FMM Business Conditions Survey

RESILIENCE AMIDST COMPLEXITY IN 1H2024, POSITIVE YET PRAGMATIC OUTLOOK IN 2H2024

Issue No. 2/2024 **Released on September 2, 2024**

KEY RESULTS:	
BUSINESS ACTIVITY – 1H2024	• Business conditions improve modestly in 1H2024 • Domestic sales slow down, export sales pick up • Production volume steady, capacity utilisation improves • Cost of production remains high, employment steady • Capital investment trends up
BUSINESS ACTIVITY – OUTLOOK 2H2024	• Business conditions to improve further • Higher local sales and export sales expected • Favourable domestic and external demand to drive output and capacity utilisation • Capital investment to gain momentum • Costlier production and steady employment expected
GENERAL BUSINESS ACTIVITY – OUTLOOK 2H2024	• Revenue and profit growth in 2024 vs 2023: cautious optimism • 50% and 42% expect higher revenue and profits in 2024, respectively • Business confidence outlook: cautious yet optimistic, balanced by concerns over potential economic challenges • Top 5 challenges to business operations and growth in 2H2024: weak demand, rising input costs, ringgit depreciation, increasing competition, expansion of customer base and geopolitical risks • Top 5 opportunities to business operations and growth in 2H2024: expansion of product portfolio, export diversification, value-chain opportunities associated with ESG targets, leverage on digital transformation and rebound in activity
GENERAL	• 57% support a moderate increase in the minimum wage to RM1,600 • Cautious investment in automation in the last 5 years: higher investment in hardware automation compared to software automation • 68% of respondents interested in transforming their operations into smart factories • 36% of respondents expect the Ringgit exchange rate against the US Dollar at 4.5 and 4.55 by year end 2024 • 6% service tax on logistics increase manufacturing costs of 90% of respondents • 88% of respondents not involved in government procurement • Budget 2025 top 5 key priorities: corporate tax reduction, tax and ESG incentives, talent development, energy cost control and reintroduction of GST

The Malaysian manufacturing sector has delivered a commendable performance in the first half of 2024, showcasing resilience in a challenging global environment. Despite facing headwinds such as inflationary pressures, volatile demand and global uncertainties, the sector has managed to sustain stability. Manufacturers have maintained production volumes, increased capacity utilisation and strategically managed costs, while also keeping employment levels stable. These outcomes suggest a broader trend: Manufacturers are not merely responding to external pressures but are actively positioning themselves to shape their future in a competitive global landscape.

Looking ahead to the second half of 2024, the sector is poised for continued growth, bolstered by a global economic recovery and supportive domestic policies. Key metrics, including business activity and production volumes, indicate robust momentum. Manufacturers are gearing up to meet rising demand, both domestically and internationally. However, the sector remains cognisant of rising production costs and is taking a measured approach to workforce expansion. This reflects a balanced strategy, combining optimism with prudent risk management as the sector navigates the complexities of a dynamic global economy.

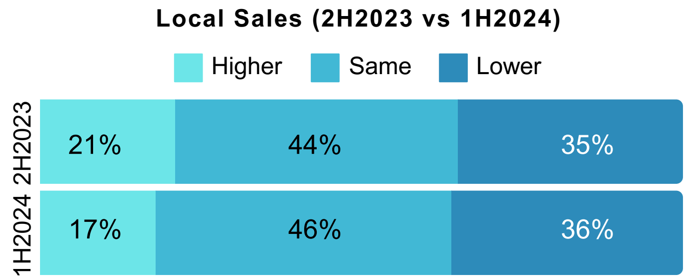
Indicators	FMM Business Conditions Index Values							
	Current (Compared to 6 months ago)				Looking forward (Next 6 months)			
	2H2022	1H2023	2H2023	1H2024	1H2023	2H2023	1H2024	2H2024
Business conditions	107	66	89	**93**	92	86	92	**106**
Local sales	98	71	86	**81**	91	81	92	**95**
Export sales	91	66	80	**85**	84	88	89	**100**
Production volume	102	69	91	**91**	97	86	99	**110**
Capacity utilisation	99	68	91	**93**	94	87	99	**108**
Capital investment	104	95	103	**107**	112	100	110	**116**
Number of employees	112	101	98	**98**	113	101	105	**105**
Cost of production	166	157	154	**155**	166	148	159	**162**

BUSINESS CONDITIONS IMPROVE FURTHER

The current general business activity index increased by 4.49% in the first half of 2024, reflecting continued stability and improving sentiment within the manufacturing sector. From 89 points in 2H2023 to 93 in 1H2024, this is the Index's second consecutive increase since 1H2023. While 26% of the 616 respondents reportedly enjoyed higher sales in 1H2024, sales have remained steady for another 42% of the respondents.This moderate growth can be attributed to steady demand from abroad, despite global economic uncertainties. Respondents are adapting to ongoing challenges such as inflation and higher interest rates, maintaining a cautious yet optimistic approach to business operations.

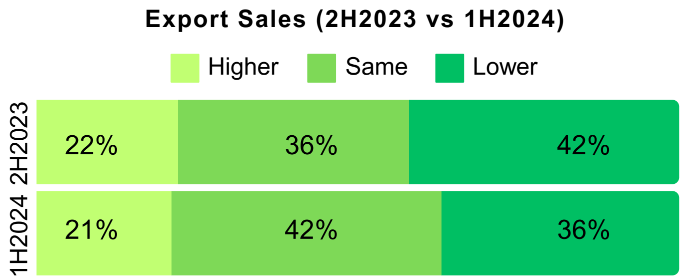
Local Sales Slow Down

The latest local sales index declined 5.81% to 81 from 86 previously, indicating weaker domestic demand in 1H2024. 17% of the respondents sold more in 1H2024, down from 21% in 2H2023. Rising inflation and the increased cost of living have dampened consumer spending, while higher borrowing costs have further constrained purchasing power. These factors have likely led to a decrease in local sales, as consumers prioritise essential goods over discretionary purchases.



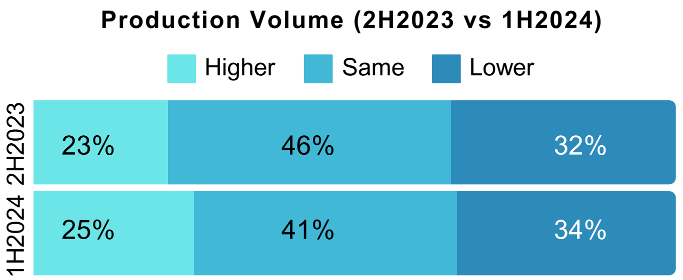
Export Sales Trend Higher

In contrast, the current export sales index rose five points from 2H2023 to 85 in 1H2024, driven by favourable demand from international markets. Malaysian manufacturers have benefited from a recovering, albeit uncertain, global economy, particularly in key export sectors such as electronics and electrical products. Stable exchange rates and improved access to global markets through trade agreements have likely supported this growth, highlighting the sector's resilience in the face of global economic challenges.



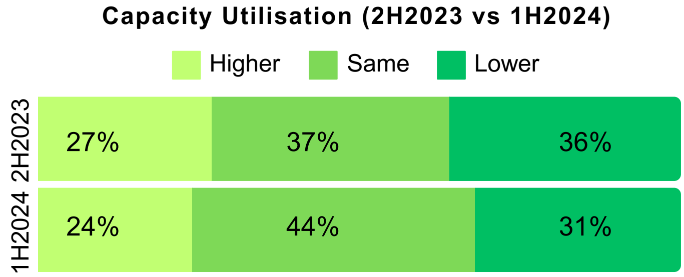
Production Volume Steady

The latest production volume index, at 91, remained unchanged in the first six months of 2024, indicating that respondents have maintained consistent output levels. This stability reflects a balanced approach to managing production capacity in line with demand. Respondents are likely optimising their production processes and inventory management, ensuring that output meets current market needs without overextending resources.



