MONTHLY ECONOMIC UPDATE

6 MARCH 2023

ECONOMIC RESEARCH

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KEY TAKEAWAYS

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- **All eyes on Powell's testimony for fresh insights in relation to future rate hikes –** The Federal Reserve (Fed) Chairman Jerome Powell is expected to give his testimony on Tuesday and Wednesday amid a solid U.S. labour market. The market will closely monitor his remarks as it would be his last public appearance before the Federal Open Market Committee (FOMC) is slated on 21-22 March. Additionally, some policymakers opine that more tightening is necessary to quell the stubborn inflation following a series of strong job reports, prices and consumption data. As the December economic projection stated, the Fed could push its policy rate beyond the 5.1% level this year.

- **The beginning of China's National People's Congress (NPC) annual meeting –** We believe that the meeting will indicate the country's policy direction following the end of its controversial Zero-Covid policy. The annual gathering will run from 5-13 March to review the government report and to earmark new leaders for the next five years. Additionally, the report will likely focus on how the country handles external challenges and how to chart its post-pandemic economic recovery. In the latest development, the government is anticipating a growth target of 5.0% this year, the lowest projection in decades.

- **Bank Negara Malaysia's (BNM) Monetary Policy Committee (MPC) under the spotlight** – During the January meeting, BNM made a surprise move when it left the Overnight Policy Rate (OPR) unchanged at 2.75% after straight hikes of 100 bps since May last year. Based on our internal assessment, we foresee resistance to a hike in the 8-9 March meeting amid static labour market recovery. However, we are pencilling in a hike during 2Q2023, perhaps in May, but subject to the labour recovery market in 1Q2023. We also believe that further direction on the OPR could be unveiled when the BNM release its 2022 Annual Report with insights or dynamic assessments relating to near-term economic prospects and inflation path.

SECTION 1

Malaysia’s Financial Market

REGIONAL EQUITY: THE MARKET ENDED LOWER IN FEBRUARY AS FOMC MEMBERS ARE OPEN TO HIGHER FEDERAL FUND RATES (FFR)

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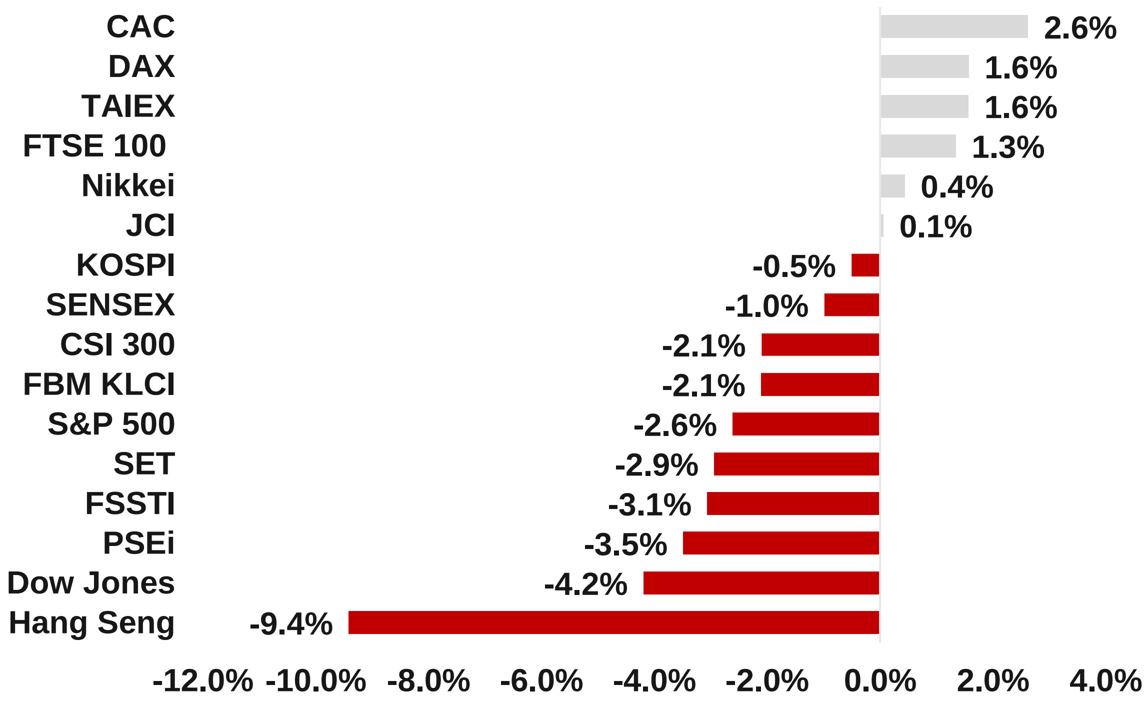
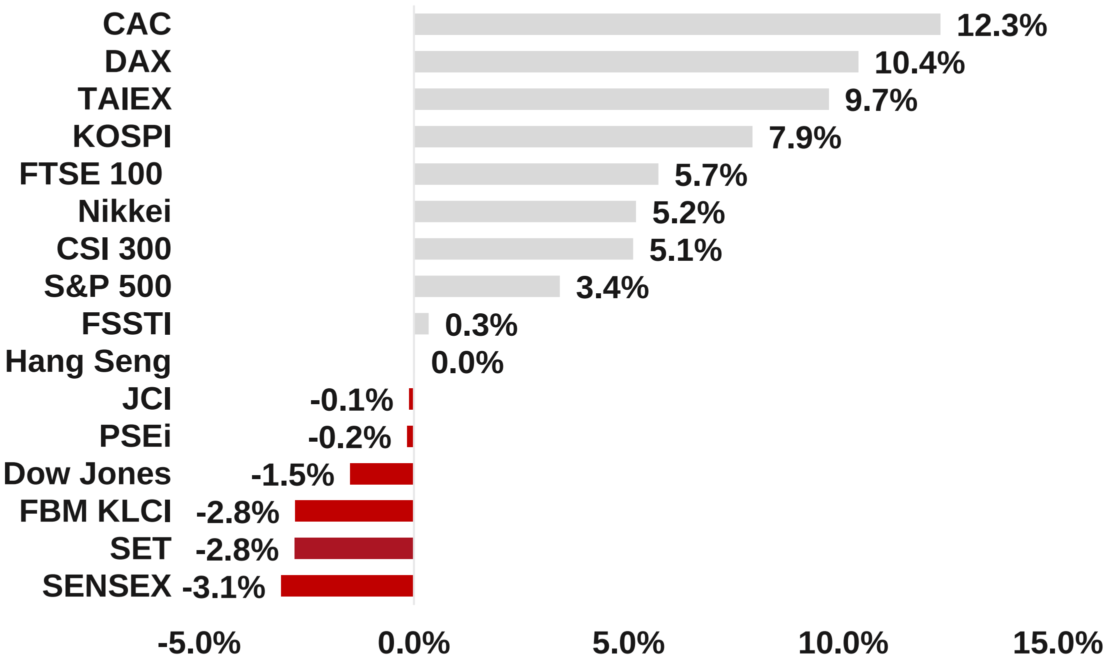
Monthly Gain/Loss of Major Equity Market, %



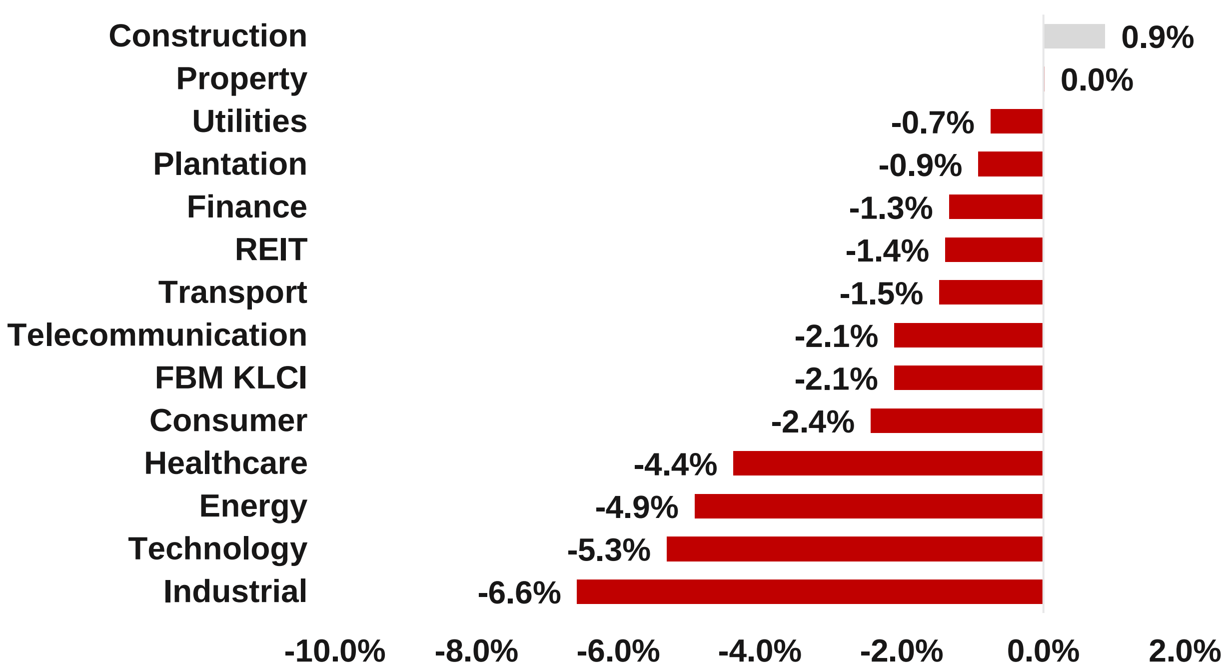
YTD Gain/Loss of Major Equity Markets, %
(As of 28 February 2023)

