From the Desk of the Chief Economist

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U.S. FOMC : THE FED GETS A LITTLE MORE HAWKISH

23 SEPTEMBER 2021

ECONOMIC RESEARCH

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THE FOMC MAINTAINED FFR TARGET RANGE OF 0.00%-0.25%

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The Federal Open Market Committee (FOMC) **decided to keep the Federal Fund Rate (FFR) range near zero** and **maintained its asset purchases at USD120.0 billion** following its 21-22 September meeting.

- ✓ The U.S. economic performance continued to strengthen fuelled by strong policy support, as well as progress in vaccinations. Following this, sectors that were severely affected by the Covid-19 crisis have started to pick-up. Nevertheless, the emergence of the Delta variant cases in the country has weighed on the economic recovery.
- ✓ The Federal Reserve (Fed) believes that the path of economy would depend on the development of Covid-19 infections. Meanwhile, the vaccination programme would continue to reduce the impact of Covid-19 to the public health.

Percent

Variable	Median[1]					Central Tendency[2]					Range[3]				
	2021	2022	2023	2024	Longer run	2021	2022	2023	2024	Longer run	2021	2022	2023	2024	Longer run
Change in real GDP	5.9	3.8	2.5	2.0	1.8	5.8–6.0	3.4–4.5	2.2–2.5	2.0–2.2	1.8–2.0	5.5–6.3	3.1–4.9	1.8–3.0	1.8–2.5	1.6–2.2
June projection	7.0	3.3	2.4		1.8	6.8–7.3	2.8–3.8	2.0–2.5		1.8–2.0	6.3–7.8	2.6–4.2	1.7–2.7		1.6–2.2
Unemployment rate	4.8	3.8	3.5	3.5	4.0	4.6–4.8	3.6–4.0	3.3–3.7	3.3–3.6	3.8–4.3	4.5–5.1	3.0–4.0	2.8–4.0	3.0–4.0	3.5–4.5
June projection	4.5	3.8	3.5		4.0	4.4–4.8	3.5–4.0	3.2–3.8		3.8–4.3	4.2–5.0	3.2–4.2	3.0–3.9		3.5–4.5
PCE inflation	4.2	2.2	2.2	2.1	2.0	4.0–4.3	2.0–2.5	2.0–2.3	2.0–2.2	2.0	3.4–4.4	1.7–3.0	1.9–2.4	2.0–2.3	2.0
June projection	3.4	2.1	2.2		2.0	3.1–3.5	1.9–2.3	2.0–2.2		2.0	3.0–3.9	1.6–2.5	1.9–2.3		2.0
Core PCE inflation[4]	3.7	2.3	2.2	2.1		3.6–3.8	2.0–2.5	2.0–2.3	2.0–2.2		3.5–4.2	1.9–2.8	2.0–2.3	2.0–2.4	
June projection	3.0	2.1	2.1			2.9–3.1	1.9–2.3	2.0–2.2			2.7–3.3	1.7–2.5	2.0–2.3		
Memo: Projected appropriate policy path															
Federal funds rate	0.1	0.3	1.0	1.8	2.5	0.1	0.1–0.4	0.4–1.1	0.9–2.1	2.3–2.5	0.1	0.1–0.6	0.1–1.6	0.6–2.6	2.0–3.0
June projection	0.1	0.1	0.6		2.5	0.1	0.1–0.4	0.1–1.1		2.3–2.5	0.1	0.1–0.6	0.1–1.6		2.0–3.0

Source: Federal Reserve

- ✓ According to the latest Summary of Economic Projections, the Fed is anticipating that the U.S. GDP will record a rapid growth of 5.9% this year though the momentum was slightly softer compared to 7.0% projection made in June.

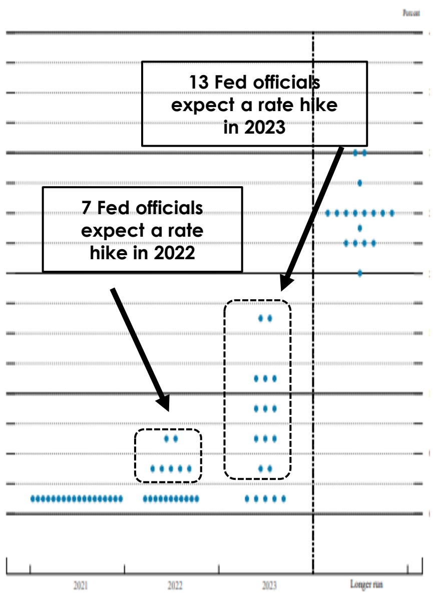
THE FOMC MAINTAINED FFR TARGET RANGE OF 0.00%-0.25% (CONT'D)

