1 November 2023

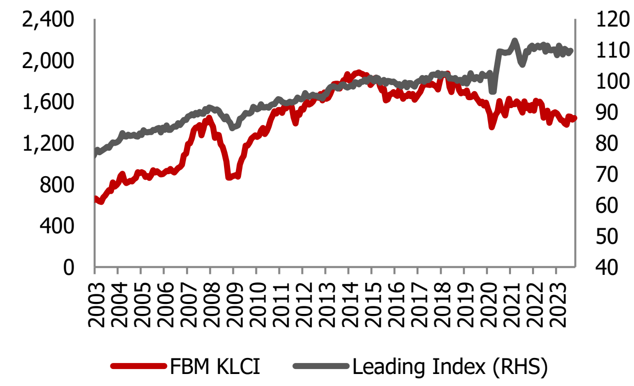
MONTHLY ECONOMIC REVIEW | October 2023

LI Signals Malaysia's Growth Prospects May Get Better

- *LI fell slower at -0.5%yoy in Aug-23. There are signs of improvement in growth prospects as the pace of contraction in Malaysia's Leading Index (LI) slowed to -0.5%yoy in Aug-23 (Jul-23: -1.0%yoy).*
- *Exports contracted slower at -13.7%yoy in Sep-23. Exports fell further for the 7th month but at slower pace of -13.7%yoy (Aug-23: -18.7%yoy). Compared to prior month, exports rebounded and surged by +8.2%mom driven primarily by stronger exports of E&E (+25.7%mom) and optical & scientific equipment (+12.5%mom).*
- *Healthy job market. Labour market conditions remained encouraging as unemployment rate remained at pandemic low of 3.4% in Aug-23. Labour force and employment continued expanding +1.8%yoy and +2.1%yoy, respectively, supported by upbeat domestic economic momentum.*
- *Economy to grow at +4.2% this year. Looking at the sequentially better LI reading and improvement in the external trade, we maintain our projection that Malaysia's economy will grow at +4.2% this year.*

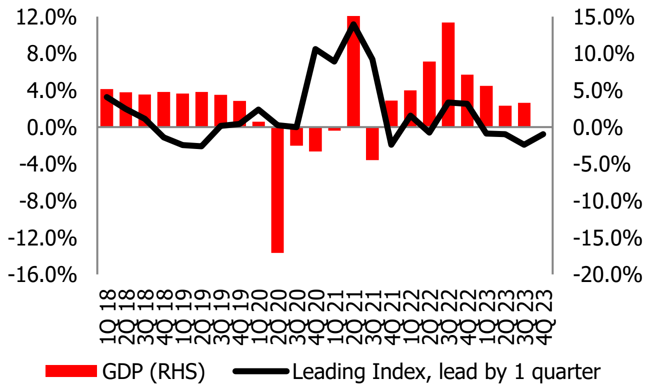
LI fell slower at -0.5%yoy in Aug-23. There are signs of improvement in growth prospects as the pace of contraction in Malaysia's Leading Index (LI) slowed to -0.5%yoy in Aug-23 (Jul-23: -1.0%yoy). It was the slowest decline in the recent sequence despite falling for the 6th straight month. Components which recorded positive contributions were *the number of housing units approved*, *the number of new companies registered*, and *real imports of other basic precious & other non-ferrous metals*. From month-to-month perspective, LI rebounded and expanded by +0.7%mom (Jul-23: -0.8%mom) mainly due to strong rise in *real imports of other basis precious & other non-ferrous metals* and increase in *real money supply (M1)*. Meanwhile, the Coincident Index (CI) continued to increase by +2.1%yoy, growing for 2 years with expansion recorded in all components except industrial production. The CI was virtually unchanged, only +0.04%mom higher than prior month (Aug-23: +0.2%mom) as increased *employment* and *salary & wages in the manufacturing* sector were offset by declines in *manufacturing capacity utilization*, *real contribution to EPF* and *industrial production*. Sustained growth in CI was in line with positive GDP growth during the quarter, as shown by the advance estimate. Reading from the improvement (i.e. slower year-on-year decline) in LI, we foresee growth momentum would improve from 4QCY23.

