BANK ISLAM

MONTHLY ECONOMIC UPDATE

3 NOVEMBER 2023

ECONOMIC RESEARCH

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KEY TAKEAWAYS

- **The Fed kept the interest rate steady at its 22-year high of 5.25%-5.50%.** This marked the second straight time decision during the November meeting, reflecting policymakers' dual focus on returning inflation to the 2.0% target while avoiding excessive monetary tightening. Also, recent indicators suggested that economic activity expanded at a strong pace in 3Q2023, with job gains remaining strong albeit at a moderate pace since earlier in the year and the unemployment rate has remained low. In a post-meeting conference, the Federal Reserve (Fed) Chairman Jerome Powell stated that the central bank would continue reviewing economic data and proceeding carefully with rate moves following a strong economy.

- **ECB halted its rate hiking cycle.** As widely anticipated, the European Central Bank (ECB) kept its key deposit facility rate on hold at 4.00% in October's policy meeting amid rising concerns about the impact of previous rate hikes on the economy. The Eurozone economy fell 0.1% in 3Q2023, following an upwardly revised 0.2% expansion in 2Q2023. Should there be no upward statistical revision, this marked the economy's first contraction since 4Q2020 during the pandemic crisis, raising the possibility of a narrow technical recession in 2H2023. Meanwhile, Eurozone headline and core inflation declined notably to 2.9% and 4.2% in October, from 4.3% and 4.5% in September, respectively. While inflation has more than halved from the peak, it remains well above the ECB's 2.0% target. ECB hinted at maintaining the current rates for a longer duration while opening the door for another hike if necessary.

- **China's economy shows green shoots as stimulus starts to take effect.** China's 3Q2023 gross domestic product (GDP) growth came in above consensus at 4.9% but slower than the 6.3% recorded in 2Q2023 as the favourable base effect dissipated. In September alone, growth in retail sales picked up to 5.5% (August: 4.6%) while industrial production maintained the highest growth rate since April 2023 at 4.5% (August: 4.5%). Moreover, the surveyed urban unemployment rate fell to 5.0% in September (August: 5.2%). The recent stronger-than-expected economic data has lifted hopes that the China's economy will meet the official growth target of 5.0% this year.

KEY TAKEAWAYS

- **MAS maintains monetary policy settings for the second time this year amid a fragile economic recovery and still-elevated inflation.** The Monetary Authority of Singapore (MAS) decided to retain the prevailing rate of appreciation of its Singapore dollar nominal effective exchange rate (SGD NEER) policy band, believing that the current SGD NEER policy band is “sufficiently tight.” Singapore’s advance GDP growth for 3Q2023 remained moderate at 0.7% while improving slightly from 0.5% in 2Q2023. The MAS expects 2023 full-year GDP growth to come in at the lower half of the official growth forecast range of 0.5%-1.5% amid the muted growth prospects in the near term. Meanwhile, core inflation has slowed but remained above the MAS’ comfort level (September: 3.0% vs. August: 3.4%). The MAS chief Ravi Menon, in his recent remarks, has said that it is too early to declare victory over inflation and that it is premature to talk about a loosening in monetary policy.

- **Indonesia and the Philippines have resumed hiking interest rates.** Bank Indonesia (BI) delivered a surprise 25bp hike, bringing the benchmark 7-day reverse repurchase rate to 6.00% in a bid to defend the Indonesian Rupiah (IDR). BI believes that “a stronger policy response” was needed as the prospects of higher-for-longer U.S. interest rates would see capital outflow persisting for the rest of the year. Meanwhile, the Bangko Sentral ng Philippines (BSP) raised the benchmark rate by 25bps to 6.50%, the highest in the region, in an off-cycle move. The rate hike decision indicated the BSP’s commitment to contain inflation, which accelerated to 6.1% in September 2023 (August: 5.3%). With inflation likely to stay elevated, another rate hike remains on the card for the rest of the year.

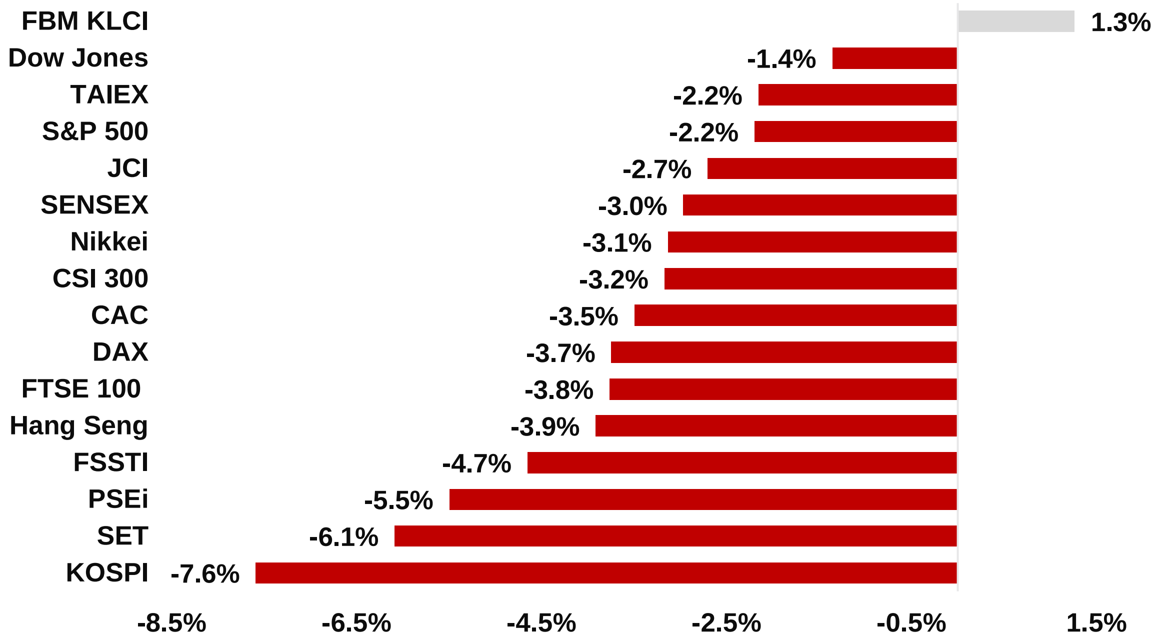
- **DOSM estimates Malaysia’s 3Q2023 GDP growth at 3.3% y-o-y.** The inaugural quarterly GDP advance estimate report by the Department of Statistics Malaysia (DOSM) showed that Malaysia’s economy likely improved in 3Q2023 (2Q2023: 2.9%), mainly driven by the services sector (5.1% vs. 2Q2023: 4.7%). The strong growth in the services sector is in line with the still robust wholesale and retail trade. The agriculture sector also rebounded (0.8% vs. 2Q2023: -1.1%) on the back of higher oil palm production. Meanwhile, the manufacturing (-0.1% vs. 2Q2023: 0.1%) and the mining and quarrying (-0.1% vs. 2Q2023: -2.3%) sectors contracted. Notwithstanding this, we opine that the actual GDP growth in 3Q2023 will come in lower than the advance estimate as September’s data pointed to still weak factory activities and a contraction in exports.

