2 August 2019

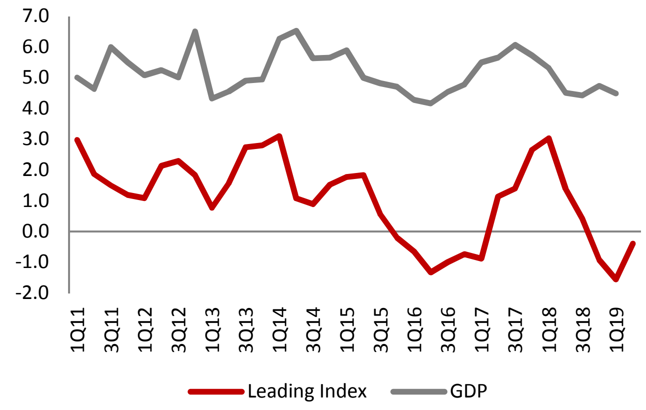
MONTHLY ECONOMIC REVIEW | July 2019

Malaysia's Economic Momentum to Continue Growing from Easing Trends of Global Monetary Rates

- *Malaysia's economy remains in upward track. Malaysia's leading economic index is still pointing towards recovery path. The latest figure recorded in May-19 is mainly drag down by expected sales value of manufacturing sector. Export-oriented and manufacturing-focus sectors are predicted to experience slowdown due to trade war between the US-China and dispute between Japan-South Korea. On a flip side, outlook for 2H19 is bright underpin by lower interest rates in developed and emerging economies, gradual pick-up in commodity prices and firm domestic demand.*
- *IPI grew higher than expected. Malaysia's IPI expanded steadily by 4%yoy in May-19, outpacing market expectation of 3.5%yoy. The growth is mainly attributed by the continuous rebound in mining output and expansion in manufacturing and electricity output. Mining output increased significantly by 3%yoy, the fastest since Aug-17.*
- *Fed's funds rate lower by 25 basis points. The Fed reduces its key policy rate to 2.00-2.25% during the FOMC meeting in Jul-19. The central bank views the economy is expanding at moderate pace while global uncertainties remain as major downside risks. Cutting the interest rate is expected to impact economic activities in the US particularly household spending and business investment. In addition, it may offset the uncertainties due to global trade tension.*

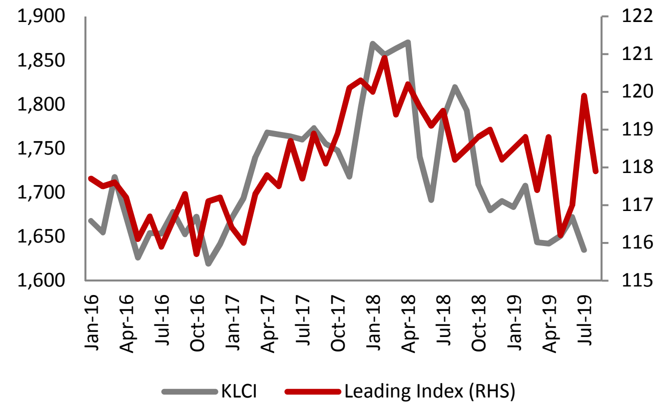
Malaysia's economy remains in upward track. Malaysia's leading economic index is still pointing towards recovery path. The latest figure recorded in May-19 is mainly drag down by expected sales value of manufacturing sector. Export-oriented and manufacturing-focus sectors are predicted to experience slowdown due to trade war between the US-China and dispute between Japan-South Korea. On a flip side, outlook for 2H19 is bright underpin by lower interest rates in developed and emerging economies, gradual pick-up in commodity prices and firm domestic demand. Among others, the US, Australia, Indonesia, Saudi Arabia and South Korea have taken the steps to ease their monetary policies. Global energy prices particularly Brent oil is at encouraging level for mining players to continue pumping output. Domestically, lower OPR in May-19 is expected to translate into higher spending and investment in 2H19. However, trade war remains as downside risks to Malaysian economy as the resumption of trade talks between the US-China remains uncertain and 50-50 chance of securing an agreement.

