20 March 2024

Global Economics & Market Strategy

BNM Annual Report 2023: Room for Optimism in 2024

- **We keep Malaysia's GDP forecast at 4.6% YoY in 2024 (2023: 3.7% YoY), versus the Bank Negara Malaysia's (BNM) projected range of 4.0 – 5.0%.**

- **With reference to the latest BNM's projection, the headline and core inflation in 2024 are expected to average between 2.0% to 3.5%, and 2.0% to 3.0% respectively. In comparison to official projected range, our in-house 2024 headline inflation projection stood at 3.3% YoY, taking into consideration upside risks from subsidy and services tax adjustments.**

- **We see the lack of impetus for BNM to tweak its policy rate level in 2024, where the Overnight Policy Rates (OPR) is likely to be maintained at 3.00%. The wide official inflation range of 2.0% to 3.5% should provide sufficient room against future price movements.**

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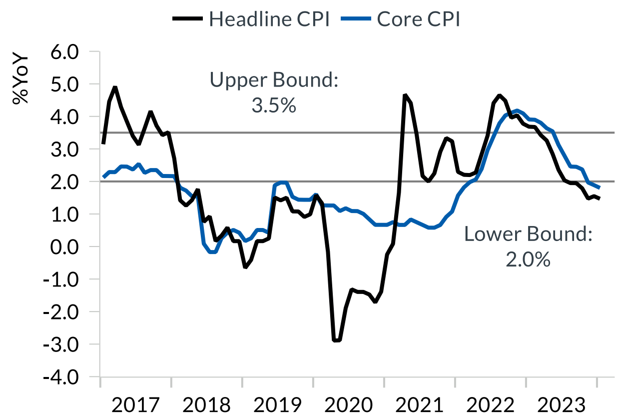
Figure 1: Malaysia's economy to expand by 4.0-5.0% in 2024, underpinned by rebound in exports and resilient consumption

	Actual	BNM	MOF	RHB
(%YoY)	2023		2024F	
Consumption				
Private	4,7	5.7	5.7	5.8
Public	3.9	3.2	2.6	3.3
Investment	5.5	6.2	6.1	6.0
Export	-7.9	4.0	4.1	4.7
Import	-7.6	4.1	3.9	4.9
GDP	**3.7**	**4.0-5.0**	**4.0-5.0**	**4.6**

Source: BNM, MOF, RHB Economics & Market Strategy.

Figure 2: BNM is likely to stay pat at 3.0% if the headline inflation fall within the projected range



Source: BNM, RHB Economics & Market Strategy.

We Maintain Our Positive View on the Economic Landscape

Overall, the central bank sounded optimistic on the economic trajectory in 2024 as Malaysia's economy would be underpinned by favourable external demand and continued resilience in domestic demand. On downside risks, the policymakers remain cautious on global developments such as prolonged high interest rates in advanced economies and escalation of geopolitical conflicts. Despite these challenges, the healthy fundamentals of the Malaysian economy would cushion the aforementioned risks.

We keep Malaysia's GDP forecast at 4.6% YoY in 2024 (2023: 3.7% YoY), versus the Bank Negara Malaysia's (BNM) projected range of 4.0 – 5.0%. Domestic confidence has shown signs of improvement. Three key proxies, specifically (1) higher manufacturing PMI, (2) increased imports of capital and intermediate goods, and (3) rising business confidence, suggest that manufacturers and businesses optimism are up. The GDP growth would be underpinned by recovery in manufacturing sector activities and improvement in trade performance. The unfolding developments i.e. strengthening of Industrial Production Index (IPI) and export momentum reinforces our view. The trade performance is expected to be underpinned by: (1) a brighter global and regional economic outlook, (2) strengthening economic dynamics of China, and (3) the re-acceleration in the global technology cycle.

