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Can't Tame the Animal Spirits

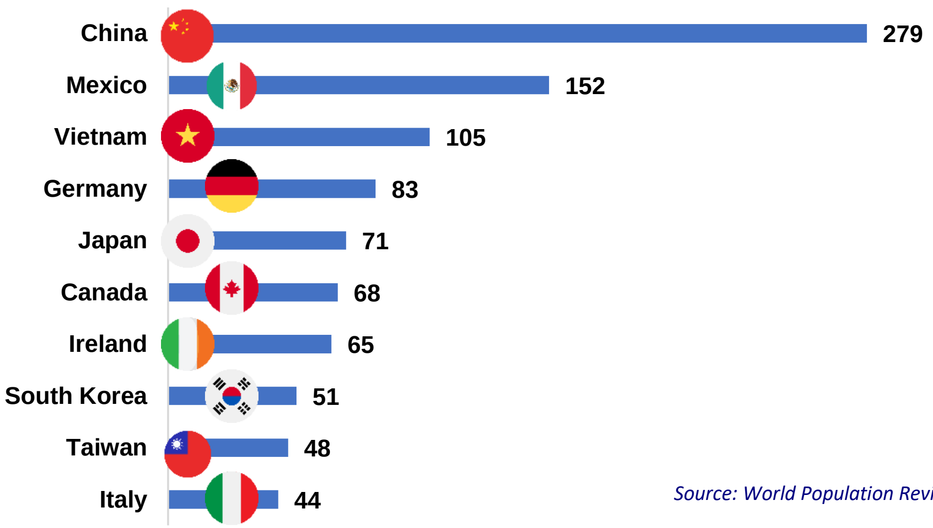
2024 could easily be summarised into 2 words: "animal spirits". This year was an awe-inspiring year to say the least with markets around the world either hitting new all-time-highs or breaking past long-term resistance levels. Magnificent 7 exceptionalism and renewed enthusiasm from a Trump victory drove US stock markets to new all-time-highs all the way since January with barely any pullback. As luck would have it, even long-ailing China enjoyed a strong but brief rally after Beijing's "bazooka stimulus" package tipped the sentiment on China banks and homeowners. Malaysia too were winners of 2024, reaching levels unseen since the 2020 glove-fuelled rally, only this time minus the gamblers' fervour and more on quality growth on the back of a flourishing DC landscape, confidence in the nation's political administration and the prevalence of well-favoured themes such as Penang/Johor infrastructure and East Malaysia development. We would not recommend counting our chickens before they hatch though, as the Federal Reserve's pivot into a more hawkish stance at the eleventh hour could put a dampener to the speculative zeal. Furthermore, geopolitical conflict in the Middle East and Ukraine-Russia continues to be major flashpoints casting an overhang on the bulls.

Stepping into 2025, we believe the best is still ahead of us with any downward volatility (such as from Trump's bellicose rhetorics) to be a buying opportunity, barring a black swan event. Together, these elements pave the way for a dynamic year ahead, encouraging us to explore the key questions that will guide our approach in the months to come, as outlined below.

Q1. What lies ahead for global markets in the Trump 2.0 environment?

"To me, the most beautiful word in the dictionary is tariff. It's my favorite word." President-elect Donald Trump is no stranger to tariffs, having implemented a plethora of punitive trade-centric policies in his first term in office. Even throughout his 2024 election campaign and in the days leading up to his coming inauguration, Trump boldly conveys that fixing US' trade imbalance is his No. 1 concern, followed closely by immigration issues. Is he justified in his hard stance on the issue? In 2023, the US had a whopping trade deficit of US$773bn, with 69% of the deficit contributed by only 3 countries: China, Mexico and Vietnam (**Fig. 1**).

Fig. 1: US Trade Deficit by Country in 2023 (US$ bn)



Source: World Population Review, PCM Dec 24

Critics argue that over-reliance on tariffs could lead to accelerated deglobalization and push inflation higher domestically in the US while simultaneously debilitating net exporters by shutting them off from the largest consumer market in the world. Be that as it may, evidently Trump has a talent for influencing consensus views. What was once a divisive topic, Joe Biden fully embraced Trump's trade policies by further raising tariffs on China and enacted protectionist policies through the Inflation Reduction Act as well as the CHIPS Act to onshore key strategic industries such as EVs and semiconductors.

