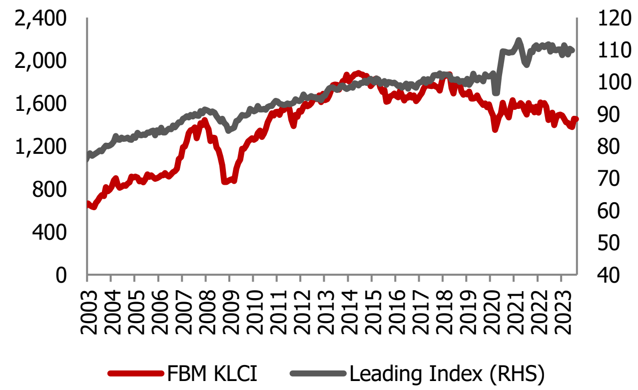
MONTHLY ECONOMIC REVIEW | August 2023

Decline in LI Signals Softer Growth Momentum Ahead

- *LI still signals weaker growth momentum. Malaysia's Leading Index (LI) declined further by -2.1%yoy in Jun-23 (May-23: -1.1%yoy), falling for the 4th straight month due to lower real imports of semiconductors and other basic precious & other non-ferrous metals.*
- *GDP growth moderated to +2.9%yoy in 2QCY23. GDP growth moderated to +2.9%yoy in 2QCY23, with large fall in external trade of goods as well as slower expansion in private consumption.*
- *Stable and sound job market. Labour market remained steady as unemployment rate was unchanged at pandemic low 3.5% in May-23. Labour force and employment continued expanding at +2%yoy and +2.4%yoy, respectively, supported by upbeat domestic economic momentum.*
- *Maintain 2023 GDP growth at +4.2%. Despite weaker-than-expected growth in 2QCY23, we maintain our full-year GDP growth forecast for 2023 at +4.2%. Although we expect the softer growth momentum will continue in 2HCY23 due to weakness in external trade, we still expect domestic demand to drive overall growth.*

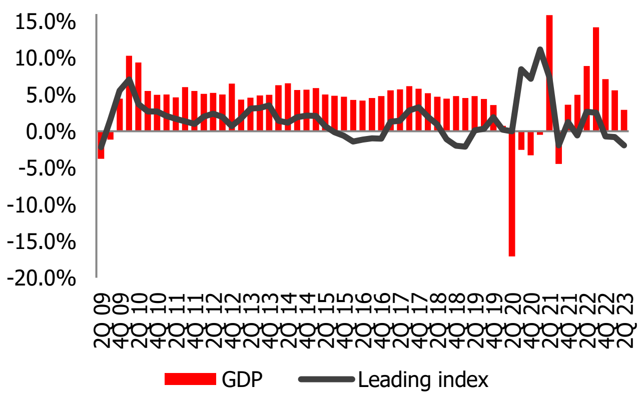
LI still signals weaker growth momentum. Malaysia's Leading Index (LI) declined further by -2.1%yoy in Jun-23 (May-23: -1.1%yoy), falling for the 4th straight month. The continued decline was due to lower real imports of semiconductors (-19.5%yoy) and other basic precious & other non-ferrous metals (-32.1%). Compared to the prior month, LI fell by -0.5%mom after the monthly rebound of +1.7%mom in May-23. The month-on-month decline was attributable to among others decreases in number of housing units approved and real imports of semiconductors. Meanwhile, current economic conditions remained on expansionary, with the Coincident Index (CI) rising by +1.6%yoy (May-23: +3.1%yoy), particular due to higher EPF contributions. The Jun-23 CI was relatively -0.9%mom lower than May-23, reflecting the reduced capacity utilization in the manufacturing sector as well as weaker retail trade. In line the slower CI growth of +2.2%yoy in 2QCY23 (1QCY23: +4.4%yoy), GDP growth moderated during the quarter. With LI falling further, we foresee growth momentum to remain soft in 2HCY23 amid weak external demand and more moderate growth in the domestic economy.

