



# **Socio-Economic Research Centre (SERC)**

## **Quarterly Economy Tracker**

**Jul-Sep 2022**

### **Can Malaysia Sustain A Resilient Recovery?**

**20 September 2022**





## GLOBAL RECOVERY AT RISK OF SLOWING FASTER THAN EXPECTED

- **Risks of the global recovery being setback persist.** Risks to the global recovery remain skewed to negative. A period of sub-par global growth is the most likely outcome. We expect uneven growth across advanced economies as tempered by high inflation, the acceleration of monetary tightening, continued aggression in the Eastern Europe, emerging market vulnerabilities as major central banks taper and a correction of bubbly financial asset markets and emerging market currencies' depreciation.

The International Monetary Fund (IMF)'s World Economic Outlook Update in July has revised lower baseline global growth to 3.2% in 2022 from April's 3.6%. In 2023, disinflationary monetary policy is expected to bite, with global output growing by just 2.9%. The World Bank has warned that global rate hikes could trigger global recession in 2023.

- **Data prints point to decelerating growth pace.** Both the latest PMIs for manufacturing and services indicated that the global economy contracts for first time in August since June 2020 with downturns signalled in all sectors except financial services and there are signs of excess capacity as backlogs fall and jobs growth slows.

**Inflation remains high in major advanced economies though some were easing off from the peak.** High crude oil and gas prices remain a wild card. As monetary policy tightens, annual inflation will remain elevated. However, further significant market instability is unavoidable even after inflation has peaked.

- (a) **The US economy has entered technical recession** (-0.6% annualized qoq in 2Q; -1.6% in 1Q), giving rise to an increasing risk of a full-blown recession in 2023. Raging inflation and higher interest rates have forced consumers and businesses to pull back on spending. While inflation will gradually recede but it will remain above the 2% target through 2023. The Federal Reserve may hike rates to 4.00% by end-2022, and further to 4.25% by 1Q 2023.
- (b) **Growth in euro zone** increased slightly higher in 2Q (0.8% qoq vs. +0.7% in 1Q), but a recession could be on the cards if Russia completely cuts off the region's gas supplies. The European Central Bank (ECB) which has raised interest rates for the first time since 2011, by 0.50% to 0.00% for deposit facility in July, hiked the rates again in September by another 75 basis points to 0.75%. The ECB promises more rate hikes to tackle inflation.
- (c) **Japan's economy** grew by 0.9% qoq in 2Q (0.1% in 1Q) as robust private consumption and private non-residential investment provided a boost. However, the economy still faces an uncertain road to recovery amid slowing global growth and rising inflation, supply chain constraints, a weakening yen, and a resurgence in domestic COVID-19 infections.
- (d) In **China**, real GDP growth slid to 0.4% yoy in 2Q from 1Q's 4.8% as the COVID-related restrictions dealt a heavy blow to sectors ranging from consumption, services to a stressed real estate. The People's Bank of China (PBC) has loosened monetary policy and implement stimulus measures to stem the economic weakness. August's economic data indicates a nascent recovery in certain facets of the economy amid despite headwinds from new COVID-related curbs. Industrial output grew by 4.2% yoy in August, up from 3.8% in July; retail sales increased by 5.4% (2.7% in July) while growth of fixed asset investment remained relatively unchanged at 5.8% in the first eight months of 2022 (5.7% in Jan-Jul).

- **Soaring inflation forces central banks to take forceful and rapid steps in raising interest rates.** With the exception of China is loosening monetary policy and Bank of Japan is keeping its negative policy rate, most central banks see the compelling need to move interest rates upward to avoid entrenched unanchored inflation expectations and damaging their credibility. Policymakers must resolute to control inflation to avoid potentially more painful and disruptive adjustments later.

The Fed chairman Jerome Powell said that interest rates will go up to a higher level and stay there until it is clear that inflation is receding. Such a policy will likely lead to “a sustained period of below-trend growth” and that there will very likely be “some softening of labour market conditions.”

- **Mind the multiple risks ahead.** Against the challenging backdrop of higher and longer inflationary pressures, weaker economic growth prospects, tighter monetary policy and financial conditions, weakening emerging market currencies, the central banks are confronted with a difficult task to act forcefully on inflation while not risking of sapping their economies.

While recession risks in the US economy and Europe have been rising, a global financial crisis is unlikely and the depth of recession if it happens will likely to be shallow.



# Global Economic and Monetary Conditions

## Real GDP growth (% , YoY)

	2020	2021	2022 Q1	2022 Q2	2022F (IMF)	2022F (WB)
<b>World</b>	-3.1	6.1	N/A	N/A	3.2	2.9
<b>United States</b>	-3.4	5.7	3.5	1.7	2.3	2.5
<b>Euro Area</b>	-6.1	5.2	5.4	4.1	2.6	2.5
<b>China</b>	2.2	8.1	4.8	0.4	3.3	4.3
<b>Japan</b>	-4.6	1.7	0.6	1.6	1.7	1.7
<b>India</b>	-6.6	8.7	4.1	13.5	7.4	7.5
<b>Malaysia</b>	-5.5	3.1	5.0	8.9	5.1	5.5
<b>Singapore</b>	-4.1	7.6	3.8	4.4	N/A	N/A
<b>Indonesia</b>	-2.1	3.7	5.0	5.4	5.3	5.1
<b>Thailand</b>	-6.2	1.5	2.3	2.5	2.8	2.9
<b>Philippines</b>	-9.5	5.7	8.2	7.4	6.7	5.7
<b>Vietnam</b>	2.9	2.6	5.1	7.7	N/A	5.8

Note: World GDP growth for 2020 and 2021 by IMF; Annual GDP for India is on fiscal year basis; N/A = Not applicable or not available

Source: Officials (unadjusted data except quarterly GDP for Euro Area); IMF (World Economic Outlook (WEO)); World Bank (Global Economic Prospects)

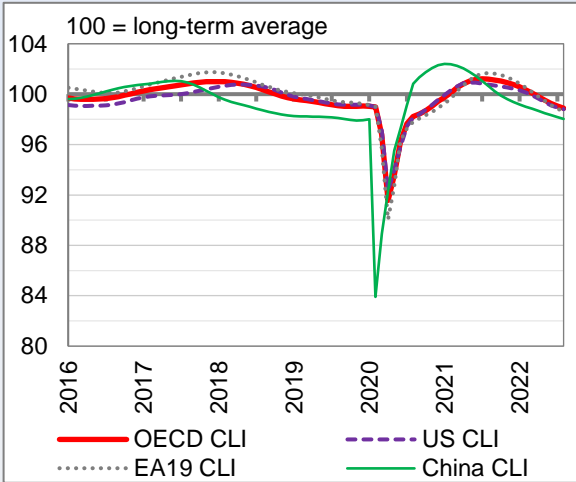
## Policy rate (%)

End-period of	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022 (Aug/ Sep)	2022f
<b>US, Fed</b> Federal Funds Rate	0.00- 0.25	0.00- 0.25	0.00- 0.25	0.25- 0.50	0.50- 0.75	1.25- 1.50	2.25- 2.50	1.50- 1.75	0.00- 0.25	0.00- 0.25	2.25- 2.50	4.00
<b>Euro Area, ECB</b> Deposit Facility	0.00	0.00	-0.20	-0.30	-0.40	-0.40	-0.40	-0.50	-0.50	-0.50	0.75	1.75
<b>Japan, BOJ</b> Short-term Policy I/R	0.00- 0.10	0.00- 0.10	0.00- 0.10	0.00- 0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10
<b>China, PBC</b> 1-Year Loan Prime Rate	6.00	6.00	5.60	4.35	4.35	4.35	4.35	4.15	3.85	3.80	3.65	3.45
<b>India, RBI</b> Policy Repo Rate (LAF)	8.00	7.75	8.00	6.75	6.25	6.00	6.50	5.15	4.00	4.00	5.40	5.60
<b>Korea, BOK</b> Base Rate	2.75	2.50	2.00	1.50	1.25	1.50	1.75	1.25	0.50	1.00	2.50	2.50
<b>Malaysia, BNM</b> Overnight Policy Rate	3.00	3.00	3.25	3.00	3.00	3.00	3.25	3.00	1.75	1.75	2.50	2.50
<b>Indonesia, BI</b> 7-Day RR Rate	5.75	7.50	7.75	7.50	4.75	4.25	6.00	5.00	3.75	3.50	3.75	4.50
<b>Thailand, BOT</b> 1-Day Repurchase Rate	2.75	2.25	2.00	1.50	1.50	1.50	1.75	1.25	0.50	0.50	0.75	1.25- 1.75
<b>Philippines, BSP</b> Overnight RR Facility	3.50	3.50	4.00	4.00	3.00	3.00	4.75	4.00	2.00	2.00	3.75	4.25

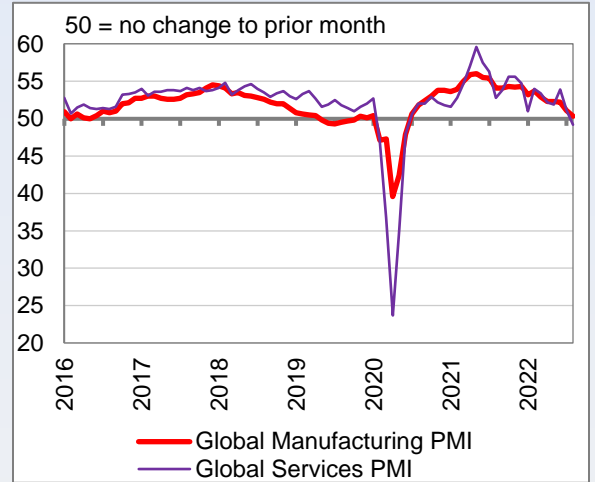
Source: Officials; SERC

# Global Current and Forward Indicators

**OECD composite leading indicators point to weakening growth in most major economies**



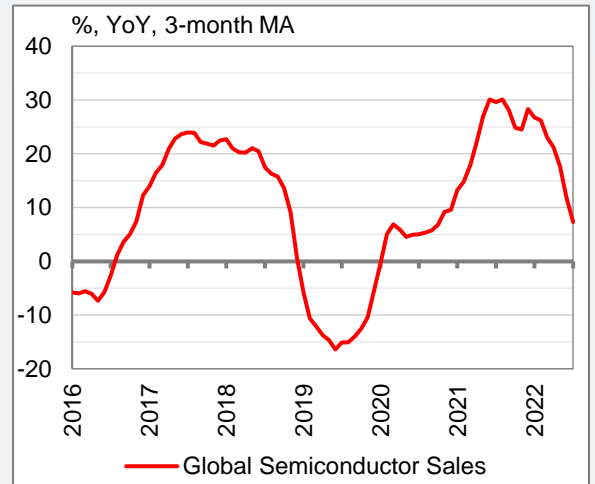
**Global Manufacturing PMI showed declining new orders, especially for exports**



