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QUARTERLY
ECONOMY TRACKER

Positive Signals Amid Downside Risks

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World Economic Outlook Update

GLOBAL GROWTH STILL GROWING AMID MULTIFACETED RISKS

- **Global economy maintains momentum, albeit moderate in 2024.** The global economy is expected to grow at a decent clip in 2024, supported by domestic demand and a gradual improvement in global trade activity. The International Monetary Fund (IMF) raised its forecast for global growth to 3.2% (from 3.1% and 2.9% previously) in 2024, though it is still below the average global GDP growth of 3.8% pa in 2000-2019.

- **Global leading and lagging indicators show a continued expansion.** (a) Global manufacturing PMI has returned to 50-pt in January 2024 and increased gradually to 50.6 in March after trapping below the threshold for 16 consecutive months, signalling an improvement; (b) The OECD composite leading indicators continued its upward trajectory; (c) Global semiconductor sales have bottomed out, registering positive growth since November 2023; (d) World trade volume growth has returned to positive trajectory after contracting for nine consecutive months in Apr-Dec 2023. According to the World Trade Organization (WTO), global trade, which has fallen by 1.2% in 2023 will regain growth traction to increase by 2.6% in 2024 though below the 2011-2019 average growth of 3.7% pa. This will be supported by the improvement in demand, increased trade in goods closely linked to the business cycle, such as machinery and consumer durables, as well as an upturn in the global technology cycle.

- **The economic tracker of major economies.** Latest data showed a mixed performance in the real activities. Headline inflation has consistently slowed, albeit the last mile to tame it will be bumpy.

  a) **The US economy ended at Q4 2023 on a pretty good shape** (3.4% annualised qoq vs. 4.9% annualised qoq in Q3), underpinned by resilient household spending and exports, while federal government spending and private investment have lost steam. A slew of data suggests continued economic expansion in Q1 2024. Better PMI readings in both the manufacturing and services sectors (manufacturing PMI returned to an expansionary track in March 2024 after 16 months of contraction), retail sales grew by 3.3% yoy in Q1 2024 (3.3% in Q4 2023), and headline inflation inched up to 3.5% in March from 3.2% in February and 3.1% in January. The unemployment rate eased to 3.8% in March from 3.9% in February (3.7% in January), while the annual wage growth eased to 4.1% from 4.3% in February and 4.4% in January. As the labour market cools and wage gains abate, consumer spending should moderate going forward.

  b) The **euro area slipped into a technical recession** as GDP declined marginally by 0.1% qoq in Q4 2023 following a -0.1% decline in Q3. The incoming economic data is still weak, suggesting subdued growth in Q1 2024, restrained by high borrowing cost and depleted savings. The Eurozone Composite PMI rose to 50.3 in March 2024 after nine months of contraction; service PMI increased for the second consecutive month in March after six months of decline while manufacturing PMI declined further for 21 consecutive months. Industrial output shrank by 6.6% and 6.4% yoy in January and February, respectively, while the Economic Sentiment Indicator (ESI) at 96.3, below the 100-pt threshold for 21 continuous months, signalling persistent pessimism. On a positive note, inflation slowed to 2.4% in March 2024 from 2.9% in December 2023, moving closer to the European Central Bank's target rate of 2.0%. The unemployment rate remained at 6.5% for four straight months in February 2024.

c) The **Japan economy** has averted a technical recession as GDP returned to marginal positive growth in Q4 2023 (0.1% qoq and 1.2% yoy), bolstered by strong capital expenditure. High inflation has crimped private consumption. Latest data suggest improved economic showing in Q1 2024: Manufacturing PMI stood at 48.2 in March (47.2 in Feb) and Services PMI rose to 54.1 in March (52.9 in Feb). Exports rose 7.8% yoy in February (11.9% in Jan) for the third month running, supported by strong exports of cars and semiconductors. While headline inflation increased by 2.8% yoy in February 2024 (2.2% in January; 3.2% in Dec 2023), core inflation (less fresh food and energy) continued its declining trend to 3.2% in February from 4.3% in Jul-Aug 2023.

d) **China's economic data displayed mixed signals.** China's GDP growth expanded by 5.3% in Q1 2024 (5.2% in Q4 2023), beating market expectations, supported by exports and a raft of stimulus measures to lift consumption amid still stressing property sector. Industrial output grew by 4.5% yoy in March, missing expectations of 6%. Retail sales grew by 3.1% yoy, lower than expectations of 4.6%. The embattled real estate sector continued to show weakness, with property investments falling 9.5% yoy in Q1. There were sharp declines in property sales, property investment and floor space under construction, and ongoing declines in home prices.

- **Global interest rates tracker.** With global headline and core inflation readings falling though remain a distance from major central banks' inflation target, the rate cut is on the horizon going forward. The central banks are waiting for more confirmation of price data before cutting interest rate. The central banks officials want to "feel more confident" that inflation is heading towards the central bank's target.

a) The **Federal Reserve** (The Fed) held its key interest rate steady for the fifth consecutive meeting, as the central bank awaits more data to determine when to cut rates. The timing of that first rate cut is critical as if it is too soon, it could undo the progress the Fed has seen to control inflation, and if it is too late, it could slow down the economy too much. While the Fed's dot plot still maintains a total three rate cuts, a string of disappointing inflation data has forced the Federal Reserve to reset the clock on its first interest-rate cut and re-evaluate the trajectory of price growth. Markets now expecting the Fed to hold interest rate longer, paring down their rate cut expectations by 1-2 times.

b) **Bank of Japan** has ended eight years of negative interest rates as it increased its overnight call rate to 0.00%-0.10% on 19 March. The central bank also abandoned yield curve control (YCC) that capped long-term interest rates around zero, and discontinued purchases of risky assets while will keep buying 6 trillion yen government bonds as before and ramp up purchases in case yields rise rapidly, underscoring its focus on preventing any damaging spike in borrowing costs. This signals that BOJ's future rate hikes will be moderate.

c) The **European Central Bank** held interest rates steady (deposit rate at 4.00%) for the fifth consecutive meeting amid the progress has been made in bringing down inflation. The officials are weighing how soon they can bring interest rates down but said they needed to see more proof of slowing price growth. For now, strong wage growth was keeping domestic price pressures high.

d) The **People's Bank of China** cut its 5-year loan prime rate by 25 basis points to 3.95% in February while the 1-year loan prime rate remains at 3.45% in the latest move to ease pressures on the failing property market. The central bank has limited room to manoeuvre given downward pressure on the Chinese yuan at a time when the major central banks have not yet begun cutting rates.

- **Risks remain skewed to the downside.** The global growth outlook remains subject to downside risks, mainly from an escalation of geopolitical conflicts in Ukraine and the Middle East, higher-than-anticipated inflation outturns, the US Presidential election and volatility in global commodity and financial markets.

- The IMF warned that an escalating Middle East conflict risks leading to higher oil prices, a reversal of the recent fall in inflation and a puncturing of the optimistic mood in financial markets. The international organisation said it was closely monitoring events in the region and stressed the possibility that a war between the two countries could lead to higher interest rates.

Global Economic and Monetary Conditions

Real GDP growth (%, Y-o-Y)

	2022	2023	2023 Q1	2023 Q2	2023 Q3	2023 Q4	2024F (IMF)	2024F (WB)
World	3.5	3.2	N/A	N/A	N/A	N/A	3.2	3.2
United States	1.9	2.5	1.7	2.4	2.9	3.1	2.7	1.6
Euro Area	3.4	0.4	1.3	0.6	0.1	0.1	0.8	0.7
China	3.0	5.2	4.5	6.3	4.9	5.2	4.6	4.5
Japan	1.0	1.9	2.6	2.3	1.6	1.2	0.9	0.9
India	7.0	7.6	6.2	8.2	8.1	8.4	6.8	7.5
Malaysia	8.7	3.7	5.6	2.9	3.3	3.0	4.4	4.3
Singapore	3.8	1.1	0.5	0.5	1.0	2.2	2.1	N/A
Indonesia	5.3	5.0	5.0	5.2	4.9	5.0	5.0	4.9
Thailand	2.5	1.9	2.6	1.8	1.4	1.7	2.7	3.2
Philippines	7.6	5.5	6.4	4.3	6.0	5.5	6.2	5.8
Vietnam	8.0	5.1	3.4	4.3	5.5	6.7	5.8	5.5

Note: World GDP growth for 2022-2023 by IMF; Annual GDP for India is on fiscal year basis; N/A = Not applicable or not available

Source: Officials (unadjusted data except quarterly GDP for Euro Area); IMF (World Economic Outlook (WEO); World Bank (Global Economic Prospects)

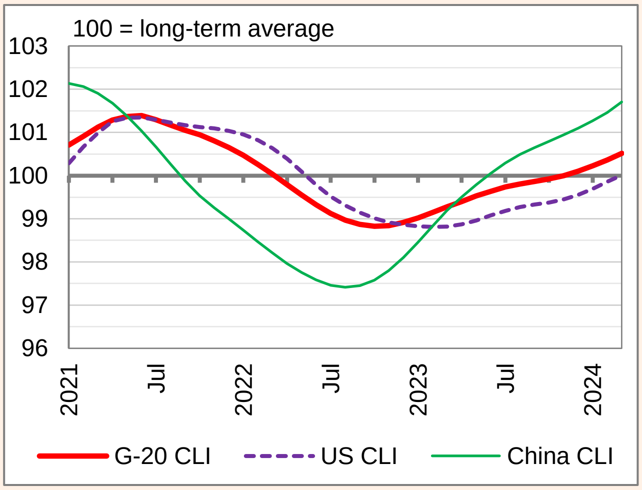
Policy rate (%)

End-period of	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024 (Mar/ Apr)	2024*f*
US, Fed Federal Funds Rate	0.25-0.50	0.50-0.75	1.25-1.50	2.25-2.50	1.50-1.75	0.00-0.25	0.00-0.25	4.25-4.50	5.25-5.50	5.25-5.50	5.00-5.25
Euro Area, ECB Deposit Facility	-0.30	-0.40	-0.40	-0.40	-0.50	-0.50	-0.50	2.00	4.00	4.00	3.50-3.75
Japan, BOJ Overnight Call Rate	0.00-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	0.00-0.10
China, PBC 1-Year Loan Prime Rate	4.35	4.35	4.35	4.35	4.15	3.85	3.80	3.65	3.45	3.45	3.45
India, RBI Policy Repo Rate (LAF)	6.75	6.25	6.00	6.50	5.15	4.00	4.00	6.25	6.50	6.50	6.50
Korea, BOK Base Rate	1.50	1.25	1.50	1.75	1.25	0.50	1.00	3.25	3.50	3.50	2.75
Malaysia, BNM Overnight Policy Rate	3.00	3.00	3.00	3.25	3.00	1.75	1.75	2.75	3.00	3.00	3.00
Indonesia, BI BI-Rate	7.50	4.75	4.25	6.00	5.00	3.75	3.50	5.50	6.00	6.00	5.00
Thailand, BOT 1-Day Bilateral Repo Rate	1.50	1.50	1.50	1.75	1.25	0.50	0.50	1.25	2.50	2.50	2.25
Philippines, BSP Target RRP Rate	4.00	3.00	3.00	4.75	4.00	2.00	2.00	5.50	6.50	6.50	5.75

