QUARTERLY ECONOMY TRACKER

(JAN-MAR 2021)

Socio-Economic Research Centre (SERC)

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MALAYSIA’S QUARTERLY ECONOMY TRACKER (JAN-MAR 2021)

A. World Economic Situation and Prospects

GLOBAL ECONOMY RETURNS TO PRE-PANDEMIC LEVEL IN 2021

Global recovery continues amid uncertainty. Global economic prospects have improved in recent months, thanks to the rollout of vaccines, albeit at a different pace of vaccination across the globe, a gradual returning of economic normalcy as well as continued fiscal and monetary support amid high uncertainty about the path of the pandemic.

The International Monetary Fund (IMF) expects the world economy to grow by 6.0% in 2021, up from its 5.5% forecast in January. GDP for 2022 is seen increasing by 4.4%, higher than an earlier estimate of 4.2%. The OECD expects global GDP to grow by 5.6% this year, and continues the recovery with 4.0% growth in 2022.

Uneven pace of recovery in advanced economies. Given the different rates of vaccination amid the periodic new waves of infection across the globe, the United States is well placed to surpass its pre-COVID-19 GDP level this year, largely driven by President Joe Biden’s US$1.9 trillion coronavirus rescue package and continued recovery in the labour market. China, which was the only major economy registered positive growth (2.3%) in 2020, continued to register the strongest GDP growth of 18.3% yoy on record in 1Q 2021, due to robust consumer spending.

The economic recovery in Europe is still halting and uneven, reflecting the periodic infection waves and slow pace of vaccinations. Japan's economy has been picking up but any recovery is likely to be modest due to lingering caution over the COVID-19 pandemic. It is still confronting a resurgence in infections, prompting the authorities to enforce stricter measures against its spread.

Global economic indicators are on track. High frequency indicators such as global Purchasing Managers’ Index (PMI) readings for both the manufacturing and services continued to expand at a solid pace, thanks to rebounding activities, higher trade demand and reopening of the services sector. Industrial production has rebounded in most countries, contributing to firming commodity prices and robust international trade. Global semiconductor sales continued to grow at double-digit rates in January (13.2%) and February (14.7%) 2021, underpinned by increasing demand of digitalisation, data solutions and sensors, analog and logic products as well as the development of 5G technology.

Attendant risks to the global recovery. With still high uncertainty about the path of pandemic and uneven pace of vaccination rates between the advanced and developing economies with the latter experiencing slower rate of immunisation, the policy makers must continue to provide fiscal and monetary stimuli to ensure a durable recovery ahead.

The risks to temper global recovery are: (a) Pre-mature withdrawal of fiscal and monetary support measures; (b) New virus mutations could spark another wave of infections during the vaccination campaign or even prove resistant to the vaccines currently deployed; (c) Renewed trade and technology frictions between the US and China; (d) The unexpected rise in the US interest rate could pose financial risks, especially in emerging economies having high foreign currencies debt burden; (e) Sustained higher inflation due to the cost-push and demand-pull, compelling sooner-than-expected rise in policy interest rates; (f) Volatility in commodity prices; and (g) Geo-political tensions.

B. Malaysia's Economic and Financial Conditions

STEADY STRIDES TOWARDS RECOVERY BUT GROWTH IS UNEVEN

Continued scarring effects in 1Q 2021. The prolonged pandemic and re-implementation of less restrictive MCO 2.0, which was subsequently moved to targeted MCO/CMCO/EMCO/RMCO continued to have scarring effects on economic and business activities as well as consumer spending.

The Government has rolled out RM15.0 billion PERMAI and RM20.0 billion PEMERKASA economic packages in 1Q 2021 to ease the scarring effects on domestic demand. This, backed by the national immunisation program starting February, albeit moving at a slow pace, helped to lift sentiment.

The on-going national immunisation program holds the key to lift a sustained revival in consumer sentiment. Hence, the slowness in the rate of vaccination amid concerns over the occurrence of 4th wave, prompting more targeted MCO/EMCO are expected to have prolonged scarring effects on economic and business activities. At the time of writing, new infected cases continue to stay stubbornly high above 2,000 since 15 April and continuously rising to breach 3,000 daily cases in recent days.

As long as the movement restrictions are less restrictive, the chances of a complete stalling of economic recovery are unlikely as the extreme "low base" effect in 2Q 2020 will give a strong lift to growth bouncing back in 2Q 2021. But we caution that 1Q 2021 could still be a sluggish growth and growth will turn positive from 2Q onwards though the magnitude of economic growth increases will depend greatly on the progress made in the immunisation program.

SERC maintains its GDP growth estimates of 4.0% (base case) and 6.0% (upside) for 2021 amid continued economic scarring effects from the movement restrictions and restricted inter-state travel ban.

Domestic demand is recovering. The pent-up demand and consumption booster measures, such as EPF withdrawals, cash handouts as well as the drawdown of savings that were unspent during the pandemic have helped to revive discretionary consumer spending. Footfall in the malls and shops as well as the number of patrons in restaurants, fashion and wearing apparel outlets have recovered though the sales still some generally 20-30% below pre-pandemic level. Purchase of durable goods, such as passenger cars and commercial vehicles increased by 28.8% yoy and 70.5% respectively in 1Q 2021, reflecting partly the rush for deliveries by companies meeting their financial year ending 31 March 2021; new model launches; and a low base in March 2020 due to the MCO. Imports of consumption goods grew by 10.1% in 1Q 2021. Household loans demand grew by 5.7% in March 2021 (3.7% in March 2020).

Nevertheless, we caution that a slow and moderate recovery in the labour market (unemployment rate of 4.8% at end-Feb 2021) and continued high loss of employment (24,688 persons in 1 Jan-25 Apr 2021 as compiled by the EIS) would cap consumer spending. In addition, the wearing off effect of consumption-fuelled catalysts would pull the brake on consumer spending towards end-year and in 2022.

We expect private investment to revive gradually (estimated 5.1% in 2021) this year from a decline of 11.9% in 2020, supported largely by investment in the manufacturing sector, especially the expansion of capacity in electronics and electrical products as well as rubber products.

Mixed pace of recovery in economic sectors. Manufacturing sales have increased by 5.3% in Jan-Feb 2021, underpinned by higher output of electronics and electrical products, food products, as well as rubber and plastic products. The services sector still slowly on the mend

– the wholesale and retail trade continued to decline by 0.2% and 2.3% respectively in Jan-Feb 2021. Some travel and tourism-related sub-services sectors would recover gradually and may take a longer while to fully restore their growth traction, depending on a complete lifting of inter-state travel restrictions and the reopening of Malaysia's international borders to travellers and tourists.

Exports continued to gain strong traction. Riding on the recovery in global demand and higher commodity prices (palm oil and crude oil), Malaysia's exports have expanded robustly by 31.0% in March (17.6% in Feb; 6.6% in January). The main drivers were electronics and electrical products, rubber products, chemicals, and manufactures of metal and palm oil-based products. Exports are expected to increase by 9.0% in 2021 (-1.4% in 2020), underpinned by sustained demand of semiconductors and machinery equipment in tandem with increasing digitalisation and 5G technology development.

Cost-induced factors to push inflation higher. After mired in persistent deflation (negative CPI) for eleven months in a row, headline consumer inflation increased by 1.7% in March (0.1% in Feb; -0.2% in Jan), largely due to moderate decrease in fuel prices, and higher prices of food items, alcoholic beverages, and furnishing & household equipment.

Cost-push inflation will be calling the shots in 2021 amid still mending domestic demand. Headline consumer price index (CPI) will be getting normal from a depressed base in 2020. Much of short-term inflation pressure is a gradual normalisation of unusual disparities in supply and demand brought about by the COVID-19 pandemic, as domestic demand and economic activity recovers. **SERC estimates inflation to increase by 3.0%-4.0% in 2021** (-1.2% in 2020).

We contend that higher fuel prices at the pump may cause public to begin behave as though inflation is occurring given a sharp rise in the price of Brent crude oil since the last quarter of 2020. The base effect of rising energy costs will work on the transport prices.

Although economic activity has recovered gradually, the economy is likely to have spare capacity as a result of the COVID-19 pandemic. The economy's output to remain below its potential level for some time. A number of factors will influence how that spare capacity affects inflation, including the frequency of price changes across different sectors.

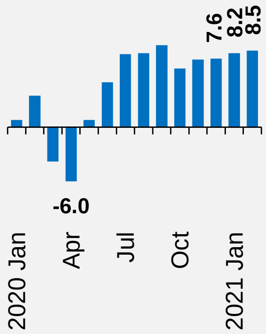
Core inflation number and other price indicators bear close tracking. The central bank has to keep a watchful eye on cost-push inflation for now, to anchor forward inflation expectations. This is to safeguard against the occurrence of unrelenting wage demand inflation when the workers asking for wage rise to compensate for rising cost of living.

BNM reaffirms no change in the monetary policy stance. Despite the central bank's projected higher cost-driven inflation (2.5%-4.0% in 2021), albeit a temporary spike to above 5.0% in 2Q due to low base effect, **we expect Bank Negara Malaysia (BNM) to hold the overnight policy rate steady at 1.75% till end-2021**. Given the moderate price pressures amid continued spare capacity in the economy, BNM reaffirmed that monetary policy will not be the most appropriate tool to manage supply-driven inflation.

Decisions on monetary policy will continue to be data-driven. The central bank will continue to closely monitor the emergence signs of a more entrenched and sustainable economic recovery in the period ahead, while keeping vigilant watch against a build-up of financial imbalances.

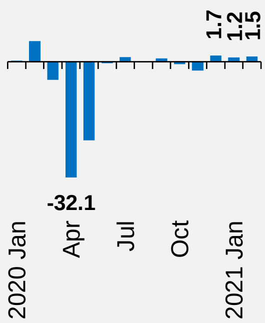
SNAPSHOTS OF MALAYSIA'S ECONOMIC RECOVERY TRACKER

Leading index (LI)
(%, YoY)



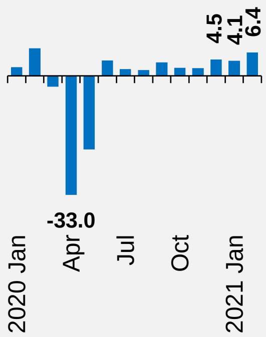
- The LI, a gauge of forward economic growth increased at a quicker pace of 8.2% in January 2021, indicating the near-term economic prospects remain upbeat, aided by the starting of vaccine inoculation program.

Industrial output
(%, YoY)



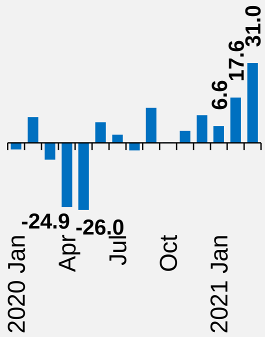
- Expanded by low single-digit growth for three months in a row since Dec 2020.
- Manufacturing output growth remained healthy (4.5% in Feb and 3.5% in Jan 2021 vs. pre-pandemic's 3.6% in 2019).
- Continued decline in mining and electricity output.

Manufacturing sales
(%, YoY)



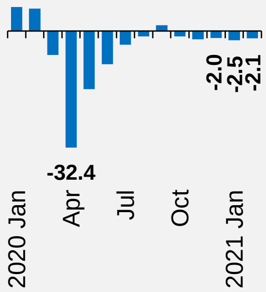
- Continued its expansion trail in Jan-Feb 2021, backed by solid increases in food products, pharmaceutical products, rubber products, motor vehicles as well as electronics and optical products.
- Partially offset by decreased sales in refined petroleum products and wood products (excluding papers and furniture).

Exports
(%, YoY)



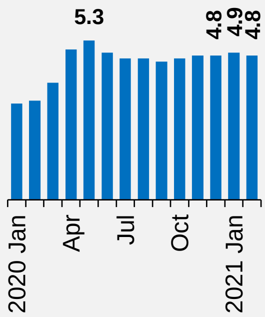
- Still going strong on recovering global demand.
- Strong demand of electrical and electronic (E&E) products, rubber and rubber products, manufactures of metal, as well as palm oil and palm-based products.
- **Exports are projected to bounce back by 9.0%** in 2021 (-1.4% in 2020), riding on recovery in global demand and higher commodity prices.

Retail sales
(%, YoY)



- Retail sales continued to decline for five consecutive months since the resurgence of a third wave of the pandemic.
- Cautious consumer sentiments given a slow recovery in the jobs market. Discretionary consumer spending has picked up.

Unemployment rate
(%)

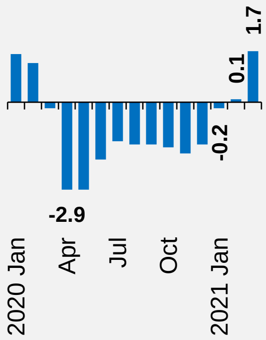


- The labour market conditions still weak and slowly on the mend.
- The Employment Insurance System (EIS)'s loss of employment registered a total of 107,024 in 2020, 267.0% higher than 2019. As of 25 Apr 2021, 24,688 employees have lost their jobs.

- The closing of international border remains a dampener on the travel, tourism and aviation industry; inter-state travel restrictions also weigh on the retail market.