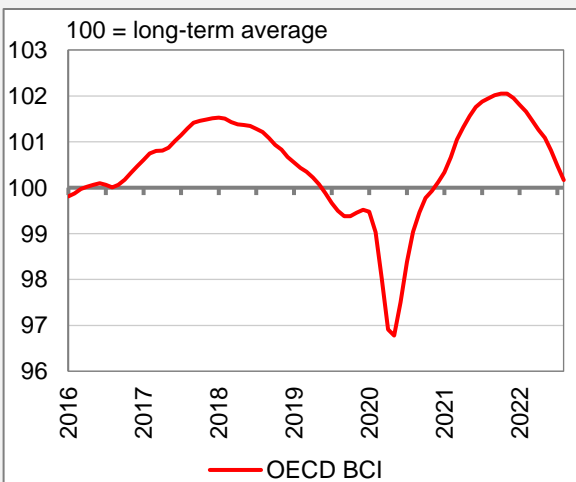
**WTO Goods Trade Barometer suggests that global goods trade is likely to remain weak in 2H 2022**



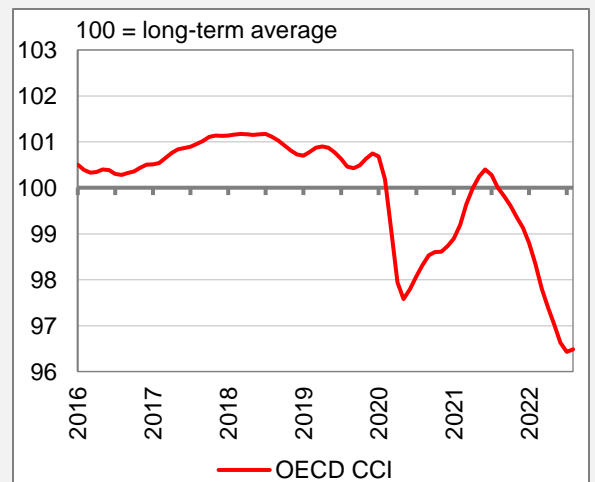
**Global semiconductor sales growth (3-month moving average) continued to moderate**



**OECD Business Confidence Index**



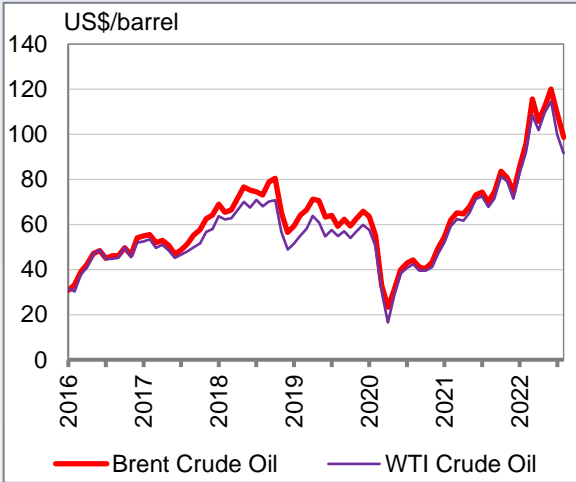
**OECD Consumer Confidence Index**



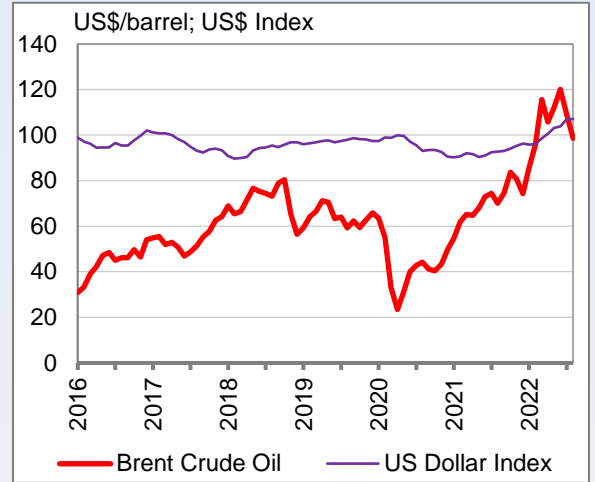


# Global Current and Forward Indicators (cont.)

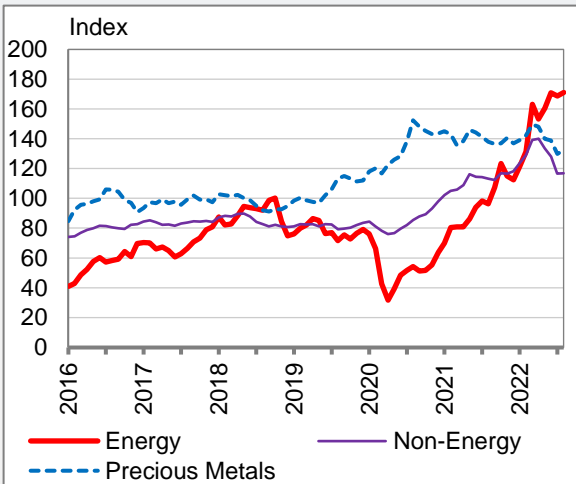
## Brent crude oil prices dropped below US\$100/bbl in Aug



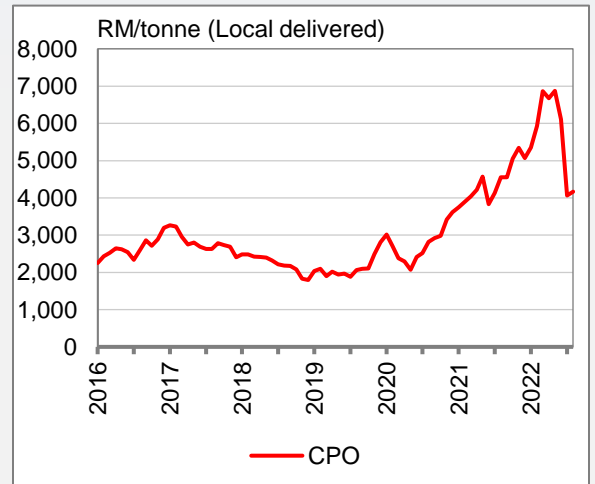
## Brent crude oil price vs. the US dollar index



## Prices of non-energy commodities continued to ease amid still-high energy prices



## Crude palm oil stock is piling up amid softening external demand

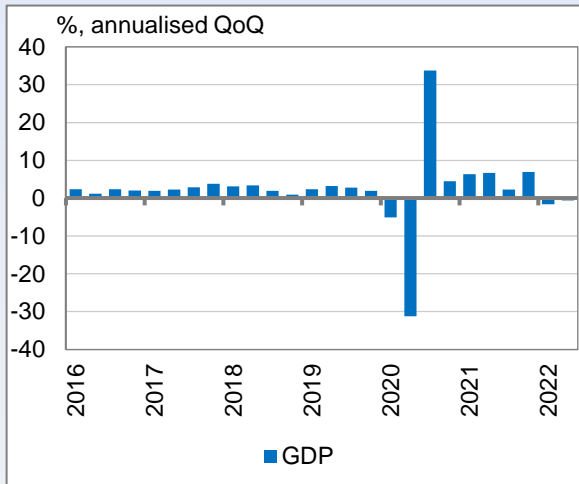


Source: Organisation for Economic Co-operation and Development (OECD); Markit; CPB Netherlands Bureau for Economic Policy Analysis; Semiconductor Industry Association (SIA); World Bank; The Wall Street Journal; Malaysian Palm Oil Board (MPOB)

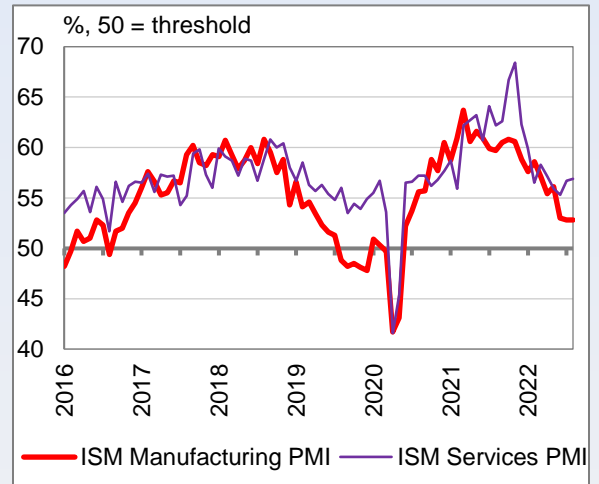


# The US – Slipping into technical recession

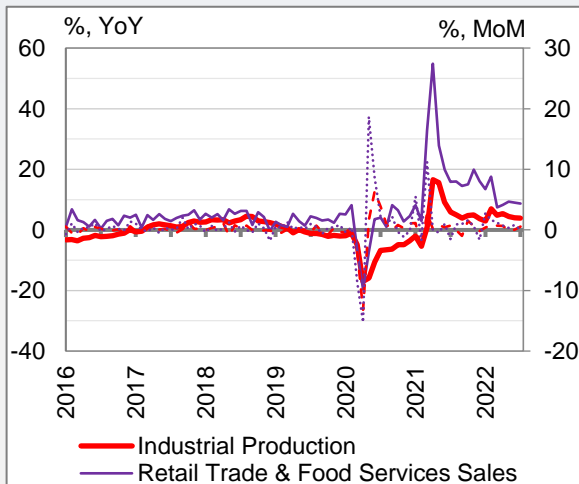
The US economy entered into a technical recession in 2Q



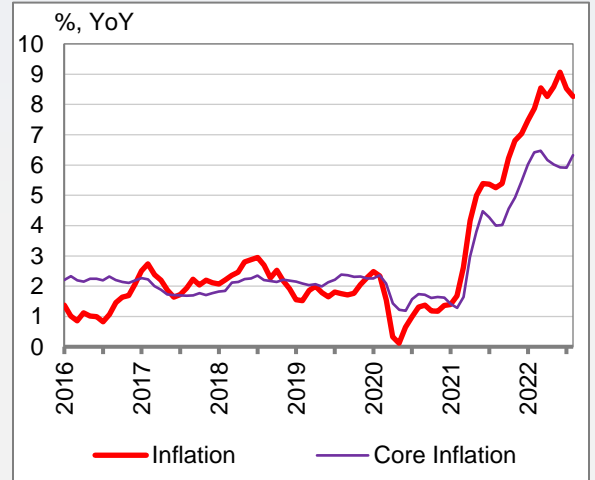
Manufacturing PMI is still growing but at a more moderate pace



