MONTHLY ECONOMIC UPDATE

4 JUNE 2024

ECONOMIC RESEARCH

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KEY TAKEAWAYS

- **Stickier-than-expected inflation dents hopes for a summer rate cut in the U.K..** The Bank of England (BoE), at its May meeting, opted to keep its key policy rate unchanged at a 16-year high of 5.25% for the sixth time in a row and dropped hints that it could start cutting interest rates as early as June, depending on the upcoming inflation and labour market data. Nonetheless, rate cut expectations were pared back sharply after the latest data showed U.K. inflation eased less-than-expected, with markets pricing in only about a 15.0% chance of a June cut at the time of writing. Of note, services inflation, a measure closely monitored by the BoE, was barely down to 5.9% in April from March's 6.0%, indicating that underlying inflationary pressures remain elevated.

- **RBA signals restrictive stance to stay for longer.** The Reserve Bank of Australia (RBA), during its May meeting, held its policy rate steady at a 12-year high of 4.35%, where it has been since November 2021. While the RBA stopped signalling further hikes and judged that the current monetary policy settings were already sufficiently restrictive to return inflation to the 2.0%-3.0% target, the central bank cautioned that signs of persistent inflation may delay its first rate cut to 2025. Latest data showed Australia's inflation came in above consensus in April, rising at a slightly accelerated pace at 3.6% compared with 3.5% in March.

- **Data points to resilient Malaysia's economy.** Malaysia's GDP growth accelerated to 4.2% in 1Q2024 (4Q2023: 2.9%), exceeding the advanced estimate of 3.9% and our expectations of 4.0%. Growth was primarily driven by robust domestic demand, evidenced by stronger private consumption growth of 4.7% (4Q2023: 4.2%) amid festive spending, government cash transfers and higher tourist arrivals. Investment activities also expanded at an accelerated pace of 9.6% (4Q2023: 6.4%), with both public and private sectors registering faster growth at 11.5% and 9.2%, respectively, supported by the progress of development projects. Meanwhile, exports rebounded to 5.2% (4Q2023: -7.9%) after four consecutive quarters of contraction, suggesting that the drag from net trade on overall growth is fading alongside the global trade turnaround. Fresh data showed Malaysia's goods exports grew at the fastest pace in 13 months at 9.1% in April, rebounding from March's 0.9% contraction. As a result, the merchandise trade balance deficit came in smaller at –RM7.7 billion as compared with –RM12.7 billion in the previous month. We maintain our GDP growth forecast for this year at 4.7%.

SECTION 1

Malaysia’s Financial Market

REGIONAL EQUITY: U.S. SHARES JUMPED IN MAY AS LATEST ECONOMIC DATA SUGGEST ROOM FOR INTEREST RATE CUTS

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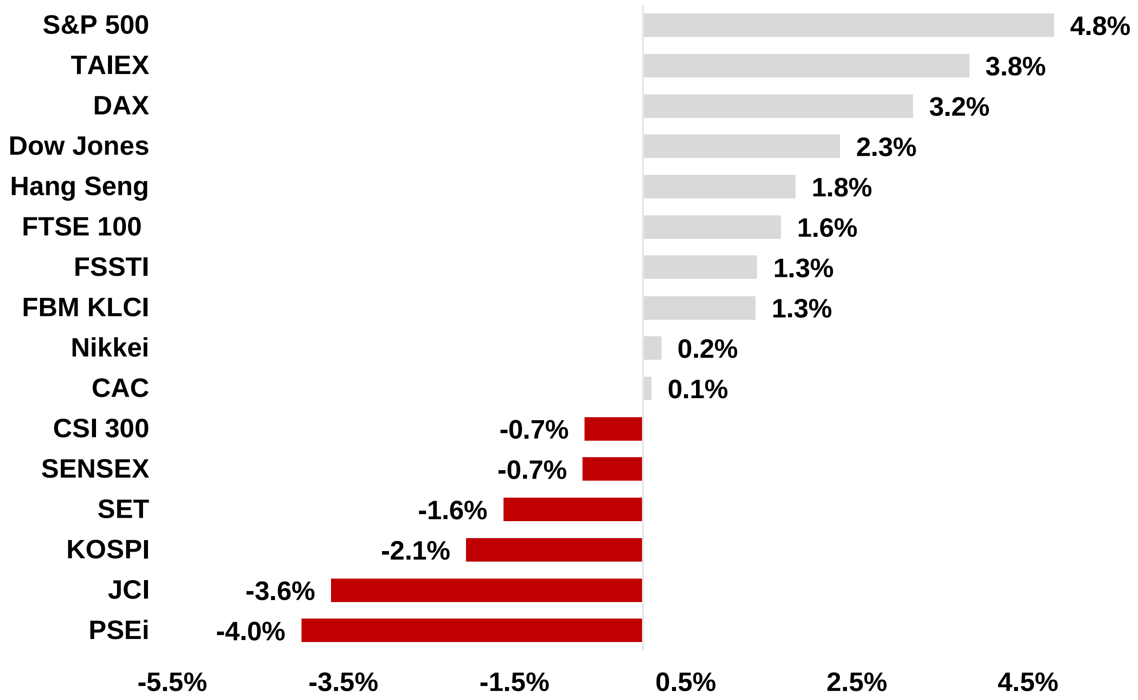
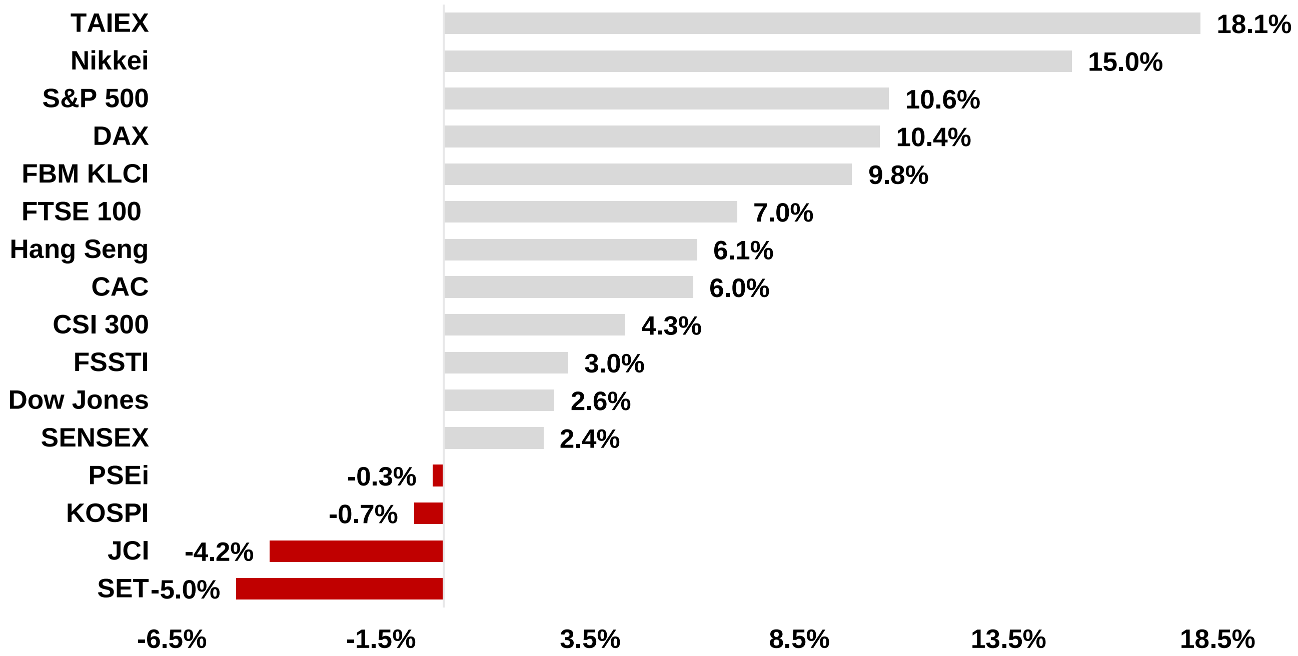
Monthly Gain/Loss of Major Equity Market, m-o-m%



