

# Update on the Malaysian Economy

September 2002

Sound economic fundamentals and the implementation of various fiscal stimulus packages have strengthened domestic demand as well as countered the impact of volatility in the external environment on the Malaysian economy.

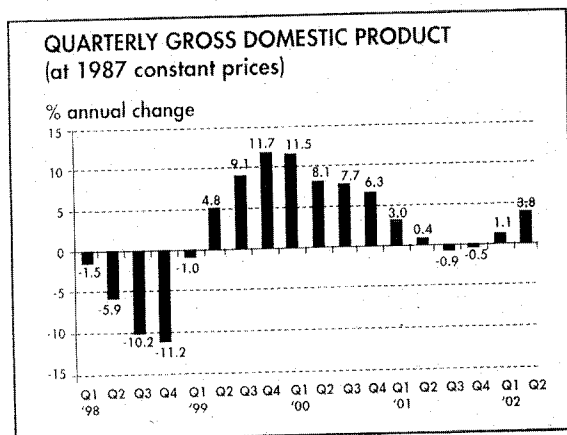
Latest economic indicators show that the economy is well into the recovery phase where economic conditions improved further in the second quarter of 2002 after averting negative growth in the previous year. Short-term prospects are expected to further improve, following measures to boost domestic sources of growth and expanding external trade.

(7.7 per cent) due to higher bank lending activity, higher insurance premium collections and stronger performance in the stock market. The utility sub-sector also recorded strong growth of 7.7 per cent in line with higher industrial demand.

	2001	2001		2002	
		Q3	Q4	Q1	Q2
GDP	0.4	-0.9	-0.5	1.1	3.8
Supply side					
- Agriculture	1.8	-3.5	-4.2	5.0	-1.3
- Mining	1.6	2.2	1.3	1.4	-4.6
- Manufacturing	-6.2	-9.1	-8.4	-2.3	5.6
- Construction	2.3	2.6	2.5	2.9	3.4
- Services	5.7	6.0	5.8	4.4	4.5
Demand Side					
- Consumption	5.8	5.6	7.6	4.8	7.8
- Investment	-2.8	-10.2	-8.1	-8.5	-2.1
- Exports	-7.5	-16.3	-12.0	-6.5	3.1
- Imports	-8.6	-20.1	-10.5	-4.8	6.7

## Gross Domestic Product – Second Quarter 2002

Real GDP expanded further by 3.8 per cent in the second quarter of 2002, on an annual basis, following a 1.1 per cent growth in the previous quarter.



On the supply side, sustained private consumption and improving consumer sentiment led to growth in the services sector of 4.5 per cent, especially in the finance, insurance, real estate and business sub-sector

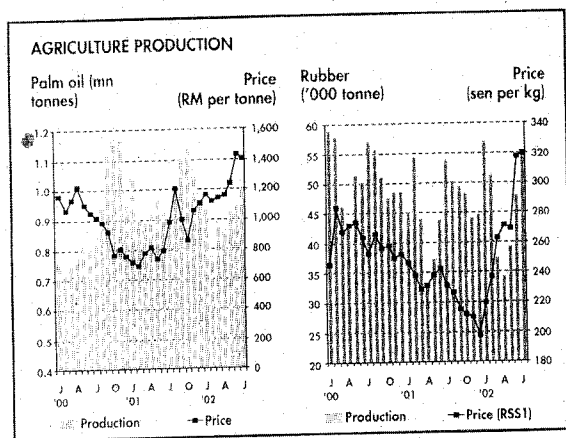
The manufacturing sector registered positive growth of 5.6 per cent in terms of value added, after contracting for 4 consecutive quarters, following improved external conditions and sustained domestic consumption. In the construction sector, growth was higher at 3.4 per cent, supported by the fiscal stimulus programme and the low interest rate environment.

The mining sector contracted in the second quarter of 2002 by 4.6 per cent mainly due to the decline in the production of natural gas. The agriculture sector also contracted in the same quarter by 1.3 per cent, following the fall in supply and to a lesser extent, lower external demand.

