midf RESEARCH

30 August 2019

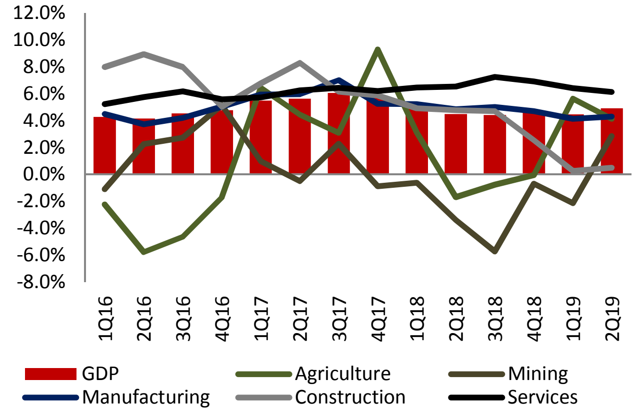
# MONTHLY ECONOMIC REVIEW | August 2019

# Malaysia's Economy Remains on Expansionary Path as Signalled by Leading Indicators

- *2Q19 GDP highest in 5-quarter. Malaysia's GDP growth expanded 4.9%yoy in 2Q19, marginally above market expectations and our forecast of 4.7%yoy and 4.8%yoy respectively. The strong pick-up in the economy is generally driven by continuous strong private consumption and recovery in commodity-based sectors. From expenditure side, private consumption and net exports contributed by 4.4% and 1.4% respectively. From supply side, services, mining and agriculture sectors contributed by 3.6%, 0.2% and 0.3% respectively during the quarter.*
- *Malaysia's economy remains in upward track. According to the Business Tendency Survey, overall business performance is set to improve at 3.1% in 3Q19. Commodity based sectors such as agriculture and mining are predicted to recover in 3Q19. In addition, manufacturing sector is also expected to recover despite external headwinds. Besides that, leading index remains in negative sign but is rebounding gradually. The index indirectly hints the economy to continue expanding at solid pace in 3Q19 and 4Q19. Effects of lower OPR are predicted to appear in 2H19 with inflationary pressure stays low and job market at full-employment condition. Henceforth, we expect GDP growth in 3Q19 to record above 5%.*
- *Trade surplus returns to above RM 10b mark despite falling exports. Trade surplus increased to RM 10.3b in June-19 from the first time in this year at below RM 10b in May-19 as imports fell harder than exports. Both exports and imports growth plunged to negative territory of -3.1%yoy and -9.2%yoy respectively after maintaining positive growth in the previous two months. Such weak external trade performances could be the result of multiple headwinds took place during the month. June-19 was the first full month of US tariff on Chinese imports after the truce and US ban on Huawei, both deteriorate global sentiment.*

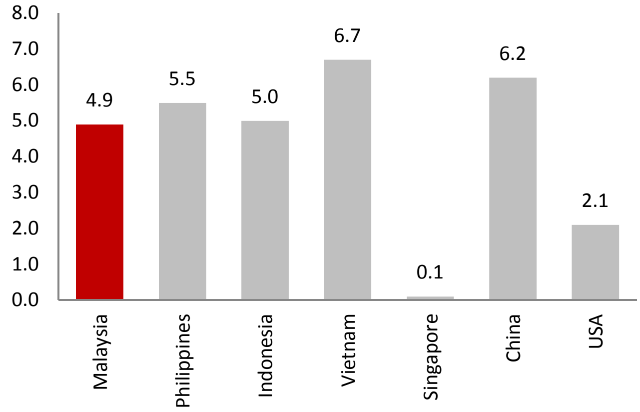
**2Q19 GDP highest in 5-quarter.** Malaysia's GDP growth expanded 4.9%yoy in 2Q19, marginally above market expectations and our forecast of 4.7%yoy and 4.8%yoy respectively. The strong pick-up in the economy is generally driven by continuous strong private consumption and recovery in commodity-based sectors. From expenditure side, private consumption and net exports contributed by 4.4% and 1.4% respectively. From supply side, services, mining and agriculture sectors contributed by 3.6%, 0.2% and 0.3% respectively during the quarter. External front remains weak due to global trade wars and decline in business optimism. On the other hand, domestic demand stays solid underpin by lower interest rate, stable labor market and low inflationary pressure.

