

Economic Focus

Navigating shocks, sustaining growth

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- **US-Iran tentative peace deal to ease inflationary pressure and fiscal concerns from elevated subsidy bills**
- **Resilient growth momentum to sustain in 2H26 with stronger focus on domestic consumption**
- **Cautiously optimistic of 2026 growth prospects with 4.5% GDP growth**

Resolution to Middle East conflict in sight

The tentative US-Iran peace deal to restore access through the Strait of Hormuz pulled oil prices down from over US\$110 to below US\$75 (YTD average: US\$88), allaying inflation and interest rate hike worries. While the timing of a full resumption of oil flows from the Middle East remains uncertain at this juncture, easing crude prices could give the government room to maneuver as it grapples with heavy monthly fuel subsidy bills of RM3-4bn, compared to full-year projection of RM15bn. This is set to provide a huge relief for the government to focus on boosting the economy without derailing its 2026 fiscal deficit target of 3.5%.

Economic growth trajectory remains on track

We believe domestic demand remains supported by sustained household spending, further realisation of investment projects and robust tourism activity. After recording impressive economic growth of above 5% in 2024-2025, Malaysia maintained its growth momentum in 1Q26, with GDP expanding by 5.4%, exceeding expectations. Admittedly, the higher crude oil prices have weighed on certain industries including logistics and energy-intensive manufacturing, but Malaysia's proactive fiscal measures and diversified economic structure with net energy export status have helped to partially cushion the impact of these temporary headwinds. While consumer and business confidence are likely to be adversely affected, with SMEs and low-income groups being more vulnerable, overall economic growth is expected to remain resilient.

Under-appreciated domestic resilience

Malaysia's robust labour market with unemployment hovering at 3% will underpin sustained domestic consumption. Importantly, 1Q26 tourist arrivals remained on a positive growth of 3% despite the air connectivity disruptions via Middle East transit hubs, thanks to the 25% y-o-y spike in Chinese tourist arrivals. Additionally, passenger movements at KLIA recorded a 14% y-o-y increase in 1Q26, reflecting solid outbound tourism for Malaysians due to broader economic growth. Meanwhile, our conviction of positive external trade despite the energy crisis has been validated by recent data – ex-E&E exports in Apr 2026 grew 29% y-o-y due to the broad transmission effect of rising oil prices on commodities. Separately, Apr 2026 E&E exports, accounting for 48% of total exports, surged 46% y-o-y, fuelled by relentless AI-related spending globally.

In a position of relative strength

We remain cautiously constructive on Malaysia's economic outlook and maintain our 2026 GDP growth of 4.5%, notwithstanding short-term challenges due to higher energy and commodity prices as well as supply chain disruptions from the Middle East. Malaysia is relatively well-positioned to weather the disruption better than many of its Asian peers given its status as a net energy exporter. We believe Malaysia's strong fundamentals anchored by firm domestic demand and a diversified export base will continue to underpin the economy's resilience. Key downside risks include a prolonged Middle East conflict, slowdown in key trading partners, higher cost of living and lower-than-expected commodity production.

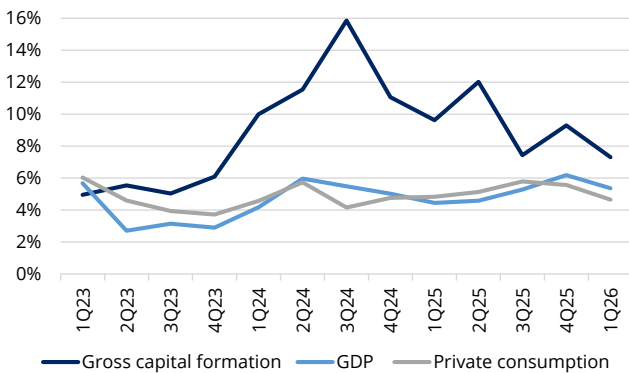
Economic Focus

Malaysia's economy remains resilient

We expect Malaysia to register a relatively healthy GDP growth of 4.5% in 2026 which is in line with the government's forecast of 4.0%-4.5%. We believe Malaysia's economy is coming from a position of relative strength as domestic demand is likely to strengthen further with sustained consumer spending and investment activities. Its strong fundamentals and diversified economic structure, coupled with government focus to spur higher economic growth will help ensure Malaysia's growth trajectory remains firmly on the uptrend.

