SME SENTIMENT INDEX 1H 2025

SME BANK — A Subsidiary of BPMB Malaysia Development Bank

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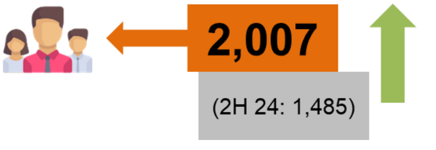
Summary: Less optimism among MSMEs

Micro, small, and medium enterprises (MSMEs) continue to be optimistic about the near future but at a reduced degree as reflected by a slightly lower index of 55.2 in 1H 2025 (2H 2024: 55.8). This also marked the turning point from our last four surveys where consistent upward trends were observed amid strong recovery post Covid-19. Currently, the moderation in sentiment among entrepreneurs was driven by lower expectations in almost all segments, such as business sales and expansion as well as weaker hiring activities.

This cautiously optimistic sentiment among MSMEs aligns with other forward-looking indicators, including Department of Statistics Malaysia's (DOSM)'s Leading Index which predicts softer economic conditions in the coming months. As a leading economic indicator, this SME Sentiment Index suggests that Malaysia's overall economy will continue to expand in 2025, albeit at a modest pace. Our 1Q 2025 GDP growth eased to 4.4% YoY (4Q 2024: 4.9%), the lowest since 1Q 2024 (4.2%) which signals a weak start to the year as it slipped off the official 2025 GDP forecast range (4.5% - 5.5%). Nonetheless, the growth rate is still above some regional peers such as Thailand (3.1%) and Singapore (3.9%).

The SME Sentiment Index survey, conducted between January and April 2025, hit a new record high of 2,007 respondents (2H 2025: 1,485), encompassing participants from 39 sectors across all business sizes.

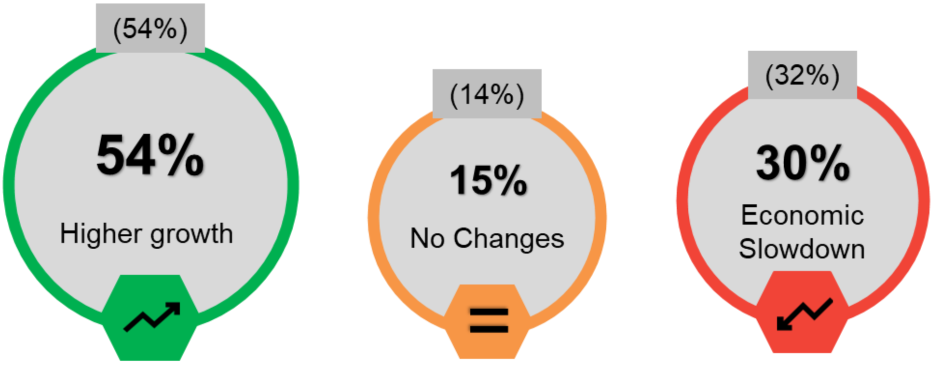
Number of respondents:



US reciprocal tariff influences MSMEs' expectation on economic outlook

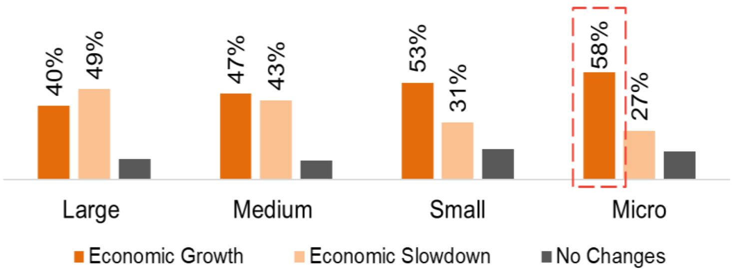
Overall, most respondents (54%) except large-sized businesses continue to **express optimism regarding the economic outlook over the next 6 to 12 months**, unchanged from 2H 2024. However, it slightly waned to 51% in the latter part of the survey window, following the announcement of the US reciprocal tariff measures on 2 April 2025. Increased uncertainty on the external front could lead to downward revision for this year's GDP growth projection of 4.5% to 5.5% (2024: 5.1%), mainly stemming from the potential slowdown in global trade. The World Trade Organisation foresees a -0.2% contraction in global trade for 2025, down from +2.9% in 2024 (2026f: +2.5%). Nonetheless, with the 90-day pause of US reciprocal tariffs, it could lend some short-term gains due to front-loading activities. Nonetheless, resilient domestic demand remains a key engine of growth for the Malaysian economy this year to cushion potential external shocks, pending the outcome of trade negotiations with the US.

