Developments in the Malaysian Economy

HIGHLIGHTS

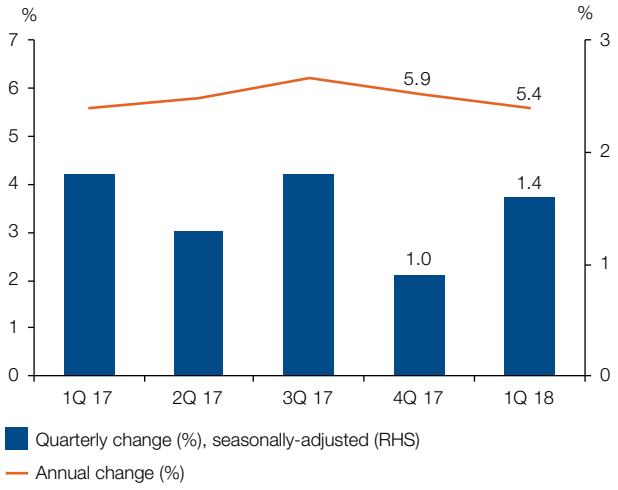
- The Malaysian economy registered a growth of 5.4% in the first quarter.
- Headline and core inflation declined to 1.8% and 1.9%, respectively.
- Current account balance widened to 4.4% of GNI, driven mainly by a sizeable goods surplus.

The Malaysian economy grew by 5.4% in the first quarter of 2018

The Malaysian economy expanded by 5.4% in the first quarter of 2018 (4Q 2017: 5.9%), driven by continued growth in private sector spending (5.2%; 4Q 2017: 7.4%) and strong growth in net exports (62.4%; 4Q 2017: 2.3%). On a quarter-on-quarter seasonally-adjusted basis, the economy grew by 1.4% (4Q 2017: 1.0%).

More moderate growth in 1Q 2018

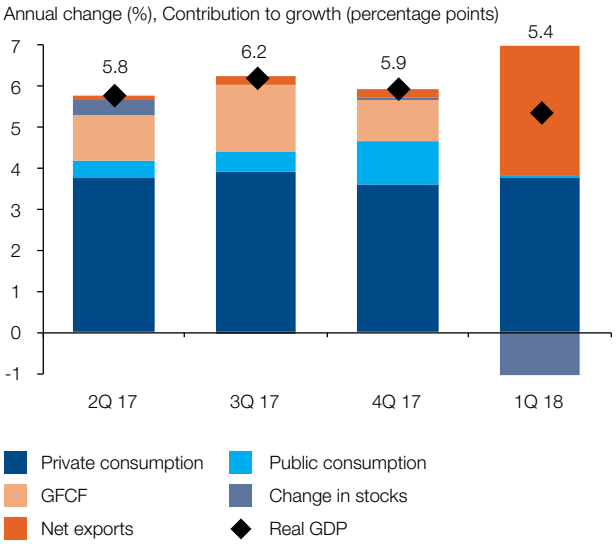
Chart 4: GDP Growth



Source: Department of Statistics, Malaysia

Growth supported by private sector spending and net exports

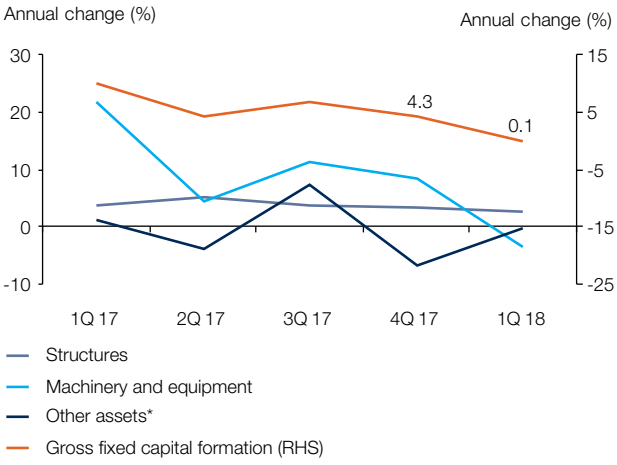
Chart 5: Contribution of Expenditure Components to GDP Growth



Source: Department of Statistics, Malaysia

Gross fixed capital formation expanded at a slower pace

Chart 6: GFCF Growth by Type of Assets



*Other assets include mineral exploration, research & development and capitalised planting.

Source: Department of Statistics, Malaysia

Domestic demand driven by the private sector

Domestic demand recorded a moderate growth of 4.1% (4Q 2017: 6.2%), due to lower growth of private sector expenditure (5.2%; 4Q 2017: 7.4%) and a marginal decline in public sector spending (-0.1%; 4Q 2017: +3.4%).