On the demand side, private consumption continued to expand by 5.6 per cent in the second quarter of 2002, while public consumption increased strongly by 15.4 per cent, reflecting the fiscal stimulus measures, including a 10 per cent salary adjustment for

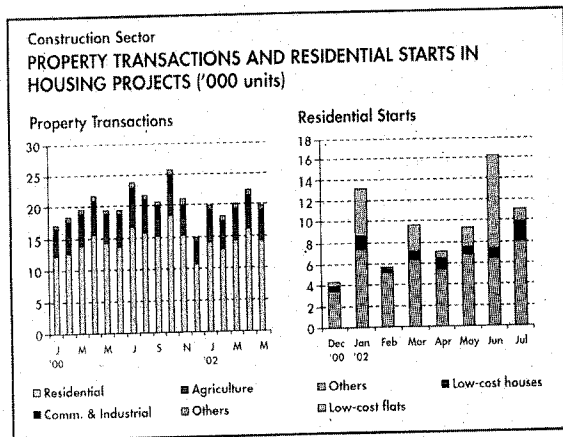


reached a new record of 10,783 MW in July 2002.

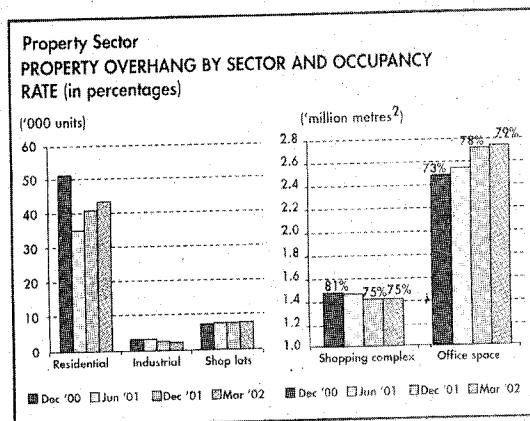


In the *agriculture sector*, the production of palm oil fell by 3.4 per cent for the January-July period of 2002, reflecting lower yields while that of rubber increased by 3.7 per cent for the January-June period. During the same period, the price of palm oil and rubber remained firm, driven primarily by lower global supplies.

In the property market, data up to May 2002 showed an overall increase in property transactions by 4.5 per cent, compared to the same period of last year. The transaction for residential properties, which made up more than three quarters of the total transactions, rose by 4.4 per cent, while that of commercial properties increased by 6.7 per cent. Residential starts in housing projects in the Peninsular Malaysia also recorded improving trends up to July 2002, especially for low-cost apartments in Kuala Lumpur and Selangor.

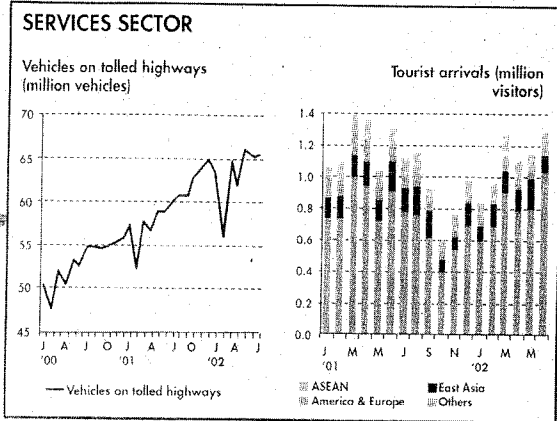


The higher activities in the property market was due to policy measures to strengthen the sector, including the exemption of stamp duties, raising of housing loan eligibility for public sector employees, relaxation of policies on withdrawals from the Employee Provident Fund for the purchase of a second house and attractive bank loan packages. The disposal of properties under the non-performing loans by *Danaharta* (an asset management company) also contributed to the higher property transactions during the period.



At the end of March 2002, the value of property overhang increased marginally by 1.1 per cent to RM27.4 billion compared to the preceding quarter. The number of unsold residential units rose by 6.3 per cent due to the relatively high increase in the number of new houses offered for sale during the period. The number of unsold shop lots and purpose-built office space also increased by 5.2 and 0.7 per cent respectively. This has led to a fall in the occupation rate for office space to 73.4 per cent (77.7 per cent in the fourth quarter of 2001).

