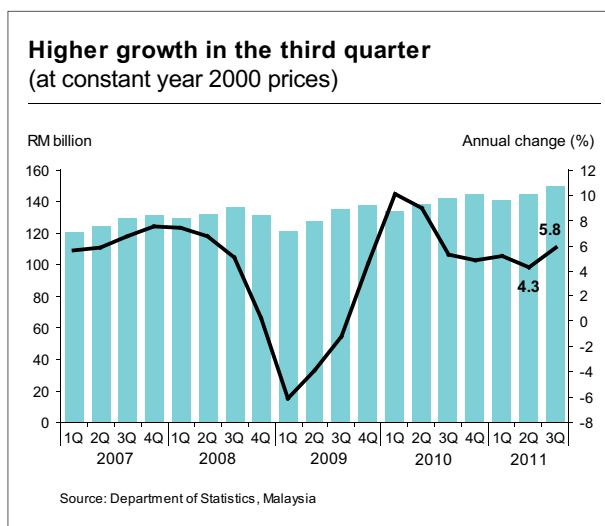


## ECONOMIC AND FINANCIAL DEVELOPMENTS IN MALAYSIA IN THE THIRD QUARTER OF 2011

### OVERVIEW

#### Growth improved in the third quarter

In the third quarter of 2011, the global economy continued to face a challenging environment. Continuing uncertainties in financial markets, unfavourable fiscal conditions and weaknesses in labour markets in the advanced economies continued to pose risks to growth in emerging economies, such as Malaysia. Despite the challenging environment, the Malaysian economy registered a higher growth of 5.8% (2Q 11: 4.3%), due to stronger domestic demand. The robust domestic demand was driven by an expansion in both household and business spending as well as higher public sector expenditure. On the supply side, most economic sectors recorded improvements in growth during the quarter, with the manufacturing sector recording a significantly better performance supported by firm regional demand for resource-based products, coupled with the normalisation in supply chain disruptions arising from the Japan natural disaster.



Domestic demand expanded by 9.0% (2Q 11: 5.6%), driven by the expansion in private sector spending and higher public sector expenditure. Private consumption increased by 7.3% (2Q 11: 6.4%), in line with favourable income growth while public consumption expanded by 21.7% (2Q 11: 6.6%) following higher expenditure on emoluments and supplies and services, as well

as bonus payments during the quarter. Gross fixed capital formation increased by 6.1% in the third quarter (2Q 11: 3.2%), supported by higher public sector capital spending, particularly the non-financial public enterprises, and continued expansion in private sector investment. Federal Government development expenditure during the quarter was mostly channelled into the public utilities, education, transportation, and trade and industry sectors. The private sector investment was underpinned by capital spending in the oil and gas industry; telecommunication sector and new growth areas such as renewable energy and medical equipment.

On the supply side, growth in most economic sectors strengthened in the third quarter. In the services sector, growth was supported mainly by domestic-driven activity. Higher growth in the manufacturing sector reflected the improvement in the supply chain and the robust performance of domestic-oriented industries. The construction sector registered a higher growth, led by the civil engineering sub-sector. The agriculture sector expanded on account of strong production of both crude palm oil and natural rubber. However, the mining sector continued to contract, albeit at a smaller pace, as output of crude oil was affected by shutdowns of production facilities.

The headline inflation rate, as measured by the change in the Consumer Price Index (CPI), rose to 3.4% on an annual basis in the third quarter (2Q 11: 3.3%). The increase in consumer prices was largely the result of higher prices in the *food and non-alcoholic beverages* category, which rose by 4.8% (2Q 11: 4.7%). Prices in the *transport* category registered a slower increase of 4.3% (2Q 11: 5.7%), in the absence of further adjustments to the prices of RON95 petrol and diesel in 2011.

In the external sector, the current account recorded a larger surplus of RM26.6 billion, equivalent to 12.5% of GNI due to a higher goods surplus and lower income deficits. The goods surplus widened to RM38.2 billion in the

3Q 2011 as export expansion outpaced import growth. Gross exports recorded a stronger growth of 11.4% (2Q 11: 8.8%), reflecting further expansion in exports of non-E&E manufactured products and commodities. Import growth was sustained at 7.4% (2Q 11: 7.4%).

The financial account turned around from a net inflow position to record a net outflow of RM23.3 billion (2Q 11: +RM44.5 billion), due to large net outflows of portfolio investments and lower net inflows of foreign direct investments. During the quarter, direct investments abroad by Malaysian companies increased further, while other investments reverted to record a net inflow, mainly by the private sector. Overall balance of payments remained strong, recording a surplus of RM10.9 billion in the third quarter (2Q 11: RM61.7 billion), as the higher surplus in the current account more than offset the net outflow position in the financial account.

The international reserves of Bank Negara Malaysia amounted to RM417.2 billion (equivalent to USD131 billion) as at 30 September 2011. The reserves level has taken into account the quarterly adjustment for foreign exchange revaluation. As at 31 October 2011, the reserves position had increased to RM429.1 billion, equivalent to USD134.8 billion, sufficient to finance 9.9 months of retained imports and is 4.1 times the short-term external debt.

### Monetary policy is supportive of economic activity

The Overnight Policy Rate (OPR) was left unchanged at 3.00% in the third quarter of 2011, following a 25 basis points increase in May. At the prevailing level, the OPR remains supportive of economic activity. The stance of monetary policy is consistent with the assessment of heightened uncertainties arising from global developments that have created greater downside risks to growth.

Reflecting the unchanged OPR, the average overnight interbank rate and interbank rates of other maturities were stable. In terms of retail interest rates, the average quoted fixed deposit (FD) rates, average base lending rate (BLR) and weighted average lending rate (ALR) on

loans outstanding of commercial banks were relatively unchanged. With retail lending rates still below pre-crisis levels, the cost of financing to the economy continues to remain supportive of the economy.

Financing activity in the third quarter remained resilient. Total gross financing raised by the private sector through the banking system and the capital market was sustained at RM223.9 billion in the third quarter (2Q 11: RM224.9 billion). On a net basis, banking system loans and PDS outstanding rose by an annual rate of 13.4% as at end-September (end-June 11: 12.8%). The major loan indicators remained healthy during the third quarter.

Net funds raised in the capital market amounted to RM12.7 billion during the quarter (2Q 11: RM20.8 billion), of which, 88%, or RM11.1 billion were raised by the private sector, especially through private debt securities. The net funds raised by the public sector amounted to RM1.6 billion in the third quarter.

The monetary aggregates continued to grow at a sustained pace during the third quarter. M3, or broad money registered an annual growth rate of 12.5% as at end-September 2011 (end-June 11: 12.4%).

The ringgit depreciated against the US dollar in the third quarter, in line with other regional currencies. The depreciation, mostly in September 2011, reflected mounting concerns over the European sovereign debt crisis and the sustainability of global economic recovery, which led to higher risk aversion and prompted some investors to unwind holdings of emerging market assets. Overall, the ringgit depreciated by 5.3% against the US dollar. Against other major currencies, the ringgit appreciated against the euro (1.5%), but depreciated against the pound sterling (-2.2%) and the Japanese yen (-9.9%). Against regional currencies, the ringgit strengthened against the Korean won (4.5%) and Singapore dollar (0.2%), but depreciated against other currencies in the range of 2.9% and 6.3%. During the period between 1 October and 16 November 2011, the ringgit appreciated against the US dollar (0.8%), Japanese yen (1.4%) and euro (1.3%) but depreciated against the pound

sterling (-0.4%). Against regional currencies, the ringgit strengthened against the Indonesian rupiah (3.3%), Singapore dollar (0.4%) and Chinese renminbi (0.1%) but depreciated against the Philippine peso (-0.1%), Thai baht (-0.3%) and Korean won (-3.0%).

### **Financial stability remained intact**

Financial stability remained intact throughout the third quarter, underpinned by sound financial institutions and orderly financial markets which continued to provide support for efficient financial intermediation in the domestic economy. Overall risks to financial stability remained low even under a more challenging external environment.

The banking sector remained highly resilient, with strong capital buffers, sustained profitability and ample liquidity. The core capital ratio and risk-weighted capital ratio of the banking system were sustained at a prudent level of 12.5% and 14.6% respectively. Similarly, the insurance and takaful sector exhibited the same resilience with a strong capital adequacy ratio of 221.1%.

### **Domestic economy to register growth amidst more challenging external environment**

Global economic recovery continued in the third quarter, albeit at a more modest and uneven pace. Global growth outlook has become significantly more uncertain following heightened downside risks. In particular, the possible escalation of the ongoing fiscal concerns in the advanced economies could add further strains to the international financial system and undermine the prospects for continued global growth.

In the Malaysian economy, the higher growth in the third quarter was underpinned by the stronger domestic demand and an improvement in the external sector arising from firm regional demand. Going forward, the more challenging international environment could present greater downside risks to Malaysia's growth prospects. Nevertheless, growth in domestic demand is expected to continue to be the anchor of growth, supported by expansion in private consumption and private investment. Public spending and investment activity are also expected to lend support to growth.

## DEVELOPMENTS IN THE THIRD QUARTER OF 2011

### INTERNATIONAL ECONOMIC ENVIRONMENT

#### Global growth continued to expand amid escalation of the European sovereign debt crisis

The global economy continued to face a challenging environment. While the impact from disruptions to the global supply chain stemming from Japan's natural disasters had receded significantly, new challenges have emerged. Against this background, global economic activity continued to expand, albeit at a modest pace, in the third quarter of 2011. Manufacturing activity rebounded amid a steady recovery from global supply chain disruptions. Nevertheless, the momentum was weaker than expected with sentiments dampened by fiscal-related concerns amid heightened volatility in the global financial markets. In the advanced economies, growth continued to be constrained by high unemployment, sluggish housing market and weakening sentiments amid rising policy uncertainties. Growth remained resilient in most Asian economies, supported by domestic demand and a gradual recovery in global production.

Conditions in the international financial markets deteriorated as developments in the advanced economies led to heightened risk aversion during the quarter. This was reflected in a sharp fall in equity markets, a sudden reversal of capital flows from the emerging market economies and the increased demand for liquid and 'safe haven' assets. Yields of the 10-year US Treasury bond reached historical lows while the sharp appreciation of the Japanese yen and the Swiss franc prompted the authorities to implement strong measures to stem further appreciation of their currencies. There has been a series of high profile events that affected investor confidence. In August, heightened financial market volatility was due mainly to intensified concerns over fiscal issues in the US, in particular uncertainties surrounding the debt ceiling debate which subsequently resulted in the downgrade of US sovereign credit rating. Market confidence was further affected in September by renewed concerns over a potential Greek sovereign debt default. Despite European leaders'

announcement of a second bailout package plan for Greece on 21 July, financial markets remained highly volatile given uncertainties surrounding the plan and growing concerns over contagion risk to the other euro area economies. In particular, Italy and Spain experienced sovereign rating downgrades while their long-term bond yields rose to record highs. In addition, banks in the region that had large exposures to troubled sovereign debt faced renewed funding stress. In October, global financial conditions improved slightly on investors' optimism that European leaders will agree on a comprehensive solution to the debt crisis, prompting a rebound in equity markets and a rise in the yields on Treasuries.

In the third quarter, growth of the **US** economy was sustained at 1.6% in annual terms (2Q 11: 1.6%). On a seasonally adjusted annualised basis, the US economy grew at a faster pace of 2.5% (2Q 11: 1.3%) as supply chain disruptions associated with the natural disasters in Japan diminished while headwinds from higher oil prices moderated. Consumption spending rose, reflecting a rebound in motor vehicle sales and an increase in services amidst a drawdown in personal savings. However, the pace of consumption spending remained modest due to a decline in real wage and financial net wealth. Private fixed investment grew by 17.4% (2Q 11: 6.3%) following higher growth in capital spending on equipment and software which offset a negative contribution from private inventory investment. Net exports continued to support growth following an expansion in exports that offset higher imports. Inflation rose by 3.8% (2Q 11: 3.4%) due mainly to higher food, housing and apparel prices.

Growth in the **euro area** moderated to 1.4% (2Q 11: 1.6%) on an annual basis while on a quarter-on-quarter basis, growth was sustained at 0.2%, supported by a rebound in economic activity in the core economies, Germany and France. Growth in the region, however, remained modest due to weak domestic demand as private sector sentiments in both the core and peripheral economies were affected by the intensification

of the sovereign debt crisis during the quarter. In several of the affected economies, the announcement of additional austerity measures further weighed on domestic economic activity. Inflation remained high, with consumer prices rising at a rate of 2.7% (2Q 11: 2.8%), due mainly to elevated energy prices.

In the **UK**, real GDP growth moderated to 0.5% on an annual basis (2Q 11: 0.6%). On a quarter-on-quarter basis, however, the economy expanded at a faster pace of 0.5% (2Q 11: 0.1%) following the rebound of activity in the production and services sectors which were impacted by temporary factors in the previous quarter. Nevertheless, domestic demand continued to be weighed down by fiscal austerity measures, weaker sentiments and higher consumer prices. Inflation increased at a faster rate of 4.7% (2Q 11: 4.4%), driven by higher energy prices and the increase in the value-added tax in January 2011.

In **Japan**, the economy recorded a flat growth on an annual basis in the third quarter (2Q 11: -1.1%). This represented an improvement in economic activity after two consecutive quarters of negative growth since the beginning of the year. On a seasonally adjusted annualised basis, the economy expanded at a faster pace of 6% (2Q 11: -1.3%), supported by the rebound in exports and domestic demand. Exports registered a strong growth of 27.4% (2Q 11: -18.4%) following the recovery in shipments of automobiles and auto parts. On the domestic front, private consumption continued to improve, supported by better consumer confidence. Core consumer prices (excluding fresh food) rose by 0.2% (2Q 11: -0.3%) due to higher energy prices.

