BANK ISLAM

MONTHLY ECONOMIC UPDATE

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ECONOMIC RESEARCH

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KEY TAKEAWAYS

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- **Weaker-than-expected labour market data pressures Fed to cut rates faster.** The U.S. Federal Reserve (Fed) left the federal funds rate (FFR) unchanged at a 23-year high for the eighth consecutive meeting in July and laid the groundwork for a rate cut in September. However, this decision was quickly followed by new data showing a deterioration in the U.S. labour market, with the number of Americans filing for unemployment benefits rising to an 11-month high. This has heightened concerns about a sharp slowdown in the U.S. economy, potentially prompting the Fed to consider more aggressive rate cuts. At the time of writing, markets have priced in a greater than 70% chance of a 50bp rate cut in September, up from around 12% a week ago. Additionally, the markets expect two 50bp cuts by the end of the year.

- **ECB holds its interest rates steady, pausing after delivering a 25bp cut at June's meeting.** July's rate pause decision echoed recent remarks from several European Central Bank (ECB) policymakers, including President Christine Lagarde, indicating the need to wait for further evidence of inflation firmly returning to the 2.0% target before making another move. However, the ECB left the door open for another rate reduction in September as it downgraded its view of the Eurozone's economic prospects and predicted that inflation would continue to trend downward. While the ECB refrained from providing stronger guidance, markets remain optimistic about ECB rate cuts, pricing in almost two reductions for the rest of the year.

- **BoE cuts policy rate for the first time in more than four years.** The rate cut decision, reached in a narrow 5-4 vote as policymakers split over whether inflation was sufficiently tamed, reduced the policy rate from a 16-year high of 5.25% to 5.00%. However, Bank of England (BoE) Governor Andrew Bailey refrained from indicating the timing of the next rate cut, stating that the BoE was not committing to a series of rapid reductions. The BoE remains concerned about the upside risk to inflation, projecting U.K. headline inflation to rise to 2.75% in Q4 2024 as the favourable effect of energy prices dissipates. Markets are still betting on a half chance of another rate cut later in the year, anticipating that stubbornly high services inflation will edge lower.

KEY TAKEAWAYS

- **China's slower-than-expected GDP growth in 2Q2024 has intensified calls for more effective stimulus measures.** GDP growth decelerated to 4.7% in 2Q2024 (1Q2024: 5.3%), raising concerns about China's ability to meet its full-year growth target of 5.0%. Domestic demand has been weakened by a prolonged property downturn, resulting in the lowest retail sales growth in 18 months in June. Meanwhile, China's exports grew at their fastest rate in 15 months in June, increasing by 8.6% (May: 7.6%), likely due to front-loading orders in anticipation of escalating trade tensions, particularly with the U.S.. In response to growth risks, the People's Bank of China (PBoC) announced a 10bp cut to the seven-day reverse repo rate, the one-year Loan Prime Rate (LPR), and the five-year LPR, reinforcing its commitment to supporting the economy. This move comes after China's Third Plenum left investors disappointed due to a lack of details on reforms.

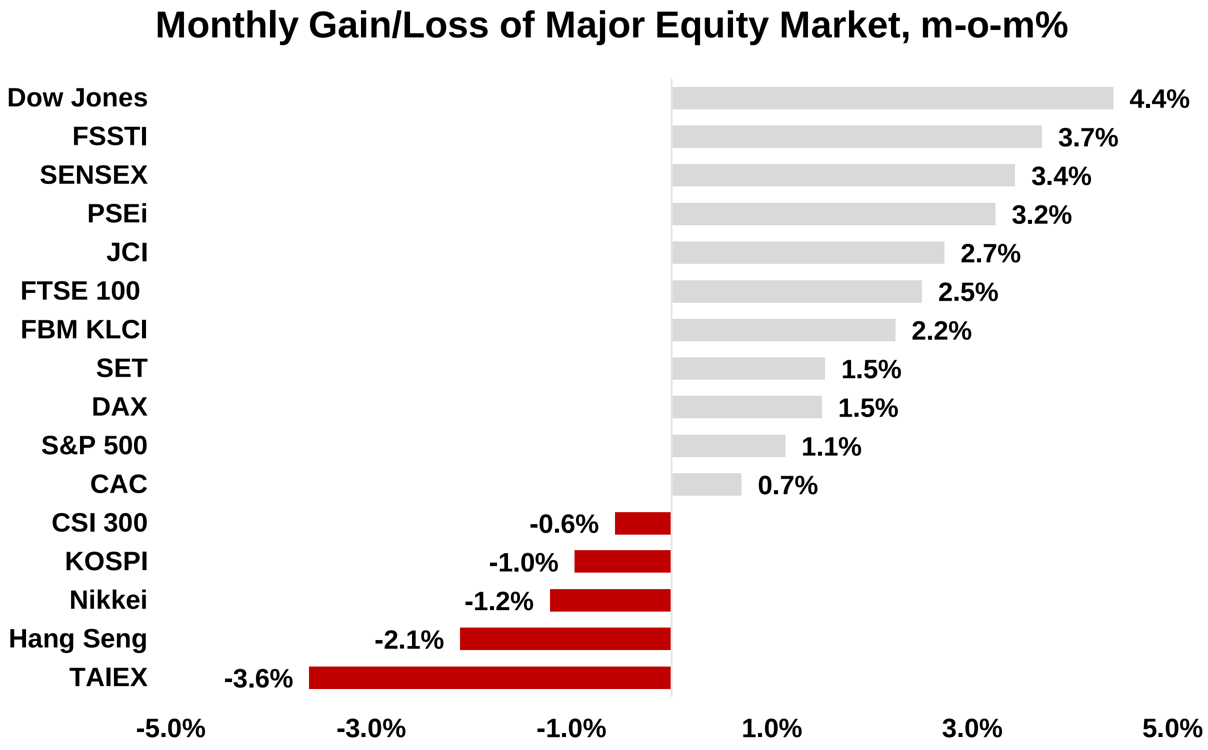
- **BoJ pushes forward monetary policy normalisation.** At its July policy meeting, the BoJ delivered a larger-than-expected rate hike, raising its short-term interest rate to around 0.25% from the range of 0% to 0.1%. The decision for this second rate hike of the year was unanimous, reflecting policymakers' growing concerns about the weakened Japanese yen which could adversely impact the economy. BoJ Governor Kazuo Ueda, in his post-meeting remarks, said that the interest rate remains very low even after the hike and indicated that the bank would consider further rate hikes if the economy progresses as projected. An expected narrowing interest rate differential between Japan and the U.S. led investors to realign their portfolios, sparking a massive sell-off across global stocks. Additionally, the BoJ unveiled plan to halve its government bond purchases to 3.0 trillion yen by early 2026.

