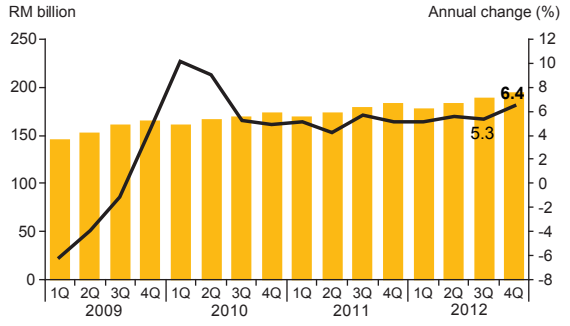
ECONOMIC AND FINANCIAL DEVELOPMENTS IN MALAYSIA IN THE FOURTH QUARTER OF 2012

OVERVIEW

Malaysian economy registered higher growth in the fourth quarter

Despite the challenging global economic environment, the Malaysian economy recorded a higher growth of 6.4% (3Q 12: 5.3%), supported by the continued strength in domestic demand. Total investment remained robust and was the main driver of growth during the quarter. The growth of private consumption continued to remain strong although the pace of increase moderated. The growth during the quarter also benefited from a significantly lower negative contribution from net exports. On the supply side, most economic sectors recorded improvements in growth during the quarter. For the year as a whole, the Malaysian economy expanded by 5.6%.

Higher growth in the fourth quarter
(at constant year 2005 prices)



Source: Department of Statistics, Malaysia

Domestic demand continued to expand at the pace of 7.5% (3Q 12: 11.4%) with gross fixed capital formation remaining strong, registering double-digit growth of 15% in the fourth quarter (3Q 12: 22.7%). Private sector investment advanced by 20.2% (3Q 12: 22.9%), supported by capital spending in the domestic-oriented manufacturing and consumer-related services sub-sectors, namely, telecommunications, real estate and aviation and the on-going implementation of projects in the oil and gas sector. Investment was also supported by capacity expansion in the primary-related manufacturing cluster and capital spending in new growth areas such as medical and communications equipment. Public investment expanded by 11.1% (3Q 12: 22.4%), driven by capital spending by public enterprises in the transportation, utilities, oil and gas and communications sectors.

Private consumption registered a growth of 6.1% in the fourth quarter (3Q 12: 8.5%), supported by stable labour market conditions and improved consumer sentiments. The stronger growth in the first half of the year reflected the effects of the various government transfers to households disbursed during the period. Public consumption grew by 1.1% (3Q 12: 2.3%), attributable to continued spending on emoluments amidst lower spending on supplies and services.

On the supply side, growth in most economic sectors improved in the fourth quarter. Growth was led by the manufacturing and services sectors, supported by domestic demand and a gradual improvement in the external environment. The agriculture sector expanded at a faster pace amidst higher crude palm oil output and production of poultry, while growth in the mining sector rebounded following a recovery in the production of natural gas. Meanwhile, growth in the construction sector continued to be robust, driven by the civil engineering and residential sub-sectors.

The headline inflation rate, as measured by the annual change in the Consumer Price Index (CPI), continued to moderate to 1.3% in the fourth quarter (3Q 12: 1.4%), reflecting lower inflation in the *food and non-alcoholic beverages* category.

In the external sector, the current account surplus increased in the fourth quarter to RM22.8 billion, equivalent to 6.6% of GNI, due to a larger goods surplus, a lower services deficit and net income payments. Meanwhile, the financial account sustained an outflow of RM9.0 billion, as net inflows of FDI and portfolio investments were offset by an increase in direct investment abroad. Consequently, the overall balance of payments turned around to record a surplus of RM5.9 billion (3Q 12: -RM7.5 billion).

The international reserves of Bank Negara Malaysia amounted to RM427.1 billion (equivalent to USD139.7 billion) as at 31 December 2012. This reserve level has taken into account the quarterly adjustment for foreign exchange revaluation changes. As at 31 January 2013, the reserves position amounted to RM428.6 billion (equivalent to USD140.2 billion), sufficient to finance 9.5 months of retained imports and is 4.6 times the short-term external debt.

