Economic Research

KDN No: PP14787/11/2008(006772)

Malaysian Rating Corporation Berhad
(Company No. : 364803 V)

Vol.: ER/008/2009

Economic Viewpoint:
Malaysia's 1Q2009 GDP

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29th May 2009

GDP: First contraction since …….

A deeper-than-expected contraction

Malaysian economy contracted by a more-than-expected 6.2% in the 1Q2009, owing to deep contractions in exports and in industrial production, sharply in contrast to consensus forecast of a 3.8% contraction. The decline was the sharpest since the 4Q1998 when GDP plunged by a massive 11.2% during the Asian Financial Crisis. On close scrutiny, it is revealed that domestic demand slipped by 2.9% (4Q2008: 2.8%) led by a decline in consumption (-0.2% in 1Q2009 vs. 4Q2008: 7.1%) and investment (-10.8% in 1Q2009 vs. -10.2% in 4Q2008). Private consumption took a beating as the number of job losses increased largely arising from a 7% decline in employment in the manufacturing sector in the period under review. The real culprit however is real exports which fell drastically by 15.2% compared with -13.3% recorded in the preceding quarter. The decline in imports was far greater at 23.5% compared with -10.2% in the 4Q2008.

On the supply side, almost all sectors recorded negative growths, led by manufacturing sector which fell by a massive 17.6% against 8.8% contraction in the preceding quarter. Agriculture and mining contracted by 4.3% and 5.2% respectively, due to lower output of palm oil and rubber as well as declines in crude oil and natural gas production. Similarly, the services sector declined by 0.2% in 1Q2009, the first negative reading since 4Q1998 (-3.0%) following negative contributions from electricity, gas & water (-8.2%) real estate & business services (-6.7%) sub-sectors.

To an extent, the decline in 1Q2009 GDP may not have come as big surprise to many observers. Weak labour market particularly in the manufacturing sector as well as the severe contractions in advanced and emerging economies gave a clear hint on what was to come in the 1Q2009. In addition, a deep contraction in Malaysia's industrial production index (IPI) – which historically has a strong correlation with the headline growth – had clearly signaled the impending weakness of the economy in the 1Q2009.

Table 1: GDP by expenditure

YoY%	1Q 08	2Q 08	3Q 08	4Q 08	1Q 09
GDP	7.4%	6.6%	**4.8%**	**0.1%**	**-6.2%**
Domestic Demand	9.8%	8.4%	6.6%	2.8%	-2.9%
Consumption Expenditure	11.8%	9.6%	7.9%	7.1%	-0.2%
Private Consumption	11.3%	9.4%	8.2%	5.3%	-0.7%
Public Consumption	14.1%	10.3%	6.4%	12.7%	2.1%
GFCF	4.6%	5.6%	3.1%	-10.2%	-10.8%
Exports	5.9%	9.5%	4.5%	-13.3%	-15.2%
Imports	3.2%	8.1%	7.7%	-10.2%	-23.5%

Source: BNM

Table 2: GDP by industry origin

YoY%	1Q 08	2Q 08	3Q 08	4Q 08	1Q 09
GDP	**7.4%**	**6.6%**	**4.8%**	**0.1%**	**-6.2%**
Agriculture	6.5%	6.3%	3.3%	0.5%	-4.3%
Mining and Quarrying	3.7%	-0.5%	-0.3%	-5.7%	-5.2%
Manufacturing	7.0%	5.6%	1.8%	-8.8%	-17.6%
Construction	5.3%	3.9%	1.2%	-1.6%	0.6%
Services	8.4%	7.9%	7.1%	5.7%	-0.2%

