ALLIANCEDBS RESEARCH

Economic Focus

Under-appreciated economic resilience

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- **Healthy growth momentum to continue in 2H26 amid global technology sector upcycle**
- **Strong underlying fundamentals cement position of strength for sustainable growth**
- **Cautiously optimistic of 2026 growth prospects with 5.2% GDP growth**

Resilience in the face of Middle East geopolitical tensions

Notwithstanding the challenging global environment stemming from a protracted energy supply shock in the Middle East, global economic growth trajectory has remained resilient thus far, largely boosted by the unprecedented global tech boom. Global equity indices have also been scaling record highs, thanks to strong corporate earnings despite rising sovereign bond yields. On the domestic front, Malaysia's 2Q26 economy exceeded expectations with an impressive 6% y-o-y growth (1H26 +5.7%), largely attributed to the sustained expansion in domestic demand (+5.1% y-o-y) and robust net exports (+169% y-o-y). It is noteworthy that Malaysia's external trade has benefitted tremendously from global tech upcycle and oil-related shipments, contributing ~40% of the incremental growth in 2Q26.

Tailwinds from AI spending

We believe domestic demand remains supported by sustained household spending and further realisation of investment projects. Strong semiconductor demand and data-centre investment are increasingly feeding through to exports, manufacturing, construction and services in Malaysia. This has been corroborated by the explosive growth of Malaysia's total exports, surging by 31% for 8M26 – the fastest over the past 20 years, thanks to the impressive E&E export growth of 47%. In fact, the World Semiconductor Trade Statistics (WSTS) projects 2026 and 2027 sales growth to come in at 108% and 29% respectively given the insatiable demand for AI infrastructure which will in turn continue to benefit Malaysia. Meanwhile, continued strength in approved investment (1H26 +12%) suggests that the investment cycle has further room to run, ensuring the growth pillar remains intact.

Budget 2027 expected to be people-centric

Budget 2027, to be unveiled on 9 Oct 2026, is likely to remain fiscally disciplined while becoming more targeted toward cost-of-living relief and growth-enhancing spending. The government explicitly emphasizes continued subsidy rationalization, better targeting of assistance, improved tax compliance and higher spending efficiency, rather than broad-based fiscal expansion. We can expect continuous incentives and facilitation to focus on semiconductors, AI and digital services, energy transition, logistics and aerospace, alongside measures to deepen local supply chains, technology transfer and high-skilled employment. Overall, we believe the on-going fiscal consolidation will remain in place, but savings are increasingly being recycled toward targeted household protection and productivity-enhancing investment.

In a position of relative strength to normalise the OPR

We remain constructive on Malaysia's economic outlook with our 2026 GDP growth projection of 5.2%, which reflects a high base in 2H25 and considers near-term challenges from higher energy and commodity prices. Malaysia is better positioned than many of its Asian peers to weather the disruption 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. With growth momentum remaining robust, we expect BNM to reverse its 2025 pre-emptive rate cut, raising the OPR by 25bps to 3.00% by 1H27. Key downside risks include a prolonged Middle East conflict, slowdown in key trading partners and higher cost of living.

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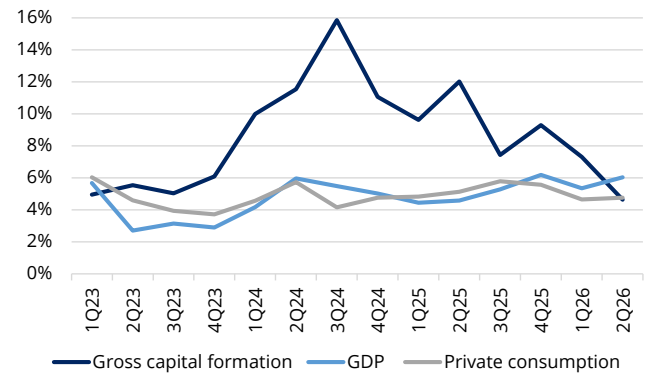
Malaysia's economy remains resilient

We expect Malaysia to register a relatively strong GDP growth of 5.2% in 2026 which is in line with the government's forecast of ~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 on the uptrend.

