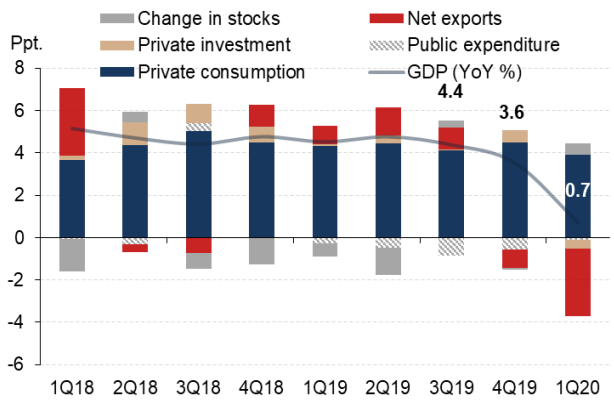
Malaysia 1Q20 GDP

Growth slows to 0.7%, lowest since 2009 Global Financial Crisis

- **Growth moderated sharply in the first quarter of 2020 (0.7% YoY; 4Q19: 3.6%), just a tad lower than house estimate of 0.8% but beating market expectation (consensus: -1.1%)**
  - QoQ: fell sharply (-7.0%; 4Q19: 2.7%).
  - Seasonally adjusted QoQ: contracted (-2.0%; 4Q19: 0.6%), signalling subsiding growth momentum ahead.
- **Broad-based moderation, led by sluggish external and domestic demand amid virus containment measures**
  - Net exports (-37.0%; 4Q19: -12.4%): growth contracted sharply as COVID-19 took its toll through the global supply chain and demand conditions as major trading partners imposed unprecedented travel and movement restriction to combat the pandemic.
    - Exports (-7.1%; 4Q19: -3.4%): growth contracted for the third straight quarter, attributable to a marked decrease in gross exports of E&E (-7.6%; 4Q19: -6.5%) amid lower shipment volume to China, Hong Kong and the EU. Meanwhile, growth contraction in exports of commodities (-7.1%; 4Q19: -18.8%) eased.
    - Imports (-2.5%; 4Q19: -2.4%): growth edged down and remained in negative territory for the fifth straight quarter. However, imports of goods rebounded by 1.3% in 1Q20 (4Q19: -3.9%) on low base effect, a depreciating ringgit and the higher growth of imports of intermediate and consumption goods though weighed by a decline in capital goods.
  - Domestic demand (3.7%; 4Q19: 4.8%): moderated on weak private spending, indicating that both consumer and business sentiment would deteriorate further going forward due to lockdowns and movement restriction to contain the COVID-19 pandemic.
    - Private spending (4.7%; 4Q19: 7.4%): slowed as reflected in falling private investment (-2.3%; 4Q19: 4.3%) and growth moderation in private consumption (6.7%; 4Q19: 8.1%). This is in line with the MIER Business Conditions Index, which dropped to 83 in 1Q20 (4Q19: 88.3) reflecting a bleak outlook, attributed to COVID-19 uncertainty and domestic political situation.
    - Public spending (-0.7%; 4Q19: -2.3%): weaker growth albeit lesser than the previous quarter supported by a sudden jump in public consumption (5.0%; 4Q19: 1.2%) on the back of economic stimulus package announced by the government. However, public investment took a dive on spending cuts, delays and deferment of mega-infrastructure projects (-11.3%; 4Q19: -8.0%).

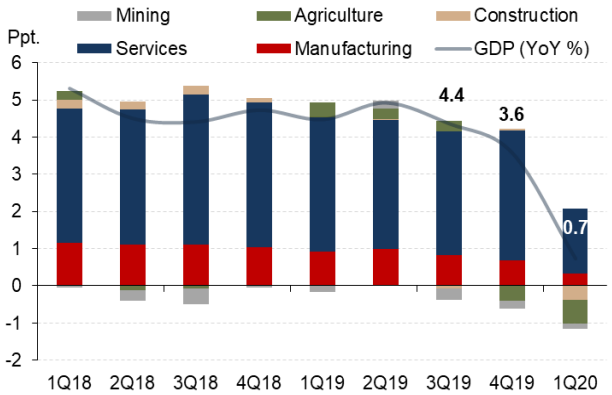
Graph 1: GDP by Expenditure



Source: Dept. of Statistics, Kenanga Research

- **By sector, sharp moderation was recorded across the board, but growth remained anchored by sustained services and manufacturing subsectors**
  - Services (3.1%; 4Q19: 6.2%): growth slowed sharply to its lowest since 2Q09, on a broad-based moderation led by sectors hit hardest by COVID-19-related measures and travel restrictions (i.e. accommodation, motor vehicles, and transportation and storage). Meanwhile, insurance and government services bucked the growth trend and expanded.
  - Manufacturing (1.5%; 4Q19: 3.0%): moderated sharply to its lowest since 1Q13, beating our forecast of a marginal growth contraction of -0.2%. The manufacturing growth was supported by its subsectors led by petroleum, chemical & plastic product, wood products, furniture, paper products and printing as well as E&E.

