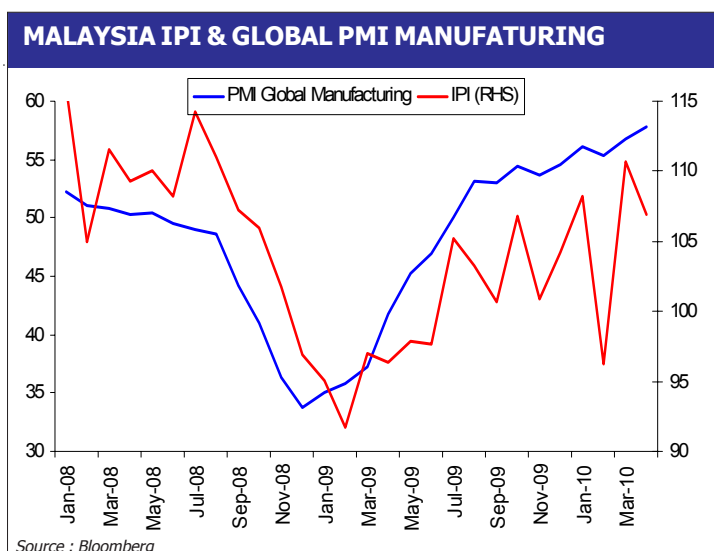
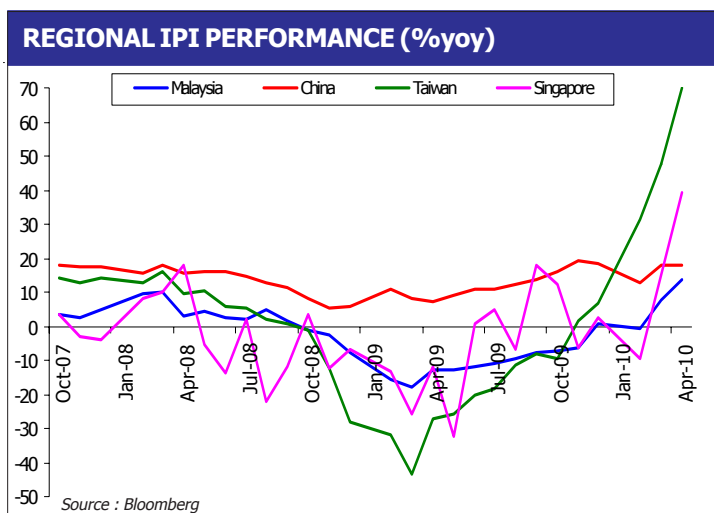
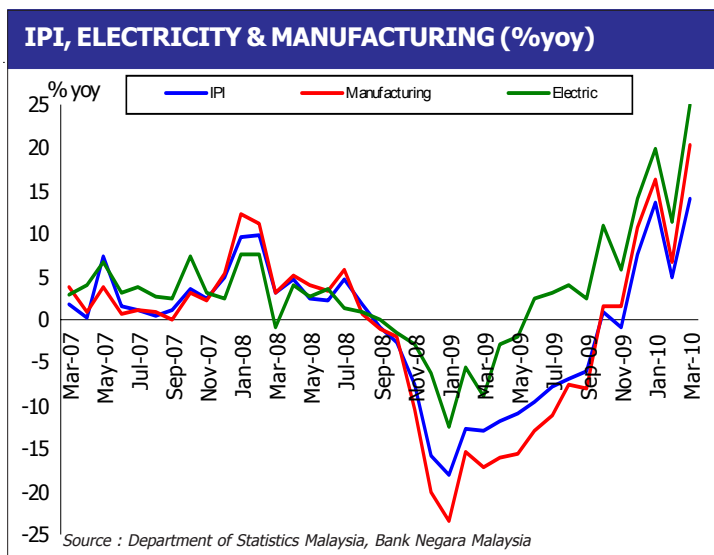


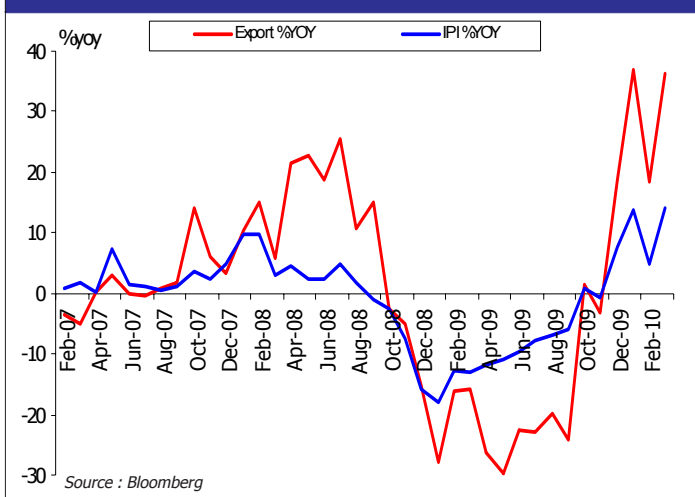
Malaysia: IPI - Solid growth reaffirms strong 1Q10 GDP