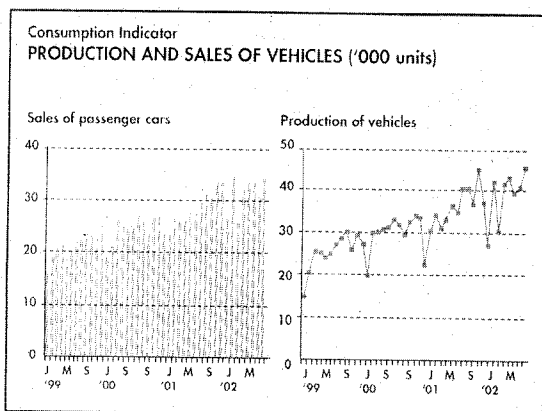
Among the indicators monitored in the *services sector* is the number of vehicles on tolled highways. The number of vehicles increased by 10.5 per cent during the first seven months of 2002 to record over 440 million vehicles, reflecting higher economic activities.



Due to the more cautious approach by tourists traveling abroad following the events in the United States and tensions in the Middle East, the total number of tourist arrivals declined by 8.4 per cent in the first half of 2002. Nevertheless, monthly increases showed improving trends, where the number of arrivals began to pick up since the end of last year.

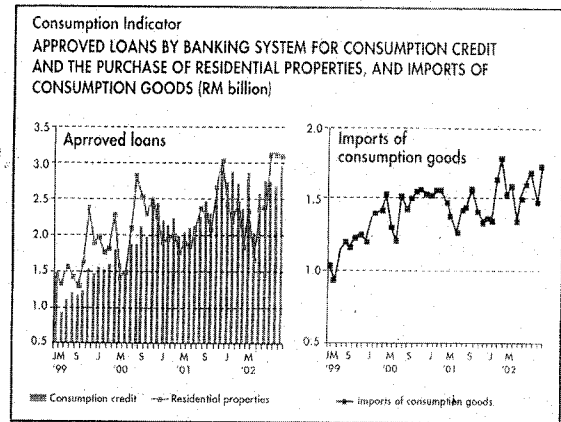
## Consumption Indicators

Several consumption indicators continued to show sustained consumer sentiments. Among others, the sale of passenger cars, which rose further by 19 per cent to over 220,000 units during the first seven months of 2002.

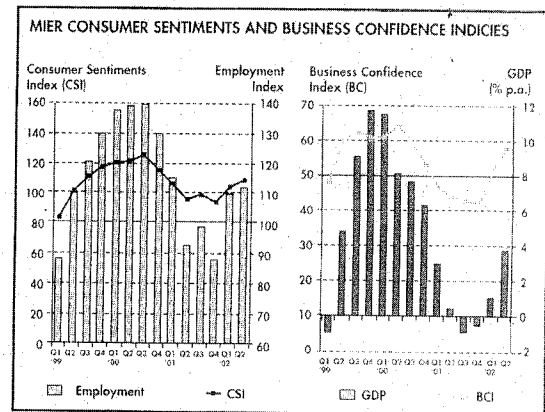


In response to efforts by the Government to stimulate domestic demand, approved loans for consumption credit grew strongly by 16 per cent and the purchase of residential properties by 19 per cent during the first

seven months of this year. Imports of consumption goods recovered to register a strong growth of 12 per cent during the same period.



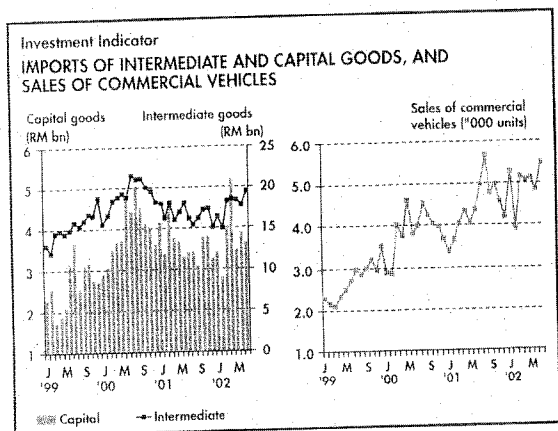
The Consumer Sentiments Index (CSI) and the Business Confidence Index (BCI), published by MIER, also pointed towards improved consumer and investor sentiments. The increase in the CSI reflects continued favourable view on incomes amidst stable labour conditions. The strengthening BCI in the second quarter 2002 to 57.5 points, the highest level since the fourth quarter of 2000, and broad-based improvements across all its components, suggest that the pace of economic expansion is likely to continue.



