ALLIANCEDBS RESEARCH

Economic Focus

2024 outlook: Brighter prospects

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- **Economic take-off with government's concerted efforts to rebuild and restructure economy**
- **Subsiding external headwinds to catalyse Malaysia's growth momentum**
- **We are positive of 2024 growth prospects and expect 4.3% GDP growth**

Domestic economy growing from strength to strength

Malaysia is well-positioned for a better economic growth in 2024 owing to its underlying strength in domestic demand that accounts for the lion share of the economy. Private consumption will continue to be the key growth driver, underpinned by robust labour market conditions with continued expansion in employment and income prospects. Revival in tourism activities in 2024 will likely provide a strong fillip, especially with the introduction of visa-free entry for tourists from China and India, further boosting domestic economy. For 9M23, Malaysia has achieved 3.9% GDP growth despite the external headwinds, and it looks set to improve further in 2024 given the positive economic landscape.

New growth catalyst from government policies

Thanks to the concreted efforts by the federal government to boost economic growth under the Madani Economy Framework, investment-driven spending is set to be a new growth driver for Malaysia in 2024. The implementation of the strategic developments and flagship projects under the 12th Malaysia Plan Mid-Term Review (12MP MTR), New Energy Transition Roadmap (NETR) and New Industrial Master Plan (NIMP) 2030 will accelerate the economic take-off envisaged by the government to be a paradigm shift for Malaysia. In addition, the realisation of record-high approved investments from foreign investors in 2021-2022 will ensure the manufacturing sector remains on a healthy growth trajectory in 2024.

Subsiding external headwinds

The drag from weak external demand in 2023 may reverse in 2024 as global monetary tightening cycle appears to be over. There are early signs of regional exports recovery in line with nascent turnaround in global E&E sector which bodes well for Malaysia's external trade. Nevertheless, should a scenario of economic hard landing take place, we believe Malaysia's diversified export structure and deep integration into global supply chain will help ensure its trade resilience.

Fiscal reforms for long-term sustainability

Malaysia's government is committed to pursue fiscal consolidation and rebuild fiscal buffer for long-term sustainability. Under the Ekonomi Madani framework, the pace of fiscal consolidation will be further accelerated to achieve the medium-term deficit target of 3% and fiscal reforms continues to be a priority to the government. We take cognisance of the immediate pains of potentially higher consumer outlays arising from subsidy rationalisation and higher sales tax, but this has also translated into an improved fiscal deficit of 4.3% (vs 5% in 2023) despite higher 2024 development expenditure of RM90bn.

Growth momentum remains intact

We remain cautiously optimistic of Malaysia's economic outlook which is expected to grow by 4.3% 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. Key downside risks include slower-than-expected recovery in external demand and heightened geopolitical tensions.

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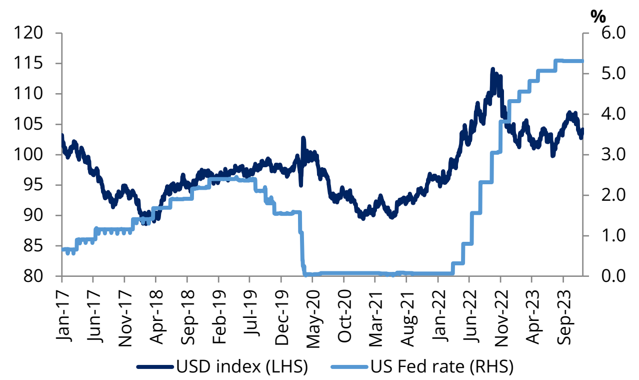
End of global monetary tightening

Global economic data has started to see much improved progress in reining in the multi-decade highs in inflation as financial markets are now pricing in more than 100 bps of rate cuts in 2024 for both the US Federal Reserve and European Central Bank. While it is still premature to conclude that that the central banks are achieving their 2% inflation target, further monetary tightening is unlikely after the most aggressive interest rate hikes in four decades as this may result in a significant slowdown in the economy.

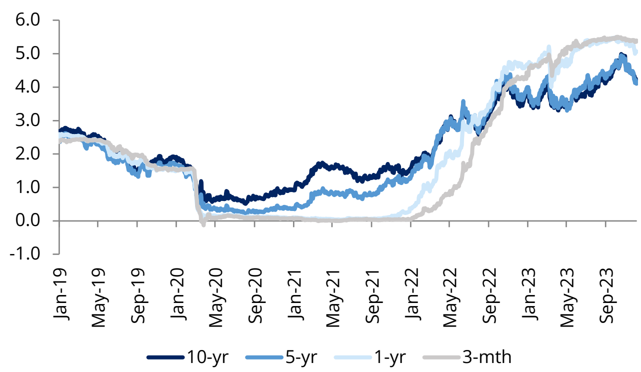
The Fed has maintained its benchmark rates in three consecutive meetings since Jul 2023 when the rates were raised to 5.25%-5.50%. The disinflation trend has worked in favour of the Fed to combat inflation after its aggressive monetary tightening and the labour market has started to show signs of weakening with unemployment rate of 3.9% hitting the highest since early 2022.

Interest rate hikes by the Fed



Source: AllianceDBS, Bloomberg Finance L.P.

