ALLIANCEDBS RESEARCH

Economic Focus

Solid growth momentum

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- **Strong growth momentum to sustain in 2H2024, underpinned by robust investment activities, firm household spending and improving exports**
- **Fed's monetary-easing cycle to spur more foreign fund inflows into Malaysia**
- **We are positive of 2024 growth prospects and expect 4.7% GDP growth**

Strong fundamentals

Our conviction of Malaysia being on the cusp of a multi-year growth cycle has been further strengthened by the stronger-than-expected 1H2024 GDP growth of 5.1%, thanks to the sustained domestic demand and a turnaround in external trade. We believe this solid growth trajectory is likely to remain intact in 2H24 given sustained consumer spending, robust investment activities and improving external trade. This is also corroborated by latest economic stats including retail sales, industrial production and total exports which are all suggesting upbeat prospects in the near term. Meanwhile, domestic demand will remain supported by robust labour market conditions as unemployment rate improved to 3.3% in Jul 2024 (vs 3.4% in Jul 2023) with historic high labour force participation rate of 70.4%.

Rising foreign interest in Malaysia

Malaysia's strong growth prospects have not gone unnoticed by the international financial markets as Ringgit emerged as one of the Asia's best-performing currency after rallying by 9% YTD, amid a surge in inflows of foreign funds and investments into the ASEAN region. A confluence of tailwinds including Fed rate cuts, on-going Madani government reforms and pro-business strategic policies under a stable ruling coalition has contributed significantly to the rising foreign interest in Malaysia. After achieving record high approved investments in 2021-2023, the winning streak has continued unabated in 2024 with the figures rising 18% y-o-y to RM160bn in 1H2024, outpacing the government's full-year target of 5%. This signifies the strong confidence that foreign investors have in Malaysia, a traditionally non-aligned country which is expected to benefit from the incessant US-China tensions.

All eyes on Budget 2025 in Oct 2024

The unveiling of Budget 2025 on 18 Oct 2024 will likely be positive for Malaysia's economy as the government is expected to strive toward achieving its socioeconomic goals under the Madani Economy Framework, as guided in its pre-budget statement. Progress on fiscal consolidation including details on further subsidy rationalisation and updates on tax revenue expansion under a better governance framework will be closely followed by the financial market. A narrower 2025 budget deficit is expected, compared to 4.3% in 2024 and 5% in 2023 as part of its plan to achieve 3% deficit in the medium term. Development expenditure is likely to be given a record high allocation to pump prime the economy given the intensified efforts to make Malaysia a world-class investment destination, especially in high value-added industries focusing on digitalisation and energy transition.

Growth momentum remains intact

We remain optimistic of Malaysia's economic outlook which is expected to grow by 4.7% in 2024 – in line with government's forecast of 4%-5%. Fundamentals remain strong as Malaysia's economy continues to take comfort from its resilient domestic demand, underpinned by sustained household spending. Private investment is expected to benefit from improved external environment and positive response to the NETR and NIMP 2030 while the government continues with its expansionary fiscal policy to drive economic growth. Key downside risks include slower-than-expected recovery in external demand and heightened geopolitical tensions.

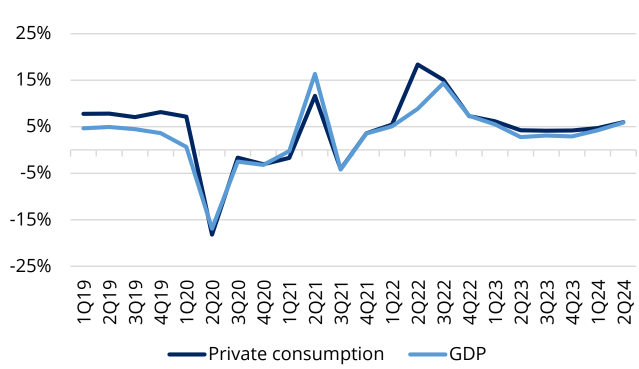
Madani Economy outperforms in 1H2024

We expect Malaysia to register a stronger GDP growth of 4.7% in 2024 after a relatively weaker growth of 3.6% in 2023. This is also in line with the government's 2024 GDP growth projection of 4.0%-5.0%. Private consumption, accounting for 60% of our economy, will continue to deliver satisfactory performance for Malaysia's economy, underpinned by robust labour market and strong economic and social activities, especially the tourism-related activities.