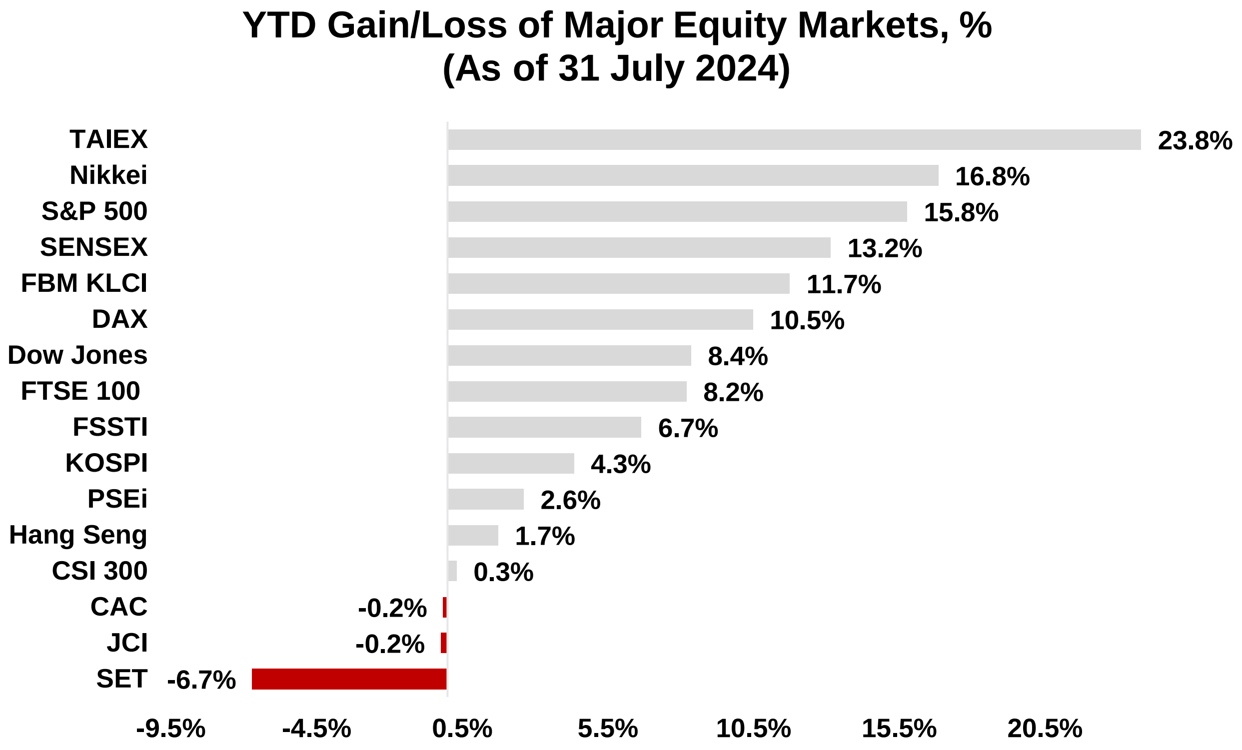
- **Malaysia's 2Q2024 GDP growth set to be the fastest in six quarters.** According to the Department of Statistics Malaysia (DOSM), the economy is estimated to have expanded by 5.8% in 2Q2024, accelerating from 4.2% in 1Q2024, thus bringing the overall growth in 1H2024 to 5.0%. All sectors except for mining registered faster growth. Of note, construction sector continued to record a double-digit growth at 17.2% (1Q2024: 11.9%), suggesting increased investments alongside development projects. Services sector, which constitutes the largest portion of GDP, grew by 5.6% (1Q2024: 4.7%) amid festive holiday demand, vibrant tourism activities, and still healthy labour market conditions. Meanwhile, Malaysia's June inflation remained steady at 2.0%, well below market expectations for an increase to 2.2% despite diesel subsidy rationalisation.

SECTION 1

Malaysia’s Financial Market

REGIONAL EQUITY: U.S. STOCKS SOARED AS FED SIGNALS A POTENTIAL RATE CUT





Sources: Bursa, CEIC data

- U.S. stocks – Dow Jones (+4.4%) and S&P 500 (+1.1%) soared in July as the Fed kept rates steady but signalled a potential September rate cut if inflation continues to ease.
- On the contrary, Taiwan's TAIEX plummeted by 3.6% in July, driven by the plunge in Taiwan Semiconductor Manufacturing Co. (TSMC), mirroring tech sector volatility in the U.S. stocks market.
- Despite the recent fall, Taiwan's TAIEX was still the top performer in July, with a YTD gain of 23.8%.
- In addition, Hong Kong's Hang Seng also slumped by 2.1% under pressure from official Manufacturing Purchasing Managers Index (PMI) data, which indicated a third consecutive month of declining factory activity due to weak demand and severe weather conditions.

DOMESTIC EQUITY: FBM KLCI REBOUNDS AS SENTIMENT LIFTS ON STRONGER-THAN-EXPECTED 2Q2024 GDP GROWTH

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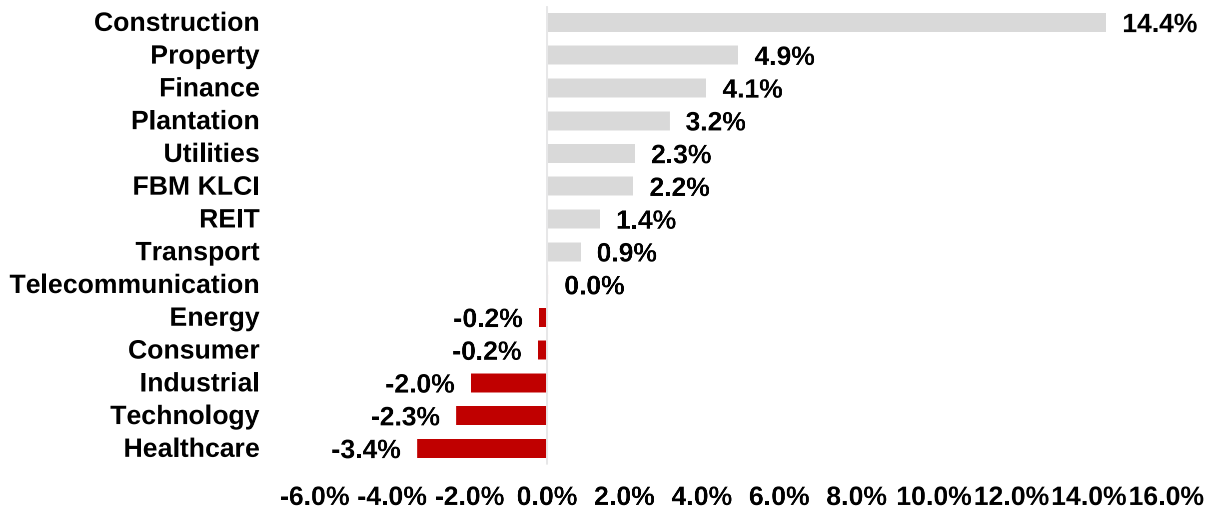

