ECONOMIC PERFORMANCE AND PROSPECTS

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ECONOMIC REPORT 2005/2006

Overview

A strong and healthy Malaysian economy continues to chart steady growth…

The Malaysian economy remains resilient despite moderation in the growth of global economy amidst high oil prices and less accommodative monetary policy, particularly in the United States (US). The nation continues to sustain its growth momentum, with strong domestic demand providing the impetus for the expansion in domestic economic activities.

Economic fundamentals have further strengthened while domestic demand continued to be resilient amidst firm consumer spending as well as continued uptrend in private investment activities. These factors, coupled with pro-active measures by the Government to promote economic activities provided the enabling environment for the Malaysian economy to expand favourably, albeit at a lower rate of 4.9% in the first half of 2005, compared with 8.1% during the same period of 2004. Despite sharp increases in oil prices, the Malaysian economy is expected to register 5.1% growth in the second half of the year, with growth for the year averaging 5%. This projection is premised on a growth of 4.8% in the Leading Index for January-June 2005 which indicates continued expansion in the second half of 2005. Growth is expected to be broad based with major sectors recording positive growth, backed by recovery in global electronics demand. The continuing build-up in international reserves arising from larger current account surplus and inflows of foreign capital has also strengthened domestic macroeconomic fundamentals.

The expansion in the economy is reflected by positive growth in all sectors, except construction. The main drivers of growth are the services, manufacturing and the primary commodity sectors. Strong domestic consumption is expected to drive the services sector, especially in wholesale and retail trade, hotels and restaurants; transport, storage, and communication; and financial services sub-sectors. The recovery of global electronics demand will accelerate manufacturing exports, resulting in a stronger momentum in manufacturing production in the second half of the year. Meanwhile, stable commodity prices will help sustain the growth momentum of the agriculture sector. Growth in private consumption remains firm, arising from higher household income. Private investment is expected to further strengthen, reinforced by continued accommodative and more flexible monetary policy as well as higher inflow of foreign direct investments (FDI).

In tandem with the expansion in economic activities, national income as measured by Gross National Product (GNP), is estimated to increase by 9.1% to RM463,546 million (2004: 14.1%; RM425,060 million), with per capita income rising by 6.8% to reach RM17,741 (2004: 11.7%; RM16,616). Based on purchasing power parity (PPP), per capita income is expected to increase by 7.2% to USD10,323 (2004: 7.4%; USD9,630).

International Developments

Global growth moderated but remains resilient despite high crude oil prices...

The world economy is expected to expand at a more moderate pace in 2005 in the midst of sharply higher oil prices as well as tighter monetary policy in the US. While the pace of global growth will be somewhat lower, it will, nonetheless, continue to remain strong with further expansion in economic activities.

World economic growth, which had recorded a thirty-year high of 5.1% in 2004, is estimated to moderate to 4.3% in 2005, as shown in *Table 2.1*. Global growth continues to be led by China and the US, with growth rates of 9% and 3.5%, respectively. Most countries in emerging Asia are expected to post satisfactory growth rates, albeit below 2004 levels. The recovery in Japan is envisaged to continue to be sustained, underpinned by rising corporate investment and private consumption as well as a rebound in exports. Performance in the euro area is anticipated to improve, although differing widely across the region, as the weak euro boosts export competitiveness.

TABLE 2.1

Real Gross Domestic Product (GDP) Growth for Selected Countries
2002-2006
(% change)

	2002	2003	2004	2005[1]	2006[2]
World GDP	***3.0***	***4.0***	***5.1***	***4.3***	***4.3***
Developed economies					
Euro area	*0.9*	*0.7*	*2.0*	*1.2*	*1.8*
Japan	*-0.3*	*1.4*	*2.7*	*2.0*	*2.0*
United Kingdom	*2.0*	*2.5*	*3.2*	*1.9*	*2.2*
United States	*1.6*	*2.7*	*4.2*	*3.5*	*3.3*
East Asia					
China	*8.3*	*9.5*	*9.5*	*9.0*	*8.2*
Hong Kong SAR	*1.9*	*3.2*	*8.1*	*6.3*	*4.5*
South Korea	*7.0*	*3.1*	*4.6*	*3.8*	*5.0*
Taiwan	*3.9*	*3.3*	*5.7*	*3.4*	*4.3*
ASEAN 5					
Indonesia	*4.4*	*4.9*	*5.1*	*5.8*	*5.8*
Malaysia	*4.4*	*5.4*	*7.1*	*5.0*	*5.5*
Philippines	*4.3*	*4.5*	*6.0*	*4.7*	*4.8*
Singapore	*3.2*	*1.4*	*8.4*	*3.9*	*4.5*
Thailand	*5.3*	*6.9*	*6.1*	*3.5*	*5.0*

[1] Estimate.
[2] Forecast.

Source: IMF World Economic Outlook (September 2005) and various sources.

The US, currently in its fourth year of expansion, continues to outperform other major industrial countries, despite high energy prices and interest rate hikes. Its real **GDP growth** recorded 3.3% in the second quarter (Q1 2005: 3.8%) of 2005. This is mainly due to increases in personal consumption, exports, equipment and software, residential fixed investment and government spending, which was partly offset by a deceleration in private inventory investment. With the outlook for the next six months remaining stable, real GDP for the year is forecast at 3.5%.

The UK economy performed marginally better in the second quarter with a GDP growth of 0.5% (Q1 2005: 0.4%), as high interest rates and rising oil prices continued to dampen consumer and business spending. Although growth in the services sector remained robust, manufacturing output declined while transport and communication as well as the housing market stagnated.

Japan registered a real GDP growth of 0.8% in the second quarter of 2005 (Q1 2005: 1.3%), with consumer spending accounting for more than half of the increase in GDP. Exports' contribution to growth turned positive for the first time in four quarters, reflecting the strength in its economic recovery. Other indicators, notably retail sales, investment plans and employment growth point towards a continued expansion in the second half of the year.

In contrast, growth across the 12-nation euro area remained subdued and uneven. The euro area posted a 0.3% growth in the second quarter (Q1 2005: 0.4%) of the year as high oil prices and global deceleration of the industrial sector, compounded by budget and constitutional crises, continued to weigh down consumer and business confidence. However, Germany saw a pick-up in domestic demand for the first time in almost a year as imports exceeded exports, fuelled by an increase in consumer and government spending as well as investment in equipment and machinery as factory orders and industrial production rose towards the end of the second quarter of 2005. This trend is expected to continue in the third quarter as business confidence further improved, buoyed by encouraging signs of growth in the manufacturing and services sectors.

The economies of the ASEAN 5 remain strong in 2005, although at lower rates of GDP growth, mainly driven by sustained exports and domestic demand. Generally, monetary and fiscal policies remain accommodative and investor sentiment strengthened in most economies in the region. Intra-regional trade is also expected to continue expanding at a brisk pace given the still robust growth of China and India, and underpinned by governments' efforts to further enhance competitiveness and regional integration.

China continued to chalk robust growth, maintaining 9.5% real GDP growth in the first half of the year, as exports surged and investment in power plants, mines and factories, gained momentum. For the rest of the year, the government is expected to continue reining in economic growth through a series of stringent administrative controls on bank loans and land development to prevent overheating in certain sectors. Notwithstanding the measures undertaken, in July, real fixed asset investment continued to grow by 27.7% (January-June 2005: 25.4%), value-added contribution of industry increased by 16.1% (January-June 2005: 16.4%) and total retail sales of consumer goods rose by 12.7% (January-June 2005: 13.2%). With current trends continuing, real GDP growth for the rest of the year is likely to record a similar strong growth as the first half of 2005.

In most regions, **labour market conditions** continue to improve. The August unemployment rate in the US was held low at 4.9% (2004: 5.5%) with 2.2 million jobs created over the year. Japan and the euro area saw an improving job market with unemployment rates at 4.4% (2004: 4.7%) and 8.6% (2004: 8.9%) in July, respectively. Similarly in the UK, it improved marginally to 4.7% in the second quarter of 2005 (2004: 4.8%).

Rising oil prices edged global **inflation** upwards, but still at manageable levels. In the US, consumer prices rose by 0.5% in July 2005 (2004: 3.3%) following increases in energy and food prices. Despite persistently high oil prices, increases in indirect taxes and administered prices, inflation in the euro area remained stable at 2.2% in July (2004: 2.1%). China too, has managed to keep inflation relatively stable, with July recording 1.8%

(2004: 3.9%). In the UK, however, inflation soared to a seven-year high of 2.3% in July (2004: 1.3%), above the Bank of England's (BOE) target of 2%, following price increases in fuel, transport, imported goods, utilities, food and financial services.

Monetary policy in industrialised countries continues to remain supportive of growth. In the US, against a backdrop of improving labour market conditions and gradually rising inflationary pressures, the Federal Reserve Board (Fed) raised the federal funds rate to 3.75% in September, the eleventh increase since June 2004. In the euro area, the European Central Bank (ECB) continues to maintain the key interest rate at a historic low of 2% since June 2003 to spur investment and consumer spending, while BOE, concerned over lacklustre growth during the first half of the year, cut the benchmark interest rate to 4.5% in August. Japan continues to maintain its quantitative easing of monetary policy to support economic growth and overcome deflation.

Malaysian Economy

Domestic Demand Performance

Domestic consumption and private sector activities sustain economic growth...

Economic growth in 2005 continues to be driven by **domestic demand**, fuelled by private sector activities and supported by rising exports. Of importance, private sector activities have expanded and continued to play a dominant role as the engine of economic growth.

The role of the private sector in promoting growth continues to gain strength. In 2005, **private sector expenditure**, which turned around in 2002, is expected to increase further by 7.5% (2004: 13.1%), following positive consumer sentiments and favourable business conditions. Private sector's share to GDP continues to increase to 60.9% and contributes 4.5 percentage points to GDP growth, as shown in *Table 2.2*. **Public sector expenditure** is estimated to expand by 5.9% (2004: -2.1%), largely due to strong capital investments by non-financial public enterprises (NFPEs). Consequently, the share of public sector expenditure to real GDP is envisaged to remain at 30.6% in 2005 (2004: 30.3%). As the momentum of private sector activities gains strength in the second half of the year, reinforced by an upturn in global electronics demand, aggregate domestic demand in real terms (excluding change in stocks) is envisaged to increase further by 6.9% and contribute 6.3 percentage points to the overall 5% GDP growth. The favourable private sector performance is largely driven by higher investment activities, while consumption spending stays firm.

The sturdy growth of 7.5% (2004: 10.5%) in **private consumption** is supported by rising household disposable income following favourable commodity prices, stable employment market and low interest rate environment. In the first seven months of 2005, key consumption indicators, especially sales of motorcycles and sales tax collection registered double-digit growths of 12.2% and 22.5%, respectively (January-July 2004: 59.3%; -16.2%), as shown in *Chart 2.1.* Other indicators such as imports of consumption goods, sales of food items, consumption credit and credit card spending also showed increases, ranging between 6.6% and 18.6%. In the second half of the year, private consumption is expected to be sustained, with moderately high commodity prices and continuing domestic economic activities.

Private investment is projected to increase by 7.6% and account for 11.5% of GDP in 2005 (2004: 25.8%; 11.3%), mainly due to higher capital outlays in the manufacturing, services, oil and gas as well as agriculture sectors. The Government liberalised the foreign exchange administration rules on 1 April 2005 to further enhance business environment and promote wider risk management options to encourage investment activities. This, together with subsequent appreciation of the ringgit, following its depeg on 21 July 2005, is envisaged to have a positive impact on private investment as firms and investors take advantage of the relatively lower import costs to upgrade plants and machinery as well as embark on new investments. Higher export earnings over the last few years also help generate additional financing for investment

TABLE 2.2

Gross Domestic Product (GDP) by Aggregate Demand
2004-2006
(in 1987 real prices)

	Change (%)			Share of GDP (%)			Contribution to GDP growth (percentage point)		
	2004	2005[1]	2006[2]	2004	2005[1]	2006[2]	2004	2005[1]	2006[2]
GDP	**7.1**	**5.0**	**5.5**	**100.0**	**100.0**	**100.0**	**7.1**	**5.0**	**5.5**
Domestic demand[3]	**7.5**	**6.9**	**5.7**	**89.9**	**91.5**	**91.7**	**6.7**	**6.3**	**5.2**
Private expenditure	**13.1**	**7.5**	**8.1**	**59.6**	**60.9**	**62.5**	**7.4**	**4.5**	**5.0**
Consumption	10.5	7.5	7.0	48.3	49.4	50.1	4.9	3.6	3.5
Investment	25.8	7.6	13.0	11.3	11.5	12.4	2.5	0.9	1.5
Public expenditure	**-2.1**	**5.9**	**0.8**	**30.3**	**30.6**	**29.2**	**-0.7**	**1.8**	**0.2**
Consumption	6.0	8.9	1.3	14.7	15.2	14.6	0.9	1.3	0.2
Investment	-8.7	3.0	0.3	15.6	15.4	14.6	-1.6	0.5	0.0
Change in stocks				**2.2**	**-0.7**	**0.2**	**2.9**	**-2.9**	**0.9**
External sector	**-22.4**	**20.8**	**-6.4**	**7.9**	**9.2**	**8.1**	**-2.5**	**1.6**	**-0.6**
Export[4]	16.3	7.7	9.3	117.4	120.5	124.9	17.6	9.0	11.2
Import[4]	20.7	6.7	10.6	109.5	111.3	116.8	20.1	7.4	11.8
GDP (RM billion, current value)	**449.6**	**487.4**	**530.6**						
Change (%)	13.8	8.4	8.9						

[1] Estimate.
[2] Forecast.
[3] Excluding change in stocks.
[4] Goods and non-factor services.

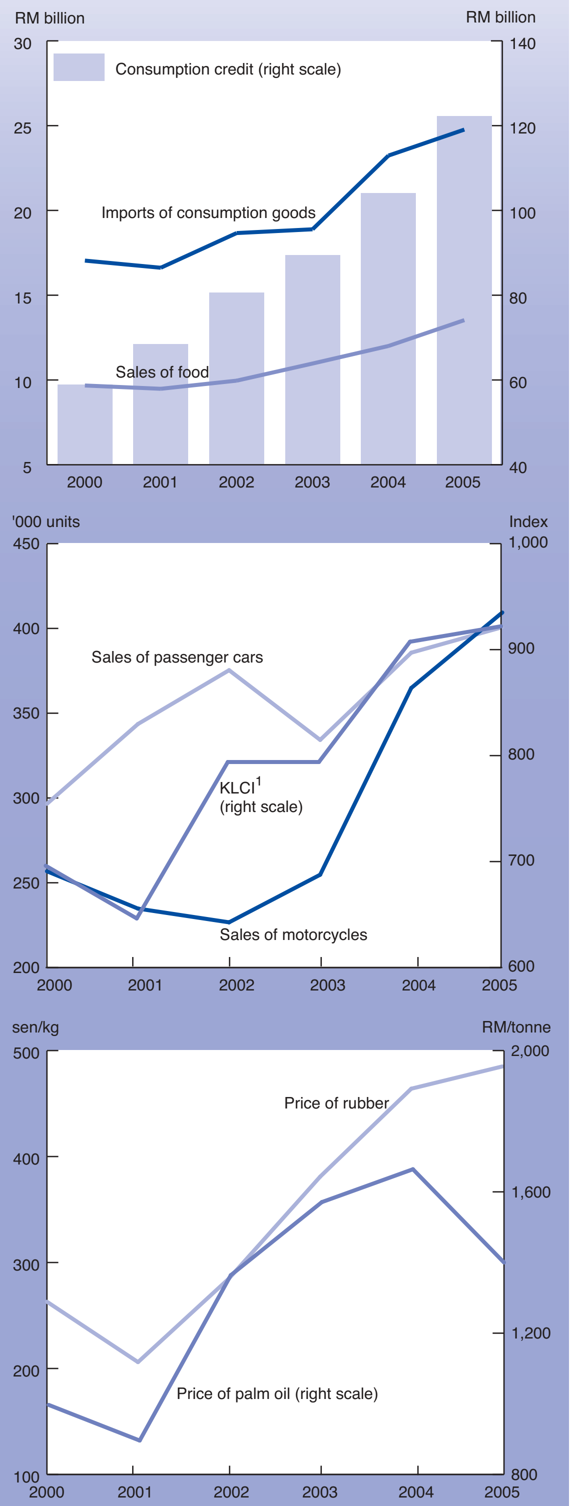
Source: Department of Statistics, Malaysia.

via internally generated funds. In addition, public-private partnership in research and development (R&D) programmes currently underway, especially in biotechnology, advanced materials and manufacturing, and information and communication technology (ICT) are expected to further stimulate investment activities. These initiatives are expected to enhance the nation's competitiveness and economic resilience.

Malaysia continues to attract FDI, particularly in the manufacturing sector. In recent years, however, inflows have been concentrated in the oil and gas industries as well as in the services sector, particularly in communication, information and financial services. This was reflected in the cash balance of payments (BOP) where overall FDI recorded a net inflow of RM2,025 million during the first half of 2005 (January-June 2004: RM1,052 million). Inflows of FDI in the manufacturing sector, as recorded by the Malaysian Industrial Development Authority (MIDA), showed a significant increase of 74.6% in the value of approved investments, totalling RM7,901 million during the first seven months of 2005 compared with a decline of 1.3% (RM4,525 million) in the corresponding period last year. Approved investments for local investors increased substantially by 54.5% to RM7,461 million in the same period, as a result of Government efforts to encourage domestic investments alongside high quality FDI. As such,

CHART 2.1

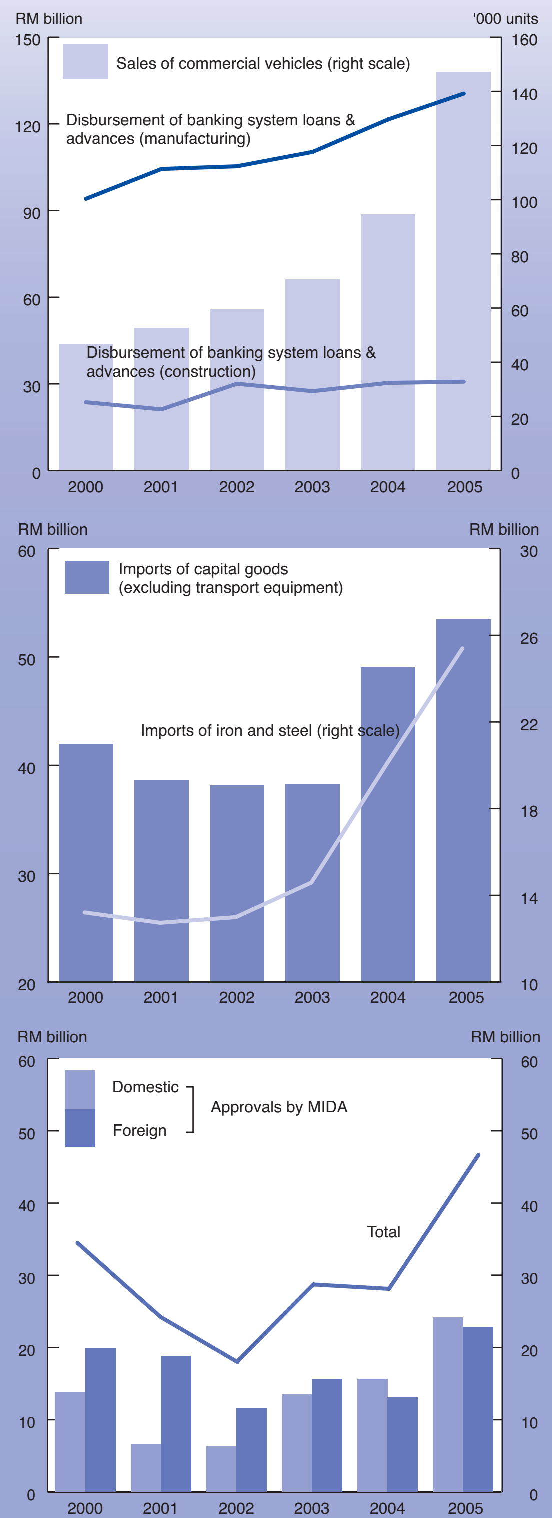
Private Consumption Indicators



[1] As at end of the year and 20 September 2005.

CHART 2.2

Private Investment Indicators



total approved investments recorded an increase of 64.2% to reach RM15,362 million, of which 52.4% is for new investments. The bulk of the approved investments were in electronics and electrical, basic metal, food manufacturing and transport equipment industries.

The expected growth in private investment for 2005 is supported by a number of investment indicators, as shown in *Chart 2.2*. These indicators, which include imports of capital and intermediate goods as well as loan disbursements from the banking system, increased between 5.6% and 10.8% during the first seven months of 2005. Significantly, the increase in sales of commercial vehicles recorded a substantial growth of 55.6% during the same period (January-July 2004: 33.6%).

Public investment expenditure is targetted to increase by 3% in 2005 (2004: -8.7%), mainly due to higher investment activities by NFPEs. Federal Government development expenditure, after taking into account transfer payments, is expected to decline by 5.3% during the year. Nevertheless, slower growth in public investment is compensated by stronger private investment as investors respond favourably to the Government's pro-business policies. Consequently, the share of public sector capital outlays to overall GDP is envisaged to decelerate to 15.4% (2004: 15.6%) while private sector's share increases to 11.5% in 2005 (2004: 11.3%).

Public consumption expenditure is projected to increase steadily by 8.9% (2004: 6%), mainly for emolument, supplies and services. Higher expenditure on supplies and services is largely to further improve public sector delivery and enhance human capital development as long-term measures to strengthen the nation's competitiveness and resilience.

