Socio-Economic Research Centre
SERC 社会经济研究中心

Bank Negara Malaysia (BNM)'s Economic and Monetary Review 2023 & Financial Stability Review, Second Half 2023

Structural Reforms for Boosting Economic Growth

20 March 2024

Key messages

1. Sustained global growth amid moderating inflation

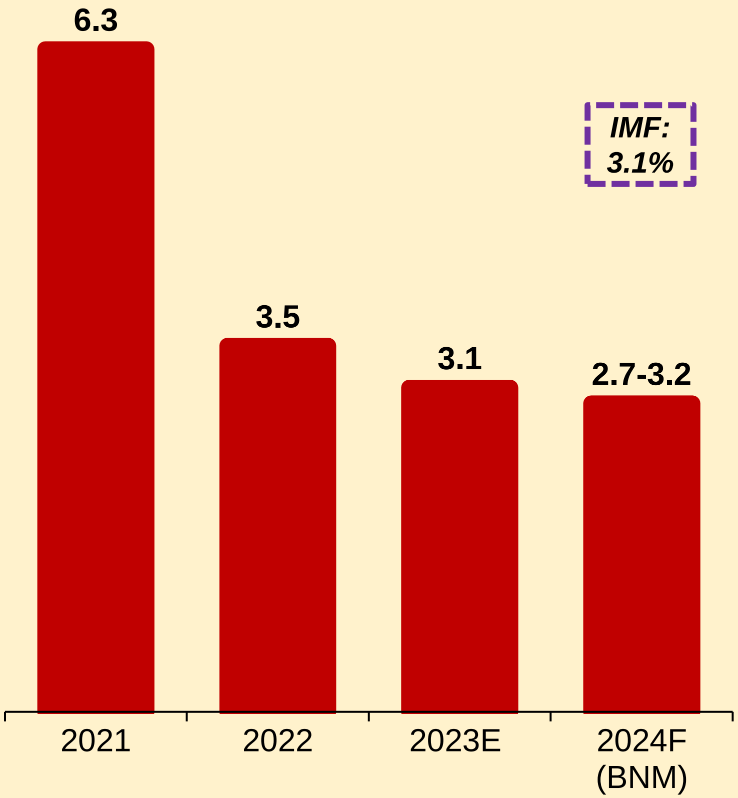
2. The Malaysian economy will expand by 4.0%-5.0% (mid-point estimate at 4.5%) in 2024, supported by continued domestic demand and exports recovery

3. Financial institutions are well-capitalised with strong buffers to support financial intermediation

4. Businesses and households' debt repayment capacity continue to be preserved

Continued global growth despite headwinds

Global real GDP growth (% YoY)



Source: IMF; BNM

Global growth is expected to be sustained at 2.7%-3.2% in 2024 though moderated from 3.1% in 2023. The challenges to growth come from persistent tight monetary policy and the withdrawal of fiscal support, while mitigated by easing inflation, strong labour markets and an upturn in global trade, especially technology cycle.

Global inflation is expected to continue moderating in 2024, primarily due to disinflation in advanced economies, providing room for major central banks to prepare for easing their monetary policy, while certain emerging market economies are witnessing inflation rates below their long-term averages.

Global growth outlook remains subject to downside risks - higher-than-expected inflation, tighter financial conditions and geopolitical escalations.

Key risk factors to global growth

Upside risks

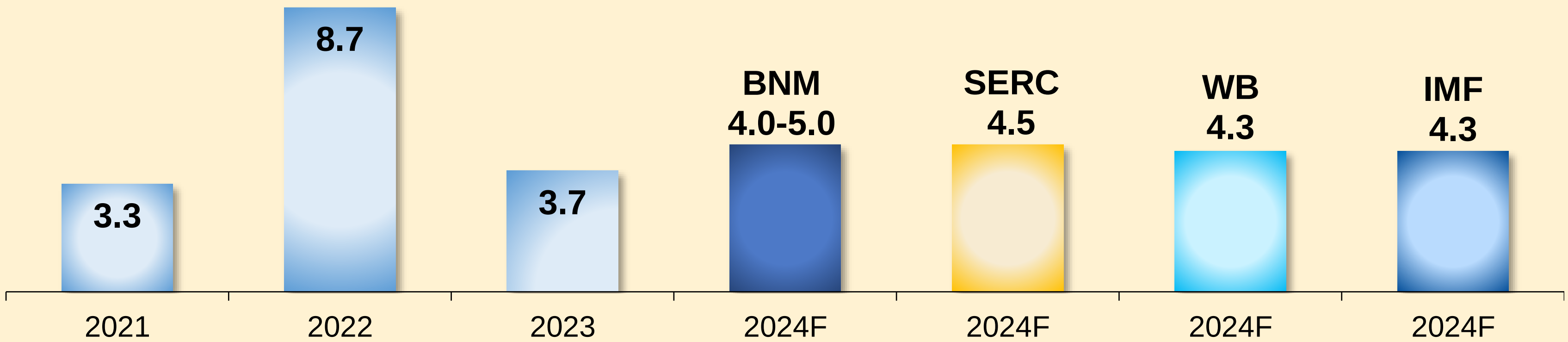
- Stronger-than-expected consumer spending
- Global trade rebound, driven by technology upcycle and tourism activities
- Continued moderation in global inflation

Downside risks

- High-for-longer policy rates
- Further escalation of geopolitical tensions
- Withdrawal of fiscal support

The Malaysian economy will be driven by continued expansion in domestic demand and improvement in external demand

Real GDP growth (%)



Source: DOSM; BNM; SERC; World Bank; IMF

Key growth drivers

Continued expansion in household spending

Higher income growth and continued expansion in employment

Improvement in investment

Supported by new and ongoing multi-year projects as well as implementation of national master plans

Recovery in goods trade activity

Rebound in global trade amid the tech upcycle

Higher tourist arrivals and spending

(2024F: Tourists arrival at 27.3 million vs. 20.1 million in 2023)

Downside risks from both external and domestic factors

2024F:
4.0%-5.0%

Upside risks to growth

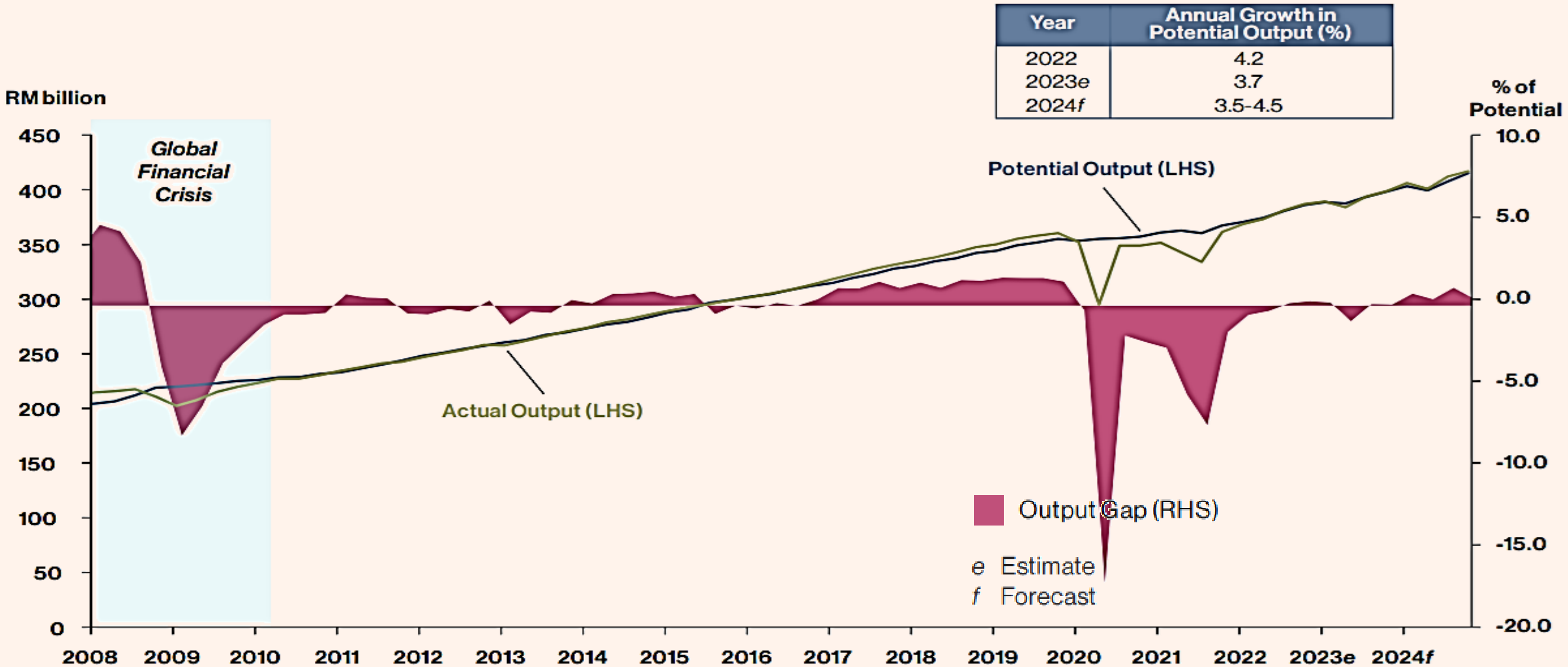
- Greater spillover from the tech upcycle
- More robust tourism activity
- Faster implementation of investment projects

