Economic Beat — midf RESEARCH

23 January 2014

MALAYSIA

December CPI – Upward pressure building up

CPI continued to tick up in December, rising by 3.2% YoY (Nov: 2.9%) as the combination of higher prices of administered items continued to take effect. That was slightly higher than the consensus estimate of 3.1% but matched ours. Overall, the index rose by 2.1% for the whole of 2013 (2012: 1.7%). Malaysia is among the last country in Asia to release the December CPI number. Across Asia, Malaysia is one of the few that recorded higher inflation during the month. Others include Indonesia (8.4%) and Philippines (4.1%). Singapore is scheduled to release its December CPI number today which consensus is expecting the index to slow markedly from 2.6% in Nov to 2.0% in December.

The index rose 0.3% MoM, the same pace as of the previous month, indicating that the upward pressure is building up, albeit at a gradual pace. The fact that the index continued to tick up MoM and by historical trend, the cumulative MoM changes in the last few months following the rise in fuel prices is rather siginificant given that fuel prices only rose by 20sen across showed that pressure is building up. The anticipation of higher electricity tariffs this year could have also led businesses to pre-emptively raising the prices of their goods and services.

Much higher food prices could be a sign that second round effects have started to gain momentum, although we still believe on wider note, the pressure would stay contained. The sub-index for Food and Non-Alcoholic Beverages rose by 4.5% YoY and 0.9%MoM during the month (Nov: 3.9%) The other two big components, namely Housing, Water, Electricity, Gas & Other Fuels and Transport rose by 2.4% (Nov: 2.3%) and 5.0% (Nov: 4.9%), respectively. Other sub-indices showed rather flattish or small changes during the month.

Businesses may have foreseen structurally, the economy will face much higher prices of inputs going forward amidst sustained strong domestic demand The temporary cost-push factor should see the effects diminishing on YoY basis after 1 year, as the increases in prices of other items stay muted or marginal, as business may not have the opportunity to pass on higher cost to consumers or willing to absorb the rising cost that is perceived as temporary. Nonetheless, with the index continuing to rise by 0.3%MoM (cumulative: 1.7% since September. 2013) with some components showing significant rise, we should not rule out that second round effects have started to kick in sooner than expected. The anticipation of compounding effects of multiple price hikes could see inflationary pressure to persist well into 2015 when the Goods and Servives Tax would be rolled out. With consumer spending likely to pull back but staying strong, businesses see the opportunity to pass on the higher cost to consumers.

Going forward, the nation should expect a structural change in factors detrmining inflation, with supply shocks and external factors to have greater impact. Before the abolishment of sugar as a subsidised item, administered items constituted about 29.3% of the CPI basket. While some major items would remain to be subsidised, the amount of subsidy would be lowered further in line with the government's move to make the economy more market-driven and trim its expenditure. There is a possibility that some items may not be subsidised anymore in the next few years.

For 2014, CPI may rise by 3.0 – 3.5% assuming that only the direct impact of the electricity tariff hikes to be reflected in the CPI and the direct effects of higher fuel and tobacco prices to dissipate by 4Q 14. Nonetheless, we expect the second round effects of electricty tariff hikes would be more widespread, compounding the second round effects coming from the fuel and tobacco price hikes. If we add on the toll rate hikes and another fuel price hike next year, that would see CPI to rise faster, by 3.5 to 4.0% in 2014.

Maintain call for 25 - 50bps hike by BNM We continue to factor in the possibility of Bank Negara raising the Overnight Policy Rate (OPR) by 25bps in 2Q 14 to restore the positive real interest rate as well as keeping inflation expectations in check. The central bank may hike up again in 2H 2014 if there is a firm sign of much wider spillover effects on prices of goods and services and growth likley to be at the top range of the official forecast (5.5 – 6.0%)

Chart 1: Consumer Price Index – Major components

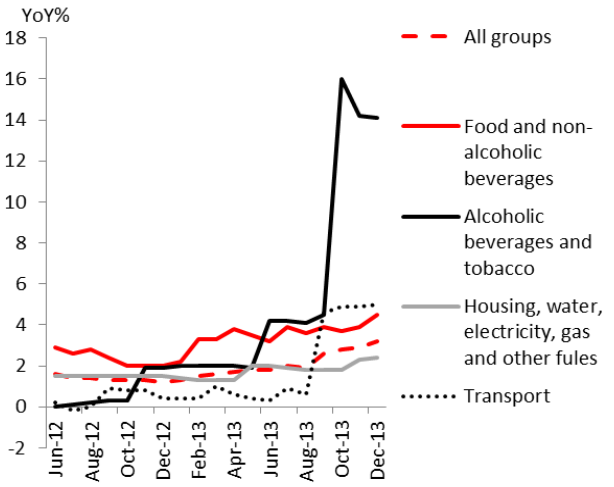
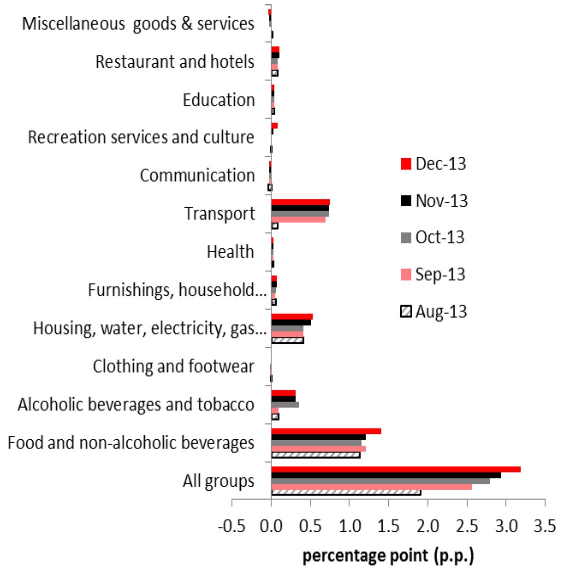


