Economic Research
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Malaysia

Economic growth accelerates as private consumption quickens

- **GDP expands at 4.3% y/y in third quarter, up from 4.0% in the second quarter, exceeds expectations**
- **Solid growth in private consumption and a positive trade balance underpin economic expansion**
- **Government spending falls while PMI signals tough times ahead**

The pace of economic growth in Malaysia beat market estimates, although substantial undercurrents still persist.

Malaysia's gross domestic product growth accelerated to an annual rate of 4.3% in third quarter, up from 4.0% in the second quarter. This took the year-to-date economic growth rate to 4.1%, which is at the lower end of the official GDP forecast range of 4.0% to 4.5%.

Private consumption was a key driver of the faster growth pace, with the annual rate of increase quickening marginally to 6.4%.

A sharper fall in imports meanwhile more than offset a decline in exports, which led to a positive contribution from trade towards overall GDP growth.

However, markedly slower rates of growth in government spending and gross fixed investment restrained the total economic expansion, expanding at annual rates of 3.1% and 2.0% respectively, compared to 6.5% and 6.1% in the previous quarter.

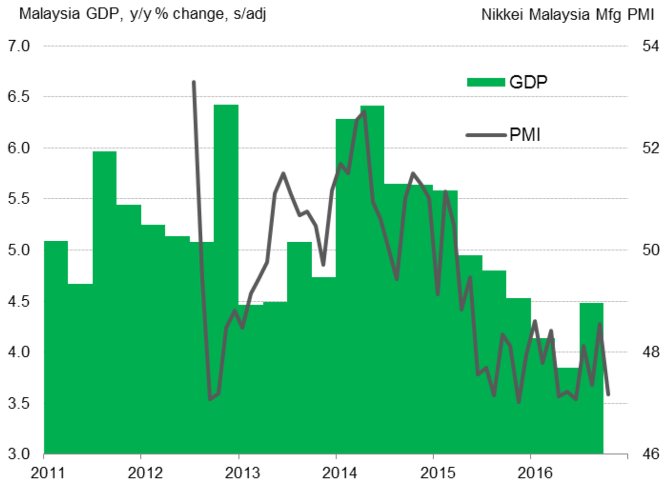
Uneven growth of various GDP components, and specifically signs of persistent weakness in the external sector, led the Bank Negara Malaysia (BNM) to cut its main policy rate for the first time in seven years during the July policy meeting.

The latest Nikkei Malaysia Manufacturing PMI has likewise signalled substantial headwinds for economic activity throughout much of 2016. This supported the case for the pre-emptive rate cut from the Malaysian central bank.

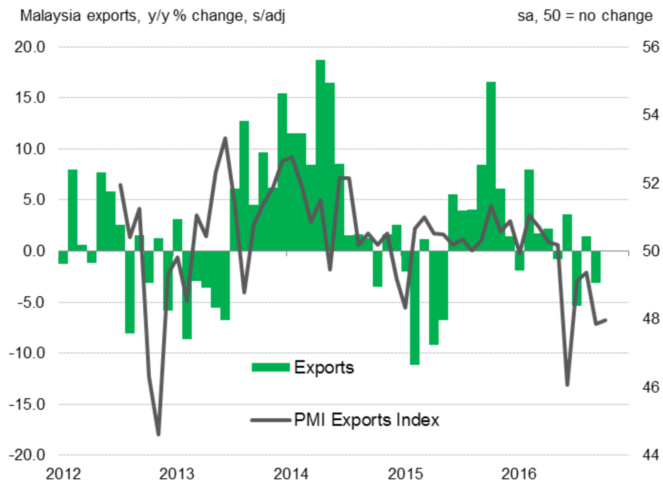
Sluggish external sector

The external sector in Malaysia has remained under pressure amid subdued global demand and low commodity prices. Within a six-year period between 2010 and 2015, the total trade-to-GDP ratio fell by more than half, from 160% to 73%.

Nikkei Malaysia PMI v GDP



Exports



Sources: IHS Markit, Nikkei, Malaysia Department of Statistics.

Lower oil prices continued to hurt export growth. In addition, a weaker ringgit contributed to the lower value of export receipts when GDP figures are denominated in local currency.

On a brighter note, the recent recovery in the global semiconductor market suggested strength in the electronics segment of Malaysian exports. Not only did the annual rate of increase in global semiconductor sales turn positive since August, growth in September was the highest since May 2015, based on statistics from the Semiconductor Industry Association.

As a whole however, prospects of foreign demand for Malaysian goods look dim, as shown by a fifth successive month of contraction in new export orders during October, according to the Nikkei Malaysia Manufacturing PMI.

Domestic demand is key growth driver

While public spending dropped in the Q3, personal consumption expenditure rose at an annual rate of 6.4%, its strongest increase in six quarters, highlighting the key role that domestic demand continues to play in sustaining economic growth.

The 2017 budget announcement of fiscal incentives for civil servants and first-time homebuyers, as well as cash hand-outs totalling MYR 6.8 billion for over half of Malaysian households, is likely to provide further support to private consumption in the coming quarters.

In addition, the projection of higher government revenues allowed the government to hike spending. Still, ongoing fiscal consolidation efforts aimed at achieving a balanced budget by 2020 may limit the expansion of fiscal policy.

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