From the Desk of the Chief Economist

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THE FIRST RATE HIKE SINCE 2018

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ECONOMIC RESEARCH

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THE FOMC INCREASED THE FEDERAL FUND RATE (FFR) BY 25 BPS

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The Federal Open Market Committee (FOMC) **decided to raise the FFR target range by 25 basis points (bps) to 0.25%-0.50% during its meeting on 15-16 March 2022.**

- ✓ The U.S. economic indicators have been pointing to a strong performance while labour market remains solid.
- ✓ As for inflation, it stays on elevating level amid pandemic-induced supply and demand imbalances, as well as high energy prices.
- ✓ Meanwhile, the implications of Russia-Ukraine conflicts alongside rising commodities prices will constrain economic growth and disrupt global trading activities.

Economic projections of Federal Reserve Board members and Federal Reserve Bank presidents, under their individual assumptions of projected appropriate monetary policy, March 2022

Percent

Variable	Median[1]				Central Tendency[2]				Range[3]			
	2022	2023	2024	Longer run	2022	2023	2024	Longer run	2022	2023	2024	Longer run
Change in real GDP	2.8	2.2	2.0	1.8	2.5–3.0	2.1–2.5	1.8–2.0	1.8–2.0	2.1–3.3	2.0–2.9	1.5–2.5	1.6–2.2
December projection	4.0	2.2	2.0	1.8	3.6–4.5	2.0–2.5	1.8–2.0	1.8–2.0	3.2–4.6	1.8–2.8	1.7–2.3	1.6–2.2
Unemployment rate	3.5	3.5	3.6	4.0	3.4–3.6	3.3–3.6	3.2–3.7	3.5–4.2	3.1–4.0	3.1–4.0	3.1–4.0	3.5–4.3
December projection	3.5	3.5	3.5	4.0	3.4–3.7	3.2–3.6	3.2–3.7	3.8–4.2	3.0–4.0	2.8–4.0	3.1–4.0	3.5–4.3
PCE inflation	4.3	2.7	2.3	2.0	4.1–4.7	2.3–3.0	2.1–2.4	2.0	3.7–5.5	2.2–3.5	2.0–3.0	2.0
December projection	2.6	2.3	2.1	2.0	2.2–3.0	2.1–2.5	2.0–2.2	2.0	2.0–3.2	2.0–2.5	2.0–2.2	2.0
Core PCE inflation[4]	4.1	2.6	2.3		3.9–4.4	2.4–3.0	2.1–2.4		3.6–4.5	2.1–3.5	2.0–3.0	
December projection	2.7	2.3	2.1		2.5–3.0	2.1–2.4	2.0–2.2		2.4–3.2	2.0–2.5	2.0–2.3	
Memo: Projected appropriate policy path												
Federal funds rate	1.9	2.8	2.8	2.4	1.6–2.4	2.4–3.1	2.4–3.4	2.3–2.5	1.4–3.1	2.1–3.6	2.1–3.6	2.0–3.0
December projection	0.9	1.6	2.1	2.5	0.6–0.9	1.4–1.9	1.9–2.9	2.3–2.5	0.4–1.1	1.1–2.1	1.9–3.1	2.0–3.0

