

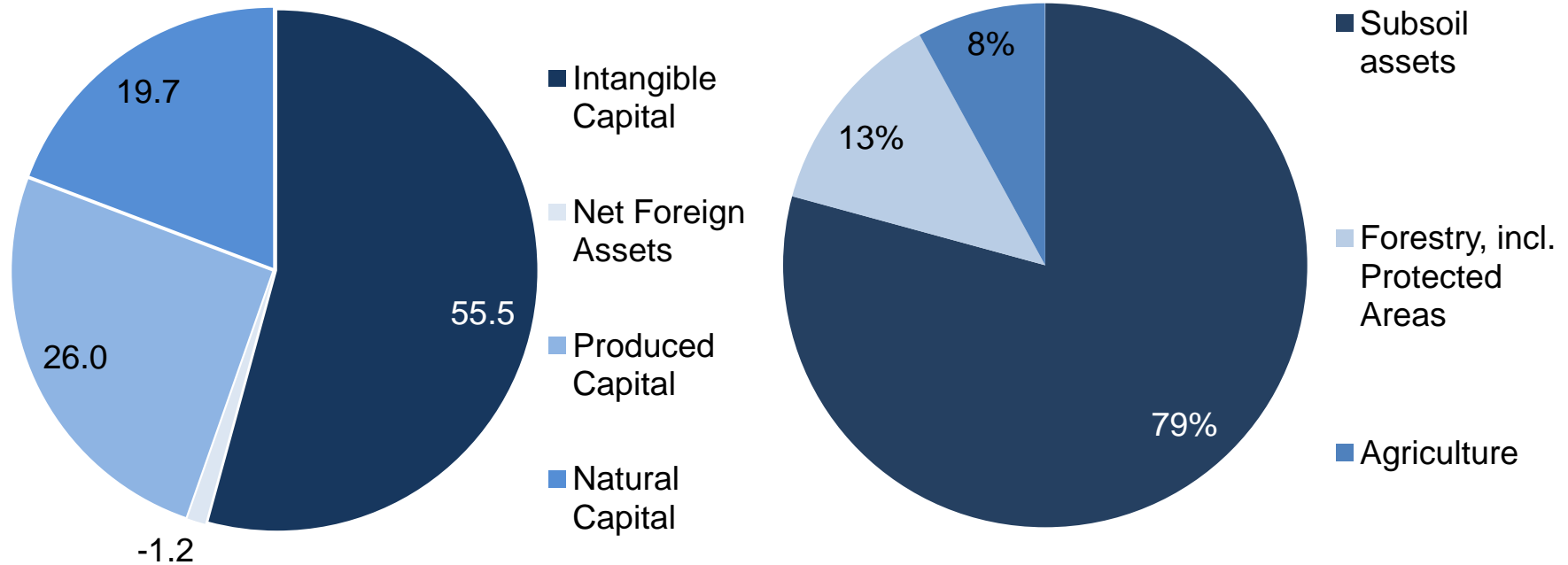


**Malaysia's Experience in
Harnessing Natural Resources**



Malaysia is rich in natural resources

Composition of Malaysia's national wealth, 2005



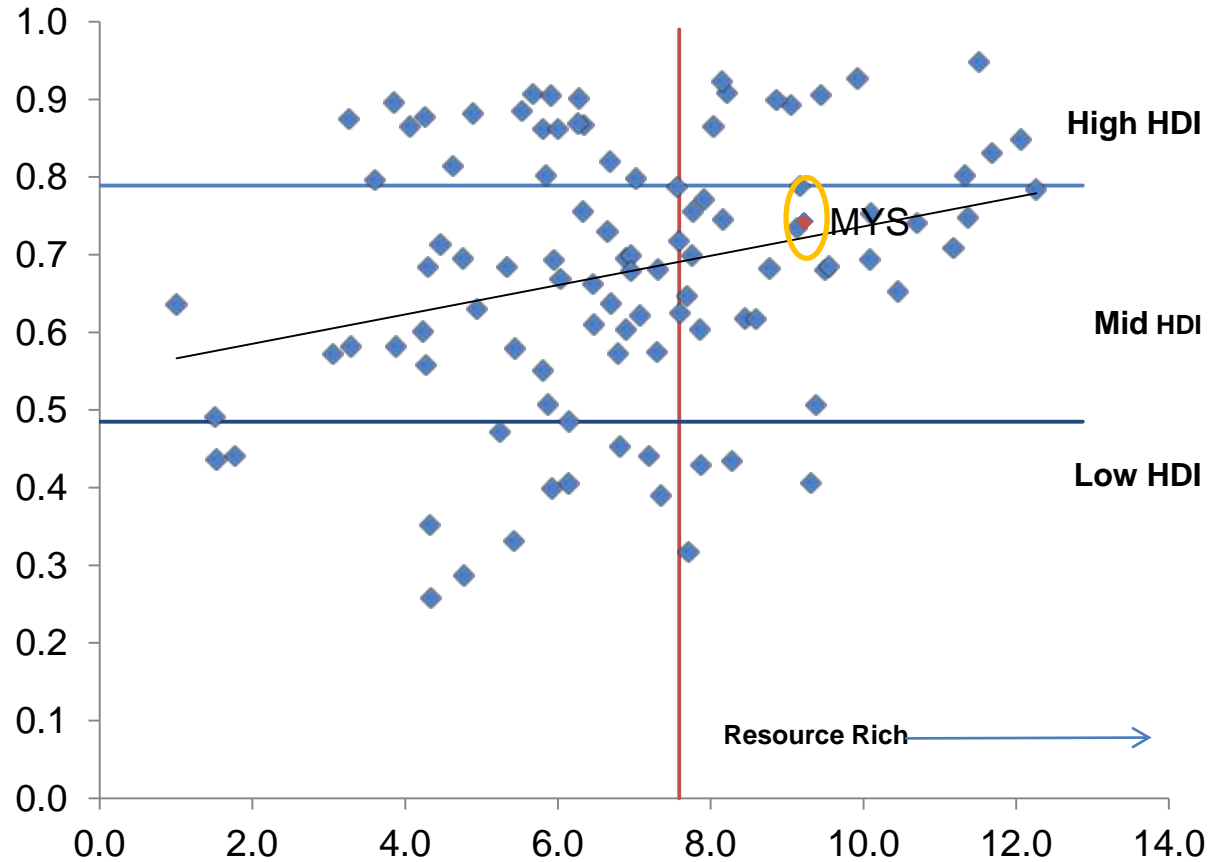
Source: World Bank, *The Changing Wealth of Nations: Measuring Sustainable Development in the New Millennium*.



Malaysia is a success story in harnessing natural resources for development

Human Development Index (2005), vertical axis;

Log of subsoil resources per capita (2005), horizontal axis

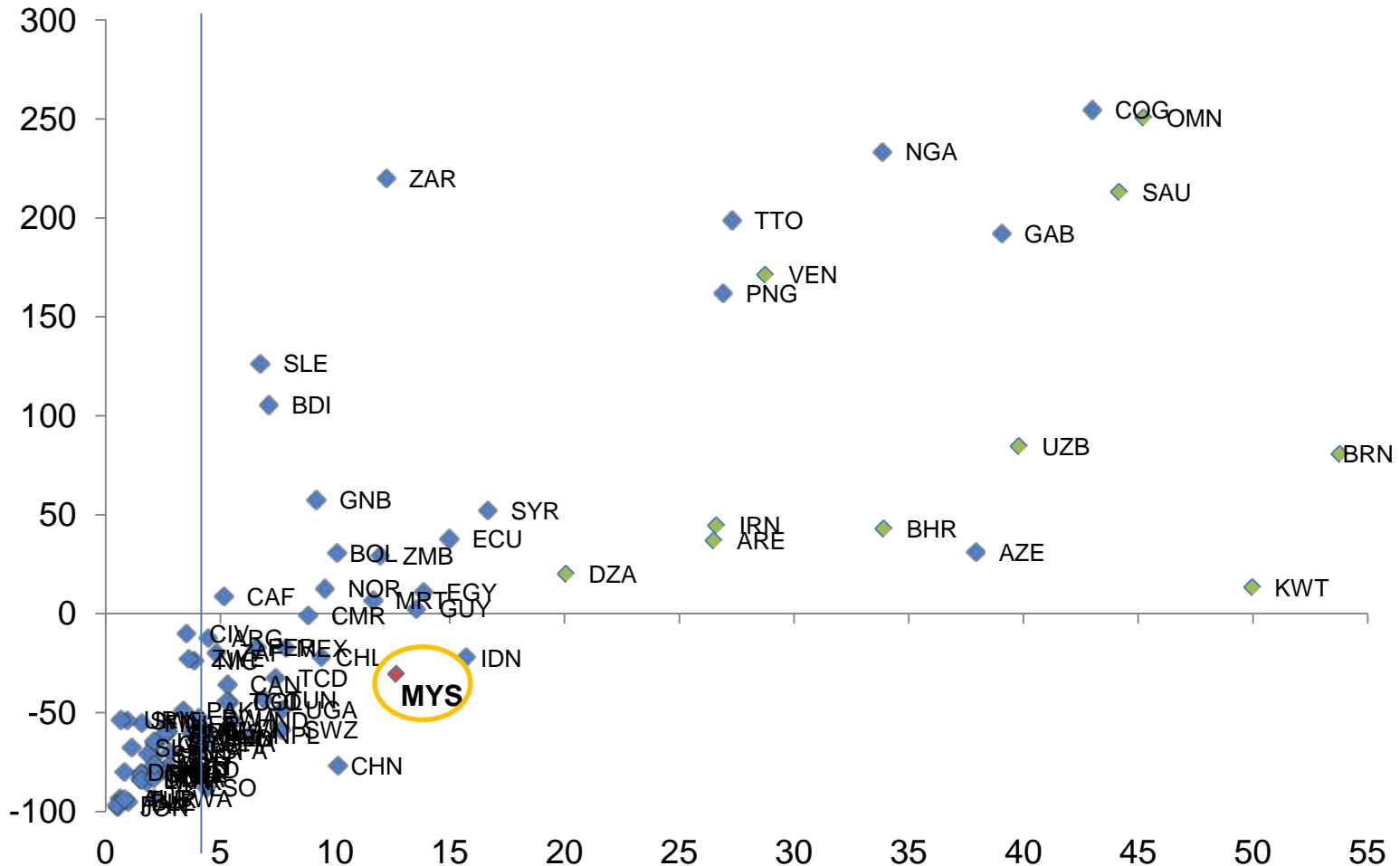


Source: World Development Indicators, World Bank staff calculations.



