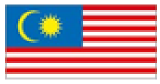
Euler Hermes Economic Research

Country Risk Analysis

Malaysia

Sound macroeconomic fundamentals



General Information

GDP	USD3,030.5 billion (World ranking 34, World Bank 2012)
Population	29.2 million (World ranking 44, World Bank 2012)
Form of state	Federal Constitutional Monarchy (parliamentary)
Head of government	NAJIB Razak (UMNO party)
Next elections	2018, legislative

Strengths

- Generally good international relations (member of ASEAN)
- Low inflation
- Large current account surpluses since 1998
- Ample foreign exchange reserves
- Low external debt burden
- Generally strong business environment
- Resilient banking sector

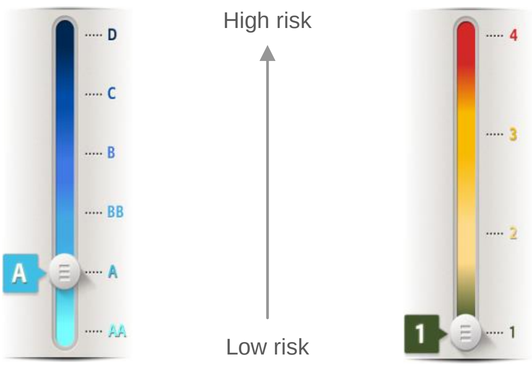
Weaknesses

- 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 in and regulation of the economy remains an issue

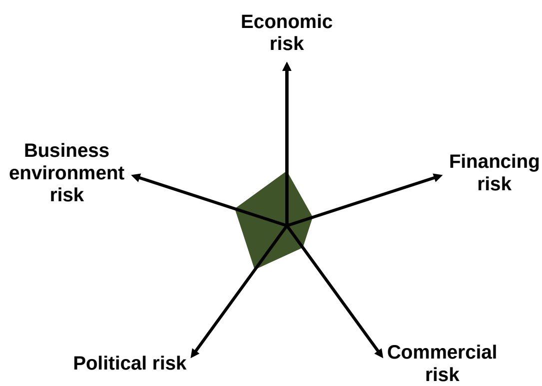
Country Rating A1

Country Grade

Country Risk Level



Risk Dimensions



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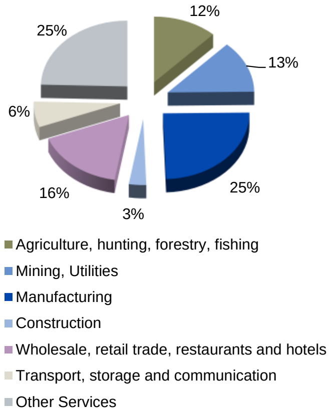
Economic Structure

GDP breakdown (% of total, 2011)



Sources: UnctadStat, Euler Hermes

Trade structure (% of total, 2011)

Exports		Rank		Imports
China	13%	1	25%	Singapore
Singapore	13%	2	14%	China
Japan	12%	3	9%	Japan
United States	8%	4	7%	United States
Thailand	5%	5	6%	Thailand

Exports		Rank		Imports
Electrical machinery, apparatus and appliances, n.e.s.	20%	1	22%	Electrical machinery, apparatus and appliances, n.e.s.
Petroleum, petroleum products and related materials	10%	2	10%	Petroleum, petroleum products and related materials
Fixed vegetable oils and fats, crude, refined or fractionated	9%	3	5%	Office machines and automatic data processing machines
Gas, natural and manufactured	8%	4	4%	Non-ferrous metals
Office machines and automatic data processing machines	8%	5	4%	Telecommunication and sound recording apparatus

Economic Forecasts

	2009	2010	2011	2012	2013f	2014f
GDP growth (% change)	-1.5	7.4	5.1	5.6	4.4	4.6
Inflation (%, end-year)	1.0	2.1	3.0	1.2	2.2	2.4
Fiscal balance (% of GDP)	-6.2	-4.5	-3.8	-4.3	-4.0	-3.7
Public debt (% of GDP)	52.8	53.7	54.5	55.5	56.0	55.7
Current account (% of GDP)	15.7	11.0	11.1	6.3	4.0	3.8
External debt (% of GDP)	34.5	34.4	32.7	33.1	33.0	32.0

Sources: IHS Global Insight, national sources, Euler Hermes

Economic Growth

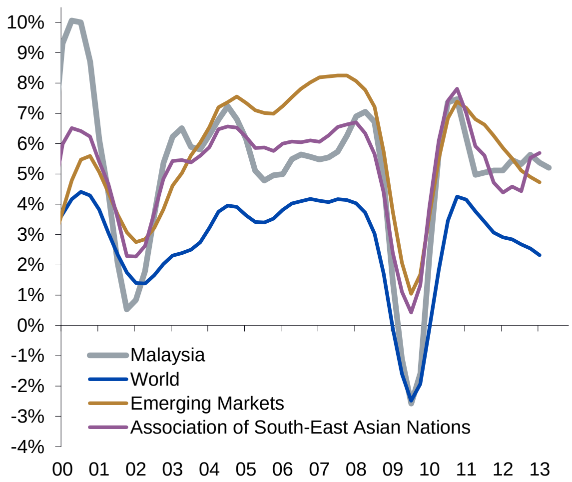
Export dependency causes cyclical growth

With an export-to-GDP ratio of about 95%, the economy is very open and re-exporting plays an important role. This creates vulnerabilities to external shocks, but the diversified export structure, combined with overall sound economic fundamentals and appropriate policies, provide some cushion. Indeed, the economy shrank by -1.5% in 2009 in the wake of the global economic crisis, but it recovered early and strongly.

