



2H2025 Outlook: ***Uncharted territory***

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Introduction

Amid the ongoing uncertainties in the global trade environment, we have chosen the theme “Uncharted Territory” to reflect our sentiment on the evolving macroeconomic conditions in 2H2025. This report is intended to serve as a rear-view mirror of 1H2025 and a forward-looking guide to the challenges and opportunities ahead.

This report builds on our earlier publication, “2025 Macroeconomic Outlook: Policy Trade-Offs for Resilient Growth” (published on 24 January 2025), by providing updated macroeconomic forecasts and insights. This macro update covers developments in the global and major economies and offers a thorough analysis of the Malaysian economy in 2H2025.

In addition to our macroeconomic outlook, we present sectoral perspectives on semiconductors and healthcare, two industries that remain central to structural transformation and policy focus. We also share our latest views on foreign exchange (FX) and fixed income markets, informed by recent trends and forward-looking indicators.

A special feature of this report is our analysis of the US reciprocal tariff (RT) on Malaysia, where we examine past bilateral trade data to infer potential/preliminary economic impacts. While this analysis is non-exhaustive and subject to the evolving nature of the tariff regime, it offers a timely perspective on Malaysia’s most pressing external risk in the year.

Our analysis is grounded in official data sources and institutional forecasts, and is intended for readers with a working knowledge of macroeconomic analysis. While we do not offer investment recommendations, we aim to provide a clear, data-driven view of the economic landscape.


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Executive Summary

The global economy in 2H2025 is navigating a complex landscape, shaped by diverging growth trajectories, evolving trade dynamics, and persistent geopolitical tensions. This report, themed “Uncharted Territory,” offers a retrospective on 1H2025 and a forward-looking assessment of macroeconomic conditions, drawing from our January publication “2025 Macroeconomic Outlook: Policy Trade-Offs for Resilient Growth.”

The International Monetary Fund (IMF) and the World Bank present contrasting views on global growth. The divergence underscores the growing complexity in assessing global momentum, particularly as trade and investment flows become more regionally concentrated. While most advanced economies struggle with tepid growth, the US remains a relative outperformer, though policy shifts and inflation risks cloud its medium-term outlook. Emerging Market and Developing Economies (EMDEs) remain the anchor of global growth. Still, Southeast Asia presents a mixed picture, with growth expected between 4.1%–4.2%, led by populous economies such as Indonesia, the Philippines, and Vietnam.

The US economy performed well in 1H2025, but the outlook for 2H2025 is increasingly uncertain amid the US policy shift. Should growth deteriorate, ripple effects could be felt across major trading partners, including Malaysia. The Euro area faces moderate growth prospects, focusing on Germany, Ireland, and Italy to reflect the broader impact of trade tensions and industrial sector weakness. Geopolitical risks and policy fragmentation will likely shape the region’s trajectory in 2H2025. China has demonstrated remarkable resilience, maintaining GDP growth above 5.0% y/y for three consecutive quarters. The 2H2025 outlook remains positive, supported by lessons learned from previous tariff cycles and a more diversified export strategy.

Malaysia’s growth in 2H2025 is expected to moderate, yet we do not foresee a sharp downturn. We project 2025 GDP growth at 3.8%, slightly below Bank Negara Malaysia’s forecast range of 4.0%–4.8%. Household consumption, accounting for over 60% of GDP, remains a key anchor, supported by rising tourist arrivals and robust construction activity. The fiscal deficit target remains achievable despite softer nominal GDP growth. The debt-to-GDP ratio is expected to edge higher, driven more by base effects than steeper borrowings. Labour market conditions remain tight, with unemployment at 3.0%, the lowest since April 2015. However, subdued inflation and low spending propensity may dampen growth. We expect inflation to rise in 2H2025, driven by potential adjustments to RON95 fuel and electricity prices, which account for 8.2% of the inflation basket.

The impact from the external sector remains a key risk for Malaysia. Although almost all major US trading partners are hit by higher tariffs, the 19% “reciprocal tariff” (RT) imposed on Malaysia poses significant challenges. Our analysis shows that 53.9% of Malaysia’s exports to the US are subject to RT. Malaysia’s competitive advantage remains intact, as RT exposure is lower than China’s but comparable to regional peers. However, we are concerned that the “reverse tariff” effects may erode producer surplus.

Meanwhile, we maintain a cautiously optimistic view of the semiconductor sector, which is supported by global digitalisation trends and strategic investments concerning data centres. The healthcare sector will continue to focus on ageing population preparedness and service delivery improvements.

On fixed income, we hold a modestly positive outlook for US Treasuries and Malaysian Government Securities (MGS). We expect the 10-year UST yield to end 2025 at 4.30%, and the 10-year MGS at 3.50%, supported by low inflation and growth risks. Net Private Debt Securities issuance is expected to rise modestly in line with expanding investment activity.

On FX, we forecast a Dollar Index upside to 99.8 by year-end, with USDMYR ending at 4.27. Risks to this outlook include concerns over US fiscal sustainability, the Fed’s independence, and potential portfolio rebalancing after recent equity gains.

AGENDA

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2H2025 Forecasts

	2024	AmBank Forecast 2025F
GDP, y/y%	5.1	3.8
Inflation Rate, %	1.8	1.5
Unemployment rate	3.2**	3.1**
OPR, %	3.00	2.75
USDMYR	4.47*	4.27*
10Y MGS	3.81*	3.50*

GDP by sector, y/y%		
Services	5.3	4.9
Manufacturing	4.2	3.1
Mining	0.9	(4.9)
Agriculture	3.1	2.7
Construction	17.5	11.0

Notes: *Year-end, **Annual average


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Global growth forecasts: Diverging narratives

Global Economic Outlook: Diverging Narratives Amid Fragile Economic Prospects

The divergence in forecasts underscores the complexity of forecasting the current global landscape, given the fluid nature of global trade policy shifts. While the IMF signals cautious optimism, the World Bank and ADB highlight persistent downside risks.

Forecasts	IMF				World Bank				ADB			
			Difference				Difference				Difference	
	Jul-25	2026	2025	(Apr-25)	2026	2025	(Jan-25)	2026	Jul-25	2026	2025	(Apr-25)
World	3.0	3.1	0.2	0.1	2.3	2.4	(0.4)	(0.3)	-	-	-	-
Advanced economies	1.5	1.6	0.1	0.1	1.2	1.4	(0.5)	(0.4)	-	-	-	-
US	1.9	2.0	0.1	0.3	1.4	1.6	(0.9)	(0.4)	-	-	-	-
Euro Area	1.0	1.2	0.2	0.0	0.7	0.8	(0.3)	(0.4)	-	-	-	-
EMDEs	4.1	4.0	0.4	0.1	3.8	3.8	(0.3)	(0.2)	-	-	-	-
China	4.8	4.2	0.8	0.2	4.5	4.0	0.0	0.0	4.3	4.0	(0.1)	0.0
India	6.4	6.4	0.2	0.1	6.3	6.5	(0.4)	(0.2)	6.5	6.7	(0.2)	(0.1)

Forecasts	IMF				World Bank				ADB			
			Difference				Difference				Difference	
	Jul-25	2026	2025	(Apr-25)	2026	2025	(Jan-25)	2026	Jul-25	2026	2025	(Apr-25)
ASEAN	4.1	4.1	0.1	0.2	-	-	-	-	4.2	4.3	(0.5)	(0.4)
Malaysia	4.5	4.0	0.4	0.2	3.9	4.3	(0.6)	0.0	4.3	4.2	(0.6)	(0.6)
Indonesia	4.8	4.8	0.1	0.1	4.7	4.8	(0.4)	(0.3)	5.0	5.1	-	-
Philippines	5.5	5.9	0.0	0.1	5.3	5.4	(0.8)	(0.6)	5.6	5.8	(0.4)	(0.3)
Singapore	-	-	-	-	-	-	-	-	1.6	1.5	(1.0)	(0.9)
Thailand	2.0	1.7	0.2	0.1	1.8	1.7	(1.1)	(1.0)	1.8	1.6	(1.0)	(1.3)
Vietnam	-	-	-	-	5.8	6.1	(0.8)	(0.2)	6.3	6.0	(0.3)	(0.5)

A tale of two perspectives

The International Monetary Fund (IMF)'s July 2025 forecasts point to stronger global growth than it forecast in April amid the better-than-expected US tariffs. Its latest forecasts are 3.0% in 2025 and 3.1% in 2026, marking a 0.2 and 0.1 percentage point increase from April. In contrast, the World Bank projects a more subdued trajectory at 2.3% and 2.4%, with downward revisions of 0.4 and 0.3 percentage points, respectively. The Asian Development Bank (ADB) had also downgraded China and India's 2025 growth forecasts by 0.1 and 0.2 percentage points, respectively.

Growth in advanced economies remains tepid. The IMF sees a slight uptick to 1.5% in 2025 and 1.6% in 2026, while the World Bank is more pessimistic at 1.2% and 1.4%, reflecting the shock of the increases in trade barriers and policy uncertainty, financial volatility, and a dip in confidence. The IMF and the World Bank see the US continuing to outperform its peers, although the latter sharply downgraded its 2025 forecast by 0.9 percentage points.

Emerging Market and Developing Economies (EMDEs) will continue to anchor global growth in 2025 and 2026. The IMF projects 4.1% in 2025, up 0.4 percentage points, while the World Bank trims its outlook to 3.8% amid downgrades of EMDEs with a high degree of trade and investment openness.

ASEAN: Multi-speed economic prospect

From the Multilateral Development Banks (MDBs) viewpoint, the Southeast Asian region presents a mixed picture. The region is expected to grow between 4.1%-4.2%, with favourable prospects for the more populous economies such as Indonesia, the Philippines and Vietnam.

Malaysia receives a notable IMF upgrade to 4.5% in 2025, suggesting confidence in the ongoing fiscal consolidation and strong investment flows amid the construction boom. In contrast, both the World Bank and ADB have downgraded their projections by 0.6 percentage points. ADB appears to be sanguine with Indonesia's growth prospects, without amendments to its April 2025 projections for ASEAN's largest economy. Notably, Thailand and Singapore face the sharpest downward revisions amid structural weakness, the city-state's economic openness, and strong correlations with the cyclical nature of the global economy.

Alas, despite the diverging narratives across institutions, the global economy faces no imminent threats of a recession. The upward adjustments by the IMF, particularly for major economies and EMDEs, underscore a resilient first half of 2025, buoyed by robust domestic demand, controlled inflationary pressures, and accommodative financial conditions.

However, the outlook becomes increasingly opaque as we transition into the second half of 2025 and beyond. The significant recalibration of US trade policy introduces uncertainty that could reshape the global growth path in the coming years. Policymakers and market participants must remain vigilant, agile, and forward-looking as the world economy navigates this uncharted terrain.


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Inflation: Disinflation now, tariff shock later

Exhibit 1: World Inflation: Average consumer prices, y/y%

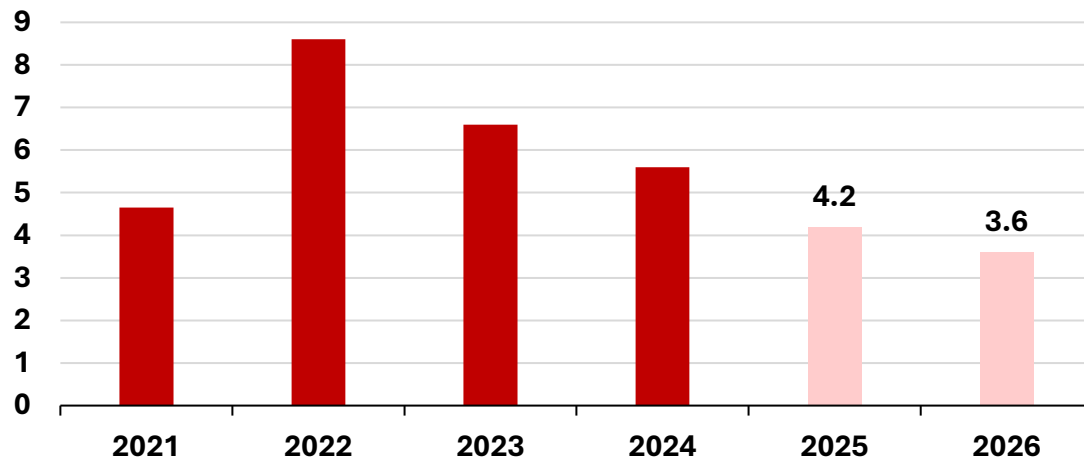
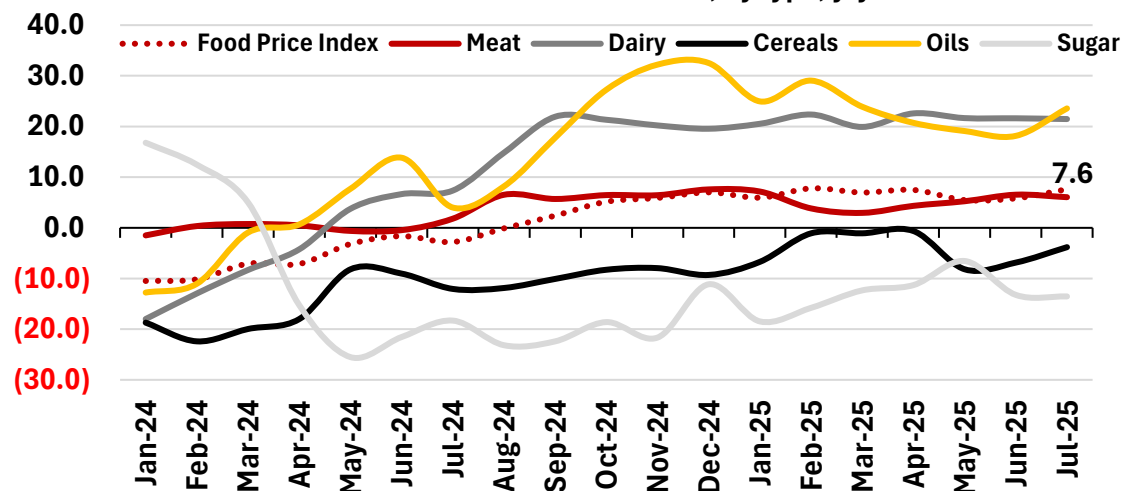


Exhibit 2: World FAO Food Price Index, by type, y/y%



Global inflation

The global inflation landscape has entered a more uncertain and fragmented phase in 2H2025, shaped by shocks and policy shifts. While the IMF expects global headline inflation to moderate steadily to 4.2% in 2025 and 3.6% in 2026, this aggregate trend masks significant cross-economy divergences and emerging structural risks.

Imminent tariff Shock?

A key source of uncertainty stems from the recent overhaul in US trade policy, which resembles the Trump 1.0 era but is more widespread. If historical precedent holds, we anticipate that tariff-induced cost pressures will not only raise inflation in the US but also embed greater persistence along the process. The World Bank has already flagged that price pressures are building along global supply chains, particularly in advanced economies.

The global economy may not witness a major inflationary impact from the US tariff shift just yet, as most tariff negotiations will only conclude in 2H2025. However, we believe it is imminent and will manifest in the latter part of the year.

While the headline global inflation trajectory appears disinflationary, the underlying dynamics are far from settled. 2H2025 and beyond could usher in a period of inflationary divergence, with the US potentially exporting price pressures through trade channels.

We concur with both the IMF and World Bank in emphasising the growing asymmetry in inflation risks. Advanced economies, particularly the US, face persistent inflation, while EMDEs may experience a more subdued and manageable price environment.

World food inflation

The World FAO Food Price Index reveals a complex and volatile global food inflation landscape, with notable fluctuations across key categories such as oils, cereals, and sugar. As of July 2025, the global food inflation stood at 7.6% y/y, indicating a renewed upward trend in global food prices after a period of moderation.

UNFAO data shows that oil and dairy inflation has been trending in double digits since September 2024. Cereals and sugar inflation prints, however, have been relatively stable and remain in the deflationary mode.

Malaysia is shielded but exposed

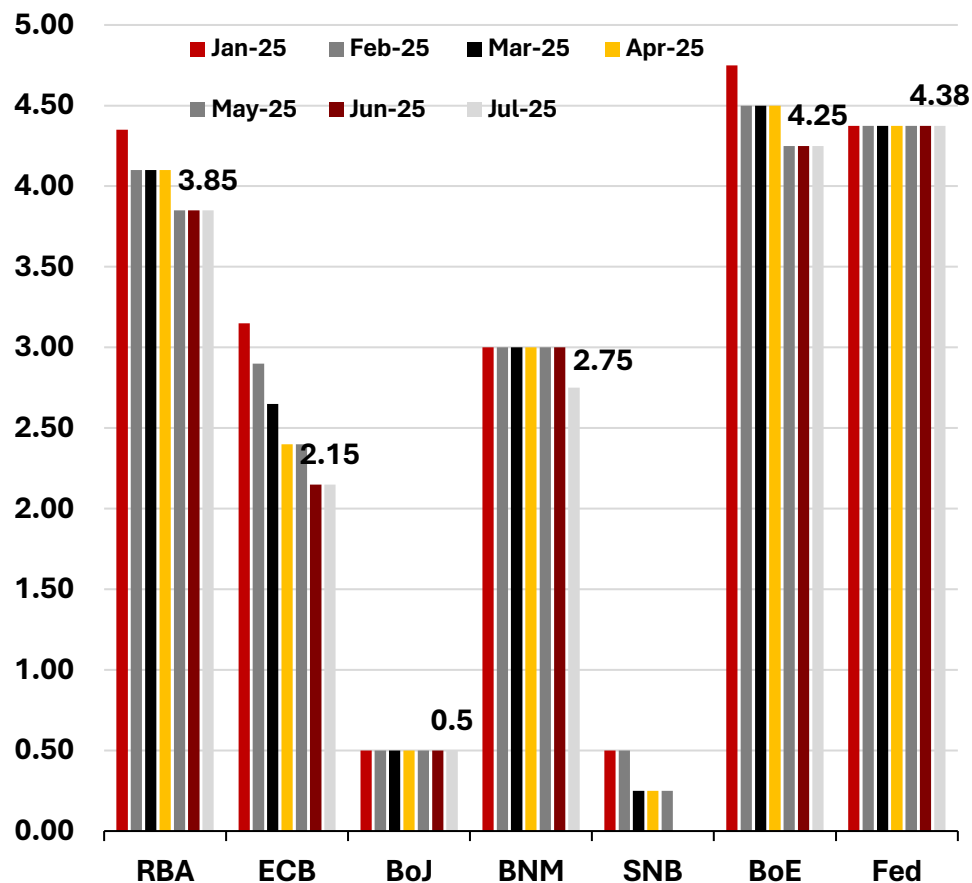
Subsidies for essential staples buffer Malaysia's food inflation outlook, but it is not immune to global volatility. Food and beverage inflation has consistently outpaced headline inflation nearly every month since the pandemic, suggesting that price pressures are seeping through.

