



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

**JP Morgan's KL Seminar**

**The Malaysian Economy –  
Glass Half Full or Half Empty?**

**Lee Heng Guie**  
**Executive Director, SERC**

**11 March 2019**

# Key Messages



**A SYNCHRONISED GLOBAL SLOWDOWN**



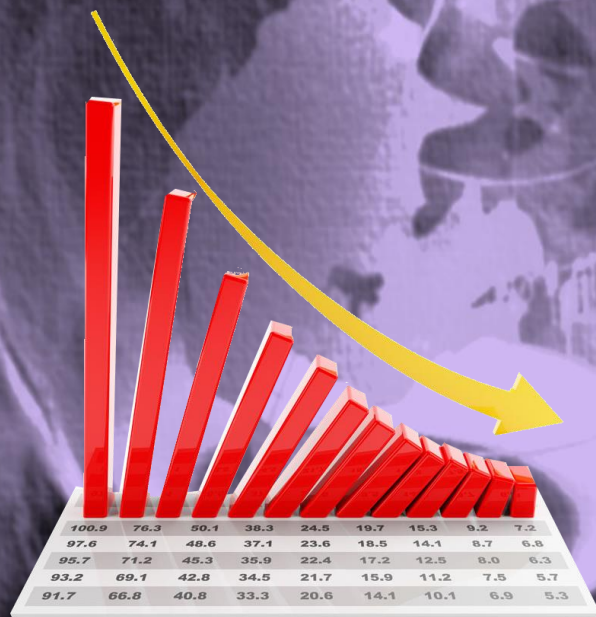
**A TUMULTUOUS YEAR FOR THE MALAYSIAN ECONOMY IN 2019**



**IMPLEMENT STRUCTURAL REFORMS TO POWER ECONOMIC GROWTH**

# Section 1

## The World Economy – *A synchronized slowdown*

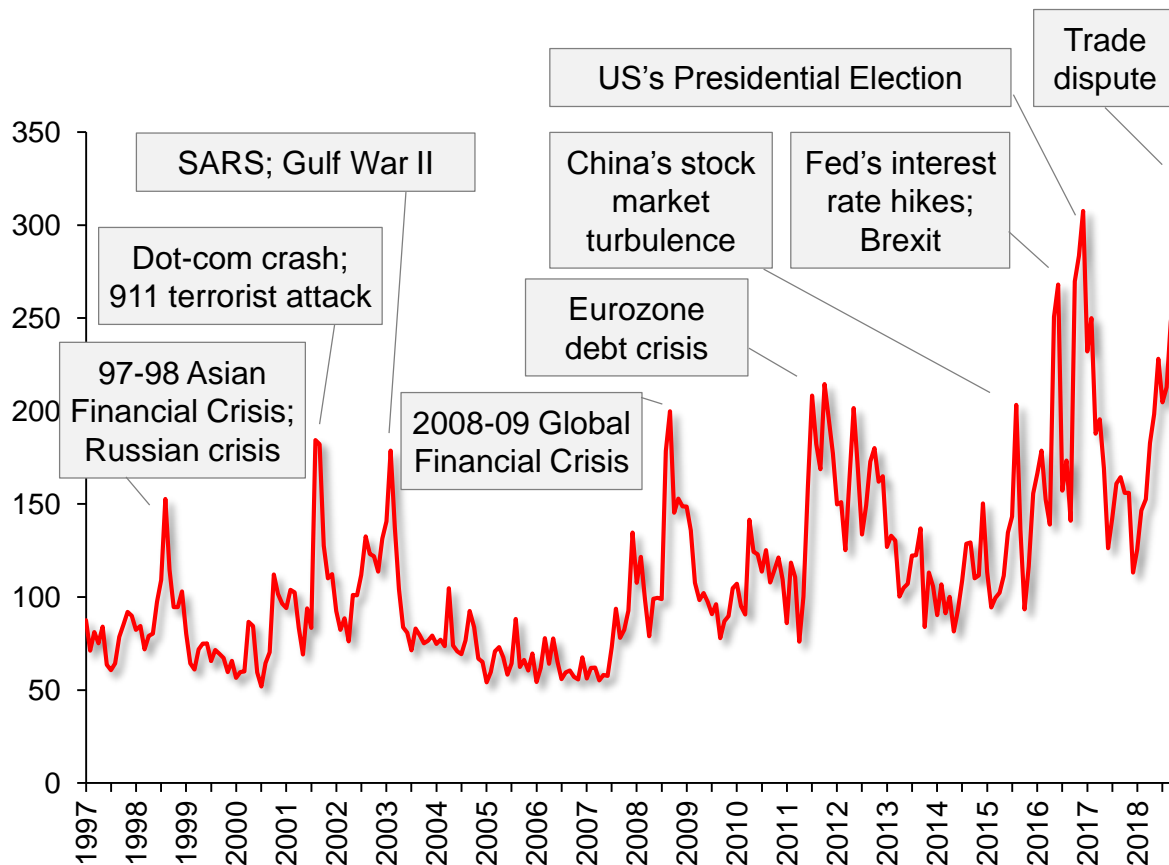


# Heightened UNCERTAINTIES weighing on global growth

**Uncertainties** in the global economy have soared to their highest level in Nov 2018.

- Lingering concerns and uncertainty about the **trade tensions**
- Uncertainty about the **Fed's future rate hikes**
- Concerns about **slowing global growth, the US and China economy**
- Induced **volatility in global financial markets**, including exchange rates in emerging markets
- Wide swings in **crude oil prices**
- **Geopolitical and political risks**

**Monthly Global Economic Policy Uncertainty Index**



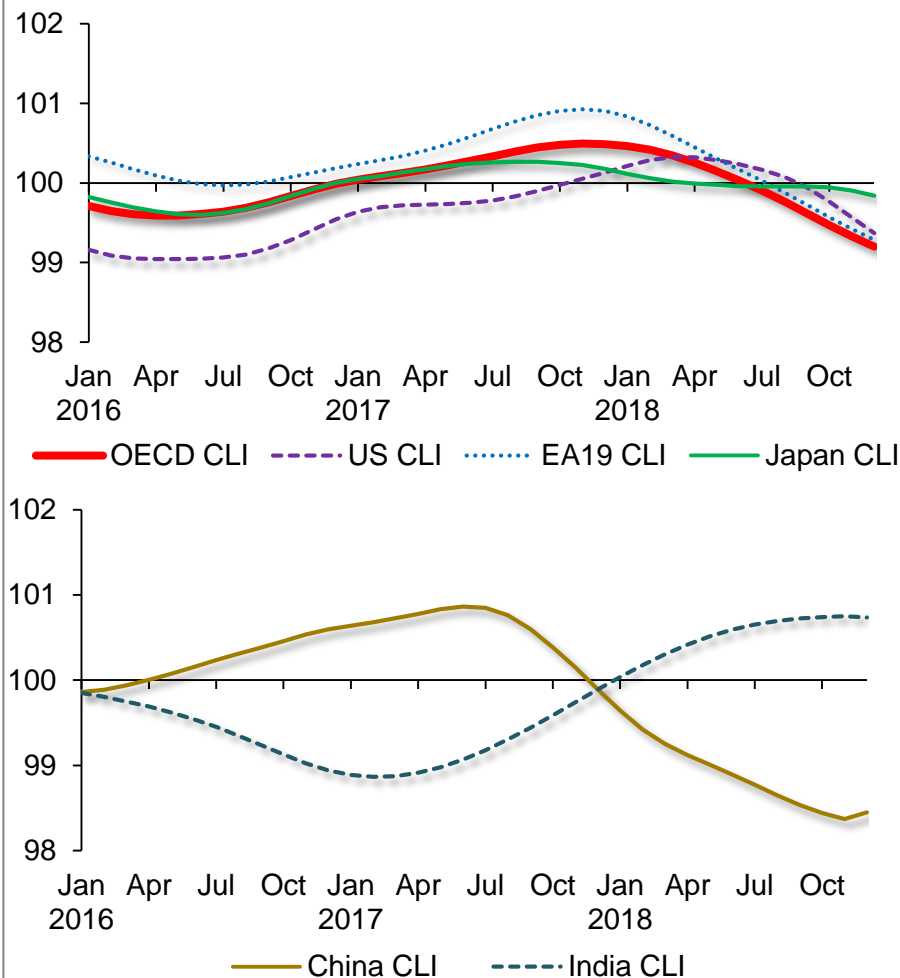
Source: *Economic Policy Uncertainty*



# Global indicators show growth PEAKING and is moderating

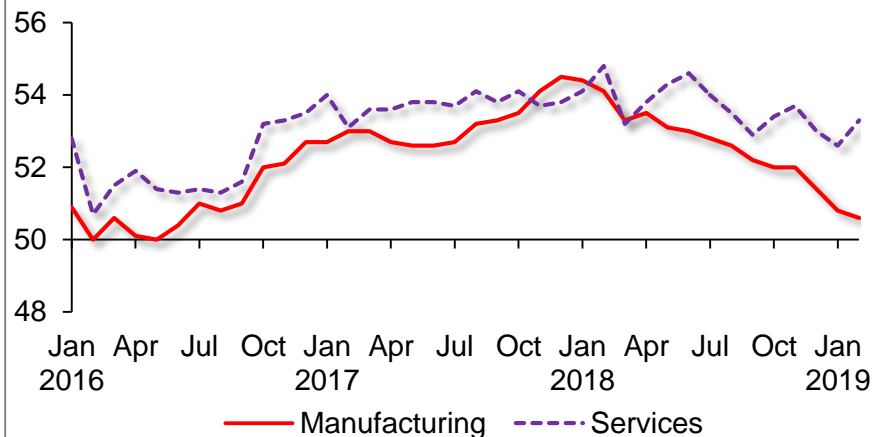
## Composite Leading Index – a gauge of forward economic outlook

Long-term average = 100



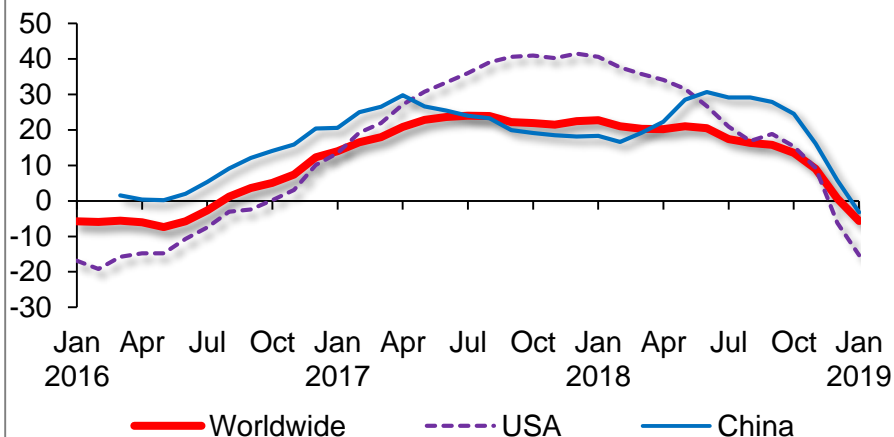
## Global PMI for manufacturing and services

