Growth slowed in 2023 on softer external demand and lower commodity prices. Inflation trended downwards as government subsidies and price controls continued from 2022. Stronger growth is expected in 2024 and 2025 as global trade and the technology sector recovers. Inflation is projected to increase slightly from an increase in taxes and lower fuel subsidies. To support Malaysia's green transition, the government needs to craft a comprehensive and holistic approach to a greener economy.

Economic Performance

The challenging external environment hampered growth. Malaysia’s GDP growth slowed to 3.7% in 2023 from 8.7% in 2022. The normalization of global goods demand led to the weaker performance, which affected manufacturing. At the same time, exports fell by 7.9% amid flat growth of global trade, weaker commodity prices, and a delayed rebound of the global technology sector. Meanwhile, higher investment and solid domestic consumption underpinned economic growth in 2023 (Figure 2.26.1).

Exports contracted by 7.9% in 2023 after expanding by 14.5% in 2022. Lower demand from major trading partners and tempering of commodity prices led to the decline. All major exports contracted, including palm oil-based commodities and palm oil, petroleum, and electrical and electronic products (Figure 2.26.2). As the export contraction outpaced the decline in imports, the trade balance decreased by 11.3% in 2023.

Resilient domestic consumption kept overall growth positive. As demand for goods normalized, private consumption continued to support growth, albeit at a more moderate 4.7% pace in 2023 compared to 11.2% in 2022. Lower inflation and improved labor market conditions continued to sustain household spending in 2023. The unemployment rate fell to 3.4% in 2023 from 3.8% the previous year (Figure 2.26.3). Household spending also benefitted from several policy measures, such as continuing fuel, food, and electricity subsidies and minimum wage increases for micro-enterprises. However, as the government rationalized electricity subsidies and price controls, public consumption growth decelerated from 4.5% in 2022 to 3.9% in 2023.

This chapter was written by James Villafuerte of the Southeast Asia Department (SERD), ADB, Manila, and Mae Hyacinth Kiocho and Joyce Marie Lagac, SERD consultants.
Public investment rose by 8.6% in 2023 from 5.3% in 2022. The increase was driven primarily by higher capital outlays of public corporations and a spike in federal government development expenditures. The substantial increase in development expenditure was supported by capital spending on the Pan Borneo Highway and the East Coast Rail Line (ECRL) projects. Private investment expanded by 4.6% in 2023, lower than the 7.2% growth in 2022. Approved investments increased by 23.0% from RM267.8 billion in 2022 to RM329.5 billion in 2023. However, realized investment for the year might be lower given reduced foreign direct investment (Figure 2.26.4).

Weak external demand and a delayed recovery in the technology sector weighed down manufacturing. Manufacturing was stagnant, posting only 0.7% growth in 2023, substantially lower than the 8.1% growth in 2022 (Figure 2.26.5). After growing in 2022 by 14.2%, manufactured electrical and electronic products contracted by 1.6% in 2023.

Accelerated infrastructure projects and vibrant tourism buoyed expansion in construction and services. Construction posted the highest growth, increasing by 6.1% in 2023 compared to 5.0% in 2022. Meanwhile, resilient domestic demand for goods,
The rise came partly from increases in interbank borrowings, loans, non-resident deposits and holdings of domestic debt securities, and partly from the ringgit’s depreciation against the US dollar—foreign currency-denominated debt.

**External factors weakened the Malaysian ringgit.** The ringgit depreciated against the US dollar by 4.0% (Figure 2.26.8) by the end of 2023. It was lowest in October 2023, averaging RM4.75 per US dollar. The US Federal Reserve’s hawkish stance and the weaker-than-expected recovery of the People’s Republic of China (PRC) drove the ringgit downward.

**The fiscal position remained stable despite weaker economic growth.** The fiscal deficit narrowed to 5.0% of GDP in 2023 from 5.5% in 2022. Government revenues expanded at a slower pace of 7.0%, following the 25.9% increase in 2022. Government expenditures also increased by a more moderate 3.2% in 2023 from 18.4% in 2022 due to the removal of COVID-19 funds and lower growth in operating expenditures.

**The external current account balance continued to be in surplus in 2023.** The surplus fell to 1.2% of GDP in 2023 from 3.2% in 2022, due to a nearly 30.0% decline in the goods account. However, the services deficit continued to shrink on increased tourism receipts.

