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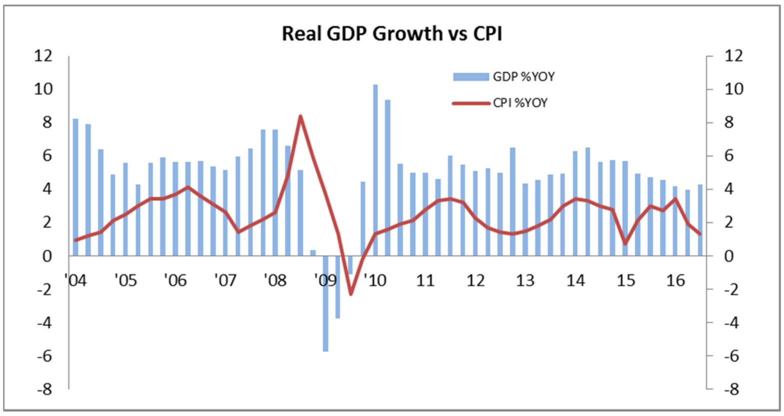
GDP growth ticked up for the first time in six quarters

The Malaysian economy snapped a five straight quarters of growth moderation and increased at its fastest pace in three quarters, by 4.3% YOY in 3Q. A rebound in net exports was the savior, offsetting the softer growth traction in domestic demand dragged by slower public spending and investment. While we see a higher headline GDP print, the rather hefty pullback in domestic demand growth to just 4.7% YOY in 3Q vs 2Q's 6.3% raised concerns if domestic growth momentum is at risks of faltering again. Hence, although the better than expected 3Q GDP print prompted us to revise our full year growth forecast higher to 4.2% (previous 4.0%), it is premature to conclude that the Malaysian economy is on a solid recovery path. In addition, the most recent outcome of the US Presidential election could also reignite global uncertainty and external risks, hence triggering increased market volatility that could have macroeconomic and policy implications. Amid a still uncertain backdrop, we feel it is too early to totally remove an OPR cut from the radar despite acknowledging that recent development has reduced the odds of a cut in the near term.

Real GDP grew at its fastest pace in three quarters, by 4.3% YOY in 3Q

Malaysia real GDP growth snapped a five straight quarters of moderation to increase 4.3% YOY in 3Q16 (2Q16: +4.0% YOY). This was a pleasant surprise vs our estimate of 3.9% and consensus estimate of 4.0%. Growth bounced back from 2Q's GFC-low and marked its first uptick in six quarters, spurring hopes the Malaysian economy may have seen its trough. **The surprisingly upbeat reading was due to a turnaround in net exports to +5.9% YOY (2Q: -7.0%), which offset slower expansion in domestic demand (+4.7% vs +6.3%) dragged by slower growth from both the private and public sectors.**

While private consumption continued to increase at a faster pace for the 4th straight quarter, its momentum has abated somewhat (3Q: +6.4%; 2Q: +6.3%; 1Q: +5.3%). Despite this, private consumption remained the main growth driver, amid **slower expansions in gross fixed capital formation (+2.0% vs +6.1%) and public expenditure (+3.1% vs +6.5%). On a seasonally adjusted QOQ basis, real GDP growth picked up for the first time in three quarters to 1.5% in 3Q** (2Q: +0.7%).

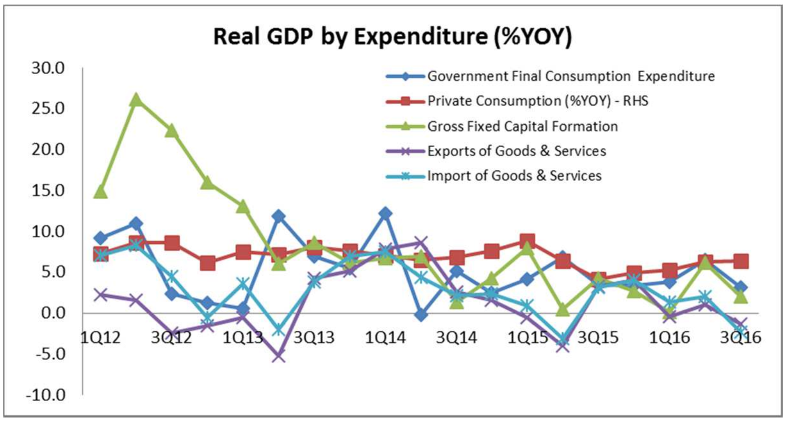


Net exports contribution the savior, offsetting slower growth in domestic demand

While we see a higher headline GDP print, **the rather hefty pullback in domestic demand growth to just 4.7% YOY in 3Q vs 2Q's 6.3% raised concerns if**

