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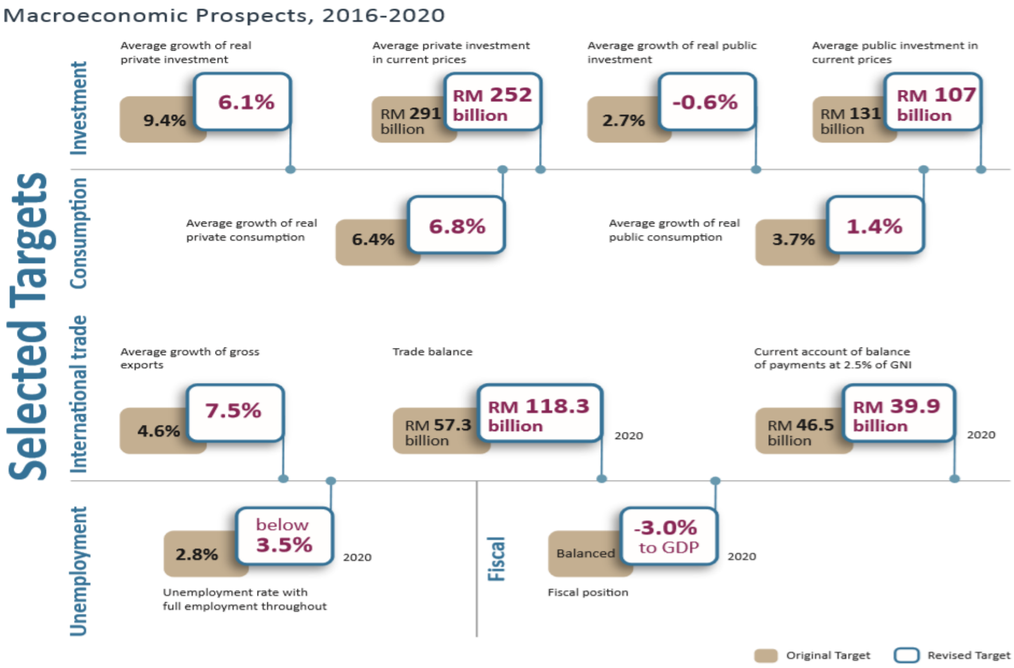
Mid-Term Review of 11th Malaysian Plan

The unveiling of the mid-term view of 11th Malaysian Plan (MTR11MP)

Prime Minister Tun Dr Mahathir Mohamad has unveiled the mid-term review of 11th Malaysian Plan 2016 – 2020 (MTR11MP) today. The MTR11MP has outlined the government strategy to steer the country in order to build a prosperous, harmonious and an inclusive nation. The articulation of such document would also shed more lights into government policy especially in the context of limited fiscal space and the need to keep a lid on the level of indebtedness. This would be critical as the external enviroment has been increasingly challenging against a backdrop of the ongoing trade tension, global monetary tightening as well as uncertainty in the commodity prices. Thus far, foreign investors have been reducing their Malaysian Government Securities (MGS) holding to 39.5% of total outstanding MGS as of September this year. This was in contrast to the previous high of 51.9% in October 2016. The decline was in tandem with the rise in the US Federal Fund Rate which has risen 200 basis points since December 2015. Therefore, the unveiling of MTR11MP should ease concerns on policy direction.

The macroeconomic targets have been revised to reflect the the current realities which were mostly non-existent when the plan was first tabled in 2015. The trade war between the US and China, global monetary tightening and the UK Brexit are some of the key external challenges that will shape investors confidence, capital flows and volatiliy in the financial markets. Notable changes is the GDP growth projection which was revised from 5% - 6% to 4.5% - 5.5% between 2016 and 2020. Inflation rate is expected to range between 2% and 3% from the original estimates of 2.8% while unemployment rate is anticipated to remain below 3.5% from 3.4% recorded at the end of 2017.

More importantly is the revision to the fiscal deficits target by end of 2020 from 0.6% of GDP to 3.0%. This suggets that the government is being pragmatic in setting its fiscal consolidation goal after taking into account the repeal of the Goods and Services Tax (GST). In the 1H2018, the fiscal deficits stands at RM30.1 billion or 4.5% of GDP. Therein lies important growth strategies that needs to be articulated especially in the context of heightened external uncertainties as well as the growing concerns on cost of living and affordable houses among the low and middle income earners.