Monetary policy in the advanced economies remained accommodative. In the US, the **Federal Open Market Committee (FOMC)** maintained the federal funds rate at 0 - 0.25% and decided to keep it at low levels at least through mid-2013. In addition, the FOMC announced a maturity extension programme, which consisted of purchasing USD400 billion of longer-term Treasury securities while selling an equivalent amount of short-term securities. In the euro area, the **European Central Bank (ECB)** raised its policy rate on 7 July by 25 basis points to 1.50% to counter rising inflationary pressures. However, amid

the increased downside risks arising mainly from stress in the financial markets, in October, the ECB introduced longer-term refinancing facilities and announced a new €40 billion covered bond purchase programme to provide additional liquidity to the financial sector. Subsequently, on 3 November, the ECB reduced its policy rate by 25 basis points to 1.25% in view of the weaker growth outlook. **The Bank of England (BoE)** maintained its policy rate at 0.5% during the quarter.

#### Advanced Economies: Real GDP Growth

	2010		2011		
	3Q	4Q	1Q	2Q	3Q
	Annual change (%)				
US <sup>1</sup>	2.5	2.4	0.4	1.3 <sup>†</sup>	2.5 <sup>‡</sup>
Japan <sup>1</sup>	2.9	-2.7	-2.7	-1.3 <sup>†</sup>	6.0 <sup>‡</sup>
Euro area	2.1	1.9	2.4	1.6	1.4 <sup>‡</sup>
UK	2.6	1.3	1.6	0.6 <sup>†</sup>	0.5 <sup>‡</sup>

<sup>1</sup> Annualised basis  
<sup>†</sup> Revised  
<sup>‡</sup> Advance estimate  
<sup>‡</sup> Preliminary

Source: National authorities

However, it announced further quantitative easing measures in October as it increased the size of its asset purchase programme by £75 billion to £275 billion to support the weak economic recovery in the UK. **The Bank of Japan (BoJ)** kept its overnight policy rate in the range of 0 – 0.1% and in August and October, it expanded its asset purchase and fixed-rate lending programmes to a total of ¥20 trillion and ¥35 trillion, respectively. The BoJ also extended its ¥1 trillion loan programme to financial institutions in areas affected by the natural disasters for another six months until April 2012.

Economic activity in **Asia** continued to grow in the third quarter amid recovery in the global supply chain network. Regional exports were supported by demand from within Asia and other emerging economies, while commodity-exporting economies continued to benefit from elevated commodity prices. Domestic demand remained resilient in the region as favourable labour market conditions and rising wages sustained private consumption, while improving capacity utilisation rates provided some support

for investment activity. **Singapore's** economic growth accelerated to 5.9% (2Q 11: 1.0%), as a rebound in the biomedical manufacturing cluster supported the economy amid continued weakness in electronics-related manufacturing. **Indonesia's** economy was sustained at 6.5% (2Q 11: 6.5%) supported by a broad-based expansion across domestic demand and exports. **Korea's** economic growth was also sustained at 3.4% (2Q 11: 3.4%) supported by government spending. In **PR China**, economic growth moderated to 9.1% (2Q 11: 9.5%) due to slower expansion in the manufacturing and services sectors. **Hong Kong's** economy grew at a slower pace of 4.3% (2Q 11: 5.3%) due mainly to a decline in exports. **Chinese Taipei's** economy moderated to 3.4% (2Q 11: 5.0%) due to contraction in capital expenditures and slower private consumption.

#### Regional Countries: Real GDP Growth

	2010		2011		
	3Q	4Q	1Q	2Q	3Q
Annual change (%)					
PR China	9.6	9.8	9.7	9.5	9.1
Singapore	10.5	12.0	9.3	1.0 <sup>†</sup>	5.9 <sup>‡</sup>
Korea	4.4	4.7	4.2	3.4 <sup>†</sup>	3.4 <sup>‡</sup>
Chinese Taipei	10.7	7.1	6.2	5.0	3.4 <sup>‡</sup>
Indonesia	5.8	6.9	6.5	6.5	6.5
Hong Kong SAR	6.9	6.4	7.5	5.3 <sup>†</sup>	4.3 <sup>‡</sup>

<sup>†</sup> Preliminary  
<sup>‡</sup> Advance estimate  
<sup>†</sup> Revised

Source: National authorities

Inflationary pressures in the region remained elevated. Headline inflation continued to increase in PR China, and Korea due to higher food prices, while in Hong Kong, it was driven mainly by increases in housing rentals. Core inflation rates also trended up in several economies such as Hong Kong, Indonesia, Korea and Thailand, reflecting underlying demand pressures. Amidst sustained economic growth and elevated inflationary pressures, several regional central banks continued to normalise or tighten their policy interest rates in the third quarter. The **People's Bank of China** raised its policy rate by 25 basis points to 6.56% in July to contain

inflationary pressures. The **Reserve Bank of India** increased its repurchase rate by a total of 100 basis points in July, September and October to 8.50% on similar concerns. Furthermore, while keeping its benchmark interest rates unchanged, the **Bangko Sentral ng Pilipinas** raised the banks' reserve requirement ratio by 100 basis points to 21% in July to better manage liquidity. However, in October, central banks in the region began to reassess the balance of risks between supporting growth and curbing inflation given heightened uncertainty in the global economy. Amid moderating inflationary pressures and increasing signs of a slowdown in the global economy, **Bank Indonesia** cut its benchmark interest rate by a total of 75 basis points to 6.00% in October and November. The **Bank of Thailand** kept its 1-day repurchase rate unchanged for the first time this year, after raising its policy rate six times since January, including 25 basis points each in July and August, given an uncertain global outlook and widespread flooding in the country.

**Crude oil prices**<sup>1</sup> moderated in the third quarter, averaging USD90 per barrel (2Q 11: USD102 per barrel). The decline in oil prices was driven by expectations of weaker demand due to growing concerns over uncertain global growth prospects. Furthermore, improved supply conditions following the restart of oil production in Libya also helped to push crude oil prices lower. By the end of the quarter, crude oil was trading at a 12-month low of USD79 per barrel. However, in October, the downward trend in oil prices reversed as a result of optimism about the announcement of more credible measures by European leaders to resolve the ongoing sovereign debt crisis. On 18 October, crude oil prices rose to USD88.30 per barrel.

The **foreign exchange markets** around the world experienced considerable volatility during the third quarter as positions were adjusted by investors in light of the various high profile events affecting the world economy. The US dollar appreciated against most major and regional currencies. The US dollar's strength was supported by flight-to-liquidity flows due to concerns over the sustainability

of global growth. The euro weakened during the quarter following intensification of the European sovereign debt crisis. Similarly, the increased risk aversion resulted in the depreciation of regional currencies against the US dollar. With the exception of the renminbi, the significant depreciation experienced by most regional currencies in September had erased the appreciation recorded earlier this year. The Japanese yen, on the other hand, strengthened against the US dollar due to safe haven flows. Despite a temporary decline following a unilateral intervention by the Bank

of Japan in early August, the yen traded near its historical high, ending the quarter at ¥77 per US dollar.

Global growth outlook has become significantly more uncertain following heightened downside risks that are exacerbated by the continued fragilities in the advanced economies. In particular, the possible escalation of the ongoing fiscal concerns in the advanced economies could add further strains to the international financial system and undermine the prospects for continued global growth.

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<sup>1</sup> Refers to West Texas Intermediate one-month futures on NYMEX

## DEVELOPMENTS IN THE MALAYSIAN ECONOMY

### Growth improved in the third quarter

In the third quarter of 2011, the global economy continued to be confronted by a number of challenges. Continuing uncertainties in financial markets, unfavourable fiscal conditions and weaknesses in labour markets in the advanced economies continued to pose risks to growth of the emerging economies, like Malaysia. Despite the challenging environment, the Malaysian economy registered a higher growth of 5.8% (2Q 11: 4.3%), due to stronger domestic demand. The robust domestic demand was driven by an expansion in both household and business spending as well as higher public sector expenditure. On the supply side, most economic sectors recorded improvements in growth during the quarter, with the manufacturing sector recording a significantly better performance supported by firm regional demand for resource-based products, coupled with the normalisation in supply chain disruptions arising from the Japan natural disaster.

### Domestic demand expanded at a faster pace

**Domestic demand** expanded by 9.0% in the third quarter (2Q 11: 5.6%). Growth was driven by the expansion in both household and business spending and higher public sector expenditure.

**Private consumption** recorded a strong growth of 7.3% (2Q 11: 6.4%) amid favourable income growth as labour market conditions remained stable and civil servants benefited from the half-month bonus payment. Firm commodity prices continued to support rural household income. Improved consumer sentiments, as reflected by the increase in the 3Q MIER Consumer Sentiments Index (108.7 points, 2Q 11: 107.9 points), also supported spending during the period. Major consumption indicators showed sustained increase in consumer spending. These include sales of food and beverages, sales of new passenger cars, imports of consumption goods, bank lending to households and credit card spending.

**Public consumption** expanded by 21.7% (2Q 11: 6.6%) following higher expenditure on emoluments and supplies and services, as

### GDP by Expenditure Components (at constant 2000 prices)

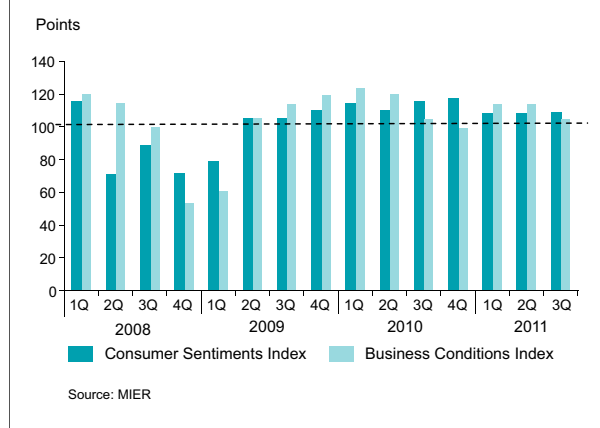
	2010		2011		
	3Q	4Q	1Q	2Q	3Q
	Annual change (%)				
Aggregate Domestic Demand (excluding stocks)	4.9	5.9	7.3	5.6	9.0
Consumption	3.3	4.8	7.6	6.4	9.9
<i>Private sector</i>	6.7	6.4	6.7	6.4	7.3
<i>Public sector</i>	-9.8	0.1	11.7	6.6	21.7
Gross Fixed Capital Formation	10.1	10.0	6.5	3.2	6.1
Net Exports	-30.8	-19.2	-39.6	17.2	18.1
<i>Exports of Goods and Services</i>	6.8	1.7	1.4	4.1	4.2
<i>Imports of Goods and Services</i>	11.2	3.5	8.4	3.2	3.2
<b>GDP</b>	<b>5.3</b>	<b>4.8</b>	<b>5.2</b>	<b>4.3</b>	<b>5.8</b>

Source: Department of Statistics, Malaysia

well as a bonus payment during the quarter. This reflected the continued efforts by the Government to improve the public delivery services through repairs and maintenance of public goods and provision of essential services such as healthcare and education.

**Gross fixed capital formation** increased by 6.1% in the third quarter (2Q 11: 3.2%), supported by higher public sector capital spending, particularly the non-financial public enterprises (NFPEs) and continued expansion in private sector investment. The latter benefited from continued growth in domestic demand and positive business sentiments. It also reflected on-going exploration and development activity in the oil and gas industry and the expansion in telecommunication sector. New capacity continued to be added in the renewable energy and medical equipment industries. Major investment indicators such as sales of commercial vehicles, production and sales of construction-related materials and bank lending to businesses exhibited steady growth, pointing to continued expansion in private sector capital spending. Business sentiments were positive as the MIER Business Conditions Index remained above the 100-point benchmark level (104.5 points, 2Q 11: 114.0 points). The bulk of government development expenditure in the third quarter was channelled into the public utilities, education, transportation, and trade and industry sectors, while the NFPEs' investments were channelled mainly into the oil and gas, utilities and transportation sectors.

### Businesses and consumers remained optimistic



### Growth strengthened in major economic sectors

On the supply side, growth in most economic sectors strengthened in the third quarter, led by higher growth in the services and manufacturing sectors. The better performance of the services sector was supported mainly by domestic-driven activity while in the manufacturing sector, growth reflected improvements in the supply chain and the higher output of domestic-oriented industries. The construction sector also registered a higher growth, supported by the civil engineering sub-sector. The agriculture sector expanded further, while the mining sector contracted at a slower pace.

The **services sector** grew by 7.0% in the third quarter of 2011 (2Q 11: 6.8%), contributing 4.0 percentage points to overall growth. Growth was supported mainly by stronger domestic demand. The **wholesale and retail trade** sub-sector advanced by 9.0% (2Q 11: 7.3%). Growth in the retail segment remained resilient, as a result of firm private consumption. The increase in private consumption also supported continued growth in the **accommodation and restaurant** sub-sector (5.4%; 2Q 11: 5.6%). The **finance and insurance** sub-sector expanded by 4.6% (2Q 11: 5.6%), with continued growth in net interest and fee-based income arising from loan growth. The **real estate and business services** sub-sector registered a growth of 6.7% (2Q 11: 7.6%), underpinned by favourable capital market-related activity during the quarter.