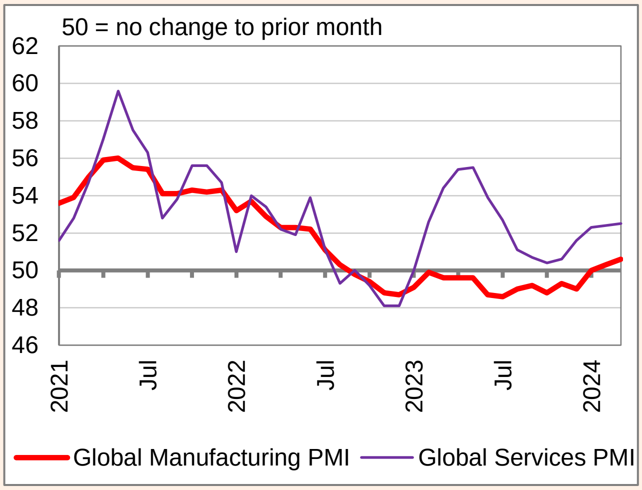
Source: Officials; SERC

Global Current and Forward Indicators

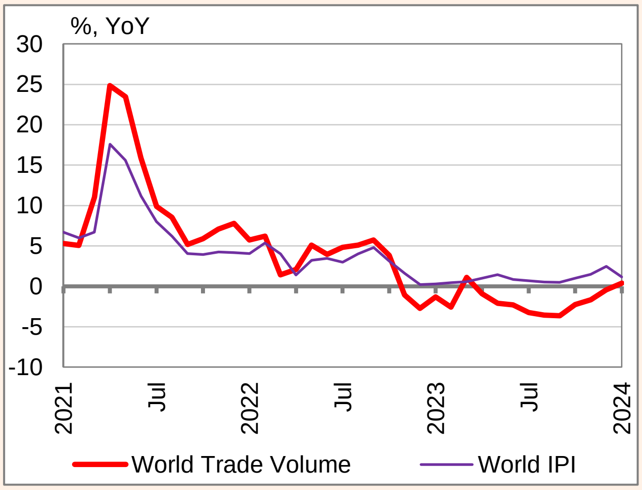
Composite leading indicators signalling an expansionary outlook



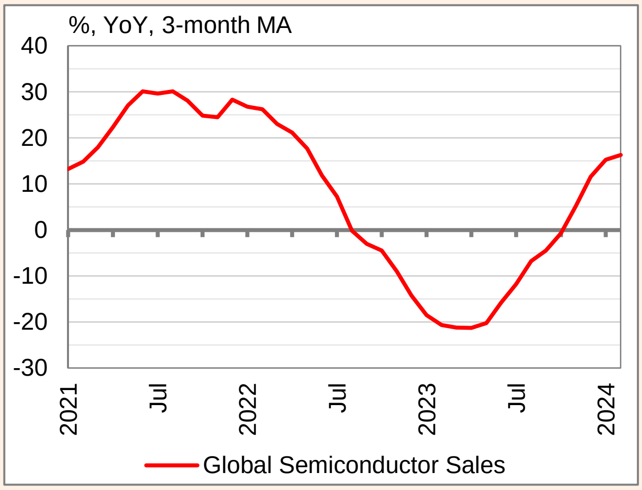
Global manufacturing PMI ended its 16-month contraction (Sep 2022-Dec 2023)



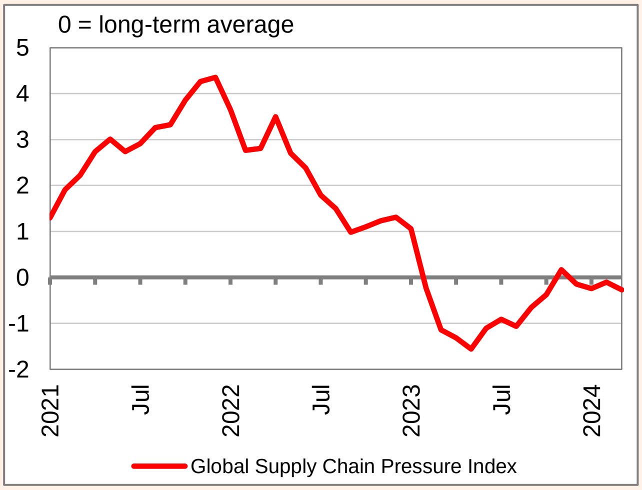
Global trade volume back to positive growth in Jan after 9 months of decline



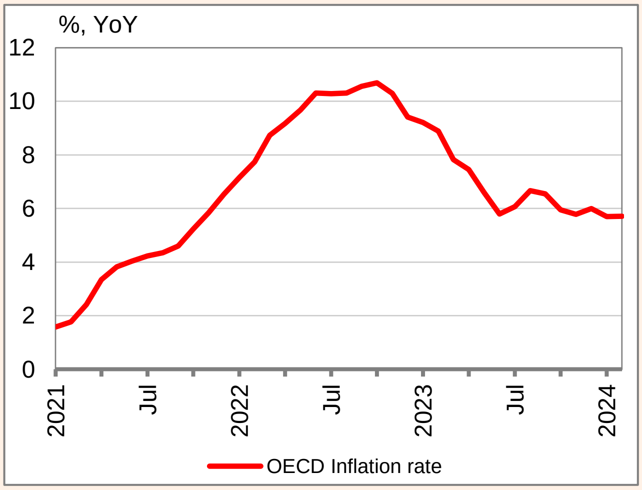
Global semiconductor sales have turned around



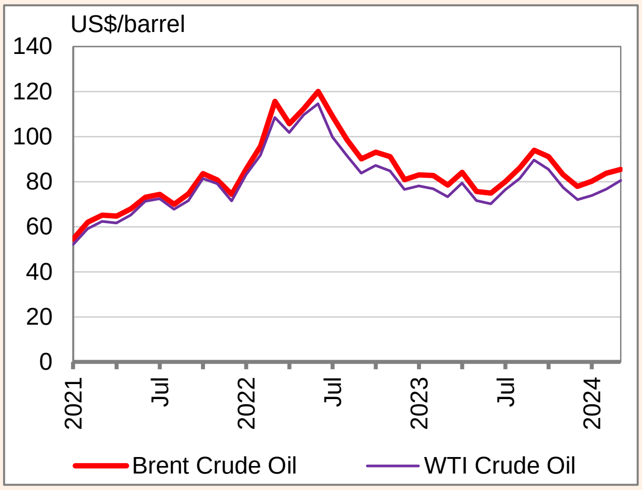
Global supply chain pressures could rise inflicted by the Middle East tensions



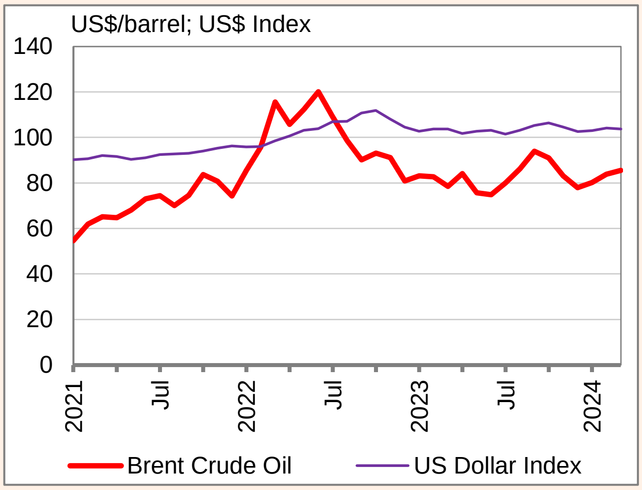
OECD inflation rate remained broadly stable but tilted to upside risks



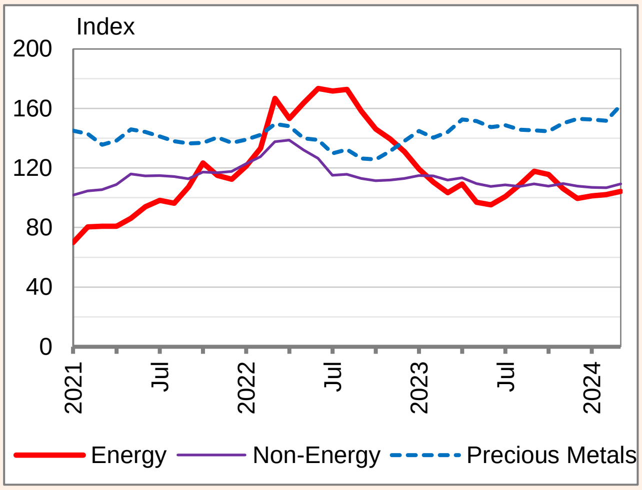
Crude oil prices in focus due to military conflicts in the Middle East



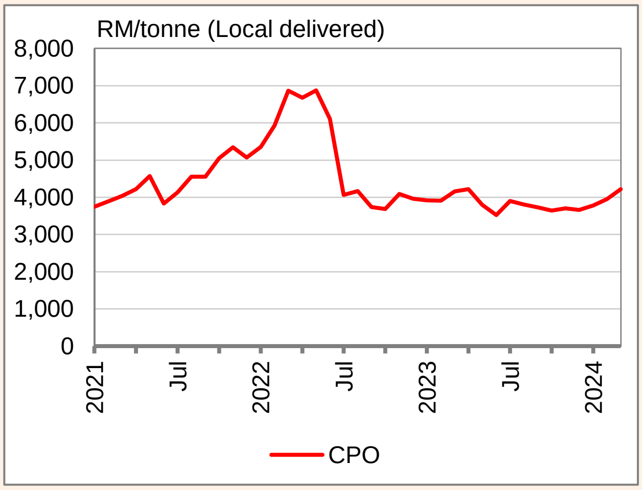
Brent crude oil prices vs. the US dollar index



Prices of precious metals on upwardly trajectory



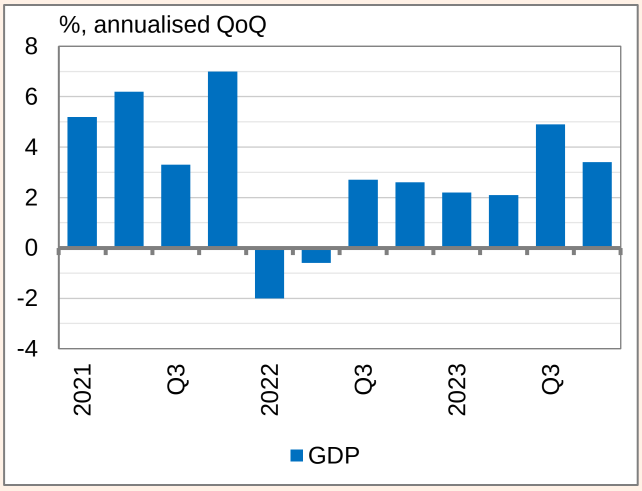
Crude palm oil prices are picking up



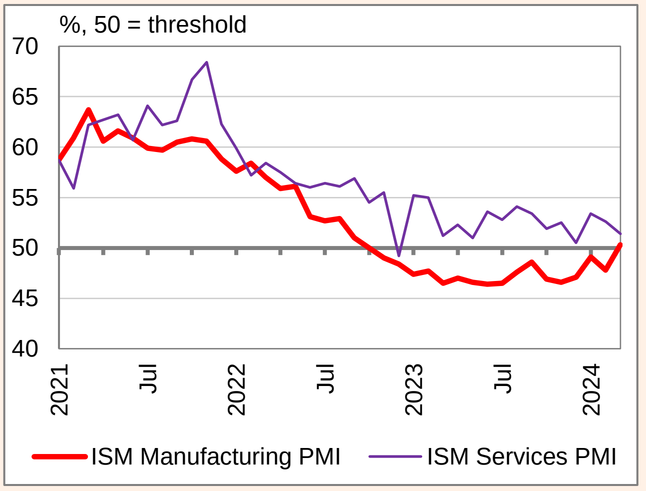
Source: Organisation for Economic Co-operation and Development (OECD); S&P Global; CPB Netherlands Bureau for Economic Policy Analysis; Semiconductor Industry Association (SIA); Federal Reserve Bank of New York; World Bank; The Wall Street Journal; Malaysian Palm Oil Board (MPOB)

The US – Soft landing remains intact

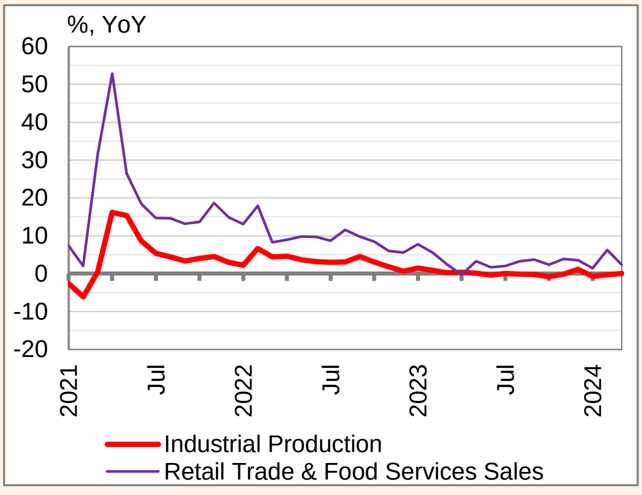
The US economy underpinned by resilient household spending and exports