For Malaysia, the key risk lies not in the headline inflation figures, but in the underlying composition. As global food prices trend higher, subsidy mechanisms may face fiscal strain, and non-subsidised food categories could continue to drive inflationary divergence. The recent expansion of the Sales and Services Tax (SST) may pressure food inflation, even if staple subsidies continue.


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Interest rates: Inflation is not fully under control

Exhibit 3: Selected Central Banks' Policy Rates, %



Global monetary policy landscape in 1H2025

The comparative central bank rate chart from January to July 2025 reveals a tight global monetary policy stance, particularly among major Western central banks. Asia-Pacific counterparts maintain a more accommodative posture. This divergence reflects asymmetric macroeconomic conditions, inflation dynamics, and policy priorities.

The Federal Reserve (Fed) and Bank of England (BoE) continue to anchor the upper end of the global rate spectrum, maintaining policy rates above 4% throughout 1H2025. This reflects a cautious approach to disinflation, with Fed Chair Jerome Powell signalling a wait-and-see stance amid uncertainty surrounding the inflationary impact of new US tariffs. The lack of rate cuts underscores the Fed's concern over potential inflation persistence, especially if trade frictions escalate.

In contrast, the European Central Bank (ECB) has embarked on a measured rate-cutting cycle, responding to sluggish growth and on-target inflation. The ECB's policy normalisation reflects confidence in its disinflation path but also highlights the fragility of the Euro Area recovery, where monetary easing is seen as necessary to support demand.

Central banks in the Asia-Pacific region, notably Bank Negara Malaysia (BNM) and the Bank of Japan (BoJ), maintain accommodative stances, reflecting benign inflation and subdued growth pressures. BNM cut its policy rate by 25bps for the first time in the post-pandemic era to preempt the inevitable slowdown in external and domestic demand. However, the latter holds up relatively well in 1H2025. The BoJ, meanwhile, continues its ultra-loose policy, consistent with its long-standing battle against deflation and weak domestic demand.

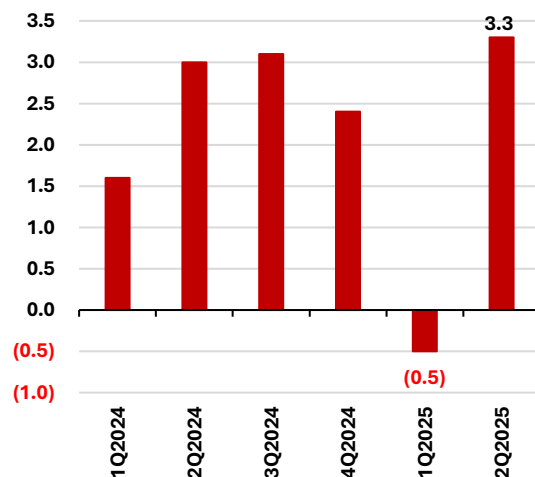
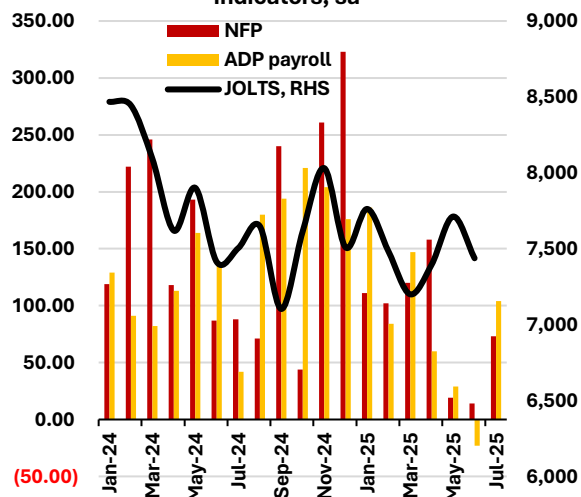
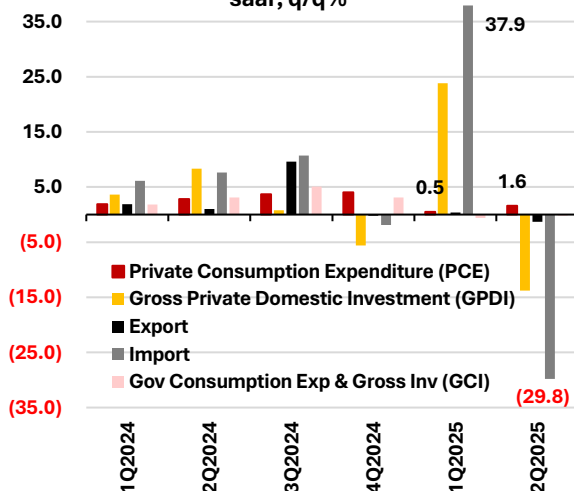
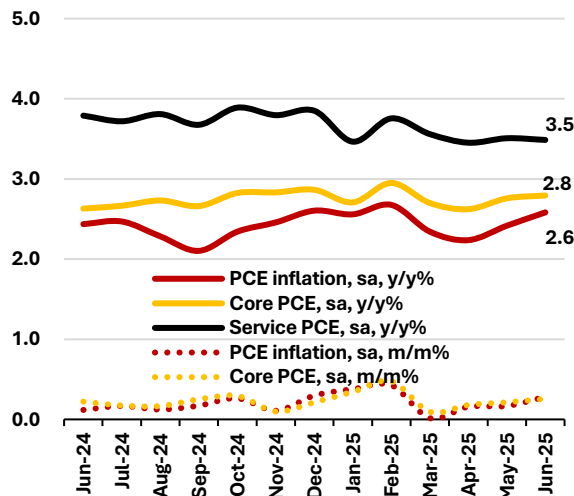
Global interest rate path in 2H2025 will likely be gradual without a looming recession

There is an increasing probability that the US will embark on a gradual easing amid weakening labour market conditions in the remaining months of the year. However, it remains to be seen whether market expectations are on point when tariff-induced inflation is set to manifest in 2H2025 or later.

Overall, the absence of broad-based rate cuts across major central banks signals a lack of confidence that inflation is fully under control. While headline inflation may be easing, central banks remain vigilant as underlying risks remain elevated. The divergence in rate paths reflects not only differing inflation and labour market realities but also varying degrees of policy space and tolerance for growth risks.


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US: Emerging signs of weakness

Exhibit 4: US: Real GDP, saar, q/q%

Exhibit 5: US: Selected labour market indicators, sa

Exhibit 6: US: Real GDP by expenditure, saar, q/q%

Exhibit 7: US: PCE inflation


Performed well in the short-term, medium-term hangs in a balance amid the US policy shift

The US economy posted a robust 3.3% q/q expansion in 2Q2025 (second estimate), rebounding sharply from the 0.5% contraction in the previous quarter. This headline strength was underpinned by resilient private consumption, which accounts for roughly 69% of GDP, supported by a still-tight labour market. However, a significant portion of the growth was driven by a sharp 29.8% decline in imports, reversing the 37.9% surge recorded in 1Q2025. These volatile trade swings likely reflect frontloading behaviour in response to US tariff announcements, as firms rushed to secure supplies ahead of higher duties.

Despite the strong quarterly print, underlying momentum appears to be moderating. Growth in 1H2025 (1.4%) was softer compared to 2H2024 (2.8%), and we expect further deceleration in 2H2025 as the frontloading effect dissipates and US reciprocal tariffs begin to bite. Labour market indicators show early signs of softening, which could affect household spending. At the time of writing, most major trading partners have finalised trade deals, with China being the notable exception, as US President Trump extended the truce by another 90 days.

Investment activity has also shown heightened volatility, and we anticipate subdued capital formation in the coming months as firms grapple with supply chain reconfigurations. The current tariff regime is estimated to be at its highest level since the 1930s, and poses structural challenges for import-dependent industries. Whether importers could readjust supplies fast enough to keep up with the ever-changing trade regime remains to be seen. Without swift adjustments, the economy risks entering a phase of stagflationary pressure, where growth slows while cost structures remain elevated.

Managing downside risks in 2H2025 and beyond

Should the US economy deteriorate in 2H2025, we may see the ripple effects for other major economies with high trade and financial linkages to the US. While a full-blown recession is premature, a pronounced slowdown could amplify downside risks for firms already contending with compressed producer surplus due to elevated input costs from tariff hikes. This concerns export-oriented economies and global manufacturers embedded in US-centric supply chains such as Singapore, Vietnam and Malaysia.

While many countries may still have room to deploy countercyclical policy tools, the US faces a more constrained policy environment. The inflationary nature of its tariff regime complicates the Fed's ability to respond with monetary easing, given its dual mandate of price stability and full employment. With inflation risks elevated, the Fed may have to prioritise between the two mandates.

This leaves fiscal policy as the more viable lever, but rising debt levels could hinder swift and effective action. Moreover, any fiscal expansion could risk undermining credibility and fueling further price instability if inflation remains sticky.

In this context, global investors and policymakers are recalibrating expectations as the situation unfolds. The US, traditionally a source of global demand, may morph into a source of volatility. EMDEs must prepare for spillover risks, particularly those with high exposure to US trade and capital flows.


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Euro Area: Resilient sans tariff impact

Exhibit 8: EA: Real GDP, %q/q, swda

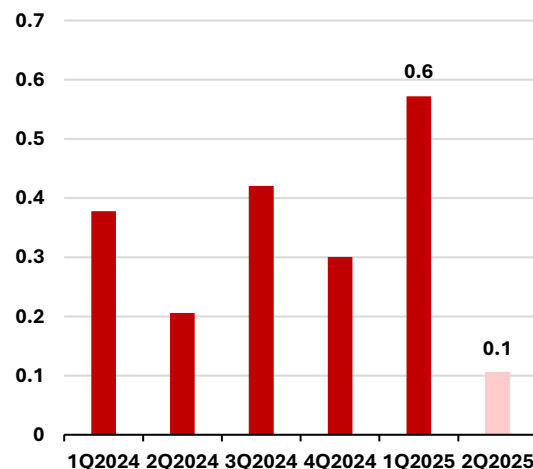


Exhibit 9: EA: Unemployment rate, sa, %

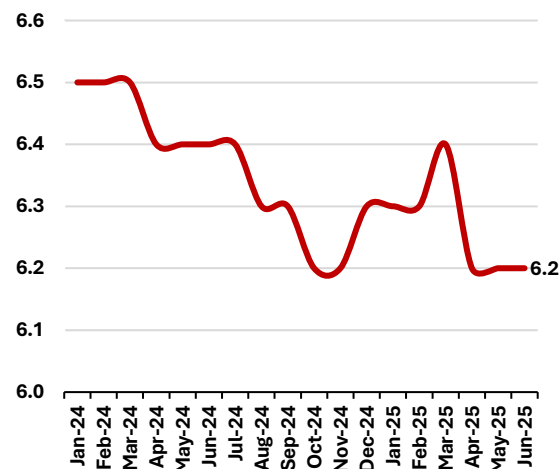


Exhibit 10: EA: Consumer inflation, y/y%

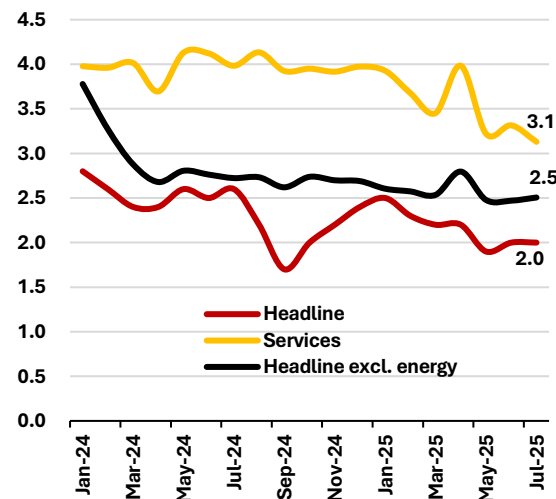
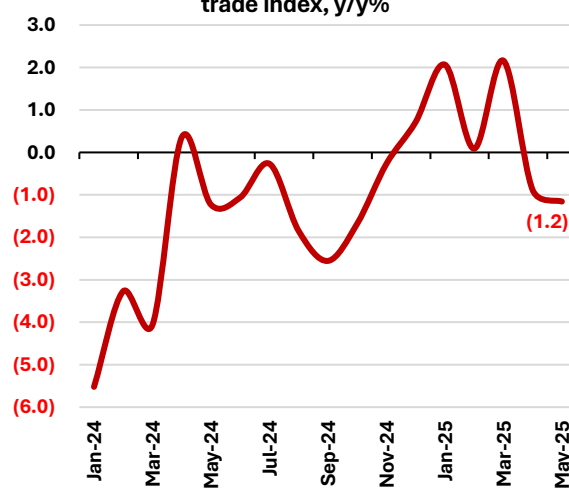


Exhibit 11: EA: Wholesale and retail trade index, y/y%



Growth will likely remain moderate in the immediate to near-term

According to Eurostat's preliminary flash estimate, the euro area's economic expansion slowed sharply in 2Q2025, with real GDP rising by just 0.1% q/q on a seasonally and working day adjusted basis. This marks the weakest growth since 4Q2023 and the steepest deceleration since 4Q2022, signalling a potential shift toward a low-growth near-term trajectory.

The slowdown was primarily driven by contractions in key economies, namely Germany, Ireland, and Italy. Ireland, in particular, saw a dramatic reversal, with GDP plunging from 7.4% to -1.0%, largely due to a downturn in its multinational-dominated industrial sector. While Ireland's Department of Finance cautions against relying solely on headline GDP figures, the decline's scale underscores export-heavy sectors' vulnerability to global demand and supply chain disruptions amid trade uncertainties.

In contrast, 1Q2025 growth stood at 0.6%, supported by investment and trade activity. However, the said data reveals a notable moderation in household consumption and spending by Non-Profit Institutions Serving Households (NPISH) over the past three quarters. This trend may be an early signal of a broader demand-side weakness, aligning with the IMF's projection for moderate growth in the euro area through 2025–2027.

Despite manageable inflation and policy rates, geopolitical tensions and escalating trade frictions continue to weigh on sentiment and external demand. These factors, coupled with industrial sector volatility and weakening household consumption, suggest that the euro area may enter a phase of structural growth moderation, rather than a cyclical downturn.

Geopolitical and trade tensions to shape the economy's 2H2025 outlook

The Euro area's economic landscape in 2H2025 presents a nuanced picture. Moderating inflation, as evidenced by the consistent decline in headline and service inflation, allowed the European Central Bank (ECB) to cut its main financing operations rate by 100bps so far this year. This trend aligns with the ECB's recent pivot toward a more dovish posture, potentially supporting domestic demand and investment amid slowing growth.

However, the steep drop in 2Q2025 growth signals a clear loss of momentum amid weakness in its large and exposed economies, which are exposed to global trade dynamics. Moreover, it is no exaggeration to say that domestic demand may not be strong enough to offset external shocks, although the economy's unemployment rate is relatively stable at 6.2%.

In 2H2025, geopolitical tensions and the evolving US tariff regime pose significant downside risks. Whether a more accommodative monetary policy environment could uplift confidence and investment sentiment remains to be seen.

The euro area enters 2H2025 with a delicate balance, with external risks posing challenges threatening the recovery. The recently concluded 15% tariff for EU goods to the US provides some certainty to trade, but not when the latter threatens to go sectoral with its tariff deal concerning semiconductors and pharmaceutical goods.


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China: Resilience amid external pressures

Exhibit 12: China: Contribution to GDP Growth, y/y%

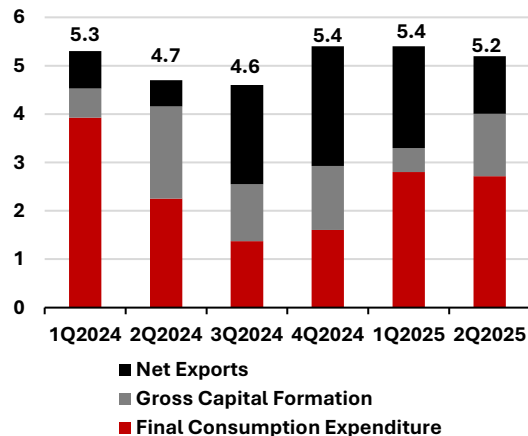


Exhibit 14: China: Share of GDP by expenditure, %

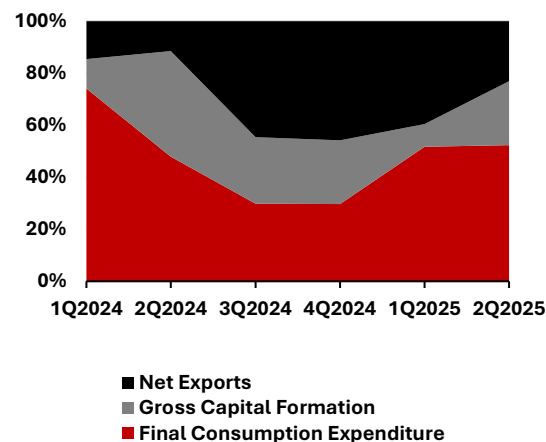


Exhibit 13: China: Consumer inflation, y/y%

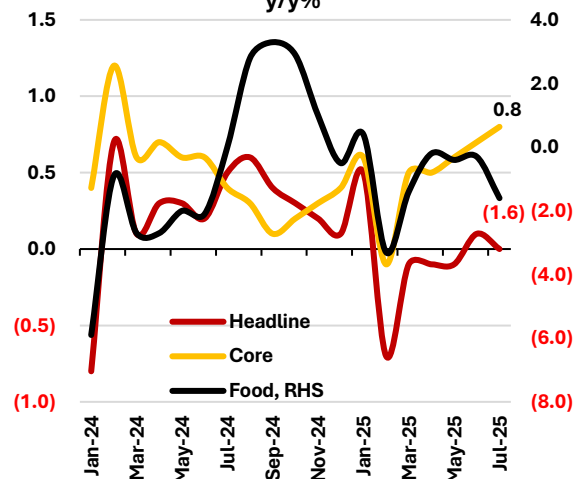
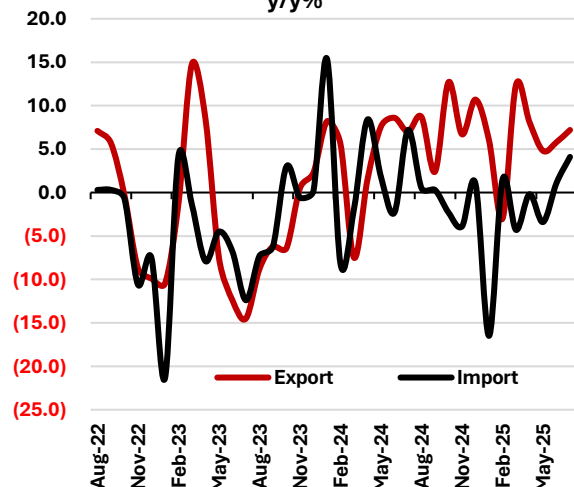


Exhibit 15: China: Trade performance, y/y%



China's structural perspective in 1H2025

Despite escalating geopolitical tensions and unprecedented/astronomical tariff threats from the US, China has demonstrated remarkable resilience, maintaining GDP growth above 5.0% y/y for the past three consecutive quarters. This performance underscores the robustness of its domestic demand base and the strategic agility of its trade and industrial sectors.

