

ECONOMIC REVIEW | July 2019 BNM MPC**BNM Holds Rate at 3% amid Low Inflationary Pressure and Stable Labour Market**

- *Overnight Policy Rate maintained at 3%. In line with our expectation, the overnight policy rate was left unchanged at 3% by BNM.*
- *Better outlook for 2Q19 and 2H19. Exports growth for 1Q19 averaged at -0.9%yoy. However, looking ahead to the 2Q19, we expect exports to register positive growth. Exports growth for the first two months of 2Q19 averaged at 1.8%yoy. Steady economic performances in the two largest economies in the world on top of Ringgit depreciation are expected to provide support to Malaysia's export performance.*
- *OPR to stay at 3.00% for the remaining of year 2019. The 25 basis point cut in May-19 is sufficient to boost economic growth particularly domestic demand. As long as GDP growth is more than 4% and core CPI still positive, we opine no further change in monetary stance is required at this juncture. In addition, the Fed has signaled possible rate cut by at least once this year. Since there will be less pressure from both domestic and external fronts, we anticipate that Bank Negara will maintain the OPR at 3.00% rest of 2019.*

Overnight Policy Rate maintained at 3%. In line with our expectation, the overnight policy rate was left unchanged at 3% by BNM. On external front, Malaysia's external trade performance is recovering as both exports and imports have been growing positively in the latest two months. Fears from US-China trade discord are comforted temporarily as the duo agreed to resume the trade talks from where they left. Domestically, distributive sales continued to expand but at a moderating pace. Nevertheless, economic activities remain solid as current jobless rate still reflects full-employment condition and inflationary pressure stays at low level due to lower retail fuel prices. In addition, the rate cut in May-19 would improve both domestic consumption activities and investment particularly in 2H19. The strong momentum in private consumption and services sector will drive Malaysia's economy into a good position in 2019. Furthermore, leading indicators such as leading index and business tendency survey are pointing towards better growth trajectory in 2H19. We foresee the economy to expand by 4.9% in 2019.

Continuous positive momentum in exports. Exports growth doubled to 2.5%yoy in May-19 from 1.1%yoy in Apr-19, continuing the gradual recovery since Mar-19. In contrast, imports expanded at a softer pace of 1.4%yoy (Apr-19: 4.4%yoy). Hence, trade surplus widened to RM 9.1b (May-18: RM 8.1b) but narrowed compared to last month. Sector wise, manufacturing exports (84.2% share) advanced at a higher rate of 3.1%yoy (Apr-19: 2.7%yoy). Furthermore, agriculture exports (7.5% share) also rebounded sharply to a double digit positive growth of 15.3%yoy (Apr-19: -9.3%yoy). Meanwhile, mining goods exports (7.5% share) growth continued to be in negative territory of -10.9%yoy).

Domestic exports at high single digit growth. Domestic exports expanded by 8.8%yoy, however moderating from a double digit growth of 11.9%yoy in the prior month. Nevertheless, the sixth consecutive months of positive growth indicates a good momentum for this year and provides brighter outlook for GDP growth in 2Q19 as domestic exports involve high value-added activities. In contrast, re-exports which have low domestic value-added contracted for the fourth consecutive month at -23.1%yoy. Meanwhile, the ratio of re-exports to total exports was lower at 14.8%, indicating that for every RM1 value of exports, approximately 15sen of it is re-exports. Re-exports activities are expected to remain weak throughout the year mainly due to higher base effects as well as external headwinds.

Better outlook for 2Q19 and 2H19. Exports growth for 1Q19 averaged at -0.9%yoy. However, looking ahead to the 2Q19, we expect exports to register positive growth. Exports growth for the first two months of 2Q19 averaged at 1.8%yoy. Steady economic performances in the two largest economies in the world on top of Ringgit depreciation are expected to provide support to Malaysia's export performance. Based on our regional partners' trade performance in June-19, Vietnam's exports grew 8.5%yoy while South Korea's shrunk -13.5%yoy. This could provide cues on what to expect from Malaysia's exports in upcoming month. In regards to manufacturing condition and activity, both global and emerging economies manufacturing PMI fell below 50 points. However, we believe it will return to expansionary mode in upcoming months as US-China trade crusade has been put on hold. We forecast exports and imports to increase by 3.6% and 3.0% respectively in 2019.

