



From the Desk
of the
Chief Economist

BANK ISLAM

CPI GREW BY 4.4% IN MAY

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ECONOMIC RESEARCH

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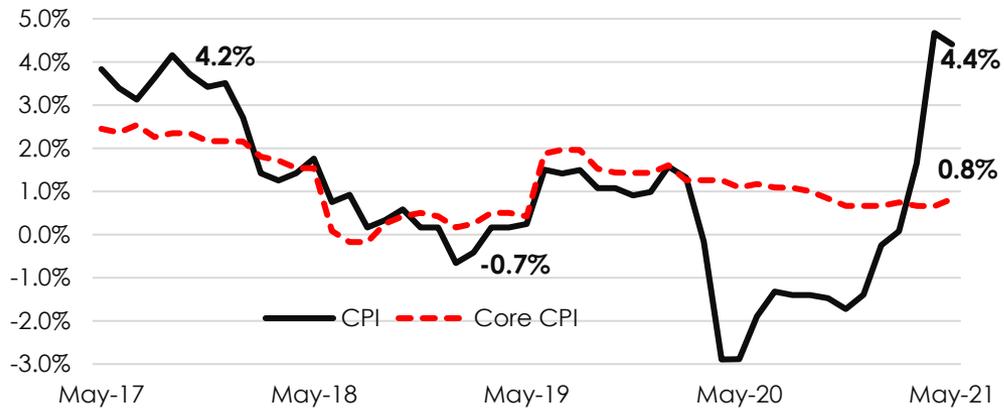
RAJA ADIBAH RAJA HASNAN

CPI INCREASED MODESTLY BY 4.4% IN MAY

01 **Headline Inflation**
 May 4.4%
 Apr 4.7%

02 **Core Inflation**
 May 0.8%
 Apr 0.7%

Inflation Rate, y-o-y% (May 2017- May 2021)



Source: CEIC

Food & Non-Alcoholic Beverages



May 1.5%
 Apr 1.9%

Alcoholic Beverages & Tobacco



May 0.7%
 Apr 0.7%

Clothing & Footwear



May -0.5%
 Apr -0.4%

Housing, Water, Electricity, Gas & Other Fuels



May 3.2%
 Apr 3.1%

Furnishings, Household Equipment & Routine Household Maintenance



May 2.1%
 Apr 1.6%

Health



May 0.6%
 Apr 0.5%

Transport



May 26.0%
 Apr 27.0%

Communication



May 0.0%
 Apr 0.0%

Recreation Services & Culture



May 0.6%
 Apr 0.7%

Education



May 0.3%
 Apr 0.2%

Restaurants & Hotels



May 0.2%
 Apr 0.2%

Miscellaneous Goods & Services



May 0.7%
 Apr 1.2%

COST OF FOOD AND NON-ALCOHOLIC BEVERAGES EASED IN MAY

	Weight	Jan-21	Feb-21	Mar-21	Apr-21	May-21	5M2020	5M2021
Consumer Price Index (CPI)	100.0%	-0.2%	0.1%	1.7%	4.7%	4.4%	-0.6%	2.1%
Food and Non-Alcoholic Beverages	29.5%	1.5%	1.4%	1.5%	1.9%	1.5%	1.1%	1.6%
Alcoholic Beverages and Tobacco	2.4%	0.7%	0.7%	0.6%	0.7%	0.7%	0.2%	0.7%
Clothing and Footwear	3.2%	-0.4%	-0.4%	-0.3%	-0.4%	-0.5%	-1.1%	-0.4%
Housing, Water, Electricity, Gas & Other Fuels	23.8%	-0.7%	-0.8%	-0.8%	3.1%	3.2%	0.0%	0.7%
Furnishings, Household Equipment and Routine Household Maintenance	4.1%	0.2%	0.3%	0.9%	1.6%	2.1%	0.6%	1.0%
Health	1.9%	0.7%	0.7%	0.5%	0.5%	0.6%	1.3%	0.6%
Transport	14.6%	-5.1%	-2.0%	9.8%	27.0%	26.0%	-9.1%	9.6%
Communication	4.8%	0.0%	0.0%	0.0%	0.0%	0.0%	1.5%	0.0%
Recreation and Culture	4.8%	0.1%	0.1%	0.5%	0.7%	0.6%	0.7%	0.4%
Education	1.3%	0.2%	0.1%	0.0%	0.2%	0.3%	1.3%	0.2%
Restaurants and Hotels	2.9%	-0.1%	-0.3%	0.0%	0.2%	0.2%	1.0%	0.0%
Miscellaneous Goods and Services	6.7%	1.8%	1.6%	1.0%	1.2%	0.7%	2.6%	1.2%
Core CPI		0.7%	0.7%	0.7%	0.7%	0.8%	1.3%	0.7%