Chart 2: Contribution to the change in main index



Source: DoS

Chart 3: Real interest rate slipping into negative Territory

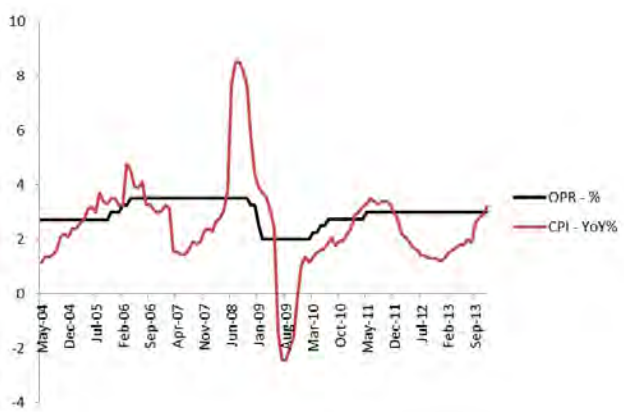
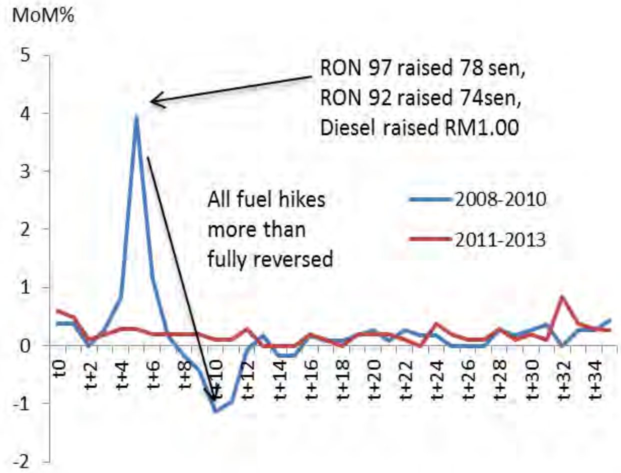
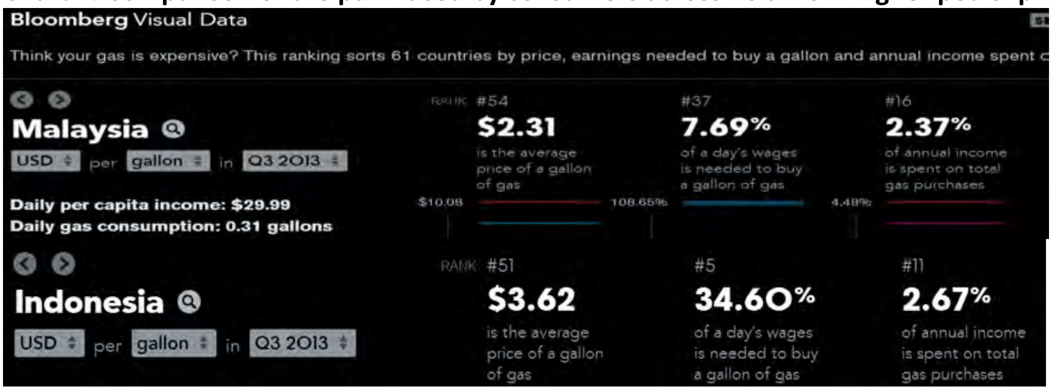


Chart 4: The MoM chnages in CPI following chnages in prices of administered goods



Source: BNM

Chart 4: Comparison of the pain faced by consumers across Asia from higher petrol prices



Source: Bloomberg

MIDF RESEARCH is part of MIDF Amanah Investment Bank Berhad (23878 - X).
(Bank Pelaburan)
(A Participating Organisation of Bursa Malaysia Securities Berhad)

DISCLOSURES AND DISCLAIMER

This report has been prepared by MIDF AMANAH INVESTMENT BANK BERHAD (23878-X). It is for distribution only under such circumstances as may be permitted by applicable law.

Readers should be fully aware that this report is for information purposes only. The opinions contained in this report are based on information obtained or derived from sources that we believe are reliable. MIDF AMANAH INVESTMENT BANK BERHAD makes no representation or warranty, expressed or implied, as to the accuracy, completeness or reliability of the information contained therein and it should not be relied upon as such.

This report is not, and should not be construed as, an offer to buy or sell any securities or other financial instruments. The analysis contained herein is based on numerous assumptions. Different assumptions could result in materially different results. All opinions and estimates are subject to change without notice. The research analysts will initiate, update and cease coverage solely at the discretion of MIDF AMANAH INVESTMENT BANK BERHAD.

The directors, employees and representatives of MIDF AMANAH INVESTMENT BANK BERHAD may have interest in any of the securities mentioned and may benefit from the information herein. Members of the MIDF Group and their affiliates may provide services to any company and affiliates of such companies whose securities are mentioned herein This document may not be reproduced, distributed or published in any form or for any purpose.

MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS

STOCK RECOMMENDATIONS	
BUY	Total return is expected to be >15% over the next 12 months.
TRADING BUY	Stock price is expected to *rise* by >15% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -15% and +15% over the next 12 months.
SELL	*Negative* total return is expected to be -15% over the next 12 months.
TRADING SELL	Stock price is expected to *fall* by >15% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.
SECTOR RECOMMENDATIONS	
POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.