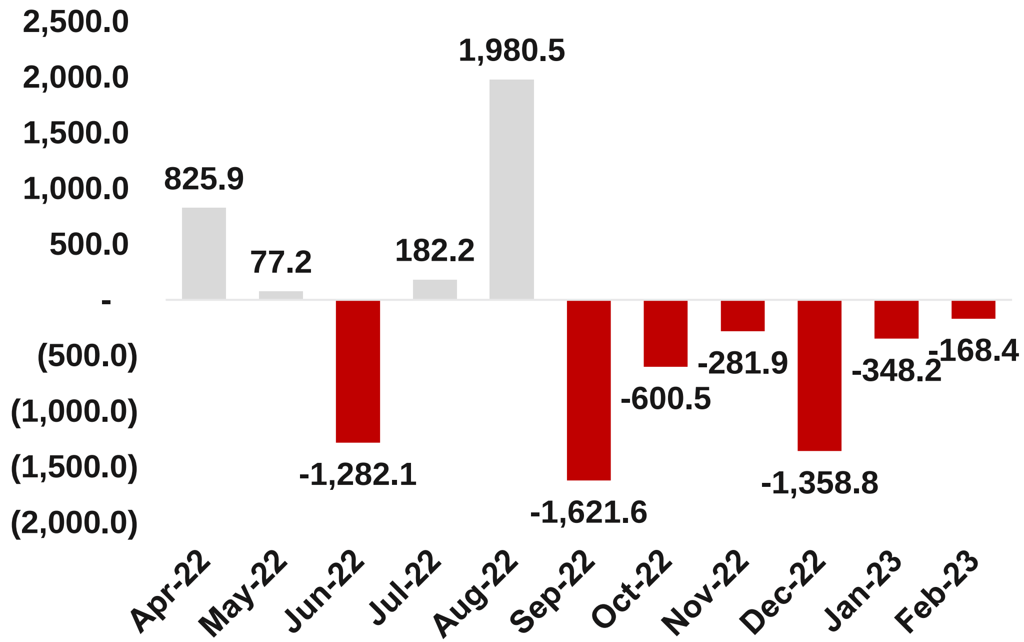


Sources: Bursa, CEIC

- 10 out of 16 regional markets closed on a negative note, with Hong Kong’s Hang Seng index tumbling by 9.4% m-o-m, followed by the U.S. Dow Jones (-4.2%) and Philippines's PSEi (-3.5%) in February.
- This scenario is mainly dragged by growing fears that the U.S. Fed will continue its monetary tightening cycle until later in the year amid upbeat U.S. data economic momentum.
- Latest U.S. job report strengthened further with the inflation stubbornly high despite a series of aggressive rate hikes by the Fed to cool down the economy.

DOMESTIC EQUITY: LOCAL MARKET ENDED IN THE RED





Sources: Bursa, BNM

- Similarly, Bursa sectoral indices also fell into negative territory in February, with Industrial (-6.6%), Technology (-5.3%) and Energy (-4.9%) sectors being the biggest losers. This was primarily due to the cautious outlook of the U.S. economy and sentiments surrounding the Malaysian 2023 Budget review on 24 February.
- Given the resilience in the job market and higher inflation numbers in the U.S., we expect the Fed to continue to hike rates at the upcoming FOMC meetings to tamp down the country's resilient economy. This will, in turn, will rattle the market in the short term.
- Meanwhile, foreign investors' selling spree continued with a total of RM168.4 million net outflows recorded in February from RM348.2 million in January. It was the sixth month of foreign net outflows amid uncertainty over the U.S. Fed Funds outlook.
- We anticipate FBM KLCI will be cautiously traded between 1,450.0-1,465.0 points ahead of the MPC meeting this week.

FIXED INCOME: BOND YIELDS SPIKED IN FEBRUARY

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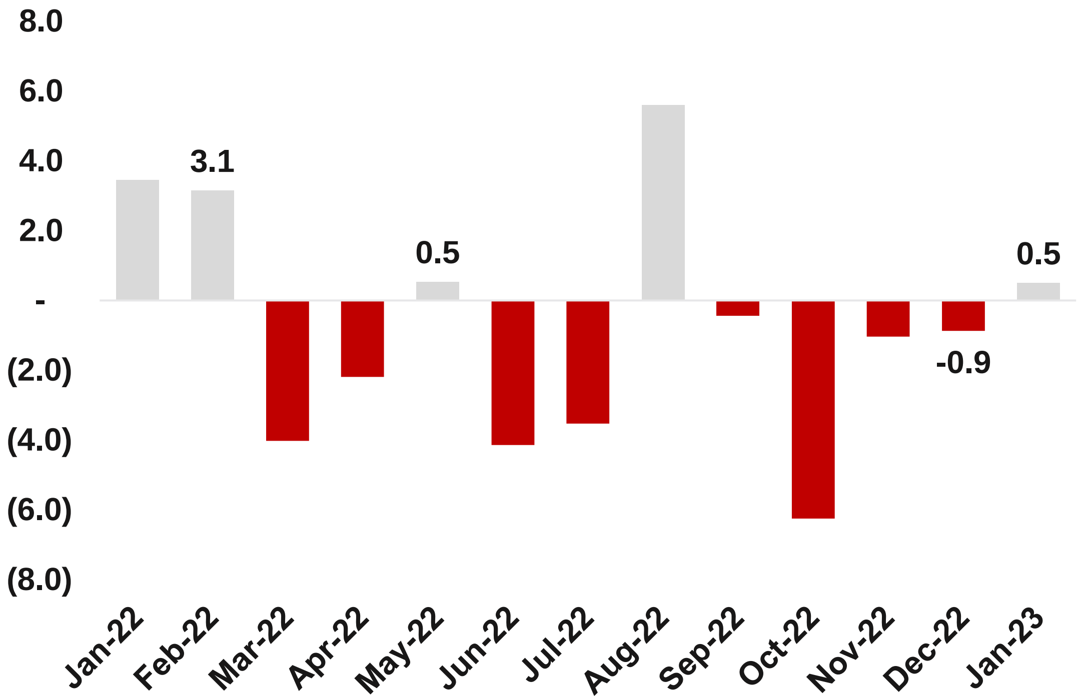
Monthly changes, basis points (bps)

UST	Yields (%) 31-Jan-23	Yields (%) 28-Feb-23	Change (bps)
3-M UST	4.70%	4.88%	18
2-Y UST	4.21%	4.81%	60
5-Y UST	3.63%	4.18%	55
10-Y UST	3.52%	3.92%	40
MGS	**Yields (%) 31-Jan-23**	**Yields (%) 28-Feb-23**	**Change (bps)**
3-Y MGS	3.39%	3.52%	13
5-Y MGS	3.55%	3.67%	12
7-Y MGS	3.69%	3.79%	10
10-Y MGS	3.80%	3.91%	11

Sources: BNM, Federal Reserve Board

Foreign Fund Flows in Bond Market, RM billion



- The U.S. Treasury (UST) and Malaysian Government Securities (MGS) yields rose significantly in February given the high inflation data amid the hot U.S. labour market, which in turn prompted investors to re-price their expectations on FFR.
- Foreign investors were the net buyers with a total of RM0.5 billion of net inflows in January 2023 (December 2022: -RM0.9 billion).
- In the medium term, we expect the fixed-income market to remain volatile amid a cautious stance among investors with the U.S.' ongoing contractionary monetary policy.

