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MONTHLY ECONOMIC UPDATE

6 JULY 2023

ECONOMIC RESEARCH

FIRDAOS ROSLI
LEE SI XIN
RAJA ADIBAH RAJA HASNAN
NOR LYANA ZAINAL ABIDIN
KHAYRIN FARZANA FAZLI

KEY TAKEAWAYS

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- **Fed's first rate-hike pause in 15 months.** The U.S. Federal Reserve (Fed) paused its aggressive monetary tightening approach, steadying the cumulative rates at 5.00% to 5.25%, following the lowest inflation print since April 2021. The price pressure has been moderating for 11 straight months and recorded a figure of 4.0% in May amid softening global energy prices. However, the inflation figure is still double the Fed's target of 2.0%, and inflationary pressures remain high. Fed officials suggest that more hikes over the next few meetings are appropriate to achieve that goal. The Fed hinted that the rates might go up to 5.6% based on the latest Summary of Economic Projections (SEPs), should the inflation outlook worsen.

- **ECB raises rate to a 22-year high.** The European Central Bank (ECB), in a hawkish move, extended the eurozone key interest rates by 25 basis points (bps) in light of persistently high inflation (May: 6.1%) and elevated projections of core inflation. The eighth consecutive hike was announced despite the eurozone economy falling into a technical recession in 1Q2023, further stifling the region's growth prospects. ECB President Christine Lagarde believes the battle against inflation is far from over, trending above the target of 2.0% through 2025, and rates will likely increase in July.

- **Puzzling Ringgit woes – the *whys* and the *hows*.** The past month saw the local note excessively depreciating against the USD, including other currency pairs as well, with the average USD/MYR exchange rate being RM4.63 to USD (May: RM4.52). The weakening of the Ringgit rang alarm bells, and Bank Negara Malaysia (BNM)'s Financial Markets Committee reassured that they would intervene to defend the note if they view "recent movements in the ringgit exchange rate to be excessive", which it did. Mixed opinions are raised on how and when these measures would be applied, but the reasons for such performance are also important. Contrary to the historical trend whereby the Ringgit would gain from the greenback's slip, the local note failed to strengthen despite the USD index lingering around the 102.0 level, suggesting said weakening was all on the ringgit. The weakness could be attributed to, among many, the hawkish remarks from the U.S. policymakers, China's slowing economic momentum, the lack of growth catalysts and the upcoming six state elections.

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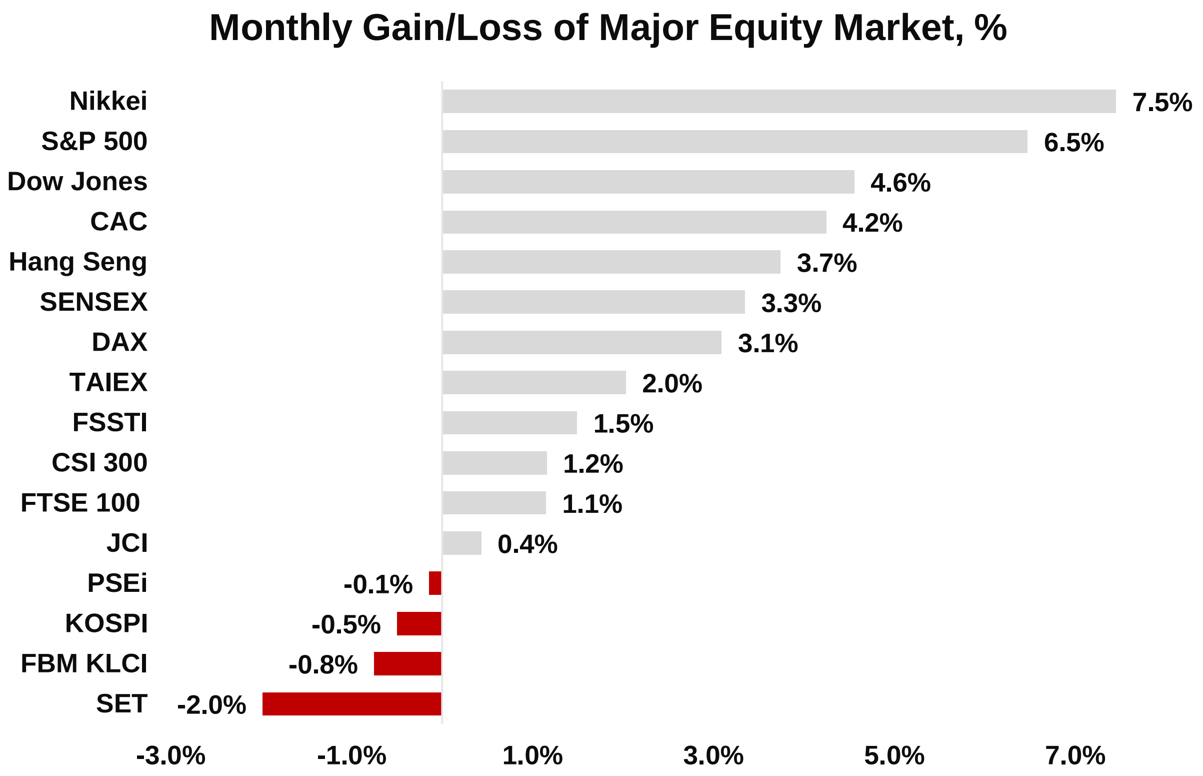
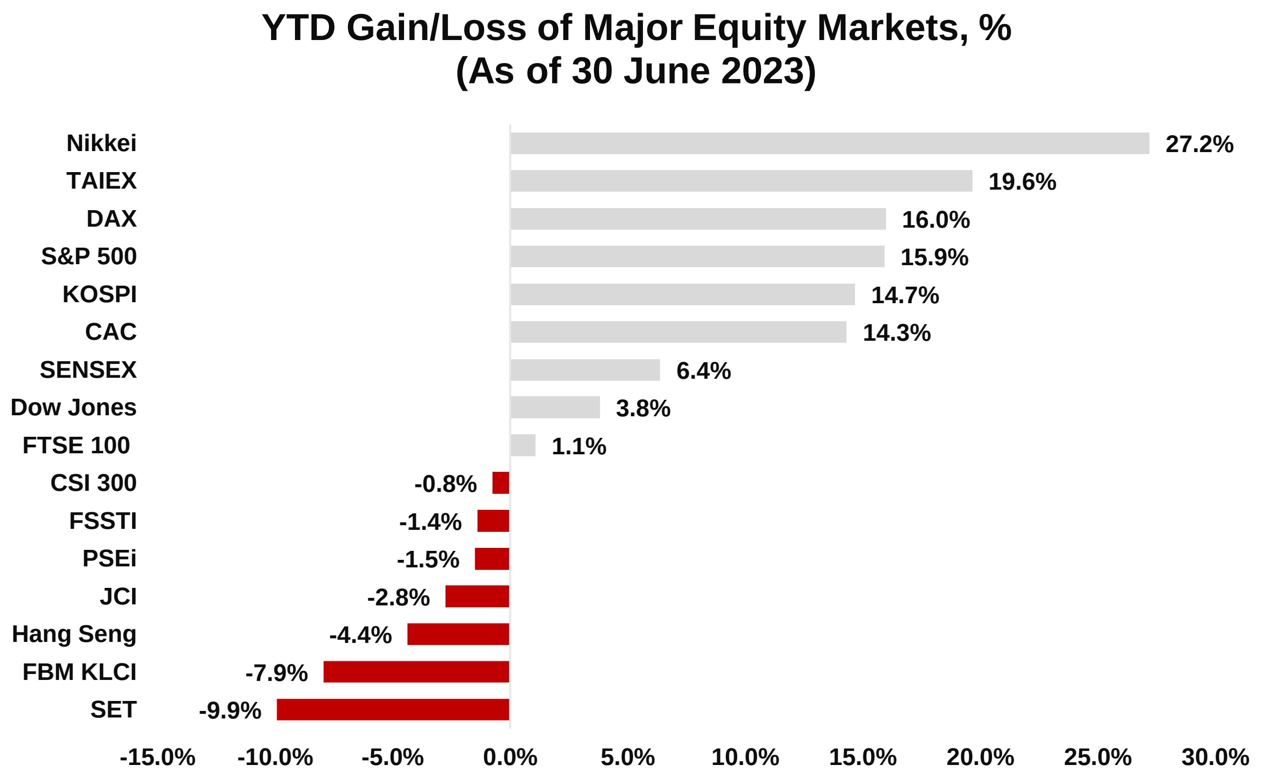
SECTION 1

