

ECONOMIC REVIEW | 2019 Minimum Wage**Higher Minimum Wage to Boost Domestic Economy Without Burdening Businesses**

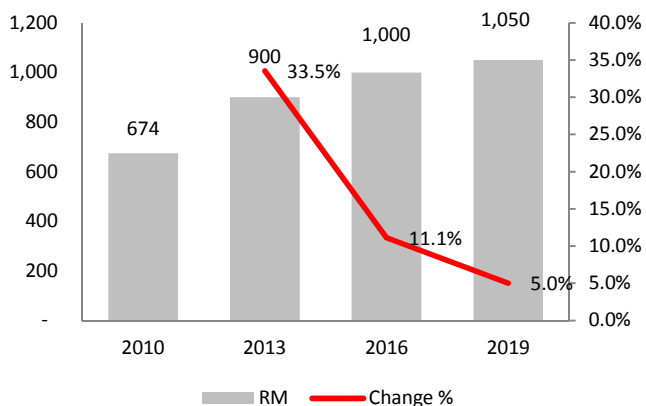
- *Gradual rise in the national minimum wage will have positive impacts on Malaysia's economic activities. Based on latest data, median salary for Malaysian is RM2,016 per month with increment of 4.2% (Inflation-adjusted) in 2017. We believe the decision to equalize the wage between Peninsular Malaysia and Sabah & Sarawak will reduce income gap between the two regions.*
- *Minimal effects on business activities. The percentage changes of minimum wage for both Peninsular Malaysia and Sabah & Sarawak are lower than the previous two revisions to the minimum wage levels. For instance, minimum wage growth of 2016 as compared to 2013 for Peninsular Malaysia and Sabah & Sarawak are 11.1% and 15% respectively.*
- *Nominal wage growth is expected to improve by 5.3% in 2018. We expect inflation to average at 1.3% this year which is mainly driven by unfavorable base effects, zero-rated GST and stabilized retail fuel prices. As inflationary pressure remains steady, we anticipate this will translate into improve labor market which unemployment rate is projected to be at 3.3%.*

Macroeconomic Analysis

Gradual rise in the national minimum wage will have positive impacts on Malaysia's economic activities. Based on latest data, median salary for Malaysian is RM2,016 per month with increment of 4.2% (Inflation-adjusted) in 2017. We believe the decision to equalize the wage between Peninsular Malaysia and Sabah & Sarawak will reduce income gap between the two regions. Comparatively in 2017, average median salary for Peninsular Malaysia is RM2,015 while Sabah & Sarawak are RM1,782. This translates to about 13% gap between median wage for Peninsular and East Malaysia.

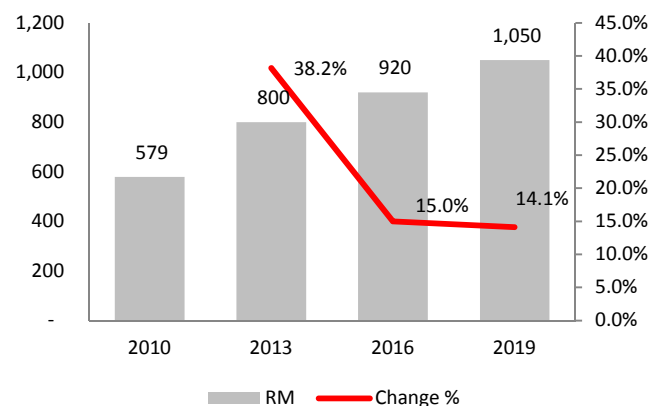
Minimal effects on business activities. The percentage changes of minimum wage for both Peninsular Malaysia and Sabah & Sarawak are lower than the previous two revisions to the minimum wage levels. For instance, minimum wage growth of 2016 as compared to 2013 for Peninsular Malaysia and Sabah & Sarawak are 11.1% and 15% respectively. Comparatively, the 2019 minimum wage sees 5% and 14.1% uplift for Peninsular Malaysia and Sabah & Sarawak. Therefore, we opine the new minimum wage level has trivial impacts toward business activities in Malaysia via changes in cost structure.