SECTION 1

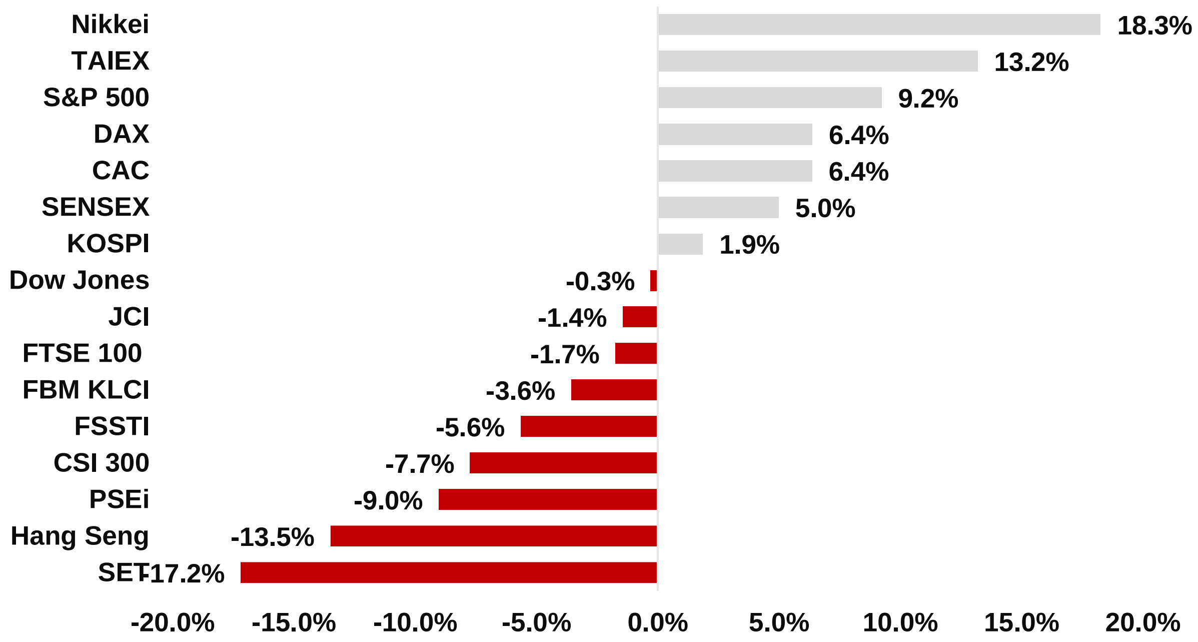
Malaysia’s Financial Market

REGIONAL EQUITY: SEA OF RED ACROSS GLOBAL STOCKS MARKET AMID CAUTIOUS SENTIMENT AMONG INVESTORS

Monthly Gain/Loss of Major Equity Market, m-o-m%



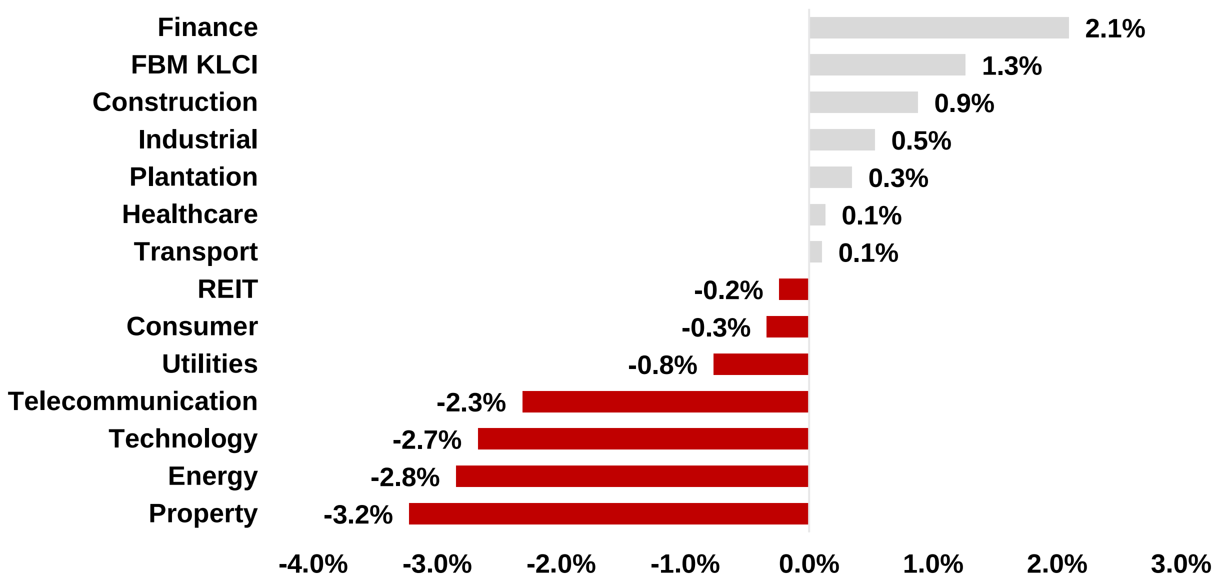
YTD Gain/Loss of Major Equity Markets, %
(As of 31 October 2023)

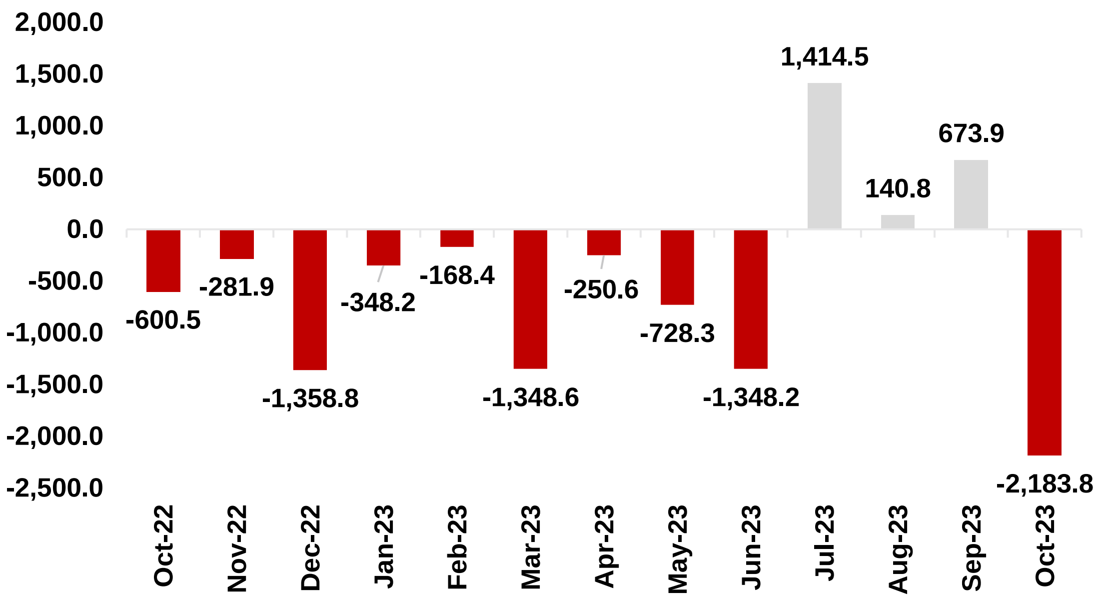


Sources: Bursa, CEIC data

- Overall, the regional benchmark indices mostly ended in the red in October, with FBM KLCI logged as the only winner, rising by 1.3%.
- Asian stocks were mainly the major losers dragged down by the weaker-than-expected Chinese data, with China's manufacturing Purchasing Managers' Index (PMI) in October dropped to a contraction zone of 49.5 points, after growing slightly to 50.2 points in September, according to the official National Bureau of Statistics (NBS) data.
- Additionally, investors continued to be cautious over the Fed's interest rates path and the possibility of another rate hike in the final Federal Open Market Committee (FOMC) meeting in December this year, as well as the precarious impact of the Israel-Hamas conflict.
- For the first ten months of 2023, Japan's Nikkei remained as the top performer, albeit with a smaller gain of 18.3% from 22.1% in the previous month.

DOMESTIC EQUITY: THE FBM KLCI ENDED IN THE GREEN ON BUYING IN HEAVYWEIGHTS





Sources: Bursa, BNM, CEIC data

- The FBM KLCI ended the month of October higher by 1.3% at 1,442.14, led by gains in Finance (2.1%) and Construction (0.9%) stocks.
- However, slightly more than half of the Bursa sectoral indices registered losses, with Property (-3.2%), Energy (-2.8%) and Technology leading the declines. The lack of fresh catalysts in the domestic market and the concerns surrounding the weakening ringgit kept investors in a cautious mood.
- Foreign investors turned net sellers for the first time after three consecutive months of net buying. They had net sold RM2.2 billion worth of equities from a buying position of RM673.9 million in September, the highest net selling month this year.
- Trading in local stock markets will be dictated by earnings reports, which will be rolling in the coming weeks.

FIXED INCOME: YIELDS SURGED AND LOCAL BONDS LOGGED SECOND CONSECUTIVE MONTHS OF NET FOREIGN OUTFLOWS

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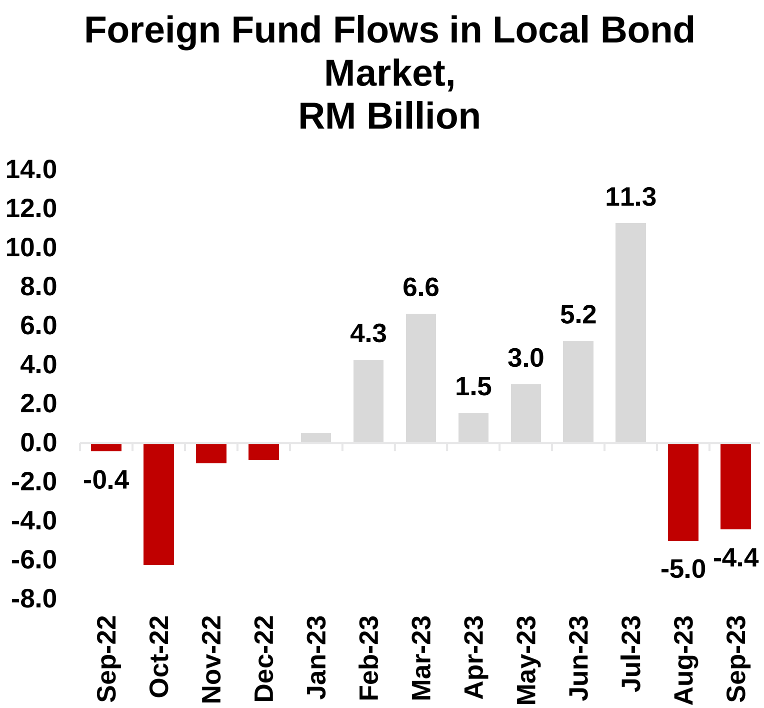
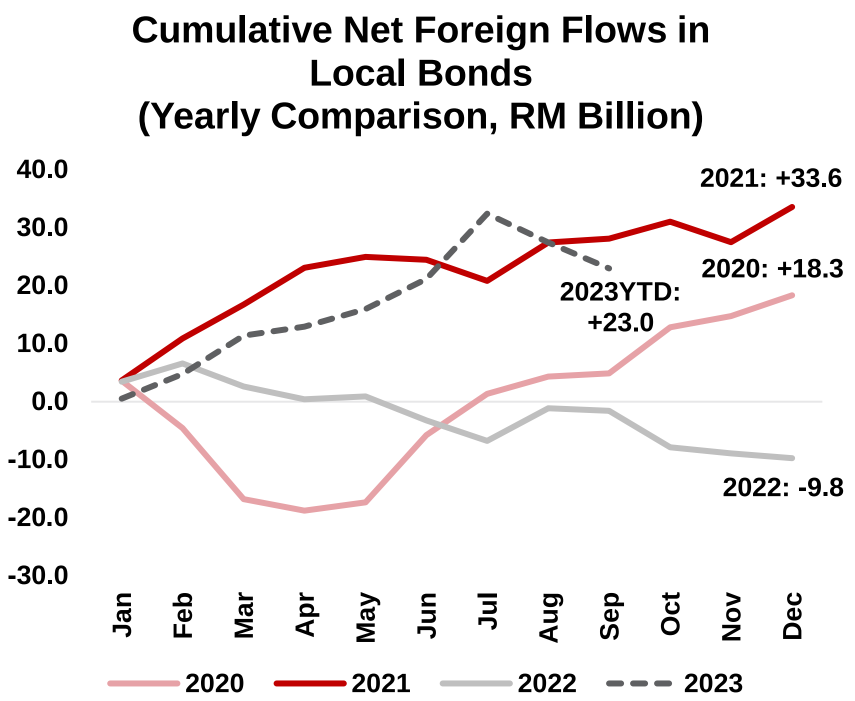
Monthly changes, basis points (bps)

