



Socio-Economic Research Centre (SERC)

Quarterly Economy Tracker

Apr-Jun 2022

Malaysia Braces for A Bumpy Ride in 2H 2022

12 July 2022





US RECESSION FEARS DARKEN OUTLOOK FOR GLOBAL GROWTH

- **Shocks have taken a toll on the global economy.** In the last Quarterly Economy Tracker (QET), we have given a picture of the shocks and threats to the world economy -- persistent supply disruptions related to the COVID-19, including the most recent lockdowns in China, new supply and price shocks associated with Russia's invasion of Ukraine, and the subsequent economic sanctions.

The World Bank cut this year's global growth estimates to 2.9% from 4.1% previously, and has warned that the toll from the war in Ukraine and COVID-19 pandemic is likely to lead to years of slow growth and high inflation. In April, the International Monetary Fund (IMF) said that the war has set back global recovery as it lowered global growth estimates to 3.6% each in 2022 and 2023 (from previous forecast of 4.4% in 2022 and 3.8% in 2023 respectively). We expect the upcoming IMF's World Economic Outlook Update in July would further review the global growth prospects. The IMF does not rule out that a global recession given the elevated risks.

- **Recent weakening.** High-frequency economic indicators offer evidence that global growth momentum has slowed owing to multitude of price and supply shocks. PMI gauges of the manufacturing and service sector activity in many advanced economies indicated a slower expansion though the PMI readings have stayed moderately above 50—the threshold signalling either an expansion or a contraction.

Inflation has been higher than expected in many economies, compelling most major central banks to raise interest rate. Both the financial and foreign exchange markets continue to remain volatile and the geopolitical tensions have increased.

- a) In the **US economy**, a recession seems inevitable. Both the exogenous supply shocks and the Fed's aggressive interest rate hikes to tame persistent high inflation (both cost-driven and wage-price spiral are at play) are expected to damp consumer spending and restrain business activity. The US GDP contracted by 1.6% annualised qoq in 1Q 2022.
- b) The **eurozone's** subdued economic growth in 1Q 2022 is leaning more towards more downside risks with a recession risk is rising. Consumers' purchasing power are being squeezed by surging inflation, dampening their willingness to spend. A prolonged period of supply chain disruptions and high energy prices poses a high downside risk to the industrial sector.
- c) While the **Japan** economy contracted slightly lower than expected by 0.5% annualised qoq in 1Q 2022, persistent supply chain disruptions remain a risk to economic momentum in April-June. Soaring raw materials cost and the faster-than-expected US monetary tightening will impact the economy.
- d) In **China**, multiple indicators (sales, industrial production, and fixed investment) have either weakened or contracted in recent months, indicating a grim economic outlook. The zero COVID-19 strategy and the lockdowns in some cities/provinces as well as the troubled real estate sector not only have disrupted the supply chains but also stalled economic and business activities in 2Q. We see China's reduction of quarantine period to 7+3 days for all inbound travellers as a positive sign. While the rolling out of a package of 33 measures covering fiscal, financial, investment and industrial policies, easing of liquidity and credit measures would help to shallow the magnitude of economic slowdown, but the uncertainties in the global environment will pose a big hurdle to China economy.

- **Central banks bite the bullet on rate hikes as taming inflation takes priority.** Against the challenging backdrop of higher and longer inflationary pressures, weaker economic growth, tighter financial conditions, weakening emerging market currencies, the central banks are confronted with a difficult task to act forcefully on inflation while not risking of sapping their economies.

If the central banks hold back to hike interest rates or raise interest rate gradually and endure the supply-crunch inflation, it will result in entrenched higher inflation expectations, prompting companies and employees to push up prices and demand higher wages, respectively. If this happens, it is extremely costly to bring inflation down if inflation expectations don't come down. The central banks may later be compelled to pump the brakes on the economy even harder to get inflation under control.

- **Downside risks outweigh upside.** Given the global growth headwinds, we caution that the odds of worsening outlook would unfold in 2H 2022 and in 2023 given the following downside risks:
 - a) The Fed's front-loaded policy to fight the wage-price spiral inflation could trigger a sooner-than-expected recession in the US economy;
 - b) The worsening economic conditions in Europe due to the persistent high energy prices and inflation. The drag from these two major economies (US and Europe recession) could spill over to the rest of the world; and
 - c) A sharper-than-expected economic slowdown in the China economy.
- **What could limit the downside risks?** The Russian war in Ukraine sees a modest de-escalation could improve investors and business sentiments as well as some softening of commodity and energy prices. The Fed's monetary tightening cycle is peaking, though we think it is unlikely in the near-term. The monetary policy starts to bite on inflation with a time lag of up to 18 months.



VS.



Global Economic and Monetary Conditions

Real GDP growth (% , YoY)

	2019	2020	2021	2022 Q1	2022F (IMF)	2022F (WB)
World	2.9	-3.1	6.1	N/A	3.6	2.9
United States	2.3	-3.4	5.7	0.5	3.7	2.5
Euro Area	1.6	-6.3	5.4	-0.9	2.8	2.5
China	6.0	2.2	8.1	18.3	4.4	4.3
Japan	-0.2	-4.5	1.7	-1.8	2.4	1.7
India	3.7	-6.6	8.7	2.5	8.2	7.5
Malaysia	4.4	-5.5	3.1	-0.5	5.6	5.5
Singapore	1.1	-4.1	7.6	2.0	4.0	N/A
Indonesia	5.0	-2.1	3.7	-0.7	5.4	5.1
Thailand	2.2	-6.2	1.5	-2.4	3.3	2.9
Philippines	6.1	-9.5	5.7	-3.8	6.5	5.7
Vietnam	7.0	2.9	2.6	4.7	6.0	5.8

Note: World GDP growth for 2019, 2020 and 2021 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)); World Bank (Global Economic Prospects)

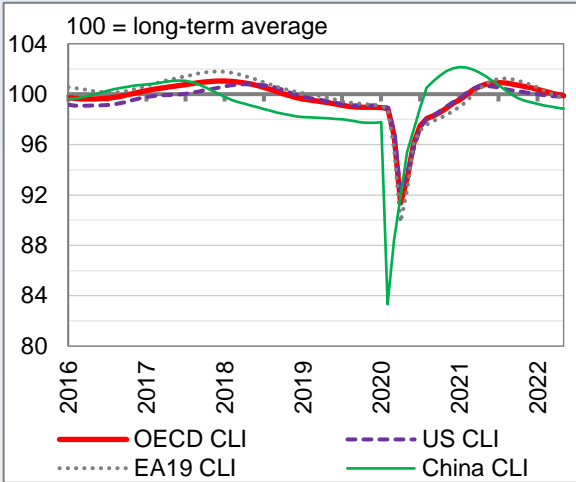
Policy rate (%)

End-period of	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022 (Jun/ Jul)	2022f
US, Fed Federal Funds Rate	0.00- 0.25	0.00- 0.25	0.00- 0.25	0.25- 0.50	0.50- 0.75	1.25- 1.50	2.25- 2.50	1.50- 1.75	0.00- 0.25	0.00- 0.25	1.50- 1.75	3.25- 3.50
Euro Area, ECB Deposit Facility	0.00	0.00	-0.20	-0.30	-0.40	-0.40	-0.40	-0.50	-0.50	-0.50	-0.50	0.75
Japan, BOJ Short-term Policy I/R	0.00- 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	-0.10
China, PBC 1-Year Loan Prime Rate	6.00	6.00	5.60	4.35	4.35	4.35	4.35	4.15	3.85	3.80	3.70	3.45
India, RBI Policy Repo Rate (LAF)	8.00	7.75	8.00	6.75	6.25	6.00	6.50	5.15	4.00	4.00	4.90	5.60
Korea, BOK Base Rate	2.75	2.50	2.00	1.50	1.25	1.50	1.75	1.25	0.50	1.00	1.75	2.50
Malaysia, BNM Overnight Policy Rate	3.00	3.00	3.25	3.00	3.00	3.00	3.25	3.00	1.75	1.75	2.25	2.50
Indonesia, BI 7-Day RR Rate	5.75	7.50	7.75	7.50	4.75	4.25	6.00	5.00	3.75	3.50	3.50	4.50
Thailand, BOT 1-Day Repurchase Rate	2.75	2.25	2.00	1.50	1.50	1.50	1.75	1.25	0.50	0.50	0.50	1.00
Philippines, BSP Overnight RR Facility	3.50	3.50	4.00	4.00	3.00	3.00	4.75	4.00	2.00	2.00	2.50	3.25

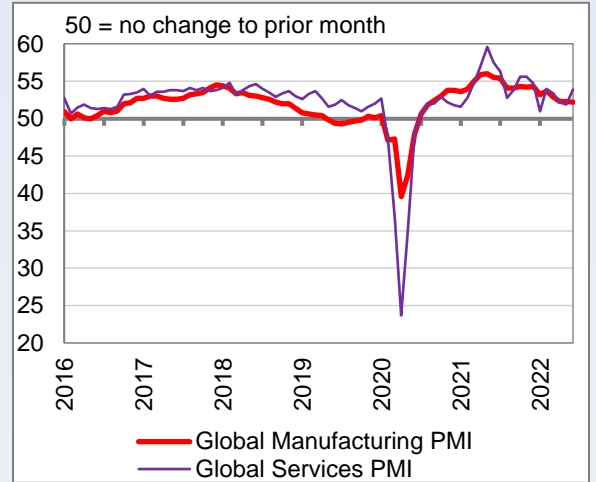
Source: Officials; SERC

Global Current and Forward Indicators

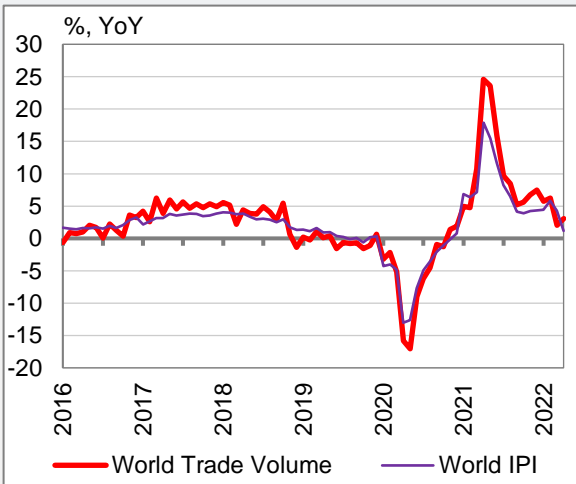
OECD composite leading indicators point to moderating growth momentum in OECD region



