BANK NEGARA MALAYSIA
CENTRAL BANK OF MALAYSIA

SIARAN AKHBAR

Ref. No.: 05/15/06

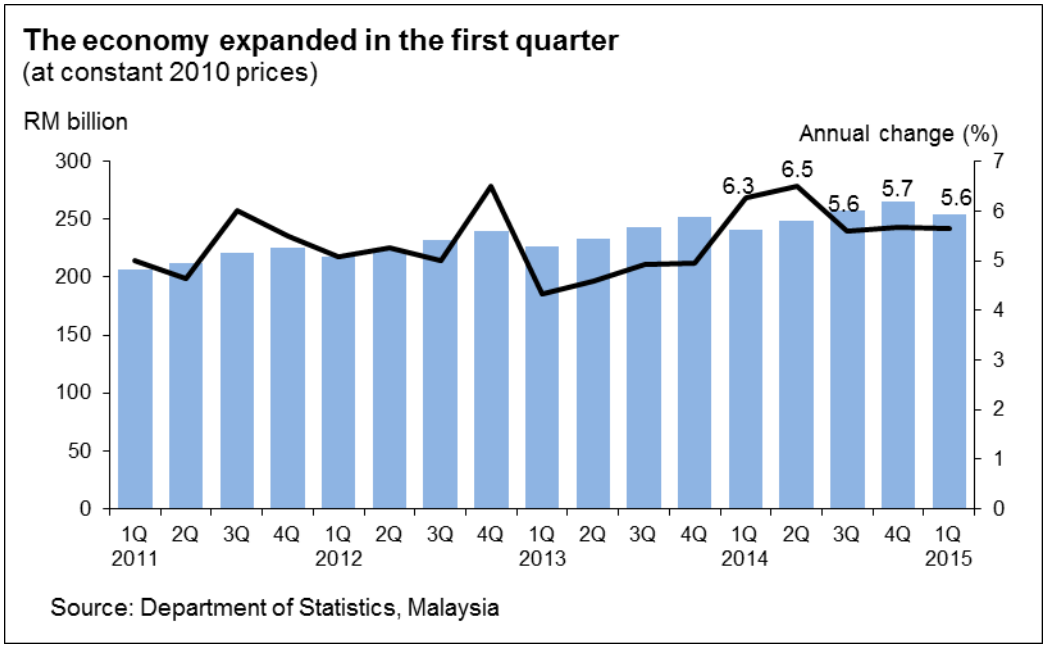
EMBARGO: Not for publication or broadcast before 1200 hours on Friday, 15 May 2015

ECONOMIC AND FINANCIAL DEVELOPMENTS IN MALAYSIA IN THE FIRST QUARTER OF 2015

OVERVIEW

The Malaysian economy grew by 5.6% in the first quarter of 2015

The global economic activity expanded with divergent growth momentum across economies in the first quarter of 2015. While the US economy registered broader improvements, the economic recovery in the euro area and Japan progressed at a more gradual pace. In Asia, growth was sustained by the continued expansion in domestic demand.



The Malaysian economy registered a growth of 5.6% in the first quarter of 2015 (4Q 2014: 5.7%), underpinned mainly by the private sector demand. On the supply side, growth was supported by the major economic sectors. On a

quarter-on-quarter seasonally-adjusted basis, the economy recorded a growth of 1.2% (4Q 2014: 1.8%).

Private sector activity remained the key driver of growth during the quarter. Private consumption expanded at a stronger pace of 8.8% (4Q 2014: 7.6%), supported by stable labour market conditions and higher wage growth. The strong private consumption growth was also contributed by the flood relief efforts early in the year, and the front-loading of household spending prior to the implementation of GST. Private investment recorded a growth of 11.7% (4Q 2014: 11.1%), underpinned by capital expenditure in the manufacturing and services sectors. Growth in public consumption improved in the first quarter (4.1%; 4Q 2014: 2.5%), due to higher growth in supplies and services amid moderate growth in emoluments. Public investment turned around to register a positive growth of 0.5% (4Q 2014: -1.9%) following higher capital spending by the Federal Government.