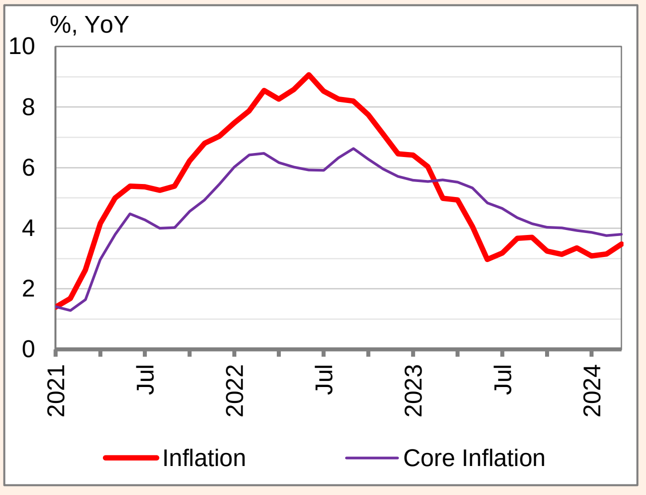
Manufacturing PMI returned to positive territory after 16 months of contraction



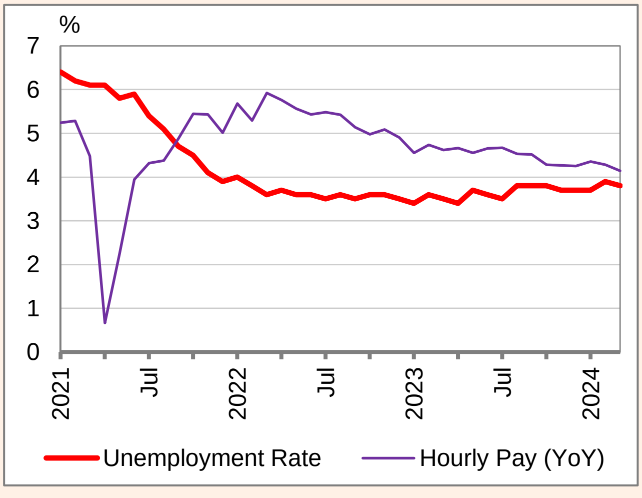
Industrial production growth was muted amid flattish retail sales growth



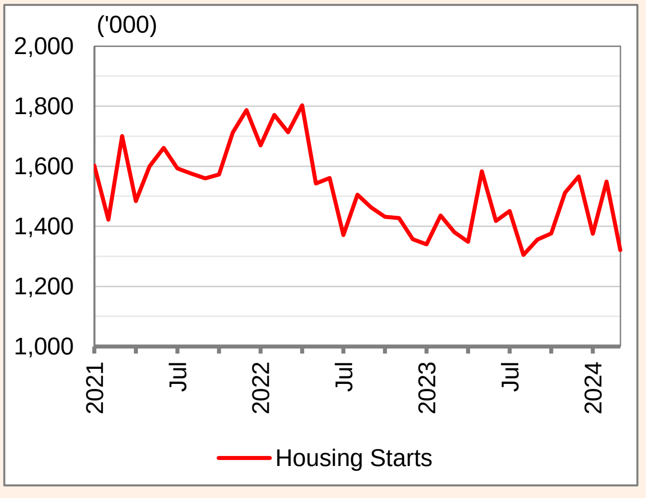
Headline inflation shows sign of uptick



Hourly paid wage growth eased; the unemployment rate stayed below 4%



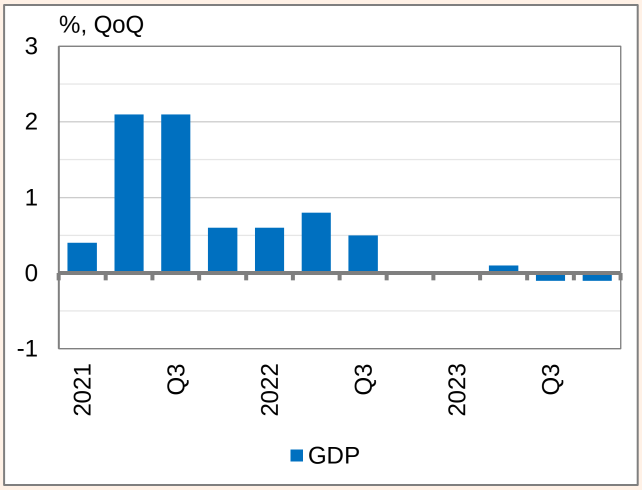
Housing starts remained uneven



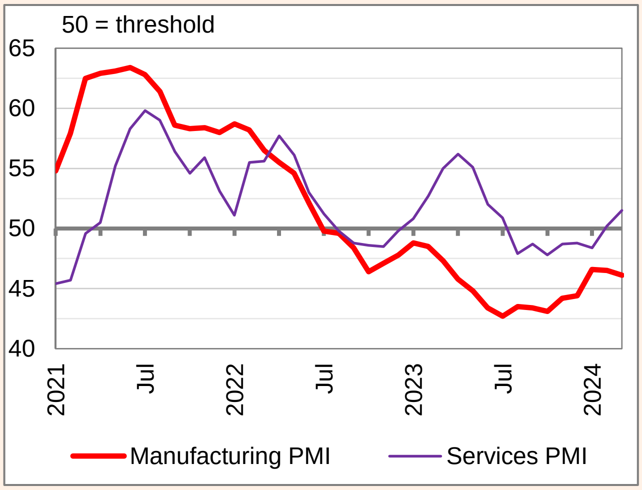
Source: Bureau of Economic Analysis (BEA); Institute for Supply Management (ISM); Federal Reserve System; US Census Bureau; US Bureau of Labor Statistics

Euro Area – Imminent rate cut to stem economic contraction

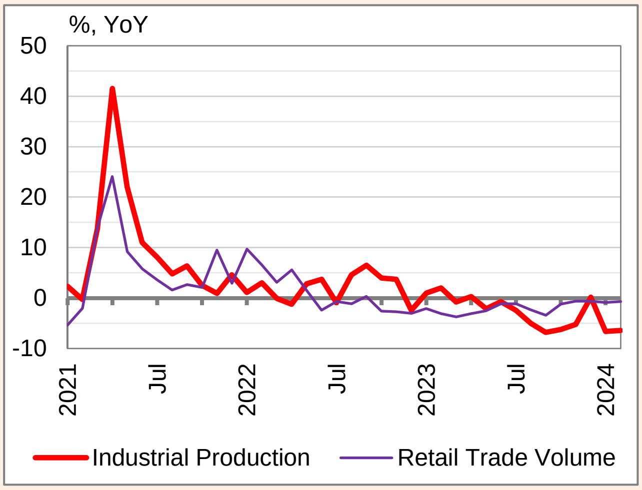
Euro area sank into a technical recession



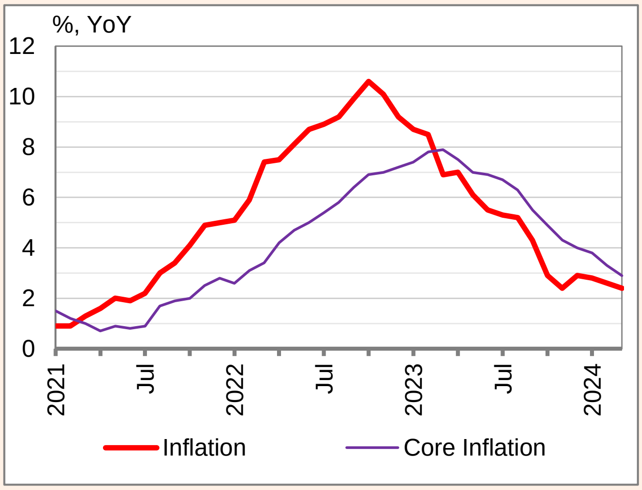
Manufacturing PMI contracted persistently; services PMI has moved higher



Retail trade continued to decline for 17 consecutive months



Soft inflation bolsters the ECB to cut rate to rescue the flagging economy



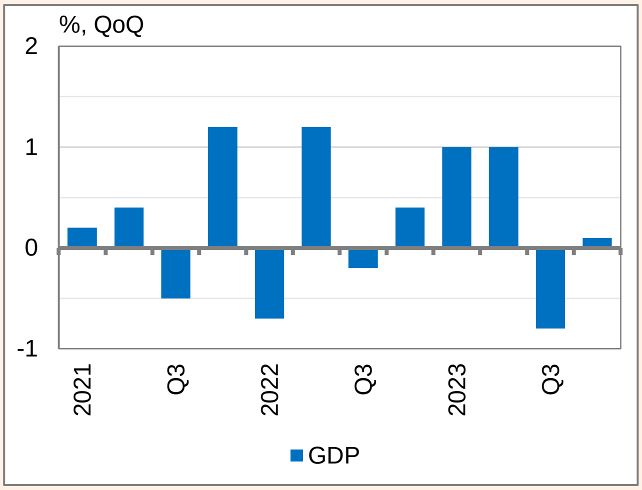
Unemployment rate held steady at 6.5% in Feb for four straight months

Exports grew mildly for two months in Feb

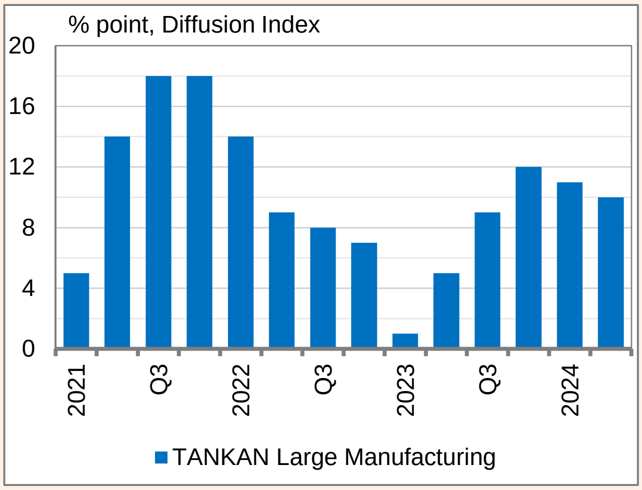
Source: Eurostat; S&P Global

Japan – An end of negative policy rate

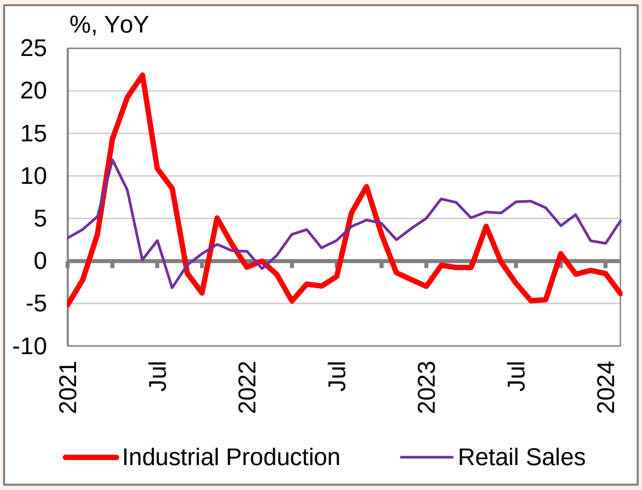
Escaped from a technical recession in Q4



