

Economic & Market Outlook

Currency fluctuations and its impact on exports

APRIL 2018

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The recommendation framework for stocks and sectors are as follows : -

Stock Ratings

Buy: Share price may exceed 10% over the next 12 months

Trading Buy: Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain

Neutral: Share price may fall within the range of +/- 10% over the next 12 months

Take Profit: Target price has been attained. Look to accumulate at lower levels

Sell: Share price may fall by more than 10% over the next 12 months

Not Rated: Stock is not within regular research coverage

Industry/Sector Ratings

Overweight = Industry expected to outperform the FBM KLCI benchmark, weighted by market capitalisation, over the next 6-12 months.

Neutral = Industry expected to perform in line with the FBM KLCI benchmark, weighted by market capitalisation, over the next 6-12 months.

Underweight = Industry expected to underperform the FBM KLCI benchmark, weighted by market capitalisation, over the next 6-12 months.

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◆ Conclusion

◆ US - China trade row and its impact on global trade

IMF optimistic on global economic growth

- ◆ IMF upgraded the global growth forecast in January based on:
 - Unemployment rate easing
 - Monetary condition remains loose despite tightening
 - Political and disintegration risks ebbing in Eurozone
 - Stabilisation in China's economic growth at higher level despite moderating growth trend
- ◆ Downside risks remain given elevated financial market valuations in the US, rising trade protectionism and geopolitics.

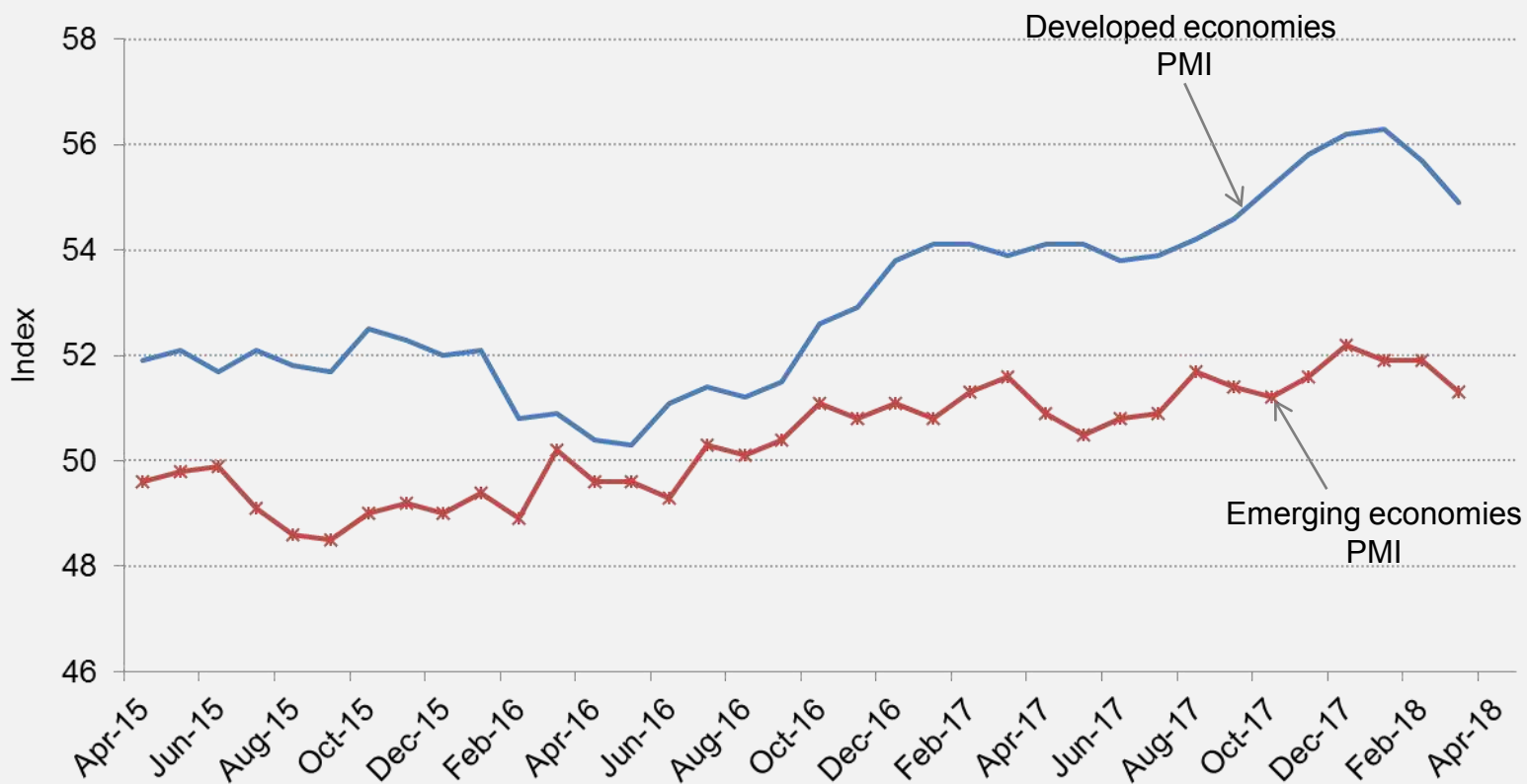
	IMF			
	2016	2017E	2018F	2019F
Global Economy	3.2	3.7	3.9	3.9
US	1.5	2.3	2.7	2.5
Euroland	1.8	2.4	2.2	2.0
UK	1.9	1.7	1.5	1.5
Japan	0.9	1.8	1.2	0.9
Canada	1.4	3.0	2.3	2.0
China	6.7	6.8	6.6	6.4
India	7.1	6.7	7.4	7.8
Malaysia	4.2	5.4	5.3	5.0
ASEAN-5	4.9	5.3	5.3	5.3
Advance economies	1.7	2.3	2.3	2.2
Emerging & developing	4.4	4.7	4.9	5.0

Source: IMF World Economic Outlook, January 2018

E: Estimates F: Forecasts

Developed industrial activity moderated somewhat but still healthy

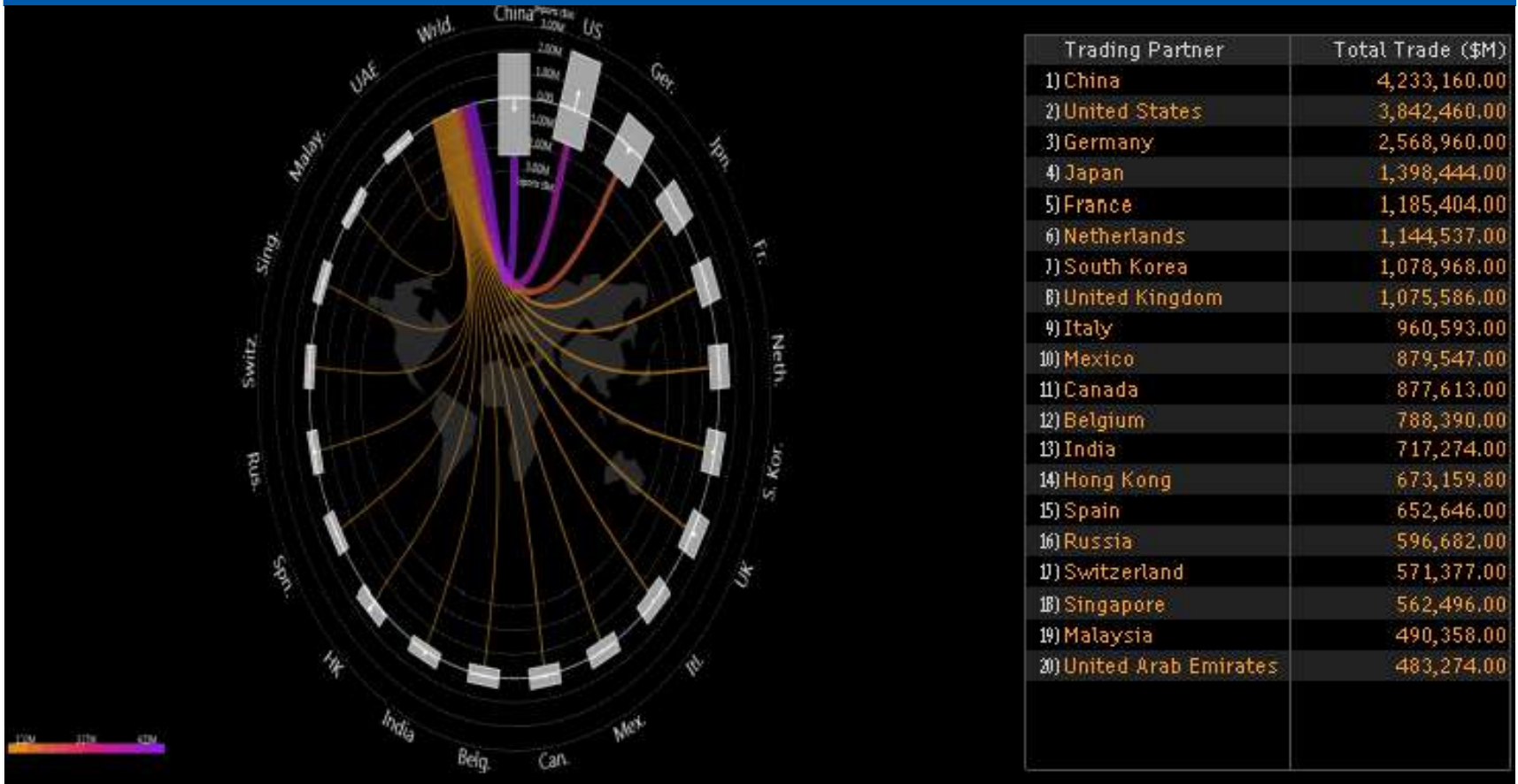
Developed and Emerging economies PMI Manufacturing index



