Economic Update

Malaysia- GDP & BOP 1Q17

Real GDP growth surprised on the upside in 1Q17

Real GDP growth rose by 5.6% in 1Q17, exceeding market expectations

Malaysia's real GDP growth rose by 5.6% yoy in 1Q17 (4.5% in 4Q16), significantly higher than market expectations of 4.7%. The positive upside surprise was attributed to strong investment activity during the quarter, where growth in gross fixed capital formation rose by 10% yoy, its first double digit growth in four years. Growth in private investment rose sharply by 12.9% yoy in 1Q17, significantly higher than 4.9% yoy in 4Q16, reflecting strong domestic and external demand in the first quarter of this year.

Private consumption driven by employment and wage growth

Growth in private consumption rose further by 6.6% yoy in 1Q17, higher than the 6.1% yoy in the previous quarter. On a seasonally adjusted basis, private consumption activity grew by 2.8% qoq in 1Q17 (2% qoq growth in 4Q16), supported by healthy expansion in employment and wage growth, as well as implementation of selected Government measures (such as BRIM cash transfers). We believe that private consumption activity will continue to be supported by steady wage growth and better consumer sentiment in the quarters ahead. Domestic demand rose strongly by 7.7% yoy in 1Q17.

Net exports was a drag on GDP growth from higher imports

On external demand, growth in exports rose by 9.8% yoy in 1Q17, while imports also surged by 12.9% yoy, its strongest yoy level in 27 quarters. Growth in imports also rose sharply from 1.6% yoy in 4Q16 to 12.9% in 1Q17, due to high imports of intermediate goods and imports capital and transport equipment goods (including a floating structure, oil and gas vessels and several aircrafts). As a result, the net exports contribution to GDP fell from 0.5 percentage points in 4Q16 to -1.2% percentage points in 1Q17.

Growth in manufacturing sector rose sharply in 1Q17

In tandem with steady global economy, growth in manufacturing sector rose sharply higher by 5.6% yoy in 1Q17 (4.7% in 4Q16), supported by strong output of electronics and electrical (E&E) products, as reflected in healthy global demand for semiconductors, as well as higher ouput in domestic-oriented industries. Services sector remains stable at 5.8% yoy in 1Q17. Growth in the services sector rose slightly by 5.8% yoy (5.5% in 4Q16), supported by wholesale and retail sub-sector improved in line with higher household spending.

Revising our real GDP growth forecast to 4.8% in 2017

We believe that the economic growth momentum will continue in the months ahead, partly on the back of strong export performance as well as domestic demand. With strong 1Q17 GDP growth and in view of higher global growth, we are revising upward our real GDP growth forecast to 4.8% for 2017, from our earlier expectation of 4.4% (4.2% in 2016).

Revising our current account surplus forecast to RM18.5bn for 2017

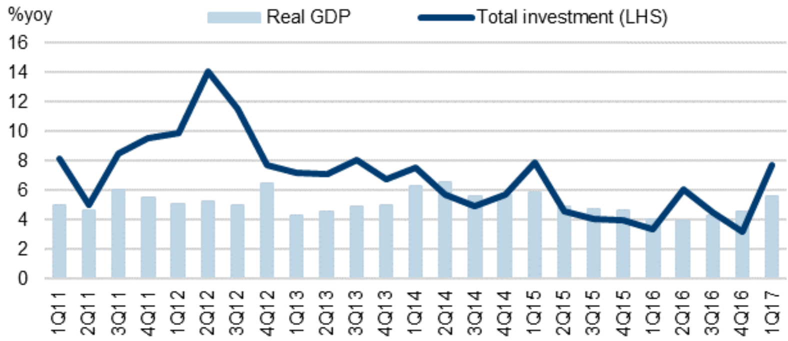
While current account surplus moderated in 1Q17, we believe the stabilization in commodity prices and strong exports performance will continue to support the current account surplus going forward. As such, we are also revising our current account surplus forecast from RM15bn previously to RM18.5bn for 2017, on higher net inflows from goods account.

Economic Research
(603) 2146 7540
alan.tan@affinhwang.com
izzuddin.yussof@affinhwang.com
maisarah.razali@affinhwang.com

Real GDP growth surprised on the upside by 5.6% yoy in 1Q17

Malaysia's real GDP growth rose by 5.6% yoy in 1Q17 (4.5% in 4Q16), significantly higher than market expectations of 4.7%. The positive upside surprise was attributed to strong investment activity during the quarter, where growth in gross fixed capital formation rose by 10% yoy, its first double digit growth in four years.

Fig 1: Real GDP growth vs total investment growth



Source: Bank Negara Malaysia (BNM)

The strong investment growth was driven mainly by private investment, which rose sharply by 12.9% yoy in 1Q17, significantly higher than 4.9% yoy in 4Q16, reflecting strong domestic and external demand in the first quarter of this year. Strong increases in capital spending was recorded in machinery and equipment, structures and other types of assets, reflecting better business sentiments on the back of improved international economic environment and more stable financial markets in 1Q17. Similarly, growth in public investment turned positive and rebounded by 3.2% yoy in 1Q17, after contracting for two consecutive quarters since 2Q16, supported by higher spending on fixed assets by public corporations.

