DEVELOPMENTS IN THE MALAYSIAN ECONOMY

Sustained growth momentum reflecting underlying strength in the economy

Real GDP expanded by 5.8% (2Q: 6.2%) in the third quarter of 2006, indicating underlying strength in the economy. The growth was supported by sustained growth in the services and manufacturing sectors, and higher growth in the agriculture sector. Growth in the manufacturing sector was reflected by expansion in export-oriented industries and improvement in the domestic-oriented industries. Meanwhile, growth in the services sector was broad based, supported by continued consumer demand, tourism, finance and trade-related activities. Similarly, growth in the agriculture sector was supported by a wide range of activities, including the key industrial crops such as palm oil and rubber as well as food-based commodities such as paddy, fish, fruits and vegetables, induced by weather-related factors and attractive commodity prices. Construction activity remained stable, while the mining sector declined due to lower crude oil production.

Quarterly GDP by Kind of Economic Activity at 1987 Prices

	2005		2006		
	3Q	4Q	1Q	2Q	3Q
	Annual Change (%)				
Agriculture	1.7	-1.5	7.4	5.6	6.2
Mining	3.4	-2.0	-1.3	-1.2	-1.2
Manufacturing	3.5	7.9	8.5	8.4	7.1
Construction	-1.4	-0.6	-1.8	-0.5	-0.4
Services	7.3	5.9	5.9	6.6	6.5
Real GDP (Ann. Chg.)	**5.3**	**5.2**	**5.9**	**6.2**	**5.8**
Real GDP (Preceding Chg.)	**3.8**	**1.8**	**-2.2**	**2.7**	**3.3**

Source: Department of Statistics, Malaysia

Sustained strength in services activities

The services sector continued to expand at a strong pace of 6.5% (2Q: 6.6%) propelled by domestic consumption, tourism, finance and trade-related activities resulting in a broad-based expansion across the sub-sectors.

Of significance, growth in the **finance, insurance, real estate and business services** sub-sector picked up to 7.5% (2Q: 6.7%) during the quarter. Both conventional and Islamic banking activity remained strong supported by lending and fee-based activities, while insurance activities picked up strongly mainly supported by investment-linked products. Growth was further augmented by real estate and business services activities, including IT-related services, benefiting from the 66 new MSC-status companies coming into operation during the quarter (2Q: 30), including 5 shared services and outsourcing (SSO) companies (2Q: 11).

The **wholesale and retail trade, hotels and restaurants** sub-sector grew by 5.8% (2Q: 6.5%) reflecting continued support from domestic spending amidst the increase in consumer sentiment during the quarter. Activities in the distributive trade sector, other than the motor vehicle segment, was supported by the Mega Sales Carnival held during the period 22 July–3 September, and also by the preparations for the up-coming major festivals in the final quarter of the year. Pick-up in tourism activities, particularly tourists from the Middle East during their summer vacation months further supported the retail and hospitality segments, particularly in the main cities and tourist areas. The distributive trade activities in the motor vehicle segment, however, remained sluggish, due to weak demand for new vehicles which was affected by the low trade-in value of second-hand vehicles.

Growth in the **transport, storage and communication** sub-sector trended higher to 7.1% (2Q: 6.7%) mainly reflecting better performance in the transportation segment, and sustained growth in the telecommunication segment. The transportation industry benefited from higher trade and port-related activities. Growth in the telecommunications industry was sustained at a strong pace driven by increased demand from IT-related services, including SSO, as well as increased subscriber base for the

cellular and broadband segments and higher usage of data and voice services in the cellular segment.

Performance in the Services Sector (Value Added)

	Share 2005	2005		2006		
		3Q	4Q	1Q	2Q	3Q
	%	Annual change (%)				
Intermediate Services	**41.5**	**5.9**	**5.5**	**5.4**	**6.7**	**7.4**
Transport, storage & communication	15.1	4.3	4.9	4.5	6.7	7.1
Finance, insurance, real estate & business services	26.4	6.9	5.8	6.0	6.7	7.5
Final Services	**58.5**	**8.2**	**6.1**	**6.2**	**6.5**	**5.8**
Electricity, gas & water	7.1	6.5	3.7	4.2	3.4	5.2
Wholesale & retail trade, hotels & restaurants	25.2	9.9	7.0	6.1	6.5	5.8
Government services	12.8	9.0	7.4	9.3	10.4	7.9
Other services	13.3	5.4	4.6	4.6	4.5	4.2
Total Services	**100**	**7.3**	**5.9**	**5.9**	**6.6**	**6.5**

Source: Department of Statistics, Malaysia

The **utilities** sub-sector recorded a higher growth of 5.2% (2Q: 3.4%), due to higher electricity generation supported mainly by increased demand from the commercial segment due to the World Cup event and extended retail hours during the Mega Sales carnival which took place during the quarter. The **Government services** sub-sector was supported by increases in emoluments and allowances paid, in addition to the bonuses accrued to the civil servants.

Selected Quarterly Indicators in the Services Sector

	2005		2006		
	3Q	4Q	1Q	2Q	3Q
	Percentage at end-period (%)				
Cellular phone penetration rate	66.8	74.1	77.7	80.8	81.6
Internet subscribers penetration rate	13.8	13.9	13.9	14.0	14.0
Broadband subscribers penetration rate	1.7	1.9	2.2	2.5	2.8
	Annual change (%)				
Total passenger traffic at all airports	5.6	1.9	6.5	2.8	-0.03
Total consumption credit outstanding	18.6	18.7	18.8	21.0	17.0
Loan outstanding to the wholesale & retail trade, hotels & restaurants	12.6	8.3	7.3	9.0	11.5
Imports of consumption goods	5.2	4.2	14.0	12.8	15.3
Total sales of passenger cars	1.5	13.6	-9.5	-6.2	-7.0
Total sales of commercial vehicles	50.2	16.5	25.2	-10.2	-15.0
SMS traffic	143.3	156.3	118.9	53.4	36.6
Total cargo handled at all airports	0.6	6.2	10.7	6.0	4.9
Container cargo handled (Port Klang and PTP)	5.2	7.8	7.8	13.9	15.7

