

ECONOMIC REVIEW | September 2019 BNM MPC**BNM Maintains Rate at 3% amid Solid Economic Growth and Benign Inflation**

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- *2Q19 GDP highest in 5-quarter. Malaysia's GDP growth expanded 4.9%yoy in 2Q19, marginally above market expectations and our forecast of 4.7%yoy and 4.8%yoy respectively. The strong pick-up in the economy is generally driven by continuous strong private consumption and recovery in commodity-based sectors.*
- *OPR to stay at 3.00% for the remaining of year 2019. The 25bp cut in May-19 is sufficient to boost economic growth particularly domestic demand. As long as major macroeconomic indicators especially GDP growth remain stable and above 4% besides gradual increase in core inflation, we opine no further change in monetary stance is required at this juncture.*

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 gradually recovering as exports growth returned to positive territory but imports remained in negative hence widening the trade surplus. Concerns over US-China trade crusade remain but comforted temporarily as the duo delayed their latest round of tariff hikes. Domestically, distributive sales continued to expand but at a slightly moderating pace. Nevertheless, economic activities remain solid as current unemployment rate still reflects full-employment condition and inflationary pressure remain benign due to lower retail fuel prices. In addition, the rate cut in May-19 would support 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.

2Q19 GDP highest in 5-quarter. Malaysia's GDP growth expanded 4.9%yoy in 2Q19, marginally above market expectations and our forecast of 4.7%yoy and 4.8%yoy respectively. The strong pick-up in the economy is generally driven by continuous strong private consumption and recovery in commodity-based sectors. From expenditure side, private consumption and net exports contributed by 4.4% and 1.4% respectively. From supply side, services, mining and agriculture sectors contributed by 3.6%, 0.2% and 0.3% respectively during the quarter. External front remains weak due to global trade wars and decline in business optimism. On the other hand, domestic demand stays solid underpin by lower interest rate, stable labor market and low inflationary pressure.

Exports return to positive territory. Exports rebounded in July-19 by 1.7%yoy from -3.1%yoy growth registered in the previous month. Meanwhile, imports continued to decline however at an improving rate of -5.9%yoy (June-19: -9.2%yoy). As a result of positive exports and negative imports, trade surplus hit four-month high at RM 14.3b. Sector wise, manufacturing exports which accounted for more than 80% of total exports rebounded by 3.8%yoy (June-19: -5%yoy). In contrast, mining and agriculture exports contracted by -11.6%yoy and -9.3%yoy respectively.

Robust domestic exports. Domestic exports expanded by 3.3%yoy, higher than 1.7%yoy gain in the previous month. The eighth consecutive months of positive growth indicate a good momentum for this year and provide brighter outlook for GDP growth in 3Q19 as domestic exports involve high value-added activities. In contrast, re-exports which have low domestic value-added contracted for the sixth consecutive month but at a far improving rate of -3.9%yoy (June-19: -22.3%yoy). Hence, the ratio of re-exports to total exports recorded higher at six-month high of 20.3% (for every RM1 value of exports, approximately 20sen of it is re-exports). Re-exports activities are expected to remain weak throughout the year mainly due to higher base effects besides external headwinds.

Cloudy outlook for 3Q19. Exports for 1H19 registered marginal negative growth of -0.2%yoy. Looking ahead to the 3Q19, exports performance is expected to be quite vulnerable especially with the latest round of tit-for-tat tariffs between the US and China. With the new tariffs in place, it could add more risks to the global economy including Malaysia due to the supply chain factor. E&E sector is likely to be impacted the most. Nevertheless, we expect commodity-based sector products particularly LNG exports to offset the less favourable impact from trade war. Based on our regional partners' trade performance in Aug-19, Vietnam's exports growth moderated to six-month low while South Korea's shrunk further by -13.6%yoy). This could provide cues on what to expect from Malaysia's exports in upcoming month. In regards to manufacturing condition and activity, global manufacturing PMI still positioned under 50 points while those of emerging economies continued to recover to 50.4 points.

Low inflationary pressure. We foresee headline inflation rate to average at 0.6%yoy this year, lower than 1%yoy in 2018. For the first seven months of this year, inflation averaged at 0.3%yoy. We expect food component to provide upside pressures for overall inflation in 2019 driven by low base effect, spill over effect from the SST and imported inflation as Malaysia is a net importer of food. Nevertheless, RON95 price cap will continue to provide downward pressure to the overall inflation. Even with the removal of RON95 price cap, the prices are expected to be on the low side in line with global crude oil prices which are affected by multiple headwinds. We anticipate inflationary pressure mainly from fuel-related items to remain weak in line with our expectation of Brent crude oil price at \$63pb for 2019 (2018: \$71.6pb).


