



MONTHLY ECONOMIC UPDATE

2 JULY 2024

ECONOMIC RESEARCH

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KEY TAKEAWAYS

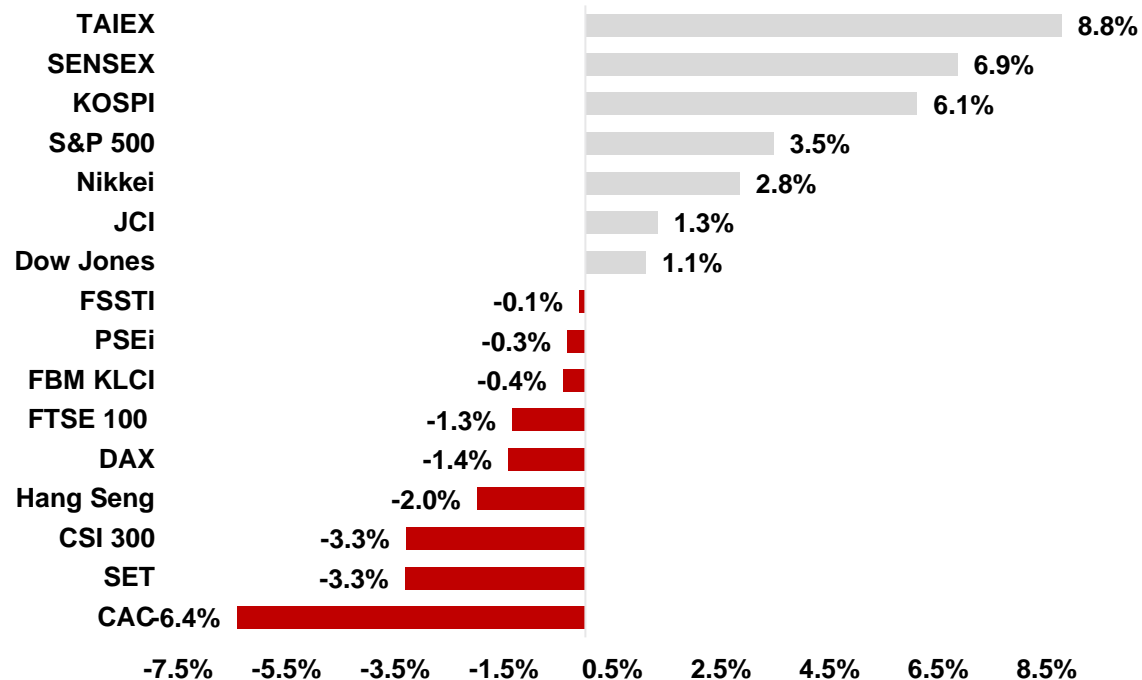
- **Fed projects just one interest rate cut this year.** The U.S. Federal Reserve (Fed) has opted to keep the federal funds rate (FFR) steady at a 23-year high for the seventh time in a row at the conclusion of its June meeting. The stand-pat decision aligned with market expectations as Fed policymakers have consistently emphasised the possibility of prolonged high interest rates. They want to see more evidence that inflation is returning to the 2.0% target before pivoting to easing. Despite a cooler-than-expected May inflation print ahead of the meeting, the Fed penciled in only one rate cut this year in its updated dot plot projections, compared to the three it projected in March. However, markets are not swayed by the hawkish-leaning messages from the Fed and insist on more rate cuts rather than just one for this year. At the time of writing, markets have priced in two Fed rate cuts by the end of this year, with more than a 60% chance of the first cut being delivered in September.
- **ECB cuts rates for the first time in almost five years but gives little hints on future rate path.** The European Central Bank (ECB), at its June policy meeting, delivered a much-anticipated 25bp cut, lowering its main interest rate to 3.75% from an all-time high of 4.00%, where it had remained since September 2023. Despite the rate cut, the ECB anticipates a bumpier disinflationary trend ahead and has raised its inflation forecasts for 2024 and 2025. This, in addition to the ECB policymakers' latest remarks that the ECB is not pre-committing to any specific path for interest rates have dampened market confidence in further rate cuts, with only one more reduction fully priced in by the end of this year.
- **BoE keeps ajar the door for an August rate cut.** At its June meeting, the Bank of England (BoE) kept rates steady at a 16-year high of 5.25%, as largely expected, in a 7-2 decision, mirroring the voting pattern from the previous May meeting where two policymakers voted for a 25bp cut. With U.K. consumer price inflation easing to the 2.0% target in May for the first time in nearly three years, and signs that both wage growth and services inflation may have peaked, the BoE has signalled that a rate cut is on the horizon. Minutes of the meeting revealed that some BoE policymakers who voted to maintain the rate judged the decision as "finely balanced", indicating they are nearing a decision to vote for a rate cut.

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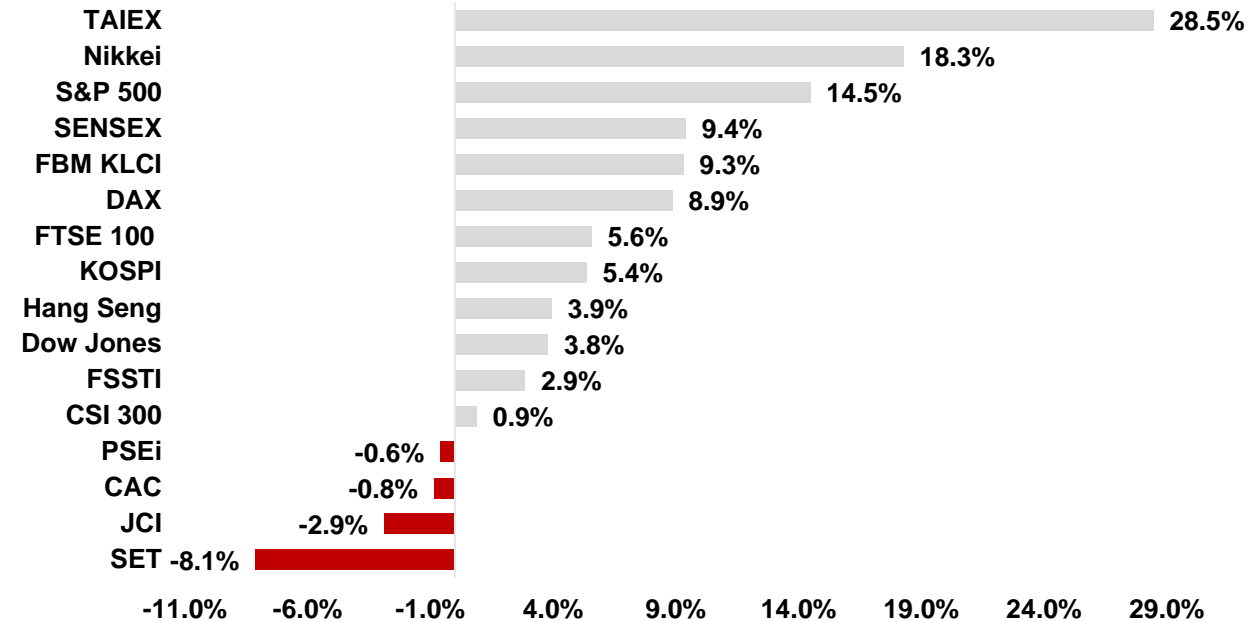
SECTION 1