**Chart 1: GDP by Supply-Side (YoY%)**




Source: CEIC, MIDFR

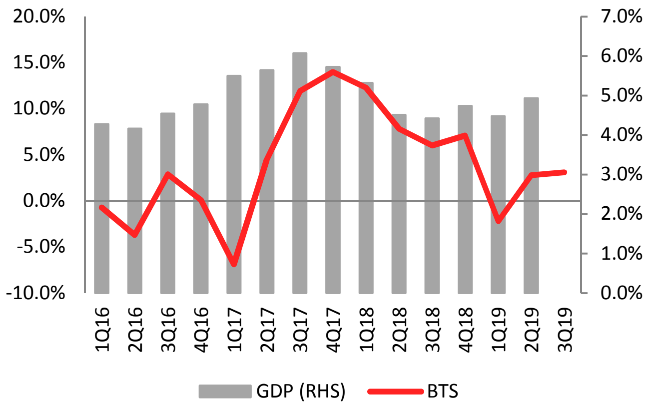
**Chart 2: GDP by Country 2Q19 (YoY%)**




Source: CEIC, MIDFR

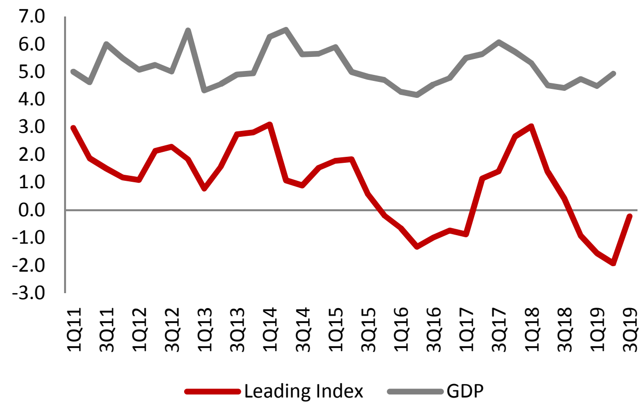
**Malaysia's economy remains in upward track.** According to the Business Tendency Survey, overall business performance is set to improve at 3.1% in 3Q19. Commodity based sectors such as agriculture and mining are predicted to recover in 3Q19. In addition, manufacturing sector is also expected to recover despite external headwinds. Besides that, leading index remains in negative sign but is rebounding gradually. The index indirectly hints the economy to continue expanding at solid pace in 3Q19 and 4Q19. Effects of lower OPR are predicted to appear in 2H19 with inflationary pressure stays low and job market at full-employment condition. Henceforth, we expect GDP growth in 3Q19 to record above 5%. However, trade war remains as downside risks to Malaysian economy.

**Chart 3: BTS (%) vs GDP (YoY%)**




Source: CEIC, MIDFR

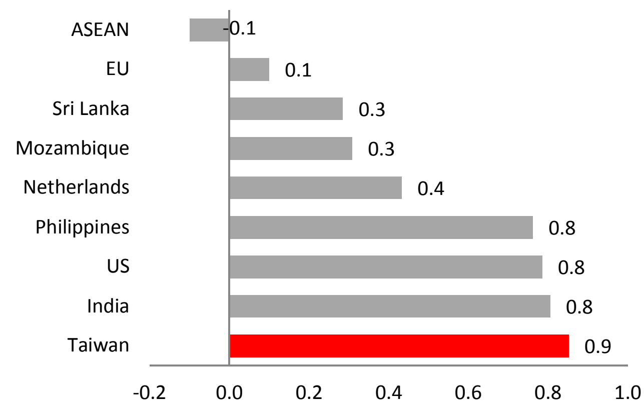
**Chart 4: Leading Index vs GDP (YoY%)**