FX MARKET: RINGGIT ENDED LOWER DURING FEBRUARY

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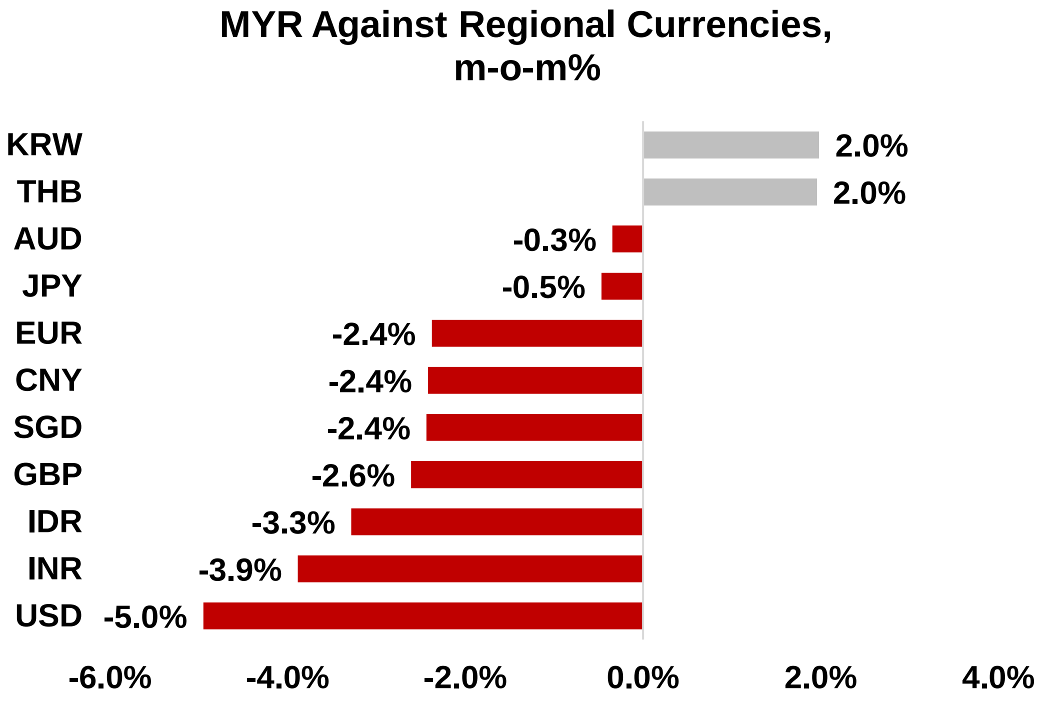

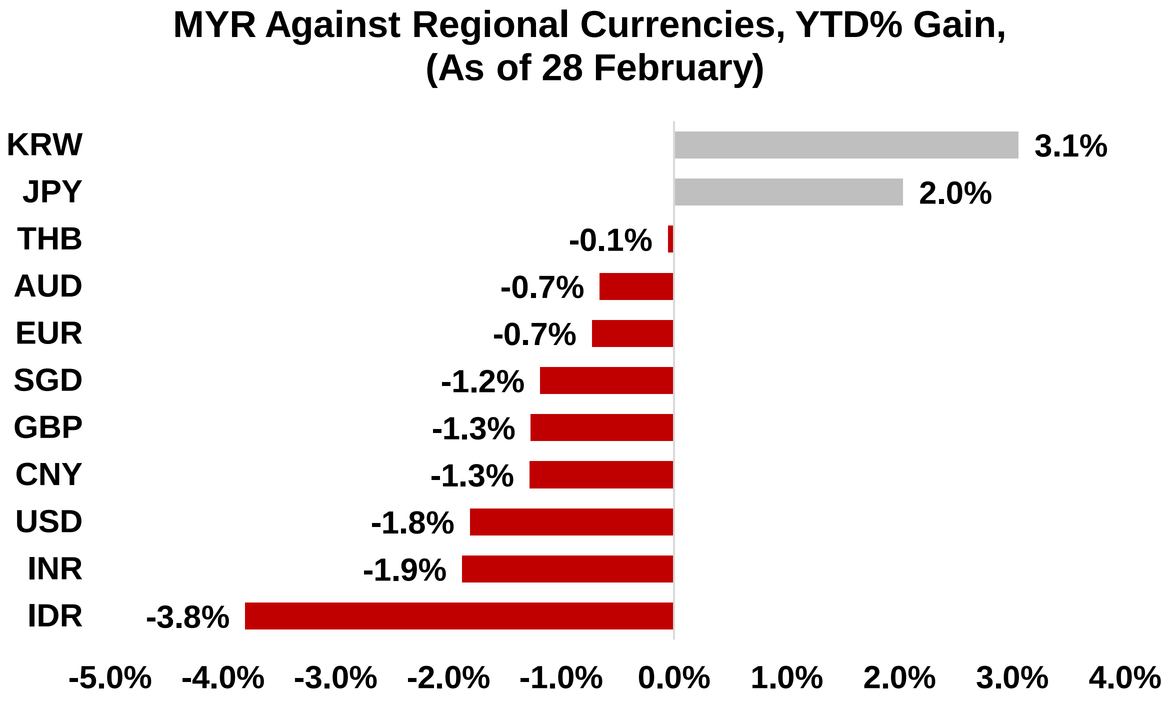

Source: Investing.com

- The Ringgit depreciated against the USD by 5.0% on a monthly basis, closing at RM4.4850 on 28 February (31 January: RM4.2630).
- One of the possible reasons was the uptick seen in the USD index, which appreciated by 2.7% during the month on the back of anticipation policymakers' decision to keep interest rates restrictive for longer than expected.
- This is consistent with the latest U.S. consumer spending data, which jumped by 0.6% m-o-m in January (December 2022: 0.2%), indicating more tightening is needed to bring inflation back to the so-called 2.0% target rate.
- Looking forward, market participants keep a close watch on Fed Chairman Powell's testimony on whether larger rate hikes would be considered following the recent data.
- In the event of Powell delivering a hawkish speech, and the U.S. data continued to remain resilient, its policy rate path to be longer and higher than anticipated. As such, we foresee the local note to remain under pressure in the near term against the USD.

SECTION 2

The Global Economy

GLOBAL MANUFACTURING ACTIVITIES RETURN TO GROWTH AS MAINLAND CHINA REOPENS

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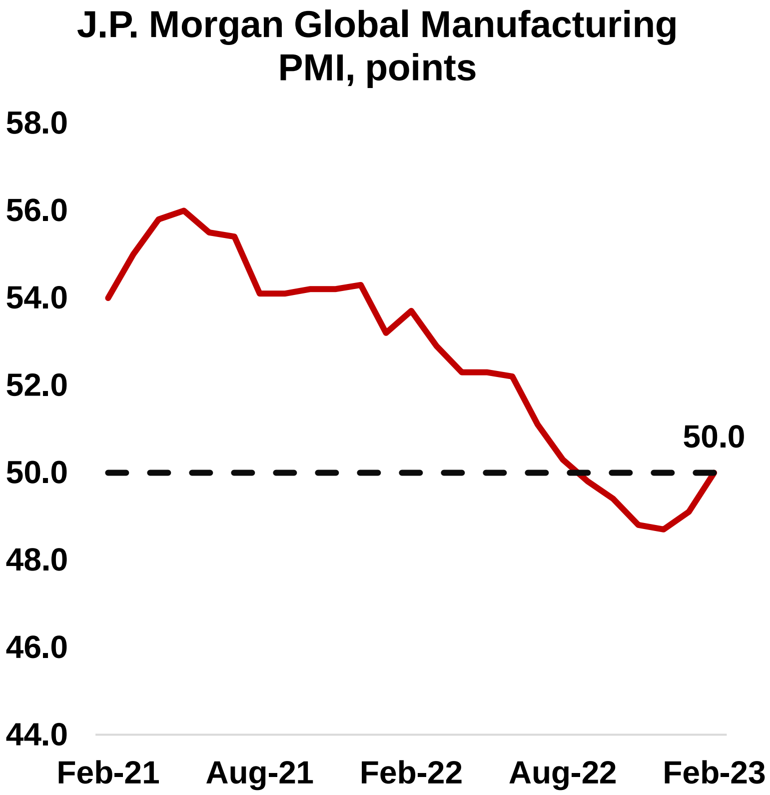