Malaysia's economy grew 5.9% y-o-y and 2.9% q-o-q on a seasonally adjusted (SA) basis in 2Q24 (1Q24: +4.2% y-o-y; 1.5% SA q-o-q), which was slightly above the advance estimate of 5.8%. The higher-than-expected 2Q24 GDP was largely driven by strong growth trajectory that further accelerated during the quarter, especially in the Services, Manufacturing and Construction sectors.

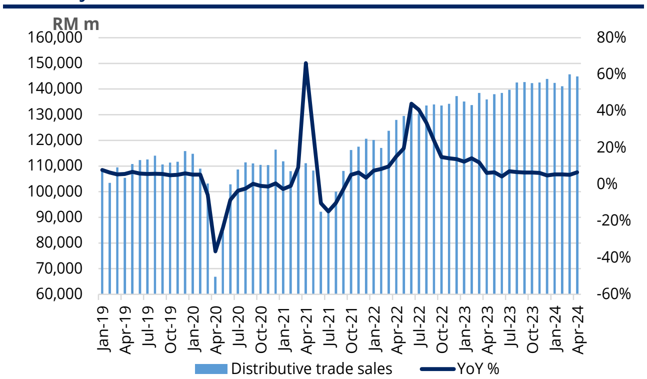
We believe the resilient household spending is likely to continue, in tandem with the continued recovery in the labour market. Meanwhile, the implementation of new and existing investment projects under the NETR and the NIMP 2030 are expected to have a positive impact to economic growth as more investment are expected from both domestic and foreign investors.

Malaysia's GDP growth



Source: AllianceDBS, CEIC

Monthly distributive trade sales



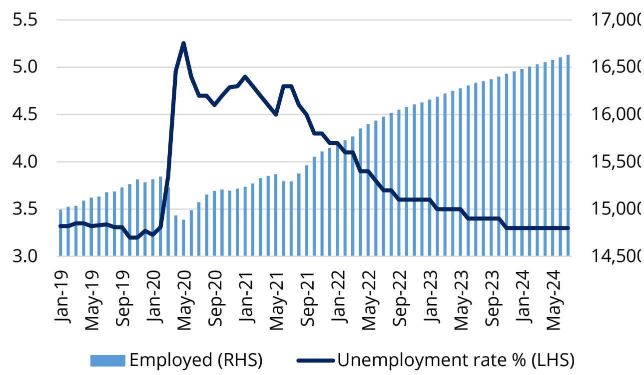
Source: AllianceDBS, CEIC

Robust labour market condition

Malaysia's economic growth momentum will continue to be underpinned by the robust employment market which has been growing from strength to strength. Malaysia's unemployment rate in Jul 2024 came in at 3.3%, which is rather impressive considering our growing workforce. Notably, we are encouraged by the continuous growth in employment market outpacing the growth in labour force, lifting the labour participation rate to a record high of 70.4% in Apr 2024. This will certainly bode well for the economic outlook in 2024 given that domestic demand forms the bulk of our economy.

