Economy

AMB

MALAYSIA - INDUSTRIAL ACTIVITIES ON A SOFT PATH

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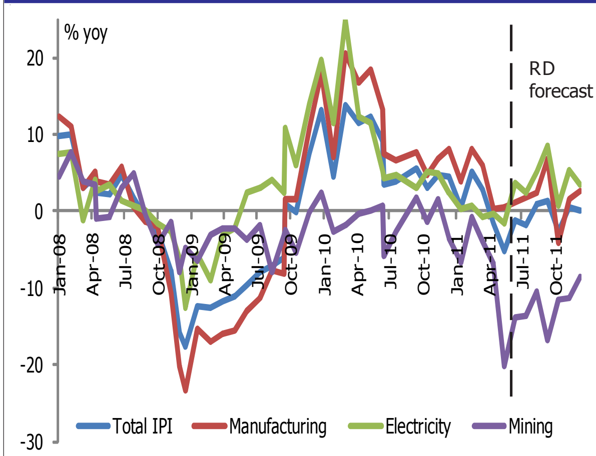
Malaysia's industrial activity continued to slide in May. The industrial production index (IPI) fell for the second straight month by 5.1% in May'11, and widening from 2.1% in the preceding month.

The performance of the mining and electricity sectors had weakened for the third consecutive month in May with the mining output posting a 20.1% fall, its biggest contraction since 1995 and the electricity output reduced by 1.6% from -0.4% in Apr'11.

The manufacturing sector performance on the other hand recorded an improvement in May but remained lethargic with a growth of 0.6% yoy compared with 0.3% in the preceding month.

On the back of continued weakening in global demand and the disruption in the global supply chain, domestic industrial production is expected to register another fall in June, thus to slow the overall 2Q11 to 4.0-4.3% from 4.6% in 1Q11.

MALAYSIA INDUSTRIAL ACTIVITIES



Source : DOSM, RESEARCH DIV. PNB

- **IPI fell the most since Sept'09.** The IPI dropped by 5.1% yoy in May'11 from 2.1% in Apr'11, marking the second consecutive fall for this year. This is the biggest rate of drop since Sept.'09 (-6.9%) and far exceeded the consensus expectations of -3.1%. However, on mom, the rate of contraction had narrowed significantly to 0.9% from -7.6% in April on account of higher manufacturing and electricity, suggesting of high base effect to depress the annual growth of the overall IPI.

- **Manufacturing growth remained flat.** Manufacturing production, which accounts for almost 64% of total IPI, generally remained flat for two straight months (May'11:+0.6% yoy, Apr'11:+0.3%). On the other hand, manufacturing output charted an increase of 2.4% on mom in May, reversing from a decline of 7.5% in the previous month. However, the sector generally had remained weak, affected by the global supply chain disruptions arising from Japan's March 11 earthquake and slowing global demand particularly for the electrical and electronics (E&E) products.

- **Electricity output weakened.** Electricity production declined for the third consecutive month in May (-1.6% yoy, Apr'11:-0.4%, Mar'11:-0.7%). This was despite a 2.1% mom gain, reversing from 1.9% drop in Apr'11. The weakening electricity sector reflects the softening demand especially following the slide in industrial activities.

- **Mining output declined on shutdown of gas production platforms.** Mining output unexpectedly dropped by a double-digit 20.1% yoy in May'11, the steepest decline since 1995, from -6.9% yoy in Apr'11. The index, which is the second largest component in the IPI after manufacturing (31% of total IPI), fell mom by a double-digit 12.2%, mainly due to the fall in the crude oil and natural gas index. On a yoy basis, the crude oil index plunged by 24.2%, while the natural gas index declined by 10.7% following the shutdown of production platforms by Petronas due to maintenance works.

- **Slowing manufacturing, exports to weigh down 2Q11 GDP.** We are expecting Malaysia's industrial activity to continue sliding in June, in the face of the softening weakness in the global demand for manufactured goods and the on-going global supply chain problems. The weakness in the domestic manufacturing outlook is also to reflect the downtrend in global manufacturing

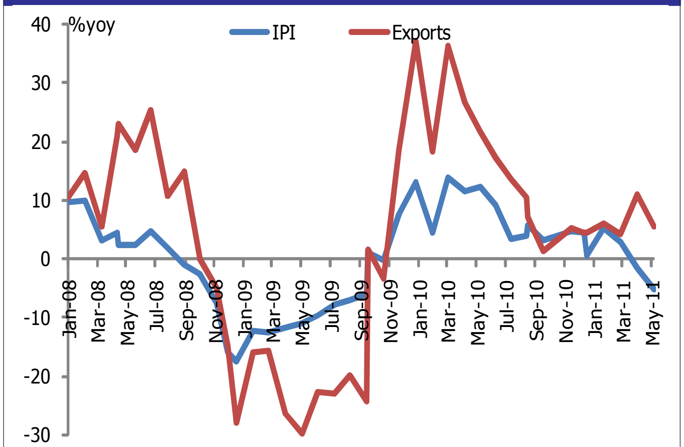
INDUSTRIAL PRODUCTION INDEX

	May-11			Apr-11			Apr-May'11	1Q11
	Index	% mom	% yoy	Index	% mom	% yoy	% yoy	
Total IPI	104.4	-0.9	-5.1	105.3	-7.6	-2.1	-3.6	2.8
Manufacturing (63.5%)*	115.6	2.4	0.6	112.9	-7.5	0.3	0.4	6.0
Mining (30.6%)*	77.0	-12.2	-20.1	87.7	-7.5	-6.9	-13.5	-3.9
Electricity (5.9%)*	125.7	2.1	-1.6	123.1	-1.9	-0.4	-1.0	0.0