YTD Gain/Loss of Major Equity Markets, % (As of 31 May 2024)

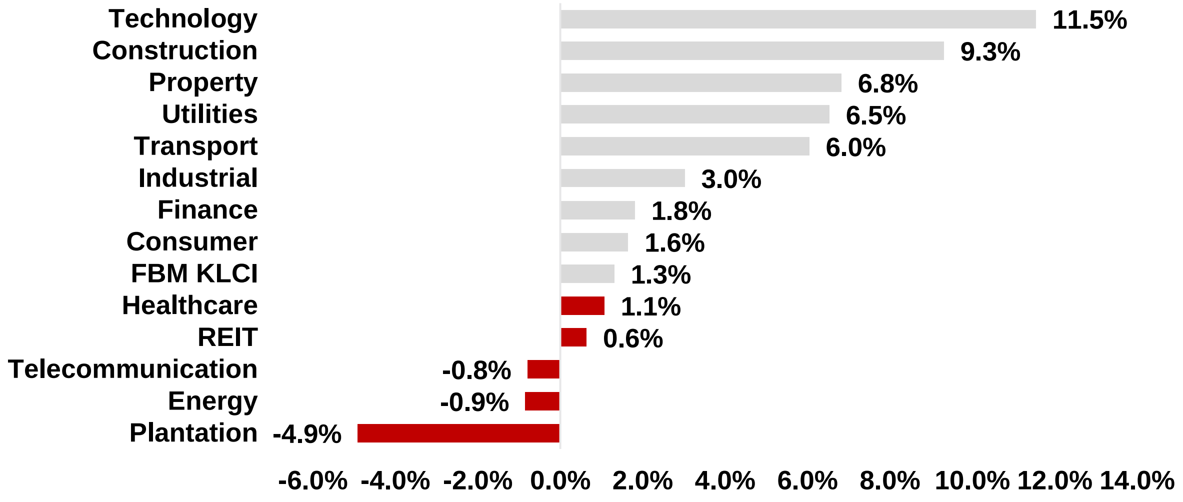


Sources: Bursa, CEIC data

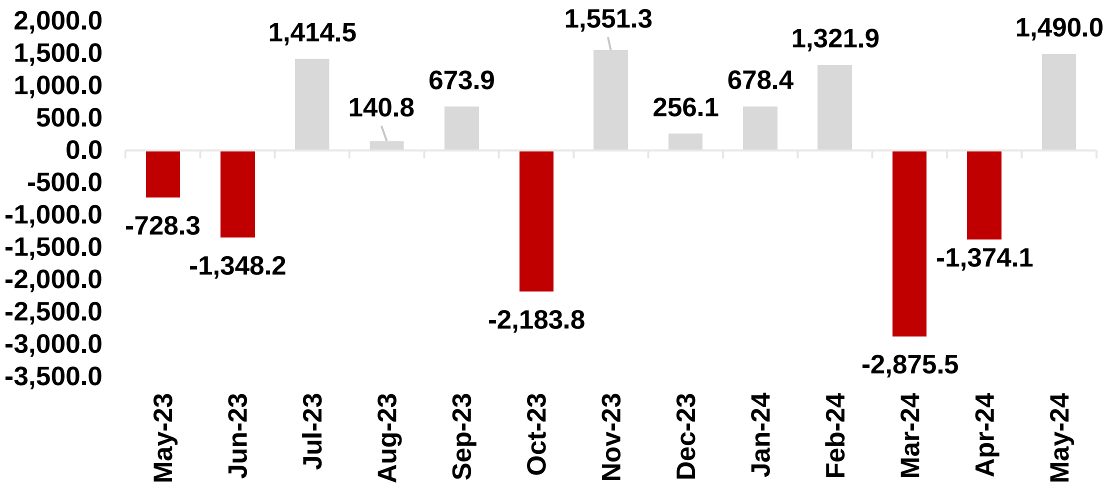
- U.S. stocks – S&P 500 (+4.8%) and Dow Jones (+2.3%) climbed as sentiment buoyed by the recent Personal Consumption Expenditure (PCE) inflation figures that met expectations, which suggest the Federal Reserve (Fed) might have room to cut interest rates later in 2024.
- Taiwan's TAIEX soared by 3.8% in May as Taiwan's GDP growth forecast for 2024 has been revised upwards to 3.94%, from the 3.43% predicted in February, fuelled by booming foreign demand for artificial intelligence (A.I.) applications and healthy domestic consumption.
- In addition, Germany's DAX jumped by 3.2% in May as investors weighed the future course of monetary policy in the Eurozone based on the latest economic data. While a rate cut at the upcoming European Central Bank (ECB) meeting remains likely, high and persistent inflation indicates a slow and cautious approach to future rate cuts.
- For the five months of the year, Taiwan's TAIEX topped the league with gains of 18.1%, surpassing Japan's Nikkei (+15.0%), for the first time this year.

DOMESTIC EQUITY: THE FBM KLCI ENDED FIRMER ON THE RETURN OF FOREIGN BUYING

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 May with a gain of 1.3% following two straight months of decline amid increased foreign buying interest, partly spurred by rising hopes of Fed rate cuts.
- The Technology index leading gains (+11.5%) on positive news flows such as the Microsoft's commitment to invest in Malaysia and the improved electrical and electronics (E&E) products exports. This is followed by Construction (+9.3%) and Property (+6.8%) indices amid investors' optimism about the prospects on both sectors with several development projects in the pipeline.
- Meanwhile, losses were led by the Plantation (-4.9%) and Energy indices (-0.9%) amid expectations that increased stockpiles will exert downward pressure on commodity prices.
- Foreign investors turned net buyers for the first time after two consecutive months of net selling. They had net bought RM1.5 billion worth of equities from a selling position of RM1.4 billion in April.
- Trading in local stocks will remain influenced by Fed rate cut expectations as the Fed will have its scheduled policy meeting in June.

FIXED INCOME: YIELDS PLUNGED IN MAY AS INVESTORS EXPECT FED TO LOWER INTEREST RATES THIS YEAR

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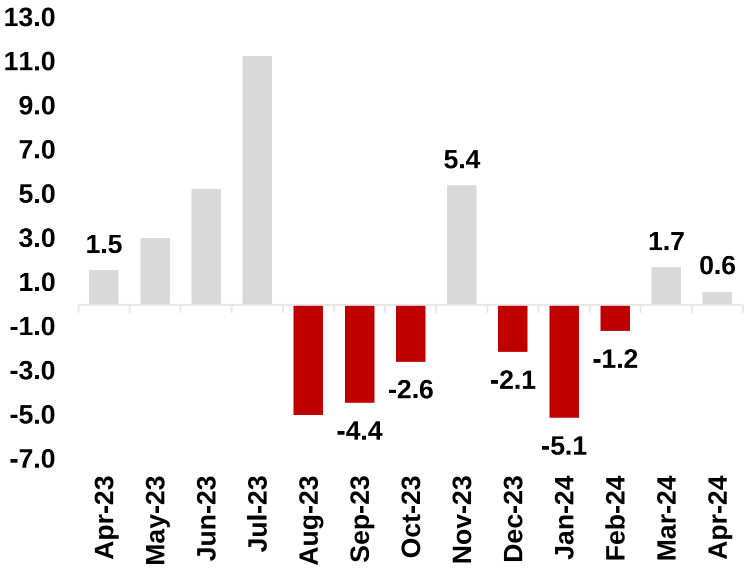
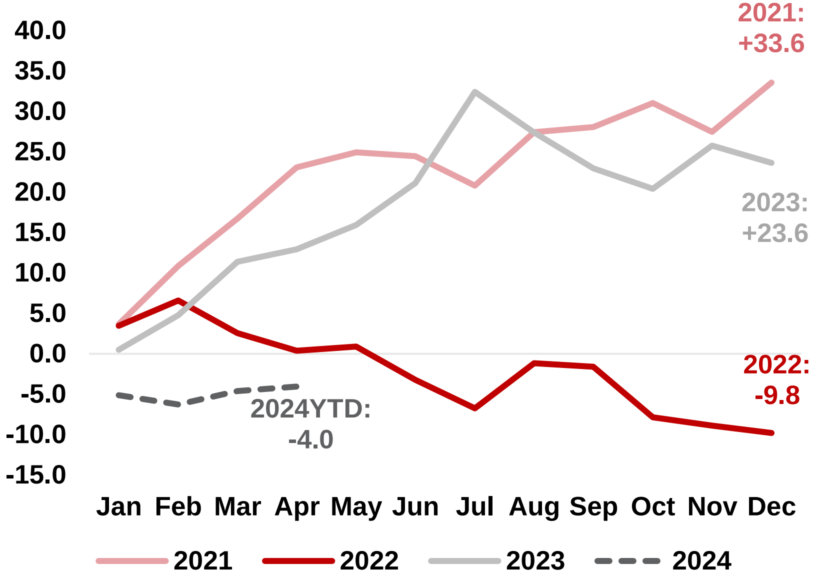
Monthly changes, basis points (bps)

