

## Business Confidence Wanes in 2H18 Due to Lack of Clarity in Policy Directions

- *Slowdown business confidence in 2Q18 expected. According to the latest Business Tendency Survey, overall business performance is expected to continue at moderate pace given that overall business confidence registered at 7.8%, slowest in 3-quarter. The slowdown is predicted mainly due to GE14 factor.*
- *Post-GE14: Policy reforms and impacts. We opine business confidence for the 3-6 months to stay low amid of policy changes and reforms made by the government. The review of mega infrastructure projects and cancellations of HSR and MRT3 will have significant impacts on overall business confidence and also investment flows.*
- *Export-oriented and commodity-based to stay on upward trajectory. Looking ahead, export-oriented sectors are expected to stay on optimistic mood given that economic environments in major and emerging economies remain upbeat.*

**Slowdown business confidence in 2Q18 expected.** According to the latest Business Tendency Survey, overall business performance is expected to continue at moderate pace given that overall business confidence registered at 7.8%, slowest in 3-quarter. The slowdown is predicted mainly due to GE14 factor. The latest election was the most contentious especially with the return of former longest-serving Prime Minister Tun Dr. Mahathir Mohamad against his former party, Barisan Nasional. High level political uncertainties are and low morale among Malaysian consumers in which choked by high cost of living issues and corruption scandals involving political leaders.

**Construction turns pessimistic.** By sector, business confidence in construction sector felt of the cliff to -24.8% post GE14. Construction sector is highly-correlated to political condition as it involves huge government investment on mega infrastructure projects. We can expect further pessimistic mood in the sector with the latest announcement of scrapping off High-Speed Railway Singapore-KL and MRT3. Other mega projects will be review by the newly-elected government. On the other hand, business confidence in manufacturing sector reached highest on record at 19.7% in 2Q18. Despite of global trade war factor, steady global demand and rising commodity prices add support for the sector to stay on uptick direction. On top of that, increase in re-exports activities possibly boost up external trade and manufacturing performances in Malaysia.

**Table 1: Business Confidences by Sector (%)**

	1Q17	2Q17	3Q17	4Q17	1Q18	2Q18
Overall	(6.9)	4.5	11.9	14.0	12.3	7.8
Industry	(2.7)	2.2	3.1	9.8	11.9	9.9
Agriculture	(0.1)	8.7	1.4	25.3	11.8	(3.3)
Mining	(10.7)	(14.3)	16.7	10.0	10.8	(17.9)
Manufacturing	(4.7)	2.4	(3.6)	6.2	10.7	19.7
Electricity and water	27.8	22.7	36.4	4.5	25.8	16.7
Construction	(3.0)	(8.3)	(7.7)	22.8	1.1	(24.8)
Wholesale and retail trade	(11.7)	3.3	20.7	8.3	0.0	7.4
Wholesale trade	(7.1)	7.1	30.5	10.7	1.2	13.5
Retail trade	(17.2)	(3.3)	24.6	3.0	(1.9)	(2.5)
Services	(13.0)	11.3	24.0	23.6	20.6	8.6
Hotels	8.8	25.3	29.4	12.3	26.2	2.7
Transport	8.3	11.8	33.3	14.7	29.9	5.6
Communications	(24.2)	12.8	31.0	26.2	11.5	26.2
Finance	(24.4)	12.8	15.7	31.4	29.4	5.6
Insurance	30.1	33.3	37.5	37.0	21.7	46.0
Real estate	(35.6)	(30.3)	22.2	(8.3)	(27.3)	(52.8)
Information and communications technology	(5.4)	7.4	10.4	11.7	20.4	15.5

Source: CEIC, MIDFR

**Export-oriented and commodity-based to stay on upward trajectory.** Looking ahead, export-oriented sectors are expected to stay on optimistic mood given that economic environments in major and emerging economies remain upbeat. For instance, underpinned by robust industrial activity in the US, jobless rate went down to 18-year low at 3.9% in Apr-18. As in China, consumer confidence has been hovering above 120 points for 7-consecutive months since Oct-17, a level not yet seen since 1993. On the other hand, further recovery in global commodity prices is positive for commodity-based sectors especially via external trade and investment. Brent oil price as mostly referred averaged at \$77 in May-18, the highest since Nov-14.