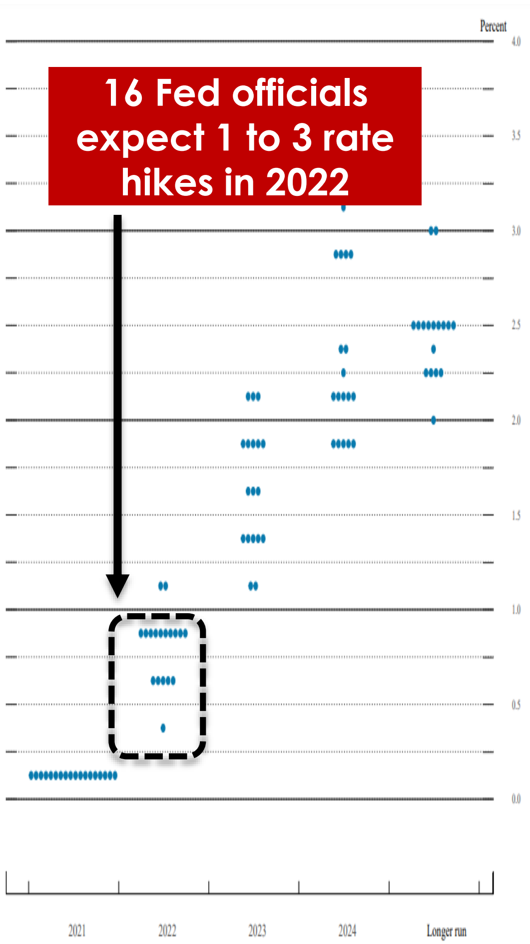
Source: Federal Reserve

- ✓ On Gross Domestic Product (GDP), the FOMC member sliced the 2022 forecast from 4.0% growth to 2.8% as ***the impacts on the U.S. economy is highly uncertain***.
- ✓ The inflation forecast for 2022 was bumped up to 4.3% from 2.6% projection made during December 2021 meeting as supply disruptions have been larger and longer than anticipated while soaring energy prices are pushing up the inflation.
- ✓ On the other hand, the Unemployment Rate (UR) is likely to remain strong at 3.5% following labour demand remains tight as employers are having difficulties to fill the job openings.
- ✓ All in all, the Committee seeks to achieve maximum employment and inflation at the rate of 2.0% over the longer run.
- ✓ In support of these goals, the FOMC will continue to monitor the implications of incoming information for the economic outlook and be prepared to adjust the stance of monetary policy as appropriate if risks emerge.

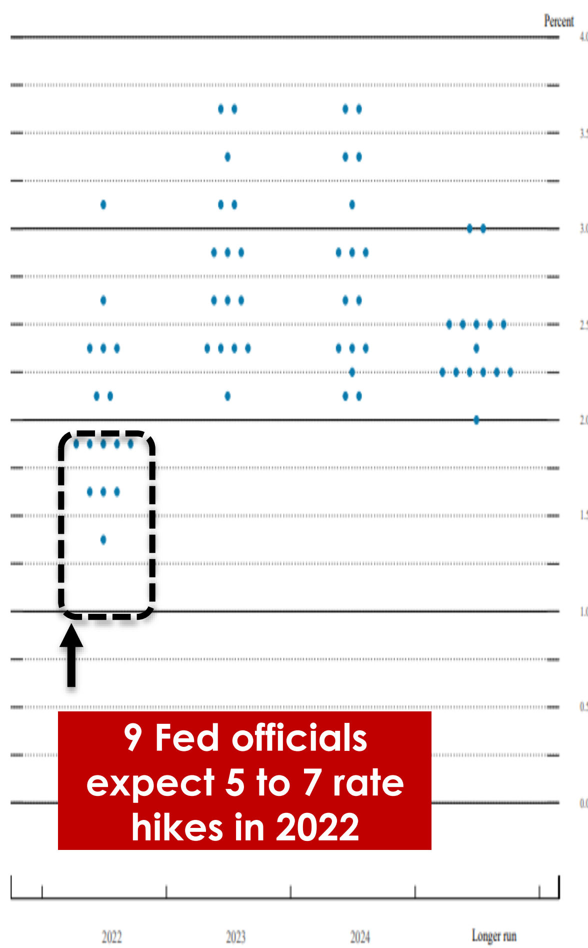
THE FED HAS SIGNALLED THAT ANOTHER RATE HIKE IS ON THE CARD AND BALANCE SHEET REDUCTION COULD START IN MAY

The dot plot- the Fed uses to signal its outlook for the path of interest rates.

December 2021 FOMC Meeting



March 2022 FOMC Meeting



Source: Federal Reserve

- ✓ The latest dot plot indicates that **9 Fed officials expect rate hikes between 125 bps and 175 bps** this year.
- ✓ Additionally, the **median projection for the appropriate level of the FFR is 1.9%** by the end of 2022, representing a full percentage point higher than projected in December 2021 (0.9%).
- ✓ Apart from that, the Committee made good progress on a plan for reducing securities holdings and beginning of balance sheet reduction will be announced during upcoming meeting.
- ✓ Judging form this, myriad factors have combined to force the Fed's hand on inflation.
- ✓ Be that as it may, the economic outlook remains cloudy as the focus has shifted from the Covid-19 pandemic to Russia's invasion of Ukraine that could push the upward price pressure further.

