3 March 2020

MONTHLY ECONOMIC REVIEW | February 2020

External & Domestic Pressures Put Malaysia Economy in Challenging Times

- *Leading Index continuous to decline. Malaysia's leading economic index fell -0.8%mom in Dec-19, faster pace decline compared to -0.2%mom in the preceding month. It was the second consecutive monthly fall and the steepest drop since May-19 as three (real imports of semiconductors and precious & other non-ferrous metals, and expected sales value in manufacturing sector) out of seven components posted decreases. However, annually, the index posted an increase of 1.4%yoy (Nov-19: 1.1%yoy). The growth rate remains favorable and suggests that the economy will continue expanding in the 1H20.*
- *Business confidence at 1-year low. Based on the Business Tendency Survey, overall business confidence further weakened to -2.1% in the first quarter of 2020. It is the lowest point since 1Q19. The slump in business confidence indicates 1Q20 GDP to remain below 4%yoy amid challenging economic environment from both external and domestic fronts.*
- *4Q19 GDP growth slides to 10-year low. Malaysia's GDP grew by 3.6%yoy in 4Q19, the slowest pace since 3Q09. The economy remains in expansion mode supported by solid domestic demand. On the other hand, external trade activities became a drag to the growth. By sector, services and manufacturing continued to back the economy during the quarter while construction stayed flat.*

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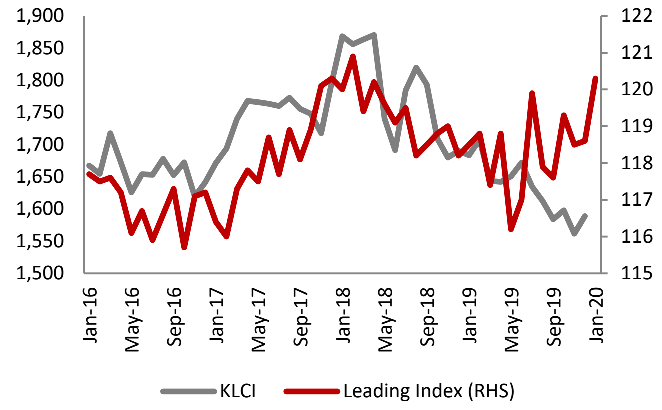
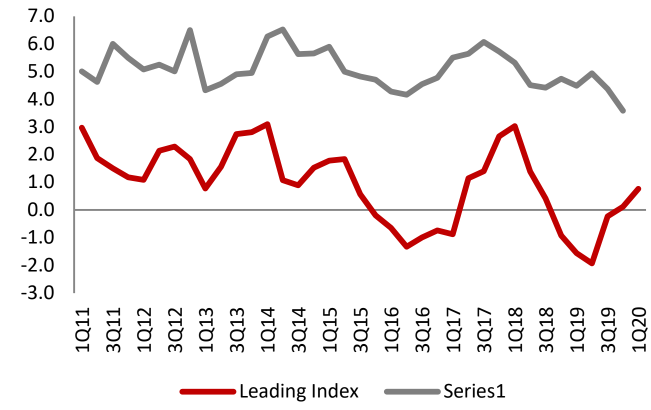
Chart 1: Leading Index vs KLCI (Points)



Source: CEIC, MIDFR

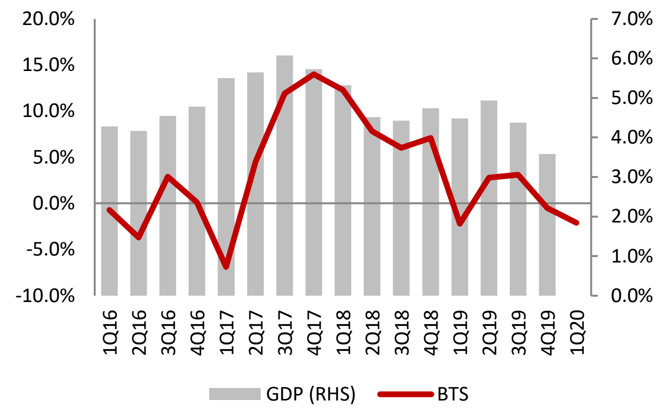
Chart 2: Leading Index vs GDP (YoY%)