Malaysia’s Financial Market

REGIONAL EQUITY: GLOBAL STOCK MARKETS CLIMBED AMID SIGNS OF COOLING FROM THE FED'S FAVOURED MEASURE OF INFLATION



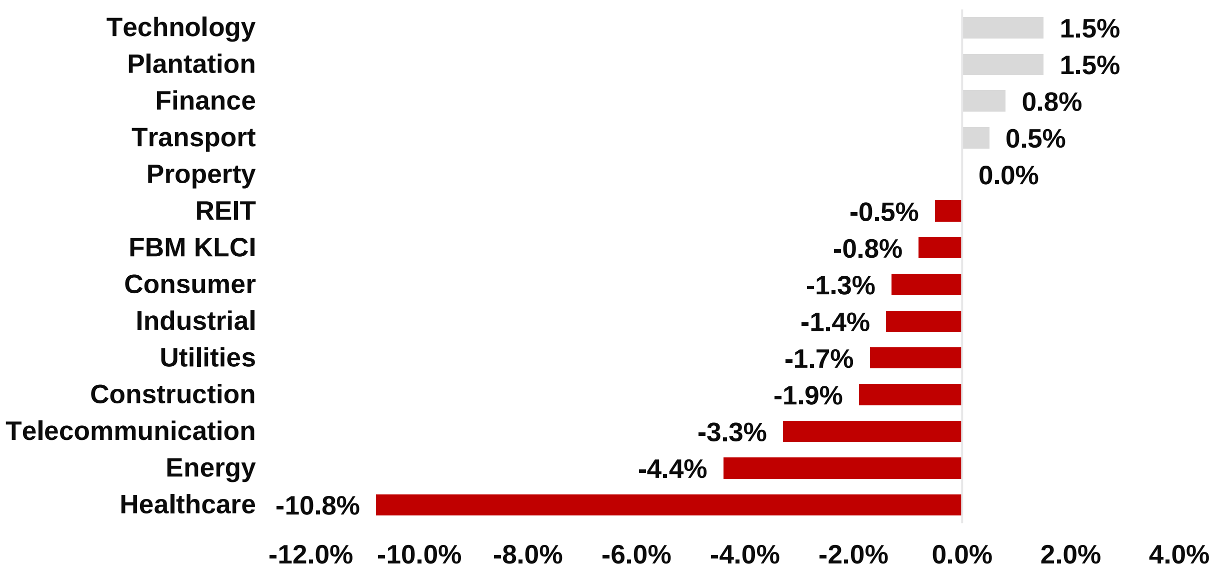


Sources: Bursa, CEIC

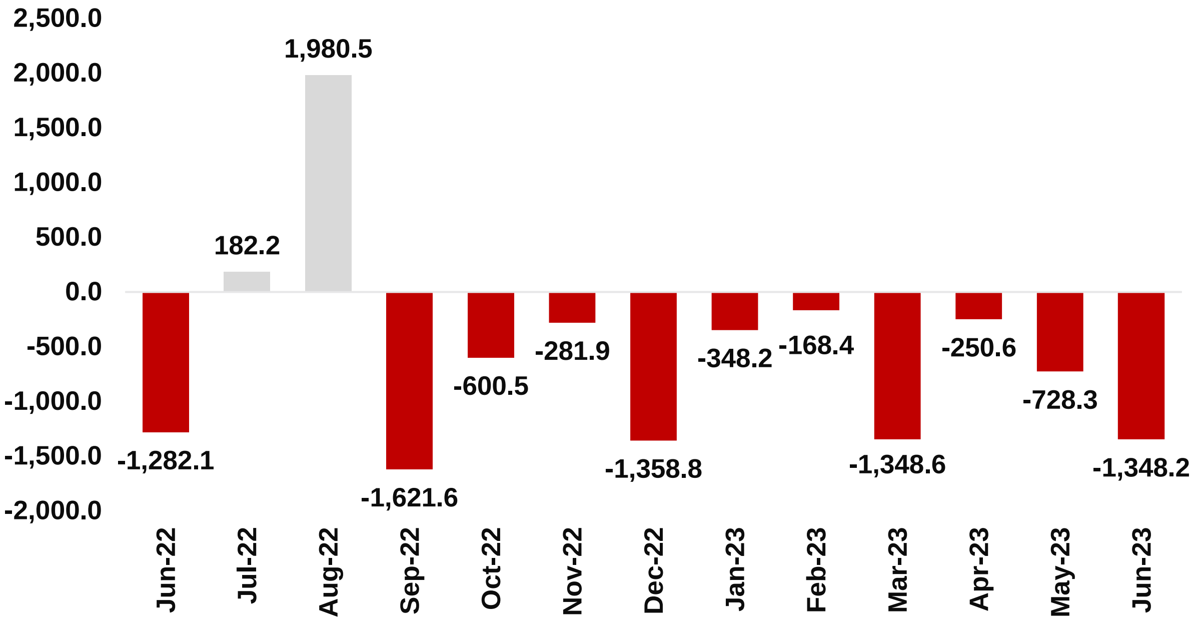
- The regional markets ended mainly positively, with Japan's Nikkei heading the gainers by 7.5% m-o-m and followed closely by the United States' S&P 500 (6.5%). On the other hand, Thailand's SET (-2.0%), Malaysia's FBM KLCI (-0.8%), Korea's KOSPI (-0.5%) and Philippines' PSEi (-0.1%) plunged into negative territory.
- Most Fed officials estimate that another two 25bp rate hikes will occur, with a remaining four more meetings this year, and inflation is not expected to fall below the central bank's 2.0% target until 2025. The Fed's preferred inflation gauge, the personal consumption expenditures (PCE) inflation, showed prices grew by 3.8% in May, down from 4.3% in April, driven by the weaker momentum in spending.
- As of 1H2023, Japan's Nikkei was the top performer, leading by 27.2% on its ultra-low interest rate policy.

DOMESTIC EQUITY: LOCAL MARKET PERSISTS IN RED AS SENTIMENTS DETERIORATE

Monthly Bursa Sectoral Performance, m-o-m%



Foreign Fund Inflow/Outflow, RM Million



Source: Bursa, BNM

- Most Bursa sectoral indices were in the red territory in June, with Healthcare (-10.8%) leading the losers by a large margin, followed by Energy (-4.4%) and Telecommunication (-3.3%).
- Wary sentiments led to the negative market movement following the weakening of the Ringgit against the greenback and uncertainties surrounding the upcoming state elections.
- On the other hand, Technology (1.5%) and Plantation (1.5%) were the top gainers during the month.
- Meanwhile, marking the tenth straight month of net foreign outflows, foreign investors sold off RM1.35 billion equities in June, with the Financial Services sector recording the highest foreign net outflow.
- We anticipate the FBM KLCI will trade cautiously until after the state elections, scheduled on 12 August 2023.

FIXED INCOME: BOND YIELDS LOOKED UP AS THE FED SIGNALLED A HAWKISH PAUSE

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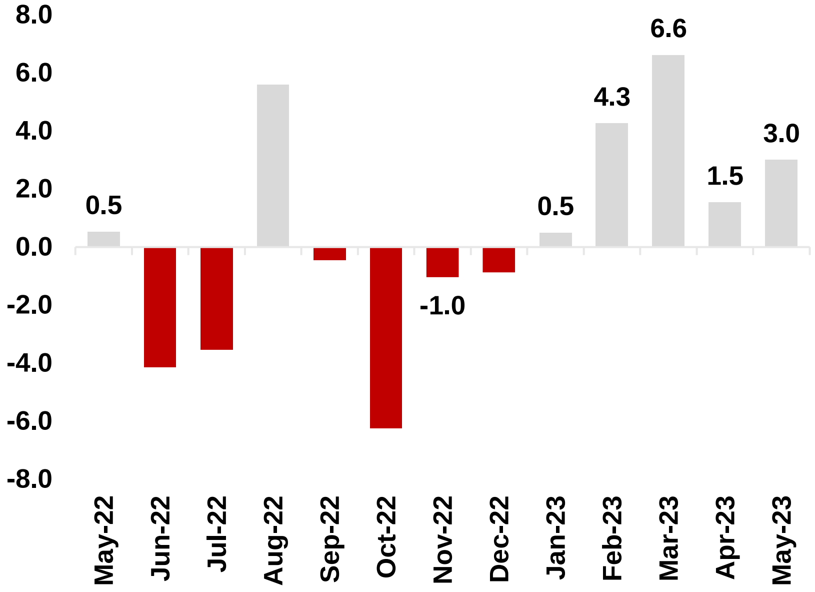
Monthly changes, basis points (bps)

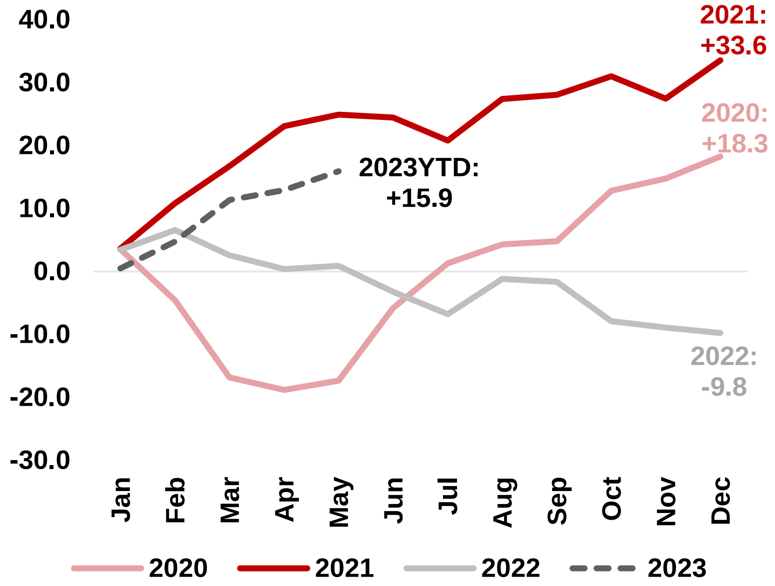
UST	Yields (%) 31-May-23	Yields (%) 30-Jun-23	Change (bps)
3-Y UST	4.04	4.49	45
5-Y UST	3.74	4.13	39
7-Y UST	3.69	3.97	28
10-Y UST	3.64	3.81	17
MGS	**Yields (%) 31-May-23**	**Yields (%) 30-Jun-23**	**Change (bps)**
3-Y MGS	3.40	3.48	9
5-Y MGS	3.46	3.61	15
7-Y MGS	3.62	3.74	12
10-Y MGS	3.71	3.84	13
GII	**Yields (%) 31-May-23**	**Yields (%) 30-Jun-23**	**Change (bps)**
3-Y GII	3.35	3.49	13
5-Y GII	3.52	3.69	17
7-Y GII	3.69	3.78	8
10-Y GII	3.81	3.88	7

Sources: BNM, Federal Reserve Board

Foreign Fund Flows in Local Bond Market, RM billion



Cumulative Net Foreign Flows in Local Bonds (Yearly comparison, RM billion)



- The U.S. Treasury (UST) yield curve bear flattened in June, with the 3y yield surging 45bps while the 10y yield climbing 17bps amid the prospect of a hawkish Fed after a pause in interest-rate hikes at the June Federal Open Market Committee (FOMC) meeting which reignited fears over the possibility of a recession.
- Local govvies also ended weaker, with the Malaysian Government Securities (MGS) yields lifted between 9bps and 15bps. Meanwhile, the Government Investment Issues (GII) yields rose between 7bps and 17bps.
- Foreign investors continued as the net buyer of local bonds for five consecutive months, with net foreign inflows of RM3.0 billion in May (Apr: RM1.5 billion). Local govvies' foreign shareholdings to total outstanding increased marginally to 22.7% in May from 22.6% in April.
- For the first five months of 2023, the cumulative net foreign inflows jumped to RM15.9 billion (Jan-May 2022: RM0.9 billion).