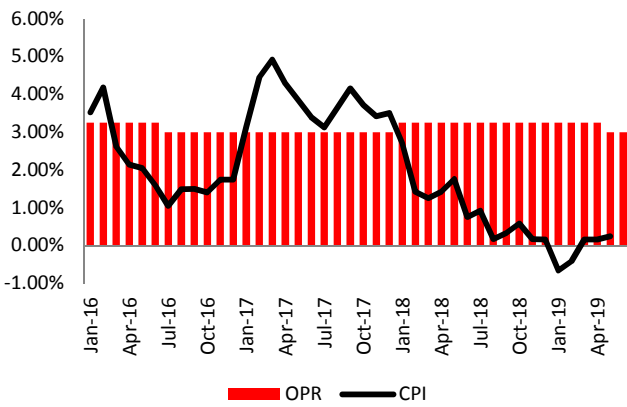
OPR to stay at 3.00% for the remaining of year 2019. The 25bp cut in May-19 is sufficient to boost economic growth particularly domestic demand. As long as major macroeconomic indicators especially GDP growth remains stable and above 4% besides gradual increase in core inflation, we opine no further change in monetary stance is required at this juncture. Besides that, the Fed has only reduced its key policy rate by 25bp so far. 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

| | Mar-19 | Apr-19 | May-19 | Mar-19 | Apr-19 | May-19 | Jun-19 | Jul-19 | Aug-19 |
|----------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| Malaysia | 3.25 | 3.25 | 3.00 | 3.25 | 3.25 | 3.00 | 3.00 | 3.00 | 3.00 |
| Indonesia | 6.00 | 6.00 | 6.00 | 6.00 | 6.00 | 6.00 | 6.00 | 6.00 | 5.50 |
| Singapore | Neut. | Neut. | Neut. | Neut. | Neut. | Neut. | Neut. | Neut. | Neut. |
| Philippines | 4.75 | 4.75 | 4.50 | 4.75 | 4.75 | 4.50 | 4.50 | 4.50 | 4.25 |
| Thailand | 1.75 | 1.75 | 1.75 | 1.75 | 1.75 | 1.75 | 1.75 | 1.75 | 1.50 |
| Vietnam | 6.25 | 6.25 | 6.25 | 6.25 | 6.25 | 6.25 | 6.25 | 6.25 | 6.25 |
| Korea | 1.75 | 1.75 | 1.75 | 1.75 | 1.75 | 1.75 | 1.75 | 1.75 | 1.50 |
| 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 | 2.25 | 2.25 | 2.25 | 2.25 | 2.25 | 2.25 | 2.25 |

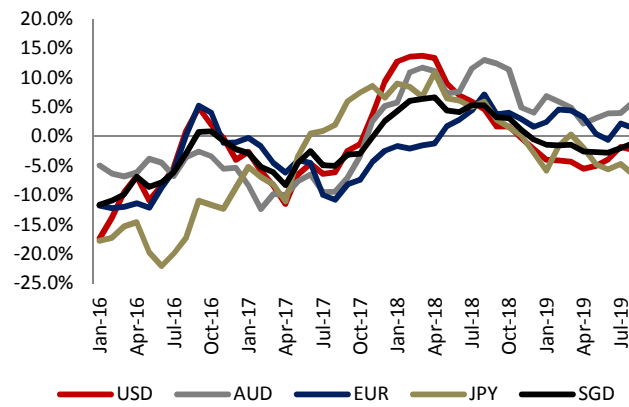
Source: CEIC, MIDFR

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



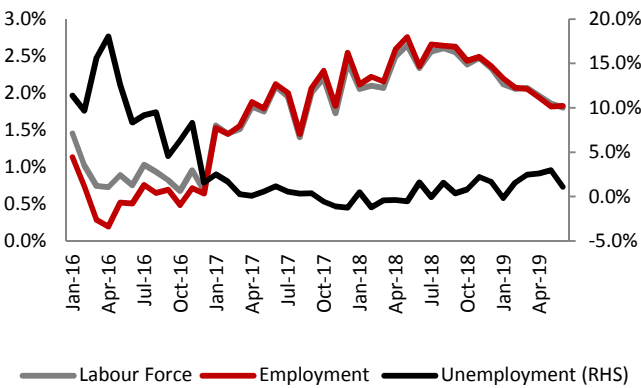
Source: CEIC, MIDFR

Chart 2: MYR Against Selected Currencies (YoY%)



