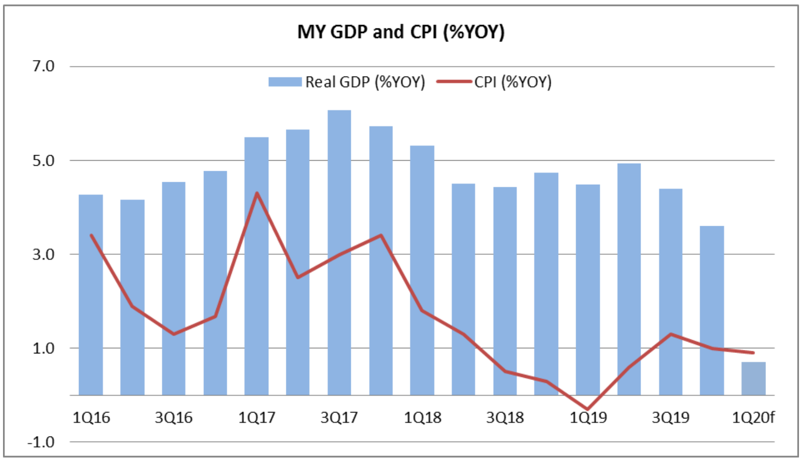
At the brink of a recession

The Malaysian economy managed to register a small positive gain of 0.7% YOY in 1Q, *a tad below our projection for a 1.2% growth but way better than consensus estimate for a 1.0% contraction. The sharp deceleration in growth was due to softer growth in domestic demand as well as a bigger drag from net exports, no thanks to the Covid-19 pandemic and Movement Control Order (MCO) in the second half of March. The macro landscape has become increasingly challenging amid protracted uncertainties surrounding the Covid-19 pandemic. Recent plunge in global crude oil prices as well as demand and supply disruption globally are expected to exacerbate the downside risks to domestic growth prospects, which are expected to hinge heavily on the containment of the pandemic, effectiveness of the recently introduced fiscal and monetary stimulus and how the world rides out of a global recession. Pessimism among the local business communities and consumers are expected to dampen investment and consumption activities, though some reliefs and supports are expected out of the PRIHATIN stimulus package. Against such an uncertain and unprecedented backdrop which requires reforms and new normal from all fronts, we believe Malaysia would not be able to spare itself from slipping into a recession this year. We are projecting a 4.3% YOY contraction in the Malaysian economy for 2020, expecting the sharp contraction in economic activities amid the MCO/ CMCO in 2Q to only recover gradually towards the end of the year. While there is still policy space to further support economic growth, we are of the view that BNM may opt to pause to assess the effectiveness of monetary and fiscal easing measures introduced todate, barring any escalation of downside growth risks.*

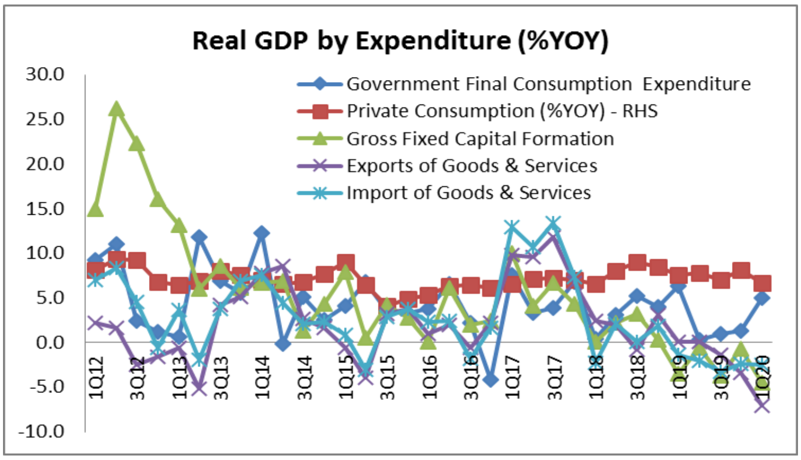
1Q GDP grew at its weakest pace since GFC, by a mere 0.7% YOY dampened by softer domestic demand and a bigger contraction in net exports