Private consumption registered a sustained growth of 6.9% (4Q 2017: 7.0%), supported by continued strength in wage and employment growth.

Growth of private investment moderated to 0.5% (4Q 2017: 9.2%). Private investment was weighed down by lower capital spending in structures, particularly in residential and commercial properties, and machinery and equipment during the quarter. On a sectoral basis, private investment was supported mainly by the services sector, particularly the education and healthcare sub-sectors.

Public consumption growth was lower at 0.4% (4Q 2017: 6.8%) on account of lower expenditure on supplies and services.

Public investment continued to decline in the first quarter (-1.0%; 4Q 2017: -1.4%), attributed to the contraction in spending on fixed assets by public corporations. The lower capital spending by public corporations was due mainly to the near completion of a few large-scale projects.

Gross fixed capital formation (GFCF) growth moderated to 0.1% (4Q 2017: 4.3%). By type of assets, capital spending on machinery and equipment registered a contraction of 3.6% (4Q 2017: +8.3%). Investment in structures grew more moderately (2.8%; 4Q 2017: 3.3%) while investment in other types of assets recorded a smaller decline of 0.2% (4Q 2017: -6.8%).

Continued expansion across major economic sectors

On the supply side, services and manufacturing sectors remained the key drivers of growth.

The services sector expanded at a faster pace during the quarter. The improvement was attributed mainly to higher growth in the finance and insurance sub-sector, resulting from higher lending activity, particularly in the household segment. Growth in the information and communication sub-sector also improved, driven by increased demand for data communication services. The wholesale and retail trade sub-sector continued to expand, supported by sustained strength in household spending.

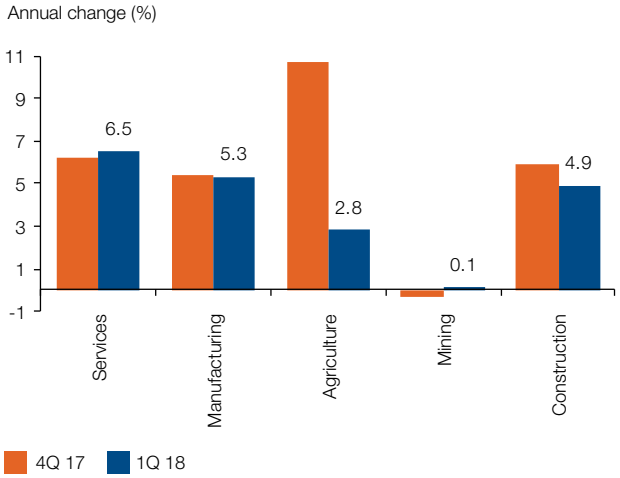
The manufacturing sector registered sustained growth in the quarter supported by improvements in the export-oriented industries and construction-related cluster. These offset the sharp moderation in the consumer-related clusters, which was mainly due to slower production of food-related items and transport equipments. Stronger output growth in the primary-related cluster (e.g. chemical- and petroleum-related products) was supported by higher oil production. The higher growth in the E&E cluster reflected the continued expansion of the global technology upcycle. Higher growth in the construction-related cluster was in line with the strength of civil engineering activities during the quarter.

Growth in the construction sector moderated in the quarter. While growth of the civil engineering sub-sector was stronger, supported by the transportation, petrochemical and power plant projects, the sector's performance was affected by weaker activity in the residential and non-residential sub-sectors. This is consistent with the significant number of unsold residential properties and the ongoing weaknesses in the commercial property segment (oversupply of office spaces and shopping complexes).

Growth in the agriculture sector moderated, reflecting mainly lower rubber tapping activities amid weak rubber prices during the quarter. However, the mining sector's growth rebounded, supported mainly by higher oil production.

