Chapter 2

Macroeconomic Performance and Prospects

2 MACROECONOMIC PERFORMANCE AND PROSPECTS

I. INTRODUCTION

2.01 The performance of the Malaysian economy during the Sixth Plan period was impressive. The strong economic fundamentals resulting from sound macroeconomic policies and the increasing competitiveness of the economy contributed to the achievement of high growth with relatively stable prices. The economy was propelled by the strong upsurge in private investment which was supported by large inflows of foreign investment, high domestic savings and privatization. The export sector performed remarkably well, despite the sluggish growth of the major industrial economies during the first half of the Plan period.

2.02 With the rapid growth, the economy also faced supply constraints such as infrastructure inadequacies and labour shortages while the current account deficit of the balance of payments persisted throughout the period. In addition, large short-term capital inflows affected the management of monetary policy in the middle of the Plan period. However, pragmatic policy measures were instituted and conscientious efforts were undertaken to overcome these developments.

2.03 Recognizing that there are limitations to sustaining high levels of investment to support high growth, the Seventh Plan will shift the focus from an investment-driven strategy towards a productivity-driven strategy, by enhancing the contribution of total factor productivity (TFP)[1] to growth from 28.7 per cent of Gross Domestic Product (GDP) in the Sixth Plan to 41.3 per cent in the Seventh Plan. Among others, emphasis will be given to increasing the rate of innovation, skill development and managerial efficiency. Since the private sector is the main engine of growth, it is expected that strategies for productivity increases will be a crucial ingredient in their operations. This shift in strategy will further strengthen the fundamentals of the Malaysian economy and contribute to its continued high growth with price stability.

[1] Total factor productivity refers to the additional output generated as a result of the introduction of new technology or upgrading of technology, innovation, superior management techniques, gains from specialization, improvements in efficiency, knowhow, worker's education, skills and experience and advancement in information technology.

II. REVIEW OF MACROECONOMIC PERFORMANCE

2.04 During the Sixth Plan period, the economy recorded an average growth of 8.7 per cent per annum which surpassed the revised growth target of 8.1 per cent in the Mid-Term Review as well as the original Sixth Plan target of 7.5 per cent. This rapid growth was attained with macroeconomic stability. The strong growth emanated mainly from higher domestic demand which grew at a rate of 11.3 per cent annually, while the recovery of the world economy in the latter part of the Plan further supported the performance of the Malaysian economy. Among others, this rapid growth resulted in an increased per capita income from RM6,099 in 1990 to RM9,786 in 1995 and enabled high inflows of foreign investment. While the private sector played the leading role, the public sector continued to provide active support to the development process. With the buoyant economic performance, the financial position of the Government improved as a result of better revenue collection and prudent expenditure. This enabled the Federal Government to record a surplus in its overall account since 1993.

Macroeconomic Progress

2.05 During the Sixth Plan, pragmatic macroeconomic management enabled the strengthening of Malaysia's productive capacity and international competitiveness. Malaysia's success in achieving consistently high economic growth with price stability was a result of the implementation of sound macroeconomic policies and strategies. Further liberalization of procedures and rules, supported by a stable political climate, provided a conducive environment for increased private investment. Malaysia was successful in financing these investments through domestic savings and high inflows of foreign direct investments (FDI). Efforts in industrial development resulted in better quality products, increased efficiency and improved competitiveness of Malaysia's exports. Resources were allocated for the development of science and technology (S&T), research and development (R&D) and human resources to improve productivity. The financial market was strengthened and this facilitated the mobilization of domestic savings, while the capital market was developed and nurtured to meet the increasing and varied needs of an industrializing economy.

2.06 The real output of the economy expanded during the period, contributed mainly by investments in physical infrastructure, R&D, education and skill training, together with large inflows of FDI. These factors also led to the doubling of the contribution of TFP from 1.2 per cent or 17.9 per cent of GDP during the 1971-90 period to 2.5 per cent or 28.7 per cent of GDP growth during the Sixth Plan period, as shown in *Table 2-1*. The contribution from capital and labour continued to be significant.

2.07 During the period, *private investment* rose by 16.6 per cent per annum in response to the better economic performance, lower corporate tax rate and the increase in reinvestment allowance. Part of this investment was contributed by FDI inflows. In 1993, the Government launched the Domestic Investment Initiative (DII) to further enhance domestic investment. The bulk of private investment was channelled particularly into the manufacturing, and the oil and gas sectors. Similarly, investment in the services sector was also large, due mainly to the increased outlays on privatized projects in the utilities, transport and communications subsectors, as a result of the accelerated implementation of the privatization programme.

2.08 The prudent budgetary policies of the Federal Government resulted in the achievement of an overall surplus in the Federal budget since 1993. The strong revenue performance also contributed to this improved position. *Public investment,* which comprised of investment by the Federal, State and Local Governments, Statutory Authorities and the Non-Financial Public Enterprises

TABLE 2-1

CONTRIBUTION OF FACTORS OF PRODUCTION
(%)

	1971-90	*6MP*	*7MP*
GDP Growth	***6.7***	***8.7***	***8.0***
Labour	*2.3*	*2.5*	*1.7*
Capital	*3.2*	*3.7*	*3.0*
TFP[1]	*1.2*	*2.5*	*3.3*

Note: [1] TFP is estimated by using the Cobb-Douglas Production Function by subtracting from output growth the portion of growth which is accounted for by increases in labour and capital.

(NFPEs)[2], grew at an average rate of 14.7 per cent per annum, exceeding the Plan target of 11.1 per cent, in response to the increased demand for social and physical infrastructure brought about by the acceleration of private investment. The bulk of public investment was, however, incurred by the NFPEs to finance their expansion and modernization programmes. Although overall public investment was higher than targeted, the public account position improved significantly under the Sixth Plan. The public sector account registered a surplus of RM3.5 billion or 0.4 per cent of Gross National Product (GNP). This performance was due to the improvement in the Federal account and the stronger position of many NFPEs following restructuring and adjustment efforts. Despite the high level of public sector investment, it was lower than private investment in terms of growth as well as contribution to GNP. This was consistent with the private sector-led growth strategy of the Sixth Plan.

2.09 *Private consumption* grew by 7.6 per cent per annum during the Plan period, higher than the target of 6.0 per cent. This higher rate of growth of consumption reflected the rising disposable income due to higher corporate profits and higher personal disposable income as a result of the good economic performance. However, *public consumption* grew slightly higher than private consumption at an average rate of 9.5 per cent, due mainly to the increasing expenditure to improve the quality and efficiency of public services as well as to modernize defence facilities.

2.10 Efforts to mobilize *national savings* were successful as evident by the high rate achieved, at 34.2 per cent of GNP, at the end of the period, compared with 30.5 per cent in 1990. The increase in national savings was attributable to the lower growth in consumption relative to the expansion in national income, increase in the contribution rate of the Employees Provident Fund (EPF), expansion in unit trust schemes, introduction of new savings instruments in the financial system, introduction of new private debt instruments in the capital market as well as the mobilization of deposits by the Islamic financial system. The good revenue performance and the strong commitment to fiscal prudence through better control of expenditure by the Government increased public sector savings, thereby contributing further to the increases in domestic savings.

[2] The Non-Financial Public Enterprises (NFPEs) are public sector agencies which undertake the selling of industrial and commercial goods and services in the economy. As defined by the International Monetary Fund (IMF), "Non-Financial Public Enterprises are government-owned and/or government controlled units which sell industrial or commercial goods and services to the public on a large scale or are corporate". In the case of companies incorporated under the Companies Act, 1965, Government control would normally refer to a Government share holding of more than 50 per cent of total equity.

2.11 Although the economy continued to achieve strong growth, *price stability* was maintained. The inflation rate, as measured by the Consumer Price Index (CPI), was contained at an average rate of 4.0 per cent, through a comprehensive anti-inflationary package comprising monetary, fiscal and administrative measures. A tight monetary policy was introduced to dampen aggregate demand by managing excess liquidity in the market. The Government undertook prudent fiscal policy by restraining operating expenditure, while development expenditure focused on projects that would alleviate infrastructure and supply constraints. In addition, import duties on more than 3,700 items were reduced or abolished so as to lower the prices of goods as well as the cost of doing business. The Government also launched a comprehensive anti-inflation campaign to further intensify efforts to educate the public on the causes and impact of inflation and on the active role of consumers in combating unjustified price increases. The implementation of administrative measures aimed at improving the dissemination of price information and encouraging fair and ethical business practices was intensified. In order to improve the measurement of price movements, the CPI was rebased from 1990 to 1994, based on the Household Expenditure Survey, 1993/94, to keep the CPI up-to-date with changes in consumption patterns as reflected in the basket of goods and services used in the construction of the CPI composite index. At the producer's level, the Producer Price Index (PPI), which measures the price of inputs for the domestic economy, registered an average growth of 3.4 per cent due mainly to the price increases of inputs for local production which averaged 4.5 per cent compared to imports averaging 0.4 per cent. The GDP deflator, which measures prices of consumption and investment goods, and export and import items, was stable, averaging 4.0 per cent during the period.

2.12 A significant development in the middle of the Plan period was the massive inflows of short-term capital in the form of portfolio investments, which was induced by high interest rates, expectation of exchange rate appreciation and opportunities in the stock market. In contrast to long-term capital inflows which contribute towards the expansion of the productive capacity of the economy, short-term capital inflows which can be subjected to sudden reversals, pose a threat to domestic financial and economic stability. The Government, therefore, implemented a series of administrative measures in 1994 to deal directly with these speculative inflows. These measures included taxing all funds sourced from abroad, subjecting banking institutions to a ceiling on their non-trade-related external liabilities and prohibiting the sale of short-term monetary papers to non-residents. When stability was achieved in the domestic financial market, these measures were lifted so as not to create market distortions and misallocation of financial resources.