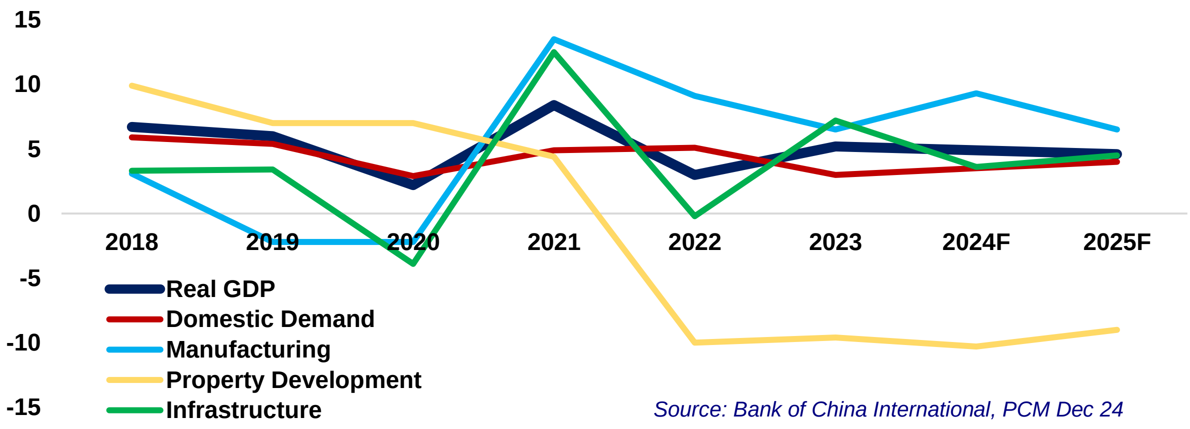
Moving into Trump 2.0 this year, we view this could go 3 ways. One way is that Trump's threats get reciprocated in the same manner with trading partners fighting back by implementing their own tariff (as Canada, Mexico and China have done) à la tit-for-tat. The Trump administration goes through with the tariffs, hastening domestic inflation while also stunting their own exports in the short term but ultimately generate more jobs in the long run as manufacturing gets relocated domestically. Another way this could go through is that the threatened countries in question negotiate new trade deals with the US, ideally creating a win-win situation where net exporters start to import more from US and avoid being penalized with unreasonably high tariffs on their exports. The third possible scenario could be that US is less concerned about onshoring production and more focused on impeding countries with unfair trade policies (subsidized production, weak labour laws, dumping, etc), in which case trade could be diverted toward emerging markets such as Malaysia, benefitting additionally on top of ongoing "China Plus One" strategic initiatives.

Ultimately, the path that Trump takes is likely to be a combination of all these scenarios. Although it is difficult to predict what Trump will do once he takes office, we can make educated guesses based on the rationale behind his brazen stance, which is to correct the unfairness in global trade where US has been absorbing most of the world's production for far too long. Trump has made his move, so what is ours?

Q2. Will China finally recover and put the bears to rest?

China economy is projected to grow at a moderate 4.5% in 2025, slowing from 4.8% in 2024 (**Fig. 2**), as domestic demand remains subdued and export challenges persist. Fiscal stimulus is expected to play a crucial role in offsetting some of these pressures. A focus on boosting consumption will dominate economic policies, with measures including enhanced consumer subsidies, stronger social safety nets, and increased central-to-local government funding transfers. The fiscal deficit is forecasted to rise to 5.5% of GDP, reflecting proactive government spending aimed at revitalizing economic activity. Complementing this, monetary policy measures, such as interest rate cuts and liquidity injections, will be critical in combating deflation and supporting growth.

Fig. 2: China Economic Forecast yoy growth %



Trade tensions with the U.S., particularly after the imposition of a 10% tariff increase in 2025, present significant risks to exports. Early-year export growth will be driven by frontloading orders, but this is expected to taper off by the second half of the year. In response, China aims to diversify its manufacturing base across ASEAN countries and strengthen advanced manufacturing capabilities in key areas such as semiconductors and electric vehicles. Additionally, China's increasing trade ties with ASEAN and India represent strategic moves to counterbalance reduced trade with the US and align with global supply chain shifts.

The real estate sector, a long-standing economic drag, is likely to stabilize due to policies such as hukou liberalization and credit support for developers. However, recovery in property sales and prices will be slow, given the overhang of unsold inventory and weak consumer sentiment. Meanwhile, consumption will be a key driver of growth, with government-backed trade-in programs for durable goods and expanded healthcare subsidies aimed at boosting spending.

