Economic Research, Strategic Management
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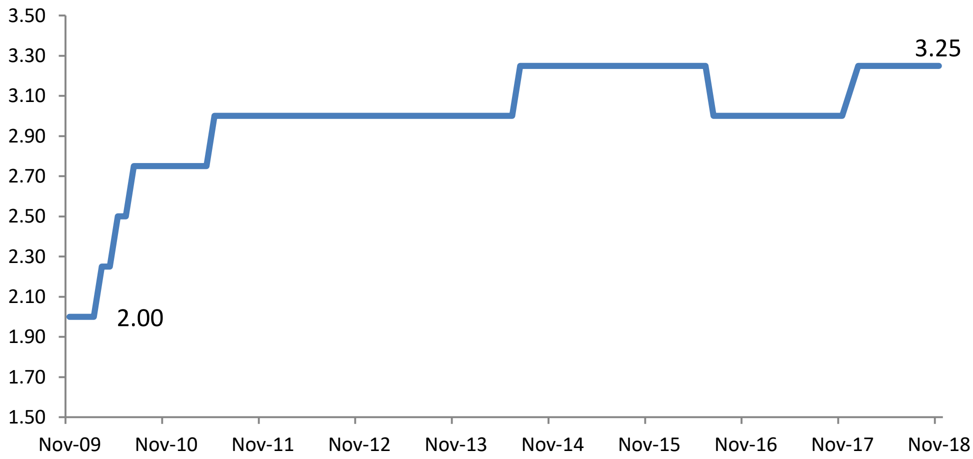
OPR at 3.25%, BNM increasingly dovish

Facts

- The BNM decided to maintain the Overnight Policy Rate (OPR) at 3.25% during the Monetary Policy Committee (MPC) meeting today. This is also marks the last MPC meeting for 2018.
- In the accompanying statement, the BNM is of the view that the balance of risks to the global growth outlook has tilted on the downside while volatility in the financial markets and monetary policy normalization in the advanced economies are expected to result in capital outflows in the emerging economies.
- Domestically, the private sector especially household spending will be the key driver to Malaysian economy while government will remain cautious on its spending program amid the reprioritization of development projects. However, there are more policy clarity from the government following the recent Budget 2019 announcement last week.
- With respect to inflation, 2018 is likely to be muted with the first nine months CPI currently hovering at 1.2% (2017: 3.7%). However, inflation rate is expected to creep up in 2019 due to the expected upward adjustment in fuel prices due to higher global oil prices as well as the adoption of floating retail fuel prices next year.
- At the current juncture, the prevailing OPR level is very much aligned with the degree of monetary accommodation.

Chart 1: Overnight Policy Rate (OPR)



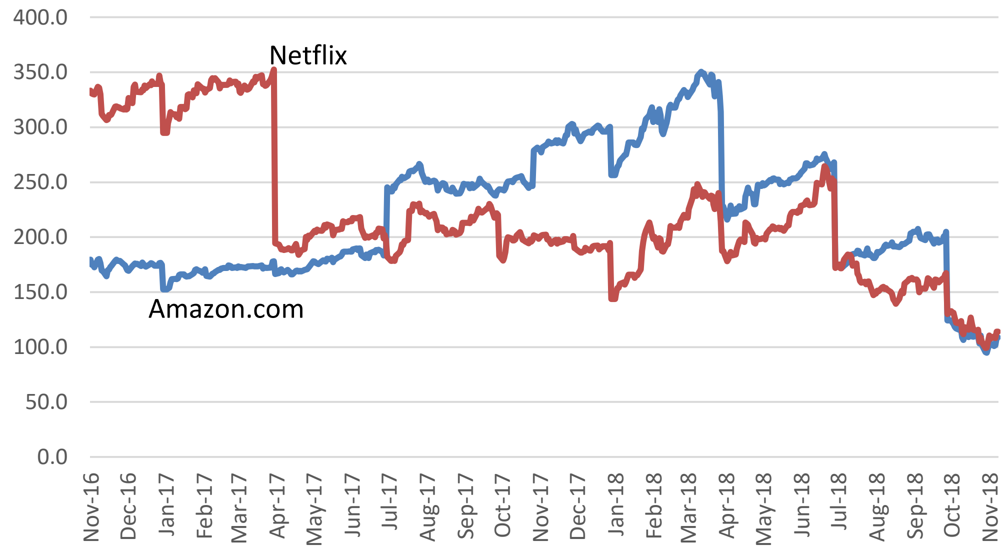
Sources: CEIC & BNM

Our view

After raising the OPR by 25 basis points in January this year, the policy rates have remained unchanged at 3.25%. While other economies in this region such as Indonesia and Philippines have been increasing their interest rates to fend off capital outflows, our central bank has remain unperturbed. We expect such resolve exemplified by the BNM will be retained next year as the country is not about to turn into twin deficits (fiscal and current account deficits) following the reprioritization of mega infrastructure projects especially the rail related projects, which typically command higher import content. Stability in the policy rates should allow conducive environment for private investment to expand further especially the export-oriented industries. Sectors such as Electrical & Electronics (E&E), Rubber Gloves and to some extent, Healthcare as well as Oil & Gas have been actively incurring capital expenditure in order to upgrade its production capacity.

Having said that, the evolving economic outlook will be the key determining factor for OPR adjustment. As such, the BNM will be rigorously data-dependent going forward especially in the context of flattening yield curve in the US. In addition, the correction in Price-Earnings (PE) multiples in key technology companies such as Amzon.com and Netflix could also serve as a reminder that equity prices could experience a bumpy ride next year. **Overall, we expect the BNM would incline to keep the OPR at 3.25% in 2019**.

Chart 2: Price-to-Earnings (PE) ratio (times)



Source: Bloomberg