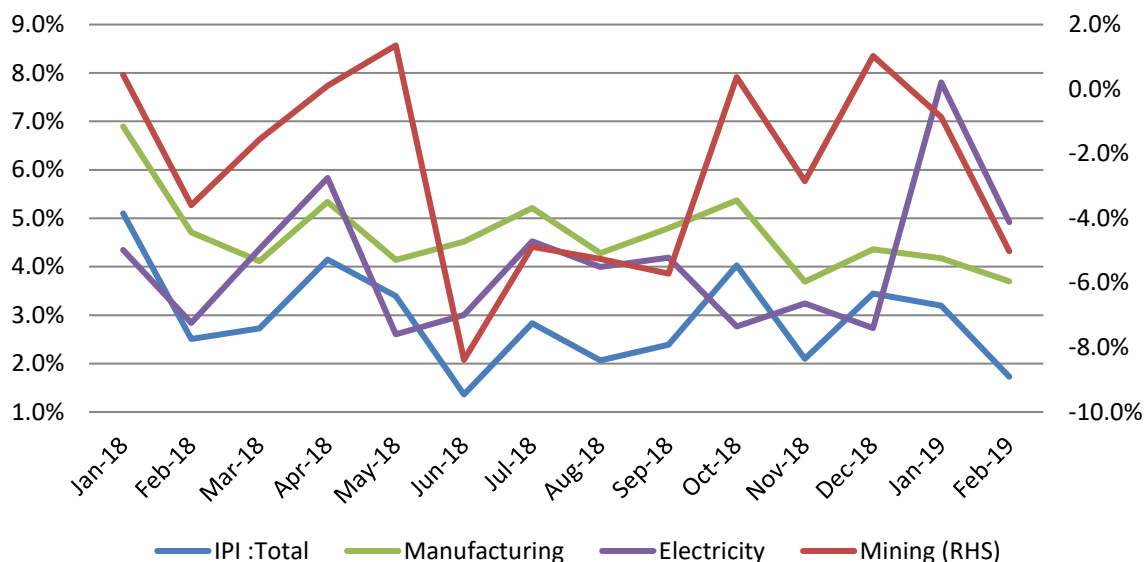


## IPI in February – shifting into lower gear

### Facts

- Malaysian Industrial Production Index (IPI) softened by 1.7% year-on-year (y-o-y) in February as compared to 3.2% growth in the preceding month (Consensus: 1.7%, Bank Islam: 2.3%). This was attributed by the contraction in the Mining sector, which slumped to 5.0% in February (Jan: -0.9%). The deterioration in the production of Crude Petroleum (Feb: -4.3% vs. Jan: -2.2%) and Natural Gas (Feb: -5.6% vs. Jan: 0.3%) were the main drivers for the decline in mining sector. The Manufacturing sector also weakened, recording 3.7% growth in February (Jan: 4.2%) and similarly, the Electricity index grew by 4.9% from 7.8% in the previous month.
- The modest print in the Manufacturing sector was led by Petroleum, Chemical, Rubber & Plastic Products which grew marginally by 1.6% in February, slower than 4.0% previously. This was followed by Electrical & Electronic (E&E) Products (Feb: 3.1% vs. Jan: 3.9%), Wood Products, Furniture, Paper Products & Printing (Feb: 5.5% vs. Jan: 5.7%) as well as Textiles, Wearing Apparel, Leather Products & Footwear (Feb: 3.6% vs. Jan: 5.4%).
- With regards to E&E Products sub-indexes, the Computer, Electronics & Optical (CE) and Electrical Equipment (EL) moderated by 2.8% (Jan: 3.5%) and 5.1% (Jan: 7.1%) in February. Both CE and EL accounted for 16.09% of E&E shares.
- Nevertheless, Non-Metallic Mineral, Basic Metal & Fabricated Metal Product (Feb: 4.6% vs. Jan: 4.3%), Food, Beverages & Tobacco (Feb: 6.3% vs. Jan: 2.6%) and Transport Equipments & Other Manufacturers (Feb: 7.1% vs. Jan: 6.3%) advanced in February has cushioned the slowdown in the overall IPI performance.
- Cumulatively, IPI grew by an average of 2.5% in the first two months of 2019. This is lower compared to 3.9% growth in 2M2018, suggesting the production momentum is shifting into lower gear now.

