BANK NEGARA MALAYSIA
CENTRAL BANK OF MALAYSIA

Statutory Requirements

In accordance with section 13 of the Central Bank of Malaysia Act 2009, 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 2009, 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 2009 is incorporated in Bank Negara Malaysia's Financial Stability and Payment Systems Report 2009 which forms an integral part of this Annual Report 2009.

Zeti Akhtar Aziz
Chairman
Board of Directors

24 March 2010

Board of Directors

Tan Sri Dato' Sri Dr. Zeti Akhtar Aziz
D.K. (Johor), P.S.M., S.S.A.P., S.U.M.W., D.P.M.J.
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 Datuk Seri Dr. Wan Abdul Aziz bin Wan Abdullah
P.S.M., S.P.S.K., S.S.A.P., S.P.D.K., D.P.S.K., S.M.W., 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.U.M.W., S.P.M.T., D.S.M.T., P.N.B.S., A.M.K.

Tan Sri Dr. Sulaiman bin Mahbob
P.S.M., P.J.N., S.S.A.P., D.J.B.S., J.S.M., S.M.J., P.M.P., K.M.N., A.M.N.
(*Tan Sri Dr. Sulaiman Mahbob was appointed as member of the Board of Directors effective 25 November 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' Muhammad bin Ibrahim
Assistant Governor	Nor Shamsiah binti Mohd Yunus
Assistant Governor	Dato' Mohd Nor bin Mashor
Assistant Governor	Gopala Krishnan Sundaram
Assistant Governor	Dr. Sukhdave Singh
Assistant Governor	Bakarudin bin Ishak
Assistant Governor	Norzila binti Abdul Aziz
Director	
Governor's Office	Suhaimi bin Ali
Corporate Communications	Abu Hassan Alshari bin Yahaya
Strategic Management	Donald Joshua Jaganathan
Special Investigation	Sani bin Ab. Hamid
Financial Intelligence	Wan Mohd Nazri bin Wan Osman
Internal Audit	Tan Nyat Chuan
Economics	
Economics	Marzunisham bin Omar
Monetary Assessment and Strategy	Fraziali bin Ismail
International	Nazrul Hisyam bin Mohd Noh
Regulation	
Prudential Financial Policy	Jessica Chew Cheng Lian
Financial Sector Development	S. Abd. Rasheed bin S. Abd Ghafur
Financial Surveillance	Madelena binti Mohamed
Islamic Banking and Takaful	Ahmad Hizzad bin Baharuddin
Development Finance and Enterprise	Kamari Zaman bin Juhari
Consumer and Market Conduct	Koid Swee Lian
Supervision	
Financial Conglomerates Supervision	Che Zakiah binti Che Din
Insurance and Takaful Supervision	Yap Lai Kuen
Banking Supervision	Marina binti Abdul Kahar
Regulation and Supervision Administration Unit	Siti Ramlah binti Ahmad
Payment Systems Policy	Cheah Kim Ling
Investment and Operations	
Investment Operations and Financial Markets	Adnan Zaylani bin Mohamad Zahid
Currency Management and Operations	Ramli bin Saad
Foreign Exchange Administration	Wan Hanisah binti Wan Ibrahim
Corporate Resources	
Human Resource Management	Mohd. Adhari bin Belal Din
Finance	Rafiza binti Ghazali
Legal	Jeremy Lee Eng Huat
Human Capital Development Centre	Arlina binti Ariff
Risk Management	Chung Chee Leong
Corporate Services	Azmi bin Abd Hamid
IT Services	Alizah binti Ali
Statistical Services	Toh Hock Chai
Central Banking Services	V. Vijayaledchumy
Property and Services	Zulkifli bin Abd Rahman
Security	Mior Mohd Zain bin Mior Mohd Tahir
Bank Negara Malaysia Museum and Art Gallery	Muhammad Fawzy bin Ahmad
Sasana and Lanai Kijang Management Office	Lim Foo Thai
MIFC Promotion Unit	Shariffuddin bin Khalid
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

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Governor's Statement

BANK NEGARA MALAYSIA
CENTRAL BANK OF MALAYSIA

While the world economy experienced the worst effects of the global financial crisis in the first half of 2009, most economies experienced a recovery in the second half of the year. The swift and concerted policy actions implemented across the world were instrumental in avoiding a deep, fundamental depression of the global economy.

As a highly open economy, the Malaysian economy was significantly affected by the collapse in world trade which started in the second half of 2008. The deterioration in the external sector had by early 2009 spilled-over to deeply affect domestic demand. The significant and swift domestic policy responses, had together with Malaysia's strong economic fundamentals, brought about an economic recovery in the second half of the year. The robust financial sector also provided crucial support for the domestic economy. Overall, the Malaysian economy in 2009 contracted by 1.7%, performing significantly better than expected.

While downside risks to growth remain in the advanced economies, emerging economies in general, and Asia in particular, have shown a higher degree of resilience and have better prospects for a sustained recovery. Asia is expected to continue to lead the global recovery as the sources of growth become more broad-based. Domestic demand is expected to strengthen with better employment conditions and uninterrupted credit flows. Investment is expected to rebound with the planned investment in infrastructure and the recovery in external demand. Of importance is the growth in intra-regional trade through the sustained expansion in domestic demand within the region. This trend will not only mutually reinforce growth in the region but will also contribute towards the rebalancing of global growth.

The positive growth of 4.5% for the Malaysian economy in the fourth quarter of 2009 is expected to improve further in 2010. The Malaysian economy is projected to expand by 4.5-5.5% in 2010, underpinned by strengthening domestic demand and supported by the improving external environment. Growth is expected to be increasingly driven by private sector activity. Private consumption will benefit from further improvements in the labour market, rising disposable incomes and improved consumer confidence. Additionally, private investment is expected to recover in 2010, in line with the strengthening of global trade and increasing domestic demand. While inflation is expected to rise with the recovery in global economic activity, the upward trend in global commodity prices, and some revisions in administered prices by the Government, inflation is nevertheless expected to remain at modest levels during the year.

With clear signs of an economic recovery, steps have been taken to normalise interest rates. The extraordinary conditions under which the interest rates were reduced, now no longer prevail. Maintaining an extremely low interest rate environment for an extended period of time could result in disintermediation, financial imbalances and the underpricing of risks. Such developments would undermine the recovery in the economy. Despite the move to normalise interest rates, the overall stance of monetary policy will continue to remain accommodative to provide support to domestic economic activity.

Over the medium term, the more competitive global environment creates urgency for Malaysia to transition to a high value-added, high-income economy. Given that private sector-led economic activity is the main driver of growth in such an economy, Malaysia is putting in place wide ranging strategies in its ongoing transformation process to provide an enabling environment in which high productivity, competitiveness and innovation are key elements in the e-economy. The economy can no longer rely on the accumulation of factors of production to remain competitive. Three key areas of priority are to have a high quality workforce, to develop competition-driven markets and to strengthen further our existing institutional and physical infrastructure. Through the development of an enabling and competitive economic environment, Malaysia will be well positioned to benefit from the new opportunities and to deal with the potential challenges in this post crisis era.

In a highly uncertain environment, regional cooperation has continued to serve as a vital anchor in maintaining regional macroeconomic and financial stability, developing regional financial infrastructure and promoting regional integration. The year 2009 marked a key milestone with the multilateralisation of the Chiang Mai Initiative (CMI) liquidity support mechanism to allow for the effective pooling and drawdown of liquidity support among member countries. Concerted steps were also taken to further enhance the integrated crisis management and resolution mechanism put in place by the Monetary and Financial Stability Committee of the Executives' Meeting of East Asia-Pacific (EMEAP) Central Banks grouping. In addition, efforts to further develop the regional bond markets and to accelerate the pace of financial integration to support economic development in the region will continue to be a focal component of regional cooperation.

Regional collaboration with other central banks and supervisory agencies of emerging economies was also expanded and strengthened during the year. This collaboration covered a wide range of areas, including organisational development and capacity building to increase Central Bank effectiveness. It also included programmes that were organised to share knowledge and information with other regulators in the area of financial inclusion, microfinance and Islamic Finance. Several of the programmes have also been conducted in collaboration with international development agencies including the Islamic Development Bank, the Consultative Group to Assist the Poor and the International Finance Corporation. The Bank's international technical cooperation has focussed on the sharing of knowledge on central banking practices and building collaborative relationships with other central bankers from emerging economies.

Amid the changing global financial landscape and continued transformation of the Malaysian economy, the Central Bank of Malaysia Act 2009, which came into force on 25 November 2009, places the Bank on a new legal foundation. The Act is the culmination of a 2-year review by the Bank of central banking legislation, taking into account the complexities of the economic and financial environment in Malaysia as well as global trends. It mandates the Bank to promote monetary stability and financial stability conducive to the sustainable growth of the Malaysian economy, and institutionalises the policy autonomy enjoyed by the Bank during the 50 years of its existence. With greater clarity and focus in the mandates of the Bank and the powers necessary to achieve these mandates, the accountability framework and governance structure have been considerably enhanced. This has been achieved by institutionalising the best practices that had been adopted for some years now by the Bank.

As part of the organisational transformation to become more strategy-focused and performance-driven, the Bank commenced the implementation of the 3-year Business Plan that has been developed in 2009. This is supported by the increased organisation-wide clarity of the strategic results and enhanced cross-functional collaboration required to deliver these results. Rigorous strategy reviews continue to be conducted to evaluate the overall performance and raise the effectiveness of the Bank in performing its mandates. In addition, in ensuring that the Bank has access to the best technical and analytical skills, significant investment has been allocated towards building a high performance workforce that includes enhanced formal training and changes to work practices. Leadership development was also accorded emphasis to ensure a continuous strengthening of the leadership pipeline. In addition, more emphasis was given to project based and collaborative work processes, which have also broadened and improved the skills and competencies of staff in core areas of the Bank's work. A structured and robust talent assessment process has also been put in place and is accompanied by a more dynamic and differentiated reward system to ensure that the incentives are appropriately aligned.

Finally, I wish to express my appreciation to my colleagues and all staff of Bank Negara Malaysia for their dedication and perseverance in performing their responsibilities to fulfil our mandates in the most challenging of conditions in 2009. I would also like to thank the Board of Directors for their unwavering support to the Bank. Under the new Central Bank Act, the Board and the various Board committees have a significantly enhanced role in the governance of the Central Bank. We wish to record our deep appreciation to a valued board member, Tan Sri Dato' Seri Mohd Hassan Marican, for his contribution to the Board. He is retiring following the completion of his term. At the same time, I wish to welcome Tan Sri Dr. Sulaiman Mahbob to the Board and Encik Chin Kwai Yoong who will be joining the Board in 2010. The Bank, going forward, will continue to persevere in discharging our responsibilities and to rise to the challenges, upholding the trust that has been placed in us.

Zeti Akhtar Aziz
Governor

24 March 2010

Economic Developments in 2009

Economic Developments in 2009

THE INTERNATIONAL ECONOMIC ENVIRONMENT IN 2009

In the first half of 2009, the global economy experienced the sharpest contraction since the Second World War, with countries accounting for more than 60% of world output mired in a synchronised recession. The full impact of the 2008 international financial crisis on the real economy was felt in the first quarter of 2009, where a large number of economies experienced significant contractions in real GDP. In the advanced economies, the financial crisis and the ensuing credit crunch led to a sharp decline in private sector demand. Household consumption was curtailed, affected by a combination of factors including deteriorating employment prospects, falling house prices and difficulties in obtaining access to credit. Similarly, businesses cut their production sharply while inventories were drawn down to abnormally low levels amid weak demand and tight credit conditions. The international production and trade network unravelled, sending shocks to the emerging economies. The Asian economies, particularly those with a higher degree of trade openness, were affected by the collapse in world trade that resulted from the sudden plunge in demand from the advanced economies, leading to double-digit declines in exports and production. The deterioration in the trade-related sectors subsequently impacted the rest of the economy as household and business confidence were adversely affected.

The global economy experienced the sharpest contraction of the post-war period in the first half of 2009 before entering into a gradual but uneven recovery in the second half of the year

The severe global financial crisis and the sharp global recession that ensued led to unprecedented policy responses by governments and monetary authorities across the world. Governments introduced large fiscal stimuli, ranging between 1 – 12% of GDP, while central banks aggressively eased monetary policy as interest rates were reduced to record lows. In the major advanced economies, quantitative easing and financial support measures were also introduced, primarily to provide liquidity to financial markets and to restore stability in their financial systems.

The extraordinary policy responses contributed to the stabilisation of the financial markets and provided some support to the real economy. Of importance, the large fiscal spending and the restoration of normal functioning of financial markets arrested the sharp deterioration in economic activity. As a result, economic activity in most economies began to stabilise by the middle of the year and countries started to gradually emerge from the recession in the second half of 2009.

Economic recovery, however, remained fragile and uneven. The fragility of the recovery was evident as the growth experienced by most countries in the second half of 2009 continued to rely heavily on the fiscal support. In the advanced economies, high unemployment, ongoing deleveraging by the private sector and weak financial systems, continued to weigh on private sector activity. Economic recovery was, however, more pronounced in the emerging economies, particularly in Asia, where domestic demand was supported by sizeable fiscal stimuli and reinforced by the uninterrupted access to financing to the private sector. The recovery of intra-regional trade also provided support to growth.

The crisis in the international financial markets reached its peak in the first quarter of 2009 following the fallout from the failure of the US investment bank, Lehman Brothers, in the fourth quarter of 2008. Further losses revealed by major global financial institutions and uncertainty over the solvency of these large institutions amid heightened concern over systemic failure in a number of financial markets caused a flight to safer assets, including cash. As a result, the securitised debt markets froze, market liquidity dried up and global equity markets declined sharply to multi-year lows by March 2009. The extraordinary policy measures, including near zero interest rates, quantitative easing, and measures to ease liquidity and credit conditions that were taken in the major advanced economies, were important in alleviating the stress in the international financial markets, hence enabling the cost of financing to decline gradually.

By the second quarter, credit spreads began to narrow and equity prices gradually recovered, as risk appetite improved. Interbank markets started to function again, followed by stabilisation in short-term money markets in response to central banks' aggressive liquidity injection into the financial system. However, the improvement in the interbank markets did not translate into higher lending to the private sector in the advanced economies, largely reflecting the continued weakness of the financial institutions.

Table 1.1
World Economy: Key Economic Indicators

	Real GDP Growth (%)		Inflation (%)	
	2008	2009*e*	2008	2009*e*
World Growth	**3.0**	**-0.8**	-	-
World Trade	**2.8**	**-12.3**	-	-
Major Advanced Economies				
United States	0.4	-2.4	3.8	-0.4
Japan	-1.2	-5.2	1.4	-1.4
Euro area	0.6	-4.1	3.3	0.3
United Kingdom	0.5	-5.0	3.6	2.2
East Asia	**6.9**	**5.1**	**5.9**	**0.3**
Asian NIEs[1]	**1.7**	**-0.9**	**4.5**	**1.2**
Korea	2.2	0.2	4.7	2.8
Chinese Taipei	0.7	-1.9	3.5	-0.9
Singapore	1.4	-2.0	6.6	0.6
Hong Kong SAR[2]	2.1	-2.7	4.3	0.5
The People's Republic of China	9.6	8.7	5.9	-0.7
ASEAN	**4.6**	**1.1**	**7.7**	**2.4**
Malaysia	4.6	-1.7	5.4	0.6
Thailand	2.5	-2.3	5.5	-0.9
Indonesia	6.0	4.5	9.9	4.8
Philippines	3.8	0.9	9.3	3.3
India[3]	7.4	6.5	9.1	2.1

[1] Newly industrialised economies
[2] Inflation refers to composite price index
[3] Inflation refers to wholesale price index
e Estimate

Source: International Monetary Fund, National Authorities and Bank Negara Malaysia estimates

In the **United States (US)**, real GDP contracted sharply by an annualised rate of 6.4% in the first quarter of 2009, its biggest contraction in 29 years. The decline in GDP was largely due to the contraction in fixed investment and large inventory drawdown as businesses responded to the significant drop in overall demand since late 2008 by cutting production aggressively. In response, the US government unveiled a USD787 billion fiscal stimulus in February 2009, consisting mainly of tax rebates to households and businesses and infrastructure spending. On the monetary front, with the federal funds rate reduced to near zero since December 2008, the Federal Reserve (Fed), US Treasury and the FDIC implemented quantitative measures in the form of recapitalisation of banks, guarantees for banks' debt, purchases of illiquid and impaired assets held by the financial institutions, particularly mortgage-backed securities and other securities backed by consumer loans, to thaw the frozen credit markets and restore market functioning.

The Fed introduced programmes to purchase USD1.25 trillion of agency mortgage-backed securities, USD175 billion of agency debt and USD300 billion of US treasury securities with the objective of lowering the interest burden for financially-constrained home mortgage borrowers. The extraordinary measures caused the Fed's balance sheet to expand by 150% to reach USD2.2 trillion, underlining the heavy reliance of the financial system on the central bank's support. The Fed's move to assist the housing market was further supported by the fiscal stimulus in the form of tax credits for home buyers, boosting demand for housing. The policy responses stabilised the housing and financial markets, as well as the overall economic conditions by the second quarter of the year. The containment of systemic risk, restoration of functioning of financial markets and large fiscal stimulus contributed to gradual recovery in the equity market from its lows in March, together with the stabilising of house prices since June helped to bring about positive wealth gain of about USD5.7 trillion for the US households from the second until the fourth quarter. The increase in wealth restored part of the wealth loss of USD17.5 trillion experienced during the period mid-2007 to the first quarter of 2009.

By the third quarter, consumption grew as households also benefited from tax incentives for the purchase of automobiles. After declining at a slower annualised rate of 0.7% in the second quarter, GDP expanded at an annualised rate of 2.4% in the second half of 2009. The recovery in the US in the second half of the year was driven by the growth in private consumption, residential fixed investment and government spending. Nevertheless, the pace of recovery remained slow and highly dependent on policy support. In spite of the weak recovery in the second half, overall private consumption continued to be constrained by rising job losses. The US economy had lost a total of 8.4 million jobs between end-2007 and end-2009 and the unemployment rate reached 10% in December 2009. Furthermore, many households continued to reduce their debt as falling house prices had eroded a large part of their wealth. For the year as a whole, the US economy declined by 2.4%.

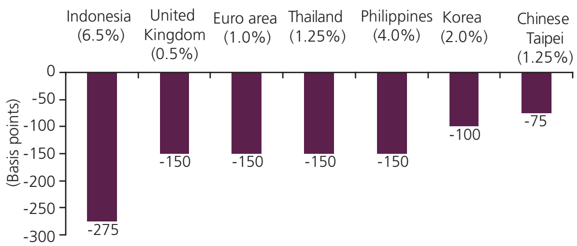
The other advanced economies mirrored the US's growth path closely throughout the year. In the **euro area**, growth contracted sharply by 2.5% quarter-on-quarter in the first quarter, its largest decline since the data was first recorded, due mainly to the large contraction in exports and fixed investment. The deteriorating external environment also spilled into weaker domestic demand following the higher unemployment, tight credit conditions and falling house prices. After reducing the interest rates by 150 basis points to 2.5% in 2008, the European Central Bank (ECB) continued to lower its refinancing rate by a further 150 basis points to 1% by May 2009. The central bank also embarked on a €60 billion covered bond purchase to inject liquidity in the financial system and stimulate lending activity in the euro area.

While the fiscal stimulus in the euro area was relatively smaller than the US, a larger part of euro area's fiscal support came through 'automatic stabilisers', particularly in terms of unemployment and health care benefits. Coupled with tax incentives for employers to retain labour, unemployment in the euro area did not rise as much as the US. Fiscal measures were also directed at boosting consumption through tax rebates, especially on automobiles as well as infrastructure spending. This had enabled a gradual revival in consumer and business confidence, allowing the euro area to turn around to register a small positive GDP growth on a quarter-on-quarter basis in the third and fourth quarters, led by Germany and France. For the year as a whole, the euro area contracted by 4.1%. Nevertheless, the recovery in the euro area was uneven as countries including Spain and Greece remained in recession given the severity of the housing crisis and high unemployment. The euro area was also affected by structural unemployment and the worsening fiscal positions in several euro economies, giving rise to concerns on the sustainability of fiscal stimulus in supporting growth.

Meanwhile, in the **United Kingdom (UK)**, the economy recorded six consecutive quarter-on-quarter declines, its longest decline on record, up to the third quarter of 2009. This was due mainly to the persistent weakness in domestic demand following rising unemployment, tight credit and negative home equity from significantly lower house prices. Meanwhile, fixed investment declined sharply in view of falling demand, difficulty in getting financing and lower capacity utilisation. The bleak outlook of the economy prompted the Bank of England (BOE) to reduce the base lending rate further by 150 basis points in early 2009 to 0.5% by March 2009, its historical low. At the same time, the BOE introduced a £200 billion plan to purchase corporate bonds and government gilts to inject liquidity into the economy and ease the credit crunch. A fiscal stimulus was also implemented to bolster consumption through tax rebates and automobile incentives. These measures began to yield some results, with the UK economy recording a small positive growth in the fourth quarter of 2009. However, for the year as a whole, the UK economy contracted by 5%. The UK economy is confronted with a continued weak labour market and a deteriorating fiscal position.

In **Japan**, real GDP contracted at an annualised rate of 13.7% in the first quarter, its largest post-war decline, due mainly to the double-digit declines in exports and fixed investment. The contraction in trade spilled into domestic demand, resulting in weak private consumption amid persistent deflation. While the Bank of Japan (BOJ) kept its overnight rate at 0.1%, the central bank first implemented quantitative easing through the monthly purchase of government bonds and later, a ¥10 trillion credit program for commercial lenders to inject liquidity into the financial system and to ease the deflationary pressure. Fiscal stimulus was also introduced to support private consumption through tax rebates. Benefiting from the close trade linkages with Asia, particularly

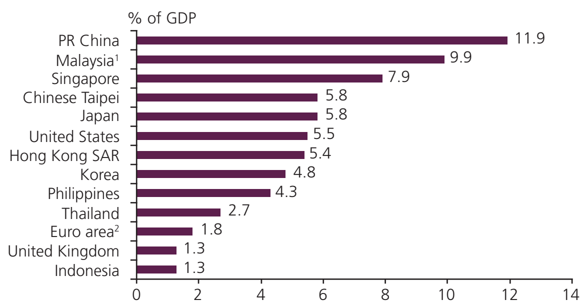
Chart 1.1
Cumulative Movements of Policy Rates since 2009



Note: Current policy rates in parentheses, as at mid-March 2010

Source: National Authorities

Chart 1.2
Fiscal Stimulus in Selected Economies



[1] Of which, direct fiscal injection is USD5.9 billion or 3.3% of GDP
[2] Amount spent under the European Economic Recovery Plan
Note: As at mid-March 2010

Source: International Monetary Fund, National Authorities, World Bank and Bank Negara Malaysia estimates

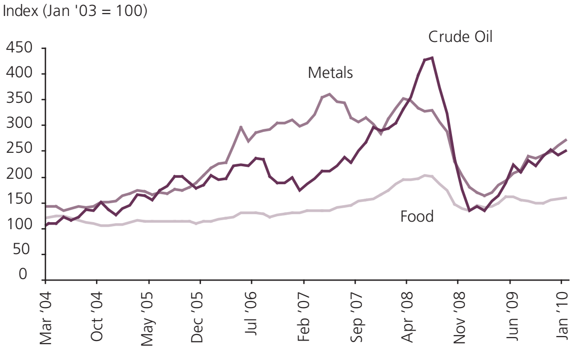
PR China, Japan's real GDP expanded quarter-on-quarter in the second quarter as exports to Asia increased. In 2009, PR China overtook the US to become Japan's largest trading partner. Meanwhile, domestic demand remained weak, lagging the recovery in external demand. For the year as a whole, Japan recorded a contraction of 5.2%.

In the **Asian region**, growth performance was adversely affected by the deterioration in the export sector, especially in the first quarter. The more open economies, particularly the newly industrialised Asian economies, experienced deeper recessions while other regional economies with larger domestic markets such as PR China, Indonesia and the Philippines experienced a moderation in growth. Growth was further affected by large inventory drawdowns as firms sharply reduced production and postponed investment plans, resulting in abnormally low level of inventories. As a result, labour market conditions also weakened, with unemployment rising in most countries, thus affecting consumer confidence and spending.

In response to the large contractionary external demand, regional central banks reduced their interest rates during the year by between 75 and 275 basis points and adopted liquidity and guarantee measures to support the overall growth prospects. Aggressive fiscal spending plans, ranging from 1% to 12% of GDP, were unveiled to bolster domestic demand through a combination of tax rebates, direct cash handouts and infrastructure spending. In some countries, tax incentives were also given to firms to retain their workers. These policy measures had an important role in restoring consumer and business confidence, and stabilising labour market conditions. In addition to the policy support, strong banking institutions and thus the continued financial intermediation, and the relatively healthy financial position of the private sector facilitated a faster recovery in the domestic demand in the region, while stronger intra-regional trade provided an additional impetus to growth. As a result, most regional economies started to experience positive quarter-on-quarter growth in the second quarter, ahead of the advanced economies. The recovery in the Asian economies gathered further momentum in the second half of the year as global economic conditions gradually improved. PR China, in particular, which introduced the largest fiscal stimulus package of 11.9% of GDP, recorded 10.7% growth in the fourth quarter of 2009, its strongest growth since the first quarter of 2008.

On the **global inflation** front, many advanced and regional economies had experienced technical deflation since the early part of the year due to lower commodity prices and the weak demand conditions. While the headline inflation was influenced by the high base in 2008, core inflation remained positive for most economies, suggesting that the threat of actual deflation had been minimal. Following the gradual recovery in the regional economies from the second quarter and by the advanced economies in the third quarter, commodity prices began to rise steadily with oil prices reaching close to USD80 per barrel by year-end. Consumer prices in most economies started to edge higher, reflecting the trend in commodity prices although demand pressure remained subdued. While consumer price inflation

Chart 1.3
Indices of Primary Commodity Prices



Source : International Monetary Fund

was benign throughout the year, rising equity and property prices in several economies raised concerns on asset price inflation. In response, several regional economies undertook measures to curb the formation of asset bubbles, either through imposing administrative measures in the property market or on short-term capital flows.

In the **foreign exchange markets**, the US dollar started the year on a strong note, appreciating against most major currencies in the first two months. The dollar strength was attributed to the portfolio flows into dollar-denominated assets, reflecting investor risk aversion amid deteriorating global growth prospects and ongoing weakness in global financial markets. The dollar also benefited from the waning confidence in the euro following concerns over European banks' exposure to the Eastern European economies. However, as the global equity markets began to recover from their multi-year lows in March, the US dollar started to weaken following the improvement in investor risk appetite that caused a shift out of low-yielding dollar-denominated assets to higher yielding assets denominated in other currencies. As a result, the other major currencies outperformed the dollar throughout most of the year. The performance of the euro and the pound sterling were strongest at about mid-2009, following expectations of a faster pace of recovery in these economies as compared to the US. However, lagging performance of the UK economy in the latter half of the year led to a slight weakening of the pound sterling. Towards the end of the year, both the euro and the pound sterling depreciated considerably due to concerns over the deteriorating fiscal positions in the two economies. Meanwhile, the yen appreciated to its strongest level in 14 years due to the higher repatriation of income from investments abroad. This trend reversed by December when the yen weakened following the decision of the Bank of Japan to expand quantitative easing. In the Asian region, most regional currencies appreciated against the US dollar following improved sentiments driven by the faster pace of recovery in the region vis-à-vis the advanced economies. Among regional currencies, the rupiah recorded the strongest appreciation due to the resilient economic conditions and more favourable political climate.

THE MALAYSIAN ECONOMY IN 2009

The Malaysian economy contracted by 1.7% in 2009, a year when the global economy experienced its deepest downturn in modern history. The domestic economy experienced the full impact of the global recession in the first quarter, declining by 6.2%, marking the first year-on-year contraction in real GDP since the third quarter of 2001. The collapse in global demand and world trade led to double-digit declines in Malaysia's exports and industrial production. Given the high degree of openness of the economy, the deterioration in external demand affected employment, income and overall business and consumer sentiment, causing private consumption and private investment activities to decline in the first quarter of the year. Growth during the quarter was also affected by large drawdowns of inventory, particularly in the manufacturing and commodity sectors.

Despite a sharp contraction in the first quarter, the Malaysian economy contracted moderately by 1.7% in 2009 as recovery strengthened in the second half of the year

However, the accelerated implementation of fiscal stimulus measures, the aggressive easing of monetary policy and the comprehensive measures introduced to ensure continued access to financing contributed to stabilisation in the domestic economy in the second quarter and subsequent recovery in the second half of the year. In addition to higher public spending, the

Table 1.2: Malaysia - Key Economic Indicators

	2007	2008	2009*p*	2010*f*
Population (million persons)	27.2	27.7	28.3	28.9
Labour force (million persons)	11.8	12.0	12.1	12.2
Employment (million persons)	11.4	11.6	11.6	11.8
Unemployment (as % of labour force)	3.2	3.3	3.7	3.6
Per Capita Income (RM)	23,033	25,784	23,381	25,180
(USD)	6,700	7,737	6,634	7,416[6]
NATIONAL PRODUCT (% change)				
Real GDP at 2000 prices[1]	6.2	4.6	-1.7	4.5 ~ 5.5
(RM billion)	504.9	528.3	519.2	543.4
Agriculture, forestry and fishery	1.4	4.0	0.4	3.1
Mining and quarrying	2.0	-0.8	-3.8	2.5
Manufacturing	3.1	1.3	-9.3	6.5
Construction	4.7	2.1	5.7	3.7
Services	9.6	7.2	2.6	4.9
Nominal GNI	12.3	14.2	-7.4	10.0
(RM billion)	625.9	715.0	661.8	727.7
Real GNI	5.9	2.0	1.2	3.6
(RM billion)	481.8	491.5	497.4	515.3
Real aggregate demand[2]	9.6	6.8	-0.4	3.2
Private expenditure[2]	10.7	7.0	-3.4	3.3
Consumption	10.4	8.5	0.8	3.8
Investment	11.8	0.8	-21.8	0.7
Public expenditure[2]	6.8	6.3	7.7	2.7
Consumption	6.5	10.9	3.7	-2.7
Investment	7.1	0.7	12.9	9.3
Gross national savings (as % of GNI)	38.2	37.9	31.3	35.2
BALANCE OF PAYMENTS (RM billion)				
Goods balance	127.7	170.6	141.5	141.6
Exports (f.o.b.)	605.9	664.3	554.2	615.2
Imports (f.o.b.)	478.2	493.8	412.7	473.7
Services balance	2.4	0.2	3.2	-0.7
(as % of GNI)	0.4	...	0.5	-0.1
Income, net	-13.9	-23.7	-12.6	-19.9
(as % of GNI)	-2.2	-3.3	-1.9	-2.7
Current transfers, net	-15.7	-17.5	-19.4	-17.1
Current account balance	100.4	129.5	112.7	103.8
(as % of GNI)	16.0	18.1	17.0	14.3
Bank Negara Malaysia international reserves, net[3]	335.7	317.4	331.3	
(in months of retained imports)	8.4	7.6	9.7	
PRICES (% change)				
CPI (2005=100)[4]	2.0	5.4	0.6	2.0 ~ 2.5
PPI (2005=100)[5]	5.5	10.3	-7.1	
Real wage per employee in the manufacturing sector	2.7	-4.8	1.9	n.a

[1] Beginning 2007, real GDP has been rebased to 2000 prices, from 1987 prices previously
[2] Exclude stocks
[3] 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
[4] Effective from 2006, the Consumer Price Index has been revised to the new base year 2005=100, from 2000=100 previously
[5] Effective from 2010, the Producer Price Index has been revised to the new base year 2005=100, from 2000=100 previously
[6] Based on average USD exchange rate for the period of January-February 2010
p Preliminary
f Forecast

Note: Numbers may not necessarily add up due to rounding

Table 1.3 Malaysia - Financial and Monetary Indicators

FEDERAL GOVERNMENT FINANCE (RM billion)	2007	2008	2009*p*
Revenue	139.9	159.8	158.6
Operating expenditure	123.1	153.5	157.1
Net development expenditure	37.5	41.9	49.0
Overall balance	-20.7	-35.6	-47.4
Overall balance (% of GDP)	-3.2	-4.8	-7.0
Public sector net development expenditure	96.3	124.4	118.0
Public sector overall balance (% of GDP)	1.5	-5.6	-3.8
EXTERNAL DEBT[1]			
Total debt (RM billion)	187.4	236.1	233.9
Medium- and long-term debt	133.0	156.5	156.0
Short-term debt[2]	54.5	79.6	78.0
Debt service ratio (% of exports of goods and services)			
Total debt	3.8	2.6	6.5
Medium- and long-term debt	3.4	2.5	6.4

MONEY AND BANKING		Change in 2007		Change in 2008		Change in 2009	
		RM billion	%	RM billion	%	RM billion	%
Money Supply	M1	27.6	19.6	14.0	8.3	17.9	9.8
	M3	72.4	9.5	99.1	11.9	85.1	9.1
Banking system deposits		56.5	7.0	103.4	11.9	90.7	9.3
Banking system loans[3]		51.2	8.6	82.3	12.8	56.9	7.8
Loan-deposit ratio (end of year)[4]		76.2		77.7		77.9	
Financing-deposit ratio[4, 5]		85.1		85.8		84.6	

INTEREST RATES (AVERAGE RATES AS AT END-YEAR)		2007	2008	2009
		%	%	%
Overnight Policy Rate (OPR)		3.50	3.25	2.00
Interbank rates				
1-month		3.54	3.30	2.06
Commercial banks				
Fixed Deposit	3-month	3.15	3.04	2.03
	12-month	3.70	3.50	2.50
Savings deposit		1.44	1.40	0.87
Base lending rate (BLR)		6.72	6.48	5.51
Treasury bill (3-month)		3.43	3.39	2.05
Malaysian Government securities (1-year)*		3.53	2.89	2.12
Malaysian Government securities (5-year)*		3.78	2.99	3.79

EXCHANGE RATES	2007	2008	2009
Movement of Ringgit (end-period)	%	%	%
Change against SDR	1.7	-2.7	0.2
Change against USD[6]	6.8	-4.5	1.2

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 Exclude financial institution transaction
5 Refers to the ratio of loans and holdings of PDS by the banking system to deposits of the banking system
6 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
* Refer to end-year

policy measures also helped to revive private sector sentiment, which, together with improving labour market conditions, led to an expansion in private consumption in the second half of the year. Signs also emerged to indicate that private investment activity had begun to stabilise towards the end of the year. Moreover, external demand provided further impetus to growth as the global economy, particularly the regional economies, gradually recovered. As a result, the Malaysian economy resumed its growth momentum in the fourth quarter, growing by 4.5%, with strengthened domestic and external demand contributing to growth.

On the supply side, growth in the first quarter was particularly affected by a sharp decline in the manufacturing sector, while other sectors, except construction, also contracted. The manufacturing sector, particularly the export-oriented industries, was severely affected by the significant deterioration in external demand. Nevertheless, the manufacturing sector gradually improved and recorded positive growth in the fourth quarter, in tandem with the recovery in external demand. Meanwhile, the services sector recorded a marginal decline in the first quarter due mainly to contractions in the sub-sectors which are related to manufacturing and trade activities. In line with the improvement in domestic demand, the performance of the services sector had gradually improved since the second quarter, with growth coming from the services sub-sectors that are dependent on domestic economic activity as well as finance and capital market-related activities. Nonetheless, growth of the construction sector had remained positive throughout the period due primarily to the implementation of construction-related projects under the Ninth Malaysia Plan (9MP) and the fiscal stimulus measures.

Labour market conditions weakened considerably in the first quarter as firms in the manufacturing sector reduced their operations, particularly in the first two months of the year. Total retrenchments increased to a seven-year high of 25,064 persons in 2009, with one-half the workers being retrenched in the first quarter. Labour market conditions began to stabilise in the second quarter and improved thereafter as retrenchments declined and firms started to hire new workers. The quicker-than-expected recovery in the labour market following improvements in both global and domestic economic conditions, resulted in a lower unemployment rate of 3.7% of the labour force, compared to the earlier forecast of 4.5%. Despite the challenging economic environment and declining productivity growth in 2009, employers in the private sector had continued to grant salary increments, albeit at a moderate rate of 3.4% (2008: 5.1%).

Headline inflation averaged 0.6% in 2009 (2008: 5.4%) as inflationary pressures in Malaysia moderated substantially, in line with global and domestic developments. Weak global demand conditions, particularly in the first quarter of 2009 led to a significant drop in global commodity prices, especially crude oil prices. As a result, several countries experienced lower inflationary pressures during the year. Inflation in the advanced economies recorded a steep decline, while inflation in emerging market economies also saw a decline in 2009, with the most notable deceleration recorded by China (2009: -0.7%; 2008: +5.9%). The decline in global fuel and commodity prices and the lower inflation in Malaysia's major trading partners in turn contributed to lower domestic inflation. The cumulative reductions in domestic retail petrol prices in the second half of 2008 contributed significantly to the moderating trend of domestic inflation in 2009.

Malaysia's external position remained strong in 2009 despite the extremely weak external environment. The current account continued to record a large surplus during the year, supported by a sizeable trade surplus and improvements in the services account. Although gross exports deteriorated significantly in 2009, particularly in the first half of the year, the trade surplus remained large as lower demand for exports was also accompanied by a decline in imports. The services account registered a significant surplus in 2009 following higher travel receipts from sustained regional travel activity, as well as an improvement in the other services deficit. Meanwhile, the financial account recorded lower net outflows in 2009, reflecting largely the significant moderation in portfolio outflows in the first half of the year and net inflows in the second half of the year. Both net inflows of foreign direct investment and outflows of direct investment abroad also moderated amid the weak economic conditions, whereas other investment outflows, which largely consist of trade credits, increased during the year. As large current account surplus more than offset the net outflows in the financial account, the overall balance of payments recorded a surplus in 2009, contributing to a further increase of RM13.9 billion in net international reserves to RM331.3 billion (or USD$96.7 billion) as at 31 December 2009.

The Malaysian economy, which was significantly affected by the developments in the global economy in the first quarter of 2009, recovered rapidly to register positive growth in the fourth quarter. In addition to the improvement in external demand, the domestic economy was supported by the accelerated implementation of fiscal stimulus measures, the accommodative monetary environment and continued access to financing. The rapid and comprehensive policy responses, which also helped to restore consumer and business sentiments, had an important role in sustaining domestic demand, which was the main factor supporting economic activities throughout the period. In addition, the domestic financial system remained strong despite the challenging international financial environment, effectively performing its financial intermediation function and facilitating the recovery in domestic demand. Overall, the continued strength in both economic and financial fundamentals, as reflected by the resilience in domestic demand, high international reserves position, low external debt, sustained high rate of savings and strong banking sector, has placed the Malaysian economy in a better position to grow further going forward.

DOMESTIC DEMAND CONDITIONS IN 2009

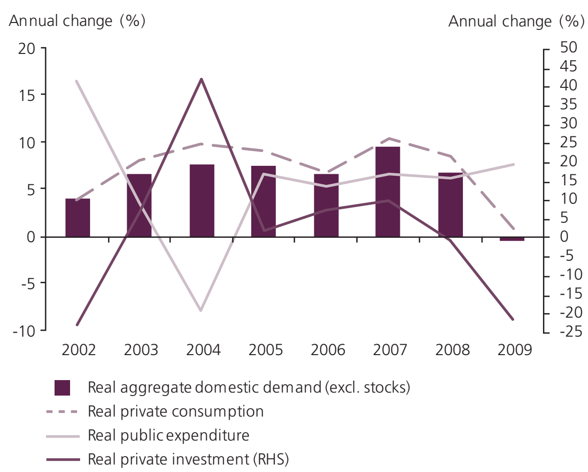
Domestic demand contracted by 2.9% in the first quarter, the first contraction since the third quarter of 2001, as households and businesses turned more cautious amid a significant deterioration in external demand, weaker labour market conditions and an overall decline in private sector sentiment. Despite the persistence of weak external demand, domestic demand conditions began to stabilise in the second quarter due to higher public sector spending following the implementation of fiscal stimulus measures to support the economy and expansion in private consumption.

The public sector had an important role in mitigating the impact of the global recession on the domestic economy through active implementation of two stimulus packages throughout the year. The strong public sector spending, together with an accommodative monetary policy, the continued access to financing, improvements in labour market conditions and a gradual recovery in external demand contributed to an expansion in domestic demand activity in the second half of the year. An increase in private consumption was supported by the rebound in consumer sentiment, stable employment prospects, low inflation and favourable financing conditions. Although private investment activity remained weak throughout 2009, there were signs of stabilisation towards the end of the year as global economic conditions and external demand started to improve. As a result, domestic demand turned around to record a positive growth of 1.7% in the second half of 2009, bringing the overall growth in aggregate domestic demand for the year to a marginal decline of 0.4% (2008: +6.8%).

Domestic demand, which contracted in the first quarter, recovered in the second half of 2009 as conditions in the labour market and external sector improved

Private consumption recorded a marginal growth of 0.8% in 2009, marking its slowest expansion since the Asian Financial Crisis. In the early part of the year, household spending was

Chart 1.4
Real Domestic Demand Aggregates



How Did the Recent Global Recession Affect the Malaysian Economy?

Introduction

The problems in the US financial system arising from the deteriorating quality of sub-prime assets that started in mid-2007, escalated into a major and severe global financial crisis in the second half of 2008. In particular, the failure of a number of large US and global financial institutions in September 2008 generated widespread fear of a systemic disruption across global financial markets which in turn had led to the "freezing" of the interbank and credit markets in many financial centres around the world. Despite the unprecedented large and aggressive financial measures taken by the authorities, the crisis intensified as prices of a large number of classes of financial assets collapsed resulting in a huge negative income and wealth effect. This, together with a widespread loss of confidence, led to a synchronised recession among the advanced economies in the second half of 2008, which deepened further in the first quarter of 2009 (Chart 1). Following the implementation of large fiscal and monetary policy stimulus, the global economy showed signs of stabilisation in the second quarter, and subsequently, gradually recovered towards the end of 2009. Nevertheless, the recovery of the global economy has been uneven, with growth still weak in the advanced economies and stronger in the emerging economies.

Chart 1
Advanced Economies in a Synchronised Recession by End-2008

Real GDP growth
(Seasonally adjusted; Annual change (%))

Source: Haver Analytics

The sharp recession in the advanced economies had a significant spillover effect on Asian regional economies through the finance and trade interlinkages. The global deleveraging process had also, towards the end of 2008, triggered large outflows from the region, of short-term portfolio funds and a sharp decline in bank financing, causing the substantial declines in equity and debt markets, slowing foreign direct investments and weakening of regional currencies against the US dollar. However, the underlying fundamental strength of the regional economies and a sound financial sector in the region enabled the regional economies to cope with these adverse developments relatively well without disruptions in the intermediation process by the domestic financial systems. The collapse in global trade led to severe declines in the region's exports and industrial production, causing the more open economies in the region to experience an economic contraction, while other economies experienced sharp deceleration in growth in the fourth quarter of 2008.

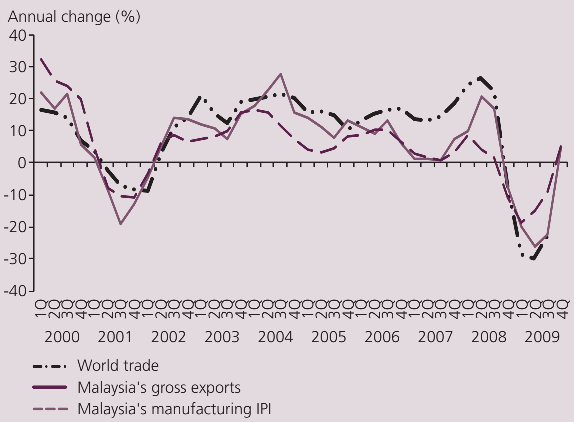
The Effects of the Global Recession on Malaysia

The global financial crisis and the deleveraging activities in the advanced economies led to disposal of assets world wide, including in the region, which caused sharp declines in the regional equity and bond markets. There was a large reversal in short-term capital flows, especially in the second half of 2008 as these funds were remitted back to the US. This sharp reversal of funds flows was, however, well absorbed by the domestic financial markets, given the ample liquidity in the financial system and the sound banking system. The strong reserves position of the country also acted as a buffer for US dollar liquidity and exchange rate movements during this turbulent period. In addition, the broad-based financial sector reforms and capacity building measures that have been undertaken following the Asian financial crisis had increased the financial sector's resilience to withstand the financial turmoil. The exposure of the domestic banking system to the sub-prime assets was also limited.

The Malaysian banking system was on a strong foundations when the global financial crisis erupted. The level of capitalisation of the Malaysian banking system remained high, with a risk-weighted capital ratio of 14.7% at end-December 2009 (end-2008: 12.6%), while the net non-performing loan ratio was low at 1.8% (end-2008: 2.2%). The strong capitalisation and ample liquidity in the banking system had ensured that the intermediation function remained uninterrupted, as reflected in the continued expansion of loans outstanding to businesses and households throughout 2009. Total business loans outstanding expanded by 2.6% in 2009 (end-2008: 13.2%) while household loans outstanding expanded at a sustained high rate of 9.8% as at end-2009 (end-2008: 9.7%).

As Malaysia is a highly open economy, the impact of the global recession was felt strongly in the external trade-related sectors. The recession in the advanced economies started to impact the Malaysian economy in the fourth quarter of 2008. Exports and manufacturing production declined by 7.4% and 11.1% respectively (Chart 2), and private investment activity was dampened by the deteriorating business conditions. However, the resilience of domestic demand, particularly private consumption, provided support to the economy, preventing it from contracting in the fourth quarter of 2008 (real GDP growth: 0.1%).

Chart 2
Collapse in World Trade Led to Sharp Contractions in Malaysia's Gross Exports and Manufacturing Production



Source: Haver Analytics; Department of Statistics, Malaysia

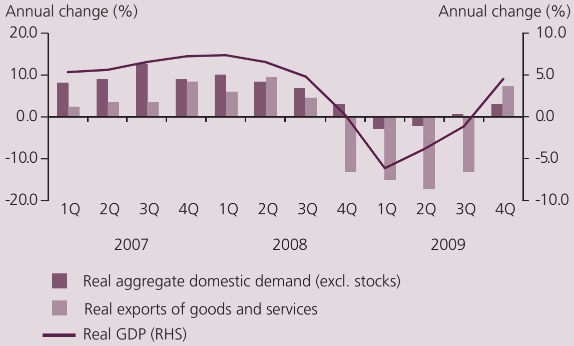
Chart 3
Export-oriented Manufacturing Sector was the Worst Affected

Source: Department of Statistics, Malaysia

Malaysia experienced the full impact of the global crisis in the first quarter of 2009, as the deepening recession in the advanced economies intensified the impact of a rapid decline in global demand on trade, production and investment activities in the domestic economy. As the advanced and some emerging economies slide into a recession in the first quarter of 2009, world trade declined sharply by 28.6% (4Q 08: -7.4%), and in turn, affected exports from the region, including from Malaysia. Malaysia's gross exports declined by 20% during the quarter (4Q 08: -7.4%), resulting in subsequent reductions in production, particularly in the manufacturing sector (Chart 3). In response to the significantly lower exports and production activity, firms undertook measures to reduce the cost of labour by enforcing a freeze on new hiring, initiating pay-cuts, reducing overtime work and laying off some workers. Retrenchments increased to 12,590 persons in the first quarter, compared with a quarterly average of 3,873 persons during the 2005-2008 period, affecting mainly workers from the manufacturing sector. The unemployment rate increased to 4% in the first quarter (4Q 08: 3.1%).

Although the income of households in the other sectors that were not directly exposed to external demand remained relatively unaffected, their spending behaviour was affected by the weak sentiment following the overall weaker economic conditions and uncertainties over their income outlook and job security. This resulted in a marginal decline in private consumption spending by 0.7%. Total investment also weakened significantly (-10.8%), following the sharper contraction in private investment spending, as capacity expansion activity was affected by the considerable decline in external demand, lower-than-normal capacity utilisation and deteriorating business confidence. As a result, aggregate domestic demand declined by 2.9% and the economy contracted sharply by 6.2% in the first quarter of 2009 (Chart 4), the first contraction since the third quarter of 2001. A large inventory drawdown during the quarter, particularly in the manufacturing and commodity sectors, further contributed to the decline in growth.

Chart 4
External Weakness Led To Broad-based Domestic Weakness in the Economy by the First Quarter of 2009



Source: Department of Statistics, Malaysia

Policy Response and the Recovery of the Malaysian Economy

In response to the global crisis, the Government introduced several policy measures to mitigate the adverse impact of the global downturn, and to prevent the economy from slipping into a fundamental economic recession (Table 1). These measures centred around three broad areas, namely, fiscal policy (two stimulus packages amounting to RM67 billion or 9.9% of GDP were unveiled), monetary easing (the Overnight Policy Rate was reduced by a total of 150 basis points to 2.00%) and reinforced by comprehensive measures to ensure continued access to finance. The implementation of these measures not only provided direct support to domestic activity, but equally important, led to a revival in business and consumer sentiments. As a result, domestic demand registered a slower decline of 2.2% in the second quarter of 2009, and subsequently recovered to record a positive growth of 1.7% in the second half of the year. Of significance is the improvement in private consumption, which recovered to post a growth of 0.5% in the second quarter, before strengthening further to 1.7% in the fourth quarter.

On the external front, the stabilisation and subsequent gradual recovery in the global economy since the middle of the year provided further support to the Malaysian economy. In particular, the strong recovery in the regional economies, especially PR China, benefited Malaysia, with exports to the region starting to improve in the second half of the year. In particular, Malaysia's exports to PR China turned around to record positive annual growth rates from as early as August. The recovery in exports became more broad-based towards the end of the year, as exports to several advanced economies also began to recover. External demand contributed positively to growth by the fourth quarter of 2009.

Conclusion

The Malaysian economy, given its high degree of openness, was affected by the global recession which set in during the third quarter of 2008 and continued into the first quarter of 2009. With the stabilisation of the global financial markets and the subsequent recovery in the economies of the advanced countries, the rapid policy responses on both the fiscal and monetary fronts had an important role in sustaining domestic demand throughout this period. Malaysia's sound economic fundamentals, strong financial system and the implementation of comprehensive policy support measures prevented the economy from slipping into a severe and prolonged period of negative growth. The strong economic and financial foundations provided the basis for a rapid recovery. The strength and stability of the domestic financial system throughout this period ensured that financing continued uninterrupted and enabled the private sector to obtain access to credit. Coupled with the healthy private sector financial position, this facilitated a fast recovery in domestic demand once the global financial crisis was contained and the global economic and financial conditions stabilised. These fundamentals enhance the prospects for a stronger recovery going forward.

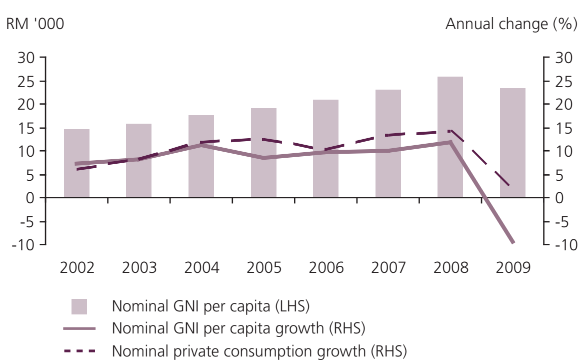
Table 1: Policy Responses to Mitigate Economic Downturn

Policy Responses	Measures
Two Economic Stimulus Packages of RM67 billion (direct fiscal injection: RM22 billion), with a primary focus on supporting domestic demand as well as mitigating the impact of the global downturn on the affected segments of the economy	➢ First package (RM7 billion) • Construction, upgrade, repair and maintenance of facilities • Construction of low and medium cost houses • Human capital development programmes • Accelerated improvement to telecommunication services • Assistance to Private Sector ➢ Second package (RM60 billion) • Reducing unemployment and increasing employment opportunities • Easing people's burden, in particular, the vulnerable groups • Assisting the private sector in facing the crisis • Building capacity for the future
Monetary stimulus to reduce the cost of intermediation	➢ Reduced Overnight Policy Rate by 150 basis points between November 2008 and February 2009 to 2.0% ➢ Reduced Statutory Reserve Requirement by 300 basis points to 1.0%
Comprehensive measures to ensure continued access to financing as well as to minimise the impact of the economic downturn on specific affected sectors	➢ Ensure continued access to financing • Financing and guarantee schemes for SMEs and businesses • Establishment of Financial Guarantee Institution (Danajamin Nasional Bhd) ➢ Restructuring and Rescheduling of Credit Facilities • Flexibilities to restructure and reschedule loans to deal pre-emptively with borrowers • Enhanced Corporate Debt Restructuring Committee and expanded Small Debt Resolution Scheme ➢ Pre-emptive measures to sustain confidence in financial sector • Full guarantee of all deposits until end-2010 • BNM's liquidity facility was extended to insurance and takaful operators ➢ Avenues for borrowers to seek assistance & redress • Integrated Contact Centre: BNMLINK, BNMTELELINK, Complaints Management and Advisory Unit • Expanded outreach of Credit Counselling & Debt Management Agency • ABMConnect Toll Free Channel • Complaint units at financial institutions • Financial Mediation Bureau • Small Debt Restructuring Committee
Other Measures	➢ Voluntary reduction of EPF employees' contribution by 3 percentage points from 11% to 8% in 2009 and 2010 ➢ Allow purchase of commercial properties above RM500,000 by foreigners for own use without FIC approval ➢ Increase vehicle loan eligibility for civil servants

affected by high retrenchments and a decline in real wages that had begun towards the end of 2008. Weak consumer spending was reflected in major consumption indicators such as the sales of new passenger cars, loan disbursements to households and imports of consumption goods. The MIER Consumer Sentiments Index (CSI) remained below the 100-point threshold (1Q 09: 78.9 points), indicating a pessimistic outlook on employment prospects and income expectations by households. As a result, private consumption declined by 0.7% in the first quarter.

Private consumption improved gradually from the second quarter onwards, before recording a higher growth of 1.7% in the fourth quarter. Improvements in labour market conditions, higher commodity prices and earlier than expected recovery in the manufacturing sector had lent support to consumer spending. Also, an early monetary policy response and the implementation of two fiscal stimulus packages helped to revive consumer confidence, as reflected by the improvement in the MIER CSI to above the 100-point threshold since the second quarter of 2009. Moreover, favourable financing conditions offered additional support to consumer spending as consumers continued to enjoy access to credit in an environment of low interest rates. Of significance, household credit continued to expand during the year with loan disbursed to households increasing strongly by 17.3% (2008: 8.9%). Despite the economic slowdown, household balance sheets remained sound, with the household debt to financial assets ratio remaining low at 40.6% (2008: 42.6%) and non-performing loan ratio for household loans declining further to 3.1% at the end of 2009 (2008: 4.1%).

Chart 1.5
GNI per Capita

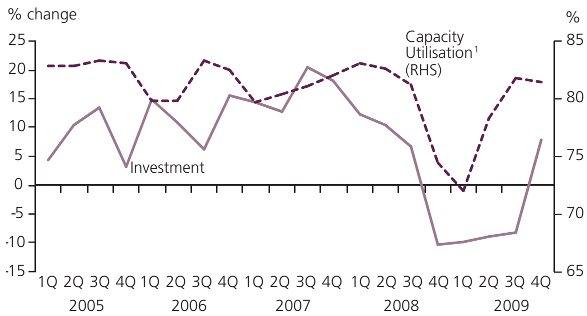


Reflecting the full impact of the global economic downturn in 2009, **private investment** declined significantly by 21.8% during the year (2008: 0.8%). The decline in capital spending activity that began at the end of 2008 had continued to worsen as the year progressed. Businesses deferred or cancelled investment decisions given deteriorating external demand and a more cautious outlook on domestic economic conditions. The sluggish private sector capital spending was also reflected in the marked decline of major investment indicators. Imports of capital goods recorded a decline of 5.9%, while sales of construction-related materials declined significantly by 26.1%. Disbursement of loans to businesses and the issuance of private debt securities for new activity also slowed down during this period, reflecting weaker demand for business financing. Meanwhile, gross inflows of FDI moderated to RM31.6 billion, as foreign investors were affected by the less favourable global economic environment. These indicators, however, gradually improved towards the end of 2009, as global economic conditions began to recover.

Investment in the manufacturing sector was the most affected by the extremely weak global economic conditions. The sharp decline in manufactured exports had led to a significant slowdown in production activity, in turn resulting in lower capacity utilisation. In the first quarter of 2009, the MIER capacity utilisation rate declined to 72%, reducing the need for firms to embark on additional capacity expansion. However, the capacity utilisation rate improved markedly to 81.4% in the fourth quarter, in line with the better performance of the manufacturing sector.

