Box Article

Divergence of Economic Performance and Public Sentiments

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HIGHLIGHTS

- **Despite the strong macroeconomic performance in recent years, there have been some reservations that the high GDP growth has not translated into improvements in the overall well-being of Malaysians.**
- **Factors that have contributed to this divergence include uneven distribution of income, rising cost of living, high debt obligations, deteriorating housing affordability and perceptions of corruption.**
- **Beyond macro headline figures such as GDP and inflation, greater emphasis must be placed on the distributional aspects of growth, with sharper focus on the quality of jobs created, cost of living and housing affordability.**

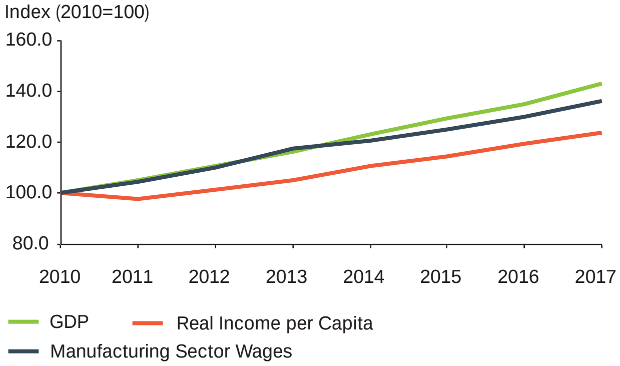
Introduction

Growth of the Malaysian economy improved significantly to 5.9% in 2017, the highest since 2014. The World Bank commended this economic performance as a "significant acceleration in growth" and expects Malaysia to "achieve high income status in the next few years" (World Bank, 2017). However, the uplifting growth narrative contrasts with the on-the-ground sentiments. In particular, the MIER Consumer Sentiment Index had consistently remained below the optimism threshold in the past three years (2014-17), the longest period that it remained below the optimism threshold. This is symptomatic of the broad-based reservations that Malaysia's strong growth performance has not translated into material improvements in the well-being of Malaysians. This article seeks to explain the paradox of Malaysia's headline macroeconomic performance and discontent among Malaysians on their economic well-being.

Uneven distribution of income

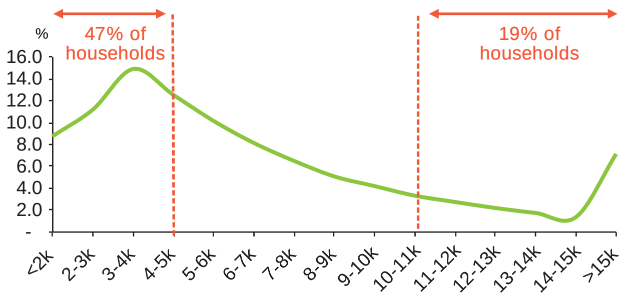
On aggregate, Malaysia's growth improvements have contributed to a steady increase in income. Real GDP grew by 5.2% per annum and income per capita rose by 3.1% per year between 2010 and 2017. This trend is also observed in the steady increase in manufacturing sector wages during the same period (Figure 1). Nevertheless, at a more granular level, it is observed that the nation's growth dividends have not been adequately distributed across all segments of society. Globally, this is a prevalent occurrence, as the world's top 1% earned twice as much as the bottom 50% between 1988 to 2008 (Milanovic, 2013). In Malaysia, while overall income inequality, as measured by the Gini coefficient, has trended lower, there is some scope to improve the nation's income distribution. In 2016, the number of households earning less than RM5,000 per month is more than double those earning more than RM10,000 (Figure 2). This partly reflects uneven job creation and wages across different skill levels. Between 2015-17, 54% of total net employment gains were in the low- to mid-skilled segments, which on average pays RM1,095 and RM1,493 monthly, respectively.

Figure 1: GDP, Real Income per Capita and Manufacturing Sector Wages (2010 Prices), 2010-2017



Source: Department of Statistics, Malaysia

Figure 2: Percentage Distribution of Households by Income Category, 2016



Source: Household Income and Basic Amenities Survey 2016, Department of Statistics Malaysia