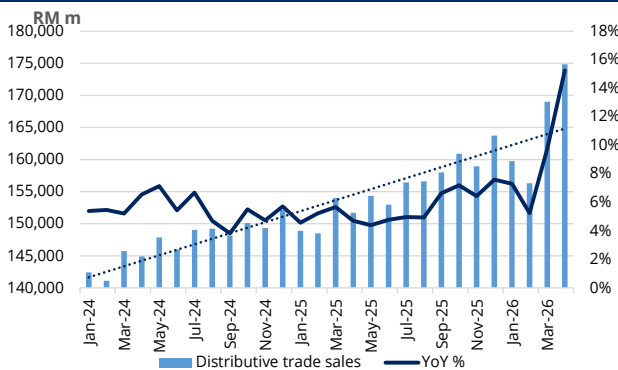
Private consumption, accounting for 61% of our economy, will continue to deliver satisfactory performance for Malaysia's economy, underpinned by robust labour market and sustained household spending, boosted by Visit Malaysia 2026. Meanwhile, private investment is expected to benefit from improved external environment and positive response to the National Energy Transition Roadmap (NETR) and the New Industrial Masterplan (NIMP) 2030 while the government continues with its expansionary fiscal policy to drive economic growth.

Malaysia's GDP growth



Source: AllianceDBS, CEIC

Monthly distributive trade sales



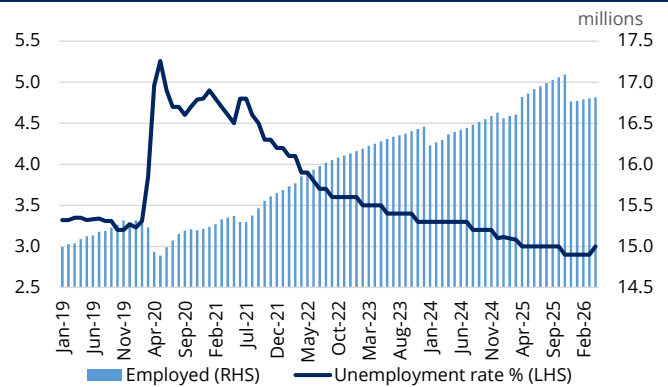
Source: AllianceDBS, CEIC

Stable labour market condition

Malaysia's economic growth momentum will continue to be underpinned by a stable employment market, which has remained solid despite heightened external uncertainties. Malaysia's unemployment rate in Apr 2026 came in at a healthy level of 3%. Notably, we are encouraged by the continuous growth in the labour participation rate, reaching a record high of 70.9% in Apr 2026. This will certainly bode well for the economic outlook in 2026 given that domestic demand forms the bulk of our economy.

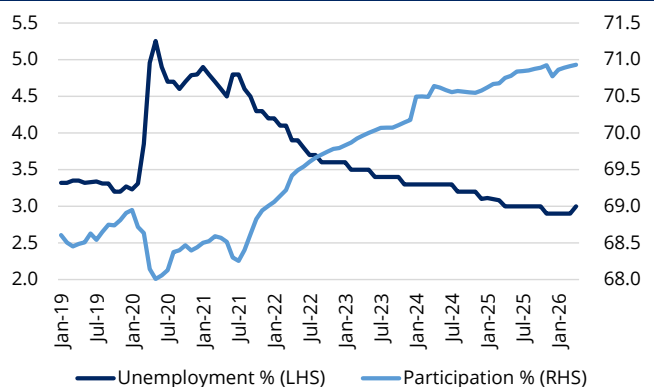
The healthy labour market condition will ensure that the growing working-age population is met with higher employment opportunities. We believe Malaysia's unemployment rate will stay low as more jobs are created with the realization of various investment activities.

Healthy labour market



Source: AllianceDBS, CEIC

Favourable labour market dynamics

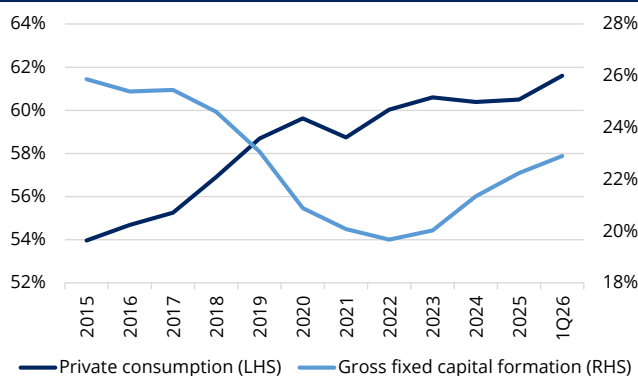


Source: AllianceDBS, CEIC

Growing momentum from investment upcycle

Thanks to the concerted efforts by the federal government to boost economic growth under the Madani Economy Framework, investment-driven spending has emerged as a new growth driver for Malaysia. The implementation of the strategic developments and flagship projects under the NETR and the NIMP 2030 will accelerate the economic take-off envisaged by the government to be a paradigm shift for Malaysia.

