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ECONOMIC/THEMATIC RESEARCH:

IMPACT OF THE MIDDLE EAST CONFLICT

Prepared by:
Lynette Lee
Mazlina Abdul Rahman
Syed Mohamad Bukhari Syed Bakeri

SMEBank-EconomicResearch@smebank.com.my
(603) 2615 2020

An agency under
MINISTRY OF ENTREPRENEUR AND COOPERATIVES DEVELOPMENT
MALAYSIA MADANI

Thematic: Minimal impact from the Middle East conflict thus far (1/5)

Timeline:

Oct 7, 2023 ←>100 Days→ Current

Oct 7
- Hamas Attack
- Operation Iron Sword by Israel

Nov 3
- Hezbollah Chief threatened to escalate the conflict.

Nov 19
- Galaxy Leader ship was **hijacked** by Houthis in the **Red Sea.**

Dec 9
- Houthis warned shipping companies against cooperating with Israel

Dec 16
- World largest shipping Company, **MSC** announced that it no longer operates via the Red sea.

Dec 18
- **Operation Prosperity Guardian** (US, UK, Canada, France, Italy, Netherland, Spain & Bahrain)

Dec 24
- **Maersk** will resume its operation backed by the Operation Prosperity Guardian

Jan 1
- Iran deployed warship in response to the 10 death of Houthis Fighters

Jan 5
- Maersk will avoid sailing through Red sea & Gulf Aden for foreseeable future

Jan 7
- **Iraq** launched attack on the Israeli base & US forces in **Syria**

Jan 12
- **UK & US** conducted airstrike at >12 Houthis' sites in **Yemen**

Jan 16
- **Iran** launched missile strikes in **Iraq** &**Syria**, citing security threats

Jan 17
- Iran carried strikes on terrorist in Pakistan territory

Jan 18
- **US** launched another airstrike on the Houthis in Yemen
- Pakistan retaliated against Iran

Jan 20
- The Islamic Resistance in **Iraq** carried a missile attack on **US forces** in Al-Asad Airbase

Jan 22
- **US, UK & other allies** carried combined strike on Houthis military target.

Feb 2
- **US** carried out a series of strikes in **Iraq & Syria targeting Iran proxies.**

Feb 12
- **Israel warplanes** are bombing Rafah, near the Egyptian border.

Key risks emerging from the conflict:

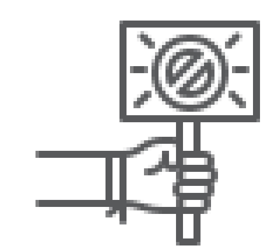
1 Renewed Inflation Shock

Business costs (e.g. shipping, insurance premium) are rising following Red Sea attacks

2 Wider War & Sanctions

Involvement of oil producing countries and beyond may lead to economic sanctions

3 Ripple Effect of Boycotts



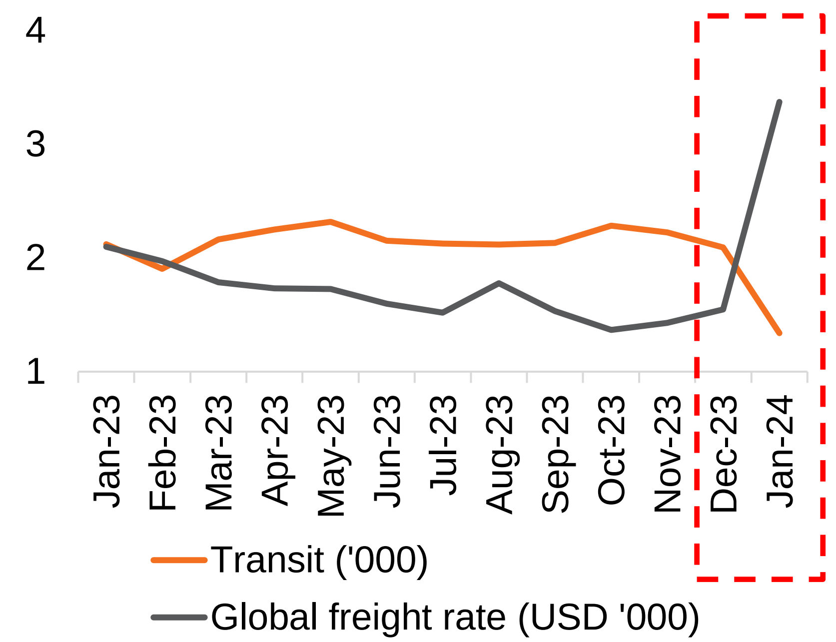
May affect business sentiment and related decisions (e.g. expansion, hiring)

