



BANK NEGARA MALAYSIA
CENTRAL BANK OF MALAYSIA

Economic and
Monetary Review

2021

EMR

Contents

Foreword

Key Highlights

11 **Executive Summary**

17 **Economic, Monetary and Financial Developments in 2021**

40 *Box Article: An Anatomy of Inflation: Effects from the Prolonged Pandemic*

55 **Outlook and Policy in 2022**

72 *Box Article: Recovery Prospects in the Global Economy: Lessons from a
Corporate Balance Sheet Perspective*

Annex

Glossary, Acronyms and Abbreviations

Foreword

The year 2022 is set to be a watershed year as most countries progressively transition towards endemic management of COVID-19. The outcomes from the economic disruptions over the past two years have led to new challenges that require a rethinking of policy strategies. At present, there remains great uncertainty surrounding the medium-term outlook for the global economy, stemming mainly from the extent of economic scarring and how these would eventually interact with post-pandemic structural shifts such as greater digital adoption. The transition path towards a greener economy will also have an important bearing on the outlook. In the near-term, such shifts may lead to some trade-offs between short-term growth and inflation in order to secure a more sustainable growth in the medium-term. As the global economy is expected to continue its recovery path, policymakers will have to adjust their policy settings against a background of rapidly evolving uncertainties, including the military conflict in Ukraine which began in February. This complicates the task of assessing the economic and financial implications of such developments. These uncertainties have also resulted in heightened global financial market volatility, with significant implications on emerging market economies. Policy formulation will, therefore, continue to be data-dependent as developments evolve.

For Malaysia, the pace of economic recovery is projected to gather further momentum amid the reopening of the economy and international borders. While we are not yet out of the woods, we are better prepared now. The better COVID-19 management and higher vaccination rates will help mitigate the adverse impact from future resurgences and thus protect our healthcare system from being overwhelmed. With these factors in mind, we expect less disruption to economic activity and spending in the event of resurgences. As an open economy, Malaysia will continue to benefit from the expansion in global demand, which would support both investment activity and the labour market. Overall, for 2022, growth is expected to expand between 5.3% and 6.3%.

Monetary policy will remain accommodative to support a sustainable economic recovery while ensuring price stability. The unprecedented conditions that warranted the significant monetary support during the height of the pandemic have since abated. With the policy rate at its historical low, we are cognisant of the consequences of keeping interest rates low for an extended period. Global experience has shown that this could lead to an unhealthy build-up in financial imbalances. As the recovery is gaining strength, we must have the discipline and foresight to begin rebuilding policy buffers for future shocks. Recently, there have also been concerns surrounding the risks to domestic inflation stemming from elevated commodity prices amid prolonged supply disruptions and the military conflict in Ukraine. Given that the outlook for inflation remains largely supply-driven, we are closely looking out for any signs of potential second-round effects, where price pressures could become more entrenched as domestic demand recovers. Ultimately, any potential adjustments to the degree of accommodation will remain data-dependent and be undertaken in a measured and gradual way that is commensurate with the appropriate level of support needed by the economy.

In securing a durable recovery, it is imperative that the overall configuration of the Bank's policies does not lose sight of longer-term economic sustainability. This underpins the Bank's policy considerations in discharging its monetary and financial stability mandates. Policies are forward looking and pre-emptively calibrated with the aim of managing immediate risks and minimising future vulnerabilities to ensure sustainable growth across economic and business cycles. Equally important is for the Bank to ensure that it continues to have sufficient policy space that can be utilised over time to deliver on its mandates. Over the past two years, the Bank, together with the financial sector, have stepped up to provide various forms of financial support, including repayment and financial assistance to affected groups who may need more time to get back on their feet. With the targeted assistance still in place, small- and medium-sized enterprises (SMEs) and other affected groups will continue to have access to financial support as they resume their activities. As the domestic economic

recovery takes hold, strategies must now evolve to account for the medium-to-long run implications of current policy settings. We must learn from the past experiences of other economies that suffered from the lost decade phenomenon, which underscore the importance of timely recalibration of policies, as well as cohesion in overall policy settings. The failure to account for such risks could be very costly for long run economic growth. Moving forward, policy measures should aim to reinstate market mechanisms to foster business dynamism and refocus on strengthening Malaysia's long-term growth prospects. Importantly, gains from past financial sector reforms which have proven crucial in supporting the economy through this challenging period must not be eroded to secure future financial and monetary stability.

Looking beyond 2022, the economic and financial landscape is likely to evolve and test the resilience of our existing policy frameworks. The Bank is currently reviewing its monetary policy framework to ensure that it remains relevant in safeguarding price stability that continues to promote sustainable growth. The health crisis has led to behavioural and structural shifts among households and businesses, with important implications to economic and financial linkages. Key elements of change on the horizon include the accelerated pace of digital technology and the shift towards greater market-based financing. As such, the review will deep dive into key areas that would have implications to the conduct of monetary policy such as the digitalisation of finance, monetary policy communications and outreach, and climate change among others. Ultimately, this review is expected to provide refinements to elements of our existing monetary policy framework to enhance the Bank's ability to achieve its monetary stability mandate across time.

Going forward, well executed structural reforms are needed to address the critical challenge of reinvigorating growth opportunities and strengthening our economic fundamentals. We must also remember that economic policies do not exist in a vacuum. Policies that are in place today will impact the future economic landscape and have a bearing on the efficacy of counter-cyclical policies, including monetary policy. For example, existing policies, such as the price ceiling on domestic retail fuel prices and price controls on selected fresh food items, have undoubtedly provided temporary relief to cost pressures. However, such policies have long run costs as artificially depressed prices will eventually distort consumption and production decisions and have adverse implications to longer-term productivity. Such measures will also weigh on the Government's fiscal position and involve trade-offs to spending on other important development areas. To address these issues, longer-term solutions that enhance productivity and incomes must be in place to help the Malaysian economy maximise on such efficiency gains. From this example, it is clear that the Bank's monetary and financial policies alone would not be sufficient to accelerate these underlying drivers of growth, which are more dependent on other forms of economic policies to secure broader macroeconomic outcomes.

For Malaysia to emerge stronger and more resilient, it is important for us to maintain focus and prioritise on the key areas of structural reforms. The shift towards higher quality investments is essential and must be done in tandem with the development of a future-ready workforce, acceleration of social protection reforms, and rapid adoption of automation and digitalisation. The continued push to adopt the Environmental, Social and Governance (ESG) agenda is also critical, particularly to ensure Malaysia remains globally competitive, whilst building a more sustainable and resilient future. It is commendable that the Government has initiated efforts on these fronts, particularly in the Twelfth Malaysia Plan (12th MP) and 2022 Budget. We welcome these efforts and see strong potential to accelerate the implementation of these reforms in the immediate horizon. As Malaysia continues to respond and recover from the effects of the pandemic, it is vital to nudge the process of creative

destruction as businesses seek to pivot and reconfigure in these post-pandemic times. The existing approach of adopting blanket measures could potentially result in a loss of future growth in years to come. Such risks could become imminent if we do not stay focused and expedite our efforts on these reforms. Our experience with instituting financial sector reforms after the Asian Financial Crisis (AFC) has shown that it is possible to push through difficult but necessary reforms which have enabled us to reap the benefits today.

In carrying out structural reforms, the Bank acknowledges the realities confronting domestic policymakers. The challenge lies in balancing the need to continue providing policy support amid an uneven economic recovery, and rebuild policy buffers, while expediting structural reforms that require strong commitments from all stakeholders. Given this, Malaysia urgently needs a comprehensive roadmap on the prioritisation, sequencing and execution of reforms that cuts across both public and private sectors. The Bank's role in supporting these structural reforms is to ensure that the financial system can facilitate the intermediation needs of transformation, which has been reflected in the recently announced Financial Sector Blueprint 2022-2026.

I firmly believe that the Malaysian economy would be able to continue to prosper. Our prospects remain highly contingent upon our policy actions today. By ensuring an enabling and competitive economic environment, Malaysia will be well-positioned to benefit from new growth opportunities, which will prepare us to face new challenges in a post-pandemic world.



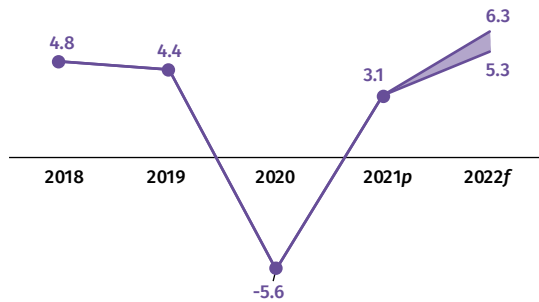
Nor Shamsiah Yunus

30 March 2022

Key Highlights on Economic Development and Outlook

Firmer recovery in Malaysia's GDP in 2022...

Real GDP growth (Annual change, %)



p Preliminary
f Forecast

Key drivers of growth in 2022 (Annual change, %)

Demand

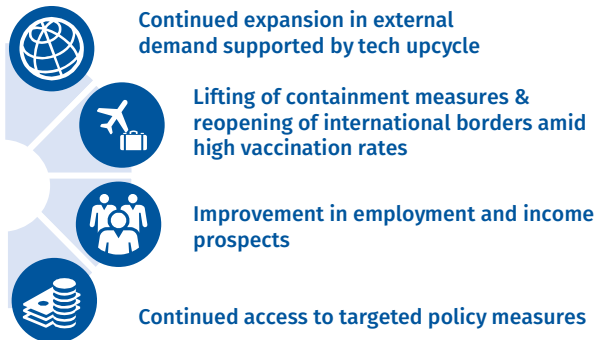


Supply



...supported by external and domestic factors amid a challenging environment

Major Contributors to Growth

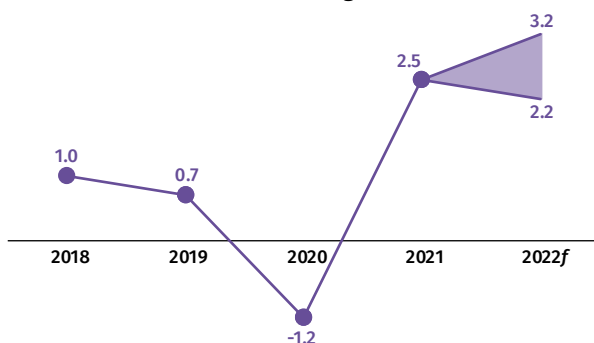


Key Challenges

- ▶ **COVID-19 pandemic developments**
Emergence of vaccine-resistant variants causing a resurgence
- ▶ **Ongoing geopolitical conflicts**
Commodity price shocks and disruptions to supply chain and trade
- ▶ **Elevated cost and price pressures**
Cost of living and profitability concerns weighing on household and business sentiments

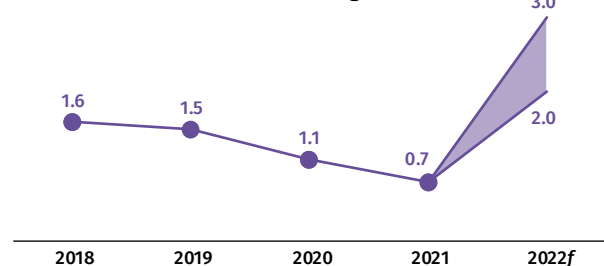
Headline inflation to average between 2.2% and 3.2% in 2022 amid higher core inflation

Headline inflation (Annual change, %)



f Forecast

Core inflation¹ (Annual change, %)



f Forecast

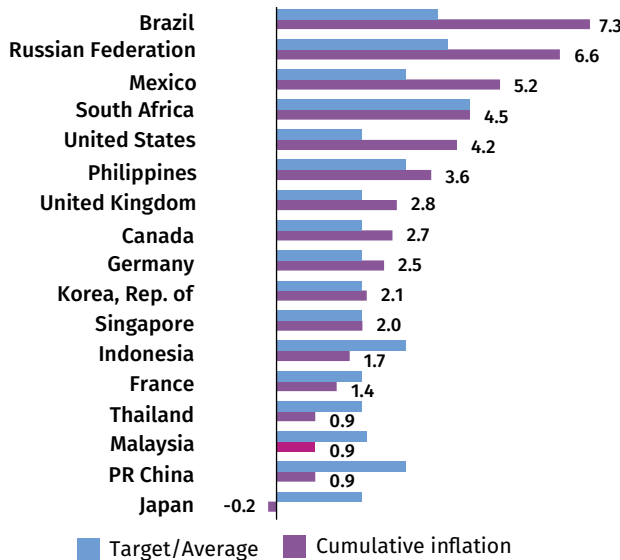
¹ Core inflation is computed by excluding price-volatile, price-administered items and the direct impact from consumption tax policy changes

Key Highlights on Box Articles

An Anatomy of Inflation: Effects from the Prolonged Pandemic

While higher CPI inflation is common globally, country-specific factors have partly contained the extent of inflationary pressure in Malaysia at this juncture

Cumulative CPI Inflation (Dec19 to Dec21; Annualised %)



Factors that could contain inflationary pressures for Malaysia:

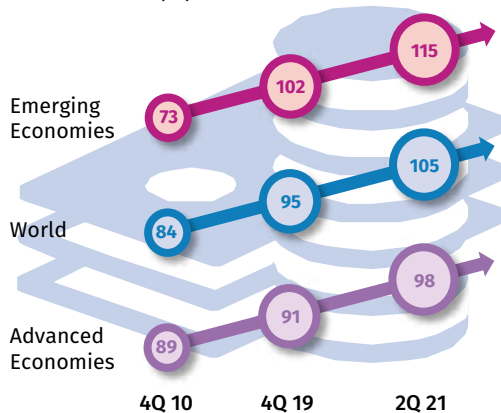
- 1 Continued spare capacity in the economy** amid a gradual recovery
- 2 Policy interventions** such as price ceilings
- 3 Relatively less severe disruptions**, reflecting factors such as proximity to global manufacturing hub

Source: National authorities and Bank Negara Malaysia estimates

Recovery Prospects in the Global Economy: Lessons from a Corporate Balance Sheet Perspective

Corporate debt has increased with higher financing needs during the pandemic

Corporate debt Share of GDP (%)



Critical to balance between short- and long-term economic goals

Timely, Direct, and Proportionate Policy Support

Unprecedented policies cushioned the downturn but requires recalibration as demand conditions improve.

Structural Reforms to Enhance Economic Resilience

Labour market flexibility and stronger insolvency laws could expedite resource reallocation and increase productivity.

Well-Capitalised Banks to Ensure Macroeconomic and Financial Stability

Healthy bank balance sheets disincentivise continued lending to zombie firms.

Source: Bank for International Settlements (BIS) Credit Database

Executive Summary



Executive Summary

Economic and Financial Developments in 2021

The global economy rebounded in 2021 from the pandemic-induced recession in 2020 with an uneven recovery: The global economy and trade rebounded by 5.8% and 9.3%, respectively. However, this recovery was uneven, especially between Advanced Economies (AEs) and Emerging Market Economies (EMEs). While new COVID-19 variants affected most economies, more advanced vaccination progress in AEs allowed for a quicker lifting of containment measures and thus, a faster rebound in economic activity. Together with stronger demand, labour shortages in several AEs and supply chain disruptions raised logistics and input prices, resulting in higher inflationary pressures in the second half of 2021. Amid this backdrop of higher inflation, some central banks began to normalise monetary policy. Inflation in Asian EMEs, however, remained muted, resulting in continued monetary accommodativeness in the region.

While domestic financial conditions were tighter, the spillovers to financial intermediation were contained: The domestic financial market movements were influenced by both external and domestic factors, which contributed to intermittent volatility in portfolio flows, elevated pressure on Malaysian Government Securities (MGS) yields, subdued equity prices, and ringgit volatility. Nonetheless, market adjustments were orderly, underpinned by Malaysia's deep and liquid financial markets and supported by the Bank's liquidity and foreign exchange operations. In addition, the strength and resilience of Malaysia's banking system anchored the effective intermediation of funds in the economy. The flexibility in the ringgit exchange rate also facilitated the appropriate adjustments in the external sector.

The Malaysian economy improved in 2021, registering a growth of 3.1%: The recovery momentum in the early part of the year was affected by the reimposition of nationwide containment measures from June to September 2021, following a rapid resurgence of cases due to the Delta variant. However, unlike the movement restrictions in the second quarter of 2020, more essential economic sectors were allowed to operate, while businesses and households were better adapted to the containment measures and standard operating procedures (SOPs). Notwithstanding this, some sectors, such as high-touch services, tourism-related industries and construction, were slower to recover due to continued restrictions on movement and operating capacity. As these restrictions were eventually lifted in October 2021 amid rapid progress in domestic vaccinations, economic activities picked up and labour market conditions improved. The expansion in employment and subsequent increase in private sector wages contributed towards increased household spending. Private investment growth was supported by expansion in productive capacity, especially in the *manufacturing* sector, alongside higher capital spending by firms on automation and digitalisation. In addition, external demand also provided additional support to our economic growth in 2021.

Headline inflation turned positive in 2021 while core inflation remained subdued: Headline inflation in 2021 increased to 2.5% (2020: -1.2%), reflecting mainly higher fuel inflation. Global supply-side disruptions also led to some upward price pressures, though the impact on consumer prices was relatively contained, as firms absorbed the higher cost. Underlying inflation, as measured by core inflation, remained relatively subdued at 0.7% in 2021 (2020: 1.1%), reflecting the spare capacity in the economy amid a moderate recovery in the labour market.

In 2021, accommodative monetary policy provided continuous broad-based support for economic recovery: The Overnight Policy Rate (OPR) was maintained at the historical low of 1.75% throughout the year. The thrust of monetary policy in 2021 was to ensure sustainable economic growth in an environment of manageable price pressures. Additionally, the extension of the Statutory Reserve Requirement (SRR) flexibility from 31 May 2021 to 31 December 2022 provided sustained liquidity support for financial intermediation throughout the year. Financial measures, such as credit guarantees and the Bank's various financing facilities, also provided targeted support for affected segments that were facing a more uneven recovery. Overall, financing remained supportive of the economic recovery, with continued flow of bank credit to households and businesses.

Outlook and Policy for 2022

Continued recovery in the global economy as countries gradually transition towards normalcy, albeit at varying degrees: In 2022, PPP-weighted global growth and Malaysia's export-weighted global growth are projected to expand between 3.8% and 4.3%, and between 4.0% and 4.5%, respectively. The improvement in labour market conditions amid the progressive reopening of economies over the past year is expected to facilitate recovery in private sector activity in 2022. The impact of resurgences of COVID-19 remains a key risk but is expected to be smaller in 2022 than in 2020 and 2021 due to factors such as continued good progress in vaccinations, among others. Nevertheless, the ongoing military conflict in Ukraine is expected to weigh on global growth. Spillovers would stem mainly from disruptions in commodity supply, leading to higher commodity prices and inflation which could raise cost pressures on firms and lower real income for households.

Global inflation is projected to rise and remain elevated in 2022: This is driven by higher energy and commodity prices and ongoing disruptions in the global supply chain in an environment of sustained demand recovery. Amid continued strength in inflationary pressures globally, a further normalisation of monetary policy is anticipated in 2022 for most central banks in both AEs and EMEs. Nonetheless, the pace and magnitude of monetary policy normalisation remain uncertain, as they depend largely on the persistence of inflationary pressures and the strength of the recovery in the economy and labour market.

Balance of risks to global growth remains tilted to the downside, amid heightened geopolitical tensions and continued uncertainties surrounding COVID-19: The main risk to growth arises from a potential reimposition of strict containment measures in the event of a COVID-19 resurgence due to severe and vaccine-resistant Variants of Concern (VOCs). This could result in higher and more persistent inflation, which extreme weather conditions and disruptions in the production of commodities could exacerbate. Downside risks also arise from slower-than-expected recovery in China and worsening geopolitical conflicts, particularly if the conflict in Ukraine continues to escalate further and is prolonged, or if trade and financial sanctions are intensified. Moreover, tighter global financial conditions risk sharp capital outflows, which could lead to disorderly exchange rate adjustments and the unwinding of prevailing financial sector imbalances. Nevertheless, there are upside risks to global growth, arising from a faster and wider rollout of COVID-19 vaccines, new treatment options for COVID-19 infections, and additional fiscal support particularly in AEs.

The Malaysian economy is expected to improve further, with growth projected to be between 5.3% and 6.3% in 2022: The economic recovery is underpinned by the continued expansion in external demand, full upliftment of containment measures, reopening of international borders, and further improvement in labour market conditions. In addition, the implementation of investment projects and targeted policy measures will provide further support to economic activity and aggregate demand.

Stronger private sector recovery, supported by labour market improvements, to be the main driver of growth in 2022: As economic activity picks up, the unemployment rate is expected to decline further in 2022 to around 4% of the labour force. The recovery in the labour market will be further supported by targeted measures to boost labour demand, facilitate re-skilling and up-skilling and reduce labour market frictions. A sustained recovery in employment and income is expected to drive an improvement in household spending. Additionally, progress in vaccinations and upliftment of containment measures will lead to an improvement in consumer confidence and some materialisation of pent-up demand. As a result, private consumption is expected to grow by 9.0% (2021: 1.9%). Private investment is also expected to recover, growing by 5.3% (2021: 2.6%), supported by the continued expansion in global demand and the implementation of new and ongoing investment projects.

Targeted policy measures to remain in place to facilitate recovery momentum: With an emphasis on assisting vulnerable segments, various policy measures will play a key role in supporting a broader economic recovery. Government measures to provide some support to household spending include various cash transfers and tax reliefs. For businesses, the Wage Subsidy Programme and numerous targeted grants are extended to vulnerable sectors such as tourism-related industries and agriculture.

Overall, the risks to domestic growth are tilted to the downside: The potential reimposition of broad-based containment measures due to a resurgence in COVID-19 such as the emergence of severe and vaccine-resistant VOCs is a key downside risk. In addition, slower-than-expected rollout of public infrastructure projects, more persistent labour shortages and supply disruptions, and higher-than-expected inflation could also affect the recovery path. On the external front, worsening supply chain disruptions, heightened volatility leading to disorderly financial conditions, as well as prolonged and further escalation of geopolitical tensions could significantly affect Malaysia's growth and trade outlook. Nevertheless, higher-than-expected global growth and stronger-than-expected improvement in tourism-related sectors amid reopening of borders pose an upside risk to domestic growth.

Headline inflation to average between 2.2% and 3.2% in 2022 amid higher underlying inflation: Fuel inflation, which contributed to higher inflation in 2021, is expected to moderate in 2022. While high input costs are projected to exert some pressures on selected fresh food prices, these pressures will be partly mitigated by price controls. Meanwhile, core inflation is expected to average higher between 2.0% and 3.0% in 2022 due to stronger demand conditions amid lingering cost pressures. For most items in the core CPI basket, the price pressures in 2022 would largely reflect a normalisation in prices after a period of subdued demand and reduced profit margins during the pandemic. However, the extent of upward adjustments in core inflation will remain partly contained by the continued slack in the economy and labour market. The upside risks to the overall inflation outlook stem mainly from cost-push factors, such as a more persistent uptrend in input costs and prolonged global supply chain disruptions, which geopolitical tensions and lockdowns in China could exacerbate. Meanwhile, downside risks to the outlook mainly reflect factors that could precipitate a weaker

recovery in economic conditions, leading to more benign price pressures.

Domestic monetary and financial conditions to remain conducive to financial intermediation activities: The lending capacity of Malaysian banks remains intact, given their healthy capital and liquidity buffers. With the improving economic conditions, credit flows to the private sector are expected to pick up during the year amid banks' strong capacity and improved willingness to lend, coupled with higher demand for financing by households and businesses. There are, however, heightened uncertainty and risks emanating from external developments, such as monetary policy normalisation globally and escalating geopolitical tensions. Nevertheless, continuous efforts to strengthen external buffers and economic fundamentals over the years have improved the resilience of the domestic economy and financial system, which will facilitate orderly intermediation of portfolio flows. Moreover, the impact from exchange rate fluctuations on domestic financing conditions is mitigated by low reliance on foreign currency financing and the availability of hedging facilities. The flexibility of the exchange rate would also remain as a key shock absorber to facilitate necessary macroeconomic adjustments from external shocks. Meanwhile, the Bank's monetary policy operations will ensure sufficient domestic liquidity in the financial system to support financial intermediation and the orderly functioning of the financial markets.

Monetary policy in 2022 will continue to support a sustainable economic recovery while preserving price stability: Going forward, the MPC will focus on ensuring that the degree of monetary accommodativeness is consistent with the expected improvement in economic conditions amid moderate upward price pressures and well-anchored inflation expectations. Against a background of rapidly evolving conditions and heightened uncertainties, the MPC will continue to monitor the outlook for growth and inflation, and the possibility of materialisation of risks. Considerations for continued monetary policy support would need to be balanced against maintaining low interest rates for a prolonged period, which could lead to an emergence of financial imbalances. The MPC is also mindful of the potential upside risks to inflation, which continue to be subject to global commodity price developments. While monetary policy may not be

the best tool to react to these “first-round” effects, the MPC will assess whether such price pressures could become more persistent and pervasive, and whether they would be reinforced by stronger domestic demand. Therefore, future monetary policy decisions will continue to be data-driven and guided by the evolving balance of risks surrounding

the outlook for domestic inflation and growth. Any potential adjustments to the degree of monetary accommodation would be made in a measured and gradual manner. Given the lingering uncertainties and downside risks to growth, monetary policy will remain accommodative, while preserving price and financial stability.

Economic, Monetary and Financial Developments in 2021

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Box Article: An Anatomy of Inflation: Effects from the Prolonged Pandemic

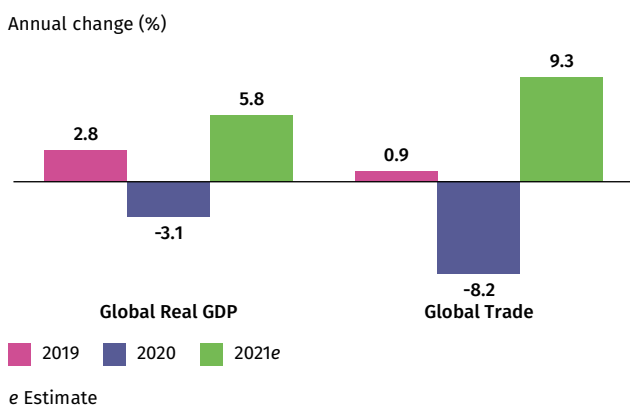
Economic, Monetary and Financial Developments in 2021

2021: MODERATE RECOVERY AMID A PROLONGED PANDEMIC

An uneven global economic recovery following periodic resurgences of COVID-19 and varying vaccinations coverage

In 2021, the global economy recovered from the pandemic-induced recession in the previous year. Developments related to the COVID-19 pandemic continued to shape the recovery path, with periodic resurgences of COVID-19 dampening the pace of the recovery. For many economies, progress in COVID-19 vaccinations facilitated the reopening and recovery of the global economy. This was further supported by a strong rebound in global trade, despite the worsening of supply chain issues. Global economy and global trade rebounded by 5.8% and 9.3%, respectively, in 2021 (2020: -3.1% and -8.2% respectively) (Chart 1.1).

Chart 1.1: Global Real GDP and Trade Growth

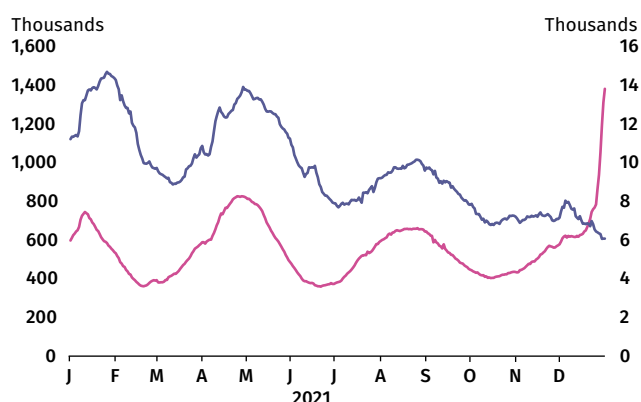


Source: International Monetary Fund (IMF) January 2022 World Economic Outlook and Bank Negara Malaysia estimates

The year started with elevated COVID-19 cases that affected many major economies. The emergence of the Delta variant in the second quarter of 2021 led to resurgences that continued throughout the rest of the year. Approaching year-end, a newer variant of concern, Omicron, caused yet another sharp resurgence in cases. Containment measures, albeit less strict than measures imposed in the second quarter of 2020, were reintroduced to manage these resurgences, affecting the pace of the recovery. The introduction of vaccines beginning December 2020, which were effective in reducing incidences of severe symptoms and deaths from COVID-19 (Chart 1.2), allowed a more sustained reopening of the global economy. However, the pace of recovery between advanced economies (AEs) and emerging market economies (EMEs) was uneven, reflecting differences in access to COVID-19 vaccines and progress of domestic vaccinations, the stringency of containment measures to curb resurgences and the degree of economic policy support.

In AEs, containment measures were tight during the first few months of the year. Nevertheless, more

Chart 1.2: Daily New Global COVID-19 Cases and Deaths (7-Day Moving Average)



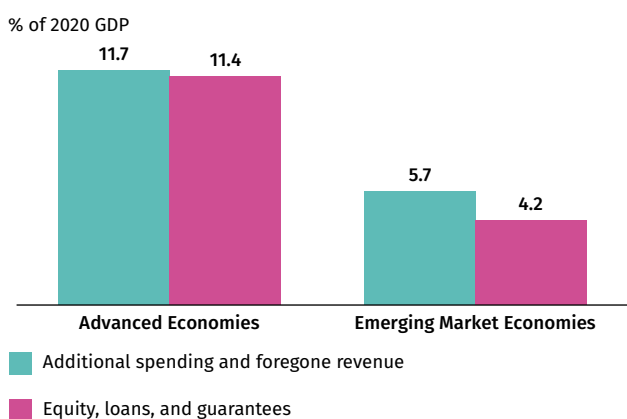
— Daily new COVID-19 cases
— Daily new COVID-19 deaths (RHS)

Source: Our World in Data

rapid progress in vaccinations allowed major AEs, such as the United States (US), the euro area and the United Kingdom (UK) to ease their stringent measures in the second quarter. This facilitated an early rebound in economic activity, especially in high-touch services activities. Large fiscal support in these economies further aided the economic recovery (Chart 1.3). In the US, there were additional cash handouts and enhanced unemployment benefits, while the European Union (EU) introduced their Multiannual Financial Framework (MFF) and NextGenerationEU recovery plan.¹

Meanwhile, EMEs maintained tighter containment measures over a longer period, given the relatively slower pace of vaccinations, delaying their economic recovery. Fiscal support among EMEs was also relatively more limited compared to AEs (Chart 1.3). In addition, several economies adhered to a ‘Zero-COVID’ policy, which saw tight containment measures introduced whenever cases were detected locally. This led to frequent disruptions to economic activity, which dampened sentiments. This was observed in the People’s Republic of China, where retail sales remained sluggish especially in the second half of the year amid repeated resurgences of COVID-19 cases. Production was also affected, albeit to a limited extent.

Chart 1.3: Discretionary Fiscal Response to COVID-19 Crisis



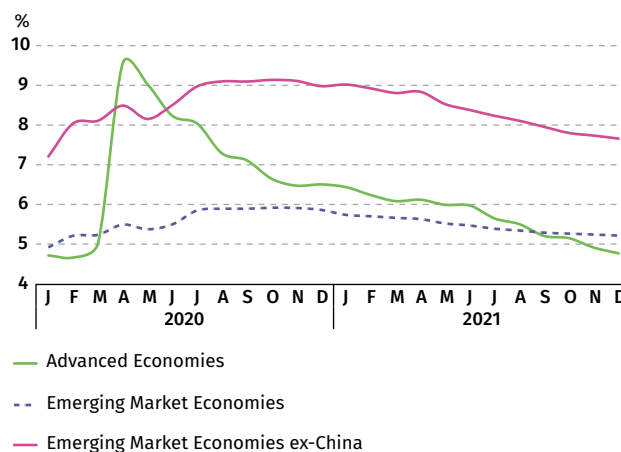
Note: Covers fiscal responses from January 2020 to September 2021

Source: International Monetary Fund (IMF) Fiscal Monitor Database of Country Fiscal Measures in Response to the COVID-19 Pandemic

¹ The MFF is the 7-year long-term budget for the European Union, with the latest MFF outlining spending between 2021 and 2027. The latest MFF includes the NextGenerationEU recovery plan, which provides additional funds to support the recovery of the EU from the COVID-19 pandemic. The budget includes fiscal support for the green and digital transitions, research and development, agricultural subsidies, and economic development support to reduce disparities between different EU regions.

Labour market conditions in AEs and EMEs recovered, albeit at different paces. Following an earlier economic reopening and more rapid rebound in domestic demand, labour conditions in AEs improved strongly in 2021. Meanwhile, unemployment remained elevated for some time in EMEs but improved towards the end of the year, following a steadier economic reopening (Chart 1.4). Nevertheless, AEs and EMEs experienced similar challenges, namely, a weaker recovery in labour force participation among vulnerable segments. Women’s participation was affected by their higher employment in the services sector, which was more impacted by the pandemic. In addition, this was compounded by increased familial and childcare needs, following closures of schools and care facilities during the pandemic.² Labour market conditions were also particularly challenging for youth, as employment among youth in many countries remained weaker than prime-age workers. Employment losses among youth not only translated into higher unemployment, but also, higher rates of discouragement and inactivity.³

Chart 1.4: Unemployment Rate



Note: Unemployment rate aggregated using PPP-weights

Source: National authorities, International Monetary Fund (IMF) and Bank Negara Malaysia calculations

² A policy brief (“An uneven and gender-unequal COVID-19 recovery: Update on gender and employment trends 2021”) published by the International Labour Organisation (ILO) provides evidence that the employment of women have been more severely affected by the pandemic. The policy brief suggests that more gender-specific policies may be needed to support a more inclusive recovery.

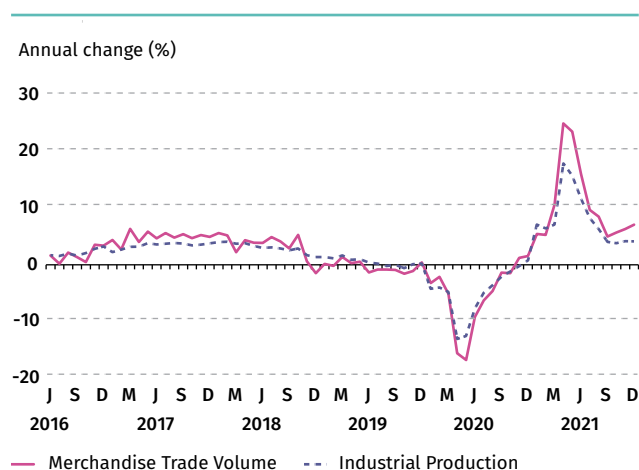
³ For further information, please refer to “ILO Briefing Note: An update on the youth labour market impact of the COVID-19 crisis” (June 2021), and “ILO Monitor: COVID-19 and the world of work. Eighth edition” (October 2021). Discouragement and inactivity are estimated by labour market exits that were not offset by participation in education and training.

Amid the resurgences and containment measures, the demand for goods was strong, especially for electrical and electronics (E&E) and commodities products. The restrictions on services activity led to a partial shift in spending towards goods, while demand for commodities products was supported by the global recovery. In particular, E&E products were also supported by continued demand for work-from-home equipment. The global technology upcycle supported strong growth in manufacturing activity globally (Chart 1.5), particularly for the regional economies.

Goods trade and production in various countries along the global value chain, however, were affected by containment measures following resurgences of COVID-19 cases. This led to intermittent disruptions in factories and logistical facilities such as shipping ports. The supply chain disruptions constrained the growth in manufacturing activity due to shortages and delays in obtaining inputs for production, as well as equipment to expand production capacity. Global shortages in semiconductor chips were particularly acute, given the strong demand for digital equipment during the pandemic and long lead times for capacity expansion. Overall, while global trade and *manufacturing* sector performance remained strong throughout the year, the supply chain disruptions had a severe impact on the automotive industry globally, due to its exposure to semiconductor chips in its production.

As economic activity resumed following the lifting of containment measures and demand started to recover, inflationary pressures began to rise in the

Chart 1.5: Global Merchandise Trade Volume and Industrial Production Growth



Source: CPB Netherlands Bureau for Economic Policy Analysis

second half of 2021. Commodity prices, including global food and oil prices, rose sharply, driven by the recovery in economic activity. For oil prices in particular, there were also supply constraints due in part from past under-investment in capacity expansion. Moreover, adverse weather conditions affected the production of crude oil, increased demand for natural gas and contributed to further increases in the prices of certain food commodities. There were also labour shortages in a few advanced economies, notably the US, which led to increased wage pressures. In addition, supply chain disruptions led to an increase in global shipping and input costs, ultimately affecting the prices of consumer goods.

The environment of stronger demand as economies reopened and rising cost pressures from commodity prices and supply chain disruptions led to increases in inflation. Hence, many central banks began to withdraw monetary support in the second half of 2021 to contain price pressures, while remaining cognisant of the need to support the economic recovery. The US Federal Reserve (the Fed) completed tapering off its asset purchases in mid-March of 2022, while the European Central Bank has announced a tapering of its Pandemic Emergency Purchase Programme. Several central banks in EMEs such as Brazil, Mexico and Russia had also raised their policy rates, in light of higher and rising inflation, far above their targets. Nevertheless, the magnitude of increase in inflation varied across countries, with inflation in most Asian economies remaining relatively lower. Thus, Asian EMEs such as Indonesia, Thailand and the Philippines did not increase their policy rates throughout 2021.

Tighter domestic financial conditions, but spillovers to financial intermediation were contained

Developments surrounding the pandemic was a key factor affecting both global and domestic financial markets in 2021. Financial markets began the year with a continuation of the upward momentum from 2020 amid more favourable prospects⁴ in relation to the pandemic. In the US, long-term US Treasury yields surged sharply in the first quarter following

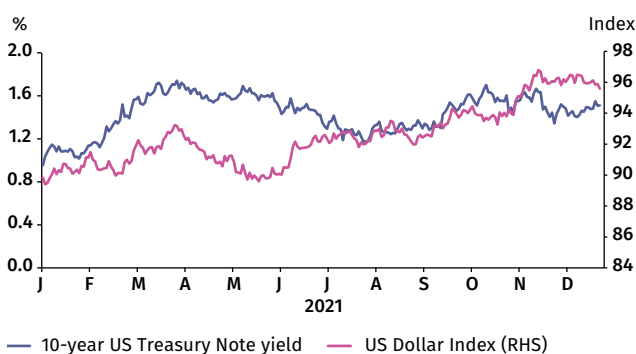
⁴ In the fourth quarter of 2020, investor sentiments were lifted. This was amid better outlook over the health crises and economic recovery following news of successful vaccine trials and subsequent vaccine rollouts in selected major economies.

increased market expectations of a faster economic recovery and higher inflation (Chart 1.6). This led to the corresponding steepening of yield curves in the other AEs and EMEs. The US dollar also strengthened (Chart 1.6), resulting in currency depreciation for most EMEs against the US dollar. Nevertheless, bond yields in the US and subsequently across other countries moderated in April amid the Fed's reiteration to maintain its monetary policy stance to support economic recovery. The decline in yields contributed to easing in financial conditions, which mitigated adverse implications of a premature tightening to the economic recovery, especially for economies that continued to face challenges in managing the impact from the pandemic.

