

Malaysia Macro View

Budget 2013: Surprising Positively On Populism and Prudence

- **Surprising positively on both populism and prudence** – Budget 2013 ambitiously seeks to balance between continued fiscal consolidation and pre-election goodies, positively surprising on both counts. Beneficiaries of pre-election measures were broadened beyond civil servants and poor to include urban middle class taxpayers and other swing voters who would deliver the greatest political bang for the buck. Measures for businesses were targeted at debt markets, oil and gas, Bumiputera contractors and property developers. Positive surprises in fiscal deficit targets in recent years could allay concerns on commitment to fiscal consolidation.
- **Ambitious but credible 2012 and 2013 deficit target of 4.5% and 4% of GDP** – While the assumed 0.4% cut in expenditure (2012: +9.5%) is challenging, spending overshoots can be offset by upside surprises to conservative revenue growth assumptions despite improvements in tax collection, stable GDP growth and Petronas dividend. If the ambitious headline 2013 deficit target is met, this should result in improvements in key fiscal metrics, including [1] a larger operating fiscal surplus of 0.7% of GDP (2012: 0.5%), [2] sizeable reduction in the primary fiscal deficit to 1.8% of GDP (2012: 2.3%), [3] a 1% decline in the fiscal deficit ex oil revenues to 10.5% of GDP (2012: 11.6%). The smaller primary deficit, stable growth and low real rates should keep public debt to GDP stable at under 55% of GDP.
- **Prioritizing countercyclical support and political expediency** – Civil servant bonuses, fiscal transfers for low income households, and income tax cuts for urban middle class take effect largely in Jan 2013 and may signal elections only in 2013 whilst prolonging fiscal cushion for consumption by 1%-pt when exports are likely to face further pressure. With private investments already at a 15-year high, there was little need for pump-priming, enabling a cut in development spending and only sector-specific measures for O&G, capital markets, and politically important groups.
- **Only incremental, steps to tackle long-standing issues with no game changers** – With the political circus of impending General Elections *still* not over, medium-term imperatives unsurprisingly remained at a standstill this year. This is not to say there was no progress. Greater emphasis on education and training can help address the human capital deficit. More explicit hints of GST implementation and subsidy rationalization were politically brave, even as they appeased ratings agencies. Cuts in personal income taxes for the middle class could be a precursor to GST or top tax rate cuts. Measures to improve home affordability however may worsen concerns over household leverage. Deeper reforms are clearly waiting for elections.
- **Market implications** – The smaller than expected deficit and stable gross issuance should be positive for MGS and MYR, but high foreign holdings (around 42% of outstanding) may limit gains. Budget 2013 is positive for equities, especially consumer and oil and gas plays, and mildly negative for developers.

Wei Zheng Kit

+65-6657-5079

wei.zheng.kit@citi.com

Brian Tan

brian.tan@citi.com

See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

Citi Research is a division of Citigroup Global Markets Inc. (the "Firm"), which does and seeks to do business with companies covered in its research reports. As a result, investors should be aware that the Firm may have a conflict of interest that could affect the objectivity of this report. Investors should consider this report as only a single factor in making their investment decision.

Surprising Positively on Populism and Prudence

Budget 2013 was clearly an ambitious pre-election, yet prudent Budget. The biggest winners were low and middle income households – expanding beyond civil servants and rural households to urban swing voters whose support is needed to reclaim the government's two-thirds parliamentary majority. The fiscal deficit target looks ambitious for an election budget, but the track record of recent successes in fiscal consolidation suggests it may be credible if measures help to cushion growth – especially consumption – against an external demand slowdown. Understandably, there were no game changers to tackle long-standing structural challenges, though there were hints of future changes after elections.

As before, in assessing Budget 2013, a few questions are worth answering. First, what accounts for the deficit projections, and are they realistic? Second, how do the announced measures square with the political backdrop? Third, what will this mean for the near-term economic outlook? Fourth, has the Budget effectively tackled the medium-term structural gaps facing Malaysia?

Delivering on Deficit Reduction

Fiscal consolidation is projected to continue at a faster than expected pace in 2013, after surprising positively in the past two years. Both 2012 and 2013 deficit targets of RM42.3bn (4.5% of GDP) and RM40bn (4% of GDP) were lower than our and market estimates. The projected 2013 deficit reduction is largely on the back of cuts in spending, especially development spending, with revenues hardly expected to rise. The projected RM40bn deficit is the smallest since 2008 (RM35.6bn), and will help offset larger refinancing needs, such that gross MGS and GII issuance will likely be kept stable at RM96.3bn in 2013 (2012: RM96.6bn).

Figure 1. Budget Estimates

	2011 Actual		2012 Budget (Oct 2011)		2012 Revised Budget (Sep 2012)		2013 Budget (Sep 2012)		2013 Citi Estimate (Sep 2012)	
	RM bn	%YoY	RM Bn	%YoY	RM Bn	%YoY	RM Bn	%YoY	RM Bn	%YoY
Revenue	185.4	16.1	186.9	0.8	207.2	11.8	208.7	0.7	212.8	2.7
% of GDP	21.0		20.4		22.1		20.8		21.2	
Direct Tax	102.2	29.4	102.1	-0.1	116.8	14.3	122.0	4.4	123.0	5.3
Companies	46.9	29.3	47.5	1.3	54.1	15.5	57.7	6.5	58.0	7.1
Petroleum Income Tax	27.7	48.3	26.5	-4.5	32.0	15.2	30.5	-4.6	30.5	-4.6
Individuals	20.2	13.5	21.3	5.4	22.4	11.1	24.6	9.5	25.0	11.4
Cooperatives & Others	7.4	18.9	7.1	-4.1	8.3	11.9	9.2	11.1	9.5	14.7
Indirect Tax	32.6	7.0	33.5	2.6	35.7	9.3	37.2	4.3	38.8	8.8
Non-Tax	50.5	0.4	51.3	1.5	54.8	8.3	49.5	-9.6	51.0	-6.9
Expenditure	227.9	12.3	229.9	0.9	249.5	9.5	248.6	-0.4	252.6	1.2
Operating Expenditure	182.6	20.4	181.6	-0.5	202.6	11.0	201.9	-0.3	206.3	1.8
% of GDP	20.7		19.8		21.6		20.2		20.5	
Subsidies	30.9	33.8	33.2	7.4	42.4	37.1	37.6	-11.3	40.0	-5.7
Operating Expenditure ex Subsidies	151.7	18.0	148.4	-2.2	160.2	5.6	164.3	2.6	166.3	3.8
Gross Development Expenditure	46.4	-12.1	49.2	6.0	49.8	7.3	47.8	-4.2	47.8	-4.1
% of GDP	5.3		5.4		5.3		4.8		4.8	
Loan Recoveries	1.1	-27.7	0.9	-16.8	2.9	167.6	1.0	-64.6	1.5	-48.2
Net Development Expenditure	45.3	-11.6	48.3	6.5	46.9	3.5	46.7	-0.4	46.3	-1.3
Fiscal Balance	-42.5	-1.8	-43.0	1.2	-42.3	-0.5	-40.0	-5.4	-39.8	-5.8
Fiscal Balance % GDP	-4.8		-4.7		-4.5		-4.0		-4.0	
Net External Borrowing	0.5		-0.5		-0.5		-0.4		-0.4	
Maturing MGS, GII			50.0		53.8		52.9		52.9	
Maturing One Malaysia Sukuk							3.0		3.0	
Estimated gross MGS issuance, based on fiscal deficit forecast			93.5		96.6		96.3		96.2	

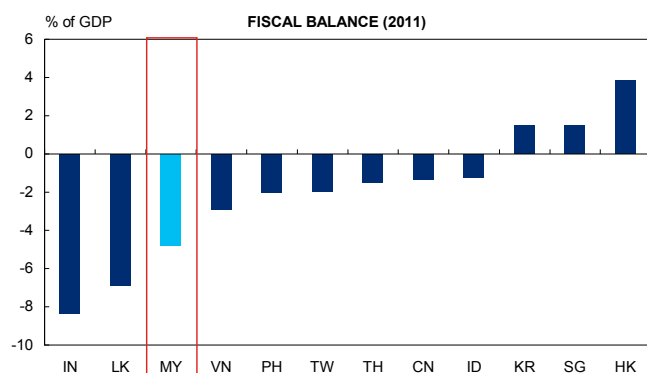
Source: MoF, Citi Research

Election imperatives notwithstanding, the government clearly had a strong incentive to surprise with a smaller than anticipated headline fiscal deficit (both in 2012 and 2013), given the threat of credit ratings downgrades. On 5th Sep, S&P maintained Malaysia's local currency long-term sovereign credit rating at 'A' with stable outlook. While dangling the carrot of a possible ratings upgrade if deficits and debt levels are reduced in line with the 10th Malaysia Plan, S&P also wielded the stick of a ratings downgrade, noting that:

"We may lower the ratings if the government can't deliver the reform measures to reduce its fiscal deficits and increase the country's growth prospects. These reforms may include, but are not limited to, the GST and subsidy reforms on the fiscal side, and private investment and economic diversification reforms on the economic growth agenda"

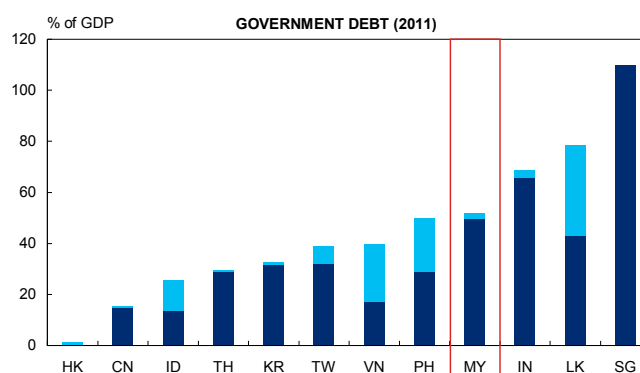
Besides a smaller headline deficit, it was this same threat of a downgrade that likely prompted the government to more explicitly hint at GST implementation and reform subsidies – which were conspicuously absent in Budget 2012 and which we view as a politically brave move so close to elections.

Figure 2. Fiscal balances in Asia



Source: Citi Research

Figure 3. Government debt in Asia



Source: Citi Research

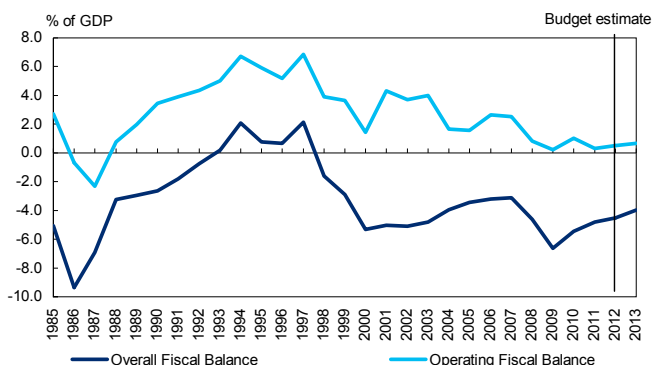
Achieving the ambitious fiscal targets would continue the improvement in key fiscal metrics that started in Budget 2012. First, the 0.3% cut in operating expenditure for 2013 would result in a slight improvement in the operating balance (which excludes development spending) to RM6.7bn, or 0.7% of GDP, from a low of just RM2.8bn or 0.3% of GDP in 2011.

Second, excluding debt service charges, the primary fiscal deficit is projected to fall to RM17.7bn or 1.8% of GDP, the smallest since 2007 (RM7.7bn or 1.2% of GDP). Higher debt service charges are a reflection of a legacy of accumulated past deficits and have resulted in debt service costs rising to 10.7% of total revenues from just 9.9% in 2012 and 8% in 2008. The smaller primary deficit reflects an attempt to offset this by reducing wastage and/or improving revenue collection. With the primary deficit slightly smaller than the likely gap between real GDP growth (around 5%) and real interest rates (around 1.5% – calculated from a nominal interest rate of around 4% on debt and 2.5% inflation) next year, the public debt to GDP ratio in 2013 could be similar or even lower than 2012's level of 53.7%.

Third, excluding oil revenues, we estimate the deficit would fall to 10.5% of GDP (2012: 11.6%), from a peak of 16.3% in 2009, with the share of oil revenues expected to fall slightly to 31.3% of total revenues from a peak 40%

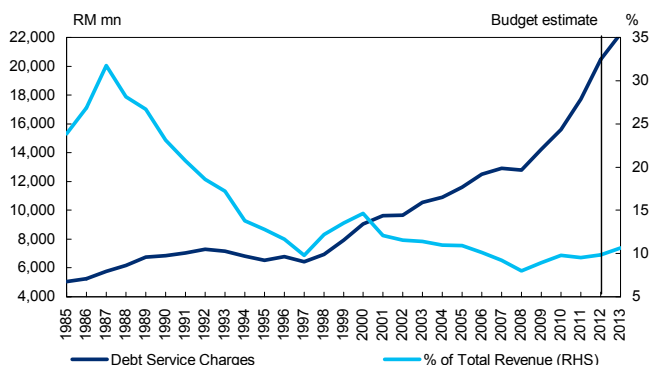
in 2009. Importantly, this assumes a slight *increase* in the Petronas dividend to RM27bn (2012: RM26.3bn). If earlier statements that the dividend would be capped at 30% of Petronas' net profits materialize after elections (forcing a cut in petroleum subsidies), the share of oil revenues could fall further.

Figure 4. Headline and Operating Fiscal Balances (ex development spending)



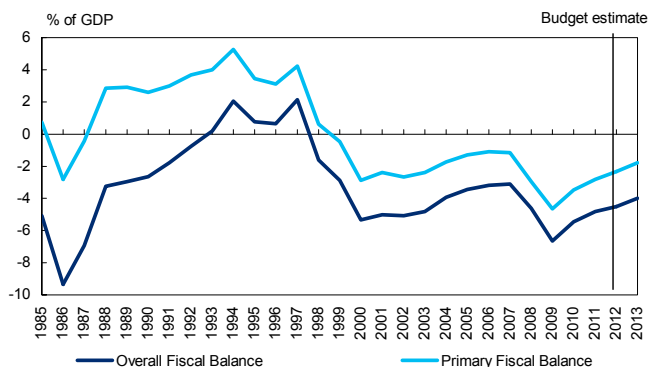
Source: MoF, CEIC, Citi Research

Figure 5. Debt Service Charges



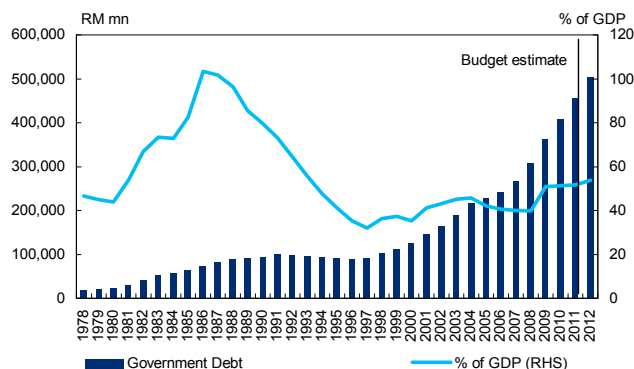
Source: MoF, CEIC, Citi Research

Figure 6. Headline and Primary Fiscal Balances (ex debt service charges)



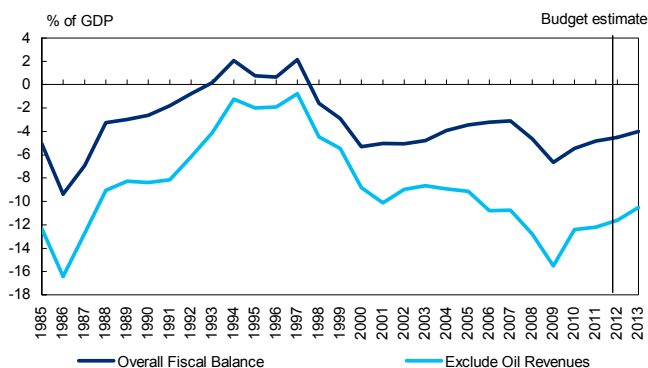
Source: MoF, CEIC, Citi Research

Figure 7. Government Debt Levels



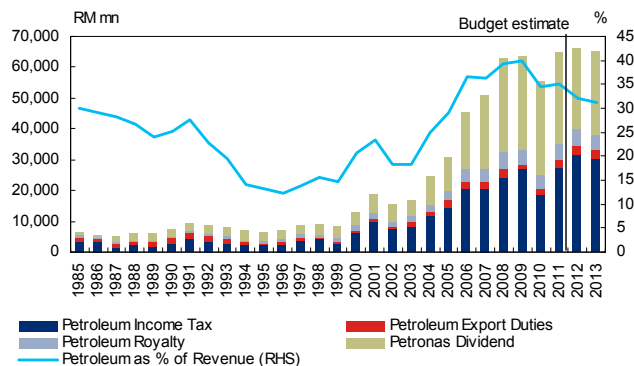
Source: MoF, CEIC, Citi Research

Figure 8. Headline and Non-Oil Fiscal Balances



Source: MoF, CEIC, Citi Research

Figure 9. Oil Revenues



Note: 2013 petroleum royalty is Citi estimate

Source: MoF, CEIC, Citi Research

The fiscal deficit targets for both 2012 and 2013 are certainly ambitious, but achievable in our view. With regards to the 2012 deficit target, the Jan-Aug fiscal deficit stood at just RM17.4bn or 41% of the revised target of RM42.3bn. Revenues have been much stronger than earlier expected – in Jan-Aug 2012, the government collected RM136bn of revenues, or 72% of the original Budget target of RM186.9bn, well above the historical average of 61% of full year revenues typically collected in the first 8 months. Indeed, a simple extrapolation of the historical average figure would yield full-year revenues of RM221bn, suggesting that the upwardly revised revenue target of RM208.7bn may be conservative. As discussed earlier in our [Budget 2013 Preview](#), the outperformance in revenues largely reflects administrative improvements to close the tax gap since 2011, which have raised tax revenues as % of GDP. While a similar straight line extrapolation applied to year-to-date spending data should likewise suggest overshoots in expenditures, this will likely be more than covered by the likely revenue outperformance. Looking at the risks to the 2012 deficit forecasts, a deficit as low as RM28bn is possible if spending is maintained at Budgeted levels but revenue outperforms in line with historical patterns, though populist pressures make this scenario improbable. Similarly, the recent tendency to match spending with revenues is likely to render the scenario of massive spending overshoots despite in line revenues improbable as well.

