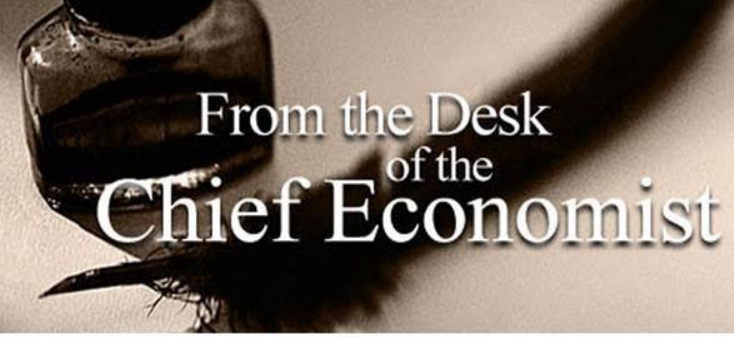

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OPR - MOVING AWAY FROM A CRISIS MODE

6 JULY 2022

ECONOMIC RESEARCH

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OVERNIGHT POLICY RATE (OPR) WAS RAISED BY ANOTHER 25 BPS

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BANK NEGARA MALAYSIA
CENTRAL BANK OF MALAYSIA

- ✓ The Bank Negara Malaysia (BNM) has decided to increase the OPR by 25 basis points (bps) to 2.25% during Monetary Policy Committee (MPC) meeting on 5-6 July.
- ✓ The new ceiling and floor rates were higher to 2.50% and 2.75% respectively.

Global

- ✓ According to the Monetary Policy Statement (MPS), the global economic activities continued to gain its momentum with the labour market condition has improved further.
- ✓ However, detrimental impacts from rising inflationary pressures, prolonged Russia-Ukraine conflicts, as well as China's Zero Covid Policy have posed risks to the global economic outlook.
- ✓ Central banks across the world are also expected to tighten monetary policy settings, some at a faster pace to ward off inflation.
- ✓ Following this, the global growth is likely to expand at moderate pace in view of rising in cost pressure, supply chain issues and volatility in financial market.

Malaysia

- ✓ On the domestic front, Malaysian economy continued to strengthen as reflected by stronger exports and retail spending.
- ✓ Nevertheless, external headwinds will weigh on economic activities moving forward while the domestic demand will remain as a pillar of growth.
- ✓ Meanwhile, the **headline inflation is projected to stay within BNM's forecast at 2.2%-3.2% this year with core inflation to average between 2.0% and 3.0%** amid pent-up demand and higher cost environment.
- ✓ Apart from that, **the BNM explicitly indicated that possible removal of monetary accommodation will be implemented is a measured and gradual manner**.

RISING GLOBAL INTEREST RATE

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Policy rates	Jul-21	Aug-21	Sep-21	Oct-21	Nov-21	Dec-21	Jan-22	Feb-22	Mar-22	Apr-22	May-22	Jun-22	Jul-22*
Advanced countries													
US (Fed Fund Rate)	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.50	0.50	1.00	1.75	1.75
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	0.25	0.25	0.50	0.75	0.75	1.00	1.25	1.25
Canada (ON Lending Rate)	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.50	1.00	1.00	1.50	1.50
Latin America													
Mexico (ON Rate)	4.25	4.50	4.75	4.75	5.00	5.50	5.50	6.00	6.50	6.50	7.00	7.75	7.75
Brazil (Selic Rate)	4.25	5.25	6.25	7.75	7.75	9.25	9.25	10.75	11.75	11.75	12.75	13.25	13.25
Argentina (LELIQ 7D Notes Rate)	38.00	38.00	38.00	38.00	38.00	38.00	40.00	42.50	44.50	47.00	49.00	52.00	52.00
Eastern Europe													
Russia (Key Rate)	6.50	6.50	6.75	7.50	7.50	8.50	8.50	9.50	20.00	14.00	11.00	9.50	9.50
Ukraine (Discount Rate)	8.00	8.00	8.50	8.50	8.50	9.00	10.00	10.00	10.00	10.00	10.00	25.00	25.00
Turkey (1W Repo Rate)	19.00	19.00	18.00	16.00	15.00	14.00	14.00	14.00	14.00	14.00	14.00	14.00	14.00
Asia													
China (1Y Loan Prime Rate)	3.85	3.85	3.85	3.85	3.85	3.80	3.70	3.70	3.70	3.70	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	4.40	4.90	4.90
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	0.75	0.75	0.75	1.00	1.00	1.25	1.25	1.25	1.50	1.75	1.75	1.75
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	2.25	2.50	2.50
Australia (Cash Rate)	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.35	0.85	1.35
New Zealand (Cash Rate)	0.25	0.25	0.25	0.50	0.75	0.75	0.75	1.00	1.00	1.50	2.00	2.00	2.00
Malaysia (OPR)	1.75	1.75	1.75	1.75	1.75	1.75	1.75	1.75	1.75	1.75	2.00	2.00	2.25

