# The Malaysian Economy in 2001

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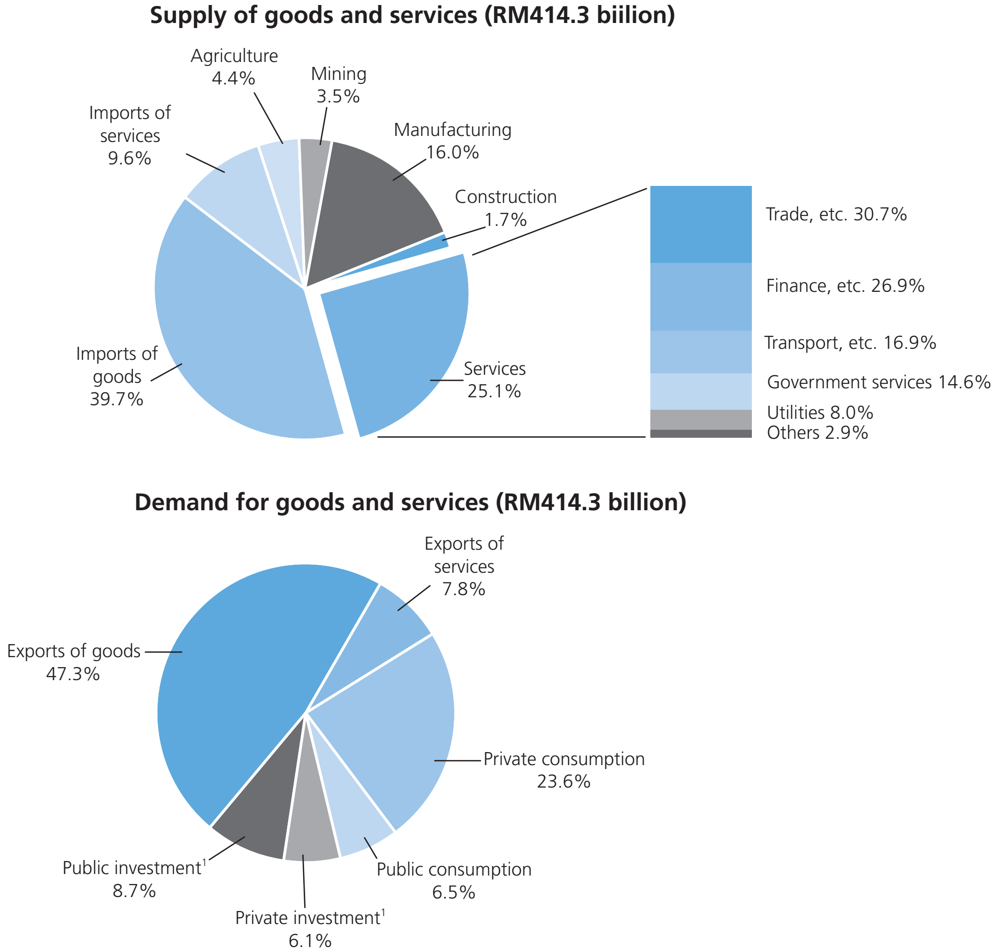
## Real GDP growth remained positive in 2001, supported by counter-cyclical measures and diversified economic structure.

**OVERVIEW**

The Malaysian economy remained resilient in 2001 in the face of a challenging external environment. While the global economic slowdown in 2001 was more severe than earlier expectations, Malaysia avoided economic contraction and growth for the year remained in positive territory. Unemployment was also contained at a low level.

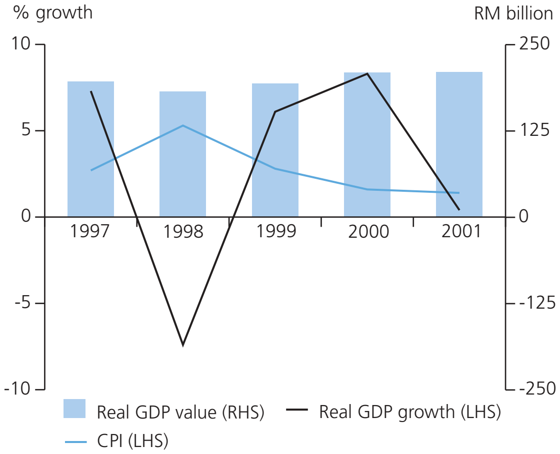
Given the openness of the Malaysian economy, the negative effects of the US economic slowdown and global electronics downturn was felt as early as March 2001. These were manifested in declining manufacturing production and negative export growth. Concerted efforts since the crisis to promote domestic sources of growth and reduce the over-dependence on exports resulted in real Gross Domestic Product (GDP) expanding by 0.4% in 2001. Fiscal stimulus measures and monetary policy that had remained accommodative led to higher public spending and positive growth in private consumption. During the year, public investment expenditure increased by 15.5%, while public

**Graph 1.1**
**The Economy in 2001 (at 1987 Prices)**

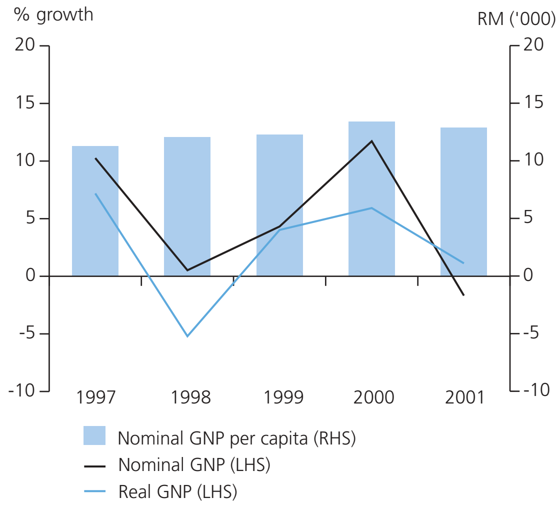



[1] Include stocks

**Graph 1.2**
**Real GDP and Inflation Rate**




**Graph 1.3**
**GNP Growth and Nominal GNP per Capita**



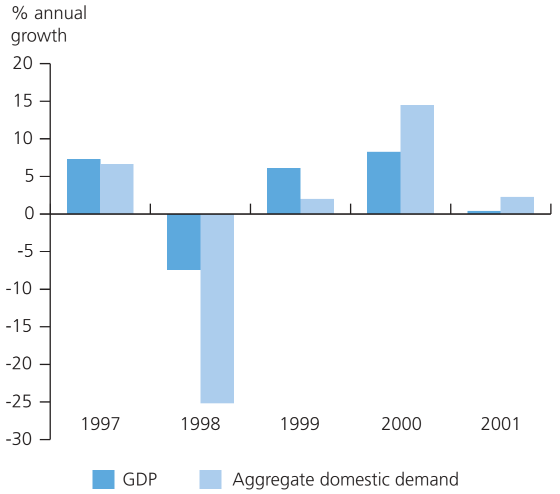

consumption expenditure increased by 11.9%. The direct contribution of the public sector (excluding the non-financial public enterprises) was significant, contributing 3.4 percentage points to GDP growth in 2001.

Through policies on several fronts, consumption has remained resilient despite lower export earnings. While national savings remained high at 34.9% of Gross National Product (GNP), total domestic consumption accounted for more than half of GDP. This resilience in private consumption together with the strong growth in public sector expenditure mitigated the impact of the external sector on the domestic economy and the contraction in domestic private investment, following the consolidation by the corporate sector.

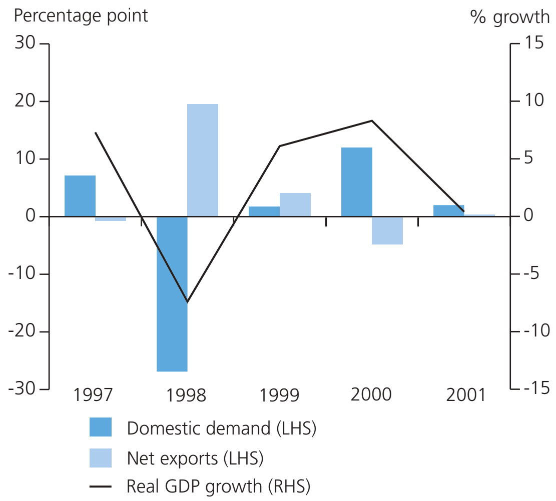
On the supply side, weaker growth in the export-oriented manufacturing industries was mitigated by positive growth in all other sectors, especially the services sector, domestic demand-oriented industries in the manufacturing sector and the construction sector. Overall, the effectiveness of policy measures and the diversified economic structure of the Malaysian economy moderated the impact of the decline faced by the export-oriented industries.

Consequently, the unemployment rate was contained below 4%. Retrenchment was mainly in industries affected by the downturn in the global electronics

**Graph 1.4**
**Real GDP and Aggregate Domestic Demand**




**Graph 1.5**
**Contribution to Real GDP Growth:**
**Domestic Demand and Net Exports**



## Table 1.1: Malaysia: Key Economic Indicators

| | | 1999 | 2000 | 2001*p* | 2002*f* |
|---|---|---|---|---|---|
| Population (million persons) | | 22.7 | 23.3 | 23.8 | 24.3 |
| Labour force (million persons) | | 9.2 | 9.6 | 9.9 | 10.2 |
| Employment (million persons) | | 8.9 | 9.3 | 9.5 | 9.8 |
| Unemployment (as % of labour force) | | 3.4 | 3.1 | 3.7 | 3.6 |
| Per capita income | (RM) | 12,304 | 13,412 | 12,889 | 13,272 |
| | (US$) | 3,238 | 3,529 | 3,392 | 3,493 |
| **NATIONAL PRODUCT (% change)** | | | | | |
| Real GDP | | 6.1 | 8.3 | 0.4 | 3.5 |
| (RM billion) | | 193.3 | 209.4 | 210.2 | 217.5 |
| Agriculture, forestry and fishery | | 0.4 | 0.6 | 2.5 | 1.0 |
| Mining and quarrying | | -2.6 | 3.1 | 0.2 | 3.0 |
| Manufacturing | | 13.5 | 21.0 | -5.1 | 4.2 |
| Construction | | -4.4 | 1.0 | 2.3 | 2.4 |
| Services | | 4.8 | 4.8 | 4.9 | 3.8 |
| Nominal GNP | | 4.3 | 11.7 | -1.7 | 5.3 |
| (RM billion) | | 279.5 | 312.2 | 306.7 | 323.1 |
| Real GNP | | 4.0 | 5.9 | 1.1 | 3.1 |
| (RM billion) | | 179.7 | 190.3 | 192.4 | 198.3 |
| Real aggregate demand[1] | | 2.0 | 14.5 | 2.3 | 2.8 |
| Private expenditure[1] | | -3.8 | 16.0 | -2.9 | 4.2 |
| Consumption | | 3.3 | 12.2 | 2.8 | 5.0 |
| Investment | | -21.8 | 28.7 | -19.7 | 1.2 |
| Public expenditure[1] | | 17.1 | 11.4 | 13.9 | 0.0 |
| Consumption | | 18.5 | 1.7 | 11.9 | 4.1 |
| Investment | | 15.9 | 19.9 | 15.5 | -3.0 |
| Gross national savings (as % of GNP) | | 41.1 | 39.5 | 34.9 | 33.8 |
| **BALANCE OF PAYMENTS (RM billion)** | | | | | |
| Goods | | 86.0 | 79.2 | 69.9 | 73.0 |
| Exports (f.o.b.) | | 319.6 | 374.0 | 334.3 | 349.1 |
| Imports (f.o.b.) | | 233.5 | 294.8 | 264.5 | 276.1 |
| Services balance | | -10.7 | -11.2 | -8.4 | -11.6 |
| (as % of GNP) | | -3.8 | -3.6 | -2.7 | -3.6 |
| Income | | -20.9 | -28.6 | -25.9 | -27.5 |
| (as % of GNP) | | -7.5 | -9.1 | -8.5 | -8.5 |
| Current transfers | | -6.6 | -7.5 | -8.1 | -8.4 |
| Current account balance | | 47.9 | 32.0 | 27.4 | 25.5 |
| (as % of GNP) | | 17.1 | 10.2 | 8.9 | 7.9 |
| Bank Negara Malaysia reserves, net[2] | | 117.2 | 113.5 | 117.2 | - |
| (as months of retained imports) | | 5.9 | 4.5 | 5.1 | - |
| **PRICES (% change)** | | | | | |
| CPI (2000=100) | | 2.8 | 1.6 | 1.4 | 1.8 |
| PPI (1989=100) | | -3.3 | 3.1 | -5.0 | 2.6 |
| Average wages in the manufacturing sector | | 3.0 | 5.0 | 1.5 | - |

Note: Figures may not necessarily add up due to rounding

[1] Exclude stocks

[2] Arising from the fixing of the ringgit/US dollar exchange rate in September 1998, all assets and liabilities in foreign currencies have been revalued into ringgit at rate of exchange ruling on the balance sheet data and the cumulative gain/loss has been reflected accordingly in the Bank's current year account. The US dollar equivalent of intrenational reserves as at 31 December 1999 was US$30.9 billion.

*p* Preliminary

*f* Forecast

### Table 1.2: Malaysia: Financial and Monetary Indicators

| | 1999 | 2000 | 2001*p* |
|---|---|---|---|
| **FEDERAL GOVERNMENT FINANCE (RM billion)** | | | |
| Revenue | 58.7 | 61.9 | 79.6 |
| Operating expenditure | 46.7 | 56.5 | 63.7 |
| Net Development expenditure | 21.5 | 25.0 | 34.2 |
| Overall balance | -9.5 | -19.7 | -18.4 |
| Overall balance (% of GDP) | -3.2 | -5.8 | -5.5 |
| Public sector net development expenditure | 46.4 | 50.4 | 68.2 |
| Public sector overal balance (% of GDP) | 2.3 | 0.7 | -4.9 |
| **EXTERNAL DEBT** | | | |
| Total debt (RM billion) | 161.1 | 157.7 | 169.8 |
| Medium and long-term debt | 138.7 | 140.3 | 146.4 |
| Short-term debt | 22.4 | 17.5 | 23.3 |
| Debt service ratio (% of exports of goods and services) | | | |
| Total debt | 6.1 | 5.3 | 6.2 |
| Medium and long-term debt | 5.7 | 4.9 | 5.8 |

| | | Change in 1999 | | Change in 2000 | | Change in 2001 | |
|---|---|---|---|---|---|---|---|
| | | RM billion | % | RM billion | % | RM billion | % |
| **MONEY AND BANKING** | | | | | | | |
| Money supply | M1 | 19.3 | 35.7 | 4.8 | 6.5 | 2.5 | 3.2 |
| | M2 | 40.7 | 13.7 | 17.6 | 5.2 | 7.8 | 2.2 |
| | M3 | 33.1 | 8.3 | 21.9 | 5.0 | 13.0 | 2.8 |
| Banking system deposits | | 20.4 | 4.7 | 14.6 | 3.2 | 8.6 | 1.8 |
| Banking system loans | | 0.6 | 0.1 | 23.6 | 5.5 | 16.4 | 3.6 |
| Manufacturing | | 0.4 | 0.6 | 2.2 | 3.3 | ... | 0.1 |
| Broad property sector | | 3.4 | 2.3 | 8.6 | 5.6 | 12.6 | 7.7 |
| Fianace, insurance and business services | | -4.1 | -10.7 | 0.4 | 1.3 | 0.9 | 2.7 |
| Loan-deposit ratio (end of year) | | 83.1% | | 84.3% | | 85.9% | |

| | | 1999 % | 2000 % | 2001 % |
|---|---|---|---|---|
| Interest rates (average rates at end of year) | | 3.18 | 3.25 | 3.27 |
| 3-month interbank | | | | |
| Commercial banks | | | | |
| Fixed deposits | 3-month | 3.33 | 3.48 | 3.21 |
| | 12-month | 3.95 | 4.24 | 4.00 |
| Savings deposit | | 2.76 | 2.72 | 2.28 |
| Base lending rate (BLR) | | 6.79 | 6.78 | 6.39 |
| Finance companies | | | | |
| Fixed deposits | 3-month | 3.49 | 3.52 | 3.22 |
| | 12-month | 4.13 | 4.27 | 4.01 |
| Savings deposit | | 3.50 | 3.44 | 2.94 |
| Base lending rate (BLR) | | 7.95 | 7.95 | 7.45 |
| Treasury bill (3-month) | | 2.71 | 2.98 | 2.73 |
| Government securities (1-year) | | 3.37 | 3.36 | 2.93 |
| Government securities (5-year) | | 5.21 | 4.80 | 3.18 |

| | 1999 % | 2000 % | 2001 % |
|---|---|---|---|
| Movement of Ringgit (end-period) | | | |
| Change against composite | -1.3 | 3.2 | 3.5 |
| Change against SDR | 2.7 | 5.2 | 3.8 |
| Change against US$[1] | 0.0 | 0.0 | 0.0 |

[1] Ringgit was pegged at RM3.80=US$1 on 2 September 1998

*p* Preliminary

cycle. More flexible labour market practices also helped to moderate the number of retrenchments. An increased number of workers accepted pay cuts and shorter working hours in 2001 as companies rationalised operations to maintain margins. This flexibility in the labour market remains a key fundamental strength of the Malaysian economy. Such flexibility allows for adjustments to adverse developments in the external environment.

Inflationary pressures remained muted with prices, as measured by the Consumer Price Index (CPI), increasing moderately by 1.4% (2000: 1.6%). The moderation in inflation was due mainly to the prevalence of excess capacity in several sectors of the economy, the moderate appreciation of the ringgit vis-a-vis non-US dollar currencies, as well as lower imported inflation. The lower inflation was also consistent with the widening output gap, estimated at 5.6% of the potential output level (details of the potential output estimation are presented in the white box).

The external position remained robust in 2001. The global economic slowdown affected export performance, but imports of goods and services for export production also declined. Hence, the current account remained in surplus, estimated at about 8.9% of GNP. In the financial account, the flows have been relatively stable. Long-term flows continued to dominate. Inward direct foreign investment flows were increasingly channelled to the services sector. These inflows were smaller in average dollar size and low in import content but have brought technology and other expertise that contribute towards raising productivity in Malaysia. Outward investments by Malaysian companies were smaller on a net basis, as Malaysian companies affected by the global slowdown repatriated proceeds of their disinvestment abroad in the second half-year.

The trade surplus and continued inflows of long-term capital resulted in higher international reserves. The reserves level fluctuated in early 2001 following volatility in foreign exchange markets. Reserves which declined in early 2001, reversed to a rising trend from end June following stronger fundamentals and lower interest rates abroad. By end-2001, international reserves of Bank Negara Malaysia (BNM) was higher at RM117.2 billion or US$30.8 billion (US$4.9 billion higher than the lowest level in 2001). Subsequently, reserves increased further to RM119.6 billion or US$31.5 billion as at 28 February 2002. This level is adequate to finance 5.2 months of retained imports and cover 5.1 times the short-term external debt.

While the external debt increased during the year, the outstanding amount remained relatively low, at about 55.4% of GNP (previous peak after the Asian crisis was 64%). The overall debt service ratio continued to remain low at 6.2%, despite the decline in export value. The debt profile also remained healthy with short-term debt accounting for only 13.7% of total debt.

The banking system demonstrated greater resilience despite adverse economic conditions. In 2001, the risk-weighted capital ratio (RWCR) remained above 12% throughout the year, whilst the increase in the levels of non-performing loans (NPLs) during the year was contained within manageable levels. The increase in the level of NPLs of banking institutions during the second half of 2001 was within expectations. As at end-2001, the net NPL ratio on a 6-month basis was 8.1% (11.5% on a 3-month classification basis). Recent measures to accelerate corporate restructuring have improved the balance sheet of the corporate sector, contributing to greater resilience of the banking system. The resolution of the debt restructuring schemes for companies in the transport sector in the final quarter of 2001 reduced the level of NPLs by 0.7 percentage points. As at end-2001, the banks' risk-weighted capital ratio stood at 12.8%, well above the Basel Capital Accord requirement of 8%. The capital position will further strengthen following the strong profits of RM7.4 billion recorded in 2001.

With improvements in the economy, Danamodal, the special purpose vehicle set up in 1998 to recapitalise viable banking institutions, received repayments amounting to RM2.3 billion in 2001 of the RM4.4 billion that was outstanding at the end of 2000. As a result, the outstanding investment in the remaining three recapitalised banking institutions amounted to RM2.1 billion. Since its inception, Danamodal has injected a total of RM7.1 billion into ten banking institutions.

With increases in NPLs remaining within manageable limits, Danaharta, the asset management company set up in 1998 to acquire NPLs from financial institutions, has shifted its focus to asset management and recovery in 2001. As at end-2001, the cumulative amount of NPLs restructured or approved for restructuring amounted to RM47.7 billion or 99.9% of the total

**Potential Output of the Malaysian Economy**

BNM's latest estimates of potential output indicate that output gap has widened in 2001 as actual output expanded at a slower pace of 0.4%, compared with an increase of 3.3% in potential output. Hence, the output gap increased to 5.6% of potential output in 2001 (peak: 12.3% of potential output in the third and fourth quarters of 1998).

As indicated in the previous studies, potential output has been expanding at a moderate rate since 1999. As shown in Table 1.3, potential output grew by 2.8% in the period 1999 - 2001, as against 4.9% GDP growth recorded in the same period. In 2001, the moderation in growth in potential output to 3.3% was attributed to the marginal decline in investment (-2.1%) and slower growth in labour (2.4%).

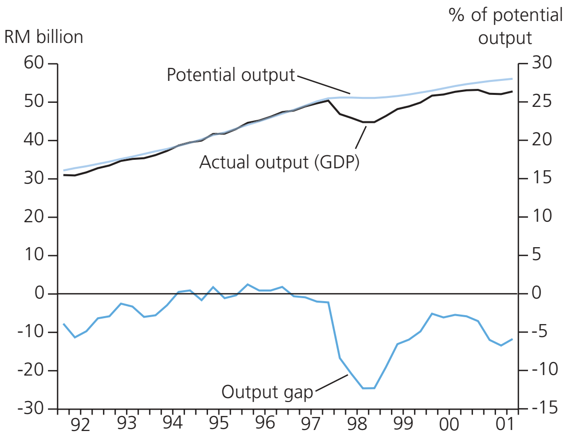
**Table 1.3**
**Actual GDP and Potential Output**

| Period | Actual GDP | Potential output | Investment | Labour | Output gap |
|---|---|---|---|---|---|
| | Annual change in % | | | | (% of potential output) |
| 1992-1997 | 9.2 | 8.2 | 14.1 | 3.9 | -1.3 |
| 1998 | –7.4 | 3.2 | –43.0 | –2.1 | –10.9 |
| 1999 | 6.1 | 1.3 | –5.9 | 3.7 | –6.8 |
| 2000 | 8.3 | 4.0 | 24.1 | 4.3 | –2.8 |
| 2001 | 0.4 | 3.3 | –2.1 | 2.4 | -5.6 |

As in the previous studies, the short-run elasticity of labour is still much higher than that of capital; implying changes in employment have greater impact on output. Firms attain higher output in the short run by hiring more labour but not by engaging in capital investment. The low elasticity of capital in the short run could also be explained by the significant investment in infrastructure projects, which have long gestation periods spanning over more than a decade and where the return is realised only after a time period.

However, the long-run elasticity of capital (0.5) is higher compared to 0.4 in the previous study, implying that the return to capital was higher in the year 2001. This could be caused by an increase in utilisation of capital stock put in place previously, as the investments in infrastructure during the 1990s begin to contribute to higher output.

**Graph 1.6**
**Actual Output and Potential Output**



NPLs in Danaharta's portfolio. Danaharta expects an average recovery rate of 56%, assuming a zero recovery rate on defaulted cases.

The market-driven corporate restructuring exercises gained momentum in 2001, moving beyond financial restructuring towards greater operational restructuring. Generally, corporate restructuring contributed to the improved financial position of corporates and the overall competitiveness of the economy. During the year, major institutional changes were effected. Institutional changes included a revamp of the CDRC guidelines to hasten the pace of restructuring of companies under its purview. Changes to the restructuring guidelines of the CDRC included improvements in the framework and approach to accelerate restructuring efforts, the establishment of a timeline for restructuring and more comprehensive disclosure and reporting. With the new initiatives, the restructuring of several large and complex cases were completed. The CDRC aims to complete the restructuring of the outstanding debts by July 2002. At the corporate level, the restructuring of debts was accompanied by operational restructuring in the form of disposal of non-core assets. Professional management was put in place by shareholders. The separation of ownership and management can be expected to further enhance corporate governance.

**Macroeconomic Management**

In 2001, macroeconomic policy was focused on managing the downside risks arising from the slowdown in the major industrial countries. Economic policies were targeted at creating an enabling environment for domestic demand to support growth. Given that there was considerable uncertainty over the severity of the slowdown in 2001, there was greater recognition that economic policies would need to address short-term cyclical risks that emerged during the course of the year, with the objective of minimising the adverse effects on the Malaysian economy.

The initial assessment was for Malaysia's GDP growth to show a moderating trend in the first two quarters of 2001, with a recovery in the second half-year. However, as the downturn in the global economy became more severe during the course of the year, policies turned more expansionary. The strengthened economic fundamentals provided Malaysia the policy flexibility to implement additional pro-growth policies in response to external shocks, without creating imbalances in the economy.

