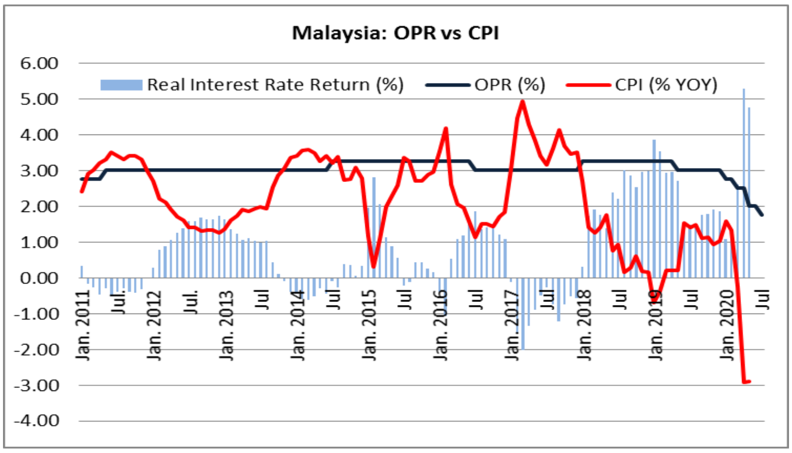
BNM delivered its fourth consecutive cut to accelerate recovery

BNM cut the OPR for the fourth straight meeting, its first such serial move in history, to provide additional policy stimulus to accelerate the pace of economic recovery. This sounds like a hawkish cut to us to safeguard the recovery traction given prevailing growth uncertainties. Even though there are recent green shoots to suggest we have sailed pass the trough in 2Q, sustainability of such uptick remains highly questionable. Following today's 25bps cut, and a cumulative 125bps reduction in the current easing cycle, OPR is settling at a fresh record low at 1.75% vs 2.00% back in 2009. Taking cue from today's dovish statement, the risk of another 25bps cut for the remaining of the year remain. We would however caution that over-easing could limit policy flexibility in the unfortunate event of further shocks and deterioration in macro outlook.

BNM cut the OPR by another 25ps to 1.75%, a fresh record low to accelerate the pace of economic recovery

BNM cut the Overnight Policy Rate (OPR) by another 25bps to 1.75% today, a fresh record low, acknowledging downside risks in both the global and domestic economy. Even though this was against our house view for a pause, the 25bps cut does not come as a complete surprise given the fluid growth backdrop. **BNM has reduced the OPR by a cumulative 125bps in the current easing cycle, 25bps shy of the 150bps cut seen during the global financial crisis back in 2008/09,** although today's cut bring about a fresh record low (2.00% in 2009). We believe there is still policy room should BNM decide to pull the trigger. **We therefore see the risk of another 25bps cut this year.**

While odds of further cut remains, we caution against risks of over-easing that could limit policy flexibility in the unfortunate event of further shocks and deterioration in the macro outlook. **Meanwhile, it is worth noting that BNM mentioned that today's cut is to "provide additional policy stimulus to <u>accelerate</u> the pace of economic recovery", instead of the usual stance "to support growth", sounding like a hawkish cut to us.**



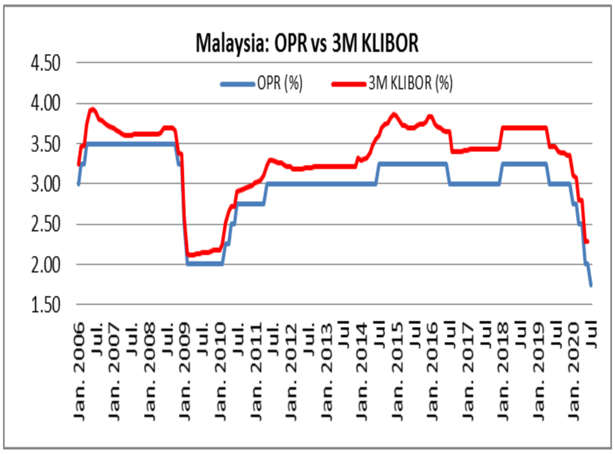
Global economic conditions remain weak; downside risks prevail