- ✓ As for the labour market, the unemployment rate (UR) is expected to improve further to 4.8% this year after 5.2% was recorded in August. Be that as it may, it was still higher compared to 4.5% projection made during June this year.
- ✓ According to the Fed, the inflationary pressure remains elevated largely due to transitory factors. However, a combination of factors such as bottlenecks, hiring difficulties and other constraints could pose upside risks to the inflation.
- ✓ In light of this, the members have revised up the personal consumption expenditure (PCE) inflation for this year to 4.2% (June projection: 3.4%) before moderating by 2.2% in 2022.
- ✓ On the other hand, the Fed signaled that a moderation in the pace of asset purchases may soon be warranted if the economic conditions satisfy the Committee's guidance.
- ✓ The Fed is of the view that it will be appropriate to maintain the FFR at current target range of 0.00%-0.25% until labor market conditions have reached levels consistent with the Committee's assessment of maximum employment and inflation has risen to 2.0% and is on track to moderately exceed 2.0% for some time.
- ✓ Furthermore, half of FOMC participants forecast that these favorable economic conditions will be fulfilled by the end of next year. Following this, the median projection for the appropriate level of the FFR lies slightly above the effective lower bound in 2022.
- ✓ All in all, the Committee will continue to monitor the implications of incoming information for the economic outlook. The FOMC members would be prepared to adjust the stance of monetary policy as appropriate if risks emerge that could impede the attainment of the Committee's goals.

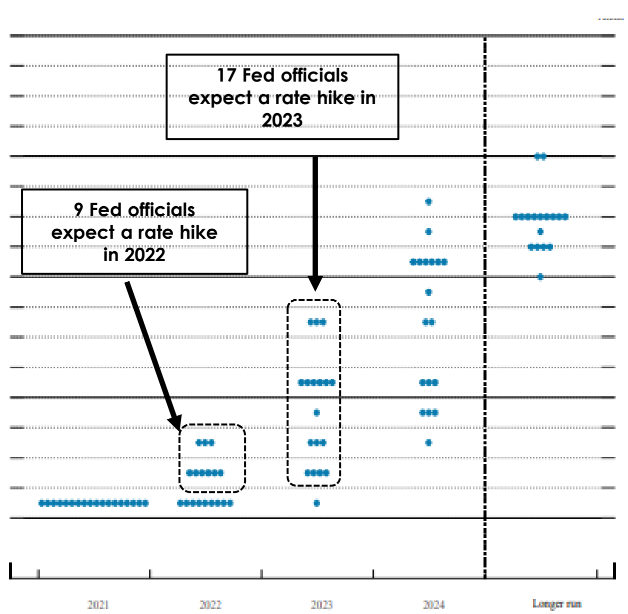
HOW HAS THE FED'S DOT PLOTS EVOLVED IN THE LATEST MEETING?

- ✓ The Fed's so-called dot plot, which the Fed uses to signal its outlook for the path of interest rates, continues to show changes in their tone regarding the target level of the FFR in 2022 and 2023.
- ✓ For example, the dot plot for the September 2021 FOMC meeting showed that 9 Fed officials expect higher interest rates in 2022 (compared to 7 and 4 Fed officials during the June and March 2021 FOMC meeting respectively).
- ✓ Therefore, expectations among policy makers about a rate hike as early as next year is building up with more businesses preparing to live and operate with the virus.
- ✓ Guidance on the timeline for tapering activities has yet to be shared, making the November 2021 FOMC meeting to be the time when FOMC announces its decision to begin scaling back bond purchases.