Given the increased prospects that the stimulus from the external sector would be relatively subdued in 2001, the overall budget deficit for 2001 announced in October 2000, was projected to remain large, at RM16.5 billion or –4.7% of GDP. The assessment was that a premature consolidation of the fiscal position in the face of a more challenging external environment would have a damaging impact on the economy. Consequently, as the downside risks facing the world economy increased in early 2001, the Government announced on 27 March, a fiscal stimulus package of RM3 billion. Following the heightened uncertainty after September 11, an additional stimulus package of RM4.3 billion was announced on 25 September.

In the Budget for 2002 announced in October 2001, the overall deficit of the Federal Government for 2001 increased to RM22.4 billion or –6.5% of GDP, an increase of RM5.9 billion from the original allocation announced a year earlier. This additional stimulus was equivalent to 2.2% of GDP. To ensure maximum impact from the increased expenditure, efforts were intensified to improve policy implementation, particularly to reduce project delays and increase efficiency for disbursements.

The 2001 Budget and the two additional fiscal packages announced in March 2001 and after September 11 not only included significant increases in both public consumption and capital outlays but also tax incentives to increase disposable income and reduce business costs. Measures to increase disposable income of households included higher tax rebates, higher allowances for civil servants in specific categories and a temporary reduction in the employees' Employees Provident Fund contribution rate. The announcement effect of the new measures to increase household income in the 2002 Budget also boosted private consumption. These measures included a reduction in personal income tax of between 1-2 percentage points and the 10% salary adjustment for civil servants, effective 1 January 2002.

Monetary conditions during the year also supported the expansion in private sector activities. Interest rates were already at historical lows at the end of 2000 with the aggressive reductions in interest rates by a total of 550 basis points in the period 1998 to 1999. Up to September 2001, the policy rate remained unchanged as the earlier interest rate reductions had been effective in promoting bank lending. Following September 11, BNM reduced its intervention rate on 20 September by 50 basis points to 5% as a pre-emptive measure to address the heightened risks biased towards further weakness. As a result, the average base lending rates (BLR) of the commercial banks and finance companies declined further to 6.39% and 7.45% respectively (6.78% and 7.95% respectively at end-2000).

Low interest rates and the initiatives to improve access to financing resulted in loans outstanding of banking institutions expanding by 3.6%. Together with private debt securities (PDS) issued by the private sector, total financing expanded by 6%. Efforts were also intensified in 2001 to ensure that selected sectors, especially the small and medium enterprises (SMEs), continued to have access to financing. The size and scope of several selected special funds were expanded and lending rates were lowered. As a result, loans extended to the SMEs by the banking system rose by 3.1% in 2001.

In pursuing the more expansionary demand management policies in 2001, care was taken that fiscal and monetary measures would not unduly increase risks of creating imbalances thereby jeopardising the long-term growth potential, price stability as well as the gains made in achieving a robust balance of payments. In particular, strengthening foreign direct investment inflows remained a priority. Incentives addressed the need for foreign direct investment inflows to be more diversified, in terms of location as well as sector. While attracting new investments, it was essential to create a more favourable environment to existing investors to expand operations in Malaysia.

The policy to allow 100% foreign equity ownership in promoted manufacturing industries, irrespective of export levels, was extended to 2003. As a measure to accelerate the development of the Eastern Corridor of Peninsular Malaysia, Sabah and Sarawak, Pioneer Status and Investment Tax Allowance that had been granted and expired on 31 December 2000 were extended for another five years. Effective 25 April 2001, the Foreign Investment Committee's guidelines on the acquisition of property by foreigners were also liberalised.

The incentive structure for investors, both domestic and foreign, is designed to attract quality investments that promote technology transfers, and not just expand production capacity. An important change made to the incentive scheme in the 2002 Budget was to extend the period for which the reinvestment allowance would remain in effect. Manufacturing companies and producers of food products would now enjoy the allowance for 15 consecutive years, commencing from the year the first investment is made, instead of the five years given previously.

Overall, the improved macroeconomic fundamentals reduced the risks that inflationary pressure would emerge over the medium term or that a significant misalignment in the exchange rate would occur. While Malaysia has pursued an expansionary fiscal stance for four consecutive years, the Federal Government debt was contained at 43.8% of GDP. The high domestic savings rate gave the flexibility to finance the deficit mainly from non-inflationary domestic sources of growth. The ample liquidity in the system, supported by strong surpluses in the balance of payments, allowed domestic financing of the deficit without crowding out the private sector.

The actual outturn of the financial position of the Government was better than expected. The overall financial position of the Federal Government registered a lower overall deficit of RM18.4 billion or -5.5% of GDP. As the shortfall on both operating and development expenditures was low at less than 5% each, the improvement was largely due to the better-than-expected revenue performance, emanating largely from higher income tax collection.

The thrust of policies introduced in 2001 to address longer-term structural issues focused on increasing domestic capacity, institution building and skills upgrading. The Government launched the Third Outline Perspective Plan (OPP 3) in April 2001, which documented the framework and strategies for economic development over the next ten years, 2001-2010. At the same time, the Government launched the Eighth Malaysia Plan, 2001-2005, which set out the first phase of implementation of OPP 3. Within the new framework for the economy, BNM and the Securities Commission took steps to develop longer-term strategies for the development of the financial sector and the capital market respectively.

The primary objective of the OPP 3 is to build a resilient and competitive nation by strengthening Malaysia's ability to meet the challenges arising from the rapid pace of globalisation and advances in information and communications technology. The Plan also takes into account the need to strengthen Malaysia's economic, financial and social resilience to withstand external shocks. Specifically, the OPP 3 aims to:

- Develop Malaysia into a knowledge-based economy where knowledge, creativity and innovation would increase productivity growth in all sectors;
- Generate domestic sources of growth by strengthening domestic investment in new areas of growth, while continuing to attract foreign direct investment in strategic areas;
- Re-orientate the strategies for human resource development to support a knowledge-based economy.

To advance the policy to increase the knowledge content of the economy, a masterplan for the transition towards a knowledge-based economy was completed in 2001.

Accordingly, the 2001 Budget as well as the 2002 Budget accorded priority to human resource development. Expenditure for education, training and skills development accounted for 23% of the Budget and 6.1% of GDP. Measures were initiated to promote computer literacy amongst students and employees, as well as improve teaching and learning methods. The existing curricula in schools and institutions of higher learning are being reviewed to meet the changing requirements of the economy. The restriction on tax deductions on bonus payments which was limited to two months, was also abolished in order to provide employers the flexibility to offer remuneration which was commensurate with workers' productivity. While emphasis has been placed on intensifying advanced skills development through training, retraining and apprenticeship schemes, efforts to pull the best talents from Malaysia and abroad have also been intensified. Incentives were provided in the 2001 Budget to attract highly skilled Malaysian citizens working abroad to return to Malaysia.

The Financial Sector Masterplan (FSMP), launched in March 2001 outlines the medium and long-term strategies for the development of the financial sector. The objective of the FSMP is to develop a competitive, resilient and dynamic financial system, based on international best practices, which would provide an enabling environment for long-term economic expansion. Phase one of the FSMP, which began in 2001 and covers a period of three years, focuses on enhancing domestic capacity and capabilities. Under the second phase, domestic competition would be intensified and in the third phase, the pace of integration with international markets will be enhanced.

A FSMP Secretariat and a FSMP Steering Committee (FSMP SC) have been set up in BNM, responsible for formulating mechanisms to effectively implement the FSMP recommendations. As at end-2001, out of the total 119 recommendations, nine of the recommendations were fully implemented and another 22 recommendations are being implemented on an ongoing basis.

The Capital Market Masterplan was launched in February 2001 with the objective of setting the strategic position and future direction for the Malaysian capital market. Of the 152 recommendations outlined in the Masterplan, 14 recommendations have been fully implemented, another 24 have been partially completed while 48 more are being addressed. Progress was made in the area of the consolidation of the stockbroking industry and the stock exchange, disclosure-based regulation and corporate bond market development.

Overall, Malaysia concluded the year 2001 in a stronger position with signs of stabilisation in the economy supported by the gradual recovery in export demand, strengthened economic fundamentals and significant progress made in addressing the long-term structural issues. The index of leading indicators which provides an early signal of the direction of the economy, has been rising for five consecutive months since July 2001, supporting the prospects for a recovery in the economy in 2002.

## SECTORAL REVIEW

### Manufacturing Sector

The overall performance of the manufacturing sector was affected by the slowdown in major industrial countries and the downturn in the global electronics cycle. While production in the export-oriented industries declined, industries that were dependent on domestic demand continued to expand, benefiting from the positive effects of the fiscal stimulus programme and low interest rates. Domestic demand for passenger cars and construction-related materials remained strong throughout the year. As a result, capacity utilisation in the domestic-oriented industries remained high at close to 80%. The strength in the domestic-oriented sector had mitigated, to some extent, the more severe contraction in the export-led manufacturing activities.

The production of export-oriented industries, which was relatively resilient in the first quarter of 2001, was affected more by the pronounced slowdown in external demand in the subsequent quarters. Nevertheless, with the emerging signs of improvements in the external environment towards the end of the year, the declines in manufacturing activities moderated in the fourth quarter of 2001, with both the exports and production of manufactured goods registering smaller declines. Given these developments, the decline in the overall manufacturing production and value added for 2001 as a whole was contained at a single-digit rate of 6.4% and 5.1% respectively (2000: +25% and +21% respectively).

While operating in a slower business environment during the year, some manufacturers had taken the opportunity to consolidate and streamline their operations in order to better position themselves in the increasingly competitive global market. This was evident in the relocation of the labour-intensive industries and lower-end operations from Malaysia to lower cost producing countries such as Thailand. At the same time, some manufacturers also transferred their higher-end operations to Malaysia to take advantage of the existing well-developed manufacturing facilities, competitive incentive structure as well as a workforce that is well-trained and proficient in the English language.

In addition, there were increasing efforts by exporters to explore export opportunities in niche markets. During the year, Malaysia's exports of manufactured goods to the Middle-East increased by 20.4%, with the share of total manufactured exports increasing to 2.4% from 1.8% in 2000. Major products that were exported included electronics, electrical products, wood products and furniture, food products and chemical products. At the same time, Malaysia's manufactured exports to the People's Republic of China have also been on an upward trend, growing significantly by 41.2% to account for a higher share of 3.9% of total manufactured exports in 2001 (2000: 2.5%). The bulk of manufactured goods exported to the People's

**Graph 1.7**
**Manufactured Production and Exports**

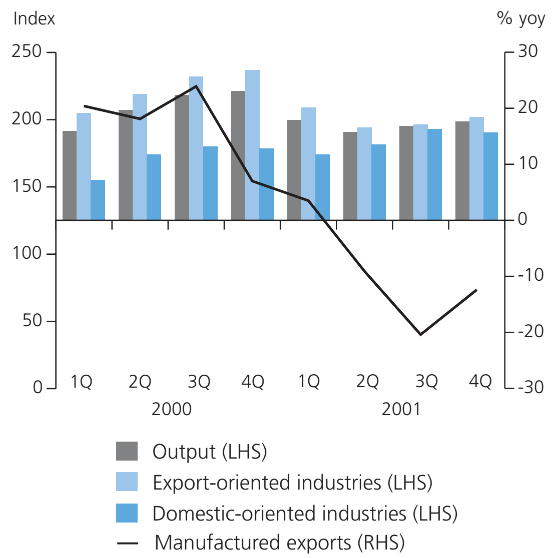
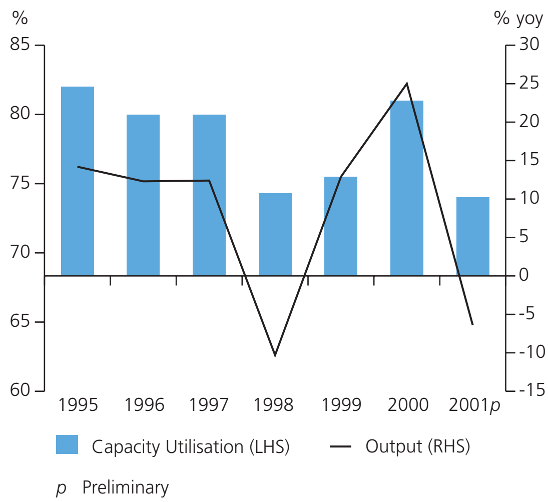


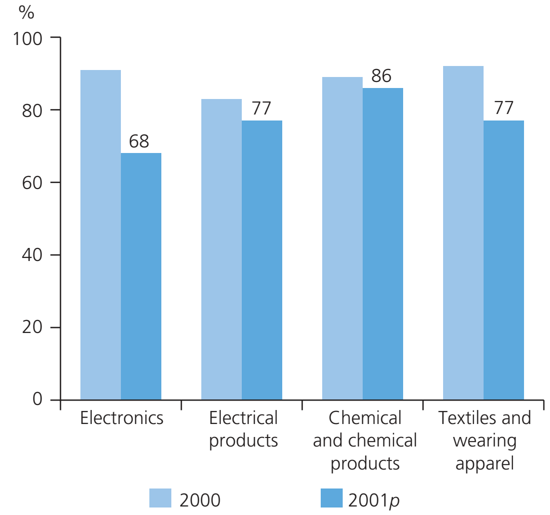

**Table 1.4**
**Manufacturing Sector: Value Added and Production**

| | 2000 | 2001 |
|---|---|---|
| | Annual change in % | |
| **Value-added (Constant prices)** | **21.0** | **-5.1** |
| **Overall Production** | **25.0** | **-6.4** |
| **Export-oriented industries** | **25.7** | **-10.2** |
| *of which:* | | |
| Electronics | 44.8 | -20.1 |
| Electrical products | 28.7 | -1.9 |
| Chemicals and chemical products | 15.1 | -7.6 |
| Wood and wood products | 4.0 | 1.3 |
| Textiles and wearing apparel | 8.7 | -8.5 |
| Rubber products | 4.0 | 3.3 |
| Off-estate processing | 11.7 | 7.7 |
| **Domestic-oriented industries** | **22.1** | **7.4** |
| *of which:* | | |
| Transport equipment | 19.1 | 20.6 |
| Petroleum products | 19.9 | 19.3 |
| Construction-related products | 18.6 | 5.0 |
| Fabricated metal products | 33.8 | 4.0 |
| Food products | 16.2 | 4.4 |

**Graph 1.8**
**Capacity Utilisation in the Manufacturing Sector**

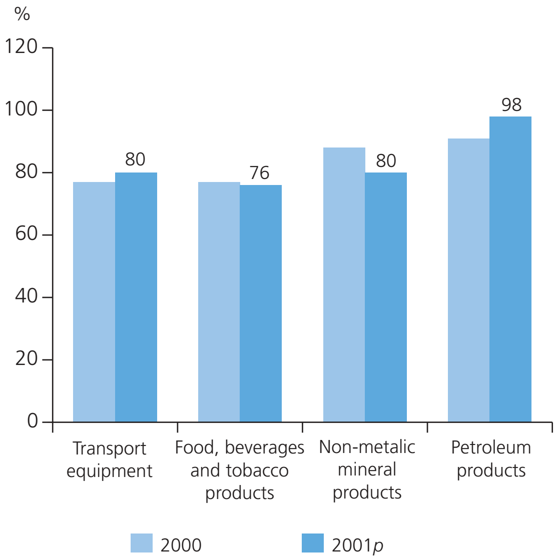


**Graph 1.9**
**Capacity Utilisation of Export-Oriented Industries**




*p* Preliminary

**Graph 1.10**
**Capacity Utilisation of Domestic-Oriented Industries**

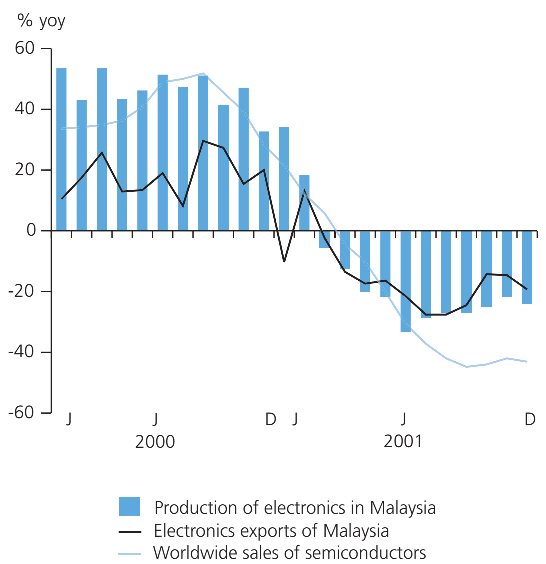



*p* Preliminary

## The strength in the domestic-oriented sector mitigated the contraction in the export-oriented industries. Growth was most pronounced in the transport-related industries.

Republic of China comprised electronics and electrical products, chemical products, wood products and metal products.

**Graph 1.11**
**Production and Exports of the Electronics Industry**




The **electronics industry** was the most affected by the slowdown in global demand in 2001. During the year, most electronics manufacturers drew down inventories accumulated from a year of strong capacity expansion in 2000. As the downturn in the global IT sector became more pronounced since the second quarter of 2001, the electronics manufacturers undertook measures to rationalise operations. These included wage cuts and shorter working hours to improve cost effectiveness as well as retraining of workers to move into higher-end operations. An encouraging development in the second half-year was the increase in demand from niche markets for products such as disk drives for the video game systems and personal video recorders. This supported the operations of disk drive makers based in Malaysia.

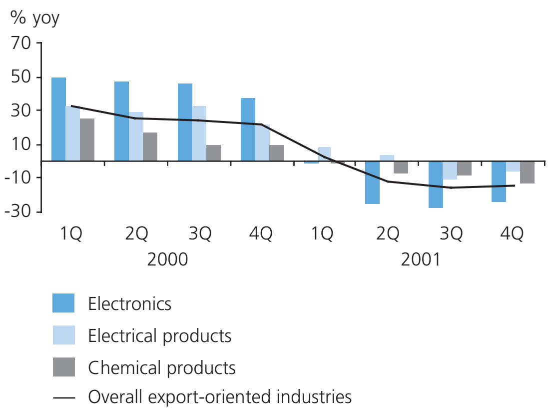
The production of **electrical products** was more resilient in the first half of 2001 and only began to moderate in the second half of the year, as external demand for audio-visual products and communication products declined. Exports to the major markets, especially the US, Japan, Singapore, Hong Kong SAR and Europe declined, due to lower demand for consumer durables, such as digital video disc (DVD) players, video compact discs (VCD) players and flat screen televisions. Nevertheless, exports to some countries in the region such as the People's Republic of China, Thailand, Indonesia and the Middle-East continued to be sustained.

Performance of the **textiles and wearing apparel industry** was adversely affected by the weak external demand conditions. During the year, both the production and exports of textiles and wearing apparel declined due to lower demand from the major buyers, namely, the US, Hong Kong SAR, Singapore and Europe.

About 50% of output of the **chemical products industry** are linked to the production of electronics and electrical products. Consequently, the lower demand for resins and plastic products as well as lower usage of industrial gases in the electronics and electrical products industries affected the production of chemical products. At the same time, slower external demand for resins, toiletries and pharmaceutical products also contributed to the decline in output of this industry. While the production of the more export-oriented chemical products declined, products which have stronger linkages with the domestic-oriented activities continued to experience output growth. These products included paints, varnishes and lacquers for use in car production and construction activities.

During the year, output of **off-estate processed products** increased, in line with the sustained demand and higher production of crude palm oil. The **rubber products industry** benefited from higher

**Graph 1.12**
**Output Performance of Selected Export-Oriented Industries**



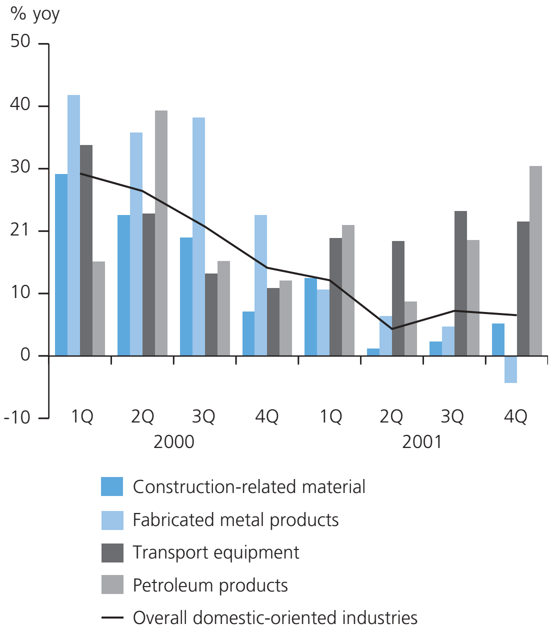

external demand for gloves, especially from the US, following the threat of the anthrax scare. Despite the increased production, export proceeds of rubber products declined further during the year, due to continued low export prices for gloves arising from competition from Thailand. Gloves accounted for about three quarters of total production and exports of rubber products. Output of tyres and tubes was also affected by competition from cheaper imports from Thailand and Indonesia as well as better quality tyres from Japan.

The production of **wood products** was sustained in 2001, reflecting mainly the strong saw milling activities in the early part of the year. Production declined towards the middle of the year when external demand deteriorated further. Like the rubber products industry, the increased volume of wood products did not translate into higher export receipts, as prices of plywood and sawn timber remained low in the global market amidst sluggish demand from Japan and the US. Similarly, lower external demand also resulted in the decline in exports of furniture and parts in 2001.

Supported by the sustained strong domestic demand, most of the industries producing for the domestic market continued to register positive growth in 2001. In particular, output from the **transport equipment** and petroleum products industries continued to record double-digit expansion. The production of transport equipment, including passenger cars as well as motor vehicle parts and accessories expanded by 20.6% during the year. Higher demand was stimulated by measures to raise disposable income and favourable financing conditions. The strong output performance of the transport equipment industry had a favourable impact on domestic demand for **petroleum products**. The export earnings of petroleum products increased further albeit at a slower pace, reflecting mainly the lower crude oil prices towards the middle of the year.

The positive effects of the fiscal stimulus programme were reflected in the continued output expansion of **construction-related materials** to meet demand from the construction sector. The production of iron and steel products as well as non-metallic mineral products, including cement and concrete products, tiles and ceramic products expanded further during the year. Nevertheless, exports of the non-metallic mineral products declined, reflecting to a large extent, the intense price competition,

**Graph 1.13**
**Output Performance of Selected Domestic-Oriented Industries**




particularly from Indonesia for tiles and ceramic products as well as other structural clay products in the international markets. These products accounted for about 28% of total exports of the non-metallic mineral products industry.

Output of all sub-sectors in the **fabricated metal products industry** increased, except for the copper and aluminium sub-sector which was affected by lower demand from the electronics industry. Meanwhile, the production of sub-sectors like structural and fabricated metal products, wire products and tin cans was sustained by continued activities in the construction sector and the beverages industry.

Output of the **paper and paper products industry** grew marginally, affected primarily by the decline in the production of containers, paper boxes and paperboard, as packaging activities especially in the export-oriented products industries slowed down. Supported by the strong sustained consumer spending, output of the **food, beverages and tobacco products industries** continued to sustain a positive growth during the year.

**Construction Sector**

The fiscal stimulus programme, privatisation of infrastructure projects and housing development contributed to a stronger growth of 2.3% in the **construction sector**. Construction activity in the non-residential sub-sector consolidated further due to the large overhang of office and retail space.

The **civil engineering sub-sector** benefited significantly from Federal Government development expenditure on construction-related projects, especially projects in the transportation, education and health sub-sectors. Growth in construction activity also emanated from commencement of four privatised road projects and one independent power plant. The former included the Kajang Ring Road, Ipoh-Lumut Highway, Guthrie Corridor Expressway and the Butterworth Outer Ring Road while the independent power plant was the Technology Tenaga in Perlis. Construction activity was also undertaken for ongoing works related to airports, rail, ports, waste disposal, water and sewerage projects. Among the major ongoing projects during the year were the New Pantai Expressway, Express Rail Link, the Kuala Lumpur Monorail System and the development of Putrajaya. Given the importance of infrastructure project financing to support growth of the civil engineering sub-sector, Bank Pembangunan dan Infrastruktur Malaysia Berhad's loan approvals totalled RM7.4 billion in 2001, compared with RM7.6 billion in 2000. The Bank increased its loan disbursement to RM4.4 billion (2000: RM2.7 billion).

Measures undertaken by the Government to support economic growth and increase disposable income led to a positive growth of the **residential sub-sector** in 2001. Growth was supported by strong underlying demand for residential units, particularly affordable and conventional housing in choice locations with good accessibility. The low interest rate environment with financial institutions offering competitive housing loan packages with lower margin requirements and longer tenure provided additional impetus. Other incentives included withdrawals of EPF funds for the purchase of a second house provided the first house has been sold; exemption from stamp duties; lifting limitations for financial institutions to finance the construction of residential properties priced above RM250,000 each and shop houses within residential areas; and allowing proceeds from private debt securities to be used to finance the development of such properties provided they achieve break-even sales in value terms.

In 2001, demand in choice locations strengthened while sales performance of new launches of housing schemes in poor locations showed a declining trend during the latter half, with the take-up rate declining from 53% in the first quarter to 40% during the third quarter. The value and number of residential property transactions also fell marginally. Nevertheless, government measures to reduce the property overhang by granting stamp duty exemptions for the purchase of completed properties from developers resulted in a total of 6,100 units of properties valued at RM1.7 billion being sold during 2001. This represented about a quarter of the 24,000 units of properties valued at RM7.7 billion that were offered by developers registered with the Real Estate & Housing Developers' Association of Malaysia (REHDA).