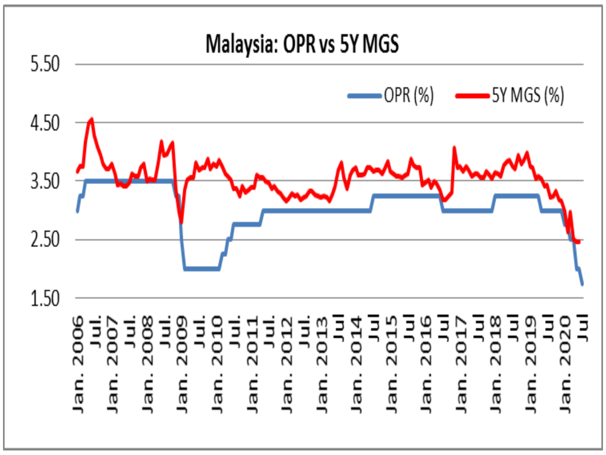
Assessment on both the global as well as Malaysian economy is dovish. BNM highlighted that global economic conditions remain weak, and reaffirmed that global growth will contract this year. Recently, IMF has further downgraded this year's global growth projection from -3.0% to -4.9%, taking cue from greater uncertainties and weaker than expected growth prospects. **While recent indicators all suggest economic conditions are bouncing back from the trough in 2Q, it is arguable if such recovery momentum could be sustained.** Specifically, BNM cited broad-based weakness in the labour markets and cautiousness among consumers and businesses could impede recovery going forward. **In addition, downside risks to the global outlook remain, especially if escalating second or even third wave of infections prompt the re-imposition of containment measures that could derail the recovery.**

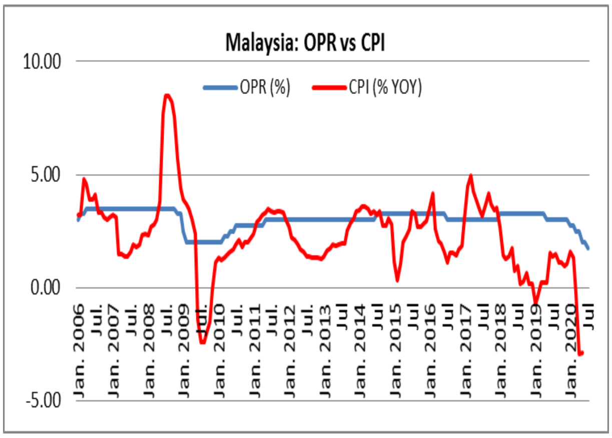
Uncertainties around the pace and strength of recovery in the domestic economy

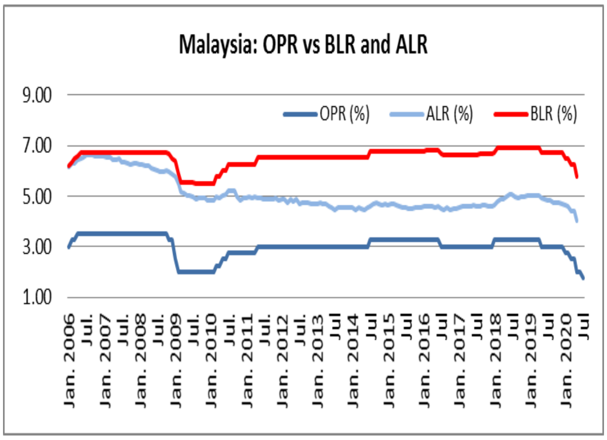
Domestic prospects remain equally challenging, closely tracking the global economic fallout. **BNM highlighted that economic activity contracted sharply in 2Q,** for obvious reason of the containment measures introduced globally and domestically. **This appears in sync with our expectation for a 12.3% YOY contraction in economic activities in 2Q.** While gradual reopening of the economy as well as policy support from both the fiscal and monetary front, **there remains downside risks to the pace and strength of the recovery.** We also believe this probably explains today's 25bps cut, to at least safeguard the recovery momentum given that the pandemic is still evolving globally although the situation appears under control in Malaysia for now.