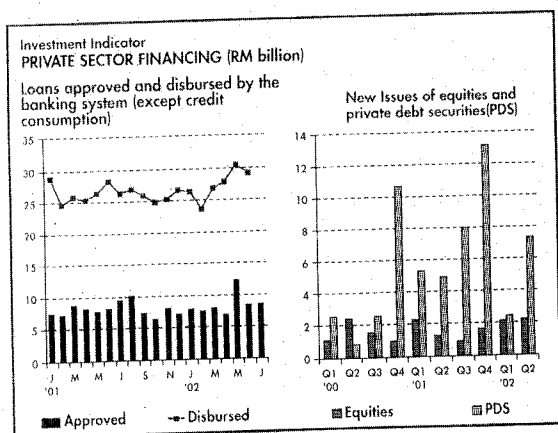
## Investment Indicators

Several indicators are also beginning to show encouraging trends in private investment. Both

the imports of intermediate and capital goods needed for production have begun to record positive growth since March/April, in line with improvements in the demand for exports. During the January-July 2002 period, the sales of commercial vehicles continued to rise strongly by 21 per cent to reach 34,800 units.



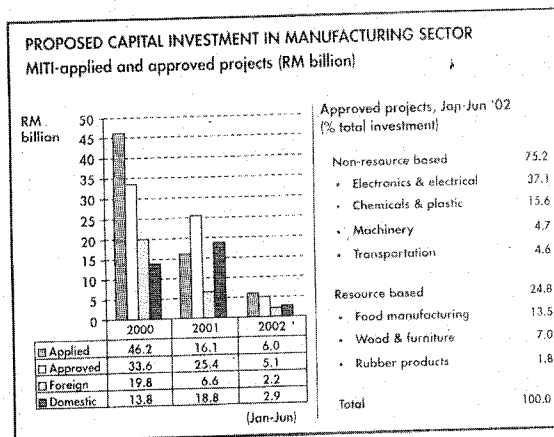
The total amount of loans approved by the banking system (excluding for consumption credit) recorded a positive growth of almost 5 per cent to reach RM59.7 billion during the first 7 months of 2002, out of which the manufacturing and construction sectors accounted for 8.7 per cent and 9.3 per cent respectively. The total disbursed funds (excluding consumption credit) also increased by nearly 4 per cent to the amount of RM193 billion during the same period.



Private sector financing through the capital market continued to show improving trends. A total of RM10.7 billion of new equities were issued during the January-July 2002 period, especially in the finance and manufacturing

sectors. During the same period, a total of RM13 billion of private debt securities were issued, especially in the transport and communications as well as the services sectors.

The number of approved manufacturing projects by the Ministry of International Trade and Industry declined during the first six months of this year. A total of 304 projects were approved, with proposed capital investment of RM5.1 billion, of which 42 per cent was foreign sourced.



In terms of sectoral breakdown, a total of 75 per cent of the proposed capital investment in approved projects went to non-resource-based industries, especially for the manufacture of electrical and electronic products, followed by chemicals as well as machinery manufacturing. The resource-based industries received the rest of the investment, out of which the majority of the investment went to food manufacturing as well as wood and furniture industries.

Survey on 160 companies by the Federation of Malaysian Manufacturers showed that capacity utilization in the manufacturing sector has begun to increase. During the first quarter of 2002, 28 per cent manufacturers reported that their capacity utilization were above the 80 per cent level. This ratio increased in the second quarter to more than 40 per cent of manufacturers. If this trend continues, this

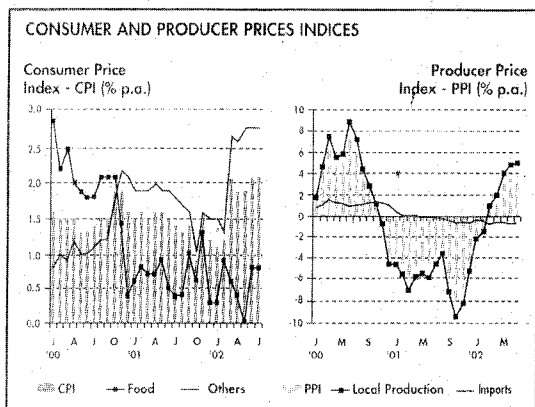
could imply higher investments in the near future.