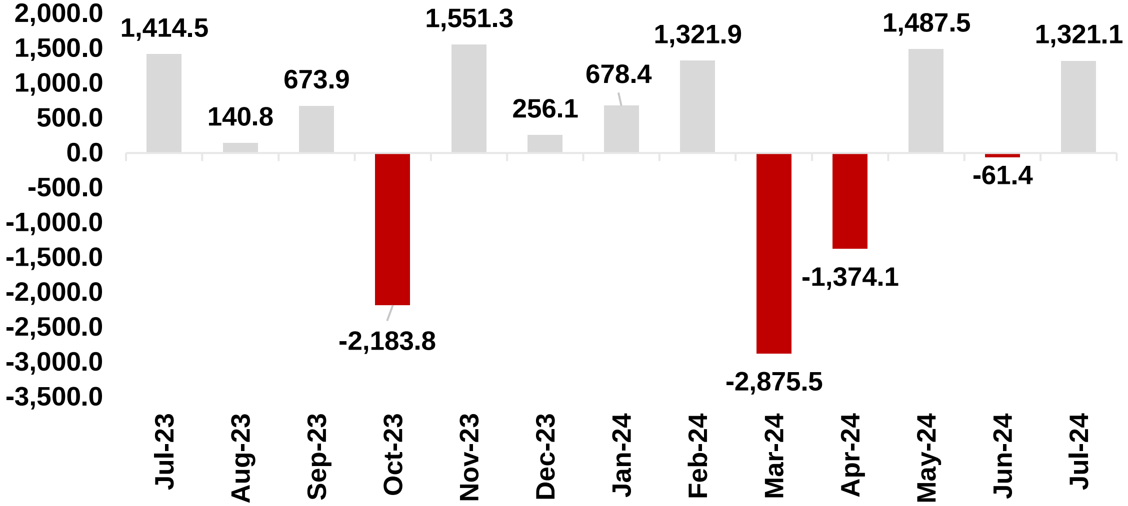

Sources: Bursa, Bank Negara Malaysia (BNM), CEIC data

- The FBM KLCI ended July with a gain of 2.2%, reversing a 0.4% decline in the previous month. Sentiment received a boost, particularly following the release of the official advance estimate of Malaysia’s 2Q2024 GDP growth, which exceeded market expectations.
- The Construction index led gains by a large margin, rising 14.4% amid optimism surrounding infrastructure projects and data centres. Construction sector is estimated to have expanded by 17.2% in 2Q2024, accelerating from 11.9% in 1Q2024 and continuing its double-digit growth streak for the second consecutive quarter. Property stocks also saw some buying interest due to the anticipated positive spillover from the infrastructure projects.
- Foreign investors turned net buyers in July, with net buying amounting to RM1.3 billion worth of equities, reversing from a net selling position of RM61.4 million in June.
- Trading in local stocks will continue to be influenced by interest rate expectations, with the Fed anticipated to deliver its first rate cut in September.

FIXED INCOME: YIELDS EDGED LOWER ON COOLING LABOUR MARKET

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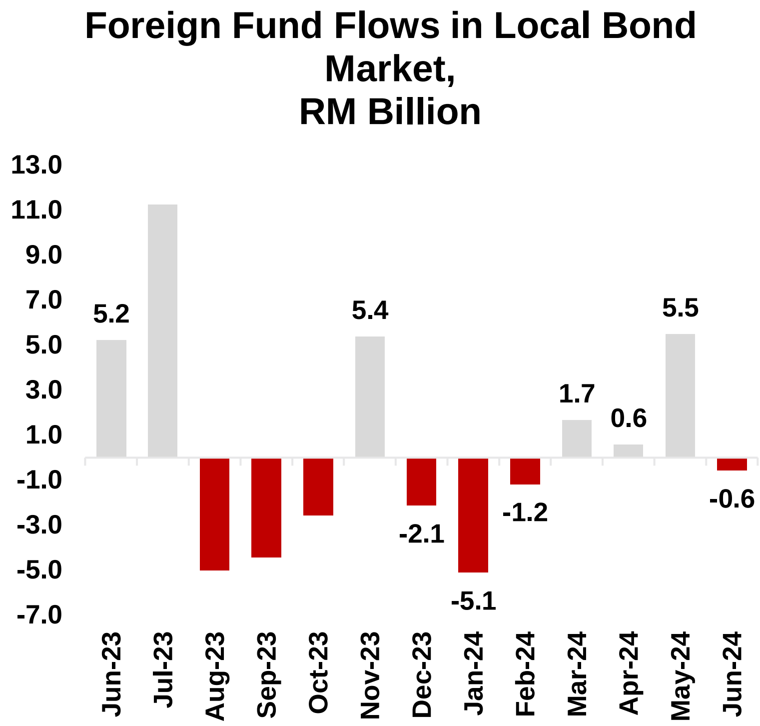
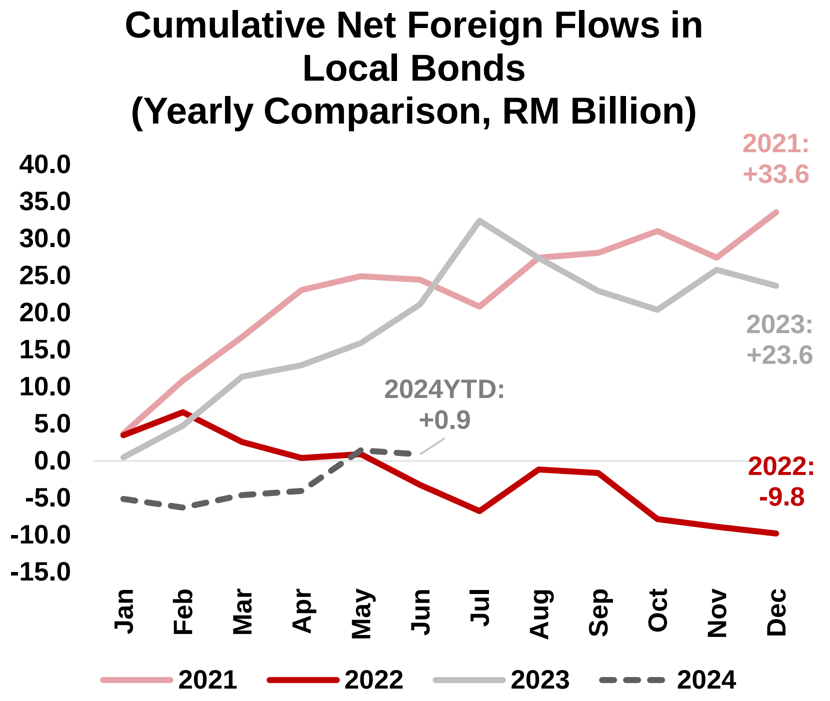
Monthly changes, basis points (bps)			
UST	**Yields (%) 28-Jun-24**	**Yields (%) 31-Jul-24**	**Change (bps)**
3-Y UST	4.52	4.10	-42
5-Y UST	4.33	3.97	-36
7-Y UST	4.33	4.00	-33
10-Y UST	4.36	4.09	-27
MGS	**Yields (%) 28-Jun-24**	**Yields (%) 31-Jul-24**	**Change (bps)**
3-Y MGS	3.53	3.37	-16
5-Y MGS	3.65	3.53	-12
7-Y MGS	3.80	3.68	-12
10-Y MGS	3.86	3.72	-14
GII	**Yields (%) 28-Jun-24**	**Yields (%) 31-Jul-24**	**Change (bps)**
3-Y GII	3.47	3.35	-12
5-Y GII	3.63	3.52	-11
7-Y GII	3.79	3.70	-9
10-Y GII	3.87	3.73	-13