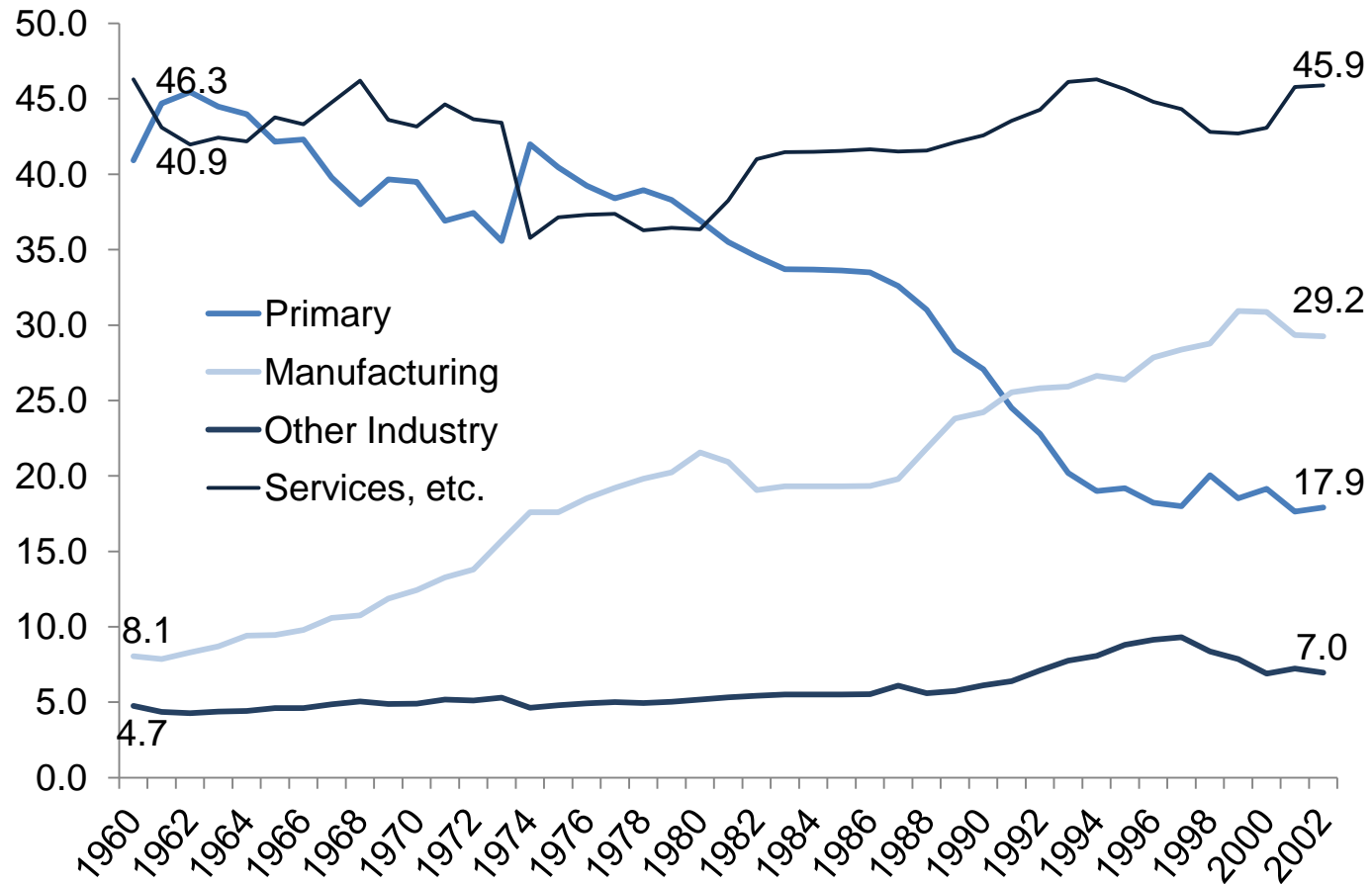
Resource revenues were invested, not consumed

Increase in produced capital if Hartwick Rule followed, percent, vertical axis;
Total natural resource rents as a share of GDP, 1970-2005 average, percent, horizontal axis