Source: CEIC, MIDFR

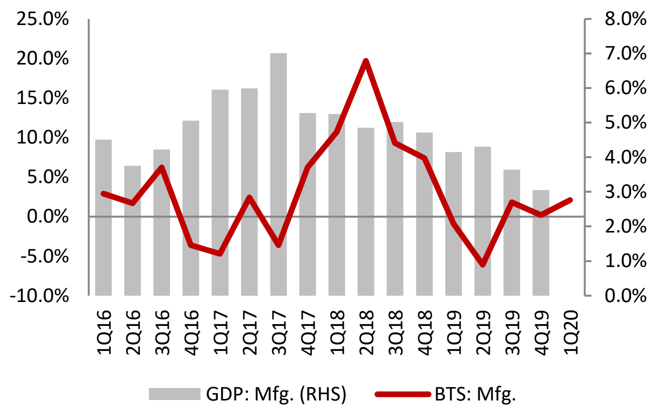
Business confidence at 1-year low. Based on the Business Tendency Survey, overall business confidence further weakened to -2.1% in the first quarter of 2020. It is the lowest point since 1Q19. The slump in business confidence indicates 1Q20 GDP to remain below 4%yoy amid challenging economic environment from both external and domestic fronts. Despite Phase One trade deal boosted positive sentiment globally, the outbreak of Covid-19 had reduced any momentum the global economic activity might have had. This also had an effect to commodity prices which struggled to move up. Domestically, political turmoil and the collapse of PH-led government cause uncertainty in the economy. However, an economic stimulus package worth RM20 billion had been announced, and we think the fiscal plan will continue regardless of the leadership of the new government.

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



Source: CEIC, MIDFR

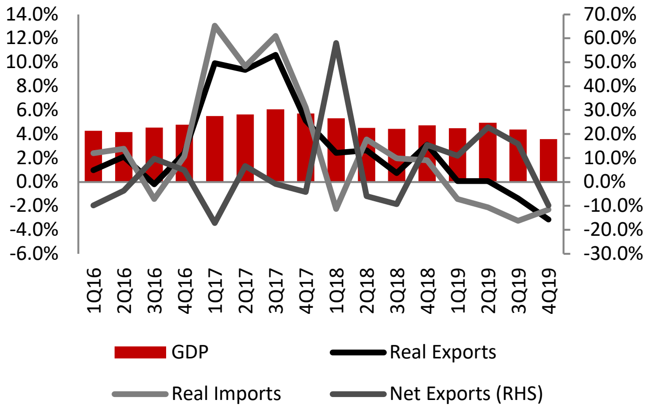
Chart 4: Manufacturing: BTS (%) vs GDP (YoY%)



Source: CEIC, MIDFR

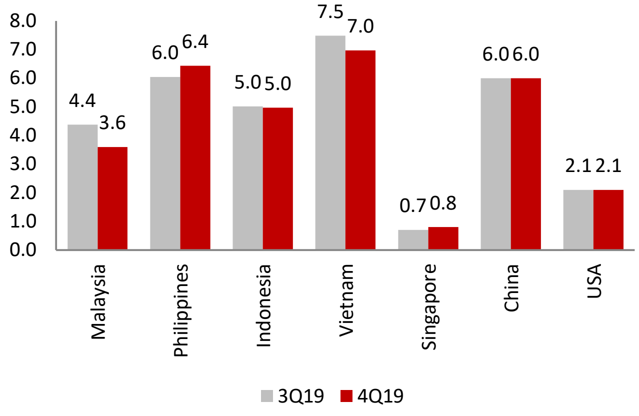
4Q19 GDP growth slides to 10-year low. Malaysia's GDP grew by 3.6%yoy in 4Q19, the slowest pace since 3Q09. The economy remains in expansion mode supported by solid domestic demand. On the other hand, external trade activities became a drag to the growth. By sector, services and manufacturing continued to back the economy during the quarter while construction stayed flat. In contrast, agriculture and mining contributed negatively to the growth in 4Q19. For the full year 2019, the economy advanced by 4.3%yoy, the slowest pace since GFC due to slowdown in all components on the expenditure side. Meanwhile, on the supply side, moderation observed in manufacturing, construction and services while agriculture and mining improved compared to 2018.

