



From the Desk  
of the  
**Chief Economist**

**BANK ISLAM**

# **OPR HOLDS STEADY AT 1.75%**

**9 SEPTEMBER 2021**

## **ECONOMIC RESEARCH**

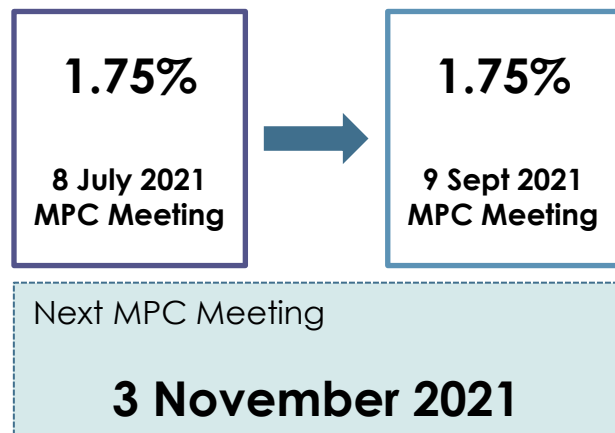
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Bank Negara Malaysia (BNM) has decided to maintain the Overnight Policy Rate (OPR) at 1.75% during the Monetary Policy Committee (MPC) meeting on 9 September 2021 (Consensus: 1.75%, Bank Islam: 1.75%).

## Global

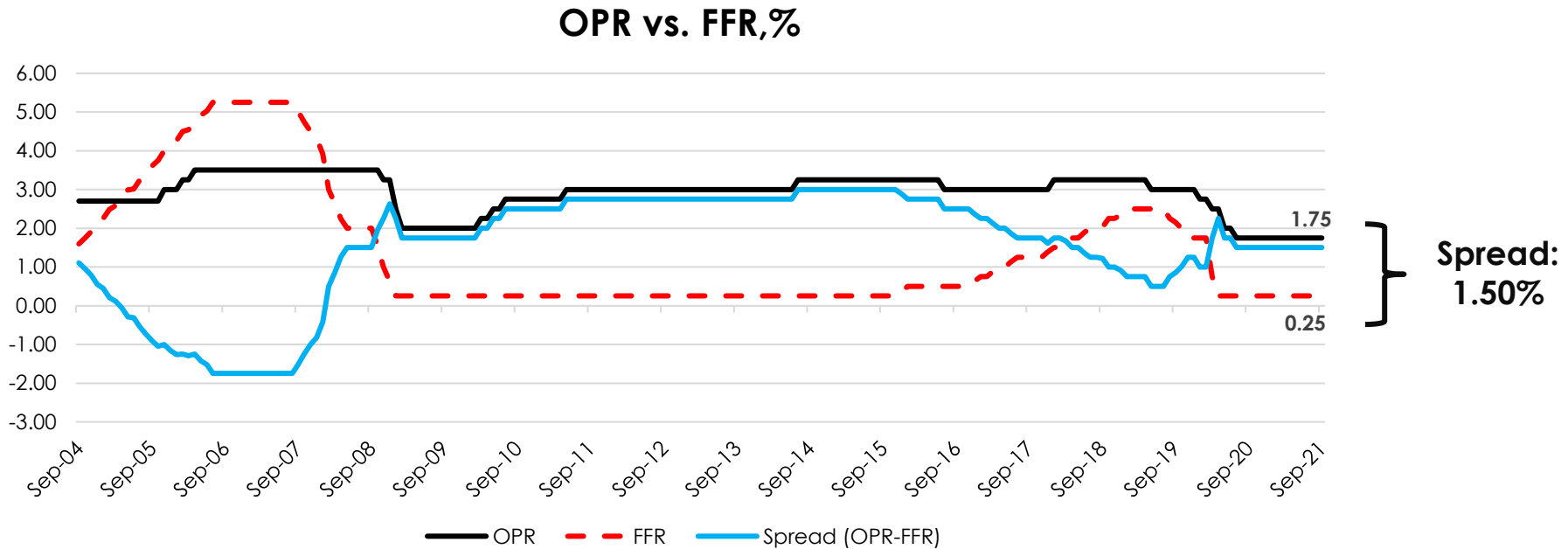
- ✓ According to the accompanying statement, global economic activities have improved further as manufacturing and services sector continued to gained its momentum.
- ✓ The recovery remains uneven in many countries depending on their vaccination coverage, as well as relaxation of restriction measures.
- ✓ Be that as it may, the emergence of new Covid-19 variants has clouded global economic outlook while any shifts in major economies' monetary policy would pose a risk to the financial market.