Chart 1: Minimum Wage for Peninsular Malaysia



Source: CEIC, MIDFR

Chart 2: Minimum Wage for Sabah & Sarawak



Source: CEIC, MIDFR

Overall wage growth registered at 4.2% in 2017. Malaysia's median wage grew on nominal term by 8% to RM2,160 last year. The growth in the wage is in tandem with solid expansion in domestic economy in 2017. Stellar performance of external trade activities, thus lead to positive spillover effects throughout the overall economic activities including improvement in income level. Moving forward, we foresee wage growth to stay on upward trajectories due to steady upbeat momentum in global trade activities, gradual recovery in crude oil prices and supportive economic policies. The recent increase and equalization in the 2019 new minimum wage will lend further support on steady overall wage growth in Malaysia in the short and long terms. We view there would not be sharp rise of RM500 over a year. The increment is expected to take place gradually over the next 5 years.

High inflation pinches wage growth. Despite of solid 8% growth, the real or inflation-adjusted wage growth is 4.2% due to inflationary effects. Among others, modest pick-up in global commodity prices and the introduction of weekly changes in retail fuel prices are major factors contributing to the rise in overall prices in Malaysia last year. Looking ahead, the governments, among its promises are to stabilize fuel prices and implementing a new tax regime in the form of SST. This development is expected to cause inflation to moderate in 2018. We expect headline inflation to average 1.3% this year. The moderating inflationary pressure will support real wage growth to remain stable above 5%.

Table 1: Malaysia – Summary of Salaries & Wages Growth (%)

	2012	2013	2014	2015	2016	2017
Median (RM)	1,450	1,700	1,800	1,942	2,000	2,160
Nominal Growth	9.8	3.4	5.9	7.9	3.0	8.0
Inflation Rate	1.7	2.1	3.1	2.1	2.1	3.8
Real Growth	8.2	1.3	2.8	5.8	0.9	4.2

Source: DOSM; MIDFR

*Wage Growth is Inflation-Adjusted Growth

Expected solid wage expansion in Sabah & Sarawak. Equalization of minimum wage across all states in 2019 will boost wage growth in Sabah & Sarawak particularly. In 2017, Melaka emerges as the state with the highest wage growth, 17.6% while Johor recorded the lowest at -2.1%. This is in line with the fact that Melaka remains as the state with the lowest youth unemployment rate for 7-consecutive years since 2011. Although the state inflation is among the highest, it is neutralized with the high wage growth. Nevertheless, there are 4 states that recorded double digit growth last year namely Melaka, Sarawak, Pahang and Terengganu. Overall, wage growth across all states registered better performances as compared to the previous year, 2016 in which only Kelantan recorded double digit growth.

New economic policies to benefit various stages. As mentioned earlier, new scale for national minimum wage as promised by the government will benefit employees across all states in Malaysia for the next 4-5 years. In addition, accommodative tax policies and stable fuel prices would provide extra rooms for businesses to invest and expand its business activities from low to high-value stages. Under the same manifesto, the new government promised to prioritize local workers and reduce the number of foreign workers. Consequently, we expect a solid increase in employment of medium and high-skilled workers as well as bright prospects for continuous solid wage growth in 2018 and in the long terms.

Table 2: Wage Level and Wage Growth by States

	Wage Level (RM)			Wage Growth (%)		
	2015	2016	2017	2015	2016	2017
Johor	2,200	2,200	2,250	7.2	(2.8)	(2.1)
Kedah	1,400	1,510	1,650	6.0	6.1	5.2
Kelantan	1,200	1,345	1,500	13.6	10.5	8.0
Kuala Lumpur	2,500	2,500	2,650	(2.8)	(2.8)	2.2
Melaka	1,600	1,760	2,145	(5.6)	8.0	17.6
Negeri Sembilan	1,950	2,060	2,170	5.9	3.6	1.1
Pahang	1,620	1,650	1,870	0.6	0.0	10.2
Penang	1,900	2,000	2,160	3.1	2.8	3.9
Perak	1,500	1,650	1,700	2.5	8.6	(0.3)
Perlis	1,495	1,630	1,800	9.0	7.3	6.4
Sabah	1,480	1,600	1,763	4.6	7.7	7.1
Sarawak	1,450	1,500	1,800	2.2	1.9	17.0
Selangor	2,500	2,500	2,580	11.2	(2.3)	(0.7)
Terengganu	1,500	1,500	1,700	18.5	(1.5)	10.2

Source: DOSM; MIDFR

*Wage Growth is Inflation-Adjusted Growth

Wage level between urban and rural widest ever recorded. Based on the latest wages and salaries survey 2017, the wage difference between urban and rural is RM860. For 2-consecutive years, urban's wage growth has outpaced rural. The huge difference is partly contributed by tepid growth in rural's wage. Plus, relatively low employment growth in sectors like agriculture and government services contribute towards the dragging rural's wage level.