Sectoral Performance

Sectoral growth remains healthy and broad based...

The Malaysian economy is expected to record a healthy growth with most sectors contributing positively to the overall GDP expansion. The services sector, in particular, with a share of

TABLE 2.3

Gross Domestic Product (GDP) by Sector
2004-2006
(in 1987 real prices)

	Change (%)			Share of GDP (%)			Contribution to GDP growth (percentage point)		
	2004	2005[1]	2006[2]	2004	2005[1]	2006[2]	2004	2005[1]	2006[2]
Agriculture[3]	*5.0*	*4.8*	*5.0*	*8.5*	*8.5*	*8.4*	*0.4*	*0.4*	*0.4*
Mining	*3.9*	*1.5*	*4.7*	*7.0*	*6.7*	*6.7*	*0.3*	*0.1*	*0.3*
Manufacturing	*9.8*	*4.8*	*4.9*	*31.6*	*31.5*	*31.3*	*3.0*	*1.5*	*1.5*
Construction	*-1.5*	*-1.1*	*3.0*	*2.9*	*2.7*	*2.7*	*-0.1*	*0.0*	*0.1*
Services	*6.8*	*5.8*	*6.1*	*57.4*	*57.8*	*58.1*	*3.9*	*3.3*	*3.5*
Less imputed bank service charges	*3.4*	*3.9*	*3.9*	*9.3*	*9.2*	*9.1*	*0.3*	*0.4*	*0.4*
Add import duties	*-5.4*	*2.7*	*0.2*	*2.0*	*2.0*	*1.9*	*-0.1*	*0.1*	*0.1*
GDP	***7.1***	***5.0***	***5.5***	***100.0***	***100.0***	***100.0***	***7.1***	***5.0***	***5.5***

[1] Estimate.
[2] Forecast.
[3] Includes livestock and horticulture.

Source: Department of Statistics, Malaysia.

57.8% to GDP is envisaged to continue to be the key driver of growth. Agriculture sector continues to benefit from the revitalising efforts aimed at modernising and transforming agriculture activities into commercially viable source of economic growth. Nevertheless, the manufacturing sector with a share of 31.5% to GDP remains the second most important source of growth and continues to play a prominent role in the economy.

The services sector is estimated to expand at a rate of 5.8% (2004: 6.8%) with all sub-sectors recording positive growth, supported by sustained domestic demand activities. Registering a 4.4% growth in the first half of 2005, the manufacturing sector is envisaged to pick up pace in the second half, leading to a 4.8% growth for the year (2004: 9.8%), following better prospects in global electronics demand.

Value added of the agriculture sector is anticipated to grow at 4.8% (2004: 5%), supported by higher production of palm oil on account of increased matured areas and better productivity. Government policies and strategies geared towards food production have also helped to expand further the sector. Value added in the mining sector is, however, expected to experience a slower growth of 1.5% (2004: 3.9%), underpinned by higher production of natural gas which cushioned the lower production of crude oil. The construction sector is envisaged to record a smaller decline of 1.1% (2004: -1.5%), following lower civil engineering activities.

Manufacturing Sector

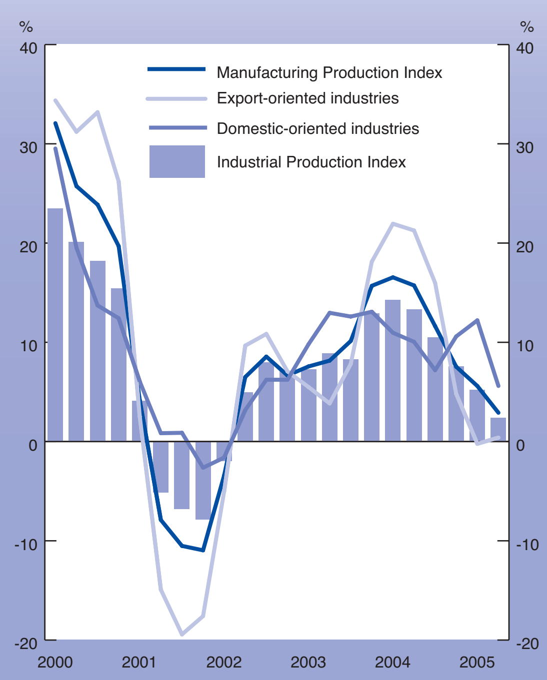
Encouraging developments as industries progress with new designs and advancements in convergent products...

Output of the manufacturing sector grew moderately during the first seven months of 2005 resulting from the slowdown in global economy, led by softer demand for semiconductors. The downcycle of the semiconductor industry was short-lived and far less severe than the one experienced in 2001, with the industry showing signs of recovery from the second quarter of 2005. Further growth is anticipated in the second half of 2005, mainly due to increasing demand for convergent products, particularly telecommunication appliances, consumer electronics and personal computers, thus, pushing manufacturing to a higher value plane.

In the first seven months of 2005, a more pronounced and broad-based expansion was recorded in domestic-oriented industries with almost all, except construction-related industries, registering substantial growth. Plastics and chemicals, food as well as transport equipment industries gained impressively, supported by robust domestic economic activities and rising disposable income. This helped cushion the contraction in output of non-metallic minerals as well as iron and steel products. In contrast, most export-oriented industries showed a lower growth trend. Despite slower growth, the subsector continues to contribute more than 50% to overall manufacturing output. Malaysia, the leading producer of natural rubber gloves, also maintained its industry competitiveness in terms of both output and export earnings.

CHART 2.3

Performance of the Manufacturing Sector
(% annual change)



Source: Department of Statistics, Malaysia.

TABLE 2.4

Manufacturing Production Index
January-July
(1993=100)

Sector	Index 2004	Index 2005	Change (%) 2004	Change (%) 2005	Share (%) 2004	Share (%) 2005
Export-oriented industries	**251.9**	**252.1**	***21.1***	***0.1***	***53.1***	***51.3***
Electrical, electronics and machinery	318.3	319.0	*24.2*	*0.2*	*41.8*	*40.4*
Semiconductors	434.8	443.5	*33.2*	*2.0*	*35.0*	*34.4*
Radio and TV sets	107.5	104.4	*-18.5*	*-2.8*	*2.8*	*2.6*
Professional, scientific, measuring and controlling equipment	137.3	137.3	*15.5*	*0.0*	*0.7*	*0.7*
Rubber-based products	226.4	237.2	*17.4*	*4.8*	*4.8*	*4.8*
Wood-based products	115.0	108.1	*17.8*	*-6.0*	*3.5*	*3.2*
Textiles and apparel	99.1	94.8	*-9.9*	*-4.3*	*2.2*	*2.0*
Domestic-oriented industries	**249.3**	**268.3**	***9.8***	***7.6***	***46.9***	***48.7***
Plastic and chemical products	311.5	350.8	*15.5*	*12.6*	*19.2*	*20.9*
Plastic products	525.8	624.9	*13.0*	*18.8*	*7.7*	*8.9*
Chemical and chemical products	244.7	265.2	*17.2*	*8.4*	*11.5*	*12.0*
Industrial chemicals	258.0	277.9	*16.7*	*7.7*	*6.7*	*10.1*
Food, beverages and tobacco	207.3	231.8	*2.0*	*11.8*	*9.2*	*9.9*
Construction related industries	233.7	221.8	*11.5*	*-5.1*	*11.1*	*10.2*
Iron and steel	217.7	201.4	*5.5*	*-7.5*	*2.8*	*2.5*
Fabricated metal products	278.4	268.3	*31.2*	*-3.6*	*5.0*	*4.7*
Non-metallic mineral	197.7	187.2	*-5.5*	*-5.3*	*3.3*	*3.0*
Transport equipment	252.6	278.4	*5.2*	*10.2*	*3.7*	*3.9*
Paper and paper products	199.3	217.1	*4.7*	*8.9*	*1.3*	*1.4*
Crude oil refineries	199.2	207.3	*-4.4*	*4.0*	*1.1*	*1.1*
Non-ferrous metal	217.3	223.9	*11.4*	*3.0*	*0.7*	*0.7*
Miscellaneous products of coal and petrol	181.4	202.2	*14.4*	*11.5*	*0.3*	*0.3*
Glass and glass products	116.9	129.1	*-0.5*	*10.5*	*0.3*	*0.3*
Total	**250.7**	**259.7**	***15.5***	***3.6***	***100.0***	***100.0***

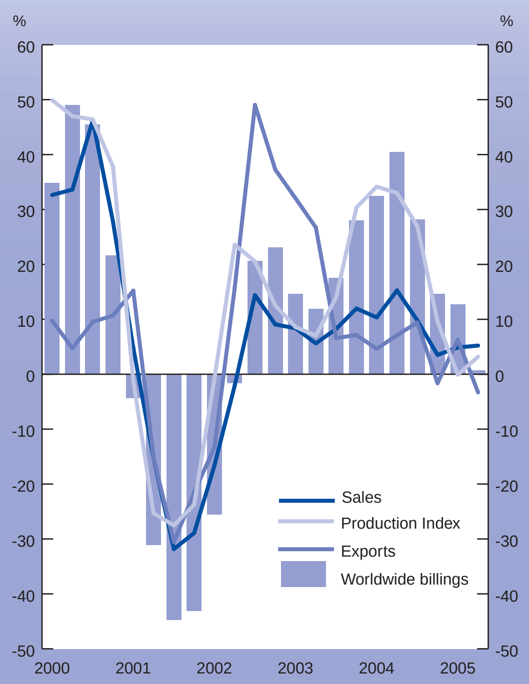
Source: Department of Statistics, Malaysia.

Capacity utilisation in the manufacturing sector was sustained at a high level, averaging 82.8% during the first half of 2005. About 40% of manufacturers were operating at high capacity (81%-100%) while another 40% maintained their operations within the 60%-80% utilisation rate. Significant increases in sales of motor vehicles, chemicals and plastic products as well as office equipment, computing and accounting machinery pushed manufacturing sales up by 15.6% to RM262,984 million (January-July 2004: 19.3%; RM227,578 million), as shown in *Table 2.5*.

Overall output of **export-oriented industries** moderated by 0.1% during the first seven months of 2005. The moderation was due to the global downcycle for **E&E** products, in particular semiconductors, since the last quarter of 2004. Consequently, manufacturers made adjustments to their production and inventories. Despite the downcycle, semiconductors' contribution to the manufacturing sector remained high at 34.4%. Capacity utilisation of the industry, which is usually higher than the average of the manufacturing sector, also remained high at above 85% as manufacturers in the industry

CHART 2.4

Performance of Semiconductor Industry
(% annual change)



Source: Department of Statistics, Malaysia and Semiconductor Industry Association (SIA).

anticipated stronger demand in the second half of 2005.

Vibrant design and development (D&D) activities in the electronic and ICT industries, particularly software and systems development as well as high-tech knowledge-based manufacturing processes also contributed to the rebound in the E&E sub-sector. These industries are also expected to benefit from dynamic changes in consumer electronics, brought about by changes in technologies, innovation and new products in the market. Leading the technology growth are digital convergent products, such as eco-friendly flat-screen panel television sets, digital cameras, digital video disc (DVD) players and camera-phones and entertainment boutique outlets. The industry also benefitted from new development in auto-electronics such as systems and sensors for safety (airbags and antilock brakes) and dedicated auto-entertainment and information devices (navigation and entertainment circuits and display control systems).

In addition, the E&E industry also attracted new entrants such as electronic manufacturing service (EMS) companies. Some of these EMS companies, which are original design manufacturers (ODM), have developed into contract manufacturers for established companies, manufacturing products at more competitive prices under their own or the latter's brand.

Output of **rubber-based products,** comprising latex-based products, tyres and tubes and rubber footwear, continued to expand at a slower rate of 4.8% in the first seven months of the year (January-July 2004: 17.4%). Sales of rubber products also increased moderately by 5.7% during the period compared to 24.5% in the corresponding period last year. To strengthen industry position, manufacturers are developing new products with higher growth potentials, such as rubber-to-metal bonded automotive parts and components (engine mountings and suspension bushes) and off-road tyres.

The **wood-based industry** contracted by 6% (January-July 2004: 17.8%). Within the industry group, sales of plywood moderated to 2.5% (January-July 2004: 25.3%) while sales of windows and doors and joinery works contracted by 1.9% (January-July 2004: 19.5%). Unlike the E&E industry which was affected by slowdown in demand, contraction in the wood-based industry was affected by shortages in supply of raw materials, in particular supply of sawn rubber wood used by furniture manufacturers. Effective 8 June this year, the Government banned the export of rubber wood sawn timber to alleviate the supply shortage in the country as well as to intensify downstream value-added activities of the wood-based industry, such as engineered solid or hardwood flooring, windows, doors and joinery works. As a world-renowned manufacturer and exporter of rubber wood furniture, and to meet the continuing demand for high quality furniture and products, Malaysia is migrating to produce high-end wood-based product inputs.

Domestic-oriented industries trended upward recording a 7.6% increase in output (January-July 2004: 9.8%) on account of positive growth in transport equipment, plastic and chemical, food and beverages as well as paper and paper

TABLE 2.5

Sales of Manufactured Goods
January-July

Sector	RM million		Change (%)		Share (%)	
	2004	2005	2004	2005	2004	2005
Export-oriented industries	**127,607**	**137,714**	***23.0***	***7.9***	***56.1***	***52.4***
Electrical, electronics and machinery	104,586	113,656	*24.7*	*8.7*	*46.0*	*43.2*
of which:						
Semiconductors	62,615	65,511	*12.2*	*4.6*	*27.5*	*24.9*
Office, computing & accounting machinery	19,264	26,890	*141.1*	*39.6*	*8.5*	*10.2*
Rubber products	8,151	8,616	*24.5*	*5.7*	*3.6*	*3.3*
Wood products	7,655	8,304	*21.3*	*8.5*	*3.4*	*3.2*
Textiles, apparel and footwear	4,994	5,243	*4.4*	*5.0*	*2.2*	*2.0*
Professional and scientific and measuring equipment	2,221	1,895	*-0.8*	*-14.7*	*1.0*	*0.7*
Domestic-oriented industries	**99,971**	**125,270**	***15.0***	***25.3***	***43.9***	***47.6***
Chemicals, chemical and plastic products	35,663	43,183	*29.6*	*21.1*	*15.7*	*16.4*
Chemicals	24,898	29,453	*32.0*	*18.3*	*10.9*	*11.2*
Plastic	10,765	13,730	*24.4*	*27.5*	*4.7*	*5.2*
Crude oil refineries	16,286	26,048	*-5.6*	*59.9*	*7.2*	*9.9*
Iron, steel and metal products	16,342	21,112	*32.1*	*29.2*	*7.2*	*8.0*
Transport equipment	9,849	12,358	*0.1*	*25.5*	*4.3*	*4.7*
Food, beverages and tobacco	9,812	10,352	*11.7*	*5.5*	*4.3*	*3.9*
Paper and paper products	5,393	5,824	*15.3*	*8.0*	*2.4*	*2.2*
Non-metallic mineral products	5,747	5,427	*-0.9*	*-5.6*	*2.5*	*2.1*
Miscellaneous products of petroleum & coal	433	489	*16.9*	*12.8*	*0.2*	*0.2*
Others manufactured goods	446	477	*20.3*	*6.9*	*0.2*	*0.2*
Total	**227,578**	**262,984**	***19.3***	***15.6***	***100.0***	***100.0***

Source: Department of Statistics, Malaysia.

products. Improved domestic demand, coupled with improving consumer sentiment and higher disposable income, contributed to the continuous performance of these industries.

In the first seven months of 2005, output and sales of **transport equipment** increased and recorded double-digit growth of 10.2% and 25.5%, respectively (January-July 2004: 5.2%; 0.1%). The growth was led by higher production of commercial vehicles, motorcycles and scooters as well as higher capacity passenger cars, which increased by 42.8%, 20.4% and 5.8%, respectively. The turnaround was attributable to rising incomes of Malaysian consumers, launching of new models with improved designs and features and attractive financing facilities. Stronger bookings for popular new models further spurred the industry's performance. Impressive sales were also recorded in the domestic automotive parts and components market, which rebounded significantly by 21.9% during the first seven months of 2005 (January-July 2004: -4.8%).

Chemical products benefitted from the increase in output of industrial chemicals. Similarly, output of other chemical products accelerated, resulting from significant increase in sales of basic industrial chemicals by 25.3%. Likewise, increased uptake in the plantation sub-sector resulted in a 25.1%

improvement in sales of fertilizers and pesticides. Output of plastic products, which are manufactured into components of E&E and packaging materials, particularly for food processing industries, also expanded significantly by 18.8% (January-July 2004: 13%).

The **food, beverages and tobacco** industry, with a significantly higher output growth of 11.8%, contributed 9.9% to the overall manufacturing output (January-July 2004: 2%; 9.2%). Malaysia's capability as a food producer is gaining strength with total sales increasing by 5.5% to RM10,352 million, while food exports expanded by 8.8% to RM5,628 million. Main contributors to higher output and sales were cocoa and chocolate confectioneries, sugar refineries, vegetable and animal oils, flour and biscuits, soft drinks and other dairy products.

Output of **paper and paper products** recorded a strong growth of 8.9% in the first seven months of 2005 (January-July 2004: 4.7%). Sales of paper and paperboard containers and boxes also recorded an expansion of 9.6% while other paper products recorded a 12.4% increase during the same period. The industry is anticipated to grow further with the setting up of new and higher production capacity pulp and paper mills in Sabah and Sarawak. Malaysia's pulp and paper industry is also expected to benefit from the average annual increase of 3.1% in worldwide demand for pulp and paperboard amounting to 440 million metric tonnes by 2010, estimated by the Food and Agriculture Organisation (FAO). In addition, Malaysia is intensifying its R&D in non-wood fibres such as *kenaf* and oil palm waste to cater for increasing domestic and external demand.

Construction-related industries recorded a decline of 5.1% in the first seven months of 2005 (January-July 2004: 11.5%), affected by contraction in output of iron and steel and non-metallic minerals such as cement and ready-mixed concrete. Production of iron and steel bars and rods, galvanised iron sheets as well as welded iron and steel pipes registered slower growth in tandem with the slowdown in the construction sector. However, these industries recorded an upsurge in sales value of 58% (January-July 2004: 61.3%) largely due to higher prices.

Agriculture Sector

Increasing output from non-plantation crops...

Value added of the **agriculture sector** is set to grow by 4.8% in 2005 (2004: 5%), as shown in *Table 2.6.* The growth is partly attributed to higher output of crude palm oil (CPO) due to improved productivity and expanded matured areas. Value added in the non-plantation sub-sector, in particular food commodities, also expanded as a result of various programmes and measures that have been implemented to revitalise the sector. Consequently, the plantation and non-plantation sectors continue to play increasingly important roles in supplying basic inputs and raw materials to agro-based and other related industries.

Production of **CPO** is expected to increase significantly by 9.5% to 15.3 million tonnes in 2005 (2004: 4.6%; 14 million tonnes), on account of expanded matured areas and improvement in yield per hectare as well as higher palm oil extraction rate. The increase in production is also encouraged by fairly high CPO prices. During the first eight months of 2005, production of palm oil rebounded and surged by 14.9% (January-August 2004: -1.5%). This is partly due to improvement in the average yield of fresh fruit bunches to 12.33 tonnes per hectare (January-August 2004: 11.41 tonnes per hectare). Likewise, higher palm oil extraction rate of 20.09% was recorded during the same period (January-August 2004: 19.93%). Matured areas also expanded by 1.9%, mainly located in Sabah (19,025 hectares) and Sarawak (7,403 hectares). Overall, the total area planted with oil palm in Malaysia is expected to increase by 1.9% to reach 3.949 million hectares, taking into account new areas identified for the cultivation of oil palm, especially in Sabah and Sarawak. Of this total, 60% is owned by the private sector while 30% are smallholdings, organised under the Federal Land Development Authority (FELDA) and FELCRA Berhad and the rest comprise independent smallholdings. Malaysia remains the leading palm oil producer and exporter, arising from successes attained from intensive R&D activities, best agronomic practices as well as productivity improvement.

TABLE 2.6

Value Added in the Agriculture Sector
2004-2006
(in 1987 real prices)

	Growth (%)			Share to Agriculture (%)		
	2004	2005[1]	2006[2]	2004	2005[1]	2006[2]
Agriculture	***5.0***	***4.8***	***5.0***	***100.0***	***100.0***	***100.0***
Oil palm	*3.9*	*9.5*	*6.6*	*34.9*	*36.5*	*37.1*
Forestry and logging	*4.3*	*3.0*	*2.4*	*14.0*	*13.7*	*13.4*
Fishing	*5.5*	*-0.4*	*5.3*	*12.4*	*11.8*	*11.8*
Rubber	*16.5*	*-2.0*	*1.8*	*11.1*	*10.4*	*10.1*
Other agriculture[3]	*2.4*	*4.7*	*5.3*	*27.6*	*27.6*	*27.6*

[1] Estimate.
[2] Forecast.
[3] Including livestock, cocoa, paddy and miscellaneous agriculture such as fruits, copra, vegetables, tobacco, tea, flowers and pepper.

Source: Department of Statistics, Malaysia.

CPO is expected to trade at a moderately high average price of RM1,400 per tonne (2004: RM1,664 per tonne) in 2005. The palm oil industry is also expected to benefit from tight world supply of vegetable oils and fats as well as higher demand for palm oil from China, the 25-nation euro area and the US. The price of CPO is projected to trend up following higher prices of competing oils and fats, including soybean and rapeseed oils on account of increasing use of these oils for biodiesel in the US and the euro area. Consequently, the price of CPO increased to RM1,353 per tonne in August compared to RM1,298 per tonne in February 2005. Meanwhile, stocks stood at 1.33 million tonnes at end August 2005 as output exceeded exports. The stock level, however, is projected to decline as exports of palm oil, a trans-fatty-acid free oil, to the US are expected to increase due to higher demand arising from the imposition of compulsory labelling of all food products that contain trans-fatty-acids, by the US in January 2006. Demand from the euro area is also expected to rise on account of increasing use of palm oil for biodiesel.