Chart 1: Leading Index vs KLCI (Points)



Source: Macrobond, MIDFR

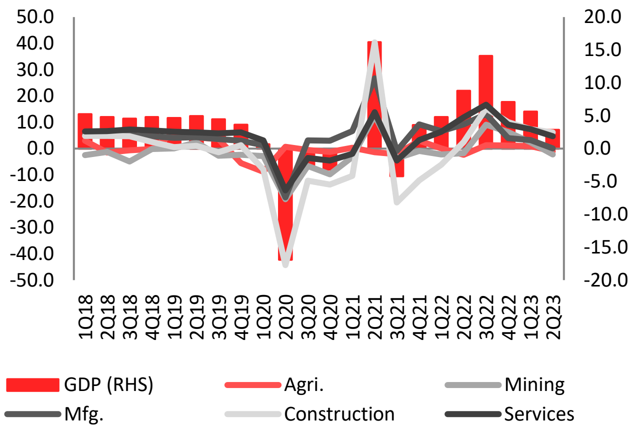
Chart 2: Leading Index vs GDP (YoY%)



Source: Macrobond, MIDFR

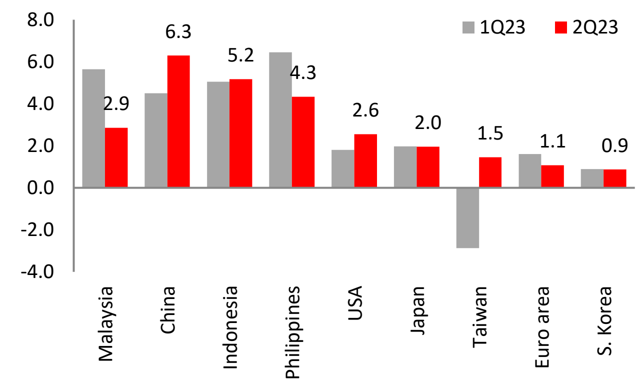
GDP growth moderated to +2.9%yoy in 2QCY23. GDP growth moderated to +2.9%yoy in 2QCY23 (1QCY23: +5.6%yoy). While we anticipated the growth to moderate in view of the slower growth as seen in latest economic indicators, the sharper moderation was largely due to larger fall in external trade of goods as well as slower rise in private consumption. Nevertheless, the sustained rise in domestic demand was the major driver of growth during the quarter, contributing +3.0%-pts to 2QCY23 growth, while net exports contributed a small drag of -0.1%-pt. Thanks to the sharp fall in real imports, the drag from net exports was not significant, cushioned by recovery in services exports. On quarter-to-quarter basis, Malaysia's GDP grew stronger by +1.5%qoq (1QCY23: +0.9%qoq) after seasonal adjustment. The sequential growth was more encouraging, supported by stronger quarterly increase in private consumption (2QCY23: +5.9%qoq; 1QCY23: +2.0%qoq) as well as rebounds in government spending (2QCY23: +4%qoq; 1QCY23: -1.7%qoq) and investment activities (2QCY23: +4.7%qoq; 1QCY23: -1.4%qoq). Given the stronger quarter-to-quarter growth, the sharper moderation in annual GDP growth to a certain extent can be explained by the higher base in 2Q last year, when the economy was first fully reopened after the pandemic. This supports our expectations that overall growth will be more moderate this year against the high growth last year.

Chart 3: GDP by Supply-Side (YoY%)



Source: Macrobond, MIDFR

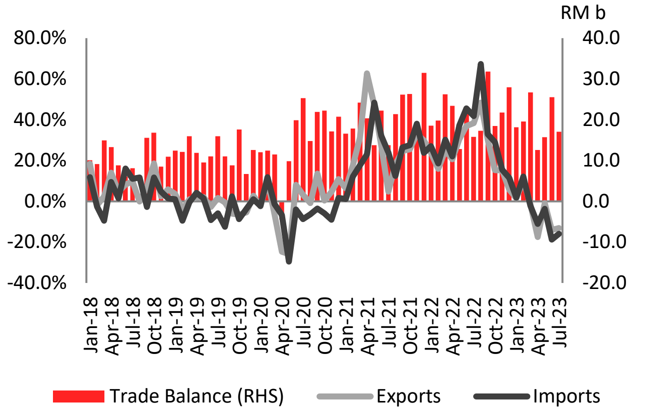
Chart 4: Growth for Selected Countries (YoY%)