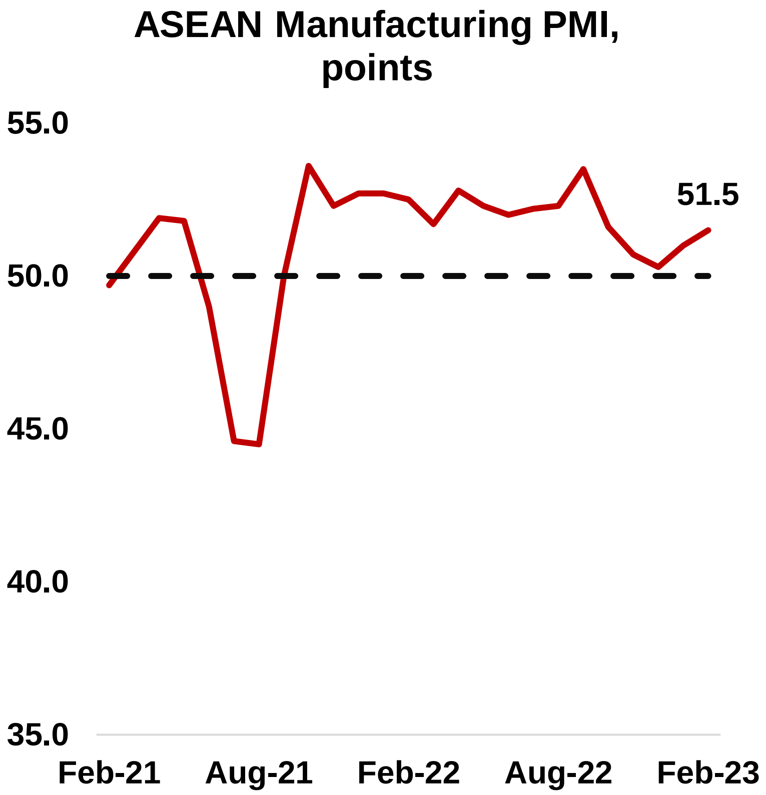

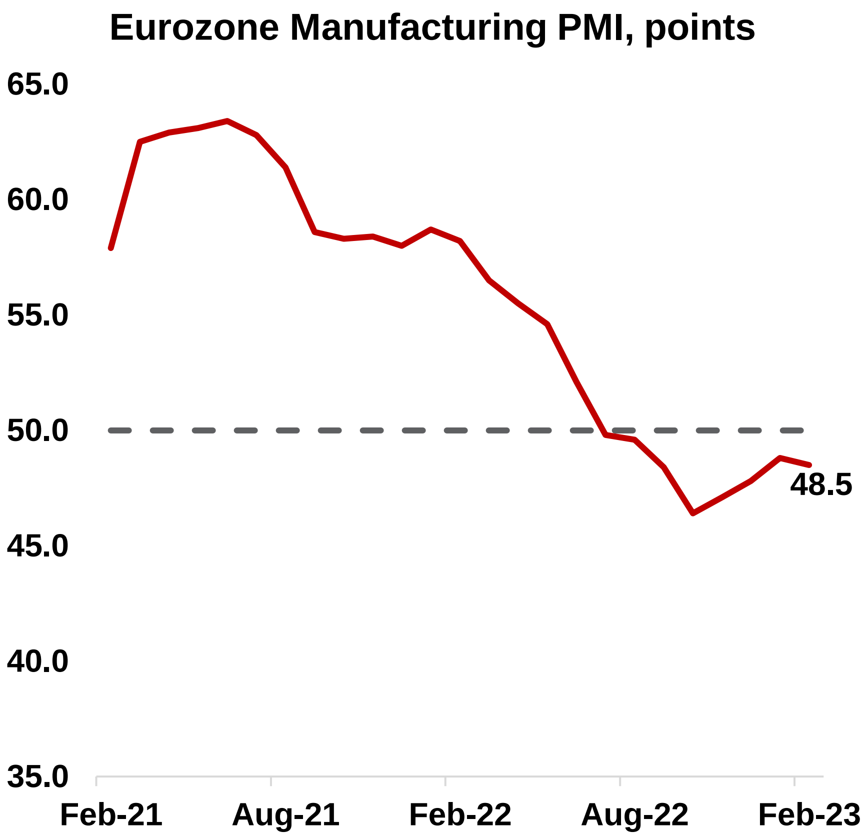

Source: S&P Global

- ASEAN's manufacturing Purchasing Managers' Index (PMI) remained sturdy in February as it trended above the 50.0 mark amid suppliers' delivery time had stabilised, among others.
- On the contrary, the Eurozone's PMI print fell slightly to 48.5 points during the month (January: 48.8 points). This indicates the eighth straight month of contraction since July last year as demand continues to fall, alongside supply-side inflationary pressures.

ON THE OTHER HAND, U.S. LABOUR MARKET REMAINS TIGHT

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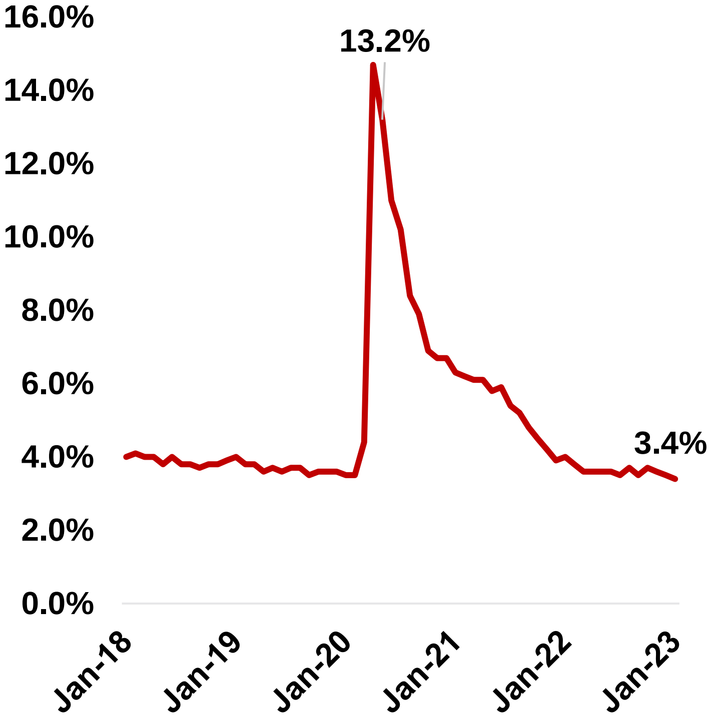
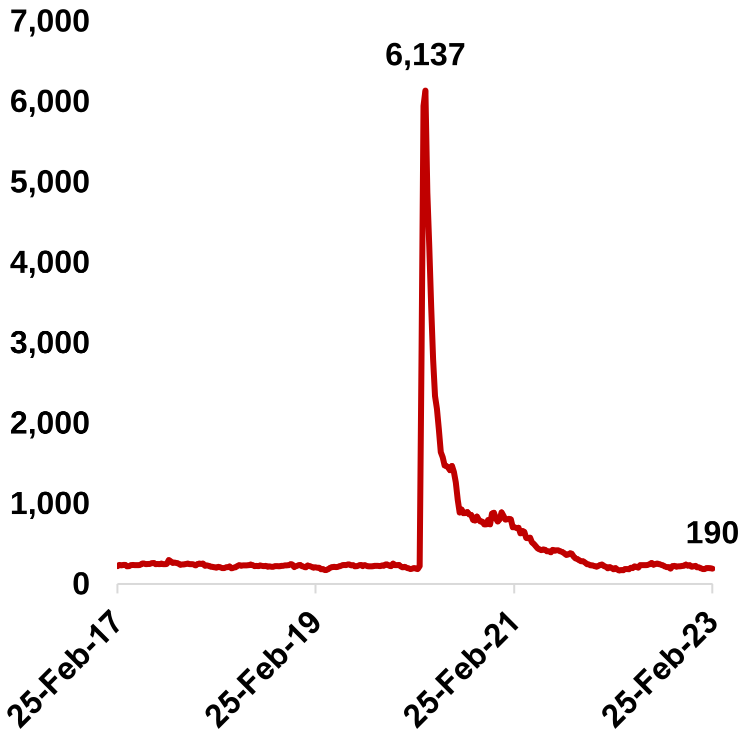
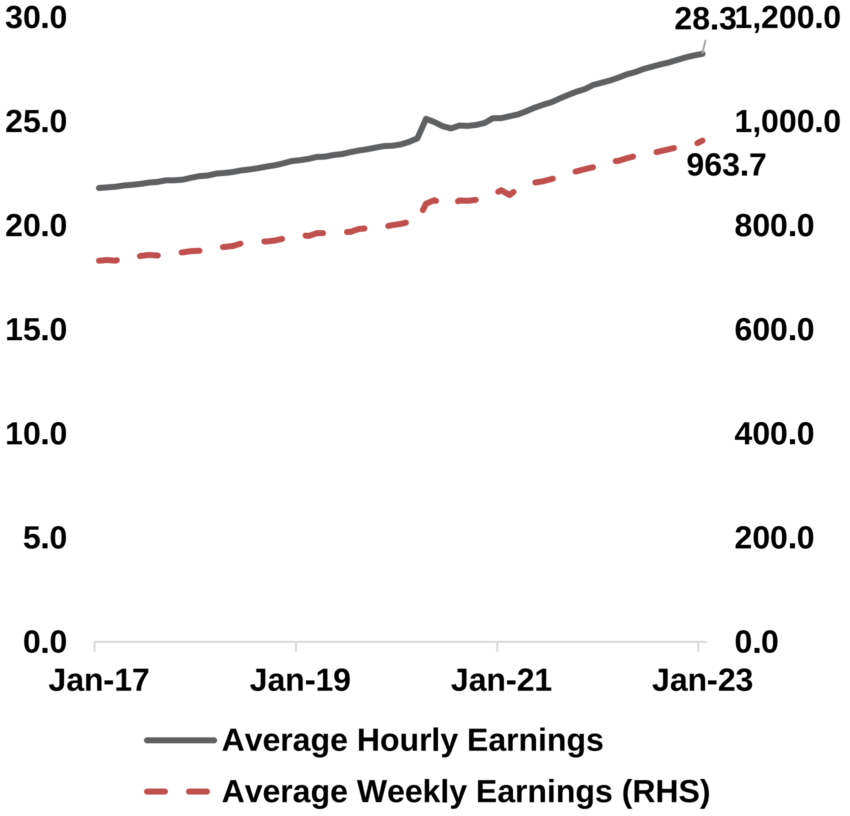
Unemployment Rate, %