Table 3: Wage Level and Wage Growth by Strata

	Wage Level (RM)			Wage Growth (%)		
	2015	2016	2017	2015	2016	2017
Urban	2,000	2,115	2,260	(2.1)	3.7	3.1
Rural	1,300	1,350	1,400	6.2	1.7	(0.1)

Source: DOSM; MIDFR

*Wage Growth is Inflation-Adjusted Growth

Table 4: Wage Level and Wage Growth by Age Group

	Wage Level (RM)			Wage Growth (%)		
	2015	2016	2017	2015	2016	2017
15–19	900	900	1,180	(2.1)	(2.1)	27.3
20–24	1,200	1,200	1,400	(2.1)	(2.1)	12.9
25–29	1,800	1,865	2,000	3.8	1.5	3.4
30–34	2,180	2,230	2,365	6.9	0.2	2.3
35–39	2,350	2,500	2,500	4.1	4.3	(3.8)
40–44	2,470	2,500	2,600	7.1	(0.9)	0.2
45–49	2,500	2,500	2,500	6.6	(2.1)	(3.8)
50–54	2,500	2,600	2,750	(2.1)	1.9	2.0
55–59	2,500	2,600	2,845	16.9	1.9	5.6
60–64	1,400	1,500	1,800	9.0	5.0	16.2

Source: DOSM; MIDFR

*Wage Growth is Inflation-Adjusted Growth

Table 5: Wage Level and Wage Growth by Education

	Wage Level (RM)			Wage Growth (%)		
	2015	2016	2017	2015	2016	2017
No Formal Education	900	960	1,100	3.8	4.6	10.8
Primary	1,110	1,206	1,400	(1.2)	6.5	12.3
Secondary	1,500	1,650	1,750	(2.1)	7.9	2.3
Tertiary	3,090	3,300	3,400	0.9	4.7	(0.8)

Source: DOSM; MIDFR

*Wage Growth is Inflation-Adjusted Growth

Table 6: Wage Level and Wage Growth by Occupation

	Wage Level (RM)			Wage Growth (%)		
	2015	2016	2017	2015	2016	2017
Managers	5,300	5,450	5,800	3.9	0.7	2.6
Professionals	4,200	4,400	4,467	2.9	2.7	(2.3)
Technicians & Associate Professionals	2,720	2,784	2,840	1.9	0.3	(1.8)
Clerical Support Workers	1,900	2,000	2,000	3.5	3.2	(3.8)
Service & Sales Workers	1,300	1,300	1,600	6.2	(2.1)	19.3
Skilled Agricultural, Forestry & Fishery Workers	1,500	1,350	1,450	22.9	(12.1)	3.6
Craft & Related Trade Workers	1,500	1,600	1,650	2.1	4.6	(0.7)
Plant & Machine-Operators & Assemblers	1,500	1,620	1,650	1.3	5.9	(1.9)
Elementary Occupations	1,000	1,050	1,200	(2.1)	2.9	10.5

Source: DOSM; MIDFR

*Wage Growth is Inflation-Adjusted Growth

Positive economic outlook would spur solid wage growth in 2018. Wage growth in manufacturing sector expanded by 1.8% in 2017. As for services sector, wage growth went up by 3.4%. Firmer wage growth in certain sub-sectors such as utilities, wholesale & retail trade activities and transportation & storage activities contributed towards the steady wage growth in overall services sector. Moving forward, we expect wage growth for manufacturing and services sectors to perform better than 2017 given that economic indicators of domestic and global economic activities are showing signs of sustained recovery. Moreover, as exports and industrial productions continue expanding, it is expected to translate into better performance in employment and wage growths especially in manufacturing sector. Added with supportive economic policies and low inflationary pressure, we opine solid wage growth will positively contribute to domestic consumption in 2018.