### GDP by Economic Activity (at constant 2000 prices)

	2010		2011		
	3Q	4Q	1Q	2Q	3Q
	Annual change (%)				
Agriculture	3.0	-3.9	-0.2	6.9	8.2
Mining	-0.7	-1.2	-4.2	-9.2	-6.1
Manufacturing	7.6	6.2	5.5	2.1	5.1
Construction	2.8	5.6	3.8	0.6	3.0
Services	5.3	6.1	7.0	6.8	7.0
<b>Real GDP (Annual Change)</b>	<b>5.3</b>	<b>4.8</b>	<b>5.2</b>	<b>4.3</b>	<b>5.8</b>
<b>Real GDP (Preceding Change)</b>	<b>2.3</b>	<b>1.7</b>	<b>-2.5</b>	<b>2.8</b>	<b>3.7</b>

Source: Department of Statistics, Malaysia

### Performance of the Services Sector (value added at constant 2000 prices)

	Share 2010 (%)	2010		2011		
		3Q	4Q	1Q	2Q	3Q
		Annual change (%)				
<b>Intermediate Services</b>	<b>43.7</b>	<b>6.7</b>	<b>6.0</b>	<b>6.8</b>	<b>6.0</b>	<b>6.0</b>
Finance & insurance	20.3	6.4	3.7	6.8	5.6	4.6
Real estate & business services	9.5	6.3	8.7	8.8	7.6	6.7
Transport & storage	6.6	5.6	5.2	4.3	4.7	6.1
Communication	7.4	9.2	9.8	6.4	6.4	8.7
<b>Final Services</b>	<b>56.3</b>	<b>4.2</b>	<b>6.3</b>	<b>7.1</b>	<b>7.5</b>	<b>7.9</b>
Wholesale & retail trade	23.6	5.7	8.3	6.8	7.3	9.0
Accommodation & restaurant	4.2	5.1	3.7	4.0	5.6	5.4
Utilities	5.2	3.8	4.2	1.3	2.4	4.6
Government services	13.0	2.0	6.1	13.7	12.8	10.7
Other services	10.2	3.7	3.9	3.9	4.6	4.3
<b>Total Services</b>	<b>100.0</b>	<b>5.3</b>	<b>6.1</b>	<b>7.0</b>	<b>6.8</b>	<b>7.0</b>

Source: Department of Statistics, Malaysia

### Selected Quarterly Indicators in the Services Sector

	2010			2011		
	2Q	3Q	4Q	1Q	2Q	3Q
<b>Index</b>						
MIER Consumer Sentiments Index	110.4	115.8	117.2	108.2	107.9	108.7
MIER Retail Trade Index	134.1	140.0	132.0	99.1	120.8	150.0
MIER Tourism Market Index	118.2	118.8	124.6	113.1	125.4	115.2
<b>Annual change (%)</b>						
Tourist arrivals	3.9	5.6	1.2	-3.7	-4.8	n.a.
Total passenger traffic at all airports	14.1	10.0	6.3	11.8	13.4	10.8
Total consumption credit outstanding	10.6	10.7	9.8	9.5	8.7	8.5
Loans outstanding to the wholesale & retail trade, hotels & restaurants	8.6	7.3	7.5	7.2	6.8	9.6
Imports of consumption goods	12.8	2.8	6.9	5.8	17.5	26.5
Total sales of motor vehicles	17.4	3.7	9.3	7.5	-9.7	0.6
Container cargo handled (Port Klang and PTP)	21.3	10.9	9.6	14.4	9.6	9.8

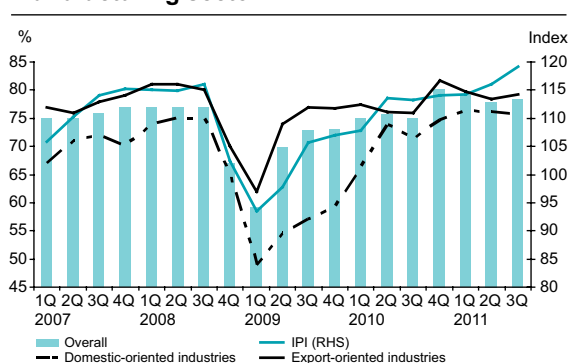
Source: Various sources

In the **manufacturing sector**, value-added growth increased to 5.1% (2Q 11: 2.1%), due to improvements in the production of both domestic-oriented and **export-oriented industries**. In the export-oriented industries, growth was supported by the primary-related cluster with the chemicals and chemical products industry recording a faster expansion during the quarter, driven by firm regional demand. Output of E&E continued to decline, but at a slower pace, as sustained regional demand for semiconductors more than offset the double-digit decline in the production of computers and parts. On the other hand, the robust performance of **domestic-oriented industries** cluster reflected the turnaround in the consumer-related cluster and further strengthening of the construction-related cluster. The turnaround in the consumer-related cluster was due mainly to the gradual normalisation in the production of transport

equipment, as global automotive supply chain pressures continued to recede.

Overall capacity utilisation rate in the manufacturing sector was sustained (78%; 2Q 11: 78%). Export- and domestic-oriented industries operated at 79% and 76% of total capacity respectively during the quarter (2Q 11: 78% and 76% respectively).

### Capacity utilisation rate in the manufacturing sector\*



\* Beginning 2009, the capacity utilisation rate in the manufacturing sector has been rebased from value-add in year 2004 to value-add in year 2006

Source: Bank Negara Malaysia & Department of Statistics, Malaysia

### Performance of the Manufacturing Sector

	2010		2011		
	3Q	4Q	1Q	2Q	3Q
<b>Annual Change (%)</b>					
Value Added (at constant 2000 prices)	7.6	6.2	5.5	2.1	5.1
Overall Production <sup>1</sup>	7.2	6.6	5.9	2.2	5.2
<b>Export-oriented industries</b>	<b>6.4</b>	<b>4.6</b>	<b>5.1</b>	<b>1.7</b>	<b>3.8</b>
<b>Electronics and electrical products cluster</b>	<b>9.6</b>	<b>0.1</b>	<b>-5.3</b>	<b>-5.5</b>	<b>-0.5</b>
<i>Of which:</i>					
Electronics	-7.4	-16.5	-18.1	-13.4	-3.8
Electrical products	44.6	34.8	17.9	6.8	4.0
<b>Primary-related industry cluster</b>	<b>4.7</b>	<b>7.2</b>	<b>11.3</b>	<b>6.0</b>	<b>6.3</b>
<i>Of which:</i>					
Chemicals and chemical products	8.0	4.7	5.5	6.1	9.2
Petroleum products	0.2	16.3	26.0	1.4	1.7
Rubber products	17.5	12.7	12.4	18.3	15.5
Off-estate processing products	2.9	-14.1	-7.4	17.6	9.9
<b>Domestic-oriented industries</b>	<b>9.8</b>	<b>13.6</b>	<b>8.9</b>	<b>3.8</b>	<b>9.7</b>
<b>Construction-related cluster</b>	<b>9.3</b>	<b>22.2</b>	<b>22.1</b>	<b>17.4</b>	<b>18.6</b>
<i>Of which:</i>					
Construction-related materials	14.8	20.4	15.3	15.4	13.0
Fabricated metal products	2.5	24.7	32.0	20.1	26.5
<b>Consumer-related cluster</b>	<b>10.1</b>	<b>7.6</b>	<b>-0.3</b>	<b>-6.2</b>	<b>3.3</b>
<i>Of which:</i>					
Transport equipment	20.7	20.8	-3.9	-14.7	-0.1
Food, beverage & tobacco products	11.1	9.3	6.7	2.1	4.6

<sup>1</sup> Industrial Production Index (2005=100)

Source: Department of Statistics, Malaysia

In the commodities sector, value-added growth of the **agriculture sector** increased to 8.2% (2Q 11: 6.9%), reflecting mainly continued strong production of both crude palm oil and natural rubber, as well as a turnaround in fisheries and forestry. However, the **mining sector** contracted by 6.1% (2Q 11: -9.2%), as the production of crude oil declined, attributed to shutdowns of several crude oil production facilities for maintenance purposes, declining production from mature fields and lower-than-expected production from new fields.

The **construction sector** registered a higher growth of 3.0% during the quarter (2Q 11: 0.6%), led by a turnaround in the civil engineering sub-sector. In addition to the progress made in major projects such as the Second Penang Bridge and KLIA2, the sub-sector was also supported by a pick-up in the implementation of other infrastructure projects. The residential sub-sector expanded further, underpinned by accommodative financing and stable labour market conditions while the non-residential sub-sector was supported by ongoing construction of commercial properties.

### Performance of the Agriculture Sector

	2010		2011		
	3Q	4Q	1Q	2Q	3Q
	Annual change (%)				
<b>Value Added (at constant 2000 prices)</b>	<b>3.0</b>	<b>-3.9</b>	<b>-0.2</b>	<b>6.9</b>	<b>8.2</b>
<b>Industrial Crops</b>	<b>-1.9</b>	<b>-10.2</b>	<b>-8.3</b>	<b>9.9</b>	<b>10.4</b>
<b>Food Crops</b>	<b>8.7</b>	<b>4.5</b>	<b>8.9</b>	<b>3.5</b>	<b>5.8</b>
<b>Production</b>					
<i>Of which:</i>					
Crude palm oil	3.1	-15.1	-7.7	22.2	12.8
Rubber	0.4	6.1	2.5	16.8	15.8
Fish	6.1	2.4	2.0	-1.4	2.7
Livestock	2.6	-2.2	-6.3	6.7	5.6

Source: Malaysian Palm Oil Board (MPOB)  
Malaysian Rubber Board (MRB)  
Fisheries Department, Malaysia  
Department of Veterinary Services, Malaysia  
Department of Statistics, Malaysia

### Indicators for the Construction Sector

	2010		2011		
	3Q	4Q	1Q	2Q	3Q
	Annual change (%)				
New sales and advertising permits	8.6	13.0	25.1	11.6	6.0
Housing approvals	43.1	31.7	31.6	14.1	54.1
Production <sup>1</sup> of construction-related materials	9.3	22.2	22.1	17.4	18.6
Loans approved for construction	77.0	49.7	29.3	31.8	-20.5
Imports of construction materials and mineral products	13.7	23.1	-1.2	23.3	24.4

<sup>1</sup> Industrial Production Index (2005=100)

Source: Ministry of Housing and Local Government, Department of Statistics, Malaysia and Bank Negara Malaysia.

### Performance of the Mining Sector

	2010		2011		
	3Q	4Q	1Q	2Q	3Q
	Annual change (%)				
<b>Value Added (at constant 2000 prices)</b>	<b>-0.7</b>	<b>-1.2</b>	<b>-3.0</b>	<b>-9.2</b>	<b>-6.1</b>
<b>Production</b>					
<i>Of which:</i>					
Crude oil and condensates	-5.5	-4.4	-7.3	-17.8	-9.9
Natural gas	5.6	0.2	-0.9	2.7	-1.5

Source: PETRONAS  
Department of Statistics, Malaysia

## Inflation increased in the third quarter

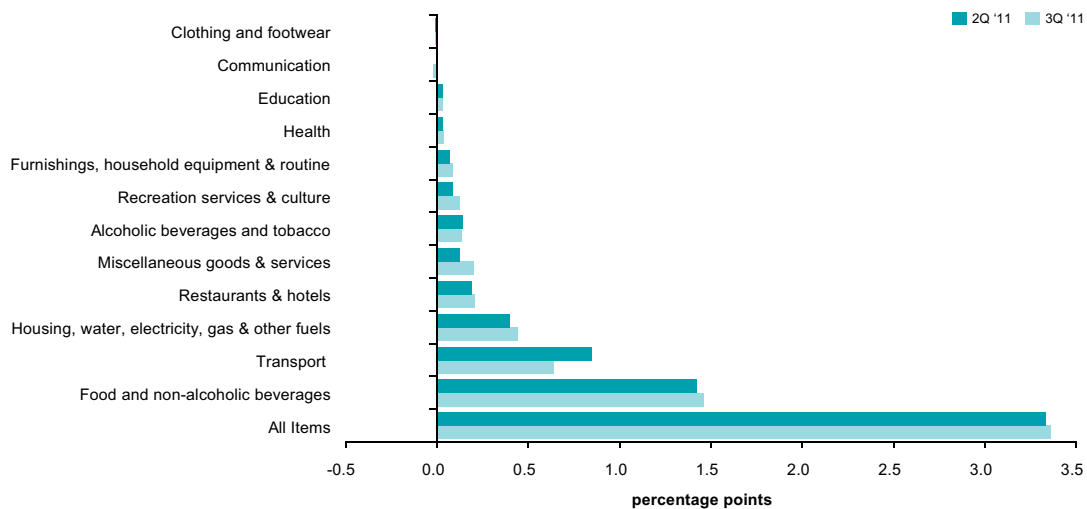
The headline inflation rate, as measured by the change in the Consumer Price Index (CPI), rose to 3.4% on an annual basis in the third quarter (2Q 11: 3.3%). The increase in consumer prices was largely the result of higher prices in the *food and non-alcoholic beverages* category, which rose by 4.8% (2Q 11: 4.7%). Higher food prices were mainly due to higher prices in the *food away from home* category which has been rising gradually since early 2011 (4.9%, 2Q 11: 4.4%). Prices in the fish and seafood category also recorded a higher inflation of 6.7% in the third quarter (2Q 11: 5.2%).

Prices in the *transport* category registered a slower increase of 4.3% (2Q 11: 5.7%) in

the third quarter, in the absence of further adjustments to the prices of RON95 petrol and diesel in 2011. Price increases in the third quarter were partially mitigated by declining prices in the *communication* and *clothing and footwear* categories.