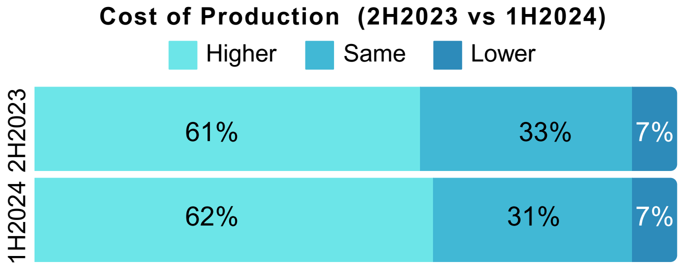
Capacity Utilisation Up

The current capacity utilisation index rose two points to 93 in 1H2024, suggesting that respondents are using their production capabilities more efficiently. The rise in capacity utilisation is likely driven by steady demand, particularly from export markets, and ongoing investments in technology and energy-efficient practices. Respondents are likely focusing on maximising the productivity of their existing facilities, even as they face economic pressures such as rising costs.



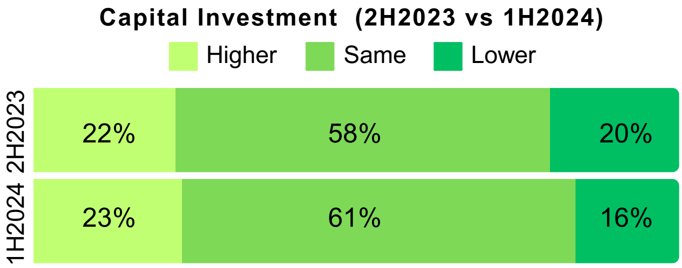
Cost of Production Remains High

The current cost of production index picked up a point to stand at 155 in 1H2024, reflecting ongoing inflationary pressures. Rising raw material and energy costs, coupled with higher wages, may have contributed to this modest rise. Despite these challenges, respondents are likely controlling costs through efficiency improvements and strategic investments in technology, helping to limit the overall increase in production expenses.



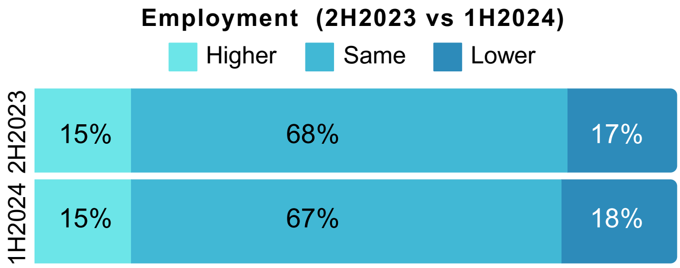
Capital Investment Increases

The latest capital investment index rose four points to 107 in 1H2024, indicating continued confidence in the sector's growth prospects. 23% of the respondents increased their capital investment (CAPEX) recently, while 61% have maintained theirs in 1H2024, up from 22% and 58% in 2H2023, respectively. Respondents may be investing in advanced technologies, automation and energy-efficient infrastructure to enhance productivity and competitiveness. This rise in capital investment, despite higher borrowing costs, underscores the sector's commitment to long-term growth and modernisation.



Employment Stable

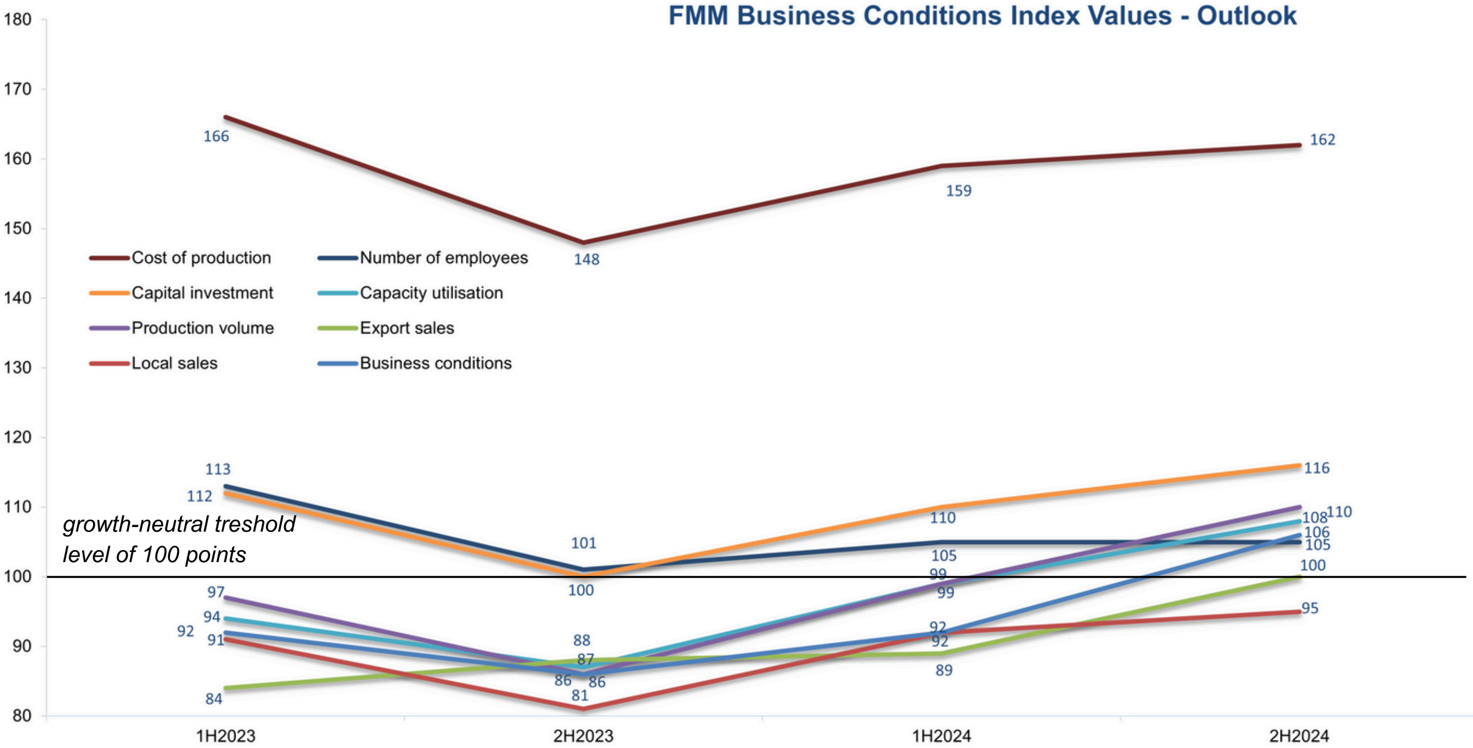
The current employment index remained stable at 98, with no change in employment levels in 1H2024. As in 2H2023, 15% of the respondents have also increased their headcount in 1H2024. With 67% of the respondents putting hiring and retrenchment on hold for now, they are clearly prioritising employee retention and, likely, training, ensuring that their workforce is equipped to handle advanced technologies and maintain productivity without significant workforce expansion.



POSITIVE BUT PRAGMATIC OUTLOOK FOR 2H2024

As the Malaysian manufacturing sector approaches 2H2024, optimism grows, driven by global economic recovery and supportive government initiatives. Key indicators, including business activity and production volumes, point to strong growth as respondents gear up to meet rising demand locally and globally. However, rising production costs and a cautious approach to workforce expansion highlight the challenges that remain as the sector continues to manage a complex global and domestic terrain.

The expected general business activity Index rose significantly from 92 to 106, reflecting increased confidence among respondents. This optimism is driven by global economic recovery, particularly in key export markets like the U.S. and Europe, as well as supportive domestic policies that are fostering industrial growth. 29% of the respondents replied positively, while 23% were negative, compared to 23% and 31% in the prior survey, respectively.