Source: Various sources

Manufacturing sector continued to expand

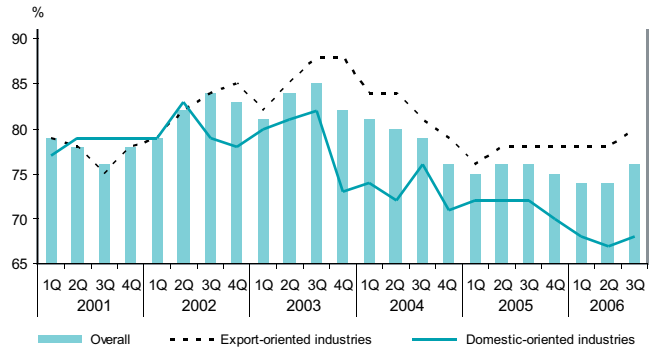
Value-added growth in the **manufacturing sector** expanded by 7.1% (2Q: 8.4%), reflecting the expansion in export-oriented industries and further improvement in domestic-oriented industries. The overall capacity utilisation rate of the manufacturing sector averaged at 76% during the quarter (2Q: 74%), with the export-oriented and domestic-oriented industries operating at 80% and 68% respectively (2Q: 78% and 67% respectively).

In the **export-oriented industries,** the growth of 6.3% (2Q: 9.6%), was mainly supported by selected resource-based industries. Meanwhile, the E&E industry registered a growth of 5.4% during the quarter (2Q: 8.3%) reflecting sustained growth in semiconductors and a more moderate growth in computers and computer peripherals. Among the resource-based industries, output of rubber products grew at a stronger pace of 13.9% (2Q: 8.6%), supported by the strong external demand for rubber gloves, which more than offset the sluggish performance in the tyre segment due to the ongoing conversion to higher value-added products. In addition, the petroleum products and the off-estate processing industries increased by 18.5% (2Q: 15.5%) and 10% (2Q: 7.2%) respectively. The latter was in line with the upward trend in output of primary commodities such as crude palm oil and rubber.

At the same time, the **domestic-oriented industries** showed a discernable improvement during the quarter, increasing at a double-digit growth of 12.1% (2Q: 5.3%), as a result of the combined effects of the turnaround in construction-related materials industry (8%; 2Q: -0.6%) as well

as the robustness of the fabricated metal products (35.9%; 2Q: 24.4%) and food-related products industries (15.3%; 2Q: 3.7%). The strong growth rates in these industries more than offset the contraction in transport equipment industry (-4.3%; 2Q: 3.9%) which continued to be affected by the lackluster demand for new passenger cars. The output of glass and metal products was supported by both domestic and external demand, while the food and beverage sectors showed a significant growth as manufacturers prepared for year-end festivities.

Capacity Utilisation in the Manufacturing Sector



Performance in the Manufacturing Sector

	2005		2006		
	3Q	4Q	1Q	2Q	3Q
	Annual change (%)				
Value Added (Constant Price)	**3.5**	**7.9**	**8.5**	**8.4**	**7.1**
Overall Production	**4.7**	**8.2**	**8.9**	**8.7**	**7.4**
Export-oriented industries	**5.7**	**10.1**	**10.8**	**9.6**	**6.3**
Of which:					
Electronics and electrical	3.3	10.5	17.3	8.3	5.4
Chemicals and chemical products	13.1	16.8	5.6	10.8	-1.4
Petroleum products[1]	10.8	11.5	8.7	15.5	18.5
Textiles, wearing apparel & footwear	12.7	10.3	10.6	14.5	1.9
Wood and wood products [2]	1.4	3.1	3.3	-1.3	4.5
Rubber products	-4.0	-1.6	-7.3	8.6	13.9
Off-estate processing	2.0	-4.6	-4.9	7.2	10.0
Domestic-oriented industries	**0.7**	**0.4**	**1.1**	**5.3**	**12.1**
Of which:					
Non-metallic mineral products	-1.6	1.5	-5.1	1.2	7.9
Iron & steel and non-ferrous metal	-7.1	-13.4	-9.8	-4.1	8.2
Food	7.7	4.8	-1.6	3.7	15.3
Transport equipment	6.5	6.7	6.6	3.9	-4.3
Fabricated metal products	-5.6	-5.7	15.2	24.4	35.9
Total Manufactured Exports	**6.3**	**13.1**	**10.6**	**10.0**	**14.2**
Of which:					
Electronics and electrical products	6.8	14.7	8.4	5.6	10.3
Chemical and chemical products	1.3	4.5	-6.9	9.9	22.4
Petroleum products	19.4	20.6	40.3	39.0	31.8
Optical & scientific equipment	-0.7	12.4	7.9	5.2	24.3
Wood and wood products	-14.9	6.6	-3.7	10.0	34.3
Furniture & parts	3.0	0.8	8.0	5.4	10.5
Rubber products	10.0	18.7	17.7	38.4	46.3

[1] Under the new Industrial Production Index (2000=100), LNG has been reclassified as petroleum products (previously classified as chemicals and chemical products). Consequently, petroleum products have been reclassified as export-oriented industries.
[2] Output of furniture and parts are not captured in the wood production data.

Source: Department of Statistics, Malaysia

Broad based strengthening in agriculture, while the mining sector declined

The agriculture sector continued on its strong growth momentum for the third consecutive quarter, rising by 6.2% (1Q: 7.4%; 2Q: 5.6%), underpinned by a wide range of activities including palm oil, rubber, paddy, fisheries, fruits and vegetables. The mining sector, meanwhile, declined by 1.2% (2Q: -1.2%) due entirely to lower output of crude oil.