Sources: Bloomberg, Al Jazeera, Middle East Eye, Reuters, and SME Bank Economic Research

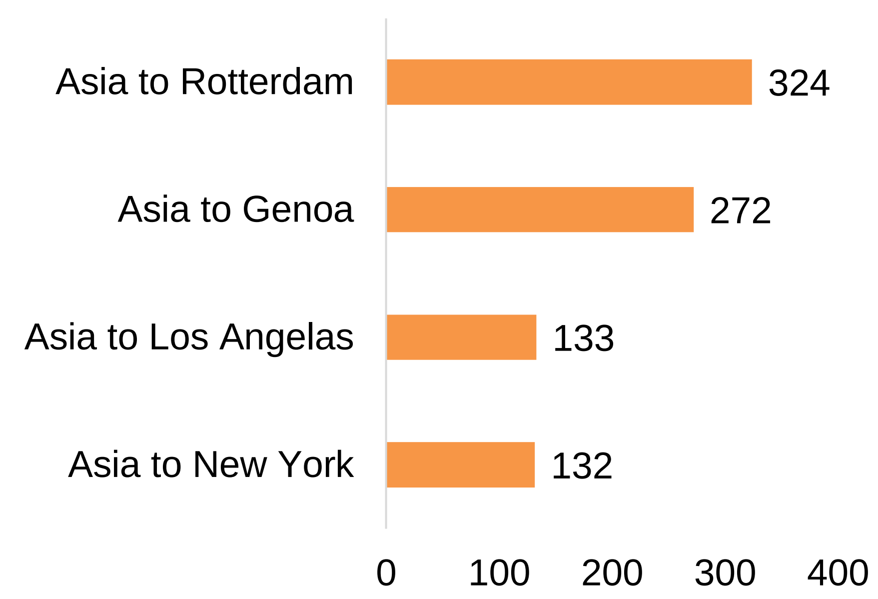
Thematic: Minimal impact from the Middle East conflict thus far (2/5)

Renewed Inflation Shock

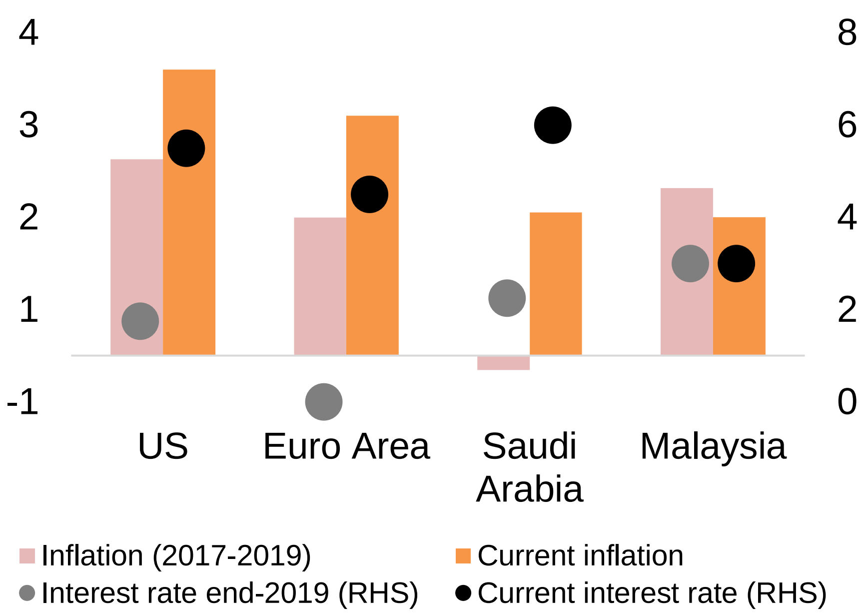
Transit in Suez Canal vs Global freight rate



