From the Desk of the
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Economic Research

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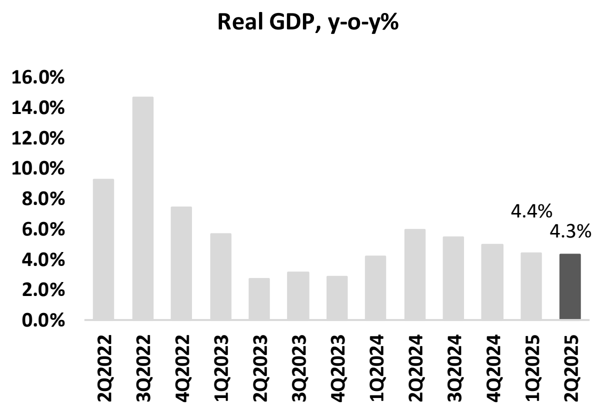
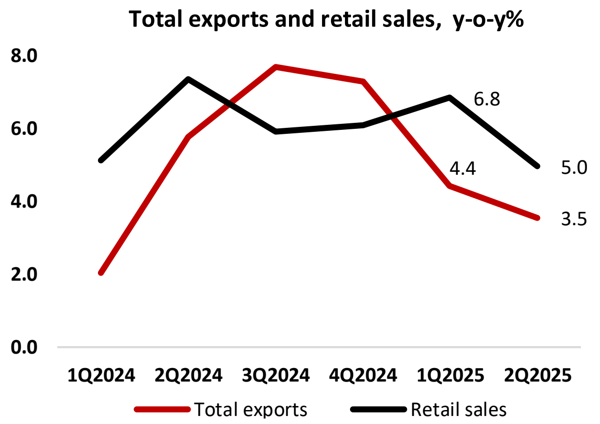
2Q2025 GDP PREVIEW: GROWTH LIKELY BELOW ESTIMATES AMID SOFTER CONSUMER SPENDING AND EXPORTS





Sources: Department of Statistics Malaysia (DOSM), Bank Islam

- **2Q2025 GDP growth expected to fall slightly below DOSM's Advance Estimate**. Malaysia's economic growth for 2Q2025 is projected to come in slightly below the Department of Statistics Malaysia's (DOSM) advance estimate of 4.5%, with GDP likely to expand by 4.3% (1Q2025: 4.4%). Demand-side indicators in 2Q25 were mixed. Private consumption, the key growth driver, is expected to have moderated, with retail sales growth easing to 5.0% (1Q25: 6.8%), the slowest pace in six quarters. The Index of Services also softened slightly to 5.0% from 5.2% in the previous quarter. Despite this moderation, labour market conditions remained firm, with the unemployment rate edging down to 3.0%, the lowest since April 2015. This continued strength in employment likely provided some support to household spending, alongside the disbursement of Phase 2 of the Sumbangan Tunai Rahmah (STR) at end-March, which may have lifted expenditure in early 2Q25. However, the absence of major festivals during the quarter, combined with fading effects from February's minimum wage hike and the civil servant salary adjustment, likely tempered consumption growth. Externally, trade momentum eased, with exports slowing to 3.5% (1Q25: 4.4%) amid softer growth in both manufacturing and agriculture. Overall, these trends suggest a slightly weaker GDP performance for 2Q2025 than DOSM's preliminary estimate.

- **Weaker manufacturing and decelerating export growth amid persistent global headwinds.** Manufacturing activity was at a slower momentum in the second quarter of 2025. The Industrial Production Index (IPI) growth eased for the fourth consecutive quarter, moderating to 2.0% in 2Q25 from 2.3% in 1Q25. Manufacturing output also slowed, with growth softening to 3.9% from 4.2% in the previous quarter. In addition, the Manufacturing PMI remained in a state of contraction of below the 50-point expansion mark to close at 48.9 points in 2Q2025. The latest manufacturing PMI data in July also pointed to weakness at 49.7 points. While overall exports still grew by 3.4%, this was a slower pace than the previous quarter of 4.3%. Export growth to the U.S. and EU remained strong at 20.2% (1Q2025: 36.4%) and 5.5.% in 2Q2025 (1Q2025: 4.7%), though the export growth to U.S. decelerated. Exports to China, however, continued to shrink, with a 4.4% contraction in the second quarter, deteriorating from the decline of 4.2% in the previous quarter.

- **Investment momentum is anticipated to remain solid, although a slight moderation is to be expected.** While investment momentum has remained remarkably solid thus far, the heightened global volatility characterised by Trump's tenure and the likelihood of it persisting throughout his four-year term have casted a dark cloud over the Malaysian economic outlook. As such, the dampened growth prospects are increasingly eroding investor confidence, leading to more subdued investment activities in the near term and tempering the construction sector performance. Of note, construction work done expanded at a slower pace of 12.9% y-o-y in 2Q2025 from 16.6% y-o-y in 1Q2025, underpinned by slower growths across the special trade activities (2Q2025: +22.2% vs. 1Q2025: +35.5%), non-residential buildings (2Q2025: +16.2% vs. 1Q2025: +21.0%) and residential buildings (2Q2025: +13.9% vs. 1Q2025: +27.0%) subsectors while the civil engineering subsector accelerated by 7.5% in the same quarter (1Q2025: +3.7%). However, it is not all doom and gloom as numerous ongoing multi-year development projects are providing crucial support to the sector. Latest figures showed that most construction work done are concentrated around Selangor, Johor and Sarawak where multiple projects such as the Subang Airport regeneration, the Light Rapid Transit (LRT) 3, Rapid Transit System Link (RTS Link) between Johor Bahru and Singapore, the Pan-Borneo Highway projects and the Kuching Urban Transportation System (KUTS) are in progress. Looking ahead, Malaysia's long-term outlook remains favourable, supported by proactive government policies, strategic regional partnerships, firm domestic demand, and the gradual stabilisation of the global economy. The recently launched 13th Malaysia Plan underscores the government's commitment to expanding high-growth, high-value industries, advancing the Artificial Intelligence (AI) ecosystem, and improving the affordable housing landscape for the rakyat. Together with other MADANI policy initiatives, these measures are expected to attract new investments and provide strong impetus for Malaysia to achieve its growth objectives.

- **Malaysia's economic growth is projected to moderate in the second half of 2025**, primarily due to escalating external headwinds following President Trump's announcement of a potential 100% tariff on semiconductor imports, in addition to a newly imposed 19% levy. Moreover, the U.S. implementation of varying fresh tariff rates on other major economies, including Malaysia's key trading partners such as China, presents additional downside risks to external demand. Should these tariffs lead to prolonged adjustments in global supply chains or result in higher trade costs being passed through to trading partners, global trade activity could face further pressures. Of particular concern is the potential 100% tariff on semiconductor produced outside the U.S. given that electrical and electronics (E&E) products comprise around 40.0% of Malaysia's total exports, with approximately 20.0% of these destined for the U.S. market. Any disruptions in this segment could weigh heavily on Malaysia's export performance, particularly in semiconductors segment. Nonetheless, domestic demand is expected to remain resilient and provide a buffer against external shocks. The government's additional stimulus measures including a one-off RM100 cash transfer to all Malaysian adults effective end-August are anticipated to support household consumption in the near term. In addition, the 25bps reduction in the Overnight Policy Rate (OPR) in July is expected to provide further support to domestic activity by lowering borrowing costs. All in all, while external uncertainties may weigh on the export-oriented sectors, domestic policy measures are expected to help sustain Malaysia's near-term growth momentum.