



**Prospect of MSMEs
in Malaysia**

Chapter

3



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COVID-19 has not only disrupted the health welfare of the society, but has remarkably taken a heavy toll on any country's economy. Governments across the globe are putting immense efforts to bring it under control, while prioritising the livelihood of people, businesses and jobs at the same time. Amidst significant changes brought about by the pandemic in the way businesses operate, MSMEs are gradually adapting and embracing the new normal. Lessons learnt about resilience in the face of disruption will be vital for future prospect in ensuring business sustainability.

OUTLOOK OF THE GLOBAL AND MALAYSIAN ECONOMY

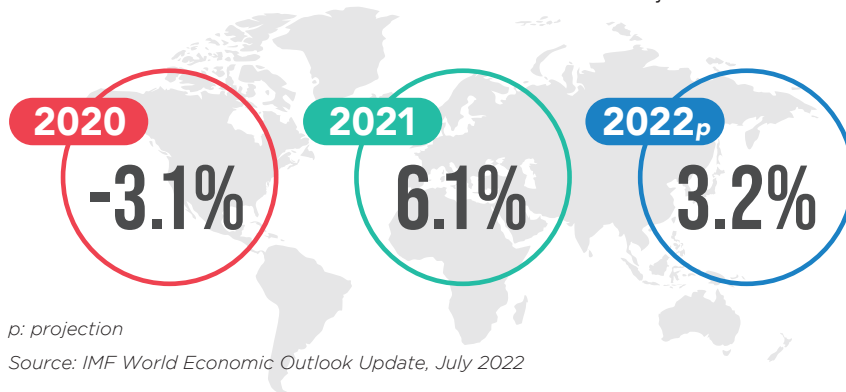
In the face of ongoing pandemic spread, countries all over the world were forced to face tough challenges simultaneously, namely saving lives and livelihoods while ensuring economic stability. In 2021, the global economy managed to rebound but the recovery momentum weakened towards the end of the year. Containment measures being put in place in response to a rise in COVID-19 cases following the emergence of the highly contagious Omicron variant in some countries have led to increasing uncertainty in the global economic growth. Findings from the World Economic Outlook (WEO) Update July 2022 published by the International Monetary Fund (IMF) showed that the global economy grew by 6.1% in 2021 (2020: -3.1%).

Recognising the crisis triggered by the Russia-Ukraine war and the slowdown in China, the growth of global recovery for 2022 has been revised downward for the third time and is projected to expand at a slower pace of 3.2% in 2022 (refer to Chart 3.1). The revised figure was 0.4 percentage points lower than the one estimated previously at 3.6% in WEO April 2022 and 1.2 percentage points lower than 4.4% estimated in WEO Update January 2022, reflecting weaker-than-expected recovery momentum as the crisis contributed to a significant gloomy development in 2022. The economic effects of the war are spreading far and wide mainly through commodity markets, trade and financial linkages. Against a backdrop of potential soaring inflation, war-related supply shortages will lead to price increase of energy, metals and food, thus squeezing living standards worldwide.

Furthermore, with the pandemic maintains its grip, China's economic slowdown has added to the global supply chain disruptions as the country implemented lockdown recently in its key trade hub. Emergence of more contagious variants have driven a worrisome surge in COVID-19 cases, which may lead to worse-than-anticipated deceleration in China. Further escalation of the country's property sector too might further suppress its growth. Also, other risk to the outlook includes renewed outbreak of the pandemic should new variant of virus arises and geopolitical fragmentation which may impede global trade and cooperation.



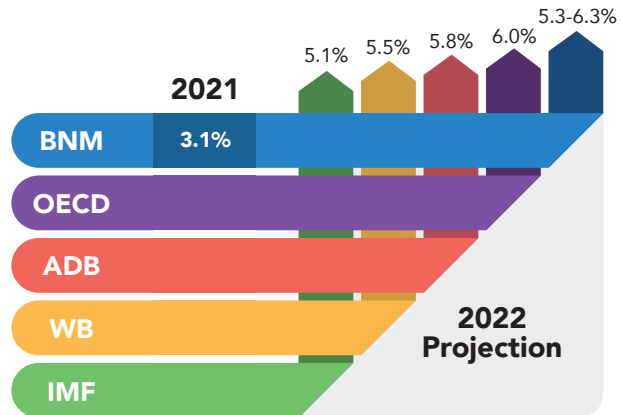
Chart 3.1: World's Growth Performance in 2021 and Projection for 2022



Zooming on to the domestic economy, the year 2021 was rather tense as Malaysia too was not spared from the resurgence of COVID-19 cases which in turn led to prolonged lockdowns. This was reflected in declining year-on-year growth of Malaysian economy in the first and third quarter of the year following renewed demand and supply shocks arising from measures to combat the outbreak. Nevertheless, the economy rebounded to register positive growth in the second and fourth quarters, of which the latter was anchored by an improvement in domestic demand and recovery in the labour market as economic activities resumed with the relaxing of containment measures across states. Rapid vaccination progress, greater firm adaptability and more widespread adoption of digitalisation and automation had also enabled firms and households to partly mitigate the impact. For 2021 full-year performance, the Malaysian economy expanded by 3.1% as compared to a contraction of 5.5% in the preceding year.