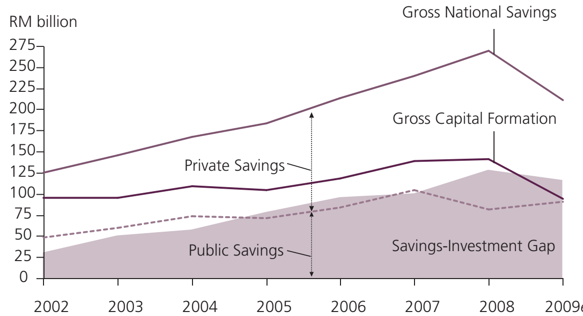
Capital spending programmes in the other sectors of the economy continued in 2009, albeit at a smaller scale compared to the previous year. Capital expenditure in the oil and gas sector, mainly for upstream production facilities and exploration activity, remained sizeable. Investment in the services sector was also sustained, reflecting the ongoing capacity expansion and upgrading exercise in the transportation, utilities and telecommunication sub-sectors, as well as the opening of new retail outlets.

Chart 1.6
Total Nominal Investment and Manufacturing Sector Capacity Utilisation



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

Chart 1.7
Gross National Savings and Savings-Investment Gap



e Estimate

Public investment expanded strongly in 2009, recording a double-digit growth of 12.9% (2008: 0.7%) following the introduction of the two economic stimulus packages to mitigate the impact of the global economic downturn. In the economic sector, expenditure was aimed mainly at developing the rural and agriculture sector, improving the transport system, enhancing public utilities and upgrading industrial infrastructure. Capital spending in the social services sector continued to be targeted at improving the provision of essential services, namely education, healthcare and housing. Of importance, high impact projects outlined in the first stimulus package had been fully implemented, while about 64% of the allocated development expenditure in the second package had been implemented in 2009.

Capital spending activity by the non-financial public enterprises (NFPEs) had also supported the strong expansion in public sector investment in 2009. Investment by the NFPEs was largely concentrated in the mining, transportation, utilities and communication sectors. In the mining sector, capital expenditure in the upstream oil and gas segment remained high, while the increased capital spending in the transportation sector was attributable to capacity expansion undertaken by both the rail and air transport companies. Additional capital spending was also evident in the power utility segment due to continuous upgrading and improvement of the power generation, transmission and distribution systems. Meanwhile, capital spending in the communication sector was mainly focused on the development of the broadband infrastructure facility under the High Speed Broadband initiative.

Public consumption increased by 3.7% in 2009 (2008: 10.9%), largely on the account of higher expenditure on emoluments, partly as a result of the higher emoluments incurred under the Government's initiative to fill up almost 50,000 vacancies in the public sector. Expenditure for supplies and services remained large due to the enhancement of the public sector's administrative machinery and delivery system as well as the maintenance of buildings and fixtures.

Public sector savings increased to RM92.3 billion or 13.9% of gross national income (GNI) in 2009 (2008: RM80.9 billion or 11.3%) following larger operating surpluses of the NFPEs. Private sector savings, however, declined to RM114.9 billion or 17.4% of GNI (2008: RM189.9 billion or 26.6%), reflecting the sustained household consumption spending amid the decline in income growth. In total, **gross national savings (GNS)** declined for the first time since 2001 by 23.5% to RM207.2 billion. Nevertheless, the decline in GNS was largely offset by a contraction in private sector investment, which led to a slightly lower savings-investment surplus of RM112.7 billion or 17% of GNI in 2009 (2008: RM129.5 billion or 18.1%).

SECTORAL REVIEW

Overall, 2009 was a challenging year for most economic sectors in the Malaysian economy. In the first quarter, amid the worsening global and domestic economic environment, all sectors, except construction, registered negative growth. In particular, the external demand-dependent sub-sectors were significantly affected, with an unprecedented rate of contraction in the electronics and electrical products cluster of the manufacturing sector and sharp contractions in trade-related services sub-sectors. In addition, spill-over weaknesses from the external sector to domestic demand, as well as lower commodity prices, also resulted in weak performance across most of the other sub-sectors.

Conditions began to improve in the second quarter, underpinned by the concerted and timely domestic policy support and stabilising external environment. The implementation of the two fiscal stimulus packages and the accommodative monetary policy environment cushioned the weakness in external demand and contributed towards improving consumer and business sentiments in the domestic-oriented sectors. Of significance, the construction sector registered positive growth in all four quarters, benefiting mainly from the projects under the 9MP and the fiscal stimulus packages. The pace of improvements gathered momentum in the third quarter, with smaller rates of decline in the manufacturing, agriculture and mining sectors. By the fourth quarter, growth resumed in all sectors, except mining, as domestic demand strengthened and external conditions improved further.

Services Sector

The **services sector** expanded by 2.6% in 2009 (2008: 7.2%), providing support to the Malaysian economy during the global economic crisis. Consequently, the sector's share to GDP increased further to 57.4% from 55.0% in 2008. The sector benefited from the resilient domestic demand, which was supported by the fiscal stimulus and an accommodative monetary policy. After registering a marginal decline of 0.2% in the first quarter of 2009, the services sector turned around to record an expansion of 1.6% in the second quarter, and continued its positive growth path to expand by 4.3% in the second half of 2009 (1H 2009: 0.8%). While most services sub-sectors followed the same growth trend, those that are largely dependent on trade and manufacturing activities, namely transport and storage; and utilities, recovered at a slower pace.

The services sector provided support to the overall economy in 2009

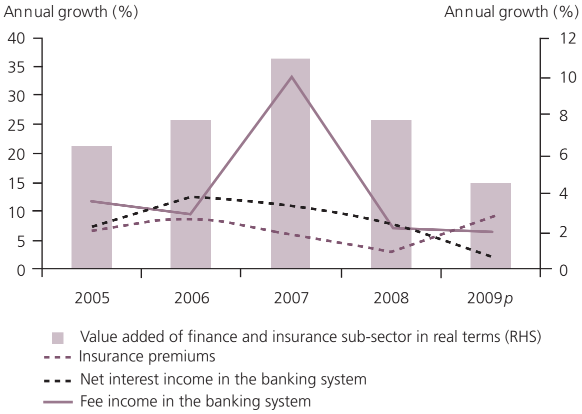
The **finance and insurance** sub-sector recorded a moderate growth of 4.4% (2008: 7.7%), reflecting the subdued performance of domestic demand especially in the first half of the year. In the finance segment, total loans approved and disbursed by the banking industry declined by 12.2% and 3.7% respectively in the first half of the year, as demand for financing moderated in tandem with lower economic activity. As a result, net interest income

Table 1.4
Services Sector Performance at Constant 2000 prices

	2008	2009*p*	2008	2009*p*
	Annual change (%)		Share to GDP (%)	
Services	**7.2**	**2.6**	**55.0**	**57.4**
Intermediate services	6.0	3.0	23.8	25.0
Finance and insurance	7.7	4.4	11.0	11.7
Real estate and business services	1.5	2.1	5.1	5.3
Transport and storage	6.1	-2.8	3.8	3.8
Communication	7.3	6.0	3.9	4.2
Final services	8.3	2.2	31.2	32.4
Wholesale and retail trade	9.8	1.2	12.8	13.2
Accommodation and restaurant	7.3	2.7	2.4	2.5
Utilities	2.1	0.4	2.9	3.0
Government services	11.1	3.0	7.4	7.7
Other services	5.2	4.4	5.7	6.0

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

Chart 1.8
Performance of the Finance and Insurance Sub-sector vis-à-vis Related Indicators



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Source: Department of Statistics, Malaysia; Bank Negara Malaysia

of the banking system recorded a lower growth. Meanwhile, fee-based income declined in the first quarter, due mainly to a drop in fees related to capital market activity. However, conditions in the finance segment improved during the second half-year, as economic recovery gathered momentum. Loan indicators registered marked improvements, while net interest income recorded better growth and fee-based income increased significantly by 18% following higher turnover in the equity market. In the insurance industry, growth was more moderate, as both the life and general business segments were affected by the weak economic activity and the decline in motor vehicle sales in the first half. However, both segments improved in the second half, in tandem with the economic recovery.

The **wholesale and retail trade** sub-sector was affected by weak private consumption, especially in the first half of the year. The sub-sector contracted by 1.7% in the first quarter, due to lower wholesale activity, cautious consumer spending and the contraction in motor vehicle sales. As consumer sentiments subsequently improved amid better domestic economic and labour market conditions, the sub-sector turned around to register a marginal growth in the second quarter before gradually strengthening in the second half of the year. For the year as a whole, the sub-sector grew by 1.2% (2008: 9.8%).

Similarly, the **real estate and business services** sub-sector registered a decline of 6.7% in the first quarter but recovered subsequently to expand by 2.1% for the year as a whole (2008: 1.5%). Affected by weak business sentiments at the beginning of the year, the sub-sector improved in the second half of 2009, benefiting from higher real estate and capital market-related activities as domestic demand strengthened. In 2009, the Kuala Lumpur Composite Index rallied 45.2%, to close the year at 1,272.8 (end-2008: 876.8).

Both the **accommodation and restaurant** and **other services** sub-sectors recorded lower growth

Table 1.5
Selected Indicators for the Services Sector

	2008	2009*p*
	Annual change (%)	
Utilities		
Electricity production index	1.2	0.8
Wholesale & Retail Trade and Accommodation & Restaurant		
Consumption credit disbursed	10.8	14.0
Tourist arrivals	5.1	7.2
Total sales of motor vehicles	12.5	-2.1
Finance & Insurance and Real Estate & Business Services		
Loans outstanding in the banking system	12.8	7.8
Insurance premiums	2.9	9.1
Bursa Malaysia turnover (volume)	-59.8	60.6
Transport & Storage and Communication		
Total container handled at Port Klang and PTP (TEUs)	7.7	-1.8
Airport passenger traffic	5.9	6.9
Air cargo handled	-6.7	-13.7
SMS traffic	28.7	22.1
	%	
Penetration rate:		
- Broadband[1]	21.1	31.7
- Cellular phone[2]	98.9	106.2
- Fixed line[1]	44.9	44.0

[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; Pelabuhan Tanjung Pelepas Sdn Bhd; Malaysia Airports Holdings Berhad; Senai Airport Terminal Services Sdn Bhd; Malaysian Communications and Multimedia Commission; and Bank Negara Malaysia.

rates of 2.7% and 4.4% respectively in 2009 (2008: 7.3% and 5.2% respectively). Growth in the accommodation and restaurants sub-sector remained weak in the first half of the year, in tandem with sluggish private consumption activity. Growth improved in the second half, supported by better consumer sentiments and a rise in regional travel, following the expansion of new routes by airlines and various tourism promotional activities organised during the year. Meanwhile, growth in the other services sub-sector was affected mainly by softer demand for private education and private healthcare during the year. In addition, the global economic slowdown had affected the number of foreign students and foreign patients seeking education and healthcare services in the country.

The **communication** sub-sector was only marginally affected by the economic slowdown, registering a strong growth of 6% (2008: 7.3%). Growth was supported by continued demand for cellular and broadband services arising from competitive pricing by service providers as well as the aggressive rollout of broadband services. The year also saw extensive promotions by both the fixed and wireless broadband players to attract new subscribers. In addition, the availability of affordable smart phones and Wi-fi-enabled devices in the market also boosted demand for data services. These positive developments were reflected in the increase in both the cellular penetration rate (end-2009: 106.2%; end-2008: 98.9%) and broadband penetration rate (end-2009: 31.7%; end-2008: 21.1%).

In contrast, the **utilities** sub-sector registered a marginal growth of 0.4% compared to a 2.1% growth in 2008 as it was affected by lower demand for electricity during the year. In the first half of the year, growth declined by 4.6%, in line with the sharp drop in manufacturing activity. The sub-sector returned to positive growth in the third quarter before expanding strongly in the fourth quarter. The improvement in the utilities sub-sector was reflective of the gradual recovery in electricity demand from industrial users, and the steady increase in demand from household and commercial users.

Meanwhile, the **transport and storage** sub-sector was the worst performing services sub-sector, with three consecutive quarters of contraction before turning around to record a positive growth in the fourth quarter. Performance was affected by the decline in global trade and local manufacturing activity, which resulted in lower demand for shipping, haulage, ports and other trade-related services. However, the performance of the sub-sector gradually improved in the second half, in line with the improvement in trade and manufacturing activity. This was further supported by the steady increase in passenger travel, benefiting from improvements in consumer sentiments and the aggressive discounts offered by both full-service and low-cost carriers. For the year as a whole, the sub-sector declined by 2.8% (2008: 6.1%).

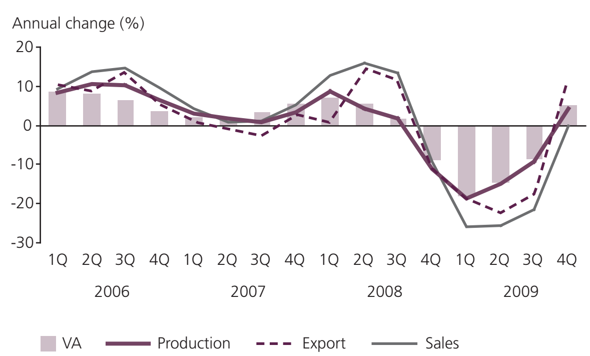
Manufacturing Sector

The **manufacturing sector** faced a challenging start in 2009, as the sharp decline in exports at end-2008 worsened further. The contraction in the sector stabilised in the second quarter of 2009 and conditions became more favourable towards the year-end, with production recording a positive growth in the fourth quarter of 2009, after experiencing four consecutive quarters of declines.

Manufacturing sector contracted significantly in the first quarter, but conditions gradually improved from second quarter onwards

In the export-oriented industry, the **electronics and electrical products (E&E) cluster** was the worst affected by the global downturn,

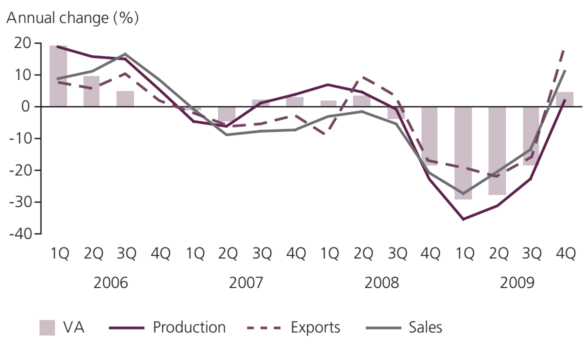
Chart 1.9
Manufacturing Sector: Value-added, Production, Exports and Sales



Source: Department of Statistics, Malaysia

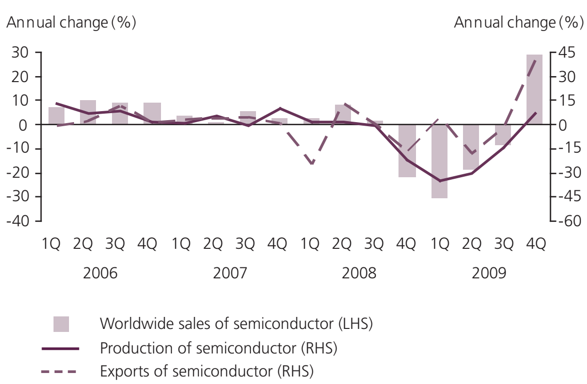
declining by 22.8% in 2009. Production fell sharply by 35.4% in the first quarter, following a significant drop in global demand. Manufacturers across the global E&E supply chain reacted by cutting back production and drawing down from inventory, adversely affecting the semiconductor segment. Similarly, broad contraction in global demand also led to substantial declines in the computer and parts and electrical product segments. In particular, lower output of computer and parts was due to corporations delaying investment in equipment and software, while the electrical products segment was influenced by lower consumer spending. However, the decline in output moderated from the second quarter onwards, especially for semiconductors and electrical products, supported by an improvement in regional demand and inventory replenishment activity. In the region, the implementation of economic stimulus measures partially helped to boost demand for final electronic products. The E&E cluster performed better in the fourth quarter to record a marginal expansion, driven by higher consumer spending on electronics such as netbooks, smartphones and flat panel televisions, during the festive season, both in the advanced and regional economies.

Chart 1.10
E&E Cluster : Value-added, Production, Exports and Sales



Source: Department of Statistics, Malaysia

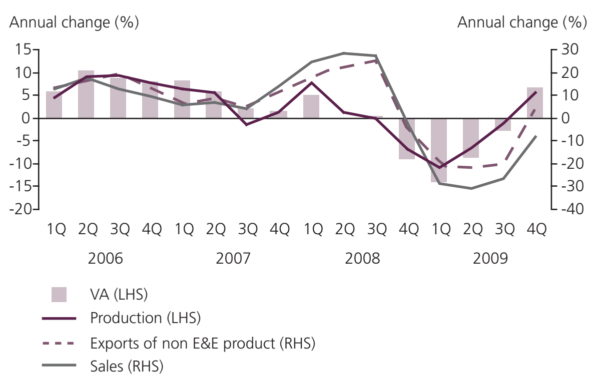
Chart 1.11
Production and Exports of Semiconductors



Source: Department of Statistics, Malaysia
Semiconductor Industry Association (SIA)

The **primary-related cluster** recorded similar trends to the E&E cluster, but fared better due to support emanating from the domestic consumer market and regional demand. Of significance, the sharp fall in the chemical products industry in the first quarter was due to lower demand for plastic parts and components used in the E&E and automotive industries. Meanwhile, production of the off-estate processing industry was affected by unfavourable commodity prices, providing less incentive to process off-estate products. The cluster performed better from the second quarter onwards, led by the chemical products industry as demand for plastic parts and components picked up with the improving E&E and household goods segments. The rubber products industry turned positive in the third quarter, driven by increasing demand for hygiene and medical products due to the Influenza A (H1N1) pandemic, while movements in commodity prices in the second half of the year contributed positively to the production in the petroleum and off-estate processing industries. By the fourth quarter of 2009, the cluster turned around to grow by 6.7%, led by

Chart 1.12
Primary-related Cluster: Value-added, Production, Exports and Sales



Source: Department of Statistics, Malaysia

Remaining Competitive: Issues in Enhancing Productivity, Energy Efficiency and Innovation in the Manufacturing Sector

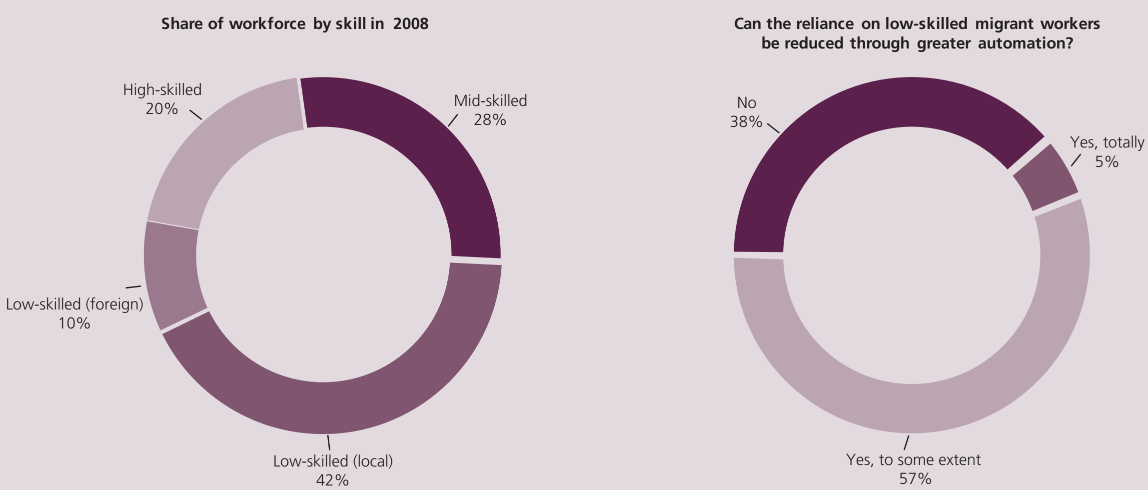
Introduction

As Malaysia advances towards becoming a high value-added economy, productivity, energy efficiency and innovation will increasingly gain importance for the economy to remain competitive and to move up the value-added chain. The manufacturing sector is no exception, where the reliance on cost competitiveness will not be sustainable in the longer term. This article discusses the various efforts undertaken and constraints faced by Malaysian manufacturers in enhancing productivity, energy efficiency and innovation amidst an increasingly challenging global environment. The analysis draws on the BNM Biennial Manufacturing Survey 2008[1].

Productivity

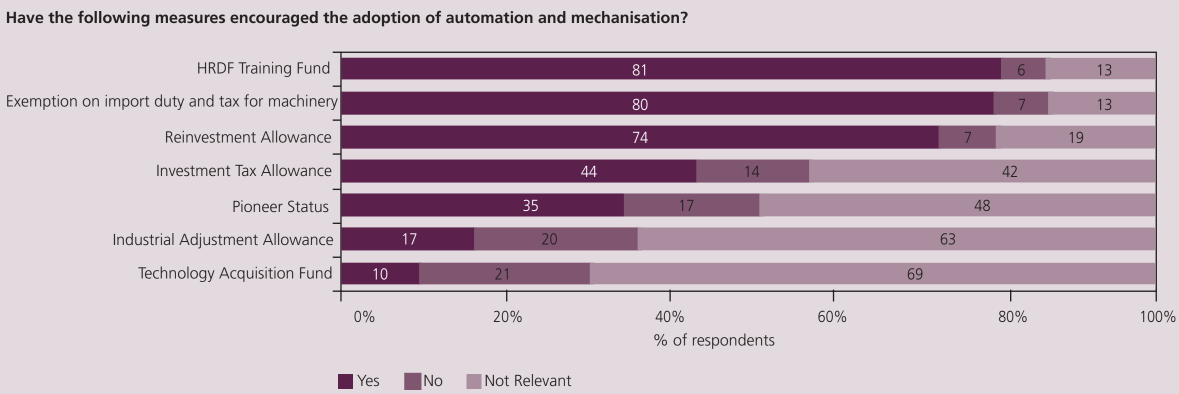
Improving the skills of the workforce and increasing automation in the existing production lines are the most common strategies adopted by manufacturers in enhancing productivity. **Upskilling** is vital as about 80% of the manufacturing workforce is low to mid-skilled, and less than half of the workers have received formal training. Training and retraining opportunities focus mainly on improving technical skills, with about half of the training budget allocated for this. To enhance **automation**, manufacturers continue to face several impediments, particularly in terms of the high cost of machinery and equipment as well as an insufficient scale of production to justify extensive automation. In addition, the presence of easily available and relatively cheap low-skilled workers potentially further hinders the adoption of greater automation, as the survey result indicates that about 60% of the jobs currently undertaken by low-skilled foreign workers can to some extent, be replaced by automation (Chart 1). Manufacturers also highlight the importance of Government incentives in supporting automation, identifying the Human Resource Development Fund (HRDF) training fund, exemption on import duty and tax for machinery, and Reinvestment Allowance as the three most effective measures (Chart 2).

Chart 1
Large presence of low cost, low-skilled workers potentially hinders greater adoption of automation



[1] The BNM Biennial Manufacturing Survey 2008 was conducted in December 2008, covering 301 manufacturing companies in 17 industries, categorised into four clusters: electronics and electrical products (E&E): 90 companies; primary-related: 119 companies; consumer-related: 47 companies and construction-related: 45 companies. The response rate was at 56% at the close of the survey on 30 April 2009.

Chart 2
Exemption on import duty and tax on machinery and Reinvestment Allowance are effective in encouraging automation



Innovation

Innovation, proxied by the extent of **research and development (R&D**) **activity**, is fundamental for manufacturers to move up the value chain. About 57% of the manufacturing firms surveyed undertook R&D activity in 2008. A major constraint to greater R&D activity that has been identified by manufacturers is the quality of the workforce. At present, only about 20% of the manufacturing workforce consists of **high-skilled labour**, while manufacturers face difficulties in the hiring of high and semi-skilled workers, to the extent that there is currently a critical shortage of engineers, technicians, supervisors and quality control experts. This situation is expected to remain for at least the next three years (Chart 3). Meanwhile, only about 10% of the respondents that undertook R&D activity in 2008 utilised the available Government incentives, citing heavy administrative burdens as discouraging application (Chart 4). Most respondents suggested that easing the application process and the eligibility criteria for the Government incentives would enhance accessibility to these incentives.

Chart 3
Difficulties faced in hiring skilled workers with critical shortages of engineers and technicians

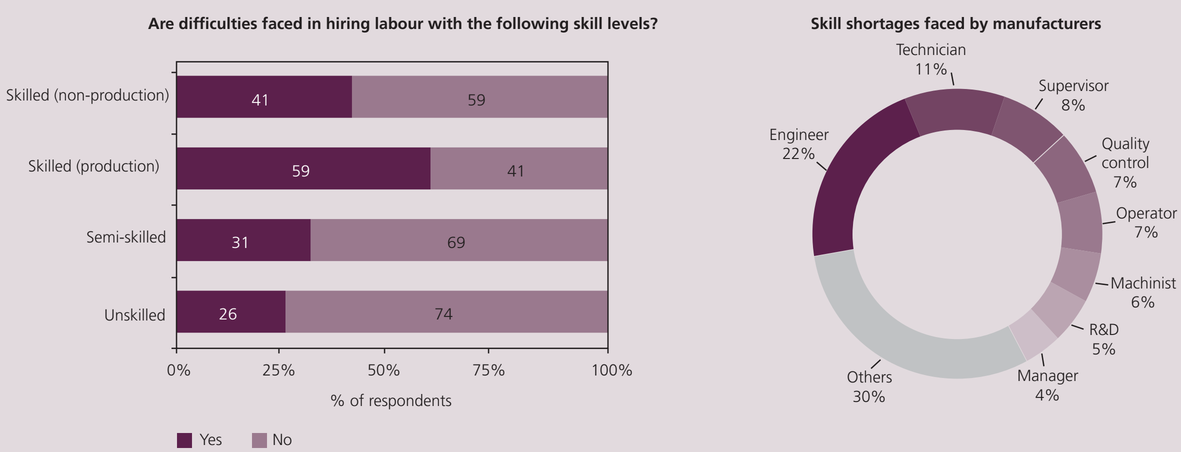
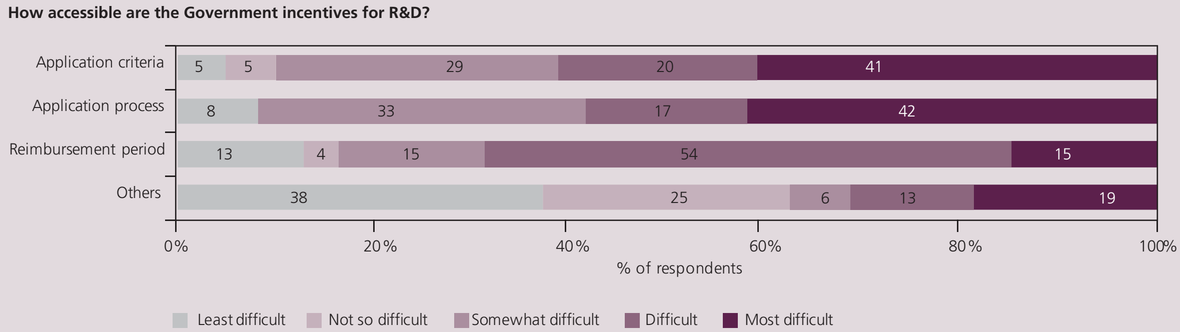


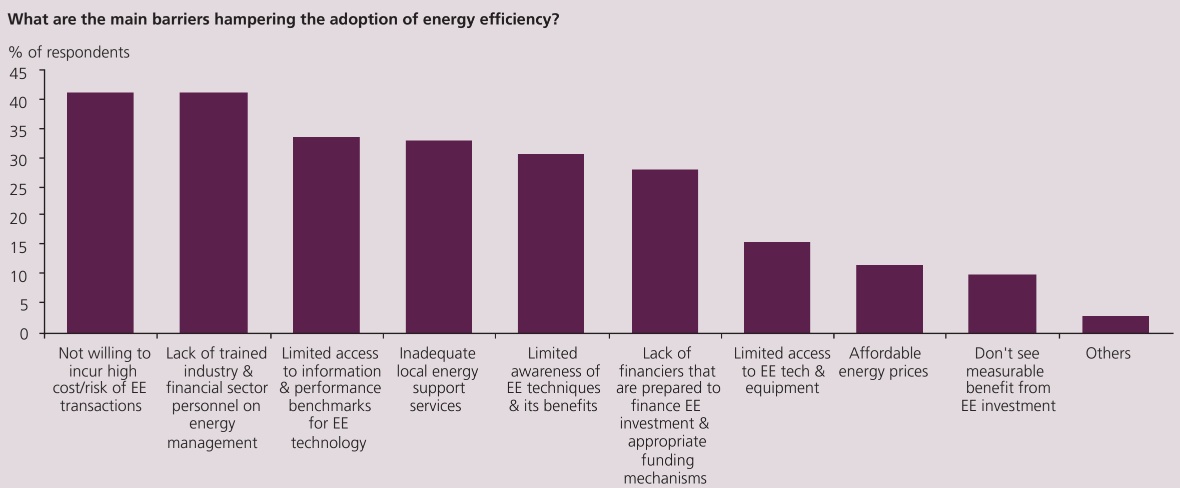
Chart 4
Heavy administrative burdens discourage application for Government incentives on R&D



Energy Efficiency

Given the high energy consumption in the manufacturing sector and the rise in utility costs since 2005, **energy efficiency** (EE) constitutes an important component of enhancing the overall efficiency of the sector. However, despite the importance of energy management and due, in part, to different levels of awareness of the benefits of EE, less than 30% of the firms surveyed have a full-time energy manager, while only about 40% have conducted an energy audit since 2005. Furthermore, less than 20% of the respondents had utilised the various Government incentives available for EE. The key challenges reported to be faced in the adoption of EE include the unwillingness to incur additional costs from the significant capital outlays to adopt EE, especially given uncertain potential returns, and the lack of trained human capital and information specific to EE (Chart 5).

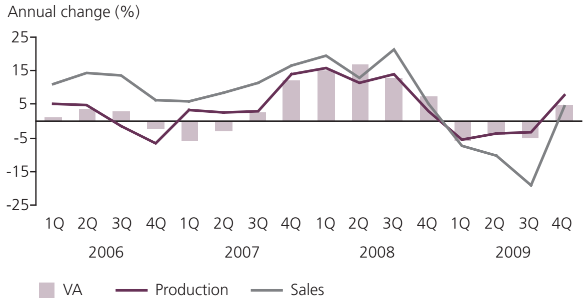
Chart 5
Significant barriers exist against the adoption of energy efficiency



Conclusion

The Malaysian manufacturing sector has, in varying degrees, employed strategies, such as upskilling, increasing automation, undertaking R&D activities and conducting energy audits, to enhance productivity, improve energy efficiency and strengthen innovation, so as to remain competitive in an increasingly challenging global environment. However, there remain challenges and constraints in these endeavours that need to be promptly addressed for the successful movement up the value chain. Of significance are the issues of human capital, high initial investment costs and administrative burden in gaining access to the incentives and funding programmes.

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

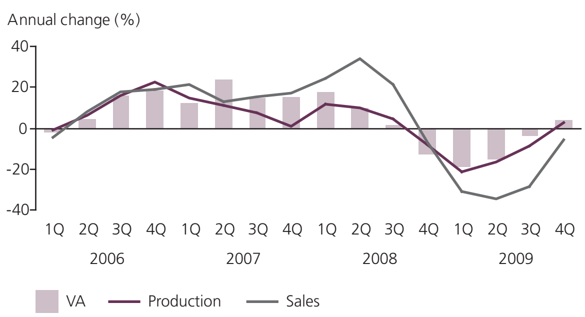


Source: Department of Statistics, Malaysia

higher demand for chemical, rubber and off-estate processing products.

In the domestic-oriented industry, performance in the first quarter was affected by the weak labour market conditions and dampened consumer spending. As domestic conditions improved from the second quarter onwards, production also recovered gradually to register a positive growth in the fourth quarter. The **consumer-related cluster** was negatively affected by the large decline in the transport equipment industry, in line with the sharp decline in new motor vehicle sales. Nonetheless, the food, beverages and tobacco industry provided some support to the cluster, due to sustained demand for food products. Output dipped slightly in the first quarter, before recovering from the second quarter onwards to grow by 7.7% in the fourth quarter, reflecting the improvement in domestic private consumption.

Chart 1.14
Construction-related Cluster: Value-added, Production and Sales



Source: Department of Statistics, Malaysia

Performance of the **construction-related manufacturing cluster** mirrored both external and domestic demand, registering a sharp contraction in the first quarter, particularly in production of iron and steel due to slower domestic civil engineering activity and lower regional demand. The cluster, however, gradually improved from the second quarter onwards to record a positive growth in the fourth quarter. The improvement in the cluster reflected the strong pick up in the domestic construction activity, as the implementation of stimulus measures gathered momentum.

Table 1.6
Performance of the Manufacturing Sector

	2008	2009
	Annual change (%)	
Value-added (RM million at 2000 prices)	**1.3**	**-9.3**
Manufacturing Production[1]	**0.7**	**-10.0**
Export-oriented industries	**-1.2**	**-11.1**
Electronics & electrical products cluster	**-3.6**	**-22.8**
of which:		
Electronics	-5.4	-24.6
Electrical products	0.9	-18.8
Primary-related cluster	**0.4**	**-3.5**
of which:		
Chemicals and chemical products	-3.5	-1.7
Petroleum products	5.9	-0.8
Rubber products	4.7	-3.0
Off-estate processing	9.4	-2.1
Domestic-oriented industries	**8.0**	**-5.7**
Consumer-related cluster	**11.0**	**-1.2**
of which:		
Transport equipment	23.4	-12.4
Food, beverage & tobacco products	7.4	1.5
Construction-related cluster	**4.3**	**-11.4**
of which:		
Construction-related products	3.2	-18.1
Fabricated metal products	6.1	-1.1
Exports	**3.8**	**-12.5**

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

Agriculture Sector

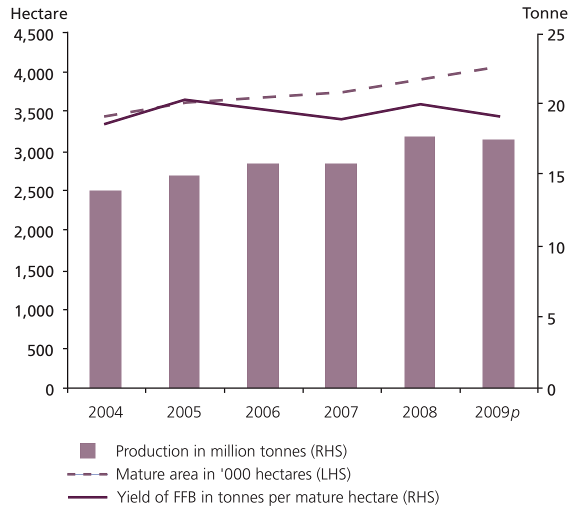
The agriculture, forestry and fishing **(agriculture) sector** grew at a slower pace of 0.4% in 2009 due to lower production of industrial crops. However, higher output of key food-related industries such as fisheries and livestock provided support to the sector.

The agriculture sector recorded marginal growth due to lower production of industrial crops

The production of **crude palm oil** declined by 1% to 17.6 million tonnes in 2009, due to the biological yield down-cycle, unfavourable weather conditions and replanting activity. Consequently, average national fresh fruit bunches (FFB) yield per hectare declined by 4.9% to 19.2 tonnes. Yields in Sabah and Sarawak, which accounted for 42% of total production, registered sharp drops of 8.1% and 5.7% respectively, due mainly to the heavy rainfall in East Malaysia in early 2009. Despite weaker production, palm oil stocks were higher by 12.2% at 2.24 million tonnes at the end of 2009, due to weaker global demand. As a result, the average CPO price fell by 19.2% to RM2,245 per tonne in 2009 (2008: RM2,778 per tonne).

Natural rubber production contracted by 20.2% to 0.86 million tonnes in 2009 due to weather-related factors, weak prices in the early part of the year, as well as the implementation of a programme to curb exports by the three major rubber producing countries. As prices plunged sharply towards the end of 2008, Malaysia, Thailand and Indonesia agreed to cut

Chart 1.15
Oil Palm: Area, Production and Yield



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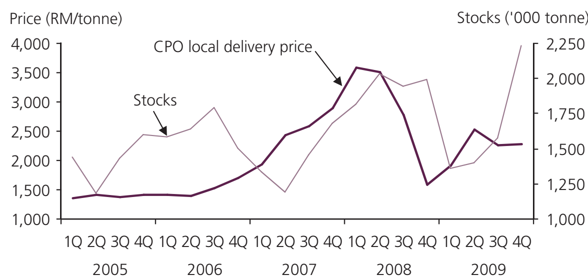
Source: Malaysian Palm Oil Board (MPOB)

Chart 1.16
Palm Oil Price and Stocks



Source: Malaysian Palm Oil Board (MPOB)

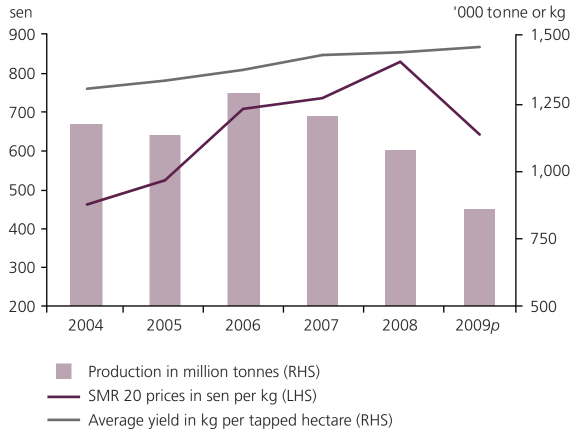
Table 1.7
Agriculture Sector:
Value Added and Production

	2008	2009*p*
	Annual change (%)	
Value added	**4.0**	**0.4**
Industrial crops	**2.9**	**-4.6**
Production of which:		
Crude palm oil	12.1	-1.0
Rubber	-10.6	-20.2
Saw logs	-8.9	-10.9[2]
Cocoa beans	-20.5	-35.1
Food crops	**5.6**	**7.2**
Production of which:		
Fish	5.2	6.7
Livestock [1]	4.3	7.6
Vegetables	11.9	3.1
Fruits	3.2	0.6

[1] Refers to Peninsular Malaysia only
[2] Jan-Nov 2009
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

Chart 1.17
Natural Rubber: Production, Prices and Yield



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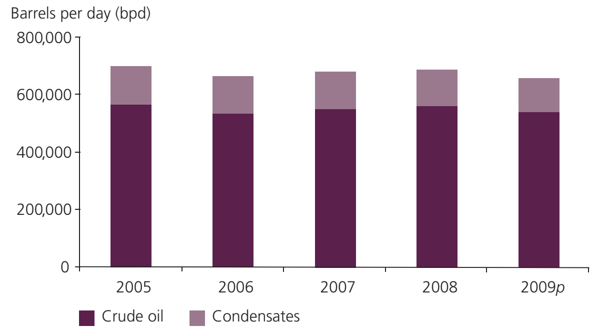
Source: Malaysian Rubber Board (MRB) and Department of Statistics, Malaysia

Chart 1.18
Production of Crude Oil and Condensates



p Preliminary

Source: PETRONAS

exports of natural rubber by 700,000 tonnes in 2009. In addition, low prices in early 2009 discouraged tapping activity, especially amongst price-sensitive smallholders. The drop in output was further compounded by the frequent occurences of heavy rainfall at the end of the year, which further disrupted tapping activity. As such, rubber prices more than doubled by the end of 2009 to 958 sen per kg.

Mining Sector

Value-added of the **mining sector** contracted by 3.8% in 2009, largely reflecting the lower output of crude oil and natural gas, following lower external demand and the shutdown of several oil and gas facilities during the year for maintenance purposes.

Table 1.8
Mining Sector: Value Added and Production

	2008	2009*p*
	Annual change (%)	
Value added	**-0.8**	**-3.8**
Production		
of which:		
Crude oil and condensates	1.1	-4.4
Natural gas	0.3	-4.0

p Preliminary

Source: PETRONAS
Department of Statistics, Malaysia

Production of **crude oil (including condensates)** averaged 659,845 barrels per day (bpd) in 2009, lower by 4.4% compared to 2008. In abiding to the production limits set by the National Depletion Policy, production in Peninsular Malaysia declined by 11.7% and accounted for 45% of total output of crude oil of the country. However, production in Sabah increased by 20%, supported by output from the deepwater oil field in Kikeh.

The mining sector contracted further due to lower output of both crude oil and natural gas

Output of **natural gas** contracted by 4% to 5,667 million standard cubic feet per day due to lower

Table 1.9
Malaysia: Crude Oil and Natural Gas Reserves[1]

	As at 1 January	
	2008	2009*p*
Crude oil (including condensates)		
Reserves (billion barrels)	5.46	5.52
Reserve/Production (year)	22	22
Natural gas		
Reserves (billion barrels of oil equivalent)	14.67	14.66
Reserve/Production (year)	36	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

demand for liquefied natural gas (LNG) from major importers. Nonetheless, support for LNG demand emerged in the fourth quarter with the commencement of the long-term contract for Petronas exports to China from October 2009. The output from Sarawak, which accounted for the bulk of the country's LNG production, declined by 4.7%.

Oil reserves in the country increased to 5.52 billion barrels or a lifespan of 22 years at current production levels. Meanwhile, natural gas reserves were at 14.66 billion barrels of oil equivalent, which are sufficient to cover 36 years of gas output at current production levels.

Construction Sector

The **construction sector** recorded a stronger growth of 5.7% in 2009 with improved performance across all sub-sectors. Growth picked up progressively throughout the year due primarily to the implementation of the construction-related activities under the 9MP and the fiscal stimulus packages. The performance of the sector improved significantly in the second half of the year, growing by 8.5% compared to 2.9% in the first half of the year. Meanwhile, stable costs of construction materials provided a further boost to activities in the sector.

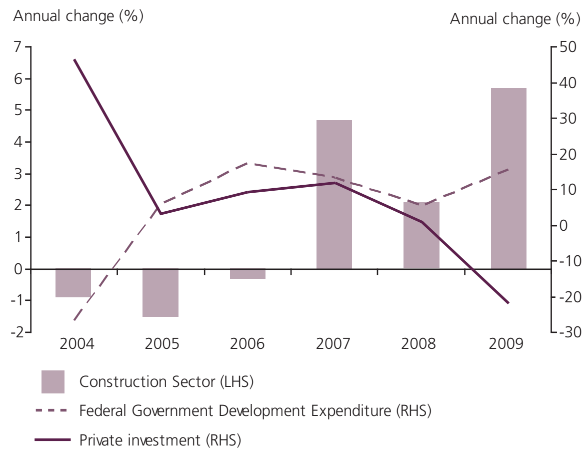
The construction sector recorded stronger growth in 2009

In the **civil engineering** sub-sector, growth was bolstered by the continued implementation of projects associated with the 9MP as well as those under the stimulus packages. This was evident from the 15.6% increase in the Federal Government development expenditure to RM49.5 billion, partly to upgrade existing infrastructure.

Growth in the **non-residential** sub-sector was robust, driven mainly by stimulus spending on the upgrading, repairing and maintenance of public buildings, as well as the on-going construction of commercial buildings. Incoming supply of office space in the Klang Valley was 6.4 million square feet at end-2009 (end-2008: 7.6 million square feet). Demand for office space in the Klang Valley was driven mainly by the relocation of existing tenants into new office buildings while new take-up was modest. As such, the occupancy rate in the area eased marginally to 82% in 2009 (2008: 84%). Rental rates generally remained stable during the year as incentives such as longer rent-free periods and free furnishing sustained the demand.

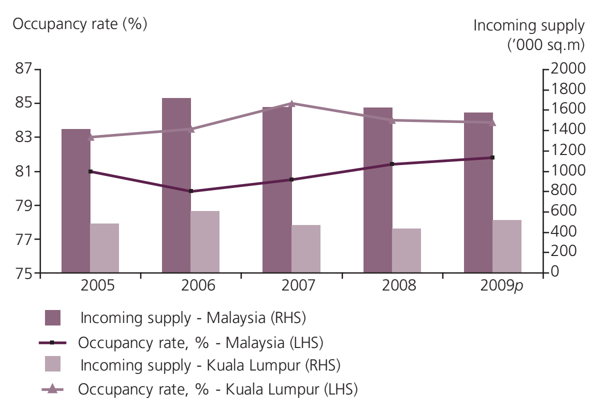
On retail space, fewer shopping complexes were constructed nationwide in 2009 following the considerable supply of large shopping centres that became available during 2007-2008. The 26 newly constructed shopping complexes were mainly neighbourhood malls catering to nearby residential

Chart 1.19
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

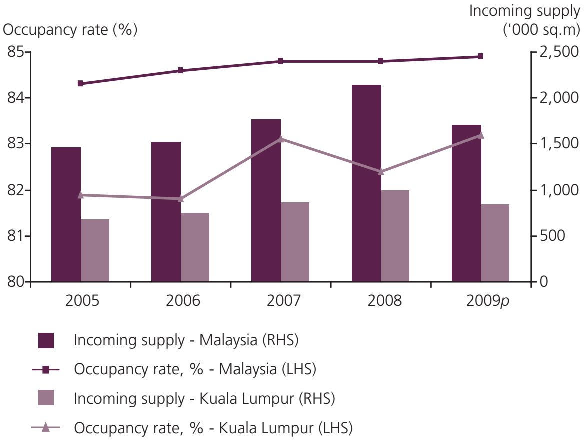
Chart 1.20
Incoming Supply and Occupancy Rate of Retail Space in Malaysia and Kuala Lumpur (as at end period)



p Preliminary

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

Chart 1.21
Incoming Supply and Occupancy Rate of Purpose-Built Office Space in Malaysia and Kuala Lumpur (as at end period)



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

areas. As at the end of 2009, the stock level of retail space rose to 10 million square metres (2008: 9.4 million square metres). Rental rates remained stable in prime centres, but softened slightly in other areas. Similar to the office market, landlords provided various incentives to attract tenants, in turn maintaining the occupancy rate at 81.8% (2008: 81.4%).

Performance in the **residential** segment was relatively mixed during the year. In the first quarter, demand for properties weakened due to uncertainty about the global and domestic economic outlook. Demand, however, started picking up in the second quarter as developers introduced attractive financing packages while borrowing costs were lowered following

Table 1.10
Demand and Supply Indicators of the Residential Property Market

	1H '08	2H '08	1H '09	2H '09*p*
Annual change (%)				
Demand indicators				
Residential property transactions				
Value (RM million)	35.5	-3.0	-14.3	17.1
Volume	20.7	-1.2	-10.4	5.7
Finance for purchase of residential property				
Loan applications	43.4	9.1	11.1	50.6
Loan approvals	42.3	3.4	0.3	44.1
Supply indicators				
New launches	**25.0**	**-23.0**	**-29.6**	**17.7**
New sales and advertising permits	**2.0**	**-38.6**	**-16.8**	**57.8**
Housing approvals	**19.0**	**-52.6**	**-23.7**	**66.7**
Loans for construction				
Loan applications	19.3	-33.2	-31.4	36.5
Loan approvals	20.5	-19.8	-38.2	4.2

p Preliminary

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

Table 1.11
Overhang of Residential Property in Malaysia by Price Range

Residential Price Range	Units	Share (%)	Units	Share (%)
	As at end-2008		As at end-2009*p*	
RM50,000 or less	3,602	13.8	2,946	13.0
RM50,001 - RM100,000	7,491	28.8	6,920	30.6
RM100,001 - RM150,000	4,045	15.5	3,550	15.7
RM150,001 - RM200,000	3,786	14.6	3,419	15.1
RM200,001 - RM250,000	2,119	8.1	1,947	8.6
RM250,001 - RM500,000	3,888	14.9	3,225	14.3
RM500,001 - RM1,000,000	993	3.8	481	2.1
More than RM1,000,000	105	0.4	104	0.5
Total	**26,029**	**100**	**22,592**	**100**

p Preliminary

Source: National Property Information Centre (NAPIC), Valuation and Property Services Department reductions in the OPR by a total of 150 basis points between November 2008 and February 2009. Between the second and fourth quarter of 2009, loan applications and approvals increased at an annual rate of 39.8% and 32.6% respectively, with relatively stronger growth in loans for the purchase of properties priced above RM250,000. With respect to the public sector, there was also an increase in the construction of low- and medium-cost houses as allocated under the stimulus packages.

For the whole year, the volume of residential property transactions contracted by 2.3%, while the value of property transactions rose by 1.3% to RM41.8 billion. Reflecting the overall cautious sentiments of property developers, the number of new launches declined by 15.8%. Given the lower incoming supply and the gradual improvement in demand, the property overhang declined by 13.2% to 22,592 units.

EXTERNAL SECTOR

Balance of Payments

Malaysia's external position remained strong in 2009. The **overall balance of payments** turned around to record a surplus as the continued large surplus in the current account more than offset the lower net outflows in the financial account. Despite the sharp contraction in external demand, the surplus in the current account was supported by a sizeable trade surplus, as lower demand for exports induced a corresponding decline in imports. Meanwhile, sustained regional travel activity resulted in improvements in the services account. The lower net outflows in the financial account largely reflected the significant moderation in portfolio outflows in the first half and the net inflows in the second half of the year. Both net inflows of foreign direct investment and outflows of direct investment abroad also moderated with the weak economic conditions. Other investment

Table 1.12
Balance of Payments

Item	2008			2009*p*		
	+	-	Net	+	-	Net
	RM billion					
Goods	664.3	493.8	170.6	554.2	412.7	141.5
Trade account	*663.5*	*521.6*	*141.9*	*553.3*	*434.9*	*118.4*
Services	101.0	100.9	0.2	99.1	95.9	3.2
Balance on goods and services	**765.4**	**594.7**	**170.7**	**653.3**	**508.6**	**144.7**
Income	39.9	63.6	-23.7	40.5	53.1	-12.6
Current transfers	1.4	18.9	-17.5	3.7	23.1	-19.4
Balance on current account	**806.7**	**677.2**	**129.5**	**697.5**	**584.8**	**112.7**
% of GNI			**18.1**			**17.0**
Capital account			0.6			-0.2
Financial account			-118.5			-82.9
Direct investment			-26.1			-24.9
Portfolio investment			-84.4			0.8
Other investment			-8.1			-58.9
Balance on capital and financial accounts			**-117.9**			**-83.1**
Errors and omissions			-29.9			-15.8
of which:						
Foreign exchange revaluation gain (+) or loss (-)			*-5.8*			*10.7*
Overall balance			**18.3**			**13.8**
Bank Negara Malaysia international reserves, net			**317.4**			**331.3**
USD billion equivalent			**91.5**			**96.7**

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

outflows, which largely reflected trade credits, increased during the year. After taking into account the foreign exchange revaluation gains arising from the strengthening of major currencies against the ringgit, the net international reserves increased by RM13.8 billion to RM331.3 billion (or US$96.7 billion) as at 31 December 2009. As at 25 February 2010, reserves amounted to RM331.8 billion (or USD96.8 billion). This level of reserves is adequate to finance 10 months of retained imports and is 4.3 times the short-term external debt.

Malaysia's external position remained strong despite the weak external environment

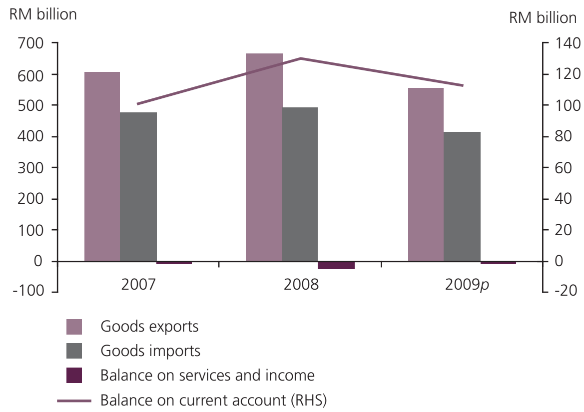
Current Account

The **current account** recorded a marginally smaller surplus of RM112.7 billion or 17.0% of GNI (2008: RM129.5 billion or 18.1% of GNI). Despite the sharp contraction in external trade, the trade surplus remained sizeable as the decline in intermediate imports largely offset the contraction in exports. A larger inflow of tourism receipts, particularly from Asia, contributed to a higher surplus in the services account, while the narrowing of the income account deficit was attributed mainly to lower profits and dividends accruing to the MNCs operating in the manufacturing sector.

Current account surplus remained large, supported by a sizeable trade surplus and an improvement in the services account

For the year as a whole, **gross exports** contracted by 16.6% (2008: +9.8%). Gross exports closely mirrored the developments in the global economy. The export contraction in the first half was exacerbated by the sharp adjustment in inventories by final producers in the importing countries. In addition, the decline in commodity prices also affected exports performance given that commodity and resource-based exports accounted for 39.4% of gross exports. In tandem with the gradual improvement in the global economy, particularly the regional economies, exports started to stabilise in the third quarter, before picking up momentum to register a positive growth of 5.1% in the fourth quarter. Inventory replenishment and a rebound

Chart 1.22
Current Account



p Preliminary

Source: Department of Statistics, Malaysia

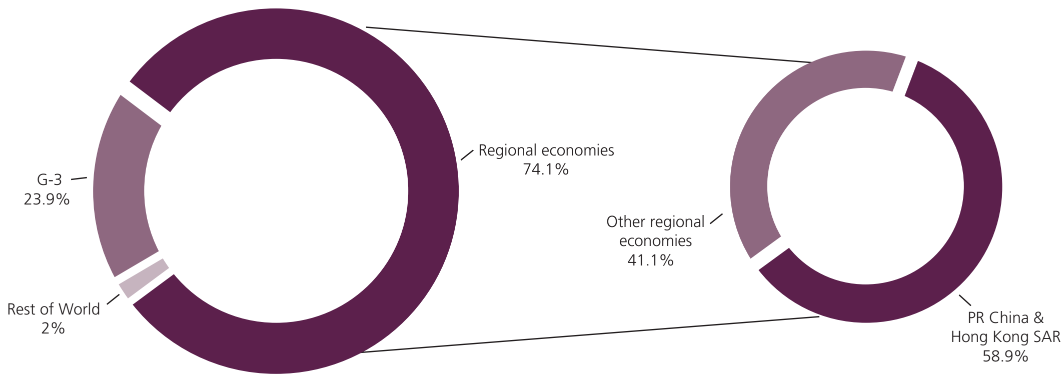
Table 1.13
Gross Exports

	2008	2009*p*
	Annual change (%)	
Gross exports	**9.8**	**-16.6**
Manufactures	**3.8**	**-12.5**
of which:		
Electronics	*-8.3*	*-8.6*
Semiconductors	*-7.1*	*3.5*
Electronic equipment and parts	*-9.3*	*-18.8*
Electrical products	*9.9*	*-16.6*
Resource-based products[1]	*20.9*	*-17.4*
Commodities	**36.0**	**-27.6**
Agriculture	**29.7**	**-21.6**
of which:		
Palm oil	*43.5*	*-20.9*
Rubber	*10.6*	*-45.0*
Minerals	**41.4**	**-32.2**
of which:		
Crude oil and condensates	*33.0*	*-42.0*
LNG	*51.2*	*-23.4*

[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

Chart 1.23
Direction of Semiconductor Exports in 2009



Note: G-3 refers to the US, Japan and Euro Area

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

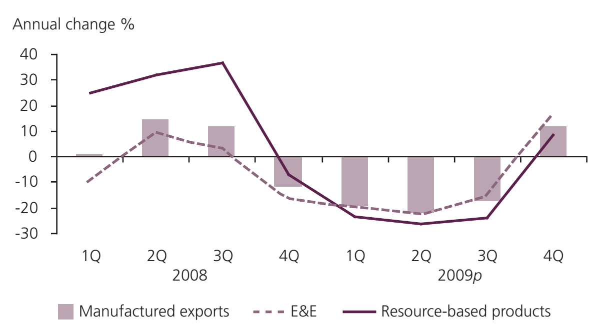
in commodity prices lent further support to export recovery. All segments of exports, except for exports of minerals, registered positive growth in the fourth quarter.

Manufactured exports contracted by 12.5% in 2009, with all major segments recording negative growth. Exports of **E&E** declined by 11%, largely reflecting the sharp contraction in exports in the first half year, following the decline in demand from both advanced and regional countries. Exports recovered in the second half, amid improvements in the global economic conditions, led by stronger growth in the regional economies. The impetus for the recovery was driven by exports of electronics, particularly semiconductors. Exports of semiconductors constituted half of electronic exports, with regional markets accounting for 74% of semiconductor exports. Of significance, PR China and Hong Kong SAR emerged as the largest export destinations for semiconductors with a share of 44%, with the demand coming primarily from the production of netbooks and smart phones. This development was underpinned by the pivotal role played by PR China in the regional production network. Consequently, Malaysia benefited from PR China's demand for parts and components, both for re-exports to advanced economies and increasingly, for its domestic demand. Demand for electronic equipment and parts by advanced countries, however, remained subdued due to lower spending on information technology by corporations.

Exports of **non-E&E** declined by 14.4% in 2009, with the decline being more pronounced in the first half of the year. The sharp fall in commodity prices contributed to a substantial drop in resource-based exports, which accounted for 57.4% of non-E&E exports. These included rubber products, chemicals and chemicals products, and petroleum products. However, the improvement in regional demand and the rebound in commodity prices in the second half led to the recovery in non-E&E exports, which recorded a positive growth in the fourth quarter.

