge with licensed onshore banks and licensed IIBs based on committed capital inflows or outflows<br>• Residents are also allowed to hedge their existing holdings of foreign currency assets<br>• Hedging involving ringgit shall only be undertaken with licensed onshore banks |
| **IMPORT AND EXPORT OF RINGGIT AND FOREIGN CURRENCY NOTES BY RESIDENT TRAVELLERS** | |
| • Import and export of ringgit notes | • Allowed to import or export ringgit notes up to RM1,000 |
| • Import of foreign currency notes and traveller's cheques | • No limit |
| • Export of foreign currency notes and traveller's cheques | • Allowed to export foreign currency notes and traveller's cheques up to an equivalent of USD10,000 |
| • Import and export of ringgit and foreign currency exceeding permitted limits | • Application can be made online, using Form 13 which can be obtained at http://www.bnm.gov.my/fxadmin, or submitted via written application to Foreign Exchange Administration Department, Bank Negara Malaysia<br>• Response is given within one day from receipt of application with complete information |

| RESIDENT COMPANIES ACCORDED SPECIAL STATUS | |
|---|---|
| • Multimedia Super Corridor Companies | • Companies with Multimedia Super Corridor status are exempted from foreign exchange administration requirements for transactions undertaken on own account |
| • Approved Operational Headquarters | • Free to invest any amount in foreign currency assets to be funded with own foreign currency funds or borrowing<br>• Free to obtain any amount of foreign currency credit facilities from licensed onshore banks, licensed IIBs and from any non-residents, provided the operational headquarters do not on-lend to, or raise the funds on behalf of, any resident<br>• Free to utilise proceeds of any amount from the issuance of ordinary shares through initial public offering on the Main Board of Bursa Malaysia for investment in foreign currency assets<br>• Free to lend foreign currency sourced from listing of shares on foreign stock exchanges to other resident companies within the same corporate group in Malaysia |
| • Regional Distribution Centres and International Procurement Centres | • Regional Distribution Centres and International Procurement Centres are subject to rules applicable to resident companies |

# Key Economic and Financial Statistics

**Table A.1**
**Gross Domestic Product by Kind of Economic Activity in Constant 2000 Prices**

| | 2004 | 2005 | 2006 | 2007 | 2008*p* | 2009*f* |
|---|---|---|---|---|---|---|
| | RM million | | | | | |
| Agriculture | 34,929 | 35,835 | 37,769 | 38,593 | 40,073 | 39,260 |
| Mining and quarrying | 42,627 | 42,472 | 41,315 | 42,663 | 42,337 | 42,176 |
| Manufacturing | 131,127 | 137,940 | 147,672 | 152,262 | 154,195 | 141,934 |
| Construction | 14,903 | 14,685 | 14,604 | 15,279 | 15,604 | 16,071 |
| Services | 214,528 | 230,043 | 246,895 | 270,761 | 290,588 | 303,695 |
| Less: Undistributed FISIM[1] | 17,705 | 17,742 | 18,351 | 19,727 | 20,786 | 20,853 |
| Plus: Import duties | 6,099 | 6,017 | 5,287 | 5,521 | 6,793 | 6,576 |
| **GDP at purchasers' prices[2]** | **426,508** | **449,250** | **475,192** | **505,353** | **528,804** | **528,860** |
| | Annual change (%) | | | | | |
| Agriculture | 4.7 | 2.6 | 5.4 | 2.2 | 3.8 | -2.0 |
| Mining and quarrying | 4.1 | -0.4 | -2.7 | 3.3 | -0.8 | -0.4 |
| Manufacturing | 9.6 | 5.2 | 7.1 | 3.1 | 1.3 | -8.0 |
| Construction | -0.9 | -1.5 | -0.5 | 4.6 | 2.1 | 3.0 |
| Services | 6.4 | 7.2 | 7.3 | 9.7 | 7.3 | 4.5 |
| Less: Undistributed FISIM[1] | 0.3 | 0.2 | 3.4 | 7.5 | 5.4 | 0.3 |
| Plus: Import duties | -5.5 | -1.3 | -12.1 | 4.4 | 23.0 | -3.2 |
| **GDP at purchasers' prices[2]** | **6.8** | **5.3** | **5.8** | **6.3** | **4.6** | **-1.0 ~ 1.0** |

[1] Financial intermediation services indirectly measured
[2] Numbers may not necessarily add up due to rounding
*p* Preliminary
*f* Forecast

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

**Table A.2**
**Growth in Manufacturing Production (2005=100)**

| | 2005 | 2006 | 2007 | 2008 | 2006 | 2007 | 2008 |
|---|---|---|---|---|---|---|---|
| | Index | | | | Annual change (%) | | |
| **Export-oriented industries** | **100.0** | **110.0** | **111.1** | **109.8** | **10.0** | **1.0** | **-1.2** |
| **Electrical and electronics cluster** | **100.0** | **113.5** | **111.8** | **107.9** | **13.5** | **-1.5** | **-3.5** |
| *Electronics* | *100.0* | *116.4* | *119.9* | *113.4* | *16.4* | *3.0* | *-5.4* |
| *Electrical products* | *100.0* | *107.9* | *96.2* | *97.2* | *7.9* | *-10.8* | *1.1* |
| **Primary-related cluster** | **100.0** | **107.7** | **110.6** | **111.1** | **7.7** | **2.7** | **0.4** |
| Chemicals and chemical products | 100.0 | 107.6 | 111.4 | 107.6 | 7.6 | 3.6 | -3.5 |
| Petroleum products | 100.0 | 108.2 | 110.8 | 117.4 | 8.2 | 2.5 | 5.9 |
| Textiles, wearing apparel and footwear | 100.0 | 102.2 | 100.3 | 100.3 | 2.2 | -1.9 | 0.0 |
| Wood and wood products | 100.0 | 97.1 | 94.3 | 89.7 | -2.9 | -2.8 | -4.9 |
| Rubber products | 100.0 | 112.7 | 122.5 | 128.2 | 12.7 | 8.6 | 4.7 |
| Off-estate processing | 100.0 | 115.4 | 105.1 | 115.0 | 15.4 | -8.9 | 9.4 |
| Paper products | 100.0 | 112.4 | 140.8 | 120.6 | 12.4 | 25.3 | -14.4 |
| **Domestic-oriented industries** | **100.0** | **104.5** | **112.5** | **121.5** | **4.5** | **7.6** | **8.0** |
| **Construction-related cluster** | **100.0** | **110.5** | **121.6** | **126.9** | **10.5** | **10.0** | **4.3** |
| Construction-related products | 100.0 | 104.4 | 113.2 | 116.9 | 4.4 | 8.5 | 3.2 |
| *Non-metallic mineral products* | *100.0* | *103.3* | *105.3* | *114.9* | *3.3* | *1.9* | *9.1* |
| *Basic iron & steel and non-ferrous metal* | *100.0* | *105.6* | *122.9* | *119.3* | *5.6* | *16.3* | *-2.9* |
| Fabricated metal products | 100.0 | 122.4 | 137.8 | 146.2 | 22.4 | 12.5 | 6.1 |
| **Consumer-related cluster** | **100.0** | **100.2** | **105.9** | **117.6** | **0.2** | **5.6** | **11.0** |
| Food products | 100.0 | 106.4 | 114.5 | 125.8 | 6.4 | 7.6 | 9.9 |
| Transport equipment | 100.0 | 95.3 | 94.3 | 116.4 | -4.7 | -1.1 | 23.4 |
| Beverages | 100.0 | 98.5 | 114.2 | 117.2 | -1.5 | 15.9 | 2.6 |
| Tobacco products | 100.0 | 95.7 | 99.0 | 93.5 | -4.3 | 3.5 | -5.6 |
| Others | 100.0 | 99.7 | 110.4 | 101.7 | -0.3 | 10.7 | -7.9 |
| **Total** | **100.0** | **108.9** | **111.4** | **112.1** | **8.9** | **2.2** | **0.7** |

Source: Department of Statistics, Malaysia

**Table A.3**
**Production of Primary Commodities**

| | 2004 | 2005 | 2006 | 2007 | 2008*p* | 2005 | 2006 | 2007 | 2008*p* |
|---|---|---|---|---|---|---|---|---|---|
| | Volume | | | | | Annual change (%) | | | |
| Crude palm oil ('000 tonnes) | 13,976 | 14,962 | 15,881 | 15,824 | 17,734 | 7.1 | 6.1 | -0.4 | 12.1 |
| Rubber ('000 tonnes) | 1,169 | 1,126 | 1,284 | 1,200 | 1,078 | -3.7 | 14.0 | -6.6 | -10.1 |
| Saw logs ('000 cu. metres) | 21,782 | 22,398 | 21,894 | 22,052 | 18,463 | 2.8 | -2.3 | 0.7 | -16.3 |
| Cocoa ('000 tonnes) | 33 | 28 | 32 | 35 | 28 | -16.3 | 14.2 | 10.2 | -20.5 |
| Crude oil (including condensates) ('000 bpd) | 762 | 704 | 667 | 683 | 694 | -7.7 | -5.2 | 2.4 | 1.7 |
| Natural gas (mmscfd) | 5,196 | 5,797 | 5,774 | 5,884 | 5,579 | 11.6 | -0.4 | 1.9 | -5.2 |
| Tin-in-concentrates ('000 tonnes) | 2.7 | 2.9 | 2.4 | 2.3 | 2.5[1] | 4.1 | -16.1 | -5.5 | 36.8[1] |

[1] January - October 2008
*p* Preliminary

Source: Malaysian Palm Oil Board
Department of Statistics, Malaysia
Forestry Departments (Peninsular Malaysia, Sabah & Sarawak)
Malaysian Cocoa Board
PETRONAS
Minerals and Geoscience Department, Malaysia

**Table A.4**
**GNP by Demand Aggregates**

| | 2004 | 2005 | 2006 | 2007 | 2008*p* | 2009*f* |
|---|---|---|---|---|---|---|
| | at Current Prices (RM million) | | | | | |
| Consumption | 268,206 | 298,750 | 325,938 | 371,021 | 427,286 | 454,411 |
| *Private consumption* | *208,571* | *234,234* | *257,412* | *292,724* | *334,219* | *352,143* |
| *Public consumption* | *59,635* | *64,516* | *68,526* | *78,297* | *93,067* | *102,268* |
| Investment | 99,336 | 107,185 | 119,596 | 139,142 | 146,127 | 142,157 |
| *Private investment* | *50,592* | *53,705* | *61,116* | *74,499* | *79,797* | *63,356* |
| *Public investment* | *48,744* | *53,480* | *58,480* | *64,643* | *66,330* | *78,801* |
| Change in stocks[1] | 9,930 | -2,770 | 577 | 1,654 | -4,532 | 1,556 |
| Exports of goods and services | 546,925 | 613,694 | 669,776 | 707,156 | 766,360 | 579,222 |
| Imports of goods and services | 450,350 | 494,414 | 542,150 | 577,110 | 594,520 | 471,972 |
| GDP at purchasers' value | 474,048 | 522,445 | 573,736 | 641,864 | 740,721 | 705,373 |
| Net factor payments abroad | -24,402 | -23,961 | -17,356 | -13,758 | -25,441 | -10,620 |
| GNI at purchasers' value | 449,646 | 498,485 | 556,380 | 628,106 | 715,280 | 694,753 |
| | at Constant 2000 Prices (RM million) | | | | | |
| Consumption | 253,025 | 274,642 | 291,480 | 320,327 | 349,407 | 364,392 |
| *Private consumption* | *198,193* | *216,247* | *230,222* | *255,028* | *276,527* | *286,205* |
| *Public consumption* | *54,832* | *58,395* | *61,258* | *65,299* | *72,880* | *78,187* |
| Investment | 94,562 | 99,266 | 107,116 | 117,375 | 118,670 | 117,469 |
| *Private investment* | *49,239* | *50,841* | *54,643* | *59,996* | *60,896* | *50,118* |
| *Public investment* | *45,322* | *48,425* | *52,473* | *57,378* | *57,775* | *67,351* |
| Change in stocks[1] | 4,052 | -3,080 | 111 | -5,918 | -10,081 | -2,811 |
| Exports of goods and services | 511,774 | 554,261 | 592,898 | 617,628 | 626,824 | 522,913 |
| Imports of goods and services | 436,906 | 475,838 | 516,412 | 544,059 | 556,015 | 473,102 |
| GDP at purchasers' value | 426,508 | 449,250 | 475,192 | 505,353 | 528,804 | 528,860 |
| Net factor payments abroad | -23,670 | -24,956 | -20,567 | -23,114 | -32,727 | -23,996 |
| GNI at purchasers' value | 402,838 | 424,295 | 454,625 | 482,239 | 496,077 | 504,864 |