Interest rates remained stable

The Overnight Policy Rate (OPR) was maintained at 3.00% during the fourth quarter of 2012. At this level of the OPR, monetary conditions remain supportive of economic activity.

Reflecting the unchanged OPR, the average interbank rate of all maturities was relatively stable. In terms of retail interest rates, the average quoted fixed deposit (FD) rates of commercial banks were relatively unchanged. The average base lending rate (BLR) of commercial banks remained unadjusted at 6.53%, while the weighted average lending rate (ALR) on loans outstanding moderated slightly to 5.52% as at end-December (end-September: 5.55%).

Total gross financing raised by the private sector through the banking system and the capital market was sustained at RM262.5 billion (3Q 12: RM272.9 billion). On a net basis, banking system loans and PDS outstanding expanded at an annual growth rate of 12.4% as at end-December (end-September: 12.8%).

Net funds raised in the capital market were higher at RM37.7 billion during the quarter (3Q 12: RM28.7 billion). The bulk of funds were raised by the private sector through new issuances of private debt securities. After adjusting for redemptions, net funds raised by the private sector amounted to RM20.1 billion (3Q 12: RM18.3 billion). Net funds raised by the public sector were RM17.6 billion in the fourth quarter (3Q 12: RM10.4 billion).

The monetary aggregates grew at a more moderate pace during the fourth quarter. M1, or narrow money, increased by RM15.4 billion during the period. On an annual basis, M1 expanded by 11.2% as at end-December (end-September 12: 12.3%). M3, or broad money, increased by RM15.2 billion on a quarterly basis to record an annual growth rate of 8.8% as at end-December (end-September 12: 12.5%). M3 continued to expand on account of the sustained credit extended to the private sector by the banking system. The placement of proceeds from the Government's fundraising activities and outflows of funds during the period, however, exerted a contractionary impact on broad money.

The ringgit appreciated against the US dollar supported by investor optimism over growth prospects for the region, including Malaysia. The uncertainty surrounding developments in the US economy, however, prompted some investors to unwind their holdings of emerging market assets, thus partially offsetting the ringgit appreciation during the quarter. Overall, the ringgit appreciated by 0.3% against the US dollar in the fourth quarter. The ringgit also appreciated against the Japanese yen (11.1%) and pound sterling (0.8%), but depreciated against the euro (-1.9%). The ringgit's performance against regional currencies was mixed.

Between 1 January and 18 February 2013, the ringgit appreciated against the Japanese yen (8.0%) and pound sterling (3.0%) but depreciated against the US dollar (-1.3%) and the euro (-2.2%). Against regional currencies, the ringgit strengthened against the Korean won and Singapore dollar by 0.2% and 0.1% respectively but depreciated against the Indonesian rupiah, Chinese renminbi, Philippine peso and Thai baht by between -0.9% and -3.6%.

Financial stability continued to be preserved

Financial stability was sustained throughout the quarter amidst continued challenges in the global environment. Stable financial conditions were underpinned by sound and well-capitalised financial institutions, orderly financial market conditions and sustained confidence in the financial system, which provided continued support for effective financial intermediation.

With strong level of capitalisation as core capital ratio and risk-weighted capital ratio improved to 13.4% (3Q 12: 13.2%) and 15.2% (3Q 12: 14.9%) respectively, the banking sector is well poised to withstand economic and financial shocks. The insurance sector also maintained a sound capital adequacy ratio of 222.3% (3Q 12: 218.6%) with excess capital buffer of RM22.5 billion.

Domestic economy to register growth, supported by firm domestic demand amidst gradual improvement in external environment

Going forward, there are emerging signs of improvements in the global economy. Latest economic indicators also suggest further stabilisation in the growth performance in Asia. Notwithstanding these improvements, considerable structural challenges remain in the advanced economies, which would constrain the prospect for a stronger economic recovery. In particular, several advanced economies will continue to address the issues relating to fiscal sustainability and persistently weak labour market conditions. In the emerging markets, the highly accommodative monetary policy sustained in the major advanced economies requires close surveillance given the potential impact of excessive global liquidity on asset price inflation.

For the Malaysian economy, the sustained expansion in domestic activity is expected to continue to drive growth, supported by the sustained private sector expansion. The stabilisation of external conditions is also expected to lend support to our economic growth prospects.