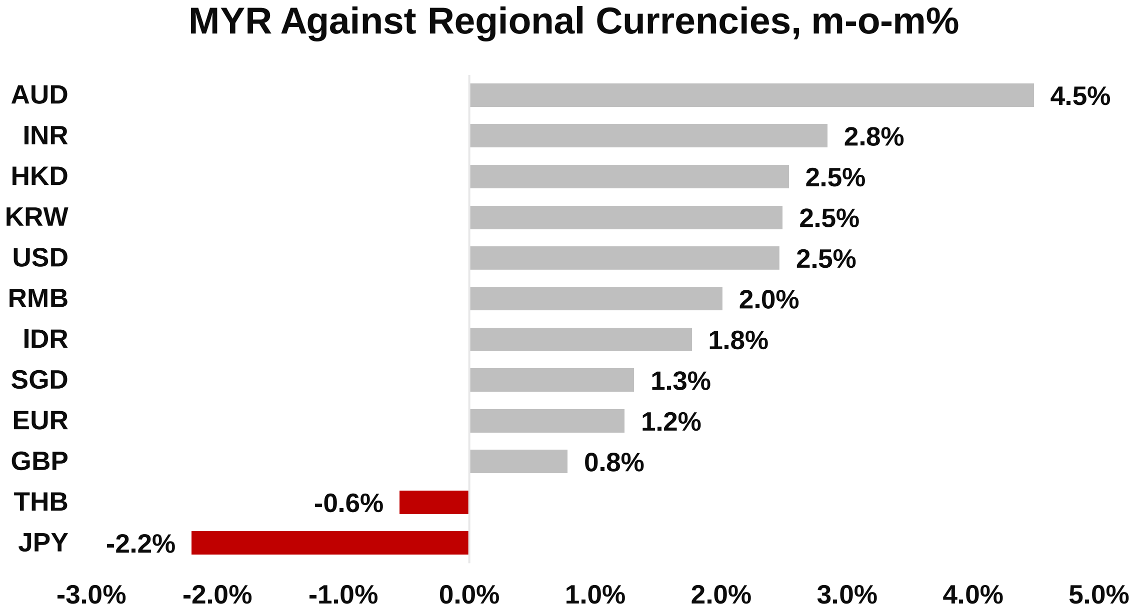
Sources: BNM, Federal Reserve Board

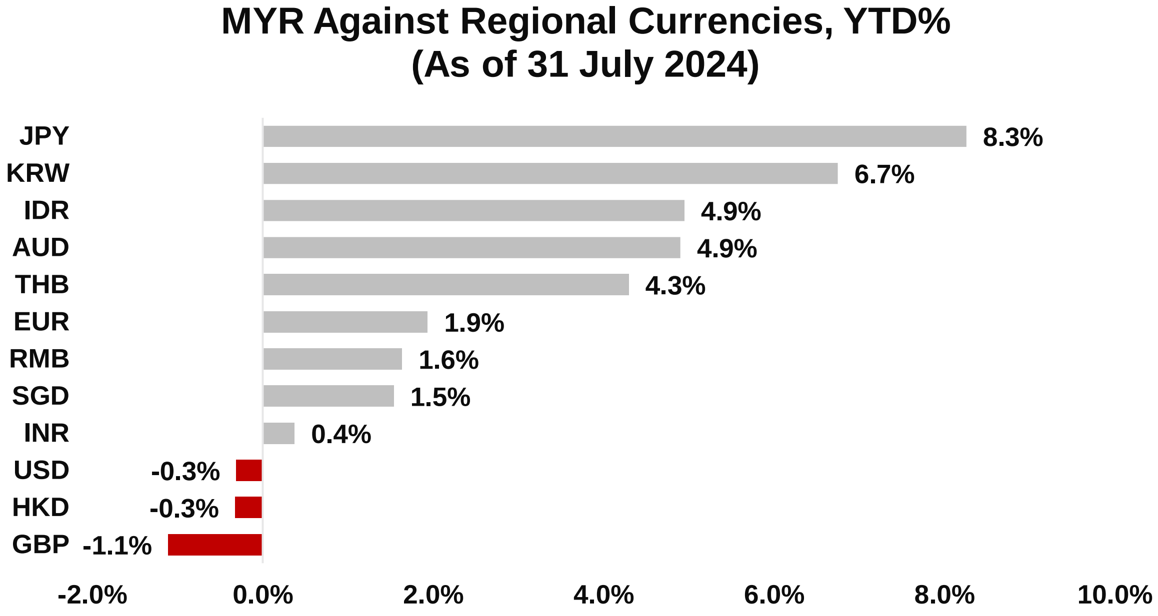




- The U.S. Treasury (UST) yield curve bullishly steepened, with yields falling in the range of 27bps and 42bps as markets digested the Fed's decision to hold interest rates steady at 5.25%-5.50% and expressed concerns about both inflation and employment, acknowledging a cooling labour market.
- Domestically, Malaysian Government Securities (MGS) and Government Investment Issues (GII) yields dipped between 9bps and 16bps.
- Foreign fund flows in the local bond market slumped into the negative territory with a net foreign outflow of RM0.6 billion in June (May: +RM5.5 billion). Nevertheless, local govvies' foreign shareholdings to total outstanding plateaued at 21.6% in June.
- As of 1H2024, the local bond market recorded the cumulative net foreign inflows of RM0.9 billion, significantly lower than the inflows of RM21.2 billion in the same period in the previous year.

FX MARKET: RINGGIT ON A WINNING STREAK AS WEAK U.S. ECONOMIC DATA SLIDES THE SCALE TOWARDS A FED RATE CUT SOON





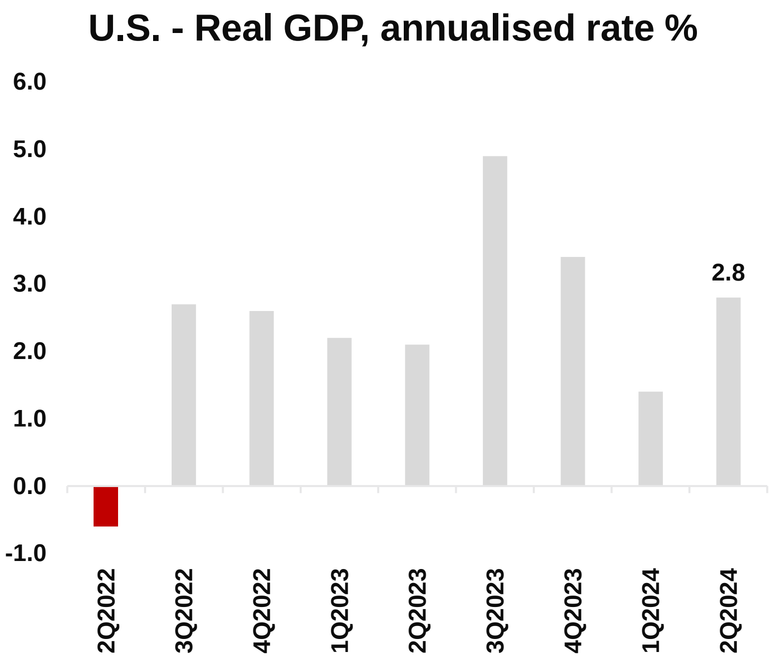
Sources: BNM, Federal Reserve Board, Bank of Japan (BoJ)

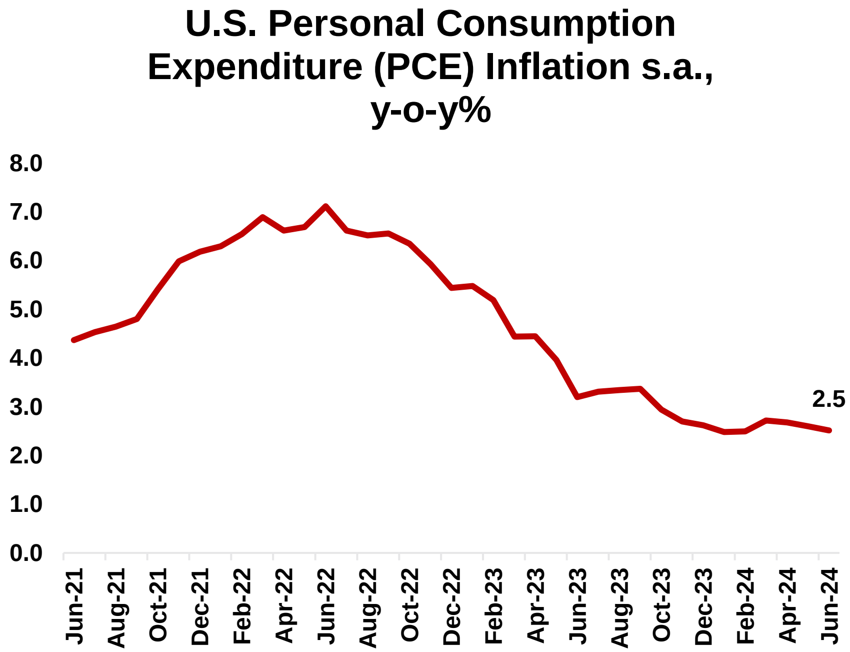
- The Ringgit appreciated against the USD on a monthly basis to close at RM4.606 (June 28: RM4.7195), marking the highest level since the beginning of the year (January 2: RM4.6025). Additionally, the local note had outperformed most other regional currencies for the month.
- Such performance was underpinned by the weakness of the greenback as the USD index trended around the 104-level in the latter half of July, dragged by heightened expectations of Fed rate cuts. A series of softer than expected U.S. economic data throughout the month had reinforced market bets of multiple Fed rate cuts in store, with the first to happen in September. Of note, the inflation gauges had shown signs of moderating price pressures while the job market indicators points towards a cooling labour market.
- Furthermore, the Fed's dovish tone during its July Federal Open Market Committee (FOMC) meeting as well as BoJ's larger-than-expected rate hike to 0.25% from the range of 0% to 0.1% had further weighed on the greenback.
- Nevertheless, following the BoJ rate hike, the local note slipped by 2.2% against the Japanese Yen as it rallied from its multi-decade weakness.