Commodity exports contracted by 27.6%, attributed to weaker demand and lower prices. Both agriculture and mineral exports declined

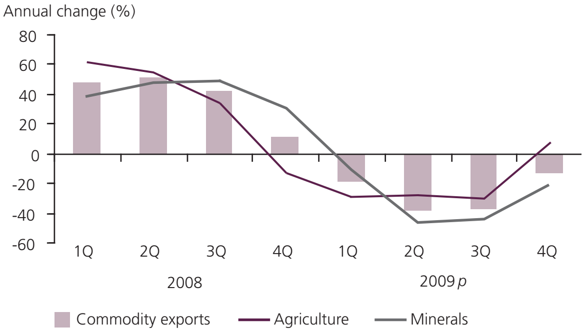
Chart 1.24
Export Performance of Electronics & Electrical (E&E) and Resource-Based Industries



p Preliminary

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

Chart 1.25
Commodity Export Performance



p Preliminary

Source: Department of Statistics Malaysia and Bank Negara Malaysia

significantly in the first half, where rubber, crude petroleum and LNG experienced lower prices and export volumes. Meanwhile, the higher export volume of crude palm oil was unable to cushion the fall in prices. The contraction in export receipts eased in the second half on the back of improved commodity prices and some recovery in volume demand, particularly from the region, following the improvement in the economic conditions.

Gross imports declined by 16.6% (2008: +3.8%), with contractions in all major categories of imports. Imports of **intermediate** goods declined by 21.6%. In the first half year, the weak external demand for E&E exports led to the curtailment of intermediate imports, particularly imports of parts and accessories for capital goods. In tandem with the decline in non-E&E exports, imports of fuels and lubricants, as well as industrial supplies such as chemicals and metals were also lower. In the second half, consonant with improvements in exports, imports for intermediate goods recovered and recorded positive growth in the fourth quarter.

Imports of **capital** goods contracted by 5.9%, reflecting lower domestic private investment spending. In the first half year, imports of agricultural, construction, mining and manufacturing equipment contracted significantly, following deterioration in domestic demand conditions and business confidence. Weak external demand and lower capacity utilisation had affected capacity expansion particularly in the manufacturing sector. However, imports of telecommunication equipment remained strong, reflecting investment for wireless networks, following the accelerated migration to mobile services as well as the expansion in the coverage of broadband services. In the second half year, the contraction in capital imports moderated, with imports of office machines recording positive growth in tandem with capacity expansion.

Table 1.14
Imports by End-Use

	2008	2009*p*
	Annual change (%)	
Capital goods	**...**	**-5.9**
Capital goods (except transport equipment)	2.2	-8.2
Transport equipment	-13.6	10.5
Intermediate goods	**5.7**	**-21.6**
Food and beverages, mainly for industry	30.0	-16.8
Industrial supplies, n.e.s.	9.7	-21.8
Fuel and lubricants	32.0	-36.0
Parts and accessories of capital goods (except transport equipment)	-5.0	-19.0
Consumption goods	**11.8**	**-2.7**
Food and beverages, mainly for household consumption	21.4	7.8
Consumer goods, n.e.s.	5.5	-9.1
Re-exports	**-6.5**	**24.0**
Gross Imports	**3.8**	**-16.6**

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

Source: Department of Statistics, Malaysia

Consumption imports also declined, albeit, at a more moderate rate of 2.7% as consumers were more cautious in their spending on imported consumer durables and semi-durables. Nevertheless, imports of food and beverages for household consumption continued to increase. Growth in consumption imports resumed in the fourth quarter in tandem with the strengthening of private consumption.

With the earlier and stronger rebound in economic activity in the Asian economies, exports to the region began to recover as early as the third quarter and strengthened further in the fourth quarter. The greater role by Asia in supporting the recovery in global trade resulted in a shift in Malaysia's trade pattern. The share of exports to the region increased to 49.3% (2008: 45.7%), with the share to PR China increasing to 12.2% (2008: 9.5%). The share of exports to advanced economies including the US, EU and Japan, declined to 31.6% in 2009 (2008: 34.6%).

In 2009, the **services account** recorded the third consecutive year of surplus, the largest recorded surplus of RM3.2 billion (0.5% of GNI). The surplus stemmed from higher travel receipts, as well as an improvement in the other services deficit.

Despite the economic downturn and outbreak of influenza A (H1N1), tourist arrivals expanded strongly by 7.2% to 23.6 million visitors (2008: 5.1%, 22.1 million visitors), where most of the tourists were from Asia. Malaysia benefited from the increase in tourist arrivals spurred by the growing number of middle income travelers from Asia. In addition, the expansion of short and medium-haul leisure travel was further facilitated by the low cost carriers.

The other services account recorded a lower deficit of RM10.7 billion, as a result of mainly lower net outflows for construction services, as well as royalties and licence fees. In addition, net inflows from computer and IT services also improved, attributable to the higher shared services outsourcing (SSO) activities by foreign financial institutions and IT companies in Malaysia. Regional economies emerged as one of the major markets for Malaysia's export of software and IT support services, earnings of which accounted for about 40% of total receipts. Growth was further supported by regional IT centres for the oil and gas industry. Net payments for professional services, however, increased reflecting imported consultancy services by the financial and manufacturing sectors.

Table 1.15
Direction of External Trade

	2009*p*				
	Exports		Imports		Trade balance
	RM billion	Annual change (%)	RM billion	Annual change (%)	RM billion
Total	**553.3**	**-16.6**	**434.9**	**-16.6**	**118.4**
of which:					
United States	**60.6**	**-26.8**	**48.6**	**-13.9**	**11.9**
European Union (EU)	**60.0**	**-19.9**	**50.8**	**-17.7**	**9.2**
Selected ASEAN countries[1]	**141.0**	**-16.8**	**109.0**	**-13.4**	**32.1**
Selected North East Asia countries	**131.6**	**-1.5**	**110.1**	**-15.2**	**21.6**
The People's Republic of China	*67.2*	*6.4*	*60.7*	*-9.3*	*6.6*
Hong Kong SAR	*28.8*	*1.9*	*10.8*	*-20.8*	*18.0*
Chinese Taipei	*14.4*	*-11.1*	*18.5*	*-26.4*	*-4.0*
Korea	*21.1*	*-18.5*	*20.1*	*-16.9*	*1.0*
West Asia	**21.4**	**-18.0**	**14.8**	**-41.0**	**6.6**
Japan	**54.4**	**-24.2**	**54.3**	**-16.6**	**0.1**
India	**17.0**	**-31.3**	**7.9**	**-23.6**	**9.1**

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

Table 1.16
Services and Income Accounts

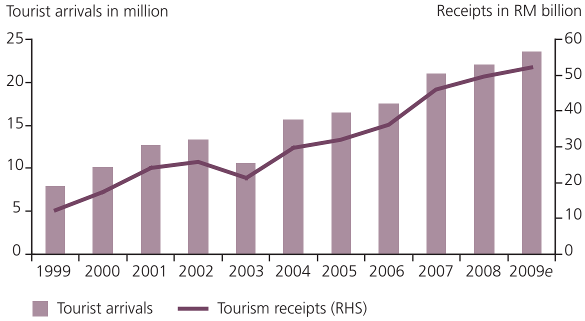
	2008	2009*p*		
	RM billion			
	Net	+	-	Net
Services Account	**0.2**	**99.1**	**95.9**	**3.2**
% of GNI	*...*			*0.5*
Transportation	-15.4	14.9	32.0	-17.1
Travel	28.5	54.2	22.6	31.6
Other services	-12.4	29.8	40.5	-10.7
Government transactions n.i.e.	-0.6	0.1	0.7	-0.6
Income Account	**-23.7**	**40.5**	**53.1**	**-12.6**
% of GNI	*-3.3*			*-1.9*
Compensation of employees	-0.7	4.0	5.4	-1.4
Investment income	-23.0	36.5	47.7	-11.2

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

For the year, the transportation account recorded a larger deficit of RM 17.1 billion as lower earnings from passenger fares and cargo offset the lower freight payments due to the declining volume of trade. The global economic downturn inevitably led to lower passenger traffic against the backdrop of excess capacity and greater competition within the travel industry. The decline in earnings from passenger fares moderated in the second half year following the upturn in regional travel demand amidst reductions in capacity.

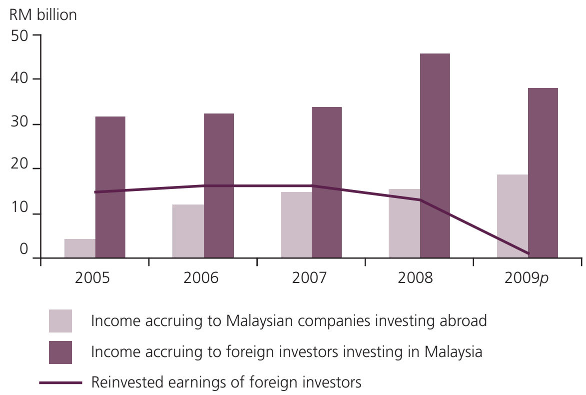
The **income account** deficit narrowed to RM12.6 billion or 1.9% of GNI, reflecting mainly lower

Chart 1.26
Tourist Arrivals and Tourism Receipts



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

Chart 1.27
Direct Investment Income



p Preliminary
Source: Department of Statistics, Malaysia

profits and dividends accruing to foreign direct investors in Malaysia, particularly in the E&E sector. This was due to the weak performance of manufacturing sector in the first half of the year. Meanwhile, profits and dividends accruing to Malaysian companies investing abroad were higher, reflecting the improvement in earnings from commodities.

Financial Account

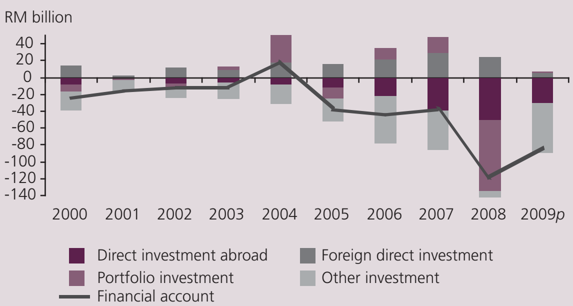
In 2009, the **financial account** recorded a lower net outflow of RM82.9 billion (2008: -RM118.5 billion). Of significance, net portfolio outflows moderated sharply in 2009 as the large reversal of short-term capital flows experienced since the second half of 2008 turned to net inflows in the second half of 2009, following improved global and domestic economic conditions. Meanwhile, both foreign direct investment and direct investment abroad by Malaysian companies moderated, particularly in the first half of 2009, due to the sharp deterioration in global economic conditions. Outflows in the other investment category were higher as a result of the continued extension of trade credits by Malaysian exporters and the placement of deposits abroad by residents.

For the year as a whole, **portfolio investment** recorded a small net inflow of RM0.8 billion. In the first half, portfolio outflows moderated to RM22.1 billion (2H 2008: -RM88.5 billion) as deleveraging by international investors subsided. Subsequently, this outflow turned around to register a net inflow of RM22.9 billion in the second half of the year,

Nature and Trends of Capital Flows in Malaysia

Malaysia is one of the most open economies in the world. Throughout its development, Malaysia has been highly integrated with the global economy and international financial system, resulting in not only significant trade expansion, but also large investment flows. For more than a century, Malaysia has received foreign direct investment, which has been an important contributor to the country's economic development. As the Malaysian economy evolves to become more developed, the nature of the capital flows has changed responding to the changing conditions prevailing in the country. Two distinct developments have emerged in the recent years. First, short-term capital flows have become more prominent in the Malaysian financial system, in tandem with the global surge in this form of capital flows. Short-term flows, in particular, portfolio flows, have risen in volume and their volatility has been increasing, with potentially destabilising effects on exchange rates, the financial markets and the real economy. Second, a more recent development has been the large increase in investment abroad by Malaysian companies in search of new growth opportunities and markets.

Chart 1
Trends of Net Capital Flows in Malaysia



p Preliminary

Source: Department of Statistics, Malaysia

Chart 2
Net FDI Flows

p Preliminary

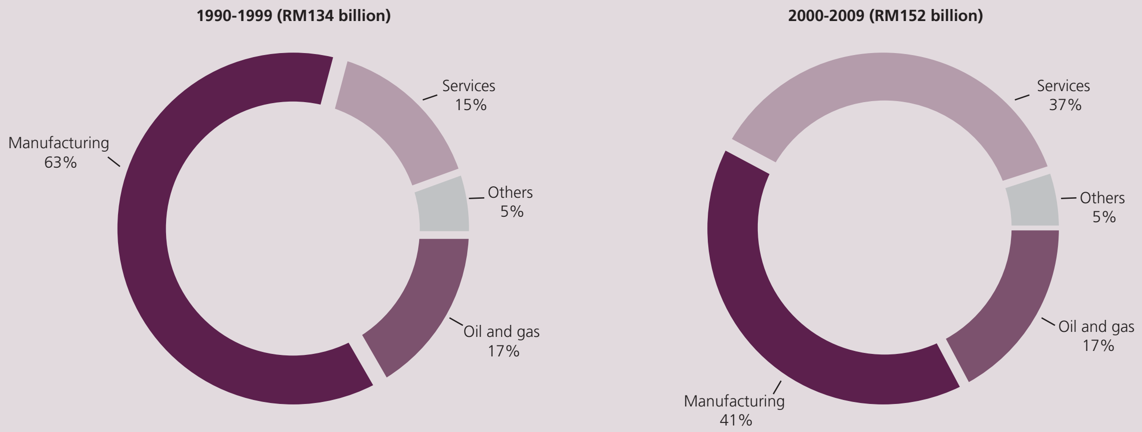
Source: Department of Statistics Malaysia

Foreign Direct Investment

Foreign direct investment (FDI) is an important contributor to the growth and the transformation of the Malaysian economy, particularly in establishing new industries, enhancing production capacity, employment, trade and technological capability. Malaysia has attracted a steady inflow of net FDI in the recent decade, averaging 3% of GDP per annum with a peak of 4.5% of GDP in 2007. However, relatively lower FDI inflows were recorded in 2001 and 2009, similar to the global trend, following the collapse of the technology bubble and the global financial crisis respectively.

In absolute volume, Malaysia recorded RM152 billion in net FDI inflows during the period of 2000-2009, higher than the RM134 billion received during the period of 1990-1999. However, as a share of GDP, the net inflows of FDI were lower during the period of 2000-2009 (3% of GDP) compared to the period of 1990-1999 (6.3% of GDP). This moderation was mainly attributed to two reasons. Firstly, the FDI inflows into Malaysia in this recent decade have increasingly been channelled into the higher value-added services sector, namely the financial services and shared services operations. The scale of the investments in these sub-sectors are less and are also less capital-intensive compared to the manufacturing sector, thus involving lower amounts. More importantly, however, is the value-add and contribution to growth of this lower amount of FDI is higher as these sub-sectors are more skill-intensive and have higher labour productivity. Secondly, the rising competition for FDI in the region from new emerging market economies such as PR China, India and Vietnam as well as established investment centres, namely Singapore and Hong Kong SAR. While global net FDI flows into the region have more than doubled during the period

Chart 3
Cumulative Net FDI Flows by Sector



Note: Others mainly consist of the agriculture and construction sectors

Source: Department of Statistics, Malaysia

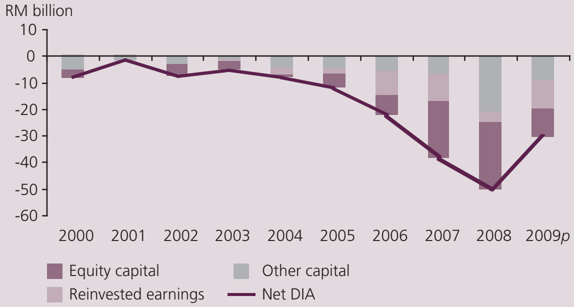
of 2000-2009 (USD1.4 trillion; 1990-1999: USD0.6 trillion), Malaysia's share of the regional FDI flows has declined as a major part of these flows went to PR China.

In terms of the sectoral distribution, inflows of FDI into Malaysia are relatively broad-based. While FDI inflows continue to be underpinned by the large and long-standing presence of MNCs in the manufacturing sector and investments in the oil and gas sector, the period 2000-2009 saw the rising importance of FDI into the services sector, with the share of FDI in this sector more than doubling to 37% of the total FDI flows (1990-1999: 15%). FDI in the services sector is well diversified, with investment being channelled to the financial services, shared services and outsourcing, communications, transportation, hotels and wholesale and retail trade sub-sectors. A significant development is the sizable increase in FDI in the financial sector, including Islamic finance. It is estimated that net FDI inflows into this sector amounted to RM41.6 billion over the recent 10-year period following the liberalisation that has been undertaken in this sector. In the oil and gas sector, investment in upstream activity continued to be significant as PETRONAS and its foreign partners continued to be actively engaged in exploration, production and the development of oil and natural gas resources in the country. Additionally, the manufacturing sector in Malaysia continues to be successful in attracting FDI in new growth areas such as renewable energy and medical equipment.

Direct Investment Abroad

An important development in recent years has been the sharp increase in direct investment abroad (DIA) by Malaysian companies, averaging 3.5% of GDP per annum between 2000 and 2009, and peaking at 6.8% of GDP in 2008. Cumulatively, net DIA amounted to RM182 billion over this period, with 78% occurring between 2006 and 2009. The increasing trend of DIA reflects the growing presence of Malaysian companies abroad, especially in the Asian region. Similar to other global companies, the factors driving Malaysian companies to invest abroad include expanding markets for their products, gaining access to more competitive supply of land and labour, expanding into rapidly growing industries, acquiring brands and technology, and taking advantage of the comparative advantage of host countries. In particular, given the relatively small domestic market, regional and global expansions allow Malaysian companies to achieve greater economies of scale by tapping into new and larger markets. Generally, Malaysian companies which invested abroad have also enhanced their domestic operations by expanding capacity and moving up

Chart 4
Net DIA Flows



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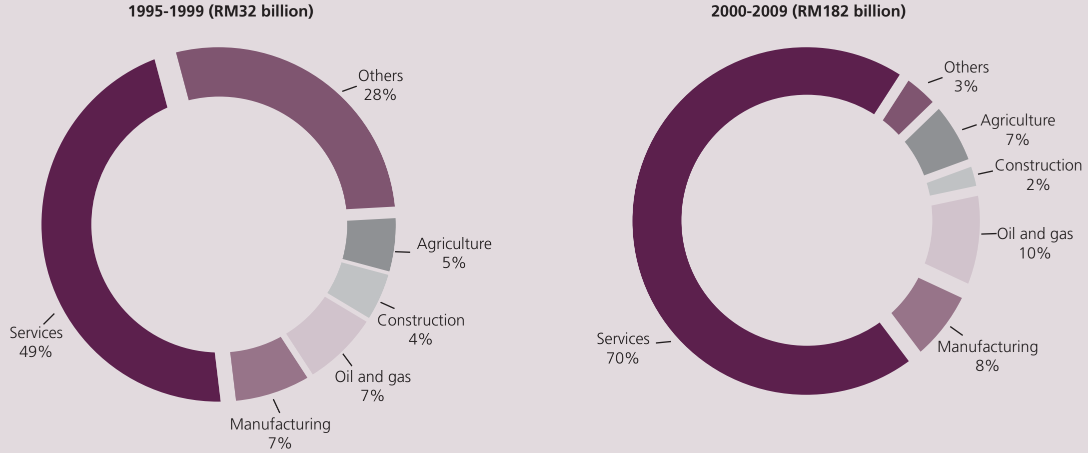
Source: Department of Statistics, Malaysia

the production value chain in order to establish an integrated supply chain management with their overseas subsidiaries. This has increased their overall efficiency and enabled them to better compete in the global market. Therefore, the rising investment abroad by Malaysian companies, over a medium term, will benefit the country through having more competitive and globalised Malaysian companies, through greater job opportunities for Malaysians, higher dividends for shareholders, and higher inflows from profit repatriation.

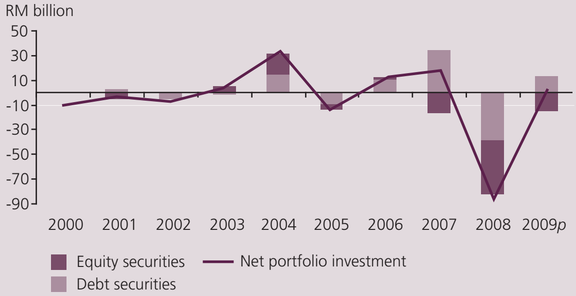
The scope of DIA by Malaysian companies has also broadened over the years. In the earlier years, investments were undertaken mainly by PETRONAS and Government-linked plantation companies, to explore the potential for further natural resources such as oil and gas as well as to increase the available land for plantation activity. This has, however, changed in recent years, with investments, mainly in the services sector, being undertaken by both the Government-linked companies and private companies, particularly in the financial services, telecommunication, utilities and business services sub-sectors. Most of the investments were undertaken in the region, particularly in ASEAN, the Asian Newly Industrialised Economies (NIEs), PR China and West Asian economies.

Chart 5
Cumulative Net DIA Flows by Sector



Source: Department of Statistics, Malaysia

Chart 6
Net Portfolio Flows



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Source: Department of Statistics Malaysia

Portfolio Investment Flows

A key development since the early nineties has been the surge in portfolio flows to Malaysia. At its peak in 2008, total gross portfolio inflows and outflows in absolute terms were 23 times higher than in 2000. In addition, a distinct characteristic of the portfolio flows in recent years has been the increased volatility of the flows. Since 2004, there have been several episodes of large inflows and outflows of portfolio funds in response to the developments in global financial markets as well as changes in domestic economic conditions. Of significance, between 2004 and the first half of 2008, Malaysia experienced net portfolio inflows of RM54 billion. These inflows were mainly driven by Malaysia's strong economic fundamentals as well as the prospects of better corporate outlook as the economy recovered strongly following the aftermath of the Asian financial crisis. In addition, the rapid development of the domestic bond market has also attracted sizeable inflows of foreign portfolio investment into the debt securities market. The emergence of debt securities as an asset class for foreign investors alongside the equities has resulted in an increasingly diversified composition of portfolio investment flows in Malaysia.

The build-up of inflows of speculative funds in 2005 was due to the expectations for the appreciation of the ringgit which was floated on 21 July 2005. The surge of portfolio inflows since 2005 was interrupted by several external market developments which led to episodes of reversals in flows by foreign investors. Among others, the deteriorating global inflation outlook in 2006, the Shanghai stock market correction in February 2007 and the heightened global market uncertainty following the US sub-prime mortgage problem in July-August 2007 had subsequently led to outflows of foreign funds. Of significance was the massive deleveraging activities by foreign financial institutions following the global financial crisis in the second half of 2008 that triggered large-scale liquidation of portfolio funds by international investors, which affected emerging markets across the board including Malaysia. These reversals culminated in a net portfolio outflow of RM111 billion between the second half of 2008 and the first half of 2009. Nevertheless, inflows of foreign portfolio funds resumed in the second half of 2009 amid stronger growth prospects in the region as well as further normalisation of conditions in the international financial markets. This subsequently led to an improvement in investors' risk appetite for financial assets in the emerging markets, including Malaysia.

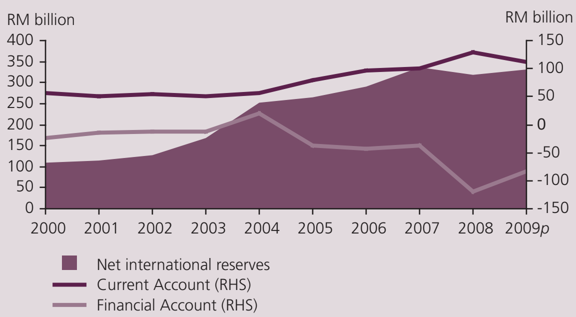
While the magnitude of the recent reversals were larger than the net outflows recorded during the height of the Asian financial crisis, the impact on the domestic economy was limited given Malaysia's well-developed financial system. In particular, the development of the debt market allowed for the diversification of the composition of portfolio flows into Malaysia. As such, the reversals of the flows did not cause a significant disruption in any particular asset market. In addition, the depth of the domestic financial market also provided greater liquidity and price sensitivity to changes in financial conditions, facilitating more effective monetary operations to sterilise the impact of large capital flows. The strong international reserves position has been able to accommodate these outflows of funds without affecting overall domestic liquidity or interrupting the normal functioning of the foreign exchange and domestic money markets. Given these conditions, Malaysia has not only been able to withstand large shifts in funds but has also managed to ride out the recent period of turbulence in international financial markets without serious disruptions to the domestic economy.

Meanwhile, portfolio outflows due to residents investing abroad have been steadily growing over the years, averaging about 3.9% of GDP during the period of 2000-2009 and were mainly in the form of equity securities. The liberalisation of the foreign exchange administration rules since 2005 has also allowed for greater flexibility for residents to invest abroad. The increase in external portfolio assets resemblance similar trends in other parts of the region, especially among the Asian NIEs in which the build-up in external portfolio assets at the international level has become increasingly significant.

Other Investment

In addition to portfolio investment, other investment comprising mainly net external loans undertaken by the official and private sectors, net placements of deposits by the banking institutions as well as trade credit extension, have consistently recorded net outflows, averaging 5.6% of GDP over the recent ten years. The net external loan repayments by both the official and private sectors have contributed to these outflows. Another component of other investment includes activities by the banking institutions in managing their liquidity. This reflected mainly placement of deposits abroad and inter-bank borrowings. These flows in the banking sector have in part been responsive to interest rate and liquidity movements. The non-bank private sector experienced an outflow during this period, due mainly to extension of trade credits by Malaysian exporters and repayments of trade credits by Malaysian importers. These flows have been fairly volatile and large, and they were mainly driven by financing requirements and business decisions of the non-bank private sector.

Chart 7
Movement of International Reserves



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Source: Department of Statistics Malaysia

International Reserves

The changes in net international reserves over this recent decade have been shaped by developments in both the current and financial accounts of the balance of payments, particularly movements in portfolio investments. With current account surplus exceeding financial account deficits, there was a build-up of external reserves from 2001-2003. The large inflows of portfolio funds from 2004 up to the first half of 2005 coupled with the continued surplus in the current account resulted in a significant increase of international reserves from RM168 billion (USD44.2 billion) as at end-2003 to RM297.1 billion (USD78.2 billion) as at end-July 2005. While a significant amount of these inflows were attracted to the investment opportunities provided by the deepening Malaysian capital market, there were also significant speculative portfolio inflows over this period in anticipation of the ringgit exchange rate realignment. These speculative inflows reversed in the second half of 2005 after the ringgit was floated in July 2005 and reserves stabilised at RM265.2 billion (USD70.2 billion) as at end-2005.

In 2007 and the first half of 2008, Malaysia again received substantial capital inflows, particularly portfolio funds. These large capital inflows coupled with the current account surplus, resulted in a significant appreciation of the exchange rate and an increase in the international reserves which peaked in June 2008 at RM410.9 billion (USD125.8 billion). The significant deleveraging activities following the intensification of the global financial crisis led to a large reversal of portfolio flows of RM111 billion between the second half of 2008 to the first half of 2009, resulting in a substantial decline in the international reserves to RM322.9 billion (USD91.5 billion) as at end-June 2009. The decline in reserves during this period is less than the net portfolio outflow as Malaysia continued to record a current account surplus during this period. The portfolio inflows resumed since the second half of 2009. The external reserves as at end-2009 amounted to RM331.3 billion (USD96.7 billion). This reserves position was sufficient to finance 9.7 months of retained imports and is 4.3 times of the short-term external debt. As at 25 February 2010, the net international reserves was amounted at RM331.8 billion (USD96.8 billion).

Conclusion

This review of developments in capital flows in Malaysia over the recent ten years has brought to the forefront several important policy considerations for Malaysia moving forward. First, investments abroad by Malaysian companies can be expected to continue to remain sizeable in the future and this development is in response to the changing structure and competition in the region and in the global economy. The changing composition of capital flows would contribute to Malaysia’s long-term competitiveness, economic transformation and growth. Second, competition for FDI will continue to intensify, going forward. Malaysia has shifted gear to attract FDIs in the high value-added activities and those that will bring in new technology, required to support Malaysia’s transition into a high income economy.

The third, is the challenge with respect to managing the increasingly volatile nature of short-term capital flows. The strategy adopted is to further deepen and broaden the domestic financial system to cope with and manage the volatile capital flows without resulting in disruptions and instability in the domestic financial markets. Malaysia has also consistently maintained vigilance over developments in capital flows through close surveillance and assessments of the risks associated with these flows. Maintaining Malaysia’s strong macroeconomic fundamentals and a sound and strong banking system will provide the flexibility for the country to intermediate volatile capital flows while maintaining financial stability and promoting growth in the domestic economy.

Table 1.17
Balance of Payments: Financial Account

	2008	2009*p*
	RM billion	
Financial Account	**-118.5**	**-82.9**
Direct Investment	**-26.1**	**-24.9**
Abroad	-50.2	-30.5
In Malaysia	24.1	5.7
Portfolio Investment	**-84.4**	**0.8**
Other Investment	**-8.1**	**-58.9**
Official sector[1]	0.8	4.1
Federal Government	*-0.5*	*-0.6*
NFPEs	*1.3*	*-1.9*
Bank Negara Malaysia	*0.0*	*6.6*
Private sector	-8.9	-63.0

[1] Excludes bonds and notes raised abroad by the Federal Government and NFPEs
p Preliminary
Note: Numbers may not necessarily add up due to rounding

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

going mainly into long-term debt securities. The inflows took place following further normalisation in the international financial markets and stronger growth prospects in Asia, which led to the improvement in investors' risk appetite.

The financial account recorded a lower net outflow following the return of portfolio funds in the second half of the year

Gross inflows of **foreign direct investment** (FDI) moderated to RM31.6 billion (or 4.8% of GNI) in 2009. This largely reflected the significantly lower amount of earnings retained for investments by existing multinational corporations (MNCs) due to lower profits during the year. In addition, a significant share of the profits was also repatriated to home countries. Rising excess capacity amid the falling export demand and uncertainty in the global economic outlook further discouraged inflows of FDI during the year. After taking into account the adjustments for outflows due largely to loan repayments to parent companies, net inflows of FDI amounted to RM5.7 billion or 0.9% of GNI.

The FDI continued to be broad-based, with inflows mainly into the manufacturing (47% share), services (28%) and oil and gas (25%) sectors. In the manufacturing sector, the bulk of FDI was in the E&E sub-sector, largely undertaken by MNCs for the upgrading of equipment and technology. There were also sizeable investments in the petroleum refining and petroleum-related industry, as well as in the solar energy industry. FDI in the services sector was channelled primarily into the finance and insurance, as well as wholesale and retail trade sub-sectors. Investment in the oil and gas sector reflected on-going extraction operations and production activities undertaken by MNCs jointly with PETRONAS.

Direct investment abroad (DIA) by Malaysian companies was also affected by global developments. However, DIA continued to remain sizeable. For the year as a whole, net DIA amounted to RM30.5 billion and was mainly channelled into the services (46%), oil and gas (38%), and manufacturing sectors (6%). Although investments in terms of equity and inter-company loans were lower, reinvested earnings more than doubled in 2009. This largely reflected the continued investment by Malaysian companies in their existing operations.

In the services sector, DIA was mainly undertaken through increased participation in existing operations abroad, particularly in the Asian region. Of significance, the domestic banking and telecommunication players have strategised to realign their operations on a regional scale to remain competitive. The investment in the oil and gas sector mainly reflected the continued expansion into global markets by PETRONAS to improve returns and to diversify geographical risks. During the year, PETRONAS invested in a gas processing plant in Turkmenistan, an LNG project in Australia and other existing projects in Asia, Africa and Central Asia. Meanwhile, investments in the manufacturing sector were primarily in the form of reinvestments into upstream and downstream activities related to palm oil.

The **other investment** account recorded a higher net outflow as outflows in the private sector more than offset inflows in the official sector. The private sector outflows reflected the net placement of deposits abroad by residents and the extension of trade credits by Malaysian exporters. During the year, trade credits extended by Malaysian exporters were higher than the trade credits received by Malaysian importers, as foreign exporters experienced constraints in trade financing as a result of the global financial crisis. Meanwhile, the net inflows of the official sector were due mainly to the special allocation of IMF's Special Drawing Rights (SDR) to Bank Negara Malaysia, which was partially offset by external loan repayments by the Federal Government and the Non-Financial Public Enterprises (NFPEs).

International Reserves

The international reserves held by Bank Negara Malaysia comprise the holdings of gold and foreign exchange holdings, the reserve position with the IMF and the holdings of Special Drawing Rights (SDR). In 2009, net international reserves increased by RM13.8 billion to RM331.3 billion (equivalent to USD96.7 billion) as at 31 December 2009.

International reserves increased by RM13.8 billion to RM331.3 billion in 2009, supported mainly by the continued surplus in the current account

For the year as whole, the increase in international reserves was largely supported by the continued surplus in the current account. Foreign exchange inflows arising from export proceeds and FDI were more than able to cover the external obligations arising from external loans and imports as well as net outflows arising from both DIA and portfolio investments. The movements of the international reserves during the year were to a large extent influenced by developments in portfolio flows. In the first half of the year, the moderation of deleveraging activities by international investors led to small gains in the net international reserves as portfolio outflows subsided. Net international reserves position subsequently increased moderately in the second half with the revival of investor sentiments and the return of net foreign portfolio inflows. Meanwhile, the cumulative foreign exchange revaluation gain amounted to RM10.7 billion, reflecting the strengthening of major currencies against the ringgit, particularly in the first three quarters of 2009.

Malaysia is 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 2009 reflected mainly net purchases of currencies by various member countries under the Financial Transactions Plan. Meanwhile, the significant increase in international reserves held in the form of SDRs was attributed mainly to an additional allocation of **SDRs** to Malaysia by the IMF in a move to strengthen the financial safety net available to member countries during the financial crisis in 2009.

For the first few months of 2009, the global financial markets remained in turmoil. Central banks and governments implemented large scale and unprecedented measures to arrest the crisis. The functioning of global financial system was impaired by the failure of some financial markets. Market volatility was large, and at times were extreme. Credit markets were frozen while large

Table 1.18
Net International Reserves

	As at end		Change
	2008	2009	2009
	RM million		
SDR holdings	786.4	7,279.2	6,492.8
IMF reserve position	1,127.1	1,515.8	388.7
Gold and foreign exchange[1]	315,554.2	322,505.6	6,951.4
Gross International Reserves	**317,467.7**	**331,300.6**	**13,832.9**
Less Bank Negara Malaysia external liabilities	22.5	23.9	1.4
Net International Reserves	**317,445.3**	**331,276.7**	**13,831.4**
USD million equivalent	**91,529.5**	**96,688.1**	**5,158.6**
Months of retained imports	7.6	9.7	
Reserves/Short-term external debt[2] (times)	4.0	4.3	

[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

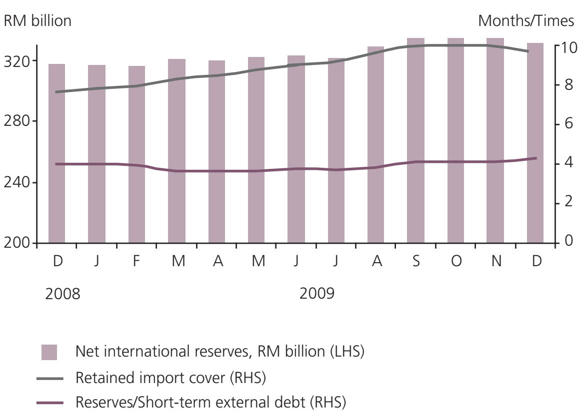
Note : Numbers may not necessarily add up due to rounding

Source: Bank Negara Malaysia

financial institutions in distress were rescued by governments. At the end of the first quarter, governments in major advanced economies had announced a wide range of unprecedented fiscal and monetary measures to stabilise the financial system. Aggressive monetary accommodation brought down policy rates to historical lows and unconventional quantitative measures were introduced to ease liquidity and restart financial intermediation. Subsequently, the volatility subsided and financial conditions stabilised. This was then followed by a strong recovery of the equity market. For the remaining part of the year, major equity and commodity markets rebounded, benefiting from the abundance of liquidity while credit spreads tightened considerably. Investment flows returned to riskier assets and emerging markets were the best performing asset class for the year.

During the course of the year, the reserves management strategy shifted towards anticipating the financial and economic recovery. Investment duration and asset allocation were managed in anticipation of an expected rise in bond yields due to the record debt supply as well as rising long-term inflationary risk from the unprecedented fiscal and monetary expansions. Diversification into other currencies and asset markets resumed, capitalizing on improving financial market conditions, which led to a strengthening of non-US dollar currencies and credit markets in general. Throughout the crisis and the ensuing recovery, risk management practices remained robust and were continually reviewed, particularly in managing elevated operational and credit risks.

Chart 1.28
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

As at 25 February 2010, the reserves level amounted to RM331.8 billion (equivalent to USD 96.8 billion), which is adequate to finance 10 months of retained imports and is 4.3 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 ringgit related options activity in the foreign currency markets.

External Debt

Malaysia continues to undertake a prudent yet pragmatic external debt management strategy which facilitates diversification of external borrowings by the private and public sectors while instituting prudential measures to minimise risks associated with large external obligations and debt servicing ability. In promoting monetary and financial stability as well as in safeguarding the balance of payments position, the country's external debt management is supported by a comprehensive surveillance and debt monitoring system which enables early detection of emerging risks and vulnerabilities arising from the country's overall external debt exposure.

Malaysia's external debt remained low at 35.3% of GNI

As at the end of 2009, Malaysia's total external debt moderated to RM233.9 billion (or USD67.7 billion), or equivalent to 35.3% of GNI. During the year, **the medium- and long-term external debt** declined due to net repayments by both the Federal Government and the private sector, which more than offset the larger net drawdown by the NFPEs. The appreciation of the ringgit against the US dollar also contributed to the decline in the overall external debt.

The **Federal Government** debt registered a larger net repayment of RM6.3 billion in 2009, due primarily to the maturity of the Global Bond (1999). For the sixth consecutive year, no market loan was raised from the international

Table 1.19
Outstanding External Debt

	2008	2009*p*	2008	2009*p*
	RM billion	RM billion	USD billion	USD billion
Total debt	**236.1**	**233.9**	**67.4**	**67.7**
Medium- and long-term	156.5	156.0	44.6	45.1
Short-term[1]	79.6	78.0	22.7	22.6
As % of total debt	*33.7*	*33.3*	*33.7*	*33.3*
As % of net international reserves	*25.1*	*23.5*	*25.1*	*23.5*
As % of GNI				
Total debt	33.0	35.3		
Medium- and long-term debt	21.9	23.6		
As % of exports of goods and services				
Total debt	30.9	35.8		
Medium- and long-term debt	20.5	23.9		
Debt service ratio (%)	**2.6**	**6.5**		

[1] Excludes currency and deposits held by non-residents with resident banking institutions
p Preliminary

Source: Ministry of Finance, Malaysia and Bank Negara Malaysia

capital market as the Federal Government maintained its practice of sourcing its funding requirements from non-inflationary domestic sources. Meanwhile, the higher external debt of the **NFPEs** (end-2009: RM71.6 billion; end-2008: RM63.1 billion) was due mainly to the issuance of a USD4.5 billion two-tranche bond by PETRONAS in August 2009, to finance its future capital expenditures. Excluding this transaction, the NFPEs registered a net repayment of their external debt following the maturity of several large bonds as well as reduced borrowings for capital expenditure and expansion abroad.

Similarly, the **private sector** registered a net repayment of RM3.3 billion in 2009, due mainly to larger repayments of debt by companies in the manufacturing and oil and gas sectors. Meanwhile, loan drawdowns also declined as investment expansion plans slowed down.

During the year, the **short-term external debt** outstanding declined to RM78 billion as inter-bank borrowings arising from treasury operations moderated. The short-term external debt accounted for only 11.8% of GNI, 23.5% of international reserves and 11.9% of exports of goods and services. The bulk of the short-term debt continued to be held by the banking sector (88.5%). Short-term external debt of the non-bank private sector, comprising mainly of revolving credits and overdraft facilities, remained low.

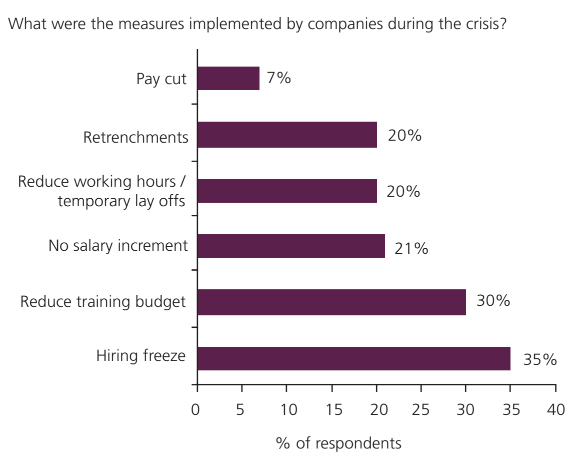
LABOUR MARKET DEVELOPMENTS

The labour market was adversely affected by the significant deterioration in the global economy in the early part of the year. In response to the sharp decline in export orders and weakening domestic demand, firms particularly in the trade-related sectors reduced operations, particularly in the first two months of the year.

Weak labour market conditions in the early part of 2009 but conditions had steadily improved

According to a survey conducted by Bank Negara Malaysia, various measures were undertaken by companies to reduce costs, of which imposing a hiring freeze and reducing the training budget were the most common. Firms also stated that retrenchment was generally implemented as a last resort, only after all other cost-cutting measures had been exhausted. For the year as a whole, total retrenchments increased to a seven-year high of 25,064 persons, with one-half of these retrenchments occurring in the first quarter.

Chart 1.29
Various Measures to Reduce Labour Costs by Companies



Source: Annual Survey, Bank Negara Malaysia

Table 1.20
Selected Labour Market Indicators

	2005	2006	2007	2008	2009e
Employment[1] ('000 persons)	10,892.8	11,159.0	11,398.0	11,576.5	11,609.1
Annual change (%)	4.1	2.4	2.1	1.6	0.3
Labour force[1] ('000 persons)	11,290.5	11,544.5	11,775.1	11,967.5	12,061.1
Annual change (%)	4.1	2.2	2.0	1.6	0.8
Retrenchments (persons)	16,109	15,360	14,035	16,469	25,064
Annual change (%)	-19.3	-4.6	-8.6	17.3	52.2
Unemployment rate[1] (% of labour force)	3.5	3.3	3.2	3.3	3.7
Real labour productivity growth[2] (%)	1.2	3.3	4.0	3.0	-2.0

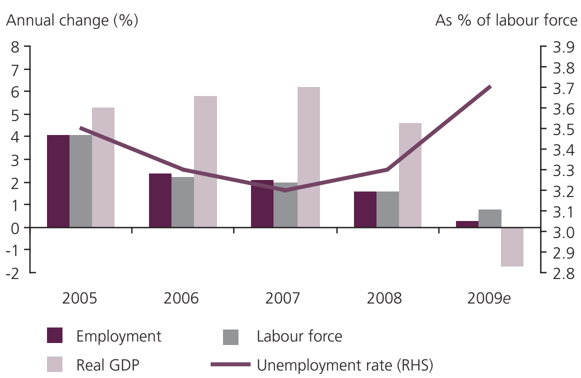
[1] Based on estimates by Economic Planning Unit
[2] Based on estimates by Bank Negara Malaysia
e Estimate

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

Labour market conditions began to stabilise in the second quarter and improved thereafter, in tandem with the overall improvement in global and domestic economic conditions. The implementation of expansionary fiscal policy and accommodative monetary policy domestically had contributed to a rebound in business and consumer sentiments, and together with a gradual improvement in the global economic conditions, led to a significant decline in retrenchments and a revival in hiring activity by firms from the second quarter onwards. The quicker-than-expected improvements in labour market conditions in turn resulted in a lower unemployment rate of 3.7% of the labour force, compared to the earlier forecast of 4.5%. Despite the challenging economic environment and declining productivity growth, employers in the private sector continued to grant salary increments, although the quantum moderated to 3.4% (2008: 5.1%).

Total **retrenchments** in 2009 were significantly higher than in the previous year, with the highest number of retrenched workers being recorded in the first quarter of the year (12,590 persons). Workers in the manufacturing sector were the worst affected (78% of total retrenchments in the first quarter), particularly in the E&E cluster (45% of total retrenchments) following the sharp drop in export orders. The number of retrenched workers,

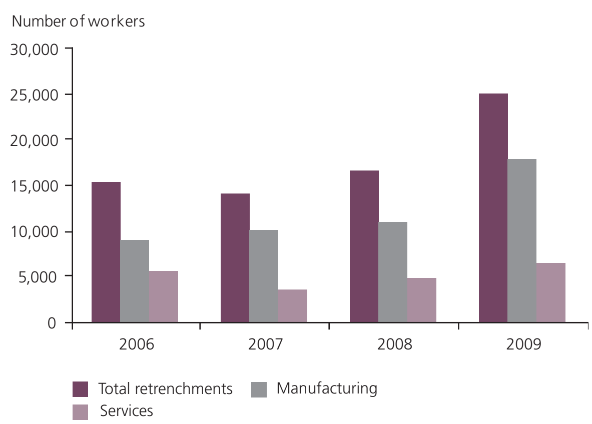
Chart 1.30
Output and Employment



e Estimate

Source: Economic Planning Unit
Department of Statistics, Malaysia

Chart 1.31
Retrenchment in Selected Sectors



Source: Ministry of Human Resources

however, declined significantly from the second quarter onwards (7,470 persons) and by the third quarter, normalised to pre-crisis level. Overall, total retrenchments increased by 52% to 25,064 persons in 2009 (2008: 16,469 persons), of which 71% were from the manufacturing sector and 25% were from the services sector.

Recruitment activity also ceased in the first quarter amidst heightened uncertainty about the business outlook. Total **vacancies** posted during the first quarter amounted to about 222,000 positions, a decline of 16% from the preceding period. However, business sentiments began to improve subsequently, which translated into higher job offerings in the second half of the year, particularly in the services, manufacturing and construction sectors. For the year as a whole, the cumulative number of vacancies rose to 1.5 million positions (2008: 1.1 million positions), with most positions being offered in the manufacturing and services sectors, particularly in the distributive trade, financial intermediation, and community, social and personal services sub-sectors.

The improving economic conditions in the second half of the year and the various measures undertaken by the Government helped to support overall **employment** conditions, which recorded a marginal increase of 0.3% (2008: 1.6%). The increase in employment was mainly in the services sector, as well as in the construction and agriculture sectors. In contrast, the manufacturing sector recorded a net decline in employment, reflecting largely the freeze in new hiring and the higher number of retrenchments. In order to mitigate the impact of the global recession on employment, the Government introduced several measures, including filling about 50,000 vacant positions in the professional and support group levels in the public sector, while another 100,000 individuals were provided with on-the-job training and were put in temporary job placements with various Government agencies, government-linked companies (GLCs) and private companies. These included more training places provided under the Special Training and Re-Training Programmes, industrial and technical skills training courses managed by various states' skills training centres as well as on-the-job training and job placements in the financial sector and GLCs. In addition, the Government also assisted firms to lower labour costs by reducing the Human Resource Development Fund levy and providing a double-tax deduction to companies that hired retrenched workers. A total of 22 new JobsMalaysia Centres were set up and 109 existing centres were upgraded to provide job-placement assistance, career counseling and information on training opportunities to unemployed workers.

In 2009, the total number of registered **foreign workers** (migrant workers and expatriates) declined by 23% to 1.62 million workers, of which 98% were the low-skilled migrant workers. Total migrant workers declined by 23% to 1.59 million (2008: 2.06 million) due to retrenchment and early termination of work contracts by employers. In addition, the Government also imposed stricter rules on the hiring of migrant workers, including a freeze on the hiring of new migrant workers in the manufacturing and services sectors, a prohibition of the practice of deducting levy payments from the wages of new migrant workers thereby increasing the cost of hiring, and a freeze on the issuance of new licenses for labour outsourcing companies. Foreign expatriates employed in the country declined by 13% to 32,138 persons.

Labour productivity, as measured by real value-added per worker, was also affected by the weak economic performance during the year. Labour productivity growth contracted by 2.0% in 2009 (2008: +3.0%) due mainly to a sharp decline in labour productivity in the manufacturing sector, as production fell in response to the significant deterioration in external demand in the early part of the year. Despite the challenging economic environment and lower productivity, employers in the private sector continued to grant salary

Chart 1.32
Labour Productivity Trends

e Estimate

Source: Bank Negara Malaysia
Department of Statistics, Malaysia

increments, albeit at a moderate rate. According to the survey conducted by Bank Negara Malaysia, average **salary** increments in the private sector moderated to 3.4% (2008: 5.1%), with both the executives and non-executives receiving a lower salary increment of 3.2% and 3.7% respectively (2008: 4.9% and 5.1%).

PRICE DEVELOPMENTS

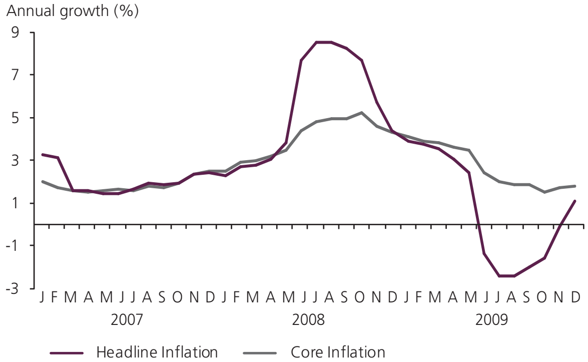
Consumer Prices

In line with global and domestic developments, inflationary pressures in Malaysia moderated substantially during the year. Headline inflation, as measured by the annual percentage change in the Consumer Price Index (CPI), averaged 0.6% in 2009 (2008: 5.4%). The marked decline in headline inflation during the year was driven by supply-related factors and subdued demand conditions. Meanwhile, core inflation, an indicator of the demand-driven pressure on prices, moderated to 2.7% in 2009 (2008: 4%).

Inflation in 2009 was influenced by both external and domestic factors. Externally, the economic weakness that emerged in the second half of 2008 had led to disinflationary pressures in both the major and emerging market economies. This impact was particularly evident in the first quarter of 2009. Two major forces responsible for these disinflationary pressures were the significant drop in global commodity prices, especially for crude oil, and the increasing slack in the economy as the global recession deepened.

After reaching its historical peak at USD147.27 per barrel in July 2008, oil prices plummeted by more than 60% in January 2009 (USD41.68 per barrel). The sharp reversal had a direct impact on inflation through lower retail fuel prices across the globe. Lower energy costs and lower prices for a wide-range of oil-related inputs also allowed producers to decrease their prices.

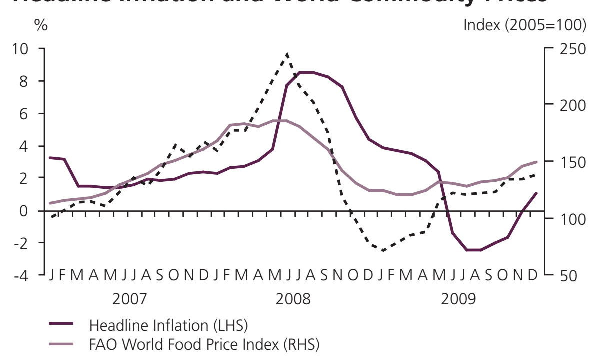
Chart 1.33
Consumer Price Inflation



In an environment of tighter credit conditions, rising unemployment and deteriorating consumer and business confidence, households and businesses restrained their spending activities and contributed to the weak global demand conditions, particularly during the early part of the year. As a result, many countries experienced lower inflationary pressures during the year. Inflation in the advanced economies recorded a steep decline. The annual inflation rate in the US dropped to levels that were not seen since the late 1940s, while annual inflation in the euro area declined to its lowest levels since the inception of the European Union. Similarly, inflation in emerging market economies also saw a decline in 2009 with considerable deceleration evident in PR China, where the inflation rate decreased from 5.9% in 2008 to -0.7% in 2009.

On the domestic front, Malaysia's position as a highly trade-oriented economy meant that external developments had a sizeable impact on the domestic economy. The decline in global fuel and commodity prices, and the deflationary conditions experienced by Malaysia's top trading partners, contributed to lower domestic inflation. Most significantly, the cumulative reductions in the retail petrol prices in the second half of 2008 contributed significantly to the moderating trend of domestic inflation. The effect was particularly

Chart 1.34
Headline Inflation and World Commodity Prices



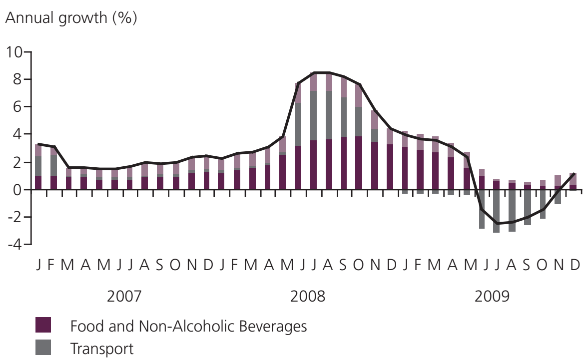
Note: 1. FAO stands for Food and Agricultural Organisation of the United Nations.
2. The FAO Food Price Index consists of a weighted average of 55 food commodities considered by FAO specialists as representing the international prices of food.
3. FAO Food Price Index and World Crude Oil Price Index were re-based using 2005 average as the base year.

significant in July 2009, as the high base effect accounted for a 19.9% drop in the *transport* category, which contributed to a 3.2 percentage point fall in inflation.

The impact on headline inflation was sizeable, with the annual rate of price level falling by -2.4% in July, its lowest rate since August 1986. The CPI for *food and non-alcoholic beverages* also moderated to an average of 4.1% during the year (2008: 8.8%). This mainly reflected the receding effect of global supply constraints. In particular, the CPI sub-category for *rice, bread and other cereals* moved into negative territory in June 2009 following the significant fall in global grain prices from the second half of 2008. As most of these base effects began to dissipate towards the end of the year, the headline inflation gradually recovered and started to turn positive again. Meanwhile, prices for other CPI categories remained relatively stable, with an average increase of 1.5% in 2009 (2008: 2.3%). Another important factor affecting headline inflation during the year was the imposition of an additional excise duty of 1 sen per cigarette in October, which resulted in higher CPI for the *alcoholic beverages and tobacco* category.

A key concern during the year was the risk of deflation. Given the base effect of high inflation in 2008 and the rapid disinflation, many countries registered negative inflation rates in 2009. As a result of the extensive scale of the global financial crisis that triggered a global recession, and the large uncertainties surrounding the prospects for resolution of the financial crisis and its impact on the real economy, some countries in the region faced the risk of a more prolonged and deeper deflation. By definition, deflation is a situation of a persistent and broad-based decline in the general price level. When such conditions prevail and result in entrenched deflationary expectations, the reinforcing postponement of consumption, falling asset prices and rising real debt burdens could drive the real economy into a more severe and protracted recession. The IMF World Economic Outlook in October 2009 reported that the deflation vulnerability indicator, which combines a range of macroeconomic indicators such as core inflation, output gap, house and equity prices as well as credit and broad money growth, pointed to an increased risk of deflation in a number of major and emerging market countries. However, the very strong policy responses both on the fiscal and monetary fronts succeeded in mitigating such an outcome. Concerns over deflation abated in the second half of 2009 as the financial crisis stabilised and global economic conditions began to show signs of improvement on the back of large and aggressive fiscal stimulus.

Chart 1.35
Contribution to Inflation



Note: Others refer to communication, clothing and footwear, health, education, recreation services and culture, furnishings, household equipment and routine maintainence, alcoholic beverages and tobacco, restaurant and hotels, miscellaneous goods and services and housing, water, electricity, gas and other fuels

For Malaysia, although headline inflation was negative between June and November 2009, deflation was mostly a statistical development and there was no evidence of deflationary pressures being embedded in the economy. Although core inflation moderated, it continued to remain positive throughout the year. Consumer and business confidence also remained resilient, underpinned by the significant policy measures undertaken by the Government and the Bank. More importantly, while demand conditions were relatively subdued during the year, they remained sufficiently strong to mitigate the risk of a protracted deflation.

Producer Prices

Producer price inflation, as measured by the Producer Price Index[1] (PPI), declined in 2009 amidst the broad decline in commodity prices. The annual change in the PPI averaged -7.1%

[1] Effective from 2010, the Producer Price Index (PPI) has been revised to the new base year 2005=100, from 2000=100 previously.

in 2009 compared with an increase of 10.3% in 2008. The annual change in the PPI followed a moderating trend in the first half of the year and reached its lowest rate for the year at -13% in July. This was largely consistent with the sharp decline of 32.5% in the commodity components of the PPI over the same period. Since then, PPI inflation has been increasing moderately, reflecting a mild rebound in global commodity prices. Overall, the PPI for commodity-related components recorded a decline of 19.8% in 2009 (2008: 26.6%). Meanwhile, non-commodity related producer prices declined at a relatively slower average annual rate of 2.5% in 2009 (2008: 5.8%).

In terms of composition, both the local and imported components of the PPI declined during the year. The annual growth of the PPI for local components fell to -10.4% in 2009 (2008: 13.3%), reflecting a broad-based decline across its sub-groups. Meanwhile, the weak global demand conditions and lower commodity prices were also reflected in the lower PPI for imported products, which declined by an average of 0.5% in 2009 (2008: 4%).