Chart 5: GDP vs External Trade (YoY%)



Source: CEIC, MIDFR

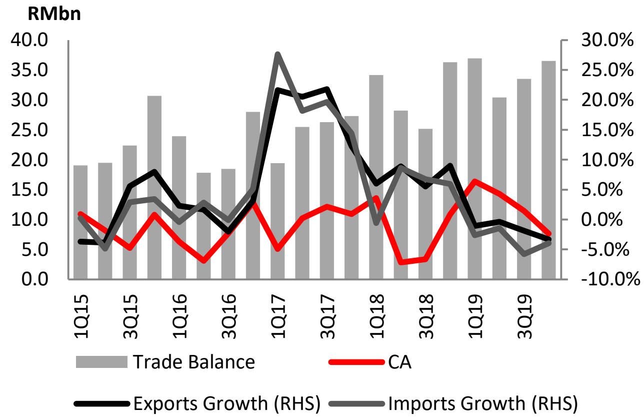
Chart 6: GDP Growth by Selected Country (YoY%)



Source: CEIC, MIDFR

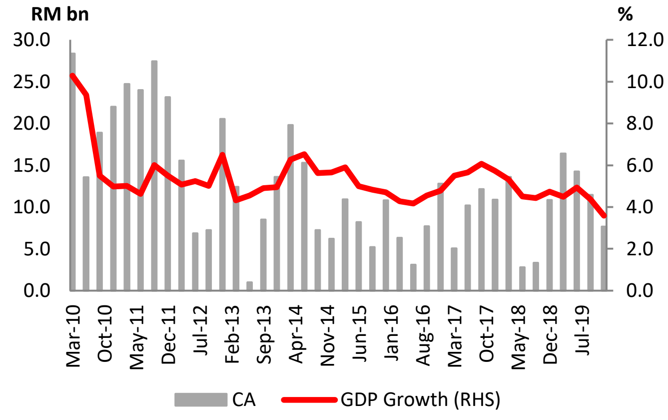
Current account surplus at five-quarter low. Malaysia's current account surplus dropped further to RM7.6b (or 1.9% of the GDP) in 4Q19, the lowest since 3Q18. The quarterly sequential moderation was mainly due to higher deficit in primary income and services account which increased to RM15.7b and RM4b compared to RM12.2b and RM1.6b in 3Q19. In contrast, goods account continued improving to RM32.8b due to solid trade surplus of RM36.5b (3Q19: RM 33.5b) resulting from harder fall in imports compared to exports. Exports and imports contracted by -3.3%yoy and -4%yoy respectively during the quarter. Meanwhile, secondary income continued to be in deficit but unchanged at RM5.5b compared to 3Q19. For full year 2019, current account surplus recorded at seven-year high of RM49.7b (or 3.3% of the GDP). Hence, Malaysia is still positioned as a net domestic saver built up from a record of current account surpluses.

