

# Malaysia CPI, Jan 2015

## Temporary disinflation...

- Inflation rate dropped sharply in Jan 2015 to +1.0% YoY (Dec 2014: +2.7% YoY) mainly due to lower transport costs as crude oil price plunge led to cheaper fuel prices.
- Adjust our 2015 inflation forecast to 3.0%-4.0% from 4.0%.
- Amid volatility and mixed trends in key factors influencing inflation, namely volatility in crude oil price and MYR; application of incentive-based regulation (IBR) on electricity tariff; still uncertain price impact of GST.

**Inflation rate in Jan 2015 dropped to +1.0% YoY** (Dec 2014: +2.7% YoY) and -1.1% MoM (Dec 2014: -0.1% MoM), mainly on the impact of the cut in the retail fuel prices that resulted in -6.0% YoY and -9.6% MoM declines in “*Transport*” cost.

**Revised our 2015 inflation rate forecast to 3.0%-4.0% from 4% amid volatility and mixed trends in key determinants.** CPI is likely to remain low in Feb 2015 as fuel prices were cut further this month. However, fuel prices may rise in Mar 2015 as crude oil prices rebounded recently. Meanwhile, the implementation of fuel cost pass through mechanism under the incentive-based regulation (IBR) on Tenaga’s electricity tariff means the costs of power will be market-driven depending on the movements of the energy commodity prices that make up Tenaga’s fuel mix. On the incoming GST on 1 Apr 2015, although in general, prices should pick up due to the broad-based nature of the tax, the inflationary effect depends on industries’ responses in terms of the pass through, which so far appears to be mixed, based on feedbacks and indications from sectors like telecommunications, gaming, auto and property. We also expect a volatile Ringgit this year with weakness bias on average.

**Expect Bank Negara Malaysia (BNM) to keep the Overnight Policy Rate (OPR) at 3.25% in 2015.** This is in view of the recent downward revisions to the official real GDP growth and inflation rate forecasts for this year. At the same time, with BNM still maintaining the reference to the risk of financial imbalances in its Monetary Policy Statement (MPS), we are not expecting OPR cut, notwithstanding the recent trends of monetary policy easing and benchmark interest rate cuts by central banks across the globe.

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## Malaysia: Consumer price index (CPI, 2010=100)

% YoY	Jul 14	Aug 14	Sep 14	Oct 14	Nov 14	Dec 14	Jan 15	2014	2013
Total	3.2	3.3	2.6	2.8	3.0	2.7	1.0	3.2	2.1
Food and Non-Alcoholic Beverages (FNAB)	3.1	3.3	3.2	2.8	2.9	2.4	2.8	3.3	3.6
Alcoholic Beverages & Tobacco	11.6	11.6	14.8	0.2	10.5	10.6	10.6	11.6	6.0
Clothing and Footwear	(0.2)	(0.2)	(0.3)	(0.4)	(0.4)	(0.3)	(0.1)	(0.2)	(0.6)
Housing, Water, Electricity, Gas and Other Fuels	3.2	3.4	3.4	3.4	3.5	3.4	2.1	3.4	1.7
Furniture, Household Equipment and Routine Household Maintenance	0.8	1.1	0.9	0.9	0.8	0.6	0.5	1.1	1.5
Health	3.3	3.3	3.4	3.4	3.4	3.3	3.2	2.9	1.9
Transport	5.4	5.5	0.5	5.3	5.0	4.0	(6.0)	4.8	2.0
Communication	(0.7)	(0.7)	(0.8)	(0.9)	(0.9)	(0.9)	(1.0)	(0.7)	(0.7)
Recreation Services and Culture	1.9	1.8	1.9	1.8	1.3	0.0	0.5	1.6	0.1
Education	2.3	2.5	2.4	2.4	2.2	2.2	2.1	2.4	2.4
Restaurants & Hotels	5.0	5.1	4.8	4.6	4.3	4.1	3.4	4.6	2.5
Miscellaneous Goods & Services	1.4	0.9	0.7	0.7	0.9	1.4	1.7	0.6	0.3

Source: Dept. of Statistics

## Down on pass-through effect of lower fuel prices

Inflation rate in Jan 2015 dropped sharply to +1.0% YoY (Dec 2014: +2.7% YoY; Maybank-KE: +2.2% YoY; Consensus: +1.9% YoY) as reduction in retail fuel prices resulted in -6.0% YoY drop in “Transport” cost. MoM, CPI fell -1.1% MoM (Dec 2014: -0.1% MoM).