2.13 Malaysia's total trade expanded by 19.1 per cent per annum during the period, as shown in *Table 2-2*. The Association of South-East Asian Nations (ASEAN) was Malaysia's largest trading partner constituting 22.2 per cent of total trade in 1995, with Singapore being the largest market. This was followed by Japan, the United States of America (US) and the European Union (EU). The ASEAN countries, Japan, the US and the EU continued to be the nation's major trading partners accounting for 75.5 per cent of Malaysia's total exports in 1995 as compared to 76.3 per cent in 1990. This declining trend reflected the increased trade with South countries as a result of efforts by the Government to diversify its markets. Malaysia's total trade with the South countries, excluding Singapore, expanded by 20.8 per cent during the Plan period, with its share increasing from 12.9 per cent in 1990 to 13.9 per cent in 1995.

2.14 Strong economic growth in the ASEAN economies and increasing intra-ASEAN investment contributed to the rapid expansion of intra-ASEAN trade. During the Plan period, intra-ASEAN trade grew by 21.7 per cent, with Malaysia and Singapore contributing 47.1 per cent and 26.4 per cent of the growth, respectively. Malaysia's exports to ASEAN countries increased by 18.3 per cent, while imports grew by 21 per cent.

2.15 *Gross exports* grew at an average rate of 18.4 per cent per annum, higher than the Plan target of 13.2 per cent, as shown in *Table 2-3*. This was contributed by the high growth of 25.8 per cent per annum in the exports of manufactures, higher than the target of 19.8 per cent, due to the good performance of the manufacturing sector. These achievements reflected the improved competitiveness of Malaysia's export products. The exports of electrical machinery, appliance and parts accounted for 65.7 per cent of total manufactured exports in 1995, compared with 56.6 per cent in 1990, as shown in *Chart 2-1*.

2.16 Malaysia's exporters continued to improve their utilization of preferential access to the markets of the fourteen preference-giving entities under the Generalised System of Preferences (GSP). The share of GSP exports in Malaysia's total exports increased from 11.9 per cent in 1991 to 12.5 per cent in 1995, valued at RM11.2 billion and RM23.1 billion, respectively. The EU accounted for almost half of GSP exports from Malaysia while the US and Japanese schemes accounted for 25.8 per cent and 13.7 per cent, respectively. Manufactures and semi-manufactures constituted more than 80 per cent of total GSP exports from Malaysia with electrical and electronic products being the largest beneficiary of the GSP. Growth in exports, greater awareness of the system among exporters and the ability of more products to meet specific rules of origins under various schemes contributed to the higher utilization of the GSP scheme.

TABLE 2-2

DIRECTION OF TRADE, 1990-95

Direction	RM million						Share of Total (%)						Average Annual Growth Rate (%), 1991-95		
	Exports		Imports		Total Trade		Exports		Imports		Total Trade				
	1990	1995	1990	1995	1990	1995	1990	1995	1990	1995	1990	1995	Exports	Imports	Total
ASEAN[1]	**23,065.5**	**50,418.0**	**15,085.0**	**33,733.2**	**38,150.5**	**84,151.2**	***29.0***	***27.2***	***19.1***	***17.4***	***24.0***	***22.2***	***16.9***	***17.5***	***17.1***
Singapore	18,052.1	37,598.7	11,800.0	24,059.7	29,852.1	61,658.4	*22.7*	*20.3*	*14.9*	*12.4*	*18.8*	*16.2*	*15.8*	*15.3*	*15.6*
Indonesia	920.7	2,444.0	850.8	3,059.7	1,771.5	5,503.7	*1.2*	*1.3*	*1.1*	*1.6*	*1.1*	*1.4*	*21.6*	*29.2*	*25.4*
Thailand	2,788.0	7,265.6	1,881.2	5,134.7	4,669.2	12,400.3	*3.5*	*3.9*	*2.4*	*2.6*	*2.9*	*3.3*	*21.1*	*22.2*	*21.6*
Philippines	1,064.6	1,694.0	427.3	1,154.5	1,491.9	2,848.5	*1.3*	*0.9*	*0.5*	*0.6*	*0.9*	*0.7*	*9.7*	*22.0*	*13.8*
European Union[2]	**12,204.5**	**26,204.5**	**12,494.4**	**29,634.7**	**24,698.9**	**55,839.2**	***15.3***	***14.2***	***15.8***	***15.2***	***15.6***	***14.7***	***16.6***	***18.9***	***17.7***
United Kingdom	3,136.0	7,486.2	4,312.3	5,482.3	7,448.3	12,968.5	*3.9*	*4.0*	*5.5*	*2.8*	*4.7*	*3.4*	*19.0*	*4.9*	*11.7*
Republic of Germany	3,096.8	5,928.0	3,389.2	8,600.5	6,486.0	14,528.5	*3.9*	*3.2*	*4.3*	*4.4*	*4.1*	*3.8*	*13.9*	*20.5*	*17.5*
United States of America	**13,487.0**	**38,322.6**	**13,232.5**	**31,757.5**	**26,719.5**	**70,080.1**	***16.9***	***20.7***	***16.7***	***16.3***	***16.8***	***18.4***	***23.2***	***19.1***	***21.3***
Japan	**12,588.9**	**23,584.6**	**18,973.8**	**53,127.7**	**31,562.7**	**76,712.3**	***15.8***	***12.7***	***24.0***	***27.3***	***19.9***	***20.2***	***13.4***	***22.9***	***19.4***
NIEs (excl. Singapore)	**7,928.2**	**20,936.9**	**7,854.1**	**22,073.3**	**15,782.3**	**43,010.2**	***10.0***	***11.3***	***9.9***	***11.3***	***9.9***	***11.3***	***21.4***	***23.0***	***22.2***
Hong Kong	2,523.1	9,928.5	1,497.5	4,195.0	4,020.6	14,123.5	*3.2*	*5.4*	*1.9*	*2.2*	*2.5*	*3.7*	*31.5*	*22.9*	*28.6*
South Korea	3,677.0	5,195.3	2,033.6	7,960.9	5,710.6	13,156.2	*4.6*	*2.8*	*2.6*	*4.1*	*3.6*	*3.5*	*7.2*	*31.4*	*18.2*
Taiwan	1,728.1	5,813.1	4,323.0	9,917.4	6,051.1	15,730.5	*2.2*	*3.1*	*5.5*	*5.1*	*3.8*	*4.1*	*27.5*	*18.1*	*21.1*
Rest of the World	**10,372.3**	**25,858.3**	**11,478.8**	**24,202.6**	**21,851.1**	**50,060.9**	***13.0***	***13.9***	***14.5***	***12.5***	***13.8***	***13.2***	***20.0***	***16.1***	***18.0***
Total	**79,646.4**	**185,324.9**	**79,118.6**	**194,529.0**	**158,765.0**	**379,853.9**	***100.0***	***100.0***	***100.0***	***100.0***	***100.0***	***100.0***	***18.4***	***19.7***	***19.1***
South Countries[3] **(excl. Singapore)**	**12,033.3**	**32,158.0**	**8,464.0**	**20,527.8**	**20,497.3**	**52,685.8**	***15.1***	***17.4***	***10.7***	***10.6***	***12.9***	***13.9***	***21.7***	***19.4***	***20.8***

Notes:

[1] Includes Vietnam.

[2] Include Austria, Finland and Sweden.

[3] South countries include ASEAN and the other South East Asian countries, Indo-China, South Asia, North-East Asia excluding NIEs and Japan, Latin America, Africa, West Asia and the developing island countries in the South Pacific.

TABLE 2-3

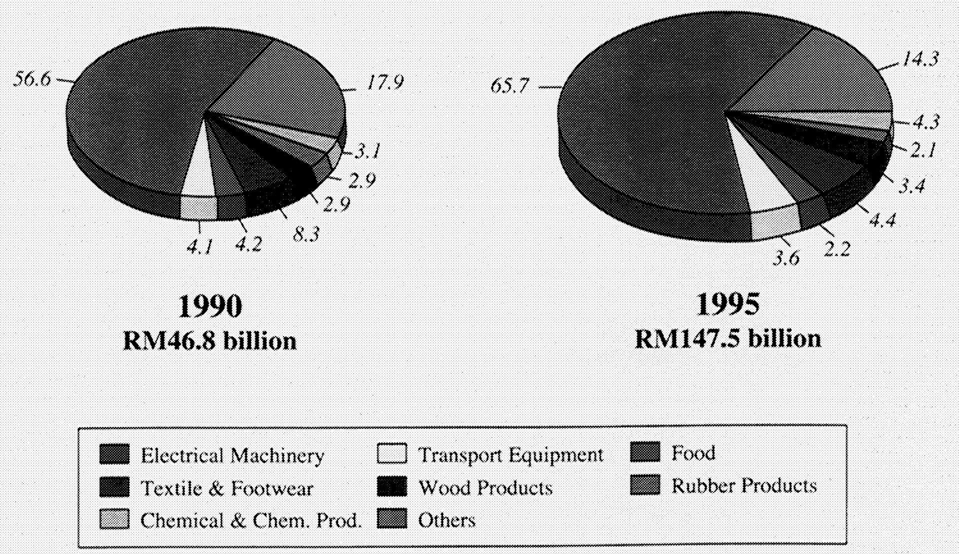
MERCHANDISE TRADE, 1990-95

Item	RM million		Share of Total (%)		Average Annual Growth Rate (%)
	1990	1995	1990	1995	6MP
Gross Exports					
Agriculture	17,761	24,368	22.3	13.1	6.5
Mining	14,573	10,826	18.3	5.8	-5.8
Manufacturing	46,835	147,524	58.8	79.6	25.8
Others	477	2,607	0.6	1.5	40.5
Total	**79,646**	**185,325**	**100.0**	**100.0**	**18.4**
Gross Imports					
Consumption Goods	13,015	27,527	16.4	14.2	16.2
Investment Goods	29,658	78,730	37.5	40.5	21.6
Intermediate Goods	35,904	87,242	45.4	44.8	19.4
Import for Re-export	541	1,030	0.7	0.5	13.7
Total	**79,119**	**194,529**	**100.0**	**100.0**	**19.7**

CHART 2-1

GROSS EXPORTS OF MANUFACTURED GOODS, 1990-95

(% of total)



2.17 During the Sixth Plan, many developed countries reviewed their GSP schemes. In this regard, the Government continued its efforts to negotiate against any unfair withdrawal of the GSP schemes for Malaysia. At the same time, Malaysian exporters were encouraged to prepare themselves for increased competition by improving efficiency and productivity of their trade operations as well as strengthening linkages and networking with importers in preference-giving countries.

