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Malaysia's 1Q2019 GDP at 4.5%

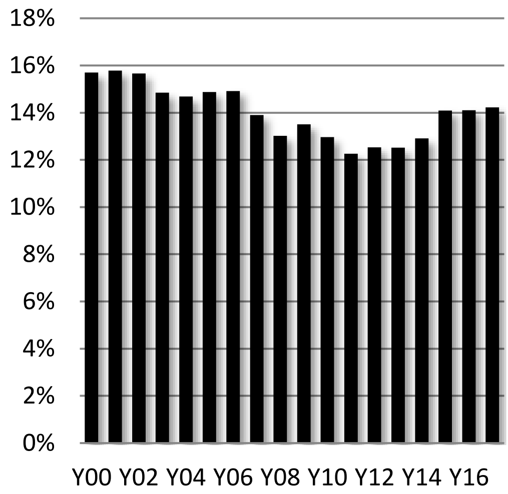
Our take on the 1Q2019 GDP – growth is slowing

The 1Q2019 Gross Domestic Product (GDP) growth came in at 4.5% year-on-year (y-o-y). While this is better than median estimates of 4.3% (Bank Islam: 4.3%), the result was still lower than 4.7% growth in the preceding quarter. As expected, weak business sentiments as indicated by the recent fall in Business Condition Index (BCI) may have contributed to lethargic growth in private investment. At the same time, public sector spending has been very weak especially public investment as government remains guarded on their spending plans amidst near-completion of some of the big projects (RAPID Pengerang). Real exports growth was also weak in tandem with the prevailing global economic condition following the uncertainty in the trade tensions and volatile commodity prices.

Nonetheless, net exports has contributed 0.9 percentage points to the overall growth. But this is on account of weak imports and therefore, there is nothing to shout about. As such, private consumption was the savior, growing 7.6% (trend level: 6.9%) albeit slower compared to 8.4% growth in the previous quarter. We could see that there is a dichotomy between the Consumer Sentiment Index (CSI) which has remain below 100 points for two quarters in a row and the actual spending among the consumers. As such, it remains to be seen whether the consumers will continue to be the key pillars for growth going forward especially in the context of rising cost of living and higher household indebtedness.

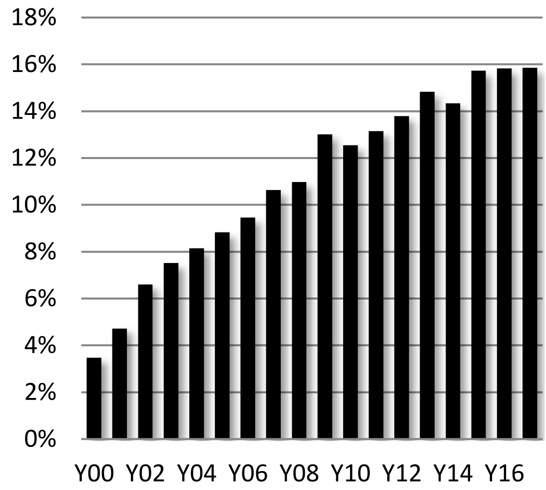
The prospects for the Malaysia's economic growth for the remainder of 2019 have been increasingly challenging. This is especially true when the ongoing trade tension between the US and China is likely to be disruptive to global trade if both countries are unable to find amicable solution immediately. Since China's accession to World Trade Organisation (WTO) in 2001, Asian economies have become integrated with China. For instance, Malaysia's total trade with China stood at 3.5% in 2000 and the share has grown to 16.7% in 2018. Other economies also demonstrated similar trajectory as the region's economy has become globalised. It remains to be seen how the trade friction could eventually pan out. The recent move to curb and blacklisting China's Huawei from selling their equipment in the US could only magnify the confrontation. Therefore, hope for a quick resolve to the conflict is utterly delusional.

Chart 1: China Total Trade with US (%)



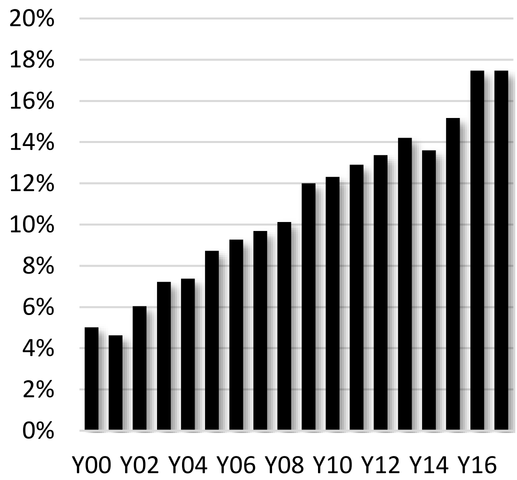
Source: ADB

Chart 2: Malaysia Total Trade with China (%)