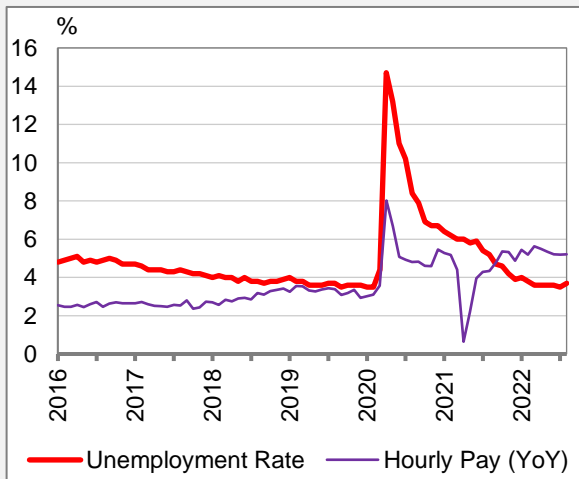
Both industrial production and retail trade sales growth continued to ease



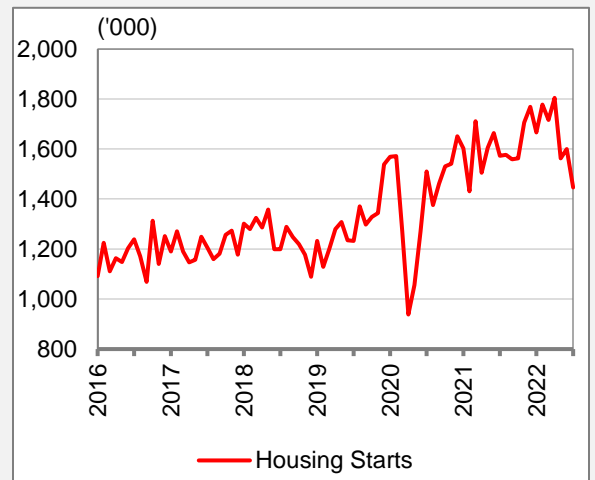
Inflation seems reaching the peak but core inflation still rising



Labour shortage persists amid higher wage growth



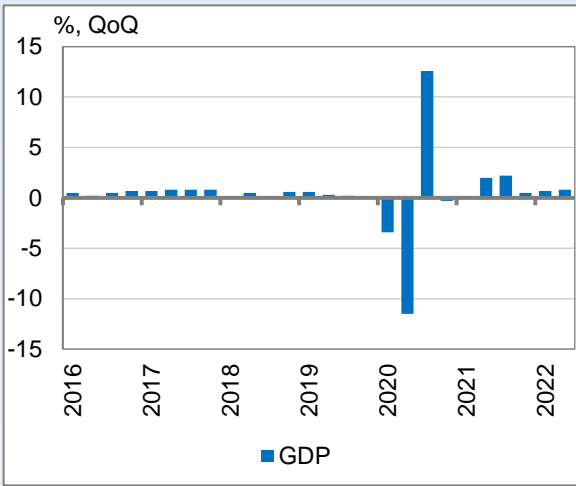
Housing starts slowed down



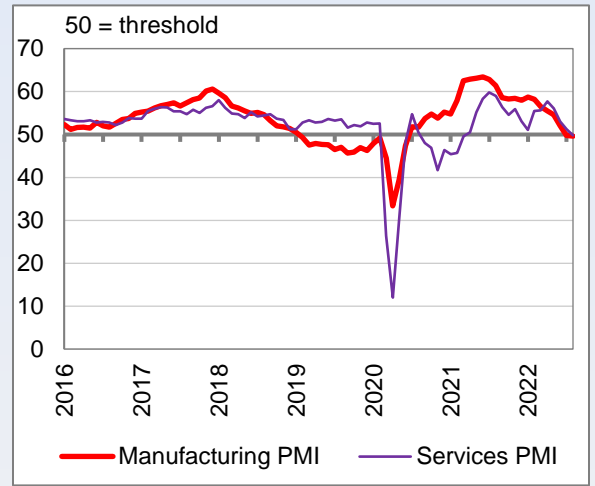
Source: Bureau of Economic Analysis (BEA); Institute for Supply Management (ISM); Federal Reserve System; US Census Bureau; US Bureau of Labor Statistics

# Euro Area – Recession risk is brewing

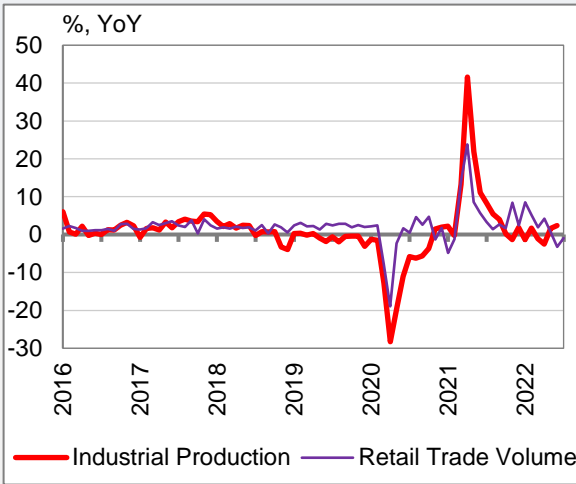
## Continued expansion in 2Q ....



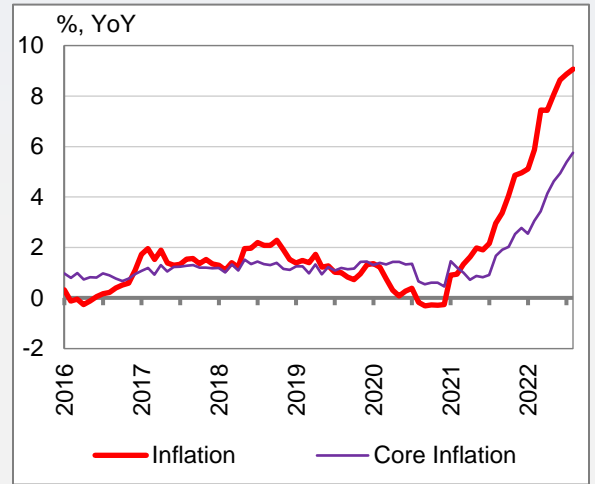
## ... but PMIs signalled contraction ahead



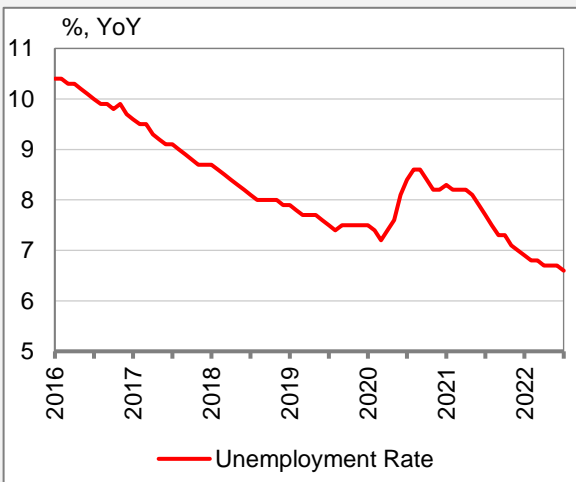
## Retail trade contracted in Jun-Jul after 15 months of expansion



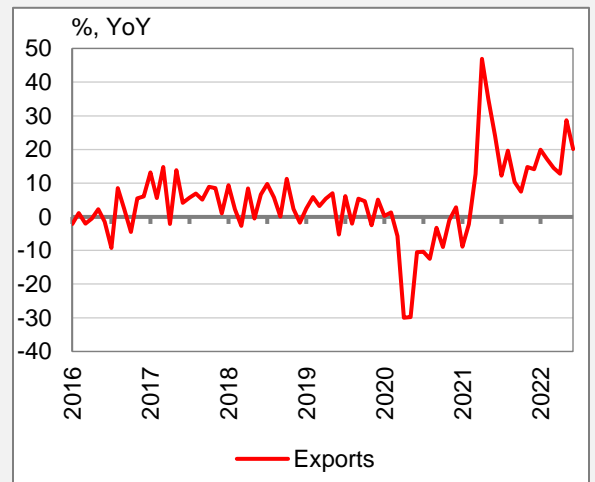
## Inflation continued to climb higher; ECB raised policy rate aggressively



## Unemployment rate continued to trend lower



## Exports growth remained at double-digit for eight straight months in Jun

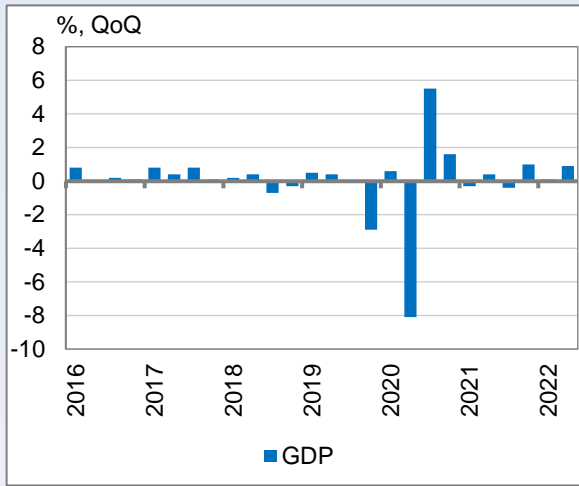


Source: Eurostat; Markit

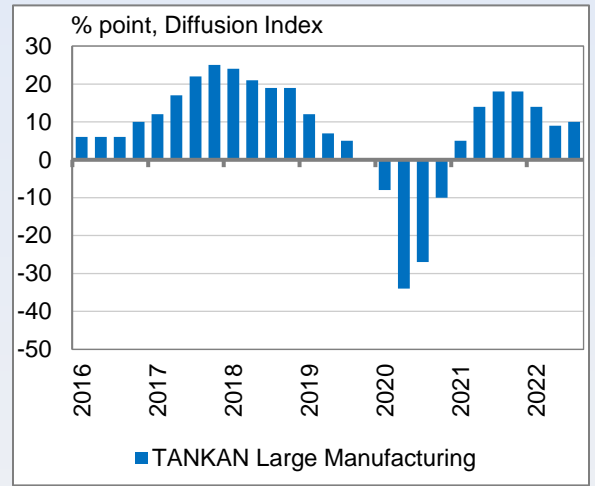


# Japan – Lifted by the COVID-19 curbs

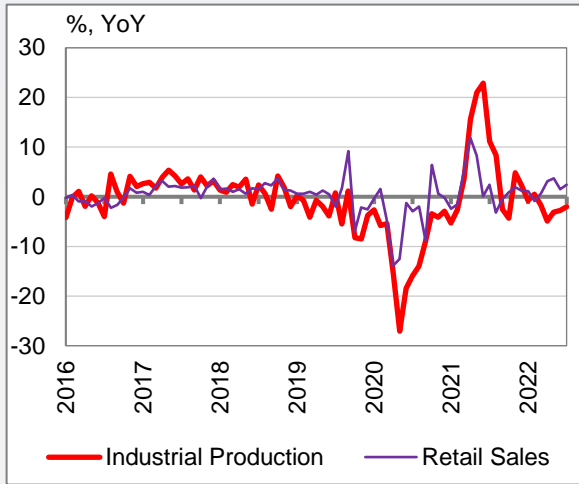
**Economic expansion in 2Q mainly driven by consumption activity**