Source: CEIC, MIDFR

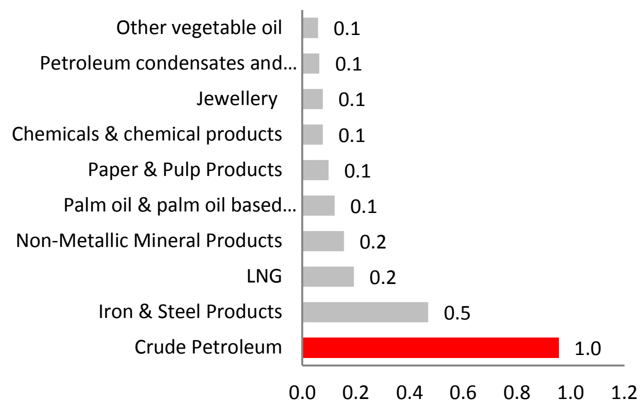
**Trade surplus returns to above RM 10b mark despite falling exports.** Trade surplus increased to RM 10.3b in June-19 from the first time in this year at below RM 10b in May-19 as imports fell harder than exports. Both exports and imports growth plunged to negative territory of -3.1%yoy and -9.2%yoy respectively after maintaining positive growth in the previous two months. Such weak external trade performances could be the result of multiple headwinds took place during the month. June-19 was the first full month of US tariff on Chinese imports after the truce and US ban on Huawei, both deteriorate global sentiment. Sector wise, manufacturing and agriculture exports contracted by -5%yoy and -0.8%yoy respectively. In contrast, mining exports rebounded sharply to a double digit positive growth of 15.4%yoy (May-19: -10.9%yoy).

**Chart 5: % Contribution by Destination to Exports Growth**




Source: CEIC, MIDFR

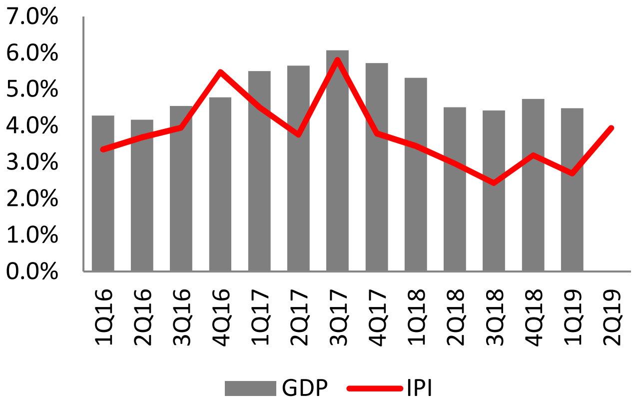
**Chart 6: % Contribution by Product to Exports Growth**




Source: CEIC, MIDFR

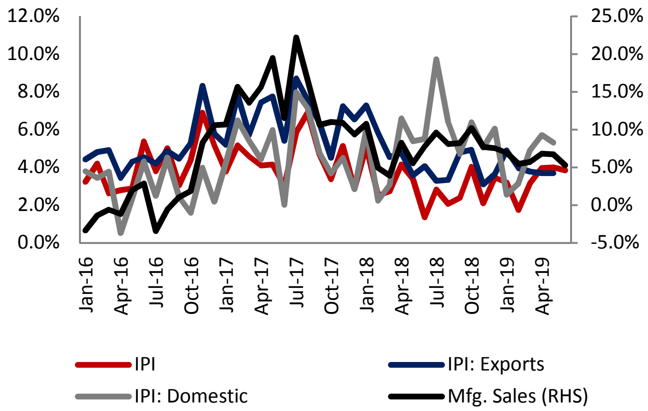
**IPI growth moderated slightly**. Malaysia's IPI growth inched down to a three-month low of 3.9%yoy in June-19 after maintaining at 4%yoy for the past two months. Manufacturing and electricity output growth moderated sharply to 3.8%yoy and 1.7%yoy (May-19: 4.2%yoy and 5.7%yoy) respectively. However, mining output increased significantly by 4.6%yoy, fastest growth since Dec-16 and partly offset the overall impact from slower manufacturing activities. For the 2Q19, IPI growth averaged at 3.9%yoy, higher than 2.7%yoy in 1Q19 hence signalled better performance in economic growth for 2Q19. Moving forward, we foresee IPI performance to continue expanding but at a moderating pace in 2H19 as trade war factor remains as a major downside risk to global trade activities and manufacturing production in particular which has the highest weightage in the overall IPI index. Nevertheless, effects of OPR cut, low inflationary pressure, positive progression in construction activities and stable domestic demand would provide support to the industrial production performance.