The economy diversified

Sectoral shares in GDP, percent

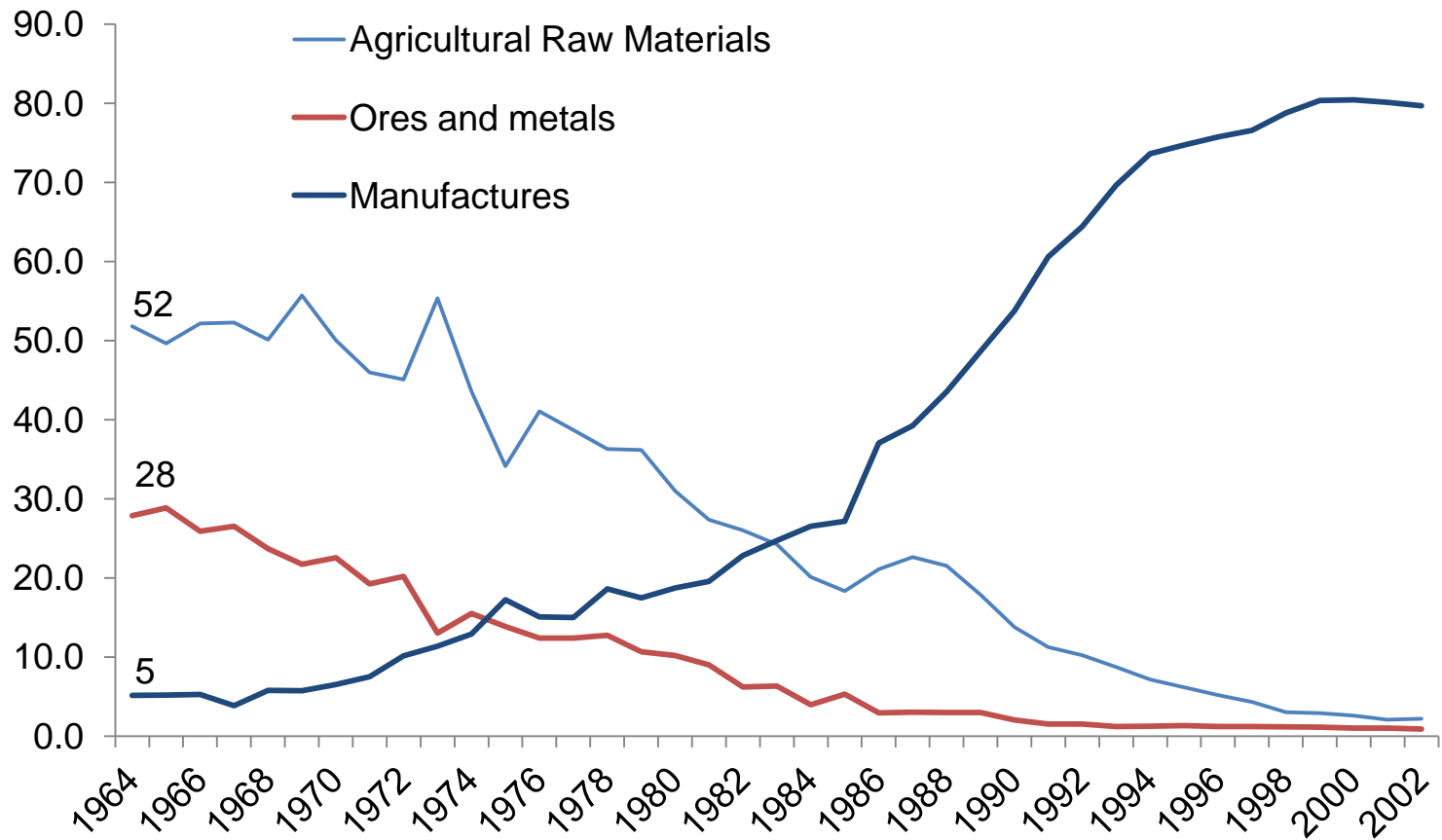


Source: World Development Indicators



The export basket diversified

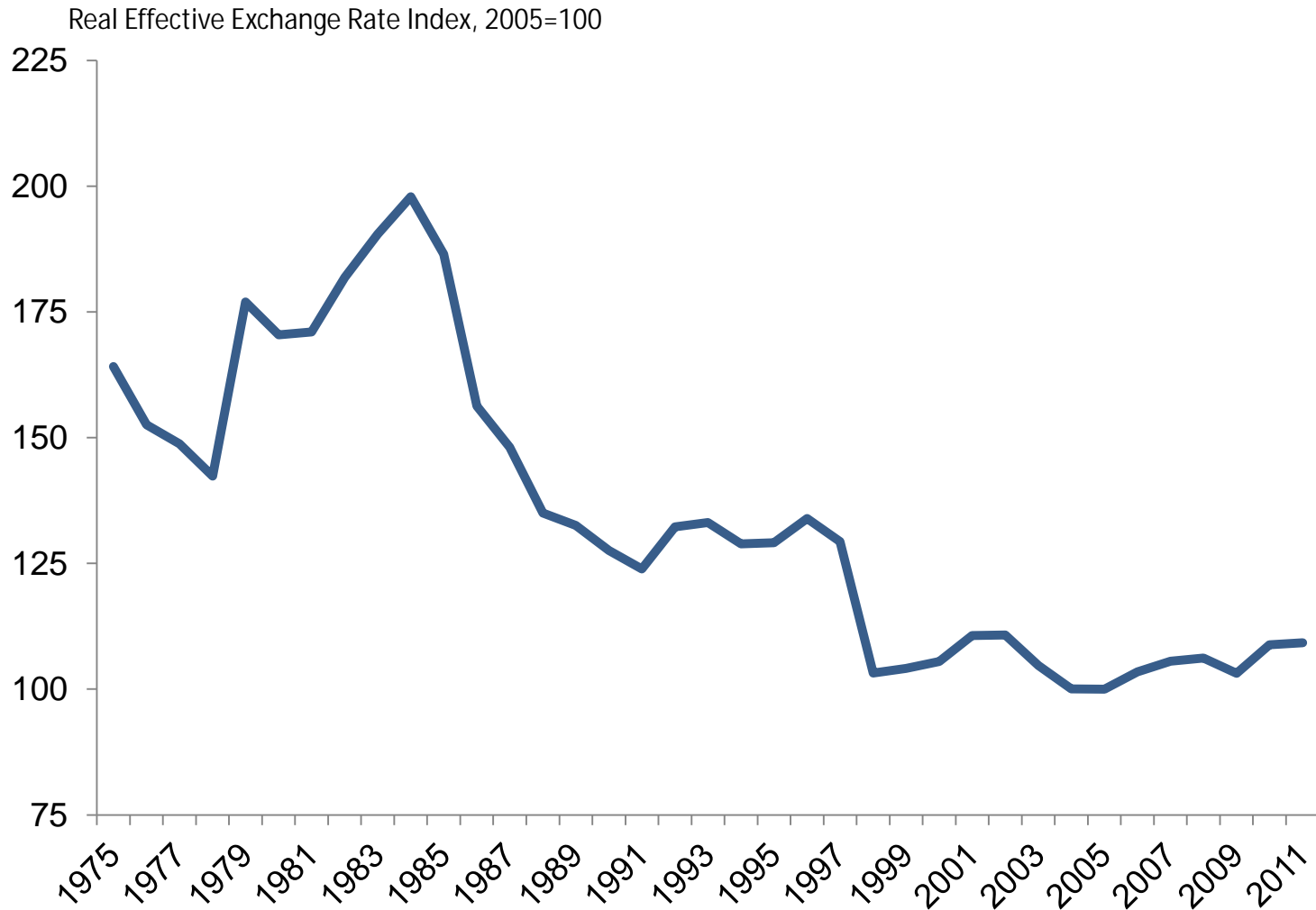
Sectoral shares in exports, percent



Source: World Development Indicators



No Dutch Disease

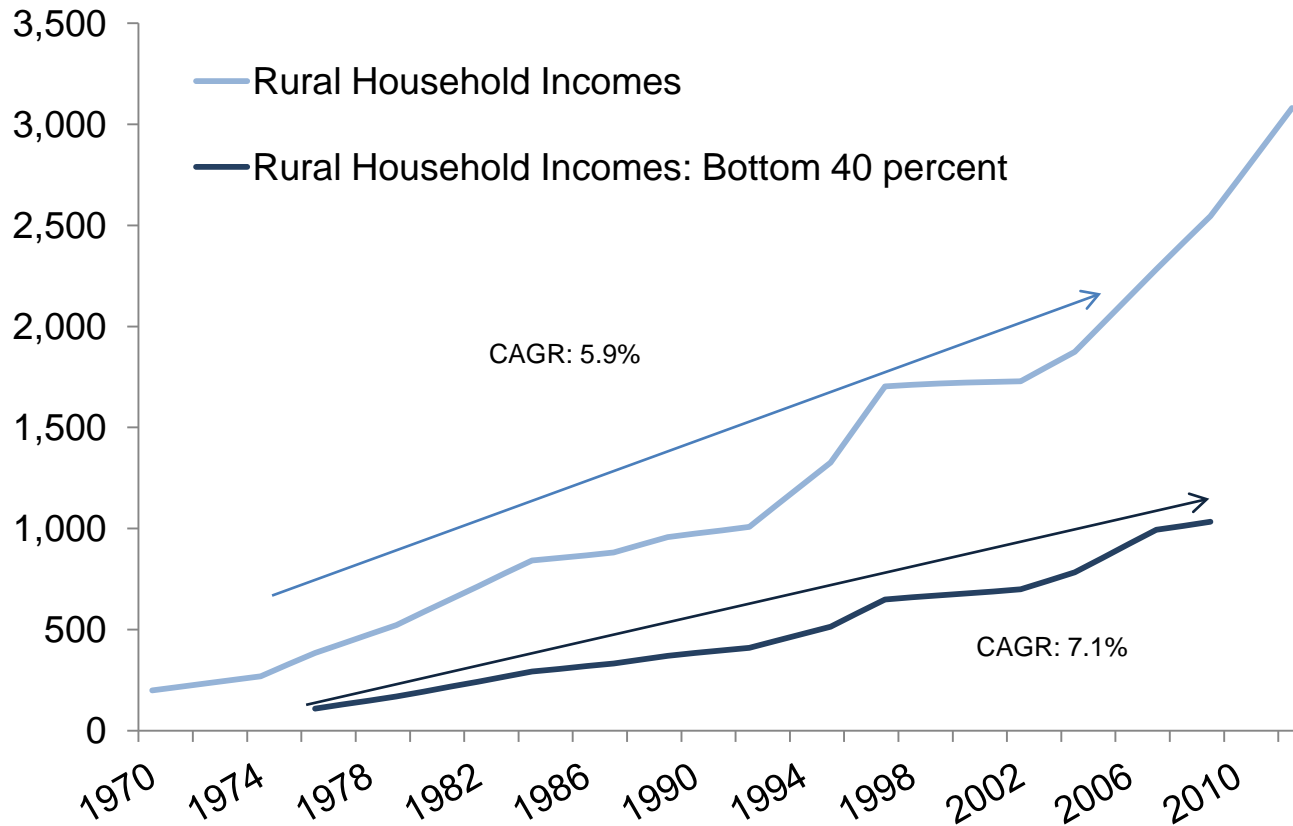


Source: World Development Indicators, World Bank staff calculations



Benefits from growth were widely shared

Rural household incomes, RM per month



Source: CEIC, Department of Statistics, Malaysia, World Bank staff calculations



How did Malaysia do it?

- ü Malaysia pro-actively diversified the asset-base of the economy
 - ü Export & GDP diversification = flow
 - ü *Asset diversification* = stock (natural resources, human capital, infrastructure, etc.)
 - ü Both sector-specific and economy-wide policies played a role

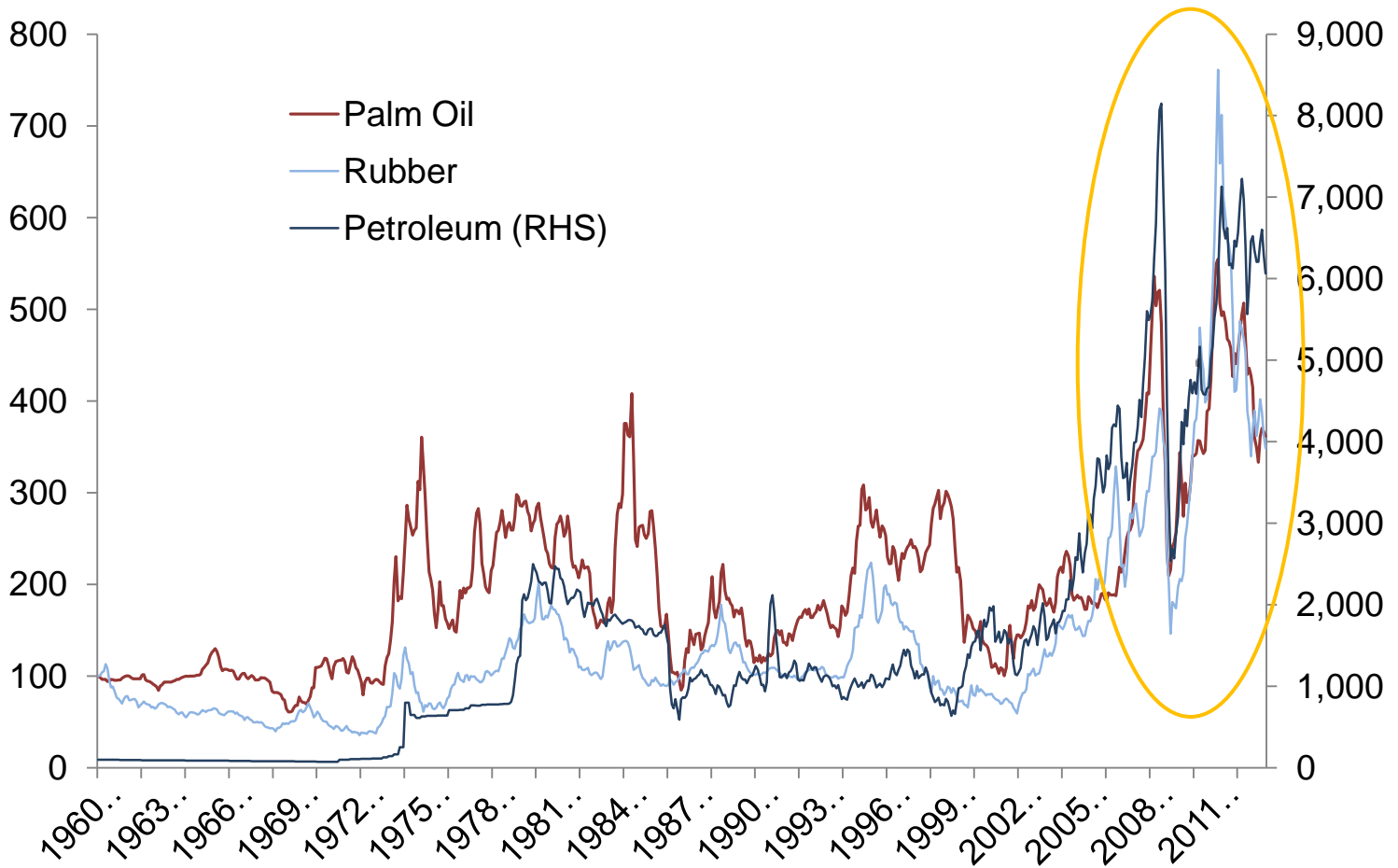
- ü PETRONAS as an effective 'resource fund'