In the **agriculture sector, crude palm oil production** reached a new high of 4.52 million tonnes during the quarter, surpassing the previous peak of 4.09 million tonnes recorded in the corresponding period of 2004. The strong expansion of 10.6% (2Q: 7.4%) was largely due to an encouraging rise in yields of fresh fruit bunches (FFB) at 5.66 tonnes per hectare (2Q: 5.14 tonnes per hectare) induced by the favourable weather conditions which accelerated harvesting activities. Similarly, output of **natural rubber** strengthened further to record higher growth of 8.1% (2Q: 7.6%), as rubber prices, while levelling off from the record high of 895 sen per kilogramme seen in the first week of July 2006, continued to remain attractive, averaging 760 sen per kilogramme. The high prices have motivated increased tapping activities, especially among smallholders who dominate the sector, to use modern technologicies such as Low Intensity Tapping System (LITS) to raise yields.

Performance in the Agriculture Sector

	2005		2006		
	3Q	4Q	1Q	2Q	3Q
	Annual change (%)				
Value Added (at 1987 prices)	**1.7**	**-1.5**	**7.4**	**5.6**	**6.2**
Production[1]					
Of which:					
Crude palm oil	0.2	-6.0	-5.4	7.4	10.6
Crude palm kernel oil	7.8	-5.4	-8.9	6.7	11.5
Rubber	4.4	-3.8	24.7	7.6	8.1
Fish	-5.6	-1.7	8.0	9.3	5.9
Livestock	4.4	30.4	22.7	16.9	9.8
Cocoa	-19.0	-7.8	24.1	52.4	17.8
Exports (RM million)	**-0.1**	**3.2**	**4.5**	**3.3**	**20.4**
Of which:					
Palm oil					
('000 tonnes)	4.0	-0.2	2.7	-4.9	11.4
(RM/tonne)	-13.5	-8.2	-4.6	1.0	11.7
(RM million)	-10.0	-8.4	-2.0	-4.0	24.5
Palm kernel oil					
('000 tonnes)	-14.3	-2.1	-45.8	-23.3	58.7
(RM/tonne)	-5.8	-12.4	-12.4	-19.6	-10.1
(RM million)	-19.2	-14.2	-52.6	-38.3	42.7
Rubber					
('000 tonnes)	4.4	-0.2	3.0	5.1	-4.1
(Sen/kilogramme)	13.0	28.7	43.9	53.9	59.5
(RM million)	18.0	28.4	48.2	61.7	53.0
Sawn timber					
('000 cu.metres)	9.1	-0.8	-19.6	-15.1	-8.0
(RM/cu.metre)	5.7	23.5	37.2	17.6	11.1
(RM million)	15.3	22.4	10.3	-0.1	2.2
Saw logs					
('000 cu.metres)	-4.4	1.6	-19.4	-23.0	-21.6
(RM/cu.metre)	14.7	17.0	18.1	9.9	7.7
(RM million)	9.7	18.8	-4.8	-15.4	-15.6
Cocoa beans					
('000 tonnes)	-77.6	-5.6	101.1	1.6	321.3
(RM/tonne)	18.6	3.5	0.1	1.4	4.4
(RM million)	-73.4	-2.3	101.2	3.1	339.8

[1] In '000 tonnes, except for saw logs in '000 cubic metres and livestock in numbers slaughtered (Peninsular Malaysia only)

Source: Malaysian Palm Oil Board (MPOB)
Malaysian Rubber Board (MRB)
Fisheries Department, Malaysia
Malaysian Cocoa Board (MCB)
Veterinary Services Department, Malaysia
Department of Statistics, Malaysia

Growth was also experienced in the 'other agriculture' subsectors, particularly paddy, fish, fruits, vegetables and cocoa. Output of **fish** rose by 5.9% to 403,317 tonnes, due mainly to increase in marine landings, while **fruits, vegetables** and **paddy** output increase was supported by weather-related factors.

Performance in the Mining Sector

	2005		2006		
	3Q	4Q	1Q	2Q	3Q
	Annual change (%)				
Value Added (at 1987 prices)	**3.4**	**-2.0**	**-1.3**	**-1.2**	**-1.2**
Production					
Of which:					
Crude oil and condensates	-5.7	-6.1	1.9	0.2	-3.5
('000 barrels)					
Natural gas (net)	15.9	-0.6	-6.0	-3.0	3.5
(million standard cubic feet)					
Exports (RM million)	**25.8**	**20.2**	**23.0**	**10.1**	**1.3**
Of which:					
Crude oil and condensates					
('000 tonnes)	-9.4	8.6	-7.3	-5.3	-15.8
(USD/barrel)	43.6	26.3	40.8	31.0	16.9
(RM million)	29.0	36.3	28.1	19.2	-4.1
Liquefied natural gas					
('000 tonnes)	5.7	-1.7	-2.6	-8.5	1.8
(RM/tonnes)	16.8	17.6	19.6	15.2	13.0
(RM million)	23.4	15.5	16.4	5.4	15.0

Source: PETRONAS
Department of Statistics, Malaysia

Cocoa production strengthened again for the third straight quarter by 17.8% to 4,683 tonnes, due to fewer incidences of the black pod infection.

The **mining sector** was affected by the lower production of crude oil, while the production of natural gas rose during the quarter. Output of crude oil (including condensates) fell by 3.5% to 695,289 barrels per day (2Q: +0.2% to 657,423 bpd), due to a scheduled shutdown of an oil field for maintenance purpose. Meanwhile, production of natural gas rose by 3.5% to 5,550 million standard cubic feet per day (2Q: -3%) supported by higher external demand from the major importing countries.

Construction activity remained stable

Construction activity remained stable during the quarter, with the sector registering a mild decline of 0.4%. The performance was reflected by a more modest contraction in the civil engineering sub-sector. Activity in the non-residential sub-sector was influenced by renewed interest in commercial and mixed development in line with business activities, while the residential sub-sector was supported by demand in prime locations. Going forward, the construction sector is expected to benefit from the acceleration of projects under the Ninth Malaysia Plan.

Construction Indicators

	2005		2006		
	3Q	4Q	1Q	2Q	3Q
	Annual change (%)				
New sales and advertising permits	45.4	11.4	-23.6	-20.3	-21.7
Housing approvals	2.8	2.8	-43.4	-7.4	-12.6
Production of construction-related materials	-3.5	-3.8	-6.6	-0.6	8.0
Loans approved for construction	-7.3	3.4	-33.0	5.5	8.2
Imports of construction materials and mineral products	-23.7	0.2	2.6	-0.8	37.3[1]

[1] July-August 2006
Source: Ministry of Housing and Local Government and Department of Statistics, Malaysia.