50 = no change on prior month



## Global semiconductor sales

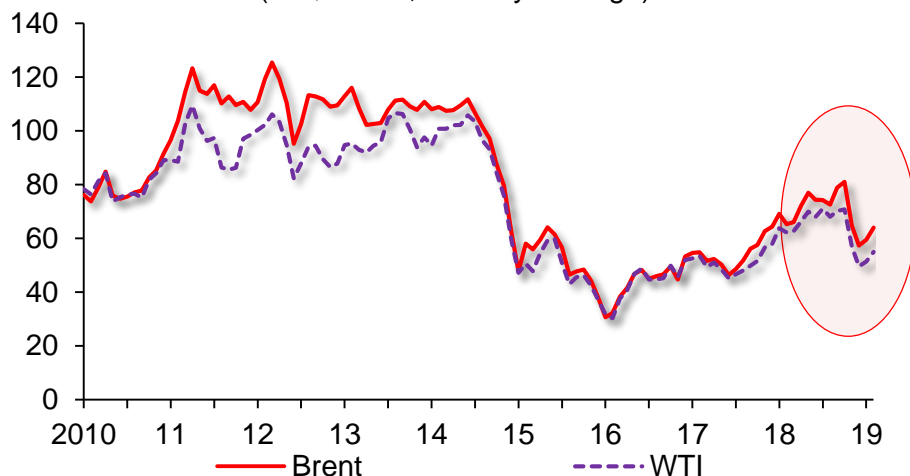
%, 3-month moving average YoY



Source: OECD; Markit; SIA

# COMMODITIES are flagging a WEAKER global economy

**Crude oil prices**  
(US\$/barrel, monthly average)



**Crude palm oil prices**  
(RM/metric tonne, monthly average)



Source: EIA; MPOB

- **Crude oil prices:**

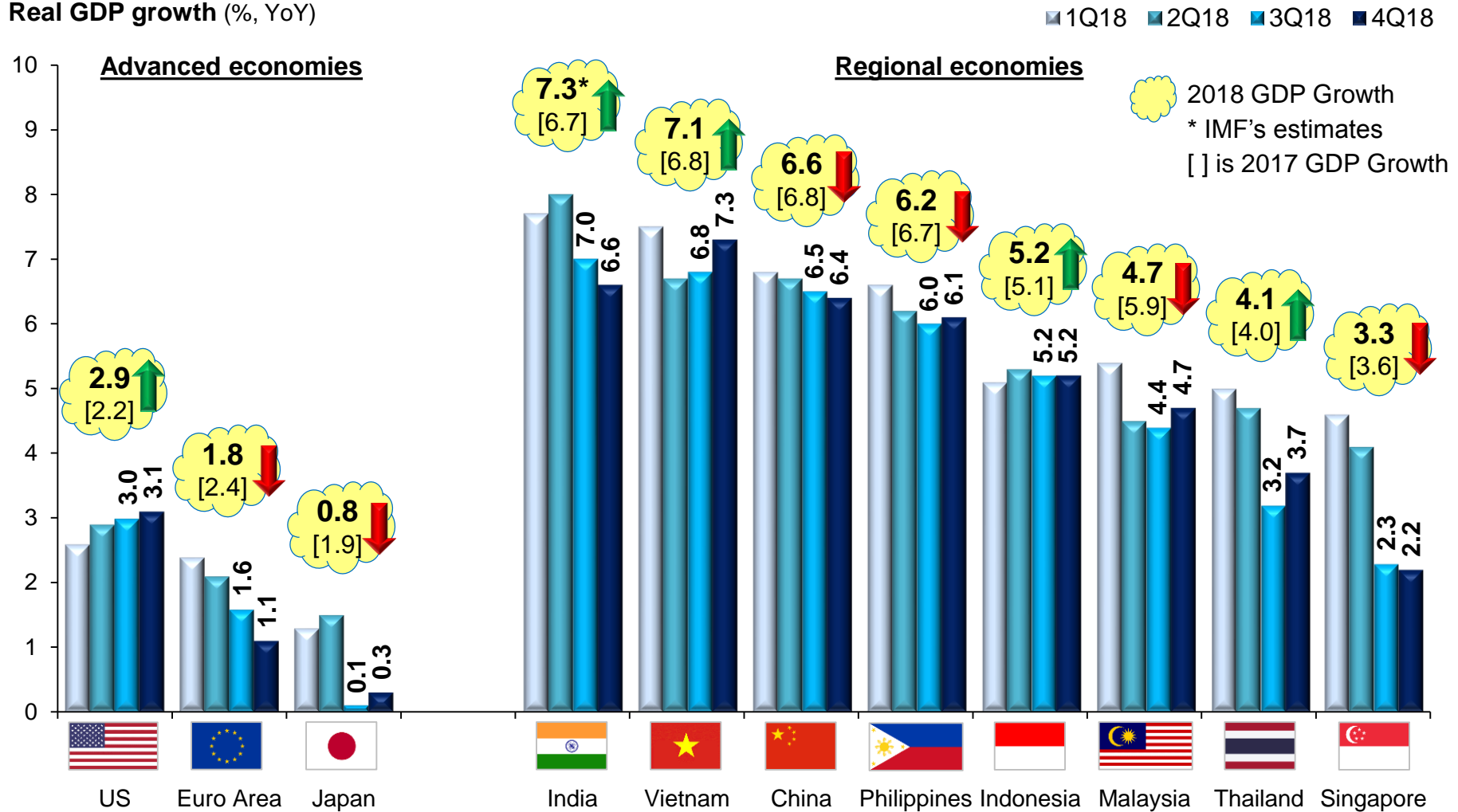
- ❑ Surpassed US\$80/barrel in end-Sep 2018 but dropped dramatically after then (US\$51/bbl as at end-2018).
- ❑ **Downside risks:** Trade tensions, slower global economic growth, higher OPEC output, stronger than expected Canadian and US production.

- **CPO prices:**

- ❑ High palm oil inventory in Malaysia and Indonesia. Stocks are piling up in May-Dec 2018.
- ❑ Soybean planting in South America.
- ❑ Proposed ban on the utilization of palm oil as biodiesel in Europe starting 2021.
- ❑ Short-term catalysts: (a) India lowered the duty on crude palm oil to 40% from 44% while a tax on the refined variety was cut to 50% from 54%. Malaysian shipments of refined palm oil will be taxed lower at 45% compared with 54%; (b) Higher purchase of palm oil (1.62 million tonnes) from China.

# Uneven EXPANSION in advanced and regional economies...

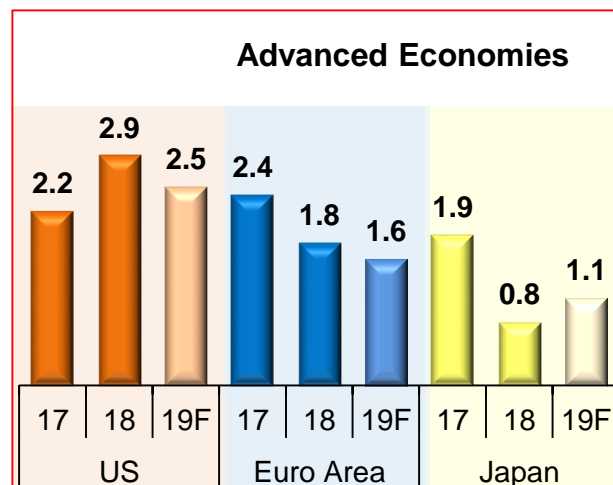
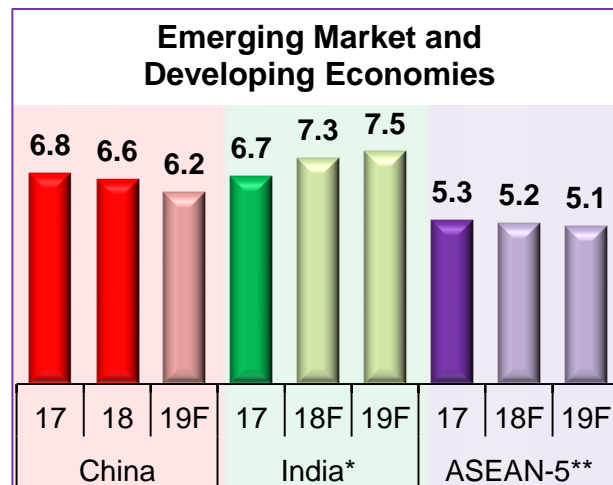
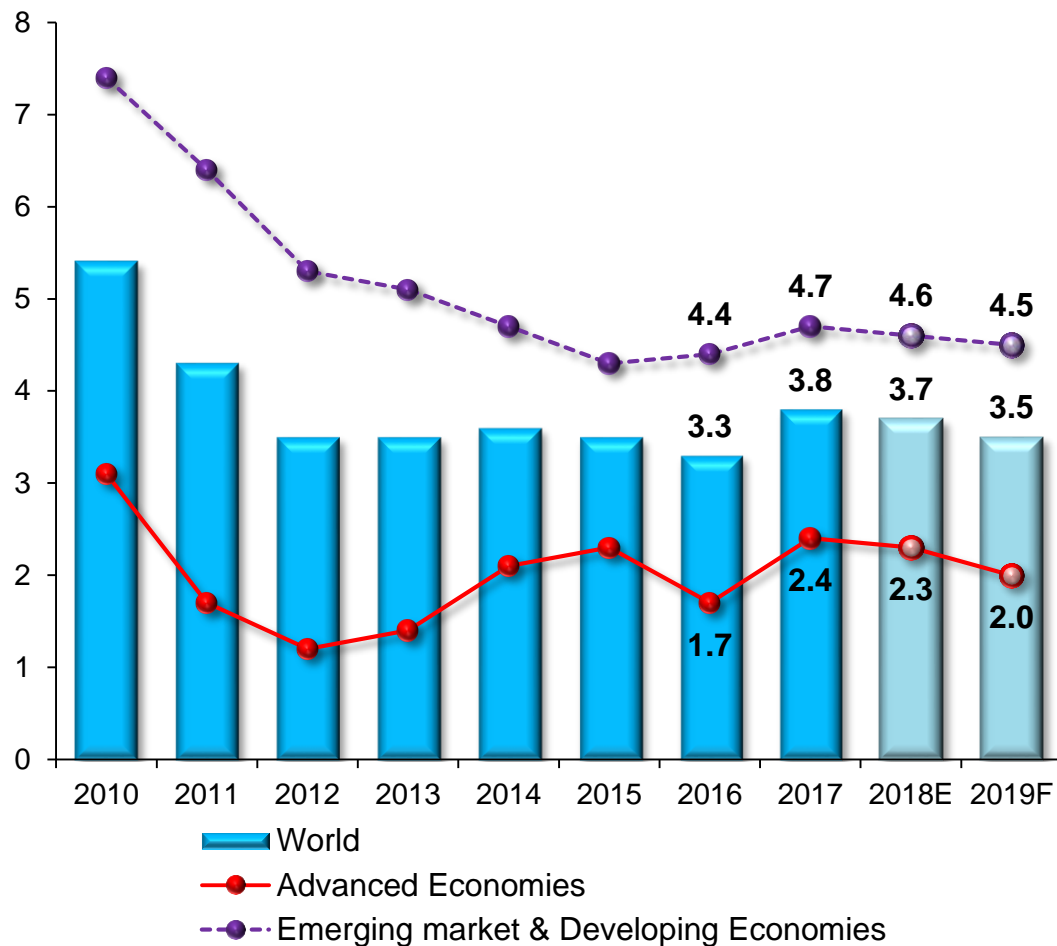
Real GDP growth (% , YoY)



Source: Officials (unadjusted data except Euro Area); IMF

# GROWTH prospects for advanced and emerging economies

Real GDP Growth (%)



Source: Officials; IMF

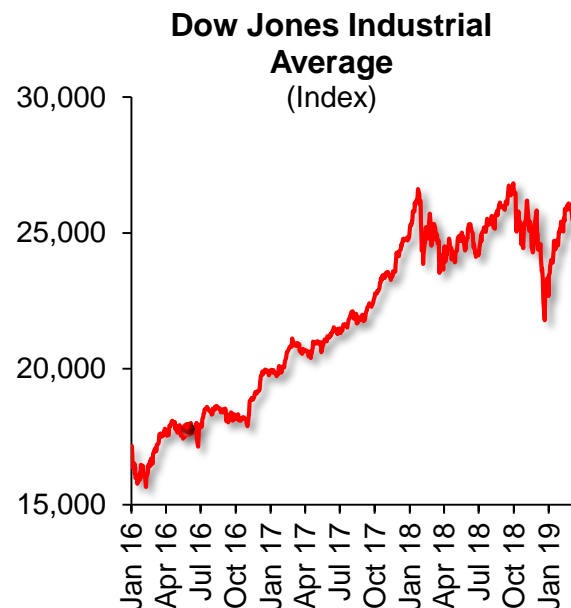
\* Annual GDP for India is on fiscal year basis

\*\* ASEAN-5: Malaysia, Indonesia, Philippines, Thailand, Vietnam

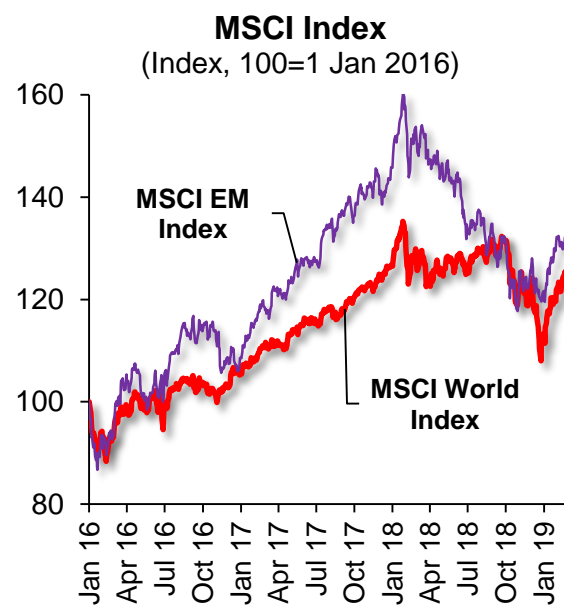


# Global equity markets VOLATILITY

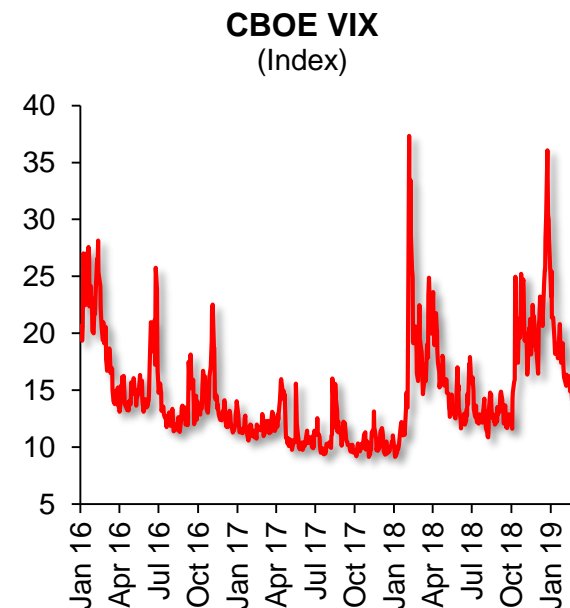
**A correction in DJIA after hitting record highs**