The global outbreak of the Delta variant started affecting sentiments towards the end of the second quarter. The resulting increase in risk aversion induced portfolio rebalancing towards safe-haven assets, such as the US Treasury securities and the US dollar. Equity markets globally also recorded some declines amid uncertainties in the economic outlook. In the EMEs, the ensuing bouts of outflows, which weighed on the broader inflows trend for the year, resulted in increased market volatility. As the extent of the pandemic disruption was uneven, the impact on individual financial markets differed across EMEs. Sentiments were more affected in economies that experienced higher COVID-19 resurgences and stricter implementation of containment measures.

Developments in the financial markets were also influenced by the increased investors' expectations over faster US monetary policy normalisation, which led to further episodes of increases in US bond yields and a stronger US dollar. This was particularly

Chart 1.6: 10-year US Treasury Note Yield and US Dollar Index



Source: Bloomberg

prominent towards the end of the year, following the increased indication by the Fed for a quicker pace of monetary policy normalisation.⁵ During such episodes, global financial markets experienced bouts of tightening, although the adjustments mostly remained orderly amid the Fed's more active communication. During the year-end period, other global factors such as rising inflationary concerns and emergence of the new Omicron variant led to further market adjustments, reflecting the fluctuating risk sentiments.

For Malaysia, while the domestic financial markets were largely affected by the global developments, market conditions were also influenced by domestic factors, primarily in relation to the pandemic and its implications for the economic outlook. The confluence of these external and domestic factors contributed to intermittent volatility in portfolio flows, elevated pressure on the Malaysian Government Securities (MGS) yields, subdued equity prices, and ringgit depreciation.

Movements of domestic equities were particularly sensitive to developments related to the containment measures, given their impact on the outlook for corporate earnings. The equity market was subdued throughout periods of resurgences in cases published during the year (Chart 1.7). Nevertheless, significant progress in vaccinations allowed for

Chart 1.7: 10-year MGS Yield and FBM KLCI



Source: Bank Negara Malaysia and Bloomberg

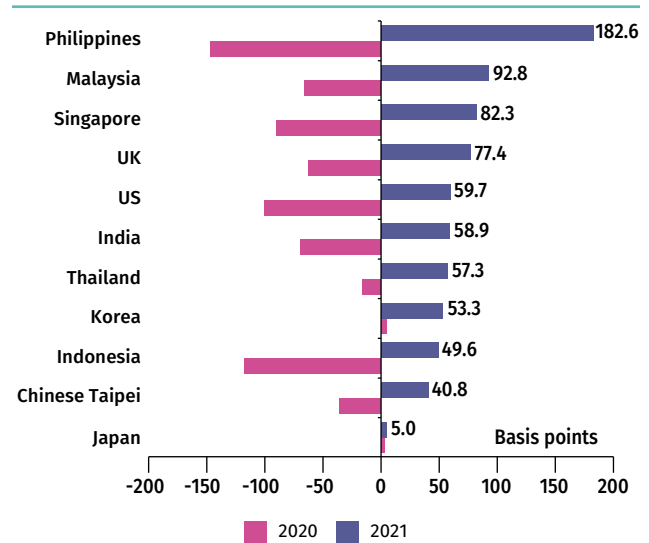
⁵ Signs of increasing willingness by the Fed to start, and quicken, the tapering of its asset purchase programme were evident in the Federal Open Market Committee (FOMC) decisions and meeting minutes, and through communications by individual Fed officials, mainly in the second half of the year. The projection from the 'dot plot' published in December 2021 also indicated an upward revision to at least three rate hikes in 2022, compared to only one rate hike in the September 2021 'dot plot'.

easing of containment measures in August. The subsequent improvement in sentiments provided some support in the equity market, offsetting part of the earlier declines. Despite the rebound in the latter half of 2021, for the year as a whole, the FTSE Bursa Malaysia Kuala Lumpur Composite Index (FBM KLCI) declined by 3.7% (2020: +2.4%) to close at 1,567.5 points. Correspondingly, the equity market recorded non-resident outflows of RM1.1 billion in 2021 (2020: -RM23.9 billion), primarily reflecting the risk aversion due to domestic pandemic resurgences.

Notwithstanding the development in the equity market, the domestic bond market recorded sizable non-resident inflows of RM56.2 billion in 2021 (2020: RM35.0 billion) amid the continued ample liquidity globally. The inflows were also supported by improvement in investors' risk appetite following the reopening of domestic economy and other favourable developments such as Malaysia's retention in the FTSE World Government Bond Index (WGBI), increase of Malaysia's weightage in other major bond indices and the affirmation of Malaysia's sovereign rating⁶ by credit rating agencies. In line with the higher regional bond yields, domestic bond yields increased despite the inflows, mainly reflecting the spillovers from increases in US bond yields (Chart 1.7 and 1.8). This was, to some extent, exacerbated by expectations of higher MGS issuances in relation to the additional pandemic-related fiscal support. As a result, the 3-year, 5-year and 10-year MGS yields increased by 92, 103 and 93 basis points, respectively (2020: -113, -106, and -66 basis points, respectively).

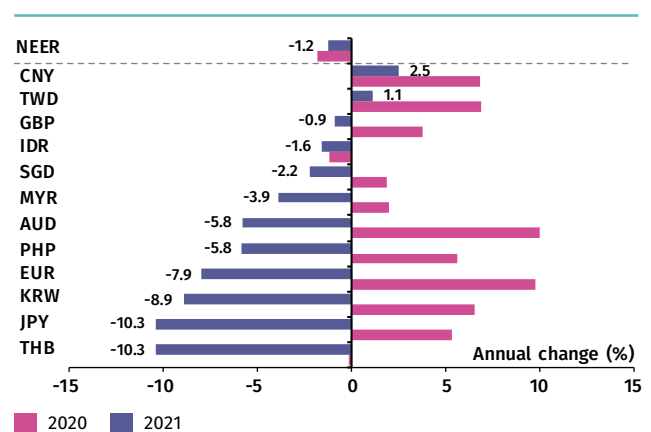
Movements in the ringgit exchange rate largely reflected the strengthening of the US dollar, with the ringgit depreciating by 3.9% to end the year at RM4.1760 against the US dollar (Chart 1.9). This was in line with the movements in most regional currencies, which depreciated between 10.3% and 0.9% against the US dollar. Overall, the Nominal Effective Exchange Rate (NEER) depreciated by 1.2%, reflecting the depreciation of the ringgit against the currencies of Malaysia's key trading partners, including the Chinese renminbi and the Singapore dollar.

Chart 1.8: Change in 10-Year Government Bond Yields of Selected Economies



Source: Bank Negara Malaysia and Bloomberg

Chart 1.9 : Performance of Major and Regional Currencies against the US Dollar and Ringgit Nominal Effective Exchange Rate (NEER)



Note: (+) indicates an appreciation of currencies against the US dollar. NEER shows the value of the ringgit against a trade-weighted basket of Malaysia's major trading partners' currencies.

Source: Bank Negara Malaysia and Reuters

Despite tighter financial conditions and periodic market volatility, adjustments in the domestic financial markets have remained orderly, underpinned by Malaysia's deep and liquid financial markets. The Bank's liquidity and foreign exchange operations provided further support in mitigating excessive market volatility and preserving orderly market conditions. Importantly, spillovers to financial intermediation were contained despite the adjustments in financial conditions. Financing

⁶ Affirmation of Malaysia's sovereign rating of "A3" by Moody's Investors Service and "A-" by S&P Global Ratings in January and June 2021, respectively.

remained supportive of economic recovery, with sustained fundraising activity in the capital market and continued flow of bank credit. The strength and resilience of domestic banking system, in particular, was integral in anchoring an effective intermediation of funds within the economy. Banks' cost of funds were largely unaffected by the higher bond yields given their low reliance on market-based funding instruments.⁷ Active risk management⁸ by banks further mitigated revaluation losses from their bond holdings. This was crucial as financing of the economy remained dominantly bank-based even as market-based financing had been increasing over the years.⁹ More broadly, the impact of external shocks on the domestic economy was also cushioned by the continued flexibility in the ringgit exchange rate, which facilitated the appropriate adjustments in the external sector.

The Malaysian economy grew by 3.1% in 2021, as the recovery was affected by the reimposition of containment measures

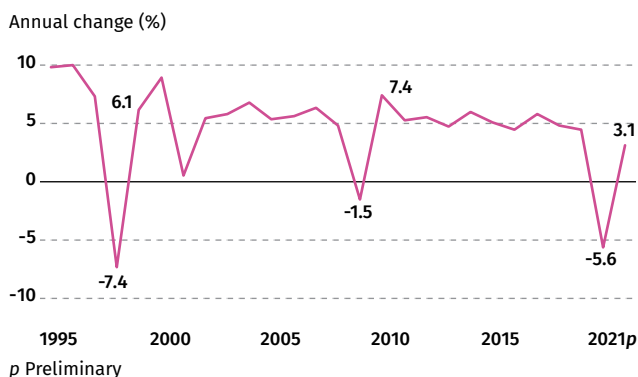
After experiencing significant supply and demand shocks triggered by the COVID-19 pandemic in 2020, economic activity improved moderately in 2021 (Chart 1.10). An incipient recovery which began in the second half of 2020 resumed in the first five months of 2021 (Chart 1.11), despite the imposition of the Second Movement Control Order (MCO 2.0) and the Second Conditional Movement Control Order (CMCO 2.0), as most businesses were allowed to operate during these phases. Thus, together with continued policy support, domestic demand gradually improved. The recovery was further supported by robust exports performance amid favourable external demand. The labour market also rebounded, as the unemployment rate fell from 4.9% in January to 4.5% in May and underemployment declined, amid a decline in jobless claims and an increase in the pace of hiring.

⁷ Funding via equity and interbank financing, and bond issuances accounted for 17.4% and 2.4% of total banking system funding, respectively, as at December 2021.

⁸ For example, banks' hedging strategies and their own internal limits on extent of exposure to bond holdings on their balance sheet.

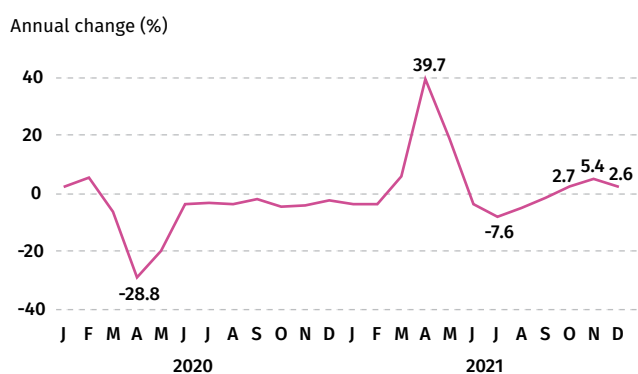
⁹ Private sector financing by the banking system and in the corporate bond market accounted for 72% and 28% of total net financing, respectively, as at end-2021 (2010: 77% and 23%, respectively).

Chart 1.10: Malaysia's Real GDP Growth (1995-2021)



Source: Department of Statistics, Malaysia

Chart 1.11: Real GDP growth (Jan 2020 - Dec 2021)



Source: Department of Statistics, Malaysia

The recovery momentum, however, was affected by the reimposition of nationwide containment measures under the first phase of the National Recovery Plan (NRP)¹⁰ in June 2021, following a rapid resurgence of cases due to the Delta variant. These measures weighed on household spending and investment activity in the third quarter, particularly affecting the *services* and *construction* sectors. Nevertheless, the severity of containment measures in 2021 was smaller compared to the first MCO in the second quarter of 2020, as essential

¹⁰ NRP replaced the Full Movement Control Order (FMCO) that was originally announced on 28 May 2021. The four phases of the NRP allows for a safe reopening of the economy based on three indicators, namely daily symptomatic hospital admission cases, healthcare capacity and vaccination rate. The first phase is the most stringent with strict restrictions on sectors allowed to operate and community mobility. Under this phase, only essential services and industries integral to the supply chain were allowed to operate, while only two individuals per household could travel no further than 10km from their residence, and interstate travel was not allowed. This was followed by gradual relaxations in restrictions across the second, third and fourth phases.

economic sectors were allowed to operate. Additionally, businesses and households adapted better to the containment measures and standard operating procedures (SOPs) during the NRP Phase 1 period. Greater adoption of technology and digitalisation, more effective remote working arrangements, and increased automation helped mitigate further losses arising from the lockdowns. Meanwhile, the rapid progress of domestic vaccinations¹¹ and phased lifting of restrictions under the NRP supported a safe economic reopening and gradual normalisation in economic activity towards the end of the year.

External demand provided robust support to growth in 2021. Strong global trade activity boosted Malaysia's gross exports (2021: 26.0%, 2020: -1.1%). Recovery in economic conditions in advanced and regional economies resulted in strong demand from key trade partners. Similarly, the continued global technology upcycle and robust demand for semiconductors led to strong growth in electrical and electronic (E&E) products. As a key player in the global supply chain, Malaysia was also affected by the supply disruptions, although to a much lesser extent, as trade and manufacturing performance remained resilient during the year.¹² This is mainly attributed to firms having taken proactive measures to mitigate the impact of supply disruptions on their operations.¹³ Meanwhile, exports of services contracted for a second year in a row (-9.4%, 2020: -48.0%), reflecting weak tourist arrivals (2021: 0.1 million persons, 2020: 4.3 million persons¹⁴), as most international borders remained closed.

In terms of developments across economic sectors, the improvement in the domestic economy was

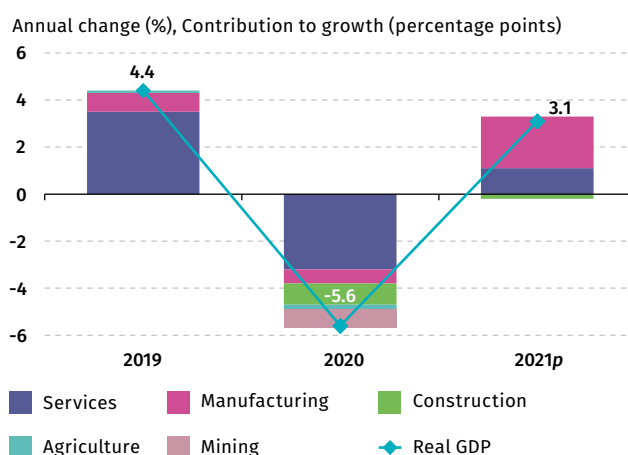
¹¹ As at 31 December 2021, 97.2% of Malaysia's adult population had been fully vaccinated, while 27% of them had received booster shots. Vaccines are also being rolled out to adolescents aged 12 to 17 and children aged 5 to 11.

¹² Although manufacturing production declined in the third quarter, this was attributed to the reimposition of containment measures, rather than disruptions in the global supply chain.

¹³ BNM's industrial engagements revealed that Malaysian firms have taken key mitigation strategies including building inventories by placing advanced bookings and paying expedited fees to secure supplies, expand production capacity by investing in new plants and machinery, as well as opting to use alternative modes of transport which are costlier, such as air cargo or land trucking, to avoid shipment delays. Some firms have taken proactive steps to negotiate with their clients to spread out orders and avoid "bunching" during peak periods, while others have diversified their supplier base. For more detailed analysis on impact of global chip shortages to Malaysia's E&E sector, please refer to the box article titled 'The Global Chip Shortage: Implications and Opportunities for Malaysia' in the BNM Quarterly Bulletin in 2Q 2021.

¹⁴ The bulk of the tourist arrivals in 2020 were in the first quarter, before international borders were closed (1Q 2020: 4.2 million persons).

Chart 1.12: Real GDP by Economic Sectors



P Preliminary

Source: Department of Statistics, Malaysia

fairly uneven, as the pace of recovery differed across sectors. Strong external trade supported the exceptional performance of the *manufacturing* sector (Chart 1.12). Meanwhile, the *services* sector remained constrained by weak demand amid restrictions on mobility and high-touch activities (such as dine-ins and tourism), while activity in the *construction* sector was hampered by labour and operating capacity restrictions. Additionally, adverse weather conditions and continued foreign worker shortages affected output in the *agriculture* sector.

From the demand perspective, economic activity continued to be underpinned by household spending, as labour market conditions improved. Continued investments, particularly in machinery and equipment as firms increased their efforts in automation and digitalisation, as well as expansion in production capacity provided further support to growth (Chart 1.13). In the labour market, employment improved amid a return of workers into the labour force. Underemployment also improved, albeit it remained at a slightly elevated rate compared to long-term averages. Overall conditions, however, remained subdued during the year, as the unemployment rate remained elevated and wage growth was modest amid an uneven recovery across labour market segments.¹⁵ Supportive measures continued to remain in place to enable businesses and households to better withstand the impact of these shocks, support incomes, and mitigate

¹⁵ See white box on "Moderate Recovery in Labour Market Conditions in 2021" for more details.

Table 1.1

Malaysia - Key Economic Indicators

	2019	2020	2021 ^p	2022 ^f
Population (million persons)	32.5	32.6	32.7	32.7
Employment (million persons)	15.1	15.1	15.3	~ 15.6
Unemployment (as % of labour force)	3.3	4.5	4.6	~ 4.0
Per Capita Income (RM)	45,311	42,598	45,874	49,673
(USD)	10,938	10,134	11,066	11,799 ⁴
NATIONAL PRODUCT (% change)				
Real GDP at 2015 prices (RM billion)	4.4 1,424.3	-5.6 1,343.9	3.1 1,386.0	5.3 ~ 6.3 1,466.6
Agriculture, forestry and fishery	2.0	-2.2	-0.2	1.5
Mining and quarrying	-0.6	-10.6	0.7	2.5
Manufacturing	3.8	-2.6	9.5	5.2
Construction	0.4	-19.4	-5.2	6.1
Services	6.2	-5.5	1.9	6.9
Nominal GNI (RM billion)	5.1 1,473.7	-5.8 1,388.0	7.9 1,498.0	8.5 1,626.0
Real GNI (RM billion)	5.0 1,402.5	-5.2 1,330.2	2.4 1,362.3	5.0 1,430.0
Real aggregate domestic demand ¹	4.3	-5.8	1.9	7.2
Private expenditure	6.3	-6.0	2.0	8.2
Consumption	7.7	-4.3	1.9	9.0
Investment	1.6	-11.9	2.6	5.3
Public expenditure	-2.8	-4.7	1.6	3.2
Consumption	1.8	3.9	6.6	1.2
Investment	-10.7	-21.3	-11.4	9.6
Gross national savings (as % of GNI)	25.2	24.5	26.5	23.8
BALANCE OF PAYMENTS (RM billion)				
Goods balance	124.7	138.7	170.2	227.9
Exports	817.3	777.7	977.4	1,086.3
Imports	692.5	639.0	807.2	858.4
Services balance	-10.9	-47.4	-61.1	-62.3
Primary income, net	-39.5	-28.6	-46.2	-69.2
Secondary income, net	-21.4	-2.7	-9.5	-20.7
Current account balance	52.9	60.0	53.5	75.8
(as % of GDP)	3.5	4.2	3.5	4.2 ~ 4.7
Bank Negara Malaysia international reserves, net ² (in months of imports of goods and services) ³	424.0 5.8	432.3 6.7	486.8 6.1	- -
(in months of retained imports)	7.5	8.4	7.7	-
PRICES (% change)				
Consumer Price Index (2010=100)	0.7	-1.2	2.5	2.2 ~ 3.2
Producer Price Index (2010=100)	-1.4	-2.7	9.5	-

¹ Exclude stocks.² All assets and liabilities in foreign currencies have been revalued into ringgit at rates of exchange ruling on the balance sheet date and the gain/loss has been reflected accordingly in the Bank Negara Malaysia's audited accounts.³ For further details, please refer to "Expansion of the Measure on Reserves Coverage of Imports – from Retained Imports to Imports of Goods and Services" article in BNM's Quarterly Bulletin for the Fourth Quarter of 2021.⁴ Based on average USD exchange rate for the period of January-February 2022.^p Preliminary^f Forecast

Note: Figures may not necessarily add up due to rounding.

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

Table 1.2

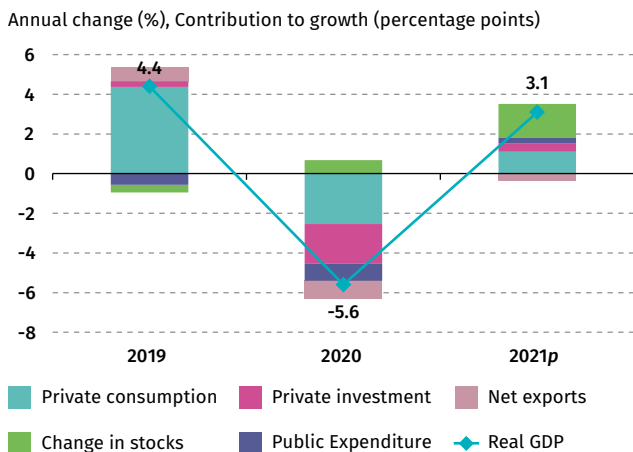
Malaysia - Financial and Monetary Indicators

FEDERAL GOVERNMENT FINANCE (RM billion)		2019		2020		2021	
Revenue		264.4		225.1		233.8	
Operating expenditure		263.3		224.6		231.5	
Net development expenditure		52.6		50.1		63.3	
COVID-19 Fund		-		38.0		37.7	
Overall balance		-51.5		-87.6		-98.7	
Overall balance (% of GDP)		-3.4		-6.2		-6.4	
Public sector net development expenditure		134.5		117.5		141.8	
Public sector overall balance (% of GDP)		-3.4		-7.0		-4.4	
EXTERNAL DEBT							
Total debt (RM billion)		947.4		958.1		1,070.3	
Medium- and long-term debt		557.9		590.7		676.1	
Short-term debt		389.5		367.5		394.2	
Debt service ratio ¹ (% of exports of goods and services)							
Total debt		12.6		13.6		10.8	
Medium- and long-term debt		12.0		13.3		10.6	
		Change in 2019		Change in 2020		Change in 2021	
MONEY AND BANKING		RM billion	%	RM billion	%	RM billion	%
Money supply	M1	24.8	5.8	71.1	15.7	54.6	10.4
	M3	67.0	3.5	79.4	4.0	130.8	6.4
Banking system deposits		55.5	2.9	88.9	4.4	132.4	6.3
Banking system loans ²		65.8	3.9	59.6	3.4	82.6	4.5
Loan to fund ratio (% , end of year) ^{3,4}		83.2		82.5		81.2	
Loan to fund and equity ratio (% , end of year) ^{3,4,5}		72.8		71.9		70.9	
INTEREST RATES (% , AS AT END-YEAR)							
		2019		2020		2021	
Overnight Policy Rate (OPR)		3.00		1.75		1.75	
Interbank rates (1-month)		3.08		1.82		1.83	
Commercial banks							
Fixed deposit	3-month	2.90		1.58		1.57	
	12-month	3.09		1.75		1.71	
Savings deposit		0.97		0.48		0.56	
Weighted average base rate (BR)		3.68		2.43		2.43	
Base lending rate (BLR)		6.71		5.49		5.49	
Malaysian Treasury Bill (3-month) ⁶		2.98		1.72		1.79	
Malaysian Government Securities (1-year) ⁶		2.96		1.73		1.85	
Malaysian Government Securities (5-year) ⁶		3.18		2.12		3.15	
EXCHANGE RATES (AS AT END-YEAR)							
		2019		2020		2021	
Movement of Ringgit (%)							
Change against SDR		1.9		-1.8		-1.4	
Change against USD		1.1		2.0		-3.9	

¹ Excludes prepayment.² Includes loans sold to Cagamas.³ Loans exclude loans sold to Cagamas and loans extended to banking institutions. Beginning July 2015, loans exclude financing funded by Islamic Investment accounts.⁴ Funds comprise deposits (excluding deposits accepted from banking institutions and Bank Negara Malaysia) and all debt instruments (including subordinated debt, debt certificates/sukuk issued, commercial paper and structured notes).⁵ Equities comprise ordinary and preferred shares, share premium and retained earnings.⁶ Refers to data from Fully Automated System for Issuing/Tendering (FAST), Bank Negara Malaysia.

Source: Ministry of Finance, Malaysia and Bank Negara Malaysia

Chart 1.13: Real GDP by Expenditure



p Preliminary

Source: Department of Statistics, Malaysia

displacements in the labour market. These comprise in large part a continuation of measures put in place in 2020, including *Bantuan Prihatin Rakyat*, the Targeted Repayment Assistance (TRA) and the Wage Subsidy Programme.

The current account in the balance of payments remained in surplus during the year. While exports recorded a robust performance, the improvement in external and domestic demand also resulted in a strong rebound in imports in 2021 (23.3%;

2020: -5.8%). In tandem with higher manufacturing production and exports, intermediate imports registered a double-digit growth. Capital and consumption imports also recovered during the year, due to the pickup in investment and consumer spending. Overall, the goods account registered a higher surplus as exports growth outpaced imports growth. A larger decline in travel receipts, however, resulted in a higher services deficit,¹⁶ while the primary income deficit widened due to higher income accrued to foreign investors in Malaysia amid strong external demand for manufactured goods. These factors more than offset the larger goods surplus, contributing to a lower current account surplus of RM53.5 billion or 3.5% of GDP in 2021 (2020: RM60.0 billion or 4.2% of GDP).

Following the trough in the third quarter of 2021, economic activity resumed towards the end of the year in line with the lifting of restrictions. As containment measures were gradually eased during the third quarter, most economic activities restarted, and labour market conditions improved further. This enabled a quick recovery in mobility and consumer spending in the fourth quarter. The lifting of interstate travel bans in October, in conjunction with the year-end holiday season, also provided support for domestic tourism activities. Towards the end of the year, Malaysia also detected growing cases involving the new and highly transmissible Omicron variant.

¹⁶ Malaysia is a net services importer, recording deficits in the services account since 1947, except for 2007 until 2011. Other than travel and manufacturing services, Malaysia customarily records deficits in all other services accounts (e.g., transport, business services, and telecommunications, computer and information services) during the pre-pandemic years.

Domestic demand anchored growth in 2021

In 2021, the Malaysian economy rebounded by 3.1% (2020: -5.6%), mainly supported by a turnaround in private sector spending. The recovery momentum, however, was affected by the imposition of containment measures during the year. These include the Second Movement Control Order (MCO 2.0) in January 2021 and the National Recovery Plan (NRP) in June 2021. Nevertheless, less restrictive restrictions compared to 2020 as well as better adjustments to the new norm, improved compliance to the standard operating procedures (SOPs) and rapid vaccination progress had minimised the adverse impact on households and businesses. The gradual improvement in income and labour market conditions during the year had provided support to household spending. Meanwhile, investment activity benefitted from continued capital spending, particularly by private firms in the export-oriented sectors. Importantly, policy support remained available for impacted households and businesses. On the external front, the robust exports performance was driven by the rebound in world growth and trade activity, lifted further by the global technology upcycle. However, net exports contracted, as import growth outpaced the growth in exports.¹⁷

Table 1

Real GDP by Expenditure (2015=100)

	2021p	2020	2021p	2020	2021p
	% of GDP	Annual change (%)		Contribution to growth (percentage point)	
Domestic Demand¹	92.7	-5.8	1.9	-5.4	1.8
Private sector expenditure	74.3	-6.0	2.0	-4.5	1.5
Consumption	58.8	-4.3	1.9	-2.5	1.1
Investment	15.6	-11.9	2.6	-2.0	0.4
Public sector expenditure	18.3	-4.7	1.6	-0.9	0.3
Consumption	13.8	3.9	6.6	0.5	0.9
Investment	4.5	-21.3	-11.4	-1.3	-0.6
Gross Fixed Capital Formation	20.1	-14.5	-0.9	-3.3	-0.2
Change in stocks	1.3			0.7	1.7
Net Exports of Goods and Services	6.0	-13.0	-5.8	-0.9	-0.4
Exports	69.2	-8.9	15.9	-5.7	9.8
Imports	63.2	-8.4	18.5	-4.8	10.2
Real Gross Domestic Product (GDP)	100.0	-5.6	3.1	-5.6	3.1

¹ Excluding stocks
p Preliminary

Note: Figures may not necessarily add up due to rounding.

Source: Department of Statistics, Malaysia

Private consumption registered a modest recovery of 1.9% in 2021 (2020: -4.3%). This was primarily supported by the improvement in wages and employment, as well as less restrictive containment measures compared to 2020. Household spending on both necessities and discretionary items improved in 2021. The recovery in household spending was temporarily halted by the containment measures under the NRP in June 2021. However, as restrictions were gradually relaxed beginning mid-August, private consumption turned around to register positive growth in the fourth quarter. Notably, discretionary spending on high-touch segments such as restaurants, hotels and recreational services increased due to the materialisation of some pent-up demand. Throughout the year, various policy measures remained in place to assist affected households, particularly those in the lower-income group. These measures include Bantuan Prihatin Rakyat (BPR) and targeted loan repayment assistance.

¹⁷ Despite larger trade surplus and nominal net exports, real net exports contracted due to higher export deflator as compared to import deflator.

Gross fixed capital formation (GFCF) registered a smaller contraction of 0.9% in 2021 (2020: -14.5%). This was mainly driven by higher capital spending by the private sector and a smaller decline in public investment. By type of asset, machinery and equipment (M&E) investments rebounded strongly (2021: 13.0%, 2020: -8.6%) underpinned by capacity expansion in the export-oriented sectors. Meanwhile, investments in structures continued to contract, albeit by a smaller pace (2021: -10.0%, 2020: -18.3%) as the implementation of containment measures had affected the commencement and progress of construction projects.

Private investment grew by 2.6% (2020: -11.9%), lifted by higher capital spending particularly in M&E. The high M&E investment reflected capacity expansion by export-oriented manufacturers to fulfil the strong global demand. During the year, approved investment remained encouraging, mainly in the electrical and electronics (E&E) and metal sub-sectors. Notwithstanding this, the reimposition of containment measures had led to continued weakness in structures-related investments, especially the construction of residential and non-residential buildings.

Public investment registered a smaller decline of 11.4% (2020: -21.3%). This was supported by increased spending on fixed assets by the Federal Government. The continued progress of large infrastructure projects provided some support to growth, as these projects were allowed to operate during the lockdown period. Capital spending by public corporations, however, remained weak across most sectors, weighed by the restrictions due to the containment measures.

Public consumption rose by 6.6% (2020: 3.9%), mainly on account of higher spending on both supplies and services and emoluments. This reflected higher Federal Government expenditure related to COVID-19, including on vaccine procurement and logistics services, purchases of medical equipment and services, and special allowances for frontliners.

Growth supported by *manufacturing* and *services* sectors

The recovery in 2021 was mainly driven by expansion in the *manufacturing* and *services* sectors. The *mining* sector recorded marginal growth while the *agriculture* and *construction* sectors contracted. The uneven pace of recovery across sectors reflected several factors. First, the reimposition of various containment measures had affected high-contact segments such as tourism-related industries and *construction* sectors more than others. Nonetheless, rapid vaccination progress, greater firm adaptability and more widespread adoption of digitalisation and automation had enabled firms and households to partly mitigate the negative impact. Second, export-oriented sectors benefitted from strong external demand arising from the continued global technology upcycle and demand for healthcare-related products. Third, labour shortages and adverse weather conditions hampered activity in the *agriculture* sector.

Table 1

Real GDP by Kind of Economic Activity (2015 = 100)

	2021p	2020	2021p	2020	2021p
	% of GDP	Annual change (%)		Contribution to growth (ppt) ¹	
Services	57.0	-5.5	1.9	-3.2	1.1
Manufacturing	24.3	-2.6	9.5	-0.6	2.2
Mining and quarrying	6.7	-10.6	0.7	-0.8	0.0
Agriculture	7.2	-2.2	-0.2	-0.2	0.0
Construction	3.7	-19.4	-5.2	-0.9	-0.2
Real Gross Domestic Product (GDP)	100¹	-5.6	3.1	-5.6	3.1

¹ Figures may not necessarily add up due to rounding and exclusion of import duties component
p Preliminary

Source: Department of Statistics, Malaysia

The *services* sector recovered gradually in 2021, expanding by 1.9% (2020: -5.5%). Activity, particularly within the high-touch sub-sectors (e.g. retail, dining out and recreational activities), continued to be affected by the containment measures implemented during the year. The impact, however, was partially mitigated by higher firm and consumer adaptability to the new operating environment. For example, previous experience with operating procedures such as rearrangement of dining areas and limits to the number of customers at any one time helped reduce frictions for reopening businesses. These were further supported by the increased use of delivery services and greater adoption of e-commerce. Consequently, online retail trade activity grew on average by 18.4% in 2021. Meanwhile, the transport and storage subsector continued to be weighed by international travel restrictions. Nevertheless, as operating restrictions eased towards the end of the year, including on interstate travel, services activity gradually picked up. The finance and insurance sub-sector expanded throughout the year driven by sustained net interest income and strong growth in premiums less claims respectively. The information and communication subsector also continued to grow, supported by stronger demand for broadband data amid greater digitalisation in the economy.

The *manufacturing* sector expanded by 9.5% (2020: -2.6%) as the recovery in global and domestic demand supported production activity. The overall effect of global supply chain disruptions on production activity was partly mitigated as manufacturers were able to implement measures to cushion the impact. This included building inventory buffers, negotiating with clients to spread orders, paying for expedite fees and using alternative modes of transportation to avoid shipment delays. For the year as a whole, growth was mainly driven by the expansion in E&E, primary, and consumer-related clusters. Aided by structural shifts towards digitalisation, the E&E sector recorded a robust growth of 14.6% (average: 2010-2019: 6.4%) driven by strong demand for products associated with remote working, e-commerce, cloud-based services, and medical devices. In addition, E&E firms' ability to adapt to SOPs and the highly automated nature of many large semiconductor firms lessened the impact of operating restrictions imposed during the NRP, enabling firms to continuously meet demand. Meanwhile, production in the primary sector benefited from pandemic-induced demand (e.g. rubber gloves and pharmaceuticals) while the consumer-related cluster (e.g. food and beverages and passenger cars) was supported by improvement in domestic household spending and continued fiscal support (e.g. PEMERKASA+ extended SST exemption on passenger cars).

The *agriculture* sector contracted by 0.2% (2020: -2.2%) due to weaker oil palm output. This was amid acute impact from labour shortages and floods in the earlier part of the year which continued to affect harvesting activities. Furthermore, weaker production in the rubber and fisheries subsectors also contributed to the decline in growth. Nonetheless, the decline was partially offset by the expansion in livestock and other agriculture sub-sectors amid a turnaround in domestic demand.

The *mining* sector registered its first positive growth since 2017 (0.7%; 2020: -10.6%). The turnaround was mainly attributed to the gradual recovery in global oil demand and new output from the PETRONAS Floating Liquefied Natural Gas DUA (PFLNG2) facility located in offshore East Malaysia, which commenced operations in February 2021. These factors had more than offset the impact of facility closures such as the Gumusut-Kakap field for maintenance purposes, and production disruptions in the other mining sub-sector due to restrictions from containment measures.

The *construction* sector declined by 5.2% (2020: -19.4%), as the industry faced limitations on operating capacity and the stop-start nature of construction works, due to the movement restrictions. Special trade was the sole subsector with positive growth, supported by end-works¹⁸ from selected commercial and civil engineering projects, as well as implementation of small-scale projects. Meanwhile, construction activities in the residential and non-residential subsectors remained subdued following extended periods of lockdown and reduced operating capacity. Nevertheless, the easing of the containment measures since August and the reopening of the economy supported the gradual improvement across all subsectors towards the end of the year.

¹⁸ Include works such as electrical, plumbing, heat, air conditioning and other construction installation, as well as building completion and finishing.

Moderate Recovery in Labour Market Conditions in 2021

After experiencing significant disruptions in 2020, conditions in the Malaysian labour market improved moderately in 2021. The labour market was in recovery in the first five months of the year, in line with the pick-up in economic activity. The recovery momentum, however, slowed in conjunction with Phase 1 of the NRP in June.

Following the reimposition of nation-wide containment measures, unemployment increased, from 4.5% in May, to 4.8% in July 2021, alongside a decline in employment levels. Restrictions on movement and economic activity led to some exits from the labour force, as the population outside the labour force increased during this period. Similar to MCO 1.0, most of the increase was due to reasons such as housework and family care, as well as going for further studies. Underemployment also increased, but rebounded rapidly with the relaxation of restrictions starting in August 2021. Overall, the impact of containment measures to labour market conditions in 2021 was much smaller compared to MCO 1.0 in 2Q 2020.

The difference in impact was likely due to a few factors. First, labour capacity restrictions were less restrictive during Phase 1 of the NRP.¹⁹ Second, having experienced lockdowns before, firms and workers had greater adaptability to labour capacity restrictions, health-related standard operating procedures (SOPs), and remote work. Third, the efficient rollout of the national vaccination drive saw 90% of the adult population being fully inoculated by October 2021, allowing for a rapid and safer reopening of the economy. Throughout the pandemic, the labour market also benefitted from the continuous support from key Government measures, such as the continuation and expansion of the Wage Subsidy Programme, and hiring incentives under *PenjanaKerjaya*.

The labour market resumed its recovery towards the end of the year, following the lifting of restrictions. For 2021 as a whole, the labour force participation rate improved slightly to 68.6% (2020: 68.4%), while the labour force and employment grew at a faster pace of 1.4% (2020: 1.1%) and 1.3% (2020: -0.2%) respectively. Time-related underemployment²⁰ declined to 315,000 persons, or 2.0% of the labour force (2020: 367,000 persons or 2.3%, 2017-2019 average: 1.4%)²¹. While the unemployment rate remained elevated at 4.6% for the year (2020: 4.5%), this was mainly due to the re-entry of workers into the labour force, as employment conditions improved amid the gradual normalisation of economic activity.

The improvement in employment growth was attributed to the net increase of employment in skilled and mid-skilled occupations, which increased by 1.7% and 1.5% respectively.²² This was partially offset by decline in employment in the low-skilled occupation at 0.9%, as this segment remained affected by the reimposition of containment measures, as well as the shortages of foreign workers in selected sectors in the economy. From a sectoral perspective, the improvement in employment growth was driven mainly by the *services* sector, supported by growth in the wholesale and retail trade, food and beverages as well as other services subsectors. Employment in the *manufacturing* sector also increased, driven mainly by higher employment in the vegetable and animal oils & fats and food processing, the petroleum, chemical, rubber and plastic products, as well as the E&E subsectors. Meanwhile, retrenchments reported to the Ministry of Human Resources declined to 63,321 persons during the year (2020: 104,432 persons).

Aggregate nominal wages in the private sector²³ grew marginally in 2021 (0.4%; 2020: -2.4%), driven mainly by *manufacturing* sector wages. During the year, *manufacturing* sector wages rebounded and grew by 3.0% (2020: -1.1%), driven mainly by the export-oriented sectors. The *services* sector wages, on the other hand, continued to record a contraction, albeit at a smaller rate of 1.0% (2020: -3.1%). The weakness in *services* sector wages was

¹⁹ The private sector was allowed to operate at 60% of headcount, while the agriculture sector was allowed to operate at 'optimal capacity'. Under MCO 1.0, a 50% limit was imposed on all essential sectors that were allowed to operate.