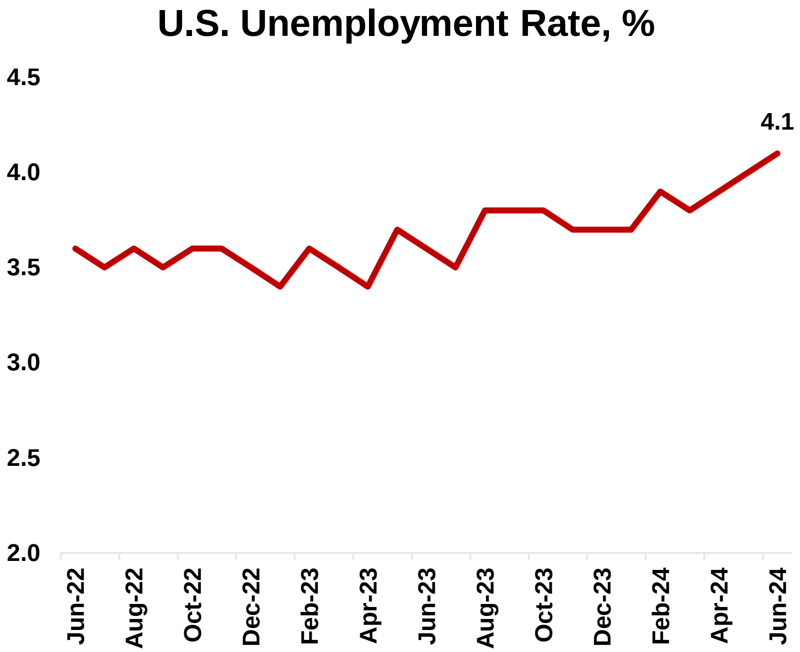
SECTION 2

The Global Economy

THE LOOMING THREAT OF A HARD LANDING IN THE U.S.







Sources: Bureau of Economic Analysis, CEIC Data

- Powered by robust consumer spending and business investment, the U.S. economy expanded at a faster-than-anticipated pace in 2Q2024 (Act: 2.8% vs. Est: 2.0%). Despite this growth, cooling inflation pressures kept expectations intact for a Fed interest rate reduction in September. The Fed's preferred inflation measure, PCE inflation, cooled to 2.5% in June (Jul: 2.6%), as expected, increasing the likelihood of a rate cut this year.
- More Americans filed for unemployment for the week ending July 27, with weekly jobless claims increased by 14K to 249K, higher than the market forecast of 236K, signaling a potential slowdown in the job market. However, the initial jobless initial claims number can fluctuate during summer. Additionally, the U.S. unemployment rate also ticked higher to 4.1% in June (May: 4.0%).
- As expected, the Fed opted to hold interest rates steady at its July FOMC meeting, marking the eighth consecutive time it has done so.
- The anticipated soft landing for the U.S. economy is no longer expected. Instead, the looming threat of a hard landing in the U.S. are growing.

CHINA'S 2Q2024 GROWTH DISAPPOINTS, FULL-YEAR TARGET IN JEOPARDY

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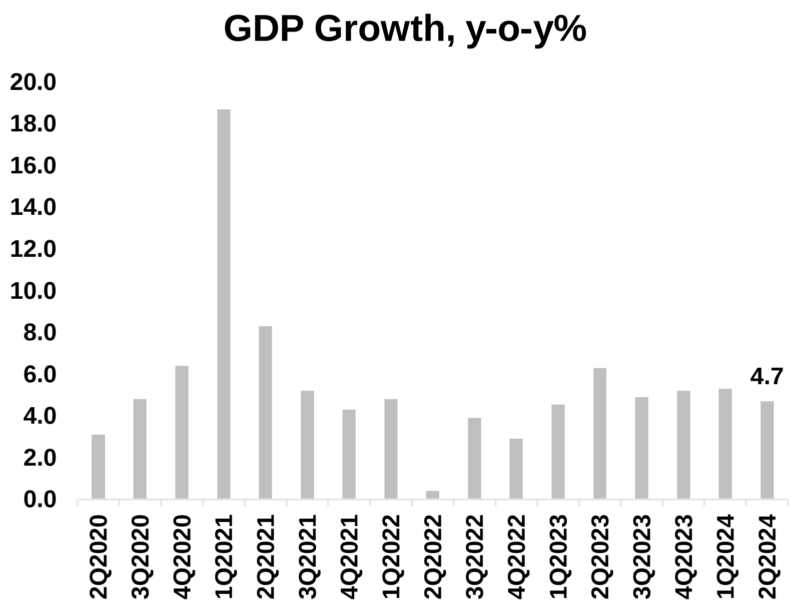

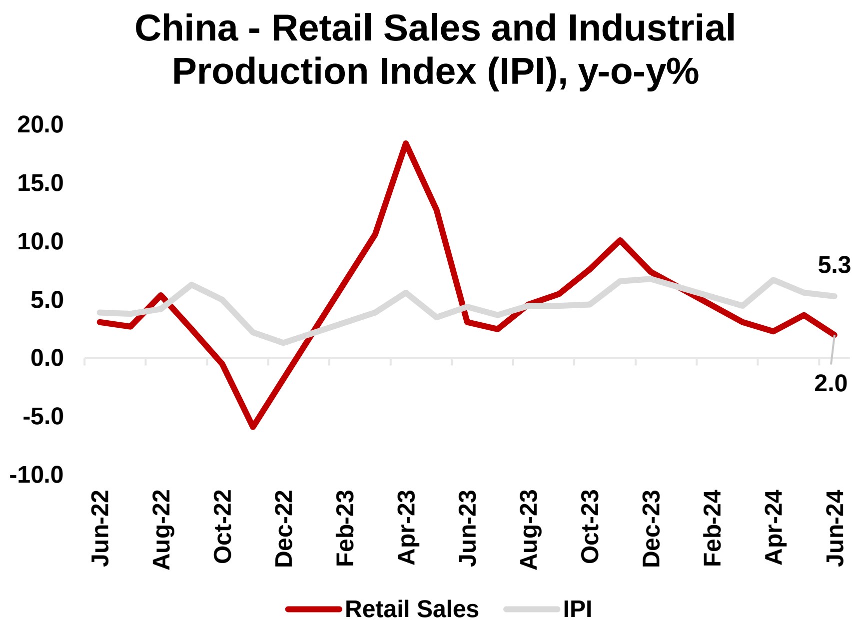

Sources: National Bureau of Statistics, CEIC Data

- China's economy grew slower than expected in 2Q2024 with the GDP expanded by 4.7%, falling short of the market's projection of 5.1%. Additionally, retail sales also underperformed forecasts, increasing by 2.0% instead of the anticipated 3.3% in June.
- On a brighter note, industrial production exceeded expectations, growing by 5.3% in June compared to the market forecast of 5.0%. The high-tech sector was a standout, with a robust 8.8% increase in value added.
- China's exports have surprisingly buoyed the economy, growing by a stronger-than-expected 8.6% in June (May: 7.6%).
- However, imports underperformed expectations, falling by 2.3% in June (May: 1.8%). While exports have been a bright spot, ongoing trade tensions cloud the outlook.
- China faces an uphill battle to achieve its target of around 5.0% growth for the year. The economy expanded by merely 5.3% in 1H2024, and further expansion is likely to be more subdued in 2H2024.

