

Economic Research

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The State of Sarawak



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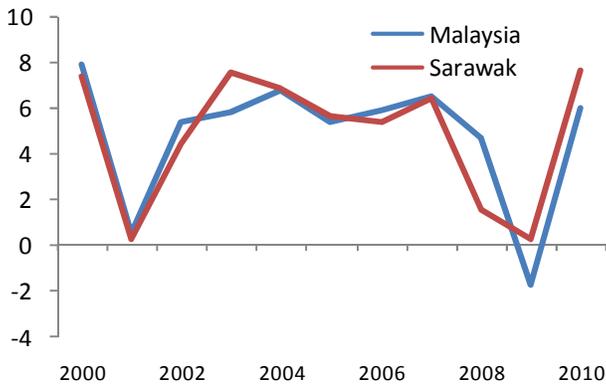
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Economic structure and performance

The Sarawak economy was not spared from the global malaise in 2009. Its GDP growth moderated sharply from 1.6% in 2008 to 0.3% in 2009, led by key sectors such as mining & quarrying and manufacturing which contracted by 5.0% (2008: -4.6%) and 2.5% (2008: -0.9%) respectively. Because of the structure of the economy whereby crude palm oil (CPO), crude petroleum and liquefied natural gas (LNG) are the state's main export products, Sarawak is quite susceptible to global shocks. Additionally, Sarawak is highly dependent on external trade, with total exports continuing to be in excess of 100% of its GDP, suggesting that the economy is highly vulnerable to global trade conditions.

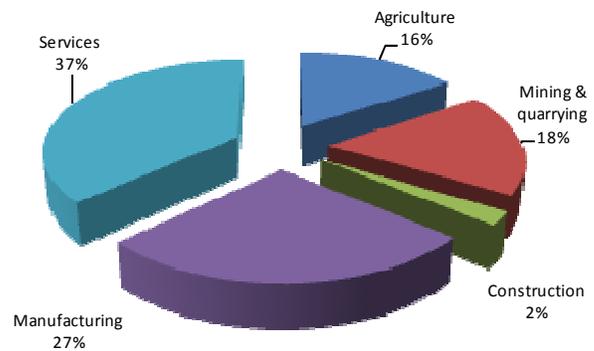
The federal government's policy response to support the economy during the recession in 2009 appears to be effective in reversing the cyclical downturn brought by the fall in global demand. The state GDP managed to register a positive growth in 2009 as opposed to the 1.7% contraction recorded on a national scale. The second stimulus package announced by the federal government in March 2009 which put greater emphasis on projects that will improve the state's basic amenities in rural areas as well as school facilities has been successful in preventing the economy from slipping into contractionary mode. Not surprisingly, the construction sector has been the immediate beneficiary of the stimulus package, growing by 22.1% in 2009 after contracting 7.4% in the earlier year. In 2010, the economy is expected to register a decent growth of 7.7%, underpinned by improvements in mining and manufacturing output.

Chart 1: GDP growth %



Source: Sarawak State Planning Unit, CEIC & MARC Economic Research

Chart 2: Economic structure



Source: Sarawak State Planning Unit & MARC Economic Research

Table 1: Sarawak GDP growth by sector

Growth	2007	2008	2009	2010E
Agriculture	1.7%	1.5%	3.6%	4.2%
Mining & quarrying	9.2%	-4.6%	-5.0%	3.1%
Construction	15.8%	-7.4%	22.1%	5.2%
Manufacturing	4.2%	-0.9%	-2.5%	7.2%
Services	8.4%	8.2%	7.6%	6.7%
GDP	6.5%	1.6%	0.3%	7.7%

Source: 10 MP

Natural resources, demographic profile and labour market

The Sarawak state is blessed with abundant natural resources such as minerals (petroleum, gas, coal, silica sand and kaolin clay), hydropower potential and land. In addition, the age profile of Sarawakians indicate that a majority of the population is young with 62% of the population between the age of 15 and 64 years. This suggests an adequate supply of labour in the state in light of increasing economic activities going forward. Generally, most of its population work in the agricultural sector where its share to total employed persons was 26.3% in 2008, followed by wholesale and community, social, personal and other services (20.4%) and retail trade, restaurants and hotels (20.0%).