Malaysia's Financial Market

Monthly Gain/Loss of Major Equity Market, m-o-m%



YTD Gain/Loss of Major Equity Markets, % (As of 28 June 2024)

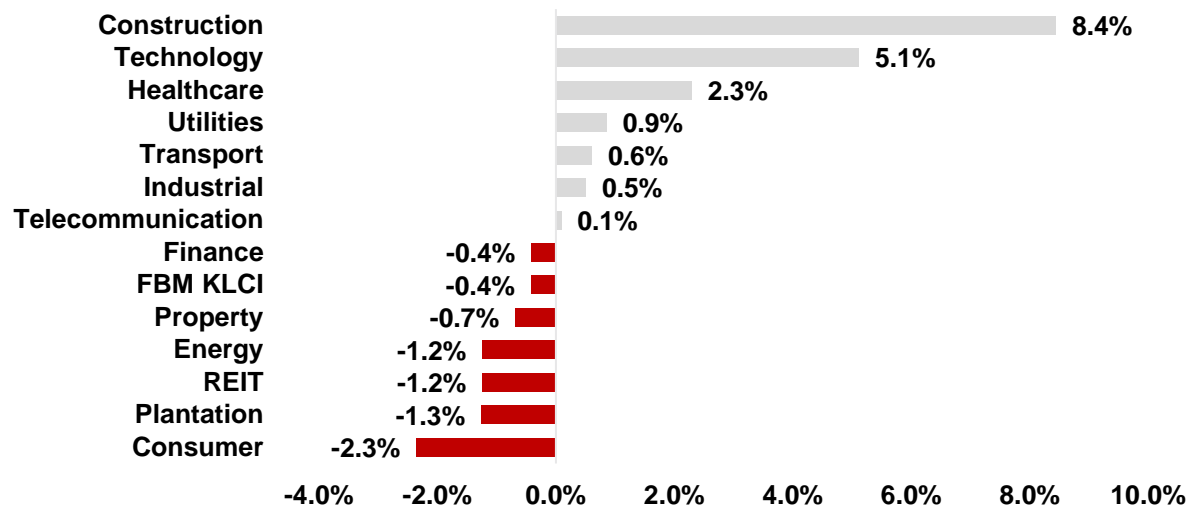


Sources: Bursa, CEIC data

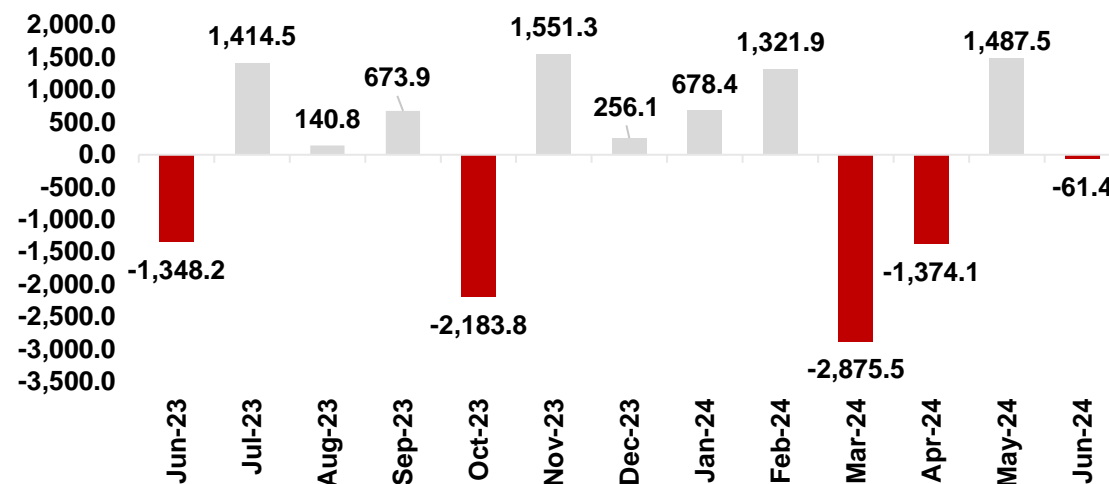
- In June, Taiwan’s TAIEX surged by 8.8% as investors increased their holdings in major chip manufacturers like Taiwan Semiconductor Manufacturing Co. (TSMC) and electronics manufacturers like Hon Hai Precision Industry Co., driven by the positive outlook for artificial intelligence (A.I.). This impressive performance made TAIEX the world's best-performing index as of 1H2024, with gains of 28.5%, largely due to the strength of A.I.-related stocks.
- U.S. stocks saw gains in June, with the S&P 500 rising by 3.5% and the Dow Jones increasing by 1.1%. These gains were driven by the latest inflation figures, which indicated that the Fed’s preferred measure, core Personal Consumption Expenditures (PCE) inflation, eased in May, reinforcing market expectations of the Fed lowering interest rates later in 2024.
- In contrast, France’s CAC contracted by 6.4% in June, lagging behind European markets as anxieties mounted ahead of France's parliamentary elections.

DOMESTIC EQUITY: THE FBM KLCI ENDED MARGINALLY LOWER ON PROFIT TAKING

Monthly Bursa Sectoral Performance, m-o-m%



Monthly Foreign Fund Net Inflows/Outflows, RM Million

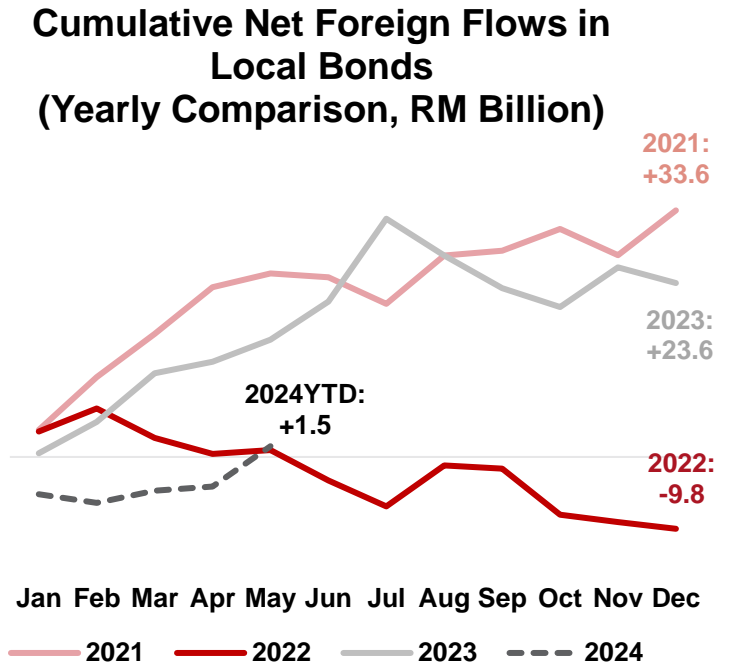
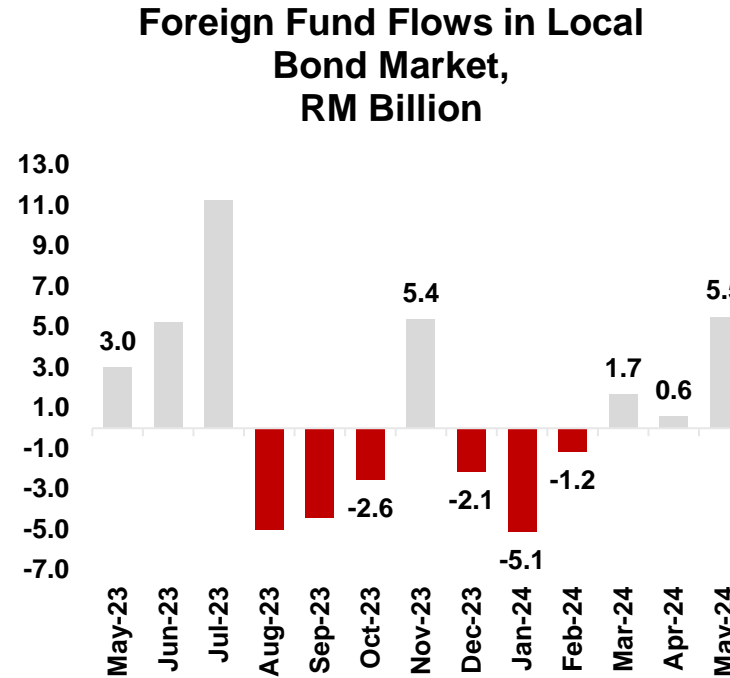