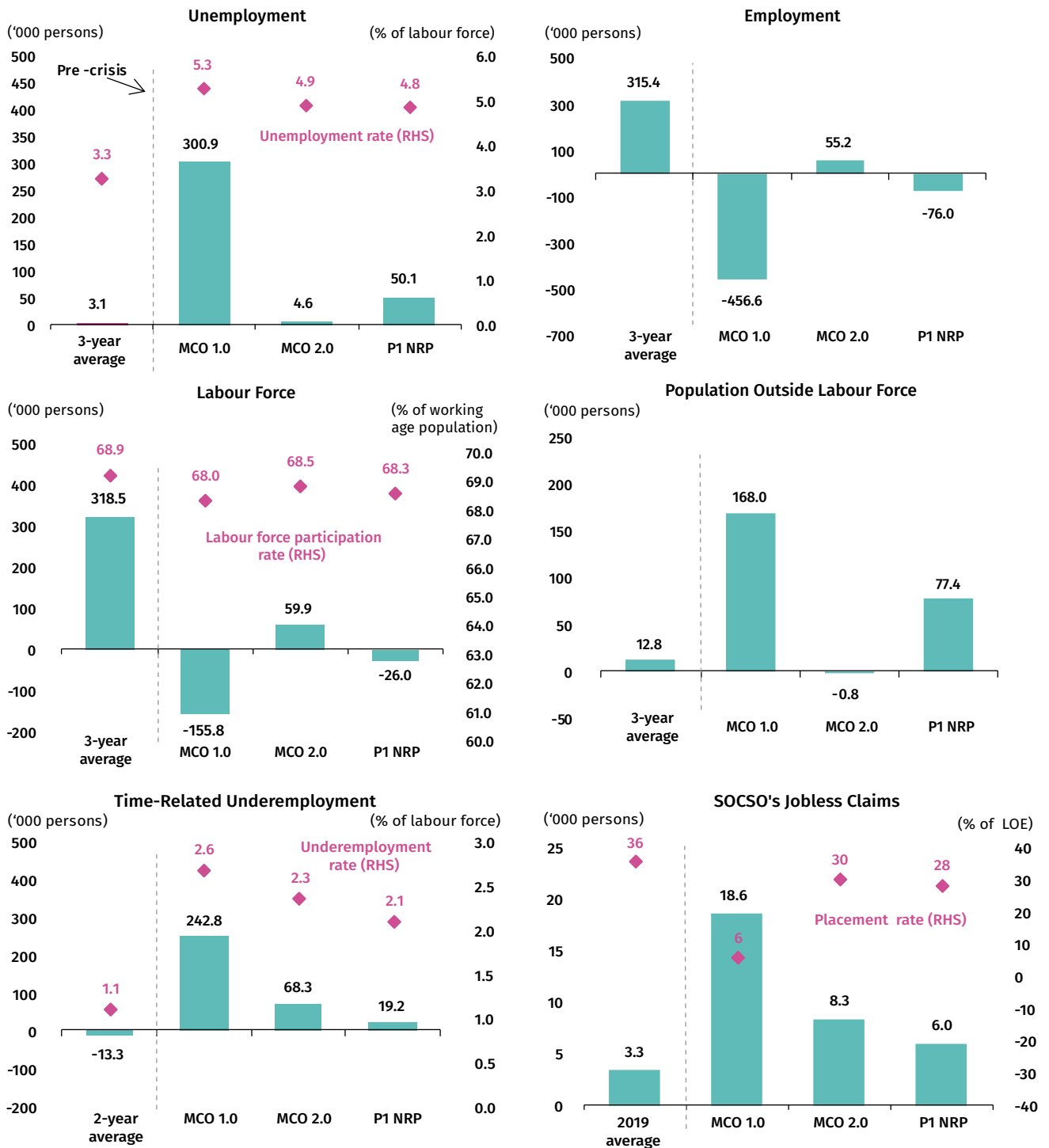
²⁰ Time-related underemployment is defined as those who are employed less than 30 hours per week due to the nature of their work or because of insufficient work. Additionally, they are able and willing to accept additional hours of work.

²¹ Time-related underemployment rates are estimated based on the quarterly averages from the Department of Statistics Malaysia's Labour Force Survey. These figures do not include workers who could not work at all due to labour restrictions in the second quarter.

²² Mid-skilled workers continued to account for the largest share of total employed persons at 59.0% (2020: 58.8%), followed by high-skilled workers at 29.1% (2020: 28.9%).

²³ Private sector wages are derived from the salaries and wages data published in the Monthly Manufacturing Statistics and Quarterly Services Statistics by the Department of Statistics Malaysia. It covers 66% of total employment.

Chart 1: Impact of Movement Controls on Labour Market Conditions



Note:

¹ Impact is measured by changes in respective indicators in the months corresponding closest to various phases of containment measures, with the exception of jobless claims from SOCSO. MCO 1.0 includes CMCO: 18 March 2020 - 10 Jun 2020. MCO 2.0: 13 Jan 2021 - 4 Mar 2021. Phase 1 of the NRP includes MCO3.0: 12 May 2021 - 31 July 2021.

² For underemployment, increases correspond to periods of tightening restrictions. MCO 1.0: 1Q 2020 - 2Q 2020. MCO 2.0: 4Q 2020. P1 NRP includes MCO 3.0 and CMCO 3.0: 2Q 2021. Data on quarterly underemployment only available since 1Q 2017.

³ Markers (diamonds) refer to highest/lowest rates reached during the period. Pre-crisis refers to December 2019 or 4Q 2019 figures.

Source: Department of Statistics, Malaysia (DOSM), Bank Negara Malaysia estimates

Table 1

Selected Labour Market Indicators

	2016	2017	2018	2019	2020	2021p
Employment ('000 persons)	14,180	14,459	14,810	15,126	15,096	15,290
Annual change (%)	0.6	2.0	2.4	2.1	-0.2	1.3
Unemployment rate (% of labour force)	3.4	3.4	3.3	3.3	4.5	4.6*
Labour force participation rate (% of working age population)	67.7	68.0	68.3	68.7	68.4	68.6
Retrenchments (persons)	37,699	35,097	23,168	29,605	104,432	63,321
Non-Malaysian citizens employment ('000 persons)	2,209	2,274	2,239	2,254	2,214	2,149

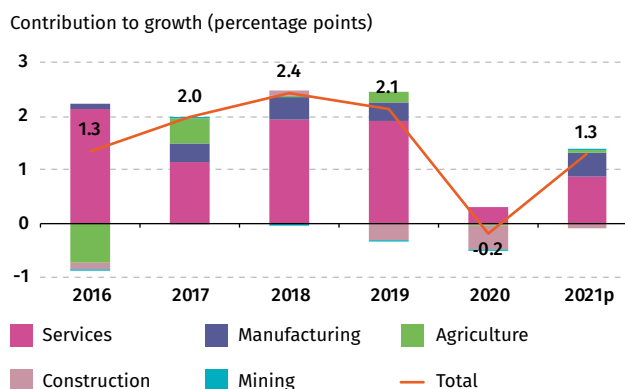
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Note: Annual employment, unemployment, and non-Malaysian citizens employment (a proxy for foreign workers) for 2021 were estimated based on quarterly figures from the Labour Force Survey.

*The slight increase in the unemployment rate in 2021 is mainly due to a faster growth in labour force relative to employment, following the re-entry of workers into the labour force during the year.

Source: Department of Statistics, Malaysia, Ministry of Human Resources and Bank Negara Malaysia estimates

Chart 2: Employment Growth by Sector, 2016 - 2021



p Preliminary

Source: Labour Productivity Statistics published by the Department of Statistics, Malaysia

attributed to the consumer- and tourism-related industries such as food and beverages, accommodation, as well as arts, entertainment and recreation, which continued to face relatively stricter restrictions for the most part of the year. Meanwhile, public sector wages increased by 5.4% (2020: 4.5 %).

Developments surrounding labour productivity were mixed, and partly reflected the impact of containment measures on the labour market in 2020 and 2021. As measured by real value-added per hour, productivity declined by 2.6% in 2021 (2020: 3.4%). This was due mainly to the larger increase in total hours worked compared to output, relative to the significant decline in hours worked in 2020, particularly during MCO1.0. Nevertheless, labour productivity as measured by real value-added per worker increased by 1.8% in 2021 (2020: -5.5%) due to the more significant increase in output relative to employment. The *manufacturing* sector recorded the largest improvement by 6.8%, driven mainly by the E&E as well as petroleum, chemical, rubber and plastic products subsectors. *Services* sector productivity also improved slightly, registering a marginal positive growth of 0.5% in 2021 (2020: -6.0%) amid the gradual normalisation of economic activity.

Strong external sector performance in 2021

Malaysia continued to register a healthy current account surplus despite the challenging global and domestic economic landscape in 2021. The surplus amounted to RM53.5 billion or 3.5% of GDP (2020: RM60.0 billion or 4.2% of GDP), supported mainly by a larger goods surplus.

Table 1

Balance of Payments¹

Item (Net)	2019	2020	2021 ^p
	RM billion		
Current account	52.9	60.0	53.5
Goods ²	124.7	138.7	170.2
Services	-10.9	-47.4	-61.1
Primary income	-39.5	-28.6	-46.2
Secondary income	-21.4	-2.7	-9.5
Capital account	0.4	-0.4	-0.8
Financial account	-38.0	-76.2	29.7
Direct investment	6.6	2.8	32.9
Portfolio investment	-32.4	-48.2	18.9
Financial derivatives	-0.5	0.4	-0.2
Other investment	-11.7	-31.1	-21.9
Net errors and omissions³	-6.8	-2.7	-36.7
Overall balance	8.4	-19.3	45.6

¹ In accordance with the Balance of Payments and International Investment Position Manual, Sixth Edition (BPM6) by the International Monetary Fund (IMF)

² Adjusted for valuation and coverage of goods for processing, storage and distribution

³ As at 1Q 2018, the net E&O excludes reserves revaluation changes. This practice is backdated to 1Q 2010

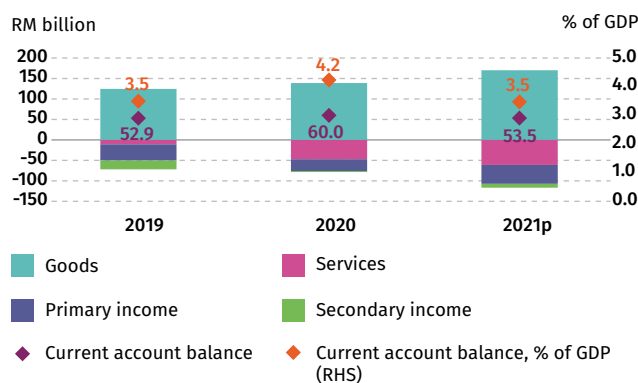
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Source: Department of Statistics, Malaysia and Bank Negara Malaysia

In the goods account, exports increased faster relative to imports resulting in a higher goods surplus of RM170.2 billion (2020: RM138.7 billion). This was mainly on account of strong external demand for both manufactured goods and commodities, amid the recovery in global growth and higher commodity prices. The services account recorded a larger deficit of RM61.1 billion in 2021 (2020: -RM47.4 billion). This mainly reflected a larger travel account deficit of RM14.6 billion (2020: -RM7.7 billion) following prolonged international border restrictions.

In the income account, the primary income deficit widened to RM46.2 billion (2020: -RM28.6 billion), due mainly to higher investment income accrued to foreign investors in Malaysia, amid robust export performance. The secondary income account recorded a larger deficit of RM9.5 billion (2020: -RM2.7 billion), due mainly to the lower transfers received amid continued foreign workers' outward remittances.

Chart 1: Current Account Balance

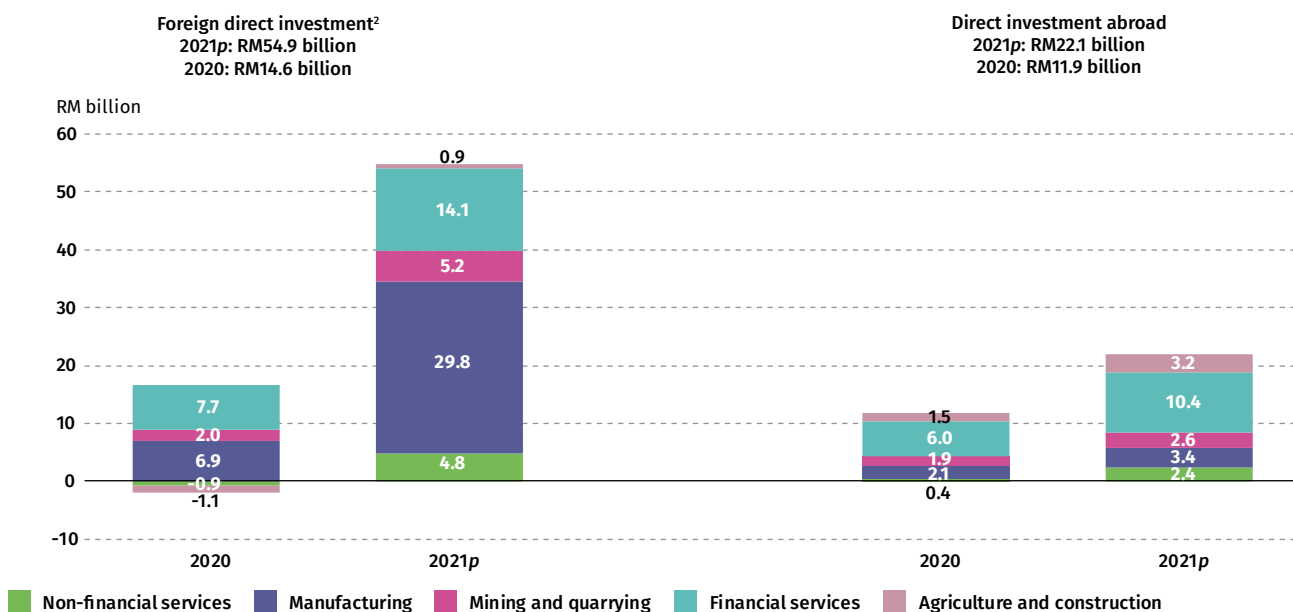


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Source: Department of Statistics, Malaysia and Bank Negara Malaysia

In 2021, the financial account turned around to record a net inflow of RM29.7 billion (2020: -RM76.2 billion). This was due mainly to higher inflows in the direct and portfolio investment accounts.

Chart 2: Net Foreign Direct Investment and Direct Investment Abroad¹ by Sector



¹ Foreign direct investment and direct investment abroad as defined according to the Balance of Payments and International Investment Position Manual, Fifth Edition (BPM5) by the International Monetary Fund (IMF).

² Negative values refer to net outflows.

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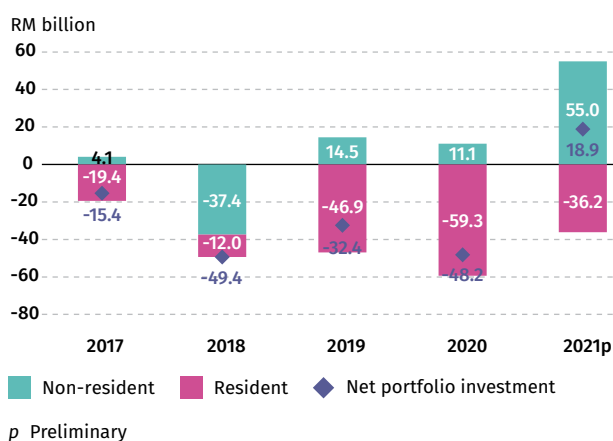
Note: Figures may not necessarily add up due to rounding.

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

The direct investment account registered a larger net inflow of RM32.9 billion (2020: +RM2.8 billion) as net FDI inflows improved to RM54.9 billion in 2021 (+3.7% of GDP; 2020: +RM14.6 billion, +1.0% of GDP). The higher FDI was driven by the recovery in global and domestic economies, which encouraged global MNCs to expand capacity and undertake new investment in the country. Malaysia’s FDI was also supported by the continued global technology upcycle as foreign firms invested to meet rising demand for E&E related products. By economic activity, the increase in net FDI inflows was broad-based, driven mainly by the *manufacturing* sector and financial services sub-sector. Firms from United States (28.9% of net FDI for the year), Singapore (15.1%) and Netherlands (10.2%) were the top contributors to FDI in the year.

DIA outflows were also higher at RM22.1 billion (-1.5% of GDP; 2020: -RM11.9 billion, -0.8% of GDP). These investments abroad were mainly channelled into the financial services sub-sector as well as the *manufacturing* and *mining* sectors. Netherlands (33.3% of net DIA for the year), Canada (21.7%) and Indonesia (15.8%) were the major recipients of DIA in 2021.

Chart 3: Portfolio Investments



Source: Department of Statistics, Malaysia and Bank Negara Malaysia

The portfolio investment account turned around to register a net inflow of RM18.9 billion (2020: -RM48.2 billion), due mainly to sizeable non-residents (NR) portfolio inflows (RM55 billion; 2020: RM11.1 billion). These investments were mainly in domestic debt market, particularly in Government bonds. This was supported by the improvement in investor sentiment and ample liquidity amid continued policy support from central banks globally. Resident portfolio investment abroad recorded a smaller net outflow of RM36.2 billion (2020: -RM59.3 billion). This was primarily driven by domestic institutional investors in equity markets abroad, in line with their continued efforts to diversify risks and enhance portfolio returns.

The other investment account recorded a lower net outflow of RM21.9 billion (2020: -RM31.1 billion) as outflows from net interbank lending abroad by the domestic banking system were partially offset by the additional allocation of Special Drawing Rights (SDR) (RM20.8 billion) by the International Monetary Fund (IMF).²⁴ Net errors and omissions (E&O) amounted to -RM36.7 billion or -1.6%²⁵ of total trade during the year (2020: -RM2.7 billion, or -0.2% of total trade).

²⁴ The overall IMF additional allocation of SDRs amounted to SDR456.5 billion (equivalent to about USD650 billion) and took effect on 23 August 2021. The SDR allocation will provide additional liquidity to the global financial system, bolster reserves, build confidence, and enhance the resilience of the world economy. The allocation is distributed to all member countries in proportion to their respective quota share in the IMF.

²⁵ The E&O level remains below 5% of total trade, which is the threshold of acceptable E&O as per the guidelines on balance of payments compilation issued by the IMF.

Malaysia's international investment position remained favourable

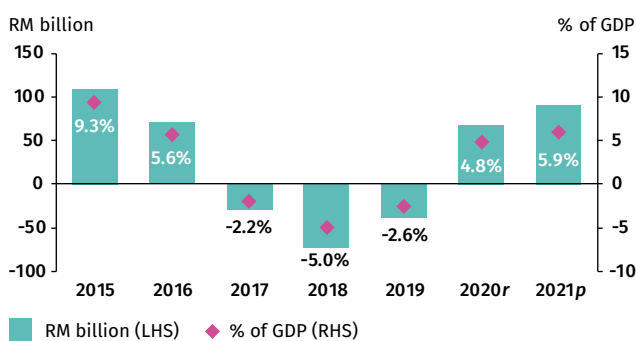
Malaysia's international investment position (IIP) registered a second consecutive year of net external asset position, amounting to RM91.0 billion, or equivalent to 5.9% of GDP as at end-2021 (end-2020: RM67.5 billion or 4.8% of GDP). External assets increased by RM212.1 billion in 2021, largely on account of three main factors. First, there was an increase in reserve assets with close to half attributed to the additional allocation of SDR by the IMF. Second, banks and corporates registered a net portfolio investment abroad during the year. Third, higher external assets also reflected exchange rate valuation effect of the weaker ringgit as well as price valuation gains following better performance in global equity markets during the year. External liabilities increased by RM188.7 billion, partly reflecting net inflows of foreign direct and portfolio investments by non-resident investors, amid Malaysia's improving economic prospects.

The net foreign currency (FCY) external asset position, as measured by external assets denominated in FCY less FCY external liabilities, increased to RM1.1 trillion, or 74.2% of GDP (2020: RM1.0 trillion, or 74.1% of GDP). Given this position, periods of ringgit exchange rate depreciation will result in a larger increase in external assets compared to external liabilities, thus further increasing Malaysia's net creditor position in ringgit terms.

Malaysia's external debt amounted to RM1,070.3 billion as at end-2021, or 69.3% of GDP (2020: RM958.1 billion or 67.6% of GDP). The higher external debt reflected primarily increased non-resident holdings of Government domestic debt securities, net issuance of bonds and notes by corporates, and an additional allocation of SDRs to Malaysia by the IMF.²⁶ These were partially offset by the lower interbank borrowings and external loans.

Risks surrounding Malaysia's external debt remained manageable and were well contained given the favourable maturity and currency profiles, coupled with the Bank's prudential and hedging requirements²⁷ on corporates and banks. As at end-2021, the external debt-at-risk for corporates²⁸ and banks²⁹ amounted to RM29.2 billion and RM55.9 billion, respectively (2020: RM26.4 billion and RM62.1 billion). Cumulatively, these amounted to 7.9% of Malaysia's total external debt and 17.5% of international reserves. This was relatively lower than the position in 2020 (9.2% and 20.5% respectively), due partly to lower banks' external debt-at-risk and higher international reserves.

Chart 1: Net International Investment Position (IIP)

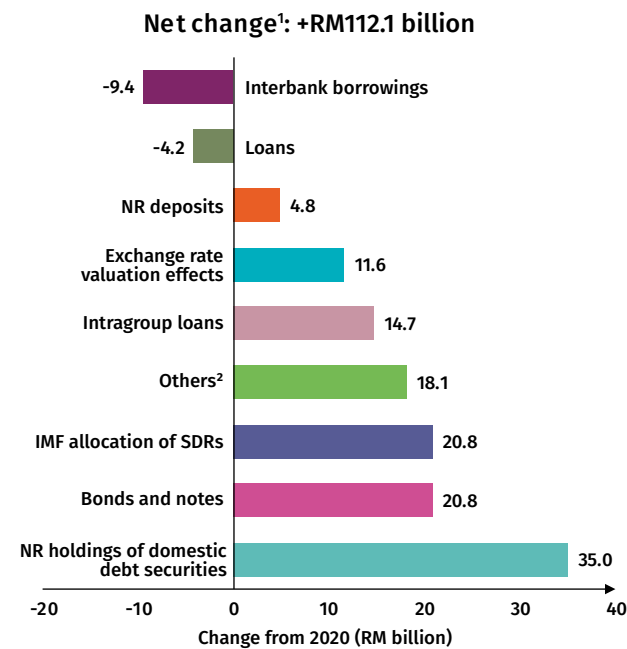


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Source: Department of Statistics, Malaysia

Chart 2: Changes in External Debt



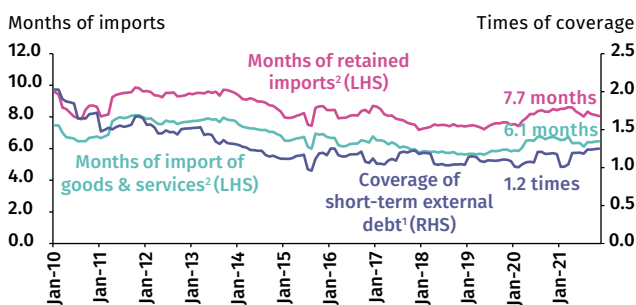
¹ Changes in individual debt instruments exclude exchange rate valuation effects.

² Comprises trade credits and other debt liabilities.

Note: Figures may not add up due to rounding.

Source: Ministry of Finance Malaysia and Bank Negara Malaysia

Chart 3: International Reserve Adequacy Indicators



¹ Adequacy threshold of 1-time.

² Adequacy threshold of 3-months.

Source: Department of Statistics Malaysia and Bank Negara Malaysia

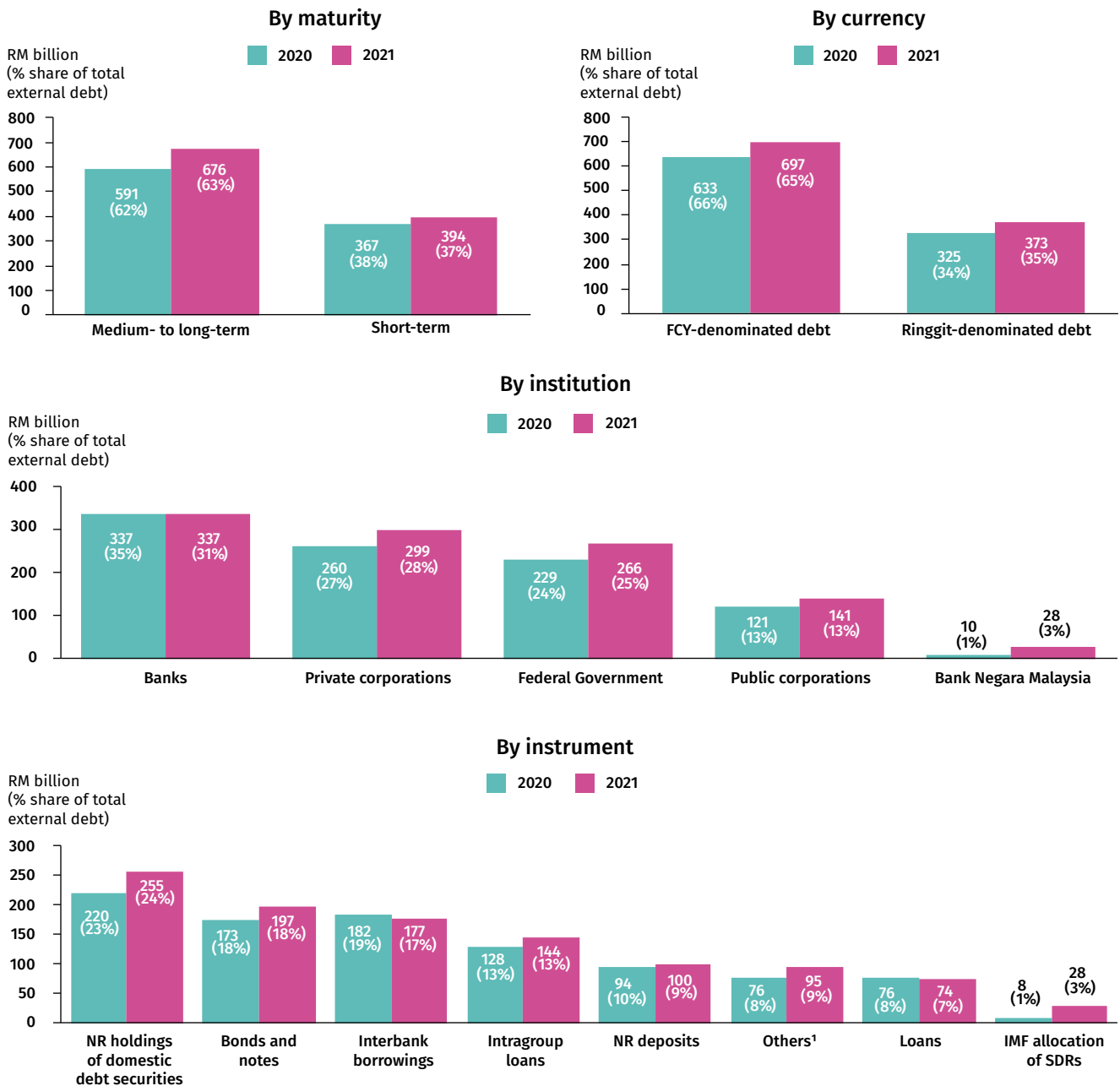
²⁶ The IMF additional allocation of SDRs to Malaysia amounted to SDR3.5 billion (equivalent to about RM20.8 billion) and took effect on 23 August 2021. According to the IMF Balance of Payments and International Investment Position Manual – Sixth Edition (BPM6), new allocations of SDRs are to be recorded as increases in the respective member countries' gross international reserves (holdings of SDRs), with an equal increase in the countries' long-term debt liabilities (allocation of SDRs).

²⁷ For more details on Malaysia's external debt management, please refer to "Malaysia's Resilience in Managing External Debt Obligations and the Adequacy of International Reserves" box article in BNM's Annual Report 2018 on external debt.

²⁸ Based on offshore loans raised and bonds issued by high-risk corporate borrowers.

²⁹ Refers to the portion of banks' external debt that were more susceptible to sudden withdrawal shocks. These include interbank borrowings (RM33.9 billion), financial institutions' deposits (RM17.3 billion) and other short-term debt (RM4.6 billion) from unrelated counterparties.

Chart 4: Profile of Malaysia's External Debt (% share)



¹ Comprises trade credits and other debt liabilities, such as insurance claims yet to be disbursed and interest payables on bonds and notes.

Note: Figures may not necessarily add up due to rounding.

Source: Bank Negara Malaysia

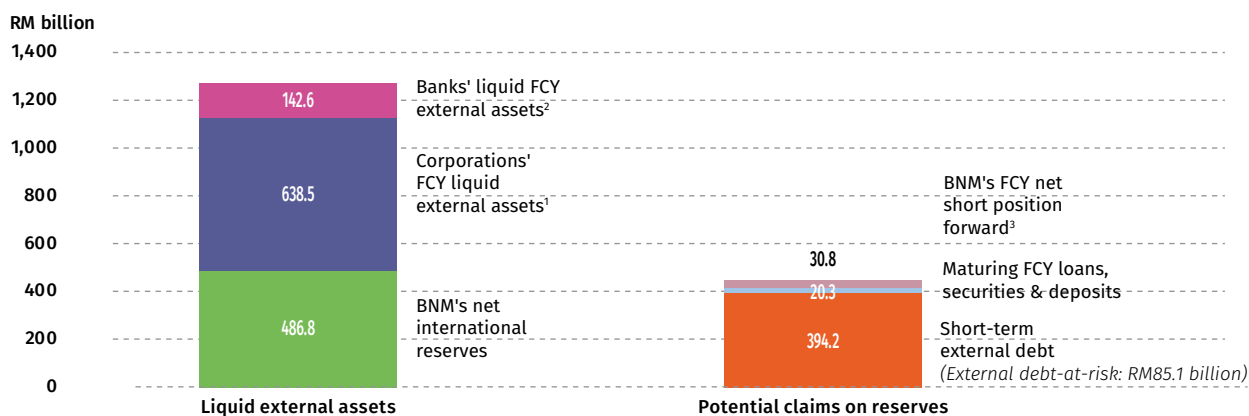
The net issuance of international long-term bonds and notes in 2021 primarily reflected prudent and strategic capital management efforts by corporates to refinance at lower interest rates while extending the debt maturity profile, amid the highly accommodative global and monetary conditions. This partly contributed to the rising share of medium- to long-term external debt during the year (end-2021: 63.2% share of total external debt; 2020: 61.6% share), and thus reducing rollover risks.

More than one-third of external debt was denominated in ringgit (34.8%; 2020: 33.9%), and therefore not affected by fluctuations in the ringgit exchange rate. The remainder of external debt that was denominated in FCY was largely subject to prudential requirements on liquidity and funding risk management.³⁰ Moreover, intragroup borrowings³¹ accounted for 35.5% of FCY external debt, which were generally more stable and on concessionary terms.

BNM's international reserves increased to USD116.9 billion as at end-2021 (2020: USD107.6 billion), sufficient to finance 7.7 months of retained imports and was 1.2 times the short-term external debt³². The international reserves were also adequate to finance 6.1 months of imports of goods and services, a new reserves adequacy indicator communicated by BNM since the release of fortnightly reserves position of 15 February 2022.³³ Additionally, Malaysia's international reserve is deemed adequate by the IMF, exceeding 100% of the IMF Reserve Adequacy Metric (ARA), under a floating exchange rate regime. In 2021, the gross short position of FCY swaps increased to USD7.6 billion (2020: USD5.8 billion), reflecting the Bank's operations to manage liquidity in the domestic financial system.

It is important to emphasise that international reserves are not the only means to meet external obligations. In particular, BNM's progressive liberalisation of the foreign exchange policy³⁴ has facilitated the accumulation of FCY external assets by banks and corporates. These assets, particularly the liquid portion amounting to RM781.1 billion, can be drawn down to meet resident entities' external debt obligations without creating a claim on international reserves.

Chart 5: Liquid External Assets and Potential Claims on International Reserves



¹ Consist of portfolio investments and currency and deposits

² Consist of deposits and interbank placements, bonds and notes and money market instruments

³ Including the forward leg of currency swaps

Source: Bank Negara Malaysia

³⁰ Including requirements imposed on banks under local banking regulations.

³¹ Comprises intragroup loans and intragroup interbank borrowings.

³² For more details on BNM's international reserves, please refer to "Building Buffers: Roles and Functions of BNM's International Reserves" feature article in BNM's Annual Report 2020.

³³ For more details, please refer to "Expansion of the Measure on Reserves Coverage of Imports – from Retained Imports to Imports of Goods and Services" article in BNM's Quarterly Bulletin for fourth quarter of 2021.

³⁴ A set of prudential measures related to the foreign exchange market to promote monetary and financial stability conducive to the sustainable growth of the economy and safeguarding the balance of payments position.

Headline inflation turned positive in 2021 while core inflation remained subdued

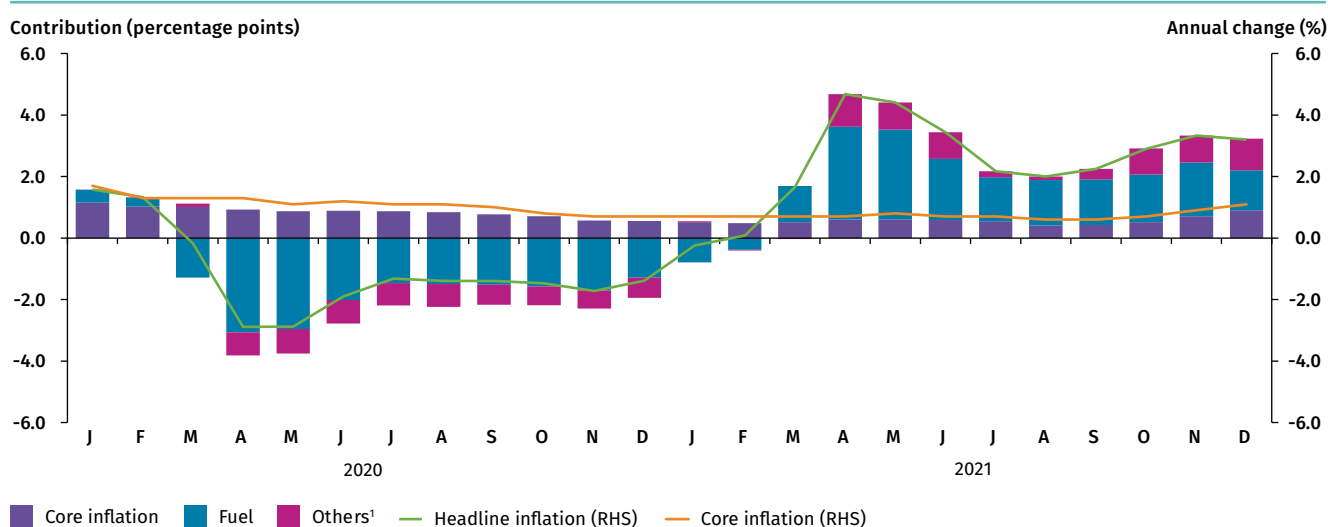
Headline inflation increased in 2021, averaging at 2.5% for the year (2020: -1.2%). The higher inflation was driven mainly by fuel inflation³⁵ (Chart 1.14), which largely reflected the base effects from the low retail fuel prices in 2020. Furthermore, the lapse in the effect from the tiered electricity tariff rebate³⁶ also contributed to increased inflation.

Global supply-side disruptions³⁷ also contributed to the upward price pressures. The impact on domestic consumer prices, however, was mostly limited, due in part to the absorption of rising cost prices along the supply chain amid the uncertain demand environment. In particular, despite the increase in the Producer Price Index (PPI) for crude and intermediate materials throughout 2021, the pass-through to finished goods and consumer prices was dampened for most of the year.³⁸ Administered

prices on selected goods³⁹ also partly contained the impact. Nevertheless, towards year end, there was some uptick in prices attributed to supply-related factors, particularly for fresh food items. Domestic seasonal factors, including the adverse weather conditions, were also at play in driving the higher prices of selected food items such as *fresh vegetables*.

Despite the higher headline inflation in 2021, price pressures were not broad-based for the most part of the year. Towards the end of the year, however, upward pressure on prices was more pervasive as economic activity picked up amid an environment of higher input costs⁴⁰ (Chart 1.15). This led to some pressure on households' cost of living, as selected items that recorded higher inflation were essential and frequently-purchased items, such as *fresh meat* and *eggs*. Nevertheless, mitigating factors remained in place to alleviate households' cost burdens, including subsidies on key consumer items, income transfers to vulnerable segments, and festive season price controls on certain necessities.⁴¹

Chart 1.14: Contribution to Headline Inflation by Components



¹ Others include price-volatile items and other price-administered items (excluding fuel).

Source: Department of Statistics, Malaysia and Bank Negara Malaysia estimates

³⁵ The extent of fuel inflation was capped due to the fuel price ceiling (RON95: RM2.05/litre; Diesel: RM2.15/litre) despite the rising global oil prices throughout the year. The fuel price ceiling was reintroduced in February 2021, and was lower from the previous ceiling of RM2.08/litre for RON95 and RM2.18/litre for Diesel.

³⁶ The tiered electricity tariff rebates were implemented under the Bantuan Prihatin Elektrik scheme from April to December 2020, with rebates ranging from 2% to 50% depending on monthly electricity consumption.

³⁷ These included disruptions in factories and shipping ports due to resurgences of COVID-19 and higher operating costs due to pandemic-containment measures.

³⁸ For further details, please refer to BNM EMR 2021 Box Article on 'An Anatomy of Inflation: Effects from the Prolonged Pandemic'.

³⁹ For example, fuel price ceiling, cooking oil subsidy and the Festive Season Maximum Price Control Scheme on selected fresh food items.

⁴⁰ The higher input costs were reflective of the higher global commodity prices, which contributed to higher feed costs and fertiliser costs domestically.

⁴¹ For further details, please refer to Spotlight article in BNM Annual Report 2021 on 'Cost of Living Revisited: Causes and Consequences'.