UST	Yields (%) 30-Apr-24	Yields (%) 31-May-24	Change (bps)
3-Y UST	4.87	4.69	-18
5-Y UST	4.72	4.52	-20
7-Y UST	4.71	4.52	-19
10-Y UST	4.69	4.51	-18
MGS	**Yields (%) 30-Apr-24**	**Yields (%) 31-May-24**	**Change (bps)**
3-Y MGS	3.61	3.58	-4
5-Y MGS	3.79	3.70	-9
7-Y MGS	3.90	3.84	-6
10-Y MGS	3.98	3.90	-9
GII	**Yields (%) 30-Apr-24**	**Yields (%) 31-May-24**	**Change (bps)**
3-Y GII	3.60	3.53	-7
5-Y GII	3.79	3.67	-12
7-Y GII	3.89	3.83	-7
10-Y GII	3.99	3.90	-9

Foreign Fund Flows in Local Bond Market, RM Billion



Cumulative Net Foreign Flows in Local Bonds (Yearly Comparison, RM Billion)



Sources: BNM, Federal Reserve Board

- The U.S. Treasury (UST) yields slumped in the range of 18bps and 20bps amid a downward revision in U.S. GDP growth figure and that investors interpreted this as a sign that the Fed is more likely to cut interest rates at least once before the year's end.
- On the domestic front, Malaysian Government Securities (MGS) and Government Investment Issues (GII) yields inched lower between 4bps and 12bps, tracking the downward movements in UST yields.
- Foreign fund flows in the local bond market remained in the positive territory albeit at a smaller magnitude with a net foreign inflow of RM0.6 billion in April (March: +RM1.7 billion). Nevertheless, local govvies' foreign shareholdings to total outstanding decreased slightly to 21.2% in April (March: 21.4%).
- For the first four months of this year, the local bond market recorded the cumulative net foreign outflows of RM4.0 billion, significantly lower than the inflows of RM12.9 billion in the same period in the previous year.

FX MARKET: RINGGIT WINS ON MALAYSIA'S ROSY ECONOMIC OUTLOOK

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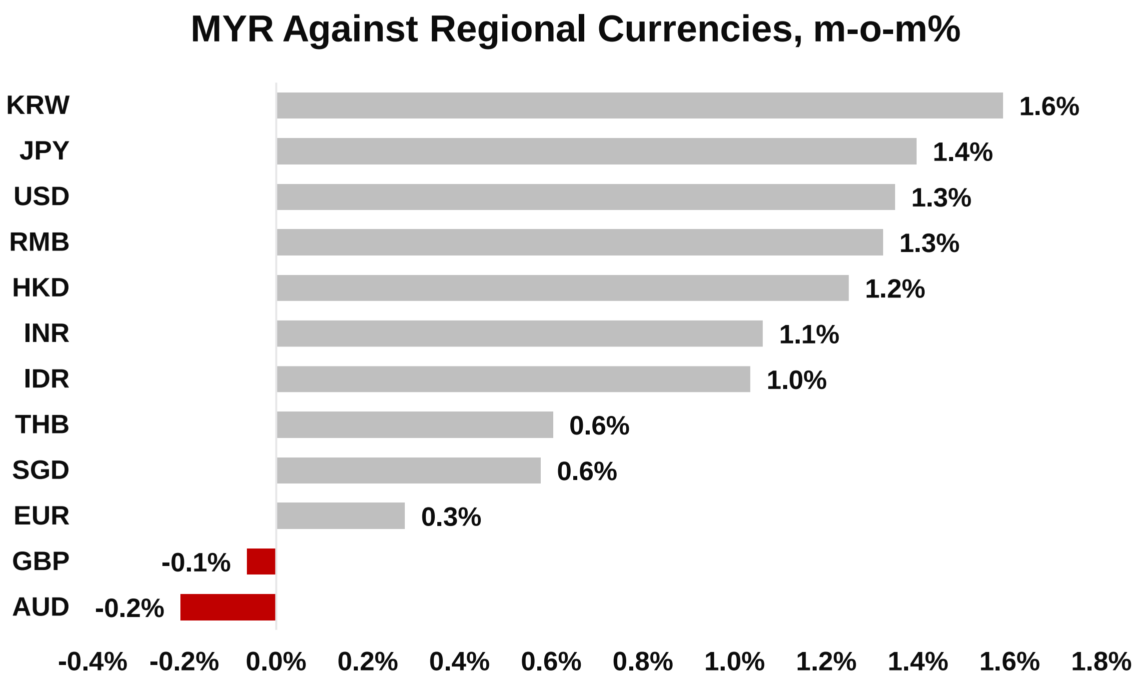

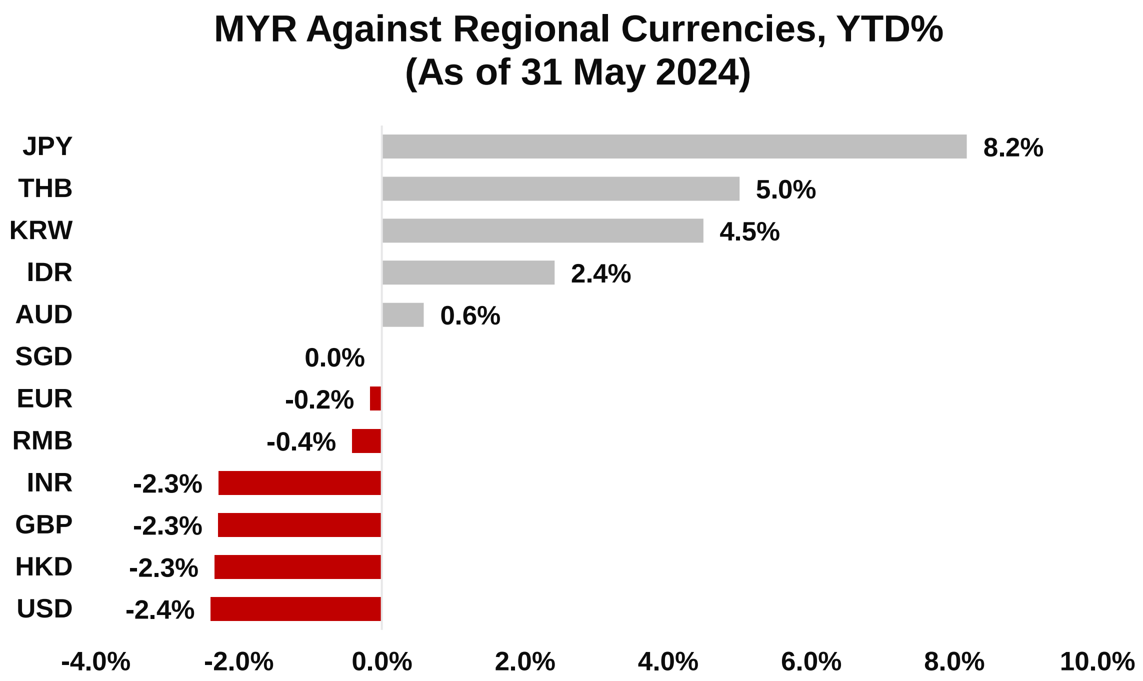

Source: BNM

- Ringgit appreciated against the USD to close at RM4.7040 in May (April:RM4.7675) as both domestic and U.S. economic performance had come into play in tipping the scale in favour of the local note.
- Domestically, Malaysia's economy had taken the market by surprise to beat official advanced estimate, expanding at 4.2% in 1Q2024 (4Q2023: 2.9%), spearheaded by resilient private consumption as well as strong investment activities. Furthermore, exports rebounded by 5.2% in the same quarter (4Q2023: -7.9%) after its sticky stint in the contractionary zone previously.
- On the other hand, U.S. job market had shown signs of cooling while retail sales had stagnated on a monthly basis, which in turn had pressured the greenback to hover around the 104-level for most of the month. Meanwhile, the steady core PCE had reignited hopes of a Fed rate cut in September.
- Nevertheless, downsides to the greenback was capped by the hawkish stance adopted by the Fed in their May Federal Open Market Committee (FOMC) minutes, pointing to a possibility of tighter rates should the risks necessitate it and all but confirms that the current policy environment will be maintained for longer than expected.