Indicators of optimism of rising demand in the residential sub-sector included increase in new developers' licences issued with more units approved for construction in Peninsular Malaysia;

**Table 1.5**
**Residential Property Indicators**

| | 2000 | 2001 |
|---|---|---|
| | Number | |
| Residential property transactions | | |
| Number | 170,932 | 165,309 |
| Value (RMb) | 21.9 | 20.8 |
| Approvals[1] | 214,290 | 227,260 |
| Developers' licences | | |
| New | 997 | 1,095 |
| Renewals | 416 | 413 |
| Sales and advertising permits | | |
| New | 969 | 1,014 |
| Renewals | 1,249 | 1,461 |
| Loans by banking system - value (RMb) | | |
| Outstanding | 74.3 | 87.1 |
| Approvals | 24.9 | 27.1 |

[1] Units approved for construction by private developers in Peninsular Malaysia

Source: NAPIC, Valuation and Property Services Department, Ministry of Housing and Local Government and Bank Negara Malaysia

## Growth in the construction sector was supported by fiscal stimulus programme and low interest rates.

new sales and advertising permits as well as renewals of such permits; and increase in loans for residential properties. Mortgage loans granted by the banking system rose by 17.2% (RM12.8 billion). Similarly, loans approved by other housing credit institutions also increased during the year. In particular, loans by the Treasury Housing Loans Division increased significantly due to higher loan eligibility for civil servants and the ability to utilise the balance of loan eligibility to purchase a second house. In line with higher approvals, total housing loans outstanding increased in 2001.

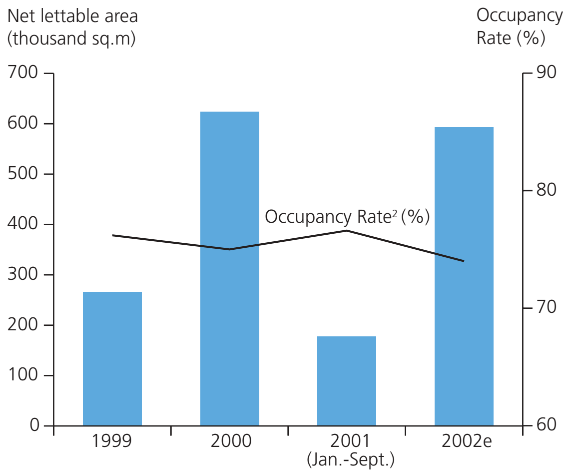
Prices of residential properties rose marginally during 2001 after appreciating by 15.4% since the first half of 1999. The Malaysian House Price Index rose at an annual rate of 0.9% during the first half of 2001. However, prices declined marginally compared with the preceding six months. Prices of terraced and semi-detached houses recorded increases, while the detached and high-rise units registered price declines. Although the index remained below the peak level recorded in 1997, house prices in several states exceeded the pre-crisis levels. Generally, all states registered price

**Table 1.6**
**Property Overhang, Incoming Supply and Planned Supply**

| | Overhang | | In-coming Supply | Planned Supply | In-coming Supply | Planned Supply |
|---|---|---|---|---|---|---|
| | June-01 | | June-01 | | Sept-01 | |
| | Units/ '000 s.m. | Value (RMb) | Units/ '000 s.m. | | Units/ '000 s.m. | |
| Residential (units) | 35,203 | 4.9 | 477,693 | 342,972 | 471,835 | 359,077 |
| Purpose-built office ('000 s.m.) | 2,528 | 8.8 | 2,540 | 1,951 | 2,453 | 1,917 |
| Shopping complexes ('000 s.m.) | 1,449 | 9.3 | 1,508 | 1,718 | 1,509 | 1,715 |
| Retail shops (units) | 7,817 | 2.2 | 25,154 | 25,351 | 25,339 | 26,180 |
| Industrial properties (units) | 3,295 | 1.3 | 8,254 | 23,170 | 8,395 | 23,017 |

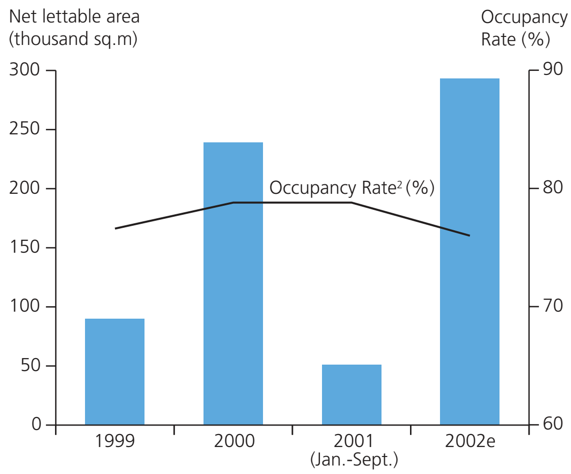
Source : NAPIC, Valuation and Property Services Department

**Graph 1.14**
**New Supply of Purpose-Built Office Space in the Klang Valley[1]: 1999-2002**




[1] Refers to Kuala Lumpur and Selangor
[2] Refers to end of period
e Estimates by BNM
Source: NAPIC, Valuation and Property Services Department

**Graph 1.15**
**New Supply of Retail Space in the Klang Valley[1]: 1999-2002**

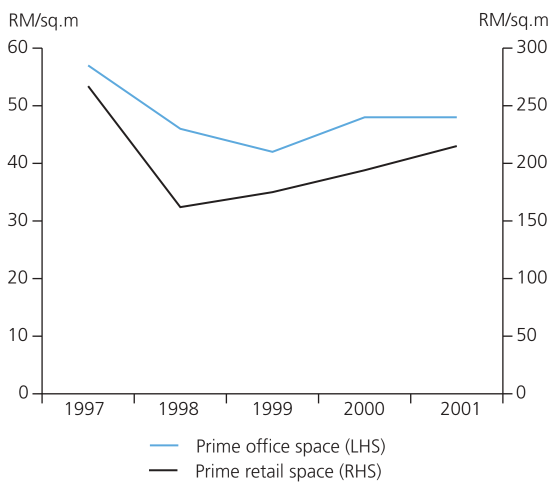



[1] Refers to Kuala Lumpur and Selangor
[2] Refers to end of period
e Estimates by BNM
Source: NAPIC, Valuation and Property Services Department

increases, except for Selangor and Kelantan where prices declined marginally. In particular, terraced houses in Kuala Lumpur recorded the highest price increase of 20.5%.

The **property overhang** situation improved primarily due to the sales of residential properties. As at end-June 2001, data compiled by the National Property Information Centre (NAPIC) of the Valuation and Property Services Department showed that the

**Graph 1.16**
**Average Monthly Rentals for Prime Office and Retail Space in Klang Valley[1]**




[1] Refers to Kuala Lumpur and Selangor
Source: BNM, CH Williams Talhar & Wong Sdn. Bhd.

overhang of residential properties improved by 31.4% to 35,203 units, while the improvement in value terms was 26.5% to RM4.9 billion. The remaining unsold units were located mainly in poor locations. Demand for residential units was more resilient in the well-established locations.

Several measures were introduced during the year to reduce the property overhang. With the liberalisation of the FIC guidelines effective 25 April 2001, foreign purchases of commercial properties increased by 14% to RM634 million. However, sale of residential properties to foreigners declined.

The large overhang and low occupancy rates of office and retail space continued to restrain growth of the **non-residential sub-sector**. Construction of **purpose-built office and retail space** during 2001 was supported mainly by ongoing projects. Overall, with the decline in incoming supply, the average occupancy rate for office space and retail complexes in the Klang Valley stabilised in 2001. Commercial property transactions adjusted downwards by 5% in terms of value and 11% in volume terms.

Arising from higher demand, rentals of prime office and retail space edged upwards during the year, although the rental rates remained lower than pre-crisis levels. Rentals for office and retail space in secondary locations were most affected by the excess

**Table 1.7**
**Office and Retail Space-Unoccupied Space, Incoming Supply and Planned Supply by State (as at end-September 2001)**

| | Office Space | | | Retail Space | | |
|---|---|---|---|---|---|---|
| | Unoccupied Space | Incoming Supply | Planned Supply | Unoccupied Space | Incoming Supply | Planned Supply |
| | ('000 square metres) | | | | | |
| Kuala Lumpur | 1,388 | 1,376 | 1,037 | 320 | 767 | 738 |
| Selangor | 460 | 422 | 164 | 194 | 121 | 0 |
| Johor | 230 | 262 | 431 | 272 | 178 | 859 |
| Pulau Pinang | 189 | 141 | 47 | 277 | 290 | 22 |
| Negeri Sembilan | 29 | 62 | 140 | 53 | 60 | 64 |
| Perak | 43 | 68 | 6 | 62 | 47 | 0 |
| Melaka | 10 | 15 | 0 | 41 | 0 | 0 |
| Kedah | 16 | 23 | 16 | 72 | 18 | 25 |
| Pahang | 13 | 13 | 56 | 48 | 2 | 6 |
| Terengganu | 7 | 7 | 0 | 5 | 7 | 0 |
| Kelantan | 13 | 0 | 20 | 2 | 19 | 0 |
| Perlis | 5 | 34 | 0 | 8 | 0 | 0 |
| Sabah | 224 | 3 | 0 | 44 | 0 | 0 |
| Sarawak | 64 | 26 | 0 | 34 | 0 | 0 |
| **Total** | **2,692** | **2,453** | **1,917** | **1,432** | **1,509** | **1,715** |

Source : NAPIC, Valuation and Property Services Department

supply situation, as tenants became more selective, favouring commercial space in more strategic locations. Although the incoming supply of new office and retail space was on a declining trend, it was estimated that it would take five years to fully utilise existing office space, and 4.4 years for retail space. This was based on the assumption of an average annual take-up rate of 535,000 square metres for office space and 327,000 square metres for retail space as recorded during the period of 1992 to September 2001.

In the development of hotels, new hotels completed during the year increased to 288, which provided 6,344 rooms. The occupancy rate of hotels improved marginally to 59% as tourist arrival for the year rose to a record level of 12.8 million from 10.2 million in 2000.

### Agriculture sector

Value added in the **agriculture, forestry and fishery sector** (agriculture) expanded by 2.5% in 2001 due primarily to higher crude palm oil production and, to a lesser extent, higher output of livestock, fruits and vegetables. The latter reflected the initial signs of the positive impact of the Government's measures to increase domestic sources of growth through higher food production. Production of other major agricultural commodities including rubber, saw logs and cocoa declined during the year, reflecting mainly weaker global demand. Consequently, commodity prices, except for cocoa prices, fell in 2001. As a result of the decline in export prices as well as volume, the export earnings of the agriculture sector for 2001 declined by 13.2%.

Production of **crude palm oil**, which accounts for 35% of total value added in the agriculture sector, increased by 8.9% in 2001. The increase was on account of two factors: firstly, the area with newly matured trees particularly in Sabah was higher; and secondly, the volume of oil extracted was higher in line with favourable weather conditions. However, due to ample global supplies of vegetable oils, the export price of Malaysian palm oil remained below RM1,000 per tonne during January-July 2001. Thereafter, the price breached the RM1,000 level in August 2001 and remained above this level for the rest of the year. This turnaround was driven mainly by lower supplies of palm oil, particularly since August 2001, as external demand from Malaysia's traditional buyers was sustained. For 2001 as a whole, palm oil prices averaged RM944 per tonne (2000: RM1,122).

The low palm oil prices in the first half of the year prompted the Government to introduce incentives to reduce the supply of palm oil. This was done by reducing existing stocks and encouraging replanting. To reduce stocks and to promote exports, the Government allowed a full waiver of export duties on one million tonnes of crude palm oil and abolished

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

| | 2000 | | 2001*p* | |
|---|---|---|---|---|
| | Volume and Value | Annual change (%) | Volume and Value | Annual change (%) |
| **Value Added (RM million at 1987 prices)** | **17,687** | **0.6** | **18,129** | **2.5** |
| **Production** [1] | | | | |
| *of which:* | | | | |
| Crude palm oil | 10,842 | 2.7 | 11,804 | 8.9 |
| Rubber | 615 | -20.0 | 546 | -11.2 |
| Saw logs | 23,076 | 5.9 | 19,554 | -15.3 |
| Cocoa beans | 70 | -16.0 | 58 | -17.9 |
| **Exports (RM million)** | **23,014** | **-16.8** | **19,966** | **-13.2** |
| *of which:* | | | | |
| Palm oil | | | | |
| ('000 tonnes) | 8,863 | -1.1 | 10,466 | 18.1 |
| (RM/tonne) | 1,122 | -30.5 | 944 | -15.9 |
| (RM million) | 9,948 | -31.3 | 9,876 | -0.7 |
| Rubber | | | | |
| ('000 tonnes) | 978 | -0.6 | 822 | -16.0 |
| (sen/kilogramme) | 263 | 10.4 | 230 | -12.7 |
| (RM million) | 2,571 | 9.7 | 1,886 | -26.6 |
| Saw logs | | | | |
| ('000 cubic metres) | 6,484 | -3.8 | 4,834 | -25.5 |
| (RM/cubic metre) | 384 | -2.9 | 315 | -17.9 |
| (RM million) | 2,489 | -6.5 | 1,523 | -38.8 |
| Sawn timber | | | | |
| ('000 cubic metres) | 2,876 | 2.1 | 2,411 | -16.2 |
| (RM/cubic metre) | 1,050 | 5.4 | 943 | -10.2 |
| (RM million) | 3,020 | 7.6 | 2,273 | -24.7 |

[1] All in '000 tonnes, except for saw logs in '000 cubic metres.

*p* Preliminary

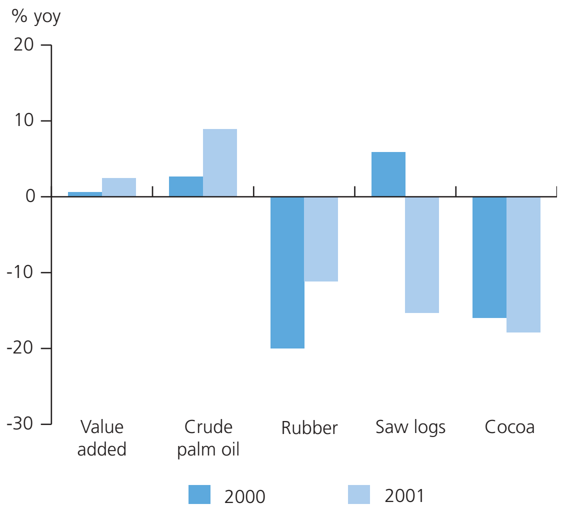
Source: Department of Statistics, Malaysia
Malaysian Palm Oil Board
Forestry Departments (Peninsular Malaysia, Sabah and Sarawak)
Malaysian Cocoa Board

the 5 percent duty on exports of semi-processed palm oil. To encourage replanting, the oil palm replanting scheme, which aimed to reduce 200,000 hectares of land planted with oil palm trees older than 25 years was introduced in March 2001. A total of RM200 million was allocated for the scheme. However, as palm oil prices improved in the latter half of 2001, the response to the replanting scheme, particularly among the smallholders, was not encouraging. As at end-2001, only 58,600 hectares or almost 30% of the area with old oil palm trees have been replanted. This has prompted the Government to extend the application period for the scheme to the end of June 2002.

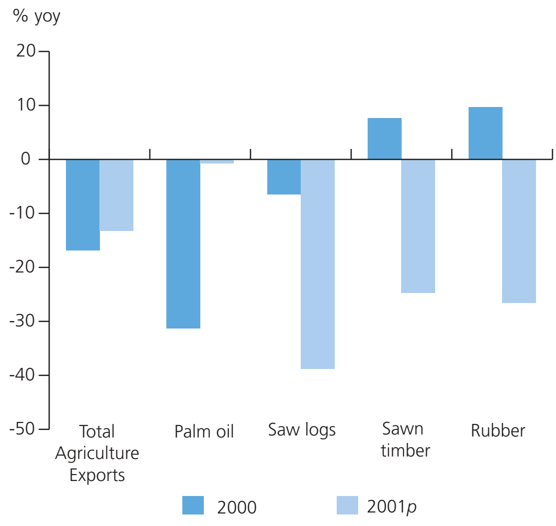
In 2001, the contraction in palm oil exports moderated to 0.7% due to the higher volume of exports (18.1%) and a more moderate decline in export prices (-15.9%). In particular, the higher export volume of palm oil was mainly on account of higher imports from major buyers, namely India, the European Union, the People's Republic of China and Pakistan. These markets accounted for 60% of Malaysia's total palm oil exports. Favourable export demand throughout the year coupled with lower production since September 2001 led to a reduction in total stocks of palm oil to 1.2 million tonnes at the end of the year (end-2000: 1.4 million tonnes).

As part of efforts to further expand and diversify Malaysia's export markets, the Malaysian Palm Oil Promotion Council together with the Technical Advisory Services (TAS) unit of the Malaysian Palm Oil Board undertook promotional activities. The TAS unit focused on market development through the provision of technical support to create greater

**Graph 1.17**
**Agriculture Production**



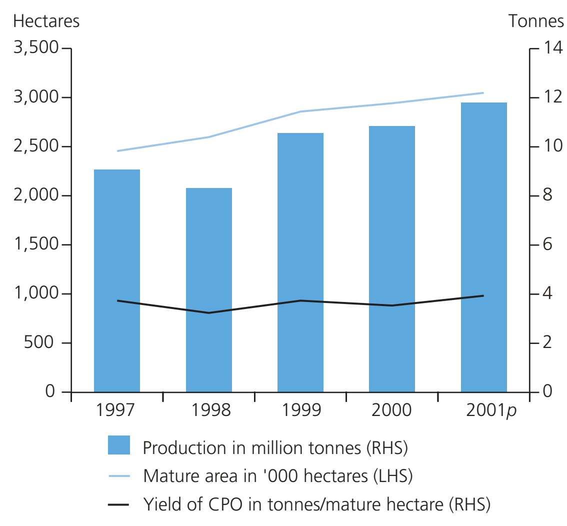

**Graph 1.18**
**Agriculture Exports**




*P* Preliminary

awareness of the technical attributes of the Malaysian palm oil in overseas markets. As a result, several new export markets such as in Ecuador, Liberia, Armenia and Palau were established. Meanwhile, research and development (R&D) activities on palm oil continued in 2001. Generally, such R&D activities can be grouped into innovative products, lipid technology and the oil and fats technology. The Oil and Fats Technology Centre continued to focus its R&D on the formulation of new palm-based food products that have potential for commercialisation by the relevant industrial sectors.

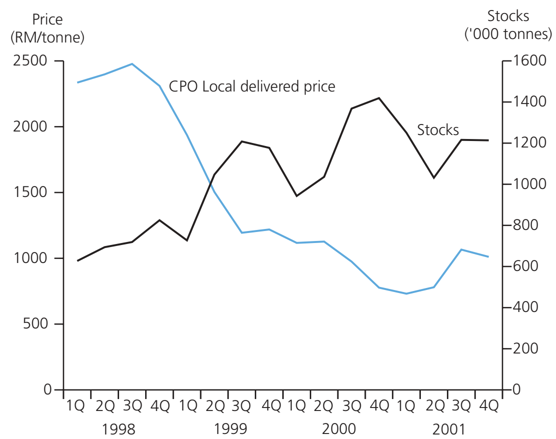
**Graph 1.19**
**Oil Palm: Area, Production and Yield**




*p* Preliminary for mature area and yield

The stronger growth in the agriculture sector in 2001 was also the result of higher production of the other agriculture group, which comprised mainly the livestock, fishery, fruits and vegetables sub-sectors. This increase was in line with efforts to increase domestic food production. **Livestock** production rose by 7.4% while the production of **fish** remained virtually unchanged from the preceding year's level. To further encourage cultivation of vegetables and fruits, the Ministry of Agriculture has established the Permanent Food Production Parks through the development of lands allocated by State Governments. By end-2001, 800 hectares of such land had been developed. Consequently, production of **fruits** and **vegetables** grew by 10.2% and 15.7% respectively.

**Graph 1.20**
**Palm Oil Prices and Stocks**



In 2001, Malaysian **natural rubber** (rubber) production declined to a record low of 546,180 tonnes, or 11.2% lower than in 2000. The decline was due mainly to the low rubber price, which continued to discourage tapping activities, particularly among the rubber smallholders. Smallholders contribute 82% to Malaysia's total rubber output. The production of rubber was also affected by the continuous conversion of areas planted with rubber to other crops or use. During the year, more than 16,000 hectares of rubber smallholdings were replanted with other crops. Taking cognisance that the incomes of most rubber smallholders were adversely affected by the prolonged period of low prices, the Government introduced monetary incentives of 30 sen per kilogramme for latex and 15 sen per kilogramme for cuplumps in the second half of 2001. These incentives were also aimed at encouraging tapping activities. Besides the monetary incentives, smallholders were encouraged to use modern and labour-saving tapping technology known as the Low-Intensity Tapping Systems (LITS) - a gaseous stimulation that can help raise tree productivity. For this purpose, the Government has allocated a total of RM180 million. Generally, LITS are encouraged for use in rubber plantations, primarily to ease the labour shortage and improve productivity.

Reflecting lower export prices and export volume, total earnings from rubber exports (including re-exports), declined by 26.6% in 2001. Rubber prices, which picked up in 2000, were unsustainable in 2001 as global supply exceeded consumption. The average price of rubber (as measured by RRS 1 prices) fell to RM2.27 per kilogramme. Prolonged low international rubber prices amidst an oversupply in the international markets, prompted the three major rubber producing countries, namely Thailand, Indonesia and Malaysia (which together account for 85% of the world's total natural rubber output), to co-operate to revive rubber prices through supply management. This Government-to-Government co-operation culminated in the establishment of the International Tripartite Rubber Organisation (ITRO) in July 2001. ITRO is responsible to a governing council, the International Tripartite Rubber Council. Among the initial arrangements under ITRO endorsed in December 2001, was an annual natural rubber production cutback of 4% and a reduction in exports by 10%, to commence in January 2002.

Arising from poor external demand, production of **saw logs** fell by 15.3% in 2001. In particular, demand from Japan, Taiwan, Hong Kong and Korea was lower in tandem with the global economic slowdown. In 2001, Malaysia's tropical logs continued to face stiff competition from softwoods particularly from Russia, Europe, Chile and New Zealand. As export demand was lower, export prices of saw logs fell to RM315 per cubic metre in 2001. Similarly, **sawn timber** also posted poor export performance with earnings declining by 24.7%. Lower export volume, particularly to major traditional buyers in the Asia-Pacific region, and lower prices contributed to the decline.

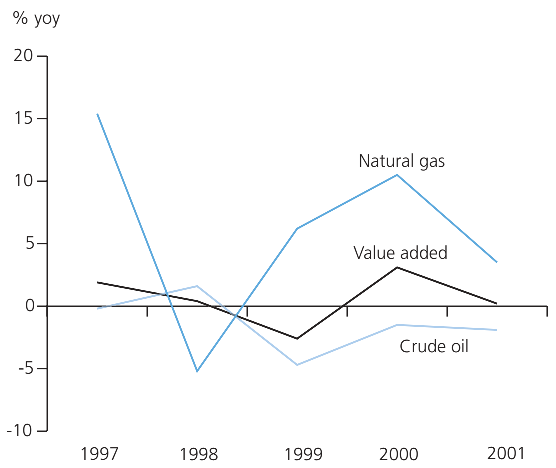
The Malaysian Timber Certification Council (MTCC), which was set up in January 1999 with the objective of operating a voluntary national timber certification scheme for Malaysia, officially launched its certification scheme in January 2002. The certification scheme is to be implemented in two phases. Under the first phase, the Malaysian Criteria, Indicators, Activities and Standards of Performance for forest management Certification (MC & I) would be used as the standard to assess forest management practices in the permanent forest estates at forest management unit levels. The MTCC certification scheme provides buyers of Malaysian timber products the assurance that the products are sourced from sustainably managed forests. In order to ensure a wider market acceptance of its scheme and certified products, MTCC has been working closely with the Forest Stewardship Council (FSC) and local stakeholders through the National Steering Committee to design an FSC-compatible certification standard that can be used under the second phase of the MTCC scheme. Based on the current progress in the implementation of the certification scheme, MTCC-certified timber products are expected to be available in the market by mid-2002.

Production of **cocoa beans** contracted by 17.9% in 2001 as yields were affected by unfavourable weather conditions. In addition, production was affected by continued conversion of cocoa cultivated land to other crops. Nonetheless, the Malaysian Cocoa Board intensified its efforts to increase cocoa productivity through rehabilitation programmes in selected areas. A significant development for the cocoa sector in 2001 was the marked pick up in international cocoa prices. This was brought about mainly by lower global supplies as production in major producing countries declined significantly. Malaysian cocoa prices rose to RM3,494 per tonne in 2001 (2000: RM2,879) leading to a 73.3% increase in total foreign earnings from cocoa exports.

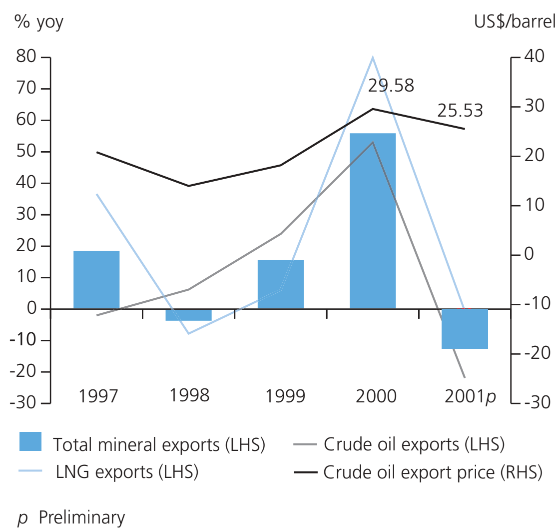
### Mining sector

In 2001, the **mining** sector grew moderately by 0.2%. The growth was driven primarily by higher production of natural gas, which increased by 3.2% in response to higher demand, particularly from the domestic power generation sub-sector. In contrast, production of crude oil and tin declined. Total **crude oil** production of 581,000 barrels per day (bpd.) was 2.3% lower than that of the previous year in response to lower external demand particularly by traditional markets in the region. It was also marginally below the 600,000 bpd. production target set for the year under the National Depletion Policy which aims to sustain the exploitation of the nation's crude oil reserves. Malaysia's total earnings from mineral exports were lower by 12.6% (2000: +55.9%) primarily due to weaker crude oil prices.

