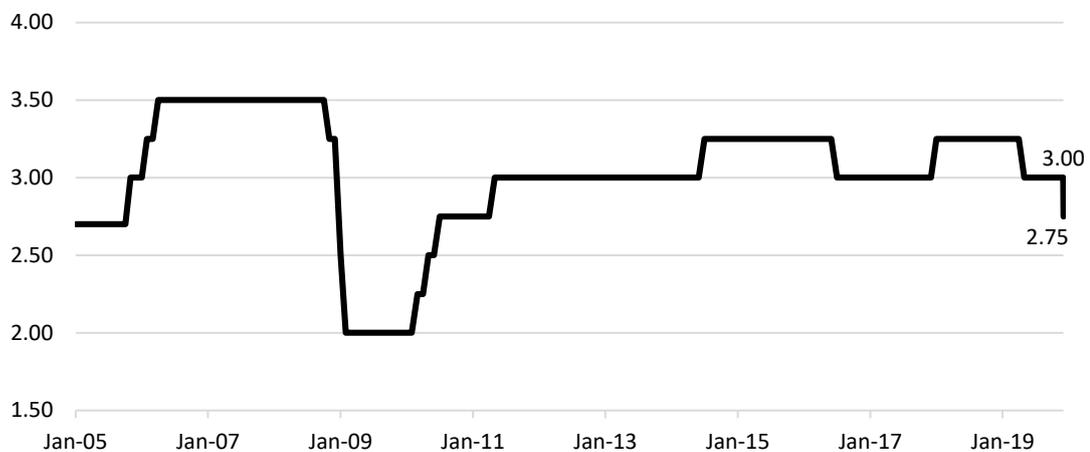


## **BNM cut the OPR by 25 bps to 2.75% while inflation rate remained modest**

### **Facts**

- The Monetary Policy Committee (MPC) has surprised the market, slashing the Overnight Policy Rate (OPR) by 25 basis points (bps) to 2.75% during its first meeting in 2020. The ceiling and floor rates for the OPR have reduced to 3.00% and 2.50% respectively.
- According to the accompanying statement, the economy is expected to grow at a modest pace while easing in trade frictions will continue to support the global trade activities. Nonetheless, heightening geopolitical tensions and policy uncertainty could weigh on the global growth outlook.
- Be that as it may, the MPC members are of the view that domestic economic activities are likely to improve in 2020 supported by public and private sectors.
- The Consumer Price Index (CPI) increased by 1.0% year-on-year (y-o-y) in December from 0.9% growth in the preceding month (Consensus: 1.0%, Bank Islam 1.2%). This was primarily driven by Food & Non-Alcoholic Beverages (December: 1.7% vs. November: 1.5%) and Education (December: 1.7% vs. November: 1.6%).
- On the contrary, Transport (December: -1.9% vs. November: -2.4%) and Clothing & Footwear (December: -1.0% vs. November: -1.1%) declined during December last year.
- Meanwhile, our core inflation which excludes Food & Non-Alcoholic Beverages and Transport sustained its growth during the month at 1.4% (November: 1.4%).
- In 2019, inflation rate has moderated by 0.7%. This was lower compared to 1.0% in the previous year. Nevertheless, the annual core inflation remains elevated at 1.2% in 2019 from 0.6% in 2018.