**2018 was a bad year for emerging markets' equities**



**Two sharp spikes (above 30-pts) in the 'Fear index' during 2018**



Source: WSJ; MSCI; CBOE



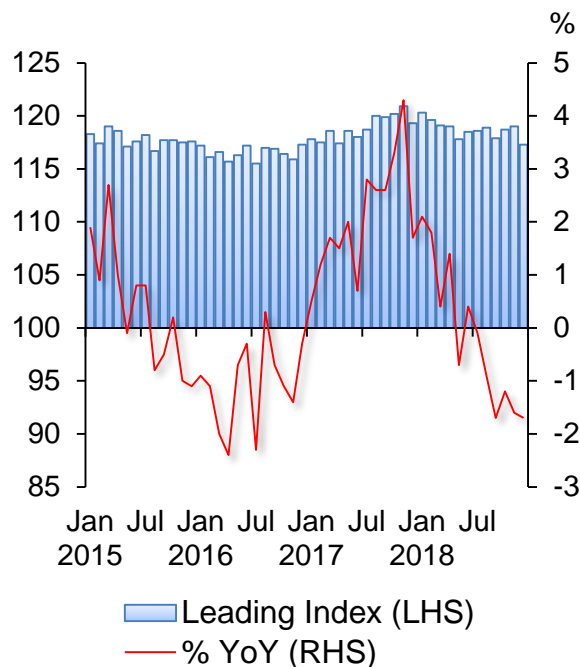


## Section 2

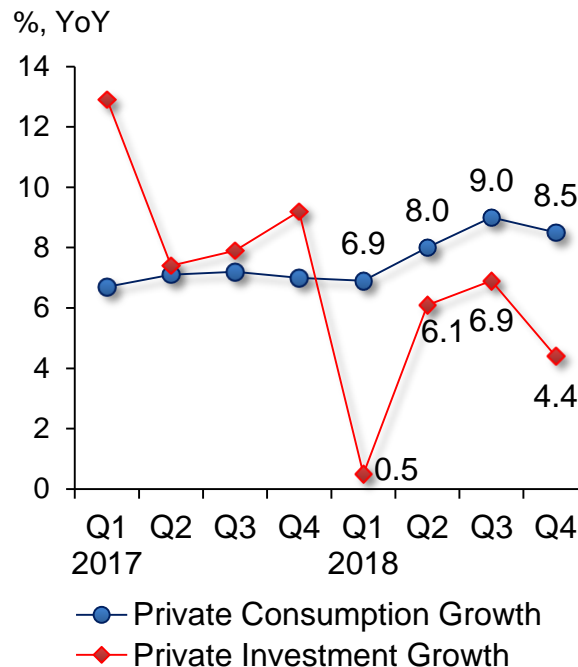
# The Malaysian Economy – *Where are we now?*

# GDP growth is LOSING MOMENTUM but still manageable

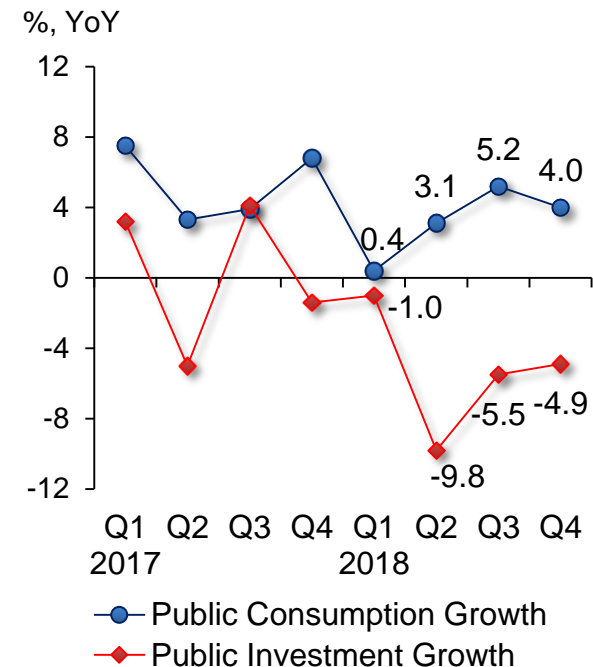
Leading index presages slower economic growth ahead



GDP growth by largely private spending underpinned



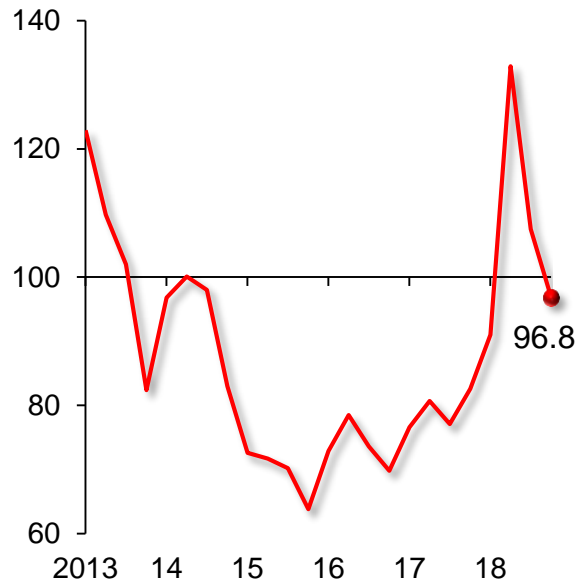
Public sector spending remains a drag



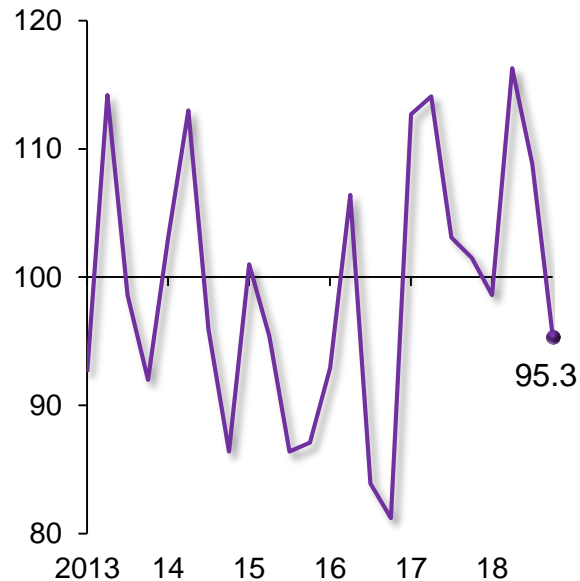
Source: DOSM

# Weakening CONSUMER SENTIMENT and BUSINESS CONFIDENCE

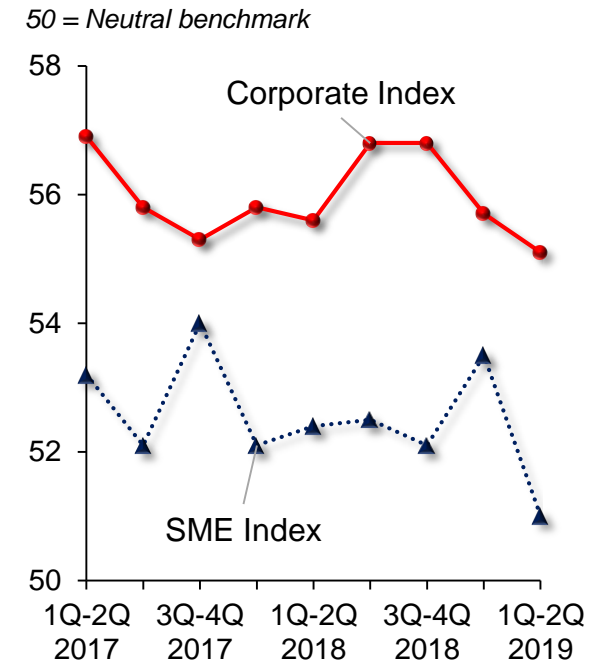
MIER's Consumer Sentiments Index (CSI)



MIER's Business Conditions Index (BCI)



RAM Business Confidence Index



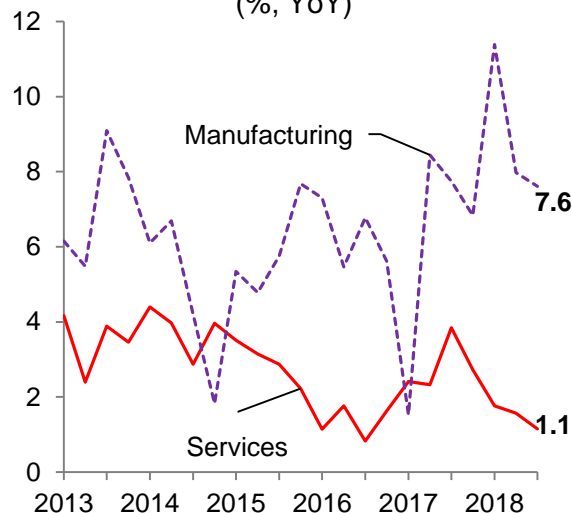
Source: MIER; RAM



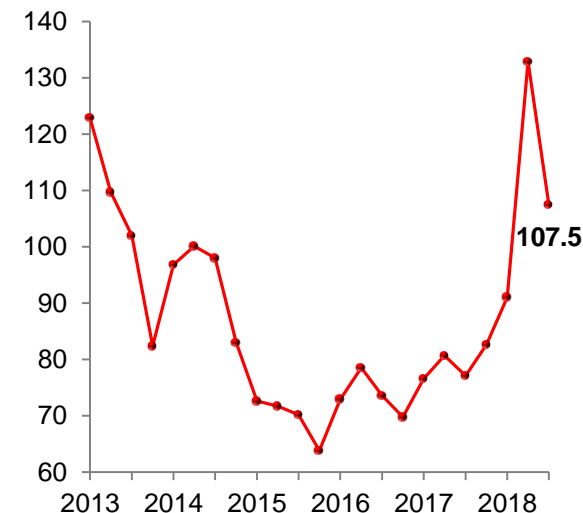
# SOLID consumer spending but will it normalise?