- **The unemployment rate will gradually improve to an estimated 4.5% at end-Dec 2021**, translating a near 720,000 unemployed persons, about 40% higher than nearly 520,000 unemployed persons pre-COVID-19.

Headline inflation
(%, YoY)



- The eleventh continuous month of deflation starting March 2020 has ended in February (+0.1% yoy) and March 2021 (+1.7%), marking the highest rate since May 2018.
- Cost-push inflation remains in focus. Expect consumer inflation to soar higher in April and May 2021 due to extreme low base effect, higher fuel and food prices before moderating starting June. Real inflation pressures have increased.
- **Inflation is expected to increase by 3.0%-4.0% in 2021** (-1.2% in 2020), largely boosted by a relatively lower fuel price-induced low base effect in 2020, higher fuel and food prices as well as the lapse of electricity discount.

Source: Department of Statistics, Malaysia

WORLD ECONOMIC SITUATION AND PROSPECTS

GLOBAL ECONOMY RETURNS TO PRE-PANDEMIC LEVEL IN 2021

Global recovery on track amid high uncertainty about the path of pandemic. The International Monetary Fund (IMF) and Organisation for Economic Co-operation and Development (OECD) have raised optimism prospects of the global recovery in 2021, thanks to the rollout of vaccines. We see sharply divergent growth prospects across various regions due to the different vaccination rates as the developing countries were slow in getting the supply of vaccines.

Divergences in restarting trajectories are becoming more apparent. The progress of vaccination and attendant hopes of a rapid and broad-based recovery have been tempered by a fresh COVID-19 wave sweeping through a number of economies, putting their growth trajectory at risk.

Both the US and China will be the main drivers of global growth in 2021, underpinned by pent-up household consumption and revived business investment. The US economy is in pole position as its vaccine rollout accelerates. China's factory and consumer activity have returned largely to normal following the coronavirus pandemic. Japan's recovery remains uneven on the periodic waves of infection. Both the core and periphery of the eurozone are struggling as they cope with another wave of COVID-19 infections, floundering vaccination programs, and a lack of policy direction.

Global economic recovery tracker. High frequency global economic indicators showed a revival in economic and business activities as well as trade flows.

a) The **OECD composite leading indicators** (CLIs), which is designed to anticipate turning points in economic activity relative to trend, continue to strengthen in most major economies, including the US, China, Japan and euro area as a whole.

b) **Global Purchasing Managers Index (PMI) for manufacturing and services** rose higher, marking one of their best reading over the past decades. Global economic recovery accelerates as reflected in the continued expansion of both manufacturing PMI (55.0 in March 2021, highest since April 2011) and services PMI (54.7 in March 2021, highest since February 2018), underpinned by strengthened new business intakes, improved job creation and brighter business optimism.

c) **Global trade volume and industrial production** growth have returned to positive territory with a record-high index registered in January 2021, supported by increasing global demand during the recovery phase. The World Trade Organization (WTO) expects world trade volume to increase by 8.0% in 2021 and 4.0% in 2022 after fallen by 5.3% in 2020. Notably, global chips shortage may disrupt some downstream production in 2021.

d) **Global semiconductor sales** continue its strong upward trend (14.7% yoy in February and 13.2% in January 2021; 8.0% in 4Q 2020), attributable to stronger sales of sensors, logic and memory products. The World Semiconductor Trade Statistics (WSTS) projects semiconductor sales to grow robustly by a double-digit of 10.9% in 2021 (6.8% in 2020) on a broad-based products and regional contributions.

e) **Commodity prices continue to trend up strongly.** The energy price index surged by 90.1% yoy (or 35.3% qoq) in March 2021, thanks to a recovery in global demand amid continued production cut. The average price of Brent crude oil rose to US$65.19 per barrel (bbl) in March 2021 from US$49.87/bbl in December 2020. Since April 2020, the OPEC+ has reduced global oil supply by 2.6 billion barrels by end-February 2021. The U.S. Energy Information Administration (EIA) projects that Brent crude oil price to average US$62.28/bbl in 2021 (49.4% higher than US$41.69/bbl in 2020) in its monthly Short-Term Energy Outlook (STEO) in April.

Prices of non-energy commodities also rose on a solid uptrend, with the price index soaring higher by 34.8% yoy (or 11.8% qoq) in March 2021. Reflecting a relatively lower production and inventory level, crude palm oil prices have breached a record high of RM4,428.50 per metric tonne (mt) on 23 April 2021, bringing the year-to-date average price of RM3,990/mt as at 26 April 2021. This represented an increase of 48.6% from an average of RM2,685.50/mt in 2020. With demand picking up, it is expected that the price level will remain high in coming quarters.

Table 1: Real GDP growth (% YoY)

	2019	2020	2020 Q1	2020 Q2	2020 Q3	2020 Q4	2021*f* (IMF)	2021*f* (WB)
World	2.8	-3.3	N/A	N/A	N/A	N/A	6.0	4.0
United States	2.2	-3.5	0.3	-9.0	-2.8	-2.4	6.4	3.5
Euro Area	1.3	-6.6	-3.3	-14.6	-4.2	-4.9	4.4	3.6
China	6.1	2.3	-6.8	3.2	4.9	6.5	8.4	7.9
Japan	0.3	-4.8	-2.0	-10.3	-5.8	-1.4	3.3	2.5
India	4.0	-8.0	-3.0	-24.4	-7.3	0.4	12.5	5.4
Malaysia	4.3	-5.6	0.7	-17.1	-2.6	-3.4	6.5	6.7
Singapore	1.3	-5.4	0.0	-13.3	-5.	-2.4	5.2	N/A
Indonesia	5.0	-2.1	3.0	-5.3	-3.5	-2.2	4.3	4.4
Thailand	2.4	-6.1	-2.1	-12.1	-6.4	-4.2	2.6	4.0
Philippines	6.1	-9.6	-0.7	-17.0	-11.6	-8.3	6.9	5.9
Vietnam	7.0	2.9	3.7	0.4	2.6	4.5	6.5	6.7

Note: *World GDP growth for 2019 and 2020 by IMF; Annual GDP for India is on fiscal year basis; N/A = Not applicable or not available*

Source: *Officials (unadjusted data except quarterly GDP for Euro Area); IMF (World Economic Outlook (WEO), Apr 2021); World Bank (Global Economic Prospects, Jan 2021)*

Loosened monetary stance still needed. The continued monetary accommodation is needed until the global recovery is firmly underway amid a pick-up in inflation. The premature withdrawal of interest rate easing would risk tempering the pace of recovery. The normalisation of interest rates in major advanced economies, if any probably starting late 2021 or 2022 will be on a measured pace.

Rising US treasury yields, a steepening yield curve (2Y-10Y) and inflation expectations are leading markets to expect the Federal Reserve (Fed) may resume a normalisation of interest rate sooner than expected. We see a low risk of the Fed taking pre-emptive measures to stop its buying programme in the next 12 months. The Fed will remain cautious and downplay inflation risks.

Despite the US economy is heading for its strongest growth in nearly 40 years, the Fed is pledging to keep her foot on the gas despite an expected surge of inflation, which is temporary and also largely low base effect.

We expect central banks in emerging Asia to maintain their current easy monetary policies.

It must be mindful that keeping interest rates low for a prolonged period can lead to over-indebtedness of the economy, overvalued asset prices and undervalued risks, misallocation of resources and credit, and lower overall productivity. As at end-September 2020, total global credit of non-financial sector-to-GDP ratio has shot up to 251.9% (225.3% as at December 2019), of which government credit to GDP ratio has breached 100% to 103.7% (86.5% as at

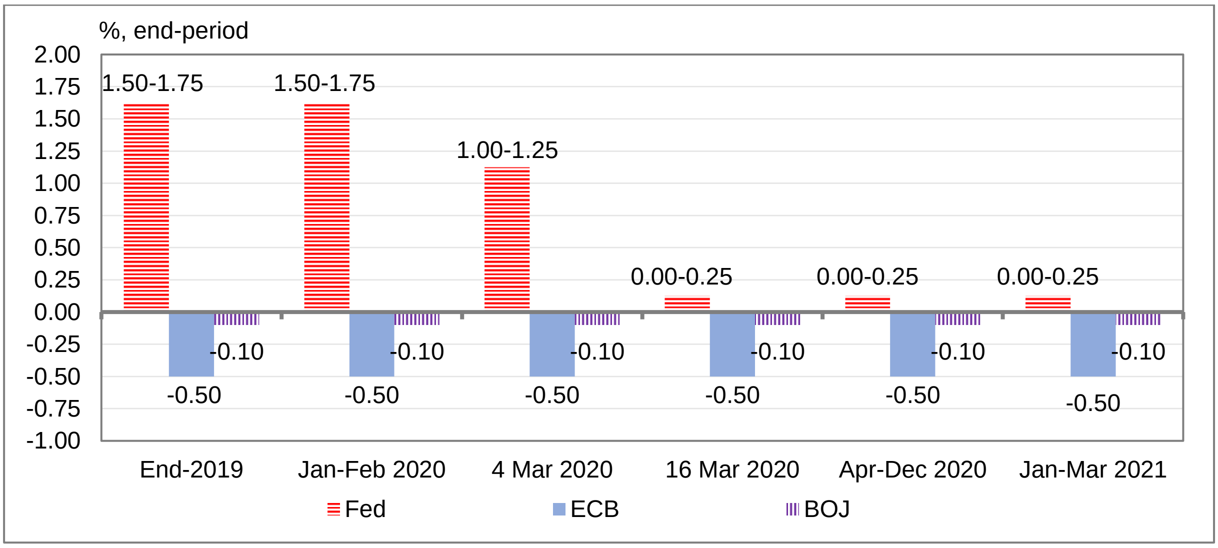
December 2019) given the sizeable amount of stimulus packages rolled out to combat the COVID-19 impact.

Table 2: Policy rate (%)

End-period of	2008	2009	2010	2011	2012	2016	2017	2018	2019	2020	2021 (Apr)	2021*f*
US, Fed Federal Funds Rate	0.00-0.25	0.00-0.25	0.00-0.25	0.00-0.25	0.00-0.25	0.50-0.75	1.25-1.50	2.25-2.50	1.50-1.75	0.00-0.25	0.00-0.25	0.00-0.25
Euro Area, ECB Deposit Facility	2.00	0.25	0.25	0.25	0.00	-0.40	-0.40	-0.40	-0.50	-0.50	-0.50	-0.50
Japan, BOJ Short-term Policy I/R	0.10	0.10	0.00-0.10	0.00-0.10	0.00-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10
China, PBC 1-Year Loan Prime Rate	5.31	5.31	5.81	6.56	6.00	4.35	4.35	4.35	4.15	3.85	3.85	3.85
India, RBI Policy Repo Rate (LAF)	6.50	4.75	6.25	8.50	8.00	6.25	6.00	6.50	5.15	4.00	4.00	4.00
Korea, BOK Base Rate	3.00	2.00	2.50	3.25	2.75	1.25	1.50	1.75	1.25	0.50	0.50	0.50
Malaysia, BNM Overnight Policy Rate	3.25	2.00	2.75	3.00	3.00	3.00	3.00	3.25	3.00	1.75	1.75	1.75
Indonesia, BI 7-Day RR Rate	9.25	6.50	6.50	6.50	5.75	4.75	4.25	6.00	5.00	3.75	3.50	3.50
Thailand, BOT 1-Day Repurchase Rate	2.75	1.25	2.00	3.25	2.75	1.50	1.50	1.75	1.25	0.50	0.50	0.50
Philippines, BSP Overnight RR Facility	5.50	4.00	4.00	4.50	3.50	3.00	3.00	4.75	4.00	2.00	2.00	2.00

