Macroeconomic Outlook

HIGHLIGHTS

- Global growth to expand at a faster pace in 2018, supported by continued growth in advanced economies and improvements in emerging market economies.
- The Malaysian economy is expected to remain favourable in 2018.
- Going forward, inflation is expected to moderate due mainly to a smaller contribution from global cost factors and a stronger ringgit compared to 2017.

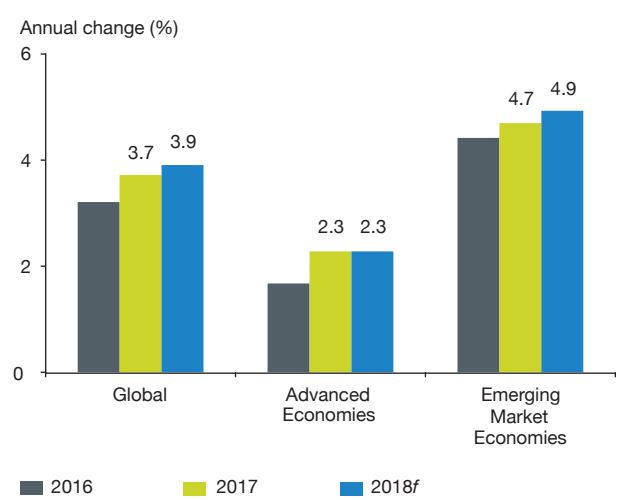
Global growth to expand at a faster pace

The sustained strong performance of the global economy in 4Q 2017 suggests that the current phase of expansion is likely to continue going into 2018. Of significance, the IMF revised its 2018 global growth projections upwards for the third time in its January 2018 publication of the World Economic Outlook Update.

The outlook is underpinned by expectations for continued synchronised expansions in both the advanced and emerging market economies. In the advanced economies, leading economic indicators such as purchasing managers' indices (PMI), manufacturers' orders and capital spending intentions surveys point towards continued expansion in business spending by corporations and smaller firms. Economic activity is projected to be further supported by favourable labour market conditions, continued access to financing and the implementation of pro-growth policies. In the US, the passing of the Tax Cuts and Jobs Act in December 2017 is expected to provide additional impetus to domestic demand, with positive spillovers to the rest of the world. Strong external demand will continue to benefit Asian economies. In addition, recently announced fiscal measures, including higher infrastructure spending, will complement the strength in domestic demand in several regional economies.

Global economic activity to expand at a faster pace in 2018

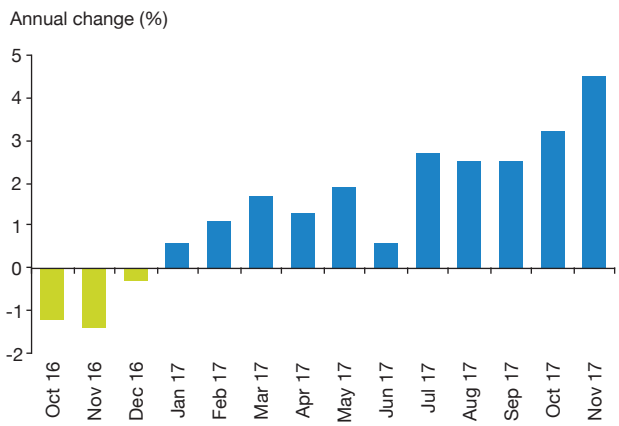
Chart 33: GDP Growth



Source: IMF World Economic Outlook (January 2018)

Leading indicators suggest continued expansion in the domestic economy

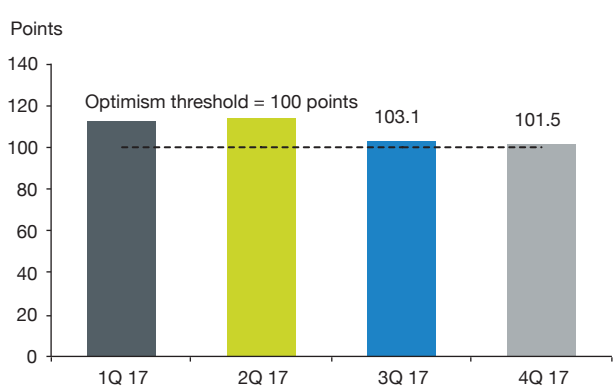
Chart 34: Composite Leading Index



Source: Department of Statistics, Malaysia

Business sentiments remained above the optimism threshold in 4Q 2017

Chart 35: MIER Business Conditions Index



Source: Malaysian Institute of Economic Research (MIER)

Risks to the growth outlook have become more balanced. Upside risks to the forecast include higher-than-expected investment growth due to the tax cuts in the US, stronger wage growth in the advanced economies and a continued expansion of the global tech cycle. In contrast, downside risks to the outlook arise mainly from uncertainty regarding the timing, pace and magnitude of monetary policy normalisation in major economies in the event of stronger inflationary pressures and wage growth, the lingering risk of rising trade protectionism and residual political risks in certain European countries. A sudden escalation of geopolitical tensions, abrupt corrections in the global financial markets and significant reversals of capital flows in emerging markets also pose additional downside risks to the global growth outlook.

Growth in the Malaysian economy to remain favourable in 2018

Malaysia registered a strong growth of 5.9% in 2017 (2016: 4.2%). For 2018, growth is expected to remain favourable with domestic demand continuing to be the key driver of growth. The positive growth momentum will continue to benefit from spillovers from better global growth on to domestic economic activity.

The Department of Statistics Malaysia's composite leading index has shown a sustained increase in recent periods. The MIER Business Conditions Index also points towards sustained expansion of the economy. Overall, the assessment is for growth to remain strong in 2018.

On the supply side, the manufacturing and services sectors are expected to benefit from continued growth across both export- and domestic-oriented sub-sectors. The agriculture sector's growth will be driven by further improvements in CPO yields and the maturing of oil palm trees. Growth in the mining sector is projected to be supported by higher output from new oil and gas facilities. In the construction sector, growth will be mainly supported by new and existing civil engineering projects.

Going forward, inflation is expected to moderate due mainly to a smaller contribution from global cost factors and a stronger ringgit compared to 2017

While global oil prices are expected to be higher in 2018, the magnitude of increase would likely be smaller compared to 2017. The impact of higher global oil prices on domestic fuel prices will also be partly offset by a stronger ringgit exchange rate. As such, the contribution of domestic fuel prices to headline inflation in 2018 will be smaller leading to a moderation in headline inflation.

Underlying inflation, as measured by core inflation, is expected to moderate following the expectation of smaller spillovers from external and domestic cost factors and a stronger ringgit. Upward pressures from the robust demand condition will be contained by continued spare capacity in the labour market and on-going investment for capacity expansion.

For 2018 as a whole, while the expectation is for inflation to moderate, the trajectory will remain dependent on the trend of global oil prices, which is highly uncertain.