FX MARKET: THE DIVERGENCE OF FBM KLCI AND RINGGIT - WHAT CAUSES THE TREND?

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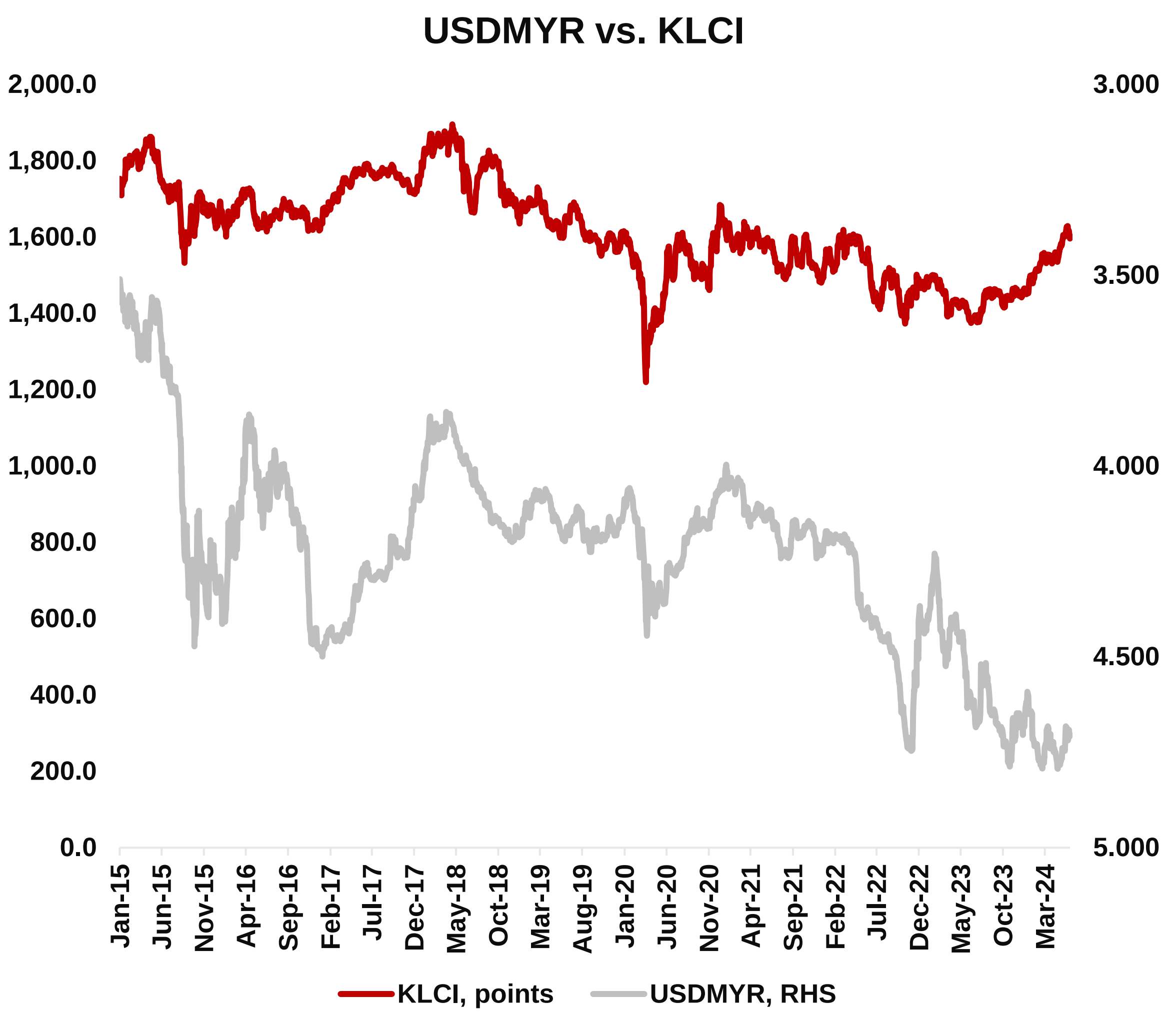

Sources: BNM, Bursa

- Historical trend shows that Ringgit and the KLCI had been strongly positively correlated. During a period of healthy economic developments, capital flows into Malaysia had provided support to Ringgit whilst increased buying interest lifted the KLCI.
- However, there was a divergence in the correlation recently when KLCI has been on a winning streak, breaching the highest level in three years in May 2024, whereas Ringgit is still under pressure, notably touching the RM4.80-threshold in February.
- The YTD depreciation the local note does not reflect the healthy trend of the local market and vice versa. Therefore, this begs the question of what causes the divide?
- Markets were optimistic of Malaysia's growth in 2024, leading to both increased local and foreign buying in the local market. Such performance had then been boosted by the better-than-expected 1Q2024 GDP figures alongside rebound in exports and the manufacturing sector.
- While the strong economic fundamentals had buoyed KLCI's performance thus far, the local note was instead pressured by widened gap between the Overnight Policy Rate (OPR) and the U.S.' Fed Funds Rate (FFR). As the Fed remains hawkish due to stickier than expected inflation, Ringgit will be weighed by the prolonged high FFR environment.
- Nevertheless, we noted signs of improvement in Ringgit's trend following BNM's effort to lift the local note as well as the pick-up in Malaysia's economic performance. Hence, we maintain that the local note will close the year at RM4.45.

SECTION 2

The Global Economy

U.S. ECONOMY'S GROWTH MOMENTUM SLOWED DOWN AS CONSUMER SPENDING WEAKENED

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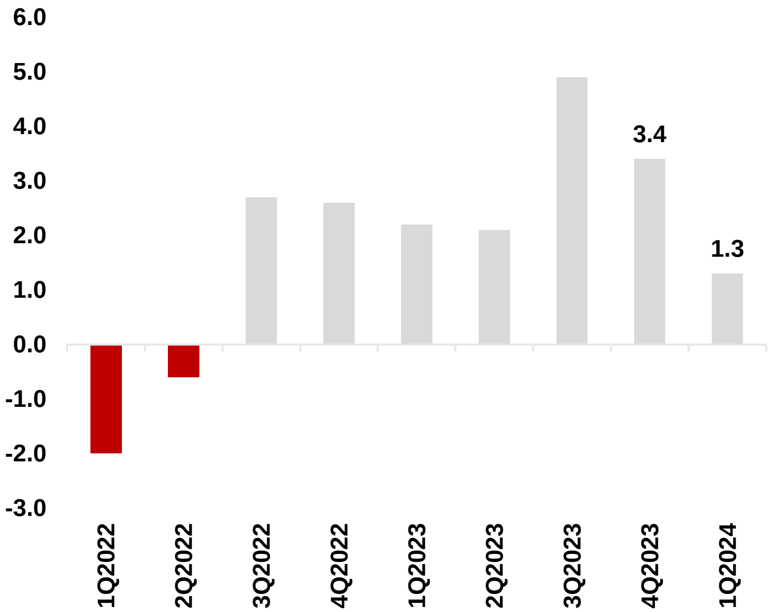