Monetary and Financial Conditions

Monetary and Financial Conditions

OVERVIEW

Following the widespread fallout from the US sub-prime crisis and the collapse of Lehman Brothers in September 2008, global monetary and financial conditions deteriorated in the first quarter of 2009. In the advanced economies, the crisis reached its peak in March 2009 and contributed to the worst global recession since World War II. Economic and financial conditions only stabilised in the second half of 2009 following unprecedented large scale interventions by the authorities in the advanced economies to support their financial system and revive the economy. Emerging economies were also adversely affected given the significant financial and economic linkages with the advanced economies. However, prompt fiscal and monetary stimulus mitigated the impact of the external shocks on the emerging economies.

As with many regional economies, Malaysia was adversely affected by the large contraction in external demand and the sharp decline in domestic financial asset prices as the worldwide deleveraging by investors caused large outflows of portfolio funds. Nevertheless, the implementation of two fiscal stimulus programmes, together with the easing of monetary policy, provided support for domestic demand. Additional measures to facilitate access to financing ensured that the environment was supportive of domestic consumption and investment. Meanwhile, the existence of a strong financial sector continued to support financial intermediation and reinforced the expansionary fiscal and monetary influences on domestic demand.

INTERNATIONAL MONETARY AND FINANCIAL CONDITIONS

Developments in international monetary and financial conditions in 2009 broadly followed three distinct phases. The first quarter of the year was characterised by turbulent financial market conditions amidst a severe global recession. This was followed by the stabilisation phase in the second and third quarters of the year, as the unprecedented scale of policy measures undertaken earlier in the year began to take effect. By the fourth quarter, economic and financial conditions stabilised and the expansionary impact of large fiscal and monetary stimulus led to a revival of growth.

After a tumultuous first quarter, the global monetary and financial conditions stabilised by mid-year and improved following the large scale fiscal support and unprecedented monetary stimulus in the advanced economies

In early 2009, monetary and financial conditions continued to deteriorate in the aftermath of the collapse of Lehman Brothers and the continued fallout from the excessive leverage in the US financial system. The broad-based loss of confidence arising from the Lehman episode led to heightened risk aversion which continued into the first two months of 2009. In many countries, liquidity conditions tightened amid significant sell downs and volatilities in the equity and bond markets.

Chart 2.1
Measures of Volatility*

*Chicago Board of Exchange (CBOE) Implied Volatility Index (VIX) and Merrill Lynch Option Volatility Estimate (MOVE)

Source: Bloomberg

Financial conditions were particularly dire in the advanced economies. In the first two months of the year, the S&P 500 equity index declined by 21.1% while the 3-month LIBOR less OIS spread, which measures the level of liquidity and credit risk in the interbank market, continued to remain elevated at levels indicating failures of financial intermediation. The dysfunctioning interbank markets severely impaired the financial intermediation process which in turn disrupted credit flows to the broader economy. This had significant repercussion on economic activity. The real sector plunged into a deep recession amid contracting consumption, investment and trade activity. Most advanced economies experienced a sharp contraction in economic activity in the first quarter, with the growth outlook being very bleak. The IMF's forecast for growth in 2009 for advanced economies was downgraded from 0.5% in October 2008 to -2% in January 2009. Key economic indicators, including industrial production and labour market conditions continued to deteriorate significantly and at a faster pace. The strong feedback loops between the real and financial sector meant that weaknesses in economic activity further intensified financial sector dislocations and vice versa.

The intensity of the problems in the financial and real sectors prompted a wide range of government interventions. These interventions were designed to restore the functioning of the financial and financial institutions, and to provide support to the real economy. To stabilise financial conditions, various conventional and unorthodox measures were implemented

Chart 2.2
Selected Equity Market Indices

Source: Bloomberg

including government guarantees, purchases of private sector assets, recapitalisation programmes and quantitative easing. This was strongly reinforced by sizeable fiscal stimulus programmes of between 1% to 6% of GDP by authorities in advanced economies, and monetary policy easing to provide support to growth. These policies, however, took some time to gain traction given the severity of the financial conditions.

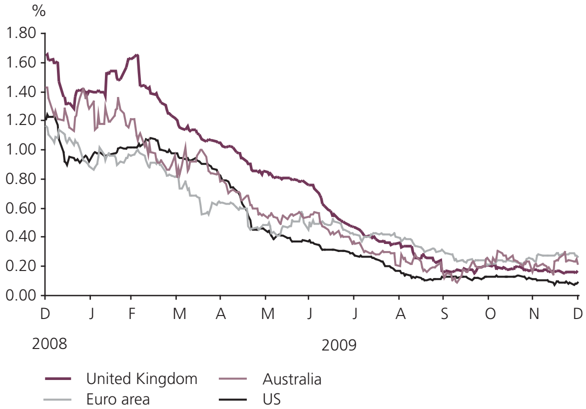
Meanwhile, despite minimal direct exposure to the sub-prime crisis and to the problems in the derivatives markets, financial markets in emerging economies were also significantly impacted given the financial inter-linkages with the major financial markets. The MSCI Emerging Index declined by 14.1% year-to-date in February as global deleveraging caused foreign investors to dispose their assets in emerging economies. As these funds were remitted back to the US, it resulted in large capital outflows causing the currencies of some emerging economies to depreciate by an average of 8.8% against the US dollar during the period.

Growth in open emerging economies was also impacted by the contraction in global trade following the collapse in external demand from advanced economies. Export growth for Hong Kong, Singapore and Malaysia fell by 21.1%, 20.7% and 15.7% year-on-year respectively at the end of the first quarter. In addition, the contraction in trade was intensified by a shortage of dollar liquidity in international financial markets, which affected trade financing.

Policy responses by authorities in emerging economies were rapid and generally aimed at mitigating the impact of the crisis from the advanced economies. The measures involved a combination of monetary and fiscal measures that included lowering interest rates to sub-normal low levels, improving access to financing and large fiscal spending. The strong overall initial conditions of emerging market economies as a group, their sound banking systems and fiscal flexibility, placed emerging economies in a better position to institute decisive and strong counter-cyclical measures in response to the crisis.

By the second quarter, there were visible signs of stabilisation in the financial markets coupled by some improvements in business and consumer sentiments. In the advanced economies, financial conditions began to show improvements as a result of the wide range of measures initiated by

Chart 2.3
Money Market Spreads*



* 3-month LIBOR less 3-month Overnight Index Swap (OIS)

Source: Bloomberg

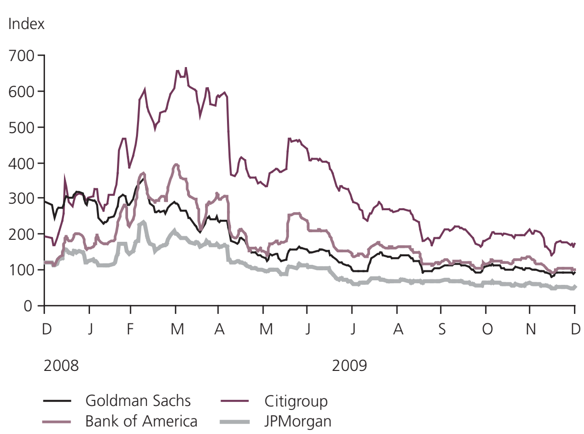
the authorities. Interbank money market spreads declined considerably from the second quarter onwards, indicating that the additional liquidity provided to the financial markets were taking effect. The 3-month LIBOR less OIS spreads declined from an average of 101 basis points in the first quarter of 2009 to an average of 23 basis points in the third quarter of 2009.

The health of major financial institutions also improved as indicated by the positive results from the bank-wide stress tests to ascertain the solvency of financial institutions. The decline in credit default swaps of major banks in the US by almost one-third was a testament to the renewed confidence in the financial institutions. As conditions improved, financial markets rose steadily albeit at a cautious pace. Between March and May 2009, the S&P 500 index rose by 25.2%, recovering all of the losses incurred since the beginning of 2009. In the third quarter, volatility in the financial markets as proxied by the VIX index, dropped significantly and returned to levels prior to the collapse of Lehman Brothers.

Though the measures had a positive effect on reducing stress in the financial markets and restoring the functioning of the markets, the underlying economic conditions in the advanced economies remained weak. Credit to the broader economy was still constrained as both lenders and borrowers remained cautious. Lending standards in major advanced economies remained tight. While key economic indicators were at depressed levels, there were however incipient signs that economic conditions were deteriorating at a slower pace. Nevertheless, as economic and financial conditions improved, questions lingered on the sustainability of the recovery given that the financial system remained impaired.

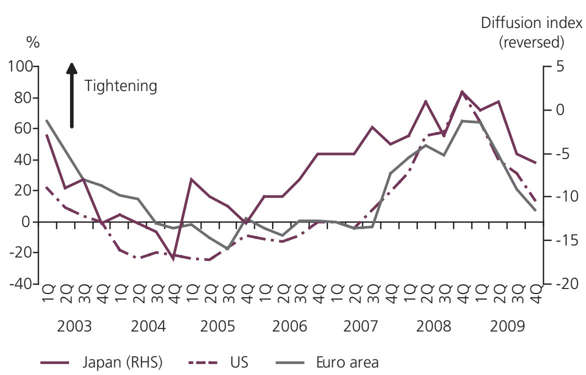
Emerging economies, in contrast, had shown firm indications of economic recovery by the second quarter of 2009. With stronger initial conditions and reinforced by comprehensive fiscal and monetary responses, emerging economies were able to recover at a faster pace. Given the strong signs of economic recovery, investors' risk appetites for emerging market financial assets rose. Equity markets in emerging economies rallied by an average of 61.6% compared to 36.2% in the advanced economies.

Chart 2.4
US Banks 5-year Credit Default Swaps (CDS)



Source: Bloomberg

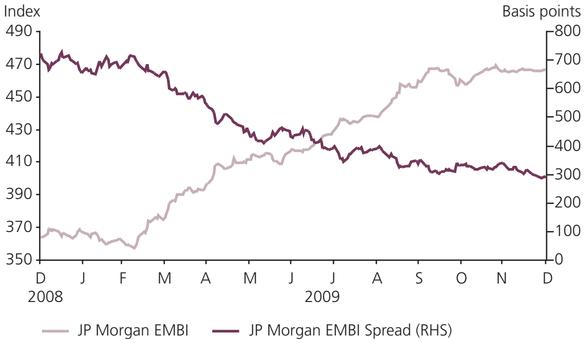
Chart 2.5
Bank Lending Conditions for Business*



*Based on Senior Loan Officer Survey conducted in selected countries

Source: Central Banks' Websites

Chart 2.6
Emerging Market Bond Index (EMBI) and Bond Spreads EMBI

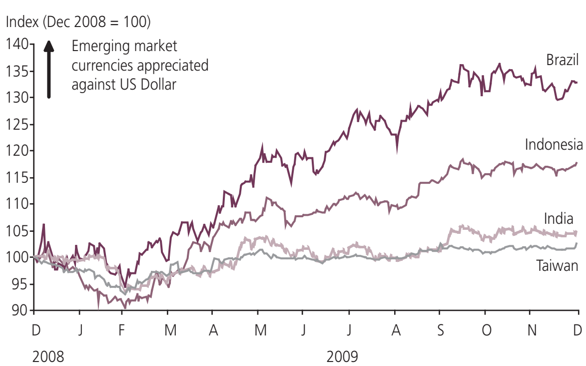


Source: Bloomberg

By the fourth quarter of the year, economic and financial conditions in both advanced and emerging economies showed visible and firm signs of recovery. This improved investor confidence and revived financial market trading activities globally. With the world awash with liquidity amid record-low interest rates globally, the search for yields led to a sharp increase in foreign portfolio inflows into emerging markets. As a result, emerging market currencies, in particular the Indonesian rupiah, Brazilian real and Korean won appreciated strongly by 17.7%, 33.0% and 10.0% respectively in 2009. Better recovery prospects and expectations of further currency appreciation also added to the interest towards emerging markets.

The surge in capital inflows, coupled with the uptrend in commodity and property prices, begun

Chart 2.7
Emerging Market Currencies against the US Dollar



Source: Bloomberg

to raise concerns over the possible formation of asset price bubbles in emerging economies. Some emerging economies such as Brazil and Taiwan imposed restrictions on capital inflows to avoid undue volatility in the financial markets and to mitigate the impact on monetary conditions. These restrictions included a tax on flows into equity and fixed-income securities, as well as a ban on foreign investors placing their money in time deposits.

By the end of the year, stronger signs of recovery had emerged. This prompted discussions among policymakers on the need to review the policy stance. The exceptionally low interest rate environment implemented when the risk of a fundamental economic downturn was high needed to be realigned to avoid the risk of the build-up of financial imbalances. Thus, whilst remaining accommodative, a number of central banks including the Reserve Bank of Australia began to raise policy rates, with several others stated the intent to do so in the near future. The pace, timing and magnitude of policy rate adjustments would, however, differ across countries and regions given the disparities in economic and financial conditions across countries.

DOMESTIC MONETARY AND FINANCIAL CONDITIONS

The domestic monetary and financial conditions continued to remain favourable and supportive of economic activity in 2009 despite being subjected to adverse economic and financial shocks in the aftermath of the global financial crisis. Prompt policy response and the resilience of the banking sector and capital market ensured that the financial intermediation process functioned effectively and smoothly. Domestic conditions improved markedly towards year-end with firm indications of a sustainable recovery.

Exchange Rate

The ringgit performance during the year reflected the volatile developments in international financial markets. Early in the year, the ringgit and regional currencies faced intense depreciation pressure as the global financial and economic crisis were in full force. Nevertheless, the sell down of financial assets across the world eased by March 2009 following emerging signs of stabilisation in the international financial markets and in global economic activity.

The ringgit continued its depreciating trend into early-2009 as the full impact of the global financial crisis enveloped the global economy. Against the background of heightened market risk and as investors continued to deleverage to reduce their level of borrowings, assets in emerging economies were sold off. During this stressed financial environment, investor preference also shifted to holding cash to preserve capital. The consequent reversal of portfolio investments and the surge in the demand for US dollar as these funds were remitted to the US generated significant depreciation of currencies in the regional economies. The ringgit weakened to RM3.7255 against the US dollar on 2 March 2009, the lowest level since February 2006. The depreciation was, however, partly mitigated by the continued net trade surplus, which provided underlying support for the demand for ringgit. The strong international reserve position also instilled greater market confidence on the ability of Bank Negara Malaysia to maintain orderly market conditions despite the volatile global environment.

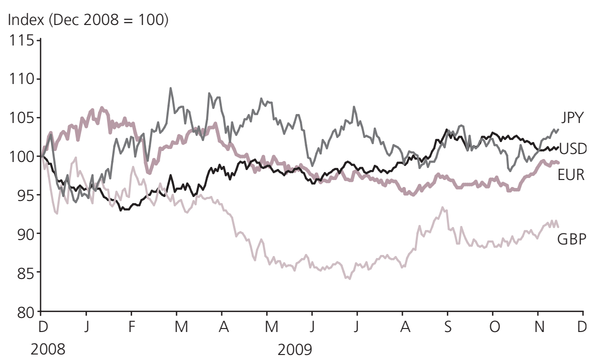
Despite the volatile global financial market conditions, the movement of the ringgit remained orderly and had an important role in absorbing external shocks to the domestic economy

The downward trend of the ringgit subsequently reversed in March 2009, following a confluence of external and domestic factors. The large scale expansionary measures undertaken by policymakers to arrest the global economic slide were instrumental in restoring confidence and stabilising global financial market conditions. These measures served to lift investor sentiment and risk appetite, and shifted their focus to the better outlook in the regional economies. The sound financial systems and stronger economic fundamentals amongst emerging economies point to prospects for an earlier and stronger recovery. These conditions attracted large portfolio flows into emerging markets and raised the demand for regional currencies including the ringgit. The ringgit also benefited from positive market reaction to the second stimulus package announced on 10 March. In addition, the accelerated implementation of the fiscal stimulus measures, the accommodative monetary conditions, the resilient financial system and the continued access to financing have further supported positive investor sentiments towards the domestic financial markets. Consequently, net portfolio inflows increased by RM13.3 billion in the second half of the year and the ringgit strengthened to RM3.3475 against the US dollar on 15 October, an appreciation of 11.3% from its lowest level recorded in early March 2009.

The ringgit, however, fluctuated within a broad downward trend from mid-October 2009 until the end of the year, amid greater market volatility arising from heightened and volatile global risk aversion. The imposition of capital controls in Brazil and Taiwan fuelled concerns that other central banks in the region could also move in the same policy direction, which dampened investors' risk appetite for regional markets. Market sentiments were also affected by concerns about the potential systemic impact of the debt crisis in Dubai and the sovereign debt issue in Greece. On balance, the ringgit ended the year at RM3.4245 against the US dollar, 1.2% stronger compared to the level at end-2008.

Against other major currencies, the ringgit appreciated against the Japanese yen (3.4%). The yen was particularly vulnerable to swings in carry trade activity. The ringgit ended the year marginally weaker against the euro (-0.9%) and more significantly against the pound sterling (-9.1%). To a large extent, the appreciation in

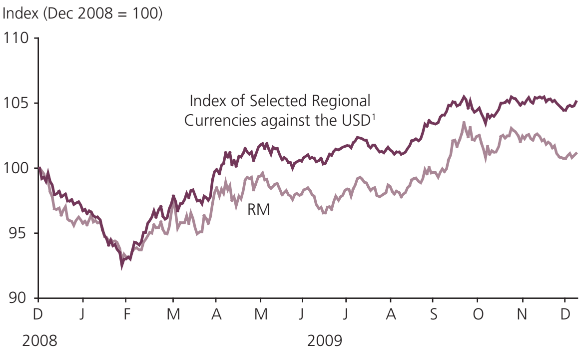
Chart 2.8
Exchange Rate of the Malaysian Ringgit (RM) Against Major Currencies



Note: An increase in the index indicates an appreciation of ringgit against the currency

Source: Bank Negara Malaysia

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

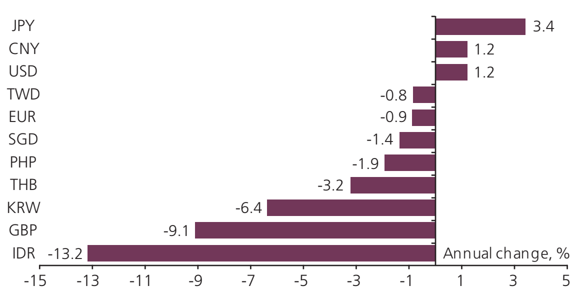


[1] Regional currencies: Chinese renminbi, Indonesian rupiah, Korean won, Philippine peso, Singapore dollar, New Taiwanese dollar and Thai baht. Each currency is of equal weight.

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

Source: Bank Negara Malaysia

Chart 2.10
Summary of Malaysian Ringgit Performance Against Major and Regional Currencies in 2009



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

the pound sterling was a correction from the significant depreciation of the currency against most international currencies in 2008, after the UK economy was severely affected by the financial crisis.

In 2009, the ringgit was broadly weaker against regional currencies with this trend reversing in early 2010. Intra-regional exchange rate performance was differentiated by country-specific factors. In particular, the Korean won and the Indonesian rupiah strengthened significantly against most currencies, following positive market sentiments. Strong domestic demand contributed to Indonesia's relatively better economic performance. It also partly reflected recovery in both the Indonesian rupiah and Korean won from the large depreciation experienced in 2008. Between September 2008 and February 2009, the Indonesian rupiah and the Korean won had depreciated against the ringgit by 20.3% and 28.3% respectively. This provided greater appreciation potential for these currencies relative to other regional currencies when the global conditions improved.

The ringgit depreciated by 1% in Real Effective Exchange Rate (REER) terms during the year. The REER refers to the weighted average of the ringgit against the currencies of Malaysia's major trading partners, adjusted for differences in inflation rates. By and large, the depreciation of the REER during the year was due mainly to the broad depreciation of the Nominal Effective Exchange Rate (NEER), which also declined by 1% during the same period. Malaysia's prices relative to the major trading partners remained stable, as the pace of changes in prices of goods and services across countries decelerated in an almost synchronised manner amidst global disinflationary pressures.

The intensification of two-way movements of capital flows into emerging economies in an environment of an uncertain recovery of the global economy raised concerns of the potential risks to the trade sectors of these economies. In addition, strong financial inflows could become destabilising with the potential for a sudden reversal of these flows. To Malaysia's advantage, the country's capacity and resilience in managing these sizeable and volatile financial flows had been fortified in a number of ways. First, our economic fundamentals have remained healthy and the financial markets were more diversified and developed. This has enhanced the ability of the financial system to absorb capital inflows and outflows, thereby minimising disruptions while ensuring that the capital flows can be effectively intermediated. Second, the managed float regime accorded the necessary flexibility for the ringgit to adjust to changing conditions. Since exiting from the fixed exchange rate regime, the managed float regime has served the economy well by providing a good balance between flexibility and stability. Third, the ability to manage domestic liquidity has also improved significantly, supported by a wider range of instruments to conduct monetary operations and having in place better surveillance and information system. This ability to manage liquidity effectively meant that financial flows have limited impact on financial intermediation and the level of economic activity, including reducing the risk of the build-up of large imbalances in the economy.

Interest Rates, Bond Yields and Equity Prices
Interest rates in 2009 were lowered substantially to support a highly accommodative monetary policy. The thrust of monetary policy during the year was focused on mitigating the impact of the economic and financial crisis on domestic demand. In addition to the 25 basis points reduction in November 2008, the Overnight Policy Rate (OPR) was lowered by 75 basis points in January 2009, and a further 50 basis points in February 2009. To expedite the transmission of the policy rate reductions to retail rates, the Statutory Reserve Requirement (SRR) was also concurrently reduced from 4% to 1%. The monetary policy measures were transmitted quickly by the domestic financial system and had a material impact on the economy.

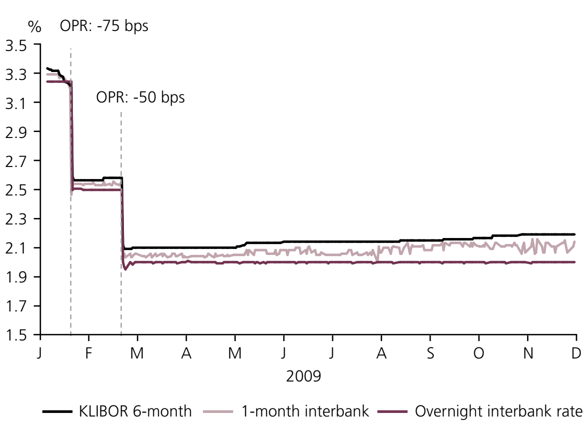
Sound financial institutions and stable liquidity conditions facilitated a rapid pass-through of the OPR reductions into lending rates

Following Bank Negara Malaysia's decision to reduce the OPR, the overnight interbank rate in the money market decreased from 3.25% on 1 January 2009 to 2.00% on 25 February with concurrent reductions in the interbank rates of other maturities. The high degree of pass-through from the OPR to the money market rates was supported by stable liquidity conditions in the interbank market. The sound financial institutions also underpinned orderly trading in the market, with little signs of market disruptions despite the volatile conditions in the global financial market. Accordingly, money market rates were stable and at historical lows during the year.

Reflecting the high pass-through of the OPR reduction to the money market interest rates, banks responded by lowering retail lending rates to households and businesses. The benchmark lending rate, as measured by the average base lending rate (BLR) of commercial banks, was reduced by 121 basis points, from 6.72% to 5.51%, by end-2009. This lowered the interest cost on variable rate loans pegged to the BLR, increasing the disposable income of borrowers. The adjustment in the BLR was transmitted quickly, with all banks lowering their respective BLRs within two weeks of the OPR adjustments.

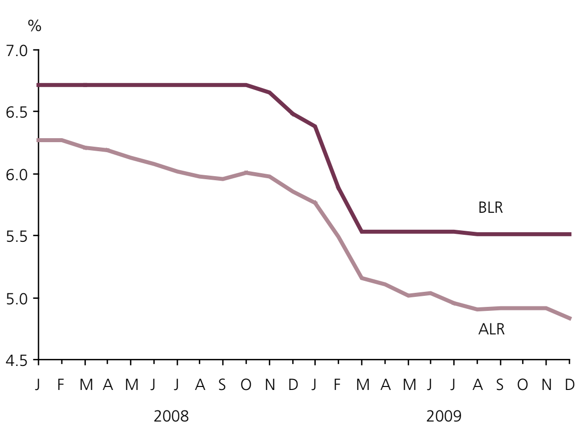
New borrowers also benefited from the low interest rate environment, as lending rates on new loans to both businesses and households were reduced. This was evidenced by the 127 basis points decline in the average lending rate (ALR) on new loans approved, from 6.17% in October 2008 to 4.90% in December 2009.

Chart 2.11
Money Market Rates



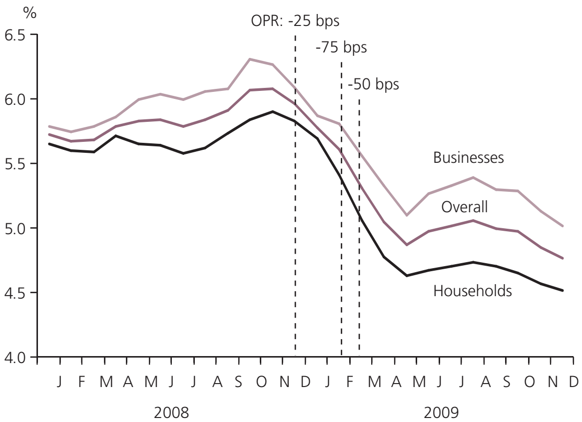
Source: Bank Negara Malaysia and Bloomberg

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



Source: Bank Negara Malaysia

Chart 2.13
ALR on New Loans Approved (3-month moving average)

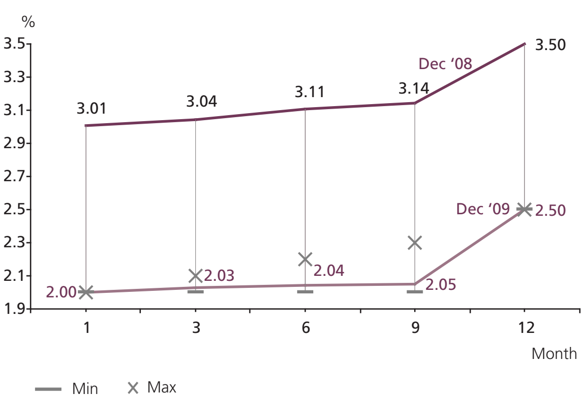


Source: Bank Negara Malaysia

The reduction in lending rates on new loans was broad based, with loans to all sectors of the economy registering lower interest rates after the OPR was reduced. With the re-pricing of new and existing loans, the ALR on loans outstanding stood at a historic low of 4.83% as at end-2009. The low interest rate environment, in turn, provided a supporting environment to financing activity.

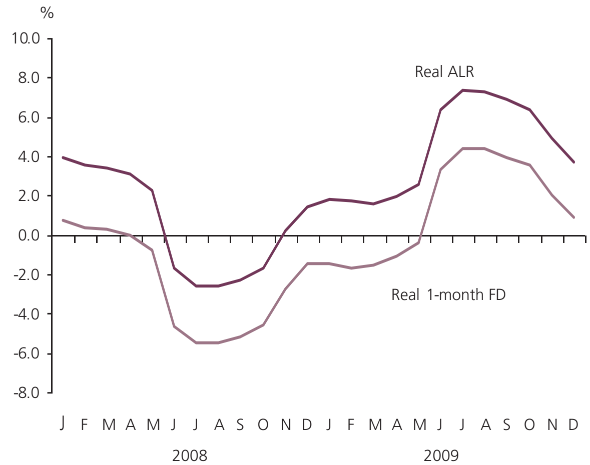
Deposit rates were also adjusted downwards. Nevertheless, fixed deposit (FD) rates were supported by the floor imposed by Bank Negara Malaysia. As a result, the interest rates on FDs with tenures between 1 to 12 months ranged from 2.00% to 2.50%, at end-2009. Towards the middle of the year, depositors also received a positive real rate of return as inflation turned negative.

Chart 2.14
Commercial Banks' Fixed Deposit Rates



Source: Bank Negara Malaysia

Chart 2.15
Real Deposit and Lending Rates



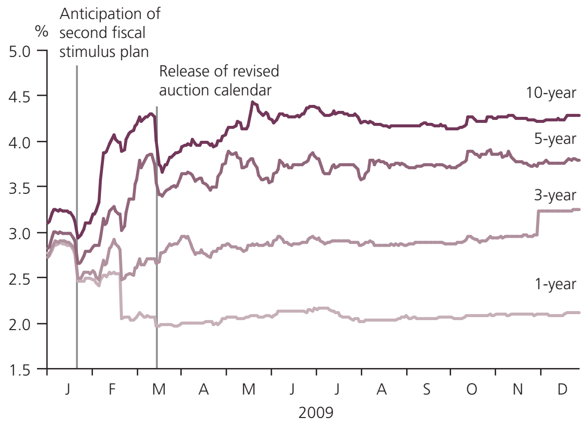
Source: Bank Negara Malaysia

Sovereign bond yields rose initially due to concerns on the large increase in the issuances of Government securities, but remained generally stable for the major part of the year as economic conditions improved amid a benign inflation outlook. Trading activity was mainly focused on the shorter end of the market, reflecting investors' cautious sentiments.

MGS yields were stable for most part of 2009

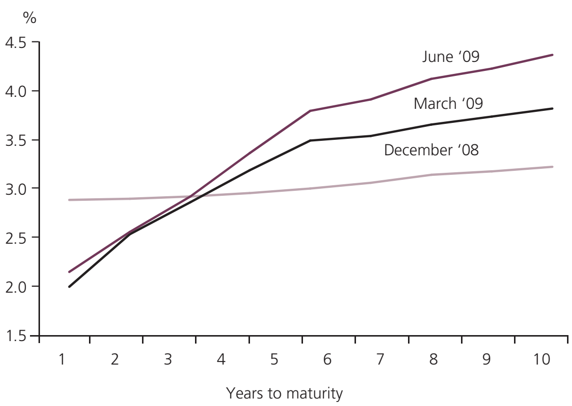
Yields on Malaysian Government Securities (MGS) were initially on a declining trend in early 2009 due to heightened risk aversion among investors as the outlook for the global economy deteriorated. The reduction in the OPR on 21 January added further impetus to the downward trend in MGS yields, amid expectations that inflation was moderating. The declining trend, nevertheless, reversed following the Government's announcement to introduce a second stimulus package. Market soon became anxious about the size of the stimulus and the potential additional issuances of Government securities. As these concerns mounted, MGS yields rose markedly, particularly those for the longer maturities. The 5-year and 10-year MGS increased by 106 and 116 basis

Chart 2.16
MGS Yields



Source: Bank Negara Malaysia

Chart 2.17
MGS Benchmark Yield Curve



Source: Bank Negara Malaysia

points respectively between end-January to mid-March. The reduction in the OPR in February provided only a temporary downward effect, as MGS yields continued to rise on concerns over the potential large size of new Government borrowings.

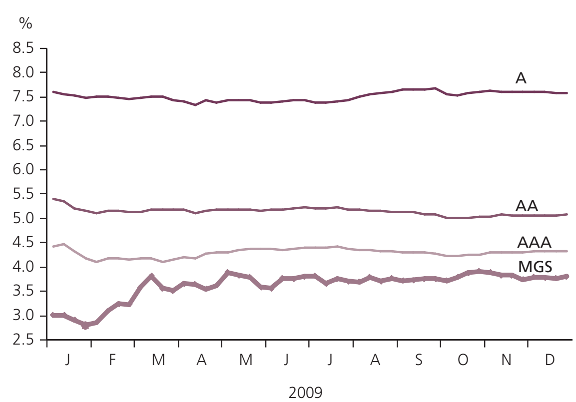
MGS yields fell by end-March as such anxieties dissipated following the release of a revised auction calendar for Government securities. Investors, nevertheless, remained broadly cautious given the continued uncertainty on the macroeconomic outlook and tended to focus on securities of shorter maturities. This led to the reduction of liquidity at the longer end of the MGS yield curve, thus exerting upward pressure on long-term yields. In turn, following the stronger interest in the shorter-tenure MGS, the 1 and 3-year MGS yields rose only marginally by 15 and 6 basis points respectively between end-March and end-June, resulting in a further steepening of the slope of the yield curve.

By end-June, market sentiments began to improve amid investors' easing concerns over the larger supply of Government securities. The upward pressure on long-term yields also began to ease. MGS yields across all maturities became more stable thereafter and through most of the second half of 2009. Towards year-end, MGS yields trended slightly higher on firmer expectations of an economic recovery driven by news of better economic data on trade and industrial production. In December, the 3-year MGS yields recorded an increase of 26 basis points following the issuance of the new 3.5-year MGS, which replaced the previous 3-year MGS as the new benchmark. The higher yields mainly reflected the slightly longer maturity of the new benchmark.

PDS yields affected by risk aversion

In the private debt securities (PDS) markets, yields were mainly affected by investors' increased risk aversion. Factors such as investor concerns over credit conditions significantly influenced the yields of lower-rated PDS. Concerns over deteriorating credit conditions were amplified by the rising number of negative rating actions, especially in the first half of 2009. The heightened risk aversion led to a low level of

Chart 2.18
MGS and PDS Yields (5-year)



Source: Bank Negara Malaysia

liquidity in the PDS market, which pushed the yields of lower-rated PDS higher.

Mirroring the trend in the MGS market, liquidity in the PDS market improved as sentiments became better towards end-July. The establishment of Danajamin Nasional Berhad, a financial guarantee institution that provides credit guarantees to selected issuers, also contributed to the improved sentiments in the bond market. Lower-rated PDS yields, however, registered only a marginal improvement towards the end of the year due to lingering credit concerns.

Credit spreads for PDS narrowed in 2009. This may initially have seemed counter-intuitive in an economic downturn. Nevertheless, further analysis revealed that earlier in the year, credit spreads narrowed following higher MGS yields, as markets anticipated more issuances by the Government. Subsequently, relative stability returned to both the PDS and sovereign markets as the economic and financial outlook improved. Credit spreads were generally stable in the second half of the year. For the year as a whole, credit spreads for higher-rated securities (5-year) fell by between 96 to 104 basis points.

Chart 2.19
Turnover of Corporate Debt Securities

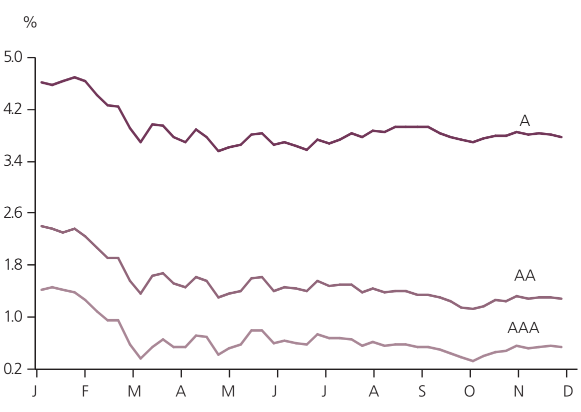
Source: Bank Negara Malaysia

Firmer signs of economic improvement spurred the equity market

In the early part of the year, the domestic equity market experienced bouts of volatility amid highly challenging domestic and global conditions. Subsequently, from the second quarter, equity markets around the world including Malaysia staged a strong rebound from the depressed levels in early 2009 as investors turned opportunistic amid highly accommodative monetary conditions and stabilising financial markets. Risk appetite improved further on the improving outlook for economic revival as the fiscal stimulus began to support economic activity.

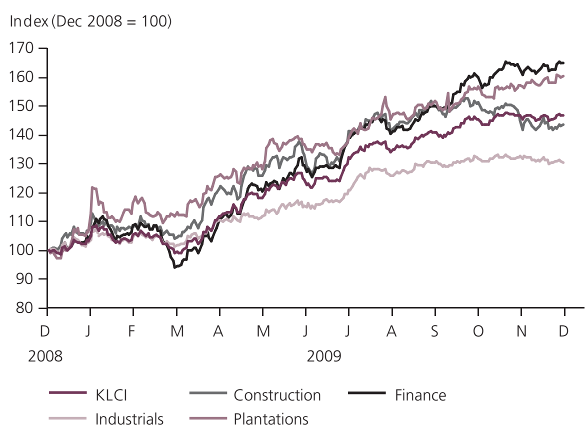
The domestic equity market experienced significant volatility in the early part of the year amid heightened uncertainties in the global

Chart 2.20
Corporate Credit Spread Against MGS (5-year)



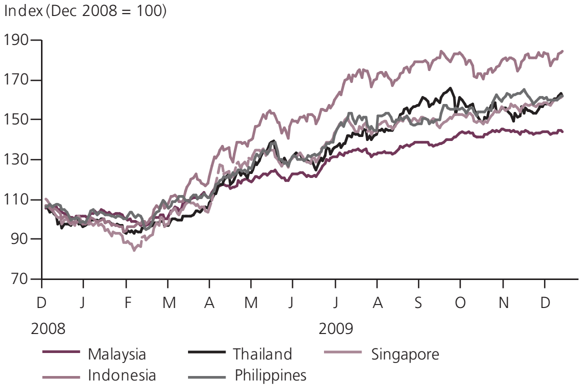
Source: Bank Negara Malaysia

Chart 2.21
KLCI and Bursa Malaysia Sectoral Indices



Source: Bloomberg

Chart 2.22
Regional Indices

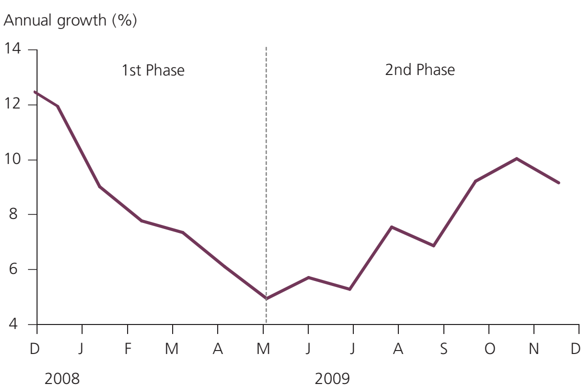


Source: Bloomberg

financial markets. The benchmark FTSE Bursa Malaysia Kuala Lumpur Composite Index (FBM KLCI) reached a low of 838.4 points on 12 March but began rising, albeit modestly, from end-March 2009. This was supported by the rise in commodity prices which boosted the plantation and oil and gas-related stocks. In addition, domestic participation increased as market sentiment began to improve.

In the second half of 2009, regional equity markets including Bursa Malaysia was lifted further by the reallocation of global funds to emerging markets, including Asia, on optimism for a stronger pace of economic recovery. Equity prices were further boosted by improving corporate earnings outlook. The announcement by the Government of the liberalisation of the services and financial sectors and efforts to increase liquidity of the stock market by Bursa Malaysia also provided additional impetus to the market. For the year as a whole, the FBM KLCI rose by 45.2% (2008: -39.3%).

Chart 2.23
Broad Money, M3



Source: Bank Negara Malaysia

Liquidity and Monetary Aggregates

Liquidity conditions were ample throughout 2009 and supportive of economic activity. Private sector liquidity was affected by global and domestic credit conditions. This was largely due to the deleveraging activities of international financial institutions, which caused the outflow of funds from Malaysia. As such, private sector liquidity, as measured by broad money, exhibited two distinct stages in 2009.

Between January and May, lending by banks to businesses and households moderated, reflecting the slowdown in economic activity that affected the demand for credit. The impact of slower credit growth on broad money was compounded by the contractionary impact of net foreign outflows

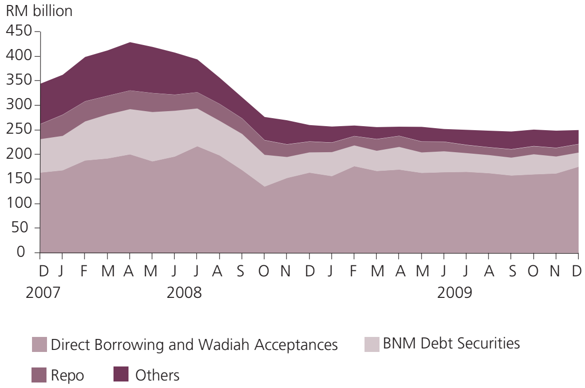
Table 2.1
Broad Money, M3

	Change (RM billion)	
	2009	
	1H	2H
M3	**18.6**	**66.5**
Currency in circulation	0.5	2.6
Demand Deposits	1.7	13.0
Broad Quasi-Money	16.5	51.0
Fixed deposits	*17.5*	*5.7*
Savings deposits	*5.7*	*4.4*
NIDs	*-1.2*	*-7.6*
Repos	*0.0*	*0.9*
FX deposits	*1.2*	*14.1*
Other deposits	*-6.7*	*33.5*
Determinants of M3		
Net claims on Government	11.5	14.2
Claims on the private sector	10.8	40.7
Loans	*12.3*	*34.7*
Securities	*-1.5*	*6.0*
Net foreign assets*	-0.4	12.1
*Bank Negara Malaysia**	*-6.0*	*2.7*
Banking system	*5.6*	*9.4*
Other influences	-3.3	-0.5

* Pre-revaluation of the international reserves

Source: Bank Negara Malaysia

Chart 2.24
Outstanding Liquidity Placed with Bank Negara Malaysia (at end-period)



Source: Bank Negara Malaysia

on domestic liquidity. These factors, however, were partially mitigated by the Government fiscal spending which supported broad money growth throughout the year. The expansion in broad money moderated in the first half of the year, growing at an annual pace of 5.7% in June.

Subsequently, the broad money trend reversed to grow at a faster annual pace. The turnaround in broad money reflected the improvement in the domestic and external economic and financial environment. Financing by the banking system to the private sector picked up, reflecting the recovery in economic activity and was supported by the low interest rate environment. In addition, broad money also expanded in the second half of the year due to net foreign inflows. Broad money ended the year with a higher rate of growth of 9.2% in December.

Bank Negara Malaysia conducted monetary operations in the domestic money market to ensure liquidity in the banking system remained ample. Compared to 2008, however, liquidity conditions in the interbank money market in 2009 were far more benign. Outflows of liquidity following foreign selling of domestic assets, which continued from 2008 into the first quarter of 2009, were offset by the release of liquidity absorbed by Bank Negara Malaysia. In this respect, the large interbank placements with the Bank acted as a liquidity buffer for the banking system. For the remainder of the year, liquidity in the interbank market was ample and relatively stable.

While the size of the surplus liquidity was reduced by foreign portfolio outflows, banking system liquidity, nonetheless, remained in surplus. This was evident from the loan-deposit ratio, which ranged between 77.7 in January and 77.9 in December. At the institution level, all banks operated from a position of surplus liquidity with net placements of funds with the Bank. The large number of institutions with surplus liquidity was one of the factors underpinning the resilience of the banking system as a whole.

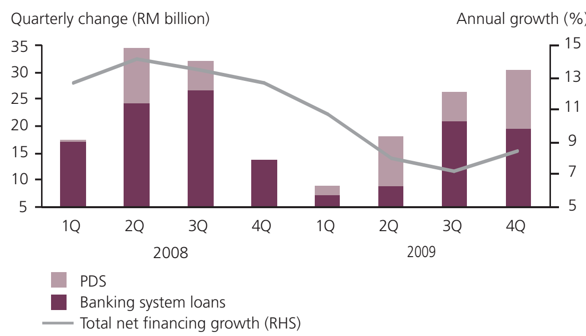
Bank Negara Malaysia also reduced the level of required reserves that banks hold against eligible liabilities from 4% to 1%. While this move increased the liquidity available to banks, Bank Negara Malaysia's main motivation for cutting the SRR was to reduce the cost of intermediation in the banking system. As a result, banks were able to pass on a larger share of the OPR reduction through reductions in their retail lending rates.

FINANCING OF THE ECONOMY

Financing conditions in 2009 remained conducive and supportive of economic activity. The sound banking system and functioning capital markets, coupled with historically low interest rates and ample liquidity, ensured that financing activity continued to expand.

Growth of private sector financing was slower in the early part of the year in tandem with the general weakness in the economy. Financing, nevertheless, gained momentum towards the second half of the year, supported by lower lending rates and extensive measures put in place to ensure continued access to funds for all sectors of the economy. In addition, the resumption

Chart 2.25
Total Net Financing to the Private Sector through Banking System Loans and PDS



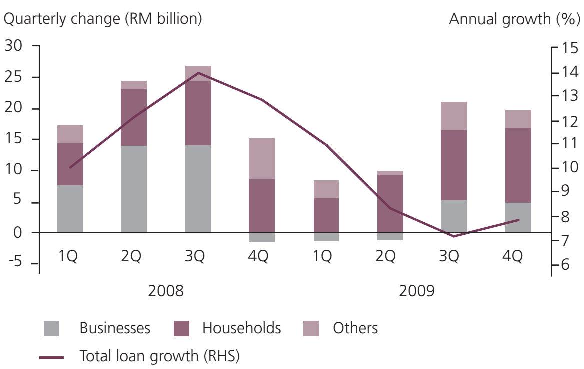
Source: Bank Negara Malaysia

of growth in the fourth quarter of the year contributed to increased demand for financing. For the year as a whole, net financing to the private sector raised through banking system loans and PDS rose by 8.5% (2008: 12.7%).

The lower cost of borrowing and continued availability of financing supported the financing requirements of businesses and households

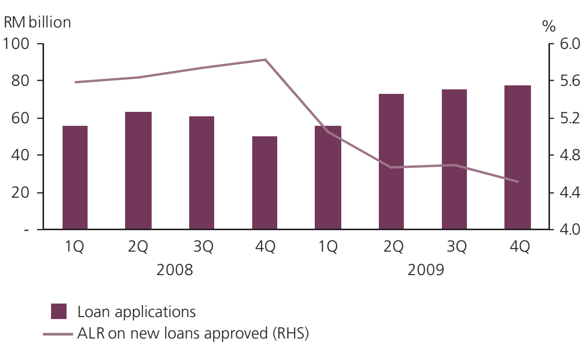
During the year, higher loans extended to the household sector were underpinned by both the lower cost of borrowings and the availability of financing in a competitive environment. From the demand side, the lower interest rates provided the opportunity for households to refinance loans contracted earlier at higher rates, including housing, personal and credit card loans. For new housing loans, demand was also augmented by measures announced by the Government in the first and second stimulus packages to promote home ownership. These measures included a 50% stamp duty exemption extended to loan agreements for the purchase of houses up to RM250,000, as well as tax relief of up to RM10,000 a year for three years on interest paid on housing loans. Towards the second half of the year, households' financing were further supported by improvement in consumer sentiments and labour market conditions.

Chart 2.26
Loans Outstanding by Customers



Source: Bank Negara Malaysia

Chart 2.27
Households: Loan Applications and ALR on New Loans Approved*



* Exclude credit cards

Source: Bank Negara Malaysia

From the supply side perspective, banking institutions placed greater focus on the lending to households as economic slowdown clouded the outlook for businesses. Many banks offered more attractive packages for the refinancing of housing loans and promoted transfers of credit card balances. Banks also lowered rates on newly approved personal loans to an average of 6.31% (2008: 7.72%). As such, notwithstanding the moderation in economic activity, household loans outstanding rose by 9.8% in 2009 (2008: 9.7%), accounting for a higher share of total loans outstanding at 55.1% (end-2008: 54.1%). More loans were extended for the *purchase of residential* and *non-residential properties, personal use, purchase of passenger cars* and *purchase of securities.*

Loans extended to individuals for the *purchase of securities* expanded at a faster pace of 24.5%. This trend was in tandem with the rally in the stock market. However, the overall volume of loans

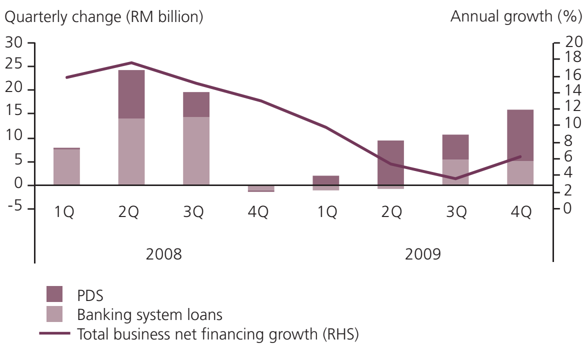
Chart 2.28
Households: Loans Outstanding for the Purchase of Securities and KLCI Index

Source: Bank Negara Malaysia and Bloomberg for the *purchase of securities* remained small, accounting for only 4.8% of household loans and 2.6% of total loans at end-2009.

Notwithstanding the increase in debt, the household sector's balance sheet improved as evidenced by the decline in household debt to liquid financial asset ratio. The ratio of non-performing households' loans over loans outstanding also remained low at 3.1% (end-2008: 4.1%). To ease the loan repayment burden of households, the banking institutions actively undertook debt restructuring and rescheduling. In addition, the Government announced in March 2009 a one-year moratorium on housing loans for retrenched workers.

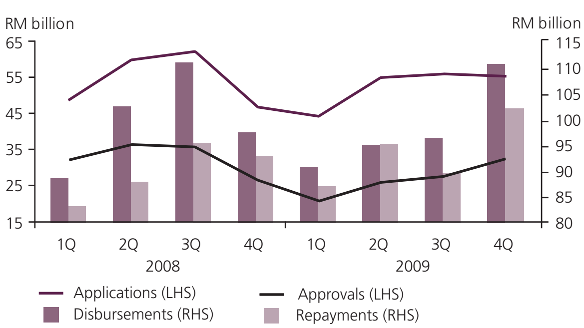
In contrast to the household sector, the growth in financing to the business sector was more moderate. Net financing extended to the business sector through the banking system and the PDS market increased by 6.3% (2008: 12.9%). The slowdown in global and domestic demand clearly affected business profitability. Consequently, some businesses scaled down their operational capacity and postponed their expansion plans, reducing their demand for financing for their working capital requirements and investment activities. As such, loan applications from the business sector contracted by 2.8% in 2009 (2008[1] : +0.8%).

Chart 2.29
Businesses: Net Financing through Banking System Loans and PDS



Source : Bank Negara Malaysia

Chart 2.30
Businesses : Loan Indicators



Source: Bank Negara Malaysia

For a brief period in the early part of the year, some businesses faced difficulty in accessing financing from the banking system and the capital market. This reflected the more cautious stance by both banks and investors in the PDS market due to the perception of the increased risk of borrowers due to the weaker economic conditions.

Recognising that access to financing is paramount to support the recovery process, the authorities intensified efforts to ensure the continued flow of financing to all segments of the economy. Towards this end, several measures were introduced by Bank Negara Malaysia and the Government, including the setting up of several special funds for the SMEs and the establishment of Danajamin Nasional Berhad to provide financial guarantees for the issuances of private debt securities and Sukuk by those companies assessed to be viable. The Bank continued to initiate active dialogues between the private sector and banking institutions to understand the development in the international and domestic environment. Avenues to seek help and redress established by the Bank and the Association of Banks in Malaysia (ABM)[2] also had a major role in enabling businesses and individuals to address enquiries relating to banking services and credit issues.

These measures yielded positive results. Financing conditions for the business sector improved from the second quarter onwards. In the third quarter, loans outstanding to businesses registered a quarterly expansion after three consecutive quarters of contraction. Higher loans were disbursed to

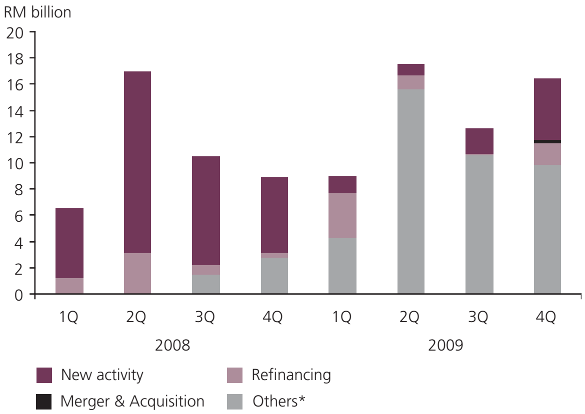
[1] The growth rate for 2008 excluded one large loan extended in 2007 for a privatisation activity

[2] Bank Negara Malaysia established the enhanced Integrated Contact Centre comprising BNM Link and BNM Telelink that includes the Complaints Management and Advisory section in July 2008. The Association of Banks in Malaysia (ABM) in collaboration with banking institutions also set up the *ABMConnect* Toll Free Channel in December 2008.

the *manufacturing, construction, wholesale and retail trade, restaurants and hotels* as well as the *agriculture* sectors. In the capital market, improved market sentiments also contributed to higher liquidity in both the PDS and equity markets.

The developed capital market provided a more diversified source of financing for the larger businesses. In 2009, fund-raising activity in the capital market was particularly active, accounting for 82.5% of total net financing raised by the business sector (including issuances of equity)

Chart 2.31
Gross PDS Issued by Purpose

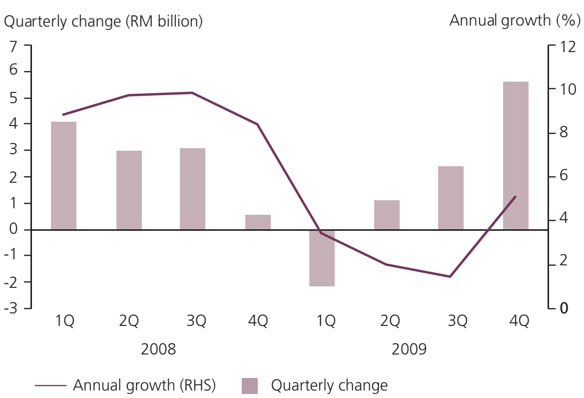


*Others include financing for working capital, equity investments and general business activities.

Note: Data excludes Cagamas bonds and issuances by non-residents.

Source: Bank Negara Malaysia

Chart 2.32
SMEs Loans Outstanding*



* Adjusted to include the reclassification of SMEs to large corporations

Source: Bank Negara Malaysia

(2008: 37.9%). In the PDS market, gross issuances increased by 30.9% in 2009, coming mainly from large government-linked companies and financial institutions. The bulk of the PDS issued during the year were to fund working capital requirements, refinance debt and for equity investments. Meanwhile, funds raised in the equity market amounted to RM26 billion (2008: RM5.5 billion). The significantly larger funds raised reflected issuances of several large rights issues and initial public offerings (IPOs).

For the SMEs and micro enterprises, financing was primarily sourced from the banking institutions and development finance institutions (DFIs). In 2009, loans outstanding to the SMEs contracted slightly. This mainly reflected the exclusion of a number of companies from the SMEs classification as they have grown beyond the definition of SME. Without such exclusion, SMEs loans outstanding would have increased by 5.1% in 2009. As at end-2009, SMEs loans outstanding accounted for 39.6% of total business loans of the banking system and development finance institutions.

Financing to SMEs was augmented by special funds established by the Bank and the Government. During the year, there were a total of three new funds set up to facilitate SMEs' access to financing. Firstly, the SME Assistance Guarantee Scheme (SAGS) was established in February 2009 with an allocation of RM2 billion to provide access to financing for viable SMEs that were adversely impacted by the economic slowdown. The fund was fully utilised and closed to applications in September 2009 after benefiting more than 9,000 SMEs from various sectors. Meanwhile, the Working Capital Guarantee Scheme (WCGS) and the Industry Restructuring Loan Guarantee Scheme (IRLGS) were both established in March 2009, with an allocation of RM5 billion each. Subsequently, in September 2009, due to the overwhelming response from borrowers, the Government reallocated RM2 billion from the IRLGS to WCGS. The WCGS, which was closed for new applications in October 2009, has benefited 5,329 companies. As at 4 March 2010, a total of RM5.4 billion in loans had been disbursed to 4,339 companies under this scheme. The IRLGS will continue to remain open until end-2010 or until the fund has been fully utilised, whichever earlier. As at 4 March 2010, 190 companies have benefited from this scheme with RM815 million worth of loans being approved.