2.18 Malaysian industries continued to have high import content in its structure of production, despite efforts to deepen and broaden the industrial base, as reflected in the acceleration of *gross imports* at 19.7 per cent per annum. However, at the end of the Plan, 85.3 per cent of these imports consisted of intermediate and investment goods which were for productive purposes. On average, imports of intermediate goods grew by 19.4 per cent per annum to account for 44.8 per cent of gross imports at the end of the Plan period, as shown in *Table 2-4*. This growth was due mainly to the rapid growth in manufacturing activities, with imports of materials for manufacturing growing by 21.6 per cent and constituting 38.8 per cent of gross imports in 1995. In line with the robust construction activities in the country, imports of building and construction materials grew rapidly at 15.4 per cent per annum, especially building materials such as lime, cement, clay, asbestos and glass. Similarly, imports of investment goods grew by 21.6 per cent per annum and constituted 40.5 per cent of imports at the end of 1995. This reflected the continued strong investment activities in the manufacturing, construction and transport sectors. Imports of transport equipment rose by 14.1 per cent per annum as a result of increased imports of aircraft and ships, railway locomotives, commercial vehicles and buses as well as automobiles to meet the growing demand of the transport sector. At the same time, imports of machinery increased by 19.9 per cent per annum as a result of higher demand especially from the manufacturing sector. Efforts to expand, upgrade and modernize telecommunications infrastructure resulted in the surge in imports of telecommunications equipment by 35 per cent. As a result, even though the export performance was impressive, the net external sector's contribution to economic growth declined by 2.7 per cent. Malaysia's terms of trade, on the other hand, improved by 1.3 per cent, due to improvements in export prices.

2.19 The upsurge in imports, however, resulted in the deficit in the *trade balance* in 1994, for the third time in history. This, together with the widening deficit in the services account which was largely due to the high outflow of investment income, freight and insurance and other services, resulted in deficits

TABLE 2-4

IMPORTS OF SELECTED INVESTMENT AND INTERMEDIATE GOODS, 1990-95

Item	*RM million*		*Share of Total (%)*		*Average Annual Growth Rate (%), 1991-95*
	1990	*1995*	*1990*	*1995*	
Total Investment Goods	**29,658.2**	**78,730.2**	***37.5***	***40.5***	***21.6***
Metal	4,994.2	11,714.3	*6.3*	*6.0*	*18.6*
Iron and Steel and Alloys of Iron	3,011.7	7,289.0	*3.8*	*3.7*	*19.3*
Non-ferrous Metal	1,204.0	3,166.0	*1.5*	*1.6*	*21.3*
Tools	313.5	624.9	*0.4*	*0.3*	*14.8*
Others	465.0	634.4	*0.6*	*0.3*	*6.4*
Transport Equipment	5,775.9	11,169.7	*7.3*	*5.7*	*14.1*
Commercial Vehicles	827.4	1,543.5	*1.0*	*0.8*	*13.3*
Railway Locomotives	111.0	328.5	*0.1*	*0.2*	*24.2*
Aircraft and Parts	3,111.2	6,374.3	*3.9*	*3.3*	*15.4*
Ships and Boats	1,457.5	2,393.5	*1.8*	*1.2*	*10.4*
Others	268.8	529.9	*0.3*	*0.3*	*14.5*
Machinery	8,828.0	21,900.0	*11.2*	*11.3*	*19.9*
Mining and Construction	1,369.2	2,780.0	*1.7*	*1.4*	*15.2*
Manufacturing	3,658.8	9,846.6	*4.6*	*5.1*	*21.9*
Printing	604.0	725.8	*0.8*	*0.4*	*3.7*
Others	3,196.0	8,547.1	*4.0*	*4.4*	*21.7*
Other Investment Goods	10,060.1	33,946.2	*12.7*	*17.5*	*27.5*
Generators	2,274.4	8,786.4	*2.9*	*4.5*	*31.0*
Electronic Fittings and Equipment	3,282.8	10,480.3	*4.1*	*5.4*	*26.1*
Telecommunications Equipment	832.7	3,735.3	*1.1*	*1.9*	*35.0*
Office Equipment	1,885.8	6,363.3	*2.4*	*3.5*	*29.5*
Others	1,784.4	4,080.9	*2.3*	*2.1*	*18.0*
Total Intermediate Goods	**35,904.0**	**87,242.0**	***45.4***	***44.8***	***19.4***
Materials for Agriculture and Husbandry	1,095.0	1,703.8	*1.4*	*0.9*	*9.2*
Feeding Stuff for Animals	346.7	613.2	*0.4*	*0.3*	*12.1*
Fertilizer	661.2	938.1	*0.8*	*0.5*	*7.2*
Others	87.1	152.5	*0.1*	*0.1*	*11.9*
Materials for Manufacturing	28,379.5	75,404.9	*35.9*	*38.8*	*21.6*
Parts for Motor Assembly	2,322.8	4,434.7	*2.9*	*2.3*	*13.8*
Chemical Items	2,491.0	5,865.9	*3.1*	*3.0*	*18.7*
Paper and Pulp	1,357.8	3,042.6	*1.7*	*1.6*	*17.5*
Food Items	1,912.0	2,803.3	*2.4*	*1.4*	*8.0*
Plastic Material	2,165.4	4,465.2	*2.7*	*2.3*	*15.6*
Electronic Component	10,302.9	39,258.4	*13.0*	*20.2*	*30.7*
Semi-manufactured Gold	3,780.2	4,874.4	*4.8*	*2.5*	*5.2*
Others	4,047.4	10,660.4	*5.1*	*5.5*	*21.4*
Building and Construction Material	2,147.1	4,385.0	*2.7*	*2.3*	*15.4*
Building Materials of Lime, Cement, Clay, Asbestos and Glass	286.8	1,220.4	*0.4*	*0.6*	*33.6*
Tubes, Pipes and Fittings	988.1	1,129.5	*1.2*	*0.6*	*2.7*
Others	872.2	2,035.1	*1.1*	*1.0*	*18.5*
Other Intermediate Goods	4,282.4	5,748.3	*5.4*	*3.0*	*6.1*
Crude Petroleum	432.3	402.6	*0.5*	*0.2*	*-1.4*
Petroleum Products	2,049.6	1,463.8	*2.6*	*0.8*	*-6.5*
Others	1,800.5	3,881.9	*2.3*	*2.0*	*16.6*
Total Consumption Goods	**13,015.4**	**27,526.6**	***16.4***	***14.2***	***16.2***
Import for Re-export	**541.0**	**1,030.2**	***0.7***	***0.5***	***13.7***
Total Imports	**79,118.6**	**194,529.0**	***100.0***	***100.0***	***19.7***

in the current account throughout the Sixth Plan period. The current account registered a deficit of 6.7 per cent of GNP or RM53.5 billion during the Plan period. However, due to strong net capital inflows, the overall balance registered a surplus of 4.6 per cent of GNP.

2.20 Malaysia's favourable trade performance was also attributed to the better performance of world trade which grew at an average rate of 5.8 per cent per annum. Increased economic activities in the industrialized countries as well as the increased trade between industrialized and developing countries and among developing countries, contributed to the higher growth of world trade. The Plan period witnessed the successful completion of the Uruguay Round of multilateral trade negotiations under the auspices of the General Agreement on Tariffs and Trade (GATT), resulting in the establishment of the World Trade Organization (WTO) and this augured well for multilateralism and free trade. The period also saw the signing of the North American Free Trade Agreement (NAFTA), the formation of the EU single market, further developments in the Asia-Pacific Economic Cooperation (APEC), the establishment of the ASEAN Free Trade Area (AFTA) and the ASEAN endorsement of the East Asian Economic Caucus (EAEC) which was supported by many Asian countries as an economic platform to discuss common interests. Developments in these regional economic groupings are also expected to contribute to increased trade, provided these groupings are outward looking. The world economy grew at an average rate of 2.7 per cent per annum during the period. The average growth of the developing countries and industrialized countries was 5.8 per cent and 1.9 per cent respectively. The East Asian countries were the main contributors to world economic growth.

2.21 On the *supply side*, the growth of the manufacturing, construction and services sectors provided the major impetus to overall economic growth. The *manufacturing sector* grew at an average rate of 13.3 per cent per annum which was higher than the targeted rate of growth of 12.2 per cent. As a result, its share in GDP increased from 26.9 per cent in 1990 to 33.1 per cent in 1995. This growth was due to improved productive efficiency and capability of industries brought about by the absorption and upgrading of technology. The growth was also supported by the continued expansion of the export-oriented industries, with the major contributor being the electrical machinery and apparatus subsector which had diversified into higher value-added products such as consumer and industrial electronics. Similarly, the domestic-oriented industries such as the industrial chemical and other chemicals subsector was also a major contributor to growth, especially from the development of petroleum resources in downstream activities. The presence of multinational corporations (MNCs), with their skill training and cost effective plant operations, helped to enhance technology absorption and increase overall competitiveness. They also provided an important benchmark for local industries to adapt quickly to the competitive international environment.