Source: Macrobond, MIDFR

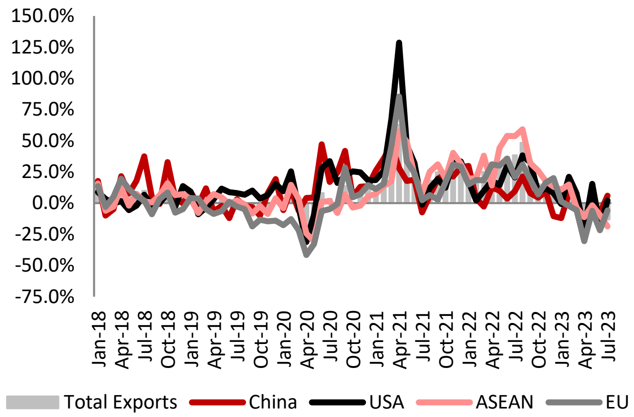
Exports fell further, more than expected. Exports continued to fall at -13.1%yoy in Jul-23 (Jun-23: -14.1%yoy). The continued decline was expected, in view of sharp falls in exports of some regional countries and with recent PMI surveys highlighting sluggishness in overseas demand. The lower exports in Jul-23 was attributable to the further drop in domestic exports (-13%yoy) as well as weaker re-exports (-13.5%yoy). The recent data continued to show the drag from commodity exports, which we believe contributed to the overall weakness in domestic exports, coupled with reduced re-exports, which fell for the second straight month. By destination, rebounds in exports to China and USA was not enough to offset the sharper fall in exports to Japan and ASEAN countries. On month-on-month basis, exports fell by -5.8%mom from the previous month mainly due to weaker exports of manufactured goods, particularly E&E and refined petroleum products. On another note, as exports fell further entering in the first month of 2HCY23, we opine the subdued external trade may continue with commodity exports (particularly palm oil and petroleum) to remain as a downward drag in the coming months, partly because of the lower price effect.

Chart 5: Exports & Imports (YoY%) vs Trade Bal. (RM b)



Source: Macrobond, MATRADE, MIDFR

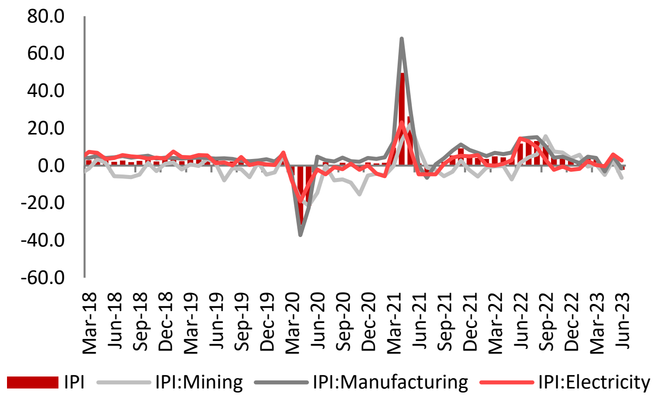
Chart 6: Exports Growth (YoY%) by Major Destination



Source: Macrobond, MATRADE, MIDFR

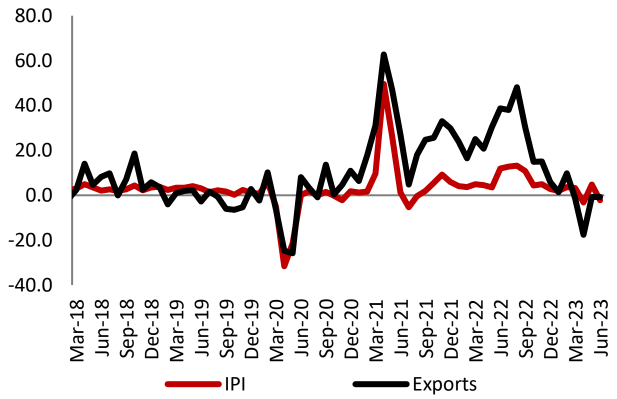
IPI growth turned back to negative. Malaysia's IPI growth weakened more than expected in Jun-23, falling by -2.2%yoy (May-23: +4.8%yoy) because of reduced output in mining and manufacturing sectors. Mining output dropped by -6.4%yoy as production for both crude petroleum and natural gas declined during the month. Manufacturing output fell by -1.6%yoy due to reduction in export-oriented output such as refined petroleum, rubber products, computer & peripherals equipment, and machinery & equipment. We believe sustained rise in electricity generation (Jun-23: +2.8%yoy; May-23: +5.9%yoy) indicates energy demand continued to grow in Jun-23. On month-to-month basis, industrial production was -1.7%mom lower than previous month (May-23: +7.3%yoy) after adjusting to seasonal difference. All sectors registered lower production. We expect the weakness particularly in mining and manufacturing sectors will continue, more or less following similar trend in export performance. In addition, the recent PMI for the manufacturing sector also indicated businesses scaled back production and hirings in reaction to softening demand.