FX MARKET: RINGGIT ENDED LOWER IN JUNE AMID CONCERN OVER GLOBAL ECONOMIC SLOWDOWN AND DOMESTIC FACTOR

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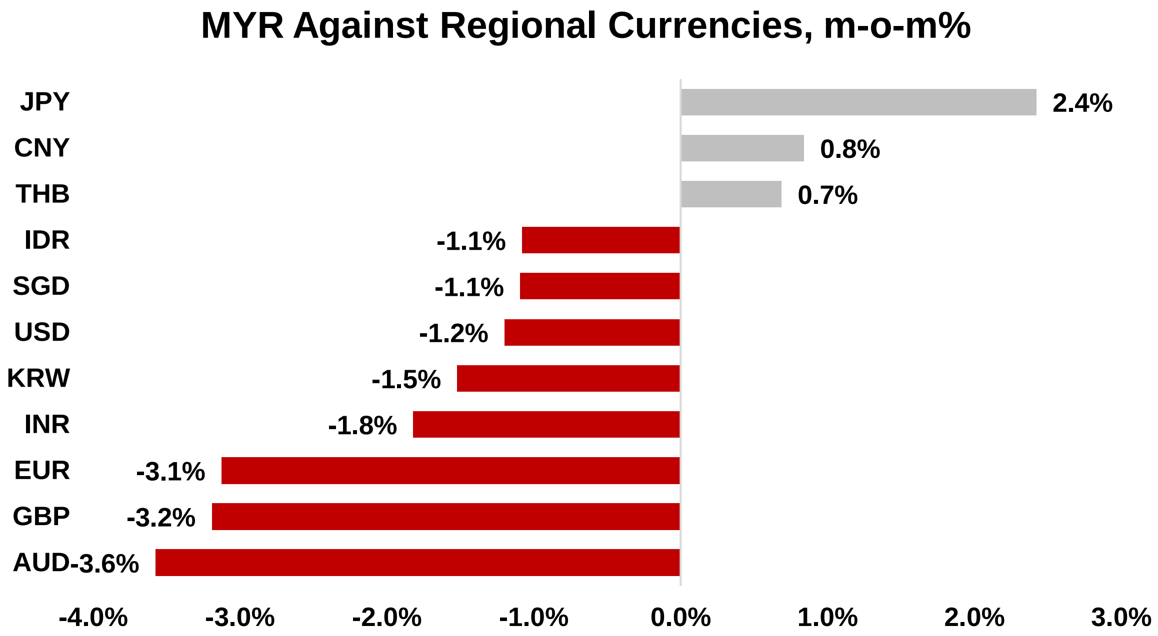

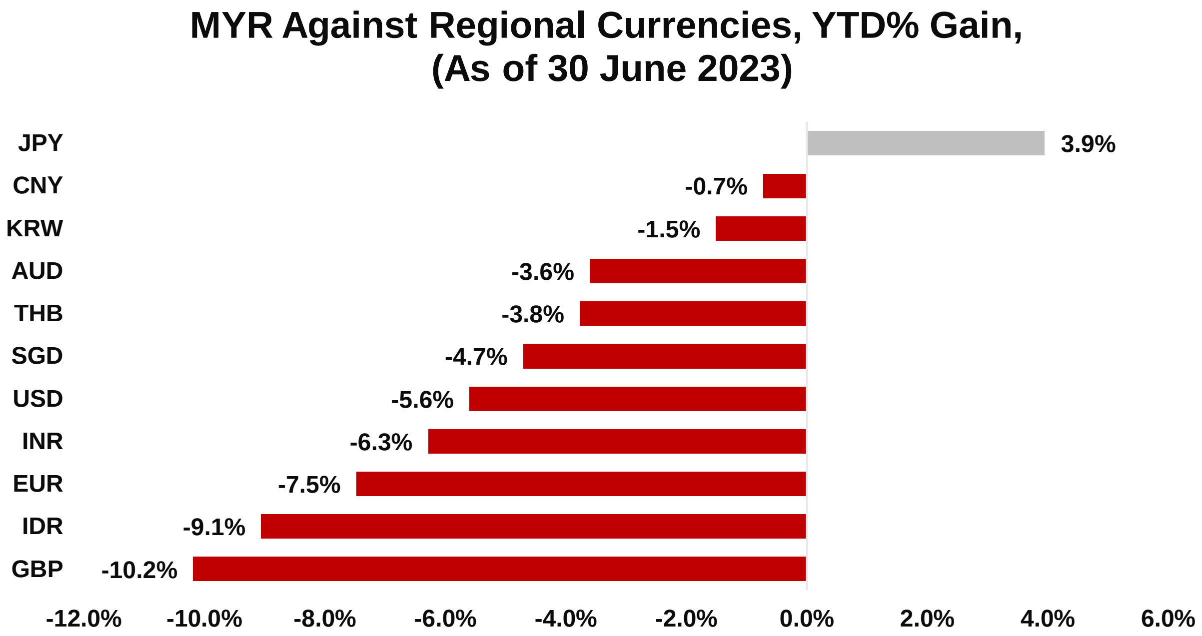

Source: Investing.com

- On a monthly basis, the Ringgit remained weak against the USD when the local note closed at RM4.6650 on 30 June from RM4.6130 in the previous month.
- The U.S. Fed decided to skip its rate hike during its June meeting, marking the first pause after a tenth straight increase in the FFR since March last year to combat the inflationary pressures. However, we noticed that such a move did not support the value of the Ringgit even though the USD index trended lower, declining by 1.3% on a monthly basis.
- We believed that the Ringgit could also have been weighed down by uneven China's post-lockdown economic recovery, which was less than impressive.
- Domestically, we posit that investors would remain cautious ahead of the highly anticipated state elections, scheduled on 12 August 2023. Thus, Ringgit might be volatile until the said polls are over.

