1 August 2018

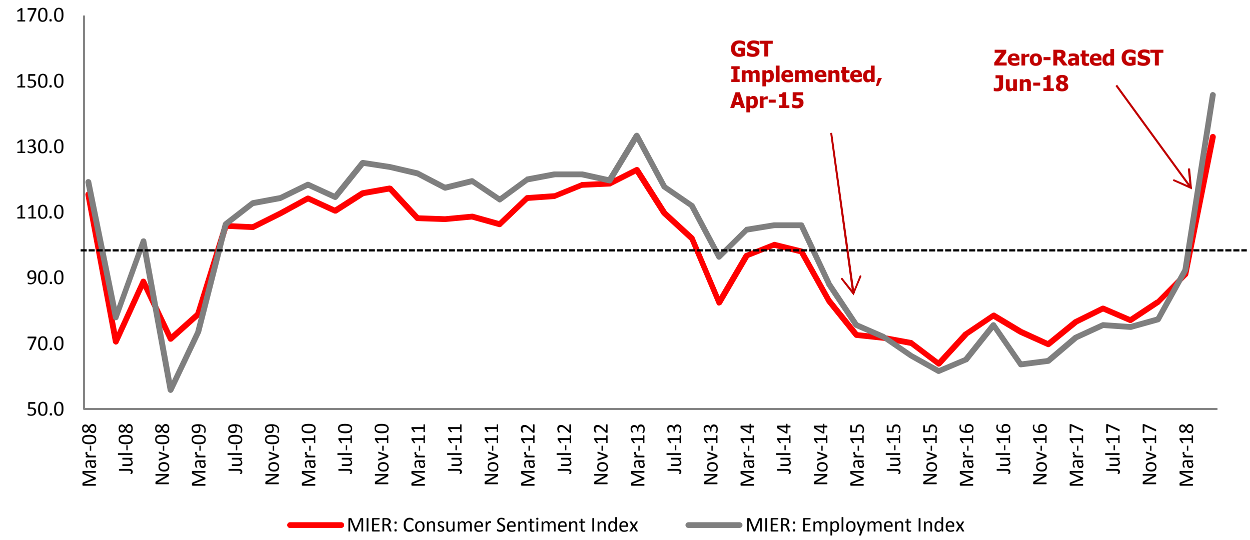
MONTHLY ECONOMIC REVIEW | July 2018

Sentiments Surge as Domestic Economy Remains Resilient Amid Trade Tensions

- *Consumer sentiment turns optimistic after 4-year. Since mid-14, consumer sentiment in Malaysia has been below optimistic level of 100 points. As a result of GE14, the PH government cancelled the GST, along with sound macroeconomic environment, push up the sentiment to optimistic level at 132.9 point, highest in 21-year.*
- *Distributive trade sales hit above RM100b again. Distributive trade rose by 7.0%yoy to RM103.7b in May-18 lifted by retail trade which expanded by 9.3%yoy to RM40.9.*
- *Inflation tumbled to 40-month low. Headline inflation rate slowed to 0.8%yoy in Jun-18, the lowest since Mar-15 mainly attributed to the three months tax holiday period which kicked off in Jun-18.*

Consumer sentiment turns optimistic after 4-year. Since mid-14, consumer sentiment in Malaysia has been below optimistic level of 100 points. Main reasons were the effects of 2014's global oil-plunge and subsidy rationalization program. The impacts of GST to pressure down the sentiment for short period of time only. The sentiment is mainly dragged by slowdown in economic growth. As a result of GE14, the PH government cancelled the GST, along with sound macroeconomic environment, push up the sentiment to optimistic level at 132.9 point, highest in 21-year. Furthermore, a survey conducted by Nielsen Malaysia showed 82% of Malaysian consumers are optimistic about the country's economic outlook and perceive the zero-rated GST will benefit consumers. Apart from GST, stable retail fuel prices will keep inflationary pressure at low level and thus supporting domestic demand.