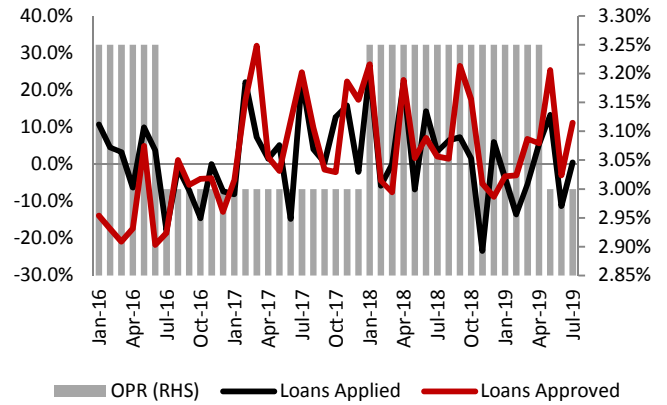
Source: CEIC, MIDFR

Chart 3: Labour Market Performance (YoY%)



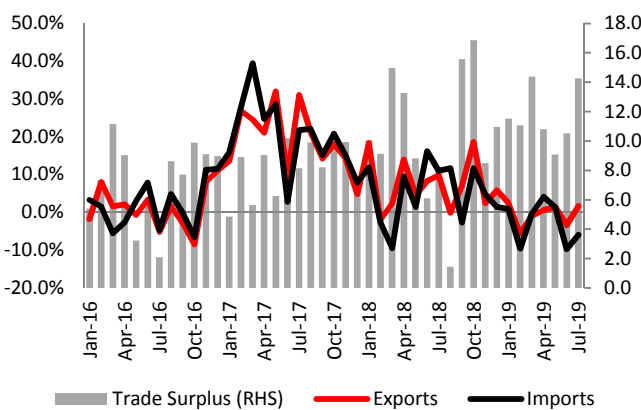
Source: CEIC, MIDFR

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



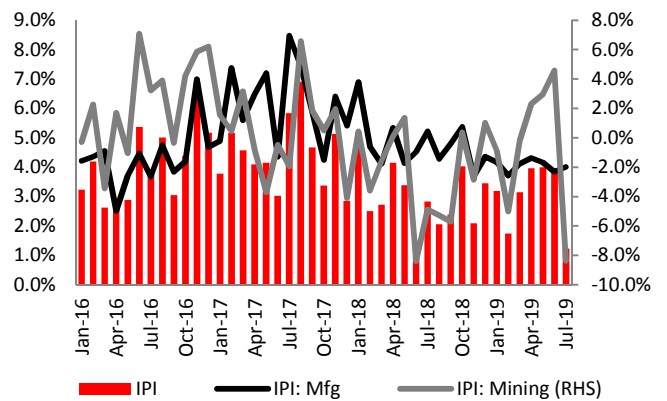
Source: CEIC, MIDFR

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



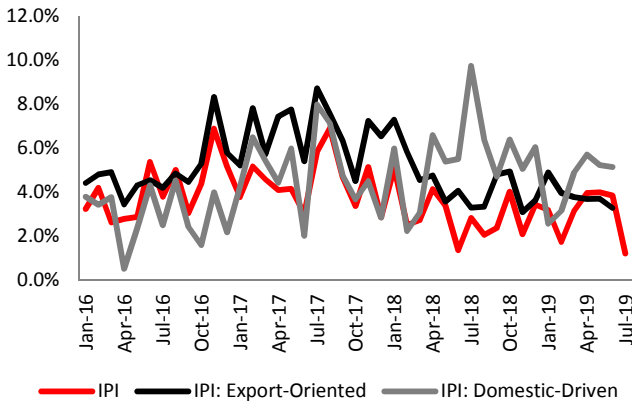
Source: CEIC, MIDFR

Chart 6: Industrial Productions Performance (YoY%)