Chart 1: Leading Index vs GDP (YoY%)



Source: CEIC, MIDFR

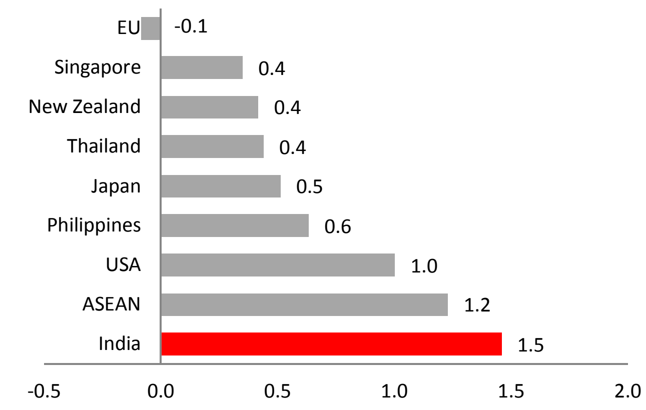
Chart 2: Leading Index vs KLCI (Points)



Source: CEIC, MIDFR

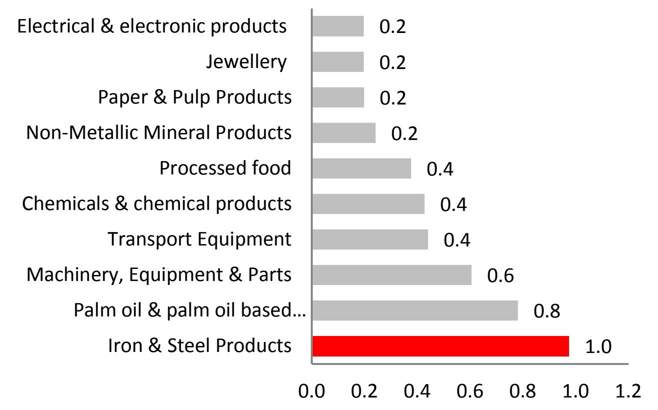
Continuous positive momentum in exports. Exports growth doubled to 2.5%yoy in May-19 from 1.1%yoy in Apr-19, continuing the gradual recovery since Mar-19. In contrast, imports expanded at a softer pace of 1.4%yoy (Apr-19: 4.4%yoy). Hence, trade surplus widened to RM 9.1b (May-18: RM 8.1b) but narrowed compared to last month. Sector wise, manufacturing exports (84.2% share) advanced at a higher rate of 3.1%yoy (Apr-19: 2.7%yoy). Furthermore, agriculture exports (7.5% share) rebounded sharply to a double digit positive growth of 15.3%yoy (Apr-19: -9.3%yoy). Meanwhile, mining goods exports (7.5% share) growth continued to be in negative territory of -10.9%yoy).

Chart 3: % Contribution by Destination to Exports Growth



Source: CEIC, MIDFR

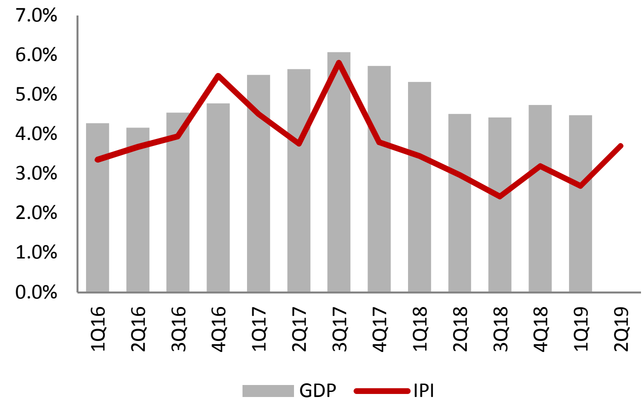
Chart 4: % Contribution by Product to Exports Growth