Source: Bloomberg
***As at 6 July 2022**

Interest Rate Hike

Interest Rate Cut

Recently, the Reserve Bank of Australia (RBA) raised the cash rate by 50 bps to 1.35% on 5 July 2022. This is a level not seen since May 2019, aiming to contain surging inflation (1Q2022: 5.1% vs. 4Q2021: 3.5%).

MALAYSIA'S ECONOMIC DATA CONTINUES TO SHOW A POSITIVE GROWTH DESPITE INFLATIONARY ENVIRONMENT

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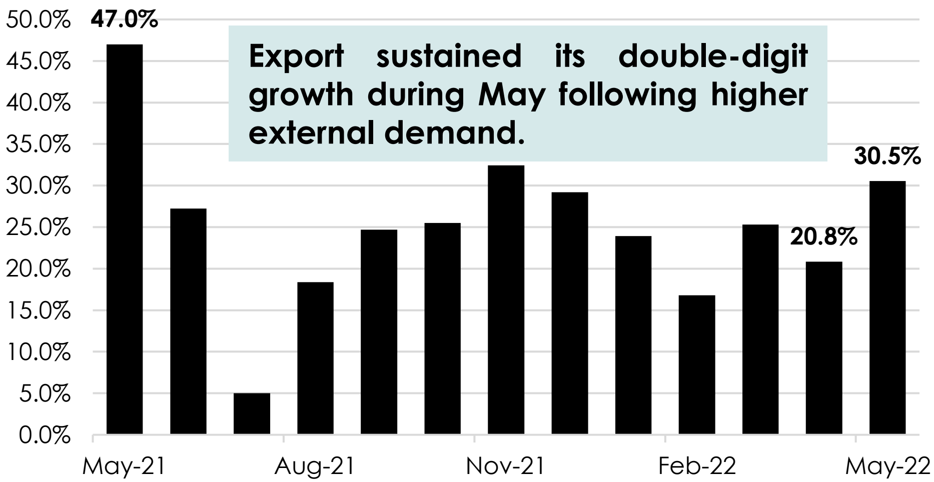
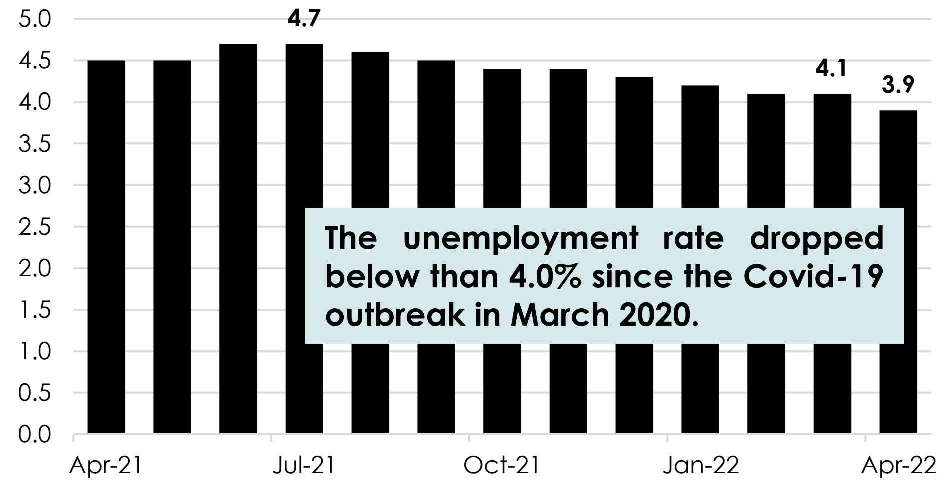
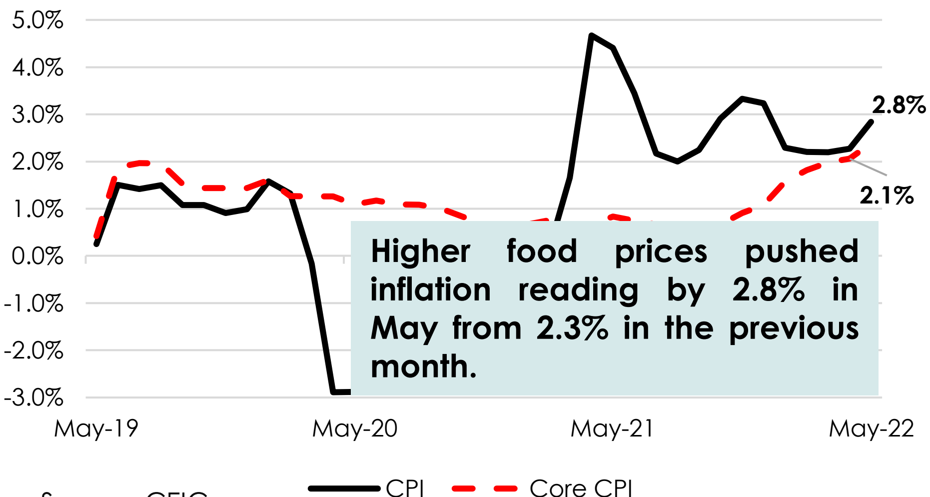
Exports, y-o-y%



