

BNM most likely to hold rates

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Highlights

- **2Q 2018 growth came out slower at 4.5% yoy (1Q 2018: 5.4% yoy) but this isn't just yet an immediate cause for concern.** The slowdown was a result of “commodity specific shocks” to the supply side, particularly due to supply disruptions to the Bintulu LNG plant and lower production in the palm oil sector. However, investment growth strengthened to 6.1% yoy (1Q 2018: 0.5% yoy) and this reflected possibly some element of optimism even amid the policy uncertainty. Consumption also came out strong at 8.0% yoy due to the tax holiday and government handouts. Going forward, there may be a slight growth pickup in 3Q 2018 as consumption growth may further strengthened as consumers frontload expenditure for the remaining period of the tax holiday. If supply issues to the LNG sector are resolved, this will also help further boost growth. However, growth will probably see some slowdown in 4Q 2018 as consumption growth slows given the frontloading of expenditure in prior quarters.
- **Recent lower inflation is transitory in nature and not really driven by demand or supply factors.** The headline CPI has come out lower for both July and August at 0.8% yoy and 0.9% yoy respectively possibly as a result of the tax holiday as GST was lifted. Inflation will most likely remain low for the rest of this year before beginning to edge up higher next year. Our forecast for the headline CPI for 2018 stands at 1.8% yoy.
- **The government appears to be trying to ensure that both fiscal and monetary policies are well-coordinated so as to ensure that economic growth remains sustainable.** The ongoing government consolidation may negatively affect growth but Finance Minister Lim Guan Eng has announced the set-up of a public finance committee. It would be chaired by him and joined by Azmin Ali, Minister of Economic Affairs and Bank Negara Malaysia (BNM) governor Nor Shamsiah Yunus as members. Lim Guan Eng has said that the committee will provide a medium-term fiscal plan that while pursuing a fiscal consolidation agenda would also support economic growth through expenditure.
- **Therefore, we continue to expect that BNM will most likely hold rates for the rest of 2018.** At this point, the central bank would probably want to be cautious and continue to monitor the state of the economy as they try to ascertain more strongly the domestic sentiment. They may also wish to more closely monitor the trade tension situation before acting too given how closely tied Malaysia's growth is to the state of the global economy. The ongoing government consolidation may hurt growth in the coming future but as discussed, the set-up of the public finance committee signals that the government will more strongly coordinate fiscal and monetary policies so as to ensure that growth remains sustainable. Inflation as mentioned is also transitory in nature.

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