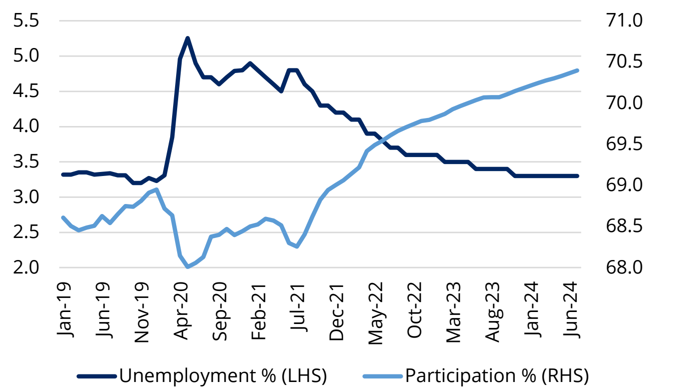
Going by the healthy growth momentum expected in 2024, the robust labour market condition will ensure that the growing working-age population is met with higher employment opportunities. We believe Malaysia's unemployment rate will continue to remain low as more jobs are created with the realization of various investment activities.

Strong labour market



Source: AllianceDBS, CEIC

Favourable labour market dynamics



Source: AllianceDBS, CEIC

New growth driver from investment spending

Madani Economy Framework has started the ball rolling on kickstarting the economic transformation that is long overdue to move up the industrial value chain in Malaysia. NETR and NIMP 2030 have provided the key government framework to drive high value-adding industrialisation and green economy which will ultimately enable Malaysia to build a high-income economy if the well-curated strategic directions are successfully executed.

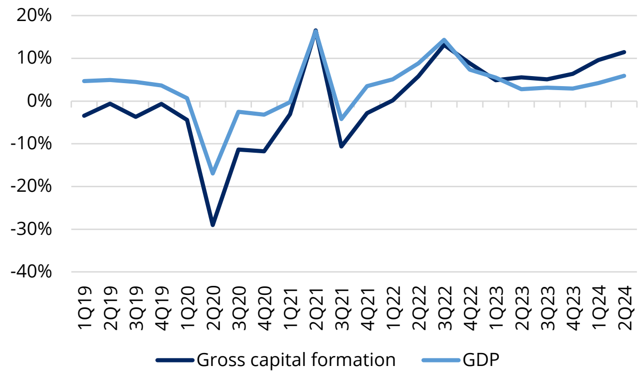
Indeed, the proactive strategy adopted by the government to revitalize the domestic economy has started to bear results as 1H24 capital expenditure surged to a multi-year high growth of 10.6%. The positive impact arising from record-high approved investments in 2021-2023 and various government-led strategic developments under national blueprints is expected to provide further tailwinds in the subsequent quarters.

More importantly, after achieving record high approved investments in 2021-2023, the winning streak has continued unabated in 2024 with the figures rising 18% y-o-y to RM160bn in 1H2024, outpacing the government's full-year target of 5%. This signifies the strong confidence that foreign investors have in Malaysia, a traditionally non-aligned country which is expected to benefit from the incessant US-China tensions, indirectly helping to uplift Malaysia's industrial capabilities and boost its value-adding exports

The NIMP 2030 particularly is poised to enhance the competitiveness of Malaysia's manufacturing industry, leveraging on the global trend of "China + 1" strategy for industrial value chain diversification. In fact, the heightened US-China trade tensions has benefitted not only Malaysia but the entire ASEAN as a whole given the attractive value proposition offered.

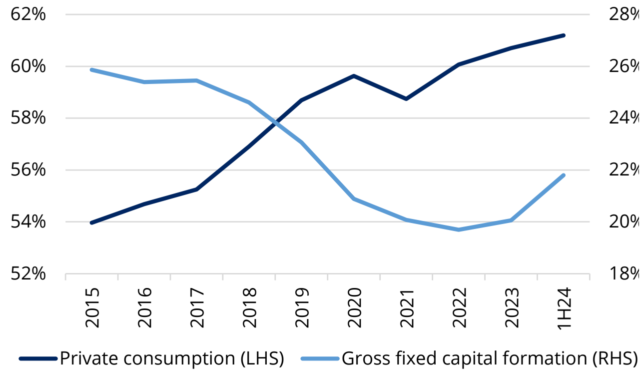
In addition, the government has recently launched the National Semiconductor Strategy with a government allocation of RM25bn which is aimed at further advancing the development of semiconductor ecosystem, moving up the value chain to capture a larger share of global investments. Therefore, it is no surprise that globally renowned technology giants such as Infineon AG, Nvidia, Microsoft and Google have all committed to step up their investments in Malaysia which will help to cement Malaysia's global position as one of the world's key semiconductor hubs.