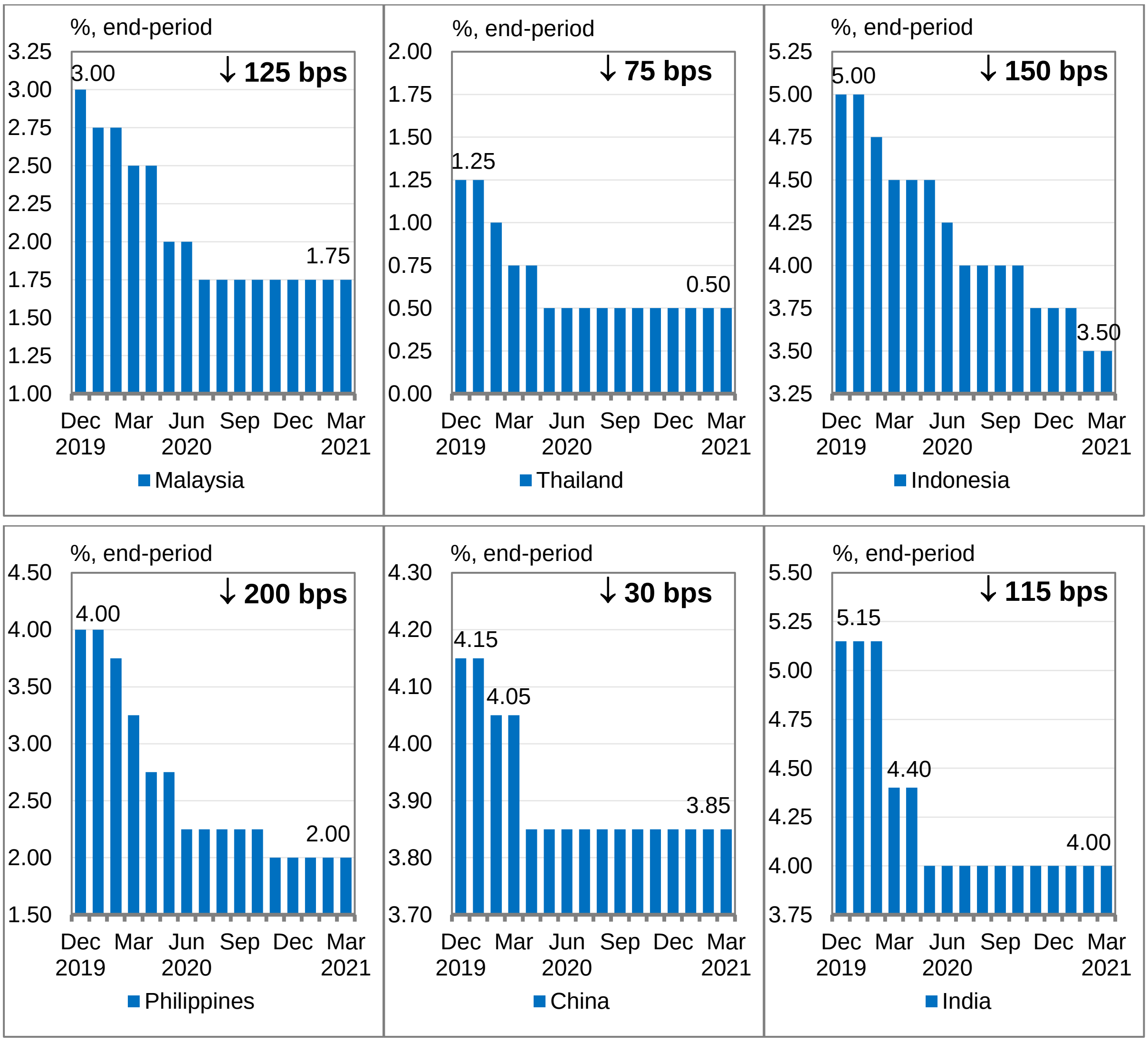
Source: Officials; SERC

Figure 1: Policy rate movements of major central banks



Source: Federal Reserve (Fed); European Central Bank (ECB); Bank of Japan (BOJ)

Figure 2: Policy rate movements of selected regional central banks



Source: Bank Negara Malaysia; Bank of Thailand; Bank Indonesia; Bangko Sentral ng Pilipinas; People's Bank of China; Reserve Bank of India

CURRENT AND FORWARD INDICATORS

Figure 3: CLIs continued to strengthen in most major economies

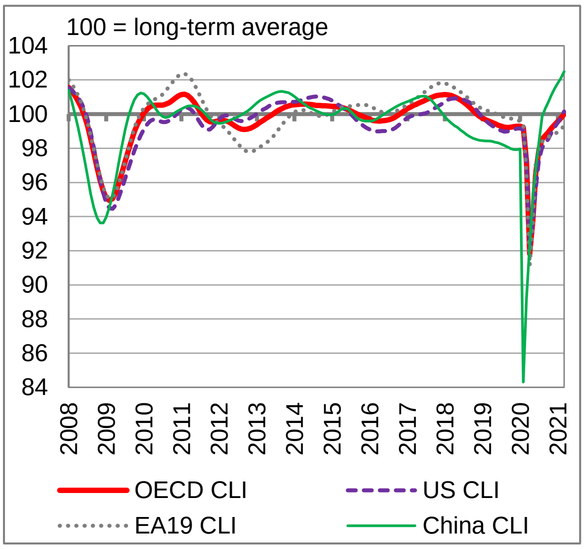
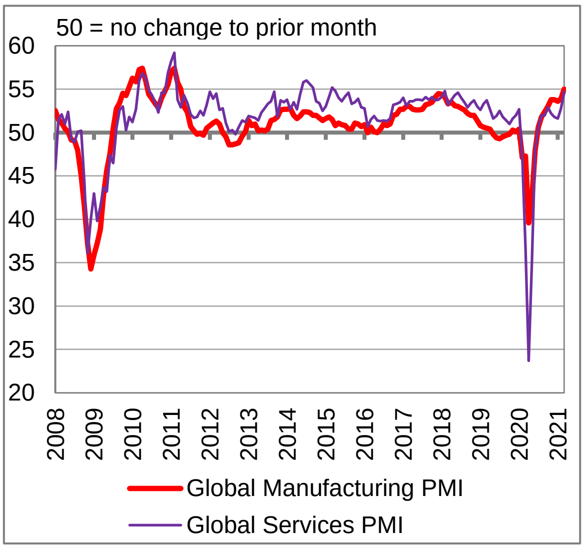


Figure 4: Global manufacturing and services activities are expanding steadily



Source: OECD; Markit

Figure 5: World trade volume and industrial production growth on a solid recovery track

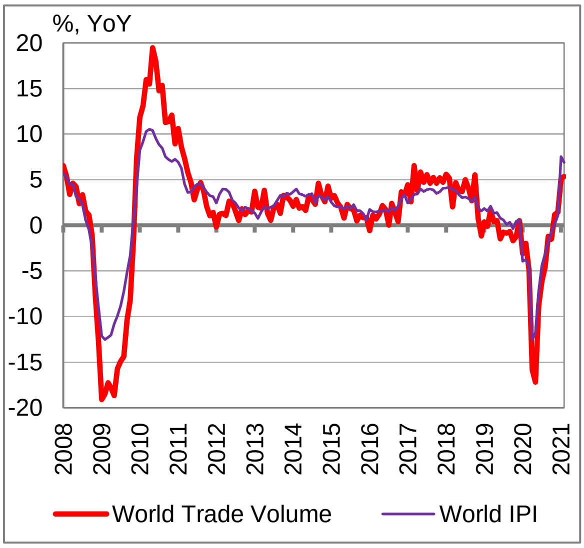
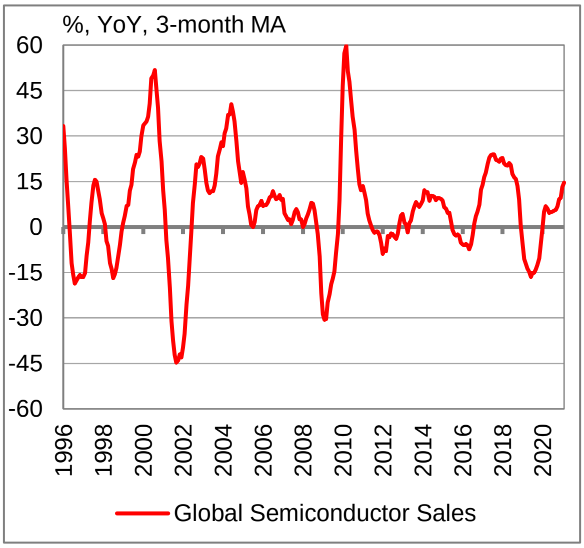


Figure 6: Global semiconductor sales growth sustained its upcycle trend



Source: CPB Netherlands Bureau for Economic Policy Analysis; Semiconductor Industry Association (SIA)

Figure 7: OECD Business Confidence Index

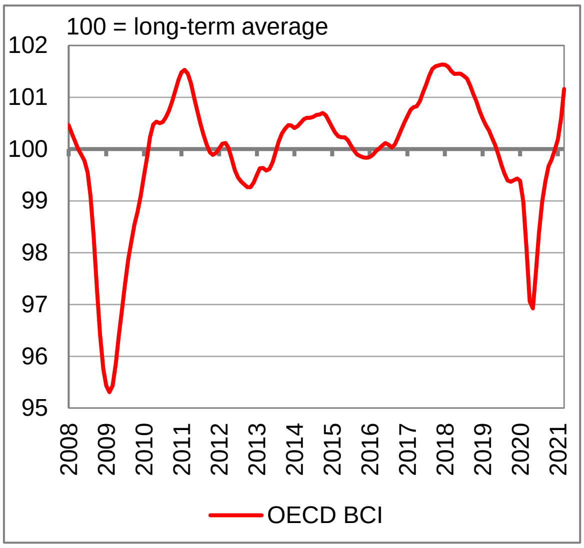
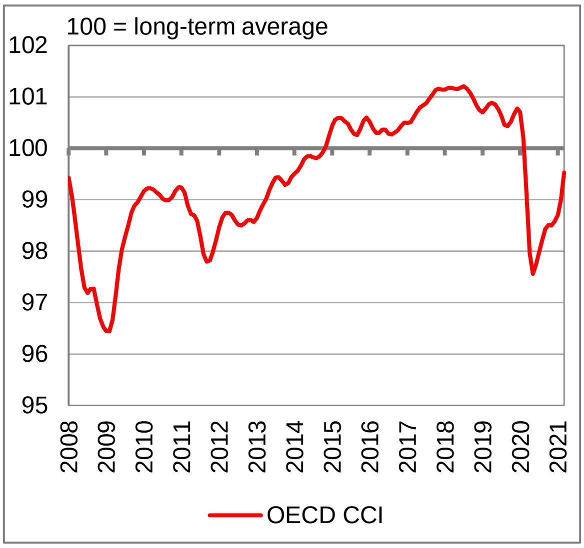


Figure 8: OECD Consumer Confidence Index



Source: OECD

Figure 9: Crude oil prices have returned to US$60/bbl level after crashing in 2020

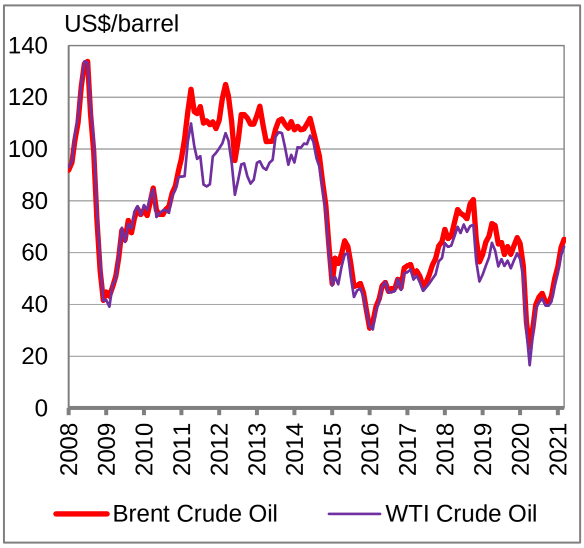
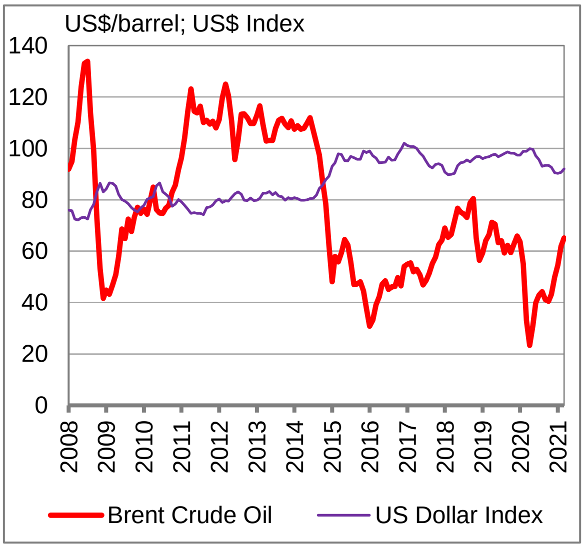


Figure 10: Brent crude oil price vs. the US dollar index



Source: World Bank; The Wall Street Journal

Figure 11: Prices of both energy and non-energy commodities moving higher

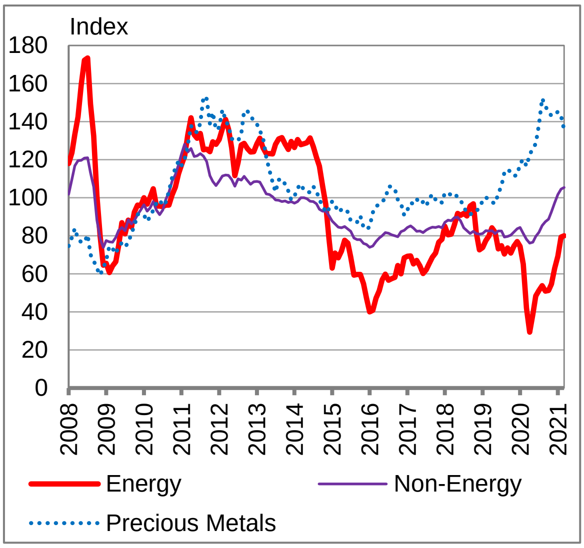
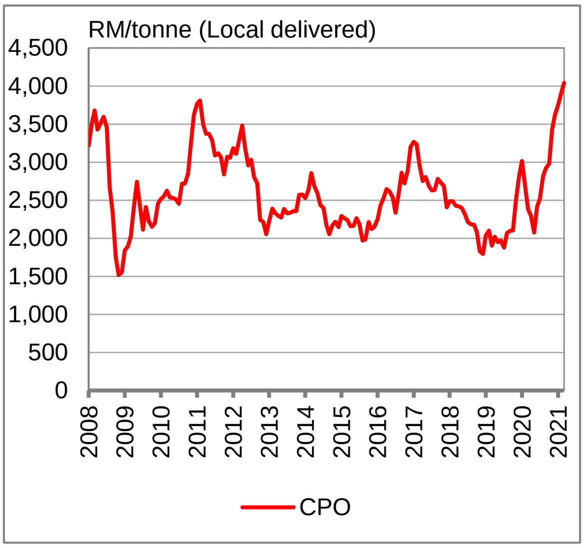


Figure 12: CPO prices have breached an all-time high in Apr 2021



Source: World Bank; Malaysian Palm Oil Board (MPOB)

ECONOMIC DEVELOPMENTS IN MAJOR ECONOMIES

The United States: The US economy soared to an annualised 6.4% qoq in 1Q 2021 (0.4% yoy vs. 4.3% qoq and -2.4% yoy in 4Q 2020), powered by consumer spending on stimulus checks, increased fixed residential and non-residential investment and government spending. With the approval of US$1.9 trillion stimulus bill, together with the potential upcoming packages (i.e., American Jobs Plan and American Families Plan) worth another few trillion dollars have fuelled market optimism. In March 2021, industrial production growth finally broke its 18-month contraction trend while retail sales continued booming, lifted by the stimulus check. The vaccination progress remains on track with more than 200 million doses have already been administrated. Despite the economic recovery is getting stronger, the Fed is unlikely to change its monetary stance in the near future.