2.22 The *construction sector* grew at an average rate of 13.3 per cent per annum and its share of GDP increased to 4.4 per cent in 1995. This growth emanated mainly from the implementation of several large infrastructure projects such as ports, highways and railways, coupled with continued expansion in the construction of residential, commercial and industrial buildings. The accelerated privatization programme also contributed significantly to the growth of this sector. Among the projects implemented were the Kuala Lumpur City Centre, the *Menara Kuala Lumpur,* the National Sports Complex and Commonwealth Village, the North Butterworth container terminal, the West Port at Pulau Indah, the South Port of Klang, the Shah Alam Expressway, the North-South Expressway Central Link, the Second Crossing Malaysia-Singapore, the Light Rail Transit and the electrified double-track commuter service.

2.23 The *services sector* as a group grew at an average rate of 9.3 per cent per annum, with its share reaching 43 per cent of GDP at the end of the Plan period. However, within the sector, the electricity, gas and water; wholesale and retail trade, hotels and restaurants; and finance, real estate and business services subsectors recorded double digit growth. The biggest contributor to the services sector's growth was the wholesale and retail trade, hotels and restaurants subsector as a result of new entrants and the expansion of existing retailers to new cities and towns. This was complemented by an increase in consumer spending, arising from higher disposable income. The Visit Malaysia Year 1994 campaign contributed to the growth of tourism services. High growth in the electricity subsector was due to increased demand mainly from the manufacturing sector. The performance of the financial subsector was enhanced by the continuous modernization process, the development of the private debt securities market, the increasing number of financial institutions offering Islamic banking services and the increasingly competitive business environment.

2.24 The *agriculture sector* grew at an average rate of 2.0 per cent per annum, while its share of GDP continued to decline to reach 13.6 per cent at the end of the period. The expansion in the palm oil, livestock and fisheries subsectors contributed to the growth of this sector. Similarly, the *mining sector* achieved a higher than targeted growth of 1.1 per cent, averaging 2.9 per cent per annum, as a result of increased production of gas and condensates, a by-product of gas. However, production of tin declined further during the Plan period. The sector's share of GDP also declined to 7.4 per cent at the end of the period.

2.25 The rapid economic growth resulted in an overall increase in the demand for labour and a further tightening of the labour market. The unemployment rate declined to 2.8 per cent in 1995, indicating that the economy was virtually at full employment. Shortages of both skilled and unskilled workers became prevalent as the number of jobs created outpaced the number of new entrants into the labour market. The Government allowed the use of foreign labour as a temporary measure and simultaneously undertook measures to upgrade skills as well as to promote greater automation and more capital- and technology-intensive industries.

III. MACROECONOMIC FRAMEWORK FOR THE SEVENTH PLAN

2.26 During the Seventh Plan period, the economy is expected to maintain the current momentum of high growth. The expanded productive capacity and the structural transformation will further enhance economic resilience. Within the framework of the Government's policy to continue to pursue prudent fiscal and monetary policies, the private sector is expected to continue to play a leading role in economic growth. In addition, private sector initiatives through an accelerated privatization programme will promote greater efficiency and productivity in the economy. At the same time, the projected improvements in the global economy are expected to contribute to the expansion of the Malaysian economy.

Macroeconomic Strategies

2.27 The focus of macroeconomic management in the medium term will be to sustain high growth with stability and to enhance the country's international competitiveness. In the pursuit of rapid growth, the Government will ensure that there is sustainable development. In view of labour constraints and the already high dependence on investment growth, the achievement of high growth will rely more on the increased contribution from TFP, which reflects the efficient use of the factors of production. This will enable the change in the productive structure of the economy to emphasize increased efficiency and productivity, particularly in higher value added activities, including more technology-intensive industries. It is through productivity-driven growth that the economy will attain high growth with low inflation throughout the Seventh Plan period.

2.28 New initiatives will be effected during the Seventh Plan period to enable the economy to meet these challenges. At the same time, the implementation of policies and strategies that are already in place will be intensified. The following strategies will be adopted:

- o *maintaining macroeconomic stability by pursuing prudent and pragmatic fiscal and monetary policies to sustain high growth with price stability;*
- o *emphasizing productivity augmenting policies over the whole spectrum of economic activities to effect a transformation from being investment-driven to a productivity-driven economy;*
- o *mobilizing high domestic savings to support domestic investments;*
- o *emphasizing large-scale industrial production for exports for the global market in order to enjoy the benefits of economies of scale and lower costs of production as well as restructuring strategic industries to nurture capital- and technology-intensive and knowledge-based activities;*
- o *instituting measures to reduce the deficit in the current account of the balance of payments by encouraging domestic production of industrial inputs to meet domestic demand as well as exports and expanding potential activities in the services sector that can be exported to correct the imbalances in the services account of the balance of payments; and*
- o *establishing strategic alliances and niche markets overseas to encourage Malaysian investors to venture abroad and source their capital from international markets in the era of increasing globalization of business operations.*

International Economic Outlook

2.29 The world economy is expected to grow at 3.3 per cent per annum during the Plan period. Output in the high-income Organization of Economic Cooperation and Development (OECD) countries is projected to grow at 2.8 per cent, following moderate success in pursuing supply-enhancing structural reforms in such areas as labour, fiscal policy and trade. Inflation is expected to average about 2.7 per cent during the period. This projection of sustained, low inflationary growth is based on the continuance of prudent monetary policies, fiscal consolidation and a reduction of rigidities in labour and product markets. The increasing importance of developing countries in world trade and output is also likely to contribute to the output growth of OECD and other industrial countries. There will be a marked improvement in the international economic environment over the coming decade as the recovery in the industrial countries has been faster than expected and the prospects for sustaining the recovery are good. This is a result of progress in reducing inflation and the continuing anti-inflationary orientation of monetary policies. Concerted policies aimed at containing inflation will further improve the international environment.

2.30 With the sustained growth of the world economy, total world demand for capital will increase and real long-term interest rates are expected to be moderately high. The expected slower growth of capital inflows to developing countries and the anticipated higher debt-service charges will require these countries to improve domestic savings and enhance export performance. However, FDI flows are expected to rise as a consequence of further globalization of corporate production and distribution strategies caused by trade liberalization, technological change and opening up of previously closed economies. Apart from finance, these flows will contribute to the development of technology and export markets. The favourable international environment augurs well for the growth prospects of developing countries. During the period, developing countries are projected to grow at 4.9 per cent per annum. These prospects will be influenced by the policy responses of developing countries.

2.31 East Asia is likely to remain the fastest growing region over the next decade, with growth expected to average 7.7 per cent per annum. As a result of the recent rapid growth of the East Asian countries of between 6.5 to 7.5 per cent compared with the 2.5 to 3.0 per cent growth in Europe and the US, the East Asian region has now reached parity with Western Europe and North America, leading to the emergence of a tripolar world. By the end of the Plan period, East Asia's share of world output is expected to be 28.2 per cent and its share of world trade will be about one-third.

2.32 World trade is expected to grow at 6.0 per cent per annum during the Plan period. The coming into effect of the WTO will contribute to greater global economic cooperation, resulting in a fairer and more open multilateral trading system. Similarly, open regionalism will also lead to increased world trade and investment. Trade integration will also be facilitated by trade initiatives at regional and sub-regional levels. In addition, trade in services is expected to grow at a faster rate than merchandise trade due to higher inflows of FDI, particularly to the services sector. However, attempts by major developed nations to restrict market access by attaching conditions relating to environment and social clauses may impede the growth of world trade. Similarly, market access will also be affected should the continuing trade disputes among industrialized nations result in numerical targeting being used. As such, greater international cooperation, mutual understanding and commitment to multilateralism are pivotal in the effective promotion of world trade.

2.33 The rapid expansion of infrastructure development in the Asia-Pacific region will attract massive private capital inflows in the form of project financing. The implementation of AFTA will facilitate the inflow of funds into the ASEAN region and the relocation of Japanese industries in the region due to uncertainties in the Japanese economy. Effective utilization of these inflows to promote growth and development will dampen possible inflationary pressures.

The Malaysian Economy

2.34 With strong macroeconomic fundamentals in place, the Malaysian economy is poised to maintain the potential output growth achieved during the Sixth Plan period. Infrastructure improvements will be continued to meet the increasing demand while the supply of skilled manpower will be increased to support the shift towards capital- and technology-intensive activities. In addition, efforts will have to be made to reduce the import content of exportables. Greater trade liberalization in international markets will enhance the prospects of increased global trade for Malaysia.

Growth Prospects

2.35 The Malaysian economy is projected to grow at an average rate of 8.0 per cent per annum with low inflation. This growth will be sustained by domestic demand, while investment will continue to be a significant contributor with private investment continuing to be an important source of growth for the domestic economy. Foreign investment will remain important, particularly in upgrading technology, skills and management expertise. Although consumption will be contained at a reasonable level, it will be higher than that achieved in the Sixth Plan period. Private consumption is expected to grow at an average rate of 7.4 per cent per annum, reflecting increasing affluence while the growth of public consumption will decline to 7.0 per cent per annum compared with the Sixth Plan growth of 9.5 per cent. The expected high growth of the economy and the projected level of consumption will ensure that sufficient domestic funds can be raised to finance domestic investment and reverse investment. With this projected growth and the achievement thus far, the economy is expected to register an average annual growth of 8.3 per cent during the Second Outline Perspective Plan (OPP2) period, far exceeding the earlier projection of 7.0 per cent.

2.36 During the Seventh Plan period, the contribution from capital will remain high at 3.0 per cent of output growth, reflecting the continued high investment required to enable the industrial structure to shift to capital- and technology-intensive activities. However, it is lower than the 3.7 per cent achieved during the Sixth Plan, as shown in *Table 2-1*. Similarly, labour contribution to growth is projected to decline to 1.7 per cent, given the projected slower employment growth of 2.8 per cent. The unemployment rate will be maintained at 2.8 per cent by the end of the Plan period, as recorded at the end of the Sixth Plan period. The contribution from TFP is expected to increase to 3.3 per cent or 41.3 per cent of output growth compared with 2.5 per cent or 28.7 per cent of growth attained during the Sixth Plan period.