SECTION 2

The Global Economy

OTHER CENTRAL BANKS STILL PURSUE FOR MORE RATE HIKES DESPITE A BRIEF PAUSE FROM THE U.S. FED

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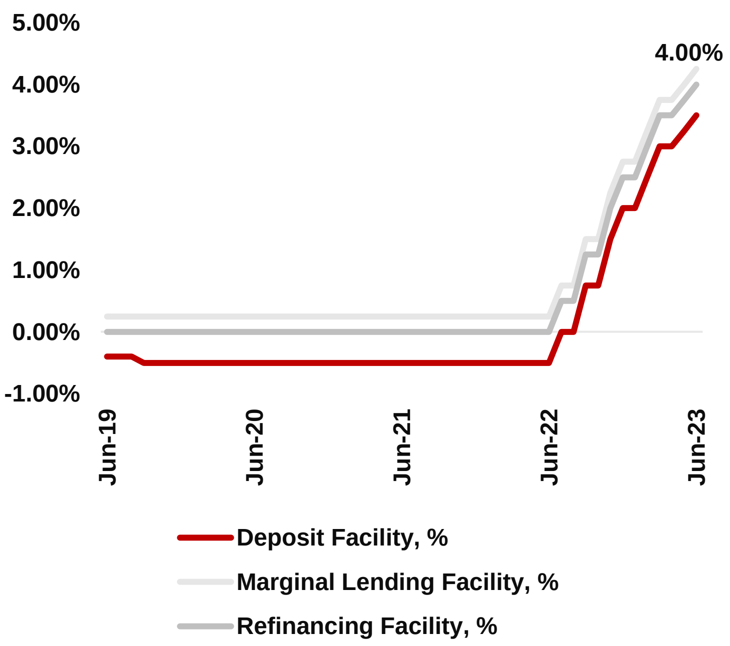
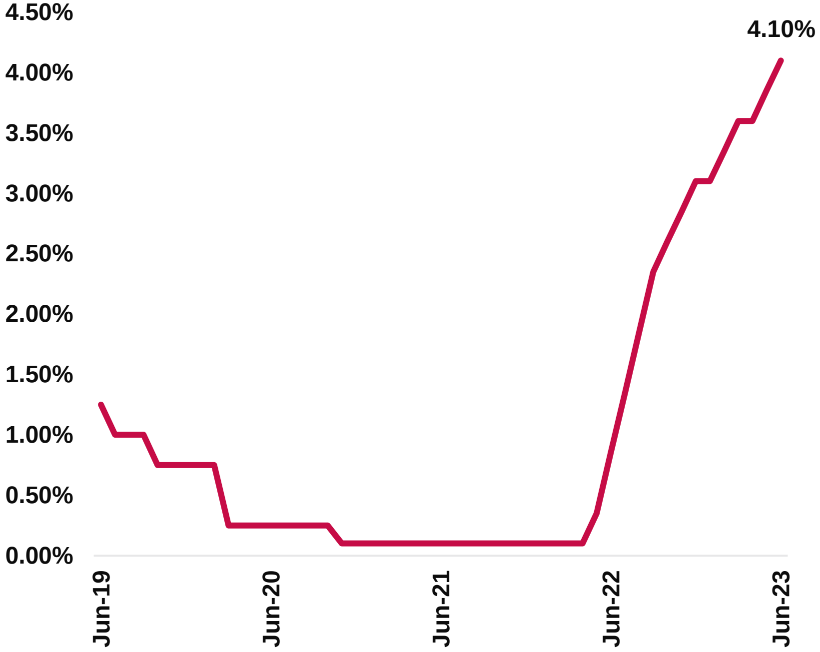
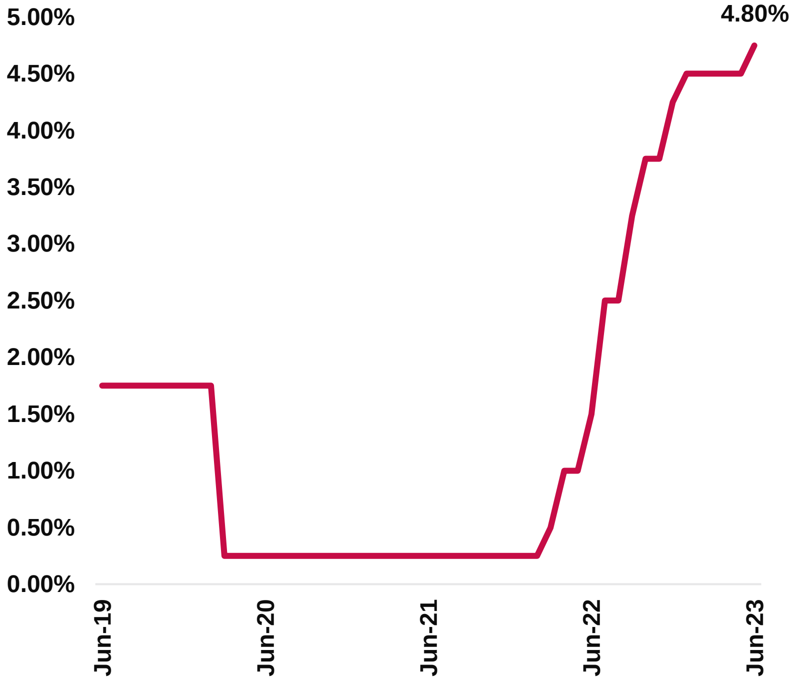
E.U.: Key Interest Rates, %



Australia: Cash Target Rate, %



Canada: Overnight Target Rate, %



Sources: European Central Bank (ECB), Bank of Canada (BoC), Reserve Bank of Australia (RBA)

- In summary, the above central banks raise interest rates in sync by 25bps to tame inflation at multi-decade highs with pressures broadening beyond food and energy prices.
- Undoubtedly, stable prices are a crucial prerequisite for sustainable economic growth. As such, central banks are geared towards normalisation to prevent inflationary pressures from spilling over.
- Though many have slowed the pace of their hikes, the fight against the price pressures is far from over, considering that the current level is still beyond the desired 2.0% target.

MEANWHILE, BOE SURPRISED THE MARKET WITH ITS HAWKISH SUPER-HIKE OF 50BPS INTEREST RATE RISE IN JUNE MEETING

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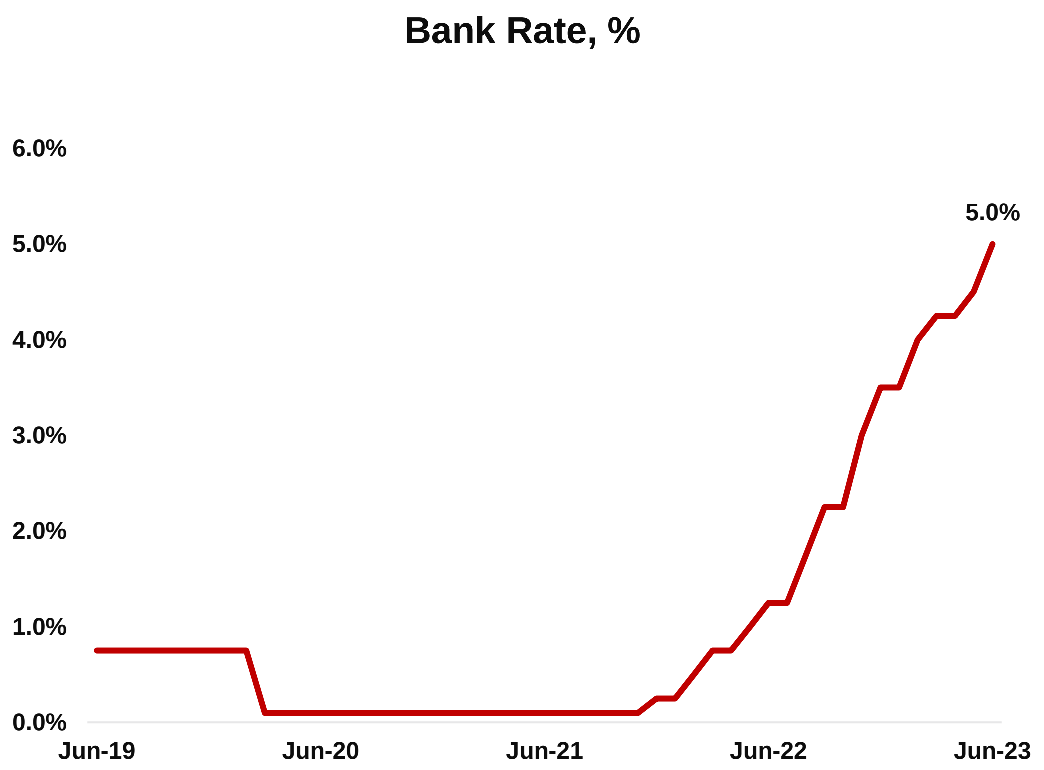
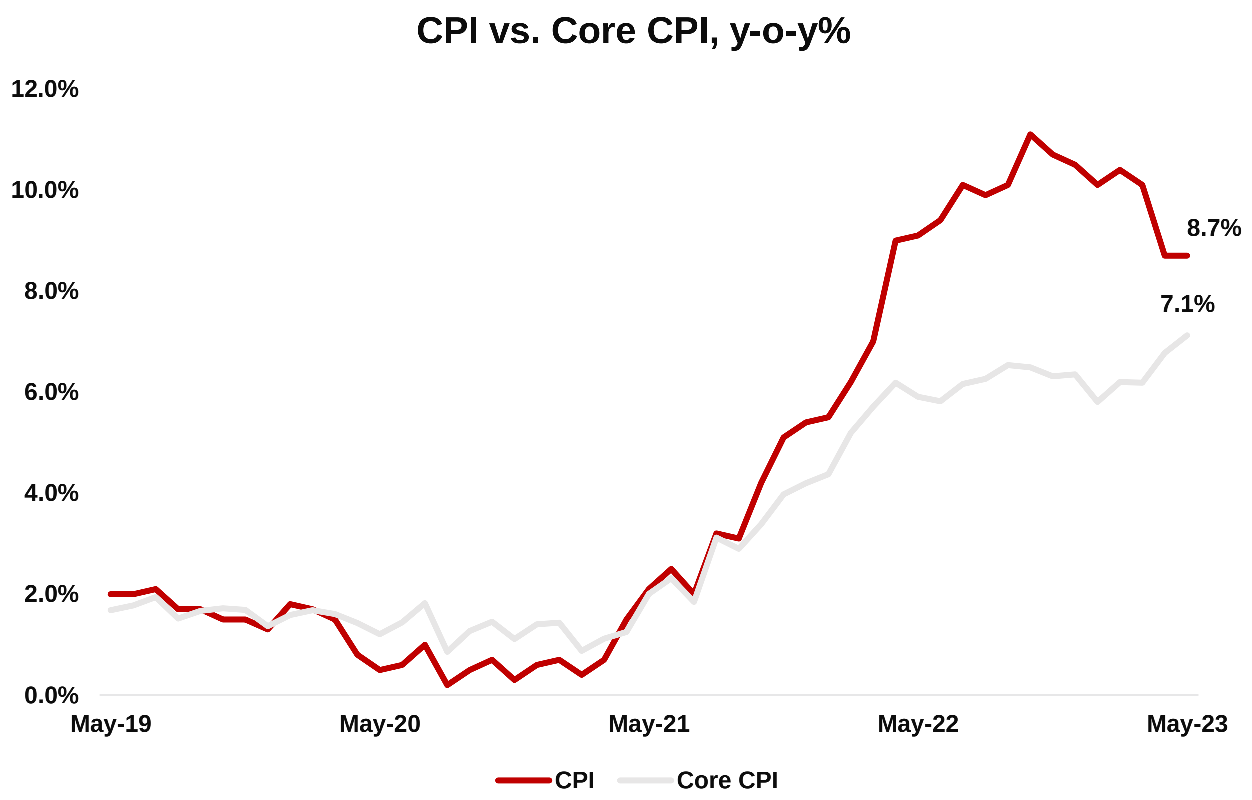


Source: Office for National Statistics (ONS)



- The central bank raised its policy interest rate to 5.0% by a majority of 7-2, pushing the borrowing costs to their highest level since 2008 as the economy grapples with persistently high inflation. The MPC's remit is clear – **inflation targets always apply**, reflecting the primacy of price stability in the U.K. monetary policy framework.
- Most worryingly, the latest print showed that core CPI accelerated to 7.1%, the highest level since March 1992 after rising by 6.8% in the previous month, perhaps, implying a sense of urgency of the majority voting among the MPC members.