Figure 1: 54% of MSMEs expect the economy to grow over the next 6 to 12 month.



In general, **there has been a significant shift in the expectation of economic growth** across business sizes this round, compared to the previous survey. In this 1H 2025 survey, **micro (58%) businesses are more optimistic, whereas small (53%), medium (47%) and large (40%) are comparatively more cautious**. This is a reversal from 2H 2024 survey, where large businesses were the most optimistic. External developments particularly of the ongoing US tariff threats seem to have taken a toll on larger businesses' sentiment as they tend to be more involved in external trade. Based on our survey, large businesses sourced 58% of their raw materials from foreign markets, followed by medium companies (47%). Likewise, large (13%) and medium (24%) sized businesses have a higher share of their export-to-overall sales, compared to their small (12%) and micro (4%) counterparts.

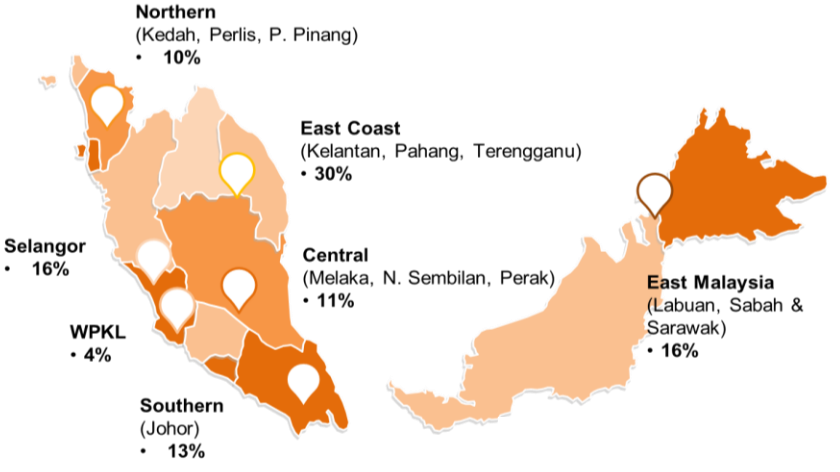
Figure 2: Micro business is the most optimistic.



By sector, **education** (1H 2025: 65%; 2H 2024: 50%) has the **highest confidence in the economic outlook**. Its nature of domestic-oriented (less exposure to external shocks) as well as other favourable growth factors such as growing wages/disposable income and government's promotion of Technical and Vocational Education and Training (TVET) are potential contributors. In line, private education sales have been growing steadily over the past few years (2024: 9.5% YoY; 2023: 8.7%).

Prime Minister has revealed that the education sector will undergo major structural reforms under the 13th Malaysian Plan (2026 – 2030), to comprehensively address the needs of students and teachers as well as future industry talent needs including strengthening STEM (Science, Technology, Engineering and Mathematics) & TVET. Second to education, the manufacture of other non-metallic mineral products (64%) sector has a promising outlook of our economy, followed by administrative & support service activities (61%).

Figure 3: Respondents by state/region (share %)



By state, while **East Malaysia are more optimistic on economic growth** in the coming months, **states in Peninsular Malaysia have mixed views**. Northern states – Kedah, Pulau Pinang and Perlis – along with Negeri Sembilan are pointing towards a slowdown. Inflow of foreign manufacturing investment to Malaysia picked up significantly especially to the Northern states, post Trump's Tariff War 1.0 in 2018, seen as partially to avoid the tariffs. Kedah's foreign manufacturing approved investment surged by 7 folds to RM167.0 bil during 2018 - 2024, up from a meagre RM20.6 bil in 2011 - 2017. Likewise, Pulau Pinang's foreign manufacturing approved investment rose almost 4 times to RM207.4 bil during the same period. Although these states could be vulnerable to the US reciprocal tariffs given heightened uncertainties at this juncture, the majority of MSME respondents in these states still plan to expand their businesses.