The expected local sales index saw a modest increase from 92 to 95, indicating cautious optimism about domestic demand. 22% of the respondents are anticipating higher sales in the coming months, up from 20% previously. This rise is underpinned by a recovering domestic economy and improved consumer confidence.

The expected export sales index jumped from 89 to 100, highlighting strong expectations for international demand. Factors such as a recovery in global markets and Malaysia's strategic trade agreements may have bolstered respondents' confidence in their export prospects. 26% and 27% are looking forward to higher and lower sales abroad in 2H2024, respectively, compared to the previous survey's 24% and 36%, respectively.

The expected production volume index increased from 99 to 110, reflecting respondents' plans to ramp up production in response to rising demand. Higher production volume is in the pipeline for 32% of the respondents for 2H2024, up from 28% previously. Improved global supply chains, increased capital investment and a favourable economic outlook are likely the key drivers behind this growth.

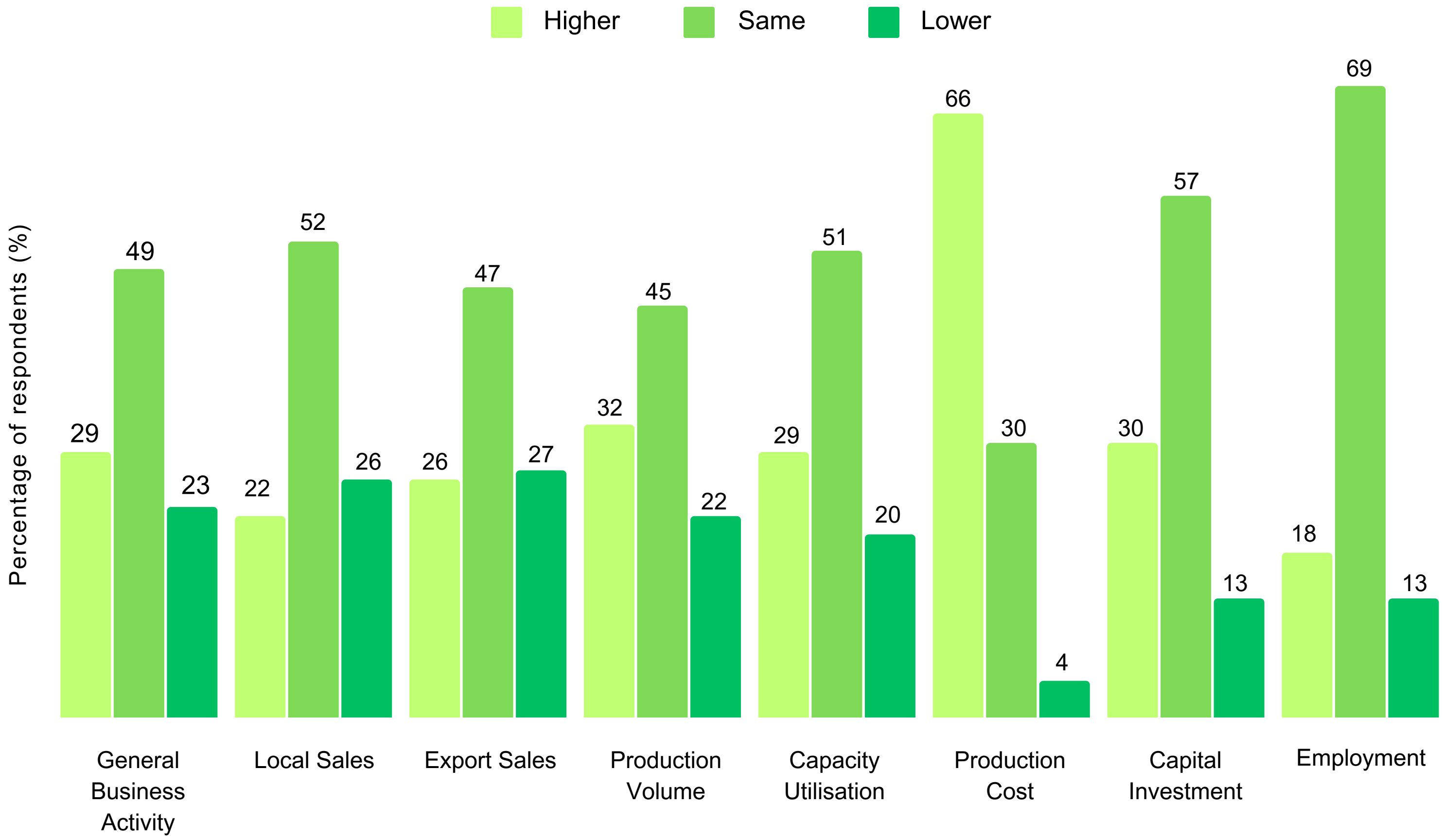
The expected capacity utilisation index rose from 99 to 108, indicating that respondents expect to operate closer to full capacity. This increase is linked to stronger demand, especially from abroad, as well as technological advancements that are enhancing production efficiency. While 29% are planning to increase their capacities sometime soon, 20% are planning to reduce theirs, compared to 26% and 28% previously, respectively.

The expected cost of production index increased slightly from 159 to 162, reflecting ongoing inflationary pressures. Rising costs for raw materials, energy and labour continue to challenge respondents, although the rate of increase has moderated somewhat due to stabilising supply chains. The increase is anticipated by 66% of the respondents in 2H2024, up marginally from 65% in the previous survey.

The expected capital investment index climbed from 110 to 116, showing respondents' commitment to expanding their production capabilities. With 30% of the respondents divulging plans to increase their CAPEX in the coming months, this rise is likely driven by a positive economic outlook, government incentives and the need to adopt new technologies to stay competitive.

The expected employment index remained stable at 105, indicating that respondents do not anticipate significant changes in workforce levels. This stability suggests a focus on productivity improvements and cost management rather than expanding headcount, despite the sector's overall positive outlook. 18% are planning to increase their workforce soon, while 69% will retain theirs and 13% are contemplating retrenchment, compared to 20%, 64% and 16% previously, respectively.

2H2024 Outlook Performance



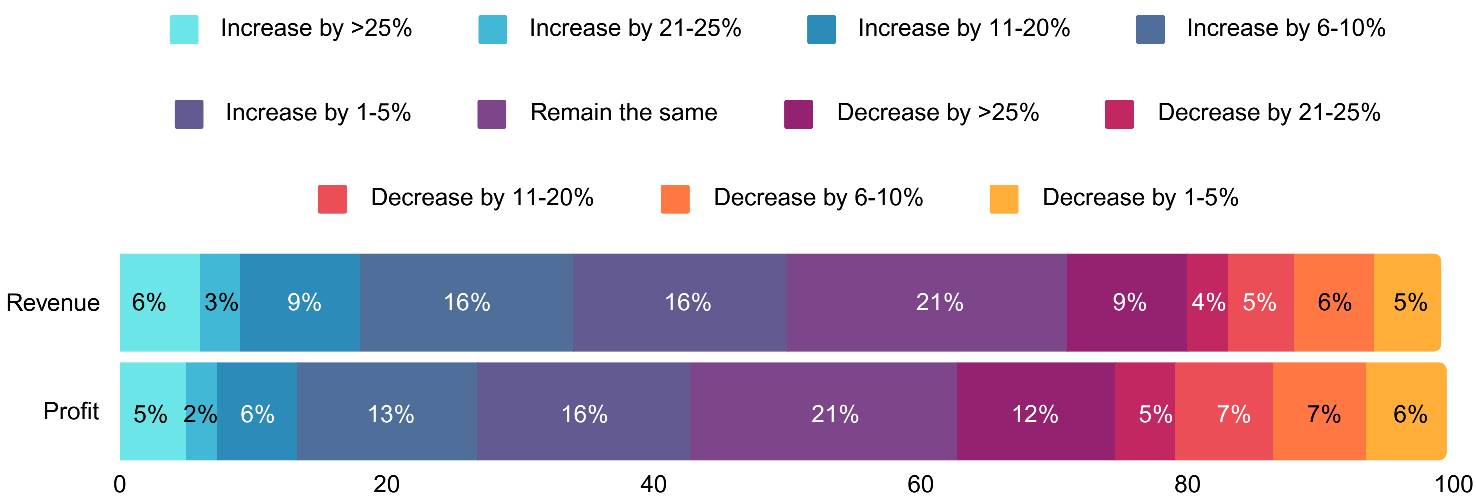
REVENUE GROWTH IN 2024 vs 2023 : MIXED OUTLOOK