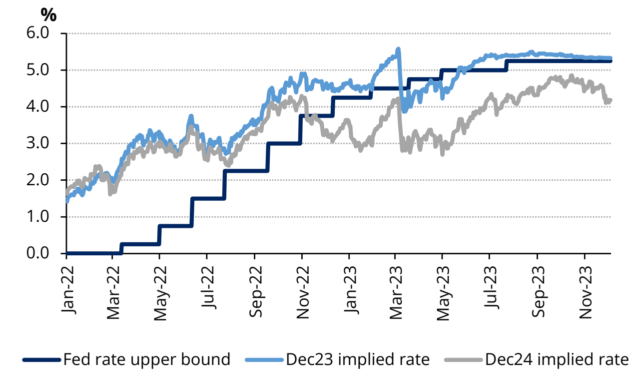
US Treasury yields may have peaked



Source: AllianceDBS, Bloomberg Finance L.P.

Based on Fed fund futures, the market is pricing in more than 100bps cut in by end-2024 after a slew of relatively softer macro data and dovish comments from Fed officials. Nevertheless, the imminent rate cuts anticipated by the markets are still subject to uncertainties. The pace of interest rate cuts in 2024 remains highly debatable going by the volatile swings in the financial markets in 2023. The interest rate outlook can fluctuate wildly within a few months from "higher for longer" to "imminent cuts", underlining the difficulty in making accurate projections of its future trajectory.

Fed funds futures price in more than 100 bps cut in 2024



Source: AllianceDBS, Bloomberg Finance L.P.

Underlying economic condition will play a key role in determining the extent of interest rate cuts to be undertaken by monetary authorities. In fact, World Economic Outlook Oct 2023 by International Monetary Fund (IMF) forecasts the global growth to slow slightly from 3.0% in 2023 to 2.9% in 2024. Global recovery remains slow, with growing regional divergences and little margin for policy error. Meanwhile, global inflation is projected to decline steadily given the tighter monetary policy as well as lower commodity prices.

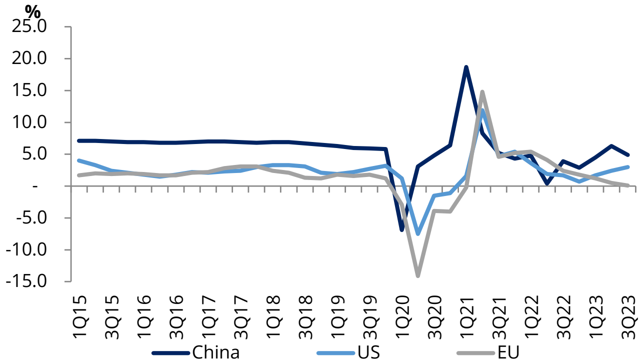
Compared to a year ago, IMF's economic projections indicate that global economic growth momentum has been rather resilient despite the aggressive interest rate hikes undertaken by global monetary authorities. It remains to be seen if 2024 will remain resilient as central bankers have started to pivot to a more dovish stance.

IMF's world economic outlook projections

Region, country	Oct 2023			Oct 2022	
	2022	2023	2024	2022	2023
World	3.5	3.0	2.9	3.2	2.7
US	2.1	2.1	1.5	1.6	1.0
UK	4.1	0.5	0.6	3.6	0.3
Euro area	3.3	0.7	1.2	3.1	0.5
China	3.0	5.0	4.2	3.2	4.4
India	7.2	6.3	6.3	6.8	6.1
Japan	1.0	2.0	1.0	1.7	1.6
Emerging & developing economies	4.1	4.0	4.0	3.7	3.7

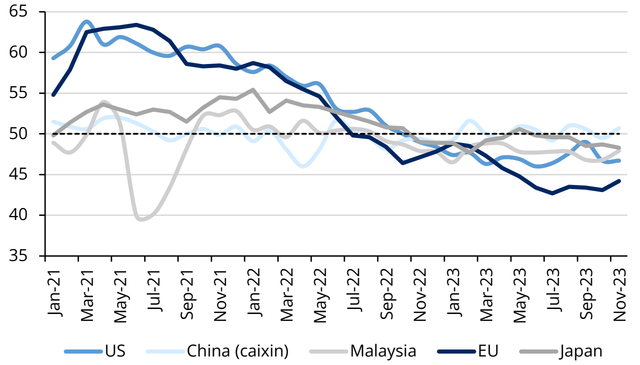
Source: AllianceDBS, IMF

Y-o-y GDP growth for major economies



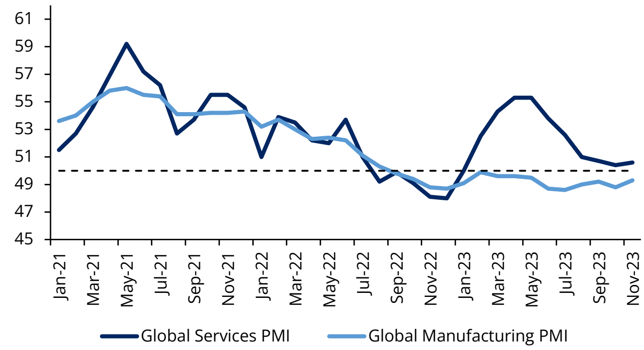
Source: AllianceDBS, Bloomberg Finance L.P.

Manufacturing PMI could be bottoming out



Source: AllianceDBS, Bloomberg Finance L.P.

