29 June 2018

ECONOMIC REVIEW | May 2018 Producer Price Index

Subdued Price Pressure Cause PPI to Remain In Negative Territory for Five Consecutive Months

- *Producer price index improves marginally for 2-consecutive months. On yearly basis, Malaysia's producer prices contracted by -0.4%yoy, marked the smallest drop since Jan-18. However, on a monthly basis, PPI went up by 0.3% followed a 0.5% gain in the preceding month.*
- *Low input cost will support industrial activities. With the declining input cost inflation in May-18, we opine this would provide support to industrial and business activities in the coming months. In fact, we noticed retail fuel pump prices have remained unchanged as the newly elected government will retain the price of fuel despite the rise in global crude oil prices.*
- *Producer price index is expected to expand by 3.2% in 2018. Amid unfavourable base effects, we foresee input cost inflation to average at 3.2% this year. We anticipate inflationary pressure from fuel-related items to pick-up at steady speed, in tandem with steady gradual rise in global commodity prices.*

Producer price index improves marginally for 2-consecutive months. On yearly basis, Malaysia's producer prices contracted by -0.4%yoy, marked the smallest drop since Jan-18. However, on a monthly basis, PPI went up by 0.3% followed a 0.5% gain in the preceding month. The decline is offset by the manufacturing, agriculture, forestry & fishing and food product which continued to shrink since earlier this year. In contrast, we noticed other sectors recorded a faster growth in input price change in May-18. Moving forward, we foresee slowdown in inflationary pressure within tax-holiday period and stable retail fuel prices. Nonetheless, rising global commodity prices remain as the major source of inflationary pressure in Malaysia, affecting domestic inflation thru non-fuel (RON95 and Diesel) channels as well as the introduction of SST in September.

Table 1: Producer Price Indices by Selected Sector

	MoM%			YoY%		
	18-Mar	18-Apr	18-May	18-Mar	18-Apr	18-May
PPI	(0.4)	0.5	0.3	(2.2)	(0.8)	(0.4)
Agriculture, forestry & fishing	(2.9)	(1.6)	(0.6)	11.0	(6.8)	(9.6)
Mining	(0.1)	8.5	4.5	5.8	15.9	29.8
Manufacturing	(0.4)	(0.2)	(0.2)	(2.3)	(2.0)	(2.5)
Electricity and gas	0.8	(0.1)	0.3	1.3	1.5	2.1
Food Product	(0.9)	0.8	(1.4)	(9.3)	(8.3)	(9.0)

Source: CEIC, MIDFR

Contain consumer's inflation. Via pass-through mechanism, we can expect Malaysia's headline inflation to stay moderate in upcoming months as producer's cost inflation continues on contraction. In addition, cost of food products shrank by -9.0%yoy, in tandem with the prices trend reflected in the agricultural-related sector. Moreover, the tax-holiday period until SST implementation in Sep-18 and stable retail fuel prices is expected to translate into reduction in prices of goods and services. Thus, indirectly provide slight relief on cost of living especially for low income earners and this may induce domestic consumption. Furthermore, we foresee this will boost private consumption and sales for producers, and the demand side would add pressure to consumer inflation amid stable wage growth, healthy labour market and the tax-holiday period.

Low input cost will support industrial activities. With the declining input cost inflation in May-18, we opine this would provide support to industrial and business activities in the coming months. In fact, we noticed retail fuel pump prices have remained unchanged as the newly elected government will retain the price of fuel despite the rise in global crude oil prices. Hence, we opine this will hold down input cost pressure and indirectly support local industrial production. As expected, Malaysia's external trade activities recorded a double digit growth and the highest April's reading ever recorded. The acceleration in exports was mainly due to growth in manufactured goods and mining goods. Consequently, we foresee Malaysia's external trade performance as well as manufacturing sales and industrial productions will continue expanding amid gradual rise in commodity prices on top of fading protectionism threat.