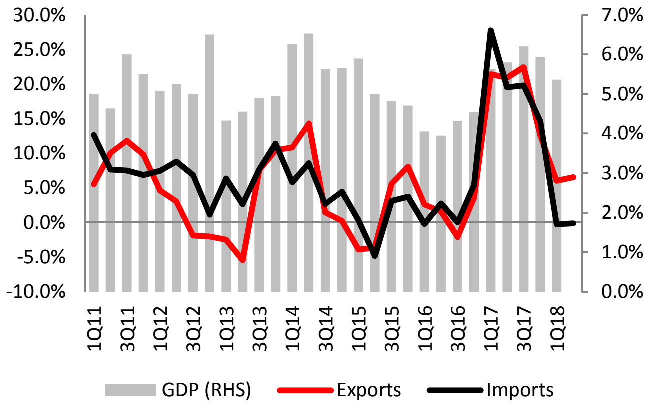
Chart 1: MIER's Consumer Sentiment (Points)



Source: CEIC, MIDFR
*Note: 100 Points is Threshold Line: Above is Optimistic, Below is Pessimistic

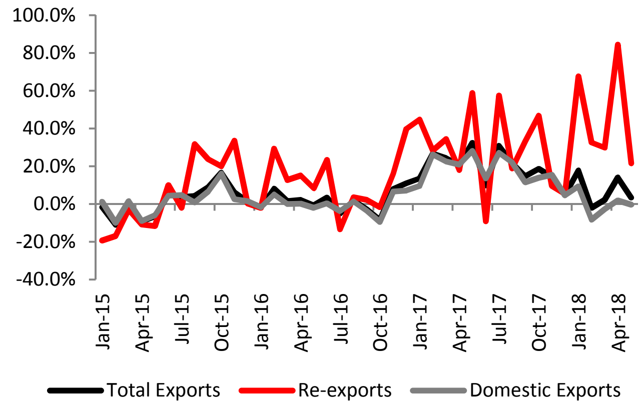
Exports growth slowed to single digit again. Exports expanded by 3.4%yoy to RM82.1b in May-18, following a double digit growth in the preceding month. Slowdown in exports was mainly due to continuous and larger contraction in agriculture goods (-21.9%yoy). However, manufactured and mining goods continue to expand by 3.2%yoy and 40%yoy respectively. Meanwhile, imports still booked a growth however at a tepid pace of 0.1%yoy during the same month. Exports growth continued to outperform imports for the fifth consecutive month, resulting in a trade surplus of RM8.1b. Moving forward, Malaysia's export performance will maintain on upbeat momentum in upcoming months amid of zero-rated GST, tax holiday period till SST implementation in Sep-18 and stable retail fuel price which will support our exports as it will reduce business cost and eventually increase competitiveness. In fact, slowdown in May's exports growth could be due to hold back in purchases by foreign countries in order to enjoy the spillover benefits of tax holiday starting June-18. Nevertheless, protectionism threats remain a concern to the economy.

Chart 2: External Trade vs GDP (YoY%)



Source: CEIC, MIDFR

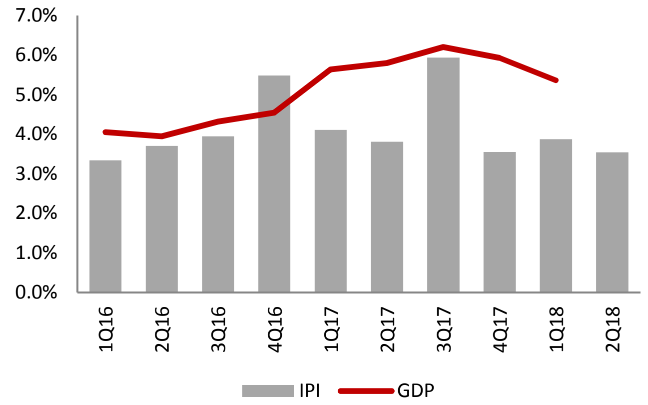
Chart 3: Total Exports: Domestic vs Re-exports (YoY%)



Source: CEIC; MIDFR

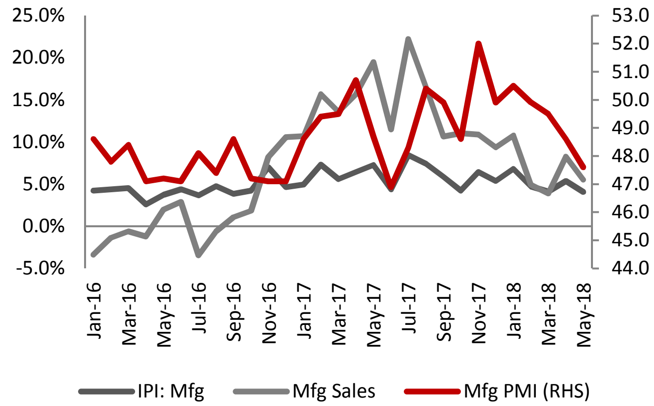
IPI meets market estimates. Malaysia's industrial production expands by 3%yoy in May-18, matched with market expectations and slightly above our forecast of 2.7%yoy. By major components, manufacturing and electricity outputs up by 4.1%yoy and 2.6%yoy respectively while mining contracted by -0.4%yoy. The moderating pace is mainly due to GE14 factor. Business uncertainties and extra holidays amid of the election caused IPI to increase at a moderate pace. Moving forward, we foresee IPI performances to expand at steady pace for the second half of 2018 amid escalating trade tension, moderating inflation and supportive policy changes for businesses such as tax-holiday and stable retail fuel prices.