June 2021 FOMC Meeting



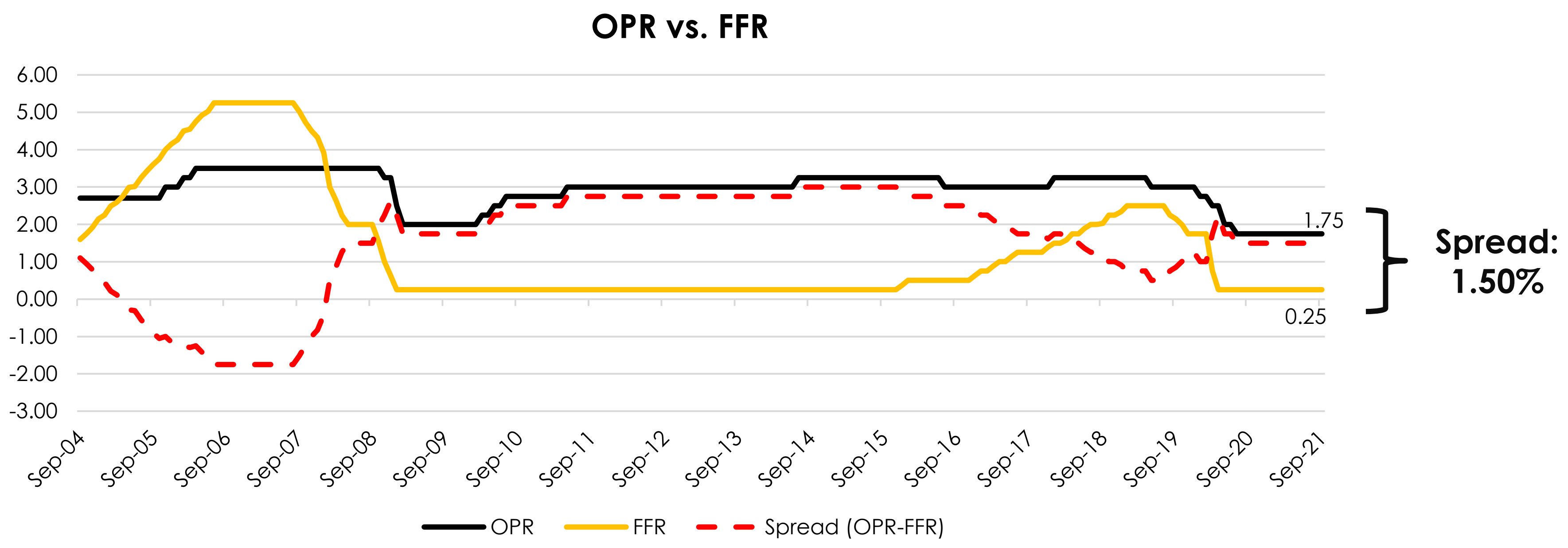
September 2021 FOMC Meeting



Source: The US Federal Reserve Summary Of Economic Projections

- ✓ Notwithstanding the absence on the exact timeline to taper asset purchases, the Fed noted that the gradual tapering of asset purchases will conclude by the end of mid-2022 provided that the economic recovery remains on track.
- ✓ Assuming that tapering activities will begin in December this year and end by end of June next year, the size of the scale down of asset purchases comes into question.
- ✓ In meantime, the Fed will continue to increase its holdings of Treasury securities by at least USD120.0 billion (USD80.0 billion of Treasury securities and USD40.0 billion of agency mortgage-backed securities) until the Fed officially announces the tapering plans.

OVERNIGHT POLICY RATE (OPR) VS. FEDERAL FUND RATE (FFR)



Source: CEIC

- ✓ As of today, the difference between Malaysia's OPR and FFR remains at 150 basis points (bps) (1.75% minus 0.25%) since July last year.
- ✓ This suggested that Bank Negara Malaysia (BNM) still has room for a possible OPR reduction if such decision lies solely on the interest rate differentials with the FFR.
- ✓ Assuming that the Fed is likely to normalize its benchmark rate to 2.50% (long run FFR), the OPR could reach 3.50% in order to maintain a reasonable spread with the FFR.
- ✓ In view of the on-going pandemic situation at the current juncture, a tightening monetary policy would be hasty considering that most of the consumers, as well as businesses including small-business owners have been struggling mightily through the Covid-19 crisis.