Sources: Bursa, Bank Negara Malaysia (BNM), CEIC data

- The FBM KLCI ended the month of June with a marginal decline of 0.4% as early gains were reversed by late profit-taking as the Fed’s hawkish policy update dampened investors’ appetites for investing in emerging market assets.
- Losses were led by the Consumer (-2.3%) index as investors assessed the impact of subsidy reforms. Plantation stocks also saw some selling pressure (-1.3%) amid expectations that increased stockpiles will weigh on crude palm oil (CPO) prices.
- Meanwhile, the Construction (+8.4%) and Technology (+5.1%) indices led gains, fuelled by growing optimism surrounding data centers. This optimism followed news that companies including Google, Microsoft, and ByteDance, plan to expand their data centers in Malaysia.
- Foreign investors turned net sellers in June, with net sales amounting to RM61.4 million worth of equities, reversing from a net buying position of RM1.5 billion in May.
- Trading in local stocks will remain influenced by Fed rate cut expectations as the Fed is scheduled to meet again in July. Investors also await details on the RON95 subsidy reforms, expected to be announced in July or no later than the Budget 2025 announcement in October.

FIXED INCOME: YIELDS CONTINUED TO BE ON THE DOWNTREND AS PCE INFLATION EDGED LOWER

| Monthly changes, basis points (bps) | | | |
|-------------------------------------|-------------------------|-------------------------|-----------------|
| UST | Yields (%) 31-May-24 | Yields (%) 28-Jun-24 | Change (bps) |
| 3-Y UST | 4.69 | 4.52 | -17 |
| 5-Y UST | 4.52 | 4.33 | -19 |
| 7-Y UST | 4.52 | 4.33 | -19 |
| 10-Y UST | 4.51 | 4.36 | -15 |
| MGS | Yields (%) 31-May-24 | Yields (%) 28-Jun-24 | Change (bps) |
| 3-Y MGS | 3.58 | 3.53 | -5 |
| 5-Y MGS | 3.70 | 3.65 | -5 |
| 7-Y MGS | 3.84 | 3.80 | -5 |
| 10-Y MGS | 3.90 | 3.86 | -3 |
| GII | Yields (%) 31-May-24 | Yields (%) 28-Jun-24 | Change (bps) |
| 3-Y GII | 3.53 | 3.47 | -6 |
| 5-Y GII | 3.67 | 3.63 | -4 |
| 7-Y GII | 3.83 | 3.79 | -4 |
| 10-Y GII | 3.90 | 3.87 | -3 |

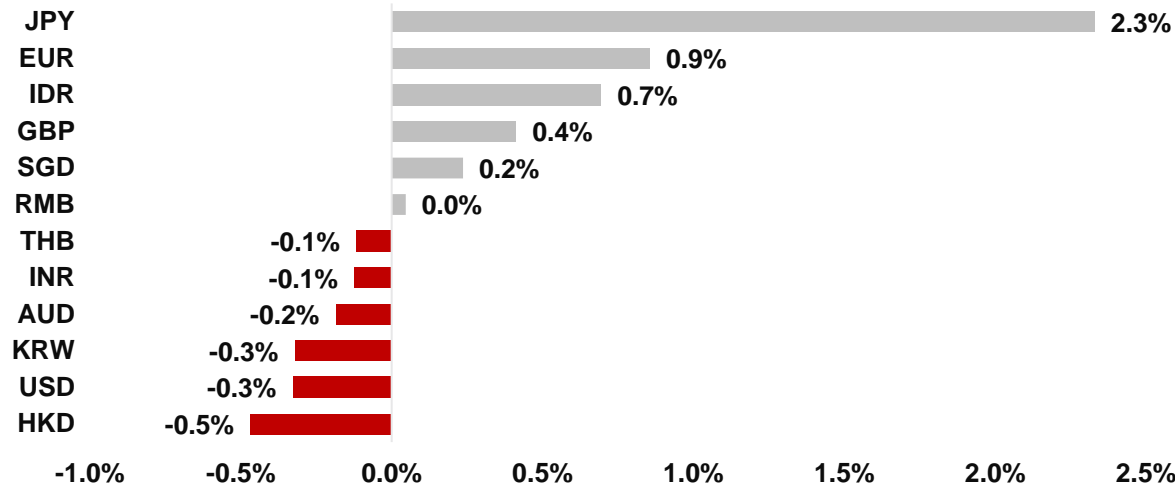


Sources: BNM, Federal Reserve Board

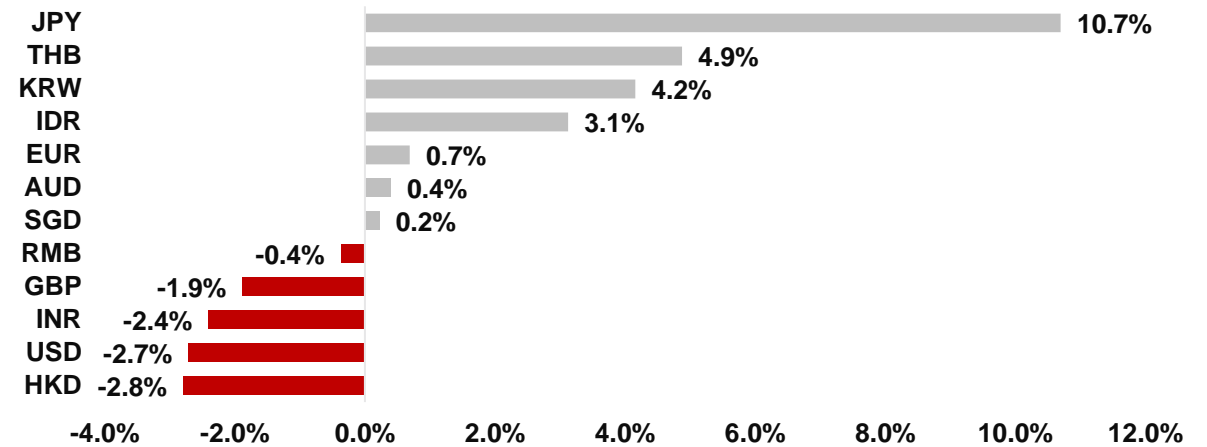
- The U.S. Treasury (UST) yields dipped in the range of 15bps and 19bps, fuelled by signs of inflation moderating, thereby prompting some market expectations of Fed rate cuts this year.
- Domestically, Malaysian Government Securities (MGS) and Government Investment Issues (GII) yields edged down between 3bps and 6bps.
- As of 1H2024, on average, investors recorded a robust bid-to-cover (BTC) ratio of 2.2x for MGS (1H2023: 2.0x). Similarly, GII also saw healthy demand with a BTC ratio of 3.0x (1H2023: 2.2x). Overall, the Malaysian government issued RM45.0 billion worth of MGS and RM49.5 billion of GII, totaling to RM94.5 billion in 1H2024 (1H2023: RM95.5 billion).
- Foreign fund flows in the local bond market remained in the positive territory with a larger net foreign inflow of RM5.5 billion in May (April: +RM0.6 billion). Consequently, local govies' foreign shareholdings to total outstanding climbed to 21.6% in May (April: 21.2%).
- For the first five months of this year, the local bond market recorded the cumulative net foreign inflows of RM1.5 billion, significantly lower than the inflows of RM15.9 billion in the same period in the previous year.