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-2009				
Special Funds					
Fund For Food[2]	1,300.0	1,727.9	1,707.1	175.7	75.4[3]
New Entrepreneurs Fund 2	2,850.0	3,741.6	3,507.4	2,181.8	89.6
Fund for Small and Medium Industries 2	6,750.0	12,813.8	12,017.4	4,823.8	91.9
Bumiputera Entrepreneurs Project Fund[4]	300.0	946.7	903.4	54.6	82.4
Micro Enterprise Fund	200.0	79.6	71.2	66.9	38.9
Bumiputera Entrepreneurs Project Fund - Islamic	300.0	12.6	0.3	0.3	4.2
Total	**11,700.0**	**19,322.2**	**18,206.8**	**7,303.1**	**87.6**
Financial Assistance and Guarantee Schemes					
SME Assistance and Modernisation Facilities[5]	1,200.0	1,076.0	975.6	779.9	
SME Assistance Guarantee Scheme[6]	2,000.0	1,889.0	1,218.7	1,093.6	
Working Capital Guarantee Scheme[7, 8]	7,000.0	7,000.0	5,127.9	1,379.9	
Industry Restructuring Loan Guarantee Scheme[7]	3,000.0	779.7	210.6	46.3	
Total	**13,200.0**	**10,744.7**	**7,532.8**	**3,299.7**	
	Change during the year				
Special Funds					
Fund For Food[2]	-	-2.5	0.1	-80.0	
New Entrepreneurs Fund 2	-	197.1	155.9	-80.1	
Fund for Small and Medium Industries 2	-	880.0	1,123.8	-148.4	
Bumiputera Entrepreneurs Project Fund[4]	-	46.8	89.2	-24.9	
Micro Enterprise Fund	-	75.4	68.9	64.5	
Bumiputera Entrepreneurs Project Fund - Islamic	300.0	12.6	0.3	0.3	
Total	**300.0**	**1,209.4**	**1,438.1**	**-268.6**	
Financial Assistance and Guarantee Schemes					
SME Assistance and Modernisation Facilities[5]	-	-	734.6	564.1	
SME Assistance Guarantee Scheme[6]	2,000.0	1,889.0	1,218.7	1,093.6	
Working Capital Guarantee Scheme[7, 8]	7,000.0	7,000.0	5,127.9	1,379.9	
Industry Restructuring Loan Guarantee Scheme[7]	3,000.0	779.7	210.6	46.3	
Total	**12,000.0**	**9,668.7**	**7,291.8**	**3,083.9**	

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.
4 Closed and replaced by the Bumiputera Entrepreneurs Project Fund - Islamic in July 2009.
5 Schemes were established in August 2008 and has been closed down in February 2009.
6 Scheme was established in February 2009 and was closed in end December 2009. The total approved amount is RM2 billion after accounting for applications that were processed after the closing date.
7 Schemes are administered by Syarikat Jaminan Pembiayaan Perniagaan Berhad (SJPP), a special purpose vehicle managed by Prokhas Sdn Bhd. Both SJPP and Prokhas are a wholly owned company of Minister of Finance Incorporated.
8 Scheme was closed in October 2009 as the limit has been met.

Source: Bank Negara Malaysia

Monetary Policy in 2009

Monetary Policy in 2009

OVERVIEW

In 2009, monetary policy was confronted with heightened risk to growth arising from the global economic and financial crisis. The economy was severely affected by the steep decline in exports and private investment activity, as global demand contracted. Growth of the Malaysian economy turned negative for three quarters, with growth in the first quarter contracting markedly by 6.2%. Comprehensive policy measures were implemented by Bank Negara Malaysia and the Government to cushion the impact of the global recession on the domestic economy. The resilient financial system and the well-functioning monetary transmission process meant that Malaysia did not need to resort to unconventional measures, such as quantitative easing and the initiatives to address conditions of financial stress. Nevertheless, the severity of the crisis necessitated extraordinary responses in terms of the scope and size of monetary and fiscal policy measures. Cumulatively, these measures succeeded in containing the severity of the impact of the external developments. By the fourth quarter in 2009, the domestic economy had improved significantly and was on a path of firm recovery.

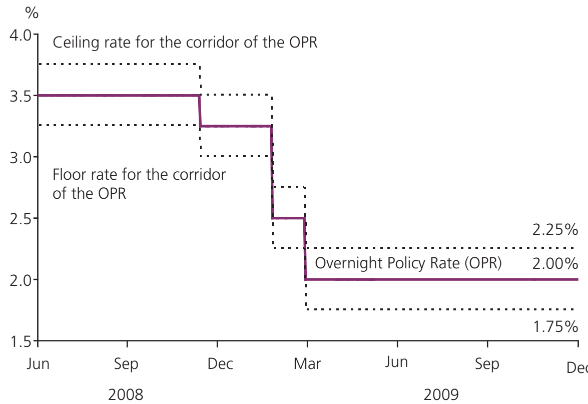
MONETARY POLICY IN 2009

Over the years, Bank Negara Malaysia has maintained a pre-emptive approach to monetary policy. Earlier in 2008, inflation was on the rise due to the sharp and significant increase in food and energy prices. The OPR, however, was left unchanged. The assessment of the Bank was that the food and energy price increases were largely supply driven. Raising interest rates under these conditions would have a limited impact in containing inflation. Importantly, it was also assessed that the Asian economies would also be affected by the spillover effects of the crisis, given the strong trade links with the developed economies. In addition, given the high percentage of food and energy in total consumption, higher prices in these categories would be contractionary on growth. While there were considerable uncertainties, the balance of risks was that growth would slow in the twelve-month period beginning mid 2008. This was the main consideration in the decision to maintain interest rates despite assertions that the Bank should have tightened monetary policy. Subsequently, as the global economy contracted, the Bank's decision to maintain interest rates was not only justified, but also enabled the initial monetary conditions to be appropriately positioned to provide support to the domestic economy.

The magnitude of the reductions in OPR and SRR were aimed at providing a highly accommodative monetary environment to prevent a fundamental economic downturn

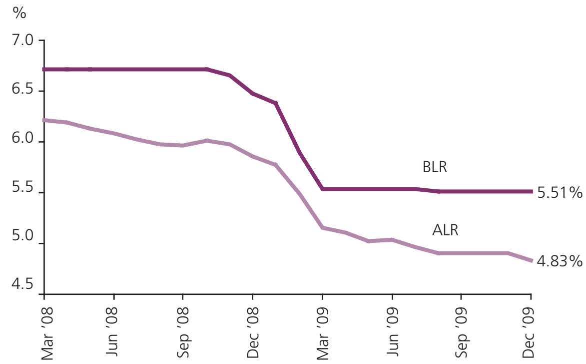
By early 2009, it was apparent that the Malaysian economy faced a severe threat of a fundamental slowdown arising from significant deterioration in global conditions. While domestic demand conditions were relatively sound, the severe collapse in exports, and the depressed economic outlook for several of Malaysia's major trade partners meant that significant policy support would be needed to prevent the economy from entering a deep and prolonged recession. With inflation decelerating, Bank Negara Malaysia frontloaded the interest rate cuts to cushion the economy from a rapidly weakening global economy. The Bank reduced its Overnight Policy Rate (OPR) by a total of 150 basis points between November 2008 and February 2009 to 2.00 percent. To ensure greater transmission from the policy rate to retail lending rates, the statutory reserve requirement (SRR) was also concurrently reduced by 300 basis points. Measures were also taken to ensure that existing borrowers benefited from the reduction in interest rate, by ensuring that monthly installments on floating rate loans were immediately reduced instead of the alternative of shortening of the repayment period. This was necessary to ensure that the reductions in interest rates led to an increase in borrowers' disposable income, which could then feed into higher domestic consumption. As variable rate loans account for a large portion of total loans in Malaysia, the increase in disposable income from lower interest costs was positive on consumption spending.

Chart 3.1
Overnight Policy Rate



Source: Bank Negara Malaysia

Chart 3.2
Base Lending Rate and Average Lending Rate of Commercial Banks



Source: Bank Negara Malaysia

With the OPR reduced to historic lows in February, the Bank left the policy rate unchanged for the rest of the year. In the Bank's assessment, the accumulated monetary policy measures were sufficient to provide support to domestic demand. Unlike countries at the epicenter of the global financial crisis, the domestic banking system was in a sound and robust position, with strong capital buffers. The strong financial system and well-functioning monetary transmission process was effective in delivering the impact of the monetary policy stimulus to the economy. Within two weeks of the last OPR adjustment in February 2009, the base lending rate (BLR) of commercial banks adjusted downwards by a cumulative 121 basis points, while new loans were also re-priced lower across the business and household sectors. As a result, the average lending rate (ALR) on new loans had declined to historic lows in 2009.

A key question for the Bank's Monetary Policy Committee (MPC) was whether further reductions in interest rates would be beneficial in the context of a high savings country like Malaysia. In addition to questions about the effectiveness of further interest rate cuts, the potential risks also had to be considered. Lower borrowing costs alone would not be a key factor in supporting demand, especially in an environment where confidence and sentiments were adversely affected by the severely weak global outlook. In economies in which the threat of deflation was significant, policymakers lowered interest rates to near zero. Bank Negara Malaysia decided against such extreme measures as there was no indication of deflationary pressures in the economy. While inflation turned negative in June 2009, this was mostly a statistical development resulting from the high base inflation in 2008. In addition, low returns for depositors and maintaining negative real interest rates for a prolonged period could have a series of negative implications. It could also create distortions that have adverse effects on the economy over the long-term. Sustained low interest rates could lead to a search for yields that may lead to the excessive rise of asset prices.

The easing of monetary policy were complemented by other measures designed to reach specific sectors of the economy

In a crisis situation, interest rate cuts by themselves are not sufficient. Several complementary measures were also introduced to reach specific sectors of the economy. Hence, in addition to easing interest rates, the Bank also introduced a number of targeted measures to ensure continued access to financing, temporary extension of safety net, safeguarding the value of wealth and real income of depositors and cushioning highly vulnerable borrowers from the full impact of the crisis.

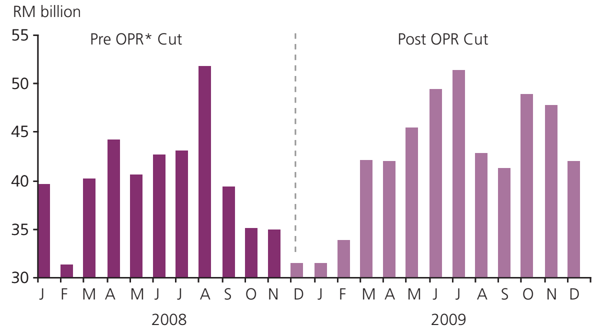
The Bank and the Government set up various special funds to ensure that viable small and medium-enterprise (SME) businesses that have been affected by the global financial crisis would continue to have access to financing. Consistent with the economic transformation objective, the Industry Restructuring Loan Guarantee Scheme was set up to assist viable enterprises in upgrading their business operations, with a long-term view of increasing efficiency and building future capacity. Danajamin Nasional Berhad was also established to provide financial guarantee insurance for investment grade companies to raise funds from the bond market.

Various dialogues between the private sector and banking institutions were initiated to allow impediments to be recognised and addressed and thus ensure the flow of credit. This alleviated concerns that lenders would be reluctant to extend credit or demand higher risk premiums. Avenues for individuals and businesses to seek help on credit issues were also established. This included the enhanced Integrated Contact Centre comprising BNMLINK and BNMTELELINK that includes the Complaints Management and Advisory Unit. In December 2008, the *ABMConnect* Toll Free Channel was set up by the Association of Banks in Malaysia (ABM), which represented a collaboration with banking institutions, to serve as a ready platform for general enquiries relating to banking and credit issues.

The reduction in cost of borrowing and measures undertaken to ensure undisrupted credit flows to the economy were successful in sustaining financing activity. Although financing growth slowed in the early part of the year, credit flows had continued despite the prevailing recessionary conditions in the domestic and external sector of the economy. There was continued flow of credit to finance domestic demand, for both businesses and households. As measures implemented by the Bank began to take effect, demand for bank loans picked up from the second quarter onwards, matched by a corresponding increase in loan approvals. In the capital market, funds raised by the private sector increased significantly, exceeding the amount raised in 2008. Given these positive developments, financing growth rebounded in the third quarter from its lowest level of 7.1% in August 2009, to register a growth rate of 8.5% by end-2009.

With the collapse of prominent financial institutions in advanced economies, and to avoid contagion to the domestic banking system, the Bank and the Ministry of Finance, announced the pre-

Chart 3.3
Loan Applications



*Overnight Policy Rate

Source: Bank Negara Malaysia

emptive measure of the blanket deposit guarantee until December 2010. In addition, Bank Negara Malaysia's liquidity facility was extended to all insurance companies and takaful operators. The blanket deposit guarantee was part of a coordinated regional response to the crisis, with both Singapore and Hong Kong also announcing the same measure simultaneously. Extending access to the liquidity facility to insurers was a precautionary move following the run on AIG in parts of the region following developments in the United States. The fact that the facility remains unutilised was an indication that the measure was successful in instilling confidence and mitigating contagion risk.

The aftermath of the Lehman Brothers collapse also witnessed a major global shortage of US dollar liquidity as investor risk aversion resulted in a pull back of funds and marked increase in deleveraging activites. This affected the ability of banks around the world to extend US dollar loans for trade activities. To facilitate international trade, the Bank provided an arrangement for firms involved in international trade by guaranteeing the availability of dollar for trade purposes.

Measures to stabilise economic activity were facilitated by orderly movements in the ringgit. Movements in ringgit throughout the year were driven mainly by external factors including global deleveraging in the first quarter, followed by renewed interest of international investors toward emerging market assets from the second quarter onwards. After depreciating in the first quarter, ringgit recorded a broad upward trend, reaching its

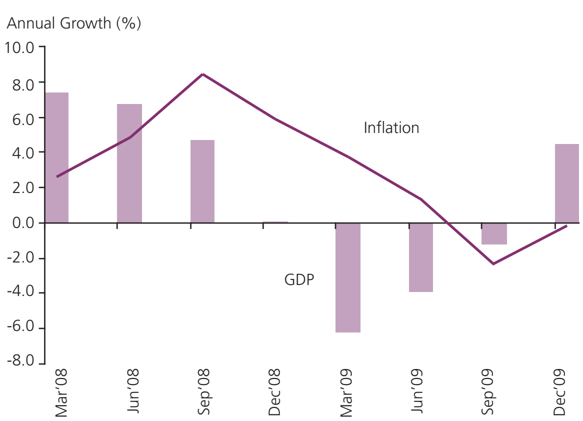
2009 peak against the US dollar at RM3.3475 on 15 October, an increase of 11.3% from its lowest level of RM3.7255 recorded in March. Ringgit adjustments and conditions in the domestic foreign exchange market remained orderly and did not adversely impact trade activity during the year.

As Malaysia is an economy with a high savings rate, and with a high level of the financialisation of these savings, it was recognised that low interest rates would reduce returns on deposits to a large segment of the economy. In order to support savers, the Bank issued Merdeka Savings Bond amounting to RM2 billion specifically targeted for segments of savers that depend on income from deposits for their livelihood. In addition, the Government issued a Sukuk Simpanan Rakyat worth RM5 billion that was also targeted at households.

A key lesson from the 1997/98 Asian Financial Crisis is the need for comprehensive and coordinated policy measures. A coordinated policy response allows for a larger and more effective impact on the economy by ensuring that the different policies reinforce each other. Accordingly, in managing the current crisis there had been a collective and coordinated response from Bank Negara Malaysia and the entire Government machinery.

The Malaysian Government responded promptly to the global economic crisis, announcing a fiscal stimulus package totaling RM7 billion on 4 November 2008 to support private spending. As the global economic outlook worsened, the Government unveiled a second stimulus package on 10 March 2009, this time amounting to RM60 billion to provide adequate support for economic activity. Balancing between the need to be decisive and bold, and the need to maintain fiscal prudence, only RM15 billion of the second stimulus package involved direct fiscal injection, with the remainder in the form of government guarantees, equity investment by Khazanah Nasional Berhad, private finance initiatives and tax incentives. The large size of the overall stimulus packages, which together amounted to 9.6% of GDP, was considered necessary to spur businesses and households at a time of heightened uncertainty. At the same time, the limited fiscal outlay was to ensure the long-term sustainability of the Government's fiscal position.

Chart 3.4
GDP and Inflation



Source: Bank Negara Malaysia

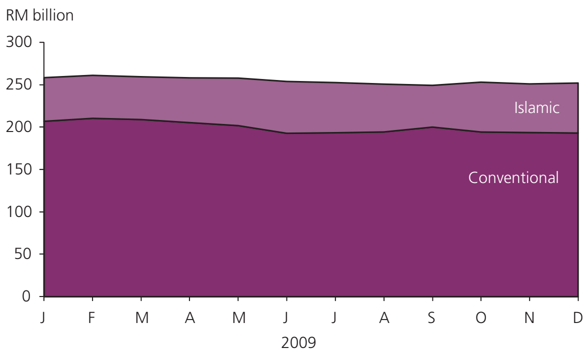
The outcome of policy measures implemented in concert was seen in the second half of 2009 as clear signs emerged that the impact of the crisis was contained. By the second half of 2009, indicators including industrial production, financing trends, external trade and conditions in the labour market, pointed towards broad-based stabilisation and improvements in the domestic economy. Business and consumer sentiments, which began to turn around in the second quarter, also improved further. The economy improved in the second half of the year, as the pace of contraction declined to -1.2% in the third quarter. By the fourth quarter, the economy expanded by 4.5%. GDP growth for the year registered a more modest decrease of 1.7% compared to the earlier projection of -4 to -5%, amid a low inflation of 0.6%.

MONETARY OPERATIONS IN 2009

Conditions in the domestic money market were generally stable in 2009. The Malaysian money market continued to operate under a surplus liquidity environment, with aggregate surplus liquidity declining only slightly from RM261 billion as at end-2008, to RM252 billion as at end-2009. The tumultuous external events proved to have a limited impact on domestic money markets. The money market continued to function smoothly and experienced minimal volatility.

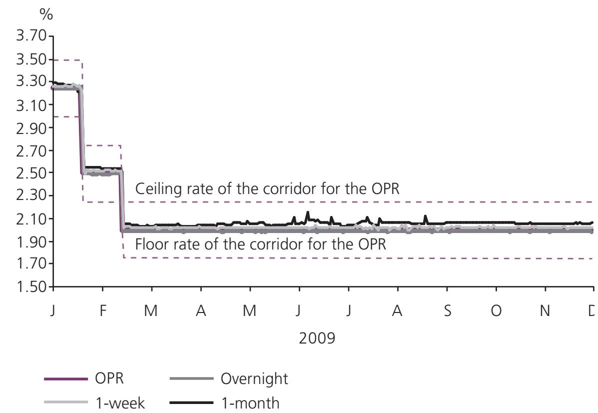
During the year, the average overnight interbank rate (AOIR) was stable and closely tracked the OPR despite the higher uncertainty and general market volatility earlier during the year. The Bank continued to use a wide range of monetary instruments for managing monetary operations and maintained the AOIR within the policy corridor of ± 25 bps.

Chart 3.5
Outstanding Liquidity Placed with Bank Negara Malaysia (RM252 billion, as at 31 Dec 2009)



Source: Bank Negara Malaysia

Chart 3.6
OPR and Interbank rates



Source: Bank Negara Malaysia

In early 2009, the domestic money market continued to be affected by the deleveraging activity of international financial institutions. Short-term portfolio outflows were recorded in the first quarter, as foreign investors reduced their holdings of domestic assets. This caused domestic liquidity to contract slightly, with the surplus liquidity placed by the banking system with Bank Negara Malaysia decreasing from RM261 billion to RM256 billion, between December 2008 and March 2009.

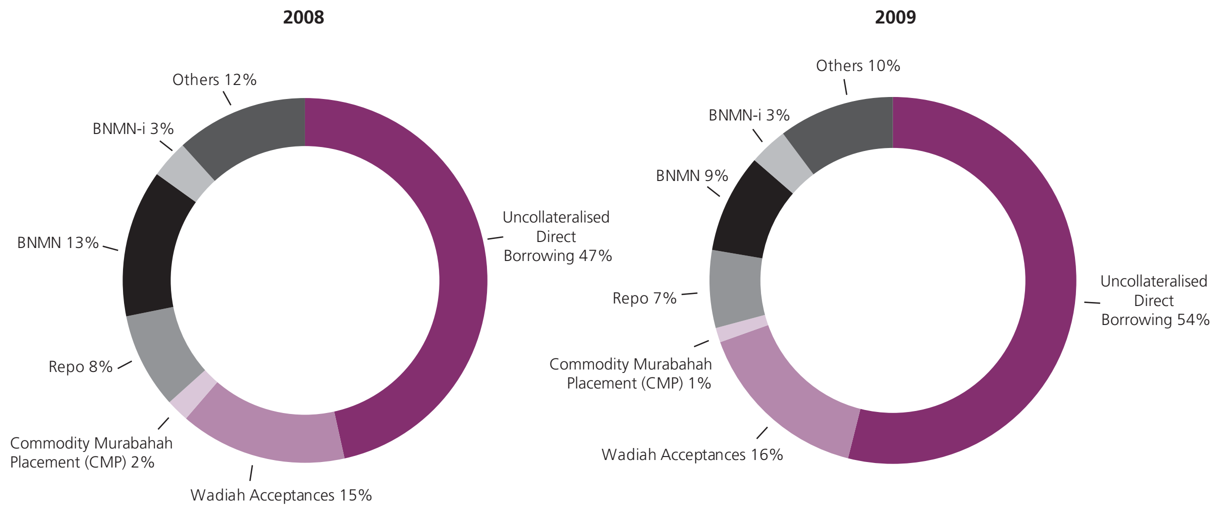
To compensate for the outflows following foreign selling of domestic assets, Bank Negara Malaysia released some of the excess liquidity kept with the Bank. In this respect, the large net interbank placements with the Bank acted as a liquidity buffer for the banking system. While the size of the surplus liquidity was reduced by the outflows, liquidity in the banking system, nonetheless, remained in surplus. This was evidenced by the loan-deposit ratio of the banking system remaining at modest levels, ranging from 72.2% in January to 77.5% in March 2009. At the institution level, all banks operated from a position of surplus liquidity. The ample liquidity condition was also supported by Bank Negara Malaysia's decision to reduce the required reserves that banks hold against eligible liabilities from 4% to 1%. While the main motivation for reducing the SRR was to bring down the cost of intermediation, lowering the SRR also increased the liquidity available to banks.

Interest rates in the interbank market remained orderly. The average overnight interbank rate (AOIR) traded within a narrow range of 1 basis point above and below the OPR. Following the reduction in the OPR on the 21 of January to 2.50%, the AOIR decreased and stabilised at a lower range of 2.49% - 2.51% during the period 22 January – 24 February. With the further reduction in the OPR on 24 February to 2.00%, the AOIR decreased accordingly and stabilised at the lower range of 1.99% - 2.01%.

From the second quarter onwards, the global economic and financial environment began to improve. Investors' risk appetites for financial assets from emerging economies increased and led to net portfolio inflows into emerging markets, including Malaysia. Conditions in the money market during this period returned to normal. Monetary operations of the Bank were focused on draining surplus liquidity in the banking system by utilising various monetary instruments.

In terms of monetary instruments, uncollateralised direct borrowings and Al-Wadiah acceptances remained as the main monetary instruments, sterilising 70% of the surplus liquidity in the banking system. While the maturities of the borrowings through direct borrowings and Al-Wadiah acceptances ranged from overnight up to 3 months, their average borrowing maturities were shorter, ranging between 7 to 25 days. The share of direct borrowings increased from 47% in 2008 to 54% in 2009, following the reduction in the level of the SRR.

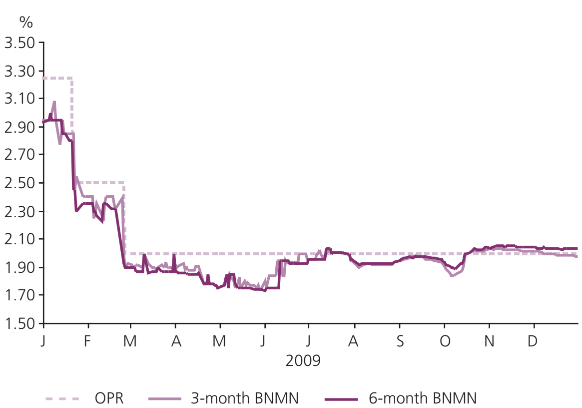
Chart 3.7
Breakdown of Outstanding Monetary Policy Instruments



Source: Bank Negara Malaysia

Bank Negara Monetary Notes (BNMN for conventional and BNMN-i for Islamic money markets) were also utilised significantly, accounting for 12% of total monetary instruments. The BNMN/BNMN-i remains an important instrument for the Bank as a steady issuance of the papers helps to promote secondary market liquidity. In addition, BNMN/BNMN-i provides a cost effective means of sterilising excess liquidity. BNMN/BNMN-i yields sometimes traded below OPR, especially during periods of expectations for interest rates cut as was the case during the first quarter of 2009, and due to the higher demand for short-term securities from non-resident investors in the subsequent quarters.

Chart 3.8
BNMN Yields and OPR



Source: Bank Negara Malaysia

In 2009, conventional monetary operations accounted for 77% of the total operations, while Islamic monetary operations accounted for the remaining 23%. The scale of Islamic monetary operations was in line with the size of the Islamic banking system in Malaysia which has increased to 19.6% of total assets of the banking system as at end-2009 (17.4% as at end-2008).

The Bank also undertook measures to improve operational efficiency in the money market. On 2 July 2009, the Bank introduced a BNMN based on the Murabahah concept (BNMN-Murabahah), to gradually replace the issuance of BNMN-i based on Bai Al-Inah concept. Issuance of BNMN-Murabahah is based on a widely accepted murabahah contract, which essentially is a certificate of indebtedness arising from a deferred mark-up sale transaction of an asset, normally commodities (e.g. crude palm oil). As murabahah is an acceptable concept by both resident and non-resident investors, it has expanded the investor base and has consequently encouraged the secondary market in the Islamic money market.

Monetary Policy Process under the Central Bank of Malaysia Act 2009

The Central Bank of Malaysia Act 2009 (``the Act´´), which came into force on 25 November 2009, formally institutionalises the monetary policy formulation procedures that have been established since the beginning of the decade.

The Act stipulates that monetary policy shall be autonomously formulated and implemented by Bank Negara Malaysia (``the Bank´´). The objective of monetary policy is also articulated with greater clarity – "In promoting monetary stability, the Bank shall pursue a monetary policy which serves the interests of the country with the primary objective of maintaining price stability giving due regard to the developments in the economy."[1]

The Act also formally and legally recognises the Monetary Policy Committee (MPC) as the body responsible for formulating monetary policy and the policies for the conduct of monetary operations. The MPC consists of 7 to 11 members, with the Governor being the Chairman of the Committee. The Governor and Deputy Governors remain as members of the MPC for so long as they hold office. Members, other than the Governor and the Deputy Governors, are appointed by the Bank's Board of Directors from amongst senior officials at the Bank with relevant expertise, on the recommendation of the Board Governance Committee. Meanwhile, the Board Governance Committee may recommend external members to the Minister of Finance for their appointment to the MPC. The appointment term of the members is 3 years, and the eligibility for reappointment is subject to the assessment of the members' performance by the Board Governance Committee. The Act also provides extensive safeguards in terms of membership of the MPC. Members of the MPC must be persons of probity, competence and sound judgment with relevant expertise and experience. The governance of the MPC meetings and the accountability of the members are guided by the MPC by-laws, which have been approved by the Board of Directors of the Bank. The current MPC members are:

Tan Sri Dr. Zeti Akhtar Aziz	(Governor)
Dato' Ooi Sang Kuang	(Deputy Governor)
Dato' Zamani bin Abdul Ghani	(Deputy Governor)
Dato' Mohd Razif bin Abd. Kadir	(Deputy Governor)
Dato' Muhammad bin Ibrahim	(Assistant Governor)
Puan Nor Shamsiah binti Mohd Yunus	(Assistant Governor)
Dr. Sukhdave Singh	(Assistant Governor)
Puan Norzila Abdul Aziz	(Assistant Governor)

The MPC is required to hold six regularly scheduled meetings during a year, and additional meetings may be convened if necessary.[2] At the MPC meetings, members review economic and financial conditions and assess the risks to achieve the long-run goals of price stability and sustainable economic growth, before deliberating and reaching the decision on the appropriate stance of monetary policy. The Committee adopts a collegial approach to decision-making. Therefore, the Governor, as Chairman, has a crucial role in leading the discussion and deliberation process, as well as in building a consensus decision amongst members. A Monetary Policy Statement[3] is released after each MPC meeting to announce the monetary policy decision. The MPS also provides an assessment of the prospects for the economy and inflation, as well as other issues relevant to the policy decision.

1 Section 22 (1) of the Central Bank of Malaysia Act of 2009
2 The schedule for the six meetings is published together with the final Monetary Policy Statement of the preceding year.
3 The Monetary Policy Statement can be found on the Bank's website at www.bnm.gov.my

Outlook and Policy

Outlook and Policy

INTERNATIONAL ECONOMIC OUTLOOK IN 2010

Recovery in the global economy, which commenced in the second half of 2009, is expected to remain gradual and uneven in 2010 as economies emerge from the worst post-World War II recession. The strength and pace of the recovery will vary considerably across the economies, depending on the extent of the region-specific structural problems in the aftermath of the global financial crisis. The advanced economies are expected to record modest growth in 2010 given the prevailing high unemployment, the ongoing deleveraging process and the weak financial systems that continue to restrain lending activity to the real sector. The Asian economies are, however, expected to continue to lead the global recovery as sources of growth become broad-based, supported by the further strengthening of both domestic demand and external demand, amid improved intra-regional trade, especially with PR China.

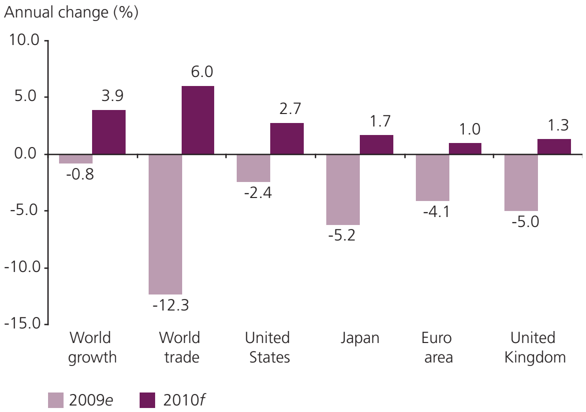
Recovery in the global economy is expected to remain gradual and uneven in 2010, with the Asian economies leading growth

A distinct feature of the ongoing global recovery process, particularly in the advanced economies, is the pervasiveness of the policy support put in place since early last year. The sustainability of recovery in the advanced economies is still dependent on the stimulus and the restoration of financial intermediation in the credit market. However, some of the quantitative easing is expected to be withdrawn beginning early 2010. As the fiscal stimulus wears off towards year-end, the sustainability of the recovery in the advanced economies will need to rely on the resumption of private sector activity. However, given the likelihood of persistently high unemployment, weak private sector balance sheets and fragile financial systems, the prospect is for a very gradual recovery in private sector demand, which will in turn affect the pace of economic recovery.

Notwithstanding the continued improving conditions in the international financial markets, credit conditions particularly in the advanced economies are likely to remain restrictive due to constraints faced by the financial institutions as they continue to grapple with weak balance sheets, tighter capital standards and regulatory changes from the ongoing reforms in the financial system. Hence, bank lending to the economy, in particular to households and small businesses, is likely to remain weak. On the international front, given the less promising prospects in advanced economies and improving investors' risk appetite for high-yielding assets, the magnitude and direction of capital flows to emerging economies with better prospects would result in more volatile capital flows to such economies.

In the **US**, the prospect is for a continued but gradual recovery in economic activity, underpinned by the considerable policy stimuli and gradual revival in private sector demand. The fiscal stimulus, which supported growth strongly in 2009, will provide further impetus to growth this year, especially through tax benefits and infrastructure spending. More than half of the USD787 billion fiscal stimulus package is targeted to be spent in 2010. There will, however, be a gradual withdrawal of monetary stimulus following the expiry of several of the Federal Reserve's liquidity and asset purchase programmes starting early this year. Nonetheless, the net impact of these policies on the recovery process is expected to remain positive, especially through their influence on private sector demand. Private consumption is expected to expand, albeit at a modest pace, following the positive wealth effect from the rise in equity markets and stabilising house prices. Households are also expected to gain from tax benefits for the housing sector. Private consumption will, however, be constrained by continued weakness in the labour market and persistently tight credit conditions. Similarly, private investment is also expected to record anaemic growth during the year due to prevailing excess capacity and very low utilisation rates. Residential investment is expected to be supported by ongoing government policies in the form of lower mortgage rates and tax credit relief. Overall, the US recovery process will continue to be driven by policy stimulus amidst a very gradual recovery in private sector demand.

Chart 4.1
World Growth, World Trade and Growth in Major Advanced Economies (2009-2010)



e Estimate
f Forecast

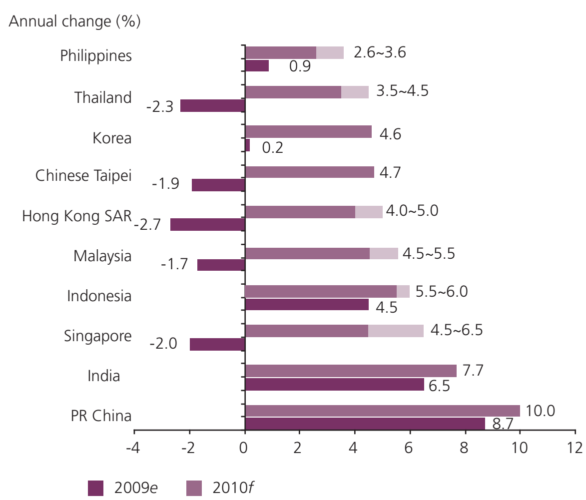
Source: International Monetary Fund and National Authorities

Economic activity in the **euro area** is projected to improve in 2010 but growth will remain modest and below potential. While fiscal stimulus will be less expansionary and fiscal consolidation in a number of countries in the euro area is expected to commence, it will still be a factor driving some growth. At the same time, private sector demand is expected to show a gradual recovery, but remain restrained by a challenging environment of persistent high unemployment and weak financial sectors. Meanwhile, in the **UK**, economic recovery will be supported by the monetary stimulus as well as external demand following the depreciation of the pound sterling. Nonetheless, domestic demand will remain weak due to the restrictive credit conditions and planned fiscal consolidation. For **Japan**, an economy that is highly dependent on trade, the recovery in exports, especially to the Asian region, in particular PR China, is expected to remain the key driver of economic growth in 2010. However, the recovery is expected to be modest, with domestic demand likely to be constrained by weak labour market conditions and subdued capital expenditure plans. Moreover, deflation is expected to persist in the economy, further weighing down on domestic demand, in particular private consumption. Given this scenario, monetary and fiscal policies are expected to remain expansionary to support growth.

The gradual recovery in the advanced economies, coupled with strong demand from the emerging economies, will support the resumption of **global trade** in 2010. Notably, the composition of global trade will shift from the advanced economies to the emerging economies, particularly Asia, as domestic demand in the region strengthens further. The changing pattern of global trade is likely to shift the global flows of foreign direct investment, as multinational companies become more region-specific in managing their global production and investment networks to take advantage of the favourable growth prospects in the emerging economies.

In line with the anticipated improvements in the global economy and trade, the **Asian economies** are poised for a more robust growth in 2010. As a major anchor of growth for the region in 2009, **PR China** is expected to continue to support intra-regional trade through the sustained expansion of its domestic demand. Besides the continued broad-based improvements in external demand for the region, domestic demand conditions in the regional economies are also expected to strengthen further. Private consumption is likely to be bolstered by better employment prospects, while private investment can be expected to rebound in view of higher capacity utilisation. This will be further reinforced by the continued implementation of fiscal stimulus packages, especially in the area of infrastructure spending.

Chart 4.2
Regional Economies: Real GDP Growth



e Estimate
f Forecast

Source: International Monetary Fund and National Authorities

Global inflation is expected to rise in 2010 in tandem with the recovery of the global economy and higher commodity prices. Prices of oil and other commodities are expected to be higher, but not to the levels seen in early 2008, reflecting more underlying real demand conditions, particularly in the emerging economies. To some extent, the anticipated rise in commodity prices will also be driven by market expectations of a recovery in global demand as well as the excess liquidity in the global financial system. However, further increases in the prices of commodities are likely to be limited by the availability of spare capacity in the production of most commodities and in some cases by large stock of inventories.

Headline inflation in the advanced economies is expected to rise to 1.3% in 2010 from a record low of 0.1% in 2009. Meanwhile, inflation in emerging and developing economies is expected to rise to 6.2% in 2010 from 5.2% in 2009[1]. Against this backdrop, these central banks are expected to gradually exit from the very low interest rate regime in addition to the reversal of quantitative easing in the advanced economies. The speed at which central banks will exit will take into consideration a broad range of factors, ranging from conditions for the sustainability of recovery and the outlook for inflation.

Several downside **risks** remain in the outlook of the global economy. The timing and magnitude of the withdrawal of the stimulus measures could pose considerable risk to the growth and inflation outlook. If there was a significant premature withdrawal of these measures, it could increase the risk of a double-dip recession, particularly in the advanced economies. If the measures are, however, withdrawn too late, this could lead to financial imbalances and heightened inflationary pressures, and in some cases, unsustainable asset price inflation. Another major risk is the fiscal health of the advanced economies that have embarked on large fiscal stimuli and financial rescue packages. This is reflected in increasing concerns on sovereign risk, particularly in Europe. If these economies are unable to outline a clear strategy to return to a sustainable fiscal position, markets would impose high risk premiums on these economies, resulting in sharper fiscal consolidations that could harm the recovery process. The advanced economies also continue to face significant challenges from their fragile financial system and structural unemployment. In the case of emerging economies, the positive growth differentials could attract large capital inflows and pose complications in the conduct of monetary policy and managing exchange rate volatilities.

[1] IMF World Economic Outlook Update, January 2010

MALAYSIAN ECONOMY IN 2010

The Malaysian economy is projected to grow by 4.5% to 5.5% in 2010, underpinned by strengthening domestic demand and an improving external environment. While the public sector will remain supportive, growth is expected to be driven by greater private sector activity and robust external demand from the regional countries. The underlying strong macroeconomic fundamentals, the healthy private sector financial position and the strong financial system will provide support to a private sector-led recovery. A supportive monetary environment, including continued access to competitive financing will remain in place to foster recovery in the private sector activity.

Real GDP is expected to expand by 4.5% to 5.5% in 2010, supported by strengthening domestic demand and an improving external environment

The main contribution to growth in 2010 would come from the expected strengthening in domestic demand, driven mainly by the private sector. Favourable domestic conditions, including the improvements in the labour market, rising disposable incomes and sustained consumer confidence, will support the further expansion in private consumption. In line with strengthening external demand and increasing domestic activity, private investment is expected to gradually recover in 2010. In addition, higher capital spending by the NFPEs and the accelerated implementation of the remaining projects under the second stimulus package, will further reinforce domestic demand. The recovery in the

Potential Output of the Malaysian Economy

Potential output is the trend level of output that is consistent with the aggregate productive capacity of an economy. It traces the sustainable growth path of the economy and is primarily determined by the expansion and non-inflationary utilisation of the available physical capital and labour force, as well as total factor productivity (TFP) growth. TFP growth captures productivity increases arising from improvements in the utilisation of factor inputs due to technological progress and overall economic efficiency. The output gap is the difference between the levels of actual output and potential output. It is a measure of the cyclical deviation from the non-inflationary trend of output, and thus provides an assessment of the position of an economy in the economic cycle.

Amidst a challenging global environment, the latest estimates indicate that the growth rate of potential output of the Malaysian economy moderated to 2.5% in 2009, the slowest pace since the Asian financial crisis. This was mainly due to the decline in investment activity and moderation of TFP growth, consistent with the experience during previous economic downturns. Given a sharper decline in actual gross domestic output (GDP), the output gap[1] was a negative 1.4% of potential output, indicating that the economy was operating below its potential in 2009.

However, with the expected recovery of the Malaysian economy going forward, driven by the strengthening of domestic activity and an improving external environment, the output gap is projected to narrow in 2010, and potential output is expected to return to its trend growth of about 5% over the medium term with the expected recovery in investment and continued improvement in productivity.

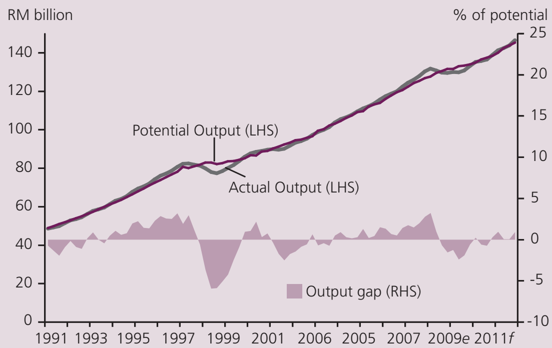
Table 1
Actual Real GDP and Potential Output

Period	Actual	Potential	Investment	Labour	Gap
	Annual change (%)				% of potential output
1993-1999	6.5	6.5	4.3	4.1	0.1
2000	8.9	4.2	26.0	4.4	1.1
2001	0.5	4.6	-2.1	1.5	-1.6
2002	5.3	4.0	0.6	1.9	-0.6
2003	5.8	6.1	2.8	3.6	-0.4
2004	6.8	5.5	3.6	1.0	0.4
2005	5.3	5.0	5.0	0.6	0.8
2006	5.8	5.6	7.5	2.1	1.0
2007	6.2	5.2	9.6	2.5	2.1
2008	4.6	4.0	0.8	1.3	0.7
2009*e*	-1.7	2.5	-5.5	2.7	-1.4

e Estimate

Source: Department of Statistics, Malaysia and Bank Negara Malaysia estimates

Chart 1
Actual and Potential GDP



e Estimate
f Forecast

Chart 2
Factor contributions and TFP growth
Shift from a factor-driven to a productivity-driven economy

e Estimate
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 economy will provide a further impetus to growth in 2010, particularly from the more robust expansion in the regional economies. Given the relatively large external sector in the economy, the strengthening of external demand will have positive spill-over effects on the broader economy, in terms of employment, production and overall sentiments, thus supporting greater private consumption and investment.

From the supply side perspective, most economic sectors are expected to record better performance in 2010, supported by strengthening domestic demand and a further improvement in external demand. The manufacturing and mining sectors are expected to record positive growth as external demand for major products such as electronics, crude oil and natural gas, recover. The services sector remains the key contributor to overall GDP growth, with growth expected to be broad-based. Both the trade and manufacturing related sub-sectors and the domestic-oriented sub-sectors are expected to improve amid the recovery in both global and domestic demand. The agriculture sector is also projected to register higher growth as demand from the major export markets for industrial crops improves with better economic prospects in 2010. Meanwhile, the construction sector is expected to sustain growth, benefiting from the continued implementation of the remaining projects under the second stimulus package and the Ninth Malaysia Plan.

Labour market conditions are projected to improve further in 2010, with the unemployment rate expected to decline to 3.6% of the labour force. Based on a survey conducted by Bank Negara Malaysia, most firms in the manufacturing, services and construction sectors plan to increase employment and provide a higher salary increment in 2010, in line with the expected recovery in global and domestic economic activity.

Headline inflation is expected to remain modest at an average of 2% to 2.5% in 2010. The price increase reflects the improving economic conditions and the possible adjustments to the administered prices following the Government's plan to revise the subsidies for petroleum products as well as to review the existing subsidies on other essential items.

On the external front, the current account surplus is projected to be lower at 14.3% of GNI in 2010. The lower current account surplus reflects the lower trade surplus, higher income account deficit, sustained current transfer outflows as well as a small services account deficit. Gross exports are projected to expand further in 2010, in line with the stronger external demand and higher commodity prices. However, the trade surplus is expected to be lower as higher exports will be partly offset by the expansion in gross imports, in tandem with the recovery in the manufacturing sector and the strengthening of domestic demand. On the financial account, foreign direct investment inflows and direct investment abroad by Malaysian companies are likely to increase given the improving global and domestic economic conditions.

The projected growth of the Malaysian economy of between 4.5% and 5.5% in 2010 is based on the expectation of a gradual and uneven global economic recovery. It is recognised that the global economy is still facing several downside risks. These risks, mainly in the advanced economies, include the effect on recovery once fiscal spending begins to diminish, the still weak and fragile financial system, the continued de-leveraging process amongst the private sector and the fiscal stress in some large advanced economies pose considerable uncertainties to the outlook for the global economy. Under these circumstances, domestic demand will be a key factor in driving growth in 2010. In this environment, policies will remain supportive of growth, in particular to ensure that private sector activity strengthens further and that the recovery is firmly established.

In addition to ensuring the timely implementation of projects, the Government has announced several measures to revive private investment, including the liberalisation of the economy, the privatisation of Government-owned corporations, the provision of incentives to high growth sectors and further improvements in the Government's delivery system. On the monetary front, monetary policy will remain accommodative while attention will continue to focus on ensuring that the private sector, in particular the small and medium enterprises, have access to financing. At the same time, there will be heightened vigilance to ensure that financial imbalances do not develop in the economy, which would threaten macroeconomic stability and the sustainability of the economic recovery. The strong economic and financial fundamentals of the Malaysian economy place the domestic economy in a better position for a stronger recovery as the global conditions improve further.

Domestic Demand Conditions

Domestic demand is projected to expand by 3.2% in 2010 as private sector activity strengthens in line with the resumption of global economic growth. The private sector is expected to be the main driver of domestic demand as the Government consolidates its expenditure in 2010.

Domestic demand will record higher growth in 2010, driven mainly by private spending as the Government consolidates

Favourable domestic conditions, in terms of an accommodative monetary policy, continued access to financing and improved labour market conditions, will help to support the further expansion of household consumption, while private sector capital spending is projected to increase gradually during the year. In addition, higher capital spending by the NFPEs will provide a further boost to domestic demand.

Private consumption is projected to increase by 3.8% in 2010. The higher expansion in consumer spending will be supported largely by improvements in the labour market, a steady increase in disposable income and sustained consumer confidence. Employment prospects will be more favourable with stronger labour demand in various sectors of the economy, in line with the recovery in economic activity. Consequently, the average private sector salary is expected to increase by 4.1% while the unemployment rate is projected to be lower at 3.6% of the labour force. The rise in income levels following the gradual recovery of the export and manufacturing sectors will benefit almost one third of the labour force in the domestic economy, and will support higher consumption spending. In addition, households in the rural area are expected to enjoy favourable income growth as commodity prices are expected to remain firm in 2010.

In view of the recovery in economic activity and improved labour market conditions, consumer confidence is likely to be sustained in 2010. Other factors providing support to private consumption growth include continued access to credit with accommodative interest rates and a relatively low inflation environment. The balance sheet of households is expected to remain strong as reflected

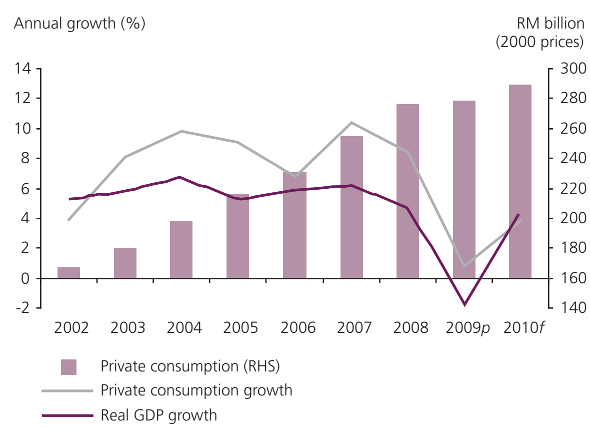
Table 4.1
Real GDP by Expenditure (2000=100)

	2009*p*	2010*f*	2009*p*	2010*f*
	Annual change (%)		Contribution to real GDP growth (percentage point)	
Domestic Demand[1]	**-0.4**	**3.2**	**-0.3**	**2.8**
Private sector expenditure	-3.4	3.3	-2.2	2.1
Consumption	0.8	3.8	0.4	2.0
Investment	-21.8	0.7	-2.6	0.1
Public sector expenditure	7.7	2.7	1.9	0.7
Consumption	3.7	-2.7	0.5	-0.4
Investment	12.9	9.3	1.3	1.1
Change in stocks			**-2.5**	**4.5**
Net exports of goods and services	**8.4**	**-18.6**	**1.1**	**-2.7**
Exports	-10.1	7.7	-12.0	8.3
Imports	-12.5	11.7	-13.1	11.0
Real Gross Domestic Product (GDP)	**-1.7**	**4.5~5.5**	**-1.7**	**4.5~5.5**

[1] Excluding stocks
p Preliminary
f Forecast
Note: Figures may not necessarily add up due to rounding

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

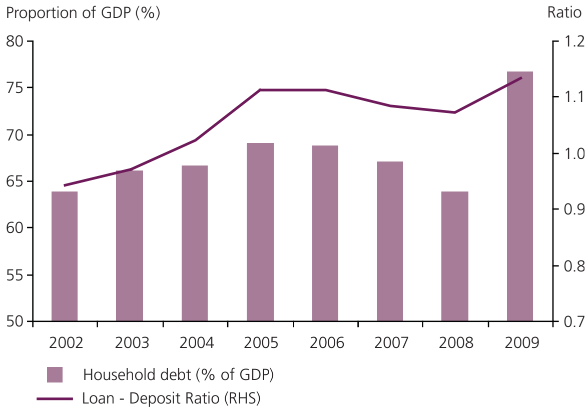
Chart 4.3
Real GDP and Private Consumption



p Preliminary
f Forecast

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

Chart 4.4
Household Debt Indicators



Source: Bank Negara Malaysia

by the stable debt levels of households and low level of non-performing loans. In addition, the continued implementation of projects from the second economic stimulus package is expected to also benefit the household sector.

Private investment is expected to register a marginal growth of 0.7% in 2010. Capital spending by businesses is likely to expand gradually from the second half of 2010, in line with the strengthening of domestic and external demand amid improving global economic conditions. The modest recovery in private investment will be supported by higher activity from the manufacturing sector. Furthermore, a faster improvement in capacity utilisation since the second half of 2009, supported by the increase in manufacturing production will encourage firms to embark on capacity expansion. The rebound in business optimism due to the improvement in external demand and increasing domestic economic activity will also encourage firms to resume investment projects that have been deferred.

In the services sector, the consumer-oriented business segments will continue to expand in view of the higher consumption activity during the year. Firms in the wholesale and retail trade industry are projected to expand their operations through the establishment of new outlets. Investment in the communications sector will be higher as companies intensify the network upgrading exercise to widen broadband service coverage. Meanwhile, investment in the transportation sector will be supported mainly by capacity expansion in air travel services. Capital spending in the mining sector is also anticipated to increase, supported by an expansion in upstream oil and gas production capacity as well as additional development expenditure for new discoveries located offshore in Peninsular Malaysia and Sarawak. In addition, capital expenditure in the construction sector is likely to benefit from the ongoing Ninth Malaysia Plan (9MP) civil engineering projects as well as continued implementation of the second stimulus package.

Although expenditure on emoluments will be higher, **public consumption** is projected to decline by 2.7% in 2010 as expenditure on supplies and services is reduced. This is in line with the Government's policy to be more efficient in its spending, without affecting the effective delivery of Government services.

Public investment is expected to expand by 9.3% in 2010, mainly on account of higher capital spending by NFPEs. Government development expenditure during the year will continue to be channelled towards improving the economic and social sectors of the economy. Capital outlay in the economic services sector will mainly be for providing transport and industrial infrastructure, improving public utilities and agricultural productivity as well as for enhancing rural development. The implementation of various projects under the 9MP as well as the second stimulus package will also be accelerated during the year. Of significance, Government direct spending consisting of RM5 billion worth of projects from the second stimulus package will be implemented in 2010. In the social services sector, a large proportion of the allocation will be utilised to improve the provision of essential public services such as education and health care, and the development of low-cost housing and quarters for civil servants.

Besides the large capital expenditure in the upstream oil and gas sector, higher investment by NFPEs is projected in the areas of transport, communication and utilities. Investment in the communication and utilities sectors will focus on upgrading the broadband network and improving power supply respectively. In the transportation sector, higher capital outlay has been committed to the implementation of rail expansion projects in 2010.

Table 4.2
Real GDP by Sector (2000=100)

	2009*p*	2010*f*
	Annual change (%)	
Agriculture	0.4	3.1
Mining & quarrying	-3.8	2.5
Manufacturing	-9.3	6.5
Construction	5.7	3.7
Services	2.6	4.9
Real Gross Domestic Product (GDP)	**-1.7**	**4.5~5.5**

p Preliminary
f Forecast

Source: Department of Statistics, Malaysia
Bank Negara Malaysia

Sectoral Outlook

Better performance is expected in most economic sectors as domestic demand strengthens and external demand continues to improve in 2010. The manufacturing and mining sectors are expected to return to growth as external demand for major products such as electronics, crude oil and natural gas recovers. The recovery in external conditions will also raise demand for trade-related services, contributing favourably to the services sector. In addition, the revival of domestic-oriented activity, which has been on a firm recovery path since the second half of 2009, will further enhance growth in all sectors. Growth will be underpinned by strengthening domestic demand, particularly private consumption, amidst continued policy support. Furthermore, the anticipated improvement in labour market conditions, together with higher business and consumer confidence, will provide incentives for private sector activity in the domestic-dependent sectors. Meanwhile, the construction sector is expected to sustain its growth, benefiting from the continued implementation of the various projects under the second stimulus package and the Ninth Malaysia Plan.

Broad-based recovery is expected in 2010 with improved performance in most sectors

The **services** sector is projected to register a higher growth of 4.9% in 2010, and will remain the key contributor to overall GDP growth. Growth will be broad-based, with most sub-sectors recording better performance compared to 2009. The trade and manufacturing-related sub-sectors, which were adversely affected by the economic downturn in 2009, are expected to improve, in line with the anticipated recovery in the global economy. Meanwhile, the more domestic-oriented sub-sectors are expected to record higher growth, benefiting mainly from strengthening domestic demand.

Within the services sector, the **finance and insurance** sub-sector is expected to register higher growth, mainly supported by the finance segment, which would benefit from increased bank lending and higher fee income as the economic recovery gathers momentum. In the insurance segment, the improvements in salaries and wages and enhanced financial literacy would contribute to increased demand for life insurance products, while the anticipated increase in the sales of motor vehicles would benefit the general insurance business.

After being adversely affected by the economic downturn in 2009, the **transport and storage** sub-sector is projected to return to positive growth in 2010. Growth will emanate from higher demand for cargo-related transportation services, following the anticipated improvement in trade and manufacturing-related activities. Growth will be further supported by improved demand in the passenger segment, in line with the expected higher tourist arrivals and improvement in domestic tourism activity. Similarly, the **utilities** sub-sector, which weakened considerably in 2009, is expected to expand favourably in 2010. Growth will be contributed by increased demand for electricity from the industrial users, in line with the improvement in manufacturing activity, as well as steady demand from the commercial and household sectors.

The services sub-sectors that are dependent on domestic consumption, such as the **wholesale and retail trade** and **accommodation and restaurant** sub-sectors, are projected to register enhanced growth rates. The anticipated increase in tourist arrivals will also contribute favourably to these sub-sectors. Outlook for the **communication** sub-sector is also positive, spurred by increasing demand for mobile data and broadband services. Intense competition among the service providers, commercial roll-out of the high speed broadband project in selected urban areas and continued expansion of WiMAX services will further contribute to the growth of the sub-sector.

The **manufacturing** sector is poised for strong growth in 2010, based on the observed momentum of recovery since the end of 2009. Broad-based expansion is expected across all clusters, reflecting improved external demand and strengthening domestic demand. The electronics and electrical (E&E) cluster is projected to turn around with the pick-up in global demand for electronics, particularly with the return of corporate IT spending, where upgrade and replacement of software and equipment were held back during the global downturn. Likewise, growth in the primary-related cluster will be driven by external demand and higher commodity prices. The chemical industry is expected to improve in tandem with the E&E, automotive and household markets, while demand for hygiene and medical products will continue to support the rubber products industry. Meanwhile, the consumer-related cluster is expected to move in line with the strengthening of domestic demand, particularly private consumption. Also, the performance of the construction-related cluster will be influenced by anticipated higher domestic construction activity and infrastructure projects in the region.

The **agriculture** sector is expected to register a higher growth of 3.1% as demand from major export markets for industrial crops, especially palm oil and rubber, improves with better economic prospects in 2010. In addition, the reduction in import duties on rubber by the PR of China as of 1 January 2010 will further boost its demand for the commodity. In terms of production, higher palm oil output is expected during the year following the recovery in yield of fresh fruit bunches and an increase in planted area ready for production. In the case of rubber, besides a continuing increase in productivity from areas replanted with high yielding clones, higher rubber prices since the second half of 2009 will continue to encourage increased tapping.

The **mining** sector is projected to expand by 2.5%, reflecting higher output of both crude oil and natural gas following the recovery in demand. The increase in LNG output will also partly reflect the first full-year of shipment under an export contract with PR China.

The **construction** sector is expected to maintain a growth of 3.7% in 2010. The civil engineering segment will be supported by the continued implementation of projects under the second stimulus package. Furthermore, apart from additional progress on projects under implementation, several other major projects identified under the Ninth Malaysia Plan are also expected to take off during the year. Meanwhile, improved business and consumer sentiments and continued access to financing will support expansion in both the residential and non-residential sub-sectors.

Balance of Payments

On the external front, improvements in exports and capital inflows, which were evident in the second half of 2009, are expected to continue in 2010 as the global economic recovery gathers strength. The expected stronger external demand, particularly from the region, and higher commodity prices is projected to contribute to a further expansion in gross exports in 2010. However, the trade surplus is expected to be lower as imports are projected to expand faster than exports. While imports of intermediate goods will increase in tandem with the expansion in manufactured exports, the stronger recovery in the domestic economy will also lead to higher imports of consumption and capital goods. The lower trade surplus, together with a higher income account deficit, sustained current transfer outflows and a small services account deficit, are expected to lead to a narrowing of the current account surplus to RM103.8 billion or 14.3% of GNI in 2010. On the financial account, foreign direct investment inflows and direct investment abroad by Malaysian companies are likely to increase given the improving global and domestic economic conditions.