[1] Includes statistical discrepancy
*p* Preliminary
*f* Forecast

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

**Table A.5**
**Savings-Investment Gap**

| | 2004 | 2005 | 2006 | 2007 | 2008*p* |
|---|---|---|---|---|---|
| | RM million | | | | |
| Public gross domestic capital formation | 48,744 | 53,480 | 58,480 | 64,643 | 66,330 |
| Public savings | 73,000 | 70,506 | 83,226 | 104,231 | 80,443 |
| Deficit/surplus | 24,256 | 17,026 | 24,746 | 39,588 | 14,113 |
| Private gross domestic capital formation | 60,522 | 50,935 | 61,693 | 76,153 | 75,265 |
| Private savings | 93,806 | 112,257 | 130,365 | 137,111 | 190,503 |
| Deficit/surplus | 33,284 | 61,322 | 68,672 | 60,958 | 115,238 |
| Gross domestic capital formation | 109,266 | 104,415 | 120,173 | 140,796 | 141,595 |
| (as % of GNI) | 24.3 | 20.9 | 21.6 | 22.4 | 19.8 |
| Gross national savings | 166,806 | 182,763 | 213,591 | 241,342 | 270,946 |
| (as % of GNI) | 37.1 | 36.7 | 38.4 | 38.4 | 37.9 |
| Balance on current account | 57,540 | 78,348 | 93,418 | 100,546 | 129,351 |
| (as % of GNI) | 12.8 | 15.7 | 16.8 | 16.0 | 18.1 |

*p* Preliminary

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

**Table A.6**
**Labour Market: Selected Indicators**

| | 2004 | 2005 | 2006 | 2007 | 2008*e* |
|---|---|---|---|---|---|
| | (number of positions/persons) | | | | |
| **Vacancies Reported by Industry[1]** | | | | | |
| Agriculture, hunting, forestry and fishery | 1,373 | 40,438 | 188,104 | 226,759 | 275,548 |
| Mining and quarrying | 41 | 150 | 861 | 1,163 | 1,450 |
| Manufacturing | 17,769 | 112,542 | 348,302 | 275,155 | 327,798 |
| Construction | 3,505 | 48,524 | 129,586 | 117,217 | 107,421 |
| Services | 18,624 | 63,441 | 154,902 | 204,599 | 346,763 |
| *Electricity, gas and water supply* | *198* | *859* | *2,227* | *1,477* | *2,047* |
| *Wholesale and retail trade, hotels and restaurants* | *5,221* | *23,921* | *67,956* | *66,600* | *99,317* |
| *Transport, storage and communication* | *1,046* | *3,892* | *8,287* | *12,578* | *15,264* |
| *Financial intermediation, real estate, renting and business services* | *6,162* | *13,874* | *26,642* | *50,235* | *125,821* |
| *Public administration, defence and compulsory social security* | *1,224* | *2,497* | *3,539* | *11,287* | *11,132* |
| *Community, social and personal service activities* | *4,773* | *18,398* | *46,251* | *62,422* | *93,182* |
| Others not elsewhere classified | 8,663 | 39,405 | 12,920 | 289 | 0 |
| **Total vacancies** | **49,975** | **304,500** | **834,675** | **825,182** | **1,058,980** |
| **Retrenchment by Industry** | | | | | |
| Agriculture, hunting, forestry and fishery | 608 | 243 | 312 | 255 | 398 |
| Mining and quarrying | 120 | 355 | 78 | 61 | 89 |
| Manufacturing | 12,333 | 11,802 | 8,890 | 9,970 | 11,014* |
| Construction | 1,041 | 411 | 603 | 291 | 199 |
| Services | 5,854 | 3,298 | 5,477 | 3,458 | 4,769 |
| *Electricity, gas and water supply* | *0* | *0* | *65* | *5* | *77* |
| *Wholesale and retail trade, hotels and restaurants* | *1,402* | *1,294* | *2,327* | *1,929* | *2,052* |
| *Transport, storage and communication* | *2,287* | *802* | *1,521* | *322* | *773* |
| *Financial intermediation, real estate, renting and business services* | *1,361* | *463* | *983* | *761* | *1,008* |
| *Community, social and personal service activities* | *804* | *739* | *581* | *441* | *859* |
| **Total retrenchments** | **19,956** | **16,109** | **15,360** | **14,035** | **16,469** |
| **Employment by Industry[2] ('000 persons)** | | | | | |
| Agriculture, forestry, livestock and fishery | 1,406.9 | 1,401.3 | 1,392.4 | 1,389.8 | 1,388.7 |
| Mining and quarrying | 42.6 | 42.7 | 42.6 | 42.9 | 42.8 |
| Manufacturing | 2,972.4 | 3,133.2 | 3,227.2 | 3,296.6 | 3,337.6 |
| Construction | 767.3 | 759.6 | 755.2 | 757.3 | 758.4 |
| Services | 5,274.5 | 5,555.9 | 5,741.7 | 5,911.4 | 5,997.1 |
| *Electricity, gas and water supply* | *89.9* | *93.0* | *95.0* | *96.8* | *97.6* |
| *Transport, storage and communication* | *594.3* | *630.6* | *646.4* | *660.0* | *670.1* |
| *Wholesale and retail trade, hotels and restaurants* | *1,729.6* | *1,861.5* | *1,930.4* | *1,957.7* | *1,979.6* |
| *Finance, insurance, real estate and business services* | *695.0* | *734.4* | *767.5* | *789.7* | *796.8* |
| *Government services* | *1,098.6* | *1,118.4* | *1,152.5* | *1,225.6* | *1,247.0* |
| *Other services* | *1,067.1* | *1,118.1* | *1,150.0* | *1,181.6* | *1,205.8* |
| **Total employment** | **10,463.7** | **10,892.8** | **11,159.0** | **11,398.0** | **11,524.7** |
| **Unemployment rate[2] (% of labour force)** | **3.5** | **3.5** | **3.3** | **3.2** | **3.7** |

*e* Estimates
[1] Refers to vacancies reported by employers through the Electronic Labour Exchange (ELX). From 2005 onwards, companies were required to first post vacancies with the ELX before they could apply to hire foreign workers
[2] Refers to estimates by Economic Planning Unit
* Excludes 7,564 retrenched workers from a company that was taken over, and rehired immediately by the new owner

Source: Economic Planning Unit and Ministry of Human Resources

**Table A.7**
**Private Consumption Indicators**

| | 2007 | 2008 | | | | |
|---|---|---|---|---|---|---|
| | | 1Q | 2Q | 3Q | 4Q | Year |
| Sales of passenger cars ('000 units) | 442.9 | 120.3 | 134.0 | 138.1 | 105.1 | 497.5 |
| Annual change (%) | 18.4 | 25.7 | 27.8 | 10.4 | -10.5 | 12.3 |
| Imports of consumption goods (RM billion) | 28.9 | 7.4 | 8.3 | 8.7 | 8.0 | 32.3 |
| Annual change (%) | 3.6 | 5.6 | 21.3 | 16.2 | 4.1 | 11.6 |
| Tax collection | | | | | | |
| Sales tax (RM billion) | 6.3 | 1.2 | 2.2 | 1.9 | 3.1 | 7.4 |
| Service tax (RM billion) | 3.0 | 0.5 | 1.0 | 0.8 | 1.0 | 3.2 |
| Narrow Money (M1) | | | | | | |
| Annual change (%) | 19.6 | 2.7 | 1.4 | 2.1 | 1.9 | 8.3 |
| Loans disbursed by banking system | | | | | | |
| Consumption credit (excl. passenger cars) | | | | | | |
| Annual change (%) | 14.9 | 15.4 | 21.0 | 3.0 | -1.5 | 8.8 |
| Retail trade, restaurants and hotels | | | | | | |
| Annual change (%) | 0.8 | 22.6 | 36.5 | 32.8 | 8.1 | 24.5 |
| MRA retail sales (Annual change in %) | 12.8 | n.a. | n.a. | n.a. | n.a. | 5.0 |
| Credit card turnover spending (RM billion) | 55.6 | 15.4 | 15.7 | 17.2 | 16.8 | 65.2 |
| Annual change (%) | 17.5 | 17.1 | 19.5 | 22.0 | 10.9 | 17.2 |
| MIER Consumer Sentiment Index | – | 115.5 | 70.6 | 88.9 | 71.4 | – |
| KL Composite Index | 1,445.0 | 1,247.5 | 1,186.6 | 1,018.7 | 876.8 | 876.8 |
| Commodity prices | | | | | | |
| CPO (RM/tonne) | 2,472 | 3,592 | 3,524 | 2,780 | 1,601 | 2,875 |
| Crude oil (USD/barrel) | 78 | 99 | 128 | 124 | 57 | 102 |
| Rubber (sen/kg) | 736 | 842 | 927 | 983 | 563 | 829 |

n.a. Not available

**Table A.8**
**Private Investment Indicators**

| | 2007 | 2008 | | | | |
|---|---|---|---|---|---|---|
| | | 1Q | 2Q | 3Q | 4Q | Year |
| Sales of commercial vehicles ('000 units) | 44.3 | 10.5 | 13.2 | 13.8 | 13.1 | 50.7 |
| Annual change (%) | -62.0 | 13.0 | 20.3 | 11.2 | 13.3 | 14.4 |
| Imports of capital goods (RM billion) | 69.9 | 16.1 | 18.3 | 18.6 | 16.9 | 69.9 |
| Annual change (%) | 7.2 | 7.8 | 11.3 | -2.3 | -13.4 | 0.0 |
| Approvals by MITI (Manufacturing sector) | | | | | | |
| No. of projects | 949 | 197 | 225 | 234 | 263 | 919 |
| Capital investment (RM billion) | 59.9 | 22.7 | 16.8 | 12.7 | 10.6 | 62.8 |
| *Foreign* | *33.4* | *16.0* | *13.7* | *9.0* | *7.4* | *46.1* |
| *Local* | *26.5* | *6.7* | *3.1* | *3.6* | *3.3* | *16.7* |
| New investment (% share) | 52.0 | 70.1 | 69.9 | 82.6 | 36.5 | 66.9 |
| Reinvestments (% share) | 48.0 | 29.9 | 30.1 | 17.4 | 63.5 | 33.1 |
| Loans disbursed by banking system | | | | | | |
| Manufacturing sector | | | | | | |
| Annual change (%) | 13.5 | 11.6 | 21.9 | 16.7 | -0.3 | 12.3 |
| Construction sector | | | | | | |
| Annual change (%) | 6.9 | 22.9 | 4.6 | 4.7 | -4.3 | 6.6 |
| Private Debt Securities (excluding Cagamas) | | | | | | |
| Total funds raised (RM billion) | 67.6 | 10.0 | 19.7 | 11.0 | 8.9 | 49.7 |
| New activities | 31.8 | 5.3 | 13.8 | 8.3 | 5.9 | 33.3 |
| Initial Public Offerings (Bursa Malaysia) | | | | | | |
| Total funds raised (RM billion) | 2.5 | 0.2 | 0.3 | 0.7 | 0.1 | 1.3 |
| MIER Business Conditions Survey | | | | | | |
| Business Conditions Index | - | 119.9 | 114.1 | 99.6 | 53.8 | - |
| Capacity Utilisation Rate | - | 83.0 | 82.6 | 81.2 | 74.4 | - |
| MSC-Status Companies | | | | | | |
| No. of companies | 266 | 35 | 47 | 66 | 94 | 242 |
| Approved investment (RM billion) | 3.7 | 0.3 | 0.4 | 0.6 | 0.6 | 1.8 |