The Malaysian economy lost steam for the 3rd straight quarter, not surprisingly given how the world and the domestic economy had succumbed to the Covid-19 pandemic, a widely recognized health and socioeconomic crisis globally. **Growth decelerated sharply to a mere 0.7% YOY in 1Q20 (4Q19: +3.6% YOY),** a tad below our forecast of +1.2% but beating consensus estimate for a 1.0% contraction. Understandably, **domestic demand expanded at a much weaker pace** of 3.7% YOY in 1Q20 (4Q: +4.8% YOY) amid softer private consumption and investment while **net exports also exerted a bigger drag** (-37.0% vs -12.4% YOY) in the wake of fast dwindling global demand. **On a seasonally adjusted basis, 1Q GDP contracted by 2.0% QOQ (4Q: +0.6%).**



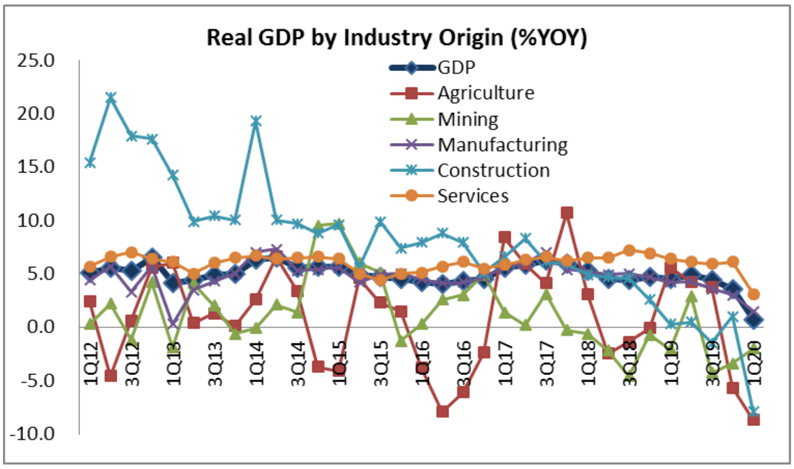
Softer private consumption and extended fall in investment dampened overall domestic demand

On the demand side, domestic demand slowed considerably as the pandemic curtailed consumer spending and business activities especially towards the later part of the quarter, where the MCO led to an almost complete halt on non-essential services. **The expansion in domestic demand, albeit softer at 3.7% YOY, was mainly underpinned by continuous growth in private consumption (+6.7% vs +8.1% YOY),** as consumers front-loaded purchases of consumer staples such as food and beverages as well as communication. This helped cushion the impact from a softer labour market and income. **Government spending, the only segment that registered bigger gain** (+5.0% vs +1.3% YOY) provided further support to overall growth. **Gross fixed capital formation extended its decline for the 5th consecutive quarter,** falling by 4.6% YOY in 1Q (4Q: -0.7% YOY), dragged by lower investments from both the private (-2.3%) and public (-11.3%) sectors, reflecting bleak growth outlook and pessimism among businesses.



Services and manufacturing provided the much needed support, albeit growing at half the pace

By economic sectors, the two key sectors, **services and manufacturing**, that contributed 58% and 22% to overall GDP respectively, **continued to see positive, albeit slower growth.** The services sector expanded 3.1% YOY in 1Q20, half the growth pace in 4Q19, supported by the information & communication, wholesale & retail, and finance & insurance subsectors. Coincidentally, growth in the manufacturing sector also halved to 1.5% YOY in 1Q20, supported by the E&E, optical equipment, petroleum, chemical, rubber & plastic products. Meanwhile, **mining and agricultural sectors continued to contract,** by 2.0% and 8.7% YOY respectively (4Q19: -3.4% and -5.7% YOY), as a result of continued declines in the production of crude oil due to supply disruption and palm oil. Construction GDP took a turn and fell 7.9% YOY in 1Q20 (4Q19: +1.0%), its worst since 2Q99, hit by slower activities in civil engineering, residential and non-residential buildings.