**Chart 7: IPI vs GDP (YoY%)**




Source: CEIC, MIDFR

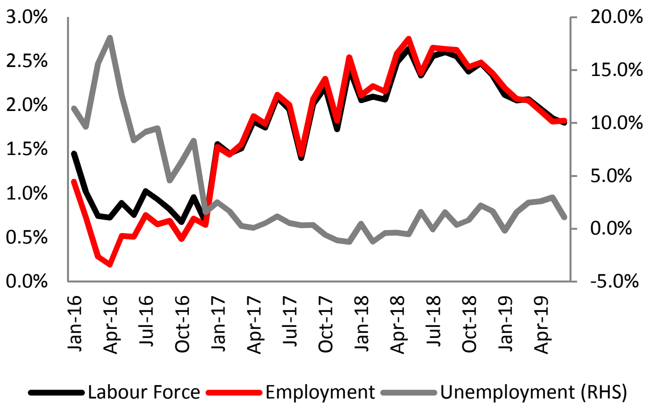
**Chart 8: IPI vs Mfg. Sales (YoY%)**




Source: CEIC, MIDFR

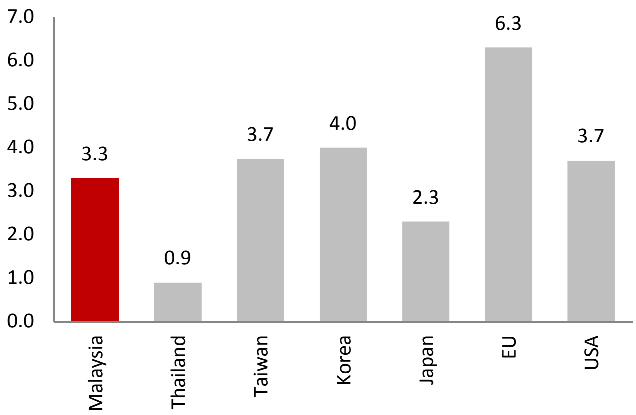
**Labour market remains stable**. Labour force grew by 1.8%yoy in June-19, the weakest gain since Nov-17 while employment growth maintained at 1.8%yoy, unchanged from previous month with monthly jobs added in the economy registered lower at 12.1k. On the other hand, unemployment growth moderated to 1.1%yoy, the lowest in five months reversing the upward trend since Feb-19 and still reflecting full-employment condition. Stable labour market is crucial for Malaysian economy as it provides solid support to the domestic demand.

**Chart 9: Labour Market Key Indicators (YoY%)**




Source: CEIC, MIDFR

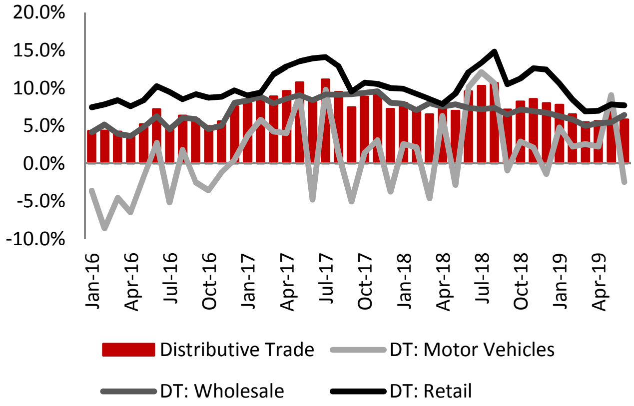
**Chart 10: Global Unemployment Rates (%) in June-19**




