

Malaysia Business Forecast Report Q3 2014

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Abstracts

Core Views

Malaysia's once-bloated current account surplus is coming under pressure from a combination of income account outflows and a dwindling trade surplus. We expect the narrowing of the surplus to continue, forecasting it to come in at 2.5% of GDP in 2014 and 1.6% in 2015. However, the risks are weighted to the downside, with the emergence of a current account deficit over the next few years increasingly likely.

Over recent years Malaysia's fiscal accounts have exhibited some worrying trends, with spending rising as a share of GDP, subsidy spending rising as a share of total spending, and indirect tax revenues declining. Going forward, we are optimistic that these trends will be halted as subsidy spending is reduced and a Goods & Services Tax is implemented, which should help stabilise Malaysia's debt metrics and support private sector real GDP growth.

Bank Negara Malaysia will find itself under increasing pressure to hike interest rates over the coming months as consumer price inflation (CPI) pressures mount following the reduction of fuel and electricity subsidies. However, we expect the central bank to maintain the policy rate at 3.00% amid growing disinflationary signs emanating from weakening money supply growth, which should see CPI pressures ease in H214.

Major Forecast Changes

We have revised down Malaysia's current account surplus for 2014 and 2015, forecasting it to come in at 2.5% of GDP in 2014 and 1.6% in 2015, rather than the 3.5% and 2.7% previously expected. Even with these revisions, the risks are weighted to the downside as the pickup in domestic investment activity and the still-wide consolidated public deficit pose risks of a current account deficit over the coming years.

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Over recent years Malaysia's fiscal accounts have exhibited some worrying trends, with

spending rising as a share of GDP, subsidy spending rising as a share of total spending, and indirect tax revenues declining. We are optimistic that these trends will be halted as subsidy spending is reduced and a Goods & Services Tax is implemented, which should help stabilise Malaysia's debt metrics and support private sector real GDP growth.

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We believe that fiscal policy-driven spikes in headline consumer price inflation (CPI) will be transitory in nature, and not a reflection of underlying price pressures in the economy. As such, we reiterate our forecast that Bank Negara Malaysia will keep its policy rate on hold at 3.00% throughout 2014. The risk of second round inflationary pressures, however, could add further upward pressure on prices. Should we see evidence that businesses are passing on higher production costs to consumers, we would revise our CPI forecasts accordingly.

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Malaysia's once-bloated current account surplus is coming under pressure from a combination of income account outflows and a dwindling trade surplus. We expect the narrowing of the surplus to continue, forecasting it to come in at 2.5% of GDP in 2014 and 1.6% in 2015. However, the risks are weighted to the downside, with the emergence of a current account deficit over the next few years increasingly likely.

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