13 February 2014

MALAYSIA

The economy grew slightly faster in the 4Q 13 on the back of continued pick up in the Manufacturing sector and faster expansion in the Services sector that helped to offset the slowdown in domestic demand. Net exports, however, continued to be a drag on growth. While the current account surplus was higher in 4Q 13, overall Balance of Payments deteriorated slightly in the 4Q 13 on bigger capital outflows leading to a drawdown in the FX reserves. External debt edged up higher to 33.5% of GDP but our fiscal position improved with the Federal Government's budget deficit narrowing to 3.9% of GDP in 2013, well within its target for the year. We maintain our call for real GDP growth at 5.0% in 2014 and revised downwards our USD/MYR to 3.30 – 3.40 by end-2014.

The economy grew at a slightly faster rate of 5.1% in the 4Q 13 (3Q 13: 5.0%), matching our (5.0%) but beating consensus expectation (4.7%) on the back of continued pick up in the Manufacturing sector and faster expansion in the Services sector that helped to offset the slowdown in domestic demand. Net exports, however, continued to be a drag on growth. For the whole of 2013, real GDP growth decelerated to 4.7% (2012: 5.6%) led by the sharp deceleration in domestic demand.

Aggregate domestic demand driving growth, contributing 6.0 p.p. to the 5.1% growth in real GDP in 4Q 13. Although domestic demand slowed rather significantly during the quarter, with growth in private and public consumption decelerated to 7.3%YoY and 5.1%YoY respectively (3Q 13: 8.2% and 7.8% respectively) and that of the gross fixed capital formation (GFCF) to 5.8% (3Q 13: 8.6%), the smaller surplus in net exports for the quarter (-11.9% YoY vs +1.6%YoY in 3Q 13) led the aggregate domestic demand contributing as much as 6.0 p.p. (3Q 13: 7.5%) to real GDP growth of 5.1%. Despite the pick up in exports during the quarter, the faster rise in imports led net exports smaller at RM16.3bn as compared to RM18.2bn in the 4Q 12. It was worth noting that private consumption did not pull back sharply during the quarter despite the higher fuel prices and other adjustments in prices of administered goods.

By sector, Services continued to be the driver supported by the acceleration in the Manufacturing sector. Services sector grew by a robust 6.4%YoY (3Q 13: 5.9%) on the back of faster consumption-driven sector i.e. Wholesale & Retail trade (8.4% YoY vs 6.1% in 3Q 13) while the other sub-sectors posting either flattish or deceleration in growth. Meanwhile the Manufacturing sector recorded a slightly faster growth of 5.1% as compared to 4.2% in the previous quarter, driven by the sharp recovery in the E&E production (9.7% vs 4.4% in 3Q 13). Construction growth slowed down, but staying robust, at 9.7% (3Q 13: 10.1%) on the back of completion of several infrastructure projects.

2013 real GDP growth slowed down to 4.7% (2012: 5.6%) mainly on the back of lost momentum in GFCF. Growth in GFCF decelerated significantly to 8.2%YoY in 2013 from 19.9% in 2012. Private consumption growth was flat (7.6% vs 7.7% in 2012) but public consumption recorded slightly faster growth of 6.3% (2012: 5.1%). By sector, all key sectors posted deceleration in growth in 2013 compared to that in 2012, except the Agriculture sector. The slower growth for Services and the Manufacturing sector were attributed to the weaker performance in the 1H 2013.

BoP deteriorated in the 4Q 13, with capital outflows and Errors & Omissions outweighing the improved CA surplus, leading to drawdown in FX reserves. Current account surplus widened to RM16.2bn or 6.4% of GNI in the 4Q 13 (RM9.8bn or 4.1% of GNI) on bigger merchandise trade surplus and smaller deficit in Services balance, putting the overall CA surplus at 3.9% of GNI in 2013 (2012: 6.3%). At the same time, the financial account of the Balance of Payments (BoP) posted a smaller outflows of RM9.7bn (3Q 12: -RM11.5bn), while the outflows categorized under Errors & Omissions cited by BNM as reflecting FX revaluation gains on international reserves was at RM9.3bn, leading to total outflows amounting to RM19.1bn. Consequently, the overall BoP posted a deficit of RM2.9bn, reflected in the foreign exchange (FX) reserves at the end of the year which stood at RM441.7bn (end-3Q 13: RM444.6bn).