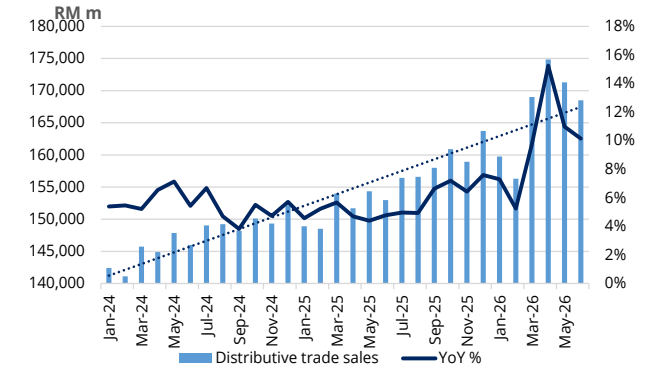
Private consumption, accounting for 61% of Malaysia's economy, will continue to deliver satisfactory performance for Malaysia's economy, underpinned by robust labour market and sustained household spending, boosted by Visit Malaysia 2026. Meanwhile, private investment is expected to benefit from improved 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



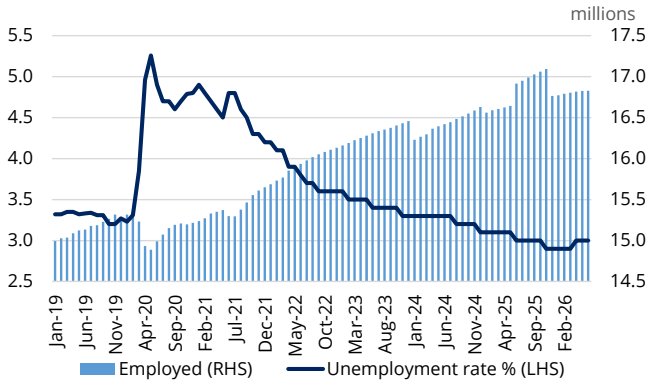
Source: AllianceDBS, CEIC

Stable labour market conditions

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 Jul 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 Jul 2026. This will certainly bode well for the economic outlook in 2026 given that domestic demand forms the bulk of Malaysia's economy.

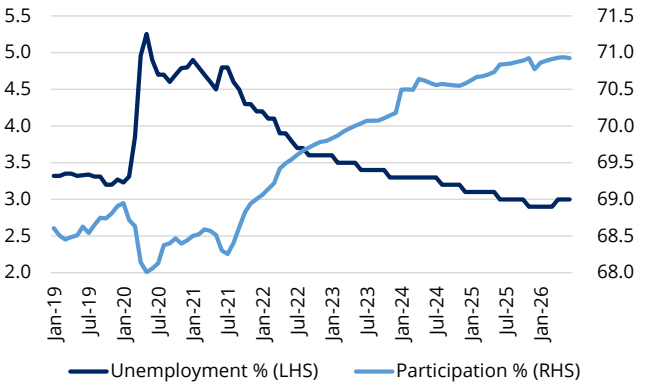
The healthy labour market condition will ensure that the growing working-age population is met with higher employment opportunities. We believe Malaysia's unemployment rate will stay low as more jobs are created with the realization of various investment activities.

Healthy labour market



Source: AllianceDBS, CEIC

Favourable labour market dynamics

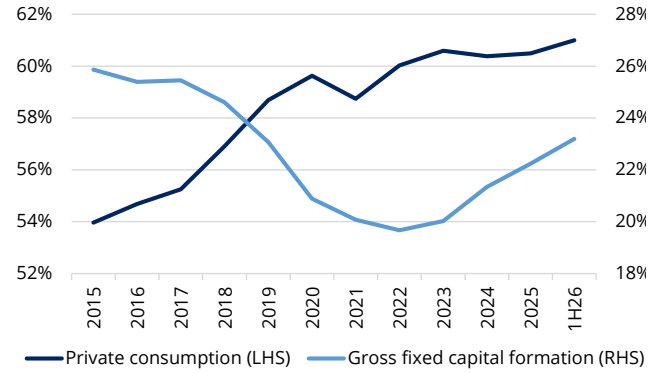


Source: AllianceDBS, CEIC

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

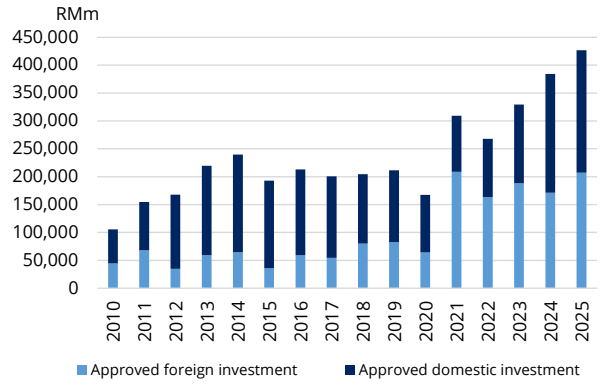
Indeed, the proactive strategy adopted by the government to revitalize the domestic economy has started to bear results as 2025 gross capital formation grew by 10% after a multi-year high growth of 12% in 2024. The positive impact arising from record-high approved investments in 2023-2025 and various 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 continues to accelerate