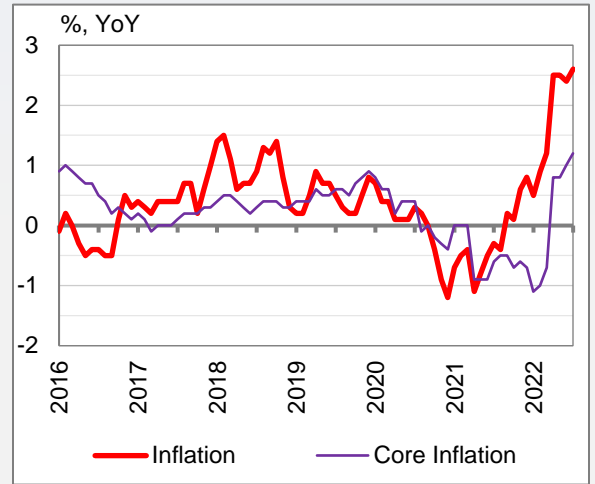
**TANKAN survey signals continued expansion in manufacturing sector ...**



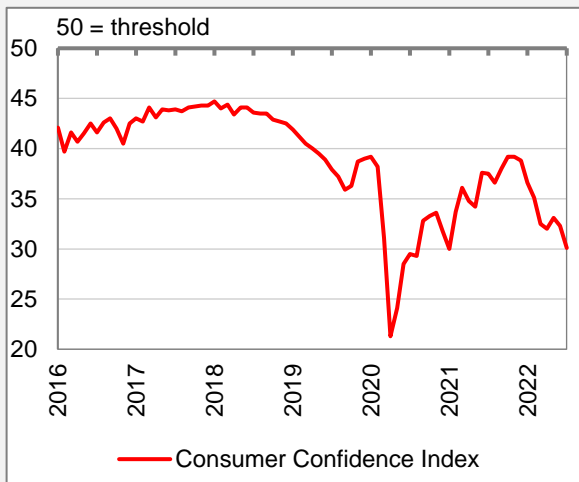
**... but industrial production growth contracted for five months in Mar-Jul**



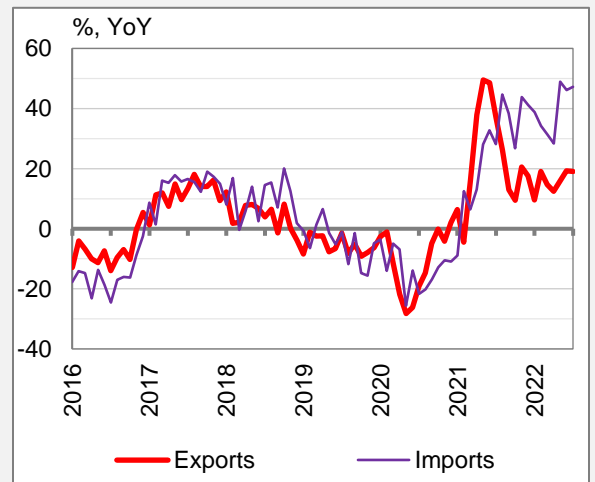
**Inflation at multiple year high**



**Consumer confidence remained pessimistic**



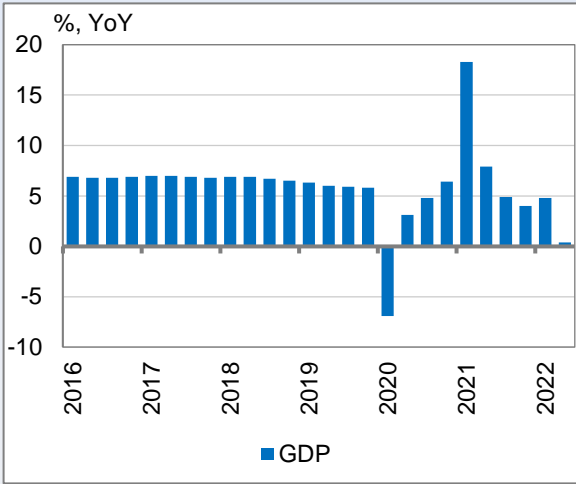
**Strong import growth; trade deficits for twelve months in a row**



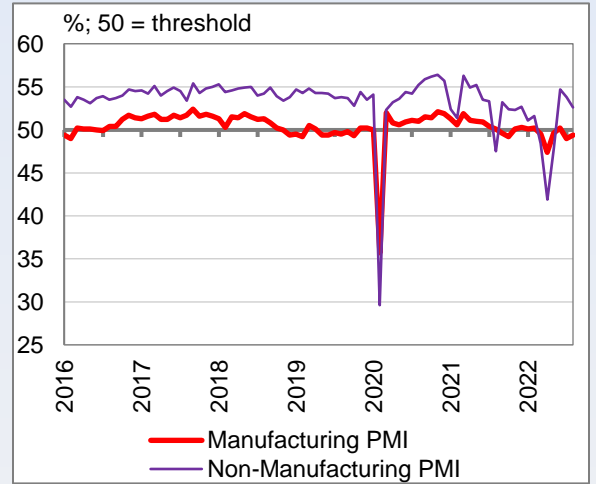
Source: Economic and Social Research Institute (ESRI), Cabinet Office of Japan; Bank of Japan (BOJ); Ministry of Economy, Trade and Industry (METI), Japan; Japan Customs; Statistics Bureau, Japan

# China – Economic activities are decelerating

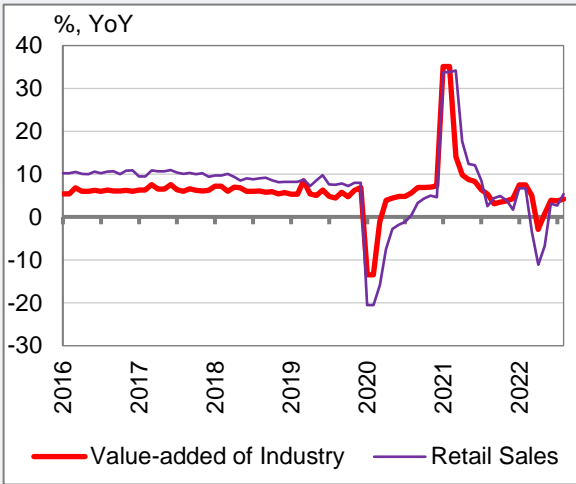
**Marginal economic growth in 2Q, the worst pace since COVID-19 outbreak**



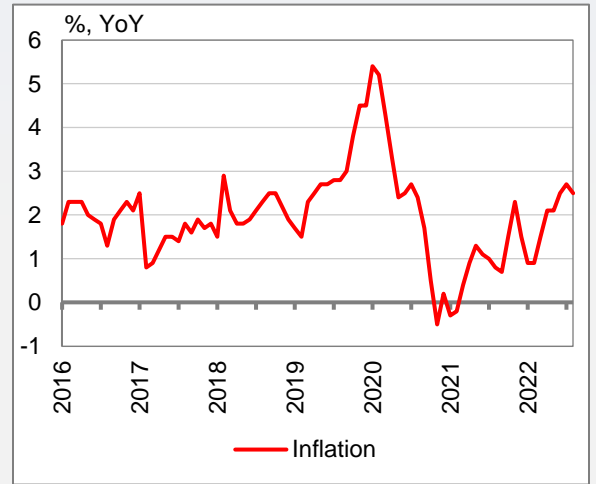
**Manufacturing PMI stayed at negative territory in Aug**



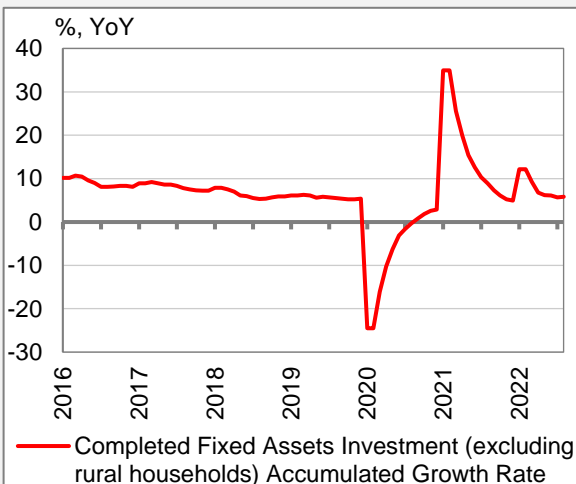
**Industrial and retail trade growth showed a nascent recovery in Aug**



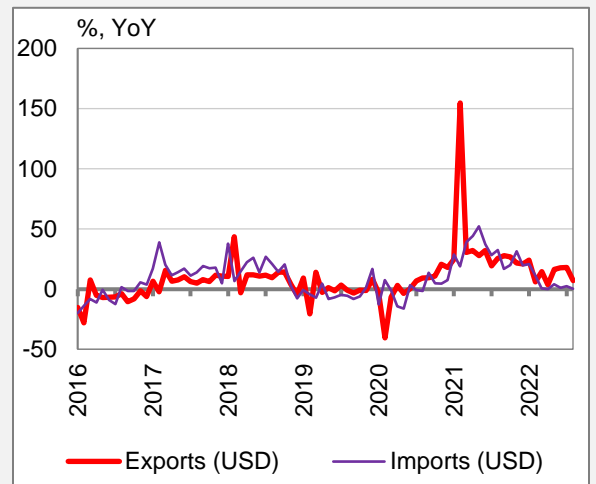
**Inflation climbs higher though lower compared to other countries**