Fig 2: GDP by expenditure component

	2Q16	3Q16	4Q16	1Q17	2Q16	3Q16	4Q16	1Q17	2Q16	3Q16	4Q16	1Q17
	%yoy				%qoq				% pts to GDP growth			
GDP by Expenditure Components												
Total Consumption	6.0	5.5	3.5	6.8	2.2	5.6	4.1	-4.9	3.9	3.6	2.4	4.4
Private consumption	6.2	6.3	6.1	6.6	0.6	7.1	-2.0	1.1	3.2	3.4	3.1	3.6
Public consumption expenditure	5.5	2.1	-4.2	7.5	9.7	-0.5	31.6	-25.2	0.7	0.3	-0.7	0.9
Total Investment	6.1	2.0	2.4	10.0	10.2	-6.3	-0.8	7.4	1.7	0.5	0.6	2.5
Private investment expenditure	5.6	4.8	4.9	12.9	15.2	-11.1	-23.7	44.5	1.1	0.8	0.6	2.3
Public investment expenditure	7.7	-3.8	-0.4	3.2	-1.5	6.8	51.0	-35.1	0.5	-0.3	0.0	0.2
Domestic Demand	6.1	4.5	3.2	7.7	4.4	2.1	2.8	-1.7	5.5	4.1	3.0	7.0
Net exports	-1.2	8.2	6.4	-14.5	-3.3	24.0	-4.3	-25.6	-0.1	0.7	0.5	-1.2
Exports	2.0	-0.6	2.2	9.8	0.3	4.4	5.5	-0.7	1.4	-0.4	1.6	6.9
Imports	2.4	-1.8	1.6	12.9	0.8	2.0	7.0	2.7	1.5	-1.1	1.0	8.1
Changes in inventories	-160.9	226.6	-211.1	-21.0	-163.0	41.7	-172.1	22.7	-1.5	-0.5	1.0	-0.2
GDP (2010 real prices)	**4.0**	**4.3**	**4.5**	**5.6**	**2.4**	**3.5**	**3.4**	**-3.6**	**4.0**	**4.3**	**4.5**	**5.6**

Source: Bank Negara Malaysia (BNM)

Private consumption driven by employment and wage growth

Growth in private consumption rose further by 6.6% yoy in 1Q17, higher than the 6.1% yoy in the previous quarter. On a seasonally adjusted basis, private consumption activity grew by 2.8% qoq in 1Q17 (2% qoq growth in 4Q16), supported by healthy expansion in employment and wage growth, as well as implementation of selected Government measures (such as BRIM cash transfers). We believe that private consumption activity will continue to be supported by steady wage growth and better consumer sentiment in the quarters ahead.

This was also reflected in the latest MIER index, with consumer sentiment index improving from 69.8 in 4Q16 to 76.6 in 1Q17. Despite the unemployment rate remained at around 3.4-3.5% level, employment growth in 1Q17 was actually the strongest in two years at 1.8% yoy, as compared to the growth of 0.9% yoy in 4Q16.

Similarly, growth in public consumption rose by 7.5% yoy in 1Q17, the highest quarterly yoy growth in three years, while on a seasonally adjusted basis, it increased by 13.4% qoq, due to higher spending for both emoluments and supplies and services during the quarter.

Net exports was a drag on GDP growth from higher capital goods

On external demand, growth in exports rose by 9.8% yoy in 1Q17, while imports also surged by 12.9% yoy, its strongest yoy level in 27 quarters. While the increase in export growth in 1Q17 was partly contributed by low base effect, the better performance was also reflected in a broad-based expansion in both manufactured (especially E&E products) and commodities exports. However, growth in imports rose sharply from 1.6% yoy in 4Q16 to 12.9% in 1Q17, due to high imports of intermediate goods and imports capital and transport equipment goods (including a floating structure, oil and gas vessels and several aircrafts). As a result, the net exports contribution to GDP fell from 0.5 percentage points in 4Q16 to -1.2% percentage points in 1Q17.

Growth in agriculture sector rebounded in line with commodity prices

On a sectorial basis, growth in agriculture sector experienced its highest yearly growth in 21 quarters at 8.3% yoy in 1Q17, after four consecutive quarters of contraction. On a seasonally adjusted basis, the sector grew as much as 5.4% qoq, reflecting a strong positive momentum for the sector. This was attributed to the recovery in crude palm oil yields as well as a double-digit expansion in rubber production.

Fig 3: GDP by kind of economic activity

	2Q16	3Q16	4Q16	1Q17	2Q16	3Q16	4Q16	1Q17	2Q16	3Q16	4Q16	1Q17
	%yoy				%qoq				% pts to GDP growth			
GDP by Economic Activity												
Agriculture, Forestry and Fishing	-7.8	-6.1	-2.5	8.3	5.7	17.7	-7.7	-5.7	-0.7	-0.6	-0.2	0.6
Mining and Quarrying	2.1	2.9	5.0	1.6	-1.3	-5.4	10.4	-1.4	0.2	0.2	0.4	0.2
Manufacturing	4.2	4.3	4.7	5.6	5.3	-0.1	4.6	-4.1	1.0	1.0	1.1	1.3
Construction	8.9	7.9	5.1	6.5	-5.4	9.6	-3.6	6.5	0.4	0.4	0.2	0.3
Services	5.7	6.2	5.5	5.8	2.2	4.1	4.1	-4.4	3.0	3.3	3.0	3.1
Import duties	4.4	5.8	1.6	8.4	-4.2	0.8	10.4	1.7	0.1	0.1	0.0	0.1
GDP (2010 real prices)	**4.0**	**4.3**	**4.5**	**5.6**	**2.4**	**3.5**	**3.4**	**-3.6**	**4.0**	**4.3**	**4.5**	**5.6**