Source: CEIC, MIDFR

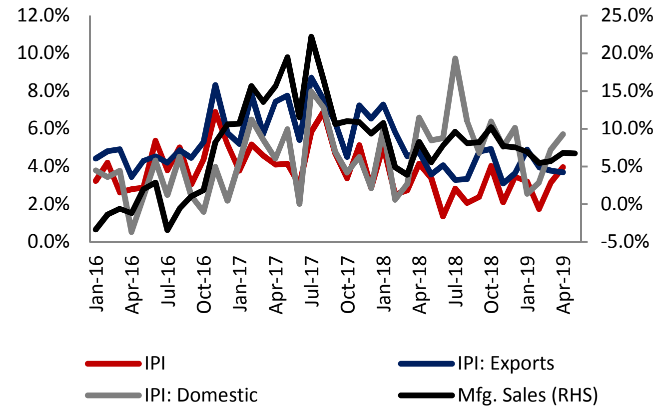
IPI grew higher than expected. Malaysia's IPI expanded steadily by 4%yoy in May-19, outpacing market expectation of 3.5%yoy. The growth is mainly attributed by the continuous rebound in mining output and expansion in manufacturing and electricity output. Mining output increased significantly by 3%yoy, the fastest since Aug-17. Moving forward, we foresee IPI performance to expand at a moderate pace in 2H19 underpin by lower OPR effects, low inflationary pressure, stable domestic demand, positive progression in construction sector and gradual pick-up in commodity prices. Nevertheless, trade war factor remains as downside risk to global trade activities as well as Malaysia's industrial activities.

Chart 5: IPI vs GDP (YoY%)



Source: CEIC, MIDFR

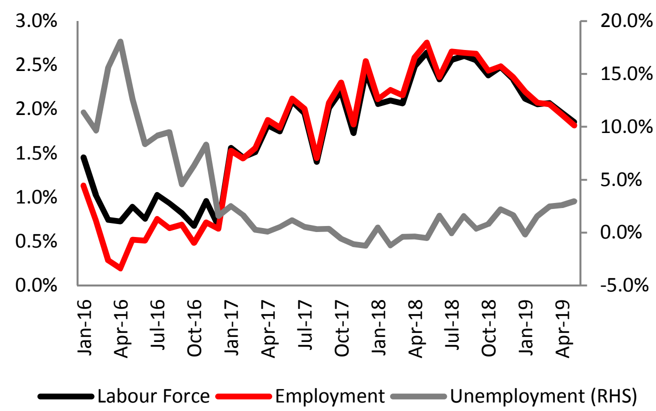
Chart 6: IPI vs Mfg. Sales (YoY%)



Source: CEIC, MIDFR

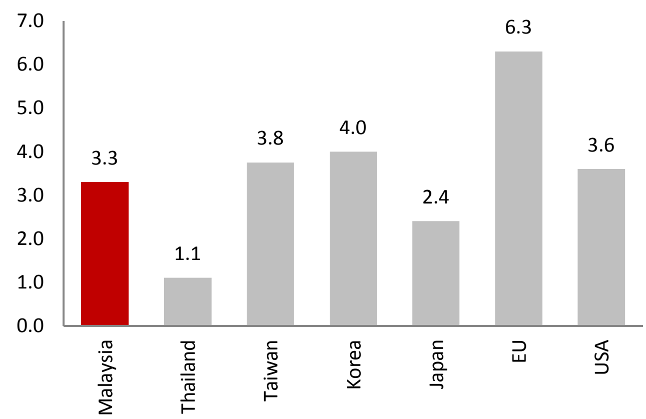
Labour market remains stable. Labour force grew at 1.9%yoy in May-19, weakest gain in 18-month. Similarly, employment growth recorded at 1.8%yoy with monthly jobs added in the economy seen at 32.7K. Meanwhile, the number of unemployment increased further by 3%yoy, highest since Nov-16. Nevertheless, labour market remains steady as the economy is expected to continue expanding at a steady pace in 2H19. The stable job market reflects full-employment condition, healthy development of Malaysia's economy and provides solid support to domestic demand.

