1 March 2019

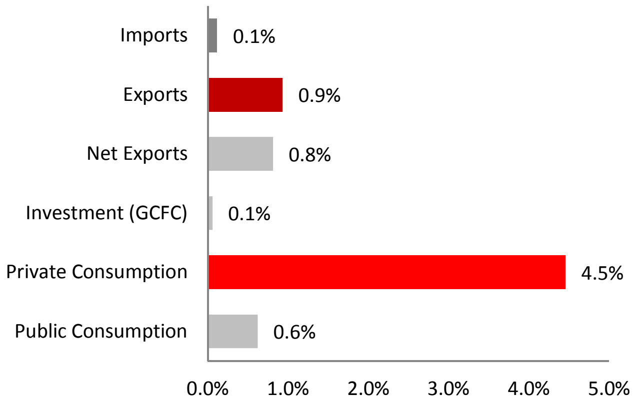
MONTHLY ECONOMIC REVIEW | February 2019

Malaysia's Economy Remains on Expansionary Path despite Global Uncertainties

- *GDP growth in 4Q18 exceeds market expectation. Malaysia's GDP growth expanded by 4.7%yoy in 4Q18, above market expectations of 4.5%yoy. Nevertheless, Malaysia's economy expands by 4.8% for the full-year 2018, meeting our forecast number. The 4Q18 GDP growth is the fastest GDP expansion since 1Q18. Recovery of economic growth is expected, thanks to improved performances of external trade, industrial activities and sustained solid domestic demand.*
- *2018's trade surplus hit MIDF's target. Malaysia's trade surplus widened to RM120.3B in 2018 (2017: RM98.5B) and slightly above MIDF's forecast of RM119B as exports outperformed imports. Exports and imports in 2018 increased by 6.7%yoy (2017: 19.3%yoy) and 4.9%yoy (2017: 20.2%yoy) respectively.*
- *Overall business confidence fell for the first time in 2 years. According to the latest Business Tendency Survey, overall business performance weakens at -2.2%, lowest since 1Q17. The main dragging factors are construction, mining, manufacturing and services sectors. Uncertainty on trade war, volatility of global commodity prices and reform measures by the federal government are reasons for the fell in overall business confidence in 1Q19.*

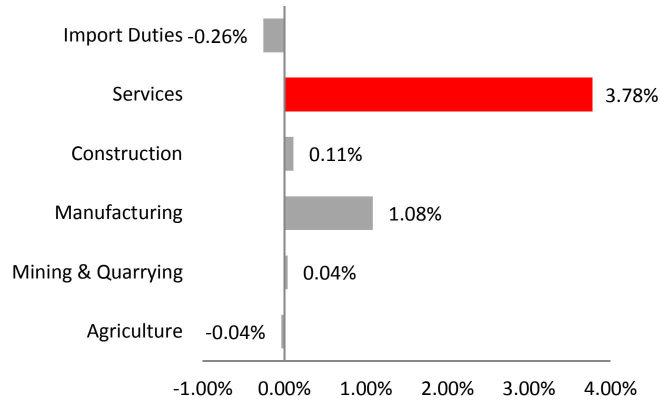
GDP growth in 4Q18 exceeds market expectation. Malaysia's GDP growth expanded by 4.7%yoy in 4Q18, above market expectations of 4.5%yoy. Nevertheless, Malaysia's economy expands by 4.8% for the full-year 2018, meeting our forecast number. The 4Q18 GDP growth is the fastest GDP expansion since 1Q18. Recovery of economic growth is expected, thanks to improved performances of external trade, industrial activities and sustained solid domestic demand. From supply side, services and manufacturing sectors contribute 3.8% and 1.1% respectively. We opine the solid GDP growth is mainly due to external factors particularly receding trade war effects and modest recovery in mining sector especially crude petroleum and LNG. In addition, moderating inflationary pressure, strengthening domestic demand and accommodative economic policies as well as strong re-exports growth continue driving up the GDP performance in the last quarter of 2018. On a flip side, slowdown in government spending and total investments as well as sluggish agriculture sector is among dragging factors during the quarter.