## Domestic

- ✓ On the local front, recent gradual relaxations for more economic sectors, as well as higher adaptability of firms to the new operating environment would cushion the negative impacts and allow the economy to resume its recovery path.
- ✓ Therefore, further easing of Covid-19 related measures alongside rapid vaccination progress would strengthen the domestic demand and push up economic growth going into 2022.
- ✓ Meanwhile, the headline inflation is projected to average between 2.0% and 3.0% for 2021 while the core inflation is expected to remain subdued, ranging between 0.5% and 1.5% in view of spare capacity in the economy.
- ✓ However, volatility in global commodity price would weigh on the outlook while policy measures are still required to ease the cost burden of the public.

All in all, the MPC considers the stance of monetary policy to be appropriate and accommodative. BNM remains committed to utilise its policy levers whenever deemed fit to nurture conducive conditions for a sustainable economic recovery.

# OVERNIGHT POLICY RATE (OPR) VS. FEDERAL FUND RATE (FFR)



Sources: CEIC, Bank Islam

- ✓ As of today, Malaysia's OPR spread against the U.S. Federal Fund Rate (FFR) stood at 150 basis points (bps) (1.75% minus 0.25%).
- ✓ This implies that BNM still has room for a possible OPR reduction if such decision is solely based on the interest rate differentials with the FFR.
- ✓ Assuming that the U.S. Federal Reserve (Fed) is likely to normalize its benchmark rate of 2.50% (long run FFR) at some point in the future as the majority of policy makers believe that the appropriate target level for the FFR in the longer run is in that region (based on dot plots in previous meetings), the OPR could reach as high as 4.00%.
- ✓ However, the OPR may not reach 4.00% (150 bps higher than the long run FFR of 2.50%) because the highest OPR ever recorded was at 3.50% from April 2006 to October 2008 when the annual GDP growth hit 5.6%, 6.3% and 4.8% in 2006, 2007 and 2008 respectively.

# CENTRAL BANK POLICY RATES

Policy rates	Sep-20	Oct-20	Nov-20	Dec-20	Jan-21	Feb-21	Mar-21	Apr-21	May-21	Jun-21	Jul-21	Aug-21	Sep-21*
<b>Advanced countries</b>													
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	0.10	0.10	0.10	0.10
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	0.25
<b>Latin America</b>													
Mexico (ON Rate)	4.25	4.25	4.25	4.25	4.25	4.00	4.00	4.00	4.00	4.25	4.25	4.50	4.50
Brazil (Selic Rate)	2.00	2.00	2.00	2.00	2.00	2.00	2.75	2.75	3.50	4.25	4.25	5.25	5.25
Argentina (LELIQ 7D Notes Rate)	38.00	36.00	38.00	38.00	38.00	38.00	38.00	38.00	38.00	38.00	38.00	38.00	38.00
<b>Eastern Europe</b>													
Russia (Key Rate)	4.25	4.25	4.25	4.25	4.25	4.25	4.50	5.00	5.00	5.50	6.50	6.50	6.50
Ukraine (Discount Rate)	6.00	6.00	6.00	6.00	6.00	6.00	6.50	7.50	7.50	7.50	8.00	8.00	8.00
Turkey (1W Repo Rate)	10.25	10.25	15.00	17.00	17.00	17.00	19.00	19.00	19.00	19.00	19.00	19.00	19.00
<b>Asia</b>													
China (1Y Loan Prime Rate)	3.85	3.85	3.85	3.85	3.85	3.85	3.85	3.85	3.85	3.85	3.85	3.85	3.85
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)	4.00	4.00	3.75	3.75	3.75	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	0.50	0.50	0.50	0.50	0.50	0.50	0.75	0.75
Philippines (O/N Lending Rate)	2.25	2.25	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)	0.25	0.25	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	0.25	0.25	0.25	0.25	0.25	0.25
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 9 September 2021

Source: Bloomberg

- ✓ Thus far, few central banks have started to increase their benchmark interest rate to contain the inflationary pressure such as Brazil's central bank which had raised its interest rate three times this year. Meanwhile, for most emerging market central banks, they are holding their key rate steady and just keeping the rate low amid ongoing uncertainties on economic prospects.
- ✓ Recently, the Reserve Bank of Australia (RBA) left its cash rate at a record low of 0.10% on 7 September and confirmed plans to taper the purchase of government bonds to AUD4.0 billion a week until at least mid February next year. The policymakers also remained committed to maintain supportive monetary conditions and will not increase the cash rate until the actual inflation can be sustained within the 2.0% to 3.0% target range.