An Anatomy of Inflation: Effects from the Prolonged Pandemic

Introduction

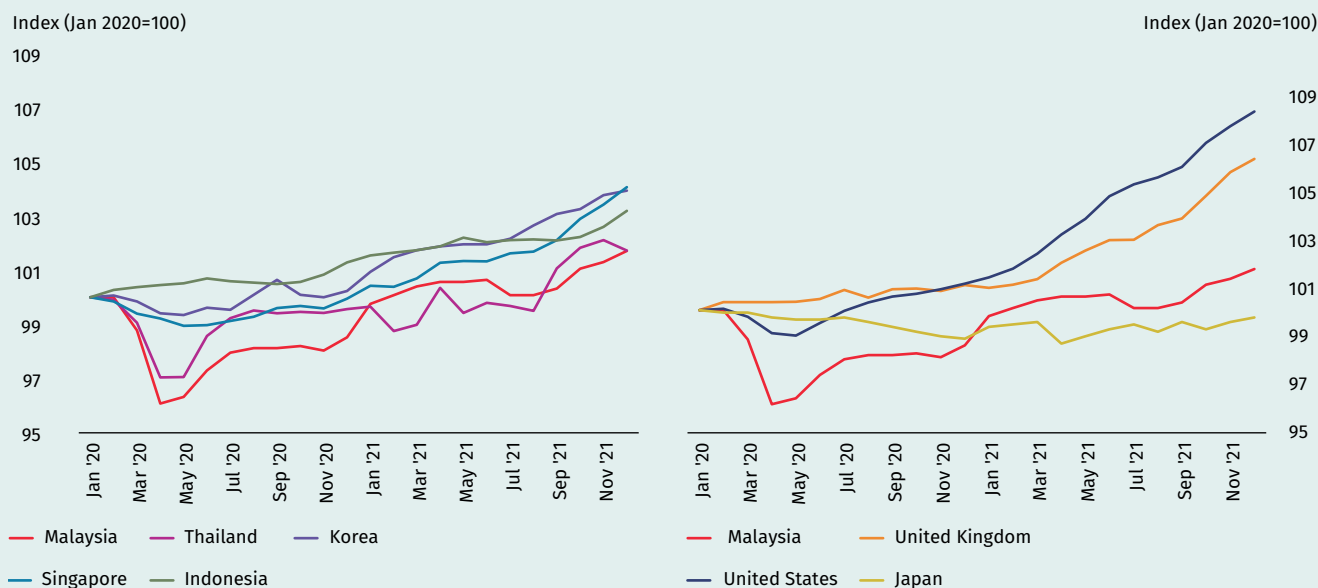
In Bank Negara Malaysia's 2Q 2020 Quarterly Bulletin¹, an interim assessment of how the COVID-19 pandemic would impact consumer inflation was outlined. Since then, the pandemic impact has not just persisted, but also evolved. Globally, the risks to consumer inflation have turned from being deflationary at the onset of the pandemic, to inflationary at present. With the uneven pace of the global economic recovery, the extent of inflationary pressures have also varied in magnitude across countries (Chart 1).

This article provides an update on the pandemic effects on consumer inflation in Malaysia. Given the highly uncertain outlook, it also contextualises the risks to consumer inflation from pandemic disruptions going forward by exploring potential country-specific factors. The findings suggest that some of the pandemic disruptions driving high consumer inflation in some other countries are either less severe or partly mitigated in Malaysia. Nonetheless, vigilance continues to be warranted. With some staple food segments more exposed to acute upward price pressures, concerns over rising cost of living remain prominent.

Breaking down the pandemic's impact on consumer inflation

In assessing the pandemic impact to consumer inflation, a framework adapted from Shapiro (2020a) is utilised.² Selected items in the Consumer Price Index (CPI) basket³ are placed into two mutually exclusive groups: COVID-

Chart 1: Evolution of Consumer Price Indices since January 2020



¹ This article is an extension to the Box Article on *COVID-19: Impact on Inflation*, published in Bank Negara Malaysia's Quarterly Bulletin 2Q 2020. The previous box article highlighted that Malaysia had experienced muted inflationary pressures since the onset of the pandemic. It also outlined the mechanisms by which the pandemic could affect inflation going forward, including changes in labour market conditions and competitive dynamics.

² A complete replication is not possible due to data limitations. In particular, while Shapiro (2020a) considered both price and quantity adjustments in the empirical exercise, this article only considered price adjustments, due to unavailability of granular and frequent personal consumption expenditure data. A framework based on difference-in-difference is used.

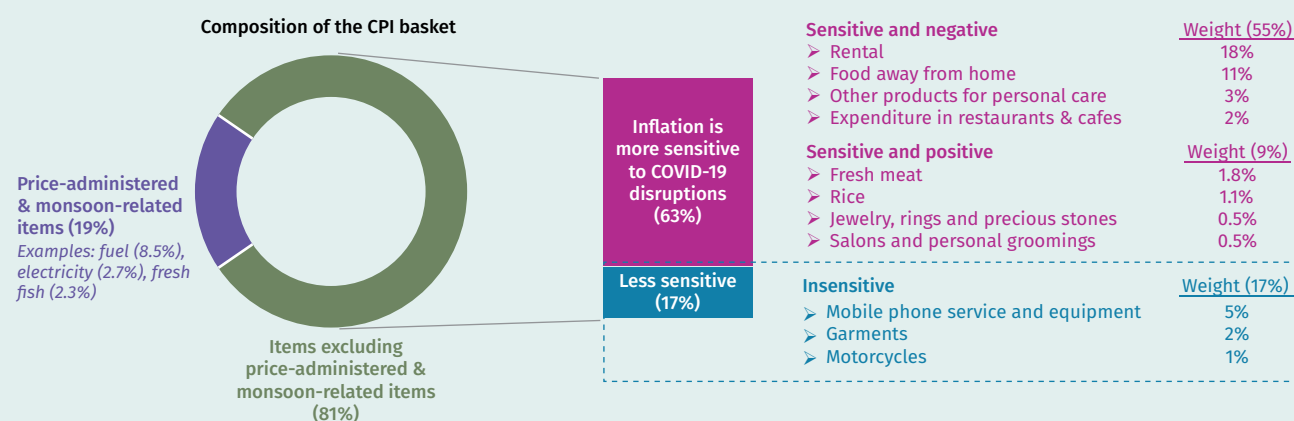
³ At the 4-digit level of the CPI basket.

sensitive⁴ or COVID-insensitive. This classification is designed to capture the direct effects of the pandemic. Namely, inflation for COVID-sensitive items would correspond more with disruptions from the pandemic, such as social distancing, supply chain constraints, or pent-up demand. As these disruptions intensify, so will the impact on consumer inflation. Conversely, as they fade away, the impact would likely moderate in tandem.

In contrast, COVID-insensitive items are less likely to be directly influenced by such factors. An implication of this is that if excessive and persistent price pressures have begun to spread in the less sensitive items, it could signal price pressures becoming more entrenched (Casselmann, 2021).

The classification is summarised in Chart 2. Sensitive categories comprise around 63% of expenditures in the CPI basket. A closer look shows that the pandemic disruptions can be either negative or positive to inflation on a net basis, reflecting the balance of demand and supply. For instance, items such as *rental* had exhibited reduced inflationary pressures relative to pre-pandemic trend at the onset of the pandemic outbreak, suggesting their greater sensitivity to demand conditions. This group of items is referred to as “sensitive and negative”. Conversely, some items had exhibited increased inflationary pressures relative to pre-pandemic trend at the onset of the pandemic outbreak, potentially reflecting their greater sensitivity to supply and cost pressures⁵ (e.g. disrupted supply chains and standard operating procedures (SOP) costs). These items are referred to as “sensitive and positive”. As the balance of demand and supply induced by the pandemic evolves, so likely would the inflation of these sensitive items.

Chart 2: CPI Items by Pandemic Sensitivity



Note: To ensure an assessment that is reflective of the pandemic shocks only, the classifications according to COVID-sensitivity exclude items that are price-administered (e.g. water bill, sewerage bill, gas, fuel, rail tickets). Furthermore, given exceptional monsoon season in 2021, directly affected items (i.e. fresh fish) have also been excluded. Together, these form the “Price-administered and monsoon-related” items (19% of the CPI basket). Numbers may not add up due to rounding.

Source: Department of Statistics, Malaysia and Bank Negara Malaysia estimates

As of 2021, the pandemic impact to overall consumer inflation has remained broadly contained, although a few segments have experienced acute upward pressures

Equipped with this framework, the evolution of the pandemic impact to inflation can be dissected (Chart 3). Firstly, the pandemic effects are most obvious in the “sensitive and positive” items, where prices tend to be more affected by cost pressures. At the onset of lockdown in early 2020, its higher inflation partly reflected supply-related pressures on selected food items. Namely, this included disruptions to production amid movement restriction measures, as well as some shortages in imported inputs, leading to higher prices of food

⁴ Sensitive categories are those that, following the outbreak of the COVID-19 pandemic, recorded price changes – either positive or negative – that are statistically significantly different from pre-pandemic trends. To ensure an assessment that is reflective of the pandemic shocks only, these classifications exclude items that are price-administered, and items whose prices have been largely affected by monsoon seasons. Furthermore, given that the classification was a data-driven empirical exercise on the 4-digit CPI basket in the periods following the initial pandemic outbreak, it is mainly focused on the shorter-term direct effects of the pandemic, and may miss out on longer-term structural changes arising from the pandemic.

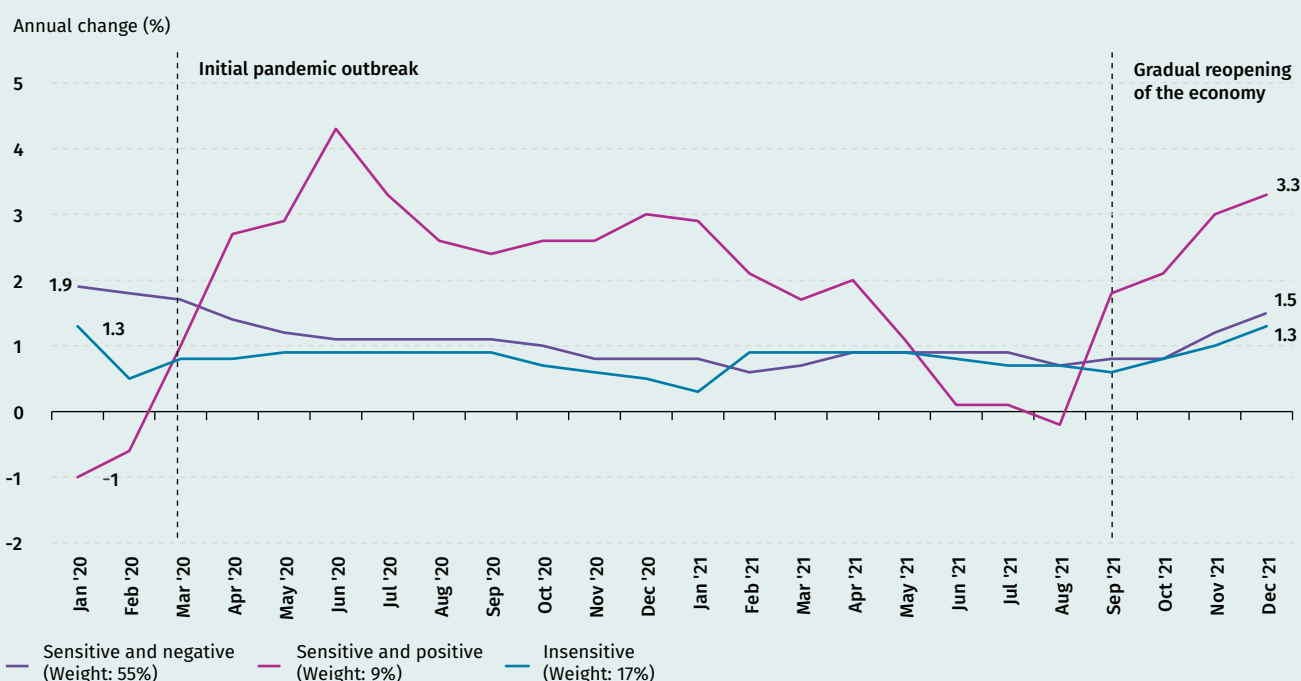
⁵ Another reason for why these items showed increased inflationary pressures at the onset of the pandemic is due to higher demand relative to supply. For instance, the pandemic led to higher global demand for safe assets such as gold, which spilled over into higher jewelry prices in Malaysia.

such as fresh chicken and eggs. These disruptions also occurred amid large-scale substitution in consumers' spending to food at home. With global supply disruptions re-intensifying towards the end of 2021, together with improving demand amid the economic reopening, its inflation has again risen in tandem.

Secondly, "sensitive and negative" inflation has been more slow-moving, broadly corresponding with domestic demand conditions. After declining for most of 2020, it has modestly increased towards the end of 2021 in line with the reopening of the economy, though remaining below the pre-pandemic level. An example of items in this category is rental inflation, which has remained subdued.⁶

Thirdly, with inflation for the "insensitive" group remaining relatively stable, there has been limited evidence of the spread of inflationary pressures beyond pandemic-related items.

Chart 3: Inflation by Pandemic Sensitivity



Source: Department of Statistics, Malaysia and Bank Negara Malaysia estimates

Ultimately, to get a better sense of how each series affects headline inflation, Charts 4 and 5 show the contributions of each category to headline inflation. Notwithstanding higher COVID-sensitive inflation at end-2021, its contribution to headline has thus far been limited (Chart 4), and somewhat close to pre-pandemic averages (Chart 5). Instead, most of the movements of headline inflation in 2021 were attributable to price-administered items, mainly reflecting the unwinding of policy measures introduced during the height of the pandemic (i.e. electricity rebates), and the base effect from fuel prices.⁷

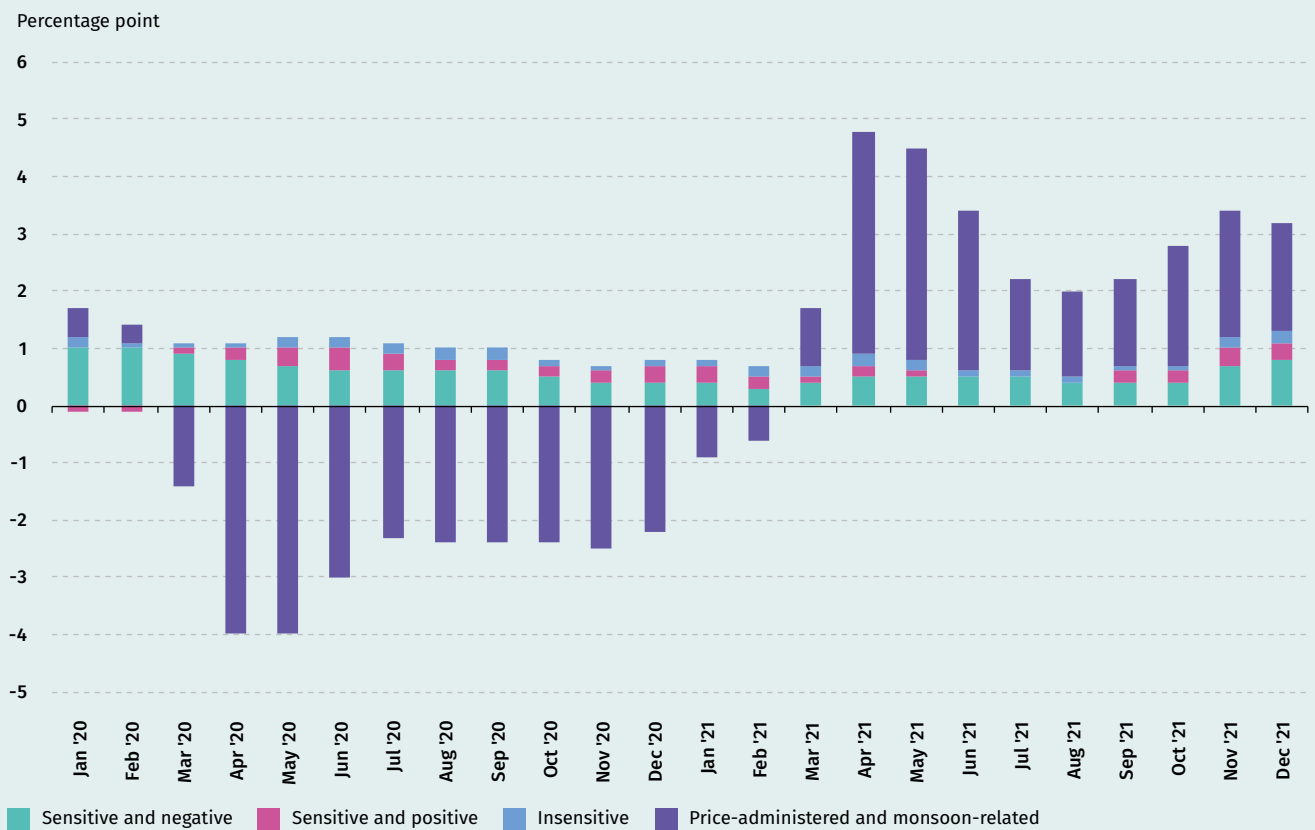
Explaining differences in consumer inflation across countries

The category-level analysis suggests that the pandemic effects to consumer inflation have so far been broadly contained, with most price pressures limited to a few segments. As demand continues to recover going forward, and with supply disruptions remaining acute, consumer prices could experience greater increases. But how high could consumer inflation be? Amid elevated uncertainty, emerging studies could provide some guidance.

⁶ Rental inflation in December 2021 is 0.6% (2011-2019: 2.5%).

⁷ The administered ceiling price of RON 95 has remained unchanged at RM2.05/litre from March 2021 to December 2021. The increase in fuel inflation was instead largely due to the low base in 2020.

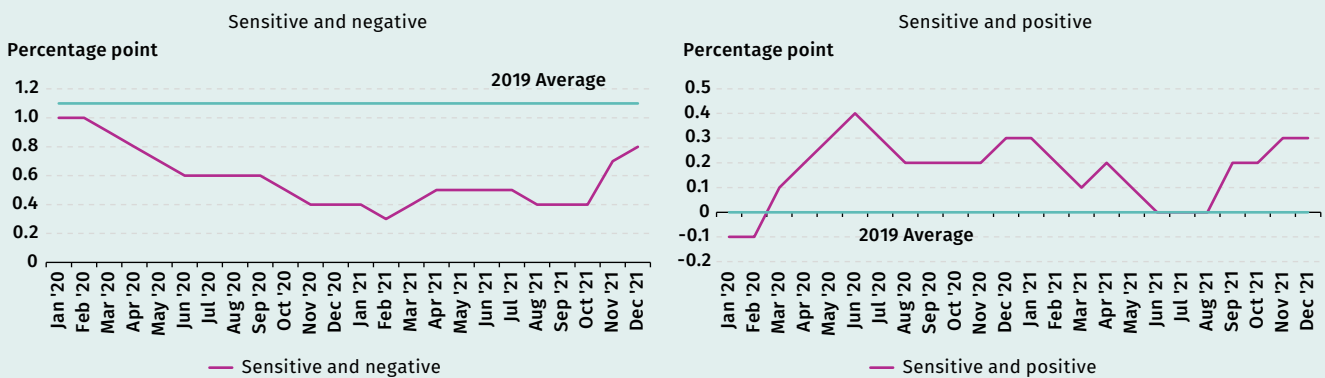
Chart 4: Contribution to Headline Inflation



Note: To ensure an assessment that is reflective of the pandemic shocks only, the classifications according to COVID-sensitivity exclude items that are price-administered. Furthermore, given exceptional monsoon season in 2021, directly affected items (i.e. fresh fish) have also been excluded. Together, these form the "Price-administered and monsoon-related" items (purple bar).

Source: Department of Statistics, Malaysia and Bank Negara Malaysia estimates

Chart 5: Contribution to Headline Inflation from COVID-sensitive Items



Source: Department of Statistics, Malaysia and Bank Negara Malaysia estimates

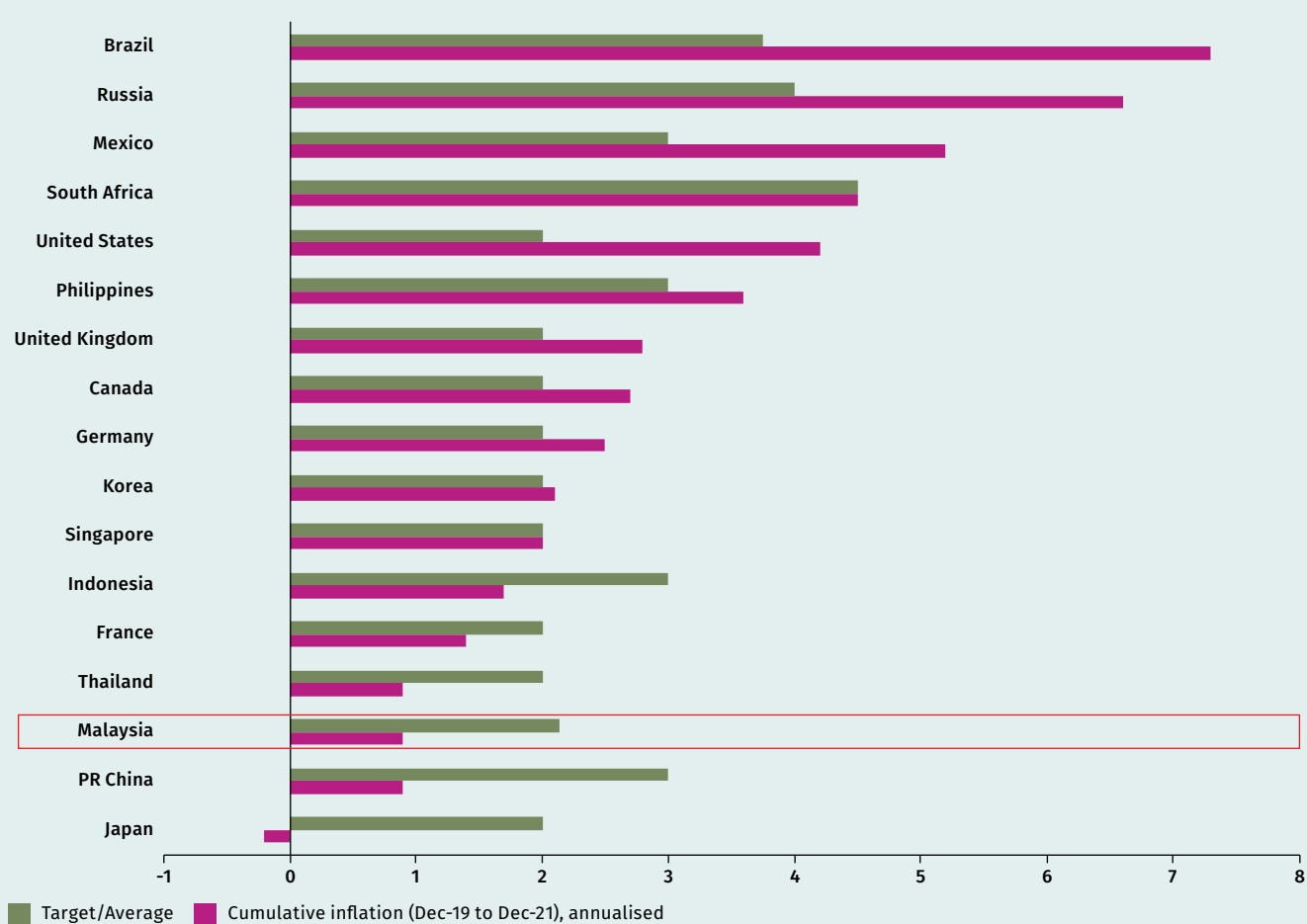
Chart 6 shows that while higher consumer inflation is common worldwide, it is more severe in some countries than others.⁸ This observation suggests country-specific factors at play, which have hindered or amplified the inflationary effects. Namely, on the demand side, these include the pace and magnitude of recovery, the strength of labour market (i.e. spare capacity), and the magnitude of policy support to the economy. On the supply side, these include price interventions by authorities, the proximity to global manufacturing hub, and the extent of labour supply disruptions.

⁸ Annualised cumulative inflation is used because some of the increase in inflation in 2021 reflects the unwinding of Government measures in 2020.

On the demand side, a factor identified by Adrian and Gopinath (2021) to be the source of this variance is the pace and magnitude of demand recovery. In several countries, economic activities have rebounded exceptionally quickly. It is in these countries, where the economy has recovered sharply, that underlying inflation⁹ has tended to increase the most (Chart 7). For some countries such as Malaysia, where economic activities remain substantially below its pre-pandemic trend, there remains spare capacity and the upside risks to underlying inflation are relatively more muted.

Partly, this reflects the differences in labour market conditions, which have recovered more sharply in some countries, contributing to stronger wage and demand pressures in these countries (Chart 8). This was in addition to the exceptional degree of policy support, for instance in the US, which has lifted demand for goods at a time when supply has not commensurately recovered, leading to greater price pressures (Chart 9) (Gopinath and Adrian, 2021; Goodhart and Pradhan, 2020). Correspondingly, a measure of COVID-sensitive items in the US has seen significant inflation throughout 2021 (Chart 10). By contrast, such recovery in demand and labour market conditions has been more gradual amongst regional economies, including Malaysia.

Chart 6: Cumulative CPI Inflation (Dec '19 to Dec '21, annualised %)

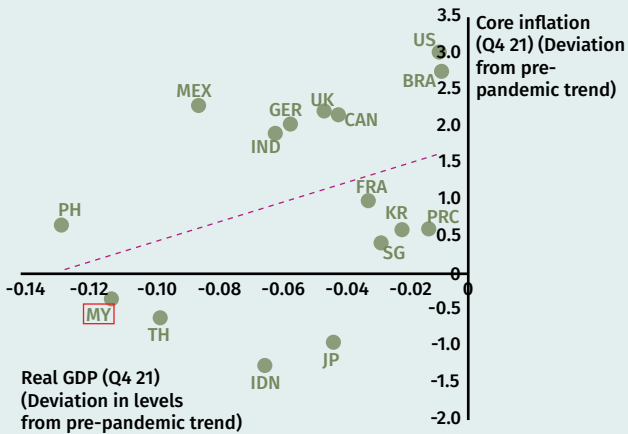


Note: For countries with a range of inflation targets, the midpoint is used. For those without explicit inflation target, inflation deemed as consistent with overall price stability as stated by respective central banks is used. Otherwise, as is the case for Malaysia, historical (2011-2019) average is used. Some countries, like the US, target core inflation. Annualised cumulative inflation is used because some of the increase in inflation in 2021 reflects the unwinding of Government measures introduced in 2020. In such a case, using a year-on-year comparison can be misleading.

Source: International Monetary Fund, FRED, national authorities and Bank Negara Malaysia estimates

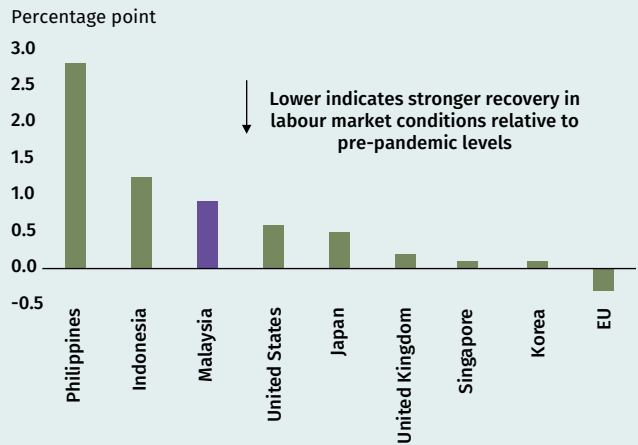
⁹ Measured by core inflation, defined as inflation excluding fuel and food inflation components.

Chart 7: Core Inflation and Economic Recovery



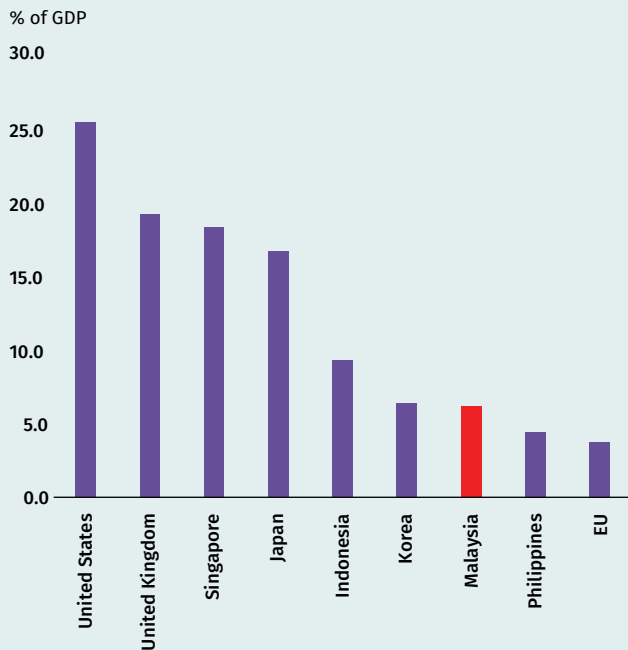
Source: Bank Negara Malaysia estimates based on Department of Statistics, Malaysia, national authorities and Adrian and Gopinath (2021).

Chart 8: Change in Unemployment Rates (percentage point change between end-2021 and end-2019)



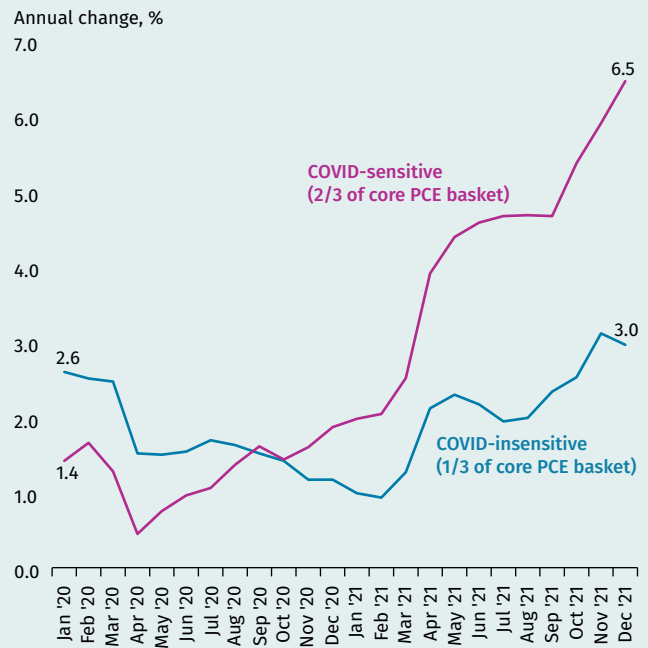
Source: Macrobond

Chart 9: Additional Spending / Foregone Revenues in Response to COVID-19



Source: International Monetary Fund

Chart 10: US Core Inflation by COVID-Sensitivity

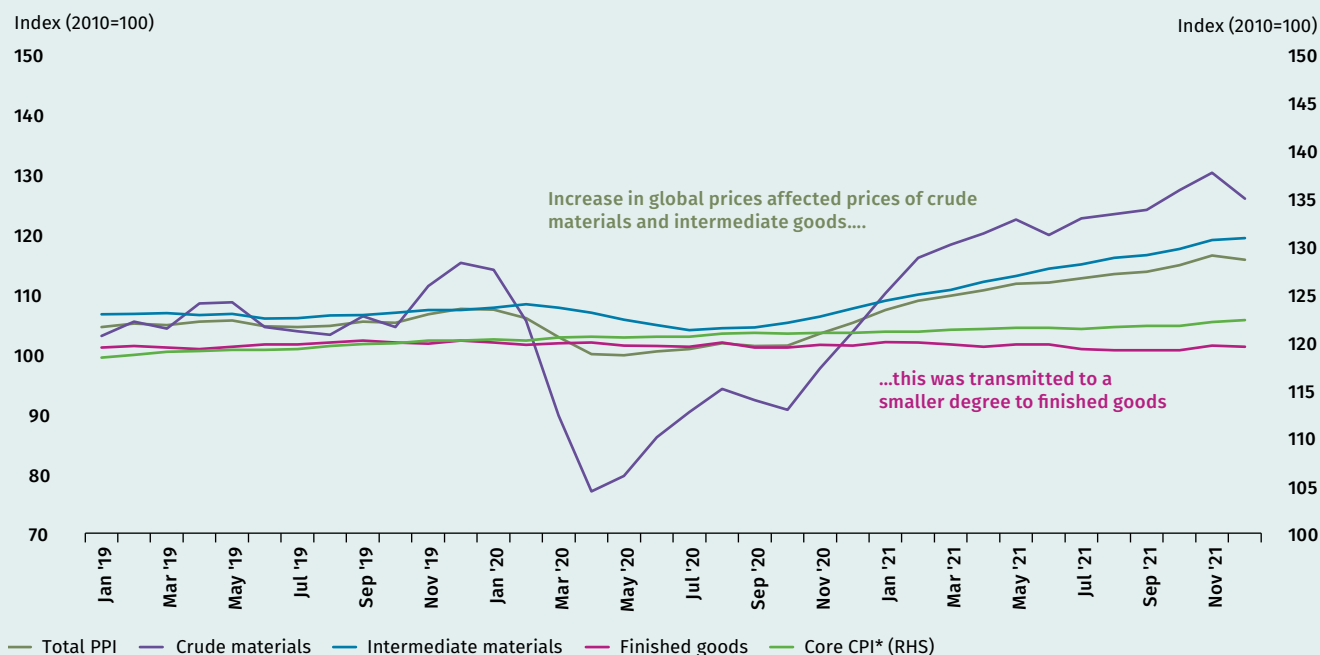


Source: Shapiro (2020a)

Nonetheless, global supply disruptions have made production inputs, from shipping to energy and commodities more expensive. At this juncture, these global supply disruptions have already been more prolonged than expected (Adrian and Gopinath, 2021). While these factors have materialised in elevated Producer Price Index (PPI) globally, the extent of pass-through to consumer prices has varied across countries. For Malaysia, the pass-through to CPI has thus far remained limited, with costs having been largely dampened along the supply chain (Chart 11).¹⁰ Should these cost pressures persist, they could be passed on to consumers to a greater degree going forward.

¹⁰ Based on recent engagements by Bank Negara Malaysia's Regional Economic Surveillance, many firms continued to cite upward pressures on costs of raw and input materials. However, most firms did not expect to fully pass on cost increases given the need to remain conservative due to demand conditions.

Chart 11: Producer Price Index: Local Production by Stage of Processing



* Core CPI excludes the direct impact from consumption tax policy changes.

Source: Department of Statistics, Malaysia and Bank Negara Malaysia estimates

However, key structural factors suggest that the impact to Malaysia's consumer inflation would likely be relatively contained at this juncture. Firstly, while higher global energy prices have contributed significantly to inflation in many countries, the direct impact has been contained in Malaysia.¹¹ This is due to price interventions, namely price controls on retail fuel and electricity tariff regulations, which have mitigated the impact to consumer prices despite surging global crude oil and coal prices.¹² More recently, price controls on key food items have further alleviated price pressures for consumers.¹³

Secondly, shipping costs have risen globally, but the severity has been less in regional Asian economies (Chart 12). In part, this reflected the sharp rebound in import demand from the US, relative to other countries.¹⁴ Such surge in demand has put upward pressure on long-distance costs, affecting other regions too. The shipping cost from China to Europe and South America has quadrupled in 2021 (Leather, 2021). In contrast, cost increases to regional Asian economies have been relatively contained, in part reflecting the proximity to the global manufacturing hub.

Thirdly, supply disruptions in labour workforce – workers leaving the workforce in large numbers, particularly the US, in what is being called the “Great Resignation” – generally do not appear to be as evident in Malaysia. For economies facing such disruptions, the resulting labour shortages could lead to stronger wage pressures as employers seek to attract workers through higher compensation.¹⁵ Notably, the majority of those who left the Malaysian labour force during phase 1 of the 2021 National Recovery Plan (NRP) cited transient factors, such as “household or family care” and “going for further studies”, as reasons for not seeking work¹⁶, rather than

¹¹ While fuel inflation was a major driver of higher headline inflation for Malaysia in 2021, this largely reflected base effects following the exceptionally low fuel prices in the previous year. The full extent of impact from higher global oil prices, however, was partly mitigated by the fuel price ceiling in place throughout most of the year (RON95: RM2.05 per litre; Diesel: RM2.15 per litre).

¹² Nonetheless, there remain ways by which the higher global energy prices could indirectly affect Malaysian inflation. For instance, fertilisers, which are by-products of natural gas, are a cost component of agricultural products, and could transmit energy costs to food inflation.

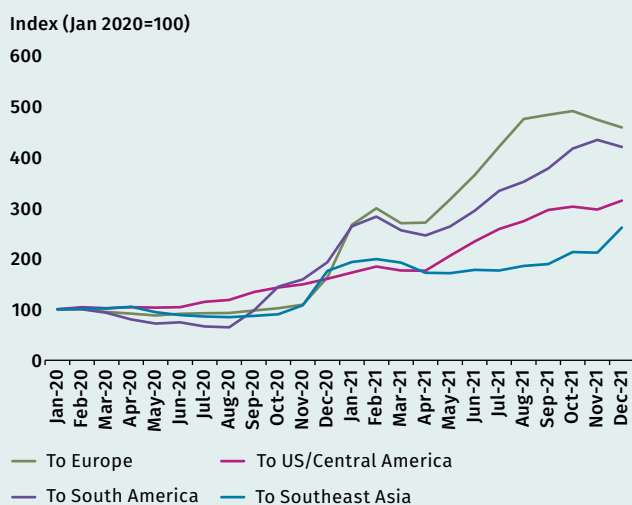
¹³ Across different countries, there are various measures undertaken to soften the impact from rising energy prices, which may not necessarily involve price controls. These include transfers to low-income households, energy tax cuts and excess profit taxes on energy companies.

¹⁴ For instance, over the course of 2021, annual US ocean retail imports are on track to set a new record, up more than 20% compared to 2019 according to estimates by the US National Retail Federation (NRF, 2021).

¹⁵ Furman (2021) partly attributes the high nominal compensation growth in the US to the reduction in labour supply coinciding with a surge in labour demand, as reflected by record-high job openings.

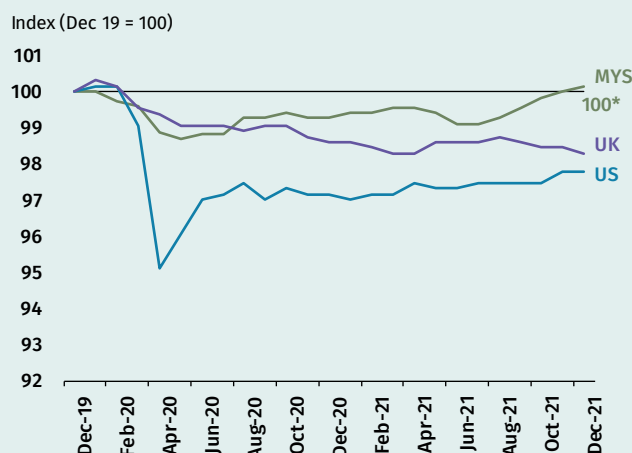
¹⁶ Staff assessment based on Quarterly Labour Force Survey, Department of Statistics Malaysia.