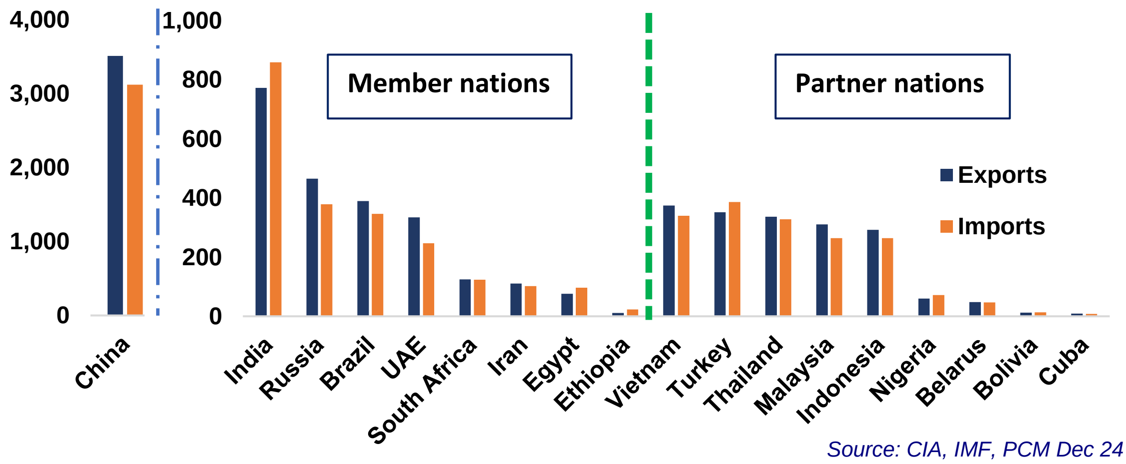
Innovation-driven growth is another cornerstone of China's strategy, with significant investments expected in high-tech industries and institutional reforms in science, education, and urbanization. These initiatives are designed to enhance economic resilience and unlock new growth engines in the medium to long term. Reform priorities also include building a unified national market and increasing rural residents' income to foster consumption and investment.

Key sectors for investment in 2025 include technology, particularly semiconductors and new energy vehicles, consumer goods and services, and renewable energy. These sectors are positioned to benefit from government support and structural shifts in the economy. However, sector-specific challenges, such as inventory overhang in real estate and global oversupply in solar energy, underscore the need for targeted strategies.

Q3. What does Malaysia gain from joining BRICS?

On 24 October 2024, Malaysia is being admitted as a partner country into BRICS, an intergovernmental bloc made up of emerging economies vying for an alternative to the current world order. To put briefly, the term BRIC (**B**razil, **R**ussia, **I**ndia, **C**hina) was originally coined in 2001 by Goldman Sachs as a way of identifying fast-growing, high potential economies ripe for investment. It then formed into an actual alliance in mid-2009, expanded to include **S**outh Africa in 2010 (leading to the current name, BRICS) and has now expanded even further to 9 members and 9 partner nations (**Fig. 3**) with the top 5 members controlling 35% of global GDP. Now this begs the question, what does it mean to be a member of BRICS and why would Malaysia want to join?

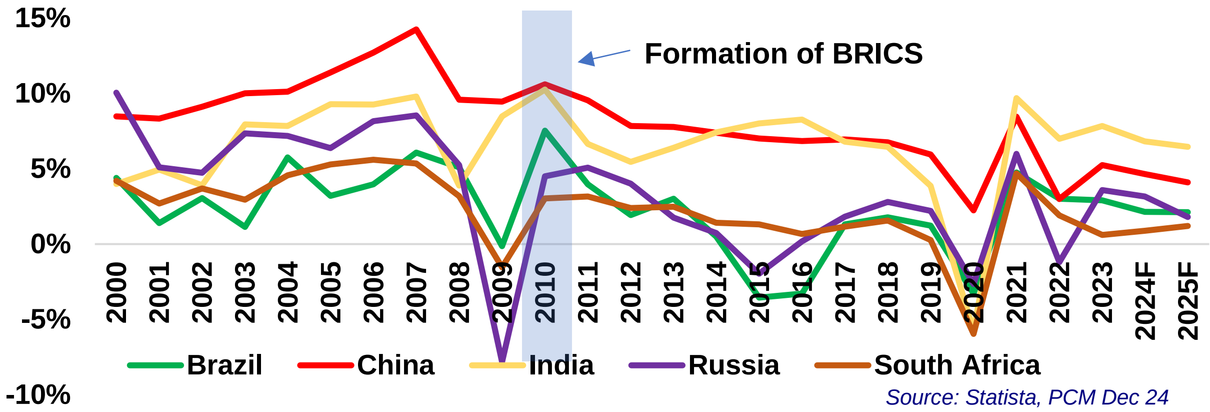
Fig. 3: BRICS members and partners by export and import value in 2023 (US$ bn)