BANK OF JAPAN’S HAWKISH POLICY TILT

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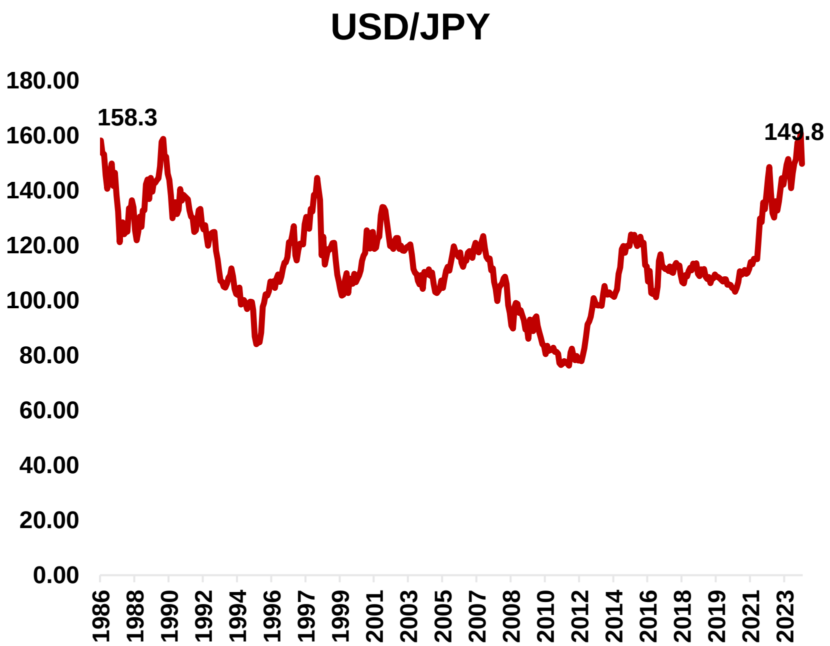
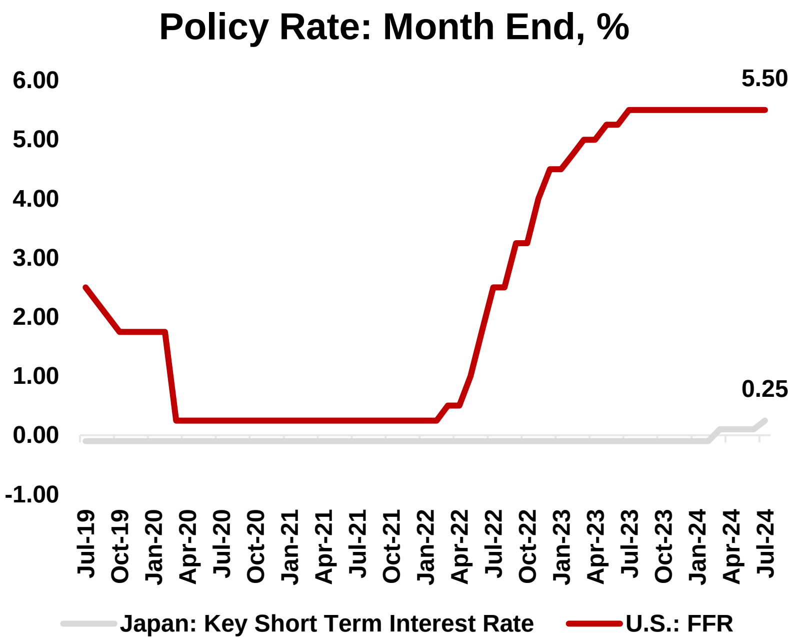
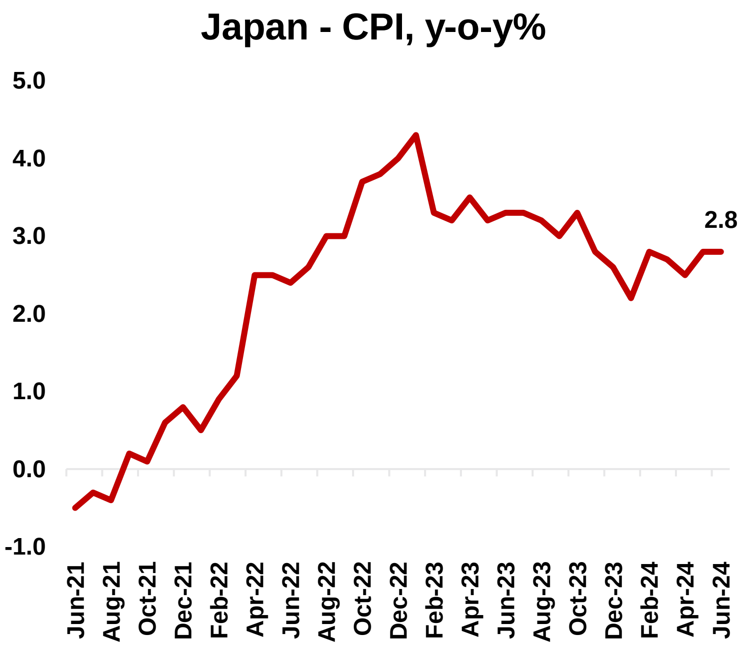






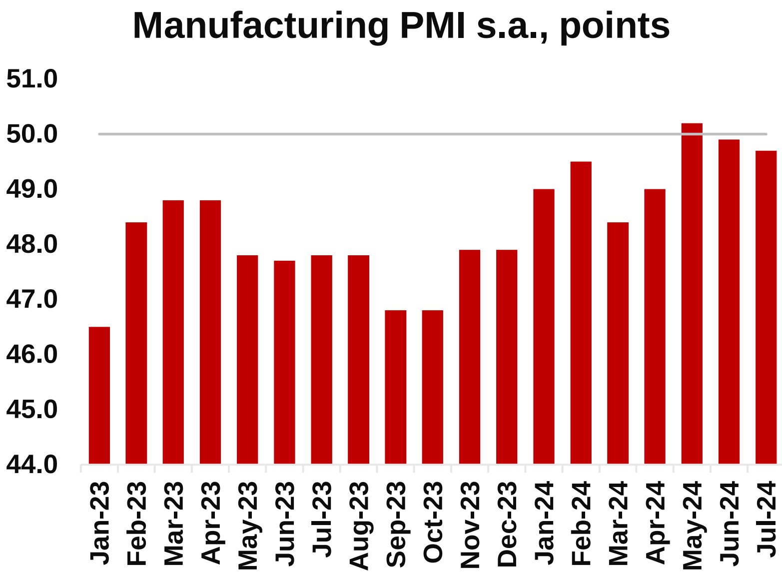
Sources: Federal Reserve Economic Data (FRED), CEIC Data

- The Japanese yen surged to its highest level since February, hovering lower than 150 per dollar as investors sought safe havens amid growing U.S. recession fears. The yen also climbed to its highest levels in months versus the pound and euro after the BoE cut rates and a ECB official made dovish remarks.
- The BoJ tightened monetary policy by raising its policy rate to 0.25%, its highest level in 16 years. The central bank also indicated a readiness to implement additional rate hikes if economic conditions warrant. Market participants anticipate two more rate increases before the end of the fiscal year in March 2025, with the next one expected in December.
- To bolster the yen, Japanese authorities intervened in the foreign exchange market in July, spending a substantial 5.53 trillion yen. The government expressed concern that a weakening yen is exacerbating inflation, outpacing wage growth, and underscored the critical importance of currency support.