GDP by Expenditure Components (at constant 1987 prices)

	2005		2006		
	3Q	4Q	1Q	2Q	3Q
	Annual change (%)				
Aggregate Domestic Demand (excluding stocks)	9.2	7.2	8.1	7.4	6.0
Consumption	9.0	9.9	6.8	7.3	7.1
Private sector	10.4	9.0	7.5	7.3	6.8
Public sector	4.7	12.6	3.8	7.2	8.3
Gross Fixed Capital Formation	9.6	0.4	11.4	7.6	3.5
Exports of Goods and Services	5.8	9.7	5.9	4.9	10.5
Imports of Goods and Services	8.2	8.0	10.8	7.7	7.4
GDP	**5.3**	**5.2**	**5.9**	**6.2**	**5.8**

Source: Department of Statistics, Malaysia

Domestic demand

The private sector continued as the main contributor to domestic demand activities in the third quarter. The public sector remained supportive of growth, with public sector spending showing clear signs of improvement during the third quarter.

The growth in consumption expenditure was sustained at 7.1%. **Private consumption** expenditure in the third quarter, increased by 6.8%. Consumer spending was supported by stable labour market conditions, stronger export earnings and firm commodity prices. In the labour market vacancies remained high amid lower retrenchments. The stronger performance of the stock market during the quarter has also created a positive wealth effect on consumers. Furthermore, various promotions held during the annual nationwide Mega Sales Carnival from end July to early September have encouraged household spending.

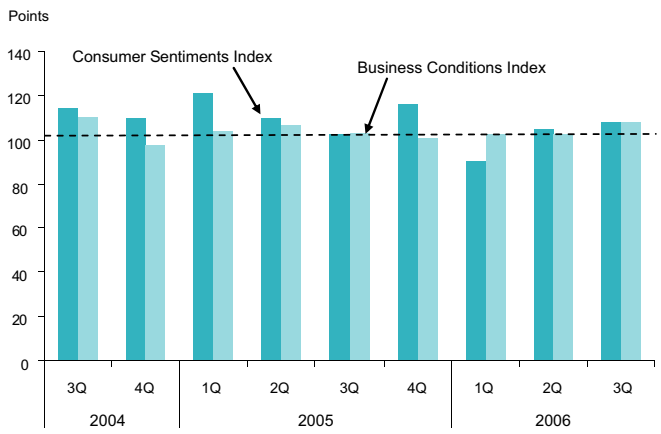
Latest data show that households have taken a more optimistic view going forward. The Consumer Sentiment Index rose further in the third quarter to 107.5 points (2Q: 104.2 points), mainly reflecting households' anticipation of stable incomes and better employment opportunities. Major consumption indicators such as imports of consumption goods and consumer spending on credit cards continued to register sustained growth, reflecting sustained consumer spending. In addition, the OPR had been left unchanged during the quarter, further mitigating the concerns of higher financing costs.

Meanwhile, **public consumption** registered a stronger growth of 8.3% during the quarter, mainly due to higher expenditure on emoluments, supplies and services and defence.

Private investment activities and increased public development spending supported the growth of 3.5% in **gross fixed capital formation.** Private sector capital spending activities were supported by the more favourable business sentiments and

higher capacity utilisation in the manufacturing sector. Improved business sentiment was reflected in the Business Conditions Index for the third quarter, which increased by 5.4 points from the previous quarter (107.8 points, 2Q: 102.4 points) as a result of stronger production activities, rising sales, higher export orders and higher outlays on new plant and equipment. At the same time, Federal Government development expenditure increased with the bulk of the expenditure during the quarter being channelled into agriculture and rural development; education and public utilities.

Improved Business and Consumer Confidence

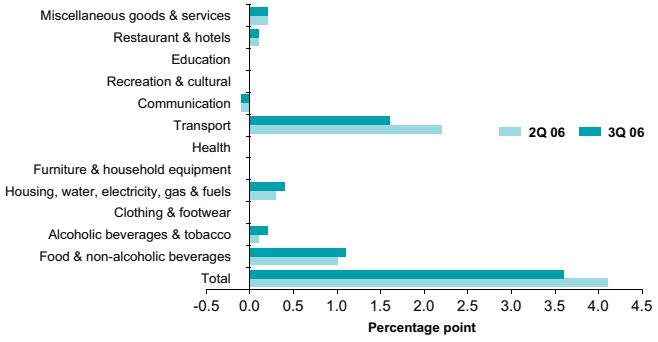


Inflation moderated in the third quarter

For the third quarter of 2006, headline inflation, as measured by the Consumer Price Index, moderated to 3.6% (2Q: 4.1%). As expected, the moderation was due mainly to the lower inflation for items in the transport category (3Q: 10%, 2Q: 13.9%) following the lapse of the August 2005 upward revision in the prices of retail petrol and diesel. The inflation rate for alcoholic beverages and tobacco was higher following the increase in excise duties on these items as announced in the 2007 Budget in September 2006. Meanwhile, the prices of clothing and footwear and communication charges continued to decline compared to levels recorded a year ago. For the first nine months of the year, the headline inflation rate averaged at 3.8% (2.9% during the corresponding period in 2005). This trend has continued in the fourth quarter with inflation moderating further to 3.1% in October.

The DOSM announced a rebasing of the Producer Price Index (PPI) to the year 2000 (previously 1989=100). This exercise also involved the revision of the weights of items in the PPI basket. Based on the new weights, the rate of increase of the PPI moderated to 6.4% in the third quarter (2Q: 7.7%) due to the slower increase in the commodity-related category. In particular, the prices of crude oil and rubber moderated during the quarter to bring down the producer price inflation.

