

**ASIA-INVEST BUSINESS PRIMING FUND
MARKET-PLACE MONITORING SCHEME**

Project Title: Market Study on Wood Sector in Indonesia, Malaysia, Thailand and Vietnam

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EXECUTIVE SUMMARY

MALAYSIA

Country Economic Overview

Over the last decade the Malaysian economy achieved an average annual growth rate of 7%, with inflation kept below 4% per year. Gross domestic product (GDP) doubled from RM66 billion in 1988 to RM133 billion in 1999, while per capita income expanded from RM 5,100 to RM 11,833. This rapid economic growth has today placed Malaysia among the world's top 20 trading nations.

From a dependence on agriculture and primary commodities in the sixties, Malaysia's manufacturing sector now accounts for 34.4%, more than a third of GDP, while exports of manufactured goods make up over 80% of the country's total exports.

Over the past three decades, the manufacturing sector progressed from import-substitution and labour-intensive industries to export-oriented, high technology and capital-intensive industries.

Today, Malaysia is one of the world's leading exporters of products manufactured from its own natural resources of rubber, palm oil and timber and of semiconductors and room air-conditioners. The country's rapid industrialisation was the result of Malaysia opening itself early to foreign direct investments (FDI). With the creation of a business-friendly environment Malaysia has been one of the largest recipients of FDI among developing countries.

Proposed FDI in manufacturing projects approved during the last five years totalled RM 62.1 billion, or 48% of total proposed investments. In its World Competitiveness Report 1999, the International Institute for Management Development ranked Malaysia fourth among the non-OECD countries in terms of overall competitiveness.

The agriculture, forestry and fishery sector remains an important sector of the Malaysian economy, contributing 12.3% to GDP and 10.5% to total exports in 1998.

Malaysia's services sector is the largest sector in the economy, contributing 48.8% to GDP and 47.5% to total employment in 1998.

Although dominated by primary processing activities such as veneer and plywood production, Malaysia's wood-based industry is heading towards greater downstream processing activities such as the manufacture of particleboard, mouldings, furniture and joinery. The manufacture of wooden furniture and parts is especially encouraged with the objective of making the country a reputable centre for furniture production. In Malaysia, rubberwood is increasingly being used as a raw material for a variety of secondary and tertiary wood products.

Forestry resources

Malaysia has traditionally been one of the greenest countries on earth and one of the major producing countries for timber.

The total area opened for harvesting in Peninsular Malaysia in 1998 was 0.11 million hectares, a decline of 17.7% as compared to 1997.

Production of sawn logs decreased from 7.38 million cubic metres in 1997 to 5.10 million cubic metres in 1998, showing a sharp fall of 30.9%. The decline was due mainly to weak demand from log-consuming industries badly affected by the Asian financial crisis. At the same time, the slow down in logging activities was in line with the Government's conservation policy and commitment to ITTO Year 2000 Objective of sustainable forest management. Production of small logs, which accounted for 17.5% of the total sawn logs production, registered a fall of 36%.

About 74.7% of the total production of sawn timber and 66.3% of the total production of plywood were domestically consumed.

Exports of major timber products by Malaysia amounted to RM 2.52 billion as compared to RM 2.28 billion in 1997, an increase of 10.4%. Export value of blockboard, plywood and mouldings dipped 58.4%, 13.4% and 0.5% against 1997's performances. For the other major timber products, the export value registered increases of between 4.1% - 161.5%.

In 1998, sawn timber exports captured 34.9% of the total export volume, followed by medium density fibreboard (30.8%) and plywood (11.0%). Positions were the same in 1997, but with a reduced share for sawn timber (40.0%) and plywood (12.8%)

In 1998, the average f.o.b. unit value of veneer (- 61.0%), plywood (- 5.5%) and blockboard (- 4.3%) recorded decreases as compared to 1997. For mouldings, the average f.o.b. unit value increased from RM 1,805.02 per cubic metre in 1997 to RM 2,039.73 per cubic metre in 1998, registering an increase of 13.0%, the highest among these eight major timber products.

Imports of wood based products are very low compared to export. They cater mainly for specific needs of consumer of higher end furniture, and industries that require species of wood not found locally or for value added processing in Malaysia. The main sources of imports are USA, Indonesia and Myanmar.

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The furniture industry

The production value in the wood based industry declined by 6.5% to RM 8,423.3 million in 1998 from RM 9,022.7 million in 1997 due to the decline in the production of plywood, hardboard and particleboard as well as wood planning, window and door and joinery products.

However, the production value of furniture and components increased by 16.9% to RM 2,124 million in 1998 from RM 1,864.4 million in 1997. This was due to the greater demand for Malaysian furniture and furniture parts and components in the international market as well as increase in the domestic sales of medium and low end Malaysian made furniture as more people become aware of its quality and competitive prices.