Nominal wage growth is expected to improve by 5.3% in 2018. We expect inflation to average at 1.3% this year which is mainly driven by unfavorable base effects, zero-rated GST and stabilized retail fuel prices. As inflationary pressure remains steady, we anticipate this will translate into improve labor market which unemployment rate is projected to be at 3.3%. We foresee better job market outlook for the commodity-based sectors given that the commodity prices have been on gradual upward trajectory since late last year, hence more job opportunities will be created in these industries. Strengthening labor market and steady wage growth will boost private consumption and contributed positively to Malaysia's economic performance in 2018.

Table 7: Wage Level and Wage Growth by Sectors

	Wage Level (RM)			Wage Growth (%)		
	2015	2016	2017	2015	2016	2017
Agriculture, forestry and fishing	1,130	1,200	1,350	6.1	4.1	8.7
Mining and quarrying	3,600	3,690	3,700	0.8	0.4	(3.5)
Manufacturing	1,610	1,800	1,900	(7.4)	9.7	1.8
Construction	1,560	1,630	1,900	1.9	2.4	12.8
Services;	2,252	2,411	2,585	2.5	5	3.4
<i>Electricity, gas, steam and air conditioning supply</i>	2,550	3,000	3,150	(0.1)	15.5	1.2
<i>Water supply; sewerage, waste management and remediation activities</i>	1,798	1,650	2,000	10.3	(10.3)	17.4
<i>Wholesale and retail trade; repair of motor vehicles and motorcycles</i>	1,400	1,600	1,650	5.6	12.2	(0.7)
<i>Transportation and storage</i>	1,900	2,000	2,000	3.5	3.2	(3.8)
<i>Accommodation and food and beverage service activities</i>	1,100	1,140	1,500	(2.1)	1.5	27.8
<i>Information and communication</i>	3,000	3,200	3,500	(1.1)	4.6	5.6
<i>Financial and insurance/ takaful activities</i>	3,000	3,070	3,100	(2.1)	0.2	(2.8)
<i>Real estate activities</i>	3,000	3,365	3,400	17.9	10.1	(2.8)
<i>Professional, scientific and technical activities</i>	2,500	2,800	3,000	(2.1)	9.9	3.3
<i>Administrative and support service activities</i>	1,150	1,200	1,350	2.4	2.2	8.7
<i>Public administration and defense: compulsory social security</i>	2,800	3,015	3,160	(2.1)	5.6	1.0
<i>Education</i>	3,990	4,132	4,458	5.3	1.5	4.1
<i>Human health and social work activities</i>	2,550	2,800	3,000	(0.1)	7.7	3.3
<i>Arts, entertainment and recreation</i>	1,544	1,682	1,700	0.8	6.8	(2.7)
<i>Other service activities</i>	1,500	1,510	1,800	5.0	(1.4)	15.4

Source: DOSM; MIDFR

*Wage Growth is Inflation-Adjusted Growth

Sectoral Analysis

Plantation

Impact on plantation sector is minimal as we expect no significant impact on planters' cost. Note that FFB harvesters monthly salary already exceeded RM1,050. FFB harvesters form more than 85% of labors for plantation companies. Net increase in cost is estimated to be between 1% to 1.5% for FY19. We maintain our **NEUTRAL** on the sector with average CPO price of RM2400 for 2018. Buy calls on **KLK (TP: RM27.38)** and **GENP (TP: RM10.70)** are maintained.

Small and Medium Enterprises

We are slightly positive on this news as the quantum in wage increase for Peninsular is only 5%, which should be manageable for business owners. The impact on cost of goods sold (COGS) for manufacturers with main operations in Peninsular are expected to be minimal, ranging from 0.75% to 1.5%. On the other hand, impact on Sabah and Sarawak manufacturers' COGS are expected at between 2.1% and 4.2%. As the implementation is more than one quarter away, it gives time for businesses to plan and budget so that the rise in operating cost is smoothened out. Overall, we expect minimal impact to company earnings.