Table 2: Producer Price Indices by Stage of Processing

	MoM%			YoY%		
	18-Mar	18-Apr	18-May	18-Mar	18-Apr	18-May
PPI	(0.4)	0.5	0.3	(2.2)	(0.8)	(0.4)
Crude Materials for Further Processing (CM)	(1.0)	2.5	3.8	(0.7)	3.7	9.5
Intermediate Materials Supplies and Components (IM)	(0.6)	0.2	(0.7)	(2.8)	(1.6)	(2.7)
Finished Goods (FG)	0.2%	(0.5)	(0.1)	(2.2)	(2.6)	(2.7)
Capital Equipment (CE)	0.7%	(0.8)	0.4	(2.5)	(2.9)	(2.7)

Source: CEIC, MIDFR

Global PPI surged in May-18 amid higher oil prices. China's producer inflation increased by 4.1%yoy, the highest reading since Jan-18 as the price of commodities such as crude oil and metals increased. Similarly, US PPI rose by 3.1%yoy which is the highest rate since Jan-12. This is boosted by a surge in petrol prices and continued gains in the cost of services which strengthens expectations that inflation will pick up and likely breach the U.S. central bank's 2% target. Moreover, Thailand recorded its highest PPI growth since May-17 at 0.7%yoy, rebounded from negative trajectories, while Japan PPI rose at a faster pace due to surge in the index of oil. The upward trends in PPI are seen to be broad-based, amid of gradual rise in commodity prices and thus will provide supportive environment for businesses to expand steadily in 2018.

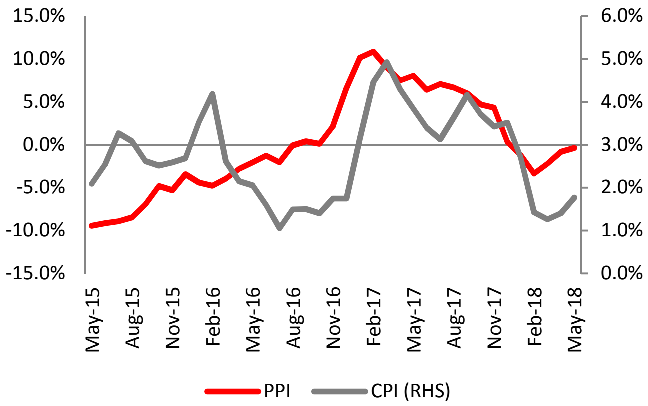
Table 3: Global Producer Price Index (YoY%)

	17-Nov	17-Dec	18-Jan	18-Feb	18-Mar	18-Apr	18-May
Malaysia	4.3	0.3	(1.2)	(3.4)	(2.2)	(0.8)	(0.4)
Indonesia	2.8	2.7	3.2	3.4	3.4	4.9	
Thailand	0.5	(0.6)	(1.1)	(1.9)	(1.4)	(0.8)	0.7
Philippines	(1.3)	(1.8)	(2.0)	(1.3)	(0.9)	0.5	
Singapore	5.4	0.6	(0.2)	(0.8)	0.9	2.5	8.2
Japan	3.5	3.1	2.7	2.5	2.1	2.0	2.7
China	5.8	4.9	4.3	3.8	3.1	3.4	4.1
EU	2.8	2.2	1.6	1.6	2.1	2.0	
United States	3.1	2.6	2.7	2.8	3.0	2.6	3.1

Source: CEIC, MIDFR

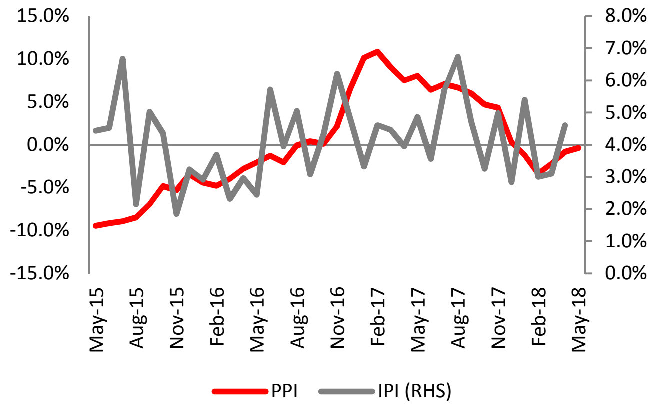
Producer price index is expected to expand by 3.2% in 2018. Amid unfavourable base effects, we foresee input cost inflation to average at 3.2% this year. We anticipate inflationary pressure from fuel-related items to pick-up at steady speed, in tandem with steady gradual rise in global commodity prices. However, we note that volatility in global commodity prices and market uncertainties due to trade war and geopolitical tensions are downside risks in putting a steep inflationary pressure for businesses as well as consumers in Malaysia.

