4 December 2018

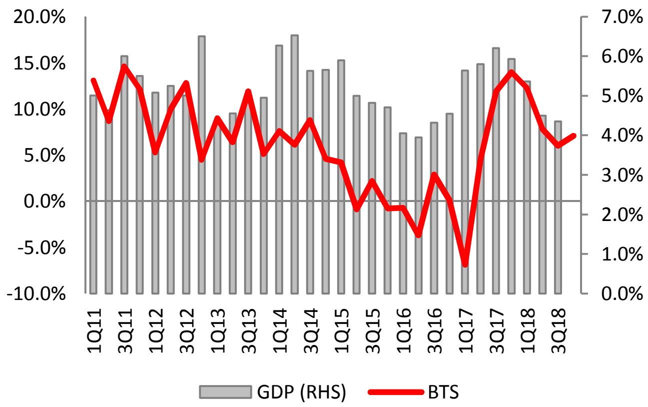
MONTHLY ECONOMIC REVIEW | November 2018

Improved Economic Sentiment, Thanks to Cooling Trade Tension & Strong Domestic Demand

- *Slight improvement in 4Q18. According to the latest Business Tendency Survey, overall business performance is expected to remain positive at a better pace given that overall business confidence registered at 7.1%, higher than the previous quarter. The improvement is supported by services and distributive trade amid robust domestic demand.*
- *GDP growth in 3Q18 missed market expectations. Malaysia's GDP growth expands by 4.4%yoy in 3Q18, slightly above our forecast of 4.2%yoy and below market expectations of 4.6%yoy. We have expected the GDP performance to moderate during the quarter as mentioned in our GDP preview report, highlighting strong domestic demand and contractions in commodity-based sectors such as agriculture and mining & quarrying.*
- *Malaysia's current account surplus at 9-quarter low. Current account still recorded a surplus however the gain is getting smaller since 2Q18. In 3Q18, current account surplus narrowed further to RM3.8B compared to RM3.9B in the previous quarter, making it the smallest surplus since 3Q16.*

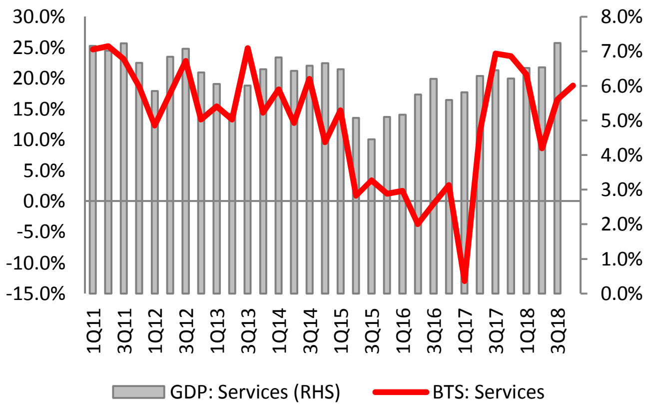
Slight improvement in 4Q18. According to the latest Business Tendency Survey, overall business performance is expected to remain positive at a better pace given that overall business confidence registered at 7.1%, higher than the previous quarter. The improvement is supported by services and distributive trade amid robust domestic demand. On the other hand, main sectors such construction, agriculture and mining & quarrying are still in pessimistic territory while manufacturing sector remains in upward trajectory despite trade war. Henceforth, we expect higher GDP growth in 4Q18 of more than 5% underpinned by solid domestic demand.