**Fixed investment growth continued to moderate**



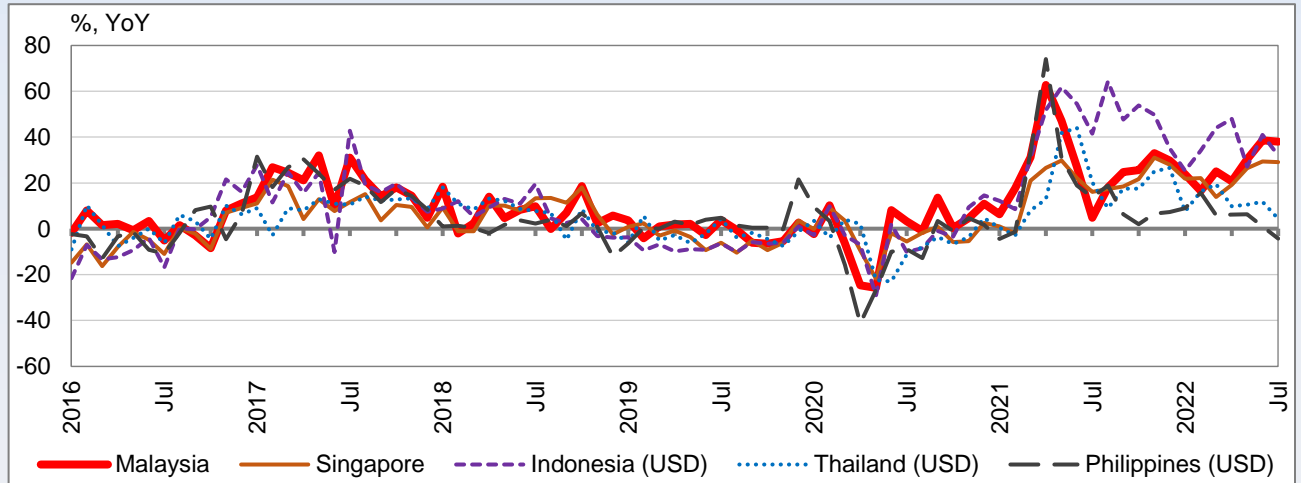
**Export growth remained favourable albeit at a more moderate pace**



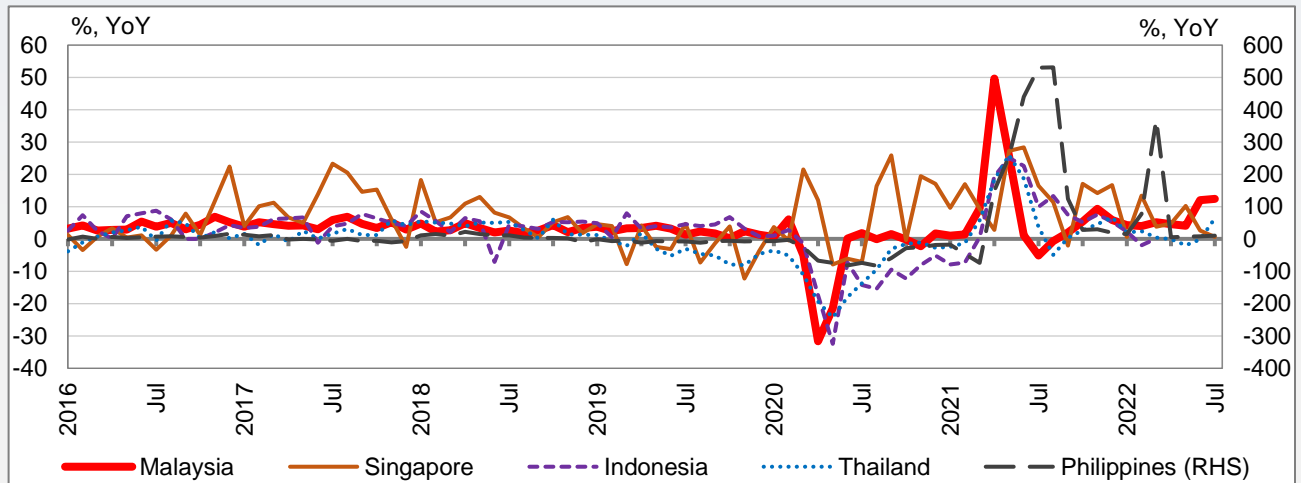
Source: National Bureau of Statistics of China; General Administration of Customs, China

# ASEAN Economies

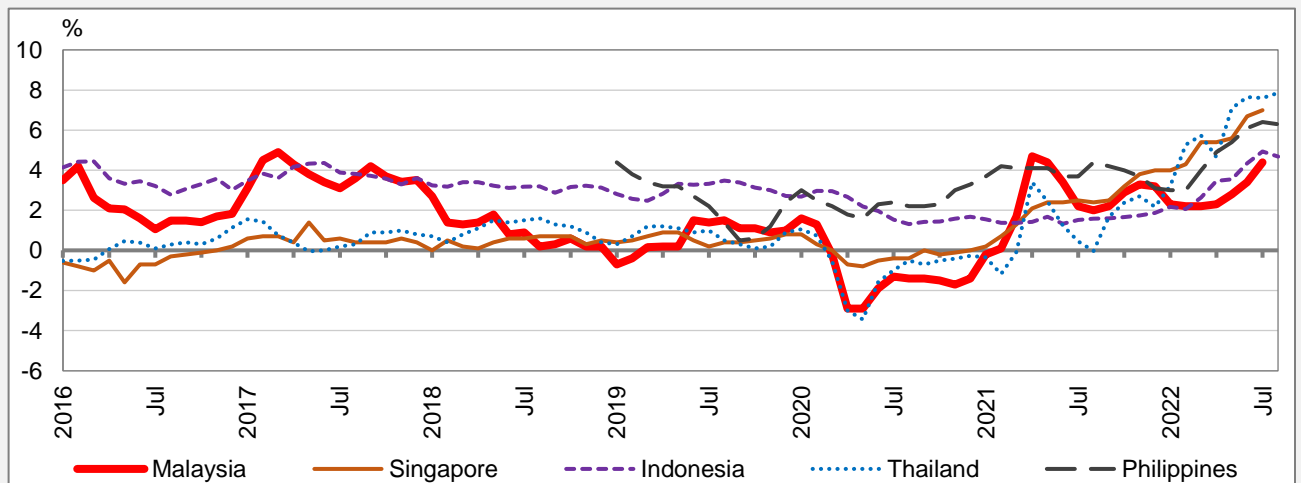
## Export growth trend



## Industrial production growth trend



## Inflation trend



Source: Department of Statistics, Malaysia; Singapore Department of Statistics; Statistics Indonesia; Bank Indonesia; Bank of Thailand; Office of Industrial Economics, Thailand; Ministry of Commerce, Thailand; Philippine Statistics Authority



## CAN MALAYSIA SUSTAIN A RESILIENT ECONOMIC RECOVERY?

- **Extraordinary economic growth in 2Q 2022.** With the reopening of economy and international borders, robust domestic demand, especially private consumption and continued exports have delivered an exceptional 8.9% yoy real GDP in 2Q 2022 (5.0% in 1Q). Real GDP averaged 6.9% in 1H 2022. On a monthly compilation, real GDP grew by 5.6% yoy in April, 5.0% in May before expanded robustly by 16.5% in June, largely boosted by a low base effect in June 2021 on the Movement Control Order (MCO).

Following a much higher 2Q GDP, we have revised this year's GDP estimate to 6.5% in 2022 from 5.2% previously. Preliminary data suggests a strong growth estimated 8.0%-9.0% in 3Q, partly aided by technical base yoy comparison (-4.5% in 3Q 2021). We maintain our real GDP growth forecast of 4.2% for 2023.

Looking behind the numbers, the recovery pace remains uneven among major economic sectors. Both services and manufacturing sectors have showed stronger-than-expected growth in 2Q; the construction sector has rebounded but still weak while the mining and agriculture sectors declined.

- **Consumers would be the deciding force in deciding whether the turbocharged 2Q GDP growth can be sustained in the quarters ahead.** The drivers for a robust private consumption growth in 2Q (18.3% yoy vs. 5.5% in 1Q) are the release of pent-up consumer spending supported by continued cash handouts; the fourth withdrawal of EPF money estimated RM45 billion; and also, higher demand during the Hari Raya Aidilfitri festive celebration. In addition, a revival in tourism activity, albeit largely supported by domestic tourists as foreign tourists are gradually returning.

As consumer spending accounts for 58.8% of the Malaysian economy, we have been closely watching for signs of a cool-down. Will robust consumer spending growth continue unabated in 2H 2022 and in 2023?

- **Going into 2H 2022 and in 2023, we remain wary about the strength of consumer spending** on rising inflation, higher cost of living and the tapering effect of consumption and cash flow assistance measures such as the ending of targeted loan repayment assistance, and resumption of the EPF employees' contribution rate starting July 2022.

While consumers keep spending, but the price increases and higher cost of living are weighing on them and could soon lead to a change in behaviour. Some consumers have locked-in purchase of cars in June 2022 due to the expiry of SST exemption; and have front-loaded purchases of goods and services in anticipation of higher price increases ahead.

The mood of shoppers is expected to remain cautious due to rising prices as consumers tightened purse strings on consumer durables and big-ticket items. The Consumer Sentiments Index dipped far below the 100-point optimism threshold to a four-quarter low of 86.0 in 2Q 2022 on tight present and expected household finances amid less inspiring employment outlook.

Essentially, Malaysians are having to spend more to buy the same amount of goods and services. Real consumer spending devalues as inflation increases. Despite an increase in nominal wage growth in 2Q 2022 (Private sector: +7.8%; manufacturing: +5.2%; services: +9.3%), the increase in prices have taken off the increase in wages; and higher expenditure incurred is also running well above the increase in income. As a result, many households are having to dip into savings or take on debt to fund their spending.

- **Domestic and external headwinds dampen private investment.** Private investment has gained higher growth traction in 2Q (6.3% yoy vs. 0.4% in 1Q 2022), due to improvement in structures and continued expansion in machinery and equipment investment. However, the headwinds remain: Shortage of workers, increased business costs, the weakening ringgit and concerns about slowing global growth and recession risk in the US economy.

While businesses are expecting a cautious business and demand outlook in the months ahead, but so far many have experienced somewhat much slower sales but not seen a sharp plunge in consumer spending.

- **On the external sector, exports increased by 38.0% yoy in July** (29.9% in 2Q), backed by higher demand of electronics and electrical products (Jan-Jul: +32.8%; 37.8% share of total exports), petroleum products (+57.9% and 9.5% share), palm oil (+51.6% and 5.7% share), chemicals and chemical products (+19.3% and 5.3% of share), manufactures of metal (+27.4% and 4.6% share), liquefied natural gas (+74.9% and 4.0% share), machinery, equipment and parts (+25.5% and 3.9% share) as well as optical and scientific equipment (+19.5% and 3.6% share).