Chart 1: Leading Index vs KLCI (Points)



Source: Macrobond, MIDFR

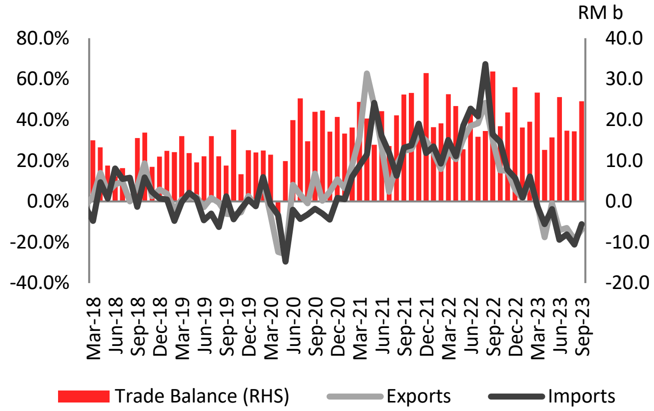
Chart 2: Leading Index vs GDP (YoY%)



Source: Macrobond, MIDFR

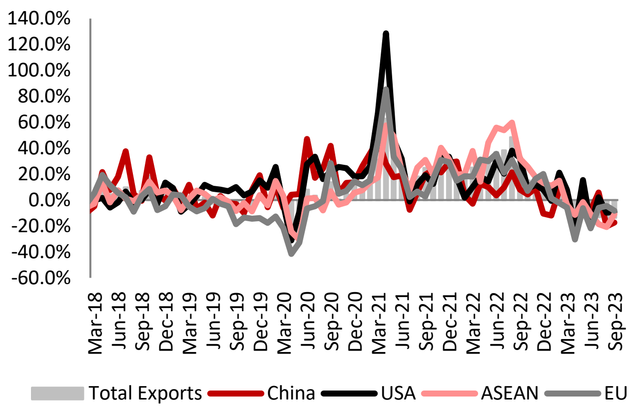
Exports contracted slower at -13.7%yoy in Sep-23. Total trade continued to decline albeit at slower pace of -12.6%yoy (Aug-23: -19.9%yoy). The slower fall was attributable to a +5.4%mom rise in monthly total trade to RM224.4b, the highest in 7 months. Exports jumped by +8.2%mom, relatively faster than +2.1%mom increase in imports, and as a result the trade surplus widened to RM24.5b (Aug-23: RM17.2b). Although exports fell further for the 7th month since Mar-23, the pace of annual contraction slowed to -13.7%yoy (Aug-23: -18.7%yoy). The improvement (as shown in the slower contraction) was better than expected because the decline in Sep-23 was not as sharp as ours and market predictions. In particular, E&E exports, which accounted for 43.7% of total exports, recorded a slower decline. Both domestic exports and re-exports fell slower at -12.4%yoy and -17.9%yoy (Aug-23: -13.8%yoy and -33.8%yoy), respectively. The continued decline in overall exports was dragged down by weak exports of crude and refined petroleum products, E&E, palm oil & palm oil-based products and LNG, compared to a year ago. Compared to the prior month, exports rebounded and surged by +8.2%mom driven primarily by stronger exports of manufactured goods, especially E&E (+25.7%mom) and optical & scientific equipment (+12.5%mom). Given the weak overseas demand, this explains the continued decline in exports relative to a year ago. For the 3QCY23, exports of goods fell sharper at -15.2%yoy (2QCY23: -11.1%yoy).

Chart 3: Exports & Imports (YoY%) vs Trade Bal. (RM b)



Source: Macrobond, MATRADE, MIDFR

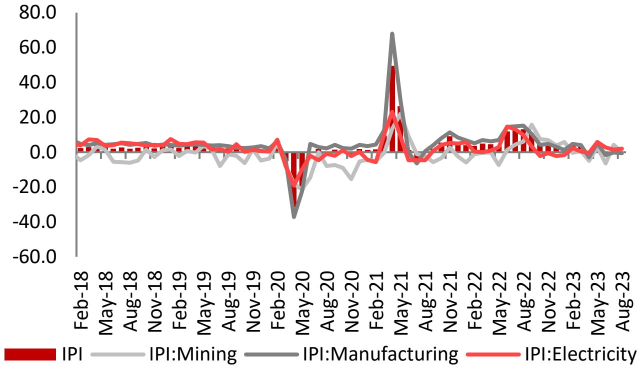
Chart 4: Exports Growth (YoY%) by Major Destination