Chart 1: BTS (%) vs GDP (YoY%)



Source: CEIC; MIDFR

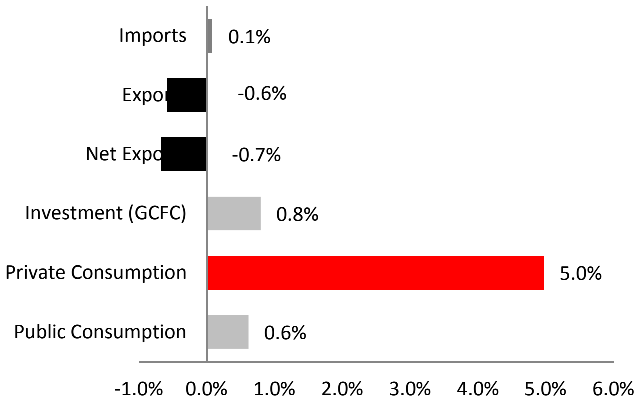
Chart 2: Services: BTS (%) vs GDP (YoY%)



Source: CEIC; MIDFR

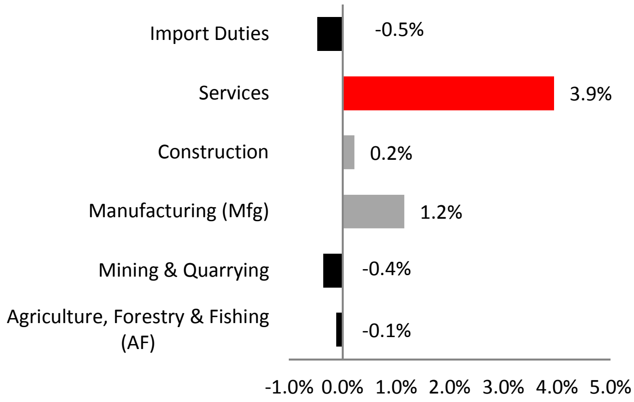
GDP growth in 3Q18 missed market expectations. Malaysia's GDP growth expands by 4.4%yoy in 3Q18, slightly above our forecast of 4.2%yoy and below market expectations of 4.6%yoy. We have expected the GDP performance to moderate during the quarter as mentioned in our GDP preview report, highlighting strong domestic demand and contractions in commodity-based sectors such as agriculture and mining & quarrying. It is the weakest growth in 7-quarters. Among others, tax holiday and stable retail fuel prices boosted growth as domestic demand contributes about 5% of the total growth during the quarter. From supply side, services and manufacturing sectors contribute 3.9% and 1.2% respectively. We opine the continuous slowdown in GDP growth is mainly due to external factors particularly escalating trade war effects and poor performances of commodity-based sectors. Moderating inflationary pressure, strengthening domestic demand and accommodative economic policies as well as strong re-exports growth are the expected to be major drivers for GDP performance in the last quarter of 2018.

Chart 3: Contribution by Expenditure Components (%)



Source: CEIC, MIDFR

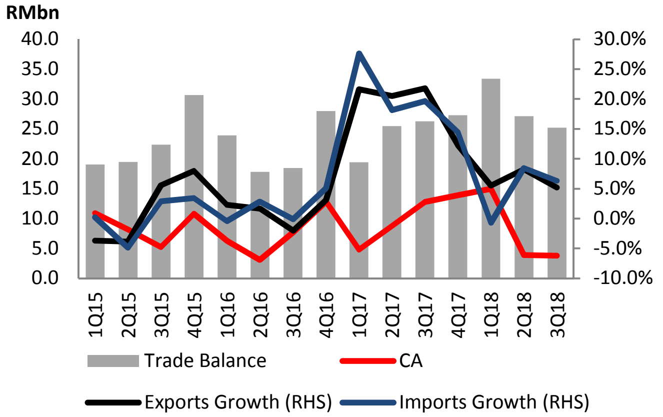
Chart 4: Contribution by Supply-Side Components (%)



