

Financial institutions remain profitable

THE Malaysian financial sector continues to showcase a high degree of resilience and remains well positioned to weather the effects of heightened external vulnerabilities on the local economy.

Loan delinquencies continued to improve to record lows and financial institutions remained profitable.

Capitalisation and solvency positions were sustained at strong levels, with sufficiently high level of financial buffers, strengthened institutional structure and supporting infrastructure, and enhanced governance and risk management practices.

The key risks to financial system stability domestically emanated from the bout of rising inflationary pressures in the first half of 2008, which shifted into concerns over significantly lower growth due to the

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rapid deterioration in global economic and financial conditions towards the later half of the year.

Meanwhile, the level of capitalisation of the banking system remained high while the solvency position of the insurance and takaful industry was sustained during the year.

The risk weighted capital ratio and core capital ratio of the banking system were at 12.7% and 10.6% respectively.

The excess capital position was at RM38.8bil against total losses recorded by the banking system of RM5.7bil in 1998 when gross domestic product contracted by 7.4%.

The banking sector remained largely supportive of the financing requirements of the economy amid the ample liquidity environment and sustained high capitalisation level.

Nevertheless, the increased uncertainties and less bullish economic outlook have resulted in both borrowers and financiers alike exercising greater caution.

The growth in total applications for new financing declined to 9.6% against 2007's 45.4%, due to lower applications from businesses, which could be scaling back, or delaying large-scale investment and expansion plans, in responding to the weaker outlook.

Total approvals granted for new financing moderated slightly to RM291.8bil during the year although disbursements continued to grow at 15.5% to RM639.9bil. As at end 2008, outstanding loans and financing expanded by 12.8% to RM726.5bil, or 98.1% of gross domestic product.

Ringgit liquidity meanwhile

remained ample despite the outflow of portfolio funds due mainly to the de-leveraging process by international financial institutions.

While ringgit liquidity was not a concern, the domestic financial system was not insulated from the global tightening in US dollar liquidity.

This prompted Malaysian banks to actively manage their foreign currency-dominated exposures to narrow the negative US dollar liquidity mismatch comprising mainly of direct lending and foreign currency swaps.

The domestic financial sector is bracing for greater challenges as moderation in economic growth begins to take shape and volatility in the domestic financial market persists given its strong linkages with the global markets.

Services sector performance at constant 2000 prices

	2007	2008p
	Annual change (%)	
Services	9.7	7.3
<i>Intermediate services</i>	11.7	6.0
Finance and insurance	11.1	7.7
Real estate and business services	18.2	1.5
Transport and storage	10.0	6.1
Communication	7.0	7.3
<i>Final services</i>	8.1	8.4
Wholesale and retail trade	12.5	9.8
Accommodation and restaurant	10.8	7.3
Utilities	3.9	2.1
Government services	4.5	11.9
Other services	5.0	4.9

p - preliminary
Source: Department of Statistics, Malaysia

Anaemic growth

Global economy not likely to expand in 2009

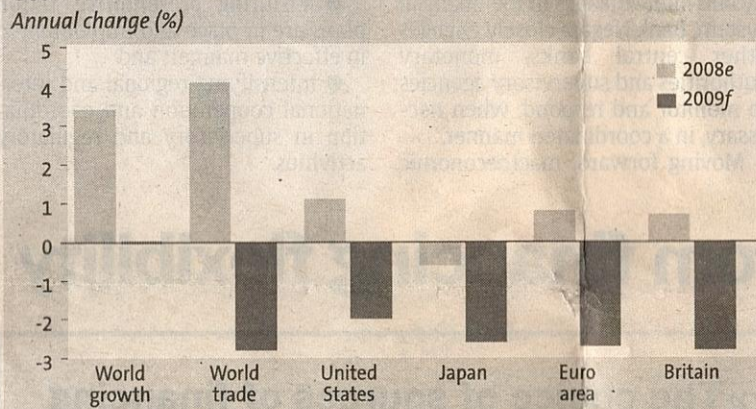
THE global economy is not expected to record any growth in 2009, with a large number of economies experiencing a synchronised recession, according to the Bank Negara 2008 annual report.

The global financial markets would remain under stress in 2009 in spite of the extensive measures, reflecting the ongoing need to repair and restructure the damaged balance sheets of financial institutions in several advanced economies.

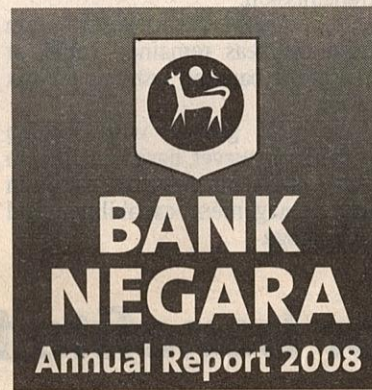
The expected loss of US-originated credit assets held by banks and other financial institutions could increase to US\$2.2 trillion.

Market conditions in the international financial system will likely remain challenging and are expected to stabilise when the announced pol-

World growth, world trade and growth in major advanced economies



e: estimates; f: forecast
Source: International Monetary Fund and National Authorities



regional economies are expected to face a sharp moderation in growth in 2009.

Global inflation is expected to decelerate further in 2009 due to sluggish real economic activity and

Malaysian economy expanded by 4.6% in 2008

AMIDST the international financial turmoil and sharp deterioration in global economic environment, the Malaysian economy registered a growth of 4.6% in 2008. Robust domestic demand, in particular sustained private consumption and strong public spending, supported growth during the year.

