DEVELOPMENTS IN THE ECONOMY

International Economic Environment

Global environment strengthens. Business investment turns positive in the US while Asian growth recovers as SARS contained.

The global economic environment strengthened further in the third quarter. The US economy expanded significantly by 7.2% during the quarter (2Q: 3.3%), its highest quarterly growth recorded in two decades. Major contributory factors were the sharp gains in consumer spending, residential and non-residential fixed investments and exports. The Japanese economy exhibited further signs of improvement as reflected in the strong recovery of private investment and exports, while the pace of decline in prices continued to moderate. However, recovery in much of Europe remained constrained by structural rigidities despite improvement in business sentiment.

Reflecting a more optimistic outlook on the international environment, the global equity markets showed stronger performance, particularly in the technology-related sectors. In the foreign exchange market, the G7 endorsement of flexibility in currency movements caused volatility in the market and a weaker US dollar. Going forward, the sustainability of the global economic recovery will hinge on the strength of expansion in business investment, the extent of fiscal and monetary stimulus in the major industrialised countries as well as orderly adjustments in the US current account and fiscal imbalances.

Industrial Countries:
Real GDP growth showed improved performance

	Yearly	Quarterly		
	2002	2Q '03	3Q '03	Contributing factors
US[1/]	2.4	3.3	7.2	Strong consumer spending, business investment and export growth.
UK	1.8	2.0	1.9	Robust consumer spending and sustained government expenditure.
Germany	0.2	-0.7	-0.2	Weak industrial output and labour market conditions but improved consumer and business sentiment.
Japan[1/]	0.2	3.5	2.2	Improvement in exports and capital spending.

1/ annualised basis

In the **Asian** region, following the containment of the Severe Acute Respiratory Syndrome (SARS) by the end of the second quarter, regional growth gained strength in the third quarter. Growth was supported mainly by stronger export performance. In addition, most of the previously SARS-affected countries registered a recovery in domestic consumption and tourist arrivals. The People's Republic of China (P. R. China) registered the highest real GDP growth (9.1%), while growth turned positive in Chinese Taipei and Singapore.

Overall, growth in the third quarter was reinforced by strong export performance on the back of continued strong domestic demand, benign inflation and low interest rates. Inflation in P. R. China continued to edge up, albeit marginally, due mainly to increased demand for raw materials. In contrast, deflationary pressures in Hong Kong China and Chinese Taipei persisted, as domestic demand conditions remained soft. In most of the regional countries, there were further declines in short-term interest rates and strengthening of international reserves positions.

Given expectations of further improvements in external and domestic conditions, growth forecasts for 2003 were raised in P. R. China,

Hong Kong China and Thailand. In contrast, the growth forecast for Korea was lowered due to political uncertainty and weakness in domestic consumption and investment activities.

Regional Countries: Real GDP growth improved

	Yearly	Quarterly		
	2002	2Q '03	3Q '03e/	Key contributing factors
P. R. China	8.0	6.7	9.1	Robust investment activity and consumption spending.
Korea	6.3	1.9	2.7	Export growth more than offset weak consumption and investment expenditures.
Singapore	2.2	-3.8	1.7	Expansion in manufacturing, particularly electronics and pharmaceuticals.
Chinese Taipei	3.5	-0.1	4.2	Supported by strong export performance.
Indonesia	3.7	3.8	3.9	Broad-based improvements in domestic and external conditions.
Philippines	4.6	4.5	4.0	Recovery in agriculture sector partially offset weakness in manufacturing sector.

e/ Estimate

Developments in the Malaysian Economy

Higher growth in the third quarter was underpinned by strong private sector activity

Growth was markedly stronger in the third quarter with real GDP expanding by 5.1% (2Q 2003: 4.5%). Aggregate domestic demand strengthened, underpinned by higher private sector spending as pro-growth measures introduced by the Government and buoyant commodity prices supported the recovery of the services sector and strengthened private consumption.

Domestic demand strengthened in the third quarter, benefiting from low interest rates and earlier measures to increase disposable incomes of households and improve access to funding to meet the financing needs of industries and the SMEs. Firm commodity prices continued to raise rural incomes and consumption. Stable labour market conditions and a more optimistic outlook regarding prospects for global economic growth led to a further improvement in consumer and business confidence. Overall, private sector demand strengthened.

