

**MONTHLY ECONOMIC REVIEW | April 2016****2016 Fiscal Target Achievable as Oil Prices Hold Its Ground Above USD40**

- *Fiscal's outlook improves as oil prices seem to hold firmly above USD40.*
- *Fed remains neutral on rate hike in most recent FOMC meeting.*
- *IMDB's default deemed to have little impact on Malaysia's sovereign debt rating.*
- *Headline inflation moderated to 2.6%yoy while leading indicator slumped further for 6 consecutive months.*

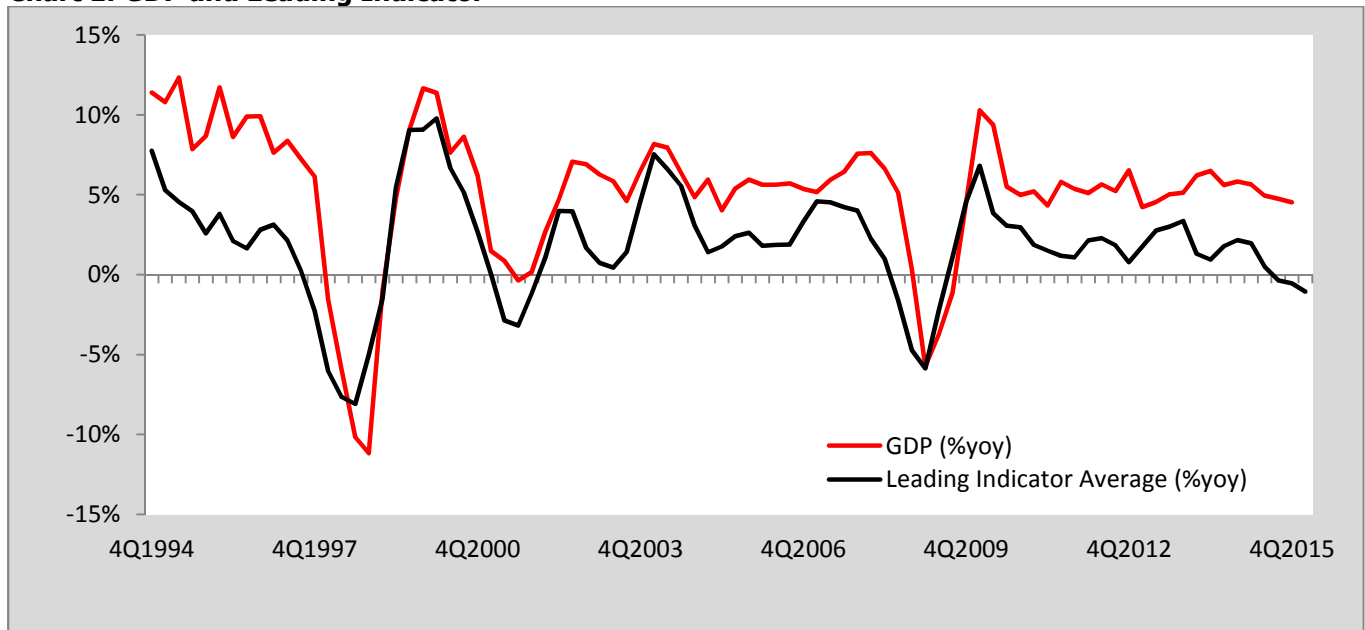
**Malaysia's Fiscal Outlook Improves as Oil Prices holds its ground above USD40.** Brent reached as high as USD48.5 per barrel on intraday trading last week. Year-to-date, oil price averaged USD37.4 and since 1<sup>st</sup> April, oil price averaged higher at USD43.4 per barrel. This was higher than optimistic scenario projected in the recalibrated Budget 2016 of USD35 per barrel, giving rise to better probability for oil price to average higher than projected for the year. We view this as a positive development of which the government is likely to meet its fiscal target this year despite moderating overall economic growth projection.

**Fed reiterated strengthening domestic economy but hints neutral stance on future rate hike.** Fed has explicitly stated that global economic and financial developments continue to pose risks for the US economy. Fed will still closely monitor indicators for the two matters in determining its interest rate decision. Although financial market has begun to stabilise recently, the global economic direction is still uncertain.

**Thus we are maintaining our year-end fed fund rate at 0.75%, but revising the timing of rate hike to September.** Despite recent positive news on US domestic economy, Fed was neutral on rate hike. We perceive the Fed is still concerned with the global economic and financial market development, as the direction is still uncertain and could pose a downside risks to US economy. As such, we are maintaining our earlier expectation that the Fed is going to increase the interest rate once this year to end 2016 at 0.75% while revising the timing of rate hike forecast from June to September 2016.