Global PMI



Source: AllianceDBS, Bloomberg Finance L.P.

Meanwhile, China's growth trajectory in 2024 will be closely monitored by market participants as it has struggled to gain traction in 2023 despite the lifting of its restrictive Covid-zero policy. Demand recovery has been weaker than expected while its unprecedented property crisis reverberates across the economy.

The results of China's stimulus measures over the past few months to stimulate its economy have been lacklustre, judging by its disappointing manufacturing and services PMIs. It is still on track to hit its 5% GDP growth target in 2023, but the debt crisis in the property sector remains the biggest threat for any sustainable recovery, undermining the fragile recovery.

Industrial profit growth slowed amid deflation pressure which could keep hopes of more impactful stimulus measures alive. Nevertheless, China's central government's commitment to spur the economy should not be underestimated as financial stability is of utmost importance to the government. In fact, the central government has already increased its fiscal deficit to the largest in decades.

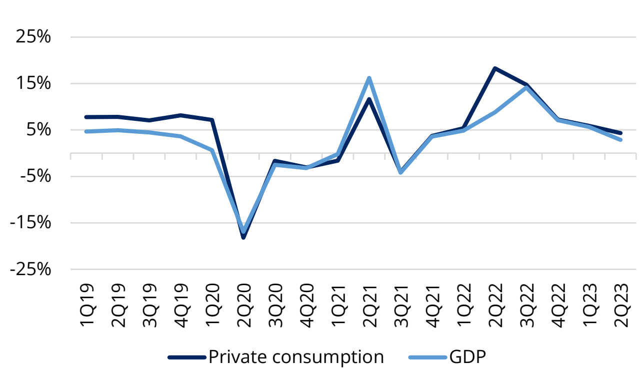
Key risks to global economy in 2024 include slower-than-expected recovery in trade activities and heightened geopolitical conflicts that have remained unabated. The global trend of de-globalisation has continued to gain traction as businesses seek to ensure supply chain security by adopting "China + 1 strategy" which has also offered opportunities for emerging countries to tap into large foreign investments.

Malaysia is progressing well under Madani Economy

Malaysia's economy is expected to pick up in 2024 as domestic demand is likely to strengthen further with sustained consumer spending and stronger investment activities. Its strong fundamentals and diversified economic structure, coupled with renewed government focus to spur higher economic growth will help ensure Malaysia's growth trajectory remains firmly on the uptrend.

We expect Malaysia to register a stronger GDP growth of 4.3% in 2024 after a healthy growth of 4.1% expected for 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, is poised 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 GDP growth

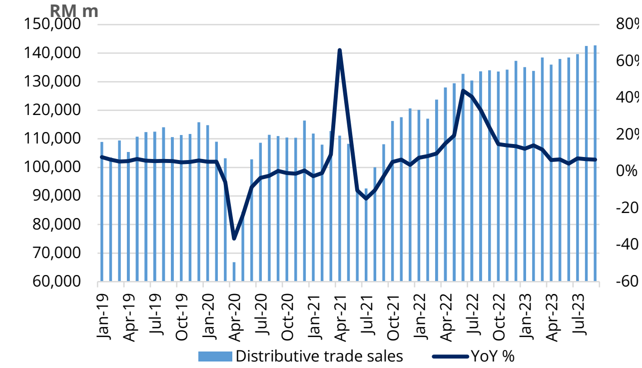


Source: AllianceDBS, CEIC

Latest government's announcement on visa-free entry for tourists from China and India is likely to further boost the tourism sector. Malaysia has also recently revised upwards its 2023 tourist arrivals from 16.1m to 19.1m, which is 73% of 2019 level. We estimate that tourist arrivals in Malaysia has only recovered to ~80% of 2019 arrivals at this juncture which will most probably translate into a more robust full-year tourism receipts in 2024. The government also plans to relax the requirements for the Malaysia My Second Home (MM2H) programme to encourage tourism and foreign investments to Malaysia.

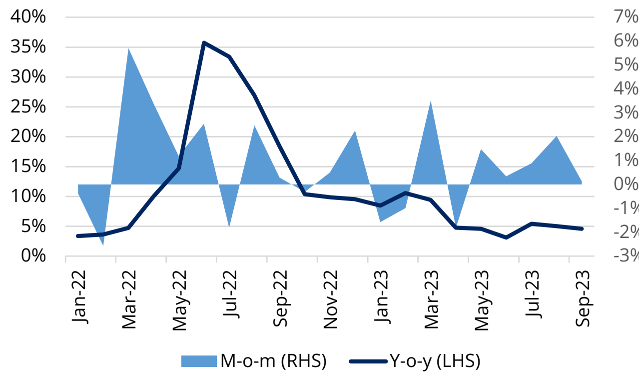
We believe the resilient household spending is likely to continue, in tandem with the continued recovery in the labour market. Meanwhile, the implementation of new and existing investment projects under the NETR and the NIMP 2030 are expected to have a positive impact to economic growth as more investment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