Source: Markit Economics, Bloomberg

World Merchandise Trade Flows

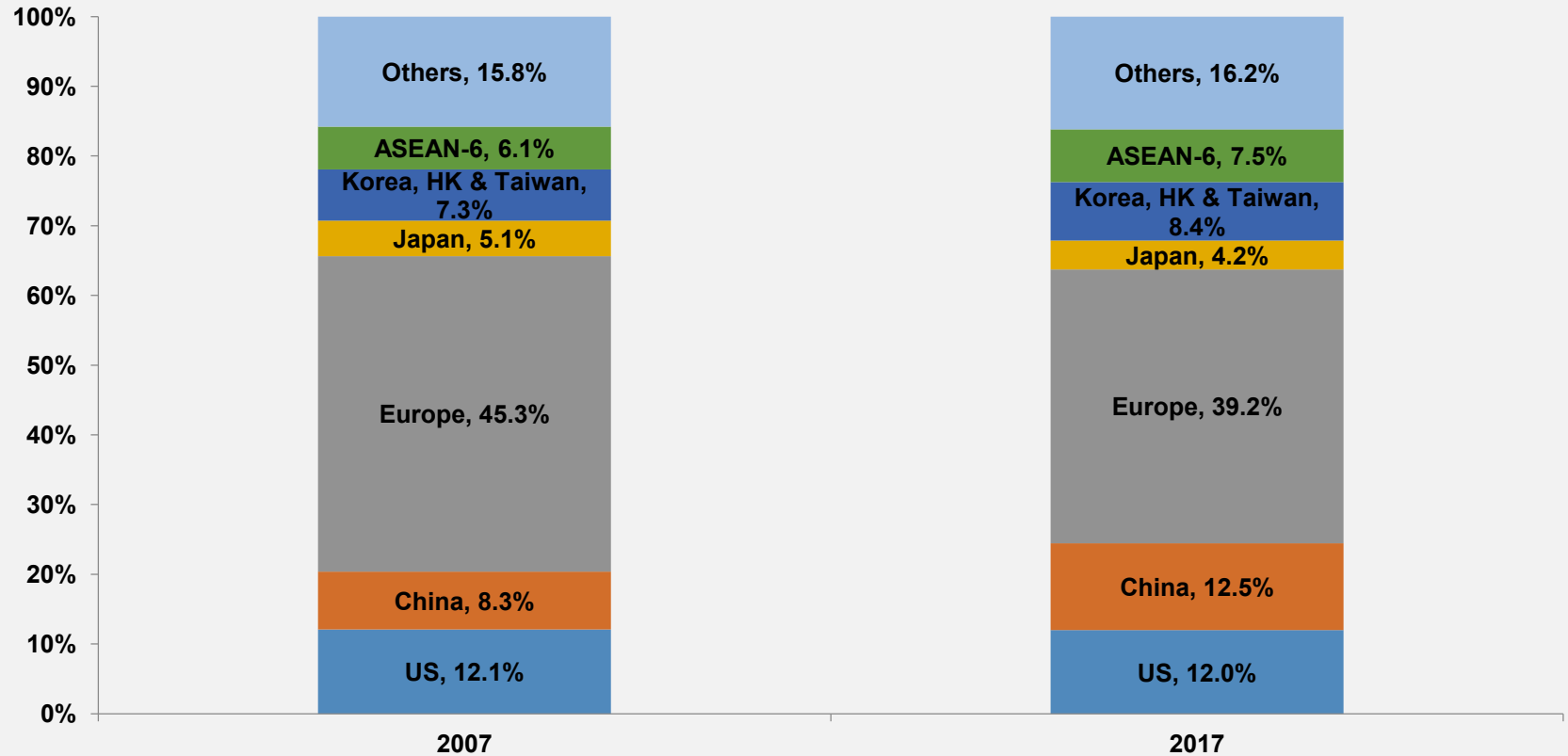
World Trade Flows in 2017



Source: Bloomberg

World Merchandise Trade Market Share

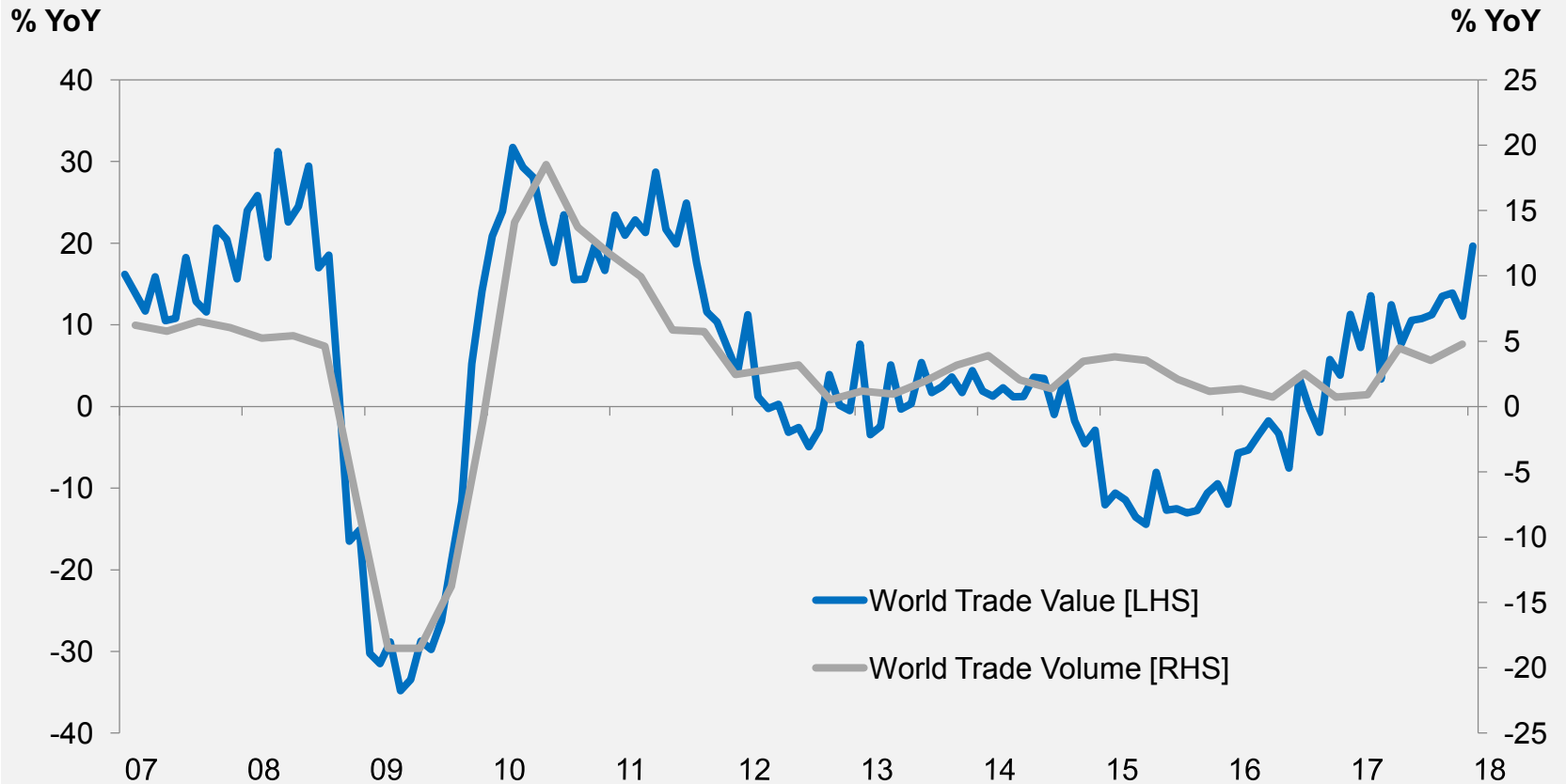
World Trade Market Share in 2017 (% share of world total)



Source: WTO, RHB

Global trade activity trending higher

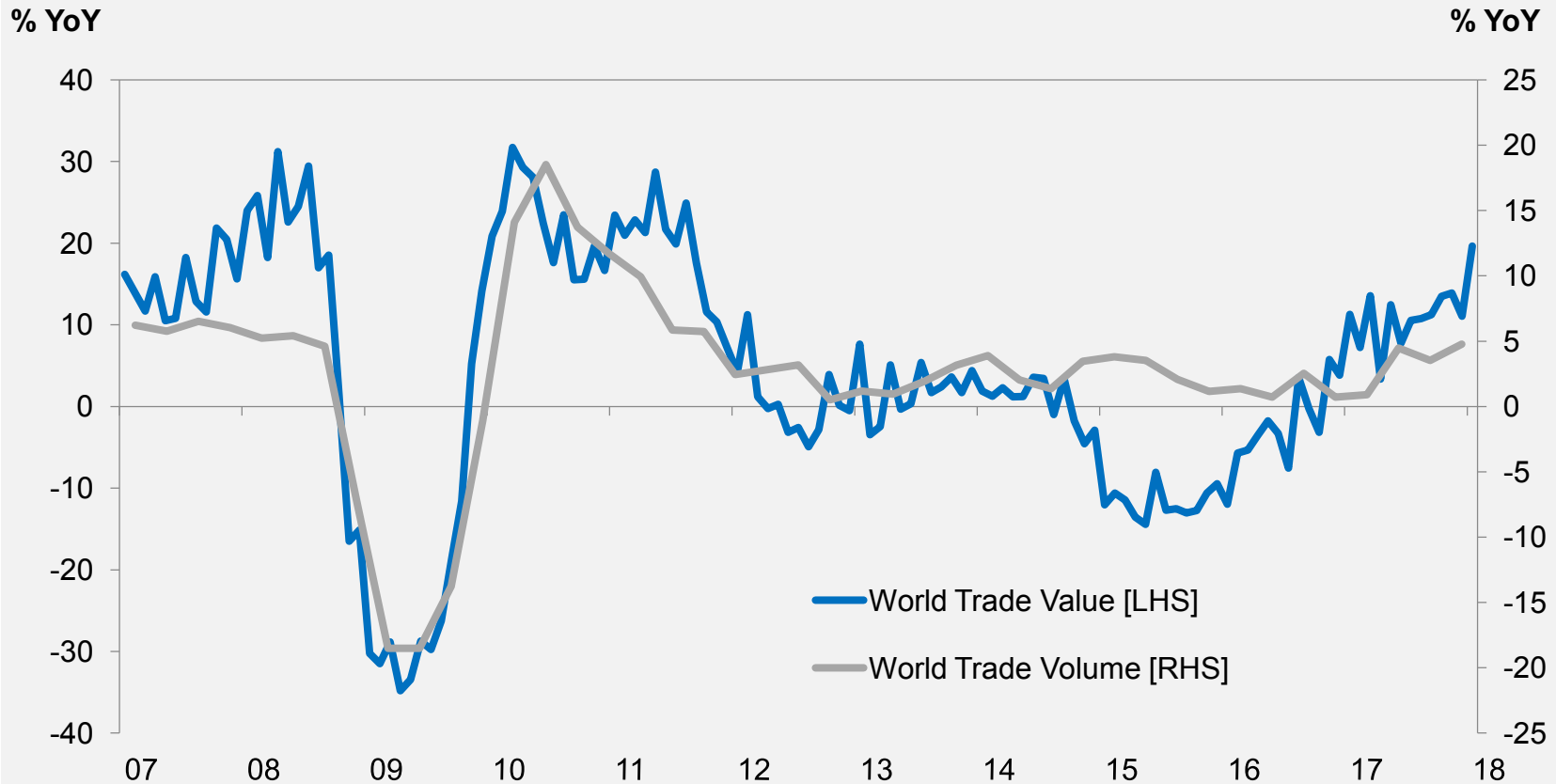
Global trade by value and volume terms



Source: WTO, RHB

Global trade activity trending higher

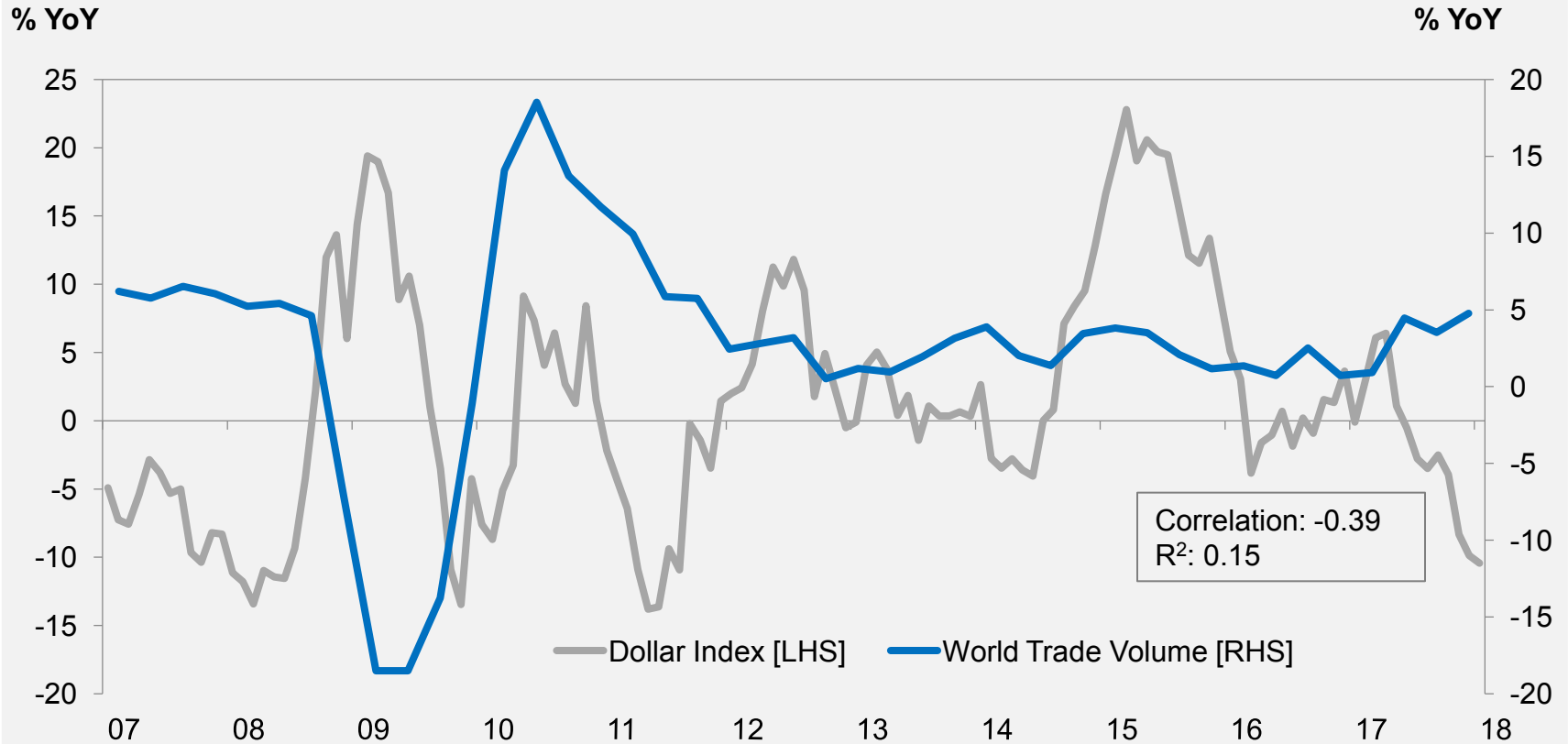
Global trade by value and volume terms



Source: WTO, RHB

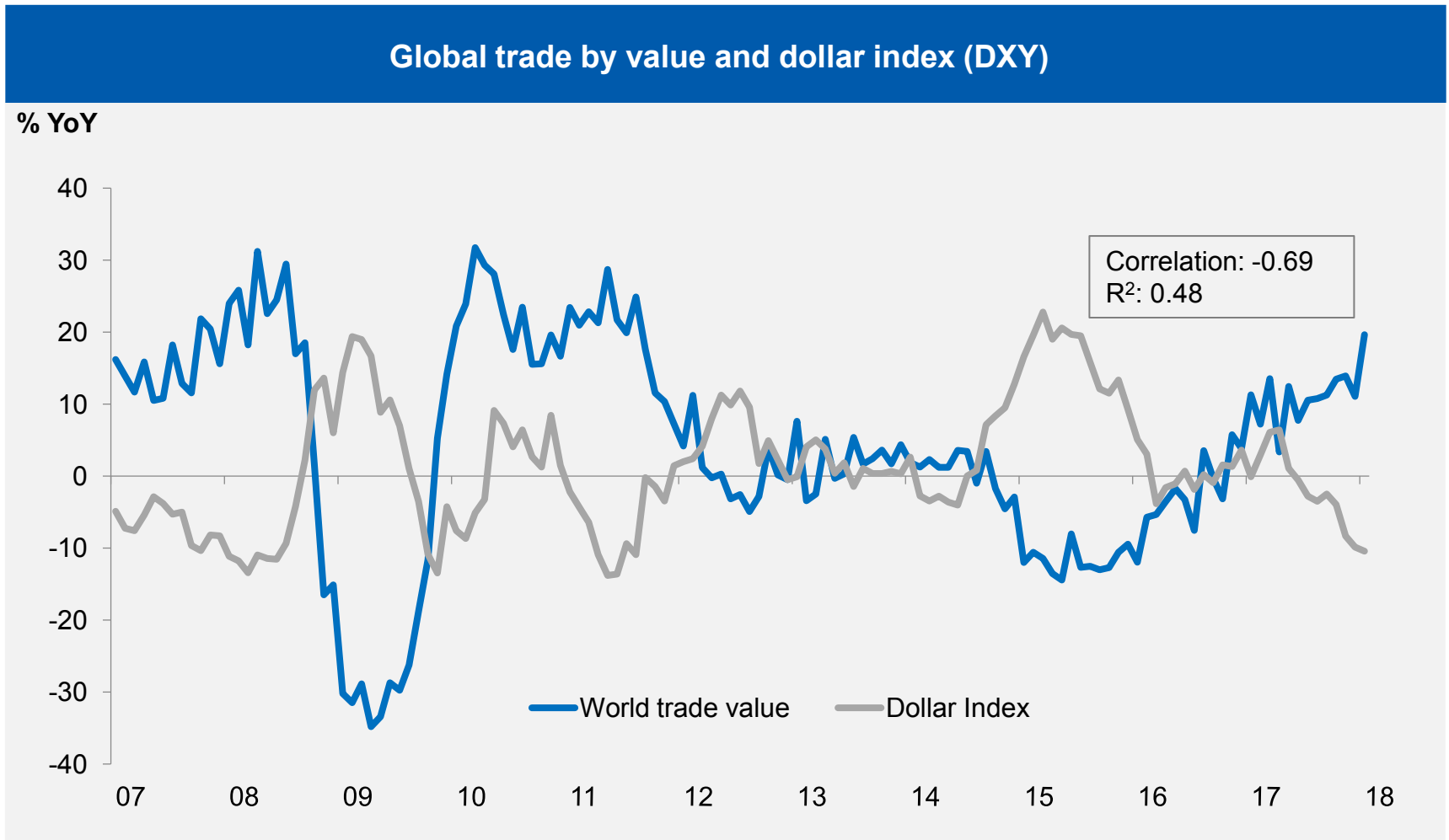
No significant relationship between trade volumes and US dollar