Figure 10. Risks to the 2012 deficit estimates

		YTD Aug-2012	Full Year Estimate Implied by Historical Average	Revised Budget 2012	Scenario: Revenues exceed, Expenditures on target	Scenario: Revenues on target, Expenditures exceed
Revenue	RM bn	136.0	221.879	207.2	221.9	207.2
Expenditure	RM bn	153.3	264.148	249.5	249.5	264.1
Fiscal Balance	RM bn	-17.3	-42.3	-42.3	-27.7	-56.9
Revenue	Aug-2012 as % of Full Year		61.3	65.6	61.3	65.6
Expenditure			58.0	61.4	61.4	58.0

Source: MoF, CEIC, Citi Research

The deficit target for 2013 is similarly ambitious but credible if the Budget assumption of 4.5-5.5% GDP growth holds, allowing for revenue outperformance to cover expenditure overshoots.

The assumption for revenue growth to slow sharply to just 0.7%YoY in 2013 (2012E: 11.8%) appears overly conservative in our view and is consistent with MOF's recent track record of under-promising but over-delivering on the revenue front. In Budgets 2011 and 2012 for example, MOF had estimated revenue growth of just 3.9% and 1.1%YoY respectively. In the event, actual revenue growth rates were four times Budget estimates in 2011 while the revised Budget 2012 estimates were ten times the initial estimate.

Digging deeper, we find that the conservative revenue assumptions reflect both [1] a 1.6% decline in oil revenues (2012E: +2.1%) and [2] much slower growth in non-oil revenues of just 1.7% (2012E: 17%). Despite valid grounds behind conservative oil revenues projections, there could still be upside risks on production increases, while non-oil revenues could also surprise positively on the upside for a variety of reasons.

- Oil revenues are projected to decline further to just 31.3% of overall revenues (2012E: 32%, 2011: 35%) mainly due to a 4.6% decline in Petroleum Income Tax (PITA) collections. We believe this is largely on account of incentives for the oil and gas (O&G) sector given in the Budget, namely the 100% Investment Tax Allowance for 10 years for investments in refinery activities. We note that other components of oil revenues which are not affected by the tax incentives are

actually projected to rise slightly. This includes the Petronas Dividend, which is projected to rise to RM27bn (2012E: RM26.3bn), but was originally expected to fall in line with plans to curb the dividend at 30% of Petronas's net income.

Figure 11. Oil Revenues

		2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012E	2013F
OIL REVENUE	RM bn	12.9	18.6	15.4	16.8	24.6	30.9	45.2	50.9	62.8	63.3	55.3	64.9	66.3	65.2
	% of GDP	3.5	5.1	3.9	3.9	5.0	5.7	7.6	7.6	8.2	8.9	7.0	7.4	7.1	6.5
	% of revenues	20.8	23.4	18.4	18.2	24.8	29.1	36.6	36.4	39.3	39.9	34.6	35.0	32.0	31.3
	%YoY	50.7	44.5	-17.2	9.2	46.4	25.5	46.5	12.5	23.4	0.7	-12.6	17.3	2.1	-1.6
Petroleum Income Tax	RM bn	6.0	9.9	7.6	8.5	11.5	14.6	20.7	20.5	24.2	27.2	18.7	27.7	32.0	30.5
	% of GDP	1.6	2.7	1.9	1.9	2.3	2.7	3.5	3.1	3.1	3.8	2.4	3.1	3.4	3.0
	% of revenues	9.7	12.4	9.1	9.1	11.5	13.7	16.7	14.6	15.1	17.2	11.7	15.0	15.4	14.6
	%YoY	110.4	64.0	-22.5	10.9	35.6	26.9	41.9	-1.1	18.3	12.6	-31.3	48.3	15.2	-4.6
Petroleum Export Duties	RM bn	1.0	0.8	0.8	1.1	1.5	2.0	2.3	2.3	2.7	1.2	1.7	2.0	2.4	2.5
	% of GDP	0.3	0.2	0.2	0.3	0.3	0.4	0.4	0.3	0.4	0.2	0.2	0.2	0.3	0.3
	% of revenues	1.6	1.0	0.9	1.2	1.5	1.9	1.9	1.6	1.7	0.8	1.1	1.1	1.2	1.2
	%YoY	63.0	-16.6	-7.7	44.2	39.2	31.8	14.6	-2.3	19.0	-55.0	43.6	13.2	21.2	5.0
Petroleum Royalty	RM bn	1.8	2.0	1.6	2.1	2.5	3.3	4.2	4.2	5.9	4.8	4.9	5.1	5.6	5.2*
	% of GDP	0.5	0.5	0.4	0.5	0.5	0.6	0.7	0.6	0.8	0.7	0.6	0.6	0.6	0.5
	% of revenues	2.8	2.5	1.9	2.3	2.5	3.1	3.4	3.0	3.7	3.0	3.0	2.8	2.7	2.5
	%YoY	81.0	13.4	-20.0	33.9	16.6	31.8	28.8	-2.1	42.3	-18.7	1.0	6.0	8.8	-7.1
Petronas Dividend	RM bn	4.1	5.9	5.4	5.1	9.1	11.0	18.0	24.0	30.0	30.0	30.0	30.0	26.3	27.0
	% of GDP	1.1	1.6	1.4	1.2	1.8	2.0	3.0	3.6	3.9	4.2	3.8	3.4	2.8	2.7
	% of revenues	6.6	7.4	6.5	5.5	9.2	10.3	14.6	17.2	18.8	18.9	18.8	16.2	12.7	12.9
	%YoY	0.0	44.1	-8.8	-5.4	78.4	20.9	63.6	33.3	25.0	0.0	0.0	0.0	-12.3	2.7

*2013 petroleum royalty figure is Citi estimate

Source: MoF, CEIC, Citi Research

- We understand that the Budget assumes Tapis oil prices will average a lower US\$95/bbl in 2013 from US\$105/bbl in 2012. This seems reasonable – our in-house analysts for example expect Brent to average US\$99/bbl in 2013, down from US\$113/bbl in 2012. Nonetheless, with possible upside risks to oil prices from QE3, and production from new oil fields coming onstream next year, there could be offsets to revenue losses from tax incentives.
- Non-oil revenues as a % of GDP are projected to fall to 14.3% of GDP, from 15.1% in 2012. This in turn comprises non-oil tax revenues (2013F: 12.6% of GDP, 2012E:12.6%) and non-oil non-tax revenues (2013F: 1.7%, 2012E: 2.4%). The assumption of stable non-oil tax revenues is conservative, as the government expects higher nominal GDP growth of 7% in 2013 vs. 6.3% in 2012, which may see more taxpayers falling into a higher tax bracket (we doubt the announced income tax cuts for middle income groups will make much of a dent to income tax collected, as the primary beneficiaries of growth could fall into higher tax brackets). Further administrative improvements in tax collections may further increase the non-oil tax revenue share of GDP. Non-oil non-tax revenues – which comprise license fees, non-oil investment returns and other revenues – could be potentially boosted by divestment returns.

Figure 12. Non-Oil Revenues

		2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012E	2013F
NON-OIL REVENUE	RM bn	49.0	61.0	68.1	75.8	74.8	75.4	78.3	89.0	97.0	95.4	104.3	120.5	141.0	143.4
	% of GDP	13.2	16.6	17.1	17.4	15.2	13.9	13.1	13.4	12.6	13.4	13.1	13.7	15.1	14.3
	% of revenues	79.2	76.6	81.6	81.8	75.2	70.9	63.4	63.6	60.7	60.1	65.4	65.0	68.0	68.7
	%YoY	-2.3	24.4	11.7	11.3	-1.3	0.8	3.8	13.7	9.0	-1.7	9.4	15.5	17.0	1.7
Corporate Income Tax	RM bn	13.9	20.8	24.6	24.0	24.4	26.4	26.5	32.1	37.7	30.2	36.3	46.9	54.1	57.7
	% of GDP	3.8	5.7	6.2	5.5	5.0	4.9	4.4	4.8	4.9	4.2	4.6	5.3	5.8	5.8
	% of revenues	22.5	26.1	29.5	25.9	24.5	24.8	21.4	23.0	23.6	19.0	22.7	25.3	26.1	27.6
	%YoY	-11.7	49.4	18.6	-2.6	1.7	8.2	0.4	21.4	17.4	-20.0	20.1	29.3	15.5	6.5
Personal Income Tax	RM bn	7.0	9.4	9.9	8.0	9.0	8.6	10.2	11.7	15.0	15.6	17.8	20.2	22.4	24.6
	% of GDP	1.9	2.6	2.5	1.8	1.8	1.6	1.7	1.8	1.9	2.2	2.2	2.3	2.4	2.5
	% of revenues	11.3	11.9	11.8	8.6	9.0	8.1	8.3	8.3	9.4	9.8	11.2	10.9	10.8	11.8
	%YoY	9.3	34.5	4.8	-19.3	12.4	-3.7	17.9	14.4	28.3	4.2	14.2	13.5	11.1	9.5
Import Duties	RM bn	3.6	3.2	3.7	3.9	3.9	3.4	2.7	2.4	2.6	2.1	2.0	2.0	2.2	2.4
	% of GDP	1.0	0.9	0.9	0.9	0.8	0.6	0.4	0.4	0.3	0.3	0.2	0.2	0.2	0.2
	% of revenues	5.8	4.0	4.4	4.2	3.9	3.2	2.2	1.7	1.6	1.3	1.2	1.1	1.1	1.1
	%YoY	-23.8	-11.3	14.9	6.8	-1.1	-12.6	-20.9	-9.5	8.7	-19.8	-7.0	3.0	10.8	5.0
Excise Duties	RM bn	3.8	4.1	4.7	5.0	6.4	8.6	8.6	9.0	10.7	10.1	11.8	11.5	12.3	12.8
	% of GDP	1.0	1.1	1.2	1.2	1.3	1.6	1.4	1.4	1.4	1.4	1.5	1.3	1.3	1.3
	% of revenues	6.1	5.2	5.7	5.4	6.5	8.1	6.9	6.4	6.7	6.3	7.4	6.2	6.0	6.1
	%YoY	-19.5	8.6	14.9	6.0	27.7	34.4	-0.7	4.8	18.8	-5.7	16.9	-2.2	7.1	3.6
Sales and Services Taxes	RM bn	7.7	9.3	11.5	10.0	9.2	10.3	9.2	9.7	11.7	11.9	12.1	13.6	15.4	16.2
	% of GDP	2.1	2.5	2.9	2.3	1.9	1.9	1.5	1.5	1.5	1.7	1.5	1.5	1.6	1.6
	% of revenues	12.4	11.7	13.7	10.8	9.2	9.7	7.5	6.9	7.3	7.5	7.6	7.3	7.4	7.7
	%YoY	29.0	21.0	23.4	-12.7	-8.4	12.3	-10.4	4.8	21.4	1.9	1.3	12.1	13.4	5.0
Other Taxes	RM bn	4.1	4.0	4.0	4.3	6.1	6.6	6.5	7.5	8.2	8.2	9.1	10.9	11.6	12.6
	% of GDP	1.1	1.1	1.0	1.0	1.2	1.2	1.1	1.1	1.1	1.2	1.1	1.2	1.2	1.3
	% of revenues	6.7	5.0	4.8	4.7	6.2	6.2	5.2	5.4	5.1	5.2	5.7	5.9	5.6	6.0
	%YoY	-3.0	-4.5	1.6	8.0	41.4	7.4	-2.2	16.5	8.9	0.2	10.8	19.5	6.7	8.7
Non-Oil Non-Tax Revenues	RM bn	8.8	10.2	9.7	20.5	15.7	11.4	14.7	16.6	11.0	17.3	15.3	15.4	22.9	17.3
	% of GDP	2.4	2.8	2.4	4.7	3.2	2.1	2.5	2.5	1.4	2.4	1.9	1.7	2.4	1.7
	% of revenues	14.3	12.8	11.6	22.1	15.8	10.7	11.9	11.8	6.9	10.9	9.6	8.3	11.0	8.3
	%YoY	7.0	15.1	-4.9	111.8	-23.1	-27.5	28.6	12.9	-33.7	57.7	-11.8	0.7	48.5	-24.3

Source: MoF, CEIC, Citi Research

Likely upside surprises to tax revenues could offset slippages to the assumed 0.4%YoY cut in expenditure to just 24.8% of GDP, comprising marginal cuts in operating expenditure and large cuts in development expenditure

The targeted cut of 0.3% in operating expenditure to 20.2% of GDP (2012E: 21.6%) looks optimistic in a likely election year, considering that operating expenditure had risen at an average rate of over 10% over the last 20 years. For 2012, the originally budgeted 1.3% increase in operating expenditure was sharply revised upwards to an 11% increase – reflecting largely higher subsidies (which include the pre-election cash handouts to low-income households) and emoluments and pensions and supplies and services, given civil servant bonuses and higher basic wages. The projected RM0.7bn decline in operating expenditures in 2013 is largely a result of a decline in subsidies (-RM4.8bn), emoluments (-RM0.6bn), pensions (-RM0.6bn), and grants to statutory bodies (-RM1bn).