The recovery of Malaysian economy is translated into a strong growth of 6.9% in the first half of 2022, while it is projected to expand further for the remainder of the year. Malaysia is anticipated to continue its recovery momentum in the range of 5.3 - 6.3% in 2022, in line with the projected improvement in global growth. The Malaysia's growth prospect will be underpinned by several factors including global and domestic demand, recovery in tourism-related sectors following the reopening of international borders and further improvement in labour market conditions. Recovery too will be aided by implementation of investment projects and targeted policy measures for households and businesses that will provide further support to economic activity and aggregate demand. Nevertheless, the growth trajectory in 2022 is also subject to some risks, mainly from the weaker-than-expected global growth, further escalation of geopolitical conflicts and worsening supply chain disruptions. Chart 3.2 depicts recovery projection by Bank Negara Malaysia (BNM) and various international agencies towards Malaysia's economic outlook for 2022.

Chart 3.2: Malaysia's Growth Performance in 2021 and Projection for 2022



Sources:

- 1) *BNM Economic and Monetary Review 2021, March 2022*
- 2) *OECD Economic Outlook for Southeast Asia, China and India 2022, March 2022*
- 3) *Asian Development Outlook Supplement, July 2022*
- 4) *World Bank East Asia and the Pacific Economic Update, June 2022*
- 5) *IMF World Economic Outlook Update, July 2022*

BUSINESS OUTLOOK FROM THE PERSPECTIVE OF BUSINESS ASSOCIATIONS

According to the survey conducted by World Bank in February - March 2022 on Malaysian firms, significant recovery signs in term of sales and demand are evidenced^[7]. Sales of firms across all sectors are gradually reverting towards pre-pandemic level, led by manufacturing sector whose sales already hit beyond the pre-pandemic level. In terms of size, small firms are catching up with average sales growth is 10.0% lower than pre-pandemic level, while sales for medium and large firms have more than fully recovered. Prospect for future sales too is positive with more respondents (34.0%) expected sales to increase in the near-term. Moreover, demand for MSMEs' goods and services is seen to be rising following the economic reopening with 29.0% firms cited increased demand. Firms that reported reduced orders have also significantly decreased to 31.0% in February 2022 (July 2021: 51.0%). Nevertheless, issues on cash flow and rising cost of doing business remained a major challenge and may hinder potential growth of MSMEs.

In line with the favourable outlook, the retail industry too is gearing up towards positive momentum in 2022 after experienced a challenging period for almost two years from the pandemic outbreak. As projected by Retail Group Malaysia (RGM) in September 2022, the retail industry growth forecast has been revised upward further and estimated to expand by 31.7% compared to 13.1% (projected in June 2022) and 6.3% (projected in March 2022), on the back of anticipated strong sales and recovery of the industry^[8]. The reopening of international border would provide ample support to the industry especially for retail businesses that heavily dependent on leisure travellers. Shopping traffic also has gradually improved in major shopping malls across the country, giving better prospect towards recovery. Nevertheless, some lingering concerns may impact the growth of the retail segment. The recent rising price of consumer goods will reduce the purchasing power of Malaysian households, thus affecting the business operation of MSMEs given that 36.2% were involved in the wholesale & retail industry in 2021^[9].

This promising performance is aligned to Malaysia's leading index published by the Department of Statistics, Malaysia (DOSM). The leading index increased annually by 5.3% to reach 111.7 points in June 2022 after a rise of 2.3% in May 2022 (111.3 points). The index which measures the future direction of the overall economic activity in the three-month ahead also signals positive economic outlook, thus allow MSMEs to re-strategise their business. Moving forward, efficient and effective inflation management by the Government is vital to ensure sustainable economic growth. Meanwhile for manufacturing sector, the survey conducted by the Federation of Malaysian Manufacturers (FMM) in January - February 2022 depicted that majority 61.0% respondents are confident they can recover their business in 2022, with interestingly almost one-third believe they can achieve better than the pre-COVID level ^[10]. However, manufacturers cited that factor such as labour shortages, supply chain disruptions and ongoing pandemic would be key risks to the industry's growth outlook apart from the implementation of higher minimum wage which is not agreeable among most respondents (72.0%).