Global trade by volume and dollar index (DXY)



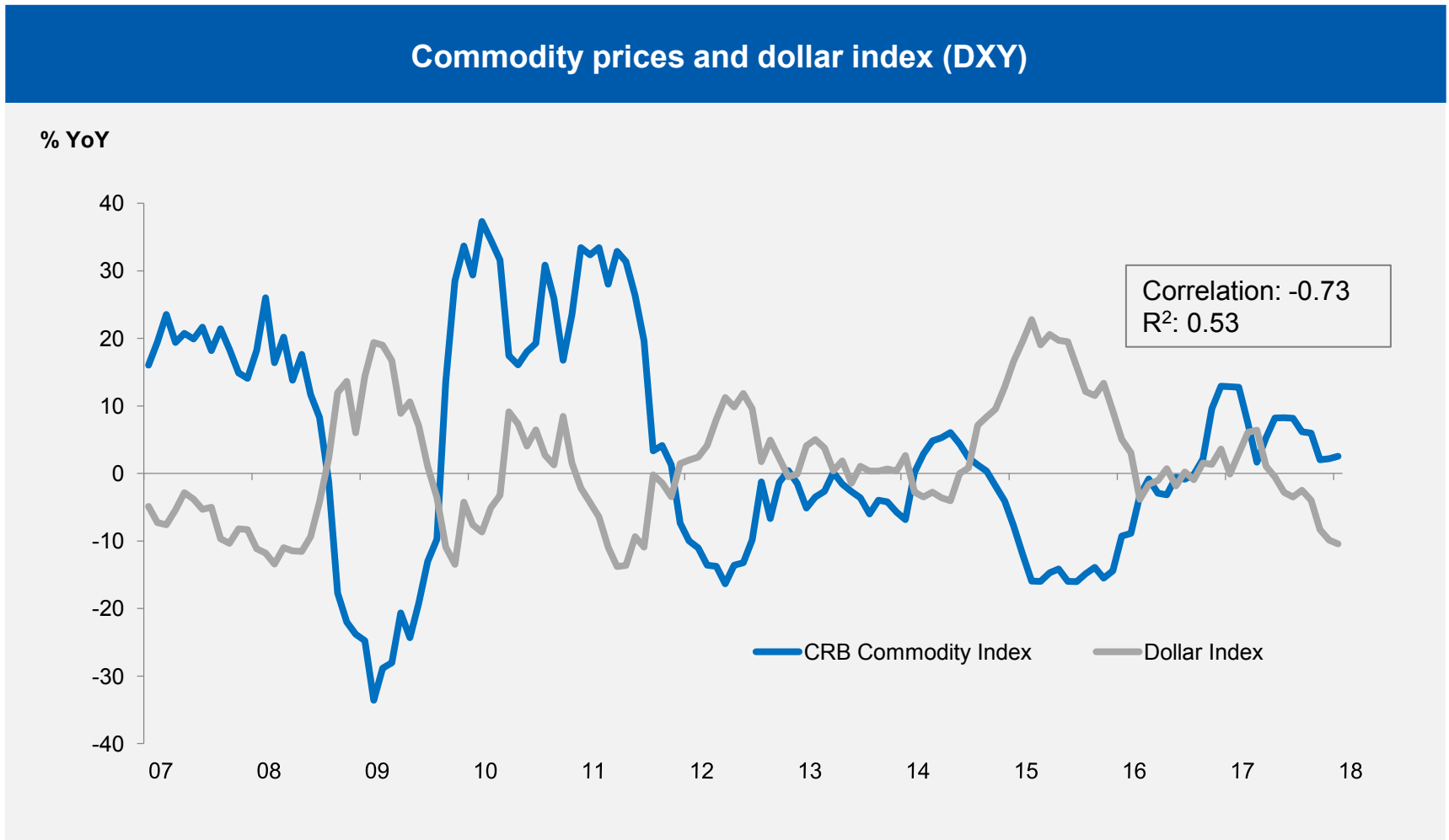
Source: WTO, Bloomberg, RHB

Global trade values tend to move in opposite direction to the dollar



Source: WTO, Bloomberg, RHB

Commodity prices have a inverse relationship with US dollar

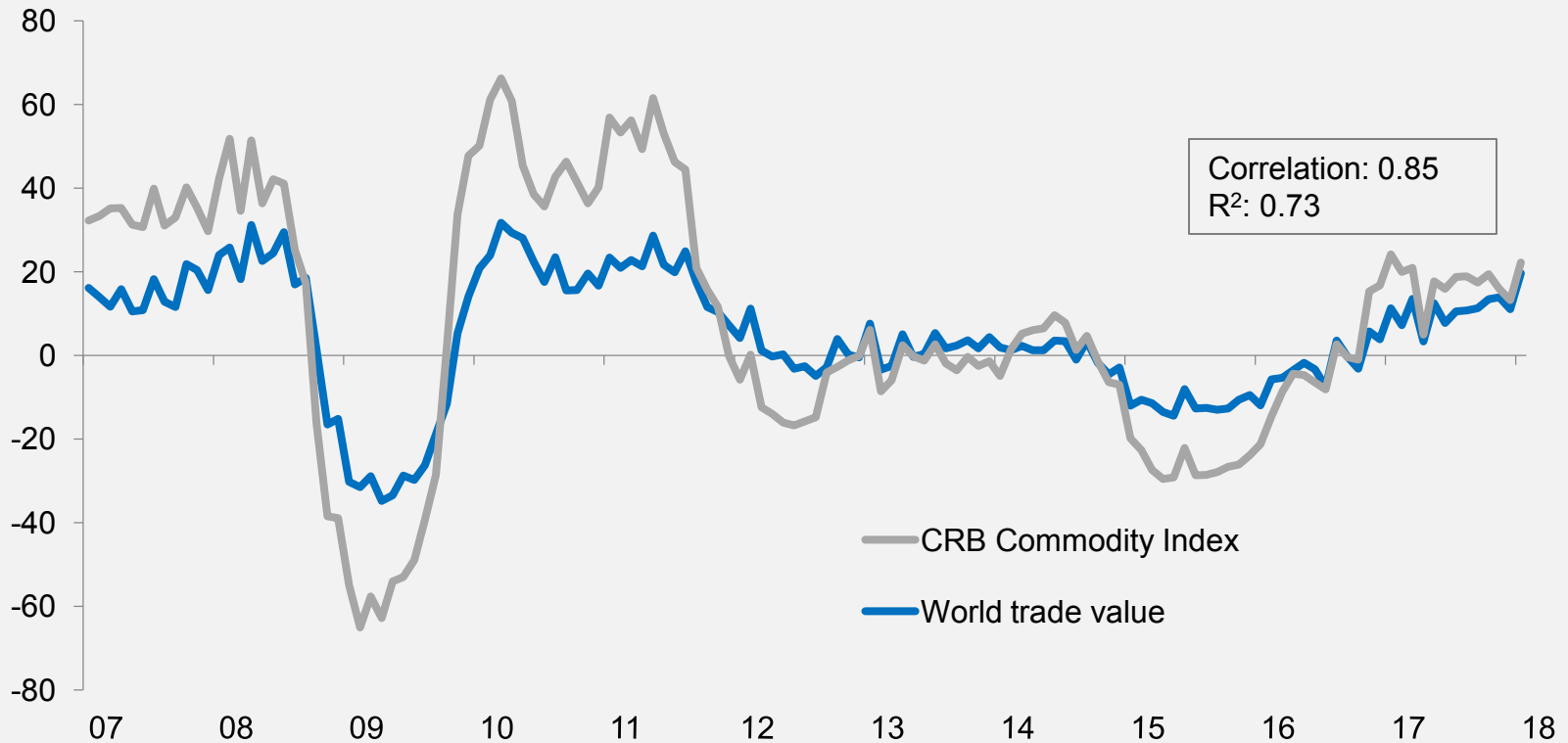


Source: WTO, Bloomberg, RHB

Commodity prices driver of trade growth

Global trade by value and commodity prices

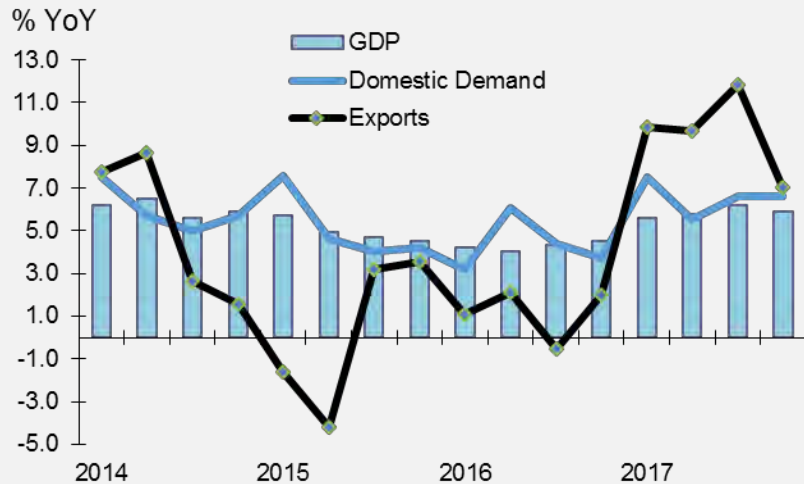
% YoY



Source: WTO, Bloomberg, RHB

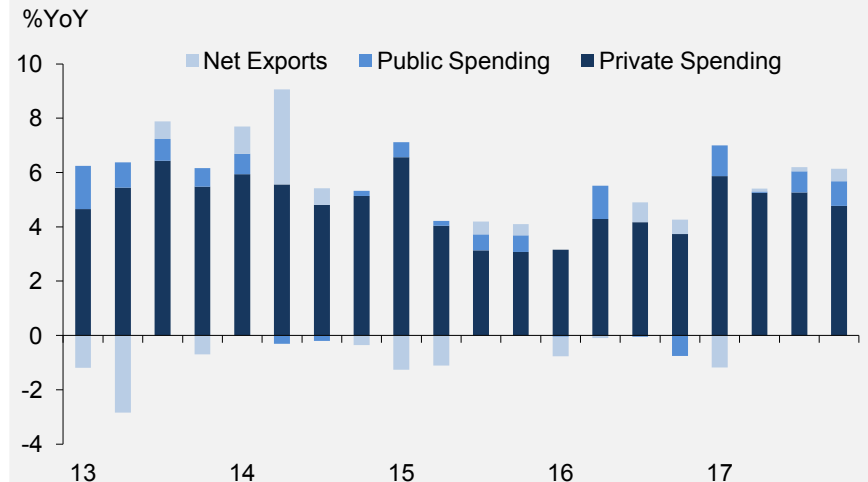
Malaysia: Slower growth anchored by stable private spending

GDP growth to moderate in 2018



Source: Dept. of Statistics

Growth led by private spending

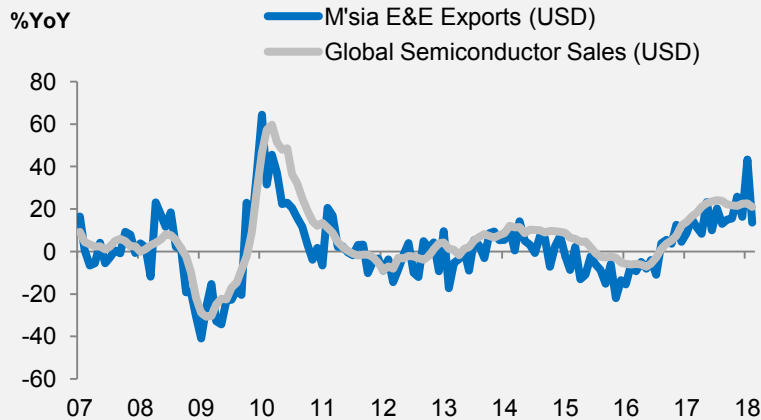


Source: DOS, RHB estimates

- ◆ Real GDP growth moderated to 5.9% YoY in 4Q17, from +6.2% in 3Q and +5.8% in 2Q amid slower export growth and domestic demand.
- ◆ Growth expected to expand at 5.2% in 2018 (2017: +5.9%) as external demand normalises while domestic demand to stay resilient. Spillover from exports to domestic demand to become more broad-based and partly cushion export slowdown in 2018.
- ◆ Fallout from potential US-China trade war may impact Malaysia through value chain. Anticipated slowdown in China to affect EM economies like Malaysia for 2018.