Consumer

Minimal impact to earnings. The recent increase in minimum wage is generally negative for the consumer sector. Nonetheless, for large F&B manufacturers such as **Nestlé (Malaysia) Berhad (NEUTRAL, TP: RM132.32)** and **F&N Holdings Berhad (NEUTRAL, TP: RM34.52)**, the increase in minimal wage has minimal impact on the companies' earnings. This stems for the fact that these companies have already paid above the new minimal wage of RM1,050 for most of its staff. In addition, most of the manufacturing sites are in Peninsular Malaysia where the increment from the previous minimal wage is only +5.0%.

Maintain NEUTRAL. As such we are maintaining our **NEUTRAL** stance on the sector. We believe that large F&B manufactures under our coverage are able to absorb the recent hike in minimum wage. This is due to the recent cost savings generated from: (i) reduction in number of staffs as a result of increasing automation at their plants; (ii) leaner operation structure; and (ii) recent decline in raw material prices such as sugar, palm oil and coffee beans.

Glove

Generally negative on the sector but... While the increase in minimum wage in general is negative news for the overall sector, however, the impact on earnings of the gloves manufacturer will be minimal as we note that most of the employees in the gloves manufacturing sectors are already earning more than RM1,050. For employees that falls below the minimum wage requirements, which we estimate to be less than 10% of the total employees, our calculation shows that the impact on earnings to gloves manufacturers will be less than 1%.

...negligible impact on gloves manufacturers. Aside from a minimal impact of less than 1% on the earnings of the gloves manufacturers, the impact of the new minimum wage on the gloves manufacturers is also negligible as the manufacturers will be transferring the increase in production costs to their customers, which has been the industry-wide practice all this while. In general, the labour cost constitutes approximately 12% from the total gloves production cost for the manufacturers.


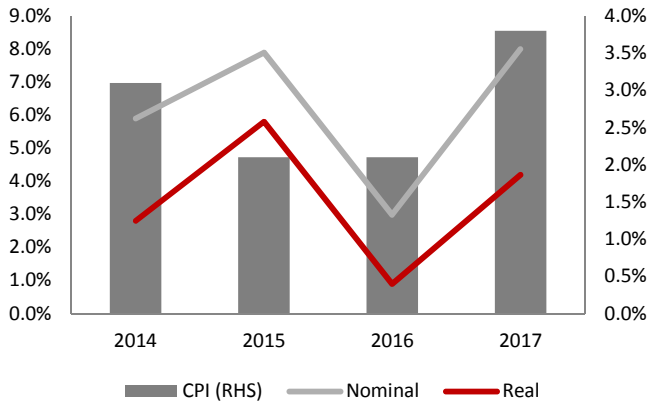
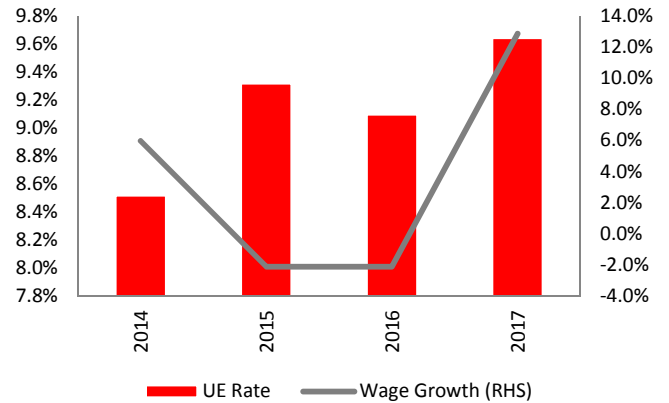
Maintain NEUTRAL. All in, we are maintaining our **NEUTRAL** stance on the sector in view of the capacity constraint due to most manufacturers already operating at a sold out capacity position at this juncture. Furthermore, potential earnings growth of these producers might be capped due to closure of some production lines for upgrades and revamps. Additionally, the sector remains unexciting due to lack of strong re-rating catalyst. 

