

Malaysia Consumer Price Index

Fell a record 2.4% in July, expect no change in BNM monetary stance

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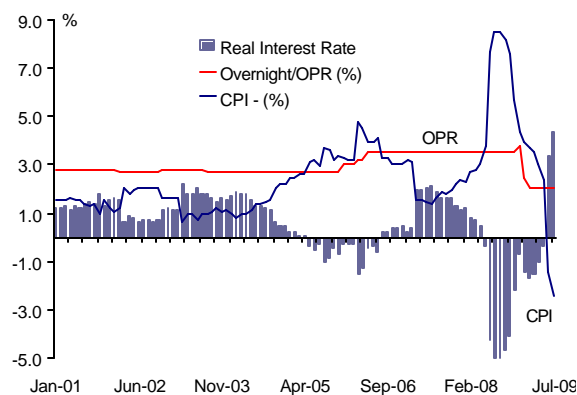
HIGHLIGHTS

- The **Consumer Price Index (CPI) contracted further to a record low of 2.4% in July from 1.4%**. It was within market expectation but smaller than our estimate of -2.6%. However, it continued to edge up by 0.1% MoM in July, its third consecutive month of increase. For the first seven months, its growth decelerated sharply to 1.7% compared with 4.4% in the same period a year ago.
- Though the base effect and weak economic growth will heightened the deflationary trend, it may soon be mitigated by fuel price revision in September and a pick up in economic growth in 4Q09. **On average the CPI may contract by at least 1.0% in 2H09 versus 2.5% in 1H09. Hence, the CPI is projected to decelerate to 0.6% this year from 5.4% in 2008.** An expected higher fuel and commodity prices backed by economic recovery, the CPI is projected to expand to 2.2% in 2010.
- Though the current deflationary trend will allow BNM room to adjust interest rates to support the economy, **we reckon that the benchmark Overnight Policy Rate may just stay put at 2.00% for the next 6-12 months.** A further rate cut may be counter productive as it may artificially inflate the monetary base and temper recovery process.

A record low. The **Consumer Price Index (CPI) for July plunged to its record low based on the data we compiled since 1976. It contracted further to a record low of 2.4% in July from 1.4%**. It was within market expectation (based on *Bloomberg's* consensus median) but smaller than our estimate of -2.6%. However, it continued to edge up by 0.1% MoM in July, its third consecutive month of increase. For the first seven months, its growth decelerated sharply to 1.7% compared with 4.4% in the same period a year ago.

Food and transport help mitigate contraction. The MoM increase in the major indices, food and transport, helped to put the brakes on CPI's


Deflationary trend pushes real interest rate up



Source: Department of Statistics, Kenanga Research

annualized contraction. The food and non-alcoholic beverage index grew 0.2% MoM, its third consecutive month of increase, while the transport index edged up by 0.1% MoM in July. Nonetheless, on YoY the food index was the lowest since May 2004 while the transport index registered its worst decline at -19.9% in July. This was primarily due to an official hike on fuel prices by 41% in June last year.

A temporary deflation in 2H09. Though the base effect and weak economic growth will heightened the deflationary trend, it may soon be mitigated by fuel price revision in September and a pick up in economic growth in 4Q09. **On average the CPI may contract by at least 1.0% in 2H09 versus 2.5% in 1H09. Hence, the CPI is projected to decelerate to 0.6% this year from 5.4% in 2008.** An expected higher fuel and commodity prices backed by economic recovery, the CPI is projected to expand to 2.2% in 2010.

Monetary policy to remain unchanged. Though the current deflationary trend will allow BNM room to adjust interest rates to support the economy, **we reckon that the benchmark Overnight Policy Rate may just stay put at 2.00% for the next 6-12 months.** A further rate cut may be counter productive as it may artificially inflate the monetary base and temper recovery process going forward. 

CPI & Its Major Components Growth Trend (%YoY)

Base2005=100	weight	2006	2007	2008	Jul-08	Mar-09	Apr-09	May-09	Jun-09	Jul-09	Jan- Jul 08	Jan- Jul 09
CPI	100.0	3.6	2.0	5.4	8.5	3.5	3.0	2.4	-1.4	-2.4	4.4	1.7
Core Inflation (Ex -Food & NAB)	68.6	3.7	1.6	3.0	7.1	0.6	0.5	0.9	-3.9	-4.8	3.2	-0.8
Food & Non-Alcoholic Bev. (NAB)	31.4	3.4	3.0	8.8	11.2	8.8	7.5	5.2	3.4	2.0	7.7	8.2
Alcoholic Bev. & Tobacco	1.9	6.9	7.8	7.3	0.5	8.3	8.3	8.1	8.1	8.0	7.7	8.2
Clothing & Footwear	3.1	-1.3	-1.4	-0.5	-0.4	-0.6	-0.6	-0.7	-1.1	-0.9	-0.6	-0.7
Hous'g, Water, Elec.Gas & Fuels	21.4	1.5	1.3	1.6	1.8	1.4	1.4	1.6	2.0	1.3	1.4	1.6
Furnishing & Household Equipm't	4.3	1.1	1.1	3.0	3.5	4.5	4.4	4.2	3.5	2.4	2.0	4.1
Health	1.4	2.2	1.6	2.2	2.3	2.6	2.4	2.5	2.5	2.3	2.0	2.5
Transport	15.9	11.0	2.3	8.8	22.7	-2.1	-2.3	-2.5	-18.0	-19.9	6.7	-7.7
Communication	5.1	-1.4	-1.2	-0.6	-0.6	-0.6	-0.5	-0.4	-0.5	-0.4	-0.6	-0.5
Recreation Services & Culture	4.6	0.8	1.4	1.8	0.9	1.0	0.9	1.0	1.0	0.7	2.1	1.0
Education	1.9	1.6	1.8	2.3	2.4	2.5	2.5	2.5	2.3	2.4	2.1	2.5
Restaurants & Hotels	3.0	3.7	3.7	6.6	6.7	4.2	3.9	3.7	3.1	2.4	7.0	3.8
Misc. Goods & Services	6.0	2.3	1.0	3.3	4.2	3.6	3.6	3.6	3.7	3.0	3.4	3.5

Source: Department of Statistics, Kenanga Research

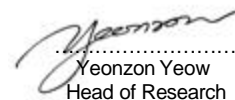
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