2.37 Given the constraints on labour and capital, the economy will rely more on contribution from TFP to ensure the achievement of the projected economic growth. Increased contribution from TFP necessitates increases in the rates of innovation and technological absorption, enhancements in technological and managerial knowledge, emphasis on quality investments, effective and efficient use of resources and improving the quality and skills of human resources. Similarly, strengthening S&T and R&D capabilities are important prerequisites for continued improvements in productivity, quality of products and the development of new products. These efforts to increase contribution from TFP is in line with the strategy towards productivity-driven growth.

Sectoral Output

2.38 Growth in the Seventh Plan period will continue to emanate from the manufacturing, services and construction sectors, as shown in *Table 2-5*. The *manufacturing sector* is expected to grow at an average rate of 10.7 per cent per annum. Although this projected growth is lower than the 13.3 per cent achieved under the Sixth Plan, the share of this sector to GDP will increase to 37.5 per cent by the year 2000, as shown in *Chart 2-2*. The main contributor to growth will continue to be the electrical machinery and apparatus subsector, arising from the rapid growth generated by strong external demand. This subsector is expected to contribute 34.5 per cent to manufacturing value-added.

TABLE 2-5

GROSS DOMESTIC PRODUCT BY INDUSTRY OF ORIGIN, 1990-2000

Sector	*RM million (in 1978 prices)*			*Average Annual Growth Rate (%)*			*Contribution to Growth (%)*		*Share of GDP (%)*		
	1990	*1995*	*2000*	*Target 6MP*	*Achieved 6MP*	*Target 7MP*	*6MP*	*7MP*	*1990*	*1995*	*2000*
Agriculture, Forestry, Livestock & Fishing	14,827	16,406	18,460	*2.1*	*2.0*	*2.4*	*0.3*	*0.3*	*18.7*	*13.6*	*10.5*
Mining & Quarrying	7,757	8,938	10,023	*1.1*	*2.9*	*2.3*	*0.3*	*0.2*	*9.8*	*7.4*	*5.7*
Manufacturing	21,340	39,825	66,251	*12.2*	*13.3*	*10.7*	*3.9*	*3.7*	*26.9*	*33.1*	*37.5*
Construction	2,832	5,277	8,560	*12.8*	*13.3*	*10.2*	*0.5*	*0.5*	*3.6*	*4.4*	*4.8*
Electricity, Gas & Water	1,526	2,823	4,686	*12.3*	*13.1*	*10.7*	*0.3*	*0.3*	*1.9*	*2.3*	*2.7*
Transport, Storage & Communications	5,487	8,787	14,599	*10.0*	*9.9*	*10.7*	*0.7*	*0.8*	*6.9*	*7.3*	*8.3*
Wholesale & Retail Trade, Hotels & Restaurants	8,806	14,568	22,378	*11.4*	*10.6*	*9.0*	*1.2*	*1.1*	*11.1*	*12.1*	*12.7*
Finance, Insurance, Real Estate & Business Services	7,758	12,884	20,977	*11.0*	*10.7*	*10.2*	*1.1*	*1.1*	*9.8*	*10.7*	*11.9*
Government Services	8,447	11,683	14,354	*4.5*	*6.7*	*4.2*	*0.7*	*0.4*	*10.6*	*9.7*	*8.1*
Other Services	1,678	2,436	3,749	*8.1*	*7.7*	*9.0*	*0.2*	*0.2*	*2.1*	*2.0*	*2.1*
(-) Imputed Bank Service Charges	4,076	8,414	13,242	*14.8*	*15.6*	*9.5*	*0.9*	*0.7*	*5.1*	*7.0*	*7.5*
(+) Import Duties	2,947	5,101	5,840	*9.9*	*11.6*	*2.7*	*0.4*	*0.1*	*3.7*	*4.3*	*3.2*
GDP at Purchasers' Value	**79,329**	**120,316**	**176,635**	***8.1***	***8.7***	***8.0***	***8.7***	***8.0***	***100.0***	***100.0***	***100.0***
Adjusted for Import Duties less Imputed Bank Service Charges											
PRIMARY SECTOR	22,267	24,665	27,337	*1.5*	*2.1*	*2.1*	*0.5*	*0.4*	*28.1*	*20.5*	*15.5*
SECONDARY SECTOR	23,832	43,894	71,802	*11.9*	*13.0*	*10.3*	*4.3*	*4.0*	*30.0*	*36.5*	*40.6*
TERTIARY SECTOR	33,230	51,757	77,496	*9.1*	*9.3*	*8.4*	*3.9*	*3.6*	*41.9*	*43.0*	*43.9*

The subsectors of industrial chemicals and other chemical products, wood and wood products, non-metallic mineral products, transport equipment, and fabricated metal products will play an increasingly important role. The expansion in these subsectors will reflect largely the significant growth in local demand brought about by the expansion in construction and industrial activities.

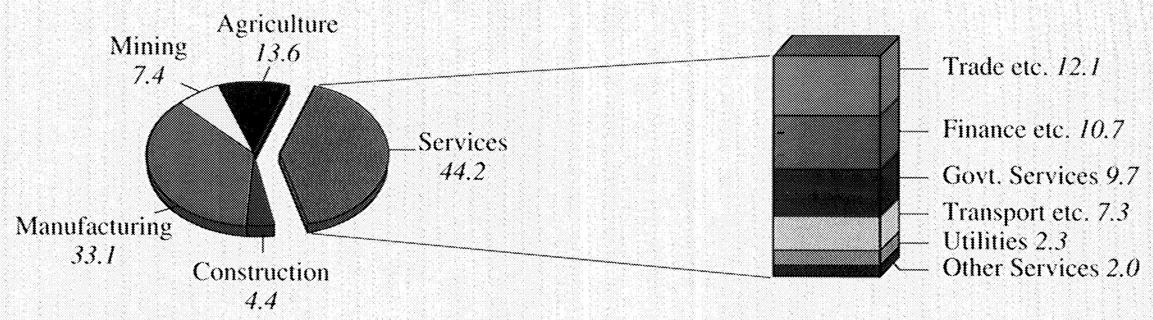
2.39 The export-oriented strategy for manufacturing industries will be strongly emphasized during the Seventh Plan. Manufactured products are projected to account for 88.6 per cent of total merchandise export earnings in the year 2000 compared with 79.6 per cent in 1995. In this regard, manufacturers particularly local entrepreneurs, will be encouraged to undertake large-scale production to benefit from economies of scale as well as increase local content in manufacturing. Apart from increasing foreign exchange earnings, the strategy will lead to the development of competitive industries as entrepreneurs target production of quality products for the export market.

CHART 2-2

GROSS DOMESTIC PRODUCT BY INDUSTRY OF ORIGIN, 1995-2000

(share of GDP (%))

1995 (RM120.3 billion)



2000 (RM176.6 billion)

Note: Total of percentages will be more than 100% as bank service charges and import duties are not taken into account.

2.40 In line with the strong domestic demand and significant expansion of the leading sectors of the economy, the *services sector* is estimated to grow at 8.4 per cent per annum, while its share of GDP will expand to 43.9 per cent by the year 2000. Policies and strategies that are formulated to develop the sector will take into account the challenges of international competition arising from the agreement to liberalize trade in services under the General Agreement on Trade in Services (GATS). The services sector must, therefore, be more competitive and prepared to enter the international market. The services sector will increasingly become another major source of growth in the economic transformation process.

2.41 The main impetus to growth of the services sector is expected to come from the wholesale and retail trade, hotels and restaurants; finance, insurance and business services; and transport, storage and communications subsectors. In addition, the exports of educational services is expected to grow in line with efforts to establish Malaysia as a regional centre of educational excellence. Similarly, the health-care industry can play an important role in contributing to the growth of the services sector, while the finance, tourism, professional and consultancy subsectors have the potential to grow as important export earners, thereby assisting in improving the services account of the balance of payments. In the longer term, the shipping and insurance subsectors will have sufficiently expanded to offset the increasing dependence on foreign freight and insurance services. Further expansion of the services sector will also depend on fast modernization and integration of information technology as it is recognized as an important catalyst for growth, particularly for the financial and business services subsectors.

2.42 The *construction sector* is expected to grow at 10.2 per cent per annum. Large infrastructure projects undertaken through privatization as well as residential and commercial development and the continued expansion of the manufacturing sector are expected to provide the growth momentum for this sector. Its share of GDP is expected to reach 4.8 per cent by the end of the Seventh Plan period compared with 4.4 per cent at the end of the Sixth Plan. This share will exceed the OPP2 target of 3.5 per cent of GDP.

2.43 The *agriculture sector* is anticipated to grow at 2.4 per cent per annum, higher than that achieved in the Sixth Plan period. Palm oil is expected to contribute significantly to the overall agriculture sector growth. Simultaneously, the cultivation of high value crops and the expansion of aquaculture activities will be promoted, given their considerable potential for further growth.

2.44 Despite the decline of its share of GDP to 10.5 per cent by the end of the Plan period, the agriculture sector is expected to remain an important sector contributing 0.3 per cent to the output growth of 8.0 per cent during the period. In view of the structural change in the economy, a complete review of the National Agricultural Policy, 1992-2010 will be undertaken. Mechanization of agricultural practices as well as ensuring economies of scale in production will be promoted. Alternative use of agricultural land for higher value-added activities will be encouraged to ensure its optimal use and increased income for the agriculture community.