- ü Social policies were supportive of income-gains by low-income households



Higher prices bring new challenges

Index, Jan 1960=100, both axes

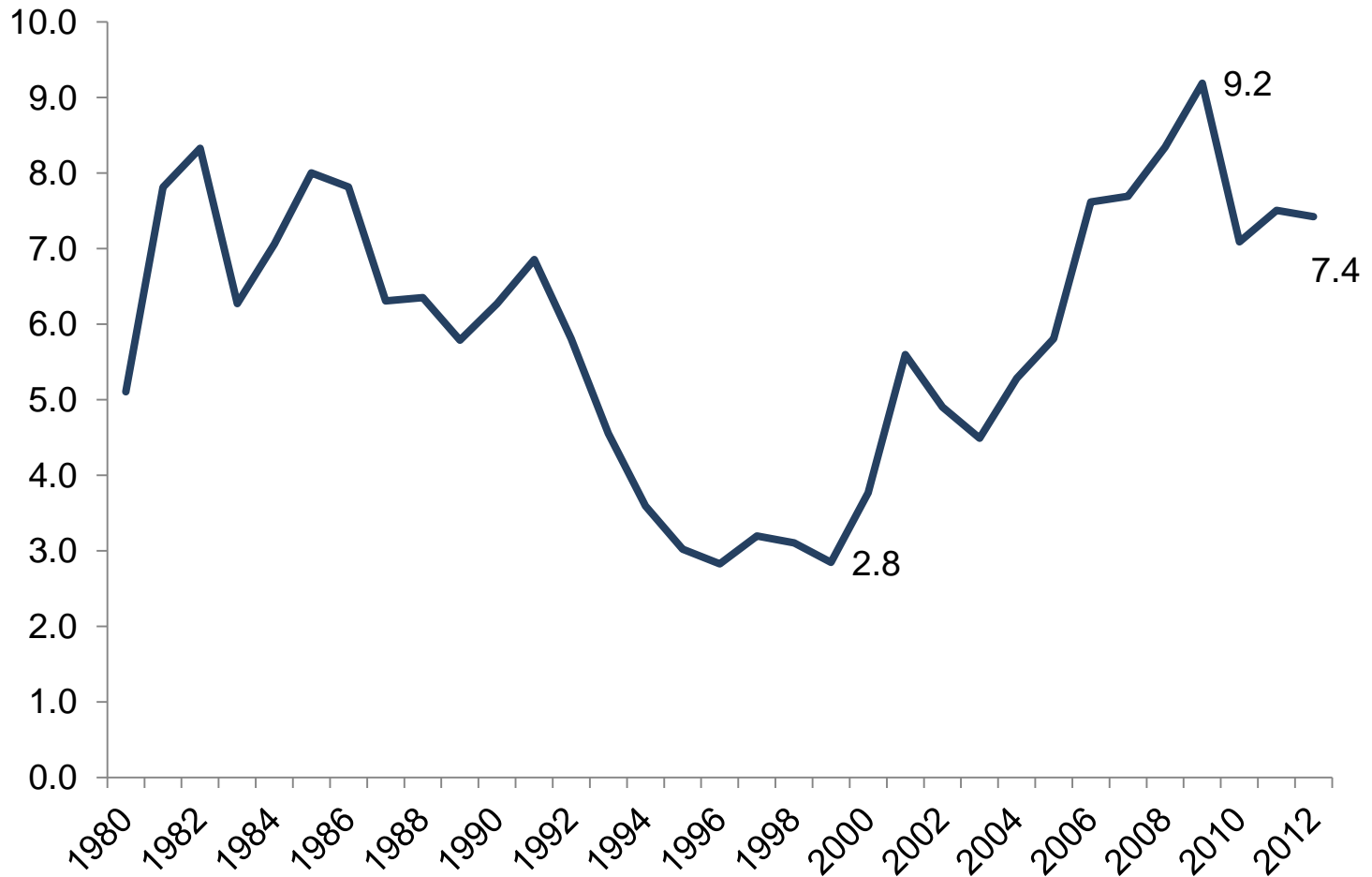


Source: World Bank DECPG, World Bank staff calculations



Higher oil prices has made fiscal revenues more commodities-dependent

Oil revenues in the Budget as a share of GDP, percent



Source: Accountant General's Department



More revenues spent on consumption by the public sector...

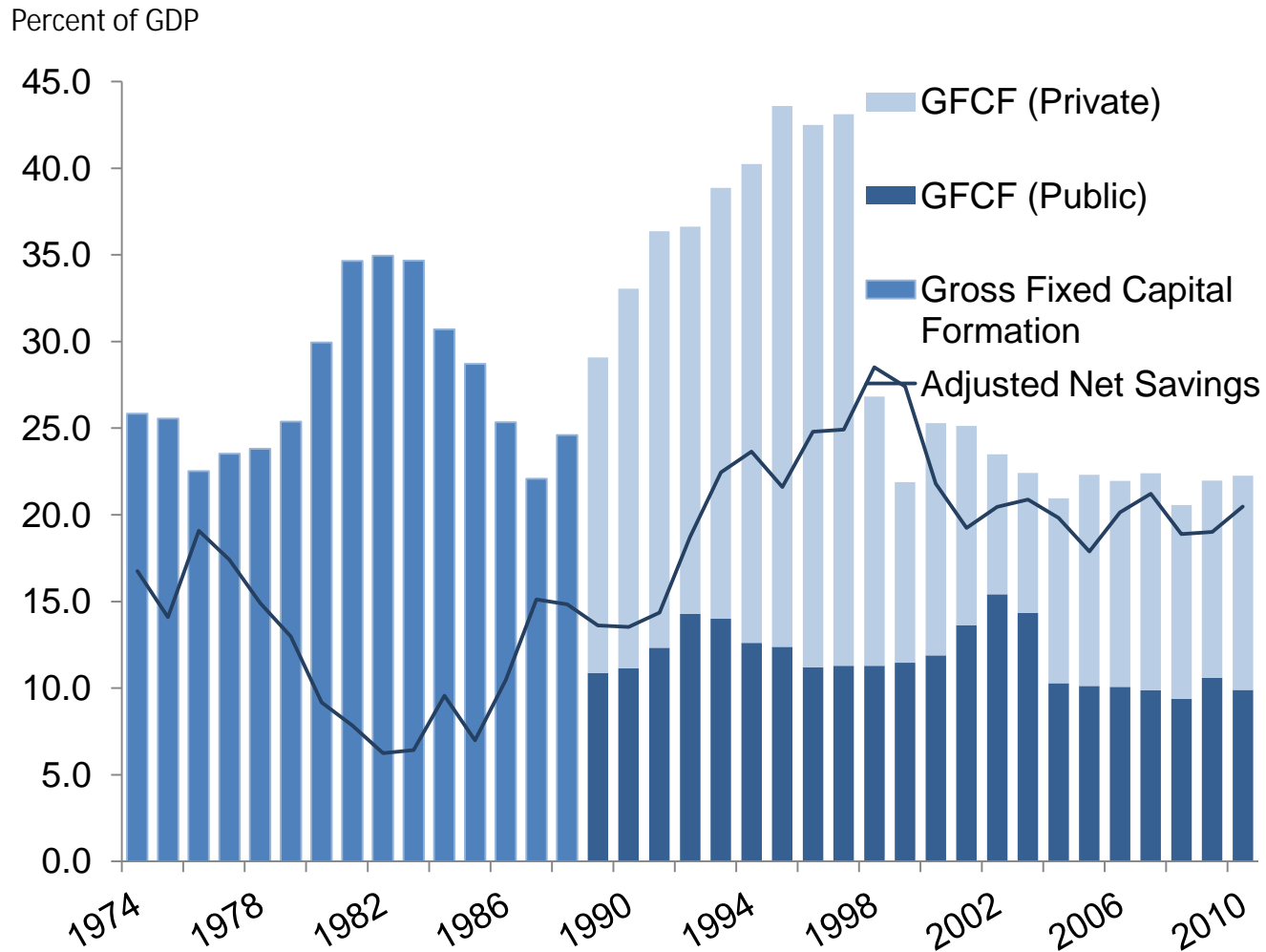
Fiscal dependence on oil revenues has increased sharply since 2000