UST	Yields (%) 29-Sep-23	Yields (%) 31-Oct-23	Change (bps)
3-Y UST	4.80	4.90	10
5-Y UST	4.60	4.82	22
7-Y UST	4.61	4.89	28
10-Y UST	4.59	4.88	29
MGS	**Yields (%) 29-Sep-23**	**Yields (%) 31-Oct-23**	**Change (bps)**
3-Y MGS	3.58	3.66	9
5-Y MGS	3.72	3.85	13
7-Y MGS	3.89	4.07	18
10-Y MGS	3.98	4.09	11
GII	**Yields (%) 29-Sep-23**	**Yields (%) 31-Oct-23**	**Change (bps)**
3-Y GII	3.60	3.70	10
5-Y GII	3.80	3.88	7
7-Y GII	3.91	4.08	17
10-Y GII	4.01	4.10	9

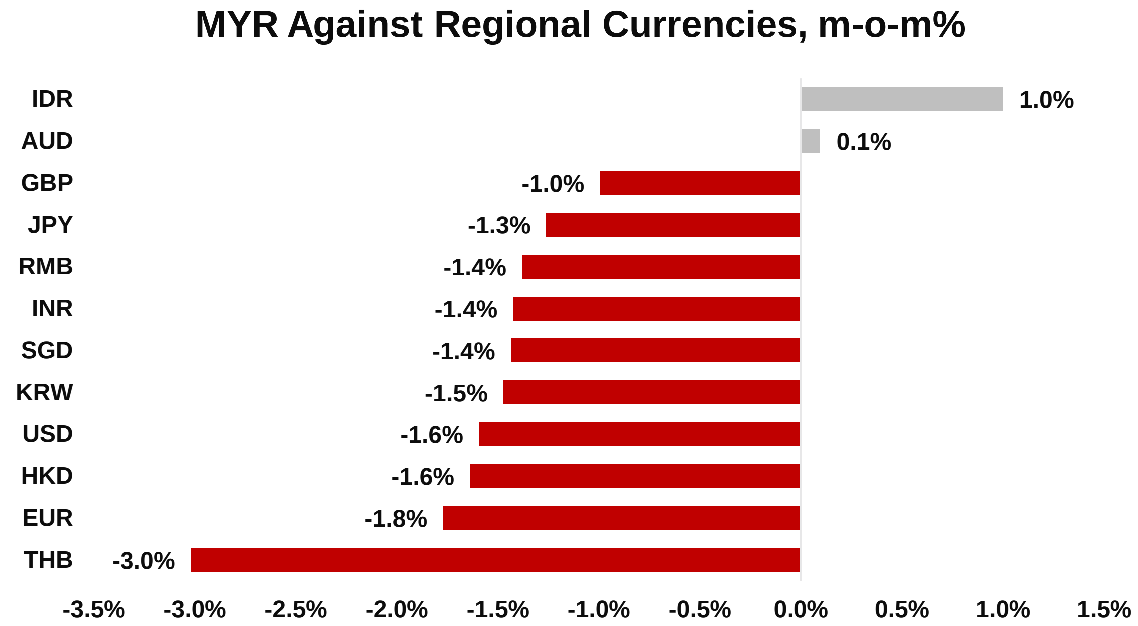
Sources: BNM, Federal Reserve Board

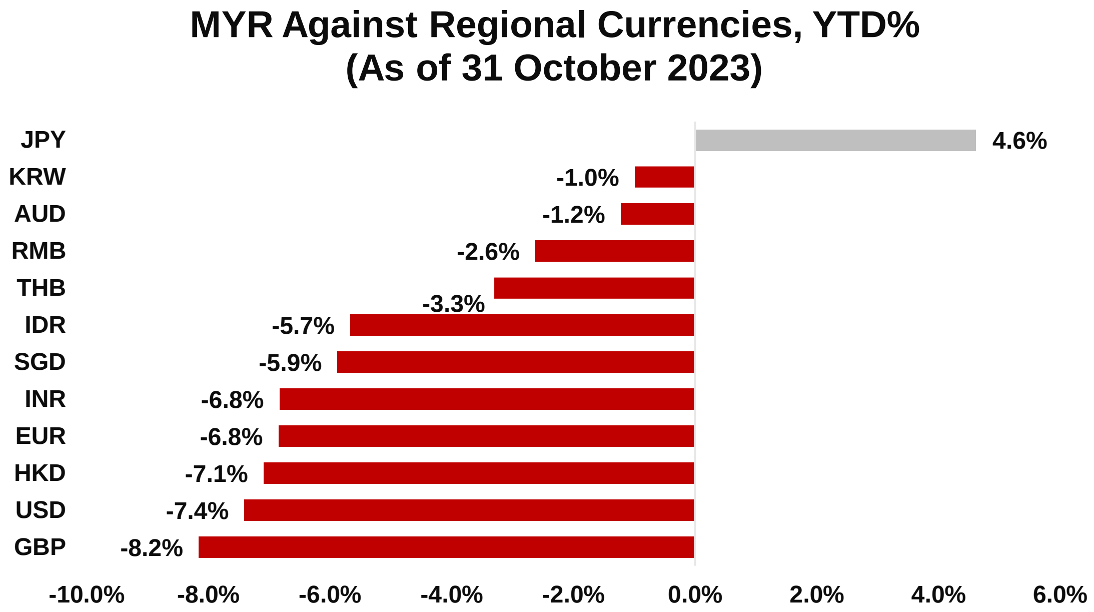




- The UST yield curve bearishly steepened, with yields surged in the range of 10bps and 29bps ahead of the Fed's monetary policy decision on November 1 and expectations on whether another rate hike is still on the card in December's FOMC meeting.
- Both Malaysian Government Securities (MGS) and Government Investment Issues (GII) yields ended weaker between 7bps and 18bps in October Meanwhile, the 10y MGS/UST yield spread remained in the negative territory of 79bps as at end-October 2023.
- Local bond market logged second consecutive months of net foreign outflows of RM4.4 billion in September albeit marginally lower than the outflows of RM5.0 billion in August. Local govvies' foreign shareholdings to total outstanding dipped to 22.8% in September (August: 23.4%).
- The outflows reduced the cumulative net foreign inflows to RM23.0 billion for the first nine month of this year although still higher than the outflows of RM1.6 billion in the same period in the previous year. The foreign flows in the local market are expected to remain volatile as the surge of UST yields will entice yield-seeking investors.