Source: BNM

Table 3: Regional GDP Y-o-Y% performance in 1Q 2009

	1Q 08	2Q 08	3Q 08	4Q 08	1Q 09
US	2.5	2.1	0.7	(0.8)	(2.6)
Japan	1.3	0.6	(0.3)	(4.3)	(9.7)
Eurozone	2.2	1.5	0.6	(1.4)	(4.6)
China	10.6	10.1	9.0	6.8	6.1
Indonesia	6.2	6.4	6.4	5.2	4.4
Singapore	6.7	2.5	-	(4.2)	(10.1)
South Korea	5.5	4.3	3.1	(3.4)	(4.3)
Taiwan	6.3	4.6	(1.1)	(8.4)	(10.2)
Thailand	6.0	5.3	3.9	(4.2)	(7.1)
Malaysia	7.4	6.6	4.8	0.1	**(6.2)**

Source: Bloomberg

In line with regional performance

Malaysia's GDP contraction in the 1Q2009 is in line with the regional economies which had been rocked by dramatic declines in exports. Singapore's economy – where exports account for more than 200% of GDP – saw its GDP decline by 10.1%. Similarly Thailand, which experienced political turmoil due to the resurgence of political support for its former Prime Minister Thaksin Shinawatra, experienced a deep contraction of 7.1% in the period under review. Only Indonesia stands out, registering a growth of 4.4% as a strong support from private consumption prevented the economy from sliding into a negative territory.

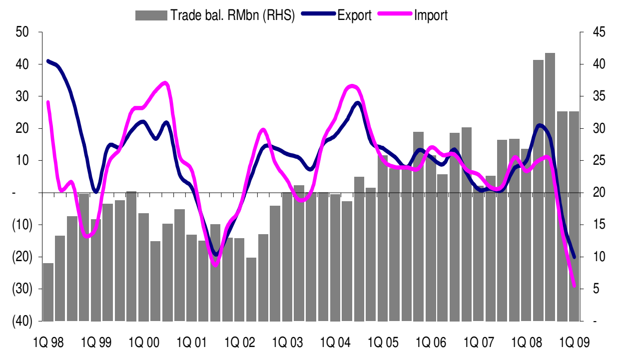
Blame it on the external sector

Massive decline in exports during 1Q2009

Even before the release of the official GDP figures, economists had been anticipating the worst following a dismal performance in exports. The collapse in export growth which begun in the final quarter of 2008 is now reaching the level of the 3Q2001 after it fell by a massive 20.0% in the 1Q2009. The main culprit is plummeting shipment in electrical and electronic products (E&E) by 18.7% and 18.8% in 4Q2008 and 1Q2009 respectively. During these periods, forward-looking indicators such as book-to-bill ratio which measures the amount of orders versus sales, dropped to the lowest point since April 2001 while growth in global chip sales remains in the red.

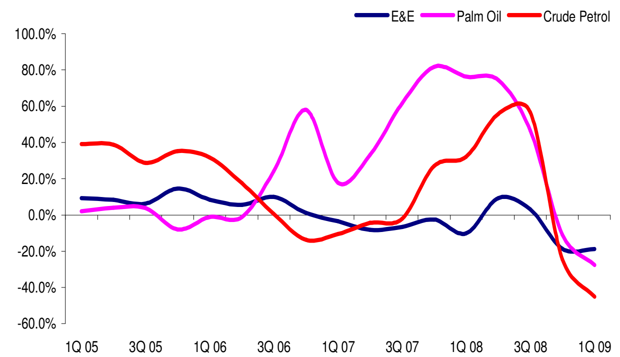
Apart from the E&E sector, non-E&E exports such as palm oil and crude petroleum have also been declining with their exports plunging 27.6% and 45.1% respectively in the 1Q2009 after declining 10.8% and 24.6% in the final quarter of 2008. Apart from lower demand from abroad, significant drop in prices of both commodities also had material effect on export value. In the 1Q2009, average prices for crude palm oil (CPO) and US West Texas Intermediate (WTI) were RM1,943.1 per tonne and US$43.0 per barrel respectively, 43.8% and 56.0% lower than their prices in the same period last year.