Source: MTR11MP

The key thrusts

1. Enhancing inclusiveness towards an equitable society by uplifiting Bottom 40% (B40) households towards a middle-class society and increase the Bumiputera ownership of financial and non-financial assests.
2. Improving wellbeing of all for quality healthcare, provide afforadable housing and implement various crime prevention. However, there are still concerns of continously increasing in house prices.
3. Accelerating human capital development for an advanced nation. There are still few challenges faced by the government such as inadequate job creation in skilled category, dependancy on low-skilled foreign workers, underemployment among graduates and lack of collaboration between public Institution of Higher Education (IHE) and research institutions as well as at industries.
4. Pursuing green growth for sustainability and resilience. Neverthelesss, issues and challenges remained, these include governance-related issues, limited green technology and products, degradation of natural resources as well as environment-related issues.
5. Strengthening infrastructure to support economic expansion. However, infrastructure development continues to be affected by issues, such as lack of coordination in transport and energy sectors, financial sustainability in water servies and regulatory conditions related to broadband infrastructure.
6. Re-engineering economic growth for greater prosperity, outlined strategies to accelerate economic growth. Persistent challenges in economic sector and gap in term of special skills set required by the workforce to exploit technology advancement still remain a concern.

GDP growth projection revised lower

The economy is anticipated to grow 4.5% - 5.5% range between 2018 and 2020. Economic growth would be primarily driven by strong domestic demand amid challenging external environment. Major source of growth would be emanated from **private consumption** which is expected to expand 7.0% during 2018 - 2020. Similarly, **private investment** growth was revised lower from 9.4% per annum to 5.7% per annum between 2016 and 2020. Realising this, a conscious efforts will be undertaken to ensure quality foreign direct investment in high value-added products and services, which will utilize and promote technology transfer to local companies. Meanwhile, **public consumption** is expected to grow moderately by 0.3% per annum in 2018 – 2020 as the government aimed to optimize its spending program. On the contrary, **public investment** growth is expected to contract -0.8% per annum in 2018 and 2020 from original target of 2.7% expansion due to the revision of the major infrastructure projects such as the East Coast Rail Link (ECRL) and High Speed Rail (HSR). In a nutshell, the anticipation of slower growth in 2018 and 2020 is well telegraphed and should set the tone for policy measures.

Gross Domestic Product by Expenditure Category, 2010-2020
(at constant 2010 prices)

Item	RM million					Average Annual Growth Rate, %				
	Actual				Revised Target	Tenth Plan	Eleventh Plan			
						Actual	Original Target	Progress	Revised Target	
	2010	2015	2016	2017	2020	2011-2015	2016-2020	2016-2017	2018-2020	2016-2020
Private Expenditure	**496,536**	**735,772**	**776,688**	**835,256**	**1,014,014**	***8.2***	***7.2***	***6.5***	***6.7***	***6.6***
Consumption	395,245	556,632	589,774	630,988	772,983	*7.1*	*6.4*	*6.5*	*7.0*	*6.8*
Investment	101,291	179,140	186,914	204,268	241,031	*12.1*	*9.4*	*6.8*	*5.7*	*6.1*
Public Expenditure	**186,347**	**238,226**	**239,031**	**246,972**	**246,183**	***5.0***	***3.3***	***1.8***	***-0.1***	***0.7***
Consumption	103,346	143,577	144,877	152,769	154,180	*6.8*	*3.7*	*3.2*	*0.3*	*1.4*
Investment	83,001	94,649	94,154	94,203	92,003	*2.7*	*2.7*	*-0.2*	*-0.8*	*-0.6*
Net Export	**130,738**	**91,212**	**92,757**	**90,958**	**95,684**	***-6.9***	***0.4***	***-0.1***	***1.7***	***1.0***
Exports of Goods and Services	714,075	771,739	781,939	855,196	913,285	*1.6*	*2.1*	*5.3*	*2.2*	*3.4*
Imports of Goods and Services	583,337	680,527	689,182	764,238	817,601	*3.1*	*2.3*	*6.0*	*2.3*	*3.7*
Gross Domestic Product	**821,434**	**1,063,998**	**1,108,935**	**1,174,329**	**1,357,520**	***5.3***	***5.0-6.0***	***5.1***	***4.5-5.5***	***4.5-5.5***

Notes: The added total may differ due to rounding.
Source: Department of Statistics Malaysia and Economic Planning Unit

On the supply side, the **services sector** is targeted to sustain the growth momentum at 6.3% in 2018 – 2020 (Original Target: 6.9%), underpinned by the various initiatives via the Services Sector Blueprint as well as efforts in promoting Digital Free Trade Zone and productivity improvements under the Malaysia Productivity Blueprint (MPB). The **manufacturing sector** is targeted to grow at 4.5% per annum in 2018 - 2020, slightly lower than the original target of 5.1%.