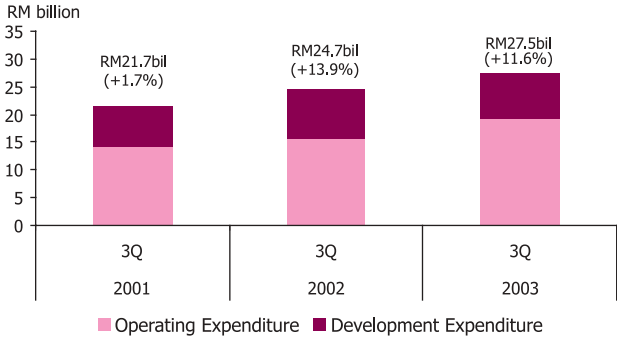
Following recovery from SARS-related concerns, private consumption recorded a strong growth of 5.4% (2Q 2003: 3.4%) during the quarter. Major consumption indicators, including the expansion of monetary aggregates, especially M1, loans disbursed to households and consumer spending on credit cards, pointed to growing consumer optimism. This was reflected in the

GDP by Expenditure Components (at Constant 1987 prices)

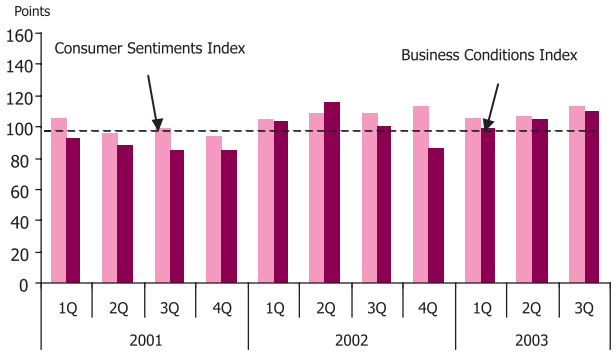
	2002		2003		
	3Q	4Q	1Q	2Q	3Q
	Annual change in %				
Aggregate domestic demand (excluding stocks)	6.1	6.6	5.9	3.0	3.5
Consumption	7.8	5.1	6.9	4.3	3.6
Private sector	*4.2*	*4.6*	*4.3*	*3.4*	*5.4*
Public sector	*19.2*	*6.5*	*18.9*	*7.2*	*-1.6*
Gross Fixed Capital Formation	2.8	10.0	3.8	0.4	3.2
Exports of Goods and Services	11.2	7.2	1.9	0.2	-5.0
Imports of Goods and Services	15.6	8.1	1.7	-2.9	-5.1
GDP	**5.8**	**5.4**	**4.6**	**4.5**	**5.1**

Source: Department of Statistics, Malaysia

Federal Government's spending remained high



Growing consumer and business confidence



Malaysian Institute of Economic Research (MIER) Consumer Sentiments Index, which rose by 5.9 points to 112.8 points in the third quarter. Public consumption also remained high, due mainly to the higher expenditure on emoluments and supplies and services.

An important development supporting higher private sector activity was the significant improvement in investment. Gross fixed capital formation expanded by 3.2% in the third quarter (2Q 2003: 0.4%). Private sector investment activities rose amidst stronger financial positions of corporations and higher capacity utilisation rates. Business sentiments turned more positive during the quarter. The MIER Business Conditions Index increased by 4.9 points to 109.8 points, reflecting improved results in most components including output, domestic orders and inventory levels. Other major private investment indicators, including sales of commercial vehicles and loan disbursements to the manufacturing and construction sectors, also pointed to stronger recovery of investment activities. Meanwhile, development expenditure of the Federal Government continued to remain high, particularly on health, public utilities and agriculture and rural development.

Sectoral Developments

Growth broad based and balanced across the sectors

Growth in the third quarter was broad based, characterised by the rapid recovery in the services sector after the transitory impact of SARS and continued strong expansion in the manufacturing and agriculture sectors.

Quarterly GDP by Kind of Economic Activity at 1987 Prices

	2002		2003		
	3Q	4Q	1Q	2Q	3Q
	Annual change in %				
Agriculture	8.3	5.5	3.4	10.4	6.2
Mining	7.9	7.1	4.5	11.1	-0.7
Manufacturing	7.3	5.7	5.9	6.5	8.5
Construction	2.6	0.5	1.2	1.4	2.4
Services	3.4	4.6	4.5	2.9	4.2
Real GDP (Annual chg.)	**5.8**	**5.4**	**4.6**	**4.5**	**5.1**
Real GDP (Preceding chg.)	**3.6**	**0.7**	**-3.8**	**4.1**	**4.2**

Source: Department of Statistics, Malaysia

Recovery in the services sector

The **services sector** rebounded to expand by 4.2% (2Q: 2.9%) following the improvement in consumer sentiment as well as

