

Sharp Pick Up in Headline Inflation

Wednesday, July 24, 2019

Key Points

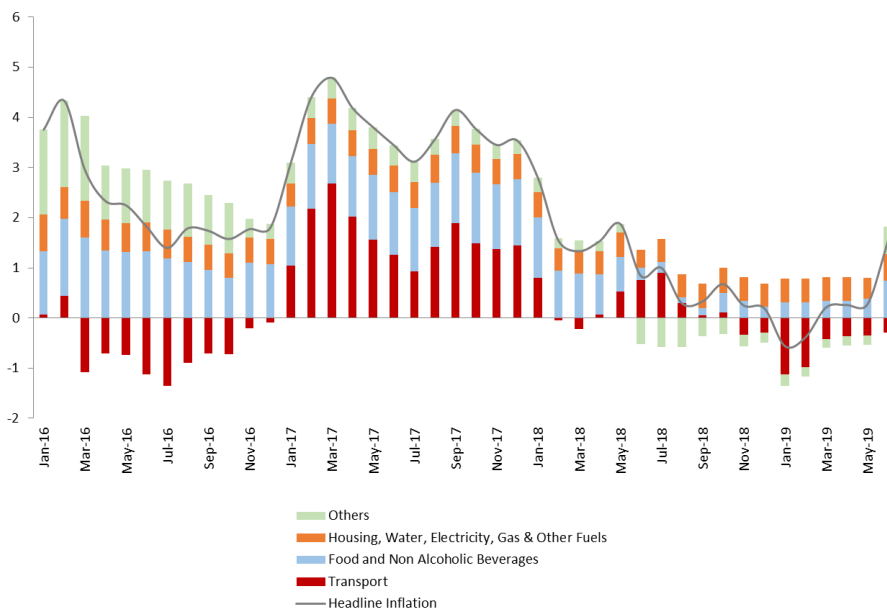
- **Headline inflation sharply picked up for June to 1.5% yoy (May 2019: 0.2% yoy), just slightly above our forecast at 1.4% yoy.**
- **Base effects caused the sharp increase given the tax holiday during the same period last year.**
- **Regardless, we revise our 2019 headline inflation forecast downwards from 1.3% yoy to 0.8% yoy due to the delay in the implementation of the targeted fuel subsidy mechanism.**
- **For now, we still see that Bank Negara Malaysia (BNM) may keep the OPR on hold for the rest of 2019, barring a worsening in growth risks.**

Headline inflation sharply picked up for June to 1.5% yoy (May 2019: 0.2% yoy), which was just slightly above our forecast at 1.4% yoy. Core inflation also rose to 1.9% yoy from 0.4% yoy, the prior month. The sharp increase was possibly due to the wearing off of the effects of the tax regime change. There was a tax holiday in June 2018 whilst in contrast, the sales and service tax (SST) was in effect in June 2019. Hence, most categories (with the exception of transport and education) saw either a significant pick-up in price increases or more subdued deflation. The transport category however saw a substantial price decrease of 2.1% yoy as the fuel price cap continued to be in place.

The inflation trajectory going forward remains heavily subject to the fuel price regime that is to be put in place. The status regarding the implementation of the targeted fuel subsidy mechanism remains uncertain at this point still. The Domestic Trade and Consumer Affairs Minister Datuk Seri Saifuddin Nasution Ismail had said in mid-July that he was optimistic that the scheme can still be implemented this year. Given the delay in the implementation of this scheme, we are now revising our headline inflation forecast for the entire 2019 to average around 0.8% yoy from our initial forecast of 1.3% yoy. This assumes that the price ceiling for RON95 is set at RM2.20 (which was the price fixed at for 2H 2018) for the remainder of 2019 starting from at least some point in August 2019. However, in the event that the existing RON95 price ceiling of RM2.08 is kept for the rest of this year, we envisage that the 2019 headline inflation may average even lower than 0.8% yoy.

As a whole, headline inflation continues to be moderate and we still see that Bank Negara Malaysia (BNM) may keep the OPR on hold for the rest of 2019, barring any worsening in growth risks such as escalating trade tensions.

Chart 1: Contributors to Headline Inflation, % yoy



Source: CEIC, Bloomberg and OCBC

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