CENTRAL BANK POLICY RATES- THE BEGINNING OF THE REMOVAL OF POLICY ACCOMMODATION

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Policy rates	Mar-21	Apr-21	May-21	Jun-21	Jul-21	Aug-21	Sep-21	Oct-21	Nov-21	Dec-21	Jan-22	Feb-22	Mar-22*
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	0.50
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	0.25	0.25	0.50	0.50
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	0.50
Latin America													
Mexico (ON Rate)	4.00	4.00	4.00	4.25	4.25	4.50	4.75	4.75	5.00	5.50	5.50	6.00	6.00
Brazil (Selic Rate)	2.75	2.75	3.50	4.25	4.25	5.25	6.25	7.75	7.75	9.25	9.25	10.75	11.75
Argentina (LELIQ 7D Notes Rate)	38.00	38.00	38.00	38.00	38.00	38.00	38.00	38.00	38.00	38.00	40.00	42.50	42.50
Eastern Europe													
Russia (Key Rate)	4.50	5.00	5.00	5.50	6.50	6.50	6.75	7.50	7.50	8.50	8.50	20.00	20.00
Ukraine (Discount Rate)	6.50	7.50	7.50	7.50	8.00	8.00	8.50	8.50	8.50	9.00	10.00	10.00	10.00
Turkey (1W Repo Rate)	19.00	19.00	19.00	19.00	19.00	19.00	18.00	16.00	15.00	14.00	14.00	14.00	14.00
Asia													
China (1Y Loan Prime Rate)	3.85	3.85	3.85	3.85	3.85	3.85	3.85	3.85	3.85	3.80	3.70	3.70	3.70
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)	3.50	3.50	3.50	3.50	3.50	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	0.75	0.75	0.75	1.00	1.00	1.25	1.25	1.25
Philippines (O/N Lending Rate)	2.00	2.00	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)	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
New Zealand (Cash Rate)	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.50	0.75	0.75	0.75	1.00	1.00
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

Source: Bloomberg
*As at 17 March 2022

- ✓ Bank of Canada has raised its policy interest rate from 0.25% to 0.50% on 2 March to bring runaway inflation under control, while noting that the current war in Ukraine was a major new source of uncertainty.
- ✓ Similarly, the Central Bank of Brazil raised its key interest rate for ninth straight time by 100 basis bps to 11.75% on 16 March 2022. The tighter monetary policy is needed to combat spiraling prices driven upward by the fallout of the coronavirus pandemic, as well as Russia's invasion of Ukraine.
- ✓ Meanwhile, while maintaining the interest rate at 0.00%, the European Central Bank (ECB) decided to revise purchase schedule for its asset purchase programme (APP) for the upcoming months on 10 March. The monthly net purchases under APP will amount to EUR40.0 billion in April, EUR30.0 billion in May and EUR20.0 billion in June.

UKRAINE-RUSSIA WAR EFFECT TO SPUR INFLATION HIGHER IN THE U.S.