Chart 4: IPI vs GDP (YoY%)



Source: CEIC, MIDFR

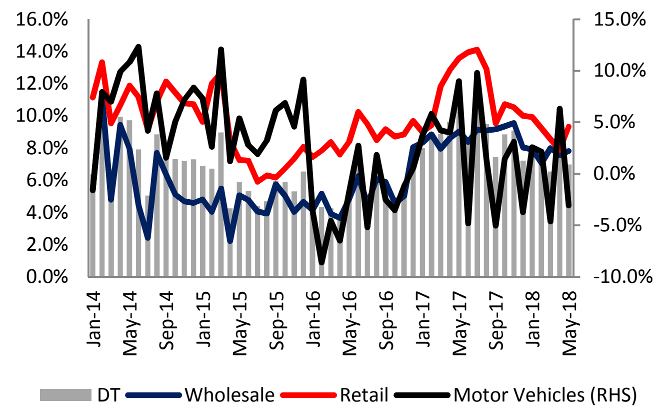
Chart 5: Manufacturing IPI & Sales (YoY%) vs PMI (Points)



Source: CEIC, MIDFR

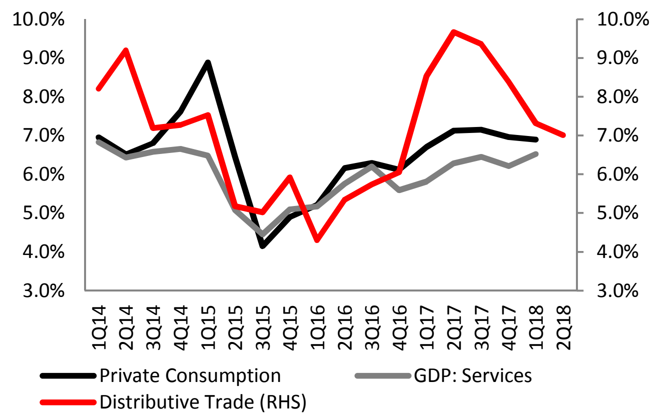
Distributive trade sales hit above RM100b again. Distributive trade rose by 7.0%yoy to RM103.7b in May-18 lifted by retail trade which expanded by 9.3%yoy to RM40.9. Furthermore, wholesale trade grew by 7.8%yoy to RM50.5b, while motor vehicle businesses dropped by 3.1%yoy to RM12.3b. Decline in motor vehicle sales could be due to postpone in spending to June-18 as zero-rated GST takes place. On a monthly basis, all three sectors rebounded from a negative growth recorded in the preceding month. Moving forward, we foresee distributive trade sales to remain on steady momentum underpin by stable job market, zero-rated GST, decelerating inflationary pressure, tourism activities and accommodative economic policies.

Chart 6: Distributive Trade, DT (YoY%)



Source: CEIC; MIDFR

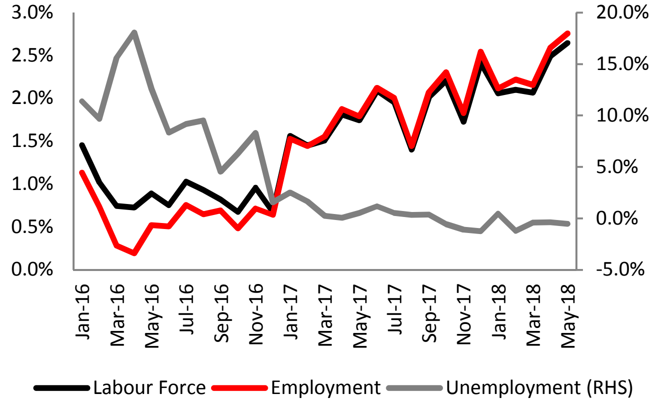
Chart 7: DT vs Private Consumption vs Services (YoY%)