**Graph 1.21**
**Mining Production**




**Graph 1.22**
**Mineral Exports**




In 2001, amidst ample supply and weak global oil demand that worsened further following the September 11 incident, the price of crude oil in the international oil markets trended downwards. International oil prices, benchmarked to Brent price, ranged between US$25-US$28 per barrel in the first nine months of the year, before declining further to US$21.36, US$19.19 and US$18.80 in October, November and December respectively. For 2001 as a whole, the average Brent price was US$25 per barrel, lower by US$4.00 than the average oil price in the previous year. Oil prices declined despite efforts by the Organisation of Petroleum Exporting Countries to support oil prices through three crude oil production cutbacks totalling 3.5 million bpd. In line with the trend in global oil markets, the price of Malaysian crude oil exports was lower at an average of US$25.53 per barrel in 2001 (2000: US$29.58). Combined with lower export volume, export proceeds from crude oil declined by 21.9% (2000: +53%).

Production of **natural gas** increased in 2001. The increase was driven mainly by higher domestic demand, particularly from the power generation sub-sector, accounting for about 72% of the total domestic utilisation of natural gas. The district cooling system sub-sector, another main domestic user which utilises natural gas to produce chilled water for air-conditioning systems and generate electricity for several new business and administration centres in and around Kuala Lumpur, also recorded an increase in demand for gas. External demand for liquefied natural gas (LNG) also increased, albeit marginally by 0.4%. In tandem with lower crude oil prices, LNG prices also declined in 2001. With a marginal increase in export volume and a decline in price, export earnings from LNG declined by 0.7% in 2001.

In December 2001, a new gas field located offshore in Terengganu commenced operations to cater for the projected future increase in demand for gas. A total of 34 exploration wells and 56 development wells were drilled during the year, in addition to the 438,702 line kilometres of seismic data acquired for exploration and development purposes. In 2001, only one new production-sharing contract was signed.

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

| | 2000 | | 2001*p* | |
|---|---|---|---|---|
| | Volume and Value | Annual change (%) | Volume and Value | Annual change (%) |
| **Value Added (RM million at 1987 prices)** | **14,416** | **3.1** | **14,444** | **0.2** |
| **Production** | | | | |
| Crude oil and condensates (barrels per day) | 681,000 | -1.5 | 668,000 | -1.9 |
| *of which:* *Crude oil (barrels per day)* | *595,000* | *-2.2* | *581,000* | *-2.3* |
| Natural gas – net (million standard cubic feet) | 1,598,325 | 10.8 | 1,649,490 | 3.2 |
| Tin-in-concentrates (tonnes) | 6,307 | -14.1 | 4,900 | -22.3 |
| **Exports (RM million)** | **26,811** | **55.9** | **23,445** | **-12.6** |
| *of which:* | | | | |
| Crude oil | | | | |
| ('000 tonnes) | 16,672 | -5.9 | 15,077 | -9.6 |
| (US$/barrel) | 29.58 | 62.7 | 25.53 | -13.7 |
| (RM million) | 14,241 | 53.0 | 11,118 | -21.9 |
| Liquefied natural gas | | | | |
| ('000 tonnes) | 15,430 | 2.3 | 15,492 | 0.4 |
| (RM/tonne) | 740 | 75.9 | 732 | -1.1 |
| (RM million) | 11,422 | 79.9 | 11,342 | -0.7 |
| Tin | | | | |
| ('000 tonnes) | 21 | -14.2 | 27 | 32.3 |
| (RM/tonne) | 21,089 | 3.3 | 16,900 | -19.9 |
| (RM million) | 435 | -11.4 | 461 | 6.0 |

*p* Preliminary

Sources: PETRONAS
Department of Statistics, Malaysia
Department of Minerals and Geosience, Malaysia

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

| | As at 1 January | |
|---|---|---|
| | 2000 | 2001 |
| **Crude oil** | | |
| Reserves (billion barrels) | 3.43 | 3.39 |
| Reserve/Production (year) | 16 | 15 |
| **Natural gas** | | |
| Reserves (trillion standard cubic feet) | 84.4 | 82.5 |
| Reserve/Production (year) | 30-40 | 30-40 |

[1] The National Depletion Policy (NDP) 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).

Source: PETRONAS

### Services Sector

In a moderating growth environment, pro-growth policies to stimulate domestic activities resulted in growth of the services sector being sustained at a high level of 4.9% in 2001 (2000: 4.8%). Growth continued to be broad-based, with the intermediate services group expanding at a faster rate than the final services group. Supported by the strong growth, the contribution of the services sector to GDP rose to 55.8% (53.4% in 2000 and 51.9% in 1997).

**Intermediate services**, comprising transport, storage and communication; and finance, insurance, real estate and business services recorded stronger growth of 6.5% in 2001. The strong expansion in the **transport, storage and communication** sub-sector was primarily due to the rapid growth in the mobile phone and Internet services segment of the telecommunications industry and the increase in the local ports' transhipment activities. The market size for fixed telephones increased to 4.7 million as at end-2001 (2000: 4.6 million) while that for cellular telephones was 7.5 million (2000: 5.1 million). The prepaid service of the cellular telephone services also expanded in 2001 as it appealed to the younger generation and casual users. Demand for other value-added services with additional applications and features, such as the Short Messaging Services (SMS), also increased in 2001.

Government initiated programmes to enhance and expand the domestic shipping and ports services sub-sector contributed to the increase in cargo transhipment activities as well as in the handling capacity of cargo at local ports. With the continuous flow of new investment and with improvement in services provided by the port authorities nationwide, the activities of Malaysian ports expanded further in 2001. Container throughputs at six major ports recorded an increase of 43.5%.

The strong performance of the Port of Tanjung Pelepas (PTP) and Port Klang was the result of concerted plans by the Government to promote Malaysian ports as regional trade and shipping hubs. Port Klang has made significant progress in the past few years. In 2000, it was ranked 12th among the world's container ports, up two notches from the 14th position in 1999.

In year 2001, PTP managed a throughput of 2.04 million TEUs (20-ft equivalent units) with a total of 2,283 container vessels, calling at the port. This represented an increase of about five times over the 424,924 TEUs registered in 2000.

In terms of capacity expansion, Westport in Port Klang has increased its capacity from 1.8 million TEUs to 2.5 million TEUs with the construction of an additional 600 metres of berth length and an investment of more than RM100 million on equipment. Northport, in turn, has invested RM1.3 million to develop Phase I of the Wireless Application Protocol service designed for the logistics and transportation industry. Northport also invested in 10

**Graph 1.23**
**Services Sector: Quarterly Annual Growth**

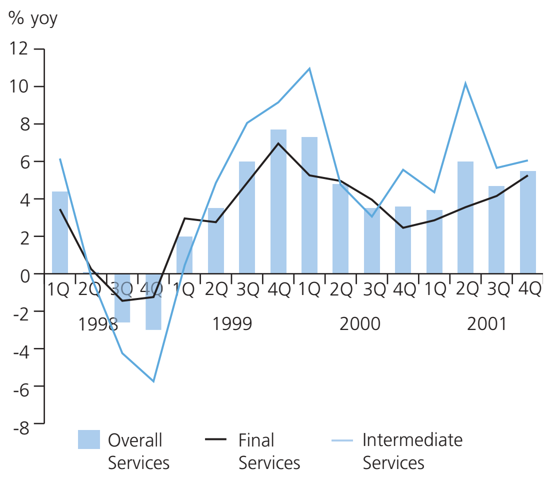



**Table 1.11**
**Growth in the Services Sector at Constant 1987 Prices**

| | 2000 | 2001*p* | 2000 | 2001*p* |
|---|---|---|---|---|
| | Annual change % | | % share of GDP | |
| **Services** | **4.8** | **4.9** | **53.4** | **55.8** |
| Intermediate services | 5.9 | 6.5 | 20.5 | 21.7 |
| Transport, storage and communication | 7.3 | 5.2 | 8.0 | 8.4 |
| Finance, insurance, real estate and business services | 5.1 | 7.3 | 12.5 | 13.4 |
| Final services | 4.1 | 3.9 | 32.9 | 34.1 |
| Electricity, gas and water | 7.5 | 5.6 | 3.8 | 4.0 |
| Wholesale and retail trade, hotels and restaurants | 5.8 | 3.3 | 14.8 | 15.2 |
| Government services [1] | 1.4 | 5.4 | 6.9 | 7.2 |
| Other services [2] | 1.5 | 2.9 | 7.5 | 7.7 |

[1] Include general public services (general public administration, external affairs and public order and safety), defence, health, education, and others.
[2] Include imputed rent from owner-occupied dwellings; community, social and personal services; products of private non-profit services to households; and domestic services of households.
*p* Preliminary

Source: Department of Statistics, Malaysia new straddle carriers and has ordered another seven carriers to complement the existing fleet.

The performance of the air transport industry was less favourable in 2001, due largely to the slowdown in international trade. Shipment of electronics and other goods from Malaysia were affected by the slowdown in electronics exports. Global passenger traffic also declined, particularly after the September 11 incident when passengers became more risk averse. Current measures to increase flight frequency from KLIA include open sky policy agreements for passenger and cargo services with several developed countries, bilateral agreements and strategic alliances with other airports to allow additional international landing rights, flight frequencies and new destinations.

Rail transport recorded a higher revenue in 2001, attributed mainly to the cargo business sector. The opening of the landbridge linking Thailand and Port Klang by rail has increased KTM Berhad's cargo revenue. In the case of the LRT, the total ridership for the year increased by 16.5% with 85 million passengers.

In the **finance, real estate and business services** sub-sector, value added growth was also higher. The increase reflected mainly higher collection of insurance premium income as well as the stronger performance of the banking institutions. Strong pick-up in activity in the stock market in the second half-year has contained the negative contribution of this sub-sector.

Growth in the **final services** group, which comprised utilities; wholesale and retail trade, hotels and restaurants; government services and other services was sustained at 3.9% in 2001 (2000: 4.1%). The **utilities** sub-sector recorded a higher growth despite weakening demand from lower manufacturing activities. Value added of electricity generation increased further due to higher demand by the domestic-oriented industry and the commercial sector. Growth in the sub-sector was also supported by an increase in the consumption of water, which rose by 7% in 2001.

The **wholesale and retail trade**, **hotel and restaurants** sub-sector recorded a positive performance in 2001, supported mainly by the fiscal stimulus measures that raised disposable incomes of the household sector. Higher tourist arrivals also contributed to positive performance of this sub-sector. In addition, Malaysia also benefited from the hosting of the South East Asia (SEA) Games in September.

## Growth in the services sector was sustained at a high level, with increased activity in new growth sectors.

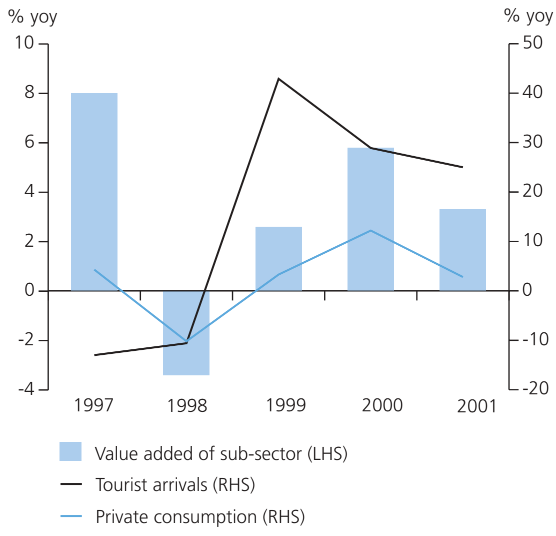
**Table 1.12**
**Selected Indicators for the Services Sector**

| | 2000 | 2001*p* |
|---|---|---|
| | Annual change % | |
| Cargo throughput at five major ports[1] | 14.9 | 10.4 |
| Container throughput at six major ports[2] | 30.3 | 43.5 |
| KLIA passenger | 11.9 | -1.3 |
| KLIA cargo | 21.6 | -13.7 |
| LRT ridership[3] | 81.1 | 16.5 |
| Insurance premiums | 28.6 | 12.4 |
| KLSE (turnover, volume) | –19.7 | –27.3 |
| Tourist arrivals | 28.9 | 25.0 |
| Hotel occupancy rate | 57.7 | 58.6 |
| Electricity production index | 6.1 | 8.6 |

[1] Include Port Klang, Johor Port, Penang Port, Sabah Ports and Bintulu Port.
[2] Include Port Klang, Johor Port, Port of Tanjung Pelepas, Penang Port, Sabah Ports and Bintulu Port.
[3] Include STAR and PUTRA
*p* Preliminary

Sources: Relevant port authorities; Sistem Transit Aliran Ringan Sdn Bhd (STAR); Projek Usahasama Transit Ringan Automatik Sdn Bhd (PUTRA);
Kuala Lumpur Stock Exchange (KLSE); Bank Negara Malaysia;
Malaysia Tourism Promotion Board;
and Department of Statistic, Malaysia

**Graph 1.24**
**Wholesale and Retail Trade, Hotels and Restaurants, Private Consumption and Tourist Arrivals**



In the **Government services** sub-sector, value added was higher in 2001. The increase reflected mainly higher expenditure on emoluments arising from the bonus payment of half month salary or at least RM1,000 to all civil servants.

**DOMESTIC DEMAND CONDITIONS**

In 2001, measures to promote domestic demand led to a stronger expansion in public sector spending and sustained growth in private consumption. As a result, the slowdown in **real aggregate domestic demand** (excluding stocks) was contained at 2.3% in 2001 (2000: 14.5%).

**Public sector expenditure** registered a stronger growth of 13.9% in 2001, supported by the expansionary budget and two additional fiscal stimulus packages. Efforts to improve efficiency of project implementation resulted in the implementation shortfall being contained at less than 5%. Consequently, growth in **public investment** expenditure remained strong at 15.5% in 2001 (2000: 19.9%). The higher capital spending allocated in the Budget and the first stimulus package was mainly for education and training, as well as infrastructure and industrial development, with the objective of stimulating economic growth in the immediate term, enhancing human resource development and capacity building in the longer term. The capital spending allocated under the second stimulus package was mainly for small projects for which funds could be disbursed immediately.

During the year, total capital expenditure of the Non-Financial Public Enterprises (NFPEs) was higher, attributed to the modernisation and expansion programmes of several major NFPEs, notably, Petroleum Nasional Berhad (PETRONAS), Tenaga Nasional Berhad (TNB), Putrajaya Holdings Sdn. Bhd., as well as Telekom Malaysia Berhad (TMB). Capital expenditure by PETRONAS included the implementation of the Malaysia Liquefied Natural Gas Tiga (MLNG 3) project, the integrated petrochemical complexes in Kertih and Gebeng as well as acquisition of new LNG tankers. Capital outlays by TNB were mainly for expansion and upgrading of power generation, transmission and distribution networks to ensure adequate supply of electricity to meet longer-term demand. TMB continued to channel its capital spending in information and communication technology. Capital outlays by Putrajaya Holdings Sdn. Bhd. were mainly for the new administrative centre in Putrajaya. Meanwhile, the two wafer fabrication plants, namely, First Silicon in Kuching and Silterra in Kulim, continued to expand their capacity.

The strong growth in **public consumption** expenditure of 11.9% in 2001 was due mainly to procurement of office supplies related to e-Government flagship applications, payments for professional services and bonus payments for the year 2001.

In an environment of low external demand, fiscal stimulus measures played an instrumental role in contributing to the positive growth in private consumption. **Private consumption**, as such, increased by 2.8% during the year. Low interest rates and the Government's measures to increase household disposable income through a temporary reduction in employee's EPF contribution rate, higher tax rebates and the increase in the taxable

## Public sector expenditure provided the main impetus to contain the slowdown in domestic demand.

**Graph 1.25**
**Real Domestic Demand Aggerates**

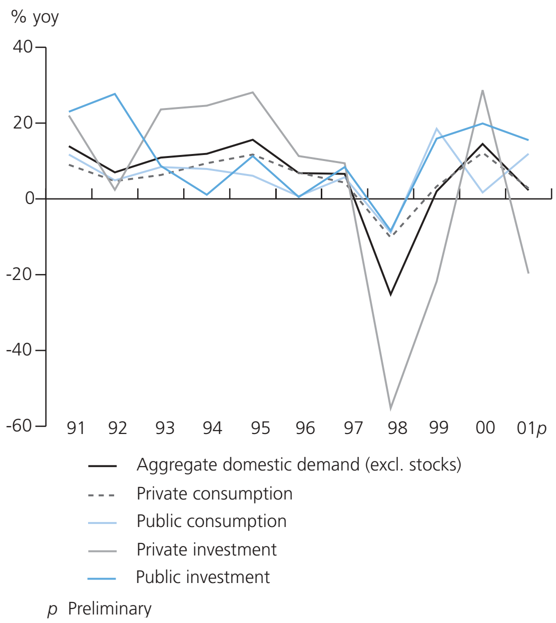


**Table 1.13**
**Private Consumption Indicators**

| | 2000 | 2001 | | | | |
|---|---|---|---|---|---|---|
| | | 1Q | 2Q | 3Q | 4Q | Year |
| **Sales of passenger cars (incl. 4WD)** | | | | | | |
| '000 units | 296.6 | 76.5 | 81.8 | 91.8 | 93.2 | 343.3 |
| Annual change (%) | 15.9 | 16.2 | 7.8 | 18.9 | 19.9 | 15.7 |
| **Imports of consumption goods** | | | | | | |
| US$ billion | 4.5 | 1.1 | 1.2 | 1.1 | 1.3 | 4.6 |
| Annual change (%) | 14.9 | 5.0 | 1.5 | –5.8 | 11.4 | 3.0 |
| **Tax collection (AG)** | | | | | | |
| Sales tax (RM billion) | 6.0 | 1.1 | 2.1 | 1.4 | 2.8 | 7.4 |
| Service tax (RM billion) | 1.7 | 0.3 | 0.6 | 0.4 | 0.7 | 1.9 |
| **Loans disbursed by banking system** | | | | | | |
| Consumption credit (excl. passenger cars) (RM billion) | 26.8 | 7.2 | 7.7 | 7.8 | 8.3 | 31.0 |
| Wholesale, retail, restaurants & hotels (RM billion) | 62.9 | 16.7 | 17.0 | 16.6 | 15.7 | 65.9 |
| **MRA retail sales** | | | | | | |
| Annual change (%) | 10.6 | 4.8 | -1.6 | 1.6 | 0.7 | 1.7 |
| **Credit card operation** | | | | | | |
| Turnover spending (RM billion) | 19.3 | 5.2 | 5.6 | 6.1 | 6.5 | 23.4 |
| Annual change (%) | 39.5 | 23.2 | 20.5 | 20.9 | 20.0 | 21.0 |
| **MIER Consumer Sentiments Index** | – | 105.7 | 96.2 | 98.7 | 93.8 | – |

**Table 1.14**
**Private Investment Indicators**

| | 2000 | 2001 | | | | |
|---|---|---|---|---|---|---|
| | | 1Q | 2Q | 3Q | 4Q | Year |
| **Sales of commercial vehicles (incl. 4WD)** | | | | | | |
| '000 units | 46.6 | 11.1 | 12.8 | 15.4 | 13.8 | 53.1 |
| Annual change (%) | 42.7 | 12.9 | 5.0 | 20.4 | 17.1 | 14.0 |
| **Imports of capital goods** | | | | | | |
| US$ billion | 11.6 | 3.2 | 2.8 | 2.6 | 2.9 | 11.5 |
| Annual change (%) | 38.6 | 42.4 | –5.2 | –24.4 | –2.6 | -1.1 |
| **Applications to MITI** | | | | | | |
| No. of projects | 974 | 168 | 201 | 197 | 146 | 712 |
| Capital investment (RM billion) | 46.2 | 3.6 | 4.9 | 3.9 | 3..4 | 15.8 |
| Foreign | 30.2 | 2.4 | 3.6 | 2.4 | 2.4 | 10.8 |
| Local | 16.0 | 1.2 | 1.3 | 1.5 | 1.0 | 5.0 |
| **Approvals by MITI** | | | | | | |
| No. of projects | 805 | 240 | 210 | 222 | 141 | 813 |
| Capital investment (RM billion) | 33.6 | 11.1 | 5.3 | 4.6 | 3.7 | 24.7 |
| Foreign | 19.8 | 8.1 | 3.7 | 3.5 | 3.0 | 18.3 |
| Local | 13.8 | 3.0 | 1.6 | 1.1 | 0.7 | 6.4 |
| **Loans disbursed by banking system** | | | | | | |
| Manufacturing sector (RM billion) | 94.1 | 25.1 | 27.3 | 25.6 | 26.0 | 103.9 |
| Construction sector (RM billion) | 23.6 | 5.8 | 5.5 | 4.6 | 4.9 | 20.9 |
| **Private Debt Securities** | | | | | | |
| Total fund raised (RM billion) | 22.5 | 5.2 | 4.9 | 7.8 | 12.6 | 30.6 |
| **MIER Business Conditions Survey** | | | | | | |
| Business Conditions Index | – | 46.3 | 44.0 | 42.6 | 42.3 | – |
| Capacity Utilisation Rate | – | 79.2 | 77.4 | 79.4 | 79.6 | – |

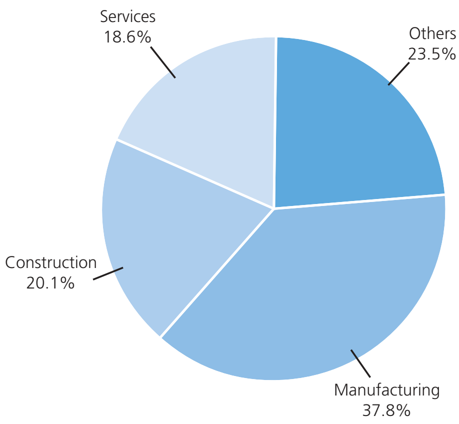
income bracket for the low- and medium-income groups contributed positively to growth in consumer spending. Major indicators for consumption, including sales of new passenger cars, sales and service tax collections as well as loans disbursed for both consumption purposes and general commerce, confirmed that consumption spending was sustained in 2001.

Reflecting the effect of lower external demand and excess capacity in selected sectors of the economy, particularly in the export-oriented industries, **private investment** declined by 19.7% in 2001. This trend was also reflected in several key investment indicators, including lower imports of capital goods and lower applications received for investment in the manufacturing sector.

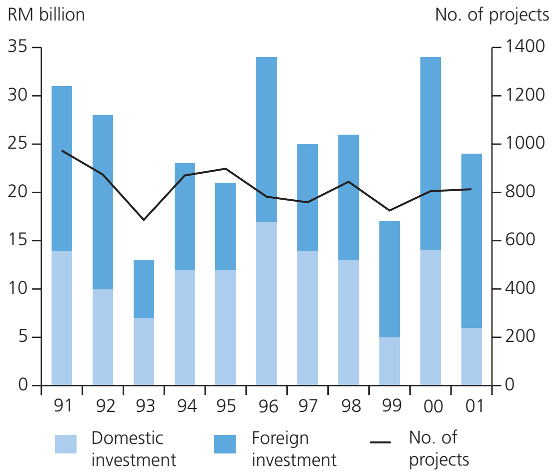
Capital investment in the **manufacturing sector** was estimated to decline by 24.1% in 2001. The overall capacity utilisation in the export-oriented industries in the manufacturing sector was below 80% throughout 2001. New investment activities in the manufacturing sector were mainly sustained by ongoing petrochemical projects, electrical and electronics projects approved in 2000 and 2001, as well as capacity expansion in the non-metallic mineral products industry where producers were already operating at high capacity.

The total value of investment in the manufacturing sector approved by the Ministry of International Trade and Industry (MITI) amounted to RM24.7 billion in 2001 (2000: RM33.6 billion). Of the total investment approved,

**Graph 1.26**
**Private Investment by Sector, 2001 (% share)**




**Graph 1.27**
**Approved Investment in the Manufacturing Sector**

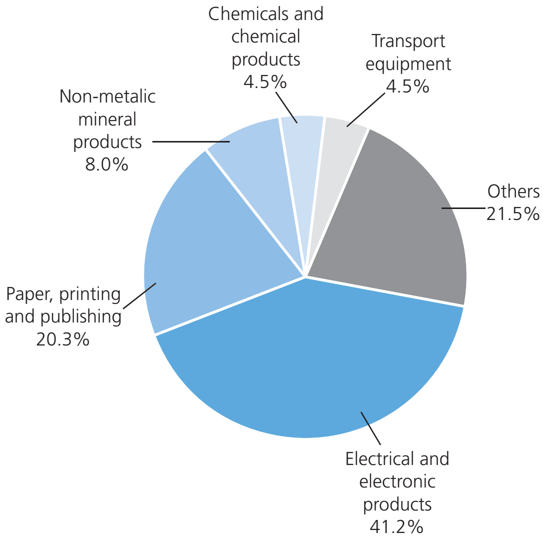



eight large projects, each with capital investment exceeding RM500 million, accounted for RM11.5 billion or 46.4% of the total investment approved. The electrical and electronic products industry continued to account for the highest share of 41.2% of total investment approved in 2001. This was followed by the paper, printing and publishing industry (20.3%); non-metallic mineral products industry (8%) and chemicals and chemical products industry (4.5%).