Downside risks to growth

- Weaker-than-expected external demand
- Further escalation of geopolitical conflicts
- Larger decline in commodity production

Malaysia's potential output and the output gap

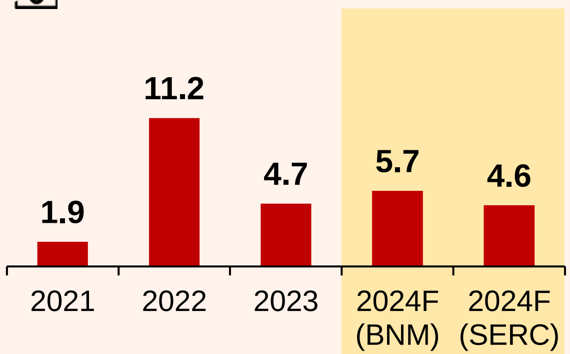
- **Output gap is expected to turn positive (3.5%–4.5% in 2024)**. The **actual output growth of 4.0%–5.0% is projected to grow at a faster pace**, underpinned by continued expansion in domestic demand and improvement in external demand.
- Over the medium term, potential output will remain supported by higher investments and improvements in productivity amid continued implementation of multi-year investment projects as well as national masterplan such as New Industrial Master Plan (NIMP) 2030 and National Energy Transition Roadmap (NETR) with a projected growth rate of 4%–5%, reverting to the pre-crisis level.



Source: DOSM; BNM estimates

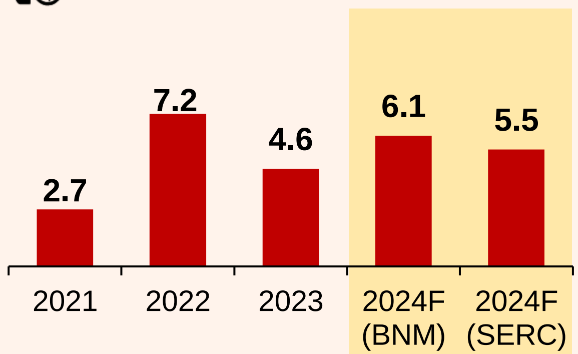
Domestic demand remains the anchor of growth

Private Consumption (%) **[60.8% of GDP]**



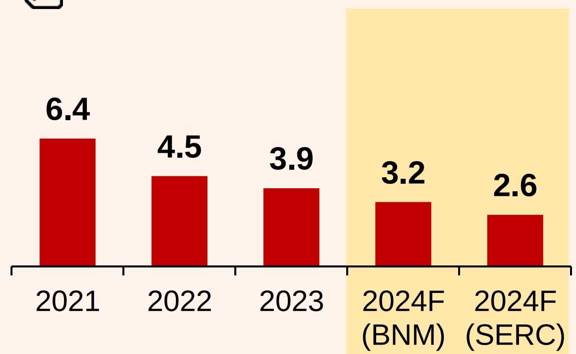
- Improving labour market conditions
- Higher income growth
- Expansion of Sumbangan Tunai Rahmah and the early incentive payment for civil servants

Private Investment (%) **[15.5% of GDP]**



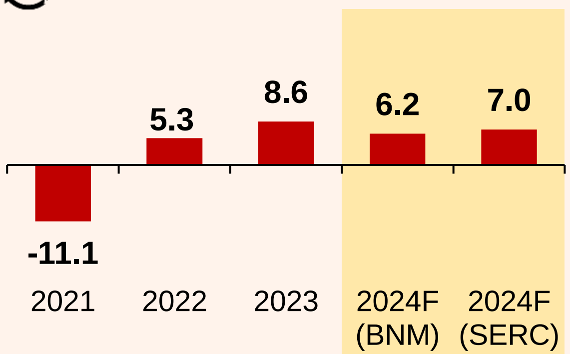
- Further progress in the implementation of multi-year projects
- Ongoing efforts in automation and digitalisation
- Continued capacity expansions

Public Consumption (%) **[13.3% of GDP]**



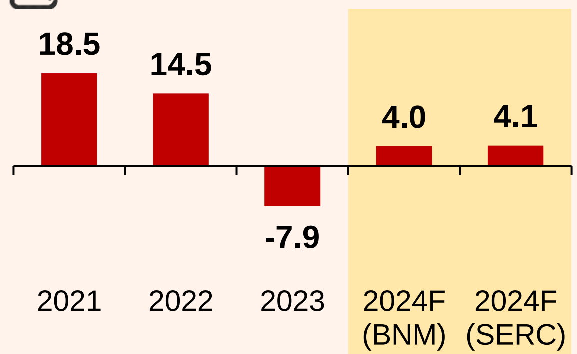
- Emoluments spending amid annual salary increment for civil servants and new hirings in the public sector

Public Investment (%) **[4.6% of GDP]**



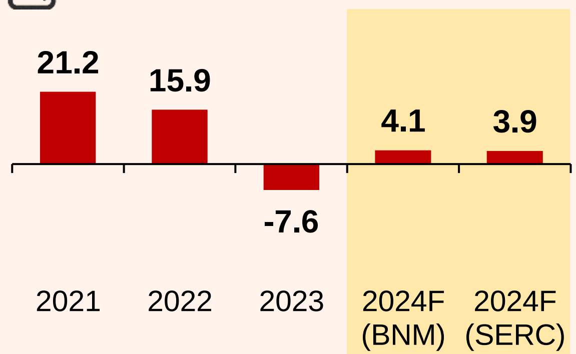
- Large-scale transport and digital infrastructure projects
- Catalytic projects under the National Energy Transition Roadmap (NETR)

Real Exports (%) **[66.3% of GDP]**



- Recovery in global trade and the technology upcycle
- Further recovery in tourism activity

Real Imports (%) **[61.6% of GDP]**

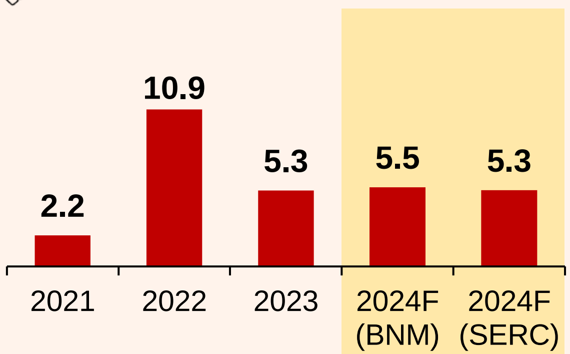


- Higher intermediate imports
- Stronger domestic demand for consumption goods
- Continued expansion in capital goods in tandem with investment growth

Note: Figure in parenthesis [ ] indicates share of GDP in 2023
Source: DOSM; BNM; SERC

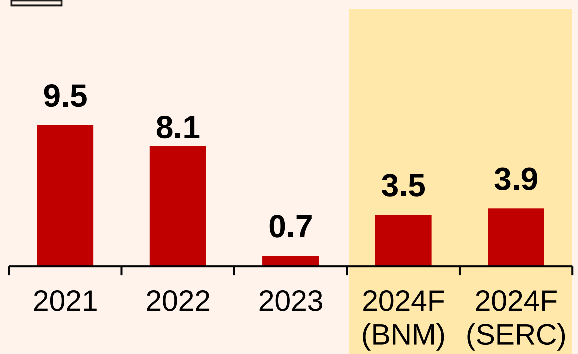
Expansion in most economic sectors

Services (%) **[59.2% of GDP]**



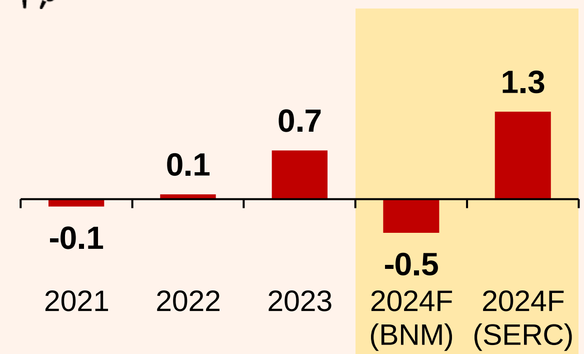
- Improvement in business-related subsectors
- Further rollout of 5G network coverage drive growth in the ICT subsector
- Tourism activities drive consumer-related subsectors

Manufacturing (%) **[23.4% of GDP]**



- Recovery in export-oriented industries
- Sustained growth in domestic-oriented cluster
- Upswing in the global technology cycle

Agriculture (%) **[6.4% of GDP]**



- Dry weather conditions; El Niño and effects of under-fertilisation lead to lower oil palm production
- Unfavourable weather also affect other agriculture subsectors

BNM's Forecast

Brent crude oil:

2024F: US$80-90/bbl

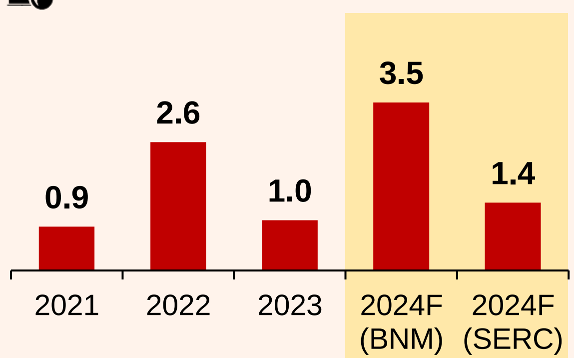
(2023: US$83/bbl)

Crude palm oil:

2024F: RM4,200-4,400/tonne

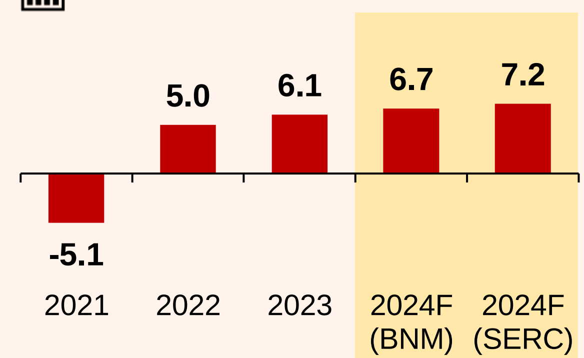
(2023: RM3,832/tonne)

Mining and quarrying (%) **[6.2% of GDP]**



- Increased production in existing oil and gas fields
- Production enhancements in Block SK320 and commencement of new gas field in Sarawak

Construction (%) **[3.6% of GDP]**

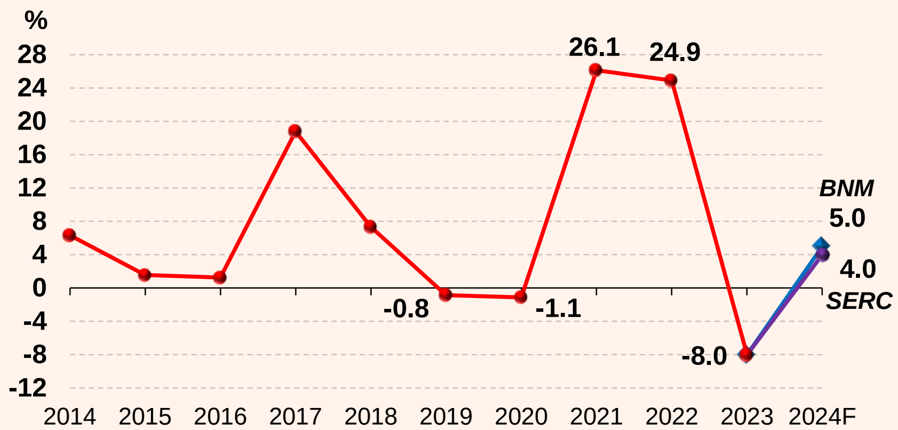


- New and ongoing large infrastructure and small-scale projects
- New housing launches amid further improvement in housing demand

Note: Figure in parenthesis [ ] indicates share of GDP in 2023
Source: DOSM; BNM; SERC

Export growth rebounds; Current account regains ground

Exports will rebound, support by higher global trade activities, recovery in global technology cycle and higher commodity prices

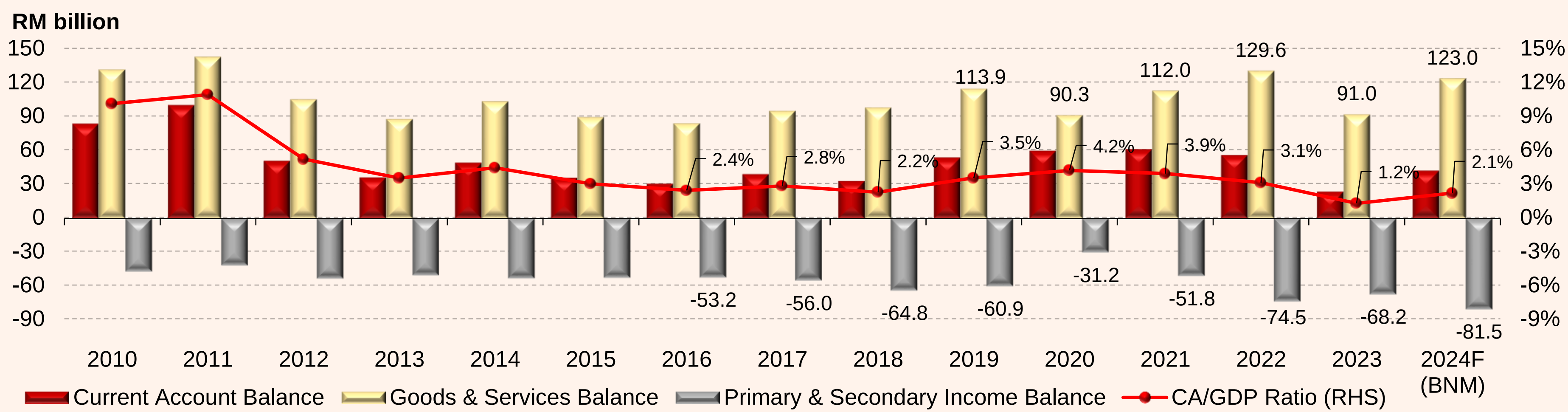


Contraction in major export products in 2023

Major export products	RM billion	% Growth
Electrical & electronic products [40.4%]	575.5	-3.0
Petroleum products [10.1%]	143.5	-11.0
Chemical & chemical products [5.0%]	71.5	-11.3
Liquefied natural gas [4.2%]	59.6	-12.4
Palm oil [4.2%]	59.4	-27.9
Machinery & equipment [4.0%]	57.3	-5.2
Manufactures of metal [4.0%]	56.3	-11.4
Optical & scientific equipment [3.8%]	54.6	-3.6

Figure in parenthesis indicates % share of gross exports in 2023

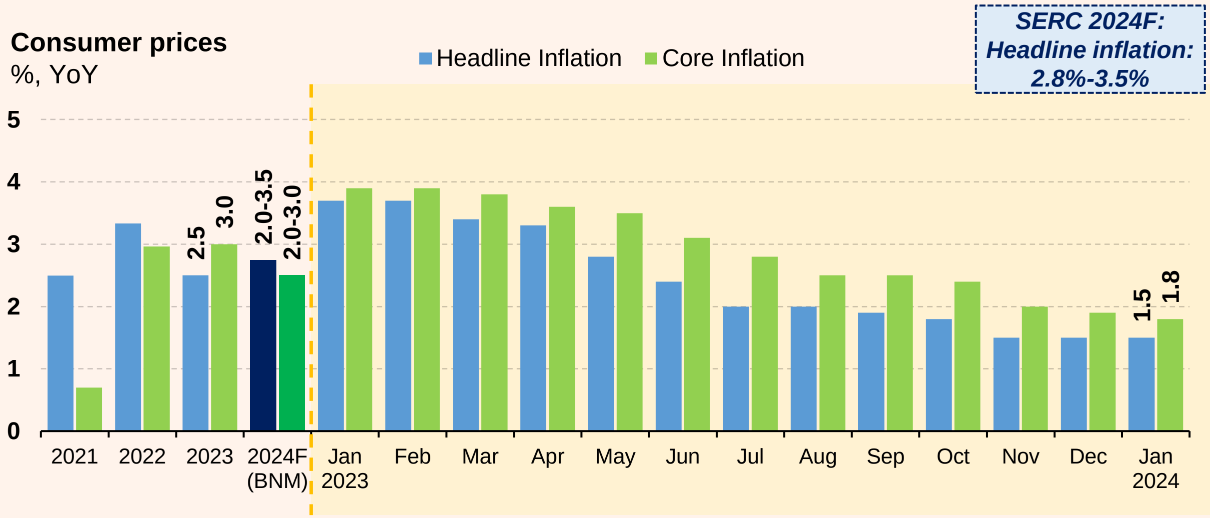
The current account is projected to register a higher surplus of between 1.8% and 2.8% of GDP in 2024