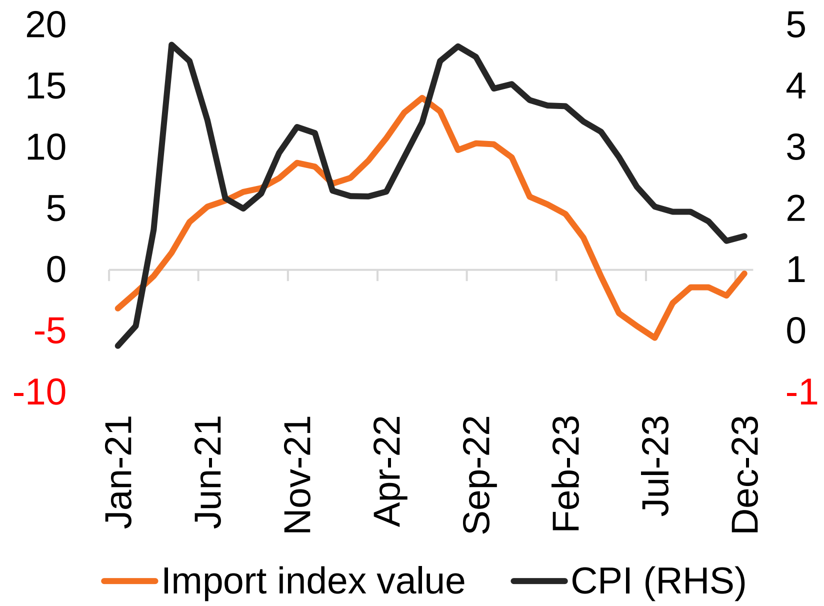
Freight rate in Oct-23 vs Feb-24 (% change)



Selected Countries' Inflation vs Interest Rate (%)



Malaysia Import Index vs CPI (% YoY)



1 Rising business costs are likely to be passed on to consumers…

- Red sea trade route – accounts 30% of global container shipping volumes – connecting Asia with the Europe via Suez Canal.
- Number of transit in Suez canal nosedived by -36% MoM in Jan 2024 (Dec: -6%), indicating **reroute from Red sea to alternative routes**: 1) sailing via Cape of Good Hope; 2) bypass via land (Dubai - Saudi ports); 3) air freight
- **Freight rate and insurance premium are increasing**:
  - ➢ Global freight rate spiked by 87.7% YoY to USD3.7k in Feb (Jan: USD3.4k; 2019: USD1.4k), the fastest rise since Covid's time (peak of USD9.6k or 328% YoY in 3Q 2021).
  - ➢ Insurance premiums have also risen to currently around 0.5-0.7% of the ship value, from 0.07% in Dec-23.

2 … may reverse global inflation trend and cause interest rate to remain high for longer.

- Countries are mostly on standby to start reducing their interest rates (after a series of hike previously) following a downtrend in inflation.
- Rising costs from the middle east crisis on top of other long-standing conflicts (e.g. Russia-Ukraine war; US-China trade war) are **feared to reverse the downtrend in inflation, causing interest rate to stay high for longer period.**
- For Malaysia, there is a **strong positive correlation** between import price index and headline consumer price index (CPI) – hence any **increase in import prices may push inflation rate up.**
- Nonetheless, according to Goldman Sachs, transportation costs including sea freight account for a trivial share (avg. ~1.5%) of overall cost of goods – hence impact to inflation could be limited.

Sources: DOSM, CEIC, Bloomberg, UNCTAD, Suez Canal Authorities (SCA), Sea Rates DP World, Goldman Sachs, CNA and SME Bank Economic Research

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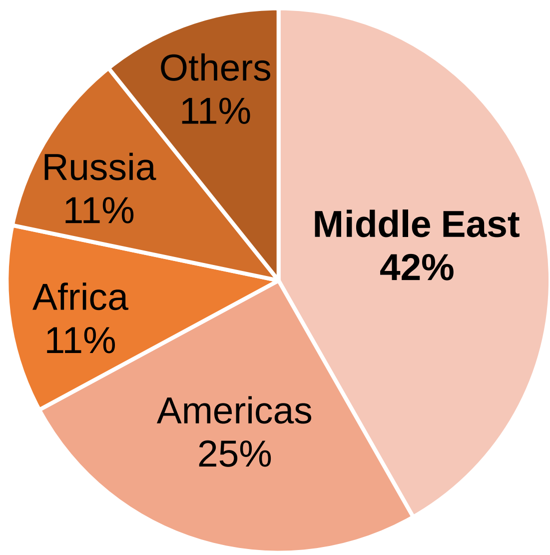
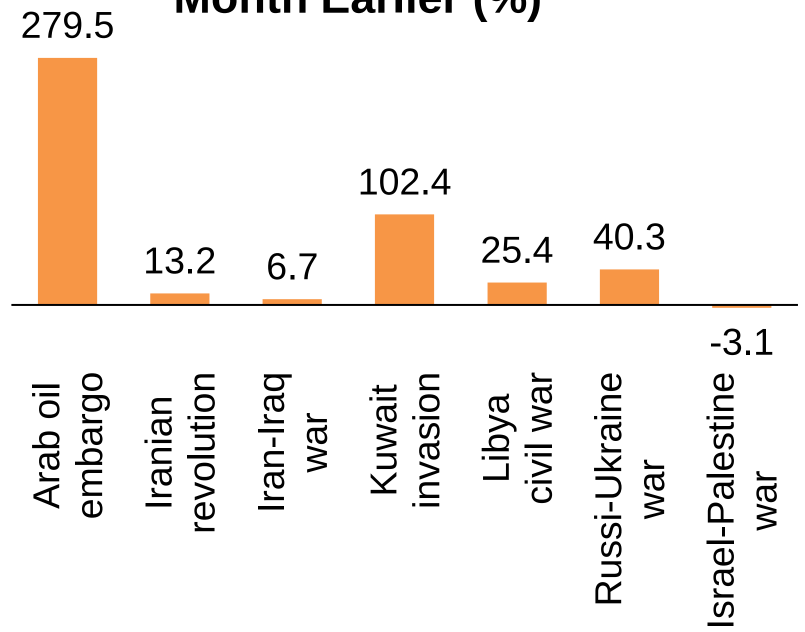
Wider War & Sanctions