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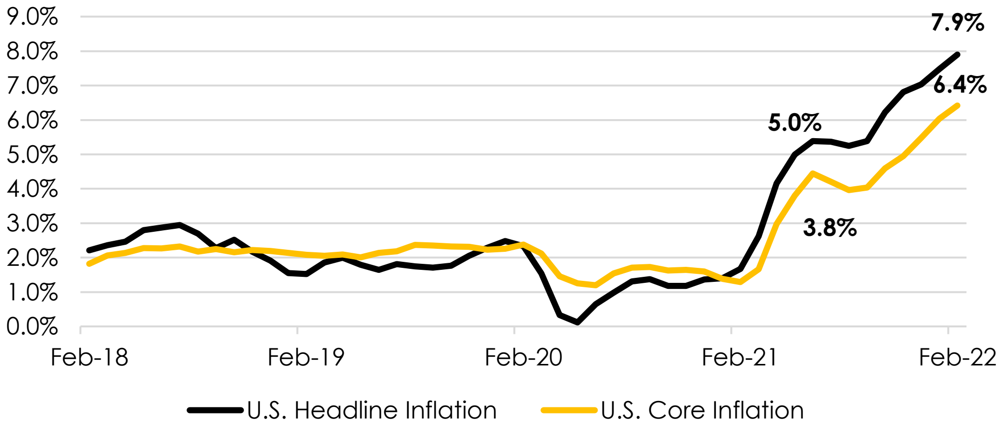
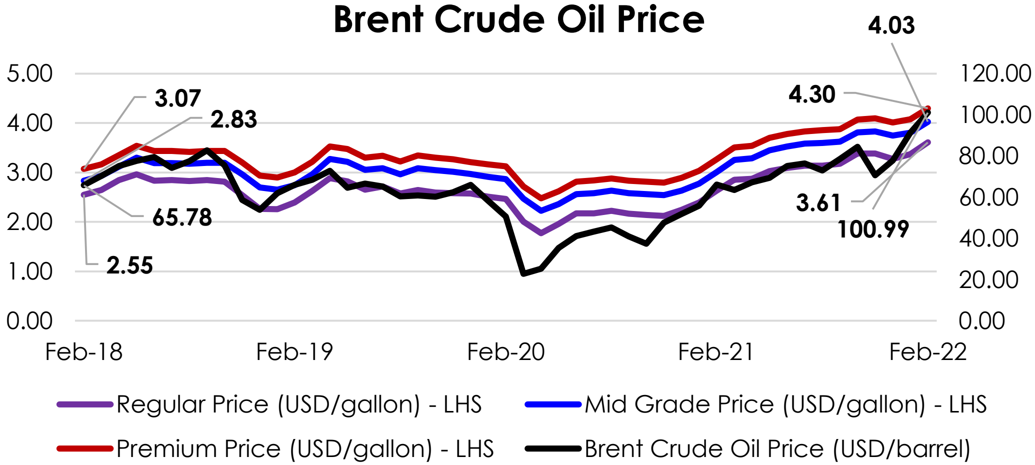
U.S. Headline Inflation vs. U.S. Core Inflation, y-o-y%



Different Grade of U.S. Gasoline Prices vs. Brent Crude Oil Price



Sources: Bloomberg, CEIC

- ✓ The U.S. inflation rate continued to climb high to reach 7.9% y-o-y in February (January: 7.5%), marking a new record pace in 40 years since 1982. Similarly, the core inflation maintained its upward trend to 6.4% in the said month (January: 6.0%).
- ✓ It is no doubt that Russia's invasion of Ukraine on 24 February has been the biggest factor boosting the already-high inflation in the country.
- ✓ The ongoing conflict between the two countries has triggered big increases in the cost of oil, wheat and other commodities.
- ✓ For instance, all grades of U.S. gasoline prices surged by more than 30.0% y-o-y which translates into 25.6% increase in the price of consumer index for energy during the month (January: 27.0%).
- ✓ The inflation for the month of February caught only the start of surge in gas prices following the geopolitical war late last month.
- ✓ Subsequently, economists expect that inflation could pick up even more in March amid prices at the pump have jumped to record-breaking highs. According to American Automobile Association (AAA), the average price for a gallon of gas was USD4.31 as of 16 March 2022.
- ✓ With the Europe's recent development, ongoing supply constraints, strong demand, as well as labour shortages, these will likely to maintain inflation elevated for longer.

U.S. LABOUR MARKET – MOMENTUM REMAINS COMMENDABLE

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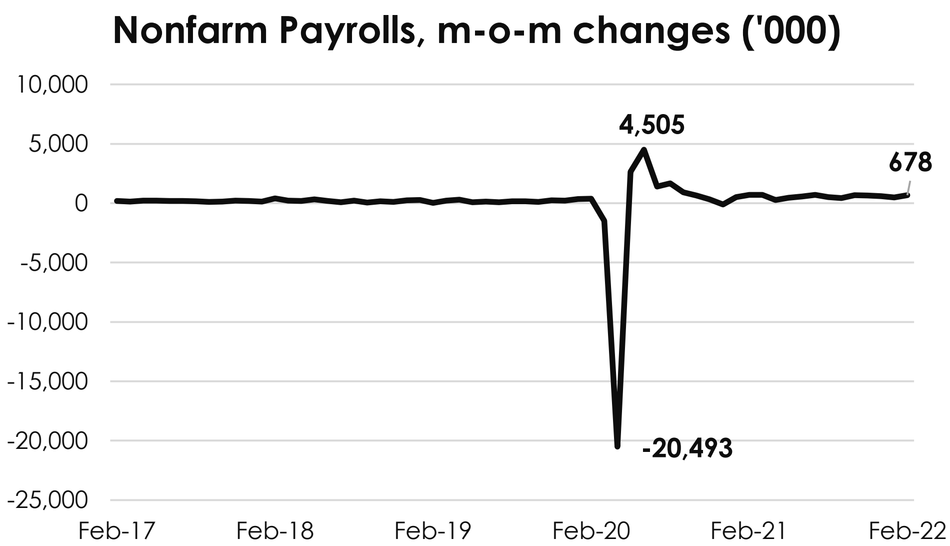