Chart 1: Export & import y-o-y % and trade balance (RM bn)



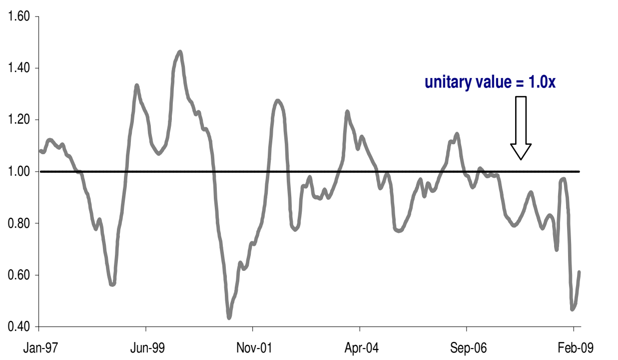
Source: CEIC

Chart 2: Exports of major products y-o-y%



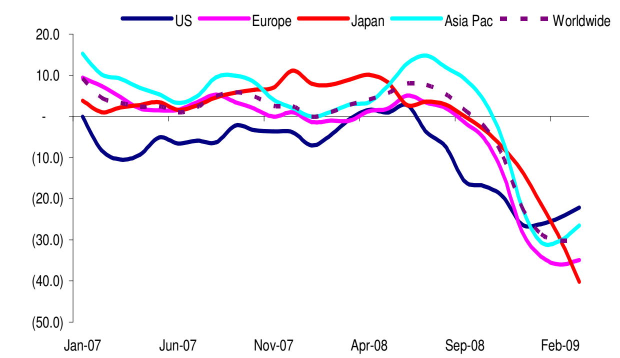
Source: CEIC

Chart 3: Book-to-bill ratio (x)



Source: SEMI

Chart 4: Global chip sales Y-o-Y%



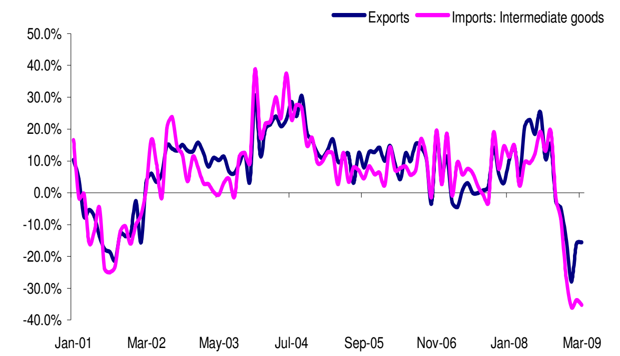
Source: Semiconductor Industry Association (SIA)

Shrinking imports highlighted the weakness in exports

Total imports took a severe beating in the 1Q2009, contracting by 28.9%. The sharp fall in imports of intermediate goods was the main reason for a dismal overall trade performance given its close linkage with total exports as well as its sizeable share to total imports (66%). A quick run on the correlation estimate shows that the two variables are positively correlated at 89%. This is not surprising as intermediate goods which comprise primary industrial supplies, processed industrial supplies and parts & accessories of capital goods are mainly used in the production process of exports.

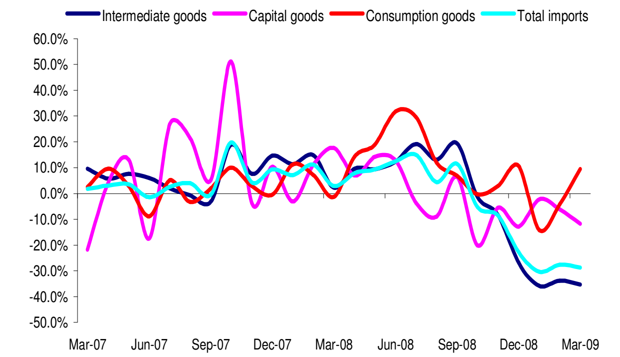
To some extent, weak domestic demand has some bearings on total imports, notably on investment and consumption activities. Thus far, import of capital goods, a close proxy to private investment activities has remained in negative territory since October last year. Meanwhile, imports of consumption goods have seen a marked improvement when it grew by 9.5% in March after posting two months of consecutive decline in January and February this year.