“Transport” cost was virtually the entire reason for the moderation in inflation rate as it fell -6.0% YoY (Dec 2014: +4.0% YoY) and -9.6% MoM (Dec 2014: -1.3% MoM) drop, reflecting the pass through of lower crude oil prices to petrol and diesel prices via the implementation of the manage float retail fuel pricing mechanism since Dec 2014. Retail prices for RON97, RON95 and diesel in Jan 2015 were reduced to MYR2.11/litre (Dec 2014: MYR2.46/litre), MYR1.91/litre (Dec 2014: MYR2.26/litre) and MYR1.93/litre (Dec 2014: MYR2.23/litre). Their prices were further reduced on 1 Feb 2015 to MYR2.00/litre for RON97 and MYR1.70/litre for RON95 and diesel, which should keep Feb 2015 CPI at sub-2% YoY.

“Housing, Water, Electricity, Gas and Other Fuels” (HWEGOF) was another key contributor as it eased to +2.1% YoY (Dec 2014: +3.4% YoY) and -0.5% MoM (Dec 2014: 0.0% MoM).

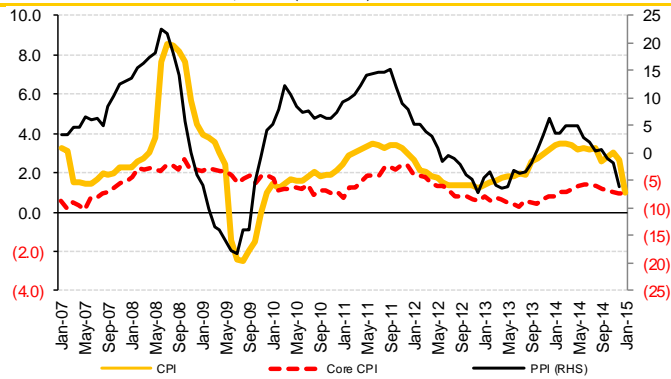
**Outweighing the rise in other key CPI components.** Prices of “Food and Non-Alcoholic Beverages” (FNAB) edged up (Jan 2015: +2.8% YoY; Dec 2014: +2.4% YoY) while “Alcoholic Beverages & Tobacco” maintained its double-digit rise due to cigarette price hikes (Jan 2015: +10.6% YoY; Dec 2014: +10.6% YoY) following the 12% increase in tobacco excise duty effective 1 Nov 2014.

Services inflation rate was relatively stable (Jan 2015: +2.8% YoY; Dec 2014: +2.9% YoY) amid mixed trends in the its components, namely “Recreation Services & Culture” (Jan 2015: +0.5% YoY; Dec 2014: +0.0% YoY), “Restaurants & Hotels” (Jan 2015: +3.4% YoY; Dec 2014: +4.1% YoY), “Health” (Jan 2015: +3.2% YoY; Dec 2014: +3.3% YoY) and “Miscellaneous Goods & Services” (Jan 2015: +1.7% YoY; Dec 2014: +1.4% YoY).

**But stable core inflation**

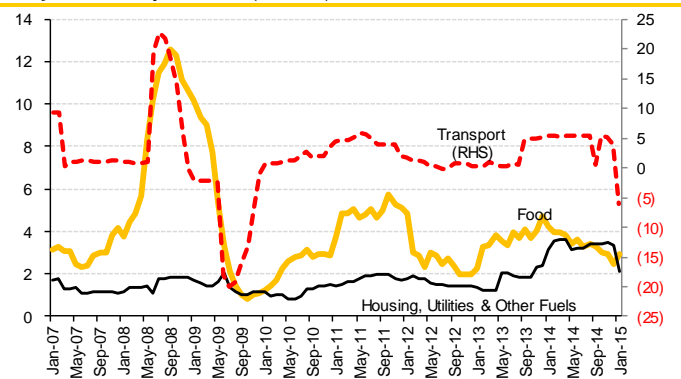
Our measure of core inflation rate (excluding “FNAB”, “Transport” and “HWEGOF” to strip out the subsidised and volatile components of CPI) was stable at +1.7% YoY (Dec 2014: +1.7% YoY) but fell -1.1% MoM (Dec 2014: 0.0% MoM). Further excluding the impact of the tax-related cigarette price hike by removing “Alcoholic Beverages & Tobacco” from our core inflation computation, the adjusted core inflation figure edged up to +1.0% YoY (Dec 2014: +0.9% YoY) and +0.3% MOM in Jan 2015 (Dec 2014: 0.0% MoM).