Malaysia's external trade has resumed a powerful acceleration in 2026, hitting a historic RM2.5tr in total trade for Jan-Aug 2026 (+27% y-o-y), thanks to a broad-based expansion across crude oil-based commodities and E&E shipments. The strength of Malaysia's diversified export structure and deep integration into the global supply chain has been clearly reflected by the 31% and 22% y-o-y increase for Jan-Aug 2026 exports and imports, respectively.

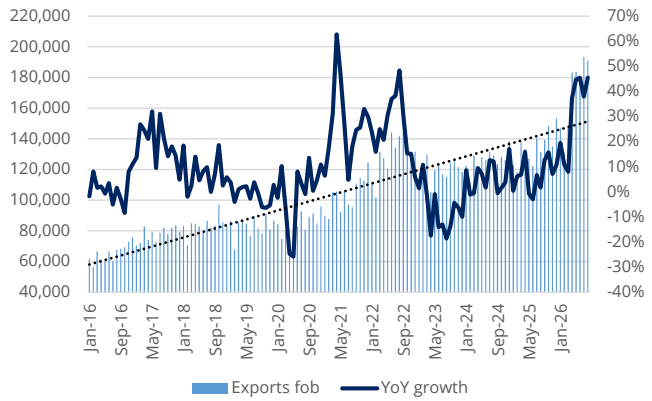
Our conviction of positive external trade despite the energy crisis has been validated by recent data – ex-E&E exports in Aug 2026 grew 30% y-o-y due to the broad transmission effect of rising oil prices on commodities. Separately, Aug 2026 E&E exports, accounting for 48% of total exports, surged 67% y-o-y, fuelled by relentless AI-related spending globally. We believe the prospects for external trade in the remainder of 2026 should remain positive as the impact of the energy shock from the Middle East conflict remains manageable.

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 Aug 2024 to 48% in Aug 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.

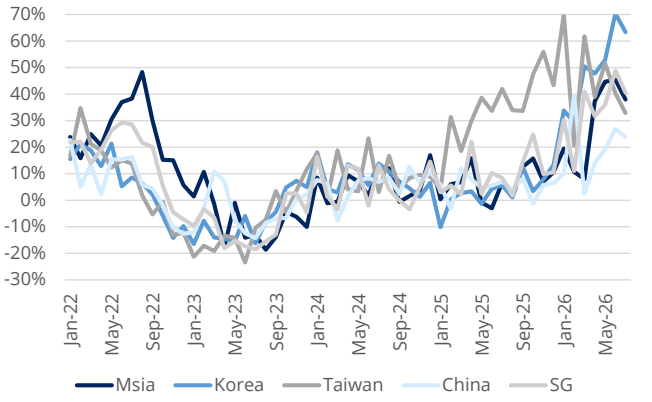
In addition, Visit Malaysia 2026 is expected to contribute to stronger services exports (tourism receipts) given the extensive collaboration between the government and the private sector to promote the tourism sector. Notably, the government has allocated RM700m to ensure Visit Malaysia 2026 turns out 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