Sources: DOSM, CEIC

1

Malaysia's Consumer Price Index (CPI) growth toned down to the tune of 4.4% year-on-year (y-o-y) in May, after rising by 4.7% in the preceding month (Consensus: 4.7%, Bank Islam: 4.8%).

2

This was mainly attributed by the slower price increase in Food and Non-Alcoholic Beverages at 1.5% in May (April: 1.9%), which forms a sizeable share of 29.5% out of the total CPI.

3

Nonetheless, higher costs of Housing, Water, Electricity, Gas & Other Fuels (May: 3.2% vs. April: 3.1%), Furnishings, Household Equipment and Routine Household Maintenance (May: 2.1% vs. April: 1.6%), as well as Education (May: 0.3% vs. April: 0.2%) were seen in May.

4

Apart from that, costs for Transport still recorded a double-digit growth, increasing by 26.0% in May, slightly lower than previous month's figure of 27.0%.

5

However, the Core CPI which excludes most volatiles items of fresh food, as well as administered prices of goods and services went up by 0.8% in May compared to a 0.7% growth in the previous month.

6

Cumulatively, the CPI growth jumped by 2.1% in 5M2021 from a 0.6% decline in the same period last year. Meanwhile, the core CPI growth softened by 0.7% in 5M2021 (5M2020: 1.3%).

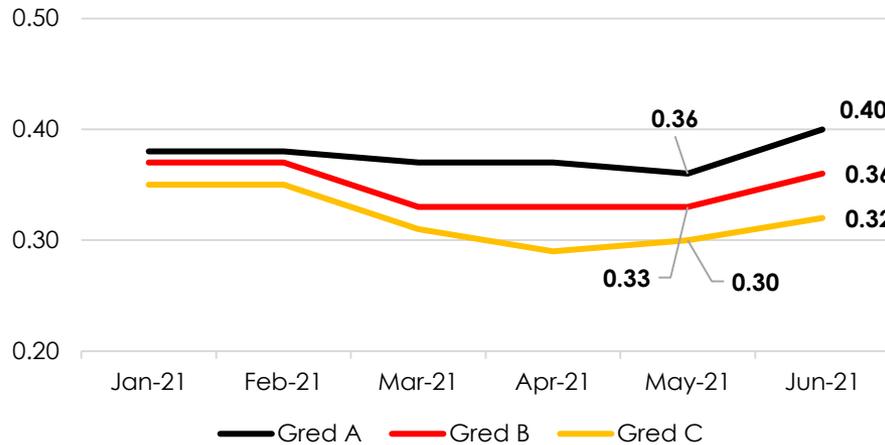
States	Nov-20	Dec-20	Jan-21	Feb-21	Mar-21	Apr-21	May-21	5M2020	5M2021
Nationwide	-1.7%	-1.4%	-0.2%	0.1%	1.7%	4.7%	4.4%	-0.6%	2.1%
WP Kuala Lumpur	-1.2%	-0.9%	0.1%	0.2%	1.5%	3.8%	3.7%	-0.1%	1.8%
Selangor & WP Putrajaya	-1.2%	-0.9%	0.2%	0.4%	1.9%	4.7%	4.5%	-0.1%	2.3%
Melaka	-2.6%	-2.0%	-0.6%	-0.2%	1.3%	4.4%	4.1%	-1.3%	1.8%
Negeri Sembilan	-2.4%	-1.9%	-0.5%	-0.1%	1.8%	5.0%	4.7%	-1.0%	2.2%
Johor	-2.1%	-2.0%	-0.8%	-0.2%	1.5%	4.9%	4.6%	-0.8%	1.9%
Pahang	-2.1%	-1.3%	0.1%	0.2%	1.9%	5.6%	5.1%	-0.7%	2.5%
Kelantan	-1.7%	-1.2%	0.2%	0.7%	2.3%	5.7%	5.6%	-1.1%	2.8%
Terengganu	-1.5%	-1.0%	0.3%	0.8%	2.8%	6.3%	6.2%	-1.1%	3.3%
Kedah & Perlis	-2.6%	-2.2%	-0.8%	-0.3%	1.6%	5.1%	4.8%	-1.2%	2.0%
Pulau Pinang	-1.5%	-1.1%	0.0%	0.2%	1.5%	3.9%	3.7%	-0.3%	1.8%
Perak	-2.0%	-1.4%	-0.1%	0.2%	1.7%	4.7%	4.5%	-0.7%	2.2%
Sabah & WP Labuan	-2.5%	-2.0%	-1.5%	-1.0%	0.8%	3.9%	3.6%	-1.3%	1.1%
Sarawak	-2.4%	-1.9%	-1.2%	-0.7%	1.2%	4.3%	4.1%	-1.2%	1.5%