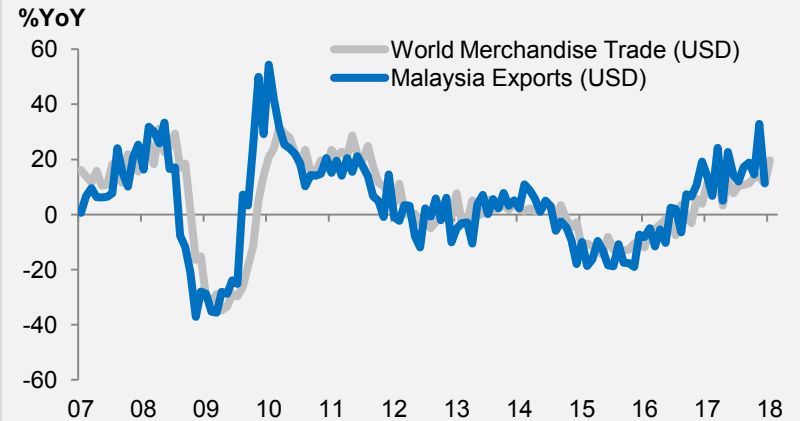
External trade to normalise, though momentum still strong

Robust global semicon sales supports E&E exports



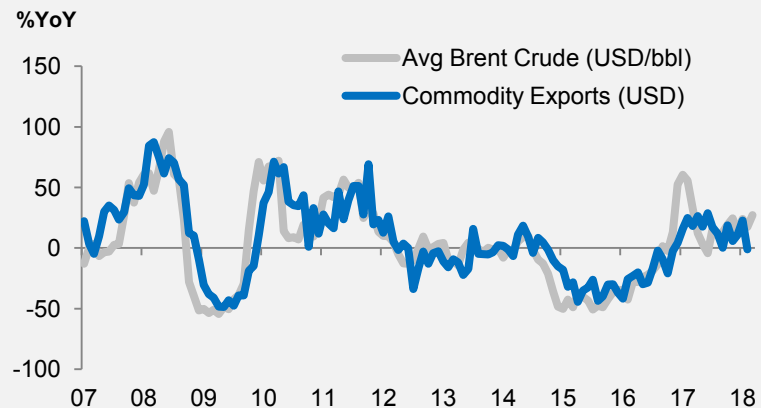
Source: Semiconductor Industry association (SIA)

Global merchandise trade still on uptrend



Source: Dept. of Statistics

Higher oil prices boon to commodity exports



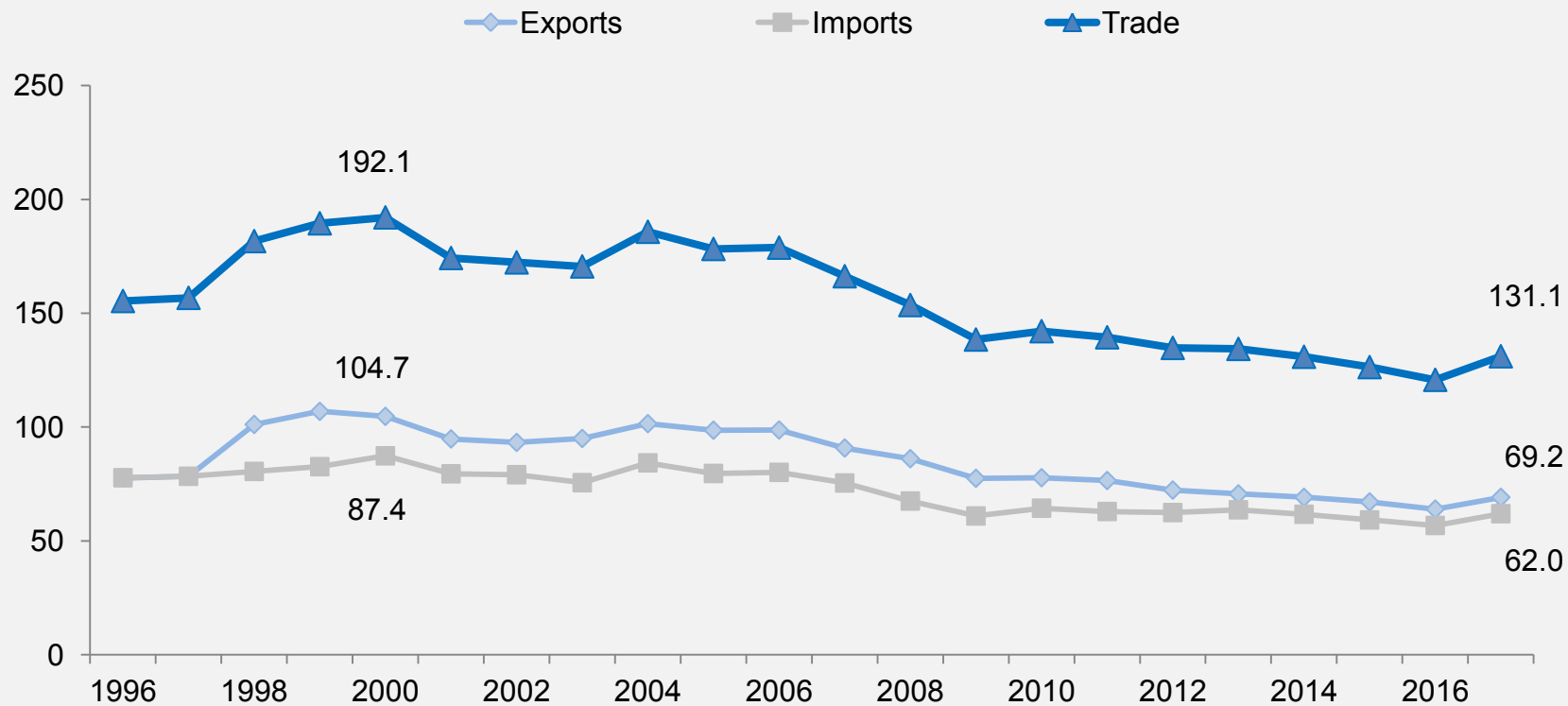
Source: CPB World Trade Monitor

- ◆ Malaysia's export growth grew 7.8% YoY in 2M18, slowing from +18.9% in 2017.
- ◆ Looking ahead, Malaysia's external outlook in 2018 remains supported by sustained global growth and trade outlook; strong global E&E demand; and stable commodity prices.
- ◆ Risk, however, still emanates from potential US-China trade war and anticipated slowdown in China's growth.

External trade has always played major role in Malaysian economy

Malaysia External Trade Percentage Share of GDP

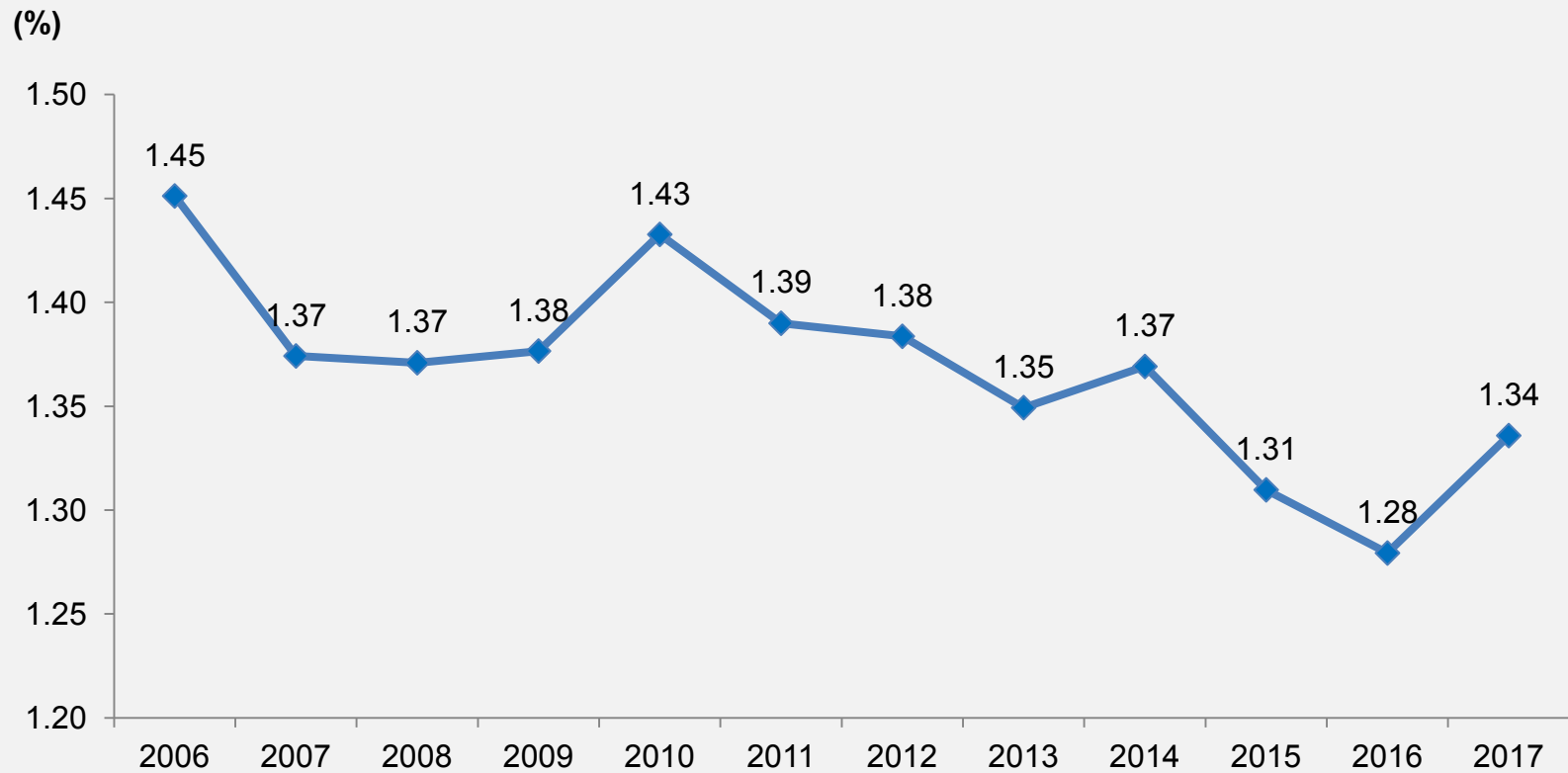
% Share of GDP



Source: DOSM, RHB

Exports share has seen a gradual decline over the years

Malaysia Export Market Share of World (%)



Source: WTO, RHB

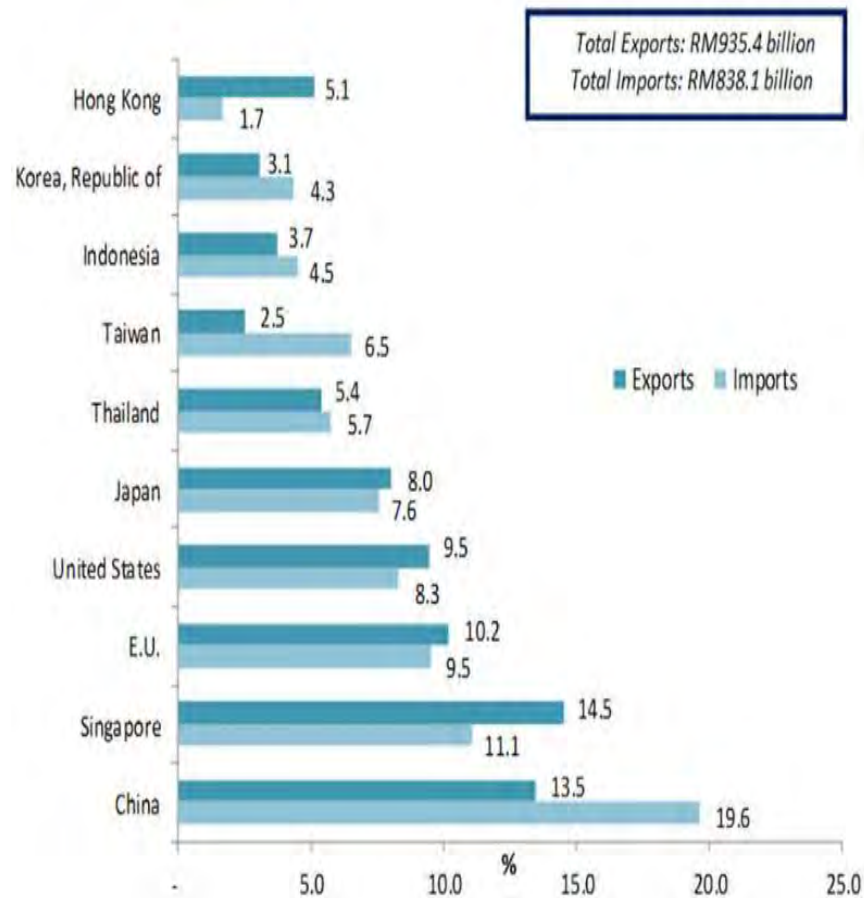
Malaysia external trade breakdown by country

Malaysia's Top 10 Trade Partners
(% share)