Chart 7: IPI Performances by Sector (YoY%)



Source: Macrobond, MIDFR

Chart 8: IPI vs Exports (YoY%)



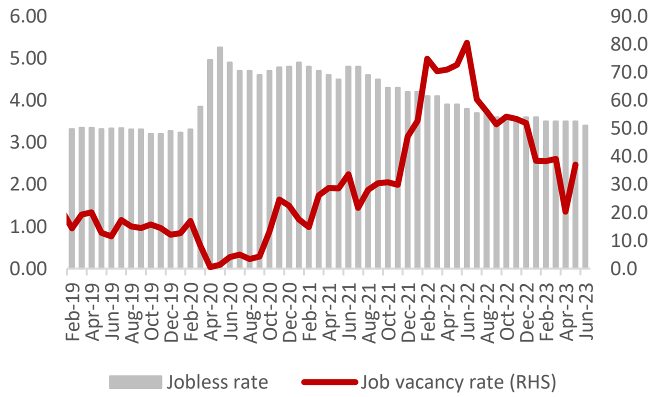
Source: Macrobond, MIDFR

Improving job market. Malaysia's labour market continues to show improvement as the unemployment rate registered a new pandemic low 3.4% in Jun-23. Labour force and employment expanded by +1.9%yoy and +2.3%yoy respectively, supported by upbeat domestic economic momentum. Based on seasonally adjusted data, labour force participation rate increased to 70.2% (May-23: 70.0%) as more people entered the job market, benefiting from the sustained post-pandemic economic expansion. On a monthly basis, employment grew by +0.2%mom which was the 24th consecutive months of positive gains. Meanwhile, unemployment dipped further by -7.8%yoy which marking the 22nd consecutive months of contraction. In addition, outside labour force contracted for the 20th consecutive months by -0.4%yoy. For youth aged 15~24, unemployment rate maintained at a post-pandemic low of 11% but remained above pre-pandemic level (2019: 10.4%). By employment type, employee which made up about 75.4% of the employment market grew steadily by +1.4%yoy while employer and own-account-worker increased by +5%yoy and +6.6%yoy respectively in Jun-23. As at 2QCY23, employment grew by +2.4%yoy (1QCY23: +2.9%yoy) and average jobless rate was at 3.47% (1QCY23: +3.53%yoy). We opine that the improvement in the job market will further reinforce consumer consumption and support the overall GDP growth for this year. However, we do expect slight moderation of employment growth in 2HCY23 due to the slump in external trade performances.

Chart 9: Labour Market Key Indicators (YoY%)

Source: Macrobond, MIDFR

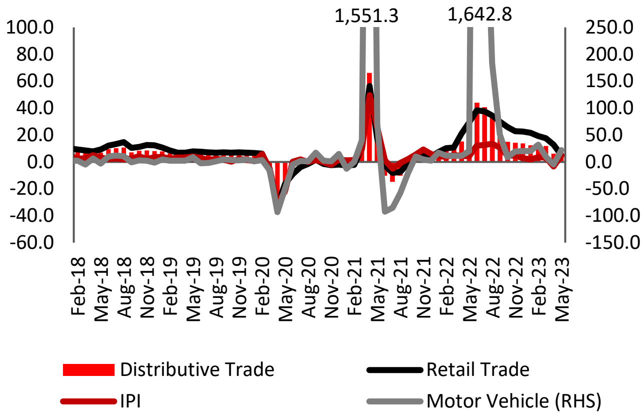
Chart 10: Unemployment Rate (%) vs. Job Vacancies