MPC Meeting No.	Dates of Monetary Policy Committee Meetings for 2020
1st	21 and 22 January 2020 (Tuesday and Wednesday)
2nd	2 and 3 March 2020 (Monday and Tuesday)
3rd	4 and 5 May 2020 (Monday and Tuesday)
4th	6 and 7 July 2020 (Monday and Tuesday)
5th	9 and 10 September 2020 (Wednesday and Thursday)
6th	2 and 3 November 2020 (Monday and Tuesday)


Malaysia: OPR vs 3M KLIBOR
OPR (%)
3M KLIBOR (%)
4.50
4.00
3.50
3.00
2.50
2.00
1.50
Jan. 2006 Jul. Jan. 2007 Jul. Jan. 2008 Jul. Jan. 2009 Jul. Jan. 2010 Jul. Jan. 2011 Jul. Jan. 2012 Jul. Jan. 2013 Jul Jan. 2014 Jul Jan. 2015 Jul Jan. 2016 Jul Jan. 2017 Jul Jan. 2018 Jul Jan. 2019 Jul Jan. 2020 Jul


Malaysia: OPR vs 5Y MGS
OPR (%)
5Y MGS (%)
5.50
4.50
3.50
2.50
1.50
Jan. 2006 Jul. Jan. 2007 Jul. Jan. 2008 Jul. Jan. 2009 Jul. Jan. 2010 Jul. Jan. 2011 Jul. Jan. 2012 Jul. Jan. 2013 Jul Jan. 2014 Jul Jan. 2015 Jul Jan. 2016 Jul Jan. 2017 Jul Jan. 2018 Jul Jan. 2019 Jul Jan. 2020 Jul


Malaysia: OPR vs CPI
OPR (%)
CPI (% YOY)
10.00
5.00
0.00
-5.00
Jan. 2006 Jul. Jan. 2007 Jul. Jan. 2008 Jul. Jan. 2009 Jul. Jan. 2010 Jul. Jan. 2011 Jul. Jan. 2012 Jul. Jan. 2013 Jul Jan. 2014 Jul Jan. 2015 Jul Jan. 2016 Jul Jan. 2017 Jul Jan. 2018 Jul Jan. 2019 Jul Jan. 2020 Jul


Malaysia: OPR vs BLR and ALR
OPR (%)
ALR (%)
BLR (%)
9.00
7.00
5.00
3.00
1.00
Jan. 2006 Jul. Jan. 2007 Jul. Jan. 2008 Jul. Jan. 2009 Jul. Jan. 2010 Jul. Jan. 2011 Jul. Jan. 2012 Jul. Jan. 2013 Jul Jan. 2014 Jul Jan. 2015 Jul Jan. 2016 Jul Jan. 2017 Jul Jan. 2018 Jul Jan. 2019 Jul Jan. 2020 Jul