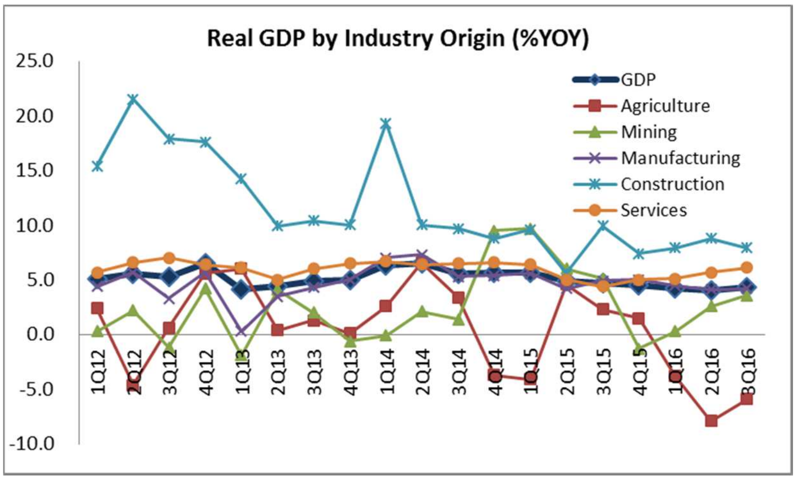
domestic growth momentum is at risks of faltering again. This worry is not unfounded since both consumer and business confidence indices by MIER had plunged below the 100-threshold to 73.6 and 83.9 respectively in 3Q, signaling a less optimistic outlook ahead. **Private sector activities grew at a slightly slower pace of 6.0% YOY in 3Q (2Q: +6.1%) while growth in public sector activities plummeted to 0.3% YOY in 3Q (2Q: +6.9%),** no thanks to a 3.8% YOY contraction in public investment and halved public spending growth of 3.1% YOY. Private sector activities were holding up better as quicker increase in private spending (+6.4% vs +6.3%) cushioned the slower growth in private investment (+4.7% vs +5.6%).

Net exports bounced back into positive territory for the first time in three quarters, increasing 5.9% YOY in 3Q (2Q: -7.0%), as exports of goods and services contracted at a smaller pace of 1.3% YOY in 3Q vs a 2.3 YOY decline in imports (2Q: +1.0%; +2.0%). On the contrary, inventories drawdown (-1.6% YOY) remained a drag on overall GDP growth.



Services and manufacturing remained in the forefront of growth

On the supply side, **all sectors registered improvement with the exception of slower growth in the construction sector. Services and manufacturing sectors remained in the forefront in spearheading growth**, growing 6.1% and 4.2% YOY respectively in 3Q (2Q: +5.7% and +4.1%). Consumption-related services were the biggest growth driver for services while the manufacturing sector was boosted by export-oriented industries. Higher crude oil production led to quicker growth in mining (+3.6% vs +2.6%) but lagged effect of El Nino on CPO yields resulted in extended, albeit smaller, decline in the agriculture sector (-5.9% vs -7.9%). Meanwhile, growth in the construction sector tapered off to 7.9% YOY in 3Q (2Q: +8.8%), supported by continued expansion in civil engineering subsector.

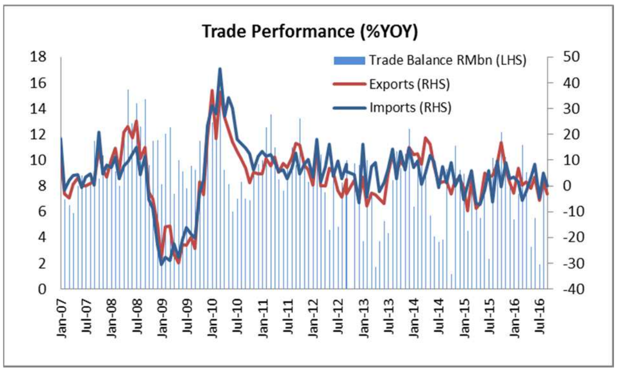


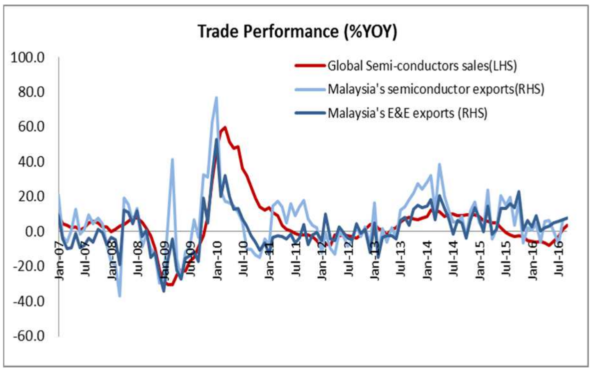
Tripling in current account surplus eased concerns on twin deficits