Chart 7: Current Account Balance vs External Trade



Source: CEIC; MIDFR

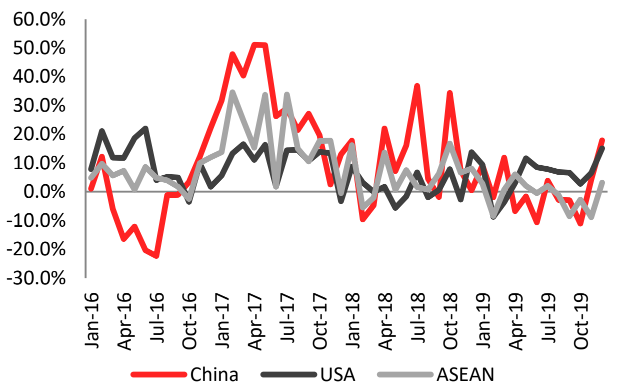
Chart 8: Current Account vs GDP Growth



Source: CEIC; MIDFR

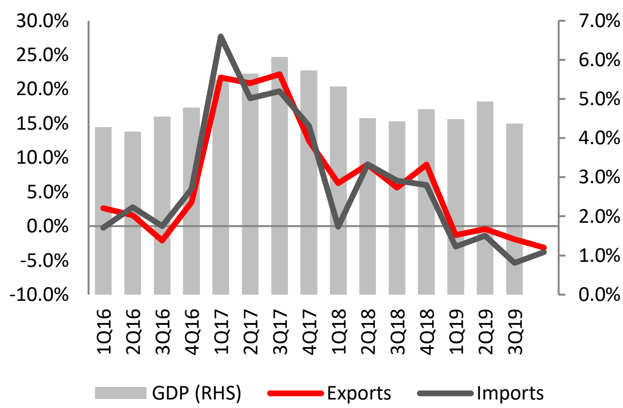
First export growth in five months. Malaysia total trade recorded positive growth in Dec-19 at +1.9%yoy, ending a six-month contraction streak as both export and import grew. Export expanded by +2.7%yoy after four consecutive months of negative growth. Similarly, import increased tepidly by +0.9%yoy following two months of decline. For full year of 2019, total trade fell -2.5%yoy as both export and import dropped. Export contracted by -1.7%yoy, slightly higher than MIDF's estimate of -1.1%yoy. It was the first contraction since GFC (-15.7%yoy in 2009), mainly due to the rising protectionism, loss of growth momentum of world's major economies and lower global commodity prices. However, its performance was not in isolation. We observed similar performance in other key economies such as Singapore, Indonesia, Thailand, South Korea and Japan which also recorded a decline in exports due to mostly externally driven issues. In particular, exports of Thailand and South Korea in 2019 went down to the levels last seen during the GFC, comparable to Malaysia.

Chart 9: Exports Growth (YoY%) by Major Destination



Source: CEIC, MIDFR

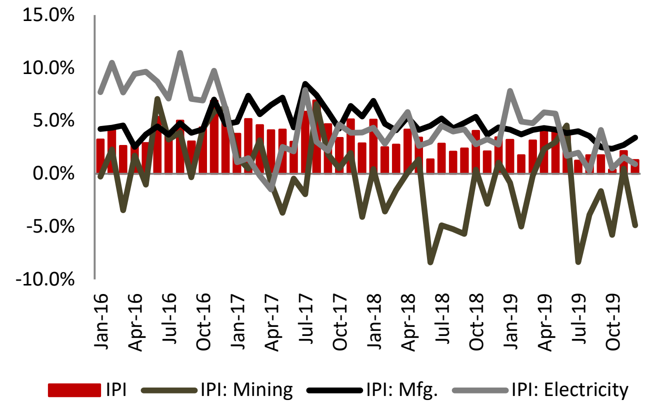
Chart 10: External Trade vs GDP, (YoY%)



Source: CEIC, MIDFR

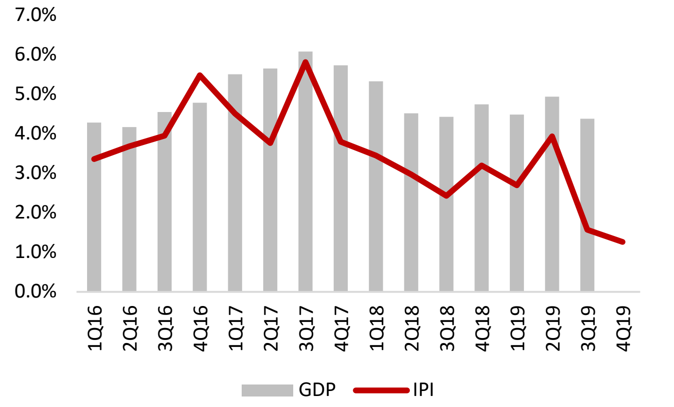
Manufacturing sector improved. Manufacturing production rose by 3.4%yoy, fastest in 4-month while the sales growth registered at 5-month high in the final month of 2019. Overall IPI growth moderated to 1.3%yoy amid contraction in mining output. The improvement of manufacturing sector in Dec-19 among others was due to positive sentiment of easing trade tension between the US and China. Nevertheless, the effects of Phase One trade deal may not be seen in 1Q20 amid Lunar New Year celebration, coronavirus and off-peak cycle for semiconductor industry. For 2019, overall IPI growth was 2.4% while manufacturing expanded by 3.6% and mining shrank by -1.7%, two-consecutive years of negative rate.