	1990-1994	1995-1999	2000-2004	2005-2009	2010-2012	2010-2012 vs...	
						1990-1994	2000-2004
Emoluments, Pensions and Gratuities	7.6	6.3	6.3	6.5	7.5	-0.1	1.2
Fuel Subsidies	0.1	0.1	0.6	1.5	2.1	2.1	1.5
Other Operating Expenditure	12.1	9.7	11.0	11.5	11.0	-1.1	0.0
Net Development Expenditure	5.7	5.8	8.1	5.8	5.4	-0.3	-2.7
Oil Revenues	5.2	3.0	4.8	7.8	7.3	2.1	2.5
Non-Oil Revenues	19.9	18.6	16.2	13.1	13.8	-6.1	-2.4
Deficit Financing	-0.3	-0.3	-5.0	-4.3	-4.9	-4.6	0.1
Non-Oil Primary Deficit	-1.0	-0.7	-7.3	-10.2	-10.2	-9.2	-2.9
All Expenditures	25.4	21.9	26.0	25.2	26.0	0.6	0.1

Source: MoF, CEIC, World Bank staff calculations



... and private sector, since investment rate lower even as non-oil revenues declined

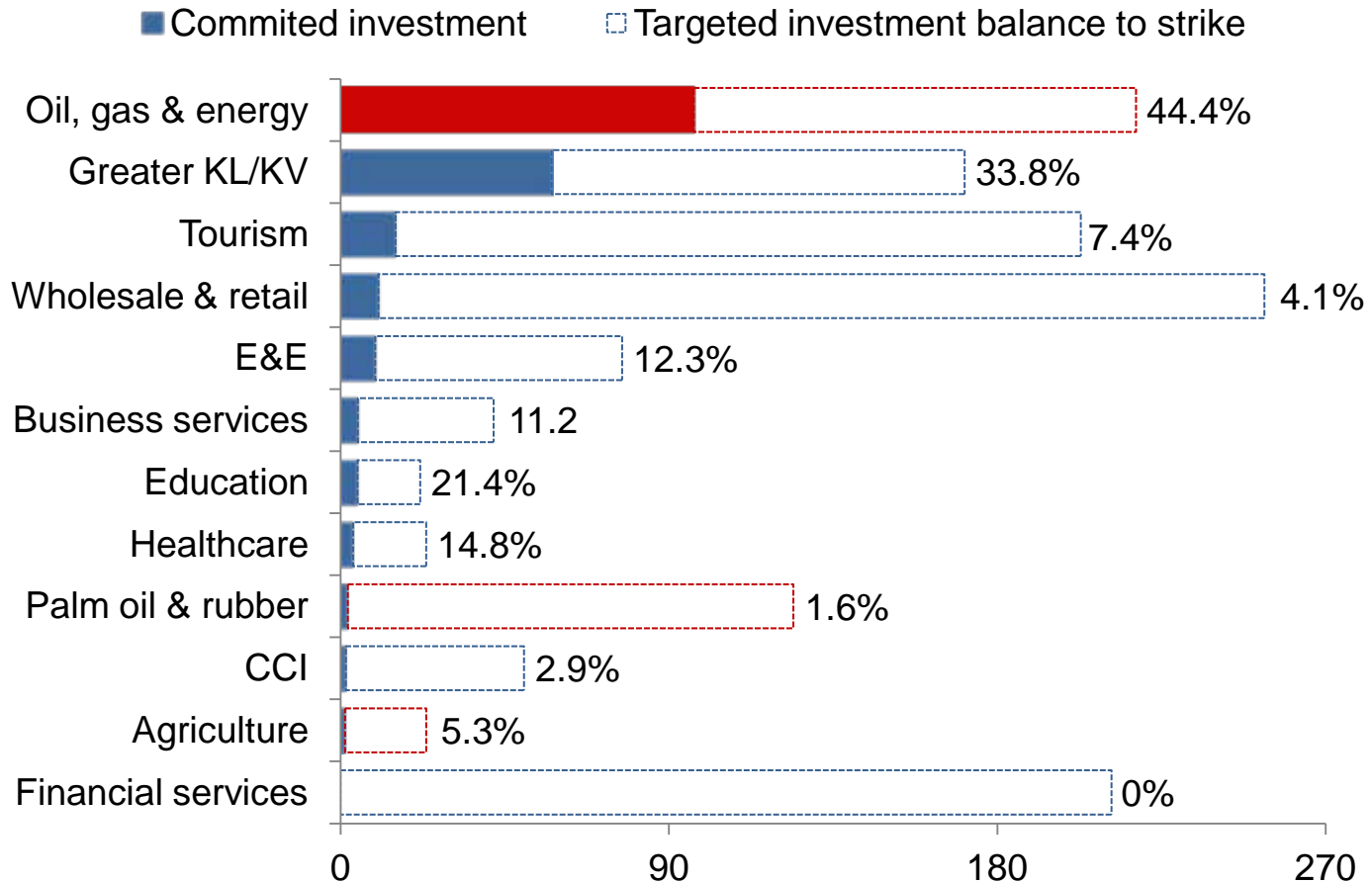


Source: World Development Indicators and World Bank staff calculations



Investments picked up in 2011 and 2012, but mostly in commodity sectors

NKEA Investments, RM billion

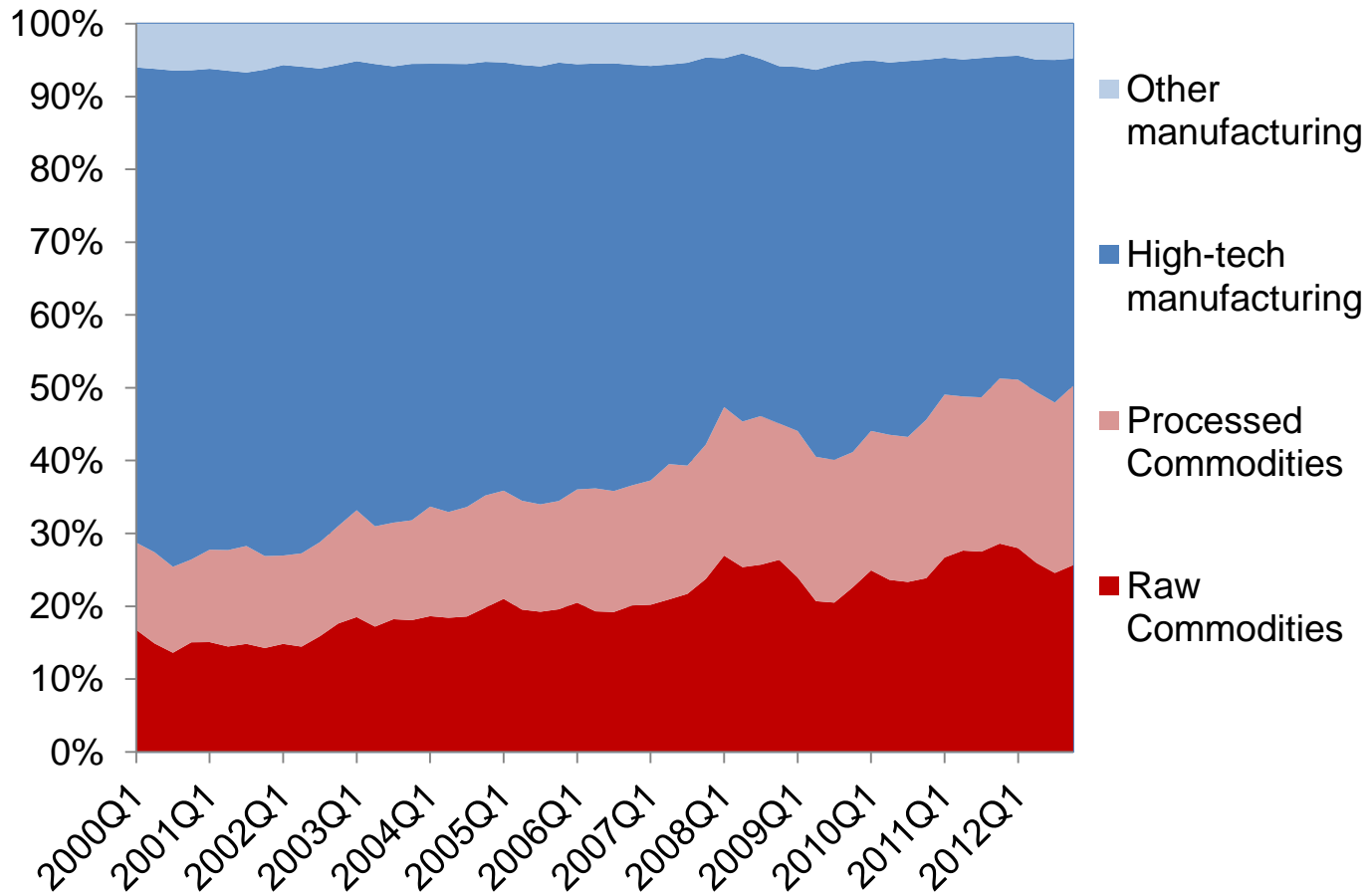


Source: PEMANDU



Higher prices has also made the export basket more commodities-dependent...