Micro businesses foresee better sales performance than previously

Easing sales expectations but still generally positive with 62% of respondents anticipating an increase in the coming months (2H 2024: 64%). Although **medium-sized businesses are cautious** over future economic prospects, 69% of them had optimistic views of sales performance, though moderated from 2H 2024 (73%). Meanwhile, **micro establishments foresee better future sales performance** (63%) this round compared to 2H 2024 (61%). This is attributable to its least share (4%) of export businesses to their total and they have been mostly shielded from the government's fiscal reforms alongside receiving regular support. Nonetheless, we foresee that the sentiment may change following recent announcements on (1) egg subsidy reduction to RM0.05 from RM0.10 per egg starting May before a full removal in Aug, and (2) the ban on eateries from using household subsidised gas cylinders, as most of the micro-sized respondents are centered around food.

Figure 4: Most MSMEs (62%) remain positive on their sales although moderated (64%) from 2H 2024.

Top 3		Bottom 3	
Information & communications	72%	Repair & installation of equipment	54%
Education	71%	Manufacture of wearing apparel	51%
Human health activities	71%	Manufacture of printing & recorded materials	42%

Among the five key sectors, the **mining & quarrying sector (70%) has the brightest expectations in future sales**, followed by construction (68%) and services (62%). Despite lower projection for global oil & gas prices and production this year, more scheduled plants shut down for maintenance purposes domestically may present opportunities and jobs to the MSMEs players in the oil and gas services and equipment sector.

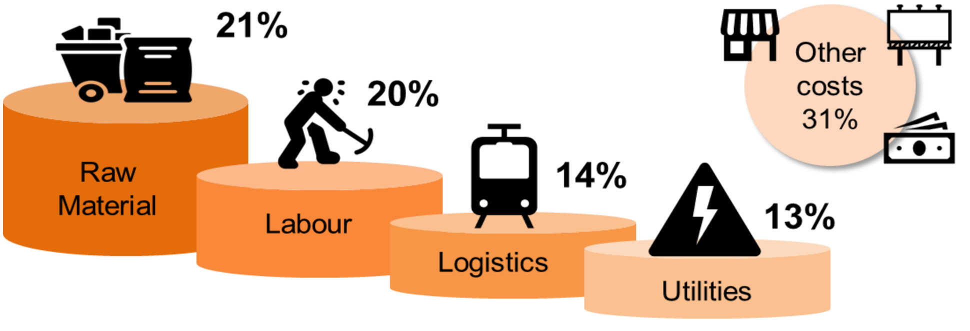
Meanwhile, **construction will continue to benefit from higher investment approval** (2024: RM378.5 bil: 2023: RM329.5 bil; avg 2015 - 2019: RM204.5 bil), ongoing & new transportation infrastructure projects, more energy projects from Tenaga Nasional Berhad with higher CAPEX allocation (RM14.3 bil annually for the period 2025 - 2027 vs RM6.9 bil annually 2022 - 2024), and ongoing data center investments (approved investment 2024: RM24.1 bil; 2023:RM16.0 bil). Breaking down the services sector, **information and communication (72%), education (71%), and human health (71%)** subsectors exhibit the **strongest optimism**.