GDP share of consumption vs investment



Source: AllianceDBS, BNM, CEIC

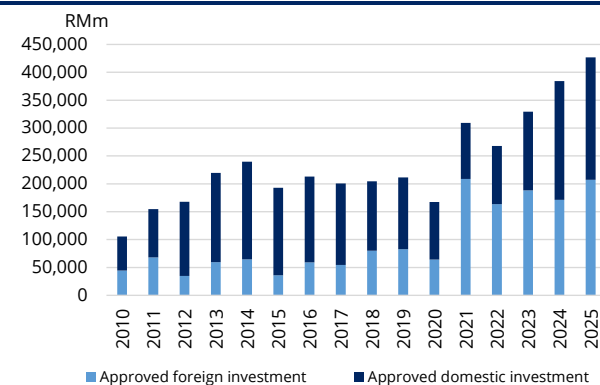
Indeed, the proactive strategy adopted by the government to revitalize the domestic economy has started to bear results as 2025 gross capital formation grew by 10% after a multi-year high growth of 12% in 2024. The positive impact arising from record-high approved investments in 2023-2025 and various government-led strategic developments under national blueprints is expected to provide further tailwinds in the subsequent quarters.

More importantly, the all-time high approved investments recorded in 2025 (+11% y-o-y) underscores Malaysia’s appeal as an attractive investment destination amid the heightened trade uncertainty. It is noteworthy that approved investments have been breaking record highs for three years consecutively. This signifies the strong confidence that foreign investors have in Malaysia, a traditionally non-aligned country which is expected to benefit from the 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 industrial value chain diversification. In fact, the heightened US-China trade tensions have benefitted not only Malaysia but the entire ASEAN as a whole given the attractive value proposition offered.

Meanwhile, the government is also committed to revive economic growth in 2026 by undertaking various large-scale infrastructure projects which will create positive spillover effects to the local businesses. Major projects such as Madani Submarine Cable (RM2bn), sovereign AI cloud (RM2bn) and Large-Scale Solar 6 (RM6bn) reflect government’s focus to drive high-value investments in advanced technology and renewable energy. In addition, various investments and financing are directed to high-impact sectors which are set to uplift Malaysia’s technological capabilities. 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.

Record-high approved investments



Source: AllianceDBS, BNM, CEIC

Some of the major government projects

| Project | Investment RMbn | Timeline |
|--|-----------------|-----------|
| Water-related investments | 13.0 | 2026-2030 |
| Penang LRT | 10.0 | 2025-2030 |
| Flood mitigation | 2.2 | 2026 |
| Airport upgrade in Penang, Sabah & Sarawak | 2.3 | 2026 |
| Large-Scale Solar 6 with 2GW | 6.0 | 2026 |
| Madani submarine cable | 2.0 | 2026 |
| ECRL | 50.0 | 2018-2027 |
| Johor-SG RTS | 3.7 | 2021-2026 |
| My Digital 5G | 16.5 | 2021-2031 |
| GLIC investments under GEAR-UP | 30.0 | 2026 |

Source: AllianceDBS, MoF

External trade resumes acceleration

Malaysia’s external trade has resumed a powerful acceleration in 2026, hitting a historic RM1.1tr in total trade for Jan-Apr 2026 (+15% y-o-y), thanks to a broad-based expansion across crude oil-based commodities and manufacturing goods. The strength of Malaysia’s diversified export structure and deep integration into the global supply chain has been clearly reflected by the 19% and 11% y-o-y increase for Jan-Apr 2026 exports and imports, respectively.