# OUR VIEW – OPR TO REMAIN UNCHANGED IN THE NEXT MPC MEETING.....

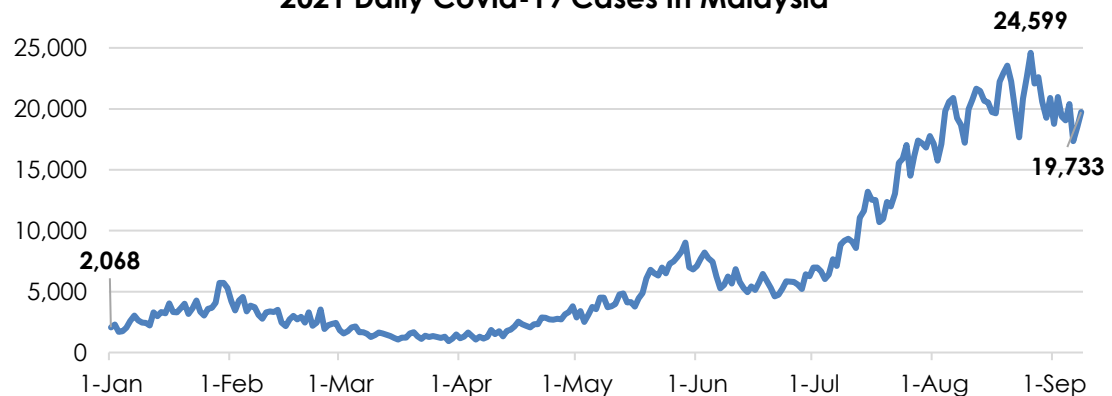
- ✓ For the next MPC meeting scheduled on 3 November, which will also be the last meeting for 2021, we opine that the OPR will be kept at 1.75%.
- ✓ We are cognizant of the government's move to relax movement restrictions mainly for vaccinated individuals and workers combined with the transition of certain states into the remaining phases of the National Recovery Plan (NRP) which may boost the nation's economic growth in 4Q2021.
- ✓ With that in mind, businesses are expected to gradually rehire workers but the pace of rehiring is something that is hard to ascertain at the moment because other factors have to be taken into account such as the ability to reach the break-even point.
- ✓ On further scrutiny, Malaysia's unemployment rate remained unchanged at 4.8% in July (June: 4.8%).
- ✓ In other words, the trickle down effect from the loosening of movement restrictions towards the expansion of business activities may somewhat take time as the overall sentiment appears cautious with regard to the pandemic.
- ✓ The daily tally of new Covid-19 cases in the country continues to remain high above 15,000 cases per day since late July this year partly due to the highly transmissible Delta variant. Aside from that, the Mu variant has recently been added to the World Health Organization's (WHO) watchlist, suggesting that the threat of other variants of the pandemic continue to linger.
- ✓ Henceforth, the current OPR level should strike a delicate balance between expected economic growth fuelled by increased human mobility and the downside risks posed by the pandemic.

## Progress of the National Recovery Plan as at 8 September 2021

States			
Phase 1	Phase 2	Phase 3	Phase 4
Kedah	Pulau Pinang	Perlis	Labuan
	Perak		
	Kelantan		
	Terengganu		
	Pahang		
Johor	Sabah	Sarawak	
	Federal Territory Of Kuala Lumpur		
	Federal Territory Of Putrajaya	Negeri Sembilan	
	Selangor		
	Melaka		

