14 March 2014

MALAYSIA

January IPI - A temporary blip or a sign of losing momentum?

The growth in IPI slipped in January as Manufacturing production (MPI) eased along with a sharp deceleration in Electricity index growth while that of Mining turned around albeit marginally. We believe the deceleration was mainly driven by non-E&E export-oriented sectors (on the back of the slowdown in our major trading partners, notably China) and domestic-oriented sectors due to higher input costs and cool off in demand. This was reflected in the sharp deceleration in the Electricity index for the month. The low base implies the IPI can rebound in the next few months but the rather still volatile performance indicates that a firmer trend may not emerge until well into late 2Q 14.

IPI growth decelerated in January on possible multitude factors. The overall index slipped to 3.6%YoY from 4.8% in December 2013, again falling short of consensus expectation (4.2%) and ours (4.5%) as Manufacturing eased along a sharp drop in growth for Electricity index while that of Mining turned around albeit very marginally.

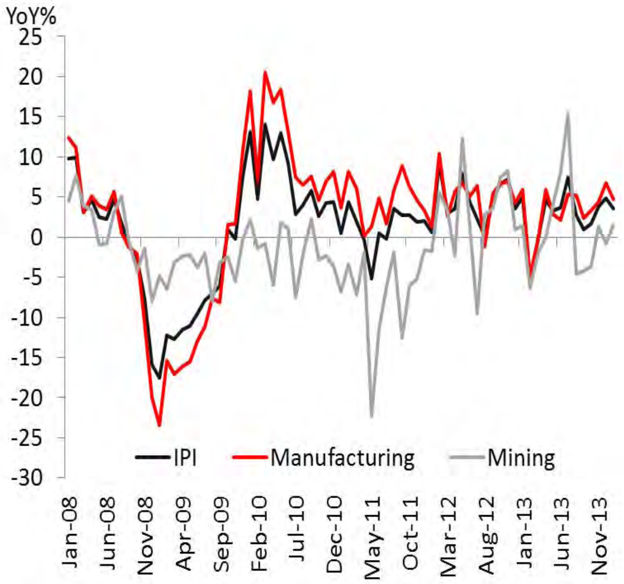
Attributing the deceleration in the Manufacturing production (MPI) to the cold winter in the US may be tough to be justified given its lead time period of at least 2-3 months ahead of our MPI. Data on the breakdown by BNM for the month has yet to be out but we believe the deceleration was mainly driven by the other export-oriented sectors (on the back of the slowdown in our major trading partners, notably China) and domestic oriented sectors due to higher input costs and cool off in demand. This was reflected in the sharp deceleration in the Electricity index for the month.

Nonetheless, the sharp deceleration in Electricity index may not only be industrial-related The Electricity index would normally track the performance of the MPI and while the latter slowdown helped to explain the similar direction for the Electricity index, the deceleration was rather significant indicating that it was also being driven by non-industrial related, as non-industrial consumers might have cut down their consumption well ahead of the higher electricity tariff rates that came into effect in January, causing production to adjust much lower. The downward adjustment on MoM term of 2.2% was similar to that seen in June 2011 when Tenaga last raised its tariff with the index showing a 2.0% decline but low base YoY effect then saw the index posted a much higher growth. Having said that, the index only accounts for just 5.9% of the overall IPI, according to BNM estimation.

The low base ahead implies the IPI can rebound in the next few months but the rather still volatile performance indicates that a firmer trend may not emerge until well into late 2Q 14. Our preferred leading indicators that are mainly E&E-driven showed that the IPI may rebound, in the next few months before adjusting lower again. Nonetheless, the overall index has remained rather volatile, for both MPI and the Mining index. We are also looking at how best to include China's indicators into our composite index tracking to reflect the growing importance of it as our main trading partner particularly the primary-clustered export-oriented industries, which accounts for 60% of MPI.

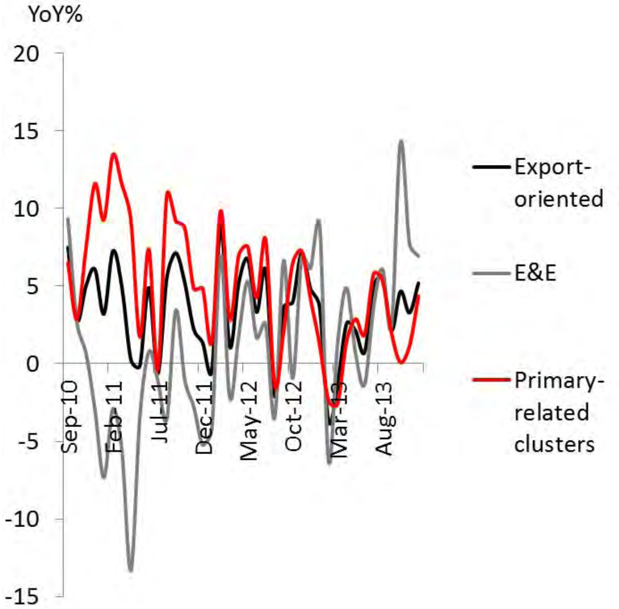
The much lower correlation between IPI and GDP indicates that it is too early to detect any indication. IPI is widely used as reference indicator or proxy for real GDP, but our calculations showed the cross correlation of the two variables have come down markedly, from 0.98 in 1995 - 2007 to about 0.83 in the 2005 – 2013 period. This makes modeling the leading indicator tougher as we need to track economic activity on month-to-month basis with an attempt to draw reference to GDP using the IPI.