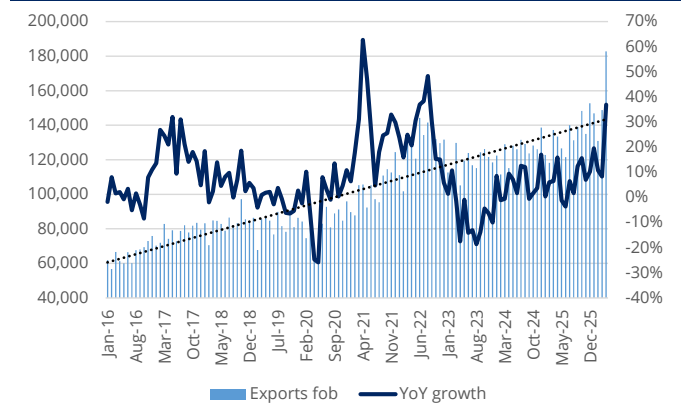
Our conviction of positive external trade despite the energy crisis has been validated by recent data – ex-E&E exports in Apr 2026 grew 29% y-o-y due to the broad transmission effect of rising oil prices on commodities. Separately, Apr 2026 E&E exports, accounting for 48% of total exports, surged 46% y-o-y, fueled by relentless AI-related spending globally. We believe the prospects for external trade in the remainder of 2026 should remain positive as the energy shock from the Middle East conflict starts to unwind.

Malaysia’s entrenched ecosystem in the global semiconductor supply chain, especially in the packaging, assembly and testing services continues to benefit from the global tech upcycle as AI-related spending has turned into a strong structural tailwind. This has also been reflected in the rising contribution of the E&E sector to Malaysia’s total exports, growing from a share of 39% in Apr 2024 to 48% in Apr 2026 despite the strong appreciation of MYR against USD over the past two years. We believe the sustained expansion in AI-related technology demand and continued robust capital spending by multinational tech giants bode well for Malaysia, reinforcing the strength of its established technology ecosystem.

The new 10% US global tariff introduced on 24 Feb 2026, replacing the previous 19% tariff, provides temporary relief for global trade, although tariff levels are likely to remain fluid for now. US importers may take advantage of the relatively lower tariff to front-load shipments, which could provide a near-term boost to global trade.

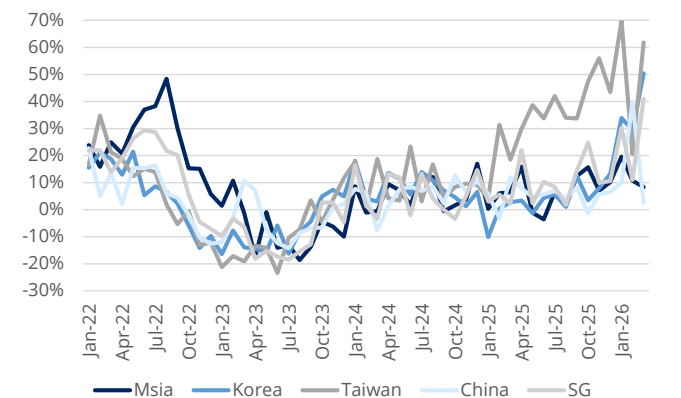
In addition, Visit Malaysia 2026 is expected to contribute to stronger services exports (tourism receipts) given the extensive collaboration between the government and the private sector to promote the tourism sector. Notably, the government has allocated RM700m to ensure Visit Malaysia 2026 turns out to be a resounding success. Various tax incentives including 100% tax exemption for international-level conferences and exhibitions have also been introduced.

