



**社会经济研究中心**  
**SOCIO-ECONOMIC**  
**RESEARCH CENTRE**

**Quarterly Economy Tracker (Oct-Dec 2017)**

**Malaysia: Seeking sustainable growth**

**Lee Heng Guie**  
**Executive Director, SERC**  
17 January 2018

# Agenda



**GLOBAL ECONOMY TO CONTINUE MOMENTUM**



**GLOBAL ECONOMIC RISKS TO WATCH**



**MALAYSIA: WHAT TO EXPECT IN 2018?**



**HOW RESILIENCE IS MALAYSIA TO SHOCKS?**



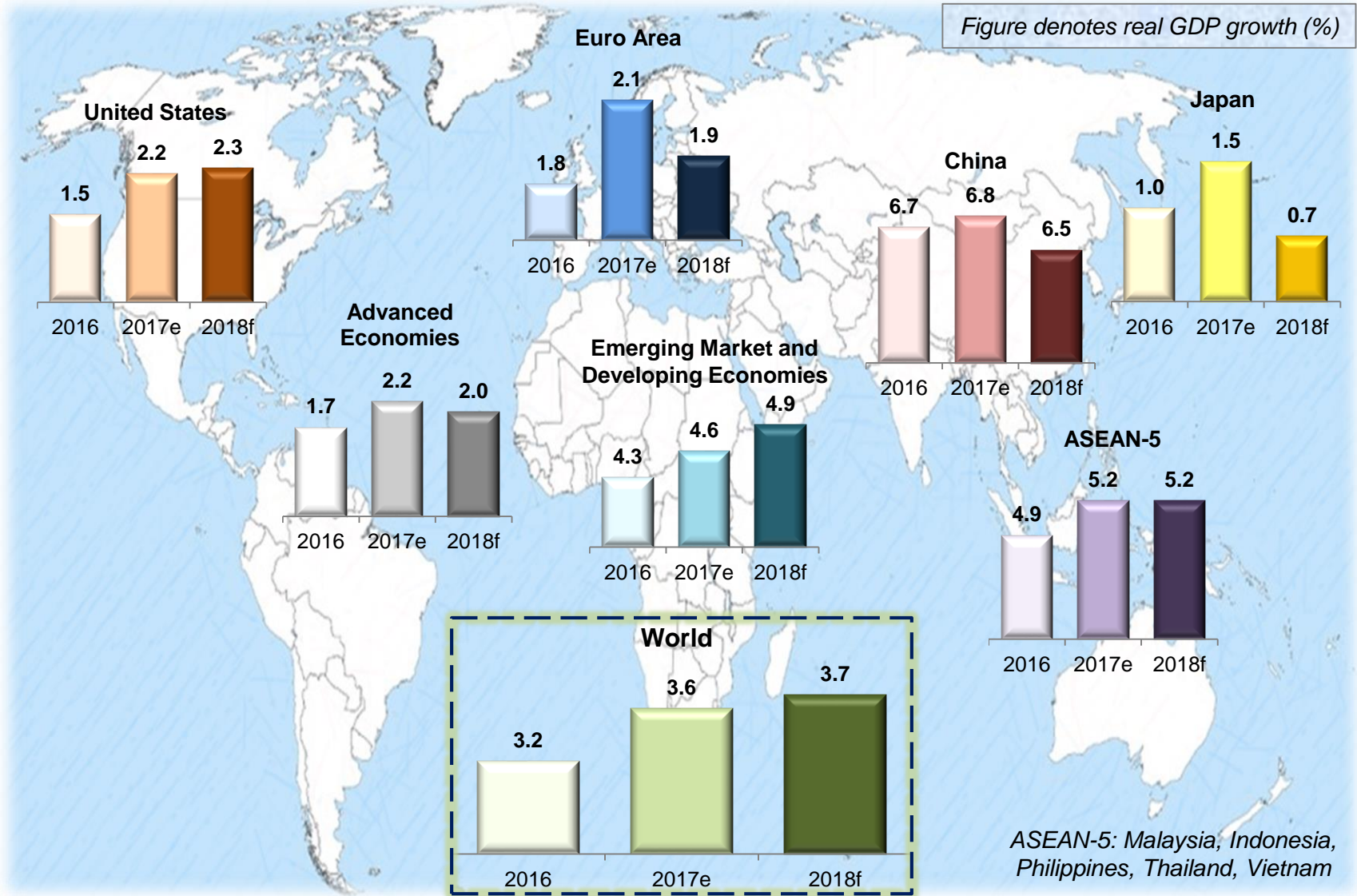
**MEDIUM- AND LONG-TERM POLICY CHALLENGES**

# PROBING questions

- How **SUSTAINABLE** is the current global economic upswing?
- What are key **CHALLENGES** to boost potential output while building resilience against downside risks?
- Will there be a **SYNCHRONISED TIGHTENING** in global monetary policy in 2018?
- Can Malaysia stay **RESILIENT** in challenging times?
- Step up **POLICY REFORMS** to address and contain **VULNERABILITIES** to build economic resilience



# Global ECONOMIC UPSWING, is the recovery COMPLETE?



Source: IMF

# Mapping global prospects, **CHALLENGES** and **RISKS**

## Global economy on upswing, but risks remain

- Recovery is **INCOMPLETE**; some still weak
- Short-term growth supported by improved confidence and pent-up demand
- Potential for much faster growth - **WEAK PRODUCTIVITY; AGING POPULATION**
- Improve **GOVERNANCE** and the **INVESTMENT CLIMATE**

## Policy risks

- Hopes fading if policy outcomes fall short of market expectations
- **POTENTIAL DISRUPTIONS**: inward-looking policies, Brexit's negotiation & geo-politics
- Volatility induced by the withdrawal of monetary easing and shrinking balance sheet
- Monetary policy – From **DIVERGENCE TO CONVERGENCE?**

## Contain financial vulnerabilities

- Stretched asset valuations and increasing **LEVERAGE** (Global debt to GDP: 318% at 3Q17)
- **UNSUSTAINABLE** asset prices, credit growth and debt implosion
- Chinese to rein in **CREDIT EXPANSION AND CONTROL DEBT** (2017: 257% of GDP)