TABLE 2.7

Oil Palm Area and Palm Oil Production
2004-2005

			Change (%)	
	2004	2005[1]	2004	2005[1]
Planted areas ('000 hectares)	3,875	3,949	*1.9*	*1.9*
Matured areas ('000 hectares)	3,451	3,516	*4.5*	*1.9*
Production ('000 tonnes)	13,976	15,300	*4.6*	*9.5*

[1] Estimate.

Source: Ministry of Plantation Industries and Commodities.

During the first seven months of 2005, output of **rubber** declined by 6.9% to 625,654 tonnes (January-July 2004: 24.5%; 672,164 tonnes) largely due to prolonged wintering that affected production. Total production of rubber is expected to decline by 2% to 1.14 million tonnes in 2005 (2004: 18.5%; 1.17 million tonnes) with decreasing planted area due to conversion of rubber plantations to other more lucrative and less labour intensive economic activities, mainly oil palm. Total land area now under rubber cultivation is estimated at 1.25 million hectares in 2005 (2004: 1.28 million hectares), a decrease of 2.5%, as shown in *Table 2.8.* To overcome the shortage of workers and reducing planted areas, the

BIOTECHNOLOGY – THE NEW GROWTH INDUSTRY

Introduction

Biotechnology is currently one of the fastest growing and leading industries that can enhance food security, healthcare and environmental safety. The US is the industry leader, while others including UK, Germany, Sweden, Australia, Japan, India, China, and Korea are joining the biotechnology bandwagon and are fast making their mark. Globally, there are about 5,000 biotechnology companies with a market capitalisation of USD700 billion and an annual turnover of USD50 billion. Together, these companies will create a biotechnology value chain with a captive market estimated at USD1.8 trillion by the year 2010.

Setting the Foundation for Biotechnology

Malaysia's venture into biotechnology started in the 1960s with strong involvement by government research institutions (GRIs). Early R&D investments in the agriculture sector were geared towards boosting yields of primary commodities, such as paddy and rubber. The emergence of biotechnology companies, however, has a shorter history, having its origin in the late 1990s, boosted by rising demand for food supplies and advances in the plantation sector. Both Government and private sector initiatives have laid the foundation for the development of the biotechnology industry, as their initial research in biology, agronomy and plant breeding advanced into biotechnology to produce, among others, high-yielding planting materials through tissue culture, good agronomic practices and crop protection to boost productivity and return on investment.

Biotechnology in Malaysia

Biotechnology is still an infant industry in Malaysia, given its recent history. Nevertheless, Malaysia's strong foundation in agriculture biotechnology (agrobio) and natural biodiversity provides the leverage to harness the potential of the high growth biotechnology sector. Malaysia's experience in commodities especially in palm oil, rubber and cocoa has led to a strong foundation in agrobio. Additionally, Malaysia's large rainforest contains a rich diversity of flora and fauna, which can be sourced to produce, among others, medicinal and health products. Leveraging on these advantages, the Government has identified three areas of biotechnology for commercialisation, namely agrobio, healthcare (including pharmaceutical and nutraceutical) and industrial biotechnology.

Biotechnology in the Agriculture Sector

With an estimated global annual value of USD6 billion in 2005, agrobio holds vast potential for biotechnology applications in Malaysia. Malaysia has successfully applied agrobio in practical genetic engineering works to improve food crops, fish breeding as well as meat production and quality. Agrobio has also improved yields of major plantation crops in the country and also the means to regenerate and mass propagate plantlets for pineapple, bananas, papaya and orchids for commercial farming. R&D in agrobio has led to the development and commercialisation of new products and processes which include vitamin E from palm oil, animal recombinant vaccines, new varieties and hybrids of horticulture crops, diagnostic kits for white spot virus syndrome of shrimps, and anti-fungal extracts from sea cucumbers.

Similarly, breeding of ornamental fish through agrobio has grown from a mere hobby into a lucrative industry in Malaysia. In 2004, the industry recorded 8.8% increase in net export of ornamental fish, valued at RM44.8 million (2003: RM41.1 million). For the first half of 2005, net export increased further by 10.2% to RM24.8 million (January-June 2004: RM22.5 million). The global industry, valued USD281 million in 2003 is estimated to increase to USD303 million in 2005.

Malaysia's untapped rich biodiversity also offers vast commercialisation potential. Biotechnology research by the Forest Research Institute Malaysia (FRIM) focusses on the enhancement of commercial values of the country's forest plants, medicinal plants and fragrance trees. FRIM has also labelled, catalogued and documented the country's flora and fauna. While the Government welcomes strategic international alliances in research and bio-prospecting activities, there is a need to regulate access to the nation's natural resources and protect her proprietary rights. To ensure this, the Access and Benefit Sharing Bill is currently being drafted and will be tabled in Parliament next year. The Government is also taking precautionary measures to regulate the industry through a Biosafety Bill, which will be tabled by end of this year. The Bill will cover biotechnology R&D, production and processing in Malaysia as well as imported genetically modified organisms (GMO) and products.

Biotechnology in Healthcare and Medicine

Globally, herbal medicine (neutraceutical and biopharmaceuticals) is becoming more popular and its market value is estimated to reach USD200 billion in 2008. Malaysia with its tropical rainforest provides vast potential for the development of neutraceutical and biopharmaceutical products to meet world demand. In this regard, bioactive compounds in *tongkat ali, pegaga, kemunting china, senduduk, kacip fatimah* and *misai kucing* are being researched for the treatment of cancer, eczema, diabetes and hypertension. With initial promising results, such research activities are expected to continue.

Commercialisation of Biotechnology

Worldwide, the private sector assumes the leading role in commercialisation and development of biotechnology. In Malaysia too, the private sector is expected to take the lead. However, funding for commercialisation of biotechnology research findings and inventions remains a challenge, as it usually is a high-risk investment requiring large capital and long gestation period. It is also a very knowledge-intensive venture requiring extensive specialised skills. To enhance commercialisation, the Government established relevant institutions to provide grants for pre-commercialisation and venture capital for prototype development and commercialisation to complement conventional bank financing.

A RM1 billion fund is being provided through the Malaysia Technology Development Corporation (MTDC) for companies involved in biotechnology and life sciences projects. Fourteen biotechnology projects have been approved and commercialised, utilising RM88.9 million from the fund. Another 65 biotechnology commercialisation projects amounting to RM615.5 million are being evaluated. Projects successfully commercialised include pan malaria test kit, natural anti-mosquito punch, production of rice rich in Vitamin A, essential fatty acids, aquaculture of tiger prawns, and low protein powdered or powder-free rubber gloves. Meanwhile, among projects that are being evaluated include phytoparmaceutical products for hypertension and ecological-friendly paper from palm waste.

Apart from bank and venture capital financing, aspiring bio-technopreneurs can also apply for grants from the Commercialisation of Research and Development Fund (CRDF) and Technology Acquisition Fund (TAF) to undertake commercialisation. CRDF provides grants for market surveys and research; product/process design and development; standards and regulation compliance; intellectual property protection; and demonstration of technology, while TAF facilitates the acquisition of strategic and relevant biotechnology for the industrial sector.

In addition, bio-technopreneurs also benefit from various tax incentives. The Government introduced various tax deductions and allowances to approved biotechnology companies or their holding companies in the form of group tax relief, double deductions for qualifying capital and R&D investments. Other incentives include Pioneer Status, Investment Tax Allowances, automatic exemption of import duties and sales tax on equipment and materials used, double deductions on expenses for promotion of exports and tax-exempt dividends paid to shareholders.

Government's Initiatives

National Biotechnology Policy

The National Biotechnology Policy (NBP), launched by the YAB Prime Minister on 28 April 2005, provides guidelines to spearhead the development of the biotechnology industry in Malaysia. The landmark policy will focus on three areas, namely agrobio, healthcare and industrial biotechnology with nine policy thrusts. The NBP will be implemented in three phases over a 15-year period, namely:

a. Phase I (2005-2010) - Capacity building which includes education and training of knowledge workers, developing intellectual property and legal framework, developing Malaysian branding, as well as industry and job creation;

b. Phase II (2011-2015) - Intensifying scientific development for commercialisation through new product development, developing spin-off companies, strengthening branding, and developing technology licensing capabilities; and

c. Phase III (2016-2020) - building international recognition by consolidating strength and capabilities in technology development, strengthening innovation and technology licensing and promoting Malaysian global companies.

Summary of Targets of The NBP

	Phase I (2005-2010)	**Phase II** (2010-2015)	**Phase III** (2015-2020)	**Total**
Policy Statements	Capacity Building	Creating business out of science	Turning Malaysia into global player	Biotechnology for Wealth Creation and Social Well-being
Creation of employment	40,000	80,000	160,000	280,000
Establishment of companies	25	25	50	100
Contribution to GDP (%)	2.5	4.0	5.0	5.0
Compounded Annual Growth (%)	32.8	21.7	14.7	23.7

Source: The National Biotechnology Policy

Malaysian Biotechnology Corporation

The Malaysian Biotechnology Corporation (MBC) is a one-stop agency with the main objective of developing the country's biotech industry. As a one-stop agency, the MBC will work closely with relevant ministries and agencies to develop the biotechnology industry in Malaysia. Some of the functions of the MBC include:

a. Catalysing commercial spin-offs to the private sector;

b. Facilitating market-driven R&D and commercialisation *via* funding and industry development services; and

c. Advancing R&D and commercialisation in agrobio, healthcare and industrial biotechnologies.

The National Biotechnology Directorate

The National Biotechnology Directorate (BIOTEK) at the Ministry of Science, Technology and Innovation (MOSTI) is established to promote and coordinate biotechnology R&D activities in the country *via* human resource development and commercialisation of public sector biotechnology R&D findings. BIOTEK also promotes private-public sector participation in national biotechnology programmes, through collaborative R&D works and outsourcing of the private sector R&D requirements to available qualified researchers from universities and GRIs.

BioNexus Malaysia

In addition to the NBP and the MBC, the Government also established BioNexus Malaysia (BioNexus). BioNexus is a network of centres of excellence based on the capabilities of existing institutions and companies, with specific specialisation in biotechnology. Three centres of excellence have been identified, of which two have begun operations using existing facilities. They are:

a. The Centre of Excellence for Agro-Biotechnology in MARDI and Universiti Putra Malaysia at Serdang;

b. The Centre of Excellence for Genomics & Molecular Biology in Universiti Kebangsaan Malaysia at Bangi; and

c. The Centre for Excellence for Pharmaceuticals & Nutraceuticals, to be established in BioValley, Dengkil.

Biofuel

The National BioFuel Policy was announced by the YAB Prime Minister on 11 August 2005. The Biofuel Policy and its various incentives are aimed at encouraging the use of biofuel as an alternative to petroleum-based diesel or fossil fuel, promoting downstream activities and expanding the uses and usage of palm oil. The patented B5 blend biofuel, is a palm diesel fuel with 5% palm olein blended with 95% fossil fuel. The biofuel technology was developed by the Malaysian Palm Oil Board and is also exported to Korea.

Demand for biodegradable fuels including palm diesel by developed countries such as the US, Japan, the EU and Korea, is expected to reach 10.5 million tonnes by 2007. Currently, major producers of biodiesel in the EU use rapeseed, soya bean, sunflower and other edible oils to produce the methyl esters for fuel. Malaysia, with 3.6 million hectares of oil palm plantation and more than 360 palm oil mills, has the capacity and capability, and is thus well-positionedto meet the increasing global demand for biodegradable fuels.

Prospects

The biotechnology industry is experiencing strong growth in revenues, employment and output worldwide. Malaysia aims to be an active participant in the industry by leveraging on her comparative advantages. The industry is expected to generate RM270 billion in revenue, create approximately 280,000 jobs and establish 100 companies by the year 2020. With the Government’s strong supportive policies and institutional framework, aided further by the growing pool of technical expertise and on going research activities, biotechnology will become one of the forefront niches of new growth industries to help elevate Malaysia to a higher plane of progress and development.

TABLE 2.8

Rubber Area, Yield and Production
2004-2005

	2004	2005[1]	Change (%) 2004	2005[1]
Total area ('000 hectares)	**1,282**	**1,250**	***-2.5***	***-2.5***
Smallholdings	1,156	1,135	*-1.7*	*-1.8*
Estate	126	115	*-9.4*	*-8.7*
Yield (kg per hectare)				
Smallholdings	1,365	1,400	*7.5*	*2.6*
Estate	1,290	1,320	*-3.9*	*2.3*
Total production ('000 tonnes)	**1,168**	**1,145**	***18.5***	***-2.0***
Smallholdings	1,097	1,077	*20.7*	*-1.8*
Estate	71	68	*-6.6*	*-4.2*
% of world production	***13.5***	***13.1***	***66.5***	***-3.0***

[1] Estimate.

Source: Ministry of Plantation Industries and Commodities and Department of Statistics, Malaysia.

Government encourages the wider use of Low Intensity Tapping System (LITS) and adoption of higher yield rubber clones as well as continuation in rubber replanting programmes. Efforts were also undertaken to consolidate uneconomic-sized rubber smallholdings into mini estates to enhance production, efficiency of operations and ultimately raise income of smallholders.

The average price of Standard Malaysian Rubber 20 (SMR 20) in the first eight months of 2005 increased by 3.8% to RM4.84 per kg (January-August 2004: RM4.66 per kg). The price of rubber is expected to remain strong in consonance with the higher price of synthetic rubber following rising world crude oil prices and increasing demand for natural rubber in China and Germany, particularly for the tyre industry. The strong rubber price was also due to tight supply from major producers of rubber, following severe drought during the first half of the year.

Output in the **fishing** sub-sector, comprising marine landing and aquaculture harvest, is expected to decline by 0.4% mainly due to lower landings of marine fish in the first half of the year. This was due among others to the effects of tsunami on 26 December 2004 and lower landings. Despite the declining output, this sub-sector continues to account for 12% of the overall agriculture sector's value added in 2005.

To further develop the fishing sub-sector, the Government introduced specific measures for coastal and deep-sea fishing as well as aquaculture. Deep-sea fishing, which has yet to

TABLE 2.9

Production of Other Agriculture
2004-2005
('000 tonnes)

	2004	2005[1]	Change (%) 2004	2005[1]
Cocoa	33.4	34.3	*-7.7*	*2.7*
Livestock				
Meat[2]	230	239	*3.0*	*4.0*
Poultry	927	980	*7.9*	*5.7*
Eggs[3] (million)	7,230	7,500	*0.9*	*3.7*
Milk[4] (million)	38.8	41.1	*6.0*	*6.0*
Miscellaneous agriculture				
Paddy	2,145	2,162	*-5.0*	*0.8*
Fruits[5]	1,142	1,207	*-32.4*	*5.7*
Pepper	20	20.1	*-9.1*	*0.5*
Tobacco[6]	115	103	*-4.2*	*-10.4*
Tea	12	10	*-27.3*	*-16.7*
Vegetable	1,000	1,100	*23.0*	*10.0*
Copra	10.3	12.0	*-12.0*	*16.5*

[1] Estimate.
[2] Including beef, pork and mutton.
[3] Number.
[4] Litre.
[5] Consists of starfruit, papaya, jackfruit, *ciku, durian*, guava, *langsat,* mango, mangoesteen, pineapple, banana, *rambutan,* watermelon and other tropical fruits.
[6] Green and dry tobacco leaves.

Source: Ministry of Agriculture and Agro-Based Industry and Ministry of Plantation Industries and Commodities.

be fully exploited is currently given high priority by the Government. Various efforts have been taken to develop deep-sea fishing, including issuance of more deep-sea fishing permits and providing training for fishermen. One of the training programmes, *Program Nakhoda*, conducted at *Institut Perikanan Malaysia,* aims to produce skilled seamen.

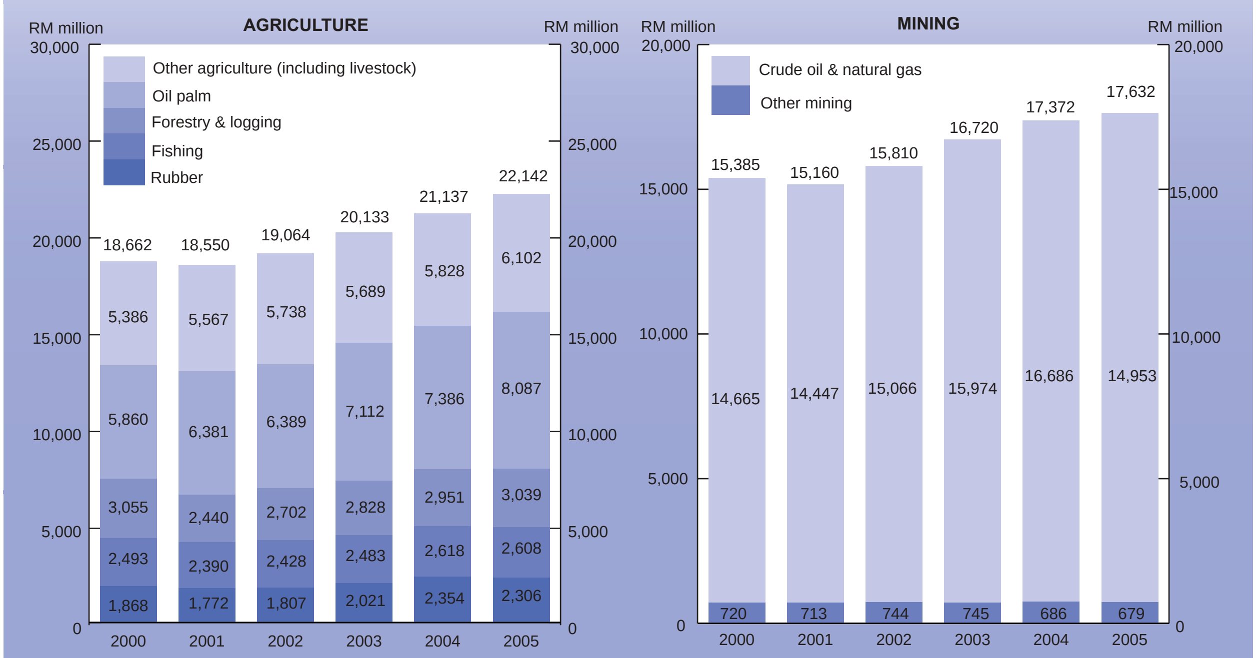
Success in aquaculture has been encouraging, with production estimated to increase significantly by 15.4% to about 250,000 tonnes in 2005. The increase is mainly due to expansion in hectarage from 13,844 hectares in 2001 to 15,680 hectares in 2005, involving an additional 15,650 ponds largely managed by private operators.

Other agriculture, comprising livestock, cocoa, paddy and miscellaneous agriculture, is envisaged to expand by 4.7% and contributes to almost one third of total value added in the sector. Livestock, the biggest contributor, is expected to grow by 5.2%, mainly due to higher production of beef (5.2%) and mutton (4%). Production of fresh milk, poultry and eggs is projected to increase by 6%, 5.7% and 3.7%, respectively. FELDA, RISDA and FELCRA are largely responsible for the increase in livestock production, particularly from rearing of cattle and goats in oil palm and rubber plantations, which contribute about 12% of total meat production. In addition, feedlot cattle rearing constitutes the bulk of production at about 54% and the balance, by individual farmers.

Cocoa production is poised to grow by 2.7% in 2005 compared to a contraction of 7.7% last year. The price of Standard Malaysian Cocoa 1B (SMC 1B) is projected to strengthen to around RM5,000 per tonne (January-August 2005: RM4,812 per tonne) following an expected shortage of global supply in 2005. This has encouraged cocoa planters to rehabilitate their holdings. The total planted area is expected to increase marginally by 0.2% to 678,600 hectares in 2005. Despite prolonged drought in the first half of 2005, paddy production is expected to increase by 0.8% due to higher yields of 3 tonnes per hectare in 2005 (2004: 2.8 tonnes per hectare). Value added of **miscellaneous agriculture,** which

CHART 2.5

Value Added of Major Commodities



Source: Department of Statistics, Malaysia.

includes fruits, vegetables, flowers, pepper, pineapples, copra, tea and tobacco, is expected to increase by 4.5% (2004: 1%) this year due mainly to higher production of fruits and vegetables. Fruit production is projected to expand by 5.7% in 2005 on account of various projects and programmes introduced by the Government, such as the Permanent Food Production Parks like the Selangor Fruit Valley in Rawang, and the utilisation of higher quality seeds and clones. Efforts taken to encourage fruit exports include the provision of phytosanitary certification services, promotions in potential markets and bilateral discussions to facilitate exports to countries such as Australia, China and Japan.

Mining Sector

Rising contribution from gas...

The mining sector is envisaged to expand moderately by 1.5% in 2005 (2004: 3.9%), as shown in *Table 2.10*. For the year, growth will emanate from higher production of natural gas, while oil production is expected to decline due to repair and maintenance works on oil installation facilities in the first half of 2005.

