09 May 2024

Global Economics & Market Strategy

Malaysia: Lack of Catalysts for OPR Adjustments in 2024

- **We maintain our view that Overnight Policy Rate (OPR) to remain unchanged at 3.00% for 2024.**
- **The key factors that the Monetary Policy Committee (MPC) might consider in the decision making will include (1) the economic momentum; (2) the inflation momentum and (3) future global economic and rates outlook.**
- **Bank Negara Malaysia (BNM) held its OPR at 3.00% in May's meeting, in line with our in-house view and market expectations.**

Economist

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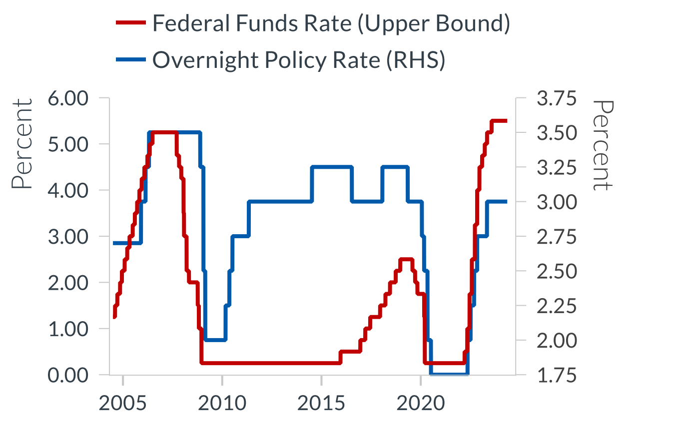
2024 Monetary Policy Committee's (MPC) meeting schedule

1st	23 and 24 January 2024
2nd	6 and 7 March 2024
3rd	8 and 9 May 2024
4th	10 and 11 July 2024
5th	4 and 5 September 2024
6th	5 and 6 November 2024

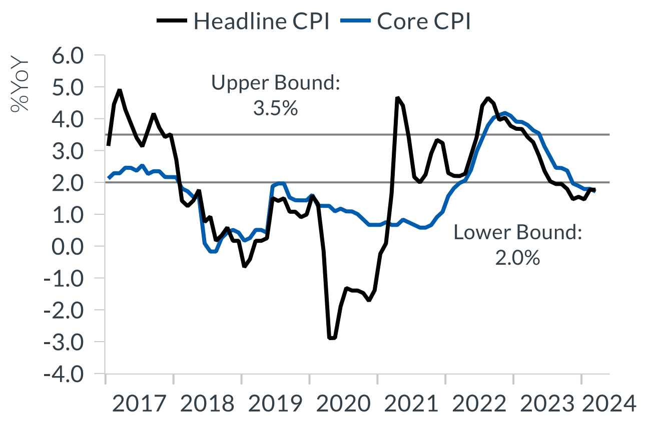
Source: BNM, RHB Economics & Market Strategy

Figure 1: BNM to stay pat at 3.0% into 2024…



Source: Macrobond, RHB Economics & Market Strategy.

Figure 2: …as both headline and core CPI remains tame against BNM's 2024 CPI forecast



Source: Macrobond, RHB Economics & Market Strategy.

OPR Behaviour to be Driven by Economic and Inflation Outlook

We maintain our view that Overnight Policy Rate (OPR) would remain unchanged at 3.00% for 2024. At this juncture, we see the lack of impetus for BNM to tweak its policy rate level in 2024, considering the rosier domestic economy prospect amid uncertainties in the inflationary trajectory. In our view, three key factors will drive the OPR behaviour: (1) Malaysia's economic momentum, whereby we are expecting growth to expand by 4.6% in 2024 (against 2023's 3.7%), (2) the inflation momentum, which we think headline CPI will expand by 3.3% in 2024 (from 2023's 2.5%), and (3) to a smaller extent, on how global rates may behave in the foreseeable future.

Fiscal consolidation measures such as adjustments in fuel prices and utility tariffs coupled with revision in services tax, could potentially lift the headline inflation by 0.7%-1.1% (versus 2.5% YoY in 2023) to our annual forecast of 3.3%. The inflation momentum has picked up in the recent two months amid upward adjustments in the water tariffs for the domestic users in Peninsular Malaysia and the Federal Territory of Labuan. Higher water tariffs have contributed to 0.2% increase in overall headline inflation. With regards to the fuel subsidy rationalisation, there is no final decision on when Malaysia will implement fuel subsidy cuts at the time of writing. In our opinion, the fuel subsidy rationalisation is likely to be implemented on a gradual and measured approach to limit the shock to the overall price movements. The balance of risks is towards a delay in fuel subsidy rationalisation towards end-2024. Thus, the official inflation range of 2.0% to 3.5% should provide sufficient room against future price movements.