CHINA'S POST-LOCKDOWN RECOVERY FACES A BUMPY ROAD AHEAD

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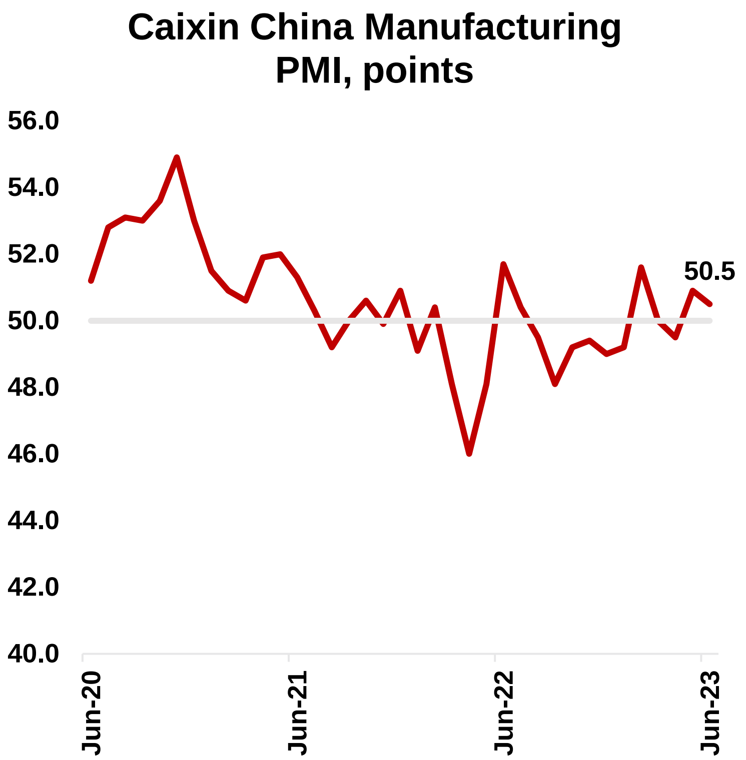

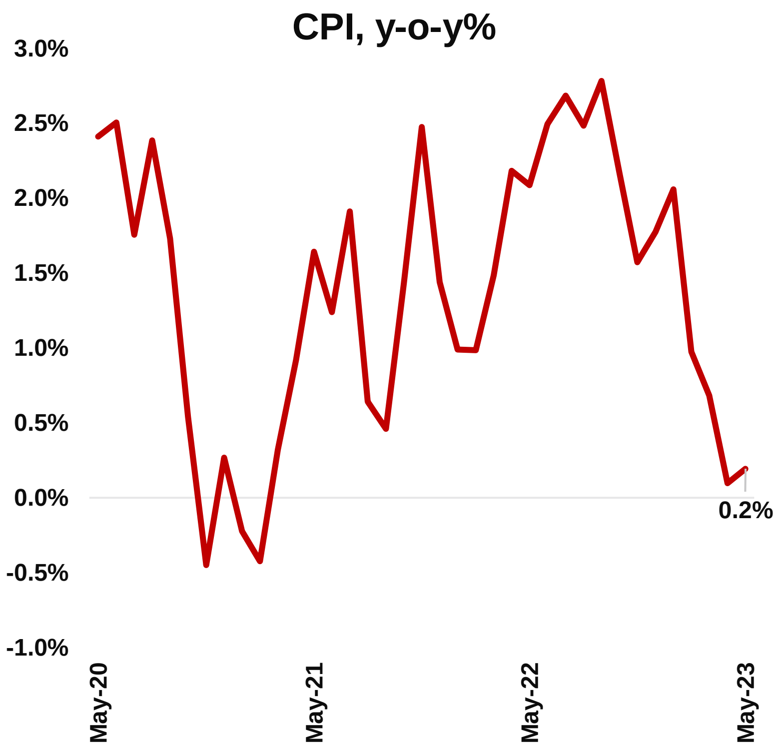

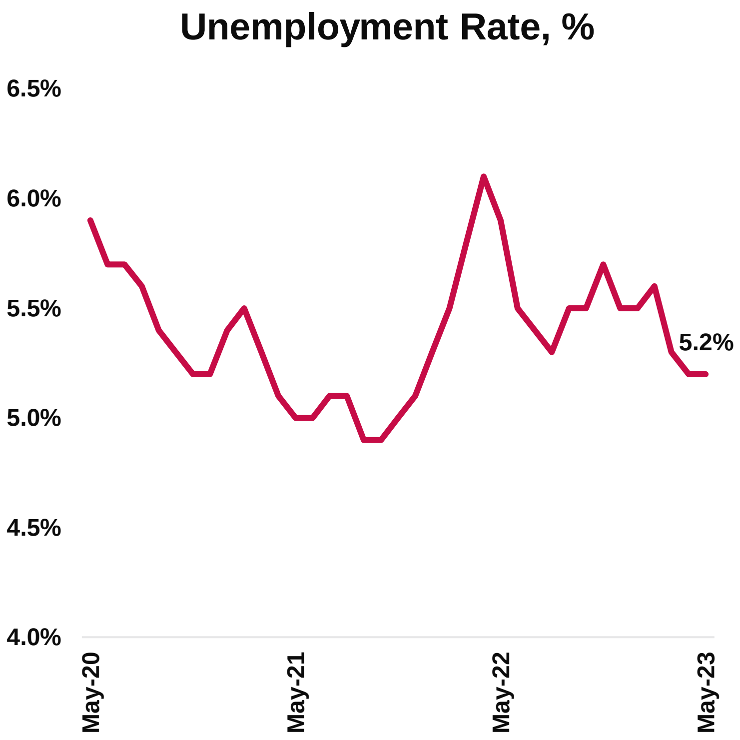

Sources: S&P Global, IMF, National Bureau of Statistics

- China's factory activity eased to 50.5 points in June from 50.9 points in the previous month, showing that the world's second-largest economy is struggling to sustain its post-lockdown recovery seen earlier this year following an entrenched property down, high unemployment rate, specifically on the still double-digit youth unemployment rate, (May: 20.8% vs. April: 20.4%) as well as deflationary pressures.
- Consumer prices increased at the slowest pace in two years, suggesting weak consumer demand, which raised questions over the strength of the country's economic rebound.
- For now, the market anticipated more policy support to bolster the stuttering economic recovery. However, the central bank cut its key lending benchmark rates in June to shore up economic activity.

THE JAPANESE YEN (JPY) PLUNGED AGAINST USD TO ITS LOWEST SINCE 1998

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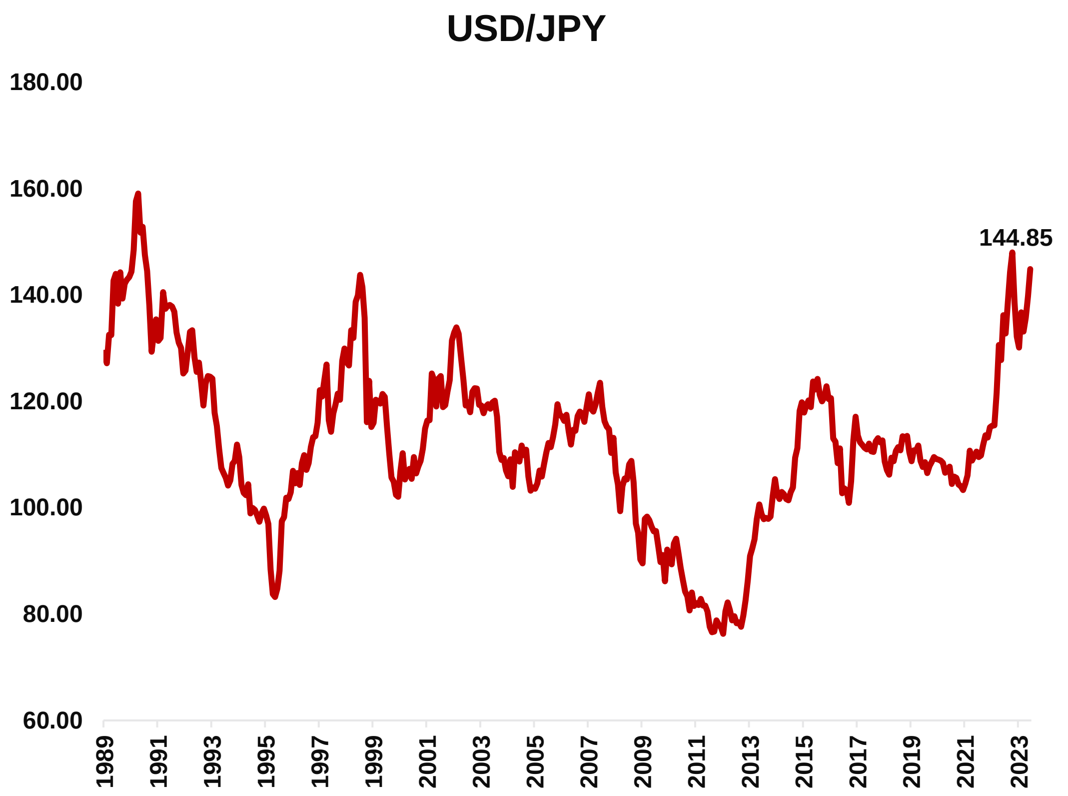
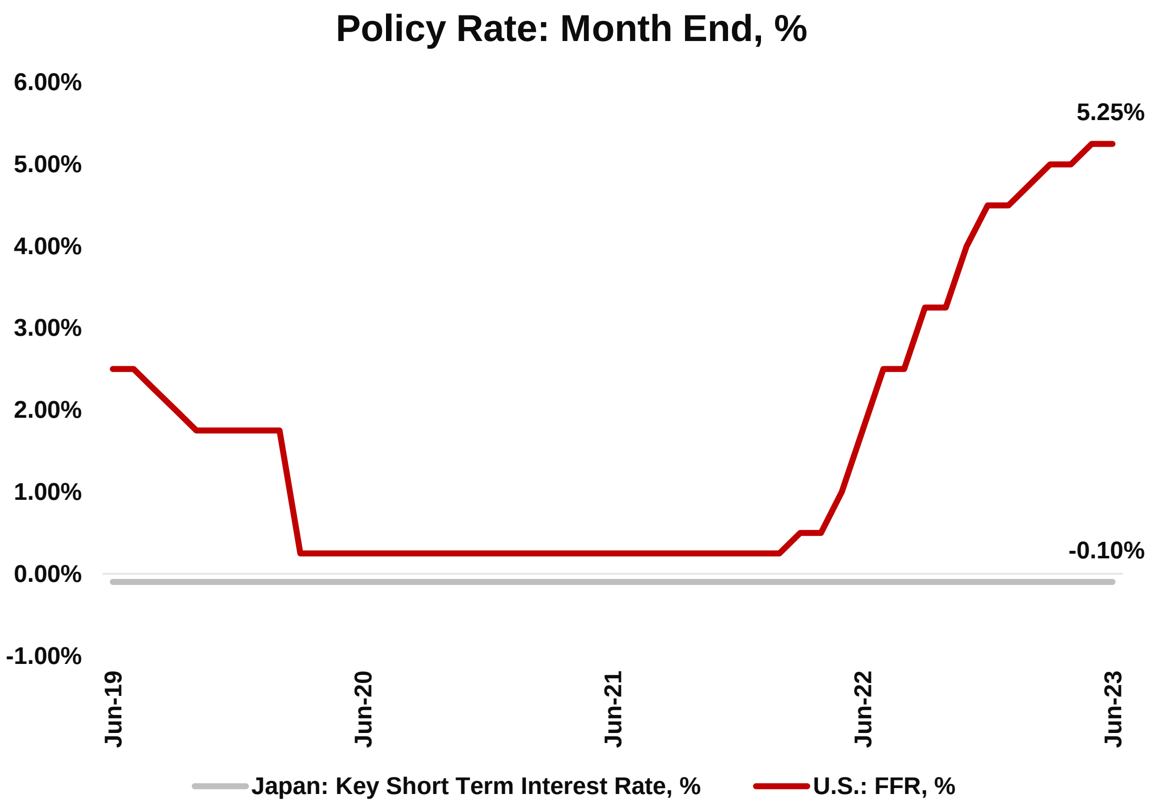