The Producer Price Index (PPI) increased at a higher rate of 10.9% on an annual basis during the quarter (2Q 11: 10.2%). In terms of composition, the prices of commodity-related components were higher by 29.6% (2Q 11: 27.1%). Price increases in the non-commodity-related components of the PPI were unchanged at 2.3% (2Q 11: 2.3%). Prices of the local components of the PPI rose by 14.9% (2Q 11: 13.6%) while prices of the imported components of the PPI recorded a slower increase of 2.3% (2Q 11: 2.8%).

### Contribution to Consumer Price Inflation

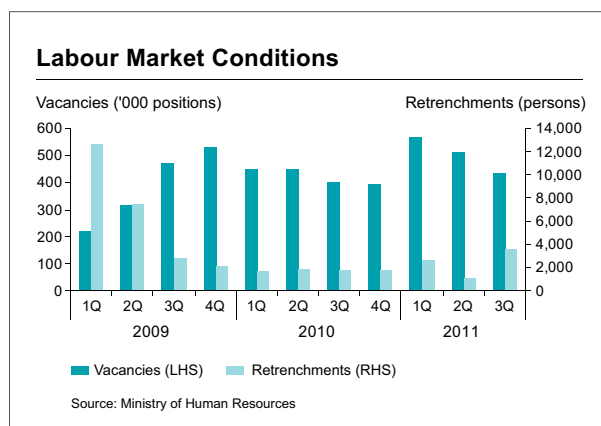


Source: Bank Negara Malaysia

## Stable labour market conditions

Overall labour market conditions remained stable, with the unemployment rate unchanged at 3.0% during the first two months of the quarter (2Q 11: 3.0%). Retrenchments increased to 3,605 persons (2Q 11: 1,105 persons), due mostly to one-off incidences in the month of August, in which a total of 2,545 workers were retrenched. Closures of several companies in the low end segment of the E&E and furniture industries accounted for 77% for total layoffs during the month. Despite the higher retrenchment, there was a net employment gain, mainly in the domestic-oriented sectors (July-Aug employment: 12.32 mil persons; 2Q 11: 12.13 mil persons).

Labour demand during the quarter remained high, as evidenced by the sustained high number of job vacancies posted in the JobsMalaysia Portal (431,437 positions; 2Q 11: 514,189 positions). The decline from the previous quarter reflects the lower number of job openings in the manufacturing and services sectors. Real wages in the manufacturing sector expanded at a slower pace as compared to the preceding quarter (3.9%; 2Q 11: 4.7%).



## External sector remained strong

**Overall balance of payments** remained strong, recording a surplus of RM10.9 billion in 3Q 2011 (2Q 11: RM61.7 billion), as the higher surplus in the current account more than offset the net outflow position in the financial account.

## Balance of Payments

	2010		2011		
	3Q	4Q	1Q	2Q	3Q
	RM billion				
<b>Current Account</b>	<b>20.2</b>	<b>23.8</b>	<b>25.9</b>	<b>23.4</b>	<b>26.6</b>
(% of GNI)	10.7	11.9	13.1	11.5	12.5
Goods	28.0	32.3	38.1	36.3	38.2
Services	1.1	0.9	-1.3	-0.7	-2.4
Income	-3.5	-4.0	-5.7	-6.9	-3.8
Current transfers	-5.3	-5.5	-5.2	-5.3	-5.3
<b>Financial Account</b>	<b>-3.3</b>	<b>1.2</b>	<b>-6.0</b>	<b>44.5</b>	<b>-23.3</b>
Direct investment abroad	-24.1	-8.9	-10.1	-7.9	-12.9
Foreign direct investment	6.5	10.7	11.1	10.2	5.2
Portfolio investment	18.3	3.5	8.4	48.1	-23.4
Financial derivatives	0.8	0.1	0.1	0.4	-0.3
Other investment	-4.8	-4.3	-15.5	-6.3	8.2
- Official sector	1.4	-0.2	-0.5	-0.2	-0.5
- Private sector	-6.2	-4.2	-14.9	-6.1	8.7
Errors & omissions	-15.9	-7.0	-4.0	-6.2	7.6
<b>Overall Balance</b>	<b>1.0</b>	<b>17.9</b>	<b>15.9</b>	<b>61.7</b>	<b>10.9</b>

Source: Department of Statistics Malaysia

The **current account** recorded a larger surplus of RM26.6 billion, equivalent to 12.5% of GNI due to higher goods surplus and lower income deficits. The goods surplus widened to RM38.2 billion in the 3Q 2011 as export expansion outpaced import growth. Gross exports recorded a stronger growth of 11.4% (2Q 11: 8.8%), reflecting further expansion in exports of non-E&E manufactured products and commodities. Import growth sustained at 7.4% (2Q 11: 7.4%).

## Trade Account

	2010		2011		
	3Q	4Q	1Q	2Q	3Q
	Annual change (%)				
<b>Gross Exports</b>	<b>9.0</b>	<b>3.3</b>	<b>4.9</b>	<b>8.8</b>	<b>11.4</b>
Manufactured	5.4	-0.3	-0.6	1.6	4.9
E&E	4.0	-8.0	-7.5	-5.0	-4.0
Non-E&E	7.1	10.2	7.5	9.4	15.8
Commodities	25.0	15.8	19.5	28.9	28.6
Agriculture	17.8	31.9	26.5	43.3	44.9
Minerals	30.1	5.7	14.8	19.3	17.8
<b>Gross Imports</b>	<b>16.4</b>	<b>10.2</b>	<b>12.5</b>	<b>7.4</b>	<b>7.4</b>
Capital goods	18.4	9.0	16.7	10.2	5.6
Intermediate goods	16.1	10.6	12.5	3.8	3.7
Consumption goods	2.8	6.9	5.8	17.5	26.5
<b>Trade balance (RM billion)</b>	<b>22.1</b>	<b>25.5</b>	<b>31.8</b>	<b>27.4</b>	<b>30.1</b>

Source: MATRADE and Department of Statistics, Malaysia

### Malaysia: Direction of Exports

	2010		2011			2010		2011		
	3Q	4Q	1Q	2Q	3Q	3Q	4Q	1Q	2Q	3Q
	Annual change (%)					Share of total exports (%)				
United States	-1.3	-11.0	-8.0	-7.1	-3.6	9.7	9.1	8.3	8.5	8.4
European Union (EU)	10.6	0.3	5.3	3.4	6.3	10.8	10.8	10.7	10.2	10.3
Selected ASEAN countries <sup>1</sup>	4.4	1.9	0.1	6.3	10.1	24.1	25.3	24.6	24.6	23.8
North East Asia	7.0	1.4	2.5	9.0	14.6	24.6	24.2	24.4	24.5	25.3
People's Republic of China	2.4	-0.5	3.9	9.7	27.1	12.4	12.3	12.9	12.5	14.2
Hong Kong SAR	-1.7	-0.7	0.0	-4.6	-2.2	5.2	5.0	4.6	4.7	4.5
Chinese Taipei	18.0	30.6	16.9	14.7	4.3	3.4	3.3	3.2	3.3	3.2
Korea	32.1	-8.3	-8.3	22.1	5.0	3.6	3.7	3.8	4.0	3.4
West Asia	-8.1	11.0	17.6	13.1	11.9	3.4	3.7	3.7	3.7	3.4
India	28.2	20.2	24.2	45.6	36.0	3.5	3.3	3.9	4.1	4.3
Total exports	9.0	3.3	4.9	8.8	11.4	100.0	100.0	100.0	100.0	100.0

<sup>1</sup>Singapore, Thailand, Indonesia, Philippines, Brunei Darussalam and Vietnam

Source: Department of Statistics, Malaysia

The stronger export performance reflected a broad-based expansion in all major export sectors. Higher growth in exports of non-E&E products was attributable mainly to higher demand for chemicals and chemical products; machinery appliances and parts, manufactures of metal, and iron and steel products. The elevated commodity prices and higher demand boosted exports of commodities. In contrast, exports of E&E products remained weak due to sluggish global demand for computers and computer-related products.

Growth of gross imports was sustained at 7.4% in 3Q 2011. Improvement in manufactured exports contributed to the sustained growth in intermediate imports. Consumption imports expanded strongly, particularly for transport equipment as well as food and beverages. Growth in capital imports moderated due to lower lumpy imports while capital goods for capacity expansion continued to increase.

During the quarter, the **income account** recorded a lower deficit of RM3.8 billion attributed to higher investment income accruing to Malaysian companies investing abroad and lower investment income accruing to foreign direct investors in Malaysia. The **services account** deficit widened to RM2.4 billion, attributable mainly to lower net receipts from travel amid higher net payments for imported transportation services.

The **financial account** turned around from a net inflow position to record a net outflow of RM23.3 billion in 3Q 2011 (2Q 11: +RM44.5 billion), due to large net outflows of portfolio investment and lower net inflows of foreign direct investment (FDI). **Portfolio investment** reversed to record a large net outflow of RM23.4 billion during the

quarter (2Q 11: +RM48.1 billion), largely on account of the liquidation of both debt and equity securities by foreign investors amid increased volatility in the global financial markets.

**FDI** recorded a lower net inflow of RM5.2 billion (2Q 11: +RM10.2 billion) as higher earnings retained by the multinational companies (MNCs) in Malaysia were partly offset by lower inflows of equity and other capital. During the quarter, the bulk of FDI inflows was mainly undertaken by companies in the manufacturing sector, particularly the E&E and petrochemical sub-sectors. There were also sizeable investments in the oil and gas sector, and finance and insurance sub-sector. Of significance, net FDI in the first nine months of the year was higher than the corresponding period in 2010, broadly indicating continued improvement in FDI flows in Malaysia (Jan-Sept 2011: +RM26.4 billion; Jan-Sept 2010: +RM18.6 billion).

**Direct investment abroad (DIA)** by Malaysian companies increased further, registering a net outflow of RM12.9 billion in the third quarter (2Q 11: -RM7.9 billion). The larger net DIA reflected higher outflows of equity capital and larger earnings retained abroad. These investments were mainly channelled into the finance and insurance sub-sector, and the oil and gas sector, mainly in the Asian countries.

**Other investment** recorded a net inflow of RM8.2 billion (2Q 11: -RM6.3 billion), reflecting mainly the turnaround from a net outflow position to a sizeable net inflow by the private sector, particularly the banking sector. The official sector recorded a small net outflow due to net external loan repayments.

## External debt increased

Malaysia's **total external debt** rose to RM262.6 billion or USD81.6 billion as at end-September 2011 (end-June 2011: RM241.6 billion or USD79.1 billion), equivalent to 32% of GNI.

The **medium- and long-term external debt** was higher at RM157.8 billion (end-June 2011: RM149.2 billion), reflecting the net borrowing position of the private sector and an increase in debt following the strengthening of major currencies against the ringgit during the quarter. In the private sector, the higher debt reflected mainly the intercompany borrowings in the E&E, healthcare and retail sub-sectors. Although the NFPEs recorded a net repayment position, the medium- and long-term debt of the public sector increased following the Federal Government's successful issuance of a dual tranche (5-year and 10-year) Wakala Global Sukuk of USD2 billion.

As at end-September 2011, the **short-term external debt** amounted to RM104.8 billion or

USD32.6 billion (end-June 2011: RM92.3 billion), reflecting mainly higher interbank borrowings. Short-term external debt accounted for 39.9% of total external debt. The latest international reserves position as at 31 October 2011 is 4.1 times the short-term external debt.

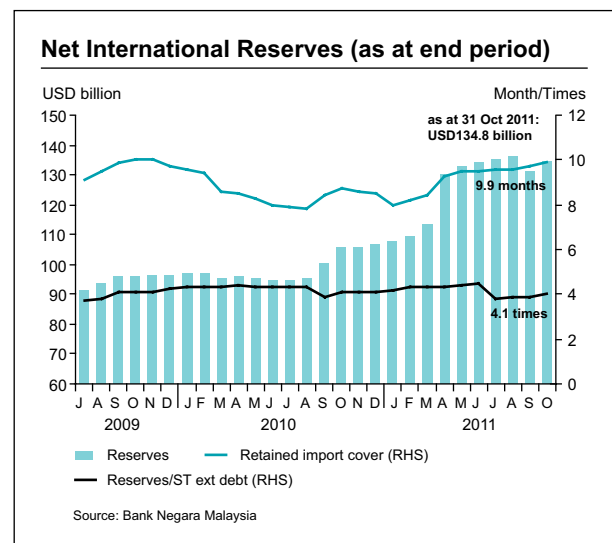
## International reserves remained high

The international reserves of Bank Negara Malaysia amounted to RM417.2 billion (equivalent to USD131 billion) as at 30 September 2011. The reserves level has taken into account the quarterly adjustment for foreign exchange revaluation gain following the strengthening of some major currencies against the ringgit during the quarter. As at 31 October 2011, the reserves position had increased to RM429.1 billion, equivalent to USD134.8 billion. The reserves position is sufficient to finance 9.9 months of retained imports and is 4.1 times the short-term external debt.