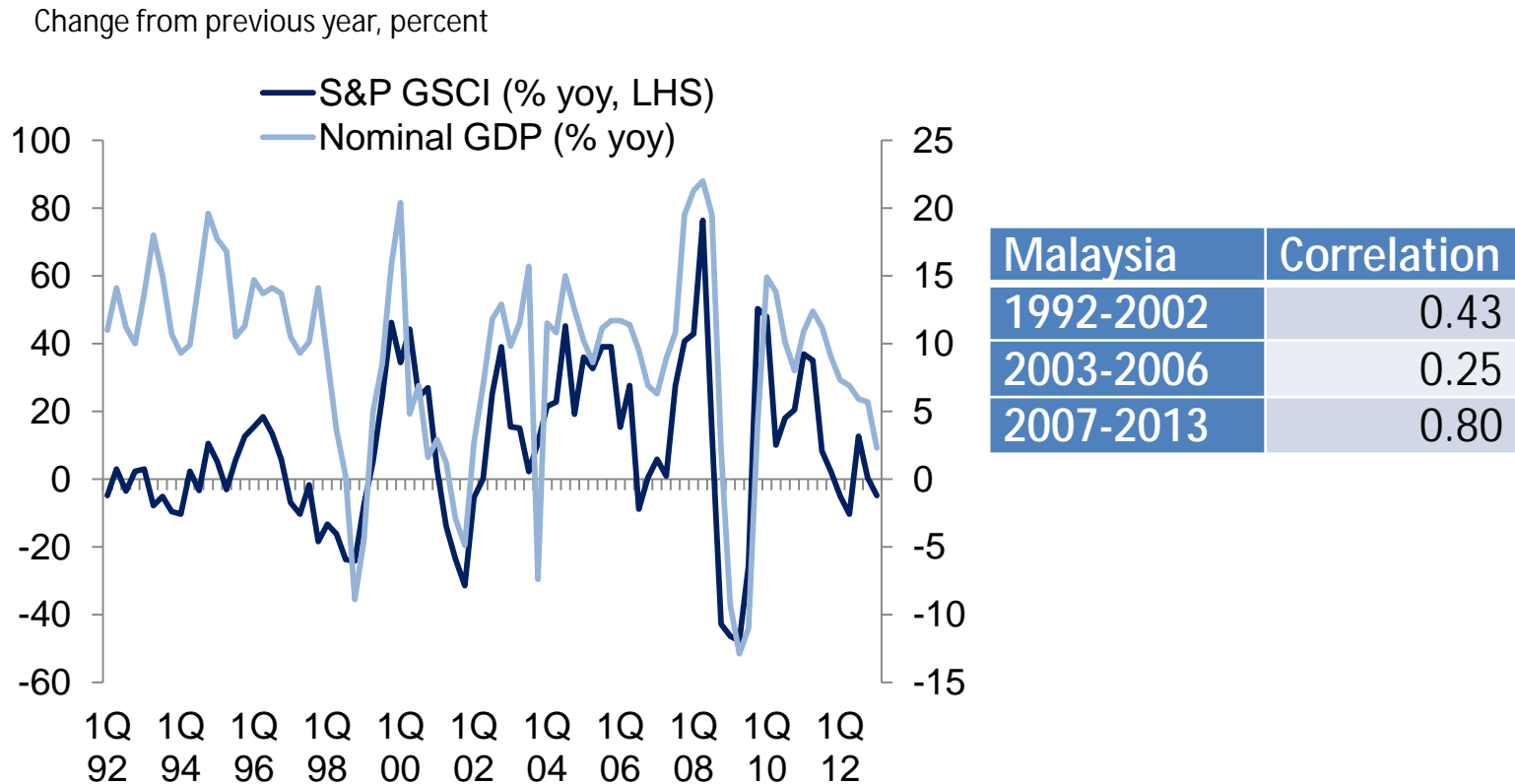
Share of total exports of goods, percent



Source: CEIC and World Bank staff calculations.



Economic performance became more strongly correlated with commodity prices

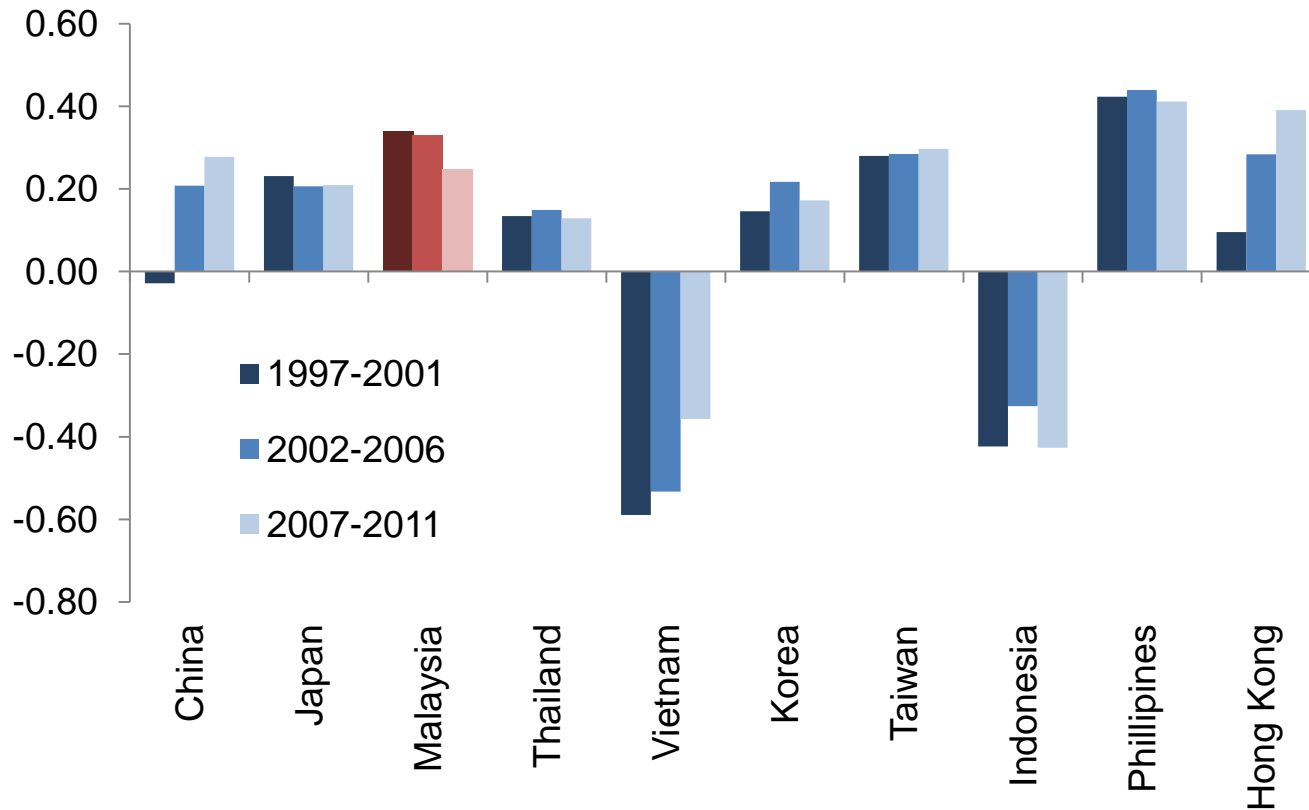


Source: Haver Analytics and World Bank staff calculations.



Competitiveness of E&E appears to have declined

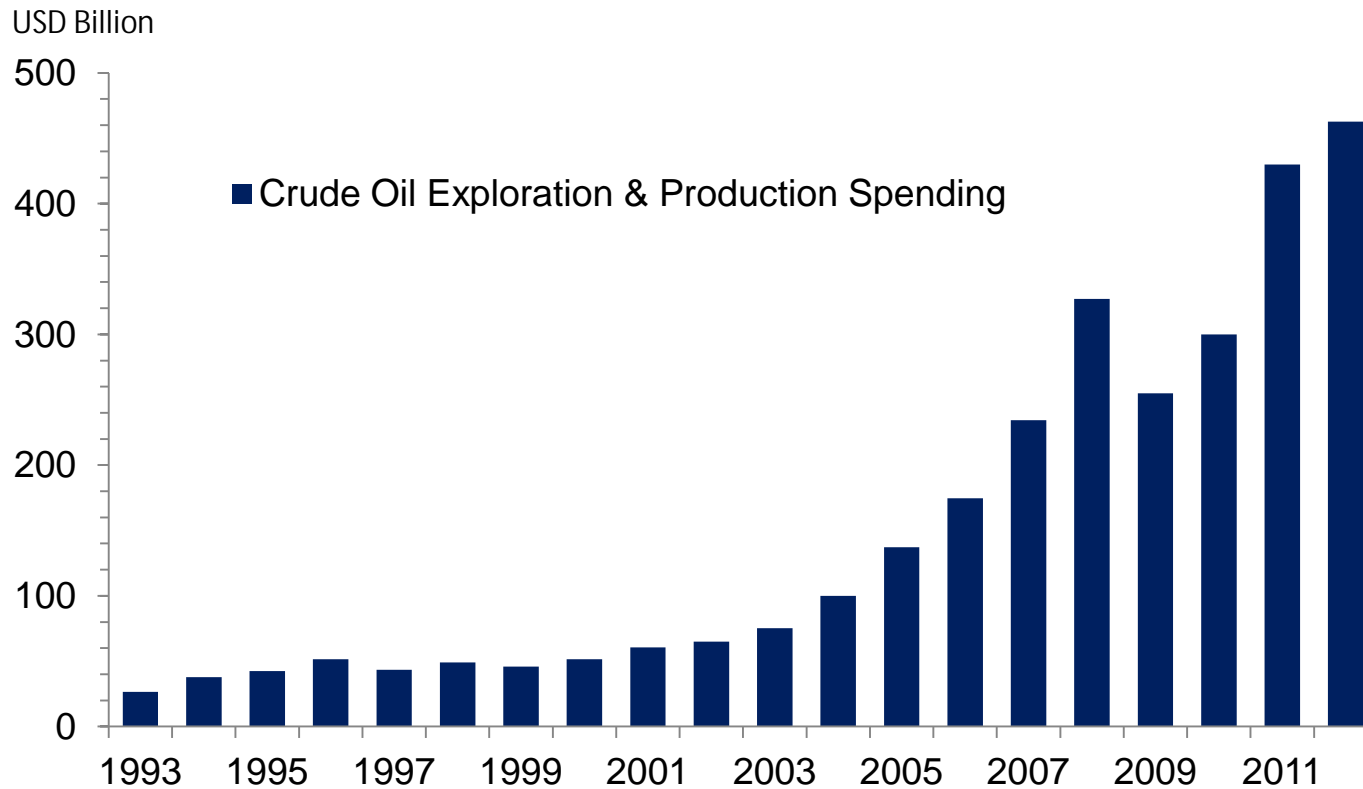
Revealed Comparative Advantage Index, -1 to 1