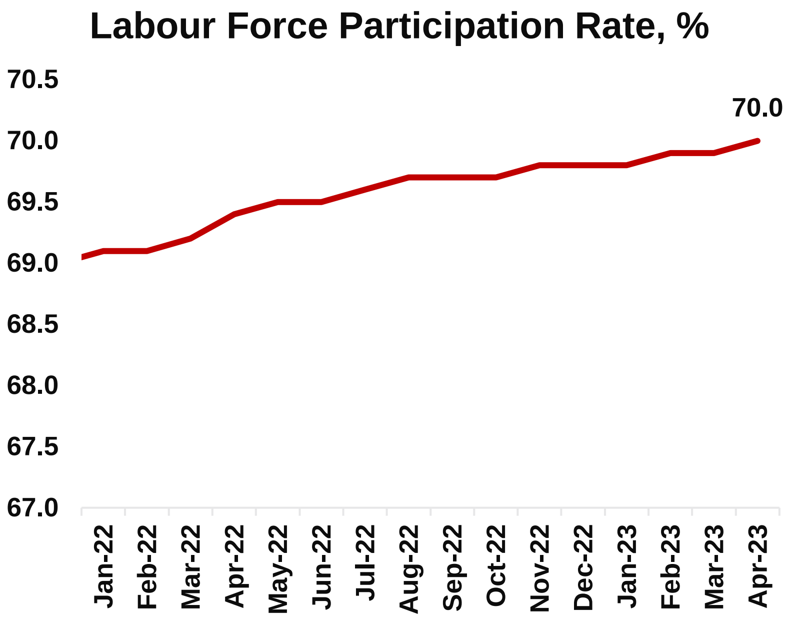
Sources: Bank of Japan (BoJ), Federal Reserve Board, CEIC

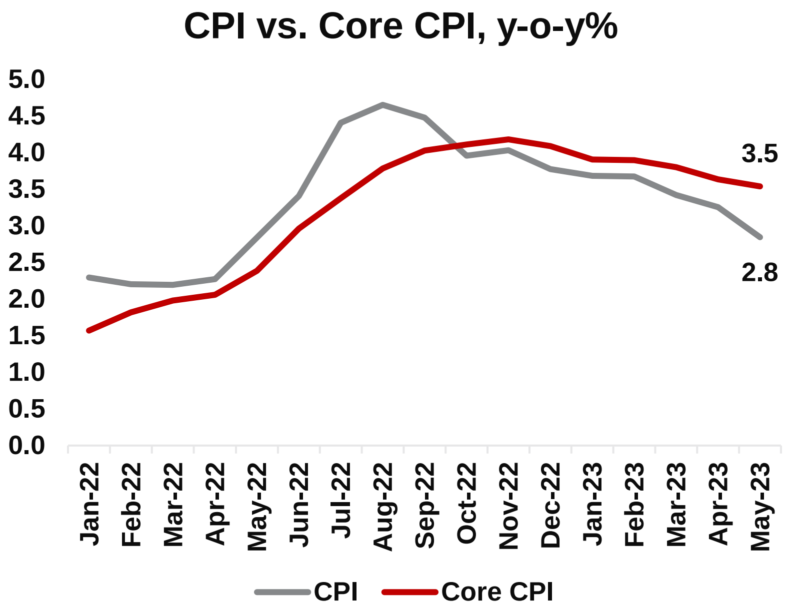
- The yen weakened to 145.00 per USD for the first time since November last year, closing to a level where the central bank intervened to support the currency for the first time since 1998.
- The JPY has lost more than other major currencies against the greenback due to the massive gap between the U.S. interest rates and ultra-low level maintained by BoJ which caused the country’s currency to fall from around 130.00 per USD since the beginning of the year.
- While a weak JPY is welcomed for boosting exports, further decline is bad for the economy which could derail its recovery from the pandemic.

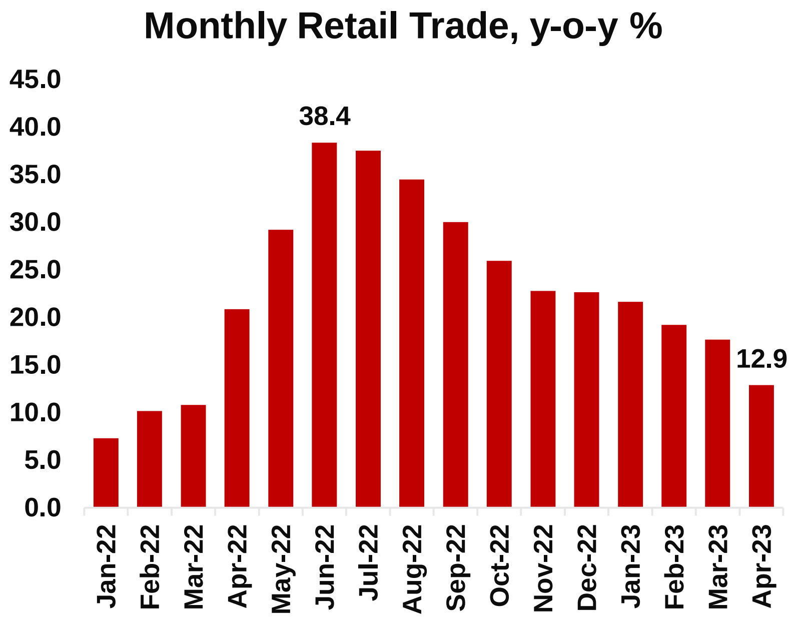
SECTION 3

Domestic Landscape & Banking Sector Update

RESILIENT LABOUR MARKET AND EASING INFLATION LENDS A HAND TO RETAIL TRADE EXPANSION







Sources: DOSM, CEIC

- Malaysia's unemployment rate remained flat for three consecutive months, clocking in at 3.5% in April. Nonetheless, labour market conditions continued to improve, with labour force participation hitting a historic high of 70.0% in April (March: 69.9%).
- The Consumer Price Index (CPI) eased to 2.8% in May (April: 3.3%), the first print below 3.0% since May 2022. However, core inflation remained sticky during the said month (May: 3.5% vs. April: 3.6%).
- Malaysia's monthly retail trade remained robust, albeit decelerating, trending within double digits of 12.9% in April (March: 17.7%), buoyed by festivities spending.
- Despite global recessionary fears brought on by global financial market volatility and domestic concerns on monetary policy outlook, the solid labour market and moderating inflation had supported the growth in private consumption.
- Moving forward, we believe the resilient domestic demand, supported by a favourable domestic landscape and a pick-up in tourism activities, should drive Malaysia's GDP growth in 2023.