Chart 1: Industrial Production Index y-o-y%



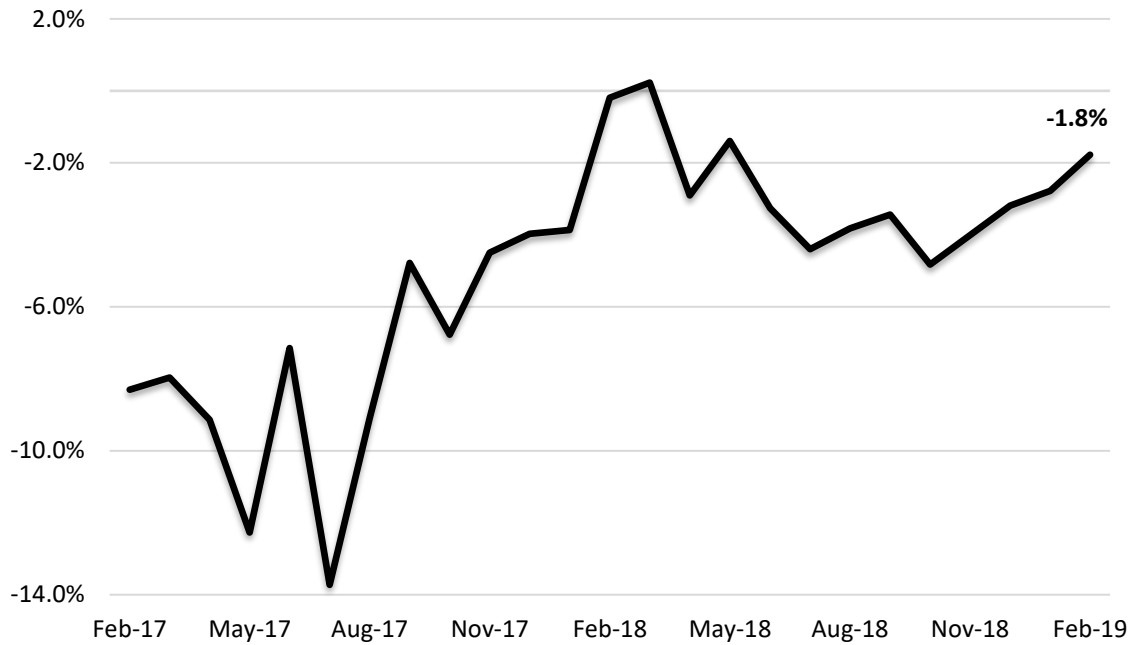
Source: CEIC

Table 1: Industrial Production Index (IPI) y-o-y%

	Weight	Nov-18	Dec-18	Jan-19	Feb-19	2M2018	2M2019
<b>IPI</b>	<b>100.0%</b>	<b>2.1%</b>	<b>3.4%</b>	<b>3.2%</b>	<b>1.7%</b>	<b>3.9%</b>	<b>2.5%</b>
<b>Mining</b>	<b>25.1%</b>	<b>-2.8%</b>	<b>1.0%</b>	<b>-0.9%</b>	<b>-5.0%</b>	<b>-1.5%</b>	<b>-2.8%</b>
Crude Petroleum	12.2%	-4.9%	2.5%	-2.2%	-4.3%	-3.5%	-3.2%
Natural Gas	12.9%	-1.0%	-0.2%	0.3%	-5.6%	0.4%	-2.5%
<b>Manufacturing</b>	<b>68.3%</b>	<b>3.7%</b>	<b>4.4%</b>	<b>4.2%</b>	<b>3.7%</b>	<b>5.8%</b>	<b>3.9%</b>
Food, Beverages and Tobacco	8.6%	-1.7%	-1.1%	2.6%	6.3%	9.2%	4.3%
Textiles, Wearing Apparel, Leather Products and Footwear	1.3%	4.8%	4.2%	5.4%	3.6%	8.3%	4.5%
Wood Products, Furniture, Paper Products, Printing	4.6%	2.8%	5.0%	5.7%	5.5%	4.0%	5.6%
Petroleum, Chemical, Rubber and Plastic Products	20.6%	3.4%	3.6%	4.0%	1.6%	6.6%	2.8%
Non-Metallic Mineral Products, Basic Mineral and Fabricated Metal P	9.1%	4.1%	4.1%	4.3%	4.6%	5.6%	4.4%
Electrical and Electronics Products	18.2%	5.3%	7.2%	3.9%	3.1%	5.6%	3.5%
Transport Equipment and Other Manufactures	5.9%	8.3%	7.0%	6.3%	7.1%	0.8%	6.7%
<b>Electricity</b>	<b>6.6%</b>	<b>3.2%</b>	<b>2.7%</b>	<b>7.8%</b>	<b>4.9%</b>	<b>3.6%</b>	<b>6.4%</b>