Figure 13: ISM manufacturing PMI rises to multiple-decade high in Mar 2021; services PMI also hit all-time high

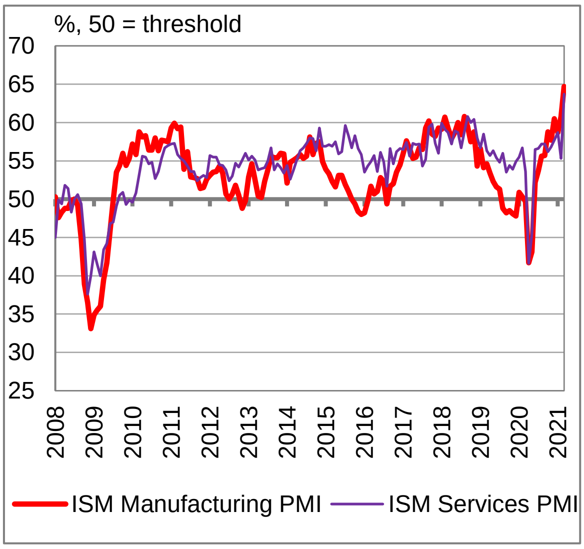


Figure 14: Consumer spending surged in Mar 2021, helped by Biden's stimulus checks

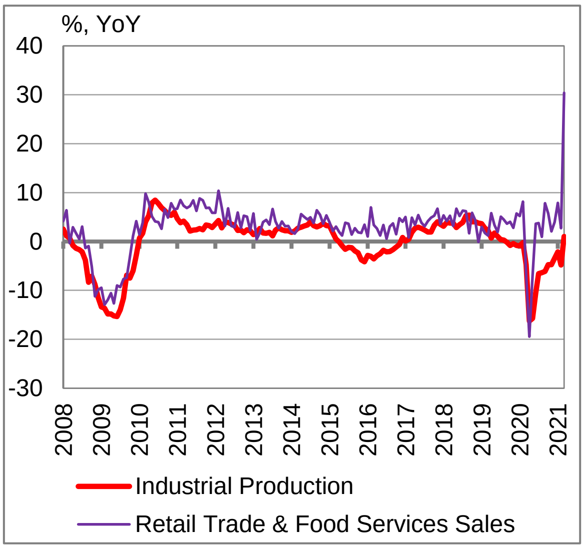


Figure 15: Jobless rate improved further to 6.0% in Mar 2021

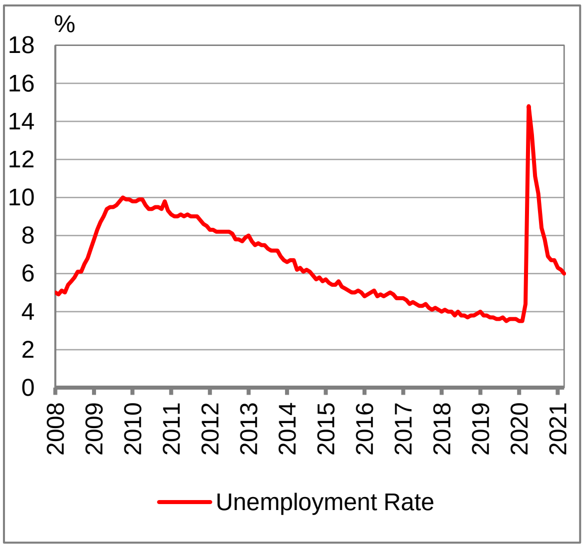
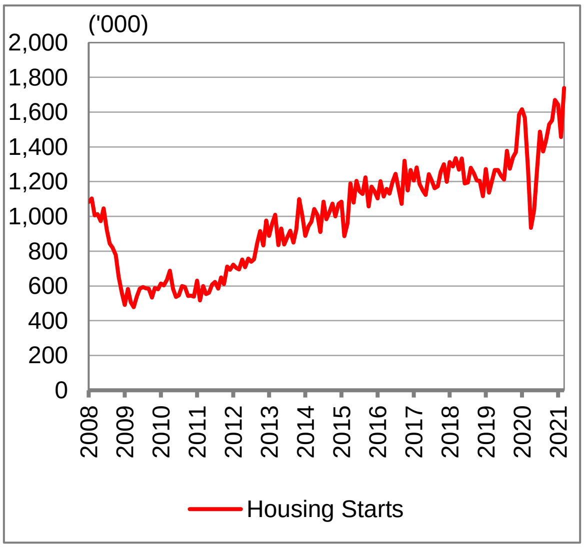


Figure 16: Housing starts rebounded sharply in Mar 2021 to a new high since Jun 2006



Source: Institute for Supply Management (ISM); Federal Reserve System; US Census Bureau; US Bureau of Labor Statistics

Euro area: The re-imposition of containment measures has pulled back the recovery strength of Eurozone in 4Q 2020 and the scarring effects will be continued in 2021. The euro area falls into another technical recession as GDP contracted by 0.6% qoq (or -1.8% yoy) in 1Q 2021 and 0.7% qoq (or -4.9% yoy) in 4Q 2020, dragged by unfavourable private consumption activities. Incoming data showed that the manufacturing sector may turnaround, but services activities remained sluggish, while exports still yet to recover back to pre-pandemic level. The European Central Bank expects to step up the pandemic emergency purchase programme (PEPP), pushing to a deepening of ultra-loose monetary policy.

Figure 17: Manufacturing PMI hit a record high in Mar 2021; services PMI remains stuck below the 50-pt threshold

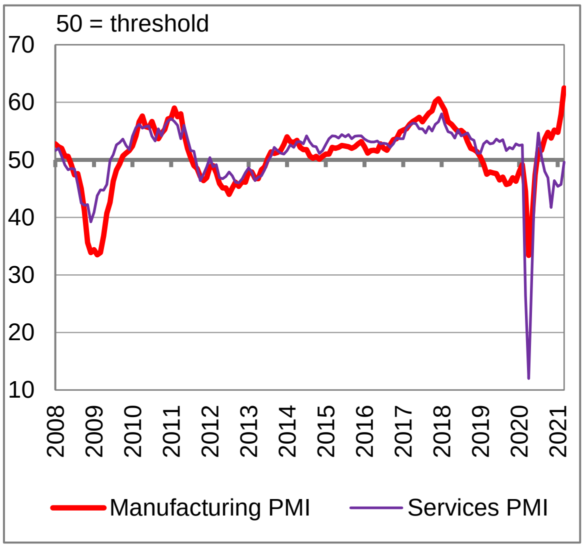


Figure 18: Both industrial production and retail trade showed mixed performance

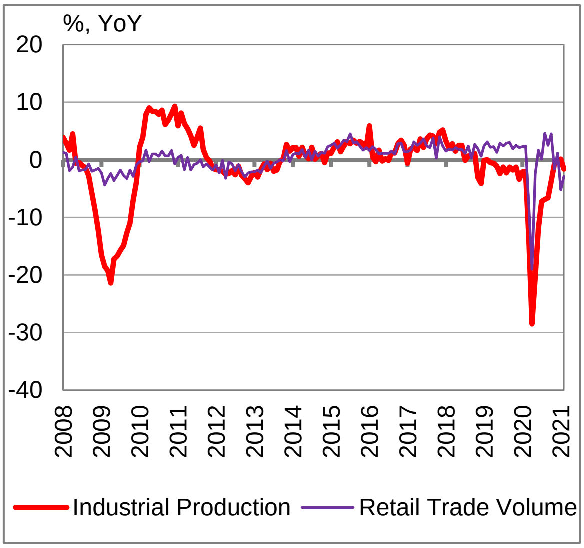


Figure 19: March's headline inflation contributed by higher services and energy prices

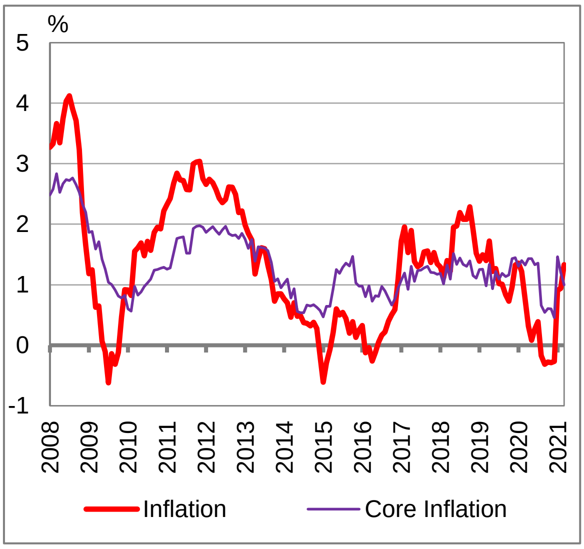
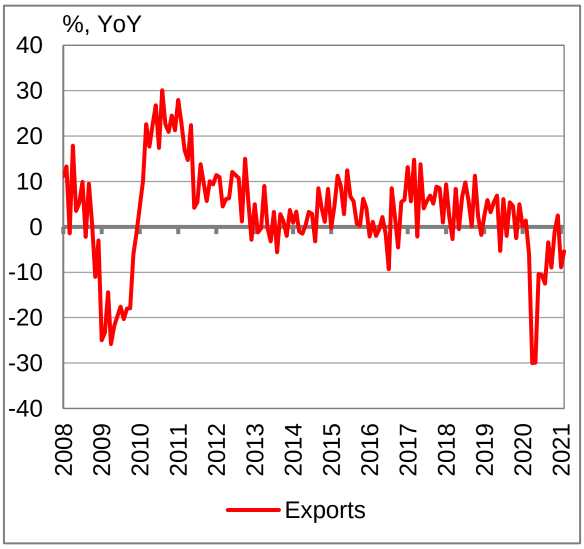


Figure 20: Exports are crawling back to pre-pandemic level



Source: Markit; Eurostat

Japan: The Japanese economy grew by 2.8% qoq (-1.4% yoy) in 4Q 2020, continued its recovery trend from the pandemic, thanks to a rebound in exports and private consumption. Industrial output declined by 2.1% in February 2021 due to a shortage of global chips that has forced automakers to cut production while a strong earthquake has disrupted the supply of parts for major automakers. Inflation level remains far from the targeted 2%. Following the declaration of the third state of emergency in Tokyo and Osaka, it is expected that a prolonged weak economic performance in the first half-year of 2021.

