BNM MAINTAINED OPR AT 1.75%

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ECONOMIC RESEARCH

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BNM DECIDED TO MAINTAIN THE OPR AT 1.75%

BANK NEGARA MALAYSIA
CENTRAL BANK OF MALAYSIA

The Monetary Policy Committee (MPC) members kept the Overnight Policy Rate (OPR) at 1.75% during its meeting on 2-3 March 2022.

Global

- ✓ Global economic activities continued to gain its momentum despite some moderation due to surge of Omicron cases.
- ✓ **Inflation** remains on an elevated level influenced by both demand and supply factors.
- ✓ Meanwhile, more countries will transition to **endemic management of Covid-19** that will support global growth in 2022.
- ✓ Heightening risks surrounding the **military conflict between Russia and Ukraine** that would cloud economic growth prospects while commodity and financial market have become more volatile.

Domestic

- ✓ Pent-up demand and stronger private consumption alongside the reopening of international borders are likely to support Malaysia's recovery.
- ✓ The negative impacts from the Omicron variant are deemed to be less severe than previous waves.
- ✓ Be that as it may, the risks to the growth outlook remain tilted to the downside in view of external and domestic factors, including a weaker-than-expected global growth, ongoing geopolitical conflicts, worsening supply chain disruptions and worries over Covid-19.
- ✓ **Headline inflation** is projected to remain moderate this year as the base effect from fuel inflation continues to dissipate while **core inflation** is expected to normalise to around its long-term average.
- ✓ Nevertheless, inflation outlook will depend on the global commodity price developments following prolonged supply-related disruptions.

✓ All in all, the MPC considers the current stance of monetary policy to be appropriate and accommodative.

Source: BNM

OPR VS. FEDERAL FUND RATE (FFR)

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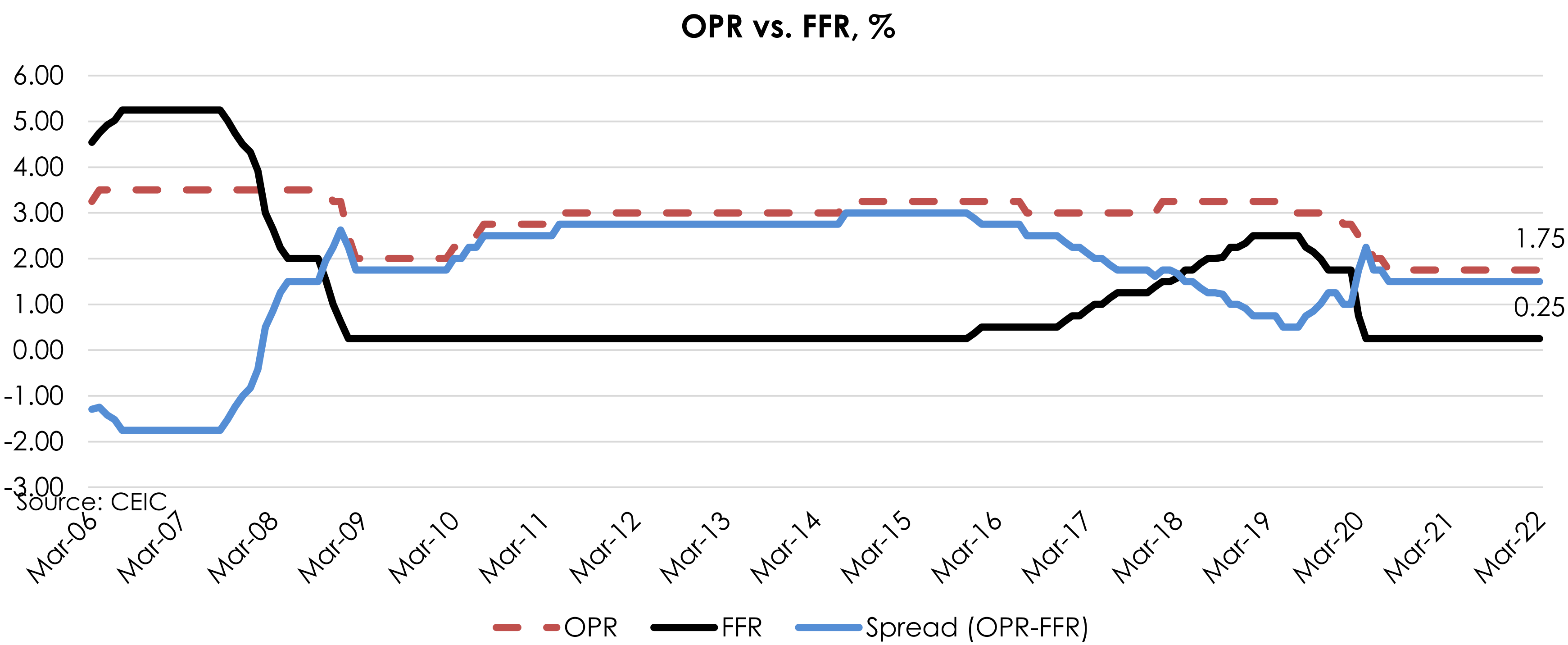


