27 June 2019

ECONOMIC REVIEW | May 2019 Producer Price Index

PPI Remains in Deflationary due to Falling Input Prices of Manufacturing & Agriculture Sectors

- *PPI stays on contractionary path. Malaysia's producer cost remains deflationary as PPI shrank by -1.5%yoy in May-19. This is mainly due to continuous falling input prices of agriculture and manufacturing sectors. Factory input price has been on negative growth for 17-consecutive months. Manufacturing sector still held the largest share at 81.6% in determining the producers' inflation.*
- *Consumer's inflationary pressure to remain benign. As a 3-6 months leading indicator of price changes at the consumer level, the latest PPI number suggests that Malaysia's headline inflation to stay low for the 2H19. Referring to input price of food product, the component has been falling since Dec-17. Despite that, the rate of decline has been contracting since Dec-18 with the latest at -8%yoy in May-19. As food items hold almost the majority share in Malaysia's CPI, we expect the improvement to partly offset gloomy inflation caused by significant decline in transport component.*
- *We forecast producer deflation at -1.5% for 2019. We foresee producer prices to grow further into deflation this year at -1.5% from -1.1% in 2018. This was mainly due to domestic oil prices which are expected to be on the low side even with the removal of RON95 price cap, in line with declining global crude oil prices. As fuel is required at least to ship goods from one place to another besides businesses that use it as a major input, we believe such low fuel prices will make production cheaper, reducing inflationary pressure for the overall PPI.*

PPI stays on contractionary path. Malaysia's producer cost remains deflationary as PPI shrank by -1.5%yoy in May-19. This is mainly due to continuous falling input prices of agriculture and manufacturing sectors. Factory input price has been on negative growth for 17-consecutive months. Manufacturing sector still held the largest share at 81.6% in determining the producers' inflation. 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.

Table 1: Producer Price Indices by Selected Sector

	MoM%			YoY%		
	Mar-18	Apr-18	May-18	Mar-18	Apr-18	May-18
PPI	(0.3)	0.6	0.2	(1.5)	(1.4)	(1.5)
Agri, forestry & fishing	(5.8)	1.0	(1.6)	(14.2)	(11.9)	(12.8)
Mining	0.5	6.9	2.7	3.0	1.4	(0.4)
Manufacturing	0.1	(0.2)	0.1	(0.8)	(0.8)	(0.6)
Electricity and gas	2.1	(0.8)	0.1	2.1	1.5	1.2
Extraction of Petroluem & Natural Gas	0.5	6.9	2.7	3.0	1.4	(0.4)
Food Product	(0.1)	(0.4)	(0.2)	(9.4)	(9.1)	(8.0)

Source: CEIC, MIDFR

Consumer's inflationary pressure to remain benign. As a 3-6 months leading indicator of price changes at the consumer level, the latest PPI number suggests that Malaysia's headline inflation to stay low for the 2H19. Referring to input price of food product, the component has been falling since Dec-17. Despite that, the rate of decline has been contracting since Dec-18 with the latest at -8%yoy in May-19. As food items hold almost the majority share in Malaysia's CPI, we expect the improvement to partly offset gloomy inflation caused by significant decline in transport component. Food inflation is predicted to stay above the overall CPI given that Malaysia is a net importer of food. On the other hand, continuous falling of input prices would somehow support Malaysia's industrial activities. Cost of crude materials and intermediate materials supplies & components remain in contraction mode in May-19. In contrast, cost of finished goods recovered marginally to 0.1%yoy.

Table 2: Producer Price Indices by Stage of Processing

	MoM%			YoY%		
	Mar-18	Apr-18	May-18	Mar-18	Apr-18	May-18
PPI By Stage of Processing (SP)	(0.3)	0.6	0.2	(1.5)	(1.4)	(1.5)
Crude Materials for Further Processing (CM)	(1.1)	4.0	0.2	(3.0)	(1.5)	(5.0)
Intermediate Materials Supplies and Components (IM)	0.1	(0.3)	0.2	(1.3)	(1.8)	(0.8)
Finished Goods (FG)	(0.2)	(0.3)	0.4	(0.6)	(0.4)	0.1
Capital Equipment (CE)	(0.1)	(0.5)	0.6	0.7	1.0	1.2