FX reserves declined further by RM5.1bn (US$1.8bn) in January; a 3.4x cover for short-term debt. BNM reported last Monday that our FX reserves continued to decline in January to RM436bn which implies a further drawdown on our BoP of RM5.1bn. At the time of the release, BNM estimated that the ratio of FX reserves/short-term debt was at 3.6x, but this was revised lower to 3.4x in the latest Quarterly Bulletin of which our report here is based upon. Although FX reserves at the end of January 2014 was relatively higher than that a year ago (RM428.6bn), the FX reserves/short-term debt ratio was higher at 4.6x then as our external debt now has grown bigger.

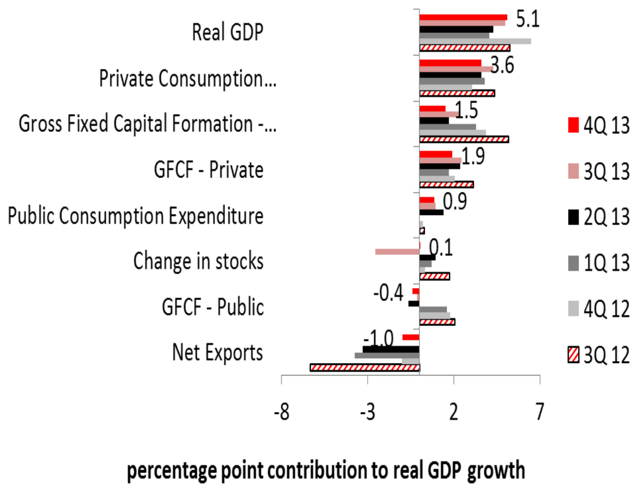
External debt swelled further with short-term debt also significantly higher. Total external debt at the end of 2013 stood at RM318.1bn or 33.5% of GNI, an increase of RM65.3bn from the level recorded at the end of 2012 (27.9% of GNI). The increase was much higher for short-term debt, at RM35.1bn from a year ago, or 37.7% YoY while that of the medium and long-term debt rose by RM30.2bn or 18.9% YoY. Short-term debt now accounts for 40.2% of the total external debt and a ratio of 0.67 to 1.0 to the medium and long-term debt, compared to a share of 36.8% of GNI in 2012 and a ratio of 0.58 to 1.0 to the medium and long-term debt.

Fiscal deficits widened to 5.2% of GDP in the 4Q 13 on higher spending in both OpEx and Net DevEx but smaller at 3.9% for the whole 2013. Federal government revenue was higher at RM61.1bn in the 4Q 13 (3Q 13: RM57bn; 4Q 12: RM57.2bn) but the Operating Expenditure (OpEx) edged up by RM5.4bn to RM58,8bn in the 4Q 13 from a quarter ago, although it was lower by 4.6% on YoY basis. At the same time Net development expenditure (DevEx) was RM7bn higher on QoQ but RM0.6bn lower YoY, That resulted in the fiscal deficit widening to RM13.8bn in the 4Q 13 or 5.2% of GDP from RM5.4bn at the end of 3Q 13 (-2.2% of GDP). Given the much smaller deficits in the 2Q and 3Q 13 period, the overall fiscal deficits for 2013 narrowed to 3.9% from 4.5% of GDP in 2012.

We maintain our call for 5.0% growth in 2014. As we had highlighted in our earlier report on December IPI, we expect the external demand boost Malaysia's GDP on the back of strengthening recovery in the developed markets, mainly the US, may be rather modest as compared to the historical trends of upward E&E cycles as exports to the US now being dwarfed by the share that is going to China, our largest export market now. At the same time, domestic demand growth is likely to be constrained by the high level of debt for all sectors – household, businesses as well as the government, which implies some deleveraging at a faster pace may take place and at the expense of growth – and the likely continued upward pressure on domestic cost.