GDP growth will remain solid in 2013-2014

Real GDP growth accelerated to +5.6% in 2012 from +5.1% in 2011. The robust performance in 2012 was entirely led by domestic demand, especially by surging fixed investment (+19.9%). Private consumption grew by +7.7% and government consumption by +5%. Net trade made a negative contribution to 2012 growth as annual exports were nearly flat (+0.1%) while imports maintained modest growth of +4.5%. GDP growth moderated to +4.2% y/y in H1 2013 as the expansion of investment slowed to a still solid +9.3% y/y. Private and government consumption remained robust in H1, expanding by +7.4% and +5.8% y/y, respectively. The contribution of net trade to H1 growth was again negative as exports contracted by -2.9% y/y while imports increased by +0.8% y/y. External trade activity weakened especially in Q2 2013 as exports declined by -5.2% y/y (-0.6% in Q1) and imports by -2% y/y (+3.6% in Q1). EH expects domestic demand to retain momentum and some fiscal stimulus amid ongoing global weakness in 2013, resulting in full year GDP growth of about +4.4%, followed by +4.6% in 2014.

GDP growth (% y/y, 4 qtrs cumulated)



Sources: IHS Global Insight, national sources, Euler Hermes

Economic Policies

Sound monetary policy

According to the central bank, monetary policy is based on the assessment of the risk to growth and inflation prospects. The key policy interest rate has been kept unchanged at 3% since May 2011.

Inflation is unproblematic

Consumer price inflation has been under control for many years. Only a 41% cut of petrol subsidies in June 2008 pushed it temporarily to 8.5% y/y in July-August of that year. More recently, headline inflation has gradually picked up from a 33-month low of 1.2% y/y in December 2012 to 2% in July 2013. We expect average inflation to remain below 3% until the end of 2014.

Banking sector has been resilient

The banking sector has shown resilience in recent years and has remained well-capitalised, profitable and liquid. Non-performing loans have declined to 2% of total loans in Q1 2013. Credit growth has accelerated since 2010 and household debt rose to 74% of GDP in 2011, posing some risk to financial stability, and should be monitored. But risks are currently contained by high bank capital buffers, ample international reserves, and sound monetary and financial policies, and the central bank has taken action to stabilise household credit growth, according to a recent IMF report.

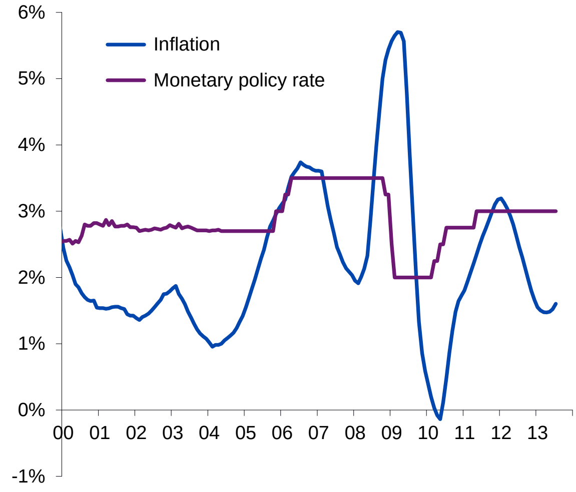
Recent exchange rate volatility appears unproblematic

The exchange rate regime is a managed float of the MYR against a trade-weighted basket of currencies. Since an all-time high of 2.95 at end-July 2011, the MYR/USD exchange rate has shown some volatility in response to external events and, overall, depreciated by around 10%, to 3.25, in the two years to July 2013. From early May to mid-August 2013, the exchange rate has fallen by 8% or so—in line with many other emerging market currencies—as a result of hints by the US Fed that the latest round of Quantitative Easing will be slowing down. This shows that the exchange rate is not immune to external events such as net capital outflows from emerging markets if investors are reducing their exposure to these countries. However, the central bank has currently sufficient foreign exchange reserves to avert a more worrisome weakening of the currency.