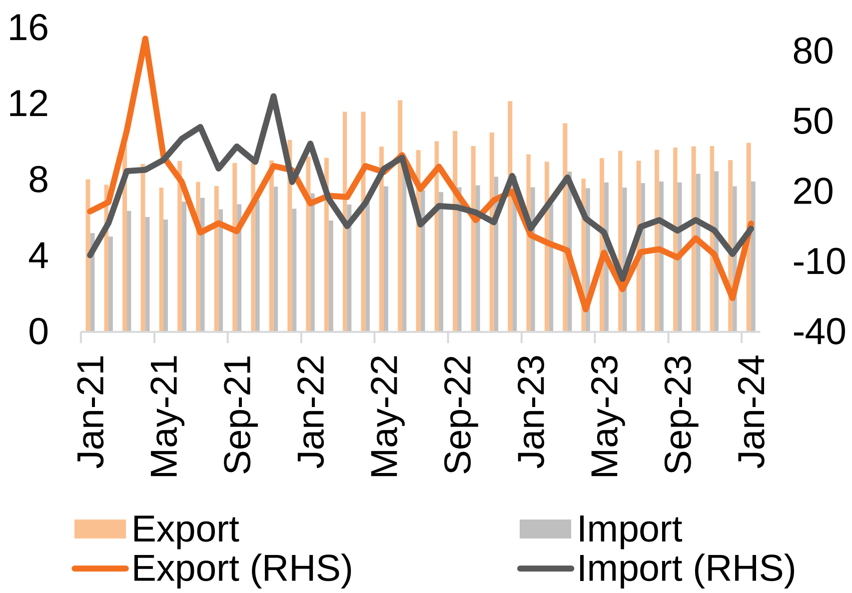
Global oil exporters (% of share)



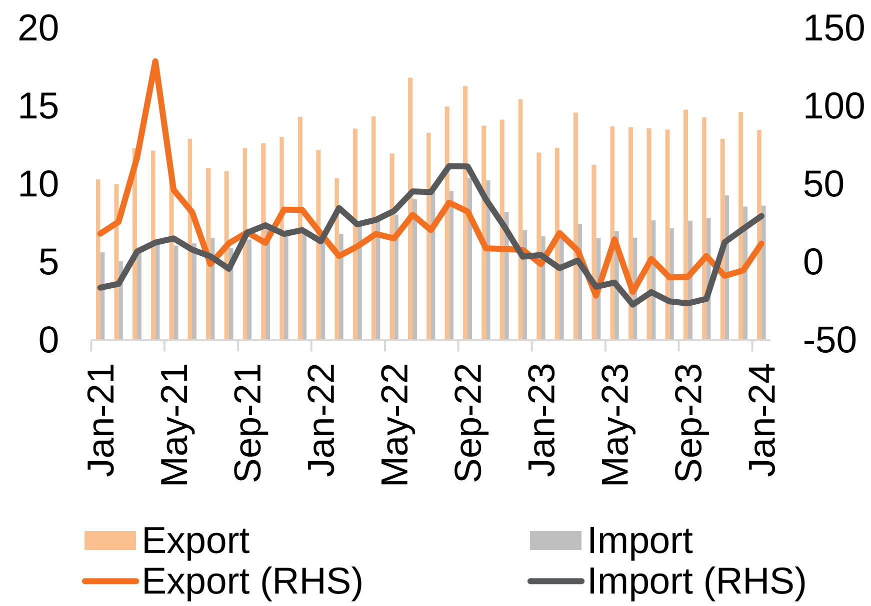
Oil Price Changes: Peak vs Month Earlier (%)



