

**Economic growth moderates**  
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**THE** Malaysian economy only managed to achieve a moderate growth rate of 5.2% in the fourth quarter of 2011 because it has traditionally been over dependent on consumer demand in America and Europe to generate a growth rate in excess of 8% or even 7%. The Malaysian economy is a dependent economy in the sense that if America's growth rate slackens, Malaysia's growth rate also slackens in tandem.

The moderate growth rate of 5.2% has been obtained on the back of growth in exports of palm oil to China and to a lesser extent on the exports of crude oil and of course domestic demand especially public sector demand in the form of consumption and investment.

Private sector investment could have played a larger role given the recent fashionable trend for Malaysian corporations including banks to use domestic savings for investments overseas.

The sharp rise in Malaysia's direct investments overseas has given the impression that the limits to investment in Malaysia has been reached and Malaysia does not need any more infrastructure development.

While the amount of private investment has been wanting, the government has given private consumption a boost by its expansionary fiscal policy and various cash handout programmes and projects. The 1Malaysia shops are also selling consumer goods at a discount and hence increasing private consumption.

Domestic demand in the form of public and private consumption and investment and increase in external demand for palm oil and crude oil have been the main drivers of growth in the fourth quarter of 2011, with domestic demand playing an increasing role in generating growth.

Exports of electrical and electronics goods although not as high as when economic growth in America is high is still important as an important contributor of economic growth in Malaysia and hence the leverage the American government has over Malaysia in terms of foreign policy and in terms of dictating the pace of democratic reforms and the development of a civil society with channels of effective dissent and voice.

In terms of consumption, the surprise is that private consumption grew by less than public consumption, reflecting the strategy of the government to stimulate the economy by expansionary fiscal policy.

It probably borrowed from the banks and issued bonds to finance its growing fiscal deficit, which by some accounts is in excess of 6% of GDP.

While one motivation for increased public consumption maybe to create a favourable economic environment to hold elections, the other more pressing need to increase public consumption may be due to the lacklustre performance of the export sector.

Public consumption increased by 23.6% in the fourth quarter of 2011 or by more than three times the growth of private consumption, which increased by 7.19% over the same fourth quarter of 2011.

The other component of domestic demand, that is, total or private and public investment increased by 8.5% in the fourth quarter of 2011. The increase in public investment was mainly due to investments made by non-financial public enterprises.

The services sector, which has been recently extensively liberalised, has not grown very rapidly in contrast to the agricultural sector and the manufacturing sector probably because of the lack of innovations and the high cost of production and lacklustre demand for its output.

Growth in the services sector in the fourth quarter of 2011 was not as impressive as it was in the previous quarter, whereas growth in the manufacturing sector was about the same as in the previous quarter.

Impressive expansion and growth in the agricultural sector has been due to output and export expansion in the oil palm sector due to increased demand from China and perhaps India.

The Economic Transformation Programme gave a major boost to the construction sector as large corporations vied for lucrative infrastructure projects, which are expected to pump prime economic growth in the Malaysian economy.

The sad news is that the growth in public spending and consumption and expansionary fiscal policy has helped fuel inflation in Malaysia reflecting the fact that the Malaysian economy could be better managed.

Although reported headline inflation had declined from 3.4% in the third quarter to 3.2% in the fourth quarter of 2011, it is still higher than the overnight policy rate (OPR) of 3%.

The interest rate on savings deposits is much lower than 3% and hence the lower income groups not only suffer from the effects of negative real interest rates but also have to cope with higher food and fuel prices.

The consumer price index which is an aggregate figure conceals the real hardship suffered by the poor as a result of escalating food prices. The recent quarterly economic report of Bank Negara Malaysia reports that "inflation in the food and non-alcoholic beverages category ... rose to 5.3%", during the fourth quarter of 2011.

The almost stagnant and low overnight policy rate of 3% continued to support loan growth which together with the issue of private debt securities increased financing available to the private sector. The increased loan growth also contributed to housing price inflation and general inflation in the economy.

The reluctance to increase the OPR was because a 3% interest rate was perceived as being conducive to economic growth without much thought given to its inflationary impact on the poor and lower-income groups and the affordability of housing.

The balance of payments remained positive as a surplus of RM6.7 billion was achieved in 2012. This was made possible by both a positive current account and financial account surplus. The financial account was in surplus largely due to an increase in FDI during the fourth quarter of 2011.

The multinational corporations also invested their retained earnings in Malaysia rather than remit them to their parent company. The financial account surplus would have been much higher if not for increasing direct investment overseas by Malaysian corporations.

There is also a reported tendency for Malaysian companies to retain their earnings overseas.

For a small developing economy, it may be a matter of national pride to invest overseas or it may be a reflection of the riskiness of domestic investments when compared to the preferred foreign investments. It appears that concerted efforts may have to be made to encourage domestic investments and produce branded Malaysian goods.

The positive current and financial accounts of the balance of payments contributed to a positive balance in the overall balance of payments as a result of which Malaysia's reserves increased to RM423.4 billion (or US\$133.6 billion) at the end of December 2011. This was sufficient to finance 9.8 months of imports or about 4.1 times the short term external debt of the country.

The impressive performance of the balance of payments and the associated relatively strong demand for the Malaysian ringgit increased the exchange value of the ringgit as a result of which the ringgit appreciated against the US dollar, the euro, the yen, the Indonesian rupiah, the Singapore dollar and the Philippine peso in the fourth quarter of 2011.

The prospects for the Malaysian economy achieving a higher growth rate of 7% or more in 2012 appear dim given the continued lack of external demand from America and Europe.

In view of the continued lacklustre demand for electronics goods amid weakening consumer demand in America, the Malaysian economy can hardly achieve a growth rate of 5% in 2012. It will probably grow by less than 4% on the strength of domestic demand and exports of palm oil and crude oil and manufactured electrical and electronics goods.

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