We recognise opposing effects on Malaysia's GDP growth in 2024, albeit the balance of risks is tilted to the upside. The dampening effects may stem from the reduced subsidies, upward revision in services tax and the implementation of low-value goods (LVG) tax, which cap consumer expenditure and disposable income from a wealth effect perspective. However, the impact would be cushioned by (1) healthy labour demand conditions; (2) continuation of social assistance to the targeted group and (3) differing impacts across income groups where the higher income group has relatively inelastic demand.

Labour market condition remains robust with healthy job creation amid expansion in economic activities. The unemployment rate is expected to stabilise around its historical average of 3.3%. Both consumer and business confidence indexes have picked-up at the end of 2023, signalling the possibility of healthier retail and business spending going forward. Further upsides on investment activities would emanate from business-friendly policies and incentives focusing on priority sectors, i.e. technology, tourism, and agriculture, as well as those with export capacity.

We maintain our 2024 headline inflation projection at 3.3% YoY. According to our estimates, the proposed fiscal consolidation measures is projected to lift the headline inflation by 0.7%-1.1% (versus 2.5% YoY in 2023). Following the adjustments in services tax and anticipated rollout of diesel subsidy rationalisation, we expect the inflation momentum to rebound as early as 2Q24. So far, the inflation risks are cushioned by steady food prices, partially due to the continuation of food subsidies and price controls for staple food items.

We see the lack of impetus for BNM to tweak its policy rate level in 2024, considering the rosier domestic economy prospect amid uncertainties in the inflationary trajectory. The OPR is likely to be maintained at 3.00% for 2024. The wide official inflation range of 2.0% to 3.5% should provide sufficient room against future price movements. The central bank might hold its benchmark rate until there is greater clarity over the exact timeline and magnitude of fuel subsidy reform, while accessing the lagged impact on overall inflationary trajectory and economic momentum.

We expect the MYR to strengthen towards 4.5 per USD in year end. For 1H24, USD carry against MYR remains rich as market price out Federal Funds Rate (FFR) cuts, suggesting MYR would be under pressure in near term. Moving forward, our proprietary MYR model suggests that the MYR will be supported by the improvement in Malaysia's fiscal and current account balances in 2024, as well as a narrower US-MY rate differential following the anticipated FFR cuts in 2H24. We pencil that the earliest FFR cut is by September and another by December, to bring FFR to 4.75 – 5.00% versus current level of 5.25 – 5.50%.

According to BNM, the Malaysian economy is projected to grow between 4.0%–5.0% in 2024, driven by continued expansion in domestic demand with additional support emanating from the expected recovery in exports. As stated in the report, the catalysts to the economy include (1) continued employment and wage growth, (2) further progress of multi-year projects and implementation of catalytic initiatives under the national master plans, (3) improvement in tourist arrivals and tourism receipts and lastly (4) stronger trade performance. Based on the official forecast, the gross exports are expected to expand by 5% (2023: -8%), driven by the recovery in global trade, technology upcycle and higher commodity prices. On tourism, Tourism Malaysia targets 27.3 million tourist arrivals in 2024, surpassing 2019 levels of 26.1 million persons (2023:

20.1 million). Tourism activities are expected to be spurred by Government measures i.e. more tourism promotion activities abroad as well as the 30-day visa-free travel for nationals from China and India.

Meanwhile, headline and core inflation in 2024 are projected to average between 2.0% to 3.5%, and 2.0% to 3.0% respectively. The wide forecast range has incorporated the potential upside on inflation amid the anticipated implementation of fuel subsidy rationalisation. Given the sizeable share of fuel in the CPI basket, the adjustments in blanket fuel subsidies would have a material impact on the inflation outlook. The extent of upside risks would depend on the knock-on effects of the policy adjustment i.e. spillover effect to other items in the CPI basket as well as wage-price dynamics. The central bank highlighted that the risk of second-round effect from wage-price dynamic is relatively limited as wage increases are aligned with productivity growth.