Low inflationary pressure. We foresee headline inflation rate to average at 0.6%yoy this year, lower than 1%yoy in 2018. Initially, food inflation was expected to provide upside pressures to the overall inflation due to the spillover effects from the SST and imported inflation as Malaysia is a net importer of food. In addition, transport inflation was anticipated to recover significantly in the 2H19 due to rising global crude oil prices, more targeted domestic petrol subsidy and removal of the RON95 price cap. However, we note that the developments in these areas have been muted. Even with the removal of RON95 price cap, the prices are expected to be on the low side in line with declining global crude oil prices which are affected by the ballooning trade tensions, among others. We anticipate inflationary pressure mainly from fuel-related items to remain weak in line with our expectation of Brent crude oil price at \$70pb for 2019 (2018: \$71.6pb).


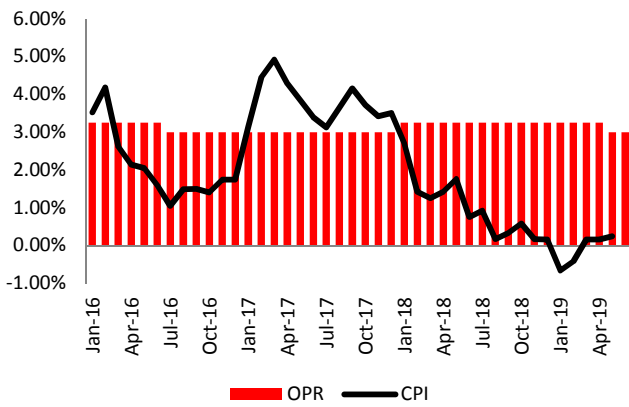
OPR to stay at 3.00% for the remaining of year 2019. The 25 basis point cut in May-19 is sufficient to boost economic growth particularly domestic demand. As long as GDP growth is more than 4% and core CPI still positive, we opine no further change in monetary stance is required at this juncture. In addition, the Fed has signalled possible rate cut by at least once this year. Since there will be less pressure from both domestic and external fronts, we anticipate that Bank Negara will maintain the OPR at 3.00% rest of 2019. 

Table 1: Central Bank Policy Rate (%) by Selected Countries

| | Oct-18 | Nov-18 | Dec-18 | Jan-19 | Feb-19 | Mar-19 | Apr-19 | May-19 | June-19 |
|----------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|----------------|
| Malaysia | 3.25 | 3.25 | 3.25 | 3.25 | 3.25 | 3.25 | 3.25 | 3.00 | 3.00 |
| Indonesia | 5.75 | 6.00 | 6.00 | 6.00 | 6.00 | 6.00 | 6.00 | 6.00 | 6.00 |
| Singapore | Neut. | Neut. | Neut. | Neut. | Neut. | Neut. | Neut. | Neut. | Neut. |
| Philippines | 4.50 | 4.50 | 4.75 | 4.75 | 4.75 | 4.75 | 4.75 | 4.50 | 4.50 |
| Thailand | 1.50 | 1.50 | 1.50 | 1.75 | 1.75 | 1.75 | 1.75 | 1.75 | 1.75 |
| Vietnam | 6.25 | 6.25 | 6.25 | 6.25 | 6.25 | 6.25 | 6.25 | 6.25 | 6.25 |
| Korea | 1.50 | 1.75 | 1.75 | 1.75 | 1.75 | 1.75 | 1.75 | 1.75 | 1.75 |
| China | 4.35 | 4.35 | 4.35 | 4.35 | 4.35 | 4.35 | 4.35 | 4.35 | 4.35 |
| Japan | -0.10 | -0.10 | -0.10 | -0.10 | -0.10 | -0.10 | -0.10 | -0.10 | -0.10 |
| United Kingdom | 0.75 | 0.75 | 0.75 | 0.75 | 0.75 | 0.75 | 0.75 | 0.75 | 0.75 |
| EU | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| United States | 2.25 | 2.25 | 2.50 | 2.50 | 2.50 | 2.50 | 2.50 | 2.50 | 2.50 |