Source: Macrobond, MIDFR

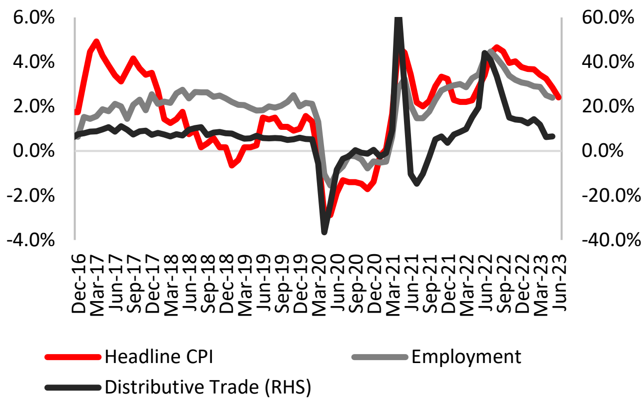
Retail trade growth remained at double-digit pace in 1HCY23. Malaysia's retail trade posted slightly better growth at +5.8%yoy in Jun-23 (May-23: +5.0%yoy). On monthly basis, non-seasonally-adjusted retail trade rebounded and grew by +1.0%mom (May-23: -2.7%mom), and the seasonally-adjusted figure dropped slower at -2.9%mom (May-23: -8.8%mom). Overall distributive trade sales continued to grow, but moderating to +4.3%yoy, the slowest pace since Jan-22. Growth in in wholesale trade and spending on motor vehicles also moderated to +3.1%yoy (May-23: 4.4%yoy) and +3.4%yoy (May-23: 22%yoy), respectively. As for 1HCY23, distributive trade sales increased by +9.1%yoy (1HCY22: +16.6%yoy), with retail sales rising by +13.3%yoy (1HCY22: +19.1%yoy). By quarter, distributive trade sales expanded by +5.7%yoy (1QCY23: +12.9%yoy), in line with the more moderate growth in private consumption as in 2QCY23 GDP. Given the continued expansion, we opine domestic demand, which is underpinned by steady labour market, softening inflation, pick-up in tourism activities and supportive economic policies, will continue to support GDP growth in 2HCY23 as well as for the whole year 2023.

Chart 11: Distributive Trade (DT) (YoY%)



Source: Macrobond, MIDFR

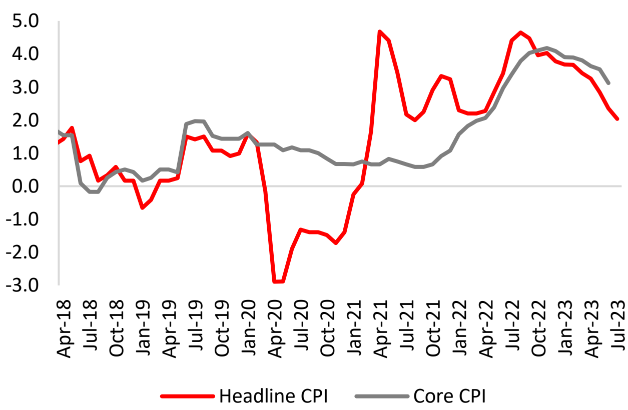
Chart 12: DT vs. CPI vs. Employment (YoY%)



Source: Macrobond, MIDFR

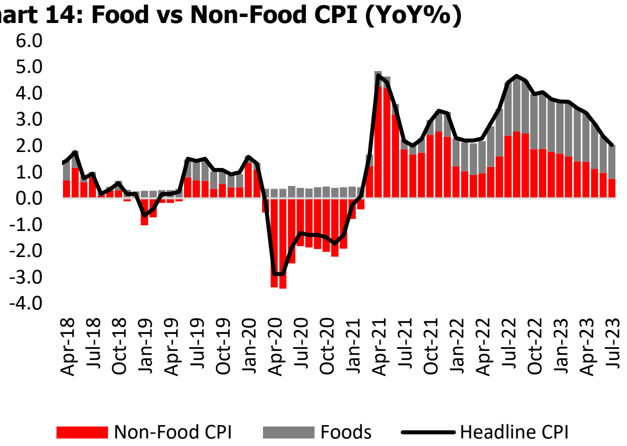
Headline inflation almost at 2-year low. Headline CPI inflation rate moderated further to +2.0%yoy in Jul-23 (Jun-23: +2.4%yoy), the slowest increase since Aug-21. Non-food inflation decelerated to 29-month low at +0.8%yoy, while food inflation softened to more than 1-year low at +4.4%yoy. The moderation of inflation among others was due to high base effects. Core inflation rate moderated below +3.0% level at +2.8%yoy yet still above pre-pandemic average of +1.7%. Similarly, services inflation was at +2.9%yoy, which remained above pre-pandemic average of +2.6%yoy. Average 7MCY23 headline inflation was +3.0% (2022: +3.4%) and core inflation rate was +3.5% (2022: +3.0%). On monthly basis, headline inflation remained firm registering positive gains of +0.1%mom core inflation stagnant. Steady core inflation trend in Malaysia is highly driven by strong consumer demand while cost factors are on slowdown pace. The moderation of inflationary pressure is a positive signal especially for domestic demand to stay on expansionary path in 2HCY23. However, persistent high domestic food inflation to remain as downside risk factor amid climate change and geopolitical war impacts on global agriculture output.