Unsurprisingly, we noticed significant frontloading activity in 4Q2024 and 1Q2025, likely in anticipation of the US' tariff threats on Chinese goods (Note: the 145% tariff on Chinese goods is postponed to 9 November 2025). Net exports surged during those quarters as exporters rushed to ship goods ahead of tariff "deadlines" but moderated sharply in 2Q2025 amid the US' Liberation Day.

Final consumption expenditure has remained robust over the past two quarters, providing a stable anchor for growth in 1H2025. This highlights the importance of domestic consumption in China's economic model beyond export-led growth. The resilience in household spending amid external headwinds suggests effective policy support and improved income dynamics by the authorities.

Meanwhile, we noticed a clear disinflationary trend, with headline and food inflation hovering near(ing) 0% y/y. Core inflation, however, has been on an increasing trend of late, but has been low. This subdued inflation environment provides ample policy space for Chinese authorities to maintain an accommodative stance, particularly as external demand weakens. Overall, the underlying demand pressures remain contained.

China's trade performance was highly volatile in 1H2025. We noted exports surged in late 2024 and early 2025, consistent with frontloading behaviour ahead of the US's tariff escalation. Imports remained weak throughout the period, suggesting soft domestic investment demand and possibly a shift toward import substitution strategies.

China's 2H2025 remains positive amid the US tariff truce

We take it that China is more strategically prepared to face high US tariffs, drawing lessons from Trump 1.0, and later, during the Biden administration. China's growth trajectory will depend on its ability to sustain domestic demand, diversify export markets, and accelerate supply chain localisation. The fading frontloading effect and tariff-induced trade compression pose risks to external demand, but if consumption and investment remain resilient, China could sustain its growth momentum even in a highly fragmented global trade environment.

Alas, China's 2H2025 outlook is positive, thanks to the extension of the US tariff truce. However, it will also depend on how the economy can effectively pivot from external to internal drivers. The disinflationary backdrop is a blessing, allowing for pro-growth policies. Even if Chinese exports to the US face speed bumps in 2H2025, we believe that China can effectively export its excess industrial capacity abroad to other markets, as evidenced by the massive global appeal and acceptance of Chinese auto exports over the past year or so.


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Malaysia: Growth risks skewed to the downside

Exhibit 16: Real GDP growth, y/y%

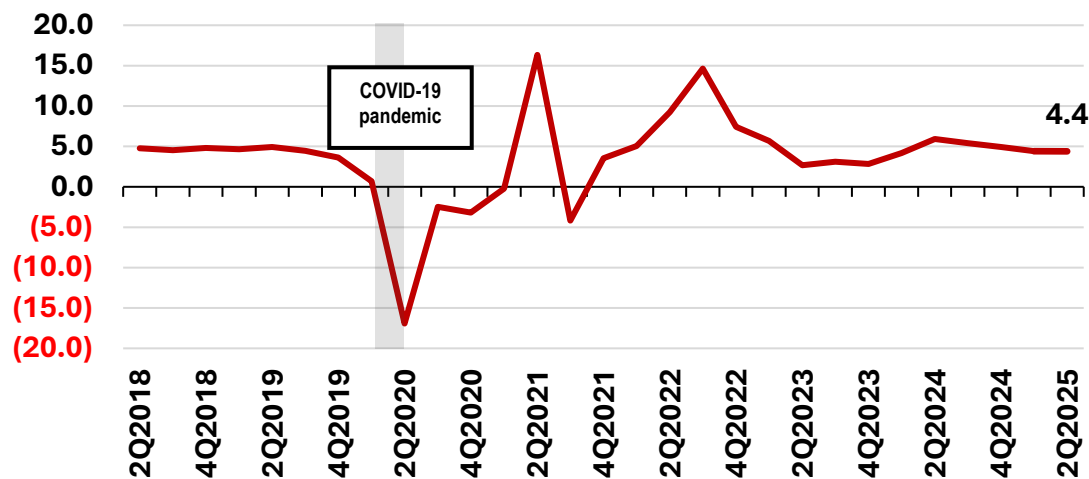
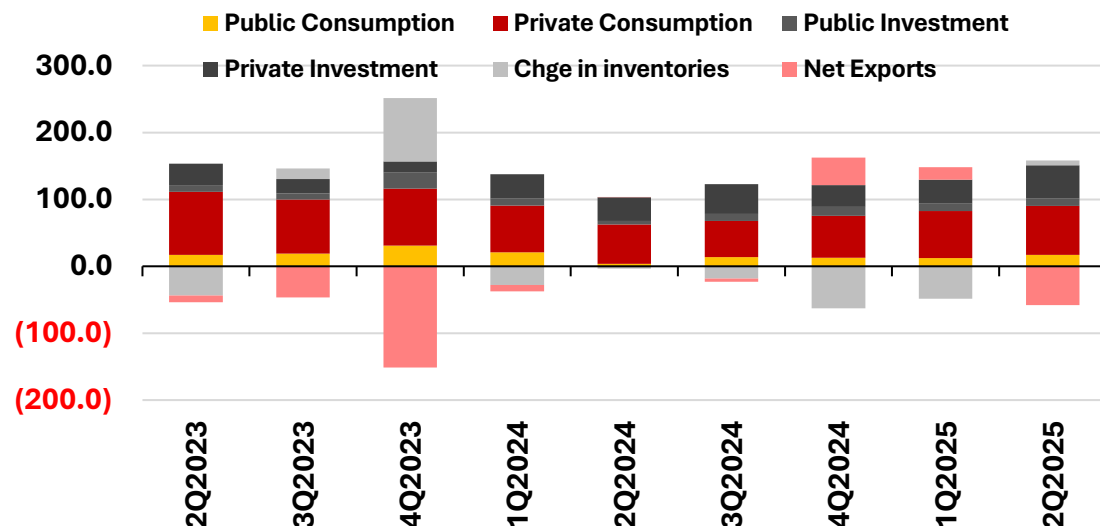


Exhibit 17: Contributions to real GDP growth, percentage points (pp)



A tale of two halves, 2H2025 will exhibit more downside risks to growth

Malaysia's economy entered 2025 on a solid footing, but growth momentum has shown signs of softening as global uncertainties stemming from trade policies and geopolitical tensions begin to weigh on sentiments. GDP growth moderated to slightly below its long-term average in 1H2025, with both 1Q and 2Q recording 4.4%, and we expect further deceleration in 2H2025 as the full impact of US tariffs materialises and the temporary boost from frontloading fades.

That said, we do not anticipate a sharp downturn or recession in the near term as resilient household consumption, rising tourist arrivals, and robust construction activity are expected to continue supporting growth. On balance, we project 2025 GDP growth at 3.8%—slightly below BNM's revised projected range of 4.0% to 4.8%—though greater clarity on global trade policy and any easing of US trade barriers could present upside potential.

Comparing Malaysia and ASEAN's growth in 1H2025

Malaysia recorded a growth of 4.4% y/y in 1H2025, which is a respectable performance as it was higher than Singapore and Thailand. However, when compared to the region's largest and fastest-growing economies, namely Vietnam, the Philippines, and Indonesia, Malaysia's momentum appears to be slowing. In fact, Malaysia saw the sharpest drop in growth among ASEAN countries, falling from 5.7% in 2H2024 to 4.4% in 1H2025.

This decline was mainly due to a steep fall in net exports, which swung from a strong growth of 29.2% in 2H2024 to -26.5% in 1H2025. This drop is worth noticing given Malaysia's high trade exposure, being the third-ranked third in ASEAN with trade-to-GDP at 149.5% in 2024. Notably, other highly trade-dependent economies like Singapore and Vietnam managed to maintain more stable growth in 1H2025, suggesting that Malaysia's export sector could be more vulnerable to recent global trade disruptions than its regional peers. We attempt to shed some light on this in the latter part of this report.

Solid labour market to keep growth steady

One encouraging sign for Malaysia's economy is the strength of private consumption, which has held up well over the past three halves. In 2024, Malaysia ranked second in ASEAN from the perspective of private consumption to GDP at 60.8%, behind the Philippines at 76.1%.

Since 1H2024, private consumption has consistently grown above 5.0%, and in 1H2025, it even picked up slightly to 5.2% versus 5.0% in 2H2024. This resilience is primarily supported by its solid labour market, low unemployment and rising wages. Key policy measures such as the civil service salary adjustment, a higher minimum wage, and the Progressive Wage Model (PWM) rollout have helped boost disposable income.


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Tariff-driven headwinds ahead

Exhibit 18: Merchandise exports, y/y%, 3-month moving average (3mma)

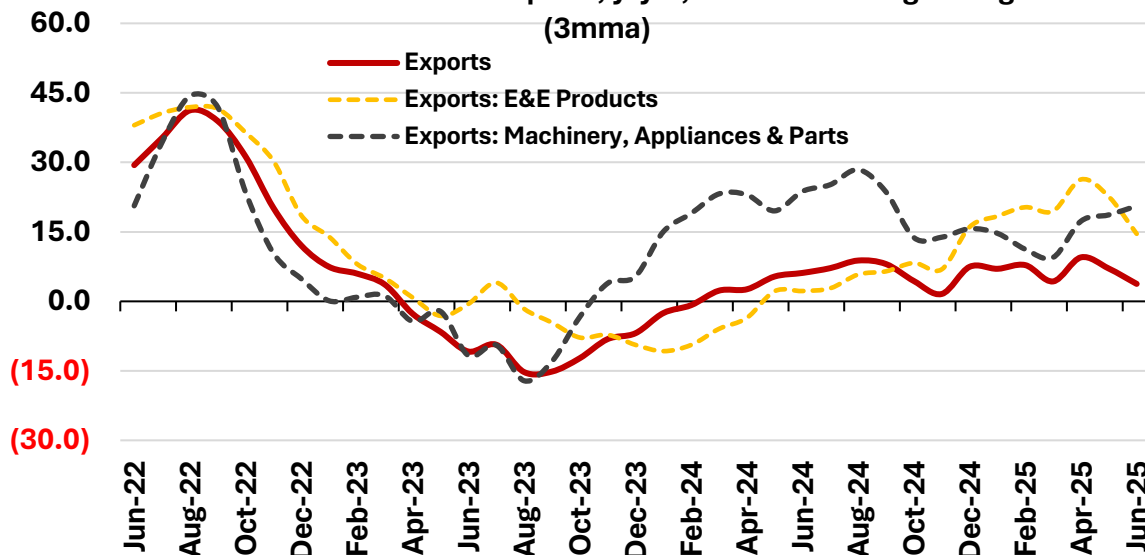
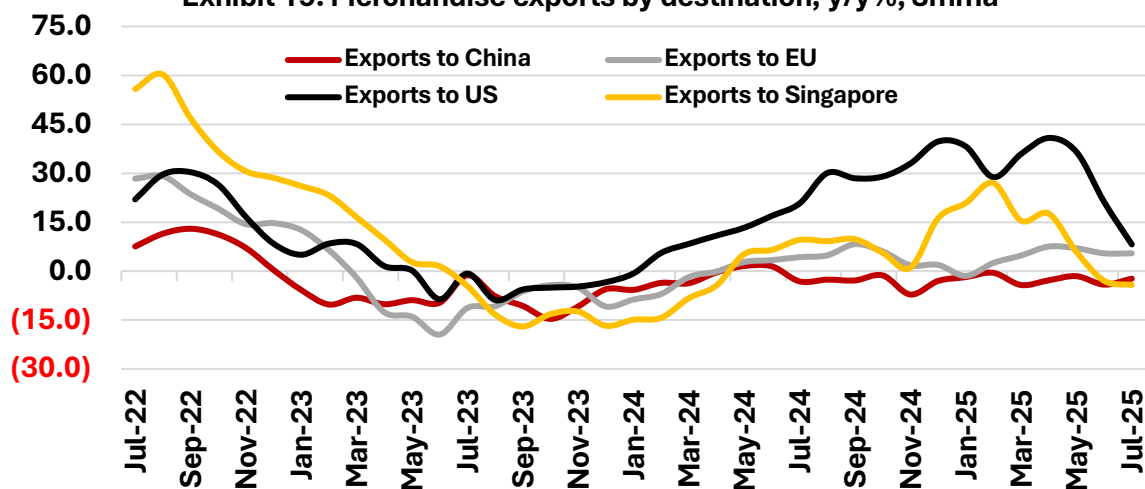


Exhibit 19: Merchandise exports by destination, y/y%, 3mma



A huge jump in US tariffs on Malaysian goods

Just ahead of the August 1 deadline, the US and Malaysia concluded a trade deal under which the US agreed to lower its tariff rate on Malaysian goods to 19%, down from the previously threatened 25% and the same as neighbouring countries such as Thailand, Indonesia and the Philippines. While Malaysia's competitive advantage will likely remain at the status quo, producer surplus may take a hit in the early months of implementation. The current tariff rate marks a sharp increase from the average Most Favoured Nation (MFN) applied rate of 3.4%. It will inevitably weigh on exports, given that the US accounts for about 13% of Malaysia's total exports.

For now, the US exclusion of selected items, particularly semiconductors, from the reciprocal tariffs provides some relief. With semiconductors accounting for nearly a quarter of Malaysia's total exports, sustained global semiconductor demand underpinned by technology advancements should give critical support to the external sector. However, there is a risk that the US may target semiconductors, either by extending reciprocal tariffs to the sector or through non-tariff measures such as export restrictions on chips, which could be damaging for Malaysia, given that the US accounts for about 20% of its semiconductor exports.

While exports are expected to weaken, a concurrent import slowdown is also anticipated due to the strong export-import link. As such, we do not foresee a significant drag from net exports on overall growth.

Current account narrows to a level unseen since 1993

Malaysia's trade balance is beginning to "normalise" after the post-pandemic export surge. It fell sharply from MYR41.0 billion in 1Q2025 to MYR14.5 billion in 2Q2025, driven by export contractions in May and June. On a year-on-year quarterly basis, the trade balance has been on a downward trend since 3Q2021. However, it briefly rebounded in late 2024 and early 2025 due to frontloading by exporters anticipating disruptions from the US trade policy shift under President Trump's second term.

From a balance of payments perspective, Malaysia has maintained a current account surplus for 110 consecutive quarters as of 2Q2025. However, the latest surplus stood at merely MYR264.9 million and was the lowest since 3Q1993, reflecting a sharp drop in goods and services surplus and weaker secondary income inflows.

While the goods and services balance fell from MYR35.0 billion to MYR13.7 billion in 2Q2025, there were more outflows of secondary income and lesser inflows of primary income. BNM views this narrowing as "temporary," expecting a rebound once key private sector projects reach completion in 2H2025.

External headwinds, including dissipating frontloading effects and broad-based softness in external demand, will likely weigh upon trade prospects in 2H2025. We do not see Malaysia's current account coming in lower than 2Q2025, but it could remain narrow if trade remains under pressure.


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Domestic demand to provide buffer

Exhibit 20: Private consumption vs. retail sales, y/y%

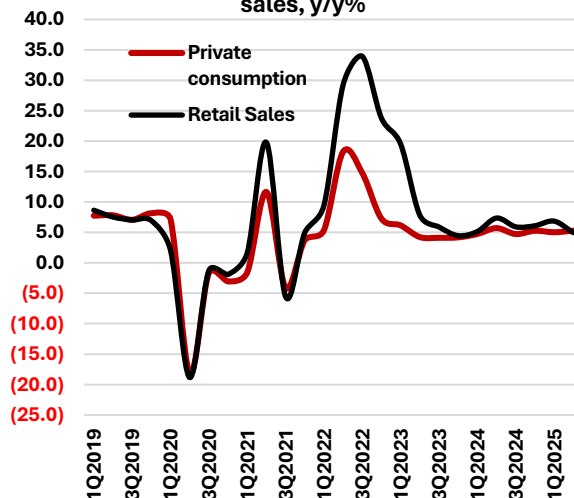
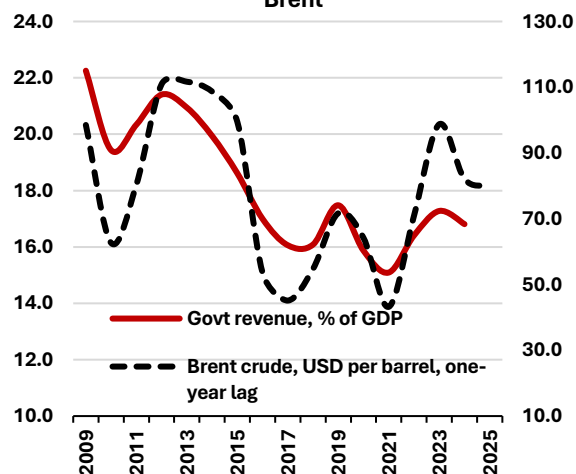


Exhibit 21: Government revenue vs. Brent



Robust domestic demand amid an investment upcycle

Private consumption, which accounts for over 60% of GDP, will remain a key anchor of growth. While household caution may persist as uncertainties still loom, consumption is expected to stay resilient, underpinned by:

- A healthy labour market, as evidenced by a record low unemployment rate and strong wage growth following civil servant salary increases, the statutory minimum wage hike from RM1,500 to RM1,700 and the implementation of PWM;
- Subdued inflation;
- The 25bps Overnight Policy Rate (OPR) cut in July; and
- Continued government cash handouts under various schemes: Sumbangan Tunai Rahmah (STR) and Sumbangan Asas Rahmah (SARA).

While global trade policy uncertainty poses a risk of delayed or reassessed investment decisions, Malaysia's investment outlook remains broadly positive. The continued rollout of large-scale infrastructure projects such as the East Coast Rail Link (ECRL) and the Penang Mutiara Line LRT, alongside the realisation of approved private investments (2024-3M2025: RM474.2 billion) is expected to sustain momentum into coming quarters. Investor interest remains underpinned by various initiatives under the New Industrial Master Plan (NIMP) 2030, National Energy Transition Roadmap (NETR) and National Semiconductor Strategy (NSS), as well as the data centre construction boom and development of several economic zones such as the Johor-Singapore Special Economic Zone (JSSEZ).