Value Added in the Services Sector

	2002		2003		
	3Q	4Q	1Q	2Q	3Q
	Annual change in %				
Intermediate Services	**2.5**	**3.8**	**4.1**	**4.3**	**6.0**
Transport, storage and communications	2.8	3.3	4.8	4.2	5.5
Finance, insurance, real estate and business services	2.3	4.0	3.8	4.4	6.4
Final Services	**4.1**	**5.2**	**4.7**	**1.9**	**3.1**
Electricity, gas and water	2.2	4.3	7.3	7.3	5.2
Wholesale and retail trade, hotels and restaurants	3.7	2.6	3.2	-2.0	1.7
Government services	6.0	9.3	5.9	6.9	4.2
Other services	4.0	6.9	5.0	1.6	3.6
Total Services	**3.4**	**4.6**	**4.5**	**2.9**	**4.2**

Source: Department of Statistics, Malaysia

the revival in tourism and travel related-sectors from the effects of SARS, aided by the positive measures introduced in the Economic Package. Of significance, growth in the wholesale and retail trade, hotels and restaurants sub-sector turned around to increase by 1.7% (2Q: -2%). Against the preceding quarter, the sector grew by almost 10%. The recovery was broad based across retail and distributive activities. Hotel businesses also recovered rapidly as monthly tourist arrivals doubled from 459,300 in April to 943,500 by September 2003.

Similarly, growth in the transport, storage and communications sub-sector strengthened further. Air travel, especially the passenger segment, which had been adversely affected in the previous quarter, saw a marked improvement, with passenger traffic increasing by 30% over the preceding quarter. Growth was also supported by sustained port activities as container cargo handled at the two major ports rose by 14.5%. In the telecommunications sub-sector, the increase in the subscriber base as well as sales of new products in the cellular segment sustained the strong growth momentum.

Growth in the finance, insurance, real estate and business services sector was stronger as the reduction in interest rates and additional funds provided under the Economic Package led to higher bank lending. The robust insurance activities and the strong return of interest in the stock market provided further support to the sector. The Government services sub-sector expanded moderately, while growth in the utilities sub-sector was underpinned by strong demand for electricity, particularly from the commercial and industrial sectors.

Growth strengthened further in the manufacturing sector

Growth in the **manufacturing sector** strengthened further to 8.5% in the quarter, supported by higher growth in both the domestic-oriented (6.1%, 2Q: 3.3%) and export-oriented industries (12.1%, 2Q: 10%). The overall capacity utilisation rate was higher at 86% (2Q: 83%), with both the export- and domestic-oriented industries operating at 88% and 82% respectively (2Q: 84% and 82% respectively).

Selected Indicators in the Services Sector

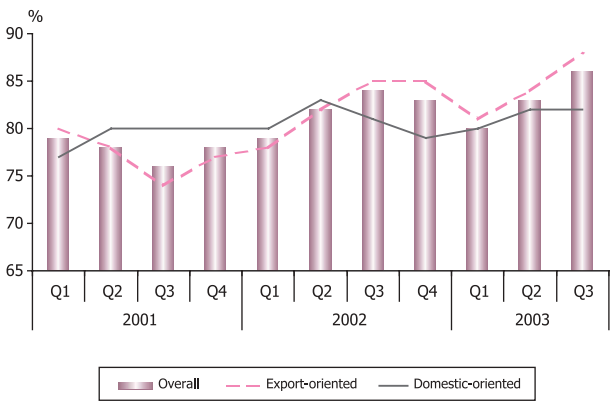
Indicators	2003 1Q	2Q	3Q	2Q	3Q
	ann. chg. (%)			preceding chg. (%)	
MRA Retail sales	-0.1	-2.9	6.4 f	n.a.	n.a.
Tourist arrivals	-6.5	-51.6	-24.2	-40.2	46.7
Disbursement of consumption credit	3.1	1.9	7.4	0.5	9.2
Total passenger traffic in all airports in Malaysia	12.5	-15.9	2.1	-21.3	29.8
	levels			preceding chg. (levels)	
MIER Retail Survey Index	78.1	96.3	125.0	+ 18.2	+ 28.7
MIER Hotel Operators Index	101.5	81.0	139.0	- 20.5	+ 58.0
MAS passenger load factor (%)	67.3	56.0	73.0	-11.3	+ 17.0