Chart 13: Headline vs. Core CPI (YoY%)



Source: Macrobond, MIDFR

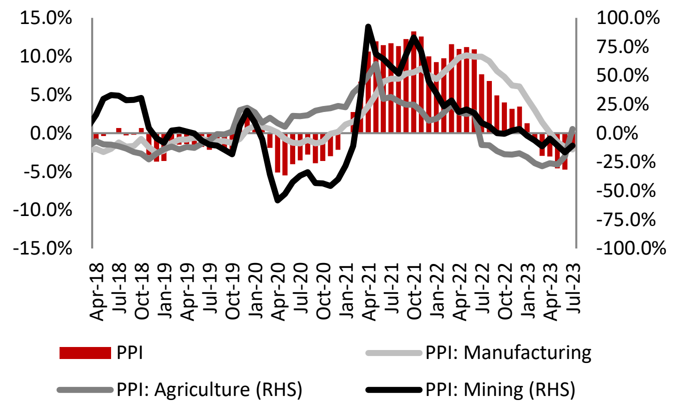
Chart 14: Food vs Non-Food CPI (YoY%)



Source: Macrobond, MIDFR

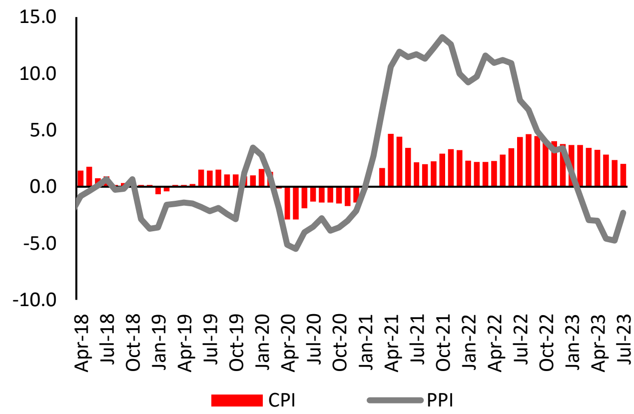
PPI fell further for the 6th straight month. Producers' prices deflated for the 6 consecutive month in Jul-23, declining by -2.3%yoy (Jun-23: -4.8%yoy). The contraction continued as manufacturing input prices deflated by -2.1%yoy, the steepest in 3-month. Producer prices for the mining sector also declined further by -10.8%yoy (Jun-23: -16.6%yoy). In contrast, the production cost for agriculture, forestry & fishing ended 1-year of contraction, rebounding to +3.6%yoy (Jun-23: -20.4%yoy). PPI for electricity & gas rose at the softest pace in 3 months at +0.1%yoy while inflation for water supply eased slightly to +3.1%yoy (Jun-23: +3.2%yoy). By the processing stage, prices for crude materials dropped by -6.3%yoy (Jun-23: -18.7%yoy), attributable to the decline in prices of non-food materials which more than offset higher inflation in crude food materials and feedstuffs. Cost for intermediate materials, supplies & components declined by -3.3%yoy, the largest drop in 4-month. On the other hand, growth in prices for finished goods inched up by +3.4%yoy (Jun-23: +3.3%yoy). On a month-on-month basis, PPI rose +0.2%mom after -0.3%mom decline last month. Given the continued decline in PPI, we foresee this would explain the more moderate reading in CPI inflation. With the exception of rising input costs for foods and feedstock, we expect reduced cost pressures will not compel local suppliers to raise selling prices. However, elevated food inflation will be an upside risk to the near-term inflation outlook.