Monthly wholesale & retail sales



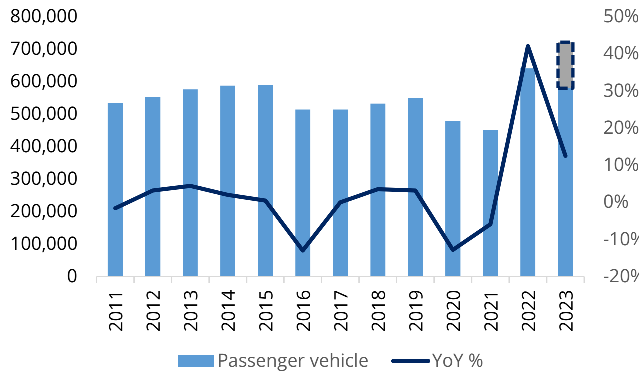
Source: AllianceDBS, CEIC

Distributive trade sales volume on healthy growth trend



Source: AllianceDBS, CEIC

Record high car sales volume despite SST exemption expiry



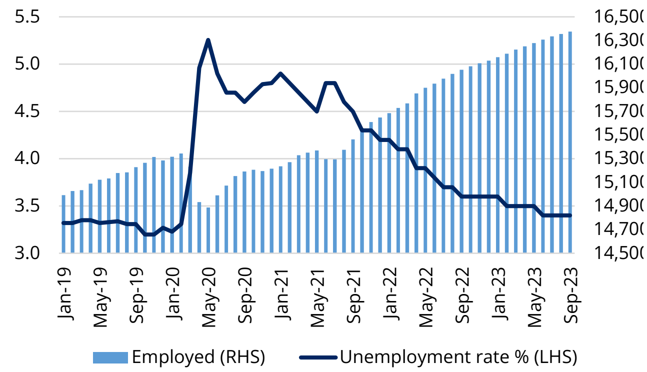
Source: AllianceDBS, CEIC

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 Sep 2023 came in at 3.4%, compared to 4.2% in Jan 2022. 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 70.1% in Sep 2023. This will certainly bode well for the economic outlook in 2024 given that domestic demand forms the bulk of our economy.

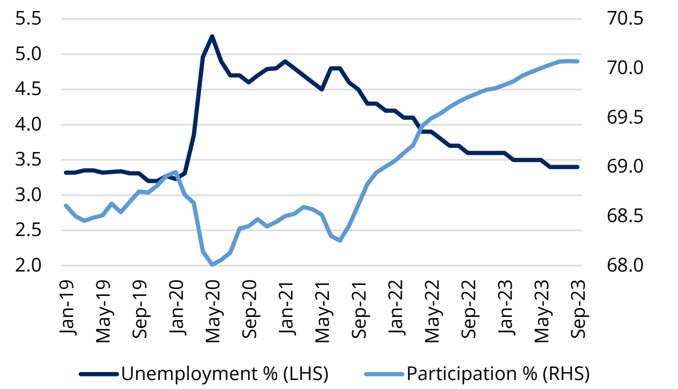
Going by the healthy growth momentum of Malaysia's economy in 2023, the robust labour market condition will ensure that the growing working-age population is met with higher employment opportunities. We believe Malaysia's unemployment rate will continue to decline towards pre-pandemic level of 3.3% by end of 2023.

Strong labour market



Source: AllianceDBS, CEIC

Favourable labour market dynamics

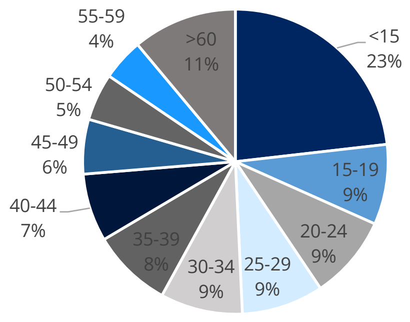


Source: AllianceDBS, CEIC

We believe this healthy strength in the employment market is a key growth pillar that will continue to sustain Malaysia's economic growth as the country enjoys the demographic dividend. The median age of Malaysia's population is relatively young at 30.7 years, underpinning the healthy growth in our labour force.

According to the Department of Statistics Malaysia, Malaysia's population is expected to grow by 2.1% to 33.4m in 2023, compared to 0.4% growth to 32.7m in 2022. The astounding growth projection in 2023 is largely due to the sharp increase of non-citizens from 2.5m to 3m, in line with the reopening of national borders starting from Apr 2022 and the implementation of the employment recalibration program 2.0 since Jan 2023.

Malaysia's 2022 demographic breakdown by age



Source: AllianceDBS, CEIC

As the Malaysian government continues to advance its economic transformation agenda by attracting more quality investment to Malaysia, international migration especially skilled labour force could further lift the overall employment market in Malaysia. According to the 12MP Mid-Term Review (MTR), Malaysia's population is projected to grow by 4.9% in 2023-2025, implying annual growth rate of 1.6%. This could be in tandem with the various investment programs undertaken by the government.

Madani Economy sets the tone for all-inclusive growth

The government unveiled several key policies in 2H23, starting with the introduction of Madani Economy Framework in Jul 2023 which serves as a guiding principle over the next 10 years to propel Malaysia's goals to achieve a progressive, inclusive and dynamic economy. Subsequently, the NETR and the NIMP 2030 were rolled out, both of which have the lofty ambitions of lifting Malaysia's economic competitiveness and elevating the overall socioeconomic status of the people.

In Sep 2023, the 12MP MTR was tabled in the Parliament which serves as a comprehensive policy document that strives to address major economic challenges of Malaysia, namely disparity in development and income, limited fiscal space and slow structural transition of the economy over 2023-2025. The 12MP MTR details its 17 "Big Bolds" initiatives that shape the main strategies accordingly, incorporating governance and institutional reforms, fiscal sustainability and socioeconomic upliftment.