Chart 1: Contribution by Expenditure Components (%)



Source: CEIC, MIDFR

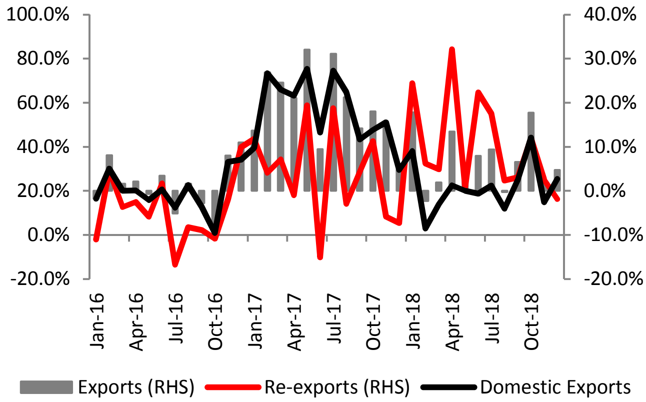
Chart 2: Contribution by Supply-Side Components (%)



Source: CEIC, MIDFR

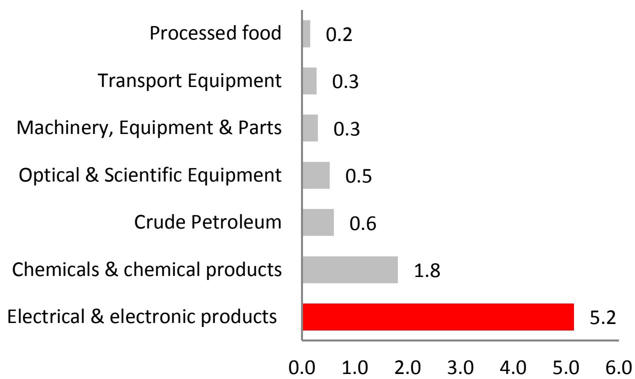
2018's trade surplus hit MIDF's target. Malaysia's trade surplus widened to RM120.3B in 2018 (2017: RM98.5B) and slightly above MIDF's forecast of RM119B as exports outperformed imports. Exports and imports in 2018 increased by 6.7%yoy (2017: 19.3%yoy) and 4.9%yoy (2017: 20.2%yoy) respectively. The lower growth of exports was a result of moderating sectoral performances. Manufactured goods, the largest contributor to exports experienced a slowdown in growth to a single digit of 9.1%yoy (2017: 18.9%yoy). Similarly, outbound shipment of mining goods grew by 7.1%yoy (2017: 23.9%yoy) while agriculture goods contracted by 14.2%yoy (2017: 10.9%yoy). For Dec-18 alone, exports growth tripled to 4.8%yoy from 1.6%yoy recorded in the previous month with value maintaining above the monthly average of RM83B. Meantime, imports growth slowed to 3-month low of 1%yoy in Dec-18. On a monthly basis, both exports and imports contracted by 1.9% and 5.4% respectively. Hence, trade surplus is recorded at RM10.4B during the month.

Chart 3: Total Exports: Domestic vs Re-exports (YoY%)



Source: CEIC, MIDFR

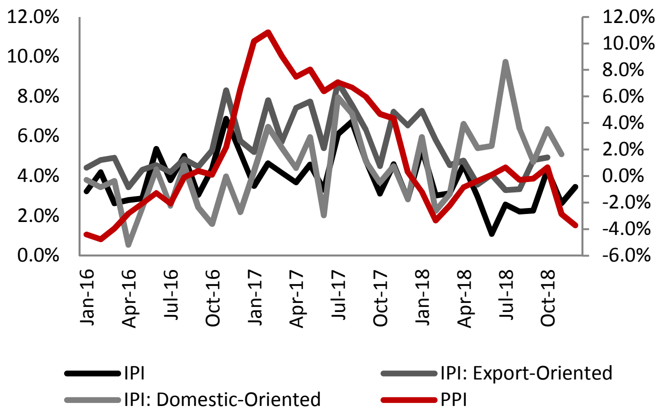
Chart 4: % Contribution to Exports Growth by Products