Source: DOSM, RHB

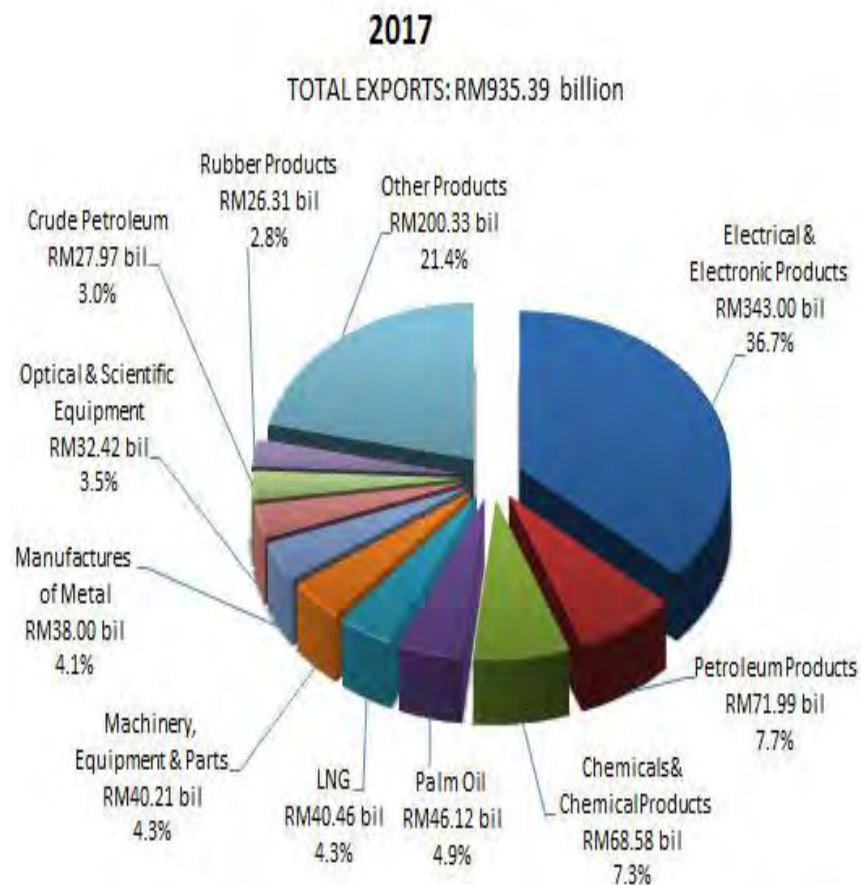
Malaysia's Top 10 Trade Partners
Exports-Imports (% share)



Source: DOSM, RHB

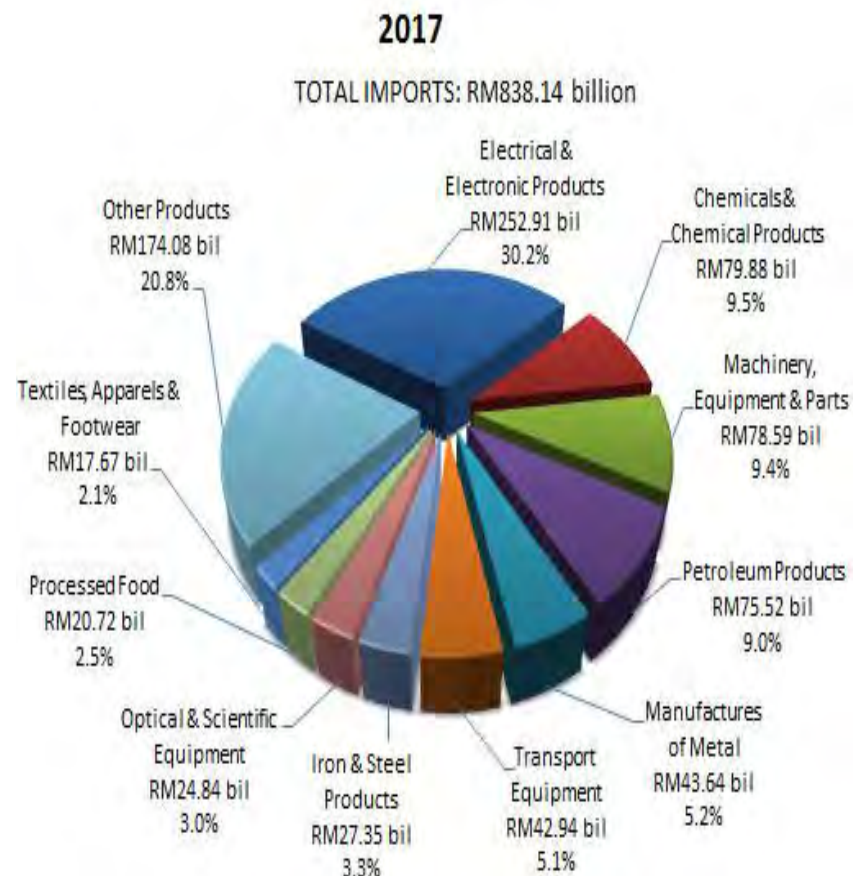
Malaysia external trade breakdown by products

Malaysia's Top 10 Export Products (% share)



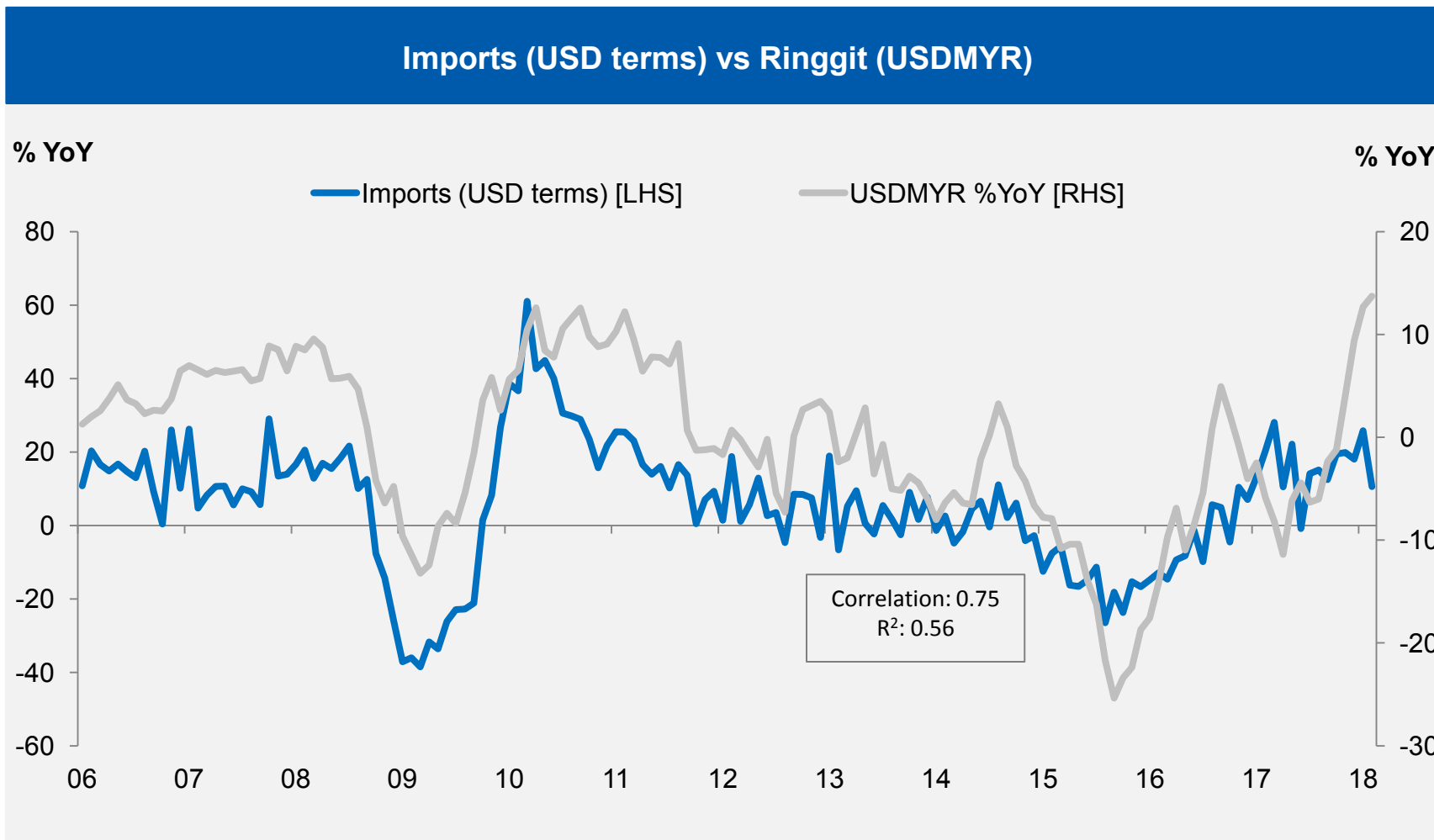
Source: DOSM, Matrade, RHB

Malaysia's Top 10 Import Products Exports-Imports (% share)



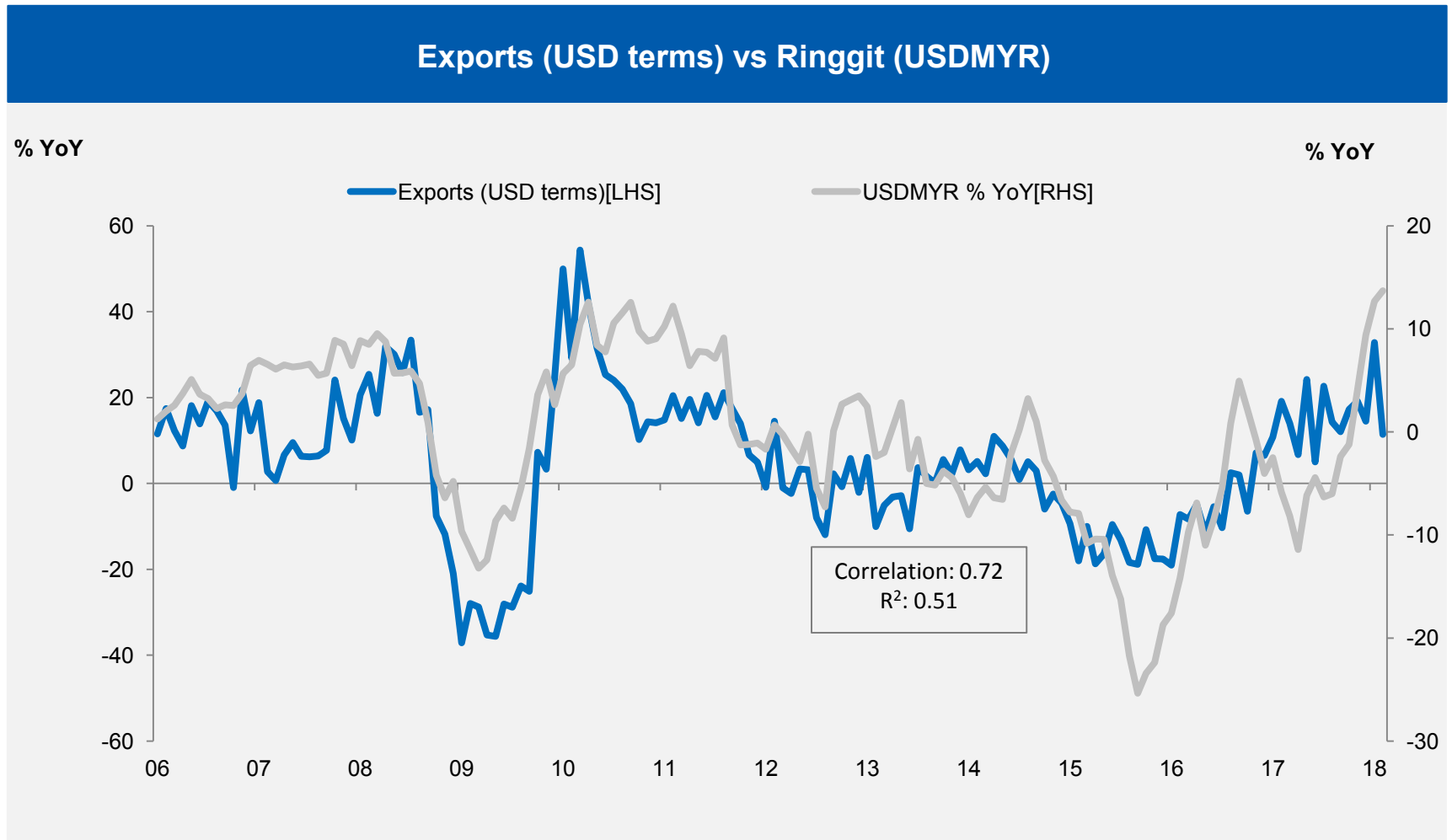
Source: DOSM, Matrade, RHB

Import growth move along with ringgit performance



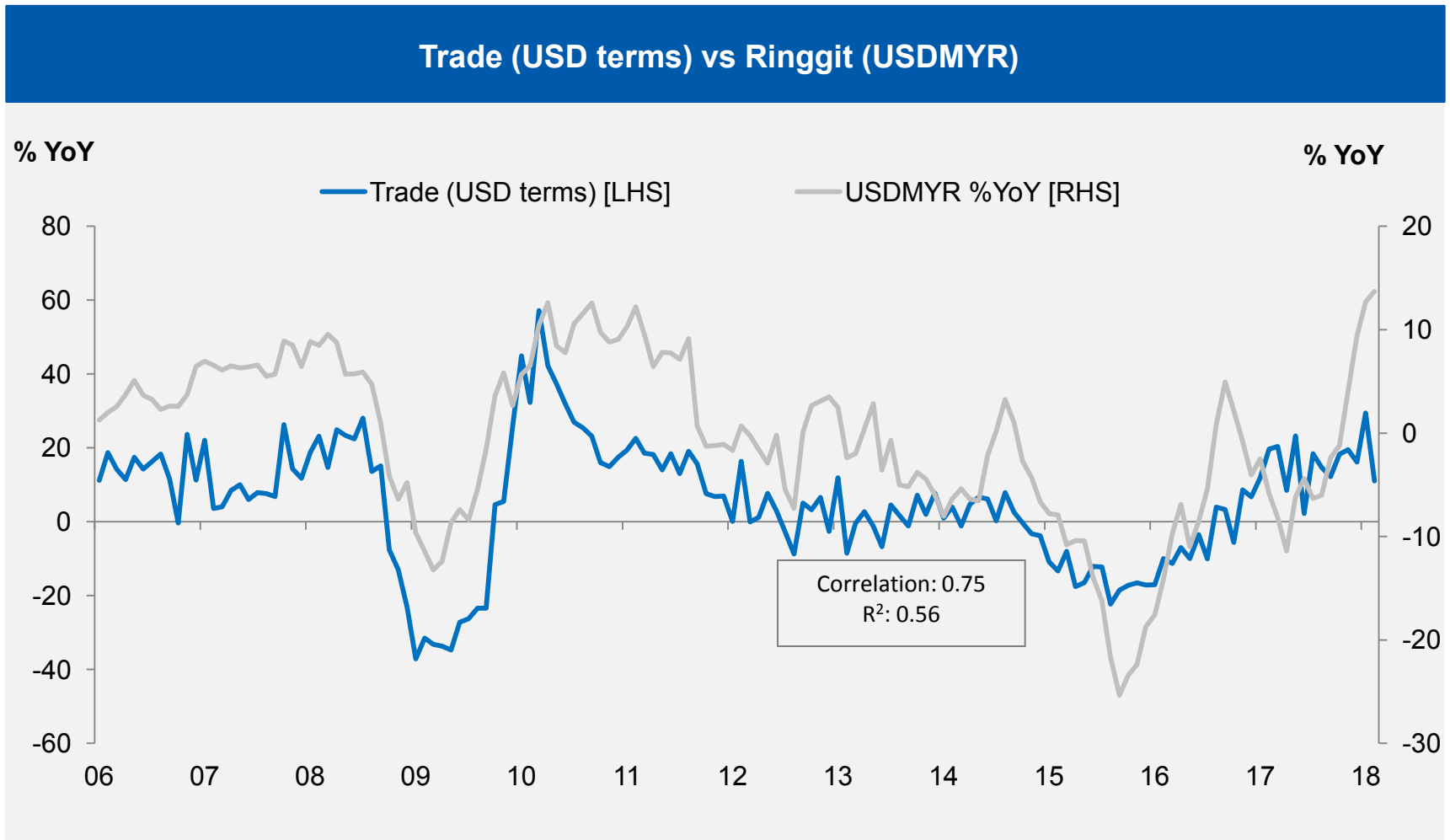
Source: DOSM, Bloomberg RHB

... So is export growth???