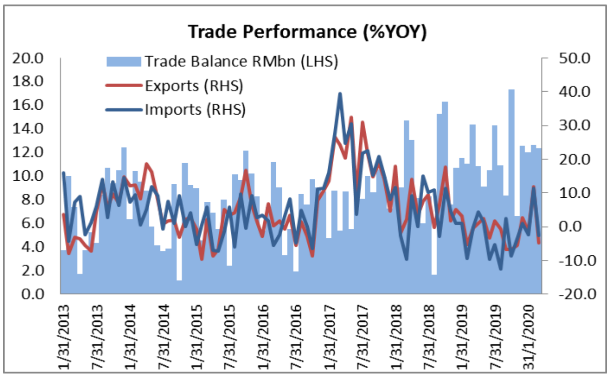


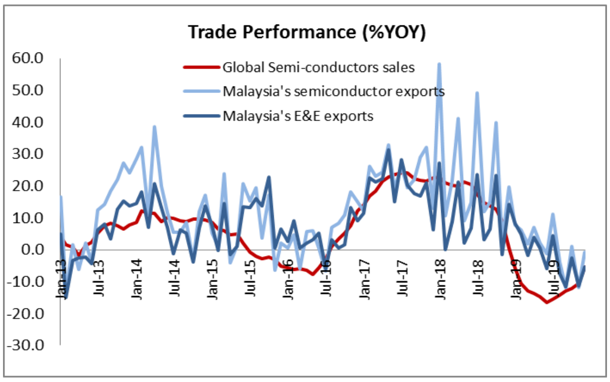
Current account surplus widened again to RM9.5bn on smaller deficit in primary income account

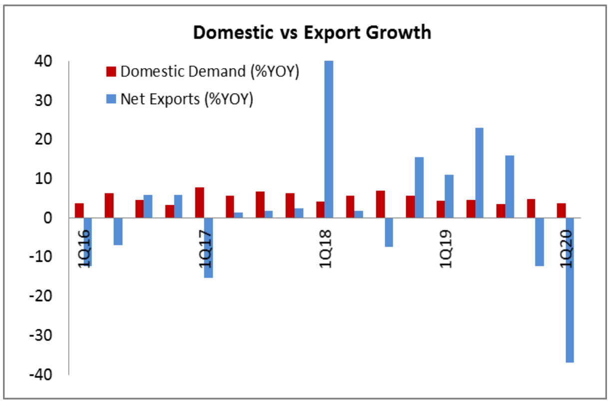
In a separate release, **Malaysia's current account surplus widened again for the first time in a year, to RM9.5bn in 1Q20 (4Q19: RM7.5bn), underpinned by continuous albeit smaller surplus in the goods account (RM28.9bn vs RM32.3bn) and smaller deficit in the primary income account (-RM6.0bn)** as foreign companies operating in Malaysia were earning less. **This offset a bigger deficit in the services account (RM8.0bn vs RM4.0bn) as the outbreak of the Covid-19 virus dented tourism receipts,** which came in at its lowest since 3Q03 (during SARS epidemic) at RM2.1bn. On a separate note, **the financial account continued to see net outflow for the 7th consecutive quarter.** Outflows jumped to RM13.3bn in 1Q20 (4Q19: RM0.1bn outflow) on the back of a **hefty outflows seen in portfolio investment** amounted to RM41.3bn during the quarter under review (4Q19: -RM1.3bn) amid redemption and selling by foreign investors during the reporting period.