CENTRAL BANK POLICY RATES

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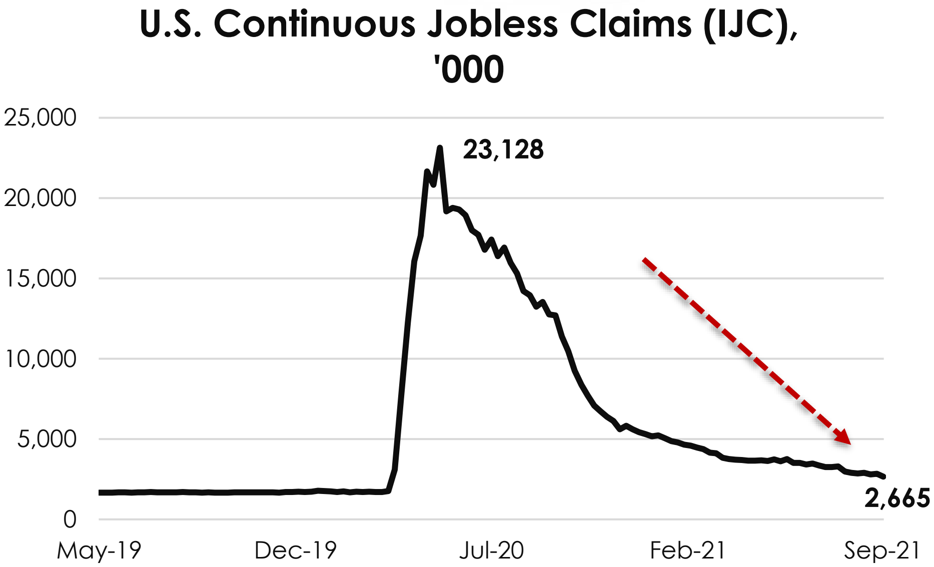
Policy rates	Sep-20	Oct-20	Nov-20	Dec-20	Jan-21	Feb-21	Mar-21	Apr-21	May-21	Jun-21	Jul-21	Aug-21	Sep-21*
Advanced countries													
US (Fed Fund Rate)	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
Japan (Policy Balance Rate)	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10
Euro Zone (Main Refinancing Rate)	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
UK (Bank Rate)	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
Canada (ON Lending Rate)	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
Latin America													
Mexico (ON Rate)	4.25	4.25	4.25	4.25	4.25	4.00	4.00	4.00	4.00	4.25	4.25	4.50	4.50
Brazil (Selic Rate)	2.00	2.00	2.00	2.00	2.00	2.00	2.75	2.75	3.50	4.25	4.25	5.25	6.25
Argentina (LELIQ 7D Notes Rate)	38.00	36.00	38.00	38.00	38.00	38.00	38.00	38.00	38.00	38.00	38.00	38.00	38.00
Eastern Europe													
Russia (Key Rate)	4.25	4.25	4.25	4.25	4.25	4.25	4.50	5.00	5.00	5.50	6.50	6.50	6.75
Ukraine (Discount Rate)	6.00	6.00	6.00	6.00	6.00	6.00	6.50	7.50	7.50	7.50	8.00	8.00	8.50
Turkey (1W Repo Rate)	10.25	10.25	15.00	17.00	17.00	17.00	19.00	19.00	19.00	19.00	19.00	19.00	19.00
Asia													
China (1Y Loan Prime Rate)	3.85	3.85	3.85	3.85	3.85	3.85	3.85	3.85	3.85	3.85	3.85	3.85	3.85
India (Repo Rate)	4.00	4.00	4.00	4.00	4.00	4.00	4.00	4.00	4.00	4.00	4.00	4.00	4.00
Indonesia (7D Repo Rate)	4.00	4.00	3.75	3.75	3.75	3.50	3.50	3.50	3.50	3.50	3.50	3.50	3.50
Thailand (1D Repo Rate)	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
South Korea (Base Rate)	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.75	0.75
Philippines (O/N Lending Rate)	2.25	2.25	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00
Australia (Cash Rate)	0.25	0.25	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
New Zealand (Cash Rate)	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
Malaysia (OPR)	1.75	1.75	1.75	1.75	1.75	1.75	1.75	1.75	1.75	1.75	1.75	1.75	1.75

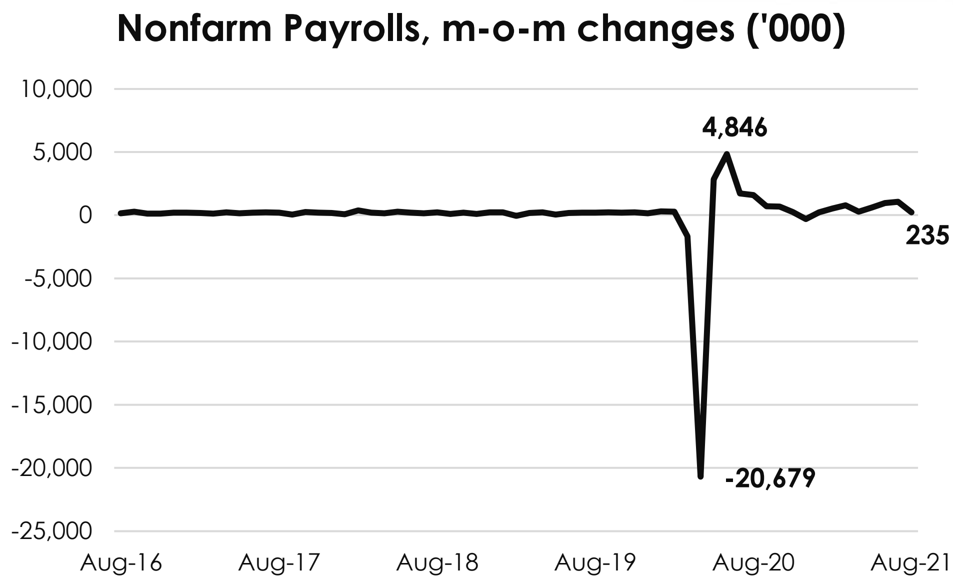
As at 23 September 2021

Source: Bloomberg

- ✓ We have seen few central banks decided to increase their benchmark interest rate in September to contain the inflationary pressure.
- ✓ Yesterday, the Central Bank of Brazil has raised the Selic rate by 100 bps to 6.25% and is expected to do another adjustment of same magnitude for the next meeting. At the current stage, the policymakers consider this pace is the most appropriate to guarantee inflation convergence to the target at the relevant horizon. Thus far, the inflation target for 2021, 2022 and 2023 stood at 6.8%, 3.8% and 3.25% respectively.