As the economic prospect is anticipated to remain robust for 2024, there is limited probability to cut the OPR as well. As aforementioned, we expect Malaysia's growth momentum to accelerate this year. The recovery will be underpinned by improvement in external demand and manufacturing sector activities. The industrial production and export's momentum (MoM, 3MMA) has picked up in recent months amid higher outbound shipments of E&E and petroleum-based products. Meanwhile, the private consumption growth in Malaysia is expected to be buoyed by healthy labour market demand conditions. We maintain our GDP projection at 4.6% for 2024 versus 3.7% for 2023.

Our proprietary MYR model suggests that the MYR movement is a reflection of US-MY rate differential into the year as well as fiscal and current account balances. We forecast the Federal Funds Rates (FFR) to see one cut in 4Q24, with the balance of risks magnified towards no cuts in 2024. The USD carry against MYR is likely to remain rich as market price out FFR cuts, suggesting MYR weakness may persist into 2Q24. The MYR is projected to hover at 4.8 per USD on average in 2Q24. Further out into 4Q24, the MYR is forecasted to strengthen to 4.7 per USD on assumption of one FFR cut by end-2024, improvement in current account balance and fiscal position.

BNM held its OPR at 3.00% in May's meeting, in line with our in-house view and market expectations. Policymakers maintained its neutral tone on the monetary policy stance; - at the current OPR level, the monetary policy stance remains supportive of the economy and is consistent with the current assessment of the inflation and growth prospects.

On economic assessment, the central bank maintained its optimism on Malaysia's domestic economy. Policymakers cited that growth would be underpinned by resilient domestic expenditure, recovery in exports and improvement in tourism activities. Investment activity would be buoyed by the continued progress of multi-year projects, the implementation of catalytic initiatives under the national master plans, and higher realisation of approved investments. Besides that, the central bank inferred that the inflation outlook is subjected to changes to domestic policy on subsidies and price controls, as well as global commodity prices and financial market developments. On the global front, the economy would continue to expand amid continued recovery in global trade and robust labour market conditions in selected economies. The policymakers highlighted that the global monetary policy stance is likely to remain tight in the near term, with prospect of interest rates to stay high for longer (particularly for U.S.), as the pace for disinflation has slowed in some advanced economies.

On MYR, the bank commented that the recent weakness in MYR does not reflect Malaysia's economic fundamentals and growth prospects. Regional currencies including MYR is subjected to external influence such as adjustments in expectation for major economies' monetary policies and ongoing geopolitical tensions. Hence, the Government and BNM are taking coordinated actions with Government-Linked Companies (GLCs) and Government-Linked Investment Companies (GLICs), in order to cushion the pressures on MYR. Over the medium term, ongoing structural reforms will provide more enduring support to the Ringgit as well.