Source: Bank Negara Malaysia (BNM)

However, growth in mining activity remained slow in 1Q17

Despite the significant recovery in oil price as compared to last year, growth in mining and quarrying activity only rose slightly by 1.6% yoy in 1Q17 (5.0% yoy in 4Q16). This was attributed to the global initiative to reduce oil production, where Petronas joined along with OPEC members in capping their production until June 2017. Petronas has agreed to cut their production by approximately 20,000 barrel per day, representing approximately 3.0% of their total output. We believe growth in mining and quarrying activity will likely to remain slow for the whole of 2017, as there is some possibility that OPEC will likely call for an extension of the production freeze until the end of this year.

Growth in manufacturing sector rose sharply in 1Q17

In tandem with steady global economy, growth in manufacturing sector rose sharply higher by 5.6% yoy in 1Q17 (4.7% in 4Q16), supported by strong output of electronics and electrical (E&E) products, as reflected in healthy global demand for semiconductors, as well as higher output in domestic-oriented industries, mainly in demand for food-related products and a rebound in the motor vehicle production. Manufacturing sector remained as one of the sectors that hires the most employees in the country, with approximately 16.9% of the total employments coming from the sector.

Construction sector continues to hold up in 1Q17

Growth in the construction sector improved slightly to 6.5% yoy in 1Q17, after experiencing the slowest yearly growth in 4Q16 at 5.1%, supported by civil engineering activity in the petrochemical, power plant and transportation segments. However, we opine that the construction sector will continue to be supported by various Government projects, along with the improving demand for residential properties coming from strong employment and wage growth.

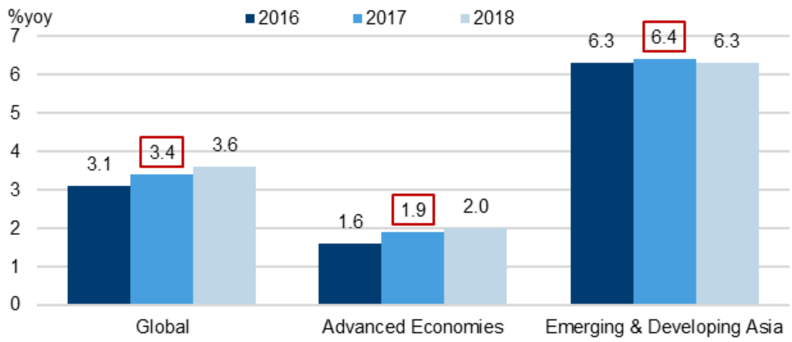
Services sector remains stable at 5.8% yoy in 1Q17

Growth in the services sector rose slightly by 5.8% yoy (5.5% in 4Q16), supported by wholesale and retail sub-sector improved in line with higher household spending. According to BNM, the finance and insurance sub-sector also registered higher growth, supported by improvements in loan growth and capital market activity amid higher issuance of IPOs. Services sector, which has the largest share of about 54.2% from overall GDP, contributed 3.1% to GDP growth in 1Q17. As a side note, motor vehicles recorded its first yearly growth after four consecutive quarters of contraction, growing by 3.5% yoy during the quarter.

Revising our real GDP growth forecast to 4.8% in 2017

In the latest World Economic Outlook (WEO) released by International Monetary Fund (IMF), the global GDP growth forecast was revised higher to 3.5% yoy in 2017, a 0.1 percentage point increase from 3.4% projected in January WEO update, in view of healthy global growth momentum since early this year. Likewise, since December last year, the global semiconductor sales data released by Semiconductor Industrial Sales (SIA) grew by double-digit growth for four consecutive months, contributed from robust performance from US, Europe, Japan and China economies. In March, it recorded the highest growth since October 2010, bringing the total global sales to US$30.88bn. For the full year forecast, SIA also expect the global Growth sales to pick up from 1.1% yoy in 2016 to 3.3% yoy in 2017.

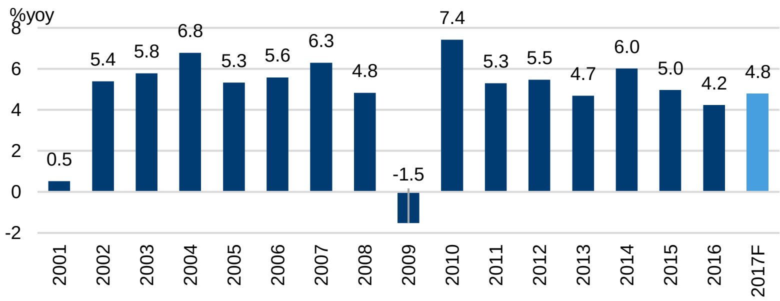
Fig 4: IMF GDP growth projection



Source: IMF

In tandem with rising growth from global semiconductor sales, Malaysia's manufacturing sector also improved since early this year, where in the month of April, Malaysia's manufacturing PMI has finally crossed the 50-level threshold, a level which divides between expansion and contraction phase of the economy. This is a healthy signal to our country's manufacturing sector, especially after being positioned in contraction level for two straight years. We believe that the momentum will continue further in the months ahead on the back of strong export performance. The demand for electronic-related products, which grew strongly in 1Q17, leading by higher demand from China as well as stability in commodity prices will continue to support country's growth of export in both manufactured goods and commodity goods. With strong 1Q17 GDP growth and in view of likely higher global growth, we are revising upward our real GDP growth forecast for Malaysia to 4.8% for 2017, from our earlier expectation of 4.4% (4.2% in 2016).