Source: CIA, IMF, PCM Dec 24

There are several viewpoints we can observe from this. According to our Prime Minister Datuk Seri Anwar Ibrahim, joining BRICS will offer economic opportunities free from external pressure and strengthen the "Global South", a sentiment in dire need as the US tends to flex its economic muscle by sanctioning countries that defy it or pose a threat i.e Russia and China. By aligning with BRICS, pressure to pick a side between US and China may be alleviated. Antagonizing US is not the goal here, as it is noted that many BRICS members maintain good relations with US and other western countries. Furthermore, creating and strengthening new economic and trade ties may lead to the flourishing of new markets and industries Malaysia can participate in.

Fig. 4: Real GDP Growth yoy of BRICS core members (2000 - 2025F)



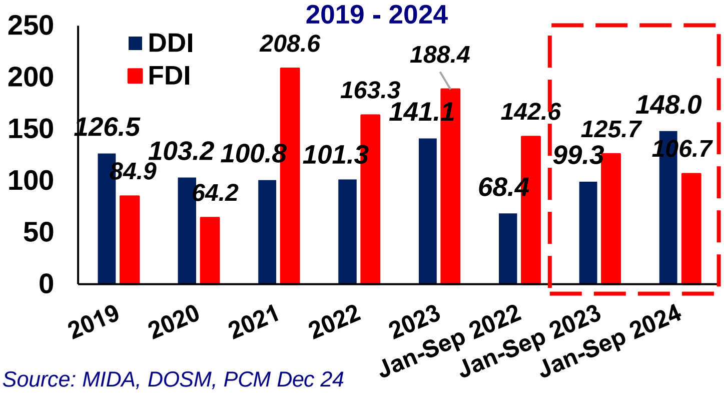
Source: Statista, PCM Dec 24

Joining BRICS would also strengthen the role of the Straits of Malacca as a shipping route bridging the Pacific and Indian Oceans. Malaysia already enjoys strong relations with 3 BRICS members, namely China (largest trade partner for 15 years), India (largest buyer of Malaysian palm oil) and Russia (8th largest trading partner). According to MITI (Ministry of Investment, Trade and Industry), Malaysia's participation in BRICS will not include any free trade agreements with other members, which should breathe a sigh of relief for the competitiveness of our budding SMEs and local industries. Although there is not much evidence of accelerating growth from joining BRICS evident from the declining growth rates in **Fig. 4**, other ways Malaysia could benefit is by way of a common currency for trade as an alternative to the US dollar as well as being able to tap into BRICS New Development Bank for financing infrastructure projects. Overall, having more allies is never a bad thing and Malaysia, due to its strong relations with both sides of the globe, can benefit tremendously from increased cross-border cooperation from both political and economic angles.

Q4. How did Malaysia's Foreign Direct Investment (FDI) and Domestic Direct Investment (DDI) trends shifted over time, and what factors influenced these changes?

From 2021 to 2023, Malaysia's Foreign Direct Investment (FDI) consistently outpaced Domestic Direct Investment (DDI), driven largely by the China Plus One strategy adopted by multinational corporations. However, in 2024, a volatile global economic landscape, characterized by trade tensions, geopolitical risks, and economic slowdowns, resulted in a decline in 9M2024 FDI to RM106.7 bn (9M2023: RM125.7bn). Despite this, FDI levels remained above pre-pandemic figures (**Fig. 5**).

Fig. 5: Approved Investment in Malaysia in RM bn, 2019 - 2024



Source: MIDA, DOSM, PCM Dec 24

In contrast, DDI surged to RM148.0bn (9M2023: RM99.3bn), surpassing FDI as local investors sought stability in domestic markets amid global uncertainties. Government initiatives like the GEAR-uP program, which commits RM120bn in DDI over the next five years, have further bolstered local investments.