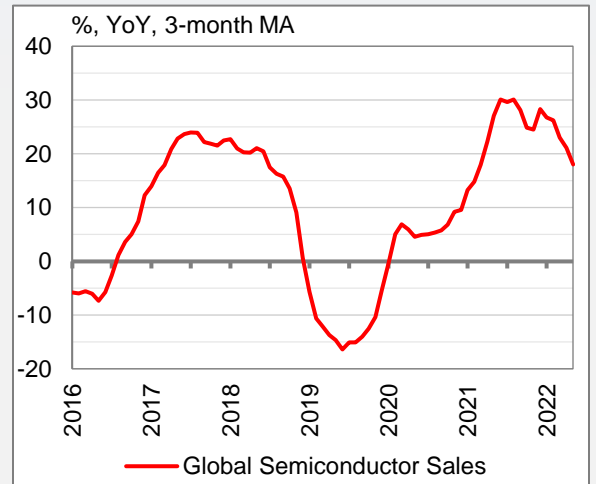
Global Manufacturing PMI at its 22-month low in Jun



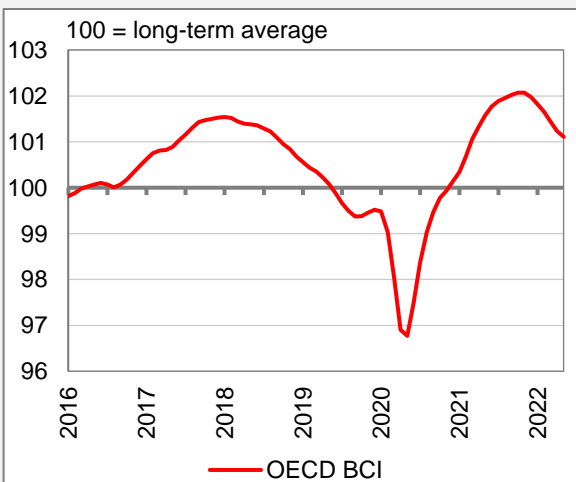
WTO revised downward world trade growth to 3.0% in 2022 from 4.7% previously (9.8% in 2021)



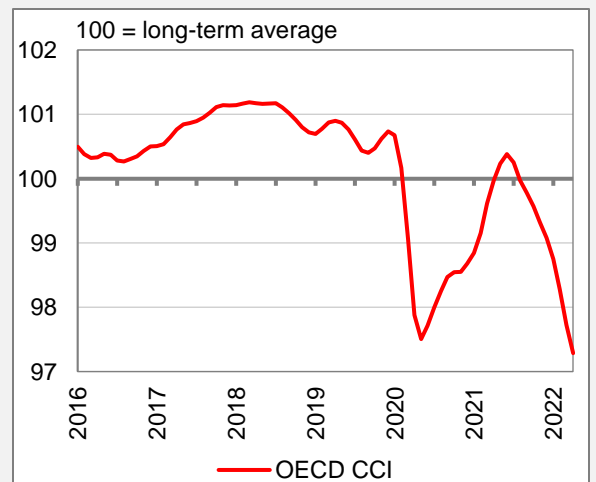
WSTS revised forecast of chip sales growth higher to 16.3% in 2022 from 10.4% previously (26.2% in 2021)



OECD Business Confidence Index

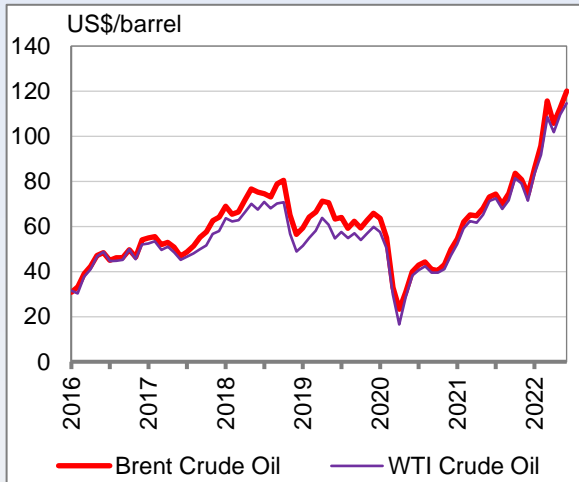


OECD Consumer Confidence Index

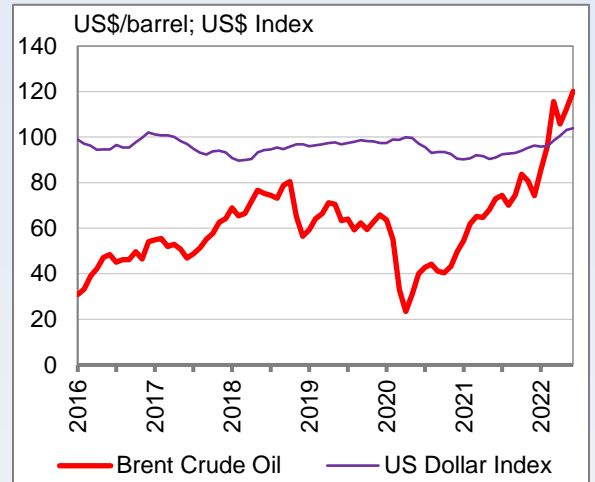


Global Current and Forward Indicators (cont.)

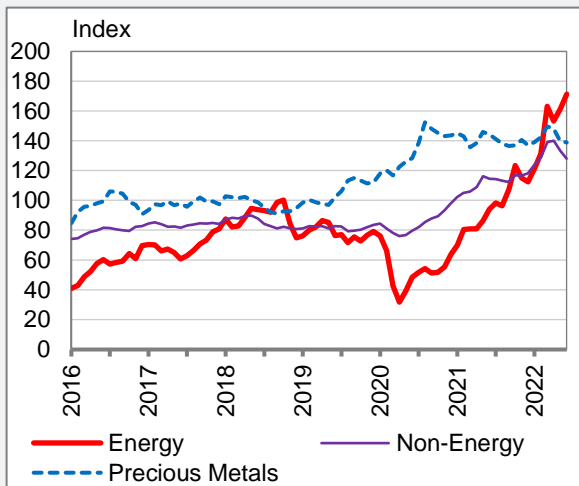
Crude oil prices sustained above US\$100/bbl since Mar



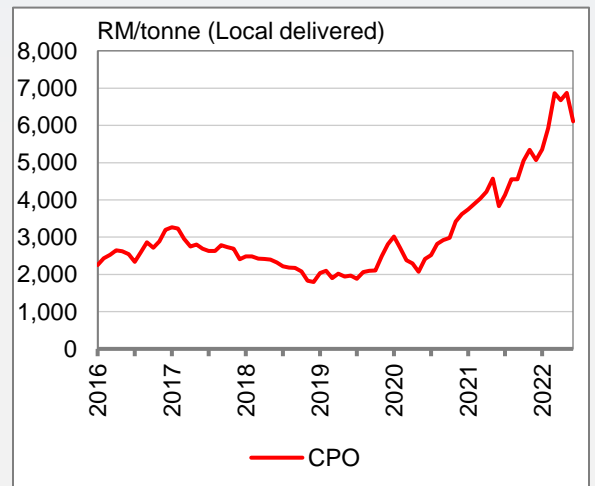
Brent crude oil price vs. the US dollar index



Prices of energy remained elevated while non-energy commodities eased a little



Crude palm oil price pulled back significantly in Jun-Jul after hitting the peak of RM7,000+ level

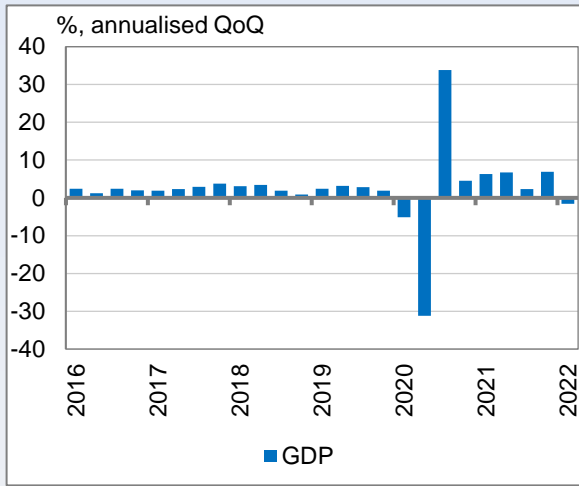


Source: Organisation for Economic Co-operation and Development (OECD); Markit; CPB Netherlands Bureau for Economic Policy Analysis; Semiconductor Industry Association (SIA); World Bank; The Wall Street Journal; Malaysian Palm Oil Board (MPOB)

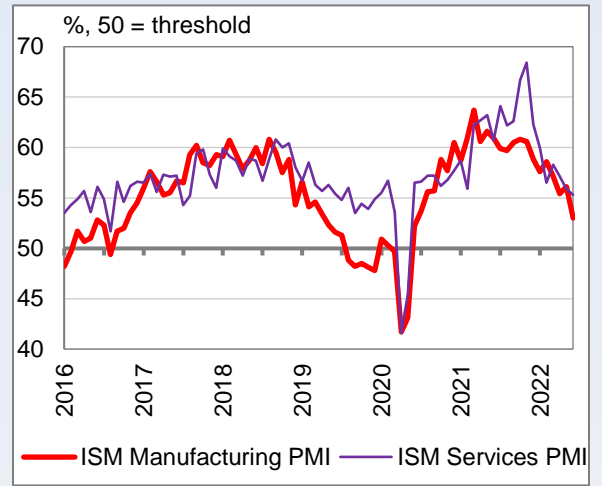


The United States – Rising recession risk

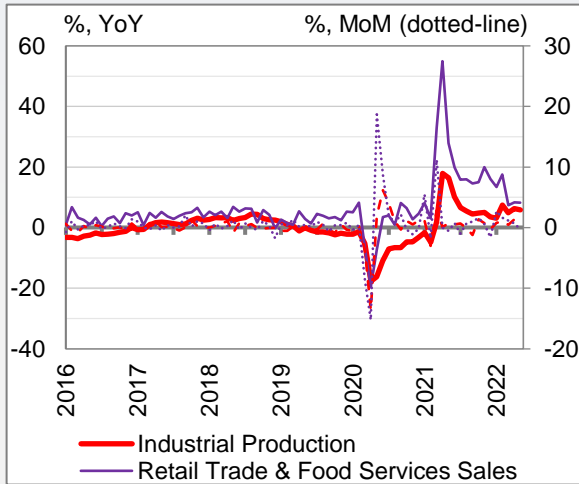
Rising recession risk as the Fed fiddles between rate hikes and inflation