Gross exports are projected to recover from a low base, registering a growth of 11.2% in 2010. This projection of export growth is based on the assumption that the global economic recovery will be gradual, with sluggish growth in the advanced economies but stronger activity in the emerging economies, particularly the regional economies. Export recovery is expected to be broad-based, as exports will be supported by a recovery in the manufacturing and commodity sectors. This broad-based recovery will continue to be led by intra-regional trade and the gradual pick-up in exports to G-3 economies. The recovery in manufactured exports is projected to emanate from both electronics and electrical (E&E) and non-E&E exports. The stronger growth in the E&E exports is expected to be in both electronics and electrical segments, attributable to the continued strong demand for personal computers, smart phones and new electronics gadgets, as well as the expected recovery in IT spending by the corporate sector. The outlook for commodity and resource-based manufactured exports is expected to improve, with the higher commodity prices and stronger regional demand likely to be sustained.

Exports and capital inflows are expected to continue improving in 2010 as the global economic recovery gathers strength. The current account surplus, while still sizeable, will be reduced, as imports are expected to expand faster than exports

With the anticipation of a recovery in exports and domestic demand, the recovery of **gross imports** is expected to be more pronounced, increasing by 14.6% in 2010. As the bulk of Malaysia's gross imports are intermediate goods, intermediate imports will increase and contribute the most to the import recovery, in tandem with the strengthening demand for manufactured exports. Imports of capital goods are expected to increase as the corporate sector gradually revives investment activity and undertakes new capital investments to increase production capacities. Imports of consumer goods are also expected to increase with the improvement in consumer spending.

The **services account** is projected to record a marginal deficit of RM0.7 billion in 2010, as higher deficits in the transportation and other services accounts are expected to more than offset the higher surplus in the travel account. With global trade, investment and tourism activities improving, payments for transportation, construction, communication and professional services, are also anticipated to increase.

Meanwhile, tourism earnings are expected to continue to increase with the anticipated improvements in global and regional tourist arrivals and well targeted tourism promotional activities. The **income account** deficit is projected to widen to 2.7% of GNI as a recovery in exports is expected to translate into higher repatriations of profits and dividends by MNCs operating in Malaysia, particularly in the E&E industries as well as the oil and gas sector. Meanwhile, profits and dividends accruing to Malaysian companies with investments abroad are expected to remain large, mainly from the oil and gas, and services sectors, supported by higher commodity prices and the improving regional economic outlook.

On the financial account, gross inflows of **foreign direct investment (FDI)** are anticipated to increase in 2010 amid improving global growth prospects and corporate profitability. As global FDI inflows are expected to recover only moderately in 2010, the improvement in FDI in Malaysia is thus projected to be moderate with inflows mainly into the manufacturing, services and oil and gas sectors. In the manufacturing sector, the bulk of the FDI is likely to continue to be in the form of reinvestment by the MNCs for capacity expansion in tandem with the recovery in the E&E industries. In addition, investment is also expected in the new growth areas such as renewable energy and medical devices. Higher FDI flows are also expected in the services sector, particularly in the financial services sector following the further liberalisation in April 2009, which included the issuance of new licenses to foreign financial institutions, increasing foreign equity limits and allowing greater operational flexibility to locally-incorporated foreign financial institutions. Meanwhile, FDI in the oil and gas sector will be supported by rising prices and increasing demand for crude oil as global activity rises.

Direct investment abroad (DIA) by Malaysian companies is expected to increase and remain large in 2010 as companies continue to expand regionally and globally. The higher DIA is expected to be channelled mainly into the services, oil and gas, as well as manufacturing sectors with the focus being on regional and other emerging economies. Regional and global expansion represents opportunities for

Table 4.3
Balance of Payments

	2009*p*	2010*f*
	RM billion	
Goods	141.5	141.6
Trade account	118.4	116.7
Exports (% annual change)	*-16.6*	*11.2*
Imports (% annual change)	*-16.6*	*14.6*
Services	3.2	-0.7
Balance on goods and services	**144.7**	**140.8**
Income	-12.6	-19.9
Current transfers	-19.4	-17.1
Balance on current account	**112.7**	**103.8**
% of GNI	**17.0**	**14.3**
Capital account	-0.2	
Financial account	-82.9	
Balance on capital and financial accounts	**-83.1**	
Errors and omissions	-15.8	
of which:		
Foreign exchange revaluation gain	*10.7*	
Overall balance	**13.8**	

p Preliminary
f Forecast
Note: Numbers may not necessarily add up due to rounding
Source: Department of Statistics, Malaysia and Bank Negara Malaysia

Table 4.4
External Trade

	2009*p*		2010*f*	
	RM billion	Annual change (%)	RM billion	Annual change (%)
Gross exports *of which:*	**553.3**	**-16.6**	**615.1**	**11.2**
Manufactured	430.4	-12.5	474.0	10.1
Agriculture	53.4	-21.6	60.3	12.8
Minerals	59.3	-32.2	70.8	19.4
Gross imports *of which:*	**434.9**	**-16.6**	**498.4**	**14.6**
Capital goods	65.8	-5.9	70.7	7.6
Intermediate goods	297.3	-21.6	348.8	17.3
Consumption goods	31.4	-2.7	33.2	5.7
Trade balance	**118.4**	**-16.6**	**116.7**	**-1.4**

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

Malaysian companies to access a larger consumer market, to increase their scale of operations, and to increase their global competitiveness. This would, over a medium term, benefit the country through having more competitive and globalised Malaysian companies, and also increase the potential for greater income repatriation.

Labour Market Outlook

Conditions in the labour market are expected to improve further in 2010, in line with the recovery in global and domestic economic activity. The improvements in business confidence and economic activity since the second half of 2009 are expected to gain traction during the year, and this in turn will underpin recruitment and salary decisions. Based on a survey conducted by Bank Negara Malaysia, most firms in the manufacturing, services and construction sectors plan to increase employment by about 5% in 2010. With the expected stronger labour demand, the unemployment rate is projected to decline to 3.6% of labour force in 2010 (2009: 3.7%). In addition, about 70% of companies surveyed indicated that they would unwind the freeze on salary increases in 2010. Overall, the average salary increment in the private sector is expected to be higher by 4.1% in 2010 (2009: 3.4%).

Inflation Outlook

Headline inflation is expected to remain modest at an average of 2 – 2.5% in 2010. This projection reflects the improving economic conditions and takes into account the possible adjustments to administered prices and subsidy restructuring by the Government. In the absence of further price revisions and inflation related external developments, inflation in Malaysia will remain contained.

Demand prospects for economic growth in the region and the global economy have improved. The cautious attitude of businesses and households, lingering excess capacity and the withdrawal of Government stimulus measures, however, would in varying degrees affect economic activity across countries. Hence, despite the expected improvement in economic activity, demand conditions are not expected to exert pressure on global inflation in 2010.

Similarly, demand pressures on domestic prices are expected to be manageable. Sustained consumer confidence, the accommodative monetary conditions and the Government's stimulus packages will likely support consumption and investment activity by households and businesses. The output gap will narrow as domestic demand increases. Nevertheless, as output is recovering from low levels, the impact on price pressures is likely to be limited.

On the supply side, the improvement in economic activity since the second half of 2009 is likely to lead to an upturn in global commodity prices. The IMF WEO update in January 2010 projected that crude oil prices could trade higher at around USD76 per barrel in 2010 (USD62 per barrel in 2009). This increase is significantly less compared to the sharp increase in July 2008 when oil prices peaked at USD147 per barrel. Other non-fuel commodities such as food and metals are broadly expected to follow similar trends. The December 2009 edition of the Food and Agriculture Organisation of the United Nation's (FAO) Food Outlook maintained that the overall improvement in the global supply and demand balance would keep price increases for food commodities at moderate levels. Rice prices however, are expected to rise due to lower production amid adverse weather conditions. The price of sugar is also expected to remain firm although lower than the August 2009 peak, as the relatively tight supply conditions are counterbalanced by recovery in production and reserve drawdown.

It should be noted that while the underlying demand for commodities is expected to remain modest, the environment of prolonged low interest rates and excess liquidity could encourage greater speculative activities in the commodity markets. Consequently, non-fundamental factors could periodically push global commodity prices to higher levels. Producers could face higher and more volatile input costs. More subdued demand conditions and above-average inventory levels could moderate the price increases. Nevertheless, the ample global liquidity conditions, if prolonged, would pose heightened risk of higher commodity prices.

On the domestic front, the Government has announced its intention to revise the subsidy for petroleum products. A comprehensive review on the existing subsidies on other essential items is also being undertaken. This could generate some upward adjustment on domestic headline inflation. However, given that demand conditions are not expected to exert strong pressures on consumer prices, the impact is likely to be transitory and contained. Core inflation is likely to exhibit a benign trend and is not expected to be a source for concern.

MONETARY POLICY IN 2010

The global economy entered 2010 on a recovery mode compared to the height of the global crisis in early 2009. Global GDP growth picked up greater momentum in the final quarter of 2009, underpinned by stronger activity, particularly in emerging economies. While there were significant elements of policy support in driving the expansion in economic activity, there were also signs of recovery in private demand, notably in private consumption. The expectation is for private sector demand to strengthen further in 2010.

Monetary policy in 2010 will focus on promoting the sustainability of economic recovery

The recovery process nevertheless appears to be uneven across countries, which implies that the timing and magnitude of the exit from the extraordinary policy measures implemented during the crisis may vary across countries. Emerging economies however, are leading the recovery process in the world economy. The better fundamentals of the emerging markets, especially in Asia, imply that these economies will have an important role in supporting global demand over the next few years.

The emerging markets' better fundamentals could also make these economies vulnerable to large scale capital inflows driven by the combination of low global interest rate, excess liquidity and the rising appetite for risks and search for yields. Given the still uncertain international economic outlook, such capital flows are likely to react suddenly to shifts in global developments and changing expectations. As a consequence, the inflows of funds are equally susceptible to be interrupted by episodes of reversals. The resulting higher volatility in the financial markets could complicate policymaking in the emerging economies where the financial markets are less developed. The challenges to intermediating the large and volatile capital inflows could create financial imbalances and misallocation of resources while the sudden and rapid withdrawals of such funds could disrupt financing and real economic activity. Therefore, the economic and financial environment will remain challenging for emerging economies.

Domestically, the Malaysian economy is expected to strengthen. The ongoing improvement in consumption and investment activities will boost domestic demand and raise national output closer to the productive potential of the economy. Sustained consumer confidence and the accommodative monetary conditions will support consumption and investment activity by households and businesses. The Government has announced plans for a gradual consolidation in its fiscal position in 2010. Nevertheless, the overall fiscal policy remains expansionary and will continue to lend support to the recovery process. External demand, particularly from regional economies, will also sustain trade and economic activity. Accordingly, the prevailing negative output gap will narrow as domestic demand increases.

Inflation is expected to rise in line with the recovery in economic activity. Nevertheless, given that output is recovering from low levels, the resultant pressure on inflation from the narrowing output gap is expected to be limited. Core inflation is likely to exhibit a modest upward trend and is not expected to be a source for policy concern. On the supply side, the Government has announced its intention to undertake a comprehensive review of the subsidy delivery system. The restructuring of subsidies and the reemergence of rising global energy and food prices could generate some upward pressure on domestic inflation. However, the assessment is that the potential impact on consumer prices is likely to be transitory and manageable.

With the threat of a fundamental recession having now diminished, the Monetary Policy Committee (MPC) raised the OPR by 25 basis points in March 2010 towards normalising monetary conditions. A very high degree of monetary stimulus was considered no longer warranted following the robust recovery and improved economic outlook. The concern was that maintaining interest rates at too low a level over an extended period could encourage excessive risk taking behaviour, and the unhealthy build up of leverage. At the same time, it could also result in disincentives to save, and lead to disintermediation, causing savers to move into risky investments. Such developments can undermine the recovery process, while reducing the longer term growth potential of the economy. Thus, while monetary policy remains accommodative and supportive of the economy, the normalisation of interest rates is meant to reflect the improving economic environment and to prevent financial imbalances from developing in the economy.

With price pressures expected to be modest going forward, monetary policy in 2010 will focus on promoting the sustainability of economic recovery and ensuring that financing continues to be available to the private sector at a reasonable cost. Given the lingering uncertainties surrounding the future growth path of the global economy, an accommodative monetary policy stance will be maintained to support and strengthen private investment and consumption demand and thus overall economic growth.

FISCAL POLICY IN 2010

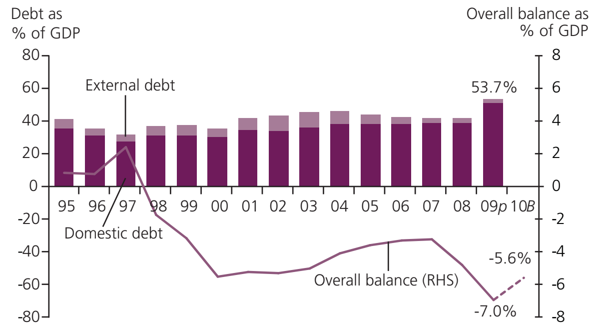
Fiscal policy was significantly expansionary in 2009 to prevent the Malaysian economy from sliding into a fundamental economic downturn as the global financial and economic crisis drove the global economy into a deep recession. Along with accommodative monetary policy and pro-active measures to support access to financing by the private sector, these measures were successful in mitigating the recessionary impact of the crisis on the Malaysian economy. As a result, the economic contraction begun to stabilise as early as the second quarter of 2009. As the economy continues to recover in 2010, fiscal policy will remain geared towards preparing the foundation for a stronger recovery of private sector demand. Key to a sustained economic recovery is a strong resumption of private consumption and investment. Thus, fiscal policy has accorded significant priority towards enhancing the role of the private sector as the driver of economic growth.

Table 4.5
Federal Government Finance

	RM billion		% change	
	2009*p*	2010*B*	2009*p*	2010*B*
Revenue	158.6	148.4	-0.7	-6.4
Total expenditure	206.6	189.5	5.2	-8.3
Operating expenditure	*157.1*	*138.3*	*2.3*	*-12.0*
Gross development expenditure	*49.5*	*51.2*	*15.6*	*3.4*
Loan recoveries	0.5	0.6		
Overall balance	**-47.4**	**-40.5**		
% of GDP	**-7.0**	**-5.6**		
Sources of financing:				
Net domestic borrowing	56.9	-		
Net external borrowing	-6.3	-		
Realisable assets[1] and adjustments	-3.2	-		

[1] A positive (+) sign indicates a drawdown in the accumulated realisable assets
p Preliminary
B 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 Budget
Source: Ministry of Finance

Government efforts to strengthen private investment and increase the participation of the private sector in the economy were reflected in the measures announced in the 2010 Budget. These include privatization initiatives, and measures that provide a more conducive business environment. Moreover, to encourage private sector involvement in the economy, the Government is also providing incentives to several high growth sectors. Among the sectors identified are tourism, information technology and communication (ICT), finance and Islamic banking, halal products and green technologies. To further support growth of private consumption, the Government has reduced the personal income tax, and raised individual tax relief to increase the disposable income of consumers.

In response to the contractionary influences on the domestic economy as the global economy slipped into a recession, the Government implemented a sizeable fiscal stimulus in 2009, resulting in a higher deficit of 7% of GDP (2008: 4.8% of GDP) and a higher Federal Government debt of 53.7% of GDP (2008: 41.5% of GDP). For 2010, whilst remaining largely accommodative, fiscal policy has taken into account the need to ensure that it will not exert undue strain on the Government's finances. Specifically, the large Government support introduced at the height of the global economic crisis would be gradually scaled back.

With a view towards a phased consolidation of the fiscal position, the 2010 Budget placed emphasis on measures to improve the effectiveness and efficiency of the Government's revenues and expenditures. To enhance the efficiency of Government expenditures, the measures that will be implemented and prioritised include the restructuring of the fuel subsidy system which accounts for a significant portion of the Government's annual outlays as well as a review of the whole system of subsidies and price controls. To maintain a sustainable fiscal position without compromising the overall growth and development objectives, the Government will also intensify its public-private partnership programme for several high impact projects. Some of these projects include the high speed broadband, regional development corridors and public transportation infrastructure projects.

To strengthen its revenue streams, the Government has undertaken a study on the feasibility of implementing the goods and services tax (GST). With the GST, the Government revenue base will be broadened and thus better insulated from the adverse cyclical swing in oil prices. Currently, the revenue base is too narrow, depending mainly on direct taxes and petroleum-related revenues. In addition, it is significantly exposed to the swings in the business cycle that has a large impact on government finance. The Government has also announced plans to review the tax assessment system, especially for petroleum related activities, which are currently assessed with a lag of up to a year.

With the implementation of these measures, the Federal Government fiscal deficit is expected to narrow to 5.6% of GDP in 2010. Operating expenditure will be lower by 12% from RM157 billion in 2009 to RM138 billion. Meanwhile, development expenditure will remain high at RM51.2 billion. Most of the development expenditure will be channeled towards the economic services and education services sectors.

Given the ample liquidity in the domestic market, the Government has financed its fiscal deficit mainly from the domestic bond market. Apart from raising funds through the issuance of government securities, the Government will also issue an RM3 billion retail bond known as 1Malaysia Sukuk. The issuance will also serve as an alternative investment avenue for Malaysians to receive better returns in an environment of low domestic interest rates.

Transitioning into a High Income Economy: Policy Considerations

From Past to Present: Development of the Malaysian Economy

Malaysia has achieved significant economic progress since attaining Independence in 1957, developing from a low income to an upper middle income economy over a half-century. Income per capita has risen by approximately twenty fold in the last four decades, while the incidence of poverty has been reduced by more than ten fold. Major structural changes have also occurred in the economy. The predominantly primary commodity-based economy with a heavy reliance on rubber and tin in the 1960s was transformed by the rise of the manufacturing sector as the main contributor to growth in the late 1980s, and subsequently, by the services sector becoming the main driver of growth since 2000. Throughout this development process, Malaysia has strengthened and deepened its integration with the global economy.

Malaysia is currently confronted with a global economic environment that is changing significantly. While the global landscape has been gradually shifting in this recent decade, the current global financial and economic crisis has accelerated this shift. Of significance, two distinct developments stand out. First, the global economic landscape is increasingly multi-polar with the rising economic importance of the emerging market economies, especially the economies of Brazil, Russia, India and PR China (BRIC). Importantly, the significant rise of PR China has changed the dynamics of growth in Asia. Favourable structural factors in the emerging market economies, including a large and growing middle class, will support domestic demand and thus the continued growth of these economies post-crisis. The crisis has, however, revealed several structural weaknesses in the advanced economies, all of which will limit the growth potential of these economies in the medium term. Second, the rise of the relatively large emerging market economies, such as the BRICs, Vietnam and Indonesia, will also intensify competition in the global economy, not only among businesses, but also among countries in attracting investment and human capital.

In this more challenging environment, strategic initiatives are being taken to strengthen the flexibility of the Malaysian economy in adapting to the changing circumstances, so as to effectively benefit from new opportunities while addressing potential challenges. The existing economic model is being reviewed and policies that support greater competitiveness, a faster pace of innovation and the elevation to more knowledge-intensive industries are the strategies to transition Malaysia to a high income economy.

The Future: Characteristics of the High Income Malaysian Economy

A high income country is defined by the World Bank as a country with an income per capita of more than US$11,905. Therefore, from its current level of US$6,634, Malaysia needs to approximately double its income per capita to become a high income country. Beyond the level of income, an assessment of the existing high income countries highlights five key economic characteristics, namely:

1. **Knowledge and innovation-intensive economic activity**

   A high income economy is knowledge and innovation-driven as opposed to investment-driven. All sectors of the economy are involved in high value economic activity, where knowledge, innovation and productivity are central to value creation.

   For Malaysia, given the existing strong manufacturing base, movement towards higher value activity will be driven by the existing industries moving up the value chain. Firms in these industries will increasingly rely on niche strategies as well as continuous improvements, higher sophistication and greater specialisation. Some of the potential areas include advanced electronics, solar panel manufacturing, medical equipment and downstream palm oil. This movement towards higher value activity will be complemented by the development of the knowledge-intensive services sub-sectors. These modern services include computing, information and communication technology (ICT), research and development (R&D), health and education, and entertainment. Alongside these knowledge-intensive services, established manufacturing-related services, such as logistics, marketing and branding, will also provide strong support to industrial growth.

In addition, while multinational and large domestic corporations remain important, small and medium enterprises (SMEs) will form the backbone of the economy. Of significance, a strong base of highly dynamic, innovative and competitive SMEs will be a critical feature of a high income Malaysian economy.

2. Competition-driven private sector-led economy

Economic activity in a high income economy is led by the private sector in a competitive environment. Competition will contribute to the efficient allocation of resources and the creation of vibrancy and dynamism in economic activity. For markets to function effectively and efficiently, the absence of market distortions, particularly those that result in inappropriate price signals, is a necessary precondition. Nevertheless, a strong institutional framework needs to be in place to address the potential for market failure and to ensure a competitive and fair business environment.

3. Government as a facilitator of economic growth

As the economy will be private sector-led, the role of the Government has to shift to become a key facilitator of growth. In this role, the focus of the Government is on providing a competitive enabling environment for the efficient functioning of the private sector. This will primarily involve the provision of enabling infrastructures, including public transportation and modern internet-related infrastructure, as well as the provision of security and basic social services, such as health and education. In addition, a comprehensive technology and innovation policy would encourage high value activity and knowledge creation. Close collaboration between the public and private sectors is necessary to effectively achieve these objectives.

4. Greater balance between domestic and external demand

Consistent with the ongoing trend, a high income economy needs to have a more balanced model of development. Whilst competitive advantage in the external sector can remain key, the domestic sector needs to have a greater role in contributing to growth. First, a higher and larger middle income group will support even higher and more sophisticated private consumption. Second, an increase in the quality of private investment will contribute to a more sustainable growth of high income and high value-added employment. Private investment will need to increasingly shift away from being predominantly in construction and low value machinery towards advanced automation and R&D to facilitate movement up the value chain as well as to support innovation. High productivity, meanwhile, will complement this rise in capital sophistication to deliver high value products and services.

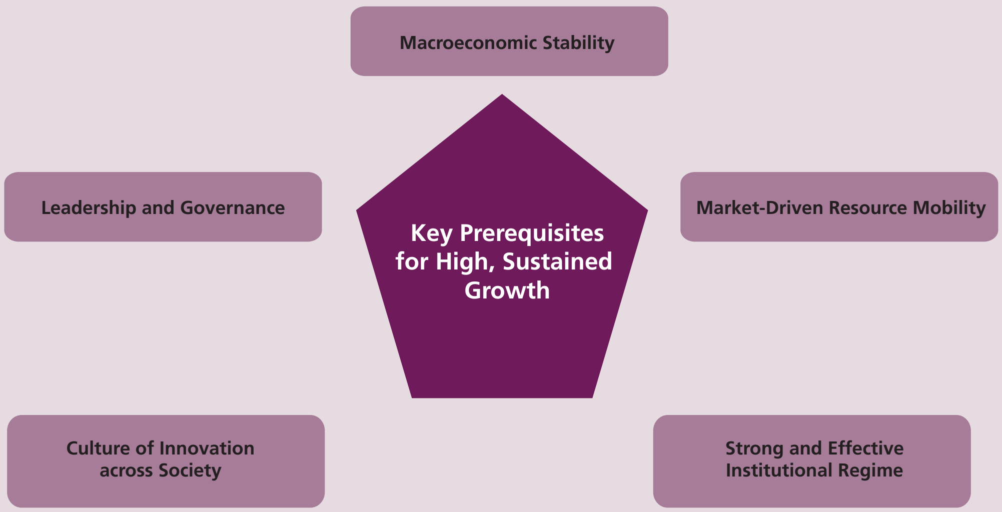
5. Deeper global and regional integration

Given that the domestic market in Malaysia is small, firms will, as they grow in size and strength, increasingly integrate with the region and the rest of the world for greater access to larger markets. Deeper integration with the international markets will encompass both final demand and the supply of factor inputs. For Malaysia, further integration with the regional economies and other emerging economies will be a key characteristic of the transition to becoming a high value-added economy. In particular, the recent rising trend of investment abroad by Malaysian companies can be expected to continue and over the medium term will bring increased benefits to Malaysia as new opportunities and markets are gained.

Strategies for a Sustainable and Dynamic Malaysian Economy

Despite relatively distinct views as to the characteristics of a high income economy, there is no consensus on the requirements to successfully become a high income economy. The experiences of the high income countries do, however, offer some indication that five factors are particularly important (Figure 1). First is macroeconomic stability, which provides an environment conducive for high savings and business investment in an environment of reduced uncertainty. Second, market-driven resource mobility across all markets is essential for the efficient allocation of resources in the economy. Third, there must exist a strong institutional regime with adequate enforcement, encompassing, amongst others, an effective regulation of competition, the prevention of market failures and an effective protection of property rights. Fourth, a culture of innovation needs to

Figure 1
Five Pillars for Sustained Economic Progress



be instilled nationwide, with collaborative efforts within and between the private and public sectors as well as academia. Fifth is that strong leadership and governance must continue to have an important role, particularly in ensuring stability, developing a competitive environment and providing the enabling infrastructure.

Although the broad development literature does not provide a single clear recipe for economic development, experiences do, however, give examples of factors that should be resisted (Figure 2). Of significance are market distortions that are put in place to artificially sustain cost competitiveness. Across many developing economies, market distortions have ranged from price controls and energy subsidies, to the open-ended protection of specific sectors and industries. While there may be circumstances to justify the temporary adoption of some of these measures, such policies over a prolonged period of time usually involve high costs.

For Malaysia going forward, established strengths and foundations will provide the support for continued economic development. To successfully transition into a high value-added economy, Malaysia has the potential to capitalise on existing comparative advantages and develop deeper capabilities and expertise. It has been recognised that fundamental reforms will be required in several areas of the economy. In this regard, three key strategic priorities have been identified, namely to nurture a quality workforce, foster a competitive environment and develop an efficient enabling infrastructure.

Figure 2
Global Experience in Common Constraints to Growth

Pillar 1 : Macroeconomic Stability

- Misdirected spending
- Unsustainable fiscal deficit
- Monetary and financial instability

Pillar 2 : Market-Driven Resource Mobility

- Price distortions:
  - Energy subsidies
  - Artificial wage levels
  - Excessive price controls
- Market distortions:
  - Open-ended protection of specific sectors and industries

Pillar 3: Effective Institutional Regime

- Poor competition policy and weak regulation to address market failures

Pillar 4: Innovation Discipline across Society

- Progress in education in terms of quality, extent of learning and innovative thingking

Pillar 5: Leadership & Governance

- Neglect of environmental issues
- Oversized public sector
- Corruption

1. Quality workforce with an instilled culture of innovation

A knowledgeable, innovative and entrepreneurial workforce is essential to drive the value creation necessary in a high income economy. Therefore, world-class education and training are critical for developing skills and creative talent.

Malaysia is, therefore, embarking on the reform of its education system into one that is capable of developing human talent equipped with the relevant skills and competencies required to enhance productivity and economic development. In this regard, strong emphasis is being placed on strengthening the learning institutions in order to ensure top-quality teaching. Relating to this, the salary and reward schemes for university lecturers and teachers are currently being improved to better attract and retain quality educators. In addition, a technical education system is being enhanced to successfully provide the skilled talents required for the advanced manufacturing and services sectors. To ensure that quality is continuously upheld, performance of the premiere polytechnics will be benchmarked against renowned technical institutions, including those in Germany, Austria and Sweden. There have also been ongoing efforts to engage with the private sector in ensuring the relevance and effectiveness of the education system in meeting the needs of the industry.

While reform of the education system is a critical priority, flexibility is being given to draw on the global flow of talent. In this regard, a series of measures has been undertaken to increase the flexibility to employ expatriates, while initiatives are being put in place to reduce brain drain.

2. Competition-driven and efficient markets

Sophisticated high value economic activity requires well-functioning market mechanisms, guided by undistorted price signals, to efficiently allocate the scarce resources. Market distortions would potentially lead to considerable inefficiencies and wastage, while protectionist policies undermine the fundamental incentive structure needed for a thriving entrepreneurial society.

At present, a number of market distortions exist in several areas of the Malaysian economy. These market distortions are highly intertwined in nature, with the measures in place impacting various industries and sectors in the economy. Such subsidies heavily burden the Government and divert resources away from other investment activities. The removal of such distortions should, however, be gradual and sequenced to avoid disruptions to the economy. Equally important is for the savings from the removal of the existing broad-based distortions to be reallocated as more targeted subsidies and direct income transfers to support the low and middle income groups.

3. **Extensive and efficient enabling infrastructure**
   Both traditional and modern infrastructures have a key role in enabling the transition towards a high value-added economy. As Malaysia already has in place high quality physical infrastructure including roads, ports and utilities, the focus is now on the development of an efficient public transportation system, modern internet-related infrastructure and energy efficiency-related infrastructure, which are important in enabling high value activity and improving overall economic productivity. In an effort to expand broadband services nationwide, the Government, in partnership with Telekom Malaysia, has embarked on a RM11.3 billion High Speed Broadband initiative.

   As Malaysia adopts these changes, policy implementation needs to take into account three important considerations. First, policies should be gradual and sequenced in order to allow businesses and households to adjust to the new environment. Second is the importance of transparency to allow for public awareness on the new opportunities and constraints. Third, support needs to be provided to the low income group to minimise the negative impact during the transition, as well as to enhance the necessary skills and capabilities required to take advantage of the new opportunities.

Conclusion

The Malaysian economy is currently positioned at a critical juncture of its development and future progress will be confronted with many challenges. Throughout Malaysia's development process of more than 50 years, the economy has exhibited the ability and flexibility to move to new areas of comparative advantage and to new areas of growth. Similarly, in this current process of transitioning into a high value-added economy, Malaysia needs to develop new growth areas and adopt a new economic model for development. With the development of an enabling and competitive economic environment comprising of a quality workforce and an efficient infrastructure, Malaysia will be ready with the necessary foundations to take advantage of the emerging and rapidly changing regional and global trends in order to transition into a high value-added economy.

Governance, Communications and Organisatonal Development

Governance, Communications and Organisational Development

OVERVIEW

Emphasis on governance, communications and organisational development initiatives in 2009 aimed at strengthening the performance and effectiveness of the Bank in delivering its mandate. During the year, focus continued to be on strengthening organisational capacity and capability through the further enhancement in the areas of strategic management, governance, risk management, communications and talent management. This is to ensure the Bank remains effective in discharging its mandate and well positioned to meet the challenges posed by the rapidly changing environment.

The communications function of the Bank continued to have a crucial role in sustaining stakeholders' confidence amidst the volatile environment. Greater strategic engagement with a wide range of stakeholders has heightened understanding and awareness of the Bank's policy actions and measures. The timely dissemination of economic and financial information has also facilitated the public and businesses in making more informed decisions.

As a strategy-focused organisation, high-level attention and interventions are continuously made to enhance the strategic orientation of the Bank. Of importance in 2009 was the successful commencement of the Bank's 3-year Business Plan. The Plan provides clarity to the organisational goals and the alignment of the resources of the Bank towards achieving these objectives. The implementation of the Plan also facilitated the evaluation and review of the Bank's strategies and performance to ensure the organisation is outcome-based and continues to achieve its desired strategic results.

A significant development during the year was the enactment of the new Central Bank of Malaysia Act 2009 (CBA) on 25 November 2009. A key aspect of the CBA is aimed at providing greater clarity on the Bank's mandates and to equip the Bank with enhanced capacity to undertake its mandate. It also institutionalises a more robust governance framework that ensures a high level of accountability and transparency. In line with this, the Board's oversight function was further strengthened through the establishment of two additional Board committees with specialised roles and functions to reinforce the checks and balances, and to contribute towards better decision-making in the Bank.

Risk management capabilities were also reinforced further through the enhanced Enterprise Risk Management (ERM) framework. The framework embeds risk management considerations in all areas of strategic importance such as policy making and key operations of the Bank and allows a more robust oversight of the organisation's risks and controls. This enables solid and informed decision-making by Management, particularly in light of the complex and challenging environment facing central banks today. In addition, efforts were also undertaken to review both the existing framework for Financial and Operational Risk Management, with the view of inculcating a strong risk management culture by increasingly empowering the business units to identify and manage risks within their functional areas.

The focus on talent management is aimed at ensuring a solid talent pipeline. Ensuring proper job fit reflects the Bank's continued commitment towards building a high performance workforce that will support the ability of the Bank to deliver the strategic outcomes. Towards this end, continued investments were made in the profiling and development of the talent pool, while the career growth policies and framework were reviewed to ensure the Bank's talent management strategies remain relevant. This was complemented by the learning and knowledge management initiatives to provide continuous support for talent development. Efforts were undertaken to ensure better alignment of learning solutions to the requirements of the Bank through increased customisation of learning arrangements, improved flagship programmes and e-learning.

During the year, ICT management remained focused on the use of technology solutions and leading-edge infrastructure to enable efficient operations in a number of business functions.

As part of the continuous effort to enhance regional and international cooperation, the Bank in collaboration with external agencies, expanded its technical assistance in the areas of institutional capacity building, financial inclusion and Islamic Finance.

GOVERNANCE

An essential component of a performance-based organisation is sound governance. Several key initiatives were undertaken in 2009 to further strengthen the Bank's governance to ensure that it remains effective and efficient in carrying out its functions.

Consolidating and enhancing the Bank's governance framework

The enactment of the new CBA on 25 November 2009 represented an important part of enhancing the governance framework of the Bank. It also strengthened the capacity of the Bank to enhance financial sector resilience especially in light of the increasingly challenging business landscape. Firmly embedded in this new and forward-looking legislation are the revised corporate governance framework and processes that have been further streamlined and strengthened while maintaining the governance principles of independence, accountability and transparency.

The CBA takes into consideration the changed environment within which the Bank is operating, and provides the enabling legal framework to address new and emerging risks and challenges. It enables the Bank to be in a greater state of readiness to function more effectively. A key aspect of the CBA is the adoption of a more holistic approach that provides greater clarity to the Bank's mandates and enhances the Bank's capacity in performing its functions. It also reinforces the existing governance practices and provides the necessary checks and balances to ensure accountability and sound decision-making.

To ensure the sustained effectiveness of the Bank in performing its primary functions, the CBA institutionalises the autonomy of the Bank in the formulation of monetary policy and provides greater flexibility in monetary policy implementation. At the same time, the legislation of the Monetary Policy Committee (MPC) also provides the necessary safeguards through the strengthened governance and accountability framework, which are important in further enhancing the quality of decision-making in the Bank. The operationalisation of the new MPC in January 2010 comprising committee members with the required skills profile and competency mix is aimed at further enhancing the Bank's effectiveness in achieving the objective of monetary stability.

The mandate of promoting financial stability is also made explicit in the CBA. Oversight of the Bank's mandate for financial stability is provided through the Financial Stability Policy Committee. The Committee is responsible for reviewing developments affecting risks to financial stability and deciding on actions, including macroprudential policy responses, to address systemic risks. Deliberations on micro-prudential measures to emerging risks within individual financial institutions with broader implications for financial stability are also consolidated under the Committee. This allows for more integrated assessments of appropriate responses to identified risks, particularly where the actions with respect to individual institutions will invoke exigent powers accorded to the Bank under the CBA. Recommendations by the Bank on actions that affect institutions that are not regulated by the Bank, or resolution actions involving financial institutions that are no longer viable, must be further approved by an independently constituted Financial Stability Executive Committee established under the CBA. The Bank's public accountability for financial stability is additionally supported by the publication of an annual financial stability report which provides an assessment of risks to financial stability, actions taken by the Bank to avert such risks as well as ongoing initiatives to strengthen the foundations for financial stability.

In strengthening the Board's oversight on the management and performance of the Bank, the new legislation has institutionalised the establishment of two additional Board committees and an existing Board committee whose members comprise non-executive directors of the Bank so as to ensure independent oversight over the Bank's operations. These are the Board Governance Committee, the Board Risk Committee and the existing Board Audit Committee. The Board Governance Committee was established to review the effectiveness and to recommend the principles and practices of governance in the Bank, to nominate members of the MPC and other

The Central Bank of Malaysia Act 2009

Introduction

The Central Bank of Malaysia Act 2009 (“the Act”) which came into force on 25 November 2009 heralds a new era for central banking in Malaysia. The Act is a completely new piece of legislation which replaces the Central Bank of Malaysia Act 1958. The Act modernises the central banking law of the country and brings greater clarity and focus to the mandates of the Bank and provides the Bank with the necessary powers and autonomy to continue to undertake its mandates effectively. Commensurate with these powers and autonomy of the Bank, the governance framework has been strengthened with the accountability and transparency of the Bank significantly enhanced. Bank Negara Malaysia, the body corporate which was established under the Central Bank of Malaysia Act 1958, continues as the central bank for Malaysia under the new Act notwithstanding the repeal of the 1958 Act.

Mandates

The Act states the principal objects of the Bank are to promote monetary stability and financial stability conducive to the sustainable growth of the Malaysian economy. The Act also provides that the primary functions of the Bank are to:

(a) formulate and conduct monetary policy in Malaysia;
(b) issue currency in Malaysia;
(c) regulate and supervise financial institutions which are subject to the laws enforced by the Bank;
(d) provide oversight over the money and foreign exchange markets;
(e) exercise oversight over payments systems;
(f) promote a sound, progressive and inclusive financial system;
(g) hold and manage the foreign reserves of Malaysia;
(h) promote an exchange rate regime consistent with the fundamentals of the economy; and
(i) act as financial adviser, banker and financial agent of the Government.

In giving effect to the above objects and functions, the Bank is required to have regard to the national interest.

Monetary stability

The Act institutionalises the existing practices of the Bank for the formulation and implementation of monetary policy with the establishment of the Monetary Policy Committee (“MPC”). Monetary independence, which has been enjoyed by the Bank in the 50 years of its existence and which is key to the effective formulation and implementation of monetary policy, has now been legislated for in the Act. In promoting monetary stability, the Act requires the Bank to pursue a monetary policy which serves the interests of the country with the primary objective of maintaining price stability while giving due regard to the developments in the economy. To ensure the soundness of monetary policy decisions, the Act incorporates extensive safeguards that include setting the criteria for the appointment of MPC members, the requirement for the publication of a monetary policy statement following every MPC meeting and the processes for the decision-making by the MPC. To implement the decisions of the MPC, the Bank is accorded flexibility to conduct monetary operations through a broad range of instruments (see box article “Monetary Policy Process under the Central Bank of Malaysia Act 2009”).

The exchange rate regime will continue to be determined by the Minister of Finance on the recommendation of the Bank. The Bank will autonomously conduct the foreign exchange operations to promote the efficient and effective functioning of the exchange rate regime and the foreign exchange market.

Financial stability
The duties and powers vested with the Bank under the Act establish the Bank as the financial stability authority for Malaysia. The Act gives the Bank the necessary powers to minimise the likelihood and impact of adverse developments that may affect financial stability including the financial intermediation process, the orderly functioning of the foreign exchange and money markets or public confidence in the financial system. The Bank continues to act as lender of last resort and may now additionally extend liquidity assistance to entities not regulated by the Bank but that are regarded as systemically important.

Expanded powers have been given to the Bank to promote financial stability including the power to obtain information for the purpose of identifying and monitoring risks to financial stability and undertake pre-emptive actions. The Act also empowers the Bank to facilitate the resolution of financial institutions which are in financial stress to ensure swift and orderly resolution, thereby minimising the impact and costs of the failure of a financial institution to the domestic economy and to preserve public confidence. Actions that may be taken by the Bank include purchasing capital instruments, financing the purchase of the business or capital instruments of such institutions, and transferring to and vesting the business or capital instruments of these institutions in the Bank, another financial institution or person. The Act further sets out a clear accountability framework for such actions and where such actions involve the transfer of business or capital instruments, the Act has put in place an independent valuation process.

Given the increased interconnectedness between the domestic financial system and the global financial system, the Bank has also been empowered to coordinate with other financial regulatory authorities on joint efforts in crisis prevention, management and resolution (see box article in Financial Stability and Payment Systems Report 2009 "Safeguarding Financial Stability under the Central Bank of Malaysia Act 2009").

Money and foreign exchange markets
The Act empowers the Bank to have oversight of the money and foreign exchange markets and the market for derivatives related to currency, securities and other financial instruments that are traded in these markets, to develop and maintain the orderly conditions and the integrity of these markets. These markets are core components of the financial system and have significant implications for the resilience of the financial system. The Bank is empowered to issue rules, codes, standards, principles or guidelines for these markets. The Bank may also appoint a self-regulatory organisation for the foreign exchange market and the market for derivatives related to currency, securities and other financial instruments that are traded in this market.

Financial inclusion
The Act makes an explicit provision for financial inclusion to be incorporated as one of the primary functions of the Bank. Financial inclusion is vital for creating balanced sustainable economic growth and provides the opportunity for all segments of the economy to benefit from economic progress. For this purpose, the Act empowers the Bank to establish funds to provide financing in exigent circumstances or to any segment of the economy to promote financial inclusion.

Islamic finance
Building on the existing legislative infrastructure for Islamic finance including the Islamic Banking Act 1983, the Takaful Act 1984 and the Government Funding Act 1983, the Act sets out a legal framework for the further development of the Islamic financial system in Malaysia. The Act gives due recognition to the Islamic financial system which operates in parallel with the conventional financial system and also mandates the Bank together with other agencies in Government to promote Malaysia as an international Islamic financial centre.

Under the Act, the Shariah Advisory Council which was established under the Central Bank of Malaysia Act 1958 continues to exist with its current members appointed by the Minister of Finance. The Act provides that new members to the Shariah Advisory Council will henceforth be appointed by the Yang di-Pertuan Agong in view of the enhanced role of the Shariah Advisory Council. Where a question concerning a Shariah matter arises in any court proceedings or arbitration relating to Islamic financial business, the court or arbitrator is required to refer such question to the Shariah Advisory Council for a ruling. The ruling made by the Shariah Advisory Council is binding.

Management of foreign reserves

The Bank will continue to manage the foreign reserves of Malaysia. The range of assets which the Bank can hold has been enlarged to include securities and financial instruments including derivatives that are approved by the Board of Directors. The Bank is required to manage the foreign reserves in accordance with the policies and guidelines issued by the Board of Directors.

Financial adviser, banker and financial agent to the Government

As in the Central Bank of Malaysia Act 1958, the Bank will continue to act as the financial adviser, banker and financial agent to the Government. In addition, the Act also provides for the Bank to advise the Government generally on economic matters that are within the competence and expertise of the Bank.

International co-operation

The Act empowers the Bank to engage in international co-operation by participating or providing financial resources in any arrangement or initiative with other central banks, monetary authorities or international financial institutions to promote monetary, financial or economic co-operation at the bilateral, regional or international level. The Bank shall also continue under the Act to exercise the rights and perform the obligations arising from Malaysia's or the Bank's membership, as the case may be, in the International Monetary Fund, Islamic Financial Services Board, Bank for International Settlements and any other international organisation as provided under federal law.

The Bank, with the approval of the Minister of Finance, is also empowered to issue regulations or directions to financial institutions to discharge the Government's international obligations under the resolutions passed by the United Nations Security Council.

Governance

The Act strengthens the general governance framework of the Bank, in particular, the oversight powers of the Board of Directors. The Board of Directors is responsible for the general administration of the affairs and business of the Bank and the approval of the budget and operating plan of the Bank. For the purposes of carrying out its oversight function under the Act, the Board is empowered to issue by-laws.

The Board in its oversight role is assisted by the Board Governance Committee, Board Audit Committee and the Board Risk Committee, whose members are non-executive directors.

The Board Governance Committee is responsible for examining and recommending the budget and operating plan of the Bank to the Board for approval. The Committee will also recommend the persons to be appointed to the MPC and other Committees of the Bank.

The Board Audit Committee is responsible for assisting the Board in its oversight of the integrity of the accounts and financial statements of the Bank, the effectiveness of the internal control system, the performance of the internal audit function and compliance with legal and regulatory requirements.

The Board Risk Committee is responsible for assisting the Board in the oversight on the management of the enterprise risks of the Bank.

Under the Act, the Governor and Deputy Governors are answerable to the Board for their actions and decisions. This is consistent with the Board's duty to keep under constant review the performance of the Bank in giving effect to its objects and functions and the use of the resources of the Bank (for a more detailed discussion of the governance aspect of monetary stability and financial stability functions of the Bank, see box article "Monetary Policy Process under the Central Bank of Malaysia Act 2009" and box article in Financial Stability and Payment Systems Report 2009 "Safeguarding Financial Stability under the Central Bank of Malaysia Act 2009").

Accountability

The Act provides for the accountability of the Bank to the Parliament, the Minister of Finance and the public in general.

The Bank continues to be accountable to the Parliament and the Public Accounts Committee under the Houses of Parliament (Privileges and Powers) Act 1952 and the respective Standing Orders of the Houses of Parliament. The Act also requires for the annual financial statements and report of the Bank to be laid in the Houses of Parliament within three months from the close of the financial year of the Bank. If the Houses of Parliament are not in session at that time, the annual financial statements and report of the Bank have to be laid at the next session of the Houses of Parliament.

The Bank is required to submit to the Minister, the Bank's statement of assets and liabilities on a fortnightly basis and its annual financial statements and report within three months from the close of the financial year.

The Bank is also required to keep the Minister informed of the policies relating to the principal objects of the Bank. In this respect, a mechanism has been put in place in the Act to resolve differences between the Minister and the Bank on such policies. In the event the differences are not resolved, the mechanism provides for the matter to be tabled to the Cabinet for a determination of the policy to be adopted by the Bank. In the event the differences remain, the matter is to be laid before the House of Representatives.

The Bank is required to keep the public informed of the monetary policy decisions of the Bank after every meeting of the MPC by publishing a monetary policy statement which shall include the rationale for the decision. Additionally, while the Bank is required to publish the statement of assets and liabilities of the Bank on a fortnightly basis, the annual financial statements and report have to be published within three months from the close of the financial year.

Conclusion

The Act provides a comprehensive legal foundation for the Bank to ensure monetary stability and financial stability and to foster a progressive, resilient and inclusive financial system to meet the challenges of the rapidly changing financial and economic landscape of the 21st century.

committees and to evaluate the roles of the Board and Board committees. Another key function of the Committee is to examine and recommend to the Board the budget and operating plan of the Bank for approval. Meanwhile, the Board Risk Committee assists the Board in the oversight over the Bank's management of enterprise risk through identification, assessment and management of risks that could affect the performance of the Bank. The function of the Board Audit Committee remains to assist the Board in its oversight of the integrity of the accounts and financial statements of the Bank, the effectiveness of the Bank's internal control system, performance of the internal audit function, and the Bank's compliance with legal and regulatory requirements.

Enhanced internal controls and risk management

In March 2009, the Board Audit Committee approved the Bank's revised Internal Audit Charter, which defines the purpose, authority and responsibilities of the Internal Audit Department (IAD). The charter was revised to better align the audit activities to support the functions of the Board Audit Committee and to support IAD's adoption of a risk-based auditing framework.

To balance the effectiveness and efficiency of operations with good risk management practices, the rationalisation of the management structure and the strengthening of the coordination between the risk management and internal audit functions were also carried out. Amongst the key initiatives was the transformation of the Risk Management Department, the conceptualisation of enterprise risk management approach and the adoption of a risk-based auditing methodology.

Within the area of procurement management, efforts were also expended in the review and rationalisation of the application of risk mitigating instruments by the Bank. While the objective of the exercise was aimed at managing the risks associated with procurement activities in the Bank, other key considerations included timely delivery of products and services by vendors and suppliers as well as ensuring fair business practices.

Governance in external engagements

As financial systems and economies become increasingly connected, activities that promote the Bank's engagements with external organisations have also been important in achieving the objectives of the Bank and its key stakeholders. With the activities being centrally coordinated by the International, Central Banking Services and Corporate Services Departments, the collaborative approaches adopted by the Bank include the conduct of bilateral meetings, entering into Memoranda of Understanding (MOU), particularly in the areas of trade and investments, financial surveillance and regulations, and the exchange of information to combat activities relating to money laundering and terrorism financing.

To further strengthen the governance in external engagements, the Bank centralised the management of its involvement in external committees and organisations. At the same time, the flow of information from the Bank's external engagements to the organisation was also enhanced through the development of the Management Insights, a centralised electronic repository to capture the relevant events and issues to the Management, with the view of enabling more robust and informed decision-making.

Risk Management Approach

Risk Management is an integral part in the Bank's governance framework to safeguard its reputation and to ensure the safety and soundness of the Bank's assets and operations. Since 2007, the Bank has adopted an Enterprise Risk Management (ERM) approach to better manage risks in a multi-dimensional manner in the achievement of the key objectives across areas outlined in the Business Plan and in the strategic initiatives, policy making and operations of the Bank. The implementation of ERM contributed significantly to the more robust oversight, controls and discipline that drive continuous improvement in the Bank's risk management capabilities.

Enhanced risk management governance structure

Best practices in risk management dictate the need for constant improvement in the governance and risk culture at all levels of the organisation. The Bank undertook periodic review and monitoring to ensure risks are identified and adequate controls are in place to mitigate these risks. In 2009, two significant changes took place in the risk management of the Bank; the establishment of the Board Risk Committee, and the approval of the enhanced Financial and Operational Risk Management frameworks by the Risk Management Committee (RMC).

The primary objective of the Board Risk Committee is to provide oversight on the management of risks faced by the Bank that could lead to financial losses, disruptions to operations, failure to attain objectives or damage to the Bank's reputation. The Committee also oversees the Management's activities in identifying, mitigating and managing credit, market, liquidity, operational, reputation and other risks while ensuring appropriate risk management processes are in place and functioning well.

The risk management function of the Bank is primarily driven by the RMC, which is chaired by the Governor. The RMC continues to be the main forum for focused and regular deliberation of organisational risks and also ensures effective risk management within the Bank. Significant risk issues are raised by two sub-committees under RMC i.e., Financial Risk Management Committee (FRMC) and Operational Risk Management Committee (ORMC). The two sub-committees, each headed by a designated Deputy Governor, provide important platforms to assist the RMC in making informed decisions on both financial and operational risks.

The Risk Management Department (RMD) is responsible for developing and maintaining the risk management framework of the Bank. This includes the development of policies, processes, tools and methodologies, as well as the operationalisation of the Enterprise, Financial and Operational Risk Management frameworks and ensuring all elements within the frameworks are functioning as intended. In addition, RMD also collaborates with all operating units in identifying, assessing, measuring and monitoring their risk exposures. It also gives an independent assessment of the significant risks from an enterprise-wide perspective and provides an evaluation on whether these risks are being sufficiently managed.

In 2009, the financial risk and operational risk frameworks were reviewed and enhanced further to strengthen the existing governance structure within the Bank. The initiatives are intended to build a strong risk management culture in the Bank by empowering line departments to manage risks within their own functions. To facilitate this, the Bank adopted a 'three lines of defence' mechanism. The line departments are the first line of defence in managing the risks and are responsible for identifying, mitigating and managing risks within their area of operations. These units are to ensure that their day-to-day activities are carried out within the established risk policies, procedures and limits, and risk issues are given due consideration. The second line of defence resides within the risk management function. This function assumes both the monitoring and advisory role, actively challenges assessments by the first line of defence, engages with risk owners/takers and looks at risk oversight across all risk types. The third line of defence resides within the Audit function. This function provides corporate assurance and verification of the efficacy in the implementation and overall validation of the Risk Management Framework.

Managing the Bank's financial risk

Financial Risk in the Bank is defined as 'the risks associated with the Bank's management of its financial assets and liabilities, including the financial sustainability of the current and future operations which include credit, market and liquidity risks'. The FRMC focuses on monitoring, reporting and assessing the sustainability of financial resources to support the Bank's operations, the management of financial exposures and commitments to external parties. It also provides an oversight function on key financial risk management processes. All financial risk exposures were consolidated and analysed in their totality in terms of their impact on the balance sheet and the need for provisioning, if necessary. In addition, the Bank's three year projections on major expenditure items were stress-tested based on various scenarios and further analysed and deliberated at the FRMC. Inputs for the stress-test model include the macroeconomic outlook and statistical assumptions to anticipate any significant variations in future expenditure.

Independent treasury risk management

The Treasury Risk Management section (TRMS) of the Investment Operations and Financial Market Department is responsible for managing the risks in international reserves in the key areas of market, credit and operational risk. These risks are monitored and managed to be within established policies and guidelines as approved by the Board of Directors. TRMS is independent of the investment activities and provides the necessary checks and balances through its direct reporting to a dedicated Deputy Governor.

Amidst the highly volatile and uncertain global financial markets in 2009, the overall credit exposure of international reserves remained low as the Bank's investments were focused on high grade assets. Investment transactions were conducted mainly with strong international financial institutions. For the Bank's investment portfolio, a review of the risk-return profile on the approved asset classes was also conducted in view of the significant changes in volatility and liquidity for some of the instruments. This was undertaken to ensure that the portfolio risk exposure of reserves remain within the risk tolerance of the Bank.

With the new CBA coming into effect, the investment guidelines for reserves management have also been revised to further strengthen the governance process and enhance its clarity covering all related reserves management activities. At the same time, a new performance attribution model was also implemented to allow more comprehensive and detailed risk-adjusted return analysis.

Moving forward, the Bank will continue to strengthen its risk management framework. Both the market and credit risk policies will be enhanced with granular analysis of risk factor and emerging trends. Further focus will also be placed on the governance framework to ensure continued effectiveness of the risk management process and the independent reporting line of the risk unit within the TRMS.

Managing the Bank's operational risk

Operational risk in the Bank is defined as 'the risk resulting from inadequate or failed systems, processes, people and external events leading to financial losses, reputational damage or inability to achieve business objectives'. In ensuring operational risks are well managed and amalgamated in the day-to-day operations, heads of departments continue to have direct responsibility in ensuring that risk management practices are integral in the daily operations and that all risks are sufficiently addressed. Key measures at an organisational level to address operational risks include effective budgetary controls, a sound procurement framework and a robust internal audit function that has a crucial role in monitoring operational risks.

In 2009, ORMC deliberated on significant risk issues affecting controls, efficiency and effectiveness of the main levers of the Bank's operations with specific focus on people risks and technology risks. Analysis and discussion on people risks covered a wide range of issues including on competencies and skills, manpower, adherence to the code of conduct and improvements in working conditions. The discussions on technology risks covered areas such as infrastructure, vendor management, security and access management as well as the relocation to the new data centre in 2009.

Business Continuity Management in enhancing Bank's readiness and response capabilities

During the year, much attention was given to the outbreak of Influenza A (H1N1). This external risk triggered some concern in mid-2009 given its implications on business operations as affected staff were required to observe the quarantine or 'work from home' requirements. In response to this risk, the Bank activated its Pandemic Influenza Plan and activated split operations for three months to minimize the risk of contagion whereby a number of staff from critical functions were stationed offsite for the period as a contingency measure. The Crisis Management Committee drew up a travel advisory for staff and monitored closely the severity of the pandemic on a weekly basis.

The Bank continued to strengthen the readiness and response capabilities of line departments to business disruptions. Periodic assessment of the Bank's Recovery Centre capacity was conducted through quarterly live-run exercises. Assessments were made to evaluate system readiness and the ability of the staff involved to respond appropriately to a crisis situation. Several initiatives were introduced such as the 'surprise people readiness' exercise which was also conducted for all critical departments. Selected staff were notified to head for the recovery centre with various modes of transport; car, taxis and train. To reinforce staff awareness, RMD organized Desktop Walkthrough Exercises for critical support departments so as to further enhance their Business Continuity Plans.

COMMUNICATIONS

Sustaining stakeholders' confidence in the challenging environment

The full impact of the global crisis was felt in 2009 and the Bank played a major role in ensuring the stability and sustainability of the economy and the financial system. The Bank continuously provided assessments of the global developments and highlighted their impact on Malaysia and the policy measures implemented to keep the business community and the public well informed.

The Bank increased the frequency of its communications on its assessment on the nation's economy and financial stability and continuously highlighted the various policy responses to strengthen public understanding and confidence. Communication efforts were also centred on the resilience of the financial system and the various measures undertaken to ensure continuous access to financing for businesses and households.

Monetary policy communications – key in anchoring monetary stability

The monetary policy statements (MPSs) released after each MPC meeting, contained a description of the Bank's assessment of global, regional and domestic economic and financial developments. It also provided the basis and considerations in determining the MPC's decision. Engagements with analysts and economists were also carried out to facilitate greater understanding of the Bank's policies and for the Bank to obtain feedback on issues, providing important information on areas of potential policy concern.

Greater engagements to sustain confidence during the period of uncertainty

In addition to MPSs, the Bank's communications outreach was expanded, through numerous engagements with the financial industry and businesses, the media and analysts as well as the public at large. These initiatives include extensive financial education to raise the level of financial literacy.

The Bank was actively involved in the dissemination of information on financing and related assistance to businesses. These included the RM2 billion SME Assistance Guarantee Scheme for viable SMEs adversely impacted by the economic slowdown and the establishment of the SME Credit Bureau towards ensuring greater access to credit for the SME sector. The establishment of Danajamin Nasional Berhad was also highlighted as part of efforts to ensure the continued flow of credit to businesses through the provision of financial guarantee insurance to private debt and Islamic securities issues. Attention was drawn to the re-commencement of operations and expanded scope of coverage of Corporate Debt Restructuring Committee, a voluntary forum for corporate borrowers and creditors to work out feasible debt resolutions without having to resort to legal proceedings.