For 9M2024, approved investments totalled RM254.7bn (DDI: 58%; FDI: 42%), marking a 13% increase from 9M2023 and a slight rise above the 10-year average of RM233.3bn. Key sectors receiving these investments included Information and Communications Technology (RM71.1bn), Electrical and Electronics (RM47.0bn), and Real Estate (RM48.8bn). The Electrical and Electronics (E&E) sector has consistently contributed an average of 21% to total approved investments over the past five years.

Malaysia also achieved remarkable growth in digital investments, attracting RM141.72bn in the first 10 months of 2024—triple the digital investments approved in 2023 (RM46.2bn). Major contributions came from global tech giants such as Oracle (US$6.5bn), Amazon Web Services (US$6.2bn), and NVIDIA (US$4.3bn), which invested heavily in data centres (DCs), AI infrastructure, and cloud technologies. By Dec 2024, Malaysia had 54 operational DCs with an IT capacity of 504.8 MW and 61 additional DCs under construction, expected to add 1,313 MW of capacity (**Fig. 6** overleaf). These developments have provided significant spillover benefits to the real estate and construction sectors.

Fig. 6: Distribution of Data Centre (DC) IT Capacity in Malaysia

Region/State	Existing Supply		Future Supply (Under Construction & Committed)	
	No of DCs	Estimated IT Capacity (MW)	No of DCs	Estimated IT Capacity (MW)
Johor	12	396.9	28	898.7
Klang Valley	37	107.0	28	378.5
Penang	3	0.4	-	-
Sarawak	2	0.6	2	17.8
Negeri Sembilan	-	-	2	16.0
Kedah	-	-	1	2.0
Total	**54**	**504.9**	**61**	**1,313.0**

Source: DC Byte, Knight Frank Malaysia Research, PCM Dec 24

To sustain balanced and sustainable economic growth, Malaysia must continue attracting FDI while fostering domestic investments. FDI is expected to remain robust in the E&E and ICT sectors, driven by initiatives like the National Semiconductor Strategy (NSS) and the newly established National AI Office (NAIO). These efforts will ensure Malaysia leverages both local and international capital, technology, and expertise for its economic advancement.

Q5. How the Federal Reserve's interest rate cuts and the current Treasury yield curve shape investor sentiment and economic forecasts for 2025?

In Dec 2024, the Federal Reserve (Fed) announced its third consecutive interest rate cut of the year, reducing the federal funds rate by another 25 basis points (bps) to a range of 4.25% to 4.5%. This decision, despite a recent uptick in inflation, aims to support the labour market and manage economic growth. The Fed's latest dot-plot projections indicate a slower pace of rate cuts in 2025, with only two cuts totaling 50 bps, compared to the four cuts previously forecasted. This cautious approach reflects ongoing concerns about reaccelerating inflation and the potential impact of President-elect Donald Trump's proposed policies.

Recent data shows that US inflation remains a significant concern for the Fed. The annual inflation rate rose to 2.7% in Nov 2024, up from 2.6% in Oct 2024. This increase is partly influenced by low base effects from the previous year and persistent price pressures in various sectors, including energy and food. On the other hand, the Fed's preferred gauge of inflation, the Personal Consumption Expenditures (PCE) price index, also showed a slight increase, reinforcing the need for a cautious approach to rate cuts.

The same expectation is being reflected in the current Treasury yield curve, which has flattened, indicating the Fed rate cuts and the market expectations of slower economic growth and persistent inflation (**Fig. 7**). The flattening of the yield curve suggests that investors are cautious about the economic outlook, despite the Fed's efforts to stimulate growth through rate cuts.

The Fed's recent rate cuts and its projections for a slower pace of cuts in 2025 reflect a difficult landscape characterized by persistent inflation and global uncertainties. The US Treasury yield curve and the Fed projections provide valuable insights into institutional capital market expectations which we can take into consideration in our asset allocation.

Fig. 7: 10 - 2-year Spread, US Treasuries

Source: Federal Reserve Bank of St. Louis, PCM Dec 24

Q6. State election in East Malaysia, a litmus test between Federal and Borneo?

Both states in East Malaysia will soon have their own state election, with Sabah holding their election in 2025 and Sarawak in 2026. Currently, Sabah and Sarawak play an important role in the coalition government, contributing 20% of the coalition government block or 32 parliamentary seats (**Fig. 8**). Now, the Borneo region carries significant political influence in the federal government as support from both GPS and GRS are crucial to maintain the stability of unity government. Additionally, Federal government budget allocation towards East Malaysia has been steadily increasing for the past 3 years (**Fig. 9**) and is currently at an all-time high. Therefore, we anticipate more contracts dishing out at both the federal and state level as Sabah gears up for its state election.