LABOUR MARKET IS GRADUALLY IMPROVING





Sources: CEIC, US Department of Labor

- ✓ The number of Americans who have been receiving unemployment benefits fell to 2.67 billion for the week ended 4 September from 2.85 billion in the preceding week. This is a fresh pandemic low since March last year, suggesting that the labour market recovery is still on track.
- ✓ Thus far, the U.S. economy added 235k number of jobs in August, though at a softer pace as compared to 1,053k number of jobs offered in the preceding month. The slower jobs creation last month was mainly contributed by the surge in Covid-19 infections linked to the Delta variant. However, we believe the pace was enough to sustain the economic expansion moving forward.
- ✓ Apart from that, we can see that the unemployment rate in the U.S. dropped to 5.2% in August (July: 5.4%), the lowest since March last year, following broader reopening of economy in the U.S. As such, there will be more reasons for the Fed to consider to start their tapering asset purchases soon.
- ✓ Should businesses continue to scale up operations smoothly and proceed with further rehiring later in 2022, the Fed's goal of maximum employment could be reached, fulfilling one of the criteria to begin moving away from its accommodative monetary policy.

THE U.S. INFLATION RATE IS STILL EXACERBATED BY SUPPLY CHAIN PRESSURES BUT HAS RECENTLY SHOWN SIGNS OF SLOWING DOWN

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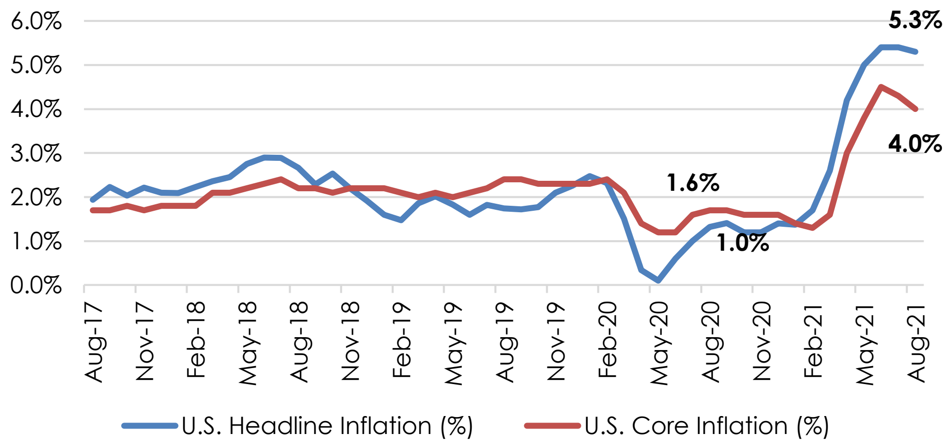
U.S. Headline Inflation vs. U.S. Core Inflation (%)



Source: CEIC

Congestion at the Port of Long Beach

Source: Freight Waves

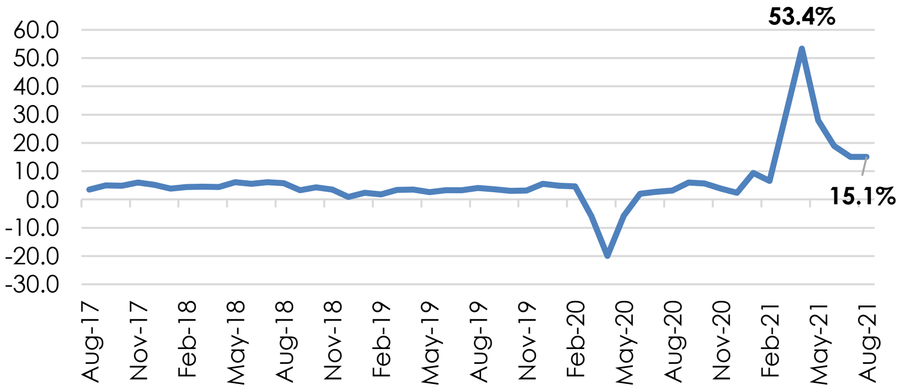
- ✓ The U.S. inflation rate reached 5.3% y-o-y in August (July: 5.4%) while the U.S. core inflation stood at 4.0% in the same month (July: 4.3%).
- ✓ Although there has been signs of slowdown, the current inflation trend in the U.S. is still partly due to the low base effect combined with the supply chain bottleneck.
- ✓ The vulnerability of the supply chain can be seen from the congestion at the Port of Long Beach in the east cost of the U.S. To illustrate this, there were 70 container ships in queue with a total capacity of 432,909 twenty-foot equivalent units (TEUs) on 20 September alone, which is higher than the inbound container volume that Port of Long Beach handled in the entire month of August of 419,475 TEUs.
- ✓ Nevertheless, inflationary pressures are expected to wane further in 2022 when the supply chain bottleneck eases as manufacturers are likely to ramp up production and manage fulfill more orders. In addition, the spike in inflation seen throughout this year may cause the low base effect in inflation to wear off.
- ✓ As such, the inflation rate in 2022 could gyrate towards the range of 2.0% to 2.5% , in line with Fed's long term inflation expectation goal, With this, one of the Fed's criteria to consider increasing interest rates can be met.