**Headline & Core CPI, PPI (% YoY)**



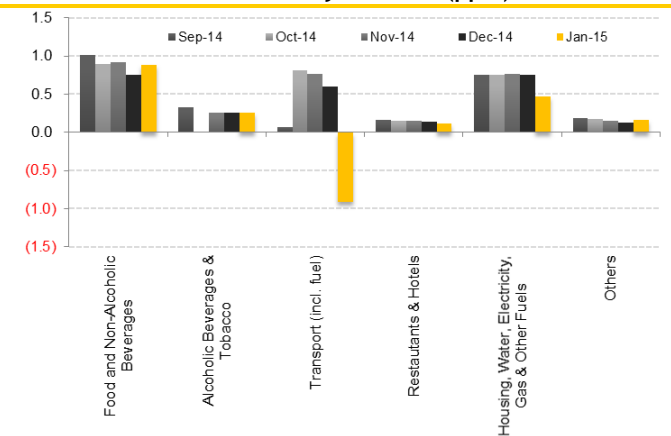
Sources: Dept of Statistics, Maybank KE

**Key CPI Components (% YoY)**



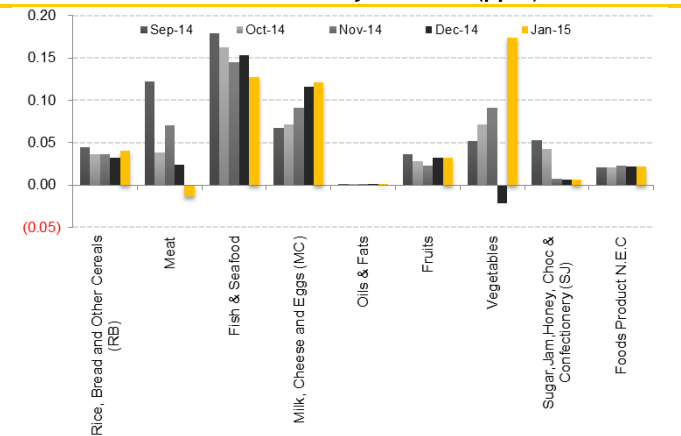
Sources: Dept of Statistics, Maybank KE

**CPI: Contributions to Monthly Inflation (ppts)**



Sources: Dept of Statistics, Maybank KE

**FNAB: Contributions to Monthly Inflation (ppts)**



Sources: Dept of Statistics, Maybank KE

## Volatile & mixed trends in key determinants of 2015 inflation

Revised our 2015 inflation forecast to 3.0%-4.0% (official 2015: 2.5-3.5%; 2014: 3.2%) from 4.0% previously. The revision reflects the volatility in, and the mixed picture on, the key factors influencing inflation. This is in view of the volatile crude oil price so far this year; the application of incentive-based regulation (IBR) on electricity tariff that will be affected by the movements in the prices of energy commodities that makes up Tenaga's fuel cost mix; the still uncertain effect of GST introduction on 1 Apr 2015; and the expectation of volatility - with weakness bias - in the Ringgit.

**Volatile crude oil price - so volatile fuel prices...?** Fuel prices were further reduced on 1 Feb 2015 following continued decline in crude oil prices in Jan 2015. RON97 price was cut to MYR2.00/litre (Jan 2015: MYR2.11/litre) and the costs of RON95 and diesel were both lowered to MYR1.70/litre (Jan 2015: MYR1.91/litre and MYR1.93/litre). However crude oil price (Brent) rebounded sharply so far this month to average USD57/bbl versus the USD48/bbl average in Jan 2015. Under the managed float retail fuel pricing mechanism that replaced the blanket fuel subsidy, the prices of RON97, RON95 and diesel for the current month are set by the Government based on the average prices of the related benchmark petroleum product prices that are tied to the crude oil price movement. The crude oil price trends in Feb 2015 should result in increase in fuel prices in Mar 2015.

**Implementation of IBR on Tenaga's electricity tariff to add to volatility in producer costs and consumer prices?** Under the fuel cost pass-through mechanism, which is part of IBR, Tenaga Nasional Berhad (TNB) will cut its electricity tariff by 2.25 sen/kwh or 5.8% for Peninsula Malaysia and by 1.20 sen/kwh or 3.5% for Sabah & Labuan for the period Mar-June 2015. Such a mechanism will result in market-driven cost of electricity, subject to the movements in energy commodity prices that affect Tenaga's fuel costs.