- **FUNDAMENTAL DRIVERS:** Income growth and labour market conditions
- Household spending will **NORMALIZE** post 3-month zeroed GST tax holiday and the introduction of **SST** on 1 Sep
- Potential **DAMPENING FACTORS:** Review of fuel subsidy and cost of living aid

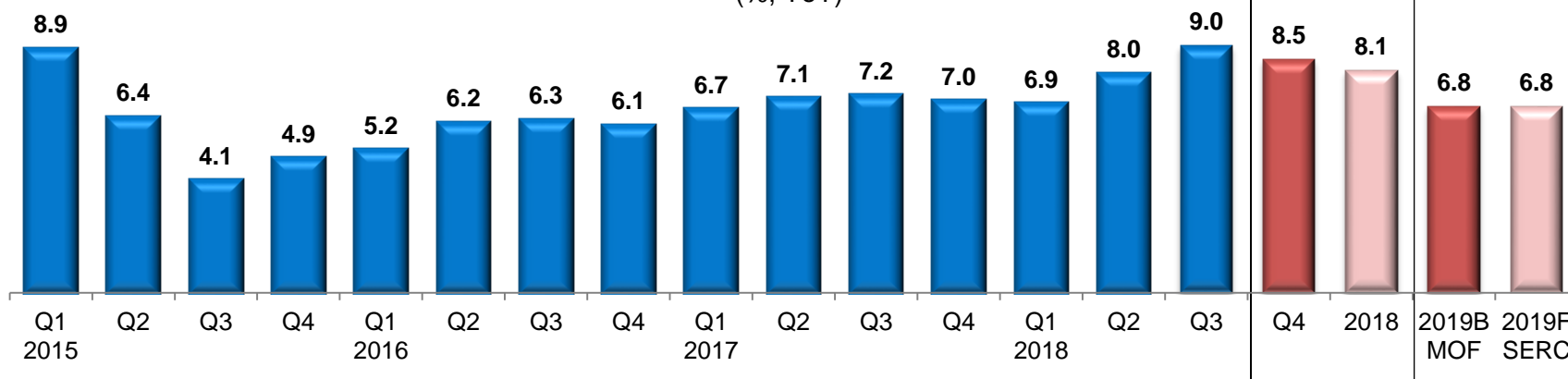
Private Sector's Employee Income  
(%, YoY)



MIER Consumer Sentiments Index (CSI)



Private Consumption Growth  
(%, YoY)



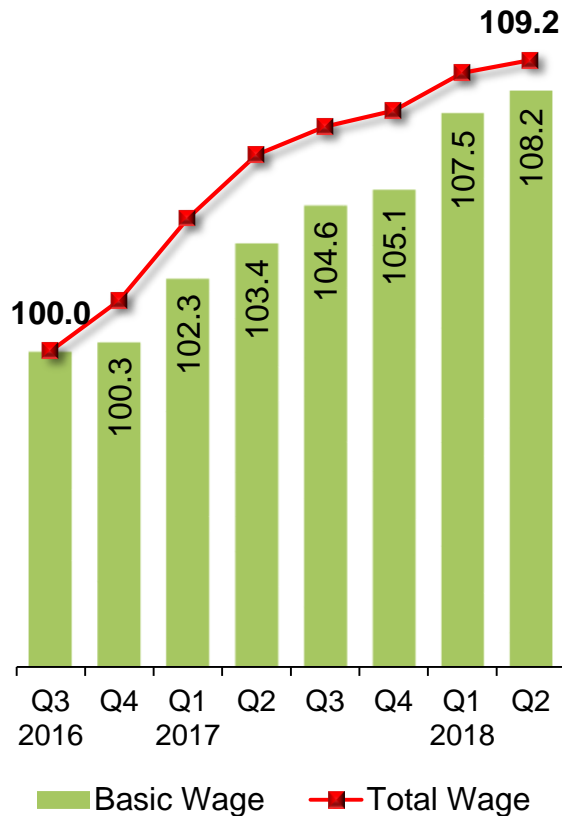
Source: Department of Statistics, Malaysia (DOSM); MIER



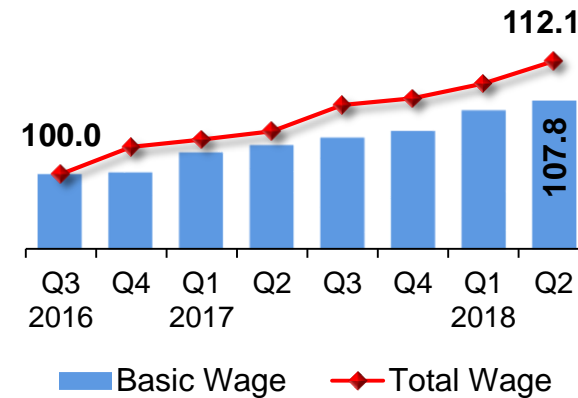
# Wages in MANUFACTURING & SERVICES sector increased, albeit less uniformly

- W.e.f. Jan 2019, minimum wage increased by 10.0% and 19.6% respectively to RM1,100 per month from RM1,000 in Peninsular Malaysia and RM920 in East Malaysia respectively.

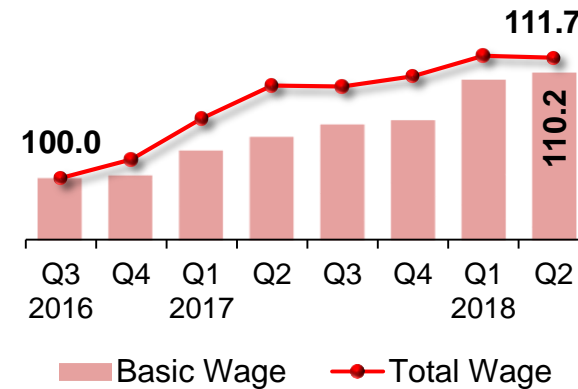
National Wage Index



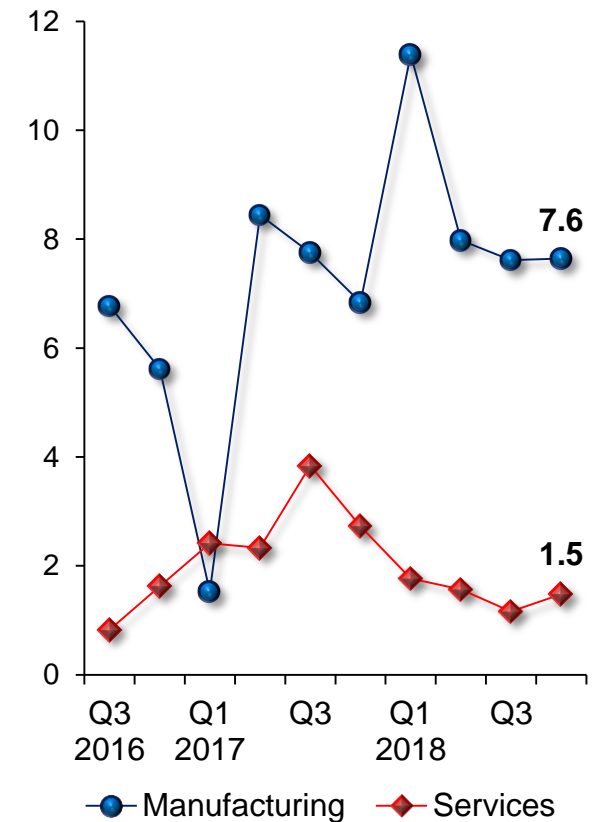
Manufacturing



Services



Average wage growth per employee

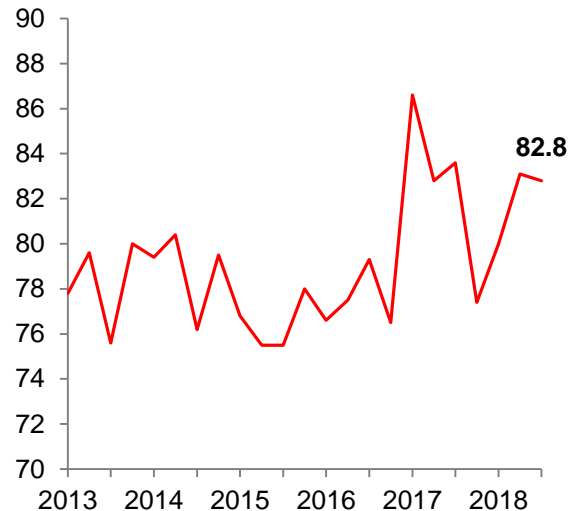


Source: ILMIA; DOSM

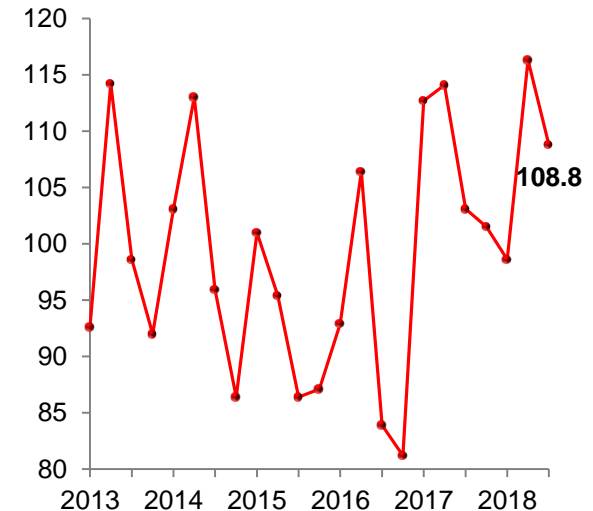
# Private investment growth ON TRACK but CAUTIOUS

- Private investment growth **SLOWED** to 4.4% yoy in 4Q (6.9% in 3Q18; 10.5% pa in 2011-17).
- CAUTIOUS** about external environment; new government's policy implications
- 2019 Budget to **BOOST** private investment in tourism, manufacturing, IR 4.0 and e-commerce

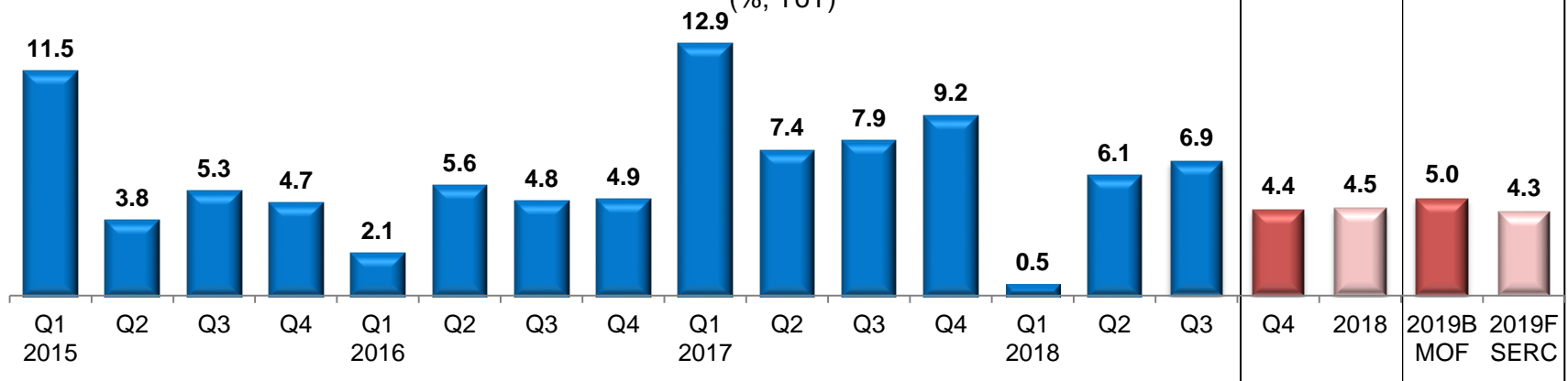
Capacity Utilisation Rate (%)



MIER Business Conditions Index (BCI)



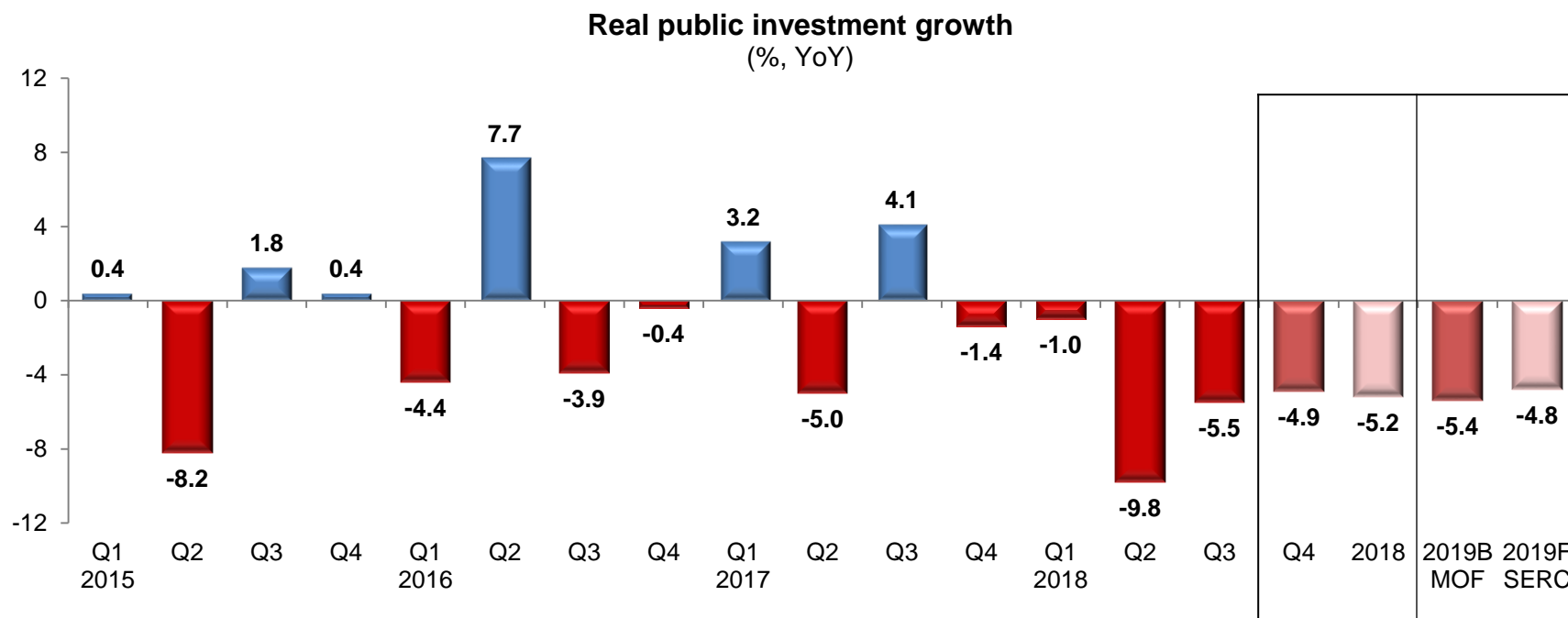
Private Investment Growth (% YoY)