Malaysia's external trade with EU



Malaysia's external trade with the US



1 Direct involvement/ sanction by oil producing countries may have more catastrophic impact

- Middle East is the biggest oil's supplier, suppling 42% of crude oil to the world, followed by Americas (25%).
- Any significant development of the war e.g. **joint war or economic sanctions**, involving these suppliers will have **major impact to the price and supply of oil.**
- Historically, oil price shot up by 279% to the peak from a month earlier during Arab oil embargo in Oct 1973.
- However, during the Israel-Palestine war, the peak of **oil price is down** by -3% from a month before the event as there are 1) no disruption in oil production; 2) no direct involvement of major oil producing countries; 3) availability of alternative routes for shipping

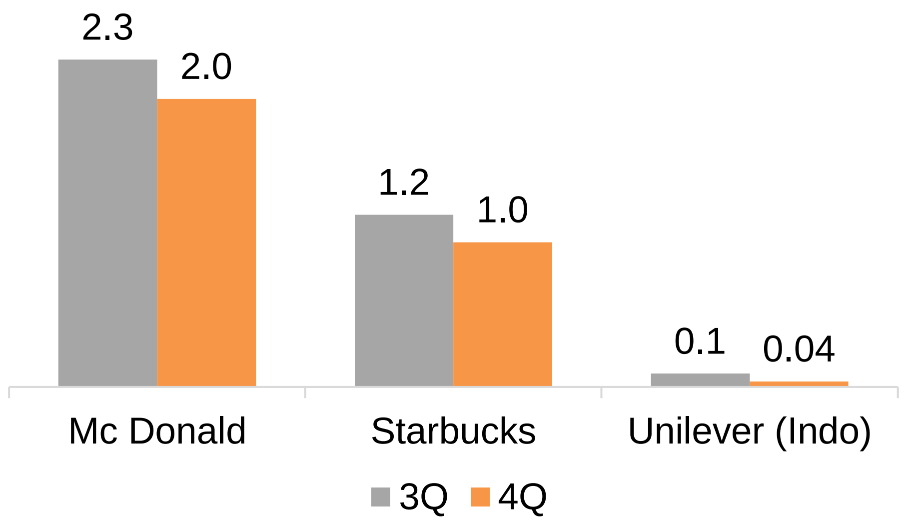
2 Direct and indirect impact to Malaysia's trade have been minimal thus far

- Taking cue from Suez Canal blockage that happened for 6-7 days in Mar 2021, Malaysia's total exports and imports were unaffected.
- This could be due to **Malaysia's exports to Europe** (likely pass through Suez Canal) only formed **circa 8% of total exports**.
- Although Red Sea crisis is lasting longer, attacks have been **selective,** and **ships can still pass through**.
- So far, **no significant impact** to Malaysia's exports (Jan 2024: 6.4% YoY) and imports (4.1% YoY) to/from Europe.
- On the other hand, Malaysia received several notices from the US over our stance on Middle East war, but this has **not resulted in any economic sanction** by the US, as reflected in the robust performance of exports and imports to/from the US in Jan 2024.

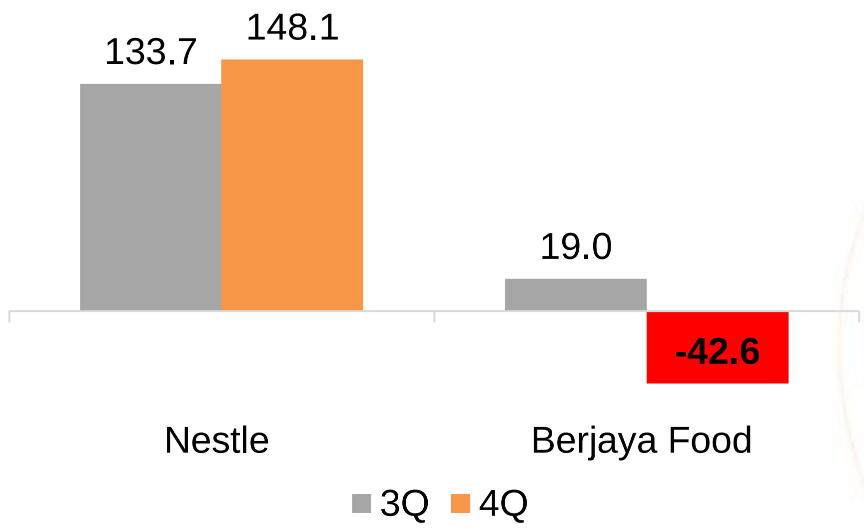
Sources: DOSM, CEIC, Bloomberg, CGS-CIMB, OPEC and SME Bank Economic Research