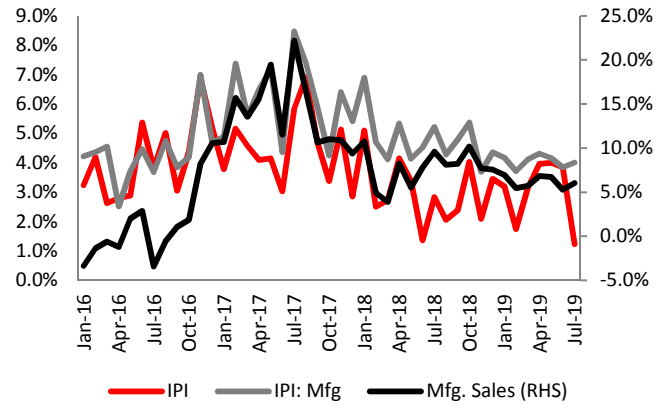
Source: CEIC, MIDFR

Chart 7: IPI Performance (YoY%)



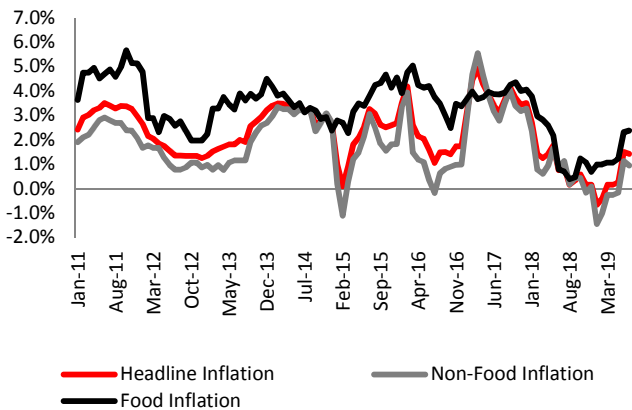
Source: CEIC, MIDFR

Chart 8: IPI vs Manufacturing Performances (YoY%)



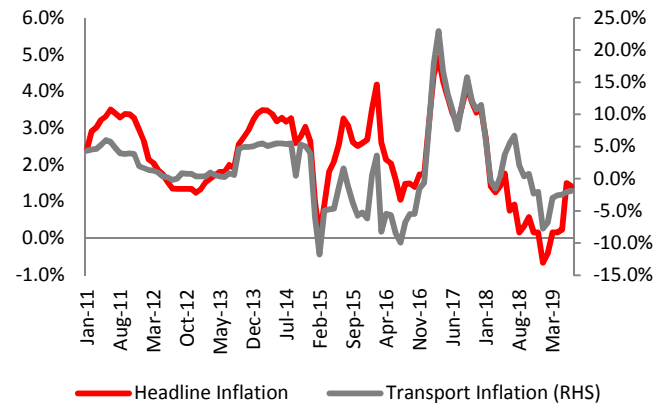
Source: CEIC, MIDFR

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



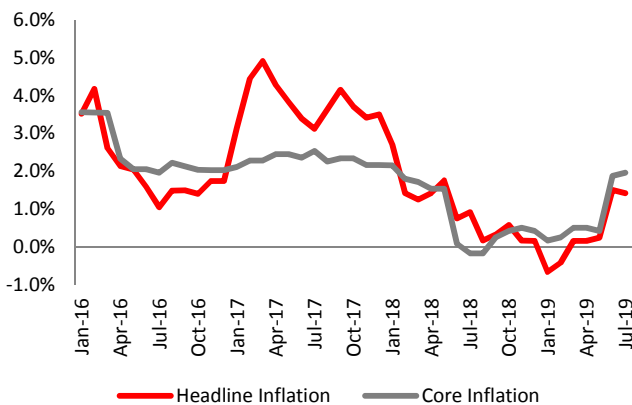
Source: CEIC, MIDFR

Chart 10: Headline vs Transport Inflation (YoY%)



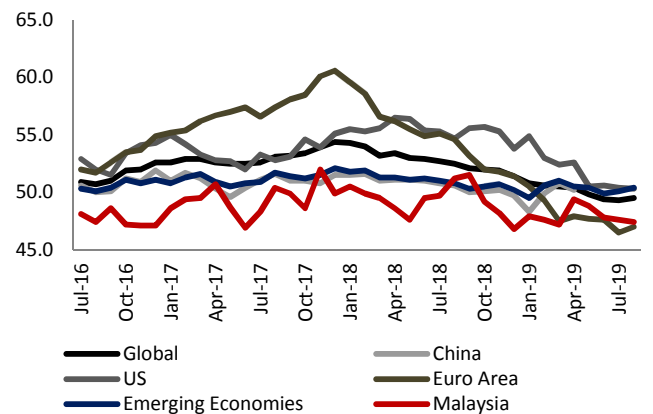
Source: CEIC, MIDFR

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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