**IPI expanded by 3.9%, higher than expected.** The industrial output was solid in February, expanding by 3.9% year-on-year supported by stronger manufacturing and mining output. Both sectors grew 4.5%yoy and 1.1%yoy respectively. We expected that mining sector would contract in February due to plunging commodity prices but it continued to grow during the month, proving its resiliency. However, the expansion in electricity output is almost in line with our forecast of 11.0%. On a seasonally adjusted basis, IPI expanded by 0.89%mom, almost twice the growth recorded from the previous month. This has been the second consecutive months that all of the three sub-indices registered positive growth.


**Chart 1: GDP and Leading Indicator**



Source: DoS, CEIC, MIDF Research

**The 3-month average of leading indicator has been in negative for six consecutive months since September 2015.** The leading indicator has performed well in predicting the economy two quarters ahead. Malaysia's official leading indicator entered into negative territory for the first time in the third quarter of last year and had dive deeper into the red in 4Q15. The past two quarters have been in negative while the latest reading in February registered -1.2% year-on-year decline. Thus, we stand by our forecast of moderating growth for the first half of 2016.

**Headline inflation came in at much lower than consensus though in line with our forecast.** Inflation in March came in at 2.6%, slightly lower than our estimate at 2.7%. However, the number is much lower than the consensus at 3.4%. We have expected the lower number particularly due to the difference in pump price, where RON95 reached an all-time low at RM1.60/litre, compared to the same period last year at RM1.95/litre. Core inflation moderated a little from 3.56% in February to 3.55% in March. Inflation ex-fuel, where we excluded the pump price from CPI basket, rose higher to 4.55% in March, higher than February's number at 4.36%.

**1MDB default hit Ringgit initially but has little impact to fiscal condition.** Ringgit was weaker yesterday arguably in reaction to the default news but rebounded same day. We opine that the default has little impact to the fiscal condition hence a sovereign debt rating downgrade is unlikely. 

<b>(YoY%) unless stated otherwise</b>	<b>2014</b>	<b>2015</b>	<b>2016f</b>	<b>1Q16</b>	<b>2Q16f</b>	<b>3Q16f</b>	<b>4Q16</b>
Real GDP	6.0	5.0	4.4	4.2	4.2	4.7	4.7
Private consumption expenditure	7.1	5.5	4.9	4.3	5.4	5.7	4.2
Government expenditure	4.4	4.7	2.7	1.7	1.7	2.6	4.9
Gross fixed capital formation	4.8	3.4	4.2	1.4	9.0	4.7	1.7
Exports of goods and services	5.1	0.6	2.2	2.0	5.8	1.0	0.0
Imports of goods and services	4.2	1.2	2.0	2.3	6.4	0.5	-1.3
Net exports	12.8	-3.3	3.8	-0.3	1.2	4.4	9.8
Nominal GDP	8.6	4.5	4.1	4.7	4.5	3.8	3.5
Exports of Goods (f.o.b)	6.3	1.9	3.9	2.2	5.9	6.2	1.6
Imports of Goods (c.i.f)	5.3	0.4	3.2	2.3	5.3	3.7	1.8
Trade Balance – RMb	82.5	94.3	102.9	21.7	22.7	27.9	30.6
Consumer price index	3.2	2.2	2.6	3.5	2.0	2.5	2.9
Current account – RMb	47.3	34.0	25.0	-	-	-	
Current account - % of GNI	4.8	2.8	2.5	-	-	-	
Fiscal balance - % of GDP	-3.5	-3.2	-3.1	-	-	-	
Federal government debt - % of GDP	52.7	54.3	53.8	-	-	-	
	<b>2014</b>	<b>2015</b>	<b>2016f</b>	<b>1Q16</b>	<b>2Q16f</b>	<b>3Q16f</b>	<b>4Q16</b>
Brent Crude Oil (Avg)	99.4	53.6	40.0	-	-	-	
Crude Palm Oil (Avg)	2,415	2,168	2,450	-	-	-	
USD/MYR (Avg)	3.273	3.907	4.000	-	-	-	
EUR/MYR (Avg)	4.347	4.336	4.400	-	-	-	
JPY/MYR (Avg)	3.096	3.228	3.350	-	-	-	
SGD/MYR (Avg)	2.583	2.840	2.800	-	-	-	
Brent Crude Oil (End of)	57.3	37.3	40.0	39.0	40.0	40.0	40.0
Crude Palm Oil (End of)	2,297	2,200	2,250	2,600	2,800	2,250	2,250
USD/MYR (End of)	3.497	4.294	3.850	3.900	4.000	3.950	3.850
EUR/MYR (End of)	4.251	4.691	4.350	4.446	4.500	4.450	4.300
JPY/MYR (End of)	2.922	3.572	3.150	3.464	3.300	3.200	3.150
SGD/MYR (End of)	2.647	3.040	2.850	2.895	2.950	2.850	2.850
Yield on generic 10-year MGS (%)	4.15	4.19	3.65	3.77	3.85	3.70	3.65
3-month KLIBOR (%)	3.86	3.84	3.40	3.71	3.65	3.40	3.40
Overnight policy rate (%)	3.25	3.25	3.00	3.25	3.25	3.00	3.00