Figure 13. Operating Expenditure

	2011			2012 Budget			2012 Revised Budget			2013 Budget			Change between 2012 Revised and 2013 Budget
	RM bn	% of GDP	%YoY	RM bn	% of GDP	%YoY	RM bn	% of GDP	%YoY	RM bn	% of GDP	%YoY	RM bn
Operating Expenditure	182.6	20.7	20.4	181.6	19.8	1.3	202.6	21.6	11.0	201.9	20.2	-0.3	-0.7
Emolument	50.1	5.7	7.5	52.0	5.7	0.5	59.2	6.3	18.0	58.6	5.9	-1.0	-0.6
Pensions and Gratuities	13.6	1.5	17.8	12.1	1.3	4.7	14.2	1.5	4.6	13.6	1.4	-4.2	-0.6
Debt Service Charges	17.7	2.0	13.4	20.5	2.2	-4.3	20.5	2.2	15.4	22.2	2.2	8.8	1.8
External	0.7	0.1	4.0	0.5	0.1	-16.9	0.5	0.1	-21.8	0.6	0.1	6.0	0.0
Domestic	17.0	1.9	13.8	19.9	2.2	-3.7	19.9	2.1	16.9	21.7	2.2	8.8	1.8
Grants and Transfers to State Governments	5.5	0.6	18.0	5.8	0.6	0.4	5.8	0.6	5.6	6.3	0.6	7.4	0.4
Constitutional Grants	3.6	0.4	11.3	3.9	0.4	-0.4	3.9	0.4	8.3	4.7	0.5	20.5	0.8
Other Grants/Transfers	2.0	0.2	32.8	2.0	0.2	2.1	2.0	0.2	0.8	1.6	0.2	-18.5	-0.4
Supplies and Services	28.9	3.3	21.4	30.5	3.3	-2.0	32.0	3.4	10.4	33.7	3.4	5.3	1.7
Subsidies	30.9	3.5	33.8	33.2	3.6	-5.7	42.4	4.5	37.1	37.6	3.8	-11.3	-4.8
Asset Acquisition	2.7	0.3	42.6	1.1	0.1	75.2	1.2	0.1	-56.7	1.0	0.1	-9.4	-0.1
Refunds and Write-offs	1.0	0.1	67.9	1.4	0.1	-6.8	1.4	0.1	35.0	1.1	0.1	-18.6	-0.3
Grants to Statutory Bodies	13.8	1.6	11.0	14.5	1.6	3.0	15.1	1.6	9.3	14.0	1.4	-6.7	-1.0
Other Expenditure	13.0	1.5	14.7	10.6	1.2	-13.9	11.0	1.2	-15.3	13.7	1.4	24.7	2.7

Note: Figures may not add up due to rounding

Source: MoF, CEIC, Citi Research

The cuts in operating expenditure are dominated by a RM4.8bn cut in subsidies, where implementation would be partly contingent on elections, thereby raising risks of slippage. We also question whether proposed cuts in emoluments and pensions are realistic in a likely election year.

- The subsidy cut partly reflects the announced 20sen/kg cut in sugar subsidies to 34sen/kg or a total RM278mn, but the overall subsidy savings of roughly RM230mn is only a small fraction of the overall subsidy cuts.
- Embedded in the subsidy figures are the cash assistance for low income households, which are projected to fall to RM3bn in 2013 from RM5bn in 2012, despite the eligibility criteria being extended to singles earning less than RM2K/m. With elections to be held latest by Mar/Apr 2013, this 2013 projection does not envisage additional transfers beyond the planned Jan 2013 disbursement. However, a poor election result for the BN may see handouts even after election to meet a growing sense of entitlement built up after successive earlier handouts.
- Also planned are RM5bn of fuel subsidy cuts to RM20bn, partly reflecting lower oil product prices – and, we suspect, two planned hikes in RON95 prices in Jun and Dec – after elections. Whether hikes actually materialize will depend crucially on the timing and outcome of elections. Previous attempts to exclude upper income groups from subsidies had not been successful. Upside risks to fuel subsidies could also stem from higher than expected oil prices due to QE3, though with oil revenues at RM65bn – more than thrice the fuel subsidy bill – this should still be net positive for the fiscal position.

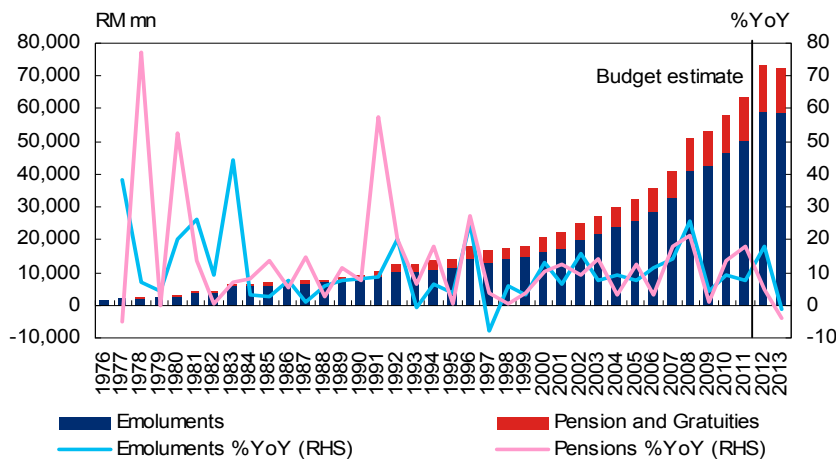
Figure 14. Allocations with Subsidies

Subsidy Components	2012 Budget (Oct 2011)		2012 Revised Budget (Sep 2012)		2013 Budget (Sep 2012)	
	2012 (RM mn)	% of total	RM mn	% of total	RM mn	% of total
Fuel subsidies	17.0	51.2	25.2	59.4	20.0	53.2
Other subsidies	5.5	16.6	6.3	15.0	6.3	16.8
Cooking oil price stabilization scheme			1.5	3.5		
Toll compensation			0.8	1.8		
Flour subsidy			0.2	0.4		
Rural air and rail services			0.2	0.5		
Rebate for low-income households consuming electricity below RM20/month			0.2	0.4		
Interest rate differentials			1.5	3.5		
Incentives	0.9	2.7	0.9	2.0	0.9	2.3
Social assistance programmes	9.8	29.5	10.0	23.6	10.4	27.7
TOTAL	33.2	100	42.4	100	37.6	100

Source: MoF, Citi Research

- Considering that over the past 20 years, emoluments have risen an average of 9.5%, only falling once (by 7.8% in 1997, during the Asian financial crisis), the projected 1% cut in emoluments and 4.2% cuts in pensions clearly do not look realistic. This is especially when one considers the growing size of the civil service and hikes in minimum pensions and military wages. Moreover, Budget projections of emoluments have almost been consistently revised upwards subsequently, reflecting civil servant bonus payments and/or wage hikes.

Figure 15. Emoluments and Pensions



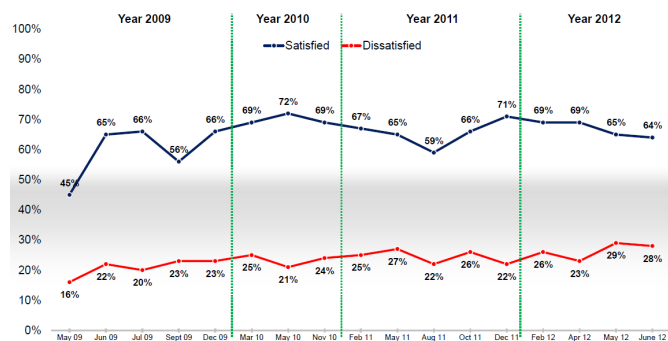
Source: MoF, CEIC, Citi Research

Fiscal Fireworks for Swing Voters

With elections to be held no later than April 2013, Budget 2013 was also PM Najib's last major opportunity to shock and awe the electorate with fiscal firepower. The most recent Merdeka Center survey taken in June shows PM Najib's approval rating fell just 1pt from May to remain high at 64% but the government's approval rating had dropped 6pts to 42%. Worryingly for the BN government, Malay voters' satisfaction with the government had tumbled to 58% from 65%. With global economic conditions deteriorating, 39% of survey respondents cited economic concerns as the top problem facing the country, jumping from 33%. Meanwhile the Opposition had begun to engineer defections

amongst BN leaders in the state of Sabah, casting doubt that the ruling BN coalition had secured the Sabah vote in its favour¹.

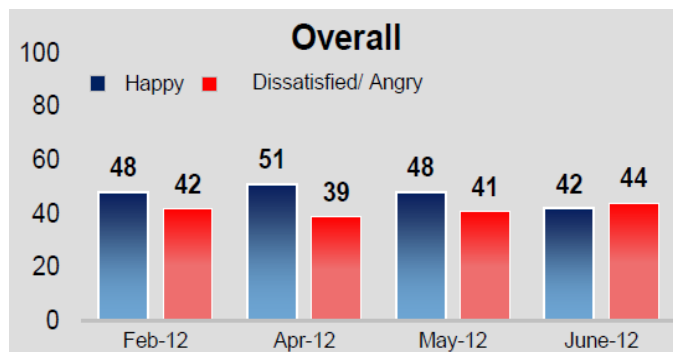
Figure 16. PM Najib's approval rating remains high at 64%, though falling from 71% in late 2011



Note: Respondents were asked "How satisfied or dissatisfied are you with the performance of Najib Tun Razak as Prime Minister?"

Source: Merdeka Centre

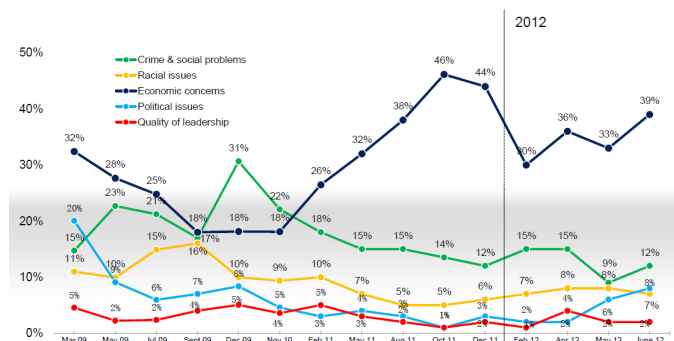
Figure 18. Approval for the government has fallen by 6pts...



Note: Respondents were asked "Some people say they are happy with the Government while others are dissatisfied and others say they are angry? Which one best describes how you feel?"

Source: Merdeka Centre

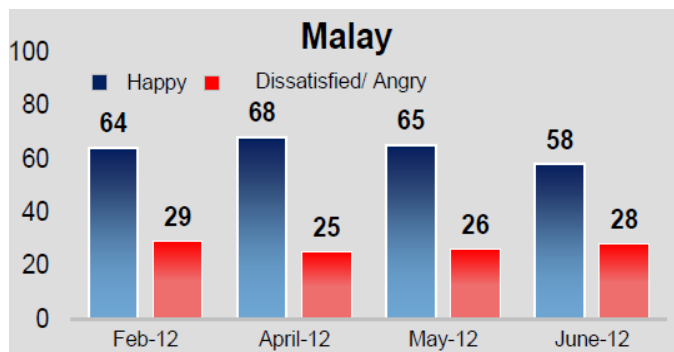
Figure 17. Economic concerns are increasingly the main problem cited by survey respondents



Note: Respondents were asked "Being as specific as you can, what is the number one problem facing people in this country today?"

Source: Citi Research

Figure 19. ...including amongst Malays



Note: Respondents were asked "Some people say they are happy with the Government while others are dissatisfied and others say they are angry? Which one best describes how you feel?"

Source: Merdeka Centre

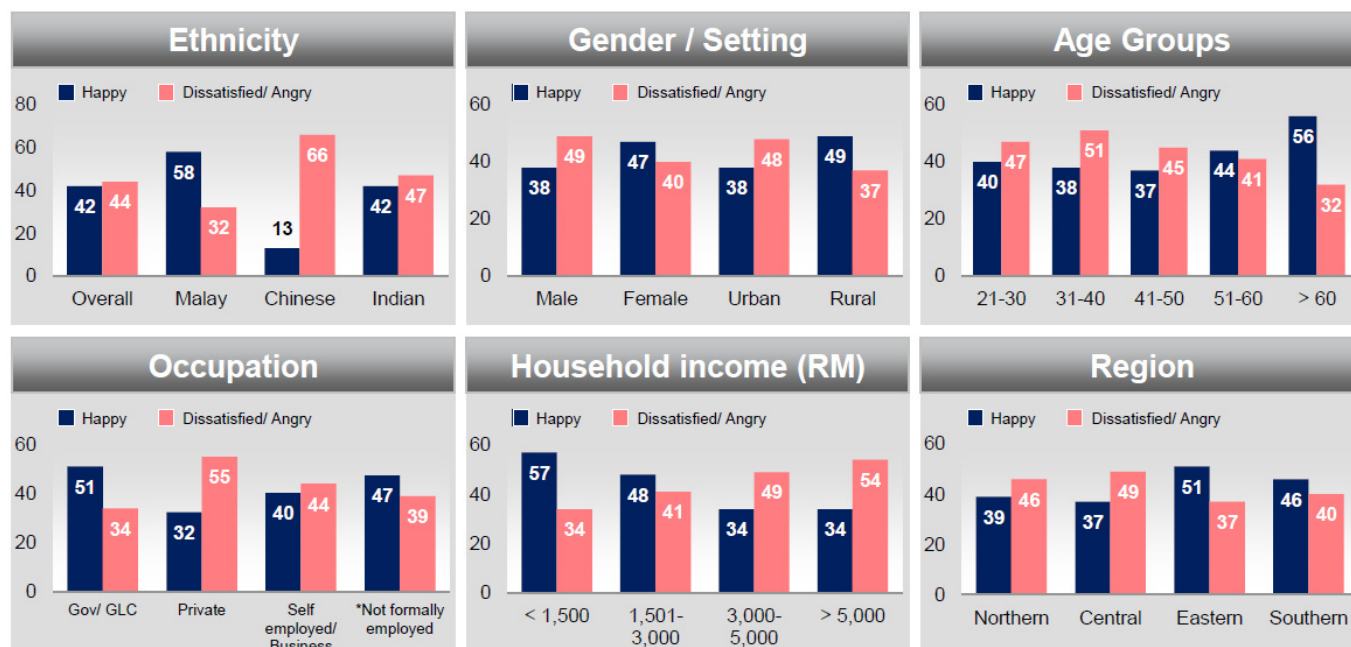
The details of the Merdeka Survey reveal who are the core government supporters as well as the swing voters who are most evenly split between government and opposition:

- By ethnicity, 58% of **Malays** were satisfied with the government vs. 32% dissatisfied. **Indians** appear to be the swing voters where the opposition has a slight advantage.
- By setting, 49% of **rural** voters were satisfied with the government vs. 37% dissatisfied. By contrast, only 38% of **urban** voters were satisfied vs. 48% dissatisfied.

¹ Jahabar Sadiq, "Sabah BN Leaders Exit Likely to Delay Polls, Say Sources", The Malaysian Insider (30 July 2012). Retrieved on 30 July 2012

- By age groups, 56% of **senior citizens** aged 60 and above were satisfied with the government vs. 32% dissatisfied. The swing voters appear to be **older voters** aged 51-60 (44% vs. 41%) as well as **young voters** aged 21-30 (40% vs 47%).
- By occupation, 51% of **government and GLC workers** were satisfied with the government vs. 34% dissatisfied while **voters not formally employed (homemakers, retirees, students, and the unemployed)** were also relatively satisfied (47% vs. 39%). The swing voters appear to be the **self-employed and business owners** (40% vs. 44%).
- By household income, 57% of **voters earning less than RM1,500/month** were satisfied with the government vs. 34% dissatisfied. The swing voters appear to be **voters earning between RM1,501-3000/month** (48% vs. 41%).
- By region, 51% of voters in **East Malaysia** (Labuan, Sabah and Sarawak) were satisfied with the government vs. 37% dissatisfied.

Figure 20. Perception towards the government by various categories of respondents



Note: Respondents were asked "Some people say they are happy with the Government while others are dissatisfied and others say they are angry? Which one best describes how you feel?"

Source: Merdeka Centre

Accordingly, the measures announced in Budget 2013 were almost methodically targeted at cementing the BN's grip over its core supporters while courting swing voters, though the electoral effectiveness of such handouts remains to be seen.

- A section of the Budget speech was devoted to "developing Bumputera entrepreneurs" (primarily the **Malays** but also including other indigenous races in **Sabah** and **Sarawak**), promising that RM9bn or 43% of the total infrastructure cost of the MRT project was reserved for Bumiputera contractors along with other measures for Bumiputera SMEs and small-scale entrepreneurs. The Budget speech also specifically earmarked support for the Malaysian **Indian** community in allocations to TEKUN (which provides loans for small-scale entrepreneurs) as well as RM50mn to train 3,200 Malaysian Indians in the estates.