Malaysian manufacturers face a mixed outlook for revenue growth in 2024, balancing optimism with caution in a challenging economic setting. Survey data indicates that 50% of respondents expect revenue growth, driven by factors such as global economic recovery and resilient domestic demand. However, 21% foresee no change, and 29% anticipate revenue declines, driven likely by concerns over rising operational costs, persistent inflation and global economic uncertainties. Notably, 9% of respondents expect significant revenue declines, particularly in export-dependent and struggling sectors.

PROFIT GROWTH IN 2024 vs 2023: CAUTIOUS OPTIMISM AMID RISING COSTS

In 2024, Malaysian manufacturers express cautious optimism about profit growth, tempered by rising costs and market volatility. Survey results show that 42% of respondents expect profit increases, supported by global economic recovery and operational efficiency improvements. However, 21% anticipate no change in profits, while 37% foresee declines, including 12% who predict a significant drop of more than 25%. These concerns are likely driven by escalating input costs, market volatility and sector-specific challenges.

Expectations on Revenue and Profit Growth for 2024



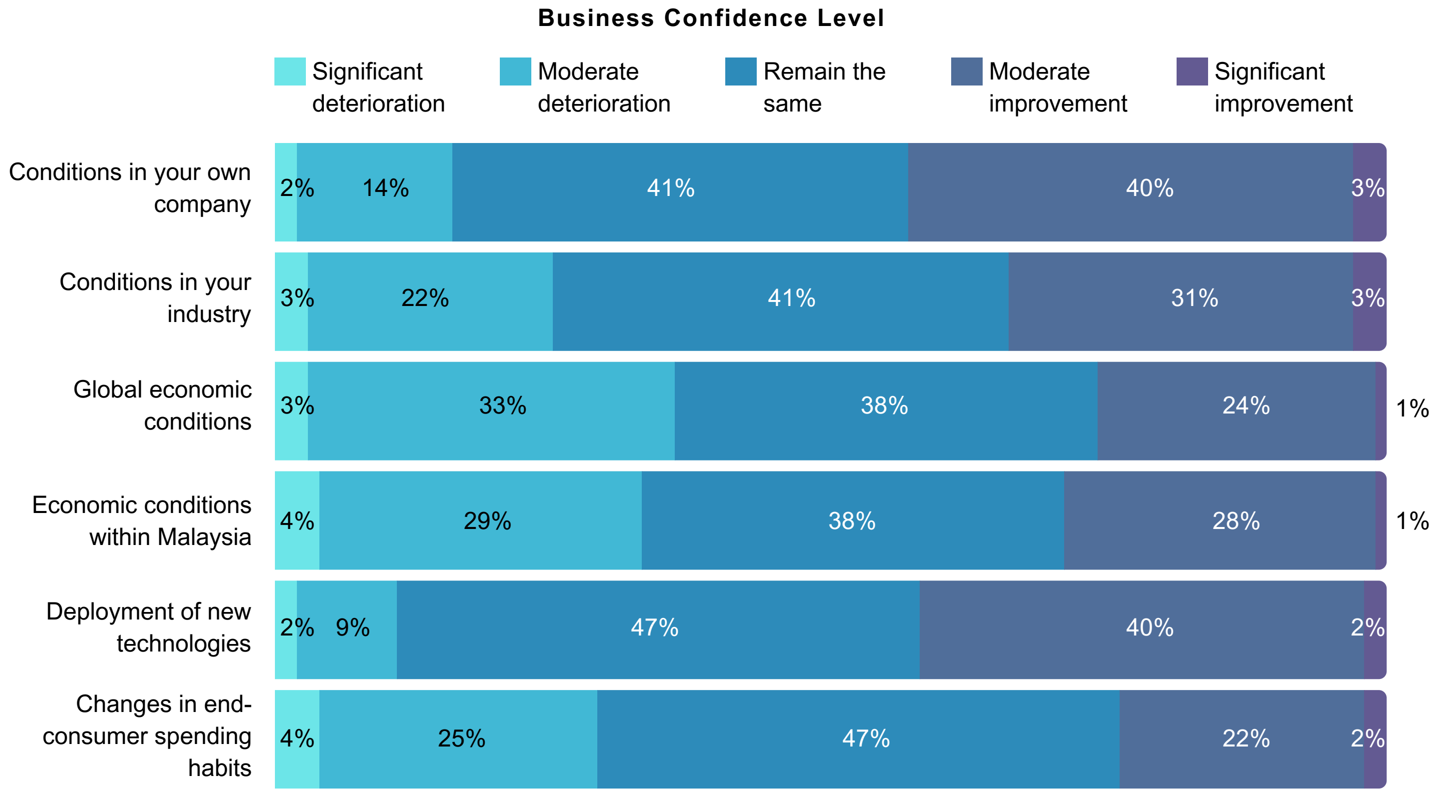
BUSINESS CONFIDENCE LEVEL IN 2024

The survey results reveal a cautious yet optimistic outlook among Malaysian manufacturers as they navigate 2024. Key focus areas included company-specific conditions, industry dynamics, and broader economic indicators, both domestic and global. The prevailing sentiment reflects a preference for stability, underscored by concerns about potential economic headwinds.

While 41% expect stability in company conditions, 40% anticipate moderate improvement, and 14% foresee moderate deterioration. Only 3% predict significant improvements, reflecting a conservative outlook. Industry expectations are similarly reserved, with 41% of respondents expecting industry conditions to remain unchanged and 31% anticipating moderate improvements. On the downside, 22% predict moderate deterioration, signaling concerns over sector volatility.

The global economic outlook is a point of concern. A notable 33% of respondents anticipate moderate deterioration, contrasted with a mere 1% expecting significant improvement. Stability remains the expectation for 38%, reflecting uncertainty in the global environment. The domestic economic forecast shows a balanced view. While 38% expect stability, 29% foresee moderate deterioration, and 28% anticipate moderate improvement, but significant gains are not widely expected.

There is cautious optimism regarding technology deployment, with 40% predicting moderate improvements and 47% expecting no major changes. Consumer spending, however, remains a concern, with 25% expecting moderate deterioration, 47% anticipating stability and 22% foreseeing moderate improvements.