2.45 The *mining sector* is expected to grow at 2.3 per cent per annum, lower than the achievement recorded during the Sixth Plan. The gas and quarrying subsectors, which expanded significantly in the Sixth Plan, will continue their momentum of growth in the Seventh Plan period. However, crude oil will remain the major contributor to overall value-added in the sector, with an average contribution of almost 80 per cent. Production of crude oil will be about 606,000 barrels per day (bpd) in line with the National Depletion Policy. However, production of condensates is expected to increase from approximately 42,000 bpd in 1995 to 95,000 bpd in the year 2000, consistent with the increased production of gas. The sector's share of GDP is expected to be 5.7 per cent by the end of the Plan period.

Aggregate Demand

2.46 The continued expansion of the economy during the Plan period will be buoyed by strong domestic demand as well as the sustained growth of the world economy. Total investment is expected to grow by 5.6 per cent per annum, as shown in *Table 2-6. Private investment* will continue to provide the stimulus for the economy, growing at an average rate of 7.8 per cent per annum, and its share is expected to be 73.6 per cent of total investment in the year 2000. Although this growth rate is lower than the 16.6 per cent achieved during the Sixth Plan period, the RM384.8 billion of private investment in current terms, required for the Seventh Plan period, is higher by 85.5 per cent compared with the RM207.4 billion invested during the Sixth Plan. *Public investment* is expected to grow at 0.6 per cent per annum to record a total of RM150.8 billion in current terms. Public investment will continue to focus on providing basic amenities such as health and education and other infrastructural facilities as well as developing skilled manpower and deepening the S&T base to complement activities and support initiatives of the private sector.

TABLE 2-6

GROSS NATIONAL PRODUCT BY EXPENDITURE CATEGORY, 1990-2000

(in current prices with 1978 prices in italics)

Category	*RM million*			*Average Annual Growth Rate (%)*			*Contribution to Growth (%)*		*Share of GNP (%)*		
	1990	*1995*	*2000*	*Target 6MP*	*Achieved 6MP*	*Target 7MP*	*6MP*	*7MP*	*1990*	*1995*	*2000*
Consumption	77,112	133,653	217,961	10.3	11.6	10.3	7.6	6.3	69.7	66.1	63.4
	51,240	*75,332*	*107,401*	*6.7*	*8.0*	*7.4*	*5.1*	*4.5*	*67.5*	*66.3*	*64.0*
Private	60,903	106,407	177,451	10.3	11.8	10.8	6.1	5.3	55.0	52.6	51.6
	39,728	*57,230*	*81,969*	*6.0*	*7.6*	*7.4*	*3.7*	*3.5*	*52.3*	*50.4*	*48.8*
Public	16,209	27,246	40,510	10.3	10.9	8.3	1.5	1.0	14.7	13.5	11.8
	11,512	*18,102*	*25,432*	*9.1*	*9.5*	*7.0*	*1.4*	*1.0*	*15.2*	*15.9*	*15.2*
Investment	37,490	86,795	124,546	13.1	18.3	7.5	6.6	2.8	33.9	42.9	36.2
	25,872	*54,291*	*71,326*	*10.8*	*16.0*	*5.6*	*6.0*	*2.4*	*34.1*	*47.9*	*42.5*
Private	24,207	57,652	91,693	12.9	19.0	9.7	4.5	2.5	21.9	28.5	26.7
	16,705	*36,062*	*52,512*	*10.6*	*16.6*	*7.8*	*4.1*	*2.3*	*22.0*	*31.8*	*31.3*
Public	13,283	29,143	32,853	13.4	17.0	2.4	2.1	0.3	12.0	14.4	9.5
	9,167	*18,229*	*18,814*	*11.1*	*14.7*	*0.6*	*1.9*	*0.1*	*12.1*	*16.1*	*11.2*
Change in Stocks	-1,335	242	117	—	—	—	0.2	0.0	-1.2	0.1	0.0
	-1,103	*164*	*57*	—	—	—	*0.3*	*0.0*	*-1.5*	*0.1*	*0.0*
Exports of Goods & Non-factor Services	88,354	201,522	394,581	13.4	17.9	14.4	15.1	14.4	79.9	99.5	114.7
	62,990	*122,482*	*205,631*	*10.1*	*14.2*	*10.9*	*12.6*	*11.9*	*83.0*	*107.9*	*122.5*
Imports of Goods & Non-factor Services	85,920	208,483	376,352	12.4	19.4	12.5	16.4	12.5	77.7	103.0	109.4
	59,670	*131,953*	*207,780*	*10.6*	*17.2*	*9.5*	*15.3*	*10.8*	*78.6*	*116.2*	*123.7*
GDP at Purchasers' Value	115,701	213,729	360,853	12.3	13.1	11.0	13.1	11.0	104.6	105.6	104.9
	79,329	*120,316*	*176,635*	*8.1*	*8.7*	*8.0*	*8.7*	*8.0*	*104.5*	*106.0*	*105.3*
Net Factor Payments	-5,064	-11,255	-16,832	—	—	—	—	—	-4.6	-5.6	-4.9
	-3,425	*-6,788*	*-8,826*	—	—	—	—	—	*-4.5*	*-6.0*	*-5.3*
GNP at Purchasers' Value	**110,637**	**202,474**	**344,021**	**12.4**	**12.8**	**11.2**	—	—	**100.0**	**100.0**	**100.0**
	75,904	***113,528***	***167,809***	***8.2***	***8.4***	***8.1***	—	—	***100.0***	***100.0***	***100.0***
GNP Per Capita at Purchasers' Value (RM)	6,099	9,786	14,788	9.8	9.9	8.6	—	—	—	—	—

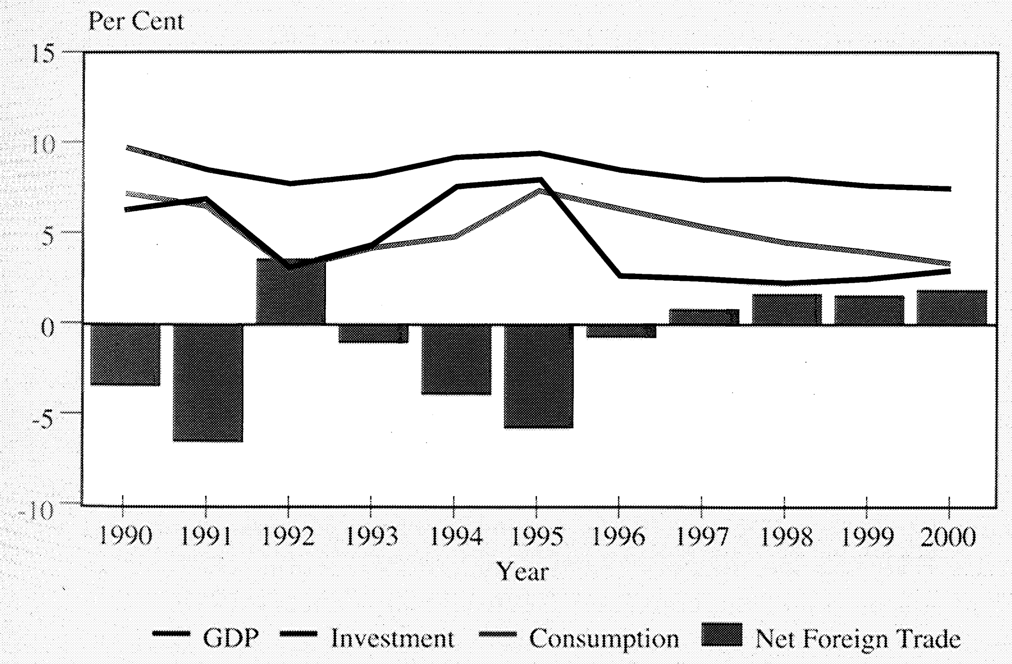
2.47 Total consumption will be maintained at a reasonable level and is forecasted to grow at an average rate of 7.4 per cent per annum, lower than that achieved during the Sixth Plan period. *Private consumption* is expected to grow at 7.4 per cent per annum. As evident by the expected increase in per capita income from RM9,786 in 1995 to RM14,788 in the year 2000, private consumption per capita is forecasted to increase from RM5,143 in 1995 to

RM7,628 in the year 2000. *Public consumption* is estimated to grow at 7.0 per cent, lower than that recorded during the Sixth Plan, reflecting continued prudent fiscal management by the Government.

2.48 With regards to *external demand*, exports of goods and non-factor services are expected to grow at 10.9 per cent per annum due to the improvement in the country's competitiveness and the increased prospects for world trade. The growth of imports of goods and non-factor services will be slower at 9.5 per cent per annum, in line with the anticipated increase in domestic production of some of the capital and intermediate goods required by industries. The net contribution of external trade to the economy is expected to improve by 1997, as shown in *Chart 2-3*.

CHART 2-3

GROSS NATIONAL PRODUCT BY EXPENDITURE CATEGORY, 1990-2000
(contribution to growth, %)



International Trade

2.49 Gross exports are expected to grow at an average rate of 14.4 per cent per annum during the period. The strong demand in the world market, resulting from the sustained growth of the industrialized countries and improved world trading environment, will act as an impetus to the growth of Malaysia's exports. The competitiveness of Malaysian products, particularly manufactured products, as well as the expansion of trade into new markets will also contribute to this growth. Policies will be formulated to reduce the import content of exportables. This will lead to increased local sourcing of production inputs particularly capital and intermediate goods. This will also reduce imports of these goods which formed 85.3 per cent of total imports in 1995.

2.50 The export of manufactures is expected to expand by an average rate of 16.9 per cent per annum during the Plan period, with earnings expected to double from RM147.5 billion in 1995 to RM322.4 billion in the year 2000, as shown in *Table 2-7*. The major manufactured products exported will include electronics and electrical products; transport equipment; wood products; textiles, clothing and footwear; and chemical and chemical products. The significant growth of manufactured exports reflect the sustained expansion in external demand with the anticipated recovery in a number of Malaysia's major trading partners. The widening of Malaysia's manufacturing base will help boost manufactured exports. In addition, the sustained growth of the Asia-Pacific region and greater efforts undertaken to penetrate non-traditional markets will increase the markets for Malaysian manufactured exports.