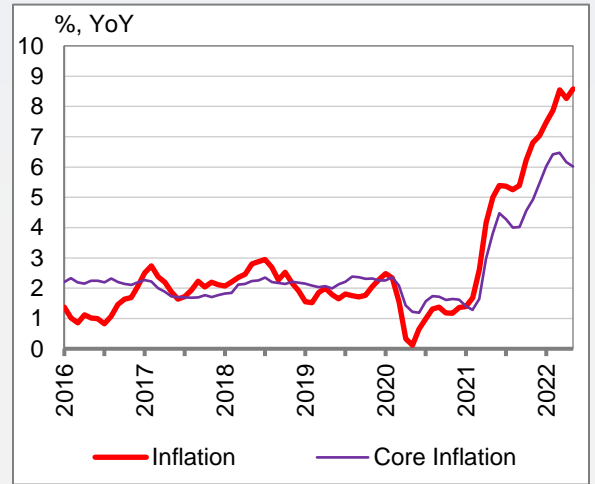
PMI for both sectors are moderating though above the 50% threshold



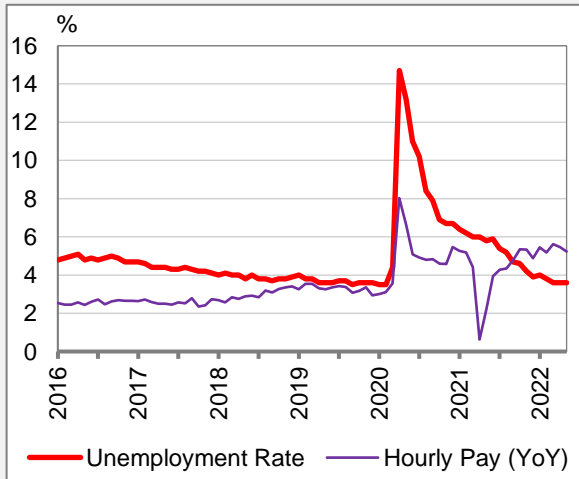
Industrial production and retail trade sales slowed mom...



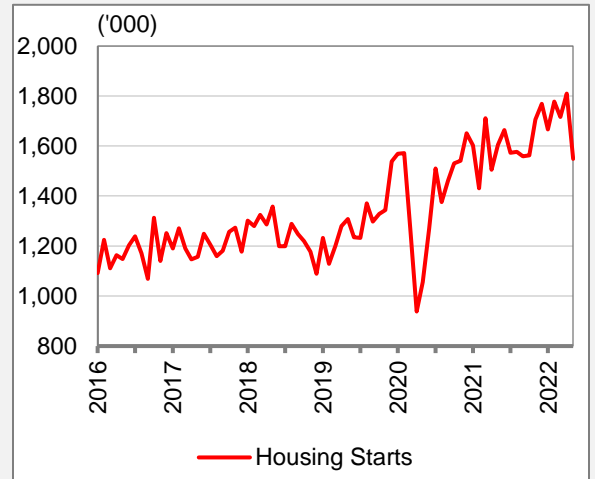
Inflation level at its 40-year high



Unemployment rate steady; wage growth accelerated at a faster pace



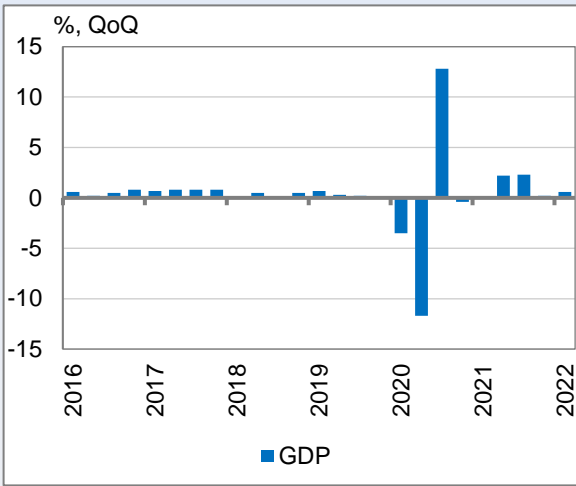
Housing starts presented an uneven trend



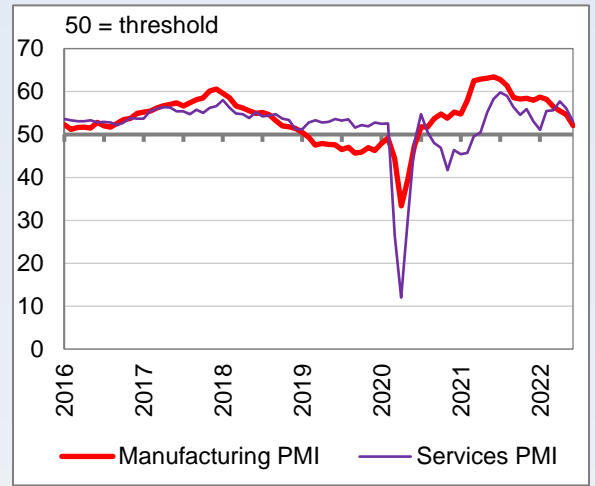
Source: Bureau of Economic Analysis (BEA); Institute for Supply Management (ISM); Federal Reserve System; US Census Bureau; US Bureau of Labor Statistics

Euro Area – Growth momentum lost its steam

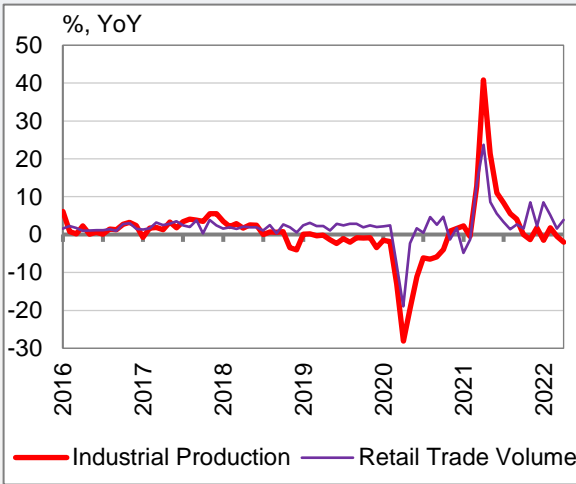
GDP growth returned to pre-pandemic pace – low growth



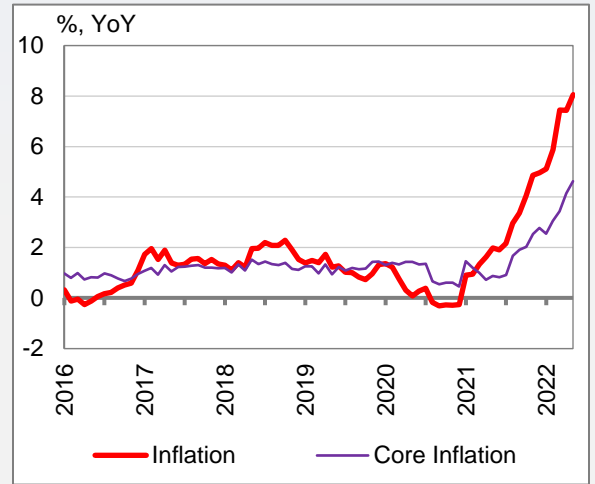
Eurozone growth slows to 16-month low in Jun



Industrial production printed uneven growth in recent months



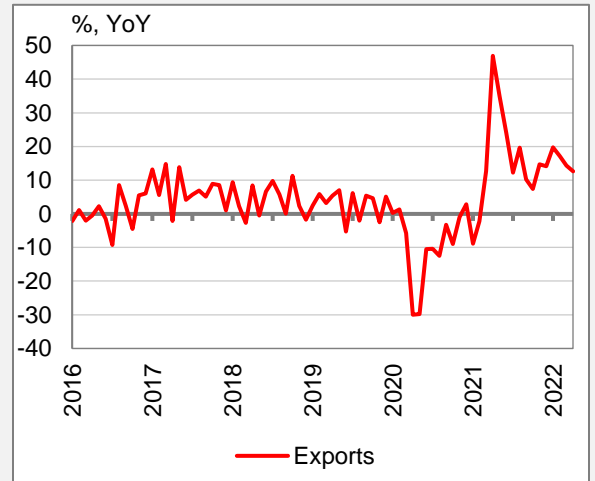
Soaring inflation rate; ECB is preparing for first interest rate hike since 2011



Jobless rate and unemployed persons at record low level in May



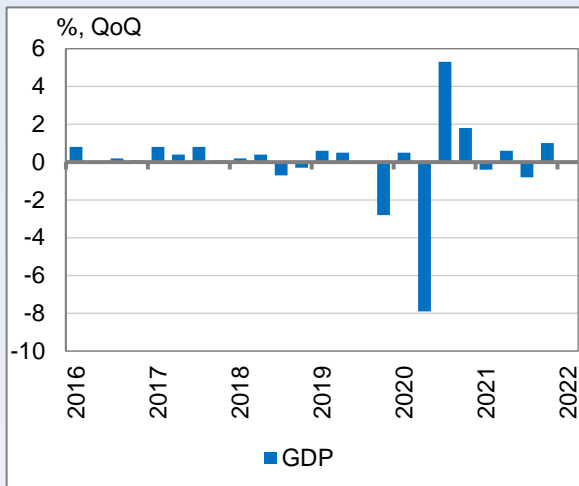
Exports growth at double-digit for six months in a row in Apr