**Chart 1: Malaysia OPR (%)**



Source: Bloomberg

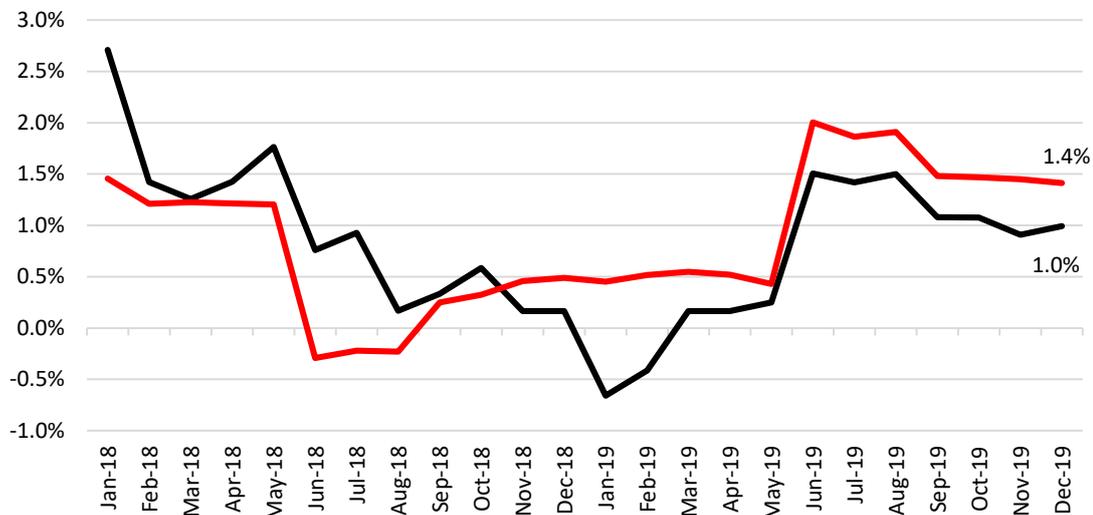
**Table 1: Central Bank Policy Rates**

	Aug-19	Sep-19	Oct-19	Nov-19	Dec-19	Jan-19*
<b>Advanced countries</b>						
US (Fed Fund Rate)	2.25	2.00	1.75	1.75	1.75	1.75
Japan (Policy Balance Rate)	-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
UK (Bank Rate)	0.75	0.75	0.75	0.75	0.75	0.75
Canada (ON Lending Rate)	1.75	1.75	1.75	1.75	1.75	1.75
<b>Latin America</b>						
Mexico (ON Rate)	8.00	7.75	7.75	7.50	7.25	7.25
Brazil (Selic Rate)	6.00	5.50	5.00	5.00	4.50	4.50
Argentina (7D Reference Rate)	83.26	78.37	68.00	63.00	55.00	50.00
<b>Eastern Europe</b>						
Russia (Key Rate)	7.25	7.00	6.50	6.50	6.25	6.25
Ukraine (Discount Rate)	17.00	16.50	15.50	15.50	13.50	13.50
Turkey (1W Repo Rate)	19.75	16.50	14.00	14.00	12.00	11.25
<b>Asia</b>						
China (Loan Prime Rate 1 Year)	4.25	4.20	4.20	4.15	4.15	4.15
India (Repo Rate)	5.40	5.40	5.15	5.15	5.15	5.15
Indonesia (7D Repo Rate)	5.50	5.25	5.00	5.00	5.00	5.00
Thailand (1D Repo Rate)	1.50	1.50	1.50	1.25	1.25	1.25
South Korea (Base Rate)	1.50	1.50	1.25	1.25	1.25	1.25
Philippines (O/N Lending Rate)	4.25	4.00	4.00	4.00	4.00	4.00
Australia (Cash Rate)	1.00	1.00	0.75	0.75	0.75	0.75
New Zealand (Cash Rate)	1.00	1.00	1.00	1.00	1.00	1.00
Malaysia (OPR)	3.00	3.00	3.00	3.00	3.00	2.75