Figure 21: TANKAN indicates that manufacturers have turned more optimistic in 2021

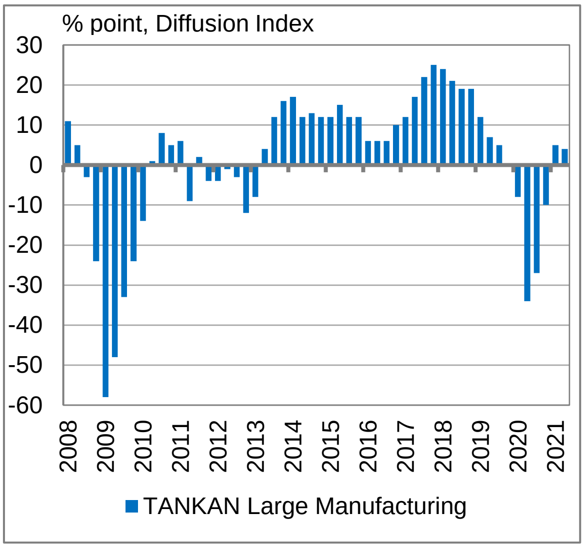


Figure 22: Industrial production contracted for 17 months; retail sales declined for 3 straight months in Mar 2021

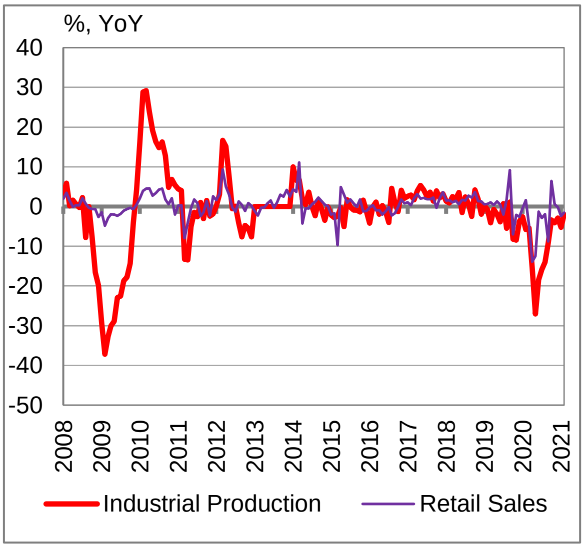


Figure 23: Deflation for the sixth consecutive month, though core inflation has reverted to positive territory

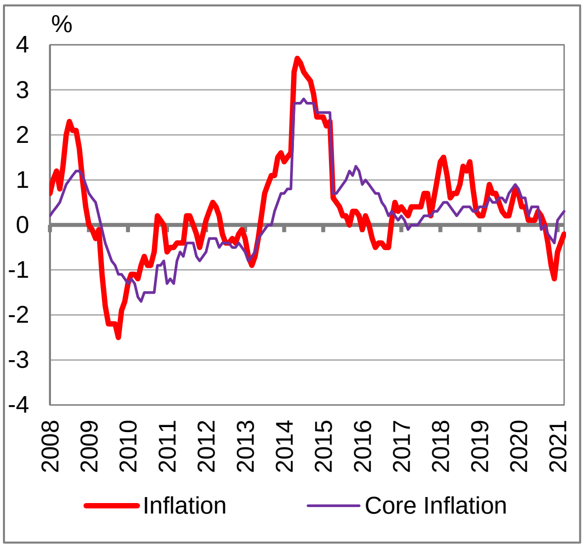
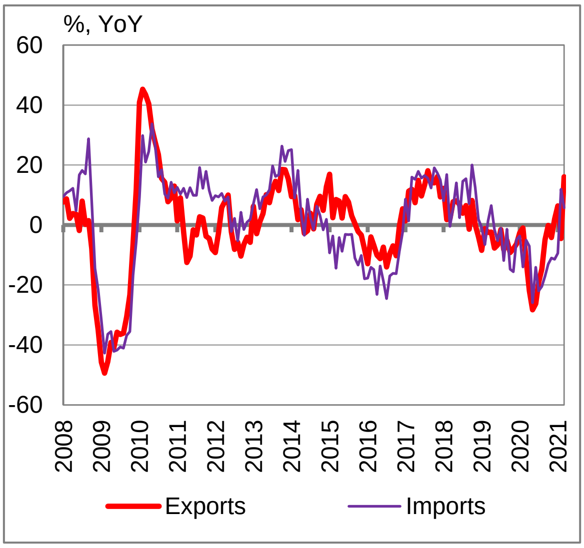


Figure 24: Exports grew strongly in Mar to 7.4 trillion yen, highest since Mar 2018



Source: Bank of Japan (BOJ); Ministry of Economy, Trade and Industry (METI), Japan; Japan Customs; Statistics Bureau, Japan

China: The Chinese's economy has proven its robust recovery from the COVID-19 pandemic to record a double-digit growth of 18.3% yoy in 1Q 2021 (+6.5% in 4Q 2020; +2.3% in 2020), well above its pre-pandemic level, driven by broad-based factors. For 2021, China's Government targets GDP growth to expand over 6%. Both manufacturing and services PMI remained in expansionary mode for 13 months in a row. High frequency data indicates a strong start in 2021. Price level has climbed back to a marginal inflation in March (0.4%) after slipping into deflation for two months in Jan-Feb 2021. On the labour market conditions, the Government sets the urban unemployment rate within 5.5% in 2021, with new employment opportunities of more than 11 million.

Figure 25: Both PMI readings signalled continued expansion for 13 straight months

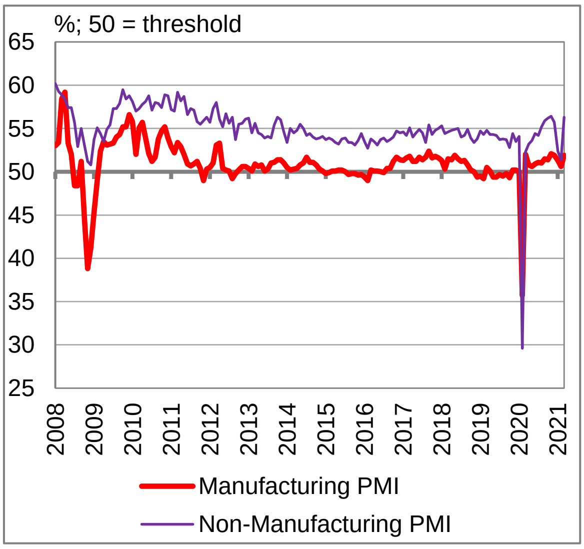


Figure 26: Both industrial output and retail sales growth have a strong start in 2021

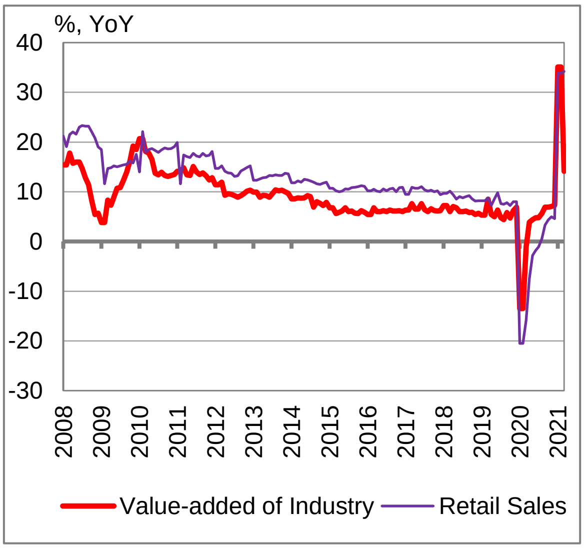


Figure 27: Fixed assets investment grew by 25.6% in 1Q 2021

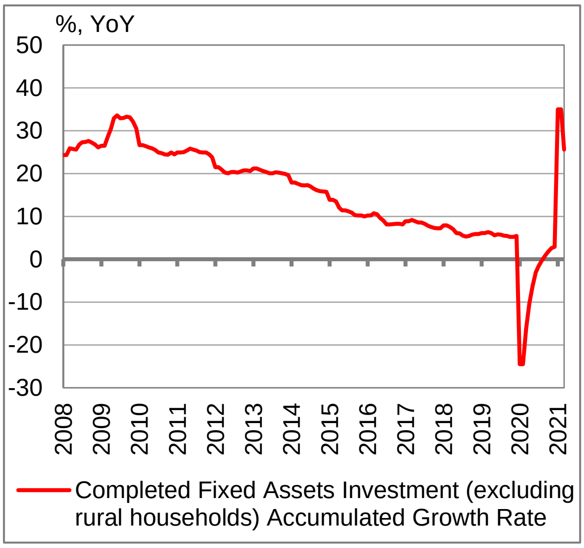
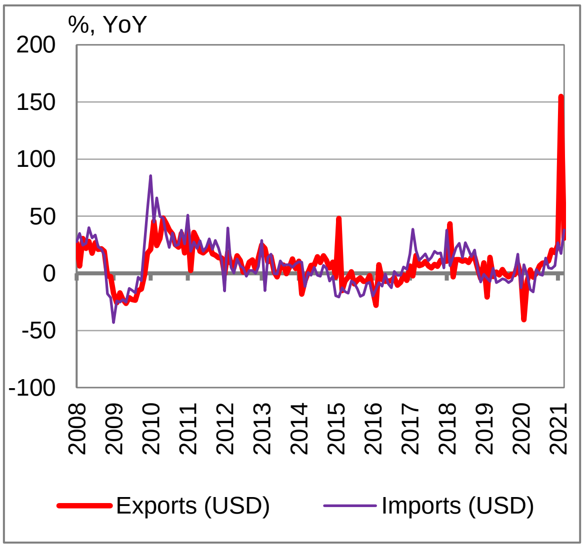


Figure 28: Exports grew by strong double-digit growth in Mar 2021; imports at all-time high

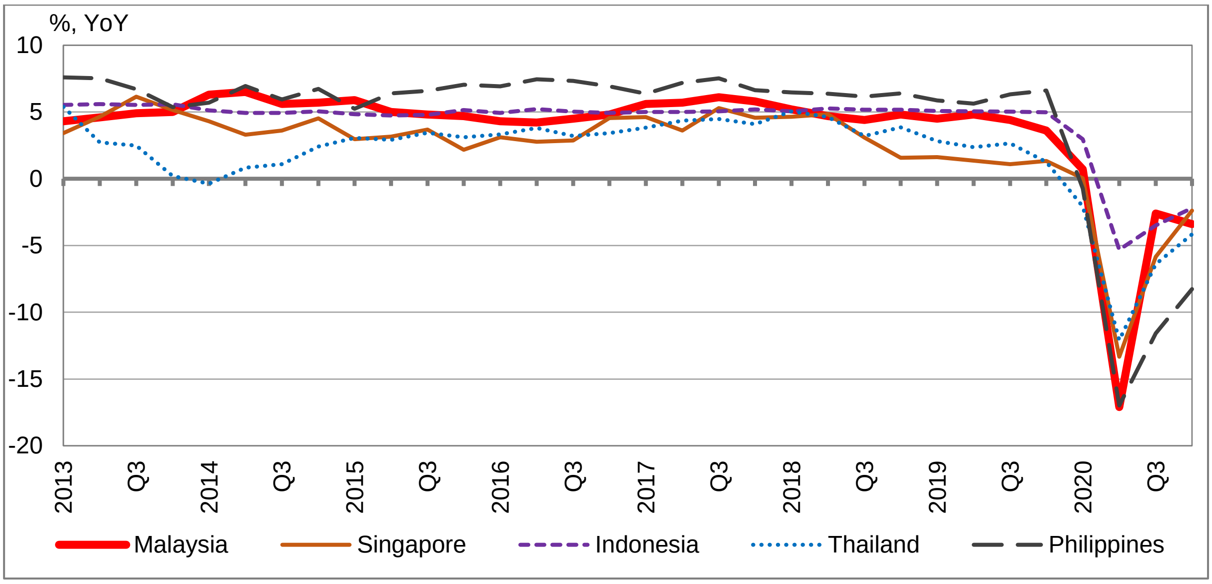


Source: National Bureau of Statistics of China; General Administration of Customs, China

ASEAN-5 ECONOMIES' KEY ECONOMIC DATA TRACKER

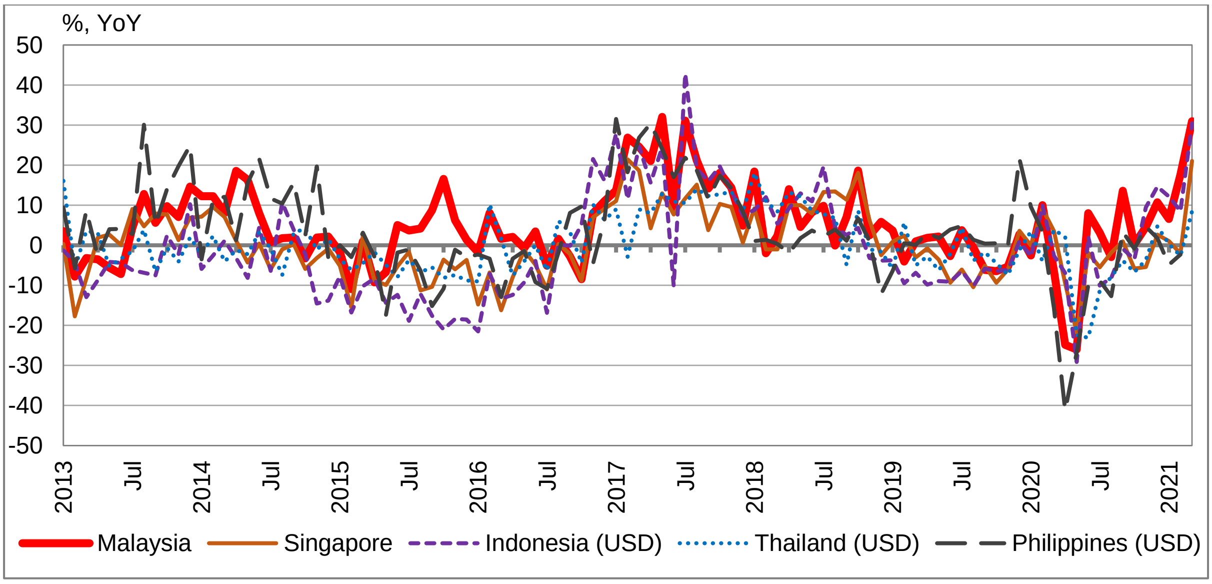
ASEAN-5 (Malaysia, Singapore, Indonesia, Thailand and the Philippines)'s economic output contraction has narrowed in 4Q 2020, with the exception of Malaysia. While the industrial output recorded a mixed performance, exports have made a strong comeback, riding on the global recovery and robust external demand. Overall, the recovery path remains critically on the path of pandemic and the effectiveness of respective countries' vaccination program.