During the first eight months of 2005, **crude oil** production including condensates averaged 713,300 barrels per day (bpd), a reduction of 5.9% from 757,900 bpd in the same period last year. Based on Petroliam National Berhad's (PETRONAS) planned work programme for 2005, oil production for the whole year is expected to decline by 2.4% with an average of 743,000 bpd (2004: 761,000 bpd). In tandem with higher world crude oil prices, the price of Tapis Blend increased to an all time high of USD71.86 per barrel on 29 August 2005. The escalating oil price is largely due to rising demand, particularly from China and US amidst tight supply in the global oil market. The average US Light Sweet Crude price for the first eight months of 2005 increased by 42% to USD54.20 per barrel (January-August 2004: USD38.21 per barrel). The Government has taken several steps to reduce the dependence on diesel and petrol, including encouraging the use of natural gas and biodiesel for vehicles.

The production of **natural gas** expanded 11.8% to 5,703 million standard cubic feet per day (mmscfd) in the first eight months of 2005 (January-August 2004: 3.3%; 5,099 mmscfd). Total production for the year is projected to increase by 5% to 5,721 mmscfd (2004: 5,449 mmscfd) in tandem with the anticipated increase

TABLE 2.10

Value Added in the Mining Sector
2004-2006
(in 1987 real prices)

	RM million			Change (%)		
	2004	**2005[1]**	**2006[2]**	**2004**	**2005[1]**	**2006[2]**
Mining sector	**17,372**	**17,632**	**18,453**	***3.9***	***1.5***	***4.7***
Crude oil and natural gas	16,686	16,953	*17,739*	*4.5*	*1.6*	*4.6*
Other mining	686	679	*714*	*-8.0*	*-1.0*	*5.1*

[1] Estimate.
[2] Forecast.

Source: Department of Statistics, Malaysia.

TABLE 2.11

Production and Reserves of Crude Oil and Natural Gas
2004-2005

	2004	2005[1]	Change (%) 2004	2005[1]
Crude oil				
Production[2] ('000 barrels per day)	761	743	*3.1*	*-2.4*
Reserves (billion barrels)	3.8	4.1	*-15.6*	*7.9*
Reserves/ production (years)	17	18	*6.3*	*5.9*
Natural gas				
Production[3] (million standard cubic feet per day)	5,449	5,721	*8.7*	*5.0*
Reserves (trillion standard cubic feet)	87	85	*-2.3*	*-2.3*
Reserves/ production (years)	40	37	*-9.9*	*-7.5*

[1] Estimate.
[2] Including condensates.
[3] Excluding flaring and reinjection.

Source: PETRONAS.

in new operational gas fields. During the first eight months of 2005, three new gas fields were discovered. These were Bunga Kesumba, located in offshore east coast of Peninsular Malaysia and Golok Barat and Belum, Sarawak.

Construction Sector

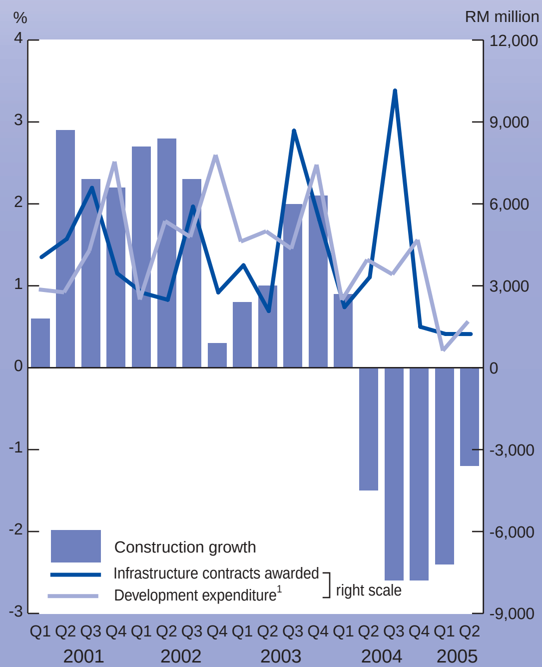
Construction sector consolidates...

The **construction sector** contracted by 2.2% during the first half of 2005 (January-June 2004: -0.3%) due mainly to lower civil engineering activity. The residential sub-sector, however, remained active while the non-residential sub-sector improved further during the period as business confidence and consumer sentiment remained strong. For the year as a whole, the sector is envisaged to register a smaller contraction of 1.1% (2004: -1.5%) on account of some improvement in civil engineering activity in the second half.

Activity in the **civil engineering sub-sector** tapered off during the first half of 2005, partly due to the reduction in the number and value of infrastructure contracts awarded compared to the corresponding period last year. Increasing private sector construction activities, especially in oil and gas fabrication works as well as water pipe-laying projects, cushioned the contraction in public civil engineering works. Ongoing major projects include the Stormwater Management and Road Tunnelling (SMART) project for flood mitigation and traffic dispersal in Kuala Lumpur, KL-Putrajaya Highway, upgrading of Kuching International Airport as well as construction of Low Cost Carrier Terminal at Kuala Lumpur International Airport (KLIA). In addition, the implementation of the RM500 million maintenance works on existing public buildings and facilities is expected to further support the sub-sector.

CHART 2.6

Construction Growth, Development Expenditure and Infrastructure Contracts Awarded

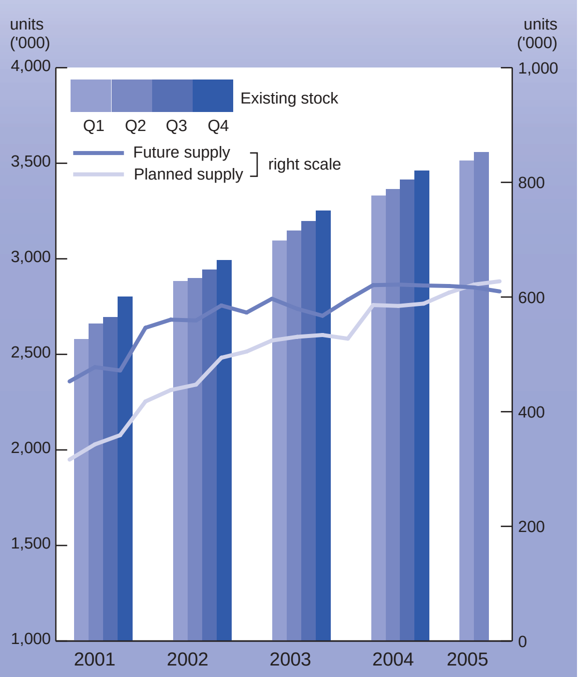


[1] Selected ministries.
Source: Various agencies.

Activity in the **residential sub-sector,** on the other hand, remained encouraging during the first half of 2005 on the back of favourable economic and business conditions, rising household income, attractive loan packages, low mortgage rates, favourable labour market conditions as well as increasing proportion of young working population to support demand for housing. A total of 95,858 houses were added during the period, resulting in total existing stocks increasing by 2.8% to 3.558 million units. Housing starts edged up 5.9% (January-June 2004: 2.1%), with 83.5% comprising terraced and strata titled units. Backed by higher disposable income and a preference for better quality housing as well as new lifestyle-based features, sales of new housing schemes priced at RM250,000 and above, strengthened to 32% during the first half of 2005 (January-June 2004: 19.1%). In the second quarter of 2005, house prices continued to trend upwards, albeit moderately, as reflected in the 1.7% increase in the House Price Index (Q2 2004: 5.7%).

CHART 2.7

Residential Supply Indicators



Source: National Property Information Centre (NAPIC).

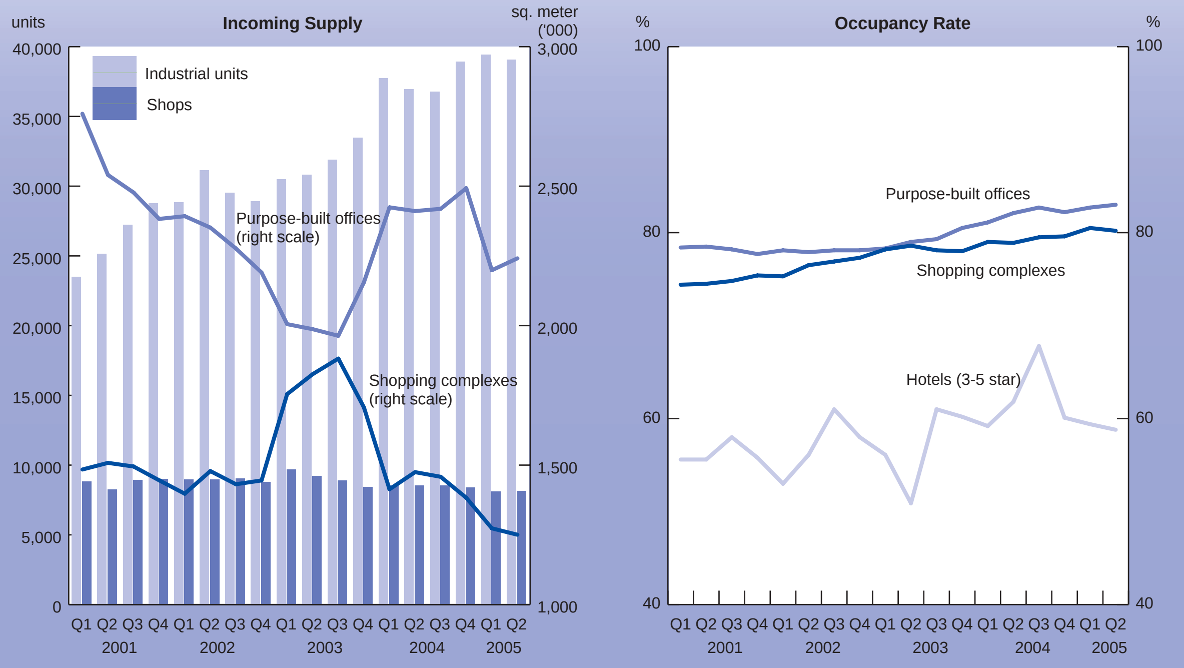
In the **non-residential** segment, office space increased by 522,231 square (sq.) metres, representing 3.7% of the total stock of 14.004 million sq. metres as at end-June 2005 (end-June 2004: 432,761 sq. metres; 3.2%; 13.482 million sq. metres), mostly in the Klang Valley. Occupancy rate of office space remained high at 83% during the period (end-June 2004: 82.1%), encouraged by stronger performance of the private sector, especially service-related businesses, including relocation of regional and operational headquarters of foreign companies. Meanwhile, total existing space in shopping complexes rose by 304,430 sq. metres or 4.1% of the total stock of 7.281 million sq. metres as at end-June 2005 (end-June 2004: 600,049 sq. metres; 8.6%; 6.976 million sq. metres). The occupancy rate of shopping complexes rose to 80.2% (end-June 2004: 78.9%) supported by favourable business conditions and increased consumer spending.

Property transactions increased marginally by 0.5% in the first half of 2005 with the value amounting to RM28,508 million (January-June 2004: 41.9%; RM28,139 million). Residential transactions contracted by 1.3% during the period while transactions for industrial, commercial and agriculture sub-sectors increased by 9%, 7.6% and 4.4%, respectively. Overall property transactions involving foreigners swelled by 51.3% during the first half of 2005 with the value reaching RM7,553 million (January-June 2004: 78.3%; RM6,917 million). As for residential transactions, the volume rose sharply by 50.8% with a total value of RM2,161 million during the period (January-June 2004: 87.2%; RM879 million).

In response to limited domestic construction opportunities in the last two years, local construction companies which have garnered considerable experience and built up their reputation during boom times have ventured abroad. From 1987 to June 2005, Malaysian construction companies completed a total of 246 projects abroad worth RM13.1 billion. Another 50 projects valued at RM13.9 billion are ongoing. Most of these projects are in India and the Gulf and ASEAN countries, involving the construction of highways, residential units and commercial buildings.

CHART 2.8

Non-residential Supply Indicators



Source: National Property Information Centre (NAPIC).

Services Sector

A vibrant services sector...

The **services sector** continues to play an important role in the economy. In 2005, activities in the services sector are expected to grow further by 5.8% (2004: 6.8%), higher than the overall GDP, and broad-based with all sub-sectors registering positive growth. Consequently, the services sector's share to GDP is envisaged to be higher at 57.8% (2004: 57.4%), maintaining its position as the largest sector in the economy with strong potentials in new growth areas. Growth emanates largely from robust expansion in most sub-sectors with transport, storage and communication recording the highest growth of 7.4% (2004: 8.5%). Strong performance in wholesale and retail trade, hotels and restaurants; and finance, insurance, real estate and business services is expected to further reinforce the overall growth of the services sector.

The expansion in **transport, storage and communication** is mainly on account of increase in trade and travel-related activities as well as continued pick-up in the telecommunications industry. All modes of transportation are expected to expand as a result of increased flight frequencies, connectivities and destinations, improved transport infrastructure, particularly ports and roads as well as higher load capacities due to rapid growth in tourism and trade activities. The emergence of new manufacturing-related services such as operational headquarters (OHQs), logistics and regional distribution centres (RDCs) and international procurement centres (IPCs) further support growth of the sub-sector.

Key performance indicators of the sub-sector point towards robust growth in 2005. During the first half of 2005, the number of vehicles on tolled highways expanded by 7.5% (January-June 2004: 6.4%) while rail commuter revenue grew 9.5% (January-June 2004:13.6%). As for

TABLE 2.12

Services Sector Performance
2004-2006
(in 1987 real prices)

	Change (%)			Share of GDP (%)		
	2004	2005[1]	2006[2]	2004	2005[1]	2006[2]
Electricity, gas and water (utilities)	*8.1*	*6.3*	*6.1*	*4.1*	*4.2*	*4.2*
Transport, storage and communication	*8.5*	*7.4*	*7.1*	*8.8*	*9.0*	*9.1*
Finance, insurance, real estate and business services	*6.3*	*5.3*	*5.4*	*15.1*	*15.1*	*15.1*
Wholesale and retail trade, hotel and restaurants	*7.1*	*6.9*	*6.5*	*14.3*	*14.6*	*14.7*
Government services	*6.5*	*3.5*	*5.1*	*7.3*	*7.2*	*7.2*
Other services	*4.9*	*5.0*	*5.9*	*7.8*	*7.8*	*7.8*
Total	***6.8***	***5.8***	***6.1***	***57.4***	***57.8***	***58.1***

[1] Estimate.
[2] Forecast.

Source: Department of Statistics, Malaysia.

port services, the overall container volume throughput handled at major ports grew by 3.3% to 5.8 million twenty-foot equivalent units (TEUs) (January-June 2004:15.9%; 5.6 million TEUs). The introduction of value-added services by port operators, including expanding distriparks and support facilities, a more integrated port infrastructure, comprehensive services and arrivals of major shipping lines have contributed significantly to the overall growth of port activities. For example, Westport in Port Klang has established its own tugboat and pilotage services to handle vessels, resulting in shorter vessel waiting time. With respect to integrated port infrastructure, Pelabuhan Tanjung Pelepas (PTP) in Johor developed a 400-hectare free zone in its vicinity equipped with multi-modal infrastructure facilities. In addition, PTP developed an international *halal* distribution hub within its free zone area focussing on activities involving regional and international distribution of *halal* products. After five years of operation, PTP has established itself as Malaysia's largest container terminal and was awarded the "Container Terminal of the Year" at the 2004 Asia Logistics Awards. Likewise, Northport in Port Klang has set up a Vehicle Transit Centre which serves as a vehicle distribution hub for the ASEAN region. A review of maritime transport by United Nations Conference on Trade and Development (UNCTAD) in 2004 ranked Port Klang as the 12th largest in the world in terms of volume (million TEUs), while PTP emerged the 16th largest.

As for **air transport,** the advent of low-cost carriers has made travel more affordable. This, together with aggressive marketing strategies by airlines and tour operators, especially in new markets, has resulted in an increase of 14.5% to 10.9 million passengers in the first half of 2005 (January-June 2004: 24.2%; 9.5 million). Passenger traffic growth at KLIA is expected to increase by 6.6% to 22.5 million in 2005 (2004: 20.6%; 21.1 million). The surge in air passenger traffic volume in KLIA is attributed to significant growth of no-frills airlines, higher tourist arrivals, increased flight frequencies of several international airlines and new landings of other international airlines. Air cargo recorded higher growth of 12.1% in the first half of 2005 (January-June 2004: 9.9%), mainly due to aggressive promotion and expansion of services by respective airlines, including increased flight frequencies and cargo destinations. Exporters are increasingly using air cargo for shipments and transshipments not only to benefit from competitive rates but also faster delivery time to meet just-in-time delivery and the special needs of fresh produce like vegetables, fruits, cut flowers and frozen food.

The **communication industry** continued to record strong growth of 9.7% in the first half of 2005 (January-June 2004: 10.1%), resulting from rapid expansion in mobile phone usage, Internet and broadband services. As at end-June 2005, mobile phone subscribers rose by 33.5% to reach 16.6 million users (end-June 2004: 24.8%; 12.4 million), registering a 63.3% penetration rate. The intrinsic features of mobile phones with frequent introduction of new and innovative uses and cheaper mobile phones which are in sync with current lifestyles, continue to enhance its popularity as a communication tool. Competitive charges and rates for postpaid and prepaid lines and short message services (SMS), multimedia applications as well as widespread and innovative use of SMS, further encourage the usage of mobile phones. SMS increased significantly to 7,394 million in the first half of 2005 (January-June 2004: 4,084 million). In comparison, the number of fixed line subscribers declined further by 4.9% to 4.3 million (end-June 2004: -1.6%; 4.5 million) despite lower charges compared to postpaid and prepaid lines as well as better coverage and services. As at end-June 2005, the number of Internet subscribers rose by 14.5% to reach 3.6 million (end-June 2004: 14.2%; 3.1 million) and Internet users also increased by 14.5% to reach 10.7 million, accounting for 41% of the total population (end-June 2004: 14.2%; 9.4 million; 36.6%). Meanwhile, broadband services rose markedly by 103.2% to reach 353,978 subscribers (end-June 2004: 225.1%; 174,234), in line with the progress made towards a knowledge-based society and economy.

The **finance, insurance, real estate and business services sub-sector** is envisaged to grow by 5.3% in 2005 (2004: 6.3%), supported by higher bank lending, insurance and business services activities. Bank lending remained robust on the back of strong consumption spending and continued expansion in private investment activity, with loan applications, approvals and disbursements recording growth of 15.6%, 7.4% and 9%, respectively in the first half of 2005. Insurance premiums rose significantly, driven by strong consumer demand for investment-linked life insurance and endowment products. Conventional insurance premiums grew by 8.6%, while takaful premiums increased by 50.6% during the period.

Growth momentum of the **wholesale and retail trade, hotels and restaurants sub-sector** is expected to be sustained at 6.9% in 2005 (2004: 7.1%), following higher disposable income, strong domestic consumption spending as well as higher tourist arrivals and establishment of new retail outlets. Meanwhile, the introduction of creative and innovative retail store concepts supported the growth in retail trade. In addition, retail sales also benefitted from the growing number of foreign travellers cum shoppers. In 2005, it is expected that tourists will spend RM8,500 million on shopping in Malaysia, representing an increase of 28.8% from RM6,600 million in 2004. With aggressive promotions and marketing campaigns in niche markets, especially in West Asia and South Africa, the retail industry is expected to gain from the arrivals of more high-spending tourists.

Gradual liberalisation of the retail industry, which allows foreign-owned hypermarkets to open outlets in Malaysia, is also expected to spur growth of the industry. Foreign-owned hypermarkets are becoming popular among Malaysians, attracting customers with their ‘all-under-one-roof’, modern, convenient and competitive pricing concept. Currently, there are four foreign-owned companies operating 37 hypermarket outlets in major cities, mostly in the Klang Valley, Johor Bahru and Penang compared with 14 outlets in 1999. New hypermarket outlets are also expected to be established in the East Coast of Peninsular Malaysia, Sabah and Sarawak.

Tourism continues to maintain its position as the second largest foreign exchange earner. In

SHARED SERVICES AND OUTSOURCING: LEVERAGING MALAYSIA'S POTENTIAL

Background

Shared services and outsourcing (SSO) industry is a new source of growth for Malaysia. The industry has grown tremendously in the last few years, securing world recognition for Malaysia as a global outsourcing hub. A recent survey by Deloitte in 2005 ranks Malaysia as number one, ahead of Bangalore in customer support and back-office processing services.

The term "SSO" encompasses both outsourcing and offshoring activities. Shared services is an arrangement where common services are provided by a single organisation leveraging on economies of scale, such as outsourcing and call-centre consolidation. Outsourcing is to seek resources outside an organisational structure, usually to reduce costs and to exploit competencies of other entities. Offshoring is the provision of services from a country that is geographically removed from the client, for example, services provided to a US enterprise by a service provider located in a developing country.

Tracing the history of the SSO industry, large investments in global ICT infrastructure in the 1990s have been the impetus to the growth of the industry. Motivated by the need to increase profitability and shareholder returns, large corporations from developed economies resorted to cost cutting measures by outsourcing business processes to foreign locations with lower cost structures. The "Y2K" software problem in 2000 is often cited as the first wave of the industry and India became the first entrant. Thus far, almost 350,000 workers are employed in this industry in India and is projected to grow 41% annually.

The SSO industry can assist in bridging the economic gap between developed and the more advanced developing economies which have relevant infrastructure and skills. These strategies, which have become a necessity for ensuring competitiveness, is gaining momentum and will continue to dominate business strategies in the future. It has been reported that at the end of last year at least 400 of the Fortune 500 companies utilised offshore services. In developing economies, it has been estimated that a total of 3.5 million jobs will be created in the SSO industry over the next few years.

Today, the global SSO industry is starting to mature. Global players have begun to give higher consideration to other factors such as soft skills and economic stability. A.T. Kearney undertook a global assessment and ranking exercise of various economies in 2004 based on these criteria. The report ranked Malaysia third in the world in SSO, as shown in *Chart 1.* Taking cognisance of the global industry's growth which is expected to exceed 8% with its value projected at USD750 billion by 2006, Malaysia is strengthening its efforts to further enhance her competitive advantage in this industry.