Cost of doing business remains high due to both domestic and international affairs

Even though MSMEs still anticipate positive sales performance and steady economic activity in the near future, they are conscious of rising cost pressures. The majority of MSMEs (83%) expect their costs to increase (2H 2024: 87%), despite deeper decline in producer prices (YTD Apr 2025: -1.1% YoY; 2H 2024: -0.5% YoY). Implementation of e-invoicing, electricity tariff hike, the increase in minimum wage to RM1.7k, multi-tiered levy system on foreign workers, mandatory Employee Provident Fund (EPF) contributions (2% of monthly wages) for foreign workers effective 4Q 2025 and potential expansion of sales and service tax (SST), among others are expected to push costs higher moving forward. Nonetheless, RM1.5 bil in government guarantees and financing, including RM500 mil allocated for soft loans to assist SMEs impacted by US tariffs, and the recent government's announcement to push RON95 subsidy rationalisation to the latter part of the year with more leniency in terms of eligibility, may provide some relief in the near term.

While structural reforms are vital for long term fiscal sustainability, the delay in implementation of RON95 subsidy rationalisation to 2H 2025 is viewed as an effort to alleviate businesses and consumers from simultaneous cost pressures at this juncture. Nonetheless, **most respondents are currently neutral (47%) on the potential impact resulting from the implementation of targeted subsidies.**

Figure 5: 83% (2H 2024: 87%) of MSMEs foresee a broad-based increase in costs



Similar to 2H 2024, survey respondents have indicated that **raw materials (21%) are the main cost driver** in 1H 2025, followed closely by labour (20%), transportation and logistics (14%), and utilities (electricity, water, internet) (14%). While concerns over transportation cost may ease moving forward due to RON95 subsidy rationalisation being put on hold, those of utilities are expected to escalate with the 14.2% increase in electricity base tariff in Peninsular Malaysia starting July 2025 and the ban on usage of subsidised gas cylinders for eateries.

Sector wise, the **mining and quarrying sector continue to face the highest cost pressure** as indicated by 93% of its respondents, although moderated from the unanimous view (100%) in 2H. Their biggest cost concerns are labour and raw materials. **After mining are the ICT (92%) and education (90%) sectors**. The Ministry of Natural Resources and Environmental Sustainability has indicated that technology companies such as data centres should be subjected to premium rates for energy and water due to their heavy consumption. While the ministry has mentioned that large companies are indeed willing to pay more, smaller firms may not be agreeable.

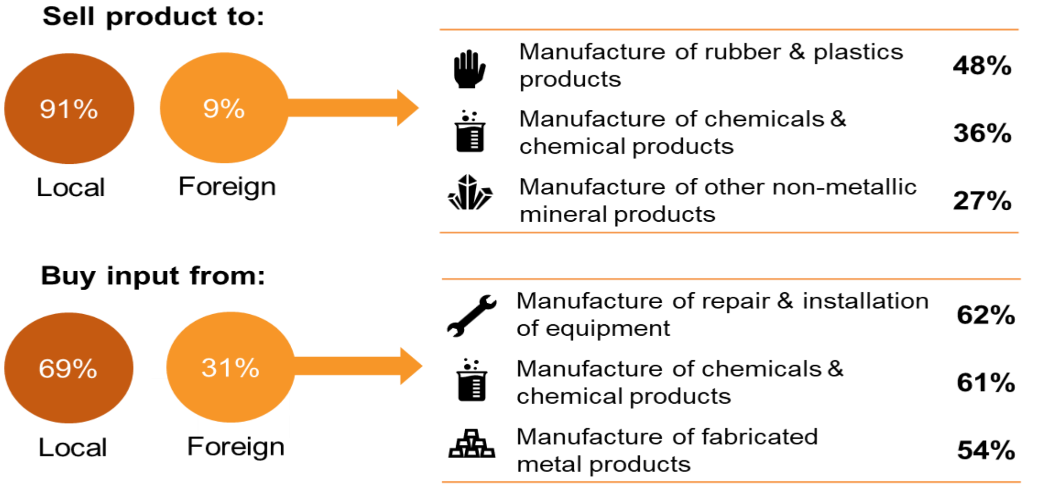
The same three states, namely Pahang (94%), Perak (90%) and Terengganu (88%) continue to dominate the higher cost expectations among MSMEs in 1H 2025, similar to our previous round's survey. Labour (30%) contributes the most to higher cost expectations in Pahang while raw materials dominate in Terengganu (20%) and Perak (19%).