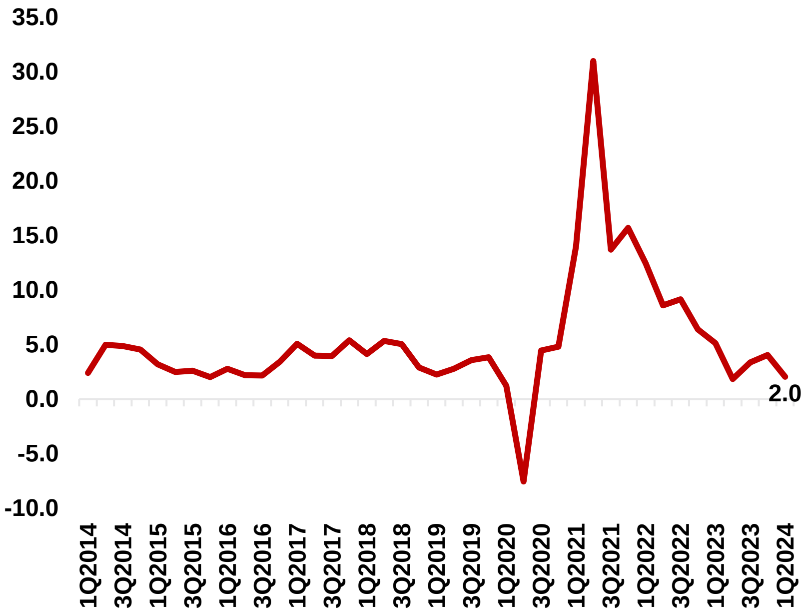

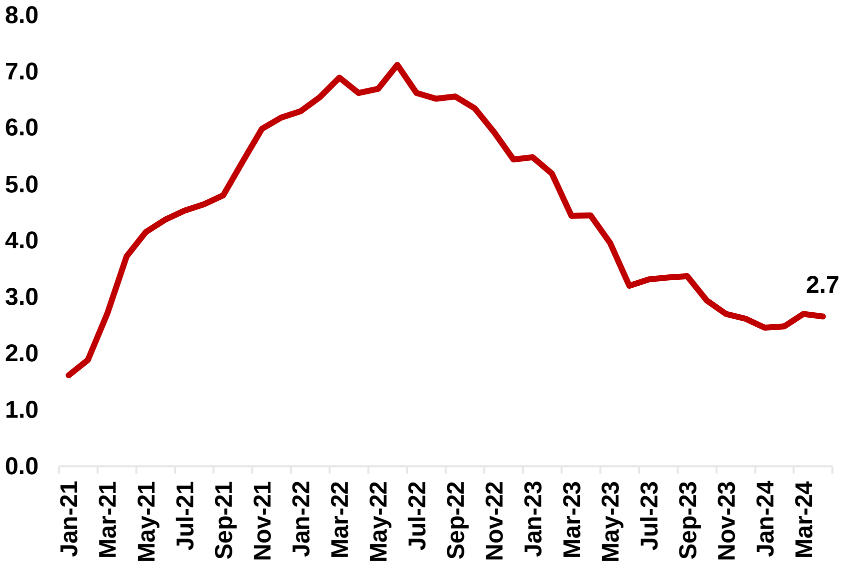

Sources: Bureau of Economic Analysis, CEIC Data

- The U.S. economy's growth in 1Q2024 was revised downward to 1.3% (4Q2023: 3.4%), lower than the initial estimate of 1.6%, reflecting a slowdown in consumer spending on goods.
- The downward revision of economic growth aligns with earlier signs of a slowdown, as data on retail sales also showed weakness, growing at a slower pace of 2.0% in 1Q2024 (4Q2023: 4.0%).
- A small rise in unemployment claims of 219k for the week ending May 25 which was above initial estimates of 218k and higher than the previous weekly gain of 216k. In April, the U.S. jobs data portrayed signs of cooling with a lower non-farm payroll figures (April: 175k vs. March: 315k) and an uptick in unemployment levels (April: 3.9% vs. March: 3.8%).
- Additionally, the Fed's preferred inflation gauge, the PCE inflation, expanded by 2.7% in April (March: 2.7%), in line with expectations, rekindled interest-cut hopes by the Fed this year.

MIXED PICTURE FOR CHINA'S ECONOMY

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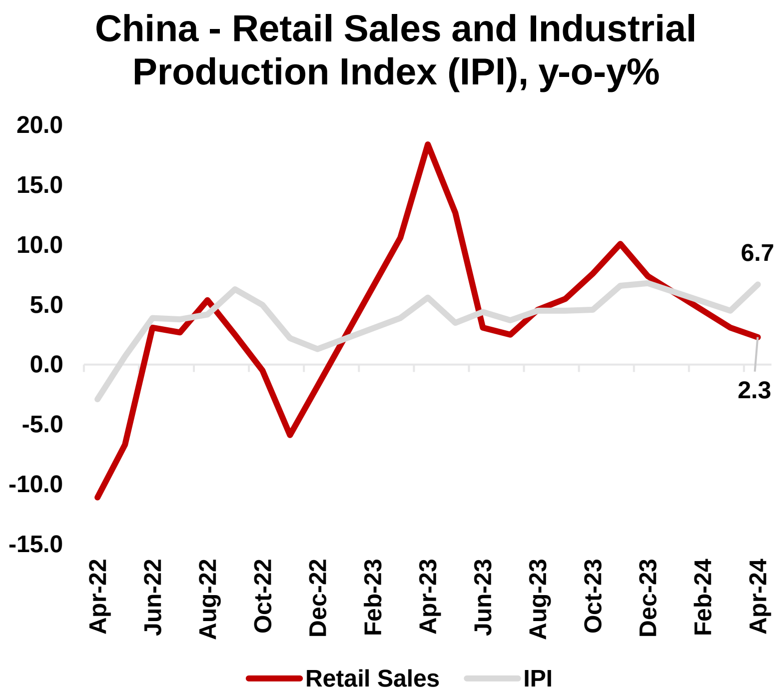

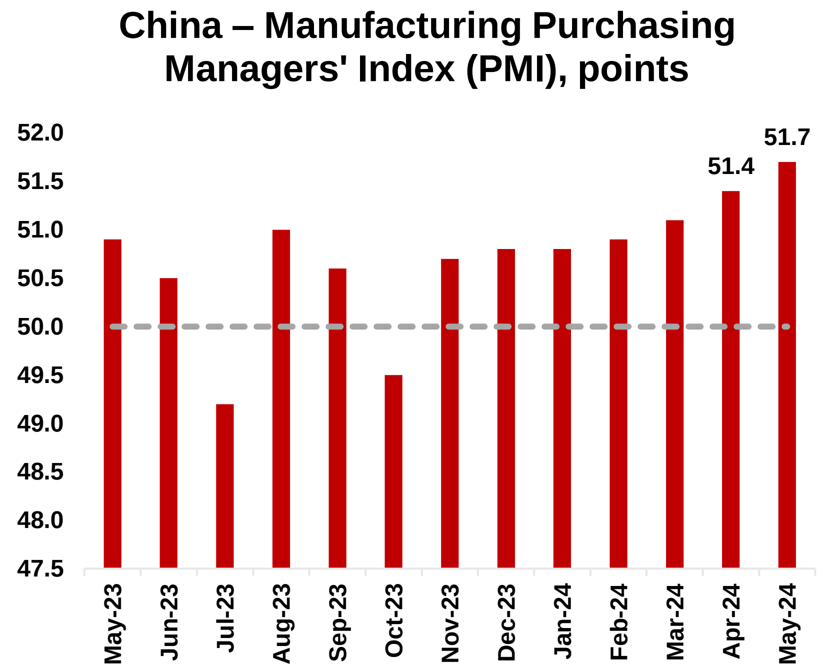

Sources: National Bureau of Statistics, CEIC Data

- Recent data from China shows a slowdown in consumer spending with retail sales grew at a slower pace of 2.3% in April relative to 3.1% in the previous month. Meanwhile, industrial activity maintains its strength, with the IPI expanded by 6.7% in April, a pickup from 4.5% in March.
- On the external front, China's exports grew marginally by 1.5% in April (March: -7.5%), buoyed by the recovery in global demand.
- Adding to the positive signs for China's strong economic performance, the inflation rose for three consecutive months by 0.3% in April.
- However, the downturn in the real estate market is dragging on, with little indication of a major improvement. China's real estate investment fell sharply, declining by 9.8% in the first four months of 2024 (3M2024: 9.5%).
- In a bid to stimulate economic growth, China is prioritising a resurgence in manufacturing, especially high-tech sectors. This strategy aims to counter declining property investment, consumer hesitancy, and inefficiencies in infrastructure spending.