**Table A.9**
**Balance of Payments**

| Item | 2005 | | | 2006 | | |
|---|---|---|---|---|---|---|
| | + | - | Net | + | - | Net |
| | RM million | | | | | |
| **Goods[1]** | **539,420** | **410,529** | **128,892** | **589,743** | **455,185** | **134,558** |
| *Trade account* | *536,234* | *432,871* | *103,363* | *588,965* | *480,773* | *108,193* |
| **Services** | **74,274** | **83,886** | **-9,612** | **80,034** | **86,964** | **-6,931** |
| Transportation | 15,807 | 31,687 | -15,880 | 15,491 | 35,111 | -19,620 |
| Travel | 33,503 | 14,820 | 18,684 | 38,237 | 14,736 | 23,501 |
| Other services | 24,537 | 36,603 | -12,066 | 25,905 | 36,283 | -10,378 |
| Government transactions n.i.e.[2] | 428 | 777 | -350 | 401 | 834 | -433 |
| **Balance on goods and services** | **613,694** | **494,414** | **119,280** | **669,776** | **542,150** | **127,627** |
| **Income** | **20,627** | **44,569** | **-23,943** | **31,103** | **48,375** | **-17,271** |
| Compensation of employees | 4,313 | 4,848 | -535 | 5,004 | 5,287 | -283 |
| Investment income[3] | 16,313 | 39,721 | -23,408 | 26,100 | 43,088 | -16,988 |
| **Current transfers** | **1,137** | **18,107** | **-16,971** | **1,147** | **17,999** | **-16,852** |
| **Balance on current account** | **635,458** | **557,092** | **78,367** | **702,026** | **608,526** | **93,504** |
| **% of GNI** | | | **15.7** | | | **16.8** |
| **Capital account** | | | **-** | | | **-** |
| **Financial account** | | | **-36,991** | | | **-43,488** |
| Direct investment | | | 3,749 | | | 22 |
| *Abroad* | | | *-11,647* | | | *-22,161* |
| *In Malaysia* | | | *15,396* | | | *22,183* |
| Portfolio investment | | | -14,116 | | | 12,911 |
| Other investment | | | -26,624 | | | -56,422 |
| *Official sector* | | | *-3,149* | | | *-8,019* |
| *Private sector* | | | *-23,474* | | | *-48,403* |
| **Balance on capital and financial accounts** | | | **-36,991** | | | **-43,488** |
| **Errors and omissions** | | | **-27,825** | | | **-24,857** |
| of which: | | | | | | |
| Foreign exchange revaluation gain (+) / loss (-) | | | -15,496 | | | -6,945 |
| **Overall balance (surplus + / deficit -)** | | | **13,550** | | | **25,158** |
| **Bank Negara Malaysia international reserves, net[4]** | | | | | | |
| RM million | | | 265,240 | | | 290,399 |
| USD million | | | 70,193 | | | 82,451 |
| Reserves as months of retained imports | | | 7.7 | | | 7.8 |

[1] Adjusted for valuation and coverage to the balance of payments basis. Imports include military goods which are not included in trade data
[2] Include transactions of foreign military and diplomatic establishments
[3] Include undistributed earnings of foreign direct investment companies. The counterpart of these earnings is shown as reinvested earnings under "Direct Investment" in the Financial Account
[4] All assets and liabilities in foreign currencies have been revalued into ringgit at rates of exchange ruling on the balance sheet date and the gain/loss has been reflected accordingly in the Bank's account
*e* Estimate
*f* Forecast
n.i.e. Not included elsewhere
Note: Numbers may not necessarily add up due to rounding

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

| 2007 | | | 2008*e* | | | 2009*f* | | |
|---|---|---|---|---|---|---|---|---|
| + | - | Net | + | - | Net | + | - | Net |
| RM million | | | | | | | | |
| **605,916** | **478,243** | **127,673** | **664,181** | **494,065** | **170,116** | **495,751** | **387,647** | **108,103** |
| *605,153* | *504,814* | *100,339* | *663,494* | *521,611* | *141,883* | *495,665* | *410,771* | *84,895* |
| **101,240** | **98,867** | **2,373** | **102,179** | **100,455** | **1,725** | **83,471** | **84,325** | **-854** |
| 24,582 | 37,755 | -13,173 | 22,972 | 37,616 | -14,644 | 15,242 | 29,391 | -14,148 |
| 48,289 | 19,174 | 29,115 | 50,738 | 22,517 | 28,221 | 43,138 | 18,875 | 24,263 |
| 28,068 | 41,246 | -13,178 | 28,343 | 39,644 | -11,301 | 24,971 | 35,824 | -10,853 |
| 301 | 691 | -390 | 126 | 677 | -551 | 120 | 235 | -115 |
| **707,156** | **577,110** | **130,047** | **766,360** | **594,520** | **171,840** | **579,222** | **471,972** | **107,250** |
| **38,840** | **52,733** | **-13,893** | **39,097** | **64,538** | **-25,441** | **25,963** | **36,583** | **-10,620** |
| 5,372 | 5,972 | -600 | 4,438 | 5,164 | -726 | 3,050 | 4,200 | -1,150 |
| 33,468 | 46,761 | -13,294 | 34,660 | 59,374 | -24,715 | 22,913 | 32,383 | -9,470 |
| **1,444** | **17,187** | **-15,743** | **1,425** | **18,474** | **-17,049** | **1,075** | **17,702** | **-16,627** |
| **747,439** | **647,030** | **100,410** | **806,882** | **677,532** | **129,351** | **606,260** | **526,257** | **80,003** |
| | | **16.0** | | | **18.1** | | | **11.5** |
| | | **-95** | | | **585** | | | |
| | | **-37,710** | | | **-123,875** | | | |
| | | -9,142 | | | -20,458 | | | |
| | | *-38,224* | | | *-47,123* | | | |
| | | *29,081* | | | *26,665* | | | |
| | | 18,355 | | | -92,406 | | | |
| | | -46,923 | | | -11,011 | | | |
| | | *-5,788* | | | *-2,710* | | | |
| | | *-41,135* | | | *-8,300* | | | |
| | | **-37,805** | | | **-123,290** | | | |
| | | **-17,309** | | | **-24,311** | | | |
| | | -5,597 | | | -5,824 | | | |
| | | **45,296** | | | **-18,250** | | | |
| | | 335,695 | | | 317,445 | | | |
| | | 101,338 | | | 91,529 | | | |
| | | 8.4 | | | 7.6 | | | |

**Table A.10**
**Gross Exports**

| | 2006 | 2007 | 2008*p* | 2007 | 2008*p* | 2008*p* |
|---|---|---|---|---|---|---|
| | RM million | | | Annual change (%) | | % share |
| **Manufactures** | **473,213** | **474,714** | **491,930** | **0.3** | **3.6** | **74.1** |
| *of which:* | | | | | | |
| Electronics, electrical machinery and appliances | 300,861 | 288,326 | 277,282 | -4.2 | -3.8 | 41.8 |
| Electronics | 221,257 | 213,450 | 195,933 | -3.5 | -8.2 | 29.5 |
| *Semiconductors* | *93,505* | *96,471* | *89,819* | *3.2* | *-6.9* | *13.5* |
| *Electronic equipment & parts* | *127,752* | *116,978* | *106,113* | *-8.4* | *-9.3* | *16.0* |
| Electrical machinery & appliances | 79,604 | 74,876 | 81,349 | -5.9 | 8.6 | 12.3 |
| *Consumer electrical products* | *19,099* | *16,469* | *21,388* | *-13.8* | *29.9* | *3.2* |
| *Industrial & commercial electrical products* | *34,489* | *29,690* | *31,088* | *-13.9* | *4.7* | *4.7* |
| *Electrical industrial machinery and equipment* | *22,844* | *25,183* | *25,382* | *10.2* | *0.8* | *3.8* |
| *Household electrical appliances* | *3,172* | *3,534* | *3,491* | *11.4* | *-1.2* | *0.5* |
| Chemicals & chemical products | 32,893 | 37,421 | 40,926 | 13.8 | 9.4 | 6.2 |
| Manufactures of metal | 22,817 | 26,410 | 29,257 | 15.7 | 10.8 | 4.4 |
| Petroleum products | 21,274 | 22,093 | 31,149 | 3.8 | 41.0 | 4.7 |
| Optical and scientific equipment | 13,558 | 13,612 | 14,944 | 0.4 | 9.8 | 2.3 |
| Textiles, clothing and footwear | 11,226 | 10,632 | 10,911 | -5.3 | 2.6 | 1.6 |
| Wood products | 10,343 | 9,689 | 9,767 | -6.3 | 0.8 | 1.5 |
| Rubber products | 9,101 | 10,323 | 12,426 | 13.4 | 20.4 | 1.9 |
| **Minerals** | **56,844** | **61,117** | **87,536** | **7.5** | **43.2** | **13.2** |
| *of which:* | | | | | | |
| Crude oil and condensates | 30,814 | 31,880 | 43,040 | 3.5 | 35.0 | 6.5 |
| Liquefied natural gas (LNG) | 23,285 | 26,157 | 40,732 | 12.3 | 55.7 | 6.1 |
| **Agriculture** | **42,106** | **52,366** | **68,097** | **24.4** | **30.0** | **10.3** |
| *of which:* | | | | | | |
| Palm oil | 21,643 | 31,983 | 45,955 | 47.8 | 43.7 | 6.9 |
| Rubber | 8,235 | 7,335 | 8,112 | -10.9 | 10.6 | 1.2 |
| **Others** | **16,803** | **16,956** | **15,931** | **0.9** | **-6.0** | **2.4** |
| **Total** | **588,965** | **605,153** | **663,494** | **2.7** | **9.6** | **100.0** |

*p* Preliminary
Note: Numbers may not necessarily add up due to rounding

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

**Table A.11**
**Exports of Primary Commodities**

| | 2006 | 2007 | 2008*p* | 2007 | 2008*p* |
|---|---|---|---|---|---|
| | Volume and value | | | Annual change (%) | |
| **Commodity exports (RM million)** | **98,950** | **113,483** | **155,634** | **14.7** | **37.1** |
| **Agriculture exports (RM million)** | **42,106** | **52,366** | **68,097** | **24.4** | **30.0** |
| *of which:* | | | | | |
| Palm oil | | | | | |
| ('000 tonnes) | 14,017 | 13,505 | 15,699 | -3.7 | 16.2 |
| (RM/tonne) | 1,544 | 2,368 | 2,927 | 53.4 | 23.6 |
| (RM million) | 21,643 | 31,983 | 45,955 | 47.8 | 43.7 |
| Palm kernel oil | | | | | |
| ('000 tonnes) | 518 | 588 | 684 | 13.4 | 16.3 |
| (RM/tonne) | 1,969 | 2,747 | 3,792 | 39.6 | 38.0 |
| (RM million) | 1,020 | 1,615 | 2,592 | 58.3 | 60.5 |
| Rubber | | | | | |
| ('000 tonnes) | 1,143 | 1,018 | 916 | -10.9 | -10.1 |
| (sen/kilogramme) | 721 | 720 | 886 | ... | 23.0 |
| (RM million) | 8,235 | 7,335 | 8,112 | -10.9 | 10.6 |
| Saw logs | | | | | |
| ('000 cubic metres) | 4,772 | 4,644 | 4,368 | -2.7 | -5.9 |
| (RM/cubic metre) | 474 | 455 | 471 | -4.0 | 3.5 |
| (RM million) | 2,261 | 2,112 | 2,057 | -6.6 | -2.6 |
| Sawn timber | | | | | |
| ('000 cubic metres) | 3,318 | 2,985 | 2,854 | -10.1 | -4.4 |
| (RM/cubic metre) | 1,306 | 1,373 | 1,211 | 5.1 | -11.8 |
| (RM million) | 4,333 | 4,096 | 3,455 | -5.4 | -15.7 |
| Cocoa beans | | | | | |
| ('000 tonnes) | 13.5 | 17.8 | 7.6 | 31.9 | -57.2 |
| (RM/tonne) | 5,624 | 6,522 | 7,883 | 16.0 | 20.9 |
| (RM million) | 76 | 116 | 60 | 53.0 | -48.3 |
| **Mineral exports (RM million)** | **56,844** | **61,117** | **87,536** | **7.5** | **43.2** |
| *of which:* | | | | | |
| Crude oil and condensates | | | | | |
| ('000 tonnes) | 16,304 | 16,390 | 16,898 | 0.5 | 3.1 |
| (USD/barrel) | 67.82 | 74.63 | 101.14 | 10.0 | 35.5 |
| (RM million) | 30,814 | 31,880 | 43,040 | 3.5 | 35.0 |
| Liquefied natural gas (LNG) | | | | | |
| ('000 tonnes) | 21,534 | 22,668 | 22,873 | 5.3 | 0.9 |
| (RM/tonne) | 1,081 | 1,154 | 1,781 | 6.7 | 54.3 |
| (RM million) | 23,285 | 26,157 | 40,732 | 12.3 | 55.7 |
| Tin | | | | | |
| ('000 tonnes) | 19.4 | 15.8 | 27.5 | -18.7 | 74.7 |
| (RM/tonne) | 30,093 | 49,522 | 61,675 | 64.6 | 24.5 |
| (RM million) | 583 | 780 | 1,698 | 33.8 | 117.6 |