MSMEs' low exposure to external markets, a blessing in disguise

Based on our survey, **only 9% of MSMEs are engaged in export activities in 1H 2025**, slightly down from 11% in 2H 2024. Likewise, the **share of MSMEs that import raw materials narrowed to 31%** (2H 2024: 33%). While this may not bode well in achieving the Twelfth Malaysia Plan (12MP)'s aim for MSMEs to contribute 25% to Malaysia's total exports by 2025, it provides temporary relief with the unfolding of Trump's trade war 2.0 as it means less impact from external shocks. Hence, the **MSMEs could emerge as the main pillars of support for the country's economic growth this year**.

Nonetheless, by sector, **rubber and plastic products may be significantly affected** as most of the respondents (48%) export their products. Likewise, manufacturing sectors such as repair and installation of equipment (62%), chemicals and chemical products (61%) and fabricated metal products (54%) are exposed to external risks as most raw materials are sourced from foreign countries.

Figure 6: MSMEs that engage in export and import activities may be more exposed to Trump's tariff risks.



Despite overall neutral stance on the potential impact resulting from increasing import tariffs and protectionism policies from other countries (48%), majority of MSMEs from several sectors such as **manufacture of fabricated metal products (61%), manufacture of furniture (56%), and manufacture of printing and recorded materials (55%) voiced concerns over the negative impact to their operations**. Furniture sector, for instance, is heavily reliant on the US market as reflected by its 44% share to total exports in 2024, followed distantly by Singapore (9%) and Saudi Arabia (8%). Nonetheless, as far as this survey is concerned, 78% of MSME respondents from the furniture sector sell most of their products locally. **While we may stand to benefit from more options of inputs/raw materials made available at cheaper prices as countries affected by Trump's trade war 2.0 seek alternative buyers, local suppliers could be hurt.**

In navigating through this rough time, **MSMEs need to diversify their export destinations as well as sources of raw materials** rather than relying heavily on a single market to mitigate potential trade shocks. Additionally, **we also recommend MSMEs to be more proactive in terms of smoothening out their cashflow or inventory management** by creating inventory buffers to maintain cost efficiency during periods of spike in prices or negotiating with suppliers for cost-sharing strategies.

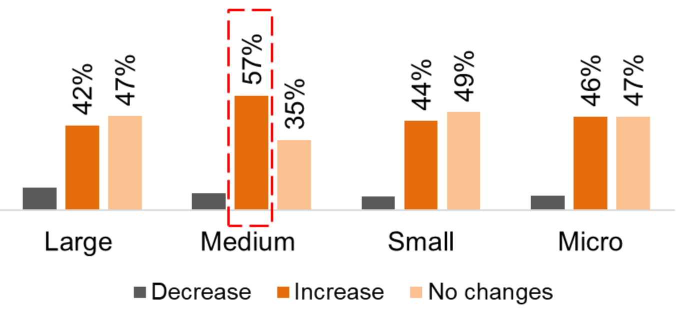
Slow hiring due to easing economic outlook and sales expectations

Most of the MSMEs (47%) plan to maintain their current workforce level (2H: 43%), contrary to the previous survey where businesses were keen to increase hiring. This is likely due to heightened uncertainties at both domestic and external front. As the cost of labour is rising , MSMEs could be incentivised to upskill and reskill their existing workforce to enhance labour productivity. Although Malaysia has a target of employee compensation (CE)'s share to hit 40% of GDP by 2025 (2024f: 33.1%; 2023: 32.4%), it is likely to be missed. Nonetheless, the government has started the ball rolling with some labour market reforms such as the progressive wage policy. At this juncture, most MSMEs are neutral (45%) on the potential impact resulting from progressive wages.