FX MARKET: RINGGIT UNDER PRESSURE AS THE FED'S POLICY OUTLOOK OUTWEIGHS

MYR Against Regional Currencies, m-o-m%



MYR Against Regional Currencies, YTD% (As of 28 June 2024)



Sources: BNM, Bureau of Economic Analysis (BEA)

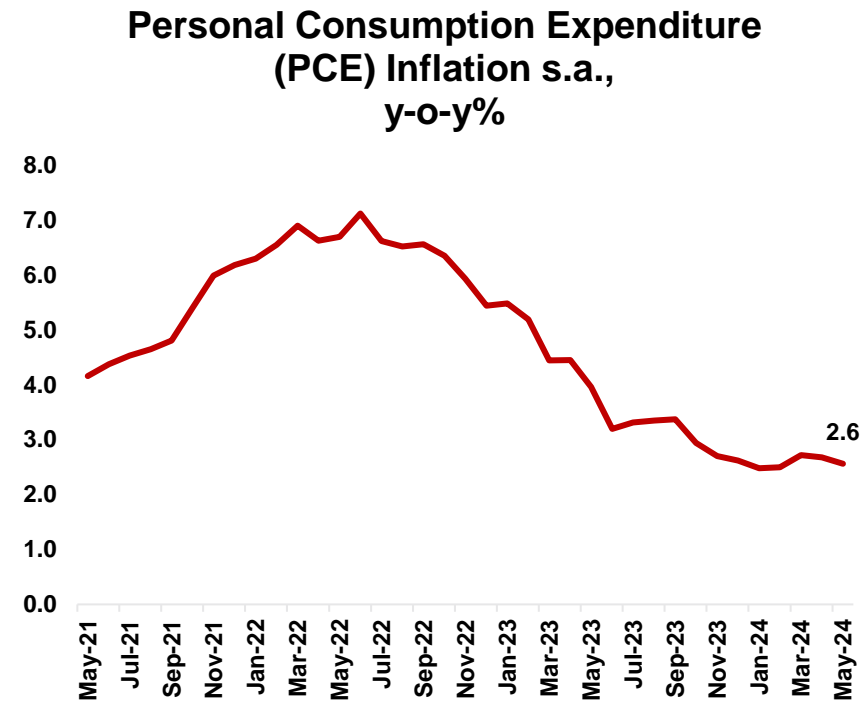
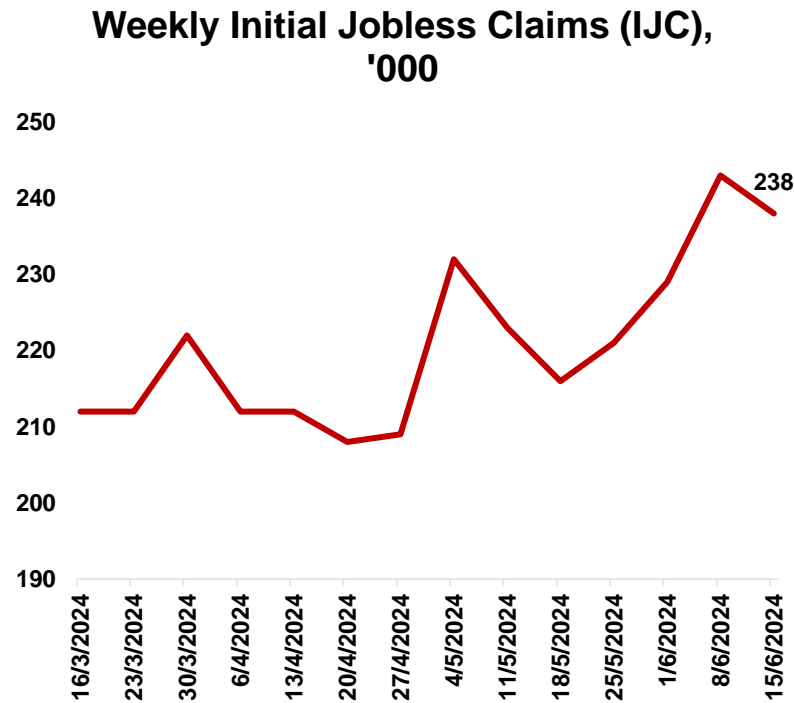
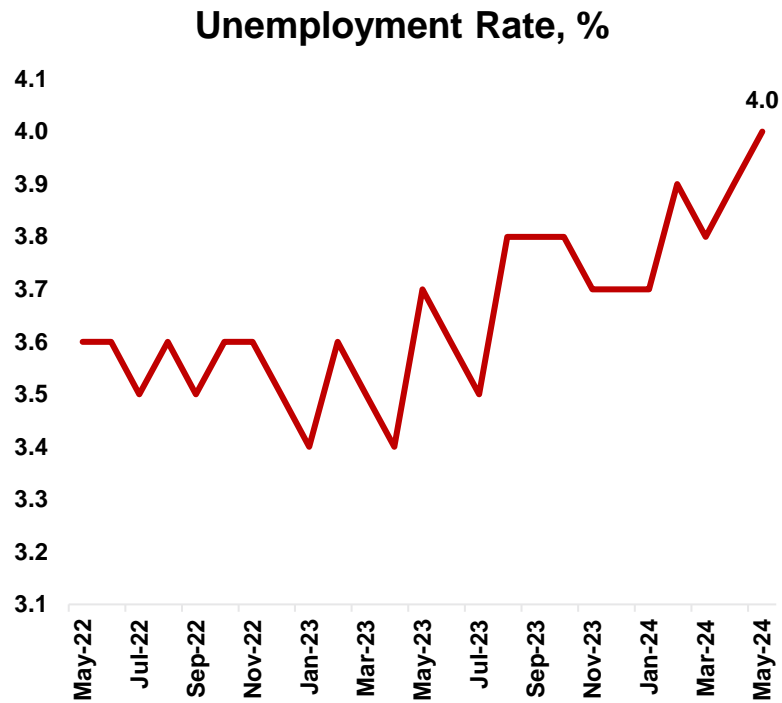
- The Ringgit depreciated against the USD on a monthly basis, closing at RM4.7195 compared to RM4.7040 the previous month. This decline was driven by the strength of the USD index, which briefly hit its highest level since the end of April.
- The strength of the greenback was driven by a slew of robust U.S. economic data, one of which is the final 1Q2024 Gross Domestic Product (GDP) print which expanded by 1.4% q-o-q, revised upwards from the earlier estimate of 1.3%. Stronger readings were also displayed from the manufacturing and services activities as well as retail sales, signalling that the economy is healthy.
- Such figures support the hawkish tone in the Fed's dot plot projections released earlier, where the median forecast now points to only one rate cut this year, down from the earlier estimate of three cuts released in March.
- However, market remained optimistic about at least two cuts before year-end as the tight monetary policy environment has proven effective in cooling inflation thus far (Core PCE inflation; May: 2.6% vs. April: 2.8%).
- Nevertheless, even with anticipated two cuts, the FFR would still hover at the highest range since 2007. In line with this view, the local note will remain pressured against the greenback.