This is largely driven by the shift towards high value-added, diverse and complex products, particularly in the fields of electrical and electronics i.e. automotive industry, machinery and equipment, chemicals products, aerospace, medical devices as well as artificial intelligence applications.

The **construction sector** is targeted to be moderating at 4.3% in 2018 – 2020 due to slower growth of residential and non-residential subsectors. Meanwhile, the limited fiscal space lead to reprioritisation of major infrastructure projects gives a significant impact on the growth momentum of construction sector. However, greater adoption of the industrialised building system and ongoing civil engineering projects such as the Mass Rapid Transit (MRT 2) and Pengerang Integrated Petroleum Complex in Johor are expected to expand the sector further.

The **agriculture sector** is targeted to grow at 2% per annum in 2018 - 2020, owing to increase in the production of palm oil, rubber and food crops. In addition, the contribution of the agro-food subsector to agriculture sector is targeted to increase as well, with emphasis on productivity improvements and modernisation as well as the introduction of new sources of wealth, such as premium-grade fruits, high-yielding coconut varieties and large scale grain corn production.

The **mining sector** is targeted to grow marginally at 0.1% in 2018 - 2020 due to the extended commitment to cut production by the Organization of the Petroleum Exporting Countries (OPEC) and non-OPEC countries as well as the disruption of natural gas supply in the Sabah-Sarawak Gas Pipeline in 2018. However, the production of natural gas is expected to expand following the construction of the PETRONAS floating liquefied natural gas 2 at the Rotan field, offshore Kota Kinabalu, Sabah to meet expected higher global demand for low-carbon energy.

Again, growth parameters are generally on slower trajectory on the supply side. Combination of supply disruption in commodity space as well as external demand uncertainties are the main consideration during the forecast period.

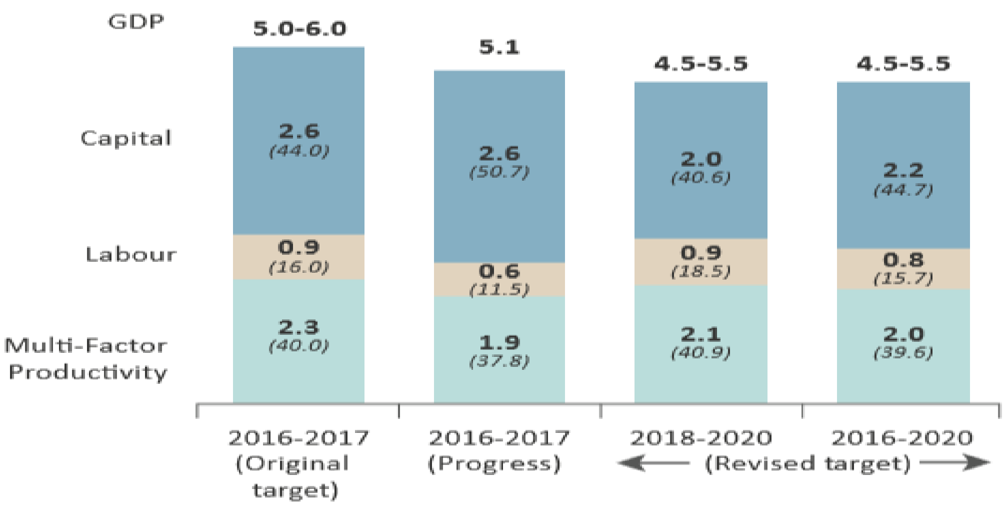
Gross Domestic Product by Kind of Economic Activity, 2010-2020 (at constant 2010 prices)