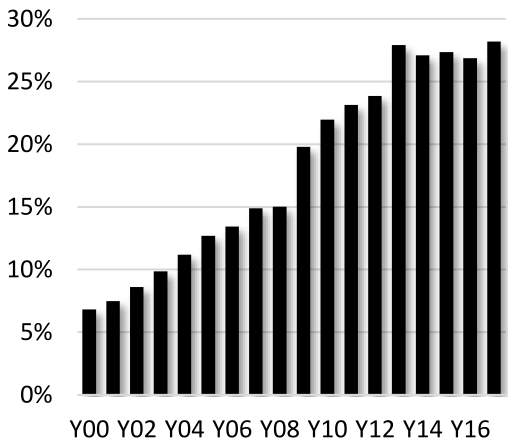
Source: ADB

Chart 3: Indonesia Total Trade with China (%)



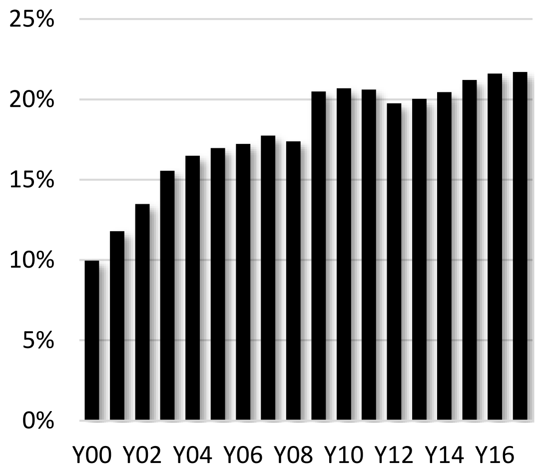
Source: ADB

Chart 4: Australia Total Trade with China (%)



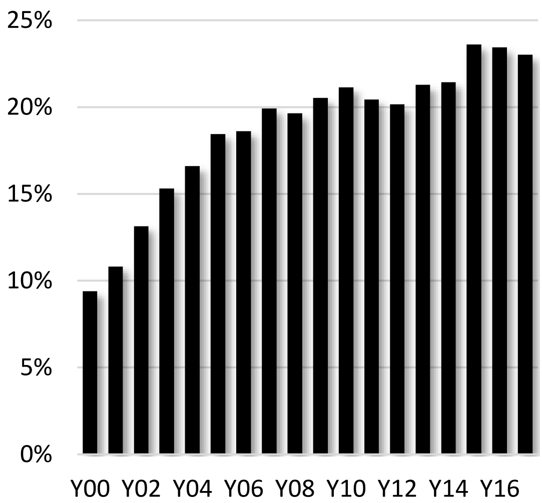
Source: ADB

Chart 5: Japan Total Trade With China (%)



Source: ADB

Chart 6: South Korea Total Trade With China (%)



Source: ADB

Apart from that, the technology sector appears to be scaling down which could have immediate impact to our Electrical and Electronic (E&E) exports. The Global Semiconductor Sales (GSS) growth has been declining for three consecutive months since January 2019. This is very much in line with the fall in Global Smartphones Shipments which has been in contraction for six consecutive quarters (see Table 1). In the past, GSS would decline between 7 to 16 months while the correlation between GSS and Malaysia's E&E exports stood at 77% (See Chart 13). We believe the rollout of 5G network would hold the key to the revival of the technology sector as data speed, lower latency and devices connectivity are the critical success factor for the fourth industrial revolution (IR 4.0). Thus far, the earliest 5G roll out could happen as early as 2020. Until then, expect technology sector to remain lackluster.

Table 1: Global Smartphones Sales

Million units	1Q 2017	2Q 2017	3Q 2017	4Q 2017	1Q 2018	2Q 2018	3Q 2018	4Q 2018	1Q 2019
Samsung	80.1	79.8	83.3	74.5	78.2	71.5	72.2	70.4	71.9
Apple	50.8	41.0	46.7	77.3	52.2	41.3	46.9	68.4	36.4
Huawei	34.5	38.5	39.1	42.1	39.3	54.2	52.0	60.5	59.1
Xiaomi	14.8	21.4	28.3	28.2	27.8	31.9	34.3	28.6	25.0
OPPO	25.8	28.0	30.6	27.3	24.6	29.4	29.9	29.2	23.1
Others	138.3	139.5	149.8	145.3	110.6	113.7	119.9	118.4	95.3
Total	**344.4**	**348.2**	**377.8**	**394.6**	**332.7**	**342.0**	**355.2**	**375.4**	**310.8**