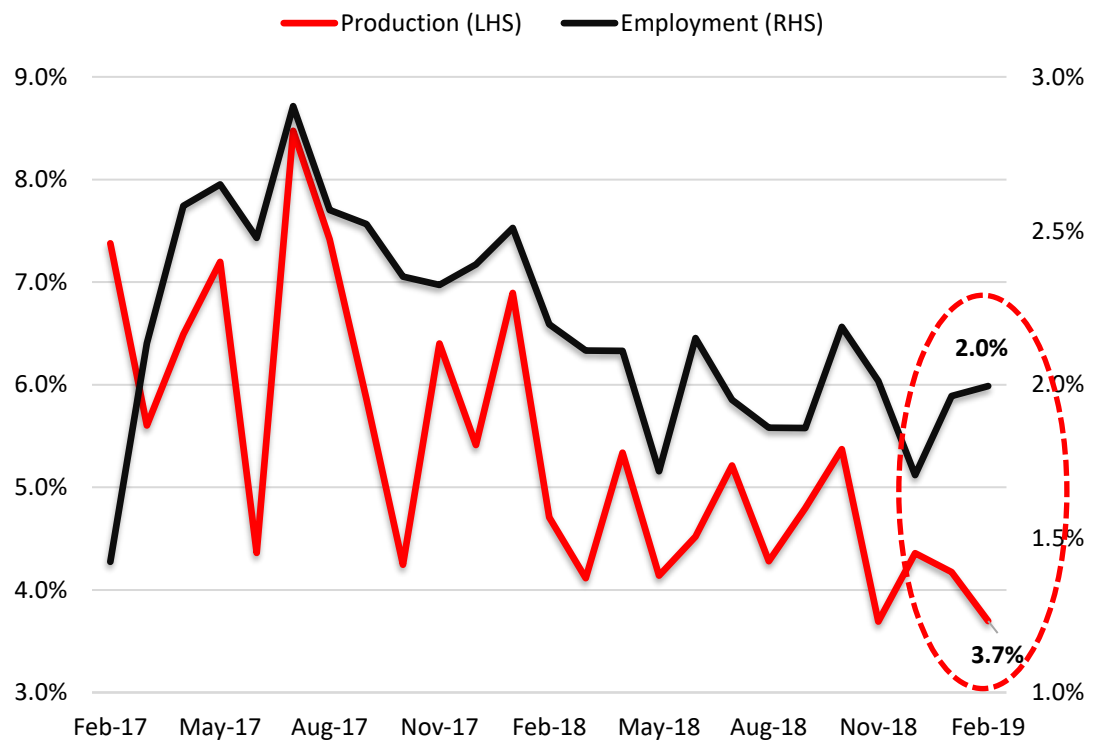
Source: CEIC

**Chart 2: Estimates of Inventory level in manufacturing (production less sales)**



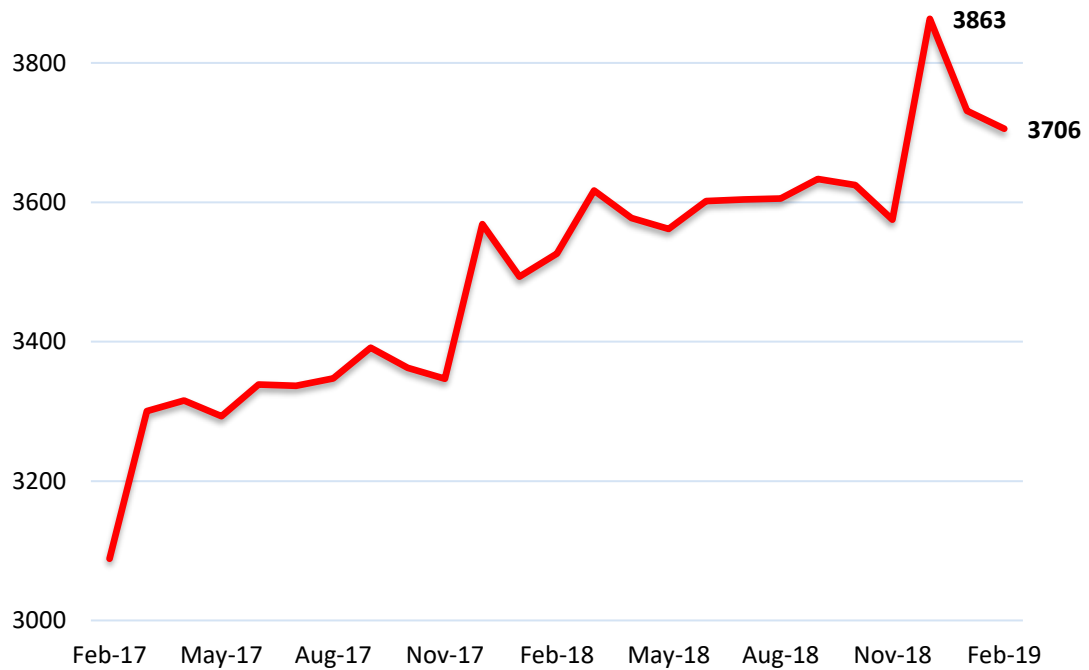
Source: CEIC

**Chart 3: Total production and employment growth in manufacturing sector y-o-y%**



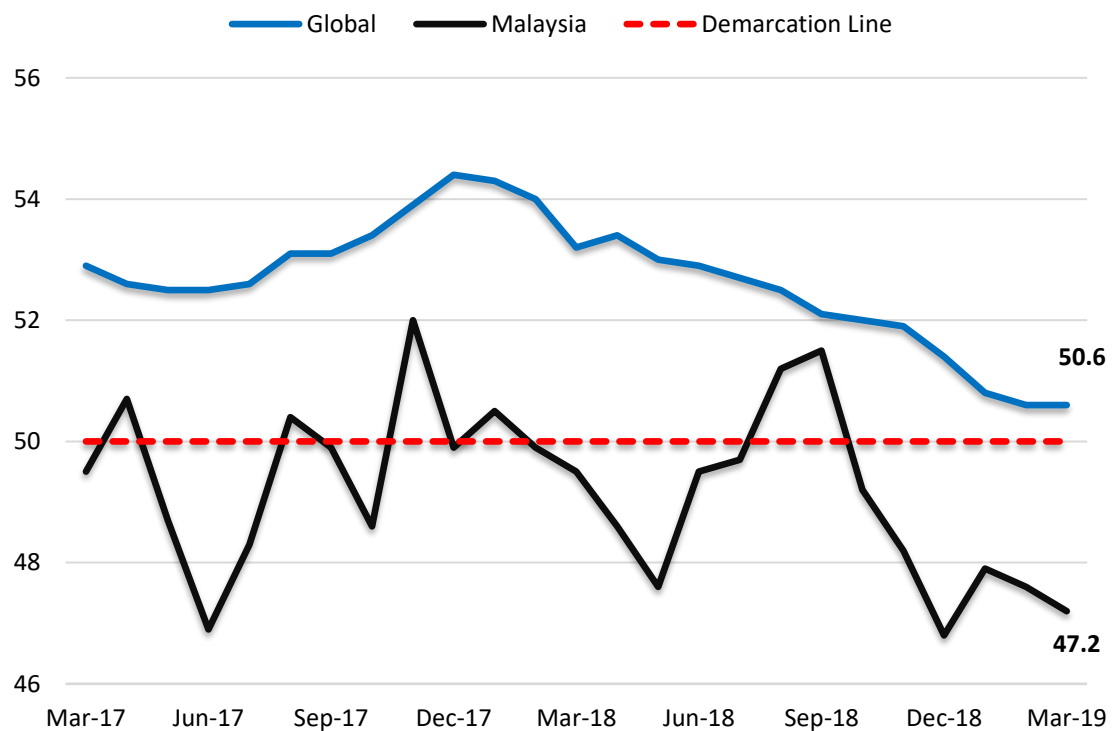
Source: CEIC

Chart 4: Average monthly salaries in the manufacturing sector (RM)



Source: DOS Malaysia, CEIC

Chart 5: PMI for Manufacturing (points)



Source: Bloomberg

## Our view

Industrial production pace is moderating. Such connotation was very much in line with the J.P. Morgan Global Purchasing Manager's Index (PMI) which sustained at 50.6 points for two consecutive months in March, approaching the demarcation line between contractionary and expansionary zone (See chart 5). Additionally, the recent fall in Malaysia's Manufacturing PMI to 47.2 points in March from 47.6 points in February have demonstrated a cautious view among the manufacturers. Malaysia's employment growth