Chart 1: PPI vs CPI (YoY%)



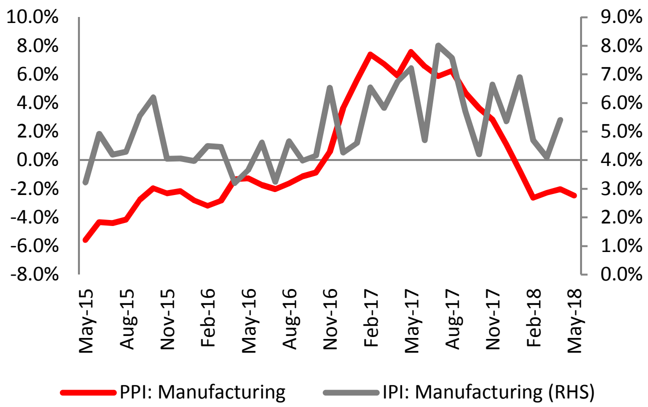
Source: CEIC, MIDFR

Chart 2: PPI vs IPI (YoY%)



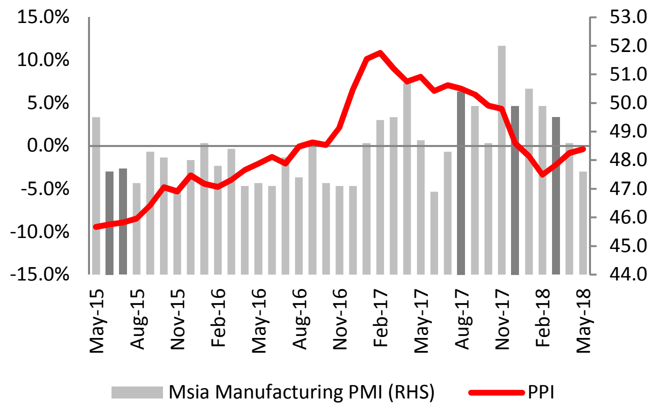
Source: CEIC, MIDFR

Chart 3: Manufacturing: PPI vs IPI (YoY%)



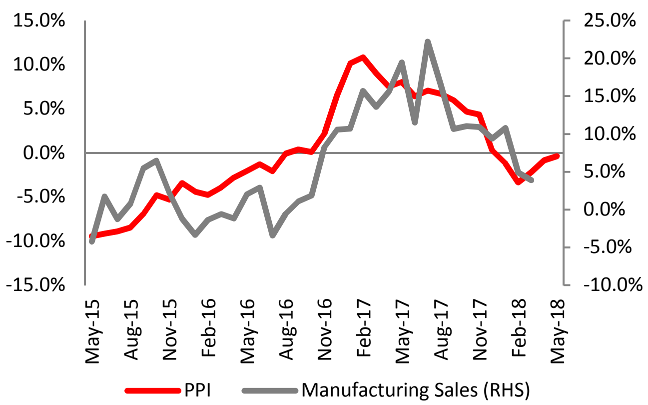
Source: CEIC, MIDFR

Chart 4: PPI (YoY%) vs Manufacturing PMI (Points)



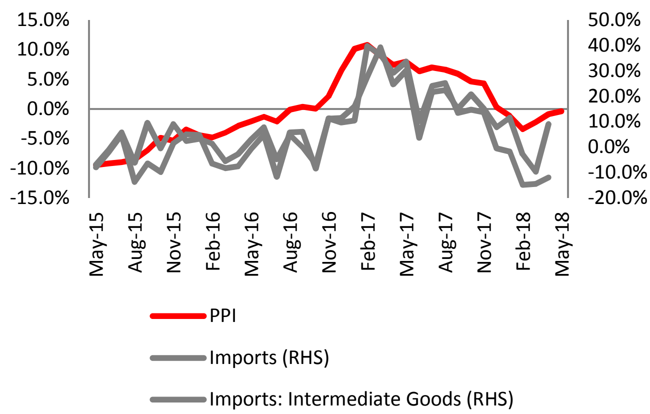
Source: CEIC, BLOOMBERG, MIDFR

Chart 5: PPI vs Manufacturing Sales (YoY%)



Source: CEIC, MIDFR

Chart 6: PPI vs Imports (YoY%)



Source: CEIC, MIDFR

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