Source: CEIC

- ✓ At present, the spread between Malaysia's OPR and the U.S. Federal Fund Rate (FFR) stood at 150 basis points (bps) (1.75% minus 0.25%).
- ✓ Thus far, Jerome Powell, the Federal Reserve (Fed) Chairman confirmed on 2 March 2022 that the Fed is on track to raise the interest rate this month, pivoting to tackle the fastest inflation in 40 years as prices rose by 7.5% in 2021. Hence, such policy stance could increase the real interest rate differential over the U.S.
- ✓ As such, we anticipate the BNM would follow suit by increasing the OPR by 25 bps somewhere in 2H2022 in order to rebuild policy buffers and maintain ringgit stability.

CENTRAL BANK POLICY RATES

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	0.25
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	0.25	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	10.75
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

**** As at 3 March 2022***

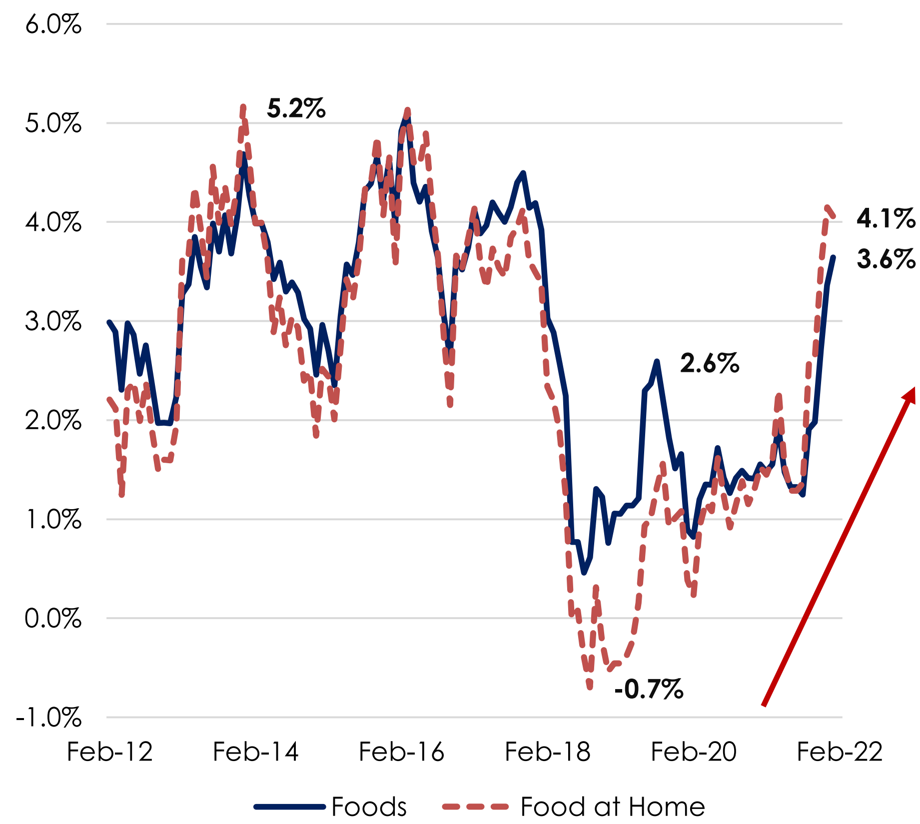
Source: Bloomberg

- ✓ Following the recent geopolitical issues, the Central Bank of Russia has decided to increase its interest rates twice in the month of February with the latest at 20.0% from 9.5% during its meeting on Monday. The emergency move was due to the sanctions put by the West following its invasion of Ukraine to offset the increased risk of Ruble depreciation and inflation.
- ✓ In view of this, it has put greater pressure for other central banks to follow suit in order to curb the inflationary pressure due to soaring in price of oil and commodities which was already felt prior to Ukraine war.