# Malaysian economy: What to EXPECT in 2018? UPSIDE RISK!

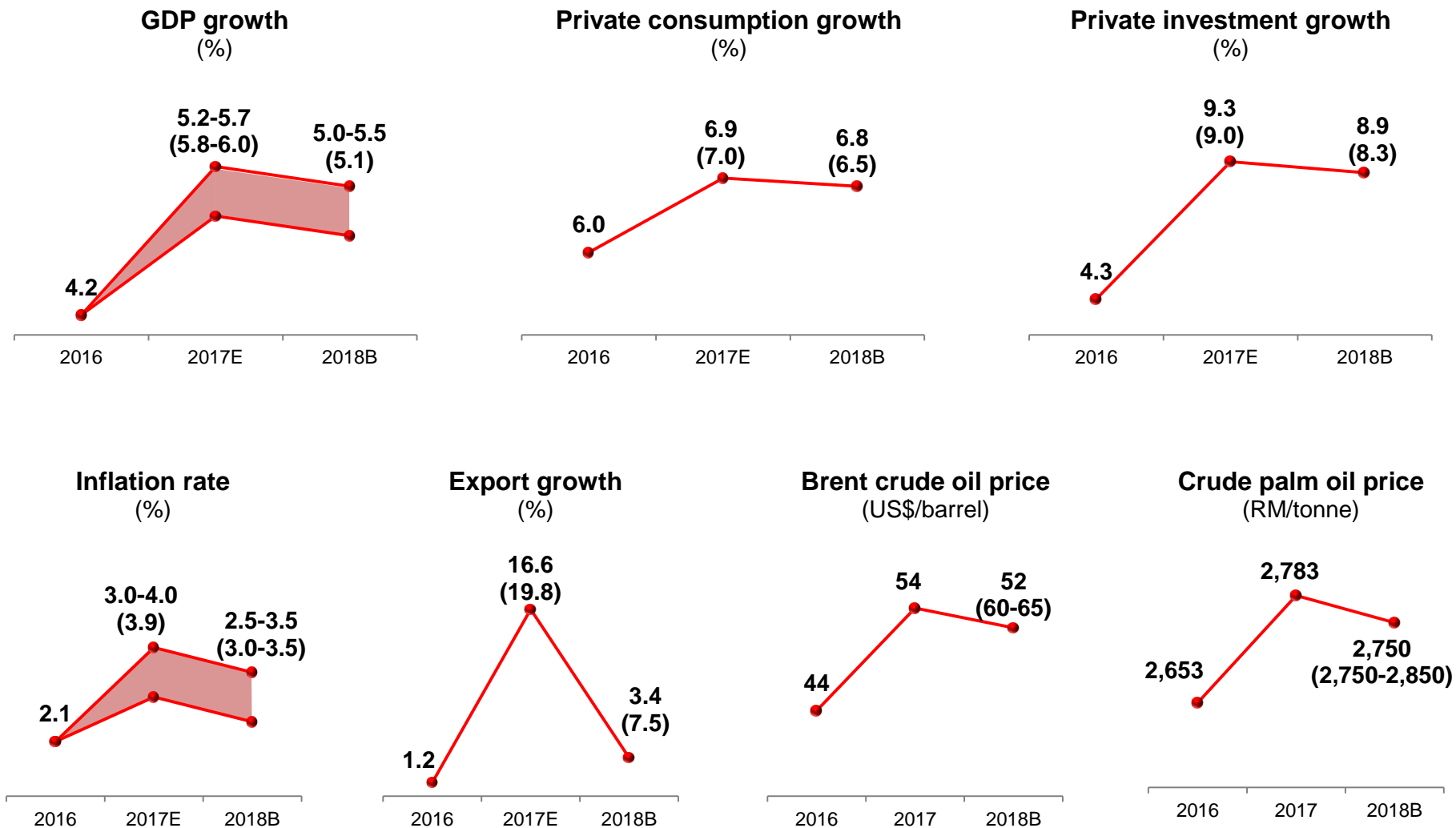


Figure in parenthesis denotes SERC's estimation and forecast  
 Source: MOF (Economic Report 2017-18); EIA; MPOB; SERC

# Sectoral outlook: Positive, BROAD-BASED EXPANSION

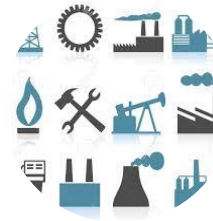


## Services

**2018F: 5.6% (2017E: 6.1%)**

*% share of GDP: 54.5*

- Sustained domestic spending, higher tourist arrivals, logistic services and financial services
- Higher growth in wholesale and retail trade, F&B, information and communication, transport and storage as well as finance and insurance subsectors



## Manufacturing

**2018F: 5.5% (2017E: 6.3%)**

*% share of GDP: 23.0*

- Export-oriented industries: sustained demand for electronics and electrical products, refined petroleum and wood products
- Domestic-market oriented: construction-related building materials, food products and transport equipment



## Agriculture

**2018F: 3.8% (2017E: 5.5%)**

*% share of GDP: 8.1*

- Slower rise in CPO production and rubber output
- Livestock, fruits and vegetables



## Construction

**2018F: 8.0% (2017E: 7.2%)**

*% share of GDP: 4.6*

- On-going civil engineering infrastructure projects such as ECRL, MRT SSP line, Electrified Double Track Gemas-Johore Bahru, SPE, Pan Borneo Highway and Bokor Central Processing Platform
- Property overhang glut Slow growth in commercial development due to property overhang