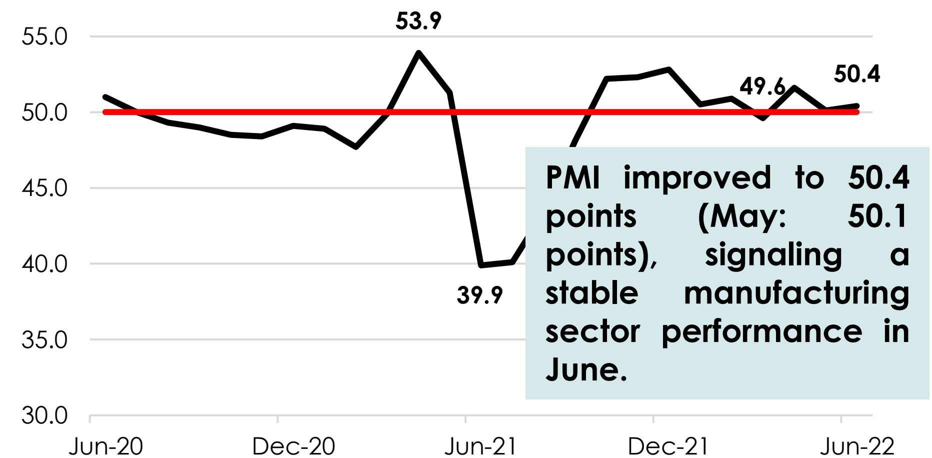
Unemployment Rate, y-o-y%



CPI, y-o-y%



Manufacturing Purchasing Manager's Index (PMI), points



Source: CEIC

IT SEEMS THAT THE BOND MARKET HAS PRICED IN FOR THE OPR TO RISE FURTHER IN 2H2022