- A slew of projects and handouts were promised and extended to the **rural** population. In contrast, urban measures appeared to be more concerned with development, i.e. public transport and provision of public services, though the 1%pt personal income tax cut will be to the first RM2,500-RM50,000 of annual income – or about RM200-RM4,000/month – providing disproportionate tax savings to these largely **urban middle class** swing voters.
- In appealing to **older and senior citizens**, the government appears to have limited itself to (not insubstantial) increased minimum pensions for pensioners who have served for at least 25 years and discounts on passport processing fees. Greater effort was made to reach out to the **youth**, including the rather blatant offer of one-off RM200 rebates for purchases of 3G smartphones.
- Higher minimum pensions also appeal to **government and GLC workers** on top of an additional month of civil servant bonus (half month to be paid out at end Dec-2012 and another half month in Jan-2013) and other measures for civil servants and the armed forces. There were measures to reduce the cost of education for **students**, including a Graduate Employability Blueprint to retrain **unemployed** graduates. Incentives for SMEs and small-scale entrepreneurs will also likely appeal to the **self-employed and business owners**.
- Households whose heads of household earn **less than RM3,000/month** will receive a second round of Bantuan Rakyat 1Malaysia (BR1M) handouts. In addition, the BR1M handouts have been extended to single unmarried individuals aged 21 and above earning not more than RM2,000/month.
- The government has allocated RM386mn under the new Price Uniformity Scheme to reduce the price discrepancies for essential goods in **East Malaysia** (Labuan, Sabah and Sarawak).

With the timing of many of the handouts converging on Jan-2013, we now suspect that elections will be delayed to next year to allow time for the fiscal fireworks to revive enthusiasm for the BN. Many of the handouts, subsidies, and assistances appear to have relatively short implementation periods and could be completed in a matter of months; the administrative groundwork for these measures likely already exist (such as the registry of households qualifying for the BR1M handouts) or could have been laid out in preceding months in preparation for the Budget. Given the increasingly skeptical electorate, it is unlikely that PM Najib will call for elections before he has delivered on the handouts he has promised and before he can take advantage of any feel-good factor.

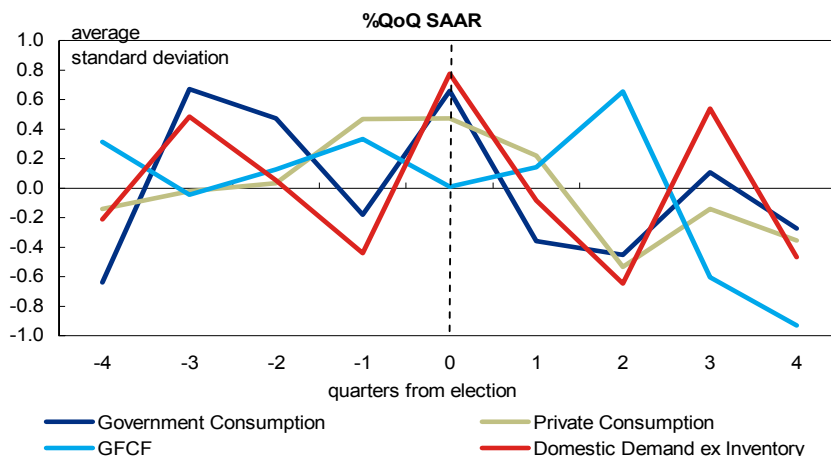
What Does The Budget Imply for Near-Term Growth Outlook?

Apart from garnering voter support, these fiscal carrots will prolong (and possibly expand) earlier countercyclical fiscal support provided in Budget 2012 for consumption, cushioning against spillovers from a worsening export slowdown into 2013. Seen from another angle, historically, domestic demand has typically fallen off in the quarter after elections. If elections are to be held in 1Q13, then it may be necessary to prolong fiscal support to avoid an unwelcome slowdown in consumption when exports are hit by headwinds such as a possible fiscal cliff in the US.

The measures earlier announced in Budget 2012 have proven effective. In 1H12, RM3.2bn of handouts, together with civil service wage hikes, allowed private consumption to accelerate from 7.3% in 4Q11 to 8.8% in 2Q12 despite lower CPO prices. In July 2007 for example, a 7.5-42% civil service pay hike, a 100% increase

in the civil servant cost of living allowance, together with record CPO prices, contributed to an acceleration in consumer spending to 12.1%YoY in 2H07 from 9% in 1H07. Into 2H12, the RM4bn of handouts and civil servant bonuses in 2H12 from Budget 2012 will likely contribute around 0.4-0.5% of GDP (assuming a marginal propensity to consume of 1), not including spillovers such as GLC pay hikes which tend to follow the civil service.

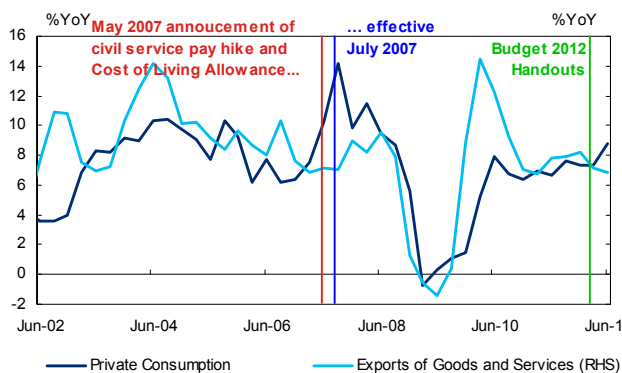
Figure 21. QoQ SAAR Growth in Quarters Before and After Elections



Note: Using the nine quarters surrounding the election (four quarters before, four quarters after, and the quarter of the election itself), we normalize the QoQ SAAR growth to the number of standard deviations from the mean for each election and then take the average standard deviations for each quarter across the four elections.

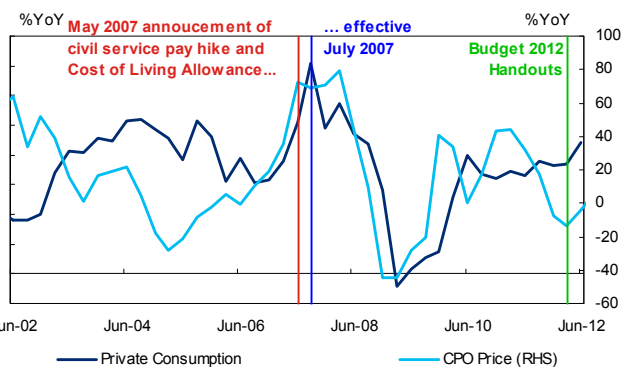
Source: CEIC, Citi Research

Figure 22. Budget 2012 handouts have succeeded in boosting consumption in 1H12, though not as aggressively as in 2007...



Source: CEIC, Citi Research

Figure 23. ...when CPO prices had reached new highs



Source: CEIC, Citi Research

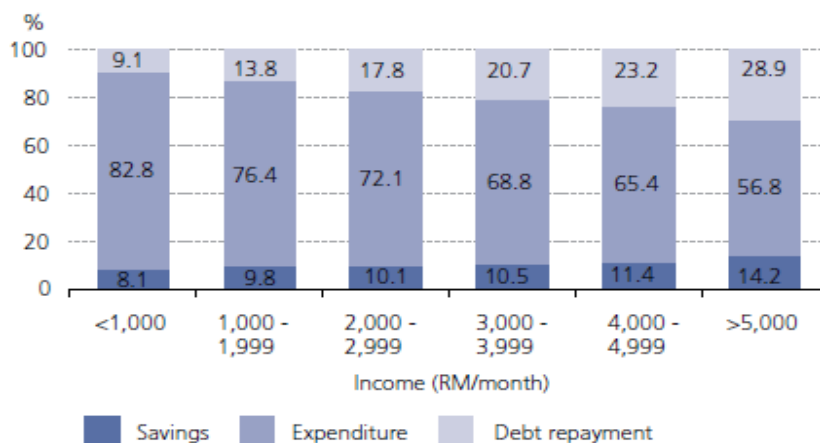
As the Budget 2013 measures target a broader portion of the population as compared to those in 2012, the impact on consumer spending could be possibly larger – and since these measures will be dished out in Jan 2013, the impact will be felt mainly in 1H13. Excluding the additional 1 month bonus for civil servants, we estimate the handouts to be dished out in Jan 2013 will lift consumer disposable incomes by RM3.9bn, or close to 0.9% of nominal private consumption in 2011. Adding another RM3bn for the civil servant bonuses, the cumulative

addition to consumer incomes could total 1.5% of private consumption in 2012. **Conservatively assuming a marginal propensity to consume of around 70%, the civil servant bonuses and handouts alone would effectively boost 2013 private consumption by close to 1%-pt.**

Note that this estimate has yet to include the boost to disposable incomes from the income tax cuts and earlier announced minimum wage hikes. With respect to the income tax cuts, the government noted that 170,000 taxpayers will be removed from paying tax, with sizeable tax savings for the remaining 1.6mn taxpayers. PM Najib illustrated that an unmarried young professional with a monthly income of RM5K/mth (or RM60K annually) will enjoy income tax savings of up to RM425 per person – or roughly tax savings of 0.7% of each taxpayers' gross incomes (and a larger % of disposable incomes). With regards to the minimum wage, we had earlier noted that assuming that the 3.2mn workers earning under RM700/m each see a RM200/m increase in wages, the annual increase in incomes will be around RM7.7bn or 0.9% of GDP (1.9% of PCE). Given an implementation of six to twelve months, the minimum wage – if fully implemented and properly enforced – could start seeing an impact on consumption in early 2013.

Finally, as the Budget measures are finely targeted at those generally earning less than RM3K/M, this may also provide temporary fiscal relief for the most indebted group of consumers who may otherwise see their consumption crimped by credit constraints. For example, the Bank Negara 2011 Financial Stability Report noted that those earning less than RM3K/m account for 23% of banks' exposures to households, with the majority concentrated in vehicle and personal financing. Leverage positions for this group were between 4.4-9.6 times annual incomes, compared to 2.3-3.3 times for upper income groups. Estimates suggest that savings for this group would be sufficient to sustain spending and debt repayment for only three months in the event of a complete loss of income or absence of financial assistance. While a tight labour market suggests that this worse case is not about to materialize, the handouts will nonetheless alleviate what would otherwise be a tight cash flow for these households.

Figure 24. Household Sector: Savings and Expenditure by Income Group



Source: Bank Negara Malaysia Financial Stability Review 2011, Department of Statistics

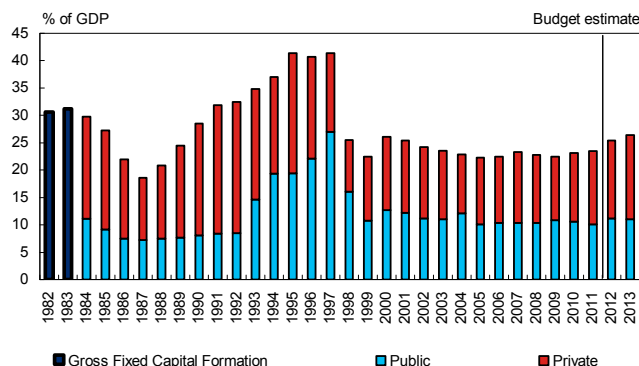
Figure 25. Budget 2013 measures for households, split by voter category (bolding indicates likely swing voters)

Voter Category	Budget 2013 Measures
Bumiputeras (Malays 58% satisfied vs 32% dissatisfied)	See business measures for Bumiputeras in Fig 30
Indians (42% vs 47%)	RM350 million allocation to Tabung Ekonomi Kumpulan Usaha Niaga (TEKUN), including RM50 million to the Malaysian Indian community RM50 million allocation to train 3,200 Malaysian Indian students in the estates to equip them with skills in line with market demand
Rural (49% vs 37%)	RM230 million allocated to continue providing living allowance of RM200 per month to 55,000 registered fishermen and incentive of RM0.10-0.20 per kilogramme to encourage fish landings at licensed jetties nationwide Government to expand the Rural Transformation Centre to Melaka, Johor, Pahang and Sarawak to provide integrated services. Government to upgrade Medan Info Desa to Mini-RTCs nationwide RM4.5 billion allocation for various rural infrastructure development projects: [1] RM1.2 billion to develop 441 kilometres of rural roads and village link road projects to benefit 220,000 villagers. [2] RM1.6 billion for rural utility infrastructure projects which involves water supply to 24,000 houses and electricity supply to 19,000 houses. [3] RM137 million to finance Program Desa Lestari involving 29 villages nationwide and benefiting 38,000 villagers. [4] RM88 million for economic development programmes and water supply projects for the Orang Asli community
Urban (38% vs 48%)	RM200 million Urban Transformation Programme (UTP) to develop the urban community to ensure seamless public and private services Government to launch RapidKuantan on 1 December 2012 to provide high-quality bus transport services in Kuantan
Older and Senior Citizens (Age 51-60 44% vs 41%, Age >60 56% vs 32%)	Minimum pension increased from RM720 to RM820 for pensioners who have served for at least 25 years, effective <u>1 January 2013</u> . Addition RM60 million a year allocated, benefiting 50,371 pensioners including derivative pension recipients For senior citizens and children aged 12 and below, Government proposes to reduce processing fee of a 5-year passport by 50%, from RM300 to RM150, while processing fee for 2-year passport reduced from RM100 to RM80, effective <u>January 2013</u>
Youths (Age 21-30 40% vs 47%)	RM50 million to establish New Entrepreneur Foundation (NEF) to assist young ICT entrepreneurs SME Bank to provide RM50 million to establish Young Entrepreneurs Fund to provide soft loans aimed at youths aged 30 and below with 2% interest rate subsidy for loans up to RM100,000 with 7-year repayment period RM300 million to introduce Youth Communication Package providing youths aged 21 to 30 years with monthly income of RM3,000 and below a one-off rebate of RM200 for purchase of one unit of 3G smartphone from authorised dealers, benefiting 1.5 million youths
Government and GLC Workers (51% vs 34%)	Government to improve career advancement opportunities through time-based promotion for Privates to Lance Corporals, and for Lance Corporals to Corporals within period of eight years for those who fulfil necessary requirements and based on performance Special incentive of RM200 per month to all military personnel totalling 125,708, effective 1 January 2013. RM301 million allocated Services allowance revised from RM4.00 per hour to RM6.00 for ordinary members, and from RM5.80 to RM7.80 for officers One-off RM1,000 to assist former members of armed forces who have opted for early retirement; served less than 21 years; and did not receive any pension. RM224 million allocation to be equally shared by Government and Armed Forces Fund Board Government to introduce Group Insurance Coverage Scheme to serving armed forces and police personnel providing maximum insurance coverage up to RM15,000 to almost 242,000 armed forces and police personnel. RM12 million allocated Government will reduce cost of living of trainees undergoing pre-service courses at first degree, diploma and certificate level by increasing the pre-service allowance for 31,135 trainees. RM84.2 million allocated Additional one month civil servant bonus. Half month bonus to given end-of December 2012 and another half month in <u>January 2013</u>
Not formally employed (47% vs 39%): Students	RM2.6 billion allocation to continue providing special allocations to primary and secondary school students RM540 million allocation for second distribution of Schooling Assistance of RM100 to all primary and secondary students, to commence from <u>January 2013</u> RM325 million allocation to increase value of 1Malaysia Book Voucher programme for all students in institutions of higher learning (IPT) and at pre-university level from RM200 to RM250, benefiting 1.3 million students Existing tax relief on children's higher education amounting to RM4,000 per person to be increased to RM6,000, commencing from year of assessment 2013 Current relief of RM3,000 for savings in the National Education Savings Scheme (SSPN) to be increased to RM6,000 Incentives to facilitate repayment of PTPTN study loan
Not formally employed (47% vs 39%): Unemployed	Government to launch Graduate Employability Blueprint by end-2012 to assist unemployed graduates. Government will establish Graduate Employability Taskforce with allocation of RM200 million
Not formally employed (40% vs 44%): Self-Employed and Business Owners	See business measures for SMEs in Fig 30
Lower Income Groups (Income <RM1,500 57% vs 34%, RM1,501-3,000 48% vs 41%)	RM3 billion allocation for second distribution of Bantuan Rakyat 1Malaysia (BR1M 2.0). Eligibility remains unchanged: households where the head of the household earns less than RM3,000. BR1M extended to single unmarried individuals aged 21 and above and earning not more than RM2,000 a month. Estimated to benefit 4.3 million households and 2.7 million single unmarried individuals, to be paid effective <u>January 2013</u> . New applicants may register commencing November 2012 Malaysian Communications and Multimedia Commission (SKMM) to provide RM150 million allocation to establish 100 1Malaysia Internet Centres from 2013 to 2015 in suitable areas in the city such as PPR locations Individual income tax rate to be reduced by 1 percentage point for each grouped annual income tax exceeding RM2,500 to RM50,000. Tax cut will remove 170,000 taxpayers from paying tax from current 1.7 million taxpayers Government to extend 50% discount on KTM Komuter fares to all Malaysians with monthly income of RM3,000 and below from current coverage of the disabled, retirees and students
East Malaysians (51% vs 37%)	RM386 million allocation to ensure prices of essential goods in Sabah and Sarawak as well as in Labuan are sold at lower prices through opening of 57 KR1M and to bear cost of delivering products from Peninsular Malaysia to Sabah, Sarawak and Labuan including the interior areas 50% discount on ferry charges to all passengers commuting between Labuan and Sabah/Sarawak