Rising cost of living

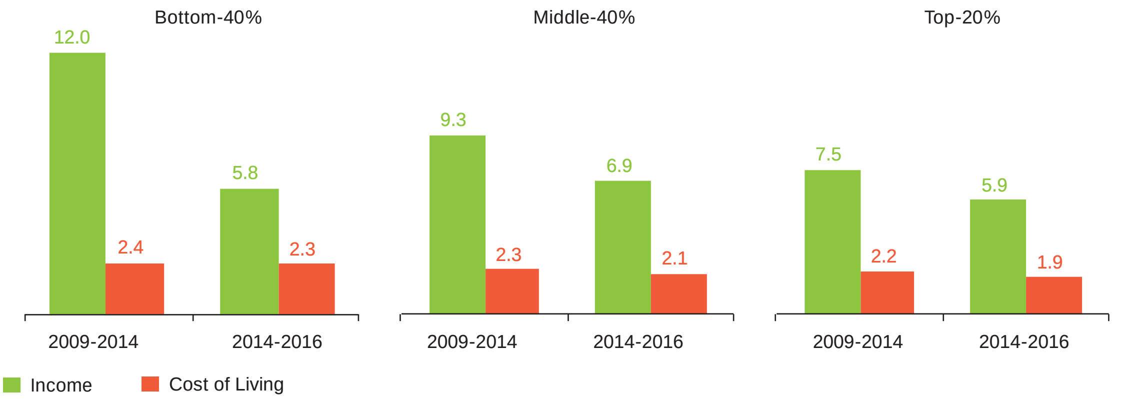
Households are also forced to grapple with higher expenditure commitments, which is one of the key factors that affect their optimism. In the past three years, multiple shocks, such as subsidy rationalisation, the introduction of GST and a weaker ringgit, have collectively led to higher cost of living. The rising cost pressures were reflected in the higher average inflation of 2.7% post-GST (Apr. 2015 – Apr. 2018), compared to the pre-GST average of 2.0% (Jan. 2009 – Mar. 2015). During the same period, following the ringgit depreciation, the cost of imported finished goods in the CPI basket also increased by 2%, compared to a smaller increase of 0.8% between Jan. 2009 – Mar. 2015.

The higher cost of living has been more profoundly felt by vulnerable and lower-income households. Notably, 35%[1] of a bottom-40[2] (B40) households' average expenditure is on food, which experienced the largest price increase during the same period (Food inflation between Apr. 2015 – Apr. 2018: 3.8%; Other expenditure: 2.3%). B40 households also experienced much slower income growth relative to higher-income households (Figure 3). As a result, these households are also more vulnerable to the increase in living costs as they have more limited income buffers. In particular, the income increase for B40 households were almost completely offset by the increase in expenditure in 2016 (Figure 4), mainly for the purchase of necessities. In contrast, households in the middle-40% (M40) and top-20% (T20) accumulated higher income buffers, due to larger income increases in level terms. This reinforces the notion that the improvement in macroeconomic conditions only benefits selected segments of the Malaysian society, which also dampens household sentiments.

[1] Refers to spending on food and non-alcoholic beverages, including food away from home.
[2] B40 households refer to households with income levels below RM4,360 (M40: RM4,361 to RM9,615, T20: ≥RM9,616) in 2016.

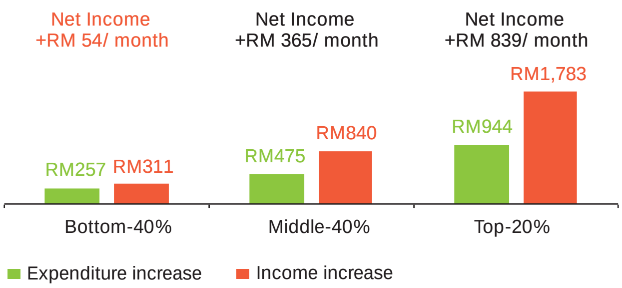
Given the uneven distribution of income and sustained increase in cost of living, some households are unable to realise their aspiration for a higher standard of living. Even a decent living standard may be unattainable for some. In 2016, up to 27% of households in Kuala Lumpur were earning below the living wage[3] required to achieve a socially acceptable minimum standard of living (Chong et al., 2018). The shortfall between living wage and current wage levels prevents households from meaningful societal participation and opportunity for personal and family development, such as festive season travel and recreational activities. This is even more prominent for the vulnerable households, given their persistently low income levels.

Figure 3: Household Income and Cost of Living Growth (%, CAGR)[4]



Source: Household Income and Basic Amenities Survey 2016, Household Expenditure Survey 2016, Department of Statistics Malaysia

Figure 4: Net Average Income and Change in Mean Household Income and Expenditure, 2014-2016



Source: Household Income and Basic Amenities Survey 2016, Household Expenditure Survey 2016, Department of Statistics Malaysia

[3] The living wage in Kuala Lumpur for a single adult is RM2,700, (Couple without child: RM4.500, Couple with two children: RM6,500)
[4] Cost of living is computed based on the share of household expenditure by category for different income groups obtained from the 2016 Household Expenditure Survey and the Consumer Price Index.

Housing affordability

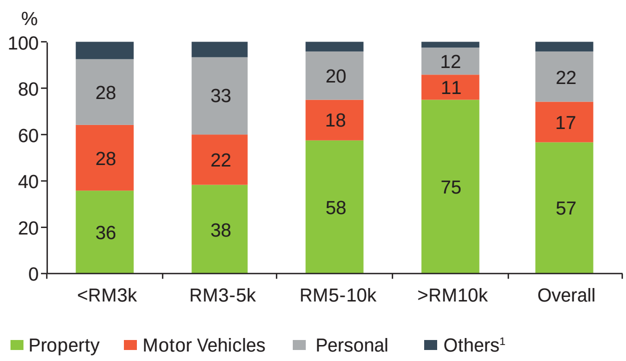
Owning a property is the aspiration of many Malaysians, as evidenced by the nation's high homeownership rate (2016: 76.3%). This Malaysian dream, however, is becoming more elusive, as houses are now less affordable across most parts of the nation. In 2016, Malaysian house prices were on average about 5 times the annual median household income (2009: 4.4 times), making houses seriously unaffordable compared to the international affordability standard of 3.0 times. Based on the median household income of RM5,228, the maximum affordable house price in Malaysia is estimated to be RM282,000 (Cheah et al., 2017). However, actual median house price was 11% higher at RM313,000.