Among the salient highlights of the 12MP MTR include an upward revision of GDP target to 5%-6% from 4.5%-5.5% as 2021-2022 GDP growth outperformed on low base in 2020 due to the COVID-19 pandemic. The government is also committed to allocate development expenditure of at least RM90bn per annum for 2023-2025, an indication that existing and new investment projects will continue to strengthen our economic growth.

12MP MTR will focus on infrastructure spending as some major projects such as Johor BRT, Subang and Penang airport expansions, new phases of Sabah Pan Borneo Highway and Sarawak-Sabah Link Road, Trans Borneo Highway, as well as expansion of North-South Expressway and Senai-Desaru Expressway. All these developments involve investments that are supportive of economic development.

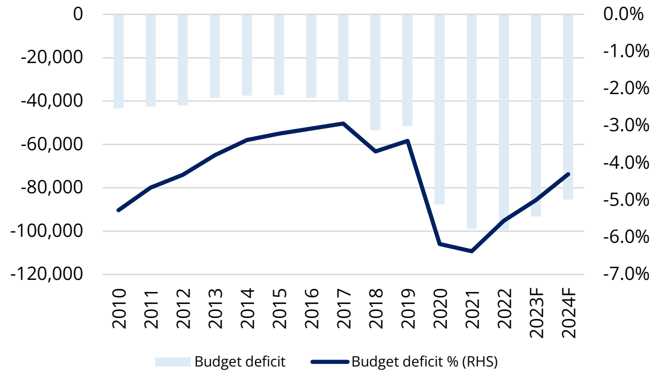
In Oct 2023, the government unveiled Budget 2024 which marked a critical milestone to deliver on the government's reform initiatives, encompassing the key strategies laid out in the 12MP MTR. Notably, 2024 development expenditure is expected to increase by 8% to RM90bn (excluding US$3bn 1MDB bond redemption in 2022 base) while operating expenditure is projected to increase by 1.2%, mirroring the projected revenue growth of 1.5% in 2024.

For revenue base expansion, some of the new taxes introduced are capital gains tax on unlisted shares, luxury goods tax as well as higher rates for service tax at 8% (from 6%) and sugar sweetened beverages. In addition, we take cognizance of the lower 2024 PETRONAS dividend of RM32bn, compared to RM40bn in 2023 and RM50bn in 2022 which clearly reflects government's commitment for long-term fiscal sustainability.

Meanwhile, diesel subsidies will be rationalised and targeted subsidy for petrol is expected to be implemented in phases in 2024 with some of the savings channelled to the allocation for Rahmah Cash Aid (STR) of RM10bn in 2024 (vs RM8bn in 2023), benefitting 9m recipients (vs 8.7m).

Fiscal sustainability has often been cited as a key concern for Malaysia given the fast-rising federal debt on persistent budget deficit throughout the years. Budget 2024 follows through with specific measures to address this long-overdue concerns. Therefore, 2024 budget deficit is expected to fall to the lowest since 2019 at 4.3% (vs 5.0% in 2023).

Consolidating budget deficit



Source: AllianceDBS, BNM, Ministry of Economy

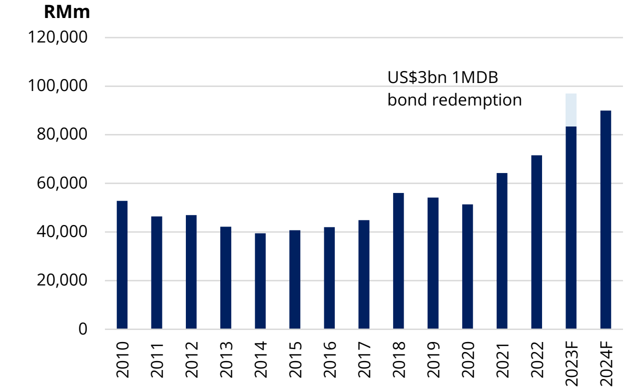
PADU (Pangkalan Data Utama), a new single database integrating all databases will be used as the main reference for socioeconomic assistance that includes poverty alleviation and targeted subsidy programs. The central database is set to be rolled out in early 2024, ensuring the right target groups benefit from assistance. According to the Ministry of Finance, RM50.8bn was spent on petrol, diesel and LPG subsidies in 2022, of which 35% or RM17bn benefitted the T20 high-income group. Assuming half of the subsidy for the T20 is saved by the government, this could easily shave off 0.4% budget deficit.

There are questions on the impact of subsidy rationalisation on people's purchasing power in 2024. While the risk of subsidy rationalisation affecting consumer sentiment is there, it is likely to be undertaken in phases and those in need will continue to receive subsidies. At the same time, the higher development expenditure in 2024 to ensure a growing economy for the benefit of the nation will help to limit the impact.

Budget 2024 reaffirms the long-term strategies under NETR and NIMP 2030 with various tax incentives provided such as RM50k tax deduction for ESG-related expenses, enhanced green technology tax incentives and tiered investment tax allowance to attract investment in high-growth high-value industries. SME development is also emphasized with RM2.4bn financial facilities offered and RM900m loan funds for automation and digitalisation.