Chart 7: Labour Market Key Indicators (YoY%)



Source: CEIC, MIDFR

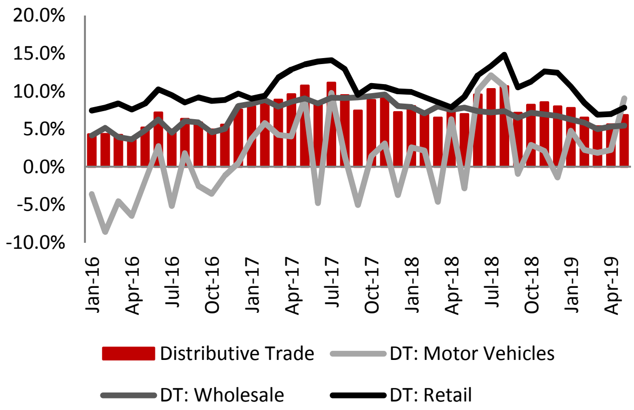
Chart 8: Global Unemployment Rates (%) in May-19



Source: CEIC, MIDFR

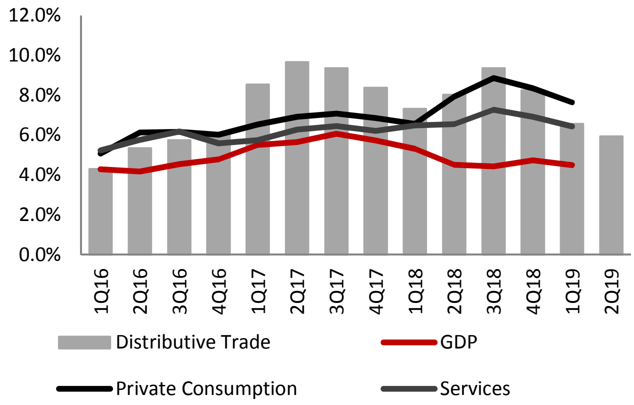
Distributive trade growth at 4-month high. Distributive trade grew by 6.8%yoy (Apr-19: 5.6%yoy) to a new record high of RM110.8b in May-19 as all three components registered higher growth compared to the previous month. Wholesale and retail sales expanded by 5.5%yoy and 7.8%yoy respectively, the highest growth since Feb-19. Motor vehicles sales soared to a 9-month high of 9.1%yoy mainly due to OPR cut effects. In line, loan approved for transport vehicles and passenger car surged to a 9-month high of 19.6%yoy and 16.7%yoy respectively. Looking ahead, we foresee domestic demand to continue increasing in upcoming months buoyed by the OPR cut, stable job market, wage growth and low inflationary pressure.

Chart 9: Distributive Trade, DT (YoY%)



Source: CEIC; MIDFR

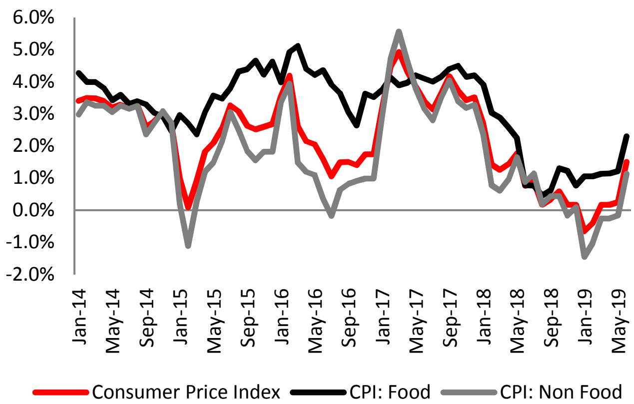
Chart 10: DT vs Private Consumption vs Services (YoY%)



Source: CEIC; MIDFR

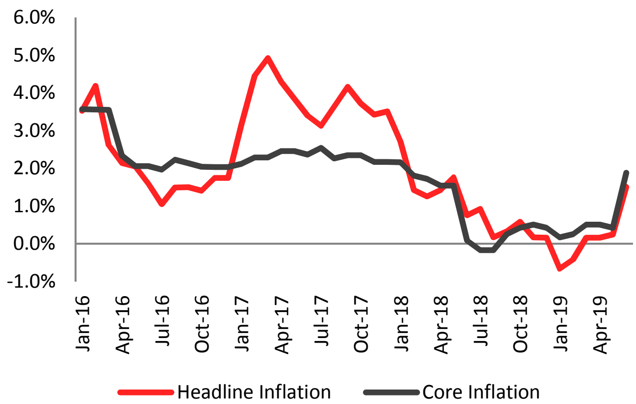
Inflation at 13-month high. Headline inflation accelerated to 1.5%yoy in June-19 from tepid 0.2%yoy in May-19 mainly due to low base effect resulting from the removal of GST last year. On top of that, increasing demand arising from OPR cut and festival season could have also contributed to the increase. The upward pressure continued to come from both food (2.3%yoy vs 1.2%yoy in May-19) and housing & utilities prices (2.3%yoy vs 1.8%yoy) while transport prices continued to drop but at slower pace of -2.1%yoy (May-19: -2.5%yoy). Similar to the headline figure, core inflation surged to 1.9%yoy from 0.4%yoy in the previous month. Looking ahead, inflation is likely to remain high in upcoming months mainly due to the lower base. Nevertheless, RON95 price cap at RM2.08 will continue to downwardly pressure transport inflation.