Ripple Effect of Boycotts

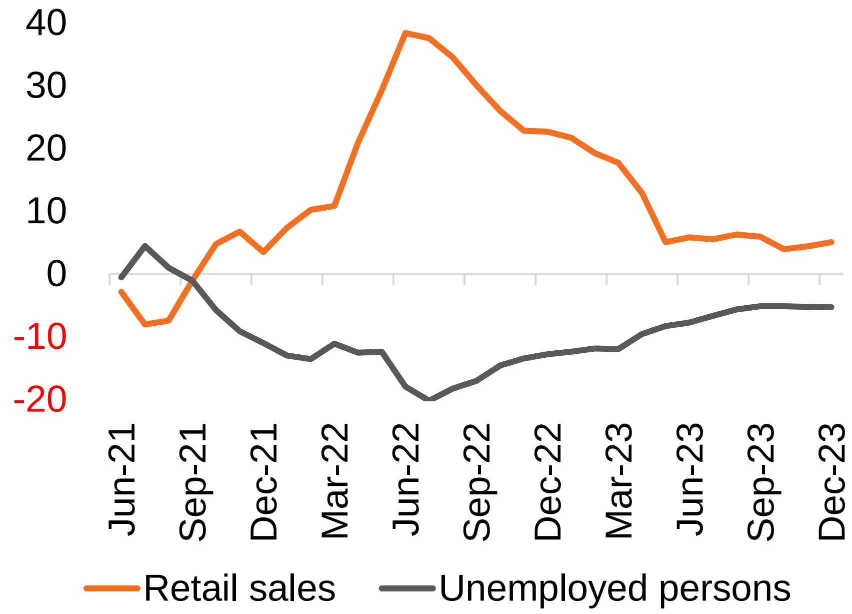
Net profit of selected brands listed in foreign countries 2023 (USD bil)



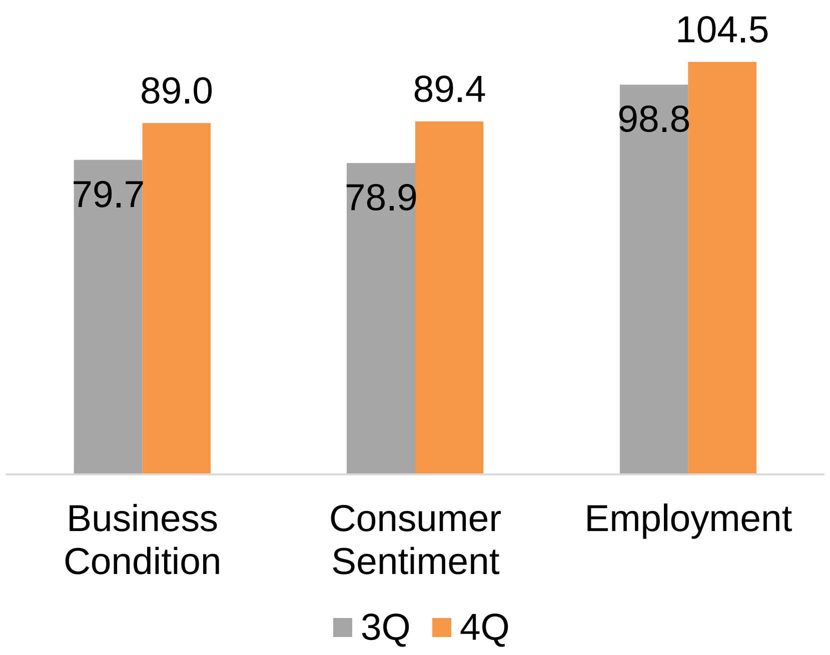
Net profit/loss of selected brands listed domestically (RM mil)



Retail sales and Unemployed persons (% YoY)



MIER Business Index 2023



1 Boycott campaigns hit certain Western brand…

- Major Western brands listed outside Malaysia such as Mc Donald, Starbucks and Unilever (Indo) have posted decline in net profit as **Middle East conflict weighs on quarterly sales**.
- Starbucks even cut its full-year comparable sales growth forecast to 4% - 6% range (previously: 5% - 7%).
- For companies listed in Malaysia, significant impact was seen for Berjaya Food (owner of Starbucks Malaysia) - **loss of RM43 mil** in 4Q 2023, a **324% QoQ plunge.**
- Nonetheless, Nestle which was also on the boycott list still managed to record improvement in its net profit in 4Q 2023, probably due to the nature of its diversified products (mostly essential and for daily intake).

