GI / 05 / 2023

March 17, 2023

To: CEO/ Directors/ Managing Directors/
Finance/ Business Development/Sales Managers

FMM Business Conditions Survey 2H2022

The Federation of Malaysian Manufacturers (FMM) is pleased to publish the findings of the 22nd biannual survey of business conditions in the manufacturing sector for the second half of 2022 (2H2022). The findings were successfully released to the media via a press conference on March 16, 2023. We are pleased to enclose a copy of the survey findings for your reference and record.

The survey revealed that weak external demand, especially from key trading partners, further escalation of geo-political tensions and the impact of China's zero-Covid policy, among others, have likely weighed on the Malaysian manufacturing sector which showed a moderation in manufacturing activities in 2H2022. Local and export sales, as well as production levels had remained subdued, while capacity utilisation, production cost and capital investment lost further growth momentum, but employment had picked up:

- ***Activity in the manufacturing sector had held up fairly well, albeit slower, in 2H2022*** *as reflected in the latest business activity index which, at 107, had remained above the 100-point optimism threshold, but lost two points from 1H2022. Most (37%) respondents believed that their business activity in 2H2022 had remained the same as in 1H2022, while 35% reported an increase in theirs and 28% stated otherwise.*
- ***Local and export sales have remained generally steady,*** *although local sales had grown at a faster pace than export sales. In 2H2022, the current indexes for local sales and export sales stood at 98 and 91, respectively, little changed from 1H2022. Among those who sold domestically, 27% reported higher sales, while 43% had managed to maintain their sales in 2H2022. Exports also rose for 27% of those who export, with another 37% saying their exports have remained the same during this period. Poor sales affected more of those who export than those who sell locally, with 36% and 30% confirming this, respectively*
- ***Production had remained relatively stable, while capacity utilisation had trended down in 2H2022.*** *Suggesting this is the latest production index which had remained at its 1H2022's level of 102, with 33% and 36% of the respondents having expanded or retained their production volume in 2H2022, respectively. The index for capacity utilisation dipped just below the optimism level to 99 in 2H2022, losing five points from the prior period. 29% of the respondents increased their capacities lately, down from 33% in 1H2022.*
- ***Manufacturing cost had eased in 2H2022,*** *as depicted by the decline in the cost of production index to a two-year low of 166. 72% of the respondents reported higher production costs, down from the preceding period's 85%. Those who managed to keep their costs lower had also doubled from the 3% in 1H2022.*
- ***The capital investment index retreated five points*** *to 109, an implication that capital investment (CAPEX) had waned recently. 23% increased their CAPEX in 2H2022, while it remained the same for another 57% of the respondents.*
- ***Employment was the only current index that registered an increase in 2H2022.*** *At 112, the index had gained 12 points from 1H2022, indicating that recruitment in the manufacturing sector had picked up recently. Labour intake rose for 26% of the respondents in 2H2022 while 61% put hiring and retrenchment on hold.*

Looking ahead, the manufacturing sector is expected to grow at a slow pace in 1H2023 in tandem with the slowing global economy. Forward-looking indicators are suggesting a slowdown in capacity utilisation, capital investment, hiring and a relatively tame outlook on production for 1H2023. Except for cost of production, capital investment and employment, all the other indexes had also registered below the demarcation level of optimism, further surmising the slow outlook going forward.

- ***For the second survey in a row, the expected index for business activity had stayed below the optimism threshold.*** *At 92, this index had lost two points from the prior survey, inferring that business activity is expected to slow further in 1H2023.*
- ***The latest expected index for local sales is higher than that for export sales.*** *At 91 and 84, respectively, it suggests that local sales are expected, once again, to be ahead of export sales in early 2023. Notwithstanding this, both indexes had remained below the optimism threshold for the second survey in a row, implying that a slowdown in sales is expected on both the local and external fronts.*
- ***With sales expectations looking cautious, plans for production and capacity utilisation are similarly prudent.*** *Not only have both these indexes in the latest survey fallen from the preceding survey to 97 and 94, respectively, but their position below the optimism threshold also indicates that a slowdown in both of them is imminent in the coming months as well.*
- *The expected index for cost of production fell for the second consecutive survey to 166, inferring that* ***production costs are expected to moderate, but remain at elevated levels amid persistent cost and demand pressures.*** *73% projected higher production costs soon, down from 81% previously.*
- ***Capital investment is expected to be relatively flat in 1H2023,*** *as indicated by the expected index which, at 112, is little changed from the previous survey's 113. 32% in the latest survey are contemplating increasing their capital expenditure (CAPEX), marginally down from 33% in the previous survey.*
- ***Labour intake in the manufacturing sector will continue in 1H2023, albeit at a slower pace.*** *This is shown by the expected index for employment which fell to 113 from the 117 previously. 28% of the respondents planned to recruit more workers soon, while 57% are planning to retain their existing workforce for now, compared to the preceding survey's 33% and 50%, respectively.*

Topical issues covered in the survey revealed the following:

- *Employment costs (including higher wages, labour shortages, employee retention schemes, employee benefits, etc) are expected to increase moderately or significantly for most respondents in 2023. Energy cost is the second top cost factor to increase significantly.*
- *36% of respondents expect global economic conditions to deteriorate moderately while 43% and 35% of respondents believe that conditions in their own company and industry, respectively will improve moderately in 2023 compared to 2022. 31% of respondents anticipate moderate improvement in domestic economic conditions while 33% are less optimistic.*
- *Top 3 risks to business recovery and growth: input cost pressures, higher energy cost and Ringgit fluctuations*
- *41% and 30% of respondents, respectively, estimate higher revenue and profits by 1-24% in 2023*
- *Top 5 investments to boost competitiveness: new product development, automation, upskilling and retraining of existing workers, export market expansion, and adoption of green technology/energy efficiency measures*
- *59% of respondents able to meet their foreign worker needs and obtain quota approval. Only 8% not able to meet their foreign worker needs mainly due to slow and lengthy approval process. Employers are willing to work with education and skills training institutions to offer work-integrated learning programmes and curriculum development to address their skilled worker needs.*
- *66% of respondents aware of the Regional Comprehensive Economic Partnership (RCEP) and Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), but 77% have not started utilising them yet.*
- *The 4th increase in OPR by BNM in November 2022 increases the cost of production of 55% of respondents*
- *59% of respondents believe now is too early to gauge performance of new Government, but 33% see positive changes.*

The 2H2022 survey, which was conducted from January 18, 2023 to February 28, 2023, continued to receive great support from members and we achieved yet another high response rate of 745 companies. FMM would like to thank all members who took the time to respond and give their valuable feedback. The next survey would be in May 2023. FMM members' support and continued participation would ensure that the Business Conditions Index (BCI) is representative and an accurate monitor of business condition trends in the manufacturing sector.

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