*p* Preliminary
... Negligible

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

**Table A.12**
**Principal Markets for Manufactured Exports**

| Country | 2004 | 2005 | 2006 | 2007 | 2008*p* | 2004 | 2005 | 2006 | 2007 | 2008*p* |
|---|---|---|---|---|---|---|---|---|---|---|
| | RM million | | | | | % share | | | | |
| **Selected ASEAN countries** | **100,217** | **113,081** | **123,776** | **124,246** | **134,858** | **25.6** | **26.1** | **26.2** | **26.2** | **27.4** |
| Singapore | 66,434 | 75,507 | 81,863 | 78,990 | 85,286 | 17.0 | 17.5 | 17.3 | 16.6 | 17.3 |
| Thailand | 17,752 | 21,639 | 24,271 | 24,990 | 25,664 | 4.5 | 5.0 | 5.1 | 5.3 | 5.2 |
| Indonesia | 8,956 | 9,492 | 10,650 | 12,598 | 16,339 | 2.3 | 2.2 | 2.3 | 2.7 | 3.3 |
| Philippines | 6,113 | 5,429 | 6,041 | 6,486 | 6,225 | 1.6 | 1.3 | 1.3 | 1.4 | 1.3 |
| Brunei Darussalam | 963 | 1,014 | 951 | 1,182 | 1,344 | 0.2 | 0.2 | 0.2 | 0.2 | 0.3 |
| United States | 86,251 | 100,859 | 106,466 | 90,105 | 76,689 | 22.1 | 23.3 | 22.5 | 19.0 | 15.6 |
| **European Union** | **52,478** | **55,025** | **64,818** | **66,999** | **63,161** | **13.4** | **12.7** | **13.7** | **14.1** | **12.8** |
| Netherlands | 12,886 | 14,741 | 17,635 | 19,072 | 18,646 | 3.3 | 3.4 | 3.7 | 4.0 | 3.8 |
| Germany | 9,339 | 9,989 | 11,145 | 13,412 | 13,597 | 2.4 | 2.3 | 2.4 | 2.8 | 2.8 |
| United Kingdom | 9,727 | 8,721 | 10,088 | 9,232 | 8,620 | 2.5 | 2.0 | 2.1 | 1.9 | 1.8 |
| Others | 20,527 | 21,575 | 25,950 | 25,284 | 22,298 | 5.3 | 5.0 | 5.5 | 5.3 | 4.5 |
| The People's Republic of China | 22,414 | 26,086 | 31,818 | 38,138 | 44,494 | 5.7 | 6.0 | 6.7 | 8.0 | 9.0 |
| Japan | 33,632 | 32,327 | 33,238 | 32,712 | 36,004 | 8.6 | 7.5 | 7.0 | 6.9 | 7.3 |
| Hong Kong SAR | 27,596 | 30,188 | 28,067 | 26,744 | 27,045 | 7.1 | 7.0 | 5.9 | 5.6 | 5.5 |
| Middle East | 10,896 | 13,237 | 15,995 | 18,822 | 23,378 | 2.8 | 3.1 | 3.4 | 4.0 | 4.8 |
| Australia | 9,710 | 10,854 | 11,250 | 12,209 | 14,808 | 2.5 | 2.5 | 2.4 | 2.6 | 3.0 |
| Chinese Taipei | 11,933 | 10,551 | 10,625 | 11,666 | 10,501 | 3.1 | 2.4 | 2.2 | 2.5 | 2.1 |
| Korea | 9,249 | 9,564 | 10,337 | 10,718 | 10,304 | 2.4 | 2.2 | 2.2 | 2.3 | 2.1 |
| India | 5,169 | 6,532 | 7,172 | 9,178 | 10,129 | 1.3 | 1.5 | 1.5 | 1.9 | 2.1 |
| Latin American countries | 4,274 | 4,789 | 6,123 | 7,138 | 9,181 | 1.1 | 1.1 | 1.3 | 1.5 | 1.9 |
| Canada | 2,817 | 2,637 | 3,535 | 2,972 | 2,964 | 0.7 | 0.6 | 0.7 | 0.6 | 0.6 |
| Rest of the World | 14,302 | 16,801 | 19,992 | 23,071 | 28,413 | 3.7 | 3.9 | 4.2 | 4.9 | 5.8 |
| **Total** | **390,938** | **432,531** | **473,213** | **474,714** | **491,930** | **100.0** | **100.0** | **100.0** | **100.0** | **100.0** |

*p* Preliminary
Note: Numbers may not necessarily add up due to rounding

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

**Table A.13**
**Principal Export Markets for Electronics**

| Country | 2004 | 2005 | 2006 | 2007 | 2008*p* | 2004 | 2005 | 2006 | 2007 | 2008*p* |
|---|---|---|---|---|---|---|---|---|---|---|
| | RM million | | | | | % share | | | | |
| United States | 51,900 | 64,527 | 68,628 | 56,405 | 43,360 | 27.5 | 30.9 | 31.0 | 26.4 | 22.1 |
| Singapore | 33,398 | 35,044 | 34,829 | 34,241 | 33,828 | 17.7 | 16.8 | 15.7 | 16.0 | 17.3 |
| The People's Republic of China | 10,881 | 13,236 | 17,240 | 22,634 | 27,259 | 5.8 | 6.3 | 7.8 | 10.6 | 13.9 |
| Hong Kong SAR | 19,623 | 21,651 | 18,657 | 17,513 | 17,433 | 10.4 | 10.4 | 8.4 | 8.2 | 8.9 |
| Netherlands | 8,104 | 9,954 | 13,306 | 13,416 | 11,210 | 4.3 | 4.8 | 6.0 | 6.3 | 5.7 |
| Japan | 11,209 | 10,319 | 11,432 | 11,211 | 10,171 | 5.9 | 4.9 | 5.2 | 5.3 | 5.2 |
| Thailand | 8,286 | 9,377 | 9,692 | 9,952 | 9,392 | 4.4 | 4.5 | 4.4 | 4.7 | 4.8 |
| Germany | 5,159 | 5,153 | 5,126 | 6,620 | 6,587 | 2.7 | 2.5 | 2.3 | 3.1 | 3.4 |
| Chinese Taipei | 6,877 | 5,447 | 5,212 | 5,348 | 4,513 | 3.6 | 2.6 | 2.4 | 2.5 | 2.3 |
| Korea | 4,438 | 4,210 | 4,250 | 4,091 | 3,612 | 2.4 | 2.0 | 1.9 | 1.9 | 1.8 |
| Others | 28,690 | 29,626 | 32,883 | 32,018 | 28,568 | 15.2 | 14.2 | 14.9 | 15.0 | 14.6 |
| **Total** | **188,567** | **208,543** | **221,257** | **213,450** | **195,933** | **100.0** | **100.0** | **100.0** | **100.0** | **100.0** |

*p* Preliminary
Note: Numbers may not necessarily add up due to rounding
Source: Department of Statistics, Malaysia and Bank Negara Malaysia

**Table A.14**
**Principal Export Markets for Electrical Products**

| Country | 2004 | 2005 | 2006 | 2007 | 2008*p* | 2004 | 2005 | 2006 | 2007 | 2008*p* |
|---|---|---|---|---|---|---|---|---|---|---|
| | RM million | | | | | % share | | | | |
| United States | 18,175 | 18,944 | 19,070 | 15,783 | 14,886 | 26.5 | 25.5 | 24.0 | 21.1 | 18.3 |
| European Union | 10,635 | 11,045 | 13,272 | 12,376 | 13,451 | 15.5 | 14.9 | 16.7 | 16.5 | 16.5 |
| Singapore | 10,584 | 13,119 | 14,921 | 11,366 | 10,988 | 15.4 | 17.7 | 18.7 | 15.2 | 13.5 |
| Japan | 7,667 | 7,553 | 6,191 | 6,080 | 7,326 | 11.2 | 10.2 | 7.8 | 8.1 | 9.0 |
| Middle East | 2,585 | 2,679 | 3,341 | 4,377 | 5,633 | 3.8 | 3.6 | 4.2 | 5.8 | 6.9 |
| The People's Republic of China | 2,949 | 3,340 | 3,082 | 3,560 | 3,816 | 4.3 | 4.5 | 3.9 | 4.8 | 4.7 |
| Australia | 1,425 | 1,829 | 1,794 | 2,550 | 3,598 | 2.1 | 2.5 | 2.3 | 3.4 | 4.4 |
| Hong Kong SAR | 2,556 | 2,940 | 3,423 | 3,331 | 3,425 | 3.7 | 4.0 | 4.3 | 4.4 | 4.2 |
| Thailand | 2,310 | 2,557 | 2,647 | 2,849 | 2,705 | 3.4 | 3.4 | 3.3 | 3.8 | 3.3 |
| Others | 9,768 | 10,248 | 11,863 | 12,604 | 15,519 | 14.2 | 13.8 | 14.9 | 16.8 | 19.1 |
| **Total** | **68,654** | **74,253** | **79,604** | **74,876** | **81,349** | **100.0** | **100.0** | **100.0** | **100.0** | **100.0** |

*p* Preliminary
Note: Numbers may not necessarily add up due to rounding
Source: Department of Statistics, Malaysia and Bank Negara Malaysia

**Table A.15**
**Principal Export Markets for Chemicals and Chemical Products**

| Country | 2004 | 2005 | 2006 | 2007 | 2008*p* | 2004 | 2005 | 2006 | 2007 | 2008*p* |
|---|---|---|---|---|---|---|---|---|---|---|
| | RM million | | | | | % share | | | | |
| The People's Republic of China | 4,066 | 4,322 | 4,285 | 5,011 | 5,140 | 14.6 | 13.5 | 13.0 | 13.4 | 12.6 |
| Indonesia | 2,249 | 2,459 | 2,608 | 2,934 | 3,972 | 8.1 | 7.7 | 7.9 | 7.8 | 9.7 |
| Singapore | 2,582 | 3,129 | 2,997 | 3,366 | 3,720 | 9.3 | 9.8 | 9.1 | 9.0 | 9.1 |
| Thailand | 2,360 | 2,809 | 3,145 | 3,394 | 3,659 | 8.5 | 8.8 | 9.6 | 9.1 | 8.9 |
| Japan | 3,111 | 3,199 | 3,066 | 2,942 | 3,221 | 11.2 | 10.0 | 9.3 | 7.9 | 7.9 |
| India | 1,205 | 1,678 | 1,719 | 1,875 | 2,195 | 4.3 | 5.2 | 5.2 | 5.0 | 5.4 |
| Hong Kong SAR | 1,858 | 2,174 | 2,380 | 2,005 | 1,965 | 6.7 | 6.8 | 7.2 | 5.4 | 4.8 |
| Chinese Taipei | 1,347 | 1,319 | 1,358 | 1,788 | 1,610 | 4.8 | 4.1 | 4.1 | 4.8 | 3.9 |
| United States | 1,108 | 1,404 | 1,248 | 1,516 | 1,569 | 4.0 | 4.4 | 3.8 | 4.1 | 3.8 |
| Korea | 1,188 | 1,486 | 1,519 | 1,567 | 1,302 | 4.3 | 4.6 | 4.6 | 4.2 | 3.2 |
| Others | 6,762 | 7,986 | 8,568 | 11,021 | 12,575 | 24.3 | 25.0 | 26.0 | 29.5 | 30.7 |
| **Total** | **27,836** | **31,965** | **32,893** | **37,421** | **40,926** | **100.0** | **100.0** | **100.0** | **100.0** | **100.0** |