## Mining

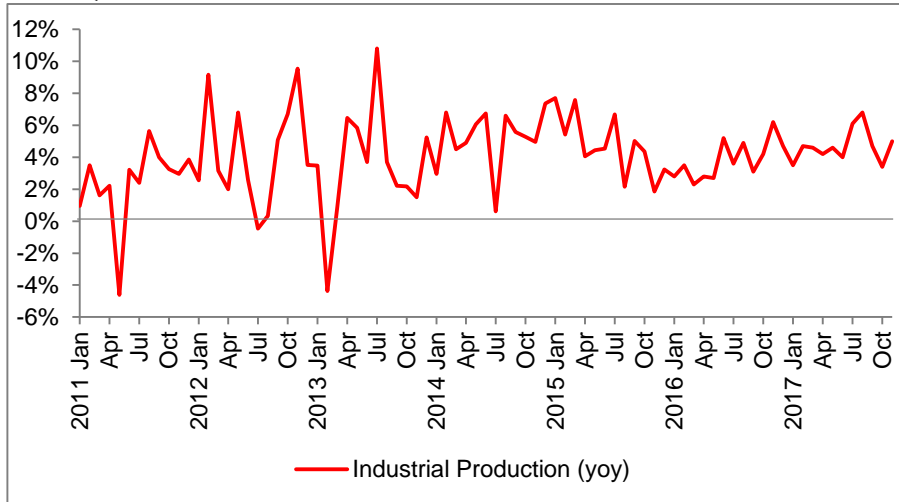
**2018F: 1.5% (2017E: 1.7%)**

*% share of GDP: 8.4*

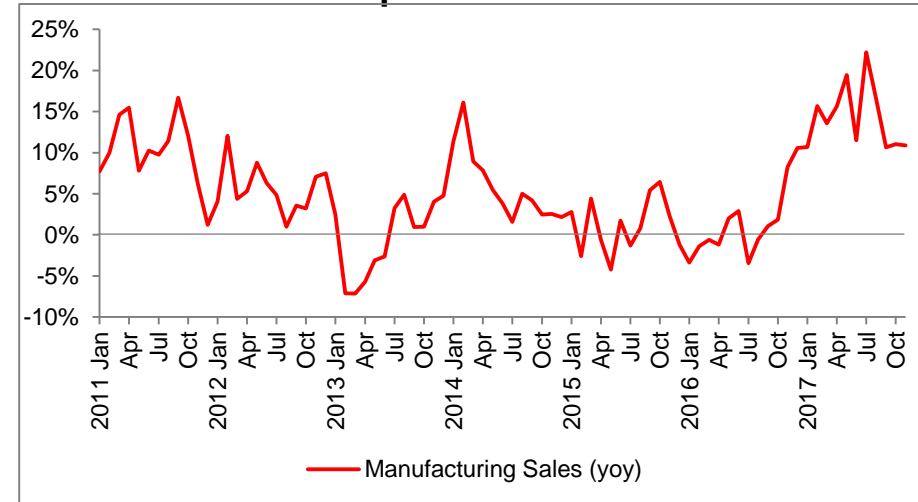
- Higher natural gas output
- Malaysia agrees to extend oil output cuts until end-2018
- Brent price to average US\$60-65 per barrel in 2018 vs 2018 Budget's US\$52

# Economic indicators still looking GOOD

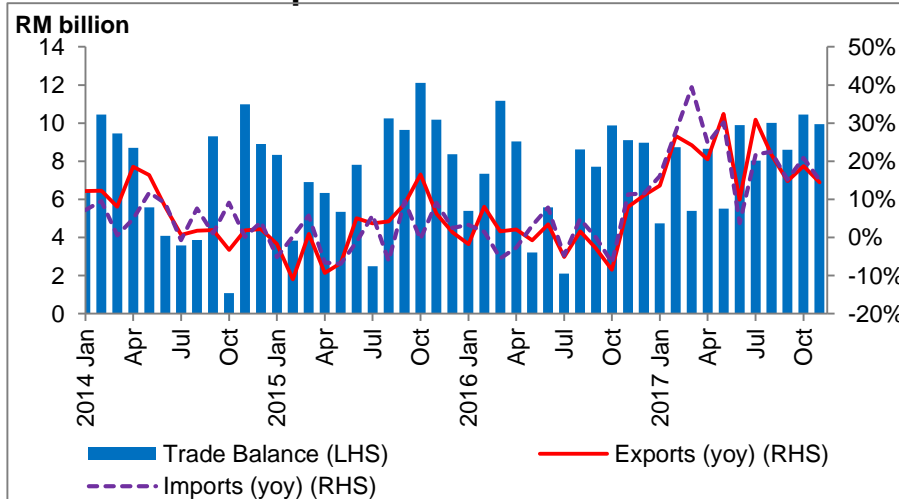
## Industrial production continue to grow steadily in 4Q17



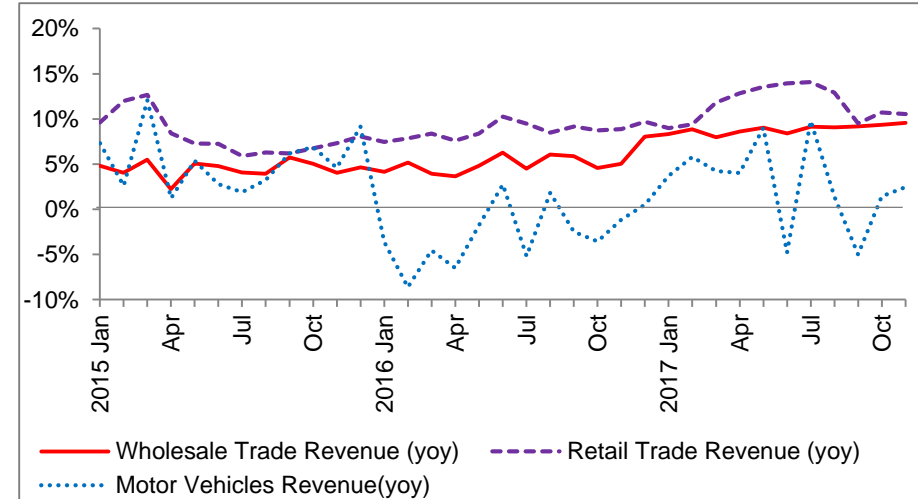
## Manufacturing sales held strongly, albeit moderated from the peak