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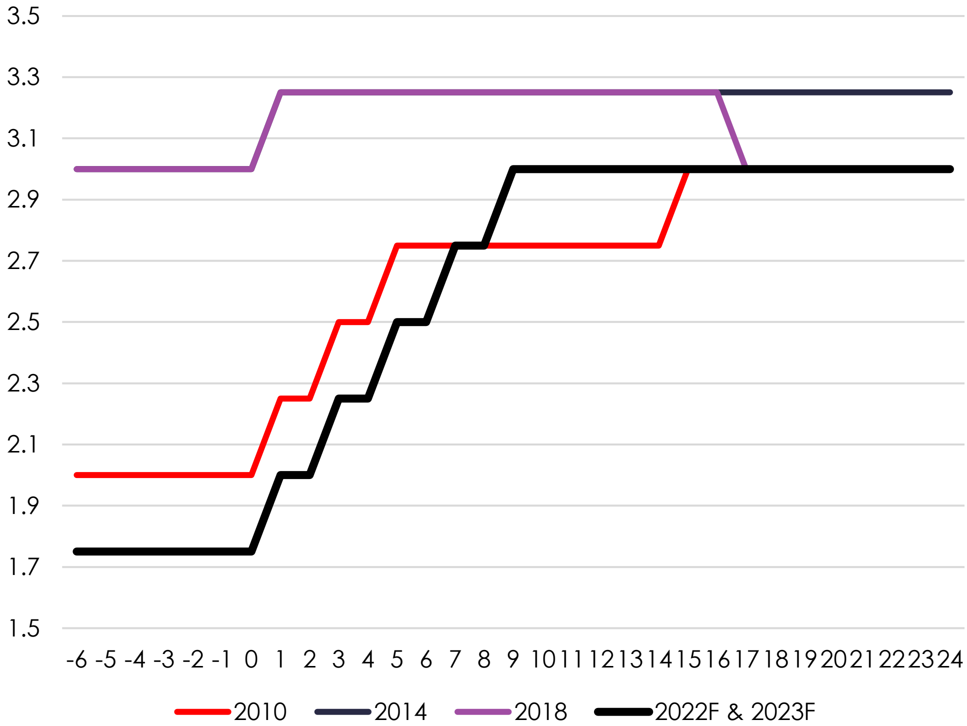
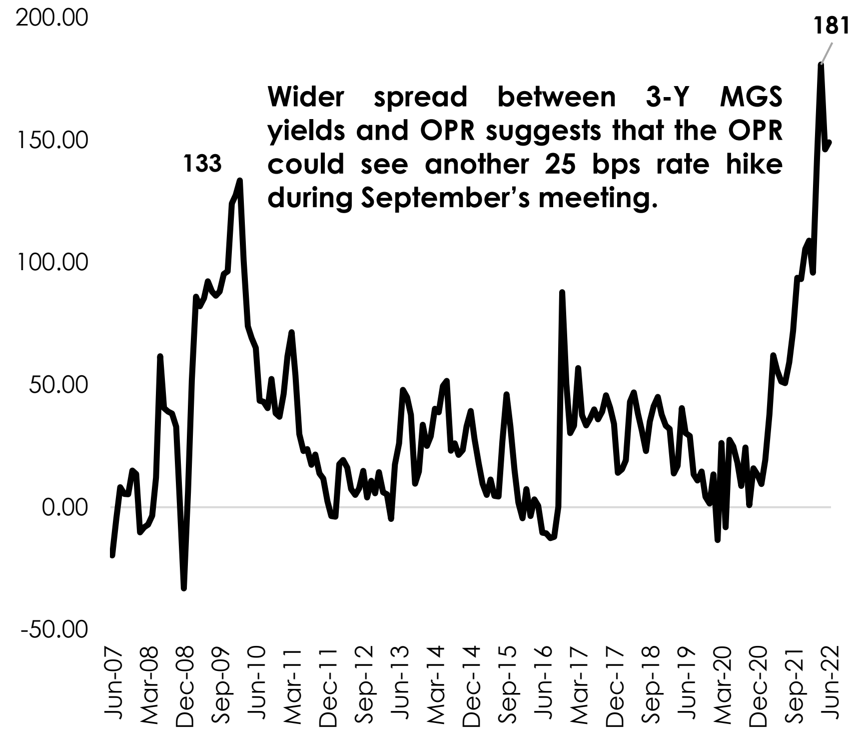
OPR during post economic shocks tightening in the past