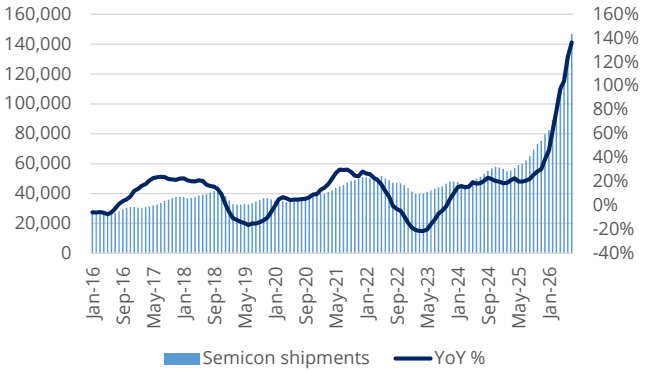
Source: AllianceDBS, CEIC

Rapid export growth for key Asian exporters



Source: AllianceDBS, CEIC

Global semiconductor shipments

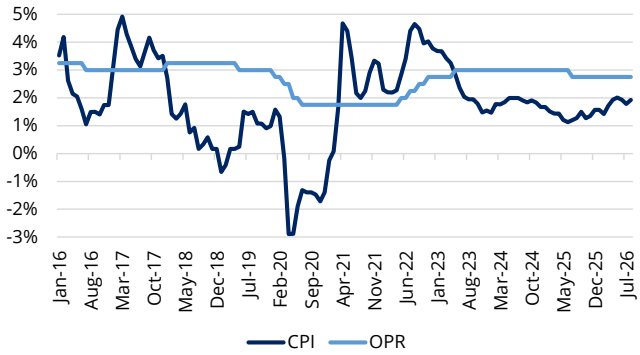


Source: AllianceDBS, SIA, CEIC

OPR normalisation likely by 1H27

In Jul 2025, BNM cut the OPR by 25bps to 2.75% as a pre-emptive measure to preserve Malaysia's growth path amid moderate inflation prospects. With 1H26 GDP growth of 5.7% and exports at their strongest in two decades, the rationale for that cut has largely played out. We therefore expect BNM to normalise the OPR by 25bps to 3.00% by 1H27, returning it to its pre-cut level. We believe the move will be well-absorbed given sustained loans growth and healthy system liquidity.

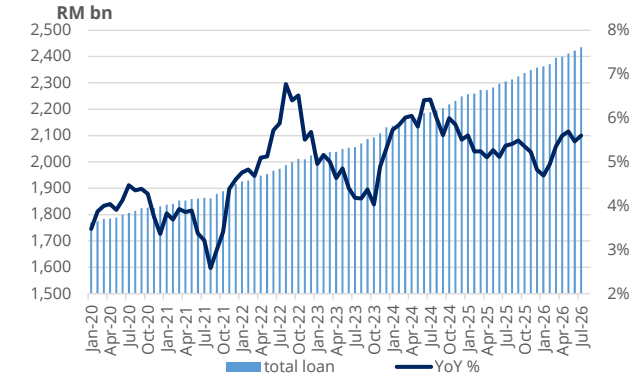
Interest rate vs inflation



Source: AllianceDBS, DOSM, CEIC

Headline inflation remained moderate at 1.9% in Aug 2026 despite the elevated crude oil prices. While the Middle East conflict remains unresolved, overall inflationary pressure is expected to be under control in the coming months, thanks to the extensive system of subsidies and price controls on essential goods like fuel and food.

Banking system loans growth

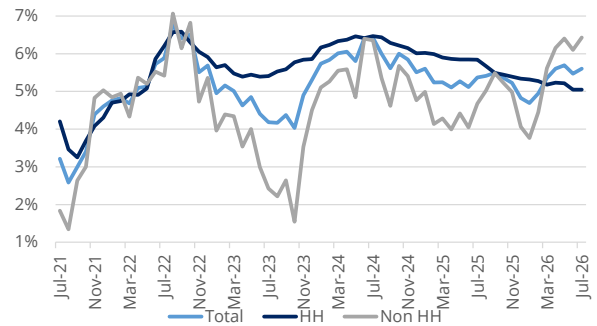


Source: AllianceDBS, BNM

Liquidity conditions remain healthy

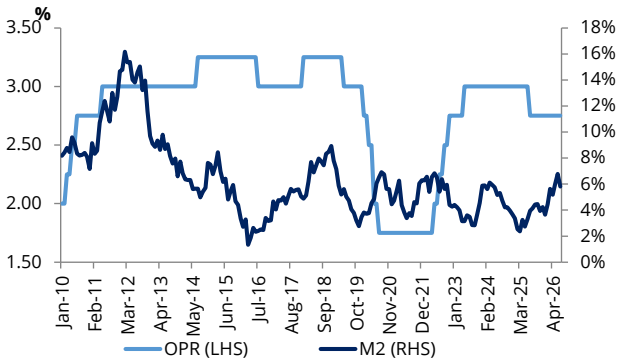
Malaysia's banking system has been seeing steady credit demand with Aug 2026 loans growth coming in at 5.6% (vs 5.4% in Aug 2025). The growth momentum has held up well in recent months despite concerns of rising inflation, driven by higher loan growth from larger corporates. We believe resilient domestic demand will continue to underpin the banking sector loans growth in 2026, notwithstanding the external uncertainties.

Loans growth remains at healthy levels



Source: AllianceDBS, BNM

Healthy liquidity condition in the economy



Source: AllianceDBS, BNM

Meanwhile, M2 money supply was strong at 5.8% in Jul 2026 (3.9% in Jul 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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