

Malaysia Consumer Price Index

Edged lower to 3.5% YoY in March

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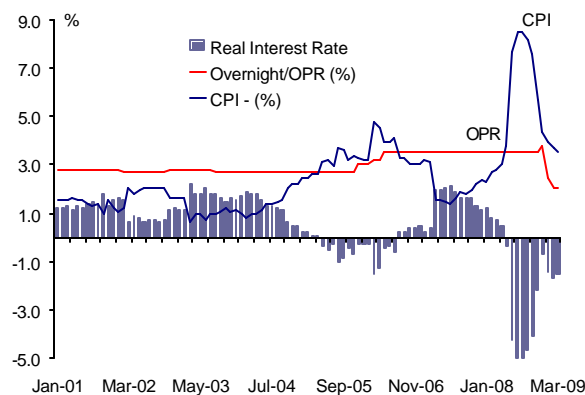
HIGHLIGHTS

- Malaysia's **Consumer Price Index (CPI) edged lower to 3.5% YoY in March from 3.7% in February**. It was slightly below consensus and our estimate of 3.6%. A combination of weakening domestic demand and continued decline in commodity prices exerted downward pressure on inflation.
- The growth downtrend of CPI will continue until it reaches 2H09 when deflation starts to kick in. Average growth in the 1H09 is forecast at 2.6% while the 2H09 will likely see the CPI decline by 1.2%. Hence, **on average the CPI is projected to slow sharply to 0.8% in 2009 from 5.4% in 2008**.
- Given further deceleration in CPI growth trend, we believe it will continue to provide BNM the flexibility to reduce the Overnight Policy Rate (OPR) by another 50 basis points (bps) to support the economy. Nonetheless, **we expect the rate cut would be measured and gradual or 25 bps each at its two remaining policy meetings before end of 1H09**.

Slightly lower than expected. Malaysia's **Consumer Price Index (CPI) continues to edge lower to 3.5% YoY in March from 3.7% in February**. It was slightly below consensus and our estimate of 3.6%. From the preceding month, it fell 0.2%. A combination of weakening domestic demand and continued decline in commodity prices exerted downward pressure on inflation. The average CPI growth for the first three months of this year was 3.7% a deceleration from 5.9% in 4Q08.

Monthly downtrend resumes. March saw the CPI fell by 0.2% MoM after it registered a positive 0.1% MoM in February. The main contributor to the monthly contraction was food and non-alcoholic beverages index which fell 0.5% MoM, its first decline in a year. The other major contributor to the decline was housing, water, electricity, gas and other fuels index which fell 0.1%, its first decline since June last year. Though the monthly CPI contraction may not be


CPI Vs. Overnight Policy Rate Trend



Source: Department of Statistics, Kenanga Research

a prominent feature the base effect will continue to influence the CPI downtrend till the 2H09. **Even if we assume the monthly growth trend to remain positive in the coming months, the prospect of a deflation will persist.**

Deflation in 2H09. The growth downtrend of CPI will continue until it reaches 2H09 when deflation starts to kick in. Average growth in the 1H09 is forecast at 2.6% while the 2H09 will likely see the CPI decline by 1.2%. Hence, **on average the CPI is projected to slow sharply to 0.8% in 2009 from 5.4% in 2008**. Nonetheless, we reiterate that deflation will not pose a problem given that it is largely the result of a high-base effect. Deflation would only be detrimental if it prolonged. However, **we expect that a pick-up in global commodity prices on the back of a global economic recovery will push domestic CPI up by 2.0% in 2010.**

Still room to adjust rates. Given further deceleration in CPI growth trend, we believe it will continue to provide BNM the flexibility to reduce the Overnight Policy Rate (OPR) by another 50 basis points (bps) to support the economy. Nonetheless, **we expect the rate cut would be measured and gradual or 25 bps each at its two remaining policy meetings before end of 1H09**. The next two BNM Monetary Policy Committee meetings to decide on the rates will be on April 29 and May 26. 

CPI & Its Major Components Growth Trend (%YoY)

Base 2005=100	weight	2006	2007	2008	Mar-08	Nov-08	Dec-08	Jan-09	Feb-09	Mar-09	Jan-Mar 09	Jan-Mar 09
CPI	100.0	3.6	2.0	5.4	2.8	5.7	4.4	3.9	3.7	3.5	2.6	3.7
Core Inflation (Ex -Food & NAB)	68.6	3.7	1.6	3.0	1.8	2.9	1.0	0.7	0.6	0.5	1.7	0.6
Food & Non-Alcoholic Bev. (NAB)	31.4	3.4	3.0	8.8	4.9	11.0	10.4	9.8	9.2	8.8	4.4	9.2
Alcoholic Bev. & Tobacco	1.9	6.9	7.8	7.3	9.0	8.4	8.4	8.3	8.2	8.3	9.0	8.3
Clothing & Footwear	3.1	-1.3	-1.4	-0.5	-0.9	-0.5	0.1	-0.8	-0.6	-0.6	-0.8	-0.8
Hous'g, Water, Elec.Gas & Fuels	21.4	1.5	1.3	1.6	1.4	1.8	1.8	1.7	1.5	1.4	1.3	1.6
Furnishing & Household Equipm't	4.3	1.1	1.1	3.0	1.5	4.5	4.6	4.9	4.7	4.5	1.4	4.6
Health	1.4	2.2	1.6	2.2	1.8	2.8	2.6	2.6	2.7	2.6	1.8	2.6
Transport	15.9	11.0	2.3	8.8	0.8	6.2	-0.3	-2.1	-2.1	-2.1	0.9	-2.1
Communication	5.1	-1.4	-1.2	-0.6	-0.6	-0.6	-0.6	-0.5	-0.5	-0.6	-0.7	-0.5
Recreation Services & Culture	4.6	0.8	1.4	1.8	2.7	1.3	1.3	1.1	1.0	1.0	2.6	1.0
Education	1.9	1.6	1.8	2.3	2.1	2.8	2.8	3.0	2.5	2.5	1.9	2.7
Restaurants & Hotels	3.0	3.7	3.7	6.6	7.1	5.6	5.2	4.6	4.3	4.2	7.0	4.4
Misc. Goods & Services	6.0	2.3	1.0	3.3	3.7	2.4	2.6	2.7	3.8	3.6	3.3	3.4

Source: Department of Statistics, Kenanga Research


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