We expect exports to grow by 19.9% in 2022 (26.1% in 2021), with a more moderate pace of averaging 14.4% in 2H 2022 from an average growth of 26.1% in 1H. This reflected the impact of weakening global economy as well as easing commodity and energy prices.

- **Headline inflation accelerates. Headline inflation** increased higher to a 14-month high of 4.4% yoy in July (3.4% in Jun vs. 2.5% in 1H 2022), in tandem with the strengthening of consumer demand, increased prices of some essential food items (i.e. chicken, eggs, and cooking oil) and services as well as the lapse of low base effects, especially for electricity tariffs. **Core inflation** also quickened to 3.4% in July from 3.0% in June (2.2% in 1H 2022), marking the highest level since March 2016, reflecting higher consumer spending.

The Government has implemented various administrative measures such as subsidies and price ceiling on cooking oil, fuel, chicken and eggs as well as electricity and gas. This will offer some relief and protect consumers by keeping prices low in the current environment of rising consumer price pressures and cost of living. In Jan-Jul 2022, inflation increased by 2.8%. SERC estimates headline inflation to increase by 3.5% in 2022, higher than Bank Negara Malaysia (BNM)'s estimated between 2.2% and 3.2%. The drivers of inflation are low-base effects particularly electricity tariffs, still-high commodity prices, persistent weak ringgit and cost pass-through effects will push headline inflation above 4.0% in the months ahead.

- **Interest rate to remain 2.50% by end-December 2022.** We believe that Bank Negara Malaysia will take into consideration the impact of its gradual and measured pace of interest rate hiking trajectory due to growth risks while keeping inflation under its radar. Bank Negara Malaysia has been raising interest rates for three consecutive meetings since May to 2.50% currently, still 50 basis points away from 3.00% in 2019. BNM highlighted that they will ensure the monetary policy to remain accommodative to support a sustainable economic growth in an environment of price stability.
- **Risks to economic growth in 2H 2022 and 2023.** We concur with Bank Negara Malaysia's assessment of downside risks to the growth outlook. These include the deceleration in global growth and we are concerned about recession risks in the US economy and Europe, supply disruptions and further increases in energy and commodity prices, acute labour shortages, stronger cost and price pressures as well as the disruptive spill-over effects of higher US interest rates on global financial and foreign exchange markets.



We believe that policymakers need to watch consumption and business investment for signs of cyclical strength or weakness over the next 6-12 months. **Lingering concerns about the global and US economy prospects, softening demand, inflation and cost pressures would weigh on household consumption and business activity.**

## 2023 BUDGET - FISCALLY RESPONSIBLE WITH REFORMS THRUST

- **The 2023 Budget must be fiscally responsible with reforms thrust to keep the fiscal consolidation on track.** As the economy has moved out of the economic contraction, it is no longer require extraordinary massive deficit fiscal spending packages as delivered during the COVID-19 pandemic in 2020-2022.
- **We estimate a deficit budget of 4.5%-5.5% of GDP in 2023** compared to an estimated average deficit of 6.2% in 2020-2022. The short-term intentions to sustain firmer economic recovery must ensure that fiscal resources are managed effectively and efficiently, having regard to its likely impact on present and future generations. Managing prudently the fiscal and debt risks facing the Government.
- The Budget's strategies focus on implementing credible economic policies and undertaking structural reforms geared towards enhancing our nation's competitiveness and better investment climate, ensuring economic growth sustainability as well as making life better for individuals and families.
- The Budget must seek to **re-prioritize public spending towards expenditures in infrastructure, climate change related projects, health, transportation, skills development, education and supporting the vulnerable segment of the population. The implementation of 5G infrastructure must be accelerated; facilitate private sector, especially SMEs transition towards the adoption of ESG.**

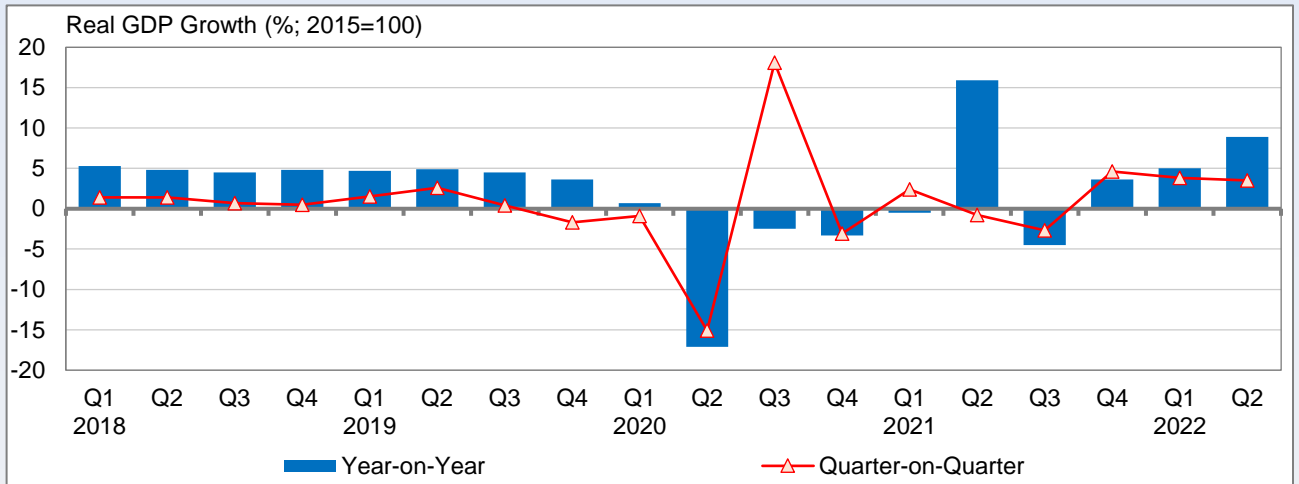
## Real GDP growth (% , YoY)

Economic Sector [% share to GDP in 2021]	2020	2021	2022 Q1	2022 Q2	2022E (BNM)	2022E (SERC)
<b>By kind of economic activity</b>						
Agriculture [7.1%]	-2.4	-0.2	0.1	-2.4	1.5	-1.4
Mining & Quarrying [6.7%]	-9.7	0.3	-1.1	-0.5	2.5	-0.8
Manufacturing [24.3%]	-2.7	9.5	6.6	9.2	5.2	6.6
Construction [3.7%]	-19.3	-5.2	-6.2	2.4	6.1	3.2
Services [57.0%]	-5.4	1.9	6.5	12.0	6.9	8.7
<b>By type of expenditure</b>						
Private Consumption [58.8%]	-4.2	1.9	5.5	18.3	9.0	10.0
Public Consumption [13.8%]	5.0	5.3	6.7	2.6	1.2	5.1
Private Investment [15.6%]	-11.9	2.6	0.4	6.3	5.3	5.2
Public Investment [4.5%]	-21.2	-11.3	-0.9	3.2	9.6	3.0
Exports of Goods and Services [69.1%]	-8.6	15.4	8.0	10.4	4.8	8.5
Imports of Goods and Services [63.1%]	-7.9	17.7	11.1	14.0	5.1	11.1
<b>Overall GDP</b>	<b>-5.5</b>	<b>3.1</b>	<b>5.0</b>	<b>8.9</b>	<b>5.3-6.3</b>	<b>6.5</b>

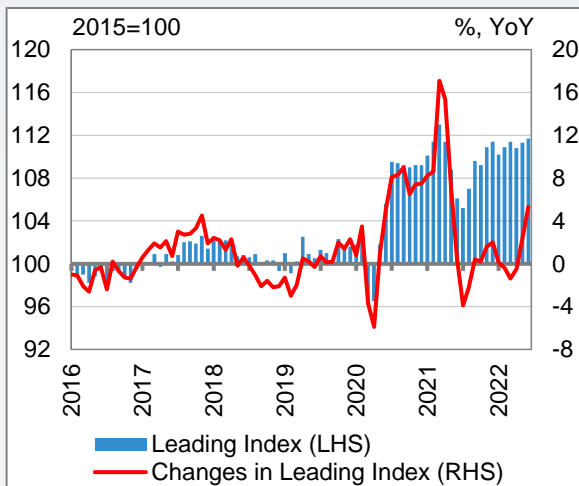
Source: Department of Statistics, Malaysia (DOSM); SERC estimates and forecast

# Spotlight on the Malaysian Economy

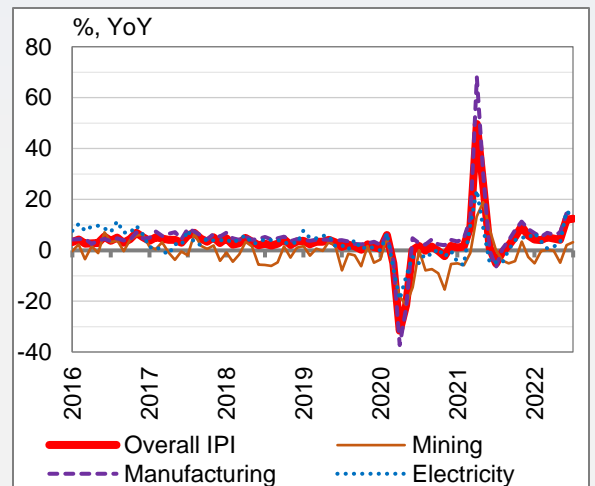
Malaysia's extraordinary 2Q GDP growth outperformed most countries in the world



Leading Index (LI) continued its good performance in Jun

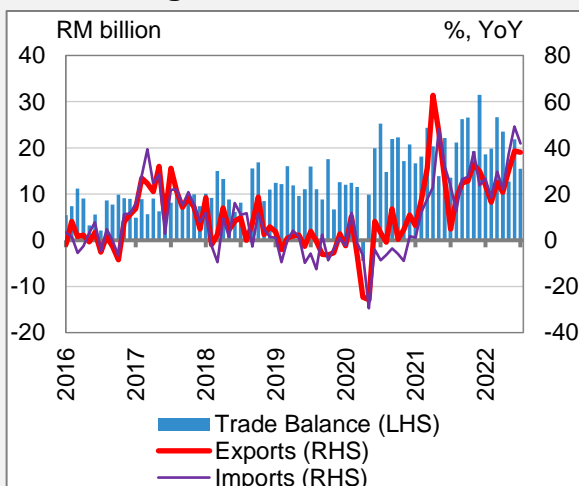


Industrial production growth at double-digit in Jun-Jul; mining growth turns positive