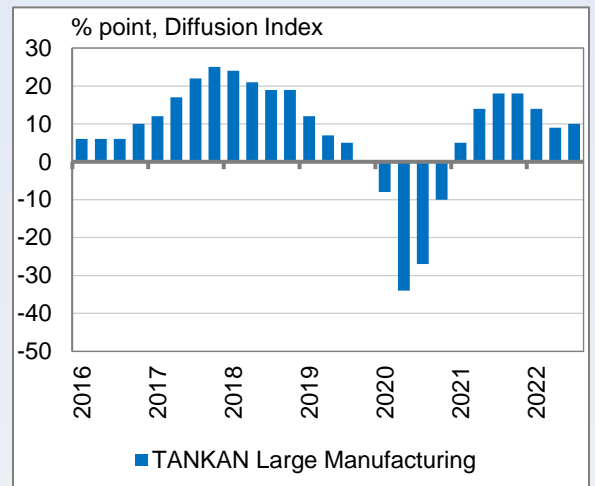
Source: Eurostat; Markit

Japan – Precarious growth; yen at multiple-year low

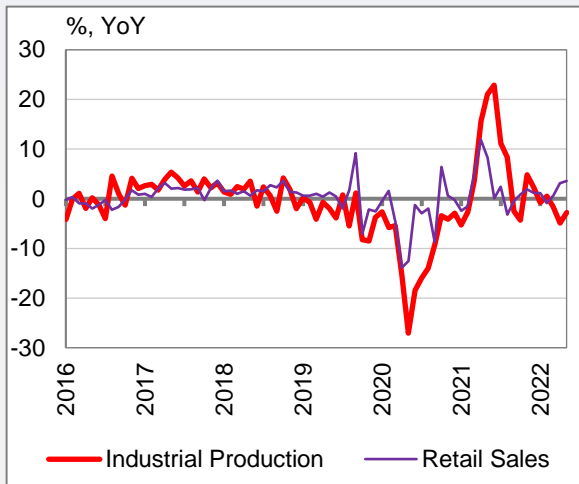
Uneven economic growth



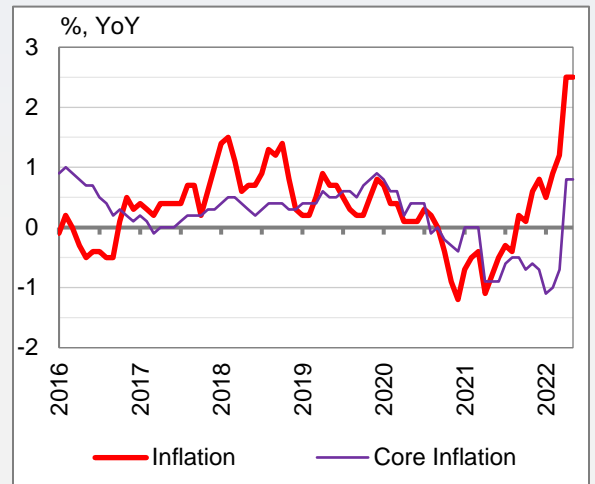
TANKAN survey signals some growth prospects in the manufacturing sector



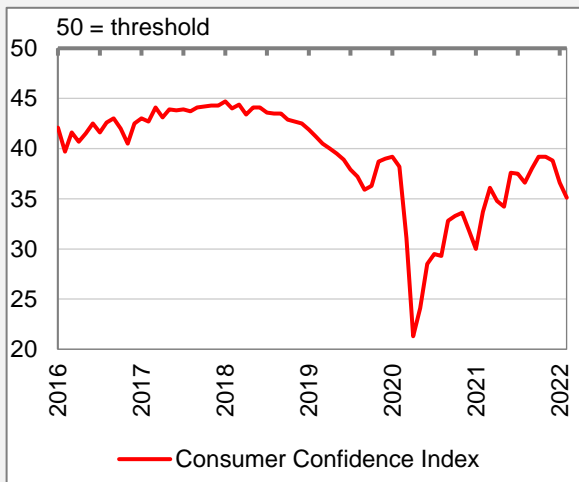
Industrial production growth contracted in Mar-May



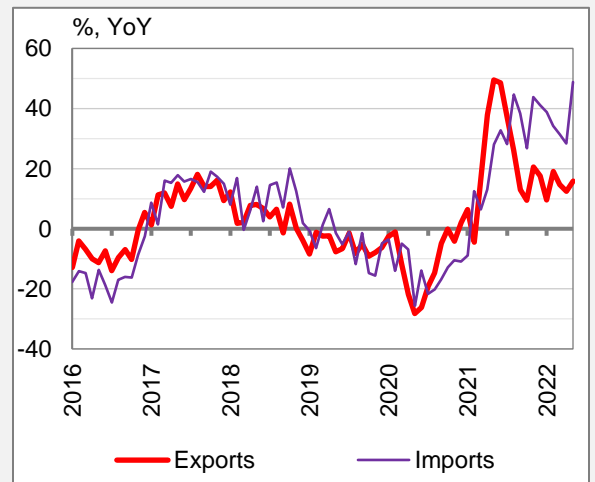
Headline inflation climbed up while core inflation still below 1%



Consumer confidence turning more pessimistic



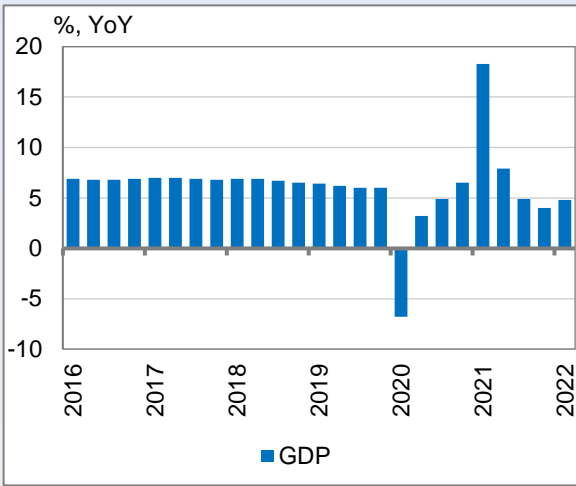
Trade deficit widened and lasted for ten consecutive months in May



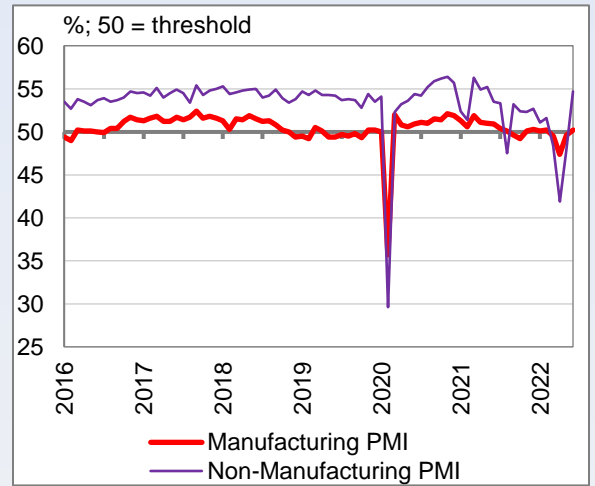
Source: Economic and Social Research Institute (ESRI), Cabinet Office of Japan; Bank of Japan (BOJ); Ministry of Economy, Trade and Industry (METI), Japan; Japan Customs; Statistics Bureau, Japan

China – Most likely missing its growth target

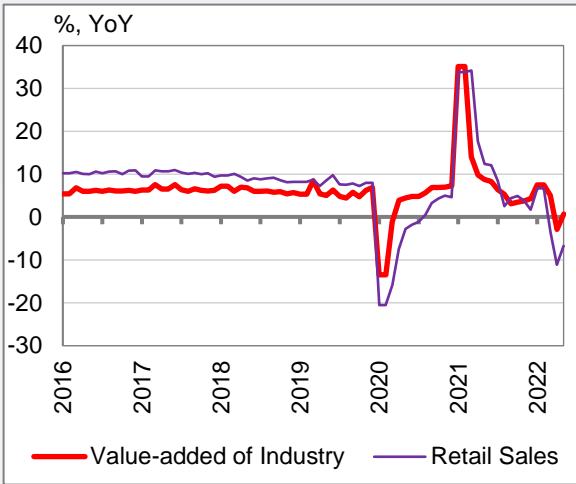
Economic growth in 2Q is expected to contract due to several lockdowns



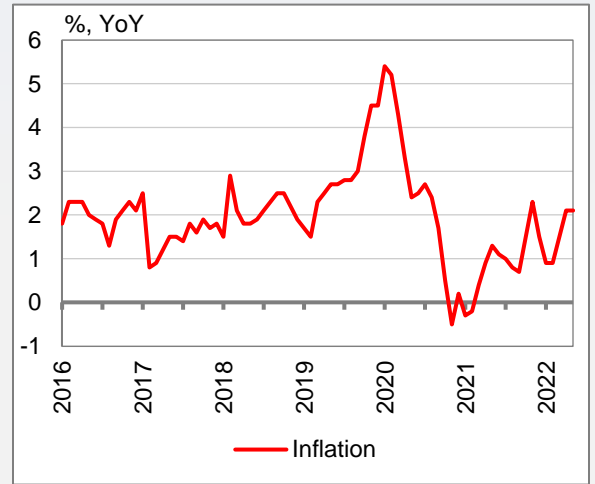
Both PMI reverted to positive territory in Jun



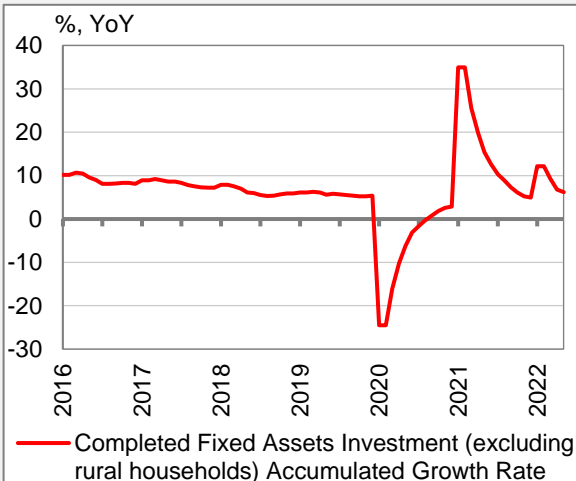
Economic activities were affected by the containment measures