Despite the overall preference to maintain the workforce at status quo, sectors like **ICT (62%), food manufacture (56%), and professional, scientific and technical activities services (54%) still exhibit strong hiring intentions**. For ICT, there is a significant increase compared to 45% in 2H 2024, to support growing demand particularly for data centers, driven by acceleration in cloud adoption and artificial intelligence (AI) development. Based on Knight Frank's report, Malaysia currently has 54 operational data centers and 61 upcoming new ones. Overall, ICT is also supported by government digitalisation initiatives such as the Madani Economy and Jalinan Digital Negara (JENDELA), with rising demand for cybersecurity and e-commerce.

By business size, **medium enterprises (57%) showed the strongest hiring intentions** for the upcoming period, followed by micro (46%), small (44%), and large (42%) businesses. Besides that, **employers continue to prefer hiring permanent staff (66%) over temporary roles, a trend that has been in place since 1H 2024**. This may reflect **greater confidence in the long-term prospect of the economy**.

Figure 7: 47% of MSMEs plan to maintain current workforce while 46% intends to hire more.



E-invoicing creates positive impression as implementation kicks in

MSMEs continued to indicate that **e-commerce and cashless transactions** (65% of respondents), as well as **automation and AI** (53%) have a **positive impact on their business performance in 1H 2025**. In addition, **most of the MSMEs (45%) now view e-invoicing as beneficial to their businesses, contrary to our previous survey in 2H 2024 where the majority were indifferent** about this initiative. Nonetheless, the positivity came mainly from smaller sized businesses i.e. micro (50%), small (42%) vs medium (36%) and large (36%), probably due to the low cost involved given the less complex nature of their businesses while still getting to enjoy general benefits such as faster payment cycles, reduced administrative burden and increased accuracy. The government has just recently revised e-invoicing deadlines for businesses earning below RM5 mil and raised the e-invoicing exemption threshold to RM500k, up from the previous limit of RM150k.

Table 1: Timeline of Malaysia e-invoice implementation.

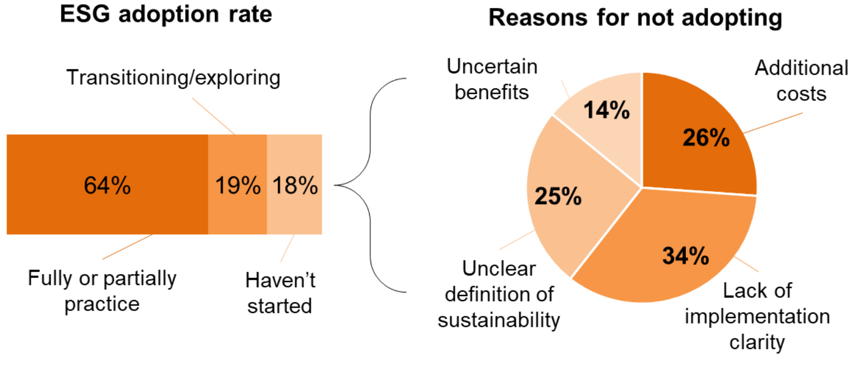
Implementation date	Annual turnover/ revenue	
	Original	Revised
1 July 2025	>RM500k and up to RM25 mil	>RM5 mil and up to RM25 mil
1 January 2026	All businesses except <RM150k	>RM1 mil and up to RM5 mil
1 July 2026	-	All businesses except <RM500k

Gradual increase in ESG adoption

As Environmental, Social, and Governance's (ESG) gains centre stage, more MSMEs continue to move towards fully or partially implementing ESG practices (1H 2025: 64% vs 2H 2024: 62%) while 19% (2H 2024: 18%) are in the transitioning or exploring process. **Those who have embraced ESG acknowledged that it helps them save costs** (1H 2025: 51% vs 2H 2024: 46%). Other key reasons cited for the adoption of ESG are new business opportunities (19%), branding (18%) and mandatory requirements (12%).

There has been **a notable increase in embracing ESG among the large sized MSMEs** (1H 2025: 84% vs 2H 2024: 63%), probably pushed by evolving regulatory requirements which often starts with large companies such as Bursa Malaysia's mandatory disclosure of sustainability goals, performance metrics and climate-related assessments in annual reports of companies with a market capitalisation exceeding RM2 bil since Jan 2025. Top 3 subsectors which have claimed that they have fully implemented ESG practices were from the manufacture of other non-metallic mineral products (55%), manufacture of furniture (41%) and manufacture of wearing apparel (30%).