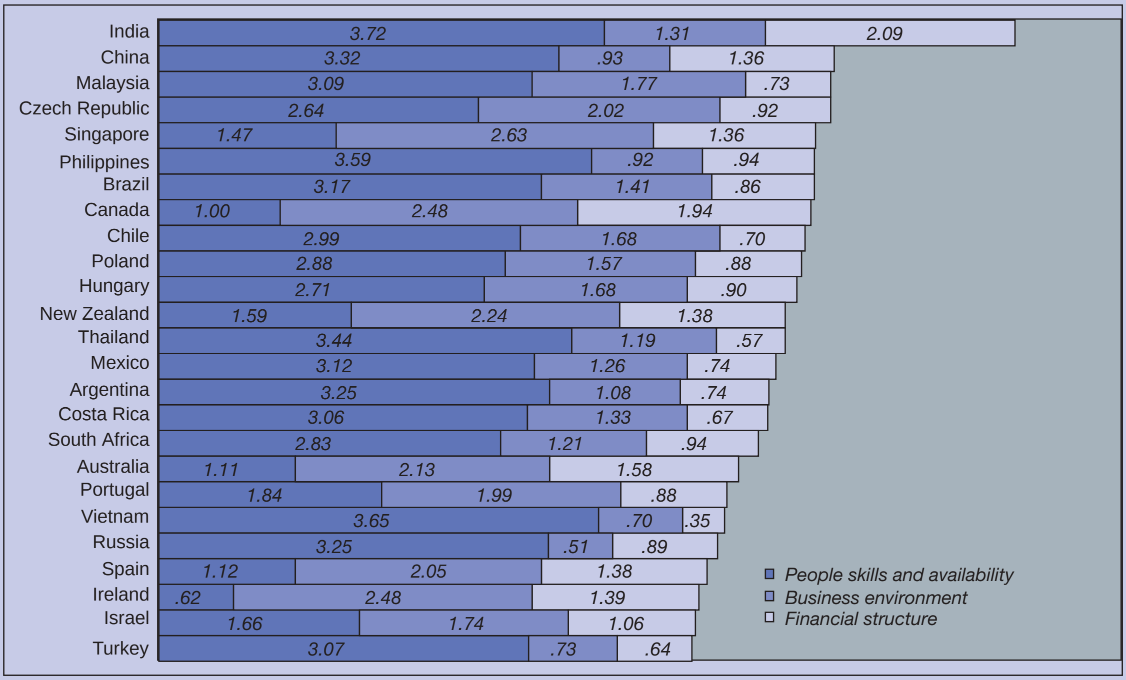
Environment for the SSO Industry

Countries like India, China and the Philippines, traditional hubs of the SSO industry, currently account for some 50% of the global industry. Malaysia too, is fast gaining its market share in this industry. Factors in favour of Malaysia include first-class infrastructure, competitive cost structure, conducive business environment, strong government support, English speaking workforce and, more importantly, political stability.

Deloitte survey "The Asian Advantage in the Outsourcing Revolution" (2005), places Malaysia as an emerging contender to be reckoned with. The report is bullish on Malaysia's position, challenging the current traditional hubs. It ranks Malaysia first in two out of five categories of shared services – customer support and back-office processing. Malaysia is ranked second in supply chain management, third in IT support and fourth in analytics. The report acknowledges that Malaysia draws much

CHART 1:

A.T. Kearney Offshore Location Attractiveness Index (2004)



advantage from the Multimedia Super Corridor (MSC). With more than 40% of the population below the age of 25 and a literacy rate of 95.1%, Malaysia's pool of knowledge workers is expected to grow in the coming years. Prospects for Malaysia are encouraging as observed by A.T. Kearney that "Malaysia is an often overlooked, but natural choice for offshore services."

Multimedia Super Corridor: Malaysia's Node to the SSO Industry

The rapid growth of the SSO industry in MSC is a fairly new phenomenon, primarily driven by offshoring services. This growth is supported by waves of offshore projects moving from more developed and high-cost economies. Offshoring activities are propelled primarily by traditionally outsourced processes such as call-centre support, IT support and back-office processing. The inherent advantage of the MSC attracted the SSO industry into Malaysia. To date, 48 companies involved in SSO have been given MSC status, accounting for 12,000 or 40% of total jobs in MSC. As at end 2004, revenue of SSO companies in the MSC was RM2.04 billion. It is estimated that by end 2005 revenue from the same companies will increase to more than RM2.58 billion, representing an increase of 30%. Through its phenomenal growth, the SSO industry is now a pillar to the development of MSC.

The number of companies is expected to grow and expand further especially with the presence of big players which have set up business process outsourcing (BPOs) in Malaysia such as DHL, IBM, Hong Kong and Shanghai Banking Corporation (HSBC), Standard Chartered Bank, Shell, Motorola and Nippon Telegraph and Telephone Corporation (NTT). HSBC has a big presence in the MSC and in 2004 alone had created some 2,000 jobs in processing and customer service activities for its group of companies, including those in Australia, New Zealand, Singapore, the United Kingdom and the US. The Shell Group has also made Malaysia its hub for its global IT support centre with a staff strength of 1,000 personnel, of whom about 90% are Malaysians.

Malaysia is fast gaining worldwide recognition for providing highly skilled knowledge workers at competitive rates in an attractive business environment. Moving forward, Malaysia is now progressing into the next wave, Knowledge Process Outsourcing (KPO), as shown in *Chart 2*. This entails business management and integration as well as business transformation requiring high skilled human resources in dealing with more complex and demanding environment.

CHART 2:

Phases in the SSO industry

First Wave		Current Wave	Next Wave	
Technology Infrastructure	**Business Applications**	**Business Processes**	**Business Management & Integration**	**Business Transformation**
• Telecoms	• Vertical (Industry Specific) Applications	• Customer Relations Management (CRM) Billing	• Business, Finance and Project Management	• Global Business Integration
• Device Management	• Horizontal (Process Specific) Applications	• Administration Finance	• Sourcing and Procurement	• Research, Product Design and Development
• Hosting		• Human Resource Training	• Process Design and Engineering	• Investor Relations and Management
• Customer Support		• Supply Chain	• Marketing, Sales	• Market Strategy
ITO[1]		**BPO[2]**	**KPO[3]**	

Note:

[1] Information Technology Outsourcing

[2] Business Process Outsourcing

[3] Knowledge Process Outsourcing

Technology Infrastructure	Automated systems that support business applications spanning across various countries
Business Applications	Software development and maintenance services for ICT-based applications used by businesses
Business Processes	A variety of front office and back office service functions. May be categorised into core (specialised to the business) and non-core activities
Business Management & Integration	Management of high impact, large scale projects and divisional operations spanning across various regions
Business Transformation	High value service activities requiring executives and technologists experienced in specific global industries

In the meantime, the SSO global market continues to grow in size and sophistication in tandem with the maturity of the industry. In consonance with the continued growth and progress towards the next wave, the demand for high value-added activities are expected to increase, which in turn will lead to accelerated demand for higher skilled knowledge workers. For Malaysia to continue to be a key SSO hub, the nation has to gear and prepare for the future niches of the SSO industry.

Realising Malaysia's Potential

The contribution of the services sector to GDP was 57.4%, in 2004, accounting for 50.3% of total employment. Using the benchmark in developed countries where the services sector's contribution to GDP is more than 70%, this sector, with its diverse activities, has immense potential for further development in Malaysia. The SSO, as a growing component of the services sector, is set to become one of its major contributors.

To ensure that Malaysia continues to be in the forefront of the SSO industry, Malaysia has to articulate a number of strategies. Firstly, branding Malaysia as a major global hub for SSO activities will be vital for the growth of the industry. Thus, there is further need to significantly increase awareness of Malaysia's competitiveness in international markets. International promotions and campaigns would highlight Malaysia's unique tagline "The Best of All Worlds". In addition, leveraging on the country's strengths, the Government has identified niche areas such as creative multimedia, Pan-Asian services (e.g. multi-language and contact centre support), business continuity and specific sectors, namely energy, finance, logistics and high-technology, for development.

Secondly, the Government views human capital development as crucial for the nation to be a big player in the SSO industry. In the long term, human capital has to be resilient and flexible to changing demands. Malaysia is strategising its human capital to match demands of the industry. In line with this, the Government views a reform in the education system a prerequisite, requiring teaching and learning methods that create an environment for students to think creatively, take risks and be discovery-oriented. In addition, human capital should be nimble and flexible enough to compete in the global market.

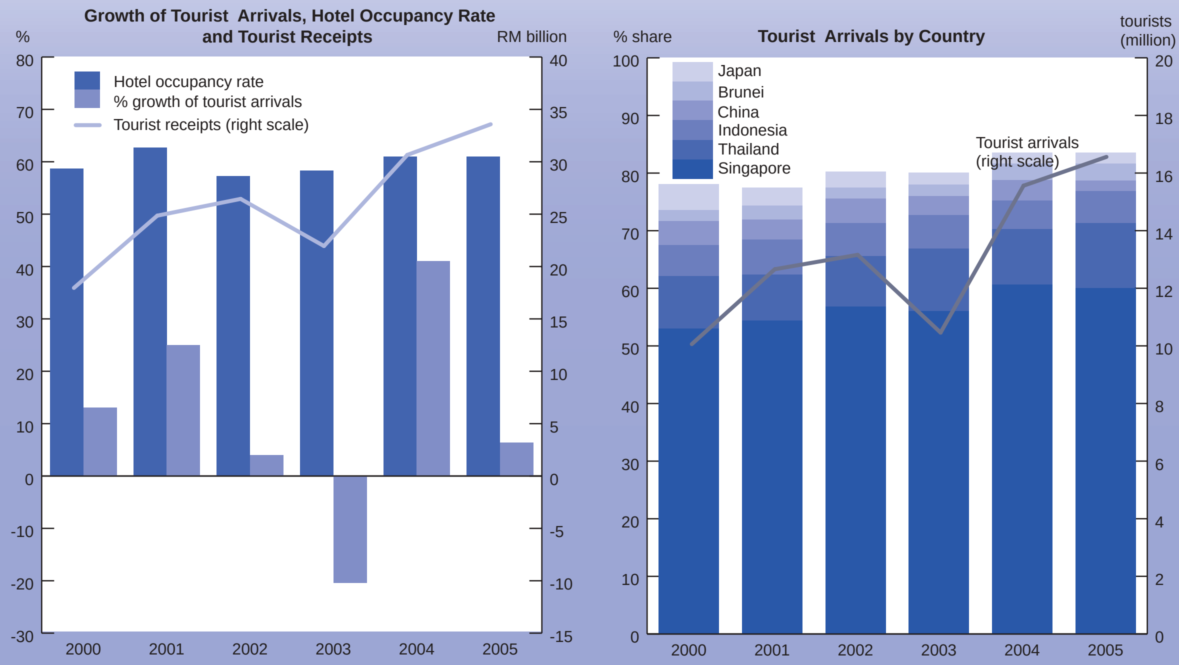
Malaysia's third strategy is to strengthen third party vendors through the "Outsourcing Malaysia" initiative. Incentives will be provided to local outsourcing service providers to develop world-class competencies and large scale operations in order to attract outsourcing businesses. Thus, it is expected that the presence of multinationals (MNCs) in Malaysia will serve as a significant customer base for local third party vendors. Local companies such as SnT Global in supply chain management, EPIC-I and Symphony House in finance related processes and Vsource and Scicom for call-centres have made inroads in the outsourcing business. The estimated revenue generated by these companies was approximately RM300 million in 2004.

Conclusion

The commitment of the Government to ensure Malaysia remains in the forefront of the SSO industry is reflected in its strategies to leverage on its core competencies and building an eco-system supportive to the industry. This will enable Malaysia to rapidly advance to the high value activities of the next wave, making Malaysia the "natural" choice for the SSO industry.

CHART 2.9

Tourism Industry



Source: Malaysia Tourism Promotion Board.

conjunction with aggressive promotions in new and non-traditional markets, particularly in West Asia as well as increasing number of international conferences and exhibitions held in the country, tourist arrivals have increased by 3.5% to reach 8.2 million during the first half of 2005 (January-June 2004: 71.7%; 7.9 million). Consequently, average hotel occupancy rate improved to 61% (January-June 2004: 59.7%). In terms of market share, tourists from the ASEAN region, especially Singapore, Thailand and Indonesia constituted 60%, 11.4% and 5.5%, respectively. The highest monthly tourist arrivals was recorded in March 2005 with an all-time high of 1.42 million tourists. Based on the average monthly tourist arrivals of 1.37 million in the first half of 2005 (average 2004: 1.31 million), tourist arrivals for the year are expected to reach 16.7 million or an increase of 6.4% (2004: 15.7 million; 48.5%). Tourist spending in 2005 is estimated to concomitantly increase by 11.8% to about RM33,200 million. In addition to rising contribution from foreign tourists, domestic tourism is expected to benefit from the implementation of the five-day workweek in the public sector.

Growth in the **government services sub-sector** as anticipated, continued to expand at a slower rate of 3.5% (2004: 6.5%). The expansion was due in part to higher expenditure on emolument, which also included increases in housing allowances for several categories of civil servants during the year, as well as payments for professional and technical services.

In line with moderate expansion in manufacturing activities and sustained domestic consumption, the **utilities sub-sector** is expected to increase by 6.3% (2004: 8.1%) with increases in demand for electricity by all categories of users, namely industrial, commercial and household. Maximum demand for electricity peaked at 12,493 megawatts (MW) in May 2005. Electricity sales rose by 5.5% during the first half of 2005 (January-June 2004: 8.9%).

Other services, made up of community, social, and personal services as well as imputed rent of owner-occupied dwellings, is anticipated to register an increase of 5% in 2005 (2004: 4.9%). The growth of this sub-sector is partly attributable to rising demand for private healthcare and education services. The continuous efforts in spearheading the promotion of both health and education tourism have brought about great benefits to this sub-sector. To date, there are 35 private hospitals offering various services to both local and foreign patients. Given the competitive pricing and quality of healthcare services available in the country, it is envisaged that these services will expand further and generate RM400 million in foreign exchange earnings in 2005 (2004: RM105 million). Similarly, apart from 17 public universities, the number of private institutions of higher learning in the country has increased to 559, of which 26 have been accorded university status. The total number of foreign students studying in Malaysia is expected to increase by 22.9% to reach 50,000 by end of the year (2004: 26.1%; 40,686).

Export Performance

Exports remain strong...

Malaysia's gross export earnings remain strong despite moderate expansion in global trade. Gross exports are projected to grow by 10.8% for the whole of 2005 (2004: 20.8%), given the favourable performance of 10.7% during the first seven months of the year, as shown in *Table 2.13.* This growth is supported by 10.4% growth in exports of manufactured goods (2004: 19.6%), due to demand for electronic products, particularly personal computers (PCs) and ICT products. Likewise, growth in demand for resource-based products is expected to drive exports of non-electronic products. Exports of major commodities are expected to grow by 11.6% (2004: 20.2%), on the back of 19.7% growth in exports of major minerals and 1.7% growth in exports of major agriculture produce.

Exports of Manufactured Goods

Manufacturing exports moderated, expected to pick up in second half of 2005...

Growth of **manufactured goods**, the biggest export earner for Malaysia, moderated during the first seven months of 2005, as E&E experienced slowing demand since the fourth quarter of 2004 in tandem with the downcycle of global demand for semiconductors. Exports of E&E increased by 8.3% during the first seven months of 2005 (January-July 2004: 17.4%), largely contributed by higher receipts from electronic equipment and parts. Meanwhile, exports of non-E&E products, including petroleum and transport equipment, continued to expand

TABLE 2.13

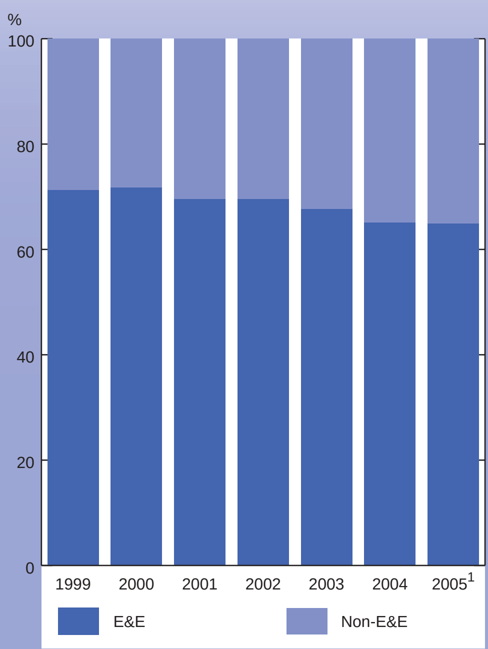
Gross Exports
January-July

	RM million		Change (%)		Share (%)	
	2004	2005	2004	2005	2004	2005
Manufactured goods	221,918	242,421	*20.8*	*9.2*	*82.7*	*81.6*
Agricultural goods	18,067	18,930	*8.0*	*4.8*	*6.7*	*6.4*
Mining goods	20,681	27,321	*26.7*	*32.1*	*7.7*	*9.2*
Others	7,550	8,276	*51.7*	*9.6*	*2.9*	*2.8*
Total	**268,216**	**296,910**	***21.2***	***10.7***	***100.0***	***100.0***

Source: Department of Statistics, Malaysia.

CHART 2.10

Share of E&E and Non-E&E to Total Manufacturing Exports
(% annual share)

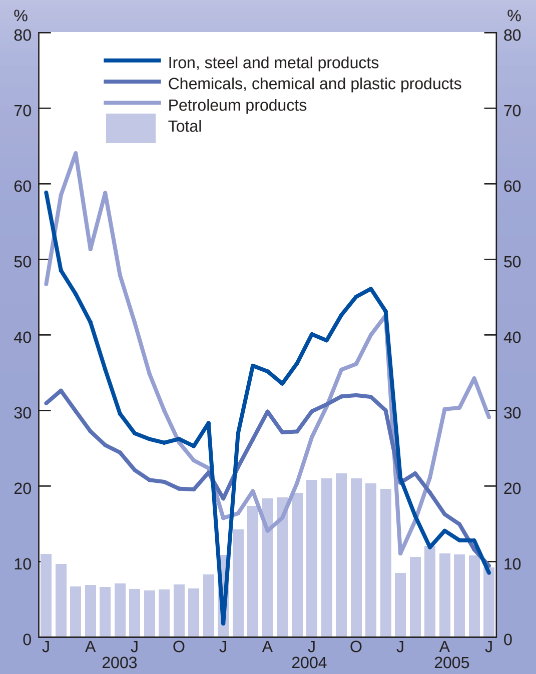


[1] January-July

Source: Department of Statistics, Malaysia.

CHART 2.11

Performance of Selected Manufacturing Exports
(% annual change)



Source: Department of Statistics, Malaysia.

with double-digit growth and resulting in the share of non-E&E to total manufacturing exports increased to 35.1% (January-July 2004: 34.6%).

Exports of **E&E** is expected to improve in 2005 as worldwide sales of semiconductors staged a turnaround and recorded a 5.8% increase during the first seven months of the year. In line with the book-to-bill ratio of the North American semiconductor industry, which trended upwards in anticipation of a pick-up in demand for ICT-related products, the Semiconductor Industry Association of the US forecasted a sales growth of 6% for the global semiconductor industry (2004: 28%). Hence, demand for Malaysia's E&E exports is also anticipated to improve for the rest of the year. The key drivers of E&E growth will be personal computers and optoelectronic products (high-end mobile phones and cameras, LCD and plasma digital televisions).

Exports of **non-E&E** products increased moderately by 11% during the first seven months of 2005 (January-July 2004: 27.8%), with positive growth in all major products except non-metallic minerals and textiles, apparel and footwear. Higher growth was recorded for petroleum and to a lesser extent, transport equipment. Exports of petroleum products also expanded higher by 29.1% in the first seven months of 2005 (January-July 2004: 26.5%). Higher oil prices as well as increased external demand for refined petroleum products and liquefied natural gas contributed to the industry's strong export growth during the period. This trend is expected to continue until the end of 2005, given the increasing demand from East Asia.

Meanwhile, exports of transport equipment maintained its strong pace, growing by 20.3% during the first seven months of 2005 (January-July 2004: 43.5%), arising from increasing

TABLE 2.14

Exports of Manufactured Goods
January-July

	RM million		Change (%)		Share (%)	
	2004	2005	2004	2005	2004	2005
Electronics, electrical and machinery appliances	**145,279**	**157,359**	***17.4***	***8.3***	***65.4***	***64.9***
Semiconductors	51,750	51,412	*7.1*	*-0.7*	*23.3*	*21.2*
Electronic equipment and parts	55,482	64,428	*21.4*	*16.2*	*25.0*	*26.6*
Machinery and electrical products	38,047	41,519	*28.0*	*9.1*	*17.1*	*17.1*
Non-E&E	**76,639**	**85,062**	***27.8***	***11.0***	***34.6***	***35.1***
Chemicals, chemical and plastic products	17,122	18,740	*29.9*	*9.5*	*7.7*	*7.8*
Iron, steel and metal products	9,033	9,802	*40.1*	*8.5*	*4.1*	*4.1*
Petroleum products	8,086	10,439	*26.5*	*29.1*	*3.7*	*4.3*
Wood-based products	6,922	7,514	*25.1*	*8.6*	*3.1*	*3.1*
Textiles, apparel and footwear	5,988	5,876	*20.1*	*-1.9*	*2.7*	*2.4*
Food, beverages and tobacco	5,175	5,628	*19.7*	*8.8*	*2.4*	*2.3*
Rubber products	3,559	3,919	*20.7*	*10.1*	*1.6*	*1.6*
Transport equipment	2,683	3,226	*43.5*	*20.3*	*1.2*	*1.3*
Non-metallic mineral products	1,796	1,690	*11.2*	*-6.0*	*0.8*	*0.7*
Other manufactured goods	16,275	18,228	*28.4*	*12.0*	*7.3*	*7.5*
Total	**221,918**	**242,421**	***20.8***	***9.2***	***100.0***	***100.0***

Source: Department of Statistics, Malaysia.

overseas demand for automotive parts and components, such as oil filters, wipers, absorbers and suspension systems. Export markets for Malaysia's automotive parts are the US, Taiwan, Thailand, Singapore and Indonesia.