Source: Macrobond, MATRADE, MIDFR

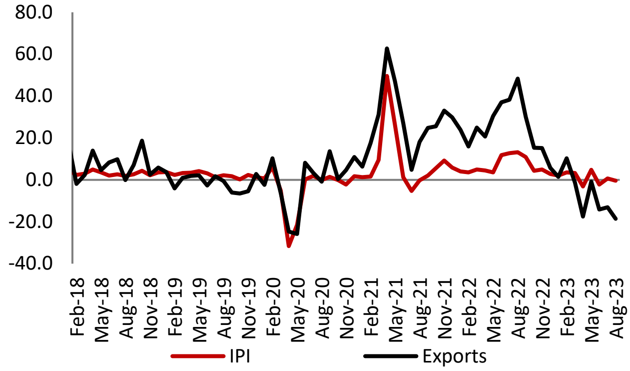
IPI fell by -0.3%yoy in Aug-23. IPI fell again by -0.3%yoy after the 1-month rebounded to +0.7%yoy in Jul-23. It was not as sharp as our and market expectations, but the decline was in line with the sharper fall in external trade during the month. The decline in Aug-23 IPI was due to the weak manufacturing production (Aug-23: -0.6%yoy; Jul-23: -0.2%yoy), particularly lower production in the export-oriented sectors. Mining output growth eased to +0.1%yoy (Jul-23: +4.2%yoy) as the increased natural gas production was offset by weaker output of crude petroleum. Electricity generation, on the other hand, sustained positive growth (+1.9%yoy) for the 4th straight month on the back of higher electricity demand. In the months to come, we believe the performance of IPI will continue to be influenced by external trade performance given manufacturing output accounted for more than two-thirds of the IPI calculation but will be partly cushioned by the strength and sustained growth in domestic demand.

Chart 5: IPI Performances by Sector (YoY%)



Source: Macrobond, MIDFR

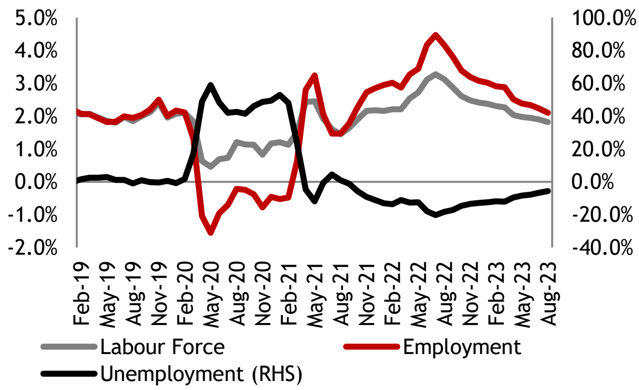
Chart 6: IPI vs Exports (YoY%)



Source: Macrobond, MIDFR

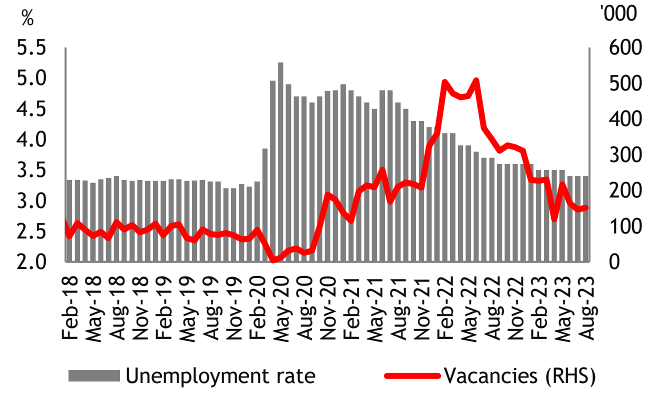
Healthy job market. Labour market conditions remained encouraging as unemployment rate remained at pandemic low of 3.4% in Aug-23. Labour force and employment continued expanding +1.8%yoy and +2.1%yoy, respectively, supported by upbeat domestic economic momentum. On month-on-month basis, employment grew +0.1%mom, marking the 26th-straight months of positive gains. Unemployment dipped further by -8.9%yoy, marking the 24th-consecutive months of contraction rate. The unemployed persons dropped further by -3.8%mom to 557K, approximately 38K higher than average jobless persons 519K in 2019. In addition, outside labour force was reduced by -0.1%yoy, registering the 22nd-straight months of negative growth rate. For youth aged 15~24, unemployment rate hit a new pandemic low of 10.8%, but remained higher than pre-pandemic (2019: 10.4%). By employment type, employee which made up about 75.4% of the employment grew steadily by +1.3%yoy while employer and own-account-worker increased by +4.6%yoy and +5.8%yoy respectively in Aug23. The strengthening job market in our view will further reinforce consumer consumption and support overall GDP growth for this year.

Chart 7: Labour Market Key Indicators (YoY%)



Source: Macrobond, MIDFR

Chart 8: Unemployment Rate (%) vs. Job Vacancies

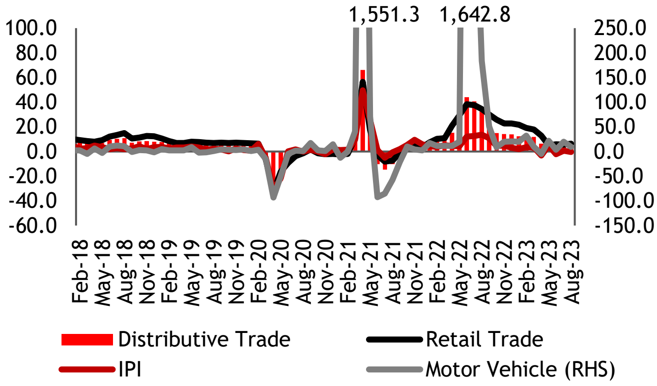


Source: Macrobond, MIDFR

Retail trade sales growth improved to 4-month high. Malaysia's retail trade growth posted at +6.7%yoy in Aug-23, the strongest pace since May-23. On month-on-month basis, non-seasonally adjusted retail trade increased by +1.4%mom. Overall distributive trade sales increased by +6.7%yoy and +2%mom. By component, sales of motor vehicles remained solid grew by +9.7%yoy and wholesale trade growth at 5-month high