Source: DOSM; MIER

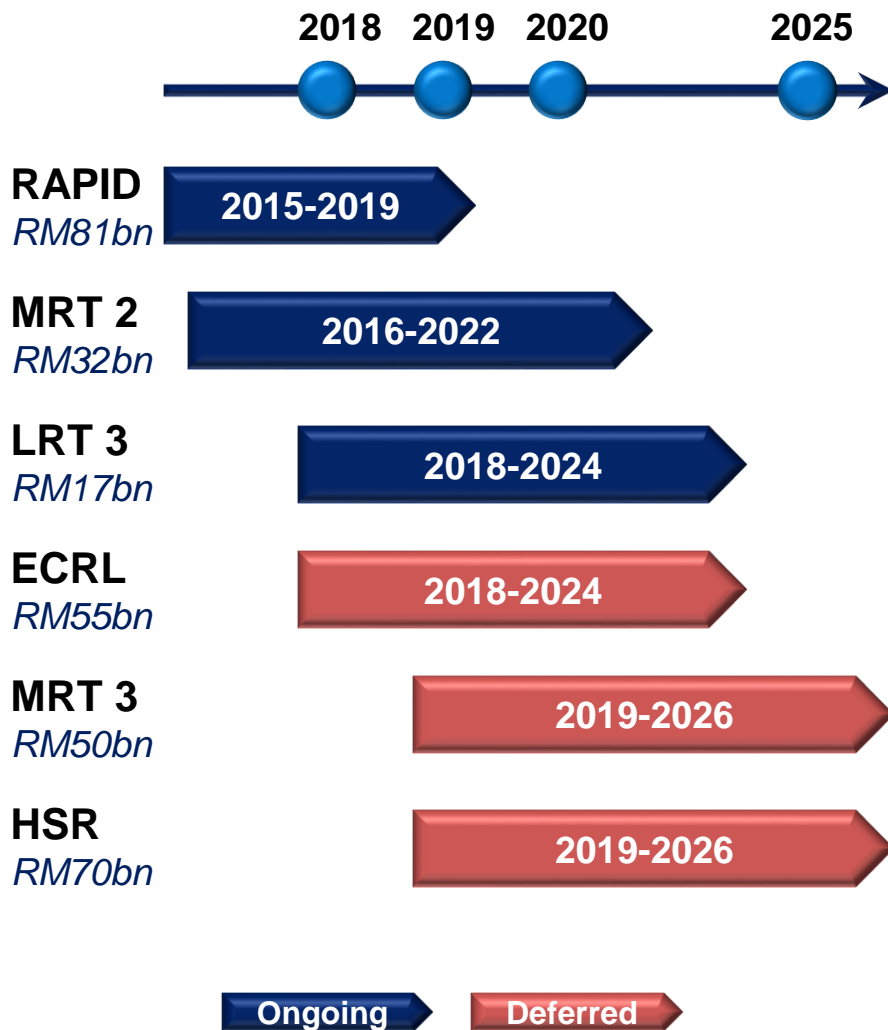
# Public investment remains **CLOUDED** ahead

- **PUBLIC INVESTMENT GROWTH CONTRACTED** for four straight quarters.
- Rationalisation of development expenditure means moderate public investment growth.
- Further consolidation of development expenditure in 2019.



Source: DOSM

# DEFERRED OR CANCELLED mega projects: manageable impact



On-going projects help mitigating the impact on growth:



In early stages of construction or have yet to commence



Spreading effects (contained impact in single year) due to long period of development

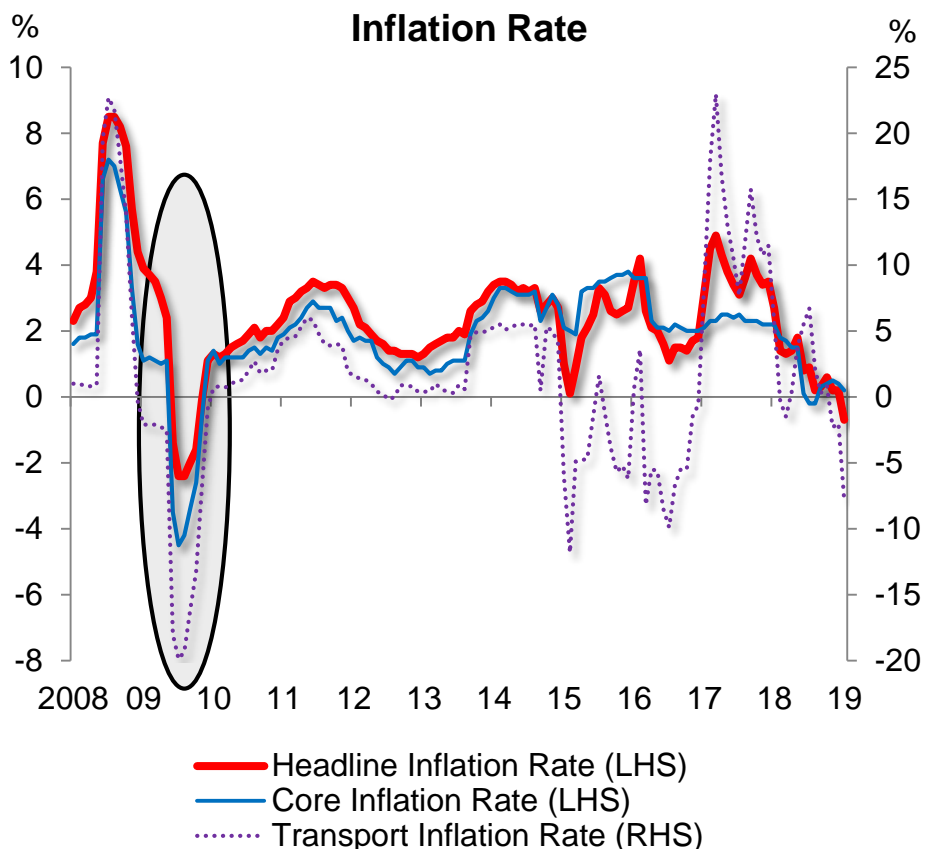


Depend on the localisation vs. imported of construction related materials and services



Manageable impact on domestic employment

# “Technical” base-induced DEFLATION is transitory



- First deflation (Jan 2019: -0.7% yoy) since end-2009. It is merely a technical deflation due to:
  - i. Decline in RON95 petrol price; and
  - ii. Change in consumption tax regime: Removal of GST and reintroduction of SST which SST covered 38% of the goods and services in CPI basket vis-à-vis 60% by GST.
- Excluding both effects, core inflation still stood healthy at 1.5% yoy in January 2019.
- Overall inflation rate will rise gradually in second half of the year and is expected to increase by 1.0-1.5% in 2019 (1.0% in 2018).

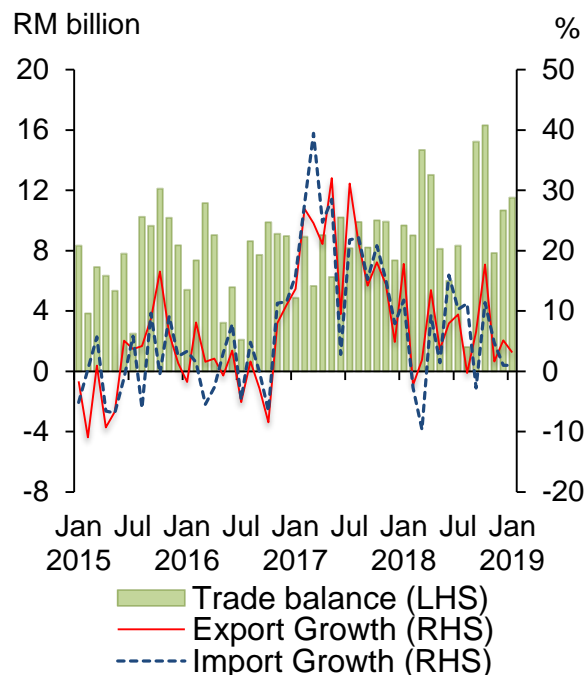
Source: BNM; DOSM

Note: Core inflation in 2008-2014 excludes food and non-alcoholic beverages only.

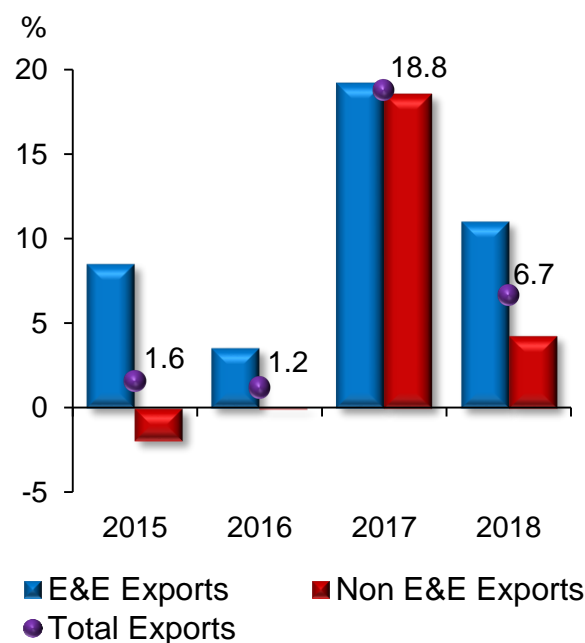


# EXPORT growth outlook remains challenging

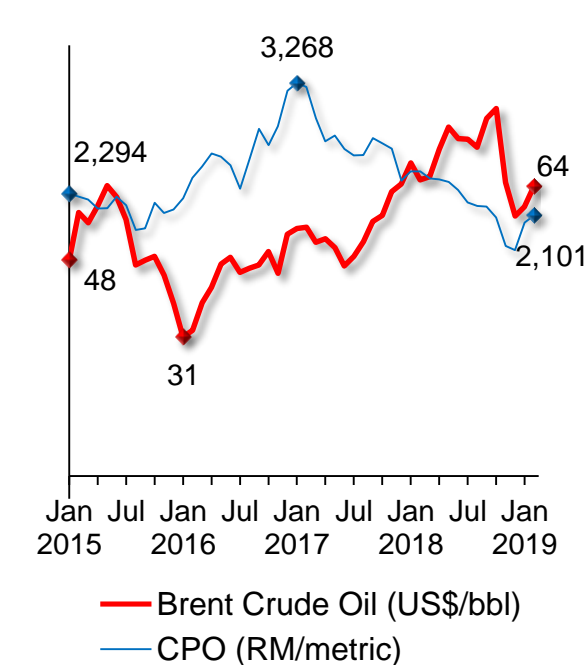
External trade balance remains in surplus