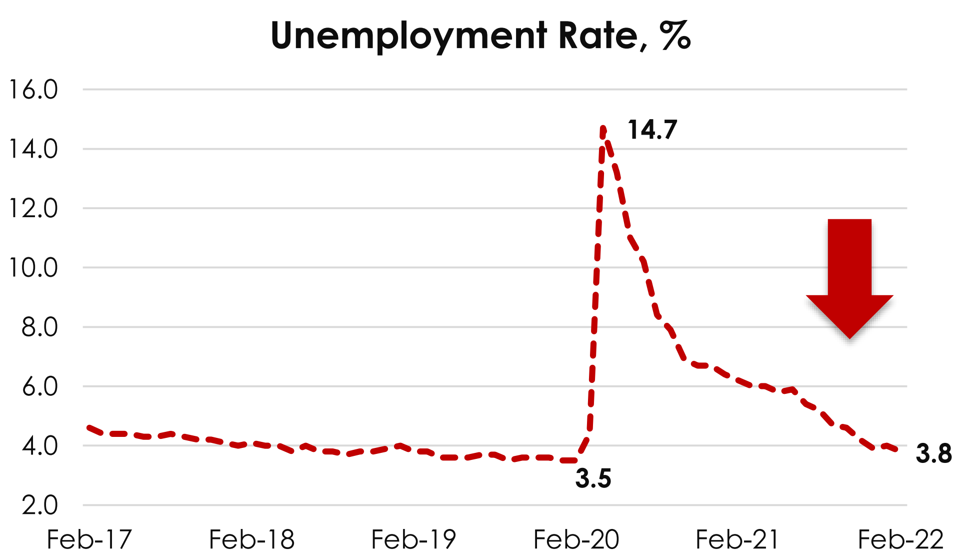

Source: CEIC

- ✓ February's jobs report reflected a continuous improvement in the U.S. labor recovery with unemployment rate declined to 3.8% (January: 4.0%), the lowest since February 2020 at 3.5%.
- ✓ Apart from that, total nonfarm payroll employment rose by 678,000 in February, higher than 481,000 number of jobs added in the previous month, suggesting solid employment gains.
- ✓ Be that as it may, we anticipate that the rising headwinds from the geopolitical tensions could hurt businesses confidence, affecting job growth in the months ahead.