\*As of 22 January 2020

Source: Bloomberg

**Chart 2: Consumer Price Index (CPI), y-o-y %**



Source: CEIC, DOSM, Bank Islam

**Table 2: Consumer Price Index (CPI), y-o-y %**

	Weight	Aug-19	Sep-19	Oct-19	Nov-19	Dec-19	2018	2019
<b>Consumer Price Index</b>	<b>100.0%</b>	<b>1.5%</b>	<b>1.1%</b>	<b>1.1%</b>	<b>0.9%</b>	<b>1.0%</b>	<b>1.0%</b>	<b>0.7%</b>
Food and Non Alcoholic Beverages	29.5%	2.6%	2.2%	1.8%	1.5%	1.7%	1.6%	1.6%
Alcoholic Beverages and Tobacco	2.4%	2.5%	2.4%	2.2%	0.4%	0.2%	-0.1%	1.5%
Clothing and Footwear	3.2%	-1.1%	-0.9%	-1.3%	-1.1%	-1.0%	-2.0%	-1.9%
Housing, Water, Electricity, Gas & Other Fuels	23.8%	1.8%	1.6%	1.6%	1.7%	1.7%	2.0%	1.9%
Furnishings, Household Equipment and Maint.	4.1%	3.2%	2.1%	1.7%	1.5%	1.4%	0.4%	1.4%
Health	1.9%	1.4%	1.3%	1.4%	1.4%	1.4%	0.8%	0.6%
Transport	14.6%	-2.1%	-2.2%	-2.3%	-2.4%	-1.9%	1.5%	-3.1%
Communication	4.8%	2.2%	-0.1%	1.5%	1.5%	1.5%	-1.8%	0.4%
Recreation and Culture	4.8%	2.3%	0.8%	0.7%	0.8%	0.6%	-0.4%	0.7%
Education	1.3%	1.4%	1.8%	1.9%	1.6%	1.7%	1.1%	1.4%
Restaurants and Hotels	2.9%	1.7%	1.4%	1.2%	1.1%	1.1%	1.5%	1.2%
Miscellaneous Goods and Services	6.7%	2.5%	2.7%	2.2%	2.5%	2.4%	-1.4%	0.4%
<b>Core CPI (excluding F&amp;B and Transport)</b>		<b>1.9%</b>	<b>1.5%</b>	<b>1.5%</b>	<b>1.4%</b>	<b>1.4%</b>	<b>0.6%</b>	<b>1.2%</b>

Source: CEIC, DOSM, Bank Islam

## Our View

We must admit that we were caught off guard. We thought the decision would come in perhaps in May as the BNM would want to wait for the FTSE Russell review in March. The central bank has indicated that it is a pre-emptive move to secure the improving growth trajectory amid price stability. It also said that the current monetary stance is appropriate in sustaining economic growth with price stability. In other words, the central bank is very mindful on the external development and would be data-dependent in deciding their next course of actions. We believe inflation is not an issue given that the government has decided to put on hold the targeted fuel subsidy program indefinitely. Fuels & Lubricating Personal Transport Equipment accounted for 8.5% of total weight in the Consumer Price Index (CPI) whereby RON95 is also embedded in this category. Should RON95 prices remained at RM2.08 per liter in 2020, it could bring down the inflation rate to below 1.00%. Apart from that, the expected reduction in the toll rates in major highways could also help to ease the inflation rate during the year although the representation of highways in the CPI is small circa 0.40%. As such, rooms for additional OPR reduction is widely open. However, at this juncture, we believe the BNM would want to maintain the prevailing OPR throughout the year subject to the evolving economic outlook globally.

## Appendix

### Monetary Policy Statement

At its meeting today, the Monetary Policy Committee (MPC) of Bank Negara Malaysia decided to reduce the Overnight Policy Rate (OPR) to 2.75%. The ceiling and floor rates of the corridor of the OPR are correspondingly reduced to 3.00% and 2.50%, respectively.

The global economy continues to expand at a moderate pace. Latest indicators and the recent dissipation of trade tensions point to improving global trade activity. Monetary easing across major economies in the second half of 2019 has helped ease financial conditions, and is expected to continue to support economic activity. However, downside risks remain due to geopolitical tensions and policy uncertainties in a number of countries. This could cause a resurgence of financial market volatility and weigh on the global growth outlook.

For the Malaysian economy, latest indicators and supply disruptions in commodity-related sectors point to moderate expansion of economic activity in the fourth quarter. For 2019, growth will be within the projected range. For 2020, growth is expected to gradually improve, with continued support from household spending and better export performance. Overall investment activity is expected to record a modest recovery, underpinned by ongoing and new projects, both in the public and private sectors. However, downside risks to growth remain. These include uncertainty from various trade negotiations, geopolitical risks, weaker-than-expected growth of major trade partners, heightened volatility in financial markets, and domestic factors that include weakness in commodity-related sectors and delays in the implementation of projects.

Headline inflation averaged at 0.7% in 2019. In 2020, headline inflation is expected to average higher but remain modest. The trajectory of headline inflation will be dependent on global oil and commodity price developments and the timing of the lifting of the domestic retail fuel price ceilings. Underlying inflation is expected to remain broadly stable, reflecting the continued expansion in economic activity and the absence of strong demand pressures.

The adjustment to the OPR is a pre-emptive measure to secure the improving growth trajectory amid price stability. At this current level of the OPR, the MPC considers the stance of monetary policy to be appropriate in sustaining economic growth with price stability.

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