Fiscal deficit target remains achievable despite persistent uncertainties

The government's target to narrow the fiscal deficit to 3.8% of GDP in 2025 (2024: 4.1%) is achievable, although the path may be uneven as persistent uncertainties could pose challenges to fiscal consolidation. Unforeseen headwinds may necessitate additional fiscal support. Lower global crude oil prices – averaging around USD70 per barrel YTD, below the budget assumption of USD75–80 per barrel – pose downside risks to revenue. That said, the government's ongoing efforts to broaden the tax base represent a positive step in strengthening fiscal resilience.

The government debt-to-GDP ratio is expected to edge higher this year (2024: 64.6%), driven mainly by softer nominal GDP growth rather than a surge in borrowings. Despite this upward pressure, statutory debt is expected to remain within the current debt ceiling of 65%. Risks are further contained by the low share of external debt and the largely domestic debt profile.

Exhibit 22: Approved private sector investments, RM billion

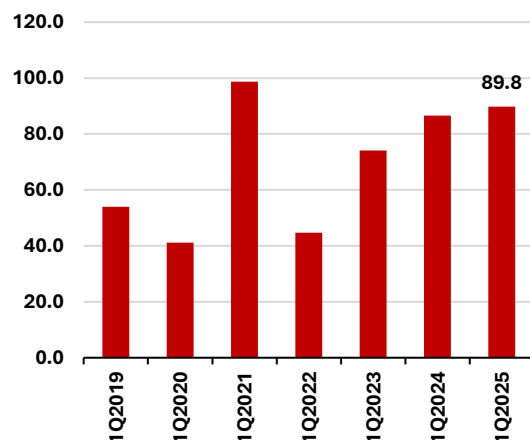
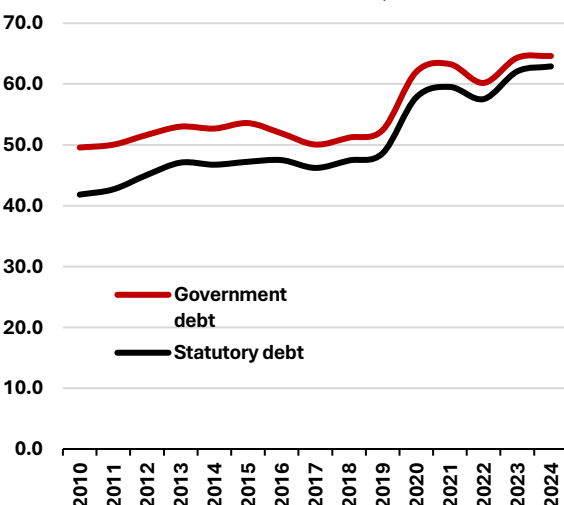


Exhibit 23: Government debt, % of GDP




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1H2025 Fiscal Position

2025			
Description	Budget	Actual 1H	% Actual 1H
	(MYR mil)		
Revenue	339,706	147,624	43.5%
Expenditure	419,679	188,084	44.8%
Fiscal balance	(79,973)	(40,460)	50.6%

2024			
Description	Budget	Actual 1H	% Actual 1H
	(MYR mil)		
Revenue	307,600	139,081	45.2%
Expenditure	393,000	190,646	48.5%
Fiscal balance	(85,400)	(51,565)	60.4%

2023			
Description	Budget	Actual 1H	% Actual 1H
	(MYR mil)		
Revenue	291,500	148,406	50.9%
Expenditure	385,440	188,190	48.8%
Fiscal balance	(93,940)	(39,785)	42.4%

Early concerns about achieving the fiscal deficit target were dispelled

In 2024, there were notable concerns surrounding the government's ability to meet its fiscal deficit target of 4.3%, particularly due to lower-than-expected revenue collection in 1H2024. Revenues during this period represented only 45.2% of the budgeted amount, a decline from 50.9% in the corresponding period of the previous year (1H2023). Conversely, expenditure was relatively stable and similar to the levels observed in 2023, hovering around 48%. Consequently, the fiscal deficit for 1H2024 surged to 60.4%, significantly above the 42.4% recorded in 1H2023.

These apprehensions were well-founded, given the government's plan for a comprehensive review of civil service salaries in August 2024, a process last conducted in 2012. Emoluments represent the largest share of government fiscal commitments, and the anticipated salary adjustments, combined with a sluggish revenue increase, raised questions among analysts regarding the feasibility of achieving the 4.3% fiscal deficit target.

However, as the year progressed, the situation improved markedly. Revenues rebounded, ultimately reaching MYR321,617, exceeding budget projections by 4.6%. Meanwhile, the increase in expenditure was contained at a modest 2.7%. This favourable development enabled the government to outperform its fiscal deficit target, achieving an actual deficit of 4.1%, which was a reassuring result compared to the initial concerns earlier in the year.

Risks to achieving the fiscal deficit are primarily external

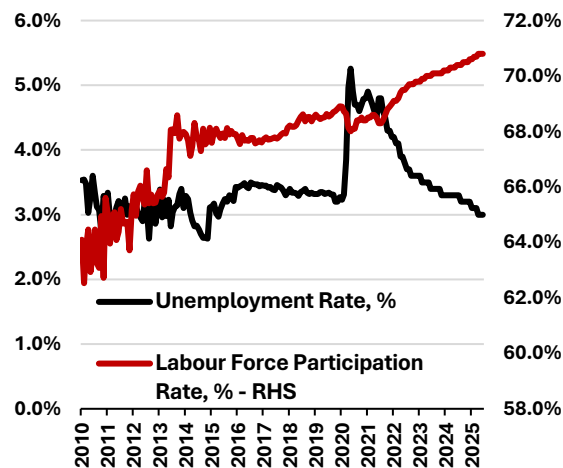
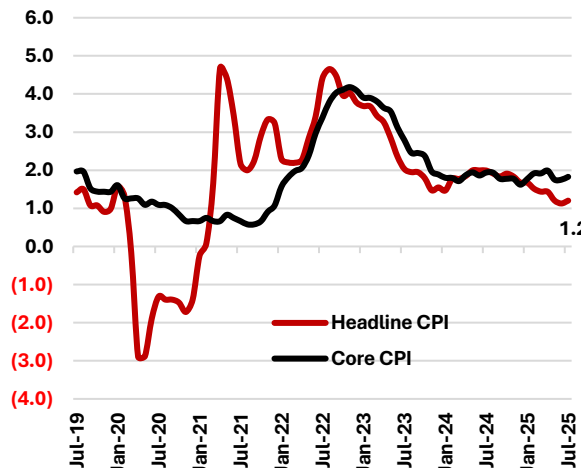
In 1H2025, revenues as a percentage of the budgeted amount declined to 43.5%, reflecting a downturn compared to the same period last year. This development aligns with our expectations, given the moderation in economic growth that could have adversely affected direct tax collection. Notably, the expenditure ratio has also declined, recorded at 44.8% in 1H2025, significantly lower than in the previous two years. This improvement and a fiscal deficit ratio to Budget 2025 of 50.6% underscore the government's commitment to fiscal consolidation.

We foresee little risk to achieving the fiscal deficit target of 3.8% for two reasons. First, we anticipate a continued labour market tightness, which is poised to facilitate a greater inflow of revenues from the planned expansion of the Sales and Service Tax (SST) beginning in July 2025, estimated to generate an additional MYR 5 billion. Second, the implementation of the second tranche of the civil service salary review is slated for January 2026, suggesting that government expenditures will remain relatively predictable throughout 2H2025. Furthermore, we posit that the recent special announcement by Prime Minister Anwar to incur an additional MYR 2.8 billion in spending represents less than 1% of the total Budget 2025 allocation.

Nonetheless, it is prudent to recognise that downside risks to achieving the 3.8% fiscal deficit target may arise from unforeseen external headwinds that could necessitate fiscal interventions. At the very least, the government could bring forward the planned emolument review this year to support private spending in 2H2025.


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Low propensity to spend

Exhibit 24: Labour Market, %

Exhibit 25: CPI, y/y%


Low propensity to spend despite tight labour market conditions

Malaysia's labour market continued to gain momentum, with the unemployment rate recorded at 3.0% in June (May: 3.0%) for the third straight month, marking its lowest level since April 2015. Additionally, the long-term unemployment, which refers to those who are jobless for over a year, accounted for just slightly over 5% of the actively unemployed, suggesting the ability of people to find jobs in a shorter period. Besides, the labour force participation rate remained at a new record high of 70.8% during the month (May: 70.8%), thanks to an encouraging economic environment, which saw the wages in both manufacturing and services on an upward trend. Concurrently, this is positive for the household consumption as of now (1H2025: 5.2% vs. 2024: 5.1%).

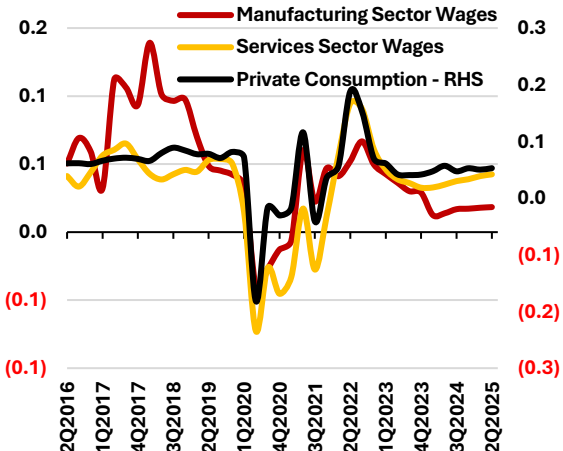
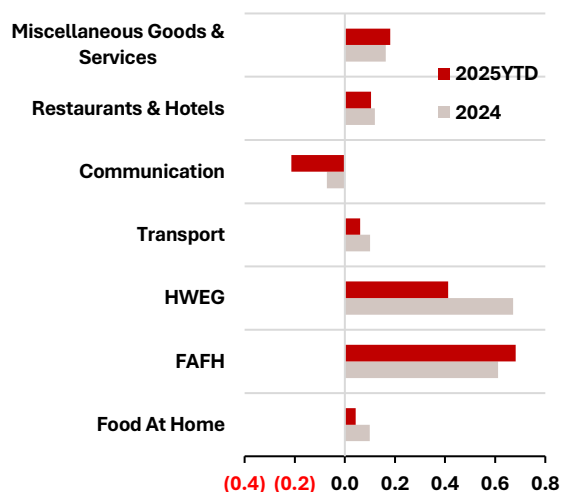
Modest inflation pressures anticipated in 2H2025, but no more OPR cuts for the rest of the year

Headline inflation had been moderating through 1H2025 before edging higher in July following the Sales and Services Tax (SST) expansion. It eased to 1.1% in June from 1.7% at the start of the year, averaging 1.4% in 1H2025 (2024: 1.8%). The disinflationary trend was driven by lower production costs, partly due to softer global crude oil prices, a relatively stronger ringgit that helped reduce import costs, and subdued demand-side pressures, as evidenced by four consecutive months of producer price deflation as of June 2025.

In light of the subdued inflation in 1H2025 and our expectation for only a modest pickup in 2H2025, we expect full-year inflation to average 1.5%, at the lower bound of BNM's forecast range of 1.5% to 2.3%. Downside pressures from lower electricity tariffs and muted demand are expected to partly offset the upside risks from the SST expansion, targeted RON95 fuel subsidy rationalisation and water tariff adjustments in selected states. While RON95 fuel – which accounts for 5.5% of the CPI basket – may experience price adjustments that could trigger spillover effects given its role as key input cost, we view this risk as manageable.

As we expected, Bank Negara Malaysia (BNM) delivered its first rate cut since July 2020 at the July meeting, lowering OPR by 25 bps to 2.75% and ending its 26-month rate pause. While the cut was a pre-emptive move in response to mounting global risks, it should not be interpreted as the start of an aggressive easing cycle. We believe the 25bp cut is sufficient to support near-term growth, with domestic fundamentals remaining broadly solid. Given the limited risk of an imminent recession, we do not see another cut over the remainder of 2025, specifically in the September and November meetings. Historically, BNM has only delivered back-to-back rate cuts during periods of recession.

While a subdued inflation should reflect an ease in living costs, the low demand could threaten growth. Additionally, the low inflation rate did not align with the country's latest unemployment rate reading. In other words, tepid household spending suggests a low propensity to spend following uncertainty from concerns over global tensions, such as US policy changes and geopolitical developments, and domestic supply-side policy changes. Therefore, we foresee that there could be a gradual uptick in the unemployment rate to 3.2% by the year-end, as weaker demand begins to weigh on hiring activity.

Exhibit 26: Private Consumption vs. Wages, y/y%

Exhibit 27: Inflation contribution, pp



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Semiconductor: Cautiously Optimistic

Exhibit 28: GSS vs. E&E, y/y%

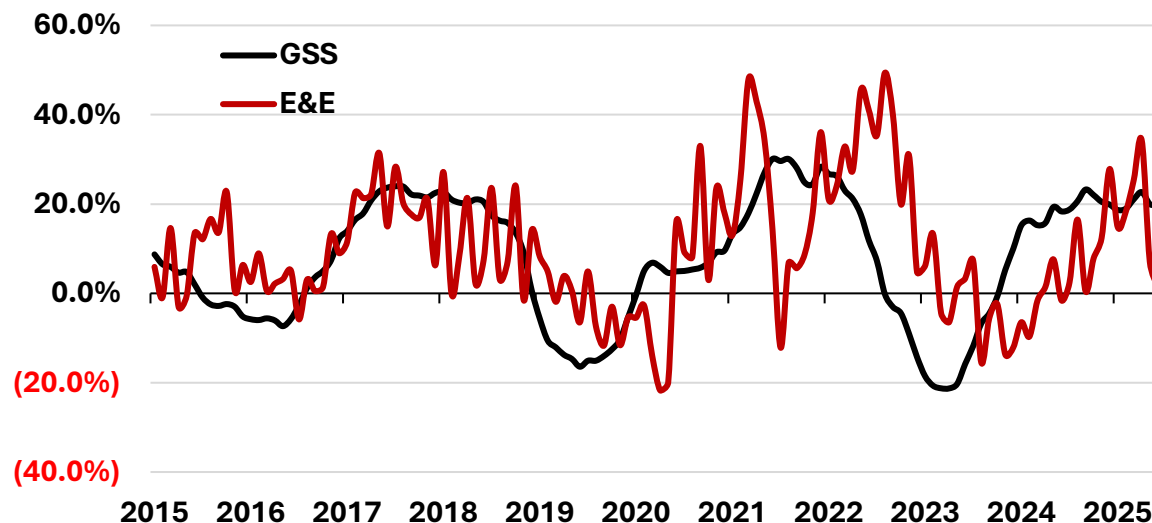
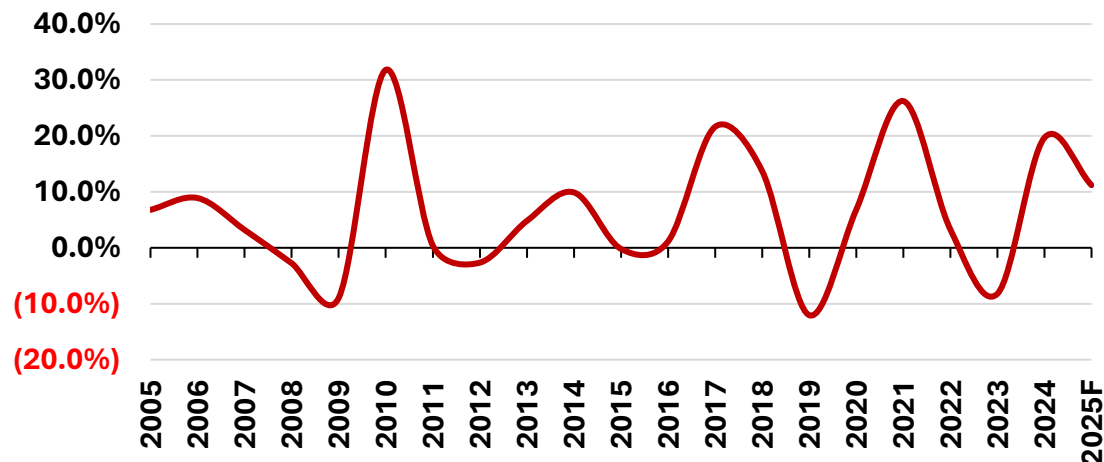


Exhibit 29: Global Semiconductor Market growth, y/y%



Sector outlook remains strong amid policy clarity despite US tariff threats possibility

On the export front, the manufacturing sector saw its sales increase to 5.8% in 7M2025 as compared to 4.8% for the same period last year, lifted by electrical and electronic products (E&E) (7M2025: 17.4% vs. 7M2024: -1.2%)

Last year, Malaysia recorded a historic high of MYR384.4 billion in investment, which saw the manufacturing sector attract over MYR120 billion, led by the E&E segment at MYR55.8 billion. In the latest update, the country started 2025 on a strong note, securing MYR89.8 billion in approved investment during 1Q2025, a 3.7% y/y increase from the previous year despite ongoing global economic uncertainties. Foreign investments dominated the landscape, contributing MYR60.4 billion or 67.3% of total investments, while domestic investments (DI) accounted for MYR29.4 billion or 32.7%.

Additionally, the steady growth was supported by the E&E segment at MYR8.6 billion in the said period. This underscores the country's role as a manufacturing powerhouse. Besides, the E&E industry contributes significantly to Malaysia's exports, earning around 40% as of 2024, vital in shaping industrial development. This could be seen when the country's E&E exports flourished amid frontloading, maintaining its double-digit growth since November last year.

The global semiconductor sales (GSS) data from the Semiconductor Industry Association (SIA) continued to grow substantially in June 2025, maintaining its double-digit growth of 19.9% y/y (May: 20.0%) since December 2023. Following a strong rebound in 2024 at 19.7% y/y (2023: -8.2%), the global semiconductor market is expected to expand by 11.2% in 2025.

Such favourable growth, buoyed by continued strength in the Logic and Memory segments, is expected to post robust double-digit increases, fuelled by ongoing demand in areas such as artificial intelligence, cloud infrastructure, and advanced consumer electronics.

In the latest development, Intel reaffirms its commitment to Malaysia with a MYR50 billion reinvestment and workforce expansion plans to expand further in the coming year. This supports the country's vision as a global semiconductor under the New Industrial Master Plan 2030 (NIMP 2030) and the National Semiconductor Strategy (NSS).

Meanwhile, the US imposed a 19% tariff on Malaysian goods, placing the country in the same range as its neighbours, namely Indonesia, the Philippines, and Thailand. Though semiconductors are currently exempt from the tariff, Malaysia needs to prepare for the possibility of the US imposing the tariff on the semiconductor industry amid a review by the country, according to Investment, Trade and Industry Minister Tengku Zafrul Aziz.