Chart 5: Close link between exports and imports of intermediate goods



Source: CEIC

Chart 6: Imports by economic functions Y-o-Y%

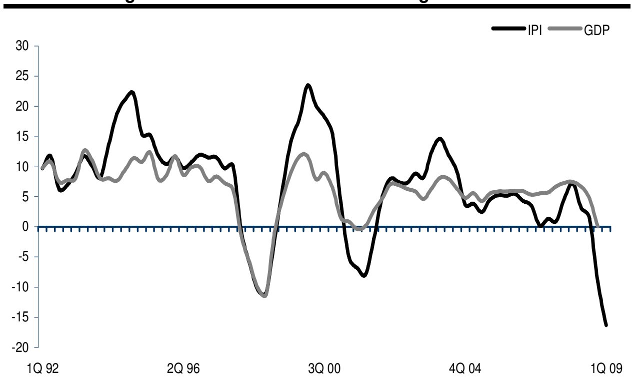


Source: CEIC

What to expect in the coming quarters?

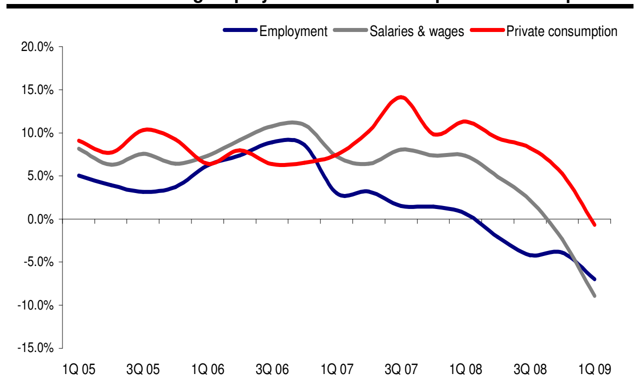
We believe that the economy will continue to contract in the second quarter due to the high base effect and continuing downward pressure on the external sector. In addition, the lag effect arising from the decline in stock market last year and increased job losses will keep consumers away from the High Street, causing private consumption to remain lackluster. While the outlook for the 1H2009 remains murky following the bottoming out of global demand particularly for Malaysia's E&E products, the prospect for 2H2009 is less gloomy. We anticipate that lower base effect couple with an expectation of slower declines in economic activities in developed countries as well as the effect of fiscal stimulus packages will likely arrest a deep contraction in the 2H2009. The anticipated process of stabilisation in domestic and global economy may be a prelude to a firmer recovery in the 1H2010.