Chart 12: Shipping Costs from PR China



Source: Macrobond

Chart 13: Labour Force Participation Rate



* Note: Malaysia's labour force participation rate in Dec-21 is 69%

Source: Macrobond and Bank Negara Malaysia estimates

retirements, as is the case in the US.¹⁷ Reflecting this, Malaysia's labour participation rate has returned close to pre-pandemic levels in November 2021 (Chart 13), as supply of labour broadly remains forthcoming, albeit with foreign labour shortages remaining in selected sub-sectors.¹⁸ In tandem, wages continue to exhibit moderate recovery and have not outpaced productivity growth, reducing the risk of second-round inflationary impact.¹⁹

Vigilance is warranted despite the expectations of manageable inflationary pressures

As domestic economy recovers, the normalisation of underlying price pressures is expected.²⁰ The analysis by CPI segments, however, implies that excessive inflation pressures from pandemic disruptions have thus far remained contained. Moreover, country-specific factors suggest that overall consumer inflationary pressures in Malaysia are likely to be relatively manageable in the medium term, given some structural and policy factors. Nonetheless, vulnerabilities remain, especially given recent geopolitical developments. Of note, some essential food items, such as fresh meat, are COVID-sensitive and could see larger price pressures that bring negative consequences to households' cost of living.²¹

It is important to remain watchful for signs of price pressures spreading persistently to the rest of the economy. More broad-based and persistent price increases could cause long-term inflation expectations to become unanchored, leading to second-round effects as businesses keep increasing prices in anticipation of higher inflation, or wages increase in an upward spiral, as workers persistently demand for higher wages to make up for the expected losses in purchasing power. Nonetheless, this remains a tail risk. For 2022, while the inflation outlook is subject to upside risks, headline inflation is projected to remain manageable.

¹⁷ IMF (2021) found that the drop in labour participation in the US was driven by more persistent factors such as increased inactivity among older workers and shifting worker preferences.

¹⁸ For example, the agriculture sector and selected manufacturing sub-sectors have experienced shortages of foreign labour due mainly to pandemic containment measures, though these are expected to gradually ease in 2022.

¹⁹ Such a phenomenon, also called "wage-inflation spiral", occurs when stronger workers' bargaining power leads to wage pressures and, in the absence of corresponding productivity improvements, firms in turn pass on the extra labour cost by increasing consumer prices. As workers in response push for even higher wages, this creates a self-fulfilling cycle of rising inflation.

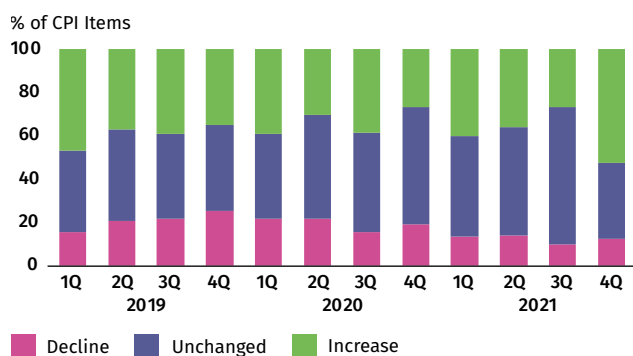
²⁰ For more details on the inflation outlook for the year, refer to Chapter 2: Outlook and Policy in 2022.

²¹ Nonetheless, the introduction of fresh chicken ceiling price from 5 February 2022 would help contain the upward pressures on consumer prices. For more details on cost of living in 2021, refer to the box article Cost of Living Revisited: Causes and Consequences in the 2021 BNM Annual Report.

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Chart 1.15: Month-on-Month Price Changes of CPI Items*



* Based on the month-on-month inflation for 125 CPI items at the 4-digit level (average for the quarter).

Source: Department of Statistics, Malaysia and Bank Negara Malaysia estimates

Underlying inflation, as measured by core inflation⁴², remained subdued throughout the year, averaging at 0.7% (2020: 1.1%) (Chart 1.14). The more muted underlying inflation reflected the spare capacity in the economy amid a moderate recovery in the labour market. This was following the reimposition of domestic containment measures during the year, which led to reduced economic activity. Nevertheless, underlying inflation edged up towards the end of the year, in line with the improved demand conditions following the resumption of economic activity (4Q 2021 average: 0.8%; 1Q – 3Q 2021 average: 0.7%).⁴³

Accommodative monetary policy supportive of economic recovery

Monetary policy remained accommodative in 2021, with the Overnight Policy Rate (OPR) unchanged at the historical low of 1.75% throughout the year. The thrust of monetary policy for the year was towards ensuring sustainable economic growth in an environment of manageable price pressures. The accommodative monetary policy was maintained to provide continuous broad-based support for the economic recovery over the prolonged pandemic period.

The Monetary Policy Committee (MPC) assessed that the domestic economy remained on track for a broad recovery in 2021. In early 2021, the economy

continued to show signs of resilience, with the growth trajectory projected to improve, driven by the stronger recovery in global demand and increased public and private sector expenditure amid continued support from policy measures. By mid-year, however, the prospects for domestic recovery were dampened by the reimposition of more stringent nationwide containment measures. Nonetheless, the economy was expected to resume its recovery path into 2022 as economic activity gradually normalised following the economic reopening towards the year end. The recovery was also expected to be underpinned by continued support from the external sector amid the strength in global demand. Notwithstanding the ongoing recovery, domestic growth outlook remained subject to downside risks throughout the year, particularly due to uncertainties surrounding the developments of the pandemic, and a weaker-than-expected global growth recovery.

Meanwhile, the risks to inflation were assessed to remain manageable. Despite some upward cost pressures from higher global commodity prices and supply-side disruptions, the spillovers to consumer prices were relatively moderate. The price increases were also from a relatively low base in the previous year and were normalising towards its long-term average in line with the improving demand conditions. Risks to inflation arising from second-round effects amid the cost-push pressures from global commodity prices were assessed to be limited. In addition, there had not been indications of significant wage pressures amid an uneven recovery across labour market segments, while longer-term inflation expectations remained anchored. Importantly, underlying inflation was subdued for most of 2021 and was projected to remain modest in 2022 given the continued spare capacity in the economy and slack in the labour market.

Given the balance of risks to the outlook for both domestic growth and inflation, the MPC therefore considered the stance of monetary policy to be appropriate and accommodative. As the pandemic evolved during the year, the MPC was faced with uncertainties surrounding the outlook for growth and inflation. Nonetheless, the ongoing monetary policy support was deemed necessary as the recovery was uneven with considerable uncertainty owing to developments surrounding the pandemic. Such accommodative stance reflected the MPC's

⁴² Core inflation is computed by excluding price-volatile and price-administered items.

⁴³ The increase in core inflation towards the end of the year was largely contributed by discretionary items such as *food away from home, restaurants and hotels, and furniture and furnishings*.

intention to avoid a premature withdrawal of policy support until the economic recovery is more entrenched and sustainable. This was feasible amid the relatively modest outlook on inflation and limited risks to financial imbalances.

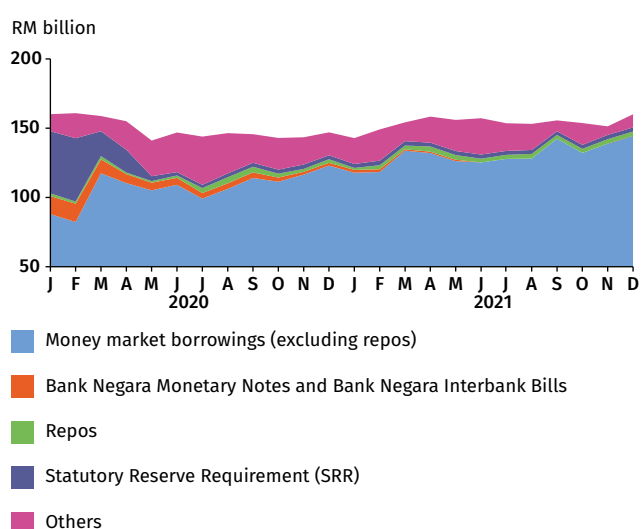
In considering the appropriate degree of monetary accommodativeness, the MPC also took into account the fiscal and financial measures that had been put in place, as well as the broad policy toolkit available to the Bank. While monetary policy was crucial in providing broad-based support, it was also complemented with the other targeted policies that were better tailored to provide support to segments of the economy that were experiencing an uneven recovery. At the same time, the MPC was mindful that other measures, including structural reforms, are needed to enhance potential growth for the economy and secure sustainable growth in the medium term.

In line with the accommodative monetary policy, the Bank's monetary operations have continued to ensure conducive domestic liquidity conditions. At the system level, aggregate outstanding liquidity placed with the Bank remained ample at RM160.1 billion (2020: RM147.0 billion) (Chart 1.16) amid net capital inflows and continued trade surplus for the year. At the institution level, almost all banking institutions continued to maintain surplus liquidity positions with the Bank, with a funding preference for shorter maturities to

better manage their liquidity needs. The Bank also conducted liquidity injection operations through various instruments, including reverse repos, the outright purchase of Government securities and foreign exchange swaps to ensure orderly market conditions during episodes of bond yield volatility and intermittent periods of portfolio outflows. The extension of the Statutory Reserve Requirement (SRR) flexibility⁴⁴ further provided sustained liquidity support for financial intermediation during the year. Collectively, this has ensured the orderly functioning of the domestic financial markets and uninterrupted intermediation activity to the real economy.

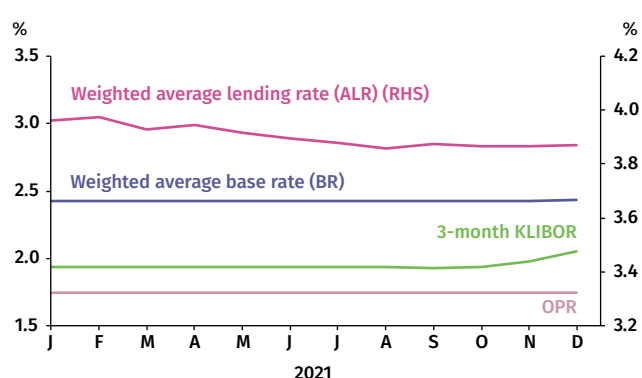
Consistent with the unchanged level of OPR, money market rates were broadly stable throughout the year. Interbank rates and the Kuala Lumpur Interbank Offered Rate (KLIBOR) were stable for the most part of the year despite some gradual increases towards year-end, particularly at the longer tenures⁴⁵ (Chart 1.17) as banks sought to bolster their stable funding sources. Banks also built up precautionary liquidity buffers in anticipation of deposit withdrawals following the expiry of tax exemption for non-individual investors' income in retail money market funds on 1 January 2022. The tighter interbank market conditions, however, was temporary, with interbank rates normalising after December. Fixed deposit (FD) rates were also stable for tenures across 1 to 12 months. As such, banks' average cost of funds

Chart 1.16: Outstanding Ringgit Liquidity Placed with Bank Negara Malaysia (at end-period)



Source: Bank Negara Malaysia

Chart 1.17: Policy, Interbank and Lending Rates (at end-period)



Source: Bank Negara Malaysia and Bloomberg

⁴⁴ The flexibility was provided for banking institutions to recognise MGS and Malaysian Government Investment Issues (MGI) as part of the SRR compliance. This SRR flexibility was initially available until 31 May 2021, and subsequently extended to 31 December 2022 in January 2021.

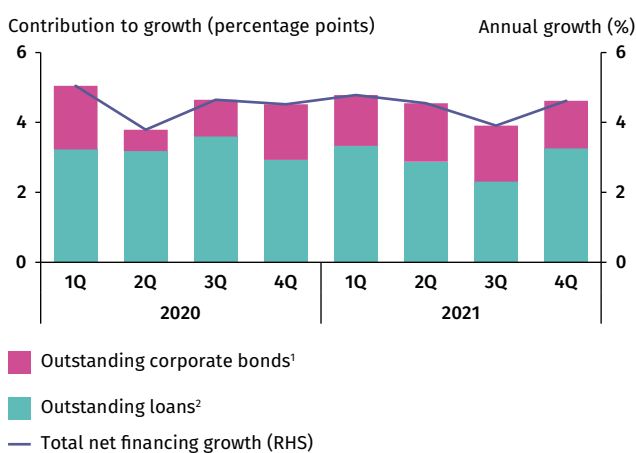
⁴⁵ Referring to rates for tenures above 1 month.

remained low (end-2021: 1.08%; end-2020: 1.21%), with continued pass-through from the earlier OPR reductions in 2020 as deposits repriced upon maturity. Amid the favourable funding conditions as well as the maturity of fixed-rate loans with higher rates, weighted average lending rate (ALR) on outstanding loans declined from 3.99% at end-2020 to 3.87% at end-2021 (Chart 1.17). Meanwhile, weighted average Base Rate (BR) was sustained at 2.43% as at end-2021 (end-2020: 2.43%). Overall, the accommodative interest rates continued to foster a conducive environment for financing economic activity.

Continued flow of credit to the private sector, with ongoing policy support

Financing to the private sector remained supportive of economic activity in 2021, underpinned by the sound banking system, orderly functioning of capital markets and ongoing policy support. The sustained growth in net financing (2021: 4.6%; 2020: 4.5%) (Chart 1.18) was driven by higher outstanding loan growth (2021: 4.3%; 2020: 3.9%) (Chart 1.19) amid a more moderate growth of outstanding corporate bonds (2021: 5.5%; 2020: 6.5%). While the growth of net financing was affected by the reimposition of movement restrictions in the middle of the year, the flow of credit rebounded subsequently, following the gradual reopening of the economy.

Chart 1.18: Total Net Financing through Banks, Non-Bank Financial Institutions and Corporate Bonds

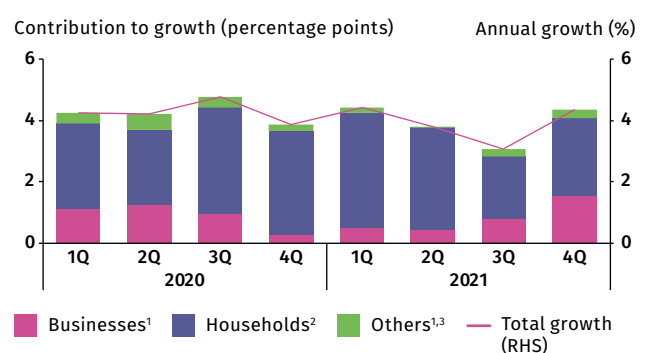


¹ Excludes issuances by Cagamas and non-residents.
² Loans from the banking system, development financial institutions (DFIs) and major non-bank financial institutions (NBFIs).

Source: Bank Negara Malaysia

The impact of movement restrictions was relatively more evident for the household segment, with outstanding household loan growth moderating to the trough of 3.3% in September before recovering to 4.1% by year end (2020: 5.5%). Nonetheless, the recovery was broad-based across all loan purposes, with improvements in both the demand and supply of credit. Stimulus measures, including the Home Ownership Campaign (HOC) and the sales tax exemption on new vehicles, also continued to provide support for household loans, especially for the purchase of residential properties and passenger cars.

Chart 1.19: Outstanding Loans by Borrower Type



¹ Loans from the banking system and development financial institutions (DFIs) only.
² Loans from the banking system, DFIs and major non-bank financial institutions (NBFIs).
³ Includes loans of financial institutions, NBFIs, Government, domestic other entities and foreign entities.

Source: Bank Negara Malaysia

For businesses, outstanding loan growth was generally sustained throughout the first eight months and picked up strongly to 4.8% by end-2021 (2020: 0.9%). Of note, financing support in the form of working capital loans was especially robust, with strong loan disbursements throughout the year (2021: RM833.4 billion; 2020: RM639.3 billion) for both small- and medium-sized enterprises (SMEs) and non-SMEs. This facilitated businesses in bridging their financing needs and tiding over the periodic disruptions to economic activity during the year. Amid the prevailing economic uncertainties, however, loans for the purpose of capital expenditure were less forthcoming, given the more moderate recovery in firms' capital expansion. Similarly, the improvement in corporate bond activity for the broader market was more gradual, with some signs of nascent recovery closer towards year end.

Policy support and financing facilities have remained in place to ensure continued flow of credit across segments of the economy. These

measures provided further targeted support for segments that were facing a more uneven recovery. These included the various facilities under the Bank's funds for SMEs, which allocations were increased and flexibilities extended⁴⁶ to benefit more SMEs. In addition, new facilities were established, namely, the Business Recapitalisation Facility (BRF) to facilitate a more sustainable financing structure through blended equity scheme and the Low Carbon Transition Facility (LCTF) to encourage the transition to low carbon practices for SMEs. Financing support

in the form of credit guarantees⁴⁷ also remained available for businesses, which played a crucial countercyclical role in mitigating the lower risk appetite by banks. For existing borrowers who faced difficulties in servicing their debt obligations, continued repayment assistance was provided by banks, while various debt advisory and resolution arrangements remained in place. Collectively, these measures cushioned the impact of the pandemic on businesses and individuals while promoting financing conditions that supported the economic recovery.

⁴⁶ Greater flexibility provided under the Targeted Relief and Recovery Facility (TRRF) and PENJANA Tourism Financing (PTF) to enable SMEs to refinance existing debt at lower costs while tapping fresh funds.

⁴⁷ These include the Danajamin PRIHATIN Guarantee Scheme (DPGS), and credit guarantees provided by Credit Guarantee Corporation Malaysia Berhad (CGC) and Syarikat Jaminan Pembiayaan Perniagaan Berhad (SJPP).

Outlook and Policy in 2022

Outlook and Policy in 2022

2022: A FIRMER RECOVERY WHILE UNCERTAINTIES AROUND

Continued recovery in the global economy as most countries gradually transition towards normalcy, albeit at varying degrees

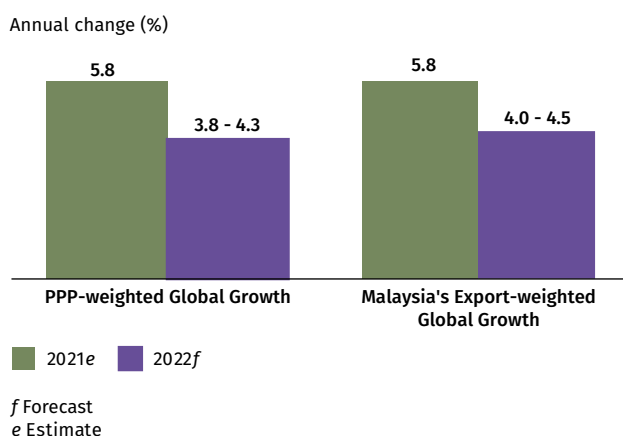
The global economy is expected to continue its recovery path in 2022, with PPP-weighted global growth and Malaysia's export-weighted global growth¹ projected to expand between 3.8% and 4.3%, and between 4.0% and 4.5%, respectively (Chart 2.1).² The improvement in labour market conditions amid the progressive reopening of economies over the past year is expected to facilitate the recovery in private sector activity. Labour markets are expected to further improve in 2022, with the unemployment rate in some major economies returning to pre-pandemic levels. With improving growth prospects and higher inflation, policy support is expected to be gradually withdrawn. Leading indicators (Chart 2.2) depict a continued recovery momentum in the first few months of the year, despite a temporary slowdown of economic activity posed by resurgences of COVID-19 cases due to the Omicron variant. Nevertheless, the ongoing military conflict in Ukraine is expected to weigh on global growth.

The growth outlook remains conditional on the path of the COVID-19 pandemic. New variants could emerge and cause a resurgence that may necessitate

¹ Aggregate growth of Malaysia's key trade partners, as weighted by their shares in Malaysia's exports. This measure of global growth is more reflective of Malaysia's exports and growth prospects.

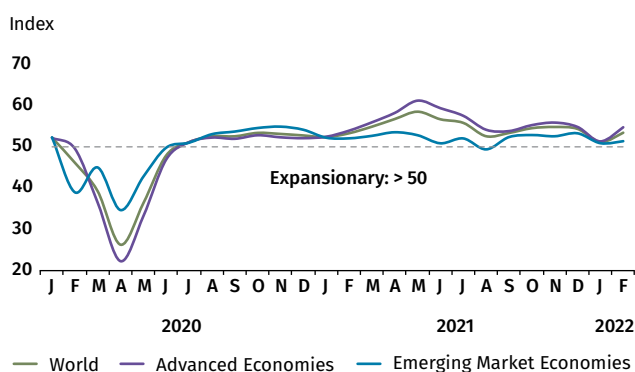
² Global growth in 2022 is expected to be more moderate compared to 2021, as economic activity normalises. The high growth in 2021 partly reflects the exceptionally low base effect from the growth contraction in 2020.

Chart 2.1: Global Real GDP Growth



Source: Bank Negara Malaysia

Chart 2.2: Composite Purchasing Managers Index (PMI)



Source: IHS Markit

a reintroduction of containment measures. In addition, resurgences of COVID-19 could also lead to labour absenteeism that would affect economic activity, due to isolation requirements and sickness. Nonetheless, the impact of such resurgences on growth is expected to be smaller compared to previous phases in 2020 and 2021, due to several factors. First, there has been continued good progress in vaccinations, as well as the introduction of new treatments. This will allow authorities to better manage the public health implications of

resurgences without resorting to tight containment measures as in previous years. Nevertheless, some countries continue to maintain a relatively stricter COVID-19 containment policy. As vaccinations progress from relatively lower rates of primary and booster vaccinations in EMEs, remaining containment measures could also be lifted.³ Second, as we move into the third year of the pandemic, more targeted approaches to containment will be favoured in balancing between considerations for public health and livelihoods. Going forward, countries will likely narrow the focus of containment measures to activities with higher risk of transmission, such as high-touch services activities, rather than the *manufacturing* sector.⁴ Some countries are also gradually phasing out the use of containment measures altogether, in an attempt to fully adapt to ‘living with the virus’. Third, greater business and consumer adaptability, through wider adoption of e-commerce, digital solutions, and efficiency-enhancing technologies, would lead to more muted impact of targeted containment measures.

Fiscal policy is expected to remain supportive of the recovery, despite some scaling back as governments pare down emergency support amid the ongoing economic recovery (Chart 2.3). In AEs, fiscal support is expected to shift away from direct support for households and firms. Instead, support will focus on long-term initiatives such as the green transition, digitalisation, as well as repairing and upgrading public infrastructure. Notably, the US Infrastructure Investment and Jobs Act⁵ is expected to allocate funds to strengthen and develop various infrastructure including transportation, power, and connectivity (broadband development). Under this initiative, funding will also be allocated to infrastructure needed for the green transition. Meanwhile, the European Union’s Multiannual Fiscal Framework and NextGenerationEU package⁶, together with national budget allocations by Member States, will continue to support investments for both the green and digital transitions. Given the shift in

³ During the recent Omicron wave, given the lower vaccination rates in EMEs (except China), containment measures were tighter compared to AEs. For example, in India, several state governments implemented weekend curfews and night curfews during the peak of the Omicron wave.

⁴ Given the continued focus of containment measures towards high-touch services, some unevenness in the pace of recovery between sectors is expected to continue.

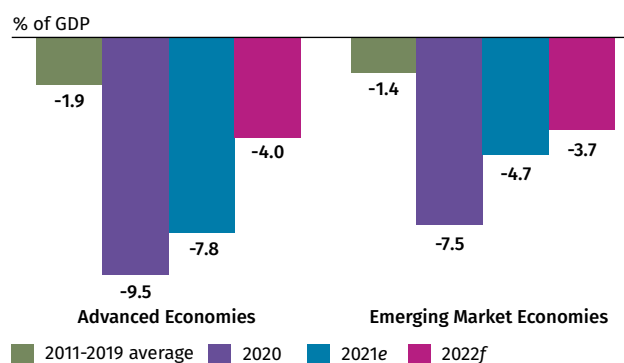
⁵ The Act authorises about USD 550 billion in new spending, to be spread over 5 years.

⁶ The package totals up to EUR 806.9 billion, of which EUR 338 billion and EUR 385.8 billion are in the form of grants and loans, respectively, for national governments. The remaining funds are allocated for additional spending of various EU programmes.

the composition, fiscal policy would provide more support for investment activity, while consumption support should moderate.

In EMEs, fiscal support is expected to remain expansionary. The scale of fiscal support, however, is expected to be smaller as some countries embark on fiscal consolidation. This reflects the more limited fiscal space and higher borrowing costs. Spending priorities for EMEs in 2022 differ according to domestic needs. India, for example, would be increasing public capital expenditure to boost infrastructure investment, amid a slight fiscal consolidation. In contrast, the Brazilian government is planning to introduce a new cash transfer programme to improve their social safety net. Meanwhile, China is expected to provide continued fiscal support to offset risks to growth from its COVID-19 containment policy and regulatory reforms. Measures include increased quota allocations for local government special bonds, which would support investment activity.

Chart 2.3: Primary Fiscal Balance



e Estimate
f Forecast

Source: International Monetary Fund (IMF)

The military conflict in Ukraine, however, is expected to weigh on global growth in 2022. The impact will be most severe for the economies of Ukraine and Russia, due to disruptions brought upon by the military incursion and impositions of sanctions, respectively. Spillovers would stem mainly from disruptions in commodity supply, given the large role of Russia and Ukraine as commodity producers in the global economy. The conflict thus far has already led to a rise in commodity prices⁷ and global inflation, which would result in increased cost pressures on firms and lower real incomes affecting household spending. While governments are expected to partially offset the impact through

⁷ Brent oil prices have risen from USD 91 at the end of January to average around USD 112 between 1st March and 24th March.

fiscal support, limited fiscal space may constrain the extent of the support. In addition, the impact of the conflict on growth prospects would vary among net commodity exporters and importers. For commodity exporters, an improvement in their terms of trade that leads to higher incomes and currency appreciation, would partially mitigate the impact of higher commodity prices on inflation, and subsequently, growth. The magnitude and timeline of the impact from the conflict remains uncertain as developments in the conflict continue to unfold. Actions of key countries, which includes the major economies, in response to the conflict will also have an important bearing on the outlook for global growth and inflation.

Elevated inflation due to higher energy prices and continued supply chain disruptions in an environment of sustained demand recovery

As the global economy recovers, inflation is projected to rise and remain elevated in 2022. This is driven by the sustained demand pressures in an environment of higher energy and commodity prices and ongoing disruptions in the global supply chain. Since late February, the ongoing conflict between Ukraine and Russia, which are major exporters of various commodities, have further exacerbated price pressures (see footnote 7), and introduced significant uncertainty to the global inflation outlook. Additionally, there is a risk that the easing of supply chain disruptions could be delayed, due to concentrated production of key inputs in Russia and Ukraine. Country-specific factors would influence the extent and sources of inflationary pressures. This would include the pace of recovery, magnitude of policy support, and regulations on energy prices.⁸ In addition, idiosyncratic factors like labour market dynamics also play a role. For example, in a number of economies, notably the US, labour shortages are expected to contribute to strong wage pressures and demand-pull inflation, amid a strong recovery in demand. Nevertheless, inflation amongst regional economies in Asia will likely remain relatively lower. This is due to existing price controls and subsidies

on energy in some regional economies.⁹ Additionally, the concentration of global manufacturing supply chains in regional economies will help to mitigate the impact of supply chain disruptions on prices, for example, through smaller increases in shipping costs.

Amid continued strength in inflationary pressures globally, a further normalisation of monetary policy is anticipated in 2022. Most central banks in AEs have signalled intentions to reduce monetary support. Having completely tapered its purchases of US Treasury and agency mortgage-backed securities, the Federal Reserve has begun to increase its policy rates. Meanwhile, the European Central Bank affirmed its intentions to scale back its asset purchase programme during the year. In EMEs, most central banks are also expected to begin normalising their monetary policies following continued inflationary pressures in some EMEs and emerging pressures in others, amid an improving growth outlook. In some European and Latin America EMEs, strong domestic demand recovery and wage pressures are expected to lead to further rate hikes. Meanwhile, regional EMEs in Asia are expected to begin normalisation of their policy rates in 2022 amid higher price pressures, following stronger recoveries during the year. In contrast, the People's Bank of China is expected to provide further monetary accommodation to support the slowing growth momentum, in an environment of low inflation¹⁰.

Nonetheless, the pace and magnitude of monetary policy normalisation remain uncertain, as they depend largely on the persistence of inflationary pressures and the strength of recovery in the economy and labour market. These uncertainties could lead to heightened financial market volatility and tightening of financial conditions. This is especially the case if there is significant misalignment between major central banks' policy paths and financial markets' expectations. As the global economy shifts away from unprecedented levels of monetary accommodation, capital flow reversals from EMEs could follow, especially from those that have seen a build-up of inflows in the past year. In addition, escalation in geopolitical tensions may exacerbate the risk of capital outflows from EMEs, as increased investor risk aversion

⁸ For further information, please refer to the box article titled "An Anatomy of Inflation: Effects from the Prolonged Pandemic".

⁹ For example, in its December 2021 Monetary Policy Report, the Bank of Thailand noted that the strength of Thailand's energy inflation would be partially offset by the Oil Fund which subsidises the diesel and cooking gas prices. Indonesian authorities have committed to keeping domestic energy prices low despite expected volatility in global commodity prices amid the recovery.

¹⁰ Aside from relatively weak domestic demand, inflation in China has remained low due mainly to a fall in pork prices as swine stocks recovered from a culling in 2020 due to an outbreak of African Swine Fever.

would lead to higher demand for safe haven assets.¹¹ These large and sudden capital flow reversals could, in turn, cause abrupt tightening of financial conditions, particularly for economies with large external financing needs, and risk derailing the global recovery momentum.

Balance of risks to global growth remains tilted to the downside, amid heightened geopolitical tensions and continued uncertainties surrounding COVID-19

The primary risk to growth arises from a potential reimposition of broad-based and strict containment measures in the event of a COVID-19 resurgence due to severe and vaccine-resistant Variants of Concern (VOCs). Strict containment measures could affect operations in production and logistics facilities, causing a re-escalation of supply chain disruptions. This, in turn, would also lead to higher and more persistent inflation, which could erode real incomes and lead to weaker spending. There is also the possibility of even higher commodity prices due to extreme weather conditions and disruptions in the production of commodities adding to inflationary pressures. Meanwhile, slower-than-expected recovery in China would pose a downside risk to global growth and trade prospects. Additionally, the unfolding developments surrounding the military conflict in Ukraine has emerged as a key risk, especially if the conflict continues to escalate further and is prolonged, or if trade and financial sanctions are intensified.

An environment of more persistent inflation or de-anchoring of inflationary expectations could lead to an increased pace of monetary policy tightening, which would lead to slower demand and tighter global financial conditions. Moreover, in an environment of tighter global financial conditions, there is an increased risk of sharp capital outflows that could lead to disorderly exchange rate adjustments and unwinding of prevailing financial sector imbalances¹² especially among vulnerable EMEs.

¹¹ This was observed during the recent military conflict in Ukraine. Greater uncertainties and investor risk aversion led to heightened volatility in the global financial markets, and higher demand for safe haven assets, such as the US dollar and Treasuries.

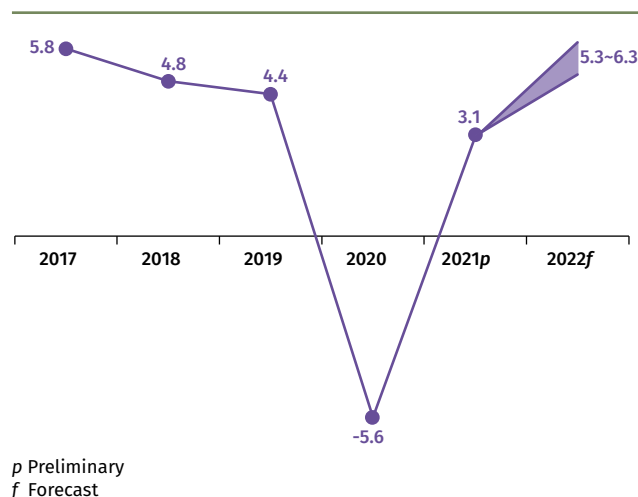
¹² Amongst EMEs, types of financial sector imbalances differ across countries. Some countries have high levels of sovereign debt that could become unsustainable amid tighter-than-expected global financial conditions, while other countries may have large external financing needs, or vulnerabilities in the banking sector.

Nevertheless, there are upside risks to global growth, arising from a faster and wider rollout of COVID-19 primary and booster vaccines as well as new treatment options for COVID-19 infections. This could reduce the severity of supply chain disruptions and the need for containment measures, supporting growth prospects while reducing inflationary pressures. There is also the possibility of additional fiscal policy support, especially in AEs.

The Malaysian economy is expected to improve further, with growth projected to be between 5.3% and 6.3% in 2022

For the Malaysian economy, the recovery is expected to gain momentum in 2022 (Chart 2.4). This is underpinned by several factors including continued expansion in external demand, full upliftment of containment measures, reopening of international borders, and further improvement in labour market conditions. In addition, the implementation of investment projects and targeted policy measures will provide further support to economic activity and aggregate demand. Taken together, these factors pave the way towards a more broad-based and sustainable recovery for Malaysia.

Chart 2.4: Malaysia's GDP Growth



Source: Department of Statistics, Malaysia and Bank Negara Malaysia estimates

Developments surrounding COVID-19 remain key in influencing Malaysia's growth trajectory in 2022, particularly in the shift towards a more calibrated and proportionate approach to managing the

domestic epidemic¹³ situation. After enduring the COVID-19 pandemic for two years, the Government, businesses, and healthcare system are now more adept at managing the spread of the virus. Under the National COVID-19 Immunisation Programme, Malaysia has achieved high vaccination rates and swiftly rolled out booster doses, which has helped to lower hospitalisations and severity of infections. As of 24 March 2022, 97.5% of Malaysia's adult population had been fully vaccinated, while 66.2% had received booster shots. Vaccines are also being rolled out to adolescents aged 12 to 17 (91.5% fully vaccinated), and children aged 5 to 11 (36.1% received first dose). The promising recent discoveries of antiviral drugs and treatments for severe COVID-19 cases would also contribute to lowering hospitalisations and deaths due to infections going forward. Therefore, where capacity of the national healthcare system remains sufficient, the Government has reaffirmed its position to avoid impositions of nationwide lockdowns and strict containment measures. Significant resurgences of COVID-19 cases could, however, impact economic activity through other channels. High absenteeism rates, for example, resulting from workers having to take medical leave and undergo quarantines may impact productivity, while cautious sentiments may suppress mobility and consumer spending. Nevertheless, measures taken to contain future outbreaks¹⁴ would balance national health considerations while minimising adverse impacts on livelihoods and the economy.

The external sector will continue to be supported by global demand, with gross exports projected to grow by 10.9% (2021: 26.0%). Strong demand from major trade partners for electrical and electronic (E&E) products, amid the continued technology up-cycle and 5G infrastructure rollouts globally, will provide support to manufacturing, investment, and exports. Being an open economy, Malaysia will, however, be affected by the impact of the military conflict in Ukraine on global growth, mainly through the trade channel. Nevertheless, the corresponding increase in global commodity prices are expected to provide support to commodity exports and some lift to nominal incomes. Meanwhile, gross imports is projected to expand by 8.1% (2021: 23.3%), reflecting

in part the demand for manufactured exports. Improvement in domestic investment activity and consumer spending will lead to higher imports of consumption and capital goods.

Domestic-specific factors, such as higher production from new manufacturing and mining facilities, expansion in existing facilities, and continued progress of large infrastructure projects,¹⁵ are expected to drive the recovery in overall economic activity. The reopening of international borders and resumption in international travel activity would lend further support to the rebound in consumer-facing and tourism-related sectors. Meanwhile, production frictions from supply chain disruptions and labour shortages¹⁶ are expected to gradually ease as the year progresses, constituting a smaller drag on growth going forward.

In the labour market, conditions are expected to improve gradually as economic activity picks up, with the unemployment rate expected to decline further to around 4% of the labour force. Early indicators suggest continued improvements in labour market conditions and affirm expectations of a further recovery in wages and income. Targeted measures also remain in place to boost labour demand, facilitate re-skilling and up-skilling, and reduce labour market frictions as re-entrants and new entrants to the labour force seek re-employment.¹⁷ These initiatives would further benefit workers who have been displaced by the COVID-19 shock, and mitigate long-term scarring effects. A sustained recovery in employment and income is expected to drive an improvement in household spending.

A stronger recovery in private sector expenditure is expected to be the main driver of growth amid the full lifting of containment measures. Private consumption is expected to record a growth of 9.0% (2021: 1.9%), as household spending will be primarily supported by recovery in income and employment. Consumer confidence is also expected to improve as vaccinations progress and containment measures are fully eased, leading to some materialisation of pent-up demand. Nevertheless, this is contingent upon the

¹⁵ Key infrastructure projects supporting growth in 2022 include East Coast Rail Link (ECRL), Pan Borneo Highways and LRT3.

¹⁶ The labour shortages in Malaysia, which were exacerbated by the closure of international borders, tend to occur in mid- and low-skilled occupations, which are usually taken up by foreign workers.

¹⁷ Job retention policies that seek to maintain existing employment relationships were newly introduced by the Government in 2020, in the form of the Wage Subsidy Programme (WSP). Additionally, the Government also implemented worker reallocation policies to boost job creation and redirect employment, through the introduction of hiring incentives under PenjanaKerjaya and JaminKerja initiatives.

¹³ 'Epidemic' refers to an increase, often sudden, in the number of cases of a disease above what is normally expected in that population in that area. 'Pandemic' refers to an epidemic that has spread over several countries or continents, usually affecting a large number of people.

¹⁴ Going forward, potential reimpositions of restrictions are expected to be targeted at reducing social activities, while most economic activity will still be allowed to operate without restrictions.

developments in the domestic epidemic situation. Meanwhile, the expected recovery in private investment (5.3%, 2021: 2.6%) reflects the resumption of existing projects and commencement of new capital spending by businesses. Overall investment intentions remain healthy, given the increase in approved investments in 2021,¹⁸ particularly in export-oriented manufacturing industries such as E&E, metal, rubber, and chemicals. Investment activity will also be supported by greater adoption of automation and digitalisation solutions, and continued capacity expansions, particularly in the *manufacturing* sector.

Importantly, policy support for households and businesses remains in place to facilitate the recovery momentum, albeit more targeted in nature, to assist vulnerable segments that were significantly affected by COVID-19. Support from the 2022 Budget measures from various cash transfers, targeted wage subsidies, and targeted loan repayment assistance will continue to provide further impetus to the economic recovery. Allocations for the Bantuan Keluarga Malaysia, EPF-related measures and tax reliefs will also provide some support to household spending. For businesses, vulnerable sectors such as tourism-related industries and agriculture would benefit from the Wage Subsidy Programme and numerous targeted grants. These measures will continue to ease cashflow burdens and safeguard

employment conditions, thereby enabling a more entrenched recovery in domestic demand.

Given the rapidly-evolving macroeconomic environment, risks to the domestic growth projection remain tilted to the downside. Downside risks stem mainly from the developments surrounding COVID-19, such as the emergence of severe and vaccine-resistant VOCs which could lead to potential reimpositions of broad-based containment measures. Other domestic factors that could affect the recovery path include slower-than-expected rollout of public infrastructure projects, more persistent labour shortages and supply chain disruptions, as well as higher-than-expected inflation which would reduce disposable income and adversely affect consumer sentiments. On the external front, worsening supply chain disruptions and heightened volatility leading to disorderly financial conditions could significantly affect Malaysia's growth and trade outlook. Additionally, prolonged and further escalation of the geopolitical tensions, particularly the military conflict in Ukraine, represents a key risk to the Malaysian economy as well, emanating from its impact to global growth and trade, prices, and financial market volatility. Conversely, factors which pose upside risks to the growth outlook emanate from higher-than-expected global growth and stronger-than-expected improvement in tourism-related sectors amid the reopening of borders.