The deterioration in housing affordability is largely attributed to supply-demand mismatches and slower income growth. On the supply front, housing construction has consistently fallen short of household demand. Between 2014-16, there was an average supply of 114,000 new houses, markedly lower than the formation of 154,000 new households. The undersupply of affordable homes is also exacerbated by the fact that recent housing launches were skewed towards the higher-end property segment, which are out of reach for many Malaysians. The supply-demand mismatch, together with the societal preference towards homeownership instead of renting, has exerted further upward pressure on house prices. Fundamentally, household income growth has also not kept up with the rise in house prices. Between 2007-16, average house prices increased by 10%, but income only grew at an average of 8%. The widening gap between income and house prices worsens the perception of rising cost of living, as housing accounts for a quarter of household spending[5].

Spending constraints resulting from elevated household debt

An additional issue weighing on Malaysians' sentiments is the elevated level of indebtedness. While household debt growth has moderated in recent years, it remains relatively high at 84.0% of GDP in 1Q 18. Despite recent income gains, the financial position of households has not improved significantly, as a sizeable portion of household income is directed to service debt obligations. Between 2014 and 2016, the debt service ratio of Malaysian households had increased from 30.9% to 32.7%. High debt burden is more prevalent among the lower-income households, accounted mostly by personal and motor vehicle loans (Figure 5). For 21% of households earning less than RM3,000, more than 60% of their income is used to repay debt (Figure 6) (Borhan et al., 2018). This situation directly affects sentiments and future spending decisions - the current accumulation of debt is akin to reducing consumption in the future. Highly indebted households are also less optimistic about their economic well-being, as they are more vulnerable to income and expenditure shocks.

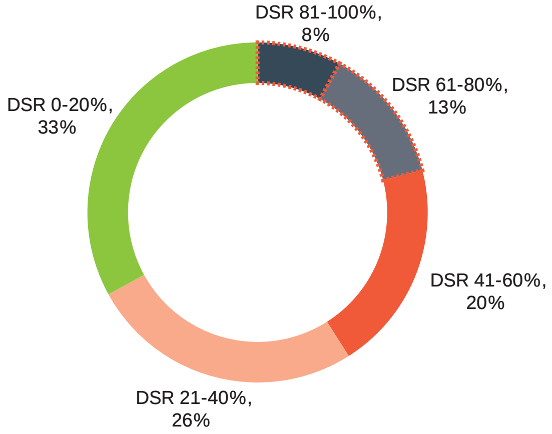
Figure 5: Household Debt by Purpose and Income Group, 2016



[1]Refers to securities and others
Source: Bank Negara Malaysia

[6] Department of Statistics, Malaysia – Household Expenditure Survey 2016

Figure 6: Debt Service Ratio (DSR) of Households Earning Less than RM3,000, 2016



Source: Bank Negara Malaysia

Perception of corruption and high exposure to negative news

The perception of corruption and frequent exposure to negative news are also factors that affect the sentiments of Malaysians on the economy and the state of the nation. Between 2015 and 2017, Malaysia experienced a steady fall in the ranking of the Transparency International Corruption Perception Index to 62nd in 2017 (2015: 54th). The perception of corruption weakens the belief among households and businesses of fair opportunities to pursue their economic aspirations. Of greater concern, studies have shown that corruption could negatively affect economic well-being through higher income inequality[6] (Gupta et al., 2002). Additionally, households are also continuously exposed to a steady flow of negative news, particularly in social media, which often stand in stark contrast to news reports in mainstream media. This fuels further scepticism over the strength of the Malaysian economy.

Conclusion

Across most economic and social metrics, it is apparent that the Malaysian economy has performed considerably well. However, there are critical gaps felt by vulnerable segments in the society, particularly the B40 and lower M40 households, which must be addressed. An immediate policy priority is to ensure that the strong economic performance will lead to better economic outcomes for all, and not just selected segments of society. If left unacknowledged and unaddressed, this gap could widen, fuelling discontent, leading to future imbalances and an undesirable outcome of uneven prosperity.

On a promising note, Malaysians are exhibiting a high degree of optimism that has not been observed in years. Consumer sentiments recently hit a 20-year high in 2Q 2018. The Malaysian economy is expected to continue on a steady growth path, with strong fundamentals supported by positive domestic and external outlook. These positive tailwinds provide fertile grounds for initiating deep economic and structural reforms, which should prioritise efforts to raise income levels across all household segments, lift productivity and wages, and improve housing affordability. This is indeed the country's opportunity to achieve higher-quality economic growth that is sustainable and beneficial to all Malaysians.

[6] Income inequality as measured through the Gini coefficient, is assessed to increase by 0.11 points when corruption worsens by 1 standard deviation.

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