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Industrial production in focus

Domestic-oriented industries likely to get solid backing

ECONOMY

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PETALING JAYA: Budget 2024 could see Putrajaya unveiling measures to lend further support for domestic-oriented industries, as the trend for weak exports continues to hold sway due to global headwinds, predicts economists.

The forecast comes in tandem with the 0.3% year-on-year (y-o-y) dip in Malaysia's Industrial Production Index (IPI) for August released by the Statistics Department yesterday.

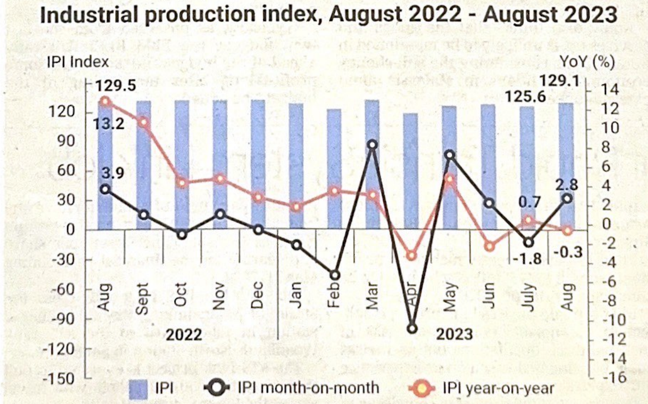
This underlines the theme of declining manufacturing production from export-oriented industries, while domestic-focused sectors continued to expand.

Chief statistician Datuk Seri Mohd Uzir Mahidin said the decline in August's IPI y-o-y was attributed by a 0.6% contraction in the manufacturing sector compared with the smaller 0.2% slowdown registered in the previous month.

On the other hand, the monthly variability in industrial production offered a silver lining, as August's IPI saw a month-on-month (m-o-m) growth of 2.8% against the 1.8% contraction recorded in July.

Malaysia University of Science and Technology Economics professor Geoffrey Williams opined that the IPI data confirms the trend that has been seen for 12 months of slower y-o-y growth.

Industrial production index, August 2022 - August 2023



"The m-o-m data shows more volatility, but has also been basically flat for 12 months on average. Any months of positive growth have been offset by other months of contraction," he observed.

More importantly, Williams said the stubborn "weak exports, strong domestic demand" trend has been part of the global headwinds discussion, and as such, it will place more emphasis for the government in Budget 2024 on the need to support domestic demand and subsequently, to increase public spending.

Shedding more information on the numbers, Mohd Uzir commented that the deterioration in manufacturing output was primarily influenced by the continuous decline in export-oriented industries, which dropped by 2.6% y-o-y in August, following a 2.7% dip in the previous month.

The contraction was mainly due to decreases in the manufacture of coke and refined petroleum products, as well as the manufacture of computer, electronics and optical products, he noted.

"These declines mirrored the country's export performance, which had been trending down since March 2023 and recorded an 18.6% decrease in August 2023," Mohd Uzir added.

Of interest, Williams pointed out that the weakening of the ringgit over the past three months was likely to have supported exports to an extent as Malaysian products would have been less costly for external purchasers.

"It looks likely that the IPI would have been in full contraction without the ringgit depreciation effect, which means ironically the falling ringgit has helped to mitigate the IPI softening.

"This is exactly what a floating exchange rate is supposed to do," he said.

Looking further ahead, Williams told *StarBiz* that the current persistent situation continues to throw up an opportunity for domestic industries to gain market share as imports are more costly, while foreseeing that these sectors will continue to support the Malaysian economy for as long as the global economy is weak.

Williams, who had previously expected improvements in the export market in 2024, said the recently erupted conflict in the Middle East has added a whole new level of risk to the geopolitical scenario.

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Local-oriented industries continue to expand

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Reinforcing the point of domestic demand support, chief statistician Mohd Uzir highlighted that local-oriented industries continued to expand in August, albeit at a more moderate rate of 4.2% y-o-y as compared to the 6.0% posted in July.

He revealed: "The increase was spearheaded by the manufacture of fabricated metal products and the manufacture of food processing products.

"In comparison with the preceding month, the production of the manufacturing sector rebounded to 5.1% m-o-m as against the weakening of 4.3% registered in July 2023."

On top of that, Mohd Uzir said the output in the mining sector also grew marginally by 0.1% y-o-y in August, although it was significantly below the 4.2% posted in July, while noting that the increase was propelled by a 2.6% upward momentum in natural gas production during the month.

"In contrast, crude oil and condensate output declined by 3.3% after a strong growth of 11.8% recorded in July 2023. As compared to the previous month, the mining index dropped by 5.4% relative to the positive 8.0% we saw in July 2023," he said.

Similarly, Mohd Uzir said electricity output advanced further by 1.9% y-o-y in August, following a 1.5% growth in the previous month.

On a m-o-m basis, the electricity index grew 0.3%, slowing to a fraction of the 1.8% recorded in July.

Meanwhile, economist with Coface Services South Asia-Pacific Pte Ltd, Eve Barre, is of the view that the IPI has actually posted two consecutive months – namely July and August – of positive growth both on an annual and a monthly basis, driven by the manufacturing sector.

"While still boosted by domestic-oriented segments, the manufacturing industry has started to benefit from signs that the downturns in export-driven segments – notably electronics – may be bottoming.

This was reflected by August trade data, which showed that exports declined to a lesser extent during the month.

While acknowledging that this is encouraging and confirms her expectations on potential better trade prospects for Malaysia in the second half of this year, this does not mean that manufacturing is set to strongly rebound in the coming months.

She said this is because global growth prospects, in particular in the United States and China – two of Malaysia's major trade partners – remains poor, with recession risk in the former.

On a separate note, Williams believes that to further improve industrial productivity, the tabling of Budget 2024 today could introduce changes in the labour market to increase value-added to working.

He commented that this can be enhanced significantly by incentives to promote flexible working arrangements such as working from home, freelancing, gig-economy activities as well as investment in technology without cutting jobs.

Concurrently, Coface's Barre is hoping the budget could allocate more resources to education to boost the productivity.

She believes that the government – having highlighted the need for automation and digitalisation of the economy – may have financial incentives and training programmes for businesses to enter these processes.

"Also, Prime Minister Datuk Seri Anwar Ibrahim is likely to give more details on the progressive wages scheme, that was approved earlier this year, and that is meant to increase labor productivity," she said.