Economic sectors continued to expand

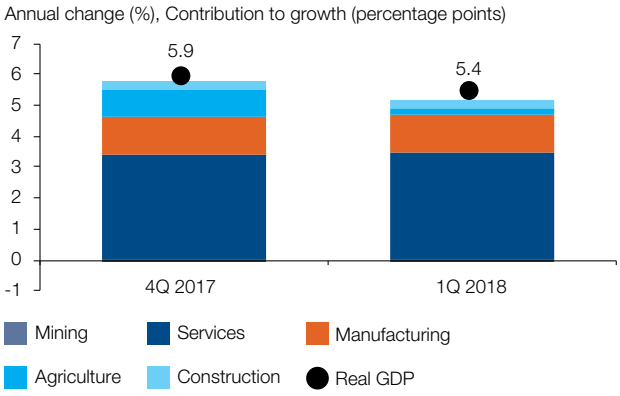
Chart 7: Growth by Sector



Source: Department of Statistics, Malaysia

Services and manufacturing sectors remained the key drivers of growth

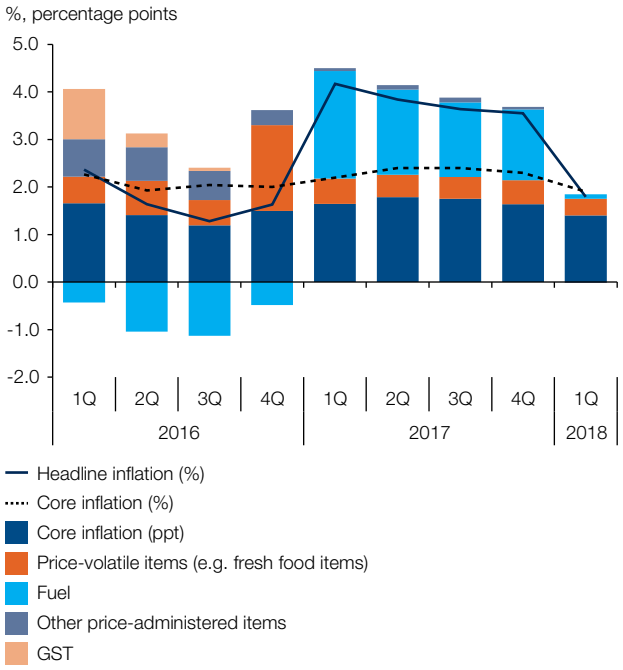
Chart 8: Real GDP by Economic Sector



Source :Department of Statistics, Malaysia

The decline in inflation reflected smaller contribution of domestic fuel prices

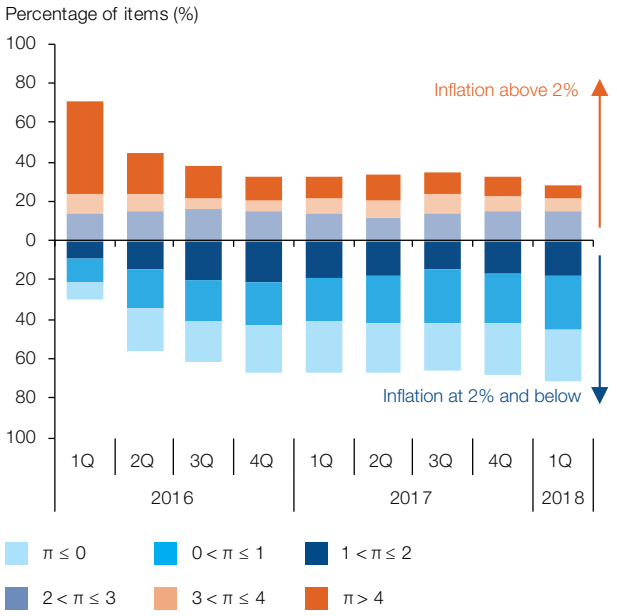
Chart 9: Contribution to Headline Inflation by Components



Source: Department of Statistics, Malaysia and Bank Negara Malaysia estimates

Inflation pervasiveness was slightly lower in 1Q 2018

Chart 10: Inflation Pervasiveness



Source: Department of Statistics, Malaysia and Bank Negara Malaysia estimates

Lower headline inflation in the first quarter amid smaller contribution of domestic fuel prices

Headline inflation, as measured by the annual percentage change in the Consumer Price Index (CPI), declined to 1.8% in 1Q 2018 (4Q 2017: 3.5%).

The low inflation outcome reflected the smaller contribution of domestic fuel prices to headline inflation. Despite higher global oil prices during the quarter, the magnitude of increase was smaller than the previous quarter. The impact of higher global oil prices was also offset by the stronger ringgit exchange rate[3]. As a result, transport inflation declined significantly during the quarter (1Q 2018: 1.3%; 4Q 2017: 11.4%). More favourable supply conditions for fresh food items also helped contain food price increases during the quarter (1Q 2018: 3.2%, 4Q 2017: 4.1%).

Core inflation also moderated during the quarter to 1.9% (4Q 2017: 2.3%). Given the lack of persistent tightness in capital stock and wage pressures, demand-driven inflationary pressures in the economy remained stable.

The decline in inflation was broad-based across the CPI categories. The percentage of items in the CPI basket that registered inflation of more than 2% moderated to 28% in 1Q 2018 (4Q 2017: 32%).

[3] The ringgit appreciated to average RM3.9246 against the US dollar in 1Q 2018 from RM4.1626 in 4Q 2017.