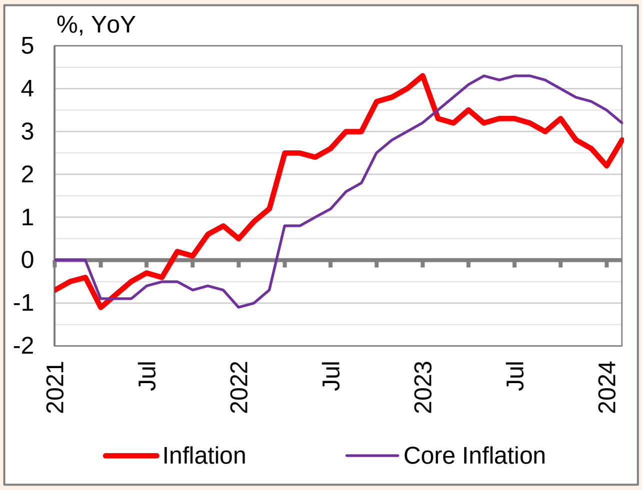
TANKAN survey indicates expansionary outlook in the manufacturing sector



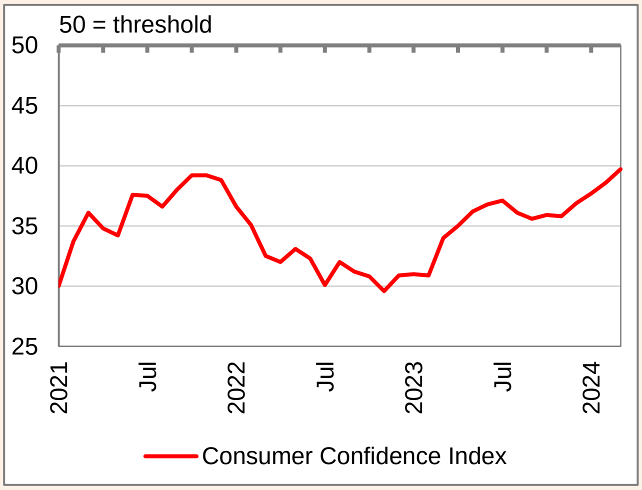
Industrial production contracted for the fourth continuous month



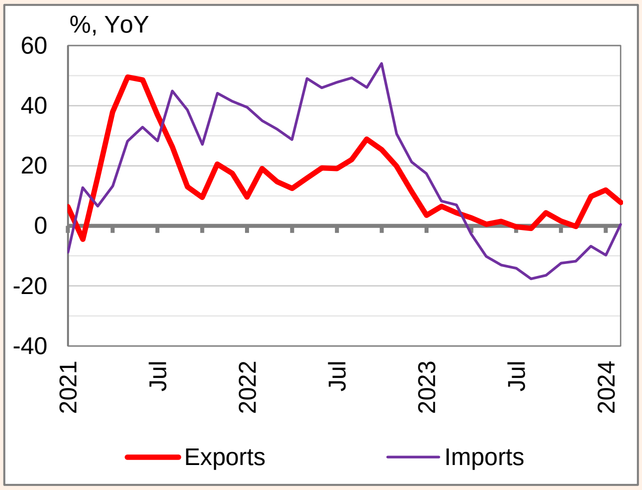
Inflation rate picked up again in Feb



Consumer confidence recovered a little yet still far from the optimism threshold



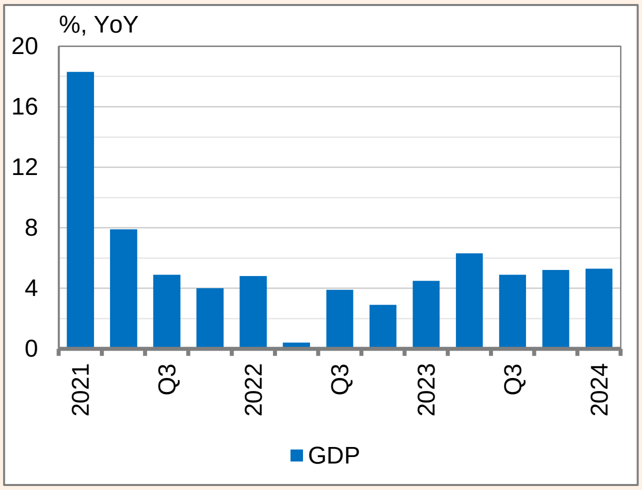
Export growth improved on low base effect



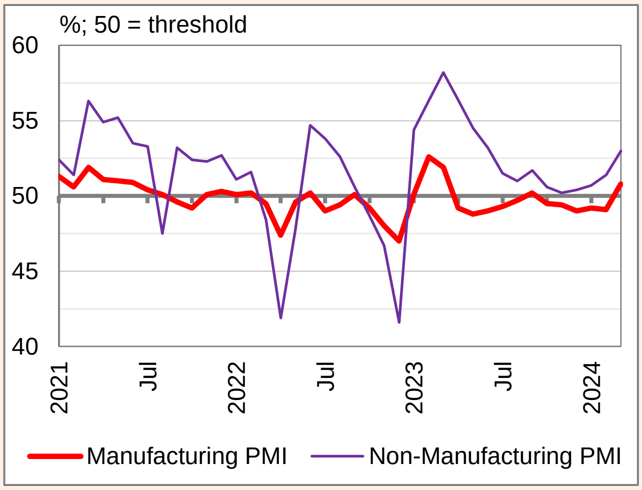
Source: Economic and Social Research Institute (ESRI), Cabinet Office of Japan; Bank of Japan (BOJ); Ministry of Economy, Trade and Industry (METI), Japan; Statistics Bureau, Japan; Japan Customs

China – Accelerating growth

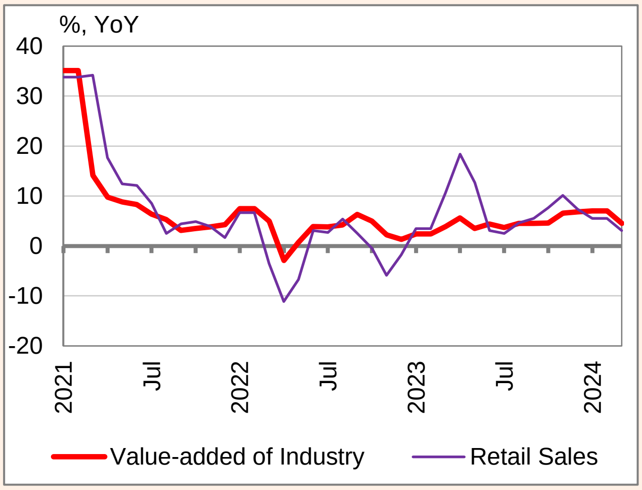
A good start for the year 2024 with real GDP of 5.3% growth in Q1



Manufacturing PMI signals expansion ahead after 5 months below threshold

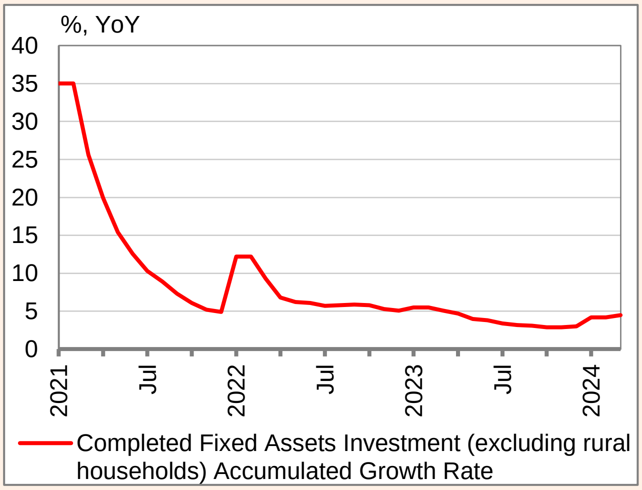


Both industrial and retail growth moderated in March

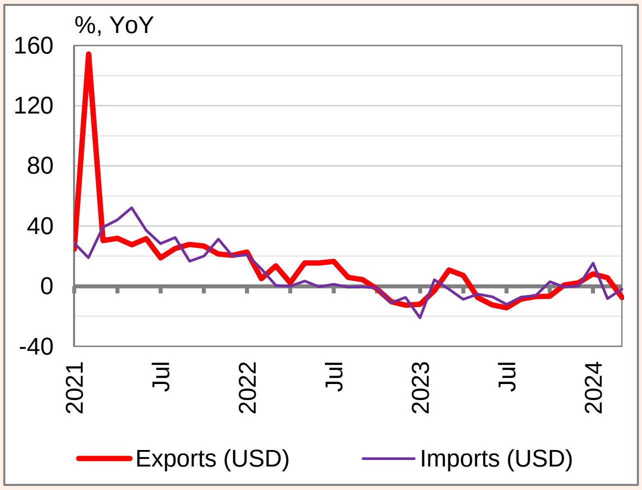


Inflation is broadly muted in Mar post festive season

Fixed investment growth improved, particularly in the secondary sector



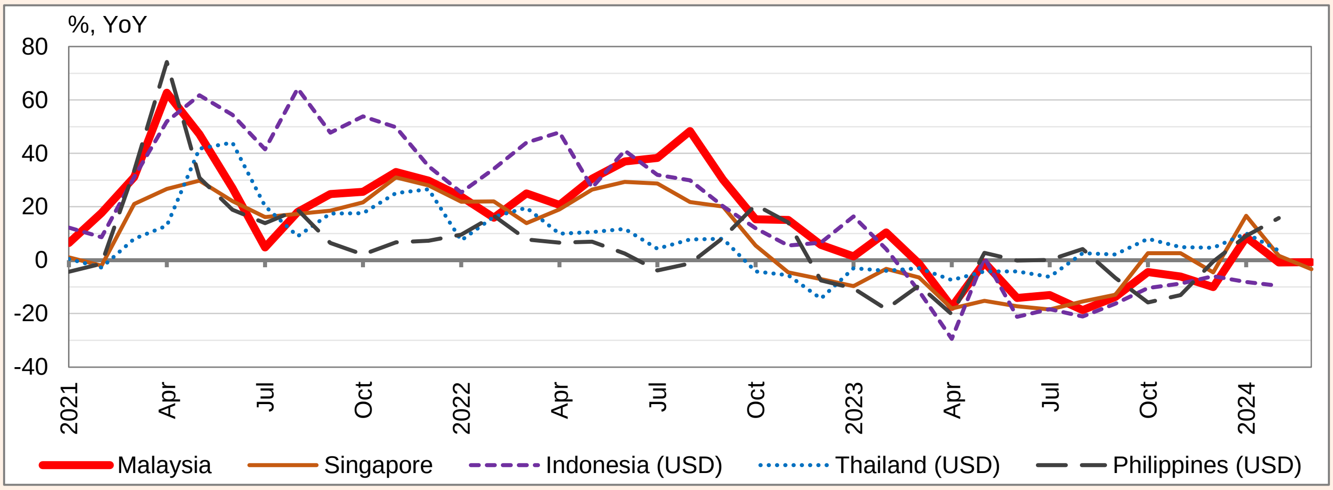
Exports declined in Mar after four months of growth



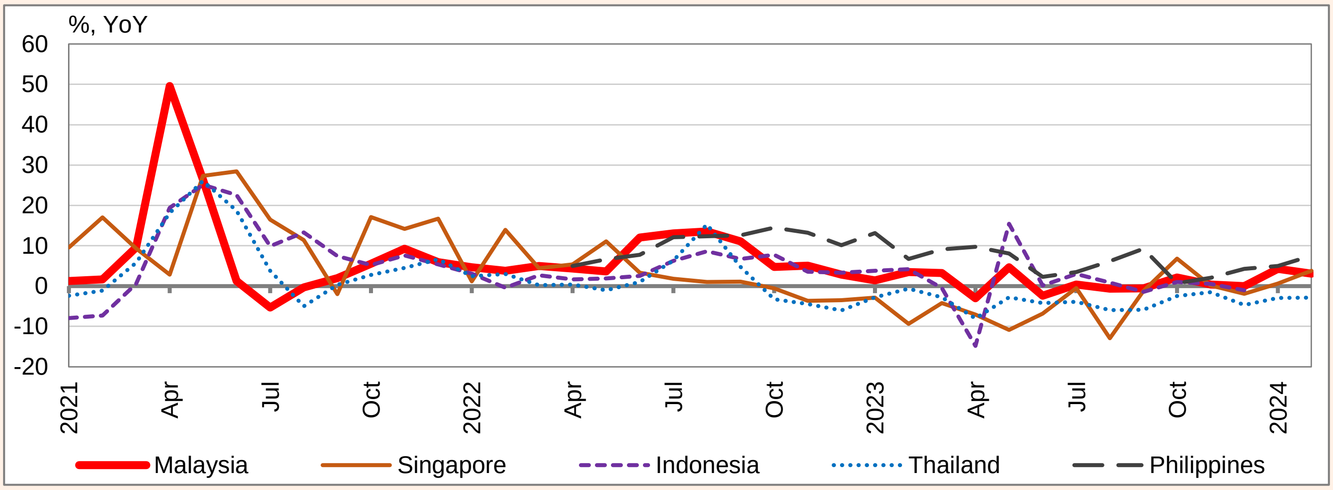
Source: National Bureau of Statistics of China; General Administration of Customs, China

