BNM not likely to adjust OPR in the near term, says MARC

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by PREMALATHA JAYARAMAN

Pic by Muhd Amin Nahsrul

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MALAYSIAN Rating Corp Bhd (MARC) does not anticipate Bank Negara Malaysia (BNM) to adjust the Overnight Policy Rate (OPR) in the near term as it could have ramifications on headline growth, capital outflows and the ringgit.

The rating agency is of the view that the monetary policy space would remain rather limited, despite the fact that Malaysia's OPR has been reduced only once since July 2016.

At the current level of 3%, MARC said real interest rates are approaching 0%, or even negative, as inflation is set to pick up in 2017.

Meanwhile, Malaysia's bond yields, which reacted to the spike in US Treasury yields post-Donald Trump's victory in November 2016, have since stabilised at lower levels.

MARC also foresees the 10-year Malaysian Government Securities (MGS) yields to remain in the range of between 4% and 4.5% as the market continues to digest rate hike expectations in the US, as well as assessing Malaysia's overall economic performance in the face of further external risks and domestic challenges.

In a report, MARC stated that issues relating to capital flows would continue to hog the limelight in the near term in view of uncertain global developments in 2017.

Overall, the outflows of short-term capital from Malaysia's bond market (less than three years) are not expected to have any material impact on the country's fundamentals.

However, MARC said with the financial market still guessing the amount of short-term debt securities still held by foreigners after the recent outflows between September 2016 and February 2017, the anxiety in the financial market could persist in the near term.

In the longer term, however, MARC said a reduction in foreign holdings of short-term securities would be a welcome development.

"Many studies have highlighted the negative repercussions of short-term capital flows in several economies such as Chile, Brazil and even Malaysia in the 1990s," it said.

As such, MARC welcomed the new financial landscape of lower foreign holdings of Malaysian short-term debt securities going forward.

With capital flows expected to remain volatile in 2017, it said the ringgit's movements would likely continue to be unpredictable in the near term.

"On a brighter side, the ringgit's volatility against the US dollar has so far been reduced by BNM's reminder on the prohibition of offshore foreign exchange transactions in the ringgit non-deliverable forward market in November 2016," it said.

The downside risk for the ringgit could arise from a correction in global crude oil prices and bond markets, as well as an overreaction to interest rate hike by the US Federal Reserve, it said.

MARC forecast the ringgit to remain within a narrow band around the present level of between RM4.40 and RM4.50 per US dollar.

Going beyond global political and economic uncertainties, MARC anticipated a stronger ringgit of RM4.20 against the greenback.

The rating agency said BNM's 2016 Annual Report was more upbeat on prospects for the global economy in 2017, despite citing reservations over some global developments such as the possibility of trade protectionism and geopolitical risks in some countries.

MARC said major global economic indicators such as the Global Purchasing Managers' Index, which has continued to ascend and lower inflation, are flashing more positive signals of further strengthening of the US and China.

"BNM's forecast of a stronger gross domestic product (GDP) growth of between 4.3% and 4.8% for Malaysia is in line with our projection of 4.3%. We share the central bank's view of better prospects for the external sector in 2017, although we think it is too early to make a conclusive assessment on its impact on headline growth," it said.

Continuing support from domestic demand will help the nation achieve another decent year of real GDP growth. This is despite a negative growth trend in private consumption following consumers' cautious sentiments reflected in the consumer sentiment statistics, MARC added.

"We anticipate private consumption growth to remain at 5.8% in 2017, slightly lower than BNM's forecast of a 6% expansion. As for private investment, BNM's projection of 4.1% growth for 2017 is lower than MARC's 5.6% expansion forecast," it added.