GDP vs gross capital formation



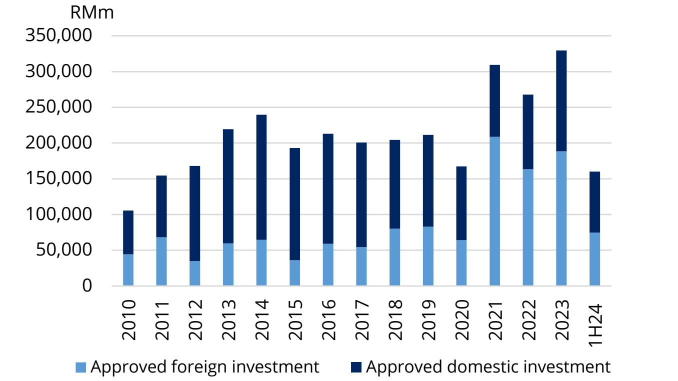
Source: AllianceDBS, BNM, CEIC

GDP share of consumption vs investment



Source: AllianceDBS, BNM, CEIC

Record-high approved investments over 2021-1H2024



Source: AllianceDBS, BNM, CEIC

Notable government projects

Project	Investment RMbn	Timeline
MRT 3	45.0	from 2024
Penang LRT	10.0	from 2024
Flood mitigation	11.8	2024
Pan Borneo Sabah phase 1B	15.7	2024
Sarawak-Sabah Link Road 2	7.4	2024
LRT 3 expansion	4.7	2024-2025
ECRL	50.0	2018-2026
Johor-SG RTS	3.7	2018-2026
My Digital 5G	16.5	2021-2031
Pan Borneo Sabah phase 1A	16.0	2016-2024
Johor BRT	2.5	2023-2025

Source: AllianceDBS, MoF

Meanwhile, the government is also committed to revive the economic growth by undertaking various large-scale infrastructure projects which will create positive spillover effects to the local businesses. Some of the major projects announced in Budget 2024 include RM10bn Penang LRT, RM11.8bn flood mitigation projects, RM 15.7bn Pan Borneo Sabah phase 1B and RM4.7bn LRT 3 expansion. We believe there will be more progress on the RM45bn MRT 3 in 2025 which will be an added impetus for Malaysia's economy. All these come on top of the existing mega projects including the likes of RM50bn ECRL and RM3.7bn Johor-Singapore RTS which have progressed well so far.

External trade recovery in full swing

The anticipated recovery in external trade since early 2024 has now come into realisation as Malaysia's 8M2024 exports and imports rose 6% and 17% respectively. We believe the prospects for external trade in 2H2024 should come in stronger as Malaysia benefits from the global technology upcycle given our entrenched position in the global semiconductor supply chain, especially in the packaging, assembly, and testing services.

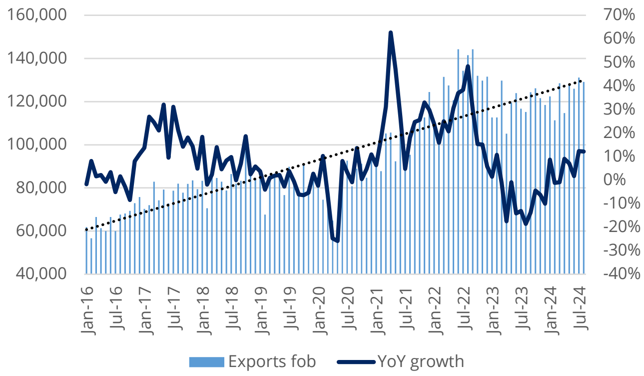
Notably, we have started to see the domestic E&E industry benefitting from the global tech cycle rebound. The improving trend of global semiconductor shipments as well as positive trade data among key Asian trading hubs will continue to spill over to Malaysia given our deep integration with the global supply chain. The de-globalisation trend, especially in the technology sector, will also result in more capital spending as countries rush to ensure supply security.