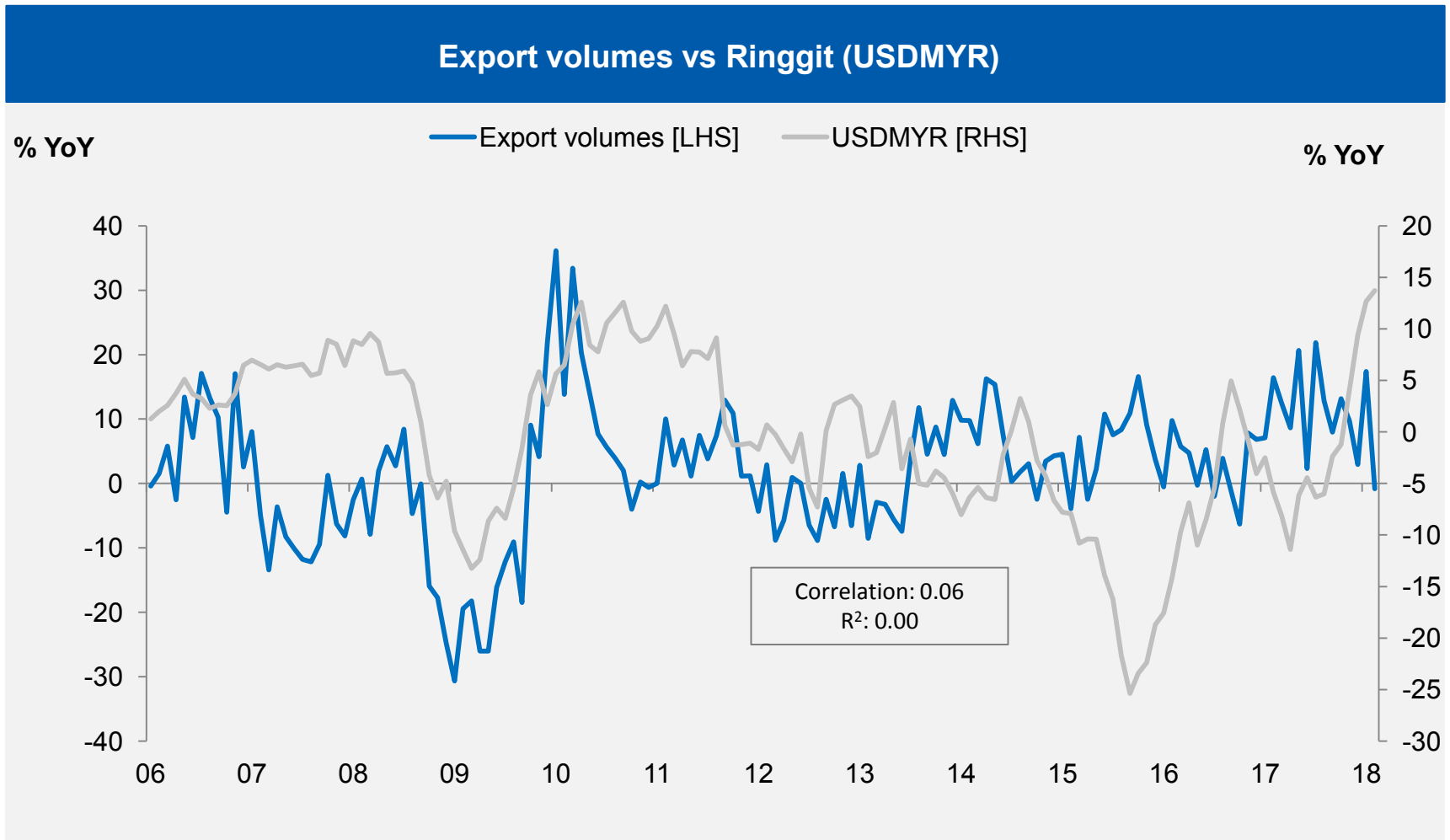
Source: DOSM, Bloomberg, RHB

Overall, trade moves in tandem with Ringgit performance



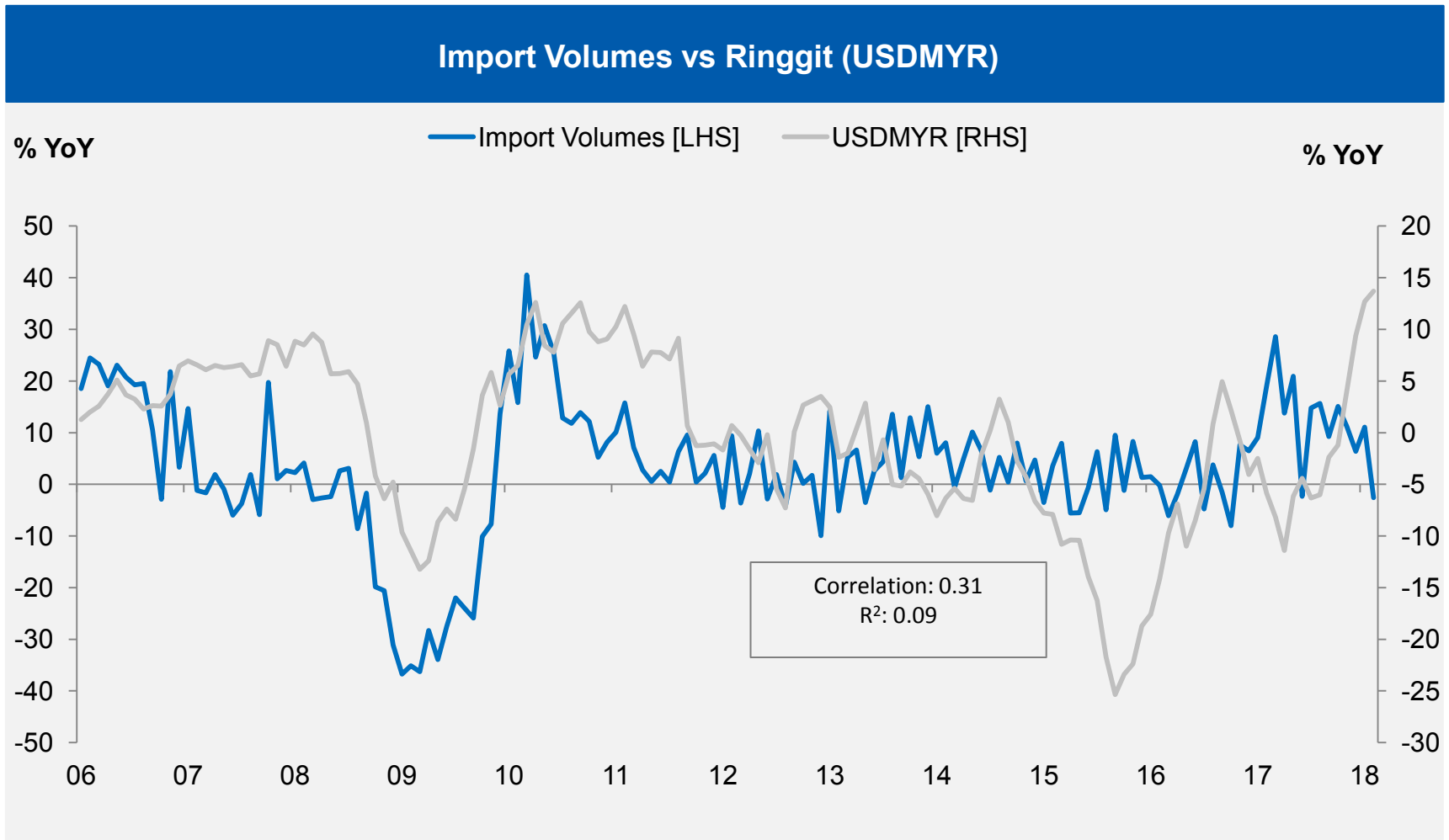
Source: DOSM, Bloomberg RHB

Ringgit impact on export volumes insignificant



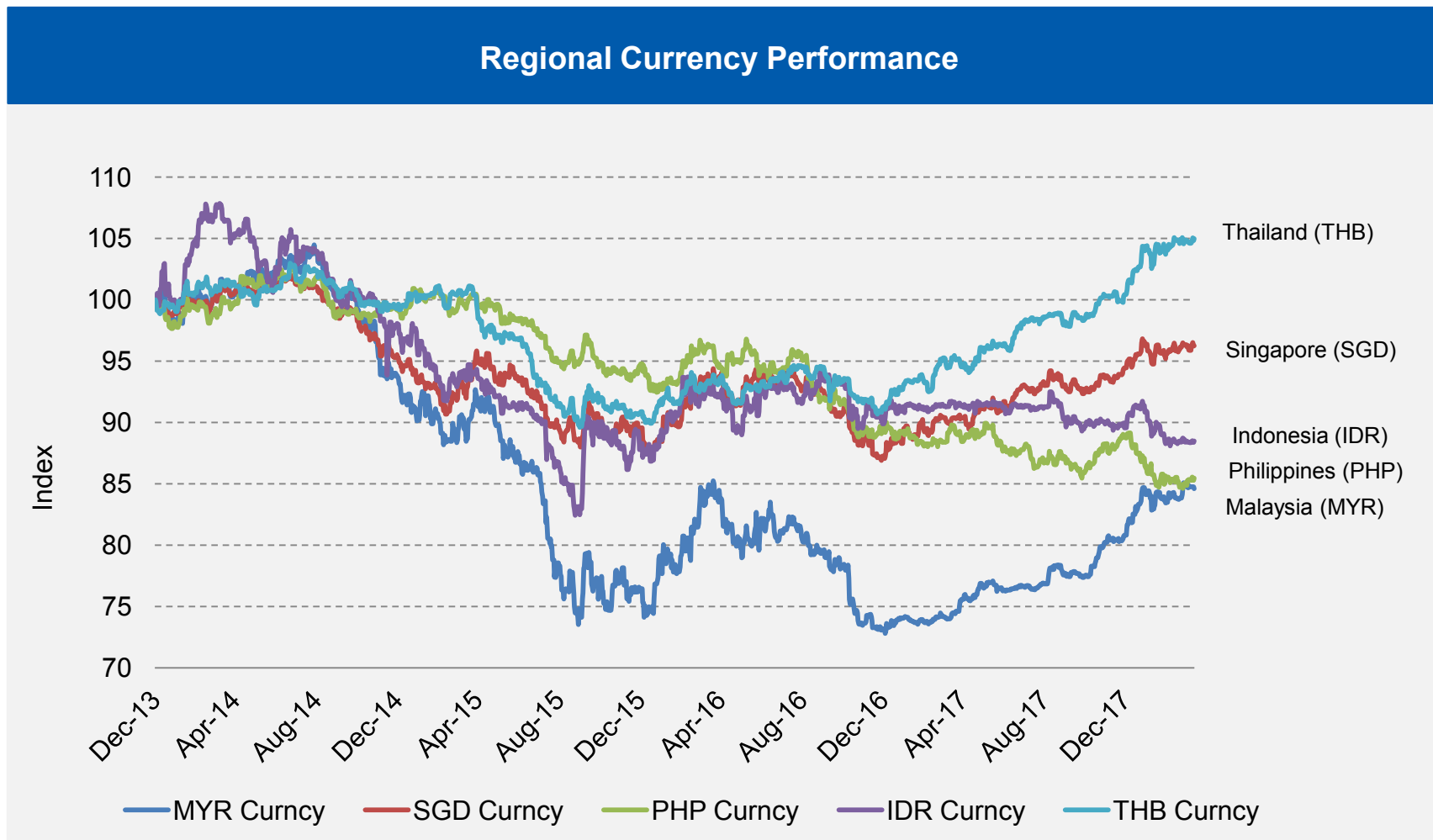
Source: DOSM, Bloomberg RHB

Slightly better for import volumes



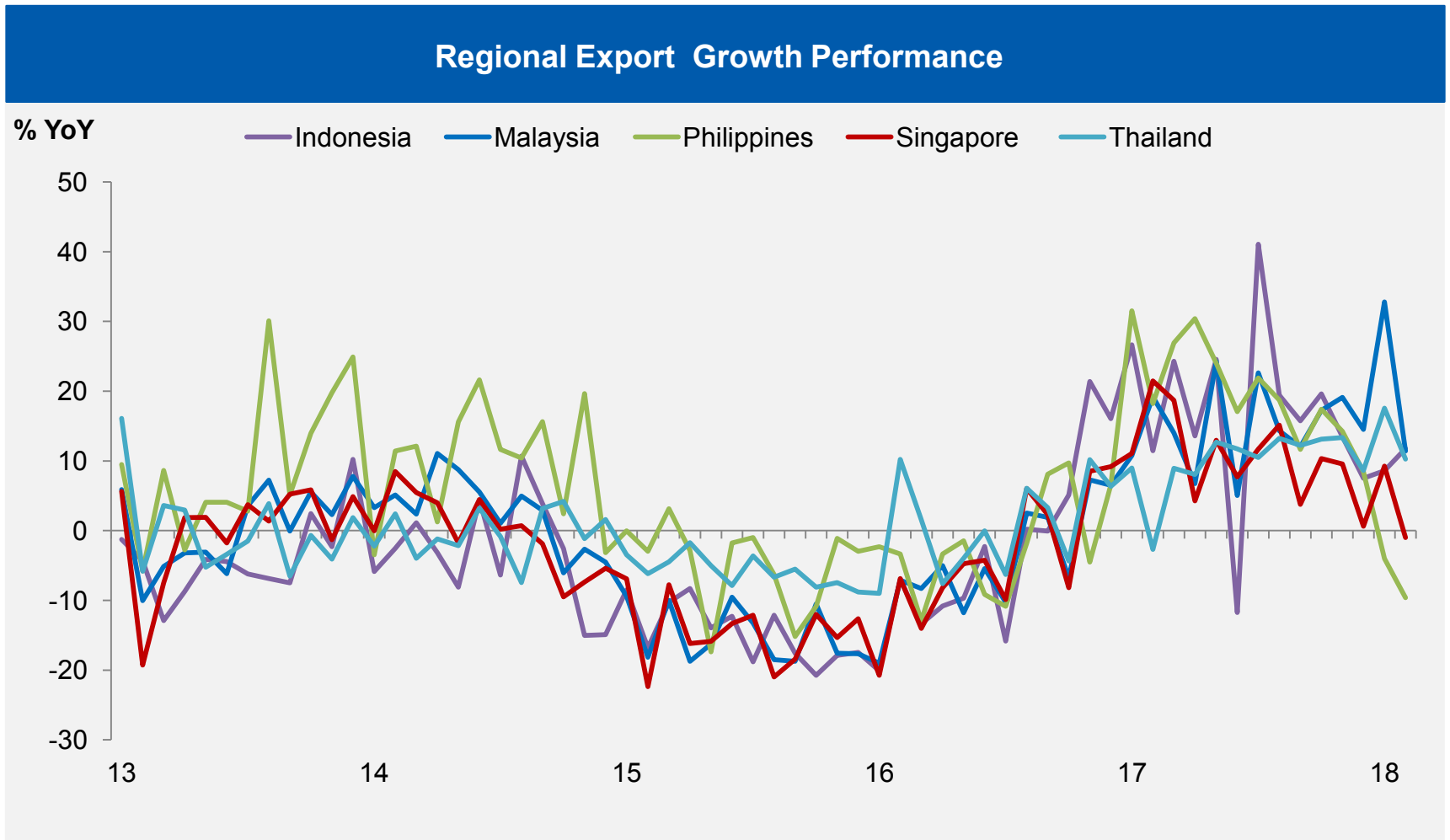
Source: DOSM, Bloomberg RHB

Ringgit performance still lags the region



Source: DOSM, RHB

Export growth move in same direction across the region



Source: DOSM, RHB

BNM study suggests ringgit contributes only 14% to export volumes

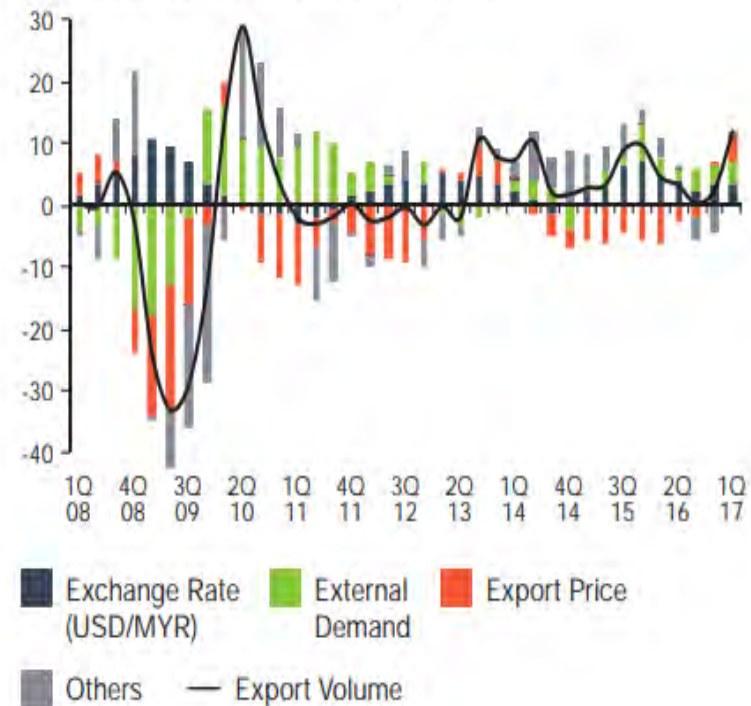
Demand and relative export price factors a larger determinant of exports

Contribution of the Determinants of Export Volume Growth (Average 2005-2016)

Determinants	Contribution (%)
External Demand	29
Relative Export Price	26
Exchange Rate (USD/MYR) <i>(inc. its interaction with backward linkages)</i>	14
Others	31

Source: Bank Negara Malaysia

Contribution to growth (percentage points)



Source: Bank Negara Malaysia

Malaysia increasingly involved in Global Value Chain (GVC)

Growing import content reduces the effect of exchange rates

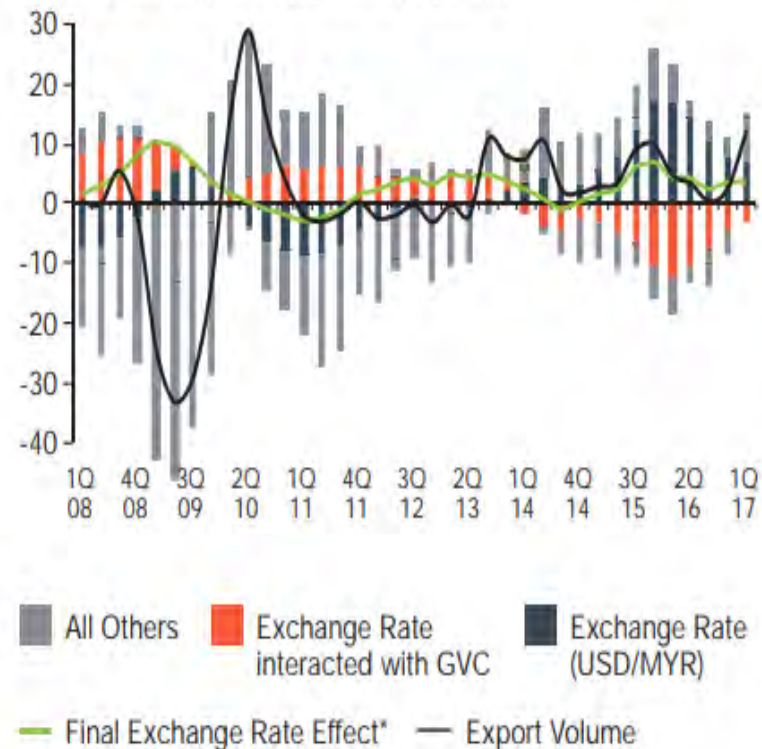
GVC and the Exchange Rate Effect

Determinants	Contribution (ppt)
Exchange rate (A)	4.2
Exchange rate interacted with GVC (B)	1.9
Final exchange rate effect* (C = A - B)	2.3
Offsetting effect (%) (B / A)	45%