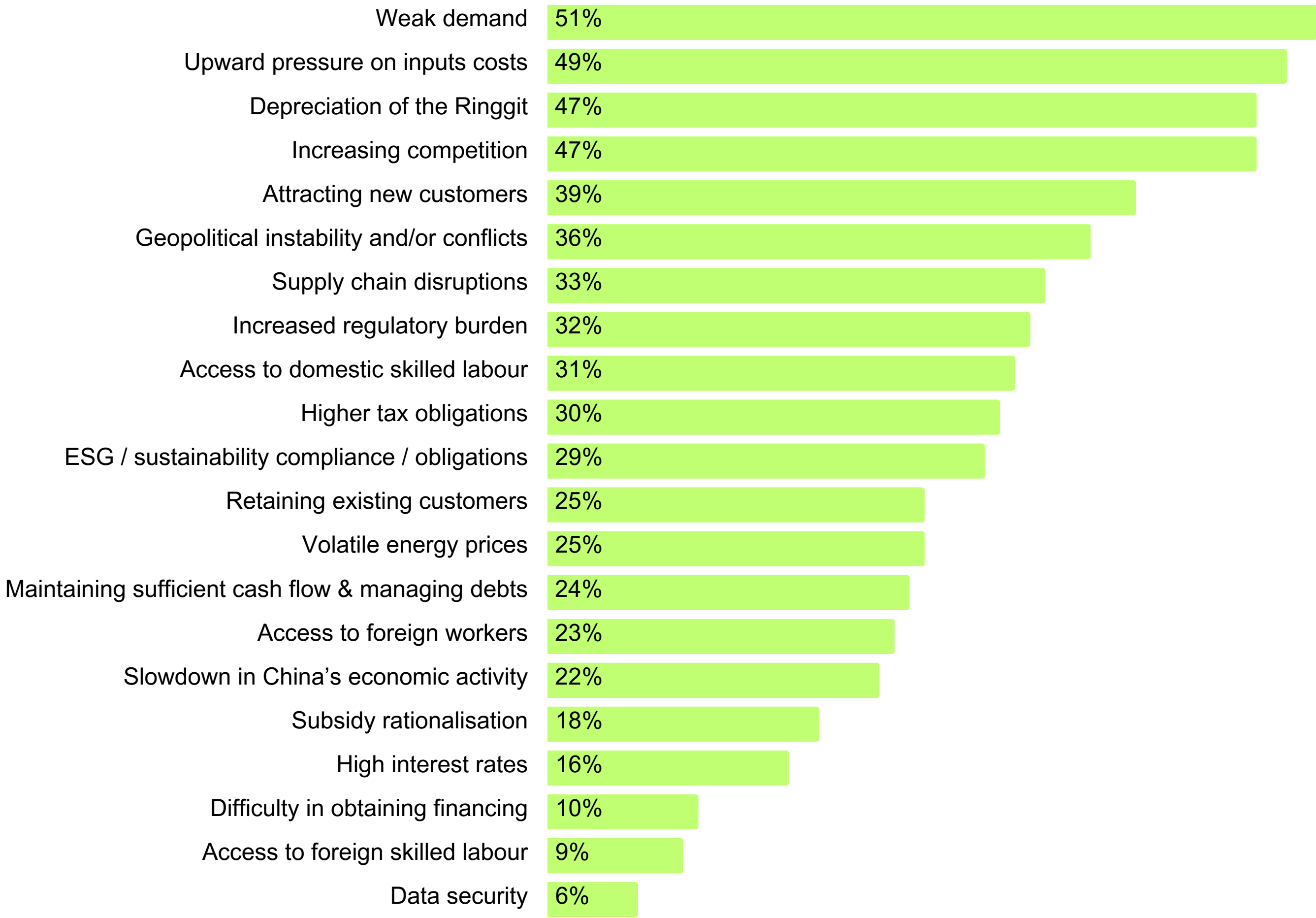
CHALLENGES TO BUSINESS OPERATIONS AND GROWTH

The top five challenges to business operations and growth in 2H2024 include weak demand, rising input costs, ringgit depreciation, increasing competition, expansion of the customer base and geopolitical risks. Weak demand tops the list of concerns for 51% of respondents, reflecting the slow recovery of the economy amidst inflationary pressures, rising interest rates and cautious consumer behaviour. Global factors, such as uneven economic growth and fears of potential recessions in major economies, could further exacerbate these challenges.

Upward pressure on input costs, driven by global supply chain disruptions, energy price hikes and raw material shortages, is a critical issue for 49% of respondents. Local factors such as labour shortages and costs further complicate the cost structure. The depreciation of the Ringgit is a significant challenge for 47% of respondents.The competitive landscape is tightening, with 47% of respondents concerned about increasing competition, particularly in the context of digitalisation and the global pivot towards sustainability.

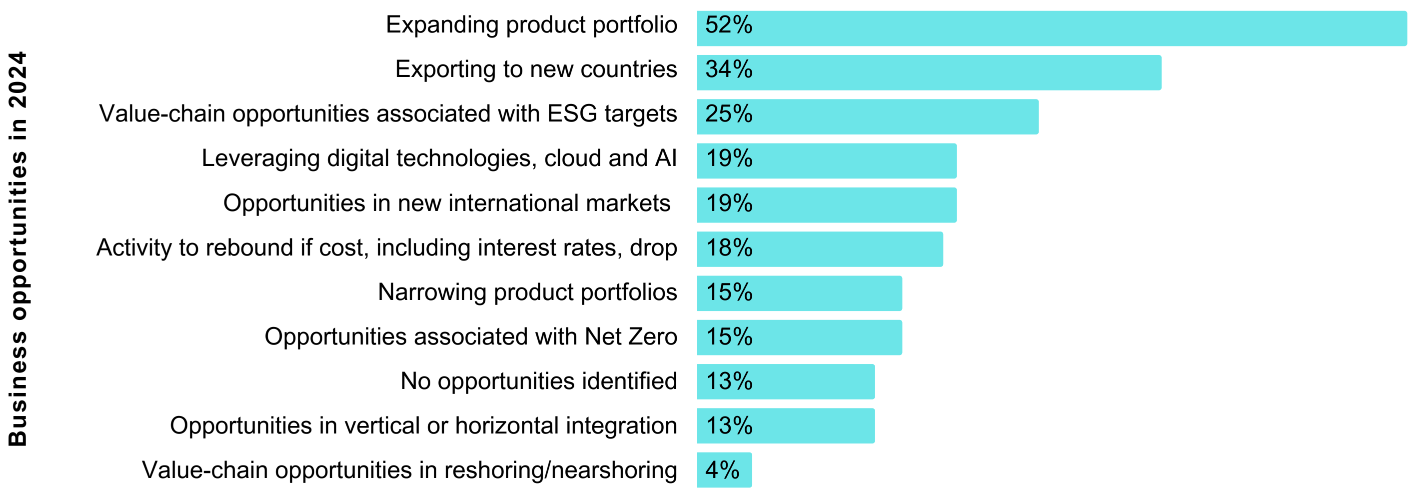
Attracting new customers is challenging for 39% of businesses, as inflationary pressures and global economic uncertainties dampen consumer confidence and demand. Geopolitical instability, highlighted by 36% of respondents, remains a significant concern. Ongoing conflicts and rising tensions in key regions could threaten global trade and supply chains, posing risks to Malaysia's key export sectors.

Challenges to Business Operations and Growth



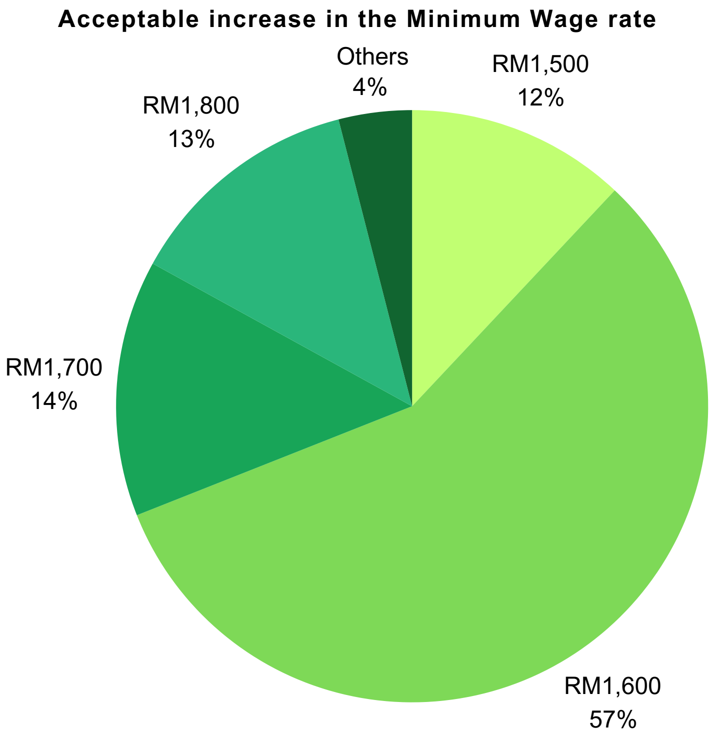
BIGGEST BUSINESS OPPORTUNITIES IN 2024

Going into 2H2024, businesses are poised to capitalise on opportunities by expanding product portfolios and exploring new markets. Identified by 52% of respondents, expanding product portfolios is seen as a key strategy to capture new customer segments and hedge against market volatility. With 34% of businesses aiming to export to new countries, export diversification is critical in navigating global economic uncertainties. ESG initiatives are gaining traction, with 25% of companies recognising value-chain opportunities tied to sustainability trends. Continued investment in digital transformation, particularly AI and cloud technologies, is a priority for 19% of respondents, while another 19% believe there are opportunities in new international markets and 18% anticipate a rebound in activity if costs decrease spurring investment and consumer spending.



