Chart 1
Actual and Potential GDP

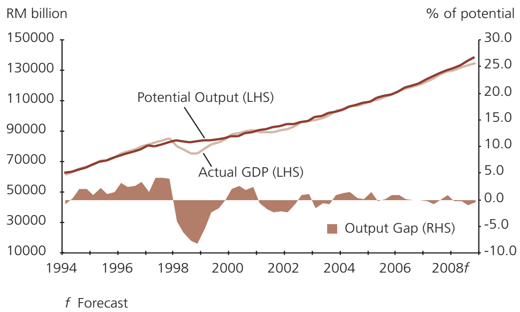
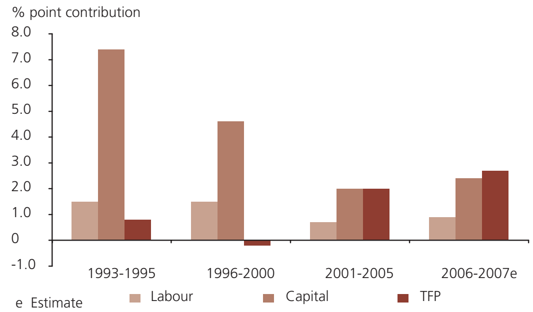


Chart 2
Factor contributions and TFP growth



strategies to increase productivity and competitiveness under the Ninth Malaysia Plan (2006-2010), it is expected that improving productivity levels through greater knowledge intensity of labour force as well as efficiency in the use of capital and technological progress will continue to enhance the contribution of TFP. Having suffered from a period of lacklustre investment climate since the Asian crisis, the pick-up in private investment activities since 2003 has contributed favourably to the growth of potential output. This trend for private investment activity is expected to be sustained in the future, given the strong domestic demand and the implementation of the Ninth Malaysia Plan projects.

Going forward, potential output of the economy is expected to grow above 6% in 2008 supported by the expansion of capital stock and the labour force. However, the output gap is expected to widen marginally following a modest moderation in actual output projected during the year.

Liberalisation of the Foreign Exchange Administration Rules

As a highly open economy, Malaysia has taken advantage of globalisation to sustain its growth momentum and diversify its economic structure. Efforts to strengthen its economic and financial relationships with the rest of the world has contributed to the high level of external trade, sustained level of foreign direct investment and an increase in overseas ventures by Malaysian corporations and financial institutions. Malaysia is committed to progressively liberalise the foreign exchange administration rules to continuously promote the competitiveness of the economy and taking into consideration that economic benefits of the liberalisation outweigh the risks and costs. The sequenced and gradual liberalisation approach that has been adopted has led to positive economic payoffs for the country through the reduction of the cost of doing business, enhancing the regulatory delivery system and facilitating the sound and healthy development of the domestic financial system.

In the early part of 2007, fifteen foreign exchange administration rules were liberalised and the details were reported in the Bank's Annual Report 2006. Subsequently, further liberalisation of the foreign exchange administration rules were announced to strengthen further the overall macroeconomic objective of enhancing Malaysia's competitiveness and promoting economic flexibility. The liberalised rules are as follows:

Objective	Rules liberalised
1. To reduce transaction cost, cost of doing business and enhancing business efficiency	• Effective 28 November 2007, a resident corporation with export earnings is free to pay another resident corporation in foreign currency for settlement of goods and services. • Effective 1 October 2007, (i) The individual reporting threshold for payment and receipts between residents and non-residents is increased to RM200,001 or its equivalent in foreign currency from the previous threshold of RM50,001 per transaction. (ii) The registration requirements on the following were abolished: ➢ Forward foreign exchange contracts entered by residents; ➢ Ringgit-denominated loans extended by a resident to a non-resident for purchase or construction of immovable properties in Malaysia; ➢ Investment in foreign currency assets by residents; ➢ Foreign currency borrowing by resident corporations from: – licensed onshore banks; – non-residents; and – another resident company within the same corporate group using proceeds from an Initial Public Offering on foreign stock exchanges; and ➢ Repayment of permitted foreign currency borrowing (without fixed schedule of repayments) or prepayment. • Effective 1 January 2008, the requirement for submission of the following reports was also abolished: (i) Overseas Account Statement (Statement OA) for accounts maintained by resident corporations with offshore banks; and (ii) Inter-Company Account Statement (Statement IA) for accounts maintained by resident corporations with non-resident corporations.
2. To facilitate the development of Malaysia as an Islamic Financial Centre	• Effective 1 October 2007, unit trust and fund management companies are free to invest the total amount of Islamic funds under their management in foreign currency assets. (Previously the limit for investment in foreign currency assets was up to 50% of the Net Asset Value or of total funds of residents with domestic ringgit borrowing).
3. To facilitate hedging and development of commodities futures market in Malaysia	• Effective 15 January 2008, the following flexibilities were granted to facilitate the transaction of the US dollar denominated crude palm oil futures contracts (USD FUPO) on Bursa Malaysia:

Objective	Rules liberalised
	(i) Exclude investments by residents in USD FUPO on Bursa Malaysia from the investment in foreign currency assets rule, if the contracts are settled in ringgit; and (ii) Allow commodity futures brokers licensed by Securities Commission to act as agents to licensed onshore banks to quote exchange rates to facilitate settlement of USD FUPO with Bursa Malaysia.
4. To support the development of new areas of economic growth	• Effective 24 September 2007, resident corporations approved under the Iskandar Development Region framework and biotechnology companies approved under the National Biotechnology Policy, are free to undertake the following: (i) To pay and receive payments in foreign currency, other than the currency of Israel, with residents; (ii) To borrow any amount of foreign currency from licensed onshore banks and non-residents; (iii) To invest any amount in foreign currency assets onshore and offshore; and (iv) To retain export proceeds offshore.
5. To enhance risk management flexibility for investment in ringgit assets by non-residents	• Effective 1 October 2007, the requirement for a non-resident to reinvest within 7 working days, the proceeds arising from the sale of ringgit assets prior to the maturity of the forward foreign exchange contract was abolished.

The remaining foreign exchange administration rules currently applicable to non-residents and residents are mainly for prudential purposes and will be progressively reviewed to continuously promote the competitiveness of the Malaysian economy. The rules can be broadly categorised into the following 6 main areas:

The explanatory notes are in the Annex.