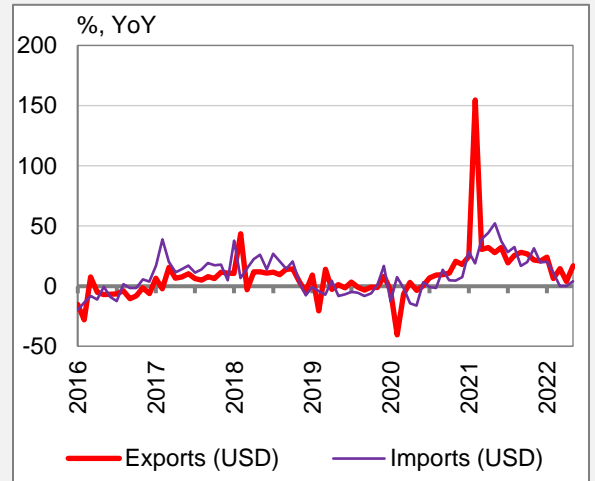
Headline inflation seen creeping up



Fixed investment growth moderated, supported by the manufacturing sector



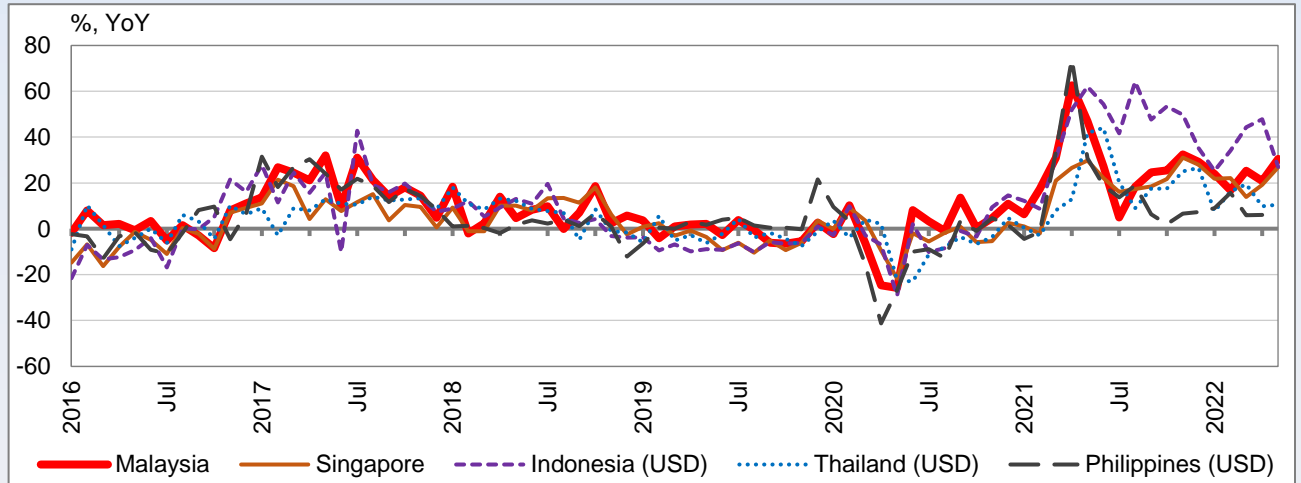
Exports still growing



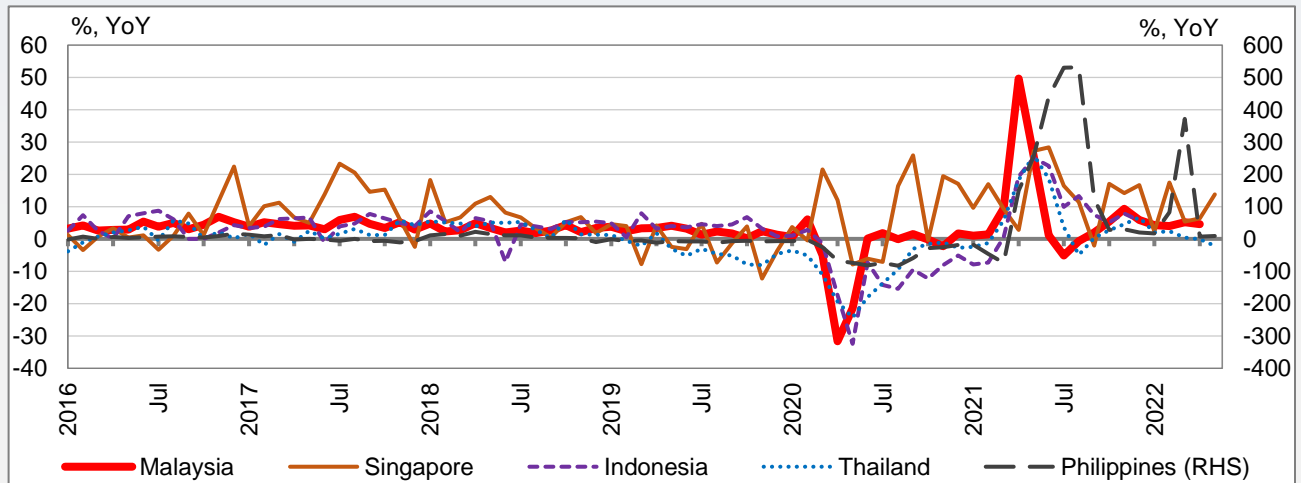
Source: National Bureau of Statistics of China; General Administration of Customs, China

ASEAN Economies

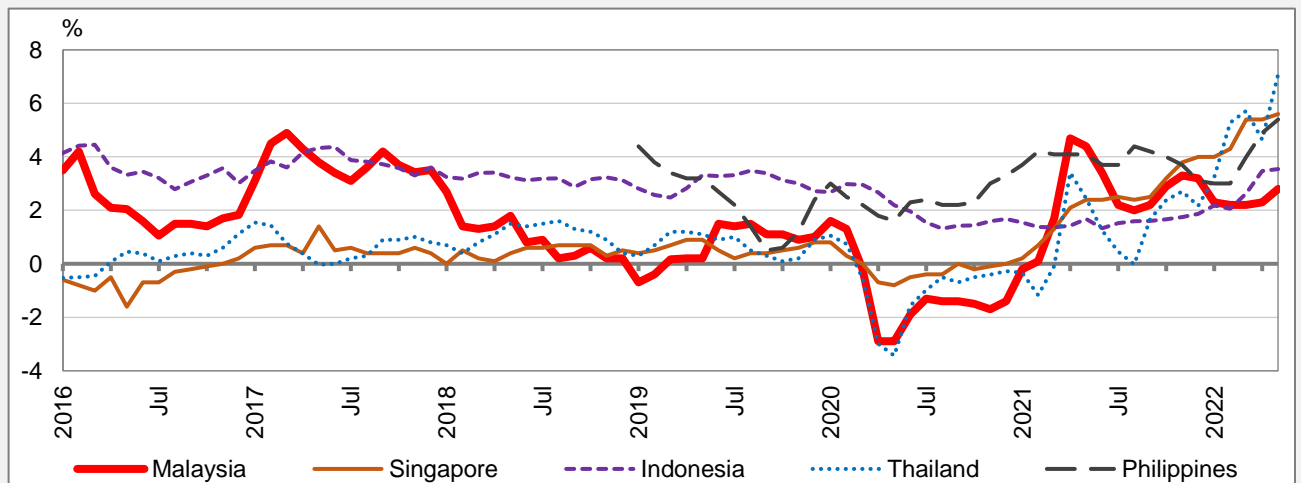
Export growth trend



Industrial production growth trend



Inflation trend



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



BRACES FOR A BUMPY RIDE IN 2H 2022

- **A good start in 1Q 2022.** The Malaysian economy off to a good start in 1Q 2022 as real GDP increased by 5.0% yoy and 3.9% qoq. This was attributable to three reasons: (a) Recovery in domestic demand, which added 4.2 percentage points to 1Q GDP growth, thanks to the reopening of economy, and also continued expansion in exports though was offset by higher imports; (b) Low-base effect; and (c) Changes in inventories, which added 2.2 percentage points to GDP growth in 1Q, are expected to remain a tailwind for economic growth this year. Faced with the persistent supply disruptions, businesses had been relying on inventories to keep up with the recovery consumer spending amid rising inflation. However, increased costs; higher cost of raw materials; and the shortage of workers would restrain companies to bolster production and restock.
- **Recovery momentum continued into 2Q 2022.** Despite restrained by a high base in 2Q 2021 (+15.9% yoy), we estimate real GDP growth to increase by 6.0%-6.5% yoy in 2Q due to: (a) The reopening of economy, including international borders help to revive international tourists and boost demand for local services; (b) Hari Raya festive celebration spending effect; and (c) The EPF's fourth withdrawal amounting to at least RM40.1 billion, of which 40% of the withdrawal will be for the purpose of supplementing daily/monthly essential expenditure.

Retail sales increased by 20.9% in April and 29.9% in May (9.4% in 1Q) while wholesale trade rose by 11.5% in April and 11.7% in May (6.8% in 1Q). Industrial output and manufacturing production expanded by 4.1% and 6.9% in May respectively (4.6% and 6.2% in April respectively; 4.5% and 6.3% respectively in 1Q 2022). Buoyed by continued demand and high prices of crude oil and palm oil, gross exports still going strong to increase by 20.8% in April and 30.5% in May (22.2% in 1Q).

- **But, rising inflation and increased business costs are dampener.** Consumer inflation is creeping higher from 2.2% in 1Q to 2.3% in April and 2.8% in May, with food inflation increasing from 3.8% in 1Q to 4.1% in April and 5.2% in May. **Core inflation**, which measures the underlying inflation trends exclude volatile food and energy, has increased steadily to 2.4% in May (April: 2.1% and 1.8% in 1Q). Bank Negara Malaysia (BNM) also tracks core inflation when setting the monetary policy.

The Government has implemented various administrative measures such as subsidies and price ceiling on cooking oil, fuel, chicken and eggs as well as electricity and gas. This will offer some relief and protect consumers by keeping prices low in the current environment of rising consumer price pressures and cost of living. **SERC estimates headline inflation to increase by 3.0%-3.5% in 2022**, higher than BNM's estimated between 2.2% and 3.2%.

- **Taking a toll on consumer spending and business investment.** Increasing prices of goods and services are expected to crimp the lower and middle-income households' spending power, leaving them with reduced disposable income for spending.

Soaring cost of raw materials, the supply disruptions, higher operating costs and the workers shortage have impacted businesses' working capital and cash flow. These costs and supply constraints coupled with lingering concerns about rising risk of the US recession and the consequential impact on domestic economy, businesses and investors as they would adopt a cautious stance amid increasing expectations of the 15th General Election will be calling soon.