Improved labour market conditions

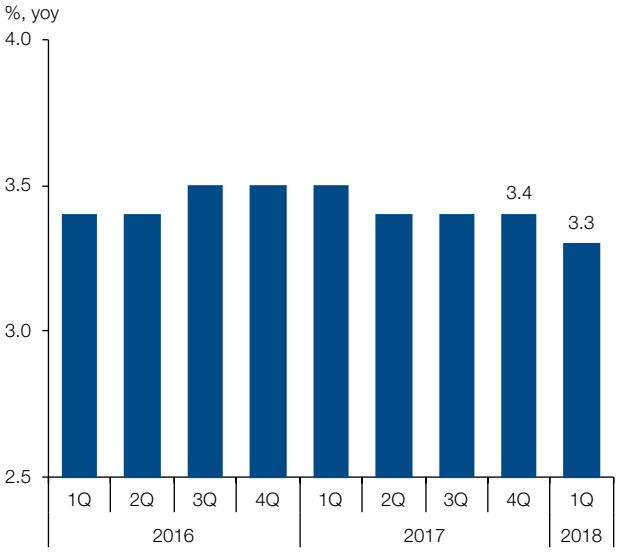
Labour market conditions continued to improve in the first quarter of 2018. Private sector wage growth increased to 6.6% (4Q 2017: 6.3%). During the quarter, net employment gains exceeded labour force expansion, resulting in a slight improvement in the unemployment rate to 3.3% (4Q 2017: 3.4%). This was amid the increase in the number of vacancies posted on a major job search website to 69,238 positions in the 1Q 2018 (4Q 2017: 61,061 positions), which suggests increasing labour demand.

In the financial sector[4], there was a net employment loss of 668 jobs to 164,216 employed persons in 1Q 2018 (4Q 2017: 164,884 persons). This was mainly due to the losses in mid-skilled occupations (-1,271 jobs), which was partly offset by gains in high-skilled jobs (+642 jobs).

Continued strength in private sector wage growth was driven by the manufacturing sector. Manufacturing wage growth increased to 13.9% (4Q 2017: 9.4%). While the low salary base in January-February 2017 did play a role, manufacturing wages in March 2018 remained strong at 11.9%. When viewed on a quarter-on-quarter basis, manufacturing wages grew by 4.8% in 1Q 2018 (4Q 2017: 2.1%). The wage growth in the major services sub-sectors decreased marginally to 3.5% (4Q 2017: 5.0%), attributed to a broad-based moderation in wage growth across all services subsectors.

Lower unemployment rate

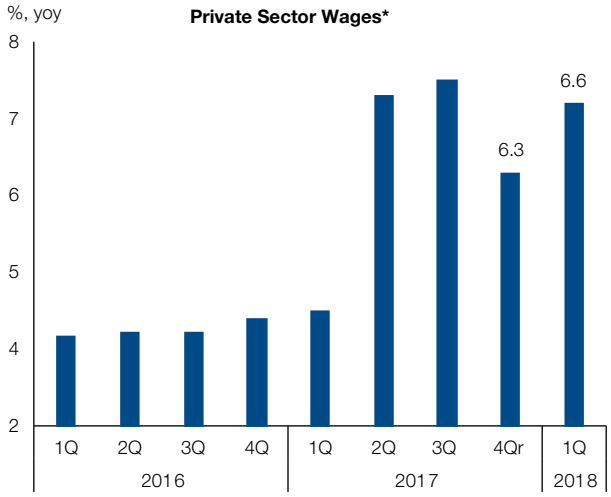
Chart 11: Unemployment rate



Source: Department of Statistics, Malaysia

Expansion in private sector wage growth

Chart 12: Private sector wages



* Private sector wages is derived from the salaries and wages data published in the Monthly Manufacturing Statistics and Quarterly Services Statistics by the Department of Statistics, Malaysia (DOSM). It covers 64% of total employment.

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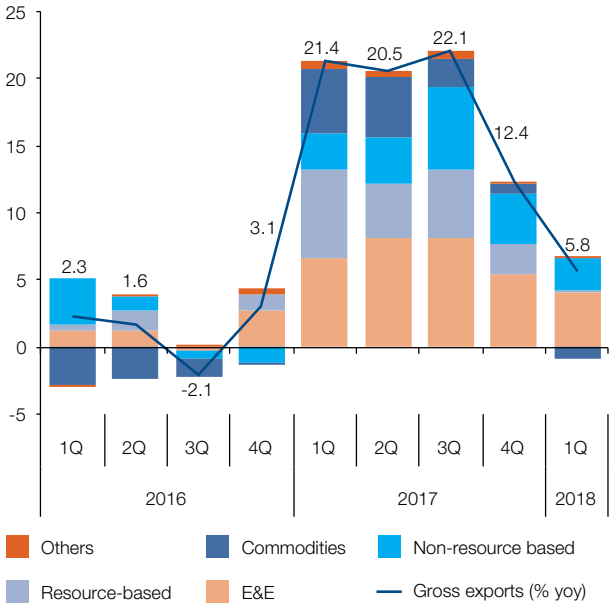
Source: Department of Statistics, Malaysia and Bank Negara Malaysia estimates

[4] Covers only the banking institutions, development financial institutions, insurance companies and takaful operators. The information is obtained from an establishment survey conducted by Bank Negara Malaysia.