**CAPACITY UTILIZATION OF THE MANUFACTURING SECTOR**  
Source : Federation of Malaysian Manufacturers (FMM)

% Capacity	% of Total Respondents					
	2001				2002	
	Q1	Q2	Q3	Q4	Q1	Q2
Below 50%	24.2	20.2	14.8	17.6	16.7	9.5
51-79%	48.4	58.2	59.3	48.6	55.4	49.4
80-90%	17.7	14.0	14.8	19.6	14.7	20.3
91-100%	9.7	7.8	11.1	14.2	13.3	20.9

## Prices

The pressure on prices remained subdued. The *Consumer Price Index* (CPI) recorded an increase of 1.8 per cent during the first seven months of this year. In March, the CPI edged up largely due to the one-off price adjustment in telephone service charges. Excluding these telephone charges, the CPI would be lower at 1.1 per cent.



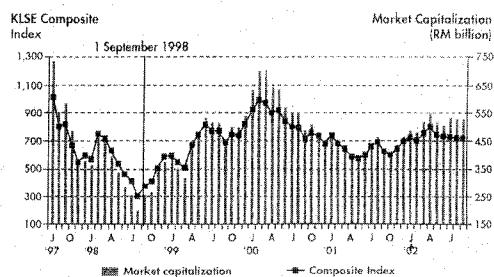
The *Producer Price Index* (PPI) rose by 1.3 per cent during the same period. The largest increase was noted for animal and vegetable oils and fats which recorded a rise of over 50 per cent.

## Financial and Corporate Sector Indicators

The *Kuala Lumpur Stock Exchange* (KLSE), which was bullish since the end of 2001, was

adversely affected since May 2002 by concerns over corporate governance and accounting practices as well as weak stock performance in the United States. The *Kuala Lumpur Composite Index* (KLCI) moderated to 713 points on 2 September 2002 with a market capitalization of RM529 billion.

**KUALA LUMPUR STOCK EXCHANGE**  
Composite Index and Market Capitalization  
July 1997 - 2 September 2002



Comparison (in terms of local currency) with the other main international bourses shows that they too were affected by the bearish performance of the US stock market. However, as activities in the KLSE were driven more by domestic investors, the KLCI recorded a stable performance compared to the other major bourses. The KLCI is currently 4.5 per cent higher than the level recorded in the beginning of the year.

**PERFORMANCE OF SELECTED MAIN STOCK EXCHANGES**

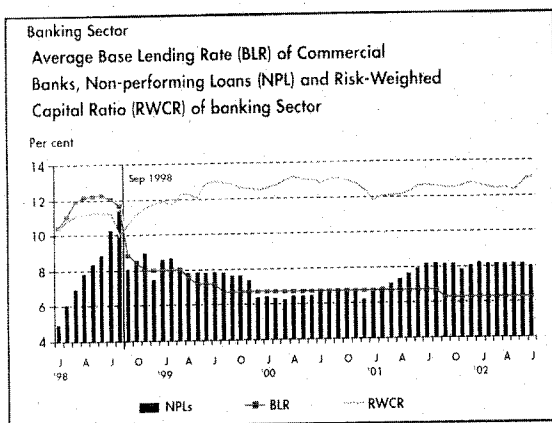
	% Change between index on 2 Sep '02 <sup>1</sup> and index on		
	1 Sep '98 <sup>2</sup>	10 Sep '01	2 Sep '02
• KLSE Composite Index	171.6	2.6	4.5
• Korea Composite Index	142.8	36.5	3.7
• Singapore ST Index	77.4	-6.3	-10.2
• Thailand SET	69.3	7.8	17.1
• Hong Kong Hang Seng	40.1	-4.5	-12.8
• Jakarta Composite Index	35.0	-0.8	14.7
• New York Dow Jones	10.7	-9.8	-14.0
• Philippines Composite Index	-7.8	-15.3	-6.1
• London FTSE 100	-19.1	-16.9	-19.9
• Tokyo Nikkei 225	-33.7	-6.6	-9.7

Note : 1/The KLSE CI was at 713.4 points

2/The KLSE CI declined to its lowest level at 262.7 points

The position of the banking system remained strong. The *Risk-Weighted Capital Ratio* (RWCR) in July 2002 strengthened to 13.1 per cent. The amount of *non-performing loans* (NPLs) as a ratio to total loans moderated to 8.0 per cent based on a 6-month classification in the same month, while the *base lending*

rate remained at 6.39 per cent since 30 September 2001. The base money supply (M1) expanded strongly by 12.2 per cent, while the broader money supply (M3) rose by 5.7 per cent in July 2002, consistent with the underlying economic activities.