MINIMUM WAGE

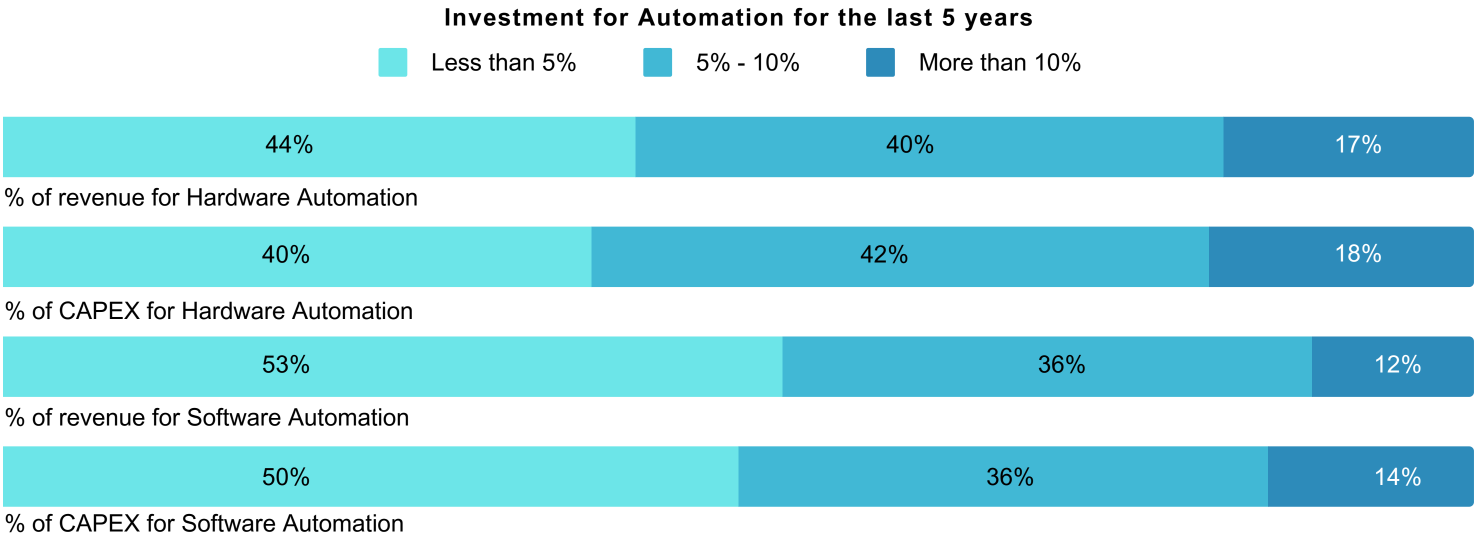
The survey reveals that a majority of respondents (57%) support an increase in the minimum wage to RM1600, reflecting a consensus that a modest rise is manageable and aligns with current economic conditions. However, support for higher increases is limited, with only 14% and 13% favouring hikes to RM1700 and RM1800, respectively, due to concerns about rising operational costs and competitiveness.



INVESTMENT IN AUTOMATION FOR THE LAST 5 YEARS

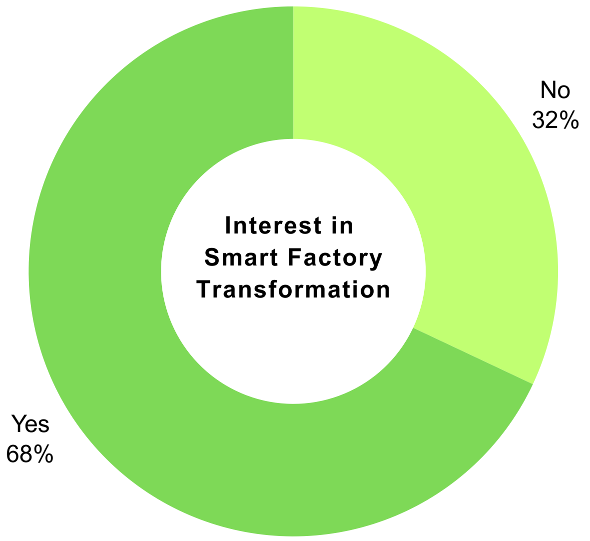
Over the past five years, businesses have cautiously invested in automation, focusing more on hardware than software. 44% of respondents invested less than 5% of their revenue in hardware automation, indicating early-stage adoption driven by cost concerns. Meanwhile, 40% allocated 5%-10% of their revenue, reflecting a balanced approach, and 17% invested more than 10%, viewing automation as critical for competitiveness. In terms of capital expenditure (CAPEX), similar patterns emerged, with 40% investing less than 5% and 42% investing 5%-10% in hardware automation.

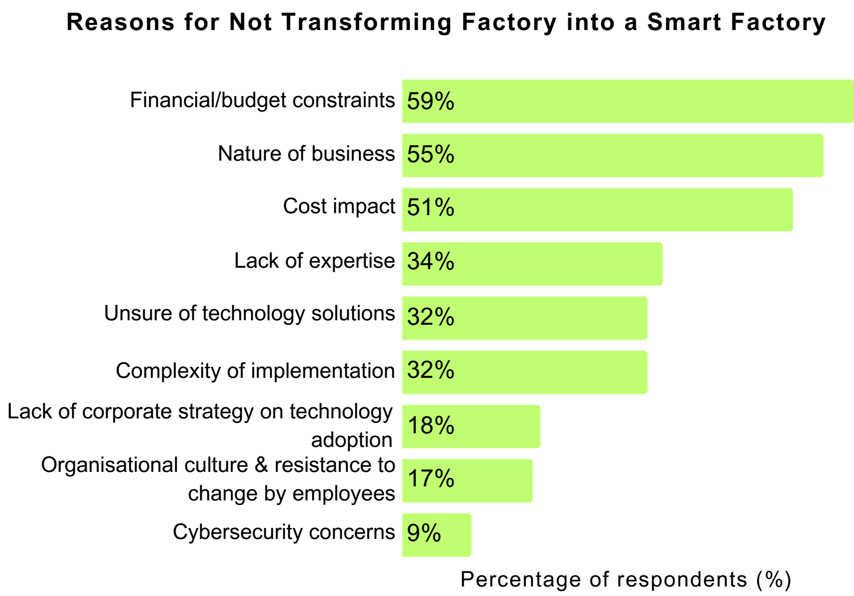
In contrast, software automation received less attention, with 53% dedicating less than 5% of their revenue, 36% investing 5%-10%, and only 12% investing more than 10%. The cautious approach to software automation, is also reflected in CAPEX allocations, with 50% allocating less than 5% of their CAPEX to software automation. Similar to revenue-based investments, 36% invested 5%-10%, while only 14% dedicated more than 10% of their CAPEX to software automation, indicating that extensive investment in digital tools is still relatively uncommon, possibly due to perceived complexities or high upfront costs.