Figure 29: Real GDP growth trend



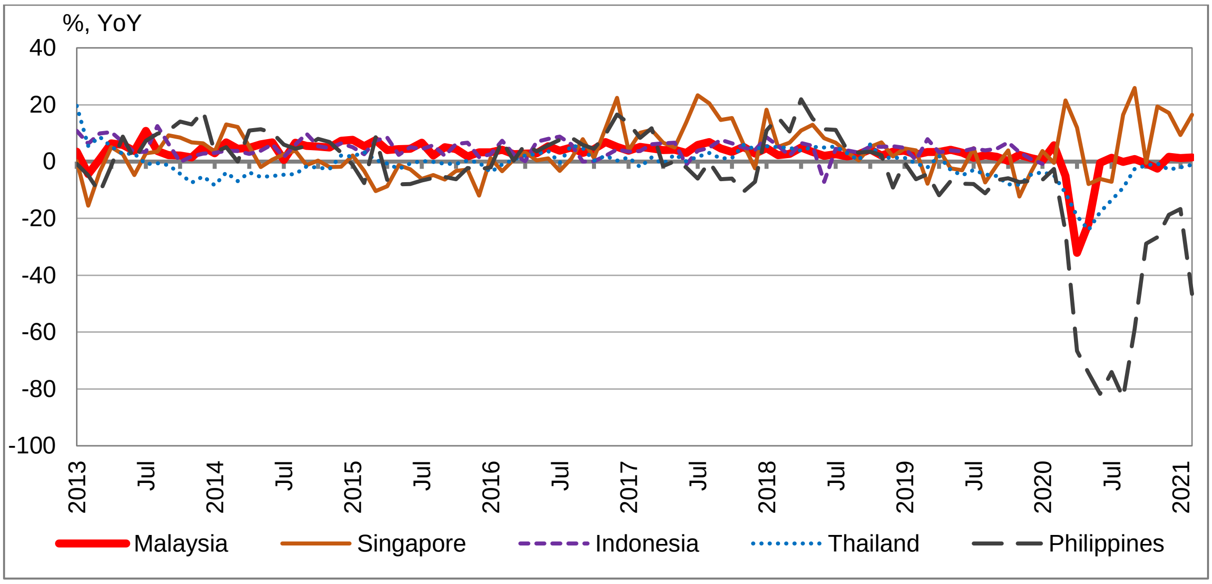
Source: Department of Statistics, Malaysia; Singapore Department of Statistics; Statistics Indonesia; National Economic and Social Development Board, Thailand; Philippine Statistics Authority

Figure 30: Export growth trend



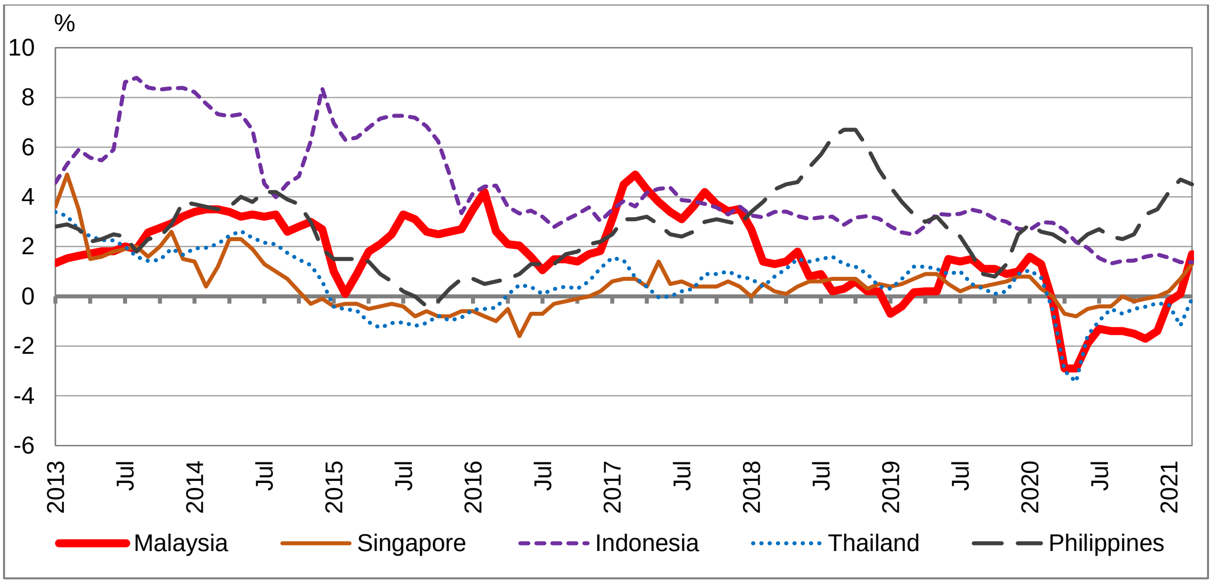
Source: Department of Statistics, Malaysia; Singapore Department of Statistics; Statistics Indonesia; Bank of Thailand; Philippine Statistics Authority

Figure 31: Industrial production growth trend



Source: Department of Statistics, Malaysia; Singapore Department of Statistics; Statistics Indonesia; Office of Industrial Economics, Thailand; Philippine Statistics Authority

Figure 32: Inflation trend



Source: Department of Statistics, Malaysia; Singapore Department of Statistics; Bank Indonesia; Ministry of Commerce, Thailand; Philippine Statistics Authority

MALAYSIA'S ECONOMIC AND FINANCIAL CONDITIONS

STEADY STRIDES TOWARDS RECOVERY BUT GROWTH IS UNEVEN

Continued scarring effects in 1Q 2021. Amid continued scarring effects from a prolonged pandemic and less restrictive movement restrictions in the early months of 2021, the Malaysian economy should continue to recover in the coming quarters, largely boosted by very "low base" effect in 2Q 2020 when the total lockdown (Movement Control Order) had halted economic and business activities.

The on-going national immunization program holds the key to lift a sustained revival in consumer sentiment. Hence, the slowness in the rate of vaccination amid concerns over the occurrence of the 4th wave, prompting more targeted MCO/EMCO are expected to have a prolonged scarring effects on economic and business activities.

As long as the movement restrictions are less restrictive, the chances of a complete stalling of economic recovery are unlikely. However, we caution that 1Q 2021 could still be a sluggish growth and a turnaround in positive growth will begin from 2Q onwards though the magnitude of economic growth increases in 2H 2021 will depend greatly on the progress made in the immunisation program.

Consumer spending has rebounded as sentiment improves on the vaccination program, albeit moving at a slow pace. This is partly helped by cash handout, the withdrawal of EPF savings, and targeted repayment assistance. The pent-up demand and drawdown of precautionary savings that were unspent during the movement restrictions.

The export sector is set to remain strong, on the back of buoyant global demand for semiconductors, rubber products and chemicals as well as palm oil products.

Uneven growth in the services sub-sectors. The main headwind is strict inter-states travel restrictions, the reopening of the border will likely be a gradual process towards end-year, and hence, the persistent weakness in tourism, aviation as well as retail and hospitality sectors will hold back the recovery of overall services sector.

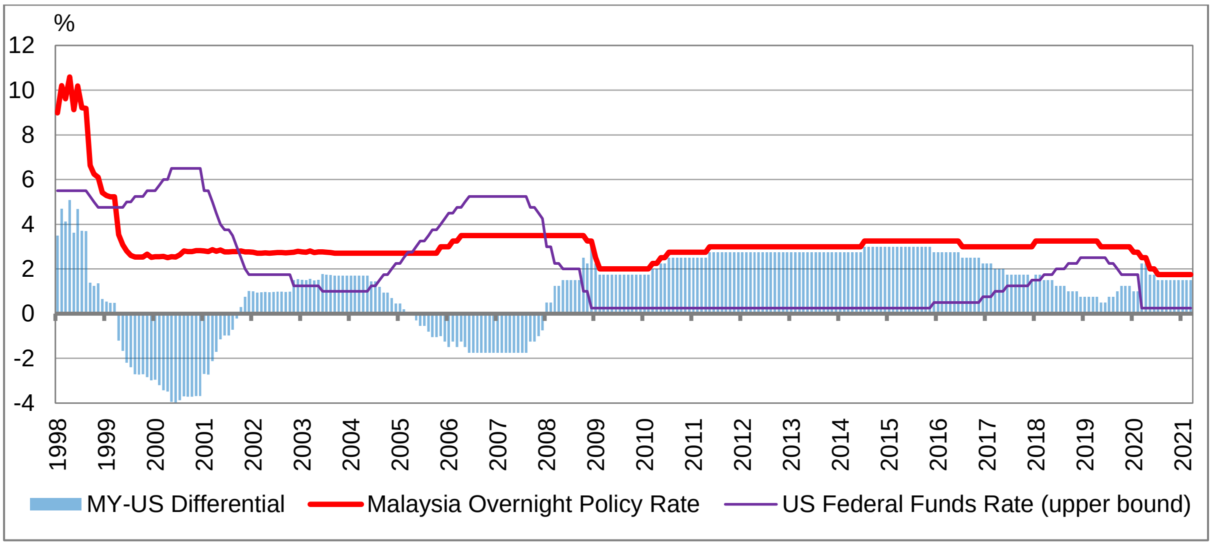
SERC maintains its GDP growth estimates of 4.0% (base case) and 6.0% (upside) for 2021 amid continued economic scarring effects from the movement restrictions and restricted inter-state travel ban.

Table 3: Real GDP growth (% YoY)

Economic Sector [% share to GDP in 2020]	**2019**	**2020**	**2020 Q1**	**2020 Q2**	**2020 Q3**	**2020 Q4**	**2021*e* (BNM)**	**2021*e* (SERC)**
By kind of economic activity								
Agriculture [7.4%]	2.0	-2.2	-8.7	1.0	-0.5	-0.7	4.2	2.7
Mining & Quarrying [6.8%]	-2.0	-10.0	-2.0	-20.0	-6.8	-10.6	3.1	2.5
Manufacturing [23.0%]	3.8	-2.6	1.5	-18.3	3.3	3.0	8.8	4.3
Construction [4.0%]	0.1	-19.4	-7.9	-44.5	-12.4	-13.9	13.4	5.0
Services [57.7%]	6.1	-5.5	3.1	-16.2	-4.0	-4.9	6.6	5.6
By type of expenditure								
Private Consumption [59.5%]	7.6	-4.3	6.7	-18.5	-2.1	-3.4	8.0	4.2
Public Consumption [13.4%]	2.0	4.1	5.0	2.3	6.9	2.7	4.4	3.4
Private Investment [15.7%]	1.6	-11.9	-2.3	-26.4	-9.3	-7.0	5.4	5.1
Public Investment [5.2%]	-10.8	-21.4	-11.3	-38.7	-18.6	-19.8	15.2	7.4
Exports of Goods and Services [61.6%]	-1.3	-8.8	-7.1	-21.7	-4.7	-1.8	13.1	3.9
Imports of Goods and Services [55.1%]	-2.5	-8.3	-2.5	-19.7	-7.8	-3.3	14.1	5.9
Overall GDP	**4.3**	**-5.6**	**0.7**	**-17.1**	**-2.6**	**-3.4**	**6.0-7.5**	**4.0**

Source: Department of Statistics, Malaysia; Bank Negara Malaysia; SERC

Figure 33: Malaysia-US's interest rate differentials



Source: Bank Negara Malaysia; Federal Reserve

REVIEW OF KEY ECONOMIC AND FINANCIAL INDICATORS

Leading indicators and Industrial production

Malaysia's leading indicators (LIs), a gauge of economic performance in the next four to six month, signals Malaysia is heading towards economic uptick in forthcoming months. The growth rate of smoothed LI is consistently above trend and moving upwards, with the leading index breaching its record-high in February 2021. The monthly change also showed a similar trend, contributed mainly by better performance in real imports of other basic precious & other non-ferrous metals and the number of new companies registered.

Industrial production expanded at low single-digit growth of 1.5% for the third consecutive month in February 2021 (1.2% in January 2021), helped by continued expansion in the manufacturing segment. Mining and electricity output continued to decline by 5.2% in Jan-Feb 2021 respectively. The export-oriented industries are the main support for higher manufacturing output, and among these were rubber and plastic products as well as electrical and electronic (E&E) products. For domestic-market oriented industries, pharmaceutical products and manufactures of motor vehicle remained the key drivers.