U.S. Weekly Initial Jobless Claims (IJC), s.a. '000



Average Earnings, USD



Sources: CEIC, U.S. Department of Labor, U.S. Bureau of Labor Statistics

- The U.S.' unemployment rate in January reached the lowest level since May 1969 at 3.4%. At the same time, the IJC fell again to 190k for the week ended 25 February, pointing to a sustained labour market strength.
- Meanwhile, an increasing trend in the average earnings has lured more workers to the workforce participation, suggesting that the labour market remains hot amid aggressive monetary tightening.
- Such a situation and persistent inflationary pressures have led to the growing expectation that the Fed will continue tightening its policy rates for higher and longer.

CHINA'S ECONOMY RESPONDED POSITIVELY AFTER THE SHIFT IN THE COVID POLICY

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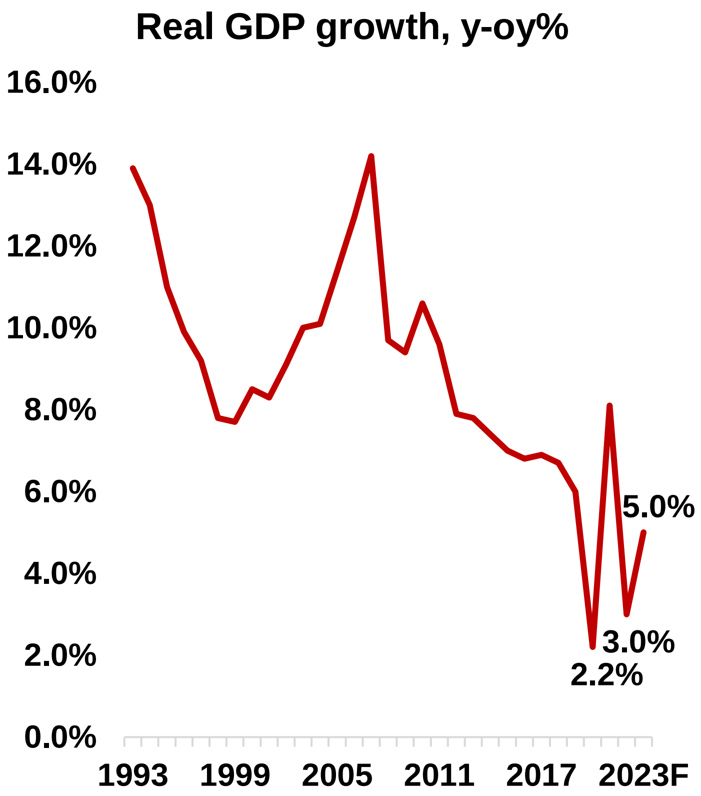

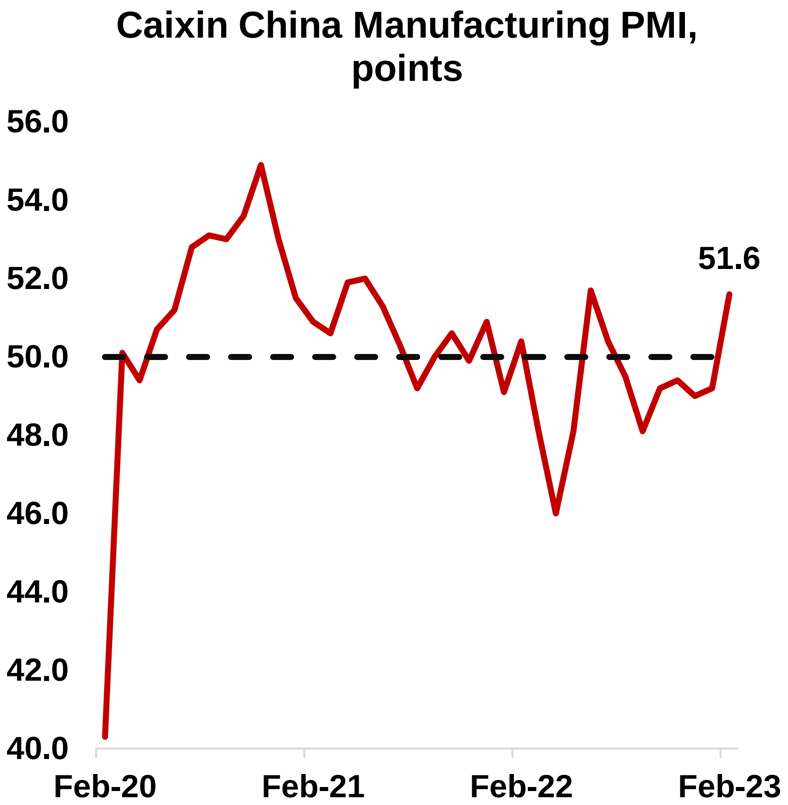

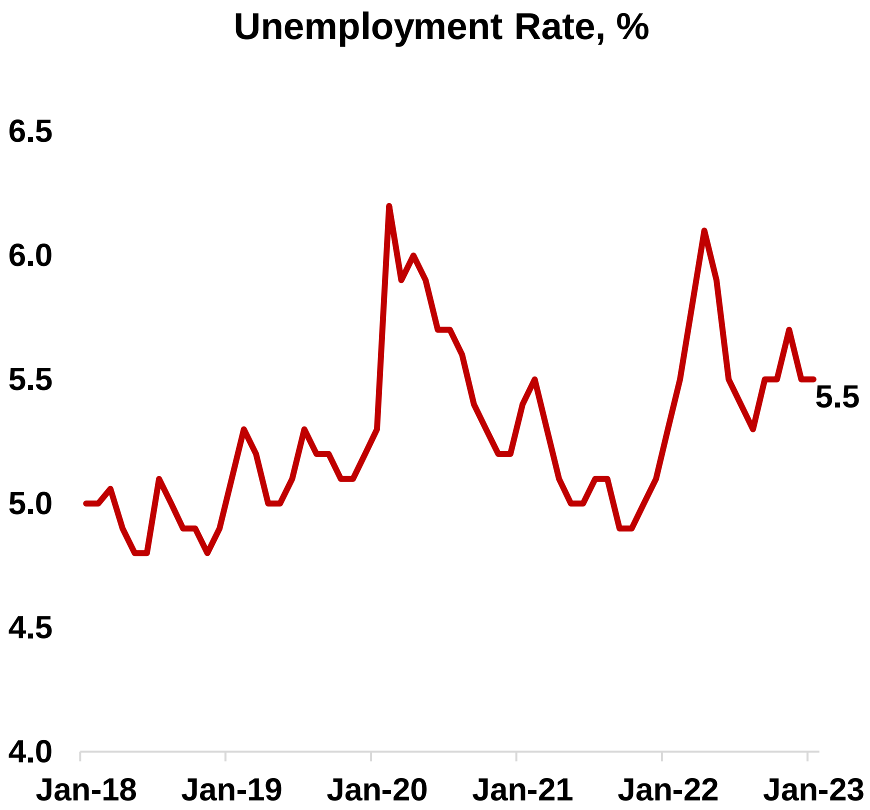

Sources: Organisation for Economic Co-operation and Development, S&P Global, National Bureau of Statistics (NBS)

- China has set an official economic target of about 5.0% in 2023 as the country exited its Zero-Covid strategy. Such growth is anticipated to come in after the expansion of 3.0% in 2022, significantly missing the said year's target, implying the slowest pace since the mid-1970s.
- The strength in the Caixin PMI reading (February: 51.6 points vs. January: 49.2 points) – the first expansion since July 2022 – showed that China's manufacturing activity started gaining steam.
- The government expects the country's unemployment rate to remain static throughout 2023, although it plans to add 12 million new urban jobs in the said year.