Contribution to Consumer Price Inflation

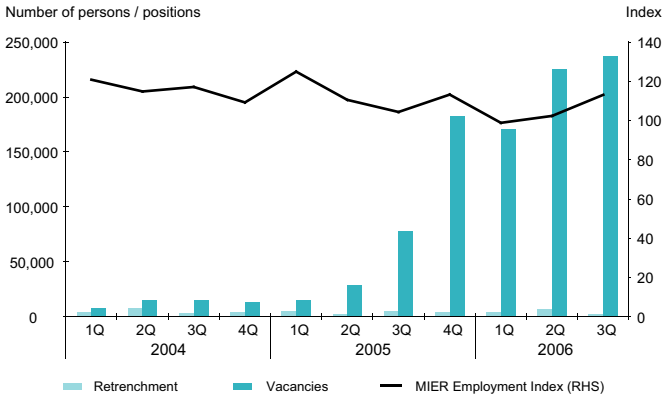


Effective from January 2006, the base reference period for the CPI series is year 2005=100

Stable labour market conditions

The latest data showed that the labour market continued to be stable as job vacancies remained high while retrenchments declined significantly. These positive developments were also reflected in the Employment Index, which climbed by 10.8 points to 113.2 points in the third quarter.

Labour Market Conditions



Total job vacancies reported via the Electronic Labour Exchange surged to 237,407 positions, (2Q: 225,863 positions); with the greatest number of openings reported in the manufacturing (41% share), agriculture (24%), services (17%) and construction (15%) sectors. However, most of the vacancies reported via the Exchange continued to be for lower level job categories, such as elementary occupations (61%), as employers still prefer to go through private employment agencies and/ or advertise in the print media to fill vacancies requiring higher expertise, talent and skills. Total retrenchments during the quarter were sharply lower, with only 2,497 persons being retrenched (2Q: 6,602 persons), in line with the sustained strong demand for labour. The retrenchments mainly affected plant and machine operators and assemblers, general workers, and craft and related trade workers (40% share). About 60% of the layoffs occurred in the manufacturing sector, with one-third of this group comprising of workers from the electronics and electrical industry.

After two quarters of negative growth, real labour productivity in the manufacturing sector recovered in the third quarter (0.7%; 2Q: -2.2%). Growth in real sales value of product per employee was also significantly higher than that of real wages, which continued to decline further (-2.3%; 2Q: -2.1%), indicating limited wage pressures in the manufacturing sector during the period.

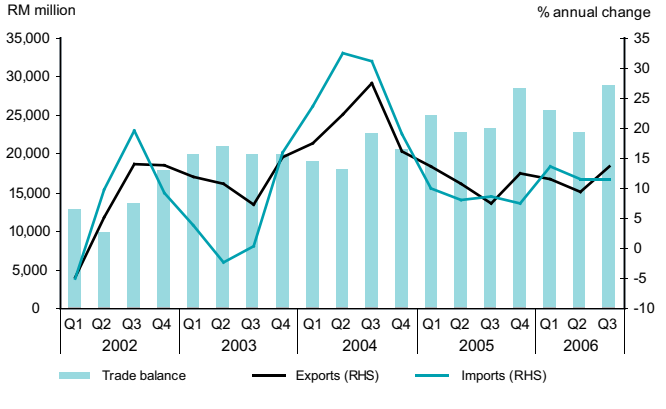
Stronger export growth

In line with strong expansion in manufactured and agriculture exports, the trade account registered a **surplus** of RM28.9 billion in the third quarter of 2006 (2Q: RM22.9 billion). Gross exports expanded by 13.6% (2Q: 9.5%) while import growth was sustained at 11.5% (2Q: 11.5%).

In the third quarter of 2006, gross exports strengthened significantly by 13.6% (2Q: 9.5%) due to higher exports of manufactured goods and agriculture. Meanwhile, exports of minerals grew at a more moderate pace.

Exports of manufactured goods increased by 14.2% (2Q: 10%) mainly supported by exports of E&E and resource-based products. Higher shipment

Trade Balance



of electrical products, in particular telecommunication equipment continued to drive the better export performance of E&E products (10.3%; 2Q: 5.6%). Exports of semiconductors also contributed to the stronger export growth, which is in line with the performance of the global semiconductor industry where unit shipments of microprocessors have increased due to introduction of new products.

Meanwhile, exports of resource-based products continued to grow strongly, led by double-digit growth in exports of chemical, petroleum, rubber and wood products. Export of chemical products improved further to increase by 22.4% (2Q: 9.9%), supported by demand from PR China as well as regional countries, while exports of rubber products (46.3%; 2Q: 38.4%) remained robust due largely to favourable prices. Shipment of wood products increased further by 34.3% (2Q: 10%), mainly supported by demand from Japan.

Agriculture exports registered a strong increase of 20.4% during the quarter (2Q: 3.3%) led mainly by the robust performance of palm oil and rubber exports. Exports of palm oil turned around markedly to rise by 24.5% (2Q: -4%) due to both higher volume (11.4%) and prices (11.7%). The strong increase in demand for Malaysian palm oil was stimulated by increased offtake for use as edible oil, particularly by the Western countries due to the increasing trend to use palm oil to substitute oil containing transfatty acid, and also as feedstock to produce biodiesel. The acceleration in demand was seen particularly from PR China, the European Union (EU), India, Pakistan, and the US. Underpinned by the upturn in demand, palm oil prices rose to an average RM1,604 per tonne (2Q: RM1,461 per tonne). Rubber exports continued to strengthen significantly for the third consecutive quarter, rising by 53%, due entirely to higher prices (+59.5% to 834 sen per kilogramme; 2Q: 727 sen per kilogramme), as volume contracted by 4.1% during the quarter.

Export proceeds from **minerals** increased at a slower rate of 1.3% (2Q: 10.1%) due to a decline in exports of crude oil (-4.1%; 2Q: 19.2%), on account of lower export volume (-15.8%) in line with production trends. Nevertheless, export prices remained high, averaging USD 72.18 per barrel during the quarter as the Malaysian oil, which is of the premium grade, was being traded above other benchmark crude oils in the global oil markets. Exports of liquefied natural gas (LNG) increased at an encouraging pace of 15% due mainly to higher prices (+13% to RM1,114 per tonne) in line with the upward trend in global natural gas prices, as export volume rose only slightly by 1.8%.