In addition, mega projects such as RM10bn Penang LRT, RM4.7bn LRT 3 (5 stations in Selangor revived), RM0.9bn PLUS highway expansion and RM15.7bn Pan-Borneo Sabah Highway will sustain investment activities in 2024. The government has also delivered on its promise to allocate more development expenditure for Sabah/Sarawak at RM12.4bn in 2024 (vs RM12.1bn in 2023).

Rising development expenditure



Source: AllianceDBS, BNM, Ministry of Economy

Madani Economy Framework

Madani Economy targets by 2033

#	Targets	Current position
1	Top 30 largest economy	36th
2	Top 12 in global competitiveness	27th
3	Top 25 on Human Development Index	62nd
4	Increase labour share of income to 45%	34.8%^
5	Top 25 in Corruption Perception Index	61st
6	Fiscal deficit of 3% or better	5.6%*
7	60% female labour force participation	55.5%^

Broad Madani Framework objectives

EKONOMI MADANI
Building a Better Malaysia Together

Raise the Ceiling	Raise the Floor
Competitive & World Class	Respectable Jobs & Decent Standard of Living
Investment Destination	Equality & Inclusive Opportunities
Digital & Innovation-led Industry	Universal Access of Quality Education & Healthcare Services
Global Leader in Islamic Finance	World-Class Basic Infrastructure & Public Services
MSMEs as Regional Champions	Social Protection for All
Security & Sustainability of Economy	

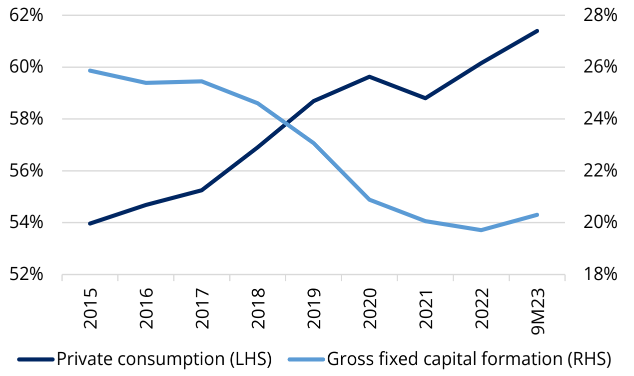
MADANI Values: Sustainability, Care & Compassion, Respect, Innovation, Prosperity & Trust

Source: AllianceDBS, BNM, Ministry of Economy

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.

GDP share of consumption vs investment



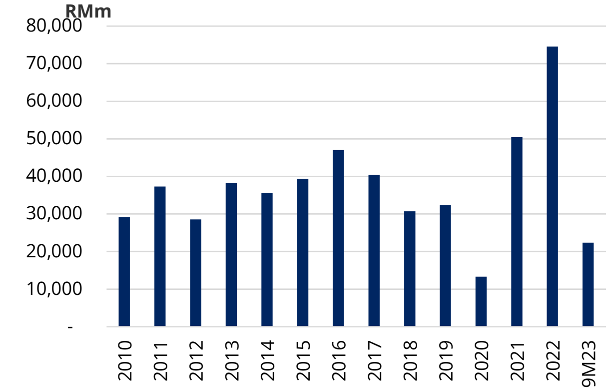
Source: AllianceDBS, BNM, CEIC

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.

For Malaysia, there has been a substantial increase in foreign direct investment (FDI) net inflows in 2021 and 2022. In 2022, Malaysia's recorded a record high FDI net inflows of RM74.6bn, a substantial y-o-y increase of 48%, of which 66% came from the manufacturing sector. While it was slower in 9M23 with only RM22bn net inflows registered, we believe this is not a cause for concern given the elevated approved foreign investment which will typically take years for the committed funds to be realised.

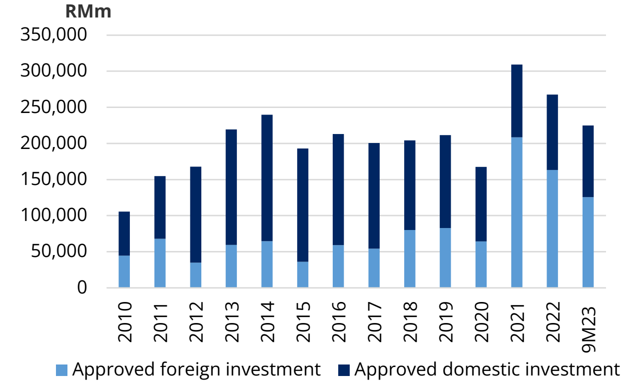
The unity government has been able to attract various multinational corporates to set up businesses in Malaysia, thanks to the stable political climate as well as the pro-investment policy championed by the government. According to the Parliament, Prime Minister Anwar Ibrahim has helped Malaysia to secure potential investments worth RM347bn as a result of his overseas visits between Nov 2022-Oct 2023. Therefore, it is no surprise that globally renowned brands such as Infineon AG, Nvidia, Tesla and Geely have all committed to step up their investments in Malaysia which will help to propel Malaysia's industrial developments.

High FDIs to spill over to domestic economy



Source: AllianceDBS, BNM, CEIC

Record-high approved investments over 2021-2023



Source: AllianceDBS, BNM, CEIC

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 2024 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.