TRANSFORMING TO SMART FACTORY

There is significant interest in smart factory transformation, with 68% of businesses expressing a positive response. However, 32% are not interested, mainly due to financial constraints (59%) and concerns about the overall cost impact (51%). These barriers include not just initial investments but ongoing costs for maintenance, training, and technology updates. Additionally, 55% cited the nature of their business as incompatible with smart factory technologies, while 32% are uncertain about which technologies to adopt. This hesitation reflects a knowledge gap and concerns about the return on investment. To encourage broader adoption, businesses may need financial support, clearer industry-specific guidelines, and examples of successful implementations to help overcome these challenges. Addressing these concerns could pave the way for more widespread adoption of smart factory technologies, helping companies enhance efficiency and competitiveness in an increasingly digital world.

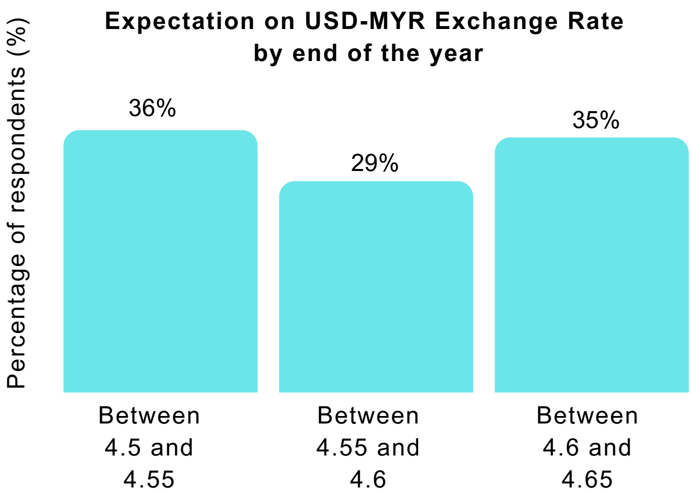


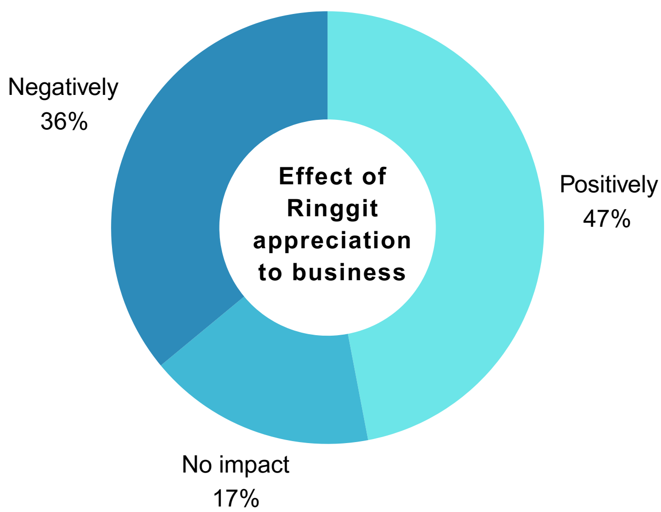


RINGGIT EXCHANGE RATE

In 2024, Malaysia's businesses are closely monitoring the Ringgit's movement against the US Dollar amidst a complex global economic environment marked by fluctuating commodity prices, geopolitical tensions, and shifts in global monetary policy. Survey results show that 36% of respondents expect the Ringgit's exchange rate to be between 4.5 and 4.55 by year-end, while 29% predict it to be between 4.55 and 4.6 and 35% anticipate a rate between 4.6 and 4.65. The cautious outlook reflects domestic challenges, including inflationary pressures and volatile oil prices, alongside global uncertainties.

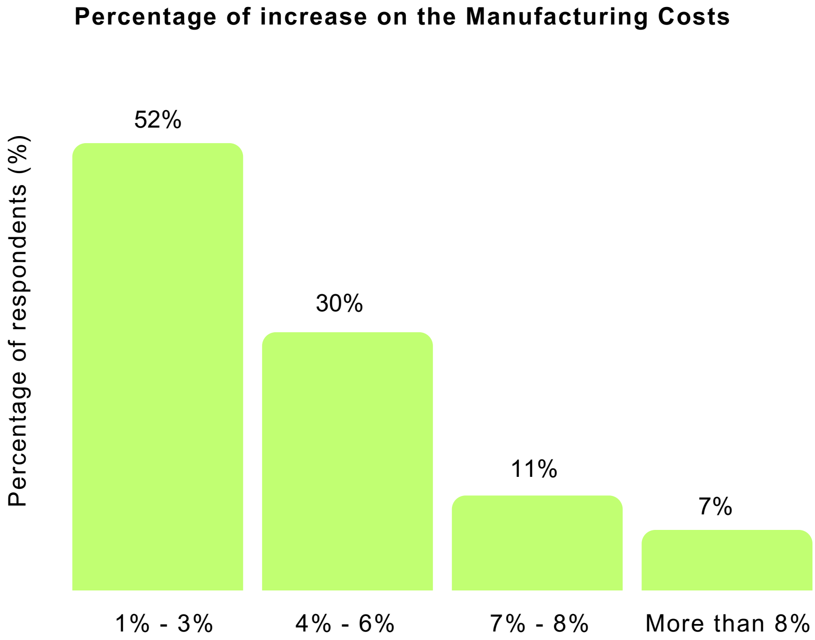
On how the Ringgit appreciation would affect businesses, a significant portion of respondents (47%) view Ringgit appreciation positively, which could imply that these businesses benefit from stronger domestic purchasing power or reduced import costs. 36% anticipate a negative impact, possibly due to reduced export competitiveness or other factors like higher costs in Ringgit for businesses relying on export sales. The 17% who foresee no impact might be involved in sectors that are less sensitive to currency fluctuations.