Source: CEIC; MIDFR

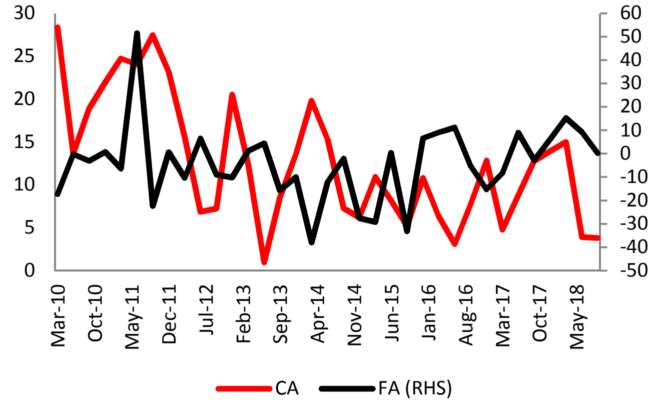
Malaysia's current account surplus at 9-quarter low. Current account still recorded a surplus however the gain is getting smaller since 2Q18. In 3Q18, current account surplus narrowed further to RM3.8B compared to RM3.9B in the previous quarter, making it the smallest surplus since 3Q16. The fall was mainly attributable to deficit in services account amounted to RM3.3B in 3Q18 however the figure has improved from a larger deficit of RM6.2B in 2Q18. Meantime, goods account surplus increased marginally to RM26.6B from RM26.1B in the previous quarter due to a modest trade surplus of RM25.2B in 3Q18 (RM27.1B in 2Q18). In addition, average imports growth of 6.3%yoy exceeded those of exports (5.3%yoy). Nevertheless, Malaysia still positioned as net external creditor built up from a record of current-account surpluses.

Chart 5: Current Account Balance vs External Trade



Source: CEIC, MIDFR

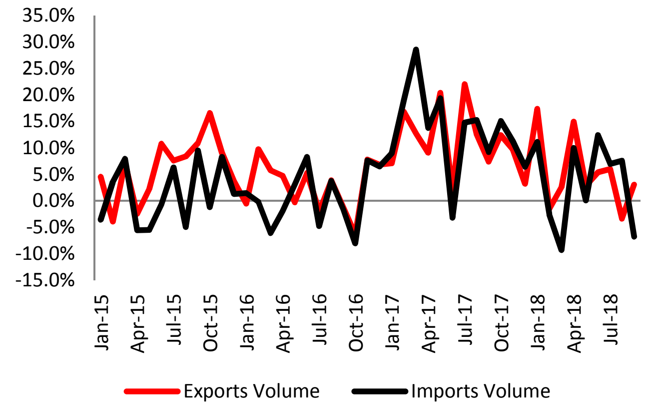
Chart 6: CA vs FA (RM Billion)



Source: CEIC, MIDFR

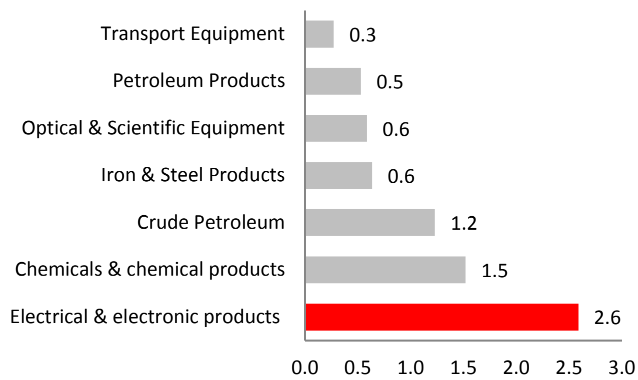
Exports growth rebounded. Exports growth in Sep-18 rebounded on both annually and monthly basis at 6.7% and 1.5% respectively, sustaining value above RM80b despite fewer working days. The improvement was mainly due to better sectoral performances. Manufactured goods, the largest contributor to exports grew further by 7.9%yoy (1.8%yoy in Aug-18). In addition, outbound shipment of mining goods soared by double digit growth of 17%yoy (5.5%yoy in Aug-18). In contrast, September's imports contracted 2.7%yoy and 15.5%mom to RM67.8b. As exports outperformed imports, trade surplus recorded at 10-year high of RM15.3b. For the first nine months, trade surplus (RM85.7b) has already hit 71% of our full-year target of RM119.9b.