Source: CEIC, MIDFR

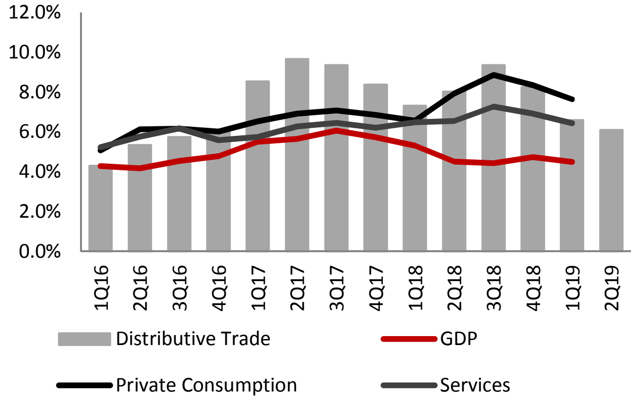
**Distributive trade hit new record high.** Distributive trade hit new record high at RM 112.3b in June-19 despite contraction in motor vehicles sales and tepid moderation in retail sales growth. Motor vehicles sales declined by -2.5%yoy as festive season promotional campaigns ended. Meanwhile, retail trade continued expanding but at a slightly lower pace of 7.7%yoy (May-19: 7.8%yoy). The moderation could also be attributed to the higher base effect resulted from June-August tax holiday period last year which caused consumers to ramp up their spending especially on big-ticket items. Motor vehicles and retail sales growth were the highest at double digit growth during the tax holiday period compared to rest of the months of 2018. In contrast, wholesale trade which constitutes about 48% of total distributive trade advanced by 6.4%yoy in June-19, the fastest pace so far this year. Looking ahead, we foresee domestic demand to continue increasing in upcoming months buoyed by the OPR cut, stable job market and low inflationary pressure.

**Chart 11: Distributive Trade, DT (YoY%)**




Source: CEIC; MIDFR

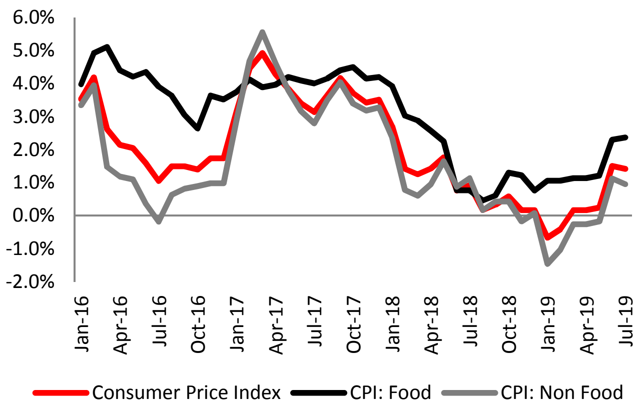
**Chart 12: DT vs Private Consumption vs Services (YoY%)**




Source: CEIC; MIDFR

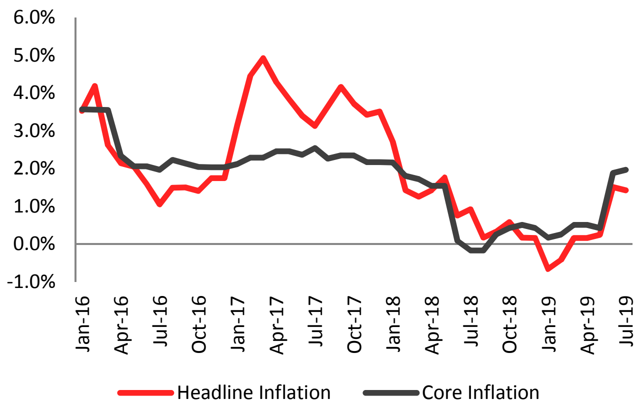
**Slim moderation in inflation**. Headline inflation inched down to 1.4%yoy in July-19 from a 13-month high of 1.5%yoy in the previous month. Food & non-alcoholic beverages prices continued to increase at faster pace of 2.4%yoy (June-19: 2.3%yoy). In addition, transport prices continued to drop but at a slower pace of -1.9%yoy (June-19: -2.1%yoy). However, better performances in both food and transport prices were inadequate to offset moderation in housing & utilities prices at 1.9%yoy (June-19: 2.3%yoy). In contrast to headline figure, core inflation edged up to 2%yoy, the fastest pace since Jan-18. Looking ahead, inflation is likely to remain high in upcoming month mainly due to the lower base effect resulting from the tax holiday period last year. Nevertheless, RON95 price cap at RM2.08 will continue to downwardly pressure transport inflation.