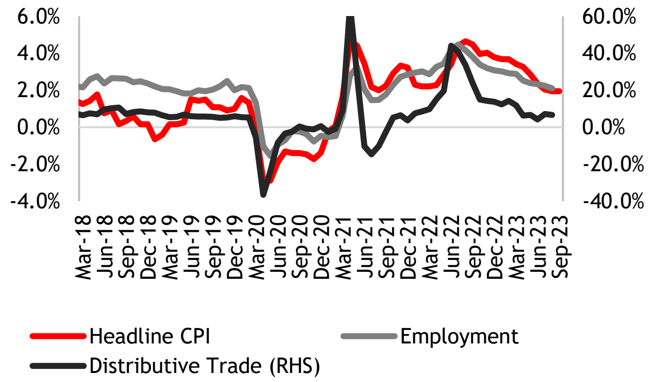
+6.2%yoy. In terms of seasonally-adjusted volume, distributive trade stayed unchanged while motor vehicles and retail trade up by +3.3%mom and +0.2%mom respectively. The resilient of consumer demand in Malaysia is in tandem with the healthy job market development and softening inflationary pressure. Looking ahead, we foresee sanguine domestic outlook for remainder of 2HCY23 amid further pick-up in tourism activities and supportive & accommodative economic policies from both fiscal and monetary sides.

Chart 9: Distributive Trade (YoY%)



Source: Macrobond, MIDFR

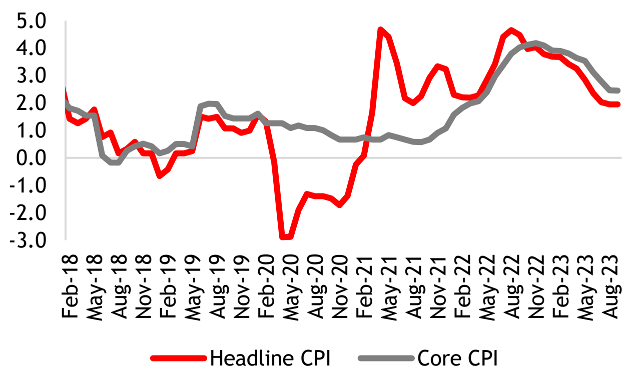
Chart 10: DT vs. CPI vs. Employment (YoY%)



Source: Macrobond, MIDFR

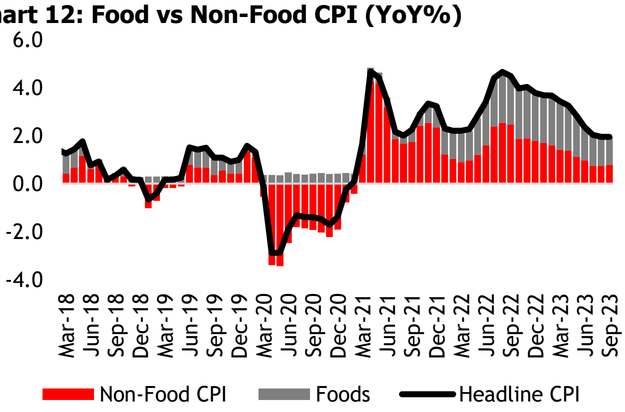
Headline inflation rate descended below +2.0%. Headline inflation eased to +1.9%yoy in Sep-23 (Aug-23: +2.0%yoy), the slowest inflation since Mar-21. Non-food inflation rate skidded to +0.9%yoy while food inflation rate moderated to 19-month low at +3.9%yoy. The softening inflationary pressure among others was due to high base effects. Core inflation rate maintained at +2.5%yoy yet still above pre-pandemic average of +1.7%. Average 9MCY23 headline inflation was +2.8% (2022: +3.4%) and core inflation rate was +3.3% (2022: +3.0%). On sequential month basis, headline and core inflation remained firm registering positive gains of +0.1%mom and +0.3%mom respectively. The softening inflationary pressure is a positive signal especially for domestic demand to stay on expansionary path in 2HCY23. However, recent uptick in global energy prices and further depreciation of ringgit are among downside risk factors especially in pressuring domestic food inflation rate.

