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Malaysia's 4Q2009 GDP: A Quick Note



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the last page of this report*

In a nutshell...

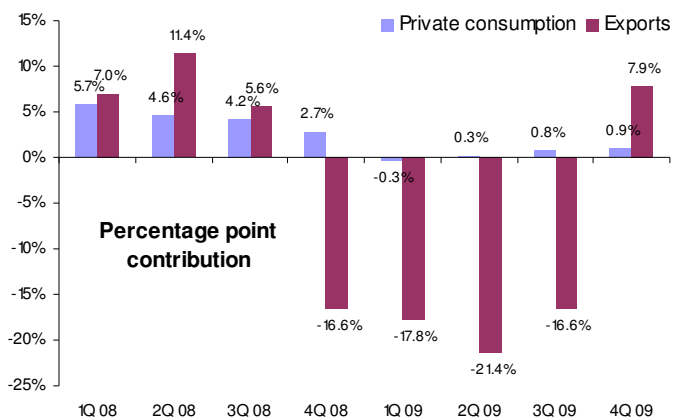
- Malaysia's 4Q2009 gross domestic product (GDP) came in better than expected at 4.5% (consensus: +3.4%) after contracting by 1.2% in the preceding quarter, marking a recovery from a shallow recession following the global economic slump that began in December 2007. For the whole of 2009, the economy contracted by 1.7% (2008: 4.6%), less than the government's expectation of a 3.0% contraction during Budget 2010.
- Growth was largely driven by the external sector, as evidenced by a positive growth in exports (+7.3%) after four consecutive quarters of contraction between 4Q2008 and 3Q2009. Private consumption remained relatively resilient, growing by 1.7% in the quarter under review. Positive development can also be seen in the investment component where gross fixed capital formation rebounded strongly, surging by 8.2% following higher public spending on public utilities, education and transport sectors after remaining weak in the preceding three quarters.
- Rising global demand has benefited the manufacturing sector, which grew at a 5.3% pace after falling by as much as 17.9% in 1Q2009. The growth in the services sector continued to accelerate to 5.1% (3Q2009: +3.4%), underpinned by strong performances of the finance and insurance, wholesale and retail trade, and real estate and business services subsectors. In the same vein, the construction sector registered a robust 9.2% expansion following the implementation of the projects under the fiscal stimulus program and the Ninth Malaysia Plan.
- The government appears to be on track to complete its spending program, while the fiscal position was more favourable than expected with a deficit-to-GDP ratio of 7%, compared with an initial estimate of 7.4% of GDP. Nevertheless, higher operating and development expenditures by 2.3% and 15.6% respectively in 2009 have led to an increase in government debt to 53.7% of GDP from 41.5% in 2008.
- Going forward, growth will likely hinge on external developments as well as the strength of domestic demand which, at this juncture, looks favourable. Against such a backdrop, Bank Negara Malaysia (BNM) is expected to start hiking up the policy rate during its Monetary Policy Committee (MPC) meeting on March 4, 2010. However, we do not expect an aggressive move by the central bank due to a persistent resource slack in the economy, as evidenced by capacity-utilisation rates which stood at 74%, well below the long-term average of 77%. We expect a total 50 bps increase in the Overnight Policy Rate (OPR) and a 100 bps hike in the Statutory Reserve Requirement (SRR) in 2010.

	4Q 08	2008	1Q 09	2Q 09	3Q 09	4Q 09	2009
GDP	0.1	4.6	-6.2	-3.9	-1.2	4.5	-1.7
Demand side							
Private consumption	5.3	8.5	-0.7	0.5	1.5	1.7	0.8
Public consumption	12.1	10.9	2.1	1	10.9	1.3	3.7
Gross fixed capital formation	-10.2	0.8	-10.8	-9.6	-7.9	8.2	-5.5
Exports	-13.3	1.3	-15.2	-17.3	-13.4	7.3	-10.1
Imports	-10.2	1.9	-23.5	-19.7	-12.9	6.9	-12.5
Supply side							
Agriculture	0.5	4.0	-4.3	0.3	-0.5	6.0	0.4
Mining & quarrying	-5.7	-0.8	-5.2	-3.6	-3.5	-2.8	-3.8
Manufacturing	-8.8	1.3	-17.9	-14.5	-8.6	5.3	-9.3
Construction	-1.6	2.1	1.1	4.5	7.9	9.2	5.7
Services	5.7	7.2	-0.2	1.6	3.4	5.1	2.6