FX MARKET: RINGGIT TO REMAIN VOLATILE IN THE MEDIUM TERM DUE TO THE EXTERNAL PRESSURES





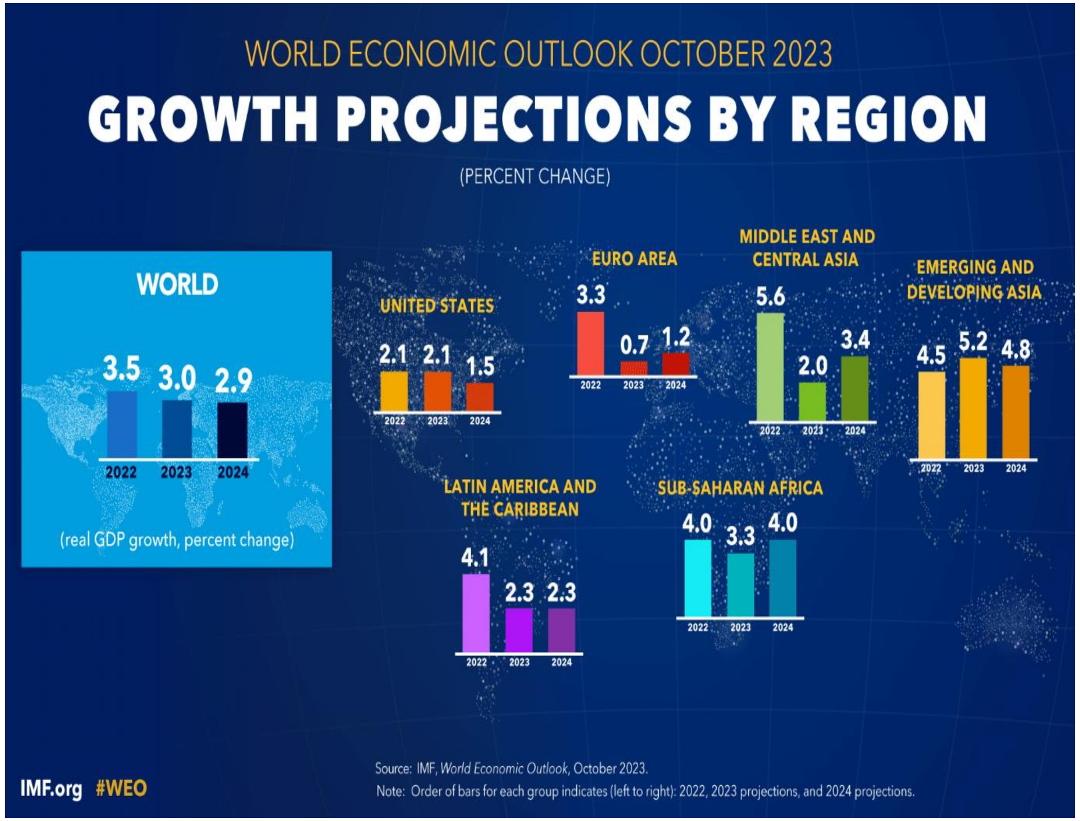
Source: BNM

- Ringgit hit an all-time low against the USD on 19 October 2023, a level that was last seen during the Asian Financial Crisis (AFC). One of the primary reasons was due to the country's widening interest rate – 250 bps below the upper bound of the U.S.'FFR.
- The volatility in the bond market also did not help when the 10-Y yield rose to 5.00% for the first time since 2007, following cues from Powell's remarks that the monetary policy was not yet too restrictive. As such, the local note weakened against the greenback on a monthly basis, closing at RM4.7660 on 31 October 2023 from RM4.6900 in the previous month.
- The recent U.S. FOMC meeting saw the central bank hold the FFR steady again, reflecting the policymakers' pledge to proceed carefully in the face of growing uncertainties. While the FFR may have peaked, it is the higher-for-longer prospect is concerning. As such, we foresee that the local note would remain under pressure against the greenback.
- Additionally, the recent local depreciation aligned with the strengthening of the USD, prompted by heightened safe-haven demand amid concerns over the ongoing Israel-Hamas conflict.

SECTION 2

The Global Economy

IMF: THE GLOBAL ECONOMY CONTINUES TO FACE STEEP CHALLENGES FOLLOWING ONGOING CHALLENGES



Source: World Economic Outlook (WEO) Update October 2023, IMF

- The global growth remains low and uneven though the remarkable strength in the U.S. economy. The global GDP growth is left unchanged at 3.0% in 2023 but cuts its 2024 growth to 2.9% from 3.0% in July's outlook.
- Likewise, advanced economies are also expected to experience a decline, dropping from 2.6% in 2022 to 1.5% in the next year and further down to 1.4% in the following year, partly attributable to the effects of monetary policy tightening in curbing the inflationary pressures.
- According to IMF, the disclosed projections in the latest WEO reflect <u>one of the lowest growth rates in decades</u> as the global economy is grappling with multiple shocks and the cost-of-living issue.

MEAWNHILE, IMF PROJECTED AN INCREASE IN MALAYSIA'S GROWTH NEXT YEAR

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	Real GDP		
		Projections	
	2022	2023	2024
Asia	**3.9**	**4.6**	**4.2**
Advanced Asia	**1.8**	**2.1**	**1.8**
Japan	1.0	2.0	1.0
Korea	2.6	1.4	2.2
Taiwan Province of China	2.4	0.8	3.0
Australia	3.7	1.8	1.2
Singapore	3.6	1.0	2.1
Hong Kong SAR	–3.5	4.4	2.9
New Zealand	2.7	1.1	1.0
Macao SAR	–26.8	74.4	27.2
Emerging and Developing Asia	**4.5**	**5.2**	**4.8**
China	3.0	5.0	4.2
India[4]	7.2	6.3	6.3
Indonesia	5.3	5.0	5.0
Thailand	2.6	2.7	3.2
Vietnam	8.0	4.7	5.8
Philippines	7.6	5.3	5.9
Malaysia	8.7	4.0	4.3
Other Emerging and Developing Asia[5]	**3.9**	**3.8**	**5.6**
Memorandum			
ASEAN-5[6]	**5.5**	**4.2**	**4.5**
Emerging Asia[7]	**4.5**	**5.2**	**4.8**

Source: World Economic Outlook (WEO) Update October 2023, IMF

- The country's real GDP is projected to grow to 4.3% y-o-y in 2024 from 4.0%, mainly driven by higher global export demand, specifically from the technology sector.
- This is in view of Malaysia's open economy particularly in the electrical and electronic products export.
- On the inflation front, the rate has been gradually slowing since the start of the year. However, it is notably that the recent subsidy reforms which tabled in Budget 2024 last month could pose some risks.

THE U.S. ECONOMY EXPERIENCED A ROBUST GROWTH RATE DESPITE HIGH INTEREST RATES

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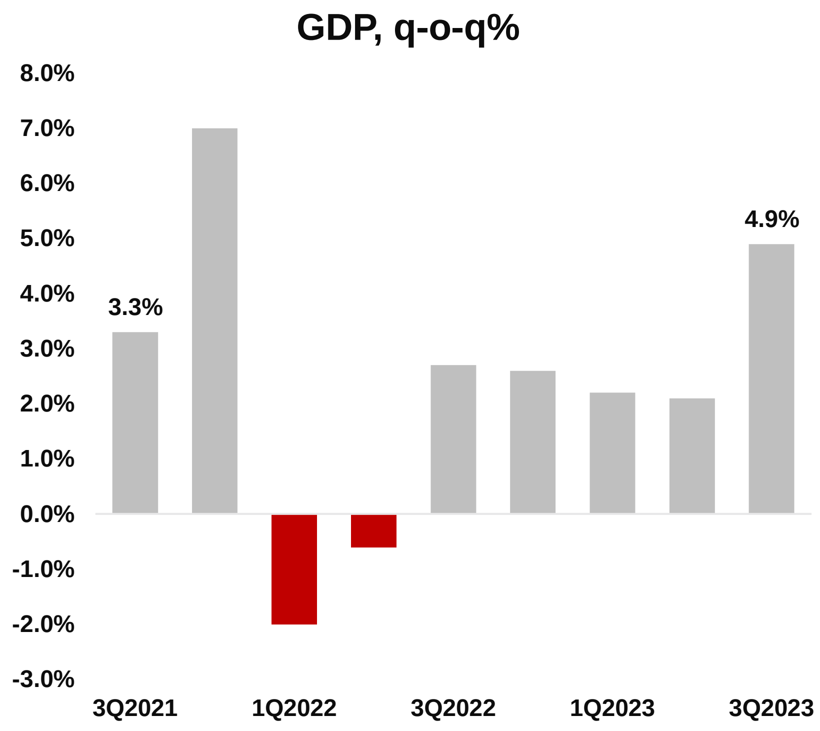

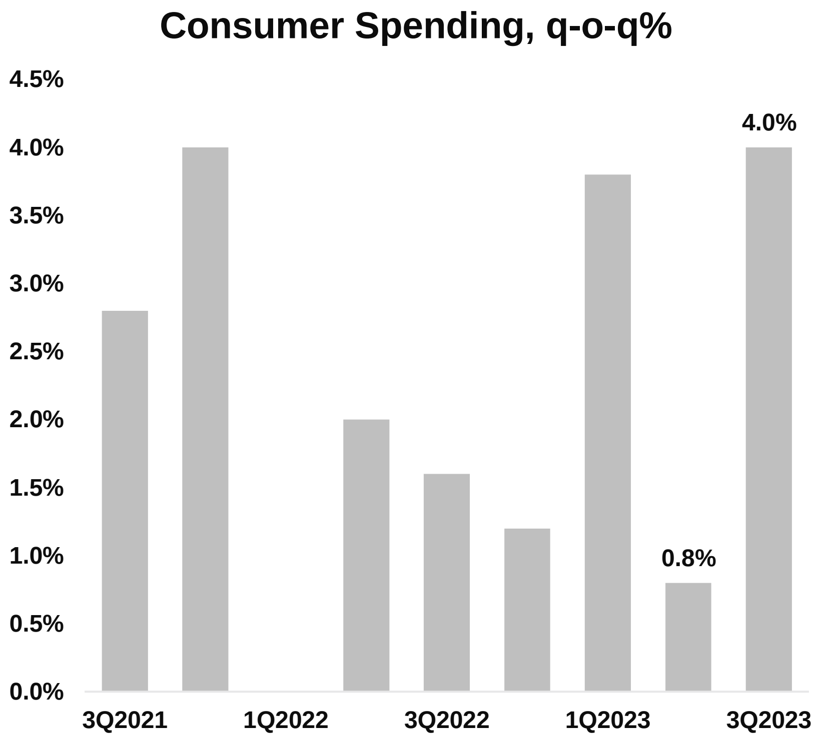

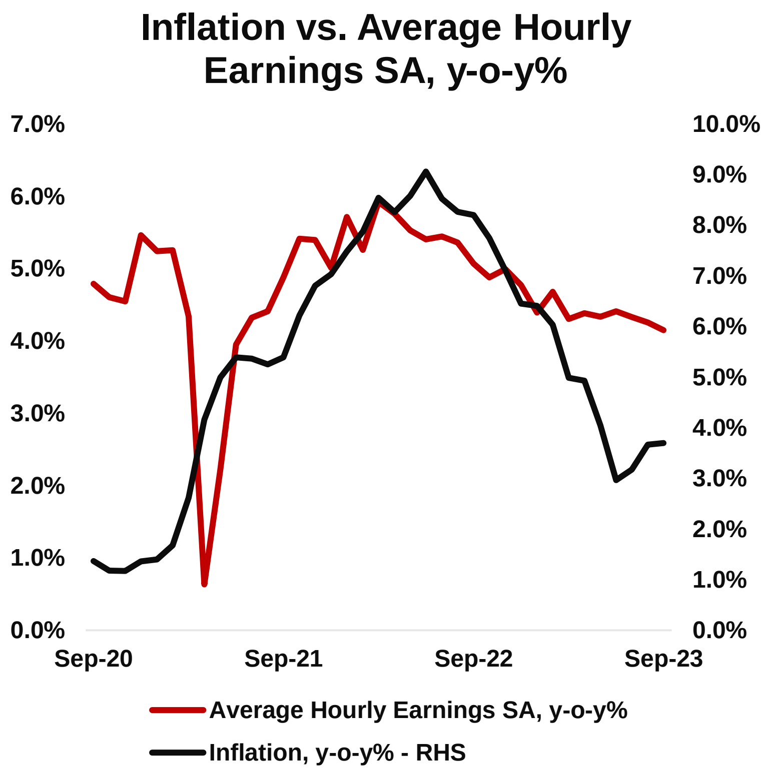

Sources: U. S. Bureau of Economic Analysis (BEA), U.S. Bureau of Labor Statistics