**Chart 13: CPI: Headline vs Food & Non-food (YoY%)**




Source: CEIC, MIDFR

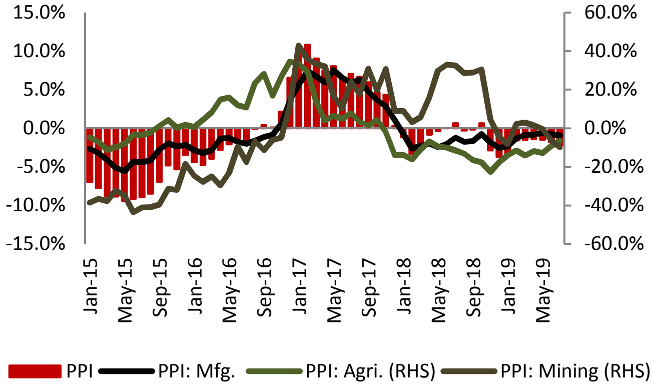
**Chart 14: Headline vs Core CPI (YoY%)**




Source: CEIC, MIDFR

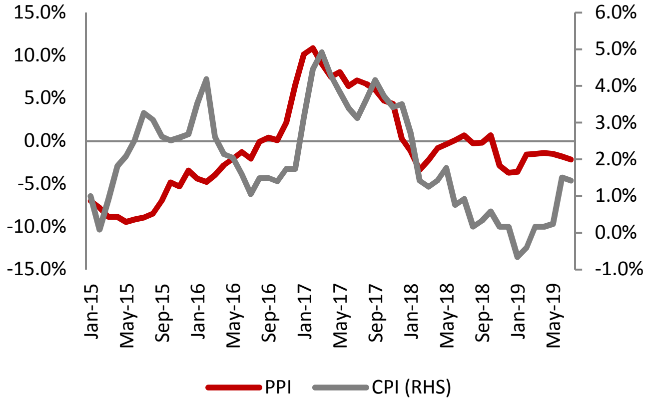
**PPI contracted for ninth straight months.** Malaysia's producer cost remains deflationary for the ninth consecutive months as PPI shrank further by -2.2%yoy in July-19. This was mainly due to higher decrease in input prices of mining and manufacturing sectors. Factory input price have contracted for 19-consecutive months. Manufacturing sector still held the largest share at 81.6% in determining the producers' inflation. Meanwhile, PPI for agriculture gradually recovered to lower negative rates compared to previous months. We expect the PPI to remain low given that retail fuel prices of RON95 and Diesel are capped at lower levels than 2018's average prices.

**Chart 15: PPI Performance by Sector (YoY%)**




Source: CEIC, MIDFR

**Chart 16: PPI vs CPI (YoY%)**




Source: CEIC, MIDFR

**Table 1: Macroeconomic Data Updates**

| (YoY%) Unless Stated Otherwise | 2016 | 2017 | 2018 | 2019f |
|---|---|---|---|---|
| Real GDP | 4.4 | 5.7 | 4.7 | 4.9 |
| Public Consumption | 1.6 | 5.5 | 3.2 | 3.5 |
| Private Consumption | 5.8 | 6.8 | 7.9 | 7.2 |
| Gross Fixed Capital Formation | 2.5 | 6.1 | 1.3 | 1.7 |
| Public Investment | (0.8) | 0.5 | (5.0) | (4.0) |
| Private Investment | 4.4 | 9.1 | 4.4 | 4.2 |
| Exports of goods & services | 1.3 | 8.8 | 2.2 | 0.8 |
| Imports of goods & services | 1.5 | 10.3 | 1.3 | 0.7 |
| Net Exports (RMb) | 88.9 | 85.5 | 95.3 | 97.5 |
| Agriculture etc. | (3.6) | 5.8 | 0.2 | 1.5 |
| Mining & Quarrying | 2.3 | 0.5 | (2.6) | 2.1 |
| Manufacturing | 4.4 | 6.1 | 5.0 | 3.8 |
| Construction | 7.5 | 6.8 | 4.3 | 4.5 |
| Services | 5.7 | 6.2 | 6.8 | 6.5 |
| Exports of Goods (f.o.b) | 1.4 | 19.3 | 7.3 | 3.6 |
| Imports of Goods (c.i.f) | 2.0 | 20.2 | 5.6 | 3.0 |
| Trade Balance - RMb | 88.1 | 98.5 | 119.8 | 126.3 |
| Consumer Price Index | 2.1 | 3.8 | 1.0 | 0.6 |
| **End of Unless States Otherwise** | **2016** | **2017** | **2018** | **2019f** |
| Brent Crude Oil (Avg) | 46.0 | 55.7 | 71.6 | 63.0 |
| Crude Palm Oil (Avg) | 2642.0 | 2659.0 | 2293.0 | 2090.0 |
| USD/MYR (Avg) | 4.14 | 4.30 | 4.00 | 4.15 |
| USD/MYR | 4.46 | 4.08 | 4.10 | 4.15 |
| Overnight Policy Rate (%) | 3.00 | 3.00 | 3.25 | 3.00 |