External Debt Outstanding			
	2010	2011	
	end-Sept <sup>1</sup>	end-June <sup>2</sup>	end-Sept <sup>2</sup>
RM billion			
Medium- and long-term debt	146.7	149.2	157.8
Public sector	84.1	80.0	83.8
Private sector	62.6	69.3	74.0
Short-term debt <sup>1</sup>	80.7	92.3	104.8
<b>Total external debt</b>	<b>227.4</b>	<b>241.6</b>	<b>262.6</b>
USD billion equivalent	73.0	79.1	81.6
External debt/GNI	30.8	29.5	32.0
Reserves/Short-term external debt	3.9	4.4	4.1 <sup>2</sup>

<sup>1</sup> Excludes currency and deposits held by non-residents with resident banking institutions  
<sup>2</sup> Based on reserves as at 31 October 2011  
<sup>3</sup> Preliminary

Source: Ministry of Finance, Malaysia and Bank Negara Malaysia



## Larger fiscal deficit due to higher Government spending

The Federal Government's total expenditure was higher in the third quarter, resulting in a larger overall fiscal deficit of 6.0% of GDP. The increase in operating expenditure was for the payment of emoluments, subsidies, and grants and transfers to statutory bodies. Higher development expenditure was also recorded during the quarter, due mainly to increased spending in the trade and industry, and public utilities sectors. The deficit was financed from issuances of government securities and the proceeds from Wakala Global Sukuk issued on 6 July 2011. As at end-Sep 2011, total outstanding debt of the Federal Government amounted to RM440.8 billion or 52.0% of GDP.

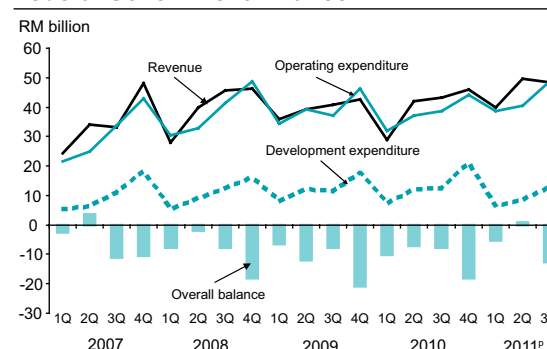
### Federal Government Finance

	2010		2011 <sup>¶</sup>		
	3Q	4Q	1Q	2Q	3Q
<b>RM billion</b>					
Revenue	43.1	45.8	39.8	49.6	48.3
% growth	5.7	7.6	38.4	18.3	12.1
Operating expenditure	38.6	44.1	38.7	40.6	48.8
% growth	3.9	-4.6	21.2	9.5	26.6
<b>Current account</b>	<b>4.6</b>	<b>1.7</b>	<b>1.1</b>	<b>9.1</b>	<b>-0.5</b>
% of GDP	<b>2.4</b>	<b>0.8</b>	<b>0.5</b>	<b>4.3</b>	<b>-0.2</b>
Gross development expenditure	12.5	20.8	6.4	8.3	12.6
% growth	8.0	18.6	-12.0	-31.3	0.3
<b>Overall balance</b>	<b>-7.8</b>	<b>-18.2</b>	<b>-5.2</b>	<b>0.8</b>	<b>-12.8</b>
% of GDP	<b>-4.0</b>	<b>-8.9</b>	<b>-2.6</b>	<b>0.4</b>	<b>-6.0</b>
<b>Memo item:</b>					
Total gross expenditure	51.1	64.9	45.1	48.9	61.4
% growth	4.9	1.8	15.0	-0.5	20.1
Total Federal Government debt (as at end-period)	397.8	407.1	430.2	437.2	440.8
% of GDP	51.9	53.1	50.8	51.6	52.0
Domestic debt	381.4	390.4	414.2	421.0	422.8
% of GDP	49.8	51.0	48.9	49.7	49.9
External debt	16.4	16.7	15.9	16.2	18.1
% of GDP	2.1	2.2	1.9	1.9	2.1

<sup>¶</sup> Preliminary

Source: Ministry of Finance

### Federal Government Finance



<sup>¶</sup> Preliminary

Source: Ministry of Finance

## MONETARY AND FINANCIAL DEVELOPMENTS

### Interest rates remained stable

The Overnight Policy Rate (OPR) was left unchanged at 3.00% in the third quarter of 2011, following a 25 basis points increase in May. At the prevailing level, the OPR remains supportive of economic activity. The stance of monetary policy is consistent with the assessment of heightened uncertainties arising from global developments that have created greater downside risks to growth.

Reflecting the unchanged OPR, the average overnight interbank rate was stable, moving within a range of 2.79% to 3.00% during the period 1 July – 30 September 2011. Interbank rates of other short-term maturities were also stable.

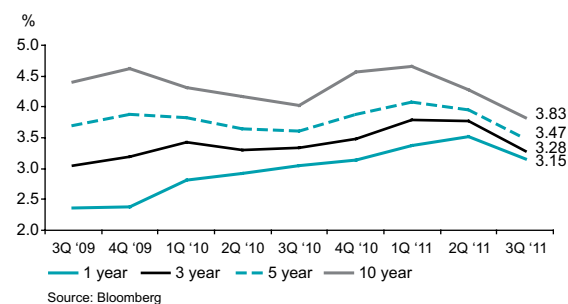
Rates on interest rate swaps and KLIBOR 3-month futures, however, declined during the third quarter. This reflected the moderation of expectations for future increases in the OPR given the uncertainties surrounding global growth and its implications to the Malaysian economy.

Retail deposit rates were stable during the quarter. The average quoted fixed deposit (FD) rates were relatively unchanged. As at end-September, the average quoted FD rates for tenures between 1 and 12 months ranged between 2.95% and 3.22% respectively.

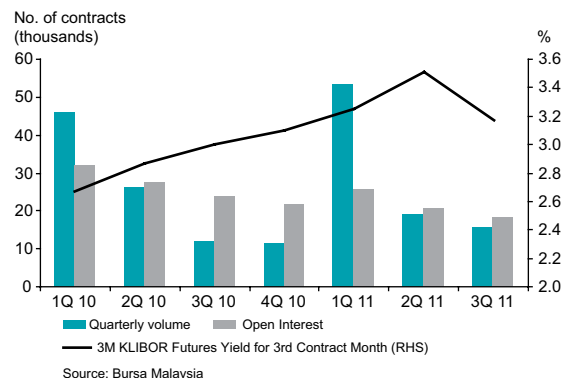
Borrowing costs were also stable between July and September 2011. The average base lending rate (BLR) of commercial banks (CBs) was unchanged at 6.54%. The weighted average

lending rate (ALR) on loans outstanding also remained stable at 5.70% as at end-September 2011 (end-June 11: 5.71%). With retail lending rates still below pre-crisis levels, the cost of financing continues to remain supportive of the economy.

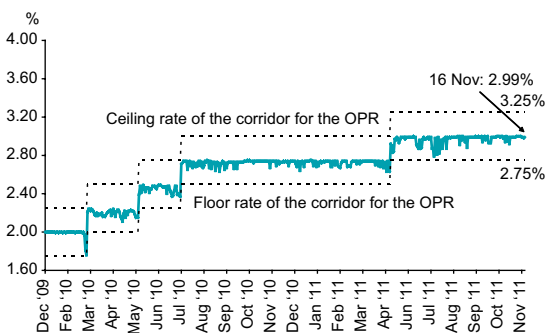
Interest Rate Swap: Rates



3-Month KLIBOR Futures



Daily Weighted Average Overnight Interbank Rate

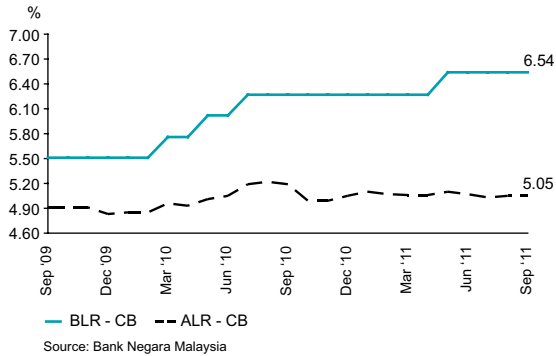


Interest Rates

	2010		2011		
	3Q	4Q	1Q	2Q	3Q
	At end-period (%)				
Overnight Policy Rate (OPR)	2.75	2.75	2.75	3.00	3.00
Interbank rates					
Overnight	2.73	2.72	2.74	2.97	2.99
1-month	2.81	2.83	2.79	3.08	3.09
Base lending rates (BLR)					
Commercial banks	6.27	6.27	6.27	6.54	6.54
Average lending rates (ALR)					
Commercial banks	5.19	5.05	5.06	5.07	5.05
Fixed deposit rates					
Commercial banks					
3-month	2.73	2.74	2.74	2.99	3.00
12-month	2.95	2.97	2.98	3.23	3.22

Source: Bank Negara Malaysia

### Lending Rates of Commercial Banks (At end-period)



### Determinants of Broad Money, M3

	Change during the period				
	2010		2011		
	3Q	4Q	1Q	2Q	3Q
	RM billion				
<b>M3</b>	<b>24.1</b>	<b>30.5</b>	<b>28.0</b>	<b>44.9</b>	<b>28.8</b>
Net claims on Govt	2.7	-3.4	-3.7	-11.4	10.4
Claims on private sector	22.5	29.1	22.8	37.8	20.2
Loans	17.2	28.6	26.5	29.3	22.6
Securities	5.3	0.5	-3.7	8.5	-2.4
Net foreign assets <sup>1</sup>	17.3	17.3	25.1	72.7	3.5
BNM	5.9	17.2	15.7	61.7	10.7
Banking System	11.3	0.1	9.3	11.0	-7.2
Other influences	-18.4	-12.5	-16.1	-54.2	-5.3

<sup>1</sup> Pre-revaluation

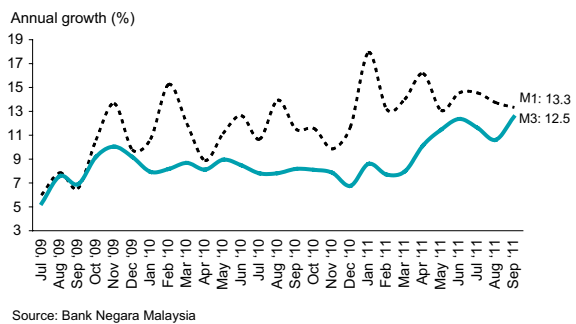
Source: Bank Negara Malaysia

### M3 rose further during the quarter

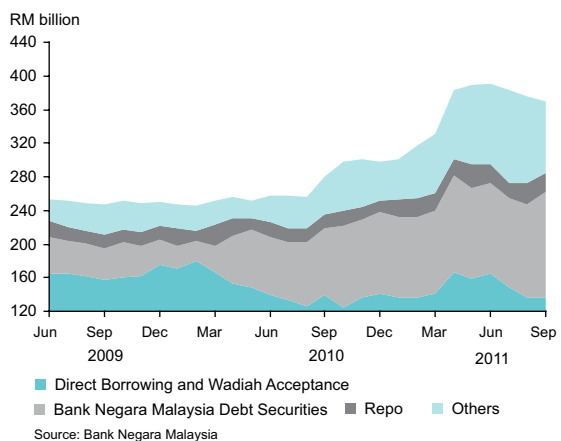
The monetary aggregates continued to grow during the third quarter. M1, or narrow money, increased by RM2.5 billion during the quarter. On an annual basis, M1 expanded by 13.3% as at end-September (end-June 11: 14.5%). M3, or broad money, increased by RM28.8 billion on a quarter-on-quarter basis to register an annual growth rate of 12.5% as at end-September 2011 (end-June 11: 12.4%).

The increase in M3 during the third quarter was underpinned by the continued expansion in credit, reflecting the sustained pace of economic activity. Adding to this expansionary impact on M3 was the increased spending by the Government. Meanwhile, net capital outflows led to a decline in the net foreign assets of the banking institutions, which in turn exerted a contractionary impact on broad money.

### Monetary Aggregates



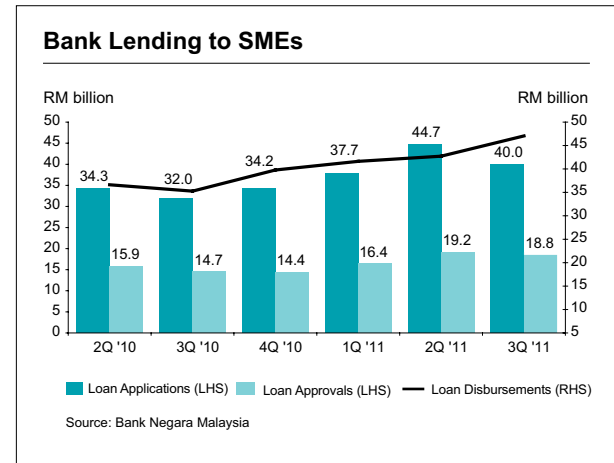
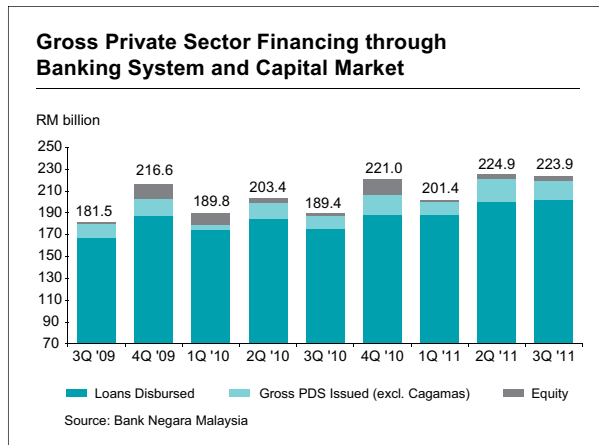
### Outstanding Liquidity Placed with Bank Negara Malaysia (At end-period, RM billion)



## Private sector financing remained resilient

Financing activity in the third quarter remained resilient with total gross financing raised by the private sector through the banking system

and the capital market sustained at RM223.9 billion (2Q 11: RM224.9 billion). On a net basis, banking system loans and PDS outstanding rose by an annual rate of 13.4% as at end-September (end-June 11: 12.8%).