In addition, continued recovery in tourist arrivals which stood at c.93% of pre-pandemic levels in 2Q24 will also contribute to better exports, supported by higher flight connectivity and visa exemptions. Meanwhile, Malaysia's strategic push to leverage on the global trend of "China + 1" industrial value chain diversification has been reflected in the record high approved investments in 2021-2023, helping to uplift Malaysia's industrial capabilities and boost its value-adding exports.

Most of the key exporting countries in Asia continue to register improved numbers over the past few months, thanks to the resilient global economy. The beginning of the Fed monetary-easing cycle may help to ensure external trade remains on a healthy trajectory as more central banks globally are expected to follow suit in pursuing an accommodative monetary policy.

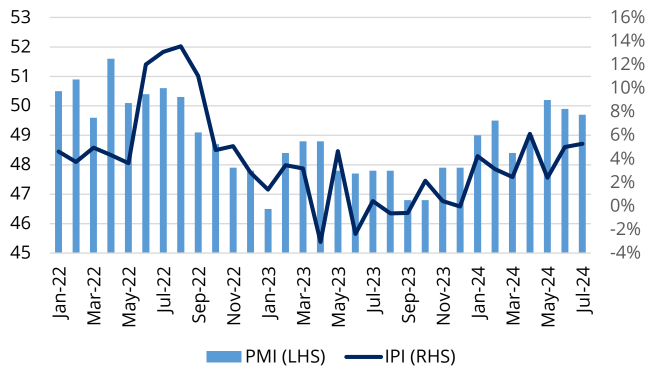
Therefore, we believe that the manufacturing sector, contributing ~23% of GDP, is expected to recover as well, in tandem with the improvement anticipated for external demand. This is corroborated by positive data from manufacturing PMI, industrial production as well as business confidence levels. In addition, the upticks in business loans since the end of 2023 lends further credence to our view that the manufacturing sector will have a better prospect this year.

Malaysia's monthly exports growth is recovering



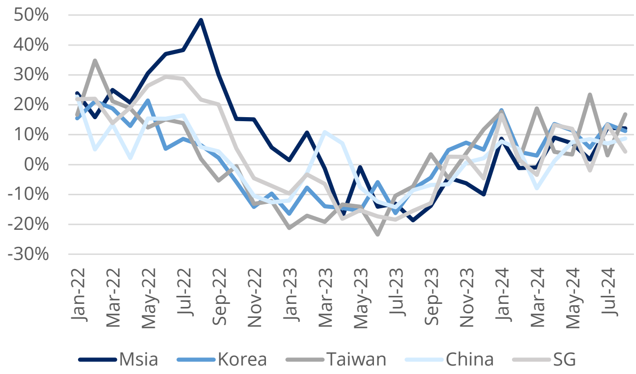
Source: AllianceDBS, CEIC

Industrial production is picking up



Source: AllianceDBS, CEIC

Strong exports growth for key Asian exporters

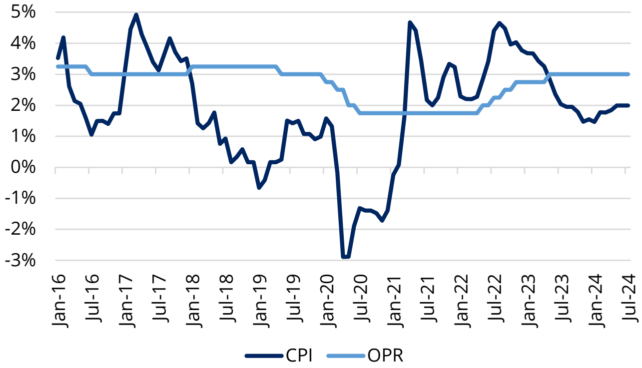


Source: AllianceDBS, CEIC

Strong loans growth momentum

Bank Negara Malaysia has been maintaining the current OPR rate of 3% which is similar to its pre-pandemic level. We believe that BNM will remain with this slightly accommodative interest rate in 2024 as the current monetary policy remains conducive to sustainable economic growth amid price stability.