**Post-GE14: Policy reforms and impacts.** We opine business confidence for the 3-6 months to stay low amid of policy changes and reforms made by the government. The review of mega infrastructure projects and cancellations of HSR and MRT3 will have significant impacts on overall business confidence and also investment flows. We predict business confidence will come back strong in 3Q18 once the National Budget 2019 tabled in Oct-18 and followed with the Mid-Term Review of the 11th Malaysia Plan: New Direction 2018-2020 by year-end. As mentioned by the Minister of Economic Affairs, the new economic direction will be focus on free market and investor-friendly as well as ensuring a humanitarian economy.

**Economic outlook for 2H18 stays healthy.** Referring to business expectations for the next 6 months, overall business performance is expected to grow at tepid pace. Overall business performance for 2Q-3Q18 is expected to experience slight slowdown especially dragged down by construction and mining sectors. Poor confidence in mining sector is possibly due to volatility in commodity prices. On different note, we project services and wholesale & retail trade sectors to be on upside, thanks to the zero-rated GST and tax holiday period till SST implementation in Sep-18.

**Table 2: Business Expectations for Next 6-Month by Sector (%)**

	1Q17-2Q17	2Q17-3Q17	3Q17-4Q17	4Q17-1Q18	1Q18-2Q18	2Q18-3Q18
Overall	3.5	11.5	21.0	29.9	17.1	4.4
Industry	8.8	11.8	22.1	30.2	15.4	(0.3)
Agriculture	11.5	13.0	25.0	32.0	8.7	0.0
Mining	(14.3)	(14.3)	6.7	20.0	6.7	(14.3)
Manufacturing	8.0	12.4	23.7	33.6	18.0	4.0
Electricity and water	63.6	63.6	36.4	18.2	27.3	(8.3)
Construction	(5.6)	13.9	18.6	24.0	17.4	(26.6)
Wholesale and retail trade	(11.8)	10.0	13.4	26.1	7.5	9.5
Wholesale trade	(8.7)	14.3	19.5	26.0	6.2	21.9
Retail trade	(15.5)	2.5	8.7	25.0	9.3	(9.3)
Services	2.1	11.4	22.8	32.1	25.0	15.3
Hotels	2.9	20.7	29.4	36.9	25.0	10.8
Transport	37.5	23.5	32.0	48.0	45.5	25.0
Communications	(27.3)	23.1	42.9	42.9	28.6	14.3
Finance	(6.7)	0.0	11.8	23.5	23.5	16.6
Insurance	55.6	62.5	25.0	33.3	33.3	55.6
Real estate	(30.0)	(45.5)	8.3	8.3	(27.3)	(50.0)
Information and communications technology	18.8	11.1	25.0	45.0	25.0	5.0

Source: CEIC, MIDFR

**Upbeat manufacturing activity in the US.** Flash US manufacturing PMI rose to almost 3.5-year high at 56.6 points in May-18. Services PMI touched 55.7 points, highest in 3-month. Among others, the strong rise is driven by the tax cuts, strong domestic demand and receding global trade war effects. Apart from the US, flash manufacturing PMI for Euro Area and Japan maintain above 50 points in May-18. Hence, we opine global demand derived from advanced economies to remain sanguine for 2H18 and indirectly will affect Malaysia's external trade performance this year. We firm with our forecast Malaysia's exports growth at 9.3% in 2018.

**Regional PMI indicates promising outlook.** Business confidences in emerging economies as well as Asean have been on uptick trends since mid-2016. Latest Apr-18, manufacturing PMI for emerging economies remains above expansion line for 22-consecutive months while major Asean economies except Thailand and Malaysia registered above 50 points. Therefore, we foresee regional demand in 2H18 stays on intact and solid, thus will support expanding regional as well as global trade activities. The declining trend in Malaysia's PMI is mainly due to pre-GE14 factor. We expect the PMI figure to improve after GE14 amid of zero-rated GST, stable retail fuel price and stable global demand.

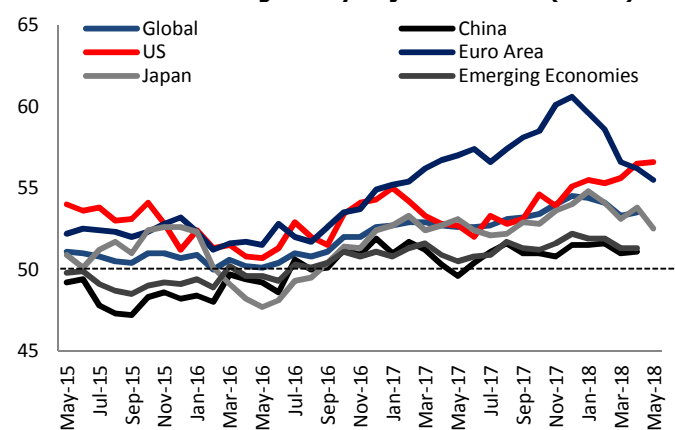
**Table 3: Manufacturing PMI by Selected Economies (Points)**