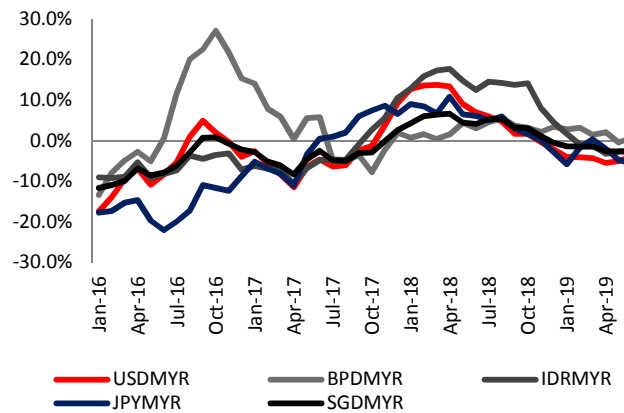
Source: CEIC, MIDFR

Chart 1: Monetary Policy (%) vs CPI (YoY%)



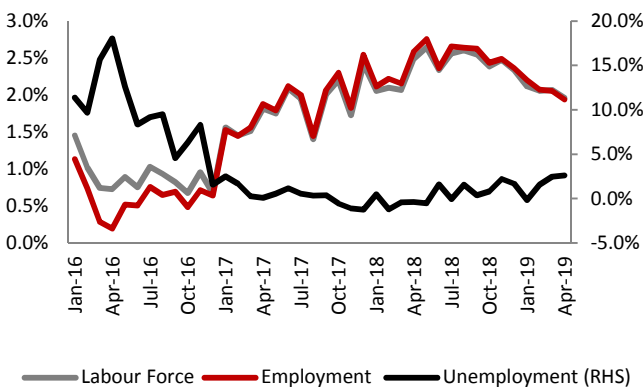
Source: CEIC, MIDFR

Chart 2: MYR Against Selected Currencies (YoY%)



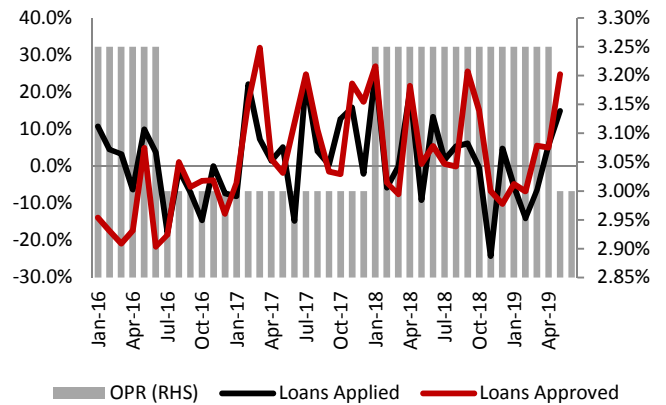
Source: CEIC, MIDFR

Chart 3: Labour Market Performance (YoY%)