At the end of 1998, the average capacity utilisation of the manufacturing companies engaged in the wood based sector was 68.3%. This data was at the same level as at December 1997 and indicated that in general the industry has not been adversely affected by the economic downturn. This was mainly attributed to the greater demand for high value added downstream products of furniture components in the export markets, which offset to some extent the decline in primary wood-based sub sector.

The furniture sector employs more than 20,000 people. Since the sector is labour intensive in nature, a wide number of foreigners are employed in the sector

In the past decade, the annual exports of Malaysian furniture rose from RM27 million to more than RM3 billion. It is forecast that the export will grow between 10 -15% from 1998 to the year 2000.

The Malaysian furniture industry is one of the country's largest export earners and crucial to the nation's growth. With over US\$1 billion in sales in 1998 to over 144 countries the Malaysian furniture industry produces world class products to compete on a global scale.

The territory of Malaysia is still now for three-quarter to four-fifth covered by forest. Its forest resources allow for more growth, opportunities and accelerated development of the downstream industries.

Malaysia is now ranked among the top exporting furniture nations in both the USA and Japan. The furniture makers of Malaysia can be assured that the increasing demand of locally produced furniture range determines that buyers are satisfied with the quality and value. The United States of America, Japan and Singapore are still Malaysia's main buyers with the United Kingdom, Australia and Taiwan gaining confidence prominently.

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The woodworking machinery industry

Most of Malaysian manufacturers have invested considerably in machinery and equipment in the period 1990-1996 to cope with greater production in response to increase in demand from local and overseas markets, with more than one third of the them having invested over 1 million RM in machinery and equipment and about half between RM1 million and RM 5 million. The average capital investment for factories with output of RM 1 – 10 million is RM 3.7 million. For factories with more than RM 10 million output, the average investment is RM 10.2 million. The process of mechanization tends to be gradual and depends a great deal on the availability of financing.

The furniture industry requires a wide range of machinery depending on the type of furniture manufactured and on the material used. In general, the manufacture of panel office furniture using plywood, particleboard and fireboard is easier to automate than the manufacture of household furniture using solid wood.

On the whole, the Malaysian furniture producers continues to depend on a large number of skilled semi-skilled and unskilled workers to carry out many process. The typical factory uses a range of independently stationed special purpose machines, each managed by a number of workers. The process of automatisisation has generated high demand of unskilled manual labour, in particular for material handling.

Higher proportion of office furniture manufacturers uses CNC and automated machinery than household furniture manufacturers, which continue to rely more on semi-automated machines and manual labour.

There is a dire need to improve the semi automated machinery used in the industry. Most of them were imported from Taiwan and have been in use for a long time. Local machinery manufacturers are not meeting the needs of wood industry. They have substantially neglected the importance of the manufacturing sector, even though the market for machinery and parts is large. Unless local machine makers can improve the quality of their products and design them to the requirements of furniture manufacturers, machinery for this sector will continue to be imported.

Conclusions and recommendations

As before mentioned, the Malaysian production of wood and of products of the primary transformation of wood has decreased in the last two years.

On the whole, the local operators in the wood markets reveal some difficulties in the export in Europe of timbers and the related products, which have their main markets in Asia. However, Malaysia is still one of the more important exporter among Asian Countries and a recovery of the production in the rare woods is forecast.

The Malaysian imports of furniture decreased of about 55%, as a consequence of the Asian financial crisis, and demand was more direct to the local and cheaper production rather than to the European high quality products. At the moment, the majority of the imported furniture in Malaysia is represented by low quality products from Indonesia and Myanmar. The Malaysian market for high quality Italian and Spanish furniture has still small dimension and it is not possible to forecast a rapid recovery in the short terms. In this sector, the Italian/Spanish companies should look instead for opportunities in contract manufacturing (CM), J/V or local production.

A lot of investments was thus placed on manufacturing infrastructure to achieve high volume and consistent quality in the shortest possible time, and also to cope with the increasing competition from countries, such as Indonesia, Thailand and the Philippines. The focus is shifting towards innovation in design, with local manufacturers reducing their dependence on contract manufacturing and developing their own brand and proprietary creations. These developments are strongly supported by the government.

There is a dire need to improve the level of technology of the Malaysian wood based industry, since most of the machines were imported from Taiwan and have been in use for a long time and local machinery manufacturers are not meeting the needs of wood industry. However, the Malaysian imports of wood working machinery decreased from RM 962 million in 1996 to RM 671 million in 1998 (approx. -30%), as a consequence of the Asian financial crisis.

The total market for the woodworking machinery in Malaysia can be estimated at about US\$500 millions in 1998, of which about 70 % is attributed to the import and 30 % to local production. In consideration of the needs of the local industry of updated technology and of the recovery in 1999 of the main Asian economies, including Malaysia, it is forecast a growth of the demand of wood working machinery for year 2000 and beyond.

There is presently no import duty for the import of woodworking machinery in Malaysia, but there is a duty of 10% on the import of parts and components, plus 5 % of VAT.