- The U.S. economy grew at 4.9% in 3Q2023 – marking its fastest rate in nearly two years, driven by a substantial increase in consumer spending. Such growth was well above the 2.1% in the previous quarter and faster than the market estimation of a 4.3% rate.
- Robust consumer spending, which accounts for more than two-thirds of the country's economy, was the catalyst for growth, highlighting the economy's surprising ability to withstand elevated borrowing costs and persistent inflation. It accelerated at a 4.0% rate after only rising at 0.8% in 2Q2023, thanks to record-breaking amounts on concert tours, including Taylor Swift's Eras Tour and Beyonce's Renaissance's Tour, as well as the blockbuster movies Barbie.
- While wage growth has decelerated, it is outpacing inflation slightly, which is bolstering households' buying power.

CHINA'S FACTORY OUTPUT DECLINED IN OCTOBER, REINFORCED THE CASE FOR A GREATER FISCAL POLICY SUPPORT FROM THE STATE

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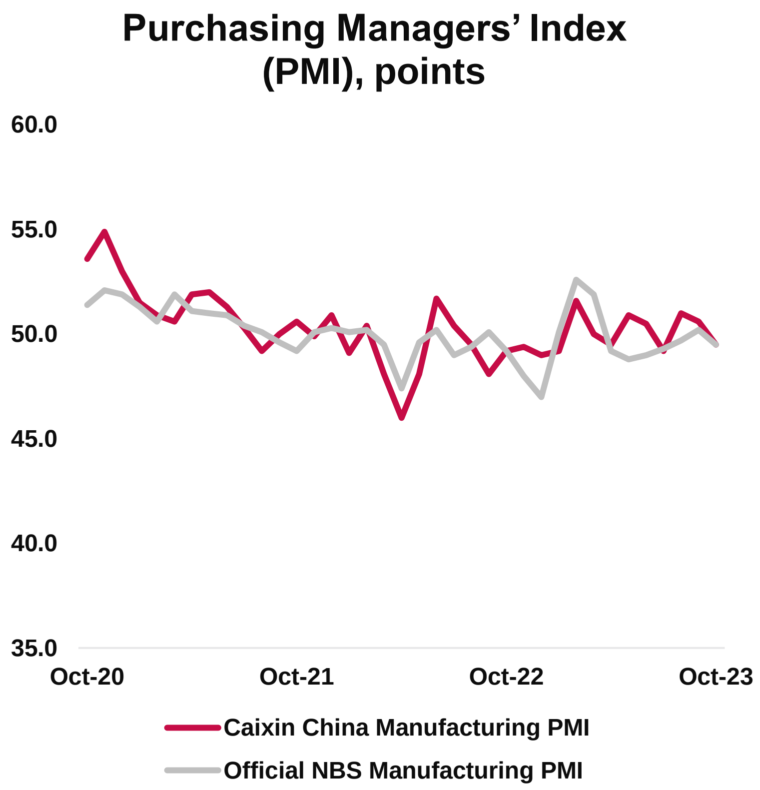

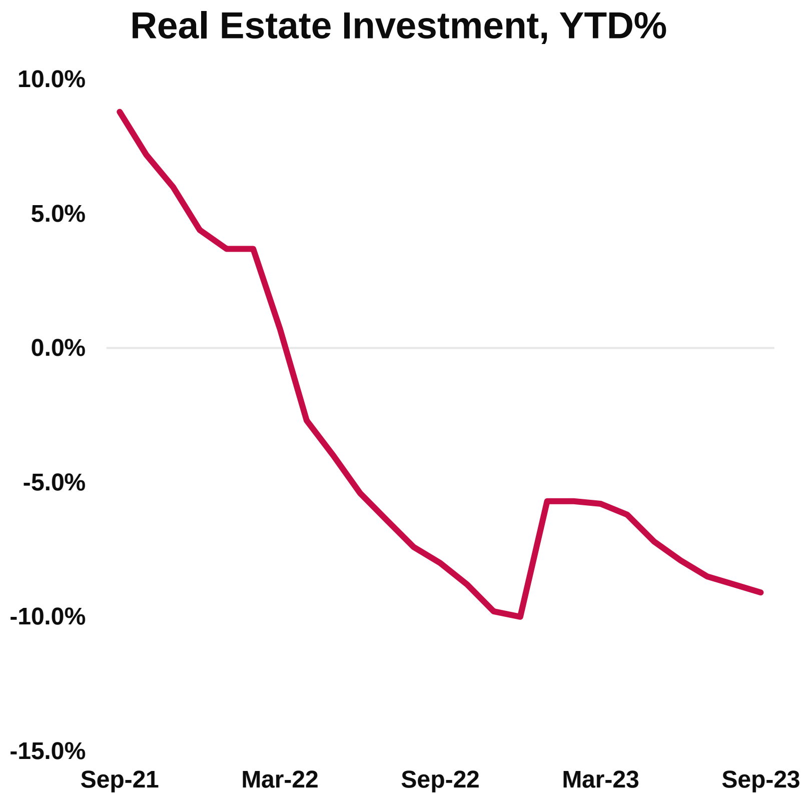

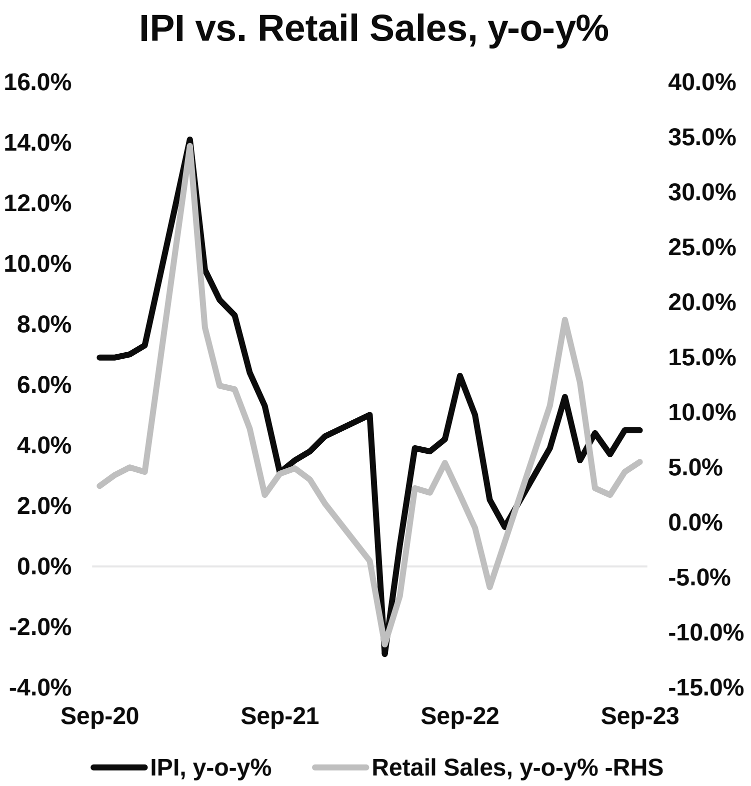

Sources: S&P Global, National Bureau of Statistics (NBS)

- A private survey showed that China's factory activity unexpectedly contracted in October, adding to a downbeat official manufacturing PMI, suggesting that the manufacturing sector was still not on solid footing despite the country's better-than-expected 3Q2023 growth.
- Additionally, the recovery in the property market was still weakening despite the country's measures to reverse the prolonged real-estate downturn. Property investment saw a drop of 9.1% for the first nine months of the year, from an 8.8% decline in the January to August period.
- While such indicators could raise questions over the country's fragile economic recovery at the beginning of the 4Q2023, the economic growth is still going due to the latest positive data from both IPI and Retail Sales – indicating that the world's second-largest economy is likely on track to achieve its annual growth target of around 5.0% this year.