Sector	RM million					Average Annual Growth Rate, %				
	Actual				Revised Target	Tenth Plan	Eleventh Plan			
						Actual	Original Target	Progress	Revised Target	
	2010	2015	2016	2017	2020	2011-2015	2016-2020	2016-2017	2018-2020	2016-2020
Agriculture	82,882	94,396	89,509	95,968	101,902	2.6	3.5	0.8	2.0	1.5
Mining and Quarrying	89,793	95,508	97,468	98,436	98,877	1.2	1.3	1.5	0.1	0.7
Manufacturing	192,493	243,703	254,472	269,804	308,128	4.8	5.1	5.2	4.5	4.8
Construction	28,213	46,719	50,197	53,574	60,750	10.6	10.3	7.1	4.3	5.4
Services	420,382	569,865	602,261	639,568	769,066	6.3	6.9	5.9	6.3	6.2
Electricity, Gas and Water	22,173	27,161	28,618	29,437	32,573	4.1	3.9	4.1	3.4	3.7
Wholesale & Retail Trade, Accommodation and Restaurants	134,634	185,260	197,167	211,258	259,783	6.6	5.9	6.8	7.1	7.0
Transport, Storage and Communications	68,511	98,062	105,120	113,107	143,563	7.4	8.8	7.4	8.3	7.9
Finance, Insurance, Real Estate and Business Services	93,939	119,399	124,470	131,565	155,440	4.9	6.8	5.0	5.7	5.4
Government Services	64,359	93,208	97,818	102,623	116,214	7.7	6.3	4.9	4.2	4.5
Other Services	36,766	46,776	49,068	51,578	61,492	4.9	9.4	5.0	6.0	5.6
Plus: Import Duties	7,672	13,808	15,030	16,980	18,797	12.5	1.4	10.9	3.4	6.4
Gross Domestic Product	821,434	1,063,998	1,108,935	1,174,329	1,357,520	5.3	5.0-6.0	5.1	4.5-5.5	4.5-5.5

Notes: The added total may differ due to rounding.
Source: Department of Statistics Malaysia and Economic Planning Unit

Factors of Production, 2016-2020

Growth, at constant 2010 prices, % p.a.
Share to growth in brackets, %



Source: Department of Statistics Malaysia and Economic Planning Unit

In terms of the quality of economic growth, the Multi-factor Productivity (MFP) has contributed 37.8% to the overall economic growth between 2016 and 2017, which was lower than the original target of 40%. However, it was still an improvement compared to 23.7% in the Tenth Plan. MFP measures the part of economic growth that cannot be explained by the increased utilization of capital and labour, and is often interpreted as the contribution to economic growth made by factors such as technical and organization innovation as well as quality of labour. MFP is synonymous to Total Factor Productivity (TFP). Among the economic issues affecting the slow pace of economic reforms are Malaysia is too depending on the traditional factor inputs, namely Capital and Labour as well as less on productivity to drive growth. Moreover, current Investment that more focused on physical structures instead of machinery and equipment has also contributed to the slow pace of economic reform.

For the remaining plan period, 2018-2020, the MFP contribution to economic growth is expected to improve to 40.9%. The contribution of capital and labour inputs to GDP growth is targeted at 40.6% and 18.5%, respectively. Greater adoption of advanced technologies, automation by industries as well as the increase of skilled and knowledge workers in the labour force have been the benchmarking for the revised target.

In short, the MFP narrative indicates the urgencies to reform the education sector that will improve employability among the graduates while upgrading production capacity at companies' level via automation and mechanisation would lead to higher demand for skilled workers.

The way we see it

The government is very mindful on its limited resources as it need to juggle between promoting sustainable economic growth while keeping its finances in check. In this regards, quality investments have been touted as the prime vehicle to uplift the value added of the economy. This would mean innovation, automation, adoption of new technology and commercialisation of intelectual property. Along the way, this would reduce the country's dependency on foreign labour especially in manufacturing and construction sector. Apart from that, the Waqaf concept is expected to make further inroads into the mainstream economics and would complement the public expenditure to some degree. On that score, the Jabatan Waqaf, Zakat dan Haji (JAWHAR) will be tasked to formulate a comprehensive framework to unlock the development potential of waqf land via collaboration with Yayasan Waqaf Malaysia, state Islamic religious councils (SIRCs) and state governments.

In a nutshell, the revision in growth targets are very much in line with our expectation and the deficits targets of 3.0% of GDP by 2020 should indicates that the government is not about to tighten its budgetary position excessively. Value for money spending mantra would be the order of the day.