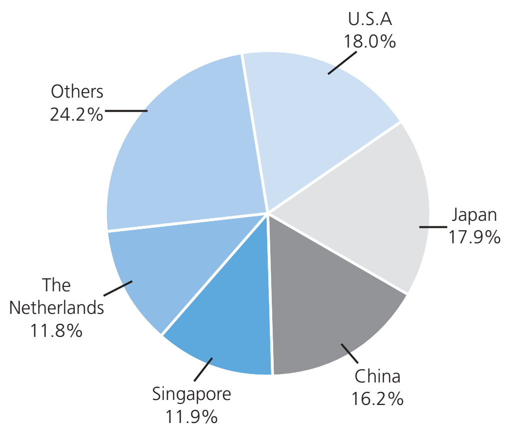
The value of foreign investment approved in the manufacturing sector in 2001 was RM18.3 billion (2000: RM19.8 billion). The bulk of the new projects approved were in the electrical and electronic products industry (51.4%); paper, printing and publishing industry (16.8%) and non-metallic mineral products industry (8.7%). The top five sources of foreign investment during the year were the United States, Japan, China, Singapore and the Netherlands. These countries together accounted for 76% of total foreign investment approved by MITI.

Capital spending in the **construction sector** in 2001 was supported by the construction of several highway projects, including SPRINT Highway and Elevated Highway (completed in 2001) as well as

**Graph 1.28**
**Approved Manufacturing Investment by Industry, 2001 (% share)**




**Graph 1.29**
**Foreign Participation in Approved Manufacturing Investment by Country, 2001 (% share)**



Kajang Ring Road, SPRINT Highway (Package C), Kajang-Seremban Expressway and Guthrie Corridor Expressway. Investment in the residential sub-sector continued to be high, due mainly to the construction activities for affordable housing and selected high-cost housing in strategic locations.

In the **services sector**, capital investment in the utilities sub-sector was lower, due to the deferment of several power plant projects, including those in Sepang, Jimah and Johor. Nevertheless, investment in this sub-sector continued to be supported by construction of ongoing power plants and water supply projects, including TNB Janamanjung, Nur Generation and Sungai Selangor water supply projects. Capital spending in the transport sub-sector was supported by the ongoing construction of the Express Rail Link and KL Monorail projects. The continuous capacity expansion of Malaysian ports, including the West Port and Port of Tanjung Pelepas, also contributed to the investment in the transport sub-sector. Investment in the telecommunications sub-sector was supported by sustained capital spending in mobile line services, particularly for upgrading of network.

Capital outlays in the mining and agriculture sectors increased in 2001, albeit at a marginal rate. Investment in the **mining sector** was estimated to increase by 2%, due mainly to continuous expansion in the oil and gas sub-sector. Investment in the **agriculture sector** expanded in 2001, attributable to the positive effects of the Government's incentives, which encouraged private sector participation on a bigger scale, modern and integrated mixed farming activities in food production, as well as higher allocation for this sector under the National Agricultural Policy.

In 2001, savings of both the public and private sectors were lower. Public sector savings declined by 15.1%, attributed to the higher growth in public consumption and a slower growth in public sector revenue as a result of lower revenue from the NFPEs. In the private sector, the Government's policies to increase disposable income and lower interest rates were effective in encouraging consumers to draw down on their past high savings to maintain a positive growth in consumption. Overall, the share of **gross national savings** to GNP declined to 34.9%. Nevertheless, given the consolidation in investment activities, the savings-investment balance remained in surplus for the fourth consecutive year, recording a surplus of RM27.4 billion or 8.9% of GNP in 2001 (2000: RM32 billion or 10.2%).

**Table 1.15**
**Savings-Investment Gap**

| | 2000 | 2001*p* |
|---|---|---|
| | (RM million) | |
| Public gross domestic capital formation | 45,686 | 47,094 |
| Public savings | 56,522 | 47,986 |
| Deficit / surplus | 10,836 | 892 |
| Private gross domestic capital formation | 45,569 | 32,657 |
| Private savings | 66,691 | 59,172 |
| Deficit / surplus | 21,122 | 26,515 |
| Gross domestic capital formation | 91,255 | 79,751 |
| (% of GNP) | 29.2 | 26.0 |
| Gross national savings | 123,213 | 107,158 |
| (% of GNP) | 39.5 | 34.9 |
| Balance on current account | 31,958 | 27,407 |
| (% of GNP) | 10.2 | 8.9 |

*p* Preliminary

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

## PRICES AND EMPLOYMENT

### Consumer Prices

Consumer price inflation or headline inflation[1] remained low in 2001. The Consumer Price Index (CPI) moderated further to 1.4% in 2001 (1.6% in 2000). Core inflation[2] or underlying inflation computed by BNM, also displayed a similar trend, moderating to 1% (1.5% in 2000). While consumer spending was sustained, the prevalence of excess capacity in several sectors of the economy led to downward pressure on prices. In addition, the moderate appreciation of the ringgit against non-US dollar currencies during the year, as well as lower inflation abroad, also contributed to lower inflation in 2001.

1 Headline inflation refers to the rate of change in the Consumer Price Index (CPI) for all items in the basket of goods and services published by the Department of Statistics, Malaysia.
2 Core inflation is a measure of the underlying inflation that excludes price-controlled items and price-volatile items, as well as items that are subject to one-off price adjustments from the original CPI basket. There are, however, several alternative measures of core inflation ( refer to Box article II in Annual Report 2000).

The moderation in the rate of inflation during the year largely reflected lower increases in the price of food. Food, which accounts for more than a third of the total CPI basket, rose by a slower rate of 0.7% in 2001 (1.9% in 2000). While demand remained moderate, food production and supplies increased during the course of the year following favourable weather conditions and continued Government measures to increase domestic food production. Imported food prices were also lower, concomitant with the moderate appreciation of the ringgit.

Despite the prevalence of excess capacity, prices for beverages and tobacco; transport and communication; as well as medical care and health expenses registered higher rates of increase. These largely reflected the impact of one-off price adjustments arising from:

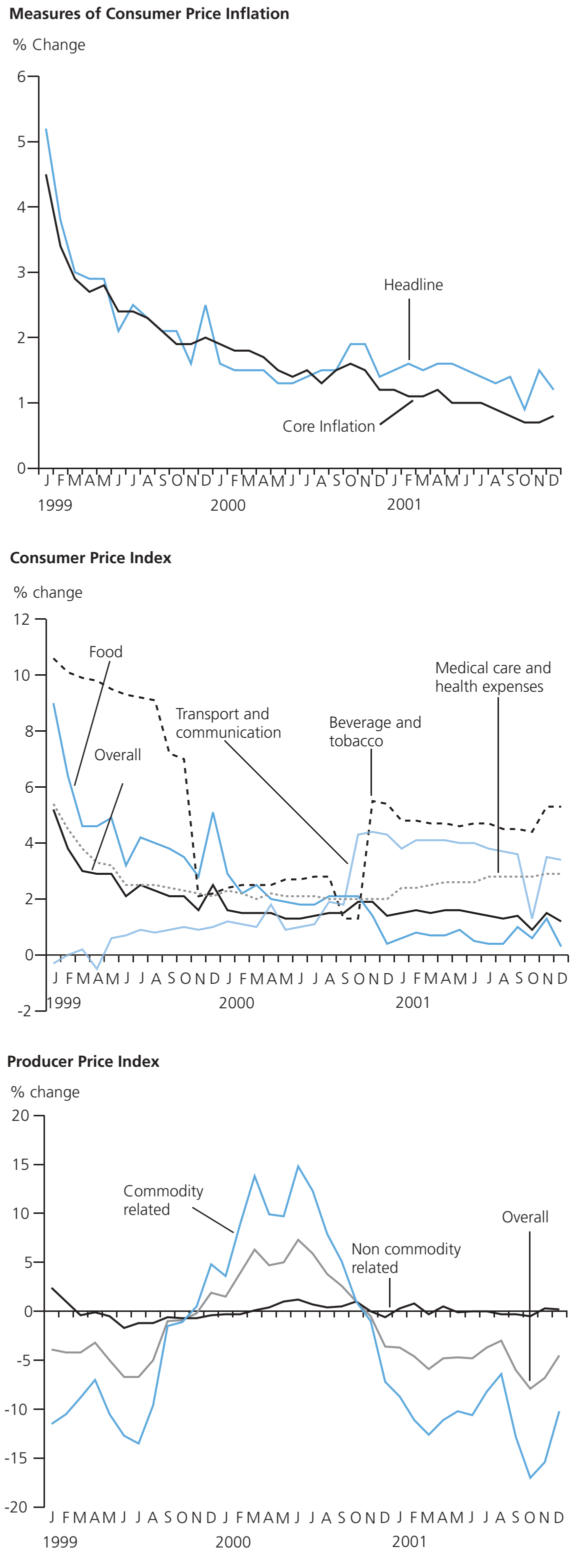
- Higher bus fares (10-30%) which were introduced in July-October 2000;
- Higher prices for several petroleum products (7.6-9.4%) from October 2000;
- Higher sales tax on alcoholic beverages (5%), and cigarettes and tobacco products (10%) as announced in the 2001 Budget, effective November 2000;
- Higher prices for several pharmaceutical products (10-20%), with effect from March 2001;
- Higher domestic airfares (51.8%) from August 2001; and
- A further price adjustment for petrol prices (8.3%) and higher import and excise duties on cigarettes and tobacco products (20%), which took effect in mid-October 2001, following the 2002 Budget presentation.

**Table 1.16**
**One-off Price Adjustments**

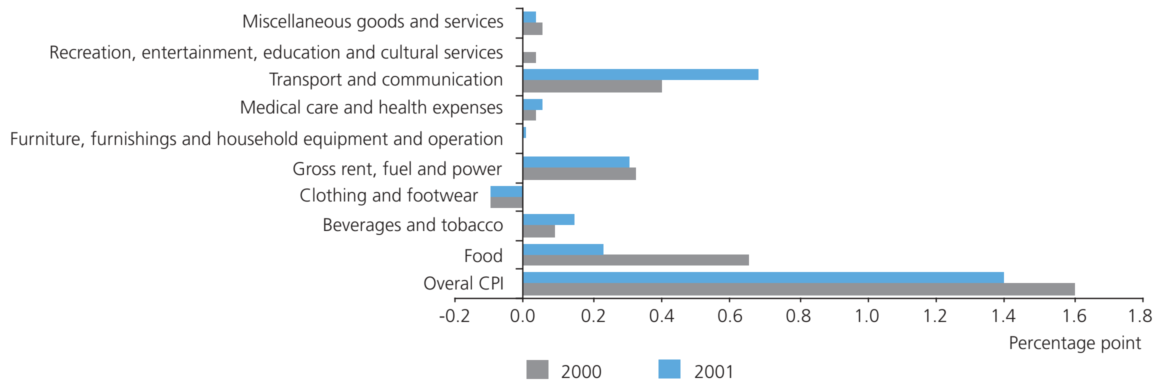
| Sub-groups | Weights (%) | Increase (%) | Contribution (%) |
|---|---|---|---|
| Beverages and tobacco | | | |
| Alcoholic beverages | 0.29 | 2.45 | 0.01 |
| Cigarettes and tobacco | 1.72 | 7.11 | 0.12 |
| Medical care and health expenses | | | |
| Medical and pharmaceutical products | 0.58 | 1.79 | 0.01 |
| Transport and communication | | | |
| Bus fares | 1.10 | 6.20 | 0.07 |
| MAS domestic airfares | 0.39 | 10.75 | 0.04 |
| Petroleum products | 4.96 | 7.82 | 0.39 |
| **Total** | **9.04** | | **0.64** |

These goods and services accounted for only 9% of the total CPI basket and the higher prices for these goods and services contributed about 0.64% to total CPI inflation in 2001. Meanwhile, price increases for other sub-groups also remained relatively stable,

**Graph 1.30**
**Inflation: Annual Rate of Change**



**Graph 1.31**
**Contribution to Annual Change in the Consumer Price Index**




except for clothing and footwear, where prices continued to decline during the year.

The upward price adjustment for the bus fares, domestic airfares, pharmaceutical products and petroleum products were allowed in order to reflect the underlying market conditions such as higher imported prices, production costs and commodity prices. In particular, crude petroleum prices had increased significantly since early 1999. It was necessary for retail prices for petroleum products to be adjusted as and when the underlying market conditions changed in order to gain long-run economic efficiency and competitiveness. The adjustment to retail prices of petroleum products during a period where inventories and excess capacity in several sectors prevailed had, to some extent, minimised the pass-through effects on prices for other consumer products, in particular, food prices.

## Producer Prices

Producer prices declined in 2001 amidst the generally weak commodity prices. The Producer Price Index (PPI) registered a decline of 5% in 2001 compared to an increase of 3.1% in 2000. The decline in producer prices reflected mainly lower prices charged by local producers. This was on account of lower prices for commodity-related products, namely inedible crude materials; mineral fuels, lubricants and related materials; and animal and vegetable oil and fats. Lower prices of these products were concomitant with the generally weak prices of crude palm oil, rubber as well as crude petroleum in 2001. Meanwhile, prices for goods paid by importers were relatively stable throughout the year amidst the stable ringgit exchange rate. Overall, excluding commodity-related products, non-commodity related producer prices were stable in 2001. This, in turn, contributed to stable consumer prices during the year.

**Table 1.17**
**Price Indicators**

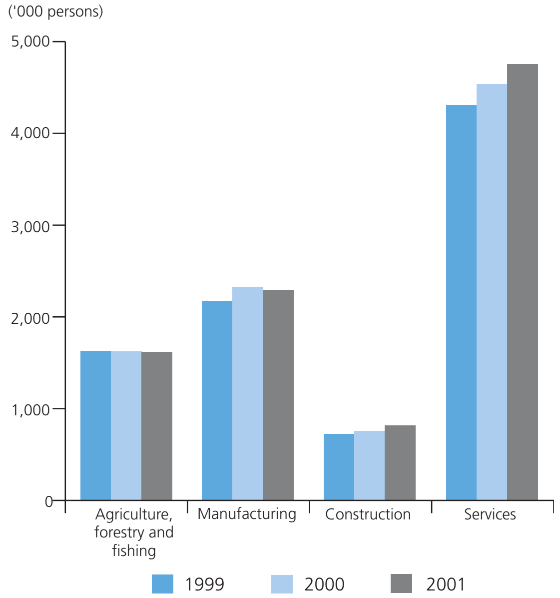
| | Weights | 2000 | 2001 |
|---|---|---|---|
| | | Annual change (%) | |
| **Consumer Price Index (2000=100)** | **100.0** | **1.6** | **1.4** |
| *of which:* | | | |
| Food | 33.8 | 1.9 | 0.7 |
| Beverages and tobacco | 3.1 | 2.8 | 4.8 |
| Clothing and footwear | 3.4 | -1.7 | -2.6 |
| Gross rent, fuel and power | 22.4 | 1.5 | 1.4 |
| Furniture, furnishings and household equipment and operation | 5.3 | 0.0 | 0.1 |
| Medical care and health expenses | 1.8 | 2.0 | 2.9 |
| Transport and communication | 18.8 | 2.1 | 3.6 |
| Recreation, entertainment, education and cultural services | 5.9 | 0.5 | -0.1 |
| Miscellaneous goods and services | 5.5 | 0.9 | 0.7 |
| **Consumer Price Index by Region** | | | |
| Peninsular Malaysia | 81.6 | 1.7 | 1.5 |
| Sabah | 8.9 | 0.6 | 0.6 |
| Sarawak | 9.5 | 1.5 | 0.8 |
| **Producer Price Index (1989=100)** | **100.0** | **3.1** | **-5.0** |
| *of which:* | | | |
| Local Production | 79.3 | 3.6 | -6.1 |
| Imports | 20.7 | 1.1 | -0.3 |
| **House Price Index (1990=100)** | | **4.7** | **0.9[1]** |
| *of which:* | | | |
| Klang Valley | | 12.4 | -0.4[1] |
| Johor Bahru | | 2.8 | -2.3[1] |
| Penang Island | | 8.3 | -3.7[1] |

[1] January-June
Source: Department of Statistics, Malaysia
NAPIC, Department of Valuation and Property Services

## Labour Market Developments

In 2001, the impact of the slowdown in economic activity was felt by the labour market, particularly in terms of retrenched workers in the manufacturing sector. However, given the flexibility accorded by the labour market, alternative measures that were adopted by employers such as pay cuts and temporary layoffs helped contain the number of workers retrenched. During the year, the slower growth environment resulted in both the total employment and labour force expanding at more moderate rates of 2.6% to 9.5 million workers and 3.2% to 9.9 million persons, respectively. Amidst low inflation and excess capacity, the slack labour market conditions contributed to some moderation in wage increases in 2001.

**Graph 1.32**
**Total Employment by Sector**




Source: Economic Planning Unit

Given the labour market conditions during the year, the unemployment rate edged upwards from 3.1% in 2000 to 3.7% in 2001, with the number of unemployed increasing by 63,500 to 364,800 persons. The unemployment rate, however, remained below the 4% deemed as full employment level.

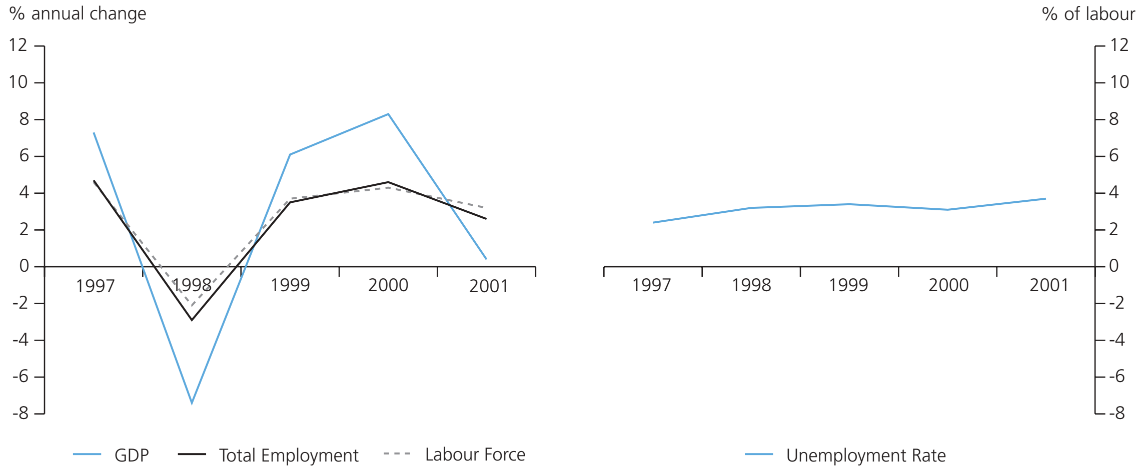
On a sectoral basis, the slower growth in **employment** in 2001 was due mainly to a pronounced decline in employment registered by the *manufacturing* sector, given declining demand for manufactured products, particularly for electronics and electrical products. As such, the manufacturing sector which accounted for a significant number of new jobs in 2000 (156,100) registered the largest contraction in employment (29,900). However, the decline in employment in the manufacturing sector was more than offset by the continued robust employment by the *services* sector which registered the majority of the total number of new workers employed (90.2% or 217,300 persons). Within the services sector, the new jobs created were concentrated mainly in the 'other services' sub-sector which include social services, private services, non-profit services of households and domestic services of households (41.5%) and the wholesale and retail trade, hotels and restaurants sub-sector (24.1%). The banking institutions' merger programme saw minimal disruption as employment in the banking sub-sector declined only marginally by 2% to 93,314 persons as at end-2001. Meanwhile, in the *construction* sector, 55,500 new jobs were generated, consonant with the increase in residential housing and public infrastructure projects.

**Table 1.18**
**Labour Market Indicators**

| | 1997 | 1998 | 1999 | 2000 | 2001 |
|---|---|---|---|---|---|
| Labour force ('000) | 9,039 | 8,849 | 9,178 | 9,573 | 9,877 |
| (annual change in %) | 4.6 | –2.1 | 3.7 | 4.3 | 3.2 |
| Employment (annual change in %) | 4.7 | –2.9 | 3.5 | 4.6 | 2.6 |
| Unemployment rate (% of labour force) | 2.4 | 3.2 | 3.4 | 3.1 | 3.7 |
| Labour productivity (GDP/Employment) | | | | | |
| (annual change in %) | 2.5 | –4.6 | 2.5 | 3.5 | –2.1 |
| Real wage per employee in manufacturing sector | | | | | |
| (annual change in %) | 6.0 | –2.4 | 3.0 | 5.0 | 1.5 |

Source: Economic Planning Unit
Department of Statistics, Malaysia
Bank Negara Malaysia

**Graph 1.33**
**Output and Employment**

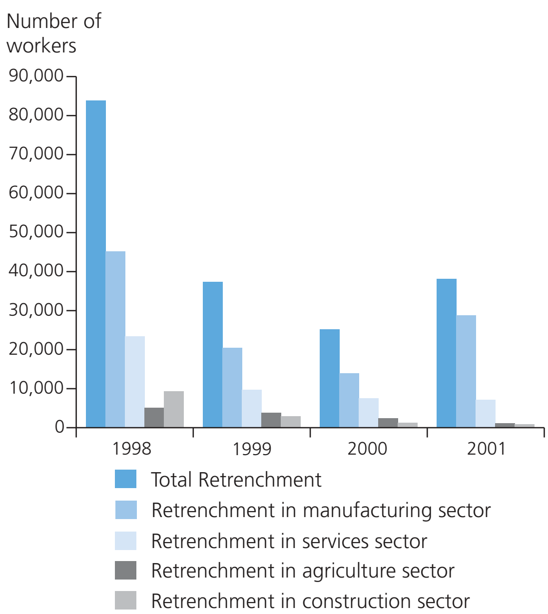



Source: Economic Planning Unit
Bank Negara Malaysia

In order to contain the contraction in earnings, employers reduced their workforce as part of the overall rationalisation process to lower production costs. The following provides an assessment of **retrenchment** in 2001:

- A total of 38,116 workers were retrenched (2000: 25,236), with 75.6% from the manufacturing sector. The electronics and electrical products sub-sector accounted for almost half (45.7%) of the total number of workers retrenched.

**Graph 1.34**
**Retrenchment by Sector**




Source: Ministry of Human Resources

- The number of employers involved in retrenchment increased by 55.2% to 1,380.

- Total retrenchment in 2001 accounted for 45.4% of the retrenchment recorded during the financial crisis in 1998.

- Almost half (48%) of the total number of workers retrenched was due to the decline in the demand for products.

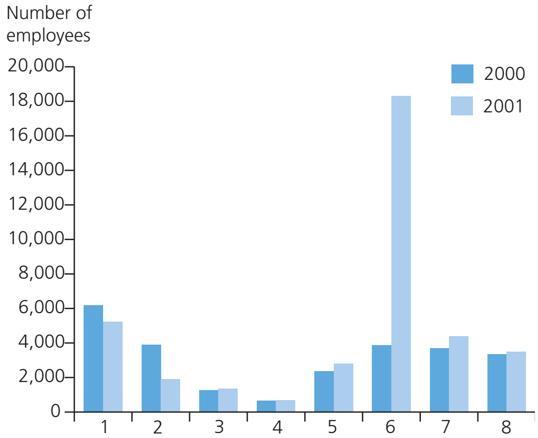
- By job category, production and related workers comprised the majority retrenched (63.6%). The retrenchment of professional, technical and related workers increased significantly by 54.8% in 2001 (2000: -36.2%), indicating that cost cutting measures affected both the high-end and low-end workers.

- Local workers accounted for the majority (86.9%) of the total number of retrenched workers.

- In terms of location, West Malaysia accounted for 96.9% of retrenched workers, with Penang, a major producer of electronics recording 23% of total retrenchment, followed by Johore (20.6%) and Selangor (15.5%).

- BNM's Company Survey findings indicated that the magnitude of layoffs during the year differed based on the type of company ownership. The majority of locally-owned companies that retrenched workers implemented layoffs across all job categories, hence, halting production completely. On the other hand, the majority of

**Graph 1.35**
**Reasons for Retrenchment**




1 Closure of companies
2 Sale of companies
3 Relocation to foreign countries
4 Relocation locally
5 High production cost
6 Reduction in demand for products
7 Company reorganisation and automation
8 Others

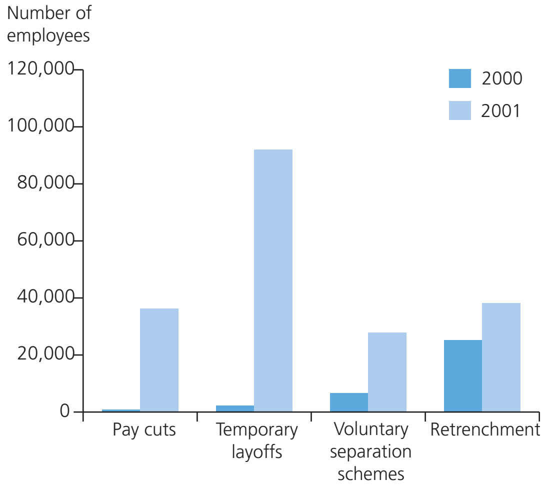
Source: Ministry of Human Resources

foreign-owned companies that retrenched, laid off only a proportion of their production and sales staff, thus, allowing production to continue, subject to shorter working hours. Also, layoffs were found to be higher for companies that export the bulk of their products to the US and Japan, compared to Europe.