Malaysia's export performance continued to be driven by regional markets. Regional exports (excluding Japan) expanded by 16.8% to account for a share of 44.3%. The export performance was underpinned by demand for E&E and resource-based products as well as primary commodities, notably palm oil and crude rubber, by PR China, Singapore, Thailand and Korea. In addition, exports to India increased by 29.2%, spurred mainly by exports of E&E products, crude and refined petroleum products as well as palm oil.

Trade Account

	2005		2006		
	3Q	4Q	1Q	2Q	3Q
	Annual change (%)				
Gross Exports	**7.5**	**12.6**	**11.5**	**9.5**	**13.6**
Manufacturing	*6.3*	*13.1*	*10.6*	*10.0*	*14.2*
Agriculture	*-0.1*	*3.2*	*4.5*	*3.3*	*20.4*
Minerals	*25.8*	*20.2*	*23.0*	*10.1*	*1.3*
Gross Imports	**8.6**	**7.5**	**13.7**	**11.5**	**11.5**
Capital goods	*21.0*	*0.3*	*27.8*	*7.9*	*-6.4*
Intermediate goods	*6.3*	*6.3*	*8.2*	*7.8*	*12.4*
Consumption goods	*5.2*	*4.2*	*14.0*	*12.8*	*15.3*
Trade balance (RM bil)	**23.3**	**28.6**	**25.8**	**22.9**	**28.9**

Source: Department of Statistics, Malaysia

Exports to major trading partners namely the US and the EU (particularly Germany, Netherlands and the UK) increased by 4.2% and 29.9% respectively to account for 32.1% of total exports. Growth was contributed

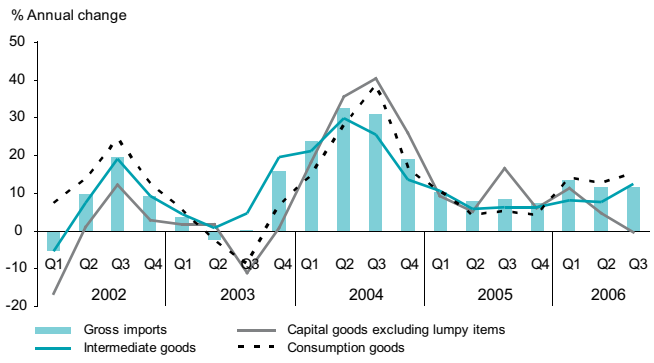
Malaysia: Direction of Exports

	2005		2006			2005		2006			2005		2006		
	3Q	4Q	1Q	2Q	3Q	3Q	4Q	1Q	2Q	3Q	3Q	4Q	1Q	2Q	3Q
	RM billion					Share of total exports (%)					Annual change (%)				
United States	28.9	27.5	24.5	28.1	30.1	21.0	19.3	17.9	19.6	19.2	15.8	18.8	13.4	4.3	4.2
European Union (EU)	15.5	17.5	16.1	17.6	20.1	11.2	12.3	11.8	12.3	12.9	-4.0	11.2	10.0	17.5	29.9
Selected ASEAN countries[1]	34.8	36.7	37.4	37.8	39.9	25.3	25.7	27.3	26.4	25.5	9.3	14.5	14.7	12.0	14.4
North East Asia	24.6	27.0	25.2	26.2	29.5	17.8	18.9	18.4	18.3	18.9	2.2	11.0	7.3	8.8	20.0
People's Republic of China	*8.5*	*10.5*	*8.3*	*9.9*	*12.7*	*6.2*	*7.3*	*6.1*	*6.9*	*8.1*	*-0.8*	*26.2*	*4.4*	*20.3*	*48.9*
Hong Kong China	*8.4*	*7.8*	*7.5*	*7.3*	*7.5*	*6.1*	*5.5*	*5.5*	*5.1*	*4.8*	*13.8*	*6.5*	*6.2*	*-7.7*	*-10.8*
Chinese Taipei	*3.9*	*4.0*	*3.3*	*4.1*	*4.6*	*2.9*	*2.8*	*2.4*	*2.8*	*2.9*	*-6.7*	*-2.4*	*7.2*	*7.3*	*15.8*
Korea	*3.7*	*4.7*	*6.1*	*4.9*	*4.8*	*2.7*	*3.3*	*4.5*	*3.4*	*3.1*	*-3.7*	*2.5*	*12.9*	*18.9*	*28.0*
India	3.9	4.2	4.0	4.1	5.0	2.8	2.9	2.9	2.9	3.2	36.5	32.2	8.3	26.1	29.2
Total exports	137.9	142.6	136.7	143.2	156.6	100.0	100.0	100.0	100.0	100.0	7.5	12.6	11.5	9.5	13.6

[1] Singapore, Thailand, Indonesia, Philippines, Brunei Darussalam and Vietnam
Source: Department of Statistics, Malaysia

mainly by higher exports of E&E products (automatic data processing machines, semiconductor devices, integrated circuits, telecommunication equipment and parts), iron and steel products, as well as primary commodities, namely crude rubber. Export growth to West Asia also strengthened, expanding by 20.4% (2Q: 19.3%).

Import Growth



Meanwhile, import components continued to be sourced from Singapore, PR China, Thailand and Hong Kong. Imports from the regional economies grew by 12.5%, comprising mainly of E&E products, chemicals and chemical products, manufactures of metal as well as iron and steel products.

Growth of **gross imports** was sustained at 11.5% (2Q: 11.5%) reflecting the increase in imported inputs for manufactured exports and domestic consumer spending. Growth of imports of **intermediate goods**, which were inputs used for manufactured goods, strengthened by 12.4% (2Q: 7.8%), driven mainly by higher imports of E&E components such as electronics and parts of telecommunication equipment. Imports of primary and processed materials used by the food and beverage industry and fuel and lubricants continued to increase.

Imports of **capital goods** amounted to RM15.9 billion. Capital imports by selected industries continued to record growth. Capacity expansion and upgrading for fuel efficiency in the manufacturing sector was accelerated. This was most evident in the petrochemicals industry, for which growth in imports reflected the increased imports for machinery, generators, turbines and electric motors. Increased exploration activities in the oil and gas industry led to higher imports of construction and mining equipment.