in the manufacturing industry has also maintained at 2.0% y-o-y for two consecutive months in February. Meanwhile, the average monthly salaries earned by the manufacturing workers dropped from RM3,731 in January to RM3,706 in February. These two factors have reinvigorated our view that manufacturers are scaling down their production lines. According to the PMI survey, Malaysian manufacturers would face a challenging business environment as output and new orders would drop further. This is especially true when demand condition is likely to be lethargic as households are expected to tighten their purse string.

Apart from that, the downward global growth forecast revision by the International Monetary Fund (IMF) recently has bolstered our conviction that 2019 growth will be a very challenging year. The world economy is expected to grow at a rate of 3.3% this year, lower from the previous estimates of 3.5% which was made in January 2019. Similarly, the global trade volume in goods and services is anticipated to increase by 3.4% in 2019. Again, this represents a downward revision from the previous estimates of 4.0%. The IMF is cautioning that the risks are skewed to the downside, citing protectionists' policies enacted by the US as the key factor. This is alongside with downside surprise in China's growth as well as the heightening risks surrounding Brexit negotiation.

The departure of Britain from the European Union (EU) without a mutual agreement which could result a "no-deal" Brexit scenario has obviously sent the negative vibes across the globe. Currently, the European Union (EU) Council and President May have agreed to extend the UK withdrawals dateline from 12 April to 22 October this year. With the additional 6 months timeline, the no-deal Brexit has been avoided, at least for now. Nonetheless, the so-called "Brextension" could potentially increase the risk of destabilising the UK government as both political parties would have to work the Brexit proposal that will satisfy their electorates.

