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Media Release

RAM Ratings expects GDP growth to moderate to 4.6% in 2019 amid uncertain external demand

As the Malaysian economy continues to readjust to the changing economic landscape stemming from both domestic and external developments, its economic resilience will continue to be tested in 2019. As such, RAM Ratings expects Malaysia's GDP growth to ease to 4.6% next year, from the 4.7% projected for 2018, mostly due to uncertain external demand and the sluggish pace of investment.

Private consumption will be the main contributor of domestic demand in 2019, despite a moderation to 6.8% (2018: 7.5%) as the labour market's resilience is tested by the more challenging business climate. That said, some reprieve will come in the form of certain policy initiatives announced under Budget 2019, aimed at alleviating the B40 group's cost-of-living pressures; this segment typically shows a higher marginal propensity to consume (MPC) with additional income. Such a boost is expected to outweigh the impact from the additional taxes and levies on consumption (such as the tax on sugary drinks, overseas travel levies and the increases for certain segments of the Real Property Gains Tax), which will affect the general public and asset owners.

Although firms are still indicating positive investment intentions, the RAM Business Confidence Index (BCI) sub-index on investment sentiment is weaker for both domestic and export-oriented firms for 4Q 2018-1Q 2019. Additional cashflow relief from tax refunds to firms and other policies introduced to ease the cost of doing business next year are anticipated to facilitate the necessary "business as usual" capacity expansion, but not envisaged to spur any incremental investment beyond that. As such, we expect private investment growth to come in slightly lower next year at 4.1%, slowing from the 4.6% anticipated in 2018.

The most pronounced uncertainty stems from the external environment, although the burgeoning US-China trade war could channel potential trade diversion and Foreign Direct Investment relocation benefits to Malaysia, especially in the electrical and electronics sub-sector. Given the front-loaded restocking activities in 2018 ahead of the imposition of the major rounds of tariffs, these benefits may be preceded by short-term weakness in export performance; any upside would only be manifested in the later part of 2019. Meanwhile, export growth is projected to moderate to 1.3% next year, from the projected 1.6% for 2018.

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Although headline inflation is expected to accelerate to 2.7% next year (2018: 1.0%) amid the introduction of targeted fuel subsidies and continued Sales and Services Tax spillover effects, it is not perceived to be a key determinant of any change in monetary policy. The delicate balance between growth and capital outflow pressures will remain paramount to Bank Negara Malaysia's decision on the Overnight Policy Rate in 2019. That said, the current level of 3.25% is considered optimal at this juncture. This should lend some support to the USD/RM exchange rate next year, amid continued pressure vis-à-vis capital outflows and more subdued growth prospects, along with higher inflation and a narrower current account surplus of 2.5% of GDP (2018: 2.8%). We expect the USD/RM exchange rate to average around 4.10–4.20 in 2019, slightly weaker than the 4.00 for 2018.

The full version of *Economic Outlook 2019* is available for download on our website, www.ram.com.my.

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Date of release: 16 November 2018

Published by RAM Rating Services Berhad