Chart 11: Headline vs. Core CPI (YoY%)



Source: Macrobond, MIDFR

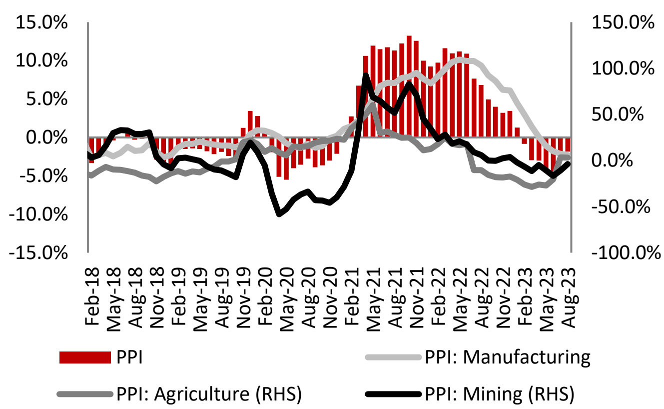
Chart 12: Food vs Non-Food CPI (YoY%)



Source: Macrobond, MIDFR

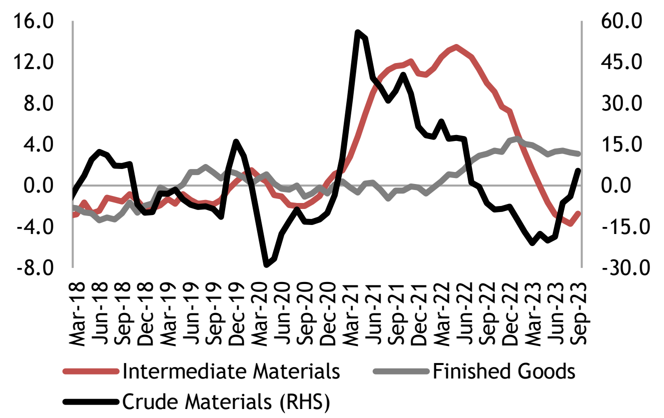
PPI registered first inflation in 8 months. Producer prices increased by +0.2% in Sep-23, marking the first annual inflation after 7 straight months of deflation. The increase in PPI was underpinned by inflation in the mining (Sep-23: +6.9%yoy; Aug-23: -3.8%yoy), agriculture, forestry & fishing (Sep-23: +3.2%yoy; Aug-23: -1.0%yoy) and electricity, gas & water supply (Sep-23: +0.5%yoy; Aug-23: -0.1%yoy) sectors. In contrast, the cost of production for the manufacturing sector, the largest component in the index, continued to register deflation albeit slower at -0.8%yoy (Aug-23: -2.3%yoy). By the stage of production, production costs for crude materials ended a deflationary run that started in Aug-22 and recorded +5.4%yoy inflation (Aug-23: -4.0%yoy), in tandem with the commodity price movement which also resulted in rising producer prices in the primary industries. Prices of intermediate goods, however, deflated further for the 6th month in a row but at slower pace of -2.7%yoy (Aug-23: -3.7%yoy). Cost of production for finished goods continued to increase at +3.1%yoy (Aug-23: +3.2%yoy). Against the previous month, producers' inflation accelerated +0.9%mom compared to no monthly inflation in the previous month. Going forward, given the PPI inflation still remained below CPI inflation (Sep-23: +1.9%yoy), we foresee pressures on local producers to increase selling prices is limited. While elevated commodity prices will continue to influence cost pressures in the primary sectors and crude material prices, we opine that the effects of weak ringgit and global food inflation would influence inflation outlook in the coming months.

Chart 13: PPI by Sector (YoY%)



Source: Macrobond, MIDFR

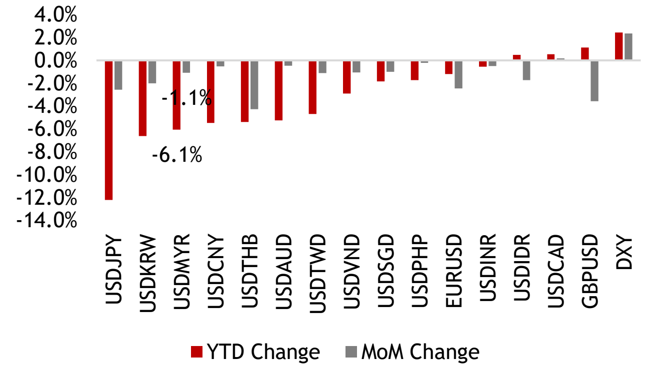
Chart 14: PPI by Processing Stage (YoY%)



