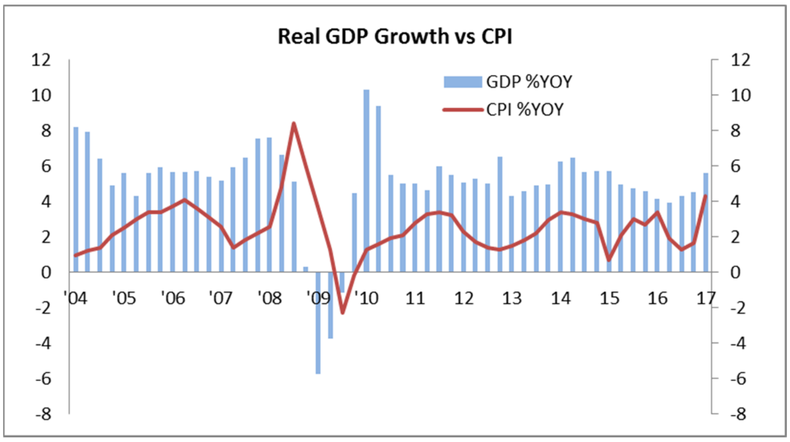
Surprisingly strong 1Q GDP

The Malaysian economy grew at a surprisingly strong pace of 5.6% YOY in 1Q17, marking its best growth in two years led by an impressive pick-up in domestic demand which more than offset the drag from net exports. The upbeat 1Q GDP print reinforced expectations for better growth outlook this year. We are revising our full year forecast up by 0.3ppt to 4.7% to take into account the sharply higher growth in the first quarter. We do not expect growth to pick up significantly from here as the global environment remains fluid plagued by potential policy shifts and geopolitical uncertainties that will have far-reaching implications on the world economy and financial markets. Domestically, continuous adjustments to higher costs of living will continue to pose challenges to consumers although pick-up in investment could help fill some of the slacks. No change to our view that modestly higher growth outlook in 2017 and transitory inflationary pressure shall support the case for OPR to stay unchanged this year.

Real GDP growth surprised on the upside at 5.6% YOY, its best in two years

The Malaysian economy surprised on the upside with a 5.6% YOY growth in 1Q17. This marked a 3rd consecutive quarter of acceleration, from +4.5% YOY in 4Q16 and its fastest in two years. **A sharp pick-up in domestic demand led by private consumption was the main catalyst pushing up growth during the quarter, offsetting the drag from net exports.** Domestic demand growth more than doubled to 7.7% YOY in 1Q17, bouncing back significantly from preceding quarter's seven-year low growth of 3.2% YOY. As we have cautioned earlier in our commentary on exports, net exports turned negative again as robust exports growth was offset by even quicker gain in imports. On a seasonally adjusted QOQ basis, real GDP increased at a faster pace of 1.8% in 1Q (4Q: +1.3%).

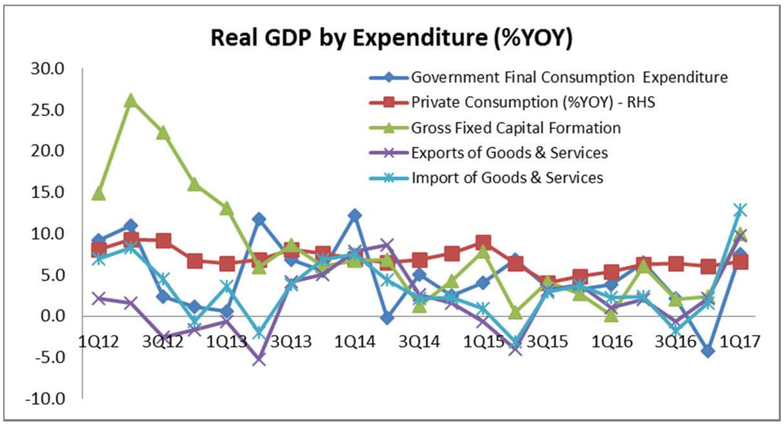


The sharp rebound in domestic demand offered some reprieves…private activities picked up and the public sector turned around

Domestic demand which accelerated for the first time in three quarters offered some reprieves. The recovery was broad-based with the private sector firmly in the driving seat and further support from the public sector. **Private consumption expanded at a faster pace of 6.6% YOY in 1Q** (4Q: +6.1%), supported by employment and wage growth as well as higher government cash assistance. **Private investment also gained traction**, rising at double-digit pace of 12.9% YOY in 1Q17 (4Q: +4.9%) driven by continued investment in the manufacturing and services sectors.