**Factually and historically, GST should be inflationary.** From the list of taxable and non-taxable goods issued by the Royal Customs in Jan 2015, we noted that out of the 1,852 items listed, only 13% are zero-rated while the rest are standard rated (6%), underlining the point about GST being a broad-based tax versus the Sales Tax and Services Tax it is replacing comes 1 Apr 2015. Moreover, the experience of other countries that introduced (or raise the tax rate) GST or similar tax (VAT, consumption tax) confirmed the one-off inflationary effect.

**The price effect of GST also hinges on industries' response to GST, which will be mixed based on indications so far.** For example, in telecommunication sector, the 6% GST on the prepaid segment is expected to be passed on to the subscribers, compared to the current 6% Services Tax which is absorbed by the telecommunication companies. For gaming, the casinos and number forecast operators (NFOs) will absorb the GST. There is no guarantee that car prices will fall as a result of replacing the 10% Sales Tax with the 6% GST. The Malaysian Automotive Association (MAA) pointed out recently that for current stock held by distributors and dealers, Customs regulations denote that car companies cannot claim the entire 10% Sales Tax, but only 2% of that. This is so because many companies buy vehicles not directly from a licensed manufacturer but through a distributor. The full claim of the Sales Tax is only for vehicles

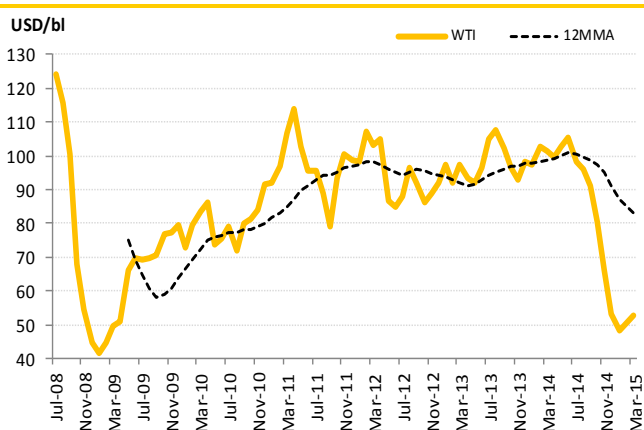
purchased directly from licensed manufacturers. Hence, the remaining 8% of Sales Tax has to be borne by the company or be passed on to customers. The 6% GST is also applied to the on-the-road selling price, which includes accessories, road tax, insurance and profit margin. Meanwhile, property developers have highlighted that there will be increase in house prices due to GST since although the purchases of residential properties are not subjected to GST, the various inputs to the process of home construction are charged with GST, and there will be some pass through to buyers. Some of these are not CPI item e.g. house prices, but will affect cost of living nonetheless.

**Nationwide price reduction campaign.** Meanwhile, amid recent public outcry over the apparent lack of pass-through impact of lower fuel prices on the prices of other goods and services, especially the essential items, the Government is launching a nationwide price reduction campaign. For a start, a few hypermarkets as well as restaurants have already cutting prices, while Nestle will announce product price cut in the range of 10%-20% on 28 Feb 2015.

## Global commodity prices remain soft

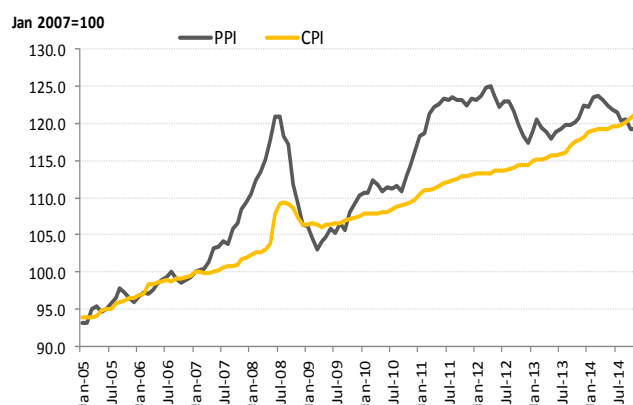
The FAO Food Price Index<sup>1</sup> continue its downward trend, sliding -1.9% MoM in Jan 2015 (Dec 2014: -1.7% MoM). The drop was attributed to fall in all sub-indices while sugar and dairy were unchanged. As for cereal, wheat prices posted a sharp -7.0% fall on ample supply and higher likelihood of higher inventories this year. Sugar prices was sustained with uncertainty over sugar harvest in Brazil, expectations of ample supplies in major sugar producing countries such as India, Thailand and the EU. Dairy products were essentially unchanged as supplies we disrupted over dry weather in Oceania while output in the EU has been curbed to avoid over-quota levies as the Apr-Mar quota year draws to a close.