**Financing of the Private Sector through Banking System and Capital Market**

	During the period (RM billion)					Annual growth (%)				
	2010		2011			2010		2011		
	3Q	4Q	1Q	2Q	3Q	3Q	4Q	1Q	2Q	3Q
<b>Gross total financing</b>	<b>189.4</b>	<b>221.0</b>	<b>201.4</b>	<b>224.9</b>	<b>223.9</b>	<b>4.4</b>	<b>2.1</b>	<b>6.1</b>	<b>10.6</b>	<b>18.2</b>
Loans disbursed*	176.1	188.9	188.6	200.8	202.1	5.1	1.0	8.2	8.4	14.8
Gross PDS (excl. Cagamas)	11.2	17.4	11.6	20.3	18.0	-11.3	5.9	161.3	45.9	61.1
Equity	2.1	14.7	1.1	3.8	3.8	73.6	12.0	-89.9	-9.7	79.3
<b>Net total financing (A)+(B)</b>	<b>22.0</b>	<b>36.9</b>	<b>32.8</b>	<b>51.2</b>	<b>31.4</b>	<b>10.6</b>	<b>10.9</b>	<b>12.1</b>	<b>12.8</b>	<b>13.4</b>
Banking system	22.9	29.5	25.9	38.9	25.9	11.0	11.9	12.4	13.1	13.1
Loans outstanding (A)	19.2	29.1	28.8	35.6	24.6	11.8	12.7	13.2	13.5	13.8
Holding of PDS	3.7	0.4	-2.8	3.3	1.3	1.3	1.9	2.1	7.7	3.4
PDS outstanding (B)	2.8	7.8	4.0	15.6	6.8	7.1	5.9	8.7	10.6	11.9
Memorandum item										
Gross PDS (incl. Cagamas)	14.4	18.3	12.2	20.9	19.1	6.5	11.4	161.3	42.0	32.4

\*Banking systems loans include loans sold to Cagamas  
Source: Bank Negara Malaysia

The major loan indicators remained healthy during the third quarter. In the business sector, the bulk of the loans were disbursed to finance working capital requirements of the *manufacturing; wholesale and retail, restaurants and hotels; finance, insurance and business services* and *construction* sectors. Demand for new financing by businesses moderated slightly with applications mainly from the *finance, insurance and business services; manufacturing* and *electricity, gas and water supply* sectors. On an annual basis, business loans outstanding rose at a higher rate of 14.1% as at end-September (end-June 11: 12.1%). The increase in business loans

outstanding was broad-based across all major sectors.

Similarly, financing to the household sector remained high. Loan disbursements to households also increased during the quarter, mainly for the *purchase of residential and non-residential properties* and for *personal use*. Although household demand for financing was sustained, it nevertheless moderated across most purposes during the quarter. Accordingly, household loans outstanding expanded by RM15.2 billion during the quarter to increase at an annual growth rate of 12.5% as at end-September (end-June 11: 12.8%).

### Loan Indicators

	During the period (RM billion)					Annual growth (%)				
	2010		2011			2010		2011		
	3Q	4Q	1Q	2Q	3Q	3Q	4Q	1Q	2Q	3Q
<b>Total</b>										
Loan applications	176.3	173.5	168.5	199.2	182.9	30.1	22.9	26.8	25.5	3.7
Loan approvals	91.2	91.8	87.6	109.7	97.3	25.5	14.1	25.0	21.4	6.7
Loan disbursements	176.1	188.9	188.6	200.8	202.1	5.1	1.0	8.2	8.4	14.8
Loan repayments	165.2	167.9	168.1	173.8	188.2	13.4	3.4	8.8	7.4	13.9
Change in loans outstanding*	19.2	29.1	28.8	35.6	24.6	11.8	12.7	13.2	13.5	13.8
<b>Of which:</b>										
<b>Business enterprises**</b>										
Loan applications	84.7	82.1	79.6	96.6	85.7	40.6	34.1	32.6	34.8	1.1
Loan approvals	43.7	43.4	38.9	55.4	46.2	47.5	17.0	32.8	29.2	5.8
Loan disbursements	116.5	124.6	122.1	134.8	135.9	5.9	-1.2	4.2	7.8	16.6
Loan repayments	113.6	113.0	109.8	116.9	130.2	15.7	0.2	4.3	5.0	14.6
Change in loans outstanding*	2.1	13.4	11.3	11.6	8.7	7.1	9.4	10.9	12.1	14.1
<b>SMEs**</b>										
Loan applications	32.0	34.2	37.7	44.7	40.0	12.2	14.9	35.0	30.6	25.2
Loan approvals	14.7	14.4	16.4	19.2	18.8	18.3	13.5	27.3	20.9	27.7
Loan disbursements	35.3	39.8	41.6	42.7	47.0	-1.3	4.0	17.3	16.6	33.4
Loan repayments	33.9	37.4	37.2	36.6	41.9	3.2	7.3	11.4	13.1	23.6
Change in loans outstanding*	2.8	3.5	3.4	7.5	5.7	4.5	2.4	2.4	14.1	16.1
<b>Large corporations</b>										
Loan applications	52.8	47.9	41.9	51.8	45.7	66.0	52.3	30.5	38.8	-13.4
Loan approvals	29.0	29.1	22.4	36.3	27.5	68.5	18.9	37.1	34.1	-5.3
Loan disbursements	81.3	84.8	80.4	92.0	88.8	9.3	-3.4	-1.5	4.2	9.3
Loan repayments	79.7	75.6	72.6	80.2	88.3	22.0	-3.0	1.1	1.7	10.8
Change in loans outstanding*	-0.7	9.8	7.9	4.1	3.0	8.7	14.2	17.0	10.8	12.8
<b>Households</b>										
Loan applications	91.6	91.4	88.9	102.6	97.2	21.6	14.3	22.0	17.8	6.2
Loan approvals	47.5	48.3	48.8	54.3	51.0	10.3	11.5	19.4	14.3	7.5
Loan disbursements	59.6	64.3	66.6	66.1	66.2	3.5	5.6	16.4	9.6	11.1
Loan repayments	51.6	54.9	58.3	57.0	58.0	8.5	10.6	18.4	12.8	12.4
Change in loans outstanding*	14.8	14.2	14.8	15.4	15.2	13.3	13.4	13.2	12.8	12.5

\* The annual growth is for end-period.  
\*\* Include loans to individual businesses.

Source: Bank Negara Malaysia

### Loans by Sector

	Loans disbursed					Loans out-standing	
	During the period					Share of total	Share of total
	3Q 10	4Q 10	1Q 11	2Q 11	3Q 11	3Q 11	
	(RM billion)					(%)	
<b>Business enterprises</b>	<b>116.5</b>	<b>124.6</b>	<b>122.1</b>	<b>134.8</b>	<b>135.9</b>	<b>67.2</b>	<b>45.0</b>
<i>Large corporations</i>	81.3	84.8	80.4	92.0	88.8	44.0	30.1
<i>SMEs*</i>	35.3	39.8	41.6	42.7	47.0	23.3	14.9
<i>Selected sectors</i>							
Agriculture, hunting, forestry and fishing	4.8	5.3	5.6	5.9	5.3	2.6	2.1
Mining and quarrying	0.9	1.2	1.1	1.1	1.6	0.8	0.4
Manufacturing	36.1	36.8	41.2	42.0	44.9	22.2	9.4
Construction	11.3	11.9	10.3	10.1	10.8	5.3	3.9
Real estate	6.9	7.5	6.4	8.5	8.9	4.4	4.9
Electricity, gas and water supply	0.9	2.6	1.5	1.2	1.6	0.8	1.1
Wholesale, retail, restaurants and hotels	30.6	30.9	30.8	33.8	37.2	18.4	7.3
Transport, storage and communication	4.2	4.3	4.4	4.3	4.6	2.3	2.8
Finance, insurance and business services	13.0	17.8	14.9	18.7	13.0	6.4	7.5
<b>Households</b>	<b>59.6</b>	<b>64.3</b>	<b>66.6</b>	<b>66.1</b>	<b>66.2</b>	<b>32.8</b>	<b>55.0</b>
Purchase of residential properties	13.7	15.1	15.0	15.7	16.8	8.3	25.5
Consumption credit	38.2	39.9	40.1	40.9	40.3	20.0	19.9
Of which:							
<i>Credit cards</i>	21.3	23.4	23.3	24.2	22.7	11.3	3.2
<i>Purchase of passenger cars</i>	9.4	9.1	8.9	8.6	8.8	4.4	11.8
Others	7.7	9.3	11.4	9.5	9.1	4.5	9.6
<b>Total</b>	<b>176.1</b>	<b>188.9</b>	<b>188.6</b>	<b>200.8</b>	<b>202.1</b>	<b>100.0</b>	<b>100.0</b>

\*Include loans to individual businesses.

Source: Bank Negara Malaysia

### Fund raising in the capital market driven by the private sector

Net funds raised in the capital market amounted to RM12.7 billion during the quarter (2Q 11: RM20.8 billion). Of this, 88%, or RM11.1 billion were raised by the private sector, especially through private debt securities. During the quarter, new PDS issuances amounted to RM19.1 billion (2Q 11: RM20.9 billion). Funds were mostly raised for working capital and general corporate purposes. Funds raised from the equity market remained unchanged from the previous quarter at RM3.8 billion. The bulk of funds was raised through initial public offerings (RM3.2 billion), while the rest was raised via rights issues (RM0.7 billion).

In the public sector, gross funds of RM24.8 billion were raised through the issuance of a 7-year Malaysian Government Securities (MGS), as well as the re-opening of a 5-year and 15-year MGS, and a 5-year and 10-year

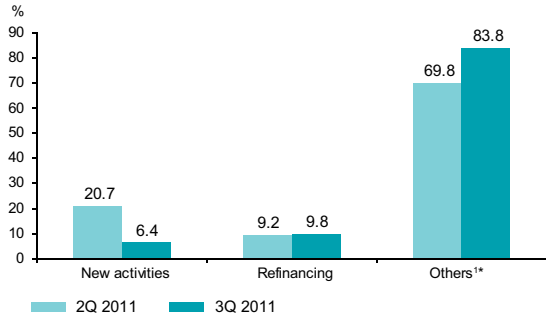
Government Investment Issue (GI). After adjusting for redemptions, net funds raised by the public sector amounted to RM1.6 billion in the third quarter.

### Net Funds Raised in the Capital Market

	2010		2011		
	3Q	4Q	1Q	2Q	3Q
	RM billion				
<b>By Public Sector</b>	<b>8.9</b>	<b>7.1</b>	<b>24.6</b>	<b>3.5</b>	<b>1.6</b>
Government securities, <i>net</i>	9.0	7.1	24.6	5.0	1.6
<i>Malaysian Government Securities</i>	9.9	6.6	15.1	16.7	14.0
<i>Government Investment Issues</i>	6.0	3.0	9.5	10.0	10.8
<i>Less: Redemptions</i>	7.0	2.5	-	21.8	23.2
Khazanah Bonds, <i>net</i>	-	-	-	-	-
Savings Bonds, <i>net</i>	(0.1)	(0.1)	(0.1)	(1.4)	(0.0)
<b>By Private Sector</b>	<b>7.9</b>	<b>23.4</b>	<b>5.1</b>	<b>17.3</b>	<b>11.1</b>
Shares	2.1	14.7	1.1	3.8	3.8
Debt securities, <i>net</i>	5.8	8.7	4.0	13.5	7.3
<i>Private Debt Securities</i>	14.4	18.3	12.2	20.9	19.1
<i>Less: Redemptions</i>	8.6	9.6	8.2	7.4	11.8
<b>Total</b>	<b>16.8</b>	<b>30.5</b>	<b>29.7</b>	<b>20.8</b>	<b>12.7</b>

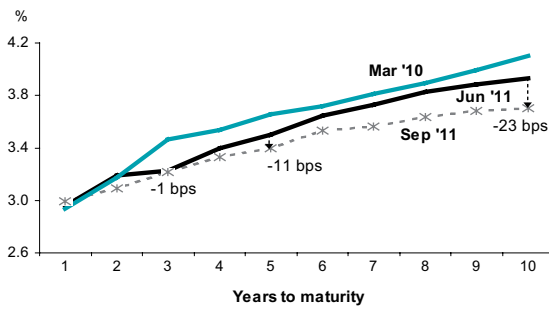
Source: Bank Negara Malaysia and Bursa Malaysia

**Private Debt Securities Issued by Purpose (% of total)**



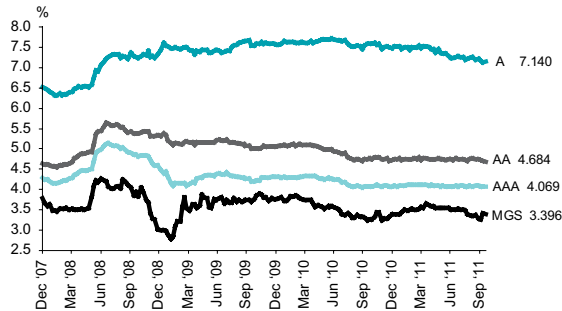
<sup>1</sup> Includes issuance by non-residents and Cagamas  
\* Includes working capital and general business activities  
Source: Bank Negara Malaysia

**Trend in MGS Yields**



Source: Bank Negara Malaysia

**5-year MGS and 5-year Corporate Bond Yields**



Source: Bank Negara Malaysia

**Bond yields declined further in the third quarter**

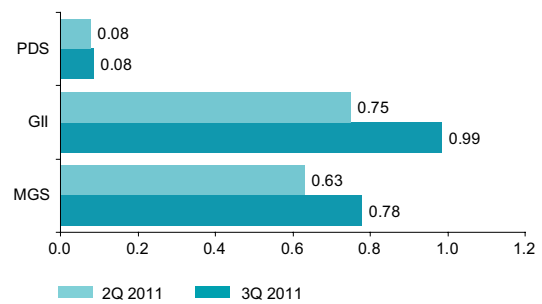
MGS yields declined in July and August 2011, on sustained demand from residents and non-residents due to concerns of a double-dip recession in the advanced economies. There was some upward pressure on yields in September following a slight decline in non-resident holdings of MGS due to the worsening sovereign debt crisis in Europe. Overall, however, yields continued to decline, with the benchmark 3-year, 5-year and 10-year MGS recording a decline of 1, 11 and 23 basis points respectively.