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SECTION 2

The Global Economy

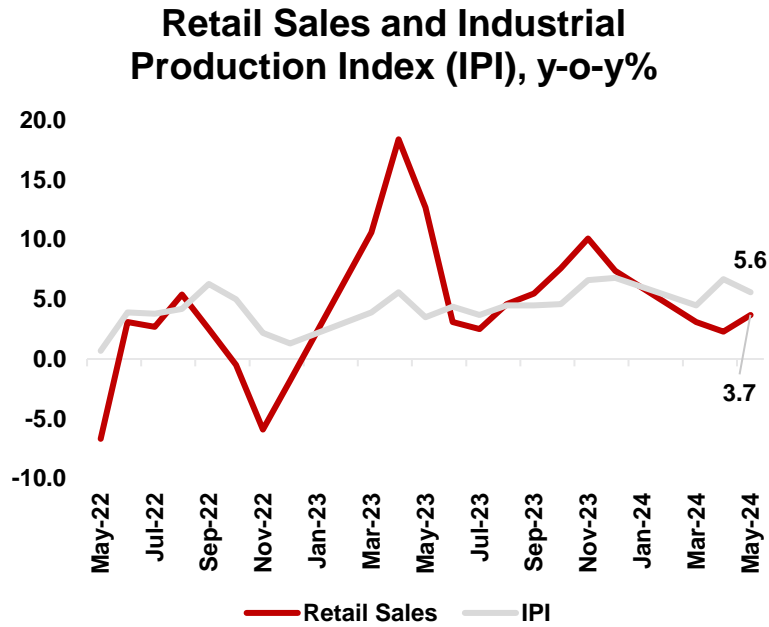
U.S. INFLATION COOLS DOWN, RAISING THE POSSIBILITY OF A FED RATE CUT BANK ISLAM



Sources: Bureau of Economic Analysis, CEIC Data

- The Fed left interest rates unchanged at its June meeting as widely anticipated. This marked the seventh consecutive meeting where rates have been held steady. However, the Fed's latest economic projections indicate a more cautious approach, with only one rate cut expected this year compared to their March forecast of three. For 2025, they now anticipate four reductions, down from the three previously projected.
- While U.S. initial unemployment claims fell slightly to 238,000 in the second week of June, this remained above expectations of 235,000, the second-highest reading since August 2023, trailing only the revised count of 243,000 claims from the previous week. On the other hand, the U.S. jobless rate edged higher to 4.0% in May (April: 3.9%).
- The PCE inflation eased to 2.6% in May (April: 2.7%), reinforcing market expectations that the Fed may cut interest rates at least once this year.

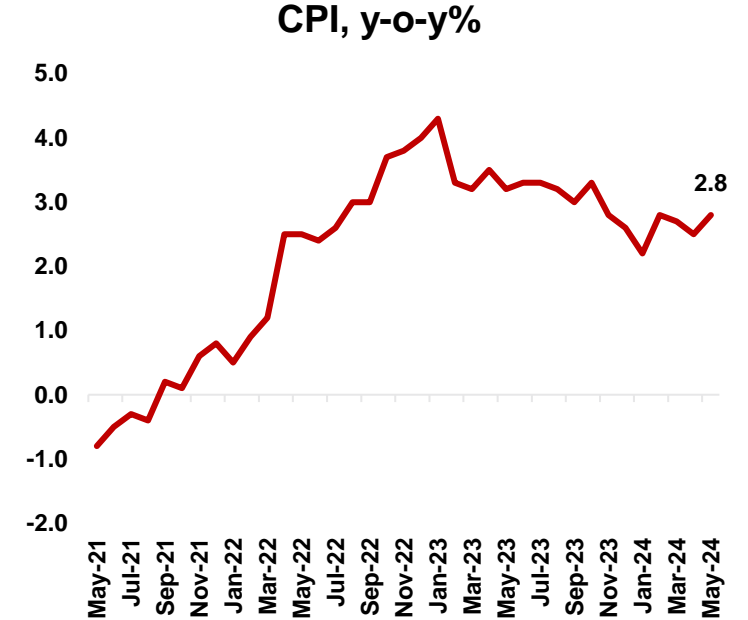
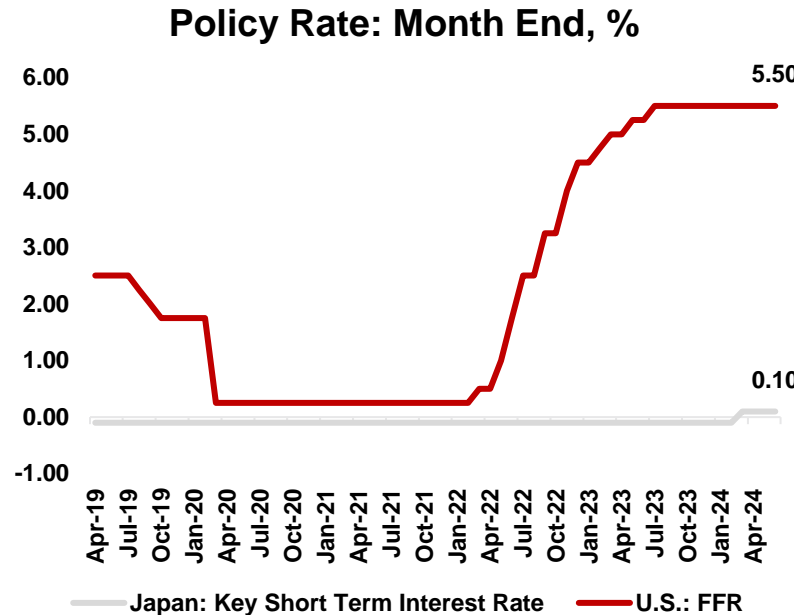
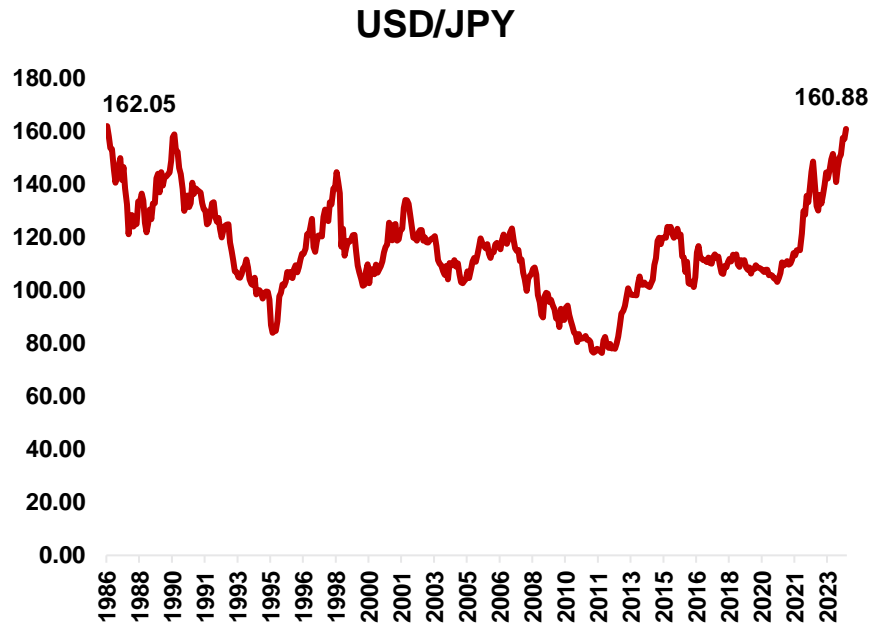
CHINA'S EXPORTS GAINED MOMENTUM BUT PROPERTY SECTOR REMAINED LACKLUSTER