## Robust exports growth on higher global demand and chip sales



## Wholesale and retail sectors remain the key economic driver

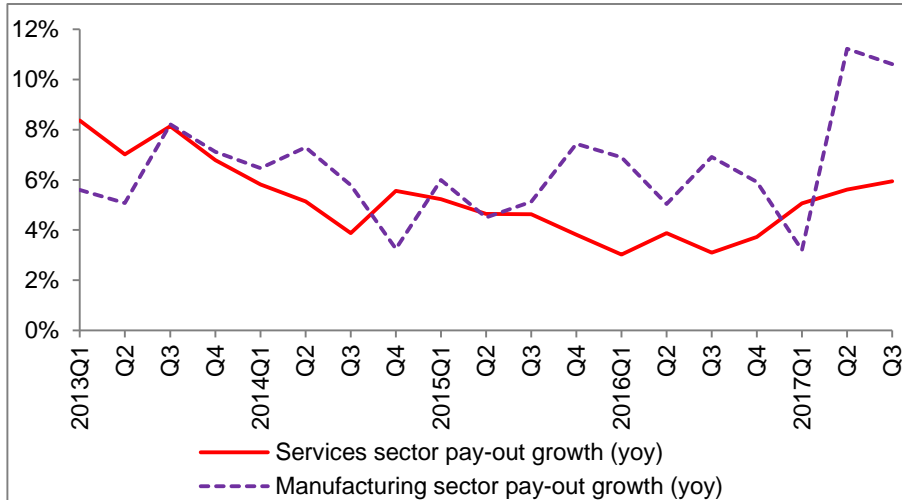


Source: DOS, Malaysia

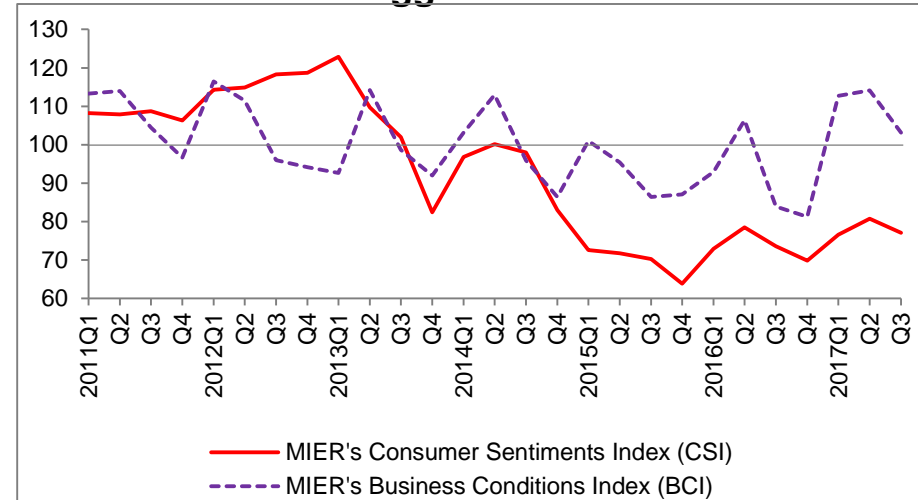


# But, SENTIMENTS move in opposite direction

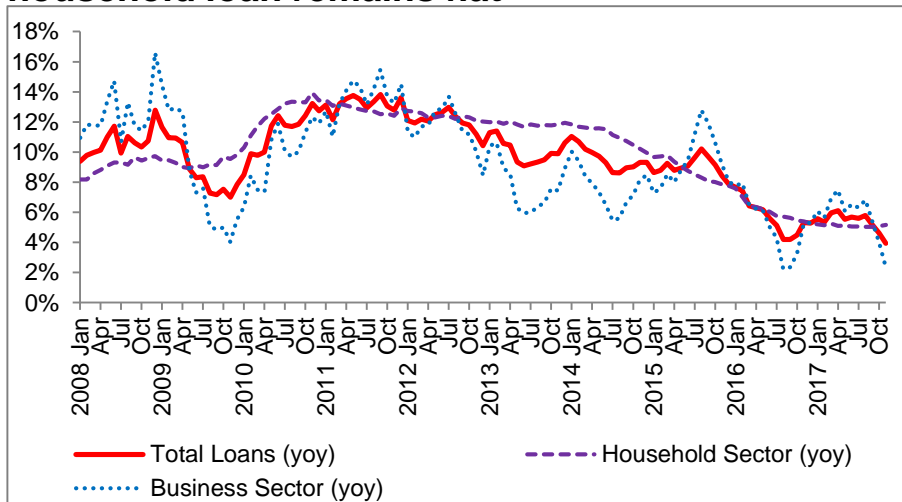
... even with higher growth in wages and salaries



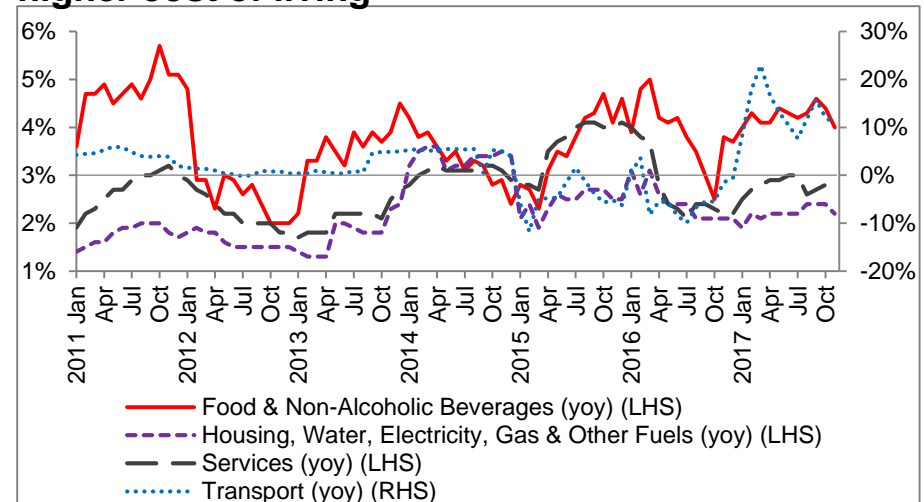
Business is more prudent and consumer sentiment remain sluggish



Business loan growth eased sharply; household loan remains flat



Increasing food and fuel prices adding to higher cost of living



Source: DOS, Malaysia; BNM; MIER

# Sources of GDP growth: Demand and supply side

- Strong growth momentum; broad-based growth; resilient private sector activity

| <i>% change, 2010=100</i>             | 2015       | 2016       | 2017<br>Jan-Sep | 2017E<br>(MOF) | 2017E<br>(SERC) | 2018B<br>(MOF) | 2018F<br>(SERC) |
|---------------------------------------|------------|------------|-----------------|----------------|-----------------|----------------|-----------------|
| <b>GDP by demand component</b>        |            |            |                 |                |                 |                |                 |
| Private consumption (53.9%)           | 6.0        | 6.0        | 7.0             | 6.9            | 7.0             | 6.8            | 6.5             |
| Private investment (17.5%)            | 6.3        | 4.3        | 9.3             | 9.3            | 9.0             | 8.9            | 8.3             |
| Public consumption (12.7%)            | 4.4        | 0.9        | 4.9             | 2.7            | 4.9             | 1.3            | 4.0             |
| Public investment (8.4%)              | -1.1       | -0.5       | 0.8             | 3.7            | 1.0             | -3.1           | 0.5             |
| Exports of goods and services (72.2%) | 0.3        | 1.1        | 10.4            | 8.0            | 9.9             | 2.3            | 6.8             |
| Imports of goods and services (64.7%) | 0.8        | 1.1        | 12.3            | 9.9            | 11.7            | 2.5            | 7.8             |
| <b>GDP by economic sector</b>         |            |            |                 |                |                 |                |                 |
| Agriculture (8.1%)                    | 1.3        | -5.1       | 6.0             | 5.6            | 5.5             | 2.4            | 3.8             |
| Mining & quarrying (8.4%)             | 5.3        | 2.2        | 1.6             | 0.5            | 1.7             | 0.9            | 1.5             |
| Manufacturing (23.0%)                 | 4.9        | 4.4        | 6.2             | 5.5            | 6.3             | 5.3            | 5.5             |
| Construction (4.6%)                   | 8.2        | 7.4        | 6.9             | 7.6            | 7.2             | 7.5            | 8.0             |
| Services (54.5%)                      | 5.1        | 5.6        | 6.2             | 5.9            | 6.1             | 5.8            | 5.6             |
| <b>Overall GDP</b>                    | <b>5.0</b> | <b>4.2</b> | <b>5.9</b>      | <b>5.2-5.7</b> | <b>5.8</b>      | <b>5.0-5.5</b> | <b>5.1</b>      |

*Parenthesis indicates % share to GDP in 2017E by MOF*

*Source: DOS, Malaysia; MOF (Economic Report 2017-18); SERC*

# Getting ready to INTEREST RATE HIKES in 2018

- **OUR BASELINE CALL IS 25 BASIS POINTS HIKE FOR A START.** The market must prepare for further rise in rates if the following conditions are met throughout the year 2018:
  - 1) If the global growth and domestic economy continues to sustain at strong levels, supported by domestic demand;
  - 2) To anchor inflation expectations should headline and core inflation continue to remain at elevated levels as oil prices remain a wild card. BNM needs to stay ahead of the inflation curve; and
  - 3) To balance the yield gaps should the Fed hike rates aggressively.