Source: Department of Statistics (DOS)

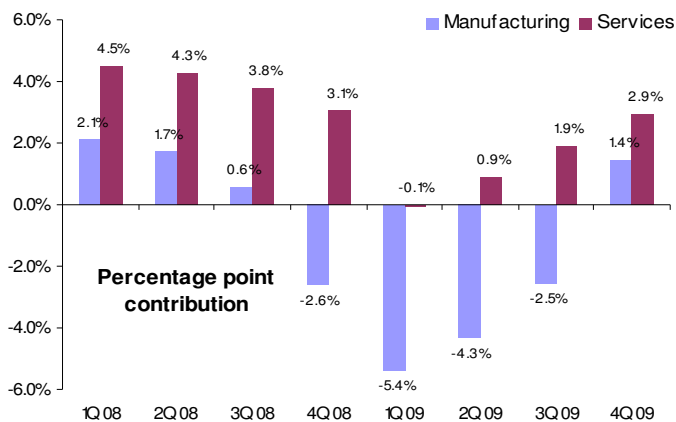
Malaysia's 4Q2009 GDP – A quick review

Chart 1: Growth drivers on the demand side



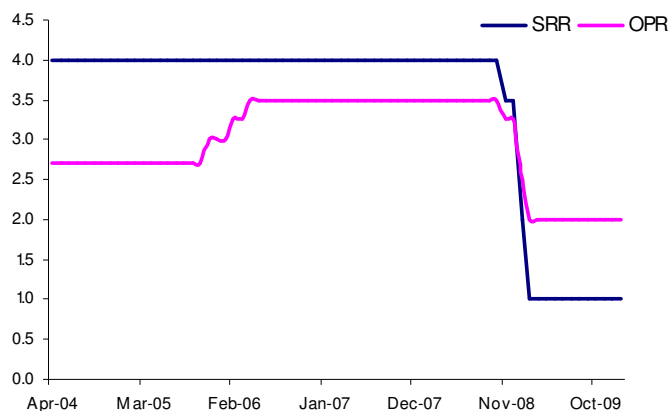
Source: MARC Economic Research

Chart 2: Growth drivers on the supply side



Source: MARC Economic Research

Chart 3: BNM policy rates



Source: CEIC

- Malaysia's GDP rebounded sharply, registering a 4.5% growth in 4Q2009 (3Q2009: -1.2%), beating the market consensus of a 3.4% expansion.

- The stronger-than-expected expansion was primarily led by a recovery in exports, which registered a 7.3% growth (3Q2009: -13.4%), following a swift recovery in global trade. Stronger demand for electronic products was the key to Malaysia's strong rebound in the external sector's performance.

- The growth in 4Q2009 was also supported by a continued expansion in domestic demand, as evidenced by a steady increase in private consumption (+1.7% versus +1.5% in 3Q2009). Investments also grew more than anticipated, expanding by 8.2% after contracting in the preceding three quarters.

- On the supply side, the manufacturing sector led the growth in 4Q2009, expanding by 5.3% year-on-year (y-o-y), compared with a deep contraction of 17.9% in 1Q2009 during the height of the recession. The manufacturing sector has, to a large extent, benefited from stronger overseas demand for electrical and electronic products (E&E) following a recovery of major global economies.