*p* Preliminary
Note: Numbers may not necessarily add up due to rounding

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

**Table A. 16**
**Principal Export Markets for Palm Oil**

| Country | 2004 | 2005 | 2006 | 2007 | 2008*p* | 2004 | 2005 | 2006 | 2007 | 2008*p* |
|---|---|---|---|---|---|---|---|---|---|---|
| | '000 tonnes | | | | | % share | | | | |
| The People's Republic of China | 2,827 | 2,914 | 3,532 | 3,786 | 3,785 | 23.1 | 22.6 | 25.2 | 28.0 | 24.1 |
| European Union | 1,862 | 2,149 | 2,586 | 2,097 | 2,022 | 15.2 | 16.7 | 18.4 | 15.5 | 12.9 |
| *Netherlands* | *1,135* | *1,367* | *1,703* | *1,527* | *1,311* | *9.3* | *10.6* | *12.1* | *11.3* | *8.3* |
| *Germany* | *149* | *180* | *190* | *30* | *101* | *1.2* | *1.4* | *1.4* | *0.2* | *0.6* |
| *Italy* | *119* | *155* | *165* | *126* | *182* | *1.0* | *1.2* | *1.2* | *0.9* | *1.2* |
| *Sweden* | *114* | *103* | *220* | *134* | *103* | *0.9* | *0.8* | *1.6* | *1.0* | *0.7* |
| *Others* | *345* | *345* | *308* | *280* | *325* | *2.8* | *2.7* | *2.2* | *2.1* | *2.1* |
| Pakistan | 838 | 929 | 855 | 1,062 | 1,552 | 6.9 | 7.2 | 6.1 | 7.9 | 9.9 |
| Middle East | 1,143 | 1,633 | 1,177 | 1,212 | 1,319 | 9.3 | 12.7 | 8.4 | 9.0 | 8.4 |
| United States | 298 | 535 | 696 | 516 | 1,234 | 2.4 | 4.1 | 5.0 | 3.8 | 7.9 |
| India | 925 | 619 | 657 | 515 | 956 | 7.6 | 4.8 | 4.7 | 3.8 | 6.1 |
| Japan | 458 | 438 | 498 | 516 | 530 | 3.7 | 3.4 | 3.6 | 3.8 | 3.4 |
| Bangladesh | 353 | 485 | 413 | 170 | 253 | 2.9 | 3.8 | 2.9 | 1.3 | 1.6 |
| Korea | 228 | 223 | 207 | 225 | 199 | 1.9 | 1.7 | 1.5 | 1.7 | 1.3 |
| Chinese Taipei | 120 | 127 | 148 | 129 | 161 | 1.0 | 1.0 | 1.1 | 1.0 | 1.0 |
| Australia | 96 | 107 | 121 | 121 | 113 | 0.8 | 0.8 | 0.9 | 0.9 | 0.7 |
| Others | 3,074 | 2,742 | 3,128 | 3,156 | 3,576 | 25.2 | 21.3 | 22.3 | 23.4 | 22.8 |
| **Total** | **12,223** | **12,901** | **14,017** | **13,505** | **15,699** | **100.0** | **100.0** | **100.0** | **100.0** | **100.0** |

*p* Preliminary
Note: Numbers may not necessarily add up due to rounding

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

**Table A.17**
**Principal Export Markets for Rubber**

| Country | 2004 | 2005 | 2006 | 2007 | 2008*p* | 2004 | 2005 | 2006 | 2007 | 2008*p* |
|---|---|---|---|---|---|---|---|---|---|---|
| | '000 tonnes | | | | | % share | | | | |
| The People's Republic of China | 289 | 386 | 406 | 371 | 301 | 26.1 | 33.5 | 35.5 | 36.4 | 32.8 |
| European Union | 346 | 313 | 316 | 294 | 279 | 31.2 | 27.2 | 27.6 | 28.9 | 30.5 |
| *Germany* | *149* | *132* | *144* | *136* | *123* | *13.4* | *11.4* | *12.6* | *13.3* | *13.5* |
| *France* | *53* | *46* | *41* | *43* | *32* | *4.8* | *4.0* | *3.6* | *4.3* | *3.5* |
| *Netherlands* | *20* | *28* | *21* | *17* | *21* | *1.8* | *2.4* | *1.9* | *1.6* | *2.3* |
| *Italy* | *29* | *24* | *22* | *20* | *17* | *2.6* | *2.1* | *1.9* | *1.9* | *1.9* |
| *United Kingdom* | *24* | *21* | *18* | *16* | *17* | *2.2* | *1.8* | *1.6* | *1.5* | *1.8* |
| *Spain* | *24* | *13* | *11* | *9* | *8* | *2.2* | *1.2* | *0.9* | *0.9* | *0.8* |
| *Others* | *47* | *49* | *59* | *54* | *61* | *4.3* | *4.2* | *5.2* | *5.3* | *6.7* |
| Middle East | 89 | 74 | 71 | 54 | 69 | 8.1 | 6.5 | 6.2 | 5.3 | 7.5 |
| *Iran* | *55* | *40* | *45* | *27* | *40* | *4.9* | *3.5* | *3.9* | *2.7* | *4.4* |
| *Turkey* | *25* | *24* | *20* | *21* | *21* | *2.2* | *2.1* | *1.7* | *2.1* | *2.3* |
| *Others* | *10* | *10* | *6* | *5* | *7* | *0.9* | *0.8* | *0.6* | *0.5* | *0.8* |
| United States | 74 | 67 | 64 | 53 | 53 | 6.7 | 5.9 | 5.6 | 5.2 | 5.8 |
| Korea | 64 | 74 | 67 | 61 | 52 | 5.7 | 6.5 | 5.8 | 6.0 | 5.6 |
| Brazil | 37 | 31 | 32 | 38 | 35 | 3.3 | 2.7 | 2.8 | 3.8 | 3.9 |
| Canada | 19 | 17 | 15 | 19 | 12 | 1.7 | 1.5 | 1.4 | 1.9 | 1.4 |
| Others | 190 | 188 | 172 | 128 | 115 | 17.2 | 16.3 | 15.1 | 12.6 | 12.5 |
| **Total** | **1,108** | **1,151** | **1,143** | **1,018** | **916** | **100.0** | **100.0** | **100.0** | **100.0** | **100.0** |

*p* Preliminary
Note: Numbers may not necessarily add up due to rounding

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

**Table A.18**
**Principal Export Markets for Crude Oil**

| Country | 2004 | 2005 | 2006 | 2007 | 2008*p* | 2004 | 2005 | 2006 | 2007 | 2008*p* |
|---|---|---|---|---|---|---|---|---|---|---|
| | '000 tonnes | | | | | % share | | | | |
| India | 3,081 | 3,496 | 4,417 | 3,908 | 3,890 | 17.1 | 19.7 | 27.1 | 23.8 | 23.0 |
| Australia | 4,229 | 3,567 | 2,269 | 3,331 | 3,001 | 23.4 | 20.1 | 13.9 | 20.3 | 17.8 |
| Singapore | 890 | 1,638 | 1,285 | 1,607 | 2,497 | 4.9 | 9.2 | 7.9 | 9.8 | 14.8 |
| Thailand | 3,024 | 3,418 | 2,528 | 1,435 | 1,367 | 16.8 | 19.3 | 15.5 | 8.8 | 8.1 |
| Korea | 1,316 | 1,389 | 1,433 | 1,545 | 1,314 | 7.3 | 7.8 | 8.8 | 9.4 | 7.8 |
| Indonesia | 1,548 | 1,431 | 1,547 | 2,038 | 969 | 8.6 | 8.1 | 9.5 | 12.4 | 5.7 |
| Japan | 1,051 | 734 | 926 | 987 | 751 | 5.8 | 4.1 | 5.7 | 6.0 | 4.4 |
| The People's Republic of China | 1,036 | 240 | 79 | 240 | 597 | 5.7 | 1.4 | 0.5 | 1.5 | 3.5 |
| New Zealand | 205 | 299 | 424 | 381 | 356 | 1.1 | 1.7 | 2.6 | 2.3 | 2.1 |
| Philippines | 406 | 743 | 471 | 872 | 341 | 2.3 | 4.2 | 2.9 | 5.3 | 2.0 |
| United States | 682 | 314 | 282 | 46 | 165 | 3.8 | 1.8 | 1.7 | 0.3 | 1.0 |
| Others | 580 | 450 | 643 | - | 1,649 | 3.2 | 2.5 | 3.9 | - | 9.8 |
| **Total** | **18,047** | **17,719** | **16,304** | **16,390** | **16,898** | **100.0** | **100.0** | **100.0** | **100.0** | **100.0** |

*p* Preliminary
Note: Numbers may not necessarily add up due to rounding

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

**Table A.19**
**Principal Export Markets for LNG**

| Country | 2004 | 2005 | 2006 | 2007 | 2008*p* | 2004 | 2005 | 2006 | 2007 | 2008*p* |
|---|---|---|---|---|---|---|---|---|---|---|
| | '000 tonnes | | | | | % share | | | | |
| Japan | 12,284 | 13,664 | 12,360 | 13,426 | 14,223 | 59.8 | 63.1 | 57.4 | 59.2 | 62.2 |
| Korea | 4,599 | 4,713 | 5,748 | 6,135 | 6,132 | 22.4 | 21.8 | 26.7 | 27.1 | 26.8 |
| Chinese Taipei | 2,834 | 3,013 | 3,306 | 3,035 | 2,496 | 13.8 | 13.9 | 15.4 | 13.4 | 10.9 |
| Others | 808 | 251 | 120 | 72 | 23 | 3.9 | 1.2 | 0.6 | 0.3 | 0.1 |
| **Total** | **20,525** | **21,641** | **21,534** | **22,668** | **22,873** | **100.0** | **100.0** | **100.0** | **100.0** | **100.0** |

*p* Preliminary
Note: Numbers may not necessarily add up due to rounding

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

**Table A.20**
**External Debt and Debt Servicing**

| | 2004 | 2005 | 2006 | 2007 | 2008[2]*p* |
|---|---|---|---|---|---|
| | RM million | | | | |
| **Medium- and long-term debt:** | | | | | |
| **Gross borrowing** | **27,064** | **29,162** | **28,620** | **23,844** | **22,930** |
| *Federal Government* | *1,136* | *651* | *834* | *489* | *472* |
| *NFPEs* | *11,545* | *6,431* | *10,909* | *1,706* | *2,400* |
| *Private sector* | *14,383* | *22,080* | *16,877* | *21,650* | *20,058* |
| **Repayment and prepayment** | **25,172** | **34,959** | **28,538** | **25,699** | **13,243** |
| *Federal Government* | *1,015* | *4,154* | *3,887* | *4,803* | *946* |
| *NFPEs* | *12,645* | *13,911* | *13,197* | *7,840* | *2,068* |
| *Private sector* | *11,512* | *16,893* | *11,453* | *13,055* | *10,229* |
| **Net borrowing** | **1,892** | **-5,796** | **82** | **-1,855** | **9,688** |
| *Federal Government* | *120* | *-3,503* | *-3,053* | *-4,314* | *-473* |
| *NFPEs* | *-1,100* | *-7,480* | *-2,288* | *-6,134* | *331* |
| *Private sector* | *2,872* | *5,187* | *5,424* | *8,594* | *9,830* |
| **Outstanding debt** | **156,849** | **150,746** | **141,704** | **132,978** | **155,628** |
| *Federal Government* | *34,654* | *30,000* | *25,005* | *19,602* | *20,316* |
| *NFPEs* | *62,244* | *56,233* | *50,378* | *41,854* | *59,640* |
| *Private sector* | *59,951* | *64,513* | *66,322* | *71,521* | *75,672* |
| **Currency composition (% share)** | **100.0** | **100.0** | **100.0** | **100.0** | **100.0** |
| *US dollar* | *76.8* | *79.6* | *80.5* | *80.7* | *75.7* |
| *Japanese yen* | *12.8* | *11.7* | *11.4* | *11.2* | *12.8* |
| *Others* | *10.4* | *8.7* | *8.0* | *8.1* | *11.5* |
| **Short-term debt:** | | | | | |
| **Outstanding debt** | **43,737** | **46,953** | **42,800** | **54,468** | **80,012** |
| *Banking sector*[1] | *35,333* | *38,871* | *28,812* | *42,134* | *72,153* |
| *Non-bank private sector* | *8,404* | *8,082* | *13,988* | *12,334* | *7,859* |
| **Total external debt:** | **200,586** | **197,698** | **184,505** | **187,445** | **235,640** |
| **Total external debt (USD million)** | **52,786** | **51,790** | **51,736** | **56,027** | **67,226** |
| *% GNI* | *44.6* | *39.7* | *33.2* | *29.8* | *32.9* |
| *Annual change (%)* | *7.4* | *-1.4* | *-6.7* | *1.6* | *n.a.* |
| **Total servicing (including short-term interest payment)** | **24,866** | **32,800** | **32,257** | **26,562** | **20,382** |
| *of which:* | | | | | |
| Medium- and long-term debt | | | | | |
| **Repayment (excluding prepayment)** | **18,675** | **25,471** | **23,759** | **19,105** | **12,776** |
| *Federal Government* | *1,015* | *4,154* | *3,887* | *4,803* | *946* |
| *NFPEs* | *10,713* | *10,166* | *11,311* | *5,035* | *2,017* |
| *Private sector* | *6,947* | *11,152* | *8,561* | *9,267* | *9,812* |
| **Interest payment** | **5,443** | **6,101** | **6,561** | **5,126** | **6,394** |
| *Federal Government* | *1,759* | *1,729* | *1,678* | *1,426* | *1,154* |
| *NFPEs* | *2,684* | *3,182* | *3,511* | *2,282* | *2,521* |
| *Private sector* | *1,000* | *1,190* | *1,372* | *1,419* | *2,719* |
| **Debt service ratio (% of exports of goods and services)** | | | | | |
| **Total debt** | **4.5** | **5.3** | **4.8** | **3.8** | **2.7** |
| Medium- and long-term debt | 4.4 | 5.1 | 4.5 | 3.4 | 2.5 |
| *Federal Government* | *0.5* | *1.0* | *0.8* | *0.9* | *0.3* |
| *NFPEs* | *2.4* | *2.2* | *2.2* | *1.0* | *0.6* |
| *Private sector* | *1.5* | *2.0* | *1.5* | *1.5* | *1.6* |