Based on a survey conducted by the Associated Chinese Chambers of Commerce and Industry of Malaysia (ACCCIM), businesses are somehow cautiously optimistic about the prospect of economic and business recovery for 2022 amid lingering risk from the easily transmissible variant as well as domestic and external headwinds ^[11]. Findings showed that a total of 42.1% expected better economic prospect and 41.3% anticipated better business outlook, an improved data than the one recorded in 2021 at 15.5% and 17.5% respectively. In addition, taking into account the rising importance of sustainability element in businesses, majority 61.6% of MSMEs being surveyed would like to learn more about green practices while 36.6% respondents including MSMEs have intention to undertake green investment in the future.

Moreover, the anticipation of sanguine, yet cautious economic prospect in the near term is also reflected in the recent 2Q 2022 Vistage-MIER CEO Confidence Index (CCI) ^[12]. The CCI that surveyed CEOs, business owners and key executives of small and medium-sized businesses indicated a less upbeat economic conditions in the year ahead. This is shown with 58.0% of CEOs perceived that the domestic economy would improve in coming months, slightly lower than 62.0% recorded previously in 1Q 2022. Other forward-looking indicators namely revenues and profits registered lower readings but fairly above the confidence threshold, signifying CEOs' stance on the firms' outlook held up quite well. Higher orders from local and abroad are expected in the second half of 2022 as the economy gains recovery momentum. The CEOs had previously cited that shortage of talents will pose as key business risk in 2022. With the country's transition into endemic phase, more than a quarter of CEOs (26.0%) cited that their company needs more than six months to a year to recover to profitable or pre-pandemic levels.



PROJECTION FOR MSME GDP

Despite the unprecedented disruption from the COVID-19 pandemic has slowed down the economic growth and challenged the business strength, the outcome from the economic disruption has also proven the resilience of entrepreneurs and MSMEs as they are able to adjust and adapt to the new normal. With health risks slightly moderated and the economy continued to recover, Malaysian MSMEs are projected to sustain its trend of positive growth for the year 2022. Taking into account that the overall economy is estimated to expand between 5.3 - 6.3% in 2022 (2021: 3.1%), MSME GDP is projected to increase by 2.4% during the year (2021: 1.0%). The improved outlook is supported by strong private consumption and increased Government assistance through SemarakNiaga, Bantuan Keluarga family assistance programme as well as Budget 2022 that will directly and indirectly benefit the MSMEs.

The recovery pace of MSMEs is expected to gain further momentum in 2022, in line with projected recovery in the global economy as most countries gradually transition towards normalcy, albeit at varying degrees and expected improvement in Malaysian economy underpinned by continued recovery in private sector expenditure. The continued expansion in external demand, full upliftment of containment measures, reopening of international borders and improvement in labour market conditions will provide further impetus to growth of MSMEs. The relaxed COVID-19 rules and standard operating procedures (SOPs) starting 1 May 2022 will help to revive the economy of Malaysia, particularly MSMEs. The new SOPs which are part of its transition to an endemic phase include physical distancing is no longer required between individuals, entry to premises is allowed regardless of vaccination status, all economic sectors are allowed to operate (including banned activities / negative list) and relaxation on testing requirements for travellers entering the country.

Though the pandemic is not over yet, economies around the world are learning to live with it. Those that ignore the fast-paced and uncertain business landscape, will risk being left behind and ultimately find their businesses unable to survive. Meanwhile for those that embrace changes, opportunities will turn into a commercial gain, deliver a competitive advantage over less proactive rivals and potentially discover whole new opportunities for business expansion. Looking ahead for 2022, strategies must now evolve to account for medium and long run strategies for MSMEs to better withstand future shocks as well as to increase contribution of MSMEs to the economy. Hence, there is a need to emphasise on three focus areas to ensure a sustainable growth of MSMEs moving forward, namely value chain in high impact industries; internationalisation activities; and digitalisation & automation (refer to Chart 3.3).

Chart 3.3: Three Focus Area for MSMEs Recovery



MSMEs will gain wider market access by participating in the value chain of large firms in high impact industries such as smart farming, aerospace, electrical & electronics (E&E), medical devices, halal industry and others, while at the same time upgrade their skills and capability to supply their products and services to these large firms. In order to enhance internationalisation of MSMEs, strategies should be towards developing a targeted market-based focus for MSMEs to engage in international trade. Besides that, it is very important to facilitate export assistance and advisory services as well as strategic alliances to engage MSMEs into the global value chain. Moreover, a structured approach to support the digitalisation and automation of MSMEs is needed to improve MSME productivity, operational efficiency and help to expand their market outreach. These strategies will lend further impetus to MSME growth in achieving the long-term targets under the RMKe-12.