MEDIA RELEASE

Economic Outlook
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Kuala Lumpur, 26 March 2010 – Global economic activity has rebounded sharply in the second half of 2009, thanks to very accommodative fiscal and monetary policy stimulus. Double-dip risks are clearly fading, with market optimism growing about 2010 growth prospects in tandem with upgrades in both private and public sector forecasts. Nevertheless, current headwinds include sovereign fiscal risks (including Greece), US-China trade tensions, and lingering fears that premature withdrawal of stimulus could decelerate the growth momentum from the robust clip in the first half going into the second half of this year. With Eurozone leaders continuing to blow hot and cold on the possibility of extending aid to Greece, and the IMF still seen as the less preferred option at this juncture, the potential for contagion effects to other peripheral Eurozone economies cannot be fully discounted. Meanwhile, US rhetoric pushing for China to appreciate the Yuan has stepped up of late, with tensions likely to escalate should domestic political pressure for the US Treasury to label China a FX manipulator succeed.

While medium-term economic fundamentals within Asia remain attractive, there are also potential pitfalls amid policy normalisation that must take place. In particular, fears about monetary policy tightening in China, following the two reserve requirement ratio hikes in January-February, generally revolve around potentially slowing growth in China, and hence for Asian economies as well. Our view is that recent Chinese measures are targeting more at managing liquidity rather than a policy shift per se. Nonetheless, recent interest rate increases in Malaysia and India have also heightened market anxiety that other Asian central banks could also front-load their monetary policy adjustments.

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The Malaysian economy has weathered the global economic crisis better-than-expected with a milder recession (-1.7%) in 2009. The official 2010 GDP growth forecast has been revised higher from the 2-3% earlier presented in the

November 2009 Budget to 4.5-5.5%. Given recent economic indicators have been fairly encouraging, especially for exports due to rising global demand for palm oil and electronics, we are optimistic that GDP growth could rebound to 5.4% this year, followed by 5.0% growth in 2011. Inflation should also remain modest around 2.6% on-year in 2010 given that both the fuel price subsidy cut and GST implementation have been postponed for now. The labour market should also continue to improve, with the unemployment rate possibly dipping below the 3% handle in the coming years.

Bank Negara Malaysia (BNM) has initiated its first OPR rate increase since November 2005, with a 25 basis point rate hike to 2.25% on 3 March with a view towards normalising monetary conditions and preventing the risk of financial imbalances that could undermine the economic recovery process. The economic prognosis is good - the economic recovery is firmly established and growth is expected to strengthen further going forward.

On the inflation front, prices will gradually increase during the year but inflation is expected to remain moderate in 2010. BNM also stressed that “at the new level of the OPR, the stance of monetary policy continues to remain accommodative and supportive of economic growth”. Looking ahead, we tip another two 25 basis point rate hikes to follow in the course of this year to bring the OPR to 2.75% by end-2010 as a continuation of policy normalisation.

Looking ahead, any structural/fundamental fiscal reform that may be unveiled in Malaysia’s “new economic model” is eagerly awaited. Market anticipation include the introduction of a Goods and Services Tax, fuel subsidy cuts, reforms to the social system, a “second wave of privatisation” and a sovereign global bond issue amongst others. Such potential measures, coupled with the healthy rebound in the domestic economy, should bode well for the plans to trim the budget deficit to 5.6% of GDP this year, and help mitigate any concerns about its budgetary health.

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