- Retrenchment peaked in September 2001 with 5,828 workers laid off. In the fourth quarter of 2001, however, retrenchment declined by 40%, compared with the preceding quarter. The improvement in the labour market situation towards end-2001 indicated that the impact of the US economic slowdown on businesses in Malaysia had somewhat stabilised and that most companies were in the midst of business consolidation.

During the year, an increased number of employers (941; 2000: 144) took alternative measures, rather than retrenchment, to contain the impact of the slowdown on their workers. Hence, salaries of 36,294 workers were cut, while 91,915 workers were temporarily laid off. Also, 27,756 workers accepted the Voluntary Separation Scheme (VSS) during the year. In the banking sector, 4,240 employees had accepted the VSS as at end-December 2001.

**Graph 1.36**
**Retrenchment of Workers vs. Alternative Measures**




Source: Ministry of Human Resources

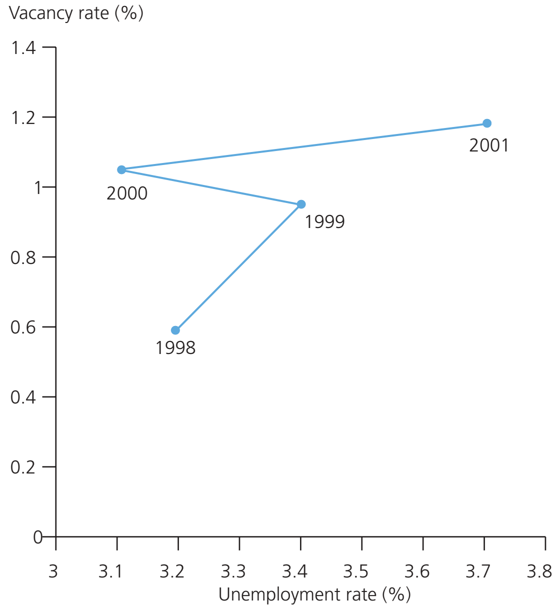
Excluding expatriate workers, the Government approved the recruitment of 258,578 new foreign workers (2000: 230,608), increasing the total number of registered foreign workers by 5% to 769,566. The foreign workers were employed mainly in the manufacturing, agriculture and domestic services sectors. In 2001, the majority (73.7%) originated from Indonesia.

**Labour demand** as measured by the number of job vacancies increased more moderately by 6.5% to 131,459 in 2001 (2000: 14%). The number of job vacancies could have been under-reported as it is not compulsory for firms to report vacancies to the Manpower Department of the Ministry of Human Resources. The vacancies were concentrated mainly in the manufacturing (46%), agriculture, forestry and fishing (27.6%) and services (15.7%) sectors. Sarawak continued to account for more than half of the job vacancies. Penang registered the largest contraction in vacancies (46.2%), compared with the preceding year.

The total number of active job seekers[1] registered with the Manpower Department increased by 22.9% to 34,200 as at end-2001 (end-2000: -12.6%). Compared with the previous year, the more moderate increase in demand for labour resulted in the widening of the ratio of vacancies to job seekers from 1:0.23 at end-2000 to 1:0.26 at end-2001. In

[1] Data is under-estimated as it is not compulsory for job seekers to register with the Manpower Department.

**Graph 1.37**
**Beveridge Curve for Malaysia (1998-2001)**




Source: Economic Planning Unit
Ministry of Human Resources
Department of Statistics, Malaysia

particular, the ratio for the professional and administrative related group widened from 1:1.40 to 1:2.15, whilst that of the clerical related group increased from 1:1.18 to 1:1.72. As at end-2001, the majority of the unemployed[2/] consisted of those with secondary school qualifications (65.7%). Whilst most job vacancies were for production operators (67%), a large part of the jobs sought was clerical related (45%). Although a significant portion of unemployment was cyclical during the year, an analysis using the Beveridge (Unemployment-Vacancy[3/]) Curve illustrates the mismatch between labour supply and demand in 2001, as shown by the upward and rightward shift in the curve from 2000 to 2001.

With the retrenchment of workers and the reduction in salaries experienced by selected sectors during the year, wage pressures generally eased:

- Data from the Monthly Survey of Manufacturing Industries conducted by the Department of Statistics indicated that on an annual basis, real wage per employee increased marginally by 1.5% in 2001 (2000: 4.9%), while labour productivity as measured by real sales value of products (SVP) per employee declined by 2.1% (2000: 16%). Labour productivity, as measured by the ratio of GDP to total employment also declined by the same magnitude. The poor productivity results in 2001 reflected the reduction in output due to the decline in external demand.

- The Malaysian Employers Federation's (MEF) Salary and Fringe Benefits Survey showed that the increase in the average private sector salary had stabilised at 6.9% in 2001 (2000: 7%). The average minimum salary offered to those with a basic degree increased marginally by 0.5% to RM1,671 in 2001. On a sectoral basis, the average salary increase in the non-manufacturing sector was higher (7.1%) than the manufacturing sector (6.7%).

The Government continued to closely monitor the employment situation and adopt pre-emptive measures to address emerging problems arising from the economic slowdown. Amongst others, job fairs were held nationwide to provide a platform for job seekers to obtain information on vacancies available from potential employers. The Electronic Labour Exchange Project which was launched on 19 September 2001 is expected to be operational online in 2002. The project is designed to match job seekers with vacancies beyond geographical boundaries, thus, improving the mobility of human resources. Of significance, the Government had, under the two fiscal stimulus packages announced in March and September 2001 as well as under the 2002 Budget, allocated funds towards the further development of human resources. In this regard, policy measures have been directed mainly at intensifying the application of information technology, upgrading skills of workers, strengthening learning and training programmes, developing various institutions of learning and improving education facilities.

A new wage agreement between the Malayan Agricultural Producers Association (MAPA) and the National Union of Plantation Workers (NUPW) resulted in a guaranteed minimum monthly wage of RM325 to be paid, with effect from 1 January 2001, to oil palm harvesters and oil mill workers.

As a measure to expedite Malaysia's transition to the knowledge-based economy, a programme to encourage Malaysian citizens with special expertise

[2] No. of unemployed at the end of the last quarter does not equal the total no. for the year as nos. for all end-quarters in a year are smoothened out to obtain the yearly no.

[3] Unemployment rate used pertain to the data from the Economic Planning Unit. Vacancy rate= (no. of job offers- no. of placements) / (no. of job offers- no. of placements + no. of employees).

who are employed overseas, to return to Malaysia came into effect on 1 January 2001. On 1 July 2001, amendments to the list of expertise, in terms of the field of expertise, eligibility and years of experience took effect. The revision was done to ensure that the quality of expertise approved under the programme commensurates with the requirements of the country for the identified fields of expertise.

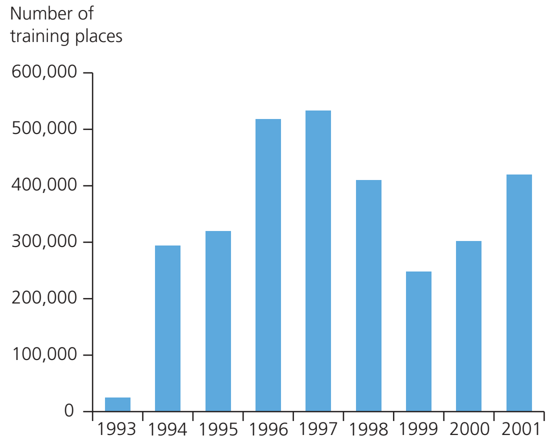
In the financial industry, a 'Staff Re-Skilling Project' or 'StaRs Project' was launched on 23 March 2001 with the objective of enhancing the mobility of staff, particularly those who accepted the VSS. The project, administered by the Institute of Bankers Malaysia and funded by the financial institutions' contributions towards the Staff Training Fund, incorporates a series of training programmes on competencies catering to the needs of a more knowledge-based economy, and a support infrastructure system to assist separating staff to seek new employment. In 2001, a total of 64 programmes was conducted, benefiting about 1,300 trainees.

In order to upgrade the skills of unemployed graduates and school leavers as well as retrenched workers, the RM4.3 billion stimulus package which was introduced in September 2001, included an allocation of RM300 million for the establishment of the Special Scheme that consists of programmes on training in IT, mathematics and languages; commercial agriculture entrepreneurship; further studies; and attachments with government agencies, public universities, private professional firms and small- and medium-scale enterprises.

Since its inception in 1993, the Human Resource Development Council (HRDC) which administers the Human Resource Development Fund (HRDF) for the retraining and skills upgrading of workers has approved a total of 3.1 million training places, involving a total expenditure of RM1 billion. In enhancing the efficiency of services provided, the HRDC which was officially corporatised on 16 May 2001 has been renamed 'Pembangunan Sumber Manusia Berhad (PSMB)'. As at end-December 2001, the number of employers registered with the PSMB increased to 7,690, with the majority (71.6%) from the manufacturing sector and the remainder from the services sector.

Given lower corporate earnings during the year, on 1 November 2001, the levy imposed by the PSMB was reduced by half from 1% of the companies' monthly wage bills to 0.5%. During the year, the HRDF levy

**Graph 1.38**
**Number of Training Places Approved by PSMB**




Source: Pembangunan Sumber Manusia Berhad

collection increased further to RM209.1 million from RM188.3 million in 2000. Effective for a year from 1 November 2001, the financial assistance provided to employers was raised from 85% to 100% of the cost of selected training programmes conducted by local trainers, including training on supervision, strategic management, financial management, human resource management and safety and health of workers.

In 2001, a total of 420,057 training places was approved by the PSMB with financial support of RM189.8 million. The PSMB was also appointed as one of the coordinating agencies for two of the nine programmes under the Special Scheme that was set up for retrenched workers and unemployed graduates. These were the 'Training Scheme for Retrenched Workers II' and 'Graduate Training Schemes', which benefited a total of 5,519 trainees with an accumulated financial assistance of RM36.1 million.

A Skills Development Fund (SDF) established by the Ministry of Human Resources with an allocation of RM140 million became operational on 2 January 2001. The Fund aimed to provide soft loans for technical and vocational training offered by institutions that are accredited by the National Vocational Training Council. In 2001, about 20,000 applications were approved and RM24.2 million was disbursed.

Overall, the adjustments observed in the domestic labour market during the year indicated that all parties concerned, including the Government, employers and workers had demonstrated flexibility in a more difficult economic environment. Going forward, productivity improvements will continue to dominate the agenda on transforming the economy to one that is more knowledge-based. In this regard, efforts will include the need to address skill mismatches and the further enhancement of labour mobility.

## EXTERNAL SECTOR

### Balance of Payments

The overall balance of payments turned around to a surplus position in 2001. The improvement was due to lower outflows in the financial account. The current account surplus narrowed in 2001, but nevertheless the surplus remained large at RM27.4 billion or equivalent to 8.9% of GNP. This reflected a moderate decline in the trade account and improvement in the income and services accounts.

The impact of the global slowdown on exports has been significant as exports of both manufactured goods and commodities declined during the year. At the same time, demand for imports of intermediate inputs used in the production of exports also declined. This contained the decline in the trade surplus. Given the lower export earnings during the year, repatriation of profits and dividends was also lower in 2001, resulting in an improvement in the income account. The services deficit also declined, reflecting not only lower payments related to export activities but also the marked improvement in the travel account surplus.

The improvement in the financial account in 2001 emanated mainly from lower short-term outflows in most major components of the short-term capital account. Net long-term inflows moderated. On balance, inflows were mainly longer-term capital (foreign direct investments and external loans).

Portfolio investors were already underweight in the Malaysian market and hence outflows moderated. Gross inflows of portfolio investment, which was moderate in the first half-year, picked up in the third quarter as market sentiment turned more positive

**Table 1.19**
**Balance of Payments**

| Item | 2001e + | 2001e - | 2001e Net |
|---|---|---|---|
| | RM million | | |
| Goods | 334,326 | 264,472 | 69,854 |
| *Trade account* | *334,420* | *280,692* | *53,728* |
| Services | 54,929 | 63,295 | -8,366 |
| **Balance on goods and services** | 389,255 | 327,767 | 61,488 |
| Income | 6,678 | 32,626 | -25,948 |
| Current transfers | 2,059 | 10,192 | -8,133 |
| **Balance on current account** | 397,992 | 370,585 | 27,407 |
| **% of GNP** | | | 8.9 |
| Capital account | | | – |
| Financial account | | | -14,841 |
| Direct investment | | | 1,017 |
| Portfolio investment | | | -2,489 |
| Other investment | | | -13,369 |
| **Balance on capital and financial account** | | | -14,841 |
| Errors and omissions | | | -8,904 |
| *of which:* | | | |
| *Exchange revaluation loss* | | | -4,061 |
| **Overall balance** | | | 3,662 |
| **Bank Negara Malaysia international reserves, net** | | | 117,203 |
| **(US$ million)** | | | 30,843 |

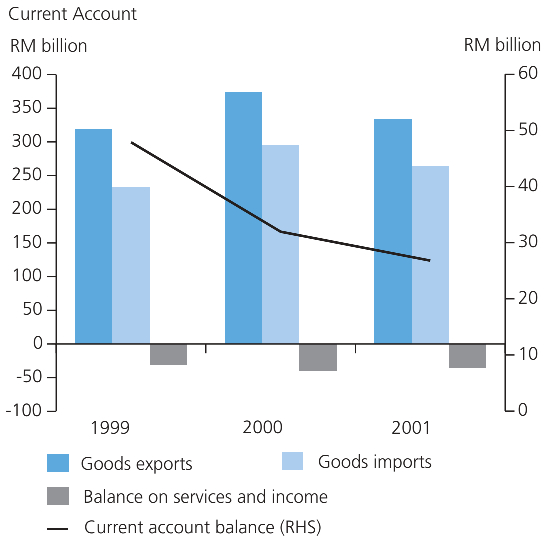
e Estimate

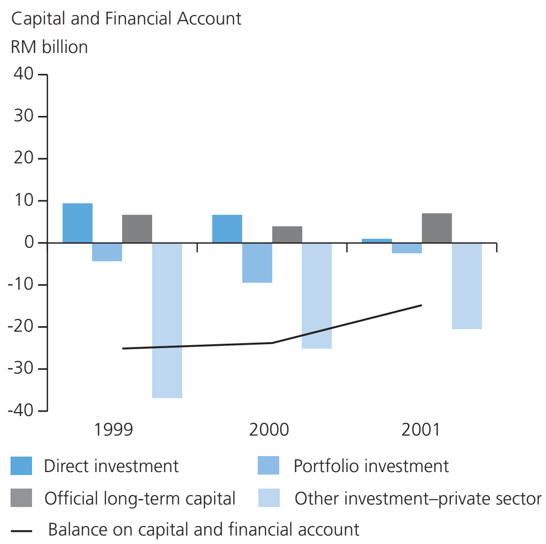
Source: Bank Negara Malaysia and Department of Statistics, Malaysia

following the accelerated pace of corporate restructuring which strengthened the longer-term outlook for Malaysia. This trend reversed following September 11, with profit-taking activities in the final quarter of 2001. During the year, there was also less incentive for the placement or retention of funds abroad as interest rate differentials shifted in Malaysia's favour since September 2001. This was reflected in the lower trade credits extended to foreign importers and the decline in the net external assets of the banking institutions in the second half of the year following the unwinding of foreign currency inter-bank placements as importers undertook reduced hedging activities.

The external position has remained robust. Large current account surplus and lower short-term outflows led to surplus in the overall balance of payments. Reserves has been on a rising trend.

**Graph 1.39**
**Malaysia: Balance Of Payments**





Long-term capital inflows reflected mainly drawdown of long-term external loans by the Federal Government to maintain regular market presence, to establish a benchmark rate for Malaysian corporations and to take advantage of lower interest rate abroad. A significant portion of borrowings by NFPEs was to refinance the more expensive existing offshore loans.

While Malaysia continued to receive inflows of foreign direct investment (FDI) in 2001, FDI for expansion and new investments were lower because of excess capacity, amidst the slowdown in the global economy. The FDI inflows were mainly new equity funds for strategic business alliances in the telecommunications and financial services sector and to a lesser extent in the manufacturing sector. For the year as a whole, the net inflow of FDI was small, mainly due to one large transaction in the private sector involving the acquisition of controlling interests by a Malaysian company from non-resident partners as part of its corporate restructuring exercise. The purchase was financed by the issuance of long-term debt securities to the non-resident investors and an offshore loan. As the outflows were to finance a change in ownership, it had no impact on reserves or total investment activities in Malaysia. Direct investment abroad remained high in the first quarter of 2001 but subsequently declined as companies adopted a cautious approach in their investment plans abroad following the global economic slowdown. Overall, the financial account recorded a substantially lower outflow of RM14.8 billion in 2001.

Errors and omissions amounted to –RM8.9 billion. Of this total, an unrealised exchange loss from revaluation of reserves due to the appreciation of ringgit against selected major currencies amounted to RM4.1 billion. Excluding this book loss, the errors and omissions of RM4.8 billion reflects the normal errors and inconsistencies that occur in the course of compilation of the balance of payments statistics. This represented less than one percent of Malaysia's total trade, well within the accepted norm of 5% of total trade. After adjusting for the errors and omissions, the overall balance of payments recorded a surplus position of RM3.7 billion or US$964 million. Consequently, the net international reserves of Bank Negara Malaysia stood at RM117.2 billion or US$30.8 billion at end-2001 and increased further to RM119.6 billion or US$31.5 billion as at 28 February 2002. This level of reserves represented 5.2 months of retained imports and was 5.1 times larger than the short-term external debt. Including the scheduled amortisation of medium- and long-term debts falling

### Compilation of the Balance of Payments based on BPM 5

Since the first quarter of 2001, Malaysia's balance of payments is compiled in conformity with the guidelines set forth in the Fifth Edition of the Balance of Payments Manual (BPM 5) of the International Monetary Fund. The major changes are summarised below:

| Previous format | BPM 5 format |
|---|---|
| **Merchandise** | **Goods** |
| **Services**<br>• Freight & insurance<br>• Other transportation<br>• Travel and education<br>• Investment income<br>• Other services<br>• Government transactions, nie | **Services**<br>• Transportation<br>• Travel<br>• Other services<br>• Government transactions, nie |
| **Balance on goods and services** | **Balance on goods and services** |
| Transfers | **Income**<br>• Compensation of employees<br>• Investment income<br><br>**Current transfers** |
| **Balance on current account** | **Balance on current account** |
| **Long-term capital account**<br>• Official sector<br>Federal Government<br>NFPEs<br>Other<br>• Private sector | **Capital account**<br>• Capital transfers<br>• Acquisition/disposal of non-produced, non-financial assets<br><br>**Financial account**<br>• Direct investment<br>• Portfolio investment<br>• Other investment<br>- Official sector<br>- Private sector |
| | **Balance on capital and financial account** |
| **Basic balance** | |
| **Private short-term capital**<br><br>**Errors and omissions** | **Errors and omissions** |
| **Overall balance** | **Overall balance** |

In terms of the **current account**, the major change is the redesignation of investment income (previously a component of the services account) as a new account named the Income account.

Under BPM 5, the former capital account has been expanded and redesignated as the **capital and financial accounts**

- The capital account consists of two categories, i.e. capital transfers and acquisition/disposal of non-produced, non-financial assets.
- The financial account is classified according to type of investment or by functional breakdown i.e. direct investment, portfolio investment and other investment. Under the previous compilation, the capital account was classified according to original contractual maturity of more than one year (long-term) or one year or less (short-term).

The balance of payments data for 1999 and 2000 have been reclassified in accordance with the BPM 5 format.

due in the next 12 months, the reserves level is more than three times the short-term debt. Malaysia's reserves are usable and unencumbered.

The impact on Malaysia of the downturn in the electronics cycle and the slowdown in the global economy was transmitted through the export channel. Growth in gross exports, which had remained positive since 1987, declined by 10.4% in 2001. Exports contracted in all sectors, manufacturing as well as primary commodities. Nevertheless, given the existing structure of high import content in exports, imports also declined by 9.9%. The **trade surplus**, therefore narrowed, but remained large at RM53.7 billion (US$14.1billion). Adjusted for

**Table 1.20**
**External Trade**

| | 2000 | 2001 | 2000 | 2001 |
|---|---|---|---|---|
| | RM billion | | US$ billion | |
| **Gross exports (f.o.b)** | **373.3** | **334.4** | **98.2** | **88.0** |
| Annual change (%) | 16.1 | -10.4 | 16.1 | -10.4 |
| | Annual change (%) | | | |
| Volume[1] | 11.6 | -3.3 | 11.6 | -3.3 |
| Prices [1] | 6.2 | -7.7 | 6.2 | -7.7 |
| **Gross imports (c.i.f)** | **311.5** | **280.7** | **82.0** | **73.9** |
| Annual change (%) | 25.3 | -9.9 | 25.3 | -9.9 |
| | Annual change (%) | | | |
| Volume[1] | 15.5 | -3.0 | 15.5 | -3.0 |
| Prices [1] | 8.5 | -7.1 | 8.5 | -7.1 |
| **Trade balance** | **61.8** | **53.7** | **16.2** | **14.1** |

[1] Volume and prices are estimates.

Source : Department of Statistics, Malaysia and Bank Negara Malaysia

valuation and coverage on the balance of payments basis, the goods account recorded a large surplus of RM69.9 billion (US$18.4 billion). The contraction in both exports and imports started in March 2001, reached its peak in September and moderated in the fourth quarter. More moderate declines in exports and sharper improvement in imports supported other indicators that, by the end of 2001, the economy was in the early stages of recovery.

**Exports of manufactured goods**, which accounted for 85.3% of total exports of Malaysia, declined by 10.3% in 2001. The decline was most pronounced in the electronics sector (-16.3%). Exports of electrical goods were more resilient in the first half-year, and only contracted in the second half-year. For the manufacturing sector as a whole, the decline in prices (-6.1%) was more pronounced than the decline in volume (-4.1%) as firms reduced prices aggressively to retain market share in an environment of weak demand and excess stocks. Reflecting signs of more positive developments in the external environment towards year-end, the rate of decline in earnings from manufactured exports moderated significantly to 12.4% during the fourth quarter from the 20.4% contraction in the third quarter. On a preceding quarter basis, manufactured exports recorded an increase of 2% in the fourth quarter, the first quarterly increase in more than a year.

While manufacturers and exporters were continuing to move up the value chain and improve product quality to enhance their international competitiveness, efforts were also undertaken to explore export market opportunities. In 2001, the Malaysian External Trade Development Corporation (MATRADE) had successfully organised the participation of Malaysian

Graph 1.40
**Export Performance of the Manufacturing Sector**


Graph 1.41
**Export Performance of Electronics and Non-electronics Industries**

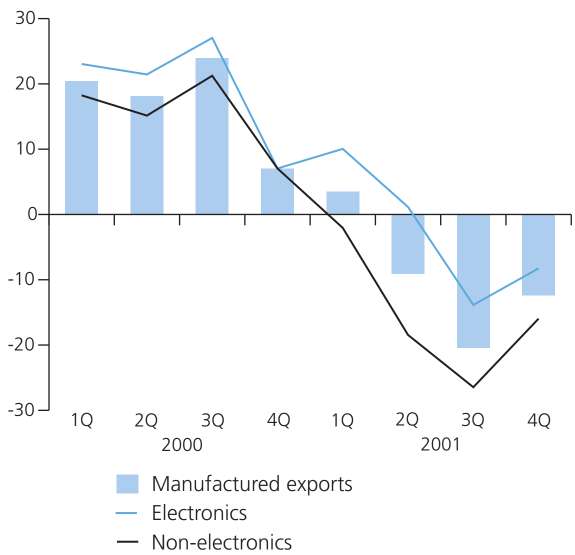



**Table: 1.21**
**Gross Exports**

| | 2001*p* | | |
|---|---|---|---|
| | RM million | Annual change (%) | % share |
| **Manufactured goods** | **285,316** | **-10.3** | **85.3** |
| *of which:* | | | |
| Electronics, electrical machinery and appliances | 200,307 | -13.1 | 59.9 |
| Electronics | 139,632 | -16.3 | 41.8 |
| *Semiconductor* | *60,530* | *-14.9* | *18.1* |
| *Electronic equipment and parts* | *79,102* | *-17.3* | *23.7* |
| Electrical machinery and appliances | 60,675 | -4.7 | 18.1 |
| *Consumer electrical products* | *23,591* | *-10.9* | *7.1* |
| *Industrial and commercial electrical products* | *23,518* | *-0.6* | *7.0* |
| *Electrical industrial machinery and equipment* | *12,462* | *-1.0* | *3.7* |
| *Household electrical appliances* | *1,104* | *22.3* | *0.3* |
| Textiles, clothing and footwear | 9,054 | -13.2 | 2.7 |
| Chemicals and chemical products | 14,879 | -0.9 | 4.4 |
| Wood products | 6,017 | -11.5 | 1.8 |
| Manufactures of metal | 8,692 | 0.9 | 2.6 |
| Transport equipment | 2,427 | -16.4 | 0.7 |
| Rubber products | 4,466 | -4.9 | 1.3 |
| Optical and scientific equipment | 7,802 | 14.3 | 2.3 |
| **Agricultural commodities** | **19,966** | **-13.2** | **6.0** |
| *of which:* | | | |
| *Palm oil* | *9,876* | *-0.7* | *3.0* |
| *Sawn timber* | *2,273* | *-24.7* | *0.7* |
| *Rubber* | *1,886* | *-26.6* | *0.6* |
| *Saw logs* | *1,523* | *-38.8* | *0.5* |
| **Minerals** | **23,445** | **-12.6** | **7.0** |
| *of which:* | | | |
| *Crude oil* | *11,118* | *-21.9* | *3.3* |
| *LNG* | *11,342* | *-0.7* | *3.4* |
| *Tin* | *461* | *6.0* | *0.1* |
| **Other exports** | **5,693** | **2.8** | **1.7** |
| **Total** | **334,420** | **-10.4** | **100.0** |

*p* Preliminary

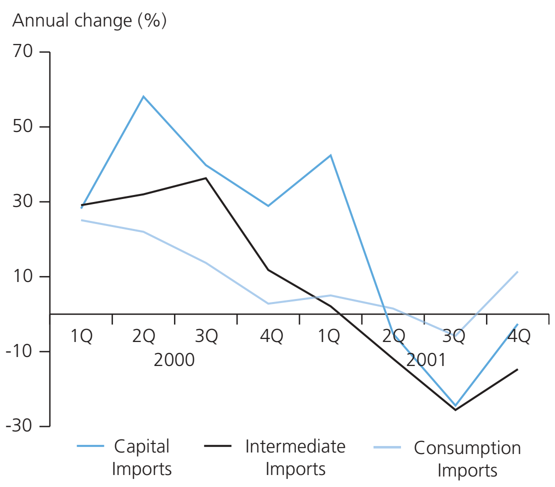
Source : Department of Statistics, Malaysia exporters in 26 international trade fairs in the traditional markets such as the United States, the United Kingdom and Germany, the Asia Pacific destinations such as Australia, Hong Kong, India, Indonesia, Thailand, the Philippines and Brunei and the newer markets of the Middle Eastern countries, South African countries and Vietnam. Reflecting the Government's commitment in promoting Malaysian products in new markets, MATRADE had organised a trade fair in Madagascar. Meanwhile, under the ASEAN Promotion Centre Technical Assistance Programme, Malaysian exporters took part in another six international trade fairs held in Japan.