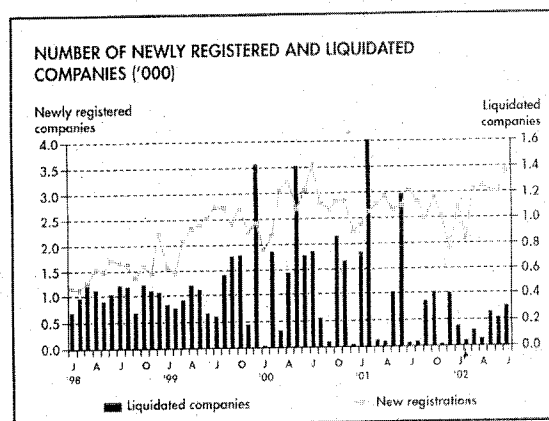
The progress of financial restructuring in the corporate sector continued satisfactorily. The proportion of non-performing loans (NPLs) that have been restructured or approved for restructuring remained at 99.9 per cent of NPLs under the purview of *Danaharta* (an asset management company to acquire and manage non-performing loans) as at 30 June 2002, with the average recovery rate of 57 per cent. In this regard, *Danaharta* is targeting for closure by 2005.

RESTRUCTURING PROGRESS OF THE BANKING SYSTEM AND CORPORATE SECTOR			
<b>Danaharta – Asset Management Company (30 Jun 2002)</b>			
• Acquired NPLs	...	RM47.7 bn	
• Restructured	...	RM47.7 bn	
• Average recovery rate on loans (%)	...		57%
<b>Danamodal – Special Purpose Vehicle (30 Jun 2002)</b>			
• Recapitalization of banks	...	RM7.6 bn	
• Repayment to Danamodal	...	RM5.5 bn	
<b>Corporate Debt Restructuring Committee (30 Aug 2002)</b>			
• Applications received	...	87 cases / RM67.6 bn	
• Withdrawn/rejected	...	28 cases / RM12.6 bn	
• Transferred to Danaharta	...	11 cases / RM2.5 bn	
• Resolved	...	47 cases / RM44.0 bn	
• Balance	...	1 case / RM8.6 bn	

Capital injection into the banking sector by *Danamodal* (a special purpose vehicle to recapitalize the banking system) remained at RM2.1 billion as at 30 June 2002 after a total of RM5.5 billion was repaid by the banking institutions.

The *Corporate Debt Restructuring Committee* or CDRC (a voluntary forum for debtors and financial institutions to work out debt) has officially ceased operations on 15 August 2002, after successfully resolving 98 per cent of cases accepted with the total value of RM44.0 billion. The remaining one case will be handled by *Danaharta*.

Restructuring activities in the corporate sector moderated as shown by the number of newly registered companies, which increased by 6.8 per cent on an annual basis to reach 20,600 companies, while that of liquidated companies fell by 71 per cent to 1,200 companies.

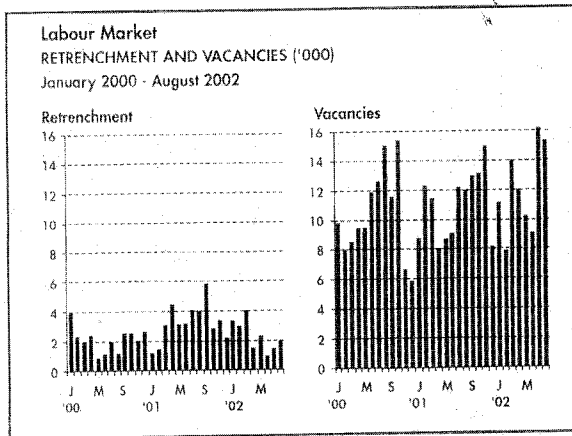


## Employment

Employment data shows a moderating trend in retrenchment after peaking in September 2001. The total number of retrenched workers fell by 25 per cent to slightly over 17,950 workers during the first eight months of this year. During the same period, a total of 95,700 vacancies were also created. The unemployment rate remained low at 3.7 per cent at the end of March 2002 (3.7 per cent at the end of 2001).