Sources: CEIC, DOSM

- ✓ All states recorded a softer increase in prices with states such as Terengganu (May: 6.2% vs. April: 6.3%), Kelantan (May: 5.6% vs. April: 5.7%), Pahang (May: 5.1% vs. April: 5.6%) and Kedah & Perlis (May: 4.8% vs. April: 5.1%), Negeri Sembilan (May: 4.7% vs. April: 5.0%), Selangor & WP Putrajaya (May: 4.5% vs. April: 4.7%) and Perak (May: 4.5% vs. April: 4.7%) recording a higher inflation rate compared to the national inflation rate of 4.4% in May.
- ✓ Cumulatively, all states posted higher price inflation during 5M2021 as compared to the same period last year led by Terengganu and Kelantan, registering at 3.3% (5M2020: -1.1%) and 2.8% (5M2020: -1.1%) respectively.

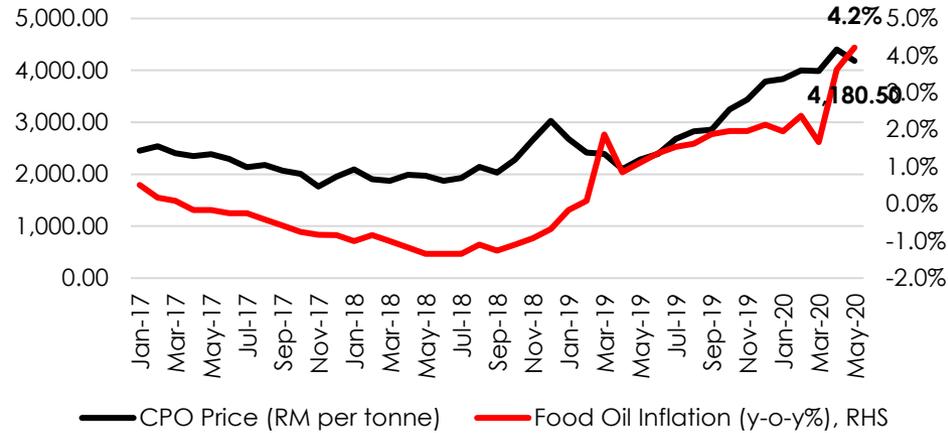
CONSUMERS WOULD CONTINUE TO FEEL THE PINCH OF HIGHER FOOD PRICES

Malaysia's Egg Price, RM per egg



Source: Department of Veterinary Services

CPO Price* vs. Food Oil Price



Source: CEIC

* Local delivery month end spot price

- ✓ Malaysia's food price continued to rise though at a slower pace of 1.5% y-o-y in May from 1.9% previously.
- ✓ Within the food sub-indices, some of the food products reported higher costs such as Milk, Cheese & Eggs (May: 0.6% vs. April: 0.5%), Oil (May: 4.2% vs. April: 3.6%), Margarine & Peanut Butter etc. (May: 2.1% vs. April: 1.8%).
- ✓ The increase food oil price was partly affected by Crude Palm Oil (CPO) price which has been showing an uptrend since March 2019 given the positive correlation of about 77.0% between CPO and food oil price.
- ✓ Apart from that, egg prices went up to RM0.40 per egg for Grade A (May: RM0.36 per egg), RM0.36 per egg for Grade B (May: RM0.33 per egg) and RM0.32 per egg for Grade C (May: RM0.30 per egg) in June.
- ✓ On the other hand, a harsh drought across major parts of the U.S. farm grew more severe, posing a risk on corn, soybean and wheat crops. Despite overnight showers and thunderstorms which have provided some relief moisture in Iowa and some portions of neighboring states, the dry condition is likely to weigh on the crop yields in key U.S production areas. As such, this could lead to an increase in livestock prices particularly Malaysia that is highly dependent on imported animal feed.
- ✓ Therefore, the continued rise in food prices are heightening concerns over bulging grocery bills at a time when the economy is grappling with detrimental impacts from the Covid-19 pandemic.