	Oct-17	Nov-17	Dec-17	Jan-18	Feb-18	Mar-18	Apr-18
Global	53.4	54.0	54.5	54.4	54.1	53.4	53.5
China	51.0	50.8	51.5	51.5	51.6	51.0	51.1
US	54.6	53.9	55.1	55.5	55.3	55.6	56.5
Euro Area	58.5	60.1	60.6	59.6	58.6	56.6	56.2
Japan	52.8	53.6	54.0	54.8	54.1	53.1	53.8
Emerging Economies	51.2	51.6	52.2	51.9	51.9	51.3	51.3
Malaysia	48.6	52.0	49.9	50.5	49.9	49.5	48.6
Indonesia	50.1	50.4	49.3	49.9	51.4	50.7	51.6
Thailand	49.8	50.0	50.4	50.6	50.9	49.1	49.5
Philippines	53.7	54.8	54.2	51.7	50.8	51.5	52.7
Singapore	54.2	55.4	52.1	53.6	55.3	53.7	53.7

Source: Bloomberg, MIDFR

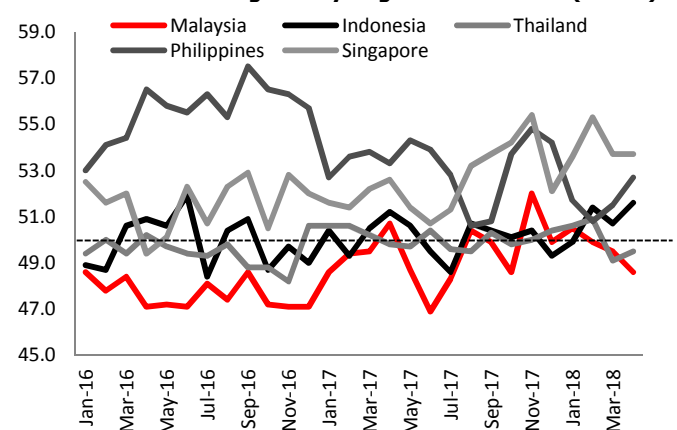
\*Above 50: Expansion Line, Below 50: Contraction Line

**Chart 1: Manufacturing PMI by Major Economies (Points)**




Source: Bloomberg, MIDFR

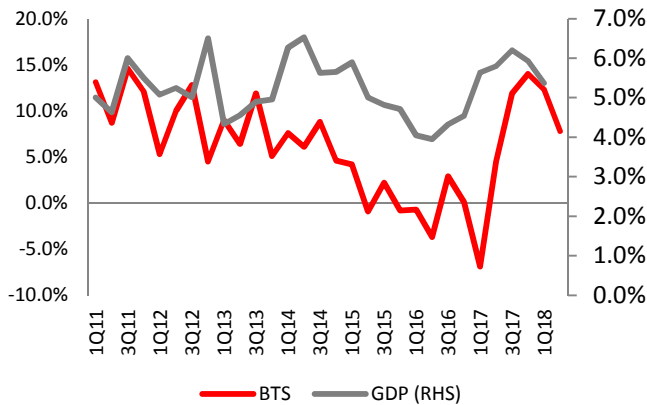
**Chart 2: Manufacturing PMI by Regional Economies (Points)**



Source: Bloomberg, MIDFR

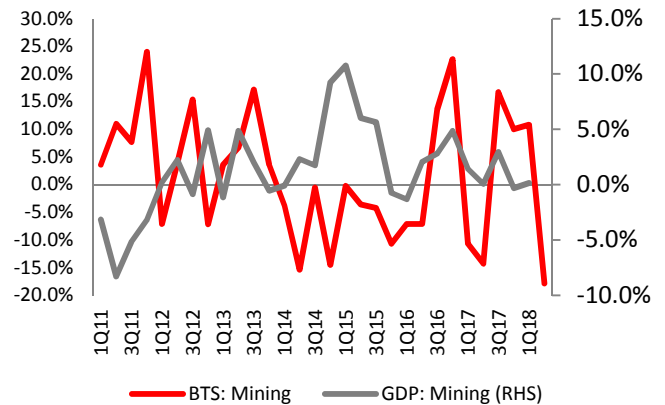
**We maintain our GDP forecast at 5.5% in 2018.** Amid steady business confidences, we maintain our estimates of Malaysia's economy to grow by 5.5% this year. On external front, we opine continuous upbeat momentum in global trade activity, receding effects of trade war and rising commodity prices are key supporting factors for Malaysia's economy to strive. On a flip side, changes in domestic policies like the zero-rated GST, stable retail fuel prices and possible tolls abolishment would support business activity in the medium term. 