Graph 2: GDP by Sector



Source: Dept. of Statistics, Kenanga Research

  - Construction (-7.9%; 4Q19: 1.0%): growth dipped to lowest since 1Q99 (-18.0%), weighed by a broad-based decline of its subsectors, led by continued weakness in the commercial and residential buildings, reflective of a persistent supply glut since

2017. It was the biggest variance in our GDP estimate vis-à-vis the official growth numbers as we had projected a marginal 0.6% drop on revival of major infrastructure projects.

- Agriculture (-8.7%; 4Q19: -5.7%): fell sharply for the second straight quarter due to weakness in the oil palm sub-sector led by a decline in the production of Crude Palm Oil (CPO). It almost single-handedly dragged the overall agriculture sector down by 0.6 percentage points contribution to the 1Q20 GDP growth.

- Mining (-2.0%; 4Q19: -3.4%): It was the biggest surprise as we had projected a sharper contraction (-7.1%) on the back of an oil supply shock triggered by oil price war between Saudi Arabia and Russia, and further amplified by the outbreak of COVID-19 pandemic, resulting in worldwide travel and movement restriction. However, it registered a lesser decline in crude oil and natural gas output.

- **Growth to fall sharply in 2Q20 with a high probability that it would be extended towards 2H20, with lingering downside risk from the impact of COVID-19 pandemic, before it gradually recovers in 4Q20 supported by the sizeable fiscal and monetary policy stimuli**

  - The impact of COVID-19 is expected to weigh heavily on 2Q20 economic growth and possibly to extend towards the year-end as a result of lockdown and social distancing measures to manage the contagion. This would further disrupt the supply chain and demand for goods and services in an unprecedented proportion.

  - The services sector, specifically the tourism-related industry and transportation, would continue to be affected the most due to travel restrictions imposed globally. Meanwhile, the manufacturing industry, in particular the export-oriented industries would have to endure a prolonged supply chain disruption as a result of movement restriction and sluggish external demand.

  - Renewed US-China trade tension after US Republican senator proposed legislation that authorised President Donald Trump to impose sanctions on China over COVID-19 probe would weigh on global trade and shake commodity market in the immediate term. Shipping giant Maersk warned that if its prediction of 20%-25% fall in shipping demand in the 2Q20 comes true it would be "the biggest drop in record," reaffirming World Trade Organisation's forecast of a 13-32% fall in global merchandise trade in 2020.

  - Resurgence of COVID-19 infection as a result of pre-mature reopening of the economy as seen by new clusters of infections in major economies especially in South Korea, China and Germany are expected to shake the financial markets. This would risk an even longer and stricter lockdown measures, potentially dragging the economy into a protracted growth or a "U"-shaped trend.

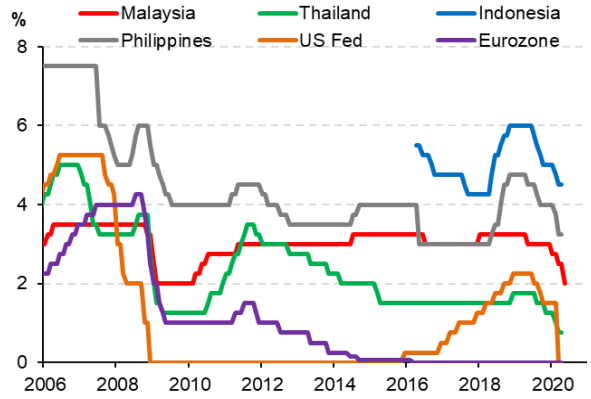
  - Against this backdrop, we are revising our 2Q20 growth forecast to drop even lower to -7.5%, from an initial projection of -4.9%. As a result, our preliminary adjusted 2020 GDP growth forecast would be -2.9% from -1.9% previously (2019: 4.3%).

- **Dovish signals by BNM pointing to a high probability of another OPR cut**

  - BNM in its recent monetary policy statement signalled a dovish tone, pointing out that "it will utilise its policy levers as appropriate to create enabling conditions for a sustainable economic recovery". Given heightened downside risk associated with the pandemic crisis on both the domestic and external front, coupled with high political and geopolitical risk premium, there is no second guess that the central bank would not hesitate to embark on further monetary easing.

  - While BNM recently reduced 50 bps in its OPR, the house believes that BNM still has ample room to ease the monetary policy as both domestic and global economy is about to enter a protracted growth recession in the 2Q20, along with a deflationary trend as well as lower or negative interest rate environment in the advanced economies.