Spread (3-Y MGS yields minus OPR), bps



Source: CEIC

- ✓ Series of external headwinds coupled with aggressive rate hike in the U.S. have sparked worries for recession risk.
- ✓ Following this, **we anticipate the MGS yields to be slightly bullish during 2H2022 with the 3-Y MGS, 5-Y MGS and 10-Y MGS yields to settle at 3.89%, 4.30% and 4.57% by end of 2022** amid risk-off mode among market participants.

STRONGER U.S. DOLLAR (USD) PUT THE RINGGIT TO BE LINGERING AROUND RM4.40 LEVEL

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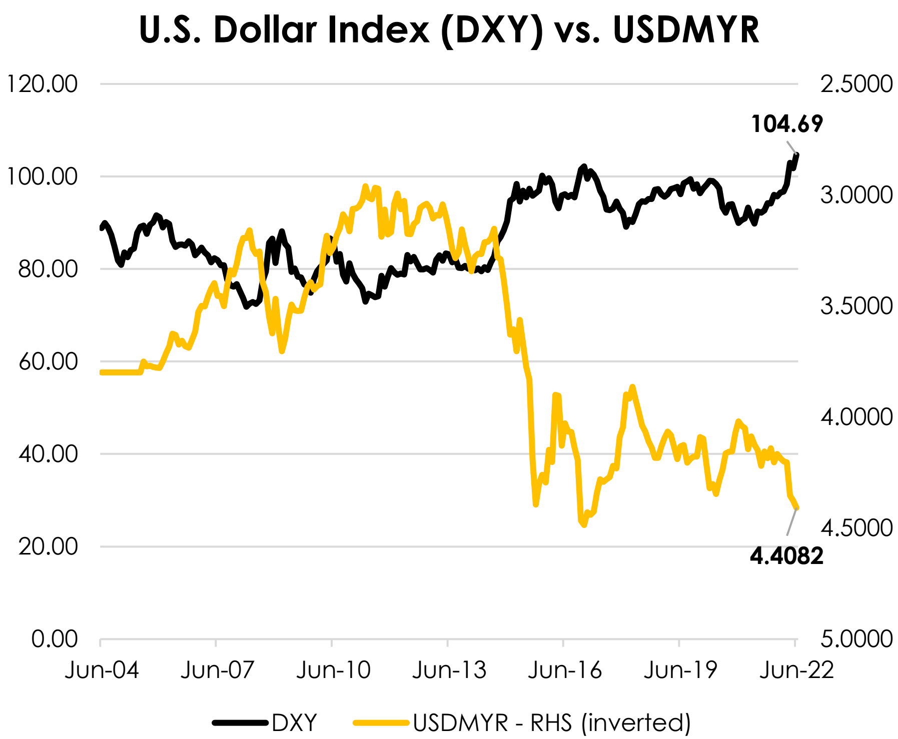