ASEAN Key Economic Indicators

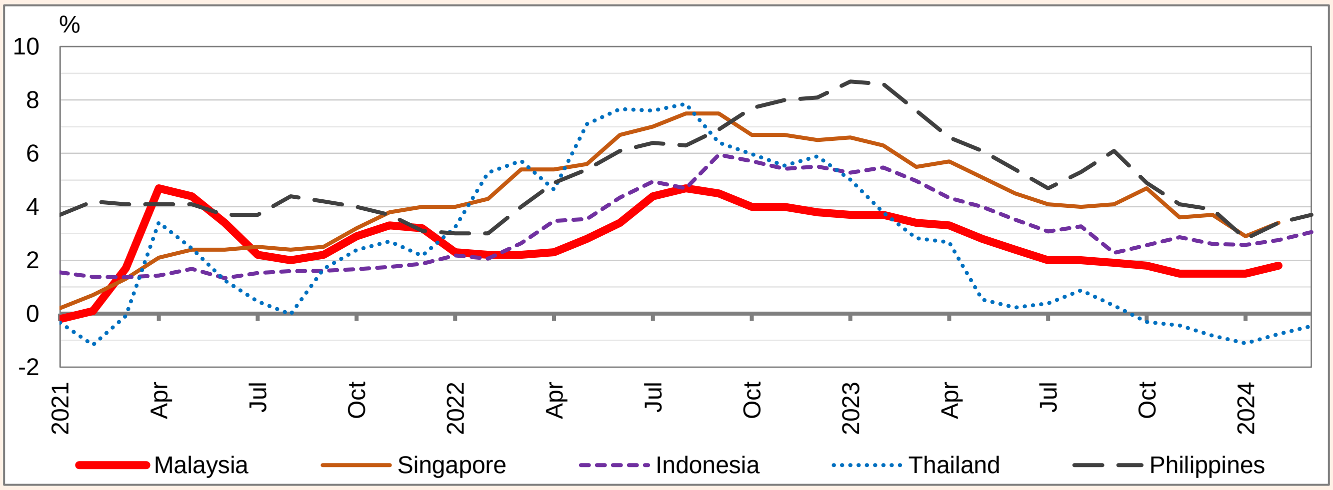
Export growth trend



Industrial production growth trend



Inflation trend



Source: Department of Statistics, Malaysia; Singapore Department of Statistics; Statistics Indonesia; Bank Indonesia; Office of Industrial Economics, Thailand; Ministry of Commerce, Thailand; Philippine Statistics Authority

Note: Industrial production growth for the Philippines only showed from April 2022 due to exceptional data prior to that.

POSITIVE SIGNALS AMID DOWNSIDE RISKS

- The Malaysian economy starting the year 2024 in a positive direction, albeit a mixed performance. The Department of Statistics Malaysia (DOSM)'s advance estimates indicated that real GDP increased by 3.9% yoy in Q1 2024 (3.0% in Q4 2023), supported by the services and construction sectors and a turnaround in the manufacturing sector. The growth outlook remains subject to downside risks.
- Global leading and forward indicators suggest continued global growth, albeit still moderate. The International Monetary Fund raised its forecast for global growth to 3.2% (from 3.1% and 2.9% previously) in 2024. However, it is still below the average global GDP growth of 3.8% pa in 2000-2019. Some central banks have begun to lower interest rates as global inflation has fallen.
- According to the World Trade Organization (WTO), global trade, which has fallen by 1.2% in 2023 will regain growth traction to increase by 2.6% in 2024 though below the 2011-2019 average growth of 3.7% pa.
- In Bank Negara Malaysia's (BNM) Economic and Monetary Review Report, it expects higher economic growth of 4.0%-5.0% (mid-point estimate at 4.5%) in 2024 (3.7% in 2023), in line with our (SERC) estimate of 4.5%. This will be driven by a recovery in exports and resilient domestic expenditure.
- What are the business expectations? The Associated Chinese Chambers of Commerce and Industry of Malaysia's (ACCCIM) Malaysia Business and Economic Conditions Survey indicated that higher respondents (40.6%) expecting "Better" economic outlook in 2H 2024 compared to 28.2% in 1H 2024. Most sectors are cautiously optimistic about their business conditions in 2024, especially in the second half-year.
- Our tracking of high frequency indicators provide a good head start for the year, albeit a weak reading in February, partly due to seasonal festive effects. But, we must keep vigilant about both external and domestic risks, which are roughly balanced. External risks may come from weaker-than-expected external demand, larger declines in commodity production and the escalation of geopolitical conflicts, especially in the Middle East. Meanwhile, domestic risks to growth could come from weaker domestic consumption and slower implementation of existing and new projects.

  a) Malaysia's **leading economic index**, which predicts economic trends for an average of four to six months ahead, bounced back to 0.3% yoy in December 2023, the first positive growth after nine consecutive months of declines. It gained stronger traction to 3.2% growth in January 2024.

  b) **Industrial production** rebounded by 4.3% yoy in January and 3.1% in February (-0.03% in December 2023). It is encouraging that growth in the manufacturing sector has turned around to increase by 3.7% in January and 1.2% in February (-1.4% in December 2023). The domestic-oriented industries expanded by 8.0% and 3.8% in January and February, respectively. Nevertheless, following a positive growth of 1.6% in January 2024, the export-oriented industries dipped by 0.1% in February, marking a return to decline after seven months of contraction in Jun-Dec 2023. Sustained growth was recorded in the electricity and mining sectors.

c) Sales of passenger vehicles jumped 16.2% yoy to 117,373 units in Jan-Feb 2024, due to the year-end rush of deliveries and bargains as well as Chinese New Year campaign, while that of commercial vehicles declined by 13.8% to 10,959 units during the same period.

d) After contracting since June 2023, manufacturing sales value rebounded to 3.2% yoy in January and 0.7% in February 2024, bolstered by the strong growth in the transport equipment & other manufactures sub-sector (11.7% in Jan-Feb 2024), non-metallic mineral products, basic metal & fabricated metal products sub-sector (7.6%), as well as textiles, wearing apparel, leather and footwear (6.1%).

e) Sales value of the wholesale and retail trade grew by 5.4% yoy in Jan-Feb 2024, contributed by all sub-sectors, namely motor vehicles (10.5%), wholesale trade (5.3%), and retail trade (4.2%).

f) **Exports**, which have been contracting at much slower pace in 2H 2023 (-6.9% in 4Q and -15.2% in 3Q), rebounded to 8.7% yoy growth in January (-8.0% in 2023), partly due to the front-loading shipment of exports ahead of the shorter working days in February. This partly explained for causing exports to decline marginally by 0.8% in February and -0.8% in March. Exports increased by 2.2% yoy in Q1 2024. However, the trade balance has narrowed to RM34.2 billion, the lowest level since Movement Control Order (MCO) in Q2 2020.

   We maintain positive export outlook for this year, estimated 4.0% growth (-8.0% in 2023) compared to BNM's estimates of 5.0%, mainly driven by a recovery in demand of electronics and electrical products as well as firming commodity and crude oil prices. BNM estimated crude palm oil price at RM4,200-RM4,400/tonne in 2024 (RM3,832/tonne in 2023) while Brent crude oil (US$80-US$90 per barrel in 2024 vs. US$83 per barrel in 2023).

g) **Imports serve as a leading indicator of the economy in terms of production, investment and consumption**. Imports grew by 13.1% in Q1. The expansion of intermediate (15.0% in Q1) and capital goods (47.0% in Q1) presages continued growth in production, exports and investment activities. Meanwhile, import of consumption goods remained strong (14.6% in Q1) on sustaining household consumption.

- While the recovery in external demand will support the economy, can consumer spending (60.8% of total GDP) continue to hold firm? We take a cautious view on private consumption growth (estimated 4.6% in 2024 vs. 4.7% in 2023 and +7.1% pa in 2011-2019) compared to BNM's 5.7%.

- **Consumers will be more cautious on discretionary spending**. The dampening factors are 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.

- Nevertheless, **stable employment growth (estimated jobless rate at 3.3% in 2024) and moderate wage growth as well as the introduction of the Flexible Account (Account 3) of the Employee Provident Fund (EPF) in May 2024 will support consumer spending**. It was observed that real wage growth (nominal wages adjusted for inflation) of the manufacturing and services sectors have been moderating in recent quarters to 1.3% and 1.7% in Q4 2023, respectively (2.4% and 6.7% respectively in Q2 2022). Additionally, 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.

- **Catalysts for private investment growth have to be sustained**. 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 more than 85% of manufacturing projects approved in 2021 to 2023 being implemented. We caution that increasing business operating costs and high cost of raw materials would dampen the business spending by small and medium enterprises (SMEs).

- **Headline inflation has been moderating** since April 2023 to 1.5% in December 2023, bringing to an average of 2.5% in 2023. Core inflation also trended lower, albeit at slower pace to average 3.0% in 2023 (3.0% in 2022). Headline inflation increased to 1.8% in February 2024 (1.5% in January), partly due to higher water and sewerage charges. Core inflation stood at 1.8% in both January and February.

- Inflation is much "sticker" in services-oriented businesses, particularly because of the heavier labour cost and other operating costs. These include restaurant and accommodation, health as well as personal care, social protection and miscellaneous price inflation.

- Bank Negara Malaysia remains cautious about the inflation outlook in 2024 (estimated 2.0%-3.5% vs. SERC's 2.8%-3.5%) on the anticipated policy changes in domestic fuel subsidy rationalisation as well as the development in exchange rates and global commodity market.

- Direct exchange rate pass-through to imports is evident, whereby 40% of exchange rate depreciation is translated to overall import prices. BNM 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. It 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%.

- We support BNM's short-term efforts through moral suasion requesting the exporters, corporates, GLCs and GLICs to repatriate their realised income and export proceeds abroad and convert into the Ringgit, and do not hold foreign exchange above normal level, to help stabilise the Ringgit.

- The Government must remain committed towards undertaking structural institutional and economic reforms to strengthen its fiscal position and contain debt level to boost the nation's productivity and competitiveness, enhance better investment climate to retain domestic investment and attract more high quality FDI, improve education outcomes, enhance manpower skillsets, accelerate the climate transition, and make growth more inclusive by 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, our own people and investors' confidence, relative competitiveness in terms of trade, as well as the capital movements in terms of real rate of return on investment.

- While the Ringgit exchange rate is determined by numerous complex external and domestic factors, the Government has to show its credibility in delivering the promised reforms, and 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.

<u>Spotlight on the Impact of an Escalation of Military Conflict in the Middle East on Malaysia</u>

- The military conflicts are high in the Middle East. An escalation into a full-scale war could send volatility in global commodity, energy and minerals markets, financial and foreign exchange markets. Year-to-date, Brent crude oil prices have risen by 12.9% to USD87.72/bbl on 19 April (averaged USD82.92 per barrel in Q1 2024) compared from USD77.69/bbl on 29 December 2023.

- It is a relief that the G7 major powers said they are committed to de-escalating the conflict between Israel and Iran.