Fig 5: Yearly GDP growth



Source: BNM, Affin Hwang estimates

Current account surplus narrowed to RM5.3bn in 1Q17

The country's current account surplus narrowed more-than-expected to RM5.3bn (1.7% of GNI) in 1Q17, lower than the revised RM12.5bn (3.8% of GNI) in 4Q16. In tandem with narrower trade surplus, the surplus in goods account also slowed from RM31.2bn in 4Q16 to RM25.3bn. This is reflected in gross exports, which grew strongly by 21.4% yoy in 1Q17 (2.8% yoy in 4Q16), supported by higher demand from China on electronic-related products and higher commodity prices, while imports rose by 27.7% yoy (5.0% in 4Q16) on higher imports of intermediate goods. As imports grew more than exports in the first quarter, this has narrowed trade surplus to RM18.9bn, as compared to RM27.5bn from the previous quarter.

Fig 6: Quarterly and Yearly Balance of Payments (BOP)

Balance of Payments (RMbn, unless stated otherwise)	2015	2016	1Q15	2Q15	3Q15	4Q15	1Q16	2Q16	3Q16	4Q16	1Q17
Current account	35.2	29.0	10.9	8.2	5.2	10.8	6.2	3.1	7.3	12.5	5.3
(% of GDP)	3.0	2.4	3.9	2.9	1.8	3.6	2.1	1.0	2.3	3.8	1.6
(% of GNI)	3.1	2.4	4.0	2.9	1.9	3.7	2.2	1.1	2.4	3.9	1.7
Goods	109.2	101.4	27.1	23.4	27.5	31.3	23.3	20.1	26.8	31.2	25.3
Services	-20.6	-19.1	-3.4	-4.9	-5.9	-6.5	-5.7	-3.8	-4.2	-5.4	-6.2
Primary income	-32.1	-34.6	-7.7	-4.6	-10.7	-9.1	-6.4	-8.3	-10.7	-9.2	-9.9
Current transfers	-21.3	-18.6	-5.0	-5.7	-5.7	-4.9	-4.9	-5.0	-4.6	-4.1	-3.9
Capital account	-1.1	0.1	0.0	-1.1	0.0	0.0	0.0	0.1	0.0	0.0	0.0
Financial account	-55.4	-1.1	-29.2	0.4	-33.2	6.6	7.8	11.1	-5.8	-14.2	-8.8
Direct investment	-1.8	14.1	-3.4	-2.0	-2.7	6.3	3.8	6.6	2.7	1.0	8.3
Portfolio investment	-26.1	-15.4	-7.9	-11.8	-24.4	18.0	14.1	0.1	-10.6	-19.1	-31.9
Financial derivatives	-0.7	-0.8	0.0	-0.4	-0.1	-0.1	0.5	0.0	-0.1	-1.2	0.6
Other investments	-26.8	1.0	-17.9	14.6	-5.9	-17.6	-10.7	4.5	2.1	5.0	14.2
Errors and omissions	25.1	-13.2	2.6	1.0	45.0	-23.4	-41.6	-5.5	13.2	20.7	1.7
Overall balance	3.8	14.8	-15.7	8.4	17.0	-6.0	-27.6	8.8	14.6	19.0	-1.8
External reserves (Outstanding in RMbn)	409.1	424.2	389.7	398.1	415.1	409.1	381.6	390.4	405.0	424.2	422.2
External reserves (Outstanding in US$bn)	95.3	94.5	105.1	105.5	93.3	95.3	97.0	97.2	97.7	94.5	95.4

Source: BNM

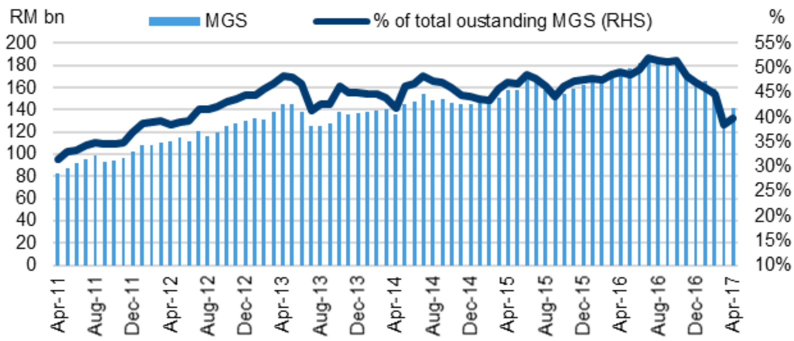
On the other hand, the services account posted a larger deficit of RM6.2bn in the first quarter (-5.4bn in 4Q16), driven by higher outlays from transportation services following the robust activities in trade. Meanwhile, construction services, charges of intellectual's use, as well as insurance & pension services also contributed to higher deficit in services account.