- ✓ Recently, 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.
- ✓ Meanwhile, the Reserve Bank of Australia (RBA) left its cash rate unchanged at 0.10% for the fifteenth month straight on 1 March. While nodding on the economic impact of Russia's invasion of Ukraine, the board will watch carefully the effect of inflation movement later on. For now, they will be patient on the rate hike until the actual inflation is sustained within the 2.0% to 3.0% target range.

OUR VIEW – HIGHER INFLATION RATE MOVING FORWARD

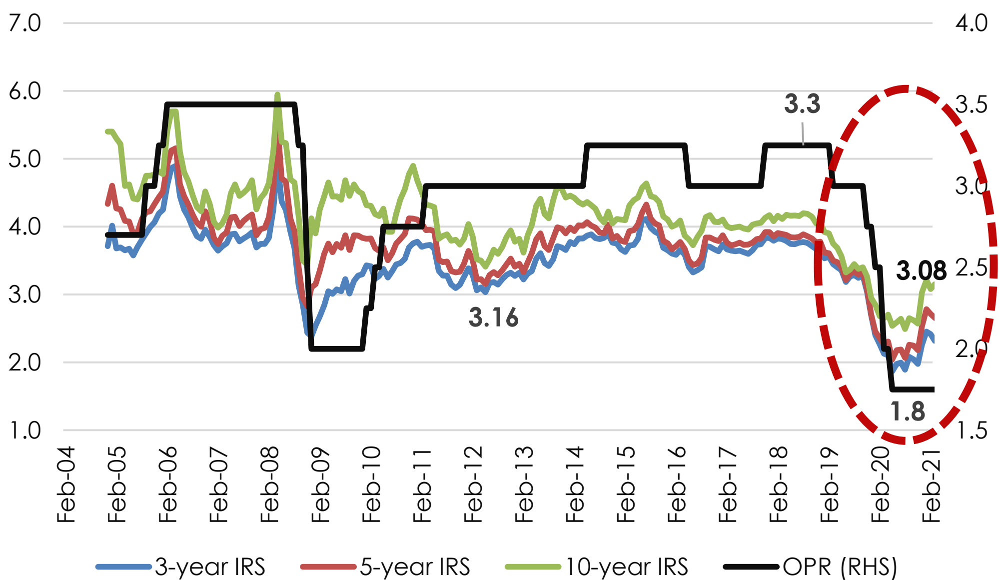
- ✓ Malaysia's inflation rate increased moderately by 2.3% y-o-y in January from a 3.2% growth in the preceding month as base effects from fuel inflation dissipates.
- ✓ Be that as it may, food prices remained high as it rose by 3.6% in January 2022 (December 2021: 3.4%) as compared to a 1.6% increase in the same corresponding period last year, suggesting higher cost of living necessities and lower purchasing power of consumers.
- ✓ Apart from that, the rise of electricity rates for commercial and industrial users alongside with an anticipation of gradual increase in minimum wages could create second round effect on costs of goods, which we believe would exert price pressure for Consumer Price Index (CPI).
- ✓ Moreover, we foresee further upside inflationary risks from geopolitical tension between Russia and Ukraine, which has pushed commodities prices higher, intensifying the inflation scenario.