2 …but performance of Malaysia's macroeconomic variables remain intact.

- A business's loss is another business's gain – boycotts have **no adverse impact on consumption so far** as consumers continue to consume but only **shifted their brand preference**.
- Retail sales remain solid with 5% YoY growth in Dec-23. It also expanded on MoM basis by 1.8% – the highest growth since Apr.
- Moreover, unemployment continued declining, suggesting **that job loss if any**, resulting from decline in sales of boycotted companies are **minimal or quickly replaced** by opportunities in other companies.
- Sentiments especially of business conditions seem to be also unaffected as reflected by improvement in all segment of Malaysian Institute of Economic Research (MIER)'s indices in 4Q 2023.

Sources: DOSM, CEIC, Bloomberg, Bursa Malaysia, and SME Bank Economic Research

Ripple Effect of Boycotts

3 Boycott of Western brands may benefit rival local MSMEs.

- For instance, Malaysian coffee chains are experiencing a surge in popularity as consumers boycott US brands like Starbucks in response to the Israel-Gaza conflict.
- Newspapers reported that local coffee shops like ZUS, Eight Ounce, Gigi, and Mukarami have seen **significant sales increases**, ranging from 15% to 30%.
- This temporary shift in consumers' spending **may turn into a long-term preference** if MSMEs seize the opportunity well and capable of retaining their customers.
- However, MSMEs who are **involved in the supply chain** (e.g. supplier/vendor) of the boycotted brands/ franchise may **face some challenges** if their customer-base are not diversified enough.

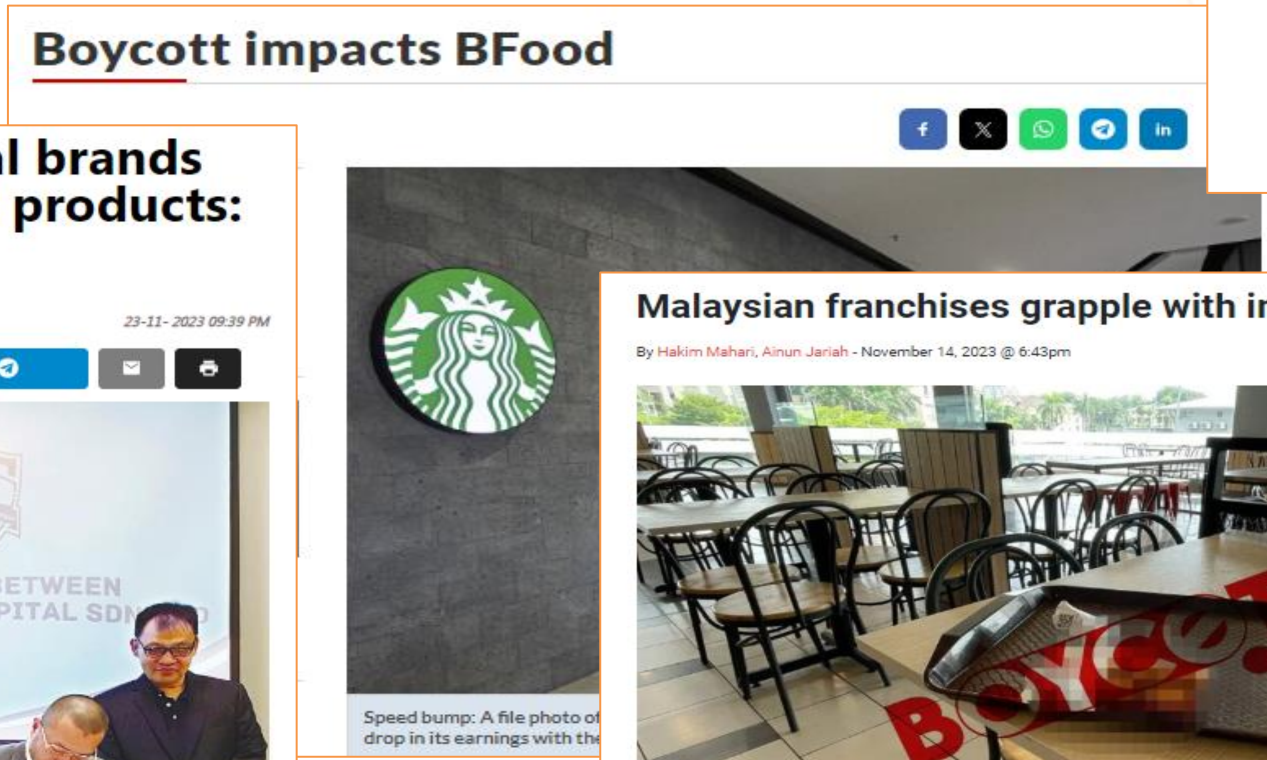

Boycott boost: Malaysian coffee chains gain as locals shun US brands over Gaza war