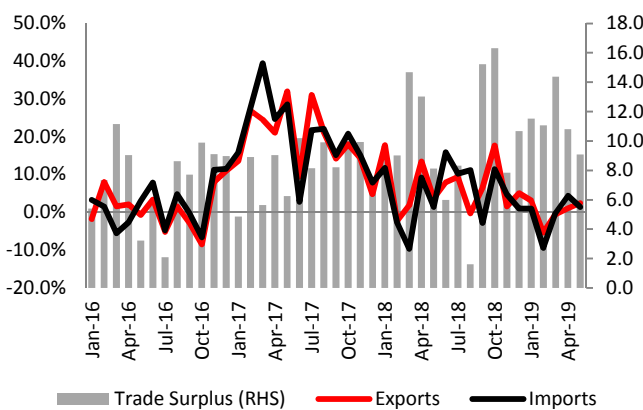
Source: CEIC, MIDFR

Chart 4: OPR (%) vs Loans Growth (YoY%)



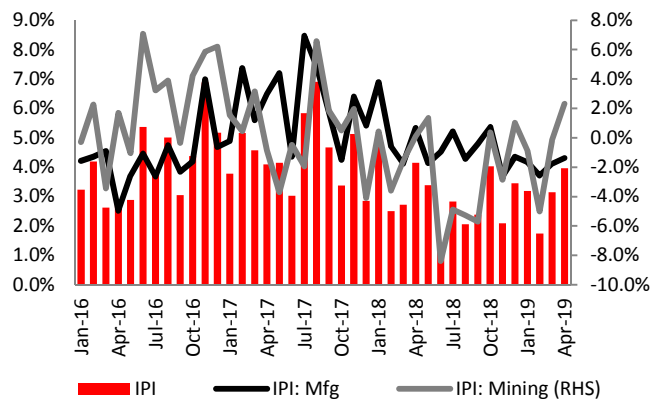
Source: CEIC, MIDFR

Chart 5: External Trade Performance (YoY% & RMB)



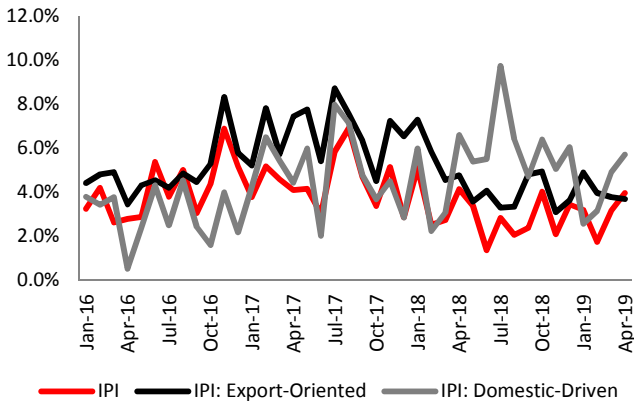
Source: CEIC, MIDFR

Chart 6: Industrial Productions Performance (YoY%)



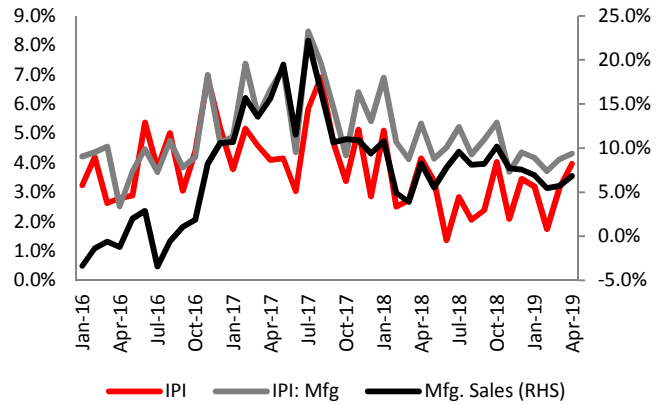
Source: CEIC, MIDFR

Chart 7: IPI Performance (YoY%)