To maintain a strategic balance between the federal government and the Borneo states, an MA63 implementation council was formed and chaired by both the Prime Minister and Deputy Prime Minister together with the Sarawak Premier and Sabah Chief Minister. The entity was set up as a channel between the federal government and state to resolve issues concerning return of authority to the state, including petroleum royalty payments and regulatory functions over minerals and resources. Among the items resolved are the handover of regulatory power on Sabah Electricity Sdn Bhd to the Sabah state, transfer of regulatory power over gas supply to Sabah and Sarawak, recognizing Sabah and Sarawak JKR as technical dept authorised to implement projects valued up to RM50m, as well as return of federal land to the two states. Further, both states have formed their own state institutions to manage their respective oil and gas supply, namely Petros (Sarawak) and SMJ (Sabah)

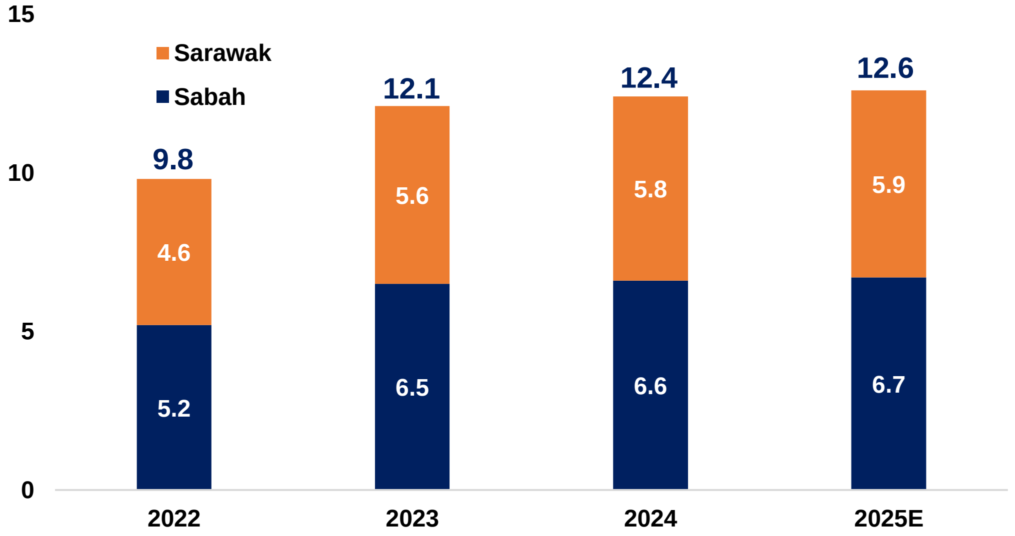
Fig. 8: The stability of Federal government depends largely on the Borneo political block

Party	Seats
GPS	23
GRS	6
WARISAN	3
PH	82
BN	30
PBM	1
Total	145

Source: Parliament of Malaysia, PCM Dec 24

Overall, East Malaysia-based listed companies are set to benefit from the bigger share of revenue from Sabah and Sarawak state governments and also increased in budget allocation for both states in Budget 2025. Key projects that are expected to take off next year include the Pan-Borneo Highway, the airport expansion for Kota Kinabalu, Miri and Tawau, Sepanggar Bay Container & Bintulu Port expansion, as well as Sabah-Sarawak Link Road Phase 2A. Furthermore, the whole Borneo region would also get a boost from the relocation of Indonesia's capital to Nusantara, which is right next to Sabah and Sarawak.