ECB EXPECTED TO CUT INTEREST RATES, DIVERGING FROM U.S FED MONETARY POLICY APPROACH

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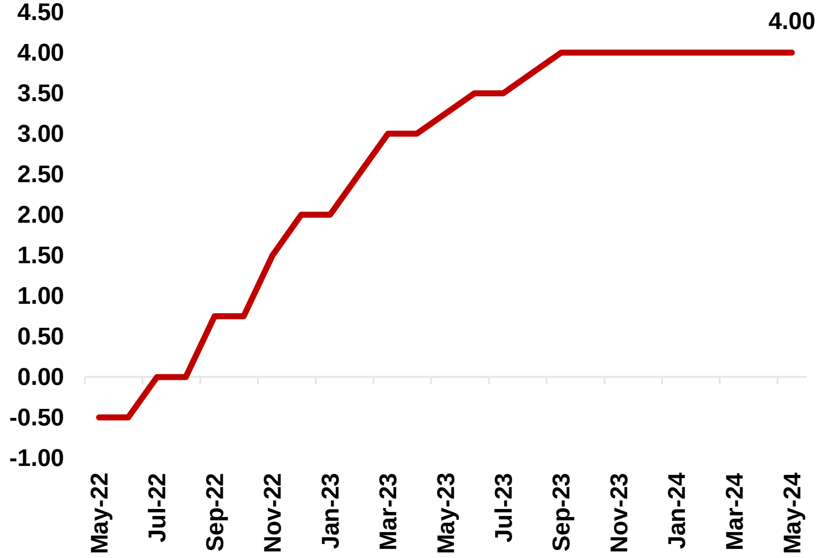
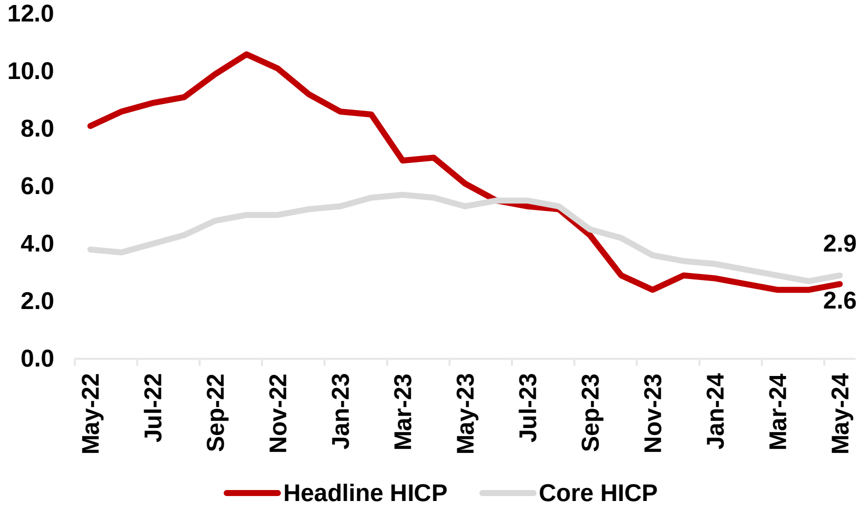
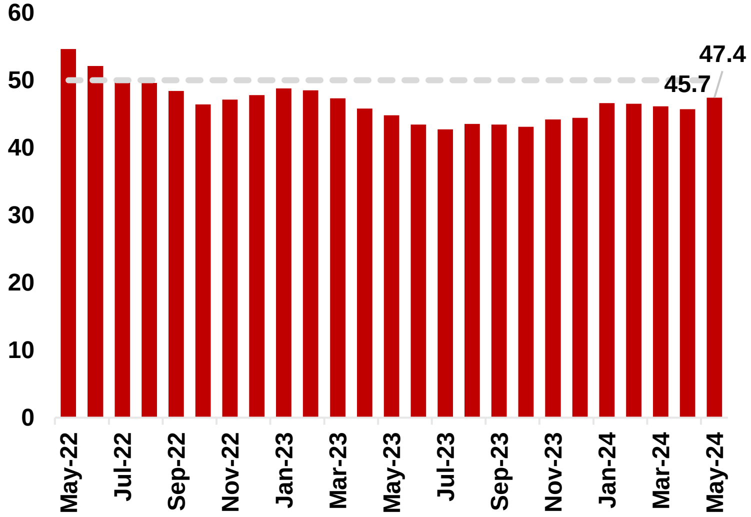
Deposit Facility Rate, %



Eurozone - Harmonised Index of Consumer Prices (HICP), y-o-y%



Eurozone – Manufacturing PMI, points



Sources: ECB, Eurostat, S&P Global

- Headline HICP inflation in the eurozone rose to 2.6% in May, an increase from 2.4% in April and slightly higher than the market expectation of 2.5%. Additionally, core HICP inflation, excluding volatile items like energy and food, also rose in May as it reached 2.9%, up from 2.7% in April and exceeding expectations of 2.8%.
- Eurozone's manufacturing PMI showed some improvement in April, with the PMI index hitting a 15-month high of 47.4 points. This exceeded expectations of 46.1 points, but still not enough to signal growth as the index remains below the expansion threshold of 50.0 points.
- The ECB is set to cut interest rates for the first time in a while this week. However, stubbornly high inflation suggests this would not be the start of a series of rapid rate cuts.
- ECB officials have openly communicated the upcoming interest rate cut and downplayed worries about a difference in approach from the U.S. Fed.