Chart 1: Industrial Production Index (IPI) – Main indices



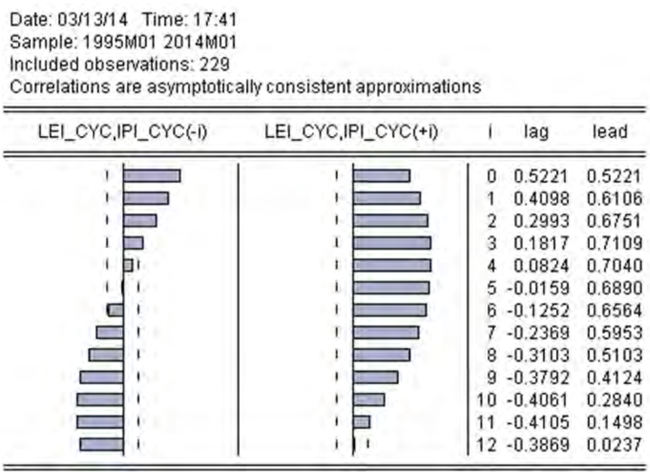
Source: DoS

Chart 2: Export-oriented industries increasingly idictated by primary-related sectors



Source: BNM

Chart 3: IPI – Our leading indicator at 3-4 months lead..

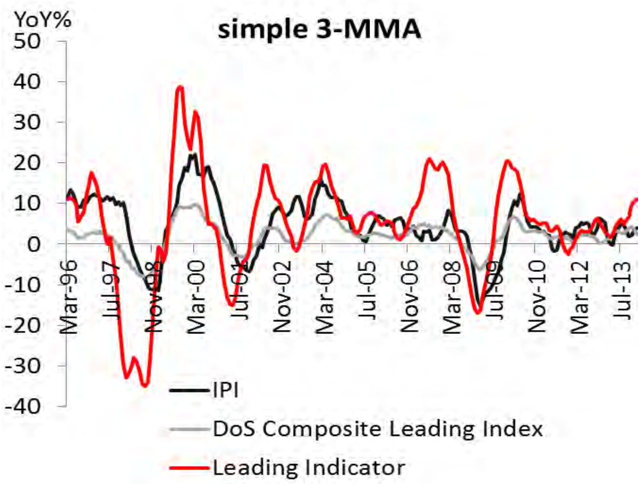


Date: 03/13/14 Time: 17:41
Sample: 1995M01 2014M01
Included observations: 229
Correlations are asymptotically consistent approximations

i	lag	lead
0	0.5221	0.5221
1	0.4098	0.6106
2	0.2993	0.6751
3	0.1817	0.7109
4	0.0824	0.7040
5	-0.0159	0.6890
6	-0.1252	0.6564
7	-0.2369	0.5953
8	-0.3103	0.5103
9	-0.3792	0.4124
10	-0.4061	0.2840
11	-0.4105	0.1498
12	-0.3869	0.0237

Source: CEIC, Bloomberg, MIDFR calculations

Chart 4: ..pointing towards a still volatile trend



Source: CEIC, Bloomberg, MIDFR calculations

Table 1: Performance of the IPI by components

	Weight (% of IPI)	Oct-13	Nov-13	Dec-13	Jan-14	1Q 13	2Q 13	3Q 13	4Q 13	2012	2013
Industrial Production Index - IPI	100	1.7	3.8	4.8	3.6	-0.1	3.9	3.7	3.4	4.4	2.7
Manufacturing	**63.5**	3.3	4.4	6.7	4.7	0.2	3.6	4.3	4.8	5.0	3.2
Export-oriented industries	**50.9**	4.7	3.3	5.2	n.a.	-0.5	1.8	4.2	4.4	3.9	2.5
Electronics & Electricals	20.5	14.3	7.8	6.9	n.a.	-0.5	1.8	4.2	9.7	2.2	4.0
Primary - clustered export-oriented industries	30.4	0.1	1.1	4.3	n.a.	-1.3	2.1	4.3	1.8	4.9	1.7
Domestic-oriented	**12.7**	-0.4	6.4	11.1	n.a.	2.4	8.3	4.4	5.7	8.3	5.2
Mining	30.6	-3.6	1.3	-0.8	1.5	-2.2	4.0	1.5	1.1	2.5	0.4
Electricity	5.9	4.8	6.1	6.0	0.2	4.7	6.3	5.1	5.6	5.1	5.4

Source: DoS, BNM

MIDF RESEARCH is part of MIDF Amanah Investment Bank Berhad (23878 - X).
(Bank Pelaburan)
(A Participating Organisation of Bursa Malaysia Securities Berhad)

DISCLOSURES AND DISCLAIMER

This report has been prepared by MIDF AMANAH INVESTMENT BANK BERHAD (23878-X). It is for distribution only under such circumstances as may be permitted by applicable law.

Readers should be fully aware that this report is for information purposes only. The opinions contained in this report are based on information obtained or derived from sources that we believe are reliable. MIDF AMANAH INVESTMENT BANK BERHAD makes no representation or warranty, expressed or implied, as to the accuracy, completeness or reliability of the information contained therein and it should not be relied upon as such.

This report is not, and should not be construed as, an offer to buy or sell any securities or other financial instruments. The analysis contained herein is based on numerous assumptions. Different assumptions could result in materially different results. All opinions and estimates are subject to change without notice. The research analysts will initiate, update and cease coverage solely at the discretion of MIDF AMANAH INVESTMENT BANK BERHAD.

The directors, employees and representatives of MIDF AMANAH INVESTMENT BANK BERHAD may have interest in any of the securities mentioned and may benefit from the information herein. Members of the MIDF Group and their affiliates may provide services to any company and affiliates of such companies whose securities are mentioned herein This document may not be reproduced, distributed or published in any form or for any purpose.

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.