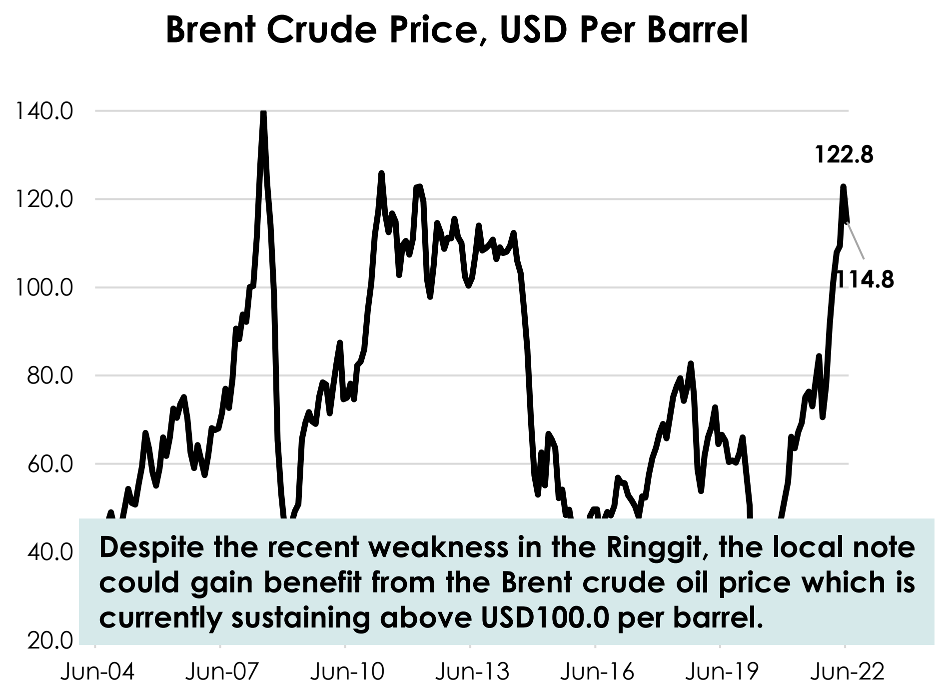

Sources: Bloomberg, CEIC

- ✓ The sky-high inflation in the U.S. has prompted aggressive rate hikes by the Fed, causing the recession fear to dominate. As a result, the USD continues to strengthen following its appeal as safe-haven currency, reaching to its highest level at 106.53 on 5 July due to risk-off sentiment surrounding the market.
- ✓ As the demand for the greenback is rising, this has affected emerging currencies such as the Ringgit to close lower at RM4.4193 on the same date from RM4.4132 on 4 July.
- ✓ While we foresee that the country's domestic outlook could support the value of Ringgit, **we revised down our USDMYR to RM4.28 in 2022** (previous estimation: RM4.15) in view of hawkish stance by the Fed at the moment.

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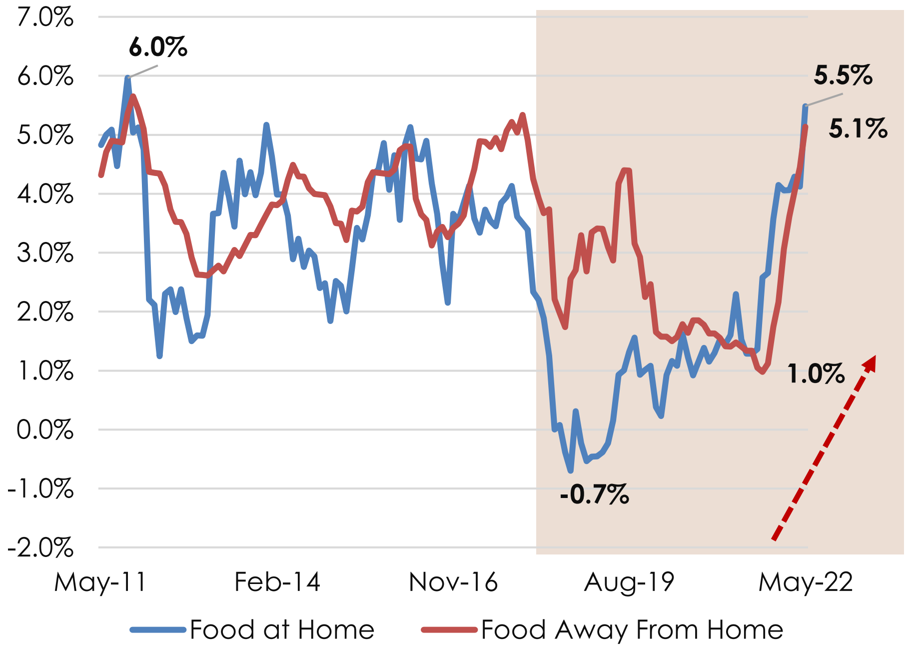
- ✓ **Food inflation persists -** Inflation rate in Malaysia seems manageable (May: 2.8% y-o-y vs. April: 2.3%) since it is still within the central bank's target range of 2.2% to 3.2% in 2022. This is mainly attributable to the government subsidies which serve as one of the main contributors to tamper the inflationary pressures in Malaysia. Nonetheless, food prices remained high as it rose by 5.3% in May (April: 4.2%). This was the largest increase recorded since 2011, suggesting higher cost of living necessities. As the government shifts from a blanket subsidy system to a more targeted subsidy, further upside inflationary risks are anticipated.