Chart 11: IPI Performances (YoY%)



Source: CEIC; MIDFR

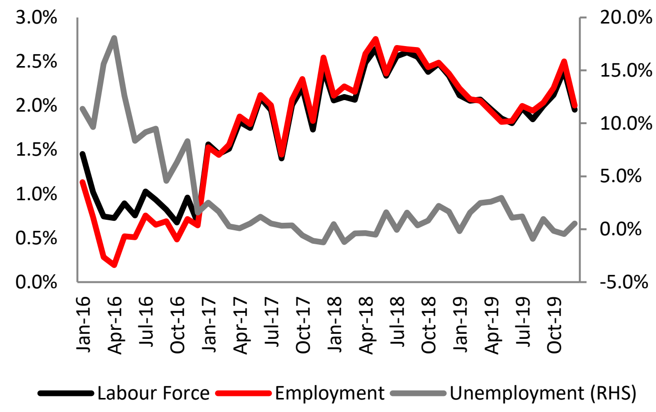
Chart 12: IPI vs GDP (YoY%)



Source: CEIC; MIDFR

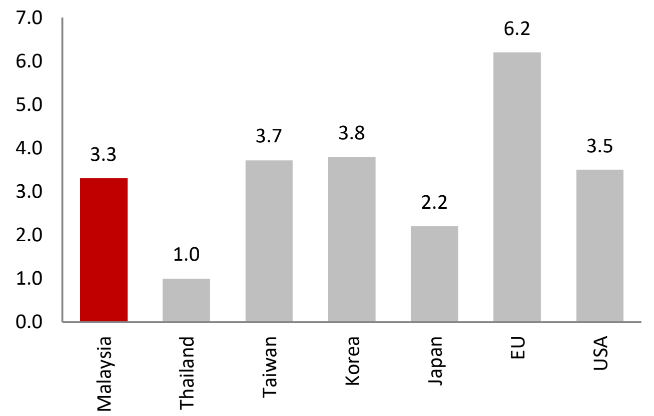
2019 average employment growth dropped. Malaysia's overall employment growth in 2019 dropped from 2.0%yoy compared to 2.5%yoy in 2018. Both the labour market and employment rose by 2.0%yoy in Dec-19, the lowest since Sep-19. Unemployment showed a slight expansion by 0.5%yoy, yet still maintaining jobless rate at 7-month low, 3.3%. Despite deterioration in external trade performance, improvement in job market was possibly due to stable expansion of IPI particularly domestic-oriented industries, commodity-based and services sectors. We opine the stable job market will provide solid foundation for Malaysia's domestic demand to grow at solid pace in 2020. In addition, we view Malaysia's labour market to remain stable despite the coronavirus outbreak and weak external demand in 1Q20.

Chart 13: Labour Market Key Indicators (YoY%)



Source: CEIC, MIDFR

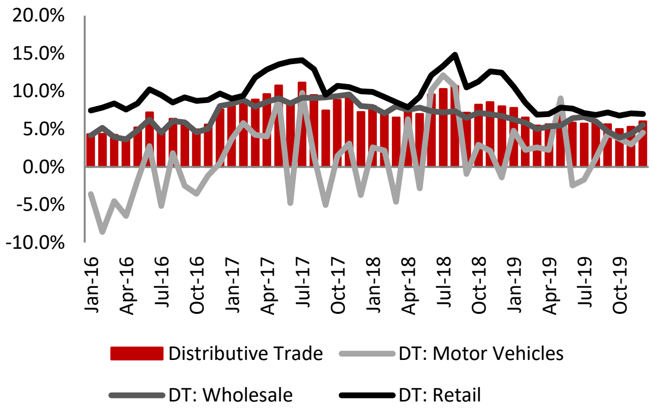
Chart 14: Global Unemployment Rates (%) in Dec-19