[1] Excludes currency and deposits held by non-residents with resident banking institutions
[2] Effective from the first quarter of 2008, the external debt data of Malaysia has been redefined to treat entities in Labuan International Business and Financial Centre (Labuan IBFC) as residents
*p* Preliminary
n.a. Not available
Note: Numbers may not necessarily add up due to rounding

Source: Ministry of Finance, Malaysia and Bank Negara Malaysia

**Table A.21**
**Consumer Price Index**

| | Weights (%) (2000=100) | 2004 | 2005 |
|---|---|---|---|
| | | Annual Change (%) | |
| Total | 100.0 | 1.4 | 3.0 |
| *of which:* | | | |
| Food | 33.8 | 2.2 | 3.6 |
| Beverages and tobacco | 3.1 | 7.8 | 10.5 |
| Clothing and footwear | 3.4 | -1.8 | -1.0 |
| Gross rent, fuel and power | 22.4 | 1.0 | 1.2 |
| Furniture, furnishings and household equipment and operation | 5.3 | 0.4 | 2.0 |
| Medical care and health expenses | 1.8 | 1.4 | 1.6 |
| Transport and communication | 18.8 | 0.8 | 4.4 |
| Recreation, entertainment, education and cultural services | 5.9 | -0.1 | 0.5 |
| Miscellaneous goods and services | 5.5 | 1.8 | 2.4 |

| | Weights (%) (2005=100)[1] | 2006 | 2007 | 2008 |
|---|---|---|---|---|
| | | Annual Change (%) | | |
| Total | 100.0 | 3.6 | 2.0 | 5.4 |
| *of which:* | | | | |
| Food and non-alcoholic beverages | 31.4 | 3.4 | 3.0 | 8.8 |
| Alcoholic beverages and tobacco | 1.9 | 6.9 | 7.8 | 7.3 |
| Clothing and footwear | 3.1 | -1.3 | -1.4 | -0.5 |
| Housing, water, electricity, gas and other fuels | 21.4 | 1.5 | 1.3 | 1.6 |
| Furnishing, household equipment and routine household maintainance | 4.3 | 1.1 | 1.1 | 3.0 |
| Health | 1.4 | 2.1 | 1.6 | 2.2 |
| Transport | 15.9 | 11.0 | 2.3 | 8.8 |
| Communication | 5.1 | -1.4 | -1.2 | -0.6 |
| Recreation services and culture | 4.6 | 0.7 | 1.4 | 1.8 |
| Education | 1.9 | 1.6 | 1.8 | 2.3 |
| Restaurants and hotels | 3.0 | 3.7 | 3.7 | 6.6 |
| Miscellaneous goods and services | 6.0 | 2.2 | 1.0 | 3.3 |

[1] Effective from 2006, the Consumer Price Index has been revised to the new base year 2005=100, from 2000=100 previously

Source: Department of Statistics, Malaysia

**Table A.22**
**Producer Price Index**

| | Weights (%) (1989=100) | 2004 | 2005 | | Weights (%) (2000=100)[1] | 2006 | 2007 | 2008 |
|---|---|---|---|---|---|---|---|---|
| | | Annual Change (%) | | | | Annual Change (%) | | |
| Total | 100.0 | 8.9 | 6.8 | Total | 100.0 | 5.1 | 6.7 | 8.2 |
| *of which:* | | | | *of which:* | | | | |
| Food and live animals chiefly for food | 14.9 | 3.6 | 3.8 | Food and live animal | 5.3 | 3.1 | 8.5 | 12.2 |
| Beverages and tobacco | 2.1 | 1.6 | 1.9 | Beverages and tobacco | 1.0 | 5.8 | -0.4 | 3.2 |
| Crude materials, inedible except fuels | 18.0 | 6.6 | 3.0 | Crude materials, inedible except fuels | 4.4 | 14.5 | 14.1 | 5.6 |
| Mineral fuels, lubricants and related materials | 18.8 | 22.3 | 26.0 | Mineral fuels, lubricants and related materials | 11.9 | 11.0 | 3.0 | 32.1 |
| Animal and vegetable oils and fats | 8.5 | 13.2 | -14.8 | Animal and vegetable oils and fats | 3.8 | -0.3 | 46.7 | 23.4 |
| Chemicals and related products n.e.c | 4.4 | 4.3 | 2.2 | Chemicals and related products n.e.s | 5.1 | 3.4 | 3.6 | 10.1 |
| Manufactured goods classified chiefly by material | 10.8 | 2.5 | 2.5 | Manufactured goods classified chiefly by material | 11.0 | 3.7 | 4.7 | 8.6 |
| Machinery and transport equipment | 18.4 | 0.1 | 0.6 | Machinery and transport equipment | 50.5 | 3.5 | 4.6 | -1.8 |
| Miscellaneous manufactured articles | 3.6 | 0.6 | 1.8 | Miscellaneous manufactured articles | 6.7 | 3.5 | 1.5 | 1.9 |
| Commodities and transactions not classified elsewhere in the S.I.T.C | 0.6 | 0.2 | 0.0 | Commodities and transactions not classified elsewhere in the S.I.T.C. | 0.4 | 13.4 | 12.3 | 3.9 |
| Local Production | 79.3 | 10.3 | 7.9 | Local Production | 65.6 | 6.7 | 7.5 | 10.3 |
| Import | 20.7 | 2.0 | 1.5 | Import | 34.4 | 2.2 | 4.7 | 4.2 |

[1] Effective from 2006, the Producer Price Index has been revised to the new base year 2000=100, from 1989=100 previously
n.e.c: Not elsewhere classified
n.e.s: Not elsewhere specified
S.I.T.C.: Standard International Trade Classification

Source: Department of Statistics, Malaysia

**Table A.23**
**Broad Money (M3)**

| | Annual change | | | | | As at end |
|---|---|---|---|---|---|---|
| | 2004 | 2005 | 2006 | 2007 | 2008 | 2008 |
| | RM million | | | | | |
| Broad money (M3)[1] | 68,167 | 51,609 | 87,467 | 72,436 | 99,042 | 931,780 |
| Currency in circulation[2] | 2,593 | 1,629 | 3,335 | 2,746 | 4,188 | 40,435 |
| Demand deposits | 10,031 | 8,683 | 11,705 | 24,247 | 11,031 | 143,413 |
| Broad quasi-money | 55,543 | 41,297 | 72,427 | 45,444 | 83,824 | 747,933 |
| *Fixed deposits* | *25,192* | *4,940* | *31,940* | *10,701* | *27,969* | *429,981* |
| *Savings deposits* | *6,129* | *1,947* | *5,195* | *8,703* | *7,786* | *92,218* |
| *NIDs* | *8,179* | *12,785* | *14,321* | *-15,279* | *144* | *31,127* |
| *Repos* | *13,337* | *17,260* | *11,799* | *-72,366* | *-3,046* | *159* |
| *Foreign currency deposits* | *2,998* | *2,467* | *3,218* | *1,570* | *16,649* | *39,306* |
| *Other deposits* | *-291* | *1,898* | *5,956* | *112,116* | *34,323* | *155,142* |
| **Factors Affecting M3** | | | | | | |
| Net claims on Government | -16,599 | -5,204 | 8,317 | -641 | 33,461 | 31,220 |
| *Claims on Government* | *4,536* | *-2,152* | *1,614* | *-490* | *33,702* | *70,117* |
| *Less: Government deposits* | *21,135* | *3,052* | *-6,703* | *151* | *241* | *38,896* |
| Claims on private sector | 30,524 | 44,501 | 34,714 | 53,407 | 94,975 | 824,466 |
| *Loans* | *39,753* | *44,840* | *36,779* | *50,926* | *76,655* | *724,302* |
| *Securities* | *-9,229* | *-339* | *-2,065* | *2,481* | *18,321* | *100,164* |
| Net foreign assets | 90,626 | 1,832 | 52,745 | 71,893 | -52,515 | 331,998 |
| *Bank Negara Malaysia*[3] | *83,728* | *13,550* | *25,158* | *45,296* | *-18,250* | *317,445* |
| *Banking system* | *6,898* | *-11,719* | *27,587* | *26,597* | *-34,265* | *14,552* |
| Other influences | -36,383 | 10,480 | -8,309 | -52,223 | 23,121 | -255,904 |

[1] Excludes interplacements among banking institutions
[2] Excludes holdings by banking system
[3] Includes exchange rate revaluation loss/gain

**Table A.24**
**Money Supply: Annual Change and Growth Rates**

| | 2004 | | 2005 | | 2006 | | 2007 | | 2008 | |
|---|---|---|---|---|---|---|---|---|---|---|
| | RM million | % | RM million | % | RM million | % | RM million | % | RM million | % |
| Currency in circulation | 2,516 | 9.6 | 1,561 | 5.5 | 3,342 | 11.1 | 2,728 | 8.1 | 4,188 | 11.6 |
| Demand deposits with commercial banks and Islamic banks | 9,594 | 12.6 | 8,227 | 9.6 | 13,688 | 14.5 | 24,913 | 23.1 | 9,801 | 7.4 |
| M1[1] | 12,110 | 11.8 | 9,788 | 8.5 | 17,029 | 13.7 | 27,640 | 19.6 | 13,988 | 8.3 |
| Other deposits with commercial banks and Islamic banks[2] | 96,089 | 29.4 | 73,923 | 17.5 | 89,308 | 18.0 | 41,552 | 7.1 | 92,514 | 14.7 |
| Deposits with other banking institutions[3,4] | -40,032 | -32.4 | -32,102 | -38.4 | -18,871 | -36.7 | 3,244 | 9.9 | -7,460 | -20.8 |
| M3[5] | 68,167 | 12.3 | 51,609 | 8.3 | 87,467 | 13.0 | 72,436 | 9.5 | 99,042 | 11.9 |

1 Comprising currency in circulation and demand deposits of the private sector
2 Comprising savings and fixed deposits, negotiable instruments of deposits (NIDs), repos and foreign currency deposits of the private sector placed with commercial banks and Islamic banks
3 Comprising fixed deposits and repos of the private sector placed with finance companies, merchant banks/investment banks and discount houses. Also includes savings deposits with finance companies, negotiable instruments of deposits (NIDs) with finance companies and merchant banks/investment banks, foreign currency deposits placed with merchant banks/investment banks and call deposits with discount houses. Excludes interplacements among the banking institutions
4 The large decline since 2004 reflected the absorption of finance companies by commercial banks
5 Comprising M1 plus other deposits of the private sector placed with commercial banks and Islamic banks and deposits of the private sector placed with other banking institutions, namely the finance companies, merchant banks/investment banks and discount houses