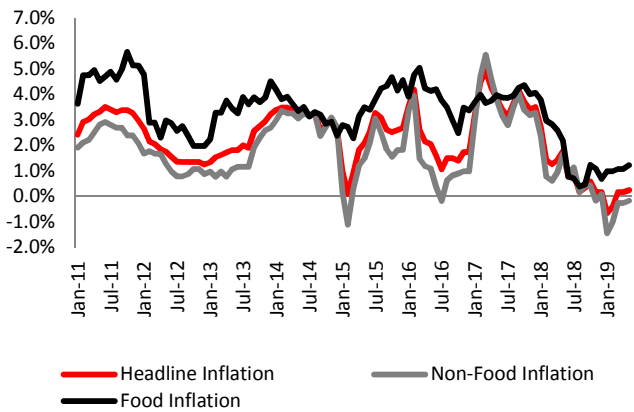
Source: CEIC, MIDFR

Chart 8: IPI vs Manufacturing Performances (YoY%)



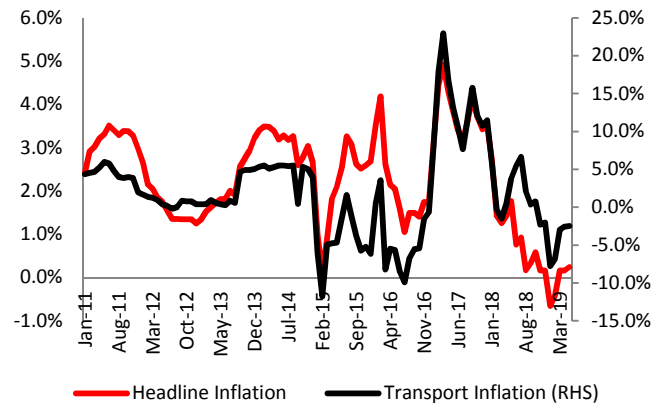
Source: CEIC, MIDFR

Chart 9: Headline vs Food & Non Food Inflation (YoY%)



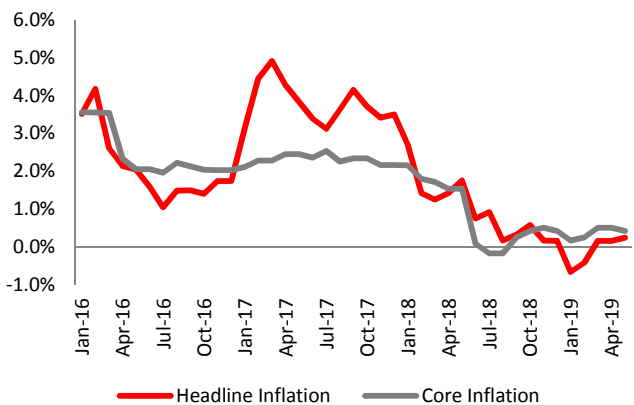
Source: CEIC, MIDFR

Chart 10: Headline vs Transport Inflation (YoY%)



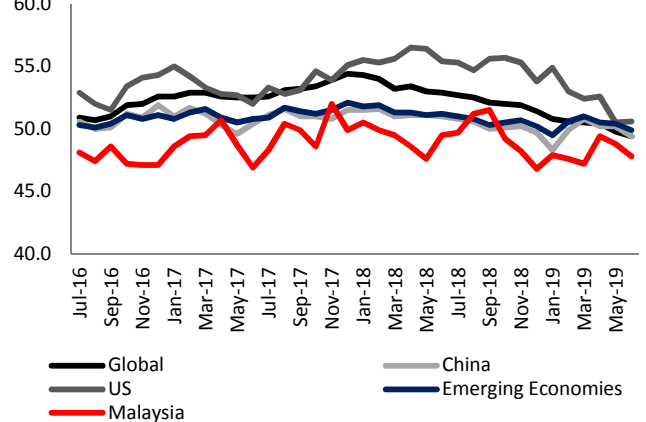
Source: CEIC, MIDFR

Chart 11: Headline vs Core Inflation (YoY%)



Source: BLOOMBERG, MIDFR

Chart 12: Manufacturing PMI (Points)



Source: CEIC, MIDFR
 *(>50:Expansionary, <50: Contractionary)

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