

## Malaysia: CPI Inflation to spike above 4%, again

The monetary and fiscal policy mix supports the prospect of continued strong economic growth, but beware inflation



Source: istock

### Inflation set to stabilise in 2018

We expect the lingering impact of a hike in retail fuel prices in early August and rising food prices to boost CPI inflation above 4% in September (INGF: 4.1%, consensus: 4.3%, prior 3.7%). The authorities are due to release CPI data tomorrow.

Food and oil-related fuel and transport prices have been the main factors responsible for near-doubling of inflation this year to 4.0% YTD in August from 2.3% a year ago. While these factors will mostly remain in play for the rest of the year, we expect the high base effect is likely to push inflation closer to 3% by the end 2017, and further below 3% in 2018.

We forecast average inflation in 2017 of 3.8%, close to the top end of Bank Negara's 3-4% forecast range. Our forecast for 2018 is 2.5%. The consensus forecasts are 3.7% and 2.5% for 2017 and 2018, respectively

## Malaysian ringgit appreciation stubbed by offshore trading curbs

A most likely source of downside inflation risk is accelerated MYR appreciation. The MYR was Asia's best performing currency in September and retains that status in October, moving up from the middle of the Asian pack until the year-to-August. We see a greater potential of MYR appreciation in correction of a large REER-basis undervaluation left by 2014 oil price crash. Although strong economic activity supports the MYR appreciation trend, recent curbs on offshore trading hinder it.

## Monetary tightening measures look increasingly possible

We think the central bank (BNM) may be among the few Asian central banks pondering a monetary tightening as of now (central banks of Korea, Singapore and Philippines are the others). Elevated inflation has left real interest rates in negative territory (the BNM's overnight policy rate is 3.00%). Unless corrected in the period ahead, the continued currency undervaluation will be potentially more inflationary. As for growth, 2017 has shaped to be the best year in last four, with our 5.6% GDP growth revised up recently from 5.4%.

**5.6%** GDP Growth 2017  
Revised up from 5.4%

## Elections in 2018

However, we are inclined to see BNM among the majority of Asian central banks which we expect to start tightening in the second half of 2018, on our view that the authorities will not desire to unsettle growth-friendly macroeconomic policy setting until the general election to be held in August 2018 (though could be called earlier than that if the ruling government wished to capitalize on a strong economic performance and a split opposition). Instead, with an eye on those elections, Prime Minister and Finance Minister Najib are likely to announce a populist Federal Budget for 2018 next week (October 27).