Malaysia: Supply shock dents GDP growth in 4Q19, though demand wasn't a problem

It's not going to be too long before demand takes a hit from the rapid spread of Covid-19. We cut our 2020 growth forecast to 3.5% from 4.5%. We now see an additional 50 basis points of central bank rate cuts by mid-year. The data should also expedite rollout of the fiscal stimulus

Source: Pexels

3.6%

4Q19 GDP growth

Year-on-year

Worse than expected

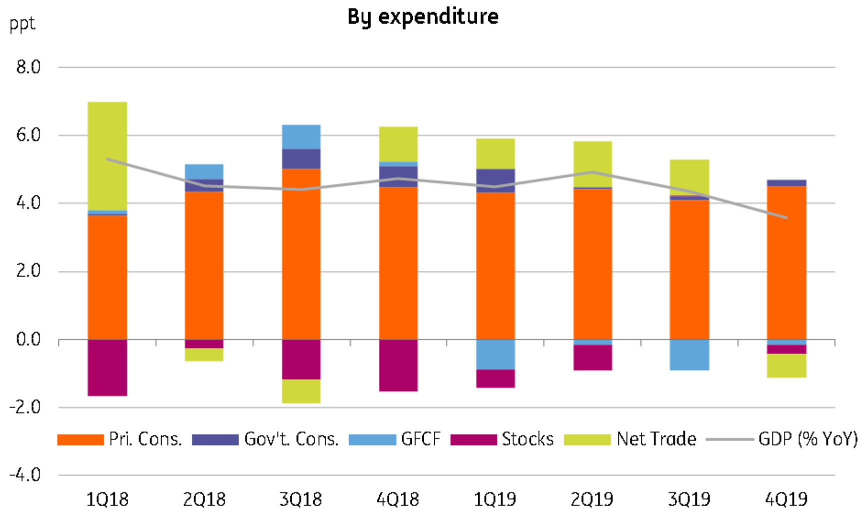
Dismal 4Q19 economic performance

In a significant downside miss, Malaysia's GDP growth slumped to 3.6% year-on-year in the final quarter of 2019, its worst performance in almost two decades (since 2Q02). The consensus median estimate was only a modest dip to 4.1% from 4.4.% in 3Q19. We were slightly optimistic with our 4.2% estimate.

The headline, however, understates the domestic economic strength which has supported the economy over the last year in the face of global trade tensions. Growth of all three expenditure-side GDP components – private consumption, government consumption and fixed capital formation - firmed up in the last quarter. Private consumption continued to lead, with a 4.5 percentage point contribution to the headline GDP growth.

Strong domestic demand coupled with accelerated export declines made net trade the main drag on GDP growth, shaving off 0.7ppt.

Sources of GDP growth - expenditure



Source: Bloomberg, CEIC, ING

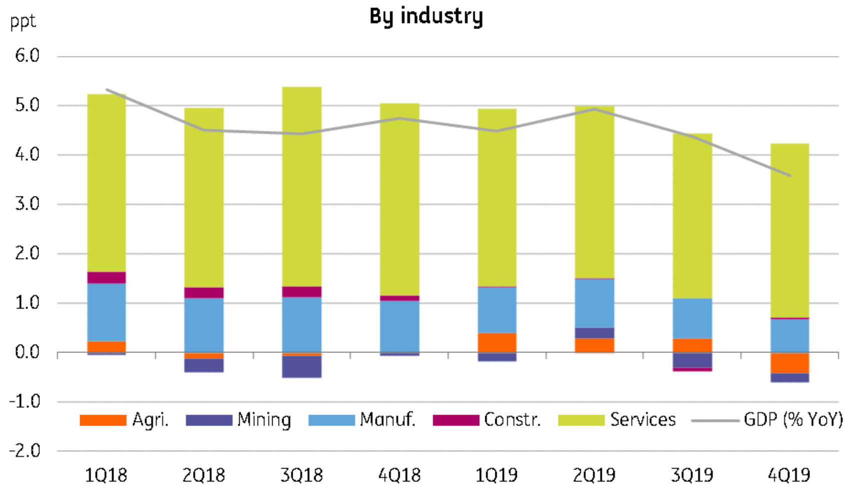
It's rather a supply shock

Bank Negara Malaysia (BNM), the central bank, attributed the sharp fourth-quarter slowdown to supply disruption to the commodity sector. This was reflected in agriculture and mining being the main industry-side sources of GDP slowdown.

> *GDP growth for 2019 would have been higher at 4.7 per cent without the supply disruptions in the commodity sector. - BNM Governor Shamsiah Mohd Yunus*

This brings full-year growth to 4.3% in 2019, shy of our 4.5% forecast for the year and down from 4.7% in 2018.

Sources of GDP growth - industry



Source: Bloomberg, CEIC, ING

Downgrade of 2020 growth outlook

It's not going to be too long before demand takes a hit from the rapid spread of Covid-19, the virus currently causing havoc worldwide. The impact will be felt in the tourism sector, while a sharp fall in global crude prices this year also bodes ill for Malaysia's commodity-driven export sector.

The way things are going, at least a couple more quarters of GDP slowdown looks more likely than not, possibly pushing growth below 3% by the second quarter of this year. Beyond that, and assuming that the virus threat ends, we are hopeful on proactive macroeconomic policies helping the recovery to above 4% GDP growth by the end of the year.

Accelerating stimulus

We believe today's bad report card on the economy will move the authorities to speed up economic stimulus measures.

Recognising the risk ahead of time, the BNM resumed its monetary easing cycle with a 25 basis point cut to the overnight policy rate to 2.75% at its most recent meeting on 22 January. Right then we added one more 25bp cut to our BNM policy forecast for this year. However, judging from the extent of the slowdown ahead, we don't think the BNM will stop at that. We now see the BNM cutting twice, by 25bp at each of its March and May meetings. This would take the OPR down to 2.25%, just shy of the 2% low reached during the global financial crisis a decade ago.

Local banks have already started offering relief for borrowers suffering from the economic impact of the epidemic. The government is also mulling a fiscal stimulus package for tourism, and now probably for the broader economy.