Consumer Price Index	Jun-20	Jul-20	Aug-20	Sep-20	Oct-20	Nov-20	Dec-20	Jan-21	Feb-21	Mar-21	Apr-21	May-21	5M2020	5M2021
Malaysia	-1.9%	-1.3%	-1.4%	-1.4%	-1.5%	-1.7%	-1.4%	-0.2%	0.1%	1.7%	4.7%	4.4%	-0.6%	2.1%
Indonesia	2.0%	1.5%	1.3%	1.4%	1.4%	1.6%	1.7%	1.6%	1.4%	1.4%	1.4%	1.7%	2.7%	1.5%
Philippines	2.5%	2.7%	2.4%	2.3%	2.5%	3.3%	3.5%	4.2%	4.7%	4.5%	4.5%	4.5%	2.5%	4.5%
Thailand	-1.6%	-1.0%	-0.5%	-0.7%	-0.5%	-0.4%	-0.3%	-0.3%	-1.2%	-0.1%	3.4%	2.4%	-1.0%	0.8%
Singapore	-0.5%	-0.4%	-0.4%	0.0%	-0.2%	-0.1%	0.0%	0.2%	0.7%	1.3%	2.1%	2.4%	-0.1%	1.4%
China	2.5%	2.7%	2.4%	1.7%	0.5%	-0.5%	0.2%	-0.3%	-0.2%	0.4%	0.9%	1.3%	4.1%	0.4%
India	6.2%	6.7%	6.7%	7.3%	7.6%	6.9%	4.6%	4.1%	5.0%	5.5%	4.2%	6.3%	6.7%	5.0%

Sources: CEIC, DOSM

- ✓ Malaysia's growth in the CPI during May was in conformity with some of its regional peers which showed an increase in their respective CPI. In fact, Malaysia's CPI was the third largest amongst its Asian peers after India and Philippines.
- ✓ India's CPI growth reached 6.3% in May (April: 4.2%), the highest in six months on account of higher food and energy prices. Food CPI accelerated by 5.0% in May (April: 2.0%), while the CPI Fuel and Light grew by 11.6% during the same month (April: 8.0%). The ebbing of the second wave of the pandemic in India and increasing vaccination numbers have led to expectations of a recovery in demand. This has led producers to expect higher prices in the coming months.
- ✓ Meanwhile, China recorded the smallest growth in CPI among Asian peers during May at 1.3% (April: 0.9%) but was the fastest growth for the country since September last year. The CPI reading picked up as food prices rose amid a tight supply of freshwater fish and eggs, while non-food prices increased with transportation costs elevated by rising international crude oil prices.
- ✓ For 5M2021, India (5M2021: 5.0% vs. 5M2020: 6.7%) recorded the highest increase in CPI compared to the same period last year while China (5M2021: 0.4% vs. 5M2020: 4.1%) was the smallest gainer among other peers.

OUR VIEW – LOW BASE EFFECT ON OIL PRICES TO SUBSIDE IN COMING MONTHS

- ✓ As mentioned earlier, costs of Transport have increased particularly for the Fuels & Lubricants For Personal Transport Equipment which rose strongly by 56.1% in May but moderated from the 59.2% growth recorded in April.
- ✓ This coincided with the increase in average fuel prices for RON95, RON97 and Diesel in May compared to the month before shown in the table below.