However, the semiconductor industry can benefit from the recent tabling of 13MP, whereby Prime Minister Anwar Ibrahim aims to implement a high-value, high-technology semiconductor industry flagship project, targeting MYR1 trillion in E&E exports by 2030. Such a vision is part of the National Semiconductor Strategy, launched in 2024 to help Malaysia evolve into a full-fledged design-to-fab semiconductor ecosystem. The plan seems to be aligning with NIMP 2030, which is eyeing a 6% growth in manufacturing's contribution to GDP, particularly through exports.


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Healthcare: Towards ageing population

Exhibit 30: Medical vs Overall Inflation, y/y%

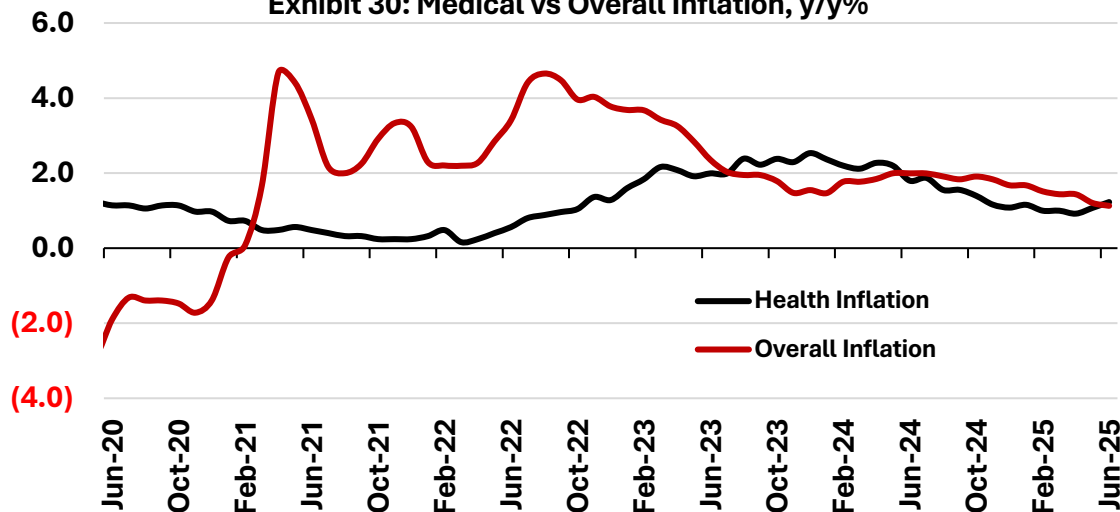
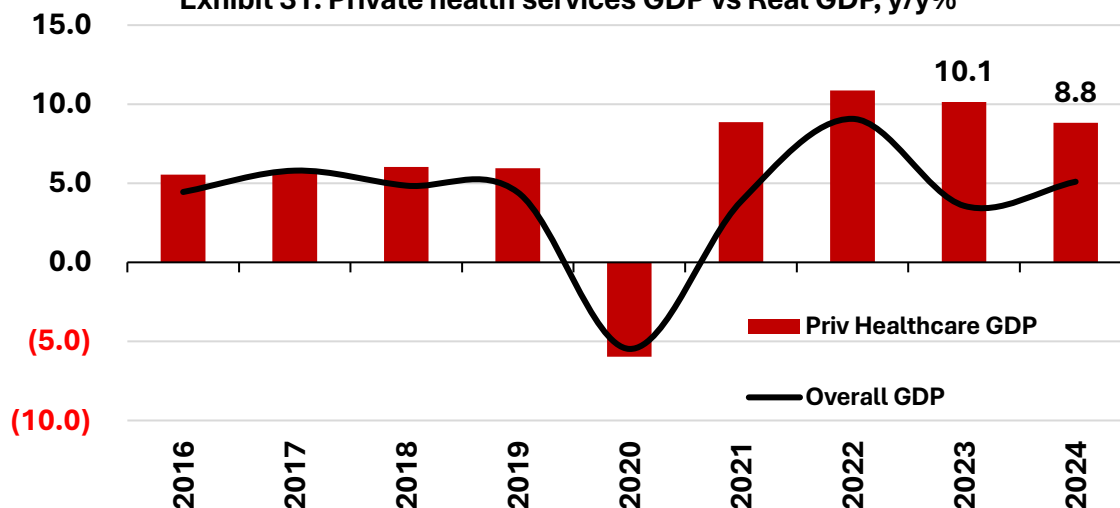


Exhibit 31: Private health services GDP vs Real GDP, y/y%



Continued government efforts encourage an optimistic outlook on the sector

As Malaysia experiences an ageing population, advancing towards the aged nation status by 2030, coupled with the rise in chronic diseases, healthcare expenses are expected to increase significantly. This surge in medical costs is driven by the growing prevalence of non-communicable diseases, demographic shifts toward older age groups, rising labour costs in the healthcare sector, and continuous advancements in medical technology. From 2021 to 2024, private healthcare experienced an average annual growth rate of 9.67%, significantly outpacing the GDP growth of 5.4%. This trend highlights a rising demand for private healthcare services.

Malaysia is steadily establishing itself as a global centre for medical tourism, with projections indicating it will generate MYR2.9 billion in revenue in 2025 (according to the Malaysia Healthcare Travel Council). Most healthcare travellers come from China, the UK, Australia, and Japan. The anticipated admission rise is bolstered by Malaysia's ageing population, which is projected to grow by 2% every five years from 2025 to 2040.

In response to the rising demand for healthcare services, the ongoing privatisation of the healthcare system is seen as a strategic move to enhance operational efficiency, reduce costs, and elevate the overall quality of care. In Budget 2025, healthcare remained a key focus, consistently accounting for an average of 9.9% of total government spending over the past five years. The latest allocation of MYR45.3 billion marks a 10% increase from the MYR41.2 billion designated in 2024, making it the second-largest expenditure in the national budget. 1Q2025, the sector secured MYR308.7 million in private investment, reflecting a significant decline from a MYR868.8 million high recorded in 1Q2024.

Additionally, under the recently announced 13th Malaysia Plan (13MP), the Ministry of Health (MOH) is committed to strengthening healthcare service delivery and accelerating digital transformation, backed by a substantial MYR40 billion allocation. A key focus of the reform agenda is improving health financing and governance. This includes:

- Expanding the Rakan KKM initiative;
- Offering private companies and insurance policyholders the option to access paid services at public healthcare facilities;
- To broaden access, private providers will introduce standardised basic health insurance or takaful products, enabling the public to obtain services from private healthcare facilities and Rakan KKM at reasonable costs; and
- Outsourcing high-cost services via expanded public-private partnerships.

Malaysia's expanded SST brings private healthcare into the tax net with a 6% service tax on all services provided to non-Malaysian patients, while care for Malaysian citizens remains fully exempt. Though minimal impact is expected on major hospitals, most revenue comes from domestic patients, and income from medical tourists typically represents a small proportion of total revenue. By targeting only non-citizen healthcare consumption, the SST expansion aims to broaden Malaysia's fiscal base without increasing out-of-pocket costs for local patients. The additional revenues, part of an expected RM5 billion in 2025 from the broader SST reforms, will help fund public-health initiatives and strengthen social safety nets under the MADANI economic framework. We remain confident in the sector's continued growth, fueled by rising private sector investment, proactive government policies, and increasing demand from international medical tourists.


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FX: Major Currencies

Exhibit 32: A slight departure of market perceptions of UST as a safe-haven asset...

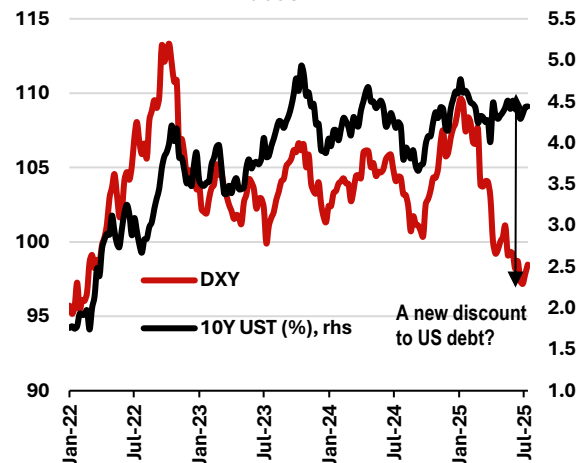


Exhibit 34: A decline in inflation risks also contributed to the DXY's recent drop

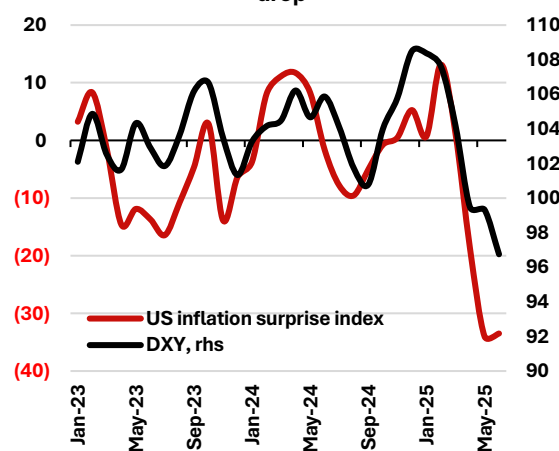


Exhibit 33: ... coming amid bearish buildups in dollar positioning

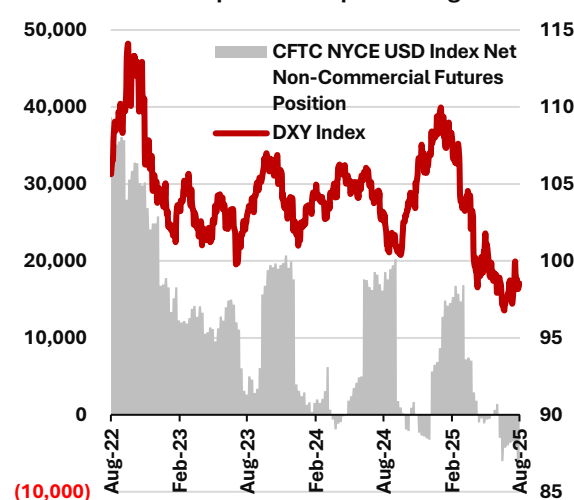
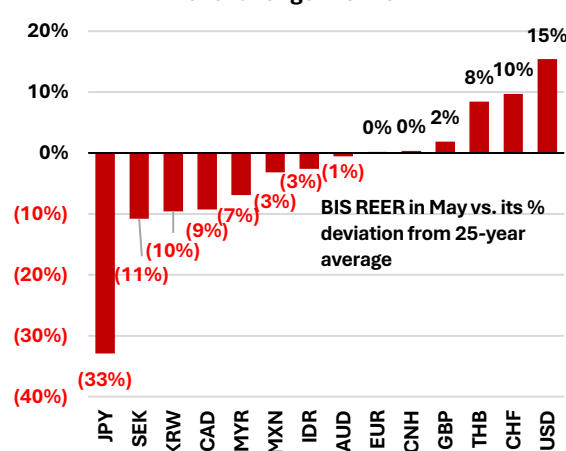


Exhibit 35: Nevertheless, the dollar value remains strong when compared over a longer horizon



DXY

After nearly topping at the 110 level in mid-January, the DXY index saw a near-consistent downtrend in 2025, bottoming below 97 in early July, before trading rangebound over the past few weeks. While we remain biased towards further USD downside over a longer horizon, a near-term slight upward correction is due, given the dissipation of the following risk factors that have driven a year-to-date correction of almost 10% for the DXY.

- The passage of Trump's fiscal bill, a USD5 trillion increase to the debt ceiling, and Treasury Secretary Scott Bessent's comment that long-dated debt will not be proportionally increased over the next several quarters, reduces US fiscal and debt-related risk premia.
- Continued US labour market resilience and upside inflation risks from tariffs indicate Fed rates will likely be kept higher for longer, denting any potential real-rate differential outflows.
- The S&P Rating Agency's reaffirmation of the US's credit rating and outlook suggests a higher fiscal deficit from the recent fiscal bill may be counteracted by higher tariff-driven revenue.

We target a DXY upside of 99.8 in 2H2025. Downside risks to our DXY call for the remaining year include greater concerns on the US fiscal outlook and/or Fed monetary independence, a more dovish than expected Fed position in the upcoming September meeting, or a paring of foreign portfolio holdings after recent US equity gains.


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FX: Major Currencies

Exhibit 36: Risk reversals for the EUR continue to indicate markets' bullish bias over the medium-term

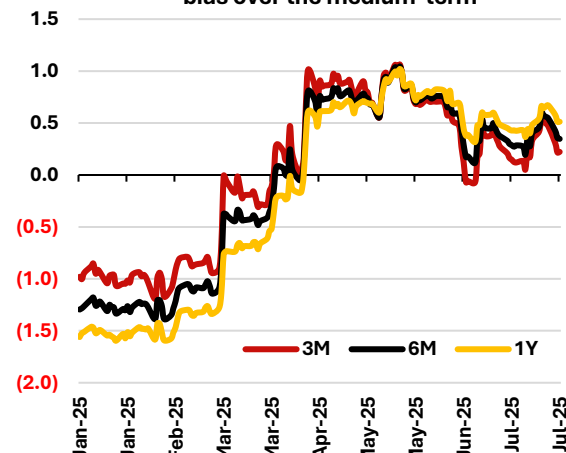


Exhibit 38: Some room for BOE rate cuts, though sticky inflation may be a challenge

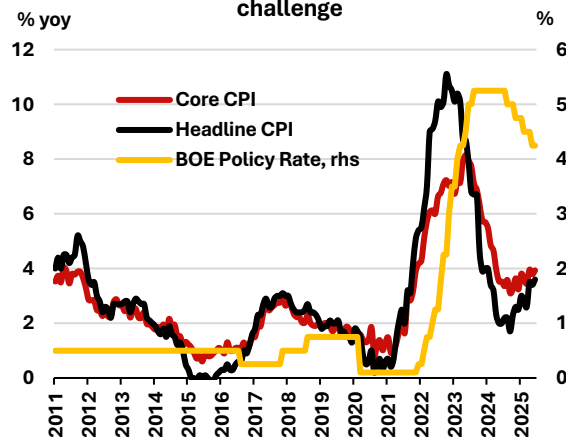


Exhibit 37: EUR vs. CFTC futures positioning

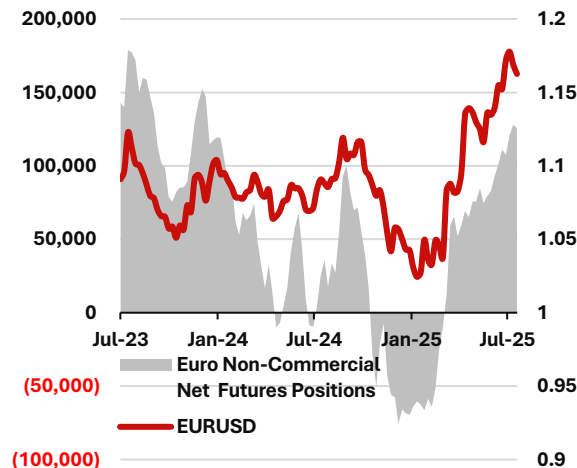
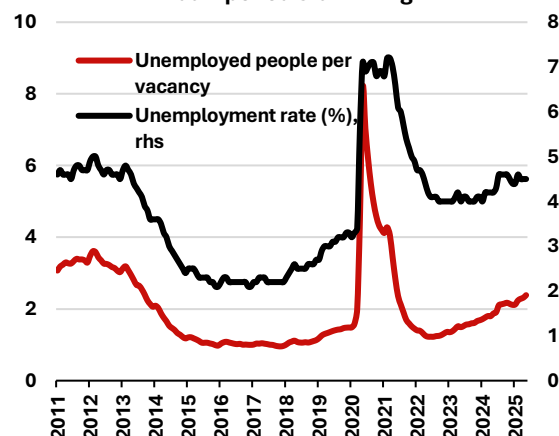


Exhibit 39: UK employers' concerns over the economic outlook and costs have dampened staff hiring



EUR

A direct beneficiary of recent weaknesses in the USD, the search for an alternative to the USD bolstered EUR/USD to top 1.18 in early July. At current levels, we think the EUR is ripe for some profit-taking on near-term tailwinds for the USD, and we pencil in an end-2025 EUR/USD level of 1.150. However, we remain constructive on EUR prospects beyond 2025, given:

- A tentative end to further ECB policy rate cuts juxtaposed against more room for the Fed to resume its easing cycle, puts forward interest rate differentials in favour of Eurozone bonds.
- Greater inflation risks in the US due to tariff policies, reducing the appeal of US debt due to suppressed inflation-adjusted yields.
- A potential Ukrainian peace deal will reduce risk premia for EU assets while leading to lower energy costs (a trade deal with Russia on energy) and current account pressure, as well as greater confidence in corporate investments/spending and private household consumption.
- Meanwhile, higher spending plans on infrastructure and defence will also support Eurozone growth, while fiscal deficit levels are relatively comfortable in the Eurozone.

Recent news flows and portfolio data also indicate a growing trend of currency diversification away from the USD. The EUR stands to benefit as the next best alternative for reserve diversification and international trade payment purposes, due to its high daily FX turnover, deep liquidity pools, high institutional trust, and strong integration into global financial and trade systems. Tacit support from several ECB policymakers also suggests little concern about knock-on effects from a stronger euro, such as reduced competitiveness of European exports.

GBP

GBP/USD also tracked USD weaknesses in 2025, though year-to-date gains of 7.8% notably lagged that of the EUR (+12.5%), driven partly by the GBP's inverse relationship with market volatility. We are relatively neutral on the GBP's prospects for the year ahead. Tailwinds include the UK's early trade deal with the US, reducing tariff-related uncertainties for UK businesses with tariffs already mostly effective at the lower rate (unlike other US trade partners such as the EU and Japan, which signed their deals later), while also securing a more competitive tariff level for its exports compared to peers. The medium-term trend of diversification away from the USD will also see the GBP as a major beneficiary

The GBP, however, may be subject to swings in expectations for BOE monetary policy in the near term, as still high and sticky inflation comes against some signs of a softening economy. Uncertainties on the pathway ahead had also driven the BOE to trim policy rates in a 'finely balanced' decision in August, while the MPC voting pattern suggests significant concerns on inflation ahead. The BOE expects inflation to peak at 4% in September, while higher payroll taxes and minimum wage hikes are also likely to strain labour markets. Meanwhile, the rising fiscal and political instability frequency also suggests a higher risk premium for UK debt and currency. As such, GBP/USD will likely trade rangebound of 1.33-1.37 levels for 2H2025.