GROWTH OUTLOOK FOR EUROZONE REMAINS BLEAK DESPITE A POSSIBLE END TO ECB'S POLICY TIGHTENING CYCLE

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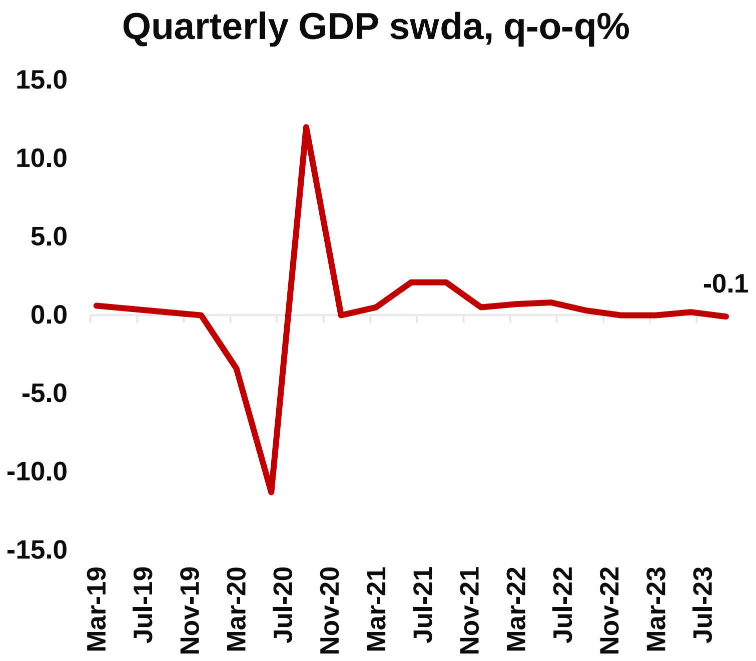

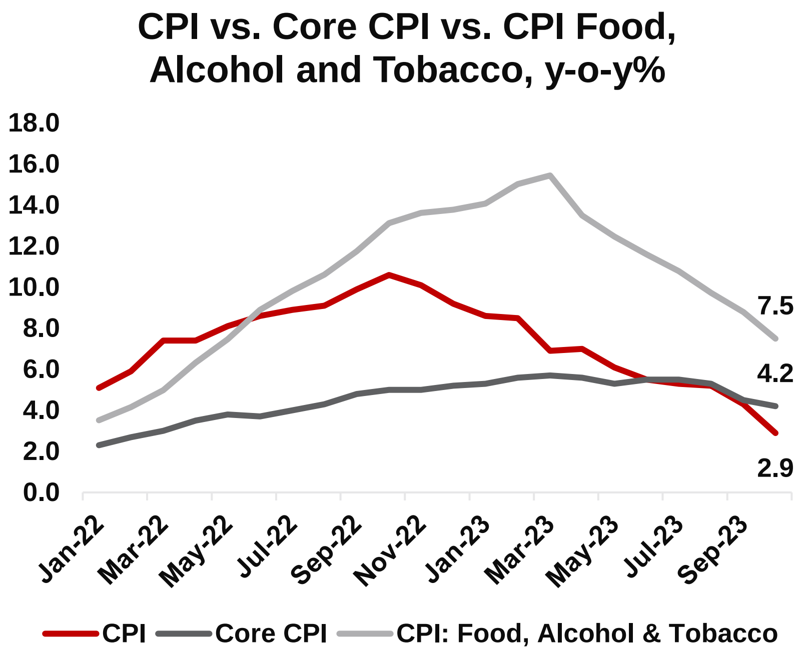

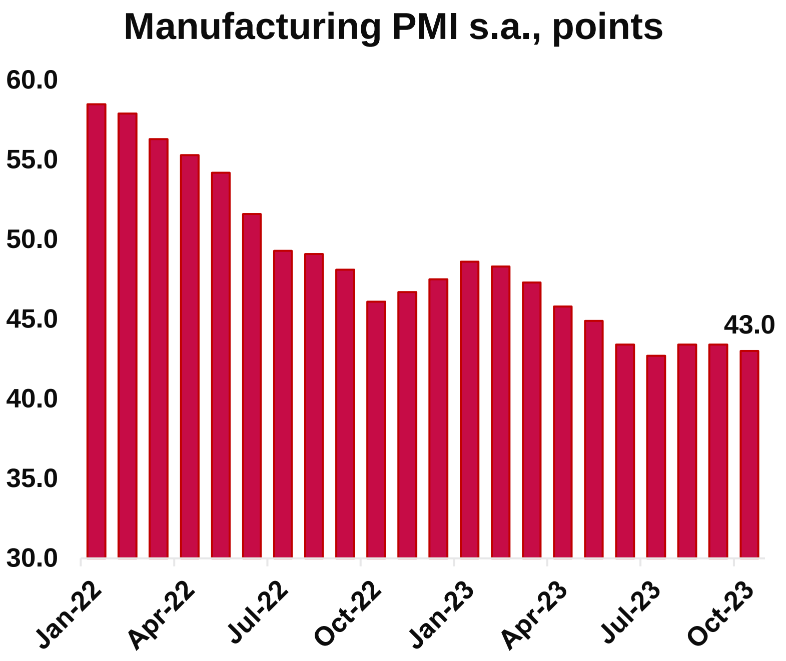

Sources: Eurostat, European Central Bank (ECB), S&P Global

- Early estimates released by Eurostat show that on a quarterly basis, the economy shrank by 0.1% in 3Q2023 (2Q2023: 0.2%). The area's top economy, Germany, also declined 0.1%, while France recorded a sluggish growth of 0.1% from the previous quarter.
- Europe's inflation fell to 2.9% in October (September: 4.3%) to record the lowest reading in more than two years, following moderating energy prices. The downtrend in inflation was also attributable to tighter financial conditions following the ECB's aggressive policy path.
- However, underlying price pressures persist amid still high food inflation (October: 7.5% vs. September: 8.8%) and the ongoing Gaza conflict, which would push oil prices to trend higher.
- Manufacturing activities slowed further to 43.0 points in October (September: 43.4 points), signaling dampening demand as the economy heads into 4Q2023. Coupled with the early estimates of contraction in 3Q2023, the outlook for this year remains cloudy.

INDONESIA VIEWS A “LIMITED LIKELIHOOD”OF AN OFF-CYCLE RATE INCREASE

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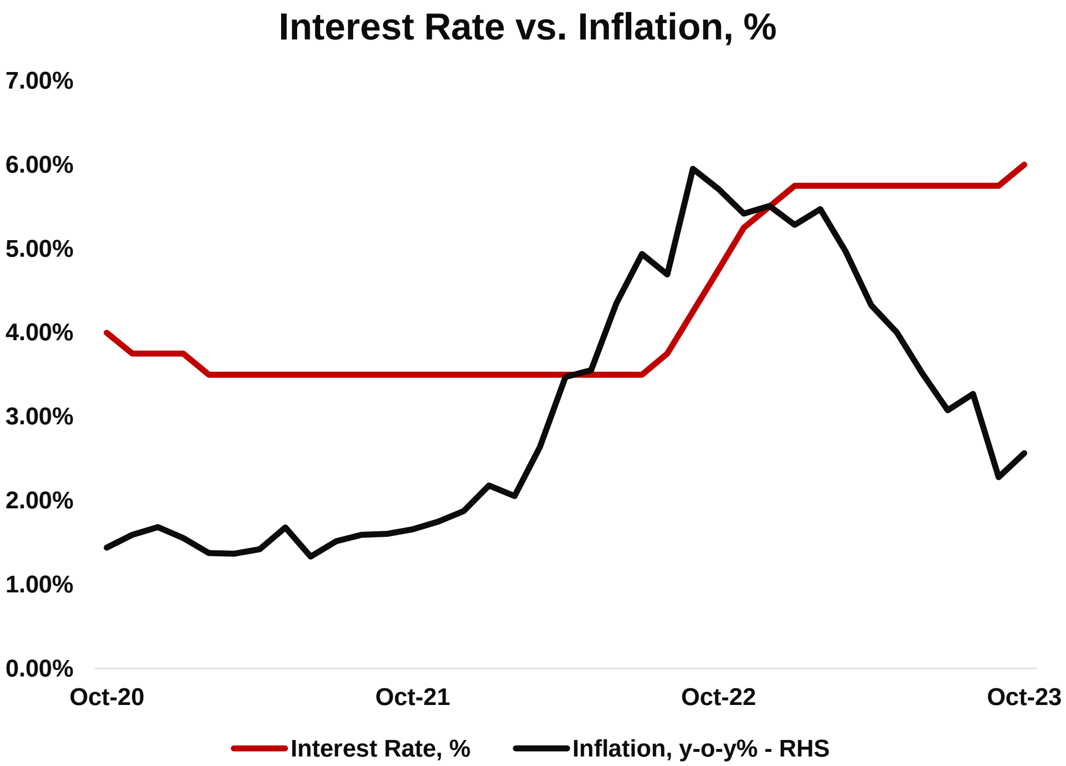

Sources: Bank Indonesia, Statistics Indonesia

- YTD, the Indonesian Rupiah (IDR) slumped to around 1.3% against the USD to reach its weakest level since April 2020. Following its October meeting, the central bank unexpectedly increased its interest rate by 25bps to 6.00%, marking the first rate hike since January as it seeks to reinforce efforts to stabilize the IDR. This is due to the rising global uncertainty despite the inflation reading maintained within the central bank’s target of between 2.0%-4.0%.
- There is growing pressure for the regional central banks to take bolder steps to support their respective currencies as the USD strengthens and UST yields rise. Neigbouring Bangko Sentral ng Pilipinas (BSP) also raised its key rate to 6.50% in a surprise off-cycle meeting last month to address rising prices. In September, the country’s inflation accelerated to 6.1% – the highest reading since May, driven by upward pressure from the food prices.
- Aside from grappling with a falling IDR, investors are turning cautious ahead of the February 14 election next year.