Figure 8: 64% of businesses (2H 2024: 62%) are embracing ESG practices while those that have not, are mostly (34%) unsure of where to start.



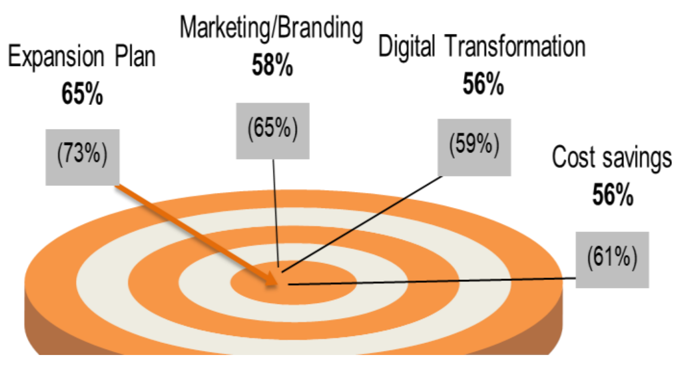
Meanwhile, 18% of the MSMEs (2H 2024: 19%) have yet to start anything on ESG and relayed that they lack the clarity on how to start and where to go for support (34%) as the main reason. This is particularly true for micro-sized businesses, likely due to insufficient knowledge and expertise in ESG compliance compared to larger companies with access to consultants. Other key reasons for not adopting ESG practices include additional costs (26%), unclear definition of sustainability (25%), and uncertain benefits of sustainability (14%). However, only a small percentage (4%) of those who cited costs as a reason that requires financing assistance related to sustainability practices from SME Bank.

Expansion remains as businesses' top priority albeit moderating

Business expansion remains as the top focus for MSMEs (1H 2025: 65% vs 2H 2024: 73%) across all business sizes, which jive with the **strong financing appetite for expansion**. However, the moderation from the last round of survey reflects more cautious sentiment at present, amid softer sales and economic expectations. **Top sector showing interest to expand their businesses include professional, scientific and technical activities (87%), agriculture (79%), and manufacture of chemical and its products (75%).** Expansion in the agriculture sector is in line with the High-Growth, High-Value (HGHV) sector strategy outlined in 12MP to enhance food security and boost agricultural productivity.

Other areas that MSMEs plan to focus on is marketing/branding (58%), digital transformation (57%), and cost-saving measures (56%). Lower focus this time around on marketing/branding and digital transformation suggests that it may have already become part of their routine operations. Meanwhile, sectors that are most keen to focus on cost-savings measures are manufacture of other non-metallic mineral products (73%), professional, scientific and technical activities (68%) and warehousing and support activities (68%). Most MSMEs in these sectors expect costs to increase over the next few months.

Figure 9: Expansion remains as top priority (65%) albeit moderating (2H 2024: 73%)



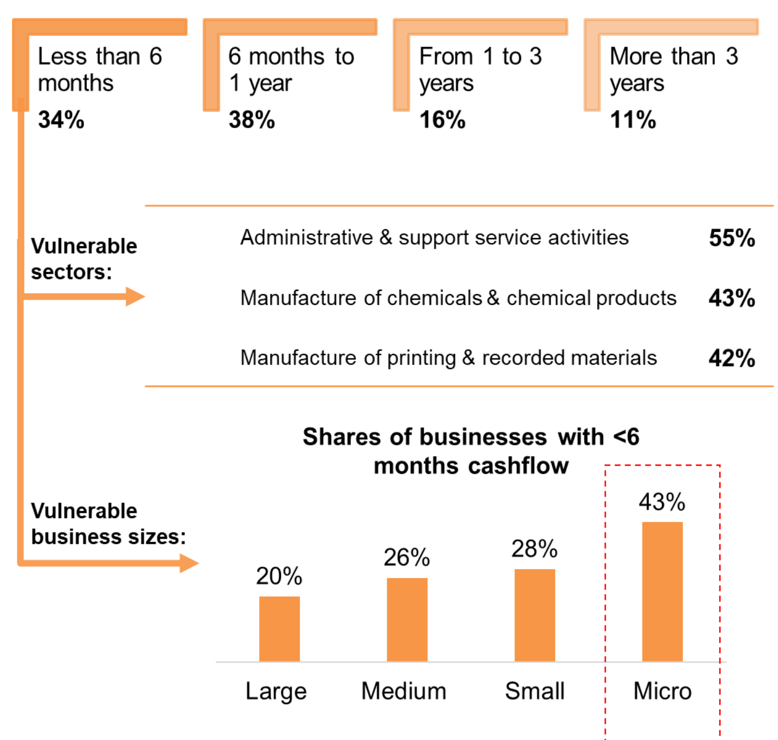
MSMEs are deemed to be financially sustainable but more challenges ahead