Export growth supported mainly by manufactured exports

Chart 13: Gross Exports by Products

Annual change (%), Contribution to growth (percentage points)

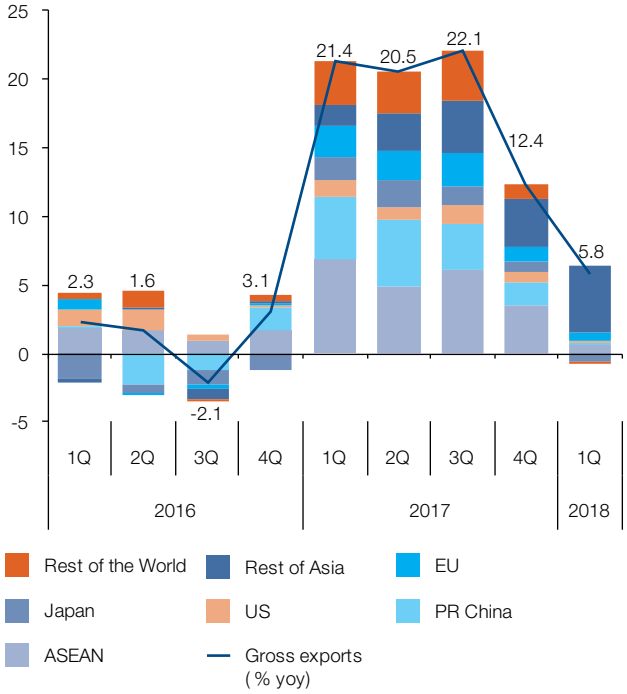


Source: Department of Statistics, Malaysia

Continued export growth to most major markets

Chart 14: Gross Exports by Markets

Annual change (%), contribution to growth (percentage points)



Source: Department of Statistics, Malaysia

Firm external sector performance

In 1Q 2018, gross exports expanded by 5.8% (4Q 2017: 12.4%), supported mainly by manufactured exports. The trade surplus rose to RM33.4 billion (4Q 2017: RM27.7 billion).

Export growth was supported by continued demand from key trading partners, particularly within the region. Manufactured exports moderated, but continued to register a strong growth of 8.2% (4Q 2017: 14.2%). Of note, semiconductor exports accelerated (29.6%; 4Q 2017: 24.4%) in line with continued expansion in the global technology upcycle. Both resource and non-resource based manufactured exports were also supportive of overall exports, driven mainly by chemical and metal products. Commodity exports contracted, owing to the decline in rubber and crude palm oil export prices, and lower LNG demand.

Gross imports declined by -0.8% during the quarter (4Q 2017: 14.4%). Intermediate imports were lower in line with more moderate manufactured export growth. Capital imports contracted amid lower delivery of high-value items compared to 1Q 2017. These weaknesses were partially offset by the strong growth in imports for re-export activity in Malaysia, particularly in the E&E sector.

Higher current account surplus

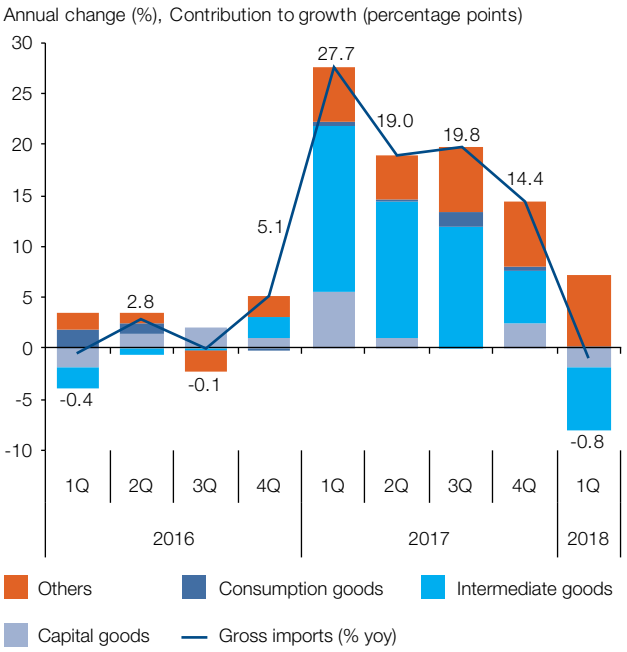
The current account surplus widened to RM15.0 billion in the first quarter of 2018 (4Q 2017: RM13.9 billion), or 4.5% of GNI (4Q 2017: 4.0% of GNI), due mainly to a higher goods surplus and lower services deficit. This was the highest quarterly current account surplus since 2Q 2014 when it reached RM15.3 billion. The secondary income account registered a smaller deficit, while the primary income account deficit widened during the quarter.