Chemicals, chemical and plastic products, Malaysia's second largest manufacturing export earner, constituting 7.8% of total manufacturing exports, increased by 9.5% (January-July 2004: 29.9%). This was mainly due to the increase in exports of plastic products by 24.2% (January-July 2004: 35.6%).

The resource-based products, including rubber and wood-based, benefitted from higher external demand and rising prices, with both products recording strong growth of 10.1% and 8.6%, respectively. Wood-based products are expected to expand further following higher demand for new designs of do-it-yourself (DIY) wooden furniture. Meanwhile iron, steel and metal products also registered strong growth of 8.5%, due to higher export prices.

Export of Primary Commodities

Export of primary commodities expanded arising from firm prices and favourable external demand...

Export earnings from primary commodities, comprising agriculture produce and mineral products, are estimated to increase by 11.6% to RM80,575 million in 2005 (2004: 20.2%; RM72,200 million). Growth is expected to emanate from higher export receipts of palm oil, crude oil as well as liquefied natural gas (LNG) on account of firm prices and strong external demand. Export earnings from **agricultural** commodities for the

TABLE 2.15

Primary Commodity Exports
2005-2006

	2005[1]	2006[2]	Change (%) 2005[1]	Change (%) 2006[2]
Palm oil[3]				
Volume ('000 tonnes)	13,700	14,640	*17.7*	*6.9*
Unit value (RM/tonne)	1,500	1,551	*-12.9*	*3.4*
Value (RM million)	20,550	22,707	*2.5*	*10.5*
Palm kernel oil				
Volume ('000 tonnes)	900	1,000	*7.0*	*11.1*
Unit value (RM/tonne)	2,220	2,380	*8.4*	*7.2*
Value (RM million)	1,998	2,380	*16.0*	*19.1*
Saw logs				
Volume ('000 cubic metres)	4,810	4,830	*-7.6*	*0.4*
Unit value (RM/cubic metres)	472	458	*18.7*	*-3.0*
Value (RM million)	2,270	2,212	*9.7*	*-2.6*
Sawn timber				
Volume ('000 cubic metres)	2,890	2,700	*-8.7*	*-6.6*
Unit value (RM/cubic metres)	1,025	1,120	*1.0*	*9.3*
Value (RM million)	2,962	3,024	*-7.8*	*2.1*
Rubber				
Volume ('000 tonnes)	1,000	1,010	*-9.6*	*1.0*
Unit value (RM/tonne)	500	511	*6.4*	*2.2*
Value (RM million)	5,000	5,161	*-3.8*	*3.2*
Pepper				
Volume ('000 tonnes)	19	21	*0.0*	*10.5*
Unit value (RM/tonne)	6,316	5,714	*9.1*	*-9.5*
Value (RM million)	120	120	*9.1*	*0.0*
Cocoa				
Volume ('000 tonnes)	10	11	*6.6*	*10.0*
Unit value (RM/tonne)	6,200	6,364	*11.2*	*2.6*
Value (RM million)	62	70	*18.5*	*12.9*
Crude petroleum				
Volume ('000 tonnes)	18,174	19,964	*-2.7*	*9.8*
Unit value (RM/tonne)	1,551	1,696	*33.2*	*9.3*
Value (RM million)	28,188	33,859	*29.5*	*20.1*
Liquefied natural gas				
Volume ('000 tonnes)	20,936	21,340	*1.0*	*1.9*
Unit value (RM/tonne)	892	972	*8.3*	*9.0*
Value (RM million)	18,675	20,742	*9.3*	*11.1*
Tin				
Volume ('000 tonnes)	25	26.3	*-16.7*	*5.2*
Unit value (RM/tonne)	30	29	*-4.9*	*-3.3*
Value (RM million)	750	763	*-20.7*	*1.7*
Total value (RM million)	**80,575**	**91,038**	***11.6***	***13.0***

[1] Estimate.

[2] Forecast.

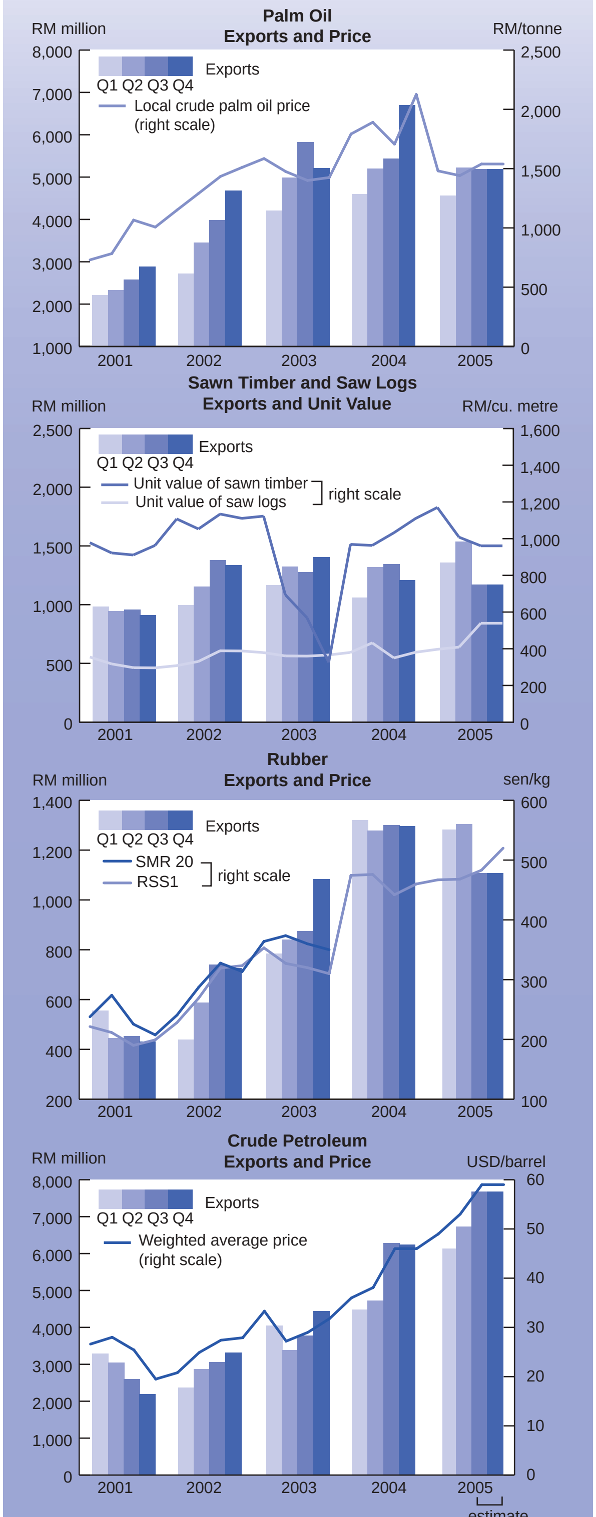
[3] Includes crude palm oil, processed palm oil and stearin.

first seven months of 2005 increased by 4.8% to RM18,930 million (January-July 2004: 8%; RM18,067 million) and expected to grow by 1.7% to RM32,962 million in 2005 due to firmer prices in the second half of the year. Similarly, export receipts from the mining sector increased by 32.1% in the first seven months of 2005 on account of stronger demand and higher prices for crude oil and natural gas. For the year, export earnings from mining is expected to increase strongly by 19.7% to RM47,613 million from RM39,787 million in 2004. Consequently, the share of total exports of primary commodities to gross exports is projected to increase to 15.1% in 2005 (2004: 15%).

Export volume of **palm oil** increased by 25.5% during the first seven months of 2005 (January-July 2004: -12.5%) although the export value remains the same on account of lower CPO prices. Nonetheless, palm oil remains the largest contributor to total agriculture export earnings, with a share of 59%. The monthly export volume reached an all time high of 1.33 million tonnes in May 2005. The surge in export volume during the first seven months of 2005 was on account of higher demand from China (16.2%) and the 25-nation euro area (33.6%). As palm oil is trans-fatty-acid free, exports to the US soared by 48.2%, on account of higher demand for palm oil in the US following the announcement on compulsory labelling for trans-fatty-acids products, which will take effect on January 2006. Exports to the euro area are also expected to pick up strongly due to increasing demand of palm oil for biodiesel following higher crude oil prices. Export receipts are estimated to increase further by 2.5% for the year due to higher demand and a sustained average export price of RM1,500 per tonne. Major importers of palm oil include China (20.2%), the Netherlands, (9.2%), Pakistan (6.7%), India (6%), and Egypt (3.8%). Meanwhile, export proceeds from **palm kernel oil** increased by 29% to RM1,156 million during the first seven months of 2005. Total export earnings of palm kernel oil in 2005 is poised to grow by 16% to RM1,998 million (2004: 17.9%; RM1,723 million). Efforts taken to further expand exports include promoting the use of palm oil for biofuel as well as increasing awareness of its techno-economic advantages

CHART 2.12

Primary Commodity Exports



Q - Quarterly

in addition to its nutritional value, especially in non-traditional markets through trade promotions, seminars and exhibitions.

The export quantity of **rubber** increased by 1.6% to 644,439 tonnes in the first seven months of 2005 (January-July 2004: 17.2%; 634,424 tonnes). For the year, total rubber exports, the bulk of which is SMR, is expected to contract by 9.6% to one million tonnes, constrained largely by lower production following unfavourable weather conditions and reduced planted areas. Export price of rubber is projected to increase by 2.2% and remain high at RM4.80 per kg (2004: 24.1%: RM4.70 per kg), due to a combination of factors including tight supply and rising demand. Total demand for natural rubber is expected to increase as manufacturers substitute synthetic rubber with natural rubber to lessen impact of soaring crude oil prices.

Export volume of **crude petroleum** contracted by 3.6% to 10.29 million tonnes in the first seven months (January-July 2004: 7.1%; 10.67 million tonnes). However, export revenue recorded an increase of 38.7% to RM15,182 million (January-July 2004: 26.4%; RM10,949 million), with export price averaging USD51 per barrel (RM1,474 per tonne) in the first seven months of 2005. Major importers of Malaysian crude petroleum are Australia (20.4%) India (18.7%), Thailand (14.6%), South Korea (11%) and Indonesia (10.5%).

Export earnings of **LNG** during the first seven months of 2005 continued to expand by 24.8% (January-July 2004: 23.3%), driven by both higher volume and unit value (export price) of 9.9% and 13.5%, respectively. The increase was partly due to rising oil prices making LNG a more competitive energy alternative, especially for power generation and industrial use. Major importers were Japan and South Korea, with imports increasing by 35.4% and 14.1%, respectively. Malaysia is presently, the second largest LNG exporter in the world, after Indonesia, with a total export of 20.8 million tonnes, accounting for 15.7% of global exports.

TABLE 2.16

Gross Imports by End Use
January-July

	RM million		Change (%)		Share (%)	
	2004	2005	2004	2005	2004	2005
Capital goods	**30,129**	**33,186**	***30.9***	***10.1***	***13.5***	***13.7***
Capital goods (except transport equipment)	27,501	30,015	*24.7*	*9.1*	*91.3*	*90.4*
Transport equipment (industrial)	2,628	3,171	*170.7*	*20.7*	*8.7*	*9.6*
Intermediate goods	**161,584**	**174,436**	***25.2***	***8.0***	***72.3***	***71.8***
Food and beverages, primary and processed mainly for industry	5,479	4,873	*66.0*	*-11.1*	*3.4*	*2.8*
Industrial supplies, primary and processed	51,067	56,471	*39.3*	*10.6*	*31.6*	*32.4*
Fuel and lubricants primary, processed, others	9,146	14,711	*15.0*	*60.8*	*5.7*	*8.4*
Parts and accessories of transport equipment	4,736	6,979	*30.0*	*47.4*	*2.9*	*4.0*
Parts and accessories of capital goods (except thermionic valves and tubes)	32,095	32,397	*26.8*	*0.9*	*19.9*	*18.6*
Thermionic valves and tubes	59,060	59,005	*13.2*	*-0.1*	*36.6*	*33.8*
Consumption goods	**12,838**	**13,736**	***22.6***	***7.0***	***5.7***	***5.7***
Food and beverages, primary and processed, mainly for household consumption	4,942	5,273	*29.7*	*6.7*	*38.5*	*38.4*
Transport equipment (non-industrial)	198	162	*-1.3*	*-18.3*	*1.5*	*1.2*
Other consumer goods	7,697	8,301	*19.1*	*7.8*	*60.0*	*60.4*
Durables	1,722	1,927	*17.0*	*11.9*	*22.4*	*23.2*
Semi-durables	2,559	2,555	*19.8*	*-0.2*	*33.3*	*30.8*
Non-durables	3,416	3,819	*19.7*	*11.8*	*44.4*	*46.0*
Others (including dual use goods)	**9,375**	**10,763**	***23.2***	***14.8***	***4.2***	***4.4***
Imports for re-exports	**9,609**	**10,958**	***115.0***	***14.0***	***4.3***	***4.5***
Total	**223,534**	**243,079**	***28.0***	***8.7***	***100.0***	***100.0***

Source: Department of Statistics, Malaysia.

Import Performance

Higher exports and robust domestic demand drive imports…

Gross imports of goods including cost, insurance and freight (c.i.f.) increased by 8.7% to RM243,079 million in the first seven months of 2005 (January-July 2004: 28%; RM223,534 million), as shown in *Table 2.16*. The increase was mainly attributed to higher demand for intermediate goods, particularly in the manufacturing sector to support rising external demand and, to a lesser extent higher imports of capital goods for capacity expansion. Likewise, imports of consumption goods also trended upwards in line with increasing household income and preference for high quality imported products. Consistent with the growth recorded in the first seven months of this year, gross imports in 2005 are expected to expand by 8.9% to RM435,653 million (2004: 26.4%; RM400,077 million). Imports of intermediate goods are envisaged to register an 8.9% growth (2004: 22%), while imports of capital goods are expected to expand further by 7.5% (2004: 36.1%). Sustained growth in private consumption is expected to drive imports of consumption goods by 6.9% in 2005 (2004: 24.1%).

Higher production in the electronics industry, which continued to enjoy strong demand and sustained activities in other manufacturing industries, drove imports of **intermediate goods** up by 8% in the first seven months of 2005 (January-July 2004: 25.2%). In tandem with increase in prices of petroleum related products, imports of fuel and lubricants as well as industrial supplies increased by 60.8% and 10.6% during the period (January-July 2004: 15%; 39.3%), respectively. Imports of parts and accessories of capital goods grew marginally by 0.9% (January-July 2004: 26.8%). However, imports of primary and processed materials by the food and beverages industry declined by 11.1% (January-July 2004: 66%). On the other hand, imports of parts and accessories of transport equipment recorded a strong growth of 47.4% (January-July 2004: 30%), driven by increase in domestic sales of motor vehicles.

Imports of **capital goods** expanded by 10.1% during the same period (January-July 2004: 30.9%). On a disaggregated basis, all sub-categories of capital goods recorded increases with imports of transport equipment for industrial purposes rising by 20.7% (January-July 2004: 170.7%). Imports of capital goods (except transport equipment) grew by 9.1% (January-July 2004: 24.7%), partly attributed to higher demand for automatic data processing machines (29.5%), parts and accessories of office machines (5.2%) and telecommunication equipment (1.9%), following strong private investment activities, particularly in the manufacturing and services sectors. Imports of capital goods, as a whole, constituted 13.7% of total imports in the first seven months of 2005 (January-July 2004: 13.5%).

In consonance with high private consumption, imports of **consumption goods** continued to rise by 7% during the first seven months of 2005 (January-July 2004: 22.6%) and sustained its share of 5.7% of total imports (January-July 2004: 5.7%). Notable increases were registered for imports of consumer durables and non-durables which expanded by 11.9% and 11.8%, respectively during the period (January-July 2004: 17%; 19.7%). Likewise, imports of food and beverages increased at a moderate rate of 6.7% (January-July 2004: 29.7%). On the other hand, imports of non-industrial transport equipment declined further by 18.3% (January-July 2004: -1.3%), while imports of semi-durables declined marginally by 0.2% (January-July 2004: 19.8%).

Other imports (including dual use goods), increased by 14.8% (January-July 2004: 23.2%) mainly attributed to higher demand for processed fuel and lubricants, motor spirits as well as transport equipment and passenger motorcars. Imports of transport equipment and passenger motorcars registered an increase of 15.1% in the first seven months of 2005 (January-July 2004: 22.3%). **Imports for re-exports,** mainly E&E, telecommunication equipment and iron and steel products which accounted for 4.5% of total imports, expanded by 14% (January-July 2004: 4.3%; 115%).

Trade Performance

Favourable export performance results in substantial trade surplus...

Malaysia's external trade continued to expand by 9.8% to reach RM539,988 million during the first seven months of 2005 (January-July 2004: 24.2%; RM491,749 million). Major trading partners are the US, Singapore, Japan and China. These countries collectively accounted for 50.7% of total trade in the first seven months of 2005 (January-July 2004: 51.1%). Trade with ASEAN (not including Singapore) continues to gain prominence with both exports and imports maintaining double-digit growth of 16.6% and 13%, respectively (January-July 2004: 37.9%; 32.1%), as shown in *Table 2.17.* With exports accounting for 55% of the total trade and imports 45%, Malaysia's trade surplus with the rest of

TABLE 2.17

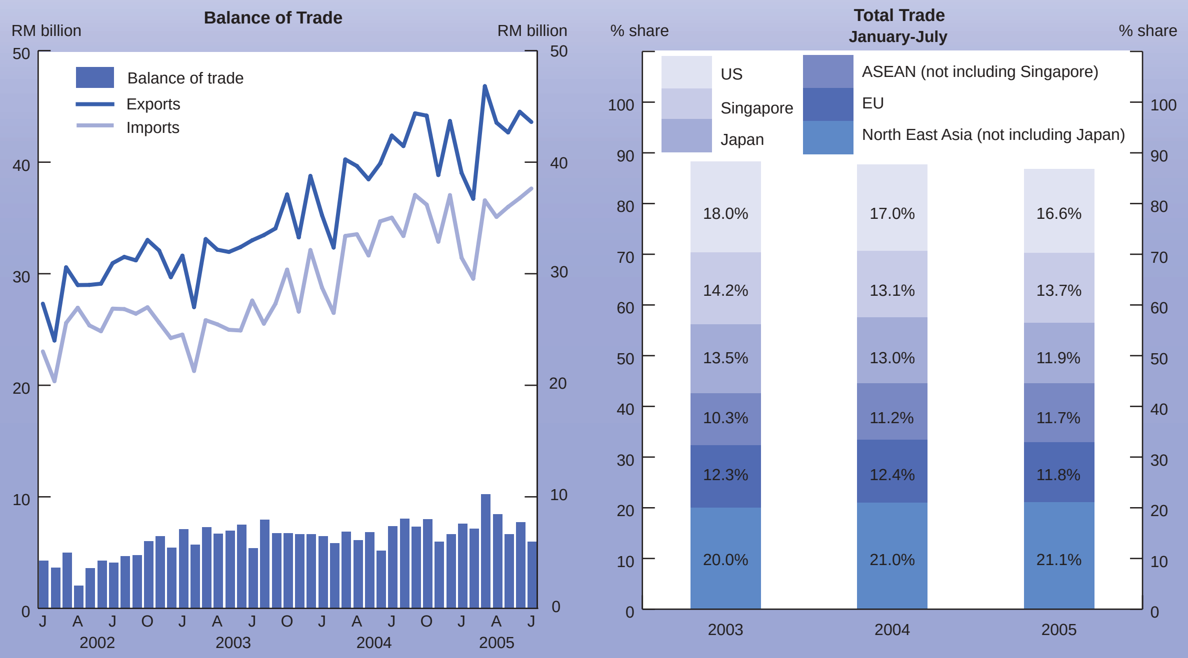
Direction of External Trade
January-July