**External debt edged higher to 68.2% of GDP in 2023 from 63.9% in 2022.** The rise came partly from increased interbank borrowings, loans, non-resident deposits and holdings of domestic debt securities, and partly from the ringgit’s depreciation against the US dollar—foreign currency-denominated debt.
comprises 66.9% of total external debt. As of the end of 2023, international reserves totaled $113.5 billion, covering 5.4 months of goods and services imports.

Economic Prospects

Solid domestic spending, moderate inflation, and improved trade will drive economic prospects for 2024. Firm private consumption, lower inflation, a supportive monetary policy stance, along with the recovery of external demand, global trade, and the global technology sector support the year’s economic prospects. GDP is projected to rise by a faster 4.5% in 2024 and 4.6% in 2025 (Table 2.26.1 and Figure 2.26.9).

Domestic consumption, both private and public, will continue to support growth. Growth in private consumption is expected to revert to its long-term trend of approximately 5.0%. Stable prices, continued improvements in the labor market, and supportive policy measures will prop up consumer sentiment and spending.

<table>
<thead>
<tr>
<th>Table 2.26.1 Selected Economic Indicators, %</th>
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<tbody>
<tr>
<td>Stronger growth and relatively stable inflation are expected in 2024 and 2025.</td>
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<tr>
<td></td>
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<tr>
<td>GDP growth</td>
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<tr>
<td>Inflation</td>
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<td>GDP = gross domestic product.</td>
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<td>Sources: Department of Statistics Malaysia; Asian Development Bank estimates.</td>
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The fiscal outlook leans towards budgetary consolidation in the coming years. The 2024 budget emphasizes reforming the fiscal position to become more sustainable. In line with the Public Finance and Fiscal Responsibility Act, the government is committed to reducing the fiscal deficit to 3.0% of GDP and ensuring that debt reaches 60.0% of GDP or below within 3 to 5 years. In 2024, the aim is to reduce the fiscal deficit further to 4.3% of GDP from 5.0% in 2023. The government plans to enact fiscal reforms that strengthen the management and mobilization of revenues and reduce spending leakages.

An expanded revenue base and shift to targeted subsidies may lead to a rise in inflation. Inflation is expected to remain manageable as oil and commodity prices moderate. Nevertheless, upward pressure on prices may come from changes in tax and subsidy policies. Several measures to increase tax revenues include expanding the scope of taxable services, introducing a capital gains tax on unlisted shares and implementing a high-value goods tax. Meanwhile, temporary price controls will be lifted, and a targeted subsidy on fuel will be rolled out in the second half of 2024.

Large infrastructure investments and initiatives to restructure the economy are needed to increase growth. The continuation and acceleration of infrastructure projects, such as ongoing transport-related projects and renovations of dilapidated rural schools and clinics, will promote public investment. Other projects expected to start in 2024 include flood mitigation projects and the expansion of the Samajaya High-Tech Park in Sarawak and Tok Bali Industrial Park in Kelantan. Meanwhile, the government’s strategic initiatives require substantial investment in the private sector. These initiatives include restructuring the economy’s growth by focusing on high-value-added activities under the New Industrial Master Plan 2030, the transition to a green economy as laid out in the National Energy Transition Roadmap, and the expansion of the digital economy as presented in the MyDIGITAL initiative.

A more optimistic outlook on global trade and upcycle in the technology sector indicate a recovery in exports and a more robust manufacturing performance. After contracting from March to December 2023, exports have started to

Figure 2.26.9 Gross Domestic Product Growth

The economy is projected to thrive in 2024 and 2025.

Source: Asian Development Outlook database.
show signs of recovery, growing by 8.7% in January 2024. Manufacturing has also improved, with the manufacturing purchasing managers’ index (PMI) increasing to 49.0 in January 2024. Although still below 50.0, the index was higher at the start of 2024 compared with the 47.8 average Manufacturing PMI in 2023 (Figure 2.26.10).

**Figure 2.26.10 Manufacturing Purchasing Managers’ Index**

The manufacturing index contracted throughout 2023, but started to improve in January 2024.

![Manufacturing Purchasing Managers’ Index](image)

Note: A purchasing managers’ index reading <50 signals deterioration, >50 improvement.
Source: CEIC Data Company.