- **Exports still going strong, but will moderate in 2H 2022.** Exports continued to increase strongly by 20.8% in April and 30.5% in May respectively (22.2% in 1Q), supported by resilient demand of electronics and electrical products, crude oil, liquefied natural gas (LNG), and petroleum products, palm oil and palm-based products, chemical and chemical products, machinery, equipment and parts, manufactures of metal, iron and steel products, etc.

Exports are expected to grow at more moderate pace in 2H 2022 due to the weakening global economy; the impact of global monetary tightening; and the moderating prices. **We have revised our exports growth estimate to 10.2% in 2022** (26.0% in 2021).

- **We are keeping our GDP estimate of 5.2% in 2022** (3.1% in 2021), **expecting a moderate pace of economic growth between 4.5%-5.0% in 2H vs. estimated 5.0%-6.5% in 1H 2022.** Entering the 2H 2022 and 2023, there is a growing danger of global stagflation and the US economy could slip into recession. Stronger consumer prices and costs pressure as well as rising cost of living are expected to weigh on domestic demand.
- **Bank Negara Malaysia to maintain a delicate balancing act between growth and inflation.** Both the headline and core inflation have been trending up in recent months, due to supply constraints cum cost driven and partly due to recovering consumer demand.

We expect BNM to continue its gradual and measured pace of policy rate adjustments, depending on the incoming data, assessing the implications of evolving external and domestic developments on economic growth prospects and inflation trajectory, especially to anchor inflation expectations.

BNM raised its overnight policy rate (OPR) for the second time this year to 2.25% in its July meeting, marking two successive rate hikes. SERC expects the central bank to raise the OPR by another 25 basis points (bps) to 2.50% at end-2022.

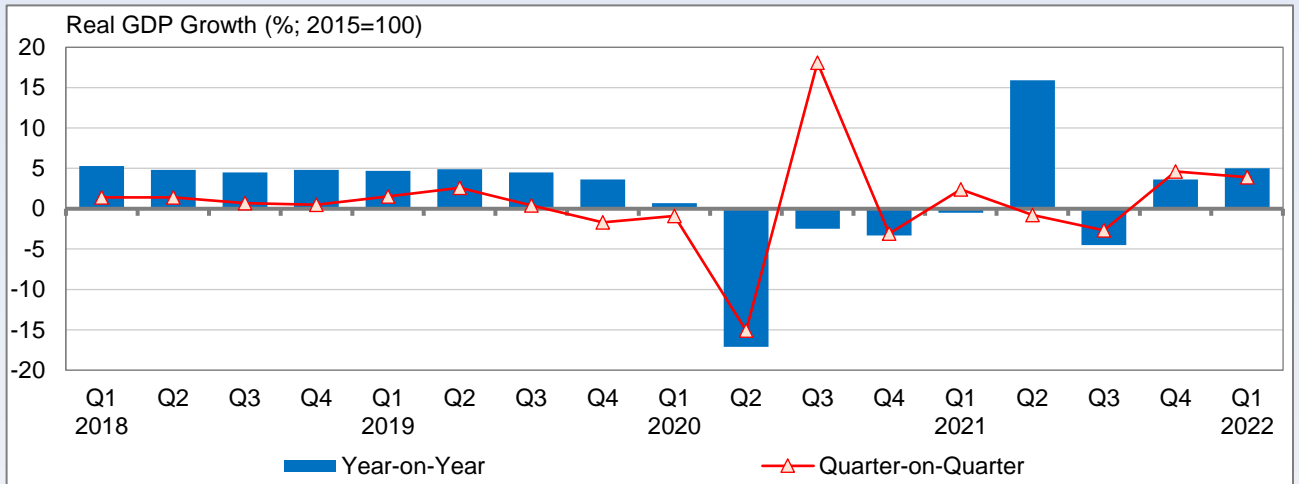
Real GDP growth (% , YoY)

Economic Sector [% share to GDP in 2021]	2019	2020	2021	2022 Q1	2022E
By kind of economic activity					
Agriculture [7.1%]	1.9	-2.4	-0.2	0.2	1.5
Mining & Quarrying [6.7%]	-0.6	-9.7	0.3	-1.1	1.8
Manufacturing [24.3%]	3.8	-2.7	9.5	6.6	4.8
Construction [3.7%]	0.4	-19.3	-5.2	-6.2	6.5
Services [57.0%]	6.2	-5.4	1.9	6.5	6.1
By type of expenditure					
Private Consumption [58.8%]	7.7	-4.2	1.9	5.5	6.5
Public Consumption [13.8%]	1.5	5.0	5.3	6.7	1.0
Private Investment [15.6%]	1.6	-11.9	2.6	0.4	5.0
Public Investment [4.5%]	-10.7	-21.2	-11.3	-0.9	9.4
Exports of Goods and Services [69.1%]	-1.0	-8.6	15.4	8.0	4.4
Imports of Goods and Services [63.1%]	-2.4	-7.9	17.7	11.1	4.9
Overall GDP	4.4	-5.5	3.1	5.0	5.2

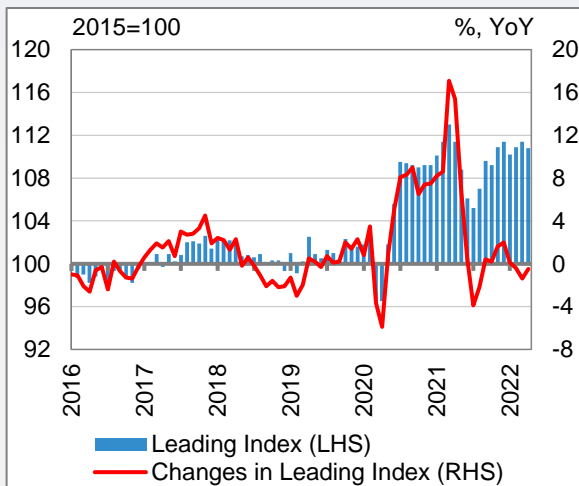
Source: Department of Statistics, Malaysia (DOSM); SERC estimates and forecast

Spotlight on the Malaysian Economy

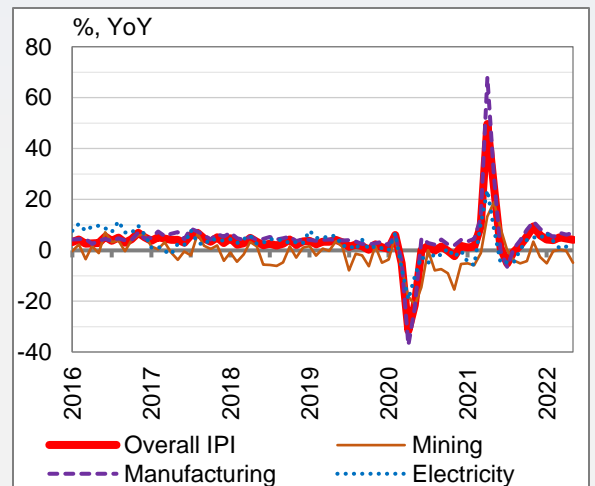
The economic recovery is on track but downside risks remain



Leading Index (LI) expects better economic recovery ahead

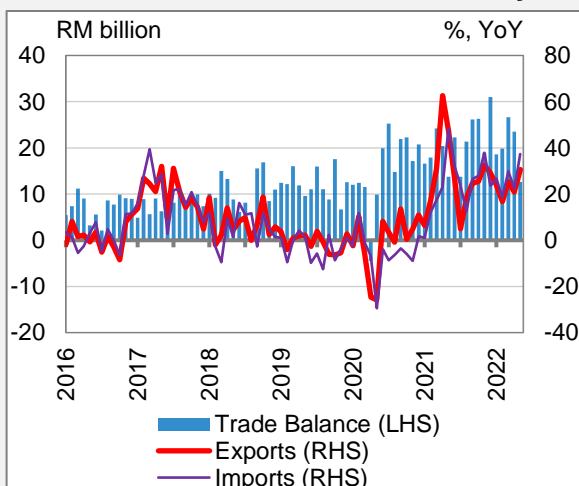


Industrial production growth sustained on solid growth in manufacturing output

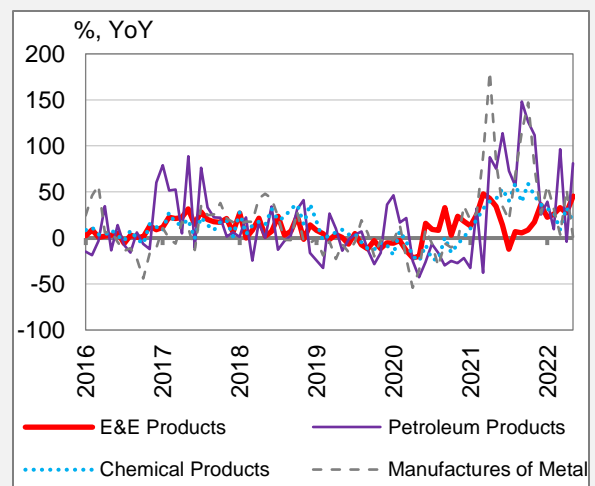


External Sector

Exports registered double-digit growth for ten consecutive months in May



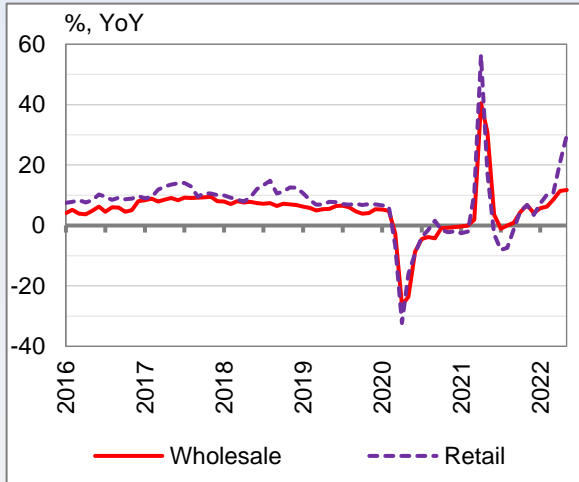
Exports by major products



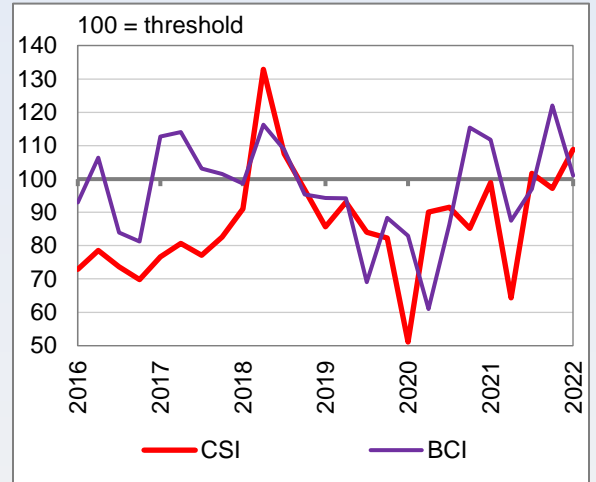
Spotlight on the Malaysian Economy (cont.)