To address the issue of rising retrenchment, the Government has initiated 2 programmes in November of last year. Under the programme for retrenched workers and the unemployed, Government-funded training in various areas as well as allowances are provided. As of 31

July 2002, out of the 41,539 registered participants, a total of 36,168 participants are currently undergoing training. Under the programme for unemployed graduates, eight schemes were established, including training in languages as well as information and communications technology (ICT) skills, short-term attachment in government agencies and private firms, and facilities for further studies. A total of 28,938 graduates participated in the various schemes as of 31 July 2002.



## Federal Government Finance

Revenue collected by the Federal Government recorded an increase during the first half of 2002 to RM36.7 billion. If this trend continues, the total revenue collected this year might well surpassed the high record level registered last year of RM79.5 billion.

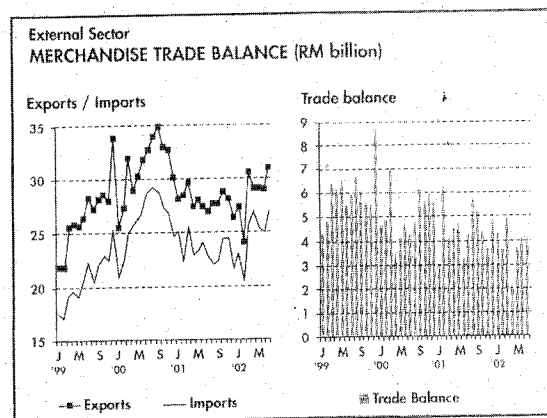
	2001				2002	
	Q1	Q2	Q3	Q4	Q1	Q2
• Revenue	14.6	20.7	18.5	25.7	17.1	19.6
• Operating expenditure	11.3	13.4	14.3	24.8	14.7	15.6
• Current balance	3.3	7.4	4.2	1.0	2.4	4.0
• Gross development expenditure	5.3	5.7	7.3	16.9	3.9	8.1
• Loan recoveries	0.4	0.1	0.2	0.3	0.2	0.1
• Net development expenditure	4.9	5.6	7.1	16.6	3.7	8.0
• Overall balance	-1.6	1.8	-3.0	-15.6	-1.3	-4.0
Memo item						
• Total Fed. Govt. debt (e.o.p.)	128.2	129.3	138.4	145.7	146.0	149.6

The budgetary operations of the Federal Government remained expansionary during

the second quarter. This reflected largely the faster implementation of projects to support economic recovery. As a result, the Federal Government recorded an overall fiscal deficit of RM4.0 billion in the second quarter of this year.

## External Sector

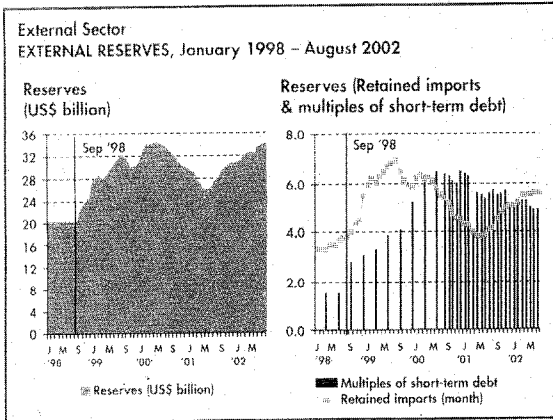
During the first 7 months of 2002, external trade continued to record a surplus of RM26.7 billion, compared with RM30.0 billion in the same period last year.