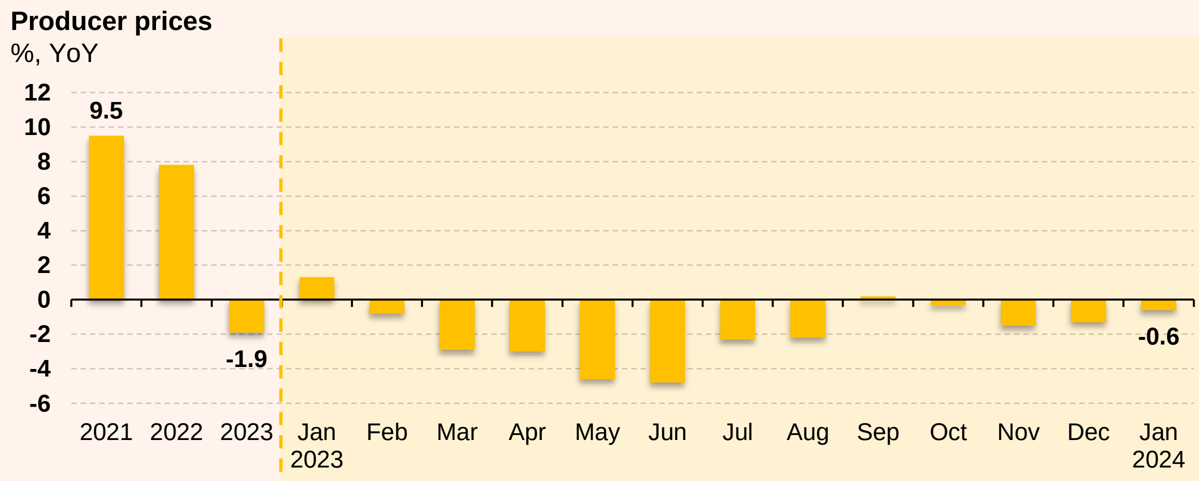
Source: DOSM; BNM; SERC

Headline inflation to average between 2.0% and 3.5% in 2024

Headline and core inflation



Producer prices



Source: BNM; DOSM; SERC estimates

Risks to the inflation outlook

Domestic policy factors such as subsidy rationalisation (fuel), tax changes and adjustments to utility tariffs.

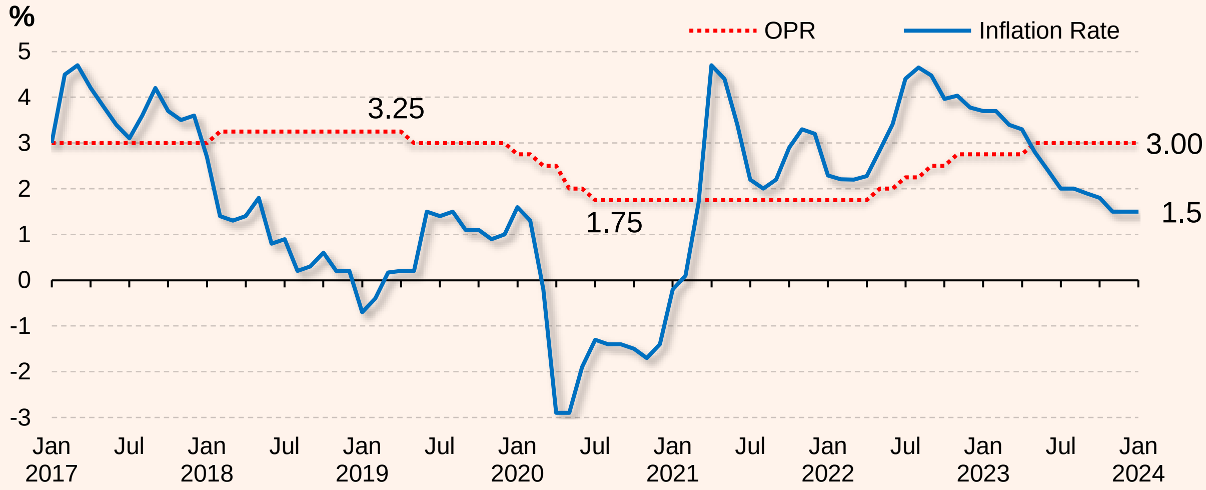
Exchange rate and **global commodity price developments** could further exacerbate the cost pressure to inflation.

Downside risks to inflation

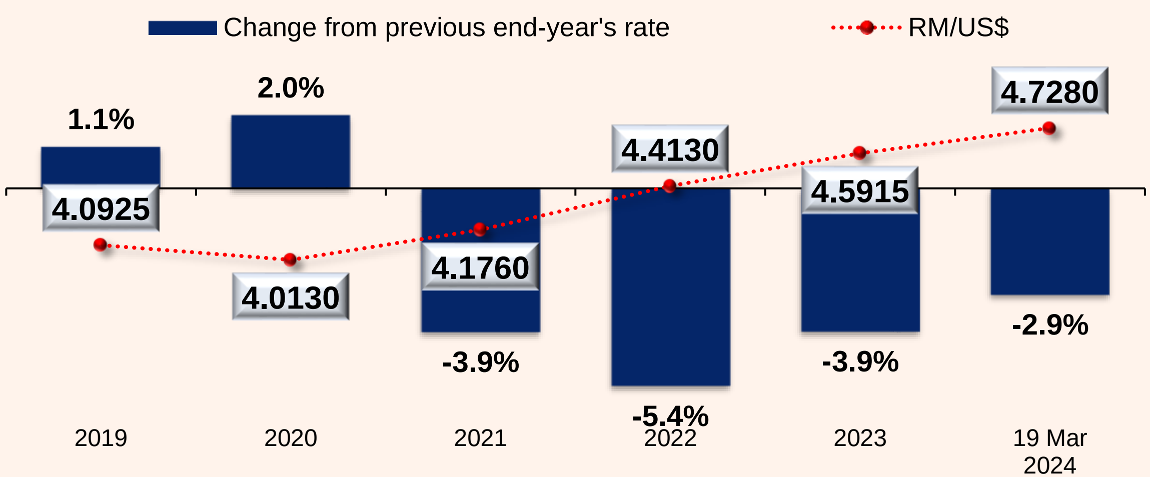
Softer commodity prices from weaker global growth.

Bank Negara Malaysia remains vigilant of ongoing developments

Overnight Policy Rate (OPR)



Exchange rates (RM/US)



Source: BNM; DOSM

Note: Exchange rate (12:00 rate) as at end-period

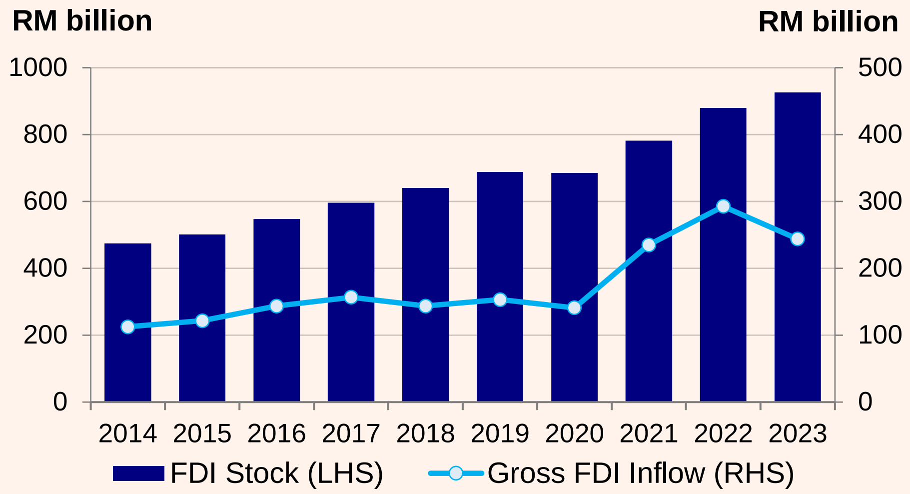
Domestic monetary and financial conditions are expected to **remain conducive to financial intermediation activities.**

Monetary policy will remain conducive to a sustainable economic growth while ensuring an environment of price stability.

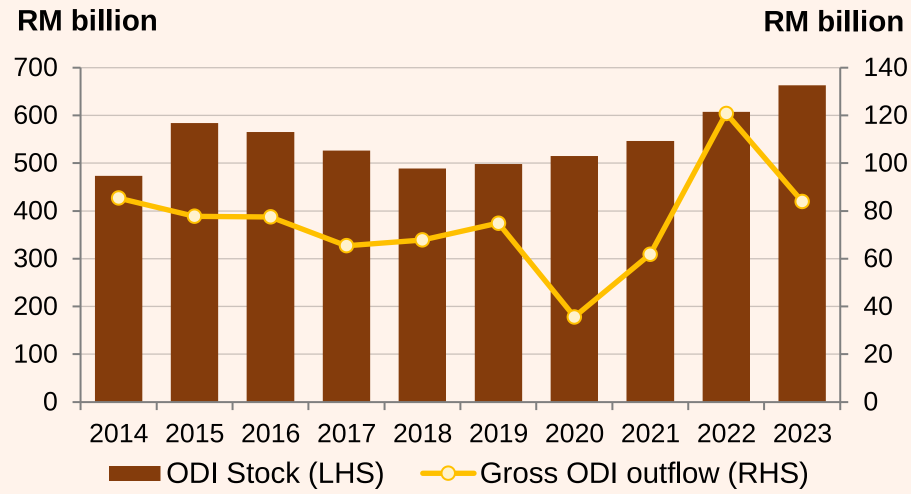
MPC remains vigilant of ongoing developments and their implications on the balance of risks surrounding domestic inflation and growth.