- ✓ **President Biden moves ahead with a plan to increase vaccination rates** – As at 21 September, 54.1% of the U.S. population has been fully vaccinated while 9.0% have only been partly vaccinated. Moving forward, the U.S. President Joe Biden has outlined a broad plan 9 September to increase Covid vaccination rates in the U.S., pressuring private employers to immunize their workforce as well as mandating the shots for federal employees, contractors and health-care workers. With this in mind, the spread of the virus in the U.S. could be contained further.

- ✓ **U.S. retail sales continue to see a double digit y-o-y growth** – Although risks from the Delta variant continue to linger, the U.S. retail sales have continued to record a double digit year-on-year (y-o-y) growth for the past six months from March to August. The growth in retail sales coincides the with the decline in personal savings as a percentage of disposable income in the U.S., reaching 9.6% in July compared to 26.6% in March this year. Notwithstanding this, the personal savings as a percentage of disposable income in the U.S. of 9.6% in August is higher than the 2019 average of 7.6%.

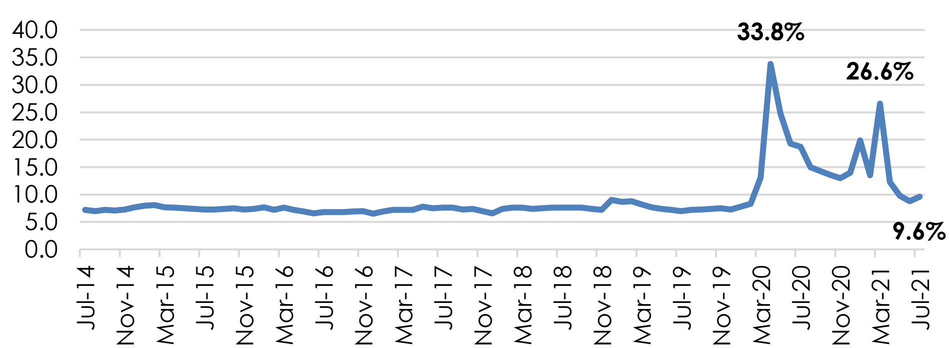
- ✓ **Consumer sentiment in September rebounded after being hit by the Delta variant in the preceding month** – Moreover, the University of Michigan's consumer sentiment for the U.S. edged up to 71.0 points in September from a decade-low of 70.3 points in August, signalling that the impact from the Delta variant may be temporary . It could be the case whereby the U.S. may eventually consider Covid-19 as endemic given its huge population size of 332.8 million, allowing businesses to move on as usual but with adherence to standard operating procedures. With that, it comes to no surprise that more Fed officials are expecting a rate hike in 2022 when the economic expansion becomes more prevalent

U.S. Retail Sales, y-o-y%



Source: CEIC

U.S. Personal Savings As A Percentage Of Disposable Income (%)



Source: CEIC

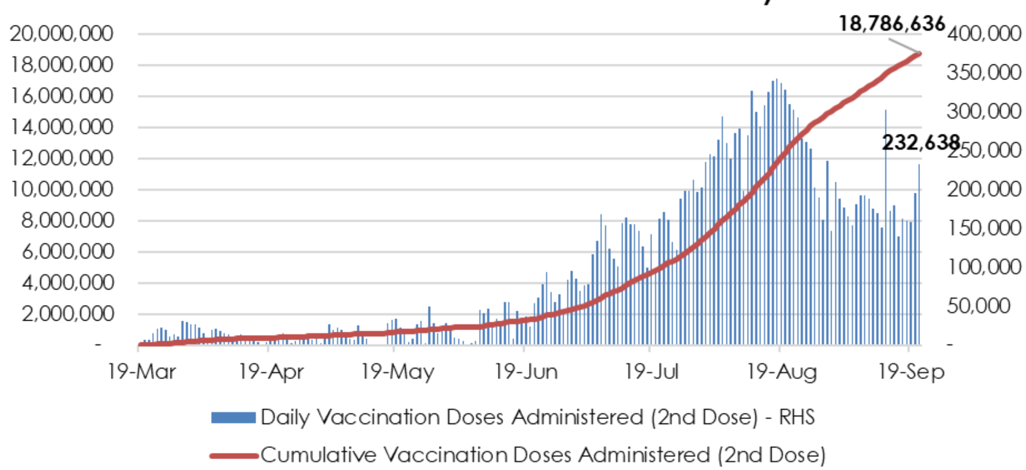
OUR VIEW (CONT'D)