CHINA'S ECONOMIC RECOVERY WILL LEAD TO A STRONG REBOUND IN THE TOURISM SECTOR

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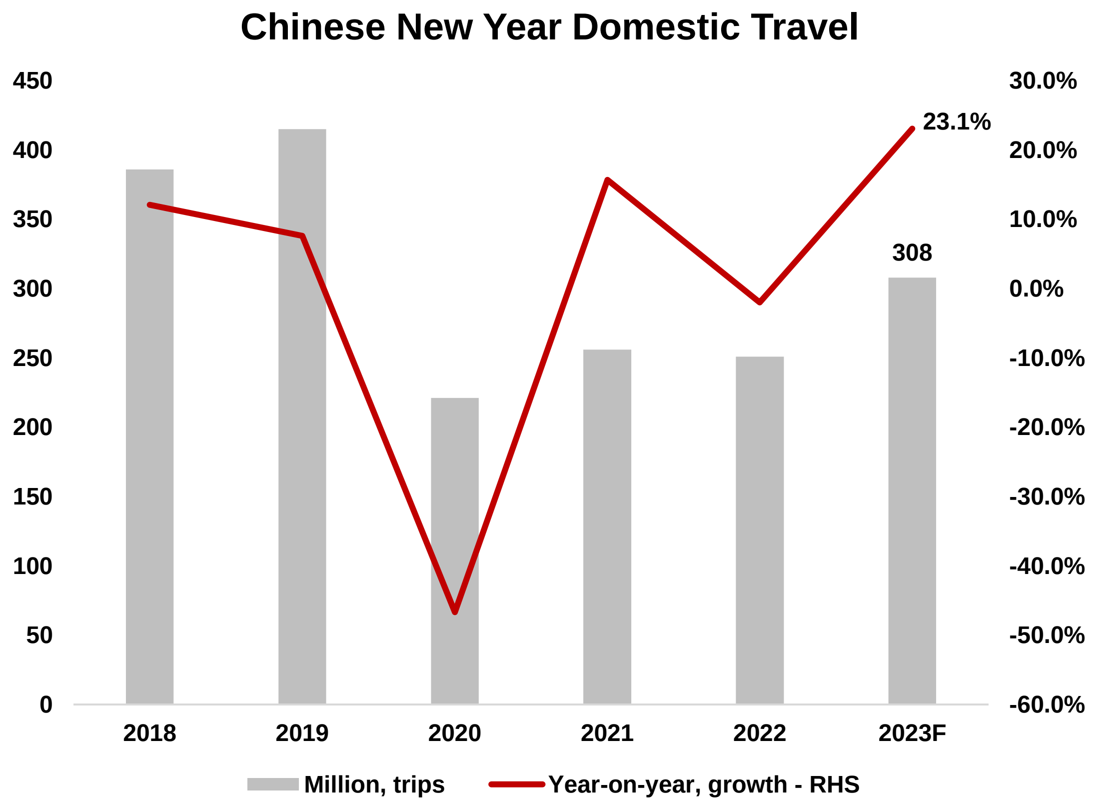

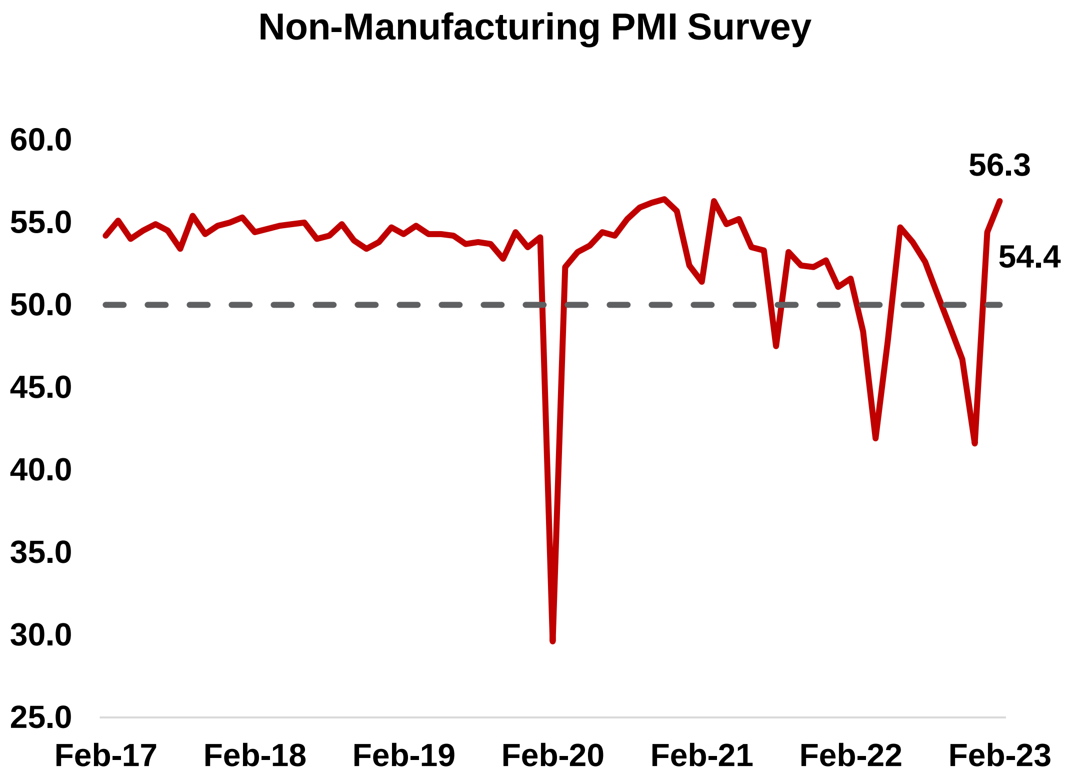

Sources: Ministry of Culture and Tourism, NBS

- This could be seen from the official data released by the Ministry of Culture and Tourism which anticipated a total of 308 million domestic trips during the year, representing a 23.1% y-o-y growth (2022: -2.0%) as pent-up demand was unleashed when the country decided to loosen its restrictions.
- Meanwhile, the official NBS Non-Manufacturing PMI increased significantly to 56.3 points in February, pointing the highest reading since March 2021 in the service sector following the lifting of the Zero-Covid policy.

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SECTION 3

Domestic Landscape & Banking Sector Update

MALAYSIAN ECONOMY IS POISED TO GROW MODERATELY AT 4.5% IN 2023

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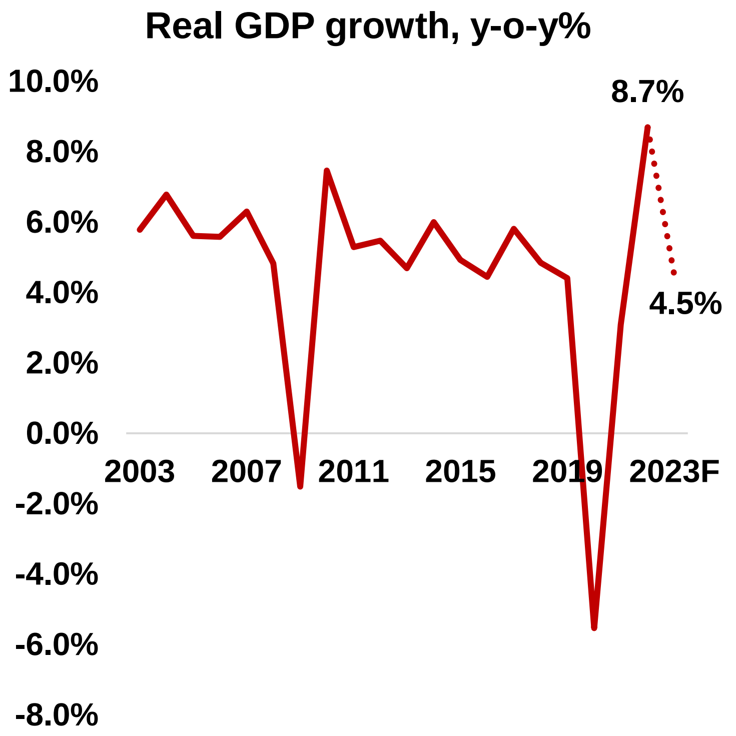
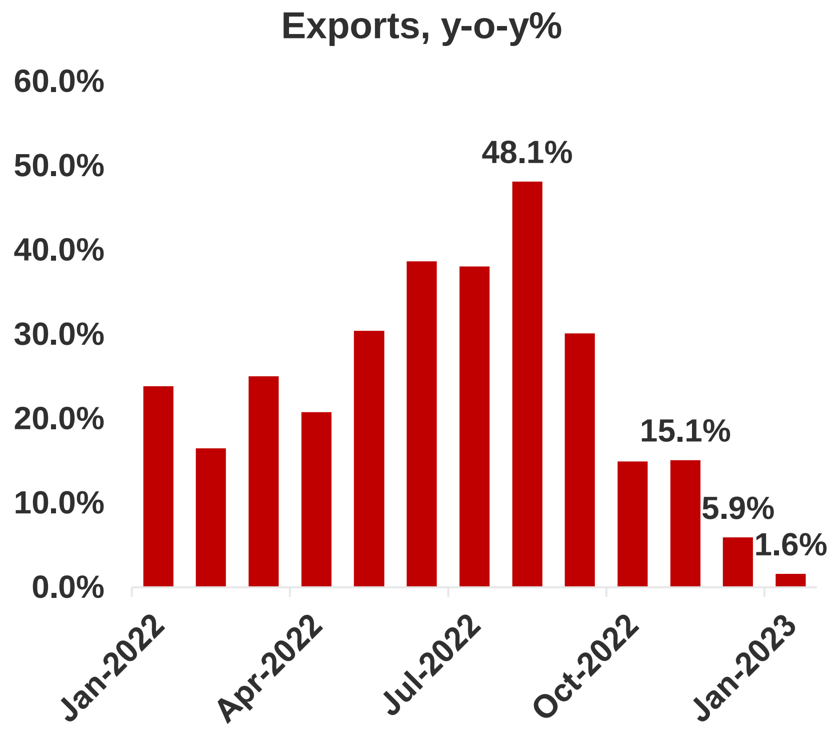
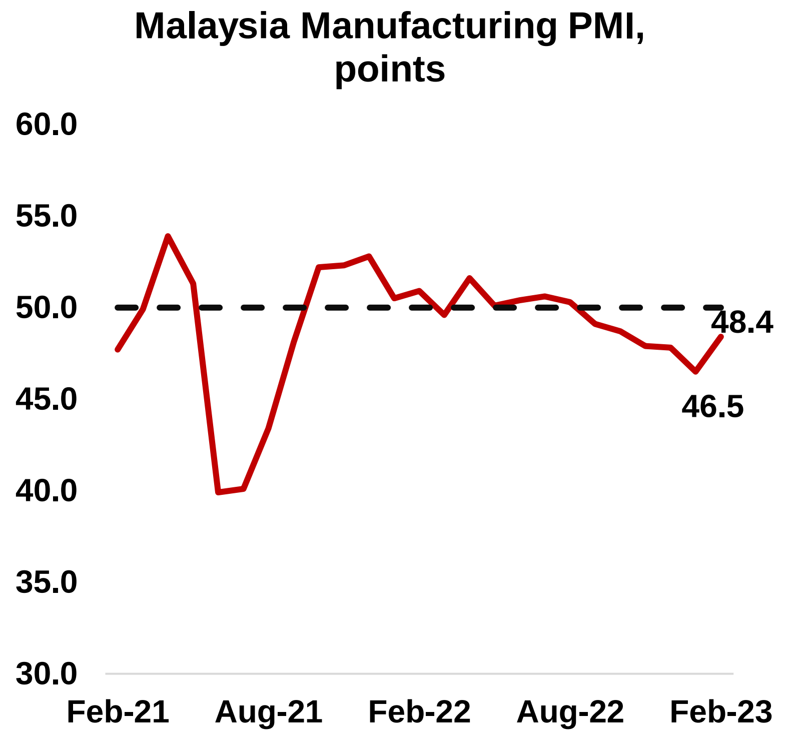