Source: Prime Minister's Office

## 2021 Daily Covid-19 Cases In Malaysia



Source: CEIC

# OUR VIEW – .....BUT THE CASE FOR AN OPR HIKE IS COMPELLING FOR 2022

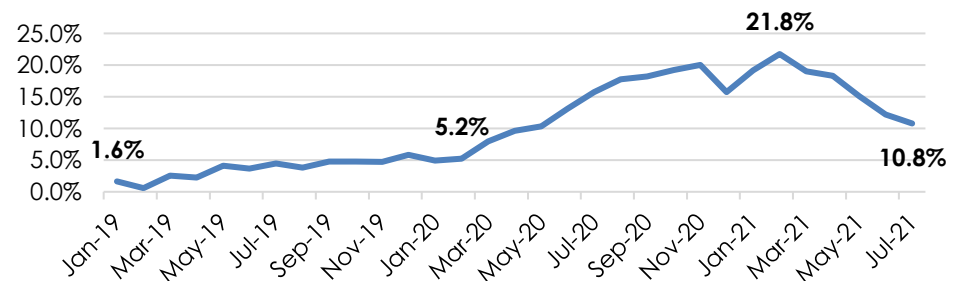
- ✓ Looking ahead in 2022, we believe that the case for an OPR hike by BNM seems to be compelling due to a confluence of factors.
- ✓ BNM would also want to weigh the cost and benefit of having lower OPR for a protracted period. This is especially true when the excessive risks taking could undermine the financial stability when the OPR is kept too low for too long. We have seen the share of fixed deposits continues to decline to 45.1% as of July from 50.5% in January last year. This suggests that Malaysians are looking elsewhere to look for better investment returns.
- ✓ In relation to the nation's vaccination progress, the majority of adults will likely be fully vaccinated by early next year. So far, 70.5% of Malaysia's adult population has already been fully vaccinated as at 8 September. Meanwhile, the nation will embark on a mass Covid-19 vaccination drive targeting teenagers below 18 years old, kicking off in the state of Sarawak starting from 9 September with Klang Valley and Labuan expected to follow suit later.
- ✓ With 28.3% or 9.2 million of Malaysia's population consisting of children and teenagers below 18 years of age, the start of vaccination programs for teenagers will gradually increase the nation's overall vaccination rate and likely curb the spread of infections. Furthermore, economic sectors such as education involving schools and learnings institutions can later operate at a larger scale especially at the start of school term next year.
- ✓ Aside from that, Malaysia's M1 money supply growth has been increasing by a double-digit growth since May last year (July 2021: 10.8% y-o-y vs. June 2021: 12.2%), suggesting that a strong propensity to consume will accompany the wider reopening of the economy next year.
- ✓ Considering that the economy needs some time to be on a stronger footing as the economy reopens further next year, a conservative assumption on when BNM will increase the OPR will be in 3Q2021.
- ✓ While this may differ from expectation of the Fed funds market showing a roughly 90% chance of a rate hike by December 2022, fully pricing in that scenario by January 2023, BNM'S policy decision will be ultimately based on prevailing data and overall economic situation.

## Malaysia's Vaccination Progress as at 8 September 2021

<b>% of Malaysia's Total Population That Has Been Fully Vaccinated</b>	<b>50.5%</b>
<b>% of Malaysia's Adult Population That Has Been Fully Vaccinated</b>	<b>70.5%</b>

Source: Covid-19 Immunisation Task Force

## Malaysia's Money Supply M1 Growth, y-o-y%



Source: CEIC

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**Thank You**



- ✓ 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, supported by improvements in manufacturing and services activity. The strength of the recovery remains varied across countries mainly corresponding to their vaccination coverage, relaxation of containment measures and degree of policy support. Economies with better progress in their vaccination programmes have eased containment measures, enabling a continued recovery in domestic activity. Sizeable fiscal and monetary stimulus in several major economies continue to support the recovery momentum. Financial conditions also remain supportive of growth. Overall, the balance of risks to the global growth outlook is tilted to the downside. This is attributed mainly to uncertainty over the path of the pandemic amid the emergence of variants of concern, and potential risk of heightened financial market volatility amid adjustments in monetary policy in major economies.
- ✓ For the Malaysian economy, the re-imposition of nation-wide containment measures to curb the resurgence in COVID-19 cases had dampened the growth momentum. However, the recent gradual relaxations for more economic sectors to operate, along with higher adaptability of firms to the new operating environment and continued policy support, would partly mitigate the impact and allow the economy to resume its recovery path. Moving forward, the further easing of containment measures, rapid progress of the domestic vaccination programme and continued expansion in global demand will support the growth momentum going into 2022. Risks to the growth outlook, however, remain tilted to the downside due to external and domestic factors. These include delays in the easing or re-imposition of broad-based containment measures due to the impact of new COVID-19 variants of concern and a weaker-than-expected global growth recovery.
- ✓ Year-to-date, headline inflation has averaged 2.3%, and is projected to average between 2.0% and 3.0% for 2021. Underlying inflation, as measured by core inflation, is expected to remain subdued, averaging between 0.5% and 1.5% for the year, amid continued spare capacity in the economy. The outlook, however, continues to be subject to global commodity price developments and policy measures to alleviate the cost burden of the public. Underlying inflation, however, is expected to remain relatively subdued in 2022.
- ✓ The MPC considers the stance of monetary policy to be appropriate and accommodative. In addition, fiscal and financial measures will continue to cushion the economic impact on businesses and households and provide support to economic activity. Given the uncertainties surrounding the pandemic, the stance of monetary policy will continue to be determined by new data and information and their implications on the overall outlook for inflation and domestic growth. The Bank remains committed to utilise its policy levers as appropriate to foster enabling conditions for a sustainable economic recovery.