

Malaysia Watch

Inflation not a pressing concern; Spotlight on MYR

Inflation not a pressing concern for now

Headline inflation remained modest at 1.5% yoy in Jan '24. This was below Consensus (1.6%) & ours (1.7%), and unchanged from Dec '23. Core inflation edged lower to 1.8% in Jan vs. 1.9% in Dec, below the 2011-19 average of 2%.

Upside risk to inflation likely contained

#1: Direct impact of new consumption taxes likely manageable – adding around 20bp to 2024 headline inflation. This includes (a) increase in SST for some services by 2ppt to 8% from 1st Mar, and (b) possible introduction of new high-value goods tax of 5-10% from 1st May. See also page 6 of [Year Ahead](#) for detailed calculations.

#2: Timing of subsidy reforms (including RON95) still uncertain amidst data collection challenges. The government plans to use the Central Database Hub (Padu) as the basis to determine eligible subsidy recipients, using a more complex set of criteria. However, to date, just 12% of residents have updated information in Padu ahead of the deadline (31st Mar) – far below the Economy Ministry's target of 80%. In any case, we expect any eventual rollout of targeted subsidies – likely earliest only from Jul and after festive period – to be gradual and modest, and thus reducing tail-risk to inflation.

For now, we maintain 2024 headline inflation forecast at 2% yoy - slightly below MOF's [Oct '23 forecast](#) of 2.1-3.6% (see report) – with softer than expected incoming prints offset by impact of new consumption taxes (we did not factor in previously). In the absence of details, we have not included potential impact from subsidy reforms to RON95 [electricity], which could lift inflation by 8bp [3bp] on a full year basis for every 10% increase in prices which affects 10% of consumers (Exhibit 1 & Exhibit 2).

High hurdle for rate hikes, despite FX pressures

Our base case is for the OPR to remain on an extended pause, with BNM seemingly comfortable on growth outlook (see [4Q23 GDP Review](#)) and inflation not a pressing concern as yet. On OPR setting, we have highlighted in previous notes that (1) it is primarily based on growth-inflation dynamics, and (2) BNM is highly unlikely to utilize the OPR as a direct response to FX and capital outflow pressure. Further, FX pass-through to inflation seems limited, with BNM earlier estimating that 5% depreciation of MYR/USD associated with 0.3% [0.2%] change in headline [core] CPI over a year.

Given the limited inflation pass-through of FX moves and weaker exports recently, FX depreciation may rather be supportive of export growth. This view is consistent with recent data on BNM's FX reserves which have been stable lately, indicating less concern from policymakers. While policymakers see MYR moves as in line with the broader region, bi-lateral weakness against USD could still lead to political pressure to defend the currency. If the volatility picks-up further or there are signs of large-scale speculation or market-dysfunction, BNM could stabilize the market by intervening, tapping USD deposits and tightening liquidity to make it costlier to hedge MYR.

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Glossary

m-o-m: month-on-month

BNM: Bank Negara Malaysia

MOF: Ministry of Finance

SST: Sales & Services Tax

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Exhibit 1: Potential impact on full-year headline CPI from RON95 subsidy reforms (ppt)

The potential impact depends on the timing, subsidy coverage & re-pricing of RON95

Increase in RON95 price vs. RM2.05/litre	RON95 price/litre	Unsubsidized motorists (% of petrol consumption)				
		100%	80%	60%	40%	20%
10%	2.26	0.8	0.6	0.5	0.3	0.2
20%	2.46	1.5	1.2	0.9	0.6	0.3
40%	2.87	3.1	2.4	1.8	1.2	0.6
60%	3.28	4.6	3.7	2.8	1.8	0.9
80%	3.69	6.1	4.9	3.7	2.4	1.2
100%	4.10	7.7	6.1	4.6	3.1	1.5

Source: BofA Global Research estimates, Haver **Note:** We assume that RON95 accounts for 90% of petrol consumption

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Exhibit 2: Potential impact on full-year headline CPI from electricity subsidy reforms (ppt)

The potential impact depends on the timing, subsidy coverage & re-pricing of electricity prices

Increase in electricity prices vs. current levels	% of household consumption affected				
	100%	80%	60%	40%	20%
10%	0.3	0.2	0.2	0.2	0.1
20%	0.5	0.4	0.4	0.3	0.2
40%	1.1	0.9	0.8	0.6	0.4
60%	1.6	1.3	1.1	1.0	0.6
80%	2.2	1.7	1.5	1.3	0.9
100%	2.7	2.2	1.9	1.6	1.1

Source: BofA Global Research estimates, Haver

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