<u>How would Higher Oil Prices Impact the Global Economy?</u>

- Price shocks that increase the price of oil tend to disrupt consumption, production, and GDP growth as well as raise domestic inflation. The transmission impact of an oil price shock on the global economy depends on several factors as follows:

  - **First**, is the size of an oil price shock, the durability of the shock and its perceived duration;

  - **Second**, the prevailing global economic conditions and political environment;

  - **Third**, the level of energy intensity; energy-intensive countries will feel a shock more than ones that do not heavily rely on oil; and

  - **Finally**, the policy responses (fiscal and monetary) of policymakers and central banks.

<u>How would Higher Oil Prices Impact the Malaysian Economy?</u>

(i) **<u>Trade channel</u>**

- In 2023, exports of crude oil made up 2.0% of total exports (RM28.7 billion); liquefied natural gas (LNG) (4.2% or RM59.6 billion) and petroleum products (10.1% or RM143.5 billion). Malaysia has been a net importer of crude oil in 2022-2023 amid declining crude oil production over the years (average 535,104 barrels per day in 2020-2023 vs. 663,091 barrels per day in 2016-2019). The crude oil trade balance registered a deficit of RM32.2 billion or 1.8% GDP in 2023 (-RM21.1 bn or 1.2% of GDP in 2022), compared to an average surplus of RM9.8 billion per year in 2000-2021.

- In contrast, the LNG has incurred trade surplus of averaging RM55.5 billion per year or 3.1% GDP in 2022-2023 while petroleum products also generated a surplus of averaging RM10.6 billion or 0.6% of GDP in 2022-2023. Overall, the trade balance for oil and gas (O&G), which consists of crude oil, LNG and petroleum products, remains in healthy surplus of averaging RM39.4 billion per year or 2.2% GDP in 2022-2023. As a result, higher oil prices should be positive for Malaysia's O&G exports.

- Nevertheless, the supply oil shocks, slower consumer spending and investment demand due to higher oil prices and inflation would temper the global economy, especially the oil importing countries. As a result, Malaysia's exports will be impacted via second order effect.

- Additionally, the immediate concerns are the disruption of trade routes in the region. Iran and Israel share a strategic location near important shipping routes, especially in the Eastern Mediterranean, Red Sea and the Persian Gulf region. As a result, supply chain disruptions, higher costs, and delays in global trade flows could be impacted by the shutdown or increased risk of these crucial waterways or even airways resulting from conflict in these areas.

(ii) **Financial channel**

- During the periods of high oil prices, investors usually become more uncertain about the economic and inflation outlook, and their impact on corporate earnings which, in turn, may lead to higher equity risk premia, putting additional downward pressure on stock prices. The volatility in global stock markets will generate volatility spillover on Malaysia's equity market, especially the risk adverse foreign investors would seek shelter in safe-haven assets such as foreign bonds, foreign currencies and gold to hedge against inflation.

(iii) **Domestic prices channel**

- There are two spillover transmission channels on Malaysia's inflation via imported inflation and fuel subsidy rationalisation.

- The share of import content in domestic consumption is approximately 26%. Compounding the impact of imported price inflation due to higher oil prices is the persistent weakening Ringgit. Direct exchange rate pass-through to imports is evident, whereby 40% of exchange rate depreciation is translated to overall import prices. BNM estimated that a change in 5% in the RM/USD will result in core inflation to increase by 0.2 percentage points. The impact could be larger amid prolonged depreciation, particularly for key necessities with high import content such as food and beverages, restaurants and hotels (7%) and transportation (5%).

- The direct impact on headline inflation via the transport price component of the CPI basket, which carries a weightage of 11.3%. Of the "Transport" component, diesel and petrol carries a weightage of 0.2% and 5.5%, respectively. Every 10% increase in petrol retail price is estimated to contribute about 0.55 percentage points to the headline inflation. Currently, RON95 and diesel retail prices are capped at RM2.05/litre and RM2.15/litre, respectively despite Brent crude prices have increased by 12.9% to USD87.72/bbl as of 19 April 2024 compared to USD77.69/bbl on 29 December 2023.

- As we expect the targeted fuel subsidy rationalisation will not lead to a complete floating of the retail petrol prices, rather a gradual adjustment in the pump price of RON95, the impact on headline inflation will be manageable though the indirect impact arising from increases in prices of other goods and services could mean higher inflation rate.

(iv) **Budget deficit**

- The 2024 Budget was based on estimated crude oil price of US$85/bbl. For every USD10/bbl increase in oil price, fuel subsidies are projected to increase by RM4.7 billion per year while the oil-related revenue will increase by RM3.0-3.5 billion, resulting overall fiscal balance to deteriorate by RM1.2-1.7 billion or 0.06%-0.09% of GDP. However, the Federal government is expected to make some re-ordering of spending priorities to keep the fiscal deficit target of 4.3% of GDP in 2024 (-5.0% of GDP in 2023).

(v) **Interest rate**

- Given the implementation of a gradual targeted fuel subsidy rationalisation and also largely cost-driven inflation, which itself will act to moderate consumer spending, Bank Negara Malaysia is unlikely to raise interest rate to act on an increase in inflation.

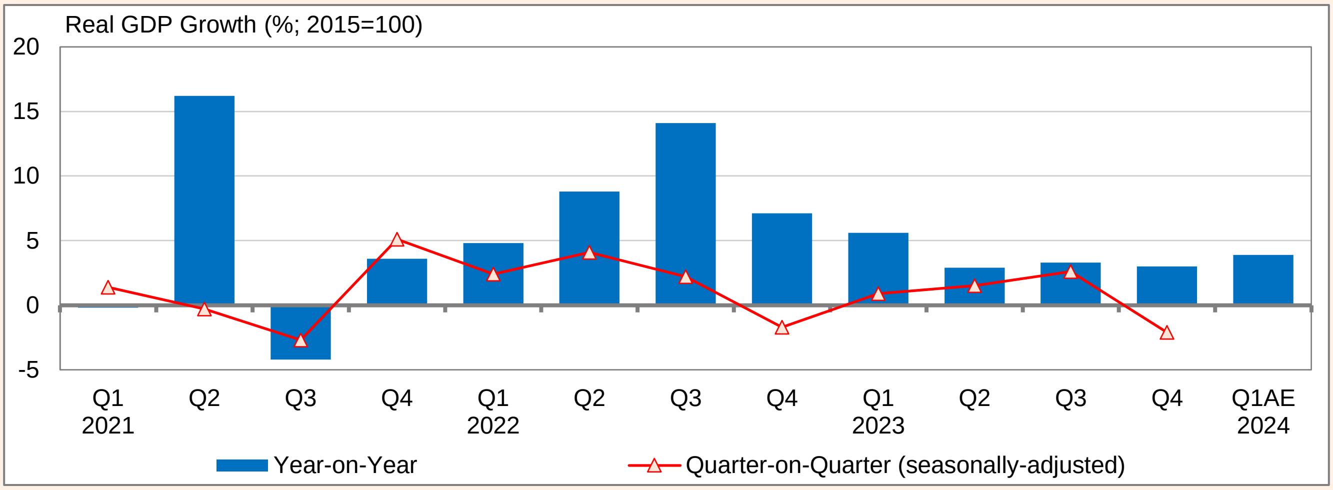
Real GDP growth (%, Y-o-Y)

Economic Sector [% share to GDP in 2023]	2022	2023	2023 Q1	2023 Q2	2023 Q3	2023 Q4	2024F (BNM)	2024F (SERC)
By kind of economic activity								
Agriculture [6.4%]	0.1	0.7	1.0	-1.0	0.9	1.9	-0.5	1.3
Mining & Quarrying [6.2%]	2.6	1.0	2.4	-2.3	-0.1	3.8	3.5	1.4
Manufacturing [23.4%]	8.1	0.7	3.2	0.1	-0.1	-0.3	3.5	3.9
Construction [3.6%]	5.0	6.1	7.4	6.2	7.2	3.6	6.7	7.2
Services [59.2%]	10.9	5.3	7.3	4.7	5.0	4.2	5.5	5.3
By type of expenditure								
Private Consumption [60.2%]	11.2	4.7	5.9	4.3	4.6	4.2	5.7	4.6
Public Consumption [13.2%]	4.5	3.9	-2.2	3.8	5.8	7.3	3.2	2.6
Private Investment [15.3%]	7.2	4.6	4.7	5.1	4.5	4.0	6.1	5.5
Public Investment [4.4%]	5.3	8.6	5.7	7.9	7.5	11.3	6.2	7.0
Exports of Goods and Services [74.6%]	14.5	-7.9	-3.3	-9.4	-12.0	-6.3	4.0	4.1
Imports of Goods and Services [69.1%]	15.9	-7.6	-6.5	-9.7	-11.1	-2.9	4.1	3.9
Overall GDP	**8.7**	3.7	5.6	2.9	3.3	3.0	**4.0-5.0***	**4.5**

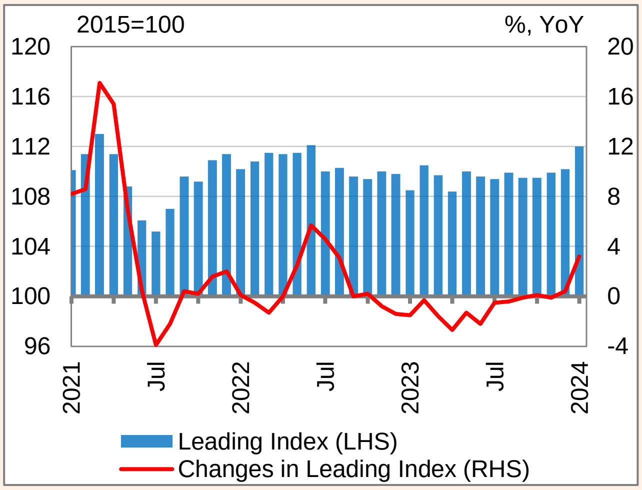
** BNM's mid-point estimate is set at 4.5%.*
Source: Department of Statistics, Malaysia (DOSM); BNM and SERC's forecasts

Spotlight on the Malaysian Economy

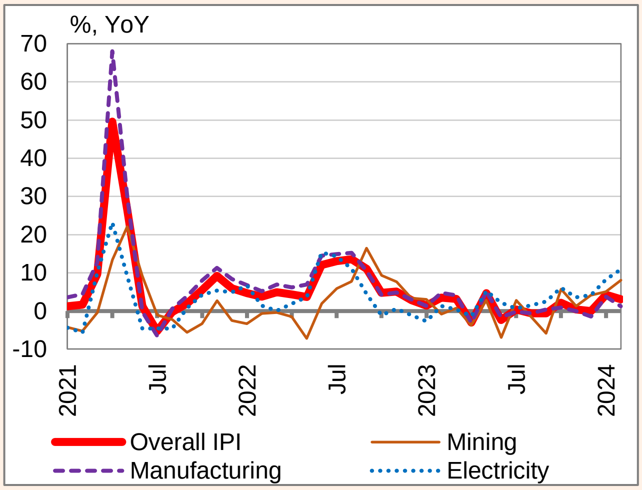
Malaysia's advance estimates GDP growth of 3.9% yoy in Q1 2024, supported by the services and construction sectors as well as turnaround in the manufacturing sector.