Some of the major foreign investment secured by the government

Date	Investor	country	location	Investment RMbn	Business
Nov-23	Enovix	US	Penang	5.8	advanced silicon battery
Oct-23	LONGi	China	Selangor	1.8	Solar PV manufacturing
Sep-23	Alton	US	Johor	2.0	industrial tools
Aug-23	Infineon	Germany	Kedah	25.0	semiconductor
Aug-23	Bosch	Germany	Penang	1.6	engineering
Jul-23	Zhejiang Geely	China	Perak	46.0	automotive
Jun-23	Texas Instrument	US	KL, Melaka	14.6	semiconductor
Jan-23	Intel	US	Penang	30.0	semiconductor

Source: AllianceDBS, MIDA, various

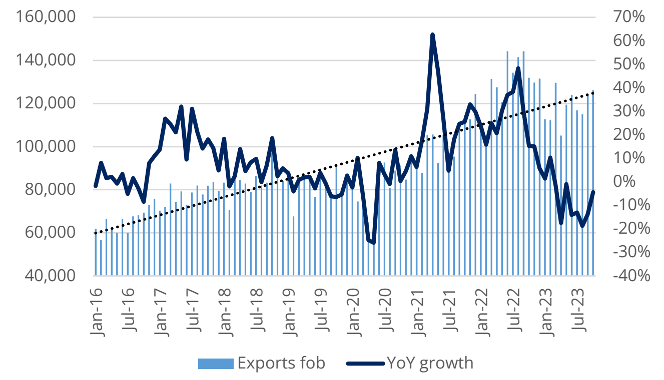
Some of the major government projects

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

External weakness is bottoming out

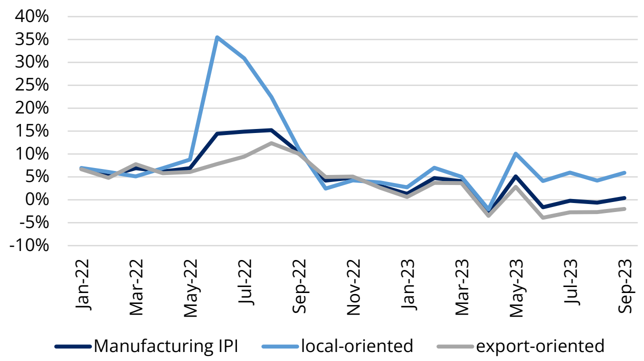
Admittedly, a widely anticipated external weakness in 2023 has dragged our manufacturing sector which contributes ~24% of our GDP. Malaysia exports have not been spared by the sluggish trade in 2023 and this has been reflected by the 8% y-o-y decline for 10M23 total exports. Demand has been weak across the key export markets in China, the US and Singapore due to the global monetary tightening and inventory de-stocking after major purchases during the pandemic.

Malaysia's monthly exports decline is narrowing



Source: AllianceDBS, CEIC

Local-oriented industries' production holding up well



Source: AllianceDBS, CEIC

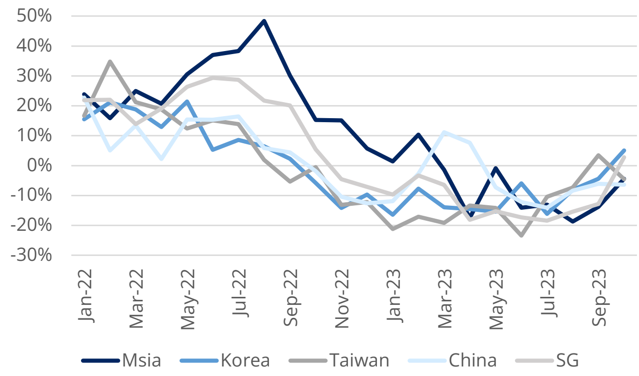
The demand weakness has been reflected in the sluggish manufacturing production which only grew 1.1% in 9M23. The lacklustre production was largely attributable to export-oriented manufacturers given weaker demand arising from inventory de-stocking. Nevertheless, the relatively subdued export-oriented manufacturing activities has been more than offset by domestic-oriented industries given our resilient demand locally.

However, the gloomy trade data has started to stabilise as most of the key exporting countries have begun to register improved numbers over the past few months. The weaker-than-expected recovery in China's economy in 2023 may reverse in 2024 as its government continues to step up on its stimulus measures.

In addition, the narrowing decline in global semiconductor shipments suggests that the global technology sector is likely to register sequential improvement in 2024, which bodes well for Malaysia as E&E accounts for ~40% of Malaysia's exports and it has a deep integration with the global supply chain which makes it vulnerable to the global trend.

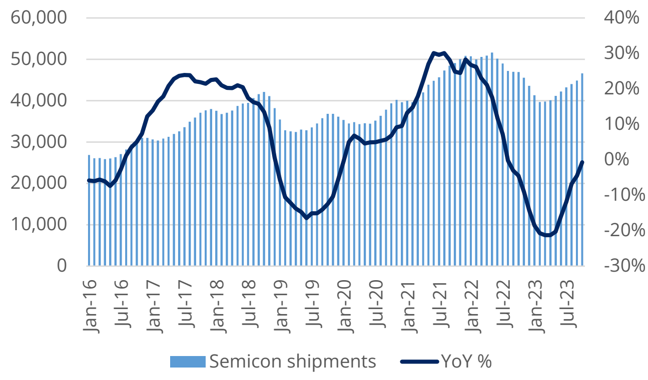
Therefore, we believe exports will recover on a gradual basis in 2024, underpinned by a recovery in global tech cycle. The de-globalisation trend, especially in the technology sector, may instead result in more capital spending as countries rush to ensure supply security.