Chart 7: Exports & Imports Volume (YoY%)



Source: CEIC, MIDFR

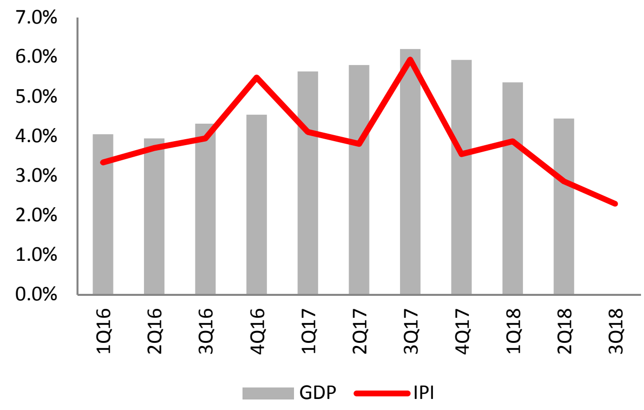
Chart 8: % Contribution to Exports Growth by Products



Source: CEIC, MIDFR

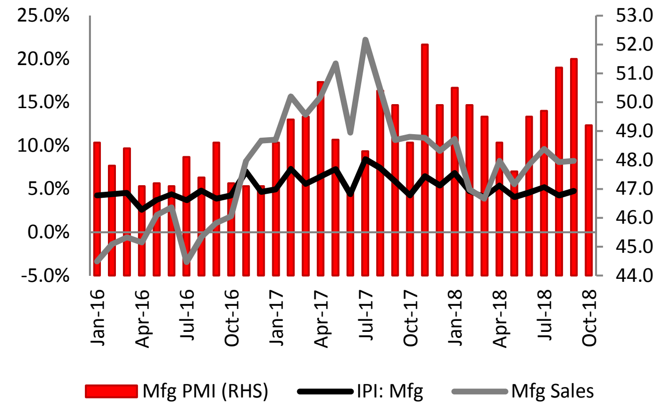
IPI growth slightly below market estimates. Malaysia's industrial production expands by 2.3%yoy in Sep-18, lower than market estimates of 2.4%yoy. By major components, manufacturing and electricity outputs were up 4.7%yoy and 4.2%yoy respectively while mining continues to decline for 5-consecutive months. On quarterly performance, overall IPI growth indicates further moderation in GDP expansion pace in the third quarter. Contraction in mining output at -5.6%yoy during 3Q18 was the major dragging factor whereas factory and electricity output increase at a steady pace. The modest pick-up in IPI performance is in tandem with the improvement of Malaysia's external trade in Sep-18. Moving forward, we foresee IPI performance to expand at steady pace for the fourth quarter of 2018 and 2019 amid tapering trade tension effects, strong global demand, optimistic business environment and volatility risks in global commodity prices & currencies.

Chart 9: IPI vs GDP (YoY%)



Source: CEIC, MIDFR

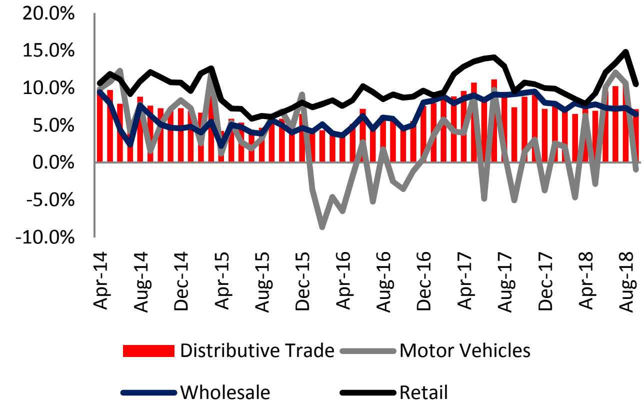
Chart 10: Manufacturing IPI & Sales (YoY%) vs PMI (Points)