### Global: Crude oil price bottomed...?



Sources: IMF

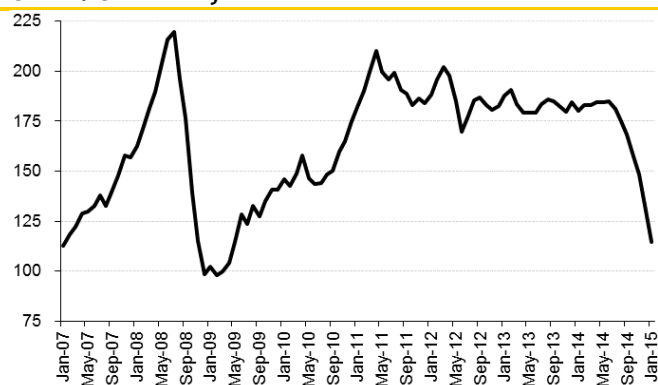
### Malaysia: Consumer Price Index (CPI) vs Producer Price Index (PPI) - Unlike 2008, CPI and PPI are not correlated now



Sources: Dept of Statistics, Maybank KE

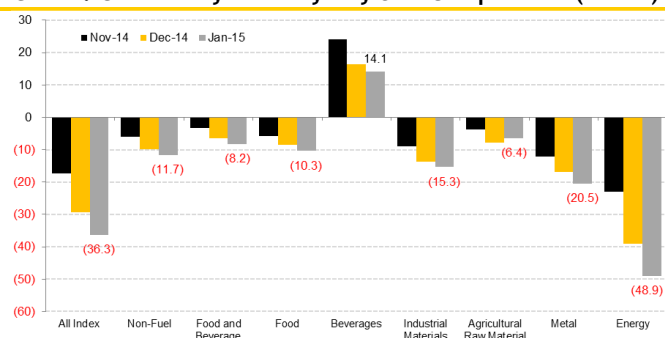
<sup>1</sup> FAO Food Price Index comprise average of five commodity food price indices; meat, dairy, cereals, oils and sugar.

## Global: Commodity Price Index



Source: IMF

## Global: Commodity Price by Key Sub-Components (% YoY)



Source: IMF

## Global Commodity Prices (% YoY)

Type of Commodity	Sep-14	Oct-14	Nov-14	Dec-14	Jan-15	2014	2013
All index	(9.0)	(13.6)	(17.5)	(29.3)	(36.3)	(6.3)	(1.4)
Non-fuel index	(4.3)	(6.4)	(6.0)	(9.9)	(11.7)	(4.0)	(1.2)
Food and beverage index	(3.3)	(4.8)	(3.3)	(6.4)	(8.2)	(2.1)	0.1
Food index	(6.1)	(8.0)	(5.8)	(8.5)	(10.3)	(4.2)	1.3
Beverages index	27.1	29.9	24.1	16.4	14.1	20.9	(11.9)
Industrial materials index	(5.4)	(8.4)	(8.9)	(13.6)	(15.3)	(5.9)	(2.2)
Agricultural raw material Index	1.5	(0.6)	(3.6)	(7.9)	(6.4)	2.0	1.6
Metal index	(9.1)	(12.3)	(12.1)	(17.0)	(20.5)	(10.1)	(4.2)
Energy index	(11.3)	(17.1)	(23.2)	(39.0)	(48.9)	(7.4)	(1.4)

Source: IMF

## Global Commodity Prices (% MoM)

Type of Commodity	Jul-14	Aug-14	Sep-14	Oct-14	Nov-14	Dec-14	Jan-15
All index	(2.1)	(3.4)	(3.9)	(6.4)	(5.9)	(12.2)	(12.0)
Non-fuel index	0.3	(1.9)	(3.7)	(1.5)	0.2	(2.2)	(3.2)
Food and beverage index	(1.6)	(2.8)	(4.7)	(0.8)	0.7	(0.4)	(2.7)
Food index	(1.9)	(3.4)	(5.2)	(1.2)	1.4	(0.3)	(2.9)
Beverages index	1.1	3.0	(1.0)	2.1	(5.4)	(1.9)	(1.0)
Industrial materials index	2.5	(1.0)	(2.7)	(2.1)	(0.2)	(4.1)	(3.7)
Agricultural raw material Index	(0.4)	(2.0)	(0.4)	(0.3)	(1.0)	(2.7)	(0.6)
Metal index	4.3	(0.3)	(4.0)	(2.9)	(0.3)	(4.9)	(5.7)
Energy index	(3.2)	(4.1)	(3.9)	(9.1)	(9.0)	(18.4)	(18.6)