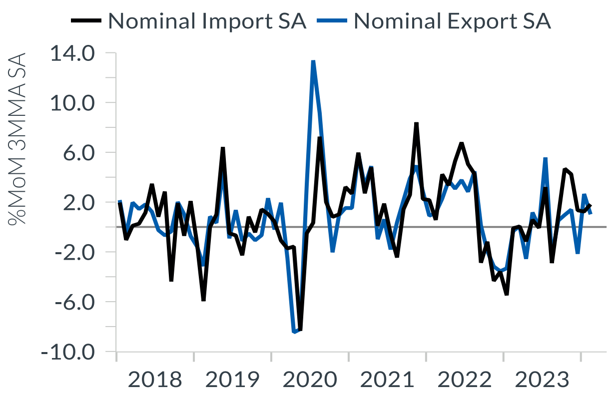
On currency, the central bank stressed that MYR is deemed to be undervalued at the current level given the sound economic fundamentals over the past two years and the resilient external sector. The policymakers further added that "the exchange rate movement is influenced by short term cyclical factors i.e. monetary policy tightening by the U.S. Federal Reserve (Fed) and shifting financial market expectations on the U.S. monetary policy outlook." The report added that "officials have intensified efforts to encourage repatriation and conversion of foreign investment income by Government-Linked Companies (GLCs) and Government-Linked Investment Companies (GLICs). In addition, there have been active engagement with the resident exporters and monitoring on the conversion of export proceeds to MYR. To reduce the U.S. dollar dependence, the officials have promoted greater use of local currency in export settlements and import payments as well."

Figure 3: Expected turnaround in manufacturing sector…

	Actual	MOF	BNM
(%YoY)	2023	2024F	
Agriculture	0.7	1.2	-0.5
Mining	1.0	2.7	3.5
Manufacturing	0.7	4.2	3.5
Construction	6.1	6.8	6.7
Services	5.3	5.6	5.5
GDP	**3.7**	**4.0 – 5.0**	**4.0-5.0**

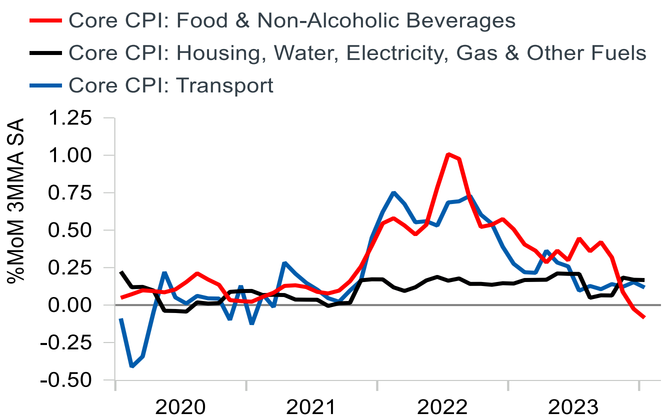
Source: BNM,MOF, RHB Economics & Market Strategy.

Figure 4: …in tandem with anticipated recovery in exports



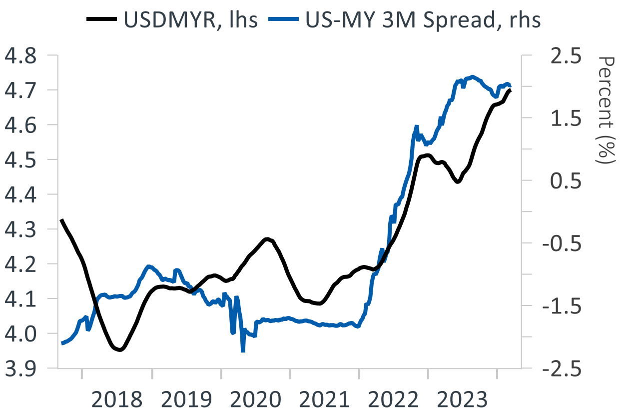
Source: Macrobond, RHB Economics & Market Strategy.

Figure 5: Inflation momentum remain steady amid stable food prices



Source: Macrobond, RHB Economics & Market Strategy.

Figure 6: Anticipated FFR cuts in 2H24 may narrow the US-MY spread and provide some support to MYR



Source: Macrobond, RHB Economics & Market Strategy.

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