…net exports turned negative again

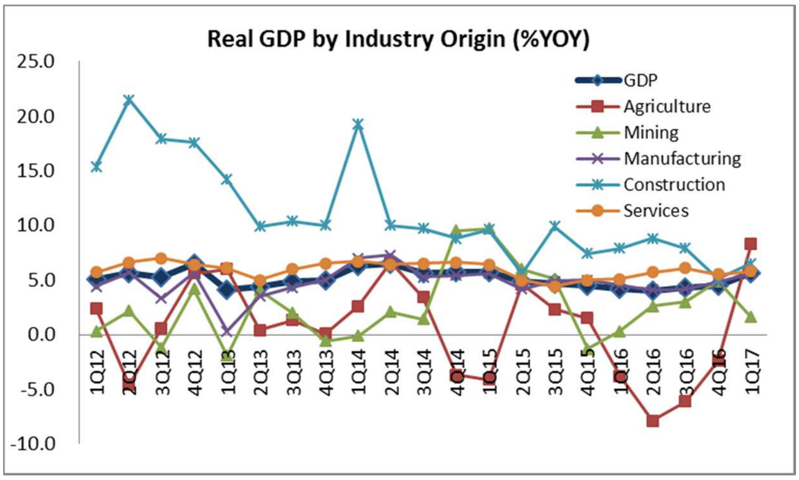
Public sector expenditure also showed better performance with turnarounds seen in government consumption (+7.5% vs -4.2% YOY) and investment (+3.2% vs -0.4%). Aggregate investment as measured by gross fixed capital formation jumped 10.0% YOY in 1Q, its fastest pace in four years. Meanwhile, **net exports turned negative again.** Even though growth in exports of goods and services quickened to 9.8% YOY in 1Q (4Q: +2.2%), imports expanded at an even quicker pace of 12.9% YOY (4Q: +1.6%), erasing all contribution from exports.



Improvement in all sectors except mining

On the supply side, growth picked up across all sectors except the deceleration in mining. The services and manufacturing sectors remained the top two growth contributors followed by a turnaround in agriculture as CPO production recovered from the adverse effect of El Nino. Growth in the agriculture sector rebounded strongly to 8.3% YOY in 1Q (4Q: -2.4%), its best performance since 3Q11. The services sector expanded 5.8% YOY in 1Q (4Q: +5.5%), thanks to higher growth in wholesale & retail trade subsector, and finance & insurance as reflected in higher loans growth and capital market activities.

Growth in the manufacturing sector also quickened to 5.6% YOY (4Q: +4.7%), driven mainly by the E&E sector and supported by continued growth in domestic-oriented sectors. Civil engineering activities in the oil & gas and transportation sector spurred growth in the construction sector to 6.5% YOY in 1Q (4Q: +5.1%). The deceleration in mining sector value-added did not come as a surprise given the oil production cut beginning January in line with global effort to curb oil production.



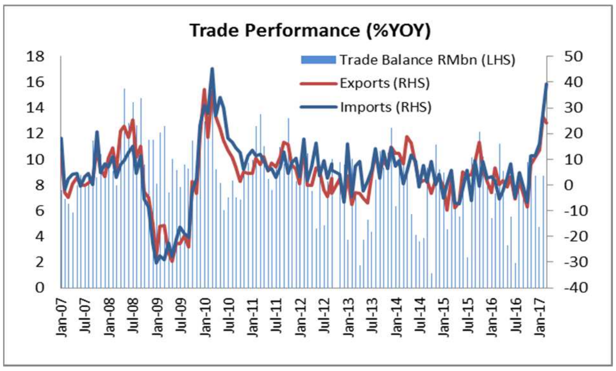
Current account surplus narrowed on smaller surplus in the goods account

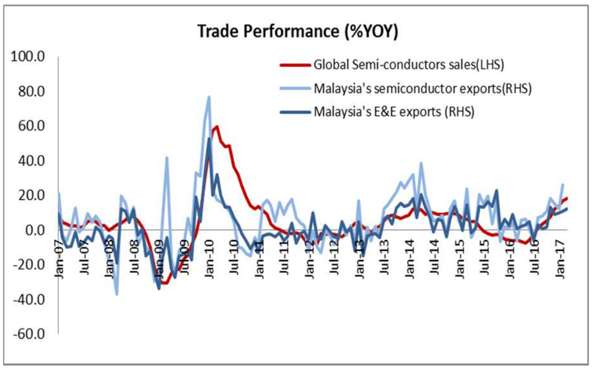
In a separate release, Malaysia's current account surplus narrowed for the first time in three quarters. **The surplus position in the current account narrowed to RM5.3bn in 1Q17,** after a hefty increase to RM12.5bn in 4Q, but still above the low of RM3.1bn seen in 2Q16. The smaller surplus was due to **lower surplus in the goods account** (RM25.3bn vs RM31.2bn) **as well as a slightly higher deficits in the services account** (-RM6.2bn vs –RM5.4bn) **and income account** (-RM13.8bn vs –RM13.3bn). **Deficit in the financial account however narrowed to RM8.8bn in 1Q (4Q: -RM14.2bn) as a result of smaller net outflow in portfolio investment** as the markets normalized from Trump aftershocks.