Source: Macrobond, MIDFR

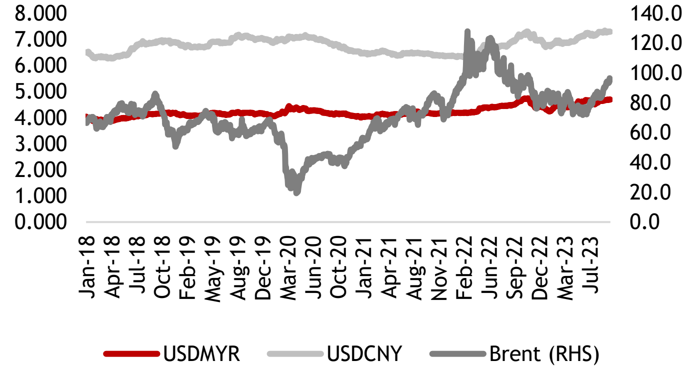
Ringgit touched an all-time low in Oct-23. Malaysian ringgit depreciated -1.4%mom to RM4.764 on the stronger dollar. In terms of mean, the ringgit averaged weaker, depreciating to RM4.747. On 23 October 2023, ringgit registered the lowest daily closing at RM4.794 as dollar strengthened on the back of the rise in US treasury yields following the recently escalated conflicts in the Middle East. Despite better-than-expected economic data out of China provided little support to the ringgit as the financial market movements (from the Israel-Palestine conflict and expectations on Fed's future decisions) posed a greater influence on the ringgit's performance. Moreover, the movement in commodity prices was unfavourable towards the ringgit as the Brent crude oil prices declined by -8.3%mom to USD87.41pb; averaging -4.2%mom lower at USD88.70pb compared to Aug-23. Despite the recent weakness, we maintain our forecast for ringgit to appreciate heading into the year-end, with our point focus remained at RM4.30 by end-2023. We foresee EM currencies, including the ringgit, will benefit from the return of fund flow into riskier markets when safe-haven demand for dollar subsides and once the Fed announce the end of its tightening cycle. Given still positive economic fundamentals, with continued growth in domestic economy, and easing inflation, we believe there is still downside bias which could prevent ringgit from appreciating such as the absence of a definitive pause by the Fed, elevated treasury yields and further escalation in the geopolitical risks.

Chart 15: Monthly and YTD Ringgit Performance vs. Regional Currencies



Source: Macrobond, MIDFR

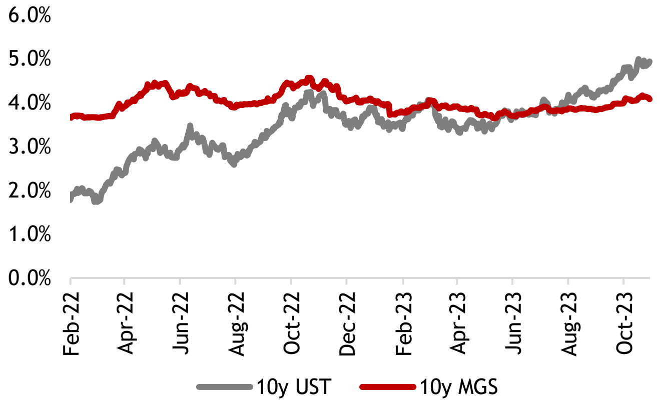
Chart 16: Movement of Malaysian Ringgit vs. Chinese Yuan and Brent Crude Oil Price (USD pb)



Source: Macrobond, MIDFR

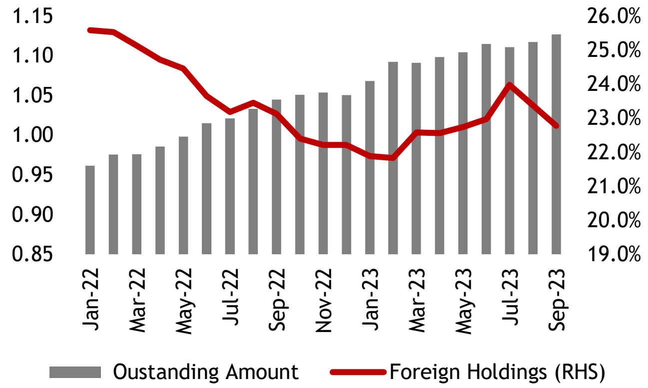
Local bond markets impacted by risk aversion. The yield for the benchmark 10y MGS rose by +10bps to 4.07% in Oct-23. As a result, the monthly average for the 10y MGS yield rose by +17bps to 4.08% during the month. In terms of foreign holding of Malaysian bonds, based on the latest data in Sep-23, foreign holdings declined for the second month to RM269.7b (Aug-23: RM274.2b). Consequently, the share of foreign holdings of govvies, which stood at RM256.6b, fell further to 22.8% of total outstanding government bonds (Aug-23: 23.4%), the lowest in 4 months and below the pre-pandemic level (2019 average: 23.1%). We foresee the domestic bond market to perform better in the coming months as we expect no further repricing, previously influenced by the higher UST and risk aversion from the conflict in Middle East. In other words, we believe the MGS yields likely have peaked and the 10y MGS yield will move downward and end the year at 3.77%. We factored in the assumptions that the Fed will finally end its tightening cycle. With no further widening of the FFR-OPR differentials, we foresee global funds to flow back into emerging markets.