Source: CEIC; MIDFR

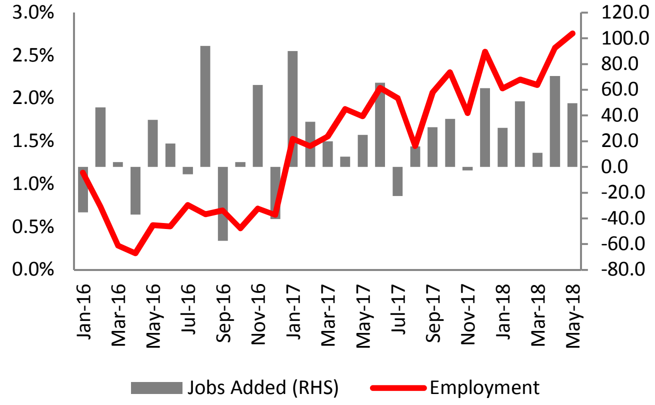
Employment grew at the highest pace ever recorded. Employment increased by 2.8%yoy, highest rate ever recorded to 14.9 million in May-18. Similarly, labour force grew by 2.6%yoy to 15.4 million. Jobs added in the economy registered at 49.5K. Unemployment rate maintains at full-employment condition of 3.3%. So far in 2018, the average expansion rate of both labour force and employment are at record high, 2.3% and 2.4% respectively. As compared to 2017, both labour market indicators rose by 1.8% and 1.9% accordingly. As both domestic and external economic activities are on upbeat momentum, growths in both labour force and employment have been outpacing unemployment growth for the last 15 months since Feb-17.

Chart 8: Labour Market Key Indicators (YoY%)



Source: CEIC; MIDFR

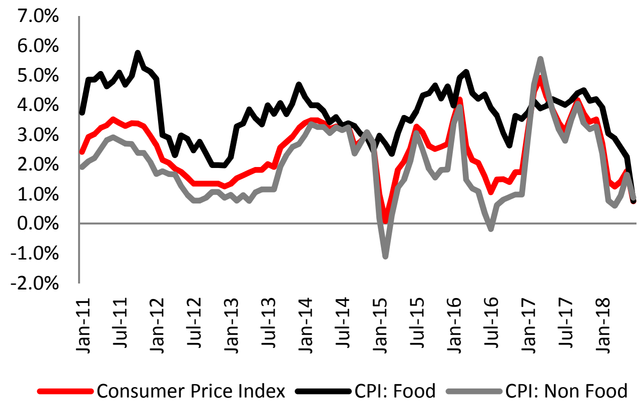
Chart 9: Jobs Added ('000) vs Employment (YoY%)



Source: CEIC; MIDFR

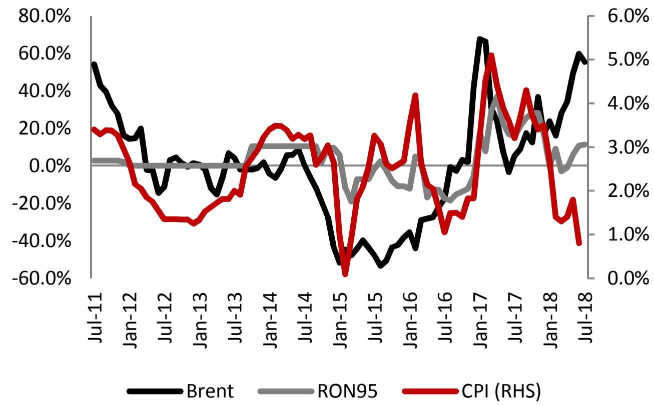
Inflation tumbled to 40-month low. Headline inflation rate slowed to 0.8%yoy in Jun-18, the lowest since Mar-15 mainly attributed to the three months tax holiday period which kicked off in Jun-18. Inflation of food & non-alcoholic beverages slowed significantly to 0.8%yoy from 2.2%yoy recorded in the preceding month. Meanwhile, prices went down sharply for clothing & footwear, communication and recreation services & culture, among others. In contrast, inflation accelerated at a faster pace for transport at 5.5%yoy, second highest so far this year. On monthly basis, inflation contracted by 1.2% in Jun-18. Meanwhile, core inflation is recorded at 0.1%yoy, far lower than 1.5%yoy in a month earlier. Moving forward, Malaysia's inflation is expected to continue to taper down in upcoming months due to higher base effects besides other significant events such as zero-rated GST, tax holiday period until SST implementation in Sep-18 and stable retail fuel price which will reduce business cost.