Year-on-year changes (%) in average fuel prices

Month	Price (RM per litre)			Year-on-year change (%)		
	RON95	RON97	Diesel	RON95	RON97	Diesel
Apr-21	2.05	2.55	2.15	60.8%	61.9%	44.2%
May-21	2.05	2.60	2.15	57.1%	62.1%	48.3%

Source: CEIC

Note: Prices are averaged for each month

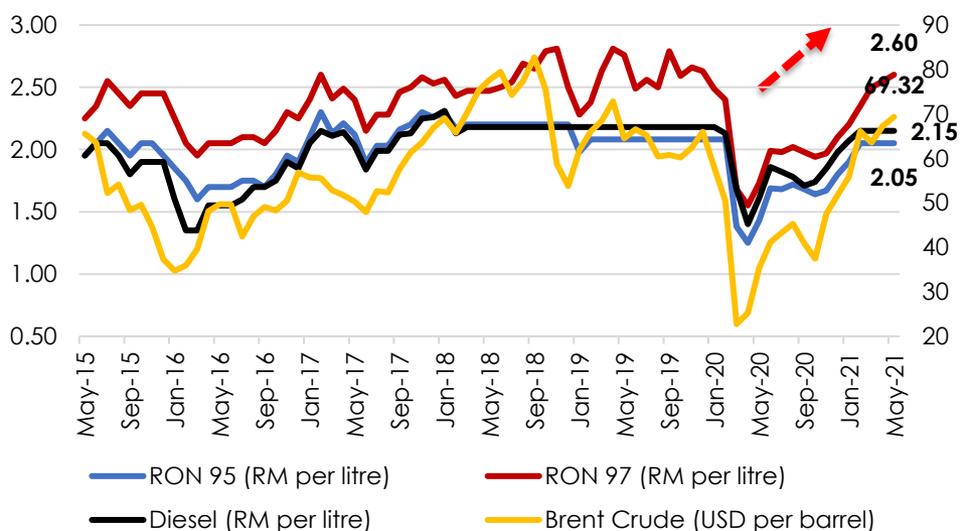
- ✓ While the low base effect may still be present, it is worthwhile to note that the average price for RON95 in particular has shown a slower growth of 57.1% in May (April 60.8%). This indicates that the effect of a lower base from last year is fading and is expected to subside further in the coming months after the government increased fuel prices starting end of May 2020 onwards.
- ✓ Likewise the, growth in average Brent crude oil price moderated to 110.8% y-o-y in May (April: 143.2%), reaching USD68.31 per barrel in May this year from USD32.41 per barrel in the same month last year.
- ✓ Looking ahead, the discussion by the Organisation of the Petroleum Exporting Countries (OPEC) to further ease production cuts is a sign that the group is prepared to cater expected higher demand while ensuring oil prices do not rise abruptly.

Costs of Fuels & Lubricating Personal Transport Equipment, y-o-y%



Source: CEIC

Malaysia Petrol Price vs. Brent Crude Oil Price

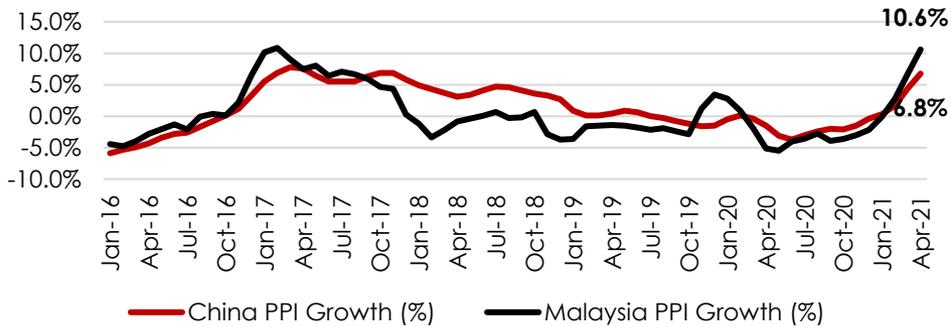


Source: CEIC

Note: Prices are taken at the end of each month

OUR VIEW- THE RELATIONSHIP BETWEEN CHINA'S PPI GROWTH WITH MALAYSIA'S PPI GROWTH

China PPI Growth vs. Malaysia PPI Growth, %



Source: CEIC

Monthly Aluminium and Iron Ore Price

Month	Aluminium (USD per Metric Ton)	Iron Ore Price (USD per Dry Metric Ton)
Jan-21	13.0%	77.1%
Feb-21	23.1%	86.8%
Mar-21	36.0%	89.0%
Apr-21	58.9%	112.2%
May-21	66.0%	121.8%

