OPTIMISM IN TIMES OF SLUGGISH RECOVERIES

The growth figures for this year have been revised to a contraction of between 4% and 5%. This revision followed Bank Negara's announcement that the economy had shrunk by 6.2% in the first quarter of 2009.

This downward fall is not at all surprising. Malaysia's growth depends very heavily on our exports and, by extension, on the export-driven manufacturing sector.

Unlike China or India, Malaysia does not have a large domestic market. Neither does Malaysia have a well-diversified portfolio of exports. With most of our exports destined for the United States (US), the European Union (EU), and Japan, what else could one expect if the demand for goods from these economies is flaccid.

Much of what lies ahead for Malaysia's growth hinges emphatically on the short-term destinies of the economies that were most severely hit by the recent global economic and financial crisis.

The recession that has resulted from the crisis has been dubbed by the International Monetary Fund (IMF) as the "most severe recession since World War II."

Yet, optimism ceaselessly abounds in Malaysian officialdom and the media. Some of the positive air of expectation springs from the way the stock markets have been performing.

The Kuala Lumpur Composite Index (KLCI) has, without a shred of doubt, done much better since October 2009 when it was known to touch 903 points. At the time of writing it stands at 1062.

Maybe it is the KLCI that nudges people into a false mood of hope. But, then, the stock market is at best an indicator of how investors expect the economy to turnaround in the next 6 months.

The expectations of short-term investors, as they are felt today, need not turn out to match the outcomes that will be realised by producers in the months ahead. In addition, the KLCI does not drive the real economy.

Ultimately, it is levels of production, consumer demand and the demand for exports as generated in the developed world that will drive Malaysia's export-led growth. As far as these variables are concerned - and these are the factors that really matter - the picture is far from clear or settled.

In desperate times, analysts hanker after the smallest glimmers of hope. The slimmest of "green shoots" give rise to prophecies of positive growth. But, how positive will this "positive" growth be?

Green shoots do not abound everywhere. In the US about 5.7 million individuals have lost their jobs to date. It is claimed that anything like another million jobs could be lost before a solid recovery is established.

The US unemployment rate could reach 10% in 2010. Until the unemployment figures regain some colour it is hard to see how the American consumer is going to be in a position to spend, and buy from countries like Malaysia. The anxiety on the part of the US consumer is reflected by its high personal savings rate. Personal savings rates rose to 5.7% in April, a high that had not been witnessed in the last 14 years.

At any rate, the current jobless rate is about 6% in the 16 Eurozone nations, an unemployment rate that has not been matched in the last 10 years. The present unemployment rate of close to 9% in the US has been unprecedented in the last 25 years.

It is a wonder where Malaysia's upbeat growth rates will come from when consumers in the world's largest economy have to battle job losses and are worried enough to save more than they customarily do.

The picture is equally bleak beyond the US. The Organization for Economic Cooperation and Development (OECD) has forecast that as many as 36 million people in the G7 nations would be unemployed in 2010. By contrast, 18 million people were on unemployment benefits in 2007.

If these figures do not inspire sobriety, then predictions regarding expected rates of growth should. While the Federal Reserve expects a growth of about 2.5% for the US economy in 2010, the IMF is less optimistic. The IMF puts its forecast for the US at zero growth.

The Fed Chairman Ben Bernanke has announced his view that the recovery in the US will be slow given the weak labour market and tight credit conditions.

Bernanke's recent statements are one of reserved optimism. He acknowledges that there is a decline in economic contraction, but that does not suggest the economy is buoyant. He has been careful to admit that "recovery will only gradually gain momentum."

Can China and India fill the role that the developed economies played? That does not seem to be a realistic expectation at all. For one, Malaysia does not engage in a great deal of trade with India. Second, India's growth is estimated to grow at a modest 4.5% in 2010, and its job loss rates at present are not exactly ground for joy.

Estimates for China's growth in 2010 range from 6.5% to 8%. That is not a rate that is as exciting as the double-digit rates it was accustomed to in the years preceding the crisis. For contrast, one should juxtapose the growth that is expected in 2010 against the 13% that was achieved in 2007.

A growth figure of 8% in 2010 for China may not actually fuel world growth or Malaysia's growth. Much of the growth in China at about this rate would be sufficient to keep its own economy under control.

Levels of growth such as this may not even be sufficient to contain the vast numbers of school graduates that are poured out every year. This is not to forget the rural-urban population drift in China that is continually in search of jobs that, in turn, depend on overseas demand and investment by the private sector.

It is important to bear in mind that a 1% growth in an OECD economy could do more to boost exports from Malaysia than a 8% growth from China. This is because the low per capita incomes in China do allow any compensation for the huge decreases in absolute amounts that are generated in developed economies. A small growth in the OECD countries could do more to spike Malaysia's growth than a huge growth in China.

As these messages of caution are transmitted across borders, doses of engineered optimism have found their way to fill the gaps of uncertainty. Malaysia by virtue of being a small, open, export-dependent economy would do well to adopt a careful stance, one that is capable of absorbing slack in export demand, rather than to assume that high rates of growth are on their way after Christmas.

Dr. Shankaran Nambiar is a Senior Research Fellow at the Malaysian Institute of Economic Research.