

Malaysia: 2018 shaping up to be a better year for inflation

Barring a political uncertainty, the Malaysian ringgit should remain among Asia's top-performing currencies this year



2.7%

January CPI inflation

Year-on-year

As expected

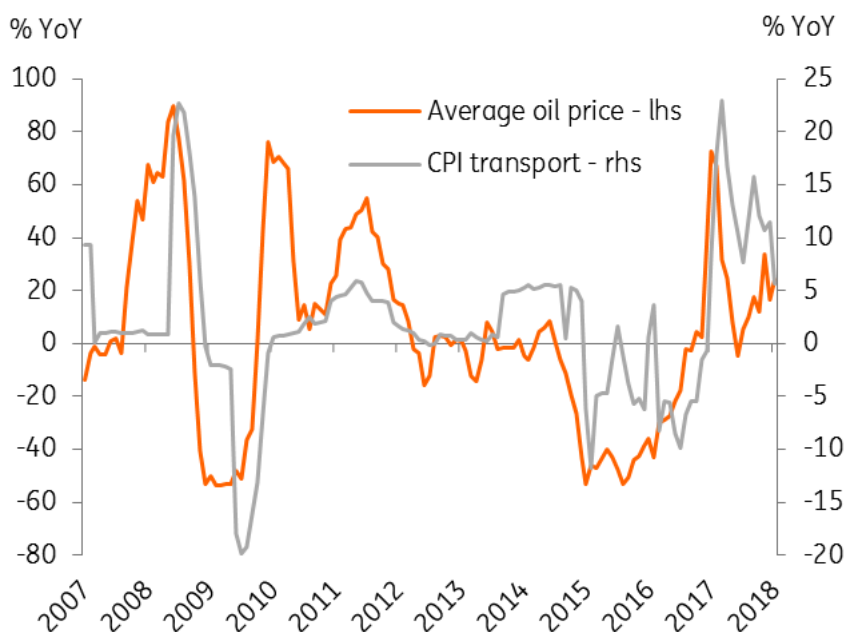
Inflation slows in January

Malaysia's consumer price inflation dipped in line with the consensus to a one-year low of 2.7% year-on-year in January from 3.5% in the previous month (consensus 2.8%, ING forecast 2.7%). Food and transport prices were the main sources of lower inflation with both CPI components starting to enjoy favourable base effects.

2017 was the worst year for Malaysian inflation in a decade with a near-doubling of prices to 3.9% from 2.1% in 2016. Higher transport costs led by fuel prices were mainly responsible. Higher import

prices, as well as factory gate prices, were the other factors. A strong Malaysian ringgit (MYR) last year wasn't much help to prevent imported inflation. The average 6.1% YoY rise in the import unit value index in 2017 compares with a 1.4% rise in 2016. The corresponding figures for producer prices are 6.7% and -1.1%.

Global oil price vs. Malaysia transport price



Source: Bloomberg, ING

2018 a better year for inflation

2018 is shaping up to be a better year for inflation. The high base should continue to dampen year-over-year price increase this year. And the sustained MYR appreciation trend should mitigate the spillover of rising global commodity prices. On the flip-side, strong domestic demand should exert an upward pull on prices. Rapid wage growth (8.6% YoY growth in manufacturing wages in 2017 was the fastest in seven years) and election cash handouts should boost consumer spending.

As things stand, the risk to our 3.0% full-year 2018 inflation forecast appears tilted to the downside. Bank Negara Malaysia (BNM), the central bank, forecasts inflation this year in a 2.5-3.5% range. That said, we expect BNM to continue to normalise monetary policy. BNM raised the policy rate by 25bp to 3.25% in January. We forecast one more 25bp rate hike in the third quarter. Barring a political uncertainty, the MYR should remain among Asia's top-performing currencies this year. Our USD/MYR forecast for end-2018 is 3.72 (spot 3.91, consensus 3.85).