Malaysia

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Help Needed

Wellian Wiranto
+65 6530 6818
WellianWiranto@ocbc.com

Malaysia's economy slowed down even before the virus hits

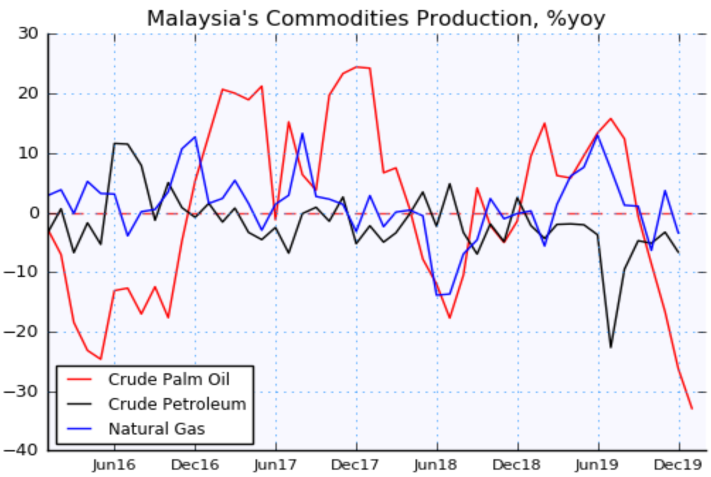
- It's a poor print. There is no way to spin a good story out of the downside surprise seen in the Q4 GDP print out today. At 3.6% yoy, it marks the slowest growth rate in a decade, and sharply lower than expectations.
- While supply disruptions – in CPO, crude and gas – contributed to the hit, the sharp degree of the momentum slowdown signals that the economy has entered 2020 on a weak footing even before the coronavirus outbreak.
- Even as the epicentre of effects – tourism - comprises just 5.8% of economy, the broader fear factor would hit consumption as well. The already-cautious BNM would likely step in further to help. March 3rd may see another OPR cut.

This explains it

When Bank Negara surprised the market on Jan 22nd with what it called a "pre-emptive" rate cut, it noted a series of downside risks that justified the move, including domestic commodity sector supply concerns.

As we noted in our report, the focus was slightly curious because palm oil production contributed just 3% to the economy. As it turns out, it looks to be the marked slowdown in the crude petroleum and natural gas production – which contributes 7-9% of national GDP – which have tipped the balance. Production in those two sectors dipped by 5% and 2%yoy in Q4, adding to the malaise in the overall economy. (Figure 1).

Figure 1. CPO slumps further. Oil and gas productions dipped too.

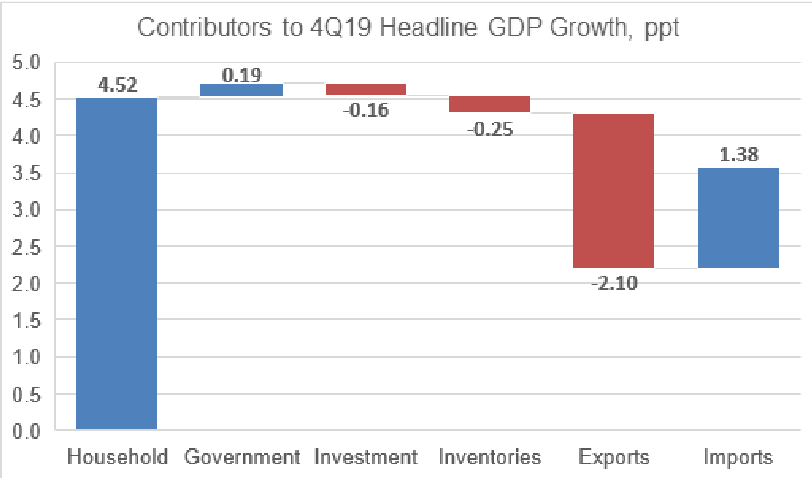


Source: OCBC, CEIC, Bloomberg.

The hit has manifested itself in the form of sectoral downtick in mining and agriculture (-2.5% and -5.7% yoy, respectively), and also in the exports side (-3.1% yoy) in Q4 data. To the extent that the supply disruption might continue into Q1 – with CPO production number in January 2020 dipping 33% yoy – this would continue to present headwinds to Q1 growth.

Looking into expenditure breakdown more broadly, it is notable that household consumption has contributed a massive 4.5ppt to headline GDP growth of 3.6%. Here, continued robust employment outlook would have been the primary support. (Figure 2).

Figure 2. Household consumption still the major driver.



Source: OCBC, CEIC, Bloomberg.