## March Key Economic Events

**1 April 2016: China Rating Outlook Cut to Negative From Stable by S&P.** Standard & Poor's has cut the outlook for China's credit rating to negative from stable, saying the nation's economic rebalancing is likely to proceed more slowly than the ratings firm had expected. The nation's credit rating is AA- with a negative outlook, S&P said in a statement, which also affirmed the long-term and A-1+ short-term sovereign credit ratings. "We revised the outlook to reflect our expectation that the economic and financial risks to the Chinese government's creditworthiness are gradually increasing," S&P said in the statement.

**16 April 2016: China GDP growth slips to 6.7% as stimulus eases slowdown.** High quality global journalism requires investment. China's economy grew at an annual rate of 6.7 per cent in the first quarter of 2016, down slightly from the end of last year but comfortably within the government's targeted range, as housing and infrastructure cushioned a slowdown from financial services. The latest gross domestic product growth figure is the lowest since the depths of the financial crisis in the first quarter of 2009.

**28 April 2016: 1MDB default on bond payment over dispute with IPIC.** 1Malaysia Development Bhd. defaulted on a \$1.75 billion bond this week. It missed a \$50 million interest payment amid a dispute with Abu Dhabi's sovereign wealth fund over who is required to make the payment. Abu Dhabi's International Petroleum Investment Co. guaranteed two separate dollar-denominated bonds for 1MDB in 2012 in deals arranged by Goldman Sachs Group Inc.

**28 April 2016: Dato' Muhammad Ibrahim Succeeds Zeti as New BNM governor.** Datuk Muhammad Ibrahim will succeed Tan Seri Zeti as the eighth Central Bank Governor with the appointment term of 5 years starting from 1st of May. The financial markets gave a thumbs-up to the news, driving up the ringgit and drawing widespread praise from bankers and analysts.

**6 April 2016: Tame inflation lets Indian central bank cut interest rate to 6.5%.** The Reserve Bank of India cut its policy interest rate by a quarter point to 6.5% on Tuesday and took other steps to increase liquidity in the financial system. The central bank's move came at a time when headline inflation has been easing and the government is making progress on fiscal consolidation. It has adopted a target of reducing its fiscal deficit to 3.5% of gross domestic product for fiscal 2016

**27 April 2016: Fed holds on rates, warns economy has slowed.** Amid a moribund economy and reduced levels of consumer spending, the Fed on Wednesday again opted not to raise interest rates. The statement highlighted the many conflicting signs in the U.S. economy – consistent job growth and an improving housing market against slowdowns in business investment and exports. Indeed, the Atlanta Fed has estimated that economic growth slowed to just 0.6 percent in the first quarter of 2016, a condition reflected in the Fed's lukewarm assessment of conditions.

**28 April 2016: Oil producers fail to agree on output freeze.** Saudi Arabia, Russia and other major oil producing nations failed to agree on a crude output freeze Sunday, as Iran's absence cast shadows over the talks. More than 10 OPEC and non-OPEC members took part in the meeting, with the aim of keeping production at January levels until October. But the absence of Iran apparently irked the Saudis and other participants. They hope to reach a conclusion at the next OPEC meeting to be held June 2.

**29 April 2016: Sluggish Global Demand Dragging Down US Economic Growth.** US GDP grew slowest in five quarters by 0.54%qoq in 1Q16, dragged down by the sluggish investment activity and global trade activity. Non-residential investment had its worst contraction since Global Financial Crisis at -5.98%qoq, marking the first time since 2009 that the year-on-year growth went into negative territory at -0.40%yoy. Despite the pessimistic data, it should be noted that US GDP had a tendency to be revised upwards

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