As such, the odds for lower Overnight Policy Rate (OPR) has increase in the upcoming Monetary Policy Committee (MPC) meeting scheduled on 7 May 2019. As such, **we are penciling in 25 basis points OPR reduction which will bring the policy rate to 3.00%.**

**Table 2: Overview of the World Economic Outlook Projections**

	2018	Projections		Difference from January 2019 WEO Update <sup>1</sup>		Difference from October 2018 WEO <sup>1</sup>	
		2019	2020	2019	2020	2019	2020
<b>World Output</b>	<b>3.6</b>	<b>3.3</b>	<b>3.6</b>	<b>-0.2</b>	<b>0.0</b>	<b>-0.4</b>	<b>-0.1</b>
<b>Advanced Economies</b>	<b>2.2</b>	<b>1.8</b>	<b>1.7</b>	<b>-0.2</b>	<b>0.0</b>	<b>-0.3</b>	<b>0.0</b>
United States	2.9	2.3	1.9	-0.2	0.1	-0.2	0.1
Euro Area	1.8	1.3	1.5	-0.3	-0.2	-0.6	-0.2
Germany	1.5	0.8	1.4	-0.5	-0.2	-1.1	-0.2
France	1.5	1.3	1.4	-0.2	-0.2	-0.3	-0.2
Italy	0.9	0.1	0.9	-0.5	0.0	-0.9	0.0
Spain	2.5	2.1	1.9	-0.1	0.0	-0.1	0.0
Japan	0.8	1.0	0.5	-0.1	0.0	0.1	0.2
United Kingdom	1.4	1.2	1.4	-0.3	-0.2	-0.3	-0.1
Canada	1.8	1.5	1.9	-0.4	0.0	-0.5	0.1
Other Advanced Economies <sup>2</sup>	2.6	2.2	2.5	-0.3	0.0	-0.3	0.0
<b>Emerging Market and Developing Economies</b>	<b>4.5</b>	<b>4.4</b>	<b>4.8</b>	<b>-0.1</b>	<b>-0.1</b>	<b>-0.3</b>	<b>-0.1</b>
Commonwealth of Independent States	2.8	2.2	2.3	0.0	0.0	-0.2	-0.1
Russia	2.3	1.6	1.7	0.0	0.0	-0.2	-0.1
Excluding Russia	3.9	3.5	3.7	-0.2	0.0	-0.1	0.0
Emerging and Developing Asia	6.4	6.3	6.3	0.0	-0.1	0.0	-0.1
China	6.6	6.3	6.1	0.1	-0.1	0.1	-0.1
India <sup>3</sup>	7.1	7.3	7.5	-0.2	-0.2	-0.1	-0.2
ASEAN-5 <sup>4</sup>	5.2	5.1	5.2	0.0	0.0	-0.1	0.0
Emerging and Developing Europe	3.6	0.8	2.8	0.1	0.4	-1.2	0.0
Latin America and the Caribbean	1.0	1.4	2.4	-0.6	-0.1	-0.8	-0.3
Brazil	1.1	2.1	2.5	-0.4	0.3	-0.3	0.2
Mexico	2.0	1.6	1.9	-0.5	-0.3	-0.9	-0.8
Middle East, North Africa, Afghanistan, and Pakistan	1.8	1.5	3.2	-0.9	0.2	-1.2	0.2
Saudi Arabia	2.2	1.8	2.1	0.0	0.0	-0.6	0.2
Sub-Saharan Africa	3.0	3.5	3.7	0.0	0.1	-0.3	-0.2
Nigeria	1.9	2.1	2.5	0.1	0.3	-0.2	0.0
South Africa	0.8	1.2	1.5	-0.2	-0.2	-0.2	-0.2
<i>Memorandum</i>							
European Union	2.1	1.6	1.7	-0.3	-0.1	-0.4	-0.1
Low-Income Developing Countries	4.6	5.0	5.1	-0.1	0.0	-0.2	-0.2
Middle East and North Africa	1.4	1.3	3.2	-0.9	0.3	-1.2	0.3
World Growth Based on Market Exchange Rates	3.1	2.7	2.9	-0.3	0.0	-0.4	0.0

Source: World Economic Outlook Report, IMF

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