Leading Index (LI) signalled an encouraging performance ahead

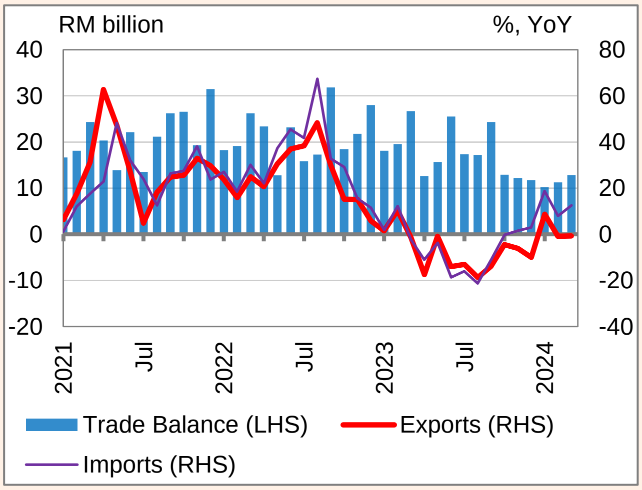


Industrial production grew in Jan-Feb, supported by all industrial sub-sectors

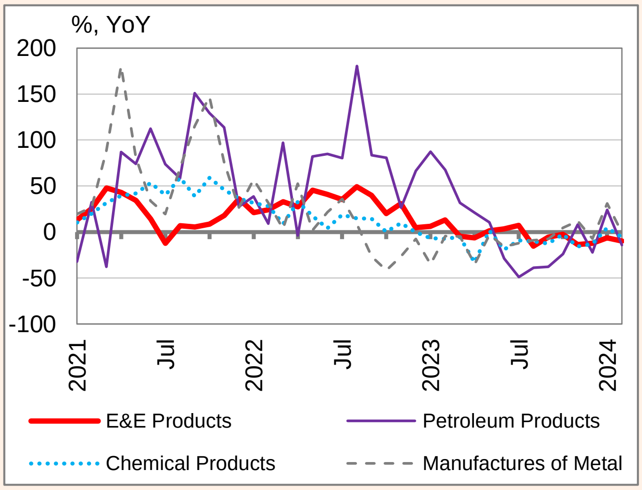


External Sector

Exports contracted by 0.8% each in Feb-Mar; trade balance remained low

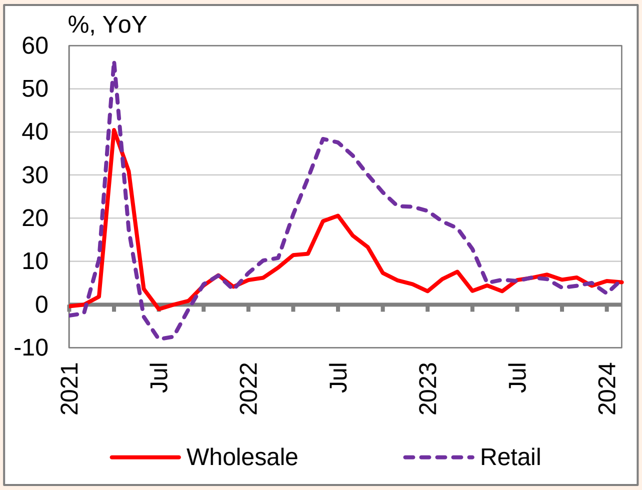


Exports by major products

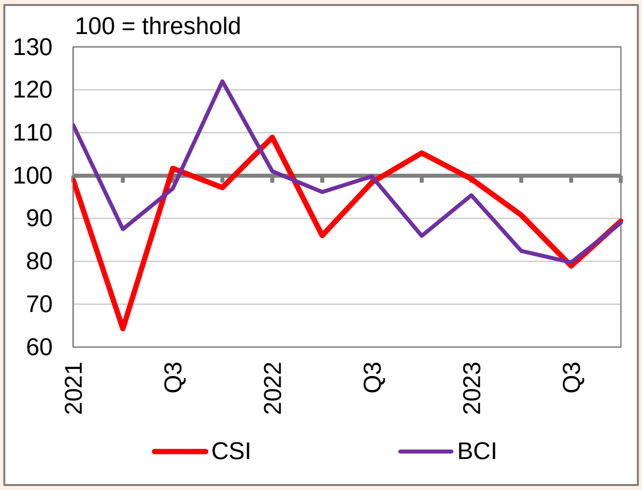


Domestic Demand

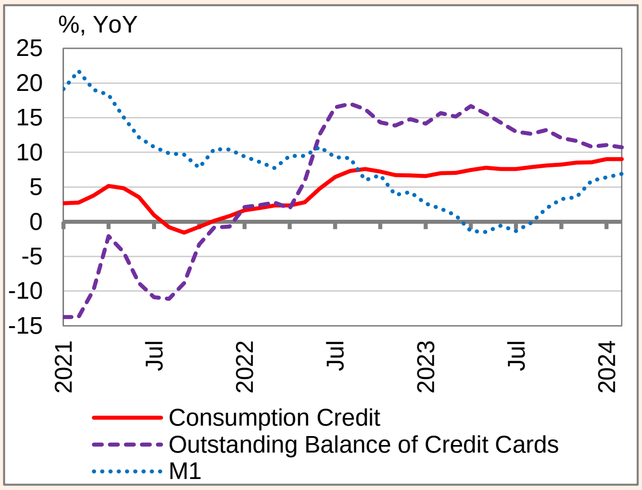
Both wholesale and retail sales growth remained intact



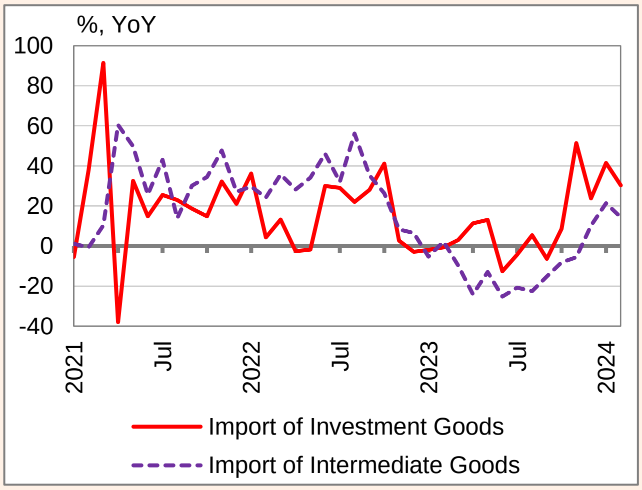
Both consumers sentiments and businesses conditions still below optimism threshold



Selected private consumption indicators

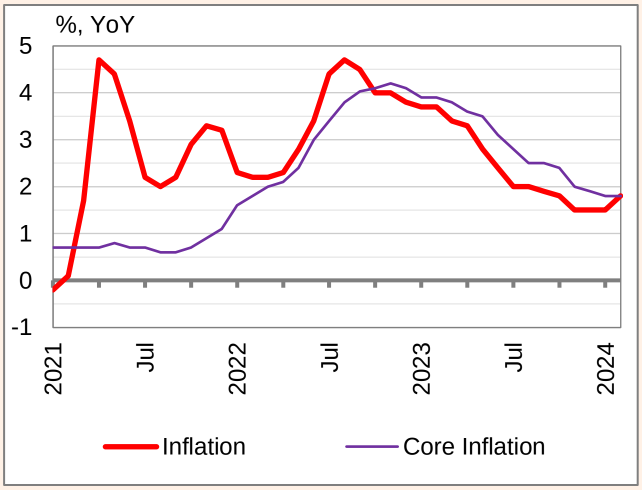


Selected private investment indicators

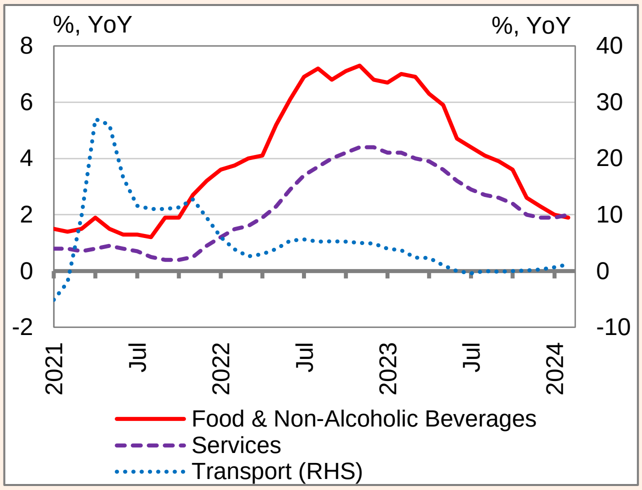


Price Indicators and Labour Market

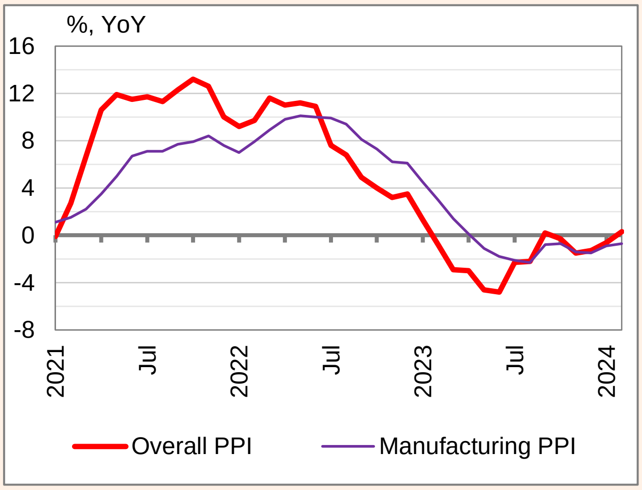
Headline inflation increased in Feb, partly due to higher water and sewerage charges



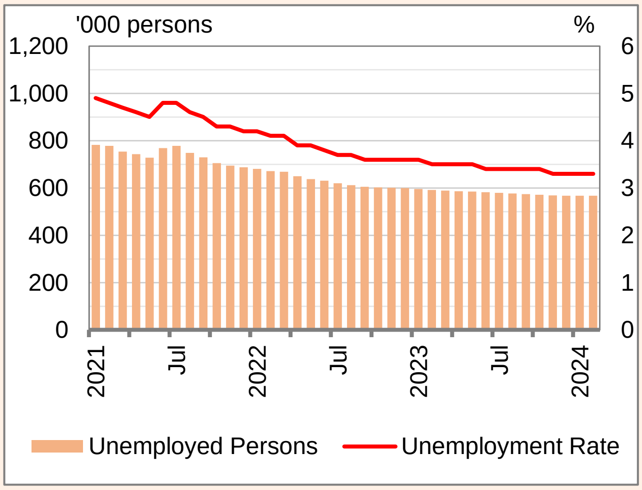
Food inflationary pressures eased; food prices away from home still high



Producer prices have normalised; may increase on higher commodity prices

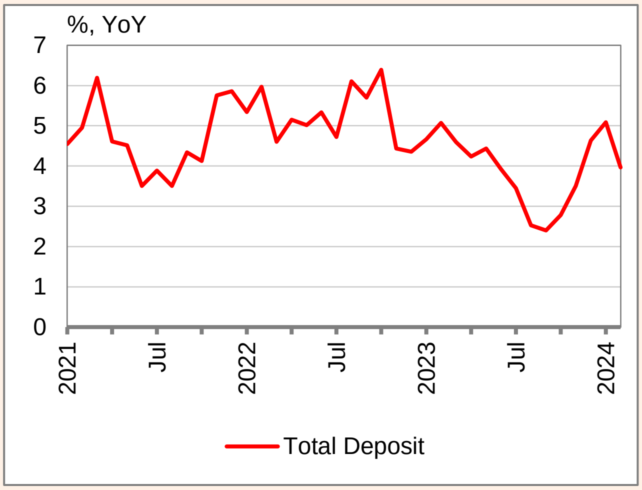


Unemployment rate remained healthy at 3.3% for four consecutive month in Feb

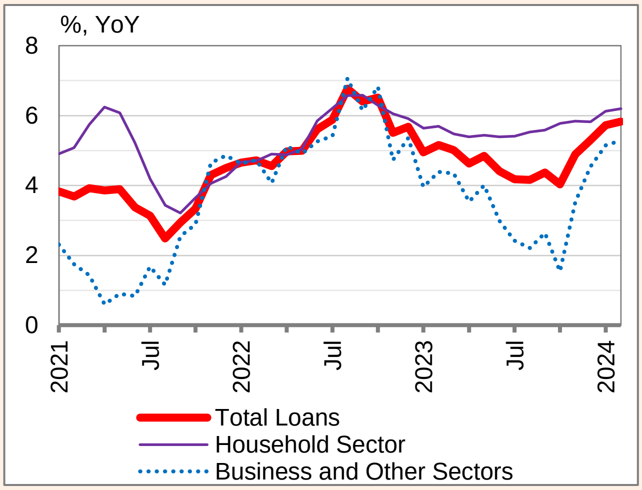


Banking and Financial Indicators

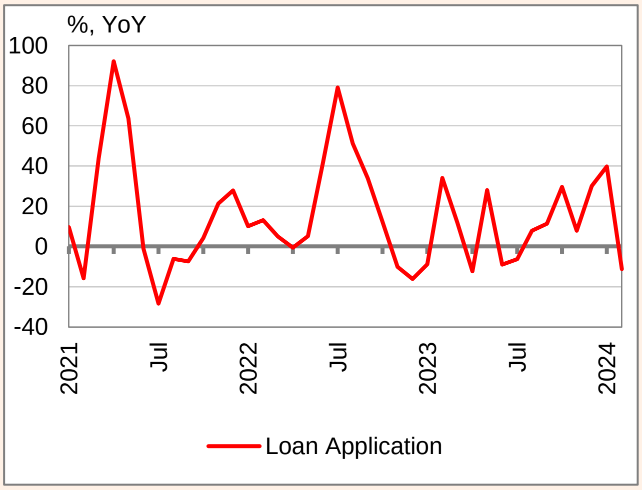
Banking deposit growth eased a little in Feb