Fig. 9: Federal Budget Allocation to Sarawak and Sabah in RM bn, 2022-2025

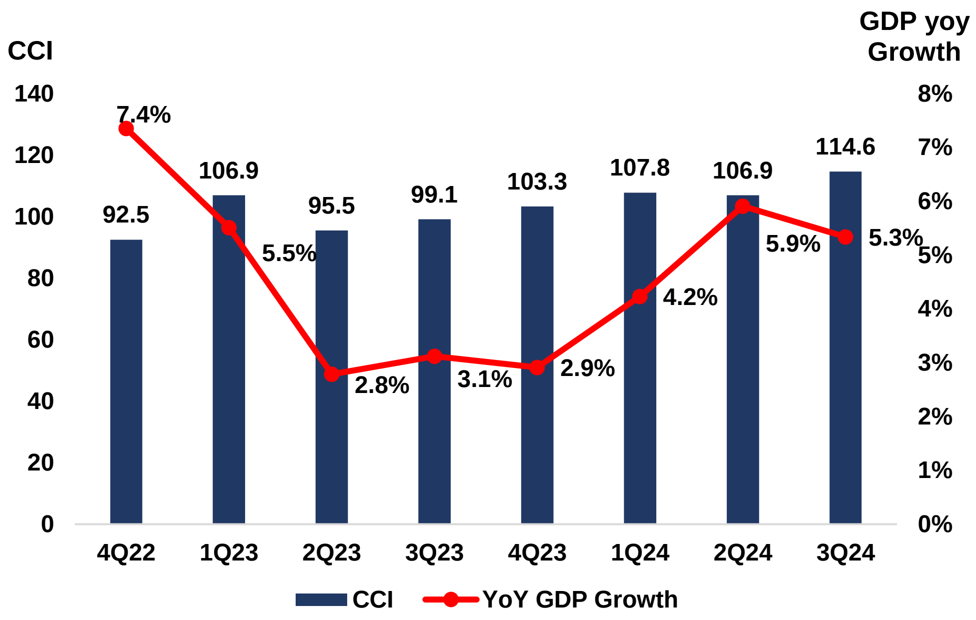


Source: MOF, PCM Dec 24

Q7. Is Malaysia on Track for a Consumer Spending Boom in 2025?

The Vistage-MIER CEO Confidence Index (CCI), which measures the sentiment of Malaysian CEOs on key economic indicators, has shown a steady increase, rising from 99.1 in 3Q23 to 114.6 in 3Q24 (**Fig. 10**). This upward trend reflects an optimistic outlook on economic prospects, further supported by Malaysia GDP growth of 5.3% yoy in 3Q24. The indices for economic conditions, planned fixed investment, and expected revenue and profit growth have also recorded yoy increases, indicating growing economic confidence and improving market dynamics.

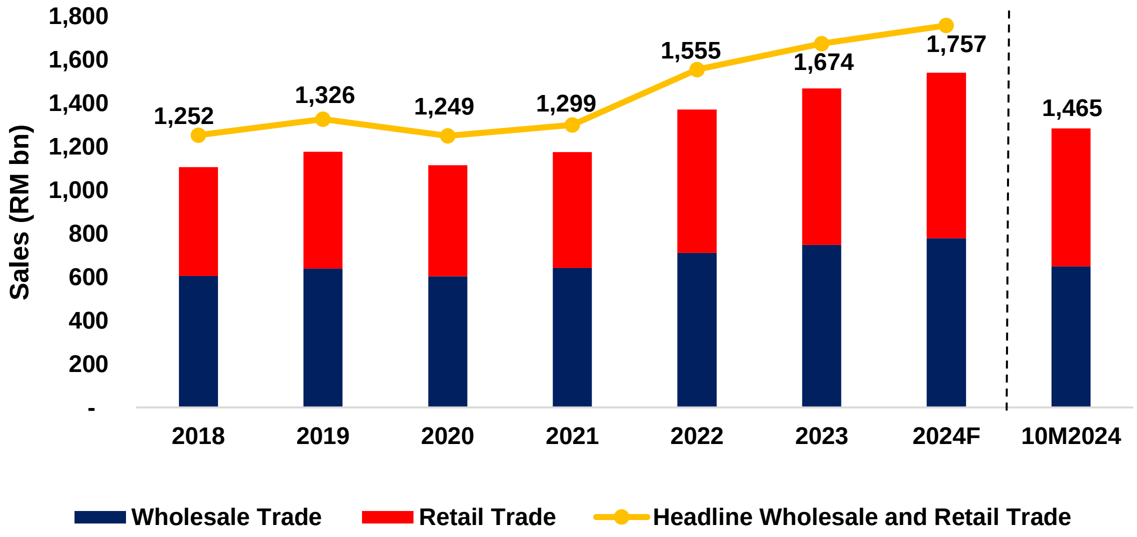
Fig. 10: CCI and GDP yoy growth, 4Q22- 3Q24



Source: MIER, PCM Dec 24

Meanwhile, consumer demand has shown exceptional growth since June, as evidenced by the 5.5% yoy rise in wholesale and retail trade in October 2024, bringing total sales for the first 10 months of 2024 to RM1,465bn (**Fig. 11**). This surge in was primarily driven by a 7.1% yoy rise in retail trade, followed by a 4.8% yoy increase in wholesale trade, fuelled by strong consumer spending, associated with seasonal factors such as the Deepavali celebrations and school holidays. The sustained performance of wholesale and retail trade since 2021 underscores Malaysia underlying economic resilience and steady recovery. Spending activity is anticipated to remain robust, supported by easing inflation, stable monetary policy, and increased international tourists' arrivals.