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FX: Major Currencies

Exhibit 40: Room for the RBA to ease policy rate settings – especially amid a weakening labour market

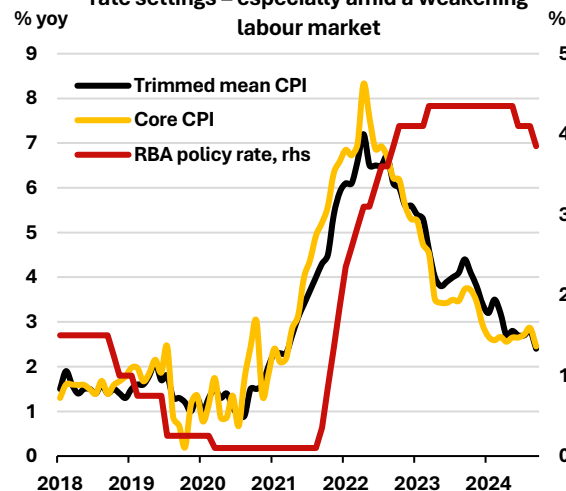


Exhibit 41: AUD and CNH 20-day correl

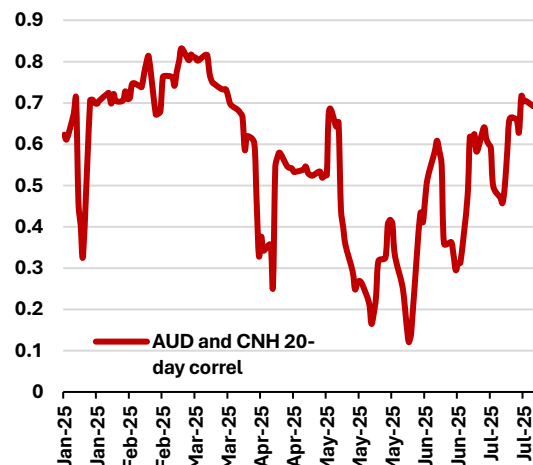


Exhibit 42: A tight labour market has helped driven a rebound in Japan's core inflation

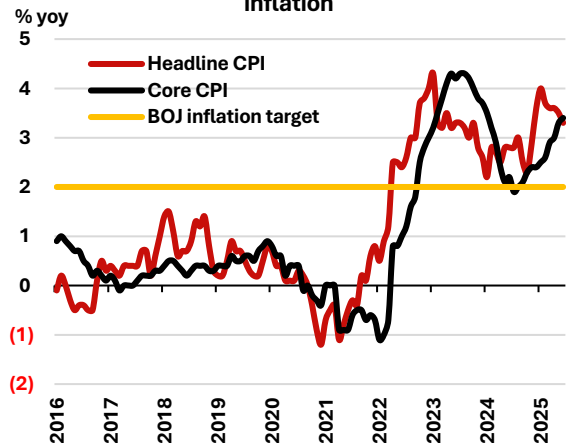
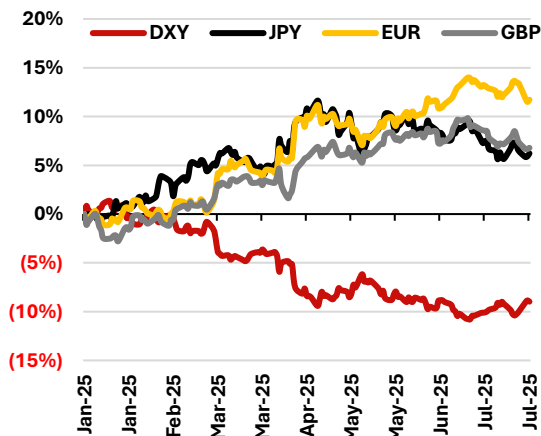


Exhibit 43: JPY traded rangebound against the USD since April 2025



AUD

AUD/USD strengthened 6.4% in 1H2025, but its performance lagged all G10 peers aside from the CAD (which was beset by constant news of tariffs on Canadian exports). Relative AUD weaknesses were driven by Australia's weakening terms of trade, which fell to a multi-year low in April. Though the AUD outperformed G10 peers in July from unexpected bullish catalysts arising from the RBA and US trade policies, we think some mean-reversion potential may be ahead in 2H2025, given the bearish mix of events for the remaining year from i) Dissipating tailwinds from a frontloading of trade activity, ii) Imminently higher US tariffs slowing global growth, iii) Commodity-linked gains to dissipate after the earlier tariff-related price spike, iv) Policy rate easing by the RBA to temper policy rate differentials amid weaknesses in labour markets. A firmer footing is expected later in 2026 when USD softness resumes, China's growth momentum stabilises, and tariff-related uncertainties on business activity subside.

JPY

Unlike other major FX, the JPY's rally against the USD ended in April, before subsequently trading within the 142-149 handle until July. The pause came amid rising growth risks in Japan, given the high tariffs imposed on Japan (in April) and the country's significant export dependency on the US – especially for automobiles. Hence, markets have dampened rate hike expectations by the BOJ despite risks of accelerating inflation in Japan. Yen carry trades have also gradually been reinstated, given near-term prospects of elevated interest rate differentials vs. the Fed. While concerns have eased near-term about political instability post-elections, traders are eyeing potential fiscal stimulus ahead and its impact on long-dated Japanese debt, given opposition success in elections and their push for expanded government spending and tax cuts. The US-Japan trade deal, which features a USD550 billion Japanese fund for investments into the US, also suggests significant medium-term portfolio outflows and balance of payment pressures ahead. Pending greater clarity on details from both the fiscal and trade agreement front, we pencil in an end-2025 USD/JPY target of 152, with the BOJ to keep policy rates unchanged for the remaining year.


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MYR outlook hinges on external developments

Exhibit 44: Ringgit held to its 5% year-to-date gain against the USD since 2Q2025

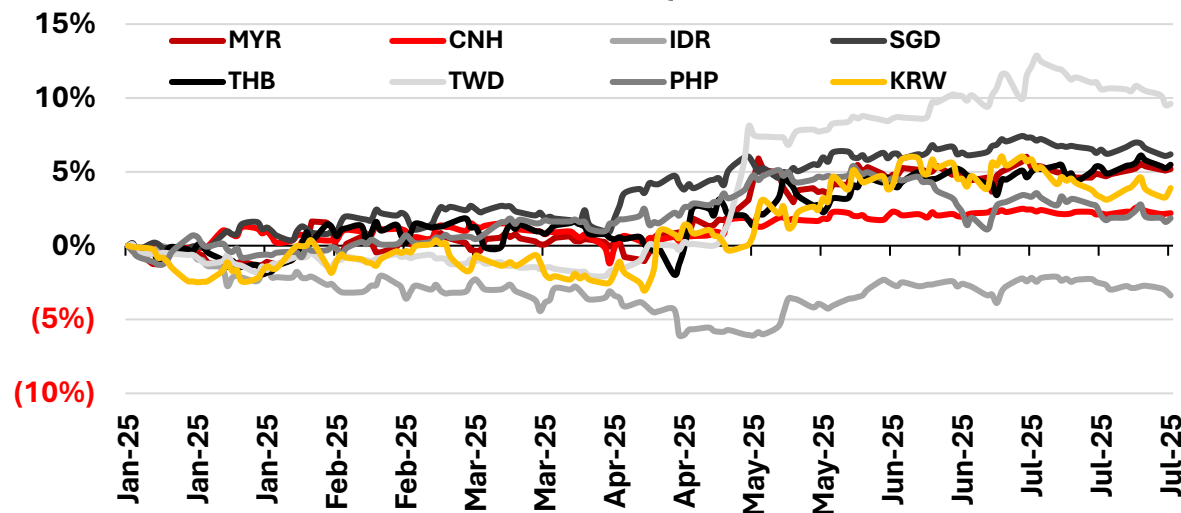
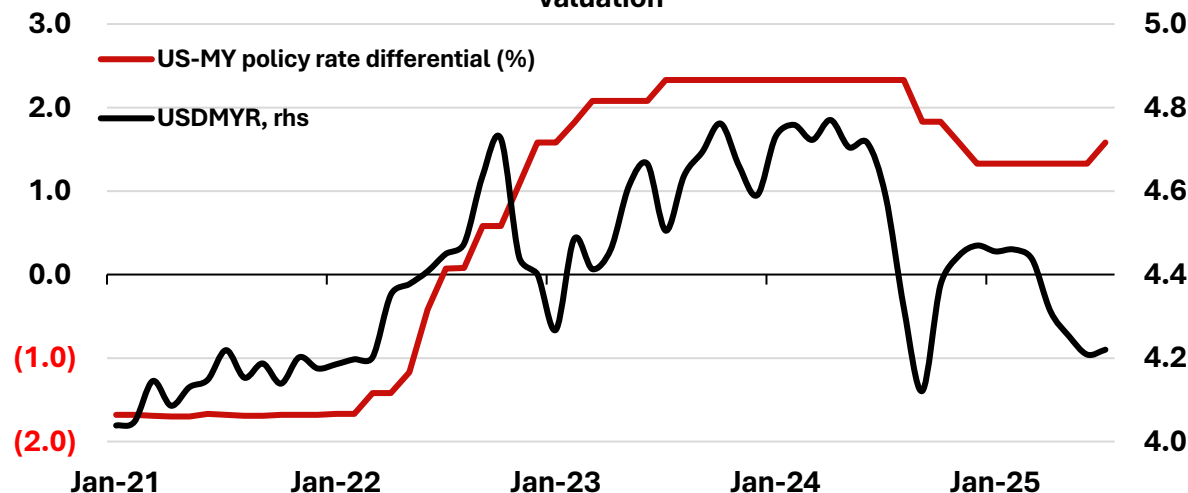


Exhibit 45: Policy rate differentials indicate slightly stretched MYR valuation



MYR

Two trading bands were noted for USD/MYR in 1H2025, maintaining within the 4.40-4.50 range earlier on before trading within 4.20-4.30 from May. Our USD/MYR forecasts of 4.27 by end-2025 are premised on a slight rebound in USD strength and reduced support from Malaysia's trade account. However, we think the trading range for the next few months will remain largely confined within the 4.20-4.25 level, driven mainly by USD-centric developments, given little reaction to significant developments over the past few weeks, such as the US tariff deal and semiconductor tariff threat, and BNM's downward revision of Malaysia's growth estimate. Malaysia's stable monetary policy settings, little surprises on the domestic fiscal or political landscape, and strong FX trading volumes when USD/MYR temporarily fell below 4.20 during intraday trading on 14 August, further bolster our conviction of a limited trading range in the near term.

Further MYR appreciation is expected later in 1H2026, when the outlook on the Fed policy rate pathway becomes clearer, sentiment on regional equities improves, and the narrowing short-term rate differential drives greater USD conversions into the ringgit. The effect may be tempered if potential semiconductor tariffs diminish Malaysia's strong current account surplus. However, BNM's increased foreign reserves in 2025 may help cushion the blow in this scenario. Upside risks to our USD/MYR call include a sharp deterioration in US-China relations, accelerating US inflation, and/or a hawkish turn for the (presently unknown) incoming Fed Chairman. Meanwhile, further signs of US labour market weaknesses or renewed worries on the US fiscal outlook or Fed monetary independence will inspire a broad-based Asian FX rally against the USD.


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Fixed Income: US Treasuries

Exhibit 46: US Treasury yields vs. inflation vs. Fed Funds Rate

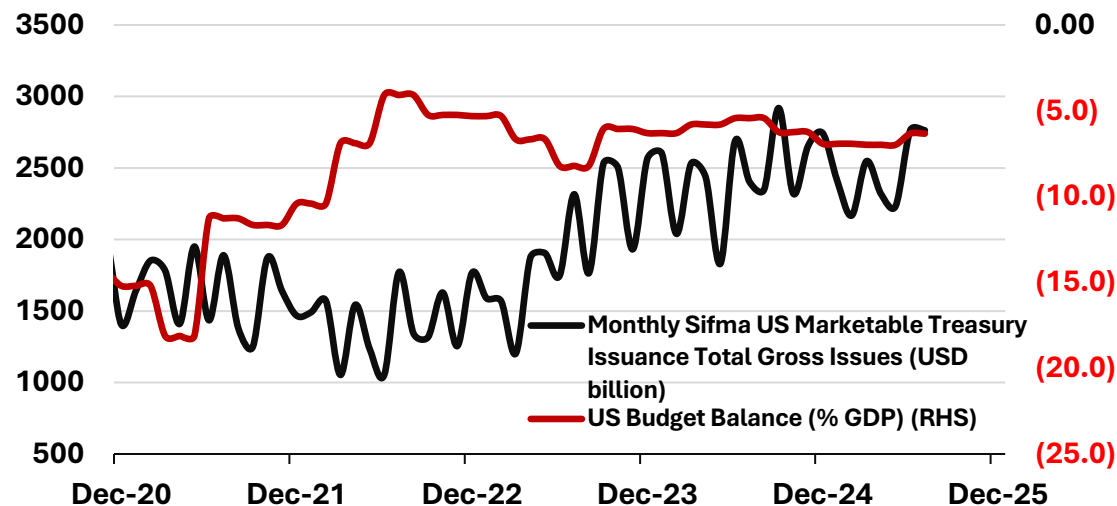
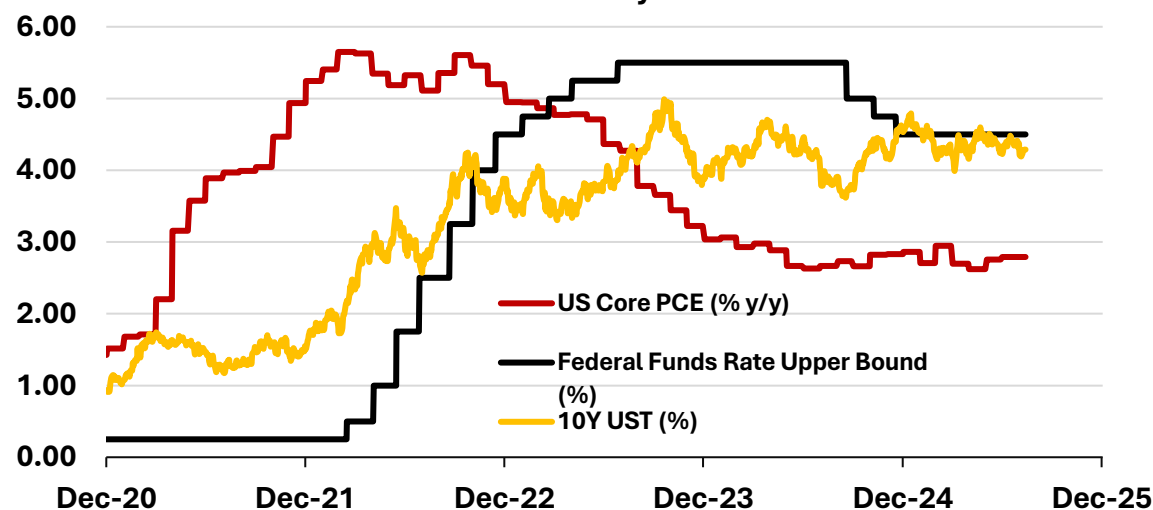


Exhibit 47: Issuance of US Treasury securities vs US fiscal deficit



UST 2H2025 outlook

We hold a modest positive outlook for the US bond market, considering the following factors. Our view is based on:

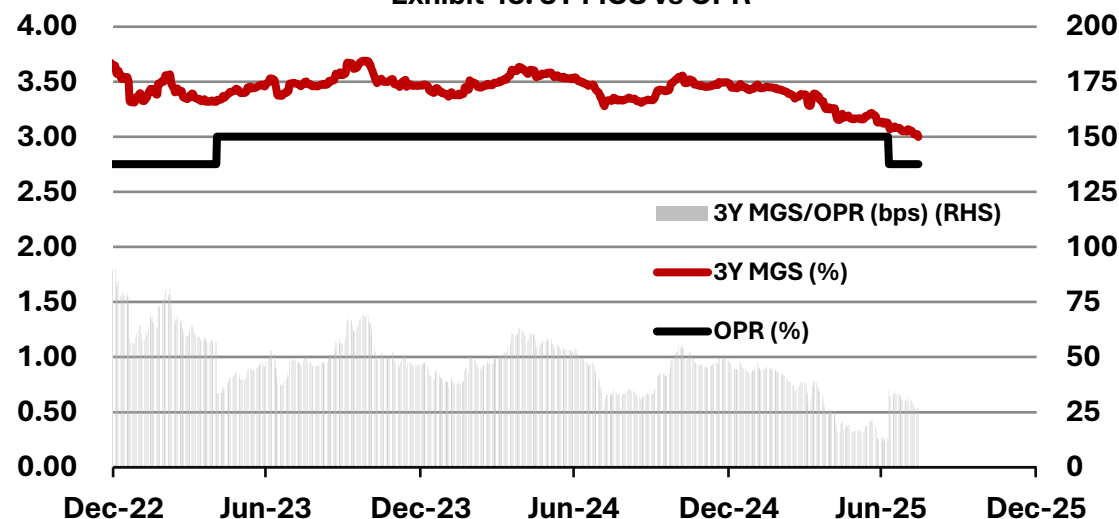
- Continued Fed interest rate cuts at a moderate pace. We foresee two (2) 25 bps cuts in the remaining months this year and two (2) cuts next year, targeting 3.50% by end-2026. In addition, despite our FFR expectations, we think bond markets will sustain pent-up expectations for more cuts, which we believe will press bond yields lower;
- Continued weak economic data and outlook, including anticipated effects of the trade war on the US economy. This feeds into our expectations of a moderate pace of Fed rate cuts;
- On the flipside, pressure on UST comes from US fiscal policy. The US fiscal bill passed as expected, according to which the US Congressional Budget Office estimates will result in a fiscal deficit addition of USD3.43 trillion over the next decade; and
- Tariffs will likely add inflationary pressures, which could limit UST yield downside. Stubbornly high inflation is likely amid the implementation of new tariffs. We think bond players will continue to be wary of short-term price pressures, though in the long term, we maintain our outlook for US inflation to progressively decline towards the Fed's 2.0% by the end of 2027. Our model uses the monthly core PCE y/y rate.