Source: CEIC, MIDFR

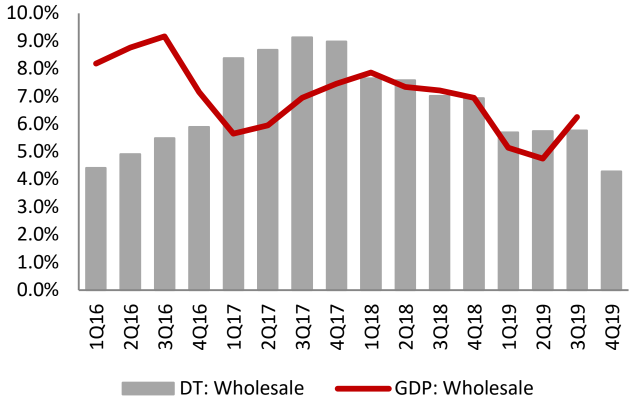
Distributive trade growth returned to 6%. Distributive trade growth hit 6%yoy in Dec-19 after hovering below that level for the past six months. In term of absolute value, it was new record high at RM115.9b. Breaking down the components, wholesale and motor vehicle trade increased at higher pace of 5.5%yoy (4-month high) and 4.5%yoy (7-month high) respectively. Meanwhile, sales growth maintained at 7%yoy for retail trade, unchanged from Nov-19. For full year 2019, distributive trade registered gowth of 6%yoy, the softest pace in three years. Wholesale, retail and motor vehicles trade expand by 5.4%yoy, 7.5%yoy and 2.8%yoy respectively. Retail sales growth in particular was the lowest on record.

Chart 15: Distributive Trade Sales, DT (YoY%)



Source: CEIC; MIDFR

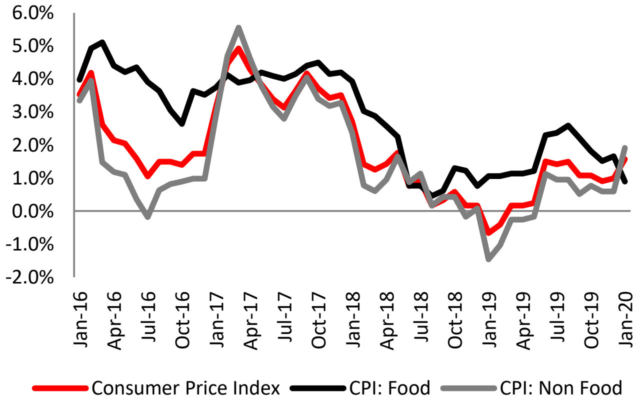
Chart 16: Wholesale Trade: GDP vs DT (YoY%)



Source: CEIC; MIDFR

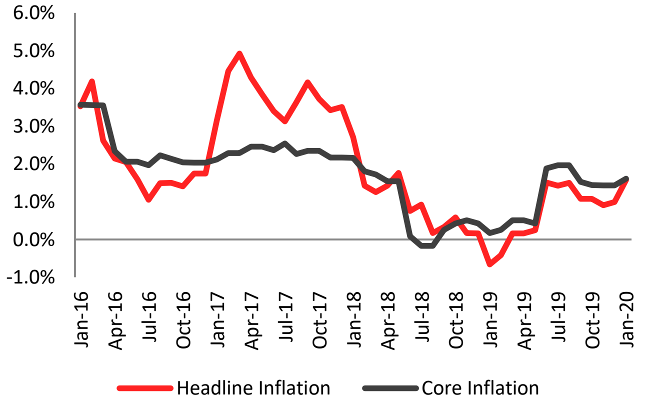
Inflation hit 20-month high. Headline inflation accelerated to 1.6%yoy in Jan-20, the fastest rate since May-18 primarily due to a rebound in prices of transport. Transport, the third largest component of CPI recorded positive growth in prices at 3.9%yoy after 14 months being in the negative territory. The 18-month high inflation of transport resulted from higher price of RON95 at RM2.08 in Jan-20 compared to RM1.95 in Jan-19 before the implementation of price cap in the final week of Feb-19. In contrast, prices of food & non-alcoholic beverages, the biggest component of CPI increased at a softer pace of 0.9%yoy, the lowest since Dec-18 while price growth for housing & utilities maintained at 1.7%yoy for the third consecutive month. Meanwhile, core inflation climbed up to 5-month high of 1.7%yoy.