Costs of Foods, y-o-y%



Source: CEIC

- ✓ **BNM is no longer in crisis mode –** Post MPC meeting with the private sector economists showed that the BNM is committed to move away from a crisis mode whereby the OPR was significantly lowered from 3.00% at the end of 2019 to 1.75% in July 2020. This is a clear indication that the OPR would be normalized further in the next two meetings in September and November this year and during the 1H2023. **All in all, we are projecting the OPR to reach 2.75% at the end of 2022 and between 3.00% and 3.25% in 2023.**

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APPENDIX - MONETARY POLICY STATEMENT

- ✓ At its meeting today, the Monetary Policy Committee (MPC) of Bank Negara Malaysia decided to increase the Overnight Policy Rate (OPR) by 25 basis points to 2.25 percent. The ceiling and floor rates of the corridor of the OPR are correspondingly increased to 2.50 percent and 2.00 percent, respectively.
- ✓ The reopening of the global economy and the improvement in labour market conditions continue to support the recovery of economic activity. However, these have been partly offset by the impact from rising cost pressures, the military conflict in Ukraine and strict containment measures in China. Inflationary pressures have continued to increase mainly due to elevated commodity prices and strong demand conditions, despite some easing in global supply chain conditions. Consequently, central banks are expected to continue adjusting their monetary policy settings, some at a faster pace, to reduce inflationary pressures. Going forward, the pace of global growth is expected to moderate, and will continue to be affected by the elevated cost pressures, conflict in Ukraine, global supply chain conditions, and financial market volatility.
- ✓ For the Malaysian economy, economic activity continued to strengthen in recent months. Exports and retail spending indicators affirm the positive growth momentum, supported by the transition to endemicity. In the labour market, the unemployment rate declined further, with higher labour participation and improving income prospects. Looking ahead, while external demand is expected to moderate, weighed by headwinds to global growth, economic growth will be supported by firm domestic demand. Additionally, the reopening of international borders since 1 April 2022 would facilitate the recovery in tourism-related sectors. Investment activity and prospects continue to be supported by the realisation of multi-year projects. However, downside risks to growth continue to stem from a weaker-than-expected global growth, further escalation of geopolitical conflicts, and worsening supply chain disruptions.
- ✓ Year-to-date, headline inflation has averaged 2.4%. While it is projected to remain within the 2.2% - 3.2% forecast range for the year, headline inflation may be higher in some months due mainly to the base effect from electricity prices. Underlying inflation, as measured by core inflation, is expected to average between 2.0% - 3.0% in 2022 as demand continues to improve amid the high-cost environment. Nevertheless, the extent of upward pressures on inflation will remain partly contained by existing price controls, fuel subsidies and the continued spare capacity in the economy. The inflation outlook continues to be subject to global commodity price developments, arising mainly from the ongoing military conflict in Ukraine and prolonged supply-related disruptions, as well as domestic policy measures.
- ✓ Amid the positive growth prospects for the Malaysian economy, the MPC decided to further adjust the degree of monetary accommodation. This is consistent with the MPC's view that the unprecedented conditions that necessitated a historically low OPR have continued to recede. At the current OPR level, the stance of monetary policy remains accommodative and supportive of economic growth. The MPC will continue to assess evolving conditions and their implications on the overall outlook to domestic inflation and growth. Any adjustments to the monetary policy settings going forward would be done in a measured and gradual manner, ensuring that monetary policy remains accommodative to support a sustainable economic growth in an environment of price stability.