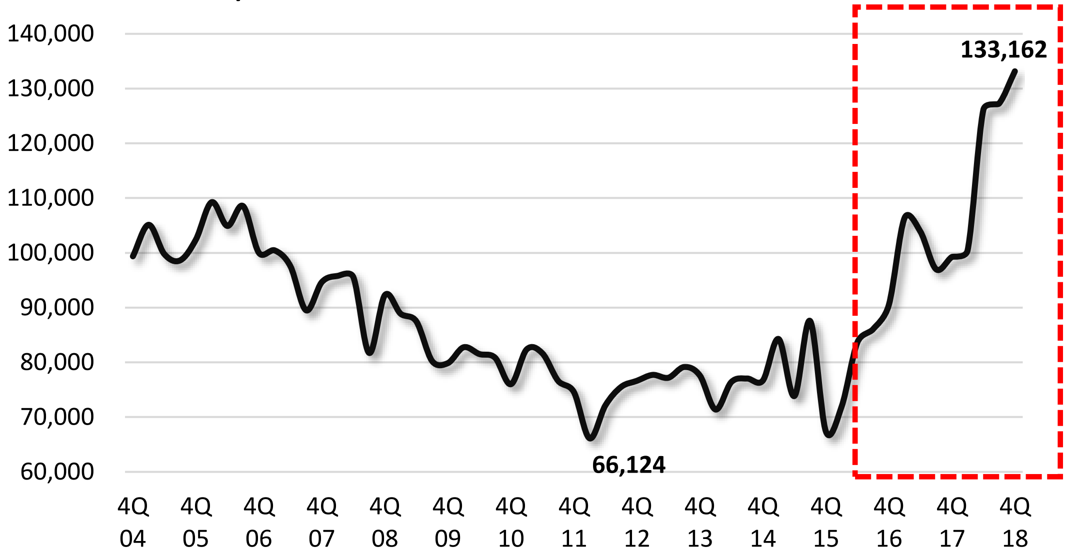
Market share	1Q 2017	2Q 2017	3Q 2017	4Q 2017	1Q 2018	2Q 2018	3Q 2018	4Q 2018	1Q 2019
Samsung	23.3%	22.9%	22.0%	18.9%	23.5%	20.9%	20.3%	18.8%	23.1%
Apple	14.8%	11.8%	12.4%	19.6%	15.7%	12.1%	13.2%	18.2%	11.7%
Huawei	10.0%	11.1%	10.3%	10.7%	11.8%	15.8%	14.6%	16.1%	19.0%
Xiaomi	4.3%	6.1%	7.5%	7.1%	8.4%	9.3%	9.7%	7.6%	8.0%
OPPO	7.5%	8.0%	8.1%	6.9%	7.4%	8.6%	8.4%	7.8%	7.4%
Others	40.2%	40.1%	39.7%	36.8%	33.2%	33.2%	33.8%	31.5%	30.7%
Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

Y-o-Y%	1Q 2017	2Q 2017	3Q 2017	4Q 2017	1Q 2018	2Q 2018	3Q 2018	4Q 2018	1Q 2019
Samsung	1.1%	1.5%	9.5%	-3.9%	-2.4%	-10.4%	-13.3%	-5.5%	-8.1%
Apple	-0.8%	1.5%	2.6%	-1.3%	2.8%	0.7%	0.4%	-11.5%	-30.2%
Huawei	22.8%	19.6%	16.0%	-7.3%	13.9%	40.8%	33.0%	43.7%	50.3%
Xiaomi	na	60.9%	108.1%	97.2%	87.8%	49.1%	21.2%	1.4%	-10.2%
OPPO	31.0%	23.3%	18.6%	-13.6%	-4.7%	5.0%	-2.3%	7.0%	-6.0%
Others	-10.5%	-12.2%	-11.2%	-20.9%	-20.0%	-18.5%	-20.0%	-18.5%	-13.8%
Total	3.5%	0.6%	4.0%	-8.4%	-3.4%	-1.8%	-6.0%	-4.9%	-6.6%

Source: International Data Corporation (IDC)

On domestic property market, rising of property overhang remained a concern as it increased to 133,162 units as of 4Q2018 (4Q2017: 99,246 units). This indicates that property developers are expected to concentrate more on clearing up their existing inventory. As such, this will translate into slower property related construction activities which was in line with the 5.9% y-o-y (4Q2018: -3.3%) contraction in total construction work done for residential properties in 1Q2019. By extension, this would result in slower demand for building materials such as steel and cement.

Chart 7: Total unsold units for residential properties (completed, under construction and not constructed)



Sources: NAPIC & CEIC

Dissecting the GDP numbers - consumer spending is the saviour

Modest economic growth was predominantly supported by domestic demand which expanded by 4.4% in the first three months of 2019 (4Q2018: 5.7%). Consumer spending was clearly the key underpinning factors although recorded a softer growth of 7.6% as compared to 8.4% in 4Q2018 (trend growth at 6.9%). Stable labour market condition as indicated by steady unemployment rate at 3.3% (4Q2018: 3.3%) as well as rising wage growth among the services and manufacturing employees by 4.9% (4Q2018: 5.9%) have been the linchpin to households spending. On the other hand, public consumption rose from 4.0% in 4Q2018 to 6.3% in 1Q2019 on account of higher spending on supplies and services.

Nonetheless, the private investment has been tepid, growing by only 0.4% in 1Q2019 from 5.8% previously. Cautious view among the private firms were the main constrain for capacity expansion as prospects for final demand looks very challenging. This was evidenced from the fall in the MIER Business Condition Index (BCI) to 94.3 points in 1Q2019 (4Q2018: 95.3). Meanwhile, public investment plummeted 13.2% in 1Q2019 (4Q2018: -5.9%) attributed by near-completion projects such as in RAPID Pengerang Johor.