Signs of bottoming out for key Asian exporters



Source: AllianceDBS, CEIC

Global semiconductor shipments

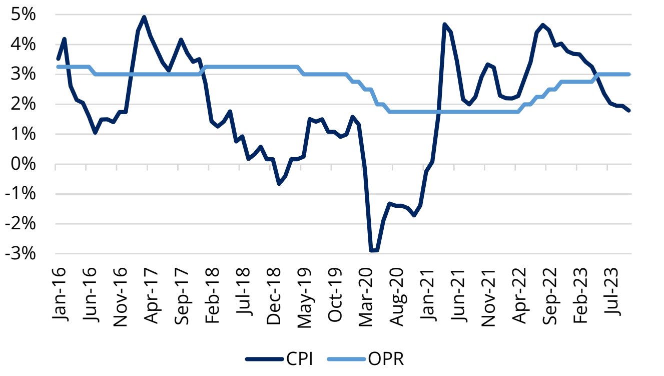


Source: AllianceDBS, SIA, CEIC

Moderating loans growth momentum

Following Bank Negara Malaysia's interest rate hike by 25 bps to 3.0% in May 2023, the central bank has continued with its extended pause for three consecutive meetings. As the OPR has reverted to its pre-pandemic level, we believe that BNM will remain with this slightly accommodative interest rate in the foreseeable future as the current monetary policy remains conducive to sustainable economic growth amid price stability.

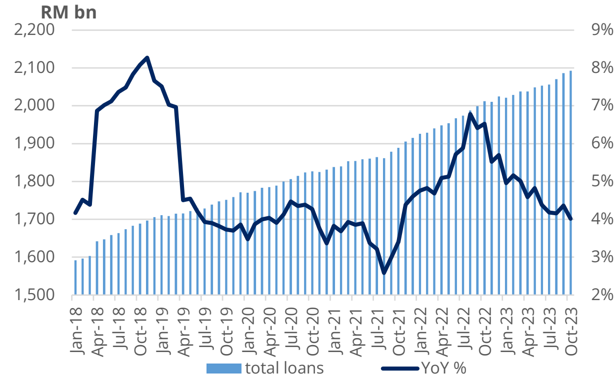
Interest rate vs inflation



Source: AllianceDBS, DOSM, CEIC

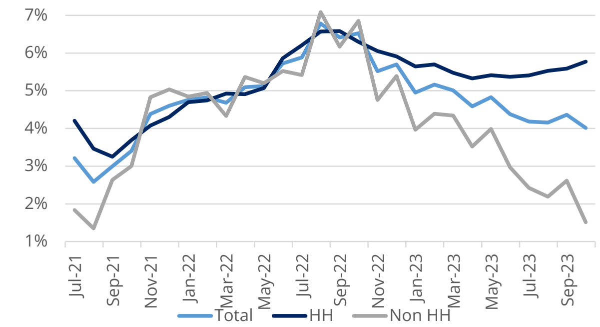
Our headline inflation has been moderating over the course of 2023, in tandem with the easing momentum of price increases which is expected to continue for the remainder of 2023. This has also resulted in positive real rates after staying negative for the past two years. Going forward, inflation outlook will be largely swayed by the global commodity price developments as well as the implementation of subsidy rationalisation in 2024.

Steady banking system loans growth



Source: AllianceDBS, BNM

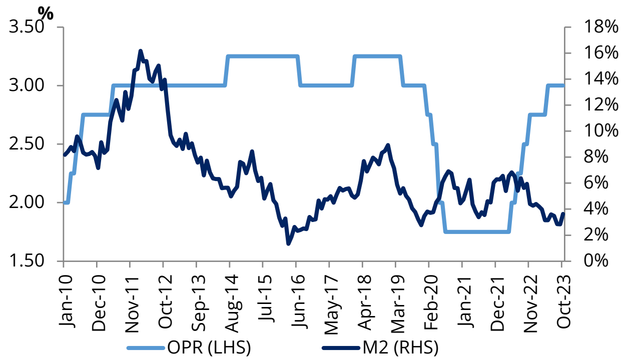
Resilient household loans growth



Source: AllianceDBS, BNM

Meanwhile, Malaysia's banking system has recorded moderating loans growth which stood at 4.0% in Oct 2023, compared to 5.7% in Dec 2022. This is largely attributable to weaker demand from non-household sectors (+1.5%), possibly due to higher financing rates and uncertainties arising from global developments. On the other hand, household loans growth remained firm at 5.8%, in tandem with resilient domestic expenditure. This diverging scenario may persist in the near term as businesses assess the macroeconomic environment before committing to new loans.

Normalising liquidity condition in the economy



Source: AllianceDBS, BNM

Meanwhile, M2 money supply continues to grow at a healthy level of 3.6% in Oct 2023 (vs 2.8% in Sep 2023, 4.3% in Dec 2022), as the domestic economy grows steadily despite the lag effects of cumulative interest rate hikes over May 2022-May 2023. Therefore, it is likely that the domestic liquidity remains sufficient, 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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