Domestic demand continues to be the main anchor of growth

On the demand side, growth in 2022 is expected to improve, underpinned by the continued recovery in private sector expenditure. Without ruling out the possibility of future COVID-19 resurgences, the operating environment is expected to be less restrictive, with a more targeted approach to manage outbreaks compared to 2021 given the high vaccination rate among the population. This would be less disruptive to economic activity, and in turn would support a more entrenched recovery in the labour market and smoother progress of investment projects. The continued expansion in the global economy will benefit Malaysia's exports, with spillover to investments in export-oriented industries. An accommodative monetary policy, as well as targeted fiscal and financial measures for households and businesses would continue to provide additional support to growth.

Private consumption is expected to expand by 9.0% in 2022 (2021: 1.9%). This is anchored in the continued improvement in labour market conditions. In addition, the absence of strict containment measures would provide a lift to household spending. The rise in online spending since the onset of the pandemic in 2020 is expected to continue and will further spur private consumption. The materialisation of some

¹⁸ Approved investments amounted to RM306.5bn in 2021 (2020: RM167.4bn; 2019: RM211.4bn). (Source: Malaysian Investment Development Authority)

pent-up demand for selected discretionary items¹⁹ which were previously restricted due to the imposition of containment measures is also expected to provide some support to overall spending. These include discretionary spending on restaurants, hotels and recreational activities. The strength of the pent-up demand, however, is subject to the path of the epidemic situation in Malaysia. Continued targeted policy measures, particularly for vulnerable households, such as Bantuan Keluarga Malaysia and targeted loan repayment assistance remain available to help support overall spending.

Gross fixed capital formation (GFCF) is projected to rebound to 6.3% (2021: -0.9%) following an increase in capital spending by both the private and public sectors. The higher growth is primarily driven by the improvement in structures investments and continued high capital spending in machinery and equipment (M&E) to meet the increasing demand as the economy gradually recovers.

Table 1

Real GDP by Expenditure (2015=100)

	2021p	2021p	2022f	2021p	2022f
	% of GDP	Annual change (%)		Contribution to real GDP growth (percentage point)	
Domestic Demand¹	92.7	1.9	7.2	1.8	6.7
Private sector expenditure	74.3	2.0	8.2	1.5	6.1
Consumption	58.8	1.9	9.0	1.1	5.3
Investment	15.6	2.6	5.3	0.4	0.8
Public sector expenditure	18.3	1.6	3.2	0.3	0.6
Consumption	13.8	6.6	1.2	0.9	0.2
Investment	4.5	-11.4	9.6	-0.6	0.4
Gross Fixed Capital Formation	20.1	-0.9	6.3	-0.2	1.3
Change in stocks	1.3			1.7	-1.0
Net Exports of Goods and Services	6.0	-5.8	2.6	-0.4	0.2
Exports	69.2	15.9	4.8	9.8	3.4
Imports	63.2	18.5	5.1	10.2	3.2
Real Gross Domestic Product (GDP)	100.0	3.1	5.3 ~ 6.3	3.1	5.3 ~ 6.3

¹ Excluding stocks

p Preliminary

f Forecast

Note: Figures may not necessarily add up due to rounding.

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

Private investment is expected to improve by 5.3% (2021: 2.6%). This is supported by the continued expansion in global demand and the realisation of new and ongoing investments. Of significance, investment intentions remained high as reflected in the increase in approved investments in 2021, particularly in the *manufacturing* sector. Investments would also be accelerated by ongoing efforts by the Government to attract new quality investments and facilitate implementation of projects such as the Project Acceleration and Coordination Unit (PACU) and One Stop Centre (OSC) for Business Travellers.²⁰ The implementation of key infrastructure projects, such as the Malaysia Digital Economy Blueprint (MyDIGITAL), coupled with the incentives announced in 2022²¹ Budget would provide additional support to private investment activity.

Public investment is projected to expand by 9.6% (2021: -11.4%), driven by continued capital spending by both the General Government and public corporations. Investment by public corporations across all sectors is

¹⁹ For more details on pent-up demand, please refer to White Box titled "Methodologies in Assessing Pent-up Demand" on page 62.

²⁰ PACU provides end-to-end facilitation services for investors throughout the investment journey while OSC aims to ease the entry of eligible business travellers.

²¹ Key 2022 Budget measures on investment include tax incentives under the Digital Ecosystem Acceleration Scheme, tax incentives to support the development of the Electric Vehicle (EV) industry, and SME Digitalisation Grant Scheme to increase digital adoption among SMEs.

projected to improve, in line with the resumption of economic activity. The increase in fixed assets spending by the Government would be largely channelled towards public projects in transportation, education, healthcare and public utilities. Among the major infrastructure projects include the Light Rail Transit Line 3 (LRT3), East Coast Rail Link (ECRL), and Pan Borneo Highway.

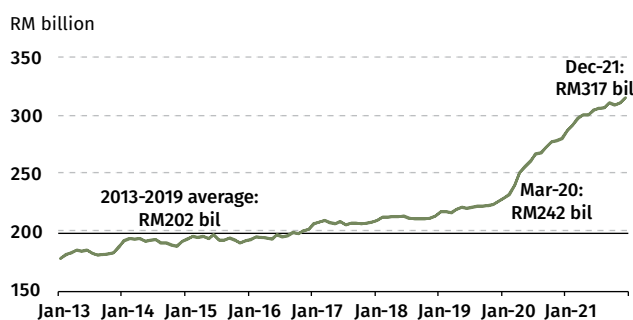
Public consumption is expected to expand by 1.2% (2021: 6.6%). The moderation is due to a slower growth in emoluments and contraction in supplies and services expenditure. Growth in public consumption, however, will remain supported by COVID-related spending which include purchases of medical supplies and procurement of vaccines and booster doses, as well as allocation for small repairs and maintenance works.

Methodologies in Assessing Pent-up Demand

Since early 2020, there was an overall increase in balances in demand and savings deposit accounts of individuals (Chart 1). Between March 2020 and December 2021, demand and savings deposits accelerated, growing at a monthly average of 18.3%. This was about five times higher than the monthly average growth in 2019 (4.1%). This increase is mainly driven by middle- and high-income households.²²

The significant build-up of large savings partly reflects precautionary behaviour as well as households not being able to spend on selected goods and services (such as restaurants, hotels, recreational activities, as well as household furnishings and equipment) due to mobility restrictions from the lockdowns. This in turn contributed to a build-up in excess savings²³ (Bank of England, 2021; Batty et al., 2021).

Chart 1: Savings and Demand Deposits of Individuals in Malaysia



Source: Bank Negara Malaysia

The build-up in excess savings is expected to be transitory as the savings accrued during lockdowns are above and beyond the average amount prior to the pandemic period (2013-2019). As the economy recovers and international borders reopen, the need for precautionary savings would lessen and together with the lifting of mobility restrictions, households are expected to draw down on the accumulated excess savings to spend on travel and selected discretionary items. In this regard, the estimation of excess savings can provide some indication on the potential strength of pent-up demand, which in turn is expected to support household spending during the year.

²² Obtained from Bank Negara Malaysia's Credit and Funding Conditions Survey conducted in August 2021. The survey is qualitative, and the data is based on aggregated responses from 16 banks with a market share of 94% of total banking sector liabilities. The question posed to banks in the survey is "Since the onset of the crisis, a significant increase in demand and savings deposit balances of individuals' bank accounts has been observed. From a distributional perspective, how does the increase in deposit balances, from end-2019 to date, differ across income groups?"

²³ Excess savings is generally estimated as the cumulative amount by which household savings during the pandemic exceed the pre-pandemic level or the level that is likely to have prevailed without the pandemic.

There are two methodologies²⁴ that BNM uses in estimating excess savings among households in Malaysia. These methodologies differ in terms of the coverage of the savings instruments based on their liquidity. Based on these methodologies, the stock of excess savings in Malaysia is estimated to be between RM60 to RM80 billion as at end-2021, which is equivalent to about 7% to 10% of consumer spending in 2021²⁵.

The first methodology takes into account the most liquid forms of household savings in Malaysia, namely savings and demand deposits. Excess savings is calculated as the deviation of the actual amount of outstanding savings from the linear trends calculated from the pre-COVID-19 period of 2013 to 2019. This reference period saw a relatively stable level of savings, averaging at about RM200 billion every month. The estimated excess savings is approximately RM82 billion as at end-December 2021.

The second methodology considers a wider range of instruments from which households with excess savings can potentially draw down and spend. Excess savings is calculated as the sum of flows into individual savings and demand deposits, fixed deposits, investments in domestic equity market and unit trust funds, above and beyond the 2013 – 2019 average. Using this method, Malaysia's excess savings is estimated to be about RM57 billion between March 2020 and December 2021.

As economic activity normalises in 2022, spending based on pent-up demand through the release of some of the excess savings will provide additional support to household consumption. It is assumed that households will only spend about 25% of the excess savings accumulated.²⁶ In addition, the pent-up demand is expected to be temporary and will gradually dissipate with the full reopening of the economy. Going forward, the recovery in labour market conditions would provide the main support to household spending, with early signs of recovery already being observed in 4Q 2021.

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²⁴ Adapted from Bank of England (2021) Monetary Policy Report February 2021, Batty, M., Deeken, E., & Volz, A. H. (2021) "Wealth Inequality and COVID-19: Evidence from the Distributional Financial Accounts", FEDS Notes, and Lydon, R. & McIndoe-Calder, T. (2021) "Saving during the pandemic: Waiting out the storm?", Economic Letter Vol. 2021 No. 4, Central Bank of Ireland.

²⁵ The translation from excess savings to consumer spending could be smaller if households choose not to draw down on the savings, but to accumulate them to build wealth.

²⁶ This is a conservative estimate given the rapidly evolving macroeconomic environment, particularly on the developments surrounding COVID-19.

Expansion in all economic sectors

All economic sectors are projected to expand in 2022. The improving growth trajectory will be driven by the recovery in domestic-oriented sectors as almost all economic and social sectors return to normalcy amid Malaysia's high vaccination rate and rapid rollout of booster shots. The re-opening of international borders will facilitate the recovery of tourism-related industries and alleviate pockets of foreign labour shortages in the domestic economy. Meanwhile, export-oriented sectors will continue to benefit from strong external demand and expansion in domestic production capacity.

Table 1

Real GDP by Kind of Economic Activity (2015=100)

	2021p	2021p	2022f	2021p	2022f
	% of GDP	Annual change (%)		Contribution to growth (ppt) ¹	
Services	57.0	1.9	6.9	1.1	3.9
Manufacturing	24.3	9.5	5.2	2.2	1.3
Mining and quarrying	6.7	0.7	2.5	0.0	0.2
Agriculture	7.2	-0.2	1.5	0.0	0.1
Construction	3.7	-5.2	6.1	-0.2	0.2
Real Gross Domestic Product (GDP)	100¹	3.1	5.3 ~ 6.3	3.1	5.3 ~ 6.3

¹ Figures may not necessarily add up due to rounding and exclusion of import duties component

p Preliminary

f Forecast

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

The *services* sector is projected to register a higher growth in 2022, led by the consumer and tourism-related subsectors. The improvement is expected to be supported by lifting of nationwide containment measures and re-opening of international borders for tourism. This would facilitate greater mobility and provide further support for the momentum in consumer spending observed in 4Q 2021, to continue into 2022. However, activities in certain subsectors such as food, beverage and accommodation are likely to remain below pre-pandemic levels, given the expectation of a gradual recovery in tourist arrivals. Business-related services will continue to remain supportive of growth. This will mostly be in the logistics and professional services, in line with the continued expansion of manufacturing and construction activity. The information and communication subsectors are also expected to provide further lift to the *services* sector. This will be driven by demand for data services mainly for e-commerce and e-payment activities.

While growth in the *manufacturing* sector is projected to increase at a more moderate pace, it will still be above the long-term average. Malaysia's E&E cluster, which is highly integrated in global value chains, will benefit from continued demand for E&E products globally. Additionally, E&E growth will be further reinforced by ongoing expansions in domestic production capacity. In the Bank's regional economic surveillance, E&E firms indicated strong order books for the year. The primary-related cluster is also projected to expand. Demand for refined petroleum products is expected increase in line with higher mobility and economic activity, while continued health and hygiene awareness will support demand for rubber and chemical products. Meanwhile, production in the construction-related manufacturing clusters is also expected to grow following the resumption of construction projects and improvement in the residential property market. In addition, growth in the consumer-related manufacturing cluster is projected to improve, in tandem with the recovery in consumption activity. Amid strong external and domestic demand, the increase in production in certain *manufacturing* subsectors such as E&E and chemical products could be affected by pockets of labour shortages and global supply disruptions. Nevertheless, higher adoption of automation and productivity improvements since the onset of COVID-19 pandemic will help to partly offset these factors.

The recovery in the *agriculture* sector will be driven primarily by higher oil palm production. This is premised on expectations for a gradual improvement in labour supply. Heavier rainfall in the early part of the year is also expected to improve soil moisture and increase oil palm yields in the latter part of the year. In addition, the recovery in domestic demand is expected to support the continued strong expansion in livestock and other agriculture subsectors.

The *mining* sector is projected to register higher growth. This reflects the continued increase in crude oil and natural gas production due to the operationalisation of new facilities such as the Pegaga gas project in Block SK320 located in offshore East Malaysia, which commenced operations in March 2022. Growth will also be supported by higher production in existing oil and gas facilities including the PFLNG2 facility and following the completion of several maintenance works. The end of OPEC+ oil output cut agreement by the second half of the year is also expected to result in higher production.

Growth in the *construction* sector is expected to rebound in 2022 following the reopening of the economy. Ongoing construction activity in large infrastructure projects and implementation of small-scale projects under the 2022 Budget measures will support growth in the civil engineering and special trade subsectors. Meanwhile, the residential subsector will benefit from new housing projects and launches, in tandem with the expected recovery in demand as income and employment prospects improve. Growth in the non-residential subsector is expected to be lifted by both existing and new commercial and industrial projects.

Potential Output and the Output Gap of the Malaysian Economy

Potential output is the highest non-inflationary level of output that can be produced in an economy. It indicates the economy's sustainable growth path, based on its prevailing factors of production (i.e. labour and capital) and productivity.

In 2021, potential output continued to expand at a moderate pace of 2.3% (2020: 1.6%, 2011-2019 average: 4.9%). The expansion was attributable to a marginal improvement in labour force participation (2021p: 68.6%; 2020: 68.4%), and in total factor productivity (TFP). This more than offset slower capital accumulation amidst a continued decline in investment activity (2021: -0.9% 2020: -14.5%).

The faster growth in actual output in 2021 (3.1%; 2020: -5.6%) led to a narrowing of negative output gap to -6.0% (2020: -6.8%). However, the negative output gap remained sizable²⁷. This reflects the economic slack arising from the underutilisation of factors of production given the moderate recovery in actual output. The negative output gap has contributed to moderate demand-driven price pressures, as indicated by low core inflation of 0.7% in 2021 (2020: 1.1%). The increase in headline inflation to 2.5% (2020: -1.2%) was mostly accounted for by base effects²⁸ and cost factors such as elevated commodity prices.

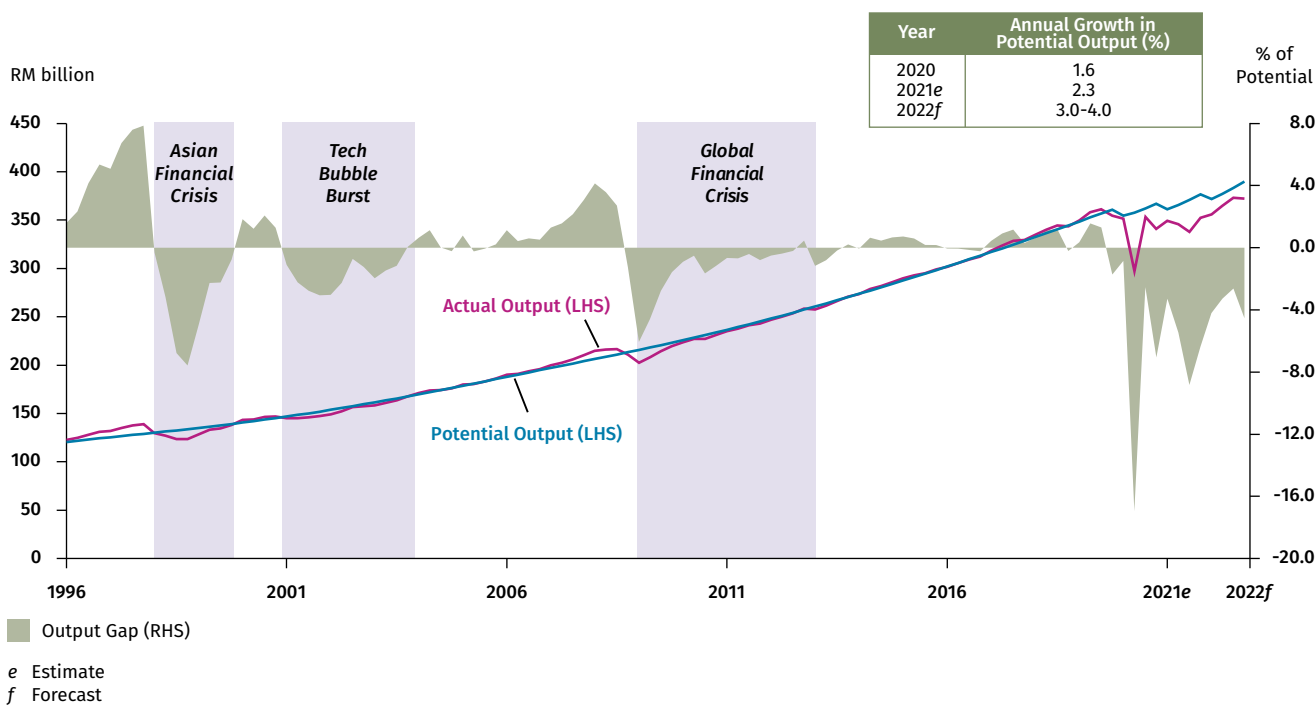
Going forward, the negative output gap is expected to narrow further in 2022, as actual output growth of 5.3%-6.3% is projected to outpace potential output growth of 3.0%-4.0%. Potential output growth will be supported mainly by a recovery in capital expenditure and labour force expansion²⁹. Over the medium term, potential output growth is projected to revert to the pre-crisis rate of 4.0-5.0%, as economic activity continues to recover. This will also be supported by the continued progress in automation, digitalisation, and implementation of digital infrastructure projects, which can enhance productivity and technology levels.

²⁷ The output gap is formally defined as $\frac{\text{Actual output level} - \text{Potential output level}}{\text{Potential output level}} \times 100\%$

²⁸ In the second quarter of 2021, fuel inflation surged higher due to base effects following the exceptionally low global oil prices in 2020 (2Q 2021 average domestic fuel (RON95) price: RM2.05/litre; 2Q 2020: RM1.37/litre). For more details, please refer to Chapter 1 Inflation Developments.

²⁹ Workers are expected to re-enter the labour market following the full lifting of containment measures and normalisation of economic activity.

Chart 1: Actual and Potential Output



Source: Department of Statistics, Malaysia and Bank Negara Malaysia estimates

Continued export growth in 2022

Malaysia’s exports are expected to grow by 10.9% in 2022 (2021: 26.0%). This is driven by continued external demand, especially from Malaysia’s key trade partners. As one of the world’s largest exporters of electrical and electronics (E&E)³⁰, Malaysia will continue to benefit from the strong global demand for E&E products amid the drive for digitalisation and automation. Improvement in commodity production and higher prices of crude oil, LNG and CPO will provide further impetus to Malaysia’s exports.

Manufactured exports are projected to expand by 5.3% in 2022 (2021: 25.6%), supported by a broad-based expansion across all segments. In particular, Malaysia is expected to continue benefitting from strong semiconductor demand in line with the global sales forecast.³¹ This is corroborated by insights from the Bank’s regional economic surveillance which suggest healthy order books for E&E firms for 2022.

Commodities exports are projected to remain robust (45.8%; 2021: 29.0%), driven by both higher commodity prices and production in 2022. Exports of agriculture products will be supported mainly by the CPO exports amid the higher prices and expected gradual easing of labour shortage. Meanwhile, minerals export growth is expected to be underpinned by higher prices and production amid the commencement of new gas fields and the end of OPEC+ output cuts in the latter part of 2022.

³⁰ Malaysia is the twelfth largest E&E exporter based on IHS Markit for 2021 trade data.

³¹ In March 2022, World Semiconductor Trade Statistics (WSTS) projected a growth of 10.4% for global semiconductor sales in 2022 (2011-2019 average: 4.1%).

Import growth supported by continued expansion of manufactured exports and improvement in domestic demand

Gross imports are projected to expand by 8.1% in 2022 (2021: 23.3%), driven by higher intermediate imports in line with continued growth in manufactured exports. Capital imports are expected to register a continued expansion driven by the recovery in investment activity. Consumption imports will be supported by the improvement in consumer spending amid better income and employment conditions.

Table 1

External Trade

	2015-2019 average	2021 ^p	2022 ^f
	Annual change (%)		
Gross exports	5.6	26.0	10.9
<i>of which:</i>			
Manufactured	7.6	25.6	5.3
Agriculture	-0.6	36.8	49.6
Minerals	-3.1	19.5	40.5
Gross imports	4.7	23.3	8.1
<i>of which:</i>			
Capital goods	1.2	14.5	5.3
Intermediate goods	3.1	26.9	8.3
Consumption goods	8.4	13.2	14.0
Trade balance (RM billion)	109.5	252.6	307.5

^p Preliminary

^f Forecast

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

Current account to remain in surplus

The current account of the balance of payments is expected to register a higher surplus in 2022 at 4.2 – 4.7% of GDP (2021: 3.5% of GDP). This will be driven by the goods surplus amid continued strength in external demand and higher commodity prices.

The services account is projected to remain in deficit, weighed mainly by transportation services amid continued strength in trade activity. The travel deficit is expected to narrow slightly, supported by the higher travel receipts amid the reopening of international borders to inbound tourists. Nevertheless, the pace of international travel recovery is expected to be gradual and remain below (around 20% of) pre-pandemic levels, given the risk aversion and international travel restrictions that still remain in some places.

The primary income account is projected to record a wider deficit, attributable mainly to the higher income payments accrued to foreign investors in Malaysia amid the improvement in the domestic growth outlook. The secondary income account is expected to register a larger deficit driven by the higher foreign worker outward remittances.

Table 2

Current Account of the Balance of Payments¹

Item (Net)	2021p	2022f
	RM billion	
Goods	170.2	227.9
Services	-61.1	-62.3
Primary income	-46.2	-69.2
Secondary income	-9.5	-20.7
Current account balance	53.5	75.8
% of GDP	3.5	4.2 ~ 4.7

¹ In accordance with the Balance of Payments and International Investment Position Manual, Sixth Edition (BPM6) by the International Monetary Fund (IMF)

p Preliminary
f Forecast

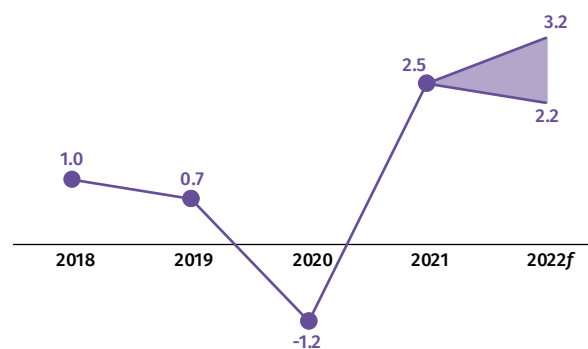
Note: Figures may not necessarily add up due to rounding.

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

Headline inflation to average between 2.2% and 3.2% in 2022 amid higher underlying inflation

In 2022, headline inflation is forecasted to remain manageable, averaging between 2.2% and 3.2% (2021: 2.5%) (Chart 2.5). Fuel inflation, which underpinned the higher headline inflation in 2021,³² is projected to moderate in 2022. This is despite expectations of higher global oil prices, given the assumption that the price ceiling on domestic retail fuel prices would remain in place throughout the year. High input costs from rising non-energy commodity prices, however, are expected to exert some pressures on selected fresh food prices, particularly in the first half of the year. Nevertheless, this will continue to be partly mitigated by the price controls on selected food items. Of note, for the second half of 2022, the base effect from electricity prices is projected to contribute to a temporary spike in headline inflation, particularly in the third quarter of 2022.³³

Chart 2.5: Malaysia's Headline Inflation, Annual Change (%)



f Forecast

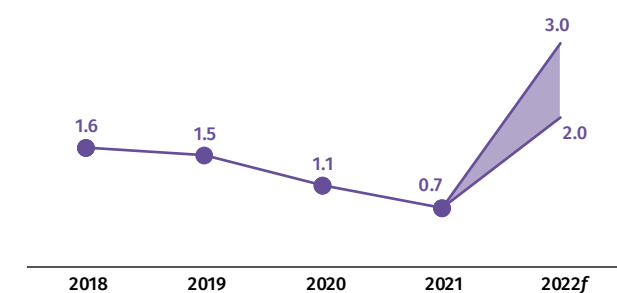
Source: Department of Statistics, Malaysia and Bank Negara Malaysia estimates

³² In 2021, fuel inflation surged higher due to base effects following the exceptionally low global oil prices in 2020 (2021 average domestic retail fuel (RON95) price: RM2.03/litre; 2020: RM1.67/litre).

³³ Electricity price inflation is expected to experience a temporary spike in the third quarter of 2022 on a year-on-year basis, reflecting the lower electricity prices in the third quarter of 2021 due to the three-month electricity bill discounts implemented from July to September 2021.

Meanwhile, underlying inflation, as measured by core inflation, is expected to average higher between 2.0% and 3.0% in 2022 (2021: 0.7%) (Chart 2.6), driven by the improvement in demand conditions amid lingering cost pressures.³⁴ For most items in the core Consumer Price Index (CPI) basket, the price pressures in 2022 largely reflect a normalisation after a period of subdued demand and reduced profit margins during the pandemic. However, prices for some CPI segments, such as *food away from home* and some high-touch services³⁵, are projected to exceed their pre-pandemic trend due to the confluence of stronger demand and the high cost environment. Nevertheless, the extent of upward adjustments to core inflation will remain partly contained by the continued slack in the economy and labour market.

Chart 2.6: Malaysia's Core Inflation, Annual Change (%)



f Forecast

Note: Core inflation is computed by excluding price-volatile and price-administered items. It also excludes the estimated direct impact of consumption tax policy changes

Source: Department of Statistics, Malaysia and Bank Negara Malaysia estimates

The overall inflation outlook, however, remains susceptible to upside risks, particularly from cost-push factors. These include a more persistent uptrend in input costs due to higher global commodity prices and prolonged disruptions to global supply chains, which could be exacerbated by geopolitical tensions and lockdowns in China. Higher input costs could also induce a larger

pass-through of costs to consumer prices, should businesses expect them to be more permanent in nature. Moreover, there is the risk that excessively high global energy prices could lead to adjustments to domestic retail fuel prices that have remained unchanged since March 2021.³⁶ On the downside, risks mainly reflect factors which could precipitate a weaker recovery in economic conditions, leading to more benign price pressures. These include larger slack in the domestic economy due to weaker-than-expected demand conditions and labour market recovery, as well as external risks which could derail Malaysia's growth and trade outlook, such as the emergence of severe and vaccine-resistant VOCs.

Domestic monetary and financial conditions to remain conducive to financial intermediation activities

Domestic monetary and financial conditions are expected to remain supportive of financial intermediation activities, and further catalyse the economic recovery in 2022 amid accommodative monetary policy. Financing activity in the economy will also continue to be underpinned by the sound banking system and well-functioning capital markets.

The lending capacity of Malaysian banks remains intact, given their healthy capital and liquidity buffers. As the economy recovers, banks' willingness to lend is likely to increase amid lower risk aversion and improvement in borrowers' debt servicing ability. Coupled with higher demand for financing by households and businesses to fund consumption and investment activities, credit flows to the private sector are expected to pick up during the year. This is in line with banks targeting a higher outstanding loan growth in 2022.³⁷ Government and BNM measures, including the targeted repayment assistance and financial management programmes,³⁸ as well as special funds for SMEs, would also provide support

³⁶ Refers to domestic retail fuel prices for RON95 and diesel, which have been fixed at the ceiling price of RM2.05/litre and RM2.15/litre, respectively, since March 2021.

³⁷ Banks' loan growth target in 2022 is 5.4% to 6.4% (2021 actual outstanding loan growth: 4.5%). This is based on the weighted responses of 20 banks, representing 96% of total outstanding banking system loans. Source: 4Q 2021 Credit and Funding Conditions Survey to banks.

³⁸ Under the Financial Management and Resilience Programme (URUS), borrowers will receive a personalised financial plan that sets out the monthly debt repayment amount scheduled for a period of up to 24 months. It includes an interest waiver for three months; or deferred payments/reduced instalments. There would also be financial advisory support and education throughout the programme.

³⁴ Cost pressures from elevated global commodity prices and supply-related disruptions are expected to be passed on to consumers to a greater degree as demand conditions improve, as firms recoup compressed margins from the persistently higher costs since 2021.

³⁵ Including restaurants and hotels, and recreational services. Please refer to the box article on 'An Anatomy of Inflation: Effects from the Prolonged Pandemic' for more details.

for financial intermediation, particularly for vulnerable segments in the economy.

As a highly open economy with substantial linkages to global financial markets, Malaysia is not insulated from the heightened uncertainty and risks emanating from external developments. These include monetary policy normalisation globally and escalating geopolitical tensions. In particular, tighter monetary policies in advanced economies are expected to raise the costs of foreign currency financing globally, increase risks of capital outflows, and result in bouts of volatility in the financial markets. With the large shifts in global liquidity, swings in international investor risk appetites could lead to portfolio rebalancing, which in turn, would affect domestic asset prices, balance sheet valuations, and liquidity in the domestic financial system. In addition, adjustments in global bond yields could spill over to domestic bond yields, leading to higher financing costs.

Nonetheless, as evident in past episodes of capital outflows and heightened volatility, spillovers to domestic financial conditions are expected to be broadly contained. Continuous efforts to strengthen external buffers and economic fundamentals over the years have improved the resilience of the Malaysian economy and financial system against external shocks. Factors supporting this resilience include the continued current account surplus, a healthy external position, and an adequate level of international reserves. Moreover, the presence of domestic institutional investors, as well as deep and liquid financial markets, will facilitate an orderly intermediation of portfolio flows, thus dampening the impact of external financial shocks. The impact from exchange rate fluctuations on domestic financing conditions is mitigated by low reliance on foreign currency financing and availability of hedging facilities for corporates and investors to manage foreign currency exposures. This resilience is vital in ensuring that episodes of capital outflows do not lead to excessive tightening of domestic monetary and financial conditions. Importantly, the flexibility of the exchange rate would also remain as a key shock absorber to facilitate necessary macroeconomic adjustments from external shocks.

Meanwhile, the Bank's monetary policy operations will continue to provide an accommodative monetary environment by ensuring sufficient

domestic liquidity in the financial system to support financial intermediation and orderly functioning of the financial markets. This includes the flexibility provided to banking institutions to comply with the SRR³⁹ which remains in place until end of the year.

Monetary policy will continue to facilitate a sustainable economic recovery while preserving price stability

Monetary policy in 2022 will continue to support a sustainable economic recovery while preserving price stability. The MPC considers the current stance of monetary policy to be appropriate and accommodative, given the prevailing outlook on growth and inflation for 2022. Going forward, the MPC will focus on ensuring that the degree of monetary accommodativeness is consistent with the expected improvement in economic conditions amid moderate upward price pressures and well-anchored inflation expectations.

Against a background of rapidly evolving conditions and heightened uncertainties, especially in the global environment, the MPC will continue to monitor the outlook for growth and inflation, and the possibility of materialisation of risks. On growth, the downside risks include developments surrounding COVID-19, a weaker-than-expected global growth, ongoing geopolitical conflicts, and a worsening of supply chain disruptions. Considerations for continued monetary policy support would need to be balanced against maintaining low interest rates for a prolonged period, which could lead to an emergence of financial imbalances through excessive risk-taking behaviour and unhealthy build-up in leverage.

The MPC is also mindful of the potential upside risks to inflation, which continue to be subject to global commodity price developments amid risks from ongoing geopolitical conflicts and prolonged supply-related disruptions. While monetary policy may not be the best tool to react to these "first-round" effects, the MPC will assess whether such price pressures could become more persistent and pervasive, and whether they would be reinforced by stronger domestic demand.

³⁹ Banking institutions are provided the flexibility to utilise MGS and MGII to meet the SRR compliance. This flexibility has been extended to 31 December 2022 from 31 May 2021 previously.

To this end, future monetary policy decisions will continue to be data-driven and guided by the evolving balance of risks surrounding the outlook for domestic inflation and growth. Any potential adjustments to the degree of monetary accommodativeness would be made in a measured and gradual manner. Given the lingering uncertainties and downside risks to growth, monetary policy will remain accommodative, while preserving price and financial stability.

Fiscal policy has played a pivotal role in providing the necessary countercyclical support and remains crucial in providing long-term support to economic development. The measures outlined in the 2022 Budget remain supportive of the economic recovery, and also serve to limit the long-term economic scarring effects from the pandemic. Going forward, the Government is embarking on fiscal reform initiatives to rebuild fiscal buffers and ensure fiscal sustainability. Examples of initiatives include the Fiscal Responsibility Act and the Medium-Term Revenue Strategy.

The recovery period presents a key opportunity to institute structural reforms to ensure a sustainable and inclusive growth going forward. While measures to limit the extent of scarring from the pandemic remain in place, the recovery provides a timely opportunity to prioritise certain structural reforms. The shift towards higher quality investments is essential and must be done in tandem with the development of a future-ready workforce, as well

as an accelerated adoption of automation and digitalisation. The continued push to adopt the Environmental, Social and Governance (ESG) agenda is also critical, particularly to ensure Malaysia remains globally competitive, whilst building a more sustainable and resilient future.

To this end, Malaysia has made important progress in enhancing measures to promote high quality investments, as well as advancing sustainability and digitalisation initiatives. In particular, the adoption of National Investment Aspirations (NIA)⁴⁰ into national strategies and the ongoing policy reforms under the New Investment Policy would accelerate the realisation of quality investments in the future. The Twelfth Malaysia Plan (12MP) has laid out further strategies to enhance the education and training ecosystem, intensify digitalisation and accelerate transition to the circular economy. Similarly, the Financial Sector Blueprint 2022-2026 has identified five priorities that would anchor the Bank's efforts to promote a financial system that would support long-term growth, planetary health and shared prosperity. Nevertheless, effective and coordinated execution of all these measures is crucial to ensure the desired outcomes are achieved.

Going into 2022, the overall focus of policies should shift towards long-term objectives of enhancing economic dynamism and increase potential, while balancing the need for short-term relief arising from evolving COVID-19 developments.

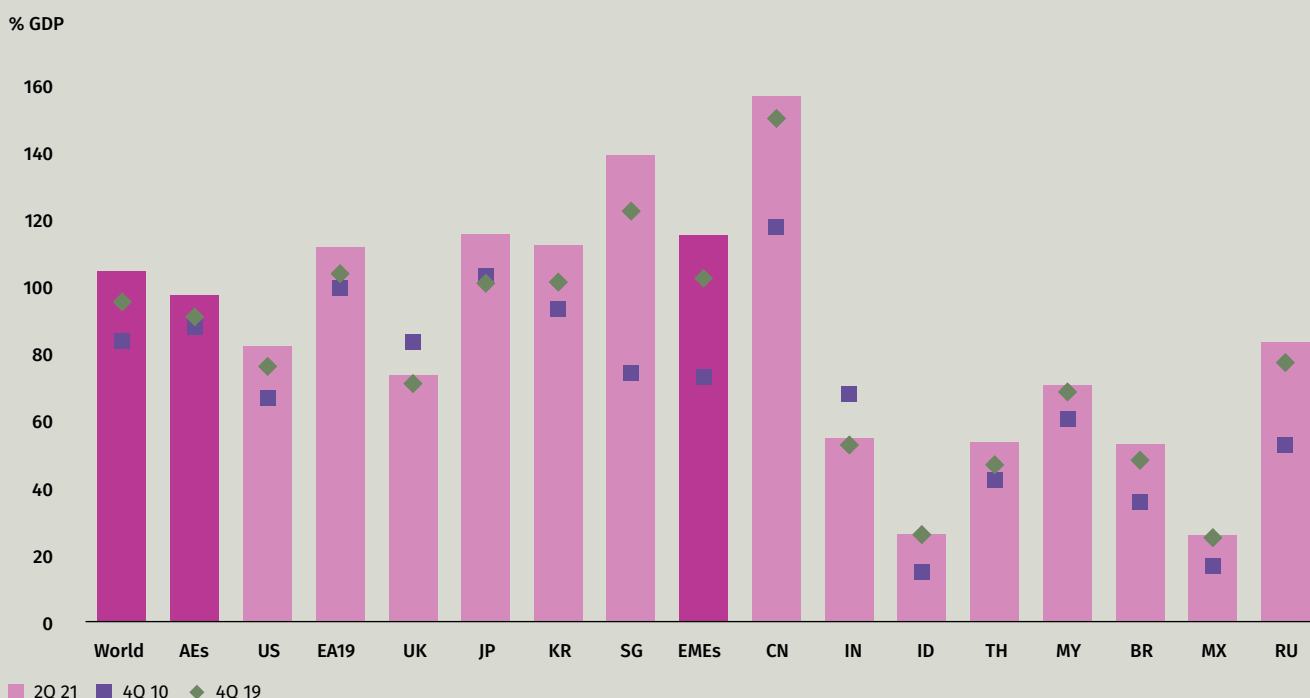
⁴⁰ NIA outlines the key criteria for quality investments, which will be used as basis for comprehensive reforms of Malaysia's investment policies. In particular, it focuses on attracting investments that will increase economic complexity, create high-skilled jobs, expand and integrate domestic linkages, develop new and existing clusters, and improve inclusivity. For more information, please refer to the box article titled 'Securing Future Growth through Quality Investments' in the BNM Economic and Monetary Review 2019 and MITI's website (<https://www.miti.gov.my/NIA/>).

Recovery Prospects in the Global Economy: Lessons from a Corporate Balance Sheet Perspective

Introduction

Since the COVID-19 pandemic, lockdowns have been one of the policy responses to manage healthcare risks globally. This was especially the case during the early phases of the pandemic. The resultant supply shock, together with the weak demand conditions, meant firms have had to operate amidst highly uncertain conditions and were often unable to generate revenue. For firms that were adversely affected, debt financing helped to tide over periods when revenue and cash flow were affected (Chart 1). Aggressive monetary accommodation and the large fiscal support provided additional support to firms. However, as the pandemic moves past an acute phase, policymakers need to strike a balance between assisting firms that would be viable under less extreme circumstances, while not stifling corporate dynamism vital to future economic growth by protecting non-viable ones, or zombies (Banerjee and Hofmann, 2020). The presence of zombies has been linked with the economic stagnation in Japan during the 1990s and euro area post-Global Financial Crisis (GFC) (Acharya et. al., 2021a; Banerjee and Hofmann, 2020; Hoshi and Kashyap, 2015). This article will cover three main issues, drawing from existing literature. Firstly, it delves into the implications of high corporate debt. Secondly, it looks at Japan and the euro area’s crisis experiences to glean some potential lessons in avoiding a slow and prolonged economic recovery. Thirdly, it concludes with important policy imperatives to secure a sustainable recovery path from the pandemic.