Public finances do not pose any immediate threat

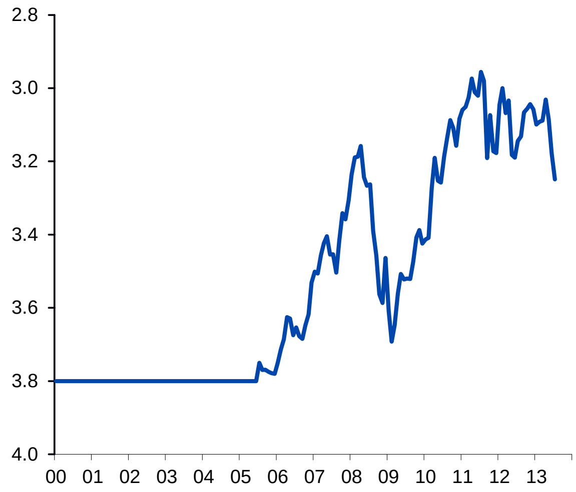
The government has proceeded slowly with fiscal adjustment after the 2008-2009 global economic crisis in view of the political cycle and concerns about sustaining growth. As a result, the general government budget deficit narrowed only slightly to 3.8% of GDP in 2011 and picked up again to 4.3% in 2012. We expect the deficit to remain at around 4% of GDP in 2013-2014. However, this should not raise too much concern as total public debt, at around 56% of GDP, is 97% domestic and manageable.

Inflation rate (12-month moving average, %) and policy interest rate (%)



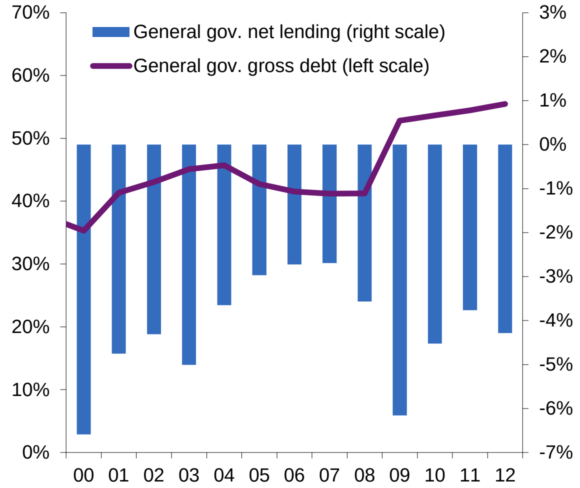
Sources: IHS Global Insight, national sources, Euler Hermes

Exchange rate (MYR/USD)



Sources: IHS Global Insight, national sources, Euler Hermes

Fiscal balance and public debt (% of GDP)



Sources: IHS Global Insight, national sources, Euler Hermes

External Sector

Current account surplus is narrowing

The current account balance has recorded large annual surpluses since 1998. In 2012, the surplus narrowed to 6.3% of GDP from 11.1% in 2011. Owing to the weak export performance amid ongoing global sluggishness, we expect the surplus to decline further to a still favourable 4% of GDP or so in 2013-2014.

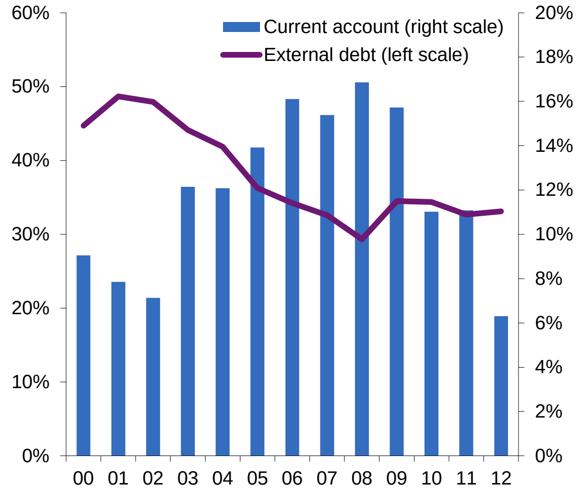
External debt burden is manageable

Gross external debt accounted for just 33% of GDP or 38% of export earnings at end-2012. We expect these ratios to remain that favourable in the next two years. The annual external debt-service in 2013 and 2014 will amount to around 5.5% of export earnings.

Ample foreign exchange reserves

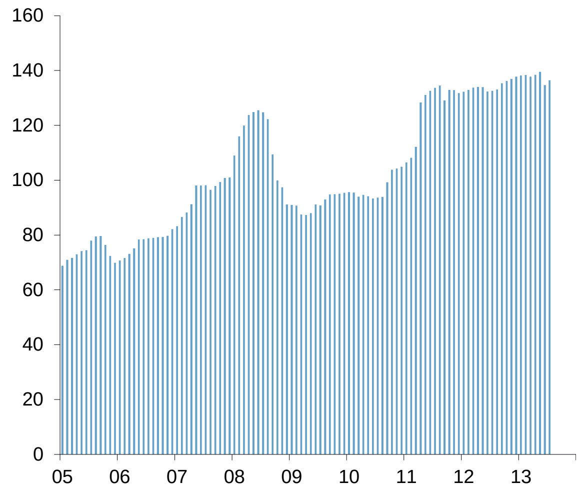
Foreign exchange reserves have increased gradually over the past two years and stood at USD136.4bn in July 2013. Current reserves are sufficient to cover around 6.5 months of imports or, in other terms, 220% of all external debt payments falling due in the next 12 months.

Current account and external debt (% of GDP)



Sources: IHS Global Insight, national sources, Euler Hermes

Foreign exchange reserves (USD billion)



Sources: IHS Global Insight, national sources, Euler Hermes

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