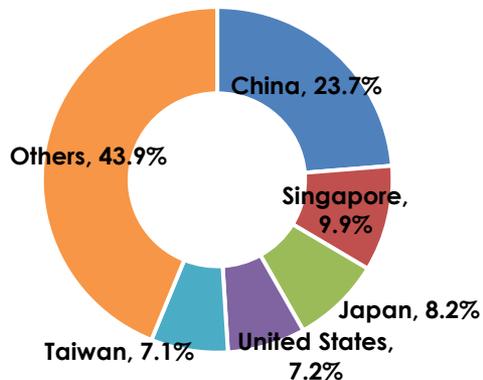
Source: Index Mundi

Correlation Matrix between China's PPI Growth and Malaysia's PPI Growth

	China PPI Growth (%)	Malaysia PPI Growth (%)
China PPI Growth (%)	1.0000	
Malaysia PPI Growth (%)	0.7438	1.0000

Sources: CEIC, Bank Islam

Malaysia's Import Destination Breakdown



Source: CEIC

Note: As at April 2021

- ✓ The price of goods leaving China's factories has risen as seen from China's producer price index (PPI) which increased by 9.0% y-o-y in May (April: 6.8%), its biggest y-o-y gain since September 2008.
- ✓ In addition to the low base effect, the rise in China's PPI in May was driven by an international rally in commodities amid expected stronger demand in the wake of the anticipated economic recovery.
- ✓ For instance, the prices for aluminium and iron ore in May increased markedly by 66.0% y-o-y (April: 58.9%) and 121.8% (April: 112.2%) respectively.
- ✓ Likewise, Malaysia's latest PPI grew by 10.6% in April (March: 6.7%). Our analysis indicates that the growth in Malaysia's PPI has a high correlation with China's PPI growth at 74.4%.
- ✓ The high correlation between the Malaysia's PPI growth and China's PPI growth can be explained by China's relationship with Malaysia as its major trading partner.
- ✓ Malaysia's imports from China constitutes 23.7% of total imports as at April this year and has always been contributing more than 20.0% on average towards Malaysia's total imports.
- ✓ Therefore, any change in China's PPI is bound to have an effect on Malaysia's PPI as some imported goods from China are used by manufacturers to produce their products.

- ✓ It is worthwhile to examine the causality between Malaysia's CPI and PPI via the Granger Causality test.
- ✓ Findings from the Granger Causality test indicate that PPI does have a causality towards CPI but not vice versa.
- ✓ This is somewhat logical as PPI are prices from factories which are sometimes passed down to consumers which is later reflected in the CPI.
- ✓ Taking into account of the strong correlation between Malaysia's PPI and China's PPI, China's country's soaring producer prices are set to increase costs for businesses in Malaysia which will in turn influence the prices imposed on consumers in the country.

Summary of Results from Pairwise Granger Causality Test from Eviews

Null Hypothesis	p-value	Decision	Outcome
PPI does not Granger Cause CPI	0.0%	Reject the null hypothesis	PPI does cause CPI
CPI does not Granger Cause CPI	27.0%	Do not reject the null hypothesis	CPI does not cause PPI

Sources: Eviews, Bank Islam

Results Output from Pairwise Granger Causality Test from Eviews

Pairwise Granger Causality Tests			
Date: 06/24/21 Time: 11:21			
Sample: 2015M01 2021M04			
Lags: 2			
Null Hypothesis:	Obs	F-Statistic	Prob.
PPI does not Granger Cause CPI	74	8.74838	0.0004
CPI does not Granger Cause PPI		1.33426	0.2701