Other components which continued to support country's services account including travel services, which increased by RM14.1bn and manufacturing services on physical goods, which rose by RM10.1bn during the quarter. However, deficit in primary income increased to RM9.9bn in 1Q17 (-RM9.2bn in 4Q16) due to higher income accrued to foreign investors, while secondary income narrowed slightly to RM3.9bn (-RM4.1bn in 4Q16) on lower outward remittances by foreign workers during the quarter.

In the financial account, the deficit narrowed but healthy from RM14.2bn in 4Q16 to RM8.8bn in 1Q17, attributed from larger surplus in direct investment, which recorded a net inflow of RM8.3bn (RM1bn in 4Q16), as incurrence of direct investment liabilities continued to outpace the accumulation of direct investment asset.

Likewise, other investment accounts also showed higher surplus of RM14.2bn in 1Q17 (RM5bn in 4Q16), as well as financial derivatives account, which recorded net inflow of RM0.6bn. Nevertheless, portfolio investment showed net outflow of RM31.9bn, the third straight quarters of outflow, and the largest outflow since December 2008. The significant outflow from portfolio investment was in line with some decline in foreign purchase of Malaysia's debt securities by RM37.4bn during the quarter, mainly concentrated in Malaysian Government Securities (MGS), which posted a total outflow of RM32.6bn. Meanwhile, errors and omissions continued to show net inflow of RM1.7bn in 1Q17, albeit lower than RM20.1bn inflow from the previous quarter. The overall balance of payment declined to RM1.8bn in 1Q17 (+RM19bn in 4Q16).

Fig 7: Foreign holding of Malaysian Government securities (MGS)



Source: CEIC, BPAM

Revising our current account surplus forecast to RM18.5bn for 2017

The current account surplus moderated in 1Q17 to RM5.3bn, mainly due to the strong imports activity on capital goods. Moving forward, the stabilization in commodity prices and strong exports performance should continue to support the current account surplus. As such, we are revising our current account surplus forecast from RM15bn previously to RM18.5bn for 2017, on higher net inflows from goods account.

Malaysia's international reserves climbed to US$96.1 as at 28 April 2017, or RM425.2bn. The current reserves is sufficient to finance 7.9 months of retained imports and 1.1 times short-term external debt. Going forward, we believe that Malaysia's reserves will continue to remain at a healthy and sustainable level, supported by continuation of net buying activities in equity market by foreigners as well as continued current account surplus. Since January to April this year, net equity of foreigners buying into Malaysian equity amounted to RM8.3bn. Meanwhile, foreign purchase of Malaysian debt securities, especially in MGS, showed some pick up in the month of April of about RM5.7bn. We are keeping our forecast unchanged on Malaysia's international reserve, which we believe will hover around US$95-98bn by end-2017. According to the central bank, the total export proceed from December 2016 to March 2017 already amounted to US$1.4bn.

Focus Charts

Chart 1: GDP by components (Demand side)

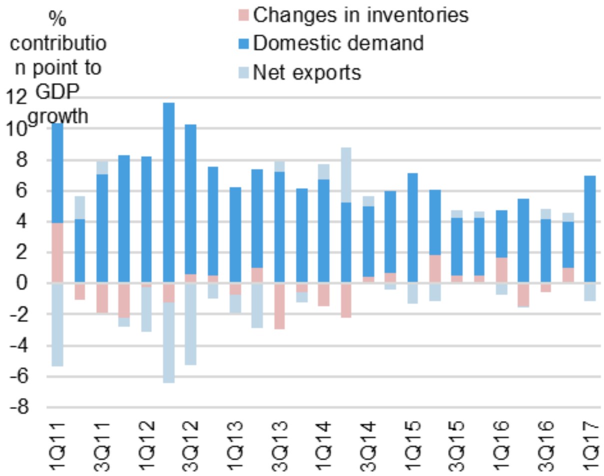


Chart 2: GDP by components (Supply side)