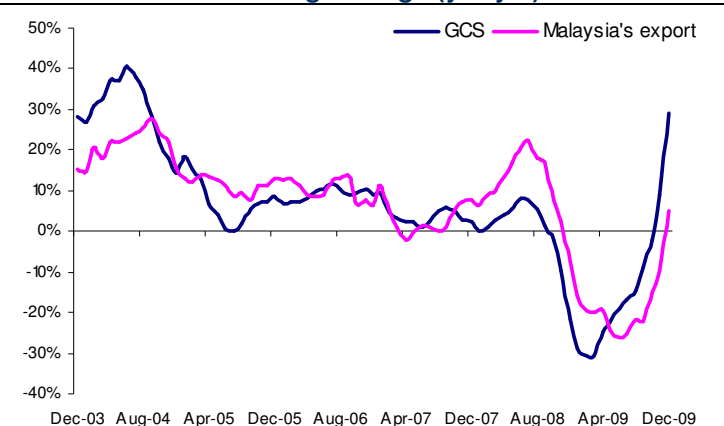
- The services sector, which constitutes the bulk of the economy, remained resilient, growing by 5.1% (3Q2009: +3.4%). The construction sector, which largely benefited from the pump-priming exercises by the government, surged by 9.2%.

- Overall, the economy experienced a mild contraction of 1.7% in 2009 (2008: +4.6%), following a synchronised recession in the advanced economies. Growth is anticipated to accelerate this year, especially in 1H2010, due to the base factor and a recovery in the external sector. With the release of this latest set of statistics, we now foresee a greater risk of an upside bias to our forecast following a sharp rebound in the external sector. However, we caution that the current recovery is mainly driven by external forces which are very much dependent on the performance of the US economy.

- In light of the stronger-than-expected growth in 4Q2009, we now envisage the BNM will normalise its benchmark OPR and the SRR starting from the next meeting on March 4, 2010. For now, we anticipate a 50 bps increase in the OPR and a 100 bps rise in the SRR in 2010.

The main force behind a quick turnaround - the external sector

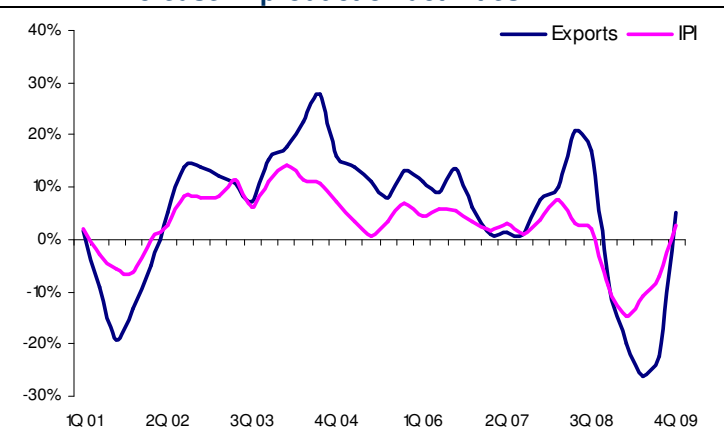
Chart 4: Global chip sales and Malaysia's exports, 3-month moving average (y-o-y%)



Sources: SIA & CEIC

- Total exports grew at a double-digit pace of 18.7% y-o-y in December 2009 owing to stronger E&E exports (+33.3% in December 2009 vs. 5.8% in November 2009) as demand from abroad improved.
- This is in tandem with the expansion in global chip sales (GCS) by 28.9% in December 2009 (November 2009: +8.8%). The Semiconductor Industry Association (SIA) attributed the large increase in sales in 4Q2009 to healthy demand for PCs, cell phones and consumer electronics.
- Apart from E&E products, crude petroleum, rubber and saw logs were the main contributors to the large increases in December's exports.