Malaysia continues to attract global investments

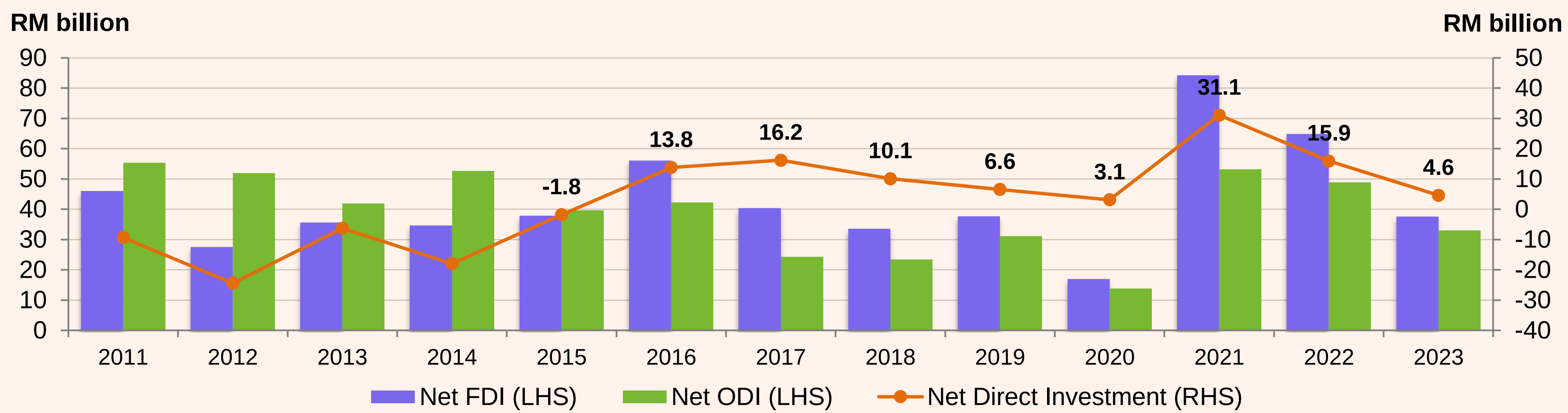
Gross FDI inflows remained high, realisation of approved investment is crucial



Gross ODI flows moderated to previous levels



Net inflows of direct investment narrowed for two consecutive years in 2023

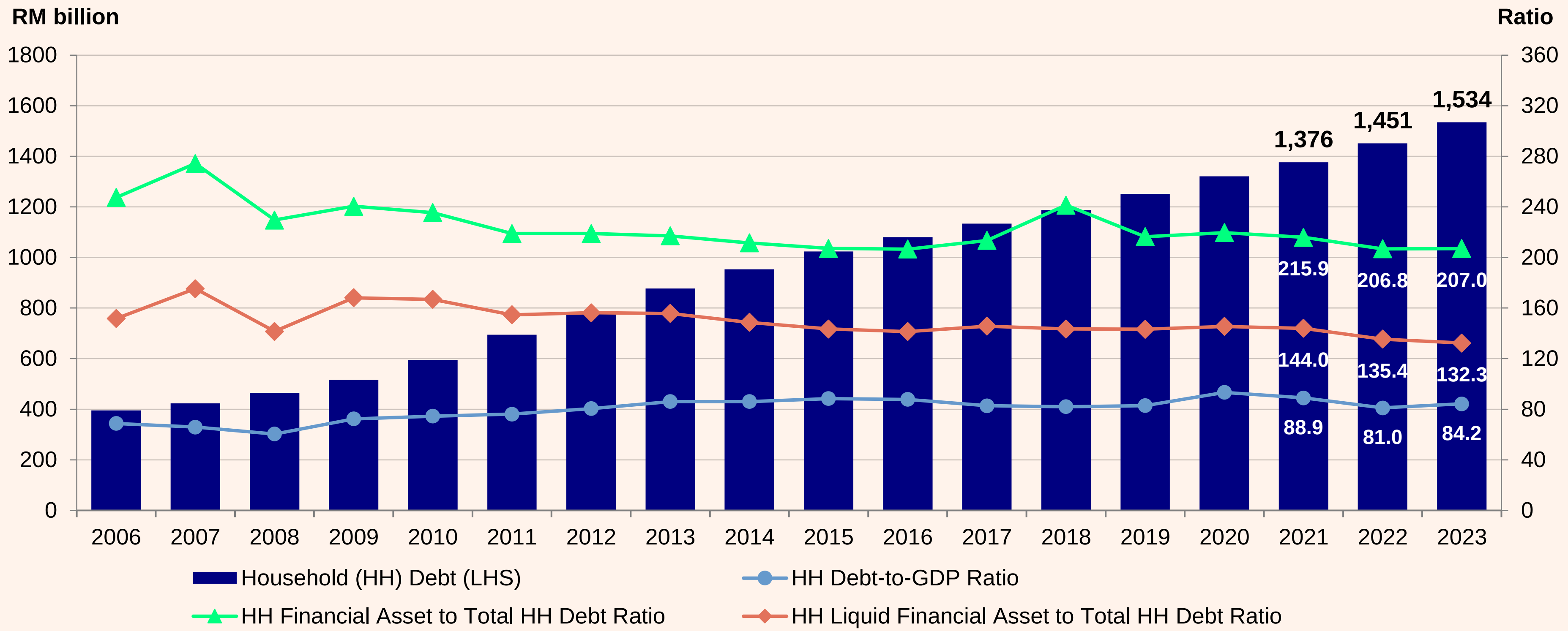


Source: BNM

FDI = Foreign direct investment; ODI = Outward direct investment

Overall household resilience remains intact amid favourable labour market conditions

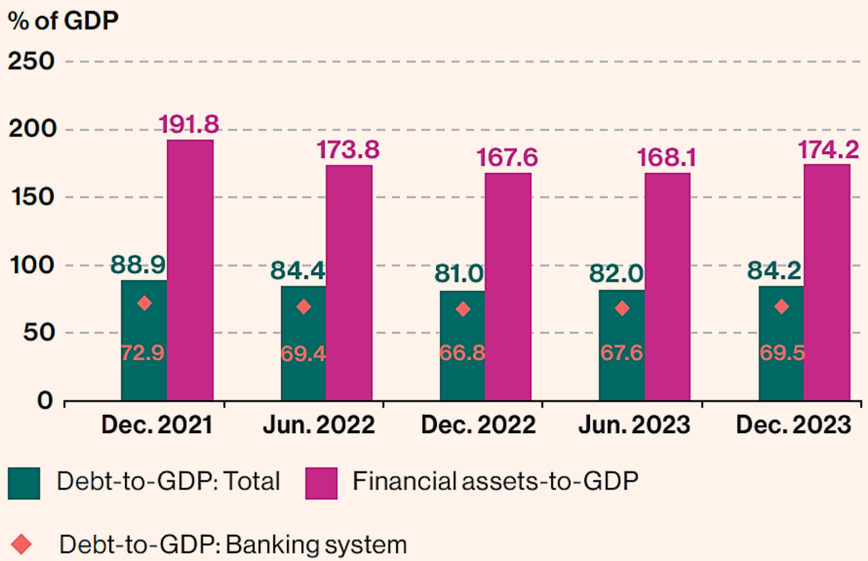
- **Household debt increased at a faster pace by 5.7% to RM1,534 billion in 2H 2023 from RM1,451 billion in 2H 2022 (5.4% in 2H 2022 and 4.2% in 2H 2021)**, largely driven by loans for the purchase of residential property and passenger cars, which collectively make up almost three-quarters (73.7%) of total household loans.
- The **ratio of household debt-to-GDP increased to 84.2% at end-2023 (81.0% in 2022)**. Nevertheless, about 70.9% of household banking system debt is held by middle-and higher-income borrowers with a monthly income of RM5,000 and above.