HOWEVER, DOWNSIDE RISKS STEMMING FROM INTERNATIONAL TRADE REMAINS

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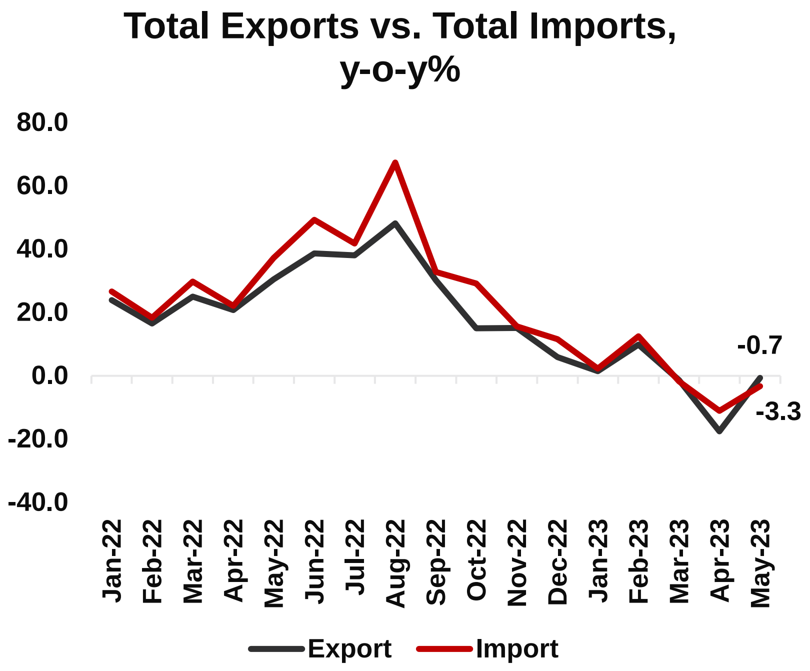

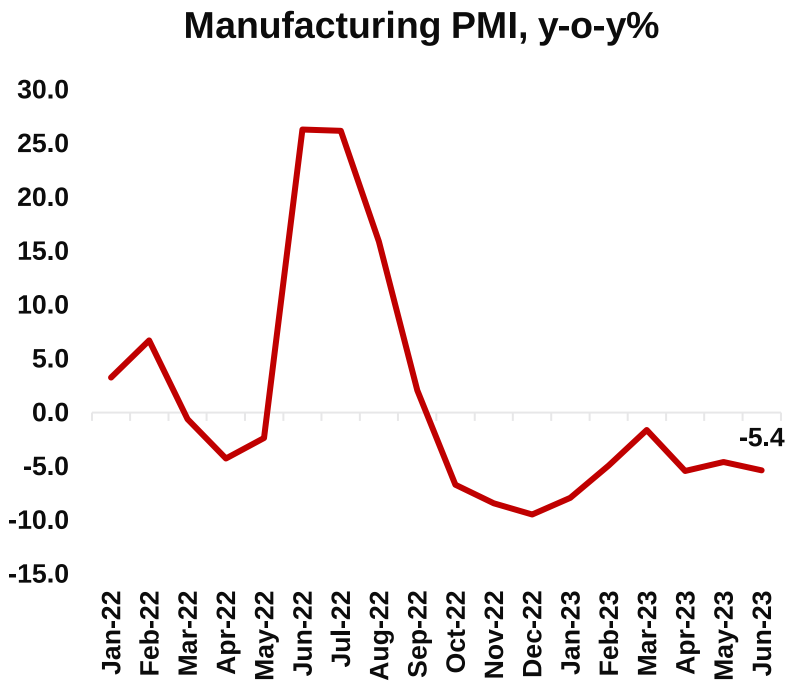

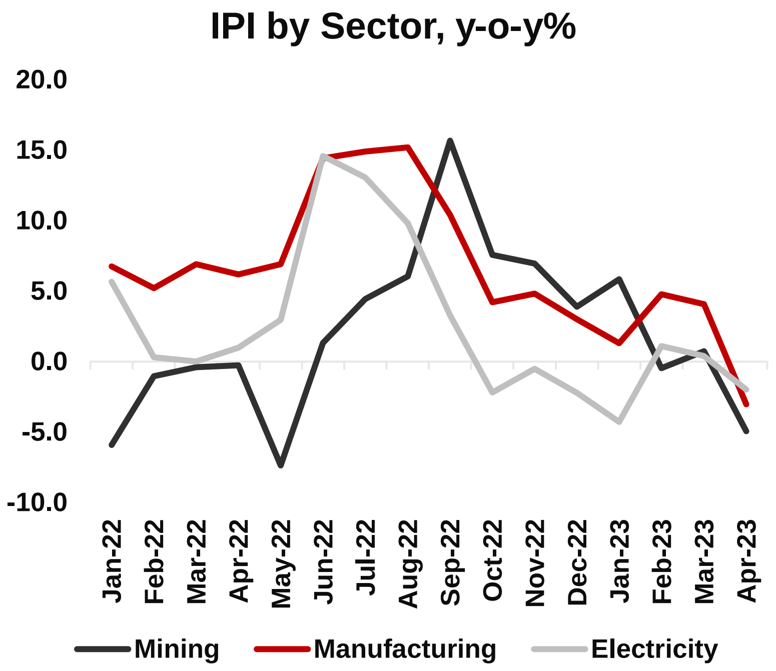

Sources: DOSM, CEIC

- Trade growth remained negative but improved in the previous month. Total exports slipped by 0.7% y-o-y (April: -17.6%), while total imports fell by 3.3% (April: -11.1%).
- Rebounds were seen in outbound shipments to major trade partners such as China (May: 1.5% vs April: -20.4%), U.S. (May: 14.9% vs April: -21.5%), Singapore (May: 6.8 vs April: -1.4) and E.U. (May: -6.1% vs April: -30.5%).
- However, the manufacturing PMI declined further by 5.4% in June (May: -5.0%), persisting at a contractionary level since October 2022 amid soft external demand, which caused firms to cut down output.
- As such, the industrial production index (IPI) plunged by 3.3% in April (March: 3.2%), recording the first decline in almost two years amid a broad-based contraction in all major sectors.

BANKING SECTOR: UPSURGED IN FINANCING GROWTH IN MAY BUOYED BY THE HOUSEHOLD AND NON-HOUSEHOLD SECTORS

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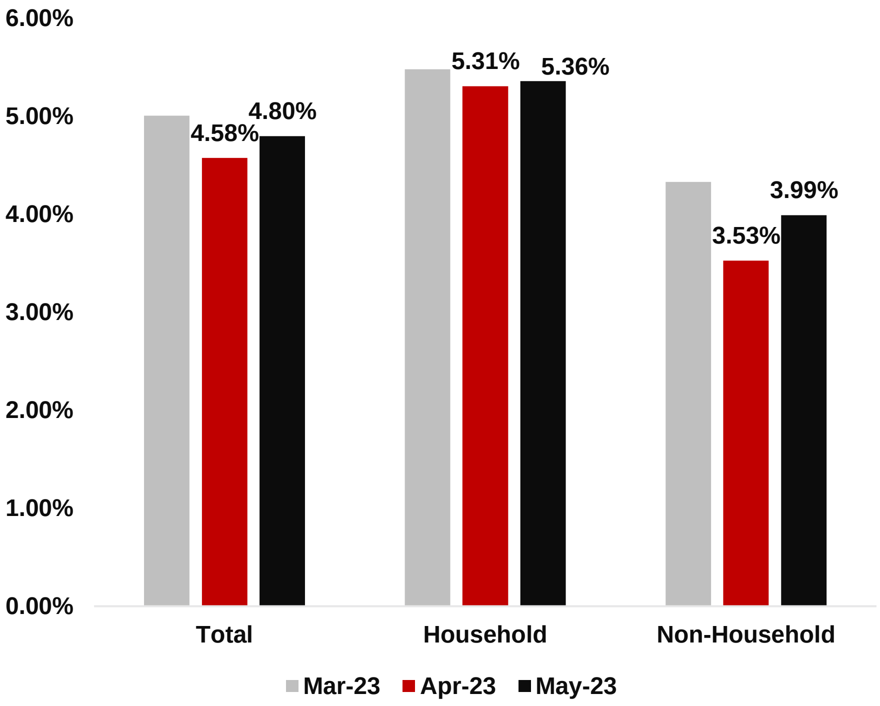
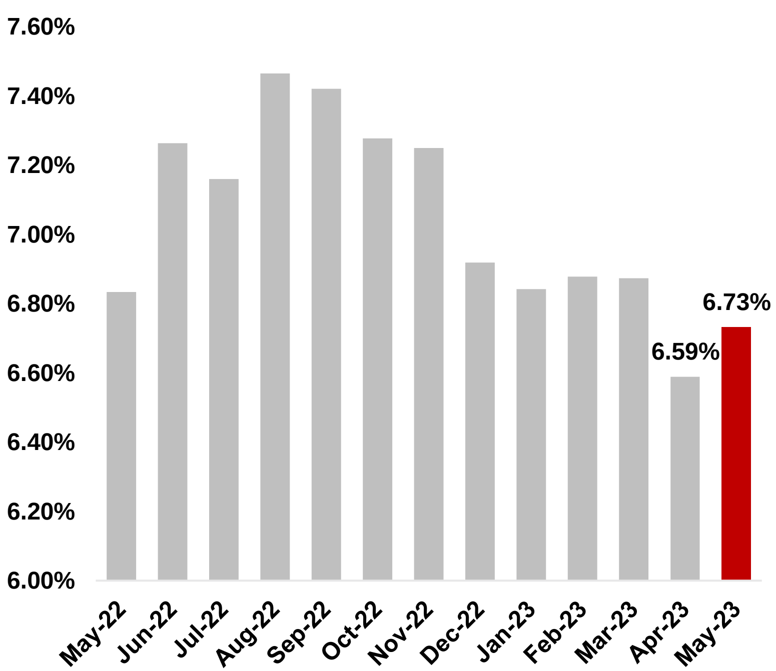
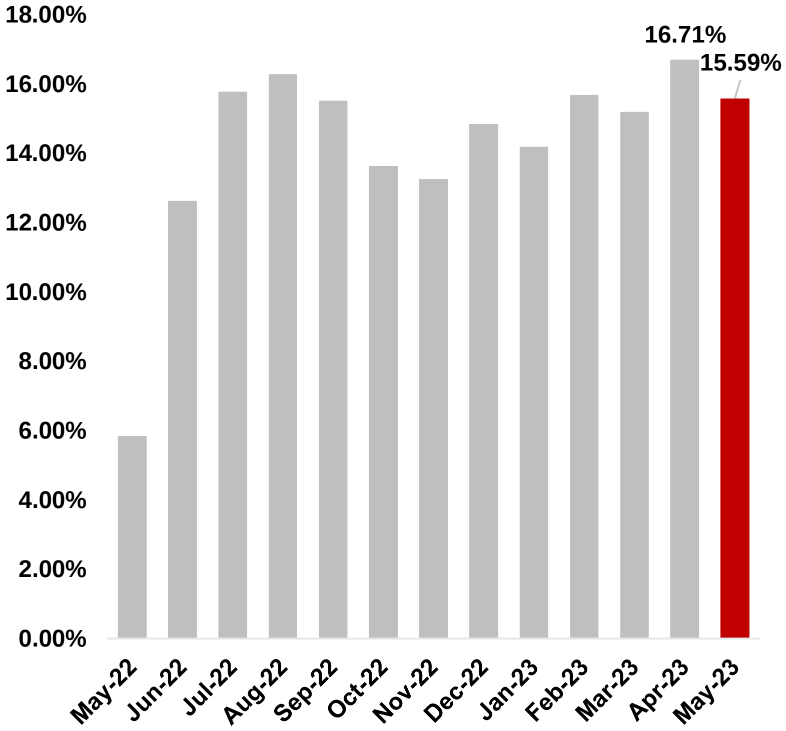