Figure 3: Comparisons of May and March MPC statement

Category	May MPC Statement	March MPC Statement	Key Message Highlighted
MPC Decision	At its meeting today, the Monetary Policy Committee (MPC) of Bank Negara Malaysia decided to **maintain the Overnight Policy Rate (OPR) at 3.00 percent.**	At its meeting today, the Monetary Policy Committee (MPC) of Bank Negara Malaysia decided to **maintain the Overnight Policy Rate (OPR) at 3.00 percent.**	**OPR maintain the Overnight Policy Rate (OPR) at 3.00 percent.**
Global Outlook	**The global economy continues to expand amid resilient labour markets in some countries and continued recovery in global trade.** **Looking ahead, global growth is expected to be sustained, as headwinds from tight monetary policy and reduced fiscal support will be cushioned by positive labour market conditions and moderating inflation.** Global trade is expected to strengthen further as the global tech upcycle gains momentum. **While global headline and core inflation continued to edge downwards in recent months, the pace for disinflation has slowed in some advanced economies.** This increases the prospect of interest rates to remain high for longer, particularly in the US. The growth outlook remains subject to downside risks, mainly from further escalation of geopolitical tensions, higher-than-anticipated inflation outturns, and volatility in global financial markets.	**The global economy continues to expand albeit moderately,** supported by domestic demand amid improvement in trade activity. Favourable labour market conditions in some countries continue to support consumption activity. **Looking ahead, growth in regional economies is expected to improve, while China's growth would likely remain modest given continued weakness in the property market.** Global trade is expected to strengthen as the global tech upcycle gains momentum. **Global headline and core inflation edged downwards in recent months with prospects of monetary easing in some countries in the second half of the year.** **Nonetheless, the global monetary policy stance is likely to remain tight in the near term, as inflation remains above average.** The growth outlook remains subject to downside risks, mainly from an escalation of geopolitical tensions, higher-than-anticipated inflation outturns, and volatility in global financial markets.	**Looking ahead, global growth is expected to be sustained, as headwinds from tight monetary policy and reduced fiscal support will be cushioned by positive labour market conditions and moderating inflation.** **While global headline and core inflation continued to edge downwards in recent months, the pace for disinflation has slowed in some advanced economies. This increases the prospect of interest rates to remain high for longer, particularly in the US.**
Domestic Outlook	**For the Malaysian economy, the latest indicators point towards higher economic activity in the first quarter of 2024, driven by resilient domestic expenditure and a positive turnaround in exports.** **Going forward, the recovery in exports is expected to gather momentum supported by the global tech upcycle and continued strength in non-electrical and electronics goods.** Tourist arrivals and spending are also poised to rise further. Continued employment and wage growth remain supportive of household spending. Investment activity would be supported by the ongoing progress of multi-year projects in both the private and public sectors, the implementation of catalytic initiatives under the national master plans, as well as the higher realisation of approved investments. The growth outlook is subject to downside risks from weaker-than-expected external demand, and larger declines in commodity production. Meanwhile, upside risks to growth mainly emanate from greater spillover from the tech upcycle, more robust tourism activity, and faster implementation of existing and new projects.	**The Malaysian economy expanded by 3.7% in 2023. Moving forward, growth is expected to improve in 2024, driven by the recovery in exports and resilient domestic expenditure. Export growth is turning positive after contracting since March 2023 and will continue to be supported by stronger global trade.** Tourist arrivals and spending are poised to rise further. Continued employment and wage growth remain supportive of household spending. Investment activity would be supported by the ongoing progress of multi-year projects in both the private and public sectors, the implementation of catalytic initiatives under the national master plans, as well as the higher realisation of investments. The growth outlook is subject to downside risks stemming from weaker-than-expected external demand and larger declines in commodity production. Meanwhile, upside risks to growth mainly emanate from greater spillover from the tech upcycle, more robust tourism activity and faster implementation of existing and new projects.	**For the Malaysian economy, the latest indicators point towards higher economic activity in the first quarter of 2024, driven by resilient domestic expenditure and a positive turnaround in exports. Going forward, the recovery in exports is expected to gather momentum supported by the global tech upcycle and continued strength in non-electrical and electronics goods.**
Inflation View	Headline and core inflation averaged 1.7% and 1.8% in the first quarter of 2024 respectively. **Looking forward, inflation in 2024 is expected to remain moderate, broadly reflecting stable demand conditions and contained cost pressures.** **The outlook for the rest of the year is dependent on the implementation of domestic policy on subsidies and price controls, as well as global commodity prices and financial market developments.** After incorporating the potential impact of subsidy rationalisation, headline and core inflation are projected to average between 2.0% - 3.5% and 2.0% - 3.0% for the year respectively.	Headline and core inflation stood at 1.5% and 1.8% respectively in January 2024, trending in line with expectations. **Inflation in 2024 is expected to remain moderate, broadly reflecting stable demand conditions and contained cost pressures.** **However, this outlook continues to be highly dependent on the implementation of domestic policy on subsidies and price controls, as well as global commodity prices and financial market developments.**	**The outlook for the rest of the year is dependent on the implementation of domestic policy on subsidies and price controls, as well as global commodity prices and financial market developments.**
Financial Market view	**The ringgit currently does not reflect Malaysia's economic fundamentals and growth prospects. External factors, namely shifting expectations of major economies' monetary policy paths and ongoing geopolitical tensions, have led to heightened volatility in both capital flows and exchange rates across the region, including the ringgit.** The coordinated initiatives by the Government and Bank Negara Malaysia (BNM) with the Government-Linked Companies (GLCs) and Government-Linked Investment Companies (GLICs), and corporate engagements have gained further traction, cushioning the pressure on the ringgit. BNM will continue to manage risks arising from heightened financial market volatility. Over the medium term, domestic structural reforms will provide more enduring support to the ringgit.	**The Ringgit is currently undervalued, given Malaysia's economic fundamentals and growth prospects.** **The Government and Bank Negara Malaysia are taking coordinated actions to encourage repatriation and conversion of foreign investment income by GLCs and GLICs.** These actions are contributing to greater inflows, lending support to a firmer ringgit. Over the medium term, ongoing structural reforms will provide more enduring support to the ringgit.	**The ringgit currently does not reflect Malaysia's economic fundamentals and growth prospects. External factors, namely shifting expectations of major economies' monetary policy paths and ongoing geopolitical tensions, have led to heightened volatility in both capital flows and exchange rates across the region, including the ringgit.**
MPC Stance	**At the current OPR level, the monetary policy stance remains supportive of the economy and is consistent with the current assessment of the inflation and growth prospects.** The MPC remains vigilant to ongoing developments to inform the assessment on the outlook of domestic inflation and growth. The MPC will ensure that the monetary policy stance remains conducive to sustainable economic growth amid price stability	**At the current OPR level, the monetary policy stance remains supportive of the economy and is consistent with the current assessment of the inflation and growth prospects.** The MPC remains vigilant to ongoing developments to inform the assessment on the outlook of domestic inflation and growth. The MPC will ensure that the monetary policy stance remains conducive to sustainable economic growth amid price stability.	**At the current OPR level, the monetary policy stance remains supportive of the economy and is consistent with the current assessment of the inflation and growth prospects.**