SECTION 3

Domestic Landscape & Banking Sector Update

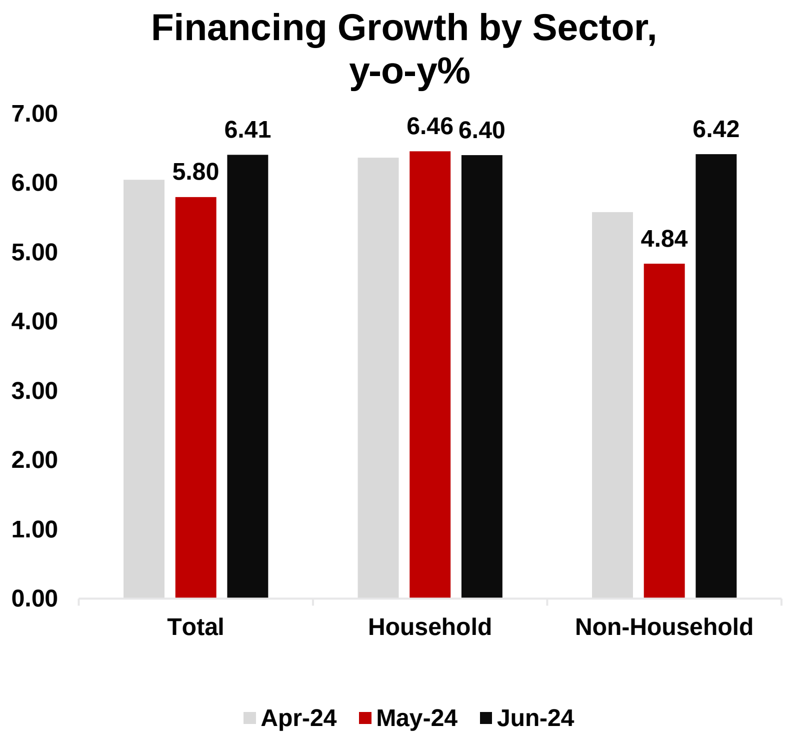
MALAYSIA'S ECONOMY IS EXPECTED TO CONTINUE ON THE ROSY ROAD WHILE TRADE WILL STRENGTHEN FURTHER

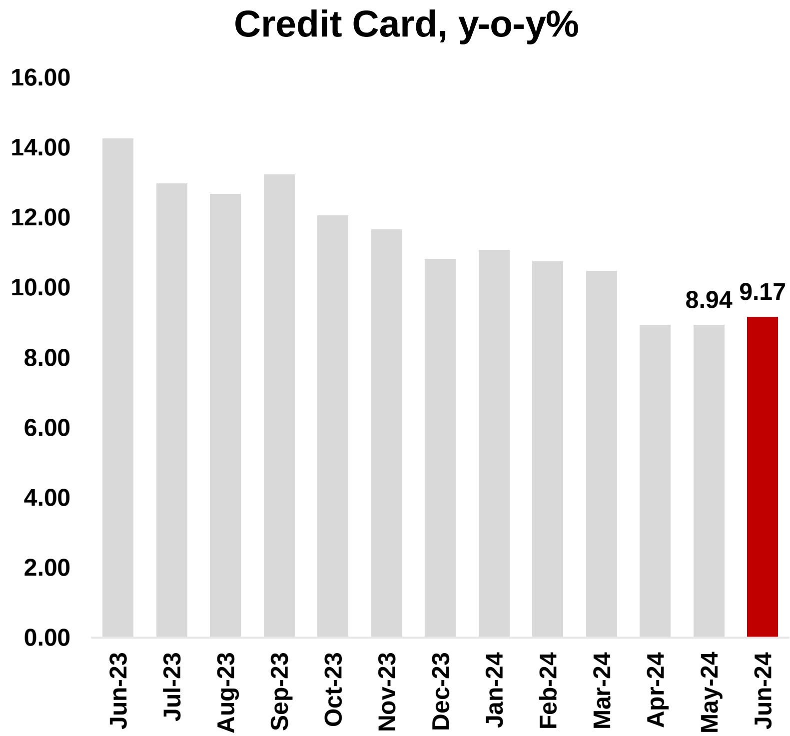


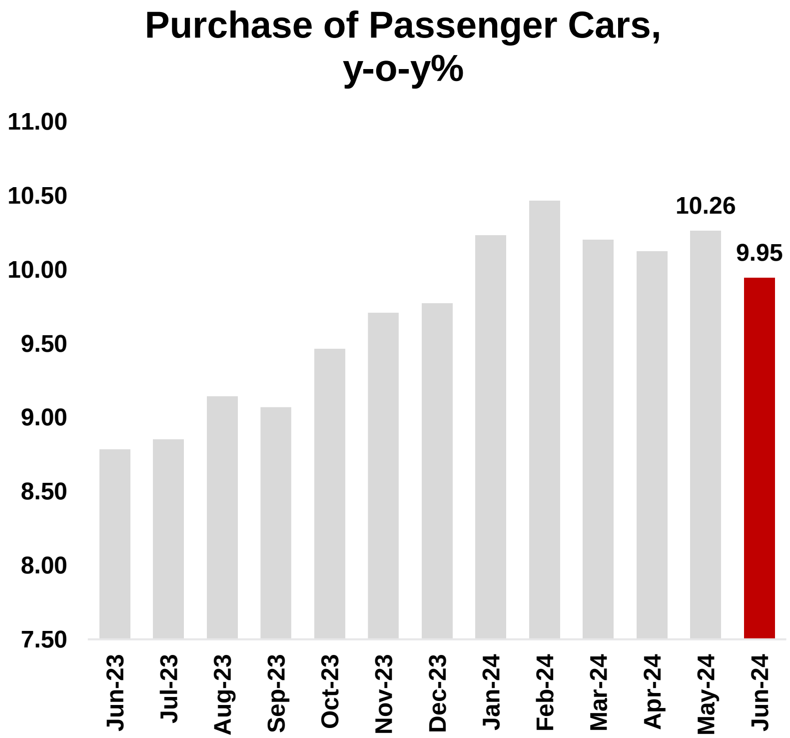
Sources: DOSM, BNM, S&P Global

- Official preliminary estimates expects Malaysia's economy to expand by 5.8% in 2Q2024 (1Q2024: 4.2%), driven by low base effect and a broad-based expansion across all sectors.
- The Construction sector, which surprised markets in the first quarter, continued its double-digit expansion at 17.2% (1Q2024: 11.9%) amid realized investment and infrastructure development projects.
- In tandem with the robust construction and production activities, imports rose by 15.0% (1Q2024: 12.5%), buoyed by the imports of capital goods (23.5%) and intermediate goods (37.2%). Meanwhile, exports picked up after last year's sluggish performance, expanding by 5.8% in the same quarter (1Q2024: 2.0%), underpinned by the tech upcycle and rising global demand.
- Nevertheless, factory activities had moderated in July with business firms reporting slowdowns in new orders, output and stocks. Malaysia's manufacturing PMI recorded the second month of contraction (July: 49.7 points vs. June: 49.9 points).
- Furthermore, the input cost inflation rose to an eight-month high amid higher raw material costs as well as transportation costs following the diesel subsidy rationalisation on June 10.