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



Source: CEIC, MIDFR

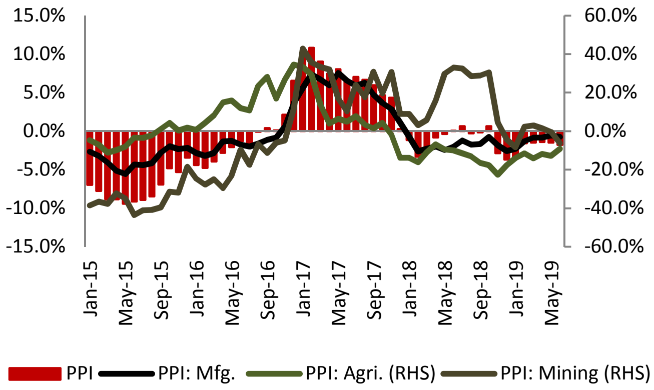
Chart 12: Headline vs Core CPI (YoY%)



Source: CEIC, MIDFR

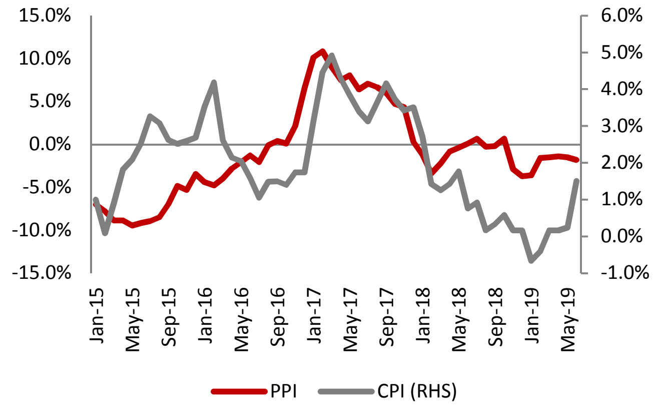
PPI stays on contractionary path. Malaysia's producer cost remains deflationary as PPI shrank by -1.8%yoy in June-19. This is mainly due to higher decrease in input prices of mining and manufacturing sectors. Factory input price have contracted for 18-consecutive months. Manufacturing sector still held 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.

Chart 13: PPI Performance by Sector (YoY%)



Source: CEIC, MIDFR

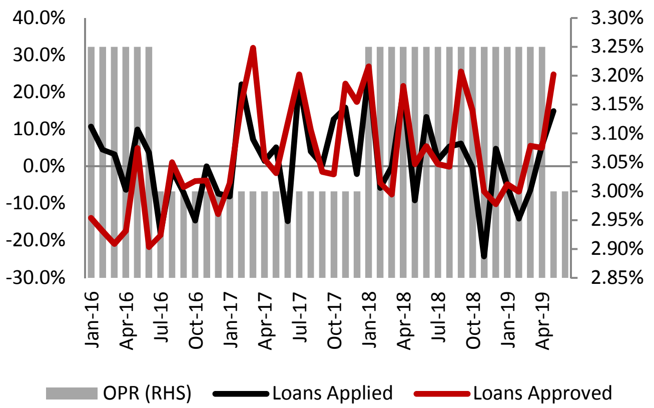
Chart 14: PPI vs CPI (YoY%)