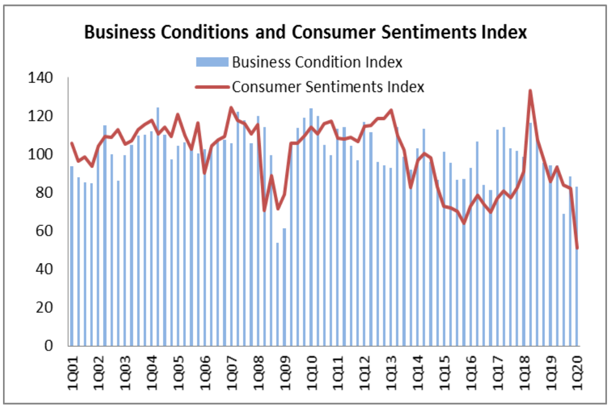
Tweaking full year 2020 growth forecast to -4.3%, first recession since the Global Financial Crisis

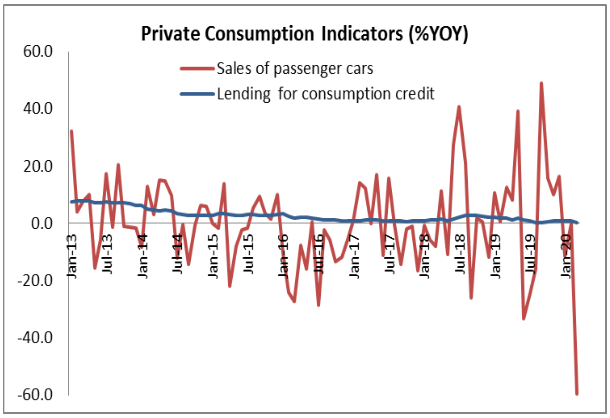
The macro landscape has become increasingly challenging amid protracted uncertainties surrounding the Covid-19 pandemic. Recent plunge in global crude oil prices as well as demand and supply disruption globally are expected to exacerbate the downside risks to domestic growth prospects, which are expected to hinge heavily on the containment of the pandemic, effectiveness of the recently introduced fiscal and monetary stimulus and how the world rides out of a global recession. Pessimism among the local business communities and consumers are expected to dampen investment and consumption activities, though some reliefs and supports are expected out of the PRIHATIN stimulus package. Against such an uncertain and unprecedented backdrop which requires reforms and new normal from all fronts, we believe Malaysia would not be able to spare itself from slipping into a recession this year. **We are projecting a 4.3% YOY contraction in the Malaysian economy for 2020,** expecting the sharp contraction in economic activities amid the MCO/ CMCO in 2Q to recover gradually towards the end of the year. **While there is still policy space to further support economic growth, we are of the view that BNM may opt to pause** to assess the effectiveness of monetary and fiscal easing measures kickstarted todate, barring any escalation of downside growth risks.

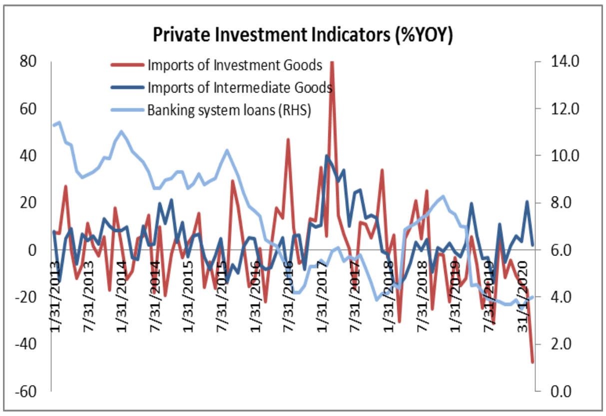

Trade Performance (%YOY)
Trade Balance RMbn (LHS)
Exports (RHS)
Imports (RHS)


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


Domestic vs Export Growth
Domestic Demand (%YOY)
Net Exports (%YOY)


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


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


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

Hong Leong Bank Berhad
Fixed Income & Economic Research, Global Markets
Level 8, Hong Leong Tower
6, Jalan Damanlela
Bukit Damansara
50490 Kuala Lumpur
Tel: 603-2081 1221
Fax: 603-2081 8936
Email: HLMarkets@hlbb.hongleong.com.my