Chart 15: PPI (YoY%)



Source: Macrobond, MIDFR

Chart 16: PPI vs CPI (YoY%)



Source: Macrobond, MIDFR

Maintain 2023 GDP growth at +4.2%. Despite the weaker-than-expected growth in 2QCY23, we maintain our full-year GDP growth forecast for 2023 at +4.2%. Although we expect the softer growth momentum will continue in 2HCY23 due to weakness in external trade, we still expect domestic demand to drive overall growth. We are optimistic that domestic factors, such as encouraging labour market conditions (and positive income growth), decelerating inflation, increased tourist arrivals (and spending), will continue to support domestic spending activities. This will support growth in domestic-oriented sectors, particularly services and construction. Furthermore, increased public sector spending and progress in infrastructure projects will translate into increased construction activities and business activities. Nevertheless, we keep a cautious view on several risks to growth outlook, which could come from sharper fall in external demand, weaker growth in major economies (such as China and the US), intensified geo-political tensions and trade war, and supply shocks, be it from fluctuations in commodity prices or supply chain disruptions as production slowed.

Table 1: Macroeconomic Past Performances (%)

(YoY%) Unless Stated Otherwise	2019	2020	2021	2022	2023f
Real GDP	4.4	(5.5)	3.3	8.7	4.2
Govt. Consumption	1.5	4.1	6.4	4.5	3.0
Private Consumption	7.7	(3.9)	1.9	11.2	6.1
Govt. Investment	(10.7)	(21.2)	(11.1)	5.3	4.8
Private Investment	1.6	(11.9)	2.7	7.2	5.4
Exports of goods & services	(1.0)	(8.6)	18.5	14.5	1.5
Imports of goods & services	(2.4)	(7.9)	21.2	15.9	1.9
Net Exports	11.2	(13.7)	(4.0)	(1.0)	(3.6)
Agriculture etc.	1.9	(2.4)	(0.1)	0.1	0.8
Mining & Quarrying	(0.6)	(9.7)	0.9	2.6	2.6
Manufacturing	3.8	(2.7)	9.5	8.1	1.4
Construction	0.4	(19.3)	(5.1)	5.0	6.5
Services	6.2	(5.2)	2.2	10.9	5.8
Exports of Goods (f.o.b)	(0.8)	(1.1)	26.1	25.0	(3.4)
Imports of Goods (c.i.f)	(3.5)	(5.8)	23.3	31.3	(1.9)
Trade Balance, RMb	145.7	183.3	257.2	253.7	227.2
Consumer Price Index	0.7	(1.1)	2.5	3.4	3.0
Current Account, % of GDP	3.6	4.2	3.9	3.1	2.2
Fiscal Balance, % of GDP	(3.5)	(6.3)	(6.5)	(5.2)	(4.9)
Federal Government Debt, % of GDP	52.4	62.1	63.4	60.3	60.6
Unemployment rate, %	3.3	4.5	4.6	3.8	3.5
Year-End or Unless Stated Otherwise	**2019**	**2020**	**2021**	**2022**	**2023f**
Brent Crude Oil (Avg)	64.3	43.3	70.9	99.0	80.0
Crude Palm Oil (Avg)	2,079	2,781	4,437	5,094	3,500
USD/MYR (Avg)	4.14	4.20	4.14	4.40	4.43
USD/MYR (end-year)	4.09	4.02	4.17	4.40	4.20
Overnight Policy Rate (%)	3.00	1.75	1.75	2.75	3.00

Source: Macrobond, DOSM, MIDFR

August 2023 Key Economic Events

1 Aug: Fitch downgrades US credit rating a notch from AAA to AA+. Rating agency Fitch on Tuesday (Aug 1) downgraded the US government's top credit rating to AA+ from AAA, citing an expected fiscal deterioration over the next three years as well as a high and growing general government debt burden.

3 Aug: Global semiconductor giant Infineon to invest 5.0bil euros in Malaysia. Infineon Technologies AG will invest up to 5.0 billion euros (about RM24.9 billion) over the next five years to build the world's largest 200mm silicon carbide (SiC) power fabrication (power fab) plant in Malaysia. The company said the investment on its Kulim facility will lead to an annual SiC revenue potential of about EUR7.0b by end of the decade.

4 Aug: Malaysia on right track to draw more high-impact investments, says Zafrul. Malaysia is on right track to realise the country's efforts to attract high-impact investments, which would elevate the economy to a higher level. Investment, Trade and Industry Minister Tengku Datuk Seri Zafrul Abdul Aziz said available incentives and focus on key sectors are able to drive employment, household income and economic sustainability.

8 Aug: Subsidy increased to RM500 per MT of paddy production, says PM. Prime Minister Datuk Seri Anwar Ibrahim announced an increase in the Padi Price Subsidy Scheme rate from RM360 to RM500 per metric tonne (MT) of paddy production, effective from Wednesday (Aug 9). With the increase, paddy farmers would receive at least RM1,700 per MT of their paddy production, giving them better income.