Source: CEIC, MIDFR

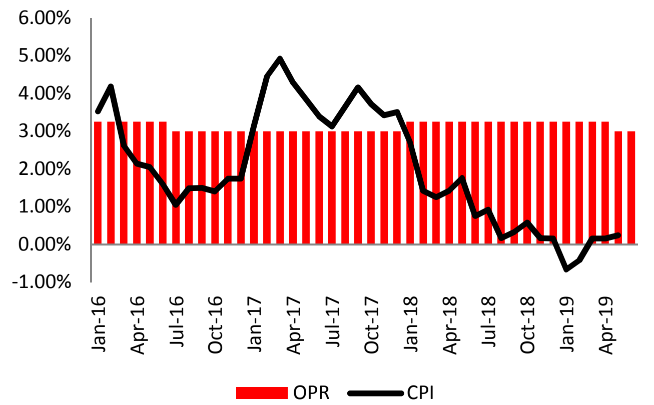
Overnight Policy Rate maintained at 3%. In line with our expectation, the overnight policy rate was left unchanged at 3% by BNM. On external front, Malaysia's external trade performance is recovering as both exports and imports have been growing positively in the latest two months. Fears from US-China trade discord are comforted temporarily as the duo agreed to resume the trade talks from where they left. Domestically, distributive sales continued to expand but at a moderating pace. Nevertheless, economic activities remain solid as current jobless rate still reflects full-employment condition and inflationary pressure stays at low level due to lower retail fuel prices. In addition, the rate cut in May-19 would improve both domestic consumption activities and investment particularly in 2H19. The strong momentum in private consumption and services sector will drive Malaysia's economy into a good position in 2019. Furthermore, leading indicators such as leading index and business tendency survey are pointing towards better growth trajectory in 2H19. We foresee the economy to expand by 4.9% in 2019.

Chart 15: OPR (%) vs Loans Growth (YoY%)



Source: CEIC, MIDFR

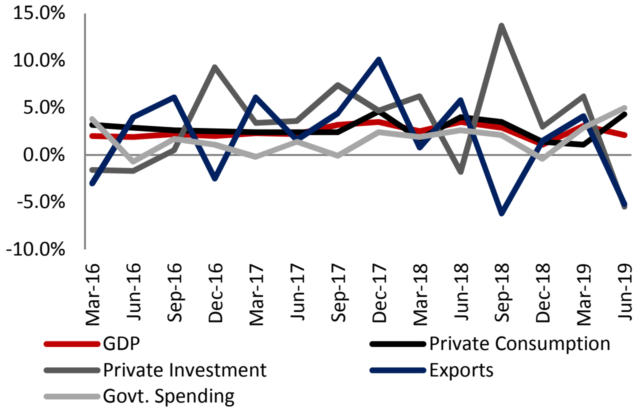
Chart 16: OPR (%) vs CPI (YoY%)



Source: CEIC, MIDFR

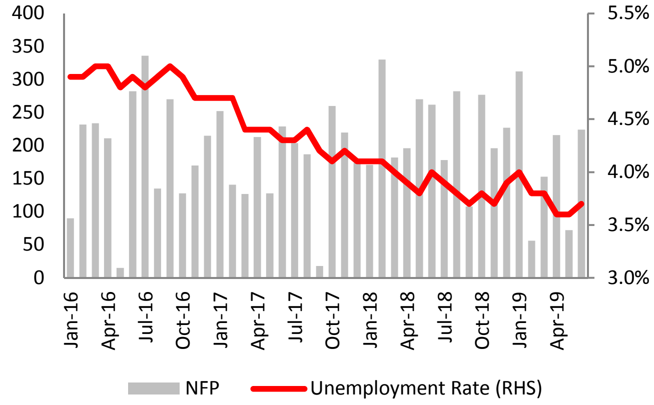
Fed's funds rate lower by 25 basis points. The Fed reduces its key policy rate to 2.00-2.25% during the FOMC meeting in Jul-19. The central bank views the economy is expanding at moderate pace while global uncertainties remain as major downside risks. Cutting the interest rate is expected to impact economic activities in the US particularly household spending and business investment. In addition, it may offset the uncertainties due to global trade tension.