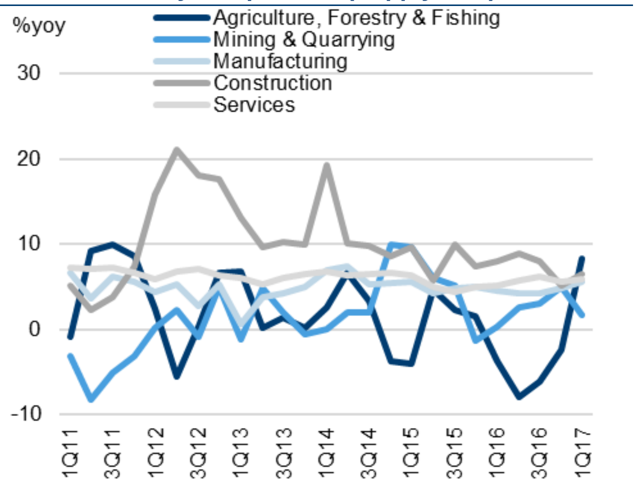


Chart 3: Share in services sector

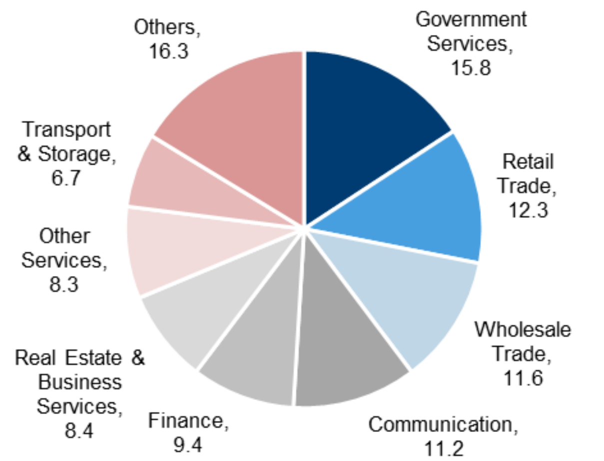


Chart 4: Index of services

Chart 5: Breakdown in manufacturing sector

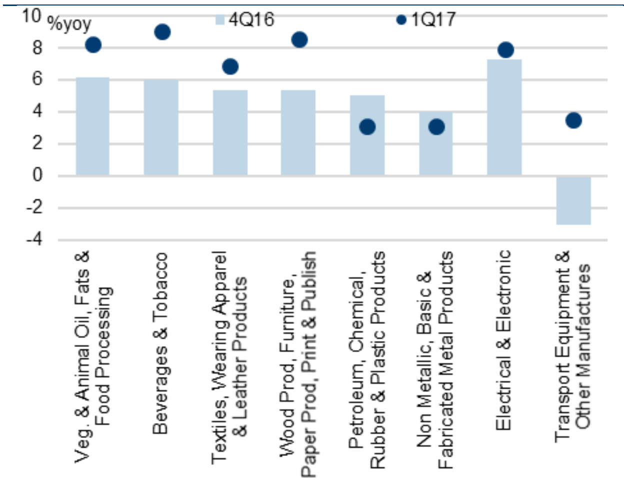


Chart 6: Manufacturing production vs sales

Source: All data for charts sourced from CEIC and BNM

Focus Charts

Chart 7: Breakdown in agriculture sector