Chart 17: CPI: Headline vs Food & Non-food (YoY%)



Source: CEIC, MIDFR

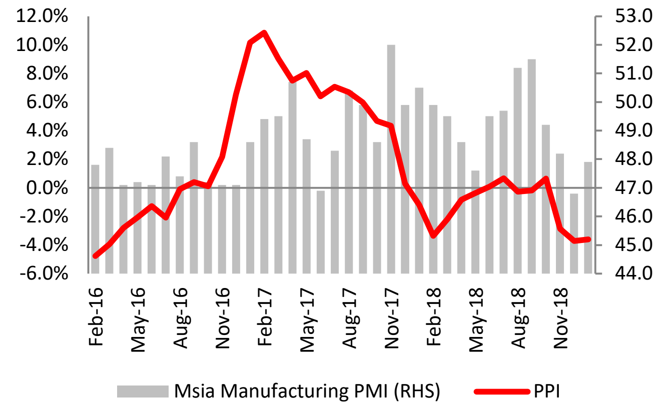
Chart 18: CPI: Headline vs Core (YoY%)



Source: CEIC, MIDFR

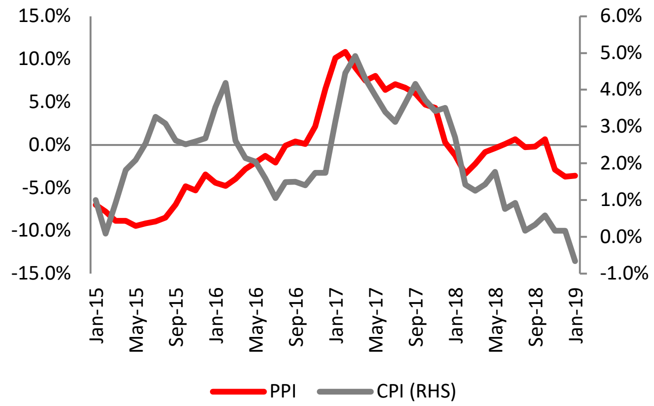
PPI stays on contractionary path. Malaysia's producer cost remains deflationary as PPI shrank by -3.6%yoy in Jan-19. This is mainly due to continuous falling input prices of manufacturing sector. Factory input price has been on negative growth for 13-consecutive months. Manufacturing sector still held 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 19: PPI (YoY%) vs Manufacturing PMI (Points)



Source: CEIC, MIDFR

Chart 20: PPI vs CPI (YoY%)



Source: CEIC, MIDFR

Table 1: Macroeconomic Past Performances (%)

(YoY%) Unless Stated Otherwise	2016	2017	2018	2019
Real GDP	4.4	5.7	4.7	4.3
Govt. Consumption	1.6	5.5	3.2	2.0
Private Consumption	5.8	6.8	7.9	7.6
Gross Fixed Capital Formation	2.5	6.1	1.3	(2.1)
Govt. Investment	(0.8)	0.5	(5.0)	(10.8)
Private Investment	4.4	9.1	4.4	1.5
Exports of goods & services	1.3	8.8	2.2	(1.1)
Imports of goods & services	1.5	10.3	1.3	(2.3)
Net Exports	0.3	(3.9)	14.6	8.9
Agriculture etc.	(3.6)	5.8	0.2	1.8
Mining & Quarrying	2.3	0.5	(2.6)	(1.5)
Manufacturing	4.4	6.1	5.0	3.8
Construction	7.5	6.8	4.3	0.0
Services	5.7	6.2	6.8	6.1
Exports of Goods (f.o.b)	1.2	18.8	7.3	(1.7)
Imports of Goods (c.i.f)	1.9	19.7	5.2	(3.5)
Trade Balance - RMb	88.1	98.5	123.8	137.4
Consumer Price Index	2.1	3.8	1.0	0.7
Current Account - % of GDP	2.4	2.8	2.1	3.6
Fiscal Balance - % of GDP	(3.2)	(3.1)	(3.8)	(3.4)
Federal Government Debt - % of GDP	51.9	50.1	51.2	52.5
Year-End of Unless States Otherwise	**2016**	**2017**	**2018**	**2019**
Brent Crude Oil (Avg)	46.0	55.7	70.0	64.3
Crude Palm Oil (Avg)	2,630	2,690	2,320	2,079
USD/MYR (Avg)	4.14	4.30	4.00	4.14
USD/MYR	4.46	4.08	4.10	4.09
Overnight Policy Rate (%)	3.00	3.00	3.25	3.00