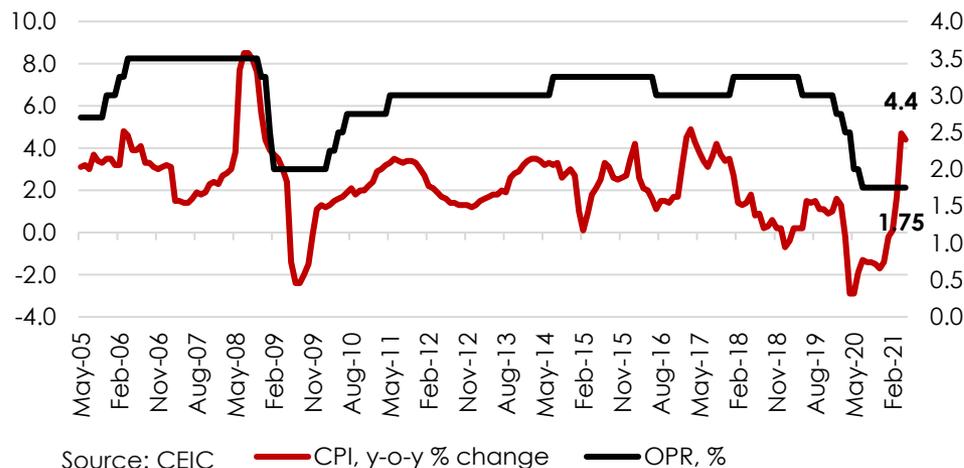
Sources: Eviews, Bank Islam

- ✓ Apart from that, the restricted work capacity during the full-scale lockdown in Malaysia has caused bottleneck supply chain issues. As such, manufacturers may face difficulty to fulfill orders from other countries that are seeing shoots of recovery whereby consumer demand is strong. In short, demand outweighs supply, pushing prices of goods higher.
- ✓ Notwithstanding this, the supply and demand dynamics of global trade will likely normalize later in 2H2021. The reason being is that the ramp up in vaccinations will pave way for higher capacity utilisation of manufacturers, enabling them to catch up with demand and subsequently tame inflationary pressures. Henceforth it is hardly a structural worry.
- ✓ Taking all of this into consideration, we are maintaining our CPI forecast of **2.5% for 2021 (2020: -1.1%)**.

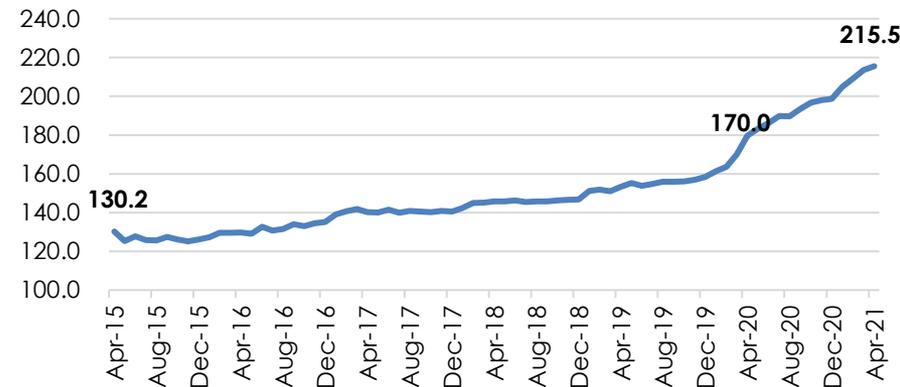
OUR VIEW- MONETARY POLICY RESPONSE

- ✓ In terms of monetary policy, we still believe that a rate hike in 2021 is premature due to the surge in inflation being partly due to low base nature and with much of the increase coming from energy prices.
- ✓ Moreover, the country is still in the midst of recovery with current cases staying above 5,000 per day so the current Overnight Policy Rate (OPR) of 1.75% is deemed appropriate at this juncture to support the economy.
- ✓ Our estimates indicate that the aim to vaccinate 80.0% of Malaysia's population by year end is possible. Once this goal is reached, a full reopening of the social and economic sectors is something that can be reasonably expected.
- ✓ We opine that the reopening of the economy will be accompanied by a strong propensity to consume. This can be seen from the number of deposits held by individuals in the country's banking system which stood at RM215.5 billion in April this year (March: RM213.6 billion) compared to RM170.0 billion when the pandemic outbreak occurred in March last year.
- ✓ Therefore, a higher OPR in 2022 would be more plausible once the majority of the country's population is fully vaccinated as restrictions for economic activities will likely be eased. The inflation rate by then would also strongly reflect the real nature of prices as large increases in energy prices will no longer be seen.

CPI, y-o-y% change vs. OPR,%



Saving Deposits by Individuals in Malaysia's Banking System (RM billion)



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An aerial photograph of a city skyline at sunset, with a prominent pink bar at the bottom. The sky is filled with soft, golden light and scattered clouds. The city features numerous high-rise buildings, with a particularly tall, slender skyscraper on the left. A highway with traffic is visible in the foreground, winding through the city. The overall mood is warm and serene.

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