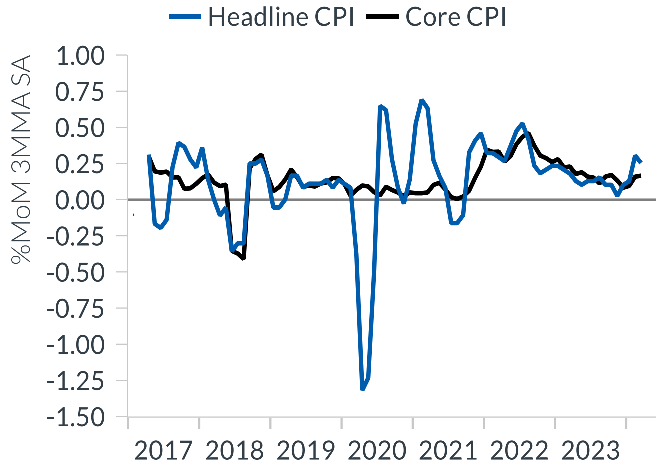
Source: BNM, RHB Economics & Market Strategy.

Figure 4: Key policy initiatives and the direct impact on headline CPI

Measures	Potential Upside on Headline CPI (ppt)	Quantum of Adjustments (Iin-house assumption/actual)	Period of Commencement	Scope of Coverage
Diesel Subsidy Rationalisation	0.15-0.20	5% increase*	Assume on 2Q24	Peninsular Malaysia
RON95 Fuel Subsidy Rationalisation	0.10-0.15	5% increase*	Assume on 2H24	Nationwide*
Services Tax Revision	0.30-0.60	2% increase in services tax	March 2024	All taxable services
Electricity Tariff Adjustment	0.01-0.02	4.2% to 6% increase in monthly bill	1 January to 30 June	15% of domestic consumers in Peninsular Malaysia
Water Tariff Adjustment	0.02-0.05	5% increase*	February 2024	47% of domestic users in Peninsular Malaysia and Labuan
Removal of Chicken Ceiling Price	0.12	10% increase*	November 2023	Nationwide
Implementation of LVGT	Unquantifiable	10% of sales tax	January 2024	Imported goods priced at RM500 or less, which are sold online.
Implementation of HVGT	Unquantifiable	5-10% of tax	May 2024	Pending details of the taxable items and their thresholds
Progressive Wage Program	Limited Impact	Pending official announcement	Full implementation after December 2024	Pending official announcements
Total direct impact on Headline CPI	**0.7-1.1**			
2023 Headline CPI (YoY%)	**2.5**			
2024 Headline CPI Range (YoY%)	**3.2-3.6**			

*Source: Source: Various Sources, RHB Economics & Market Strategy, *based on in-house assumptions*

Figure 5: Inflation momentum has picking up



Source: Macrobond, RHB Economics & Market Strategy.

Figure 6: MYR is a reflection of the country's balances (current and fiscal account), as well as US-MY real rates

Dependent Variable: USD-MYR

Regression Statistics	
Multiple R	0.867
R Square	0.751
Adjusted R Square	0.727
Standard Error	0.256
Observations	70

	Coeff	*Std Error*	*t Stat*	*P-value*
Intercept	6.96	0.40	17.38	0.00
Current Account % GDP (-1)	-0.10	0.02	-6.40	0.00
Fiscal Account % GDP (-4)	-0.07	0.04	-1.89	0.05
Public Debt YoY (3QMA) (-2)	-0.04	0.01	-2.81	0.01
KLCI (x100) (-1)	-0.13	0.00	-5.72	0.00
Brent (x100) (-1)	-0.48	0.00	-2.82	0.01
US-MY Real Rates (-4)	0.02	0.03	0.91	0.36

Source: Macrobond, RHB Economics & Market Strategy.

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