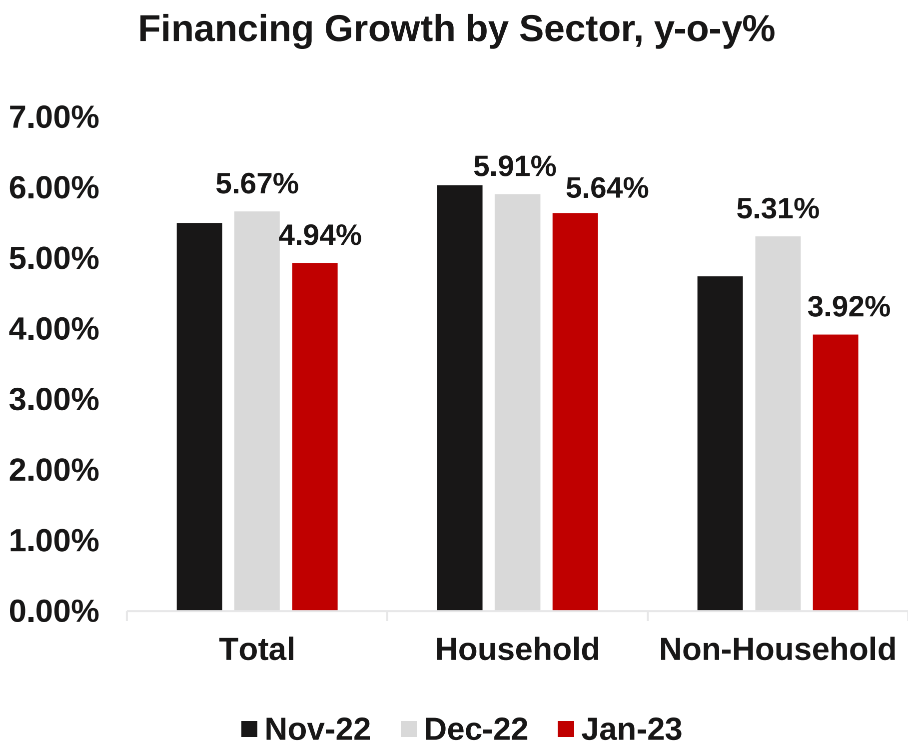


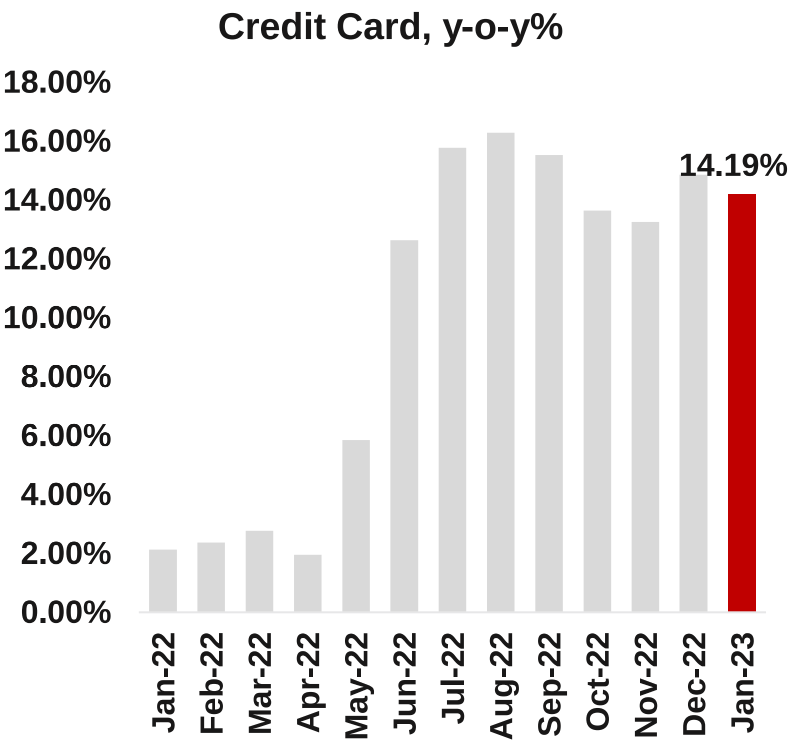


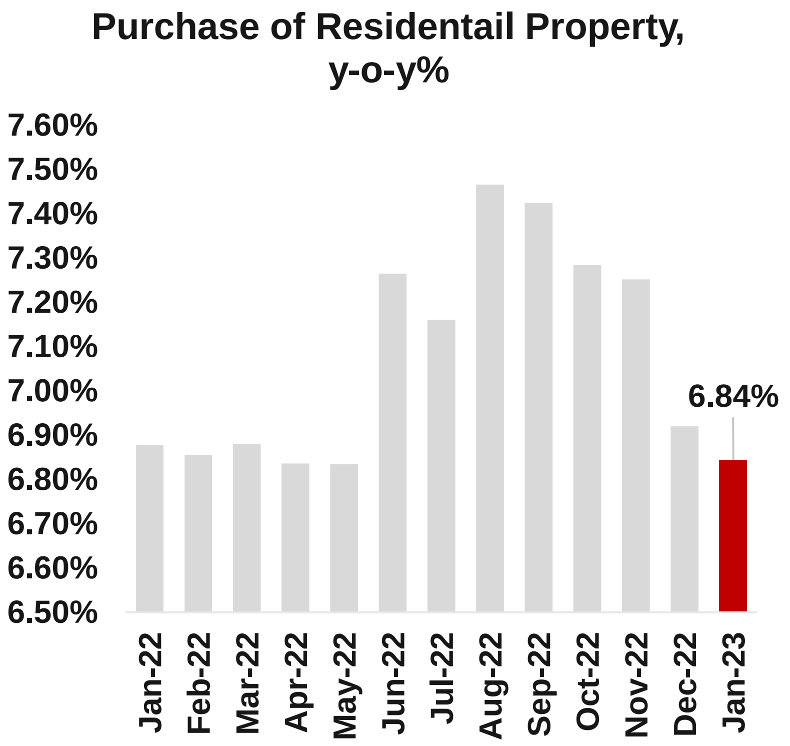
Sources: BNM, DOSM, S&P Global

- Last year saw the Malaysian economy ended on a strong note when its GDP growth came in at 8.7% (2021: 3.1%), marking the fastest expansion among Asean countries since 1996, anchored by an encouraging performance in the domestic demand, as well as firmer recovery in the labour market.
- However, the government projects the Malaysian economy to moderate to 4.5% in 2023, mirroring our in-house forecast due to the external challenging outlook, smaller fiscal injection and wage growth.
- As it stands, Malaysia’s export grew moderately at 1.6% at the start of the year, marking the weakest growth since November 2020 following the global recessionary risks and aggressive tightening by major central banks.
- The country's manufacturing activities continued to point to six straight months of challenging business conditions, although the reading improved in February.

