KENANGA RESEARCH

Economic Viewpoint

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Malaysia Consumer Price Index

Fell 1.6% in October, inflation to re-start soon

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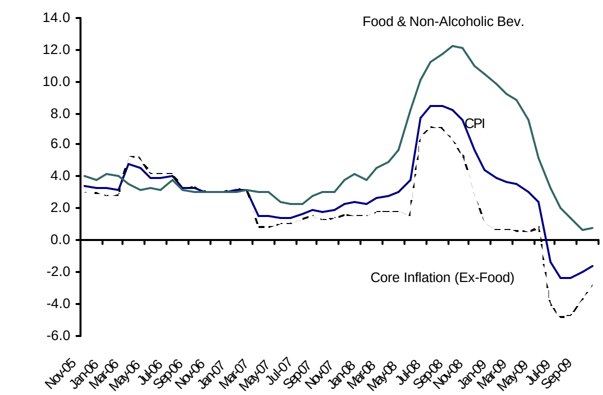
HIGHLIGHTS

- **Consumer Price Index (CPI) fell 1.6% in October, its smallest decline since June this year.** However, it was slightly bigger than consensus and our expectation of -1.4%. Compared with the preceding month it only edge up by 0.1%. In the first ten months, its growth lowered sharply to 0.6% compared with 5.5% in the same period a year ago.

- As inflation had peaked in 3Q of last year, the lower base effect has started to kick in, resulting in a reversal of deflationary trend in 4Q09. Along with the impact of improved economic environment, we project the CPI to rebound to 0.2% in 4Q09 after contracting by 2.3% in 3Q09. **On average the CPI is projected is projected to decelerate to 0.6% this year from 5.4% in 2008. For next year, the CPI is forecast to expand by 2.1% on the back of economic recovery.**

- In spite of the upward trajectory in inflationary trend we do not expect BNM to change its current easy monetary stance. This is because it still needs to nurse the seemingly weak recovery trend going forward. Hence, **we expect the benchmark Overnight Policy Rate to stay at 2.00% at least till 1H 2010.**

A diminishing deflationary trend



Source: Department of Statistics, Kenanga Research

Decline still higher than expected. The higher base effect is waning off. **Consumer Price Index (CPI) fell 1.6% in October, its smallest decline since June this year.** However, it was slightly bigger than consensus (Based on *Reuter's* survey) and our expectation of -1.4%. Compared with the preceding month it only edge up by 0.1%. In the first ten months, its growth lowered sharply to 0.6% compared with 5.5% in the same period a year ago.

Higher Food put the brakes on deflation. The large MoM increase in the major indices namely, alcoholic beverage and food helped to put the brakes on CPI's YoY contraction. The food and non-alcoholic beverage index grew 0.3% MoM, while the alcoholic beverage and tobacco jumped 2.8% MoM following the Government's surprise move to raise the excise duty on tobacco by around 5.6% on Oct 1, ahead of the Budget demonstrate d its resolve to boost revenue.

Inflation to re-start in 4Q09. As inflation had peaked in 3Q of last year, the lower base effect has started to kick in, resulting in a reversal of deflationary trend in 4Q09. Along with the impact of improved economic environment, we project the CPI to rebound to 0.2% in 4Q09 after contracting by 2.3% in 3Q09. **On average the CPI is projected is projected to decelerate to 0.6% this year from 54% in 2008. For next year, the CPI is forecast to expand by 2.1% on the back of economic recovery.**

Monetary policy to remain unchanged. In spite of the upward trajectory in inflationary trend in the coming months we do not expect BNM to change its current easy monetary stance. This is because it still needs to nurse the seemingly weak recovery trend going forward. Hence, **we expect the benchmark Overnight Policy Rate to stay at 2.00% at least till 1H 2010.**

CPI & Its Major Components Growth Trend (%YoY)

Base 2005=100	**weight**	**2006**	**2007**	**2008**	*Oct-08*	Jun-09	Jul-09	Aug-09	Sep-09	**Oct-09**	Jan-Oct 08	**Jan-Oct 09**
CPI	***100.0***	**3.6**	**2.0**	**5.4**	***7.6***	**-1.4**	**-2.4**	**-2.4**	**-2.0**	**-1.6**	**5.5**	**0.6**
Core Inflation (Ex-Food & NAB)	*68.6*	3.7	1.6	3.0	*5.3*	-3.9	-4.8	-4.8	-3.7	-2.8	4.1	-1.7
Food & Non-Alcoholic Bev. (NAB)	*31.4*	3.4	3.0	8.8	*12.1*	3.4	2.0	1.4	0.7	0.8	8.5	4.8
Alcoholic Bev. & Tobacco	*1.9*	6.9	7.8	7.3	*8.3*	8.1	8.0	8.0	0.1	2.9	7.1	6.8
Clothing & Footwear	*3.1*	-1.3	-1.4	-0.5	*0.1*	-1.1	-0.9	-0.8	-0.9	-1.5	-0.6	-0.9
Hous'g, Water, Elec.Gas & Fuels	*21.4*	1.5	1.3	1.6	*1.8*	2.0	1.3	1.1	1.0	1.0	1.5	1.4
Furnishing & Househld Equipm't	*4.3*	1.1	1.1	3.0	*4.5*	3.5	2.4	2.0	1.8	1.6	2.7	3.4
Health	*1.4*	2.2	1.6	2.2	*2.6*	2.5	2.3	2.2	2.2	1.9	2.1	2.3
Transport	*15.9*	11.0	2.3	8.8	*13.9*	-18.0	-19.9	-19.3	-16.2	-13.2	10.1	-10.4
Communication	*5.1*	-1.4	-1.2	-0.6	*-0.5*	-0.5	-0.4	-0.4	-0.5	-0.5	-0.6	-0.5
Recreation Services & Culture	*4.6*	0.8	1.4	1.8	*1.4*	1.0	0.7	2.6	2.5	2.4	1.8	1.4
Education	*1.9*	1.6	1.8	2.3	*2.8*	2.3	2.4	2.4	2.2	2.1	2.3	2.5
Restaurants & Hotels	*3.0*	3.7	3.7	6.6	*6.6*	3.1	2.4	2.1	1.9	1.7	6.8	3.2
Misc. Goods & Services	*6.0*	2.3	1.0	3.3	*4.2*	3.7	3.0	3.3	4.2	3.2	3.5	3.5

Source: Department of Statistics, Kenanga Research

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