Chart 17: 10y MGS vs 10y UST Yields (%)



Source: Macrobond, MIDFR

Chart 18: Share of Foreign Holding (%) vs Outstanding MGS/MGII/Treasury Bills (RM t)



Source: Macrobond, MIDFR

Economy to grow at +4.2% this year. Looking at the sequentially better LI reading and improvement in the external trade, we maintain our projection that Malaysia's economy will grow at +4.2% this year. We believe sustained growth in domestic spending will be supported by positive labour market, with more people entering the job market and getting employed, and increased tourist spending. We also foresee continued improvement in external trade would be supportive of better growth momentum from 4QCY23 onwards. As we expect the external trade recovery to continue into 2024, this will support Malaysia's economy to grow stronger at +4.7% next year. Nevertheless, we remain cautious on downside risks such as recent escalation of geo-political tensions, another round of supply disruptions, fluctuations in the commodity and financial markets and possibility of sharp decline in external demand. We are also wary of the effects of imported inflation and the government policy changes on consumer prices, and the adverse impact to consumer purchasing power as well as the overall spending outlook.

Table 1: Macroeconomic Past Performances (%)

(YoY%) Unless Stated Otherwise	2020	2021	2022	2023f	2024f
Real GDP	(5.5)	3.3	8.7	4.2	4.7
Govt. Consumption	4.1	6.4	4.5	2.0	2.5
Private Consumption	(3.9)	1.9	11.2	5.3	5.2
Gross Fixed Capital Formation	(14.4)	(0.8)	6.8	7.4	3.3
Govt. Investment	(21.2)	(11.1)	5.3	7.6	2.8
Private Investment	(11.9)	2.7	7.2	7.3	3.4
Exports of goods & services;	(8.6)	18.5	14.5	(5.3)	4.2
Goods Exports	(0.7)	21.4	11.1	(11.8)	3.4
Services Exports	(47.8)	(8.2)	56.8	52.7	8.6
Imports of goods & services;	(7.9)	21.2	15.9	(5.7)	3.5
Goods Imports	(3.6)	23.8	14.6	(10.2)	2.8
Services Imports	(25.3)	7.7	23.9	19.5	6.3
Net Exports	(13.7)	(4.0)	(1.0)	(1.2)	13.5
Agriculture etc.	(2.4)	(0.1)	0.1	(0.1)	1.5
Mining &	(9.7)	0.9	2.6	0.2	2.6
Manufacturing -2.7	(2.7)	9.5	8.1	1.4	4.0
Construction	(19.3)	(5.1)	5.0	7.5	5.2
Services	(5.2)	2.2	10.9	6.0	5.6
Exports of Goods (f.o.b)	(1.1)	26.1	24.9	(6.4)	5.9
Imports of Goods (c.i.f)	(5.8)	23.3	31.0	(6.9)	4.2
Headline CPI Inflation (%)	(1.1)	2.5	3.4	3.0	3.5
Current Account, % of GDP	4.2	3.9	3.1	2.2	2.6
Fiscal Balance, % of GDP	(6.2)	(6.4)	(5.6)	(5.2)	(4.7)
Federal Government Debt, % of GDP	62.0	63.2	60.3	61.9	62.3
Unemployment Rate (%)	4.48	4.58	3.82	3.50	3.30
Brent Crude Oil (Avg), USD per barrel	41.6	71.5	102.0	83.0	85.0
Crude Palm Oil (Avg), MYR per tonne	2,775	4,486	5,262	3,800	4,200
USD/MYR (Avg)	4.20	4.14	4.40	4.48	4.25
USD/MYR (End-period)	4.02	4.17	4.35	4.30	4.10
MGS 10-Yr Yield (Avg)	2.84	3.23	4.07	3.80	3.70
MGS 10-Yr Yield (End-period)	2.65	3.59	4.04	3.77	3.60
Overnight Policy Rate (%)	1.75	1.75	2.75	3.00	3.00

Source: Macrobond, DOSM, MIDFR

October 2023 Key Economic Events

2 Oct: Biden tells Congress to "get to work" on longer-term government funding deal after averting shutdown. President Biden late Saturday signed the bipartisan deal put forward by House Speaker Kevin McCarthy to keep the government funded for 45 days just before a government shutdown was to go into effect. Mr. Biden on Sunday in remarks at the White House said he was "sick and tired" of the brinkmanship.