**Table A.25**
**Interest Rates (%)**

| | Average rates at end-year | | | | | | Average rates at end-month in 2008 | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | Jan. | Feb. | Mar. | Apr. | May | Jun. | Jul. | Aug. | Sept. | Oct. | Nov. | Dec. |
| Overnight interbank | 2.73 | 2.74 | 2.70 | 2.72 | 3.38 | 3.50 | 3.50 | 3.50 | 3.50 | 3.50 | 3.50 | 3.50 | 3.49 | 3.50 | 3.49 | 3.50 | 3.45 | 3.30 |
| 1-week interbank | 2.76 | 2.80 | 2.74 | 2.75 | 3.42 | 3.52 | 3.52 | 3.52 | 3.52 | 3.52 | 3.52 | 3.52 | 3.52 | 3.52 | 3.52 | 3.52 | 3.52 | 3.27 |
| 1-month interbank | 2.87 | 2.99 | 2.86 | 2.84 | 3.54 | 3.54 | 3.55 | 3.55 | 3.55 | 3.55 | 3.56 | 3.56 | 3.56 | 3.56 | 3.56 | 3.57 | 3.49 | 3.30 |
| Commercial banks | | | | | | | | | | | | | | | | | | |
| Fixed deposit: | | | | | | | | | | | | | | | | | | |
| 3 month | 3.20 | 3.00 | 3.00 | 3.02 | 3.19 | 3.15 | 3.15 | 3.14 | 3.14 | 3.14 | 3.14 | 3.14 | 3.14 | 3.14 | 3.14 | 3.14 | 3.06 | 3.04 |
| 12 month | 4.00 | 3.70 | 3.70 | 3.70 | 3.73 | 3.70 | 3.70 | 3.70 | 3.70 | 3.70 | 3.70 | 3.70 | 3.70 | 3.70 | 3.70 | 3.70 | 3.60 | 3.50 |
| Savings deposit | 2.12 | 1.86 | 1.58 | 1.41 | 1.48 | 1.44 | 1.44 | 1.44 | 1.43 | 1.42 | 1.42 | 1.41 | 1.41 | 1.41 | 1.42 | 1.42 | 1.39 | 1.40 |
| Base lending rate (BLR) | 6.39 | 6.00 | 5.98 | 6.20 | 6.72 | 6.72 | 6.72 | 6.72 | 6.72 | 6.72 | 6.72 | 6.72 | 6.72 | 6.72 | 6.72 | 6.72 | 6.66 | 6.48 |
| Treasury bills (91 days) | 2.82 | 2.77 | 1.96 | 2.96 | 3.23 | 3.39 | 3.33 | 3.34 | 3.45 | 3.26 | 3.50 | 3.49 | 3.31 | 3.49 | 3.49 | 3.58 | 3.09 | 2.94 |
| Government securities (1 year) | 2.94 | 2.93 | 2.24 | 3.30 | 3.55 | 3.53 | 3.37 | 3.37 | 3.38 | 3.37 | 3.53 | 3.93 | 3.74 | 3.73 | 3.73 | 3.69 | 3.17 | 2.89 |
| Government securities (5 years) | 3.15 | 4.28 | 3.64 | 3.73 | 3.70 | 3.78 | 3.49 | 3.54 | 3.52 | 3.52 | 3.83 | 4.27 | 4.02 | 4.04 | 4.06 | 4.05 | 3.41 | 3.00 |
| Private Debt Securities | | | | | | | | | | | | | | | | | | |
| AAA | | | | | | | | | | | | | | | | | | |
| 3-years | 3.73 | 4.47 | 3.72 | 3.95 | 4.01 | 4.07 | 4.00 | 4.02 | 4.08 | 4.19 | 4.25 | 4.66 | 4.75 | 4.69 | 4.60 | 4.54 | 4.39 | 4.17 |
| 5-years | 4.32 | 5.22 | 4.39 | 4.38 | 4.24 | 4.28 | 4.17 | 4.20 | 4.29 | 4.46 | 4.52 | 4.99 | 5.09 | 5.01 | 4.91 | 4.84 | 4.72 | 4.48 |
| AA | | | | | | | | | | | | | | | | | | |
| 3-years | 4.48 | 5.05 | 4.27 | 4.36 | 4.38 | 4.39 | 4.32 | 4.32 | 4.39 | 4.56 | 4.62 | 5.10 | 5.21 | 5.17 | 5.05 | 5.06 | 4.98 | 4.95 |
| 5-years | 5.05 | 5.89 | 5.00 | 4.81 | 4.71 | 4.64 | 4.58 | 4.59 | 4.69 | 4.87 | 4.93 | 5.46 | 5.59 | 5.54 | 5.42 | 5.40 | 5.32 | 5.31 |
| A | | | | | | | | | | | | | | | | | | |
| 3-years | 5.88 | 6.22 | 5.82 | 5.94 | 5.91 | 6.06 | 5.96 | 5.90 | 5.97 | 6.07 | 6.16 | 6.61 | 6.83 | 6.78 | 6.90 | 6.83 | 6.77 | 6.90 |
| 5-years | 6.63 | 7.13 | 6.66 | 6.70 | 6.53 | 6.51 | 6.37 | 6.32 | 6.40 | 6.53 | 6.59 | 7.07 | 7.30 | 7.23 | 7.36 | 7.29 | 7.26 | 7.43 |
| BBB | | | | | | | | | | | | | | | | | | |
| 3-years | 9.12 | 9.96 | 9.77 | 9.44 | 9.57 | 9.71 | 9.66 | 9.60 | 9.74 | 9.73 | 9.82 | 9.94 | 10.16 | 10.17 | 10.34 | 10.37 | 10.23 | 10.32 |
| 5-years | 10.17 | 11.01 | 10.81 | 10.41 | 10.51 | 10.72 | 10.67 | 10.61 | 10.76 | 10.70 | 10.77 | 10.96 | 11.06 | 11.09 | 11.31 | 11.32 | 11.13 | 11.36 |
| BB & below | | | | | | | | | | | | | | | | | | |
| 3-years | 11.16 | 11.81 | 11.91 | 11.97 | 12.06 | 11.92 | 11.89 | 11.73 | 11.94 | 11.83 | 11.95 | 12.08 | 12.32 | 12.41 | 12.63 | 12.62 | 12.56 | 12.68 |
| 5-years | 12.26 | 12.94 | 13.10 | 13.04 | 13.13 | 13.16 | 13.01 | 12.94 | 13.14 | 13.02 | 13.08 | 13.18 | 13.46 | 13.54 | 13.89 | 13.77 | 13.64 | 13.86 |

**Table A.26**
**Movements of the Ringgit**

| | RM to one unit of foreign currency[1] | | | Annual change (%) | | Change (%) |
|---|---|---|---|---|---|---|
| | 2005 | 2007 | 2008 | 2007 | 2008 | 21 Jul.'05 - |
| | Jul.21[2] | End-Dec. | | | | Dec. 2008 |
| SDR | 5.5049 | 5.2190 | 5.3616 | 1.7 | -2.7 | 2.7 |
| US dollar | 3.8000 | 3.3065 | 3.4640 | 6.8 | -4.5 | 9.7 |
| Singapore dollar | 2.2570 | 2.2938 | 2.4070 | 0.4 | -4.7 | -6.2 |
| 100 Japanese yen | 3.3745 | 2.9534 | 3.8327 | 0.5 | -22.9 | -12.0 |
| Pound sterling | 6.6270 | 6.6070 | 4.9989 | 4.9 | 32.2 | 32.6 |
| Swiss franc | 2.9588 | 2.9445 | 3.2715 | -1.8 | -10.0 | -9.6 |
| Euro | 4.6212 | 4.8756 | 4.8759 | -4.7 | -0.0 | -5.2 |
| 100 Thai baht | 9.0681 | 9.8159 | 9.9398 | -0.0 | -1.2 | -8.8 |
| 100 Indonesian rupiah | 0.0386 | 0.0352 | 0.0316 | 11.5 | 11.3 | 22.1 |
| 100 Korean won | 0.3665 | 0.3532 | 0.2750 | 7.5 | 28.4 | 33.3 |
| 100 Philippine peso | 6.8131 | 8.0158 | 7.2774 | -10.1 | 10.1 | -6.4 |
| Chinese renminbi | 0.4591 | 0.4527 | 0.5076 | -0.1 | -10.8 | -9.6 |

[1] US dollar rates are the average of buying and selling rates at noon in the Kuala Lumpur Interbank Foreign Exchange Market
Rates for foreign currencies other than US dollar are cross rates derived from rates of these currencies against the US dollar and the RM/US dollar rate
[2] Ringgit shifted from a fixed exchange rate against the US dollar to a managed float against a basket of currencies

**Table A.27**
**Housing Credit Institutions**

| | Year of establishment | Objective | Lending rate for new housing loans (%) | | No. of branches | |
|---|---|---|---|---|---|---|
| | | | 2007 | 2008 | 2007 | 2008 |
| Commercial banks | - | | 4.4[1,2] | 4.6[1,2] | 2,125[3] | 4,018[3] |
| Treasury Housing Loans Division | 1970 | To provide housing loans to Government employees | 4.0[1] | 4.0[1] | 2 | 2 |
| Bank Kerjasama Rakyat Malaysia Berhad | 1954 | A co-operative society which collects deposits and provides banking facilities according to Shariah principles | 7.3[1] | 7.3[1] | 112 | 117 |
| Malaysia Building Society Berhad | 1950 | To be a consumer driven financial institution offering property lending and deposit taking activities leading to wealth management creation for its valued customers | 5.5[1] | 5.2[1] | 26 | 28 |
| Borneo Housing Mortgage Finance Berhad | 1958 | To provide housing loans mainly to Sabah and Sarawak State Government employees | 7.25 ~ 8.25 | 7.25 ~ 8.25 | 2 | 2 |
| Bank Simpanan Nasional | 1974 | To promote and mobilise savings particularly from small savers and to inculcate the habit of thrift and savings | 6.73[1] | 6.37[1] | 375 | 374 |
| Sabah Credit Corporation | 1955 | To uplift the social economic development of Malaysians in Sabah through the provision of easy access to financial credit | 3.0 ~ 7.5 | 3.0 ~ 7.5 | 10 | 10 |

[1] 12-month average lending rate
[2] Excludes Islamic banks
[3] Includes Islamic banks

Source: Bank Negara Malaysia and various housing credit institutions

**Table A.28**
**Outstanding Housing Loans**

| | 2007 | 2008*p* | 2007 | 2008*p* | 2007 | 2008*p* |
|---|---|---|---|---|---|---|
| | RM million | | Annual change (%) | | % share | |
| Commercial banks[1] | 174,357 | 192,185 | 7.4 | 10.2 | 82 | 82 |
| Treasury Housing Loans Division | 26,822 | 27,393 | 5.8 | 2.1 | 13 | 12 |
| Bank Kerjasama Rakyat Malaysia Berhad | 3,769 | 4,417 | -12.5 | 17.2 | 2 | 2 |
| Malaysia Building Society Berhad | 4,413 | 5,141 | 25.6 | 16.5 | 2 | 2 |
| Borneo Housing Mortgage Finance Berhad | 716 | 713 | -0.7 | -0.5 | … | … |
| Bank Simpanan Nasional | 2,656 | 2,954 | 16.9 | 11.2 | 1 | 1 |
| Sabah Credit Corporation | 190 | 179 | -6.9 | -5.8 | … | … |
| **Total** | **212,923** | **232,982** | **7.1** | **9.4** | **100** | **100** |

[1] Includes Islamic banks
*p* Preliminary
… Negligible

Source: Bank Negara Malaysia and various housing credit institutions

**Table A.29**
**Approved Housing Loans**

| | 2007 | 2008*p* | 2007 | 2008*p* | 2007 | 2008*p* |
|---|---|---|---|---|---|---|
| | RM million | | Annual change (%) | | % share | |
| Commercial banks[1] | 48,153 | 59,170 | 46.6 | 22.9 | 85 | 85 |
| Treasury Housing Loans Division | 5,830 | 7,583 | 41.0 | 30.1 | 10 | 11 |
| Bank Kerjasama Rakyat Malaysia Berhad | 573 | 297 | -9.5 | -48.2 | 1 | 1 |
| Malaysia Building Society Berhad | 1,729 | 1,566 | -3.1 | -9.4 | 3 | 2 |
| Borneo Housing Mortgage Finance Berhad | 63 | 68 | -10.4 | 7.9 | … | … |
| Bank Simpanan Nasional | 595 | 714 | -56.9 | 20.0 | 1 | 1 |
| Sabah Credit Corporation | 15 | 13 | 33.0 | -13.0 | … | … |
| **Total** | **56,958** | **69,411** | **39.4** | **21.9** | **100** | **100** |

[1] Includes Islamic banks
*p* Preliminary
… Negligible

Source: Bank Negara Malaysia and various housing credit institutions

**Table A.30**
**Financing of the Economy**

| By customer / By financing type/ institutions | Businesses[1] | | Households | Government | Total Financing |
|---|---|---|---|---|---|
| | Total | of which: SMEs | | | |
| | RM million | | | | |
| **Net Change in Financing 2007** | | | | | |
| **Financial Intermediaries** | | | | | |
| Banking Institutions | 27,066 | 9,476 | 24,485 | (328) | 51,223 |
| Development Financial Institutions (DFIs)[2] | 3,427 | 877 | 6,096 | - | 9,523 |
| Other Domestic Intermediaries[3] | 9,696 | (218) | 1,769 | - | 11,465 |
| **Capital Market** | | | | | |
| Bond Market[4] | 18,989 | - | - | 24,780 | 43,769 |
| Equity Market | 7,126 | - | - | - | 7,126 |
| **External Financing** | | | | | |
| Foreign Direct Investment | 29,081 | - | - | - | 29,081 |
| External Loan[5, 6] | 3,546 | - | - | (13,926) | (10,381) |
| **Total** | **98,930** | **10,135** | **32,350** | **10,526** | **141,806** |
| **Net Change in Financing 2008** | | | | | |
| **Financial Intermediaries** | | | | | |
| Banking Institutions | 44,932 | 10,683 | 32,458 | 4,921 | 82,311 |
| Development Financial Institutions (DFIs)[2] | 2,082 | 258 | 7,578 | - | 9,660 |
| Other Domestic Intermediaries[3] | 2,586 | 128 | 1,046 | - | 3,633 |
| **Capital Market** | | | | | |
| Bond Market[4] | 16,492 | - | - | 33,601 | 50,094 |
| Equity Market | 5,477 | - | - | - | 5,477 |
| **External Financing** | | | | | |
| Foreign Direct Investment | 26,665 | - | - | - | 26,665 |
| External Loan[5, 6] | 17,128 | - | - | 5,792 | 22,921 |
| **Total** | **115,362** | **11,069** | **41,082** | **44,315** | **200,759** |