Malaysia’s monthly exports



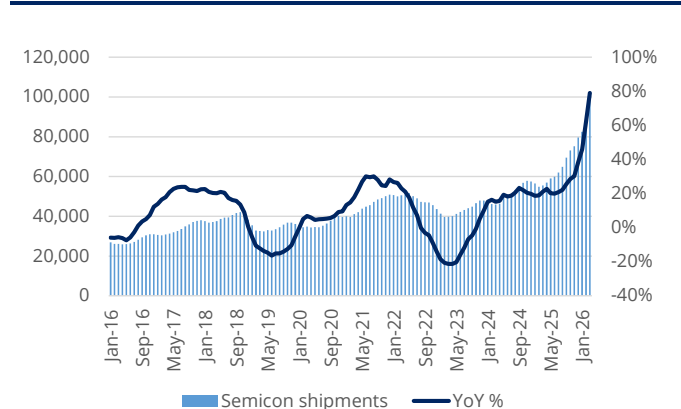
Source: AllianceDBS, CEIC

Positive exports growth for key Asian exporters



Source: AllianceDBS, CEIC

Global semiconductor shipments

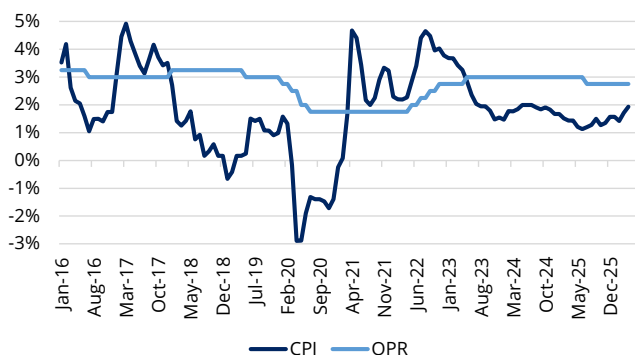


Source: AllianceDBS, SIA, CEIC

Steady loans growth momentum

In Jul 2025, Bank Negara Malaysia (BNM) has cut its benchmark OPR rate by 25bps to 2.75%. It was highlighted by BNM that the OPR reduction was a pre-emptive measure aimed at preserving Malaysia's steady growth path amid moderate inflation prospects. The accommodative move is likely to further stimulate Malaysia's economy in 2026.

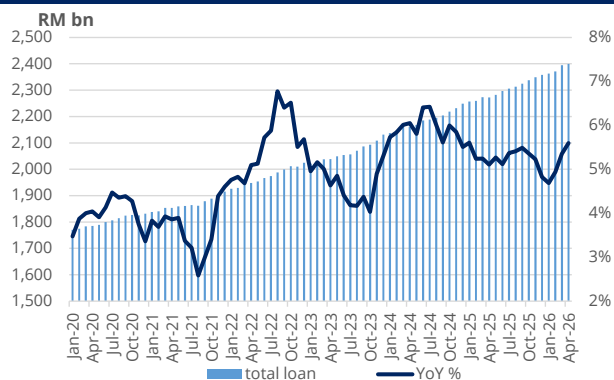
Interest rate vs inflation



Source: AllianceDBS, DOSM, CEIC

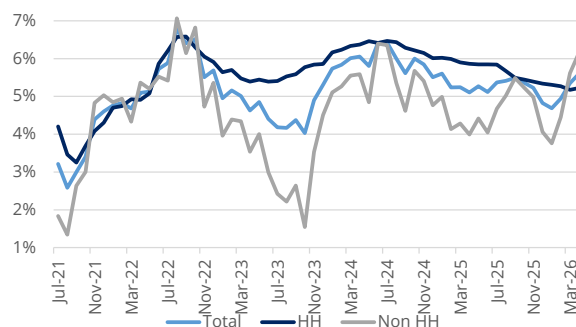
Our headline inflation remained moderate at 2.0% in May 2026 despite the elevated crude oil prices. As the US and Iran have agreed to a tentative peace deal to end months of hostilities, inflationary pressure is expected to ease in the coming months, in tandem with the latest oil price developments. We believe the positive real rates are likely to continue in the near term, reflecting continued expansion in economic activity and the absence of excessive demand pressures.

Banking system loans growth



Source: AllianceDBS, BNM

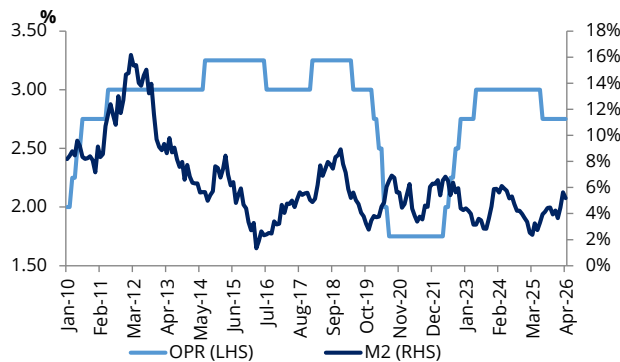
Loans growth remains at healthy levels



Source: AllianceDBS, BNM

Malaysia's banking system has been seeing steady credit demand with Apr 2026 loans growth coming in at 5.6% (vs 5.1% in Apr 2025). The growth momentum seems to have pick up pace in recent months, driven by higher loan growth from larger corporates. We believe resilient domestic demand will continue to underpin the banking sector loans growth in 2026, notwithstanding the external uncertainties.

Healthy liquidity condition in the economy



Source: AllianceDBS, BNM

Meanwhile, M2 money supply was steady at 5.2% in Apr 2026 (3.2% in Apr 2025). We believe the healthy domestic economy will ensure that domestic liquidity remains robust, with continued orderly functioning of the financial market. Household spending will continue to be underpinned by improvements in labour market conditions and income prospects.

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