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- **As expected, Malaysia's industrial production rebounded strongly in March, in line with the surge in exports. IPI grew by 14.1% yoy in March from 4.8% in February, substantially faster than consensus and our forecast of 12.9% and 13.2% respectively. On a monthly basis, IPI rebounded by 15.1% after contracting by 11.2% in February due to shorter working days.**
- The buoyant production performance in March was mostly supported by expansion in the manufacturing and electricity sectors, which saw output rising at 20.3% and 24.9% yoy respectively, accelerating from 7.1% and 11.4% in February. Within manufacturing, the production of electrical and electronics had surged by 46.1% in March from 31.6% in the preceding month, in response to the 31.8% jump in E&E exports. The mining sector however remained contractionary, decreased by 0.5% in March from 0.3% in February due to continued decline in crude oil production.
- The March IPI marked the highest level since hitting its bottom in February 2009, representing an increase of 20.7%. However, it remained 4.6% short of the pre-crisis peak.
- On a quarterly basis, production had risen by 1.0% in 1Q10 from 0.9% in 4Q09, the fourth consecutive increase. On an annual basis, growth in 1Q10 strengthened sharply to 11.0% from 2.5% in 4Q09.
- The strengthening of industrial activity suggests that the recovery is broadening and gaining pace in 1Q10. Manufacturing and services have expanded significantly, consistent with the recovery in exports and domestic consumption. Exports grew by 28.7% yoy in 1Q10 from 5.1% in 4Q09, while the pace of increase in manufacturing output accelerated to 15.2% from 4.4%. Domestic consumption indicators such as growth in outstanding loans accelerated further to 9.6% in the quarter, from 8.8% in 4Q09, while motor vehicle sales, have also accelerated, indicating a strong uptrend in the services sector.
- **Overall, we expect the 1Q10 GDP to have increased by 10.2% yoy, accelerating from the 4.5% expansion recorded in 4Q09. This is slightly higher than our earlier projection of 9.5% to 10.0%.** The 10.2% GDP expansion will be the fastest since 1Q00 although mostly supported by the depressed base in 1Q09, which was also the weakest point of the downcycle following global economic crisis.

MALAYSIA IPI & EXPORTS (%yoy)



- However, the value of GDP in 1Q10 remained about 1.8% below the level in 3Q08, before the economy slid into recession in 1Q09. The level of manufacturing output and total exports, the two most affected areas during the global financial crisis, is estimated to remain lower by 8.5% and 12.5% lower respectively compared to the 3Q08 level.
- On the monetary policy front, the strengthening of 1Q10 economic performance provides flexibility for BNM to normalise interest rate. In this regard, we expect BNM to hike the OPR by another 25bps to 2.50% on Thursday's MPC meeting.
- Going forward, we are expecting the strong growth in industrial production to be sustained through 2Q10 as the global recovery continues and the inventory cycle gains a greater pace. In particular, continued recovery in exports would support growth in E&E production, and overall expansion in manufacturing sector. At this juncture, Malaysia's production growth is still lagging behind its regional peers such as Singapore, Thailand and Taiwan which all reported more than 30% yoy growth in industrial production, suggesting that local production has the potential for an acceleration to align with regional performances.