Source: CEIC, MIDFR

Spending relaxed as tax holiday ended. Distributive trade growth slowed to 7.2%yoy in Sep-18, returned to the pace prior to tax holiday (7%yoy in June-18), however sustaining value above RM100b. Although slowing down, retail sales still maintained its double digit growth of 10.5%yoy to RM11.2b in Sep-18. Similarly, wholesale trade moderated at 6.5%yoy however reached a new all-time high of RM52.4b in Sep-18 probably due to the lower tax resulting from reintroduction of SST compared to GST. In contrast, motor vehicles posted negative growth of 0.9%yoy in Sep-18, a widely anticipated declining pattern as consumers advanced their purchases prior to the implementation of SST in Sep-18. On monthly basis however distributive trade contracted by 2.9% as both motor vehicles and retail sales posted negative growth of 17% and 5.3% respectively. Moving forward, we expect distributive trade to increase gradually as consumers adapting to the reinstatement of SST.

Chart 11: Distributive Trade, DT (YoY%)



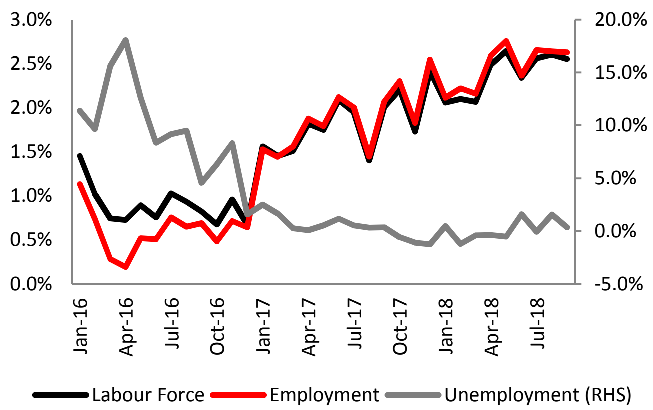
Source: CEIC, MIDFR

Chart 12: Retail Trade: GDP vs DT (YoY%)

Source: CEIC, MIDFR

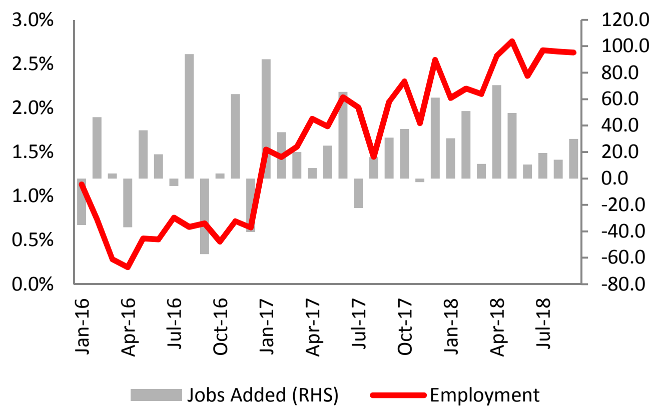
Labour market remains strong. Labour force expanded by 2.6%yoy to 15.4 million in Sep-18, unchanged for the third consecutive month. Employment growth maintained at 2.6%yoy to 14.9 million in Sep-18 and jobs added in the economy registered at four-month high of 30K during the month (14.1K in Jul-18), in line with external trade performances. Unemployment rate inched lower to a full-employment condition of 3.3% after three consecutive months maintaining at 3.4%. The number of unemployed increased 0.4% in Sep-18 however lower than 1.6% recorded in the previous month. In addition, growths in both labour force and employment have been outpacing unemployment growth for the last 19-month since Mar-17.