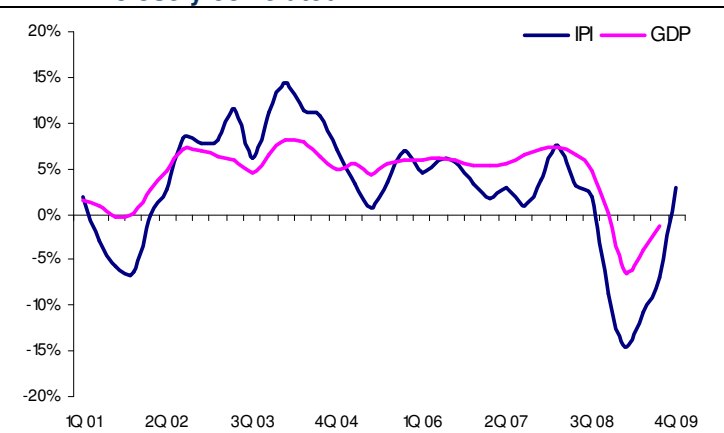
Chart 5: Higher overseas shipments causes an increase in production activities



Source: CEIC

- The pace of production picked up considerably in 4Q2009, as evidenced by the first positive growth in the industrial production index (IPI) by 2.9% after recording negative growths in the preceding four quarters.
- The growth in IPI was largely driven by a 5.1% expansion in the manufacturing sector, of which the expansion in E&E production was the key contributor. E&E output rose 2.0% in 4Q2009 (3Q2009: -22.6%).
- The electricity index was also on an upward trend, growing by 10.3% in 4Q2009 after rising marginally by 3.2% in the preceding quarter. However, output of the mining sector fell at a moderate pace of 3.1%, compared with a 4.2% contraction in the earlier quarter.

Chart 6: Industrial production index (IPI) and GDP are closely correlated

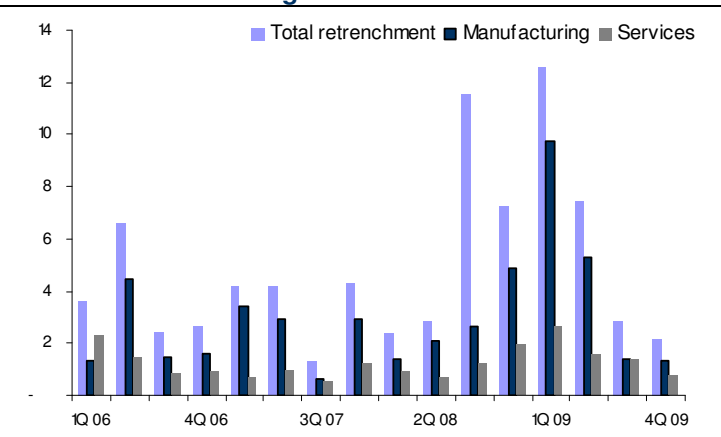


Source: CEIC

- Considering the strong correlation between industrial production and Malaysia's GDP, a sharp recovery in the former will likely lead to further improvement in the headline numbers for the economy in the next few quarters.
- Against such a backdrop, we foresee further acceleration in GDP growth in the next few quarters if the export sector continues to benefit from the global recovery in trade, particularly in the E&E sector.
- The improvement in the headline numbers will also have a positive impact on Malaysia's capacity-utilisation rate, which has improved to 74% in 4Q2009 from 73% in the preceding quarter.

Domestic economy is on the mend

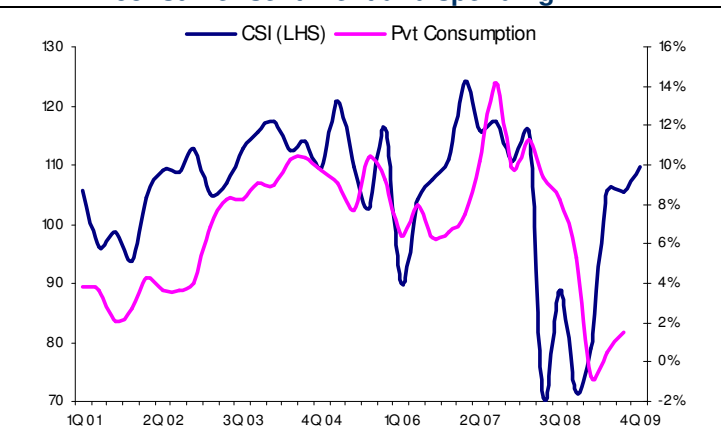
Chart 7: Total retrenchment is declining, led by the manufacturing sector