- ✓ **Malaysia's vaccination rate continues to progress smoothly -** So far, 80.2% of Malaysia's total adult population has received two doses of vaccination as at 21 September 2021. Meanwhile, the vaccination programme for children below the age of 18 years has commenced on 8 September with a target of completely inoculating 80.0% of eligible children before school reopens in 2022.

- ✓ **Gradual relaxations to spur more economic activities** – As the country prepares to live with Covid-19 virus, the government has decided to gradually relax movement restrictions with more states transitioning into the remaining phases of the National Recovery Plan (NRP). For instance, Negeri Sembilan has moved into Phase 4 from Phase 3 while Pahang has transitioned into Phase 3 from Phase 2 effective from 24 September. Johor has also progressed into Phase 2 from Phase 1, leaving Kedah to be the only state under Phase 1 of the NRP.

- ✓ **Higher OPR in 2022 is highly likely** – While the pent-up demand following series of lockdown is expected to be reflected in the remaining months of the year, we opine that the ramp up in economic activities will be more broad based next year as more of Malaysia's population including children are vaccinated. In terms of monetary policy, Bank Negara Malaysia will usually view the Fed's timeline to hike rates as a guide but will ultimately determine its decision based on prevailing data points and economic situation. Overall, the pace of economic recovery among different nations appears to be uneven. Therefore, the move towards monetary policy normalization should not be that systemic as each nation has its own set of strengths and weaknesses.

Vaccination Doses Administered in Malaysia



Source: CEIC
Note: As at 21 September 2021

NRP progress effective from 24 September 2021

States			
Phase 1	Phase 2	Phase 3	Phase 4
Kedah	Pulau Pinang	Perlis	Labuan
	Perak		
	Kelantan		
	Sabah	Pahang	
	Federal Territory Of Kuala Lumpur		
	Federal Territory Of Putrajaya	Terengganu	Negeri Sembilan
	Selangor		
	Melaka	Sarawak	
	Johor		

Source: Prime Minister's Office

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APPENDIX

FOMC STATEMENT

- ✓ The Federal Reserve is committed to using its full range of tools to support the U.S. economy in this challenging time, thereby promoting its maximum employment and price stability goals.
- ✓ With progress on vaccinations and strong policy support, indicators of economic activity and employment have continued to strengthen. The sectors most adversely affected by the pandemic have improved in recent months, but the rise in COVID-19 cases has slowed their recovery. Inflation is elevated, largely reflecting transitory factors. Overall financial conditions remain accommodative, in part reflecting policy measures to support the economy and the flow of credit to U.S. households and businesses.
- ✓ The path of the economy continues to depend on the course of the virus. Progress on vaccinations will likely continue to reduce the effects of the public health crisis on the economy, but risks to the economic outlook remain.
- ✓ The Committee seeks to achieve maximum employment and inflation at the rate of 2 percent over the longer run. With inflation having run persistently below this longer-run goal, the Committee will aim to achieve inflation moderately above 2 percent for some time so that inflation averages 2 percent over time and longer-term inflation expectations remain well anchored at 2 percent. The Committee expects to maintain an accommodative stance of monetary policy until these outcomes are achieved. The Committee decided to keep the target range for the federal funds rate at 0 to 1/4 percent and expects it will be appropriate to maintain this target range until labor market conditions have reached levels consistent with the Committee's assessments of maximum employment and inflation has risen to 2 percent and is on track to moderately exceed 2 percent for some time. Last December, the Committee indicated that it would continue to increase its holdings of Treasury securities by at least USD80 billion per month and of agency mortgage-backed securities by at least USD40 billion per month until substantial further progress has been made toward its maximum employment and price stability goals. Since then, the economy has made progress toward these goals. If progress continues broadly as expected, the Committee judges that a moderation in the pace of asset purchases may soon be warranted. These asset purchases help foster smooth market functioning and accommodative financial conditions, thereby supporting the flow of credit to households and businesses.
- ✓ In assessing the appropriate stance of monetary policy, the Committee will continue to monitor the implications of incoming information for the economic outlook. The Committee would be prepared to adjust the stance of monetary policy as appropriate if risks emerge that could impede the attainment of the Committee's goals. The Committee's assessments will take into account a wide range of information, including readings on public health, labor market conditions, inflation pressures and inflation expectations, and financial and international developments.
- ✓ Voting for the monetary policy action were Jerome H. Powell, Chair; John C. Williams, Vice Chair; Thomas I. Barkin; Raphael W. Bostic; Michelle W. Bowman; Lael Brainard; Richard H. Clarida; Mary C. Daly; Charles L. Evans; Randal K. Quarles; and Christopher J. Waller.