Source: Bank Negara Malaysia

* The Final Exchange effect (C) is the difference between the Exchange Rate (A) and its interaction with GVC (B).

Contribution to growth (percentage points)



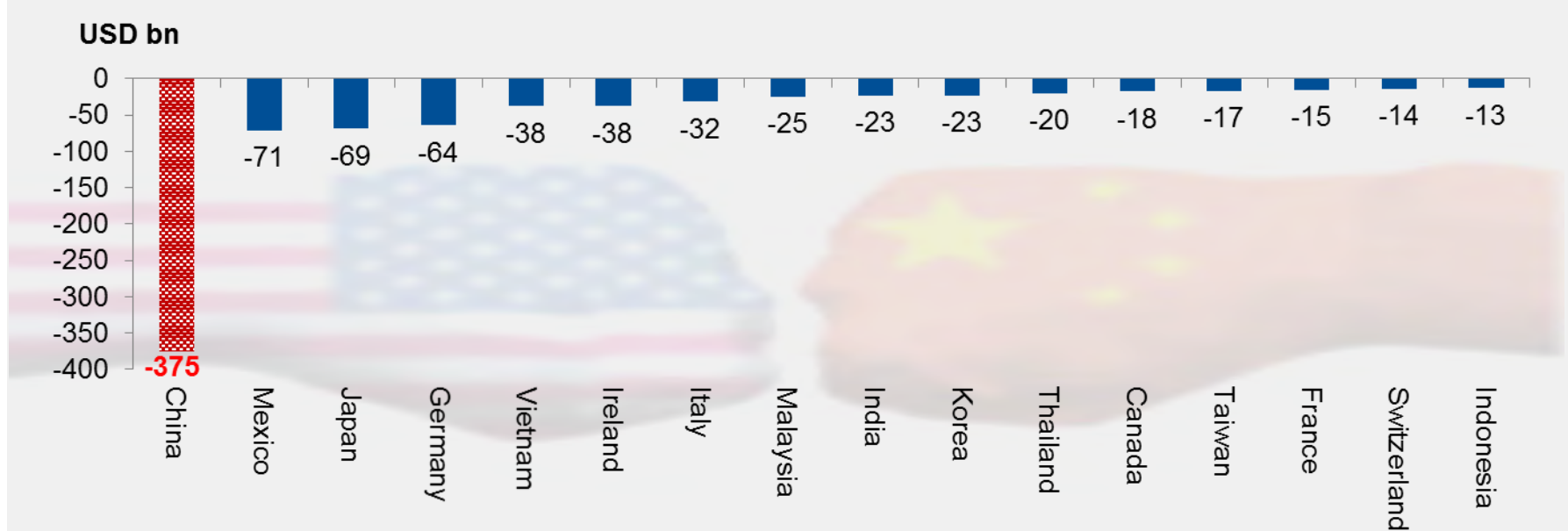
Source: Bank Negara Malaysia

Conclusion: Exchange rate not a good predictor of trade

- ◆ Global trade has inverse relationship with USD (move opposite direction), instead of same direction.
- ◆ Commodity prices a more important driver of global trade.
- ◆ For Malaysia, trade growth moves in tandem with Ringgit due to global economic and trade cycles.
- ◆ Ringgit impact on export and import volumes largely insignificant.
- ◆ External demand and relative export prices is a more important determinant of export growth.

US rising trade protectionism – Imposing import tariffs on selected Chinese products

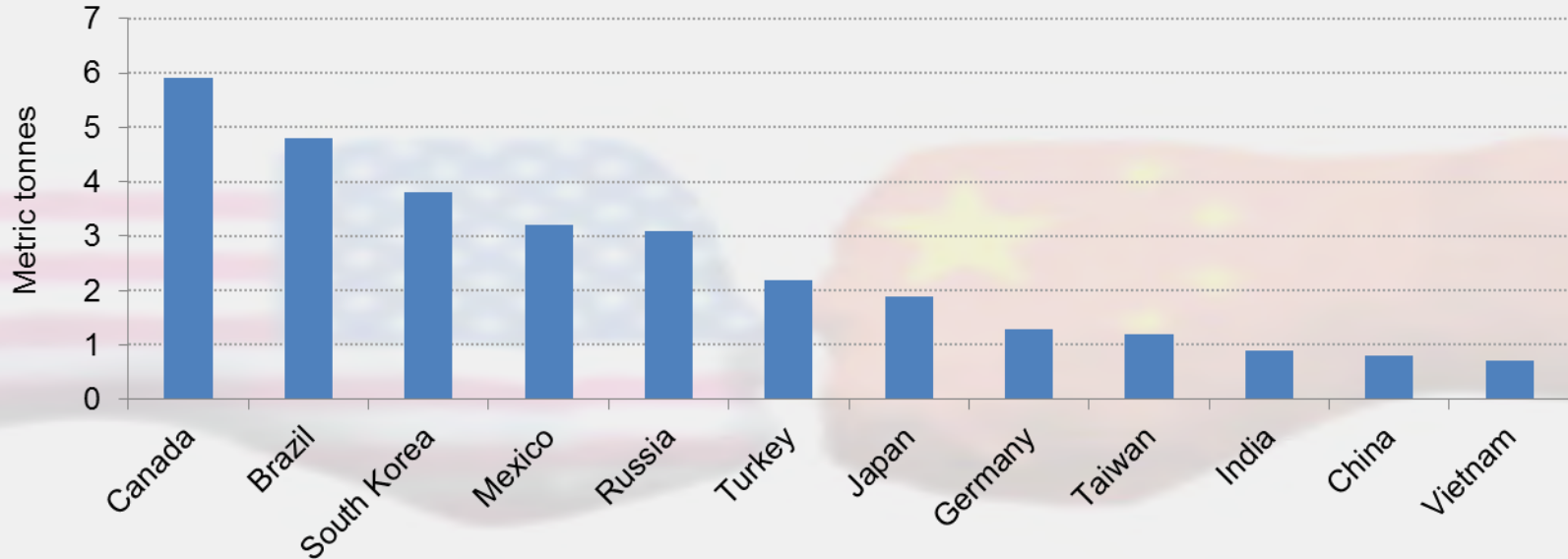
US trade deficit by country in 2017



- ◆ The Trump administration proposed to impose tariffs on a broad range of its imports from China to punish Beijing for its alleged theft of intellectual property. Also the US will restrict Chinese investments in the US.
- ◆ The 25% tariffs on USD50-60bn products accounted for 10-13% of China's exports to the US and 2.2-2.6% of China's total exports.
- ◆ China responded by proposing to impose 25% import tariffs on USD50bn of US' exports to China or a significant 38% of US' exports to China. This represents 3.2% of US' total exports.

