

Malaysia Industrial Production

Fell 5.7% YoY in Aug, manufacturing improving

Wan Suhaimie

Economist

wansuhaimi@kenanga.com.my

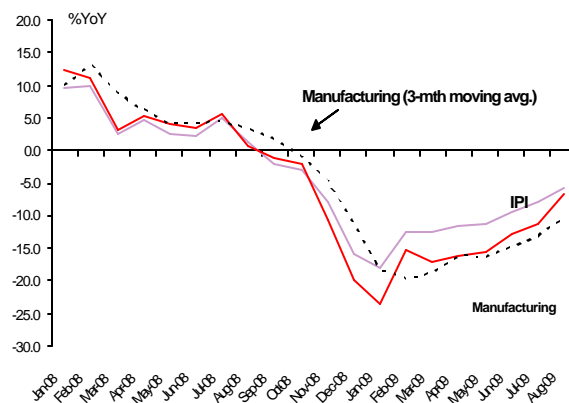
Tel: 603-2161 9657

HIGHLIGHTS

- Malaysia's **Industrial Production Index (IPI)** registered the **smallest contraction in ten months at 5.7% YoY in August on the back of continued MoM gains in manufacturing**. The contraction was within our estimate and was better than consensus' median of -6.0%.
- On MoM, however, the IPI fell 1.1% after three consecutive months of increase following sharper declines in mining output (-5.8%). **Mitigating the IPI fall was the continued monthly gains in manufacturing (+1.0% MoM)**. Coupled with the lower base effect it helped to lower IPI's YoY contraction. Sustained pick up in global semiconductor sales along with recovery in domestic demand could have support expansion in manufacturing output.
- Going forward, the lethargic growth recovery of the US economy would continue to weigh on a strong growth comeback for Malaysia in 2H09. We estimate that 3Q09 manufacturing output would decelerate to -5.8% from -10.9% in 2Q09 before projecting a rebound in 4Q09 at 3.3%. We expect the momentum would spillover well into 2010 on the back of global recovery along with support from fiscal pump priming. Hence, **we reaffirm our view that Malaysia's GDP growth is projected to stage a rebound in 2H09 (+2.3%) after declining by -5.1% in 1H09. For the whole of 2009 we maintain our GDP forecast of -1.3%. Given the uncertainty of the global economic recovery we foresee Malaysia's GDP in 2010 to grow below its potential at between 3.0% to 4.0%.**

Monthly trend taking a breather. Malaysia's industrial activity appears to take a breather in August, declining by 1.1% MoM after three straight months of steady growth. Nonetheless thanks to the base effect the **Industrial Production Index (IPI) registered the smallest contraction in ten months at 5.7% YoY in August on the back of continued MoM gains in manufacturing**. The contraction was within our estimate and was better than consensus' median (compiled by *Bloomberg*) of -6.0%. In the first eight months, however, the contraction remained large at -11.2% YoY amid sharp fall in global demand

Industrial Activity and Manufacturing On The Mend



Source: Department of Statistics, Kenanga Research

for commodities, goods and services triggered by US housing meltdown since middle of last year.

Manufacturing mitigates IPI drop. The 1.1% MoM decline in IPI after three consecutive months of increase was mainly attributed to a sharp 5.8% MoM drop in mining output. As a result, its YoY contraction accelerated to 5.8% the lowest since February this year. However, **mitigating the IPI fall was the continued monthly gains in manufacturing at 1.0% MoM, its sixth straight month of increase**. Hence, its YoY contraction decelerated to 6.6%, its lowest in ten months. Coupled with the lower base effect it helped to lower IPI's YoY contraction. Sustained pick up in global semiconductor sales along with recovery in domestic demand may have helped support expansion in manufacturing output.

... may soon take a breather. It may seem ed that the manufacturing monthly uptrend may not be sustainable following six months of uninterrupted MoM expansion. However, we expect that it may soon take a breather as it reaches year-end. Furthermore, Malaysia's lack of a more diversified manufacturing base may also render it prone to sudden pullback in global electronics and electrical (E&E) goods demand. Nonetheless, given that signs of global E&E demand may grow at a steadier pace ahead, Malaysia's manufacturing output may overcome any short-term slowdown and resume its uptrend well into 2010. The Semiconductor Industry Association projects global semiconductor sales to decline by 5.6% in 2009 before resuming growth by 7.4% in 2010.

Table 1: Malaysia Industrial Production Trend (2005=100)

	Weight	2006	2007	2008	Aug-08	Feb-09	Mar-09	Apr-09	May-09	Jun-09	Jul-09	Aug-09	Jan-Aug 08	Jan-Aug 09
IPI	% MoM				-3.7	-3.6	5.7	-0.7	1.4	0.3	7.2	-1.1		
	100.00 % YoY	4.8	2.3	0.5	1.2	-12.5	-12.7	-11.7	-11.3	-9.5	-8.4	-5.7	4.6	-11.2
	3mma				2.8	-15.5	-14.4	-12.3	-11.9	-10.9	-9.7	-7.9	5.4	-12.1
Manufacturing	% MoM				-4.0	-0.4	3.5	1.0	0.6	3.0	6.2	1.0		
	70.67 % YoY	8.9	2.2	0.6	0.6	-15.4	-17.1	-16.1	-15.6	-13.0	-12.0	-6.6	5.5	-14.8
	3mma				3.2	-19.7	-18.7	-16.2	-16.2	-14.9	-13.5	-11.2	6.7	-16.1
Mining	% MoM				-3.3	-9.9	11.0	-5.8	2.4	-5.4	-10.0	-5.8		
	23.37 % YoY	-3.8	2.2	-0.1	2.5	-7.3	-3.2	-2.9	3.0	-3.4	-1.9	-5.5	2.7	-4.3
	% MoM				-1.6	-2.8	4.1	8.8	4.0	0.2	-0.7	-0.8		
Electricity	5.96 % YoY	5.1	3.9	1.2	0.8	-5.5	-8.9	-2.9	-2.1	2.5	3.1	3.9	3.2	-2.8

Source: Dept of Statistics preliminary release, Kenanga Research, 3mma=3-month moving average %YoY growth

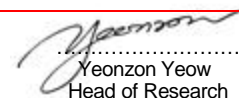
Outlook

A moderate recovery ahead. Going forward, the lethargic growth recovery of the US economy would continue to weigh on a strong growth comeback for Malaysia in 2H09. Though the US economy is stabilizing, the rising unemployment will remain a major impediment to a swift recovery. We estimate that 3Q09 manufacturing output would decelerate to -5.8% from -10.9% in 2Q09 before projecting a rebound in 4Q09 at 3.3%. We expect the momentum would spillover well into 2010 on the back of global recovery along with support from fiscal pump priming. Hence, **we reaffirm our view that Malaysia's GDP growth is projected to stage a rebound in 2H09 (+2.3%) after declining by -5.1% in 1H09. For the whole of 2009 we maintain our GDP forecast of -1.3%. Given the uncertainty of the global economic recovery we foresee Malaysia's GDP in 2010 to grow below its potential at between 3.0% to 4.0%.**

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KENANGA INVESTMENT BANK BERHAD (15678-H)
 8th Floor, Kenanga International, Jalan Sultan Ismail, 50250 Kuala Lumpur, Malaysia
 Telephone: (603) 2166 6822 Facsimile: (603) 2166 6823 Website: www.kenangaresearch.com


 Yeonzon Yeow
 Head of Research