*Source : DOSM, RESEARCH DIVISION PNB, *indicates weightage* activity as measured by its Purchasing Manager Index (PMI) in June (52 June from 53 in May). In tandem, we expect the overall domestic GDP growth to moderate further to around 4.0-4.3% yoy in the 2Q11 from 4.6% yoy in the 1Q11.

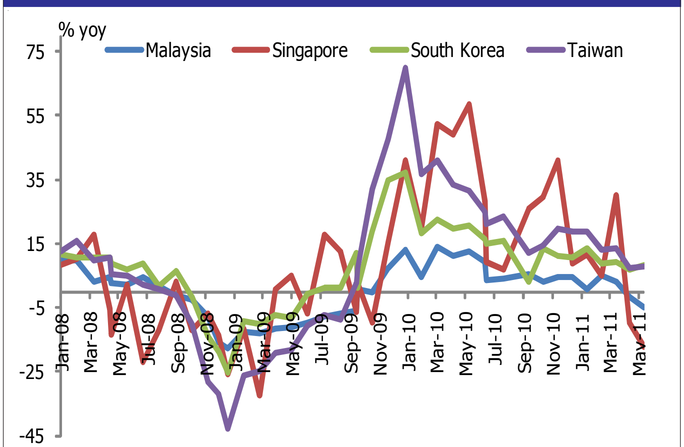
- **Manufacturing and IPI to regain traction in 2H11.** We believe that manufacturing activity may gain traction in the second part of the year, backed by improving global supply chain as Japan normalizes production level and firmer global demand on improving economic conditions in the United States and the European Union. The downside risks to global growth, however, remain high especially with the recent increase in the US jobless rate (June 9.2%, May 9.1%) coupled with its still weak housing sector, the slowdown in China's economy partially contributed by tightening measures to curb inflation, the unresolved sovereign debt issues in the Euro zone economies, and the unabated geopolitical tensions in the MENA. At this juncture, we are projecting the domestic industrial production to chart a slower growth rate by 1-2% this year from 7.5% in 2010, thus reducing the overall GDP growth rate to 5.4% from 7.2% in 2010.

IPI fell the most since Sept. 09



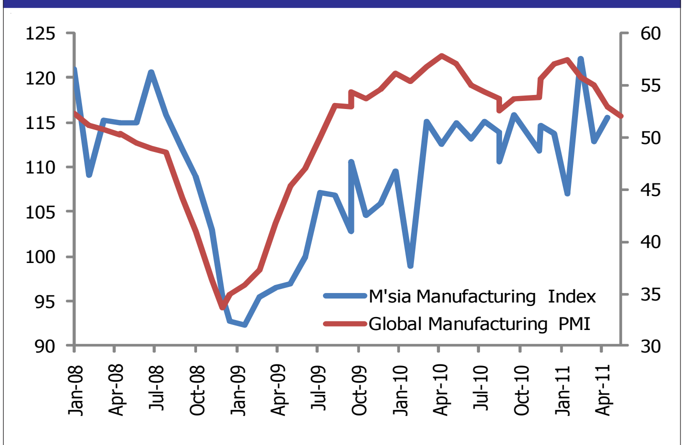
Source : DOSM, RESEARCH DIV. PNB

Malaysia still lags behind regional economies



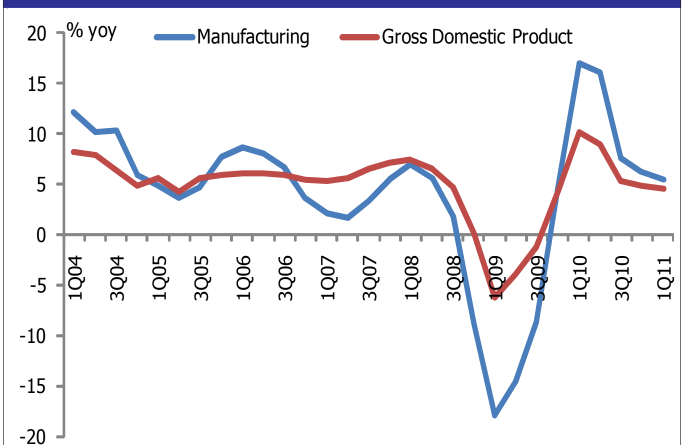
Source : DOSM, BLOOMBERG LP, RESEARCH DIV. PNB

Slowing global manufacturing activities



Source : DOSM, BLOOMBERG LP, RESEARCH DIV. PNB

Slowing manufacturing will lead to slower GDP growth



Source : DOSM, RESEARCH DIV. PNB