Source: CEIC, MIDFR

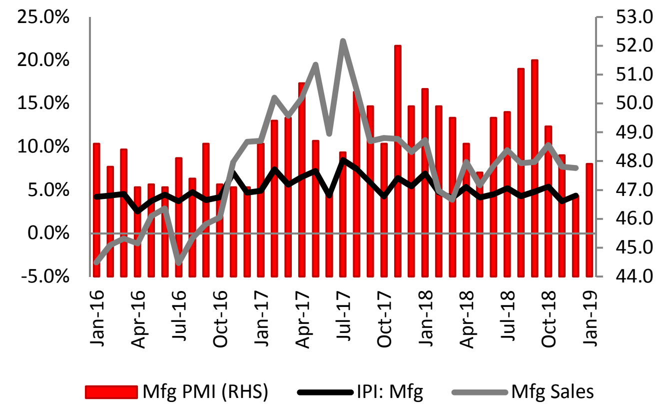
Recovery in mining supports IPI performance. Malaysia's industrial production improves by 3.4%yoy in Dec-18. Among others, mining output returns to positive rate of growth at 1%yoy and 1.6%mom. Factory output grew by 4.4%yoy, better than the previous month. For 4Q18, we expect Malaysia's GDP to expand at a stronger pace of 5% given that overall IPI growth averaged at 3.5%yoy, fastest since 2Q18. In particular, mining output rebounded to 0.6%yoy in 4Q18 after two-consecutive quarters recording contraction. Moving forward, we foresee IPI performance to expand at steady pace in 2019 amid tapering trade tension, strong global demand, expected-improve business environment and gradual pick-up in global commodity prices & currencies.

Chart 5: IPI vs PPI (YoY%)



Source: CEIC, MIDFR

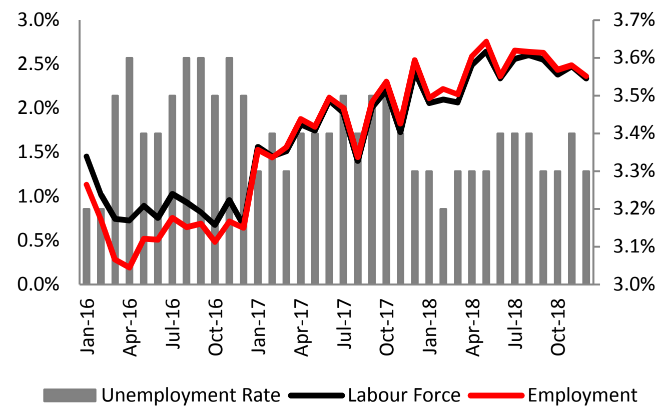
Chart 6: Manufacturing IPI & Sales (YoY%) vs PMI (Points)



Source: CEIC, MIDFR

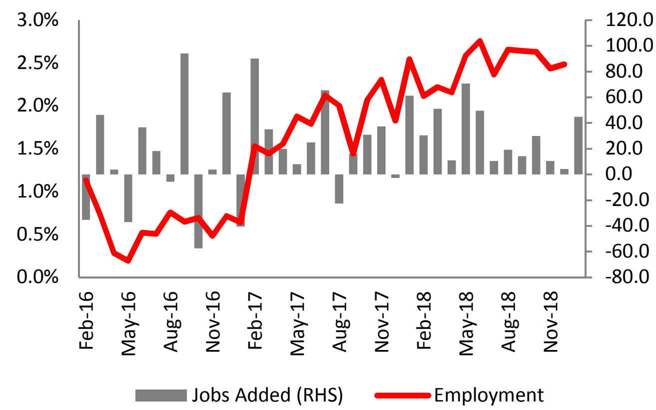
Labour market remains strong. Labour force expanded by 2.3%yoy to 15.5 million in Jan-19. Employment growth improved to 2.4%yoy to 15 million in Dec-18 while jobs added in the economy registered at 44.7K, highest in 7-month. The number of unemployed increased 1.7%yoy in Dec-18, after last month's 2.2%yoy. In addition, growth in both labour force and employment has been outpacing unemployment growth for the last 22 months since Mar-17. For full year 2018, jobless rate averaged at 3.3% while labour force and employment increases by 2.4%yoy and 2.5%yoy respectively. The stable job market among others a solid fundamental factor for the economy particularly in supporting domestic demand.