In 1H 2025, 66% of MSMEs (2H: 68%) reported having cash reserves that could last more than 6 months. By size, micro businesses were the most vulnerable (43%) to low cash reserves (<6 months), followed distantly by small (28%), medium (26%) and large (20%). Upcoming subsidy rationalisation and regulatory compliance such as e-invoicing and mandatory EPF contribution to foreign workers are expected to strain cash buffers even more, especially for companies that are tight on cashflow.

Sectors with the lowest cash reserves are administrative and support services (55%), manufacture of chemicals (43%), and manufacture of printing and recorded material (42%). On the other hand, the top 3 sectors with the strongest buffer (>6 months) are manufacture of repair and installation of equipment (88%), warehousing and support activities (79%) and sales and repair of vehicles (74%).

Financing remains the top assistance required by MSMEs where 43% have indicated the need for working capital and 38% for business expansion. Meanwhile, only a handful of survey respondents require financing for sustainability-related practices (3%) and digitalisation (3%).

Figure 10: 34% of MSMEs (2H 2024: 32%) only have short-term cash



Despite the slightly lower index, we remain confident that MSMEs are resilient as they continue to demonstrate stronger performance and growth potential, showcasing their vital role as the country's key pillars of growth and stability, especially for this challenging year of 2025. Nevertheless, regular assessment of their business operations and strategies to adapt to new trends and business dynamics are essential to fulfil the changing needs of consumers and market conditions. Below are funding programs provided by SME Bank as well as trainings by our subsidiary, CEDAR.

Table 2: SME Bank financing programs

1. Agro Food (AF)
2. All Economic Sectors Facility (AES)
3. Business Accelerator Programme Under Rancangan Malaysia Ke-12 (BAP RMK-12)
4. Contract Financing (CF)
5. Dana Kemampanan PMKS Bumiputera (DKPB 2
6. Disaster Relief Facility (DRF) 2022
7. HalalBiz Financing Program
8. High Tech & Green Facility (HTG)
9. Jaguh Serantau (JS)
10. Low Carbon Transition Facility (LCTF)
11. Pembiayaan Ekosistem Payung
12. PENJANA Tourism Financing (PTF)
13. Program Dana Kelestarian Alam (DKA)
14. Rolling SRF (RSRF)
15. Rolling TRRF (RTRRF)
16. SME Automation & Digitalisation Facility (ADF)
17. SME Technology Transformation Fund (STTF)
18. Social Enterprise Financing Scheme (SEFS)
19. Tabung Khas Pelancongan (TKP)
20. Vanigham Financing Scheme (VFS)

Table 3: CEDAR entrepreneur development programmes

1. Business Export Program – Bootcamp
2. Dana Kemampanan Ushawan Bumiputera
3. ISHRAF 4.0
4. Jelajah Keusahawanan Bersasar
5. Maju Usahawan Madani 2025
6. Mandatory Training Program
7. Program Pembangunan Kapasiti Produk Halal 2025
8. SMEs Enrichment Workshop (SEW)
9. Upward Growth Migration

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