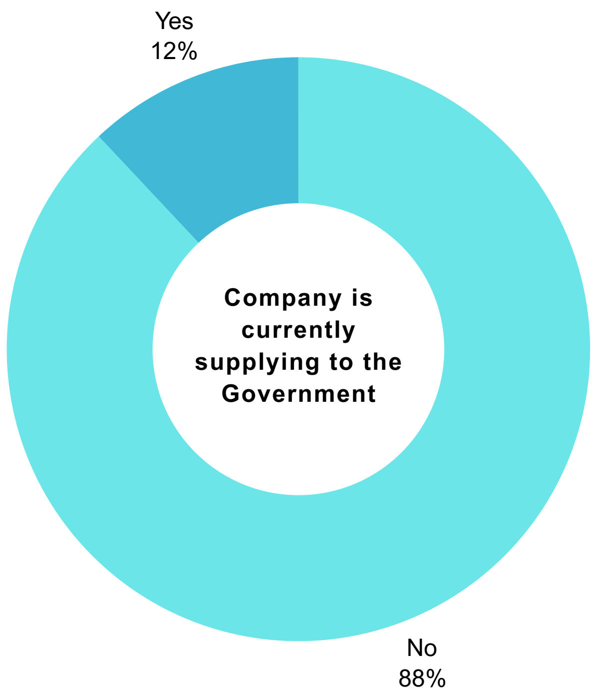
SERVICE TAX ON LOGISTICS

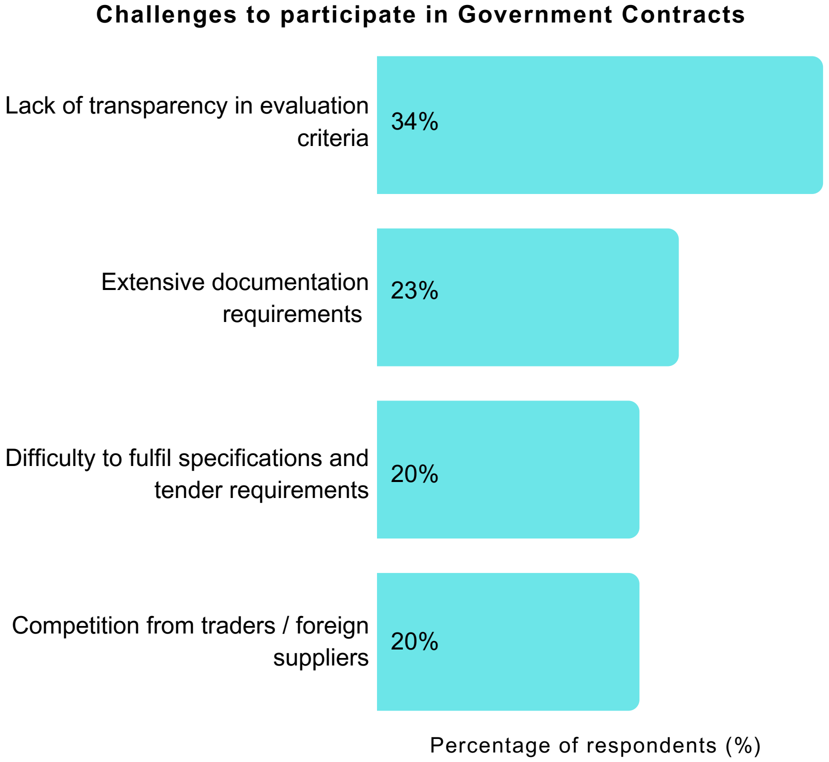
The implementation of the 6% service tax on logistics has significantly impacted manufacturing costs, with 90% of respondents reporting an increase. For 52% of these respondents, the cost rise was between 1%-3%, suggesting the tax is manageable for many. However, 30% experienced a 4%-6% increase, indicating a more substantial impact on logistics reliant businesses. Additionally, 18% reported a cost increase of 7% or more, likely affecting companies heavily dependent on logistics services or those with thinner margins, where even a small tax increase has a disproportionate effect.



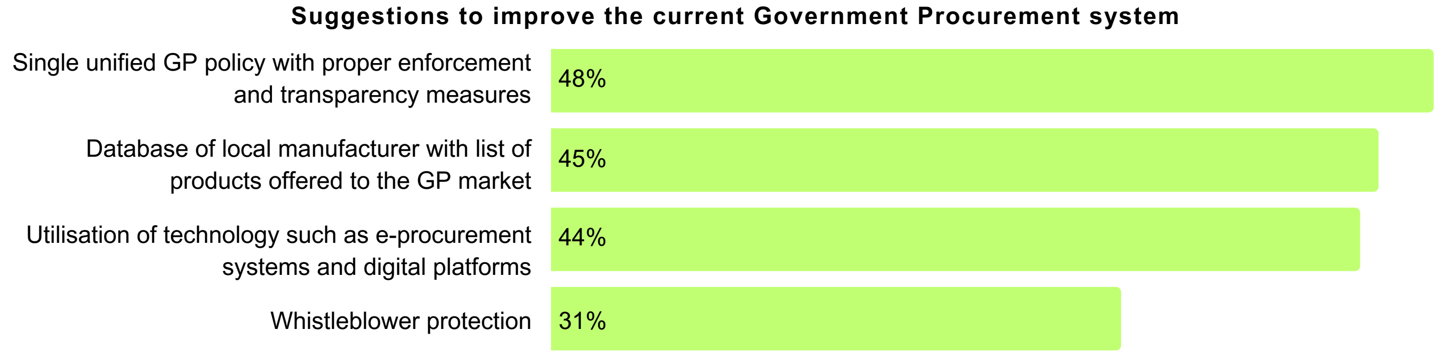
GOVERNMENT PROCUREMENT

A majority of respondents (88%) reported not supplying to the government, indicating barriers to entry or challenges in the procurement process. Only 12% are involved, suggesting government contracts are highly competitive or inaccessible. Key barriers include perceived lack of transparency (34% respondents), extensive documentation (23%), complex government procurement processes (20%) and competition from traders/foreign suppliers (20%).





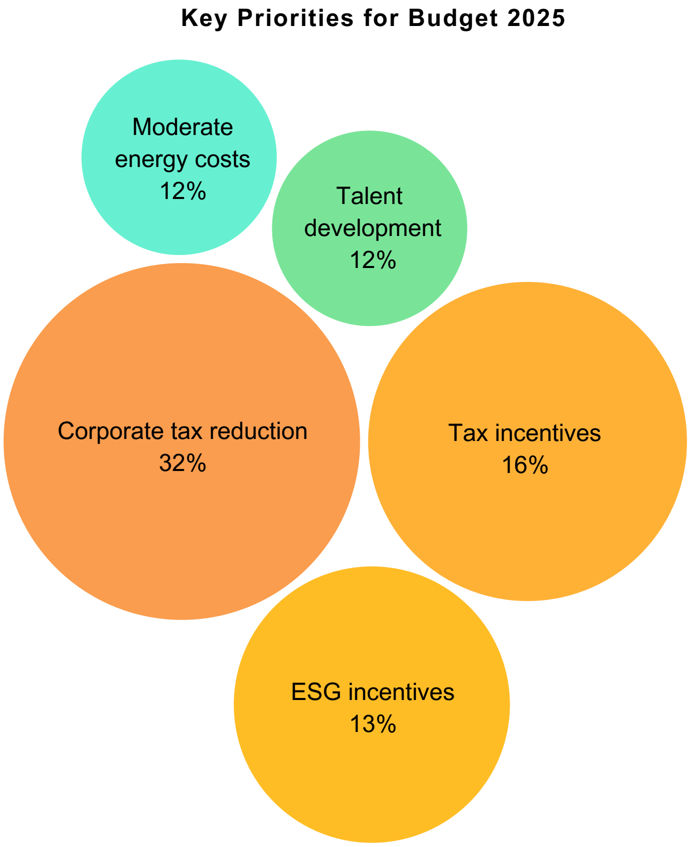
To improve the system, 48% recommend a unified procurement policy with enforcement, 45% advocate for a database of local manufacturers, 44% suggest using e-procurement platforms, and 31% support whistleblower protection. These reforms could increase transparency, standardise processes and make government contracts more accessible to a broader range of businesses.



BUDGET 2025: 5 KEY PRIORITIES

The majority (32%) of respondents prioritise reducing corporate tax rates, highlighting the importance of maintaining Malaysia's competitiveness in attracting foreign investment. Expanding tax incentives (16% respondents) is also crucial for stimulating growth, especially in key sectors like technology, manufacturing and green energy, aligning with global trends to drive innovation and economic diversification. ESG incentives (13%) are increasingly important, encouraging sustainable practices and attracting ESG-focused investments.

Talent development (12%) is vital for reducing reliance on foreign expertise and enhancing competitiveness in high-tech industries. Controlling energy costs (12%) is essential for managing inflation. Budget 2025 could focus on energy subsidies and accelerating renewable energy investments to mitigate these challenges. There is also support for reintroducing the goods and services tax (GST) at a lower rate, which could help broaden Malaysia's tax base without overburdening consumers. This move could provide a more stable revenue stream for the government while minimising inflationary pressures.



The FMM Business Conditions Index (FMM BCI) tracks the general state of the economy affecting business viability. The FMM BCI uses the current level of business activity as a proxy for current business conditions, compared to six months ago. Index values range from 0 to 200 points. A value above the growth-neutral threshold level of 100 points indicates an improvement or positive outlook, while that below the threshold indicates a worsening or negative outlook.

The FMM Business Conditions Survey 1H2024 was conducted from July 3 to August 9, 2024 and received 616 responses, of which 67.5% were SMEs (based on full-time employees), with 119, 107 & 105 responses from Klang Valley, Johor & Perak respectively. The top three industries for responses were: Food, Beverage & Tobacco (15.7% of respondents); Electrical & Electronics (11.4%); and Fabricated Metal (10.7%).

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