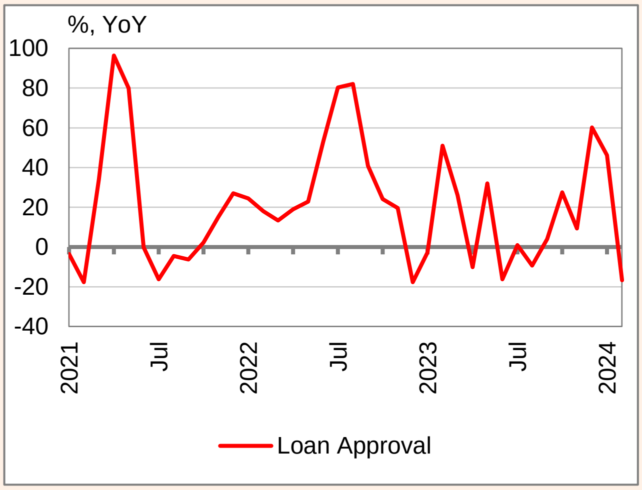
Higher households loan for purchase of residential properties and cars, personal use



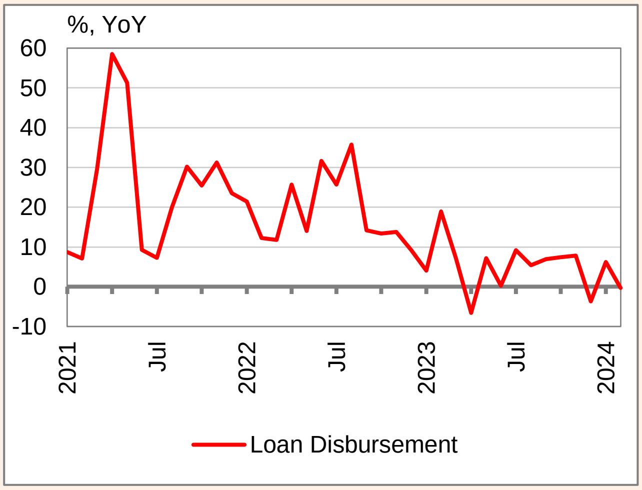
Loan applications growth



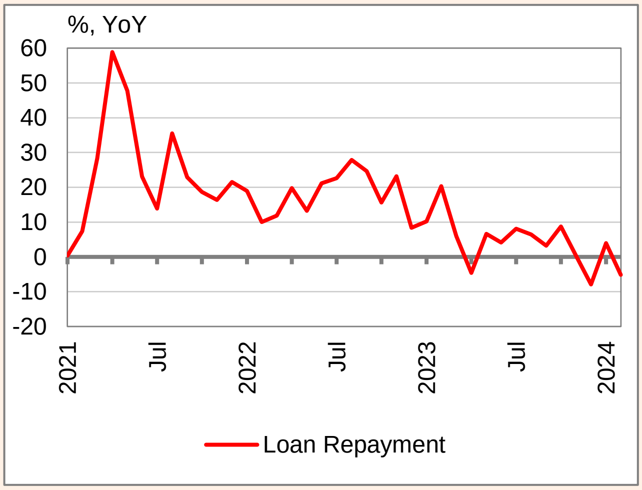
Loan approvals growth



Loan disbursements growth

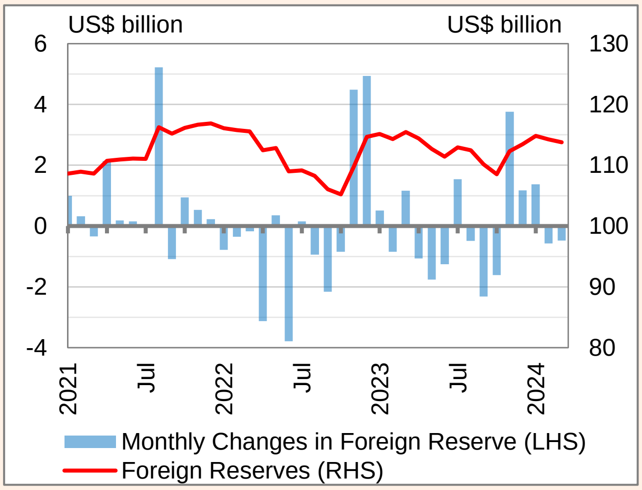


Loan repayments growth

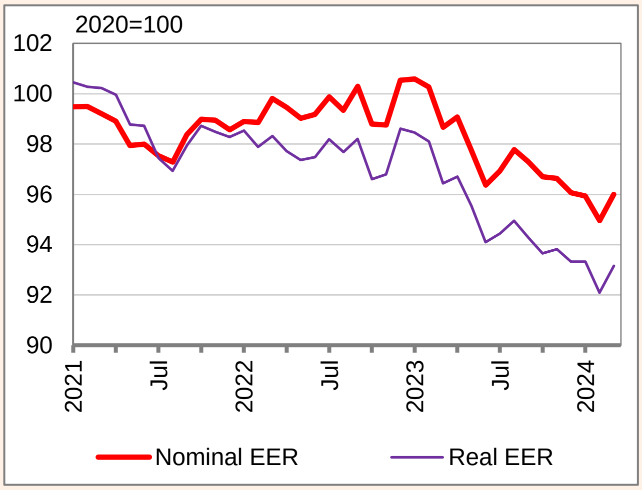


Note:: Loan data from July 2022 onwards was revised and expanded based on the latest requirements with more accurate data definition and reporting methodology. Outstanding loan excludes DFI.

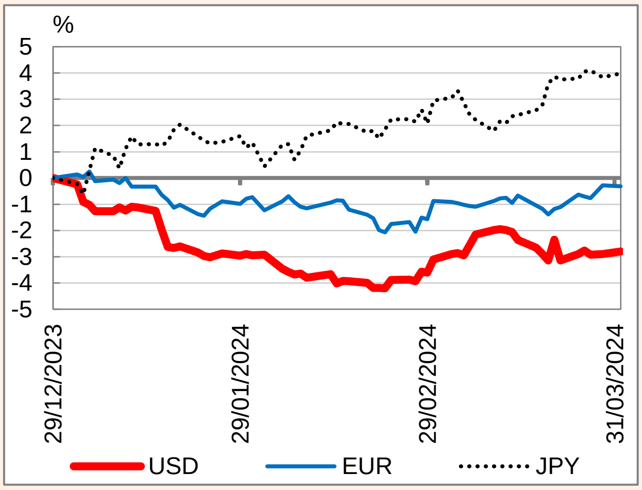
Foreign reserves declined for two consecutive months to US$113.8bn in Mar



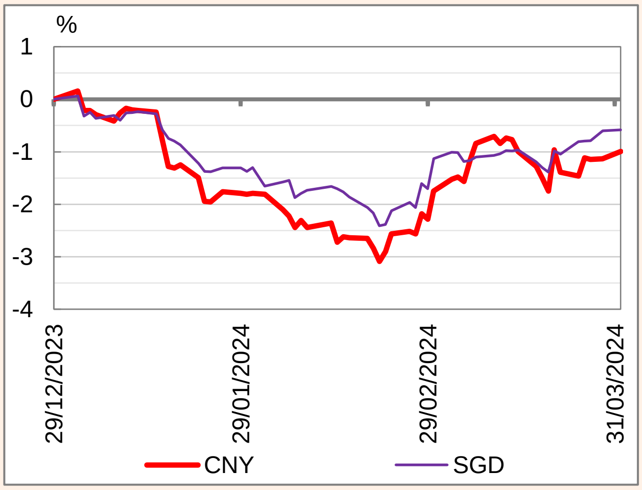
Ringgit's Effective Exchange Rate (EER)



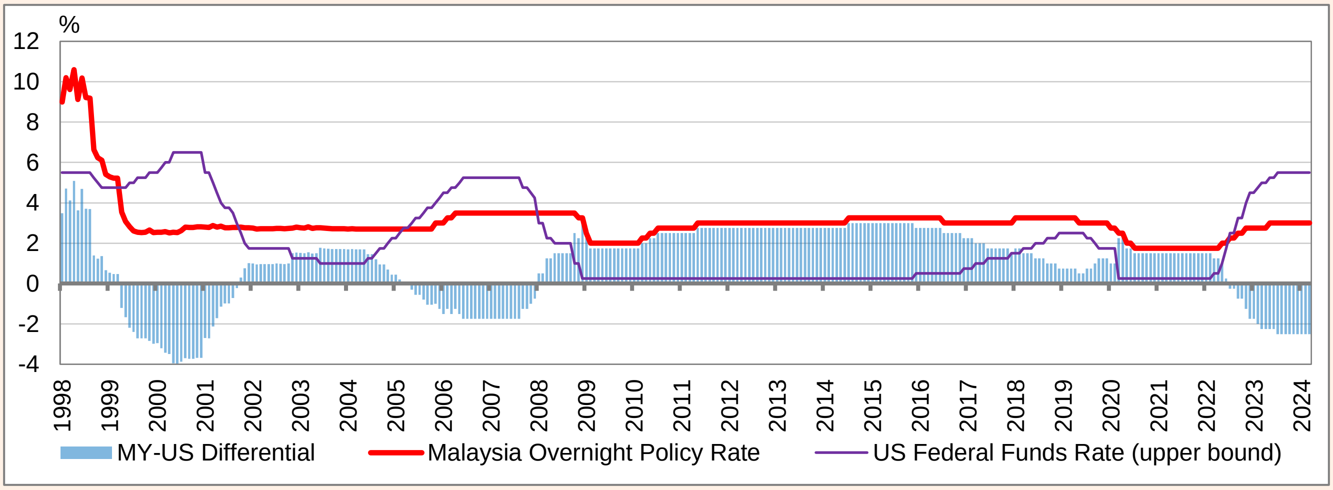
The Ringgit against the US dollar, euro and Japanese yen



The Ringgit against the Chinese renminbi and Singapore dollar



Malaysia-US's interest rate differentials



Source: Department of Statistics, Malaysia (DOSM); Malaysian Institute of Economic Research (MIER); Bank Negara Malaysia (BNM); Bank for International Settlements; Federal Reserve

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About SERC

The Associated Chinese Chambers of Commerce and Industry of Malaysia (ACCCIM)'s Socio-Economic Research Centre (SERC Sdn. Bhd.) was established as an independent and non-profit think tank on 19 October 2010. Officiated by YAB Prime Minister on 28 April 2011, SERC is funded by ACCCIM SERC Trust.

SERC is tasked with carrying out in-depth research and analysis on a wide range of economic, business and social issues in support of the formulation of public policies to shape Malaysia's national socio-economic and industrial development agenda.

The organisation will identify and explore issues and future trends that impact domestic economic and business environments. It will also focus on sharing knowledge and promoting public understanding of socio-economic issues of national importance.

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