Source: CEIC, MIDFR

Slowdown in PPI amid trade tensions. In May-19, most of the key economies' PPI moderated, attributable to the US-China impasse. US-China trade disputes cause business sentiment to deteriorate. Businesses may be less keen to make new investments and try to reduce existing costs due to uncertainty in future demand. Besides that, global oil prices also plunged on the US-China trade war escalation. The average price of Brent crude oil contracted by -9.6%yoy to USD 69.4pb in May-19 (Apr-19: USD 71.5pb). Falling oil price could be one of the major factors that pushed down the input prices. The US producer inflation fell into negative territory of -0.8%yoy after maintaining at 0.9%yoy growth for two consecutive months. China's PPI contracted further to -3.4%yoy (Apr-19: -2.4%yoy). Moving forward, we foresee PPI to stay low amid anticipations of lower average global crude oil prices this year than in 2018. Oil prices will continue to be under downward pressure if US-China fails to reach a deal.

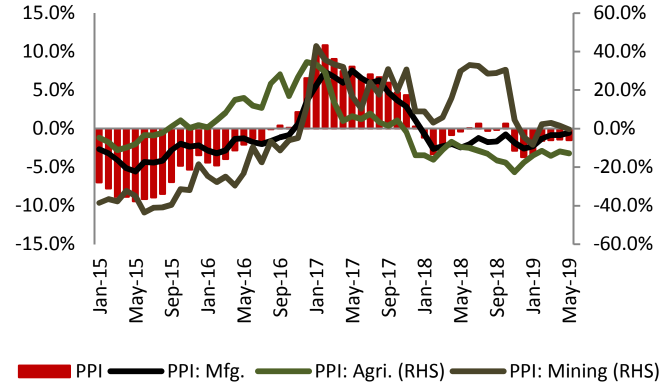
Table 3: Global Producer Price Index (YoY%)

	Oct-18	Nov-18	Dec-18	Jan-19	Feb-19	Mar-19	Apr-19	May-19
Malaysia	0.7	(2.9)	(3.7)	(3.6)	(1.6)	(1.5)	(1.4)	(1.5)
Indonesia	4.1	3.8	3.6	3.2	2.9	3.2	3.5	3.7
Thailand	1.7	0.9	(0.5)	(1.1)	(0.6)	0.4	0.7	0.0
Philippines	1.2	0.4	0.3	3.8	3.2	4.5	3.7	
Japan	3.0	2.3	1.5	0.6	0.9	1.3	1.3	0.7
China	(3.4)	(2.9)	(3.8)	(4.0)	(3.5)	(2.6)	(2.4)	(3.4)
EU	4.0	3.0	1.9	1.8	1.9	2.0	1.9	
USA	5.0	3.3	2.4	0.6	(0.3)	0.9	0.9	(0.8)

Source: CEIC, MIDFR

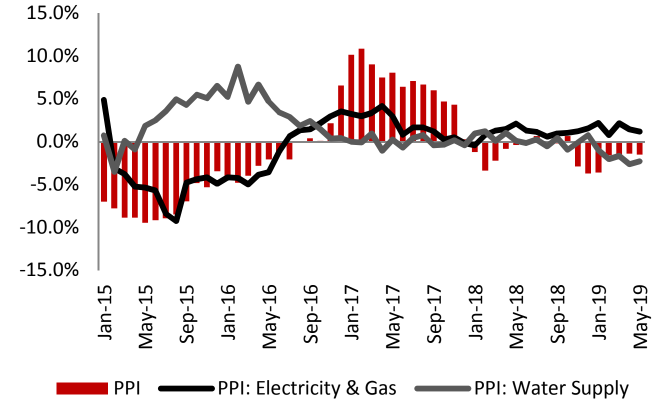
We forecast producer deflation at -1.5% for 2019. We foresee producer prices to grow further into deflation this year at -1.5% from -1.1% in 2018. This was mainly due to domestic oil prices which are expected to be on the low side even with the removal of RON95 price cap, in line with declining global crude oil prices. As fuel is required at least to ship goods from one place to another besides businesses that use it as a major input, we believe such low fuel prices will make production cheaper, reducing inflationary pressure for the overall PPI. We anticipate inflationary pressure mainly from fuel-related items to remain weak in line with our expectation of Brent crude oil price at $70pb for 2019 (2018: $71.6pb).