|                                  | 2007     | 2008     | 2009     | 2010     | 2016     | 2017                | 2018 <sup>F</sup> |
|----------------------------------|----------|----------|----------|----------|----------|---------------------|-------------------|
| <b>OPR</b>                       | 3.50% =  | 3.25% ↓  | 2.00% ↓  | 2.75% ↑  | 3.00% ↓  | 3.00% =             | 3.25-3.50% ↑      |
| <b>GDP</b>                       | 6.3% ↑   | 4.8% ↓   | -1.5% ↓  | 7.4% ↑   | 4.2% ↓   | 5.8% <sup>1</sup> ↑ | 5.1% ↓            |
| <b>Inflation</b>                 | 2.0% ↓   | 5.4% ↑   | 0.6% ↓   | 1.7% ↑   | 2.1% =   | 3.9% <sup>1</sup> ↑ | 3.0-3.5% ↓        |
| <b>RM/US\$1<br/>(end-period)</b> | 3.3115 ↑ | 3.4675 ↓ | 3.4265 ↑ | 3.0855 ↑ | 4.4860 ↓ | 4.0475 ↑            | 3.80-3.90 ↑       |

**ARE YOU PREPARED FOR  
RISING INTEREST RATES?**

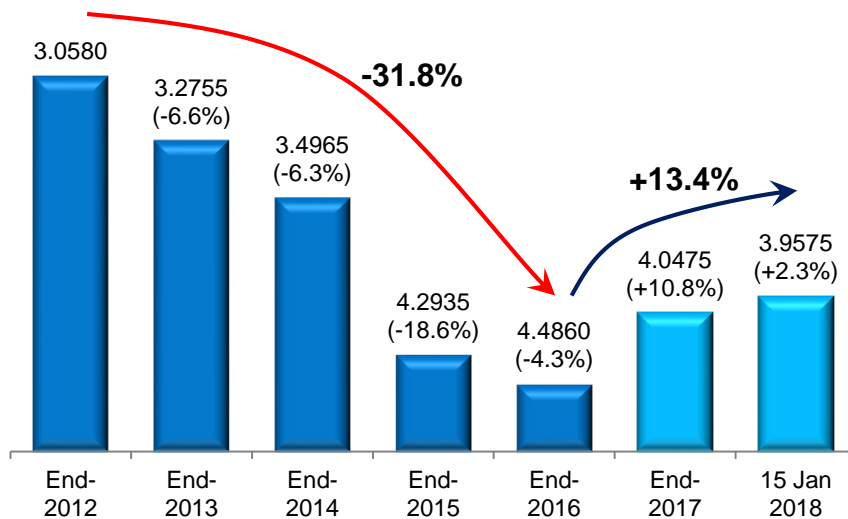


<sup>1</sup> Estimated  
Source: Bank Negara Malaysia

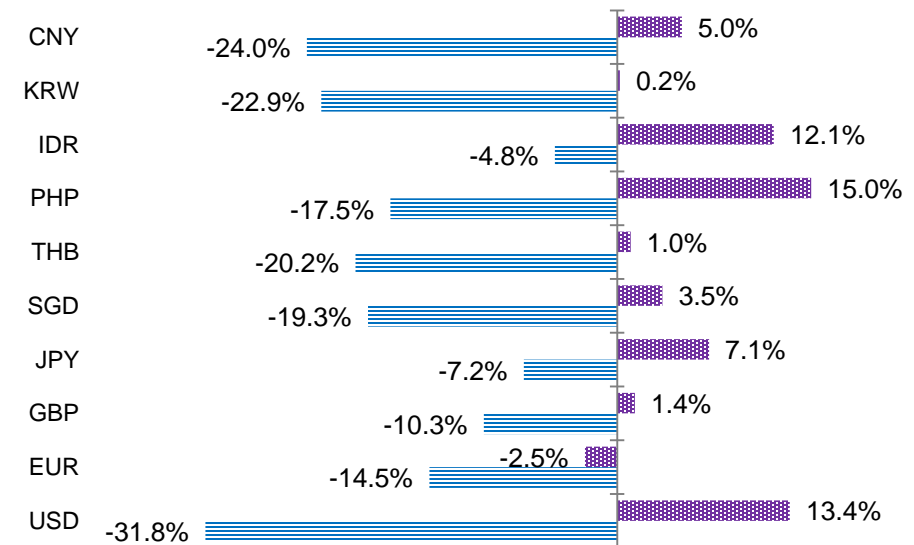
# The ringgit does not reflect its **FUNDAMENTAL** value

- **POSITIVE FUNDAMENTALS:** Brightening economic growth prospects, firming commodity prices, the onshore ringgit stabilization measures, prospect of domestic interest rate normalization, continued current account surplus, accumulation of foreign reserves.
- **COUNTERACT DAMPENING FACTORS:** Strong US dollar, higher US interest rates and yields, flows into the US dollar assets, geopolitical risks and developments in global financial markets.
- End-2018F: RM3.80-3.90/US\$1