Source: Budget 2013, Citi Research

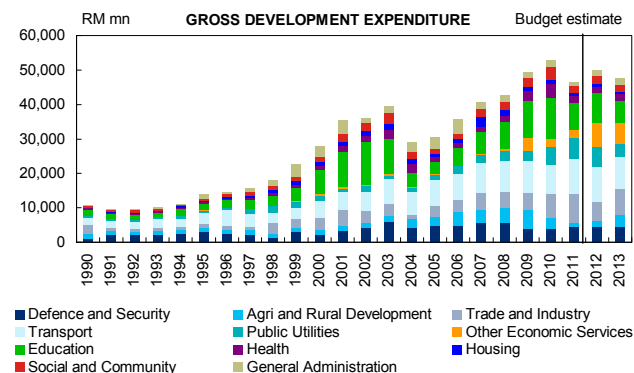
With private investments already on an upswing, measures for businesses were targeted rather than broad-based. With the private investment share of GDP already at a 15 year high and the government confident that the existing momentum from the ETP (which is 92% GLC and privately funded) will likely carry through into 2013 (private investment is projected to accelerate to 13.3% in 2013 from 11.7% in 2012), there was little need for traditional fiscal pump-priming. This enabled a 4.2% cut in development spending, with social services (especially education and training) and public utilities bearing the brunt of cuts, possibly reflecting the completion of earlier announced projects. In contrast, agriculture and trade and industry saw substantial increases in development spending – the former likely reflecting the political imperatives in cementing rural voter support.

Figure 26. Gross Fixed Capital Formation



Source: MoF, CEIC, Citi Research

Figure 27. Gross Development Expenditure



Source: MoF, CEIC, Citi Research

Reflecting the cut in development spending, in a departure from previous Budgets, apart from RM500mn allocated for the River of Life project, no other major projects were named in the Budget, perhaps suggesting less overt support for the construction sector from the Federal coffers than in the past. This was probably unnecessary in any case given the current strength of construction spending, which will likely be sustained given the pipeline of previously announced infrastructure projects.

Nonetheless, targeted support for the politically important Bumiputera contractors were announced, with a RM9bn quota in the MRT project, RM1bn to be provided by the SME Bank to the Bumiputera Financing Fund, an extension to the duration of the Working Capital Guarantee Scheme for SMEs to Dec 31 2013 while expanding the scheme to High Performing Bumiputera companies, and an extension of a loan scheme for small scale Bumiputera entrepreneurs.

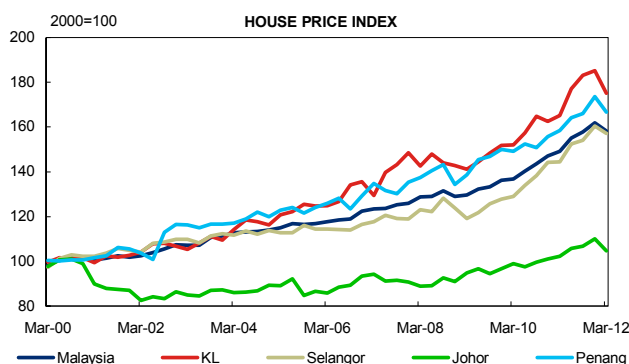
Downstream oil and gas companies were one of the key beneficiaries of tax incentives. To help develop the petroleum downstream sector, an Investment Tax Allowance of 100% for a period of 10 years will be provided to qualified companies. This will add to the US\$20bn worth of O&G investments that are already driving the bulk of the private investment boom, including those in the Pengerang Integrated Petroleum Complex.

Financial services, especially for conventional and Islamic debt capital markets, received significant help in the Budget. In particular, to encourage companies to issue retail bonds and retail sukuk, additional expenses incurred in the issuance of retail bonds and retail sukuk will be given a double deduction for 4 years from 2012-2015. Individual investors will also be given stamp duty exemptions for transactions of retail bonds and sukuk.

Also noteworthy were tax incentives to promote Malaysia as an international financial hub and attract FDI, with the launch of the Tun Razak Exchange (formerly known as the KL International Financial District). To encourage major international FIs to invest in KL, a host of tax incentives, including income tax exemption for 10 years for TRX status were announced. While the formidable competition from Singapore – and associated brain drain – may cast some doubt on KL's financial centre ambitions, Malaysia's strength in niche areas like Islamic finance alongside tightening in immigration policies in Singapore (including on professionals) provide Malaysia a window of opportunity to divert some business investments from Singapore. On the flip side however, the tax incentives may well result in a cannibalization of financial investments from other parts of KL, possibly exacerbating the oversupply in office space.

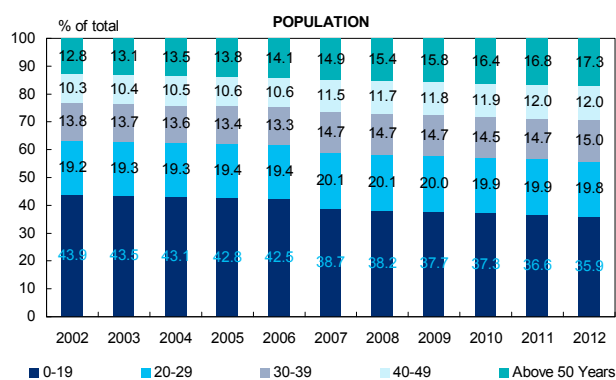
The hike in the Real Property Gains Tax may deter some speculators, but will probably be only mildly negative for property developers. For a start, the proposed hike (to 10% from 5% for sales within 2-5 years, and 15% from 10% for houses below 2 years) was not as aggressive as what some market participants had feared – of a hike up to 30%. Moreover, with completion periods typically exceeding two years and difficulties in flipping properties before completion, most investors will probably be spared the highest RPT rate of 15%. More importantly, as we had argued, it is unclear how effective these additional measures will be in curbing demand. While speculation has been blamed for pushing up house prices, the problem is more fundamentally a lack of supply from a shortfall in completions facing burgeoning demand from a young population. The supply side measures announced in the Budget, including the RM500mn Housing Facilitation Fund to build houses in collaboration with private developers, will therefore probably be more effective in tackling this issue. We understand that developers are already trying to cover the shortfall by launching more developments.

Figure 28. House Price Index



Source: CEIC, Citi Research

Figure 29. Those Aged 20-29 Constitute Around 20% of the Population



Source: CEIC, Citi Research

Figure 30. Budget 2013 measures for businesses

Sector	Budget 2013 Measures
Entry Point Projects	RM3 billion allocated for implementation of entry point projects, including RM1.5 billion for agriculture projects, RM500 million for River of Life project (beautification of Klang River) and additional RM300 million for replacement of water pipelines and sewage
Private Financing Initiatives	RM6 billion allocated under Private Financing Initiatives (PFI 2) to implement various projects and programmes
SMEs	<p>RM1 billion to facilitate SMEs' access to financing provided under SME Development Scheme to be managed by the SME Bank</p> <p>SME Bank to provide RM200 million for Halal Industry Fund to finance working capital of participating SMEs</p> <p>Group insurance coverage scheme proposed for hawkers and owners of small businesses registered with the Companies Commission of Malaysia to provide maximum coverage of up to RM5,000. Government will finance this Scheme with allocation of RM16 million a year</p> <p>Perbadanan Nasional Berhad (PNS) to introduce Business in Transformation programme to support efforts to modernise the operations of hawkers and small businesses, providing soft loans of up to RM25,000 for licensees and RM500,000 for licensors</p>
Oil and Gas	<p>Investment Tax Allowance of 100% for 10 years provided to companies investing in refinery activities on petroleum products</p> <p>Global Incentive for Trading (GIFT) programme enhanced with 100% income tax exemption on statutory income for first 3 years of operations for LNG trading companies. Commodity trading approved under GIFT extended to include other commodities such as agriculture, refined raw materials, base minerals and chemicals</p>
Tourism	<p>RM358 billion allocation to increase tourist arrivals by 42% to 26.8 million arrivals</p> <p>Income tax exemption extended for 3 years for tour operators who bring in at least 750 foreign tourists or handle 1,500 local tourists a year</p>
Agriculture	RM30 million allocated for agricultural development programmes, RM75 million allocated to increase output of food and health products, RM432 million allocated under NKEA for oil palm replanting programmes, RM127 million allocated for development of high-value oleo derivatives
Capital and Financial Markets	<p>Securities Commission (SC) will provide a framework on issuance of AgroSukuk for companies engaged in agriculture sector. Government proposes that expenses for issuance of AgroSukuk be given double deduction for four years effective from year of assessment 2012 to 2015</p> <p>Government proposes that additional expenses incurred in issuance of retail bonds and retail sukuk be given double deduction for four years effective from year of assessment 2012 to 2015</p> <p>Individual investors to be given stamp duty exemption on instruments relating to transactions of retail bonds and retail sukuk</p> <p>SC will establish a Capital Market Promotion Centre to provide consistent initiatives to position Malaysia as a centre of investment and fund raising</p> <p>SC will introduce Graduate Representative Programme to train 1,000 graduates to meet needs of securities and derivatives industry</p>
Business Trusts	<p>Government proposes business trusts be given same tax treatment as companies and that the transfer of any business, asset and real property to a business trust be given stamp duty exemption and real property gains tax exemption at the early stage of the establishment of a business trust</p> <p>RM400 million allocated to Danajamin Nasional Berhad (Danajamin) to provide guarantee facilities to viable companies to obtain funds from bond market at a reasonable cost</p> <p>RM100 million provided through the Capital Market Development Fund under the SC to Capital Market Foundation to increase competency and capability of companies to compete in a more dynamic capital market</p>
Corporate Wakaf	Malaysian Wakaf Foundation under Department of Awqaf, Zakat and Hajj (JAWHAR) to formulate Corporate Wakaf master plan
Bumiputeras	<p>RM9 billion or 43% of total infrastructure cost of the MRT project has been allocated to Bumiputera companies</p> <p>SME Bank will provide RM1 billion to Bumiputera Financing Fund</p> <p>Government will extend duration of Working Capital Guarantee Scheme for SMEs which guarantees up to a maximum of RM2.5 million of working capital to qualified companies until 31 December 2013, expand this scheme to High-Performing Bumiputera (TERAS) companies, and increase companies' shareholders fund eligibility from RM10 million to RM20 million</p> <p>RM350 million allocation to Tabung Ekonomi Kumpulan Usaha Niaga (TEKUN), including RM50 million to the Malaysian Indian community, to provide small-scale entrepreneurs with quick and easy access to loan facilities</p>
Pre-Schools	<p>RM1.2 billion allocated for pre-school education to Jabatan Kemajuan Masyarakat, MOE, PERMATA and Dept of National Unity and Integration</p> <p>RM380 million allocated to MOE for placement of kindergarten teachers</p> <p>Incentives for pre-school and childcare services: [1] Launching grant of RM10,000 to assist operators of Early Childhood Care and Education (ECCE) private centres in opening new high quality pre-schools. 1,000 new private ECCE centres estimated to benefit. [2] Double deduction on allowance or subsidies provided to employees and expenses for maintenance of childcare centres be given to employers. [3] Income tax exemption for 5 years and industrial building allowance at rate of 10% a year to be given to operators of pre-school and private childcare centres. [4] Income tax exemption for 5 years and industrial building allowance at rate of 10% a year to be given to operators of private pre-schools</p>
Intellectual Property	Valuation model to be created to enable intellectual property rights (IPR) to be valued and commercialised in the market as well as utilised as collateral to obtain financing from financial institutions: [1] Establishment of RM200 million Intellectual Property Financing Fund scheme offered through Malaysian Debt Ventures Berhad. Government to provide 2% interest rate subsidy and guarantee of 50% through Credit Guarantee Corporation Malaysia Berhad. [2] RM19 million allocation for training programmes for local intellectual property evaluators conducted by Intellectual Property Corporation of Malaysia (MyIPO) as well as create an intellectual property right market platform
Research and Development	<p>Government will allocate RM600 million to five research universities to conduct high-impact research in strategic fields such as nanotechnology, automotive, biotechnology and aerospace</p> <p>To boost the commercialisation of R&D findings of public institutions, the Government proposes that the current tax incentives for the commercialisation of resource-based R&D findings be extended to commercialisation of non-resource based findings which are products promoted under the Promotion of Investment Act 1986: [1] The company which invests in its subsidiary company that undertakes the commercialisation of R&D findings be given a deduction equivalent to the total investment made in that subsidiary. [2] The subsidiary company that undertakes the commercialisation of R&D findings be given income tax exemption of 100% on the statutory income for a period of 10 years</p>
Venture Capital	Government proposes that a deduction equal to the amount of investment made by an angel investor in a venture company be allowed to be set off against all his income
Green Technology	Additional RM2 billion and three year extension of application period to 31 December 2015 for RM1.5 billion Green Technology Financing Scheme (GTFS) fund to enable companies which are producers and users of green technology to obtain soft loans, with Government subsidising 2% of the interest rate and providing guarantee of 60% on the amount of financing
Real Property Gains Tax (RPGT)	Real property gains tax (RPGT) from the disposal of properties made within a period not exceeding 2 years from the date of purchase will be taxed at rate of between 15% and 10% of disposal of property within period of 2 to 5 years. For property disposed after 5 years from the date of acquisition, RPGT is not applicable. Gains from disposal of one residential property once in a lifetime and disposal of properties based on love and affection between husband and wife, parents and children, grandparents and grandchildren exempted from RPGT

Source: Budget 2013, Citi Research

How does Budget 2013 tackle medium-term challenges?

With the political circus of impending General Elections still not over, medium-term reforms have unsurprisingly remained in the shadows this year.

Despite what is a seemingly genuine desire among some policymakers for fundamental reforms, decisive moves are impossible with elections so close and the Opposition biting at its knees. The Opposition has not only vowed to shelve GST implementation but has also claimed that it is the right of the people to receive subsidies for fuel and other necessities – which suggests a possible reversal of subsidy rationalization. It is not hard to see how the election has paralyzed reform.

Indeed, Budget 2013 could only make incremental steps to tackle longstanding issues, keeping to tried-and-tested methods, rather than any game-changing measures or reforms. This is not to say there was no progress. Greater emphasis on education and training can help address the human capital deficit. More explicit hints of GST implementation and subsidy rationalization were politically brave, even as they appeased ratings agencies – the cuts in personal income taxes could possibly be a further hint of future GST implementation. Measures to improve home affordability however may worsen concerns over household leverage. **Deeper reforms are clearly waiting for elections to be over.**

Greater Emphasis on Education and Training

As we had expected, there was a heavy emphasis on human capital development, but the devil lies in the details. The human capital deficit had been brought to the fore once again with the recent launch of the Education Blueprint 2013-2025 and the government continued to build on this with announcements of more funding and new measures for teacher training, school infrastructure, pre-schools, and skills training. We think some of these measures could make some progress towards addressing key issues – the additional RM500mn allocated to “enhancing teaching skills” for example could help improve the quality of teachers, though the lack of details still leaves much to the imagination. The additional RM1bn allocated to the Special Fund for the Building, Improvement and Maintenance of Schools could also provide desperately needed “hardware” to poor students in rural areas but does not fundamentally improve the “software” of Malaysia’s education system which causes problems in even well-equipped urban schools.