Chart 1: PPI Performance by Sector (YoY%)



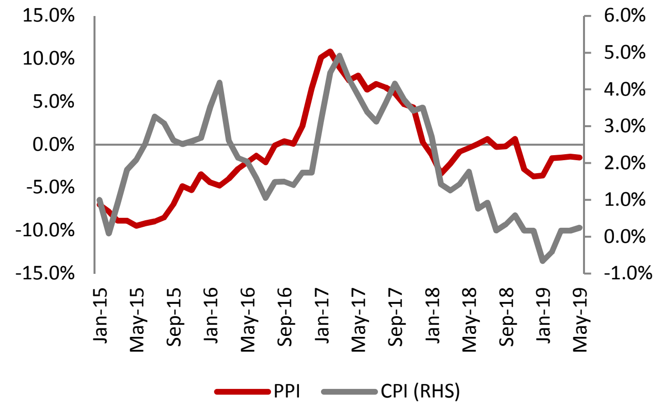
Source: CEIC, MIDFR

Chart 2: PPI vs Utilities (YoY%)



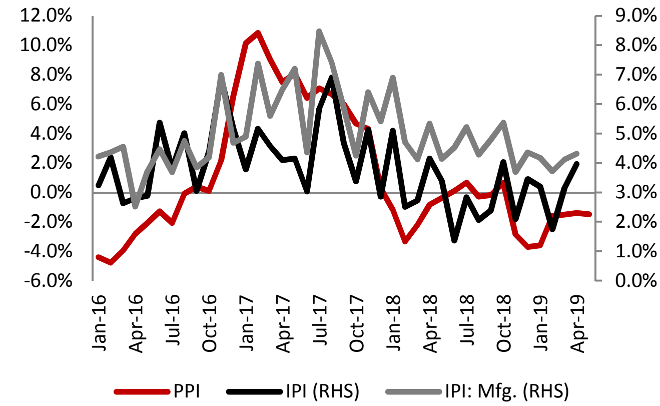
Source: CEIC, MIDFR

Chart 3: PPI vs CPI (YoY%)



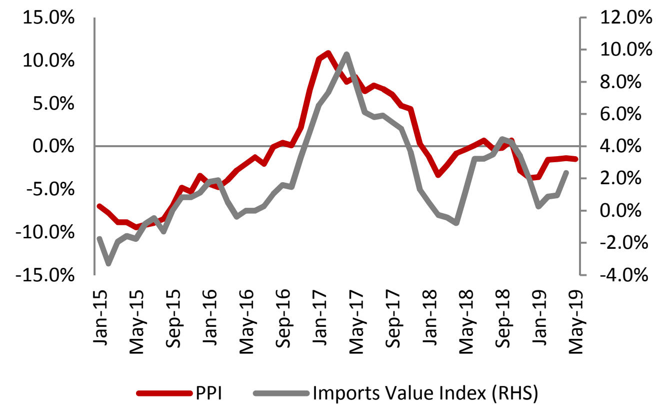
Source: CEIC, MIDFR

Chart 4: PPI vs IPI (YoY%)



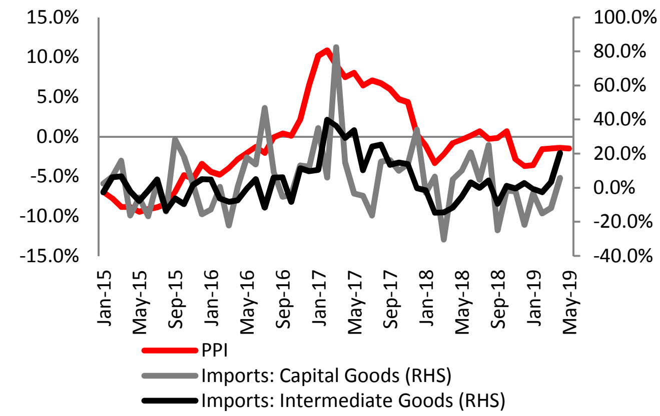
Source: CEIC, BLOOMBERG, MIDFR

Chart 5: PPI vs Imports Value Index (YoY%)



Source: CEIC, MIDFR

Chart 6: PPI vs Imports (YoY%)



Source: CEIC, MIDFR

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