Nota: MRA refers to Malaysia Retailers Association; MIER refers to Malaysian Institute of Economic Research and MAS refers to Malaysia Airlines

f Forecast

Source: Various sources

Capacity Utilisation in the Manufacturing Sector



Performance of the Manufacturing Sector

	2002		2003		
	3Q	4Q	1Q	2Q	3Q
	Annual change in %				
Value Added (Constant Price)	**7.3**	**5.7**	**5.9**	**6.5**	**8.5**
Overall Production	**8.5**	**6.7**	**7.6**	**8.2**	**10.6**
Export-oriented industries	**11.2**	**8.9**	**8.0**	**10.0**	**12.1**
of which :					
- Electronics	20.5	12.5	8.6	7.0	14.7
- Electrical	0.1	-4.2	-4.3	-7.6	-12.4
- Textiles & wearing apparel	-7.1	4.4	0.8	2.3	3.0
- Chemicals and chemical products	9.8	13.1	16.4	23.8	20.8
- Off-estate processing	17.8	12.0	4.5	27.3	17.1
- Rubber products	7.1	5.5	9.6	14.3	26.6
- Wood and wood products[1/]	-3.1	1.0	4.3	-0.4	1.4
Domestic-oriented industries	**1.5**	**0.6**	**6.4**	**3.3**	**6.1**
of which :					
- Transport equipment	3.2	-7.9	-6.6	-13.5	-2.6
- Fabricated metal products	-1.3	-1.9	3.8	7.9	-0.7
- Iron & steel and non-ferrous metal	-2.0	4.7	16.7	0.8	13.8
- Non-metallic mineral products	4.3	1.3	10.0	11.4	9.2
- Petroleum products	-1.7	-6.0	1.9	17.5	-6.1
- Food	3.5	10.3	5.5	7.3	16.0
Total Manufactured Exports	**12.7**	**5.1**	**1.7**	**1.3**	**-8.2**
- Electronics	21.6	4.4	-5.8	-4.3	-19.5
Semiconductor	48.9	36.6	27.2	22.4	-11.0
Electronic equip. & parts	3.0	-18.3	-28.3	-25.2	-27.9
- Electrical products	-4.0	-8.3	-7.4	-5.2	-4.8
Consumer electrical products	-9.7	-9.7	-12.5	-17.7	-10.7
Industrial & commercial electrical products	-5.8	-19.5	-14.2	-0.2	-7.3
Electrical industrial machinery & equipment	9.8	11.0	4.1	4.6	6.7
Household electrical appliances	11.5	81.7	78.7	39.9	18.2
- Wood and wood products	23.3	19.1	13.2	5.5	-2.3
- Furniture & parts	10.1	7.4	8.9	5.1	3.3
- Textiles, clothing & footwear	4.5	5.0	8.4	3.3	-1.9
- Optical & scientific equipment	10.1	4.8	19.1	15.7	1.1
- Chemical and chemical products	23.5	34.4	33.9	22.6	18.7
- Petroleum products	-4.1	29.7	67.3	23.8	5.6

[1/] Output of furniture and parts are not captured in the wood production data.

Growth in the export-oriented industries was supported mainly by strong expansion in the off-estate processing, rubber products, chemicals and semiconductor industries. In particular, output of the rubber products industry expanded strongly by 26.6%, benefiting from higher demand for surgical gloves. The semiconductor industry also continued to perform well, supported by improved global demand, particularly from Asia and Europe. The chemical products industry continued to record double-digit growth underpinned by higher output of plastic products and industrial chemicals. In the domestic-oriented industries, the higher output expansion was driven largely by the strong expansion in construction-related materials industries in line with the pick-up in the construction sector as well as food and paper products industries.

Sustained strong growth in agriculture, marginal decline in the mining sector

The **agriculture sector** continued to register the fifth consecutive quarter of strong growth (6.2%), attributed to robust increases in palm oil and rubber production. Rising prices of most of the major agricultural commodities, ranging between 5 to 17%, motivated higher production

Performance of the Agriculture Sector

	2002		2003		
	3Q	4Q	1Q	2Q	3Q
	Annual change in %				
Value Added (at 1987 prices)	**8.3**	**5.5**	**3.4**	**10.4**	**6.2**
Production[1/]					
Of which:					
Crude palm oil	13.0	1.6	0.4	27.3	15.2
Crude palm kernel oil	1.4	0.9	-5.2	28.7	20.6
Rubber	5.1	17.8	16.6	21.3	17.0
Saw logs	15.9	22.8	4.0	-2.6	-9.2
Cocoa	-28.2	35.2	71.5	14.7	-16.7
Exports (RM million)	**42.2**	**49.3**	**41.8**	**33.6**	**29.3**
Of which:					
Palm oil					
('000 tonnes)	12.4	12.1	9.3	15.3	36.4
(RM/tonne)	39.7	46.9	41.4	25.3	7.4
(RM million)	57.0	64.7	54.6	44.4	46.5
Palm kernel oil					
('000 tonnes)	-5.0	15.1	-33.9	7.1	93.9
(RM/tonne)	31.0	38.9	51.0	17.2	1.3
(RM million)	24.5	59.8	-0.2	25.6	96.4
Rubber					
('000 tonnes)	19.4	6.4	13.4	2.0	1.0
(Sen/kilogramme)	36.5	57.8	57.6	40.0	17.2
(RM million)	63.0	67.9	78.7	42.8	18.4
Sawn timber					
('000 cu.metres)	-0.7	4.9	7.8	6.7	8.0
(RM/cu. metre)	8.2	1.8	12.1	9.9	4.5
(RM million)	7.5	6.8	20.8	17.3	12.9
Saw logs					
('000 cu. metres)	2.4	12.9	19.5	32.8	-6.9
(RM/cu. metre)	33.8	31.8	18.9	5.6	-9.6
(RM million)	37.0	48.8	42.1	40.3	-15.8
Cocoa beans					
('000 tonnes)	8.0	71.2	51.7	-38.0	-74.3
(RM/tonne)	43.3	70.3	62.9	37.2	11.9
(RM million)	54.7	191.5	147.2	-14.9	-71.3