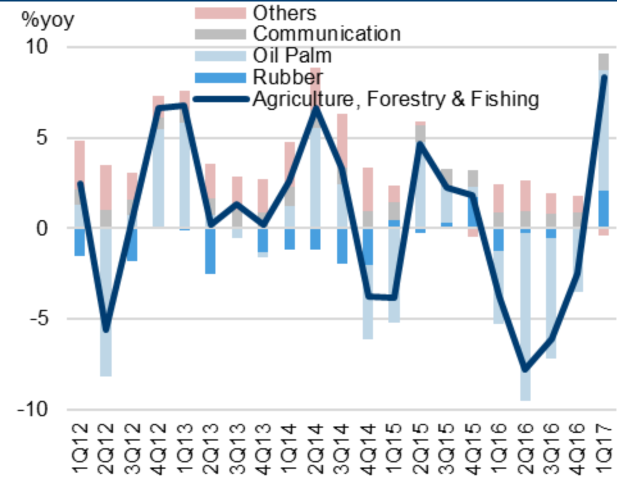


Chart 8: Mining sector

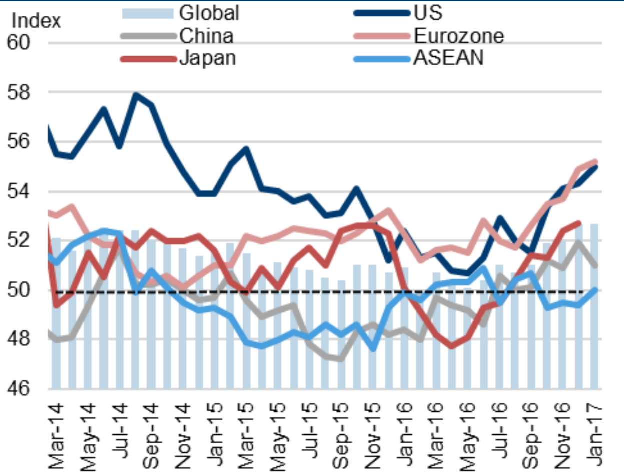


Chart 9: Gross fixed capital formation assets

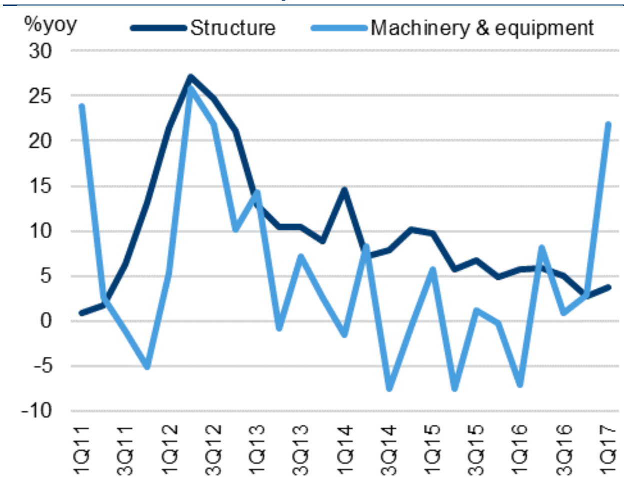


Chart 10: Net exports

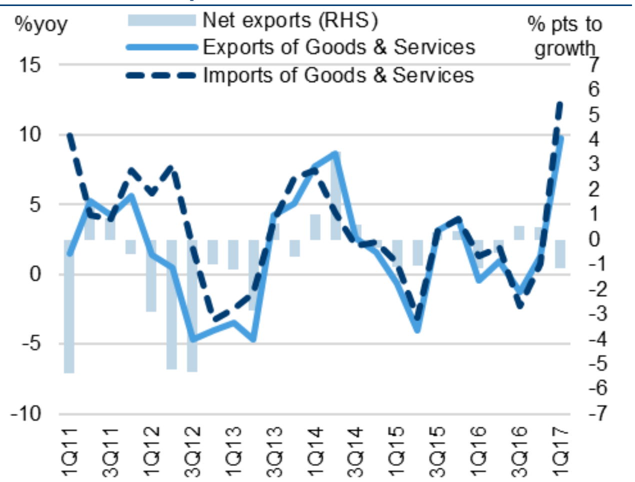


Chart 11: Global manufacturing PMI

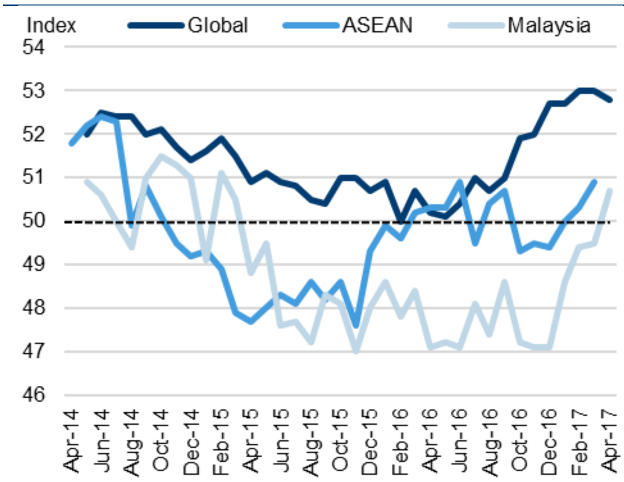
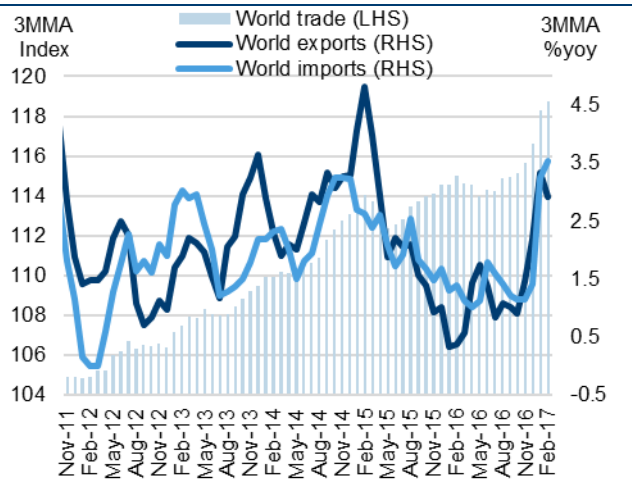