SECTION 3

Domestic Landscape & Banking Sector Update

MANUFACTURING SECTOR TO REMAIN SLUGGISH AS TRADE POSTS MAJOR CONCERN TO GROWTH

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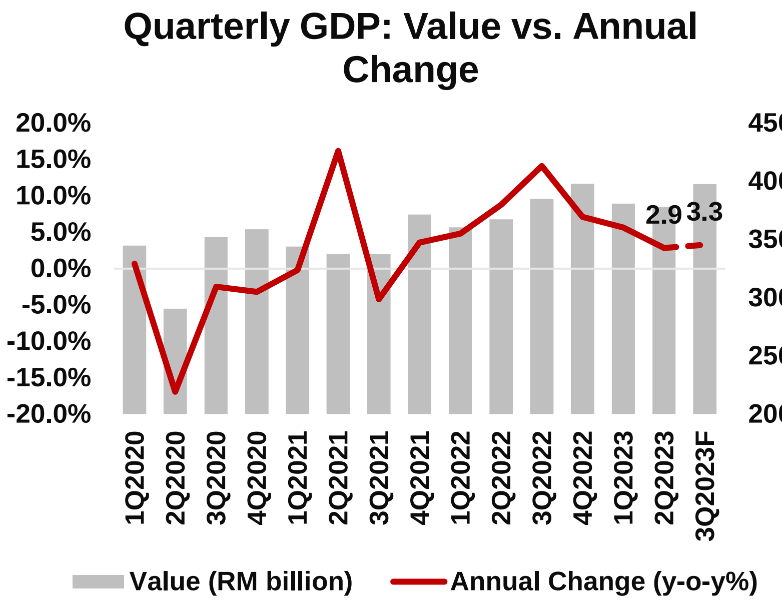
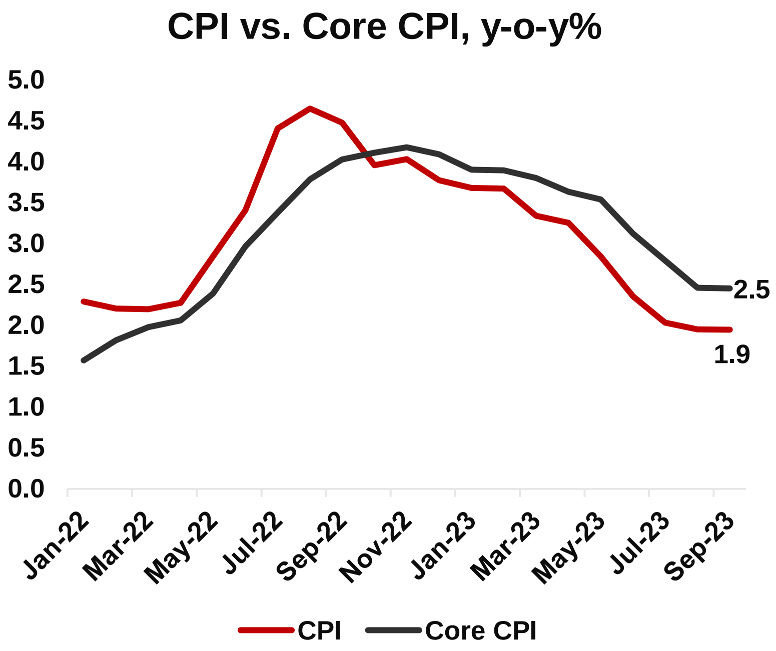
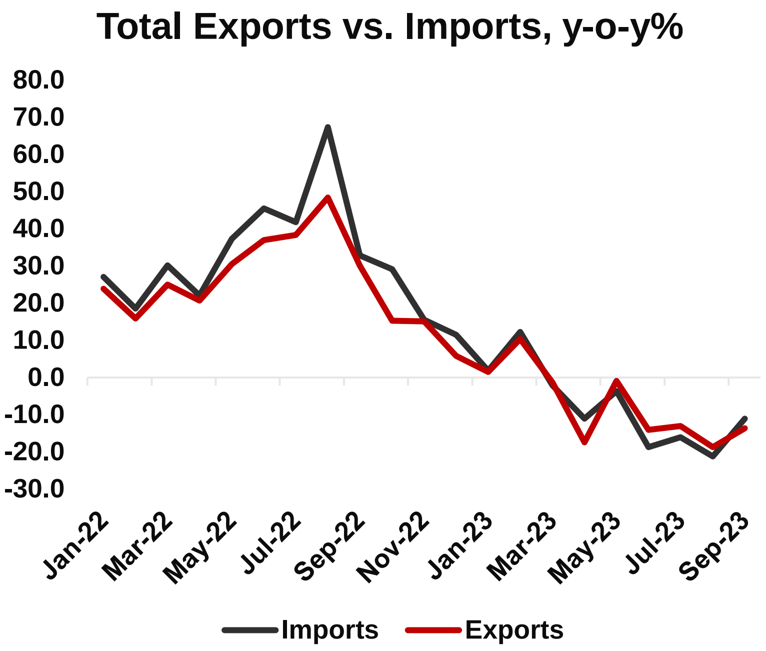