Exports of E&E is the major contributor

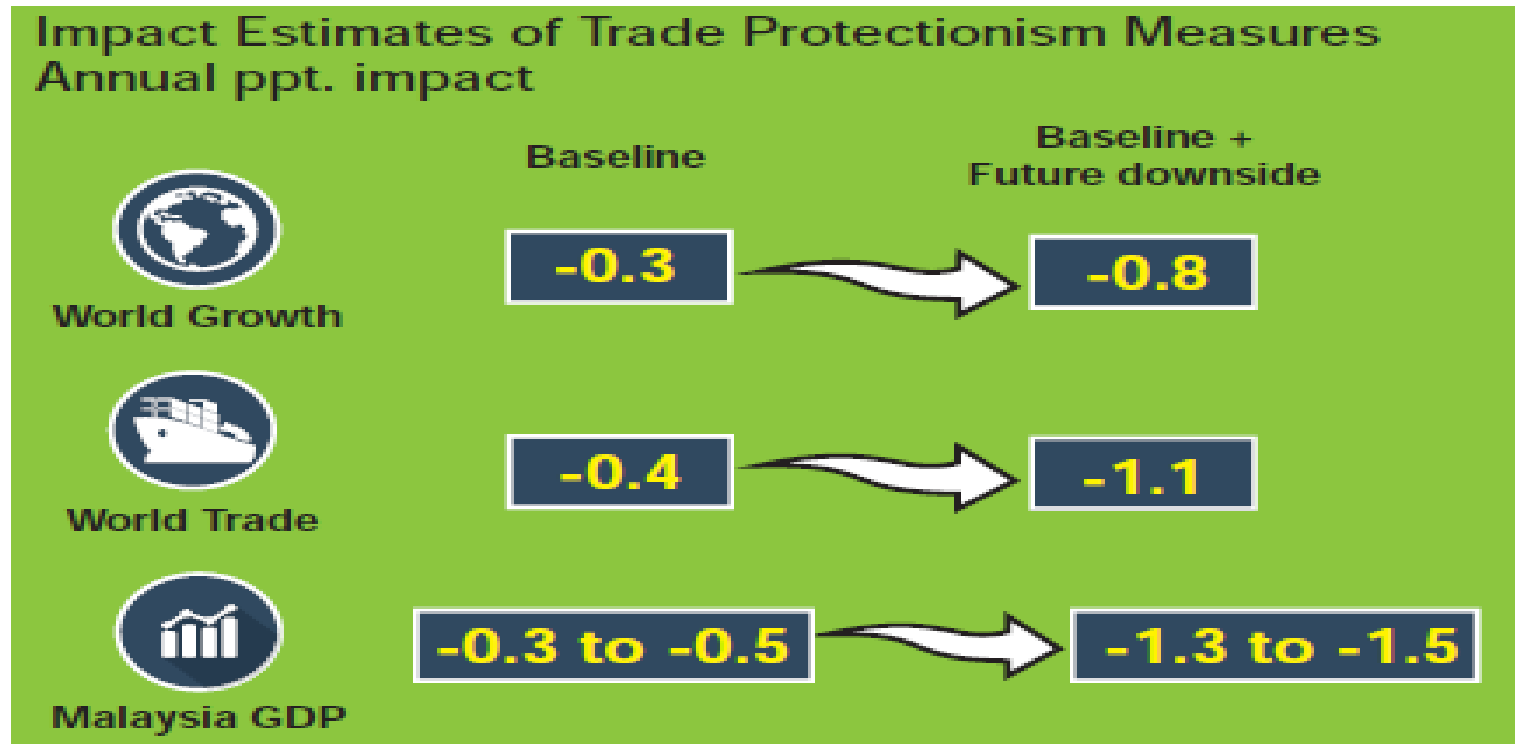


Facing headwinds from crude oil and palm oil prices



Source: DOSM; EIA; MPOB

# Further ESCALATION in trade tensions to have significant impact on GDP



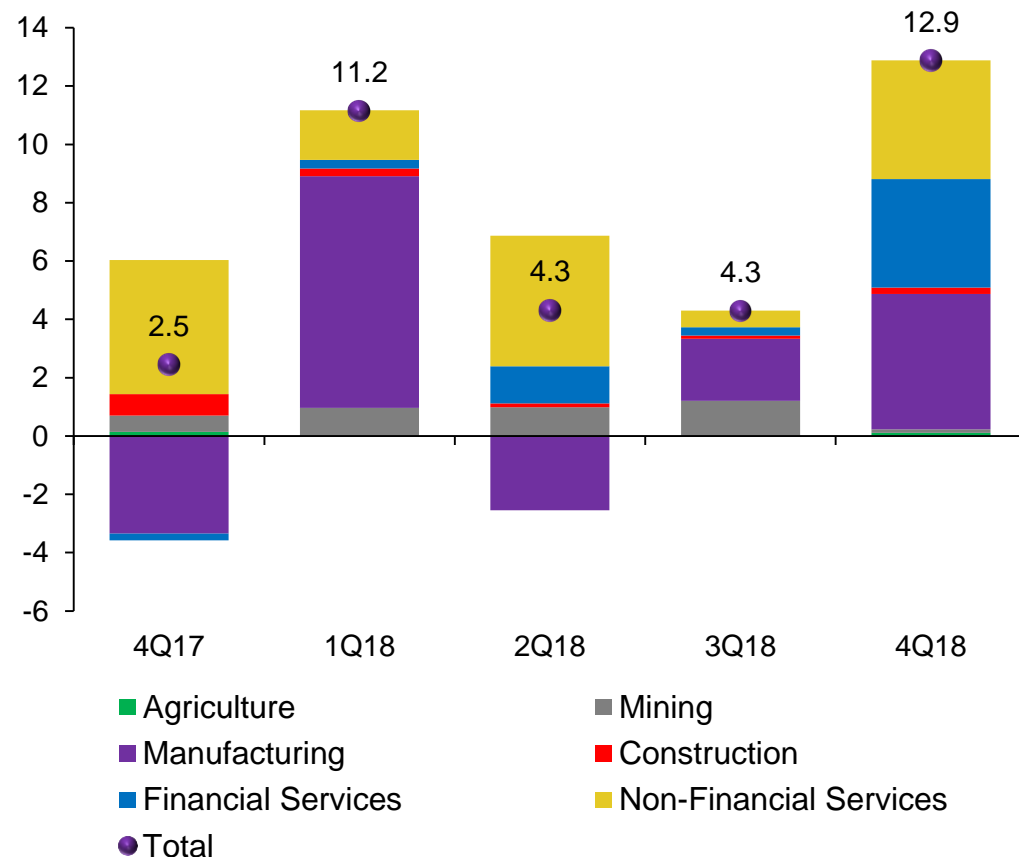
- Overall, the impact of bilateral trade tensions on Malaysia's export performance is largely dependent on the **substitutability of the affected products, manufacturing capacity constraints** and Malaysian firms' value proposition.

Source: Bank Negara Malaysia

# Higher broad-based FDI INFLOWS in 4Q2018

## Net Foreign Direct Investment in Malaysia

RM billion

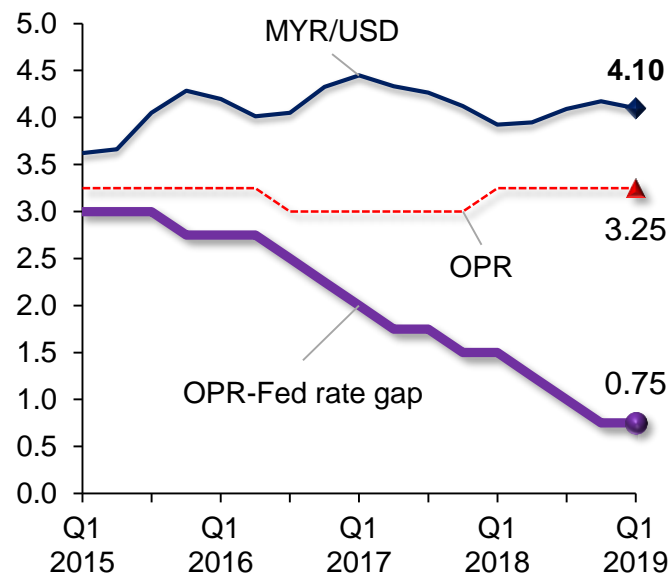


- Higher net FDI in 4Q18 (RM12.9bn vs. RM4.3bn in 3Q)
- FDI inflows were broad-based, mainly channelled into the manufacturing and non-financial services sectors.
- Advanced economies including the Netherlands, Japan and Hong Kong were the largest contributors of FDI.
- Total 29 China-participated projects worth RM15.6 billion approved in Jan-Sep 2018 (20 projects worth RM3.9bn in 2017).

Source: BNM

# MONETARY SPACE has some room but FISCAL LEVER is limited

Will the weak ringgit restrain monetary easing?



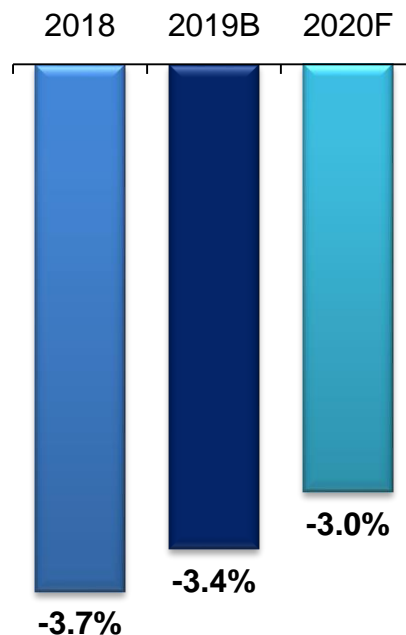
Note:

Q1 2019 refers to Jan-Feb 2019 only

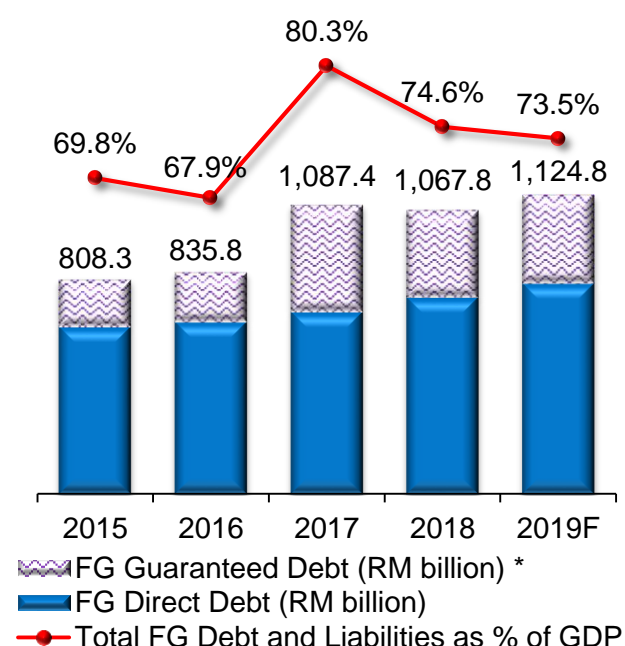
Exchange rate: Average of 12:00 rate

Rate gap: As at end-quarter

Reset fiscal deficit path (2018-2020F)



Federal Government (FG)'s debt and liabilities



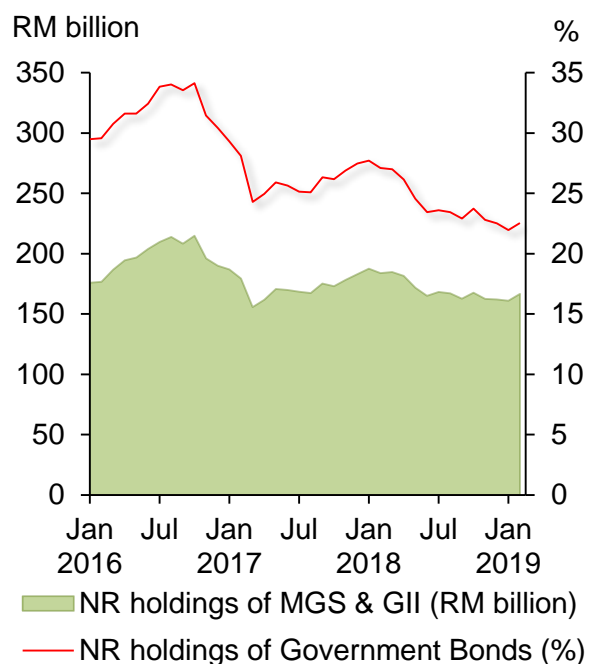
Year	2015	2016	2017	2018	2019
<b>FG Direct Debt</b>	630.5	648.5	686.8	741.0	792.7
% of GDP	54.4	52.7	50.7	51.8	51.8
<b>FG Guaranteed Debt *</b>	177.7	187.3	400.6	326.8	332.1
% of GDP	15.3	15.2	29.6	22.8	21.7