On the supply side, growth in the first quarter was supported by the major economic sectors. The services sector was underpinned by growth in all sub-sectors, particularly consumption-related sub-sectors. Growth in the manufacturing sector was supported by stronger performance in the export-oriented industries, particularly the electronics and electrical (E&E) cluster. The construction sector was supported mainly by the non-residential and residential sub-sectors, while the mining sector continued to record stronger growth amid higher crude oil production. Meanwhile, the agriculture sector contracted as a result of lower palm oil production, arising from flood-related disruptions.

Inflation, as measured by the annual change in the Consumer Price Index (CPI), averaged significantly lower at 0.7% in the first quarter of 2015 (4Q 2014: 2.8%). The lower inflation was mainly attributable to the decline in prices in the transport category (-7.6%; 4Q 2014: 4.8%), following the downward revision of domestic fuel prices in January and February amid lower global oil prices.

The trade surplus amounted to RM21.3 billion in the first quarter of 2015 (4Q 2014: RM21.5 billion). Gross exports contracted by 2.5% (4Q 2014: +0.5%), reflecting mainly a decline in the growth of commodity exports and resource-based manufactured exports, amid lower commodity prices. Gross imports moderated to a marginal growth of 0.2% (4Q 2014: 4.6%).

The international reserves of BNM amounted to RM389.7 billion (equivalent to USD105.1 billion) as at 31 March 2015. This reserve level has taken into account the quarterly adjustment for foreign exchange revaluation changes.

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As at 30 April 2015, the reserves position amounted to RM392.4 billion (equivalent to USD105.8 billion), sufficient to finance 8.0 months of retained imports and is 1.1 times the short-term external debt.

Interest rates remained stable

The Monetary Policy Committee (MPC) decided to maintain the Overnight Policy Rate (OPR) at 3.25% at its meetings during the first quarter of 2015. At the prevailing level of the OPR, monetary conditions remained supportive of economic activity. Reflecting the unchanged OPR, the average overnight interbank rate was relatively stable during the quarter. Interbank rates of longer maturities continued to be elevated in January, but subsequently moderated as funding pressures eased following BNM's announcement on 30 January 2015 on the arrangements to facilitate transition to the full implementation of the Liquidity Coverage Ratio (LCR) by 2019. For the quarter as a whole, 3-month KLIBOR decreased from 3.86% to 3.73%. In terms of retail rates, both deposit and borrowing cost to the economy were broadly stable throughout the quarter. On 2 January 2015, the Base Rate (BR) replaced the base lending rate (BLR) as the main reference rate for new retail floating rate loans and financing facilities. Upon introduction, the average BR of banks stood at 3.90% where it remained as at 31 March 2015.

The monetary aggregates continued to expand in the first quarter. M3, or broad money, increased by RM35.9 billion on a quarter-on-quarter basis to record an annual growth rate of 7.9% as at end-March (end-December 2014: 7.0%). The increase in M3 during the quarter was driven mainly by the continued expansion in credit extended to the private sector by the banking system and lower net foreign assets. The expansion in broad money, however, moderated somewhat following lower net claims on the Government. In the banking system, liquidity conditions remained ample at both the institutional and system-wide levels. The level of surplus liquidity placed with BNM was marginally lower during the quarter due to external sector outflows.

Total gross financing raised by the private sector through the banking system and the capital market amounted to RM282.5 billion (4Q 2014: RM309.8 billion). On a net basis, outstanding banking system loans and PDS expanded by 8.3% as at end-March (end-December 2014: 8.8%). Loan disbursement to businesses during the quarter remained healthy, with higher level of credit extended mainly to the *finance, insurance and business services; mining and quarrying;* and *education, health and others* sectors on an annual basis. In particular, financing for SMEs continued to be strong, with outstanding SME loans growing at 17.2% as at end-March (end-December 2014: 14.0%). Outstanding household loans growth remained stable at 9.8% as at end-

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March (end-December 2014: 9.9%). Net funds raised in the capital market moderated to RM21.0 billion in the first quarter (4Q 2014: RM26.4 billion).

The ringgit and other regional currencies continued to face volatility in the first quarter due to uncertainty in global monetary conditions, which led to portfolio investment outflows. Overall, the ringgit depreciated by 6.0% against the US dollar during the quarter. Against other major currencies, the ringgit appreciated against the euro (5.9%) and the Australian dollar (1.2%) but depreciated against the pound sterling (-1.0%), and the Japanese yen (-5.3%). Against regional currencies, the ringgit depreciated by between 1.0% and 7.0%.