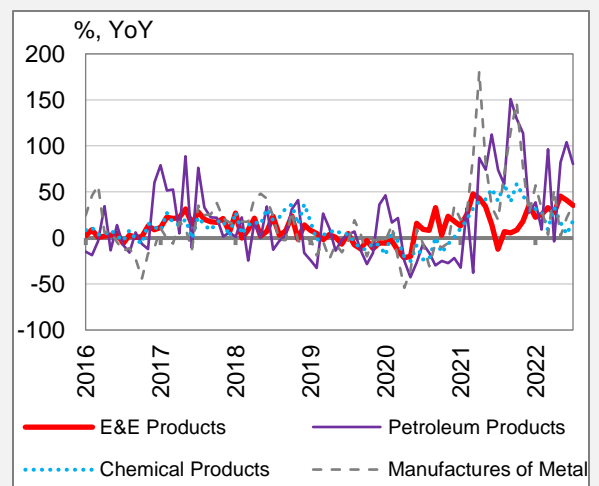


## External Sector

Export performance remained robust in most segments



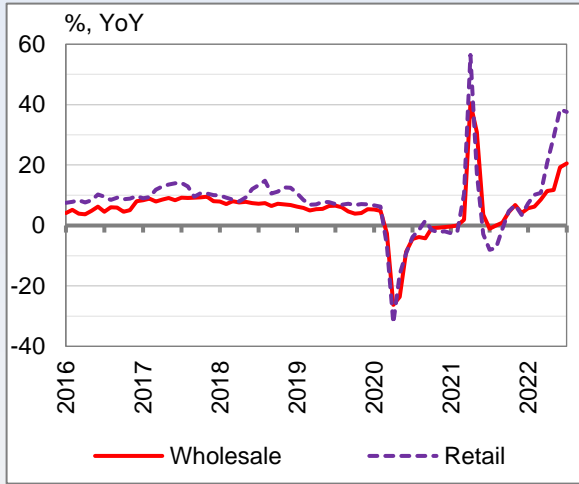
Exports by major products



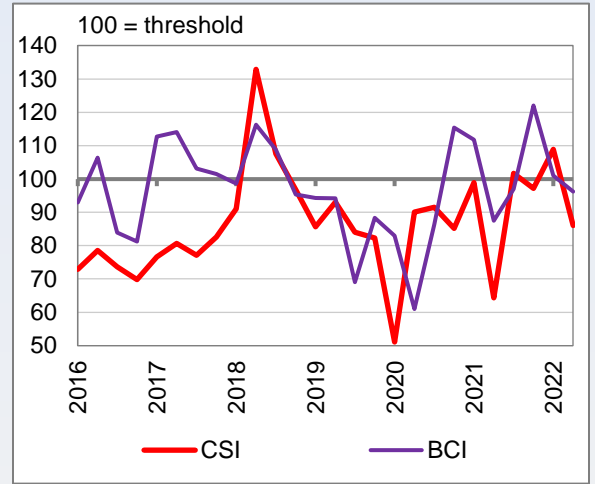
# Spotlight on the Malaysian Economy (cont.)

Domestic demand will remain a prime mover of 3Q's GDP growth

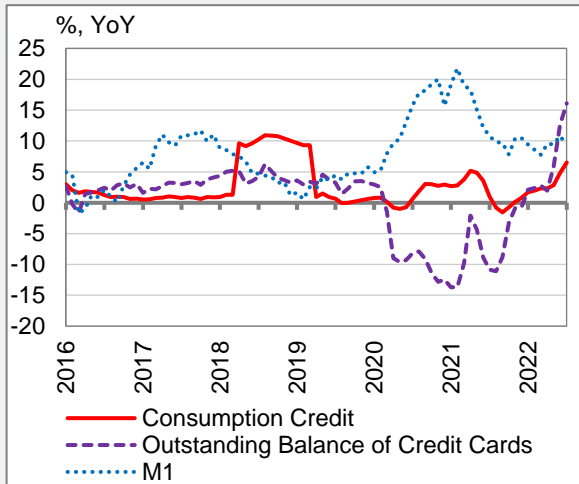
Distributive trade continued to charge ahead



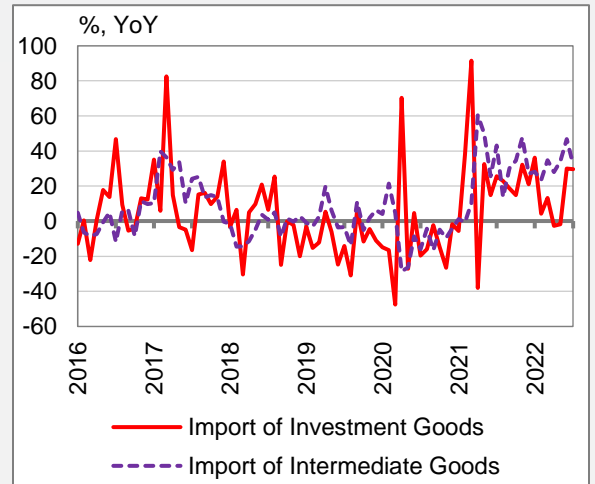
Both consumer sentiments and business confidence dipped further



Selected private consumption indicators



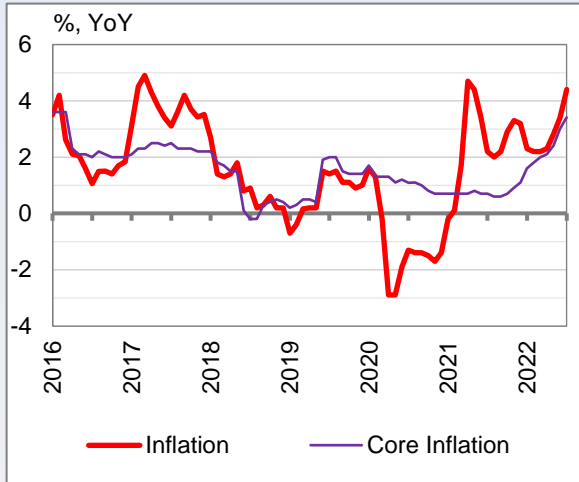
Selected private investment indicators



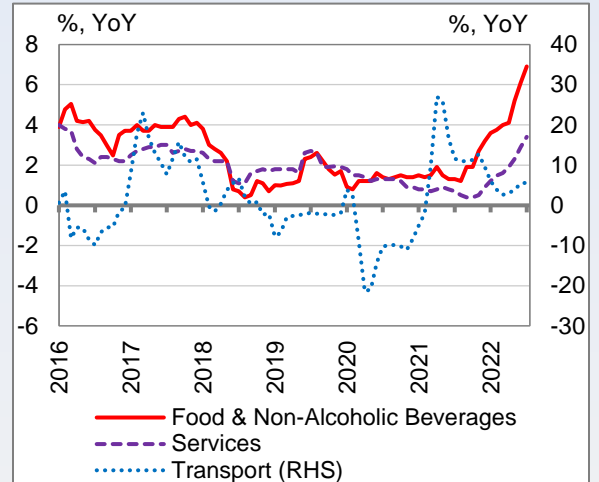
# Spotlight on the Malaysian Economy (cont.)

## Price Indicators and Labour Market

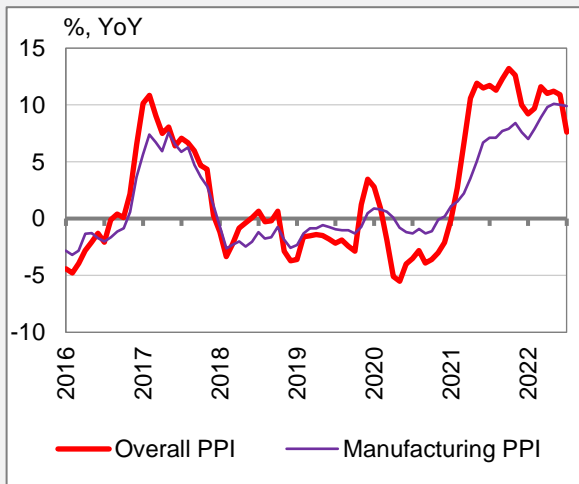
**Headline inflation will remain high in the months ahead due to high food prices and low base effect**



**Consumers feel the pinch from surging food prices amid subsidies and price controls**



**Producer prices seems coming down from the peak**



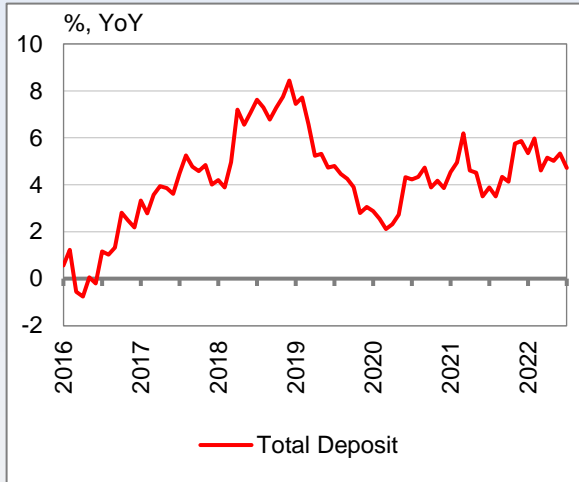
**Job market continued to improve; labour shortages have eased a little**



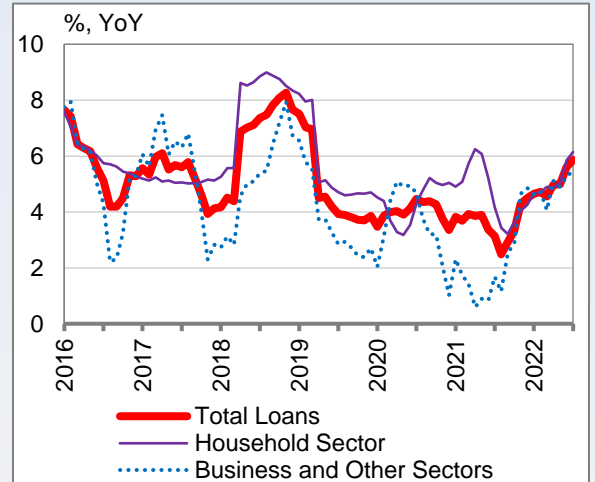
# Spotlight on the Malaysian Economy (cont.)