Figure 34: Leading index registered strong annual growth, marking a record-high reading in Feb 2021

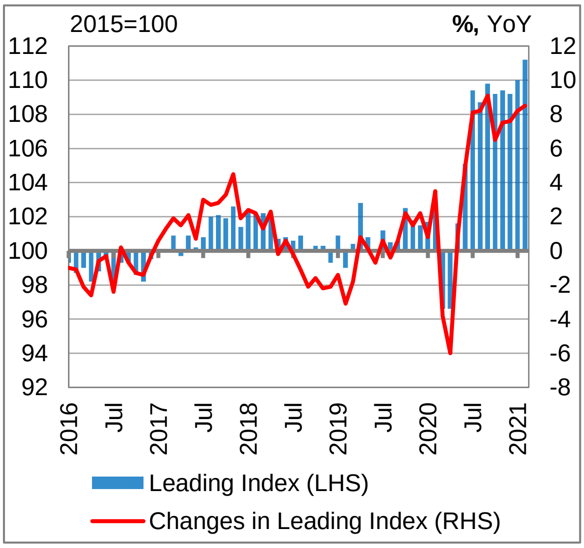
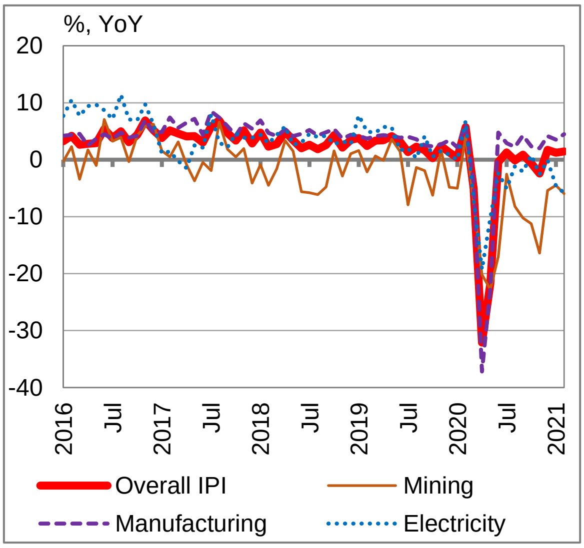


Figure 35: Industrial production grew marginally for the third consecutive month in Feb 2021, helped by the manufacturing sector



Source: Department of Statistics, Malaysia

Exports and Distributive trade

Exports sustained positive growth for seven consecutive months in March 2021, supported by continued recovery of global economy and strong external demand. In March, gross export value breached RM100 billion level to a record high of RM104.9 billion. The average monthly exports in Jan-Mar 2021 amounted to RM94.0 billion, exceeded the pre-pandemic level of average RM82.9 billion per month in 2019. Higher exports were contributed by the electrical and electronic (E&E) products, chemicals, and manufacturers of metal and palm oil and palm-based products as well as rubber and rubber products.

Retail sales had declined for five months in a row since October 2020 with sales falling in all types of specialised stores, with the exception of food, beverages and tobacco as well as information and communication equipment. The weak sales were dampened by the re-imposition of MCO 2.0 and subsequent CMCO amid still weak consumer confidence. Nevertheless, overall wholesale and retail trade are gradually returning to pre-pandemic level. Passenger car sales have performed well, buoyed by several new models launches and aggressive promotional campaigns as well as sales tax exemption.

Figure 36: Exports hit a record-high crossing RM100 billion level in Mar 2021

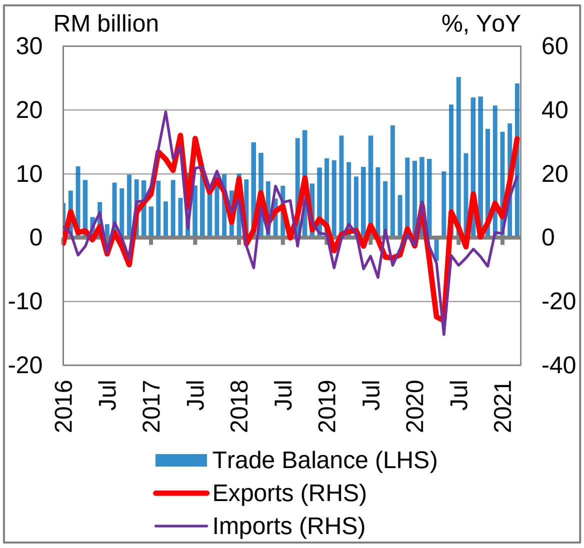
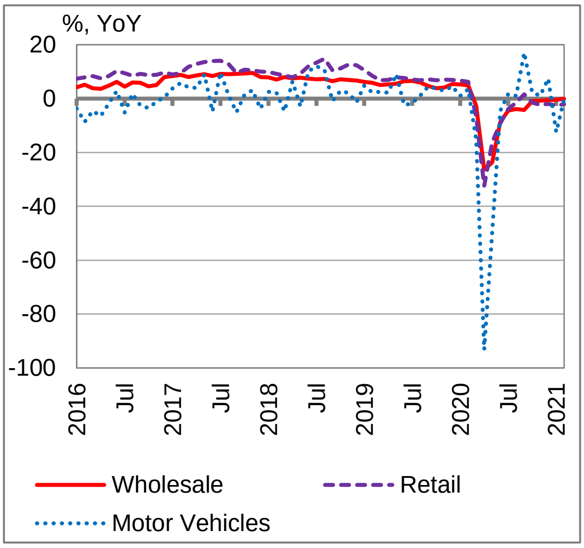


Figure 37: Wholesale and retail trade growth has yet to return back to positive territory in Feb 2021



Source: Department of Statistics, Malaysia

Private consumption indicators

Selected **private consumption indicators** show that consumer discretionary spending was mixed, with money in circulation increased strongly. Though the latest MIER's Consumer Sentiments Index (CSI) rose higher to 98.9 in 1Q 2021 (85.2 in 4Q 2020), it is still below the 100-pt optimism threshold. With new infected cases staying stubbornly high above 2,000 since 15 April and have breached 3,000 in recent days amid a slow pace of vaccination, there remain lingering concerns about the strength of consumer sentiment.

The recovery in the labour market has been moderate as unemployment rate still hovering between 4.7% and 4.8% after easing off to 4.6% in September 2020 from 5.3% in May. The number of unemployed persons eased to 777,500 persons in February 2021 (782,500 in January 2021), but still about 50% above nearly 520,000 persons before the pandemic. As of 25 April 2021, 24,688 employees have lost their jobs as reported by the Employment Insurance System (EIS).

Figure 38: Selected private consumption indicators

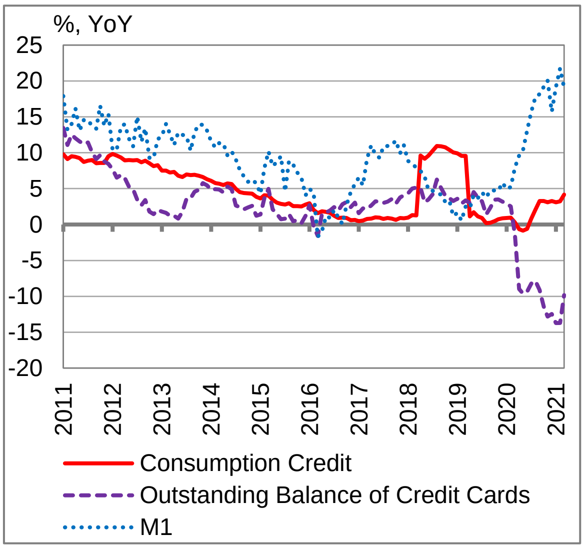
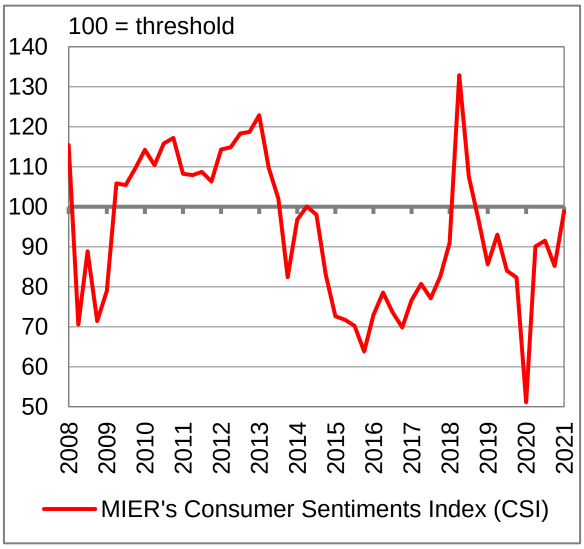


Figure 39: MIER's Consumer Sentiments Index (CSI)



Note: Loan data for April 2018 onwards have been revised to include MBSB Bank Berhad.
Source: Bank Negara Malaysia; Malaysian Institute of Economic Research

Private investment indicators

Selected **private investment indicators** showed some positive signs, echoed by the MIER Business Conditions Index (BCI) which continues to stay above the 100-pt threshold for two consecutive quarters (111.8 in 1Q 2021 and 115.4 in 4Q 2020).

Growth in commercial vehicles sales and imports of investment goods have risen significantly by 226.3% yoy and 93.4% respectively in March (30.4% and 38.3% respectively in February), largely boosted by low base effect. Revived imports of intermediate and capital goods indicate that manufacturers are replenishing their raw materials and semi-finished goods as well as planning for capital expansion in coming months. In addition, better global prospects and the on-going national immunisation programme also helped to lift business sentiments.

In 2020, MIDA has approved RM91.3 billion of manufacturing investment (10.3% higher than 2019), RM66.7 billion in services sector and RM6.0 billion in the primary sector. Nevertheless, total approved investment still declined by 22.4% to RM164 billion in 2020 from RM211.4 billion in 2019, mainly due to the COVID-19 pandemic and the implementation of MCO, which have severely halted the investment plan.

Figure 40: Selected private investment indicators

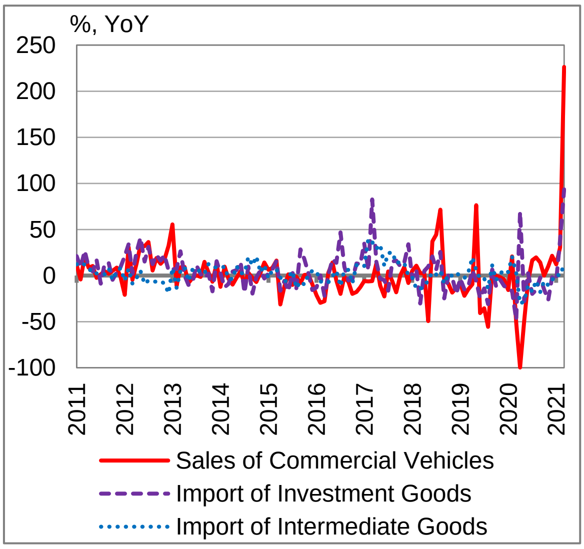
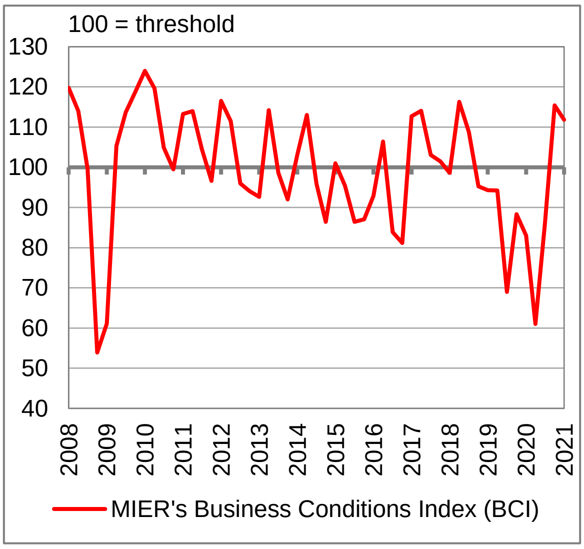


Figure 41: MIER's Business Conditions Index (BCI)



Source: Bank Negara Malaysia; Malaysian Institute of Economic Research

Price indicators

Overall **price level**, as measured by the Consumer Price Index (CPI) increased further by 1.7% yoy in March 2021 (0.1% in February), ending eleven months of deflation from March 2020 to January 2021. Price increases were mainly reflected in higher fuel prices (RM2.05/litre for RON95 retail price vs. average RM1.74/litre in March 2020), the lapse of tiered electricity rebate in Apr-Dec 2020, food prices (1.3%-1.5% since July 2020), as well as furniture and furnishings, jewellery rings and precious stones, air transports, and the repair and maintenance of personal transport.

In contrary, moderating rental charges (an average increase of 0.4% in 1Q 2021 vs. average 1.4% in 2020; 18.1% of CPI basket), an electricity tariff rebate of 2 sen in Jan-Jun 2021 (vs. a surplus of 2 sen in Jan-Jun 2020) and declining accommodation rental were among the CPI items that helped to moderate the pace of inflation. Core inflation has remained low at less than 1.0% for six months in Oct 2020-Mar 2021.

Starting April this year, headline inflation will spike up as the extremely low base in 2020 kicks in, reinforced by other cost-push factors like higher commodity prices. Bank Negara Malaysia expects inflation rate could reach as high as 5% in 2Q 2021 before averaging 2.5%-4.0% for the full year of 2021. Notwithstanding this, BNM reaffirmed that the current accommodative monetary policy will be maintained as the inflation spike will be temporary. SERC expects average inflation to increase by 3.0%-4.0% in 2021 (-1.2% in 2020).