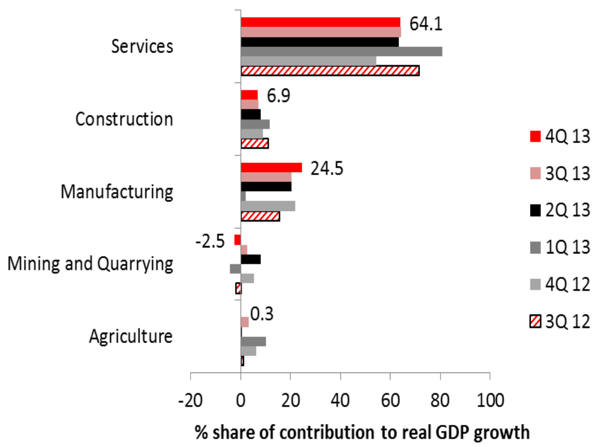
We revised downwards our USD/MYR to 3.30 – 3.40 (from 3.20 – 3.25) With the US likely to stick to the measured taper moves, the EM currencies are likely to continue to face downward pressure, although big selloffs may not be repeated unless there is some really negative newsflow or data to cause a big risk aversion. With our external position not looking good, that would add on to the likely contagion effect of any downward moves in EM currencies, casting an unfavourable outlook for Ringgit for the rest of the year.

