

The Impact of World Crude Oil Price Changes on the Malaysian Economy: an Input-Output Analysis

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Abstract: By using an input-output model, this paper attempts to examine the economic impact on the Malaysian economy resulting from an increase in crude oil petroleum price. By simulating different levels of crude oil prices, we found that an increase in the world crude oil petroleum price gives more capacity to the economy in generating output and revenue collected by the government in the form of direct and indirect taxes. However, it is very clear that if the crude oil price reaches USD60/barrel, the government will be required to subsidise about RM8.27 of the petrol retail price in order to maintain the current price level.

Keywords: Economic impact, input-output analysis, oil price, Malaysian economy
JEL classification: C67, E66

1. Introduction

Malaysia has experienced three decades of sound economic growth and development. Over the years from the sixties to the seventies, the nation witnessed an easier phase of growth based on low labour cost and strong public sector support. Nevertheless, in the 1980s, Malaysia experienced a setback to the economy due to external shock when commodity prices collapsed twice, first in 1980 and then in 1985. The economic growth thereafter was not remarkable, though some recovery took place in 1987. This was the time when the manufacturing sector for intermediate goods expanded and led the economy. This established a new structural change from merely producing primary commodities to basic manufacturing and advanced manufacturing including electric semiconductors and components of electric products. In mid-1997, the economy had to face another economic disaster when the financial crisis that began in Thailand, later spread to all the ASEAN countries including Malaysia. In fact, the exchange rate badly affected most of the ASEAN countries. ASEAN countries had no choice other than to liquidate their current assets in order to offset their losses resulting from the currency devaluation.

Malaysia's economy resumed growth in 2002 and 2003, following a stall in 2001 due to slow demand for Malaysian exports. Following growth of only 0.3 per cent and a decline in real Gross

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