4 Oct: World biggest bond markets hit by heavy selloff. World government bonds went through an unrelenting selloff on Wednesday (October 4). And that has driven U.S. 30-year Treasury yields to 5% for the first time since 2007, while German 10-year yields were at 3%. Those moves could speed up a global slowdown - hurting stocks and corporate bonds.

7 Oct: Israel and Hamas at war after surprise attacks from Gaza Strip. Israel and Hamas are once again at war after the Palestinian group launched a large aerial and ground operation from the blockaded Gaza Strip, its biggest attack in years. Sirens sounded across Israel and as far north as the contested city of Jerusalem on Saturday after Hamas claimed 5,000 rockets were launched from the blockaded enclave.

10 Oct: IMF says global economy 'limping along', cuts growth forecast for China, euro zone. The International Monetary Fund on Tuesday cut its growth forecasts for China and the euro zone and said overall global growth remained low and uneven despite what it called the "remarkable strength" of the U.S. economy. In its latest World Economic Outlook, the IMF left its forecast for global growth in 2023 unchanged at 3.0% but cut its 2024 forecast to 2.9% from its July forecast of 3.0%.

13 Oct: In second budget, Anwar govt tables record RM393.8b allocation for 2024. Almost eight months after PM DS Anwar Ibrahim tabled his first federal budget, today's tabling of Budget 2024 will be the government's biggest federal spending yet at RM393.8 billion to date. As Anwar's government seeks to rationalise existing subsidy spending with the intention of consolidating the country’s fiscal position, Budget 2024's amount is over RM7.66 billion than the one tabled last February according to Ministry of Finance's Fiscal Outlook and Federal Government Revenue Estimates 2024 report.

16 Oct: Progressive wage policy to complement minimum wage policy: Economy Ministry. The progressive wage policy will complement the minimum wage policy and is not intended to replace it, said the Economy Ministry. The progressive wage policy is a voluntary approach that employers can negotiate with employees before deciding to adhere to it, the ministry said. "The policy aims to further strengthen the reform on workers’ salaries in the country," the ministry said.

17 Oct: Putrajaya expects service tax hike to bring in additional RM3b revenue in 2024. The government expects to raise an additional revenue of RM3 billion through the increase in the sales and service tax (SST) to 8% next year, from 6% currently, according to Treasury secretary general Datuk Johan Mahmood Merican.

20 Oct: Powell sets table for November pause, warns of more rate hikes if economy heats up. Fed Chair Jerome Powell signaled the central bank could hold rates steady at its next policy meeting but warned that inflation was still too high and that more interest rate increases are still possible if the economy stays surprisingly hot.

22 Oct: Easing up MM2H conditions will boost Johor real estate. Easing the strict conditions for My Malaysia Second Home (MM2H) programme and the high rental in Singapore will provide a much-needed boost to Johor real estate sector. State Housing and Local Government Committee Chairman Datuk Mohd Jafni Md Shukor said this development can resolve the issue of unsold properties and revive Johor's housing projects.

23 Oct: Treasury 10-Year Yield Breaches 5% for First Time Since 2007. The 10-year Treasury yield crossed 5% for the first time in 16 years, propelled by expectations the Federal Reserve will maintain elevated interest rates and that the government will further boost bond sales to cover widening deficits.

23 Oct: No crisis despite ringgit hitting new low against US dollar since AFC: BNM governor. Despite the ringgit’s decline to its lowest level against the strong US dollar since the Asian Financial Crisis (AFC) in 1997, Malaysia is far from being in crisis – as the country has a resilient economy, robust banking system and strong external sector, Bank Negara Malaysia (BNM) governor Datuk Abdul Rasheed Ghaffour said.

24 Oct: China to issue $137 bln sovereign debt to support economy. China's top parliament body has approved a 1 trillion yuan ($137 billion) sovereign bond issue and passed a bill to allow local governments to frontload part of their 2024 bond quotas, state media said on Tuesday, in a move to support the economy.

26 Oct: US economic growth accelerated to 4.9% in third quarter. The US economy expanded faster than expected in the third quarter, growing at its quickest pace in almost two years in the latest sign of the country’s economic resilience despite high interest rates. Strong consumer spending was the main driver of a 4.9 per cent annualised increase in GDP, according to preliminary figures from the commerce department’s Bureau of Economic Analysis.

30 Oct: Mat Sabu: Chicken subsidy to be discontinued on Nov 1 after RM3.8b spent since Feb 2022. Agriculture and Food Security Minister Datuk Seri Mohamad Sabu said the government has agreed subsidies and price control for chicken will be discontinued starting November 1. He said chicken eggs graded A, B, and C, however, will continue using existing subsidy mechanisms. “Since February 2022, the government has borne RM3.8 billion for egg and chicken subsidies.

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