	3Q 2025	4Q 2025	1Q 2026	2Q 2026	3Q 2026	4Q 2026
2Y UST	3.75	3.70	3.60	3.40	3.30	3.20
10Y UST	4.40	4.30	4.20	4.10	3.90	3.80
3Y MGS	3.00	2.95	2.95	2.95	3.00	3.00
10Y MGS	3.55	3.50	3.50	3.45	3.45	3.50


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Fixed Income: Malaysian Bond Market

Exhibit 48: 3Y MGS vs OPR

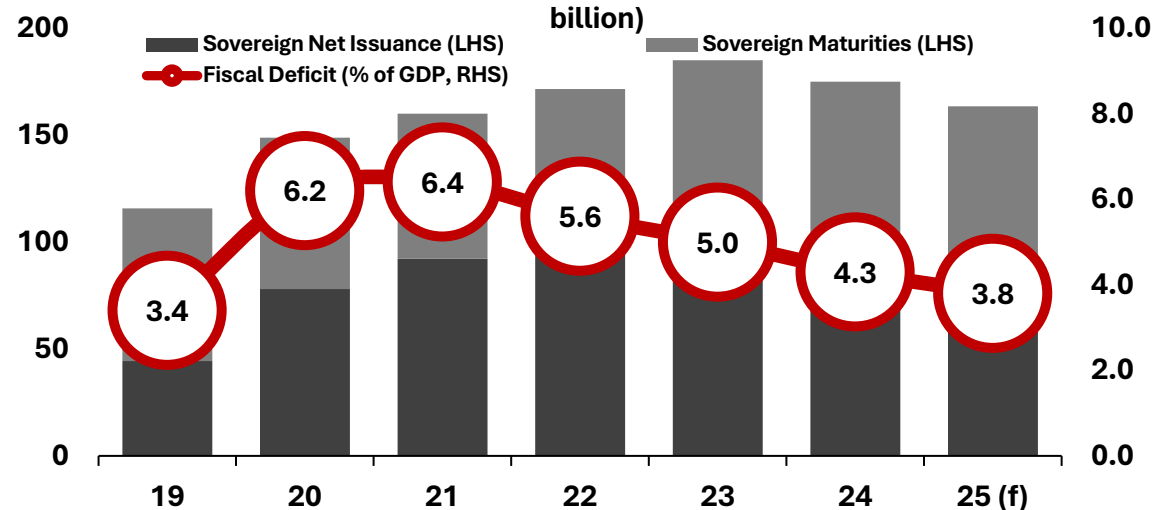


Government Bond Market Outlook

We maintain a positive view on Malaysia's government bond market. Our view is based on:

- Risks to growth and low inflation support lower for longer MGS yields. We think shorter-dated MGS+GII papers will lead gains, while the medium- to longer-tenors will likely remain supported, though longer-dated MGS yields may continue to hover near current levels. The main boost for the shorter MGS is the BNM rate cut in 2H2025. However, for longer tenors, we think players will sustain pricing of slowly rising inflation. Hence, our expectation is for a steeper MGS+GII curve in 2H2025. The onshore bond trend is likely to be aided by falling global rates. Interest rate differentials of USD will progressively be negative for the USD vs. MYR, and thus, we foresee a firm rebound in MGS foreign shareholding when the Fed commits to rate cuts;
- MYR outlook supports bonds. We maintain a firm outlook for MYR in 2H2025, and this should support sentiment for shorter to medium-term duration MGS+GII; and
- The MGS+GII primary market will be supported as fiscal consolidation continues; new supply will be contained in 2H2025. Based on the scenario of continued fiscal consolidation by GOM and the expectation that the government will be able to maintain the current pace of budgetary spending and revenue into 2H2025, we retain our current forecast of gross MGS+GII issuance of MYR165 billion for the year.

Exhibit 49: Fiscal deficits vs. Issuance of Government Bonds (MYR billion)




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Fixed Income: Ringgit Corporate Bonds Market

Exhibit 50: Bond yields, Quasi-government, AAA and AA1 (5Y) (%)

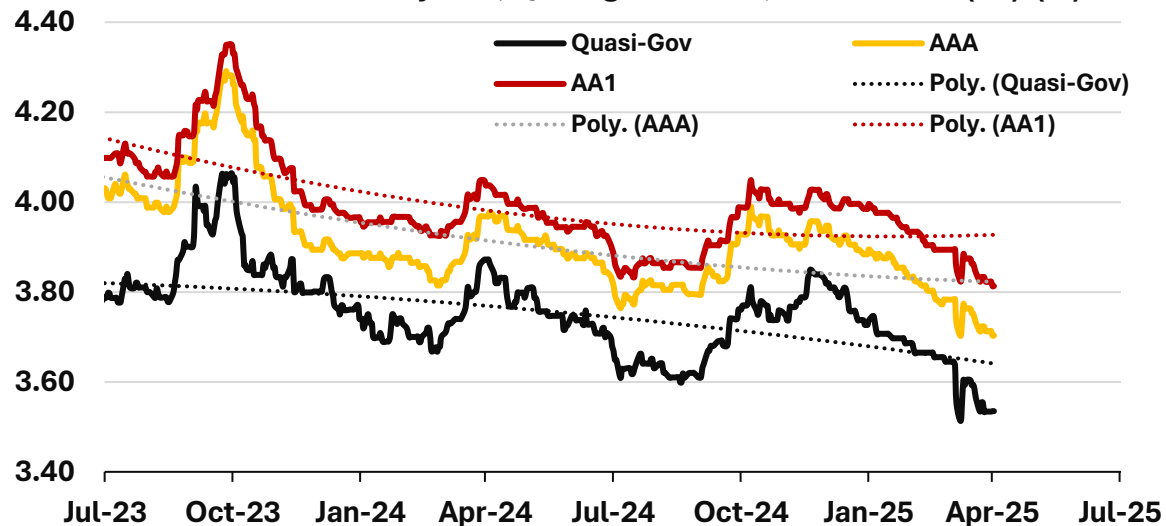
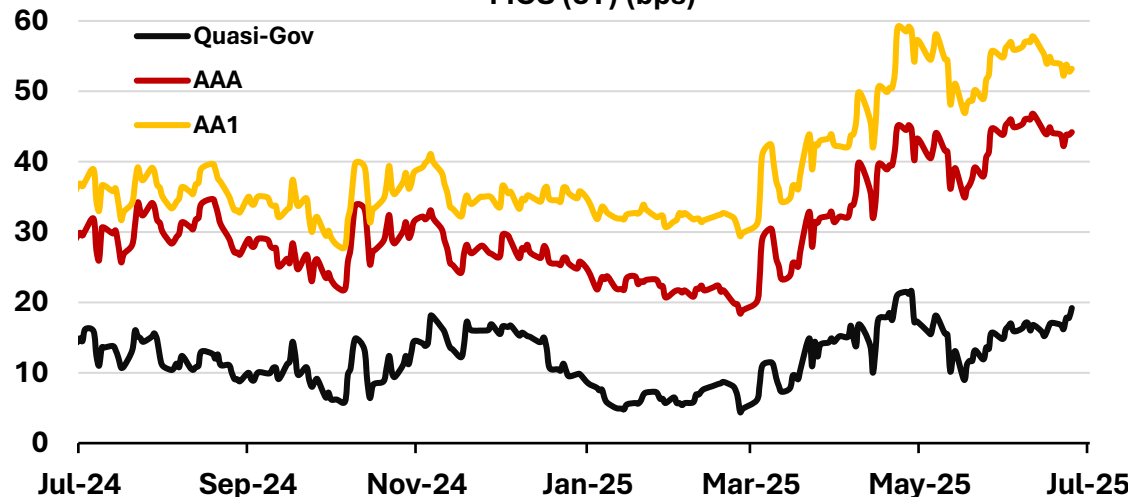


Exhibit 51: Credit spreads, Quasi-government, AAA and AA1 vs MGS (5Y) (bps)



Corporate bond market outlook

We expect net Private Debt Securities (PDS) issuances to increase modestly in 2025 as GDP grows and investments/capacity expand. We note that 2024 gross issuance exceeded 2023 but lagged the 2022 number, owing to the lack of large/infra projects requiring debt financing.

We anticipate the gross issuance of PDS in 2025 of at least MYR130 billion (2023: MYR126 billion, 2024: MYR137 billion). A modest number thus limits the upside to credit spread levels. Meanwhile, our calculations indicated that maturing PDS in 2025 will amount to MYR76.9 billion. In addition, bonds with call options expected to be exercised in 2025 are estimated to amount to MYR20.9 billion. Suppose we subtract our gross issuance expectation of MYR130 billion from the MYR76.9 billion maturing papers and callable papers of MYR20.9 billion. In that case, our estimate of net PDS issuance in 2025 will be MYR32.2 billion (2024: MYR25.2 billion). Thus, for 2025, net issuance will show a modest increase y/y, which should support our view of a controlled widening in spreads this year.

We expect credit spreads to narrow slightly in the next few quarters as corporate bond yields decline to follow MGS yields. We do not expect spreads to return to levels seen in early 2025.


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The ever-changing dynamics of global trade

Exhibit 52: World: Top 3 importers, % total imports

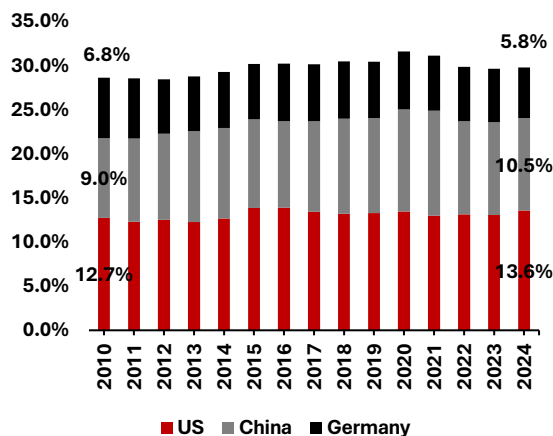
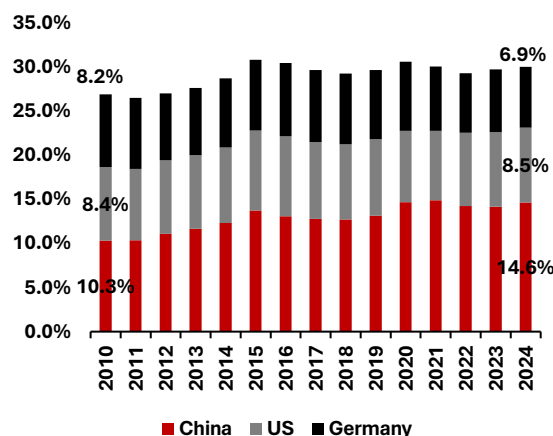


Exhibit 53: World: Top 3 exporters, % total exports



Global Trade Dynamics

The global trade landscape continues to evolve, with the US, China, and Germany maintaining their positions as the top three trading nations. Collectively, these economies account for approximately 30% of global trade, underscoring their central role in shaping international trade flows. However, global trade dynamics changed following China's entry into the World Trade Organisation (WTO) in 2001.

From an import perspective, China and the US have expanded their relative shares, gradually displacing Germany's position. While Germany remains a key player, its relative decline signals challenges in maintaining its global competitiveness and whether its industrial transformation can keep up with global trends.

On the export front, China's ascent has been remarkable. Since 2010, its share of global exports has risen from 10.3% to 14.6% in 2024, driven by its deep integration into global manufacturing and its strategic pivot from low-value towards higher-value goods. In contrast, Germany's export share has contracted, reflecting the mature state of its industrial base. The US export share has remained broadly flat. To be fair, the US still have strong comparative advantages in sectors like technology, aerospace, and services, but these advantages are not translating into growing export share, and by extension, its trade balance.

This divergence in trade performance reveals important macroeconomic implications: China's export growth has consistently outpaced its import growth, reinforcing its massive trade surplus and external resilience. Germany appears to be on a declining industrial momentum, while the US faces a more concerning imbalance with a ballooning trade deficit. This raises questions about its external sustainability and, more importantly, its influence in global trade.

Who are the US' major import sources?

Despite the US' rising import share, its dependence on Chinese imports has declined significantly post-Trump 1.0. This is not merely a function of trade diversion toward alternative suppliers such as Mexico, but also a reflection of China's expanding global reach, which has reduced its reliance on the US market with a larger trade surplus. This decoupling has contributed to persistent inflationary pressures in the US, as supply chain reconfigurations cannot take advantage of China's technological prowess and cost structure.

Again, thanks to Trump 1.0, the US' trade diversion away from China has created new opportunities for ASEAN. Vietnam has emerged as a key beneficiary, with US imports from Vietnam surging in recent years. Thailand and Singapore have also seen steady gains, while Indonesia's share has remained flat. Malaysia, however, has experienced a modest decline post-pandemic, with its share of US imports easing to 2.5% in 2024 from 3.1% in 2021. This shift has contributed to narrowing Malaysia's trade deficit with the US.

The global trade dynamics will continue to evolve, especially following the US' Reciprocal Tariff (RT). The rise of China, the reorientation of US sourcing strategies, and the evolving role of ASEAN economies reflect a broader, ever-changing trend. Understanding these shifts is crucial to navigating the next phase of global economic integration, or the lack thereof, post-RT.

Exhibit 54: US: Top 3 import sources, % total imports

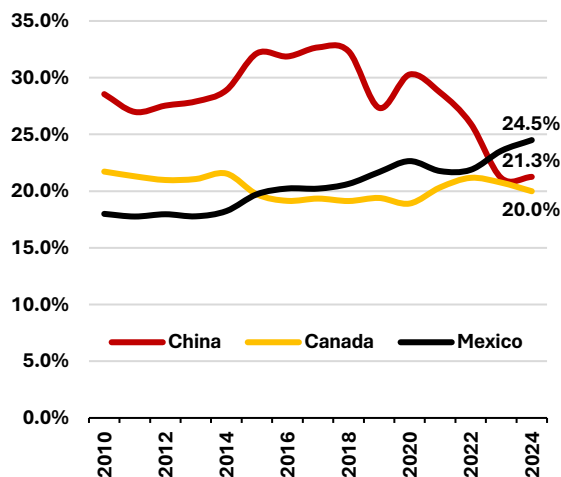
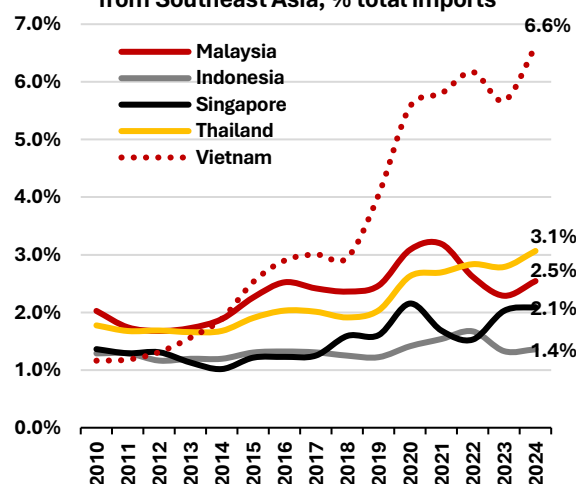


Exhibit 55: US: Top 3 import sources from Southeast Asia, % total imports




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US does not have FTAs with Malaysia and China

Exhibit 56: Most Favoured Nation (MFN): Simple average applied, %

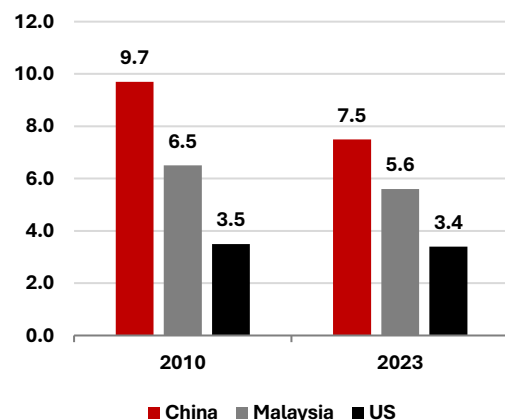


Exhibit 57: Most Favoured Nation (MFN): Duty free, %

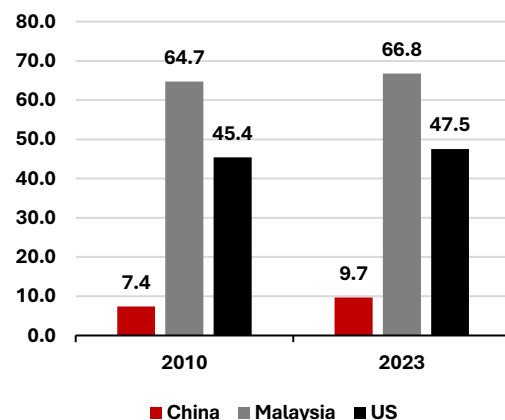


Exhibit 58: Malaysia: Total exports, y/y%

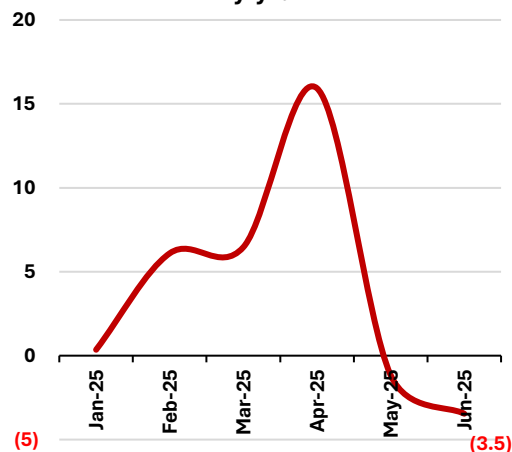
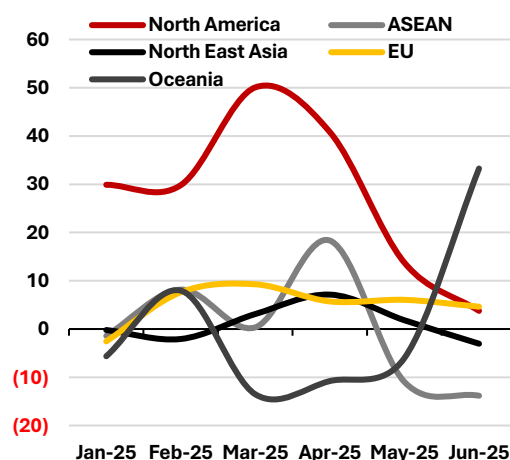


Exhibit 59: Malaysia: Top export destinations (85% share), y/y%



MFN no more

In the global trade system, Most-Favoured Nation (MFN) tariffs are the default rate applied to trading partners outside preferential agreements.

Over the past decade, the simple average MFN applied tariff has declined across major economies, reflecting a gradual liberalisation trend. China, in particular, has made notable progress, reducing its average MFN rate from 9.7% in 2010 to 7.5% in 2023, signalling its intent to integrate more deeply into global value chains. This downward trajectory aligns with China's broader trade agenda, although its relatively low share of duty-free tariff lines suggests a more selective liberalisation strategy.

In contrast, Malaysia's MFN tariff on US imports stood at 5.6% in 2023, while the US applied a 3.4% MFN rate. However, what distinguishes Malaysia is its high proportion of duty-free tariff lines. In 2023, 66.8% of Malaysia's 11,343 tariff lines (at the 6-digit HS level) were set at 0%, compared to 47.5% for the US and just 9.7% for China. This implies that Malaysia maintains a relatively open trade regime.

Enter RT: A Paradigm Shift

US' RT marks a significant departure from conventional trade policy. Under the Trump administration's expanded tariff regime, the US duty-free share is expected to collapse from 47.5% to near zero, as tariffs are applied across virtually all import categories. This shift represents a structural tightening of trade access, with profound implications for global supply chains, inflation dynamics, and bilateral trade balances.