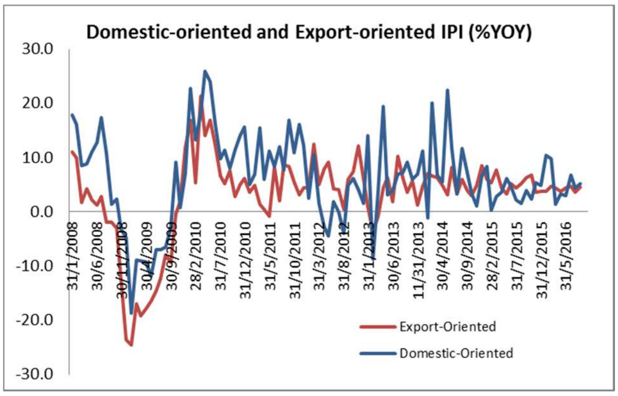
In a separate release, Malaysia's **current account surplus tripled to RM6.0bn in 3Q16, from RM1.9bn in 2Q16,** boosted by an RM6.7bn increase in surplus in the goods account to RM26.5bn (2Q: RM19.8bn). **This should further ease concerns of a twin deficits as solid surplus in the goods accounts continued to offset higher deficits in the services and income accounts.** Deficit in the services account widened to RM5.1bn while deficit in the income account widened to RM15.4bn in 3Q16 (2Q: -RM4.6bn and -RM13.3bn). The capital account reported a net outflow of RM7m vs a net inflow of RM118m in 2Q16 while the financial account saw net outflows for the first time in three quarters, of RM6.3bn (RM9.5bn in 2Q16) as a result of net outflow of portfolio investment (RM10.6bn) which offset the net inflows of FDI (RM6.5bn).

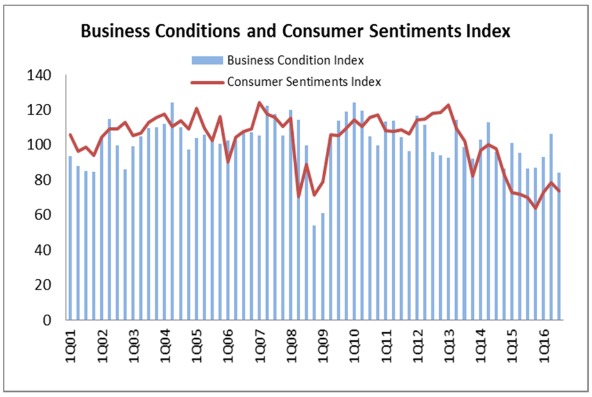
Full year growth revised higher to 4.2%...odds of a OPR cut lower in the near term

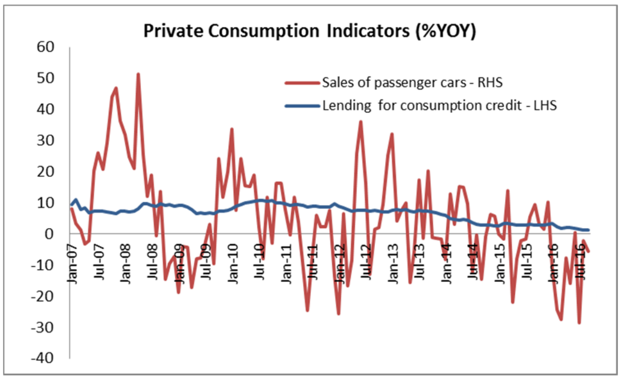
Despite the better than expected 3Q GDP print which prompted us to revise our full year growth forecast higher to 4.2% (previous 4.0%), it is premature to conclude that the Malaysian economy is on a solid recovery path. While we reckon external risks have dwindled somewhat recently, overall lift in exports could be dampened by signs of softer growth momentum in domestic demand. As mentioned above, both consumer and business sentiments have reversed course and plunged below the 100-threshold separating optimism and pessimism, signaling potential pullback in consumer spending and business activities in the immediate quarters ahead. In addition, the most recent outcome of the US Presidential election could also reignite global uncertainty and external risks, hence triggering increased market volatility that could spill over to the macro front. **Amid a still uncertain backdrop, we feel it is too early to totally remove an OPR cut from the radar despite acknowledging that recent development has reduced the odds of a cut in the near term.**

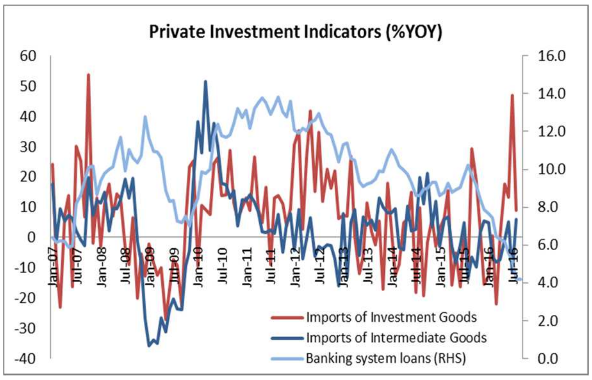

Trade Performance (%YOY)
Trade Balance RMbn (LHS)
Exports (RHS)
Imports (RHS)


Trade Performance (%YOY)
Global Semi-conductors sales(LHS)
Malaysia's semiconductor exports(RHS)
Malaysia's E&E exports (RHS)


Domestic-oriented and Export-oriented IPI (%YOY)
Export-Oriented
Domestic-Oriented


Business Conditions and Consumer Sentiments Index
Business Condition Index
Consumer Sentiments Index


Private Consumption Indicators (%YOY)
Sales of passenger cars - RHS
Lending for consumption credit - LHS


Private Investment Indicators (%YOY)
Imports of Investment Goods
Imports of Intermediate Goods
Banking system loans (RHS)

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