BANKING SECTOR: FINANCING GROWTH REMAINED STABLE IN JUNE



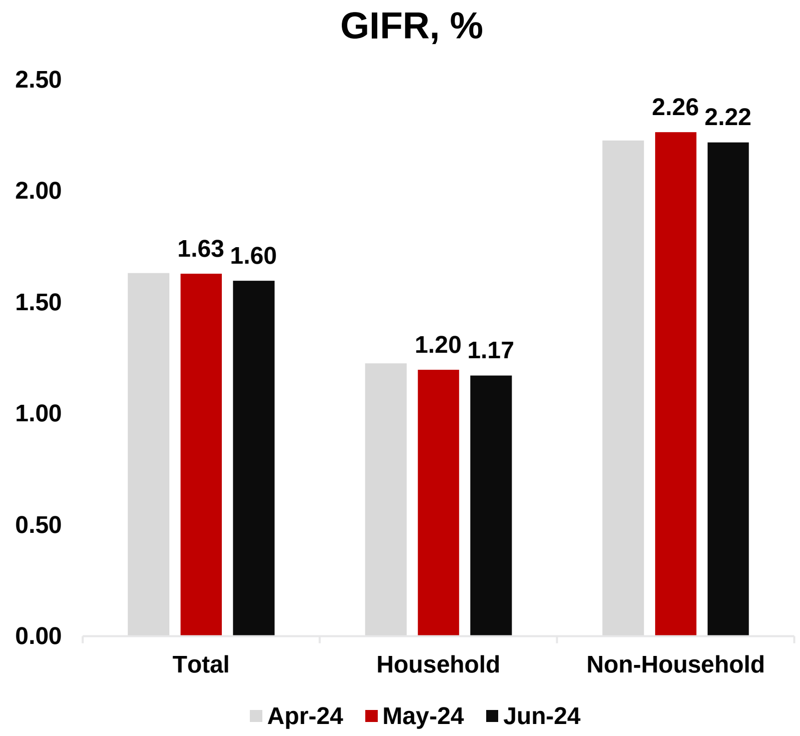


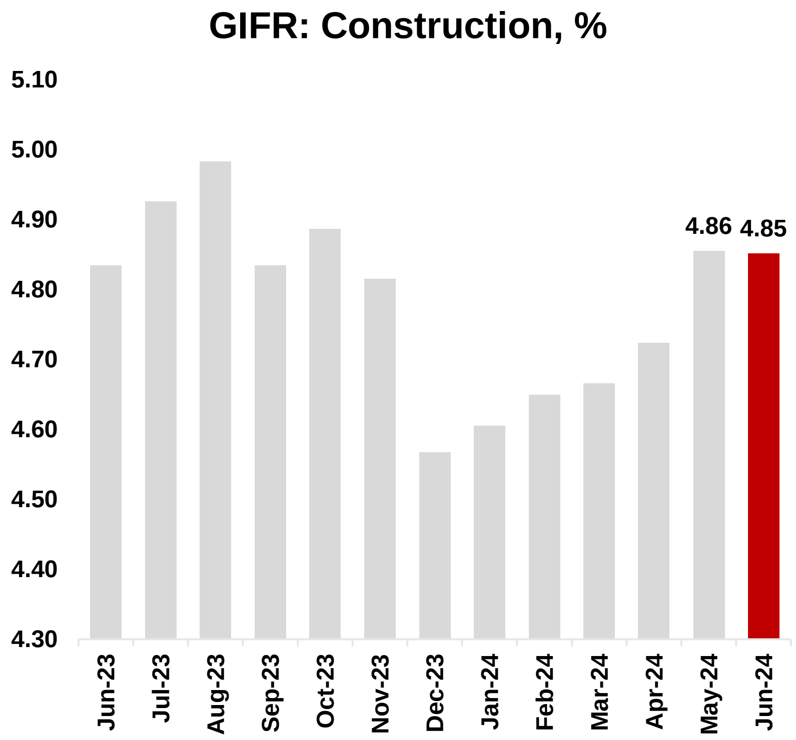


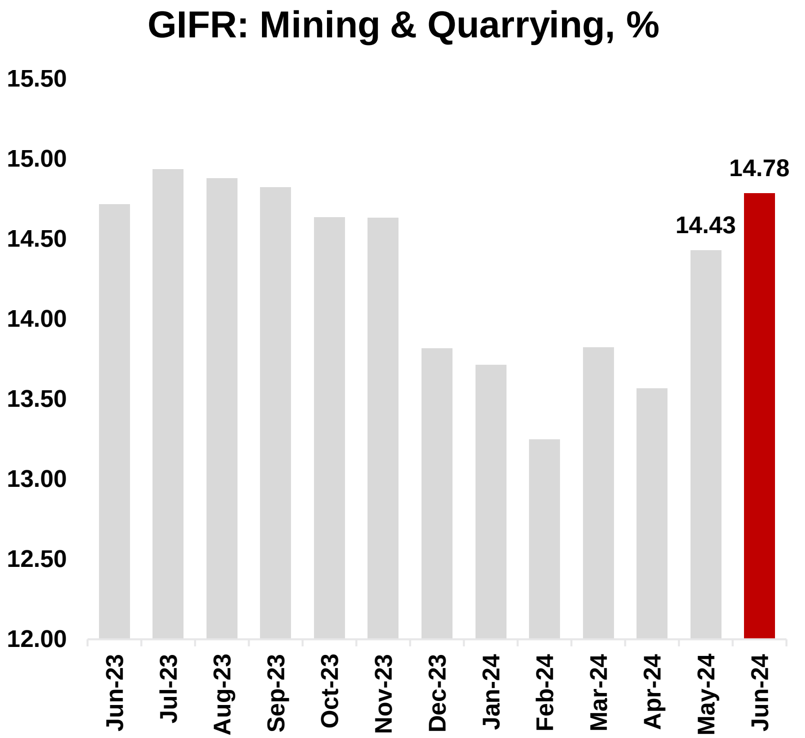
Source: BNM

- Financing activities increased to 6.41% in June, up from 5.80% in May. The non-household segment’s financing growth surged to 6.42% in June (May: 4.84%). Conversely, the household sector's growth rate decline marginally to 6.40% in June from 6.46% in May.
- The financing growth in the passenger car purchase segment dropped to 9.95% in June (May: 10.26%). However, financing growth in the credit card segment grew slightly to 9.17% in June from 8.94% in May. Meanwhile, financing activities related to the purchase of residential property reduced to 7.49% in June (May: 7.57%).

BANKING SECTOR: JUNE'S ASSET QUALITY REMAINED SOUND







Source: BNM

- Total gross impaired financing ratio (GIFR) in the banking sector decreased slightly to 1.60% in June (May: 1.63%). The GIFR in the household segment moderated to 1.17% in June (May: 1.20%). Additionally, the impairment within the non-household sector declined to 2.22% in June (May: 2.26%).
- The impairment within the construction segment eased to 4.85% in June from 4.86% in May. Conversely, the asset quality in the Mining and Quarrying industry escalated to 14.78% in June (May: 14.43%).

THANK YOU