Sources: National Bureau of Statistics, CEIC Data

- May retail sales jumped 3.7% (April: 2.3%), marking the strongest performance in three months. This surge was likely fuelled by holiday spending during the May Day and Dragon Boat Festival celebrations.
- China's exports continued their upward trend, expanding by 7.6% in May (April: 1.5%), indicating a strong growth. This suggests manufacturers are successfully finding buyers overseas, offering a much-needed boost to the nation's economic recovery efforts.
- While exports gained momentum, imports grew at a sluggish 1.8% pace in May, down from a sharp 8.4% increase in April. This underscores the weakness in domestic demand, posing a challenge to China's economic recovery.
- Data for May also showed a slowdown in China's industrial production and a struggling property market. Factory output rose by a mere 5.6% in May (April: 6.7%), coming less than market expectations of a 6.0% expansion. This added to concerns about the health of the Chinese economy. Meanwhile, China's property investment continued to decline despite government attempts to boost the market. Real estate investment fell 10.1% in May, worsening from a 9.8% drop in April.

THE WEAK YEN HIT 38-YEAR LOW



Sources: Federal Reserve Economic Data (FRED), CEIC Data

- The yen weakened past 160.88 per USD at month-end, a level not seen since December 1986. Despite pressure to defend the yen and warnings from Finance Minister, Suzuki against rapid depreciation, Japanese authorities have not intervened in currency markets since April.
- The yen's weakness persisted despite a boom in both retail sales (May: +3.0% vs. April: +2.4%) and industrial production (May: +0.3% vs. April: -1.8%), as well as rising inflation in Japan, which ticked higher to 2.8% in May (April: +2.5%). This reflects the Bank of Japan's (BoJ) slower pace of monetary tightening compared to other countries.
- The BoJ is hinting at a possible interest rate hike in July. This comes as a weakening yen threatens to raise import costs and hurt consumer spending. Additionally, the BoJ also plans to unveil a strategy in July for scaling back its bond-buying program.
- A downward revision of 1Q2024 GDP to -2.9% from an earlier estimate of -1.8% (4Q2023: +0.4%) indicates a weaker-than-expected economic performance. Businesses in the service sector grew more pessimistic in June due to rising costs, dampening their overall mood which offsets the recent boost in confidence among manufacturers. The combination suggests potential weakness in consumer spending, which is a key driver of the Japanese economy.

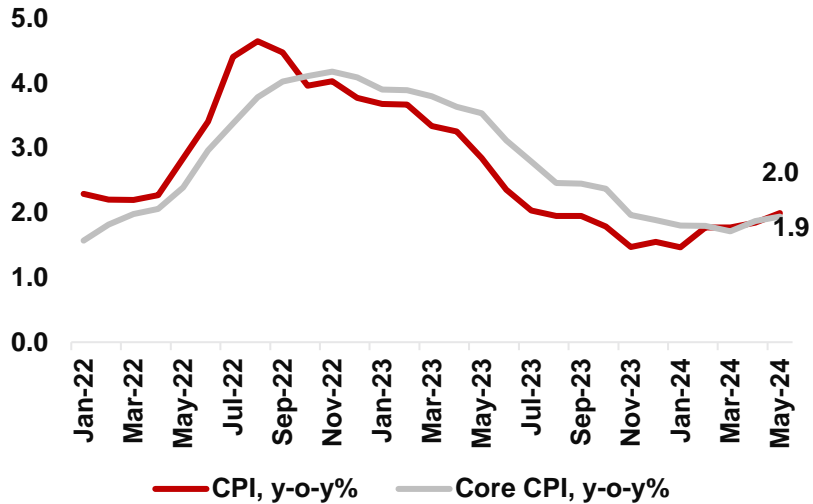
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SECTION 3

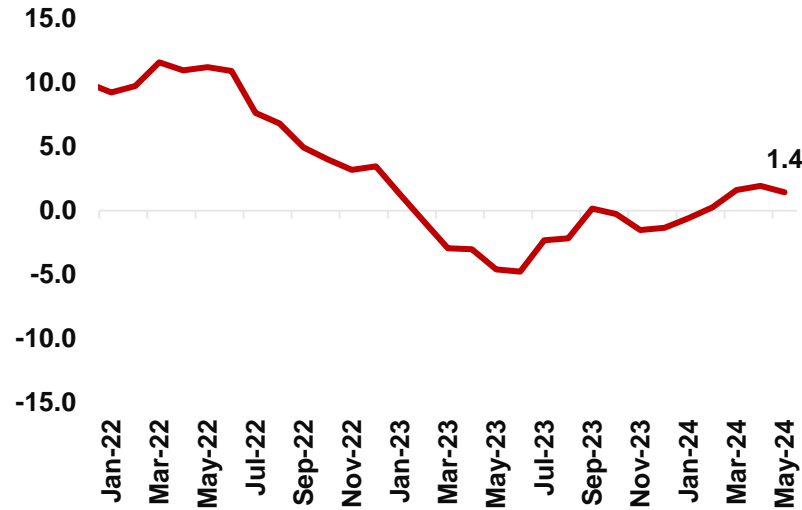
Domestic Landscape & Banking Sector
Update