Chart 3: Wage Growth vs Inflation (YoY%)



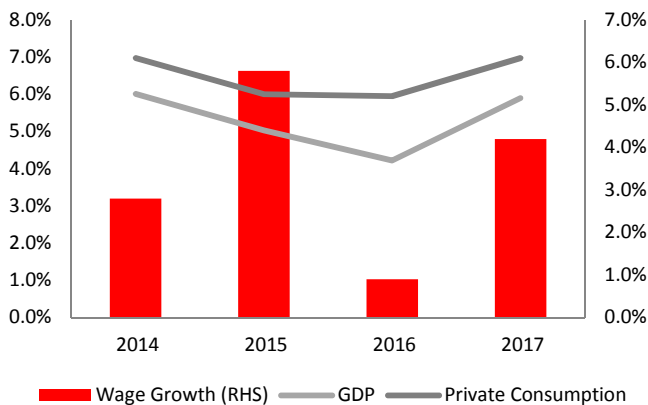
Source: DOSM; MIDFR
*Wage Growth is Inflation-Adjusted Growth

Chart 4: Graduate; Wage Growth (YoY%) vs UE Rate (%)



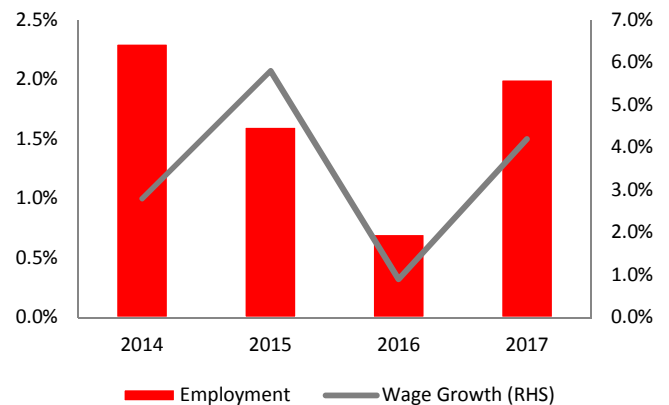
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Chart 5: Wage Growth vs Macro Indicators (YoY%)



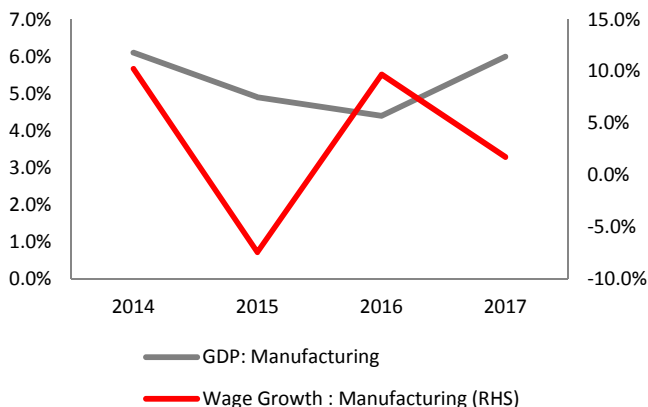
Source: DOSM; MIDFR
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Chart 6: Wage Growth vs Employment Rate (YoY%)



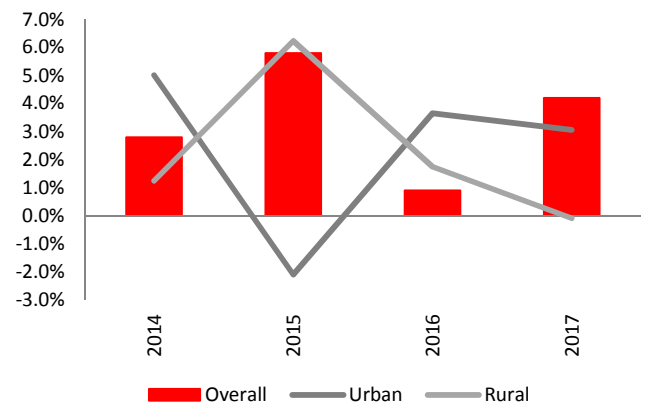
Source: DOSM; MIDFR
*Wage Growth is Inflation-Adjusted Growth

Chart 7: Manufacturing Sector Performance (YoY%)



Source: DOSM; MIDFR
*Wage Growth is Inflation-Adjusted Growth

Chart 8: Overall Real Wage Growth by Strata (YoY%)



Source: DOSM; MIDFR
*Wage Growth is Inflation-Adjusted Growth

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