8 Aug: Moody's cuts ratings of 10 U.S. banks and puts some big names on downgrade watch. Moody's cut the credit ratings of a host of small and mid-sized U.S. banks late Monday and placed several big Wall Street names on negative review. The firm lowered the ratings of 10 banks by one rung.

12 Aug: Anwar coalition holds on to power in three states in Malaysia polls. Malaysia elections in six states on Saturday essentially ended in a draw between the ruling and opposition coalitions, with each retaining control of three. However, the opposition was able to gain seats in all the contests.

16 Aug: Fed officials see 'upside risks' to inflation possibly leading to more rate hikes, minutes show. Federal Reserve officials expressed concern at their most recent meeting about the pace of inflation and said more rate hikes could be necessary in the future unless conditions change, minutes released Wednesday from the session indicated. That discussion during a two-day July meeting resulted in 25bps hike that markets generally expect to be the last one of this cycle.

21 Aug: China's central bank trims 1-year rate, but unexpectedly leaves 5-year rate unchanged. China's central bank cut its one-year loan prime rate Monday, while leaving its five-year rate unchanged. The decisions are weaker than expectations for more muscular policy intervention following a raft of data that pointed to faltering growth momentum in the world's second-largest economy.

21 Aug: Autonomous Rapid Transit tram prototype to start test run in Kuching from September 4 to October 31, says state minister. The engineering run for world's first prototype hydrogen-powered Autonomous Rapid Transit (ART) smart tram is set to commence at the Isthmus here from September 4 until October 31, said state Transport Minister Datuk Seri Lee Kim Shin.

22 Aug: MITI, agencies to focus on domestic direct investment. The National Investment Council meeting on Aug 22 agreed for the Ministry of Investment, Trade and Industry (MITI) and its related agencies to focus on domestic direct investment (DDI). Minister Datuk Seri Zafrul Tengku Abdul Aziz said setting of key performance indicator is not only concentrating on foreign direct investment (FDI) but also DDI.

24 Aug: Rafizi: Cabinet approves progressive wage policy, details to be tabled in Budget 2024. The progressive wage system policy has been approved at the Cabinet level and the details will be tabled during the upcoming Budget 2024 in October. Economy Minister Rafizi Ramli said the system is expected to be implemented in April or May next year.

24 Aug: Govt will continue efforts to keep rising prices in check, says PM Anwar. The government will continue to find ways to ensure that the prices of goods in this country are at a level that does not burden the people, Prime Minister Datuk Seri Anwar Ibrahim said. He said these include increasing food production as well as the introduction of additional measures.

25 Aug: Fed Chair Powell calls inflation 'too high' and warns that 'we are prepared to raise rates further'. Federal Reserve Chair Jerome Powell called for more vigilance in the fight against inflation, warning that additional interest rate increases could be yet to come. Acknowledging progress has been made and saying the Fed will be careful in where it goes from here, he said inflation is still above comfortable level. He noted the Fed will remain flexible as it contemplates further moves, but gave little indication it's ready to start easing soon.

25 Aug: ECRL project has achieved more than 48pc in work progress. Construction of the East Coast Rail Link (ECRL) project has achieved 48.77 per cent progress, said Malaysia Rail Link Sdn Bhd chairman Tan Sri Mohd Zuki Ali. The work progress was in line with the development of the project from Kota Baru to Gombak Integrated Terminal scheduled for completion in December 2026 for the ECRL service to operate in January 2027.

28 Aug: Malaysia's domestic banks have limited exposure to Country Garden. BNM said that banks incorporated in Malaysia faced limited financial stability risk from exposure to China's largest property developer, Country Garden. Such banks' exposure to Country Garden Real Estate Sdn Bhd, the developer's wholly-owned subsidiary, amounted to less than 0.1% of total banking system loans and bonds by June 2023, the bank told Reuters in an email.

29 Aug: PM launches energy transition roadmap, including RM2bil facility. Prime Minister Anwar Ibrahim launched the National Energy Transition Roadmap (NETR) today, with Putrajaya allocating a RM2 billion "seed fund" as an energy transition facility. Anwar said while Malaysia's move to embrace sustainability has been gaining momentum, there is a need to ensure energy is affordable and secure.

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