BRACE FOR RINGGIT VOLATILITY

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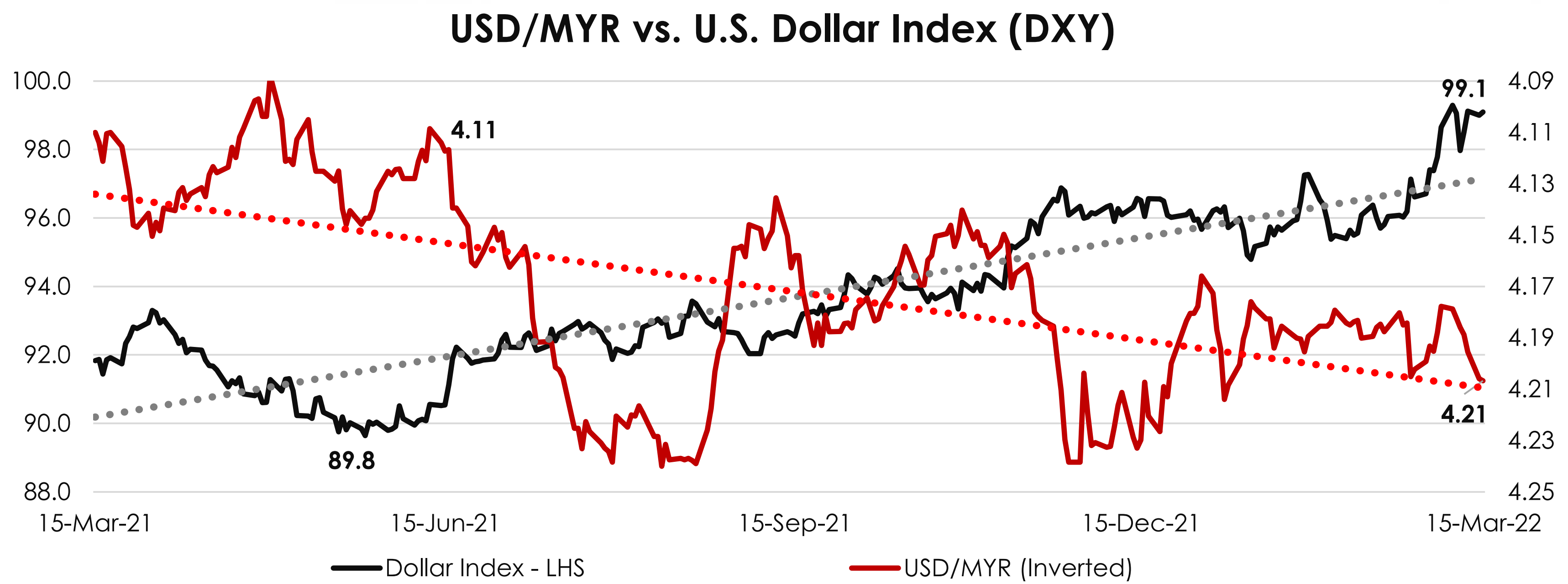
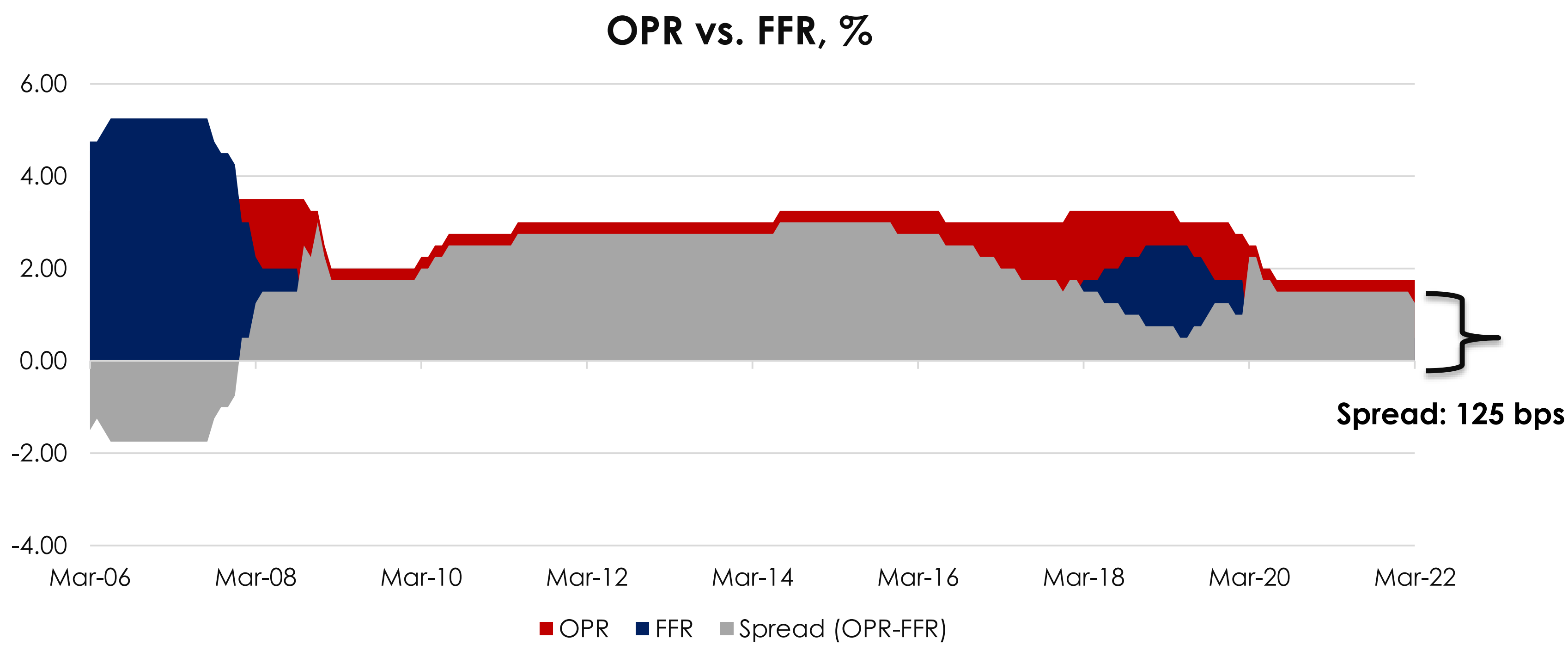