Published Mon, Feb 05, 2024 · 7:45 am

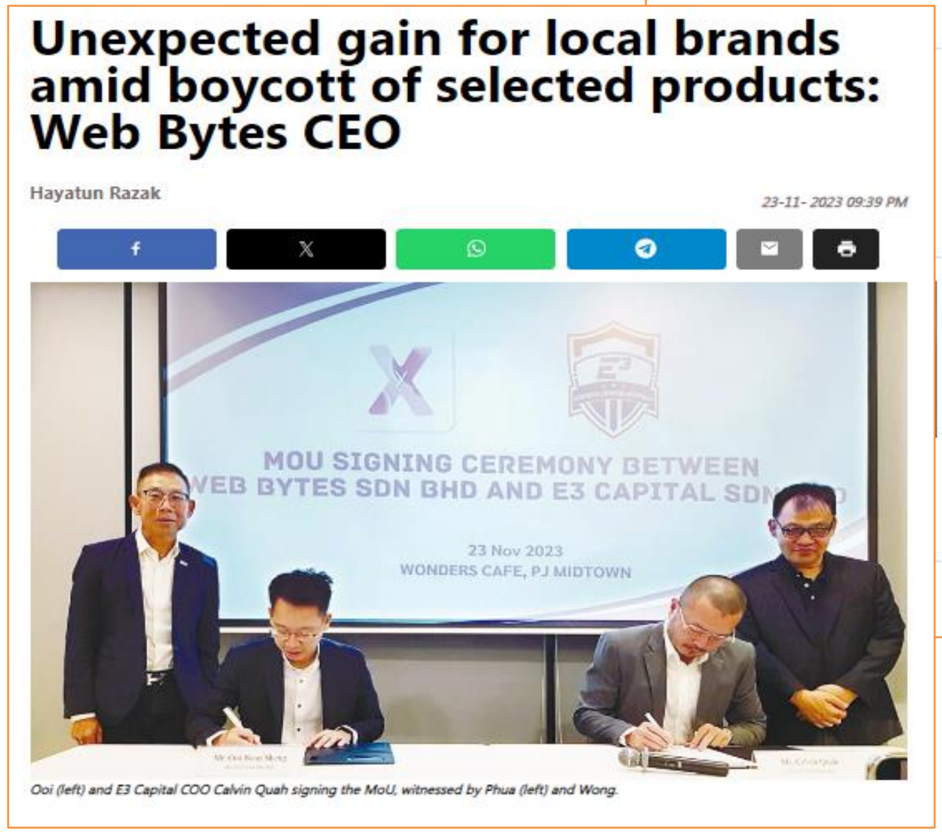

Spike in revenue for local coffee brands

By Ainun Jariah, Hakim Mahari - November 16, 2023 @ 7:21am

...ore of Gigi Coffee, a local brand, at Pavilion Kuala Lumpur, yesterday. Local coffee franchisees ... to 30 per cent as a result of the boycott on brands with Israel links. - NSTP/ASWADI ALIAS


Boycott impacts BFood

Speed bump: A file photo of ... drop in its earnings with the ...


Unexpected gain for local brands amid boycott of selected products: Web Bytes CEO

Hayatun Razak

23-11-2023 09:39 PM

Ooi (left) and E3 Capital COO Calvin Quah signing the MoU, witnessed by Phua (left) and Wong.


Malaysian franchises grapple with impact of boycott

By Hakim Mahari, Ainun Jariah - November 14, 2023 @ 6:43pm

NSTP FILE PIC, FOR ILLUSTRATION PURPOSE ONLY.

Sources: The Sun, The Strait Times, and New Strait Times and SME Bank Economic Research

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Small Medium Enterprise Development Bank Malaysia Berhad 49572-H
Menara SME Bank, Jalan Sultan Ismail, 50250 Kuala Lumpur
Tel: 03-2615 2020 **Fax:** 03-2698 1748

www.smebank.com.my
smebankmalaysia
smebankmalaysia
@SME Bank
smebank_malaysia
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