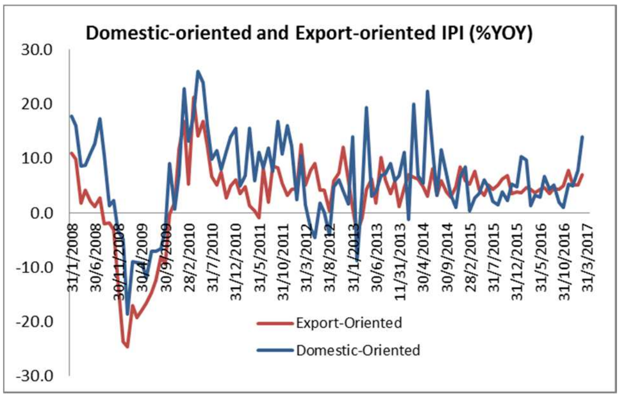
Revising full year growth forecast higher to 4.7%

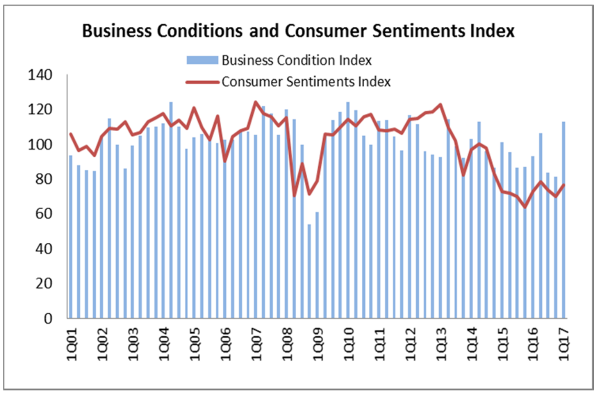
The upbeat 1Q GDP print reinforced expectations for better growth outlook this year**. We are revising our full year forecast up by 0.3ppt to 4.7% to take into account the sharply higher growth in the first quarter.** We do not expect growth to pick up significantly from here as the global environment remains fluid plagued by potential policy shifts and geopolitical uncertainties that will have far-reaching implications on the world economy and financial markets.

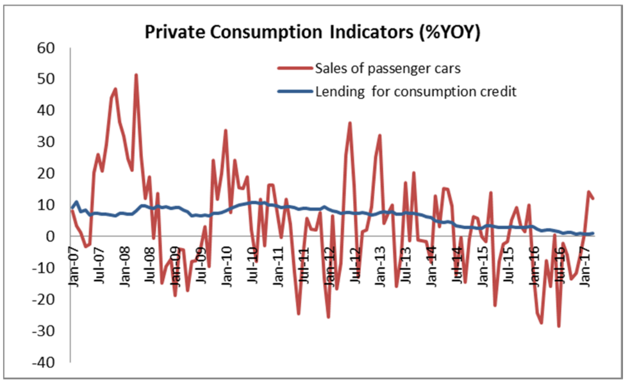
Domestically, continuous adjustments to higher costs of living will continue to pose challenges to consumers although pick-up in private investment could help fill the slack. MIER business condition index rallied above the 100-demarcation level again to 112.7, signaling renewed optimism in 1Q17, bolstering hopes for a pick-up in business activities going forward. Consumer sentiments index also rebounded to 76.6 in 1Q17 but remained subdued near record low. **In anticipation of modestly higher growth outlook in 2017 and transitory inflationary pressure, we maintain our view for OPR to stay unchanged this year.**

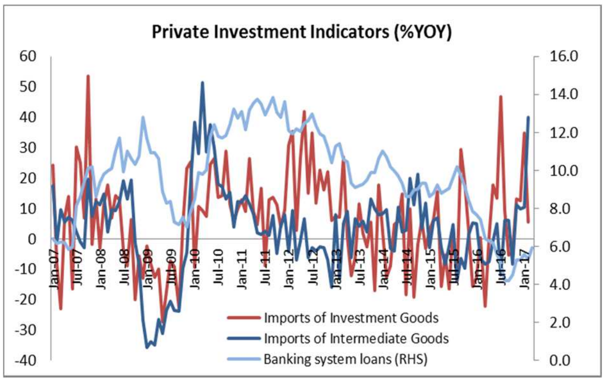

Trade Performance (%YOY)
Trade Balance RMbn (LHS)
Exports (RHS)
Imports (RHS)


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
Lending for consumption credit


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

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