Chart 7: Labour Market Indicators (YoY%)



Source: CEIC, MIDFR

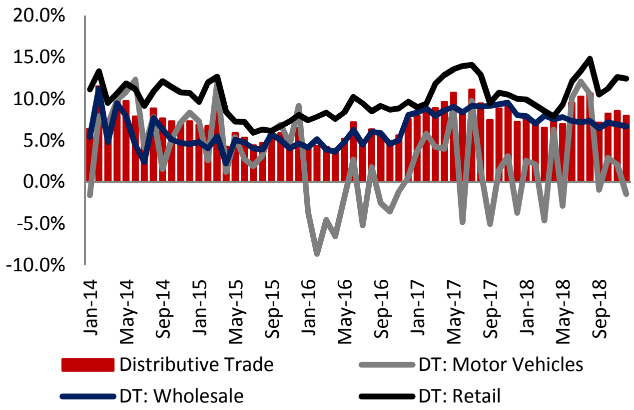
Chart 8: Jobs Added ('000) vs Empl. (YoY%)



Source: CEIC, MIDFR

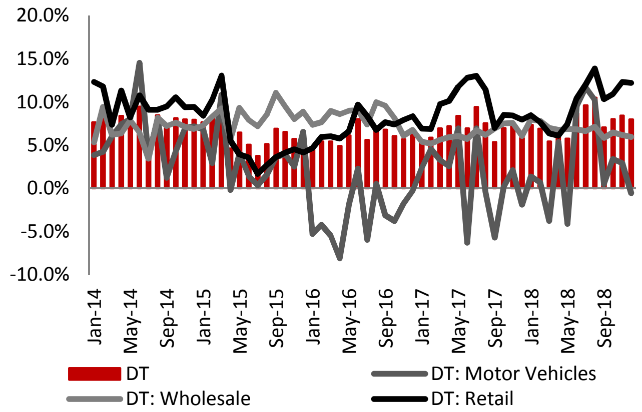
Domestic spending remains on strong tide. Distributive trade grew further by 8%yoy in Dec-18 as retail sales sustained its double digit growth for the 7-consecutive months. Wholesale trade increased by 6.7%yoy while motor vehicles fell by -1.4%yoy in the final month of 2018. On yearly basis, distributive trade expanded by 8.2%, motor vehicles by 3.3% (Highest in 3-year), wholesale by 7.3% and retail by 11% in 2018. Looking ahead, we view continuous solid domestic demand in 2019 underpin by stable job market, wage growth, moderate inflationary pressure and steady economic growth.

Chart 9: Distributive Trade, DT (YoY%)



Source: CEIC; MIDFR

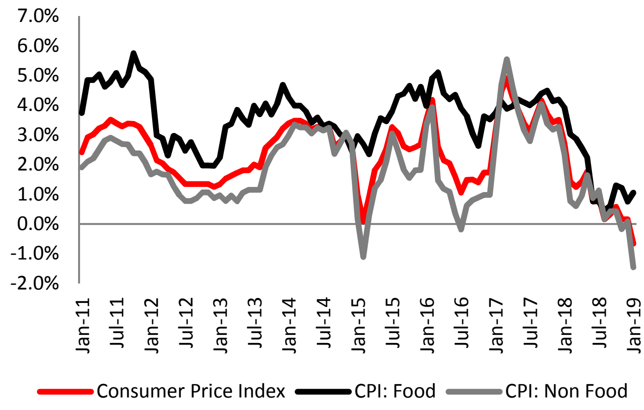
Chart 10: Distributive Trade Volume, DT (YoY%)