Chart 10: CPI: Headline vs Food & Non-food (YoY%)



Source: CEIC, MIDFR

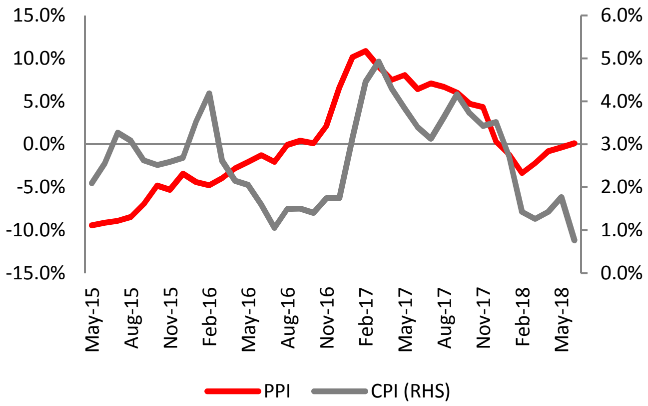
Chart 11: CPI vs Crude & Retail Fuel Prices (YoY%)



Source: CEIC; MIDFR

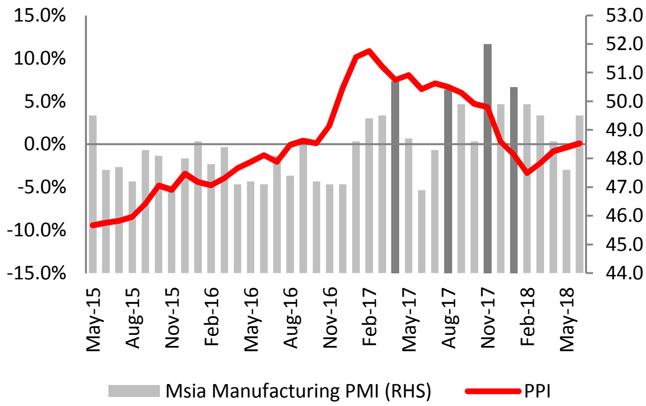
PPI grew for the first time in 2018. Malaysia's producer prices increase by 0.1%yoy in Jun-18. Despite the tepid gain, it is still notable as the first growth for this year after falling for five consecutive months. However, on a monthly basis, PPI contracted by 0.7% following two continuous months of increase. The gain was driven by mining and electricity & gas supply sectors which rose by 33.1%yoy and 1.3%yoy respectively. In contrast, input prices for agriculture, forestry & fishing, manufacturing and food product declined. Looking ahead, we foresee a slowdown in inflationary pressure amid tax-holiday period. On the other hand, rising global commodity prices on top of SST comeback in Sep-18 could induce inflationary pressure which eventually affects domestic inflation.

Chart 12: PPI vs CPI (YoY%)



Source: CEIC, MIDFR

Chart 13: PPI (YoY%) vs Manufacturing PMI (Points)



Source: CEIC, MIDFR

Table 1: Macroeconomic Data Updates

(YoY%) Unless Stated Otherwise	2016	2017e	2018f	1Q18	2Q18f	3Q18f	4Q18f
Real GDP	4.2	5.8	5.5	5.4	5.8	5.4	5.2
Private Consumption	6.1	7.0	6.5	6.9	5.8	6.5	6.8
Public Consumption	1.0	5.0	3.5	0.6	0.4	3.5	9.4
Gross Fixed Capital Formation	2.7	5.7	3.8	0.1	3.3	4.0	8.0
Exports of goods & services	0.1	9.2	5.0	3.7	7.9	3.5	5.0
Imports of goods & services	0.4	10.3	4.8	(1.9)	8.3	5.5	7.3
Net Exports - RMb	92.6	93.4	99.6	29.5	23.8	23.1	23.2
Exports of Goods (f.o.b)	1.1	14.5	9.3	6.0	12.1	8.9	10.1
Imports of Goods (c.i.f)	1.9	15.5	8.2	(0.3)	12.4	9.5	11.4
Trade Balance - RMb	87.2	97.5	119.9	33.4	27.0	29.0	30.5
Consumer Price Index	2.1	3.8	2.6	1.8	2.5	3.0	2.9
Current Account - RMb	29.0	36.6	39.6	-	-	-	-
Current Account - % of GNI	2.7	3.2	3.2	-	-	-	-
Fiscal Balance - % of GDP	(3.1)	(3.0)	(2.9)	-	-	-	-
Federal Government Debt - % of GDP	53.8	53.0	52.5	-	-	-	-
Nominal GDP	6.3	9.9	3.5	-	-	-	-
Year-End of Unless States Otherwise	**2016**	**2017e**	**2018f**	**1Q18**	**2Q18**	**3Q18f**	**4Q18f**
Brent Crude Oil (Avg)	43.6	53.0	70.0	68.4	76.9		
Crude Palm Oil (Avg)	2,652	2,825	2,400	2,480	2,359	-	-
USD/MYR (Avg)	4.15	4.32	4.00	3.92	3.95	4.05	4.00
USD/MYR	4.48	4.15	3.95	-	-	-	-
Yield on generic 10-year MGS (%)	3.85	4.00	4.10	3.95	4.15	4.00	4.05
3-month KLIBOR (%)	3.54	3.43	3.60	3.60	3.50	3.50	3.70
Overnight Policy Rate (%)	3.00	3.00	3.25	3.25	3.25	3.25	3.25