As for the external sector, real exports recorded a flat growth of 0.1% (4Q2018: 3.1%) while real imports fell 1.4% in 1Q2019 (4Q2018: 1.8%). This has resulted in 0.9 percentage points contribution from net exports to GDP growth.

Table 2: Gross Domestic Product (GDP) y-o-y%

Y-o-Y %	Share (2018)	1Q2018	2Q2018	3Q2018	4Q2018	1Q2019
GDP	**100.0%**	**5.3%**	**4.5%**	**4.4%**	**4.7%**	**4.5%**
Domestic Demand	**94.1%**	**4.1%**	**5.5%**	**6.8%**	**5.7%**	**4.4%**
Private Sector	**74.2%**	**5.2%**	**7.3%**	**7.9%**	**7.8%**	**5.9%**
-Consumption	57.0%	**6.6%**	**7.9%**	**8.9%**	**8.4%**	**7.6%**
-Investment	17.3%	1.1%	5.5%	5.0%	5.8%	0.4%
Public Sector	**19.8%**	**-0.3%**	**-1.6%**	**2.1%**	**0.0%**	**-1.4%**
-Consumption	12.5%	**0.4%**	**3.1%**	**5.2%**	**4.0%**	**6.3%**
-Investment	7.4%	-1.3%	-9.9%	-2.7%	-5.9%	-13.2%
Net Exports of Goods and Services	**7.0%**	**58.0%**	**-6.0%**	**-9.4%**	**15.5%**	**10.9%**
-Exports	67.6%	2.4%	2.6%	0.7%	3.1%	0.1%
-Imports	60.6%	-2.3%	3.6%	2.0%	1.8%	-1.4%
Change in Stocks (RM billion)	**-1.1%**	**-3.3**	**-2.2**	**-6.9**	**-2.0**	**-5.1**

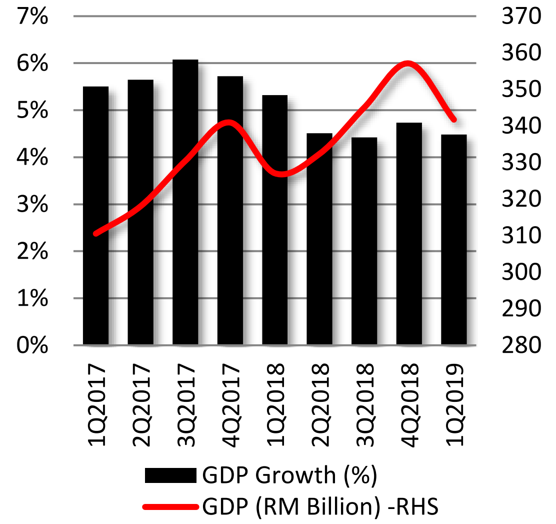
Source: CEIC, Strategic Management, Bank Islam Malaysia Berhad

Table 3: Gross Domestic Product (GDP) y-o-y% by Industry

Y-o-Y %	Share (2018)	1Q2018	2Q2018	3Q2018	4Q2018	1Q2019
Services	56.7%	6.5%	6.5%	7.3%	6.9%	6.4%
Manufacturing	22.4%	5.2%	4.9%	5.0%	4.7%	4.2%
Mining & Quarrying	7.6%	-0.6%	-3.4%	-5.7%	-0.7%	-2.1%
Agriculture	7.3%	3.1%	-1.7%	-0.7%	-0.1%	5.6%
Construction	4.9%	4.9%	4.8%	4.7%	2.6%	0.3%

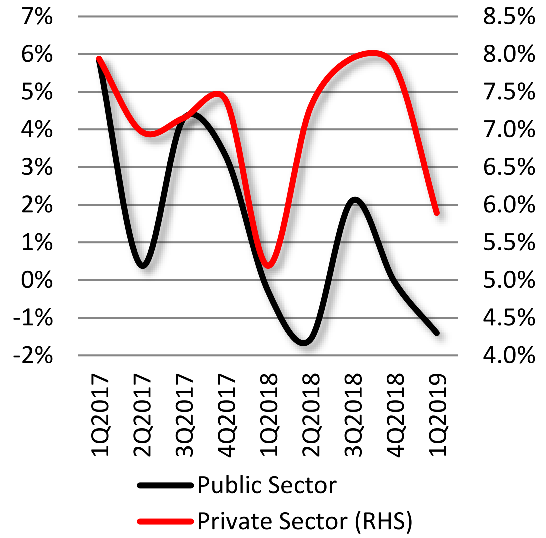
Source: CEIC, Strategic Management, Bank Islam Malaysia Berhad

Chart 8: Gross Domestic Product (GDP) growth (y-o-y%) and Total (RM billion)