Table 2: Sarawak Natural Resources

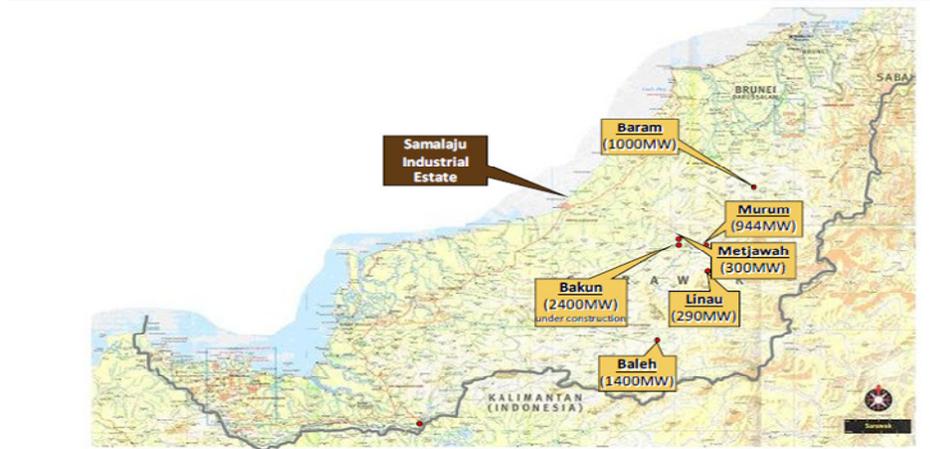
Coastline	1,051 km
Land with agriculture potential	2.2 million ha
Land under forest cover	8.2 million h.a
Area under peat soil	1.7 million ha
Marine fish production potential	300, 000 tonnes per year
Hydropower potential	20,000 MW
Surface water	306 billion cubic meter
Minerals	Approx reserves
-Petroleum	1,388 million barrels
-Gas	42.6 trillion S.C.F
-Coal	1,483 million tonnes
-Silica sand	73.8 million tonnes
-Kaolin clay	22.6 million tonnes

Source: Sarawak State Planning Unit

SCORE as growth catalyst

The Sarawak Corridor of Renewable Energy (SCORE), which is one of the five regional development corridors in Malaysia, is an important catalyst for future growth for the state. The main focus of SCORE is to leverage on Sarawak's energy resources, particularly hydropower (28,000 MW), coal (1.46 billion tonnes) and natural gas (40.9 trillion square cubic feet). These resources will, in turn, allow Sarawak to price its energy competitively and at the same time stimulate investment activities in power generation as well as energy-intensive industries that will enhance economic well-being in the central region. The 10 industries that will spearhead the SCORE are the aluminum, glass, steel, oil-based, palm oil, fishing & aquaculture, livestock, timber-based, marine engineering and tourism industries. Thus far, interest in the corridor has been quite forthcoming, evidenced by the cooperation agreement recently signed by China's state owned company State Grid Corporation of China (SGCC) and a Malaysian company, 1Malaysia Development Berhad (1MDB) in January this year. The agreement was sealed for the purpose of undertaking investment activities in an aluminum smelter plant and three hydropower dams for a total of USD11 billion.

Chart 3: Potential location of smelter and larger dams under development or planning in Sarawak



Source: OSK

State finances

Oil & gas and palm oil are the primary sectors that drive the state's government revenue. The latest audited account in 2008 indicated a bulk of the RM1.7 billion worth of dividends received by the state government was mainly from the oil & gas companies. These companies include Malaysia LNG Sdn Bhd (MLNG), MLNG 2 and MLNG 3 in which the government of Sarawak has minority stakes. Apart from that, royalty from forestry activities and land premiums were also major contributors to the state income. Following the sharp rise in commodity prices, state revenues increased by 59.3% to RM6.5 billion in 2008 while operating expenditures rose 36.0% to RM4.4 billion. Consequently, the state government managed to register a healthy surplus balance of RM2.0 billion, representing a 153% rise from the earlier year assessment.