US slaps import tariffs on steel and aluminium

US steel imports by country



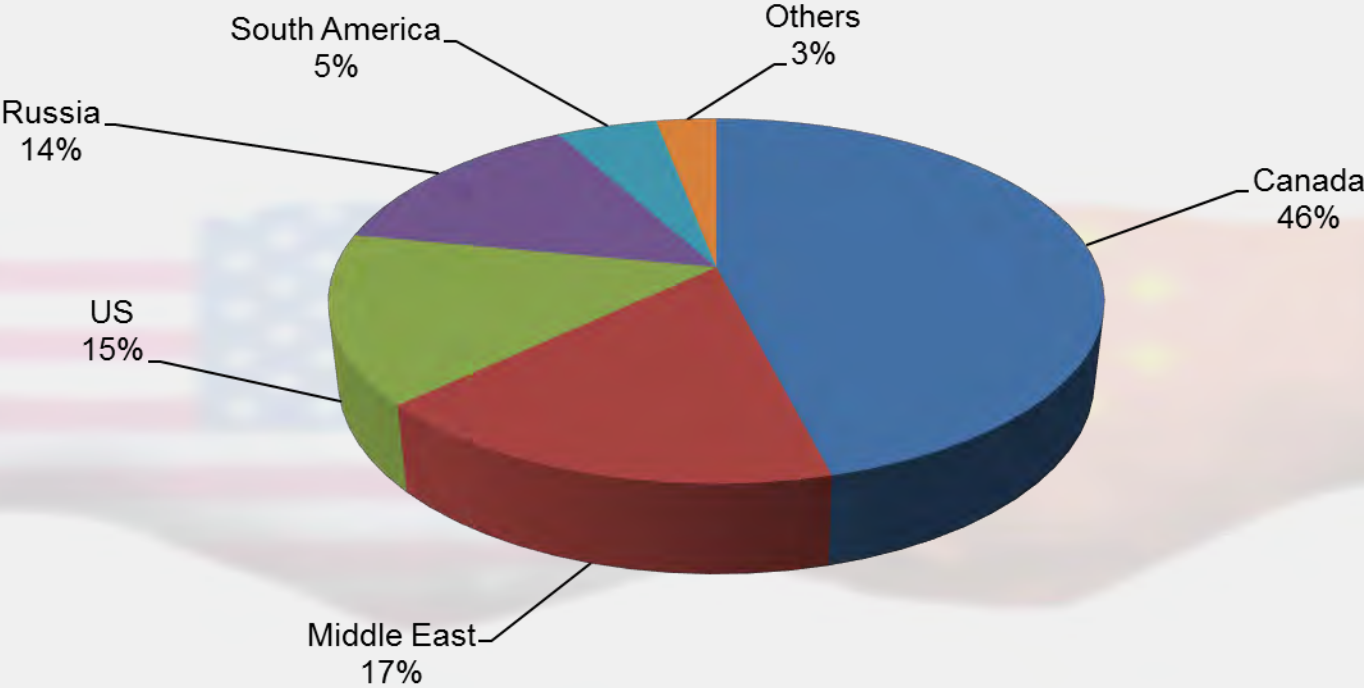
Note: Annualised 10 months 2017 data

Source: US Commerce Department, Bloomberg

- ◆ US President Donald Trump announced on 1 Mar that he would impose duties of 25% on steel and 10% on aluminium. A formal announcement would be made very soon.

US slaps import tariffs on steel and aluminium

US aluminium supply



Source: CRU Group, 2016 and Bloomberg

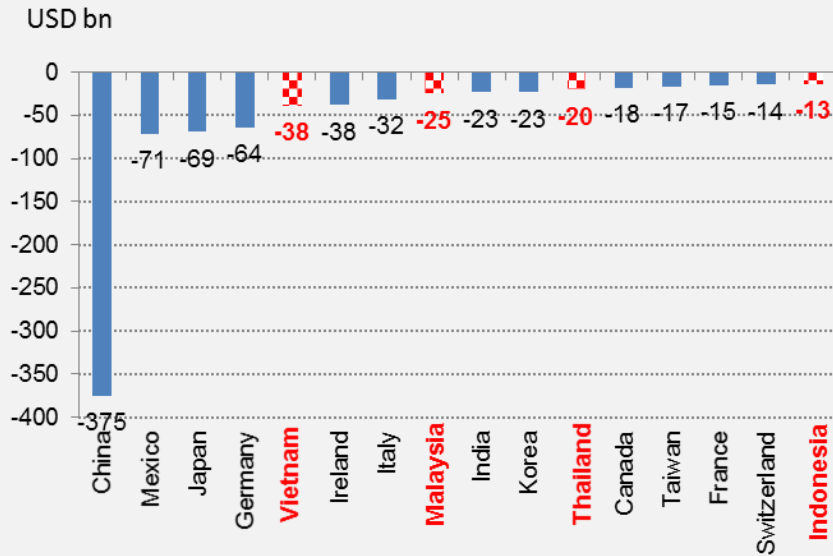
◆ Canada again the largest exporters followed by the Middle East.

US imposes higher tariffs on washing machines and solar panels

- ◆ US imposed tariffs on washing machines and solar panels on 22 January.
- ◆ A 20% tariff on the first 1.2 million imported large residential washers in the first year, and the subsequent units will be tax at 50%. The tariffs, however, will decline to 16% and 40% respectively in the third year.
- ◆ A 30% tariff will be imposed on solar cells and modules in the first year, with the tariffs declining to 15% by the fourth year. The tariff, however, allows 2.5 gigawatts of unassembled solar cells to be imported tariff-free in each year.
- ◆ The two cases were filed under the seldom-used Section 201 safeguard cases of the Trade Act of 1974. The last time this law was used is in 2002, when President George W. Bush clamped down on imports of steel. The approach has shown mixed results. The World Trade Organisation (WTO) ruled against the US in 2003, and the Bush administration ultimately withdrew the measure under threat of retaliation.
- ◆ South Korea said on 23 January that they would lodge a complaint with the WTO while China hinted that they may do the same.
- ◆ In our view, it remains to be seen whether China and South Korea will retaliate by imposing tariffs on US products and it is difficult to pin down whether it would evolve into a bigger trade war that is going to be damaging to global trade and economic growth.
 - In 2012, the US government added anti-dumping duties to Chinese solar panels, but manufacturers exploited a loophole that allowed them to bypass the duties by moving final assembly to Taiwan. When US solar manufacturers tried to get another set of tariffs installed in 2013, Chinese companies moved production to Germany, South Korea, Singapore, and Malaysia.
 - On washing machines, the US has been chasing the appliance makers since at least 2011, accusing the companies of repeatedly shifting production to low-cost countries including Thailand and Vietnam as part of an aggressive pricing strategy.
 - Asian appliance makers (LG, Samsung Electronics and China's Qingdao Haier and Midea), have set up US factories that could help ease the conflict as companies ramp up production there.

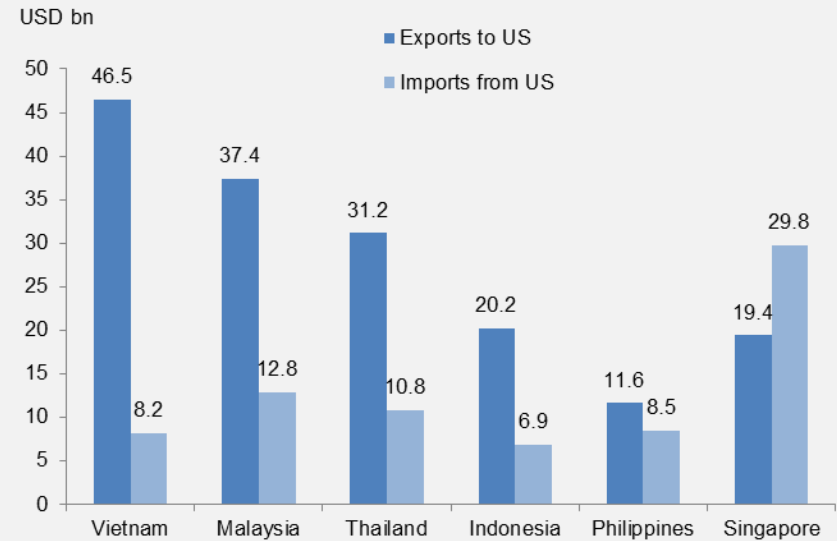
The watered down policy means impact on global trade and growth will likely be manageable

US trade deficit by country in 2017



Source: CEIC, US Department of Commerce

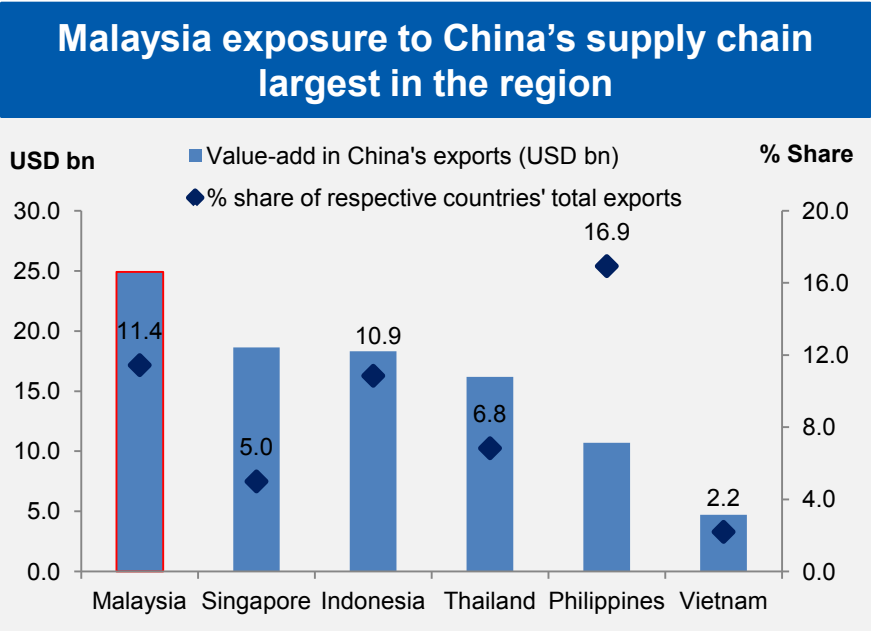
ASEAN trade with the US in 2017



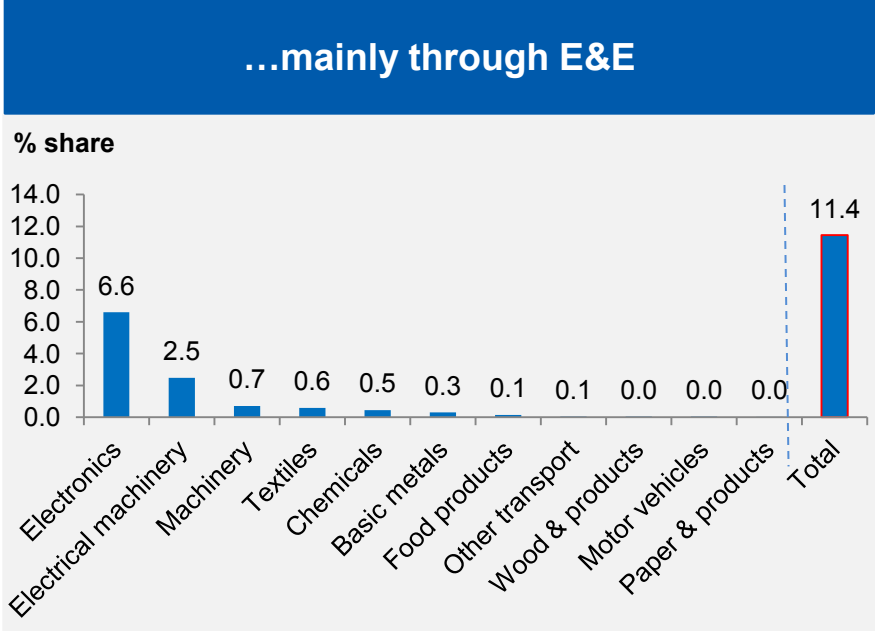
Source: CEIC, US Department of Commerce

- ◆ While trade tension among the nations has risen since Donald Trump became the US President, we believe it will unlikely evolve into a full-blown trade war as it would not benefit any country, and could affect global trade and economic growth, in our view.
- ◆ According to a recent International Monetary Fund (IMF) study, a 10% increase in import tariffs by the US, and assuming the rest of the world does the same as retaliation, it would lead to a 1% fall in world trade and 0.5% drop in world GDP.
- ◆ Given that the move by the US is somewhat diluted, it suggests that the impact on global trade and GDP will likely be manageable, in our view. As a result, we do not expect the IMF to revise down its global growth forecast of 3.9% for 2018 significantly.

US-China trade war: Exposure mainly on Msia's E&E value chain



Source: Oxford Economics, OECD, RHB



Source: Oxford Economics, OECD, RHB

- ◆ US President Trump plans to impose 25% duties on up to USD50bn of Chinese products such as aerospace, information and communication technology and machinery. Impact will likely be manageable (accounts for 2.2% of China's exports).
- ◆ China's also announces plans for reciprocal tariffs on USD50bn of imports from the US such as soybean, pork - or 3.2% of the US' total exports.
- ◆ The effect on ASEAN is likely to be through value chains – where it exports to China as an input in goods that are then exported to the world. Malaysia's exposure through China's supply chain is the largest in the region at about USD25bn or 11.4% of total exports - mainly through E&E sector.

Thank You

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