Source: MIDFR

## August 2019 Key Economic Events

**1 August: Trump announce 10% tariffs on another USD 300b of Chinese goods starting Sep. 1.** President Donald Trump said Thursday that the U.S. is putting 10% tariffs on another $300 billion worth of Chinese goods, effective Sept. 1. "Trade talks are continuing, and during the talks the U.S. will start, on September 1st, putting a small additional Tariff of 10% on the remaining 300 Billion Dollars of goods and products coming from China into our Country...We look forward to continuing our positive dialogue with China on a comprehensive Trade Deal, and feel that the future between our two countries will be a very bright one!" Trump said in a tweet on Thursday.

**2 August: Japan to strike South Korea off trusted export list as rift deepens.** Japan will remove South Korea from its list of trusted trade partners, deepening a bitter row between the two countries. The decision to strike South Korea off its so-called "white list" puts fresh trading restrictions on the country. South Korean President Moon Jae-in on Friday condemned Tokyo's "selfish" act and threatened possible retaliation. The trade spat, which includes curbs on tech supplies, has sparked fears over risks to the global electronics sector. The escalating dispute has been fuelled by diplomatic tensions over compensation for wartime labour.

**9 August: U.S. Holds Off on Huawei Licenses as China Halts Crop-Buying.** The White House is holding off on a decision about licenses for U.S. companies to restart business with Huawei Technologies Co. after Beijing said it was halting purchases of U.S. farming goods, according to people familiar with the matter. Commerce Secretary Wilbur Ross, whose department has vetted the applications to resume sales, said last week he's received 50 requests and that a decision on them was pending.

**13 August: Singapore slashes annual GDP forecast to 0-1% amid 'strong headwinds'.** With "strong headwinds" ranging from an escalating trade war to a downturn in the global electronics cycle likely to persist for the rest of 2019, Singapore has cut its expected growth for the year to between 0 and 1 per cent. Annual gross domestic product (GDP) is expected to come in "at around the mid-point of the forecast range", said the Ministry of Trade and Industry (MTI) on Tuesday (Aug 13).

**13 August: US delays China tariffs for some items including cellphones, removing other products from list.** The United States Trade Representative office said Tuesday that new tariffs on certain consumer items would be delayed until Dec. 15, while other products were being removed from the new China tariff list altogether. It cited health and security factors. The duties had been set to go into effect on Sept. 1, so the announcement eased concerns about the holiday shopping season.

**14 August: Bond markets are sending one big global recession warning.** The U.S. bond market just flashed what could be its biggest warning yet of a coming recession, and it is not alone. The spread between the 2-year Treasury yield and the 10-year yield flipped so that the 2-year was higher than the benchmark 10-year yield for the first time since June 2007. Other parts of the curve have already inverted, but traditionally the 2-year to 10-year spread is the most widely watched by market players..

**20 August: China nudges lending rates lower with new benchmark.** China's central bank has set its newly christened benchmark lending rate lower, as expected, in a bid to reduce funding costs as the world's second-largest economy grapples with slowing growth and a trade war with the US. The People's Bank of China on Tuesday set the revamped loan prime rate at 4.25 per cent — just 6 basis points below the previous level, but in line with its stated goal of bringing the rate more closely in step with its medium-term lending facility for one-year loans, which stands at 3.3 per cent.

**23 August: China announces tariff hike on $75 billion of US products.** China on Friday announced tariff hikes on $75 billion of U.S. products in retaliation for President Donald Trump's latest planned increase, deepening a conflict over trade and technology that threatens to tip a weakening global economy into recession. China also will increase import duties on U.S.-made autos and auto parts, the Finance Ministry announced. The announcement comes as leaders of the Group of 7 major economies prepare to meet in France this weekend.

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