	Exports				Imports				Trade Balance	
	Change (%)		Share (%)		Change (%)		Share (%)		RM million	
	2004	2005	2004	2005	2004	2005	2004	2005	2004	2005
United States	***14.7***	***15.8***	***18.8***	***19.6***	***20.4***	***-4.9***	***14.9***	***13.0***	**17,097**	**26,674**
Singapore	***12.9***	***15.5***	***14.9***	***15.6***	***17.5***	***14.3***	***10.9***	***11.5***	**15,531**	**18,233**
Japan	***13.6***	***6.9***	***10.1***	***9.8***	***24.6***	***-4.7***	***16.5***	***14.5***	**-9,799**	**-6,191**
North East Asia (not including Japan)	***24.9***	***4.6***	***19.7***	***18.6***	***36.7***	***16.6***	***22.6***	***24.2***	**2,332**	**-3,610**
China	*31.2*	*4.7*	*6.6*	*6.3*	*50.5*	*25.4*	*9.6*	*11.1*	-3,611	-8,220
Hong Kong SAR	*16.2*	*6.8*	*6.1*	*5.9*	*23.8*	*-3.5*	*2.7*	*2.4*	10,540	11,871
South Korea	*47.2*	*12.0*	*3.6*	*3.6*	*21.8*	*8.1*	*5.1*	*5.1*	-1,874	-1,655
Taiwan	*11.0*	*-7.9*	*3.3*	*2.7*	*37.0*	*19.0*	*5.2*	*5.7*	-2,749	-5,646
European Union	***20.5***	***1.8***	***12.6***	***11.6***	***30.1***	***7.7***	***12.1***	***12.0***	**6,820**	**5,348**
Germany	*17.1*	*3.0*	*2.3*	*2.1*	*37.2*	*0.5*	*4.7*	*4.3*	-4,377	-4,241
Netherlands	*17.4*	*10.5*	*3.2*	*3.2*	*52.6*	*-7.0*	*0.9*	*0.7*	6,596	7,631
United Kingdom	*21.4*	*-9.9*	*2.3*	*1.8*	*16.4*	*-0.4*	*1.8*	*1.6*	2,118	1,540
France	*7.4*	*-8.5*	*1.5*	*1.2*	*11.6*	*11.6*	*1.4*	*1.4*	934	236
Italy	*23.9*	*-14.7*	*0.7*	*0.5*	*53.7*	*52.6*	*0.9*	*1.2*	-113	-1,384
Ireland	*1.0*	*53.5*	*0.3*	*0.4*	*-14.7*	*39.9*	*0.5*	*0.7*	-519	-633
ASEAN (not including Singapore)	***37.9***	***16.6***	***10.1***	***10.6***	***32.1***	***13.0***	***12.4***	***12.9***	**-723**	**160**
Thailand	*35.6*	*29.5*	*4.8*	*5.6*	*58.8*	*8.4*	*5.4*	*5.3*	793	3,560
Indonesia	*40.2*	*15.4*	*2.3*	*2.4*	*51.4*	*3.3*	*4.0*	*3.8*	-2,738	-2,085
Philippines	*42.6*	*-2.4*	*1.6*	*1.4*	*-15.2*	*26.9*	*2.5*	*2.9*	-1,299	-2,920
Vietnam	*53.2*	*-5.1*	*0.9*	*0.8*	*35.8*	*71.2*	*0.4*	*0.7*	1,523	687
Brunei	*15.7*	*-11.0*	*0.3*	*0.2*	*75.9*	*52.6*	*0.0*	*0.0*	728	636
South Asia	***19.3***	***19.5***	***3.5***	***3.8***	***116.8***	***-23.0***	***1.4***	***1.0***	**6,251**	**8,849**
India	*21.3*	*22.5*	*2.4*	*2.7*	*130.0*	*-24.5*	*1.4*	*0.9*	3,397	5,596
West Asia	***39.4***	***3.5***	***2.7***	***2.5***	***7.6***	***61.2***	***2.1***	***3.1***	**2,588**	**9**
United Arab Emirates	*46.1*	*20.9*	*1.2*	*1.3*	*46.6*	*54.9*	*0.4*	*0.6*	2,302	2,453
Saudi Arabia	*17.1*	*3.5*	*0.4*	*0.4*	*34.1*	*67.3*	*0.8*	*1.2*	-722	-1,865
Iran	*2.5*	*-3.8*	*0.3*	*0.2*	*157.8*	*88.3*	*0.2*	*0.3*	278	-135
Oman	*41.9*	*21.5*	*0.1*	*0.1*	*-33.7*	*59.0*	*0.3*	*0.4*	-513	-873
Australia	***51.4***	***21.9***	***3.1***	***3.4***	***35.2***	***30.7***	***1.7***	***2.0***	**4,472**	**5,126**
New Zealand	***15.4***	***-3.2***	***0.4***	***0.3***	***11.7***	***5.0***	***0.3***	***0.3***	**187**	**118**
Africa	***13.1***	***20.9***	***1.3***	***1.4***	***79.3***	***12.0***	***0.6***	***0.6***	**2,062**	**2,610**
Rest of the world	***36.7***	***7.6***	***2.9***	***2.9***	***27.1***	***19.5***	***4.5***	***4.9***	**-2,136**	**-3,494**
Total	***21.2***	***10.7***	***100.0***	***100.0***	***28.0***	***8.7***	***100.0***	***100.0***	**44,682**	**53,831**
RM billion			**268.2**	**296.9**			**223.5**	**243.1**		

Source: Department of Statistics, Malaysia.

CHART 2.13

Trade Performance



Source: Department of Statistics, Malaysia.

the world remained large at RM53,831 million (January-July 2004: RM44,682 million). Major countries contributing to the surplus were the US, Singapore, Hong Kong SAR, Netherlands and India. On the other hand, trade with China, Japan, Taiwan, Germany and Philippines recorded deficits.

The **US** remains Malaysia's largest trading partner, accounting for 16.6% of Malaysia's total trade (January-July 2004: 17%). Malaysia recorded a higher trade surplus of RM26,674 million in the first seven months of 2005 (January-July 2004: RM17,097 million). This was largely due to the strong growth in exports of E&E, which grew by 16.8% and accounted for 77.7% of total exports to the US. Meanwhile, a 4.9% decline in imports from the US during the period did not affect its ranking as the second most important source of imports for Malaysia.

Singapore maintained its position as the second most important trading partner of Malaysia with 13.7% of total trade. E&E products were the largest export earner with receipts totalling RM24,740 million or 53.6% of total exports to Singapore. On the import side, Singapore is the third largest source for Malaysia. The bulk of imports was E&E (RM10,604 million) and refined petroleum products (RM7,889 million), which together represents 66.1% of total imports from the Republic.

Japan is Malaysia's third largest trading partner with a share of 11.9%. Export growth of 6.9% in the first seven months of 2005 was underpinned by a 35.4% increase in exports of LNG. Although exports of E&E declined by 5.2% in the same period, it remained the largest export earner and contributed 33.2% of total export earnings. Import bills from Japan declined by 4.7%, mainly on account of lower imports of E&E. Nevertheless, Japan remains the main source of imports for Malaysia. With growth of exports outpacing imports, trade balance which has always favoured Japan, narrowed to RM6,191 million (January-July 2004: -RM9,799 million).

The People's Republic of China emerged as Malaysia's fourth largest trading partner in 2001, and has since maintained its position. Exports of E&E accounted for 41.3% of total exports, followed by palm oil (13.2%), and chemicals and chemical products (12%) in the first seven months of 2005. Meanwhile, China remained Malaysia's fourth major source of imports which mainly comprised parts and accessories for office machines, transistors and valves, automatic data processing equipment as well as iron and steel products.

Trade with other economies in **North East Asia,** namely Taiwan, South Korea and Hong Kong SAR constituted 12.7% of Malaysia's total trade (January-July 2004: 13%). Among these nations, South Korea and Hong Kong SAR are the major trading partners, each accounting for 4.3% of Malaysia's total trade, followed by Taiwan (4.1%).

The **European Union** (EU), another important trading partner, accounted for 11.8% (RM63,462 million) of Malaysia's total trade (January-July 2004: 12.4%). Within the EU, Germany is Malaysia's leading trading partner, accounting for 26.3% of Malaysia's total trade with the Community, followed by the Netherlands (17.7%) and the UK (14.7%). Trade surplus with the EU was lower in the first seven months of 2005 at RM5,348 million, partly due to a decline in exports of manufactured goods to the UK and France.

Malaysia's trade with **ASEAN** (not including Singapore) expanded significantly by 14.7% and accounted for 11.7% of total trade (January-July 2004: 34.9%; 11.2%). Exports to ASEAN grew strongly on the back of higher demand for Malaysian made E&E and resource-based products. Likewise, strong imports in the first seven months of 2005 were driven by higher demand for electronic products, chemicals, manufactures of metal and iron and steel products. During the period, Malaysia registered a trade surplus of RM160 million with ASEAN, largely on account of trade surplus with Thailand (RM3,560 million) and Vietnam (RM687 million).

Balance of Payments

Current account surplus for eight consecutive years…

Malaysia's balance of payments remains favourable in 2005 with the current account recording a significant surplus for the eighth

TABLE 2.18

Current Account of the Balance of Payments
2005-2006
(RM million)

	2005[1]			2006[2]		
	Receipts	**Payments**	**Net**	**Receipts**	**Payments**	**Net**
Goods	**533,380**	**409,312**	**124,068**	**592,741**	**460,213**	**132,528**
Services	**71,245**	**81,182**	**-9,937**	**79,937**	**89,765**	**-9,828**
Transportation	14,493	32,781	-18,288	16,026	36,948	-20,922
Travel	34,096	13,615	20,481	37,375	14,700	22,675
Other services	22,140	34,066	-11,926	25,926	37,165	-11,239
Government transactions	516	720	-204	610	952	-342
Income	**19,804**	**43,637**	**-23,833**	**21,978**	**46,600**	**-24,622**
Compensation of employees	3,639	4,825	-1,186	3,716	4,986	-1,270
Investment income	16,165	38,812	-22,647	18,262	41,614	-23,352
Current transfers	**1,688**	**18,985**	**-17,297**	**1,767**	**19,543**	**-17,776**
Current account	**626,117**	**553,116**	**73,001**	**696,423**	**616,121**	**80,302**

[1] Estimate.
[2] Forecast.

consecutive year. The surplus emanates from a higher trade balance as well as lower deficit in the income account. The financial account is also expected to remain favourable following sustained inflows in FDI. Consequently, Malaysia's net international reserves in 2005 is expected to remain strong and further strengthen the nation's economic fundamentals.

Exports are expected to outpace imports in terms of value and growth, resulting in a substantial surplus of RM124,068 million in the **goods account** (2004: RM104,474 million), as shown in *Table 2.18*. Moderate expansion in global trade is expected to result in a slower growth rate of 10.8% for exports of goods (f.o.b.) to RM533,380 million (2004: 20.9%; RM481,240 million). Similarly, imports of goods (f.o.b.) are also envisaged to increase at a slower pace of 8.6% to RM409,312 million (2004: 25.5%; RM376,766 million).

The **services account** will remain in deficit in 2005, despite strong inflows in the travel component. With higher tourist arrivals projected for the year, net inflow in the travel account is envisaged to increase slightly by 5.6% to RM20,481 million (2004: 68.3%; RM19,398 million). Growth in travel receipts, comprising mainly business and leisure travel as well as receipts from education and health, is expected to expand by 9.5% to RM34,096 million (2004: 39%; RM31,152 million). Gross outflows in the travel account are expected to pick up strongly by 15.8% to RM13,615 million (2004: 8%; RM11,754 million) with more Malaysians travelling abroad, supported by rising disposable income and low fares of budget airlines. Meanwhile, other components of the services account, namely transportation, other services and government transactions will continue to register a net outflow and contribute to the overall deficit in the services account.

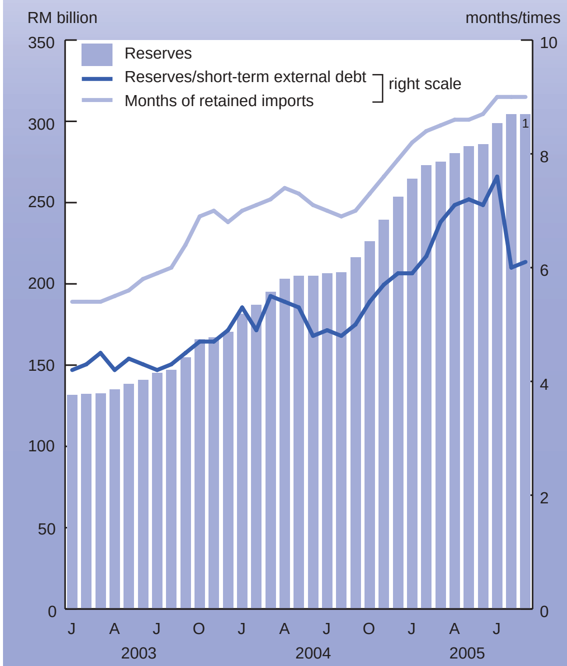
The **income account** is expected to record a lower deficit of RM23,833 million (2004: -RM24,549 million) in 2005. Gross receipts, consisting mainly of investment returns from abroad, are expected to continue rising at double digit growth of 23.6% to RM19,804 million (2004: 22%; RM16,023 million). Gross payments mainly comprising profits and dividends of MNCs, are envisaged to expand by 7.6% to RM43,637 million (2004: 13.7%; RM40,572 million).

Net outflow associated with **current transfers** is expected to increase by 18.2% in 2005 to RM17,297 million (2004: 57.3%, -RM14,633 million). Transfer receipts, largely on account of remittances by Malaysians working abroad are estimated to decline by 0.7% to RM1,688 million in 2005 (2004: -11.9%; RM1,700 million). On the other hand, transfer payments are likely to increase by 16.2% to RM18,985 million (2004: 45.5%; RM16,333 million), mainly due to higher remittances by foreign workers.

In the **financial account,** FDI is expected to remain favourable, channelled mainly into the manufacturing sector, particularly in the expansion of higher value-added E&E activities, the services sector as well as the oil and gas sector. Overseas investment is likely to remain significant as large and established Malaysian companies continue to invest abroad, particularly in oil and gas, services and construction sectors. Other investment component is expected to record a net outflow, reflecting mainly net repayments of external loans by the official sector and extension of trade credits by Malaysian exporters.

CHART 2.14

International Reserves



[1] As at 15 September 2005.

Source: Bank Negara Malaysia.

As at 15 September 2005, Malaysia's international reserves remained strong at RM304,362 million (USD80,161 million) indicating continued strong economic fundamentals. The increase in reserves was on the back of sustained repatriation of export earnings and steady inflows of foreign capital. At 6.1 times of Malaysia's short-term external debt, the reserves are adequate to finance nine months of retained imports. The high level of reserves has further strengthened the country's resilience against external shocks.

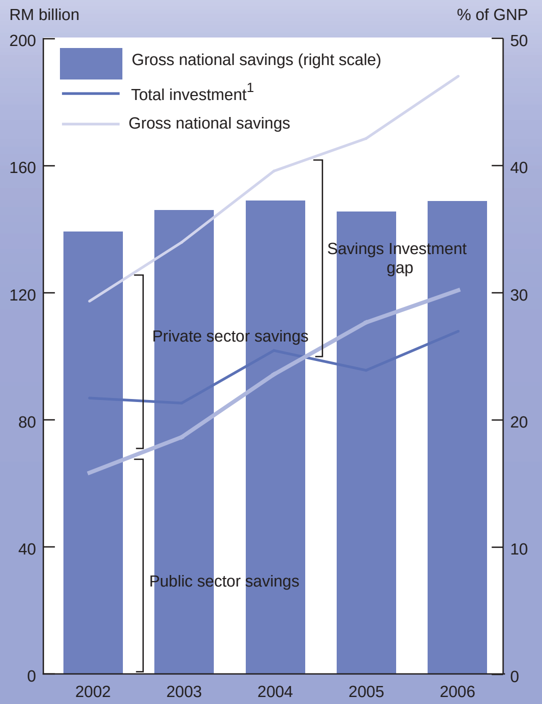
National Resource Position

Stronger resource position, with large current account surplus...

National income continues to record strong growth of 9.1% in 2005 (2004: 14.1%) an account of declining net outflows of factor payments abroad. **Gross national savings (GNS)** remains high at 36.4% of GNP, but expanding at a moderate rate of 6.5% to RM168,592 million (2004: 16.5%; RM158,338 million). GNS, the bulk of which is public sector savings, continues to surpass total investment. Consequently, **savings-investment gap** is expected to show a substantial surplus, totalling RM73,001 million or 15.7% of GNP (2004: RM56,511 million; 13.3%), providing ample liquidity in the financial system that can be mobilised to finance domestic economic activities without exerting pressure on interest rates.

CHART 2.15

Savings Investment Gap



[1] Including change in stocks.

Prices

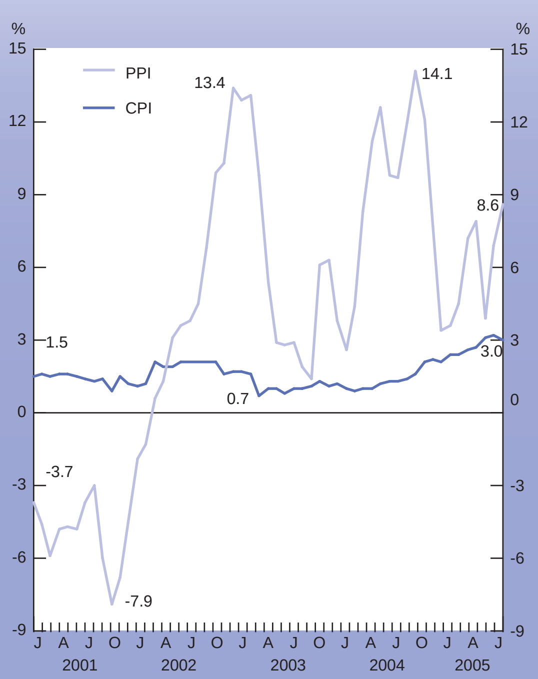
Cost-push inflation emerging due mainly to high oil prices...

Inflation as measured by annual percentage change in the **Consumer Price Index** (CPI) edged up following higher costs of transportation on the back of rising world oil prices. For the first eight months of 2005, the CPI registered an increase of 2.8% (January-August 2004: 1.2%), while world oil prices rose markedly by 40.1% during the same period (January-August 2004: 29.1%). In order to reduce its subsidy burden, the Government increased the pump prices of retail petroleum and diesel products thrice with the latest increase on 31 July by 6.6% for premium petrol, 18.5% for diesel, and 3.6% for LPG. Even though these increases resulted in higher costs of fuel, retail prices of petroleum products in Malaysia are still among the lowest in the region. Food and transport prices were up, following revisions in bus and taxi fares and the ceiling price of chicken during the course of the year, as well as the imposition of higher excise duties for liquor and tobacco in Budget 2005. Prices of other components of the CPI, however, remained stable with marginal increases.

Food, with the highest weightage of 33.8%, registered an increase of 3.5% (January-August 2004:1.9%), contributing the bulk at 43.1% of the total increase in CPI. Higher prices of meat (9.9%), fruits and vegetables (4.3%), fish (4%) and milk and eggs (3.8%) have resulted in the increase in the price of **food at home** by 3.8% (January-August 2004: 1.9%). The increase in prices of these sub-groups was due to lower supply of fresh food and higher poultry prices resulting from higher production costs. The price of **food away from home** also increased by

CHART 2.16

Trend of CPI and PPI
(% annual change)



Source: Department of Statistics, Malaysia.

3.1% (January-August 2004: 1.6%) and contributed 24.7% to the increase in the food group index.

Transport and communication, the second largest contributor added 24.7% to CPI during the first eight months of 2005. This component recorded an increase of 3.6% (January-August 2004: 0.4%) following the upward revision in fares for buses and taxis, effective 1 May 2005. Meanwhile, **beverages and tobacco** added 15.2% to the CPI. This component recorded the highest growth rate of 13.6% (January-August 2004: 5%). Increases in other components of the CPI were relatively small, with the exception of **clothing and footwear,** which registered a decline of 1% (January-August 2004: -2%), partly due to stiff competition and low cost imports, especially from China.

The higher cost of food especially meat, fish and vegetables resulted in a higher CPI at 3% for Peninsular Malaysia. In contrast, price increases in both Sabah and Sarawak were lower at 2.4% and 2.2%, respectively, on account of lower food prices.

TABLE 2.19

Consumer Price Index (CPI)
January-August
(2000=100)

		Change (%)		Contribution to CPI growth (%)	
	Weight	2004	2005	2004	2005
Total	**100.0**	***1.2***	***2.8***	***100.0***	***100.0***
Food	33.8	*1.9*	*3.5*	*57.2*	*43.1*
Beverages and tobacco	3.1	*5.0*	*13.6*	*14.2*	*15.2*
Clothing and footwear	3.4	*-2.0*	*-1.0*	*-6.3*	*-1.2*
Gross rent, fuel and power	22.4	*0.9*	*1.2*	*17.9*	*9.3*
Furniture, furnishing and household equipment and operation	5.3	*0.1*	*1.5*	*0.5*	*2.9*
Medical care and health expenses	1.8	*1.3*	*1.6*	*2.2*	*1.0*
Transport and communication	18.8	*0.4*	*3.6*	*6.1*	*24.7*
Recreation, entertainment, education and cultural services	5.9	*-0.1*	*0.4*	*-0.5*	*0.8*
Miscellaneous goods and services	5.5	*1.7*	*2.1*	*8.8*	*4.2*

Source: Department of Statistics, Malaysia.

On 7 September 2005, the Government announced four measures to ease the burden of rising domestic prices and to cushion the effects of soaring world oil prices. A moratorium was placed on further price increases for petroleum products until the end of the year. Secondly, increase in toll rates are deferred until 1 January 2007. Thirdly, road tax for commercial and private vehicles were reduced depending on its engine capacity and type of usage. The fourth and last measure is specifically to provide aid to senior citizens, the underprivilleged and orphans through welfare programmes.

The **Producer Price Index** (PPI), which has been increasing since April 2004 continued to increase, but at a slower rate of 6% during the first seven months of 2005 (January-July 2004: 8.3%). Most of the PPI components registered moderate increases except for **mineral fuels, lubricants and related materials,** which recorded a double-digit increase of 27.7% compared to 14.5% in the same period last year, reflecting the impact of high crude oil prices. **Animal and vegetable oils and fats** registered a negative 18% (January-July 2004: 20.5%) after increasing for three consecutive years due to lower CPO prices. The price of CPO registered a decline of 12.2% to an average of RM1,403 per tonne in the first seven months of 2005 compared to RM1,599 per tonne in the same period last year. The PPI for **imports** was higher at 1.8% (January-July 2004: 1.6%) on account of higher crude oil price while, PPI for **local production** moderated to 6.9% during the period (January-July 2004: 9.7%).

