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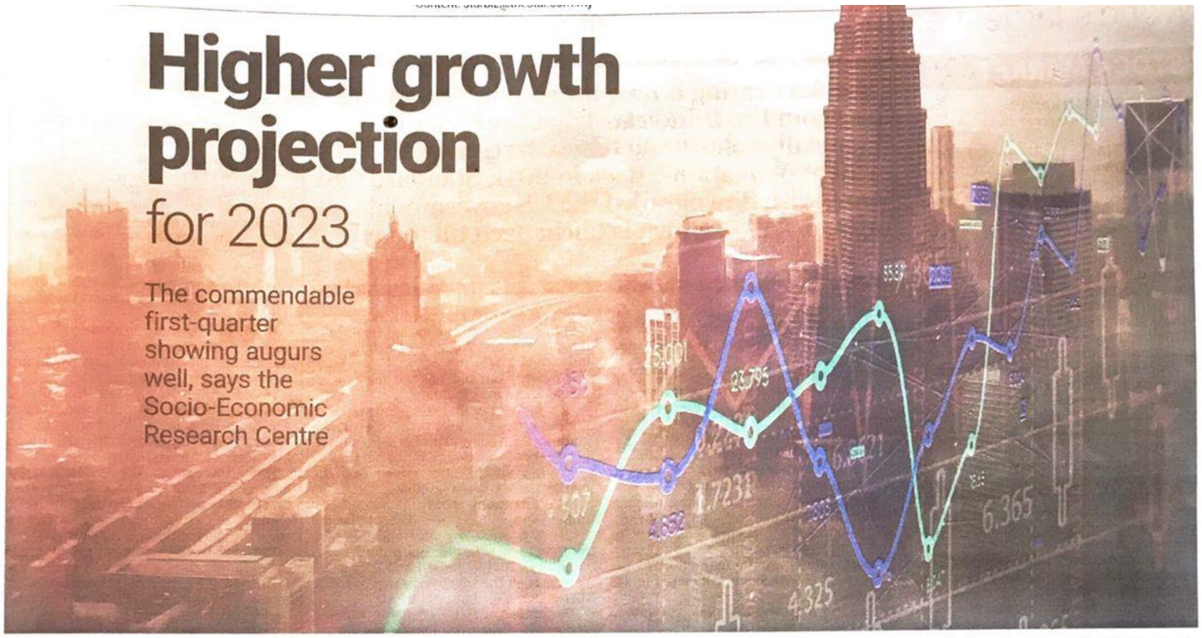
Higher growth projection for 2023



Higher growth projection for 2023

The commendable first-quarter showing augurs well, says the Socio-Economic Research Centre

ECONOMY

By KIRENNESH NAIR
kirennesh@thestar.com.my

> "Structural reforms are key to supporting the economy and the ringgit."
>
> Lee Heng Guie

KUALA LUMPUR: The combination of declining exports, persistently high core inflation and cautious consumer spending will likely see the economy experiencing a moderation in growth in the second half of the year (2H23).

Despite anticipating a deceleration in economic growth in the upcoming quarters, Socio-Economic Research Centre (SERC) has raised its 2023 gross domestic product (GDP) growth projection to 4.5% year-on-year (y-o-y) from 4.1% previously, to reflect the strength in the first-quarter (1Q23) economic growth.

The GDP expanded by 5.6% in 1Q23, exceeding the 4.8% growth achieved in 1Q22, thanks to sustained domestic demand underpinned by strong private expenditure and improvement in labour market conditions.

SERC executive director Lee Heng Guie said the robust consumer spending witnessed last year may not be replicated this year due to the high interest rate environment and more cautious consumer spending.

"The cash stimulus has already been spent and the spending boom, such as the 'revenge spending' that we saw post-pandemic, has already faded," he said during SERC's media briefing on the quarterly economic tracker for 2Q23.

Lee pointed out that the country's exports had also started to ease as global demand weakens under the strain of high inflation and interest rates.

For 1H23, exports contracted by 4.5% y-o-y and Lee projects exports to decline by between 5% and 7% for the full year on the back of lower demand.

With these factors at play, SERC expects GDP to grow in a range of between 4% and 5% in 2H23, with consumer demand continuing to be the key growth driver in the remaining months of the year.

He added the elevated base effect in 2H22 will present another challenge to the 2H23 GDP performance.

On the overnight policy rate (OPR), Lee believes the current rate of 3% is at an "accommodative and supportive" level for sustainable economic activity.

He said interest rates may stay elevated for some time and expects Bank Negara to hold the OPR at the current level in 2023 and into 2024.

"Any change to the OPR is dependent on how resilient the economy is and how consumer inflation behaves.

"I think the current level is just right, (as) it will not significantly hurt the people.

> TURN TO PAGE 2

Battle against inflation not over yet

> FROM PAGE 1

"It is still supporting the economy, but does not overburden businesses and the people. Even though central banks are likely to end their rate hike cycles, it does not necessarily imply that they will reduce rates either," he explained.

Lee expects most central banks to likely keep interest rates at current levels till inflation, both headline and core, subsides to a "comfortable range".

In the majority of advanced economies, a comfortable range of inflation is around 2%, Lee observed. Although headline inflation has eased in Malaysia, Lee stressed the battle against inflation has not been won.

"This is because subsidy rationalisation is still on the table of the government. The government needs to address that following the state elections to control the budget deficit," Lee noted.

Given the volatility in crude oil prices, Lee said the current oil subsidy scheme was fiscally unsustainable and would further contribute to deficits.

He added the ringgit had strengthened against the currencies of Japan, China, Australia, Taiwan and India since the US Federal Reserve's (Fed) first federal fund rate hike in March last year.

However, against the greenback, the local unit is among a basket of currencies that have experienced a significant weakening after having declined by about 7.4% since the start of the rate hike cycle.

"Structural reforms are key to supporting the economy and the ringgit," Lee stressed.

He said the proposed progressive wage model (PWM) plan, which is currently under consideration by the government, is a right step towards a productivity-linked wage system which will foster competitiveness by forging a stronger correlation between wages and productivity.

Lee, however, contends that a more comprehensive and practical analysis should be undertaken on the plan by a tripartite body, which includes representatives from the government, employers and employees.

This is due to the presence of valid concerns and areas of uncertainty within the proposal, such as whether the PWM would be extended to foreign workers and specific sectors.

In keeping the economy resilient, Lee emphasised on the importance of private investment.

He reiterated that private investment not only helped stimulate economic growth, but also generated jobs and thus benefiting both the community and the nation as a whole.

Speaking on the US economy, Lee believes that it is still resilient, citing the strength of its labour market and wage growth as indications. However, he said consumer spending remained robust and asserts inflationary pressure.

"In the United States, headline inflation has not reached the targeted 2% level, while core inflation remains sticky.

"This is something the Fed would be observing. If there is risk of inflation resurgence, it may still continue to increase rates," Lee said.

Globally, Lee pointed out that the purchasing managers' index for the manufacturing sector has continued its downtrend, sustaining below the 50-point threshold. The services sector, meanwhile, recorded a slight slowdown in its latest figures.

"We are worried the slowdown in the manufacturing sector has broadened and impacted the services sector," Lee added.

On world trade volume and industrial production, Lee pointed out that both have been moderating, owing to slower demand. "This is why we saw a decline in exports for regional countries, including Malaysia, recently."