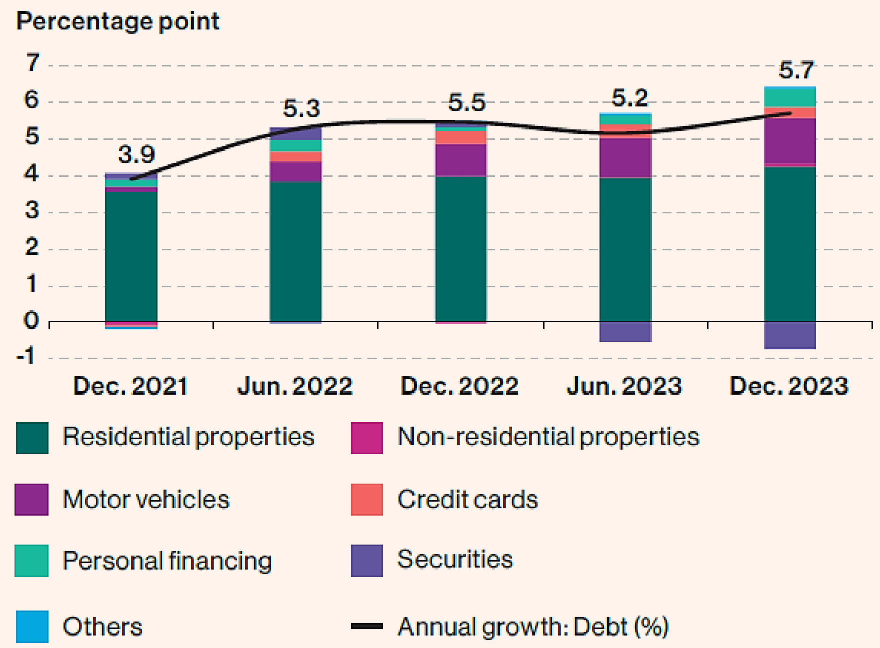
Source: BNM

Household sector debt conditions

Household Sector – Key Ratios



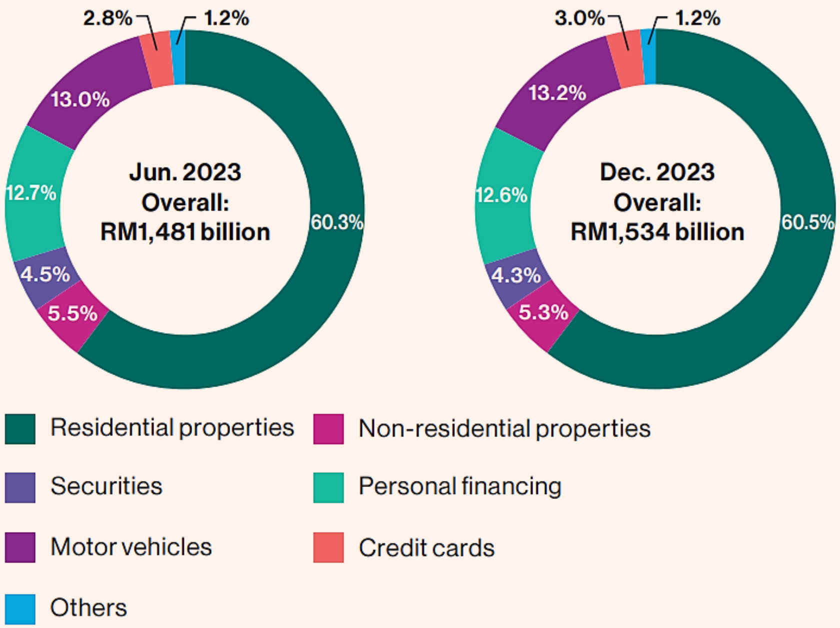
Household Sector – Annual Growth of Debt



Source: BNM; Bursa Malaysia; DOSM; Employees Provident Fund; Securities Commission

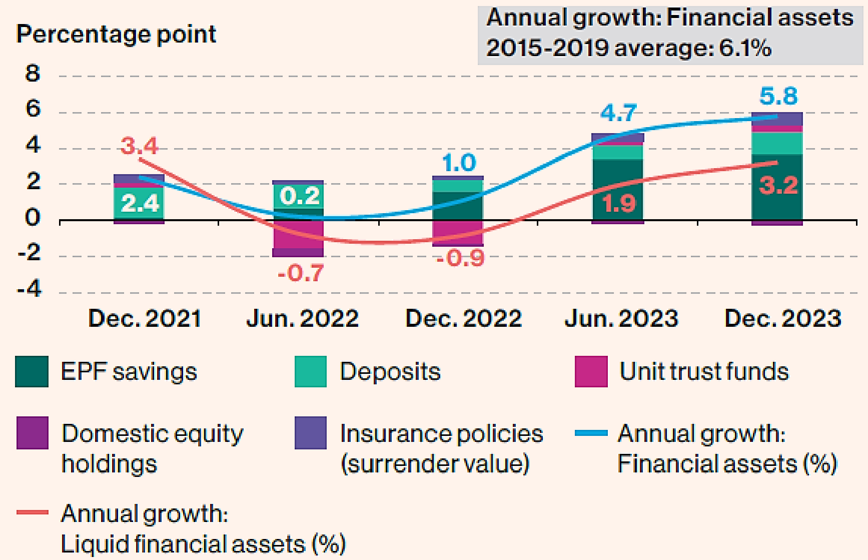
Household sector debt conditions (cont.)

Household Sector – Composition of Debt by Purpose



Note: Figures may not add up due to rounding.

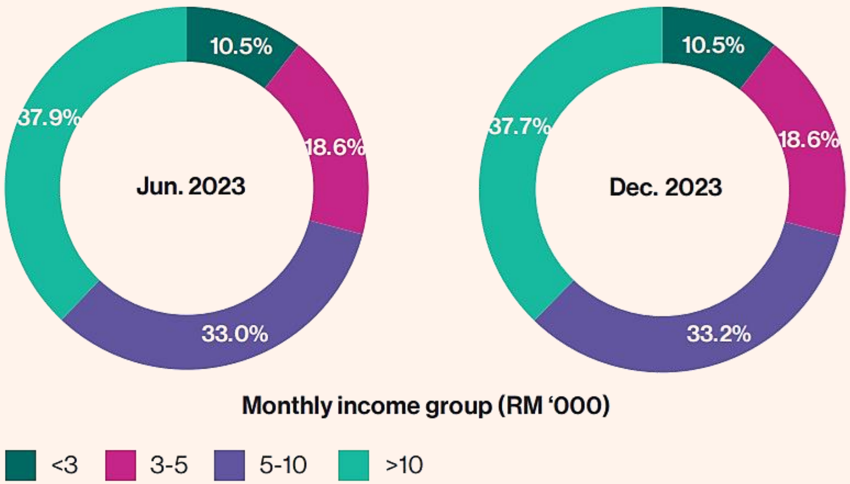
Household Sector – Annual Growth of Financial Assets



Source: BNM; Bursa Malaysia; DOSM; Employees Provident Fund; Securities Commission

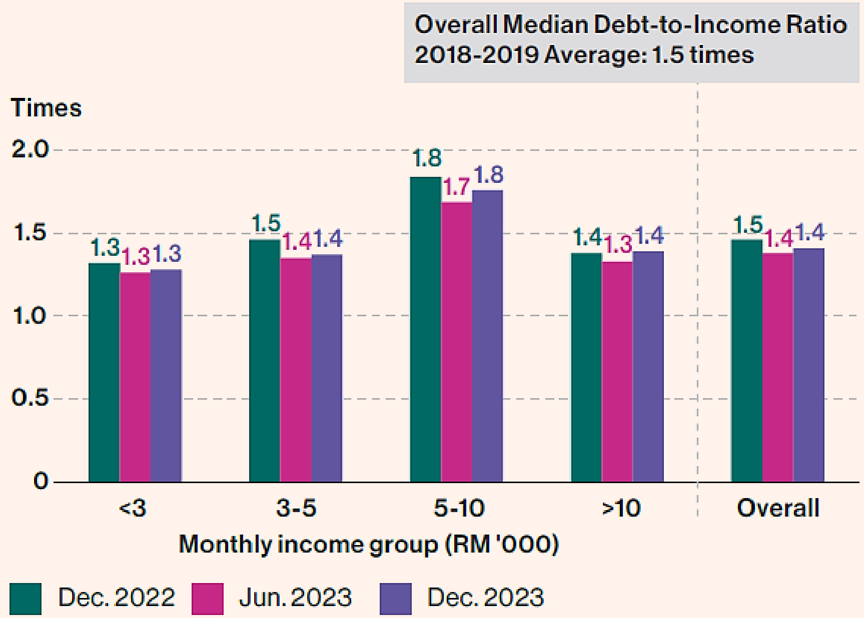
Household sector debt conditions (cont.)

Household Sector – Composition of Banking System Debt by Income Group



Note: 1. Figures exclude loan accounts with incomplete income information.
2. Figures may not add up due to rounding.

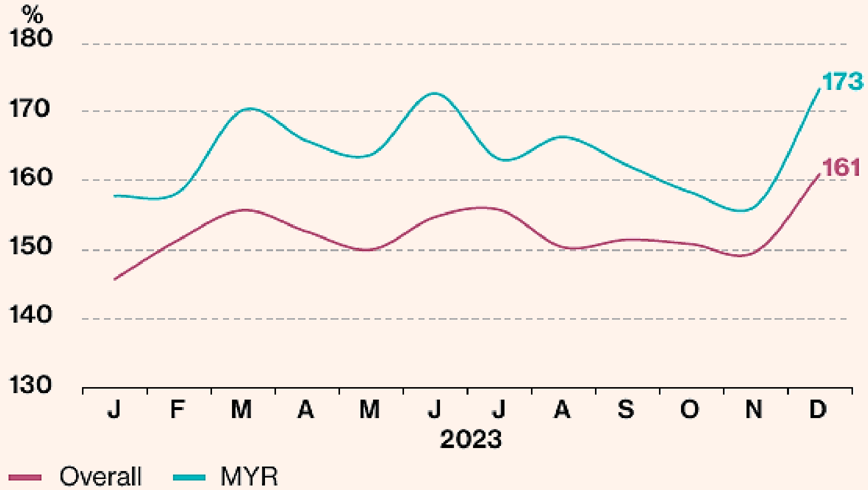
Household Sector – Median Debt-to-Income Ratios by Income Group