1 Businesses include non-bank financial institutions, domestic non-business entities and foreign entities
2 Refers to DFIs governed under the Development Financial Institutions Act, 2002
3 Other domestic intermediaries include insurance companies, Employees Provident Fund (EPF), housing credit institutions, leasing and factoring companies and the Treasury Housing Loan Division
4 Bond Market refers to outstanding private debt securities (PDS) and all Malaysian Government Securities. Data excludes Cagamas bonds and issuances by non-residents. PDS includes irredeemable convertible unsecured loan stocks (ICULS) and medium term notes (MTN) issued by the corporate sector
5 Based on the new classification of external debt, which has been redefined to treat entities in Labuan International Bussiness and Financial Centre (Labuan IBFC) as residents, effective from first quarter of 2008
6 External financing of Government includes financing to non-financial public enterprises (NFPEs)

**Table A.31**
**Consolidated Public Sector Finance**

| | 2005 | 2006 | 2007 | 2008*p* | 2009*f* |
|---|---|---|---|---|---|
| | RM billion | | | | |
| Revenue[1] | 95.0 | 102.0 | 110.7 | 125.6 | 125.4 |
| *% growth* | *-0.1* | *7.4* | *8.6* | *13.4* | *-0.1* |
| Operating expenditure | 106.6 | 117.7 | 135.0 | 163.9 | 171.8 |
| *% growth* | *5.5* | *10.4* | *14.6* | *21.4* | *4.8* |
| Current surplus of NFPEs[2] | 85.0 | 100.7 | 130.4 | 120.9 | 112.5 |
| **Current balance** | **73.3** | **84.9** | **106.1** | **82.5** | **66.1** |
| ***% of GDP*** | ***14.1*** | ***14.8*** | ***16.5*** | ***11.1*** | ***9.4*** |
| Net development expenditure[3] | 66.1 | 86.5 | 95.1 | 106.7 | 103.1 |
| *% growth* | *16.5* | *31.0* | *9.9* | *12.2* | *-3.3* |
| General government[4] | 31.7 | 40.8 | 44.7 | 47.9 | 56.5 |
| NFPEs | 34.4 | 45.7 | 50.3 | 58.8 | 46.6 |
| **Overall balance** | **7.3** | **-1.6** | **11.1** | **-24.2** | **-37.0** |
| ***% of GDP*** | ***1.4*** | ***-0.3*** | ***1.7*** | ***-3.3*** | ***-5.2*** |

[1] Excludes transfers within general Government
[2] Refers to 30 NFPEs in 2004 onwards
[3] Adjusted for transfers and net lendings within public sector
[4] Comprises Federal Government, state and local governments and statutory bodies
[p] Preliminary
[f] Forecast
Note: Numbers may not add up due to rounding

Source: Ministry of Finance and non-financial public enterprises (NFPEs)

**Table A.32**
**Major Advanced Countries: Key Economic Indicators**

| | 2004 | 2005 | 2006 | 2007 | 2008*e* | 2009*f* |
|---|---|---|---|---|---|---|
| | Annual change (%) | | | | | |
| **REAL GDP** | | | | | | |
| United States | 3.6 | 2.9 | 2.8 | 2.0 | 1.1 | -2.0 |
| Japan | 2.7 | 1.9 | 2.1 | 2.4 | -0.6 | -2.6 |
| Euro Area | 1.9 | 1.9 | 2.8 | 2.4 | 0.8 | -3.2 ~ -2.2 |
| *Germany* | *1.2* | *0.8* | *3.0* | *2.5* | *1.3* | *-2.5* |
| United Kingdom | 2.8 | 2.1 | 2.8 | 3.0 | 0.7 | -2.8 |
| **INFLATION** | | | | | | |
| United States | 2.7 | 3.4 | 3.2 | 2.9 | 3.8 | -0.2 |
| Japan | 0.0 | -0.3 | 0.3 | 0.0 | 1.4 | -1.1 |
| Euro Area | 2.1 | 2.2 | 2.2 | 2.1 | 3.3 | 0.1 ~ 0.7 |
| *Germany* | *1.8* | *1.9* | *1.8* | *2.3* | *2.9* | *0.8* |
| United Kingdom | 1.4 | 2.0 | 2.3 | 2.3 | 3.6 | 2.9 |
| | % of labour force | | | | | |
| **UNEMPLOYMENT** | | | | | | |
| United States | 5.4 | 4.8 | 4.4 | 4.9 | 7.2 | 8.4 |
| Japan | 4.5 | 4.4 | 4.0 | 3.7 | 4.3 | 4.5 |
| Euro Area | 8.9 | 8.7 | 7.9 | 7.2 | 8.0 | 9.3 |
| *Germany* | *10.4* | *10.3* | *9.0* | *7.9* | *7.2* | *7.7* |
| United Kingdom | 4.7 | 5.1 | 5.5 | 5.2 | 6.5 | 8.2 |
| | % of GDP | | | | | |
| **CURRENT ACCOUNT BALANCE** | | | | | | |
| United States | -5.3 | -5.9 | -6.0 | -5.3 | -4.6 | -3.3 |
| Japan | 3.7 | 3.6 | 3.9 | 4.8 | 4.0 | 3.7 |
| Euro Area | 1.2 | 0.5 | 0.3 | 0.2 | -0.5 | -0.4 |
| *Germany* | *4.7* | *5.2* | *6.1* | *7.6* | *7.3* | *5.2* |
| United Kingdom | -2.1 | -2.6 | -3.4 | -3.8 | -3.6 | -3.4 |
| **FISCAL BALANCE[1]** | | | | | | |
| United States | -4.4 | -3.3 | -2.2 | -2.9 | -6.4 | -12.3 |
| Japan | -6.2 | -5.0 | -4.0 | -3.4 | -4.7 | -7.1 |
| Euro Area | -3.0 | -2.5 | -1.3 | -0.6 | -1.5 | -4.0 |
| *Germany* | *-3.8* | *-3.3* | *-1.5* | *-0.2* | *-0.3* | *-2.9* |
| United Kingdom | -3.4 | -3.3 | -2.6 | -2.7 | -3.5 | -7.2 |

[1] Refers to general government fiscal balance
*e* Estimate
*f* Forecast

Source: International Monetary Fund (IMF) and National Authorities

**Table A.33**
**East Asia: Key Economic Indicators**

| | 2004 | 2005 | 2006 | 2007 | 2008*e* | 2009*f* |
|---|---|---|---|---|---|---|
| **REAL GDP** | Annual change (%) | | | | | |
| **Regional Countries** | | | | | | |
| The People's Republic of China | 10.1 | 10.4 | 11.6 | 13.0 | 9.0 | 8.0 |
| Korea | 4.7 | 4.2 | 5.1 | 5.0 | 2.5 | -2.0 |
| Chinese Taipei | 6.1 | 4.2 | 4.8 | 5.7 | 0.1 | -3.0 |
| Singapore | 9.3 | 7.3 | 8.4 | 7.8 | 1.1 | -5.0 ~ -2.0 |
| Hong Kong SAR | 8.5 | 7.1 | 7.0 | 6.4 | 2.5 | -3.0 ~ -2.0 |
| Malaysia | 6.8 | 5.3 | 5.8 | 6.3 | 4.6 | -1.0 ~ 1.0 |
| Thailand | 6.3 | 4.6 | 5.2 | 4.9 | 2.6 | -1.0 ~ 0.0 |
| Indonesia | 5.0 | 5.7 | 5.5 | 6.3 | 6.1 | 4.0 |
| Philippines | 6.4 | 5.0 | 5.4 | 7.2 | 4.6 | 3.7 ~ 4.4 |
| **CONSUMER PRICES** | Annual change (%) | | | | | |
| **Regional Countries** | | | | | | |
| The People's Republic of China | 3.9 | 1.8 | 1.5 | 4.8 | 5.9 | 0.5 |
| Korea | 3.6 | 2.8 | 2.2 | 2.5 | 4.7 | 2.2 |
| Chinese Taipei | 1.6 | 2.3 | 0.6 | 1.8 | 3.5 | 2.5 |
| Singapore | 1.7 | 0.5 | 1.0 | 2.1 | 6.5 | 3.3 |
| Hong Kong SAR[1] | -0.4 | 1.0 | 2.0 | 2.0 | 4.3 | 1.6 |
| Malaysia | 1.4 | 3.0 | 3.6 | 2.0 | 5.4 | 1.5 ~ 2.0 |
| Thailand | 2.7 | 4.5 | 4.7 | 2.3 | 5.5 | 3.2 |
| Indonesia | 6.1 | 10.5 | 13.1 | 6.3 | 10.2 | 7.3 |
| Philippines | 5.5 | 7.6 | 6.2 | 2.8 | 9.3 | 2.5 ~ 4.5 |
| **CURRENT ACCOUNT BALANCE** | % of GDP | | | | | |
| **Regional Countries** | | | | | | |
| The People's Republic of China | 3.6 | 7.2 | 9.4 | 11.3 | 9.5 | 9.2 |
| Korea | 4.1 | 1.9 | 0.6 | 0.6 | -1.3 | -0.7 |
| Chinese Taipei | 6.0 | 4.9 | 7.2 | 8.6 | 7.8 | 6.5 |
| Singapore | 16.7 | 18.6 | 21.8 | 24.3 | 19.1 | 17.0 |
| Hong Kong SAR | 9.5 | 11.4 | 12.1 | 13.5 | 12.5 | 11.2 |
| Malaysia | 12.1 | 15.0 | 16.3 | 15.6 | 17.5 | 11.3 |
| Thailand | 1.7 | -4.3 | 1.1 | 6.4 | 3.1 | 2.0 |
| Indonesia | 0.6 | 0.1 | 3.0 | 2.5 | 0.1 | -0.1 |
| Philippines | 1.9 | 2.0 | 4.5 | 4.4 | 2.4 | 2.2 |
| **FISCAL BALANCE[2]** | % of GDP | | | | | |
| **Regional Countries** | | | | | | |
| The People's Republic of China[3] | -1.5 | -1.3 | -0.7 | 0.9 | -0.1 | -2.0 |
| Korea[3] | 2.2 | 1.9 | 1.8 | 3.8 | 1.4 | -0.8 |
| Chinese Taipei | -2.3 | -1.8 | -0.8 | -0.1 | -1.9 | -3.2 |
| Singapore[4] | 5.8 | 8.2 | 7.2 | 9.5 | -0.8 | -3.5 |
| Hong Kong SAR[4] | -0.3 | 1.0 | 4.0 | 7.7 | -0.3 | -2.4 |
| Malaysia | -4.1 | -3.6 | -3.3 | -3.2 | -4.8 | -7.6 |
| Thailand[5] | 0.3 | 0.2 | 0.1 | -1.2 | -3.5 | -4.0 |
| Indonesia | -1.4 | -0.3 | -1.0 | -1.2 | -1.1 | -2.6 |
| Philippines | -3.8 | -2.7 | -1.1 | -0.2 | -0.9 | -2.2 |

1 Refers to composite prices
2 Refers to central government fiscal balance
3 Refers to general government fiscal balance
4 Refers to fiscal year starting April to March of the following year
5 Refers to fiscal year starting October to September of the following year
*e* Estimates
*f* Forecast

Source: National Sources and International Monetary Fund (IMF)

For further information about Bank Negara Malaysia and its publications:

**write to:**
Director,
Corporate Services Department
Bank Negara Malaysia
Jalan Dato' Onn
50480 Kuala Lumpur, Malaysia

Phone: +(603) 2698 8044 ext. 7494
Fax: +(603) 2691 2990

**or e-mail us at:**
info@bnm.gov.my

**or visit our World Wide Web site:**
http://www.bnm.gov.my

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