Chart 13: Labour Market Key Indicators (YoY%)



Source: CEIC, MIDFR

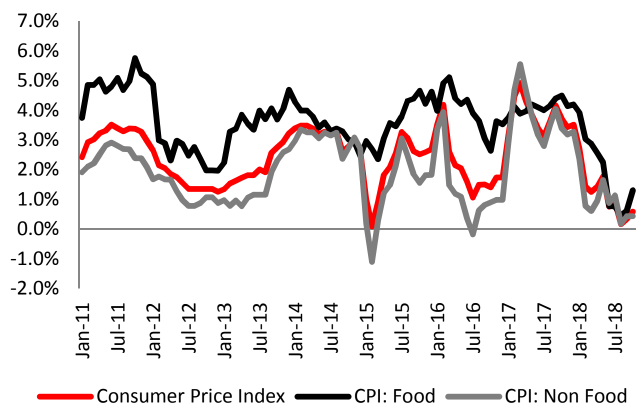
Chart 14: Jobs Added ('000) vs Empl. (YoY%)



Source: CEIC, MIDFR

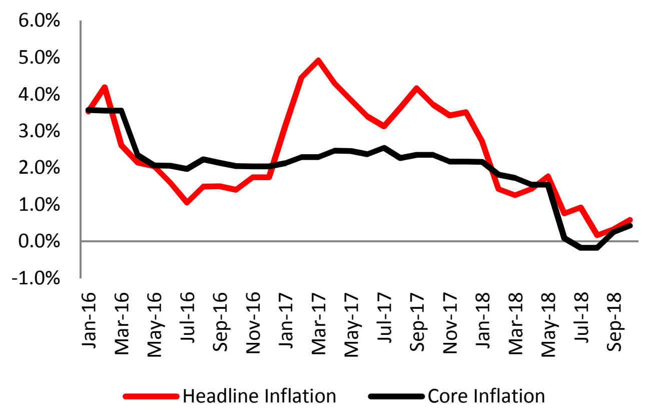
Inflation is on an upward trend. Consumer price index increased 0.6%yoy in Oct-18, doubled the rate recorded in the preceding month, slightly lower than our forecast of 0.7%yoy and matched market estimates. We have expected the inflation rate to continue trending upward during the month. However, the three-month high figure was still below 1% for the fifth consecutive month despite the reintroduction of SST, probably due to the significant impact of RON95 fuel subsidization. Transport prices increased by 0.8%yoy (0.3%yoy in Sep-18) but stay below 1% for second consecutive month. Meanwhile, core inflation rate increased further to 0.4%yoy (0.3%yoy in Sep-18). Looking ahead, Malaysia's inflation is expected to gradually increase in the upcoming months.

Chart 15: CPI: Headline vs Food & Non-food (YoY%)



Source: CEIC, MIDFR

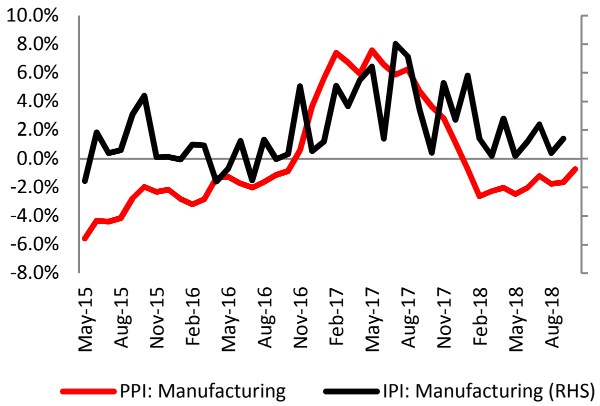
Chart 16: CPI: Headline vs Core (YoY%)