Chart 17: GDP at Annualised Growth (%)



Source: CEIC, MIDFR

Chart 18: Unemployment Rate vs Non-Farm Payroll



Source: CEIC, MIDFR

Table 1: Macroeconomic Data Updates

(YoY%) Unless Stated Otherwise	2016	2017	2018	2019[f]
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	70.0
Crude Palm Oil (Avg)	2642.0	2659.0	2293.0	2090.0
USD/MYR (Avg)	4.14	4.30	4.00	4.12
USD/MYR	4.46	4.08	4.10	4.10
Overnight Policy Rate (%)	3.00	3.00	3.25	3.00

Source: MIDFR

July 2019 Key Economic Events

1 July: Trump says he agreed with Xi to hold off on new tariffs and to let Huawei buy US products. U.S. President Donald Trump and Chinese President Xi Jinping agreed on Saturday to proceed with negotiations after a series of escalations to their nations' trade war threatened to disrupt the global economy. On the sidelines of the Group of 20 summit in Osaka, Japan, the two leaders held a highly anticipated meeting, which Chinese media outlets reported ultimately took about 80 minutes.

2 July: E.U. Nominates Two Women for Top Jobs as Bloc's Unity Is Tested. After grueling and bitter negotiations, the European Union on Tuesday finally decided on the heads of its key institutions, making history by putting forward two women for the most important jobs at a moment when the bloc's unity is being tested as never before. After the sort of exhausting, grinding process for which the bloc is now infamous, European leaders nominated two conservatives, the German defense minister, Ursula von der Leyen, as Commission president, and the French head of the International Monetary Fund, Christine Lagarde, as head of the European Central Bank.

9 July: Japan rejects S. Korea's offer to hold talks to resolve export curbs. Japan on Tuesday rejected South Korea's call for negotiations to resolve a row over Tokyo's export restrictions against the South, saying it has no intention of lifting the curbs and the issue is not a matter of talks. Trade Minister Hiroshige Seko made the remark after a Cabinet meeting, a day after South Korean President Moon Jae-in urged Japan to retract the restrictions on exports of key materials to the South and called for negotiations to resolve the issue.

15 July: China's economic growth slumps to lowest in 27 years as the trade war hits. China's economic growth has slumped to its lowest level in nearly three decades as the world's second largest economy feels the effects of a prolonged trade war with the United States. The country's gross domestic product grew at 6.2% in the quarter ended June, the slowest quarterly growth rate since 1992 and down from 6.4% in the previous quarter, according to government figures released on Monday.

25 July: Boris Johnson appointed UK's new prime minister. Boris Johnson has been appointed as the new prime minister of the United Kingdom after Theresa May stood down over her failure to lead Britain out of the European Union. Johnson, 55, was appointed to the premiership by Queen Elizabeth II in a formal meeting at Buckingham Palace on Wednesday.

26 July: US economic growth cools to 2.1% in second quarter. US economic growth cooled to a rate of 2.1 per cent in the second quarter, supporting the Federal Reserve's move towards a historic one-notch cut in its main interest rate at a pivotal policy meeting next week. The slowdown in US gross domestic product growth was significant compared with the 3.1 per cent pace of expansion in the first quarter of the year. However, the decline was not as deep as economists were expecting. The report's components showed that strength in US consumer spending was sustaining the expansion even as businesses curtailed their investments.

27 July: Huawei's China smartphone market share jumps as rivals lose ground. Huawei Technologies extended its lead in a declining China smartphone market in the second quarter, with its market share rising to 38% as all other top vendors lost ground, according to data from market research firm Canalys. Huawei, which was put on a trade blacklist by the United States since mid-May, shipped 37.3 million smartphones in China in the second quarter, up 31% year-on-year, according to Canalys. Its market share rose more than 10 percentage points from the year-ago quarter's 27.6%.

31 July: Fed cuts interest rates, signals it may not need to do more. The Federal Reserve cut interest rates on Wednesday, but the head of the U.S. central bank said the move might not be the start of a lengthy campaign to shore up the economy against risks including global weakness. Fed Chairman Jerome Powell cited signs of a global slowdown, simmering U.S. trade tensions and a desire to boost too-low inflation in explaining the central bank's decision to lower borrowing costs for the first time since 2008 and move up plans to stop winnowing its massive bond holdings.

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