While external demand was strong in the first half of 2008, the sharp and rapid deterioration in the global economic conditions as well as major correction in commodity prices in the second half, led to a contraction in Malaysia's export performance in the latter part of the second half year.

Given the high degree of openness of the Malaysian economy, the contraction in exports adversely affected income and domestic demand.

Private investment activities and private consumption moderated significantly in the fourth quarter of

policy measures when the announced policy measures are effectively implemented to restore confidence in the financial sector.

Private consumption will also face pressures from job losses and declining asset prices.

The newly industrialised Asian economies (NIEs) as well as the Asean economies are expected to record anaemic to no growth, while China is expected to record sub-par growth due to the weaker exports and investment outlook.

Real economic activity in the US is expected to decline further. Private

consumption is expected to remain depressed due to the persistent weakness in the labour and housing markets.

The aggressive monetary and quantitative easing together with the US\$787bil fiscal stimulus package are, however, expected to provide support to the economy.

The recession in the euro area is expected to deepen due to a combination of housing slump in several economics as well as the impact of the financial turmoil.

The credit crunch in Europe is also

expected to intensify due to the exposure of western European banks to the central and eastern European economies.

In Britain, there are further signs of a deepening contraction of its economy, while Japan is expected to face further deterioration in its export sector and investment activities. Global trade is expected to contract further this year and will be accompanied by a decline in global foreign direct investments.

The NIEs are anticipated to remain in recession in 2009, while other

stagnant real economic activity and sharp declines in commodity prices.

Headline inflation in advanced economies is expected to fall to a record low of 0.3% in 2009. Inflation in emerging and developing economies is expected to moderate to 5.8% in 2009 from 9.2% in 2008.

While the risks to the growth outlook in the advanced economies would have significant implications on the Asian regional economies, the region as a whole entered the current downturn from a position of strength in terms of strong fundamentals and sound macroeconomic policies.

Favourable growth seen across all major sectors

THE Malaysian economy entered 2008 with favourable growth across all major sectors, amidst strong domestic demand, supportive external environment and rising prices of commodities.

Growth in the first half of 2008 was driven by the robust performances of the services sector, with further support coming from the manufacturing and agriculture sectors.

However, the sharp deterioration in global economic conditions in the second half of 2008 led to a pronounced deceleration in external demand.

This led to weakened performance of sectors most directly exposed to global demand, particularly the electronics and electrical industry.

In 2008, the services sector

expanded by 7.3% compared with 9.7% in 2007.

The sector contributed 3.9 percentage points to the overall gross domestic product (GDP) growth, whilst its share to GDP increased to 55% against 53.6% in 2007.

The wholesale and retail trade sub-sector expanded by 9.8% compared with 12.5% in 2007.

The sub-sector registered strong growth in the first half year, in line with robust domestic demand.

However, growth moderated in the second half of 2008, affected by high inflation and weak consumer sentiment.

The finance and insurance sub-sector recorded a growth of 7.7% against 11.1% in 2007 to account for 11% of GDP at end 2008.

In the communication sub-sector,

increased competition in the telecommunications market, and the roll-out of new broadband services, particularly WiMAX, provided impetus for strong demand in both the cellular and broadband segments.

As at the end 2008, the penetration rate of broadband increased to 21.1% of households against 14.4% at the end of 2007, while the penetration rate of the cellular segment rose to 96.8% of population, compared to 85.1% as at end 2007.

Meanwhile, the transport and storage sub-sector expanded at the moderate pace of 6.1% compared with 10% in 2007.

The manufacturing sector expanded, albeit at a much slower pace in 2008 at 1.3% compared to 3.1% in 2007.

Nevertheless, the manufacturing

sector contributed to the economy with a share of GDP of 29.2% compared with 30.1% in 2007.

The agriculture, forestry and fishing sector expanded at a faster pace of 3.8% in 2008, driven mainly by stronger palm oil production, which accounted for about 30% of value add in the agriculture sector.

The value-add of the mining sector declined marginally by 0.8% in 2008 due to lower output of natural gas, while crude oil production registered a small increase.

The construction sector recorded a positive growth rate for the second successive year, registering a growth of 2.1%.

The growth was supported by higher activities across the three sub-sectors; civil engineering, non-residential and residential.

private consumption moderated significantly in the fourth quarter of 2008. In the first half of 2008, the economy grew strongly by 7.1% supported by robust domestic and external demand.

Domestic demand was led by continued strong expansion in private consumption, supported by a steady increase in disposable income, positive labour market conditions, and favourable financing environment.

External demand was supported by very high commodity prices and strong export volume. Demand from the regional countries was also strong. When the global downturn intensified in the second half of 2008, with several major advanced economies slipping into recession and growth in a number of regional economies moderating rapidly, net external demand declined significantly.

Nevertheless, real gross domestic product growth remained positive in the second half of the year, expanding modestly by 2.4%, supported by strong public consumption and continued expansion in private consumption.

On the supply side, growth in the first half was driven by robust performance of the services sector due to strong domestic demand conditions, and the expansion in trade and tourism activities.

Further support came from the manufacturing sector due to robust external demand from the non-US markets and higher exports of resource-based products, which also benefited from rising commodity prices.