Source: CEIC

- ✓ On the local bourse, the Ringgit has depreciated against the U.S. Dollar as the greenback continues to gain strength.
- ✓ As at 16 March 2022, the Ringgit stood at RM4.20 against the U.S. Dollar while a year ago the Ringgit was at RM4.11, a 2.4% y-o-y loss for Malaysian Ringgit.
- ✓ Following the FFR hike, we anticipate that the Ringgit is likely to come under downside pressure, alongside other Asian countries.
- ✓ Thus far, Japanese Yen is expected to fall further to JPY200.00 (16 March: JPY118.57) against the U.S. Dollar following Western central banks' moves to tighten monetary policy in light of higher inflationary pressure. Already, the Yen has declined to its lowest point in over five years this week.
- ✓ As such, **we revised our USD/MYR forecast for year-end 2022 from RM4.09 to RM4.15.**
- ✓ Such revision was due to the Fed tightening cycle, as well as uncertainty of geopolitical war between Ukraine and Russia. Hence, this will translate into a stronger exchange rate in favour of the U.S. Dollar.

OUR VIEW – HOW THE BANK NEGARA MALAYSIA (BNM) WOULD REACT?



Source: CEIC

- ✓ The BNM is still keeping a cautious approach and will continue to gauge the appropriate monetary policy while ensuring inflation expectation remain anchored.
- ✓ Meanwhile, the escalating geopolitical tension between Russia and Ukraine is expected to disrupt trade flows, stocking risks to global growth and inflation.
- ✓ As such, current stance of monetary policy will remain for now to support the economy that is currently facing an uneven economic recovery.
- ✓ However, **the case for a 25 bps hike of the Overnight Policy Rate (OPR) in the 2H2022** is feasible in our view of high inflationary pressure alongside economic activities that are expected to pick up following the reopening of Malaysia's international border starting 1 April this year.

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APPENDIX

- ✓ Indicators of economic activity and employment have continued to strengthen. Job gains have been strong in recent months, and the unemployment rate has declined substantially. Inflation remains elevated, reflecting supply and demand imbalances related to the pandemic, higher energy prices, and broader price pressures.
- ✓ The invasion of Ukraine by Russia is causing tremendous human and economic hardship. The implications for the U.S. economy are highly uncertain, but in the near term the invasion and related events are likely to create additional upward pressure on inflation and weigh on economic activity.
- ✓ The Committee seeks to achieve maximum employment and inflation at the rate of 2 percent over the longer run. With appropriate firming in the stance of monetary policy, the Committee expects inflation to return to its 2 percent objective and the labor market to remain strong. In support of these goals, the Committee decided to raise the target range for the federal funds rate to 1/4 to 1/2 percent and anticipates that ongoing increases in the target range will be appropriate. In addition, the Committee expects to begin reducing its holdings of Treasury securities and agency debt and agency mortgage-backed securities at a coming meeting.
- ✓ 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; Michelle W. Bowman; Lael Brainard; Esther L. George; Patrick Harker; Loretta J. Mester; and Christopher J. Waller. Voting against this action was James Bullard, who preferred at this meeting to raise the target range for the federal funds rate by 0.5 percentage point to 1/2 to 3/4 percent. Patrick Harker voted as an alternate member at this meeting.