Chart 7: Strong correlation between IPI and GDP growth



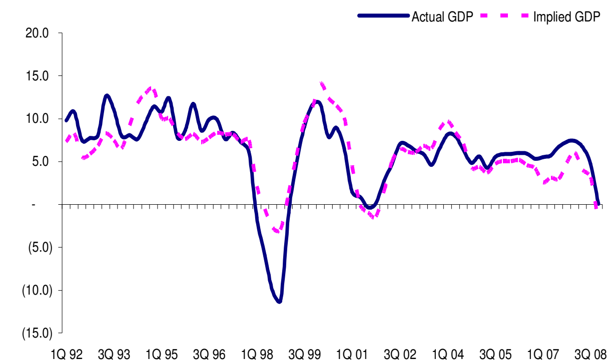
Source: CEIC

Chart 8: Manufacturing employment & salaries vs. private consumption



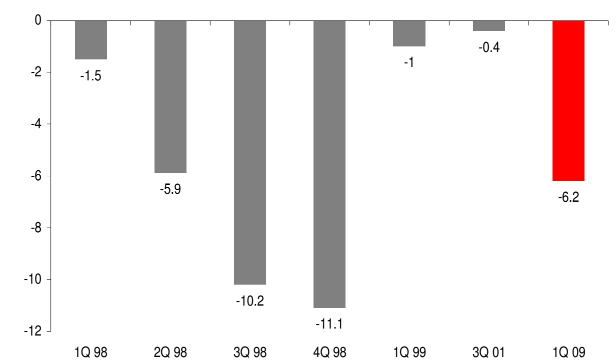
Source: CEIC

Chart 9. Actual GDP vs. implied GDP



Source: MARC Economic Research

Chart 10. Negatives GDP in the past

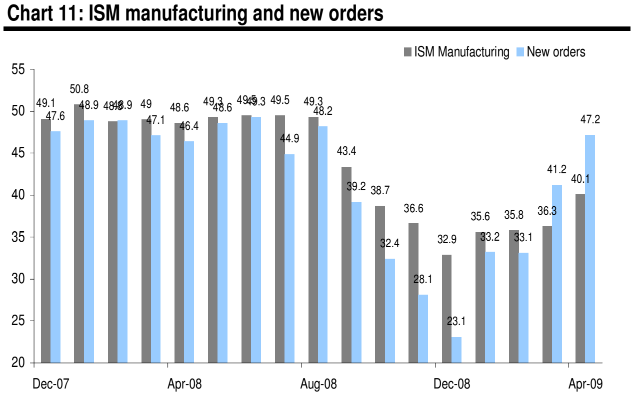


Source: MARC Economic Research

Some silver linings are worth noting. For instance, the US ISM manufacturing index has climbed to 40.1 in April after touching an all time low (since 1980) of 32.9 in January this year. What is more encouraging is the new order sub-index which jumped to 47.2 after reaching its lowest level since the series begun in 1940's! This indicates that production activities may pick up steam in the months ahead. Apart from that, the slower pace of job losses also suggests that the economy may have hit the bottom. Non-farm payroll (NFP) improved to -539,000 in April compared with -699,000 registered in the month before. China's economy has also shown some signs of stabilization reflected by its fixed asset investment which grew by 30.5% in the first four months this year. This signals that the 4 trillion yuan worth of fiscal stimulus is working its way through the economy.

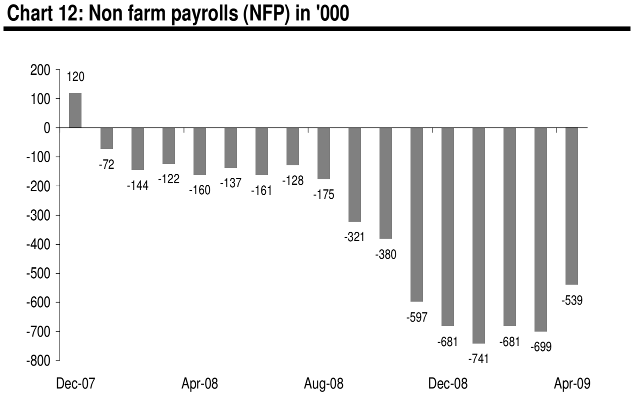
On a more micro note, the performance of Malaysian Pacific Industries (MPI), one of the major listed semiconductor players, has started to improve between February and April after registering a huge net loss of RM53.9 million in the 3QFY09. The higher demand was mainly attributed to the strong consumer sector in China. Similarly, Unisem (M) Berhad – another major semiconductor company – expects revenue and earnings to improve substantially in the 2QFY09. In 1QFY09, the company made a net lost of RM23.4 million. Should the outlook of global demand for semiconductor products continue to improve, Malaysia's external trade will slowly be on the road to recovery by the end-2009.

Chart 11: ISM manufacturing and new orders



Source: Bloomberg

Chart 12: Non farm payrolls (NFP) in '000



Source: Bloomberg