[1/] In '000 tonnes, except for saw logs in '000 cubic metres

Performance of the Mining Sector

	2002		2003		
	3Q	4Q	1Q	2Q	3Q
	Annual change in %				
Value Added (at 1987 prices)	**7.9**	**7.1**	**4.5**	**11.1**	**-0.7**
Production					
Of which:					
Crude oil and condensates ('000 barrels)	9.1	7.4	2.3	11.7	1.8
Natural gas (net) (million standard cubic feet)	8.0	9.3	8.2	17.3	-6.2
Exports (RM million)	**5.8**	**29.3**	**50.9**	**38.7**	**25.9**
Of which:					
Crude oil					
('000 tonnes)	18.3	5.5	4.2	0.3	13.7
(US$/barrel)	1.3	37.2	61.3	15.9	6.9
(RM million)	19.8	44.7	68.0	16.2	21.6
Liquefied natural gas					
('000 tonnes)	-0.7	12.9	6.9	41.0	10.3
(RM/tonne)	-4.4	6.6	28.8	33.3	8.9
(RM million)	-5.1	20.4	37.8	88.0	20.1

activity, particularly among the smallholders. Following the strong growth in the previous quarter, the mining sector recorded a marginal decline, due largely to lower production of natural gas. Crude oil production recorded a small increase.

After the strong growth of 27.3% in the previous quarter, crude palm oil production continued to increase by 15.2%, or a monthly average output of 1.3 million tonnes. The growth was underpinned by higher yields as reflected by the average oil extraction rate of 19.88% during the quarter (2Q 2003: 19.63%) as well as increased mature area, especially in Sabah. Rubber production surged further by 17% as continued rise in rubber prices, which averaged above 400 sen per kilogramme by September 2003, induced intensive tapping activity among the smallholders. Consequently, rubber smallholders accounted for about 89% of total national production during the quarter (2002: 85%).

Value added in the **mining sector** declined during the third quarter, albeit marginally by 0.7%, due mainly to lower natural gas production. Output of natural gas was affected by a temporary shutdown of a gas field for maintenance purposes. Meanwhile, crude oil production (including condensates) increased further by 1.8% to 720,390 barrels per day during the quarter.

Construction activity benefiting from the Economic Package

In the **construction sector**, the growth momentum picked up gradually in the third quarter (2Q 2003:1.4%). In particular, the residential sub-sector benefited from the Government incentives provided in the Economic Package as well as the on-going construction works on a large number of housing projects that were launched in the previous year. The stamp duty waiver on selected categories of houses, reduction in interest rates, competitive loan packages offered by financial institutions and intensive promotional activities by housing developers in the major towns encouraged demand for residential property. However, construction activity in the public sector was lower due to lower expenditure on educational facilities.

Construction Indicators

	2002		2003		
	3Q	4Q	1Q	2Q	3Q
	Annual change in %				
New sales and advertising permits	4.2	-11.4	-24.5	-16.7	14.9
Housing approvals	-25.5	-32.3	-30.7	0.8	19.3
Production of construction-related materials	1.4	2.8	13.0	6.5	11.3
Loans approved for construction	5.6	69.6	20.0	-44.3	16.6
Imports of construction materials & mineral products	32.2	8.7	4.0	-19.3	-23.4*

* *July-August '03*

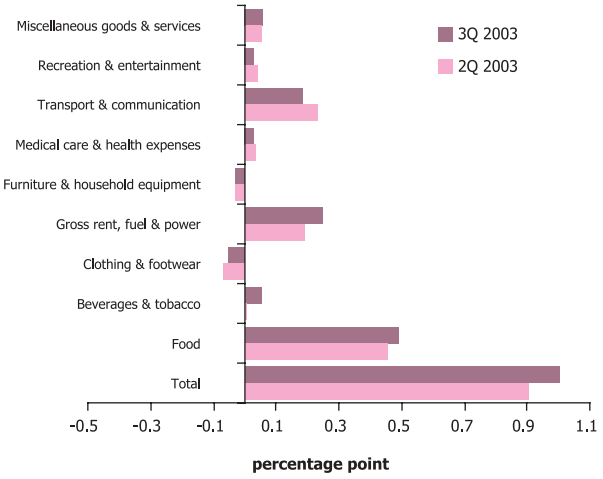
Source: Ministry of Housing and Local Government
Department of Statistics, Malaysia