MANUFACTURING SECTOR – 15 CONSECUTIVE MONTHS OF GROWTH

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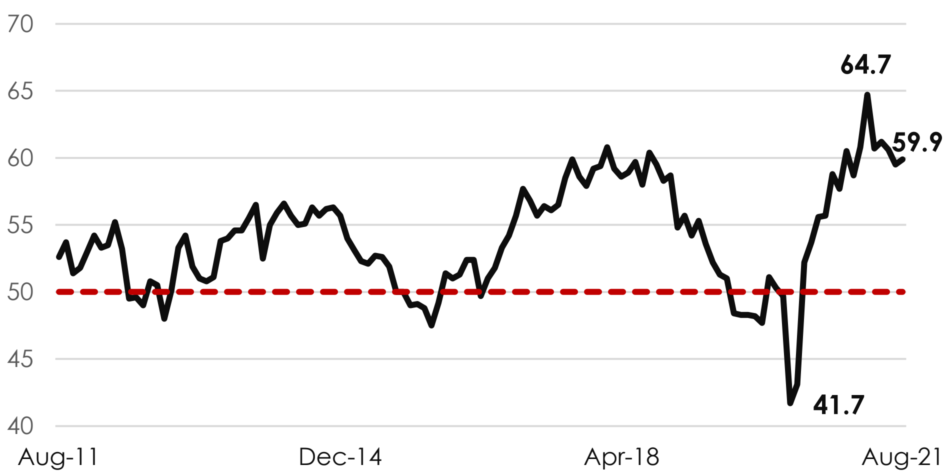
Index	Series Index August 2021	Series Index July 2021	Percentage Point Change	Direction	Rate of Change	Trend (Months)
PMI	59.9	59.5	0.4	Growing	Faster	15
New Orders	66.7	64.9	1.8	Growing	Faster	15
Production	60.0	58.4	1.6	Growing	Faster	15
Employment	49.0	52.9	-3.9	Contracting	From Growing	1
Supplier Deliveries	69.5	72.5	-3.0	Slowing	Slower	66
Inventories	54.2	48.9	5.3	Growing	From Contracting	1
Customers' Inventories	30.2	25.0	5.2	Too Low	Slower	59
Prices	79.4	85.7	-6.3	Increasing	Slower	15
Backlog of Orders	68.2	65.0	3.2	Growing	Faster	14
New Export Orders	56.6	55.7	0.9	Growing	Faster	14
Imports	54.3	53.7	0.6	Growing	Faster	14
OVERALL ECONOMY				Growing	Faster	15
Manufacturing Sector				Growing	Faster	15

Source: US ISM

US ISM Manufacturing PMI, points



Sources: Bloomberg, US ISM

- ✓ According to the US Institute for Supply Management (ISM), Manufacturing Purchasing Manger's Index (PMI) increased to 59.9 points in August from 59.5 points in the preceding month.
- ✓ The growth was mainly contributed by the higher New Orders (August: 66.7 points vs. July: 64.9 points) as demand remained at strong level amid disruptions from the Covid-19 pandemic.
- ✓ Be that as it may, the surge of Covid-19 has led to worker absenteeism, short-term shutdowns due to parts shortages, difficulties in filling open positions, as well as overseas supply chain problems. A such, these continue to limit the manufacturing-growth potential.

MANUFACTURER SENTIMENT IS STILL A MIXED BAG

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Business Sector	Responses from survey
Computer & Electronic Products	Chip shortage is impacting supply lines. Some factories can only operate at 60.0% capacity.
Chemical Products	Extended lead times due to port delays and sea container tightness.
Transportation Equipment	Production is limited due to supply issues with chip. However, still recorded strong sales.
Furniture & Related Products	Booking and sales continue to be sturdy. Notwithstanding that, persistent supply issues has hampered production activities.
Plastics & Rubber Products	Business is going robust, but experiencing labour issues and rising raw material prices.
Food, Beverage & Tobacco Products	Supply chain functions have been challenging. Apart from that, already constrained labor forces is further exacerbated by the pandemic.
Electrical Equipment, Appliances & Components	Business is strong. However, part shortages are their largest business constraint.
Machinery	Customer order backlog continues to climb because they are unable to raise production rates due to supplier parts and manpower challenges.

Source: US ISM

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