Consistent with sustained private consumer spending and higher demand in anticipation of festivities, imports of **consumption goods** increased by 15.3% (2Q: 12.8%). The growth reflected mainly

Malaysia: Imports by End Use And Broad Economic Categories (BEC) Classification

	2005		2006		
	3Q	4Q	1Q	2Q	3Q
	Annual change (%)				
CAPITAL GOODS	**21.0**	**0.3**	**27.8**	**7.9**	**-6.4**
Capital goods (except transport equipment)	18.6	5.3	16.1	2.3	1.4
Transport equipment	39.4	-26.8	173.3	50.5	-57.1
INTERMEDIATE GOODS	**6.3**	**6.3**	**8.2**	**7.8**	**12.4**
Food and beverages, mainly for industry	-6.7	6.9	29.0	28.0	24.8
Industrial supplies, n.e.s.	1.8	0.6	1.2	0.9	22.9
Fuel and lubricants	24.5	32.2	21.1	40.1	45.2
Parts and accessories of capital goods (except transport equipment)	5.3	5.6	9.2	7.2	1.4
Parts and accessories of transport equipment	39.4	11.3	8.8	-8.3	3.6
CONSUMPTION GOODS	**5.2**	**4.2**	**14.0**	**12.8**	**15.3**
Food and beverages, mainly for household consumption	5.8	-1.2	3.4	5.4	4.6
Transport equipment, non-industrial	-0.9	17.5	23.6	16.4	-35.0
Consumer goods, n.e.s.	5.1	7.4	20.9	17.2	23.3
Durables	*6.3*	*12.3*	*31.3*	*-7.5*	*5.5*
Semi-durables	*-3.0*	*5.1*	*27.4*	*41.6*	*46.8*
Non-durables	*10.9*	*6.5*	*11.6*	*13.8*	*15.4*
DUAL USE GOODS	**18.9**	**12.2**	**23.2**	**1.0**	**14.8**
OTHERS	**2.5**	**4.9**	**12.0**	**8.6**	**-25.1**
RETAINED IMPORTS	**8.5**	**5.4**	**11.6**	**7.9**	**9.1**
RE-EXPORTS	**10.2**	**53.4**	**52.7**	**92.8**	**62.0**
GROSS IMPORTS	**8.6**	**7.5**	**13.7**	**11.5**	**11.5**

Source: Department of Statistics, Malaysia

increases in semi-durable consumer goods, notably clothing and footwear and non-durables such as medicine, soap and cosmetics. Exploration activities in the oil and gas industry has contributed to strong growth in imports for re-exports (31.9%; 2Q: 46.7%) as iron and steel pipes were imported, coated for corrosion and re-exported.

Larger inflows of FDI

On a cash basis, gross inflows of **foreign direct investment (FDI)** increased to RM10 billion (2Q: RM9.1 billion), attributed mainly to larger inflows of equity capital and inflows of inter-company loans. FDI in the form of equity capital was broad based, channelled mainly into the manufacturing, oil and gas and services sectors. In the manufacturing sector, FDI inflows were mainly concentrated in the electrical and electronics, petroleum-related products as well as chemical-related industries. In the services sector, FDI inflows were directed primarily into the finance, insurance, real estate and business services as well as restaurants, hotels, wholesale and retail trade sub-sectors. Meanwhile, the bulk of the inter-company loans was in the form of short-term loans extended by foreign companies to their subsidiaries in Malaysia, particularly in the finance, insurance, real estate and business services and oil and gas sectors. The bulk of these loans was repaid during the same quarter. After adjustments for gross outflows due mainly to these repayments, net FDI had more than doubled, amounting to RM5.4 billion (2Q: RM2.5 billion). The FDI data on cash basis does not include reinvested retained earnings and investment in the form of imported machinery and equipment.

Overseas investment by Malaysian companies recorded a lower gross outflow of RM25 billion (2Q: -RM33.3 billion) reflecting mainly smaller extension of short-term inter-company loans by non-resident controlled companies in the oil and gas sector to their related companies abroad arising from their centralised treasury operations. These outflows were largely offset by inflows from the repayment of these short-term loans during the quarter. As a result, overseas investment recorded a lower net outflow of RM2 billion (2Q:-RM3.6 billion). The bulk of the net outflows for overseas investment was in the form of equity capital, channelled mainly into the services, manufacturing and oil and gas sectors. In the services sector, overseas investment was led by companies in the finance, insurance and business services as well as transport, storage and communication sub-sectors. Meanwhile, in the manufacturing sector, overseas investment was effected largely by companies in the automotive, chemical-related and wood-related industries.

Portfolio investment registered a net outflow of RM3.1 billion (2Q: +RM0.9 billion) reflecting outflows in both equity and debt securities. During the quarter, gross inflows and outflows for portfolio investment were sustained at high levels as in the preceding quarter.

External debt declined

Malaysia's total external debt declined to RM197.7 billion or USD53.1 billion as at end-September 2006 (2Q: RM198.1 billion or USD53.4 billion), equivalent to 37.6% of Gross National Product (GNP). The **medium- and long-term external debt** declined to RM148.3 billion (2Q: RM149.7 billion) on account of a higher net repayment by the public sector. In particular, the Non-Financial Public Enterprises (NFPEs) registered a higher net repayment of RM2.4 billion (2Q: -RM0.9 billion), reflecting both scheduled repayments and prepayments of some loans, particularly by companies in the oil and gas sector to reduce their debt exposure. The Federal Government also recorded a net repayment of external loans (-RM0.2 billion; 2Q: +RM0.1 billion). Meanwhile, the private sector registered a net borrowing of RM1 billion, effected mainly by companies in the manufacturing, and oil and gas sectors.

