

Malaysia: Sept industrial activity- pointing towards smaller 3Q GDP contraction 12 NOVEMBER 2009 2009/0056

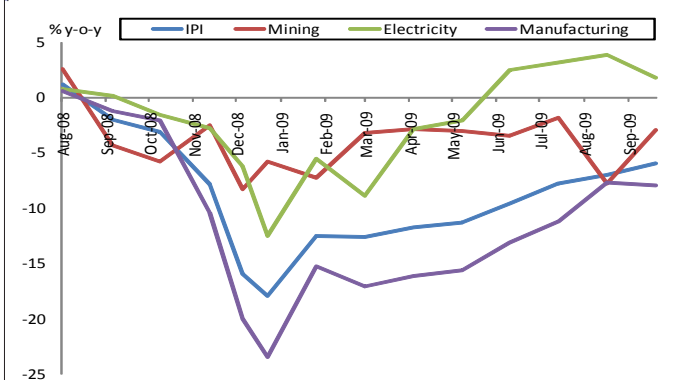
INDUSTRIAL PRODUCTION INDEX

% YOY	IPI	ELEC	MINING	MANUF
2005	3.6	5.8	-1.6	5.1
2006	5.0	5.1	-3.4	7.5
2007	2.0	3.9	3.2	1.9
2008	0.5	1.2	-0.1	0.7
Jun-09	-9.7	2.5	-4.3	-13.0
Jul-09	-7.8	3.1	-1.8	-11.2
Aug-09	-7.0	3.9	-7.8	-7.7
Sep-09	-6.0	1.8	-3.0	-7.9
4Q-08	-9.1	-3.5	-5.6	-11.1
1Q-09	-14.4	-9.1	-5.4	-18.7
2Q-09	-10.8	-0.9	-3.1	-14.9
3Q-09	-6.5	2.9	-2.6	-9.0

Source : Department of Statistics Malaysia, Bank Negara Malaysia

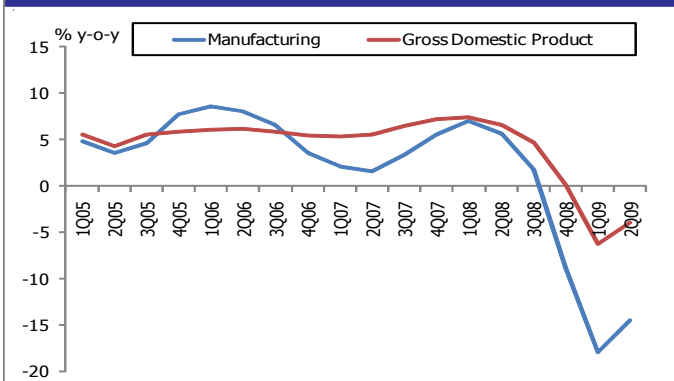
- **Despite the larger than expected drop in the industrial production index (IPI) in September, the contraction continued to narrow, signaling further improvement in growth performance for the third quarter this year.**
- The IPI contracted by 6.0% y-o-y in September, narrowing from -7.0% in August but more than our (-4.8%) and consensus (-3.8%) expectations. On a m-o-m basis, industrial output contracted by a larger magnitude of 2.3% (Aug: -1.9%), marked the second straight decline since August 09.
- The y-o-y uptrend was mainly supported by improvement in the mining sector (Sept: -3.0%, Aug: -7.8%). This resulted in a positive 1.5% m-o-m growth as against a negative 0.2% in August and -3.7% in the same month a year earlier.
- Overall industrial production however was weighed down by lower manufacturing and electricity output. Manufacturing dropped on y-o-y by 7.9% in September (Aug: -7.7%) following m-o-m drop 1.5% (Aug: -0.2%) mainly attributed to the shorter working days in September. The weak performance also reflects the continuing weak global demand for manufacturing products as displayed by a double-digit decline in electrical and electronics (E&E) exports.
- Electricity production also charted a larger drop 1.0% m-o-m (Aug: -0.8%) to result into a smaller y-o-y growth of 1.8% (Aug: +3.9%).
- For the third quarter of 2009, the IPI contracted by a smaller 6.5% y-o-y as against a double-digit decline in the preceding two quarters (2Q09: -10.8%, 1Q09: -14.4%). This was underpinned by a smaller decline in manufacturing of 9.0% and mining output (-2.6%). However, electricity production returned to a positive growth of 2.9%. Furthermore, the expansion on a quarterly basis was broad based. On q-o-q, the IPI growth rate accelerated to 5.9% in 3Q from 2.9% in 2Q.
- The improved domestic industrial performance was in line with the upward trend in the global manufacturing industry. Global factory business activity grew at its fastest pace in 39 months in October as the output index soared to its highest level not seen for more than five years. Also, the US manufacturing expanded in October to 55.7, the highest since April 2006. Other developed economies such as Eurozone and Britain of late also announced firmer recoveries in their manufacturing sector.
- Locally, improvement in manufacturing production (3Q09: -9.0% yoy, 2Q09: -14.9%) and exports (3Q09: -22.3%, 2Q09: -26.3%) point towards better Gross Domestic Product (GDP) for the third quarter. As such, we are

IPI- ELECTRICITY, MANUFACTURING & MINING



Source : Department of Statistics Malaysia, Bank Negara Malaysia

MANUFACTURING VS GROSS DOMESTIC PRODUCT



Source : Department of Statistics Malaysia, Bank Negara Malaysia

retaining our view that 3Q GDP could register a smaller 2.6% y-o-y decline compared with -3.9% in 2Q and -6.2% in 1Q.

- We believe manufacturing output will edge higher going forward as producers begin to replenish stocks in response to the huge inventory drawdown in 1H09. The likelihood of a turnaround in global demand ahead of the year-end festive season could also support improvement in industrial activities.
- On that basis, manufacturing output could possibly chart a smaller contraction in October before posting positive

growth in November and December this year. Coupled with a moderate recovery in the export sector and growing domestic demand, we envisage a positive growth of 1.7% in the 4Q09 GDP, taking the full year average of -2.7%.

- Despite the improving economic conditions, recovery going forward will not be one of steep and straight line. The high unemployment rate in major economies will remain as a main downside risk to global economic recovery, thus similarly on Malaysia's external trade and production activities. This could be compounded by the withdrawal of global stimulus measures and following monetary authorities embarking on exit strategy to contain inflation.