In tandem with continued strength in exports and more moderate imports during the quarter, the goods surplus[5] rose to RM35.7 billion (4Q 2017: RM34.1 billion). In the services account, the deficit moderated to RM5.8 billion (4Q 2017: -RM7.0 billion), owing mainly to lower net payments in the construction and transportation accounts.

The primary income account deficit widened to -RM10.2 billion (4Q 2017: -RM8.4 billion), largely attributable to lower profits earned by Malaysian firms investing abroad mainly in the finance and insurance and wholesale and retail trade services sub-sectors. The secondary income account recorded a deficit of RM4.7 billion (4Q 2017: -RM4.8 billion) due to continued outward remittances by foreign workers.

Gross imports declined slightly, weighed down by contractions in intermediate and consumption goods

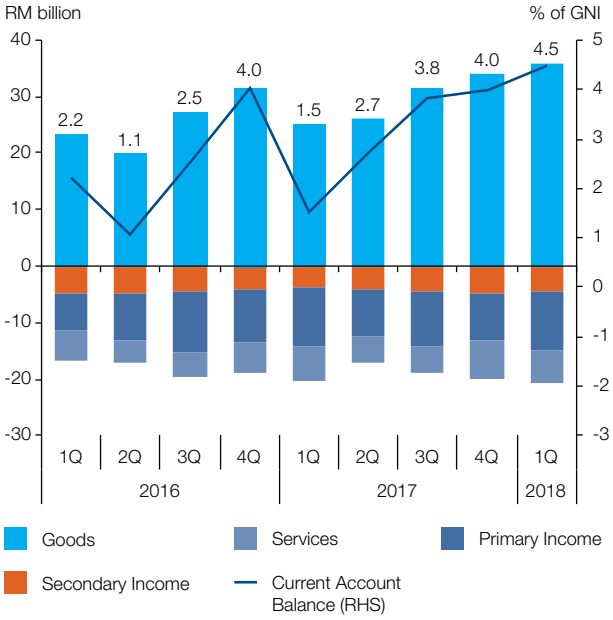
Chart 15: Gross Imports by Products



Source: Department of Statistics, Malaysia

Current account surplus widened

Chart 16: Current account balance

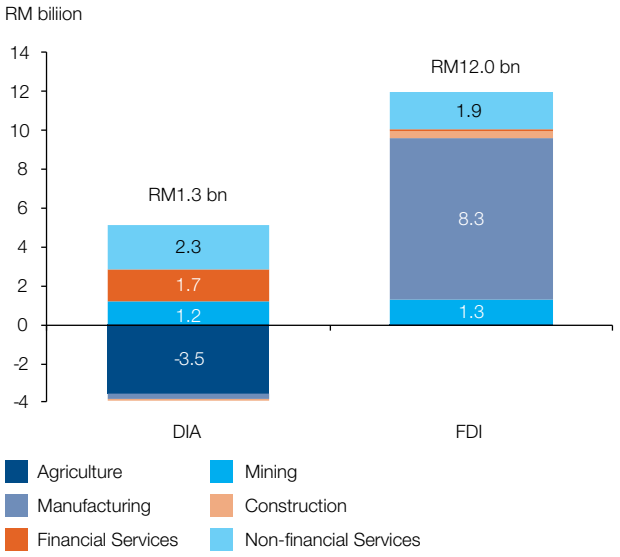


Source: Department of Statistics, Malaysia

[5] The difference between the goods surplus and trade surplus may arise from the exclusion of goods for processing, storage and distribution in the goods accounts as per the 6th Edition of the Balance of Payments and International Investment Position Manual (BPM6) by the IMF.