Post-April 2nd "Liberation Day": Dissipating frontloading effects

Malaysia's export performance in 2Q2025 offers a compelling case study of how trade shocks can rapidly reshape its trade flows. In April, Malaysia's total exports surged by 15.9% y/y before the tariff regime took effect. Post-Liberation Day, Malaysia's export growth contracted to -1.2%, and by June, it had deteriorated further to -3.5%, underscoring the sharp reversal in frontloading activity.

More nuanced data reveals further insights. Exports to North America declined by June, reflecting the direct impact of the US trade policy shift. Despite no change in trade policy within the region, exports to ASEAN also fell considerably, suggesting that a significant portion of Malaysia's exports to ASEAN may consist of intermediate goods destined for the US. Exports to North East Asia also declined, albeit to a lesser extent. Meanwhile, shipments to the EU remained relatively stable, but exports to Oceania spiked.

RT as a Drag on Global Trade Growth

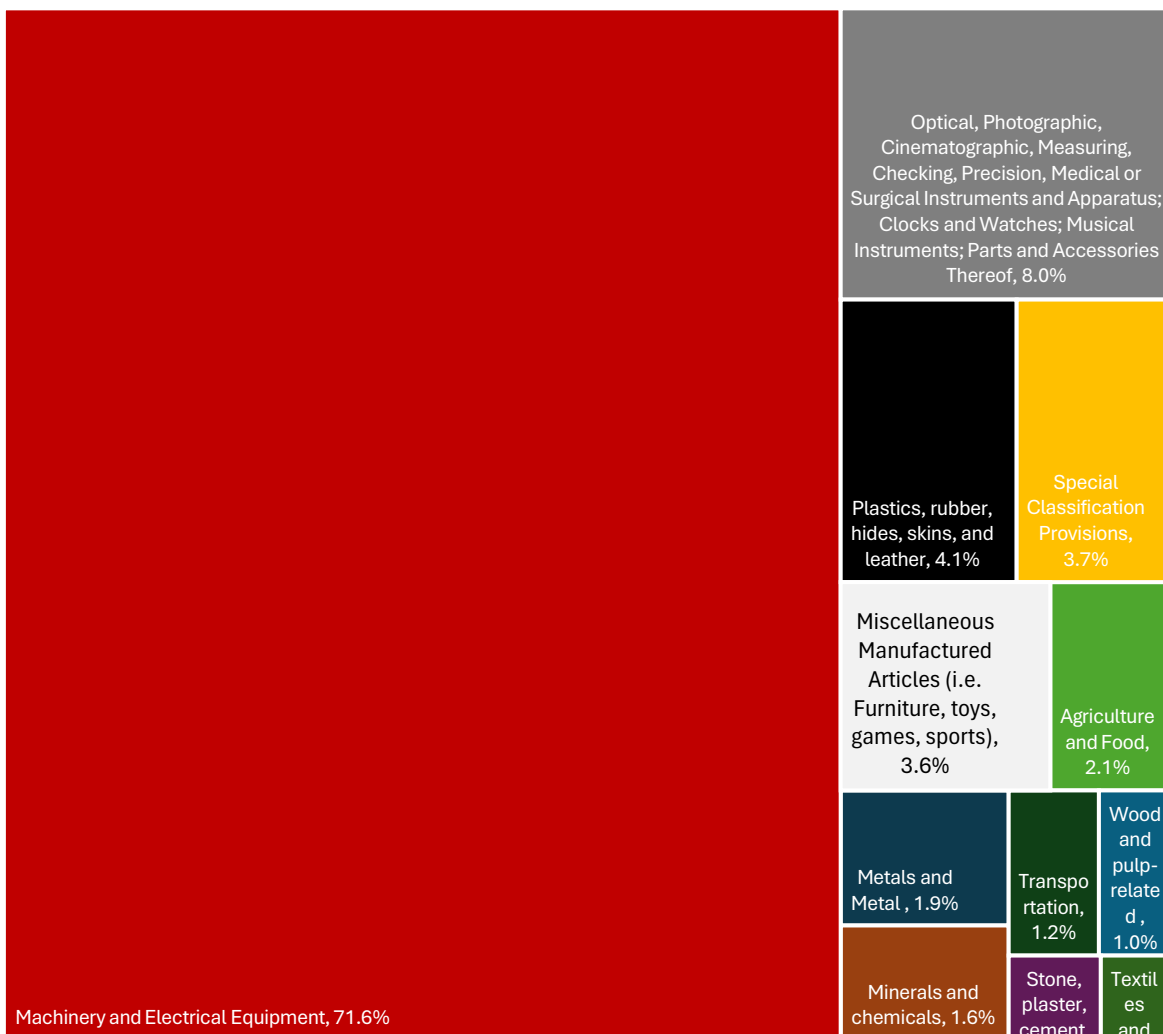
As the world's largest importer, the US imposition of reciprocal tariffs represents a structural headwind to global trade growth. Unlike targeted tariffs during Trump 1.0, the current regime is broad-based and steep, affecting a wide range of goods and trading partners.

For most US-dependent export markets, including Malaysia, the loss of export momentum could weigh on GDP growth in 2H2025. Second, the erosion of producer surplus due to tariff-induced price pressures may reduce margins and investment appetite, especially among non-American firms heavily reliant on the US market.


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Very high concentration in one key sector

Sectoral breakdown of US imports from Malaysia, %total



From the HTSUS (Harmonized Tariff Schedule of the United States) classification point of view: US imports from Malaysia

The overall US import profile from Malaysia in 2024 reveals a striking concentration in high-value, technologically intensive sectors, underscoring Malaysia's strategic role for the US. According to data from the US Census Bureau, total imports from Malaysia reached USD52.53 billion in 2024, a robust 13.7% y/y increase from 2023.

The Machinery and Electrical Equipment category (HTSUS Chapters 84–85) commands a staggering 71.6% of total imports from Malaysia. This dominance is emblematic of Malaysia's entrenched position in the semiconductor and electronics ecosystem. In recent years, the surge in demand for chips, data infrastructure, and AI-enabling hardware likely contributed to this expansion, as American firms seek diversification away from China and resilience in sourcing. While this is advantageous in value creation, it also exposes Malaysia's vulnerability to geo-technological rivalry and demand shocks.

The second-largest category, Optical and Precision Instruments (8.0%), reflects Malaysia's growing sophistication in medical devices and high-precision manufacturing. Third place is Plastics and Rubber (4.1%), which largely comprises rubber gloves, industrial rubber, and plastic articles. As the world's largest exporter of rubber gloves, Malaysia's competitive advantage remains, as the RT imposed on Malaysia at 19% is lower than that of the second largest – China.

From the United Nations (UN)'s Standard International Trade Classification (SITC) classification point of view: Malaysia's overall export structure

Malaysia's export structure in 2024 represents a highly industrialised economy with a substantial reliance on Machinery and Transport Equipment (MT), accounting for 45.7% of total exports. This sector, encompassing semiconductors, electrical machinery, and transport components, underscores Malaysia's strategic role in global technology supply chains. However, such concentration also exposes the country to cyclical demand fluctuations and geopolitical risks, particularly in the tech sector.

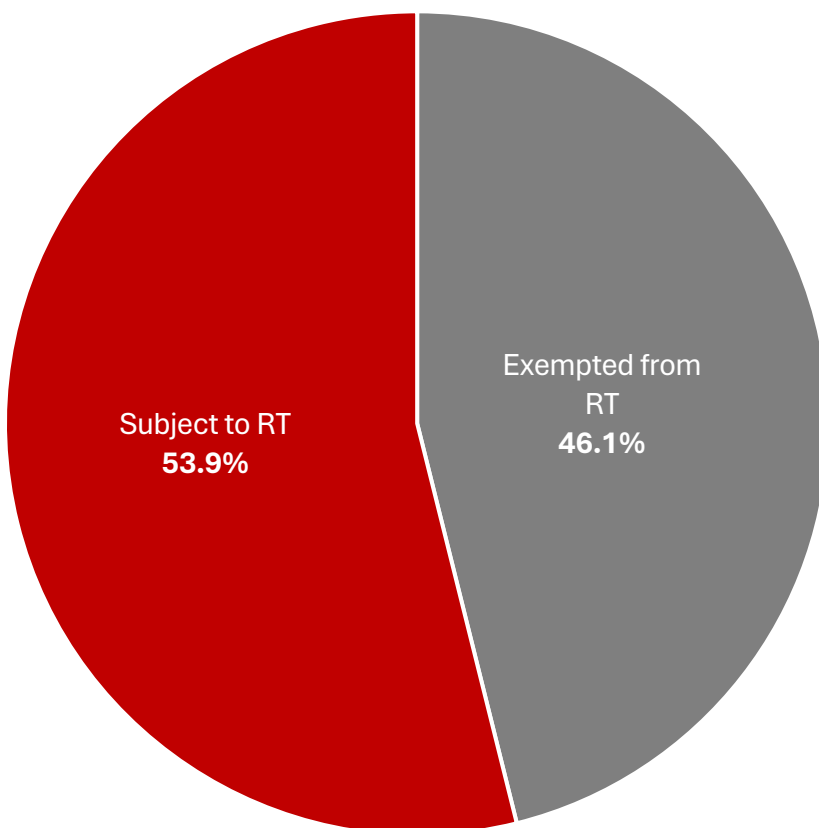
Mineral Fuels (14.5%) remain a significant contributor, driven by LNG and refined petroleum exports, though this sector faces long-term challenges from global energy transition trends. Miscellaneous Manufactured Articles (11.3%) and Manufactured Goods (9.1%) reflect Malaysia's diversified industrial base, including furniture, consumer goods, and industrial materials, while Chemicals (7.5%) highlight the importance of petrochemical clusters.

Malaysia's MT exports are geographically diversified but notably concentrated in a few key markets. Singapore and the US account for nearly 40% of MT exports, followed by Hong Kong and China (each at 10.8%), and Taiwan (6.8%). To mitigate external risks, Malaysia could pursue broader export diversification, deepen market access in emerging economies and invest in innovation. The challenge, however, is that most of Malaysia's exports are owned by MNCs, with only a handful of Malaysian-owned industry champions. Localisation policy is key to moving up the industrial value chain.


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Enter RT: A top-up tariff on Malaysian goods

RT: Estimated Percentage Composition of U.S. Imports from Malaysia, %total



RT adds to the cost of goods imported

The following estimates are derived from 2024 US imports from Malaysia, considering the relevant Executive Orders relating to RT. Out of a total import value of USD 52.53 billion, approximately 46.1% (USD 24.23 billion) is exempted from RT, while the remaining 53.9% (USD 28.31 billion) is subject to an additional tariff of 19%. This indicates that more than half of Malaysia's exports to the US are now exposed to higher trade costs.

46.1% of US imports from Malaysia are exempted as stipulated under Annex 2 of the April 2nd Executive Order and other Section 232 exclusions, particularly on major semiconductor items.

Notably, the top five import categories subject to RT account for only 9.7% of total imports.

Based on our understanding of RT, the new tariff does not replace the prevailing tariff rate but acts as a top-up. A closer look at the tariff structure reveals RT's compounding effect. For instance, HTSUS code 8473.30.11 (printed circuit assemblies) carries a prevailing tariff of 0%, but is now subject to a full 19% RT, significantly raising its landed cost to 19%. Similarly, HTSUS code 8543.70.98 (other electrical machines and apparatus), accounting for 2.1% of imports, faces a combined tariff of 21.6% (19% RT plus the prevailing 2.6%).

We must emphasise that RT is not exclusive to Malaysia but affects many other US trading partners. As such, we believe that RT not only raises the cost of imported goods in the US market and, of course, is inflationary to the US economy, but also, importantly, how the additional cost is passed on to consumers, or the lack thereof.

Will the additional tariff be borne by American importers/consumers? Yes and no.

For exporters, the RT regime is particularly disruptive. Its deployment is very abrupt, unlike the usual trade negotiations that could take years or even decades. The tariff hike from a 3.4% MFN rate to a 19% RT is steep and broad in coverage, especially when 47.5% of US tariff lines are no longer duty-free.

This abrupt shift raises concerns about "reverse tariff" effects, where exporters may be forced to absorb cost pressures to maintain market access, thereby eroding producer surplus. While Malaysia's RT exposure is lower than China's, it is comparable to regional peers, suggesting that Malaysia's competitive advantage remains intact in RT.

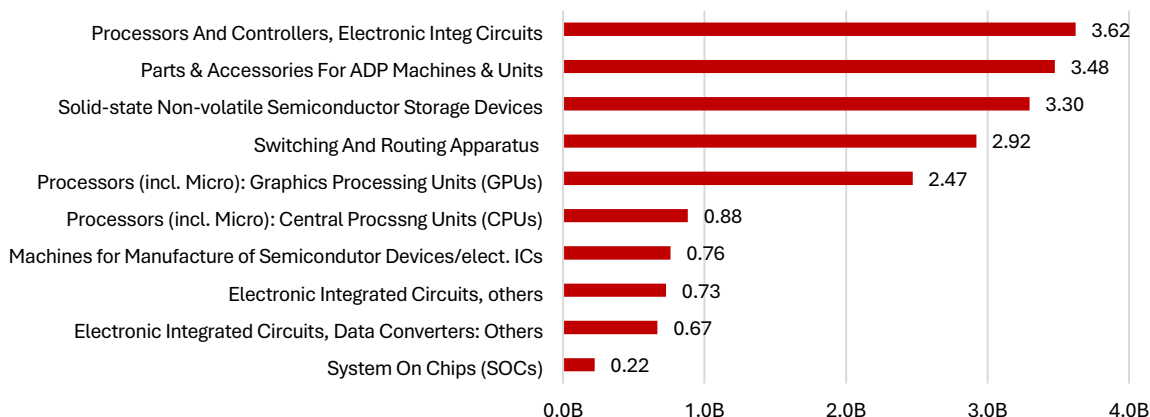
Growing anecdotal and empirical evidence suggests that US importers are bearing a significant portion of the burden from RT. Numerous US-based news reports have highlighted instances of importers renegotiating prices with overseas suppliers. Meanwhile, exporters will likely face downward pricing pressure from US buyers seeking to offset tariff-related cost increases.

Reinforcing this view, US Federal Reserve Chair Jerome Powell recently noted in his post-FOMC press conference that "the evidence suggests foreign exporters have lowered prices a little bit," while US retailers are absorbing most of the cost. This pricing behaviour helps explain why US inflation has not yet spiked in tandem with tariff hikes. However, Powell also cautioned that the risk of future consumer pass-through could be limited, further eroding producer surplus.

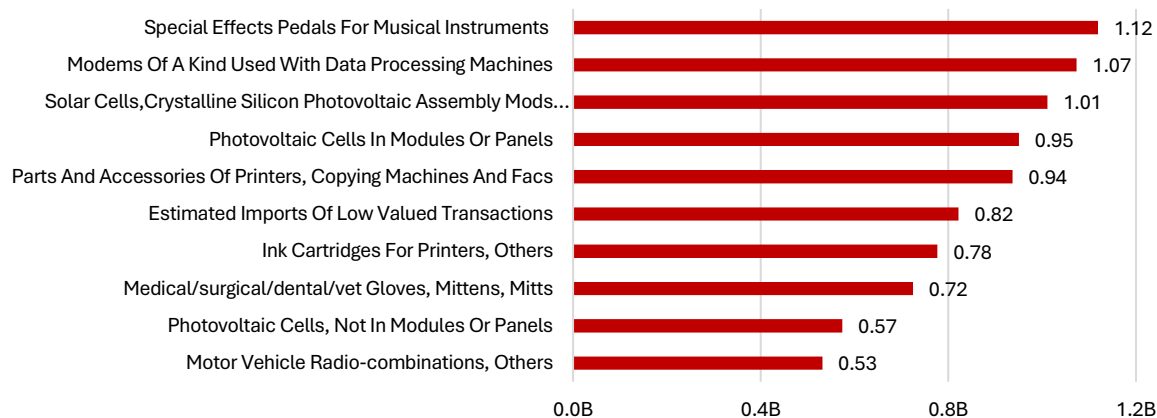

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RT by tariff lines: Small list but big in value

US imports from Malaysia: Top 10 exempted items from RT (based on 2024 figures), USD billion



US imports from Malaysia: Top 10 items subject to RT, (based on 2024 figures), USD billion



What exempted items tell us about RT

Our findings, based on 2024 figures, suggest that most of Malaysia's high-value electronics and semiconductor components remain shielded from retaliatory tariffs (RT), at least for now. The list of these items is smaller but much larger in value.

Electronic integrated circuits, particularly processors and controllers, are leading the list, which alone account for USD 3.62 billion in exempted US imports from Malaysia. This is followed closely by parts and accessories for automatic data processing (ADP) machines (USD 3.48 billion) and solid-state non-volatile semiconductor storage devices (USD 3.30 billion), underscoring Malaysia's critical role in supplying foundational components for computing and data infrastructure.

We note that many exempted items are made by American MNCs operating in Malaysia.

Switching and routing apparatus (USD 2.92 billion) and graphics processing units (GPUs) (USD 2.47 billion) further highlight Malaysia's role in capitalising on the tech upcycle. Notably, central processing units (CPUs), semiconductor manufacturing machinery, and various specialised integrated circuits also feature prominently, albeit at lower values.

RT items are mostly non-E&E, non-American-based, and low in value

Not all electrical and electronics or semiconductor-related imports are exempt from RT. The top 10 items include niche electronics and consumer tech accessories, as well as rubber gloves. Notably, solar cells and photovoltaic modules collectively represent a substantial portion of the RT-affected imports.

Other impacted items include printer accessories, ink cartridges, and low-value transactions, which point to a broader disruption in office and consumer electronics supply chains. The inclusion of medical gloves (USD 0.72 billion) is particularly significant, given Malaysia's global leadership in rubber glove production and the essential nature of these goods. Lastly, motor vehicle radio combinations round out the list, indicating that automotive electronics are also within the scope of tariff measures.

Final thoughts on RT

Overall, our analysis on RT gravitates towards three main takeaways:

1. Malaysia's exports to the US are highly concentrated in electronics and machinery, thus exposing trade to policy/market changes concerning the industry. There is growing uncertainty over whether future US trade policy could adopt a more sector-specific approach, potentially targeting even strategic tech components;
2. RT is an added layer to existing cost structures. Furthermore, the actual tariff imposed on Malaysian goods spiked from the prevailing rates to 10% (starting April) and, now, 19%; and
3. The "reverse tariff" effects: the unintended consequence of RT. While US retailers absorb much of the tariff burden to avoid passing costs to US consumers, exporters may be coerced into sharing the burden, lowering producer surplus only to secure access to the world's largest buyer.

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