Source: CEIC; MIDFR

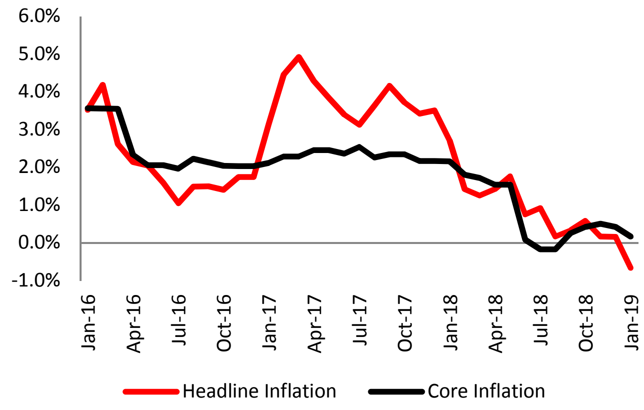
Starting the year with deflation. Consumer price index contracted 0.7%yoy in the first month of 2019, the first drop in over nine years after hovering below 1%yoy in the previous seven months. The lowest figure since Oct-09 was mainly attributed to deflationary pressures from the transport component. Transport prices continued to drop by 7.8%yoy in Jan-19, the lowest since Jul-16 following the switch to the weekly fuel price mechanism based on the Automatic Price Mechanism (APM) in order to reflect moves in global crude more quickly. Meanwhile, core inflation went down to 0.2%yoy (Dec-18: 0.4%yoy). On a monthly basis, prices fell 0.5% following a 0.1% rise in the preceding month and marking the first monthly drop in seven months. Looking ahead, Malaysia's consumer inflation is likely to improve in upcoming month as average Brent oil price for the first three weeks of Feb-19 hovered at USD64, resulting in marginally higher domestic fuel price of RM1.96.

Chart 11: CPI: Headline vs Food & Non-food (YoY%)



Source: CEIC, MIDFR

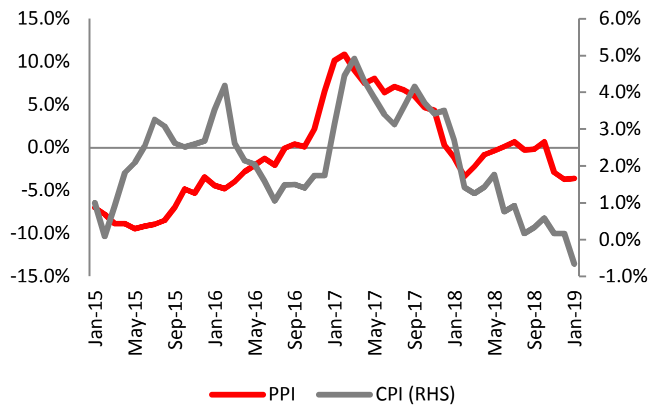
Chart 12: CPI: Headline vs Core (YoY%)



Source: CEIC, MIDFR

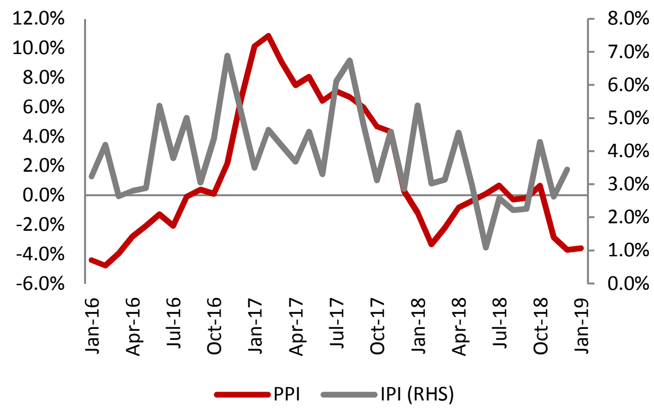
PPI stays on contractionary path. Malaysia's producer cost remains deflationary as PPI shrank by -3.6%yoy in Jan-19. This is mainly due to continuous falling input prices of manufacturing sector. Factory input price has been on negative growth for 13-consecutive months. Manufacturing sector still held the largest share at 81.6% in determining the producers' inflation. In addition, other sectors like agriculture and mining caused the dip in overall PPI. We expect the of PPI to remain low for the first half of 2019 given that retail fuel prices of RON95 and Diesel are capped at lower level than 2018's average prices.