Schemes supporting microfinance, including the RM200 million Micro Enterprise Fund (MEF) established by the Bank were publicised. As at 21 January 2010, the MEF had approved RM84.7 million of financing to 3,886 micro enterprises. Other initiatives to provide greater access to financing for local businesses, in particular to SMEs, include the Working Capital Guarantee Scheme (WCGS) and Industry Restructuring Financing Guarantee Scheme (IRFGS) which was part of the Second Stimulus Package. Although the guarantees covered RM5 billion of financing under each scheme, the WCGS was subsequently increased to RM7 billion (the additional RM2 billion reallocated from the IRFGS) benefiting 5,327 SMEs. The communication initiatives aimed at increasing the awareness of SME products and services.

The Bank carried out and participated actively in more than 90 road shows, by way of dialogues, exhibitions and seminars, across the nation to explain to the public and businesses on the availability of financing through the various mechanisms and alerting the public to be vigilant against various illegal deposit-taking and fraudulent schemes. It also provided advisory services to improve financial management and minimise the impact of the crisis on their businesses.

The Bank expanded its outreach to the public through three additional walk-in public service centers (BNMLINK) at branches of Kuala Terengganu, Kota Kinabalu and Kuching, bringing the total number of BNMLINK centers nationwide to six. The public can now also contact the Bank via SMS services and plans are underway to operate mobile LINK services in 2010. Reflecting the greater demand for the services offered by the Bank's Integrated Contact Centre (ICC), comprising BNMLINK, BNMTELELINK and the Complaints Management and Advisory Unit, the number of cases handled in 2009 showed a marked increase of more than 90% to 253,801 cases.

In addition to the ICC, the public also has access to the Financial Mediation Bureau (FMB) and the Credit Counseling and Debt Management Agency (AKPK). While FMB helps mediate disputes between customers and financial service providers, AKPK provides the public with free financial counseling and debt management services aimed at ensuring greater self-reliance in their financial affairs. In 2009, AKPK and FMB have dealt with 36,848 and 2,438 cases respectively, bringing the total to more than 39,000 cases.

Further strides in financial industry liberalisation

As the financial system remained intact despite the global crisis, the Bank confidently proceeded with further liberalisation of the financial sector to advance Malaysia's linkages with other parts of the world and to raise the level of performance of the financial system. Significant emphasis was placed on greater transparency of the liberalisation measures, with clear criteria and timelines to ensure the financial system continues to efficiently transition into this new phase of development.

Greater understanding on the roles of the central bank

The year 2009 also marked the 50th Anniversary of the Bank. Among others, the Bank hosted several international and regional high level meetings and conferences for leaders of the central banking and the financial fraternity to deliberate on current global and regional economic and financial issues. Several special supplements discussed the Bank's role in shaping the financial landscape and its contributions to nation building over the past 50 years.

With the coming into force of the new CBA, the Bank informed its stakeholders, including its staff, on how the new CBA has positioned the Bank to be in a greater state of readiness in the more challenging global environment. Greater clarity of mandates, enhanced financial stability powers, autonomy and the robust governance framework encapsulated in the CBA have set the stage for the Bank to deal more effectively with emerging risks and challenges.

The numerous briefings in conjunction with the release of the Annual Report 2008 and the Financial Stability and Payment Systems Report 2008 were another important communications channel for the Bank to engage with key stakeholders. These briefings served as a valuable platform in creating a better understanding of various economic and financial issues, as well as the economic and financial challenges on the domestic and global fronts.

The Bank's official website has also been enhanced to be more informative, comprehensive, structured and stakeholder-based to cater to the wide range of users. Reflecting these improvements, the number of visits to the website have increased significantly by about 40% to 4.2 million while the hits/pageviews rose by about 25% to more than 12.8 million. Moving forward, the website will be upgraded to broaden accessibility and to be equipped with interactivity and transactional features.

As part of staff engagement efforts, regular interactions were carried out with staff on the significance of the Bank's 3-year Business Plan, providing line of sight to the Bank's strategic focus and the required new work culture. These initiatives were important in ensuring greater alignment of staff and their roles in attaining the objectives of the Bank. Staff engagement with senior management has been stepped up with various face-to-face dialogue sessions on emerging economic and financial sector issues, in addition to the significant level of knowledge sharing activities through informal hi-tea sessions. The creation of a conducive communications environment has not only elevated the level of engagement but also contributed towards building an integrated internal team in the Bank.

ORGANISATIONAL DEVELOPMENT

Elevating Bank's Performance through Strategic Management

As a strategy-focused organisation, the Bank saw its performance driven orientation becoming more entrenched in 2009. With a new and robust strategic management process enabling the systematic planning and formulation of key priorities, execution and review of strategies at the organisational level, the Bank witnessed greater organisation-wide clarity and understanding of the Bank's objectives and goals. This was achieved through having greater line of sight on the Bank's strategic objectives by the staff and a higher degree of awareness of critical inter-linkages and inter-dependencies among the different sectors in the Bank. It has also facilitated efficient utilisation of resources to support the organisational goals. In addition, the enhanced integration of the strategic management and operational planning processes facilitated better prioritisation of financial resources to support the Bank's strategic objectives as outlined in the Business Plan. These were important factors in enabling the Bank to deliver its results during the year especially in light of more complex issues and challenges following the global financial crisis.

During the year, efforts were directed towards ensuring the effective implementation of the Business Plan. Robust mechanisms and processes were put in place to ensure the identified priorities, strategies and initiatives were effectively carried out within the specified timeframes through key performance indicators (KPIs) and other monitoring mechanisms that provided useful feedback on the progress in achieving the Bank's priorities. This is reinforced by a structured process of validation of key strategies and initiatives to ensure they remain relevant.

In line with this, the Bank conducted its strategic review of the Business Plan during the year to evaluate the overall performance towards achieving its strategic results. The strategic review process provided a platform for the management to deliberate and address both existing and potential issues that have implications on the achievement of the strategic results. The performance evaluation is based on a comprehensive assessment framework that combines both qualitative and quantitative outcome-based KPIs. This is also complemented by the use of proxy and process KPIs in gauging the achievement of outcomes that are not easily measurable in quantitative terms.

In ensuring that the Bank continues to remain effective in delivering its mandate, leadership development is given priority so as to enhance appreciation and internalisation of good governance and to enable the Bank to possess the necessary attributes to ensure the Bank is always in a state of readiness to face and address emerging issues and challenges. Towards this agenda, during the Senior Management Conference 2009, a simulation exercise was conducted to provide leaders of the Bank the opportunity to experience challenges that the Bank may face, set within a context of plausible future events. To successfully address the issues raised, participants were required to exhibit desired leadership attributes including having strategic insight, perseverance, sense of urgency and ability to manage conflicting issues, effective stakeholder management and the sense of collective accountability.

Building a High Performance Workforce
Given the dynamics of the human capital landscape, talent management continued to be a prevailing theme for the Bank in 2009. Efforts to align human capital practices to achieving the Bank's strategic objectives were enhanced during the year. Initiatives as outlined in the Integrated Human Capital Management framework (IHCM), the blueprint for the holistic development and enhancements of the Bank's human capital processes, continued to provide the impetus for talent management imperatives in 2009.

Ensuring job-fit for mission critical positions
A major focus in 2009 was to ensure that critical positions are held by the competent talents, where the talents will perform at their best to achieve the Bank's mandate and to create a healthy organisational climate. This entailed the robust and transparent assessment of talents to enhance job-fit for mission critical positions as well as strengthening the talent pool to ensure its readiness. The Bank continued to invest in both the profiling and development of its succession pool in promoting talent readiness, facilitated by the Leadership Profiling Centre (LPC) that evaluates the talent pool's potential for growth via a structured and robust profiling processes.

As the leadership strength in the Bank is being tightened and strengthened through more stringent criteria, coupled with focused leadership development and feedback, the Bank is also making concerted efforts to expand and reinforce its technical leadership capability. Career growth policies and frameworks were reviewed and enhanced to ensure the Bank's talent management strategies remain relevant. In support of the Bank's agenda to build a high performance workforce amidst the escalating performance standards, efforts are also being centered on enhancing clarity on the performance assessment ownership and processes, and reinforcing the differentiated reward and recognition structure.

Continuous building of talent pipeline
In addition to the strategic focus on leadership development, the Bank also continued with its scholarship programme aimed at nurturing young potential talent for the nation as well as deepening its own talent pipeline. The Bank Negara Malaysia Kijang Emas Scholarship award, among the most prestigious awards for

high potential young talents in the nation, has continued to inspire the most outstanding Sijil Pelajaran Malaysia (SPM) achievers nationwide. Five of the country's top achievers were accorded this award in 2009 to pursue their respective chosen fields of study. These scholars are required, as part of their contractual obligation, to return to Malaysia and serve the nation.

In addition to this award, the Bank continued sponsoring students with high potential to pursue their pre-university programmes at local colleges and first degree programmes at foreign universities in disciplines relevant to central banking. In 2009, 72 talents were awarded scholarships to pursue their education at the pre-university as well as first degree level whilst 20 excellent students at the Penilaian Menengah Rendah (PMR) level were awarded the Secondary School Scholarship award as part of the Bank's ongoing efforts to hasten early identification of its talent pool and to provide financial assistance to students from lower income families.

As part of its nation building efforts, the Bank also embarked on coordinating a programme to enhance the employability of graduates by providing them with attachment opportunities with participating companies across all economic sectors. Under 'Graduates Programme 500', more than 500 successful graduates nationwide were placed, with the assistance of industry players, with companies for on-the-job training exposures for a period of two years. The programme includes development interventions focused on their skills based on industry feedback.

As a result of the restructuring and realignment of roles bank-wide, the total staff strength in the Bank increased by 3.60% to 2,709 as at end 2009 as compared with 2,616 as at end 2008, while the attrition rate due to retirement and resignation remained at four percent. The ratio of executive to non-executive staff remained at 3:2 and concerted efforts to focus on strengthening and deepening the professional and technical talent pool will remain a key agenda for the Bank.

Improving Bank's Performance through Learning and Knowledge Management

In 2009, learning and knowledge management (L&KM) initiatives continued to provide support for human capital development in the Bank through improved alignment in meeting the business needs of line departments, focusing on performance and business impact. The effectiveness of the L&KM initiative was further augmented, particularly with the new role-based organisational structure adopted by the Human Capital Development Centre (HCDC). The principle of value creation for line departments was embedded in the L&KM initiatives undertaken by HCDC, through the learning products and services provided.

Designing and implementing learning solutions that fulfil Bank's needs

In meeting the demands for development solutions that meet the requirements of the knowledge workers in the Bank, efforts were directed towards obtaining an accurate view of the development requirements of the Bank staff at all working levels. Hence, the number of L&KM demands that had been serviced in the form of design and implementation of customised solutions increased significantly in 2009. Apart from this, overall workforce competencies were also improved through 129 L&KM bank-wide events, ensuring positive development gains and the transfer of knowledge at the workplace.

In designing learning solutions, HCDC focused on the effectiveness and its impact to the workplace. A blended learning approach with a combination of learning methods was emphasised. Besides attending the typical classroom sessions, participants underwent a range of learning and knowledge interventions such as pre-session readings, viewing of related visual materials, e-learning solutions and were given opportunities to apply their new knowledge and skills at the workplace with coaching from their supervisors. In addition, various methods and tools were employed to address specific competency gaps. These included establishing cross-functional work teams, communities of practice and peer-assist groups to enhance collaboration across divisions and department boundaries, attachments as well as integrating after-action-reviews and storytelling into work processes to capture and share knowledge.

A competency-based core central banking curriculum was developed based on the Bank's competency model. With the curriculum in place, HCDC was able to design learning solutions that were customised to the learning needs of the organisation. During the year, HCDC successfully tested the robustness of the curriculum through a pilot programme conducted in close collaboration with subject matter experts from line departments. As part of ongoing efforts to align learning solutions to the learning needs of the Bank, focus also remained centred on enhancing central banking knowledge within the Bank. Emphasis was given to improvements in the design and implementation of flagship programmes. These programmes included, among others, the Central Banking Series, Banking Supervision Foundations Course (BSFC), Insurance Supervision Course (ISC) and Islamic Finance Course for Finance Regulators (IFFR). Apart from flagship programmes, the bank-wide learning programmes also covered a wide spectrum of knowledge areas to facilitate the generic and behavioural competencies requirements for the staff of the Bank. The quality of these programmes were measured and found to be satisfactory in meeting the intended objectives.

HCDC also introduced several new learning programmes in 2009. The BNM Executive Programme (BNMEP) was conceived and designed to accelerate the time-to-competence for all new hires of the Bank. The six-month programme comprises four main modules including on-boarding, personal development, fundamentals of central banking, as well as a four-month attachment programme. To ensure a healthy leadership pipeline, the Bank embarked on a new Leadership Development Blueprint (LDB) which aims to develop leadership effectiveness, and transition leaders into different phases of leadership to ensure a more healthy and ready leadership pool for the Bank.

Knowledge Management initiatives in promoting knowledge sharing culture

In 2009, the Knowledge Management Centre (KMC) continued to provide a comprehensive range of services and relevant resources in the form of physical collections and online information resources. The KMC offered value-added services such as information scanning, information alerts and repackaging of information to meet specific needs of stakeholders. In fostering collaboration, HCDC had taken the initiative to introduce and promote a range of L&KM tools. Tools such as World Café, Open Space Technology, After Action Review, Blogs and Wikis were made readily available.

Enhancements to the Learning Management System (LMS) were made in 2009 in terms of enriching its content and improving its infrastructure. E-learning contents were expanded to provide a broader selection of courses for on-demand learning while registration for all courses and events was centralised and captured in LMS. Similarly, learning programmes offered by HCDC were uploaded into the LMS for easy access and reference, and the annual directory of L&KM was lodged and opened for access by the Bank staff in LMS. These initiatives formed part of HCDC's strategy to inculcate the culture of self-directed development, by using the LMS as a tool to manage development, as well as making e-learning an effective complement to classroom courses.

Guided by the agenda of inculcating a knowledge-sharing culture within the Bank, new KM events have been introduced. The 'Central Banking Tea Talks' series were positioned as a series of sharing sessions held in an informal setting which encourage learning and sharing between the speaker and the staff. The series provide a platform for the Bank's subject matter experts to share their knowledge on current issues of interest with their colleagues within the Bank. In 2009, five sessions of Tea Talks were held. In addition, the 'Conversations with Senior Management' programme was initiated as a dialogue session to provide an opportunity for Bank staff at various levels to exchange views with the Senior Management of the Bank.

Engagement with the L&KM agents at the line departments was also an area that was given attention. Several engagement events were organised in 2009 such as the Training Managers (TMs) and Knowledge Management Officers (KMOs) day, informal session with the KMOs, L&KM tools hands-on sessions with the TMs and KMOs as well as establishing a Community of Practice (CoP) among the TMs and KMOs. These efforts were aimed at fostering a healthy and effective working relationship with stakeholders while at the same time creating higher awareness of L&KM products and services for adoption of use at the line departments. Other initiatives by HCDC in enhancing the knowledge culture included the Knowledge Fair, the Book Fairs and the 'Bulan Bahasa Kebangsaan' celebration.

Technical Assistance and Collaboration Programmes with External Agencies

In 2009, the Bank also offered a wide range of international learning programmes. Programmes offered under the auspices of the Government-sponsored Malaysian Technical Cooperation Programme (MTCP) included Banking and Insurance Supervision courses, Islamic Finance for Regulators and the Intermediate and Advanced Central Banking courses. The Bank also collaborated with the Islamic Development Bank in organising the popular Fundamentals of Islamic Finance Course (FIFC) twice during 2009. The FIFC was attended by central bankers, Ministry of Finance officials and securities commission regulators to enhance their knowledge and skills in Islamic finance operations, Shariah and regulatory framework towards effective implementation of a resilient Islamic financial system. A special workshop in Islamic finance was organised with BAFIN (The Federal Financial Supervisory Authority) of Germany where there is strong interest amongst banking supervisors to appreciate the features of Islamic finance as it continues to gain increased interest in the European financial system.

The Bank also focused on two other areas for its international technical assistance, namely institutional capacity building and financial inclusion. With respect to institutional capacity building, the programmes included organisational development and credit bureau for risk management. With respect to financial inclusion, the Bank conducted the Financial Inclusion Advisers programme for microfinance practitioners in Lusaka, Zambia, and organised a Microfinance Policymakers Forum for Asian regulators on the policy challenges posed by branchless banking for purposes of increasing access to financial services for the poor and those living in remote areas. A total of 279 international participants attended the international programmes conducted during 2009.

In addition, the Bank received 75 ad-hoc requests for knowledge sharing during 2009, and had the opportunity to engage 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 covering monetary and financial system stability, Islamic finance, currency management, talent management and central bank modernisation.

The Bank's initiatives in international technical cooperation stress the importance of sharing knowledge on central banking practices, and building collaborative relationships with other central bankers from developing economies in the face of globalisation and regional integration.

ICT Management in Elevating Bank's Effectiveness

Information and Communications Technology (ICT) continued to function as an important enabler to achieve the Bank's strategic outcomes, serving as a key platform in supporting greater organisational effectiveness and the extension of the Bank's reach to its stakeholders.

The Bank's technology infrastructure has been enhanced and further expanded to enable integrated and efficient communication channels between the Bank and its stakeholders. In this regard, infrastructure to extend workplace mobility through accessibility to wireless Internet (Wi-Fi) in the public areas within the Bank's premises has been implemented progressively. On the external front, the efficiency and responsiveness of the Bank to the public was further enhanced by the deployment of Integrated Contact Centre (ICC) Customer Relationship Management to all the Bank's branches. An automated short-messaging service (SMS) was also implemented to complement the existing public service channels.

In 2009, the Bank also implemented several landmark ICT solutions that contributed towards the achievement of key objectives of the Bank. One key achievement is the successful implementation of nationwide image-based cheque-clearing, resulting in substantial improvements to the clearing process for the financial industry. With the advent of eSPICK, customers and businesses benefited from the speedier and more efficient cheque clearing system especially in the timing of the availability of funds from the deposit of outstation cheques, cheque conversion facility and the return of unpaid cheques to payees. Under eSPICK, outstation as well as local cheques are cleared on the same day and funds made available as early as the next business day, compared to between 5 to 8 business days for outstation cheques previously. Express clearing of cheques is also available under eSPICK which provides for same day clearing and availability of funds. The Bank also augmented the capability of its debt securities depository in the Real-Time Electronic Transfer on Funds and Securities (RENTAS) to support allotment, interest and redemption of foreign currency denominated bonds, completing the end-to-end ICT infrastructure for primary issuance, settlement of secondary trading and as depository of foreign currency denominated bonds. This ICT infrastructure had facilitated the first foreign bond issuance and deposit in RENTAS, marking an important step towards positioning RENTAS as a regional and international depository.

In its effort to enhance the information management infrastructure, the Bank has embarked on initiatives to provide a platform that is integrated and agile for better data sourcing, processing, delivery and visibility. The infrastructure will integrate financial and economic statistical data that provide comprehensive and consolidated views of the data. The architecture will comprise an enterprise data warehouse supported by centralised metadata repository and enterprise data model, information dashboard and a new data submission system using a standard reporting framework. As part of the initiative, the Bank implemented a robust infrastructure with the capacity to enable high-volume credit data analysis to facilitate better and more timely identification of emerging risks and vulnerabilities of the financial institutions and the financial system.

The use of technology solutions and leading-edge infrastructure has evolved into a strategic leverage to advance the Bank's agenda and aspirations. The journey to operationalise the new Data Centre in Cyberjaya was commenced in 2009, with relocation activities progressing as planned. Upon the migration of the infrastructure capabilities to the future-state architecture in year 2010, the new Data Centre is now equipped with technological specifications designed to cater for future business requirements, with optimum level of performance, agility and resiliency aligned with the aim of sustaining continuous operational excellence for the growing portfolio of ICT systems in the Bank.

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 2009

I have audited the financial statements of Bank Negara Malaysia for the year ended 31 December 2009. These financial statements are the responsibility of the management. My responsibility is to audit and to express an opinion on these financial statements.

2. The audit has been carried out in accordance with the Audit Act 1957 and in conformity with approved standards on auditing. Those standards require the audit be planned and performed to obtain reasonable assurance that the financial statements are free of material misstatement or omission. The audit includes examining on a test basis, evidence supporting the amounts and disclosures in the financial statements. It also includes assessment of the accounting principles used, significant estimates made by the management as well as evaluating the overall presentation of the financial statements. I believe that the audit provides a reasonable basis for my opinion.

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 2009 and of the results of its operations for the year ended in accordance with the approved accounting standards.

(TAN SRI DATO' SETIA HAJI AMBRIN BIN BUANG)
AUDITOR GENERAL
MALAYSIA

PUTRAJAYA
12 MARCH 2010

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 2009 and of the results of operations for the year ended on that date.

On behalf of the Board,

ZETI AKHTAR AZIZ
CHAIRMAN

11 MARCH 2010
KUALA LUMPUR

On behalf of the Board,

OH SIEW NAM
DIRECTOR

11 MARCH 2010
KUALA LUMPUR

DECLARATION BY THE OFFICER PRIMARILY RESPONSIBLE FOR THE FINANCIAL MANAGEMENT OF BANK NEGARA MALAYSIA

I, Rafiza Ghazali, 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 11 March 2010.)

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

PESURUHJAYA SUMPAH
No: W 027
Nama : NG LEONG HUAT
MALAYSIA

Bank Negara Malaysia

Balance Sheet as at 31 December 2009

		2009	2008
		RM	RM
ASSETS	**Note**		
Gold and Foreign Exchange	3	322,505,629,648	315,554,271,994
International Monetary Fund Reserve Position		1,515,842,594	1,127,065,750
Holdings of Special Drawing Rights		7,279,175,067	786,401,257
Malaysian Government Papers	4	2,683,093,250	2,525,239,300
Deposits with Financial Institutions	5	9,373,175,000	4,507,787,500
Loans and Advances	6	12,407,481,804	12,516,545,727
Other Assets	7	7,213,305,329	7,505,008,921
Total Assets		**362,977,702,692**	**344,522,320,449**
LIABILITIES AND CAPITAL			
Currency in Circulation		51,138,567,538	48,042,855,068
Deposits by: Financial Institutions		181,535,107,206	184,136,298,017
Federal Government		18,641,169,858	11,155,942,757
Others	8	1,270,868,081	373,848,344
Bank Negara Papers		33,357,434,443	43,710,213,247
Allocation of Special Drawing Rights	9	7,231,066,765	742,639,517
Other Liabilities	10	21,710,810,087	24,604,565,308
Total Liabilities		314,885,023,978	312,766,362,258
Paid-up Capital	11	100,000,000	100,000,000
General Reserve Fund	12	13,478,068,329	11,976,653,686
Other Reserves	13	34,514,610,385	19,679,304,505
Total Capital		48,092,678,714	31,755,958,191
Total Liabilities and Capital		**362,977,702,692**	**344,522,320,449**

Notes on the following pages form part of these financial statements.

Bank Negara Malaysia

Income Statement for the Year Ended 31 December 2009

	Note	2009 RM	2008 RM
Total Income	14	**9,826,516,615**	**8,158,398,385**
Less:			
Recurring Expenditure	15	1,071,025,015	939,599,724
Development Expenditure	16	1,085,627,775	709,518,486
Total Expenditure		**2,156,652,790**	**1,649,118,210**
Net Profit		**7,669,863,825**	**6,509,280,175**

Profit and Loss Appropriation Statement for the Year Ended 31 December 2009

		2009 RM	2008 RM
Net Profit		**7,669,863,825**	**6,509,280,175**
Transfer to Other Reserves	17	4,168,449,182	3,832,305,418
Transfer to General Reserve Fund		1,501,414,643	1,176,974,757
Amount Payable to Federal Government		2,000,000,000	1,500,000,000
		7,669,863,825	**6,509,280,175**

Notes on the following pages form part of these financial statements.

Notes to the Financial Statements - 31 December 2009

1. **Principal Activities of the Bank**

The principal objects of the Bank are to promote monetary stability and financial stability conducive to the sustainable growth of the Malaysian economy. In this regard, the Bank's primary functions are as follows:

(a) to formulate and conduct monetary policy in Malaysia;
(b) to issue currency in Malaysia;
(c) to regulate and supervise financial institutions which are subject to the laws enforced by the Bank;
(d) to provide oversight over money and foreign exchange markets;
(e) to exercise oversight over payment systems;
(f) to promote a sound, progressive and inclusive financial system;
(g) to hold and manage the foreign reserves of Malaysia;
(h) to promote an exchange rate regime consistent with the fundamentals of the economy; and
(i) to act as financial adviser, banker and financial agent of the 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 2009 and applicable Malaysian Financial Reporting Standards (FRS). Section 10 of the Central Bank of Malaysia Act 2009 provides that the Bank, in preparing its financial statements, shall comply with accounting standards to the extent that it is, in the opinion of the Bank, appropriate to do so, having regard to the objects and functions 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 at 31 December 2009 was RM331,300.6 million equivalent to USD96,695.1 million.

2.4 **Securities and Investments**

Securities and investments are stated mainly at cost and provisions have been made for diminution in value as at 31 December 2009.

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 **Fixed Assets**

The capital expenditure incurred on fixed assets are written down to nominal value or written off completely in the year of acquisition.

2.7 **Net Profit**

The net profit of the Bank is appropriated in accordance with section 7 of the Central Bank of Malaysia Act 2009 and only realised gains are made available for dividend distribution.

3. **Gold and Foreign Exchange**

	2009 RM	**2008 RM**
Foreign Securities	277,872,235,367	282,566,246,554
Foreign Deposits	14,655,589,658	10,860,543,730
Balances with Other Central Banks, Bank for International Settlements (BIS) and International Monetary Fund (IMF)	3,765,861,668	3,592,893,233
Others	26,211,942,955	18,534,588,477
	322,505,629,648	315,554,271,994

4. **Malaysian Government Papers**

	2009 RM	2008 RM
Malaysian Government Securities	2,683,093,250	2,525,239,300

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 and section 75(i) of the Central Bank of Malaysia Act 2009[1].

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[1].

7. **Other Assets**
Other assets include investments in shares and bonds of RM6,855,216,924 acquired under section 30(1)(j), section 30(1)(oo)(i) and section 30A(1)(c) of the Central Bank of Malaysia Act 1958 and section 48(1) of the Central Bank of Malaysia Act 2009[1].

8. **Deposits by Others**
A substantial part of these deposits comprises deposits from public 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. Following the 2009 General and Special Allocation of SDR by the IMF, the Bank's net cumulative allocation of SDR had increased to RM7,231,066,765 equivalent to SDR1,346,143,721.

10. **Other Liabilities**
Other liabilities include mainly placements by financial institutions under the repurchase agreements.

11. **Paid-up Capital**
The paid-up capital of RM100 million is owned by the Government of Malaysia.

12. **General Reserve Fund**

	2009 RM	2008 RM
As at 1 January	11,976,653,686	10,799,678,929
Transfer from Net Profit	1,501,414,643	1,176,974,757
As at 31 December	13,478,068,329	11,976,653,686

[1] Pursuant to section 100 of the Central Bank of Malaysia Act 2009, transactions or arrangements made under the Central Bank of Malaysia Act 1958 are deemed to have been made under the Central Bank of Malaysia Act 2009.

13. **Other Reserves**
Other reserves comprise the Exchange Rate Fluctuation Reserve, Revaluation Reserve and 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 of the Central Bank of Malaysia Act 2009.

18. **Contingencies and Commitments**

18.1 **Contingent Assets**
Total contingent assets as at 31 December 2009 amounted to RM1,300,000,000. These comprise the Bank's total contributions to International Centre for Leadership in Finance (ICLIF) Trust Fund and International Centre for Education in Islamic Finance (INCEIF) Trust Fund to finance activities related to training, research and development of human resource on banking and financial services managed by ICLIF and INCEIF. It is provided in the Trust Deeds that the total contributions will be returned to the Bank when the Centres become self-sufficient in the future.

18.2 **Contingent Liabilities**
Total contingent liabilities as at 31 December 2009 amounted to RM6,705,152,257. These comprise the following:

(a) an amount of RM6,640,289,100 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 RM64,863,157 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.

18.3 **Commitments**

Total commitments as at 31 December 2009 comprise the following:

(a) **New Arrangements to Borrow by IMF**

The Bank has participated in the New Arrangements to Borrow (NAB), a set of credit arrangements between the IMF and its member countries to provide supplementary source of financing to IMF for the purpose of safeguarding the stability of the international monetary system. As at 31 December 2009, the Bank's total commitment under the NAB credit arrangement amounted to SDR340,000,000 (equivalent to RM1,826,374,600). However, for the financial year ended 31 December 2009, there was no call on the NAB by the IMF.

(b) **ASEAN Swap Arrangement**

The Bank has participated in the multilateral ASEAN Swap Arrangement (ASA) together with other ASEAN central banks and monetary authorities to provide short-term foreign currency liquidity support to member countries with balance of payments difficulties. As at 31 December 2009, the Bank's total commitment and eligible maximum drawdown amounted to USD300 million (equivalent to RM1 billion) and USD600 million (equivalent to RM2.1 billion) respectively. However, for the financial year ended 31 December 2009, there was no request for liquidity support under ASA from any member country.

(c) **Bilateral Swap Arrangement Agreement**

On 7 January 2009, the Bank renewed the Bilateral Swap Arrangement (BSA) Agreement with the Bank of Korea under the Chiang Mai Initiative. Under the BSA agreement, each central bank can obtain financial support in US dollar up to USD1.5 billion (equivalent to RM5.1 billion) through swap arrangements against their respective local currencies. For the financial year ended 31 December 2009, there was no request to activate the BSA.

19. **Financial Risk Management**

The Reserve Management Committee oversees treasury and investment risks in the management of reserves and to ensure that the following risks are contained within acceptable levels:

(a) **Market Risk**

Market risk is the exposure of the Bank's financial position to adverse movements in market prices such as interest rates and foreign exchange rates. The management of market risk is governed by the benchmark policy approved by the Board of Directors which reflects the long-term investment objectives and acceptable risk-return profile. Within the benchmark policy, the Board of Directors allows `active risk´ to be taken through investments that deviate from the benchmark. This `active risk´ is controlled through a `tracking error´ limit. Sensitivity analysis and stress testing is also undertaken to assess potential mark-to-market losses on the reserves due to unexpected fluctuations and volatility in the market.

(b) **Credit Risk**

The credit risk on reserves is the risk that a counter party, either financial institutions or issuers, fails to perform its contractual obligation to the Bank. A comprehensive rating-based credit risk framework approved by the Board of Directors governs the permissible investment universe of the Bank. Having such a framework in place also strengthens the Bank's operational efficiency in this area and ensures the reserves are invested only with high credit quality counterparties or issuers. The policies and continuous assessment of credit exposures ensures the objective of capital preservation is met.

(c) **Operational Risk**

Operational risk on treasury operation is the risk of financial loss due to failed internal process, inadequate controls and procedures, and gaps in skill-sets. Operational risk is mitigated through a strong and robust governance framework and effective implementation of risk controls and limits.

20. **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 current foreign exchange administration rules are prudential measures to promote monetary and financial stability conducive to the sustainable growth of the economy and safeguarding the balance of payments position as well as safeguarding against shocks. The rules, however, have been progressively liberalised with significant liberalisations made in 2005 and 2007 to enhance business efficiency and promote foreign direct investments.

I. Foreign Exchange Administration Rules Applicable to NON-RESIDENTS[1]

FOREIGN DIRECT AND PORTFOLIO INVESTMENTS BY NON-RESIDENTS	
• Purchase of ringgit assets[2]	• Non-residents are free to purchase any ringgit assets including ringgit-denominated bonds/sukuk issued by non-residents in Malaysia
• Sourcing ringgit for settlement of ringgit assets	• Settlement for the investment in ringgit assets can be sourced from: ✓ Non-residents' own External Accounts[3]; ✓ Sale of foreign currency on spot or forward basis, with licensed onshore banks[4] or overseas branches appointed by licensed onshore banks; or ✓ Borrowing obtained from licensed onshore banks, resident companies[5] and individuals[6] to finance real sector activities in Malaysia
• Onshore borrowing	• Free to borrow any amount in foreign currency from licensed onshore banks and licensed International Islamic Banks • Free to borrow in ringgit of any amount from licensed onshore banks, resident companies and individuals to finance real sector activities in Malaysia, including financing the purchase of ringgit assets • 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 • Repatriation, however, must be made in foreign currency
• Hedging	• Free to hedge the exposure arising from investment in ringgit assets made on or after 1 April 2005 with the licensed onshore banks or overseas branches appointed by licensed onshore banks

1 **Non-resident:**
- An overseas branch, subsidiary, regional office, sales office or representative office of a resident company;
- Embassies, Consulates, High Commissions, supranational or international organisations;
- A Malaysian citizen who has obtained permanent resident status of a country or territory outside Malaysia and is residing outside Malaysia; and
- Any other person as may be specified by the Controller of Foreign Exchange to be a non-resident

2 **Ringgit assets** include:
- Ringgit-denominated securities, private debt securities, Cagamas bonds or notes, Malaysian Government Securities, Treasury Bills, shares and warrants;
- Derivatives traded on Bursa Malaysia (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; and
- Immovable properties in Malaysia

3 External Accounts are ringgit accounts maintained with licensed onshore banks by or for non-residents
4 Licensed onshore banks refer to licensed commercial banks, licensed Islamic banks and licensed investment banks
5 Resident companies include limited partnerships and legal entities other than companies such as co-operatives and charitable organisations
6 Resident individuals include sole proprietorships, general partnerships and partnerships with general and limited partners

<table>
<tr><th colspan="2">INVESTMENT IN IMMOVABLE PROPERTIES BY NON-RESIDENTS</th></tr>
<tr><td>• Purchase of immovable property</td><td>• Free to purchase residential and commercial properties in Malaysia</td></tr>
<tr><td>• Onshore borrowing</td><td>• Free to borrow any amount of ringgit or foreign currency to finance or refinance the purchase of residential and commercial properties in Malaysia, except for purchase of land only</td></tr>
<tr><th colspan="2">LENDING IN RINGGIT AND FOREIGN CURRENCY BY NON-RESIDENTS TO RESIDENTS</th></tr>
<tr><td>• Ringgit lending</td><td></td></tr>
<tr><td>✓ By non-resident non-bank parent companies[7]</td><td>• Free to lend any amount of ringgit to resident subsidiaries to finance real sector activities in Malaysia</td></tr>
<tr><td>✓ 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</td></tr>
<tr><td>• Foreign currency lending</td><td></td></tr>
<tr><td>✓ By non-resident non-bank parent companies</td><td>• Free to lend any amount in foreign currency to resident subsidiaries in Malaysia</td></tr>
<tr><td>✓ By other non-resident non-bank companies or individuals</td><td>• 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 of Foreign Exchange for borrowing exceeding the limits</td></tr>
<tr><th colspan="2">BORROWING BY NON-RESIDENTS FROM RESIDENTS</th></tr>
<tr><td>• Foreign currency borrowing from licensed onshore banks and licensed International Islamic Banks</td><td>• Free to borrow any amount of foreign currency from licensed onshore banks and licensed International Islamic Banks</td></tr>
</table>

[7] A non-resident non-bank parent company refers to -
(a) non-resident company with more than 50% shareholding in a resident company; or
(b) the ultimate non-resident parent company (which is not a bank, an investment holding company owned by a bank or a stockbroking company) of the resident company

<table>
<tr>
<td>• Foreign currency borrowing from resident non-bank companies or individuals</td>
<td>• 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*:
✓ Resident individual
✓ Resident company</td><td>Through conversion of ringgit up to:
✓ RM1 million in aggregate per calendar year
✓ 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>
<tr>
<td>• Ringgit borrowing from licensed onshore banks, resident non-bank companies and individuals</td>
<td>• Free to obtain ringgit borrowing from licensed onshore banks, resident non-bank companies and individuals as follows:
✓ By non-resident (other than stockbrocking companies and banks) to:
➢ Finance activities in the real sector in Malaysia; and
➢ Finance or refinance the purchase of residential and commercial properties in Malaysia
✓ By non-resident stockbrocking companies 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
✓ By non-resident (other than stockbrocking companies and banks) from licensed onshore banks and resident stockbrocking companies for margin financing
✓ By non-resident individuals from resident insurance companies up to the cash surrender value of the insurance policies purchased by the non-residents</td>
</tr>
<tr>
<th colspan="2">ISSUANCE OF RINGGIT AND FOREIGN CURRENCY DENOMINATED BONDS/SUKUK IN MALAYSIA BY NON-RESIDENTS</th>
</tr>
<tr>
<td>• Issuance of ringgit or foreign currency denominated bonds/sukuk</td>
<td>• 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</td>
</tr>
</table>

• Utilisation of bond/sukuk proceeds	• Proceeds from the issuance of bonds/sukuk are allowed to be used onshore or offshore • Ringgit-denominated bond/sukuk proceeds to be used offshore have to be converted into foreign currency with the licensed onshore banks
• Hedging	• Issuers to hedge exchange rate and interest/profit rate exposure arising from the issuance of ringgit-denominated bonds/sukuk with the licensed onshore banks if the proceeds are to be used offshore • Non-resident investors of the bonds/sukuk are free to hedge exchange rate and interest/profit rate exposure with licensed onshore banks
• Guidelines for issuance	• Specific details on guidelines for the issuance of ringgit and foreign currency denominated bonds/sukuk in Malaysia can be obtained at any of the following web-site addresses: ✓ http://www.mifc.com ✓ http://www.bnm.gov.my/fxadmin ✓ http://www.sc.com.my
HEDGING BY NON-RESIDENTS	
• Hedging of ringgit assets	• Free to hedge with licensed onshore banks, exchange rate and interest/profit 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: ✓ Ringgit accounts with licensed onshore banks; and ✓ Foreign currency accounts with licensed onshore banks and licensed International Islamic Banks • 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** ✓ Free to convert ringgit into foreign currency with licensed onshore banks for repatriation abroad; ✓ Free to pay a resident for any purpose, except for the following: ➢ Payment for the import of goods and services; ➢ Lending in ringgit to residents other than as permitted by the Controller of Foreign Exchange; and ➢ Payment on behalf of a third party ✓ Free to pay to another non-resident's External Account for settlement of ringgit assets • **Foreign currency accounts** ✓ Free to repatriate; and ✓ Free to pay a resident for any purpose including for settlement of goods and services

IMPORT AND EXPORT OF RINGGIT AND FOREIGN CURRENCY 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
• 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

II. Foreign Exchange Administration Rules Applicable to RESIDENTS[8]

INVESTMENTS IN FOREIGN CURRENCY ASSETS[9] BY RESIDENTS
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

[8] **Resident:**
- A citizen of Malaysia, excluding a citizen who has obtained permanent resident status of a territory outside Malaysia and is residing outside Malaysia;
- A non-citizen who has obtained permanent resident status in Malaysia and is ordinarily residing in Malaysia;
- A body corporate incorporated or established, or registered with or approved by any authority, in Malaysia;
- An unincorporated body registered with or approved by any authority in Malaysia;
- The Government or any State Government; or
- Any other person as may be specified by the Controller of Foreign Exchange to be a resident

[9] **Foreign currency assets** include:
- Investment in foreign currency securities;
- Loans to non-residents;
- Foreign currency deposits onshore or offshore; and
- Investment in approved foreign currency products offered by licensed onshore banks, licensed International Islamic Banks and any residents permitted by the Controller of Foreign Exchange

<table>
<tr><td rowspan="3">• Investment in foreign currency assets</td><td colspan="2">• No limit for residents without domestic ringgit borrowing
• Residents with domestic ringgit borrowing[10] are allowed to invest as follows:</td></tr>
<tr><td>Resident individuals[11]</td><td>• No limit if funded by own foreign currency funds retained onshore or offshore;
• Up to full amount of permitted foreign currency borrowing; and
• Up to RM1 million in aggregate per calendar year if funded from conversion of ringgit</td></tr>
<tr><td>Resident companies[12]</td><td>• No limit if funded by own foreign currency funds retained onshore or offshore;
• No limit if funded from proceeds of listing through initial public offering on:
- Bursa Malaysia; or
- Foreign stock exchanges
• Up to the full amount of permitted foreign currency borrowing; and
• Up to RM50 million equivalent in aggregate on a corporate group basis per calendar year if funded from conversion of ringgit</td></tr>
<tr><td>• Investment in foreign currency assets by resident institutional investors
✓ Unit trust management companies
✓ Fund management companies
✓ Insurers and takaful operators</td><td colspan="2">• Unit trust management companies:
✓ Investment of Islamic funds
➢ No limit
✓ Investment of conventional funds
Foreign currency-denominated funds
➢ 100% of the net asset value (NAV)
Ringgit-denominated funds
➢ 100% of NAV attributed to non-residents and residents without domestic ringgit borrowing; and
➢ 50% of NAV attributed to residents with domestic ringgit borrowing</td></tr>
</table>

[10] Domestic ringgit borrowing 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

[11] Resident individuals include sole proprietorships, general partnerships and partnerships with general and limited partners

[12] Resident companies include limited partnerships and entities other than companies such as co-operatives and charitable organisations

	• Fund management companies: ✓ Funds mandated to be invested in Shariah compliant assets ➢ No limit ✓ Funds mandated to be invested in non-Shariah compliant assets **Foreign currency funds** ➢ No limit **Ringgit funds** ➢ 100% of total funds managed for non-residents and residents without domestic ringgit borrowing; and ➢ 50% of total funds managed for residents with domestic ringgit borrowing • Insurers and takaful operators, including international currency business unit of takaful operators and international takaful operators: **Foreign currency-denominated funds** ➢ 100% of NAV of foreign currency investment-linked funds offered to residents and non-residents **Ringgit-denominated funds** ➢ 100% of NAV of investment-linked funds offered to non-residents and residents without domestic ringgit borrowing; ➢ 50% of NAV of investment-linked funds offered to residents with domestic ringgit borrowing; ➢ 10% of margin of solvency for insurers; and ➢ 5% of total assets for takaful operators
• Payment for purchase of foreign currency assets	• Offshore foreign currency assets: ✓ Payment must be made in foreign currency ✓ The foreign currency may be sourced from conversion of ringgit with licensed onshore banks[13] or own foreign currency funds • Onshore foreign currency assets offered by licensed onshore banks, licensed International Islamic Banks or entities[14] approved by the Controller of Foreign Exchange: ✓ Payment may be in foreign currency or in 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 with licensed onshore banks • Free to retain the proceeds in foreign currency accounts
• Hedging	• Free to hedge with licensed onshore banks and licensed International Islamic Banks for investment in foreign currency assets based on firm underlying commitment • Hedging involving ringgit shall only be undertaken with licensed onshore banks

[13] Licensed onshore banks refer to licensed commercial banks, licensed Islamic banks and licensed investment banks

[14] Example: (a) Unit trust companies offering foreign currency unit trust funds; and
(b) Bursa Malaysia for trading of foreign currency derivative products such as CPO futures

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: ✓ Licensed onshore banks; ✓ Licensed International Islamic Banks; and ✓ Non-residents • Trade financing involving export shall only be obtained from licensed onshore banks • Allowed to refinance outstanding approved foreign currency borrowing
✓ Resident companies	• Free to borrow any amount in foreign currency from: ✓ Non-resident non-bank parent companies[15]; ✓ Other resident companies within the same corporate group[16] in Malaysia; ✓ Licensed onshore banks; and ✓ Licensed International Islamic Banks • Free to borrow in foreign currency up to the equivalent of RM100 million in aggregate on a corporate group basis: ✓ From non-residents (other than non-resident non-bank parent companies); and ✓ Through the issuance of foreign currency denominated bonds onshore and offshore • Free to borrow any amount of foreign currency supplier's credit from non-resident suppliers • Allowed to refinance outstanding approved foreign currency borrowing
• 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 International Islamic Banks (other than trade financing facility involving export) • 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 • 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

[15] 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

[16] Corporate group refers to a group of companies with parent-subsidiary relationship in Malaysia

• Hedging	• Free to hedge drawdown and repayment of foreign currency borrowing with licensed onshore banks and licensed International Islamic Banks • 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 real sector activities in Malaysia • Free to borrow up to RM1 million in aggregate from other non-resident non-bank companies or individuals for use 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: ✓ Finance real sector activities in Malaysia; and ✓ Finance or refinance the purchase of residential and commercial properties in Malaysia
✓ Licensed onshore banks	• Free to lend any amount in ringgit to: ✓ Non-resident non-bank companies and individuals (other than stockbroking companies and banks): ➢ To finance real sector activities in Malaysia; ➢ For margin financing; and ➢ To finance or refinance the purchase of residential and commercial properties in Malaysia ✓ 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: ✓ Ordinary shares, including bonus and rights issues; ✓ Irredeemable preference shares; and ✓ Private debt securities • 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	• Free to issue 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 • Free to use for investment in foreign currency assets provided the issuer's total investment does not exceed RM50 million equivalent in aggregate on a corporate group basis per calendar year
✓ Foreign currency-denominated bonds/sukuk	• Free to use onshore and offshore
✓ Guidelines for issuance	• Guidelines for issuance can be obtained at: ✓ http://www.mifc.com ✓ http://www.bnm.gov.my/fxadmin ✓ http://www.sc.com.my
FINANCIAL GUARANTEE	
• Licensed onshore banks	• Free to issue any amount of financial guarantees on behalf or in favour of a non-resident • Free to obtain any amount of financial guarantees from non-residents • The above financial guarantees issued or obtained by the licensed onshore banks are not required to be registered with the Controller of Foreign Exchange
• Non-bank residents	• Free to issue any amount of financial guarantees on behalf or in favour of a non-resident • Free to obtain any amount of financial guarantees from non-residents • Financial guarantees issued or obtained by the non-bank residents are required to be registered with the Controller of Foreign Exchange at least seven working days prior to the issuance or obtaining of financial guarantee, if the aggregate amount of financial guarantees issued or obtained exceeds RM50 million equivalent, respectively

EXPORT AND IMPORT OF GOODS AND SERVICES BY RESIDENTS	
• Currency for payment of import and export of goods and services	• Payment must be made in foreign currency
• Repatriation of proceeds from the export of goods	• Export proceeds must be repatriated to Malaysia in full as per the sales contract which must not exceed six months from the date of export • Prior permission is required for residents to: ✓ Offset export proceeds against payables due to non-residents; or ✓ Receive the export proceeds exceeding six months from the date of export
• Retention of foreign currency export proceeds onshore and offshore	• Free to retain in foreign currency accounts maintained with licensed onshore banks • Prior permission is required to retain in foreign currency accounts maintained with licensed International Islamic Banks or offshore banks
• Hedging	• Free to hedge with licensed onshore banks and licensed International Islamic Banks, payments or receipts for the import or export of goods and services: ✓ Based on firm underlying commitment; or ✓ On anticipatory basis up to the actual total amount paid or received in the preceding 12 months • 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 International Islamic Banks, licensed offshore banks in Labuan and overseas banks
• Sources of funds	• The FCA can be credited with foreign currency funds sourced: ✓ From conversion of ringgit with licensed onshore banks: ➢ No limit for residents without domestic ringgit borrowing; ➢ For residents with domestic ringgit borrowing, up to permitted limits for investment in foreign currency assets. Additional limits for overseas education and employment purposes as follows: - Up to USD150,000 with licensed onshore banks and licensed International Islamic Banks; - Up to USD150,000 with licensed offshore banks in Labuan; and - Up to USD50,000 with overseas banks ✓ From other residents for permitted purposes; and ✓ From non-residents for permitted purposes. Export proceeds, however, must be retained with licensed onshore banks only
• Opening of joint FCA	• Resident individuals are free to open joint FCAs for any purpose with other resident individuals • Resident companies, however, require prior permission to open joint FCAs

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, sourced from foreign currency accounts • Resident participants[17] undertaking commodity murabahah through resident commodity trading service providers are free to make payment in foreign currency between resident participants
HEDGING BY RESIDENTS	
• Hedging of current account transactions	• Free to hedge with licensed onshore banks and licensed International Islamic Banks for payments and receipts for import and export of goods and services: ✓ Based on firm underlying commitment; or ✓ On anticipatory basis provided the amount hedged does not exceed the total amount paid or received in the preceding 12 months • 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 International Islamic Banks based on committed capital inflows or outflows • Residents are also allowed to hedge their existing holdings of foreign currency assets • Hedging involving ringgit shall only be undertaken with licensed onshore banks
IMPORT AND EXPORT OF RINGGIT AND FOREIGN CURRENCY 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

[17] The participants of commodity murabahah comprise financial institutions, companies or individuals, commodity brokers, commodity suppliers, commodity buyers and commodity trading service providers

DEALINGS WITH SPECIFIED PERSONS	
• Specified Persons	• Prior permission is required for residents to deal with the following Specified Persons: ✓ Individual or entity as designated pursuant to the United Nation Security Council Resolution (UNSCR) relating to: ➢ Osama bin Laden and The Taliban ➢ Liberia ➢ Al-Qaida Organisation ➢ Saddam Hussein's immediate family members or senior officials of the former Iraqi regime and their immediate family members ➢ Iran ➢ Democratic Republic of Congo ➢ Democratic People's Republic of Korea ➢ Sudan ✓ The State of Israel or their residents; ✓ The authorities of the State of Israel; ✓ The agencies of the State of Israel or its residents; and ✓ Any entity owned by or controlled, directly or indirectly, by the State of Israel or its resident
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 for own account except dealing in ringgit offshore
• Approved Operational Headquarters	• Free to invest any amount in foreign currency assets to be funded with own foreign currency funds or foreign currency borrowing • Free to borrow any amount of foreign currency from licensed onshore banks, licensed International Islamic Banks and from any non-residents, provided the operational headquarters do not on-lend to, or raise the funds on behalf of, any resident • Free to utilise proceeds of any amount from the issuance of ordinary shares through initial public offering on Bursa Malaysia for investment in foreign currency assets • 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

• Resident corporations approved under the following framework: ✓ Iskandar Development Region ✓ National Biotechnology Policy	• Free to undertake the following: ✓ To pay and receive in foreign currency with residents; ✓ To borrow any amount of foreign currency from licensed onshore banks, licensed International Islamic Banks and non-residents; ✓ To invest any amount in foreign currency assets onshore and offshore; and ✓ To retain export proceeds offshore

Key Economic and Financial Statistics

Table A.1
Gross Domestic Product by Kind of Economic Activity at Constant 2000 Prices

	2005	2006	2007	2008	2009*p*	2010*f*
	RM million					
Agriculture	35,835	37,701	38,224	39,769	39,929	41,175
Mining and quarrying	42,472	42,030	42,881	42,550	40,926	41,933
Manufacturing	137,940	147,154	151,789	153,744	139,448	148,455
Construction	14,685	14,639	15,332	15,657	16,548	17,157
Services	230,043	247,099	270,903	290,538	297,995	312,565
Less: Undistributed FISIM[1]	17,742	18,385	19,730	20,786	22,270	23,728
Plus: Import duties	6,017	5,287	5,521	6,839	6,642	5,824
GDP at purchasers' prices[2]	**449,250**	**475,526**	**504,919**	**528,311**	**519,218**	**543,380**
	Annual change (%)					
Agriculture	2.6	5.2	1.4	4.0	0.4	3.1
Mining and quarrying	-0.4	-1.0	2.0	-0.8	-3.8	2.5
Manufacturing	5.2	6.7	3.1	1.3	-9.3	6.5
Construction	-1.5	-0.3	4.7	2.1	5.7	3.7
Services	7.2	7.4	9.6	7.2	2.6	4.9
Less: Undistributed FISIM[1]	0.2	3.6	7.3	5.4	7.1	6.5
Plus: Import duties	-1.3	-12.1	4.4	23.9	-2.9	-12.3
GDP at purchasers' prices[2]	**5.3**	**5.8**	**6.2**	**4.6**	**-1.7**	**4.5~5.5**

[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)

	2006	2007	2008	2009	2007	2008	2009
	Index				Annual change (%)		
Export-oriented industries	**110.0**	**111.2**	**109.9**	**97.7**	**1.1**	**-1.2**	**-11.1**
Electrical and electronics products cluster	**113.5**	**111.8**	**107.8**	**83.2**	**-1.5**	**-3.6**	**-22.8**
Electronics	*116.4*	*119.9*	*113.4*	*85.5*	*3.0*	*-5.4*	*-24.6*
Electrical products	*107.9*	*96.2*	*97.1*	*78.9*	*-10.8*	*0.9*	*-18.8*
Primary-related cluster	**107.7**	**110.7**	**111.2**	**107.4**	**2.9**	**0.4**	**-3.5**
Chemicals and chemical products	107.6	111.4	107.6	105.8	3.6	-3.5	-1.7
Petroleum products	108.2	110.8	117.4	116.5	2.5	5.9	-0.8
Textiles, wearing apparel and footwear	102.2	100.3	100.3	80.4	-1.9	0.0	-19.8
Wood and wood products	97.1	95.7	91.2	76.0	-1.4	-4.7	-16.6
Rubber products	112.7	122.5	128.2	124.3	8.6	4.7	-3.0
Off-estate processing	115.4	105.1	115.0	112.6	-8.9	9.4	-2.1
Paper products	112.4	140.8	120.6	114.0	25.3	-14.4	-5.5
Domestic-oriented industries	**105.3**	**112.5**	**121.5**	**114.6**	**6.8**	**8.0**	**-5.7**
Construction-related cluster	**112.3**	**121.6**	**126.9**	**112.4**	**8.3**	**4.3**	**-11.4**
Construction-related products	107.1	113.2	116.9	95.8	5.8	3.2	-18.1
Non-metallic mineral products	*105.8*	*105.3*	*114.9*	*99.3*	*-0.4*	*9.1*	*-13.6*
Basic iron & steel and non-ferrous metal	*108.6*	*122.9*	*119.3*	*91.5*	*13.1*	*-2.9*	*-23.3*
Fabricated metal products	122.4	137.8	146.2	144.6	12.5	6.1	-1.1
Consumer-related cluster	**100.2**	**105.9**	**117.6**	**116.1**	**5.6**	**11.0**	**-1.2**
Food products	106.4	114.5	125.8	129.8	7.6	9.9	3.2
Transport equipment	95.3	94.3	116.4	102.0	-1.1	23.4	-12.4
Beverages	98.5	114.2	117.2	114.5	15.9	2.6	-2.3
Tobacco products	95.7	99.0	93.5	87.5	3.5	-5.6	-6.4
Others	99.7	110.4	101.7	129.1	10.7	-7.9	27.0
Total	**109.1**	**111.4**	**112.2**	**101.0**	**2.2**	**0.7**	**-10.0**

Source: Department of Statistics, Malaysia

Table A.3
Production of Primary Commodities

	2005	2006	2007	2008	2009*p*	2006	2007	2008	2009*p*
	Volume					Annual change (%)			
Crude palm oil (‘000 tonnes)	14,962	15,881	15,824	17,734	17,565	6.1	-0.4	12.1	-1.0
Rubber (‘000 tonnes)	1,126	1,284	1,200	1,072	856	14.0	-6.6	-10.6	-20.2
Saw logs (‘000 cu. metres)	22,398	21,894	22,052	20,083	16,682[1]	-2.3	0.7	-8.9	-10.9[1]
Cocoa (‘000 tonnes)	28	32	35	28	18	14.2	10.2	-20.5	-35.1
Crude oil (including condensates) (‘000 bpd)	704	667	683	688	660	-5.2	2.4	0.8	-4.1
Natural gas (mmscfd)	5,797	5,774	5,884	5,888	5,667	-0.4	1.9	0.1	-3.7
Tin-in-concentrates (‘000 tonnes)	2.9	2.4	2.3	2.6	2.4	-16.1	-4.9	14.3	-7.4

[1] January - November 2009
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
GNI by Demand Aggregates

	2005	2006	2007	2008	2009*p*	2010*f*
	at Current Prices (RM million)					
Consumption	298,750	326,889	371,021	426,678	435,207	454,544
Private consumption	*234,234*	*258,280*	*292,724*	*334,147*	*338,767*	*359,771*
Public consumption	*64,516*	*68,609*	*78,297*	*92,531*	*96,440*	*94,773*
Investment	107,185	119,213	138,703	145,041	137,397	149,302
Private investment	*53,705*	*62,139*	*76,981*	*80,624*	*62,547*	*65,430*
Public investment	*53,480*	*57,074*	*61,721*	*64,417*	*74,850*	*83,872*
Change in stocks[1]	-2,770	-1,722	5	-3,757	-42,900	2,964
Exports of goods and services	613,694	669,505	707,156	765,370	653,288	717,468
Imports of goods and services	494,414	539,443	577,110	594,655	508,559	576,625
GDP at purchasers' prices	522,445	574,441	639,776	738,677	674,434	747,654
Net factor payments abroad	-23,943	-17,294	-13,893	-23,707	-12,589	-19,918
GNI	498,503	557,147	625,882	714,970	661,845	727,736
	at Constant 2000 Prices (RM million)					
Consumption	274,642	292,280	320,313	348,995	353,831	362,430
Private consumption	*216,247*	*230,948*	*255,014*	*276,589*	*278,753*	*289,380*
Public consumption	*58,395*	*61,332*	*65,299*	*72,406*	*75,078*	*73,050*
Investment	99,266	106,750	116,964	117,868	111,356	117,481
Private investment	*50,841*	*55,538*	*62,101*	*62,598*	*48,956*	*49,299*
Public investment	*48,425*	*51,212*	*54,863*	*55,270*	*62,400*	*68,182*
Change in stocks[1]	-3,080	257	-4,075	-7,726	-20,939	2,410
Exports of goods and services	554,261	590,784	617,279	625,365	561,904	605,006
Imports of goods and services	475,838	514,544	545,562	556,191	486,934	543,946
GDP at purchasers' prices	449,250	475,526	504,919	528,311	519,218	543,380
Net factor payments abroad	-24,956	-20,517	-23,114	-36,781	-21,798	-28,088
GNI	424,295	455,008	481,806	491,529	497,420	515,292