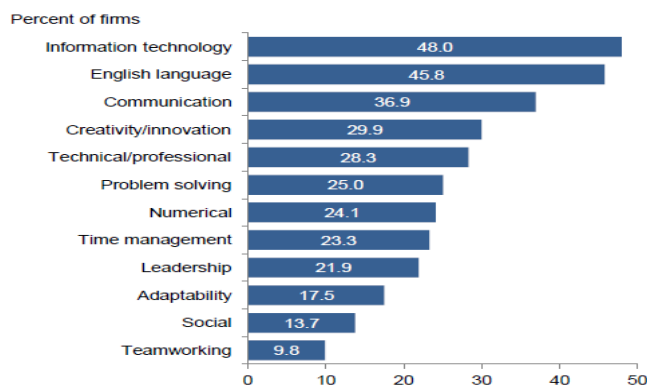
The need to address the poor “software” is highlighted by the fact that graduates need to be retrained with the necessary skills to be employable – as evidenced by the need for a Graduate Employability Blueprint in Budget 2013. The World Bank’s investment climate assessment for example has highlighted poor skills quality as the top investment climate obstacle for about 40% of 1,400 firms surveyed while Malaysian firms also identified the lack of non-routine skills as key constraints in the 2007 Productivity and Investment Climate Survey – not because there were not enough graduates but because the graduates did not have the necessary skills. The World Bank’s recent investment climate assessment also pointed to a tight labour market for skills in Malaysia – a 2007 survey of Malaysian manufacturers found that it took an average of a long six weeks to recruit a professional worker and that this had in fact worsened slightly from 2002. As a result, graduate unemployment is high, even for Science and Business graduates, and there is little that can be done after the fact except to re-train them.

Figure 31. Budget 2013 measures to improve human capital

Malaysia Education Blueprint 2013 – 2025	Another RM500 million allocated to enhance teaching skills in core subjects such as Bahasa Malaysia, English, Science and Mathematics through the Higher Order Thinking Skills approach. Allocation includes establishment of an Education Delivery Unit to monitor and evaluate effectiveness of the transformation plan
	Additional RM1 billion for RM1 billion Special Fund for the Building, Improvement and Maintenance of Schools, of which RM400 million will be channelled to national schools; RM100 million to national-type Chinese schools; RM100 million to national-type Tamil schools; RM100 million to mission schools; RM100 million to Government-assisted religious schools; RM100 million to boarding schools; and RM100 million to Maktab Rendah Sains MARA
Strengthening the Role of Pre-Schools	RM1.2 billion allocated for pre-school education to Jabatan Kemajuan Masyarakat, MOE, PERMATA and Department of National Unity and Integration
	RM380 million allocated to MOE for placement of kindergarten teachers
	Incentives for pre-school and childcare services:
	Launching grant of RM10,000 to assist operators of Early Childhood Care and Education (ECCE) private centres in opening new high quality pre-schools. 1,000 new private ECCE centres estimated to benefit
	Double deduction on allowance or subsidies provided to employees and expenses for maintenance of childcare centres be given to employers
	Income tax exemption for 5 years and industrial building allowance at rate of 10% a year to be given to operators of pre-school and private childcare centres
	Income tax exemption for 5 years and industrial building allowance at rate of 10% a year to be given to operators of private pre-schools
	Government to implement pilot project for pre-schools for disabled children (TASKA OKU)
Skills and Training	RM3.7 billion allocated to train students in technical and vocational fields
	Government to launch Graduate Employability Blueprint by end-2012 to assist unemployed graduates. Government will establish Graduate Employability Taskforce with allocation of RM200 million
	RM440 million allocation to Skills Development Fund Corporation (PTPK) to provide loans for trainees to undergo skills training. Nearly 40,000 trainees estimated to benefit
	RM366 million allocation to upgrade and purchase equipment for Industrial Training Institutes and National Youth Vocational Institutes (IKBN)
	Implementation of various skills training programmes, focusing on selected industries including oil and gas, shipping, ICT, creative and biotechnology
	RM50 million allocation to train 3,200 Malaysian Indian students in the estates to equip them with skills in line with market demand, conducted by Industrial Training Institutes and colleges under the Dual National Training Scheme

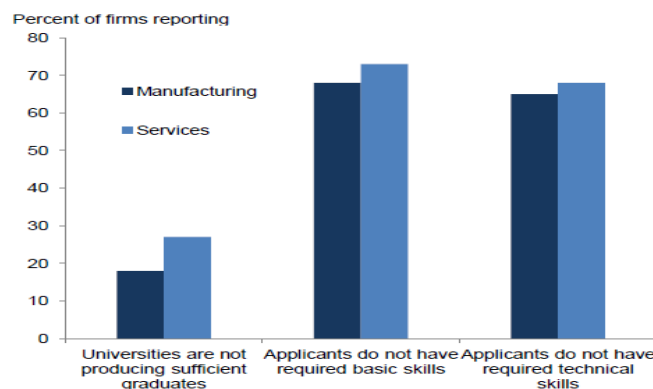
Source: Budget 2013, Citi Research

Figure 32. Non-routine and other soft skills are a constraint for firms...



Source: World Bank

Figure 33. ...despite the fact that there are enough graduates



Source: World Bank

As we have argued before, the solution to Malaysia's human capital deficit is unlikely to be as simple as increasing education spending and providing more incentives. In addition to the poor quality of teaching, the education system is hampered by inadequate emphasis on English language skills, declining standards from the rush to admit more students into universities, and affirmative action policies favouring the Bumiputera. **Any attempt to meaningfully address the human capital deficit would almost certainly be met with strong resistance, especially from the Malay rights hardliners.**

There were also practically no new measures to attract foreign talent. Compared to Budgets 2010, 2011, and even 2012 where the sole effort in this

regard was to allow expatriates to withdraw their Employees Provident Fund (EPF) contributions for the purchase of a house, the need to attract foreign talent or arrest the brain drain out of Malaysia appears to have received little attention this year. We think this was likely a missed opportunity. Building upon past measures to attract overseas talent or the large Malaysian diaspora – lowering tax rates for experts and relaxing immigration criteria – could be a timely measure to attract the large numbers of Malaysian professionals working in Singapore, especially given Singapore's tightening of immigration rules over the last two years.

Figure 34. Previous Budget measures to attract and retain human capital

Budget	Area	Measure
Budget 2010	Permanent Residency	To simplify the granting of Permanent Residency to highly talented and skilled individuals to accelerate technology transfers and the transformation process: [1] Visas will automatically be granted to working and dependent expatriate family members within 14 days; and [2] PR status will be extended to foreign men married to Malaysian women
	Iskandar Development Region	Income tax of workers residing and working in the Iskandar development region to be at 15% vs. 26% for the rest of the country's residents
Budget 2011	Talent Corporation	Establishment of a Talent Corporation to lure foreign talent to Malaysia as well as retain talent from brain drain
	Permanent Residency	Minimum length of residency required before applying for permanent residency shortened from 10 to 5 years
Budget 2012	Expatriate Home Ownership	Expatriates allowed to withdraw their Employees Provident Fund (EPF) contributions for the purchase of a house, similar to the facility available to Malaysians.

Source: Budget speeches (2010, 2011, 2012)

Hints of GST Implementation and Subsidy Rationalization

We had thought any mention of GST implementation or subsidy rationalization would be deemed politically toxic, but PM Najib surprised positively on this front. Though the word “GST” was still conspicuously absent from the Budget speech, PM Najib noted that “the transition from income based taxation system to a more comprehensive and fair taxation system will eventually benefit the *rakyat*”. He also noted in the speech that

“Government is currently undertaking a subsidy rationalisation initiative and gradually shift the provision of the bulk of subsidies that lead to leakages, and benefit the high-income group, to targeted subsidies under this principle. In reality, subsidies continue to be given to groups that truly need the subsidies. If the Government continues to provide the bulk of subsidies, it will adversely affect the financial position of the country, and causing the rakyat to bear the consequences, as has been in other countries. As a responsible Government, we will never allow this to occur”

PM Najib then announced a RM0.20/kg cut in the sugar subsidy to RM0.34/kg. As we noted earlier, the savings from the cut are small relative to the overall subsidy bill and PM Najib did attempt to deflect any potential political flak for the cut by justifying it on grounds of healthcare concerns. **Nonetheless, we thought that even any token mention of GST implementation and subsidy rationalization was politically brave, even as it appeased rating agencies.**

The targeted 1%pt personal income tax cut for lower and middle income groups may be a precursor to further cuts to top personal tax rates. Cuts in top personal tax rates would also help Malaysia draw in badly-needed talent. Historically, top personal income tax rates have also tended to align themselves with corporate income tax rates, albeit with a lag.

Figure 35. Top Personal Income Tax Rates

%	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
China	45	45	45	45	45	45	45	45	45	45
Hong Kong	15.5	16	16	16	16	15	15	15	15	15
India	30	30	30	30	30	30	30	30	30	30
Indonesia	35	35	35	35	35	35	30	30	30	30
Korea	36	36	35	35	35	35	35	35	35	38
Malaysia	28	28	28	28	28	28	27	26	26	26
Pakistan	30	30	30	30	20	20	20	20	20	20
Philippines	32	32	32	32	32	32	32	32	32	32
Singapore	22	22	21	20	20	20	20	20	20	20
Taiwan	40	40	40	40	40	40	40	40	40	40
Thailand	37	37	37	37	37	37	37	37	37	37
Vietnam	50	40	40	40	40	40	35	35	35	35

Source: KPMG

Figure 36. Malaysia Historical Corporate and Personal Income Tax Rates

Year	Corporate Tax Rate (%)	Top Personal Tax Rates (%)
1992	35	35
1993	34	35
1994	32	35
1995	30	32
1996	30	30
1997	30	30
1998	28	30
1999	28	30
2000	28	29
2001	28	29
2002	28	28
2003	28	28
2004	28	28
2005	28	28
2006	28	28
2007	27	28
2008	26	28
2009	25	27
2010	25	26
2011	25	26
2012	25	26

Source: KPMG, Citi Research

If a cut is indeed in store for top personal income tax rates, this provides further evidence that GST implementation is definitely in the cards after elections. Pemandu estimates that a 4% GST would result in net revenue gains of RM6.3bn in the first two years of implementation while a 5% GST would yield RM9.7bn and a 7% GST would result in RM25.7bn. As the GST would replace existing 6% sales tax, increases in the GST rate above 6% would result in much higher revenues, i.e. the relationship between GST rates above 6% and revenues is non-linear.

Affordable Housing Nudging Household Debt in Wrong Direction?

Once again, the focus on spurring near-term consumption and home ownership raises the risk that household debt moves in the wrong direction. We had expected that the Budget would focus on keeping housing affordable, even if largely for political signaling effects, given the issue is politically sensitive to young voters. Despite the dip in home prices in 1Q12 (the latest quarter for which data is

available), especially in Johor, KL, Selangor and Penang, this has not stopped the *perception* that young working adults have been increasingly priced out of the market. Unfortunately, the slew of measures to increase home ownership will likely only encourage lower and middle income households to take on more debt than would be prudent.

Figure 37. Budget 2013 measures to increase home ownership

RM1.9 billion allocation to build 123,000 affordable housing units in strategic locations, implemented by PR1MA, Syarikat Perumahan Nasional Berhad (SPNB) and Jabatan Perumahan Negara

PR1MA to spend RM500 million to build 80,000 houses in major locations nationwide with selling price ranging between RM100,000 and RM400,000 per unit. Among the locations are Kuala Lumpur, Shah Alam, Johor Bahru, Seremban and Kuantan

PR1MA to provide RM500 million Housing Facilitation Fund to build houses in collaboration with private housing developers. House prices under this programme will be 20% lower than market price and distributed through an open balloting system

RM320 million allocation through SPNB to build 22,855 residential units including low and medium-cost apartments, Rumah Mesra Rakyat and Rumah Mampu Milik. SPNB's housing projects, which will be implemented immediately, include construction of 1,855 medium-cost apartment units with a built-up area of 850 square feet in Shah Alam and Sungai Buloh. These units will be sold at about RM120,000 to RM220,000 per unit

SPNB to build 21,000 houses under Rumah Mesra Rakyat programme priced at RM65,000 per unit with a subsidy of RM20,000 as well as a 2% subsidy on interest rate

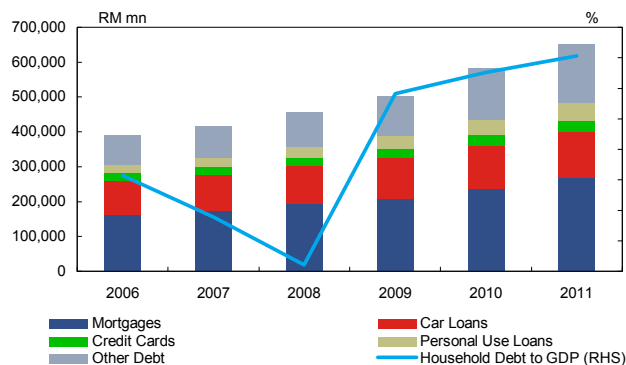
RM543 million allocation for Jabatan Perumahan Negara to implement 45 projects under Rakyat Housing Programme (PPR) involving 20,454 units which will be constructed through the Industrialised Building System (IBS) and to be sold at price between RM30,000 and RM40,000 per unit, much lower than market price of about RM120,000 per unit. Government will allocate 20% of PPR houses to public sector employees and 1% to the disabled

To enable more Malaysians to own their first residential property, My First Home Scheme to be improved by increasing income limit for individual loans from RM3,000 to RM5,000 per month or joint loans of husband and wife of up to RM10,000 per month. Requirement for a savings record equivalent to three months installment and minimum employment of six months to be abolished

Extension of 50% stamp duty exemption on instrument of transfer agreements and loan agreements for purchase of the first residential property of up to RM350,000 to 31 December 2014. Price limit on residential properties to be raised to RM400,000

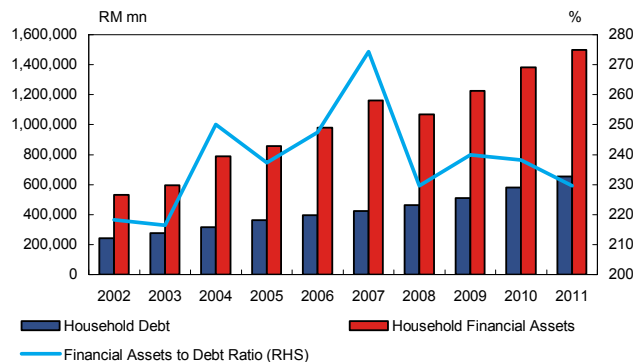
Source: Budget 2013, Citi Research

Figure 38. Household debt rose to 74.1% of GDP in 2011 (2010: 73.0%); we estimate mortgages account for about 40% of household debt



Source: CEIC, Citi Research

Figure 39. Household financial assets have declined relative to household debt in the last two years



Source: CEIC, Citi Research

As with the last two Budgets, of particular concern is the proposed relaxation of eligibility criteria for the My First Home Scheme, which guarantees for first-time house buyers with monthly household incomes of less than RM3,000 the 10% down payment for houses costing under RM400,000 – essentially providing a 100% loan without the need for a down payment. Attempts to micromanage this scheme have previously run into policy mistakes. First introduced in Budget 2011, the scheme had to be expanded in Budget 2012 following complaints that the scheme was insufficient to meet the property prices in urban areas such as the Klang Valley and Penang, only to then come under pressure to relax eligibility criteria after registering dismal approval rates of 36.3% early this year – pressure the government has clearly succumbed to. Needless to say, a relaxation of eligibility criteria would do nothing to improve the household debt situation, especially for lower income groups for whom it would not be financially prudent to take up debt to own a home. Nonetheless, given the political imperatives of the day, this was clearly discounted against the need to court the young urban electorate.