Labour Market

Labour market conditions remain healthy…

The healthy labour market conditions are expected to continue through 2005, particularly in the second half of the year in line with favourable

TABLE 2.20

Producer Price Index (PPI)
January-July
(1989=100)

	Weight	Change (%) 2004	Change (%) 2005	Contribution to PPI growth (%) 2004	Contribution to PPI growth (%) 2005
Domestic economy	**100.0**	***8.3***	***6.1***	***100.0***	***100.0***
Food and live animals chiefly for food	14.9	*4.2*	*3.8*	*8.7*	*11.1*
Beverages and tobacco	2.1	*1.4*	*2.0*	*0.4*	*0.8*
Crude materials, inedible excepts fuels	18.0	*8.8*	*0.4*	*22.2*	*1.3*
Mineral fuels, lubricants and related materials	18.8	*14.5*	*27.7*	*38.3*	*101.7*
Animal and vegetable oils and fats	8.5	*20.5*	*-18.0*	*24.5*	*-28.0*
Chemical and related products	4.4	*3.3*	*3.3*	*2.1*	*2.9*
Manufactured goods, classified chiefly by material	10.8	*2.0*	*3.2*	*3.1*	*6.8*
Machinery and transport equipment	18.3	*0.1*	*0.6*	*0.2*	*2.3*
Commodities and transactions not classified elsewhere in the SITC[1]	3.6	*0.9*	*1.5*	*0.5*	*1.1*
Miscellaneous manufactures articles	0.6	*0.2*	*0.0*	*0.0*	*0.0*
Local production	**79.3**	***9.7***	***6.9***	***95.9***	***93.6***
Import	**20.7**	***1.6***	***1.8***	***4.1***	***6.4***

[1] Standard International Trade Classification.

Source: Department of Statistics, Malaysia.

TABLE 2.21

Labour Market Indicators

	('000)		Change (%)	
	2004	2005[1]	2004	2005[1]
Labour force	10,587.7	10,926.6	*3.4*	*3.2*
Employment	10,222.0	10,547.5	*3.6*	*3.2*
Unemployment	365.7	379.1	*3.5*[2]	*3.5*[2]

[1] Estimate.
[2] Percentage of labour force.

Source: Economic Planning Unit.

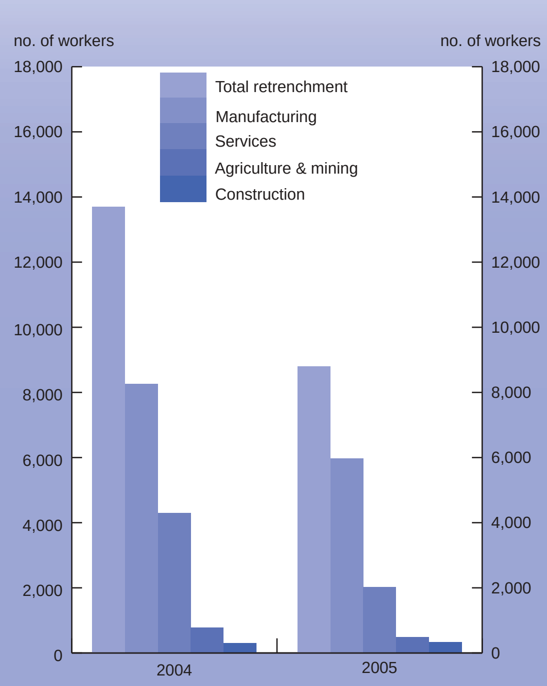
external environment, strong domestic economic activities and improved business sentiment. Employment opportunities are generally encouraging with both total employment and labour force growing at a rate of 3.2%. As a result, unemployment as a percentage of labour force is envisaged to remain low at 3.5% for the year, the 14th consecutive year of full employment for Malaysia.

The overall labour force participation rate is expected to remain relatively high at 66% in 2005 (2004: 65.5%). Participation from the younger work force, particularly those in the 15-24 years age group, has shown an increasing trend. In terms of gender, both male and female participation rate increased marginally to 85.2% (2004: 85.1%) and at 45.8% (2004: 45.7%), respectively. Although female participation rate is lower, Malaysia has one of the highest female participation rates among developing countries. Labour mobility, cultural and social preferences are some of the factors inhibiting higher female participation. The proportion of labour force with tertiary education is projected to increase from 18.1% in 2004 to 19% in 2005, reflecting higher enrolment of students in institutions of higher learning, as well as expanding tertiary education and training facilities.

Generally, all sectors of the economy are expected to generate additional employment. **Total employment** is expected to increase by 3.2% or 325,500 new jobs in 2005 (2004: 3.6%; 355,300). In terms of employment by sector, the

CHART 2.17

Retrenchment in Selected Sectors January-July



Source: Ministry of Human Resources.

manufacturing and services sectors continue to provide the highest number of jobs. Out of the 10.6 million employed, the services sector provided 50.8% of total employment, followed by the manufacturing sector (28.3%) and agriculture (13.1%), as shown in *Table 2.22.*

During the first seven month of 2005, the number of **job seekers** registered with the Manpower Department increased markedly by 256% to 98,009 (January-July 2004: -26%; 27,514), partly due to the extension of job seekers registration validity period from 3 months to 6 months starting May 2005. Of this total, over half of the jobseekers (57%) were in the 20-24 years age group, while 25% were in the age group of 25-29 years. The majority of registered job seekers were degree and diploma holders at 27% and 21%, respectively while 29% had *Sijil Pelajaran Malaysia* (SPM) qualifications. In terms of gender, female job seekers, at 59%, surpassed their male counterparts. In view of the high numbers of degree and diploma holders registered with the

TABLE 2.22

Employment by Sector

	('000)		Share (%)		Change (%)	
	2004	2005[1]	2004	2005[1]	2004	2005[1]
Agriculture, forestry, livestocks and fishing	**1,396.8**	**1,385.6**	***13.7***	***13.1***	***-0.3***	***-0.8***
Mining and quarrying	**42.2**	**42.6**	***0.4***	***0.4***	***1.2***	***0.9***
Manufacturing	**2,869.8**	**2,990.4**	***28.1***	***28.3***	***6.4***	***4.2***
Construction	**770.6**	**775.3**	***7.5***	***7.4***	***-1.2***	***0.6***
Services	**5,142.6**	**5,353.6**	***50.3***	***50.8***	***4.2***	***4.1***
Electricity, gas and water	89.7	92.5	*0.9*	*0.9*	*5.0*	*3.1*
Wholesale and retail trade, hotels and restaurants	1,771.7	1,864.2	*17.3*	*17.7*	*5.2*	*5.2*
Finance, insurance, real estates and business services	642.4	671.7	*6.3*	*6.4*	*5.0*	*4.6*
Transport, storage and communication	557.9	593.5	*5.5*	*5.6*	*5.5*	*6.4*
Government services	1,041.8	1,052.8	*10.2*	*10.0*	*1.5*	*1.1*
Other services	1,039.1	1,078.9	*10.2*	*10.2*	*3.1*	*3.8*
Total	**10,222.0**	**10,547.5**	***100.0***	***100.0***	***3.6***	***3.2***
Primary	1,439.0	1,428.2	*20.4*	*19.1*	*-0.3*	*-0.8*
Secondary	3,640.4	3,765.7	*56.3*	*56.9*	*4.7*	*3.4*
Tertiary	5,142.6	5,353.6	*18.1*	*19.0*	*4.0*	*4.1*

[1] Estimate.

Source: Economic Planning Unit.

department, the Government reintroduced the Graduate Training Scheme in September this year.

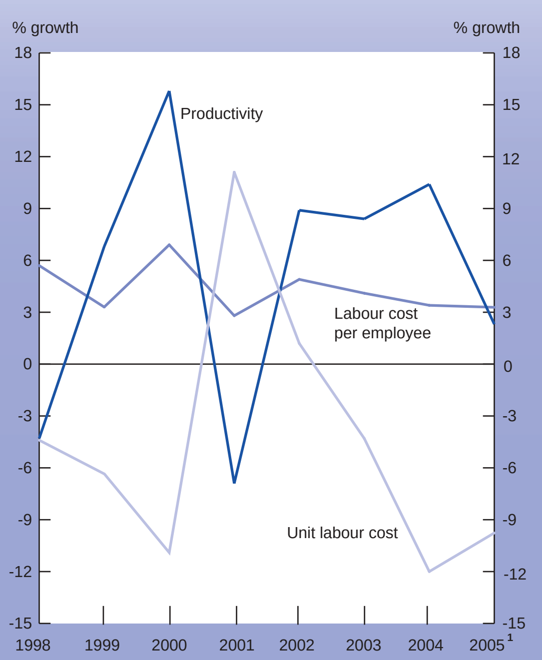
Better job prospects are reflected in the rising number of job **vacancies** as reported by the Electronic Labour Exchange (ELX) of the Ministry of Human Resources, which showed an increase of more than 87% to 52,882 during the first seven month of 2005 (January-July 2004: -51%; 28,327). The services sector registered the highest number of vacancies with 38.7%, followed by manufacturing (27%), construction (8%) and agriculture (3%). As a result of the favourable economic performance, the number of **retrenched workers** declined significantly by 36% to 8,802 (January-July 2004: -4.2%; 13,693). The retrenched were mainly general workers in the manufacturing sector, accounting for about half the total retrenchments. Major reasons cited for retrenchments include declining demand for products and increase in production costs in certain industries.

For the first seven months of 2005, **productivity** of the manufacturing sector recorded a slower growth of 2.6% (January-July 2004: 1.2%). The moderation in growth was due to a slowdown in output, particularly in the E&E industries. During the same period, 9,604 new workers were employed by the sector (January-July 2004: 26,814). Wage pressures in the short term are expected to remain subdued, given the negative growth in average wage by 7.5% and a decline in real unit labour cost by 9.9% (January-July 2004: -10%).

Malaysia has a good track record of maintaining industrial harmony and cordial relationship between employers and the trade unions.

CHART 2.18

Manufacturing Sector: Growth in Productivity and Unit Labour Cost



[1] January-July

Source: Ministry of Finance.

TABLE 2.23

Employment by Major Occupational Group

	('000)		Share (%)	
	2004	2005[1]	2004	2005[1]
Legislators, senior officials and managers	838.2	864.9	*8.2*	*8.2*
Professionals	572.4	611.8	*5.6*	*5.8*
Technicians and associate professionals	1,247.1	1,297.3	*12.2*	*12.3*
Clerical workers	950.6	959.9	*9.3*	*9.1*
Service workers and shop and market sales workers	1,472.0	1,539.9	*14.4*	*14.6*
Skilled agricultural and fishery workers	1,247.1	1,244.6	*12.2*	*11.8*
Craft and related trade workers	1,298.2	1,360.6	*12.7*	*12.9*
Plant and machine operators and assemblers	1,472.0	1,518.8	*14.4*	*14.4*
Elementary occupations	1,124.4	1,149.7	*11.0*	*10.9*
Total	**10,222.0**	**10,547.5**	***100.0***	***100.0***

[1] Estimate.

Source: Economic Planning Unit.

Industrial disputes are harmoniously resolved through consultations and negotiations. Not a single strike was reported during the first seven months of 2005 compared with three cases for the whole of last year.

Productivity for the economy as whole in 2005 is envisaged to improve with favourable outlook in the external sector, which is anticipated to have positive impact on demand and drive output in all sectors, although the manufacturing sector is expected to experience relatively lower productivity. In agriculture, where R&D activities are intense, productivity growth is projected to be higher, especially in downstream agro-based industries. These developments are expected to contribute to an overall 2.8% productivity growth for 2005 (2004: 2.9%).

Malaysia continues to remain attractive to **foreign workers**, especially from Indonesia because of geographical proximity and similarity in culture and language. As at end-May 2005, the total number of registered foreign workers increased by 10.2% to reach 1.62 million (2004: 1.47 million). Of the total, 31.1% were employed in the manufacturing sector, followed by plantations (26.9%), services (26.5%), and construction (15.5%). The majority of foreign workers are from Indonesia, comprising 69.4%, followed by Nepal (10.2%), India (6.2%), and Vietnam (4.6%).

Effective July 2005, the Government increased the levy on foreign workers in the services and plantation sectors by 50%. This is to discourage the employment of unskilled foreign workers and to promote greater mechanisation and automation. Meanwhile, levy in other sectors remain unchanged. As at 2 August 2005, a total of 33,062 (2004: 40,093) expatriates were employed in the country as professionals, specialists and skilled workers mainly in the services (14,532) and manufacturing (13,754) sectors. The majority of them are from India (22%; 7,293), Japan (12.9%; 4,250) and China (10.9%; 3,601).

Outlook for 2006

Private sector activities and favourable external sector to propel growth...

The year 2006 will face greater challenges arising from high oil prices, tightening monetary policies especially in the US, widening global imbalances as well as continued geo-political tensions and security concerns. Nevertheless, given the resilience of major economies, the **global economy** is expected to expand at 4.3%, supported by China and the US. Economic growth in China is forecast to continue, but at a slightly lower rate of 8.2%, providing the impetus for growth in Asia in general and the ASEAN region in particular, while the US is projected to register a growth of 3.3%. In Japan, growth is projected to be firm at 2% as deflation eases and domestic demand sustains.

Economic activity in the euro area is also expected to improve, although uneven across the region, at 1.8%. The expected improvement is on account of favourable financing conditions, rise in business confidence amid signs of recovery in the services and manufacturing sectors and a strong external sector. As for the UK, growth prospects are envisaged to improve by 2.2% with the services sector spurring growth, supported by a more accommodative monetary policy.

Malaysian Economy

Broad based growth...

The **Malaysian economy** is expected to maintain its growth momentum in 2006 in line with sustained private sector activities, favourable external environment and Government's continuing efforts to further diversify the economy through new sources of growth. Growth is expected to be broad-based with expansion in all sectors, driven by private investment spending and strong activities in the services sector. Accordingly, real GDP growth is forecast to expand by 5.5% in 2006 and per capita income envisaged to rise further by 7.1% to RM18,995 (2005: 6.8%; RM17,741). In terms of purchasing power parity, per capita income will increase by 6.9% to USD11,030 (2005: 7.2%; USD10,323).

Domestic Demand

Private sector to expand further, driven by investment activities...

Aggregate domestic expenditure (excluding change in stocks) in real terms is envisaged to expand by 5.7% in 2006 (2005: 6.9%), driven by higher investment spending, particularly by the private sector. Of significance, private investment activities are expected to gather strength with consumer and business confidence as well as investment climate continuing to improve in the coming year. **Private sector expenditure** is envisaged to contribute significantly to domestic economic activities, increasing by 8.1% (2005: 7.5%). **Public sector expenditure** is also projected to increase by 0.8% (2005: 5.9%) and is expected to sustain domestic demand activities. Hence, public sector contribution to GDP growth is envisaged at 0.2 percentage points (2005: 1.8 percentage points), with private sector contribution remaining high at 5 percentage points (2005: 4.5 percentage points).

Private investment expenditure is projected to increase by 13% and account for 12.4% of GDP (2005: 7.6%; 11.5% of GDP) in line with expected higher export earnings, sustained inflows of FDI and direct domestic investment, particularly in new and emerging industries. Of importance, strong investment activities in the manufacturing and manufacturing-related services sectors are expected to benefit from Government initiatives in diversifying and intensifying the manufacturing sector towards producing higher value-added products. The forthcoming Third Industrial Master Plan (IMP3), 2006-2010, will outline the direction for the further development of SMEs to play a more active role in all sectors of the economy.

Investment activities in the agriculture sector are expected to gain momentum in tandem with Government policy to revitalise the sector through modernisation and large scale mechanisation.

The robust services sector will provide opportunities for investment in the light of advanced and rapid changes in technologies, particularly in telecommunications, banking and finance, as well as trade and logistics. Spurred by persistently high oil prices since the second half of 2004 and expectation of increasing global demand amidst tight supply, investment activities in the oil and gas industry are expected to accelerate in 2006. Recent discoveries of oil and gas fields will further expedite investments in the sector.

After expanding at a strong pace of 9% per annum in 2004 and 2005, **private consumption** is expected to moderate slightly to 7% in 2006 (2005: 7.5%), amidst steady growth in disposable income. **Public consumption** is budgetted to increase further by 1.3% (2005: 8.9%), on account of rising expenditure on emolument as well as supplies and services. With a higher allocation for development expenditure totalling RM22,001 million in 2006 (2005: RM19,613 million), **public investment** is estimated to expand by 0.3% (2005: 3%).

Sectoral Outlook

All sectors to record positive growth...

On the supply side, all sectors are projected to record positive growth with manufacturing and services sectors continuing to be the key drivers of growth. The manufacturing sector is expected to grow at a higher rate following the strengthening of global electronics demand and the continuing strong pace of domestic economic activities. The services sector will continue to strengthen with all sub-sectors recording positive growth. Growth in the services sector is expected to be supported by continued expansion in new services activities such as ICT-related and business outsourcing services, as well as private healthcare and education services. The agriculture sector is projected to continue on its expansion path, on account of continuing efforts to diversify and modernise the sector, particularly the production of food commodities to help reduce high imports. The construction sector is envisaged to stage a turnaround, boosted by the commencement of new infrastructure projects under the 9MP.

Following recovery in global electronics demand in the second half of 2005, growth of the **manufacturing sector** is anticipated to grow by 4.9% (2005: 4.8%). The landscape of the manufacturing sector is expected to change in tandem with new developments and the shift towards technology-driven manufacturing processes with more R&D activities. New developments include advanced technologies such as nanotechnology, biotechnology and advanced manufacturing practices, which encompass high knowledge-content processing technologies. These developments are expected to contribute positively to growth of the manufacturing sector.

Prospect for the **services sector** remains buoyant with growth estimated stronger at 6.1% (2005: 5.8%). Growth is expected to emanate from sustained activities across major sub-sectors. The transport, storage and communication sub-sector is anticipated to continue to record strong growth, benefitting from capacity expansion of airlines and investment by telecommunication companies. Expansion in domestic tourism and trade-related activities supported by rising income will contribute to higher growth in the wholesale and retail trade, hotels and restaurants sub-sector. Increased bank lending and other financial activities will boost growth of the finance and insurance sub-sector.

The **agriculture sector** is expected to grow at a higher rate of 5% in 2006 (2005: 4.8%), contributed by higher production of palm oil and rubber as well as increase in food production. The Government continues to revitalise the food sub-sector through implementation of various strategies and measures to boost production capacity and efficiency. In addition, continued investments in niche areas of the agriculture sector, in particular aquaculture, seaweed, herbs, floriculture and ornamental fish are expected to drive growth of the sector.

Output of **crude oil and gas** is envisaged to rise in 2006 on account of continuing strong demand and higher prices as well as capacity expansion in new oil and gas fields. Crude oil and natural gas output are projected to increase by 4.2% and 10%, respectively (2005: -1.5%; 5%). As a result, growth of the **mining sector** in terms of value added is anticipated to accelerate by 4.7% in 2006 (2005: 1.5%).

The **construction sector** is set to recover next year. Growth is expected to increase by 3% (2005: -1.1%), spurred by a turnaround in the civil-engineering sub-sector, following implementation of new infrastructure projects under the 9MP. Likewise, activities in the residential and non-residential sub-sectors are also envisaged to remain active, supported by sustained demand for houses and purpose-built offices.

External Trade

Continuing substantial surplus in the current account of the balance of payments...

Malaysia's gross export earnings in 2006 will remain healthy with sustained growth in world economy, expanding trade as well as Government's efforts to encourage exporters to venture into non-traditional markets and introduction of new products. Export earnings will expand by 11.1% (2005: 10.8%) mainly on account of higher exports of manufactured goods. Likewise, payments for imports are expected to grow by 12.6% on the back of higher imports of intermediate, capital and consumption goods. Malaysia is envisaged to register a substantial trade surplus of RM101,766 million in 2006 (2005: RM97,163 million) despite imports growing faster than exports.

The goods account of the **balance of payments** is projected to record a net inflow of RM132,528 million in 2006 (2005: RM124,068 million). Although, Malaysia continues to record net outflow in the services account, it is expected to be smaller due to higher tourist receipts as well as earnings from ICT and financial services. The income account, however continues to record a higher net outflow of RM24,622 million (2005: -RM23,833 million), mainly due to higher earnings of MNCs operating in Malaysia. In addition, outflows in the transfer account, comprising mainly remittances by foreign workers are envisaged to increase to RM19,543 million (2005: -RM18,985 million). The surplus in the goods account will be sufficiently large to offset the outflows for the ninth consecutive year. Thus, the current account of the balance of payments is envisaged to record another round of substantial surplus amounting to RM80,302 million (2005: RM73,001 million) or 15.9% of GNP (2005: 15.7%).

National Resource Position

Strong resource balance, despite higher investment activities...

National income in current prices is projected to register a strong growth of 9.2% in 2006 (2005: 9.1%), in line with expansion in domestic economic activities and higher export earnings. With total consumption spending envisaged to increase at 8.1% but lower than the growth rate of national income (9.2%), GNS is estimated to increase at the rate of 11.6% to reach RM188,209 million in 2006 (2005: 6.5%; RM168,592 million). Consequently, the share of GNS as a percentage of GNP remains high at 37.2% (2005: 36.4%). Total investment expenditure (including change in stocks) is projected to increase strongly by 12.9% to RM107,907 million and account for 21.3% of GNP (2005: -6.1%; RM95,591 million; 20.6%). Accordingly, the surplus in **resource balance** is expected to increase and remain substantial at RM80,302 million or 15.9% of GNP (2005: RM73,001 million; 15.7%).