LOOKING AT THE LANDSCAPE THUS FAR – BEFORE THE IMPACT OF DIESEL SUBSIDY RATIONALISATION KICKS IN

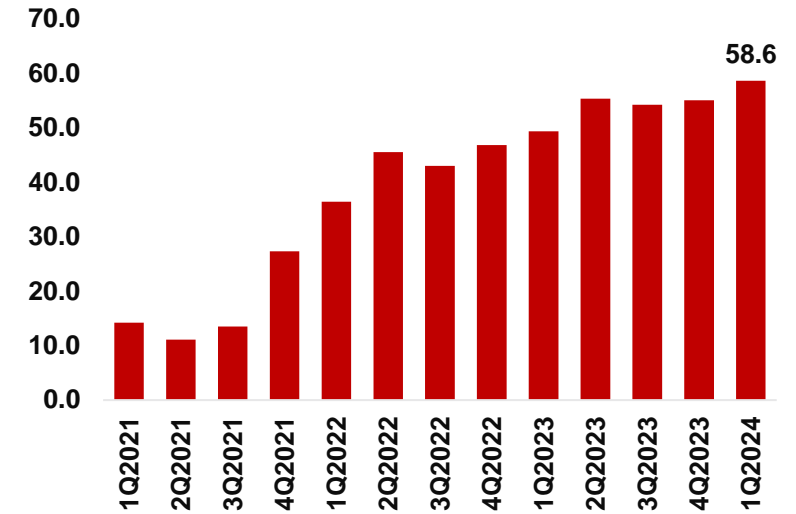
CPI, y-o-y%



Producer Price Index (PPI), y-o-y%

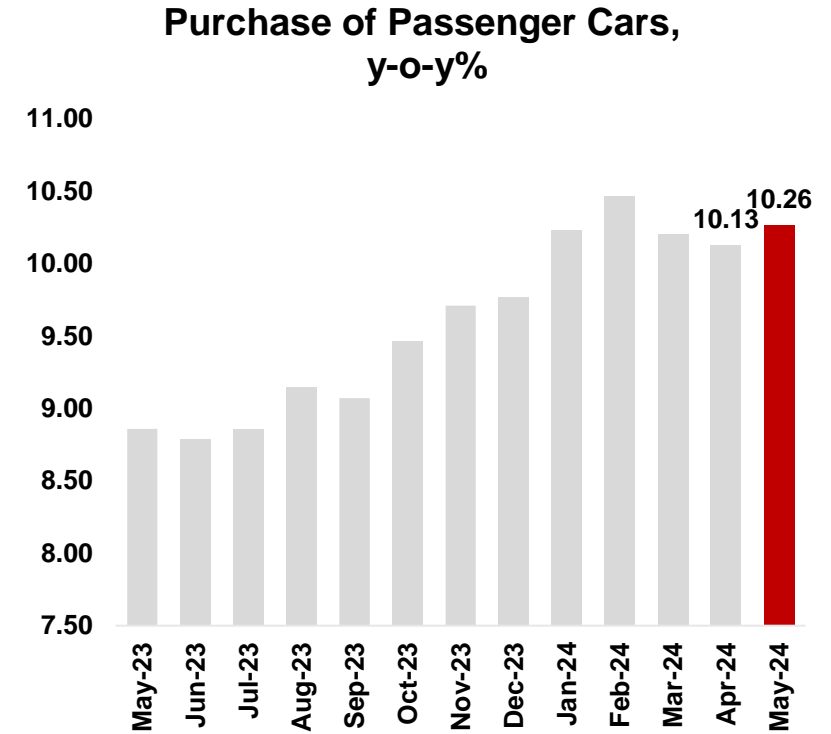
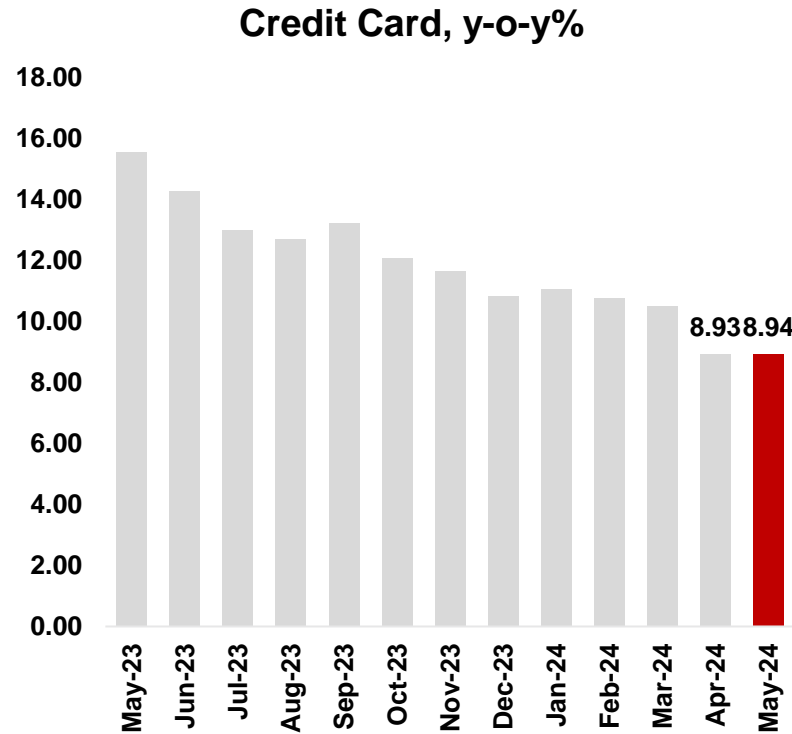
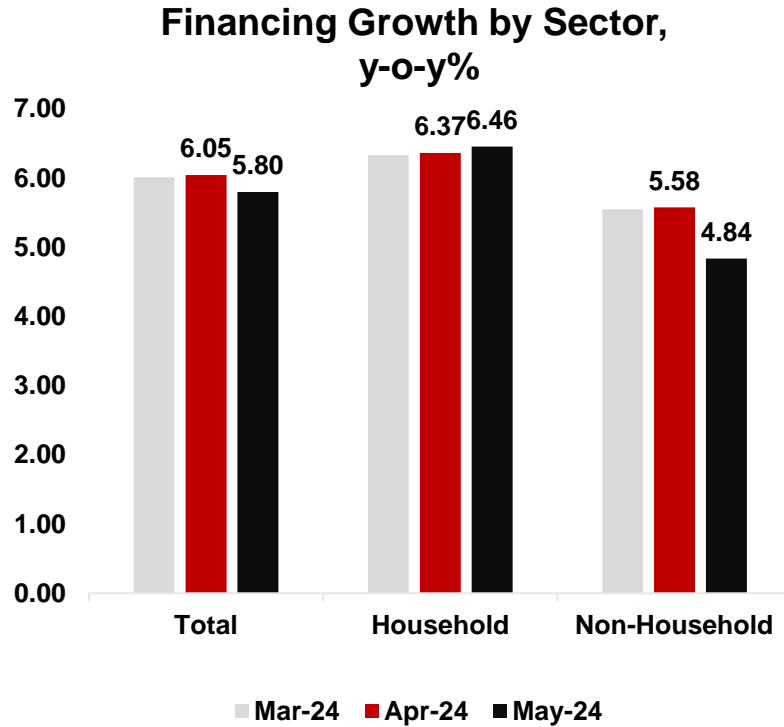