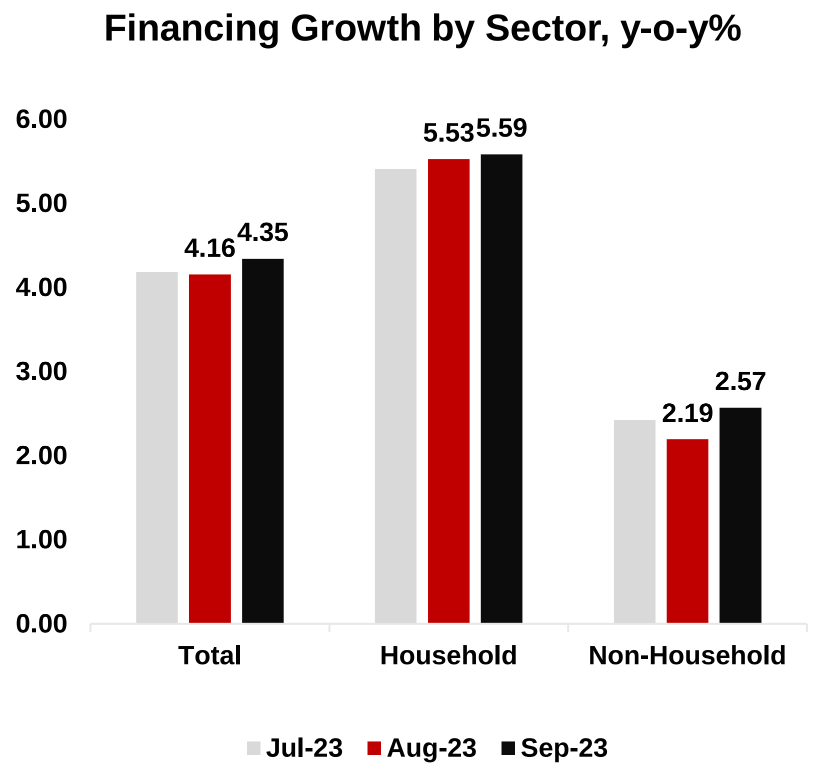


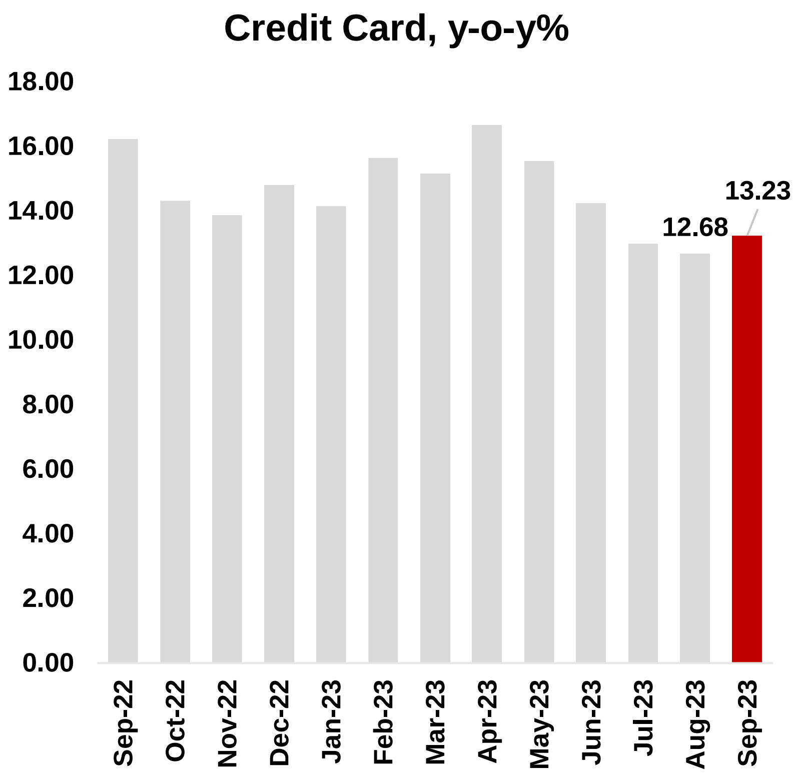


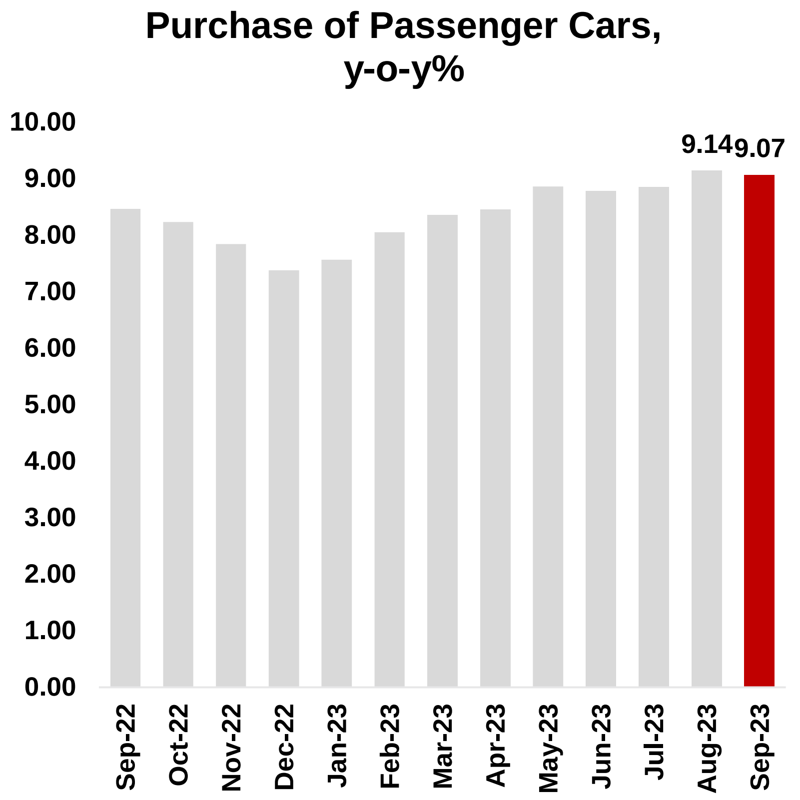
Sources: DOSM, BNM

- Advance estimates show that the economy is projected to grow by 3.3% in 3Q2023 (2Q2023: 2.9%), supported by expansion in the services, agriculture and construction sectors. Meanwhile, both mining and manufacturing sectors are expected to record slight contractions of 0.1%.
- Headline inflation eased to 1.9% in September (August: 2.0%), marking the lowest reading since August 2021. The moderation was attributed to disinflation in both Food and Non-Alcoholic Beverages (FNAB) and Restaurants and Hotels (RH) at 3.9% and 4.4%, respectively.
- Yet, core inflation remained sticky, steadying at 2.5% in September from August.
- Exports trended in the negative territory for seven consecutive months following subdued external demand, recording a contraction of 13.7% in September (August: -18.7%). Similarly, imports also declined for the same period (September: 11.1% vs. August: 21.2%). We note that, despite the downbeat trade performance this year, there is little initiative to boost trade under Budget 2024.
- Echoing market consensus, BNM maintained the Overnight Policy Rate (OPR) at 3.00% in its final meeting of the year. Nonetheless, the OPR outlook might change depending on the incoming data, which could drive the inflation trajectory next year in view of domestic policies announced in Budget 2024. For now, we foresee the OPR would stick around at 3.00% for some time.

BANKING SECTOR: FINANCING ACTIVITIES GREW IN SEPTEMBER, BUOYED BY BOTH HOUSEHOLD AND NON-HOUSEHOLD SECTORS



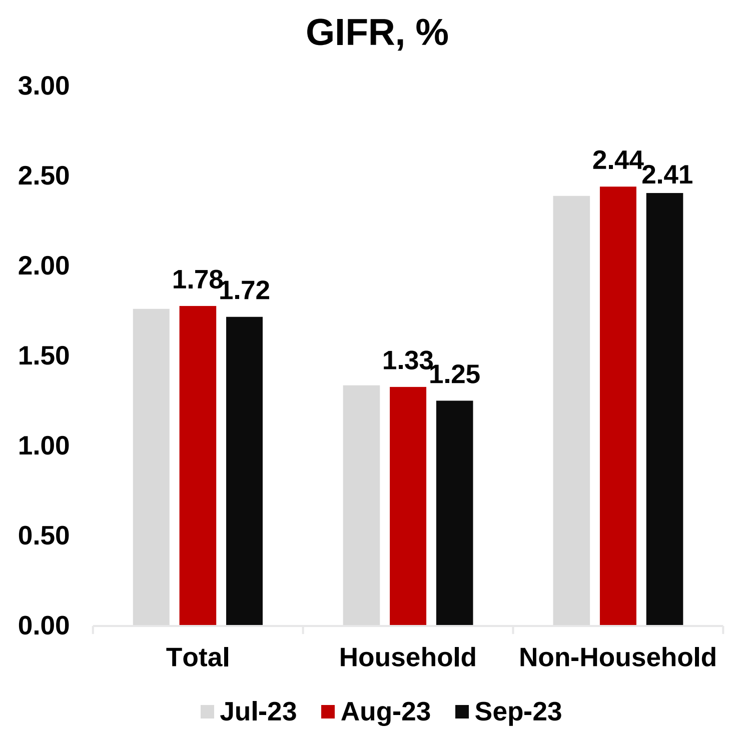


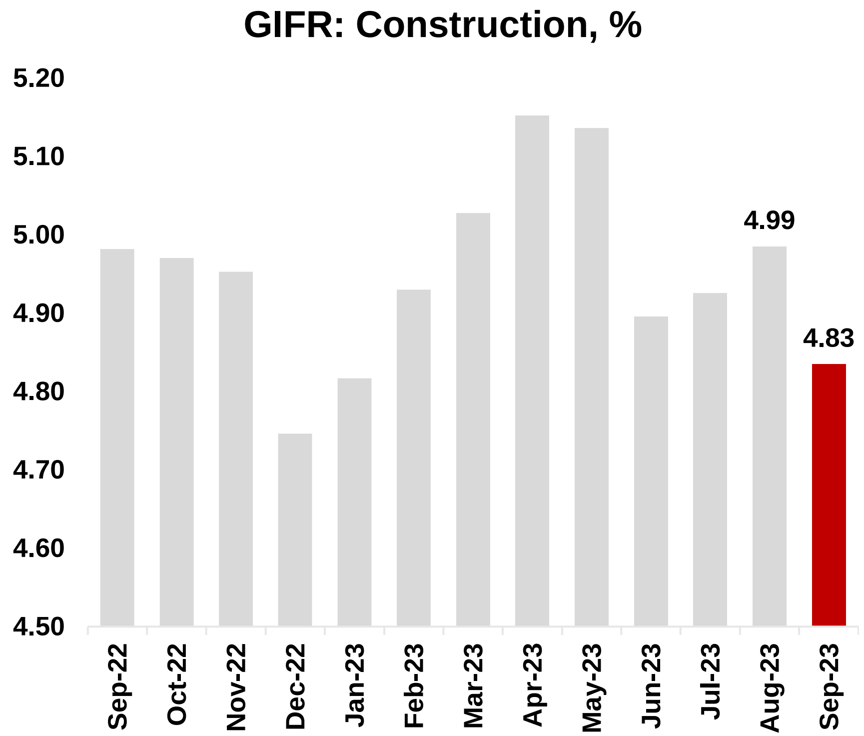


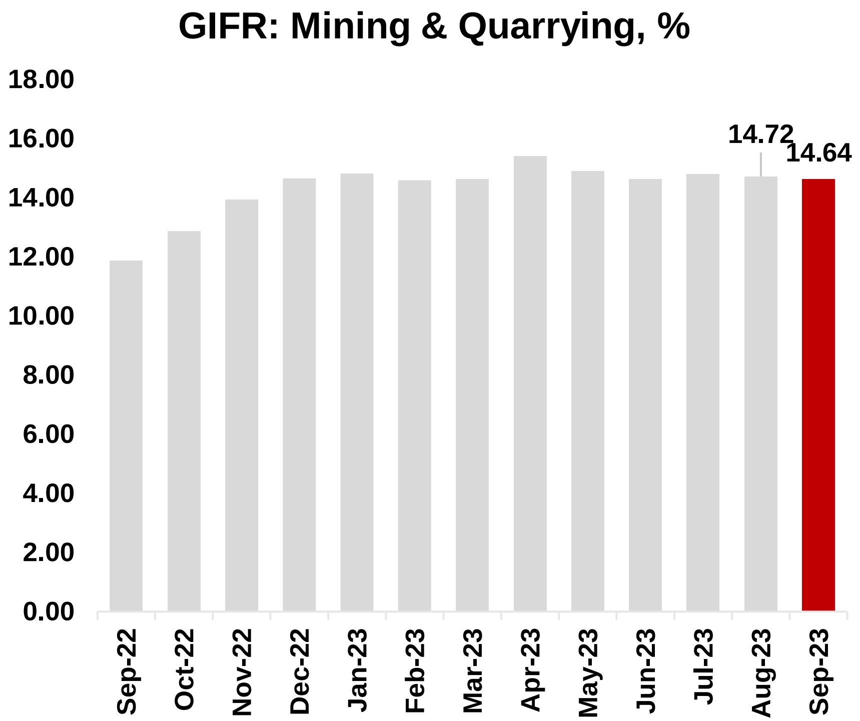
Source: BNM

- The financing activities rose in September at 4.35% relative to 4.18% recorded in August. The household sector maintained the upward momentum, rising to 5.59% in September from 5.53% in the previous month. In addition, the non-household segment's financing growth accelerated to 2.57% in September (August: 2.19%).
- In September, the financing growth within the credit card segment expanded to 13.23% from 12.68% in August. Additionally, the credit growth in the purchase of residential property segment expanded by 7.18% in September (August: 7.11%).
- In contrast, financing activities in the purchase of passenger cars segment grew at a slower pace of 9.07% in September (August: 9.14%).

BANKING SECTOR: ASSET QUALITY EDGED HIGHER IN SEPTEMBER







Source: BNM

- Total gross impaired financing ratio (GIFR) in the banking sector remained resilient at 1.72% in September (August: 1.78%). The impairment within the non-household sector slowed down to 2.41% in September (August: 2.44%). Meanwhile, GIFR in the household segment reduced slightly to 1.25% in September (August: 1.33%).
- The impairment within the construction segment decreased to 4.83% in September from 4.99% in August. On the other hand, the asset quality in the Mining and Quarrying industry improved marginally to 14.64% in September (August: 14.72%).

THANK YOU