In the **primary commodity** sector, export earnings declined by 12.9% to RM43.4 billion following lower exports of all major commodities, except cocoa. Export volume for palm oil expanded as demand from major buyers, namely, India, The People's Republic of China, Pakistan and the European Union increased during the year. However, export earnings for palm oil declined as an oversupply in the global vegetable oils market led to a decline in export prices.

Export earnings from **minerals** declined due to both lower export prices and volume. In particular, crude oil exports declined, reflecting mainly weaker oil prices, given that the price per barrel fell by US$4 to US$25.53 in line with the global trend, as well as lower export volume. Exports of LNG also declined in 2001 as prices fell in tandem with lower oil prices, while export volume increased marginally.

The decline in **gross imports** was reflected in both lower import volume and prices. Imports of **intermediate goods** which account for 72% of total

**Graph 1.42**
**Imports**




imports declined by 13.3%. The primary source of the decline was the decline in imports of electronic component parts (comprising 65% of imports of parts and accessories of capital goods and 27% of total imports) and industrial supplies which are primarily used as component parts in the production of manufactured exports. The electronics industry experienced a large contraction in output and exports orders in 2001. Most electronics manufacturers drew down on inventories accumulated from the strong capacity expansion in 2000.

A notable development was the continued increase in intermediate imports that were related to the manufacture of goods for the domestic market, supported by the positive effects of the fiscal stimulus programme and low interest rates. Imports of primary and processed materials used by the food and beverages industry increased, reflecting sustained consumer spending on food and beverage items. Imports of parts and accessories of transport equipment also increased significantly by 31.3%, in line with the strong performance of the motor assembly industry and passenger car sales. This contributed to increased domestic demand for fuel and lubricants but the value of these imports declined due to lower crude oil prices.

The postponement of private investment plans following the slowdown in economic growth and excess capacity in the domestic economy led to a 1.1% decline in imports of **capital goods**. While investment in the manufacturing sector moderated, capacity expansion in the services sector mitigated the decline in imports of capital goods. Big value capital imports used mainly in the manufacturing sector which declined included industrial machinery and equipment and generators, electrical motors and turbines for power generation. On the other hand, reflecting the upgrading and modernisation of businesses and the continued strength of the services sector, imports of office equipment increased strongly. Imports of telecommunication equipment also increased substantially, underpinned by ongoing efforts to upgrade and modernise the telecommunications system. With firms producing transport equipment operating at 95% capacity, imports of transport equipment for industrial purposes also increased substantially. Among these were imports of commercial vehicles and buses, as well as railway locomotives and coaches, following completion of the construction of the Express Rail Link connecting KLIA and Kuala Lumpur Sentral.

**Table 1.22**
**Gross Imports by End Use**

| | 2001*p* | | |
|---|---|---|---|
| | RM million | Annual change (%) | % share |
| **Capital goods** | **43,675** | **–1.1** | **15.6** |
| Capital goods (except transport equipment) | 41,000 | –2.1 | 14.6 |
| *Industrial machinery and equipment* | *12,253* | *–19.1* | *4.4* |
| *Office equipment* | *6,567* | *75.1* | *2.3* |
| *Telecommunication equipment* | *4,602* | *33.9* | *1.6* |
| Transport equipment | 2,675 | 17.7 | 1.0 |
| **Intermediate goods** | **201,753** | **–13.3** | **71.9** |
| Food and beverages, mainly for industry | 4,179 | 8.9 | 1.5 |
| Industrial supplies, n.e.s. | 63,105 | –6.5 | 22.5 |
| *Metals and metal products* | *17,083* | *–6.5* | *6.1* |
| *Chemicals* | *7,043* | *–9.9* | *2.5* |
| Fuels and lubricants | 11,659 | –3.6 | 4.2 |
| Parts and accessories of capital goods (except transport equipment) | 117,391 | –18.6 | 41.8 |
| *Electronics* | *76,341* | *–19.1* | *27.2* |
| *Parts and accessories of telecommunication equipment* | *7,239* | *–19.7* | *2.6* |
| Parts and accessories of transport equipment | 5,418 | 31.3 | 1.9 |
| **Consumption goods** | **17,555** | **3.0** | **6.3** |
| Food and beverages, mainly for household consumption | 7,174 | 11.1 | 2.6 |
| Transport equipment, non-industrial | 121 | 25.4 | 0.0 |
| Consumer goods, n.e.s. | 10,259 | –2.1 | 3.7 |
| *Consumer durables* | *2,225* | *10.0* | *0.8* |
| *Consumer semi-durables* | *3,604* | *–17.5* | *1.3* |
| *Consumer non-durables* | *4,431* | *8.2* | *1.6* |
| **Dual use goods** | **5,843** | **–8.6** | **2.1** |
| Motor spirit | 2,462 | –0.3 | 0.9 |
| Passenger motor cars | 3,381 | –13.8 | 1.2 |
| **Others** | **5,074** | **9.1** | **1.8** |
| **Re-exports** | **6,791** | **4.2** | **2.4** |
| **Gross Imports** | **280,691** | **–9.9** | **100.0** |

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

Source: Department of Statistics, Malaysia

In tandem with sustained private consumer spending, imports of **consumption goods** increased further by 3% in 2001. The growth in consumption imports was due mainly to higher imports of food and beverages, namely milk and dairy products, fish, beverages, meat and vegetables. Imports of durable and non-durable consumer goods were also higher during the year. Imports of consumption goods accounted for a small share of 6.3% of total imports.

During the year, the relative importance of Malaysia's major **trade partners**, namely the United States, Japan, Singapore and the European Union remained generally unchanged. These countries accounted for 62.6% of Malaysia's total trade. The **United States** continued to be Malaysia's largest trade partner with a share of 18.3% of total trade. Imports from the US declined by 13.3% while US demand for Malaysian goods also declined by 11.6% in tandem with slow growth in the US economy. The bilateral surplus in Malaysia's favour, although still large, declined further to RM22.8 billion.

**Japan** maintained its position as the second largest trade partner with a slightly lower share of 16% of total trade. Japan remained Malaysia's most important source of imports, although its market share declined to 19.2% of total imports. This partly reflected the cheaper cost of imports from Japan due to the valuation impact from a weaker yen. Imports from Japan comprised mainly machinery, electronics and electrical components and parts and accessories of transport equipment. Exports to Japan also declined by 8.7%, reflecting to some extent lower

**Table 1.23**
**Direction of External Trade**

| | 2001*p* | | | | |
|---|---|---|---|---|---|
| | Exports | | Imports | | Trade balance |
| | RM million | % share | RM million | % share | RM million |
| Selected South-East-Asian countries | 83,107 | 24.9 | 63,168 | 22.5 | 19,939 |
| Singapore | 56,669 | 16.9 | 35,313 | 12.6 | 21,356 |
| Thailand | 12,768 | 3.8 | 11,121 | 4.0 | 1,647 |
| Indonesia | 5,940 | 1.8 | 8,517 | 3.0 | -2,577 |
| Philippines | 4,893 | 1.5 | 6,989 | 2.5 | -2,097 |
| Other ASEAN countries | 2,838 | 0.9 | 1,228 | 0.4 | 1,610 |
| European Union | 45,462 | 13.6 | 36,075 | 12.9 | 9,387 |
| United Kingdom | 8,779 | 2.6 | 6,872 | 2.4 | 1,907 |
| Germany | 7,767 | 2.3 | 10,415 | 3.7 | -2,648 |
| Netherlands | 15,429 | 4.6 | 2,466 | 0.9 | 12,964 |
| Other EU countries | 13,487 | 4.1 | 16,322 | 5.9 | -2,836 |
| United States | 67,672 | 20.2 | 44,841 | 16.0 | 22,832 |
| Japan | 44,503 | 13.3 | 54,002 | 19.2 | -9,499 |
| People's Republic of China | 14,520 | 4.3 | 14,457 | 5.2 | 63 |
| Hong Kong SAR | 15,299 | 4.6 | 7,191 | 2.6 | 8,108 |
| Taiwan | 12,117 | 3.6 | 15,932 | 5.7 | -3,815 |
| South Korea | 11,157 | 3.3 | 11,240 | 4.0 | -83 |
| India | 5,993 | 1.8 | 2,935 | 1.0 | 3,058 |
| Australia | 7,798 | 2.3 | 5,944 | 2.1 | 1,854 |
| Rest of the world | 26,792 | 8.1 | 24,906 | 8.8 | 1,885 |
| **Total** | **334,420** | **100.0** | **280,691** | **100.0** | **53,729** |

*p* Preliminary

Source: Department of Statistics, Malaysia

export receipts from mineral fuels due to lower crude oil prices as well as weaker demand due to the recession in Japan. Consequently, the traditional trade deficit with Japan narrowed by nearly one - half to RM9.5 billion.

**Singapore** remained Malaysia's third major trade partner, accounting for a lower share of 15% of total trade. Reduced intra regional trade and the increasing importance of Malaysian ports as regional transhipment hubs contributed towards a lower share of exports bound for Singapore. As a result, the trade surplus with Singapore narrowed to RM21.4 billion. Meanwhile, trade with the **European Union** increased to 13.3% of total trade. The trade surplus in Malaysia's favour was substantially reduced to RM9.4 billion as exports to EU declined but the value of imports sourced from EU (mainly Germany) increased in 2001.

Reflecting the slowdown in economic growth in the regional countries, the trade pattern with the **East Asian** countries (except China) displayed a declining trend. Bilateral trade with several Asean countries, except Brunei Darussalam, declined in 2001. Reflecting the substitution of imports from lower cost suppliers, Malaysia continued to experience bilateral trade deficits with the Philippines and Indonesia. Similarly, bilateral trade with several developed Asian countries were also lower during the year, due to significant declines in both exports and imports.

A notable development was the significant increase in trade with the **People's Republic of China**, which has become Malaysia's fourth largest single trading partner with an increased share of 4.7% of total trade. While exports to the major industrial countries, other major destinations in the Far East region (Hong Kong, Taiwan and South Korea) and ASEAN declined in 2001, exports to China increased strongly by 26.2%, reflecting China's sustained strong economic growth.

For the fourth consecutive year, the sustained large surplus in the goods account generated sufficient foreign exchange earnings to finance the deficits in the services, income and current transfers accounts. In 2001, the net outflow in the **current transfers** account increased to RM8.1 billion. The increase reflected higher remittances by foreign workers, including one-time repatriations as some workers

**Table 1.24**
**Services and Income Account**

| Subsector | 2000 | 2001e | | |
|---|---|---|---|---|
| | RM billion | | | |
| | Net | + | - | Net |
| **Services Account** | | | | |
| Transportation | -11.4 | 10.4 | 21.8 | -11.4 |
| Travel | 10.0 | 26.1 | 9.9 | 16.1 |
| Other Services | -9.9 | 17.9 | 31.1 | -13.2 |
| Government services n.i.e. | 0.1 | 0.5 | 0.5 | ... |
| **RM billion** | **-11.2** | **54.9** | **63.3** | **-8.4** |
| **US$ billion** | **-3.0** | **14.5** | **16.7** | **-2.2** |
| % of GNP | -3.6 | | | -2.7 |
| **Income Account** | | | | |
| Compensation of employees | -0.6 | 1.4 | 2.4 | -1.0 |
| Investment income | -27.9 | 5.3 | 30.2 | -24.9 |
| **RM billion** | **-28.6** | **6.7** | **32.6** | **-25.9** |
| **US$ billion** | **-7.5** | **1.8** | **8.6** | **-6.8** |
| % of GNP | -9.1 | | | -8.5 |

*e* Estimate

Source : Department of Statistics, Malaysia and Bank Negara Malaysia

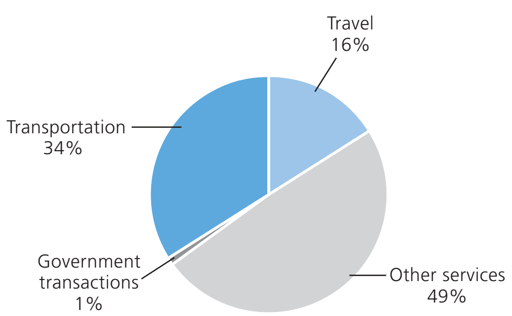
returned to their home countries following consolidation of activities in the export-oriented manufacturing industries. There was a total of 769,566 registered foreign workers in the country in 2001.

The **services account** deficit narrowed significantly by 25.4% to RM8.4 billion or 2.7% of GNP. The improvement reflected the exceptionally strong increase in the travel account surplus and lower payments related to export and import activities.

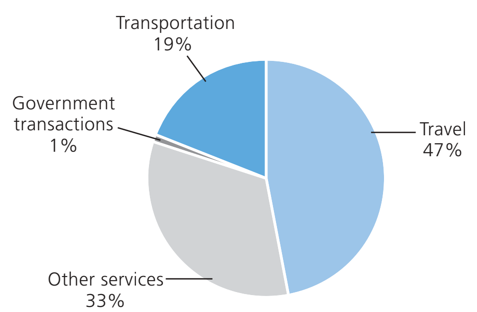
The net surplus in the **travel account** increased by 62% to RM16.1 billion. The exceptionally strong performance of the travel account reflected the marked increase in tourist arrivals (25% to 12.8 million visitors) and excursionists (46.2% to 10.2 million day trippers). Benefiting from the record number of foreign visitors and higher per capita spending (11.8% to RM1,896), tourist (including excursionist) receipts increased to an unprecedented level of RM25.8 billion, representing the second largest source of foreign exchange earnings after electronics and electrical exports. The 47.5% increase in tourist receipts exceeded the Eighth Malaysia Plan target of an average annual growth of 9.5%. The exceptional performance reflected the success of well targeted promotional strategies and policies, in particular the diversification of promotional efforts to niche areas and new markets in Eastern Europe, West Asia, India, and China. The tourism industry also benefited from the strategy to provide a wider variety of products for the tourism market including eco-tourism, agro-tourism and yachting tourism and the hosting of international conventions and major sporting events such as the Formula One Race and Le Tour de Langkawi, and events catering for shoppers such as Mega Sale Carnivals and the Langkawi International Maritime and Aviation (LIMA) exhibition. Mega Sales Carnivals, in particular, contributed towards the significant increase in the number of excursionists.

Meanwhile, efforts to establish Malaysia as an educational regional hub continued. However, in 2001, the uncertainty besetting the regional economies and increased competition from the Philippines, Singapore and Thailand affected the number of foreign students studying in Malaysia. As a result, the total number of foreign students at all levels of education (comprising tertiary, secondary and primary education) in both public and private institutions declined by 23.5% to 20,384 students. This was reflected in a decline in education receipts by 10.1%. Students from Indonesia and China

**Graph 1.43**
**2001: Components of Gross Payments in the Services Account (% share)**




**Graph 1.44**
**2001: Components of Gross Receipts in the Services Account (% share)**

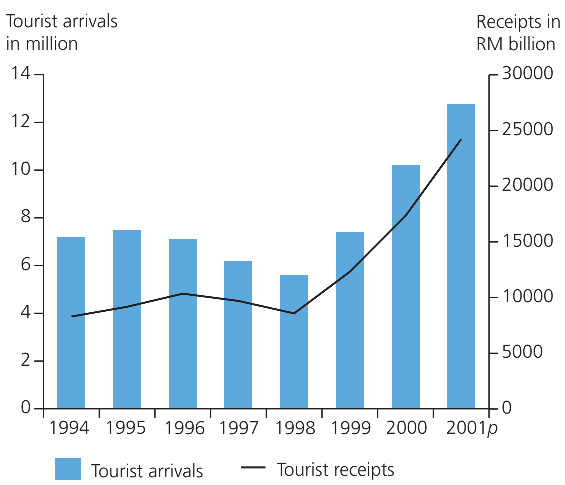


continued to account for the bulk of the foreign students in Malaysia. On the payments front, higher expenditure on travel and education abroad reflected increased business travel and a larger number of students studying abroad.

The **transportation account** deficit was contained at RM11.4 billion as the reduction in receipts was offset by a decline in payments. Gross payments abroad recorded a modest decline associated with lower freight payments on account of the lower volume of trade and freight charges. Gross receipts also declined due mainly to lower earnings on passenger fares and air cargo services provided by the national airline, reflecting lower demand from neighbouring countries. Receipts from charter services were also lower. Despite the decline in external trade, earnings from cargo services provided by major domestic shipping companies and port-related activities continued to register increases during the year. The increase in shipping capacity as well as improvement and expansion of port facilities and services resulted in container throughput of the six major ports increasing by 43.5% to 7.3 million TEUs in 2001. The increase in volume handled was underpinned by the growth in transhipment trade, in particular, transhipment handled by Port Klang and the Port of Tanjung Pelepas (PTP). Strategic business alliances and management expertise provided by foreign partners helped to improve efficiency and handling capacity at the port resulting in a higher volume of activity.

The **other services** account posted a higher net outflow of RM13.2 billion. The deterioration stemmed mainly from a sharp decline in export

**Graph 1.45**
**Tourist Arrivals and Tourist Receipts**




*p* Preliminary

earnings due to lower foreign demand for contract and professional services offered by Malaysian companies. Meanwhile, payments for imported services declined modestly due mainly to lower demand for construction and engineering services during the year. However, payments in areas relating to communication services and computer and information services (ICT enhancement) and mergers and restructuring exercises in the corporate, banking and financial services sectors remained substantial. The payments in other services account also partly reflected the increase in strategic business alliances which usually led to higher imports of other services such as professional, business and technical services.

The **income account** deficit fell by 9.1% to RM25.9 billion or 8.5% of GNP in 2001. The improvement reflected lower repatriation of profits and dividends accruing to foreign direct investors, given lower export earnings of the export-oriented electronics and electrical industries. Repatriation of profits and dividends of foreign direct investors contributed 90% of the net outflow in the income amount. However, the actual outflow of investment income was considerably lower as a significant portion of the profits and dividends were reinvested in the country. Net outflow of profits and dividends accruing to portfolio investments was also significantly lower. However, the other investments component (mainly interest income) of the income account reverted to a deficit position, as lower interest rates abroad led to lower returns from the external assets of BNM and the corporate sector (including commercial banks).

The **financial account** of the balance of payments turned more favourable in 2001, with a lower net outflow of RM14.8 billion. The improvement was attributed mainly to the lower net outflow of short-term capital and, to a lesser extent, higher external borrowings by the Federal Government and the non-bank private sector.

Reflecting the continued commitment by foreign investors to undertake new projects as well as expansion and diversification of existing projects in Malaysia, the value of proposed foreign investments in manufacturing projects approved by the Ministry of International Trade and Industry remained significant in 2001, amounting to RM18.3 billion. In terms of actual **direct investment in Malaysia**, inflows for new and expansion projects were lower in 2001. Lower inflows of direct investment in the manufacturing sector reflected the ongoing

**Table 1.25**
**Balance of Payments: Financial Account**

| | 2000 | 2001*e* | 2000 | 2001*e* |
|---|---|---|---|---|
| | RM billion | | US$ billion | |
| **Financial Account** | **-23.8** | **-14.8** | **-6.3** | **-3.9** |
| **Direct Investment** | **6.7** | **1.0** | **1.8** | **0.3** |
| In Malaysia (foreign direct investment) | 14.4 | 2.1 | 3.8 | 0.6 |
| Abroad (overseas investment) | -7.7 | -1.1 | -2.0 | -0.3 |
| **Portfolio Investment** | **-9.4** | **-2.5** | **-2.5** | **-0.7** |
| **Other Investment** | **-21.1** | **-13.4** | **-5.6** | **-3.5** |
| Official sector | 3.9 | 7.1 | 1.0 | 1.9 |
| Federal Government (net) | 0.9 | 6.3 | 0.2 | 1.7 |
| Gross borrowing | 4.8 | 7.0 | 1.3 | 1.8 |
| Repayment | 3.9 | 0.7 | 1.0 | 0.2 |
| NFPEs (net) | 3.1 | 0.9 | 0.8 | 0.2 |
| Gross borrowing | 6.9 | 10.7 | 1.8 | 2.8 |
| Repayment | 3.8 | 9.8 | 1.0 | 2.6 |
| Private sector | -25.1 | -20.5 | -6.6 | -5.4 |

*e* Estimates

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

consolidation by major multinational corporations following the decline in global demand and excess capacity. Nevertheless, inflows of new equity for the setting up of strategic alliances with Malaysian partners, particularly in the telecommunications and financial services sectors, were significant in the first three quarters of 2001. These inflows, which are smaller in average dollar size and low in import content, bring technology and other expertise that contribute towards raising productivity in Malaysia.

On a net basis, direct investment in Malaysia amounted to RM5.2 billion in the first three quarters of 2001. The sale of strategic interests in one services company to Malaysian residents in the fourth quarter largely offset this net inflow. As a result, net inflow of direct investment in Malaysia moderated to RM2.1 billion for 2001 as a whole.

The sale of strategic interests by non-resident investors in the fourth quarter of 2001 reflected the decision by a Malaysian company to acquire the stake of its non-resident partners. The move was to enable the Malaysian company to regain control over the subsidiary company, as part of its corporate restructuring exercise. The acquisition was financed by the issuance of long-term debt securities to the non-resident investors as well as by raising an offshore loan. Hence, the transaction, which merely resulted in the change of ownership of the subsidiary, had no impact on international reserves or domestic economic activities as the outflow of direct investment was offset by the inflow of funds from the debt securities issued to non-residents (portfolio investment) and offshore loans.

The Government remains committed to providing a cost-competitive business and investment environment for both foreign and domestic investors. In this regard, the Government continued to provide the Special Pre-Package Incentives that are customised to meet the specific needs of individual investors bringing in quality investment to the promoted sectors of the economy. Several existing incentives were also improved in order to attract the high technology and high value-added investment, consistent with Malaysia's growth strategies. To encourage existing foreign investors to continuously undertake expansion projects or diversify into higher quality investment, the period for the reinvestment allowance was extended from 5 to 15 years in the 2002 Budget. The Foreign Investment Committee (FIC) guidelines on property acquisition by foreigners were further liberalised in April 2001.

**Direct investment abroad** or overseas investment by Malaysian corporations continued to remain high at RM1.1 billion in the first quarter of 2001, reflecting the strategic business decisions to provide greater synergy to Malaysian corporate activities. A significant share of investment abroad during this period was attributed to the acquisition of palm oil plantations in Indonesia. Towards mid-year, direct investment abroad declined as companies began to adopt a more cautious approach in their investment plans abroad following the severe global economic slowdown. As part of corporate restructuring exercise, some companies also liquidated their businesses overseas, particularly towards the end of 2001, and repatriated the proceeds to Malaysia, thus partly offsetting the large outflows in early 2001. For the year as a whole, direct investment abroad recorded a significantly lower net outflow of RM1.1 billion. The non-financial public enterprises (NFPEs) continued to undertake investments overseas, particularly in the agriculture and oil and gas sectors, mainly in Indonesia and China.

**Portfolio investment** recorded a significantly lower net outflow of RM2.5 billion in 2001, about one-quarter of the amount recorded in the previous year. Although there were uncertainties in the global financial markets, outflows of portfolio investment were significantly lower as portfolio investors were already underweight in the Malaysian market. In the second half of the year, the accelerated pace of corporate restructuring helped to improve sentiments on the Kuala Lumpur Stock Exchange, thus attracting new inflows of funds, particularly in the third quarter. However, the uncertainty following September 11 led to profit-taking activities that resulted in some net outflows in the fourth quarter, reversing the trend in the third quarter. With the release of more indicators supporting economic recovery, portfolio investments have strengthened to record net inflows in the first two months of 2002.