Domestic Demand continued to support the overall growth

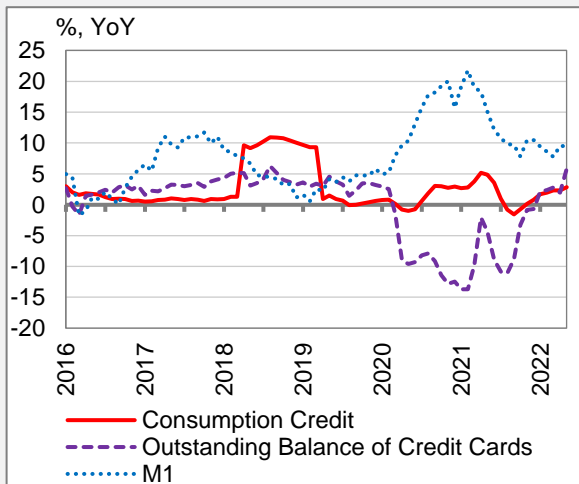
Both wholesale and retail trade sales value hit record-high in May



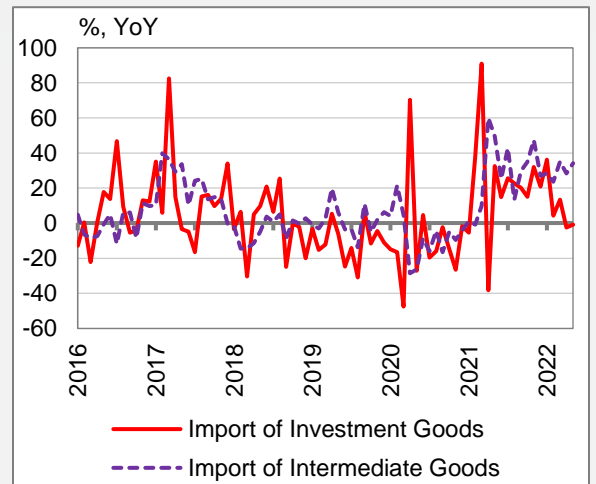
MIER's Consumer Sentiments Index (CSI) and Business Conditions Index (BCI)



Selected private consumption indicators



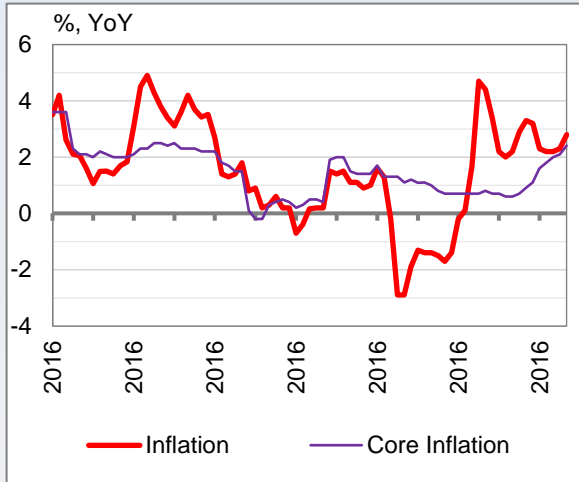
Selected private investment indicators



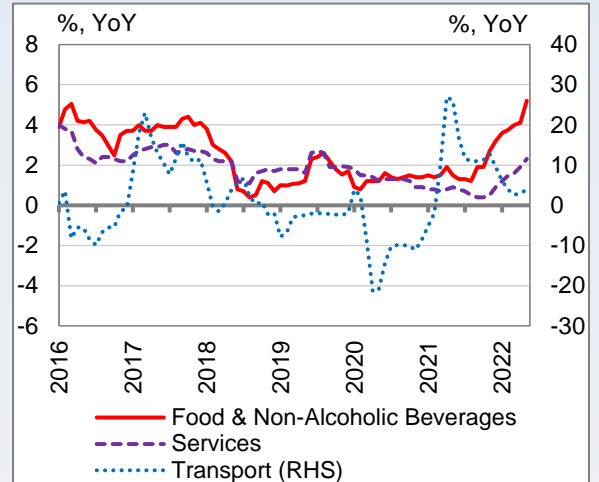
Spotlight on the Malaysian Economy (cont.)

Price Indicators and Labour Market

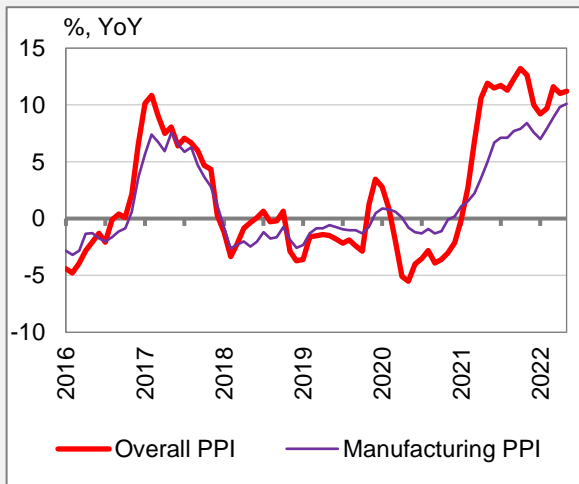
Headline inflation is buffered by price subsidies and controls; core inflation trending higher



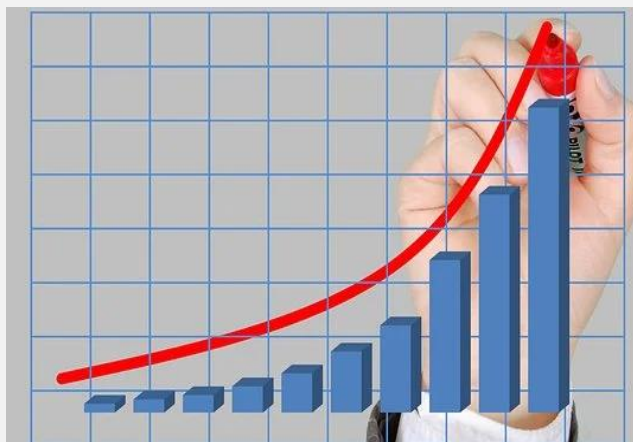
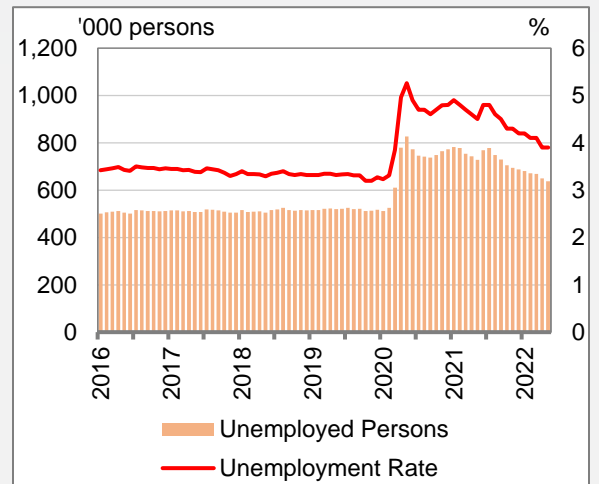
Food prices increased higher to 5.2% in May and prices of services also rising



Producer prices to remain elevated and stay longer



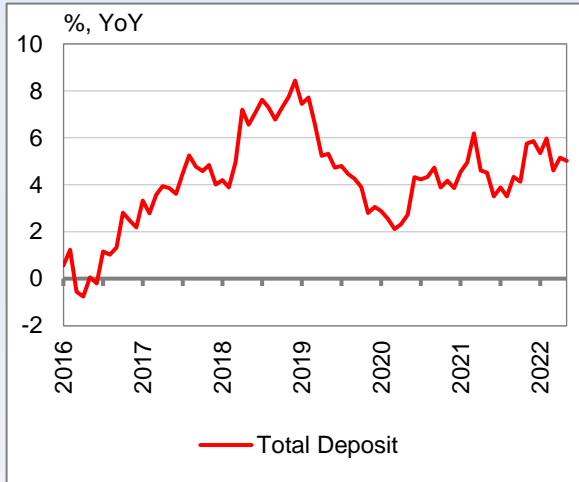
Unemployment rate registered below 4% since Apr amid the shortage of workers



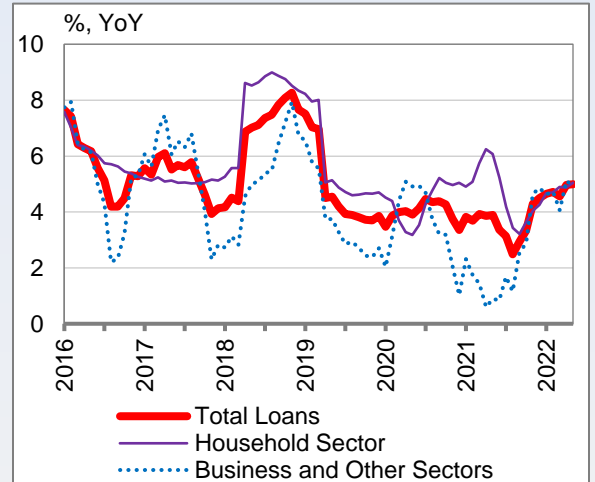
Spotlight on the Malaysian Economy (cont.)

