MALAYSIAN RATING CORPORATION BERHAD (364803 V)

MARC forecasts Malaysia's 2009 GDP growth at 3.5% : Resilient amid global financial dislocation

MARC views that the ongoing global turbulence roiling the financial markets will likely trigger a global recession in 2009 and accordingly forecasts Malaysia's GDP growth for next year at 3.5%.

The world's largest economy and Malaysia's single largest trading partner, the United States (US) is likely to experience its first recession since 2001 as the financial crisis continues unabated with adverse impact on bank lending, investment and private consumption. As a result, the US economic performance will cast a long shadow on the rest of the world. Other major economies, namely the Euro and Japan, are also not being spared from the current financial and economic malaise.

Being an open economy, Malaysia and other regional countries are not immune from any crisis, especially one that is unprecedented as the current turmoil. These economies are now bracing for a decline in global trade volume due to an expected drop in external demand. In addition to external trade performance, Malaysian economic growth in 2009 will also be impacted by a slowdown in private investment as risk aversion heightens among investors. As a consequent, business expansion plans are likely to be scaled down while portfolio investors may continue to stay on the sideline as evident by substantial net outflows in the second quarter 2008. Although Malaysia has, over the years, diversified its trade pattern with intra-trade with ASEAN countries becoming a significant feature of its economy, the expected moderations in the economies of G3 (US, Euro and Japan) could have knock-on effects on ASEAN economies as well.

However, the silver lining in the Malaysian economy is the steady domestic demand, primarily supported by private consumption, which, while expected to moderate to 4.4% in 2009 from an estimated 6.3% this year following the impact of higher consumer prices and waning consumer sentiment, is anticipated to be a bulwark against a weakening global economy. Domestic demand in 2009 is expected to be underpinned by an accommodative monetary stance and a relatively stable labour market.

In addition, Malaysia is in a more resilient position to cope with present economic challenges as reflected by huge surplus in the current account of balance of payment, a high level of external reserves and sound banking system that will help weather current economic challenges. As of September 30, 2008, the amount of external reserves stood at RM379.3 billion, sufficient to finance 9 months of retained imports and is 4.1 times the total short-term external debt. This is in stark contrast with the situation during the Asian Financial Crisis in 1997 when external reserves dropped to as low as 2.9 months of retained imports in October that year.

The country's financial institutions' ability to provide ample liquidity is also a critical factor to insulate the Malaysian economy from a credit crunch. A loan-deposit ratio in the banking system that continues to remain below 80% in the last 4 years also augurs well for its role to support lending activities. Additionally, there is no visible strain in the domestic financial market as is evident by the benign spread between interbank and Treasury Bills.

Further underscoring the strength of the country's financial institutions is the declining trend of net non-performing loans (NPL). The NPL ratio stood at 2.5% in August 2008, compared with 13.6% at the height of the Asian Financial Crisis. Another measure, loan loss coverage, has risen to nearly 85.1% in August 2008, thus providing ample buffer against possible financial losses.

From a macro policy point of view, the general stabilisation plan as announced by Finance Minister I on October 20, 2008, will, to some extent, cushion the economy from a significant slowdown in 2009. MARC opines that although the impact of the government's recent proposed measures to make investments more attractive for foreign investors will not be felt in the immediate-term, it is a move in the right direction. As for the monetary policy, MARC believes that the authorities will continue to retain sufficient flexibility to adapt to changing economic conditions should the global slowdown begin to show signs of severely impacting Malaysia's growth prospect in the near-term.

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