- The global and local indicators are also pointing towards further strengthening of manufacturing activities during 2Q10. The Global PMI Manufacturing Index rose to its highest level since May 2006 to 57.8 in April 2010, while the Baltic Dry Index, an indicator of global trade volume, had increased by 87.8% yoy in the same month from 85.6% in March. Domestically, the acceleration in growth of imports of intermediate goods to 36.7% in March from 26.4% in February suggests faster industrial production to meet external and domestic demand, while the turnaround in outstanding manufacturing loans by 1.9% yoy in March from -0.2% in February is indicating capacity expansion by manufacturers.
- As a result, 2Q09 GDP is expected to sustain a robust growth of 7.5% to 8.0%, taking the average 1H10 GDP increase to range between 8.5% to 9.0%.
- However, the growth pace in industrial production is expected to moderate in 2H10, as the base effect begins to normalise and recovery momentum slows, partly due to the waning effect of global stimulus packages. The pace of growth is also expected to be uneven and volatile as economic hiccups such as the European sovereign debt crisis would affect confidence and interrupt the growth trajectory.
- The GDP growth performance therefore is expected to be slower in 2H10 to a range of 5.5% to 6.0%, given the aforementioned reasons. **For the full year 2010, we are now projecting Malaysia's GDP growth to range between 7.0% to 7.5%, after contracting by 1.7% in 2009.**
- As BNM continues to embark on normalising interest rate, on the back of strong trade performance and overall economic growth, we expect another 25 bps hike to be made in September, thus taking the year end OPR to 2.75%. However, we are not discounting the possibility of BNM to also raise the OPR in July, which could take the benchmark interest rate to 3.00% by year end.

INDUSTRIAL PRODUCTION INDEX

	IPI			Manufacturing			Mining			Electricity		
	Index	% yoy	% mom	Index	% yoy	% mom	Index	% yoy	% mom	Index	% yoy	% mom
2008	99.7	0.5		112.1	0.7		98.2	-0.1		110.5	1.2	
2009	109.4	-7.5		101.0	-9.9		94.9	-3.4		111.6	1.0	
Mar-09	97.0	-13.0	5.8	95.5	-17.0	3.5	99.3	-4.4	10.9	101.2	-8.9	4.1
Apr-09	96.3	-11.8	-0.7	96.4	-16.1	0.9	93.5	-3.3	-5.8	110.1	-3.0	8.8
May-09	97.9	-11.0	1.7	97.0	-15.6	0.6	96.6	-2.0	3.3	114.5	-2.1	4.0
Jun-09	97.7	-9.7	-0.2	99.9	-13.0	3.0	89.7	-4.3	-7.1	114.7	2.5	0.2
Jul-09	105.2	-7.8	7.7	107.1	-11.2	7.2	98.6	-1.8	9.9	118.7	3.1	3.5
Aug-09	103.2	-7.0	-1.8	106.9	-7.7	-0.2	92.8	-7.8	-5.9	117.9	4.1	-0.7
Sep-09	100.8	-6.0	-2.5	102.7	-8.2	-3.9	94.1	-3.1	1.4	111.7	2.4	-5.3
Oct-09	106.8	0.9	6.1	110.5	1.5	7.0	96.4	-2.6	2.4	120.5	11.0	7.9
Nov-09	100.9	-0.7	-5.5	104.6	1.8	-5.3	91.0	-7.3	-5.6	112.9	5.9	-6.3
Dec-09	104.2	7.5	3.3	105.9	10.8	1.2	98.3	-0.2	8.0	117.3	14.2	3.9
Jan-10	108.2	13.8	3.8	109.5	18.2	3.5	103.3	4.0	5.1	119.8	19.8	2.1
Feb-10	96.2	4.8	-11.2	98.9	7.1	-9.7	88.2	-1.4	-14.6	108.3	11.4	-9.6
Mar-10	110.7	14.1	15.1	114.9	20.3	16.3	96.7	-0.5	11.9	126.4	24.9	16.8
1Q08	110.5	7.2	-0.7	115.0	8.7	-0.2	101.5	4.4	-1.8	109.4	4.5	4.5
2Q08	109.1	3.1	-1.3	114.9	4.2	-0.1	96.2	0.5	-5.1	114.1	3.3	4.3
3Q08	110.3	1.4	1.0	116.1	1.8	1.0	97.7	0.8	1.5	112.5	0.7	-1.4
4Q08	101.2	-9.1	-8.2	102.5	-11.1	-11.8	97.6	-5.6	-0.2	106.0	-3.5	-5.8
1Q09	94.6	-14.4	-6.5	93.5	-18.8	-8.8	96.0	-5.4	-1.6	99.5	-9.1	-6.1
2Q09	97.3	-10.8	2.9	97.8	-14.9	4.6	93.3	-3.1	-2.9	113.1	0.9	13.7
3Q09	103.1	-6.5	5.9	105.6	-9.1	8.0	95.2	-2.6	2.0	116.9	3.9	3.4
4Q09	104.0	2.5	0.9	107.0	4.4	1.4	95.2	-2.4	0.1	116.9	10.3	0.0
1Q10	105.0	11.0	1.0	107.8	15.2	0.7	96.8	0.7	1.6	118.2	18.8	1.1

Source : Department of Statistics, Bloomberg, Research Divison PNB