\* Includes liabilities from Public Private Partnership (PPP) for 2017-2019

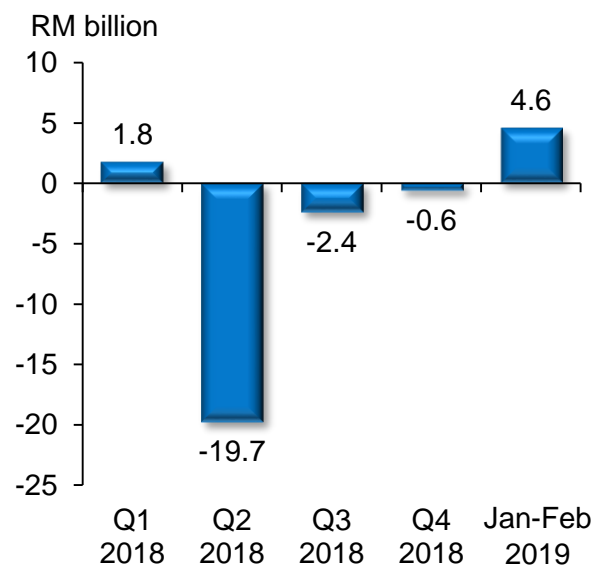
Source: BNM; Fed; MOF

# Net FOREIGN BUYING of Malaysian government bonds

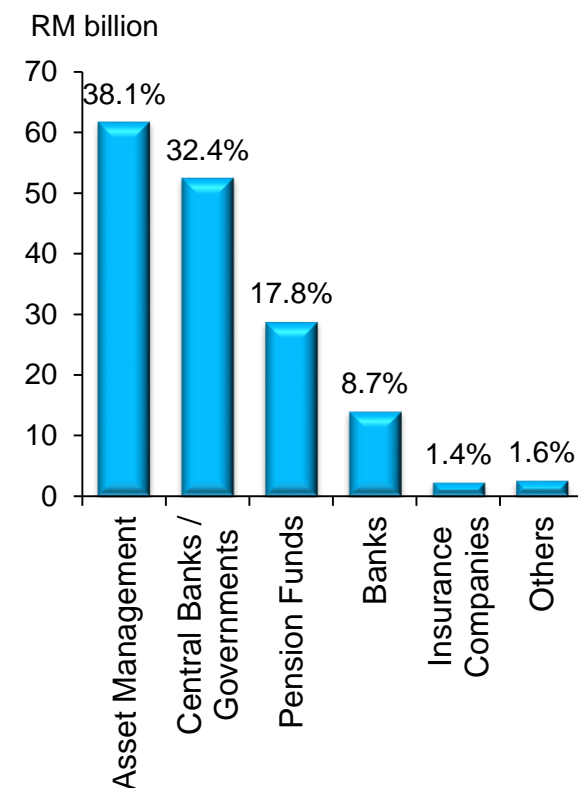
NR holdings of MGS & GII stood at 23.6% as at Feb 2019



Net foreign inflows YTD 2019



Long-term investors remain key holders of the Malaysian government bonds

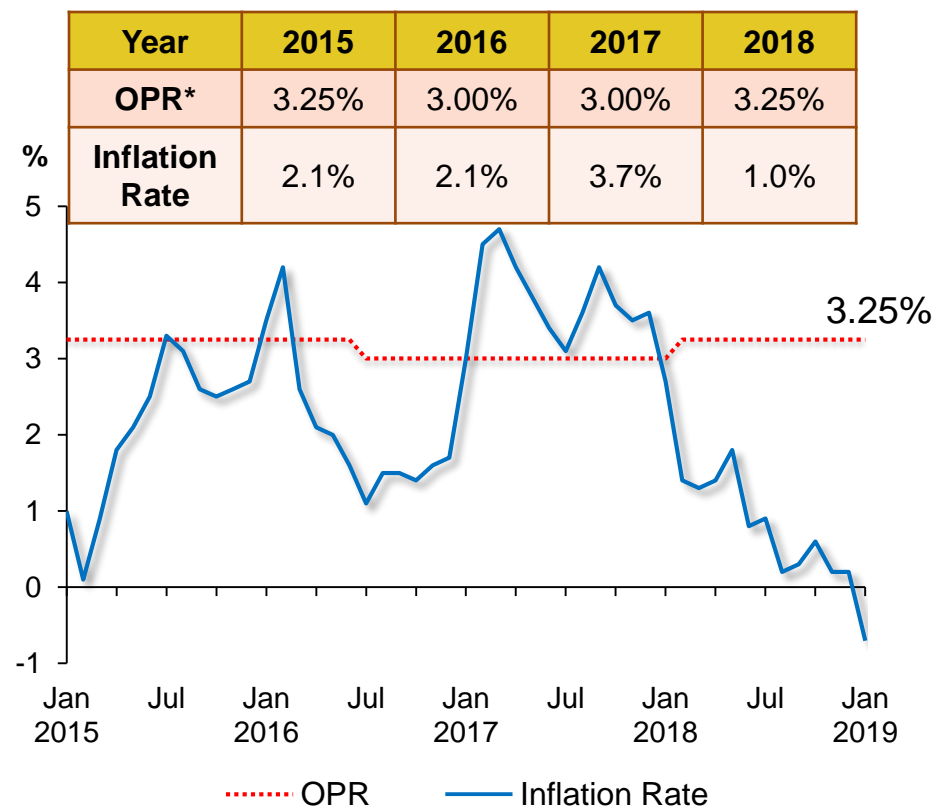


Source: BNM



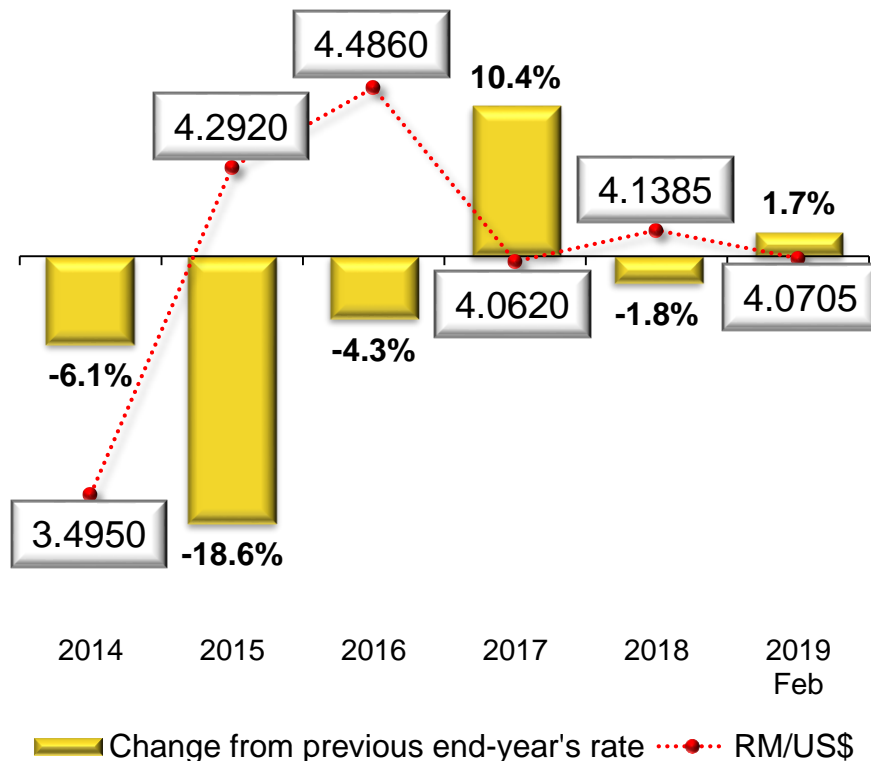
# An interest rate cut might be coming...

Inflation will rise moderately in 2019  
(1.0-1.5% vs. 1.0% in 2018)