In the PDS market, corporate bond yields also recorded a slight decline, in line with MGS yields. Yields on the 5-year AAA-rated and AA-rated papers recorded a minor decline of 2.2 and 8.7 basis points respectively, while yields on the A-rated papers declined by 12.7 basis points.

**Secondary trading in the bond market increased further during the third quarter**

Total trading in the secondary market increased to RM344 billion during the quarter (2Q 11: RM268 billion). As with the previous quarter, the increase was concentrated mainly in government securities, with both the MGS and GII segments registering higher liquidity ratios of 0.78 and 0.99 respectively. The liquidity ratio for the PDS segment remained stable at 0.08.

**Liquidity Ratio: Turnover / Outstanding**



Source: Bank Negara Malaysia

## KLCI declined in the third quarter

The FBM (FTSE Bursa Malaysia) KLCI declined by 192 points to 1,387.1 (end-June: 1,579.1) representing a decrease of 12.2% in the third quarter (2Q 11: +2.2%). This was in line with the deteriorating outlook for the advanced economies, as well as increased uncertainty and heightened risk aversion among investors. As a result, market capitalisation decreased to RM1.17

trillion at end-September (end-June: RM1.34 trillion). Daily average turnover was relatively unchanged at 1.02 billion units in 3Q 11 (2Q 11: 1.04 billion units).

On 16 November 2011, the KLCI ended higher at 1,476.8 (since end-September: +6.5%), with market capitalisation of RM1.27 trillion (since end-September: +7.9%).

**Performance of Selected Global and Regional Equity Markets in 2011 (% growth QoQ)**



Source: Bloomberg and Bank Negara Malaysia calculations

**Bursa Malaysia: Selected Market Indicators**

	2010		2011		
	As at end				
	Sept	Dec	Mar	June	Sept
Price Indices					
Composite	1,463.5	1,518.9	1,545.1	1,579.1	1,387.1
FBMEMAS <sup>1</sup>	9,811.6	10,375.0	10,612.5	10,842.3	9,397.6
ACE Market <sup>2</sup>	3,877.0	4,347.6	4,333.5	4,198.2	3,598.0
Market capitalisation (RM billion)	1,150.1	1,275.3	1,311.0	1,342.2	1,172.3
No. of companies listed	958	957	954	953	952
	During the quarter				
	3Q	4Q	1Q	2Q	3Q
Average daily turnover					
Volume (million units)	920.9	1,276.5	1,730.1	1,038.8	1,018.9
Value (RM million)	1,481.7	2,002.5	2,233.9	1,638.7	1,887.4

<sup>1</sup> FBMEMAS stands for FTSE Bursa Malaysia EMAS Index

<sup>2</sup> From 3 August 2009, Mesdaq market was replaced with ACE Market

Source: Bursa Malaysia

**Bursa Malaysia: Market Turnover**

	2010				2011					
	3Q		4Q		1Q		2Q		3Q	
	Billion units	RM billion	Billion units	RM billion	Billion units	RM billion	Billion units	RM billion	Billion units	RM billion
Turnover	58.0	93.4	79.1	124.2	102.1	131.8	65.4	103.2	63.2	117.0
Of which:										
Main Board	49.3	91.7	65.7	121.1	84.1	128.4	49.5	100.0	47.4	114.4
Of which										
Consumer Products	4.2	5.0	3.6	5.5	4.0	5.4	4.0	5.0	2.9	4.9
Industrial Products	8.9	9.9	15.4	22.7	18.8	21.2	10.5	15.7	7.9	12.9
Construction	4.5	8.5	4.5	8.7	4.6	9.0	2.8	5.9	3.3	6.1
Trading/Services	15.1	34.5	19.3	40.0	33.5	46.2	17.2	36.5	15.7	42.6
Finance	3.5	18.7	4.6	22.7	4.4	24.6	4.7	20.9	5.7	31.1
Properties	6.7	4.6	11.5	8.8	12.8	9.6	6.3	7.2	6.8	7.8
Plantations	1.0	5.1	2.3	7.9	2.4	8.2	1.2	5.2	1.9	5.6
Infrastructure	1.8	2.2	1.7	2.4	1.1	2.4	0.7	2.1	0.9	2.2
ACE Market <sup>1</sup>	4.1	0.6	5.6	1.3	8.3	1.2	10.9	2.1	9.8	1.5

<sup>1</sup> From 3 August 2009, Mesdaq market was replaced with ACE Market

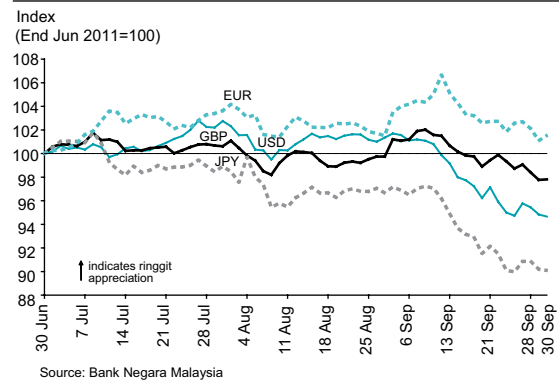
Source: Bursa Malaysia

## Mixed performance of the ringgit against major currencies

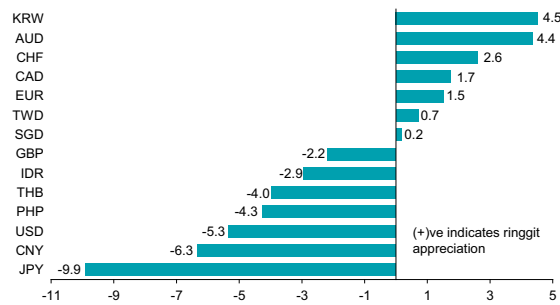
Global foreign exchange markets experienced considerable volatility during the third quarter as investors adjusted their positions in light of the various high profile events affecting the world economy. The ringgit depreciated against the US dollar in the third quarter, in line with other regional currencies. The depreciation, mostly in September 2011, reflected mounting concerns over the European sovereign debt crisis and the sustainability of global economic recovery, which led to higher risk aversion and prompted some investors to unwind holdings of emerging market assets. Overall, the ringgit depreciated by 5.3% against the US dollar. Against other major currencies, the ringgit appreciated against the euro (1.5%), but depreciated against the pound sterling (-2.2%) and the Japanese yen (-9.9%). Ringgit's

depreciation against the Japanese yen was in line with the regional trend. Against regional currencies, the ringgit strengthened against the Korean won (4.5%) and Singapore dollar (0.2%), but depreciated against the Indonesian rupiah (-2.9%), Thai baht (-4.0%), Philippine peso (-4.3%) and Chinese renminbi (-6.3%).

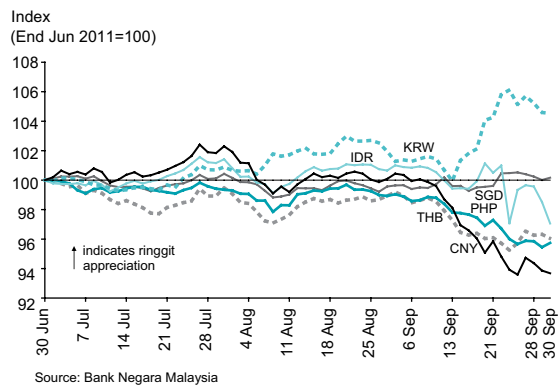
**Ringgit Performance Against Major Currencies**



**Summary of Ringgit Performance Against Selected Currencies** Percent Change (1 July - 30 September 2011)



**Ringgit Performance Against Regional Currencies**



During the period between 1 October and 16 November 2011, the ringgit appreciated against the US dollar (0.8%), Japanese yen (1.4%) and euro (1.3%) but depreciated against the pound sterling (-0.4%). Against regional currencies,

the ringgit strengthened against the Indonesian rupiah (3.3%), Singapore dollar (0.4%) and Chinese renminbi (0.1%) but depreciated against the Philippine peso (-0.1%), Thai baht (-0.3%) and Korean won (-3.0%).

#### Performance of Ringgit Against Selected Currencies

RM per foreign currency	As at end				% change since*		
	21 Jul 05	3Q 10	2Q 11	3Q 11	21 Jul 05	3Q 10	2Q 11
US dollar	3.8000	3.0875	3.0205	3.1910	19.1	-3.2	-5.3
Euro	4.6212	4.1979	4.3820	4.3160	7.1	-2.7	1.5
Pound sterling	6.6270	4.8892	4.8648	4.9738	33.2	-1.7	-2.2
100 Japanese yen	3.3745	3.6943	3.7538	4.1663	-19.0	-11.3	-9.9
Singapore dollar	2.2570	2.3442	2.4577	2.4537	-8.0	-4.5	0.2
100 Thai baht	9.0681	10.151	9.8308	10.236	-11.4	-0.8	-4.0
100 Philippine peso	6.8131	7.0254	6.9649	7.2746	-6.3	-3.4	-4.3
100 Indonesian rupiah	0.0386	0.0346	0.0352	0.0362	6.7	-4.5	-2.9
100 Korean won	0.3665	0.2706	0.2826	0.2703	35.6	0.1	4.5
Chinese renminbi	0.4591	0.4615	0.4673	0.4988	-8.0	-7.5	-6.3

\* (+) indicates appreciation of ringgit against respective currency and (-) indicates depreciation.

Source: Bank Negara Malaysia

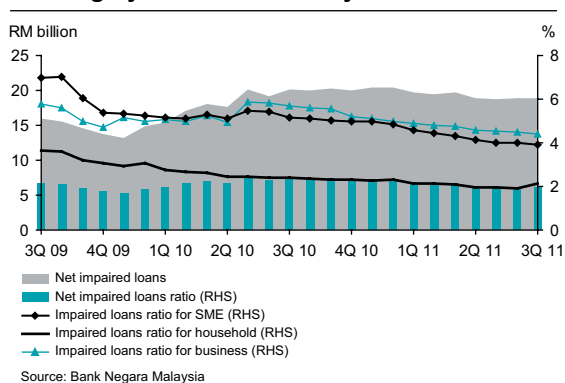
## MANAGING RISKS TO FINANCIAL STABILITY

### Financial stability remained intact

Financial stability remained intact throughout the third quarter amid more challenging external conditions and greater domestic competition. This was underpinned by well-capitalised financial institutions which provided continued support for financial intermediation activities in the domestic economy. Public confidence in the financial system was also preserved. The financial market demonstrated the capacity to absorb the increased volatility arising from concerns on sovereign risk in the US and Euro area.

Overall risks to financial stability remained low, supported by the stable credit risk outlook for the banking system. Loan (includes Islamic financing) quality was preserved with the total impaired loans ratio (net of impairment provisions) remaining stable at 2.0% of net loans (2Q 11: 2.0%) and total loans-in-arrears (for duration of one to less than three months) accounting for 3.8% of gross loans (2Q 11: 3.7%). Outstanding household debts grew by 2.4% during the quarter, while overall household indebtedness to GDP ratio was relatively stable at 77.6% (2Q 11: 77.2%). The bulk of household debts continued to be directed towards asset accumulation through the purchase of residential properties and vehicles. Banks' credit to households through personal financing and credit cards increased at a faster pace but continued to represent less than 10% of overall banking system loans, unchanged from 2010. On aggregate, the debt servicing capacity of households continued to be well-supported by financial assets that amounted to 2.3 times of total household debts (2Q 11: 2.4 times). There are, however, certain segments of households who are facing challenges from the rising cost of living. Recognising this, the Government has introduced a number of measures to ease the financial burden of this group to enable them to manage the situation. These measures should contribute favourably to overall financial and economic stability. Total impaired household loans improved slightly to account for 1.9% of gross household loans (2Q 11: 2.0%), attributed to the sound quality of loans for the purchase of residential properties.

Banking System: Loan Quality



Credit growth in the business sector expanded by 2.4% q-o-q during the quarter amid steady growth in business revenue, in tandem with expansion in real sector activities. The risk of delinquency, as measured by the expected default frequency, for businesses remained very low at 0.8% (2Q 11: 0.6%), supported further by a sound debt servicing capacity of businesses. Repayment-to-disbursement ratio improved further to 96% (2Q 11: 87%) while total impaired loans improved to account for 4.4% of gross business loans (2Q 11: 4.6%). Despite higher uncertainty in global growth and continued elevated commodity prices, the credit risk outlook for businesses remains neutral.