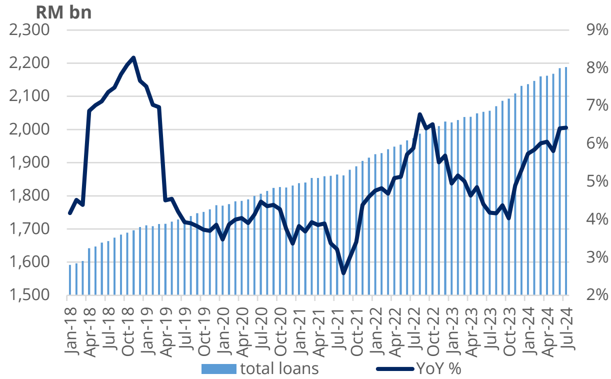
Interest rate vs inflation



Source: AllianceDBS, DOSM, CEIC

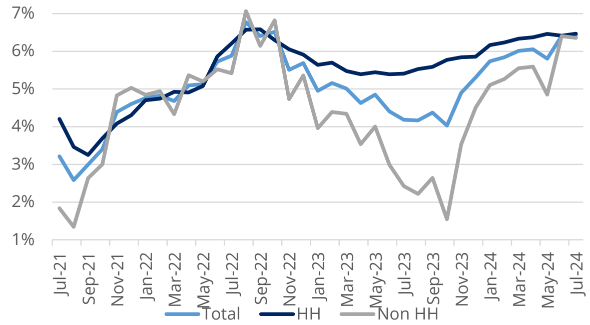
Our headline inflation has been moderating over the course of 2024, in tandem with the moderating trend of commodity prices due to demand concerns from major economies. Therefore, the positive real rates are likely to continue in the near term. Going forward, inflation outlook will be largely swayed by the global commodity price developments as well as the implementation of petrol subsidy rationalisation.

Accelerating banking system loans growth



Source: AllianceDBS, BNM

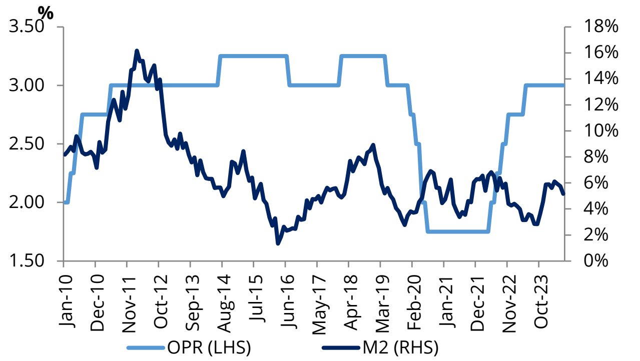
Loans growth picking up strongly



Source: AllianceDBS, BNM

Meanwhile, Malaysia's banking system has been reporting rising loans growth for six months consecutively since the low of 4% in Oct 2023. Loans growth came in strongly at 6.4% in Jul 2024, similar to the level experienced in the aftermath of post-pandemic economic reopening. Positively, business loans rebounded, suggesting that overall business operating environment has started to pick up. On the other hand, the positive landscape of the property sector continues to bolster the loans growth for the household segment.

Normalising liquidity condition in the economy



Source: AllianceDBS, BNM

Meanwhile, M2 money supply continues to grow at a healthy level of 5.3% in Jul 2024 (vs 3.5% in Jul 2023), as the domestic economy grows steadily. It is likely that the domestic liquidity remains robust, with continued orderly functioning of the financial market. Household spending will continue to be underpinned by improvements labour market conditions and income prospects.

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