\* OPR as at end-year

Ringgit outlook at RM4.00-4.10 per US dollar

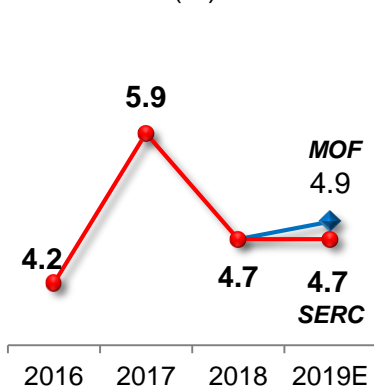


Note: Exchange rate (12:00 rate) as at end-period

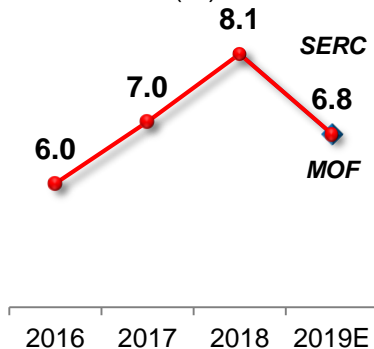
Source: BNM; DOSM

# Malaysia's key ECONOMIC INDICATORS

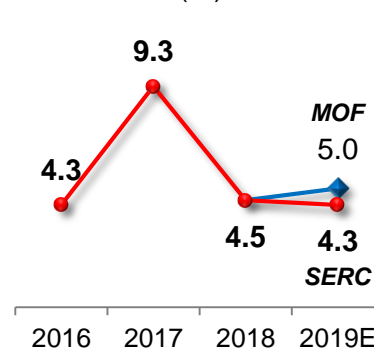
**Real GDP Growth (%)**



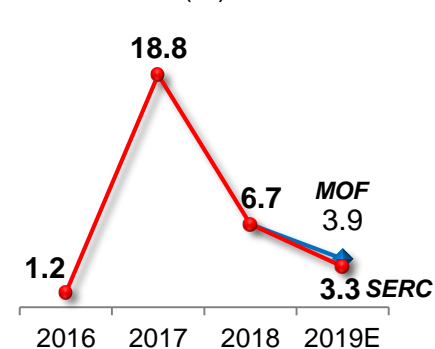
**Private Consumption Growth (%)**



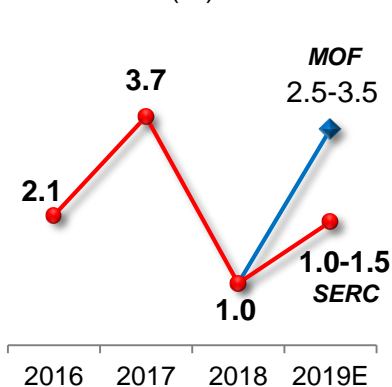
**Private Investment Growth (%)**



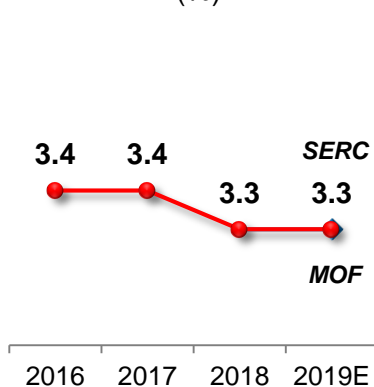
**Gross Export Growth (%)**



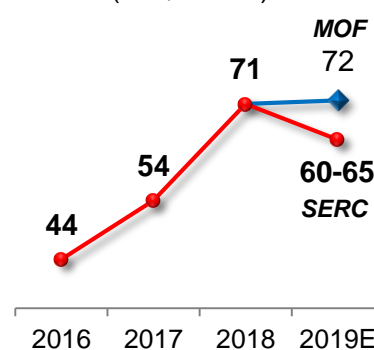
**Inflation Rate (%)**



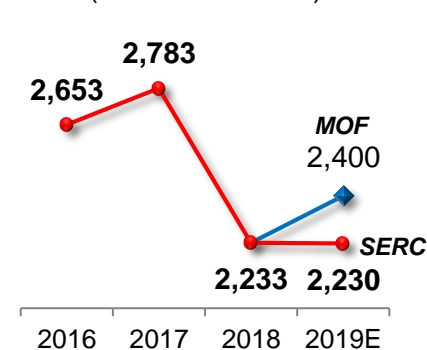
**Unemployment Rate (%)**



**Brent Crude Oil Prices (US\$/barrel)**



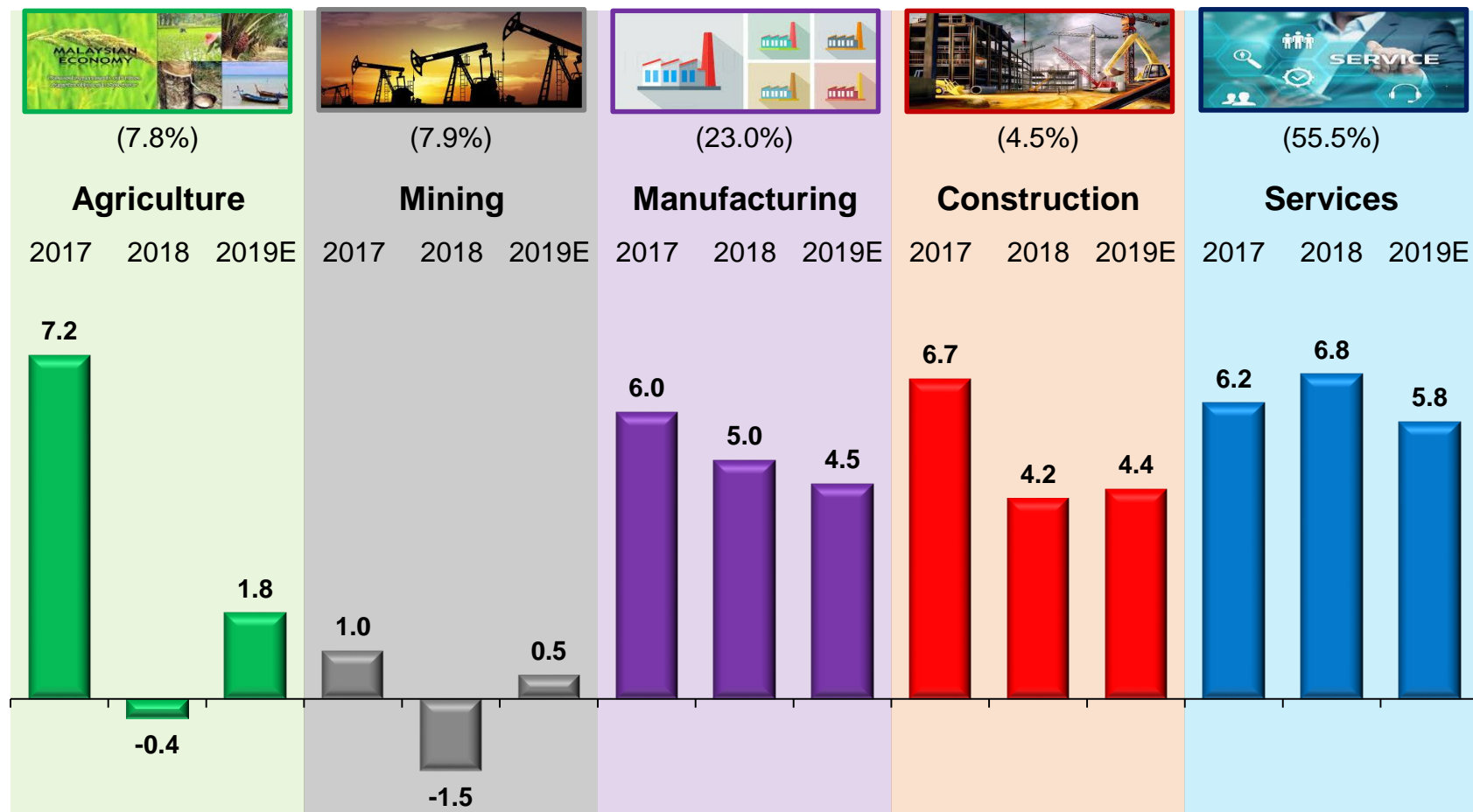
**Crude Palm Oil Prices (RM/metric tonne)**



Source: DOSM; MOF; EIA; MPOB; SERC

# A BROAD-BASED EXPANSION is expected in 2019

## Sectoral performance (%)



Note: Figure in parenthesis denotes share of GDP in 2018

Source: DOSM; SERC

# Sources of GDP growth: DEMAND and SUPPLY side

- Private sector expenditure will cushion the effects of lower public spending.
- All economic sectors are expected to register positive growth in 2019.

% growth, 2010=100	2016	2017	2018	2019F (MOF)	2019F (SERC)
<b>GDP by demand component</b>					
Private consumption (55.0%)	6.0	7.0	8.1	6.8	6.8
Private investment (17.4%)	4.3	9.3	4.5	5.0	4.3
Public consumption (12.8%)	0.9	5.4	3.3	1.8	1.8
Public investment (7.3%)	-0.5	0.1	-5.2	-5.4	-4.8
Exports of goods and services (70.6%)	1.3	9.4	1.5	1.6	1.5
Imports of goods and services (62.2%)	1.3	10.9	0.1	1.8	1.3
<b>GDP by economic sector</b>					
Agriculture (7.8%)	-5.2	7.2	-0.4	3.1	1.8
Mining & quarrying (7.9%)	2.1	1.0	-1.5	0.7	0.5
Manufacturing (23.0%)	4.4	6.0	5.0	4.7	4.5
Construction (4.5%)	7.4	6.7	4.2	4.7	4.4
Services (55.5%)	5.7	6.2	6.8	5.9	5.8
<b>Overall GDP</b>	<b>4.2</b>	<b>5.9</b>	<b>4.7</b>	<b>4.9</b>	<b>4.7</b>

Source: DOSM; MOF; SERC

Figure in parenthesis indicates % share to GDP in 2018

# What could **DERAIL** this year's domestic GDP growth?

## External Sources



- Unrelenting trade troubles, which would significantly dampen the US and China economies and severely disrupt global trade flows
- The Fed's over tightening of interest rates throwing the US economy into recession
- Sharp correction in global financial markets pulling down emerging markets, including downward pressures on currencies

## Domestic Sources



- Lack of policy clarity and inconsistency that dampens investors' sentiment
- Overly cautious spending behaviour on concerns about employment and income prospects
- Poor execution and implementation of Budget's development expenditure
- Negative external spillovers on domestic activities via exports channel and weak commodity prices





## Section 3

**What can the government do  
to power economic growth?**

*Structural reforms as cure*

# Key ISSUES and CHALLENGES facing Malaysia

- 1 **SLOWING PRODUCTIVITY GROWTH & IMPEDIMENTS:** Technology adoption, industrial structure, talent and skills gap, over-dependence on low-skilled foreign workers (Semi- and low-skilled workers: 72.5% of total employment in 2017; foreign workers: 15.5%).
- 2 **BURDENSOME REGULATORY and COMPLIANCE COSTS:** Inconsistent interpretation and application of regulations, the complex and lengthy licensing application processes have resulted in high costs and delays.
- 3 **QUALITY INVESTMENT:** Lower investment of ICT equipment (from 26% in 2010 to 22.2% in 2017). Many industries are still in the low-end to mid-range of the value chain as well as lower innovative capacity.
- 4 **VALUE ADDED SECTORAL OUTPUT:** (a) **Services sector** - dominated by traditional services subsectors while technology-driven modern services subsectors have stagnated; (b) **Manufacturing sector** – premature deindustrialization; high value added; and (c) **Agriculture sector** – less on agro-based industries; leverage on technology.
- 5 **LIMITED FISCAL SPACE:** Federal revenue has not kept pace with the economic growth and meet high committed expenditure. Tax buoyancy dropped from 2.2 in 2011 to 0.5 in 2017.
- 6 **HIGH RATES OF YOUTH & GRADUATES UNEMPLOYMENT** (unemployment rate of 10.8%) due to labour market mismatches, limited job creation and inadequate supply of industry-ready graduates.

# A multifaceted approach to **ADVANCING** future economic growth trajectory

- 1 DISCARD THE “BUSINESS AS USUAL” MINDSET.** A new mindset and attitude as well as behavioral changes
- 2 INVESTMENT POLICIES AND FRAMEWORK CONDITIONS** must be right and conducive. **EQUAL OPPORTUNITIES FOR ALL** and based on the smart Public-Private partnership
- 3** Process of **CREATIVE DESTRUCTION** to optimize resources and sharing of growth and economic dividends
- 4 DOMESTIC DIRECT INVESTMENT (DDI) initiatives** must be strongly promoted and facilitated along with foreign direct investment (FDI)
- 5 DOMESTIC SMEs** must be competitive (cost, quality and delivery) and connected to global supply chains
- 6** The **GOVERNMENT’S BUSINESS IS NOT IN BUSINESS. GLCS MUST BE OPENED TO A LEVEL PLAYING FIELD** to compete with the private sector
- 7 COMPENSATION OF EMPLOYEES (CE)** have to be improved if it is matched by the rise in productivity gains and commensurate with the skills set. Malaysia’s **CE to GDP ratio** increased from 33.9% in 2013 to **35.2% in 2017** was lower than Australia (47.3%), South Korea (44.4%) and Singapore (42.4%). The **target is to raise it to 38% by 2020.**

# STRUCTURAL REFORMS to uplift growth potential



**STRUCTURAL REFORMS** are necessary to restore **ECONOMIC DYNAMISM**, ensure **SUSTAINABLE** and sustain **COMPETITIVE** growth in the long term



**BIG-BANG** versus **GRADUALISM** comes with adjustment costs



**STRONG POLITICAL WILL  
AVOIDING DISRUPTIVE BIG-BANG CHANGES**

# A list of key measures PH Government has implemented

- 1 **REFORM** of **Malaysian Anti-Corruption Commission (MACC)** and **Election Commission (EC)** – **Electoral Reform Committee (ERC)** on 16 Aug 2018.
- 2 **ABOLISHMENT OF 6% GST** after 3 months (Jun-Aug 2018) of zero-rated GST and replaced by **REINTRODUCTION OF SST** of 5% / 6% / 10% on 1 Sep 2018.
- 3 RON95 fuel prices was kept unchanged at RM2.20/litre in 2018 after election. W.e.f 5 Jan 2019, a **WEEKLY FLOAT SYSTEM** was implemented. If the world crude oil prices rise, fuel prices will be capped at RM2.08/litre (from RM2.20 previously) for RON95 and RM2.18/litre for diesel, until **TARGETED FUEL SUBSIDY SCHEME** to be introduced by June 2019.
- 4 **FIXED BROADBAND PRICES** dropped by at least 25% by end-2018.
- 5 **REVIEW OF MEGA PROJECTS** in terms of viability and cost. (a) The deferment of HSR and MRT3; (b) Cost savings of RM15.0bn for LRT3 and RM8.8bn for MRT2 respectively; (c) Cancellation of Trans-Sabah Gas Pipeline projects; and (d) ECRL is pending review – scale and cost of project.
- 6 Established **DEBT AND LIABILITY MANAGEMENT COMMITTEE** on 15 Jan 2019, targeted to reduce government's debt and liabilities to a manageable level in 18 months.
- 7 The setting up of **ECONOMIC ACTION COUNCIL (EAC)** on 11 Feb 2019 to stimulate economic growth, ensure fair distribution of wealth and improve the well-being of the people.



- 8 The establishment of **NATIONAL COUNCIL OF COST OF LIVING** (NACCOL) to tackle issues and challenges in pertaining to rising cost of living.
- 9 **RM100 MONTHLY PASS FOR UNLIMITED RIDES** of public transport network (Rapid KL), reduced **KTM Komuter fare** by 20% starting 1 Apr 2019.
- 10 **Reform COST OF LIVING AIDS** to a more targeted approach, eligible recipient with kid(s) will receive additional cash aids of up to RM480.
- 11 **SME INCOME TAX RATE CUT** by 1% to 17%.
- 12 **SPECIAL VOLUNTARY DISCLOSURE** (Nov 18 to Jun 19; a lower penalty rate of between 10% and 15% of the tax payable compared to the penalty rate of between 80% and 300% after the deadline) offers an opportunity for taxpayers to voluntarily declare unreported income, including offshore accounts, is expected to bring in an extra **RM10 BILLION** to the government coffers.
- 13 **RENEWAL OF FOREIGN WORKERS' (FW) WORKING PERMIT** from 10 years of services to a maximum of 13 years; reduced FW levy for renewal to RM2,000 (from RM3,500 and RM10,000 previously) for agriculture and plantation sectors and to RM6,000 for other sectors (from RM10,000 previously), for a year starting 1 Mar 2019.
- 14 **FREEZE TOLL HIKES** for intra-city in 2019; **toll abolishment for motorcyclist** in using Penang Bridge I and II as well as Johor Second Link; proposed **TOLL ABOLISHMENT FOR FOUR HIGHWAYS**; would implement congestion charges at 100% during peak hours, 70% in off-peak hours and free during 11pm-5am.

# Fiscal and Debt Reconstruction

- **Sustainable** revenue base (tax less on employment and business income; more on consumption)
- Plugging **tax leakages**; shadow economy (2017: 22.9% of GDP (RM298 billion); tax gap is about 20% vs 10-15% in developed economies)
- **Tax reform** (Fair, Effective and Simpler)
- **Expenditure rationalization** (targeted subsidy; pension reform)
- Active **debt** and **responsible budget management** (Zero-based budgeting; accrual accounting)



## Labour Market and Wage Reform

- Boosting productivity through **reskilling and training**
- **Performance-driven** wage system; labour flexibility
- **Technical and Vocational Education Training (TVET)**
- Spurring **innovation**; ecosystem for **creation**
- **Phase reduction of reliance** on foreign workers
- **Living wage** and linked with productivity



## Market and Investment Liberalisation

- Equal and inclusive opportunities for **ALL**
- ‘**Schumpeterian creative destruction**’
- Targeted programs for **SMEs**
- Review **current incentives** (time bound)

## GLCs Reform

- **Leaner**, responsive and less intrusive
- **Functions to be systematically** reviewed
- **Transparency**, better **governance** & **accountability**
- Subjected to **Parliamentary oversight**
- **Optimization of resources** and mandates for real competition



## Social Safety Net

- Targeted **most vulnerable and needy households**
- **Conditionally social assistance system** – income enhancement, employability and empowerment; **Exit program** to wean off from subsidy mentality
- **Pension and healthcare** reform (ageing population)





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

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>