Graph 3: Global Policy Rate Trend



Source: BNM, Department of Statistics, Kenanga Research

  - Therefore, the house expects BNM to slash the OPR by at least another 25 bps at the next MPC meeting in July, bringing the OPR to settle at 1.75% in 2020, a new record low.

Table 1: Malaysia GDP Growth (constant 2015 prices)

% YoY Growth	2017	2018	2019	2Q19	3Q19	4Q19	1H19	2H19	1Q20
By Sector									
Agriculture	5.7	0.1	2.0	4.3	4.0	-5.7	5.1	-0.7	-8.7
Mining	0.4	-2.6	-2.0	0.9	-4.1	-3.4	-0.3	-3.7	-2.0
Manufacturing	6.0	5.0	3.8	4.3	3.6	3.0	4.2	3.3	1.5
Construction	6.7	4.2	0.1	0.5	-1.4	1.0	0.5	-0.2	-7.9
Services	6.2	6.8	6.1	6.1	5.8	6.2	6.3	6.0	3.1
Real GDP	**5.7**	**4.7**	**4.3**	**4.8**	**4.4**	**3.6**	**4.7**	**4.0**	**0.7**
Ppt. Contribution									
Agriculture	0.4	0.0	0.1	0.3	0.3	-0.4	0.4	-0.1	-0.6
Mining	0.0	-0.2	-0.2	0.1	-0.3	-0.3	0.0	-0.3	-0.2
Manufacturing	1.3	1.1	0.8	1.0	0.8	0.7	0.9	0.7	0.3
Construction	0.3	0.2	0.0	0.0	-0.1	0.0	0.0	0.0	-0.4
Services	3.4	3.8	3.5	3.5	3.3	3.5	3.5	3.4	1.8
Real GDP	**5.7**	**4.7**	**4.3**	**4.8**	**4.4**	**3.6**	**4.7**	**4.0**	**0.7**
By Expenditure									
Consumption	6.6	7.1	6.7	6.5	6.0	6.6	7.0	6.3	6.5
Public	5.5	3.3	2.0	0.3	1.0	1.3	3.2	1.1	5.0
Private	6.9	8.0	7.7	7.8	7.0	8.1	7.7	7.6	6.7
Investment	6.1	1.4	-2.1	-0.6	-3.7	-0.7	-2.0	-2.3	-4.6
Public	0.3	-5.0	-10.9	-7.8	-14.6	-8.0	-11.0	-10.7	-11.3
Private	9.0	4.3	1.6	1.5	0.4	4.3	1.1	2.1	-2.3
Public Spending	3.4	0.1	-2.8	-2.4	-4.8	-2.3	-2.0	-3.4	-0.7
Private Spending	7.4	7.1	6.3	6.1	5.5	7.4	6.0	6.4	4.7
Aggregate Demand	6.5	5.5	4.4	4.5	3.5	4.8	4.5	4.2	3.7
Exports	8.7	2.2	-1.6	0.5	-2.1	-3.4	0.3	-2.8	-7.1
Imports	10.2	1.3	-2.3	-2.3	-3.5	-2.4	-2.0	-2.9	-2.5
Real GDP	**5.7**	**4.7**	**4.3**	**4.8**	**4.4**	**3.6**	**4.7**	**4.0**	**0.7**
Ppt. Contribution									
Consumption	4.4	4.8	4.7	4.4	4.3	4.7	4.7	4.5	4.5
Public	0.7	0.4	0.3	0.0	0.1	0.2	0.4	0.2	0.6
Private	3.7	4.4	4.4	4.4	4.1	4.5	4.4	4.3	3.9
Investment	1.5	0.3	-0.5	-0.2	-0.9	-0.2	-0.5	-0.5	-1.1
Public	0.0	-0.4	-0.8	-0.5	-1.0	-0.7	-0.7	-0.9	-0.7
Private	1.5	0.7	0.3	0.3	0.1	0.6	0.2	0.3	-0.4
Public Spending	0.7	0.0	-0.6	-0.4	-0.9	-0.6	-0.4	-0.7	-0.1
Private Spending	5.3	5.1	4.7	4.7	4.2	5.1	4.6	4.7	3.5
Aggregate Demand	6.0	5.2	4.2	4.3	3.3	4.5	4.2	3.9	3.4
Exports	5.8	1.5	-0.9	0.4	-1.4	-2.3	0.2	-1.8	-4.6
Imports	6.1	0.8	-1.5	-1.4	-2.1	-1.4	-1.2	-1.8	-1.4
Real GDP	**5.7**	**4.7**	**4.3**	**4.8**	**4.4**	**3.6**	**4.7**	**4.0**	**0.7**

Source: Dept. of Statistics, Kenanga Research, F: forecast

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