2.51 Agricultural exports are expected to grow by 1.5 per cent per annum during the Plan period due mainly to the increase in demand for palm oil and cocoa. Exports from the mining sector are expected to grow at 6.7 per cent per annum mainly on account of the strong growth of liquified natural gas exports at 9.9 per cent per annum. The export of crude oil is expected to decline by 3.2 per cent due to higher demand by domestic refineries.

2.52 With the rapid pace of industrialization and concomitant increases in income levels, Malaysia will eventually graduate out of the GSP status. Future access to facilities under the GSP will depend on the policy disposition of the preference-giving countries. The US proposes to end Malaysia's GSP privileges by January 1997, while the EU is graduating four Malaysian product sectors from its GSP scheme, namely plastics and rubber, wood, clothing as well as selected subsectors of the consumer electronics by January 1998. The proposed removal of these preferences will have some impact on Malaysian exports although this impact will be offset to a certain extent by tariff reductions under the WTO.

TABLE 2-7

COMMODITY PRODUCTION AND EXPORTS, 1990-2000

Commodity	*1990*	*1995*	*2000*	*Average Annual Growth Rate (%)*	
				6MP	*7MP*
Agriculture					
Palm Oil					
Production ('000 tonnes)	6,095	7,813	9,134	*5.1*	*3.2*
Export ('000 tonnes)	5,680	6,679	7,161	*3.3*	*1.4*
Unit Value (RM/tonne)	777	1,543	1,100	*14.7*	*-6.5*
Value (RM million)	4,421	10,331	7,877	*18.5*	*-5.3*
Rubber					
Production ('000 tonnes)	1,291	1,106	1,014	*-3.0*	*-1.7*
Export ('000 tonnes)	1,322	1,013	890	*-5.2*	*-2.6*
Unit Value (sen/kg)	229	398	290	*11.7*	*-6.1*
Value (RM million)	3,028	4,038	2,581	*5.9*	*-8.6*
Sawlogs					
Production ('000 cu.m.)	40,099	32,200	26,922	*-4.3*	*-3.5*
Export ('000 cu.m.)	20,354	7,746	7,500	*-17.6*	*-0.6*
Unit Value (RM/cu.m.)	199	292	324	*8.0*	*2.1*
Value (RM million)	4,041	2,264	2,192	*-10.9*	*-0.6*
Sawn Timber					
Production ('000 cu.m.)	8,696	6,850	5,374	*-4.7*	*-4.7*
Export ('000 cu.m.)	5,222	4,367	2,953	*-3.5*	*-7.5*
Unit Value (RM/cu.m.)	587	879	1,030	*8.4*	*3.2*
Value (RM million)	3,065	3,839	3,042	*4.6*	*-4.5*
Cocoa					
Production ('000 tonnes)	247	152	156	*-9.3*	*0.5*
Export ('000 tonnes)	163	53	100	*-20.1*	*13.5*
Unit Value (RM/kg)	2.76	3.27	3.25	*3.5*	*-0.1*
Value (RM million)	449	172	325	*-17.4*	*13.6*
Mining					
Crude Oil					
Production (barrels/day)	623,000	705,500	695,000	*2.5*	*-0.4*
Export (barrels/day)	463,000	399,052	339,000	*-2.9*	*-3.2*
Unit Value (RM/tonne)	481	350	375	*-6.1*	*1.4*
Price (US$/barrel)	23.5	18.3	19.0	*-4.8*	*0.7*
Value (RM million)	10,639	6,701	5,792	*-8.8*	*-2.9*
LNG					
Production ('000 tonnes)	6,682	11,680	17,610	*11.8*	*8.6*
Export ('000 tonnes)	6,492	9,923	15,900	*8.9*	*9.9*
Unit Value (RM/tonne)	406	320	475	*-4.6*	*8.2*
Value (RM million)	2,635	3,171	7,553	*3.8*	*19.0*
Tin					
Production ('000 tonnes)	29.0	6.5	5.5	*-25.5*	*-3.3*
Export ('000 tonnes)	53.0	35.2	35.0	*-7.8*	*-0.1*
Unit Value (RM/tonne)	17.0	15.1	16.1	*-2.0*	*0.8*
Value (RM million)	902	545	564	*-9.6*	*0.7*
Manufactured Exports (RM million)	46,835	147,524	322,444	*25.8*	*16.9*
Other Exports (RM million)	3,631	6,740	11,398	*13.2*	*11.1*
Gross Export (RM million)	**79,646**	**185,325**	**363,768**	***18.4***	***14.4***

2.53 Given the anticipated strong performance of the economy, gross imports will grow at a double digit rate of 12.8 per cent per annum. Imports of investment goods and intermediate goods will continue to be major components. During the Seventh Plan period, measures will be instituted to address problems related to the structure of imports by encouraging domestic production of inputs that are currently being imported. In line with this policy of reducing imports, existing efforts to enhance domestic sourcing of inputs will be intensified by strengthening domestic linkages through Vendor Development Programmes and improving the capability of small- and medium-scale industries (SMIs). To enjoy the benefits of economies of scale, Malaysian manufacturers will also be encouraged to produce these goods for the export market. These efforts will further strengthen the merchandise account of the balance of payments. Imports of consumption goods are expected to grow moderately in line with the growth in domestic consumption and efforts to contain inflation as well as increase savings.

2.54 While Malaysia continues to trade with its traditional partners such as the ASEAN countries, Japan, the US, the EU, Taiwan, Hong Kong and South Korea, efforts will continue to be made to forge trade and other links with non-traditional trading partners and the newly emerging economies to take advantage of the increasing market opportunities. Within the ASEAN region, intra-ASEAN trade is expected to increase substantially with the implementation of the Common Effective Preferential Tariff (CEPT) as well as increased investment flows within the region as the advantages of a larger market become more evident. The efforts of member states in improving the macroeconomic environment and liberalizing their investment regimes will also have a positive effect on FDI inflows and intra-ASEAN trade. In addition, the implementation of the ASEAN Growth Triangles such as the Indonesia-Malaysia-Thailand Growth Triangle (IMT-GT), the Indonesia-Malaysia-Singapore Growth Triangle (IMS-GT) and the Brunei Darussalam-Indonesia-Malaysia-Philippines East ASEAN Growth Area (BIMP-EAGA) will further boost intra-ASEAN trade especially among the member states involved.

2.55 The liberalization of world trade will provide opportunities as well as pose challenges to Malaysian exporters. Malaysia will benefit through greater access to both developed and developing country markets as a result of reduced tariffs and subsidies, greater transparency in import regimes as well as strengthened rules and discipline in the multilateral trading system. The greatest challenge would be to remain competitive in the face of increasing competition from other producers through rationalizing production and improving efficiency and productivity. A wide range of trade promotion measures will be implemented to intensify the promotion of Malaysian exports. This will be facilitated by the formulation of strategic alliances with foreign companies. Public-private sector cooperation in the context of the Malaysia Incorporated Concept will be further strengthened. In addition, trade and industry associations are expected to assume a more significant role in promoting exports and information dissemination.

Balance of Payments

2.56 The merchandise account of the balance of payments is expected to register a higher surplus of 4.6 per cent of GNP compared with the surplus of 3.0 per cent achieved during the Sixth Plan period, due to the expected favourable performance of Malaysia's exports, as shown in *Table 2-8*. The current account, which is anticipated to be in deficit for most of the Plan period, is expected to turn around towards the end of the Plan period. This deficit will be due to the continuing large deficit in the services account which is estimated to average about 7.7 per cent of GNP. The strong growth of the merchandise account will, however, contribute to a surplus in the current account by the year 2000.

2.57 The continued large deficit in the overall services account will be due mainly to the repatriation of profits and dividends as a result of the large presence of foreign investment. In addition, increased freight and insurance payments as a consequence of the increase in trade and payments for contract and professional charges will also contribute to this deficit. Nevertheless, the projected surplus in the travel account is expected to reduce this deficit.

2.58 As the large deficit in the services balance is the main contributor to the current account deficit, the Government will continue to implement measures and strategies aimed at reducing this deficit. Among others, these measures include incentives for reinvestment, twinning programmes with foreign universities and encouraging exports on cost, insurance and freight (c.i.f.) and imports on free-on-board (f.o.b.) basis. Education will be developed as an export industry so as to make Malaysia into a regional educational centre. New strategies will include the promotion of exports of the services sector in areas such as finance, construction, engineering, architecture, estate management, privatization, recreation and tourism. Local banks will be encouraged to provide overseas investment credit to local companies for the opening of new branches overseas, especially