Chart 12: Global trade



Source: All data for charts sourced from CEIC and BNM

Focus Charts

Chart 13: Current account balance

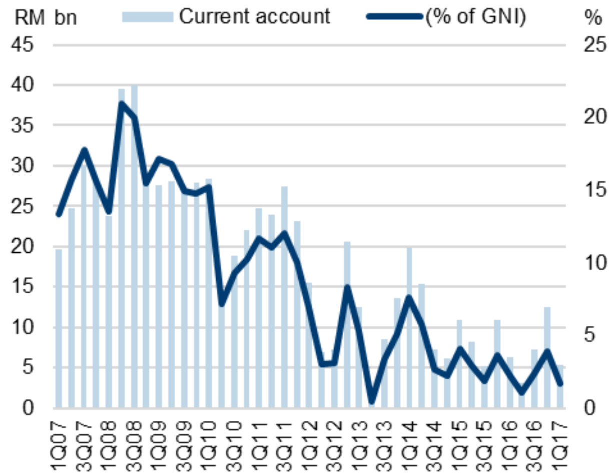


Chart 14: Main components in current account

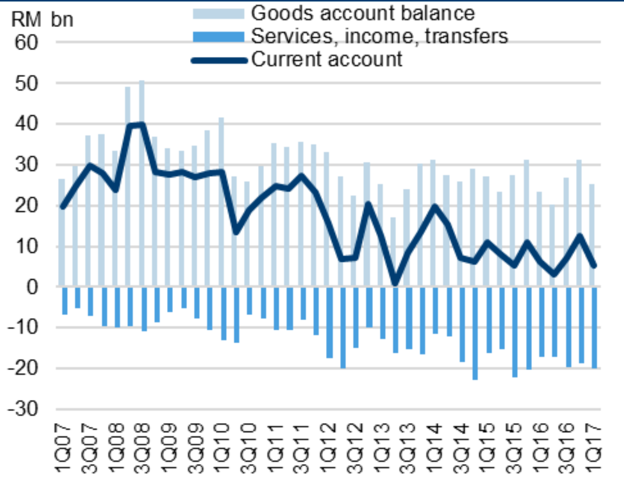


Chart 15: Direct investment and portfolio investment

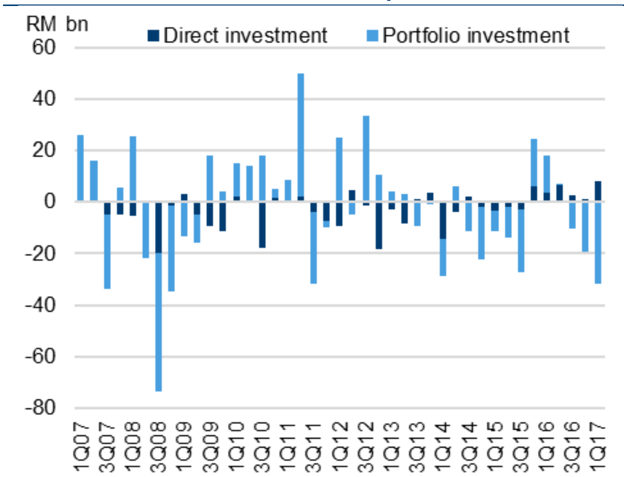


Chart 16: Services account components

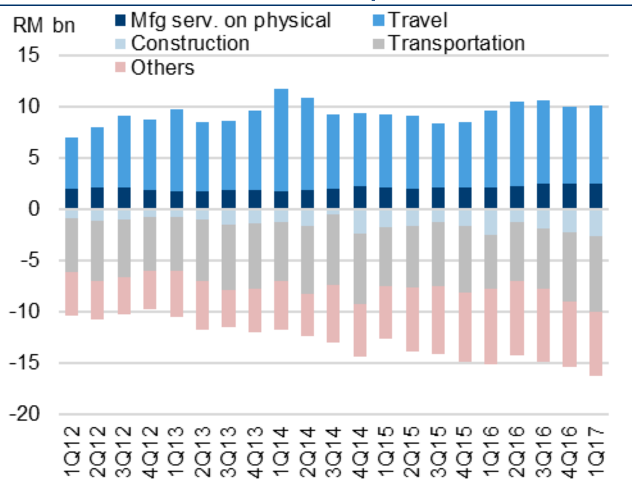


Chart 17: Trade balance

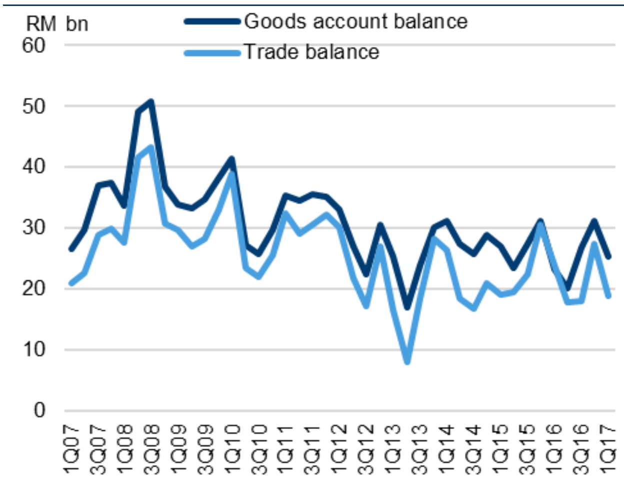
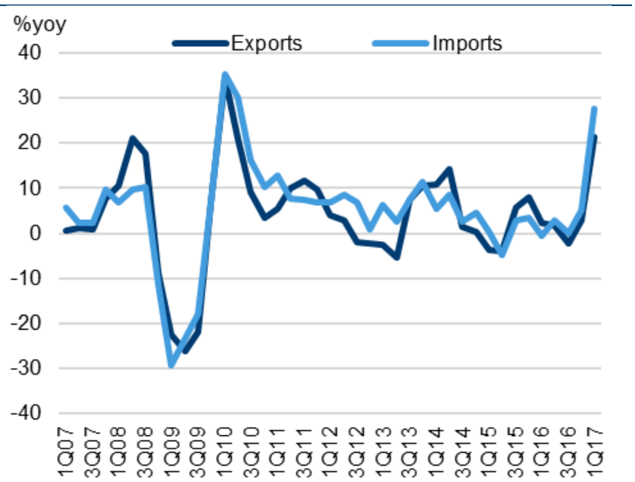


Chart 18: Trade growth



Source: All data for charts sourced from CEIC and BNM

Equity Rating Structure and Definitions

BUY	Total return is expected to exceed +10% over a 12-month period
HOLD	Total return is expected to be between -5% and +10% over a 12-month period
SELL	Total return is expected to be below -5% over a 12-month period
NOT RATED	Affin Hwang Investment Bank Berhad does not provide research coverage or rating for this company. Report is intended as information only and not as a recommendation

The total expected return is defined as the percentage upside/downside to our target price plus the net dividend yield over the next 12 months.

OVERWEIGHT	Industry, as defined by the analyst's coverage universe, is expected to outperform the KLCI benchmark over the next 12 months
NEUTRAL	Industry, as defined by the analyst's coverage universe, is expected to perform inline with the KLCI benchmark over the next 12 months
UNDERWEIGHT	Industry, as defined by the analyst's coverage universe is expected to under-perform the KLCI benchmark over the next 12 months

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A Participating Organisation of Bursa Malaysia Securities Berhad

22nd Floor, Menara Boustead,
69, Jalan Raja Chulan,
50200 Kuala Lumpur, Malaysia.

T : + 603 2146 3700
F : + 603 2146 7630
research@affinhwang.com

www.affinhwang.com