Figure 42: Core inflation remains subdued despite headline inflation shot up in Mar 2021

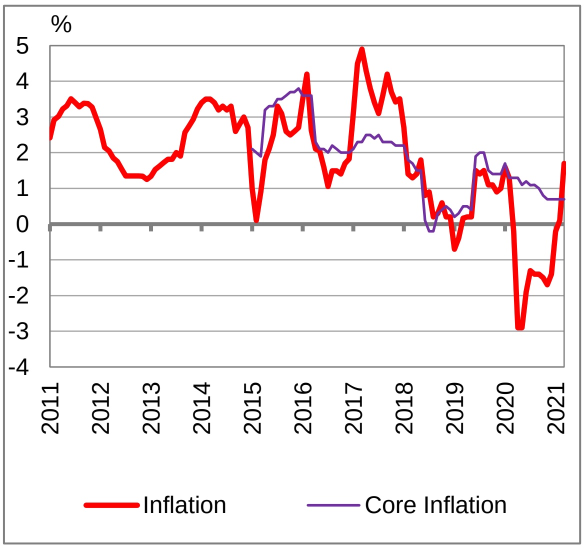
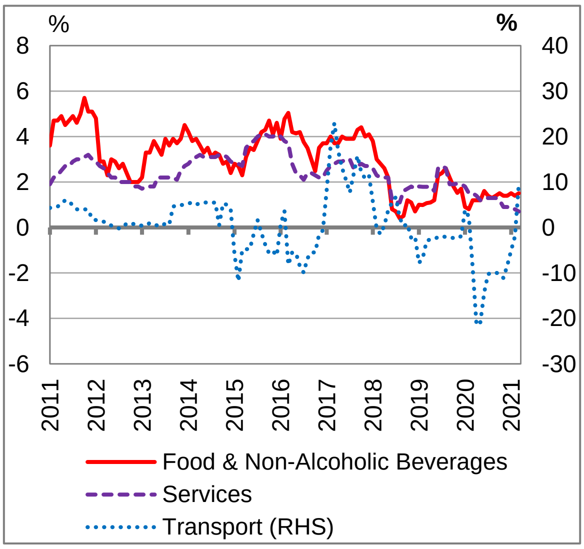


Figure 43: Transport prices soared higher due to a recovery in fuel prices and boosted by low base effect



Source: Department of Statistics, Malaysia

Banking loan indicators

Banking system's outstanding loan growth picked up to 3.9% yoy in March 2021 (3.4% in December 2020), held up by household loans (5.7% in March vs. 5.1% in February), mainly for the purchase of vehicles and still-high residential property loans. Business and other loans growth remained sluggish (1.4% in March vs. 1.8% in February), with the exception of the wholesale and retail trade sector.

Monthly loan repayment in March continues to record more than RM100 million since October on the expiry of automatic loan moratorium in September. Gross impaired loans remained at 1.6% of total outstanding loan in March 2021, while banks continued set aside a higher provision of 1.8% to total outstanding loans as a precaution against future credit losses. Banks' excess capital buffers amounting higher to RM126.3 billion in February 2021 (RM123 billion in December 2020).

Figure 44: Outstanding loan growth by type

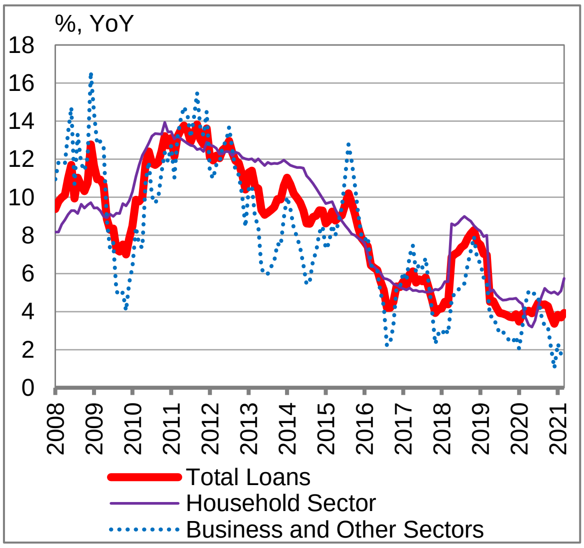


Figure 45: Loan applications growth

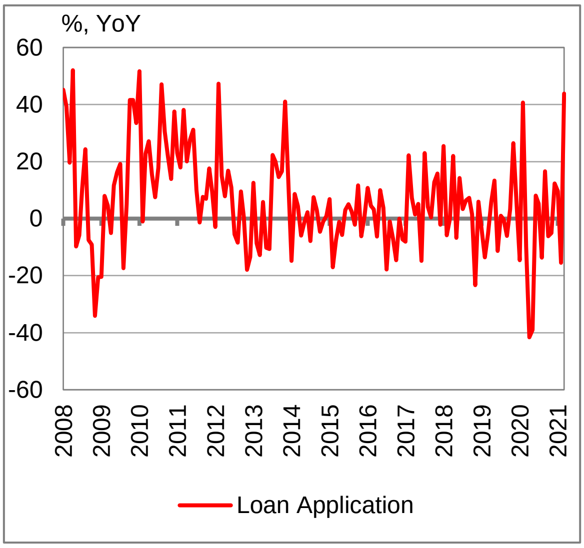


Figure 46: Loan approvals growth

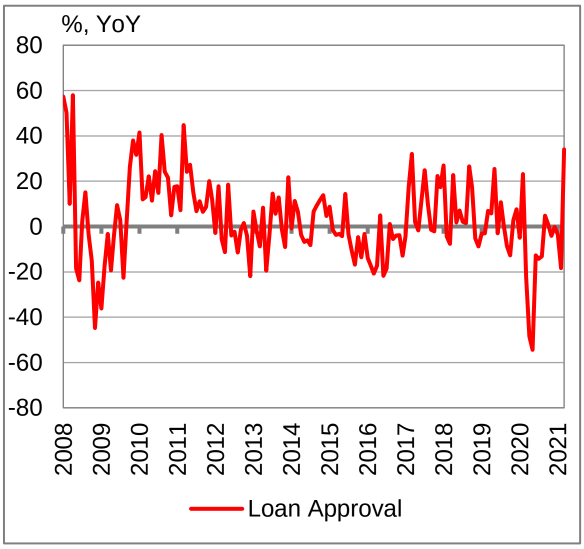
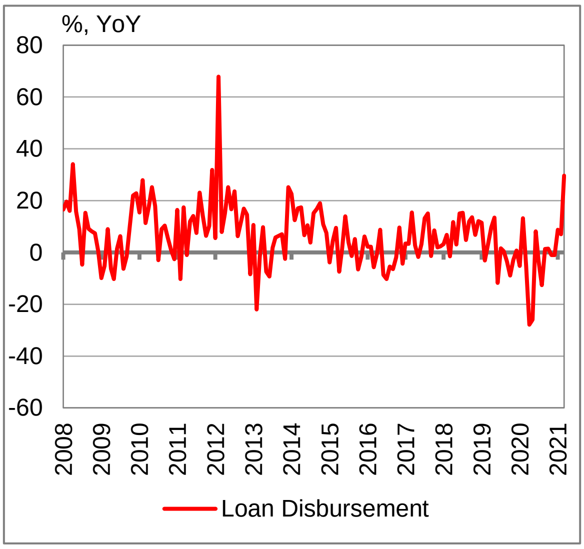


Figure 47: Loan disbursements growth



Note: Loan data for April 2018 onwards have been revised to include MBSB Bank Berhad.
Source: Bank Negara Malaysia

Financial indicators

Foreign reserves rose gradually to reach US$109.3 billion as at 15 April 2021 as it recouped the lost ground during the oil prices crash in 2014-2015. The reserves position is sufficient to finance 8.8 months of retained imports and is 1.2 times total short-term external debt.

While foreign investors continued to net sell domestic equities by another RM1.7 billion in 1Q 2021 (net sold RM24.8 billion in 2020), foreign holdings of the Malaysian equities dropped to 20.3% as at end-March 2021 (20.7% as at end-December 2020). This marks the 21st continuous month of net foreign outflows. As a result, FTSE Bursa Malaysia KLCI eased to 1,573.51 as at end-March 2021 (1,627.21 as at end-December 2020).

On the bond market front, foreign investors sustained their accumulation of the Malaysian Government Securities (MGS) for eleven months since May 2020. As at end-March 2021, foreign holdings of the Malaysian Government Securities stood at 40.8%, with a total net purchase of RM7.3 billion in 1Q 2021. Foreign investors also made net purchase of a sizeable RM5.9 billion of the Malaysian Government Investment Issues (MGII) in 1Q 2021, raising their share holding to 8.0% as at end-March 2021 (6.8% as at end-December 2020).

The ringgit depreciated by 2.2% to RM4.1045 against the greenback as at end-April 2021 from RM4.0130 as at end-December 2020. Throughout the same period, the ringgit broadly weaker against its major and regional peers: Depreciated against the pound sterling (-4.5%), Australian dollar (-3.3%), Chinese renminbi (-3.2%), Vietnamese dong (-2.2%), Philippine peso (-1.9%), Singapore dollar (-1.9%), Indian rupee (0.9%) and euro (-0.8%), and only appreciated against the Japanese yen (3.1%), Thai baht (1.8%) and Indonesian rupiah (0.7%). **SERC expects the ringgit to settle at RM4.00 per US dollar at end-2021.**

Figure 48: Foreign reserves position gradually trending up

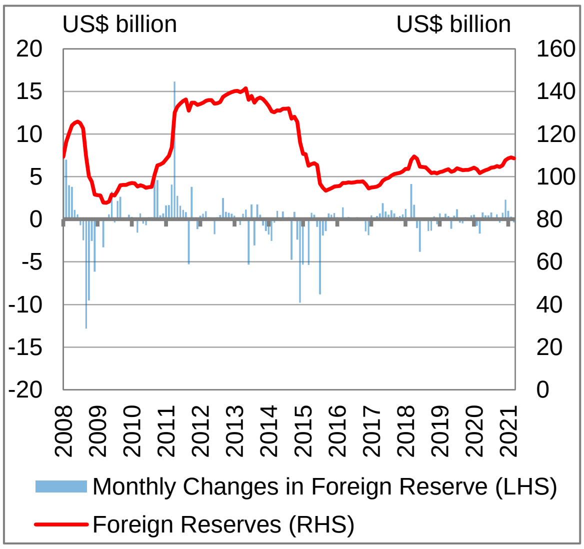


Figure 49: Ringgit's effective exchange rate (EER)

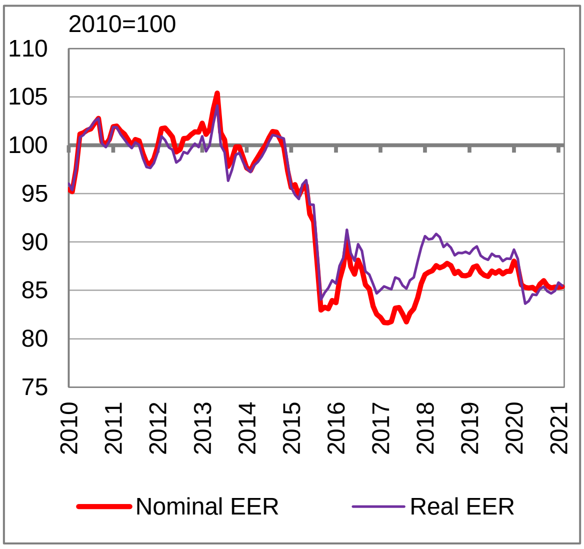


Figure 50: Ringgit against major foreign currencies

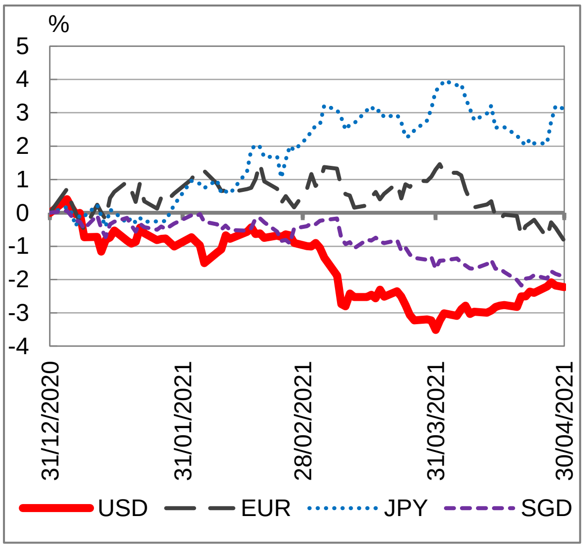
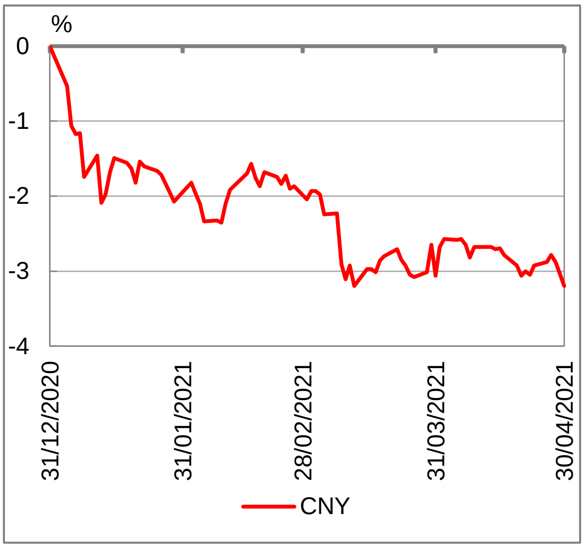


Figure 51: Ringgit against Chinese renminbi



Source: Bank Negara Malaysia; Bank for International Settlements

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