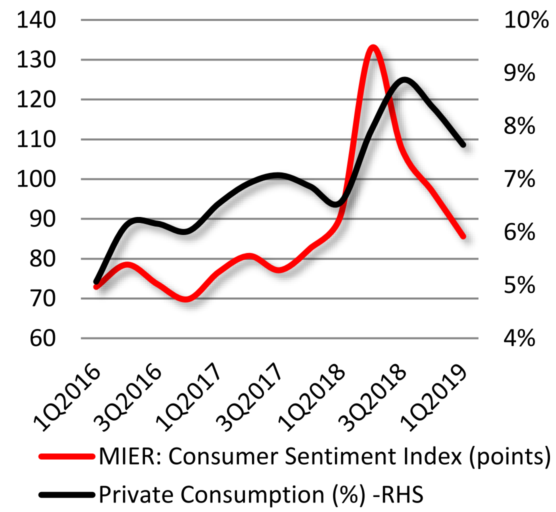
Source: CEIC

Chart 9: Private and Public Sector Growth (y-o-y %)



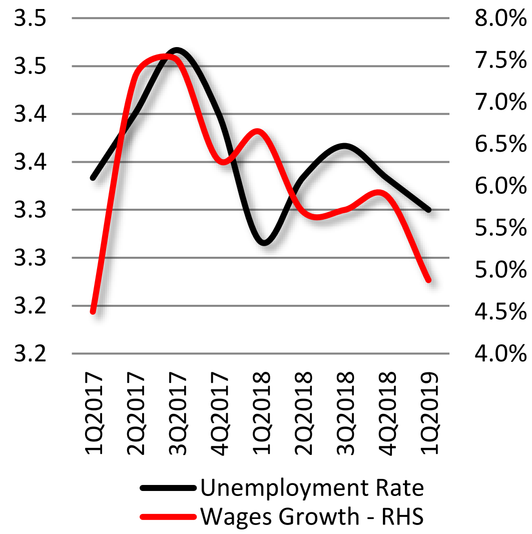
Source: CEIC

Chart 10: Private Consumption (%) vs. MIER Consumer Sentiment Index (points)



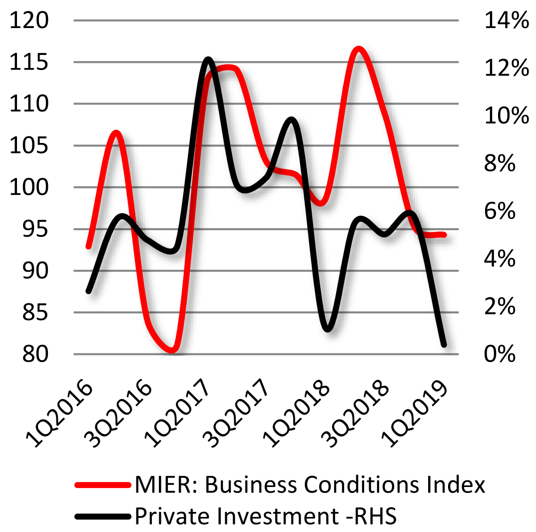
Source: CEIC

Chart 11: Unemployment Rate (%) vs. Services and Manufacturing Wages Growth (y-o-y %)



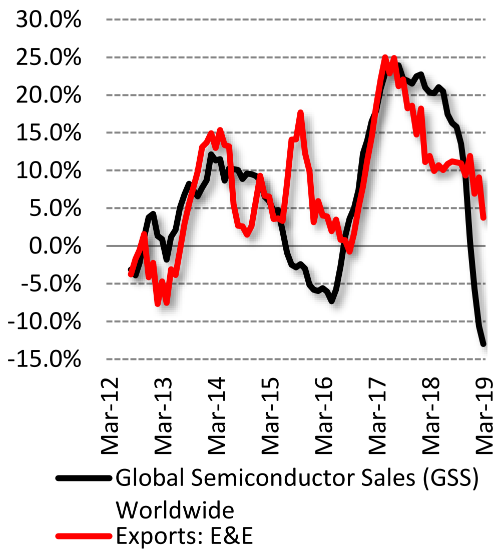
Source: CEIC

Chart 12: Private Investment (y-o-y%) vs. MIER: Business Condition Index (points)



Source: CEIC

Chart 13: GSS (%) vs. Exports: E&E (%)