Chart 1: Corporate Debt in Selected Economies



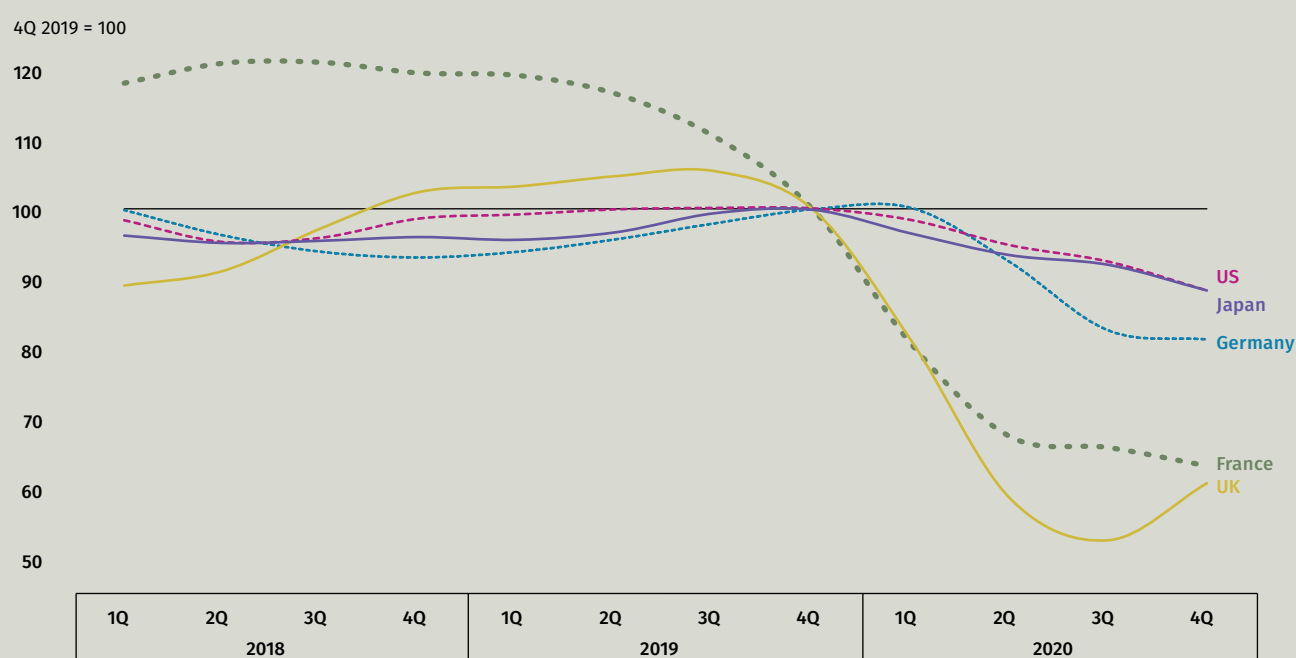
Note: Debt refers to loans and debt securities of non-financial corporates.

Source: Bank for International Settlements (BIS) Credit Database

Why is High Corporate Debt a Concern?¹

Corporate debt globally was already at an elevated level at the onset of the pandemic (Roulet, 2020). Hence, the large supply and demand shocks over the past two years increased concerns that corporate bankruptcy would surge, especially if economic recovery was not forthcoming. However, such large-scale bankruptcies have yet to materialise (Chart 2). This risk was mitigated by significant economic and financial support from governments and central banks, which ensured favourable financing conditions and a recovery in demand conditions (OECD, 2021b). Nevertheless, the high level of corporate debt remains a concern during the current phase of economic recovery.

Chart 2: Corporate Bankruptcies in Selected Economies



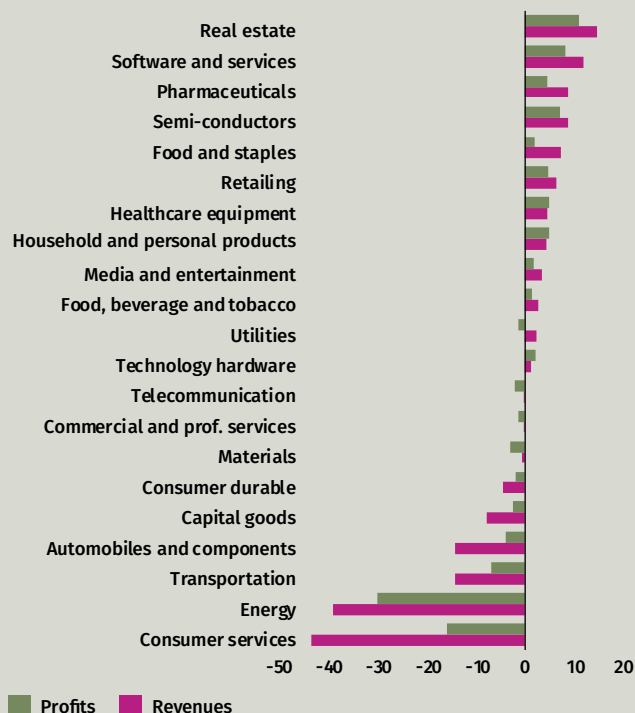
Source: OECD Timely Indicators of Entrepreneurship

Firstly, highly indebted firms tend to reduce investments after economic crises (Kalemli-Özcan et. al., 2019; Barbiero et. al., 2020). This is because they focus on paring down debt instead of investing in new capacity and innovation. However, this has not materialised during the pandemic. Instead, the rise in debt was matched by an increase in short-term and fixed investments (OECD, 2021b). The US is a case in point; investments in equipment and intellectual property recovered strongly in 2021, while structures² investments remained weak. This likely owes to higher demand for specific goods and services during the pandemic (Charts 3 and 4), such as communication and digital services and equipment. The recovery in investment was also facilitated by looser monetary policy. In contrast, investments in adversely affected sectors, such as energy, primary-related products (materials) and transportation (industrials), declined. This reflects the pandemic's disproportionate adverse impact in high-touch and travel-dependent services industries. Firm shutdowns and the general decline in movement also reduced demand for energy and fuel, which affected utilities and energy industries.

¹ High corporate debt is also influenced by corporate tax regimes. Interest expenses are deductible from taxable profits. Hence, higher corporate tax rates could incentivise firms, including healthy ones, to accumulate more debt (Graham, 2006; Feld et. al., 2013). However, risks from high corporate taxes are beyond the scope of this article.

² Structures refer to physical capital that are constructed at the location where they will be used and typically have long economic lives such as offices and warehouses (Bureau of Economic Analysis, 2018).

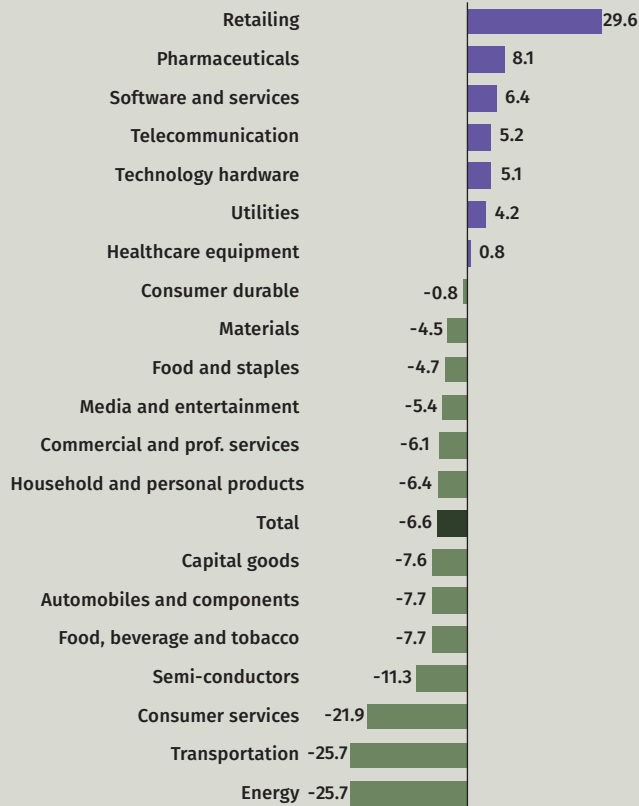
Chart 3: Changes in Revenues and Profits between FY2019 and FY2020 by Industry (%)



Notes: This chart was published in the OECD Economic Outlook (Volume 2021 Issue 1). Profits are measured using earnings before interest, taxes, depreciation, and amortisation (EBITDA). Results are reported for the median firm for each indicator and weighted by the firm's asset size in 2019. The analysis is based on firm-level data provided by S&P Capital IQ. The sample covers 55,000 public and private non-financial companies operating in OECD countries and major (non-OECD) emerging market economies (EMEs), and for which FY 2020 accounts are available. The firms covered are relatively large and collectively represent USD25 trillion of corporate debt. The median firm in the sample had USD30 million in revenues in 2019 and USD35 million in assets. 10% of firms are in EMEs.

Source: S&P Capital IQ and OECD calculations, as cited in OECD (2021a)

Chart 4: Change in Capital Expenditures by Industry (%)



Notes: This chart was published in the OECD Economic Outlook (Volume 2021 Issue 1). Bars show the change in aggregate capital expenditures for each industry. The sample of firms is the same as in Chart 3. According to the OECD (2021a), the investment increase in the retail industry is almost entirely due to the "internet and direct marketing retail" sector, and Amazon in particular.

Source: S&P Capital IQ and OECD calculations, as cited in OECD (2021a)

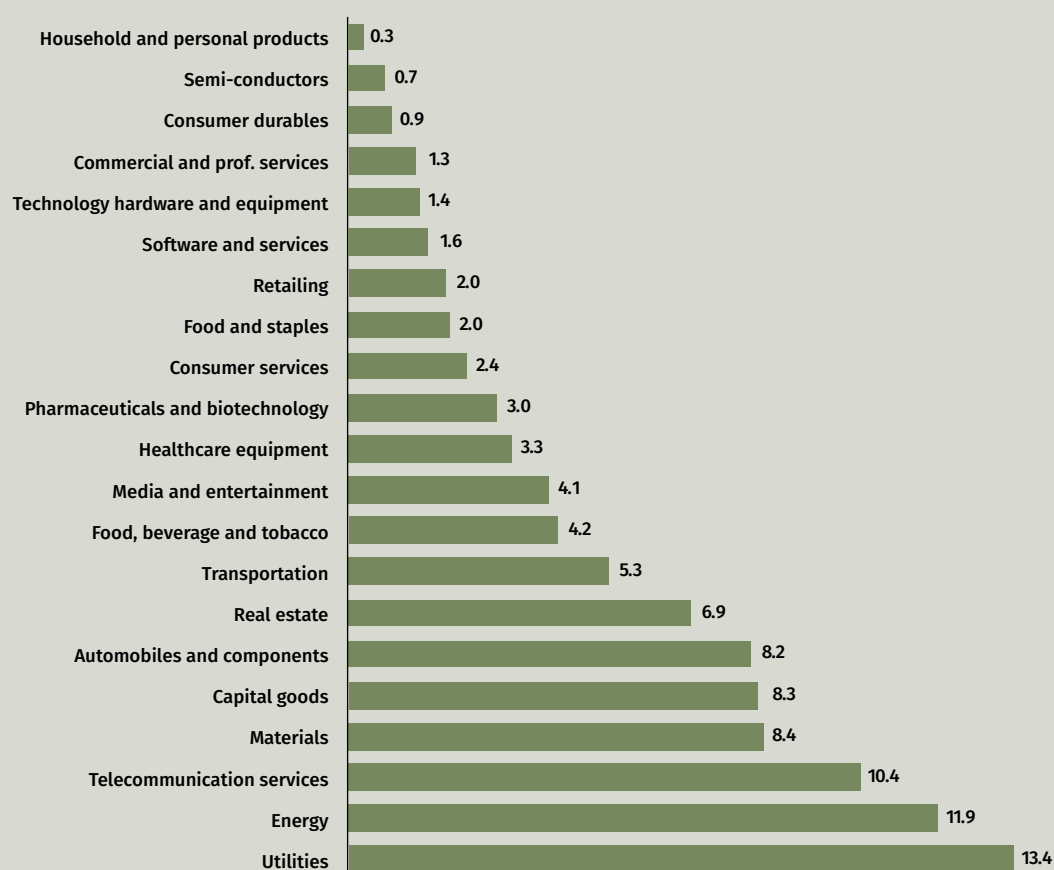
The second source of concern associated with high corporate debt is the declining credit quality of debt. Roulet (2020) found that the share of low credit-quality debt has been increasing between 2004 and 2019, particularly in the US and emerging market economies (EMEs), excluding China.³ The OECD (2021a) estimated that roughly 30%⁴ of non-financial corporate bonds globally was rated 'speculative'⁵ and hence, deemed 'risky'. The profile of 'risky' debt among corporate borrowers varies by sector, affecting mainly the energy and utilities sectors (Chart 5). It is important to note that these findings cover mainly large public listed firms. Financial information remains limited for small and medium enterprises (SMEs), who have been disproportionately affected by the pandemic (Chetty et. al., 2020) and account for a large share of debt in high-touch services industries. With interest rates expected to rise, solvency risk remains a concern. This is particularly so if the recovery in the most adversely affected sectors is slow and protracted. This could trigger rating downgrades (for medium and large firms) and defaults amid rising funding costs.

³ Roulet (2020) used data for 4,670 firms in advanced economies (AEs) and 3,691 firms in emerging market economies (EMEs). The findings highlighted large declines in credit quality of US firms since 2015. The level of debt of risky firms was similar to 2007, before the onset of the GFC. Other EMEs, particularly Latin America, Eastern Europe, the Middle East, and Africa, had the highest levels of risky debt on record. The declining trend in corporate debt quality was more moderate in Advanced Europe, Japan, and China.

⁴ The data covered 2,800 public and private non-financial corporates operating in OECD countries and major (non-OECD) EMEs with an active S&P issuer rating.

⁵ 'Speculative' indicates high level of credit risk or a default has already occurred.

Chart 5: 'Risky' Debt by Sub-sectors (% share)



Notes: This chart was published in the OECD Economic Outlook (Volume 2021 Issue 1). OECD calculated 'risky' debt as the total debt in firms rated speculative⁶ or BBB⁷ for 2019. The data covered a subset of a sample of 2,800 public and private non-financial corporates operating in OECD countries and major (non-OECD) EMEs with an active S&P issuer rating. The sample mainly covers large public listed firms incorporated in AEs, but also includes private firms (30%) and/or firms in EMEs (13%).

Source: S&P Capital IQ and OECD calculations, as cited in OECD (2021a)

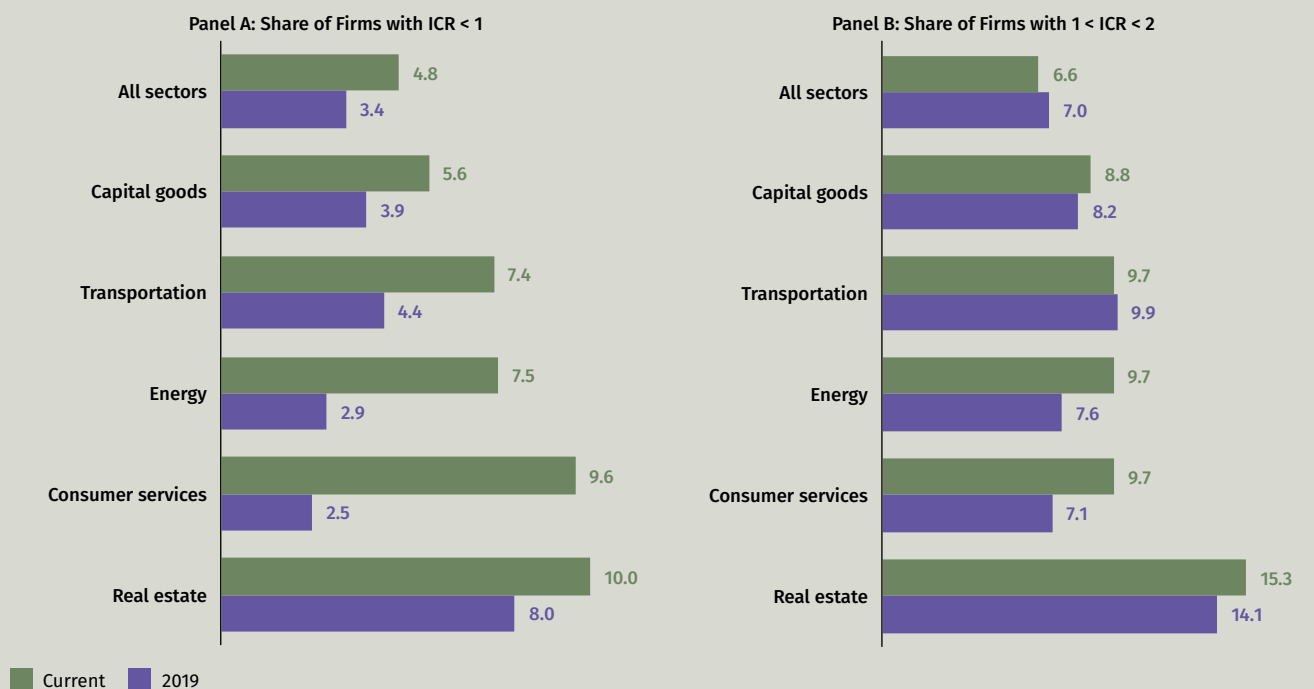
Thirdly, high corporate debt coupled with lower productivity could be symptomatic of rising zombification (Caballero et. al., 2008). Zombies can be defined as firms with insufficient revenue to cover loan interest costs (Chart 6) and are dependent on cheap credit to survive⁸ (Acharya et. al., 2020). Unhealthy banks are more likely to be funding zombies, as their weak balance sheets constrain their ability to absorb losses from zombies' defaults, if they do occur (Andrews and Petroulakis, 2017). This in turn incentivises banks to delay the recognition of losses by rolling over debt. Based on a sample of 14 advanced economies, the share of zombie firms has increased from slightly above 4% in the mid-1980s to 15% in 2017 (Banerjee and Hoffman, 2020). The same study estimated that a quarter of zombies tended to exit the industries, while 60% graduated from zombie status over time (mid-1980s to 2017). However, recovered zombies normally underperform compared to non-zombies and are more likely to fall back into zombie status. This is because weaker profitability among zombies makes them less able to weather economic downturns, compared to non-zombies. More recent research indicates that the number of zombie firms remained contained in France (Cros et. al., 2021) and the US (Favara et. al., 2021) for 2020. This is likely due to the large magnitude of fiscal support during this period. Nonetheless, the generous financial support, in the form of low interest rates and repayment assistances, has led to concerns on rising zombification, as the pandemic prolongs (Acharya et. al., 2020).

⁶ 'Speculative' indicates high level of credit risk or a default has already occurred.

⁷ Despite OECD's definition, it is acknowledged that BBB firms may not be commonly classified as 'risky', since it is technically still within the 'Investment' grade. 'Investment' grade indicates low to moderate credit risk.

⁸ Most studies linked zombies with funding by banks. However, zombies can also be funded via equity issuances (Banerjee and Hoffman, 2020). Denis and McKeon (2020) found that US firms with negative net cash flows often used equity financing, via private placements due to the lower fixed issuance costs, to cover current and subsequent cash flow shortages. Lu et. al. (2020) argued that Chinese zombie firms were often supported by the equity market and informal financing, mainly via trade credits.

Chart 6: Share of Larger Firms based on Interest Coverage Ratio (ICR)



Notes: This chart was published in the OECD Economic Outlook (Volume 2021 Issue 2). The OECD analysed 28,000 firms in the S&P database where ICR, the ratio between earnings before interest, taxes, depreciation, and amortisation (EBITDA) and total interest expenses for 2020 or 2021, are available (current ICR). The sample covered medium and large public and private non-financial companies operating in OECD countries and major non-OECD EMEs. ICR below 1 suggests profits are insufficient to pay interest expenses.

Source: S&P Capital IQ and OECD calculations, as cited in OECD (2021b)

The presence of zombies could have negative implications to growth and inflation, directly and indirectly (by affecting non-zombie firms). Firstly, zombies tend to be smaller, less productive and invest less (Banerjee and Hofmann, 2020). A 1 percentage point (ppt) rise in the share of zombies corresponds to a 0.1 ppt drop in productivity⁹ growth for the economy.¹⁰ Secondly, the presence of zombies creates excess production capacity, exerting downward pressure on prices (Acharya et. al., 2020). The subsidised credit allows zombies to continue producing despite being less viable. As a result, supply cannot adjust to a drop in demand during crisis, artificially suppressing inflation. For instance, inflation in Europe is estimated to be 0.4 ppt higher between 2012 and 2016, if funding to zombies had not risen. Thirdly, zombies crowd out growth among non-zombie firms by distorting competition in the economy (Caballero et. al., 2008; Banerjee and Hofmann, 2020). Besides depressing prices for their products, zombies also inflate wages by retaining unproductive workers. This has a spillover impact on non-zombies, as the artificially low prices could compress margins of healthy firms, subsequently hampering investments and new entries of non-zombies. A 1 ppt increase in the share of zombies corresponds to a 0.5 ppt drop in investments by non-zombies.¹¹ The crowding out effect also occurs through misallocation of resources (e.g., credit and government assistance) to zombies. The presence of zombies impedes the flow of resources to more productive firms, affecting the growth and survival of non-zombies. In short, zombies have a long-term impact on the economy as they are not only less productive, but they hinder growth of healthy firms.

⁹ Proxied by Total Factor Productivity (TFP)

¹⁰ Calculated based on firm-level data from 14 countries - Australia, Belgium, Canada, Switzerland, Germany, Denmark, Spain, France, UK, Italy, Japan, Netherlands, Sweden, and the US (Banerjee and Hoffman, 2020).

¹¹ Calculated based on firm-level data from 14 countries - Australia, Belgium, Canada, Switzerland, Germany, Denmark, Spain, France, UK, Italy, Japan, Netherlands, Sweden, and the US (Banerjee and Hoffman, 2020).

Lessons from Past Crises

In this section, we draw lessons from past crises in avoiding slow and protracted recoveries. We look at episodes in Japan and the euro area – the Japanese asset bubble burst (1989 to 1992) and banking crisis (1997), and the 2008 GFC and sovereign debt crisis in the euro area (2010 to 2012). These crises are different compared to the pandemic, but the concern on rising zombification provides common ground. Zombie lending, compounded by the slow recapitalisation of banks, was found to be a key reason behind the economic stagnation in Japan and euro area (Hoshi and Kashyap, 2015). Insufficient policy responses and lack of structural reforms also contributed to the prolonged stagnation. This indirectly leads to the creation of more zombies, which tend to emerge during periods of downturns (Banerjee and Hoffman, 2020). A potential explanation is the two-fold impact of downturns – lower revenue hurts firms’ ability to service debt, while the increased reliance on debt¹² may come at the expense of future productivity¹³.

(i) Delayed and Insufficient Policy Responses

During the GFC, monetary policy was eased in Japan, US, and euro area. However, differences in the speed and magnitude of the easing could explain the varying impacts on growth and inflation across the three countries (Hoshi and Kashyap, 2015). In particular, the US acted relatively quicker. The Federal Open Market Committee (FOMC) reduced policy rates to zero and deployed unconventional monetary policy tools, namely quantitative easing and forward guidance. As a result, it saw a relatively fast recovery and averted deflation. In contrast, euro area and Japan experienced a delayed recovery and deflation or low inflation. Concerns over the commodity price-wage spiral at the onset of the GFC in the euro area (Kang, Ligthart, and Mody, 2016; Hetzel, 2016) and the already low interest rate in Japan (Shirakawa, 2008) were among factors that could have explained differences in the speed and effects of policy responses compared to the US.¹⁴ The experience in these economies underscores a broader policy dilemma. Low interest rates mitigate short-term impact of crises and thereby contain the rise of zombies, which tend to emerge during downturns. However, keeping rates too low for too long prolongs the life of zombies. This could hurt long-term productivity, stagnating economic growth.

Fiscal support in Japan following the early 1990s asset price declines was also insufficient to cushion the initial downturn (Hoshi and Kashyap, 2015; Posen, 1988). According to Posen (1998), only one-third of the originally announced fiscal measures were implemented. Only in 1995 did the government introduce a larger fiscal package, which led to an outperformance in growth (Hoshi and Kashyap, 2015). However, the withdrawal of these measures just before the Asian Financial Crisis led Japan back into recession by late 1997. Moreover, Japan was facing diminishing return for its public investments by the early 1990s, limiting the impact of its fiscal spending (Doi and Ihuri, 2009).¹⁵ Meanwhile, lack of fiscal support in euro area during the GFC stemmed from limited fiscal space (Hoshi and Kashyap, 2015; Lachman, 2012). In addition, the lack of a fiscal union prevented more uniform support across different Member States. This in turn adversely affected banks’ ability to raise capital via private funding, which is discussed further below. This was in contrast to the US, which introduced of the Troubled Asset Relief Programme (TARP) to stabilise its financial system.¹⁶

¹² Firms borrowing to sustain operations during downturns.

¹³ As explained in the previous section, highly indebted firms tend to reduce investments after economic crises (Kalemli-Özcan et. al., 2019; Barbiero et. al., 2020). To repair their balance sheets, firms focus on paring down debt instead of re-investing in new capacity and innovation initiatives.

¹⁴ Prior to the GFC, Japan was in a position where the low interest rate was ineffective in stimulating economic activity (i.e. liquidity trap) (Akram, 2016). In this environment, other policy tools, such as fiscal, had to be relied on to restore demand (Akram, 2016). There were also concerns that further rate cuts approaching zero would create market distortions, by sustaining low quality borrowers, including zombies (Hoshi, 2013; Acharya et. al., 2021a).

¹⁵ Doi and Ihuri (2009, Chapter 3) found the marginal productivity of public investments declined by the early 1990s, particularly for transportation, agriculture-related, and flood control and forest conservation industries.

¹⁶ TARP was a USD700 billion fund created during the 2008 GFC. It enabled the purchase of the equity or capital of corporates or financial institutions, and consisted of five programmes to stabilise banks, support the automotive industry, restart flow of credit to small businesses and consumers, prevent avoidable foreclosures, and invest in the American International Group (AIG). (US Treasury, accessed online via <https://home.treasury.gov/data/troubled-assets-relief-program/about-tarp> on 3 February 2022)

(ii) Lack of Structural Reforms

Weak growth in the aftermath of the crises was also due to the lack of structural reforms to increase long-term productivity and potential GDP (Hoshi and Kashyap, 2015). These included the lack of reforms in Japan to address rigidities in the labour market¹⁷ that hindered the efficient reallocation of labour to more productive sectors in the long run. This labour market rigidity also prolongs the life of zombies, instead of facilitating an organic exit and entry of new firms after a crisis. In the euro area, the high tax burden and relatively high unemployment benefits also resulted in an inflexible labour market (IMF, 2013a; IMF, 2013b; IMF, 2013c; IMF 2014). In addition, weak firm-level competition contributed to higher input costs while government fiscal consolidation, which was still in progress, left less space for fiscal support during crises (Lachman, 2012). The slowdown in sectoral reallocation of labour and adoption of new technologies led to weak productivity and economic growth (Kollman et. al., 2016). It is worth noting that in contrast to France, Spain, and Italy, Germany was more successful in implementing labour market reforms (Deutsche Welle, 2003). Germany reduced hiring cost by lowering the premium for its national healthcare system and limited the duration of unemployment benefits. Job placement services were also enhanced through a decentralised approach and an increase in the ratio of counsellors to jobseekers.

(iii) Delayed Recovery of Banks' Balance Sheets

Efforts to recapitalise Japanese and European banks were not forthcoming, leading to slower recognition of bad loans and balance sheet recovery among its banks (Collignon, 2012; Hoshi and Kashyap, 2015). In Japan, this was driven by fears of a public outcry against the government bailing out banks using public funds. In the euro area, there was also reluctance among stronger countries to bail out banks in weaker member countries. One of the adverse implications of undercapitalisation in the banking sector is credit misallocation (Peek and Rosengren, 2005). Specifically, it incentivises banks to roll over borrowings to potentially non-viable firms rather than classifying loans as non-performing (i.e. evergreening¹⁸ of loans).¹⁹ This allows banks to avoid recognising losses which would further deteriorate their balance sheets. This sustains zombie firms instead of allowing creative destruction to occur naturally and reduces the flow of credit to more productive firms. Kalemli-Özcan et. al. (2019) found that highly indebted firms explained the depressed post-crisis corporate investments in Europe. The effect was strongest for firms with large short-term borrowings, reflecting greater rollover risk, with links to weak banks. The effect was also more apparent in peripheral euro area member countries, such as Greece, Ireland, Italy, Spain, and Portugal, with high exposure to domestic sovereign debt.

Policy Imperatives

As the global economy navigates through the recovery amidst the pandemic, several policy implications can be drawn from lessons offered by past crises.

(i) Timely, Direct and Proportionate Support

Policy support needs to be timely, direct, and proportionate to the size of economic shocks. During the pandemic, most countries met these conditions as they took swift and aggressive actions to support households and firms, especially during the initial lockdown (OECD, 2022). Now that we are past the acute phase of crisis, and with demand conditions improving along with elevated inflation, we are faced with different challenges. Importantly, this includes charting a path of normalising the policy stance. If kept

¹⁷ Japan's lifetime employment system, called the Subsidy for Employment Adjustment, was created in 1975 to avoid redundancies by implementing furloughs, transferring workers to related companies, and internal retraining (Hoshi and Kashyap, 2015). Subsidising firms to maintain employment helps to minimise job losses during crises but may hinder labour reallocation to more productive sectors or firms.

¹⁸ There have been recent guidelines to monitor banks' handling of bad debt. However, there is still scope for abuse and evergreening practices to occur. For instance, banks in Europe can resolve bad loans by renegotiating payment terms, if they feel repayment is still possible (European Banking Authority, 2015). However, there have been cases of abuse in which banks renegotiate with the sole intent of avoiding write-downs (reduction of asset value), rather than reclassifying loans as bad loans (Fredriksson and Frykström, 2019). This leads to continued extension of credit to zombies.

¹⁹ Caballero et. al. (2008) showed that evergreening of loans, proxied by the share of bank customers receiving subsidised credit, rose substantially in Japan from around 5% of firms in the early 1990s to about 30% in the late 1990s. Acharya et. al. (2019 and 2021b) found that undercapitalised banks in Europe increased credit supply to zombie firms while reducing lending to non-zombie firms, relative to better-capitalised banks after the GFC and during the sovereign debt crisis. For instance, credit growth to zombies from undercapitalised banks increased by 2 ppt in Portugal, following an unexpected rise in capital requirement (Blattner et. al., 2019).

for too long, policy accommodation, including low interest rates and generous regulatory forbearance, could lead to rising zombification and affect long-term productivity (Acharya et. al., 2021a). Policymakers will need to carefully weigh the trade-offs between the short- and long-term gains for a more sustainable recovery. As economic recovery gains traction, further government support could be made conditional on firms' viability (Banerjee and Hofmann, 2020). This could be supported by a focus on firms' pre-pandemic profitability and post-pandemic prospects.

(ii) Structural Reform is Key to Enhance Resilience

Beyond short-term measures, structural reforms are key to address long-term weakness and raise the economy's ability to weather downturns. These reforms could include investing in digitalisation in a post-pandemic era. Measures should also be taken to facilitate the efficient movement of labour to expanding firms or sectors. While job retention schemes have supported more than 50 million jobs globally during the pandemic, the recovery phase should now focus on protecting viable jobs, without hindering reallocation (OECD, 2020). For instance, Malaysia's latest five-year economic plan emphasizes the need to create high quality jobs and enhance job matching services, coupled with upskilling and reskilling efforts (Economic Planning Unit, 2021). These measures do not just target the ones retrenched during the pandemic, but those potentially displaced due to automation.

In terms of addressing zombies, policymakers should strengthen insolvency laws to enable easier exit of non-viable firms and smoother restructuring of viable firms (Andrews et. al., 2017). Reducing frictions in the corporate bankruptcy process, such as reducing processing time and personal costs to entrepreneurs, may speed up resource reallocation. For still-viable firms, facilitating a smooth restructuring helps them adapt quickly in a new environment. This includes enabling continued access to credit or a more diversified source of funding and reducing red tape. For instance, Norway passed a temporary act (the 'Restructuring Act') during the pandemic to assist still-viable firms to negotiate payments with their creditors, through a more flexible legal framework (Arntzen de Besche, 2020). This allowed firms to begin negotiations earlier, with simpler processes.²⁰ For Malaysia, out-of-court debt resolution platforms such as the Corporate Debt Restructuring Committee (CDRC) and Small Debt Resolution Scheme (SDRS) enable viable firms to restructure without resorting to lengthy, costly, and complex legal proceedings (Bank Negara Malaysia, 2021a). These platforms were further enhanced to allow more firms to benefit.²¹ Viable firms struggling to service debt obligations can also utilise court-sanctioned rescue mechanisms, under the Companies Act 2016 (CA 2016).²²

(iii) Maintaining Well-Capitalised Banks is Vital for Macroeconomic and Financial Stability

In times of weakness within the financial sector, accommodative monetary policy needs to be accompanied by a targeted bank recapitalisation programme (Acharya et. al., 2020). This helps to restore banks' balance sheet, which is crucial since zombie firms are normally funded by less healthy banks (Andrews and Petroulakis, 2017).²³ Due to post-GFC reforms, capital positions of banks have strengthened (Bank for International Settlements, 2021; Financial Stability Board, 2021) alongside strengthened resolution and recovery plans for banks in times of stress. This provided crucial countercyclical buffers, which banks could draw down on during downturns. As a result, banks remained largely resilient, averting the need for large-scale recapitalisation during the pandemic. This allowed banks to cushion, rather than amplify the economic shock at the height of the pandemic. For instance, banks in Malaysia were able to extend debt repayment assistance to affected households and businesses, while sustaining lending activities (Bank Negara Malaysia, 2021b).

²⁰ For example, the court can choose not to appoint a creditor committee if the debtor's business is small or if the case can be handled by the leader of the restructuring committee alone (Arntzen de Besche, 2020). This reduces the number of layers involved in the restructuring process and thus, saves time.

²¹ In 2017, the CDRC admission criteria was broadened by lowering the minimum debt threshold from RM30 million in 2010 to RM10 million. In September 2020, the SDRS was absorbed into the Credit Counselling and Debt Management Agency (Agensi Kaunseling dan Pengurusan Kredit, AKPK) to utilise AKPK's established online channel and create a one-stop platform on holistic debt restructuring to reach more micro, small and medium enterprises (MSMEs) (Bank Negara Malaysia, 2021a).

²² The CA 2016 introduced two new rescue mechanisms, namely the Corporate Voluntary Arrangement (CVA) and Judicial Management (JM), in addition to the widely used Scheme of Arrangement (SOA) (Bank Negara Malaysia, 2021a).

²³ Hence, reducing private costs to banks associated with letting zombie firms default and swiftly resolving non-performing loans (NPLs) could disincentivise evergreening by banks (Andrews and Petroulakis, 2017).

Conclusion

Since its trough in 2020, global growth has rebounded swiftly in 2021, aided by large-scale economic and financial support. However, the path ahead is far from certain. There remain risks which could derail recovery prospects from this pandemic. This article highlights the risks stemming from high corporate debt, as many firms had to increase leverage to sustain their operations during the pandemic. If left unaddressed, high debt held by non-viable firms (zombies) could affect long-term productivity. Policy lessons drawn from selected crises episodes indicate that the key is to achieve a delicate balance between short and long-term needs. As we move past the acute phase of the pandemic, longer-term reforms to address economic vulnerabilities and ensuring the health of the banking system are vital.

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Annex



Annex

CONTENTS

Key Economic and Financial Statistics

National Accounts

A.1	Gross Domestic Product by Kind of Economic Activity at Constant 2015 Prices	P 1
A.2	Growth in Manufacturing Production (2015=100)	P 2
A.3	Services Sector Performance at Constant 2015 Prices	P 2
A.4	GNI by Demand Aggregates	P 3
A.5	Savings-Investment Gap	P 3

External Sector

A.6	Balance of Payments	P 4
A.7	Gross Exports	P 5
A.8	Gross Imports	P 6
A.9	Malaysia's Trading Partners	P 7
A.10	Outstanding External Debt and Debt Servicing	P 8

Consumer and Producer Prices Index

A.11	Consumer Price Index	P 9
A.12	Producer Price Index	P 9

Financial Indicators

A.13	Movements of the Ringgit	P 10
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Public Finance

A.14	Consolidated Public Sector Finance	P 11
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Table A.1

Gross Domestic Product by Kind of Economic Activity at Constant 2015 Prices

	2018	2019	2020	2021 ^p	2022 ^f
	RM million				
Agriculture	99,637	101,580	99,367	99,186	100,717
Mining and quarrying	103,557	102,897	91,993	92,654	94,935
Manufacturing	304,843	316,283	307,924	337,295	354,902
Construction	66,194	66,453	53,556	50,767	53,880
Services	772,990	820,857	775,717	790,421	845,092
Plus: Import duties	16,546	16,240	15,324	15,656	17,026
GDP at purchasers' prices¹	1,363,766	1,424,310	1,343,880	1,385,978	1,466,552
	Annual change (%)				
Agriculture	0.1	2.0	-2.2	-0.2	1.5
Mining and quarrying	-2.2	-0.6	-10.6	0.7	2.5
Manufacturing	5.0	3.8	-2.6	9.5	5.2
Construction	4.2	0.4	-19.4	-5.2	6.1
Services	6.9	6.2	-5.5	1.9	6.9
Plus: Import duties	-8.5	-1.8	-5.6	2.2	8.7
GDP at purchasers' prices	4.8	4.4	-5.6	3.1	5.3 ~ 6.3

¹ Numbers may not necessarily add up due to rounding.