Source: World Bank staff calculations



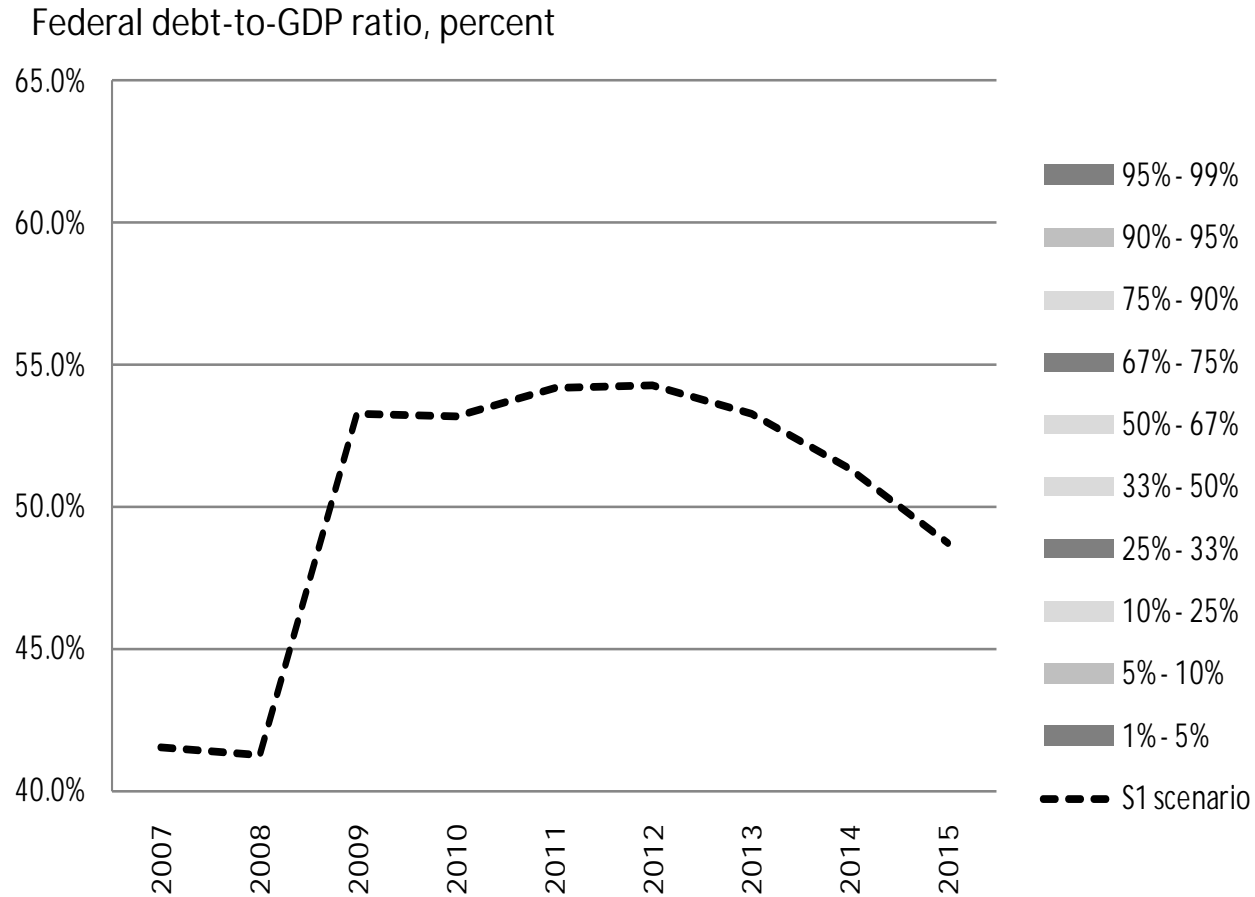
But the commodities super-cycle could be ending...



Source: CEIC and World Bank staff calculations.



...bringing significant risks especially to the fiscal position

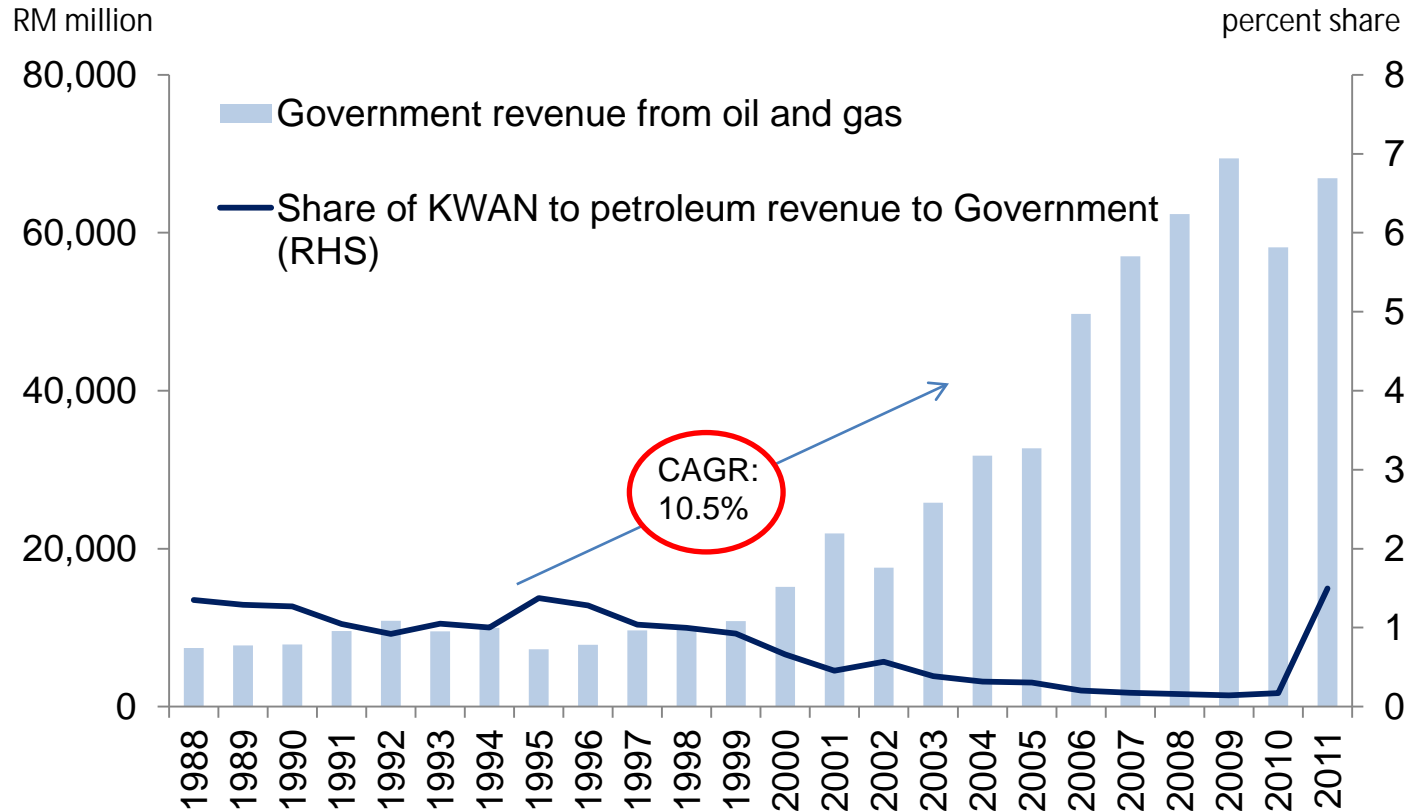


Source: World Bank Malaysia Economic Monitor November 2011



What to do? Save more...