Source: CEIC

- As production activities gather steam, demand for labour has been rising, leading to a persistent decline in job losses, as evidenced by a decline in the total number of retrenched workers.
- Total retrenched workers fell from 12,590 in 1Q2009 to 2,125 in 4Q2009, led by the decline in the number of retrenched manufacturing workers which dropped substantially from 9,778 in 1Q2009 to 1,354 in 4Q2009.
- The unemployment rate may have peaked at 4.00% in 1Q2009 and has dropped to 3.60% in 2Q2009 and 3Q2009. In light of a positive growth in 4Q2009, the jobless rate is likely to move closer to its long-term average of 3.20% in the near term.

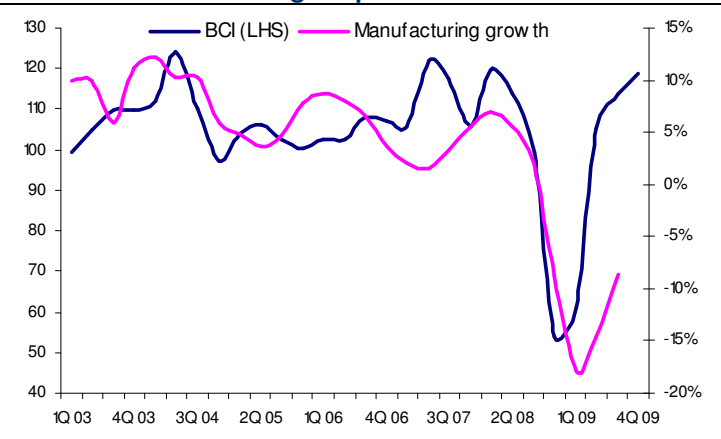
Chart 8: Better employment prospects are boosting consumer sentiment and spending



Source: CEIC

- Consumers are feeling more upbeat these days compared with the earlier part of 2009. This is evidenced by the latest MIER survey of consumer sentiment index (CSI) in 4Q2009 which saw the index rising to 109.6 points, 38.2 points higher than its cyclical low of 71.4 points in 4Q2008.
- As a result, growth in private consumption continued to edge higher at 1.7% in 4Q2009 from 1.5% in the earlier quarter.
- One possible explanation for the resilient private consumption is the labour market for the services sector, which was relatively stable compared to the manufacturing sector following a less adverse impact of the decline in the external demand.

Chart 9: Business condition index (BCI) and manufacturing output

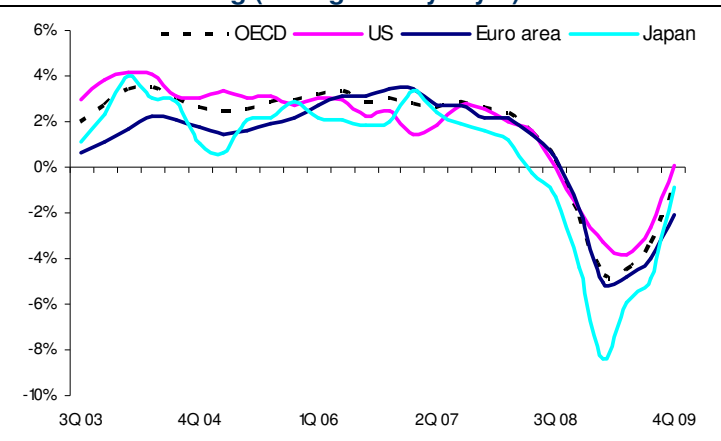


Source: CEIC

- The sentiment among manufacturers also improved in 4Q2009, as evidenced by a sharp increase in the business condition index (BCI) which ratcheted up to 118.8 points in 4Q2009 from its cyclical low of 53.9 points in 4Q2008.
- Manufacturing output also made a sharp about-turn, growing by 5.3% in the final quarter of 2009 after contracting in the precedent four quarters.
- Going forward, the performance of the manufacturing sector will continue to hinge on the global demand condition. Our main concern is that monetary tightening in advanced countries could potentially result in slower demand from abroad, thus affecting Malaysia's external trade performance.