Chart 1: Real GDP by expenditure – contribution To growth



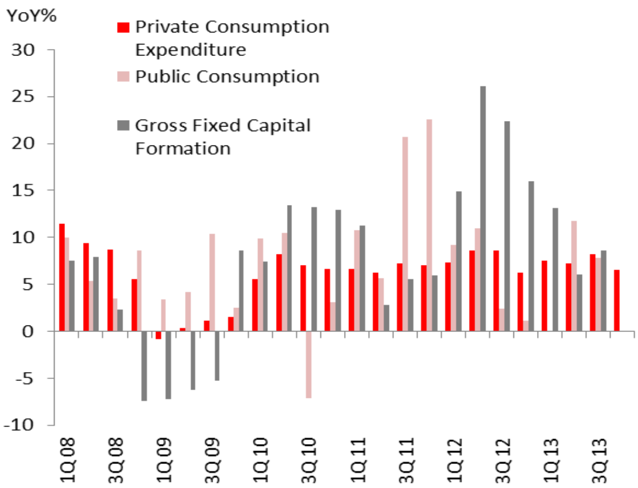
Source: BNM

Chart 2: Real GDP by sector – % share of contribution to RGDP growth



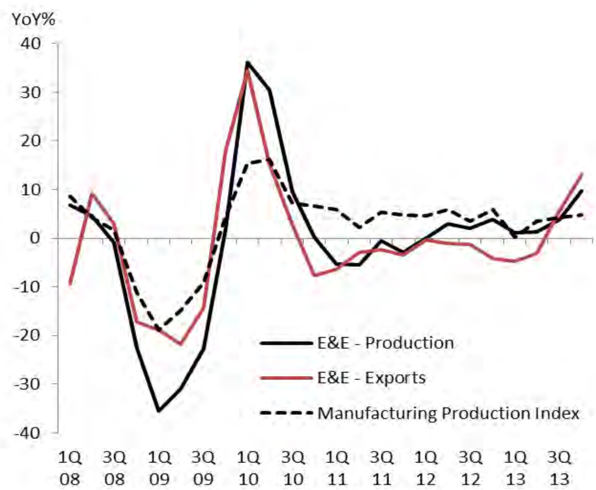
Source: BNM

Chart 3: Aggregate domestic demand components: – YoY change



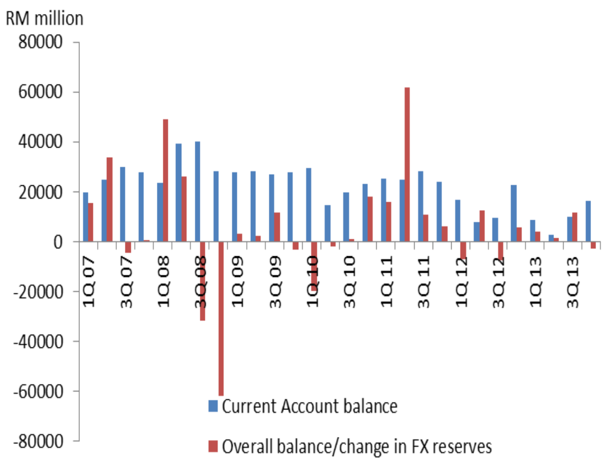
Source: BNM

Chart 4: Manuafacturing picked up on the back E&E rebound



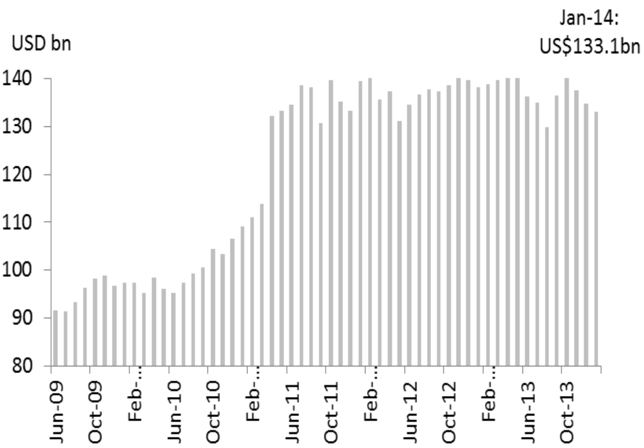
Source: BNM

Chart 5: Balance of Payments



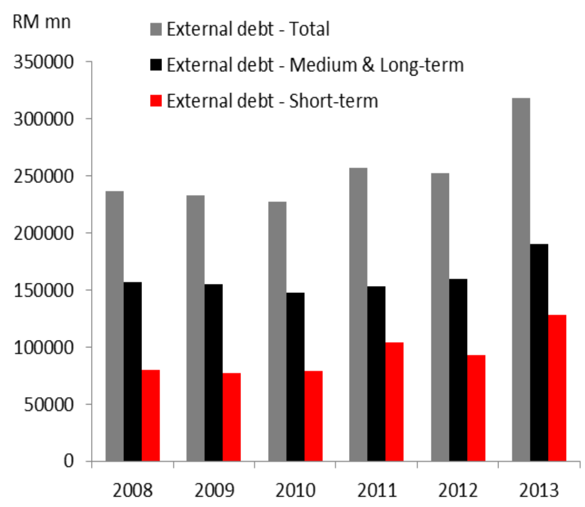
Source: BNM

Chart 6: Foreign exchange reserves – in USD term



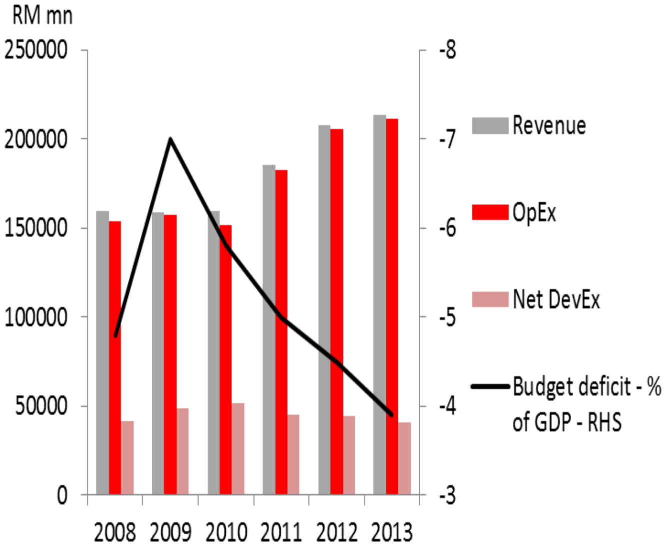
Source: BNM

Chart 7: External debt



Source: BNM

Chart 8: Federal Government Finance



Source: BNM

DISCLOSURES AND DISCLAIMER

MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS

STOCK RECOMMENDATIONS	
BUY	Total return is expected to be >15% over the next 12 months.
TRADING BUY	Stock price is expected to *rise* by >15% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -15% and +15% over the next 12 months.
SELL	*Negative* total return is expected to be -15% over the next 12 months.
TRADING SELL	Stock price is expected to *fall* by >15% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.
SECTOR RECOMMENDATIONS	
POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.