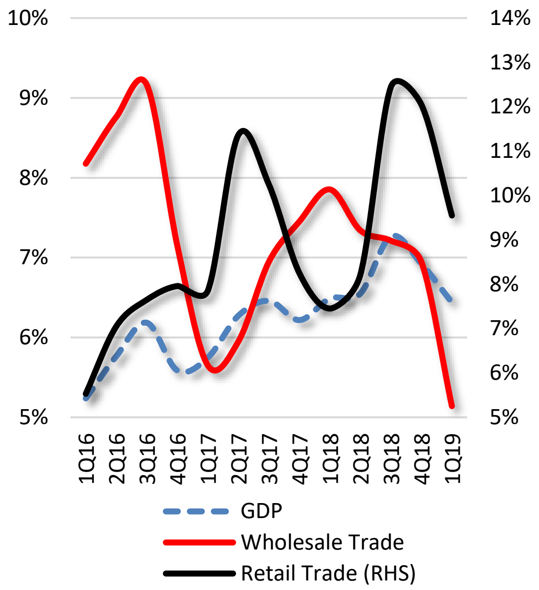


Source: CEIC

Supply-side GDP – services and manufacturing the main driver for growth

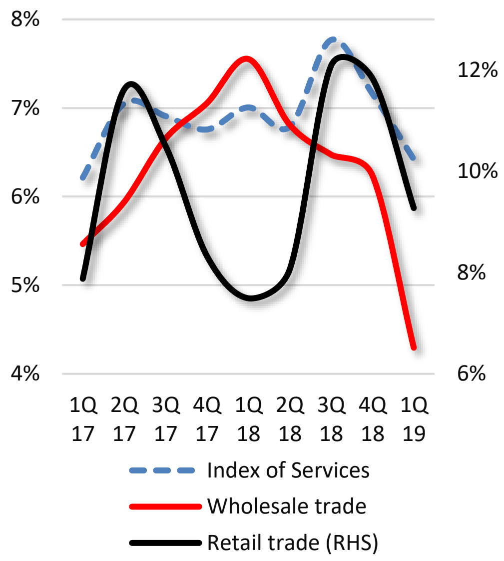
On the supply side, all sectors posted a positive growth except mining and quarrying industries. Services sector grew modestly by 6.4% in 1Q2019 from 6.9% in 4Q2018 and remained as the largest contributor to the economy at 56.7%. The moderation in the services sector was due to the slower growth registered by wholesale (1Q2019: 5.1% vs. 4Q2018: 6.9%) and retail trade (1Q2019: 9.5% vs. 4Q2018: 12.0%) sub-sector. This was in line with the Index of Services, as it cooled-off to 6.4% in 1Q2019 from 7.2% in the previous quarter.

Chart 14: Services vs. Wholesale & Retail Trade (Y-o-Y %)



Source: CEIC

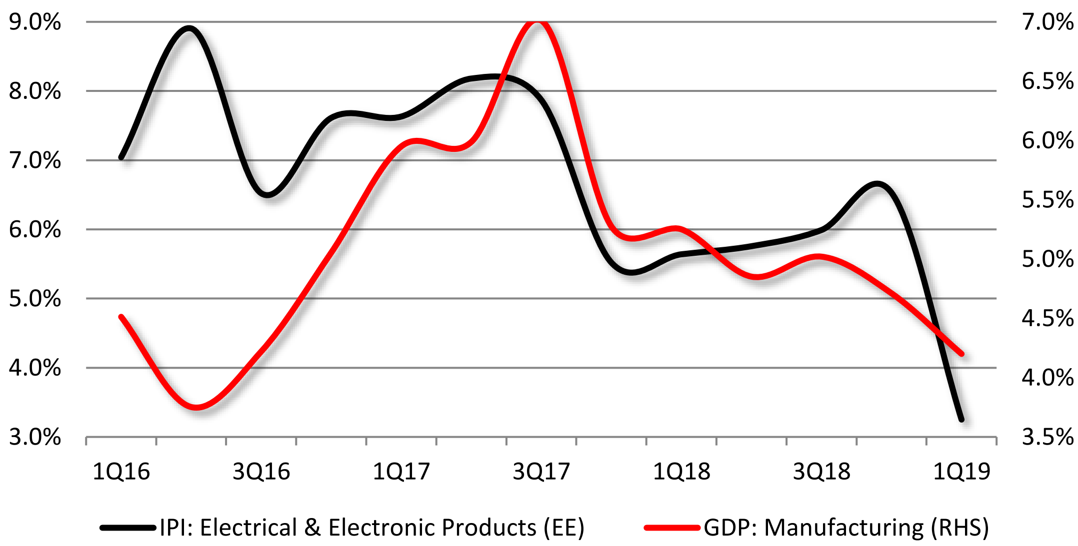
Chart 15: Index of Services vs. Wholesale & Retail Trade (Y-o-Y %)



Source: CEIC

Similarly, manufacturing sector grew moderately from 4.7% in 4Q2018 to 4.2% in 1Q2019. This was mainly driven by softer performance in the electronic and electrical (E&E) production activities (1Q2019: 5.2% vs. 4Q2018: 5.8%). Such performance was in line with three consecutive months of contraction in GSS.

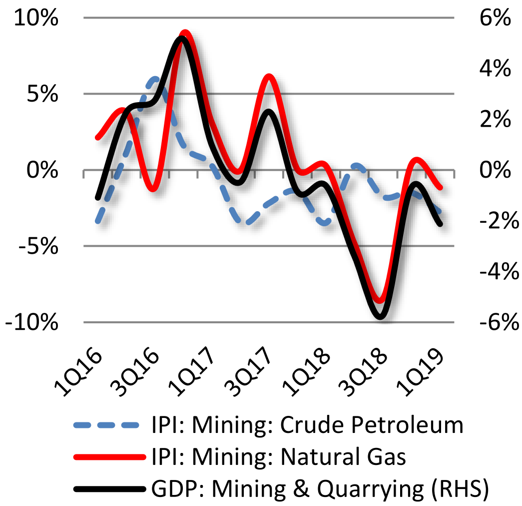
Chart 16: IPI: E&E growth vs. GDP: Manufacturing growth (Y-o -Y %)