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



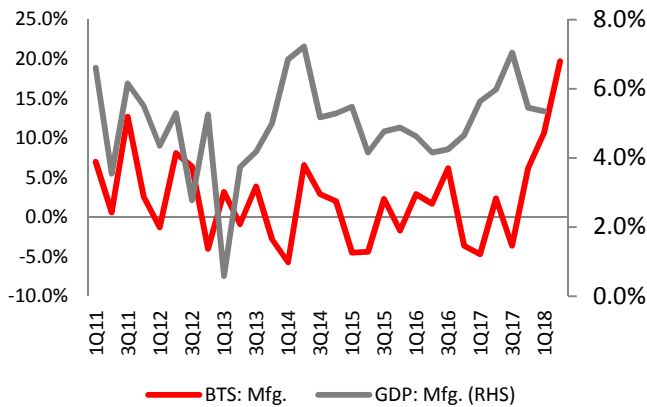
Source: CEIC, MIDFR

**Chart 4: Mining & Quarrying: BTS (%) vs GDP (YoY%)**



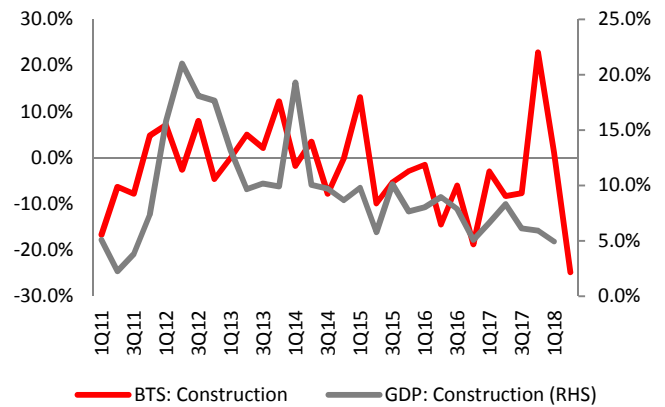
Source: CEIC, MIDFR

**Chart 5: Manufacturing: BTS (%) vs GDP (YoY%)**



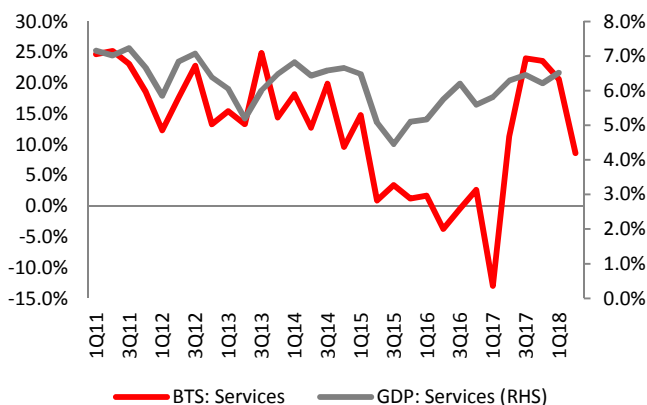
Source: CEIC, MIDFR

**Chart 6: Construction: BTS (%) vs GDP (YoY%)**



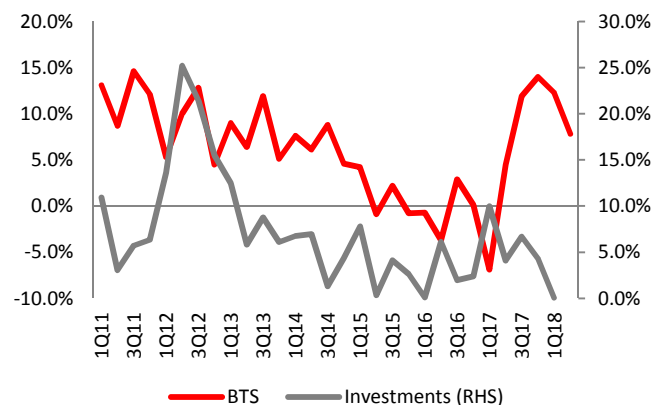
Source: CEIC, MIDFR

**Chart 7: Services: BTS (%) vs GDP (YoY%)**



Source: CEIC, MIDFR

**Chart 8: BTS (%) vs Private Investment (YoY%)**



Source: CEIC, MIDFR

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