Chart 13: PPI vs CPI (YoY%)



Source: CEIC, MIDFR

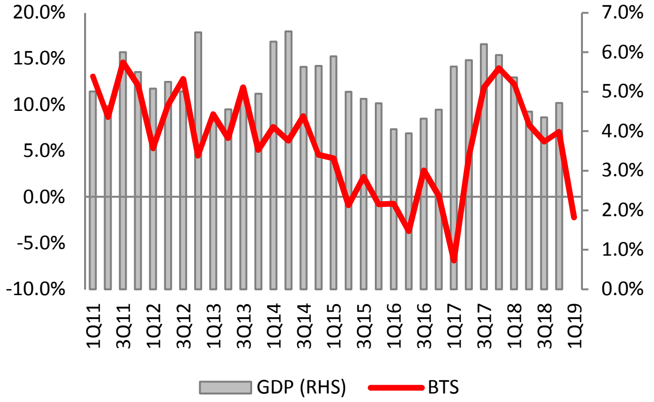
Chart 14: PPI vs IPI (YoY%)



Source: CEIC, MIDFR

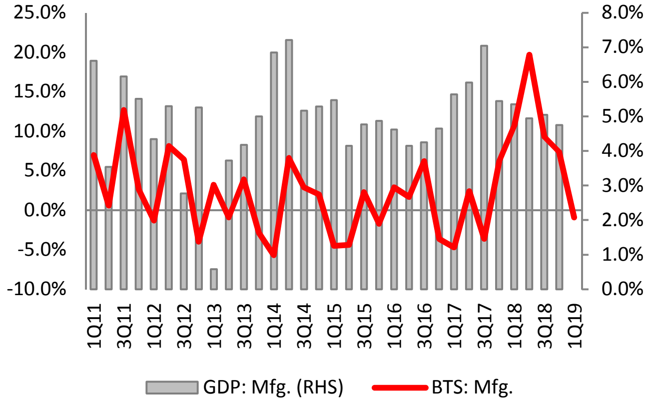
Overall business confidence fell for the first time in 2 years. According to the latest Business Tendency Survey, overall business performance weakens at -2.2%, lowest since 1Q17. The main dragging factors are construction, mining, manufacturing and services sectors. Uncertainty on trade war, volatility of global commodity prices and reform measures by the federal government are reasons for the fell in overall business confidence in 1Q19. Henceforth, we expect higher GDP growth the first quarter this year to remain below 5%.

Chart 15: BTS (%) vs GDP (YoY%)



Source: Bloomberg, MIDFR

Chart 16: Manufacturing: BTS (%) vs GDP (YoY%)



Source: Bloomberg, MIDFR

Table 1: Macroeconomic Data Updates

(YoY%) Unless Stated Otherwise	2013	2014	2015	2016	2017	2018	2019[f]
Real GDP	4.7	6.0	5.1	4.2	5.9	4.7	4.9
Private Consumption	7.2	7.0	6.0	6.0	7.0	8.1	7.5
Public Consumption	5.8	4.4	4.5	0.9	5.4	3.3	1.3
Gross Fixed Capital Formation	8.1	4.8	3.6	2.7	6.2	1.4	1.6
Exports of goods & services	0.3	5.0	0.3	1.3	9.4	1.5	2.0
Imports of goods & services	1.7	4.0	0.8	1.3	10.9	0.1	1.9
Net Exports (RMb)	83.6	94.7	91.2	92.8	91.0	103.2	106.0
Agriculture etc.	2.0	2.0	1.4	(5.2)	7.2	(0.4)	1.1
Mining & Quarrying	1.2	3.3	5.3	2.1	1.0	(1.5)	1.3
Manufacturing	3.4	6.1	4.8	4.4	6.0	5.0	4.9
Construction	10.6	11.7	8.4	7.4	6.7	4.2	2.1
Services	5.9	6.6	5.3	5.7	6.2	6.8	6.2
Exports of Goods (f.o.b)	2.5	6.7	1.5	1.4	19.3	7.3	3.6
Imports of Goods (c.i.f)	7.0	5.4	0.6	2.0	20.2	5.6	3.0
Trade Balance - RMb	71.3	82.5	91.6	88.1	98.5	119.8	126.3
Consumer Price Index	2.1	3.1	2.1	2.1	3.8	1.0	2.2
End of Unless States Otherwise	**2013**	**2014**	**2015**	**2016**	**2017**	**2018[e]**	**2019[f]**
Brent Crude Oil (Avg)	108.4	97.5	54.4	46.0	55.7	71.6	75.0
Crude Palm Oil (Avg)	2,435	2,384	2,237	2,642	2,659	2,293	2,280
USD/MYR (Avg)	3.15	3.27	3.90	4.14	4.30	4.00	4.05
USD/MYR	3.25	3.48	4.28	4.46	4.08	4.10	4.00
Overnight Policy Rate (%)	3.00	3.25	3.25	3.00	3.00	3.25	3.25