^p Preliminary

^f Forecast

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

Table A.2

Growth in Manufacturing Production (2015=100)

	2018	2019	2020	2021	2019	2020	2021
	Index				Annual change (%)		
Electrical and electronics products cluster	122.2	125.9	128.7	147.7	3.0	2.2	14.7
Computer, electronics and optical products	124.1	127.7	130.9	151.3	2.9	2.5	15.6
Electrical equipment	115.5	119.5	120.6	135.3	3.4	0.9	12.2
Machinery & equipment	117.3	121.4	122.8	137.1	3.5	1.1	11.6
Primary-related cluster	113.2	117.0	114.7	128.3	3.4	-2.0	11.9
Coke and refined petroleum products	110.2	113.2	101.2	112.9	2.7	-10.6	11.6
Chemical and chemical product	115.5	117.5	109.2	119.5	1.8	-7.1	9.4
Pharmaceutical products	115.9	120.7	138.2	159.9	4.2	14.5	15.7
Rubber and plastic products	113.4	118.9	150.2	178.4	4.9	26.3	18.8
Wood products	112.9	118.4	104.0	113.6	4.9	-12.1	9.2
Paper and paper products	115.0	120.0	116.5	133.8	4.3	-2.9	14.9
Furniture	122.1	132.0	122.8	118.3	8.1	-7.0	-3.7
Construction-related cluster	114.5	119.1	104.4	108.2	4.1	-12.4	3.7
Other non-metallic mineral products	115.1	120.3	103.1	104.2	4.5	-14.3	1.0
Basic metals	112.1	116.6	111.0	114.2	4.0	-4.8	2.8
Fabricated metal products, except machinery and equipment	115.5	119.8	101.3	107.7	3.7	-15.5	6.3
Consumer-related cluster	114.1	118.9	114.2	116.4	4.2	-4.0	2.0
Food products	116.9	120.1	121.0	123.2	2.8	0.8	1.8
Transport equipment and other manufactures	108.9	115.2	108.7	110.1	5.9	-5.7	1.3
Beverages	123.7	127.2	108.7	119.4	2.8	-14.5	9.9
Tobacco products	107.3	113.6	95.4	83.6	5.8	-16.0	-12.4
Textiles, wearing apparel, leather products and footwear	120.2	126.6	110.3	118.4	5.3	-12.8	7.3
Total	116.0	120.1	116.9	128.1	3.6	-2.7	9.5

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

Table A.3

Services Sector Performance at Constant 2015 Prices

	2018	2019	2020	2021 ^p	2018	2019	2020	2021 ^p
	Annual change (%)				Share to GDP (%)			
Services	6.9	6.2	-5.5	1.9	56.7	57.6	57.7	57.0
Intermediate services	6.9	6.4	-4.9	3.4	20.7	21.1	21.2	21.3
<i>Finance and insurance</i>	5.4	4.8	2.7	10.2	6.5	6.6	7.1	7.6
<i>Real estate and business services</i>	7.8	8.0	-15.2	-11.0	4.7	4.8	4.3	3.7
<i>Transport and storage</i>	6.3	6.8	-21.9	1.4	3.7	3.8	3.1	3.1
<i>Information and communication</i>	8.2	6.6	6.0	6.3	5.8	5.9	6.7	6.9
Final services	6.8	6.1	-5.9	1.0	36.0	36.6	36.5	35.7
<i>Wholesale and retail trade</i>	8.2	6.8	-6.1	1.6	16.7	17.0	17.0	16.7
<i>Food & beverages and accommodation</i>	9.0	9.6	-26.5	-11.0	3.3	3.5	2.7	2.4
<i>Utilities</i>	5.0	6.1	-1.3	2.6	2.6	2.7	2.8	2.8
<i>Government services</i>	4.7	3.5	4.5	5.4	8.4	8.3	9.2	9.4
<i>Other services</i>	5.5	5.6	-10.5	-3.5	4.9	5.0	4.7	4.4

^p Preliminary

Note: Numbers may not necessarily add up due to rounding.

Source: Department of Statistics, Malaysia

Table A.4

GNI by Demand Aggregates

	2018	2019	2020	2021 ^p	2022 ^f
	at Current Prices (RM million)				
Consumption	1,004,677	1,080,868	1,045,802	1,091,152	1,200,064
<i>Private consumption</i>	831,388	904,158	861,758	893,627	999,690
<i>Public consumption</i>	173,289	176,710	184,043	197,525	200,374
Investment	350,365	347,022	296,558	297,916	322,153
<i>Private investment</i>	245,819	252,572	222,238	230,999	247,539
<i>Public investment</i>	104,546	94,450	74,320	66,917	74,614
Change in stocks ¹	-4,387	-28,596	-17,016	45,995	7,364
Exports of goods and services	992,511	987,481	870,272	1,063,934	1,199,433
Imports of goods and services	895,405	873,618	779,011	954,783	1,033,800
GDP at purchasers' value	1,447,760	1,513,157	1,416,605	1,544,214	1,695,214
Balance of primary income	-45,082	-39,496	-28,584	-46,191	-69,195
GNI	1,402,677	1,473,662	1,388,021	1,498,023	1,626,019
	at Constant 2015 Prices (RM million)				
Consumption	946,083	1,008,790	979,360	1,006,133	1,081,268
<i>Private consumption</i>	776,054	835,711	799,447	814,289	887,213
<i>Public consumption</i>	170,030	173,080	179,913	191,844	194,055
Investment	335,592	328,581	281,060	278,516	295,978
<i>Private investment</i>	235,343	239,077	210,639	216,141	227,631
<i>Public investment</i>	100,249	89,504	70,421	62,376	68,347
Change in stocks ¹	-8,678	-13,987	-4,346	18,631	4,431
Exports of goods and services	917,462	907,877	827,086	958,455	1,004,917
Imports of goods and services	826,694	806,952	739,280	875,756	920,042
GDP at purchasers' value	1,363,766	1,424,310	1,343,880	1,385,978	1,466,552
Balance of primary income	-28,708	-21,856	-13,711	-23,686	-36,643
GNI	1,335,058	1,402,454	1,330,169	1,362,293	1,429,909

¹ Includes statistical discrepancy^p Preliminary^f Forecast

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

Table A.5

Savings-Investment Gap

	2017	2018	2019	2020	2021 ^p
	RM million				
Gross national savings	388,885	378,272	371,343	339,549	397,380
(as % of GNI)	29.2	27.0	25.2	24.5	26.5
Gross domestic capital formation	350,589	345,977	318,426	279,542	343,911
(as % of GNI)	26.3	24.7	21.6	20.1	23.0
Balance on current account	38,296	32,295	52,918	60,007	53,469
(as % of GNI)	2.9	2.3	3.6	4.3	3.6

^p Preliminary

Source: Department of Statistics, Malaysia

Table A.6

Balance of Payments¹

Item (Net)	2017	2018	2019	2020	2021p	2022f
	RM million					
Goods²	117,113	114,621	124,738	138,709	170,220	227,945
Services	-22,859	-17,515	-10,875	-47,448	-61,069	-62,312
Transportation	-29,622	-27,688	-25,925	-27,352	-32,493	-34,791
Travel	32,470	30,218	30,833	-7,651	-14,620	-12,578
Other services	-24,308	-19,287	-15,072	-11,842	-13,056	-14,056
Government goods and services n.i.e.	-1,398	-758	-711	-602	-901	-887
Balance on goods and services	94,255	97,106	113,863	91,261	109,151	165,633
Primary income	-38,658	-45,082	-39,496	-28,584	-46,191	-69,195
Compensation of employees	-4,848	-7,657	-9,229	-8,125	-6,553	-8,124
Investment income	-33,811	-37,425	-30,267	-20,459	-39,638	-61,071
Secondary income	-17,300	-19,729	-21,450	-2,670	-9,491	-20,679
Balance on current account	38,296	32,295	52,918	60,007	53,469	75,759
% of GDP	2.8	2.2	3.5	4.2	3.5	4.2 ~ 4.7
Capital account	-26	-89	371	-428	-783	-
Financial account	-4,730	11,430	-38,024	-76,155	29,656	-
Direct investment	16,171	10,103	6,555	2,756	32,854	-
Assets	-24,234	-23,431	-31,154	-15,219	-40,295	-
Liabilities	40,405	33,535	37,709	17,975	73,149	-
Portfolio investment	-15,358	-49,396	-32,403	-48,202	18,876	-
Assets	-19,442	-11,984	-46,919	-59,326	-36,170	-
Liabilities	4,084	-37,411	14,517	11,124	55,046	-
Financial derivatives	-197	981	-478	407	-221	-
Other investment	-5,346	49,742	-11,697	-31,116	-21,853	-
Assets	-18,081	6,527	-20,152	-5,206	-41,064	-
Liabilities	12,735	43,215	8,454	-25,910	19,211	-
Balance on capital and financial accounts	-4,756	11,341	-37,653	-76,583	28,874	-
Net errors and omissions³	-17,132	-35,878	-6,849	-2,721	-36,712	-
Overall balance	16,409	7,758	8,416	-19,297	45,630	-
Bank Negara Malaysia international reserves, net⁴						
USD million	102,431	101,429	103,599	107,621	116,876	-
RM million	414,591	419,511	424,032	432,313	486,790	-
Foreign exchange revaluation gain (+) / loss (-)	-25,691	-2,838	-3,895	-1,079	11,007	-
Reserves as months of imports of goods and services ⁵	5.7	5.6	5.8	6.7	6.1	-
Reserves as months of retained imports	7.2	7.4	7.5	8.4	7.7	-

¹ In accordance with the Balance of Payments and International Investment Position Manual, Sixth Edition (BPM6) by the International Monetary Fund (IMF)

² Adjusted for valuation and coverage of goods for processing, storage and distribution

³ As at 1Q 2018, the net E&O excludes reserves revaluation changes. This practice is backdated to 1Q 2010

⁴ All assets and liabilities in foreign currencies have been revalued into ringgit at rates of exchange ruling on the balance sheet date and the gain / loss has been reflected accordingly in Bank Negara Malaysia's audited accounts

⁵ For further details, please refer to "Expansion of the Measure on Reserves Coverage of Imports - from Retained Imports to Imports of Goods and Services" article in BNM's Quarterly Bulletin for the Fourth Quarter of 2021

p Preliminary

f Forecast

n.i.e. Not included elsewhere

Note: Numbers may not add up due to rounding

Assets: (-) denotes outflows due to the acquisition of assets abroad by residents

Liabilities: (+) denotes inflows due to the incurrence of foreign liabilities

Source: Department of Statistics Malaysia and Bank Negara Malaysia

Table A.7

Gross Exports

	2019	2020	2021p	2019	2020	2021p	2020	2021p
	RM million			Annual change (%)			% share	
Manufactures	840,586	849,498	1,067,209	0.4	1.1	25.6	86.3	86.1
<i>of which:</i>								
Electrical and electronic products	373,118	386,292	455,729	-2.2	3.5	18.0	39.3	36.8
<i>Semiconductors</i>	221,709	239,141	281,384	0.6	7.9	17.7	24.3	22.7
<i>Office machines and automatic data processing equipment</i>	49,347	45,409	54,316	-20.9	-8.0	19.6	4.6	4.4
<i>Electrical machinery, apparatus and appliances, and parts</i>	59,750	57,498	67,596	3.1	-3.8	17.6	5.8	5.5
<i>Telecommunications and sound-recording and reproducing equipment</i>	42,312	44,243	52,433	3.6	4.6	18.5	4.5	4.2
Petroleum products	71,511	61,889	95,658	-6.1	-13.5	54.6	6.3	7.7
Chemicals and chemical products	57,477	50,736	70,678	-0.4	-11.7	39.3	5.2	5.7
Manufactures of metal	41,490	36,830	61,560	-7.1	-11.2	67.1	3.7	5.0
Machinery, equipment and parts	41,599	39,446	49,590	2.3	-5.2	25.7	4.0	4.0
Optical and scientific equipment	39,905	42,220	46,926	9.1	5.8	11.1	4.3	3.8
Rubber products	25,841	44,302	64,607	-2.5	71.4	45.8	4.5	5.2
Palm oil-based manufactured products	23,338	21,006	32,704	2.4	-10.0	55.7	2.1	2.6
Processed food	21,773	21,283	24,598	12.2	-2.3	15.6	2.2	2.0
Transport equipment	19,143	18,460	15,914	6.2	-3.6	-13.8	1.9	1.3
Agriculture	65,958	71,724	98,099	-1.6	8.7	36.8	7.3	7.9
<i>of which:</i>								
Palm oil and palm oil-based agricultural products	44,208	52,326	75,812	-1.2	18.4	44.9	5.3	6.1
Sawn timber and moulding	4,251	3,116	3,274	-6.1	-26.7	5.1	0.3	0.3
Natural rubber	3,773	3,286	4,568	0.0	-12.9	39.0	0.3	0.4
Minerals	81,520	58,414	69,788	-9.3	-28.3	19.5	5.9	5.6
<i>of which:</i>								
Liquefied natural gas (LNG)	42,484	29,868	36,589	0.4	-29.7	22.5	3.0	3.0
Crude petroleum	26,346	18,843	20,009	-28.1	-28.5	6.2	1.9	1.6
Others	7,007	4,191	4,705	-27.1	-40.2	12.3	0.4	0.4
Total	995,072	983,827	1,239,802	-0.8	-1.1	26.0	100.0	100.0

p Preliminary

Source: Department of Statistics, Malaysia

Table A.8

Gross Imports

	2019	2020	2021p	2020	2021p	2021p
	RM million			Annual change (%)		% share
Capital goods	100,179	90,733	103,878	-9.4	14.5	10.5
Capital goods (except transport equipment)	91,762	91,344	98,835	-0.5	8.2	10.0
Transport equipment industrial	8,417	-611	5,043	-107.3	925.7	0.5
Intermediate goods	467,211	429,190	544,831	-8.1	26.9	55.2
Food and beverages, mainly for industry	18,050	20,670	27,138	14.5	31.3	2.7
Industrial supplies	220,877	205,422	268,051	-7.0	30.5	27.2
Fuel and lubricants	57,091	43,613	51,093	-23.6	17.1	5.2
Parts and accessories of capital goods (except transport equipment)	138,674	134,997	170,509	-2.7	26.3	17.3
Parts and accessories of transport equipment	32,519	24,488	28,040	-24.7	14.5	2.8
Consumption goods	74,155	74,134	83,896	0.0	13.2	8.5
Food and beverages, mainly for household consumption	30,782	32,590	36,810	5.9	12.9	3.7
Transport equipment non-industrial	1,017	1,091	1,700	7.3	55.8	0.2
Consumer goods, n.e.s	42,356	40,453	45,386	-4.5	12.2	4.6
Others	207,866	206,424	254,639	-0.7	23.4	25.8
<i>of which:</i>						
Dual use goods	32,482	17,281	19,608	-46.8	13.5	2.0
Re-exports	171,588	184,630	229,750	7.6	24.4	23.3
Total	849,411	800,481	987,244	-5.8	23.3	100.0

p Preliminary

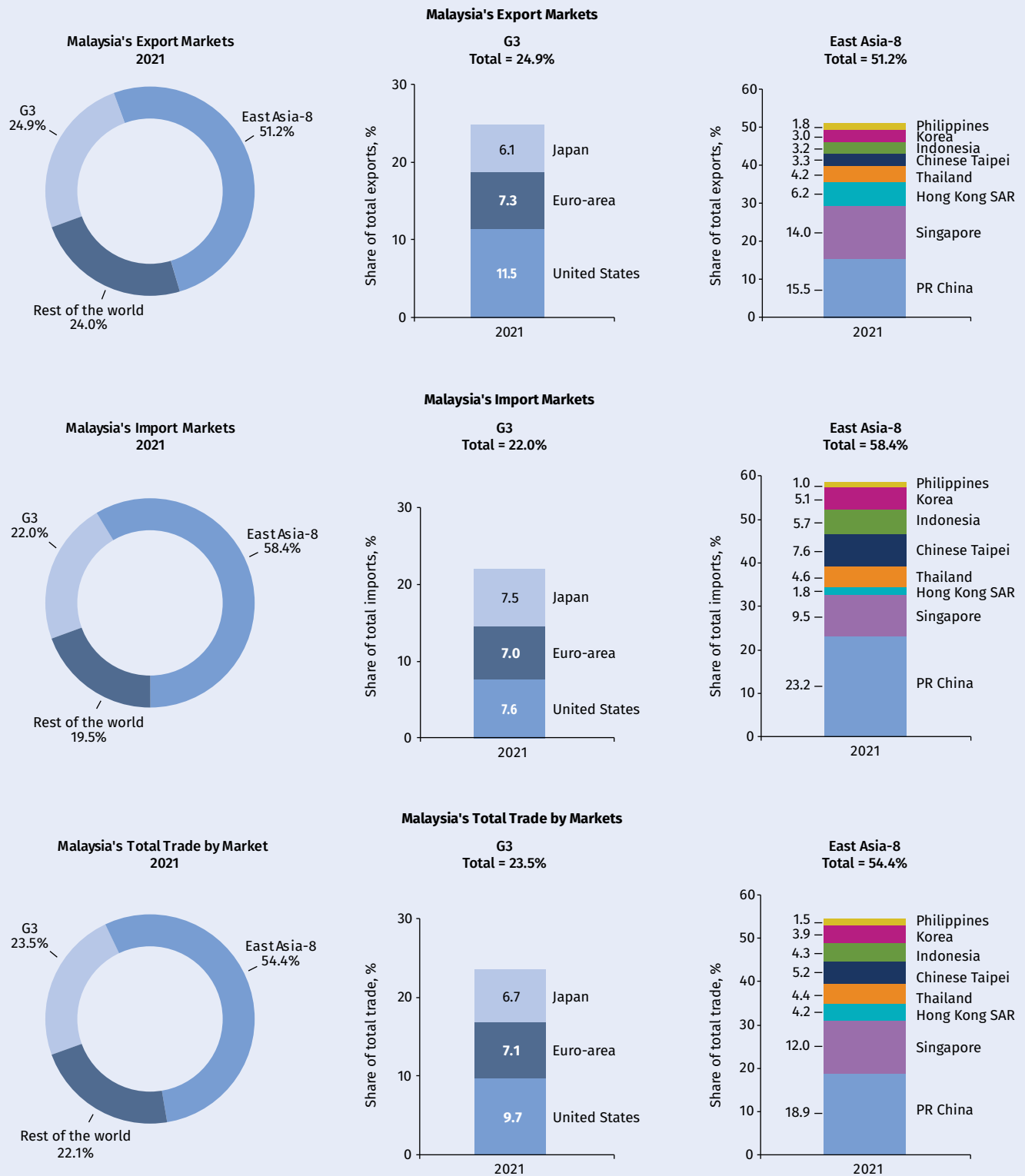
n.e.s. Not elsewhere specified

Note: Numbers may not necessarily add up due to rounding

Source: Department of Statistics, Malaysia

Chart A.9

Malaysia's Trading Partners



Source: Department of Statistics, Malaysia

Table A.10

Outstanding External Debt and Debt Servicing

	2017	2018	2019	2020	2021p
	RM million (unless stated otherwise)				
Total external debt	885,218	923,029	947,440	958,144	1,070,267
<i>USD million equivalent</i>	215,902	220,507	228,823	235,486	256,967
<i>% of GDP</i>	64.5	63.8	62.6	67.6	69.3
<i>Annual change (%)</i>	-3.2	4.3	2.6	1.1	11.7
By instrument					
Bonds and notes	151,364	152,589	158,920	172,740	197,163
Interbank borrowings	172,199	204,759	199,729	182,078	176,719
Intragroup loans	131,512	136,246	128,734	128,263	144,248
Loans	53,509	72,206	76,260	76,479	73,735
NR holdings of domestic debt securities	207,389	180,224	201,015	220,103	255,056
NR deposits	92,025	98,109	103,014	94,497	99,902
IMF allocation of Special Drawing Rights (SDRs)	7,759	7,759	7,631	7,810	28,150
Others ¹	69,461	71,137	72,137	76,173	95,295
Maturity profile					
Medium- and long-term	533,402	517,995	557,894	590,659	676,085
Short-term	351,816	405,034	389,546	367,485	394,182
Currency composition (% share)	100.0	100.0	100.0	100.0	100.0
<i>Ringgit</i>	34.7	30.3	32.6	33.9	34.8
<i>US dollar</i>	50.6	55.3	51.3	51.1	49.8
<i>Japanese yen</i>	2.2	2.2	2.9	3.2	2.7
<i>Others</i>	12.5	12.2	13.2	11.8	12.7
Total servicing (including short-term interest payment)	122,740	115,376	124,051	118,327	114,783
of which:					
Medium- and long-term debt	120,189	110,298	118,170	115,334	112,987
Repayment²	106,603	94,374	102,419	99,467	96,408
of which:					
Redemption of matured domestic debt securities held by NR	27,105	22,012	19,731	14,489	19,656
Interest payment	13,586	15,924	15,750	15,867	16,578
of which interest payment on:					
NR holdings of domestic debt securities	6,089	8,161	6,652	7,502	8,873
Debt service ratio (% of exports of goods and services)					
Total debt	12.8	11.6	12.6	13.6	10.8
Medium- and long-term debt of which:					
NR holdings of domestic debt securities	3.5	3.0	2.7	2.5	2.7

¹ Comprises trade credits and other debt liabilities² Excludes prepayment

p Preliminary

Note: Numbers may not necessarily add up due to rounding

NR refers to non-residents

Source: Ministry of Finance Malaysia and Bank Negara Malaysia

Table A.11

Consumer Price Index

	Weights (%) (2010=100)	2018	2019	2020	2021
		Annual change (%)			
Total	100.0	1.0	0.7	-1.2	2.5
Food and non-alcoholic beverages	29.5	1.6	1.7	1.3	1.7
Alcoholic beverages and tobacco	2.4	-0.1	1.5	0.3	0.5
Clothing and footwear	3.2	-2.0	-2.0	-0.8	-0.4
Housing, water, electricity, gas and other fuels	23.8	2.0	1.9	-1.7	1.5
Furnishings, household equipment and routine household maintenance	4.1	0.3	1.4	0.3	1.6
Health	1.9	0.8	0.7	1.1	0.4
Transport	14.6	1.6	-3.1	-10.0	11.0
Communication	4.8	-1.7	0.4	1.1	0.0
Recreation services and culture	4.8	-0.4	0.7	0.4	0.4
Education	1.3	1.1	1.4	1.0	0.2
Restaurants and hotels	2.9	1.6	1.2	0.5	0.4
Miscellaneous goods and services	6.7	-1.4	0.4	2.7	0.5

Source: Department of Statistics, Malaysia

Table A.12

Producer Price Index

	Weights (%) (2010=100)	2018	2019	2020	2021
		Annual change (%)			
Total	100.0	-1.1	-1.4	-2.7	9.5
Crude materials for further processing	16.4	2.6	-3.9	-12.3	30.3
<i>Foodstuffs and feedstuffs</i>	3.2	-2.0	0.2	-3.7	2.9
<i>Non-food materials</i>	13.2	3.7	-4.7	-14.2	37.0
Intermediate materials, supplies and components	56.1	-1.9	-1.4	-0.5	7.7
<i>Materials and components for manufacturing</i>	29.6	-5.2	-3.7	1.9	10.4
<i>Materials and components for construction</i>	2.9	-1.4	0.1	-0.5	0.7
<i>Processed fuel and lubricants</i>	11.9	8.7	2.3	-7.0	9.7
<i>Containers</i>	0.6	2.3	1.6	-1.3	2.8
<i>Supplies</i>	11.2	-3.8	0.5	0.3	0.7
Finished goods	27.5	-2.4	0.6	-0.1	-0.2
<i>Finished consumer goods</i>	11.5	-2.2	-1.4	0.4	2.7
<i>Capital equipment</i>	16.0	-2.5	2.0	-0.5	-2.4

Source: Department of Statistics, Malaysia

Table A.13

Movements of the Ringgit

	RM to one unit of foreign currency ¹			Annual change (%)		Change (%)
	2005	2020	2021	2020	2021	21 Jul. '05 - Dec. '21
	21 Jul. ³	End-Dec.				
SDR ²	5.5049	5.7560	5.8377	-1.8	-1.4	-5.7
US dollar	3.8000	4.0130	4.1760	2.0	-3.9	-9.0
Singapore dollar	2.2570	3.0354	3.0896	0.1	-1.8	-26.9
100 Japanese yen	3.3745	3.8891	3.6286	-3.2	7.2	-7.0
Pound sterling	6.6270	5.4653	5.6361	-1.7	-3.0	17.6
Australian dollar	2.8823	3.0896	3.0289	-7.2	2.0	-4.8
Euro	4.6212	4.9324	4.7256	-7.0	4.4	-2.2
100 Thai baht	9.0681	13.3990	12.5011	2.1	7.2	-27.5
100 Indonesian rupiah	0.0386	0.0286	0.0293	3.2	-2.4	32.1
100 Korean won	0.3665	0.3698	0.3507	-4.3	5.4	4.5
100 Philippine peso	6.8131	8.3569	8.1902	-3.4	2.0	-16.8
100 New Taiwan dollar	11.8900	14.2969	15.0400	-4.6	-4.9	-20.9
Chinese renminbi	0.4591	0.6143	0.6552	-4.5	-6.2	-29.9

¹ US dollar rates are the average of buying and selling rates at noon in the Kuala Lumpur Interbank Foreign Exchange Market. Rates for foreign currencies other than US dollar are cross rates derived from rates of these currencies against the US dollar and the RM/US dollar rate.

² The daily SDR rates published on the BNM website are based on latest available US Dollar SDR rates and prevailing USD/MYR mid-rates. The US Dollar SDR rate in this table is at a 1-day lag due to different time zones.

³ Ringgit was unpegged against the US dollar.

Source: Bank Negara Malaysia

Table A.14

Consolidated Public Sector Finance				
	2018	2019	2020	2021p
	RM billion			
Revenue ¹	241.0	252.7	248.3	243.4
% growth	4.5	4.9	-1.7	-2.0
Operating expenditure	266.0	298.2	263.6	268.4
% growth	5.8	12.1	-11.6	1.8
Current balance of NFPCs ²	128.2	128.3	71.2	135.9
Total public sector current balance	103.2	82.7	55.9	110.8
% of GDP	7.1	5.5	3.9	7.2
Development expenditure ³	144.5	134.5	117.5	141.8
% growth	9.7	-6.9	-12.6	20.7
General Government ⁴	63.7	57.9	55.6	67.8
NFPCs	80.8	76.5	61.8	73.9
COVID-19 Fund	-	-	38.0	37.8
Overall balance	-41.3	-51.7	-99.5	-68.7
% of GDP	-2.9	-3.4	-7.0	-4.4

¹ Excludes transfers within General Government

² Refers to 26 NFPCs from 2021 onwards

³ Adjusted for transfers and net lending within public sector

⁴ Comprises Federal Government, state and local governments, and statutory bodies

p Preliminary

Note: Numbers may not add up due to rounding

Source: Ministry of Finance, Malaysia and Non-Financial Public Corporations (NFPCs)

Glossary, Acronyms and Abbreviations



Aggregate outstanding ringgit liquidity placed with the Bank

Surplus liquidity absorbed by Bank Negara Malaysia, through its monetary operations and Statutory Reserve Requirement (SRR). The main borrowing instruments used for this purpose include direct money market borrowing, repurchase agreements (repo), Qard acceptance, Commodity Murabahah Programme (CMP), sell-buy swaps, Bank Negara Monetary Notes (BNMN) and Bank Negara Interbank Bills (BNIB).

Asset purchase programme

A form of expansionary monetary policy undertaken by central banks through the purchase of predetermined amounts of government bonds or other specified securities in order to lower long-term interest rates and stimulate the economy.

Balance of payments

A statistical summary of economic transactions between residents and non-residents of a country during a specific time period.

Bank Negara Interbank Bills (BNIB)

A short-term discounted note with maturity of up to one year and qualifies as Level 1 high-quality liquid assets (HQLA). BNIB can only be purchased by and traded among licensed banks and investment banks.

Base effect

The effect whereby a year-on-year growth rate, for a given month, is largely influenced by a non-seasonal deviation in the monthly growth rate of the base month (i.e. the same month in the previous year). For example, if the inflation rate was particularly low in January last year, even a moderate rise in consumer prices in January this year will arithmetically give a high year-on-year inflation rate in January.

Booster vaccination*

Doses administered to a vaccinated population that has completed a primary vaccination series (currently one or two doses of COVID-19 vaccine depending on the product) when, with time, the immunity and clinical protection has fallen below a rate deemed sufficient in that population. The objective of a booster dose is to restore vaccine effectiveness from that deemed no longer sufficient.

Core inflation

A measure of underlying inflation. One common method of calculation is by excluding items whose price fluctuations are deemed transitory from the Consumer Price Index (CPI) basket. These items include price-volatile and price-administered goods and services. Core inflation that is estimated by Bank Negara Malaysia also excludes the estimated direct impact of consumption tax policy changes.

Cost-push inflation

Inflationary pressures whereby the impetus for price increases comes from higher cost of production.

Current account

Records of a nation's transactions with the rest of the world—specifically its net trade in goods and services, its net earnings on cross-border investments, and its net transfer payments.

Direct investment abroad (DIA)

A category of cross-border investment by a Malaysian resident investor associated with the objective of establishing a lasting interest in an enterprise abroad. A 'lasting interest' is when there is a long-term relationship in which the direct investor has a significant degree of influence on the management of the enterprise (e.g. an ownership of at least 10% of the voting power).

Discretionary fiscal response

Additional actions taken by the government to influence the overall macroeconomy, through the use of revenue or expenditure measures, beyond existing fiscal rules.

Discretionary items

Non-essential items which households spend on with their income. Examples of these items include restaurants and hotels as well as recreational activities.

Domestic institutional investors

Resident financial institutions with large holdings of financial assets in domestic financial markets. These include banks, pension funds and insurance companies.

Exchange rate valuation effect

The changes in ringgit equivalent value of Malaysia's foreign-currency denominated external assets and liabilities, and export and import values due to changes in the ringgit exchange rate.

Financial account

Records of transactions that involve financial assets and liabilities that take place between residents and non-residents of a nation.

Financial conditions

Financial conditions reflect the ease of securing financing in the economy. It can be defined as the current state of financial variables that influence economic behaviour and therefore future economic activity. It is typically measured by an index, called the "Financial Conditions Index" that aggregates a wide range of financial variables, such as equity prices and bond yields.

Financial imbalances

Financial imbalances are often defined by their symptoms or manifestations. These could include over-investment in specific sectors, excessive credit growth, sharp increases in asset prices, or fiscal and current account imbalances. The most typical and frequently identified symptoms are asset price misalignments and excessive credit growth. These imbalances reflect the misallocation of resources and the disintermediation of funds towards speculative activity in asset markets.

* Source: World Health Organisation (WHO)

Foreign direct investment (FDI)

A category of cross-border investment by a non-resident investor associated with the objective of establishing a lasting interest in an enterprise in Malaysia. A 'lasting interest' is when there is a long-term relationship in which the non-resident direct investor has a significant degree of influence on the management of the enterprise (e.g. an ownership of at least 10% of the voting power).

Foreign exchange operations

The act of maintaining orderly market conditions in the domestic foreign exchange (FX) market by managing liquidity via buying or selling foreign and domestic currency with counterparties such as the commercial banks.

Headline inflation

The annual price increase for a basket of items that are commonly consumed by an average household. For Malaysia, headline inflation is computed based on the Consumer Price Index (CPI) basket.

Hedging facilities

Financial instruments that allow investors to reduce investment risk using financial derivatives such as options, swaps and futures contracts.

High-touch services

Services which are characterised by a high degree of personalised contact and face-to-face interaction with customers.

International investment position (IIP)

The external balance sheet, detailing the country's outstanding financial assets and liabilities position relative to the rest of the world. A positive net IIP denotes Malaysia's position as a net creditor nation, while a negative net IIP denotes Malaysia as a net debtor nation.

Investor risk aversion

A situation where investors prioritise preservation of capital over potentially higher returns, particularly in an environment of heightened uncertainties.

Labour productivity

Labour productivity refers to the efficiency and effectiveness of each employee to generate output or value added. It is expressed as a ratio of value added to total hours worked or to employment.

Liquidity injection operations

The use of monetary operations to provide liquidity to the banking system through instruments such as reverse repurchase agreements (reverse repos) and foreign exchange swap facilities.

Monetary Policy Committee (MPC)

The body responsible for formulating monetary policy and the policies for the conduct of monetary policy operations, as stipulated in the Central Bank of Malaysia Act 2009.

Monetary policy normalisation

Actions by central banks to return the stance of monetary policy back to more normal levels, which is consistent with the medium-term objective of achieving macroeconomic stability.

Net errors and omissions

Balancing or residual item which occurs when the current, capital and financial accounts do not mirror the change in international reserves due to imperfections in data source and compilation (e.g. incomplete data sources, difference in timing of recording, valuation factors).

Nominal wages

Nominal wages are wages expressed in a monetary form and is not adjusted for inflation.

Non-resident entity

An institutional unit which engages in economic activities and transactions for a period of one year or longer from a location outside of Malaysia.

Overnight Policy Rate (OPR)

The indicator of the monetary policy stance for Malaysia. The level of the OPR is decided by the MPC. It also serves as the target rate for the day-to-day liquidity operations of the Bank, which will influence other interest rates in the economy.

Pent-up demand

A rapid and transitory increase in demand for goods and services that is above and beyond its pre-economic downturn levels. This occurs when consumers hold off their spending on selected items during periods of economic slowdown and/or restrictions that inhibit certain purchases. This, in turn, results in a build-up of demand which would materialise when the economy recovers and/or restrictions are eased.

Portfolio Investment

A category of cross-border transactions and positions involving debt or equity securities in the capital markets, other than those categorised as foreign direct investments, direct investments abroad, or reserve asset transactions.

Portfolio rebalancing

A process whereby investors or fund managers reallocate the weightings of financial assets in their investment portfolios. This is achieved by buying and selling assets to align the investor's holdings with a target portfolio allocation.

Price controls

Government regulations which establish a fixed maximum price for specified goods and services.

Price valuation effect

Unrealised holding gains and losses on outstanding assets and liabilities following changes in market prices.

Primary income

Income earned from the contribution to production processes, provision of financial assets and renting of natural resources. These include compensation of employees (e.g. wages, salaries), investment income (e.g. dividends), interest income and rent transactions between residents and non-residents.

Primary vaccination

The initial dose(s) of a COVID-19 vaccine. Some brands of the vaccine consist of two vaccine doses for the primary series, while other brands consist of a single vaccine dose.

Producer price inflation

The annual change in Producer Price Index for local production, which is an output-based index that measures the price of goods sold to the domestic market charged by producers at the ex-factory price.

Resident entity

An institutional unit which engages in economic activities and transactions for a period of one year or longer from a location in Malaysia.

Safe haven assets

Financial assets that are expected to retain or increase in value during heightened stress in financial markets and economic uncertainty. They are typically assets that investors perceive to have guaranteed returns.

Sales and Services Tax (SST)

Sales tax is a single-stage tax levied on taxable goods imported into Malaysia and those locally manufactured in Malaysia by a taxable person, subject to the Sales Tax Act 2018. Service tax is a tax charged on taxable services provided by any taxable person in Malaysia in the course and furtherance of business, subject to the Service Tax Act 2018.

Secondary income

Current transfers (provision of goods, services, or financial assets) between residents and non-residents with no corresponding economic returns. These include transfers by the general government, personal transfers (e.g. remittance by foreign workers) and other transfers in cash or kind.

Short position

A financial position when an institutional unit sells securities (such as shares or foreign-currency) for which it is not the economic owner. This borrowed security is typically bought back in the open market, to be returned to its economic owner at an agreed upon price and date.

Statutory Reserve Requirement (SRR)

The SRR is a liquidity management instrument available to the Bank. It is used by the Bank to withdraw or release liquidity to the banking system when the excess or lack of liquidity is perceived by the Bank to be large and long-term in nature. The SRR is not a signal on the stance of monetary policy as the Overnight Policy Rate (OPR) is the sole indicator used to signal the stance of monetary policy.

Underemployment

Underemployment can be divided into two categories, which are time-related underemployment and skill-related underemployment. Time-related underemployment is defined as those who are employed less than 30 hours per week due to the nature of their work or because of insufficient work. Additionally, they are able and willing to accept additional hours of work. Skill-related underemployment is defined as those with tertiary education and working in the semi-skilled and low-skilled occupations.

Underlying inflation

The persistent trend component of inflation. It is typically constructed by removing the transitory and seasonal components from headline inflation.

Variants of Concern (VOCs)*

A SARS-CoV-2 variant that meets the definition of a Variants of Interest (VOI) and, through a comparative assessment, has been demonstrated to be associated with one or more of the following changes at a degree of global public health significance:

- Increase in transmissibility or detrimental change in COVID-19 epidemiology; or
- Increase in virulence or change in clinical disease presentation; or
- Decrease in effectiveness of public health and social measures or available diagnostics, vaccines, therapeutics.

Variants of Interest (VOI)*

A SARS-CoV-2 variant :

- with genetic changes that are predicted or known to affect virus characteristics such as transmissibility, disease severity, immune escape, diagnostic or therapeutic escape; and
- Identified to cause significant community transmission or multiple COVID-19 clusters, in multiple countries with increasing relative prevalence alongside increasing number of cases over time, or other apparent epidemiological impacts to suggest an emerging risk to global public health.

Weighted average base rate

Effective January 2015, the base rate (BR) is the main reference rate for new retail floating rate loans. The BR is determined by financial service providers' (FSPs) benchmark cost of funds and the Statutory Reserve Requirement (SRR). Other components of loan pricing such as borrower credit risk, liquidity risk premium, operating costs and profit margin would be reflected in a spread above the BR. The average BR of FSPs is weighted based on each FSP's share of outstanding floating rate loans.

Note: Beginning August 2022, the BR will be replaced with the Standardised Base Rate (SBR) as the main reference rate for new retail floating rate loans. The SBR is linked solely to the OPR, and the other components of loan pricing such as borrower's credit risk will be reflected in the spread above the SBR.

* Source: World Health Organisation (WHO)

Glossary, Acronyms and Abbreviations

12MP

Twelfth Malaysia Plan

AE

advanced economies

ALR

Average Lending Rate

BPR

Bantuan Prihatin Rakyat

BRF

Business Recapitalisation Facility

CDRC

Corporate Debt Restructuring Committee

CGC

Credit Guarantee Corporation

CMCO 2.0

Second Conditional Movement Control Order

CPI

Consumer Price Index

DFI

development financial institutions

DPGS

Danajamin Prihatin Guarantee Scheme

E&E

electrical and electronics

ECRL

East Coast Rail Link

EME

emerging market economies

ESG

Environmental, Social and Governance

FCY

foreign currency

FD

fixed deposit

Fed

US Federal Reserve

FMCO

Full Movement Control Order

FOMC

Federal Open Market Committee

GDP

Gross Domestic Product

GFC

Global Financial Crisis

GFCF

Gross Fixed Capital Formation

HOC

Home Ownership Campaign

ICR

Interest Coverage Ratio

ILO

International Labour Organisation

KLIBOR

Kuala Lumpur Interbank Offered Rate

LCTF

Low Carbon Transition Facility

LRT3

Light Rail Transit Line 3

M&E

machinery & equipment

MCO

Movement Control Order

MGII

Malaysian Government Investment Issues

MGS

Malaysian Government Securities

MPC

Monetary Policy Committee

NBFI

Non-Bank Financial Institutions

NEER

Nominal Effective Exchange Rate

NIA

National Investment Aspirations

NR

non-residents

NRP

National Recovery Plan

OPR

Overnight Policy Rate

OSC

One Stop Centre

PACU

Project Acceleration and Coordination Unit

PFLNG2

Petronas Floating Liquefied Natural Gas Dua

PPI

Producer Price Index

PTF

Penjana Tourism Financing

SDR

Special Drawing Rights

SDRS

Small Debt Resolution Scheme

SJPP

Syarikat Jaminan Pembiayaan Perniagaan

SME

small- and medium-sized enterprises

SOP

standard operating procedures

SRR

Statutory Reserve Requirement

TFP

total factor productivity

TRA

Targeted Repayment Assistance

TRRF

Targeted Relief and Recovery Facility

VOC

Variants of Concern

WSTS

World Semiconductor Trade Statistics