Significant foreign direct investments amid low direct investments abroad

Chart 17: Net Direct Investment Flows by Sector

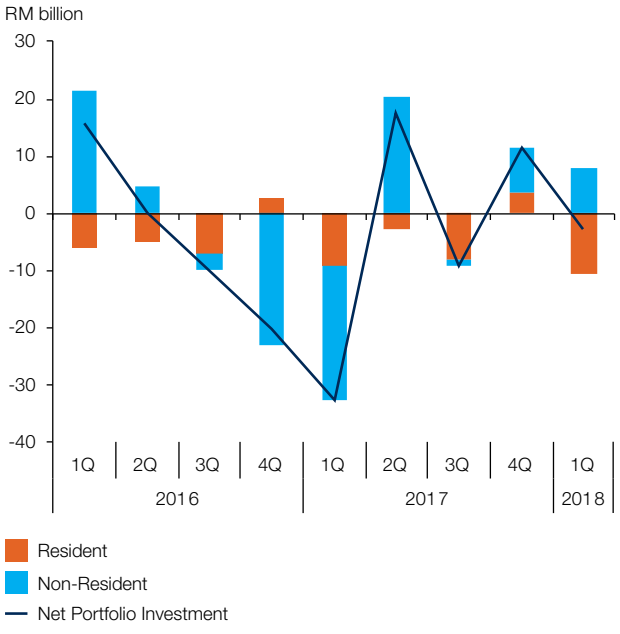


Note: For DIA, positive values refer to net outflows while negative values refer to net inflows

Source: Department of Statistics Malaysia and Bank Negara Malaysia

Net outflow in portfolio investment account contributed by residents

Chart 18: Portfolio Investments



Source: Department of Statistics Malaysia and Bank Negara Malaysia

Financial account recorded net inflows

In the first quarter of 2018, the financial account registered a net inflow of RM15.2 billion (4Q 2017: net inflow of RM6.0 billion). This was supported by continued foreign direct investments (FDI), non-resident portfolio investments, and other investment inflows. These inflows were partially offset by portfolio investments abroad by residents.

The direct investment account registered a net inflow of RM10.7 billion (4Q 2017: net inflow of RM5.3 billion), on account of strong FDI, amid low direct investments abroad (DIA) during the quarter. FDI registered a large net inflow of RM12.0 billion (4Q 2017: net inflow of RM3.4 billion), reflecting the successful formation of two joint ventures for the Refinery and Petrochemical Integrated Development (RAPID) project and continued investments by MNCs in the E&E sector. Following these developments, the majority of FDI inflows were channelled into the manufacturing sector, followed by the services sector, particularly the real estate and wholesale and retail trade sub-sectors. DIA by Malaysian companies recorded a small net outflow of RM1.3 billion (4Q 2017: net inflow of RM1.9 billion), as DIA outflows were partly offset by inflows following partial divestment of a specialty oils and fats manufacturing business in Europe. DIA outflows were channelled mainly into the services sector, particularly the real estate and financial services sub-sectors, followed by the mining sector.

The portfolio investment account registered a net outflow of RM2.6 billion (4Q 2017: net inflow of RM11.6 billion), attributed mainly to a resumption in net acquisitions of foreign financial assets by resident fund managers and banks (1Q 2018: net outflow of RM10.5 billion; 4Q 2017: net inflow of RM3.5 billion). This was partially offset by non-resident portfolio investments, which recorded a net inflow of RM7.9 billion (4Q 2017: net inflow of RM8.1 billion). Investor sentiments in the domestic financial markets continued to be supported by better-than-expected fourth quarter economic performance in 2017 and higher global crude oil prices during the quarter.

The other investment account turned around to record a net inflow of RM6.4 billion (4Q 2017: net outflow of RM9.5 billion), due mainly to the extension of short-term loans by non-residents. These inflows were partially offset by residents' loan extensions and placements of currency and deposits abroad. Net errors and omissions, excluding revaluation changes on international reserves[6], amounted to -RM12.0 billion or -2.7% of total trade. The international reserves of Bank Negara Malaysia amounted to USD107.8 billion as at end-March 2018, compared to USD102.4 billion as at end-December 2017.

[6] As part of ongoing efforts to enhance BOP reporting, quarterly net E&O now excludes reserves revaluation changes. This practice is backdated up to 1Q 2010.