## Ringgit movement against USD



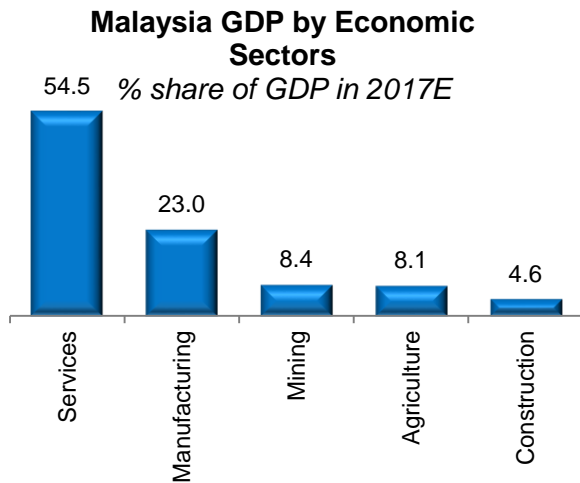
## Ringgit performance



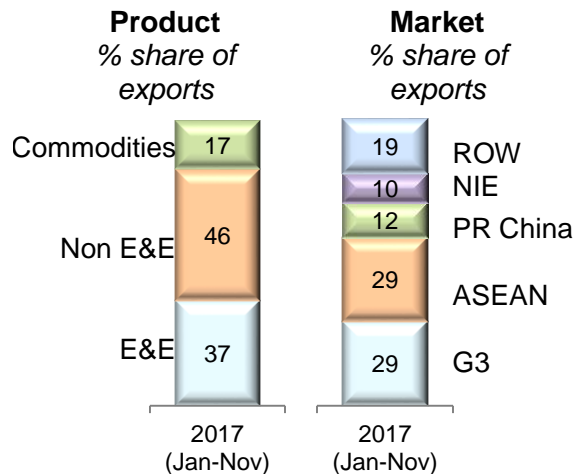
Source: Bank Negara Malaysia

# Macroeconomic FUNDAMENTALS supportive of growth

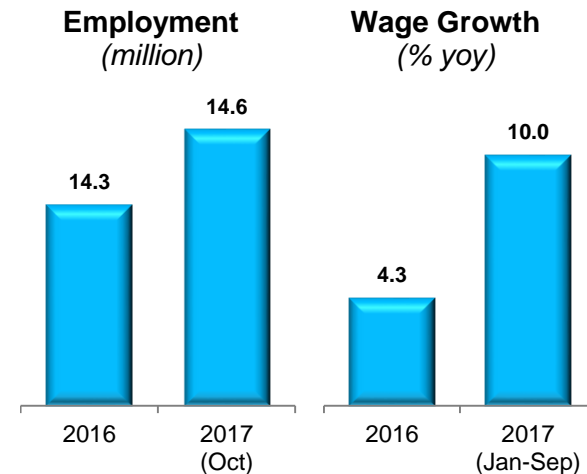
## Diversified sources of growth



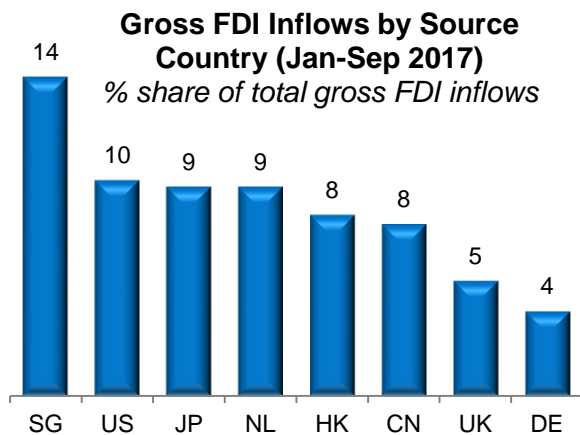
## Diversified export markets and products



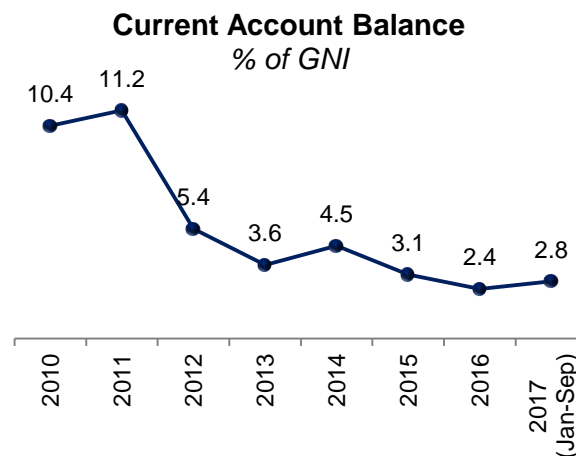
## Stable labour market conditions



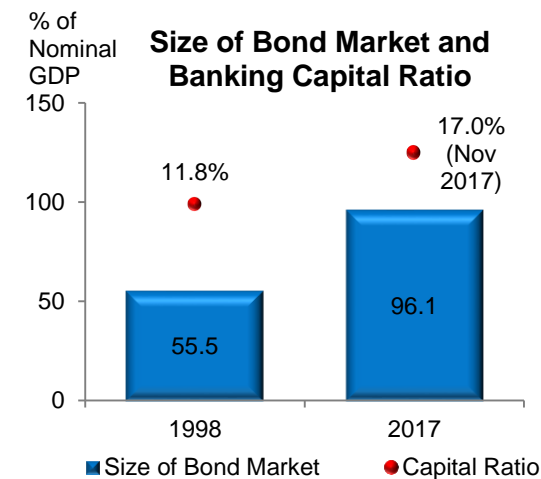
## Conducive investment destination for foreign investors



## Current account balance reflects strong investment



## Deeper markets and strong financial buffers

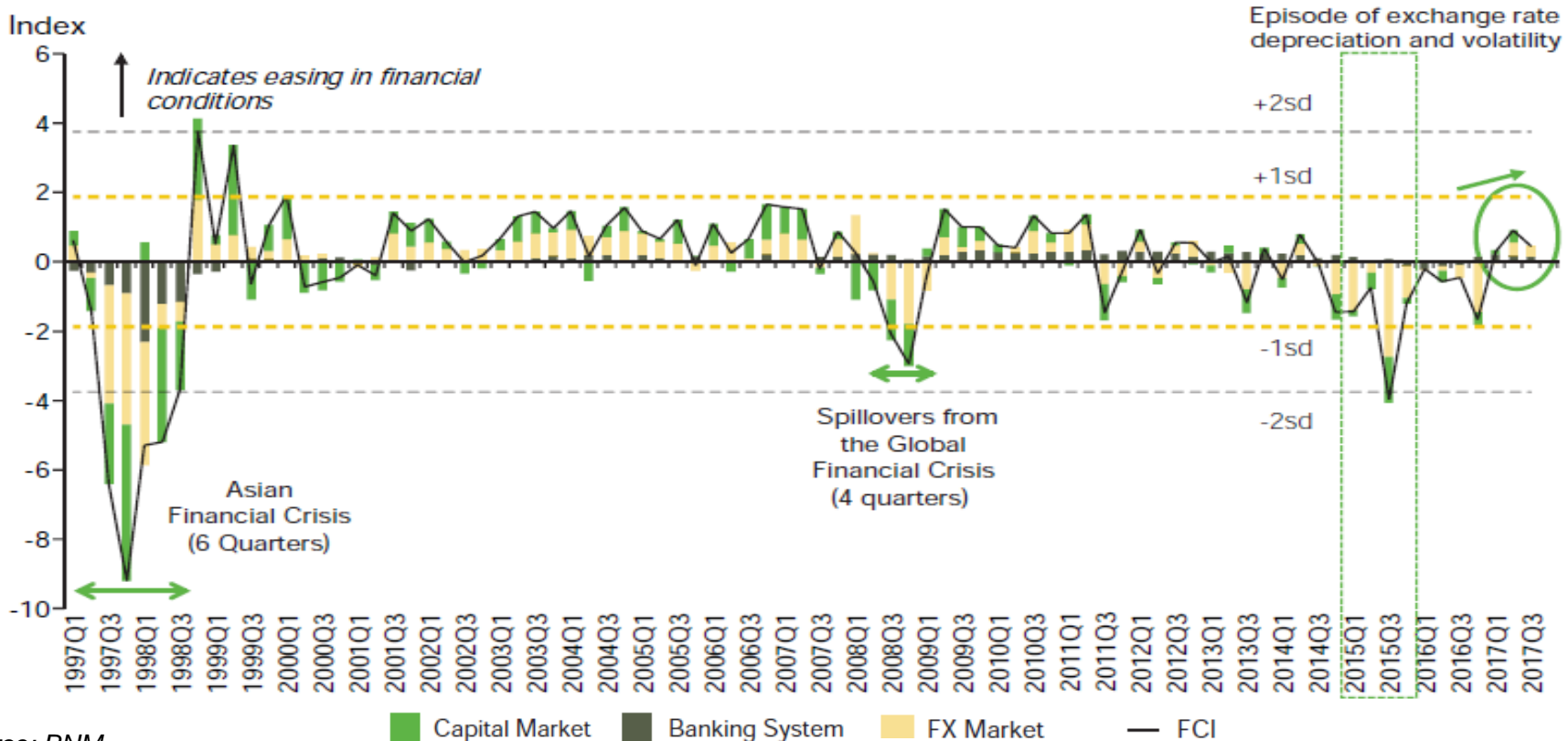


Source: MOF; DOS, Malaysia; BNM (MHS Nov 2017; AR2016) Notes: Numbers may not add up due to rounding and exclusion of import duties.