Source: CEIC

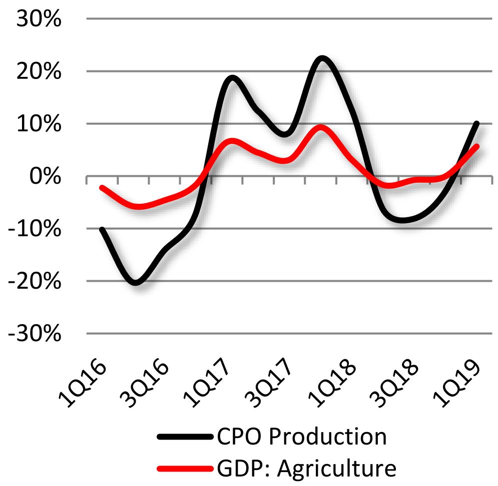
The agriculture sector recorded a stellar performance, rebounding from 0.1% contraction in 4Q2018 to 5.6% expansion in 1Q2019. This was resulting from the strong recovery in rubber (1Q2019: 12.0% vs. 4Q2018: -17.5%), oil palm (1Q2019: 9.8% vs. 4Q2018: -2.7%) as well as forestry and logging (1Q2019: 3.0% vs. 4Q2018: -6.0%) production activities. Additionally, marine fishing continued to post a strong performance as it grew from 8.9% in 4Q2018 to 9.4% in 1Q2019. Meanwhile, mining and quarrying sector declined 2.1% in 1Q2019 after 0.7% drop in the preceding quarter. This was due to the unplanned closure of gas facilities in Sarawak that affects gas production while decline oil production was due to unplanned facility closures in Peninsular Malaysia and Sabah.

Chart 17: IPI: Mining (%) vs. GDP: Mining (Y-o-Y %)



Source: CEIC

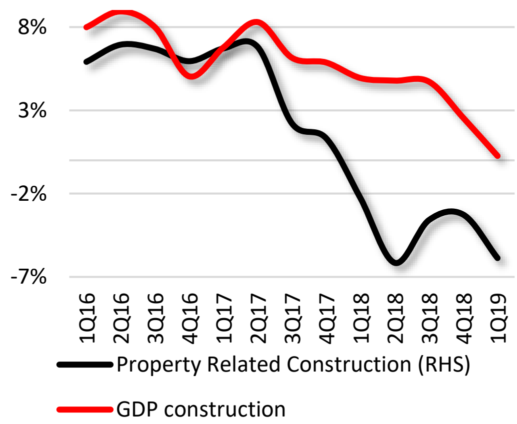
Chart 18: CPO Production Growth (%) vs. Agriculture Growth (Y-o-Y %)



Source: CEIC

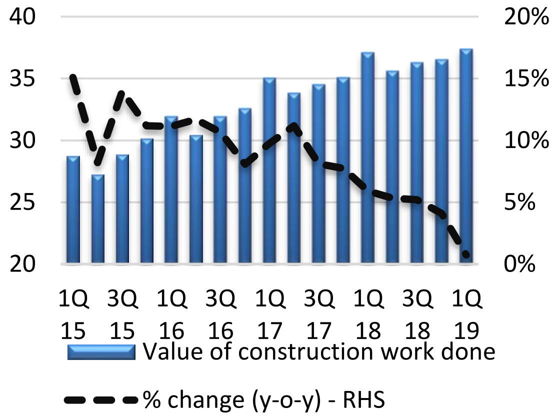
Construction sector posted a slower growth of 0.3% in 1Q2019 (4Q2018: 2.6%) due to lower value of Construction Work Done (1Q2018: 0.7% vs. 4Q2018: 4.1%). This was mainly driven by the slump in the property related construction (residential and non-residential property), recording further contraction at 5.9% in 1Q2019 (4Q2018: -3.3%). Growth remained weak as there were high number of overhang residential properties and oversupply of commercial properties. Notwithstanding, modest performance by civil engineering (1Q2019: 9.5% vs. 4Q2018: 14.3%) and special trade (1Q2019: 4.3% vs. 4Q2018: 8.2%) activities sub-sector have offset the slower growth in the construction sector.

Chart 19: Property Related Construction Growth (%) vs. GDP: Construction Growth (Y-o-Y %)



Source: CEIC

Chart 20: Value of Construction Work Done (RM billion) and growth (Y-o-Y %)



Source: CEIC

Other indicator such as current account surplus balance widened from RM10.8 billion or 2.9% of GDP in 4Q2018 to RM16.4 billion or 4.5% of GDP in the 1Q2019. Larger surplus balance was helped by growing goods surplus from RM32.7 billion to RM33.8 billion in 1Q2019. This was attributed by the lower imports of intermediate and capital goods. Apart from that, lower deficit recorded in the services account (1Q2019: -RM1.8 billion vs. 4Q2018: -RM3.8 billion) and primary income (1Q2019: -RM10.1 billion vs. 4Q2018: -RM12.9 billion) have also contributed to higher current account surplus. Smaller deficits in services account was premised on lower net payments for foreign transportation services as trade activities were moderate during the first quarter. Lower primary income deficits was due to lower portfolio investment payments (1Q2019: -RM4.7 billion vs.4Q 2018: -RM7.3 billion). Nonetheless, deficits in secondary income have been increasing to RM5.5 billion in 1Q2019 from RM5.2 billion in the preceding quarter. Continued outward remittances by foreign worker were the main reason for wider deficits.