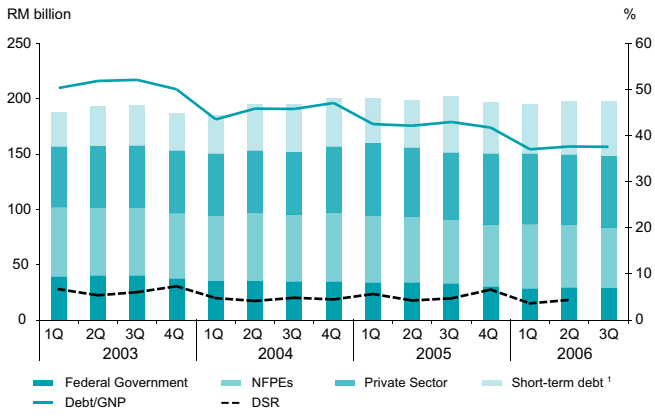
External Debt Outstanding

	2005	2006	
	3Q	2Q	3Q [P]
	RM billion		
Medium- and Long-term debt	152.0	149.7	148.3
Public sector	90.6	86.2	83.7
Private sector	61.4	63.5	64.6
Short-term debt[1]	50.7	48.4	49.4
Total external debt	202.7	198.1	197.7
- USD billion equivalent	53.3	53.4	53.1

[1] Excludes currency and deposits held by non-residents with resident banking institutions
[P] Preliminary

Source: Ministry of Finance, Malaysia and Bank Negara Malaysia

External Debt Outstanding



[1] Excludes currency and deposits held by non-residents with resident banking institutions

The total **short-term external debt** increased to RM49.4 billion or USD13.3 billion (2Q: RM48.4 billion), attributed largely to higher borrowings by the non-bank private sector arising mainly from inter-company loans. As at end-September 2006, the short-term external debt accounted for 25% of total external debt and was 16.9% of the net international reserves.

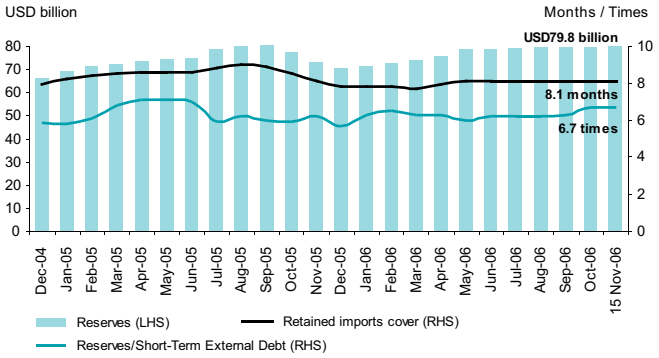
International reserves

The international reserves of Bank Negara Malaysia amounted to RM293.1 billion or equivalent to USD79.5 billion as at 29 September 2006. The reserves level also reflected the quarterly adjustment of the foreign exchange revaluation gains, following the appreciation of major currencies against the ringgit. The reserves amounted to RM294.1 billion or equivalent to USD79.8 billion as at 15 November 2006. The reserves position is sufficient to finance 8.1 months of retained imports and is 6.7 times the short-term external debt.

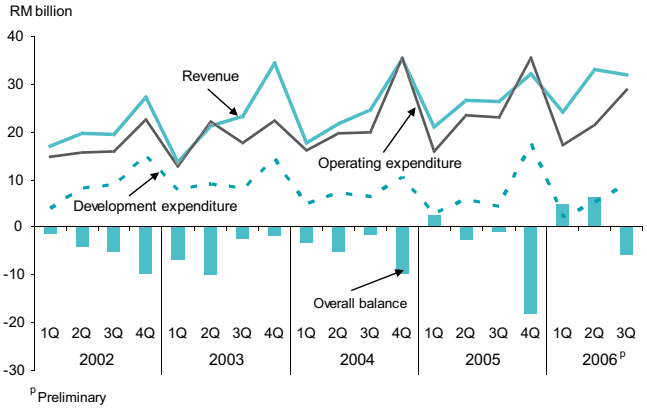
Higher Federal Government spending

Expansionary budgetary operations of the Federal Government was supportive of domestic economic activity in the third quarter. Higher development expenditure was channelled to the economic and social services sectors. Total expenditure rose by 38.4%, resulting in the financial position of the Federal Government recording a fiscal deficit of RM5.8 billion or 4.1% of GDP. The deficit was financed from domestic borrowings and the drawdown of realisable assets. Total Federal Government debt rose by 8% to RM245.8 billion at end-September 2006, equivalent to 44.8% of estimated GDP for 2006.

Net International Reserves (as at end period)



Federal Government Finance



Federal Government Finance[P]

	2005		2006		
	3Q	Jan-Sep	2Q	3Q	Jan-Sep
	RM billion				
Revenue	26.4	74.1	33.0	31.9	89.1
% growth	*7.3*	*15.6*	*24.2*	*20.8*	*20.2*
Operating expenditure	23.0	62.3	21.6	28.8	67.7
% growth	*15.3*	*11.7*	*-7.7*	*25.2*	*8.7*
Current account	**3.4**	**11.8**	**11.4**	**3.1**	**21.4**
% of GDP	***2.6***	***3.2***	***8.5***	***2.2***	***5.3***
Gross development expenditure	4.4	13.1	5.2	9.1	16.4
% growth	*-30.2*	*-28.8*	*-12.2*	*108.1*	*25.6*
Overall balance	**-0.8**	**-0.9**	**6.4**	**-5.8**	**5.5**
% of GDP	***-0.6***	***-0.2***	***4.8***	***-4.1***	***1.4***
Memo item:					
Total gross expenditure	27.3	75.4	26.8	37.8	84.1
% growth	*4.5*	*1.6*	*-8.6*	*38.4*	*11.6*
Total Federal Government debt (as at end-period)	227.6	227.6	240.2	245.8	245.8
% of GDP	*46.0*	*46.0*	*43.8*	*44.8*	*44.8*
Domestic debt	194.5	194.5	211.1	216.9	216.9
% of GDP	*39.3*	*39.3*	*38.5*	*39.6*	*39.6*
External debt	33.2	33.2	29.1	28.9	28.9
% of GDP	*6.7*	*6.7*	*5.3*	*5.3*	*5.3*

[P] Preliminary