Source: CEIC, MIDFR

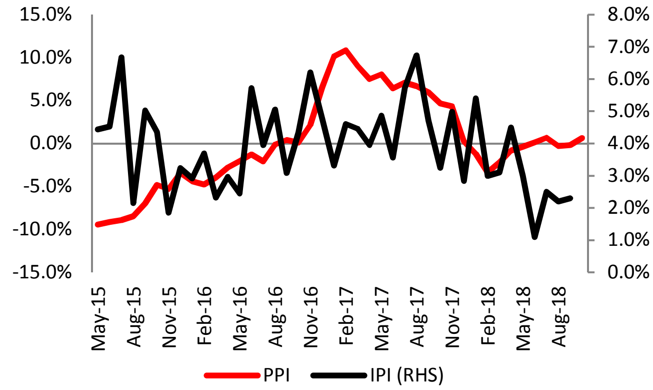
PPI rebounds to positive territory. Malaysia's producer inflation rebounded to a positive territory of 0.7%yoy in Oct-18 after a contraction in the previous two months. The growth was buoyed by an increase in index of mining (30.6%yoy) and electricity & gas (1%yoy). Meanwhile, manufacturing sector which hold the largest weightage of total PPI basket at 81.6% continued to register contraction however at an improving pace of 0.7%yoy (-1.7%yoy in Sep-18). The rising PPI is in line with our expectation that PPI will increase gradually following a pick-up in global crude oil prices and implementation of SST. In upcoming month, PPI growth could be slightly influenced by the global crude oil prices as it went below USD60pb in Nov-18.

Chart 17: Manufacturing: PPI vs IPI (YoY%)



Source: CEIC, MIDFR

Chart 18: PPI vs IPI (YoY%)



Source: CEIC, MIDFR

Table 1: Macroeconomic Data Updates

(YoY%) Unless Stated Otherwise	**2016**	**2017**	**2018f**	**1Q18**	**2Q18**	**3Q18**	**4Q18f**
Real GDP	4.2	5.9	4.8	5.4	4.5	4.4	5.2
Private Consumption	6.0	7.0	7.7	6.9	8.0	9.0	7.1
Public Consumption	0.9	5.4	3.0	0.4	3.1	5.2	3.2
Gross Fixed Capital Formation	2.7	6.2	1.7	0.1	2.2	3.2	1.5
Exports of goods & services	1.3	9.4	2.2	3.7	2.0	(0.8)	4.0
Imports of goods & services	1.3	10.9	1.2	(2.0)	2.1	0.1	4.6
Net Exports	92.8	91.0	100.6	29.5	21.3	24.6	25.2
Agriculture etc.	(5.2)	7.2	(0.7)	2.8	(2.5)	(1.4)	(1.8)
Mining & Quarrying	2.1	1.0	(0.8)	0.1	(2.2)	(4.6)	3.5
Manufacturing	4.4	6.0	5.1	5.4	4.9	5.0	5.0
Construction	7.4	6.7	4.9	4.9	4.7	4.6	5.2
Services	5.7	6.2	6.7	6.5	6.5	7.2	6.7
Exports of Goods (f.o.b)	1.1	14.5	7.3	5.8	8.4	5.3	9.5
Imports of Goods (c.i.f)	1.9	15.5	5.6	(0.2)	8.9	6.3	7.3
Trade Balance - RMb	87.2	97.5	119.8	33.4	27.1	25.2	34.1
Consumer Price Index	2.1	3.8	1.2	1.8	1.3	0.5	1.1
Current Account - RMb	29.0	36.6	32.7	-	-	-	-
Fiscal Balance - % of GDP	(3.1)	(3.0)	(3.7)	-	-	-	-
Federal Government Debt - % of GDP	53.8	53.0	52.5	-	-	-	-
End of Unless States Otherwise	**2016**	**2017**	**2018f**	**1Q18**	**2Q18**	**3Q18**	**4Q18f**
Brent Crude Oil (Avg)	46.0	55.7	70.0	67.3	75.1	76.1	
Crude Palm Oil (Avg)	2,677	2,733	2,310	2,492	2,372	2,205	
USD/MYR (Avg)	4.15	4.30	4.02	3.92	3.95	4.10	4.10
USD/MYR	4.48	4.15	4.10	-	-	-	-
Yield on generic 10-year MGS (%)	3.85	4.00	4.10	-	-	-	-
Overnight Policy Rate (%)	3.00	3.00	3.25	3.25	3.25	3.25	3.25

Source: MIDFR

November 2018 Key Economic Events

2 Nov: Budget 2019 Highlights. Government's real debt and liability as at June 2018 was at RM1,065B, RM350B higher than during reign of previous Government. GDP is expected to grow 4.9% in 2019 amid uncertainties in global economy. Government estimates RM43.9B may be required to pay off 1MDB debts. Fiscal Responsibility Act by 2021 aims to prevent uncontrolled spending. International reserves amounting to US$102.8B (RM426B) as at 15th Oct suffices to cover 7.4 months of retained imports. Inflation rate remained low (1.2%) from Jan to Sept-18. Fiscal deficit in 2018 to reach 3.7%.