Source: MIDFR

July 2018 Key Economic Events

4 July: China plans income tax cut to boost consumption and reduce inequality. China's parliament has drafted a tax cut that will slash tax for most individuals, as part of the government's efforts to boost consumption and reduce inequality. China is seeking to reduce excessive rates of savings and investment and generate a higher share of growth from household consumption. Economists say that raising post-tax household income is crucial to encouraging consumers to open their wallets.

6 July: Fed on lookout for recession but still sees strong economy: minutes. U.S. central bankers discussed whether recession lurked around the corner and expressed concerns global trade tensions could hit an economy that by most measures looked strong, minutes of the Federal Reserve's last policy meeting on June 12-13 released on Thursday showed. The minutes, which described a meeting in which the Fed raised interest rates for the second time this year, also suggested policymakers might soon signal that the Fed's rate-hiking cycle was advanced enough that policy was no longer boosting or constraining the economy.

11 July: China has its currency to use as a weapon in trade war with Trump. China's currency fell to a near 11-month low against the dollar Wednesday, after the Trump administration fired off a new list of tariffs on $200 billion in Chinese goods. China's currency has been sliding noticeably since mid-June after bumping around at higher levels from February through May. Since June 14, it has lost about 4 percent. China's currency has been a sore point for a number of U.S. administrations, which have blasted China for allowing the renminbi to weaken to help exports. With the escalating trade war, market speculation points to the possibility that China will now use a weaker currency to fight the effect of tariffs.

16 July: SST to be set at 6% for services, 10% for sales. The provision of services will be taxed at 6% under the reintroduced sales and services tax (SST), while the sales of goods will incur a 10% tax, said Finance Minister Lim Guan Eng. He said the SST bill is expected to be passed in August during the current parliamentary seating and would be implemented in September. "The SST will be reintroduced on Sept 1, and bring in a projected revenue of RM4 billion," he said at the launch of the National Tax Conference 2018 here today.

20 July: MIER: Consumer sentiment index soars to 21-year high. Consumer sentiment in Malaysia has turned positive for the first time in four years amid the change in the country's political landscape and zero-rating of the goods and services tax (GST). According to the Malaysian Institute of Economic Research (MIER), the consumer sentiment index (CSI) soared to a 21-year high of 132.9 points during the second quarter of this year. This is the first time the index has breached the 100-point optimism threshold since the second quarter of 2014.

22 July: British reject May's Brexit plan, some turn to Boris and far right: poll. Prime Minister Theresa May's plans to leave the European Union are overwhelmingly opposed by the British public and more than a third of voters would support a new right-wing political party committed to quitting the bloc, according to a new poll.

26 July: Trump relents on EU car tariffs, as U.S.-China fight derails Qualcomm deal. In what the EU chief called a "major concession," U.S. President Donald Trump agreed on Wednesday to refrain from imposing car tariffs while the two sides launch negotiations to cut other trade barriers, easing the threat of a transatlantic trade war.

30 July: Dr M is Khazanah chairman, Azmin made director. Prime Minister Tun Dr Mahathir Mohamad and Economic Affairs Minister Datuk Seri Azmin Ali have been named as Khazanah Nasional Berhad's chairman and director respectively. In a statement released by the Prime Minister's Office on Monday (July 30), Tan Sri Mohd Hassan Marican, Dr Sukhdave Singh and Goh Ching Yin were also named as Khazanah's directors.

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