[1] Includes statistical discrepancy
p Preliminary
f Forecast

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

Table A.5
Savings-Investment Gap

	2005	2006	2007	2008	2009*p*
	RM million				
Public gross domestic capital formation	53,480	57,074	61,722	64,417	74,850
Public savings	70,506	83,226	103,841	80,879	92,272
Deficit/surplus	17,026	26,152	42,119	16,462	17,422
Private gross domestic capital formation	50,935	60,417	76,986	76,867	19,647
Private savings	112,275	130,294	135,277	189,918	114,928
Deficit/surplus	61,340	69,877	58,291	113,051	95,281
Gross domestic capital formation	104,415	117,491	138,708	141,284	94,497
(as % of GNI)	20.9	21.1	22.2	19.8	14.3
Gross national savings	182,781	213,520	239,118	270,797	207,200
(as % of GNI)	36.7	38.3	38.2	37.9	31.3
Balance on current account	78,366	96,029	100,410	129,513	112,703
(as % of GNI)	15.7	17.2	16.0	18.1	17.0

p Preliminary

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

Table A.6
Labour Market: Selected Indicators

	2005	2006	2007	2008	2009e
	(number of positions/persons)				
Vacancies Reported by Industry[1]					
Agriculture, hunting, forestry and fishery	40,438	188,104	226,759	275,548	230,303
Mining and quarrying	150	861	1,163	1,450	1,377
Manufacturing	112,542	348,302	275,155	327,798	695,418
Construction	48,524	129,586	117,217	107,421	111,622
Services	63,441	154,902	204,599	346,763	507,627
Electricity, gas and water supply	*859*	*2,227*	*1,477*	*2,047*	*4,367*
Wholesale and retail trade, hotels and restaurants	*23,921*	*67,956*	*66,600*	*99,317*	*162,270*
Transport, storage and communication	*3,892*	*8,287*	*12,578*	*15,264*	*15,090*
Financial intermediation, real estate, renting and business services	*13,874*	*26,642*	*50,235*	*125,821*	*148,001*
Public administration, defence and compulsory social security	*2,497*	*3,539*	*11,287*	*11,132*	*16,128*
Community, social and personal service activities	*18,398*	*46,251*	*62,422*	*93,182*	*161,771*
Others not elsewhere classified	39,405	12,920	289	0	0
Total vacancies	**304,500**	**834,675**	**825,182**	**1,058,980**	**1,546,347**
Retrenchment by Industry					
Agriculture, hunting, forestry and fishery	243	312	255	398	278
Mining and quarrying	355	78	61	89	78
Manufacturing	11,802	8,890	9,970	11,014	17,850
Construction	411	603	291	199	503
Services	3,298	5,477	3,458	4,769	6,355
Electricity, gas and water supply	*0*	*65*	*5*	*77*	*156*
Wholesale and retail trade, hotels and restaurants	*1,294*	*2,327*	*1,929*	*2,052*	*1,429*
Transport, storage and communication	*802*	*1,521*	*322*	*773*	*643*
Financial intermediation, real estate, renting and business services	*463*	*983*	*761*	*1,008*	*1,923*
Community, social and personal service activities	*739*	*581*	*441*	*859*	*2,204*
Total retrenchments	**16,109**	**15,360**	**14,035**	**16,469**	**25,064**
Employment by Industry[2] ('000 persons)					
Agriculture, forestry, livestock and fishery	1,401.3	1,392.4	1,389.8	1,390.9	1,391.5
Mining and quarrying	42.7	42.6	42.9	42.8	42.6
Manufacturing	3,133.2	3,227.2	3,296.6	3,338.2	3,302.0
Construction	759.6	755.2	757.3	758.4	760.8
Services	5,555.9	5,741.7	5,911.4	6,046.1	6,112.2
Electricity, gas and water supply	*93.0*	*95.0*	*96.8*	*97.6*	*97.4*
Transport, storage and communication	*630.6*	*646.4*	*660.0*	*673.2*	*675.0*
Wholesale and retail trade, hotels and restaurants	*1,861.5*	*1,930.4*	*1,957.7*	*1,984.3*	*1,996.4*
Finance, insurance, real estate and business services	*734.4*	*767.5*	*789.7*	*811.9*	*814.7*
Government services	*1,118.4*	*1,152.5*	*1,225.6*	*1,263.5*	*1,286.2*
Other services	*1,118.1*	*1,150.0*	*1,181.6*	*1,215.6*	*1,242.5*
Total employment	**10,892.8**	**11,159.0**	**11,398.0**	**11,576.5**	**11,609.1**
Unemployment rate[2] (% of labour force)	**3.5**	**3.3**	**3.2**	**3.3**	**3.7**

e Estimates
[1] Refers to vacancies reported by employers through the JobsMalaysia portal (formerly known as Electronic Labour Exchange, ELX).
[2] Refers to estimates by Economic Planning Unit

Source: Economic Planning Unit and Ministry of Human Resources

Table A.7
Private Consumption Indicators

	2008	2009				
		1Q	2Q	3Q	4Q	Year
Sales of passenger cars ('000 units)	497.5	109.0	119.1	133.4	124.5	486.1
Annual change (%)	12.3	-9.3	-11.1	-3.5	18.5	-2.3
Imports of consumption goods (RM billion)	32.3	7.0	7.6	8.3	8.5	31.4
Annual change (%)	11.8	-4.3	-8.3	-4.4	6.3	-2.7
Tax collection						
Sales tax (RM billion)	7.5	1.4	1.6	1.7	2.3	7.0
Service tax (RM billion)	3.3	0.7	0.9	0.8	1.0	3.3
Narrow Money (M1)						
Annual change (%)	8.3	3.5	5.5	6.4	9.8	9.8
Loans disbursed by banking system						
Consumption credit (excl. passenger cars)						
Annual change (%)	2.2	5.5	14.7	26.1	32.1	19.6
Retail trade, restaurants and hotels						
Annual change (%)	24.5	-2.7	-13.9	-14.3	2.9	-7.5
MRA retail sales (Annual change in %)	5.0	-3.3	4.1	0.0	3.0	0.8
Credit card turnover spending[1] (RM billion)	64.2	16.0	16.4	17.3	18.5	68.1
Annual change (%)	15.8	6.0	5.7	3.1	9.7	6.2
MIER Consumer Sentiment Index	-	78.9	105.8	105.4	109.6	-
FBM KLCI	876.8	872.6	1,075.2	1,202.1	1,272.8	1,272.8
Commodity prices						
CPO (RM/tonne)	2,875	1,927	2,548	2,261	2,292	2,257
Crude oil (USD/barrel)	100	43	60	68	76	62
Rubber (sen/kg)	829	505	564	659	842	643

[1] Resident spending only

Table A.8
Private Investment Indicators

	2008	2009				
		1Q	2Q	3Q	4Q	Year
Sales of commercial vehicles ('000 units)	50.7	11.1	11.8	13.3	14.4	50.6
Annual change (%)	14.4	5.4	-10.6	-3.8	9.7	-0.2
Imports of capital goods (RM billion)	69.9	14.8	15.0	16.2	19.8	65.8
Annual change (%)	0.0	-7.8	-18.4	-13.2	17.4	-5.9
Approvals by MITI (Manufacturing sector)						
No. of projects	919	211	179	178	198	766
Capital investment (RM billion)	62.8	8.0	8.9	4.0	11.9	32.6
Foreign	*46.1*	*3.7*	*7.4*	*2.2*	*8.9*	*22.1*
Local	*16.7*	*4.3*	*1.5*	*1.7*	*3.0*	*10.5*
New investment (% share)	66.9	55.6	82.7	60.6	66.6	67.6
Reinvestments (% share)	33.1	44.4	17.3	39.4	33.4	32.4
Loans disbursed by banking system						
Manufacturing sector						
Annual change (%)	12.4	-16.6	-22.2	-20.3	-0.2	-15.3
Construction sector						
Annual change (%)	6.8	-6.7	4.7	20.0	52.4	16.4
Private Debt Securities (excluding Cagamas)						
Total funds raised (RM billion)	49.7	9.3	19.3	13.5	16.4	58.6
New activities	33.3	1.3	0.9	1.9	4.7	8.7
Initial Public Offerings (Bursa Malaysia)						
Total funds raised (RM billion)	1.3	0.0	0.2	0.3	11.6	12.2
MIER Business Conditions Survey						
Business Conditions Index	-	61.1	105.2	113.7	118.8	-
Capacity Utilisation Rate	-	72.0	78.2	81.7	81.4	-
MSC-Status Companies						
No. of companies	242	55	70	75	84	284
Approved investment (RM billion)	1.8	0.3	0.7	0.6	0.6	2.2

Table A.9
Balance of Payments

Item	2006			2007		
	+	-	Net	+	-	Net
	RM million					
Goods[1]	**590,018**	**452,726**	**137,292**	**605,916**	**478,243**	**127,673**
Trade account	*589,240*	*478,148*	*111,092*	*604,300*	*502,045*	*102,255*
Services	**79,488**	**86,718**	**-7,230**	**101,240**	**98,867**	**2,373**
Transportation	15,217	34,948	-19,731	24,582	37,755	-13,173
Travel	38,239	15,606	22,633	48,289	19,174	29,115
Other services	25,629	35,322	-9,693	28,068	41,246	-13,178
Government transactions n.i.e.[2]	403	842	-440	301	691	-390
Balance on goods and services	**669,505**	**539,443**	**130,062**	**707,156**	**577,110**	**130,047**
Income	**31,107**	**48,401**	**-17,294**	**38,840**	**52,733**	**-13,893**
Compensation of employees	5,007	5,313	-306	5,372	5,972	-600
Investment income[3]	26,100	43,088	-16,988	33,468	46,761	-13,294
Current transfers	**1,149**	**17,889**	**-16,739**	**1,444**	**17,187**	**-15,743**
Balance on current account	**701,761**	**605,734**	**96,029**	**747,439**	**647,030**	**100,410**
% of GNI			**17.2**			**16.0**
Capital account			**-264**			**-95**
Financial account			**-43,182**			**-37,710**
Direct investment			144			-9,142
Abroad			*-22,086*			*-38,224*
In Malaysia			*22,230*			*29,081*
Portfolio investment			12,786			18,355
Other investment			-56,112			-46,923
Official sector			*-8,018*			*-5,788*
Private sector			*-48,094*			*-41,135*
Balance on capital and financial accounts			**-43,446**			**-37,805**
Errors and omissions			**-27,424**			**-17,309**
of which:						
Foreign exchange revaluation gain (+) / loss (-)			-6,945			-5,597
Overall balance (surplus + / deficit -)			**25,158**			**45,296**
Bank Negara Malaysia international reserves, net[4]						
RM million			290,399			335,695
USD million			82,451			101,338
Reserves as months of retained imports			7.8			8.4

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
p Preliminary
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

2008			2009*p*			2010*f*		
+	-	Net	+	-	Net	+	-	Net
RM million								
664,325	**493,773**	**170,552**	**554,215**	**412,704**	**141,512**	**615,245**	**473,690**	**141,555**
663,494	*521,611*	*141,883*	*553,295*	*434,940*	*118,355*	*615,058*	*498,353*	*116,705*
101,045	**100,882**	**163**	**99,073**	**95,854**	**3,219**	**102,223**	**102,934**	**-711**
22,495	37,895	-15,401	14,909	31,966	-17,057	16,607	36,292	-19,685
50,961	22,446	28,515	54,213	22,625	31,588	55,439	24,261	31,178
27,463	39,839	-12,376	29,806	40,521	-10,714	30,003	41,666	-11,663
126	702	-576	144	742	-598	175	715	-540
765,370	**594,655**	**170,715**	**653,288**	**508,558**	**144,731**	**717,468**	**576,625**	**140,844**
39,930	**63,638**	**-23,707**	**40,538**	**53,127**	**-12,589**	**40,442**	**60,361**	**-19,918**
4,421	5,152	-731	4,002	5,387	-1,385	3,850	5,490	-1,640
35,509	58,486	-22,977	36,537	47,740	-11,203	36,592	54,871	-18,278
1,410	**18,905**	**-17,495**	**3,687**	**23,127**	**-19,439**	**1,390**	**18,500**	**-17,110**
806,710	**677,197**	**129,513**	**697,513**	**584,812**	**112,703**	**759,301**	**655,485**	**103,815**
		18.1			**17.0**			**14.3**
		592			**-162**			
		-118,501			**-82,948**			
		-26,058			-24,851			
		-50,192			*-30,514*			
		24,134			*5,663*			
		-84,377			830			
		-8,066			-58,927			
		852			*4,099*			
		-8,918			*-63,026*			
		-117,909			**-83,110**			
		-29,854			**-15,762**			
		-5,824			10,697			
		-18,250			**13,831**			
		317,445			331,277			
		91,529			96,688			
		7.6			9.7			

Table A.10
Gross Exports

	2007	2008	2009*p*	2008	2009*p*	2009*p*
	RM million			Annual change (%)		% share
Manufactures	**473,695**	**491,930**	**430,575**	**3.8**	**-12.5**	**77.8**
of which:						
Electronics, electrical machinery and appliances	287,696	277,282	246,897	-3.6	-11.0	44.6
Electronics	213,704	195,933	179,087	-8.3	-8.6	32.4
Semiconductors	*96,653*	*89,819*	*92,972*	*-7.1*	*3.5*	*16.8*
Electronic equipment & parts	*117,051*	*106,114*	*86,115*	*-9.3*	*-18.8*	*15.6*
Electrical machinery & appliances	73,993	81,349	67,809	9.9	-16.6	12.3
Consumer electrical products	*16,461*	*21,388*	*18,794*	*29.9*	*-12.1*	*3.4*
Industrial & commercial electrical products	*29,696*	*31,088*	*23,986*	*4.7*	*-22.8*	*4.3*
Electrical industrial machinery and equipment	*24,297*	*25,382*	*21,905*	*4.5*	*-13.7*	*4.0*
Household electrical appliances	*3,538*	*3,491*	*3,125*	*-1.3*	*-10.5*	*0.6*
Chemicals & chemical products	37,159	40,926	34,161	10.1	-16.5	6.2
Manufactures of metal	26,372	29,257	22,644	10.9	-22.6	4.1
Petroleum products	22,093	31,149	21,939	41.0	-29.6	4.0
Optical and scientific equipment	13,626	14,944	13,095	9.7	-12.4	2.4
Textiles, clothing and footwear	10,631	10,911	9,375	2.6	-14.1	1.7
Wood products	9,736	9,767	7,978	0.3	-18.3	1.4
Rubber products	10,326	12,426	12,125	20.3	-2.4	2.2
Minerals	**61,913**	**87,536**	**59,317**	**41.4**	**-32.2**	**10.7**
of which:						
Crude oil and condensates	32,865	43,698	25,360	33.0	-42.0	4.6
Liquefied natural gas (LNG)	26,936	40,732	31,195	51.2	-23.4	5.6
Agriculture	**52,491**	**68,097**	**53,394**	**29.7**	**-21.6**	**9.7**
of which:						
Palm oil	32,027	45,955	36,365	43.5	-20.9	6.6
Rubber	7,334	8,112	4,460	10.6	-45.0	0.8
Others	**16,201**	**15,931**	**10,009**	**-1.7**	**-37.2**	**1.8**
Total	**604,300**	**663,494**	**553,295**	**9.8**	**-16.6**	**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

	2007	2008	2009*p*	2008	2009*p*
	Volume and value			Annual change (%)	
Commodity exports (RM million)	**114,404**	**155,634**	**112,711**	**36.0**	**-27.6**
Agriculture exports (RM million)	**52,491**	**68,097**	**53,394**	**29.7**	**-21.6**
of which:					
Palm oil					
('000 tonnes)	13,412	15,699	16,256	17.1	3.5
(RM/tonne)	2,388	2,927	2,237	22.6	-23.6
(RM million)	32,027	45,955	36,365	43.5	-20.9
Palm kernel oil					
('000 tonnes)	598	684	1,028	14.3	50.3
(RM/tonne)	2,749	3,792	1,698	38.0	-55.2
(RM million)	1,644	2,592	1,745	57.7	-32.7
Rubber					
('000 tonnes)	1,020	916	703	-10.2	-23.2
(sen/kilogramme)	719	886	634	23.2	-28.4
(RM million)	7,334	8,112	4,460	10.6	-45.0
Saw logs					
('000 cubic metres)	4,690	4,368	4,211	-6.9	-3.6
(RM/cubic metre)	457	471	482	3.1	2.5
(RM million)	2,142	2,057	2,031	-4.0	-1.2
Sawn timber					
('000 cubic metres)	2,831	2,854	1,689	0.8	-40.8
(RM/cubic metre)	1,456	1,211	1,786	-16.9	47.5
(RM million)	4,123	3,455	3,016	-16.2	-12.7
Cocoa beans					
('000 tonnes)	18.4	7.6	14.4	-58.6	88.5
(RM/tonne)	6,471	7,883	9,064	21.8	15.0
(RM million)	119	60	130	-49.5	116.7
Mineral exports (RM million)	**61,913**	**87,536**	**59,317**	**41.4**	**-32.2**
of which:					
Crude oil and condensates					
('000 tonnes)	16,880	16,477	16,413	-2.4	-0.4
(USD/barrel)	74.69	105.31	58.00	41.0	-44.9
(RM million)	32,865	43,698	25,360	33.0	-42.0
Liquefied natural gas (LNG)					
('000 tonnes)	22,904	22,873	22,186	-0.1	-3.0
(RM/tonne)	1,176	1,781	1,406	51.4	-21.0
(RM million)	26,936	40,732	31,195	51.2	-23.4
Tin					
('000 tonnes)	16.8	27.5	22.9	63.5	-16.9
(RM/tonne)	47,227	61,675	45,771	30.6	-25.8
(RM million)	795	1,698	1,047	113.5	-38.3

p Preliminary

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

Table A.12
Principal Markets for Manufactured Exports

Country	2005	2006	2007	2008	2009*p*	2005	2006	2007	2008	2009*p*
	RM million					% share				
Selected ASEAN countries	**113,081**	**123,766**	**123,809**	**134,858**	**114,180**	**26.1**	**26.1**	**26.1**	**27.4**	**26.5**
Singapore	75,507	81,359	78,490	85,286	70,359	17.5	17.2	16.6	17.3	16.3
Thailand	21,639	24,624	24,991	25,664	24,073	5.0	5.2	5.3	5.2	5.6
Indonesia	9,492	10,677	12,574	16,339	13,074	2.2	2.3	2.7	3.3	3.0
Philippines	5,429	6,135	6,564	6,225	5,211	1.3	1.3	1.4	1.3	1.2
Brunei Darussalam	1,014	971	1,190	1,344	1,463	0.2	0.2	0.3	0.3	0.3
United States	100,859	106,009	90,102	76,689	56,653	23.3	22.4	19.0	15.6	13.2
European Union	**55,025**	**65,155**	**66,971**	**63,161**	**52,465**	**12.7**	**13.8**	**14.1**	**12.8**	**12.2**
Netherlands	14,741	17,787	19,060	18,646	15,178	3.4	3.8	4.0	3.8	3.5
Germany	9,989	11,158	13,393	13,597	13,716	2.3	2.4	2.8	2.8	3.2
United Kingdom	8,721	10,117	9,219	8,620	6,657	2.0	2.1	1.9	1.8	1.5
Others	21,575	26,093	25,299	22,298	16,914	5.0	5.5	5.3	4.5	3.9
The People's Republic of China	26,086	32,015	38,009	44,494	51,169	6.0	6.8	8.0	9.0	11.9
Japan	32,327	33,294	32,574	36,004	30,177	7.5	7.0	6.9	7.3	7.0
Hong Kong SAR	30,188	28,147	26,690	27,045	28,026	7.0	5.9	5.6	5.5	6.5
Middle East	13,237	16,008	18,815	23,378	20,688	3.1	3.4	4.0	4.8	4.8
Australia	10,854	11,287	12,081	14,808	13,736	2.5	2.4	2.6	3.0	3.2
Chinese Taipei	10,551	10,838	11,724	10,501	10,074	2.4	2.3	2.5	2.1	2.3
Korea	9,564	10,381	10,732	10,304	9,592	2.2	2.2	2.3	2.1	2.2
India	6,532	7,258	9,172	10,129	8,050	1.5	1.5	1.9	2.1	1.9
Latin American countries	4,789	6,072	7,156	9,181	7,358	1.1	1.3	1.5	1.9	1.7
Canada	2,637	3,535	2,971	2,964	2,620	0.6	0.7	0.6	0.6	0.6
Rest of the World	16,801	19,666	22,888	28,413	25,787	3.9	4.2	4.8	5.8	6.0
Total	**432,531**	**473,432**	**473,695**	**491,930**	**430,575**	**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	2005	2006	2007	2008	2009*p*	2005	2006	2007	2008	2009*p*
	RM million					% share				
The People's Republic of China	13,236	17,297	22,640	27,259	34,833	6.3	7.8	10.6	13.9	19.5
United States	64,527	68,237	56,406	43,360	28,060	30.9	30.8	26.4	22.1	15.7
Singapore	35,044	35,115	34,326	33,828	28,045	16.8	15.9	16.1	17.3	15.7
Hong Kong SAR	21,651	18,729	17,524	17,433	20,106	10.4	8.5	8.2	8.9	11.2
Japan	10,319	11,462	11,244	10,171	9,561	4.9	5.2	5.3	5.2	5.3
Netherlands	9,954	13,386	13,535	11,210	9,462	4.8	6.0	6.3	5.7	5.3
Thailand	9,377	9,681	9,954	9,392	9,248	4.5	4.4	4.7	4.8	5.2
Germany	5,153	5,136	6,618	6,587	7,657	2.5	2.3	3.1	3.4	4.3
Chinese Taipei	5,447	5,268	5,357	4,513	5,697	2.6	2.4	2.5	2.3	3.2
Korea	4,210	4,283	4,110	3,612	3,299	2.0	1.9	1.9	1.8	1.8
Others	29,626	32,914	31,991	28,568	23,118	14.2	14.9	15.0	14.6	12.9
Total	**208,543**	**221,508**	**213,704**	**195,933**	**179,087**	**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	2005	2006	2007	2008	2009*p*	2005	2006	2007	2008	2009*p*
	RM million					% share				
United States	18,944	19,025	15,759	14,886	12,970	25.5	24.0	21.3	18.3	19.1
European Union	11,045	13,235	12,214	13,451	9,344	14.9	16.7	16.5	16.5	13.8
Singapore	13,119	14,701	10,983	10,988	8,169	17.7	18.5	14.8	13.5	12.0
Japan	7,553	6,090	5,936	7,326	6,946	10.2	7.7	8.0	9.0	10.2
Middle East	2,679	3,355	4,393	5,633	5,090	3.6	4.2	5.9	6.9	7.5
Australia	1,829	1,797	2,522	3,598	4,117	2.5	2.3	3.4	4.4	6.1
The People's Republic of China	3,340	3,092	3,555	3,816	3,146	4.5	3.9	4.8	4.7	4.6
Hong Kong SAR	2,940	3,420	3,287	3,425	2,976	4.0	4.3	4.4	4.2	4.4
Thailand	2,557	2,670	2,784	2,705	2,600	3.4	3.4	3.8	3.3	3.8
Others	10,248	11,892	12,561	15,519	12,452	13.8	15.0	17.0	19.1	18.4
Total	**74,253**	**79,277**	**73,993**	**81,349**	**67,809**	**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	2005	2006	2007	2008	2009*p*	2005	2006	2007	2008	2009*p*
	RM million					% share				
The People's Republic of China	4,322	4,432	5,009	5,140	5,359	13.5	13.1	13.5	12.6	15.7
Singapore	3,129	3,084	3,329	3,720	3,299	9.8	9.1	9.0	9.1	9.7
Indonesia	2,459	2,646	2,902	3,972	3,074	7.7	7.8	7.8	9.7	9.0
Thailand	2,809	3,168	3,389	3,659	2,774	8.8	9.4	9.1	8.9	8.1
Japan	3,199	3,132	2,866	3,221	2,290	10.0	9.3	7.7	7.9	6.7
India	1,678	1,797	1,874	2,195	2,011	5.2	5.3	5.0	5.4	5.9
Hong Kong SAR	2,174	2,388	2,004	1,965	1,528	6.8	7.1	5.4	4.8	4.5
Korea	1,486	1,555	1,550	1,302	1,237	4.6	4.6	4.2	3.2	3.6
United States	1,404	1,274	1,512	1,569	1,181	4.4	3.8	4.1	3.8	3.5
Chinese Taipei	1,319	1,416	1,723	1,610	1,158	4.1	4.2	4.6	3.9	3.4
Others	7,986	8,834	11,001	12,575	10,250	25.0	26.2	29.6	30.7	30.0
Total	**31,965**	**33,725**	**37,159**	**40,926**	**34,161**	**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	2005	2006	2007	2008	2009*p*	2005	2006	2007	2008	2009*p*
	'000 tonnes					% share				
The People's Republic of China	2,914	3,532	3,786	3,785	3,672	22.6	25.2	28.2	24.1	22.6
Pakistan	929	855	1,062	1,552	1,829	7.2	6.0	7.9	9.9	11.3
European Union	2,149	2,586	2,097	2,022	1,478	16.7	18.3	15.6	12.9	9.1
Netherlands	*1,367*	*1,703*	*1,527*	*1,311*	*959*	*10.6*	*12.0*	*11.4*	*8.3*	*5.9*
Germany	*180*	*190*	*30*	*101*	*129*	*1.4*	*1.3*	*0.2*	*0.6*	*0.8*
Italy	*155*	*165*	*126*	*182*	*135*	*1.2*	*1.2*	*0.9*	*1.2*	*0.8*
Sweden	*103*	*220*	*134*	*103*	*49*	*0.8*	*1.6*	*1.0*	*0.7*	*0.3*
Others	*345*	*308*	*280*	*325*	*206*	*2.7*	*2.2*	*2.1*	*2.1*	*1.3*
Middle East	1,684	1,324	1,212	1,319	1,275	13.0	9.4	9.0	8.4	7.8
India	619	657	515	956	1,175	4.8	4.6	3.8	6.1	7.2
United States	535	696	516	1,234	804	4.1	4.9	3.8	7.9	4.9
Japan	438	498	516	530	494	3.4	3.5	3.8	3.4	3.0
Korea	223	207	225	199	269	1.7	1.5	1.7	1.3	1.7
Chinese Taipei	127	148	129	161	133	1.0	1.0	1.0	1.0	0.8
Australia	107	121	121	113	109	0.8	0.9	0.9	0.7	0.7
Bangladesh	485	413	170	253	84	3.8	2.9	1.3	1.6	0.5
Others	2,692	3,105	3,064	3,576	4,934	20.9	22.0	22.8	22.8	30.3
Total	**12,901**	**14,142**	**13,412**	**15,699**	**16,256**	**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	2005	2006	2007	2008	2009*p*	2005	2006	2007	2008	2009*p*
	'000 tonnes					% share				
The People's Republic of China	386	406	371	301	245	33.5	34.1	36.4	32.8	34.8
European Union	313	316	294	279	151	27.2	26.6	28.9	30.5	21.5
Germany	*132*	*144*	*136*	*123*	*73*	*11.4*	*12.1*	*13.3*	*13.5*	*10.4*
Netherlands	*28*	*21*	*17*	*21*	*18*	*2.4*	*1.8*	*1.6*	*2.3*	*2.5*
France	*46*	*41*	*43*	*32*	*17*	*4.0*	*3.4*	*4.3*	*3.5*	*2.4*
Italy	*24*	*22*	*20*	*17*	*9*	*2.1*	*1.9*	*1.9*	*1.9*	*1.2*
United Kingdom	*21*	*18*	*16*	*17*	*7*	*1.8*	*1.5*	*1.5*	*1.8*	*1.0*
Spain	*13*	*11*	*9*	*8*	*4*	*1.2*	*0.9*	*0.9*	*0.8*	*0.5*
Others	*49*	*59*	*54*	*61*	*24*	*4.2*	*5.0*	*5.3*	*6.7*	*3.4*
Middle East	74	71	54	69	49	6.5	6.0	5.3	7.5	7.0
Iran	*40*	*45*	*27*	*40*	*29*	*3.5*	*3.8*	*2.7*	*4.4*	*4.1*
Turkey	*24*	*20*	*21*	*21*	*15*	*2.1*	*1.7*	*2.1*	*2.3*	*2.2*
Others	*10*	*6*	*5*	*7*	*5*	*0.8*	*0.5*	*0.5*	*0.8*	*0.7*
Korea	74	67	61	52	43	6.5	5.6	6.0	5.6	6.2
United States	67	64	53	53	26	5.9	5.4	5.2	5.8	3.6
Brazil	31	32	38	35	22	2.7	2.7	3.8	3.9	3.1
Canada	17	15	19	12	8	1.5	1.3	1.9	1.4	1.1
Others	188	218	129	115	161	16.3	18.3	12.7	12.5	22.8
Total	**1,151**	**1,188**	**1,020**	**916**	**703**	**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	2005	2006	2007	2008	2009*p*	2005	2006	2007	2008	2009*p*
	'000 tonnes					% share				
Australia	3,817	2,269	3,331	3,001	3,081	20.8	13.4	19.7	18.2	18.8
India	3,783	4,417	3,908	3,890	2,887	20.6	26.2	23.2	23.6	17.6
Thailand	3,418	2,528	1,435	1,501	2,753	18.6	15.0	8.5	9.1	16.8
Indonesia	1,431	1,547	2,038	1,289	1,984	7.8	9.2	12.1	7.8	12.1
Singapore	1,638	1,285	1,607	2,732	1,516	8.9	7.6	9.5	16.6	9.2
The People's Republic of China	239	79	240	597	1,481	1.3	0.5	1.4	3.6	9.0
Korea	1,436	1,433	1,545	1,314	913	7.8	8.5	9.2	8.0	5.6
Philippines	743	471	872	867	520	4.0	2.8	5.2	5.3	3.2
Japan	808	926	987	751	512	4.4	5.5	5.8	4.6	3.1
United States	314	282	46	165	323	1.7	1.7	0.3	1.0	2.0
New Zealand	299	424	381	356	233	1.6	2.5	2.3	2.2	1.4
Others	464	1,214	491	13	209	2.5	7.2	2.9	0.1	1.3
Total	**18,390**	**16,875**	**16,880**	**16,477**	**16,413**	**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	2005	2006	2007	2008	2009*p*	2005	2006	2007	2008	2009*p*
	'000 tonnes					% share				
Japan	13,664	12,170	13,238	14,223	12,993	63.1	57.3	57.8	62.2	58.6
Korea	4,713	5,626	6,069	6,132	5,666	21.8	26.5	26.5	26.8	25.5
Chinese Taipei	3,013	3,319	3,524	2,496	2,460	13.9	15.6	15.4	10.9	11.1
Others	251	119	72	23	1,066	1.2	0.6	0.3	0.1	4.8
Total	**21,641**	**21,234**	**22,904**	**22,873**	**22,186**	**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

	2005	2006	2007	2008[2]	2009*p*
	RM million				
Medium- and long-term debt:					
Gross borrowing	**29,162**	**28,620**	**23,844**	**26,641**	**33,783**
Federal Government	*651*	*834*	*489*	*472*	*451*
NFPEs	*6,431*	*10,909*	*1,706*	*5,952*	*15,454*
Private sector	*22,080*	*16,877*	*21,650*	*20,217*	*17,878*
Repayment and prepayment	**34,957**	**28,538**	**25,699**	**13,319**	**36,069**
Federal Government	*4,153*	*3,888*	*4,803*	*946*	*6,737*
NFPEs	*13,911*	*13,197*	*7,840*	*2,068*	*8,139*
Private sector	*16,893*	*11,453*	*13,055*	*10,305*	*21,193*
Net borrowing	**-5,795**	**81**	**-1,855**	**13,322**	**-2,286**
Federal Government	*-3,502*	*-3,054*	*-4,314*	*-473*	*-6,286*
NFPEs	*-7,480*	*-2,288*	*-6,134*	*3,884*	*7,315*
Private sector	*5,187*	*5,424*	*8,594*	*9,911*	*-3,315*
Outstanding debt	**150,746**	**141,704**	**132,978**	**156,546**	**155,951**
Federal Government	*30,000*	*25,005*	*19,602*	*20,316*	*13,786*
NFPEs	*56,233*	*50,378*	*41,854*	*63,146*	*71,588*
Private sector	*64,513*	*66,322*	*71,521*	*73,085*	*70,576*
Currency composition (% share)	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**
US dollar	*79.6*	*80.5*	*80.7*	*75.6*	*76.0*
Japanese yen	*11.7*	*11.4*	*11.2*	*12.7*	*11.2*
Others	*8.7*	*8.1*	*8.1*	*11.7*	*12.8*
Short-term debt:					
Outstanding debt	**46,953**	**42,800**	**54,468**	**79,635**	**77,966**
Banking sector[1]	*38,871*	*28,812*	*42,134*	*72,043*	*69,029*
Non-bank private sector	*8,082*	*13,988*	*12,334*	*7,592*	*8,937*
Total external debt:	**197,698**	**184,505**	**187,445**	**236,181**	**233,917**
Total external debt (USD million)	**51,790**	**51,736**	**56,027**	**67,380**	**67,671**
% GNI	*39.7*	*33.2*	*29.8*	*33.0*	*35.3*
Annual change (%)	*-1.4*	*-6.7*	*1.6*	*26.0*	*-1.0*
Total servicing (including short-term interest payment)	**32,800**	**32,086**	**26,562**	**20,025**	**42,165**
of which:					
Medium- and long-term debt					
Repayment (excluding prepayment)	**25,471**	**23,760**	**19,105**	**13,290**	**36,069**
Federal Government	*4,153*	*3,888*	*4,803*	*946*	*6,737*
NFPEs	*10,166*	*11,311*	*5,035*	*2,068*	*8,139*
Private sector	*11,152*	*8,561*	*9,267*	*10,276*	*21,193*
Interest payment	**6,101**	**6,389**	**5,127**	**5,529**	**5,622**
Federal Government	*1,729*	*1,506*	*1,426*	*1,155*	*909*
NFPEs	*3,182*	*3,511*	*2,282*	*2,493*	*2,994*
Private sector	*1,190*	*1,372*	*1,418*	*1,881*	*1,720*
Debt service ratio (% of exports of goods and services)					
Total debt	**5.3**	**4.8**	**3.8**	**2.6**	**6.5**
Medium- and long-term debt	5.1	4.5	3.4	2.5	6.4
Federal Government	*1.0*	*0.8*	*0.9*	*0.3*	*1.2*
NFPEs	*2.2*	*2.2*	*1.0*	*0.6*	*1.7*
Private sector	*2.0*	*1.5*	*1.5*	*1.6*	*3.5*

[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
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 (%) (2005=100)[1]	2006 Annual Change (%)	2007 Annual Change (%)	2008 Annual Change (%)	2009 Annual Change (%)
Total	100.0	3.6	2.0	5.4	0.6
of which:					
Food and non-alcoholic beverages	31.4	3.4	3.0	8.8	4.1
Alcoholic beverages and tobacco	1.9	6.9	7.8	7.3	6.1
Clothing and footwear	3.1	-1.3	-1.4	-0.5	-0.9
Housing, water, electricity, gas and other fuels	21.4	1.5	1.3	1.6	1.4
Furnishing, household equipment and routine household maintenance	4.3	1.1	1.1	3.0	2.9
Health	1.4	2.1	1.6	2.2	2.3
Transport	15.9	11.0	2.3	8.8	-9.4
Communication	5.1	-1.4	-1.2	-0.6	-0.5
Recreation services and culture	4.6	0.7	1.4	1.8	1.5
Education	1.9	1.6	1.8	2.3	2.4
Restaurants and hotels	3.0	3.7	3.7	6.6	2.9
Miscellaneous goods and services	6.0	2.2	1.0	3.3	3.8

[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 (%) (2005=100)[1]	2006 Annual Change (%)	2007 Annual Change (%)	2008 Annual Change (%)	2009 Annual Change (%)
Total	100.0	3.1	5.5	10.3	-7.1
of which:					
Food	5.4	2.8	8.5	12.3	0.3
Beverages and tobacco	0.9	4.1	0.8	1.4	1.7
Crude materials, inedible	5.4	12.1	21.9	11.5	-11.8
Mineral fuels, lubricants etc.	17.4	9.1	4.0	34.5	-22.0
Animal and vegetable oils and fats	4.2	-2.0	43.0	24.5	-19.5
Chemicals	7.0	2.9	3.1	7.3	-7.5
Manufactured goods	10.9	2.3	2.7	6.7	-0.5
Machinery and transport equipment	42.9	0.6	1.8	0.7	1.5
Miscellaneous manufactured articles	5.4	1.4	1.4	1.7	1.5
Miscellaneous transactions and commodities	0.5	3.8	6.2	12.4	-6.2
Local Production	65.6	3.8	7.1	13.3	-10.4
Import	34.4	1.6	2.4	4.0	0.5

[1] Effective from 2010, the Producer Price Index has been revised to the new base year 2005=100, from 2000=100 previously

Source: Department of Statistics, Malaysia

Table A.23
Broad Money (M3)

	Annual change					As at end
	2005	2006	2007	2008	2009	2009
	RM million					
Broad money (M3)[1]	51,609	87,467	72,436	99,127	85,133	1,016,997
Currency in circulation[2]	1,629	3,335	2,746	4,178	3,015	43,439
Demand deposits	8,683	11,705	24,247	11,093	14,707	158,182
Broad quasi-money	41,297	72,427	45,444	83,856	67,411	815,376
Fixed deposits	*4,940*	*31,940*	*10,701*	*27,969*	*23,241*	*453,223*
Savings deposits	*1,947*	*5,195*	*8,703*	*7,786*	*10,050*	*102,268*
NIDs	*12,785*	*14,321*	*-15,279*	*144*	*-8,782*	*22,344*
Repos	*17,260*	*11,799*	*-72,366*	*-3,046*	*898*	*1,057*
Foreign currency deposits	*2,467*	*3,218*	*1,570*	*16,649*	*15,283*	*54,589*
Other deposits	*1,898*	*5,956*	*112,116*	*34,356*	*26,721*	*181,896*
Factors Affecting M3						
Net claims on Government	-5,204	8,317	-641	33,649	25,730	57,138
Claims on Government	*-2,152*	*1,614*	*-490*	*33,652*	*35,903*	*105,970*
Less: Government deposits	*3,052*	*-6,703*	*151*	*3*	*10,173*	*48,832*
Claims on private sector	44,501	34,714	53,407	94,229	51,523	875,243
Loans	*44,840*	*36,779*	*50,926*	*76,903*	*47,051*	*771,601*
Securities	*-339*	*-2,065*	*2,481*	*17,326*	*4,473*	*103,642*
Net foreign assets	1,832	52,745	71,166	-51,985	22,363	354,163
Bank Negara Malaysia[3]	*13,550*	*25,158*	*44,569*	*-18,265*	*7,343*	*324,046*
Banking system	*-11,719*	*27,587*	*26,597*	*-33,720*	*15,020*	*30,117*
Other influences	10,480	-8,309	-51,496	23,235	-14,484	-269,547

[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

	2005		2006		2007		2008		2009	
	RM million	%	RM million	%	RM million	%	RM million	%	RM million	%
Currency in circulation	1,561	5.5	3,342	11.1	2,728	8.1	4,178	11.5	3,015	7.5
Demand deposits with commercial banks and Islamic banks	8,227	9.6	13,688	14.5	24,913	23.1	9,863	7.4	14,854	10.4
M1[1]	9,788	8.5	17,029	13.7	27,640	19.6	14,040	8.3	17,869	9.8
Other deposits with commercial banks and Islamic banks[2]	73,923	17.5	89,308	18.0	41,552	7.1	92,514	14.7	67,786	9.4
Deposits with other banking institutions[3,4]	-32,102	-38.4	-18,871	-36.7	3,244	9.9	-7,427	-20.7	-557	-2.0
M3[5]	51,609	8.3	87,467	13.0	72,436	9.5	99,127	11.9	85,098	9.1

[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 2009											
	2003	2004	2005	2006	2007	2008	Jan.	Feb.	Mar.	Apr.	May	Jun.	Jul.	Aug.	Sept.	Oct.	Nov.	Dec.
Overnight interbank	2.74	2.70	2.72	3.38	3.50	3.48	3.05	2.42	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00
1-week interbank	2.80	2.74	2.75	3.42	3.52	3.50	3.07	2.44	2.02	2.02	2.02	2.02	2.02	2.02	2.03	2.03	2.02	2.02
1-month interbank	2.99	2.86	2.84	3.54	3.54	3.53	3.02	2.46	2.05	2.05	2.06	2.07	2.07	2.07	2.07	2.07	2.06	2.06
Commercial banks																		
Fixed deposit:																		
3 month	3.00	3.00	3.02	3.19	3.15	3.04	2.54	2.07	2.04	2.04	2.04	2.05	2.05	2.03	2.03	2.03	2.03	2.03
12 month	3.70	3.70	3.70	3.73	3.70	3.50	3.02	2.55	2.52	2.52	2.52	2.52	2.52	2.50	2.50	2.50	2.50	2.50
Savings deposit	1.86	1.58	1.41	1.48	1.44	1.40	1.25	1.11	0.95	0.93	0.91	0.91	0.89	0.89	0.88	0.89	0.88	0.87
Base lending rate (BLR)	6.00	5.98	6.20	6.72	6.72	6.48	6.38	5.89	5.53	5.53	5.53	5.53	5.53	5.51	5.51	5.51	5.51	5.51
Treasury bills (91 days)																		
Government securities (1 year)	2.93	2.24	3.30	3.55	3.53	2.89	2.50	2.07	1.99	1.99	2.07	2.14	2.06	2.05	2.07	2.09	2.09	2.12
Government securities (5 years)	4.28	3.64	3.73	3.70	3.78	3.00	2.79	3.21	3.49	3.61	3.57	3.80	3.69	3.75	3.74	3.91	3.73	3.79
Private Debt Securities																		
AAA																		
3-years	4.47	3.72	3.95	4.01	4.07	4.17	3.86	3.80	3.78	3.89	3.88	3.87	3.86	3.79	3.73	3.63	3.70	3.72
5-years	5.22	4.39	4.38	4.24	4.28	4.48	4.16	4.15	4.14	4.30	4.35	4.39	4.36	4.31	4.27	4.23	4.29	4.32
AA																		
3-years	5.05	4.27	4.36	4.38	4.38	4.95	4.77	4.69	4.70	4.68	4.67	4.71	4.70	4.58	4.54	4.43	4.48	4.50
5-years	5.89	5.00	4.81	4.71	4.64	5.31	5.14	5.11	5.17	5.16	5.16	5.22	5.17	5.13	5.07	5.02	5.05	5.07
A																		
3-years	6.22	5.82	5.94	5.91	6.06	6.90	6.87	6.78	6.77	6.75	6.76	6.78	6.78	6.86	6.92	6.78	6.85	6.80
5-years	7.13	6.66	6.70	6.53	6.51	7.43	7.47	7.45	7.43	7.38	7.37	7.42	7.41	7.60	7.66	7.59	7.58	7.57
BBB																		
3-years	9.96	9.77	9.44	9.57	9.71	10.32	10.19	10.17	10.25	10.19	10.20	10.26	10.20	10.32	10.37	10.09	10.21	10.18
5-years	11.01	10.81	10.41	10.51	10.72	11.36	11.34	11.19	11.23	11.15	11.18	11.24	11.19	11.36	11.41	11.19	11.31	11.32
BB & below																		
3-years	11.81	11.91	11.97	12.06	11.92	12.68	12.73	12.69	12.85	12.78	12.78	12.87	12.83	12.80	12.67	12.43	12.59	12.58
5-years	12.94	13.10	13.04	13.13	13.16	13.86	14.05	13.97	14.06	13.96	13.95	14.05	13.97	14.07	14.15	13.73	14.04	14.02

Table A.26
Movements of the Ringgit

	RM to one unit of foreign currency[1]			Annual change (%)		Change (%)
	2005	2008	2009	2008	2009	21 Jul.'05 -
	Jul.21[2]	End-Dec.				Dec. 2009
SDR	5.5049	5.3616	5.3487	-2.7	0.2	2.9
US dollar	3.8000	3.4640	3.4245	-4.5	1.2	11.0
Singapore dollar	2.2570	2.4070	2.4401	-4.7	-1.4	-7.5
100 Japanese yen	3.3745	3.8327	3.7076	-22.9	3.4	-9.0
Pound sterling	6.6270	4.9989	5.5001	32.2	-9.1	20.5
Swiss franc	2.9588	3.2715	3.3084	-10.0	-1.1	-10.6
Euro	4.6212	4.8759	4.9191	0.0	-0.9	-6.1
100 Thai baht	9.0681	9.9398	10.271	-1.2	-3.2	-11.7
100 Indonesian rupiah	0.0386	0.0316	0.0364	11.3	-13.1	6.2
100 Korean won	0.3665	0.2750	0.2937	28.4	-6.4	24.8
100 Philippine peso	6.8131	7.2774	7.4196	10.1	-1.9	-8.2
Chinese renminbi	0.4591	0.5076	0.5016	-10.8	1.2	-8.5

[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	
			2008	2009	2008	2009
Commercial banks	-		4.6[1,2]	3.6[1,2]	4,018[3]	4,086[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]	6.5	117	122
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	5.2[1]	5.12[1]	30	32
Borneo Housing Mortgage Finance Berhad	1958	To provide housing loans mainly to Sabah and Sarawak State Government employees	7.25 ~ 8.25	6.75 ~ 8.25	1	1
Bank Simpanan Nasional	1974	To promote and mobilise savings particularly from small savers and to inculcate the habit of thrift and savings	4.8	3.8	374	375
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	11

[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
Housing Loans Outstanding

	2008	2009*p*	2008	2009*p*	2008	2009*p*
	RM million		Annual change (%)		% share	
Commercial banks[1]	192,092	210,017	10.2	9.3	82.5	83.8
Treasury Housing Loans Division	27,393	26,716	2.1	-2.5	11.8	10.7
Bank Kerjasama Rakyat Malaysia Berhad	4,417	4,189	17.2	-5.2	1.9	1.7
Malaysia Building Society Berhad	5,141	5,647	16.5	9.8	2.2	2.3
Borneo Housing Mortgage Finance Berhad	742	717	3.6	-3.3	0.3	0.3
Bank Simpanan Nasional	2,887	3,034	9.1	5.1	1.2	1.2
Sabah Credit Corporation	179	163	-5.8	-9.0	0.1	0.1
Total	**232,850**	**250,484**	**9.4**	**7.6**	**100.0**	**100.0**

[1] Includes Islamic banks
p Preliminary
… Negligible

Source: Bank Negara Malaysia and various housing credit institutions

Table A.29
Housing Loans Approved

	2008	2009*p*	2008	2009*p*	2008	2009*p*
	RM million		Annual change (%)		% share	
Commercial banks[1]	57,946	70,474	20.3	21.6	84.7	89.2
Treasury Housing Loans Division	7,583	5,919	30.1	-21.9	11.1	7.5
Bank Kerjasama Rakyat Malaysia Berhad	297	115	-48.2	-61.4	0.4	0.1
Malaysia Building Society Berhad	1,566	1,650	-9.4	5.4	2.3	2.1
Borneo Housing Mortgage Finance Berhad	68	60	7.9	-11.7	0.1	0.1
Bank Simpanan Nasional	952	798	17.8	-16.2	1.4	1.0
Sabah Credit Corporation	13	4	-13.3	-67.2	…	…
Total	**68,424**	**79,020**	**19.7**	**15.5**	**100.0**	**100.0**

[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] Total	Businesses[1] of which: SMEs[2]	Households	Government	Total Financing
	RM million				
Net Change in Financing 2008					
Financial Intermediaries					
Banking Institutions	42,570	10,618	34,820	4,921	82,311
Development Financial Institutions (DFIs)[3]	3,087	258	6,573	-	9,659
Other Domestic Intermediaries[4]	12,010	(241)	571	-	12,581
Capital Market					
Bond Market[5]	15,492	-	-	33,601	49,094
Equity Market	5,477	-	-	-	5,477
External Financing					
Foreign Direct Investment	24,134	-	-	-	24,134
External Loan[6,7]	14,273	-	-	9,298	23,571
Total	**117,043**	**10,635**	**41,963**	**47,820**	**206,827**
Net Change in Financing 2009					
Financial Intermediaries					
Banking Institutions	20,371	5,589	38,559	9,085	68,015
Development Financial Institutions (DFIs)[3]	5,897	2,179	7,039	-	12,936
Other Domestic Intermediaries[4]	6,266	(744)	(676)	-	5,590
Capital Market					
Bond Market[5]	29,626	-	-	49,619	79,245
Equity Market	26,045	-	-	-	26,045
External Financing					
Foreign Direct Investment	5,663	-	-	-	5,663
External Loan[6,7]	(1,288)	-	-	1,914	626
Total	**92,581**	**7,024**	**44,922**	**60,618**	**198,121**

1 Businesses include non-bank financial institutions, domestic non-business entities and foreign entities
2 Adjusted to include reclassification of SMEs to large corporations
3 Refers to DFIs governed under the Development Financial Institutions Act, 2002
4 Other domestic intermediaries include insurance companies, Employees Provident Fund (EPF), housing credit institutions, leasing and factoring companies and the Treasury Housing Loan Division
5 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
6 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
7 External financing of Government includes financing to non-financial public enterprises (NFPEs)

Table A.31
Consolidated Public Sector Finance

	2006	2007	2008	2009*p*	2010*f*
	RM billion				
Revenue[1]	102.0	110.7	128.4	121.2	115.7
% growth	*7.4*	*8.6*	*15.9*	*-5.6*	*-4.5*
Operating expenditure	117.7	135.0	165.0	172.5	157.8
% growth	*10.4*	*14.7*	*22.2*	*4.5*	*-8.5*
Current surplus of NFPEs[2]	100.7	130.1	119.4	143.4	143.9
Current balance	**84.9**	**105.8**	**82.7**	**92.1**	**101.7**
% of GDP	***14.8***	***16.5***	***11.2***	***13.7***	***14.0***
Net development expenditure[3]	86.5	96.3	124.4	118.0	109.7
% growth	*31.0*	*11.3*	*29.1*	*-5.1*	*-7.1*
General Government[4]	40.8	44.7	50.5	52.2	55.1
NFPEs	45.7	51.6	73.8	65.8	54.6
Overall balance	**-1.6**	**9.4**	**-41.7**	**-25.9**	**-8.0**
% of GDP	***-0.3***	***1.5***	***-5.6***	***-3.8***	***-1.1***

[1] Excludes transfers within general Government
[2] Refers to 30 NFPEs from 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

	2005	2006	2007	2008	2009*e*	2010*f*
	Annual change (%)					
REAL GDP						
United States	3.1	2.7	2.1	0.4	-2.4	2.7
Japan	1.9	2.0	2.4	-1.2	-5.2	1.7
Euro area	1.7	2.9	2.7	0.6	-4.1	1.0
Germany	*0.8*	*3.2*	*2.5*	*1.3*	*-5.0*	*1.5*
United Kingdom	2.2	2.9	2.6	0.5	-5.0	1.3
INFLATION						
United States	3.4	3.2	2.8	3.8	-0.4	1.7
Japan	-0.3	0.3	0.0	1.4	-1.4	-0.8
Euro area	2.2	2.2	2.1	3.3	0.3	0.8
Germany	*1.9*	*1.8*	*2.3*	*2.8*	*0.2*	*0.2*
United Kingdom	2.1	2.3	2.3	3.6	2.2	1.5
	% of labour force					
UNEMPLOYMENT						
United States	5.1	4.6	4.6	5.8	9.3	10.1
Japan	4.4	4.1	3.9	4.0	5.1	6.1
Euro area	8.9	8.3	7.4	7.5	9.4	11.7
Germany	*10.7*	*9.8*	*8.4*	*7.3*	*7.5*	*10.7*
United Kingdom	4.8	5.4	5.3	5.6	7.6	9.3
	% of GDP					
CURRENT ACCOUNT BALANCE						
United States	-5.9	-6.0	-5.2	-4.9	-2.6	-2.2
Japan	3.6	3.9	4.8	3.2	2.8	2.0
Euro area	0.5	0.4	0.3	-0.7	-0.7	-0.3
Germany	*5.1*	*6.1*	*7.5*	*6.4*	*2.9*	*3.6*
United Kingdom	-2.6	-3.3	-2.7	-1.7	-2.0	-1.9
FISCAL BALANCE[1]						
United States	-3.2	-2.2	-2.8	-5.9	-12.5	-10.0
Japan	-5.0	-4.0	-2.5	-5.8	-10.5	-10.2
Euro area	-2.5	-1.2	-0.6	-1.8	-6.2	-6.6
Germany	*-3.3*	*-1.5*	*-0.5*	*-0.1*	*-4.2*	*-4.6*
United Kingdom	-3.3	-2.6	-2.6	-5.1	-11.6	-13.2

[1] Refers to general government fiscal balance
e Estimate
f Forecast

Source: International Monetary Fund and National Authorities

Table A.33
East Asia: Key Economic Indicators

	2005	2006	2007	2008	2009*e*	2010*f*
REAL GDP	Annual change (%)					
Regional Countries						
The People's Republic of China	10.4	11.6	13.0	9.6	8.7	10.0
Korea	4.0	5.2	5.1	2.2	0.2	4.6
Chinese Taipei	4.7	5.4	6.0	0.7	-1.9	4.7
Singapore	7.6	8.7	8.2	1.4	-2.0	4.5~6.5
Hong Kong SAR	7.1	7.0	6.4	2.1	-2.7	4.0~5.0
Malaysia	5.3	5.8	6.2	4.6	-1.7	4.5~5.5
Thailand	4.6	5.1	4.9	2.5	-2.3	3.5~4.5
Indonesia	5.7	5.5	6.3	6.0	4.5	5.5~6.0
Philippines	5.0	5.3	7.1	3.8	0.9	2.6~3.6
INFLATION	Annual change (%)					
Regional Countries						
The People's Republic of China	1.8	1.5	4.8	5.9	-0.7	0.6
Korea	2.8	2.2	2.5	4.7	2.8	2.5
Chinese Taipei	2.3	0.6	1.8	3.5	-0.9	1.5
Singapore	0.5	1.0	2.1	6.6	0.6	1.6
Hong Kong SAR[1]	1.0	2.0	2.0	4.3	0.5	0.5
Malaysia	3.1	3.6	2.0	5.4	0.6	2.0~2.5
Thailand	4.5	4.7	2.2	5.5	-0.9	2.1
Indonesia	10.5	13.1	6.3	9.9	4.8	6.2
Philippines	7.6	6.3	2.8	9.3	3.3	4.0
CURRENT ACCOUNT BALANCE	% of GDP					
Regional Countries						
The People's Republic of China	7.2	9.5	11.0	9.8	7.8	8.6
Korea	1.7	0.6	0.6	-0.7	3.4	2.2
Chinese Taipei	4.9	7.2	8.6	6.4	7.9	8.0
Singapore	22.7	25.4	23.5	14.8	12.6	12.5
Hong Kong SAR	11.4	12.1	13.3	14.2	10.7	10.8
Malaysia	15.0	16.7	15.7	17.5	16.7	13.9
Thailand	-4.3	1.1	5.7	-0.1	4.9	2.7
Indonesia	0.1	3.0	2.5	0.1	0.9	0.5
Philippines	2.0	4.5	4.9	2.5	3.2	1.2
FISCAL BALANCE[2]	% of GDP					
Regional Countries						
The People's Republic of China	-1.4	-0.7	0.9	-0.1	-2.0	-2.0
Korea[3]	1.8	1.7	3.5	1.2	-2.8	-2.7
Chinese Taipei[3]	-0.6	-0.6	-0.2	-0.8	-4.3	-3.3
Singapore[3]	7.5	7.5	11.1	6.3	2.5	2.4
Hong Kong SAR[3]	1.0	4.1	7.7	0.1	-3.4	-1.5
Malaysia	-3.6	-3.3	-3.2	-4.8	-7.0	-5.6
Thailand	0.3	1.2	-2.3	-1.1	-5.6	-3.4
Indonesia	-0.2	-1.0	-0.7	-0.6	-1.5	-1.4
Philippines	-2.7	-1.0	-0.2	-0.9	-3.7	-3.6

[1] Refers to composite price index
[2] Refers to central government fiscal balance
[3] Refers to general government fiscal balance
e Estimates
f Forecast

Source: International Monetary Fund, National Authorities and Bank Negara Malaysia estimates