Table 4: Balance of payments (RM million)

	1Q 2017	2Q 2017	3Q 2017	4Q 2017	1Q 2018	2Q 2018	3Q 2018	4Q 2018	1Q 2019
Current Account	**5,058**	**10,187**	**12,159**	**10,892**	**13,609**	**2,801**	**3,342**	**10,835**	**16,387**
% GDP	1.5%	3.0%	3.5%	3.0%	3.9%	0.8%	0.9%	2.9%	4.5%
Goods	25,315	27,376	31,579	32,844	34,156	25,919	26,373	32,733	33,849
Services	(6,003)	(4,726)	(4,995)	(7,135)	(5,510)	(5,572)	(2,886)	(3,757)	(1,836)
Primary Income	(10,147)	(8,168)	(10,132)	(10,212)	(10,396)	(12,751)	(15,517)	(12,922)	(10,115)
Secondary Income	(3,905)	(4,238)	(4,418)	-4761	(4,666)	(4,736)	(4,628)	(5,219)	(5,511)
Financial Account	**(8,313)**	**8,986**	**(6,261)**	**858**	**11,910**	**10,536**	**2,307**	**(6,145)**	**(13,816)**
Direct Investment	9,209	(7,147)	9,146	4,964	9,230	(493)	524	2,080	16,260
Asset	(2,058)	(15,563)	(6,336)	(277)	(3,187)	(4,486)	(5,573)	(10,044)	(6,881)
Liabilities	11,267	8,416	15,481	5,241	12,417	3,993	6,097	12,124	23,141
Portfolio Investment	(32,374)	17,513	(9,854)	9,357	(1,500)	(37,919)	786	(5,769)	2,053
Asset	(8,983)	(2,773)	(8,941)	1,254	(9,563)	(724)	4,427	(3,252)	(11,423)
Liabilities	(23,391)	20,286	(913)	8,103	8,062	(37,194)	(3,641)	(2,517)	13,476
Financial Derivatives	646	(286)	570	(1,127)	846	780	32	(687)	(237)
Other Investment	14,206	(1,094)	(6,123)	(12,335)	3,334	48,168	965	(1,769)	(31,892)
Errors and Omissions	**1,061**	**(8,895)**	**309**	**(9,606)**	**(7,287)**	**(14,204)**	**(9,064)**	**(10,792)**	**2,923**
Overall Balance	**(2,195)**	**10,278**	**6,208**	**2,144**	**18,233**	**(867)**	**(3,415)**	**(6,102)**	**5,494**

Source: CEIC, Strategic Management, Bank Islam Malaysia Berhad

Forward Looking View

We have met with BNM officials today to discuss about the 1Q2019 GDP performance. We sense a high degree of uncertainty on the external event notably on the trade war. At the same time, there were long discussion on the latest measures to enhance market liquidity and accessibility whereby strong emphasis has been placed on developing the onshore foreign exchange (FX) market. There are six new initiatives that includes:

- ✓ Increase repo market liquidity and flexibility
- ✓ Enhancement to the MGS futures markets (physical delivery)
- ✓ Expand participation in dynamic hedging programme
- ✓ Greater flexibility to manage FX risks
- ✓ Simplified FX trade and documentation process
- ✓ Improve Ringgit liquidity beyond local trading hours.

It is hope that the measures would alleviate concern posed by the FTSE Russell which subsequently would result Malaysian government bonds to remain in the World Government Bond Index (WGBI). The next review date will be in September 2019.

Having said that, the tone among the BNM officials were cautious. There was a mention on the Overnight Policy Rate (OPR) neutral rate which has been declining. This could have motivated BNM to reduce the OPR on May 7 in order to preserve the degree of monetary policy accommodation. With inflation rate is expected to remain fairly benign, the BNM has the flexibility to prescribe additional monetary easing. This is especially true in the context of considerable downside risks and negative output gaps. There was also question on the Statutory Reserve Requirement (SRR) - currently stands at 4.00% - whether the central bank would be inclined to reduce it at some point in the future. The quick reply was SRR is an administrative measures which aimed at controlling the level liquidity in the financial system. Thus far, liquidity is not an issue at the moment.

All in all, we maintain our **4.5% GDP projection for the year.** The revival of the East Coast Rail Link (ECRL) and Bandar Malaysia projects are noteworthy as this could be deemed as a form of fiscal pump priming measures. Therefore, we could see some support to growth in the 2H2019. Otherwise, expect market volatility to persist.