Domestic Visitors, million



Sources: Department of Statistics Malaysia (DOSM), BNM

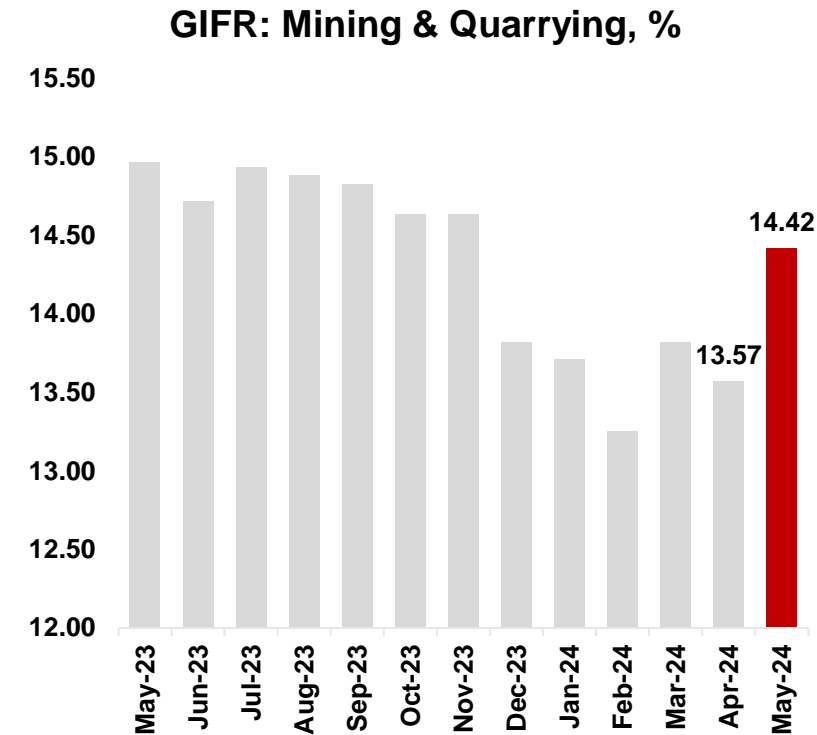
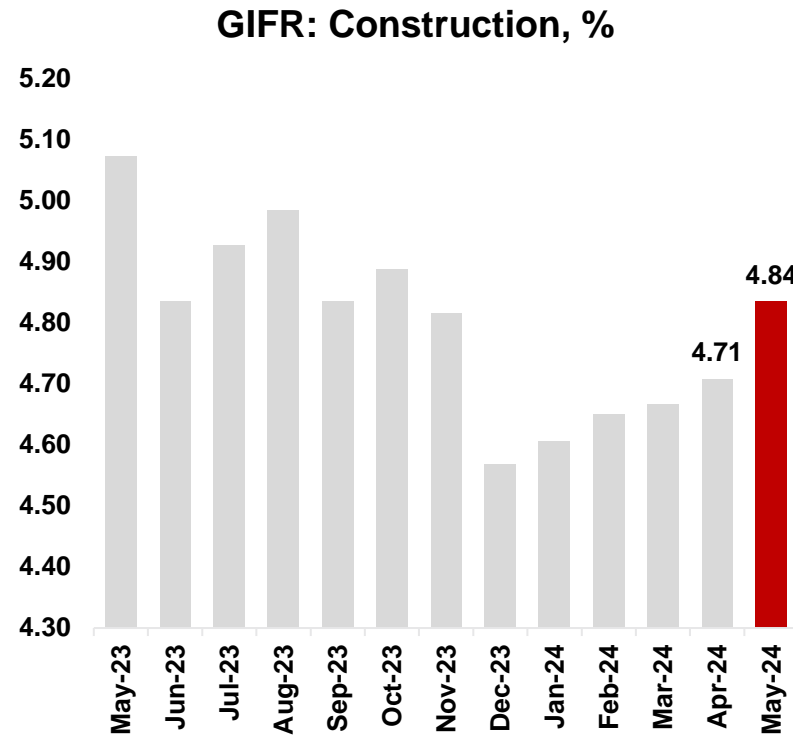
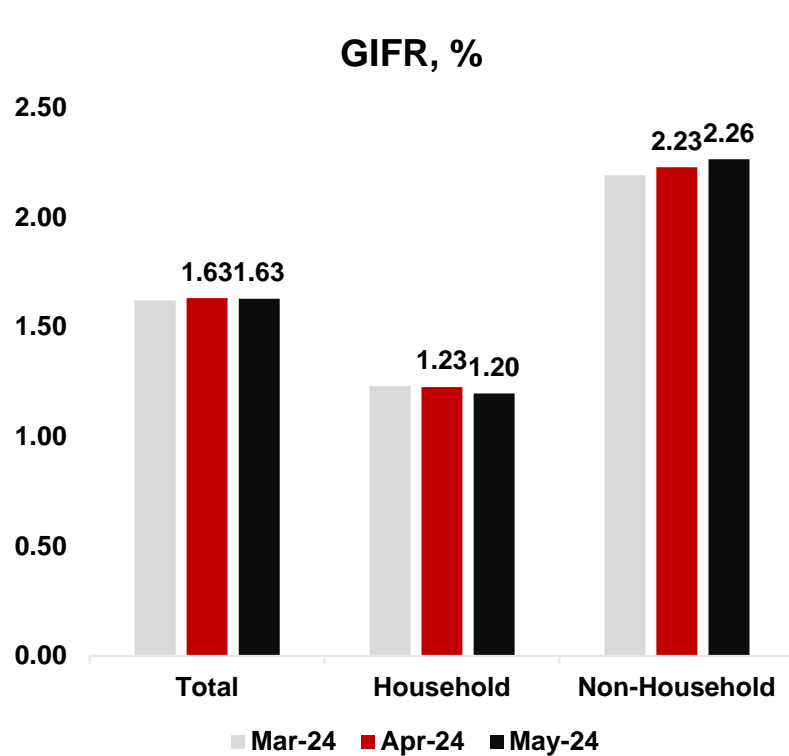
- Malaysia’s headline inflation ticked higher to a ten-month high of 2.0% in May (April: 1.9%), fuelled by the rise in the Housing, Water, Electricity, Gas & Other Fuels (HWEG) (May: 3.2% vs. Apr: 3.0%) as well as Restaurant & Accommodation Services (May: 3.2% vs. April: 3.5%) subcomponents. The HWEG inflation marked the highest level since September 2022, attributable to both higher housing costs as well as the water tariff hike for domestic users in Perak which took effect on May 1 following similar hikes in other states since February 1.
- Currently, our forecast for 2024’s inflation stands at 2.7%, with potential for an upward revision after the government announces the details of RON95 targeted subsidy rationalisation, expected in July or no later than the Budget 2025 announcement in October. In any case, we anticipate that inflation for this year will remain within the BNM’s projected range of 2.0% to 3.5%.
- Meanwhile, the prices of goods at the factory gate eases to 1.4% from 1.9% in April, driven by slower increases in the Mining (May: 6.6% vs. Apr: 10.0%) and Agriculture (May: 1.3% vs. Apr: 5.4%) categories.
- Malaysia’s domestic tourism continued to flourish, expanding by 6.5% to record 58.6 million visitors in 1Q2024 (4Q2023: 55.0 million visitors). This signals continuous healthy demand for recreational activities and entertainment.



Source: BNM

- Financing activities slowed to 5.80% in May, down from 6.05% in April. The non-household segment’s financing growth declined to 4.84% in May (April: 5.58%). Conversely, the household sector's growth rate increased to 6.46% in May from 6.37% in April.
- The financing growth in the passenger car purchase segment edged up to 10.26% in May (April: 10.13%). Similarly, financing growth in the credit card segment grew slightly to 8.94% in May from 8.93% in April. Meanwhile, financing activities related to the purchase of residential property rose to 7.57% in May (April: 7.53%).

BANKING SECTOR: MAY'S ASSET QUALITY STAYED ROBUST



Source: BNM

- Total gross impaired financing ratio (GIFR) in the banking sector remained steady at 1.63% in May (April: 1.63%). The GIFR in the household segment moderated to 1.20% in May (April: 1.23%). Additionally, the impairment within the non-household sector grew moderately to 2.26% in May (April: 2.23%).
- The impairment within the construction segment surged to 4.84% in May from 4.71% in April. Similarly, the asset quality in the Mining and Quarrying industry escalated to 14.42% in May (April: 13.57%).

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THANK YOU