Malaysia Monitor

Nothing New

Malaysia holds rate, but angles for a rate cut on global concerns

Sep 7, 2016

- **After shocking the market with its rate cut in the July meeting, Bank Negara decided to calm things down a notch by holding rate at 3.0% as expected by us and most in the market.**
- **Not much new information can really be gleaned from today's statement, but we'll still try. Indeed, the very sameness might be a message in and of its own: Things are not great on the exports front, but Malaysia will overall be okay because domestic demand is still resilient.**
- **There is only one more meeting left this year, in November. We expect BNM to help stoke local demand by cutting rate to 2.75% then, after confirming that, try as it may, the government can only give so much fiscal oomph when it announces its 2017 budget in October.**

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Don't get too excited

In an era of so much anticipation for the words and deeds of global central bankers, one can be forgiven for expecting excitement from today's Bank Negara rate announcement as well. This is especially so after the Malaysian central bank sprung a surprise rate cut when it last met two months ago. Alas, its decision to hold rate unchanged at 3.0%, as expected by us but not some in the market, puts paid to that.

Here, the wise words of Paul Samuelson, the first American economist to win the Nobel prize, come to mind, albeit in a different context. On investing, he reportedly quipped that it should be more like watching paint dry or grass grow, and that "*If you want excitement, go to Las Vegas*."

Indeed, the details of the BNM's statement today suggest that its monetary policy should not be the place to look for high drama and nail-biting thrills. Having shocked the market with its rate cut in the July meeting, today's decision to hold can also be seen as a way to calm the market down.

The unexpected nature of that rate cut in the previous meeting had ignited market expectation for further monetary easing. If left unchecked, that runs the risk of turning into a conflagration of expectation for more and more rate cuts. What better way to keep such passionate flames in check, than by creating a firebreak through today's hold?

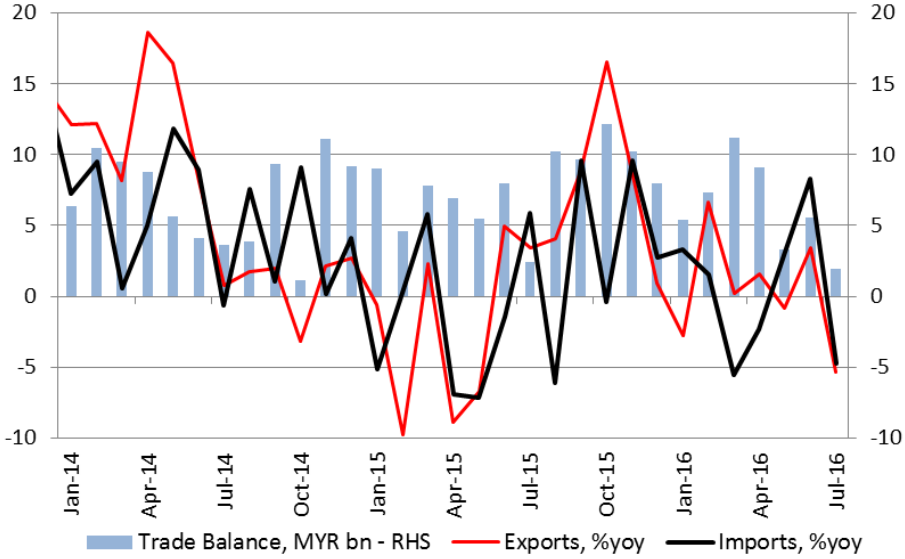
Moreover, it is not as if the economic situation has worsened all that drastically since July. For one, the proximate reason BNM mentioned for its rate cut back then – Brexit – has yet to turn into a heart-stopping global threat. Outside of perhaps the initial Zika virus outbreak – which is, thankfully, more buzzy annoyance than show-stopping epidemic at this point – BNM would have struggled to find another event that could rank as another "clear and present danger" that could warrant an immediate reaction.

Wellian Wiranto
Economist
Treasury Research & Strategy,
Global Treasury,
OCBC Bank

+65 6530-5949
wellianwiranto@ocbc.com

To be sure, the outlook for Malaysian economy can hardly be described as being all that great. As we mentioned in our August 12th note, "*Need A Lift?",* the Q2 GDP data shows that the growth momentum has weakened. Indeed, a drop in sequential growth rate to just 0.7%qoq in Q2, compared to 1.0-1.2% in the previous two quarters, was one reason why we downgraded our 2016 growth forecast from 4.3% to 4.1%.

Similarly, the most recent trade data for the month of July, out just hours before the central bank decision, should dampen hopes for any export-led uplift anytime soon. While market expected exports to grow by 1.9%yoy, the actual data show that shipments actually shrank by as much as 5.3%.



Source: Bloomberg, OCBC.

Still, as much as we focus on these numbers, we must also take a step back and wonder whether they constitute downside surprises for the central bank's own outlook. Our sense is, even as exports weakness would continue to occupy BNM's mind, it does not constitute anything new. It highlighted such concerns quite profusely already in the July statement. In today's version, somewhat of a rehash took place, with talks about how "downside risks to global growth remain high" and that "export growth is expected to remain weak following subdued demand from Malaysia's key trading partners."

Importantly, as a measure of how such 'bad stuff' is already expected and things are not getting worse, BNM said that "the economy is projected to expand within expectations in 2016, and to remain on a steady growth path in 2017."

Overall, taking July's rate cut and today's rate hold together, our sense is that BNM wants to be seen as a central bank which stands ready to act when the situation calls for it, but at the same time, it is wary of engendering market expectation for a back-to-back and protracted rate cut cycle. As we mentioned at the start, we still think BNM is not done with rate cut yet, and that it will likely reach for easing in November after the government's fiscal stance becomes clear as it tables the 2017 budget in October.

Beyond that, into 2017, we think BNM will be most inclined to leave rate unchanged at 2.75%. As we have said before, it would want all the ammunition it has to counter any further downside risk factor. As we step closer and closer into the climax (or ravine?) of US presidential election cycle, perhaps we would all find excitement outside of monetary policy guessing game after all, for better or worse.

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