Source: BNM

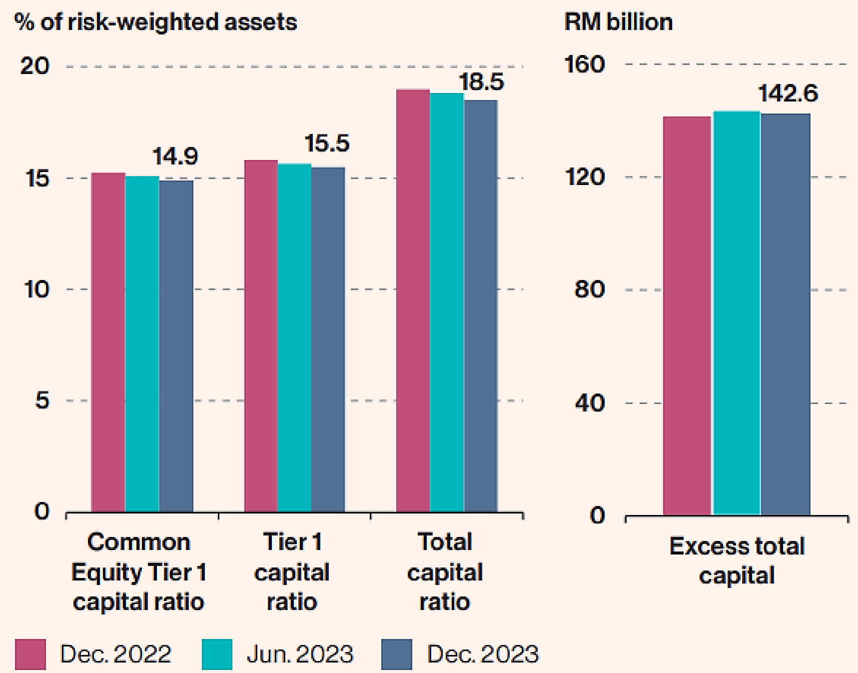
Banks' strong funding and liquidity positions supported intermediation activities

Banking System – Liquidity Coverage Ratio



Note: 1. MYR LCR is calculated based on HQLA and expected net cash outflows denominated in ringgit.
2. Overall LCR is calculated based on HQLA and expected net cash outflows denominated in all currencies.

Banking System – Capitalisation

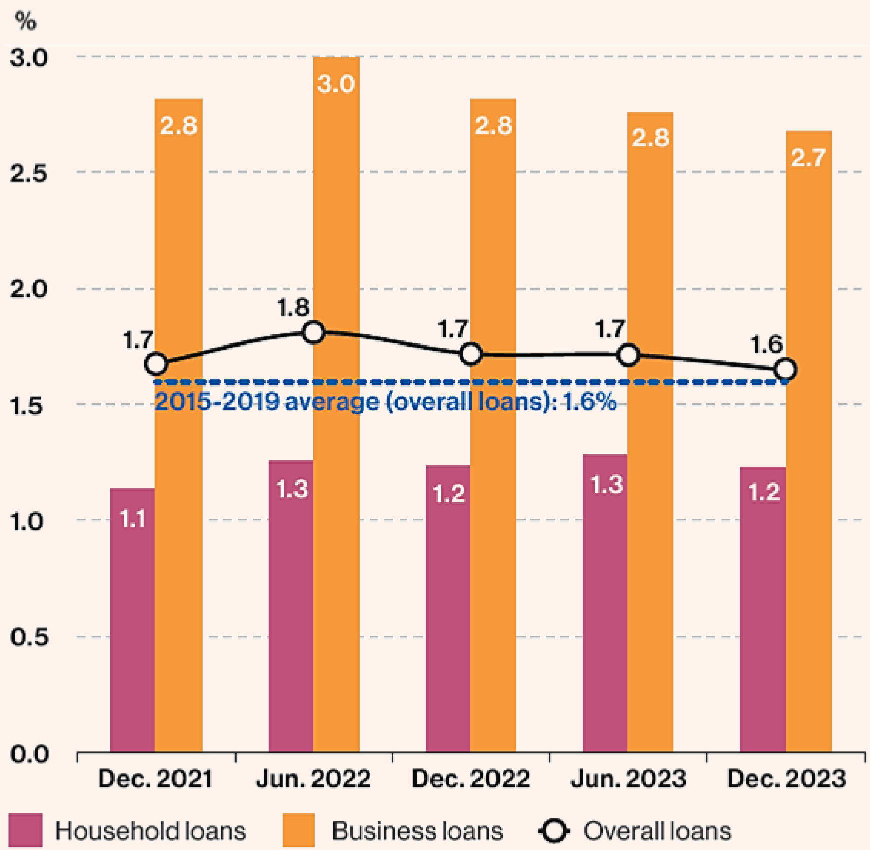


Note: Excess total capital refers to total capital above the regulatory minimum, which includes the capital conservation buffer requirement of 2.5% and bank-specific higher minimum requirements.

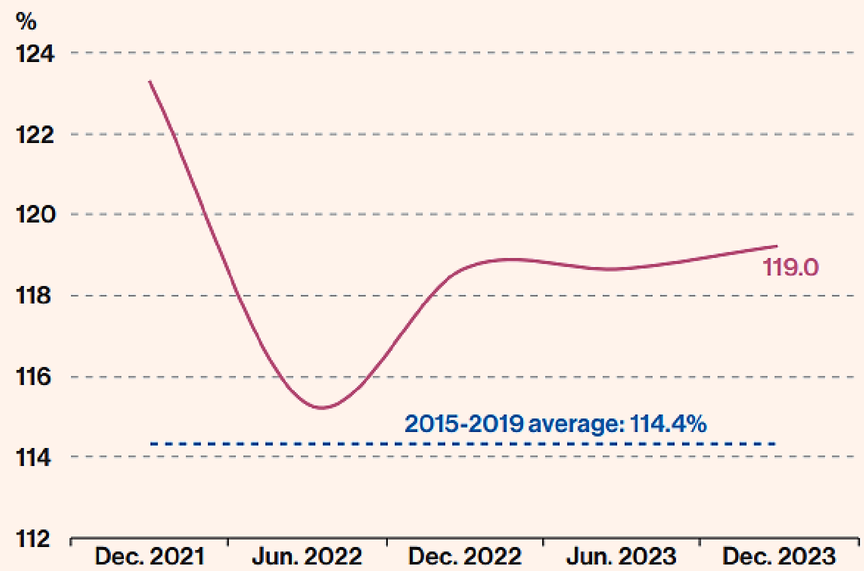
Source: BNM

Banks' asset quality improved but downside risks remain

Banking System – Gross Impaired Loans Ratio



Banking System – Loan Loss Coverage Ratio (Including Regulatory Reserves)



Source: BNM

SERC's commentaries

- Bank Negara Malaysia's (BNM) estimated **real GDP growth of 4.0-5.0% (mid-point estimate at 4.5%) in 2024 (3.7% in 2023), in line with SERC's estimates (4.5%)**. This growth will be supported by continued expansion of domestic demand and a rebound in gross exports (BNM's estimates of 5.0% vs. SERC's 4.0%).

- While the anticipated recovery in exports will aid economic growth, **we take a cautious view on the growth of private consumption (estimated 4.6% in 2024 vs. 4.7% in 2023 and +7.1% pa in 2011-2019) compared to BNM's 5.7%**. The continued high cost of living, increases in prices of food and beverages, higher service tax rate for selected categories and new scope of tax, the impact of weakening ringgit as well as the anticipated implementation of targeted fuel subsidy rationalisation will weigh on consumer spending. Nevertheless, stable employment growth (estimated jobless rate at 3.3%) and improved wage growth as well continued cash assistance (Sumbangan Tunai Rahmah) of RM10.0 billion for benefitting close to 9 million recipients will mitigate the targeted households and individuals against high cost of living.

- **BNM expects private investment to expand higher by 6.1% in 2024** (4.6% in 2023; 8.8% pa in 2011-2019) compared to SERC's 5.5%. The on-going implementation of multi-year infrastructure projects and continued capacity expansions as well as the realisation of some approved investments in previous years (2021-2022) are expected to underpin growth. Of significance, the progress of approved projects in recent years is well on track, with 74% of manufacturing projects approved from 2021 to 2023 being implemented or completed. We caution that increasing business operating costs and high cost of raw materials would dampen the business spending by small and medium enterprises (SMEs).

- **We concur with BNM's assessment that gross exports will rebound to +5.0% in 2024** (vs. SERC's +4.0%; -8.0% in 2023), thanks to an improvement in global trade, upturn in technology cycle as well as higher commodity and crude oil prices. The lead indicators lend credence to better exports ahead: A turnaround in global PMI, restocking of inventory to meet increased orders as well as higher chips demand (The World Semiconductor Trade Statistics (WSTS) expects global semiconductor sales to grow by 13.1% in 2024, rebounding from a decline of 8.2% in 2023).