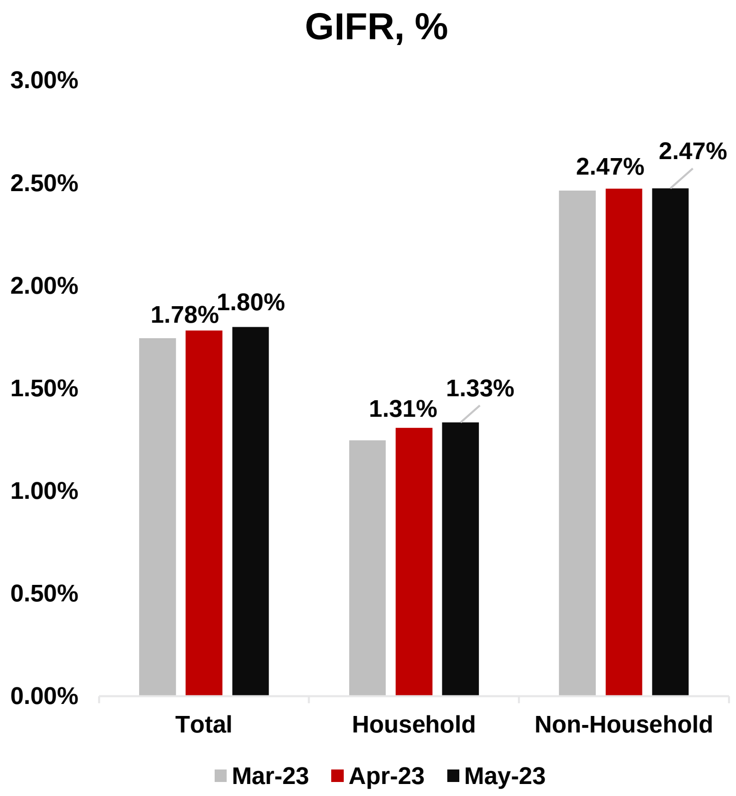


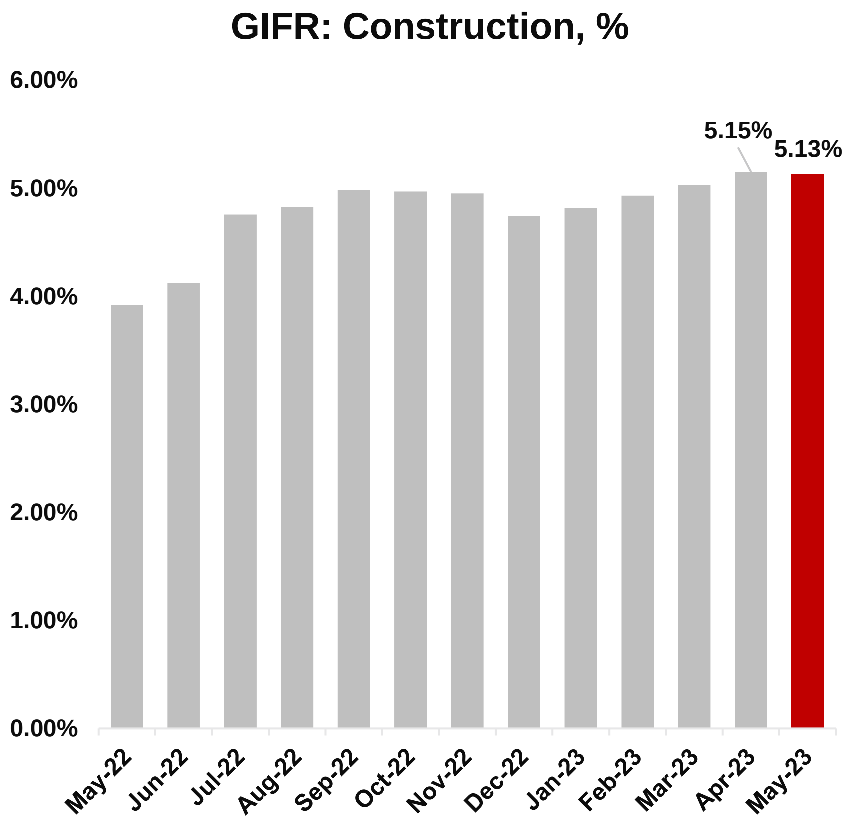


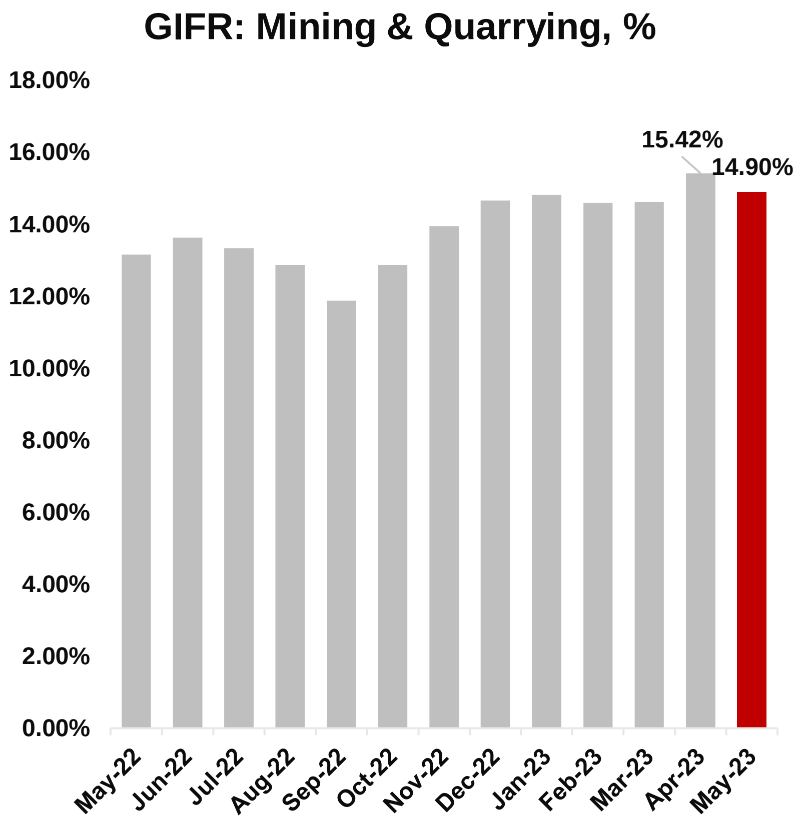
Source: BNM

- Financing growth uptrend in May, with the financing activities growing by 4.80% in May relative to 4.54% in April. The household and non-household sectors also surged in May at 5.36% (April: 5.24%) and 3.99% (April: 3.53%), respectively.
- The moves were supported by the increase in the purchase of residential property, which grew by 6.73% in May compared to 6.59% in April. Additionally, the purchase of passenger cars growth also escalated to 8.86% in May (April: 8.46%)
- Nevertheless, the financing trend in the credit card segment grew at a slower pace of 15.59% in May (April: 16.71%).

BANKING SECTOR: GIFR ESCALATED SLIGHTLY IN MAY







Source: BNM

- Total Gross Impaired Financing Ratio (GIFR) increased slightly to 1.80% in May (April: 1.78%) in tandem with higher GIFR within the Household sector which rose by 1.33% in May (April: 1.31%).
- Meanwhile, the GIFR in Non-Household sector remained stationary at 2.47% in May (April: 2.47%).
- Impairment for the Construction industry slipped marginally to 5.13% in May from 5.15% in April. In addition, the GIFR in Mining and Quarrying segment dropped to 14.90% in May from 15.42% in April.

THANK YOU