Euler Hermes Economic Research

Country Report

Malaysia

External risks rise but solid buffers exist

General Information

GDP	USD313.2 bn (World ranking 35, World Bank 2013)
Population	29.7 mn (World ranking 44, World Bank 2013)
Form of state	Constitutional Monarchy
Head of government	Mohamed NAJIB bin Abdul Najib Razak (UMNO Party)
Next elections	2018, legislative

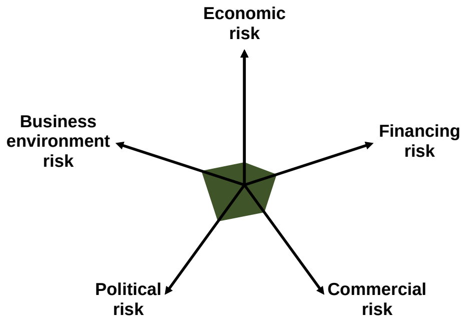
Strengths

- Comfortable foreign exchange reserves
- Member of ASEAN
- Low inflation
- Large current account surpluses since 1998
- Low external debt burden
- Generally strong business environment
- Resilient banking sector

Weaknesses

- Ethnic-religious tensions
- Export dependency causes cyclical risk
- Slightly elevated fiscal deficits in recent years (currently not a problem but should be addressed in the medium term)
- Government intervention and regulation of the economy remain an issue

Country Rating A1



Source: Euler Hermes

Trade Structure

By destination / origin

Exports		Rank		Imports
Singapore	14%	1	17%	China
China	12%	2	13%	Singapore
Japan	11%	3	8%	Japan
USA	8%	4	8%	USA
Thailand	5%	5	6%	Thailand

By Product

Exports		Rank		Imports
Electronic Equipments	28%	1	26%	Electronic Equipments
Mineral Fuels	22%	2	17%	Mineral Fuels
Machinery	10%	3	11%	Machinery
Animal and vegetable fats	7%	4	3%	Plastics
Plastics	3%	5	3%	Vehicles

Source: ITC, (2014)

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GDP growth to lose steam in 2015

GDP growth recorded a strong performance in 2014 (+6%) with a good mix of stable inflation and sound labor market. Domestic demand remains a key engine of growth with private consumption increasing by +7%. External trade has been supportive in H1 but the trend has reversed with decreasing oil prices. We expect GDP growth to slow down to +5% in 2015, with lower oil prices (-35% below 2014 level) shaving -0.5 pp from our baseline scenario. The slowdown will mainly be concentrated in H1 as the negative impact of oil prices will be exacerbated by the implementation of the Goods and Services Tax (April 2015). The economy is projected to gather pace from H2 with non-resource based exports (53% of total exports) picking up supported by rise in demand from the US. On the domestic front, investment will be a key driver for growth sustained by investment in the non-oil sector and ongoing infrastructure program. Private consumption will increase but at a moderate pace, reflecting the high household debt burden.

Economic forecasts

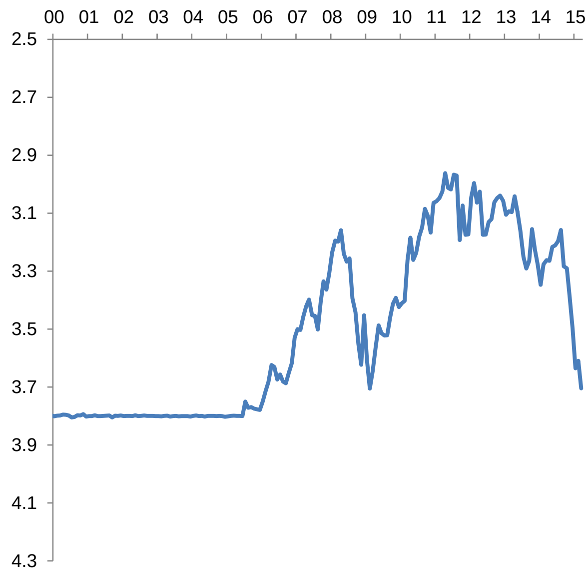
	2013	2014e	2015
GDP growth (% change)	4.7	6.0	5.0
Inflation (%, year average)	2.1	3.3	2.8
Fiscal balance (% of GDP)**	-3.9	-3.5	-3.2
Public debt (% of GDP)	54.7	53.6	53.5
Current account (% of GDP)	4.0	4.6	3.0
External debt (% of GNI)	67.9	60.3	64.0

Sources: National sources, IIF, Euler Hermes

Policy mix to be cautious

Monetary policy is based on the assessment of the risk to growth and inflation prospects. The Central Bank has a good reputation, with a positive track record anchoring inflation expectations and enhancing growth. After three years of status quo, it raised its policy rate in July 2014 to 3.25% (from 3.00%) anticipating further inflationary pressures (above 4%) with the implementation of the Goods and Services Tax. Due to the fall in energy prices, we expect inflation to edge down to 2.8% in 2015 (from 3.2% in 2014). Although this gives greater room for maneuver to the Central Bank to ease monetary policy, we expect a neutral stance in the short run in order to maintain financial stability. Fiscal consolidation will continue but at a slower pace. The 2015 budget has been revised down (-3.2% of GDP from -3%) taking into account less revenues due to lower oil prices.

MYR/USD



Sources: National sources, IHS, Euler Hermes

Currency risk is on the rise but solid buffers should mitigate external risk

The MYR deteriorated sharply during the past seven months (-15%) due to the depressed outlook in oil prices. Although this exerts downward pressures especially on importing companies, the risk on the macro side is moderate at this stage. The current account surplus remains comfortable (+4.6% in 2014) even though it is on a downward trend (+3.0% in 2015) due to lower oil exports revenues. Foreign exchange reserves have decreased but remain comfortable (close to 6 months of import cover).

Contact Euler Hermes Economic Research Team
research@eulerhermes.com

Last review: 2015-03-19
Country Risk Analyst:
Mahamoud Islam
mahamoud.islam@eulerhermes.com