Feeling the vibes of the economy

MY Say

BY NOR ZAHIDI ALIAS

If you have watched the preview of Paul Krugman's online classes, you would have noticed that he stresses the fact that — contrary to common belief — economics is not about money. It is about people and it ends up looking at how people behave, for example, how people earn a living and how they spend their income.

Unfortunately, a lot of the time, the behaviour of human beings is unpredictable because of the so-called high frequency of "immeasurable variables", or in laymen's terms, factors that shape human behaviour. This is why some regard economics as a dismal science.

Indeed, predicting the future path of the economy is an art, not a science. Economists make anecdotal observations to judge how businesses are faring, how owners of businesses are feeling about their near-term prospects and how individuals are reacting to their surroundings.

Relating to what we see around us these days, there are certainly signs of dark clouds gathering in the global economy. We read about trade tensions, the Brexit-related drama in Europe, as well as China's weakening economic momentum. We come across the word "recession" more often than before. In fact, based on a report, as at end-2018, the frequency of the word recession in stories on the Bloomberg terminal rose to its highest level since the start of 2017. Experience has shown that the "R" word is a pretty good indicator for major US recessions. So, we cannot blame people for feeling gloomy.

But there is a flip side to the story. Things may not look too bad in Malaysia, according to a number of economists. Even Bank Negara Malaysia, in its latest assessment of the economy (the Economic Report released on March 27), is expecting decent economic growth this year. Yes, it is below the trend growth but there will not be a sharp deceleration. Growth will remain at 4.3% to 4.8%.

Of course, there is another camp — the pessimists. They insist that the world around us will materially affect our economy this year. Bank Negara statistics are showing that export growth will be halved to 3.4% from 6.8% last year. This is to be expected — we observed that trade momentum has taken a turn for the worse since the third quarter of 2017. The RWI/ISL container throughput at major global ports, a high-frequency metric, has softened from its peak in the third quarter of 2017. Its growth essentially turned negative in February this year, plunging from its high of 8% in September 2017.

But domestically, the economy is still in pretty good shape — at least at the aggregate level. Most economists are still looking at respectable growth numbers, especially for private consumption (a term commonly used for consumer spending). Consumers are the champions of the Malaysian economy. Their expenditure is seen to remain above 6%, thanks to a relatively strong labour market. We owe it to consumers for helping to place the headline growth number in its current position. Last year, for instance, consumer spending contributed about 90% to overall growth.

In spite of this, we need to zoom in beyond the aggregate level. One question that pops up in the minds of economists is whether there are possible cracks in the consumer segment that we have overlooked at this juncture. Here are some points to consider. While total household debt remains on the decline, the financial health of the vulnerable group — defined as those earning less than RM5,000 per month — is slowly becoming a contentious issue.

Defaults among borrowers in this group, as a ratio to total personal financing, were roughly 27% last year — almost double that of the average borrower. This could have important implications, considering that about 50% of total outstanding personal financing is held by borrowers in this vulnerable group.

Keeping in mind Malaysia's median household income of about RM5,200 per month (according to a 2016 household income survey), we can more or less assume that a sizeable number of households have personal borrowings. That said, if the economy takes a sharper-than-expected downturn, they will be most affected unless they have sufficient financial buffers. There is some good news, though. At a macro level, liquid financial assets look respectable. However, we do not know the distribution. We only know the distribution of household liabilities.

Again, leaving aside the performance of the overall economy, one could ask: how do people and businesses feel as a whole? For this, hiring plans could provide some hints on how businesses view their prospects. For instance, the latest survey by the Department of Statistics in the first quarter of this year indicated that 8.5% of business establishments in Malaysia predicted an increase in the number of employees, while 5% predicted a decline.

This means that more establishments are keen to hire workers in anticipation of better business prospects. That left the so-called "net balance" of 3.5%, lower than the peak of almost 22% registered in the third quarter of 2017.

Another survey by Vistage-MIER shows the top-line CEO Confidence Index declined by 13% in the first quarter of this year from its peak in the third quarter of last year. Its "expectation of future economic conditions" component fell for the second consecutive quarter, while "expected change in employment" and "planned fixed investment" dropped for the third straight quarter in the first quarter of this year.

It is also critical to observe how investors react in the financial markets. By looking at their reactions to current developments, we can get an idea of how investors perceive Malaysia. A case in point: the ringgit has strengthened by 1.3% so far this year, with the inflow of foreign funds partly explaining its strength. This is good news. In the first two months of the year, there were net fund inflows worth RM2 billion into the bond market — a significant improvement over last year's net outflows of RM22 billion. In the eyes of foreign bond investors, Malaysia is again becoming an attractive investment destination.

Nonetheless, the equity market is flashing a different signal. A report from an investment bank research house indicated that Malaysia experienced net foreign outflows to the tune of RM1.7 billion from January up to the first week of April this year, the highest among the four Asean countries in its coverage. So, there are some mixed signals in the financial markets.

There will be challenges going forward, no doubt. But most of these are very much related to what is going on in the global economy. As such, other regional economies will also be affected. But the silver lining is that Malaysia is working hard to address structural issues in the economy, the most crucial of which is the huge national debt. Household indebtedness is also being studied closely, while various measures are being considered to mitigate rising living costs.

We are indeed living in interesting times. E

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