Inflation remained low

Inflation, as measured by the annual change in the Consumer Price Index (CPI), remained

low at 1% during the third quarter of 2003 (2Q 2003: 0.9%). Reflecting higher consumer spending, price increases for food and gross rent, fuel and power were higher in the third quarter compared with the previous quarter. Meanwhile, price increases for beverages and tobacco was also higher following the introduction of higher import and excise duties on alcoholic beverages and tobacco product. Nonetheless, higher prices for these products were offset by declines and lower price increases for other consumer products and services.

Contribution to Inflation



Source: Department of Statistics, Malaysia

Labour market conditions remained stable

Supported by growth in productivity, labour market conditions continued to remain stable. In the manufacturing sector, based on data for July and August 2003, labour productivity, as measured by real sales value of products per employee rose by 4%, exceeding the 2.4% increase in real wage per employee. Retrenchment during the quarter was lower (5,328 persons; 3Q 2002: 5,549 persons and 2Q 2003: 6,677 persons).

Stable Labour Market Conditions



Trade surplus remained favourable

Preliminary data published indicates that the trade surplus declined to RM15.2 billion during the quarter as both gross exports (-3.1%) and gross imports (-5.7%) declined. The trade data is currently being reviewed by the Department of Statistics (DOS) as the changeover from the manual processing system to the Electronic Data Interchange System (EDIS) has given rise to some exclusions. DOS will release the data when the review is completed.

Trade Account

	2002		2003		
	3Q	4Q	1Q	2Q	3Q
	Annual change in %				
Gross Exports	14.3	9.7	8.0	6.0	-3.1
Manufacturing	12.7	5.1	1.7	1.3	-8.2
Agriculture	42.2	49.3	41.8	33.6	29.3
Minerals	5.8	29.3	50.9	38.7	25.9
Gross Imports	19.6	8.6	2.6	-5.0	-5.7
Capital goods	17.7	0.4	-0.7	-13.1	-5.1
Intermediate goods	19.3	7.8	1.9	-4.1	-4.3
Consumption goods	20.5	19.0	6.2	-1.6	-12.2
Trade balance (RM bil)	13.5	15.1	17.7	19.0	15.2

Source: Department of Statistics, Malaysia

Strong recovery in tourist arrivals

Reflecting increased confidence in air travel in the aftermath of the SARS outbreak, tourist arrivals picked up to 2.5 million arrivals in the third quarter from 1.7 million in the second quarter. Tourist arrivals from the ASEAN region have reached levels attained in the pre-SARS period. Promotional campaigns were conducted during the quarter in SARS-affected countries such as People's Republic of China, Hong Kong China and Chinese Taipei and in new markets such as Pakistan. These were supplemented by the restoration of flights to and from SARS-affected countries and the launch of chartered flights to the People's Republic of China. As a consequence, tourist arrivals from the People's Republic of China, Hong Kong China and Chinese Taipei doubled on a preceding quarter basis. Going forward into the fourth quarter, tourist arrivals are expected to exceed the one million monthly arrivals level attained in the pre-SARS period.

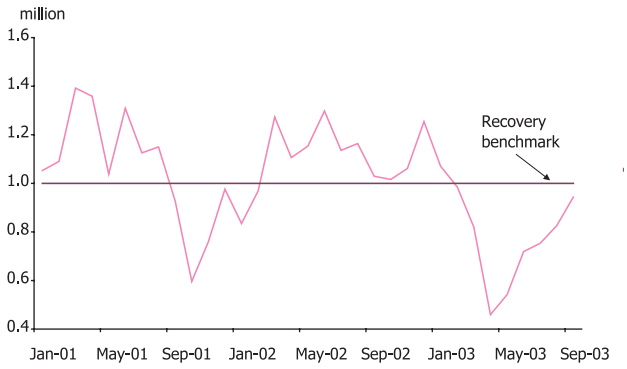
Sustained inflows of investment funds

On a cash basis, gross inflows of funds for investments (FDI) remained high, although moderately lower than the previous quarter (RM4 billion; 2Q 2003: RM5.7 billion). During the quarter, new inflows of equity doubled. Lower inflows reflected mainly lower draw-down of inter-company loans as more funding was sourced from domestic financial institutions. In the third quarter, higher FDI inflows were mainly channelled into the services sector, in particular financing and business services, wholesale and retail trade, and the transport industry. There were also new investments in the manufacturing sector, particularly in the semiconductor and petroleum-related activities. After adjusting for outflows due mainly to loan repayment by related companies, FDI recorded a net inflow of RM1 billion.