Key Economic Data and Forecasts

Malaysia – Key Economic Data and Forecasts

	2005	2006	2007	2008	2009	2010	2011	2012E	2013E
Real Sector									
Real GDP (% yoy)	5.3	5.6	6.3	4.8	-1.5	7.2	5.1	5.0	5.3
Domestic demand ex Inventory (% yoy)	7.5	6.3	9.9	6.6	0.3	7.0	8.2	10.7	8.0
Real Consumption: Private (% yoy)	9.1	6.6	10.4	8.7	0.6	6.6	7.1	7.7	7.0
Real Gross Fixed Capital Formation (% yoy)	4.9	6.3	10.4	2.4	-2.7	10.4	6.5	18.5	12.0
Consumer prices (% yoy)	3.0	3.6	2.0	5.4	0.6	1.7	3.2	1.8	2.4
GDP (USD bn)	143.5	162.8	193.7	231.1	202.4	247.0	288.2	304.9	322.1
GDP per capita (USD)	5,421	6,067	7,123	8,393	7,255	8,639	9,949	10,162	10,527
Unemployment Rate (%)	3.5	3.3	3.2	3.3	3.7	3.3	3.2	3.0	3.2
External Sector									
Exports (% yoy, US\$)	12.3	13.0	9.5	13.4	-21.2	26.4	14.4	2.2	0.6
Imports (% yoy, US\$)	9.3	13.9	12.2	6.9	-20.7	33.9	14.0	7.5	7.7
Trade balance (US\$ bn)	34.0	37.5	37.7	51.7	40.0	41.7	48.4	40.1	26.8
Current account (% of GDP)	14.4	16.1	15.4	17.1	15.5	11.1	11.0	5.0	4.0
International Reserves ex. Gold (US\$ bn)	70	82	101	92	97	105	135	153	150
MYR/USD (period average)	3.79	3.67	3.44	3.33	3.52	3.22	3.06	3.09	3.12
Other									
3-month KLIBOR fixing (% , average)	2.9	3.7	3.6	3.6	2.2	2.7	3.2	3.2	3.3
5-year MGS yield (% , average)	3.6	4.0	3.6	3.7	3.6	3.5	3.4	3.2	3.4
Fiscal balance (% of GDP)	-3.4	-3.2	-3.1	-4.6	-6.7	-5.4	-4.8	-4.5	-4.0
Population (persons million)	26.5	26.8	27.2	27.5	27.9	28.3	29.4	30.0	30.6

Source: CEIC, Citi Research Estimates

Interest and Foreign Exchange Rate Forecasts

		27-Sep	4Q12	1Q13	2Q13	3Q13	4Q13	In 3M	In 6M	In 12M
MY	Overnight Policy Rate	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00
	3-Month Interbank Rate	3.20	3.28	3.28	3.28	3.28	3.28	3.28	3.28	3.28
	5-year MGS	3.30	3.10	3.20	3.40	3.50	3.50	3.10	3.20	3.50
	USD-MYR	3.08	3.08	3.11	3.13	3.13	3.12	3.08	3.10	3.13
US	Fed Fund Rate	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
	10-Year Treasuries	1.64	1.65	1.75	2.00	2.25	2.55	NA	NA	NA

Source: Bloomberg, Citi Research Estimates

Appendix A-1

Analyst Certification

The research analyst(s) primarily responsible for the preparation and content of this research report are named in bold text in the author block at the front of the product except for those sections where an analyst's name appears in bold alongside content which is attributable to that analyst. Each of these analyst(s) certify, with respect to the section(s) of the report for which they are responsible, that the views expressed therein accurately reflect their personal views about each issuer and security referenced and were prepared in an independent manner, including with respect to Citigroup Global Markets Inc and its affiliates. No part of the research analyst's compensation was, is, or will be, directly or indirectly, related to the specific recommendation(s) or view(s) expressed by that research analyst in this report.

IMPORTANT DISCLOSURES

Analysts' compensation is determined based upon activities and services intended to benefit the investor clients of Citigroup Global Markets Inc. and its affiliates ("the Firm"). Like all Firm employees, analysts receive compensation that is impacted by overall firm profitability which includes investment banking revenues.

For important disclosures (including copies of historical disclosures) regarding the companies that are the subject of this Citi Research product ("the Product"), please contact Citi Research, 388 Greenwich Street, 28th Floor, New York, NY, 10013, Attention: Legal/Compliance [E6WYB6412478]. In addition, the same important disclosures, with the exception of the Valuation and Risk assessments and historical disclosures, are contained on the Firm's disclosure website at https://www.citivelocity.com/cvr/eppublic/citi_research_disclosures. Valuation and Risk assessments can be found in the text of the most recent research note/report regarding the subject company. Historical disclosures (for up to the past three years) will be provided upon request.

Citi Research Ratings Distribution

<i>Data current as of 30 Jun 2012</i>	12 Month Rating			Relative Rating		
	Buy	Hold	Sell	Buy	Hold	Sell
Citi Research Global Fundamental Coverage	53%	37%	10%	10%	80%	10%
<i>% of companies in each rating category that are investment banking clients</i>	44%	43%	40%	48%	43%	45%

Guide to Citi Research Fundamental Research Investment Ratings:

Citi Research stock recommendations include an investment rating and an optional risk rating to highlight high risk stocks.

Risk rating takes into account both price volatility and fundamental criteria. Stocks will either have no risk rating or a High risk rating assigned.

Investment Ratings: Citi Research investment ratings are Buy, Neutral and Sell. Our ratings are a function of analyst expectations of expected total return ("ETR") and risk. ETR is the sum of the forecast price appreciation (or depreciation) plus the dividend yield for a stock within the next 12 months. The Investment rating definitions are: Buy (1) ETR of 15% or more or 25% or more for High risk stocks; and Sell (3) for negative ETR. Any covered stock not assigned a Buy or a Sell is a Neutral (2). For stocks rated Neutral (2), if an analyst believes that there are insufficient valuation drivers and/or investment catalysts to derive a positive or negative investment view, they may elect with the approval of Citi Research management not to assign a target price and, thus, not derive an ETR. Analysts may place covered stocks "Under Review" in response to exceptional circumstances (e.g. lack of information critical to the analyst's thesis) affecting the company and / or trading in the company's securities (e.g. trading suspension). As soon as practically possible, the analyst will publish a note re-establishing a rating and investment thesis. To satisfy regulatory requirements, we correspond Under Review and Neutral to Hold in our ratings distribution table for our 12-month fundamental rating system. However, we reiterate that we do not consider Under Review to be a recommendation.

Relative three-month ratings: Citi Research may also assign a three-month relative call (or rating) to a stock to highlight expected out-performance (most preferred) or under-performance (least preferred) versus the geographic and industry sector over a 3 month period. The relative call may highlight a specific near-term catalyst or event impacting the company or the market that is anticipated to have a short-term price impact on the equity securities of the company. Absent any specific catalyst the analyst(s) will indicate the most and least preferred stocks in the universe of stocks under consideration, explaining the basis for this short-term view. This three-month view may be different from and does not affect a stock's fundamental equity rating, which reflects a longer-term total absolute return expectation. For purposes of NASD/NYSE ratings-distribution-disclosure rules, most preferred calls correspond to a buy recommendation and least preferred calls correspond to a sell recommendation. Any stock not assigned to a most preferred or least preferred call is considered non-relative-rated (NRR). For purposes of NASD/NYSE ratings-distribution-disclosure rules we correspond NRR to Hold in our ratings distribution table for our 3-month relative rating system. However, we reiterate that we do not consider NRR to be a recommendation.

Prior to October 8, 2011, the firm's stock recommendation system included a risk rating and an investment rating. **Risk ratings**, which took into account both price volatility and fundamental criteria, were: Low (L), Medium (M), High (H), and Speculative (S). **Investment Ratings** of Buy, Hold and Sell were a function of the Citi Research expectation of total return (forecast price appreciation and dividend yield within the next 12 months) and risk rating. Additionally, analysts could have placed covered stocks "Under Review" in response to exceptional circumstances (e.g. lack of information critical to the analyst's thesis) affecting the company and/or trading in the company's securities (e.g. trading suspension). Stocks placed "Under Review" were monitored daily by management and as practically possible, the analyst published a note re-establishing a rating and investment thesis. For securities in developed markets (US, UK, Europe, Japan, and Australia/New Zealand), investment ratings were: Buy (1) (expected total return of 10% or more for Low-Risk stocks, 15% or more for Medium-Risk stocks, 20% or more for High-Risk stocks, and 35% or more for Speculative stocks); Hold (2) (0%-10% for Low-Risk stocks, 0%-15% for Medium-Risk stocks, 0%-20% for High-Risk stocks, and 0%-35% for Speculative stocks); and Sell (3) (negative total return). For securities in emerging markets (Asia Pacific, Emerging Europe/Middle East/Africa, and Latin America), investment ratings were: Buy (1) (expected total return of 15% or more for Low-Risk stocks, 20% or more for Medium-Risk stocks, 30% or more for High-Risk stocks, and 40% or more for Speculative stocks); Hold (2) (5%-15% for Low-Risk stocks, 10%-20% for Medium-Risk stocks, 15%-30% for High-Risk stocks, and 20%-40% for Speculative stocks); and Sell (3) (5% or less for Low-Risk stocks, 10% or less for Medium-Risk stocks, 15% or less for High-Risk stocks, and 20% or less for Speculative stocks).

Investment ratings are determined by the ranges described above at the time of initiation of coverage, a change in investment and/or risk rating, or a change in target price (subject to limited management discretion). At other times, the expected total returns may fall outside of these ranges because of market price movements and/or other short-term volatility or trading patterns. Such interim deviations from specified ranges will be permitted but will become subject to

review by Research Management. Your decision to buy or sell a security should be based upon your personal investment objectives and should be made only after evaluating the stock's expected performance and risk.

NON-US RESEARCH ANALYST DISCLOSURES

Non-US research analysts who have prepared this report (i.e., all research analysts listed below other than those identified as employed by Citigroup Global Markets Inc.) are not registered/qualified as research analysts with FINRA. Such research analysts may not be associated persons of the member organization and therefore may not be subject to the NYSE Rule 472 and NASD Rule 2711 restrictions on communications with a subject company, public appearances and trading securities held by a research analyst account. The legal entities employing the authors of this report are listed below:

Citigroup Global Markets Singapore PTE LIMITED	Wei Zheng Kit; Brian Tan
PT Citigroup Securities Indonesia	Salman Ali, CFA

OTHER DISCLOSURES

For securities recommended in the Product in which the Firm is not a market maker, the Firm is a liquidity provider in the issuers' financial instruments and may act as principal in connection with such transactions. The Firm is a regular issuer of traded financial instruments linked to securities that may have been recommended in the Product. The Firm regularly trades in the securities of the issuer(s) discussed in the Product. The Firm may engage in securities transactions in a manner inconsistent with the Product and, with respect to securities covered by the Product, will buy or sell from customers on a principal basis.

Securities recommended, offered, or sold by the Firm: (i) are not insured by the Federal Deposit Insurance Corporation; (ii) are not deposits or other obligations of any insured depository institution (including Citibank); and (iii) are subject to investment risks, including the possible loss of the principal amount invested. Although information has been obtained from and is based upon sources that the Firm believes to be reliable, we do not guarantee its accuracy and it may be incomplete and condensed. Note, however, that the Firm has taken all reasonable steps to determine the accuracy and completeness of the disclosures made in the Important Disclosures section of the Product. The Firm's research department has received assistance from the subject company(ies) referred to in this Product including, but not limited to, discussions with management of the subject company(ies). Firm policy prohibits research analysts from sending draft research to subject companies. However, it should be presumed that the author of the Product has had discussions with the subject company to ensure factual accuracy prior to publication. All opinions, projections and estimates constitute the judgment of the author as of the date of the Product and these, plus any other information contained in the Product, are subject to change without notice. Prices and availability of financial instruments also are subject to change without notice. Notwithstanding other departments within the Firm advising the companies discussed in this Product, information obtained in such role is not used in the preparation of the Product. Although Citi Research does not set a predetermined frequency for publication, if the Product is a fundamental research report, it is the intention of Citi Research to provide research coverage of the/those issuer(s) mentioned therein, including in response to news affecting this issuer, subject to applicable quiet periods and capacity constraints. The Product is for informational purposes only and is not intended as an offer or solicitation for the purchase or sale of a security. Any decision to purchase securities mentioned in the Product must take into account existing public information on such security or any registered prospectus.

Investing in non-U.S. securities, including ADRs, may entail certain risks. The securities of non-U.S. issuers may not be registered with, nor be subject to the reporting requirements of the U.S. Securities and Exchange Commission. There may be limited information available on foreign securities. Foreign companies are generally not subject to uniform audit and reporting standards, practices and requirements comparable to those in the U.S. Securities of some foreign companies may be less liquid and their prices more volatile than securities of comparable U.S. companies. In addition, exchange rate movements may have an adverse effect on the value of an investment in a foreign stock and its corresponding dividend payment for U.S. investors. Net dividends to ADR investors are estimated, using withholding tax rates conventions, deemed accurate, but investors are urged to consult their tax advisor for exact dividend computations. Investors who have received the Product from the Firm may be prohibited in certain states or other jurisdictions from purchasing securities mentioned in the Product from the Firm. Please ask your Financial Consultant for additional details. Citigroup Global Markets Inc. takes responsibility for the Product in the United States. Any orders by US investors resulting from the information contained in the Product may be placed only through Citigroup Global Markets Inc.

Important Disclosures for Morgan Stanley Smith Barney LLC Customers: Morgan Stanley & Co. LLC (Morgan Stanley) research reports may be available about the companies that are the subject of this Citi Research research report. Ask your Financial Advisor or use smithbarney.com to view any available Morgan Stanley research reports in addition to Citi Research research reports.

Important disclosure regarding the relationship between the companies that are the subject of this Citi Research research report and Morgan Stanley Smith Barney LLC and its affiliates are available at the Morgan Stanley Smith Barney disclosure website at www.morganstanleysmithbarney.com/researchdisclosures.

For Morgan Stanley and Citigroup Global Markets, Inc. specific disclosures, you may refer to www.morganstanley.com/researchdisclosures and https://www.citivelocity.com/cvr/epublic/citi_research_disclosures.

This Citi Research research report has been reviewed and approved on behalf of Morgan Stanley Smith Barney LLC. This review and approval was conducted by the same person who reviewed this research report on behalf of Citi Research. This could create a conflict of interest.