Source: IMF

## Global: Consumer Price Index (YoY, %)

	Jun-14	Jul-14	Aug-14	Sep-14	Oct-14	Nov-14	Dec-14	Jan-15	2014	2013
Global	3.5	3.4	3.3	3.2	2.8	2.9	2.7	-	3.2	3.6
US	2.1	2.0	1.7	1.7	1.7	1.3	0.8	-	1.6	1.5
Eurozone	0.5	0.4	0.4	0.3	0.4	0.3	(0.2)	(0.6)	0.4	1.3
Japan	3.6	3.4	3.3	3.2	2.9	2.4	-	-	2.7	0.4
Germany	0.9	0.8	0.8	0.9	0.8	0.7	0.2	(0.4)	0.9	1.5
UK	1.9	1.6	1.5	1.2	1.3	1.0	0.5	0.3	1.5	2.6
OECD	2.1	2.0	1.8	1.8	1.8	1.5	1.1	-	1.7	1.6
China	2.3	2.3	2.0	1.6	1.6	1.4	1.5	0.8	2.0	2.6
India	7.5	8.0	7.7	6.5	5.5	4.4	5.0	5.1	7.2	10.1
Russia	7.8	7.5	7.6	8.0	8.3	9.1	11.4	15.0	7.8	6.8
Brazil	6.5	6.5	6.5	6.7	6.6	6.6	6.4	7.1	6.3	6.2
S. Korea	1.7	1.6	1.4	1.1	1.2	1.0	0.8	0.8	1.3	1.3
Taiwan	1.7	1.8	2.1	1.7	1.8	1.1	0.7	(0.3)	1.4	0.7
Hong Kong	3.6	4.1	4.0	6.6	5.1	5.1	4.9	-	4.4	4.3
Singapore	2.0	0.9	1.0	0.8	(0.2)	(0.2)	(0.0)	-	1.0	2.4
Indonesia	6.7	4.5	4.0	4.5	4.8	6.2	8.4	7.0	6.4	6.4
Thailand	2.4	2.2	2.1	1.8	1.5	1.3	0.6	(0.4)	1.9	2.2
Malaysia	3.3	3.2	3.3	2.6	2.8	3.0	2.7	1.0	3.2	2.1
Philippines	4.4	4.9	4.9	4.4	4.3	3.7	2.7	2.4	4.2	2.9
Vietnam	5.0	4.9	4.3	3.6	3.2	2.6	1.8	0.9	4.1	6.6

Sources: Bloomberg, CEIC, Maybank KE, IMF

## Global: Core Consumer Price Index (YoY, %)

	Jun-14	Jul-14	Aug-14	Sep-14	Oct-14	Nov-14	Dec-14	Jan-15	2014	2013
US	1.9	1.9	1.7	1.7	1.8	1.7	1.6	-	1.8	1.8
Eurozone	0.8	0.8	0.9	0.8	0.7	0.7	0.7	0.6	0.8	1.1
Japan	2.3	2.3	2.2	2.2	2.1	2.1	2.1	-	1.8	(0.2)
UK	2.0	1.8	1.9	1.5	1.5	1.2	1.3	1.4	1.6	2.1
OECD	1.9	1.9	1.9	1.8	1.8	1.7	1.7	-	1.8	1.5
China	1.7	1.6	1.5	1.3	1.2	1.0	0.8	0.6	1.5	1.6
S. Korea	2.1	2.2	2.4	1.9	1.8	1.6	1.6	2.4	2.0	1.7
Taiwan	1.5	1.6	1.7	1.5	1.6	1.4	1.4	0.6	1.3	0.7
Indonesia	13.5	6.2	5.5	6.5	7.6	11.4	17.6	12.3	13.0	9.6
Thailand	1.7	1.8	1.8	1.7	1.7	1.6	1.7	1.6	1.6	1.0
Malaysia	1.4	1.4	1.3	1.2	1.1	1.0	0.9	1.0	1.2	0.6

Sources: Bloomberg, CEIC, Maybank KE

\*Malaysia's weighted core inflation rate by our estimates has been adjusted to exclude "Alcoholic Beverages & Tobacco".

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