The **other investment account** recorded a significantly lower net outflow of RM13.4 billion in 2001. The **official sector account** recorded a higher net inflow of RM7.1 billion, comprising mainly drawdown of long-term external loans by the Federal Government. Repayments were lower during the year.

While maintaining the prudent policy of keeping the debt level low, the Federal Government, nevertheless, took advantage of favourable market conditions and low interest rates to access the international capital markets in order to maintain a market presence and to establish a benchmark rate for Malaysian corporations. Proceeds from the issuance of the US$1 billion Notes in July, a syndicated loan of US$540 million in December as well as the drawdown of loans under the Miyazawa Initiative totalled RM7 billion. Although the gross borrowings by NFPEs increased significantly in 2001, a large part of the new borrowings was used to refinance the more expensive existing offshore loans.

The **private sector** recorded a lower net outflow of RM20.5 billion due mainly to lower net outflow of other short-term capital. As interest rates abroad were reduced to support economic activities, there was less incentive for residents to place or retain funds abroad. Interest rate differentials moving in Malaysia's favour since September encouraged the early repatriation of export proceeds, while trade credits extended to foreign importers also declined. The net external assets of the banking institutions also declined in the second half of the year following the unwinding of foreign currency inter-bank placements as importers reduced hedging activities. In addition to lower short-term outflows, there was a net inflow of external borrowings by the non-bank sector, mainly to finance the purchase of non-resident assets as part of a corporate restructuring exercise.

**Table 1.26**
**Outstanding External Debt**

| | 2000 | | 2001*p* | |
|---|---|---|---|---|
| | RM million | US$ million | RM million | US$ million |
| **Total debt** | **157,720** | **41,505** | **169,778** | **44,678** |
| *Medium and long-term* | *140,266* | *36,912* | *146,437* | *38,536* |
| *Short-term* [1] | *17,454* | *4,593* | *23,341* | *6,142* |
| *As % of total debt* | *11* | *11* | *14* | *14* |
| *As % of international reserves* | *15.4* | *15.4* | *19.9* | *19.9* |
| **As % of GNP** | | | | |
| Total debt | 50.5 | 50.5 | 55.4 | 55.4 |
| Medium and long-term debt | 44.9 | 44.9 | 47.7 | 47.7 |
| **As % of exports of goods and services** | | | | |
| Total debt | 36.4 | 36.4 | 42.9 | 42.9 |
| Medium and long-term debt | 32.3 | 32.3 | 37.0 | 37.0 |
| **Debt service ratio (%)** | **5.3** | **5.3** | **6.2** | **6.2** |

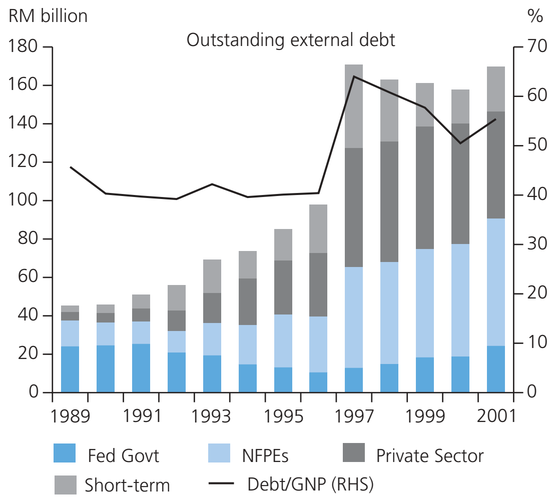
[1] Refers to bank and non-bank private sector short-term debt.
*p* Preliminary

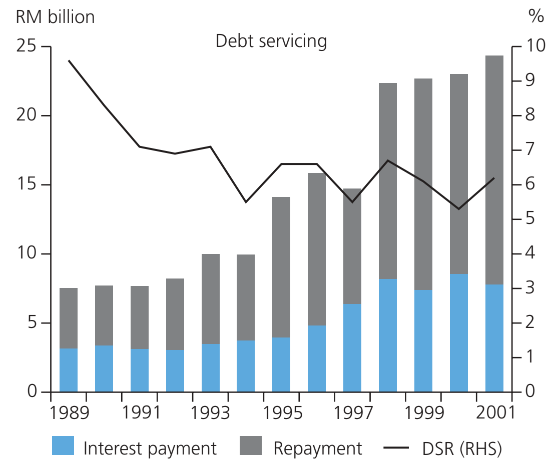
**External Debt**

Prudent external debt management remained an integral element of public policy in 2001. In the management of risk and liquidity exposure, Malaysia maintained an external debt management strategy which has already incorporated the international guidelines that were proposed for adoption by emerging market economies for effective debt management following the Asian crisis. Corporations sourcing external funds for operations in Malaysia were required to have foreign exchange income to repay the debt. At the same time, they were encouraged to raise loans with longer maturity, while short-term borrowing by the non-bank private sector to finance long-term investment were not encouraged. The policies were effective in keeping the nation's external debt low with only a small share of short-term debt, and a debt profile that is biased towards the longer end. About two-thirds of the medium and long-term debt have remaining maturities of more than three years. Overall, this active debt management strategy has served Malaysia well in strengthening the underlying fundamentals and reducing vulnerability to external shocks.

As a result of these policies and an efficient debt monitoring system, the nation's external debt position remained contained at a relatively low level. The total external debt outstanding increased moderately by

**Graph 1.46**
**External Debt**




7.6% to RM169.8 billion (US$44.7 billion) at the end of 2001. The ratio of external debt to GNP increased to 55.4% (peak of 64% in 1997 following the Asian crisis). The external debt service ratio (excluding prepayments) remained low at 6.2%. The global trend toward lower interest rates has had a positive effect in terms of reduced interest payments on Malaysia's existing external loans. Nevertheless, total debt servicing increased in absolute terms by 6.1% to RM24.4 billion, reflecting the maturity of several bond issues that were raised in the mid-1990s as well as the early retirement of some of the more expensive bonds by the non-financial public enterprises.

The new loan drawdowns were mainly by the public sector (RM7.2 billion) and to a lesser extent the private sector (RM2.8 billion), reflecting lower private investment during the year. An exchange revaluation gain of RM3.8 billion moderated the increase in the external debt level in ringgit terms. As a result, the medium and long-term external debt increased by 4.4% to RM146.4 billion (US$38.5 billion) at the end of 2001.

In terms of currency composition, the bulk of the medium and long-term external debt was denominated in United States dollars with a large share of 77% of debt outstanding at end-2001. The share of yen denominated debt was lower at 15%, reflecting the increased drawdown of US dollar loans, some diversification of borrowing into euro loans, the maturity of yen bonds during the year, as well as the depreciation of the yen. The remaining 8% of the debt was accounted for by other international currencies, including the euro, Singapore dollar and pound sterling. In the case of private sector loans, the currency composition of liabilities generally corresponds closely with the currency composition of earnings, thereby providing a natural hedge against currency risks. As the external debt is diversified in terms of major currencies, the depreciation of the yen and euro has led to an exchange revaluation gain, reducing the external debt in ringgit terms.

**Public sector external debt**: The Federal Government's external debt increased to RM24.3 billion at the end of 2001. It continued to account for a small share (14%) of total external debt. As in previous years, the Federal Governmentís financing requirements were primarily met from domestic non-inflationary sources. Nevertheless, taking advantage of the favourable market conditions and the nation's low external debt position, the Government tapped the international capital markets, partly to maintain a market presence as well as to take advantage of lower US interest rates to set a benchmark rate to facilitate the corporate sector's access to the US, European and other international markets. In July, the Federal Government issued US$1 billion 10-year Notes due 2011. Reflecting the demand for quality debt papers, these Notes were three times oversubscribed and priced at 228 basis points above the 10-year US Treasuries. In December, it raised a syndicated loan of US$540 million from offshore banks in Labuan. The Government also drew down loans committed under the Miyazawa Initiative as well as project loans from multilateral sources such as the World Bank, Islamic Development Bank and Asian Development Bank. In March 2002, the Federal Government reopened its US$1 billion 7.5% Notes due 2011 by an additional US$750 million. The reopening was priced at the comparable US Treasuries plus 175 basis points to yield 6.8% with a reoffer price of US$104.769.

Based on the US$500 million initially issued, the Notes were oversubscribed by more than seven times.

Reflecting Malaysia's strong fundamentals, the interest **spread** on Malaysia's benchmark securities tightened in 2001. The spread on Malaysian US$1.5 billion Notes due 2009 narrowed to 148 basis points at end-2001, while the spread on the US$1 billion 10-year Notes due 2011 narrowed to 167 basis points. The interest in Malaysia's US dollar bond issues had also increased since May 2001 with the removal of the exit levy and the announcement of a shift in policy by Moody's which could allow companies to be rated higher than the sovereign rating. In a move reflecting the strengthening of the country's external position, Standard & Poor's revised the outlook on Malaysia's long-term sovereign foreign currency debt rating from stable to positive on 4 March 2002, while reaffirming Malaysia's BBB rating.

The **NFPEs** also took advantage of the low interest rate environment to access long-term funds from the international capital markets to refinance their more expensive existing offshore loans. This was reflected in increased gross borrowing of RM10.7 billion in 2001. The new borrowings included the US$600 million 10-year Notes launched by Tenaga Nasional Berhad, and the US$250 million Floating Rate Notes raised by 1st Silicon (Malaysia) Sdn. Bhd. Other major borrowers were Petronas and Silterra Malaysia Sdn. Bhd. In addition, Tenaga Nasional Berhad and Bank Pembangunan continued to draw down loans offered under the Miyazawa Initiative for the development of power plants and transportation infrastructure projects.

The NFPEs as a group recorded a small net inflow of external borrowing of RM0.9 billion as repayments more than doubled, reflecting the refinancing of loans to take advantage of better interest rate spreads as well as the maturity of bonds issued in mid-1990s. Due partly to the reclassification of Malaysia Airline System Berhad (MAS) and its external debt as part of the public sector in 2001, the outstanding debt of the NFPEs increased by 13.3% to RM66.5 billion at the end of 2001.

**Private sector external debt**: Private sector debt continues to account for the bulk of the Malaysia external debt, at 47% of total debt in 2001. During the year, the private sector recorded net external borrowing of RM2.8 billion in 2001. The higher borrowing reflected mainly the issuance of debt securities to finance the purchase of non-resident assets in Malaysia as part of a corporate restructuring exercise. The non-resident controlled companies continued to account for a large share of the loans, sourcing the borrowing largely from offshore shareholders and parent and associate companies. Such loans were generally provided on flexible terms, including longer maturity and at concessionary interest rates. These loans are also naturally hedged, with foreign currency earnings to service the debt. After taking into account the reclassification of MAS external debt as an NFPE debt and the exchange revaluation gain, private sector external debt outstanding declined by 11.4% to RM55.6 billion at end-2001.

**Short-term external debt** (maturity of one year or less) comprises mainly short-term borrowing by the banks related to their trade financing activities, revolving credits and inter-company loans. In 2001, short-term external debt increased to RM23.3 billion (US$6.1 billion), largely reflecting the increase in borrowing by the commercial banks. As a prudent measure, the commercial banks are required to observe the external open position limit. As at the end of 2001, the banks' net open position was well below the total approved limit.

The share of short-term debt remained well within prudential limits at 13.7% of total external debt and 19.9% of the international reserves of Bank Negara Malaysia. Including medium and long-term debt falling due within 12 months, short-term debt would amount to RM38.5 billion (US$10.1 billion), less than one third the level of international reserves.

**International Reserves**

The **net international reserves** held by BNM (comprising gold and foreign exchange holdings, IMF reserve position and holdings of Special Drawing Rights (SDR)) increased by RM3.7 billion or US$964 million in 2001 to RM117.2 billion or US$30.8 billion as at end-2001. The reserves level increased further to RM119.6 billion or US$31.5 billion as at 28 February 2002. This level of reserves is sufficient to finance 5.2 months of retained imports and to cover 5.1 times the short-term external debt. The strengthening of the reserves position reflected the build-up in foreign exchange holdings from trade and long-term capital inflows.

During the course of 2001, there was greater variability in the net international reserves of BNM. Under a fixed exchange rate regime, greater variability in reserves would indeed occur as reserves changes reflect the supply and demand conditions in the foreign exchange market. Between January to mid-April, Malaysia's net international reserves declined to RM99.8 billion (US$26.3 billion) as at 15 April 2001, from RM113.5 billion (US$29.9 billion) at end-2000. Subsequently, the reserves level stabilised and began to steadily increase from end-June. By end-year, the reserves exceeded the level at end-December 2000. At its lowest point, the reserves level had remained high and was equivalent to 3.9 months of retained imports and 5.5 times the short-term external debt. Reserves were at all times unencumbered and usable as Malaysia did not engage in forward contracts.

In 2001, when the yen depreciated above ¥125 level against the US dollar in late March and early April, there were some sentiment driven outflows during this period of unstable market conditions. A substantial share of the reserves decline, however, reflected trade and investment-related demand for foreign exchange by the Malaysian corporate sector. There was also repayment of external debt to reduce leverage of corporations given the availability of the significantly lower cost of domestic sources of funds. Such repayment of debt reduced Malaysia's external debt and strengthened the external position of Malaysia. This period also saw outflows of overseas investments by Malaysian corporations which reflected strategic business decisions to provide greater synergy to Malaysian corporate activities. These investments also enhanced prospects for future exports of goods and services as well as income and profit repatriation to Malaysia. During the period March-April, the large demand for trade payments reflected 'pre-emptive' outflow as the 'cheaper' US dollar (due to forward

**Graph 1.47**
**Net International Reserves**

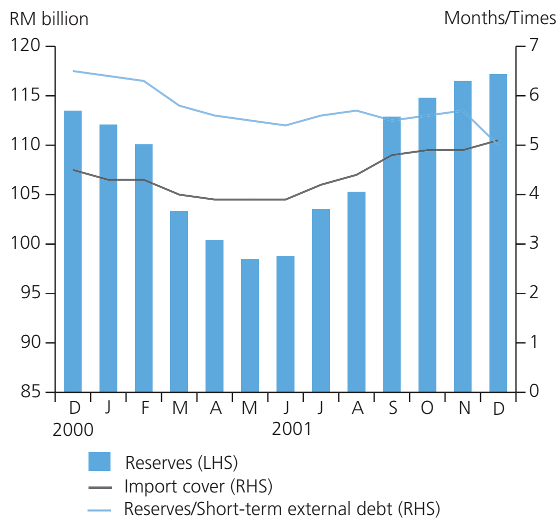



**Table 1.27**
**Net International Reserves**

| | As at end | | | Change |
|---|---|---|---|---|
| | 1999 | 2000 | 2001 | 2001 |
| | RM million | | | |
| SDR holdings | 330.3 | 418.7 | 487.8 | 69.1 |
| IMF reserve position | 3,168.2 | 3,310.9 | 3,193.5 | -117.4 |
| Gold and foreign exchange | 113,766.0 | 109,835.4 | 113,542.3 | 3,706.9 |
| **Gross International Reserves** | **117,264.5** | **113,565.0** | **117,223.6** | **3,658.6** |
| Less BNM external liabilities | 21.0 | 23.7 | 20.7 | -3.0 |
| **Net International Reserves** | **117,243.5** | **113,541.3** | **117,202.9** | **3,661.6** |
| **US$ equivalent** | **30,853.6** | **29,879.3** | **30,842.9** | **963.6** |
| Months of retained imports | 5.9 | 4.5 | 5.1 | |
| Reserves/Short-term external debt (times) | 5.1 | 6.5 | 5.0 | |

discounts arising from interest rate differentials) created incentives to pay forward for imports.

In March 2001, the exchange revaluation loss from the quarterly revaluation of external reserves holdings also led to an unrealised decline of US$0.9 billion in reserves. As the central bank reserves are diversified in terms of the major currencies, the appreciation of the US dollar led to an unrealised revaluation loss on Euro and yen denominated assets. In the third quarter, a revaluation gain of RM3 billion or US$0.8 billion was recorded as US dollar depreciated against Euro and yen. For 2001 as a whole, the total quarterly revaluation loss amounted to RM4.1 billion or US$1.1 billion.

In 2001, Bank Negara Malaysia stepped up its efforts to enhance transparency and explained in greater detail the nature of the flows. This aimed to increase understanding on the movement of the reserves, in particular that which reflected structural adjustments in the corporate sector that have contributed to Malaysia's long-term economic fundamentals.

Reserves stabilised in the region of RM98.8 billion (US$26 billion) in the period mid-April to end-June 2001. Since end-June, net international reserves increased by RM18.4 billion or US$4.8 billion. Interest rate differentials that moved in Malaysia's favour from September encouraged the early repatriation of export proceeds. While exports declined following the global economic slowdown, this decline was cushioned by a corresponding reduction in imports, resulting in a sustained large trade surplus. The larger trade-related flows was also a reflection of lower import obligations arising from earlier forward payments made in the first half of 2001. There were also continued inflows of foreign direct investment during this period, reflecting inflows from strategic business alliances. Meanwhile, the drawdown of Federal Government external loans, including the US$1 billion 10-year Notes and a syndicated loan of US$540 million from offshore banks in Labuan, more than offset the Government loan repayments during the year. With improved market sentiment, portfolio capital registered a net inflow during a major part of the third quarter. Nevertheless, this trend reversed since the second half of September following the uncertainties associated with September 11 as well as profit-taking activities, resulting in a net outflow of portfolio capital during the fourth quarter.  These flows, however, reversed again to show a steady uptrend in January - February 2002.

Malaysia's holdings of reserves in the form of **Special Drawing Rights** (SDR) increased by RM69.1 million to RM487.8 million at the end of 2001. The increase was mainly on account of the receipts of remuneration from the IMF arising from Malaysia's net creditor position with the Fund.  During the year, Malaysia's **reserve position with the IMF** remained unchanged. In ringgit terms, however, the reserves with the IMF registered a decline of RM117.4 million to RM3.2 billion at the end of 2001 on account of an exchange revaluation loss during the year.

**FLOW OF FUNDS**

The economy registered a smaller resource surplus of RM27.4 billion or 8.9% of GNP in 2001 (a surplus of RM31.9 billion or 10.2% of GNP in 2000). In terms of the balance of payments, the smaller resource surplus reflected the larger decline in exports of goods and services relative to imports. Whilst exports declined by 8.8%, imports deteriorated by 8.7% in 2001. From the savings-investment gap perspective, the smaller resource surplus largely reflected the smaller net savings position. Although net savings of the private sector were higher, these were somewhat offset by lower net savings of the public sector. The flow of funds between various sectors of the economy in 2000 and 2001 is summarised in Tables 1.24 and 1.25 respectively.

While the public sector had a lower disposable income during the year, the fiscal stimulus programme by the Government to support economic activity resulted in higher public investment and consumption expenditures. Consequently, the resource surplus of the public sector was significantly lower at RM0.9 billion in 2001 (RM10.8 billion in 2000). The resource surplus reflected entirely the surplus from the NFPEs of RM12.1 billion. This largely offset the resource gap of the general government of RM11.2 billion. The bulk of the resource gap of the

**BNM's Reserves Management and Reporting Policy**

The objectives of **reserve management** of BNM are to ensure capital preservation and liquidity of reserves whilst optimising returns. BNM has formulated a customised benchmark to serve as a guide for its investment decisions, taking into account the need to ensure the safety of reserves and to meet liquidity requirements as well as the level of tolerance for risk in investment decisions. The benchmark portfolio and BNM's international reserves are made up of the major foreign currencies and gold. The reserves are held in the form of foreign currency deposits or invested in high investment grade sovereign papers. BNM does not engage in options in foreign currencies vis-a-vis ringgit and there are no foreign currency loans with embedded options. There are also no undrawn, unconditional credit lines provided by or to other central banks, international organisations, banks and other financial institutions. Reserves are usable and unencumbered.

BNM releases a press statement on international reserves together with the statement of assets and liabilities fortnightly with a one-week lag. As part of the measures to enhance transparency in the international financial system and to facilitate an assessment of the foreign exchange risk exposure, BNM publishes detailed disclosure of international reserves at the end of each month (with a one-month lag) in line with the requirements of the reserves data template under the IMF's Special Data Dissemination Standard (SDDS). This includes the release of forward-looking information on the size, composition and usability of the official reserves and other foreign currency assets and the future and potential (contingent) inflows and outflows of foreign exchange over the next 12 months.

**Table 1.28**
**Flow of Funds: 2000**

| | National Accounts | Domestic Economy | | | Rest of the World | Sum |
|---|---|---|---|---|---|---|
| | | Public Sector | Private Sector | Banking System | | |
| | RM billion | | | | | |
| Disposable Income | -304.5 | 92.7 | 211.8 | | | 0 |
| Consumption | 181.4 | -36.2 | -145.2 | | | 0 |
| Investment | 87.1 | -43.6 | -43.5 | | | 0 |
| Change in Stocks | 4.1 | -2.1 | -2.0 | | | 0 |
| Exports of Goods and Non-Factor Services | 427.5 | | | | -427.5 | 0 |
| Imports of Goods and Non-Factor Services | -359.5 | | | | 359.5 | 0 |
| Net Factor Payment Abroad | -28.6 | | | | 28.6 | 0 |
| Net Transfers | -7.5 | | | | 7.5 | 0 |
| Non-Financial Balance | 0.0 | 10.8 | 21.1 | 0.0 | -31.9 | 0 |
| Foreign Financing | | | | | | |
| Direct Investment | | | 6.7 | | -6.7 | 0 |
| Net Foreign Borrowings | | 3.9 | -28.7 | | 24.8 | 0 |
| Net Change in Foreign Assets | | | | | | |
| BNM | | | | 3.7 | -3.7 | 0 |
| Banking System | | | | -5.7 | 5.7 | 0 |
| Domestic financing | | | | | | |
| Change in Credit | | 4.4 | 26.0 | -30.4 | | 0 |
| Change in Money Supply, M3 | | | -21.9 | 21.9 | | 0 |
| Net Borrowings from Non-Bank Sector | | -19.1 | 19.1 | | | 0 |
| Net Errors and Omissions | | | -22.3 | 10.5 | 11.8 | 0 |
| Sum | | 0 | 0 | 0 | 0 | |

**Table 1.29**
**Flow of Funds: 2001**

| | National Accounts | Domestic Economy | | | Rest of the World | Sum |
|---|---|---|---|---|---|---|
| | | Public Sector | Private Sector | Banking System | | |
| | RM billion | | | | | |
| Disposable Income | -298.5 | 88.7 | 209.8 | | | 0 |
| Consumption | 191.4 | -40.7 | -150.7 | | | 0 |
| Investment | 83.3 | -49.2 | -34.1 | | | 0 |
| Change in Stocks | 3.6 | 2.1 | 1.5 | | | 0 |
| Exports of Goods and Services | 389.8 | | | | -389.8 | 0 |
| Imports of Goods and Services | -328.4 | | | | 328.4 | 0 |
| Net Factor Payment Abroad | 25.9 | | | | 25.9 | 0 |
| Net Transfers | 8.1 | | | | 8.1 | 0 |
| Non-Financial Balance | 0.0 | 0.9 | 26.5 | 0.0 | -27.4 | 0 |
| Foreign Financing | | | | | | |
| Direct Investment | | | 1.0 | | -1.0 | 0 |
| Net Foreign Borrowings | | 7.1 | -23.0 | | 15.9 | 0 |
| Net Change in Foreign Assets | | | | | | |
| BNM | | | | -3.7 | 3.7 | 0 |
| Banking System | | | | 0.1 | -0.1 | 0 |
| Domestic financing | | | | | | |
| Change in Credit | | -1.5 | 20.4 | -18.9 | | 0 |
| Change in Money Supply, M3 | | | -13.0 | 13.0 | | 0 |
| Net Borrowings from Non-Bank Sector | | -6.5 | 6.5 | | | 0 |
| Net Errors and Omissions | | | -18.4 | 9.5 | 8.9 | 0 |
| Sum | | 0 | 0 | 0 | 0 | |

general government was financed through net domestic borrowings (RM13.4 billion). Nonetheless, together with net foreign borrowing of RM7.1 billion and the resource surplus of the NFPEs, a total of RM6.5 billion was transferred to the private sector during the year, mainly in the form of loans and grants.

With slower economic growth, private sector disposable income contracted slightly to RM209.8 billion in 2001 (RM211.8 billion in 2000). However, with low interest rates, availability of credit and the Government's policies to encourage domestic consumption spending, private consumption expenditure was higher in 2001. Consequently, private sector savings declined to RM59.2 billion (RM66.7 billion in 2000). However, reflecting the strong decline in private investment expenditure and only a marginal decline in private savings, the resource surplus of the private sector increased to RM26.5 billion (RM21.1 billion in 2000). In addition, part of the investment expenditure in 2001 was financed by inflows of FDI. On the whole, together with net borrowings from the banking system (RM20.4 billion) and transfers from the public sector (RM6.5 billion), the resource available to the private sector amounted to RM54.4 billion (RM72.9 billion in 2000).

The bulk of these excess resources of the private sector were seen in net placements of deposits of RM13 billion with the banking system (including the holdings of currency). Some of the excess also leaked from the domestic economy, mainly in the form of overseas investment (RM20.5 billion) and portfolio outflows (RM2.5 billion). Meanwhile, net external assets of the banking system remained relatively stable. The continued current account surplus and inflows of FDIs were more than sufficient to accommodate these outflows, and net international reserves of BNM rose by RM3.7 billion to RM117.2 billion as at the end of 2001.