Source: MIDFR

February 2019 Key Economic Events

1 Feb: China can no longer rely on real estate for growth. It's now turning to railways and more debt. Chinese authorities face an ever-growing list of challenges — be it an ongoing trade fight with the U.S. or headwinds in domestic demand — and it appears they don't have many tools left to spur the economy amid a slowdown. The real estate market in China has traditionally played a major role in its economic development, household wealth and public sentiment.

4 Feb: Malaysia manufacturing downturn continues in January. The Malaysian manufacturing sector began 2019 with a fourth successive monthly deterioration in operating conditions, with output and new business both declining during January. The Nikkei Malaysia Manufacturing Purchasing Managers' Index (PMI) registered 47.9 in January, up from 46.8 in December.

13 Feb: Malaysia mulls biodiesel stabilization fund. Malaysia is mulling over establishing a fund to help contain price fluctuations of biodiesel, to ensure the fuel remains attractive to domestic consumers, said Primary Industries Minister Teresa Kok. Kok said she had proposed the biodiesel stabilization fund at a cabinet meeting but further discussions are needed on the matter.

18 Feb: PMO: Malaysia-China trade volume at record high of RM443B. Total trade volume between Malaysia and China reached a record high of US$108.6bil (RM443bil) in 2018, with the number of Chinese visitors into Malaysia increasing 29% to 2.94 million last year. Malaysia-China Business Council chairman Tan Kok Wai said overall relations between Malaysia and China remain on the right track despite the controversies regarding some local large scale projects in the country.

22 Feb: Malaysia Hits Deflation for First Time Since 2009 Global Crisis. Malaysia's economy swung into deflation in January for the first time since the aftermath of the global financial crisis in 2009 as fuel prices dropped. Consumer prices declined 0.7 percent from a year ago after hovering below 1 percent in the previous seven months, according to the statistics department. The median estimate in a Bloomberg survey of 21 economists was for a contraction of 0.4 percent. The government recently changed its fuel subsidy model by setting prices every week in order to reflect moves in global crude more quickly.

23 Feb: PMO: In future, peak-period congestion fees instead of highway tolls. The federal government plans to replace the current system of collecting tolls for highway use with congestion charge system, the Prime Minister's Office (PMO) said today. The PMO said the new system with variable fees based on peak period and non-peak hours would be introduced once the federal government succeeds in taking over the operations of four highways. Under the proposed congestion charge system, highway users will not have to pay anything during "off-peak" hours, but will have to pay a fee during peak hours when there is more traffic.

27 Feb: The U.K. and World Trade Organization Agree on a Post-Brexit Deal. Britain struck a trade deal Wednesday for a post-Brexit world, obtaining approval from other World Trade Organization members to stay part of a competitive market for lucrative government contracts after the country leaves the European Union. The agreement allows Britain to retain its place among the 47 WTO countries that are involved in the Government Procurement Agreement.

28 Feb: USTR to suspend China tariff hike 'until further notice'. The U.S. Trade Representative's office said on Wednesday it would move to formally suspend a scheduled tariff increase on Chinese goods "until further notice" following President Donald Trump's decision to delay his Friday deadline for a U.S.-China trade deal amid progress in their talks.The statement was issued after U.S. Trade Representative Robert Lighthizer's testimony to the U.S. House Ways and Means Committee, in which he said USTR was following a legal process to implement the delay.

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