Fig. 11: Wholesale & Retail Trade, 2018 – 2024F

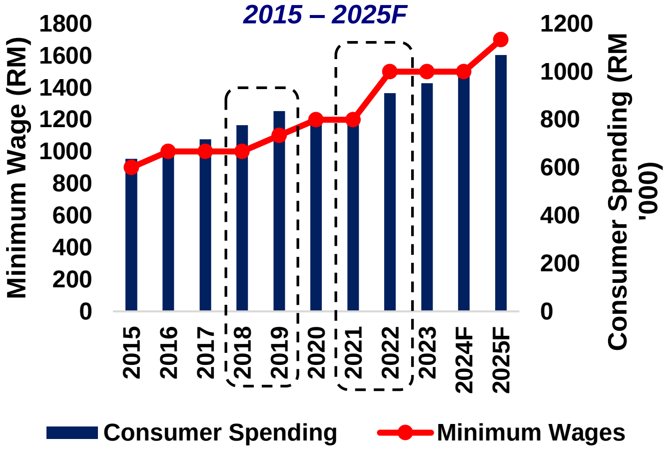


Source: DOSM, PCM Dec 24

Malaysia tourism sector saw international arrivals surged to 22.5 million in the first 11 months of 2024, up from 17.8 million in the same period in 2023, surpassing 2023 total of 20.1 million. Despite the encouraging momentum, the numbers remain below the 24.1 million arrivals in 2019. The government's efforts, such as free visas for Indian and Chinese visitors, chairing the ASEAN Tourism Forum Malaysia 2025, ASEAN Chairmanship 2025, and Visit Malaysia 2026, as well as RM550m tourism budget allocation, aim to drive recovery with a target of 31.4 million visitors for 2025.

Domestically, Budget 2025 was strategically designed to stimulate consumer spending, including a 30% increase in cash handouts, a 13% rise in the minimum wage to RM1,700, and a civil servant salary hike of 7-15%. As of December 2024, 99% of the 1.5 million civil servants will benefit, which raises the minimum monthly income for civil servants from the current RM1,795 to over RM2,000.

Fig. 12: Minimum wage & consumer spending 2015 – 2025F



Source: DOSM, Ministry of HR, PCM Dec 24

The minimum wage hike is expected to drive consumer spending as observed in 2019 and 2022 (**Fig. 12**). In 2019, a 10% increase in minimum wage boosted consumer spending 7.5% while 25% hike in 2022 resulted in 11% increase. The second part of the wage increase, effective February 2025, is anticipated to similarly boost spending and help ease inflationary pressures.

In summary, with increased civil servant salaries, a higher minimum wage, and expanded cash handouts in 2025, disposable income is expected to increase, providing relief to consumers facing household cost and inflationary pressures. Sustained recovery in the tourism sector on the back of higher international tourist arrivals will further strengthen Malaysia's economic resilience.

2025 Strategy Primer

- ❖ Fears on Trump 2.0 are likely overstated; Trump is known for his aggressive stance and rhetoric but will ultimately push for win-win deals.
- ❖ Federal Reserve likely to move forward with rate cuts in 2025, despite hawkish tone recently, on account of:-
  - i. Inflation trending down with stable services and shelter components.
  - ii. Unemployment ticking up, showing room for more easing.
- ❖ Declining US rates will lead to hot money flows outside of US (i.e emerging markets) in search of yields and risk premiums, pressuring the dollar.
- ❖ Malaysia-sector wise, anticipating a comeback for Tech stocks.
- ❖ Possible ringgit strengthening/dollar weakening will benefit export-oriented stocks especially Tech.
- ❖ We recommend having a more diversified portfolio compared to 2024 to mitigate uncertainty and risks.
- ❖ Time in the market beats timing the market!