Source: MIDFR

February 2020 Key Economic Events

10 February: Malaysia end-Jan palm oil stocks fall to lowest since June 2017. Malaysia's palm oil inventories fell a fifth straight month amidst tighter production and slower demand, with January end-stocks below two million tonnes, official data showed on Monday. January stocks slumped 12.7% to 1.76 million tonnes from the previous month, lowest since June 2017, data from the Malaysian Palm Oil Board (MPOB) showed.

14 February: US and China halve tariffs as pledged in phase one trade deal. The U.S. cut tariffs on Friday for $120 billion of Chinese goods from 15% to 7.5%, marking the first time that sanctions have been eased after nearly two years of escalating trade tensions between the world's two biggest economies.

19 February: South Korea coronavirus cases surge, majority linked to Daegu church. The mayor of a South Korean city at the centre of a new coronavirus outbreak told residents to stay indoors on Thursday as a surge in confirmed cases linked to a local church raised the prospect of wider transmission. Malls, restaurants and streets in Daegu, the country's fourth largest city with a population of 2.5 million, were largely empty in scenes that local social media users likened to a disaster movie.

20 February: Chinese banks cut lending rate to prop up coronavirus-hit economy. Chinese lenders have cut a benchmark lending rate in a bid to prop up the country's virus-hit economy as S&P warned that banks faced a surge of up to $1.1tn in bad loans. Major lenders on Thursday reduced the one-year loan prime rate — a key lending rate used across China's financial system — by 0.1 percentage points to 4.05 per cent. The reduction, which had been expected following the central bank's own cut to its medium-term lending rate earlier this week, will ease lending conditions.

24 February: EPF dividend rate highly dependent on global economy. The Employees' Provident Fund's (EPF) dividend rate is highly dependent on the state of the global economy and volatility in the financial markets, said market observers. Bank Islam Malaysia Bhd chief economist Dr Mohd Afzanizam Abdul Rashid said the dividend rate of 5.45% for Simpanan Konvensional and 5.0% for Simpanan Shariah for 2019 were respectable returns considering that the global economic environment had been so uncertain.

24 February: Bursa Malaysia closes at lowest level in almost 10 years on Dr M's resignation. Political turmoil brought about by the collapse of the Pakatan Harapan government has placed further strain on Malaysia's economy, as the country's stock exchange closed at its lowest point since late 2010 on Monday. Economists say that political uncertainty brought about by the shock resignation of Prime Minister Tun Dr Mahathir Mohamad today could deter investors looking for stability at a time when the global Covid-19 coronavirus outbreak and trade wars are hurting growth.

27 February: Government unveils RM20b stimulus package to boost spending. The Malaysian government has allocated RM20 billion under a stimulus package to boost the sluggish economy by putting more cash into the hands of consumers and providing tax reliefs to sectors particularly hard hit by the Covid-19 outbreak. It will also accelerate planned investment projects by government-linked companies this year including one involving 1,400mw of solar power generation to flush more money into the economy.

28 February: Malaysia's monarchy to rule on pathway out of political turmoil. Malaysia's nine monarchs are due to meet on Friday to determine how the country's next government will be formed after the shock resignation of Mahathir Mohamad earlier this week created political turmoil. Mahathir's move, which broke a coalition with old rival Anwar Ibrahim that had secured a surprise election victory two years ago, has been widely perceived as an attempt to consolidate the 94-year-old leader's power.

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