1. Shift the balance of funds going to KWAN vs. directly to the budget



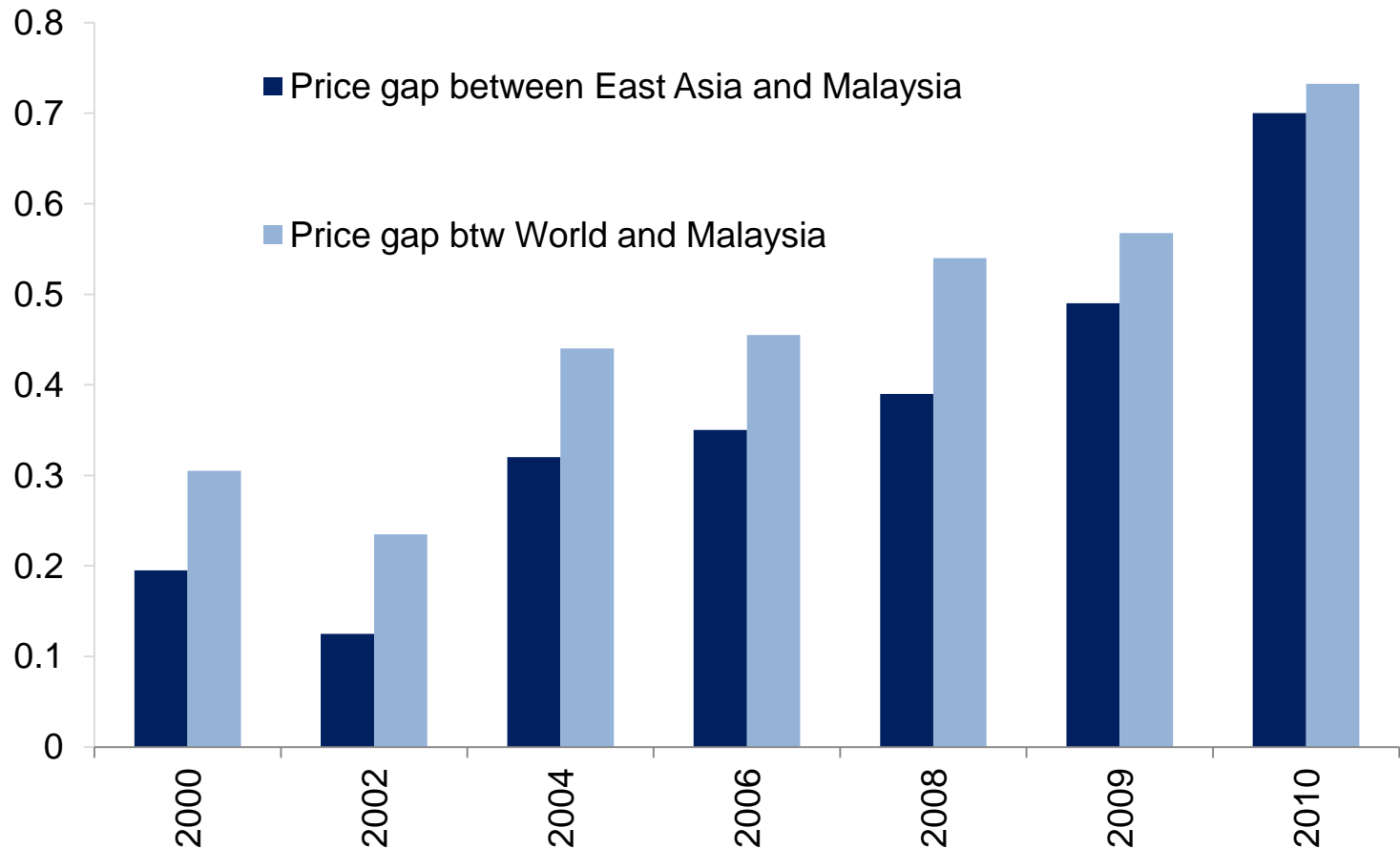
Source: Accountant General's Office, Malaysia

This requires raising new revenues through broader tax base (e.g. GST), and/or...



Spend less on distorting and environmentally-unfriendly subsidies on fuel...

Price gap between Malaysia's fuel prices and East Asia and world prices, USD per liter



Source: World Bank

WORLD BANK

...and gas

Potential Revenue foregone from gas subsidies, RM billion unless otherwise indicated

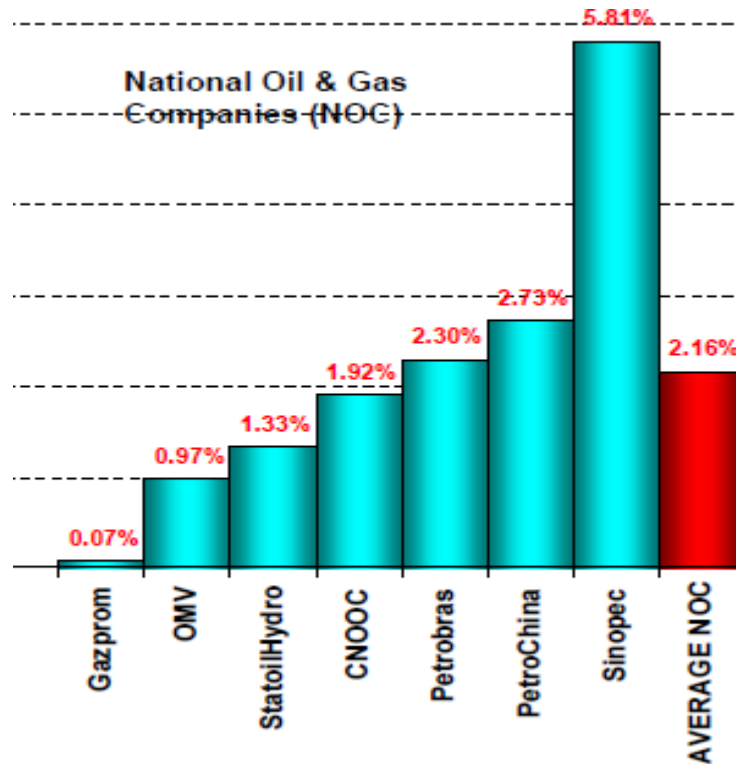
	FY 2011	% of GDP	Cumulative since 1997
Power Sector	11.6	1.3	108.5
- Tenaga Nasional Bhd	4.9	0.6	46.1
- Independent Power Producers	6.7	0.8	62.4
Non-Power Sector, including industrial, commercial, residential users and NGV	8.5	1.0	46.4
Total	20.1	2.3	154.9

Source: PETRONAS (2012) and World Bank staff calculations



Invest more in R&D...

R&D Spending as % of Sales in 2007



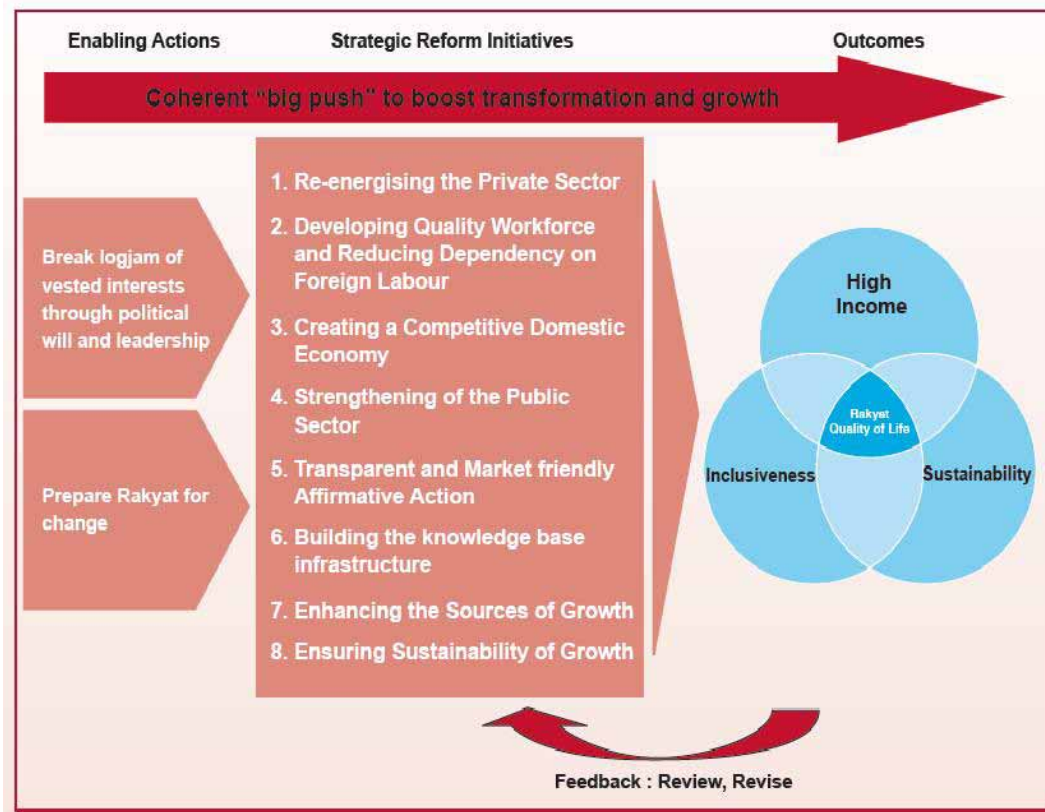
**PETRONAS:
0.01% (2011)**

Source: Presentation given by Datuk (Dr) Abdul Rahim Hj Hashim, PETRONAS VP for Research & Technology, December 2008.



... and in assets that promote horizontal diversification

Promote growth of high value-added, externally-oriented manufacturing and services through structural reform



Improve public investment management to increase effectiveness of public investment

Public investment management...

...to convert natural resource revenues into public infrastructure with maximum efficacy

“Bolstering public investment management capacity is critical to ensure that scaled-up spending will yield the expected growth benefits. Project proposals should be carefully appraised and the capacity for project implementation strengthened, including by improved procurement practices. These reforms should be implemented in the context of wider public financial management reforms that provide a credible medium-term orientation to the budget (Rajaram et. al. 2010).”

ü Introduce rigorous cost-benefit analysis to capital budgeting



Key Messages

While recent trends have raised some concerns, Malaysia remains a success story in natural resource management and offers many lessons to other resource-rich countries

An evolution to the management of natural resources by PETRONAS: from direct contributions to the budget towards an Increased role for KWAN as a natural resource fund. This can be supported by:

- Broadening the tax base

- Replacing fuel subsidies with targeted transfers

- Reviewing gas pricing

Export-orientation and openness key to ensure economy builds competitiveness in both manufacturing and services

Rigorous evaluation of policy experiments

- E.g., rigorous cost-benefit analysis of fiscal incentives across industries