TABLE 2-8

BALANCE OF PAYMENTS, 1990-2000

Item	*RM million*			*% of GNP*			*Cumulative* *RM million*		*Cumulative* *% of GNP*	
	1990	*1995*	*2000*	*1990*	*1995*	*2000*	*6MP*	*7MP*	*6MP*	*7MP*
Merchandise Account	**7,093**	**630**	**25,876**	***6.4***	***0.3***	***7.5***	**23,480**	**64,727**	***3.0***	***4.6***
Exports	77,458	180,956	354,948	*69.9*	*89.4*	*103.2*	640,975	1,405,332	*80.8*	*99.3*
Imports	70,365	180,326	329,072	*63.5*	*89.1*	*95.7*	617,495	1,340,605	*77.8*	*94.7*
Services Account	**-9,723**	**-18,845**	**-24,479**	***-8.8***	***-9.3***	***-7.1***	**-78,482**	**-109,164**	***-9.9***	***-7.7***
Freight & Insurance	-3,837	-8,835	-7,521	*-3.5*	*-4.4*	*-2.2*	-30,204	-44,217	*-3.8*	*-3.1*
Other Transportation	-25	672	2,158	*-0.0*	*0.3*	*0.6*	555	7,215	*0.1*	*0.5*
Travel	632	4,900	3,964	*0.6*	*2.4*	*1.2*	11,310	27,213	*1.4*	*1.9*
Investment Income	-5,072	-11,208	-16,732	*-4.6*	*-5.5*	*-4.9*	-43,423	-73,446	*-5.5*	*-5.2*
Government Transactions	-3	-45	-60	*-0.0*	*-0.0*	*-0.0*	-154	-114	*-0.0*	*-0.0*
Other Services	-1,418	-4,329	-6,288	*-1.3*	*-2.1*	*-1.8*	-16,566	-25,815	*-2.1*	*-1.8*
Transfers	**147**	**400**	**439**	***0.1***	***0.2***	***0.1***	**1,537**	**2,085**	***0.2***	***0.1***
Current Account	**-2,483**	**-17,815**	**1,836**	***-2.2***	***-8.8***	***0.5***	**-53,465**	**-42,352**	***-6.7***	***-3.0***
Capital Account										
Official Long-term Capital	-2,836	5,569		*-2.6*	*2.8*		3,487		*0.4*	
Corporate Investment	6,309	10,000		*5.7*	*4.9*		58,494		*7.4*	
Overall Balance	**5,365**	**-4,403**		***4.8***	***-2.2***		**36,745**		***4.6***	
Central Bank Reserves	27,025	63,770		*24.4*	*31.5*		57,205		*5.3*	
Months of Retained Imports	4.1	4.0					5.3			

in new markets in the South countries, as well as enter into bilateral agreements and economic relationships with overseas banks. Similarly, large and specialized foreign reinsurance companies will be encouraged to operate in Malaysia. The introduction of the electronic data interchange and multi-modal transportation will improve port clearance and haulage facilities in order to increase efficiency.

Terms of Trade

2.59 The terms of trade is expected to improve during the Plan period as export prices are envisaged to be higher than import prices. With improvements in the quality of exports and the anticipated stable exchange rate, export prices are expected to increase by 3.1 per cent per annum as against the growth of 2.8 per cent for import prices. The expected favourable export prices will increase export earnings during the Plan period. Improvements in the terms of trade will increase real purchasing power by 8.5 per cent per annum.

Price Development

2.60 With greater focus given to efforts at ensuring price stability, inflation is projected to be low. Supply-side measures as well as import liberalization will ensure that the supply of goods and services will be able to meet demand. This implies that the current constraints, especially in the supply of food items, will be overcome. The greater liberalization of the criteria for the drawdown of the Fund for Food scheme is expected to accelerate and increase domestic food production. Such efforts will also contribute towards lowering imports and this will in turn help improve the trade balance. In addition, the Government will continue to adopt a tight monetary policy complemented by a prudent fiscal policy. The monetary aggregates will be closely monitored to ensure that money supply will not be a source of inflation. At the same time, fiscal restraints will include a better control on expenditure as well as selective expenditure on development projects that will alleviate infrastructural and supply constraints. Some of these projects will be implemented through privatization. Similarly, the effective rate of protection will be reduced through the gradual reduction or abolishment of tariffs, in line with greater trade liberalization commitments under AFTA and WTO.

2.61 Measures will be undertaken to encourage automation and labour-saving techniques as well as encourage higher female participation in the labour force in order to moderate labour demand pressures and contain wage increases. Productivity gains that surpass wage increases will be encouraged to ensure that unit labour costs and eventually prices will not rise. The quality of services provided by the public sector will also be improved to facilitate private sector efficiency.

2.62 The Government's anti-inflationary campaign will continue to include various administrative measures such as the enforcement of price-tagging and the prevention of restrictive trade practices. Better information on prices will be provided so as to increase consumer awareness as well as educate the public on their role in the fight against inflation. At the same time, a separate CPI for the low-income group will be developed to facilitate the monitoring of price developments and appropriate measures will be instituted to maintain the purchasing power for this category of consumers.

2.63 Nevertheless, the long term objective of the Government is to achieve zero inflation with respect to basic necessities such as food, clothing, shelter and transportation which have a high weightage in the basket of goods of the lower-income group. The prices of these items will be monitored closely to ensure that the prices of these basic essentials will not increase. However, in the process of achieving zero inflation, the Government will restrain the increased use of price controls which can distort the market.

Resource Balance

2.64 The resource position is expected to be stronger during the Seventh Plan period. Gross national savings will average 34.9 per cent of GNP compared with 32.5 per cent during the Sixth Plan period. Private savings will account for 24 per cent of GNP, while public savings will account for 10.9 per cent, as shown in *Table 2-9*. Further sophistication of the capital market with innovative saving instruments and institutions will be prerequisites to the achievement of this high savings rate. However, the share of gross investment to GNP during the Plan period is expected to decline to 37.9 per cent from 39.2 per cent in the Sixth Plan, resulting in a narrower resource gap of 3.0 per cent of GNP. This gap will be financed through inflows of foreign capital.

TABLE 2-9

RESOURCE BALANCE, 1990-2000
(% of GNP)

				Cumulative	
Sector	*1990*	*1995*	*2000*	*6MP*	*7MP*
Public					
Savings	*12.7*	*15.5*	*9.1*	*14.0*	*10.9*
Investment	*12.0*	*14.4*	*9.6*	*13.2*	*10.7*
Resource Balance	***0.7***	***1.1***	***–0.5***	***0.8***	***0.2***
Private					
Savings	*17.8*	*18.7*	*27.4*	*18.5*	*24.0*
Investment	*20.7*	*28.6*	*26.4*	*26.0*	*27.2*
Resource Balance	***–2.9***	***–9.9***	***1.0***	***–7.5***	***–3.2***
Total					
Savings	*30.5*	*34.2*	*36.5*	*32.5*	*34.9*
Investment	*32.7*	*43.0*	*36.0*	*39.2*	*37.9*
Resource Balance	***–2.2***	***–8.8***	***0.5***	***–6.7***	***–3.0***

2.65 The public sector resource position is expected to show a balance during the Seventh Plan period. The Federal Government account is expected to improve with a better overall surplus position of 0.4 per cent of GNP, due to enhanced revenue performance following the continued high economic growth and improvements in tax administration. The NFPEs are expected to improve further their economic performance with emphasis on quality investments and modernization as well as concentration on productivity and quality enhancements. These efforts will place them in a stronger position to record higher current surpluses.

Public Sector Account

2.66 With the forecasted surplus position in its overall account during the Seventh Plan period, the Federal Government will be able to finance its development expenditure of RM67.5 billion or 4.8 per cent of GNP. Without the Federal Government resorting to borrowing from the financial system, more resources will be made available for private sector investment. With the expected improvements in the financial position of the NFPEs, the public sector overall account will register a surplus of 0.2 per cent of GNP. The total development expenditure for the consolidated public sector is RM162.5 billion, as shown in *Table 2-10*. This level of expenditure will not crowd out the financial resources of the private sector.

TABLE 2-10

CONSOLIDATED PUBLIC SECTOR DEVELOPMENT EXPENDITURE, 1990-2000

Item	*RM million*			*% of GNP*			*Cumulative*				*Average Annual Growth Rate (%)*	
							RM million		*% of GNP*			
	1990	*1995*	*2000*	*1990*	*1995*	*2000*	*6MP*	*7MP*	*6MP*	*7MP*	*6MP*	*7MP*
General Government	**10,076**	**17,107**	**17,894**	*9.1*	*8.5*	*5.2*	**68,691**	**87,500**	*8.7*	*6.2*	*11.2*	*0.9*
Federal	4,472	10,392	13,854	*4.0*	*5.1*	*4.0*	39,310	67,500	*5.0*	*4.8*	*18.4*	*5.9*
States	3,057	4,016	2,434	*2.8*	*2.0*	*0.7*	16,355	12,046	*2.1*	*0.8*	*5.6*	*-9.5*
Statutory Authorities	2,218	1,664	982	*2.0*	*0.8*	*0.3*	9,594	4,874	*1.2*	*0.3*	*-5.6*	*-10.0*
Local Governments	329	1,035	625	*0.3*	*0.5*	*0.2*	3,432	3,081	*0.4*	*0.2*	*25.8*	*-9.6*
NFPEs	**4,511**	**16,320**	**16,390**	*4.1*	*8.1*	*4.8*	**48,967**	**75,000**	*6.2*	*5.3*	*29.3*	*0.1*
Total	**14,587**	**33,427**	**34,284**	*13.2*	*16.5*	*10.0*	**117,658**	**162,500**	*14.8*	*11.5*	*18.0*	**0.5**

IV. CONCLUSION

2.67 During the Sixth Plan period, the Malaysian economy performed remarkably well. With macroeconomic management focusing on strengthening the foundations of the economy and the strategic shift to productivity-driven growth, the performance of the Malaysian economy will continue to be robust during the Seventh Plan period. The expansion of the economy will be broad-based, emanating from the manufacturing, services and construction sectors. Output from the agriculture sector will improve with new sources of growth, while the increased production of gas will boost the growth of the mining sector. Concerted efforts to improve the current account position in the balance of payments are expected to result in a surplus position by the end of the Plan period. On the demand side, the performance of the economy will be buoyed by strong domestic demand and sustained world economic growth. Inflation will continue to be maintained at a low level through various efforts by all sectors of the economy to ensure high growth with price stability.

2.68 High domestic investment with continued foreign investment and the improved quality of human resources will contribute to the overall performance of the economy. Simultaneously, the improved quality of Malaysian products and the increased liberalization of international trade will further boost Malaysia's export performance. The development of a globally-linked information industry will facilitate the availability and transmission of information that will further enhance Malaysia's competitiveness.