SECTION 3

Domestic Landscape & Banking Sector Update

TRADE PERFORMANCE ON A POSITIVE MOMENTUM, DRIVING EXPANSION IN FACTORY ACTIVITIES ALONGSIDE RESILIENT DOMESTIC DEMAND

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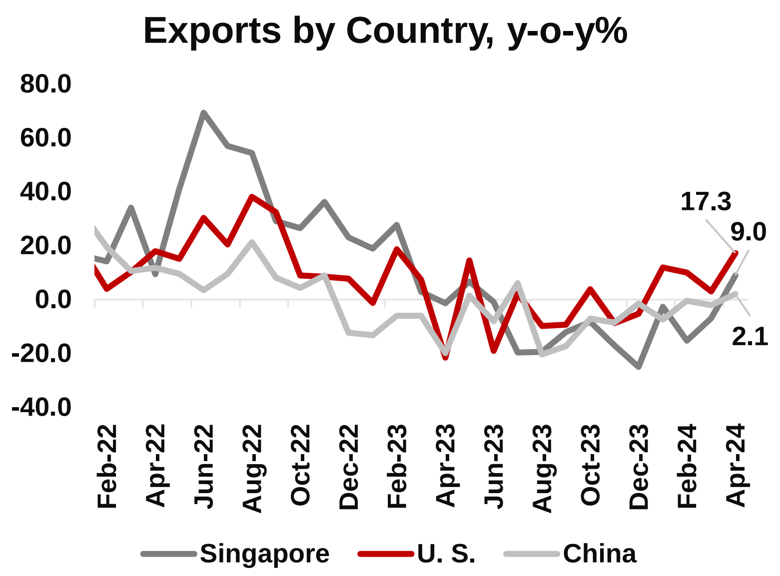
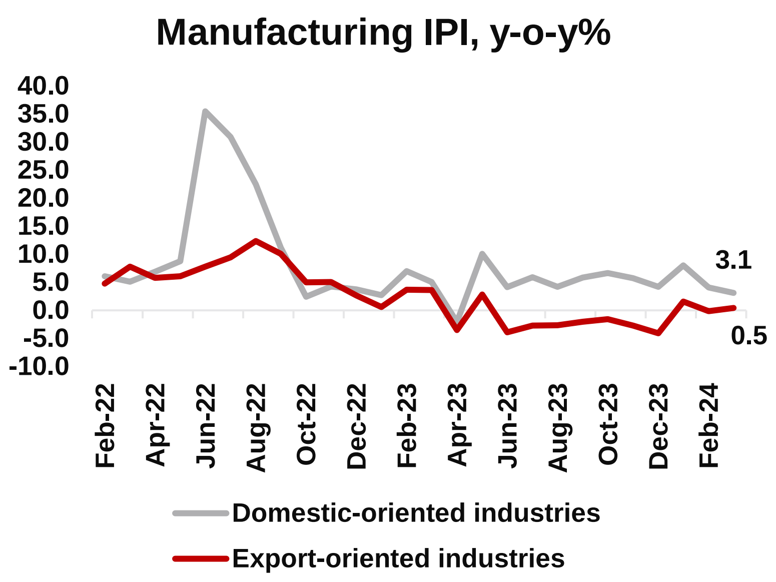
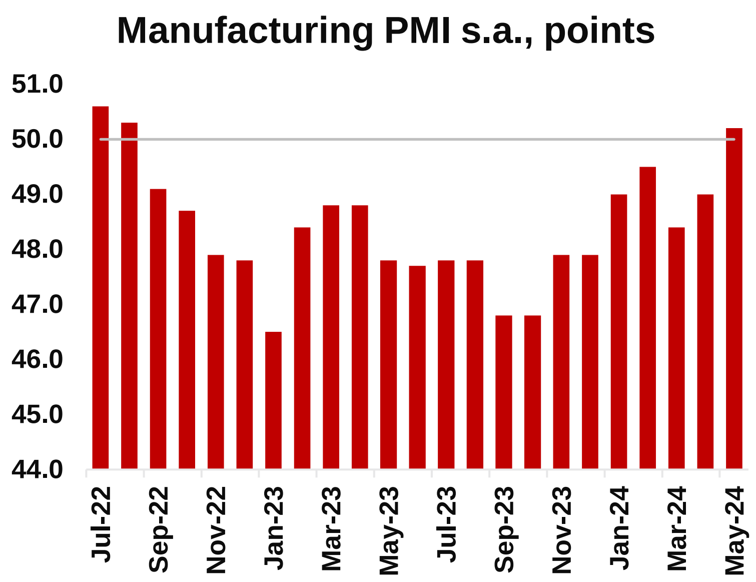


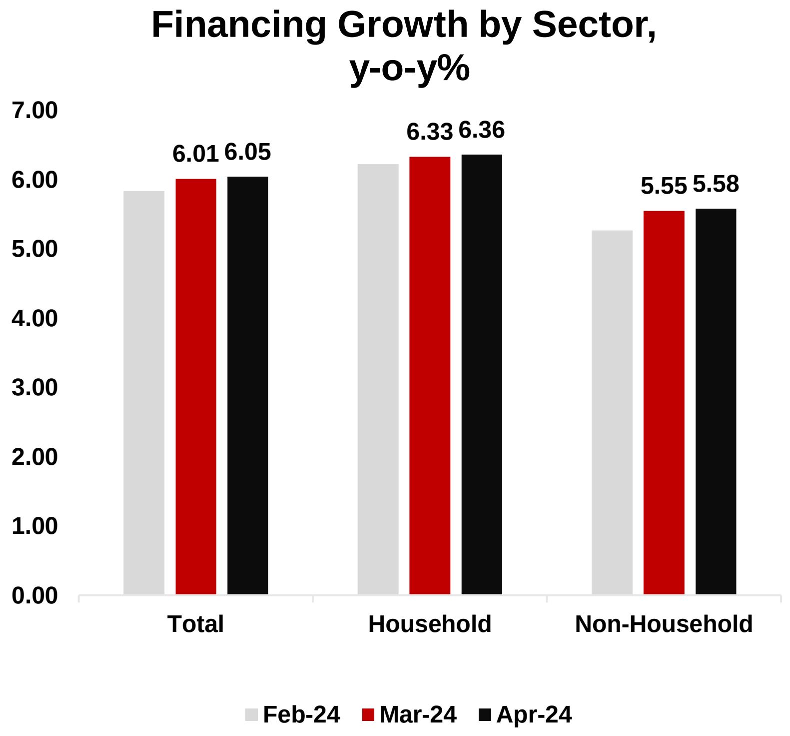


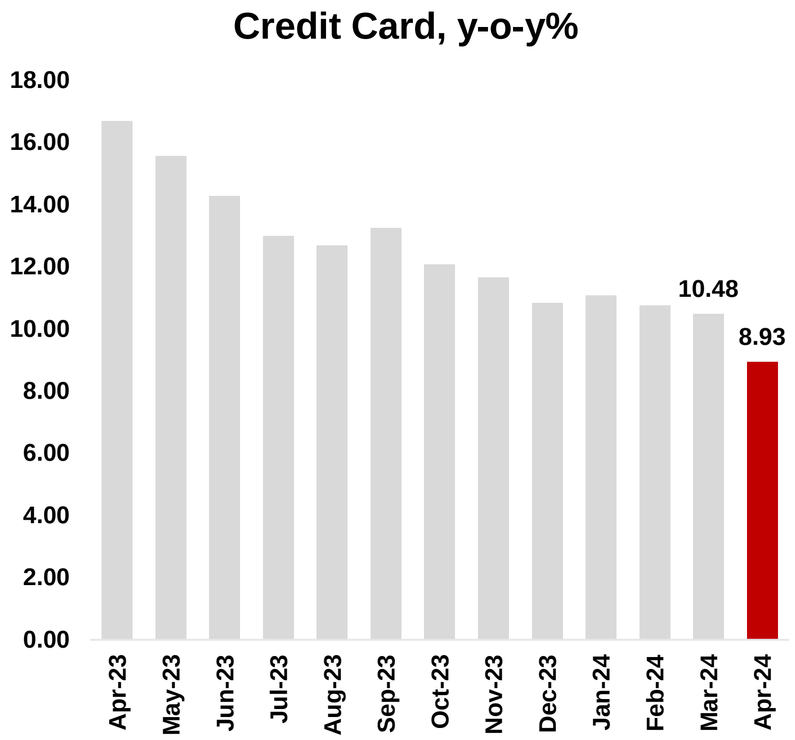


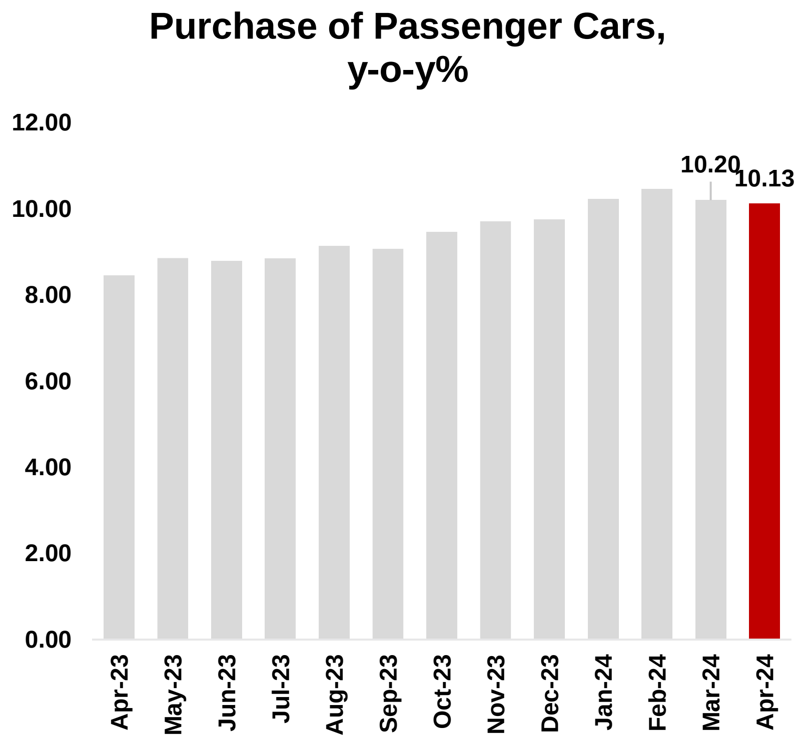
Sources: Department of Statistics Malaysia (DOSM), S&P Global

