

CHAPTER 2

ECONOMIC OUTLOOK 2005

2.1 The World Economy

The global economy is forecasted to grow at a slower pace of 4.3 per cent in 2005 and 4.1 per cent in 2006 from 5.0 per cent in 2004. This is due to an anticipated slower growth of the US economy.

The US economy is forecasted to expand at a slower but more sustainable pace in 2005 and 2006 resulting from some expenditure adjustments to addresses the problem of its current budget deficit. With interest rate on the upward trend in the US, its domestic consumption is expected to soften due to tight savings.

The huge US current account deficit has also weakened the US dollar against the Euro and the Yen. The resulting strengthening of Euro and Yen will somewhat adversely hurt the European and Japanese economies that are both export oriented. On the other front, China's slowdown is expected in 2005 as the Government's efforts to engineer a soft-landing of its economy takes effect.

A softening in global semiconductor sales following a rapid growth in 2004 is expected to further put a downward pressure on the global growth prospect. Pressure from oil price hike experienced in late 2004 is likely to sustain its stifling effect on the growth of the world economy at least in the medium term.

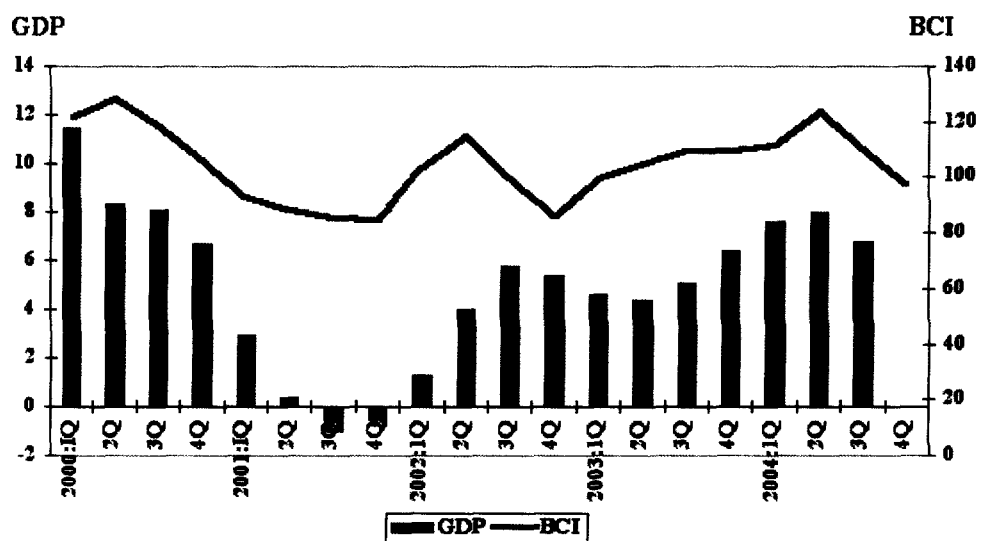
2.2 The Malaysian Economy

The Malaysian economy is expected to register a slower growth of 6% in 2005, compared to 7% in 2004. Inflation is expected to increase by 2.3% in 2005 compared to a growth of 1.4% in 2004 due to the lagged effects of higher energy prices and business cost. While the Malaysian interest rate is still in its low regime, interest rate is expected to increase at least by 25 basis points in tandem with the increase in US interest rate and possible increase in inflation rate.

As the pace of expansion in industrial countries moderates, Malaysia's export performance may cool down, while FDI inflows could be affected as well. Outlook for the overall business sector in 2005 may not be bullish due to the decrease in government infrastructure spending and signs of slowdown in the global economy. This can be observed in the declining trend of the Business Confidence Index (BCI) since the 2nd quarter of 2004 in Figure 2.1 below:

Figure 2.1
Malaysian GDP vs BCI

Source: Malaysian Institute of Economic Research (MIER)



On the other hand, consumer spending is expected to at least continue its momentum into 2005 from the previous, as evident in the Malaysian Consumer Sentiments Index (CSI) trend in the following Figure 2.2:

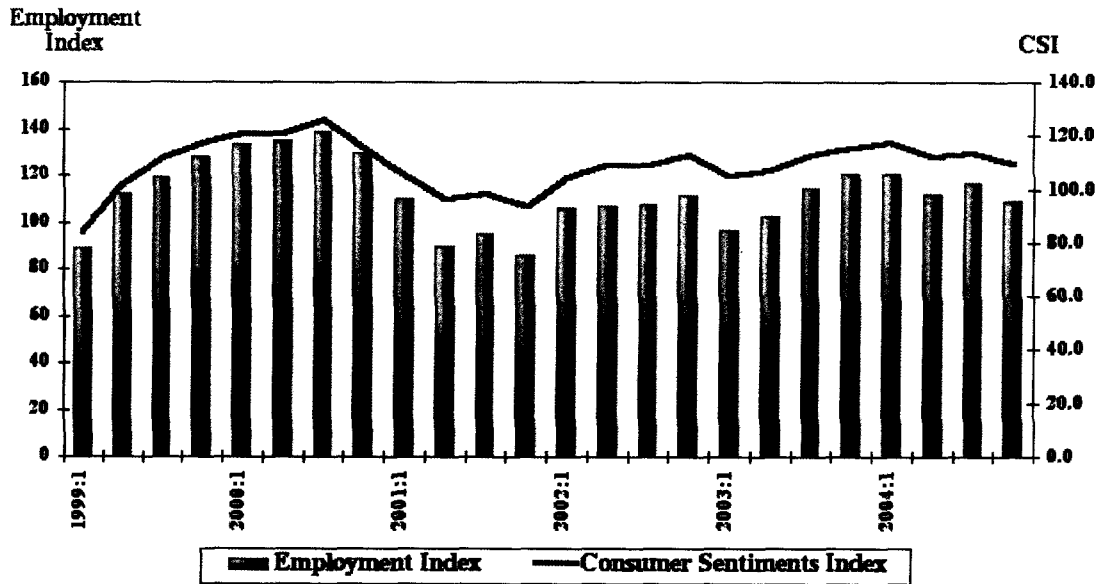


Figure 2.2
Malaysian Employment Index vs CSI
Source: Malaysian Institute of Economic Research (MIER)