Notwithstanding this, the state public debt in 2008 was substantially higher compared to the earlier year, rising by 15.2% to RM1.6 billion. The increase was mainly attributed to higher expenditure on infrastructure such as water supplies, industrials and sewerage. Nonetheless, such increases were not alarming considering that there were no overdue loan repayments by the state and the fact that Sarawak continued to enjoy a surplus balance in its fiscal position.

Table 3: State government revenue and expenditure

(RM' Million)	2004	2005	2006	2007	2008
Tax revenue	892	939	901	994	1,072
Non-tax revenue	1,894	2,179	2,961	2,951	5,246
Non-revenue receipts	24	23	22	16	22
Federal grants and reimbursements	122	88	90	95	121
Total revenue	2,933	3,229	3,974	4,055	6,461
Operating expenditure	2,499	2,483	2,752	3,248	4,418
Balance	434	746	1,221	807	2,043

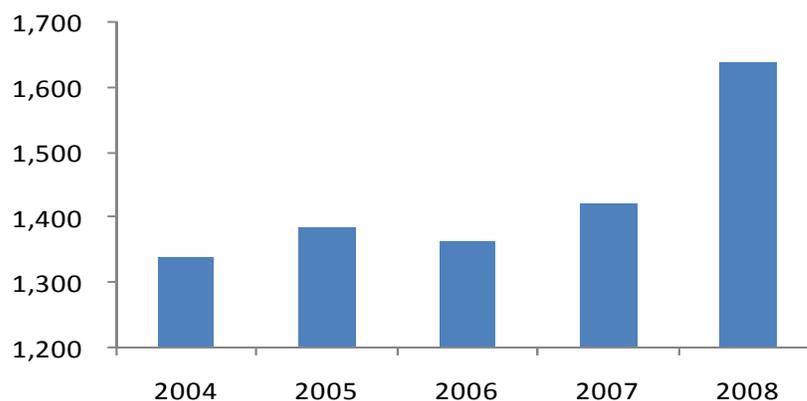
Source: Jabatan Audit Negara

Table 4: Main contributors of state government revenue

(RM'Million)	2004	2005	2006	2007	2008
Dividend	513	560	761	676	2,319
Compensation in lieu of oil rights	517	740	951	991	1,323
Compensation in lieu of gas rights	381	427	541	561	820
Forestry royalty	648	691	631	630	596
Land premiums	150	158	201	159	170
Total	2,210	2,576	3,086	3,018	5,227

Source: Jabatan Audit Negara

Chart 4: State public debt in RM'Million



Source: Jabatan Audit Negara

Key risk areas

Volatility in commodity prices

The economy is vulnerable to gyrations in commodity prices, reflecting its exposure to global trade. Any significant weaknesses in global trade conditions will adversely affect its economy. In addition, the state government's revenue relies heavily on commodities such as crude oil, LNG and CPO. Prices of these commodities are highly influenced by weather conditions and global demand. As such, Sarawak's economy is essentially dependent on external demand.

Global economy

At this juncture, the global economic condition remains fragile and talks of a possible double dip recession have resurfaced following concerns that economic recovery in the US has lost its momentum. Recent signs of weaknesses have been reflected in the 2Q GDP growth which tumbled to 2.4% from 3.3% in the earlier quarter. In addition, the austerity measures in the eurozone economy will likely have a significant negative repercussion given that some of its member countries are still in recession. All this should warrant some degree of concern considering the large exposure of Sarawak's economy to the global economy.

Political dynamics – State election in 2011

The present Chief Minister (CM), Tan Sri Abdul Taib Mahmud who has helmed the ruling dominant party Pesaka Bersatu Sarawak (PBB) for 29 years is now 74 years old. There is speculations that the CM will name his successor but at this juncture there are no solid indications as to who would likely replace him. This creates some degree of uncertainty which has a profound effect on the overall political landscape of Sarawak. It is worth noting that the CM post has never been contested in previous elections. There are also talks that the CM will name his successor after the state election, which is expected to be held in 2011.

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