Services will remain a key contributor to growth with innovations in the retail trade and the rebound in tourism. Wholesale and retail trade growth, particularly retail, is poised to strengthen from wider use of digital transactions. Based on the Business and Economics Survey, the income of establishments from e-commerce transactions reached RM1,153.5 billion in 2023, an increase of 4.9% from 2022. Under the MyDIGITAL initiative, the government has taken steps to harness investments to develop the digital economy, aiming to expand the digital economy by 25.5% of GDP in 2025. This will increase retail digital transactions. Also, introducing environmentally friendly motor vehicle models at lower prices should expand the segment. Meanwhile, tourism arrivals are projected to increase to 27 million in 2024, higher than the pre-pandemic level (Figure 2.26.11).

**Figure 2.26.11 Tourist Arrivals**

The rise in tourist arrivals continued to support services.

![Tourist Arrivals](image)

Source: Haver Analytics.

are looking into measures aside from using the monetary policy rate to strengthen the ringgit. These include examining export proceeds, encouraging government-linked companies and investment companies to constantly revert and convert foreign investment income into ringgit, controlling overseas investments, and encouraging Malaysians to support local products and investments.

Although the prospects appear optimistic, growth remains subject to downside risks. Particularly notable are a lower-than-expected recovery of external demand, especially from the PRC, and worsening geopolitical tensions that can lead to a rise in commodity prices. On the other hand, the upsides to growth include better-than-expected consumption and tourism activities, higher spillovers of the uptrend in the technology sector, and accelerating implementation of new and existing projects.

**Policy Challenge—Advancing Green Growth**

Malaysia is committed to advancing growth sustainability and conserving natural resources. Malaysia is focused on advancing green growth, enhancing energy sustainability, and transforming its water sector. It has adopted a whole-of-nation approach to pursue green growth, an inclusive way for all stakeholders to share responsibility and accountability in implementing a clean, green, and resilient agenda. Energy sustainability will be supported by an adequate
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supply of energy resources, infrastructure, and renewable energy as alternative energy sources to complement energy efficiency measures. Adopting Integrated Water Resource Management (IWRM) is key to achieving Malaysia’s long-term goal to increase water management efficiency and generate greater employment in the water sector.

In energy, the government has pledged to phase out coal-fired power plants and increase the share of renewable energy to 70% of installed capacity by 2050 to achieve net-zero. In 2020, the total national installed capacity from renewables increased to 23%. Numerous initiatives support the shift to renewables. The Green Investment Tax Allowance grants companies allowances to adopt renewable energy in their operations and upgrade their energy efficiency. The Green Income Tax Exemption offers generous tax cuts for companies providing services related to green technology activities. The Green Electricity Tariff allows consumers to reduce their carbon footprint by using electricity from renewable energy. Institutional and financing capacities were also strengthened to support the green agenda.

To improve the coordination between stakeholders, the Climate Governance Malaysia was set up in 2019 and the Malaysia Climate Action Council was established in 2020. In 2019, BNM and the Securities Commission coordinated a collective financial sector response to climate risks and improve climate-related financing opportunities in capital and financial markets. Malaysia also established the Sustainable Development Financing Fund and Public Transport Fund to support sustainable development initiatives. In addition, the Amanah Lestari Alam was established in 2020 to increase awareness and change behavior concerning the environment through long-term, inter-generational and education-focused initiatives.

Despite ongoing progress, several challenges remain to accelerate Malaysia’s transition to a green economy. The unsustainable consumption and production practices of Malaysia’s economy use resources inefficiently. The large volume of waste generated from economic activities damages the environment and results in expensive clean-up and mitigation measures. To support and finance the transition, Malaysia requires considerable investment. According to the National Energy Transition Roadmap, an estimated RM1.3 trillion ($280 billion) of investments is needed for Malaysia’s energy transition.

Malaysia must increase access to sustainability-related education and public awareness on green issues. In a recent survey conducted by The Economist magazine (2023), only 15% of employees in Malaysia consider green skills to be important. Employees have also reported that a lack of time and the high cost of courses are key barriers to acquiring green skills. The fragmentation, inaccessibility, and insufficient data quality have hindered comprehensive data analysis to support evidenced-based risk-informed decision-making processes.

Malaysia is committed to fostering the development of a clean and efficient economy. However, governance-related issues need to be addressed, including limited enforcement capacity, inadequate monitoring, reporting, and evaluation. These are key barriers to accelerate Malaysia’s transition toward a green economy. It is imperative to create an enabling environment for the circular economy and more sustainable and responsible businesses, particularly micro, small, and medium-sized enterprises.