Overseas investment recorded a net outflow of RM1.6 billion (2Q 2003: -RM2.6 billion). In terms of gross outflows, more than a third of these investments were effected by the investment holding companies for investment in the transportation, manufacturing and services sectors in Singapore, Mauritius and South Korea. There were also significant investments by companies in the oil and gas in Africa, and manufacturing sectors, particularly the electrical and electronics industries in the US and Switzerland. An important development is the increasing repatriation of profit and dividend by Malaysian corporates operating abroad. In the period January to September 2003, RM1.3 billion was repatriated, compared to RM1.4 billion for the whole of 2002.

Portfolio investment recorded a higher net inflow, amounting to RM3.6 billion (2Q 2003: RM 0.6 billion), as improved domestic and foreign investor sentiments led to more robust activities on the KLSE.

Monthly Tourist Arrivals



Source: Tourism Malaysia

External debt remains manageable

The significantly large repayments and prepayments (RM6.6 billion) during the quarter offset somewhat the exchange revaluation loss, resulting in Malaysia's external debt stabilizing at RM194 billion (US$51 billion) as at end September 2003, equivalent to 54% of GNP. The repayments and prepayments of **medium and long-term external debt** were mainly by the non-financial public enterprises (NFPEs) and, to a lesser extent, the Federal Government. This is the sixth consecutive quarter of net repayments by the NFPEs, reflecting the settlement of several large external loans. In the private sector, repayments were effected by companies operating in the telecommunication, manufacturing and agriculture sectors. After taking into account the exchange revaluation loss following the appreciation of yen and euro, the medium and long-term debt was slightly higher at RM158.1 billion or US$41.6 billion (2Q 2003: RM157.9 billion).

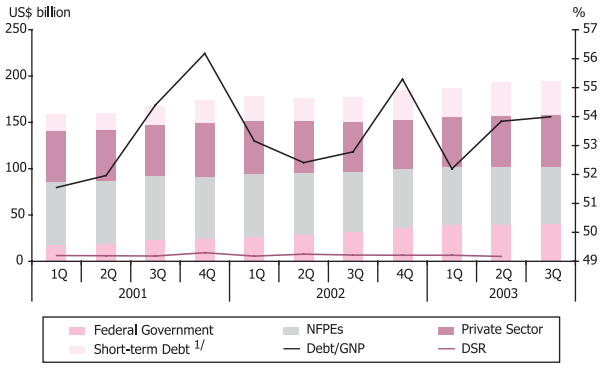
Short-term external debt remained stable at RM35.9 billion or US$9.5 billion (2Q 2003: RM35.6 billion). As at end-September, the short-term debt accounted for only 18.5% of total external debt, and is about 23.2% of the net international reserves.

External Debt Outstanding

	2002	2003	
	3Q	2Q	3Q
	RM billion		
Medium & Long-term debt	151.3	157.9	158.1
Public sector	97.1	102.1	102.2
Private sector	54.3	55.8	55.8
Short-term debt [1]	25.8	35.6	35.9
Total external debt	177.1	193.4	194.0
- US$ billion equivalent	46.6	50.9	51.0

[1] Excludes currency and deposits held by non-residents with banking institutions.
Source: Ministry of Finance, Malaysia and Bank Negara Malaysia

External Debt



1/ Excludes currency and deposits held by non-residents with banking institutions.
Source: Ministry of Finance, Malaysia and Bank Negara Malaysia

Under the IMF Special Data Dissemination Standard (SDDS) on external debt, currency and deposits held by non-residents with banking institutions were included in the coverage of external debt with effect from 30 September 2003. While Bank Negara Malaysia has adopted this coverage for external debt in the SDDS templates, publications by Bank Negara Malaysia, for the time being, will not include currency and deposits held by non-residents with banking institutions in the external debt tables. This item will continue to be shown as part of external liabilities of the banking system in the monthly statistics published by Bank Negara Malaysia. To be consistent with the SDDS coverage, Bank Negara Malaysia intends to adjust the external debt tables in all its publications at a future date, when the new Bank Negara Malaysia statistical system to collate external debt data is completed.