Between 1 Apr and 13 May 2015, the ringgit appreciated against the US dollar by 3.1%. The ringgit also appreciated against the Japanese yen (2.8%), but depreciated against the euro (-0.9%), the Australian dollar (-1.5%) and the pound sterling (-2.8%). The ringgit appreciated against most regional currencies.

Domestic financial stability continued to be preserved

Financial system resilience remained intact amid continued volatile financial and commodity market conditions during the quarter. Financial intermediation activities were well-supported by sound financial institutions, orderly financial market conditions and continued ample domestic liquidity. Domestic financial system stability is expected to be maintained and this will continue to support sustained growth of the domestic economy.

The strong capitalisation of the banking system was well-preserved with the common equity tier 1 (CET1) capital ratio, tier 1 capital ratio and total capital ratio remaining well above the minimum regulatory levels at 12.5%, 13.2% and 15.2% respectively. More than 80% of banks' total capital consists of high quality capital, that is, retained earnings, paid-up capital and reserves. The excess total capital buffer for banks was sustained in excess of RM90 billion. The capital adequacy ratio of the insurance sector similarly remained strong at 246.5% (4Q 2014: 252.1%) with an excess capital buffer of RM30.1 billion.

Domestic demand will remain the key driver of growth

Moving forward, global economic growth is projected to improve at a moderate pace, but with diverging growth momentum across major economies. Although lower oil prices will have varying impact on economies, overall global growth is expected to benefit from this development. Downside risks to the growth outlook continue to persist, arising from the prolonged weakness in domestic demand and low inflation in a number of major economies, concern on the growth prospects of several net commodity-

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exporting emerging economies and the re-emergence of geopolitical tensions, which could heighten financial market volatility.

The Malaysian economy is expected to remain on a steady growth path. Domestic demand will remain the key driver of growth amid the lower oil prices. Investment activity is projected to remain resilient, with continued capital spending by both the private and public sectors. While private consumption is expected to moderate as households adjust to the introduction of the Goods and Services Tax (GST), the steady rise in income and stable labour market conditions would support household spending. The recovery in global growth while remaining moderate, will provide support to manufactured exports, although lower commodity prices will likely weigh down on overall exports.

Bank Negara Malaysia
15 May 2015

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GDP by Economic Activity (at constant 2010 prices)

	Share 2014 (%)	2014			2015
		1Q	4Q	Year	1Q
		Annual change (%)			
Agriculture	9.2	2.6	-3.7	2.1	-4.7
Mining	9.0	-0.1	9.5	3.3	9.6
Manufacturing	23.0	7.0	5.4	6.2	5.6
Construction	4.3	19.3	8.8	11.8	9.7
Services	53.5	6.7	6.6	6.5	6.4
Real GDP	**100.0**[1]	**6.3**	**5.7**	**6.0**	**5.6**
Real GDP (q-o-q seasonally adjusted)	**-**	**1.4**	**1.8**	**n.a.**	**1.2**

[1] Numbers do not add up due to rounding and exclusion of import duties component

Source: Department of Statistics, Malaysia

GDP by Expenditure Components (at constant 2010 prices)

	Share 2014 (%)	2014			2015
		1Q	4Q	Year	1Q
		Annual change (%)			
Aggregate Domestic Demand (excluding stocks)	91.5	7.6	5.7	5.9	7.9
Private Sector	68.5	8.9	8.3	7.9	9.6
Consumption	*51.8*	*7.0*	*7.6*	*7.0*	*8.8*
Investment	*16.6*	*14.9*	*11.1*	*11.0*	*11.7*
Public sector	23.0	3.6	0.6	0.4	2.5
Consumption	*13.6*	*12.2*	*2.5*	*4.4*	*4.1*
Investment	*9.5*	*-6.3*	*-1.9*	*-4.7*	*0.5*
Net Exports	9.3	8.2	-4.0	12.8	-10.2
Exports of Goods and Services	*76.1*	*7.9*	*1.9*	*5.1*	*-0.6*
Imports of Goods and Services	*66.8*	*7.8*	*2.6*	*4.2*	*1.0*
GDP	**100.0**	**6.3**	**5.7**	**6.0**	**5.6**
GDP (q-o-q growth, seasonally adjusted)	**-**	**1.4**	**1.8**	**-**	**1.2**

Source: Department of Statistics, Malaysia