BANKING SECTOR: FINANCING GROWTH STARTED OFF WITH WEAKER PERFORMANCE IN JANUARY 2023



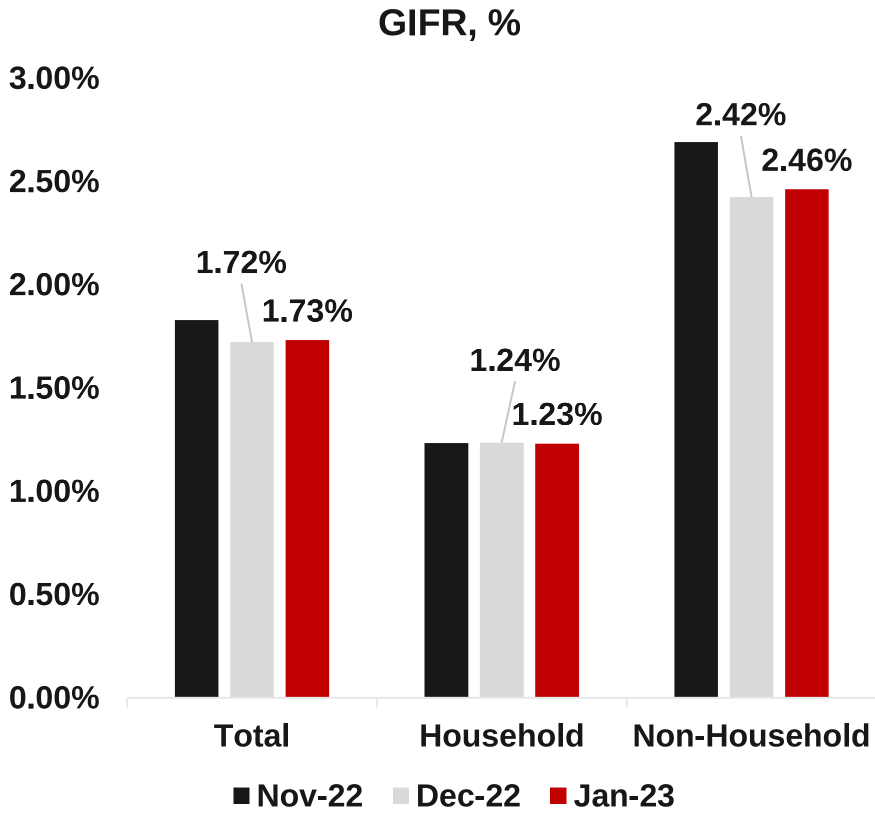


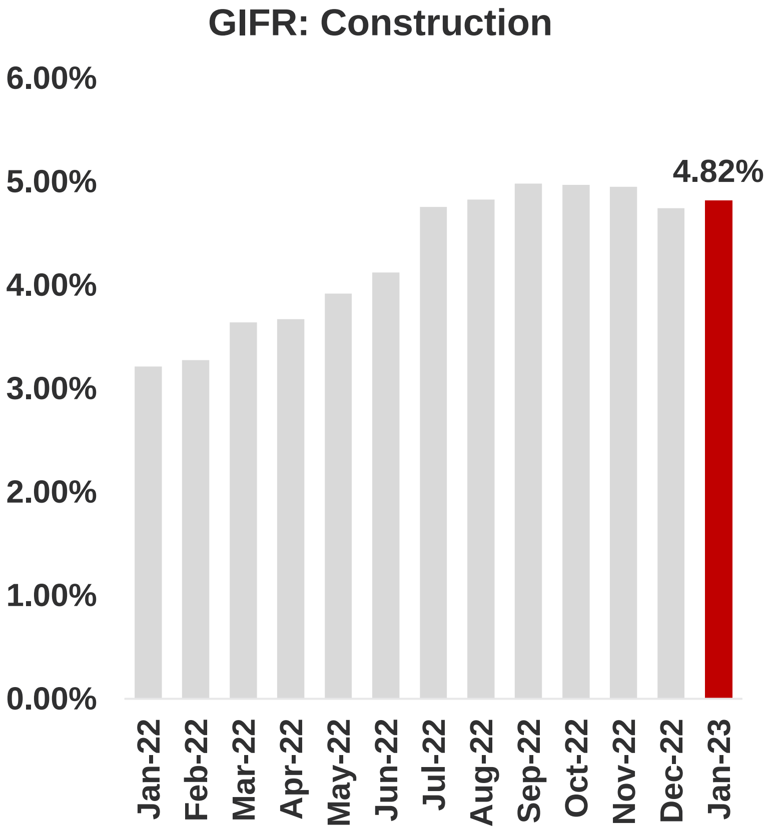


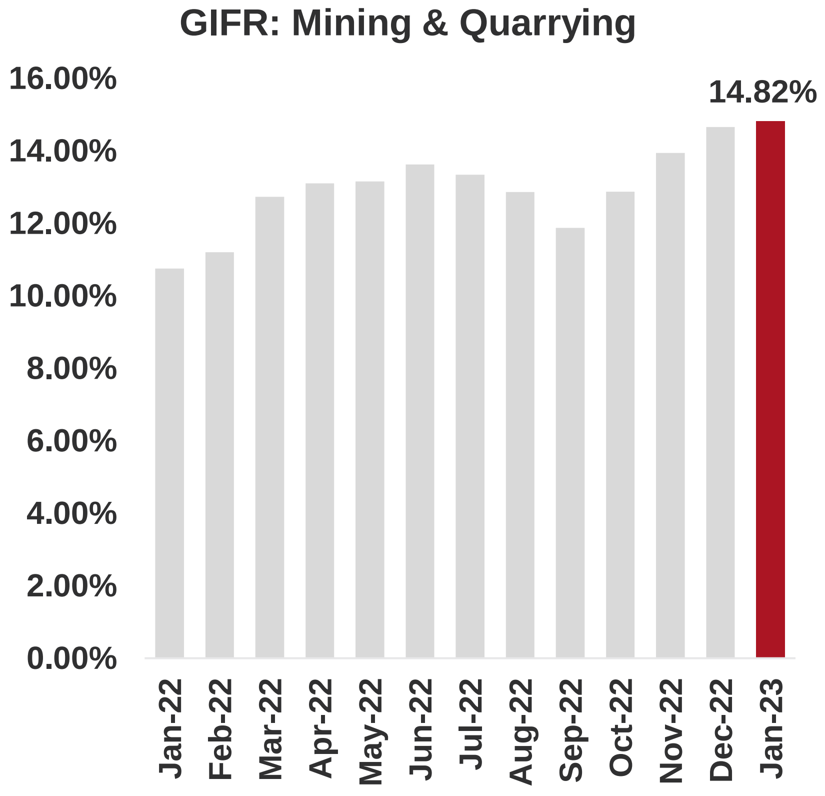
Source: BNM

- Total financing activities moderated to 4.94% y-o-y in January 2023 compared to 5.67% in December 2022. The slower growth is mainly underpinned by the Non-Household sector which came in significantly lower to 3.92% in January 2023 from 5.31% in December 2022. Similarly, the Household segment also softened to 5.64% in January 2023 (December 2022: 5.91%).
- Within the Household sector, financing for residential property (January 2023: 6.84% vs. December 2022: 6.92%) and credit card (January 2023: 14.19% vs. December 2022: 14.85%) have started to moderate, suggesting the tendency for private consumption to decline further as consumers are faced with higher financing cost and inflationary pressure.

BANKING SECTOR: GIFR INCHED UP IN JANUARY 2023







Source: BNM

- The total Gross Impaired Financing Ratio (GIFR) inched up slightly higher at 1.73% in January 2023 from 1.72% in December 2022 on the back of asset quality deterioration in the Non-Household sector (January 2023: 2.46% vs. December 2022: 2.42%).
- Within the Non-Household, GIFR for Construction climbed to 4.82% (December 2022: 4.75%) while impairment for Mining & Quarrying maintained at a double-digit of 14.82% (December 2023: 14.66%) in January 2023.
- Nevertheless, asset quality for the Household sector was relatively stable at 1.23% in January 2023 from 1.24% in December 2022.

THANK YOU