Side by Side Comparison of BNM Monetary Policy Statement

5-May-2020	7-July-2020
At its meeting today, the Monetary Policy Committee (MPC) of Bank Negara Malaysia decided to reduce the Overnight Policy Rate (OPR) by 50 basis points to 2.00 percent. The ceiling and floor rates of the corridor of the OPR are correspondingly reduced to 2.25 percent and 1.75 percent, respectively. Global economic conditions have weakened significantly. Measures to contain the COVID-19 pandemic have disrupted economic activity across most economies. Recent indicators show that the global economy is already contracting, with global growth projected to be negative for the year. Financial conditions have also tightened amid elevated risk aversion and uncertainty. Substantial policy stimuli introduced by many economies, coupled with the gradual easing of containment measures globally, would partially mitigate the economic impact of COVID-19. Growth prospects should improve in 2021 with the expected containment of the pandemic. For Malaysia, domestic economic conditions have similarly been affected by the pandemic. Widespread containment measures globally, international border closures and the consequent weak external demand environment will exert a larger drag on domestic economic activity. The Movement Control Order, while necessary to contain the spread of the virus, has also constrained production capacity and spending. Labour market conditions are also expected to weaken considerably. Economic conditions would be particularly challenging in the first half of the year. The fiscal stimulus measures, alongside monetary and financial measures will, however, offer some support to the economy. With more businesses allowed to operate under the Conditional Movement Control Order, economic activity is projected to gradually improve. The outlook for growth continues to be subject to a high degree of uncertainty, particularly with respect to developments surrounding the pandemic. Inflationary pressures are expected to be muted in 2020, with average headline inflation likely to be negative this year, due mainly to projections for substantially lower global oil prices. Nevertheless, the outlook remains significantly affected by global oil and commodity prices, as well as evolving demand conditions. Underlying inflation is expected to be subdued given the projections of weaker domestic growth prospects and labour market conditions. The financial sector is sound, with financial institutions operating with strong capital and liquidity buffers. Liquidity remains ample, augmented by liquidity injections by Bank Negara Malaysia. Since March 2020, Bank Negara Malaysia has provided additional liquidity of approximately RM42 billion into the domestic financial markets, via various tools including outright purchase of government securities, reverse repos and the reduction in Statutory Reserve Requirement. Bank Negara Malaysia stands ready to provide liquidity in the interbank market to ensure orderly market conditions, conducive to support financial intermediation activity. With the decision today, the OPR has been reduced by a total of 100 basis points, complementing other monetary and financial measures by Bank Negara Malaysia as well as fiscal measures this year. Together, these measures will cushion the economic impact on businesses and households and support the improvement in economic activity. The MPC will continue to monitor the outlook for domestic growth and inflation. The Bank will utilise its policy levers as appropriate to create enabling conditions for a sustainable economic recovery.	At its meeting today, the Monetary Policy Committee (MPC) of Bank Negara Malaysia decided to reduce the Overnight Policy Rate (OPR) by 25 basis points to 1.75 percent. The ceiling and floor rates of the corridor of the OPR are correspondingly reduced to 2.00 percent and 1.50 percent, respectively. The impact of COVID-19 on the global economy is severe. Global economic conditions remain weak with global growth projected to be negative for the year. Although a trough is expected in the second quarter, broad-based weakness in labour markets and precautionary behaviour by households and businesses could affect the recovery going forward. Several major economies have begun relaxing measures to contain the COVID-19 pandemic, leading to the gradual resumption of economic activity. Financial conditions have improved, although risk aversion remains elevated. Downside risks to the global outlook remain, especially if a resurgence of the pandemic necessitates the reintroduction of containment measures. For Malaysia, economic activity contracted sharply in the second quarter of the year, due to measures introduced to contain the pandemic globally and domestically. Following the gradual and progressive re-opening of the economy since early May, economic activities have begun to recover from the trough in the second quarter. The fiscal stimulus packages, alongside monetary and financial measures, will continue to underpin the improving economic outlook. The projected improvement in the domestic economy is expected to be further supported by a gradual recovery in global growth conditions. The pace and strength of the recovery, however, remain subject to downside risks emanating from both domestic and external factors. These include the prospect of further outbreaks of the pandemic leading to re-impositions of containment measures, more persistent weakness in labour market conditions, and a weaker-than-expected recovery in global growth. Inflationary pressures are expected to be muted in 2020. Average headline inflation is likely to be negative this year, primarily reflecting the substantially lower global oil prices. The risks of a broad-based and persistent decline in prices are assessed to be limited as economic activity resumes and demand conditions improve. Nevertheless, the outlook remains significantly affected by global oil and commodity prices. Underlying inflation is expected to be subdued and within expectations. The reduction in the OPR provides additional policy stimulus to accelerate the pace of economic recovery. The MPC will continue to assess evolving conditions and their implications on the overall outlook for inflation and domestic growth. The Bank will continue to utilise its policy levers as appropriate to create enabling conditions for a sustainable economic recovery.

Hong Leong Bank Berhad
Fixed Income & Economic Research, Global Markets
Level 8, Hong Leong Tower
6, Jalan Damanlela
Bukit Damansara
50490 Kuala Lumpur
Tel: 603-2081 1221
Fax: 603-2081 8936
Email: HLMarkets@hlbb.hongleong.com.my