Economic outlook appears favourable for now...

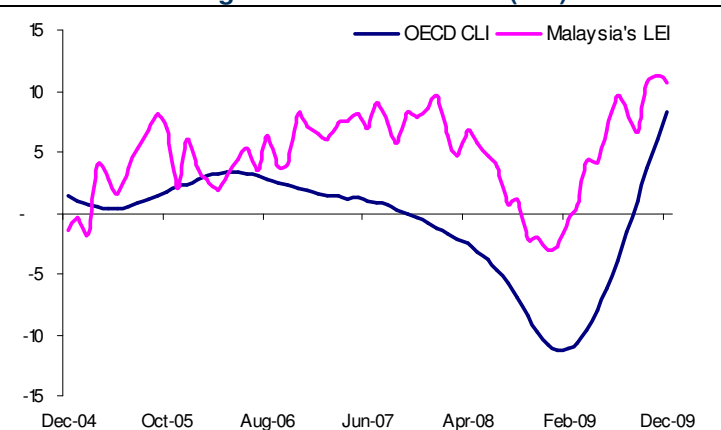
Chart 10: Output lost in OECD countries is clearly receding (GDP growth y-o-y%)



Source: OECD

- Growth performance in OECD countries has been favourable in 4Q2009 where the pace of contraction has substantially declined to an average of 0.7% from as low as -4.8% recorded in 1Q2009. Thus far, the advanced economies have contracted for five consecutive quarters.
- On a more positive note, the US economy managed to register its first positive growth of 0.1% in the quarter under review, while the euro and Japanese economies declined moderately by 2.1% (3Q2009: -4.0%) and 0.9% (3Q2009: -4.9%) respectively.
- Thus far, indicators such as manufacturing PMIs across the globe suggest that production activities will continue to gain momentum in the near term.

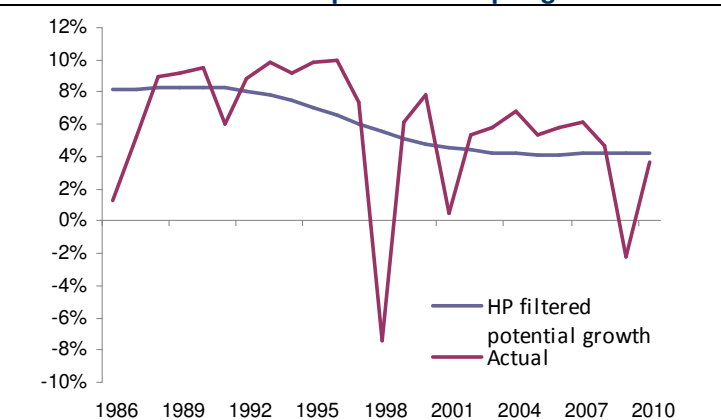
Chart 11: Leading economic indicators (LEI)



Sources: OECD & CEIC

- The economic outlook for Malaysia in the next three to six months is generally positive, as evidenced by a sharp increase in the LEI. Given that, we will likely see further improvement in the headline growth numbers in Malaysia in 1H2010.
- Malaysia's external demand is also expected to improve in 1H2010, leading to positive export growth especially for E&E products as well as major commodities such as crude palm oil, crude oil and LNG.
- Imports are also expected to pick up pace, particularly for capital and consumption goods, in tandem with a recovery in exports.

Chart 12: Actual GDP vs. potential output growth



Source: MARC Economic Research

- Despite a sharp recovery anticipated for 1H2010, we are of the view that the current growth trajectory is below its potential which is estimated to be around 4.2% to 4.5%.
- While we anticipate measures to be undertaken to exit from the current accommodative monetary stance, we do not foresee it to happen in an aggressive manner, given the resource slack that still exists in the economy.
- We believe keeping rates too low could result in a further buildup in household indebtedness which could be detrimental to the economy in the long term. As such, we foresee the rate adjustment to start taking place in the March 4th MPC meeting. Our target for now is a 50 bps increase in the OPR and a 100 bps hike in the SRR in 2010.

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