7 Nov: The 2018 U.S. midterm elections are over. Here's what you need to know. Among those were the voters who on Tuesday night returned control of the Senate to Republicans and along with it, the power to all but ensure the confirmation of any further Supreme Court justices that Trump gets to nominate over the next two years. Voters in Florida and Texas also upheld their support for Trump, handing defeats to Democratic gubernatorial candidate Andrew Gillum and Ted Cruz's Senate challenger, Beto O'Rourke. Heidi Heitkamp, the Democratic senator for North Dakota, also lost out.

16 Nov: BNM: Malaysia GDP grew 4.4% in 3Q, expected to remain on steady growth path. The Malaysian economy is expected to remain on a steady growth path remaining of the year, after recording a gross domestic product (GDP) growth of 4.4% in 3Q18. According to Bank Negara Malaysia (BNM), private sector activity continued as the primary driver of growth as private consumption expanded strongly, following zerorisation of Goods and Services Tax (GST). According to BNM governor Datuk Nor Shamsiah Mohd Yunus, supply of services and manufacturing sectors supported growth while mining sector continued to be affected by production shocks.

16 Nov: Malaysia's external debt fell to 66.2% of GDP at end Q3 2018. Malaysia's total external debt declined to 66.2% of gross domestic product (GDP) as at end-Q3, 2018 from a peak of 74.3% of GDP as at end-2016. Bank Negara said on Friday that the bulk of the external debt was by corporations and banks. "Foreign currency-denominated external debt stood at 46.0% of GDP as at end-Q3 2018, compared to the highest level of 60.0% of GDP during the 1997 Asian Financial Crisis," it said in a report on the country's external debt. The report said the government's foreign-currency denominated external debt was very low (1.2% of GDP).

18 Nov: Azmin and Rafizi close ranks after bruising polls. Rafizi Ramli emphasizes strong and united leadership is a common goal among party members and to move forward after competition party polls. Different views and ideas is natural to arise however the organization should grow healthily by solving problems objectively. The reconciliation between Rafizi and Ramli also helped fixed tension between delegates.

23 Nov: Oil prices hit a 2018 low as OPEC considers an output cut. Global oil supply has surged this year, with the top-three producers — the United States, Russia and Saudi Arabia — pumping more than a third of global consumption. Saudi Arabia is pushing OPEC to cut oil supply by as much as 1.4 million bpd to prevent a supply glut. Shanghai stocks fell the most in five weeks on Friday, by 2.5 percent, amid worries over China's economic growth and the U.S.-Sino trade war.

28 Nov: Fed chair sends markets soaring with suggestion that rate hikes may slow. Federal Reserve Board Chair Jerome H. Powell suggested that the central bank could slow the pace of its interest rate increases, a statement welcomed by investors worried about the strength of the global economy and swooning markets. His comments appeared to mark a change from his position last month, when he said that the Fed still had a "long way" to go before it reached what economists consider an appropriate level. Powell's description of the central bank's approach sent the stock market soaring, with investors eager for any sign that the Fed might be preparing to pause its slow but steady effort to raise interest rates.

30 Nov: What to expect from the crucial G-20 meeting between Trump and Xi this weekend. Discussions around trade are expected to dominate the G-20 summit, with the meeting between U.S. President Donald Trump and his Chinese counterpart Xi Jinping likely to take center stage. Most experts are not expecting a major breakthrough in the ongoing U.S.-China tariff fight. "At most, there might be an agreement for the president to withhold further tariffs ... in exchange for discussions over the next several months," said Gary Locke, former U.S. ambassador to China.

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