# FCI indicates IMPROVING financial conditions since 2016

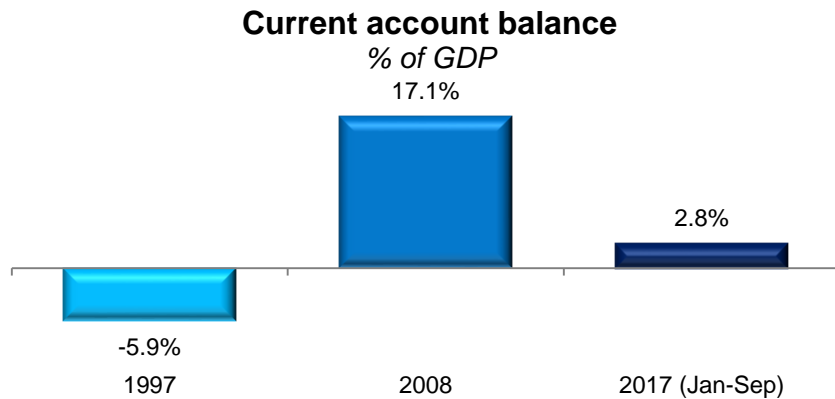
- Decreased **VOLATILITY** in the foreign exchange and equity markets.

Financial Conditions Index for Malaysia  
(Bars represent the variance decomposition of the index by markets)

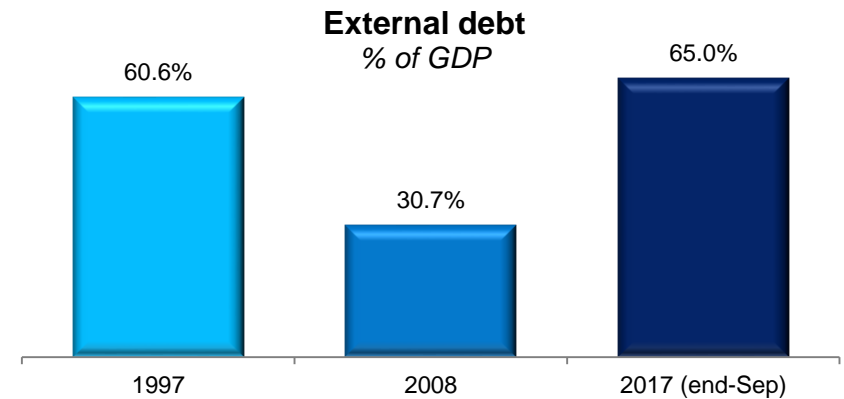


# Malaysia's SUSTAINABILITY heatmap

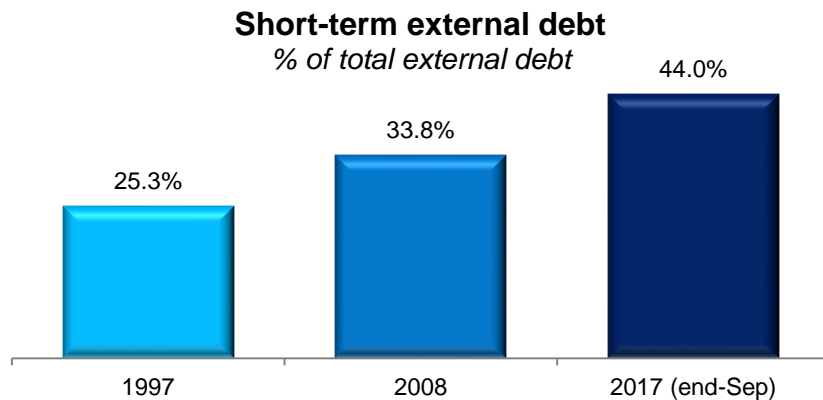
## Shrinking current account surplus



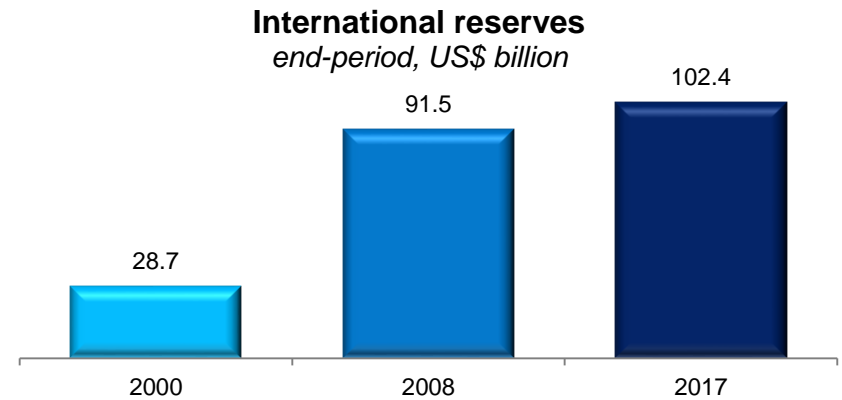
## Higher external debt (reclassification & exchange rate revaluation)



## Rising short-term external debt



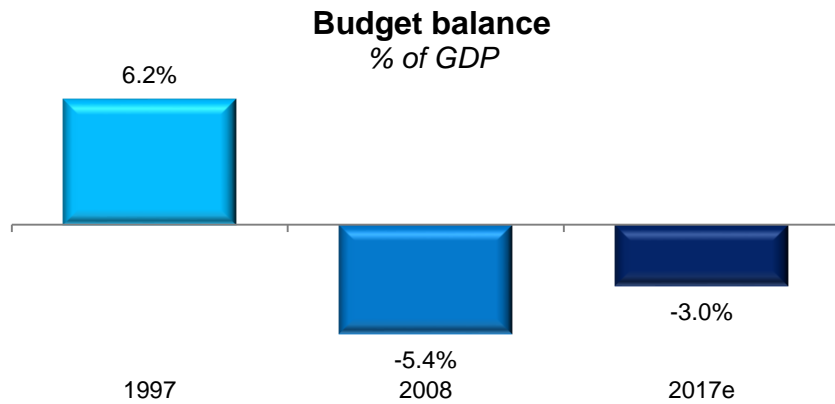
## Reserves adequacy (7.2 months of retained imports; 1.1 times short-term external debt)