- Malaysia's exports rebounded better than expected in April, jumping to 9.1% y-o-y from the 0.9% contraction the month before. Such performance was indicative of the recovering external demand with the exports to Malaysia's top three trading partners, namely Singapore, U.S. and China showing positive growth.
- Additionally, the much-anticipated lift from the global semiconductor upcycle has finally materialises with the revival of E&E exports (April: 0.6% vs. March: -1.7%).
- Such performance had supported the IPI which rose by 2.4% in March (February: 3.1%), driven by the growth of the manufacturing IPI (March: 1.3% vs. February: 1.2%).
- Looking closer, the export-oriented industries IPI also experienced a rebound (March: 0.5% vs. February: -0.2%) albeit only slightly while the import-oriented industries increased by 3.1% in the same month (February: 4.1%).
- As domestic and external demand strengthens further, factory activities ramped up with the manufacturing PMI climbing to 50.2 points in May (April: 49.0 points) after trending the contractionary zone for the past twenty consecutive months.

BANKING SECTOR: FINANCING GROWTH PICKED UP IN APRIL







Source: BNM

- Financing activities increased to 6.05% in April, up from 6.01% in March. The non-household segment's financing growth edged up slightly to 5.58% in April (March: 5.55%). Likewise, the growth rate in the household sector experienced a slight increase, reaching 6.36% in April from 6.33% in March.
- The financing growth in the passenger car purchase segment slightly dipped to 10.13% in April (March: 10.20%). Similarly, financing growth in the credit card segment plunged to 8.93% in April from 10.48% in March. Conversely, financing activities related to the purchase of residential property rose to 7.53% in April (March: 7.43%).

BANKING SECTOR: APRIL'S ASSET QUALITY REMAINED INTACT

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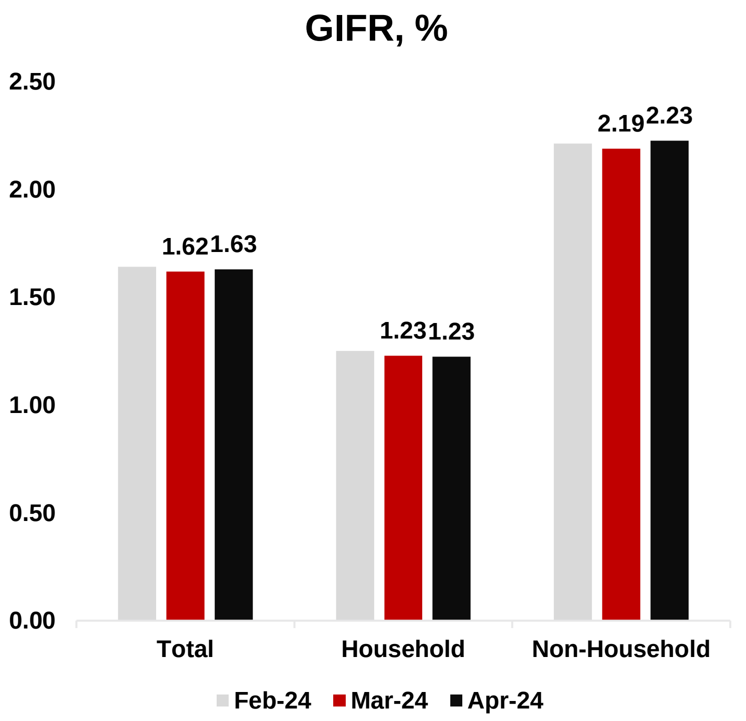

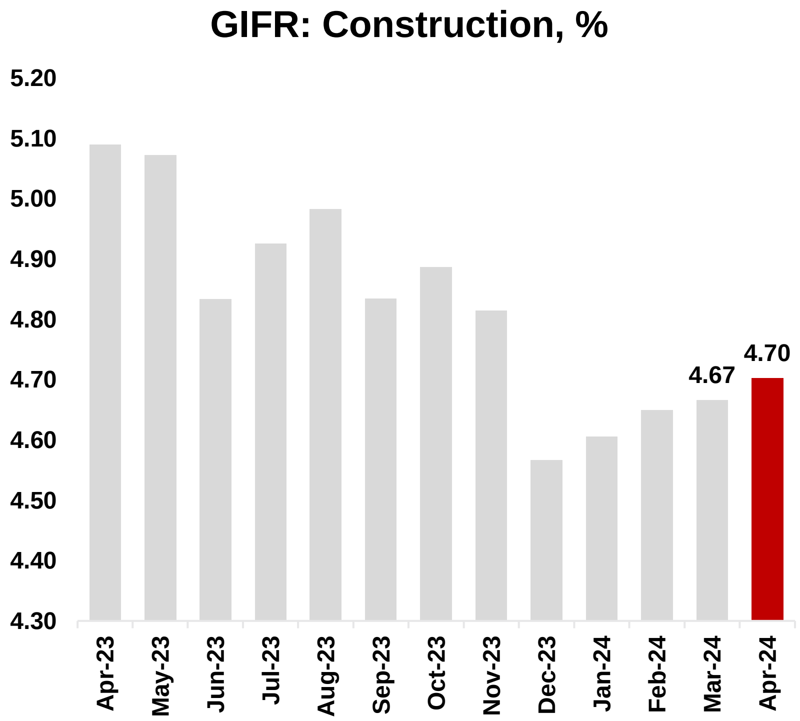

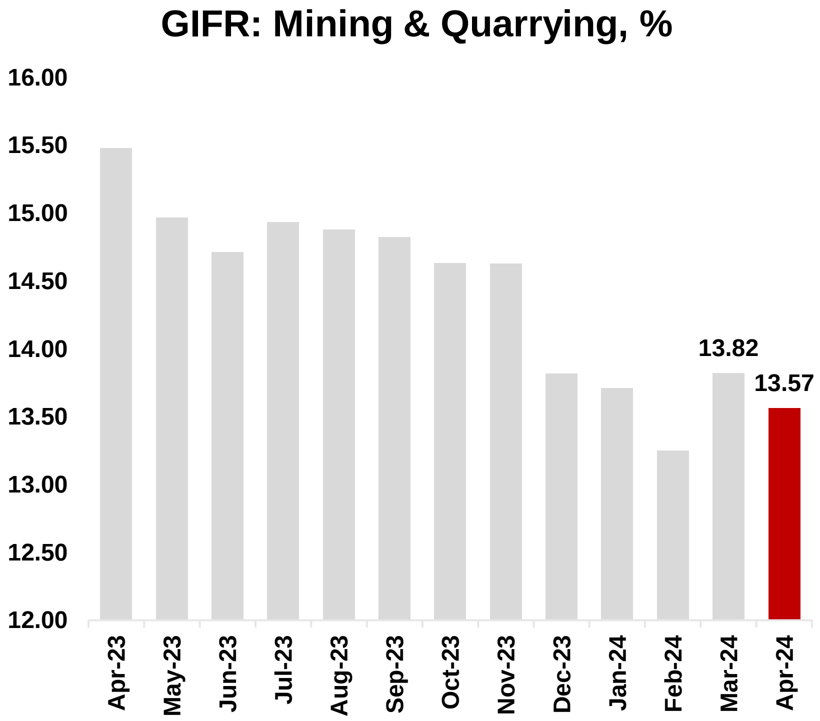

Source: BNM

- Total gross impaired financing ratio (GIFR) in the banking sector held steady at 1.63% in April (March: 1.62%). The GIFR in the household segment remained at 1.23% in April (March: 1.23%). Additionally, the impairment within the non-household sector grew moderately to 2.23% in April (March: 2.19%).
- The impairment within the construction segment rose slightly to 4.70% in April from 4.68% in March. In contrast, the asset quality in the Mining and Quarrying industry declined to 13.57% in April (March: 13.82%).

THANK YOU