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Analysts tip Bank Negara to raise policy rate in second half of 2018

THE SUN 12/11

PETALING JAYA: Analysts have projected a 25 basis point (bps) increase in the Overnight Policy Rate (OPR) to 3.25% in the second half of 2018 (2H18), following signs of hawkishness at Bank Negara Malaysia's Monetary Policy Committee (MPC) meeting last Thursday.

In its final meeting of the year, the MPC said it "may consider reviewing the current degree of monetary accommodation".

"We take this as a signal that Bank Negara Malaysia (BNM) is getting ready to normalise interest rates should domestic demand growth pan out as expected," Hong Leong Investment Bank (HLIB) Research said in a report last Friday.

Despite the hawkish stance in the monetary policy statement, HLIB Research said, a rate increase is not likely in 1H18 as the threat of financial imbalances is still largely absent, with moderate loan growth of 5.2% in September and the house price index increasing 5.6% in the first quarter amid expectations of milder inflation in 2018.

"We introduce 2018 interest rate forecast that BNM will hike the OPR by 25bps in 2H18, bringing the OPR to 3.25% by end of 2018," it said.

Besides the MPC's statement on "may consider reviewing the current degree of monetary accommodation", Kenanga Research noted that the MPS conspicuously dropped any mention of core inflation remaining contained.

"This is MPC's most hawkish statement yet and may be BNM's earliest official statement communicating possible tightening down the road. However, we note that while hawkish, the MPC's language sought to keep its options open but



File picture of Fornca staf monitoring prices in a hypermarket after the implementation of the Goods & Services Tax. Core inflation is expected to be mild next year.

simply considered a review," it said in its report.

It also noted that any timetable or specific economic variables of interest were not mentioned in the MPS's statement but suspects that any further elevation of core inflation and sustained growth in 2018 will likely trigger a 25bps increase in the OPR to 3.25%.

On the flip side, it expects deterioration in 2018 manufacturing and service sector growth significantly below the Finance Ministry's 5.3% and 5.8% respective target to reduce the case for a rate hike.

"Given the house view of a 4.9% growth target for 2018 instead, we believe that the timing that MPC will likely consider its first rate hike is in 2H18 as it awaits confirmation of sustained growth trajectory at least for 1H18," it added.

Meanwhile, Affin Hwang Capital has maintained its view that BNM will likely increase the OPR by 25bps to 3.25% in 2H18, on expectations that the current strong economic momentum continues on a favourable global economic environment.

"However, we believe that any increase in the OPR in 2H18 would be at a measured pace, and the magnitude of increase would be gradual and dependent on macro growth and CPI data, following closely also the development in US monetary policy, direction of the Fed Funds rate and reduction in the Fed's balance sheet," it said in its report.

It believes the rationale for a rate increase, if it materialises, would be to prevent the economy from exceeding its potential output level, which would translate into higher inflationary pressure.

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