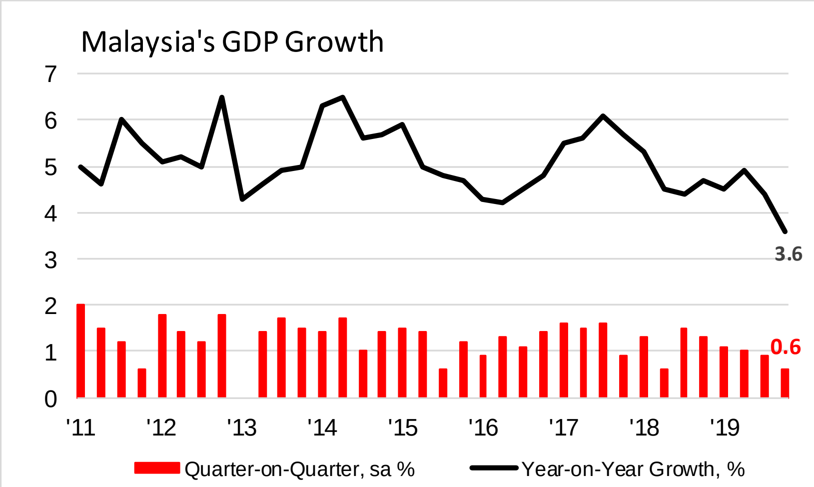
As much as it is a good thing to have domestic support at a time of still-uncertain global trade outlook, however, the impact of coronavirus on consumption in the immediate period would have to be keenly watched.

While Malaysia's number of cases is hardly the top outside of China at this point, the 'fear factor' of going out and mingling about in general may present the ultimate challenge to the continued performance of this growth segment. In other words, to get a sense of how Malaysia's GDP is going to be in Q1 specifically – hopefully we don't have to talk about the virus any longer beyond that – we'll have to watch whether the malls are empty or not.

Elsewhere, investment activities remained broadly lacklustre. Even though the yoy growth rate has picked up to 4.2% in Q4 from 0.3% in Q3, the contribution to headline growth remains negative, at -0.16ppt, in Q4, albeit an improvement from -0.92ppt of the prior quarter. Here, even as FDI inflow has been encouraging especially into the tech cluster, domestic investment activities may remain curtailed by lingering concerns about political uncertainties.

Zooming out onto the broader headline level data, the sequential growth rate of 0.6% on a seasonally adjusted basis in Q4 is a concern. It is the slowest since mid-2018 and stands at the tail-end of 5 consecutive quarters of lower and lower sequential growth rate. (Figure 3).

Figure 3. Slower and slower sequential growth is a concern.



Source: OCBC, CEIC, Bloomberg.

If the economic momentum was already slowing even before the coronavirus outbreak, what chance do we have of a pickup if the current scare drags on and on in the coming weeks?

Bank Negara has hinted as much in a press release today, stating that "*Going into 2020, growth, particularly in the first quarter of the year, will be affected by the coronavirus outbreak*." The central bank is reportedly updating its forecast on March 3rd at its next MPC meeting. One thing for certain is that it will not be revising up its current 4.3-4.8% forecast. A shade-down to 4.0-4.5%, given the weak momentum and uncertainties is not out of the picture.

Our forecast of 4.2% for 2020 is already at the low end of the street and below the existing BNM forecast range. Given the ongoing concerns, however, we are shading it down to 4.0%. In particular, assuming some – but not complete – recovery in the various commodity production, and some impact on private consumption and exports from the viral outbreak, Q1 may see growth of 3.5% yoy.

In terms of policy action, having surprised the market with its "pre-emptive" cut last month, we think there is a distinct possibility for BNM to cut rate again, and soon, in the next meeting on March 3rd. This will be especially so if the commodities production does not pick up. Needless to say, much will depend on how the coronavirus outbreak develops as well, be it contagion of the viral sorts or the economic variety.

While the government is preparing a stimulus package to help, we caution against harbouring hopes of any forceful injection, given fiscal constraints. Indeed, given the denominator effect, the slower GDP growth that we are likely to see is already going to present some challenges to meeting the 3.2% debt-to-GDP target. Hence, for all the help that the Malaysian economy needs this year, BNM remains the main source relative to the fiscal side.

Treasury Research & Strategy

Macro Research

Selena Ling
Head of Research & Strategy
LingSSSelena@ocbc.com

Tommy Xie Dongming
Head of Greater China Research
XieD@ocbc.com

Wellian Wiranto
Malaysia & Indonesia
WellianWiranto@ocbc.com

Terence Wu
FX Strategist
TerenceWu@ocbc.com

Howie Lee
Thailand, Korea & Commodities
HowieLee@ocbc.com

Carie Li
Hong Kong & Macau
carierli@ocbcwh.com

Dick Yu
Hong Kong & Macau
dicksnyu@ocbcwh.com

Credit Research

Andrew Wong
Credit Research Analyst
WongVKAM@ocbc.com

Ezien Hoo
Credit Research Analyst
EzienHoo@ocbc.com

Wong Hong Wei
Credit Research Analyst
WongHongWei@ocbc.com

Seow Zhi Qi
Credit Research Analyst
ZhiQiSeow@ocbc.com