International reserves increased further

The rising trend in the international reserves of Bank Negara Malaysia continued into the third quarter. As at 30 September 2003, the net international reserves amounted to RM154.8 billion or US$40.7 billion, reflecting an increase of RM13.9

billion or US$3.7 billion since end-June 2003. The increase in reserves was attributed mainly to sustained repatriation of export earnings and inflows of foreign funds for direct and portfolio investment. The reserves level at the end of September has also taken into account the quarterly adjustment of the unrealised foreign exchange revaluation gain amounting to US$542 million, mainly as a result of the appreciation of euro and yen against the US dollar during the quarter.

The international reserves increased further to RM165.8 billion or US$43.6 billion as at 31 October 2003, attributed largely to sustained repatriation of export earnings and larger inflows of foreign direct investment and portfolio funds . The current level of reserves is adequate to finance 6.9 months of retained imports and is 4.7 times the short-term external debt.

Smaller fiscal deficit

While the budgetary operations of the Federal Government remained supportive of domestic economic activities in the third quarter, the Federal Government recorded a lower deficit of RM4 billion or 4% of GDP (2Q 2003: -8.4% of GDP). The improvement came from both lower expenditure and higher revenue. Stronger revenue performance in the third quarter arose largely from higher investment income and petroleum-based revenue. Most sources of indirect taxes registered better growth following the pick-up in aggregate demand. Lower receipts for service tax was due to the exemption of service tax for hotels and restaurants under the economic package announced in May 2003.

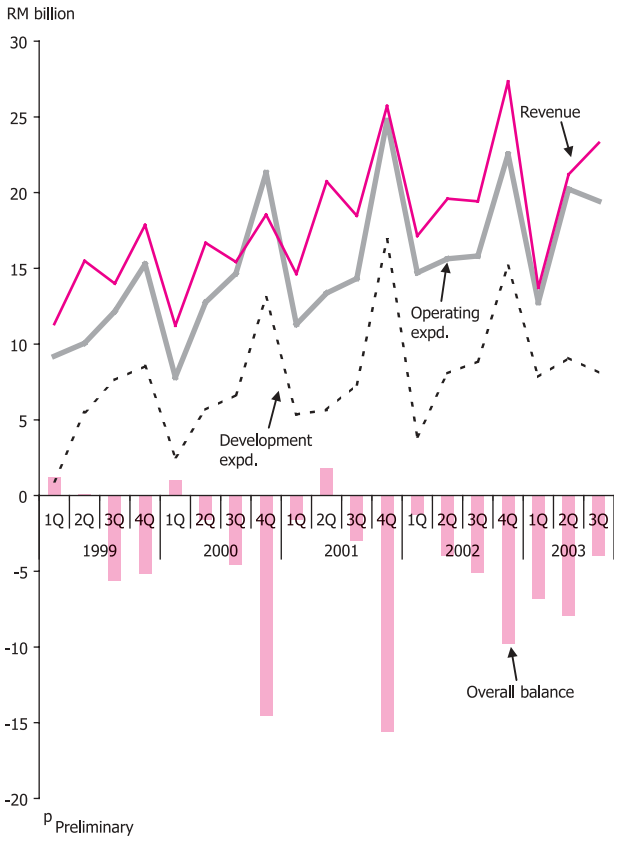
The deficit was financed through non-inflationary domestic borrowings, given the ample

Federal Government Finance [p]

	2002		2003		
	3Q	Jan.-Sept.	2Q	3Q	Jan.-Sept.
	RM billion				
Revenue	19.4	56.2	21.2	23.3	58.2
% growth	5.1	4.3	8.1	19.9	3.6
Operating expenditure	15.8	46.2	20.2	19.4	52.4
% growth	10.4	18.4	29.4	22.9	13.5
Current account	3.6	10.0	1.0	3.9	5.8
% of GDP	3.9	11.8	1.0	3.9	2.0
Gross development expenditure	8.9	20.8	9.1	8.1	25.0
% growth	20.8	13.5	12.7	-8.5	20.2
Loan recoveries	0.1	0.4	0.1	0.3	0.5
Overall balance	-5.1	-10.4	-8.0	-4.0	-18.8
% of GDP	-5.5	-12.3	-8.4	-4.0	-6.5
Memo item:					
Total gross expenditure	24.7	67.0	29.3	27.5	77.4
% growth	13.9	16.8	23.7	11.6	15.6
Total Federal Government debt (as at end period)	156.7	156.7	182.1	188.6	188.6
% of GDP	43.4	43.4	47.2	48.9	48.9
Domestic	124.6	124.6	142.3	148.4	148.4
External	32.1	32.1	39.9	40.2	40.2

[p] Preliminary

Federal Government Finance [p]



[p] Preliminary

liquidity situation. Total Federal Government debt rose moderately by 3.6% to RM188.6 billion, accounting for 48.9% of GDP as at end-September 2003 (47.2% as at end-June). The Federal Government's external debt was contained at 20.7% of the nation's external debt.