The Citigroup legal entity that takes responsibility for the production of the Product is the legal entity which the first named author is employed by. The Product is made available in **Australia** through Citi Global Markets Australia Pty Ltd. (ABN 64 003 114 832 and AFSL No. 240992), participant of the ASX Group and regulated by the Australian Securities & Investments Commission. Citigroup Centre, 2 Park Street, Sydney, NSW 2000. The Product is made available in Australia to Private Banking wholesale clients through Citigroup Pty Limited (ABN 88 004 325 080 and AFSL 238098). Citigroup Pty Limited provides all financial product advice to Australian Private Banking wholesale clients through bankers and relationship managers. If there is any doubt about the suitability of investments held in Citigroup Private Bank accounts, investors should contact the Citigroup Private Bank in Australia. Citigroup companies may compensate affiliates and their representatives for providing products and services to clients. The Product is made available in **Brazil** by Citigroup Global Markets Brasil - CCTVM SA, which is regulated by CVM - Comissão de Valores Mobiliários, BACEN - Brazilian Central Bank, APIMEC - Associação dos Analistas e Profissionais de Investimento do Mercado de Capitais and ANBID - Associação Nacional dos Bancos de Investimento. Av. Paulista, 1111 - 11º andar - CEP. 01311920 - São Paulo - SP. If the Product is being made available in certain provinces of **Canada** by Citigroup Global Markets (Canada) Inc. ("CGM Canada"), CGM Canada has approved the Product. Citigroup Place, 123 Front Street West, Suite 1100, Toronto, Ontario M5J

2M3. This product is available in **Chile** through Banchile Corredores de Bolsa S.A., an indirect subsidiary of Citigroup Inc., which is regulated by the Superintendencia de Valores y Seguros. Agustinas 975, piso 2, Santiago, Chile. The Product is made available in **France** by Citigroup Global Markets Limited, which is authorised and regulated by Financial Services Authority. 1-5 Rue Paul Cézanne, 8ème, Paris, France. The Product is distributed in **Germany** by Citigroup Global Markets Deutschland AG ("CGMD"), which is regulated by Bundesanstalt fuer Finanzdienstleistungsaufsicht (BaFin). CGMD, Reuterweg 16, 60323 Frankfurt am Main. Research which relates to "securities" (as defined in the Securities and Futures Ordinance (Cap. 571 of the Laws of Hong Kong)) is issued in **Hong Kong** by, or on behalf of, Citigroup Global Markets Asia Limited which takes full responsibility for its content. Citigroup Global Markets Asia Ltd. is regulated by Hong Kong Securities and Futures Commission. If the Research is made available through Citibank, N.A., Hong Kong Branch, for its clients in Citi Private Bank, it is made available by Citibank N.A., Citibank Tower, Citibank Plaza, 3 Garden Road, Hong Kong. Citibank N.A. is regulated by the Hong Kong Monetary Authority. Please contact your Private Banker in Citibank N.A., Hong Kong, Branch if you have any queries on or any matters arising from or in connection with this document. The Product is made available in **India** by Citigroup Global Markets India Private Limited, which is regulated by Securities and Exchange Board of India. Bakhtawar, Nariman Point, Mumbai 400-021. The Product is made available in **Indonesia** through PT Citigroup Securities Indonesia. 5/F, Citibank Tower, Bapindo Plaza, Jl. Jend. Sudirman Kav. 54-55, Jakarta 12190. Neither this Product nor any copy hereof may be distributed in Indonesia or to any Indonesian citizens wherever they are domiciled or to Indonesian residents except in compliance with applicable capital market laws and regulations. This Product is not an offer of securities in Indonesia. The securities referred to in this Product have not been registered with the Capital Market and Financial Institutions Supervisory Agency (BAPEPAM-LK) pursuant to relevant capital market laws and regulations, and may not be offered or sold within the territory of the Republic of Indonesia or to Indonesian citizens through a public offering or in circumstances which constitute an offer within the meaning of the Indonesian capital market laws and regulations. The Product is made available in **Israel** through Citibank NA, regulated by the Bank of Israel and the Israeli Securities Authority. Citibank, N.A. Platinum Building, 21 Ha'arba'ah St, Tel Aviv, Israel. The Product is made available in **Italy** by Citigroup Global Markets Limited, which is authorised and regulated by Financial Services Authority. Via dei Mercanti, 12, Milan, 20121, Italy. The Product is made available in **Japan** by Citigroup Global Markets Japan Inc. ("CGMJ"), which is regulated by Financial Services Agency, Securities and Exchange Surveillance Commission, Japan Securities Dealers Association, Tokyo Stock Exchange and Osaka Securities Exchange. Shin-Marunouchi Building, 1-5-1 Marunouchi, Chiyoda-ku, Tokyo 100-6520 Japan. If the Product was distributed by SMBC Nikko Securities Inc. it is being so distributed under license. In the event that an error is found in an CGMJ research report, a revised version will be posted on the Firm's Citi Velocity website. If you have questions regarding Citi Velocity, please call (81 3) 6270-3019 for help. The Product is made available in **Korea** by Citigroup Global Markets Korea Securities Ltd., which is regulated by the Financial Services Commission, the Financial Supervisory Service and the Korea Financial Investment Association (KOFIA). Citibank Building, 39 Da-dong, Jung-gu, Seoul 100-180, Korea. KOFIA makes available registration information of research analysts on its website. Please visit the following website if you wish to find KOFIA registration information on research analysts of Citigroup Global Markets Korea Securities Ltd. <http://dis.kofia.or.kr/fs/dis2/fundMgr/DISFundMgrAnalystPop.jsp?companyCd2=A03030&pageDiv=02>. The Product is made available in Korea by Citibank Korea Inc., which is regulated by the Financial Services Commission and the Financial Supervisory Service. Address is Citibank Building, 39 Da-dong, Jung-gu, Seoul 100-180, Korea. The Product is made available in **Malaysia** by Citigroup Global Markets Malaysia Sdn Bhd (Company No. 460819-D) ("CGMM") to its clients and CGMM takes responsibility for its contents. CGMM is regulated by the Securities Commission of Malaysia. Please contact CGMM at Level 43 Menara Citibank, 165 Jalan Ampang, 50450 Kuala Lumpur, Malaysia in respect of any matters arising from, or in connection with, the Product. The Product is made available in **Mexico** by Acciones y Valores Banamex, S.A. De C. V., Casa de Bolsa, Integrante del Grupo Financiero Banamex ("Accival") which is a wholly owned subsidiary of Citigroup Inc. and is regulated by Comision Nacional Bancaria y de Valores. Reforma 398, Col. Juarez, 06600 Mexico, D.F. In **New Zealand** the Product is made available to 'wholesale clients' only as defined by s5C(1) of the Financial Advisers Act 2008 ("FAA") through Citigroup Global Markets Australia Pty Ltd (ABN 64 003 114 832 and AFSL No. 240992), an overseas financial adviser as defined by the FAA, participant of the ASX Group and regulated by the Australian Securities & Investments Commission. Citigroup Centre, 2 Park Street, Sydney, NSW 2000. The Product is made available in **Pakistan** by Citibank N.A. Pakistan branch, which is regulated by the State Bank of Pakistan and Securities Exchange Commission, Pakistan. AWT Plaza, 1.1. Chundrigar Road, P.O. Box 4889, Karachi-74200. The Product is made available in the **Philippines** through Citicorp Financial Services and Insurance Brokerage Philippines, Inc., which is regulated by the Philippines Securities and Exchange Commission. 20th Floor Citibank Square Bldg. The Product is made available in the Philippines through Citibank NA Philippines branch, Citibank Tower, 8741 Paseo De Roxas, Makati City, Manila. Citibank NA Philippines NA is regulated by The Bangko Sentral ng Pilipinas. The Product is made available in **Poland** by Dom Maklerski Banku Handlowego SA an indirect subsidiary of Citigroup Inc., which is regulated by Komisja Nadzoru Finansowego. Dom Maklerski Banku Handlowego S.A. ul.Senatorska 16, 00-923 Warszawa. The Product is made available in the **Russian Federation** through ZAO Citibank, which is licensed to carry out banking activities in the Russian Federation in accordance with the general banking license issued by the Central Bank of the Russian Federation and brokerage activities in accordance with the license issued by the Federal Service for Financial Markets. Neither the Product nor any information contained in the Product shall be considered as advertising the securities mentioned in this report within the territory of the Russian Federation or outside the Russian Federation. The Product does not constitute an appraisal within the meaning of the Federal Law of the Russian Federation of 29 July 1998 No. 135-FZ (as amended) On Appraisal Activities in the Russian Federation. 8-10 Gasheka Street, 125047 Moscow. The Product is made available in **Singapore** through Citigroup Global Markets Singapore Pte. Ltd. ("CGMSPL"), a capital markets services license holder, and regulated by Monetary Authority of Singapore. Please contact CGMSPL at 8 Marina View, 21st Floor Asia Square Tower 1, Singapore 018960, in respect of any matters arising from, or in connection with, the analysis of this document. This report is intended for recipients who are accredited, expert and institutional investors as defined under the Securities and Futures Act (Cap. 289). The Product is made available by The Citigroup Private Bank in Singapore through Citibank, N.A., Singapore Branch, a licensed bank in Singapore that is regulated by Monetary Authority of Singapore. Please contact your Private Banker in Citibank N.A., Singapore Branch if you have any queries on or any matters arising from or in connection with this document. This report is intended for recipients who are accredited, expert and institutional investors as defined under the Securities and Futures Act (Cap. 289). This report is distributed in Singapore by Citibank Singapore Ltd ("CSL") to selected Citigold/Citigold Private Clients. CSL provides no independent research or analysis of the substance or in preparation of this report. Please contact your Citigold/Citigold Private Client Relationship Manager in CSL if you have any queries on or any matters arising from or in connection with this report. This report is intended for recipients who are accredited investors as defined under the Securities and Futures Act (Cap. 289). Citigroup Global Markets (Pty) Ltd. is incorporated in the **Republic of South Africa** (company registration number 2000/025866/07) and its registered office is at 145 West Street, Sandton, 2196, Saxonwold. Citigroup Global Markets (Pty) Ltd. is regulated by JSE Securities Exchange South Africa, South African Reserve Bank and the Financial Services Board. The investments and services contained herein are not available to private customers in South Africa. The Product is made available in **Spain** by Citigroup Global Markets Limited, which is authorised and regulated by Financial Services Authority. 29 Jose Ortega Y Gasset, 4th Floor, Madrid, 28006, Spain. The Product is made available in the **Republic of China** through Citigroup Global Markets Taiwan Securities

Company Ltd. ("CGMTS"), 14 and 15F, No. 1, Songzhi Road, Taipei 110, Taiwan and/or through Citibank Securities (Taiwan) Company Limited ("CSTL"), 14 and 15F, No. 1, Songzhi Road, Taipei 110, Taiwan, subject to the respective license scope of each entity and the applicable laws and regulations in the Republic of China. CGMTS and CSTL are both regulated by the Securities and Futures Bureau of the Financial Supervisory Commission of Taiwan, the Republic of China. No portion of the Product may be reproduced or quoted in the Republic of China by the press or any third parties [without the written authorization of CGMTS and CSTL]. If the Product covers securities which are not allowed to be offered or traded in the Republic of China, neither the Product nor any information contained in the Product shall be considered as advertising the securities or making recommendation of the securities in the Republic of China. The Product is for informational purposes only and is not intended as an offer or solicitation for the purchase or sale of a security or financial products. Any decision to purchase securities or financial products mentioned in the Product must take into account existing public information on such security or the financial products or any registered prospectus. The Product is made available in **Thailand** through Citicorp Securities (Thailand) Ltd., which is regulated by the Securities and Exchange Commission of Thailand. 18/F, 22/F and 29/F, 82 North Sathorn Road, Silom, Bangrak, Bangkok 10500, Thailand. The Product is made available in **Turkey** through Citibank AS which is regulated by Capital Markets Board. Tekfen Tower, Eski Buyukdere Caddesi # 209 Kat 2B, 23294 Levent, Istanbul, Turkey. In the **U.A.E.**, these materials (the "Materials") are communicated by Citigroup Global Markets Limited, DIFC branch ("CGML"), an entity registered in the Dubai International Financial Center ("DIFC") and licensed and regulated by the Dubai Financial Services Authority ("DFSA") to Professional Clients and Market Counterparties only and should not be relied upon or distributed to Retail Clients. A distribution of the different Citi Research ratings distribution, in percentage terms for Investments in each sector covered is made available on request. Financial products and/or services to which the Materials relate will only be made available to Professional Clients and Market Counterparties. The Product is made available in **United Kingdom** by Citigroup Global Markets Limited, which is authorised and regulated by Financial Services Authority. This material may relate to investments or services of a person outside of the UK or to other matters which are not regulated by the FSA and further details as to where this may be the case are available upon request in respect of this material. Citigroup Centre, Canada Square, Canary Wharf, London, E14 5LB. The Product is made available in **United States** by Citigroup Global Markets Inc, which is a member of FINRA and registered with the US Securities and Exchange Commission. 388 Greenwich Street, New York, NY 10013. Unless specified to the contrary, within EU Member States, the Product is made available by Citigroup Global Markets Limited, which is regulated by Financial Services Authority.

Pursuant to Comissão de Valores Mobiliários Rule 483, Citi is required to disclose whether a Citi related company or business has a commercial relationship with the subject company. Considering that Citi operates multiple businesses in more than 100 countries around the world, it is likely that Citi has a commercial relationship with the subject company.

Many European regulators require that a firm must establish, implement and make available a policy for managing conflicts of interest arising as a result of publication or distribution of investment research. The policy applicable to Citi Research's Products can be found at https://www.citivelocity.com/cvr/eppublic/citi_research_disclosures.

Compensation of equity research analysts is determined by equity research management and Citigroup's senior management and is not linked to specific transactions or recommendations.

The Product may have been distributed simultaneously, in multiple formats, to the Firm's worldwide institutional and retail customers. The Product is not to be construed as providing investment services in any jurisdiction where the provision of such services would not be permitted.

Subject to the nature and contents of the Product, the investments described therein are subject to fluctuations in price and/or value and investors may get back less than originally invested. Certain high-volatility investments can be subject to sudden and large falls in value that could equal or exceed the amount invested. Certain investments contained in the Product may have tax implications for private customers whereby levels and basis of taxation may be subject to change. If in doubt, investors should seek advice from a tax adviser. The Product does not purport to identify the nature of the specific market or other risks associated with a particular transaction. Advice in the Product is general and should not be construed as personal advice given it has been prepared without taking account of the objectives, financial situation or needs of any particular investor. Accordingly, investors should, before acting on the advice, consider the appropriateness of the advice, having regard to their objectives, financial situation and needs. Prior to acquiring any financial product, it is the client's responsibility to obtain the relevant offer document for the product and consider it before making a decision as to whether to purchase the product. With the exception of our product that is made available only to Qualified Institutional Buyers (QIBs) and other product that is made available through other distribution channels only to certain categories of clients to satisfy legal or regulatory requirements, Citi Research concurrently disseminates its research via proprietary and non-proprietary electronic distribution platforms. Periodically, individual Citi Research analysts may also opt to circulate research posted on such platforms to one or more clients by email. Such email distribution is discretionary and is done only after the research has been disseminated via the aforementioned distribution channels. Citi Research simultaneously distributes product that is limited to QIBs only through email distribution.

The level and types of services provided by Citi Research analysts to clients may vary depending on various factors such as the client's individual preferences as to the frequency and manner of receiving communications from analysts, the client's risk profile and investment focus and perspective (e.g. market-wide, sector specific, long term, short-term etc.), the size and scope of the overall client relationship with Citi and legal and regulatory constraints. Citi Research product may source data from dataCentral. dataCentral is a Citi Research proprietary database, which includes Citi estimates, data from company reports and feeds from Reuters and Datastream.

© 2012 Citigroup Global Markets Inc. Citi Research is a division of Citigroup Global Markets Inc. Citi and Citi with Arc Design are trademarks and service marks of Citigroup Inc. and its affiliates and are used and registered throughout the world. All rights reserved. Any unauthorized use, duplication, redistribution or disclosure of this report (the "Product"), including, but not limited to, redistribution of the Product by electronic mail, posting of the Product on a website or page, and/or providing to a third party a link to the Product, is prohibited by law and will result in prosecution. The information contained in the Product is intended solely for the recipient and may not be further distributed by the recipient to any third party. Where included in this report, MSCI sourced information is the exclusive property of Morgan Stanley Capital International Inc. (MSCI). Without prior written permission of MSCI, this information and any other MSCI intellectual property may not be reproduced, redisseminated or used to create any financial products, including any indices. This information is provided on an "as is" basis. The user assumes the entire risk of any use made of this information. MSCI, its affiliates and any third party involved in, or related to, computing or compiling the information hereby expressly disclaim all warranties of originality, accuracy, completeness, merchantability or fitness for a particular purpose with respect to any of this information. Without limiting any of the foregoing, in no event shall MSCI, any of its affiliates or any third party involved in, or related to, computing or compiling the information have any liability for any damages of any kind. MSCI, Morgan Stanley Capital International and the MSCI indexes are services marks of MSCI and its affiliates. The Firm accepts no liability whatsoever for the actions of third parties. The Product may provide the addresses of, or contain hyperlinks to, websites. Except to the extent to which the Product refers to website material of the Firm, the Firm has not reviewed the linked site. Equally, except to the extent to which the Product refers to website material of the Firm, the Firm takes no

responsibility for, and makes no representations or warranties whatsoever as to, the data and information contained therein. Such address or hyperlink (including addresses or hyperlinks to website material of the Firm) is provided solely for your convenience and information and the content of the linked site does not in anyway form part of this document. Accessing such website or following such link through the Product or the website of the Firm shall be at your own risk and the Firm shall have no liability arising out of, or in connection with, any such referenced website.

ADDITIONAL INFORMATION IS AVAILABLE UPON REQUEST