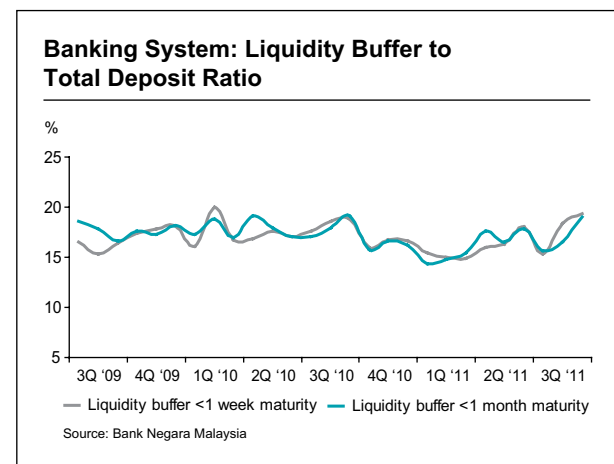
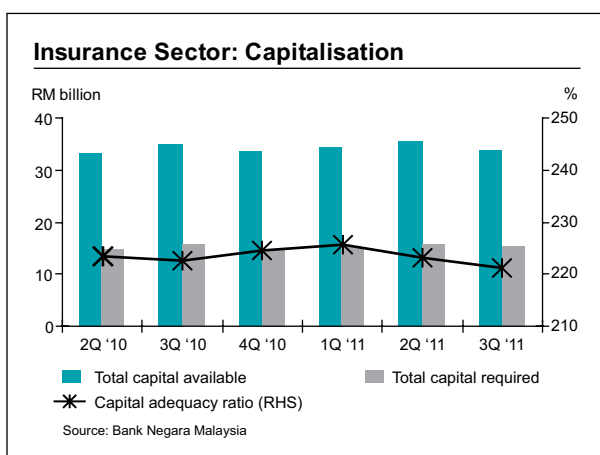
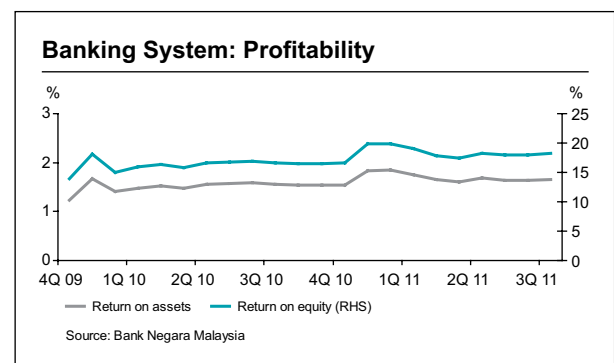
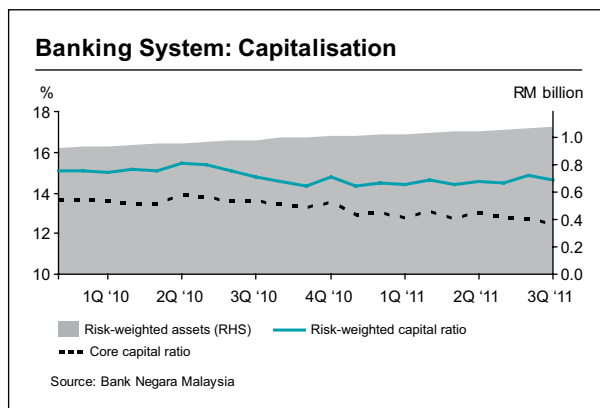
The domestic financial markets experienced higher volatility and some outflows during the quarter, but remained orderly with the capacity to absorb the changes in volume. The persistent sovereign debt concerns in Europe and ratings downgrade of some US financial institutions had a very limited impact on the Malaysian financial system owing to its minimal holdings of foreign currency denominated exposures to counterparts in these jurisdictions. The financial system also remained resilient to indirect spillovers through the trade and economic channels based on results of stress tests under severe economic scenarios. The banking system's exposures to equity risk remained small at 0.7% of capital base (2Q 11: 1.3%), while the insurance and takaful sector's exposures to equity risk was lower at 6.6% of capital base (2Q 11: 7.3%) following measures by insurers and takaful operators to

reduce equity holdings amid more uncertain market conditions. Interest rate risk remained manageable at 4.9% of capital base (2Q 11: 6.0%) for the banking system and 3.4% of capital base (2Q 11: 3.3%) for the insurance and takaful sector.

### The financial sector remained resilient

The banking system continued to maintain a high level of capitalisation with the core capital ratio and risk-weighted capital ratio remaining strong at 12.5% (2Q 11: 13.0%) and 14.6% (2Q 11: 14.6%) respectively. Approximately 85% of total capital comprised high quality Tier-1 capital primarily in the form of paid-up capital and reserves. Capital in excess of the minimum 8.0% regulatory requirement remained high at RM67.8 billion, hence providing the banking system with the strong capacity to absorb any unexpected losses from adverse market and economic conditions. Similarly, capitalisation of the insurance and takaful sector remained strong with a capital adequacy ratio of 221.1% (2Q 11: 223.2%) and excess capital of RM18.6 billion.

The banking system recorded pre-tax profits totalling RM6.7 billion for the quarter (2Q 11: RM6.6 billion) attributable mainly to sustained revenue from financing activities, and lower staff expenses (-22.8% q-o-q) and loan loss provisions (net of recoveries) (-1.4% q-o-q). As a result, returns on assets and equity remained stable at 1.6% (2Q 11: 1.7%) and 18.2% (2Q 11: 18.2%) respectively. The life insurance and family takaful businesses recorded an excess of income over outgo of RM1.3 billion (2Q 11: RM3.8 billion), while the general insurers and general takaful operators registered lower operating profits of RM476.0 million (2Q 11: RM557.2 million) during the quarter. The decline in life insurance and family takaful profitability was due mainly to higher market valuation losses in the equity investment portfolio, in tandem with heightened volatility in the capital market. The lower operating profits recorded by the general business sector was attributed mainly to higher claims incurred in the third quarter with an overall claims ratio at 62.1% (2Q 11: 61.3%). The motor 'act' business segment continued to pose significant losses with a recorded claims ratio of 286.9% (2Q 11: 284.3%).



Overall liquidity in the banking system remained ample and more than sufficient to meet demand for deposit withdrawals and other liquidity obligations. The liquidity buffer remained well above the minimum regulatory requirements, accounting for 19.0% of total deposits for liquidity needs maturing within one month.

#### Insurance and Takaful Sector: Indicators

	2010		2011		
	3Q	4Q	1Q	2Q	3Q
	RM million				
<b>Life insurance &amp; family takaful</b>					
Excess of income over outgo	5,062.8	3,151.3	3,238.5	3,775.3	1,315.0
<b>General insurance &amp; general takaful</b>					
Operating profit	480.9	563.7	562.9	557.2	476.0
Claims ratio (%)	62.2	62.1	61.2	61.3	62.1

Source: Bank Negara Malaysia

## CALENDAR OF EVENTS July – September 2011

### 7 July 2011

At its fourth meeting for 2011, the Bank's Monetary Policy Committee (MPC) decided to maintain the Overnight Policy Rate (OPR) at 3.00%. The MPC's assessment was that the risks to inflation remains. It added that while the outlook for growth remains positive, there are heightened uncertainties arising from global developments that have created higher downside risks to growth. Going forward, the MPC will assess carefully the evolving economic conditions and to the extent that the growth momentum is sustained, further normalisation of monetary conditions will be considered to safeguard price stability. The Bank also announced the increase in the Statutory Reserve Requirement (SRR) Ratio from 3.00% to 4.00% effective 16 July 2011, as a pre-emptive measure to manage the significant build-up of liquidity which may result in financial imbalances and create risks to financial stability. At its subsequent meeting on 8 September, the MPC kept the OPR at the same level, citing that it will continue to assess carefully the evolving developments surrounding inflation and the economy, and adjust monetary conditions accordingly to ensure sustainable growth and price stability.

### 18 – 19 July 2011

The Bank and Bank Indonesia collaborated to host the Joint High Level Conference on Islamic Finance in Jakarta, Indonesia. With the theme "Enhancing Financial Linkages towards Economic Prosperity", the conference was attended by over 400 participants comprising Islamic finance professionals from banking institutions, fund and wealth management, professional service providers as well as higher education institutions from both countries. In her opening remarks, Governor Dr. Zeti expressed her aspiration for the financial intermediaries in the Nusantara region, particularly Malaysia and Indonesia to seize the opportunity of the internationalisation of Islamic finance to further enhance the economic and financial linkages between the two neighbouring countries. The conference also witnessed two Memorandum of Understanding signed, namely, between Association of Islamic Banking Institutions Malaysia (AIBIM) and Asosiasi Bank Syariah Indonesia (ASBISINDO) on cooperation on liquidity management; and between Maybank Islamic Berhad and Bank Syariah Mandiri on product development, trade finance and liquidity management.

### 20 July 2011

The Bank hosted the Official Monetary and Financial Institutions Forum (OMFIF) Roundtable which provided a valuable opportunity for industry players to gain insights on economic developments and challenges in Europe including issues concerning the European sovereign debt crisis and also of Asia's perspectives on these issues. The Roundtable was jointly chaired by Governor Dr. Zeti and Governor Yves Mersch of the Central Bank of Luxembourg and centred on the theme; "International Challenges and Perspectives as Asia diverts Savings to Domestic Economic Development". Those who participated in the Roundtable were captains of industry, namely, Tan Sri Zarinah Anwar, Chairman of Securities Commission; Tan Sri Azman Mokhtar, Managing Director of Khazanah Nasional; Mr. Steven Choy, President and CEO of Cagamas Berhad; and CEOs of Malaysian financial institutions.

## 25 July 2011

The Bank issued commemorative coins set to mark the new Third Series of the Malaysian coins. The new coins series, issued in the denominations of 5 sen, 10 sen, 20 sen and 50 sen, draws inspiration from distinctive features that define the nation's rich culture and heritage. The design motifs were crafted in the form of nature, flora and fauna and traditional handicraft which are found in Malaysia. The coins are smaller and lighter, making them more user-friendly for the public. The yellow and silver coloured coins and the edge designs enable the public and also the visually impaired to identify and distinguish the different denominations. The new series of coins embodies the latest advancements in minting technology which incorporates improved counterfeit resistance security features, as well as enhanced durability against wear and corrosion.

## 1 August 2011

The Bank announced new measures on motor insurance aimed at ensuring consumers are accordingly advised when making a purchase for comprehensive motor insurance cover for their private car. With immediate effect, insurers (and takaful operators) and their agents are required to advise consumers before purchasing and renewing their motor insurance policy on, (i) the present market value of their private car, (ii) the importance of insuring the motor vehicle at the appropriate market value and (iii) the effect of over-insurance and under-insurance when a claim is made. These will contribute towards a more objective determination of the market value of motor vehicles for purposes of purchasing motor insurance and claims settlement. It also complements existing measures on motor insurance that promote fair treatment of consumers.

## 17 August 2011

The Bank announced that the Malaysian economy registered a growth of 4.0% in the second quarter of 2011, led by expansion in private domestic demand. On the supply side, most economic sectors recorded positive growth, with the exception of the mining sector, led by strong growth particularly in the services and agriculture sectors. The headline inflation rate increased to 3.3% in the second quarter driven by supply factors. In a separate announcement, the Bank accorded greater flexibility to new and existing locally-incorporated foreign banks from complying with the distribution ratio requirement for the establishment of their branches. With this flexibility, the banks can better serve their targeted customer segments and niche areas. Under the existing guidelines, locally-incorporated foreign banks can open up to eight additional branches, subject to a specified distribution ratio of 1(market centre): 2(semi-urban): 1(non-urban).

## 25 August 2011

Governor Dr. Zeti was named "The World's Best Central Bankers" over the past year, along with five other central bank heads in five countries, by the New York based Global Finance Magazine. She and the other five central bankers were graded "A" in the magazine's annually published feature entitled Central Banker Report Cards 2011 for successes in areas such as inflation control, economic growth goals, currency stability and interest rate management.

## 6 September 2011

Malaysia International Islamic Financial Centre (MIFC) was awarded the "Best Islamic Finance Centre" for the third consecutive year at the Annual Asset Triple A Islamic Finance Awards 2011. After a build-up that took decades, Malaysia has evolved into the most dynamic Islamic finance hub in the Asia Pacific region. An indication of its success is that countries and jurisdictions across the Pacific rim, in Europe and the Middle East are looking at the Malaysian examples and initiatives for inspiration to jumpstart their own ambitions for Islamic finance.

## 14 September 2011

The Prime Minister of Malaysia, Datuk Seri Najib Tun Razak, officiated the opening of Sasana Kijang - the Bank's centre of excellence in knowledge and learning in central banking and finance. Sasana Kijang is also home to the Islamic Financial Services Board (IFSB) and the South East Asian Central Banks Research and Training (SEACEN) Centre. Designed to be a nexus for thought leadership and collaboration in central banking, Sasana Kijang hosts a learning centre with state-of-the-art training facilities for assisting structured programmes and high level seminars for local and foreign participants and provides opportunities for the exchange of views and experience towards promoting capacity building in central banking to be better positioned in meeting future challenges. In addition, Sasana Kijang also houses the Bank's Knowledge Management Centre and the Bank's Museum and Art Gallery.

## 28 – 29 September 2011

The Bank held a seminar on Islamic Finance in Istanbul, Turkey, in support of the MIFC initiative. Themed "Malaysia and Turkey: The New Silk Route in Islamic Finance - Strategies for Collaboration, Cooperation and Smart Partnerships", the seminar aimed to strengthen relationship between both countries and signifies the growing internationalisation of Islamic or Participative finance. The aim is manifested by the increased presence of Islamic financial institutions in new jurisdictions, international participation in Islamic financial markets and cross border flows of Islamic finance activities. The seminar also provided a platform for the Malaysian and Turkish financial and business community to share and exchange knowledge and industry views on the development of the Islamic financial market.