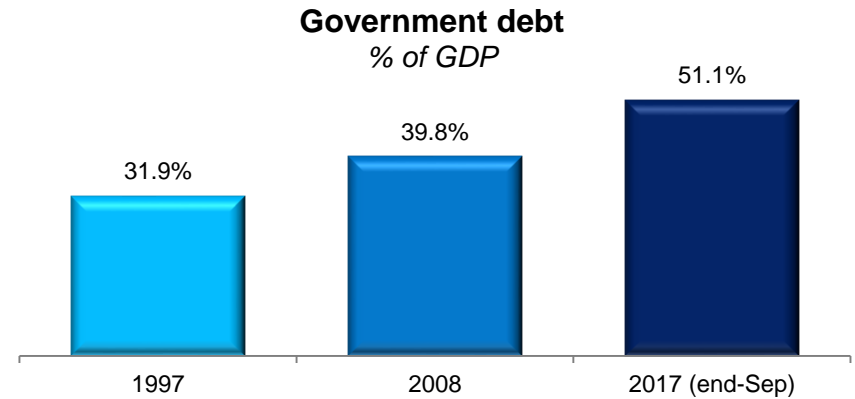
Source: BNM; CIMB Research

# Malaysia's SUSTAINABILITY heatmap

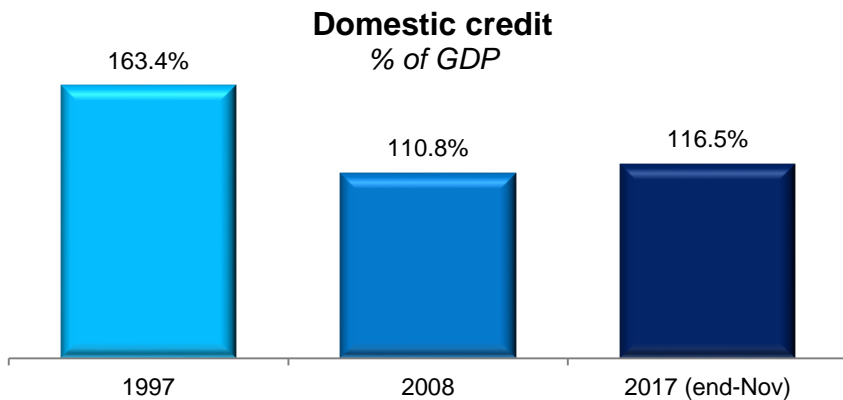
Fiscal consolidation remains on track



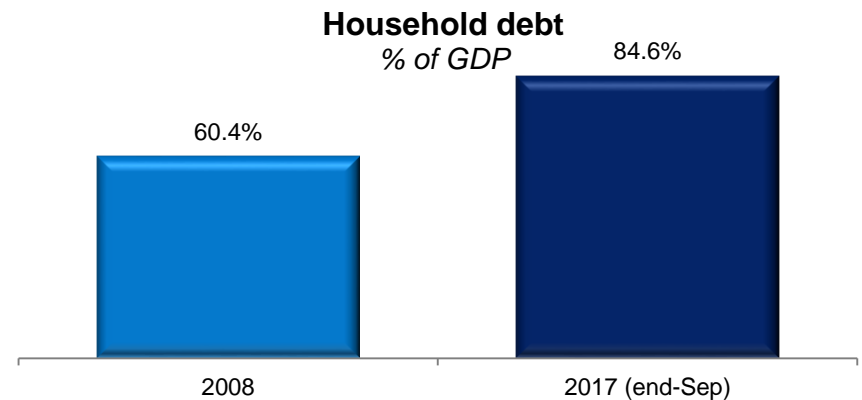
Government debt is contained below the self-imposed target of 55% of GDP



High domestic credit vulnerable to economic shock



Household debt ratio remains high amid moderate household credit



Source: BNM; CIMB Research



# Managing inflation and cost pressures

- The establishment of the National Cost of Living Action Council to address issues involving **COST OF LIVING** is a welcome development.
- The focus areas are housing, transportation, utilities as well as on food and beverages. A closer examination of the whole supply chains and distribution channels along which products travel from producers and manufacturers to track how the process flows in terms price structure, cost and ultimately the supply and demand dynamics.
- Businesses, especially small and medium-sized enterprises, whose have been coping with **HIGH COST OF DOING BUSINESS** carried forward over the last few years, would brace themselves for new wave of business cost in 2018 and 2019.
- These include the implementation of the **Employer Mandatory Commitment (EMC)**, which was postponed for implementation in 2017 (Under the EMC, the employers would be **disallowed from deducting the levy** from the wages of their workers); the **Employment Insurance System (EIS)**; **higher gas prices**; probable **review of new minimum wage** in 2018 and **new foreign workers' levy structure** in 2019.
- High operating and new regulatory costs eat into profit margins of businesses amid still challenging economic and business environments coupled with rising competition.
- Businesses must focus in operating efficiency efforts to mitigate rising input costs in order to gain extra savings. Large businesses are in better position to buffer themselves from the impact of inflation and increased operating costs compared to small businesses.

# Strengthening the **QUALITATIVE** sources of growth



## Sustaining **QUALITY** investment

- Unfavourable corporate tax rate
- Improve ease of doing business and business regulations
- Increased Total Factor Productivity (TFP) and capita intensity
- Contain overinvestment in property sector



## **DIGITALISATION**, labour skills and productivity

- Building a connected ecosystem
- Digital technology investments on business operation and productivity
- Uneven distribution of technological change benefits
- Investing in workforce skills – anticipating future skills needs



## Uplift the potential of **SMEs**

- Facilitate SMEs in e-commerce via digitalization technology investment
- High value creation in manufacturing and services
- Manufacturing for the future requires reinventing through a strong pipeline of innovations in materials, ICT, automation of production processes, robotics and digitalisation to deliver goods and services



## Supportive **FISCAL, MONETARY** & financial policies

- Setting right fiscal priorities
- Structural reforms
- Prioritize social and economic expenditure and transfer to foster a balance and inclusive growth
- Prudent monetary policy; safeguard financial stability; contain excessive leveraging



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**谢谢**  
**THANK YOU**

**Address** : 6<sup>th</sup> Floor, Wisma Chinese Chamber,  
258, Jalan Ampang, 50450 Kuala Lumpur, Malaysia.  
**Tel** : 603 - 4260 3116 / 3119  
**Fax** : 603 - 4260 3118  
**Email** : [serc@accimserc.com](mailto:serc@accimserc.com)  
**Website** : <http://www.accimserc.com>