## Banking and Financial Indicators

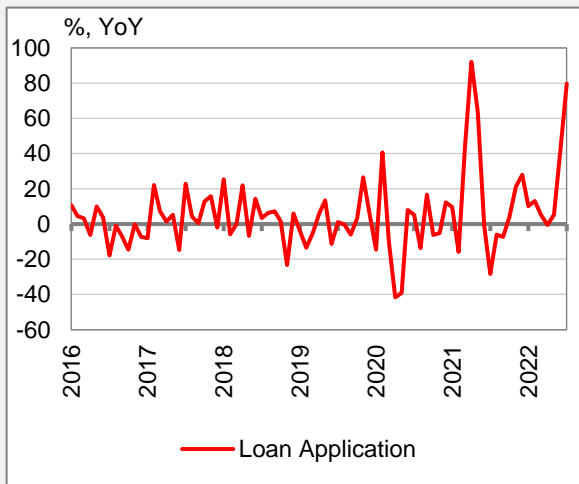
**Banking deposit growth stable around 5%**



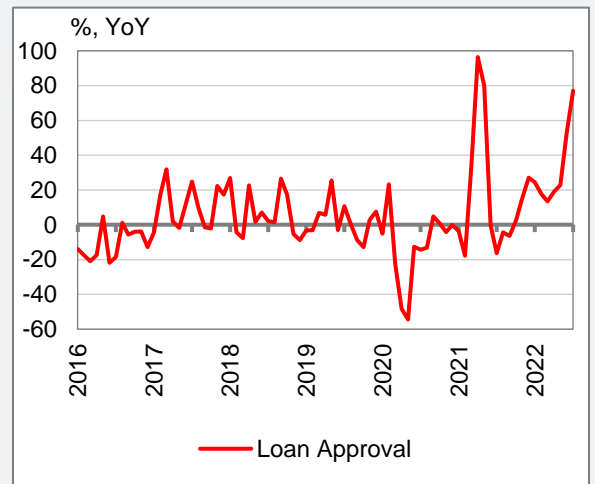
**Total outstanding loan expanded, contributed by both household and business sectors**



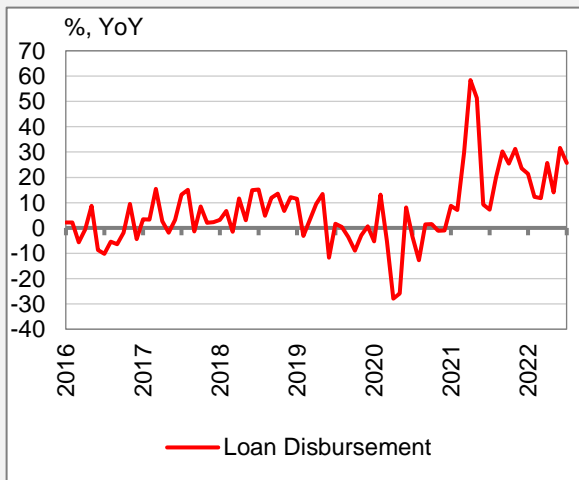
**Loan applications growth**



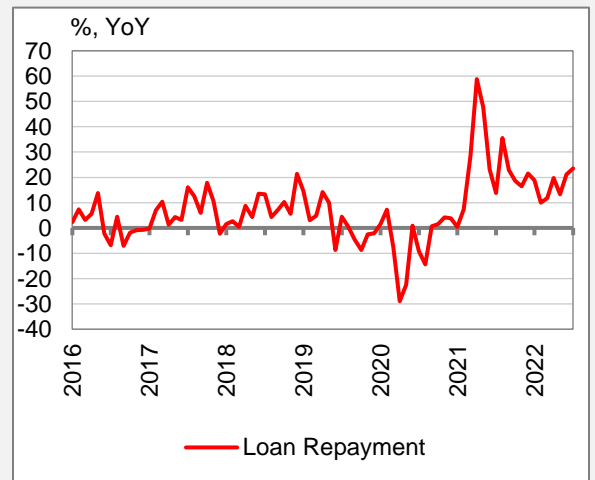
**Loan approvals growth**



**Loan disbursements growth**



**Loan repayments growth**

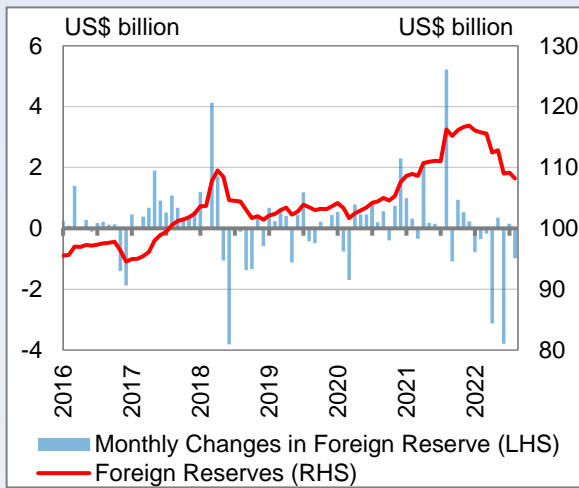


Note: Loan data from July 2022 onwards was revised and expanded based on the latest requirements with more accurate data definition and reporting methodology.

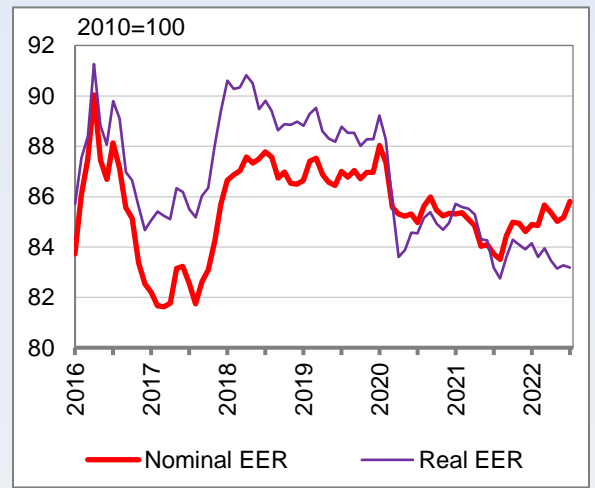


# Spotlight on the Malaysian Economy (cont.)

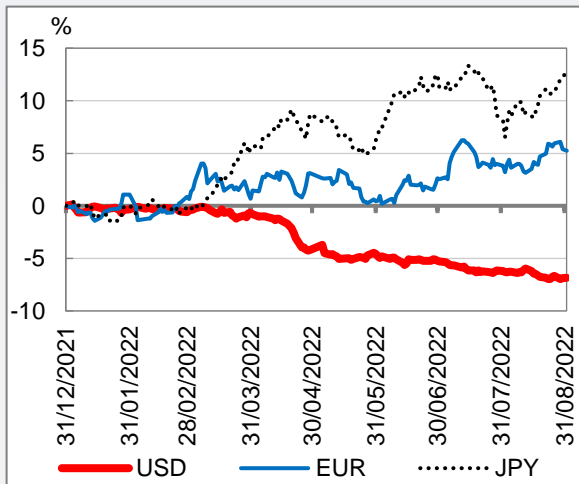
## Foreign reserves declined continuously



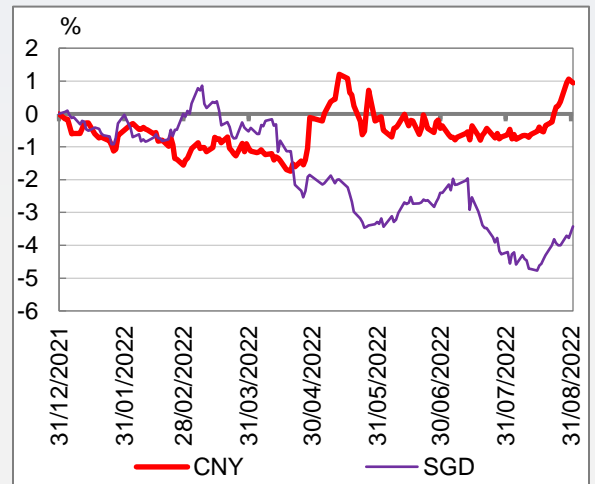
## Ringgit's Effective Exchange Rate (EER)



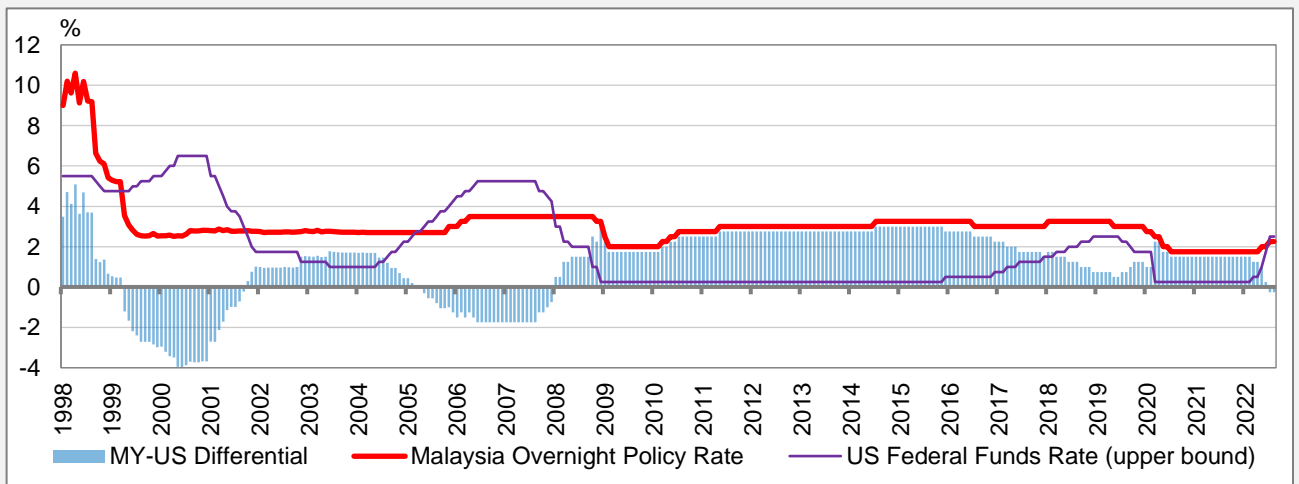
## The Ringgit against the US dollar, euro and Japanese yen



## The Ringgit against the Chinese renminbi and Singapore dollar



## Malaysia-US's interest rate differentials



Source: Department of Statistics, Malaysia (DOSM); Malaysian Institute of Economic Research (MIER); Bank Negara Malaysia (BNM); Bank for International Settlements; Federal Reserve



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### **About SERC**

The Associated Chinese Chambers of Commerce and Industry of Malaysia (ACCCIM)'s Socio-Economic Research Centre (SERC Sdn. Bhd.) was established as an independent and non-profit think tank on 19 October 2010. Officiated by YAB Prime Minister on 28 April 2011, SERC is funded by ACCCIM SERC Trust.

SERC is tasked with carrying out in-depth research and analysis on a wide range of economic, business and social issues in support of the formulation of public policies to shape Malaysia's national socio-economic and industrial development agenda.

The organization will identify and explore issues and future trends that impact domestic economic and business environments. It will also focus on sharing knowledge and promoting public understanding of socio-economic issues of national importance.