Banking and Financial Indicators

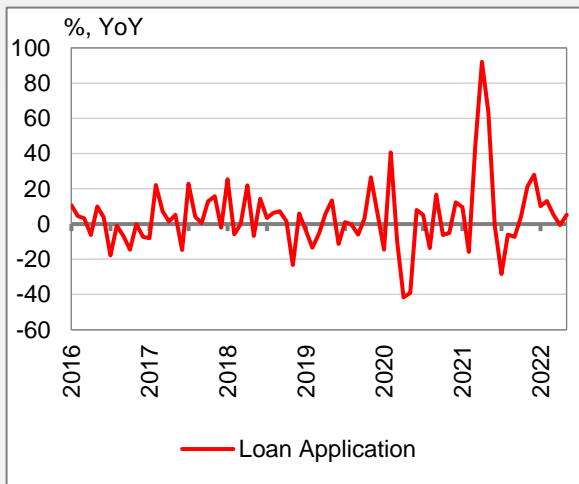
Banking deposit growth sustained steadily



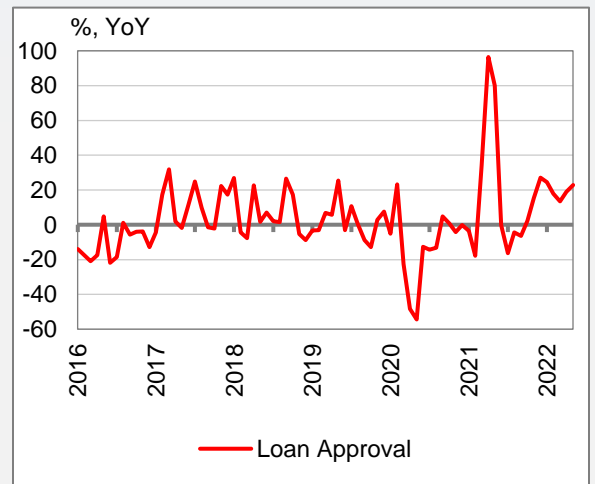
Total outstanding loan growth continued its upward trend as higher disbursements for most sectors



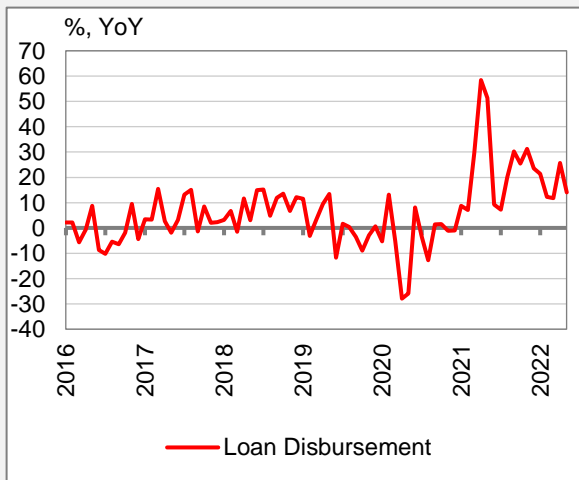
Loan applications growth



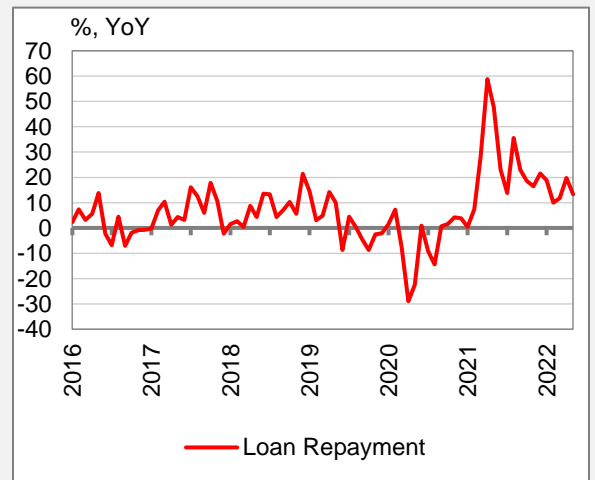
Loan approvals growth



Loan disbursements growth

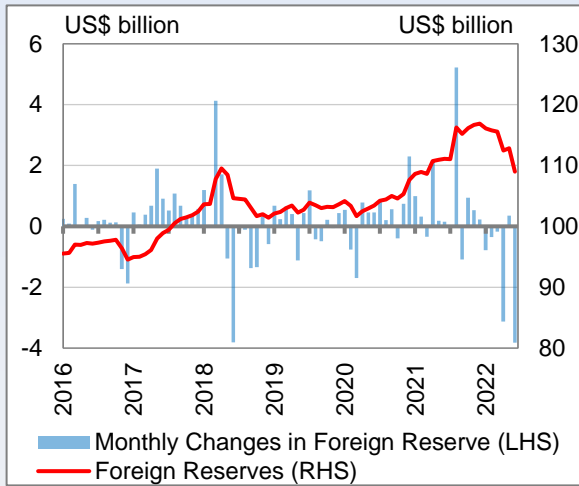


Loan repayments growth

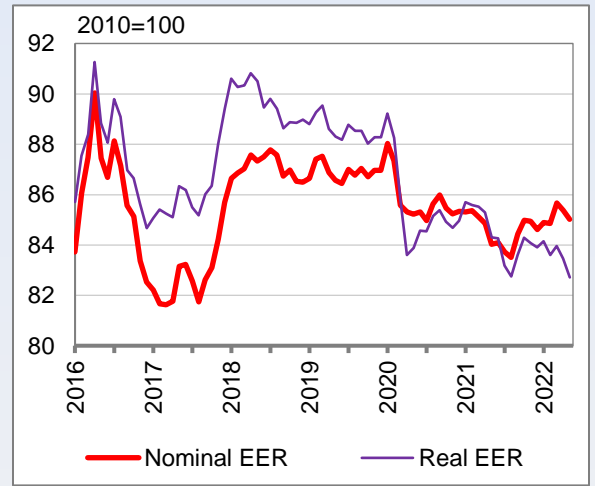


Spotlight on the Malaysian Economy (cont.)

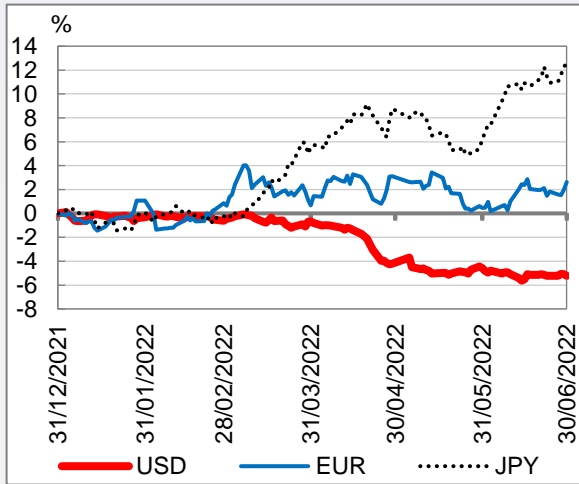
Foreign reserves declined substantially in 1H 2022



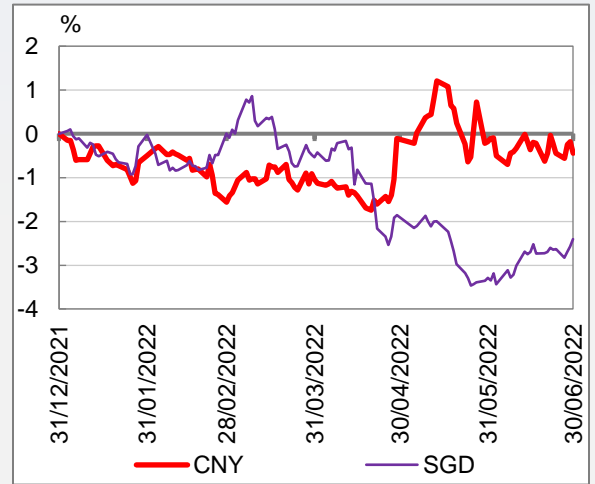
Ringgit's Effective Exchange Rate (EER)



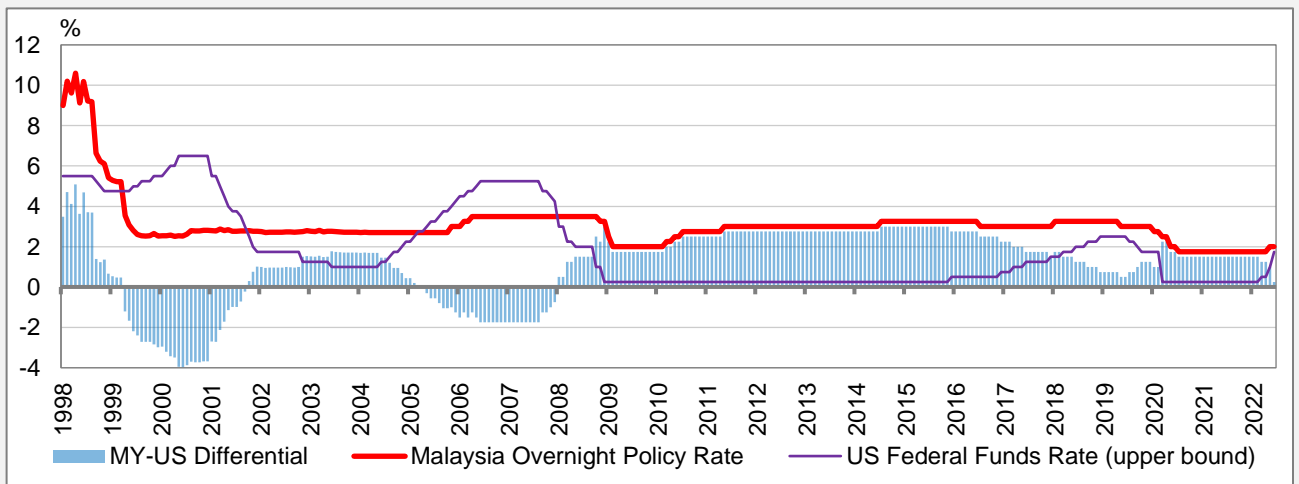
The Ringgit against the US dollar, euro and Japanese yen



The Ringgit against the Chinese renminbi and Singapore dollar



Malaysia-US's interest rate differentials



Source: Department of Statistics, Malaysia (DOSM); Malaysian Institute of Economic Research (MIER); Bank Negara Malaysia (BNM); Bank for International Settlements; Federal Reserve



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The Associated Chinese Chambers of Commerce and Industry of Malaysia (ACCCIM)'s Socio-Economic Research Centre (SERC Sdn. Bhd.) was established as an independent and non-profit think tank on 19 October 2010. Officiated by YAB Prime Minister on 28 April 2011, SERC is funded by ACCCIM SERC Trust.

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