Foods vs. Food at Home, y-o-y%



Source: CEIC

OPR vs. Interest Rate Swap (IRS), %



Source: Bloomberg

✓ **Interest rate swaps (IRS) is pointing up, signaling an OPR hike –** The IRS suggests that derivative market is pricing in rate hike this year, probably due to a tight global monetary policy and higher inflation risks amid continued supply chain disruptions and recent geopolitical tensions. Be that as it may, BNM would remain mindful in their assessment to avoid a premature withdrawal of policy support that could affect Malaysian economic recovery moving forward given heightened uncertainties in the global market.

✓ **We are maintaining our call that the OPR would be raised by 25 bps in the 2H2022 –** Based on the latest monetary policy statement, the BNM remains cautious on the trajectory of Malaysian economy due to external and domestic factors. These include a slowing global economic activities, continuing geopolitical conflicts, worsening supply chain disruptions, as well as developments surrounding Covid-19. However, the reopening of international borders this month is expected to provide further support to economic recovery. Meanwhile, catalysts for higher inflation would be from commodity price developments due to the risks from protracted supply-related disruptions. **As such, 25 bps hike in OPR would likely be imminent in the 2H2022.**

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APPENDIX - MONETARY POLICY STATEMENT

- ✓ At its meeting today, the Monetary Policy Committee (MPC) of Bank Negara Malaysia decided to maintain the Overnight Policy Rate (OPR) at 1.75 percent.
- ✓ The global economy continues to recover. Despite the recent moderation in economic activity due to the Omicron-driven COVID-19 resurgences, the overall recovery trajectory remains on track. Inflation in many economies remain elevated, due to both demand and supply factors. Going forward, more countries will transition to endemic management of COVID-19, hence supporting global growth prospects. The unfolding developments surrounding the military conflict in Ukraine, however, have emerged as a key risk to global growth and trade prospects, commodity prices and financial market conditions. The global growth outlook will also continue to be affected by developments surrounding COVID-19, risks of prolonged global supply disruptions, and heightened financial market volatility amid adjustments in monetary policy in major economies.
- ✓ Despite the challenging environment, the Malaysian economy expanded by 3.1% in 2021. Looking ahead, the growth recovery will strengthen in 2022, driven by the expansion in global demand and higher private sector expenditure, amid improvements in the labour market and continued targeted policy support. The expected reopening of international borders would also provide further support to economic recovery. The economic impact from the recent increase in COVID-19 cases due to the Omicron variant is expected to be considerably less severe than previous waves in the absence of stringent restrictions. Risks to the growth outlook remain tilted to the downside due to external and domestic factors. These include a weaker-than-expected global growth, ongoing geopolitical conflicts, worsening supply chain disruptions, and developments surrounding COVID-19.
- ✓ Headline inflation in 2022 is projected to remain moderate as the base effect from fuel inflation continues to dissipate. Underlying inflation, as measured by core inflation, is expected to normalise to around its long-term average as economic activity continues to pick up amid the environment of high input costs. Nevertheless, core inflation is expected to be modest, with the upside risk partly contained by the continued slack in the economy and labour market. The inflation outlook continues to be subject to global commodity price developments amid risks from prolonged supply-related disruptions.
- ✓ The MPC considers the current stance of monetary policy to be appropriate and accommodative. Fiscal and financial measures will continue to provide support to economic activity. Amid the prevailing uncertainties, the stance of monetary policy will continue to be determined by new data and their implications on the overall outlook for domestic inflation and growth.