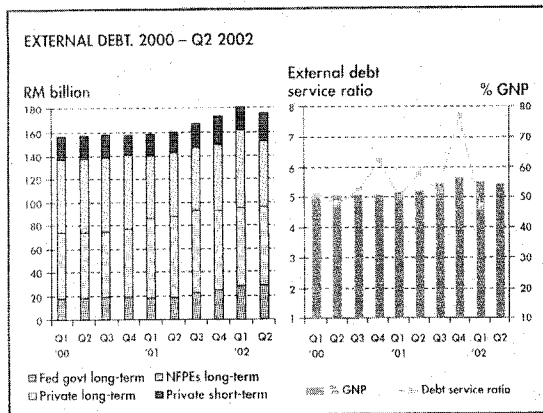
Exports, which contracted by 10.4 per cent last year, began to record positive growth since March 2002 with the recovery in the global electronics sector. During the January-July 2002 period, exports increased by 2.2 per cent, with a double-digit growth of 15 per cent recorded in July. Imports also has turned around since March 2002 to record a positive growth of 19 per cent in July.

	External Sector MAIN MANUFACTURED EXPORTS (% annual change)				
	2001	2001		2002	
		Q3	Q4	Q1	Q2
Total manufactured exports	-10.3	-20.4	-12.4	-4.0	5.5
• Electronics & electrical	-13.1	-23.7	-15.1	-3.1	7.0
• Chemicals	-0.9	-15.9	-2.5	-6.1	14.7
• Wood prod. & furniture	-12.5	-3.5	0.1	-8.5	7.7
• Metal products	0.9	-8.3	-8.0	-38.1	-16.2
• Petroleum products	4.6	-17.3	-14.2	-5.5	0.1
• Textiles, apparel etc	-13.2	-18.7	-19.6	-17.0	-14.0

The improved external demand led to the turnaround in manufactured exports, which expanded by 5.5 per cent in the second quarter of 2002. Electrical and electronics products, which made up two-thirds of total exports revenue, recorded a growth of 7.0 per cent during the same period, due to increased orders as expansion in major economies picked up.



Beginning June 2001, the net international reserves started to rise and has increased to RM130.1 billion (US\$34.2 billion) as at 31 August 2002. These unencumbered reserves were sufficient to finance 5.6 months of retained imports and were 5.1 times the amount of short-term external debt. The increase in reserves mainly reflected sustained trade surplus as well as inflows of foreign direct investment. These inflows more than offset the payment of services and overseas investment by Malaysian corporations.



Malaysia's external debt fell marginally to RM176.1 billion (US\$46.4 billion) as at end of

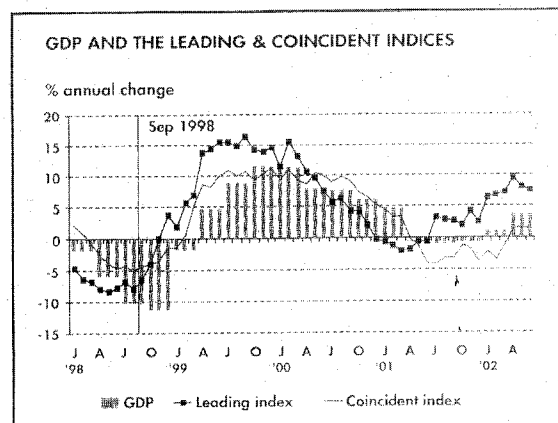
the second quarter of 2002, equivalent to 54.5 per cent of the GNP. The external debt service ratio is low at 4.7. In addition, short-term external debt made up only 13.7 per cent of the total external debt, thereby reducing Malaysia's external vulnerability to international interest rate and exchange rate developments abroad.

## Conclusion

With the turnaround in GDP growth during the first quarter of 2002 and the continued strengthening in the second quarter, prospects for the Malaysian economy remain favourable.

While the recent weakness in the global financial markets amidst the US corporate problems has raised concerns, policy response across the globe has been biased towards supporting recovery. In the US, although risk has risen, the balance of indicators suggests continued growth, but at a slower pace than earlier expected.

On the domestic front, the composite index of leading indicators registered the twelfth consecutive positive growth in June 2002, suggesting that the Malaysian economy is in its expansionary phase. The coincident index, an indicator of the current state of overall economic activities, showed a positive growth for the third straight month in June.



Therefore, barring any economic shocks, growth in the second half of the year is expected to be supported by continued expansion of domestic and external demand. Growth is also expected to take place in an environment of low inflation and unemployment. Both the current account in the balance of payments and the Federal Government account are estimated to be at sustainable levels.

*Economic Planning Unit  
Prime Minister's Department  
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**6 September 2002**