Malaysia: GST removal dents inflation

We revise our 2018 inflation forecast from 1.8% to 1.0%. Lower inflation allows greater scope for the stable central bank policy

Source: Shutterstock

Gone with the Goods and Services Tax (GST) are inflation worries. This could be a loud statement about Malaysia's just-released consumer price data for June. We revise our full-year 2018 inflation forecast from 1.8% to 1.0%. Lower inflation will allow a greater scope for the central bank (Bank Negara Malaysia) to keep the monetary policy stable for a prolonged period, or even ease in the event the global trade war adversely impacts the economy.

0.8%

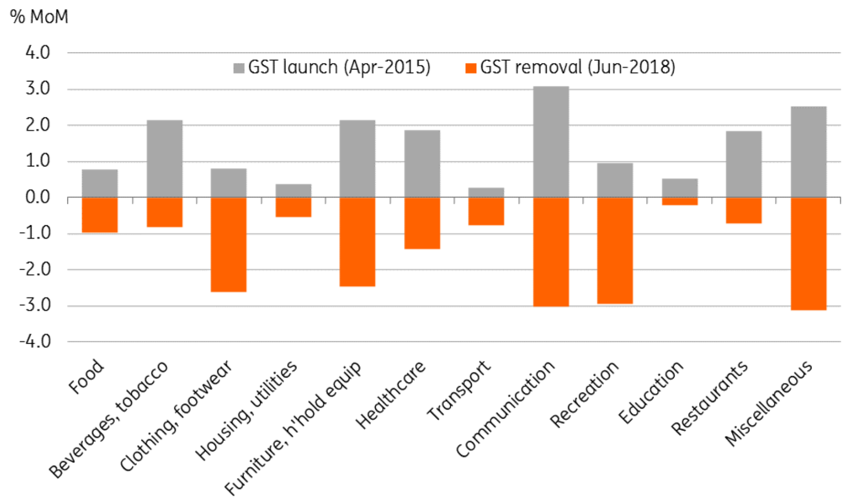
CPI inflation in June

Lower than expected

A downside inflation surprise in June

In a huge downside surprise, CPI inflation slowed to 0.8% year-on-year in June from 1.8% in the previous month. The consensus was centered on 1.3%. A sharp slowdown was mainly the result of the cut in the GST rate from six to zero percent effective June 1 by the new government. The effect is clear from the month-on-month price changes across CPI components, almost mirroring the impact upon the introduction of GST in April 2015 (see figure).

The GST impact



Source: Bloomberg, ING

Downgrade of 2018 inflation forecast, again

The year-to-date inflation of 1.6% YoY has more than halved from 4% a year ago, led by a steep slowdown in key components of food and the transport prices. The GST will be replaced by a less severe Sales and Services Tax (reportedly by September), and any impact is likely to be transitory without significantly reversing the ongoing inflation downtrend.

> *Headline inflation is likely to turn negative in some months and remain low in the first half of 2019 - BNM policy statement in July*

We now see inflation remaining well below 1% in the remainder of the year, or possibly even turning negative as the central bank has pointed out in the latest policy statement. This prompts another downgrade to our full-year 2018 forecast from 1.8% to 1.0%, the second since May when we cut it from 2.4%.