- **BNM remains cautious about the inflation outlook in 2024** (estimated 2.0%-3.5% vs. SERC's 2.8%-3.5%; 2.5% in 2023) on the anticipated policy changes in domestic fuel subsidy rationalisation as well as the development in exchange rates and global commodity market. The central bank indicated that the exchange rate pass-through to inflation is limited as it estimated that a change in 5% in the RM/USD will result in core inflation to increase by 0.2 percentage points over the year.

- **Direct exchange rate pass-through to imports is evident, whereby 40% of exchange rate depreciation is translated to overall import prices.** BNM cautions that the impact could be larger amid prolonged depreciation, particularly for key necessities with high import content such as food (7%) and transportation (5%). The share of import content in domestic consumption is approximately 26%.

- On interest rate level, **we expect BNM to keep the overnight policy rate (OPR) at 3.00% for now** to sustain firmer economic growth amid the expected higher inflation expectations. This is despite a projected cut in the Fed funds rate by 75 basis points in 2H 2024 to 4.50%-4.75%.

- **The elevated household debt of RM1.53 trillion or 84.2% of GDP at end-Dec 2023 (RM1.02 trillion or 88.4% GDP at end-2015) warrants closer monitoring** as it can be a significant destabilising factor to the economy and financial sectors. A highly leveraged household is vulnerable to income and employment shocks as well as monetary policy changes such as an increase in interest rate.

- While households' debt repayment capacity was preserved by improving labour market conditions and fiscal support for the vulnerable households, **some segments of borrowers continue to face repayment challenges, particularly those are earning lower income, their income levels have fully recovered since the COVID-19 pandemic and they were previously placed under repayment assistance programmes**. It must be noted that the enrolment to AKPK's Debt Management Programme (DMP) has increased to 52,057 persons in 2023 (34,670 in 2022).

- **Amid persisting cost pressures in some sectors, more SMEs are showing signs of vulnerabilities**. The share of SMEs missing repayments rose to 2.1% of total SME loans at end-Dec 2023 (1.6% at end-Jun 2023) while SMEs impairments also increased to 3.1% at end-Dec 2023 from 2.9% at end-Jun 2023. The continued cost pressures in 2024 are expected to weigh on some SMEs amid the expected improvement in economic and business conditions.

- We support BNM's short-term efforts (refer to slide 26) to help stabilise the Ringgit while the Government must remain committed towards undertaking structural reforms to strengthen fiscal position and contain its debt level, to boost productivity, enhance better investment climate to retain domestic investment and attract more high quality FDI, improve education outcomes, enhance skill set, accelerate the climate transition, and make growth more inclusive, ensuring access to economic opportunities for all.
- The bottom line is the Ringgit exchange rate is one of the most important determinants of a country's relative level of economic health and relative competitiveness in the terms of trade as well as the capital movements in terms of real rate of return on investment.
- While exchange rates are determined by numerous complex external and domestic factors, the Government has to offer compelling economic and investment proposition as well as strong corporate earnings prospects to lure more foreign investors and domestic investors investing in domestic asset classes. As at end-Jan 2024, Malaysians (individuals and corporates) have placed RM247.4 billion worth of foreign currencies deposit, equivalent to 10.4% of total banking system deposit, representing a big jump from RM53.5 billion or 4.7% of total deposit at end-2010. Domestic residents' portfolio outflows investing in equities, investible funds and bonds were larger at RM28.9 billion per year in 2010-2023.
- In addition to strengthening the shrinking current account surpluses and reduce services outflows, we have to strengthen the financial account (which measures foreign money flowing into the country and domestic residents' money investing abroad).

Spotlights on selected BNM's Feature Articles

1. Navigating Economic Cycles: Interactions between Monetary and Fiscal Policy

2. The Case for Labour Market Reforms in Malaysia: Challenges and Opportunities

3. The Ringgit in Perspective

4. Supporting SMEs Transition to Greener Practices

1. Navigating Economic Cycles: Interactions between Monetary and Fiscal Policy

Stylised Facts on Monetary and Fiscal Policy

	Monetary Policy	Discretionary Fiscal Policy
Definition	Involves the use of policy instruments (e.g. interest rates, liquidity operations, etc) by central banks to manage inflation and support economic activity (e.g. growth or employment)	Refers to the use of government spending, taxation, and borrowing to influence the level of aggregate demand, promote growth, and meet various socioeconomic objectives
Similarities		
Orientation	Counter-cyclical tools impacting aggregate demand	
Time-horizon	Focused on short-run impact with a timeframe of 12–36 months, although fiscal multiplier impact can persist much longer	
Distributional effect	Pervasive distributional effect on income and wealth; Fiscal policy can transfer resources between sectors and segments while monetary policy can transfer resources between savers and borrowers	
Differences		
Objectives	To control inflation and/or growth by influencing aggregate demand	Influencing aggregate demand and ensuring stability in aggregate supply towards achieving macroeconomic goals (e.g. sustainable growth, employment and price stability)
Transmission mechanism	Occurs through channels of interest rates, asset prices, credit, exchange rate and expectations	Occurs through channels of consumption and investment
Impact	Generally, a blunt tool with broad-based impact	Can be both broad-based or targeted to specific sectors or segment

Outcomes of balanced approach to policies

1. **Preserves macroeconomic stability**
2. **Maximises the effectiveness of each policy**
3. **Prevents overburdening of policies**

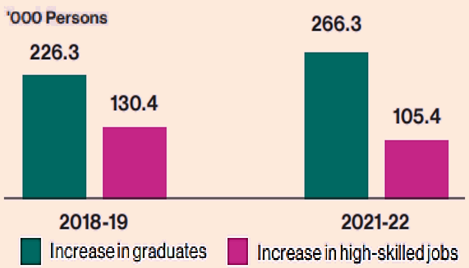
During the COVID-19 pandemic period:

- **Monetary policy:** OPR was reduced by 125 basis points to a historical low of 1.75% between January and July 2020.
- **Fiscal policy:** Eight stimulus and assistance packages totalling RM530 billion

2. The Case for Labour Market Reforms in Malaysia: Challenges and Opportunities

Comprehensive and strategic labour market reforms are critical to build a resilient workforce and secure sustainable growth

Labour market landscape



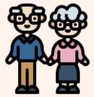
- The pace of increase in high-skilled jobs lags the average number of new graduates in the labour force.
- Malaysia also lags behind many advanced and regional economies in terms of share of high-skilled jobs.
- In 2022, the median starting salary for fresh graduates (RM1,624) was more than 20% lower compared to the 2019 level (RM2,066).

Key megatrends will present challenges and opportunities

Technological advancement

Reconfiguration of supply chains

Green transition



Ageing population

Comprehensive reforms

#1 Address skills mismatch

Government, academia & industry collaboration to enhance education and training

#2 Upskill the workforce for the future

Promote lifelong learning for an agile workforce

#3 Create high-skilled jobs

Encourage widespread technological adoption and high-quality investment

#4 Design foreign worker policies in line with development needs

Reduce low-skilled foreign workers as well as attract and retain high-skilled talents

#5 Fair compensation and social protection for workers

Enhance existing wage policies and improve social protection

3. The Ringgit in Perspective

Overall, exchange rate movements are influenced by:

Short-term:

- Cyclical fluctuations in the domestic and global economies
- Interest rate differentials
- Geopolitical developments

Long-term (by fundamental determinants):

- Nation’s relative labour productivity
- Investment environment
- Overall economic competitiveness

Recent movements of the Ringgit since 2022 has been predominantly influenced by cyclical factors:

- ➢ Aggressive monetary policy tightening by the US Federal Reserve (Fed).
- ➢ Shifting financial market expectations surrounding the outlook for US monetary policy.

Malaysia’s economic fundamentals have remained sound:

- ✓ Resilient economic growth with a declining inflation trend.
- ✓ Current account surplus, manageable external debt levels, a net external asset position, and adequate international reserves.

Measures

Short-term efforts by BNM:

- Encourage repatriation and conversion of foreign investment income by GLCs and GLICs
- Engage with resident exporters and monitor their conversion of export proceeds to Ringgit
- Advocate greater use of local currency

Long-term structural reforms by the Government:

- Ensure fiscal sustainability
- New growth potential
- Enhance labour productivity and competitiveness

4. Supporting SMEs Transition to Greener Practices

Climate change

Physical risk

- Changing climate conditions
- Extreme weather events

Transition risk

- Policy Changes
- Technological Innovation

Liability risk

- Stakeholder Litigation
- Regulatory Enforcement

Impact to businesses

- **Disruption to operations**
- **Losses and damages**
- **Increased cost of doing business**
- **Negative impact to asset values**

Initiatives and Tools to Support SMEs in their Business Transition

Tools to support SMEs transition

- JC3 ESG Jumpstart Portal
- Simplified ESG Disclosure Guide (SEDG)

Financial solutions

Financing facilities

- Low Carbon Transition Facility (LCTF)
- High Tech & Green Facility (HTG)
- Portfolio Guarantee Scheme by CGC

Blended finance programs

- GVC Programme
- Green Agritech

Products & solutions by FIs

- General financing for purchase of technology or working capital
- Climate advisory
- Protection

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