MANUFACTURING SECTOR – PERFORMING FOR 21 CONSECUTIVE MONTHS

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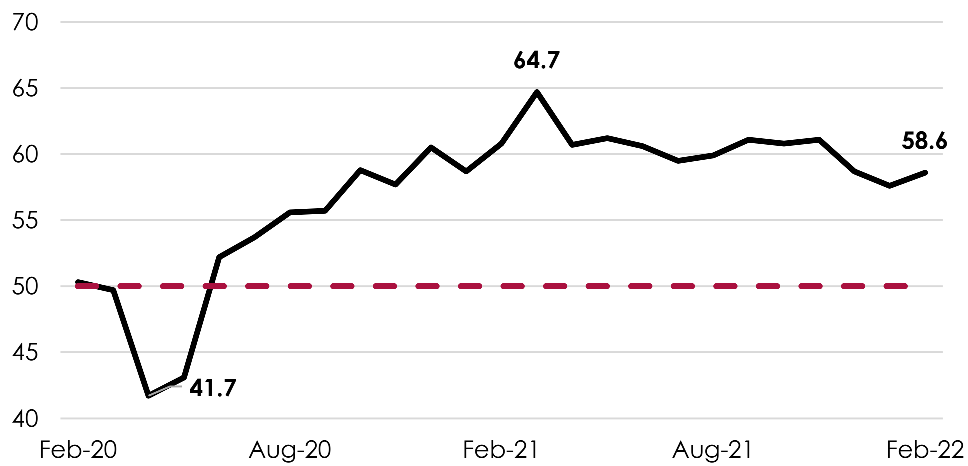
Index	Series Index February 2022	Series Index January 2022	Percentage Point Change	Direction	Rate of Change	Trend (Months)
PMI	58.6	57.6	1	Growing	Faster	21
New Orders	61.7	57.9	3.8	Growing	Faster	21
Production	58.5	57.8	0.7	Growing	Faster	21
Employment	52.9	54.5	-1.6	Growing	Slower	6
Supplier Deliveries	66.1	64.6	1.5	Slowing	Faster	72
Inventories	53.6	53.2	0.4	Growing	Faster	7
Customers' Inventories	31.8	33	-1.2	Too Low	Faster	65
Prices	75.6	76.1	-0.5	Increasing	Slower	21
Backlog of Orders	65	56.4	8.6	Growing	Faster	20
New Export Orders	57.1	53.7	3.4	Growing	Faster	20
Imports	55.4	55.1	0.3	Growing	Faster	4
	OVERALL ECONOMY			Growing	Faster	21
	Manufacturing Sector			Growing	Faster	21

U.S. ISM Manufacturing PMI, points



Sources: Bloomberg, U.S. ISM

- ✓ Based on a report from the U.S. Institute for Supply Management (ISM), manufacturing PMI recorded an increase of 1.0 point to 58.6 points in February 2022 compared to 57.6 points in previous month.
- ✓ This figure depicted expansion in the overall economy for 21 consecutive months since contraction in April and May 2020.
- ✓ However, supply-demand mismatch continues to persist in the U.S. manufacturing sector amid high Covid-19 confirmed cases, higher quits rate and early retirements.
- ✓ A moderate-to-strong growth is reported in February 2022 for all 6 biggest manufacturing industries.
- ✓ As impact of Omicron softened in February, it is anticipated that recovery in manufacturing sector will take place in March and April, backed by encouraging new orders and reducing backlogs.

MANUFACTURING SENTIMENTS – MISMATCH OF SUPPLY AND DEMAND CONTINUED TO IMPEDE OPERATIONS

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Business Sector	Responses from Survey
Computer & Electronic Products	Supply chain for electronic products remain disrupted.
Chemical Products	Strong sales growth as retail makes a comeback.
Transportation Equipment	Strong demand for transportation equipment continues albeit supply chain issues concerning transportation services.
Food, Beverage & Tobacco Products	Demand has exceeded traditional seasonality curves despite ongoing challenges which include procurement of ocean freight, operational planning and managing costs.
Machinery	Approximately 10% y-o-y revenue growth was registered. However, moderate growth in automotive sector was seen due to microchip shortages.
Fabricated Metal Products	Underpinned by the automotive and energy industries, demand for steel products grew to historic level.
Textile Mills	It is anticipated that 2022 will be a year with persistent demand, higher prices and supply chain issues will continue to prevail.
Electrical Equipment, Appliances & Components	Despite of consistent production due to availability of parts, backlog will increase as demand picks up.
Miscellaneous Manufacturing	Businesses are recovering amid challenges faced to meet the demand.
Plastics & Rubber Products	Business is resilient regardless having some issues relating to logistics and raw material shortages.

Source: U.S. ISM

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