Manageable external debt

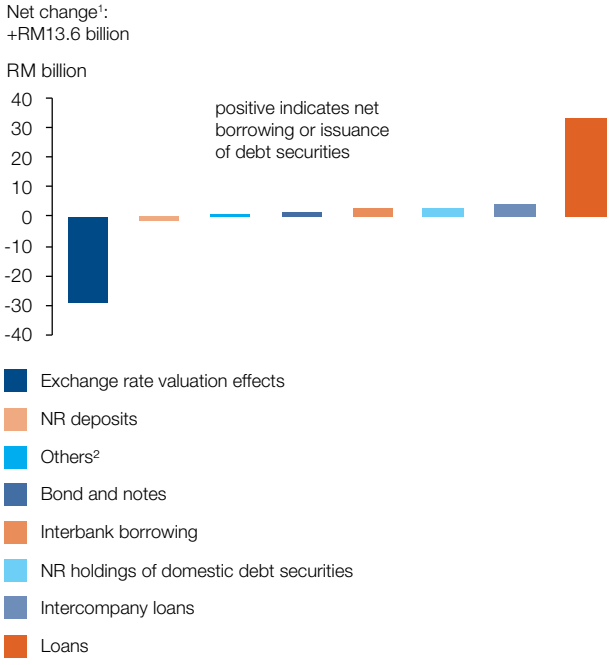
Malaysia's external debt amounted to RM893.4 billion, equivalent to USD229.0 billion or 61.8% of GDP as at end-March 2018 (end-December 2017: RM879.8 billion or USD214.6 billion or 65.0% of GDP). The higher external debt reflects the increase in loans by the non-financial corporations segment to finance investment activity. This was partially offset by valuation effects following the strengthening of the ringgit against selected major and regional currencies during the first quarter of 2018.

Malaysia's external debt remains manageable given its currency and maturity profiles, and the availability of large external assets. More than one-third of total external debt is denominated in ringgit (34.8%; end-December 2017: 34.4%), mainly in the form of NR holdings of domestic debt securities and in ringgit deposits in domestic banking institutions. As such, these liabilities are not subjected to valuation changes from the fluctuations in the ringgit exchange rate.

The remaining external debt of RM582.8 billion or 65.2% of total external debt is denominated in foreign currency (FC) and is subject to prudential liquidity management practices and hedging requirements on banking institutions and corporations. The bulk of these obligations are offshore borrowings, raised mainly to expand productive capacity and to better manage financial resources within corporate groups. As at end-March 2018, offshore borrowing stood at 35.8% of GDP (end-December 2017: 37%).

Higher external debt in 1Q 2018

Chart 19: Changes in External Debt

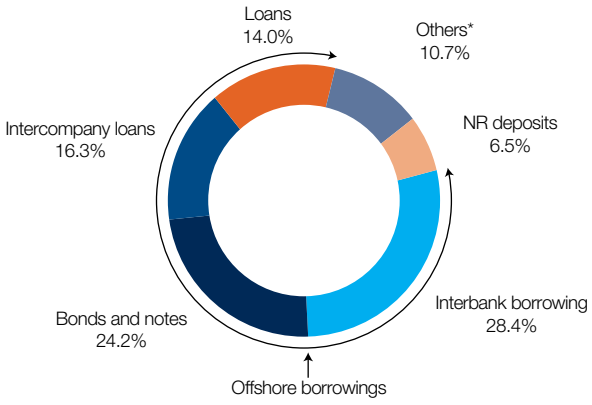


[1] Changes in individual debt instruments exclude exchange rate valuation effects
[2] Comprises trade credits, IMF allocation of SDRs and other debt liabilities
Note: NR refers to non-residents

Source: Ministry of Finance, Malaysia and Bank Negara Malaysia

FC-denominated debt subjected to prudent liquidity management practices and hedging requirements

Chart 20: Breakdown of Foreign Currency-denominated External Debt (% share)



*Includes trade credits and miscellaneous, such as insurance claims yet to be disbursed and interest payables on bonds and notes

Source: Ministry of Finance, Malaysia and Bank Negara Malaysia

Of the total FC-denominated external debt (inclusive of valuation effects), more than one-third (or amounting to RM202.9 billion) is accounted by interbank borrowing and FC deposits in the domestic banking system. This largely reflects the banks' intragroup liquidity management and placements of deposits from foreign parent entities, which are subjected to prudent liquidity management practices. Among these are internal limits on funding and maturity mismatches. This is followed by long-term bonds and notes issued offshore which amounted to RM141.2 billion as at end-March 2018, primarily to finance asset acquisitions abroad that will generate future income. The intercompany loans are typically on flexible and concessionary terms, such as no fixed repayment schedule or low interest rate.

From a maturity perspective, more than half of the total external debt is skewed towards medium- to long-term tenure (55.5% of total external debt; end-December 2017: 56.9%), suggesting limited rollover risks. Given the export earnings of borrowers and external assets, international reserves is not the only means for banks and corporations to meet their short-term external obligations. International reserves account for about a quarter of total external assets, with the remaining external assets being held by banks and corporations. As at 30 April 2018, international reserves is 1.1 times the short-term external debt and is sufficient to finance 7.5 months of retained imports.