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MEDIA STATEMENT
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Kuala Lumpur, 25 January 2019 - 2018 marked another challenging year for the global economy and businesses amid global monetary normalisation and brewing US-China trade tensions. Financial market sentiments were rather fragile, as illustrated by the roller-coastal ride for risk assets, whether equities, bonds or commodities. The IMF had shaved its global growth forecast by 0.2% points to 3.7% yoy, citing downside growth risks from heightened concerns of protectionism as the US and China engaged in a tit-for-tat retaliatory trade war. Concurrently, monetary policy normalisation was in full swing among the major central banks - the US Federal Reserve (Fed) hiked its Fed Funds rate every quarter by 25 basis points while winding down its expanded balance sheet, and the European Central Bank (ECB) also halted its monthly asset purchase programme in December 2018. Asian central banks also began raising interest rates, with Bank Indonesia (BI) and Bangko Sentral ng Pilipinas (BSP) tightening

by a cumulative 175 basis points amid narrowing interest rate differential concerns. This came as the US's economic growth outperformed the rest of the world, whilst Asian economies experienced slower growth that was exacerbated by China's growth deceleration. Towards the end of 2018, de-risking activities contributed to a sharp correction in the global equity markets, VIX (volatility index for the S&P500) spiked to 36 on 24 December 2018 (just shy of its 2018 high of 37 seen on 5 February 2018) and the 10-year US Treasury bond yield declined rapidly from 3.24% in November 2018 to a low of 2.55% on 3 January 2019.

Going into 2019, the external headwinds remain familiar, but there are two important inflection points. The Fed has turned less hawkish and is signalling patience and prudence for its 2019 rate hike intentions amid worries of slowing US growth. Indeed, while an impending US recession is not in our baseline scenario, nevertheless after several quarters of above-trend growth, economic momentum is likely to decelerate as the fiscal stimulus from the tax cuts wears off and the US-China trade tensions take a toll on the real economy. In addition, the potential US policy gridlock, following the mid-term elections which contributed to a divided Congress, has resulted in an extended US government shutdown which may further weigh on the US growth in the short-term. Moreover, with the softer crude oil price environment, the impetus for further monetary policy tightening may also be put on temporary pause mode. Separately, Brexit negotiations and Italy's fiscal issues also remain bugbears for the Eurozone.

Over in China, the economic indicators continue to point to a growth slowdown and the holistic policy stance has clearly shifted to mitigate the downside growth risks, whether through monetary or fiscal policy support. The latter is apparent in various measures such as relaxing the universal reserve ratio, injecting liquidity into the banking system, expediting government bond sales, cutting taxes and selectively relaxing property curbs, amongst others. The fiscal deficit could also widen as the government looks to utilise the fiscal channel to support the economy.

With the above in consideration, greater monetary policy caution (likely initiated by the frontrunner Fed pausing in its rate hike cycle) may give more breathing space for the world economy. As investors turn their attention from yield differentials to the eroding US growth outperformance and turning point for the Fed, this may also imply less pressure on emerging market (EM) economies in the form of fund outflows and in turn pressure on their respective currencies and financial markets.

For 2019, the IMF is expecting deceleration as it revised its growth forecast downwards to 3.5% from 3.7%. The fund had cited that slowdowns in several advanced economies may be more rapid than initially expected. Here in ASEAN, the economies of the region are also not shielded from the global slowdown, given that many of their manufacturing Purchasing Managers Indices have turned south. Moreover, there are some idiosyncratic event risks to consider such as elections. Indonesia and Thailand head to the polls to elect new leaders whilst the Philippines also faces mid-term elections. Typically, businesses, consumers and investors may adopt a cautious, wait-and-see attitude in case of any election surprises. On the positive side, members of the 11-nation Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) have confirmed their strong determination to expand the agreement through the accession of new economies.

For Malaysia, key highlights in 2018 were the government change and key reforms. GDP growth likely slowed to around 4.5% in 2018, given the LNG supply disruption and the slowdown in global manufacturing and trade activities. Nevertheless, private consumption was the main contributor to growth, with a strong boost from the three months tax holiday following the abolishment of the Goods and Services Tax (GST). 2019 may see a very marginal slowdown to 4.4% yoy as global trade activity remains uncertain at this juncture, pending the outcome of the 90-day truce for the US-China trade talks. A weaker global trade environment may negatively affect the external sector. Private consumption is again expected to remain the main anchor of growth, supported by government social transfers, stable labour market conditions and moderate inflation. Ongoing fiscal consolidation would likely focus on reducing wasteful expenditure and improving spending efficiency.

On the fiscal side, the official forecast is for the budget deficit to hit 3.7% of GDP in 2018, before easing to 3.4% in 2019, 3.0% in 2020 and 2.8% in 2021. In the medium term, the government is expecting the deficit to be in the region of around 2.0% of GDP. The government had also undertaken a zero-based budgeting approach in formulating the 2019 budget in order to improve spending efficiency. Other fiscal reforms include tabling a fiscal responsibility act and a government procurement act, and transitioning to accrual based accounting from cash-based accounting. These reforms are expected to be implemented over the next three years out to 2021. The risks related to the fiscal outlook lie either with growth and hence tax revenue slowing more than expected and/or oil prices materialising at a lower level than forecast.

We expect Bank Negara Malaysia (BNM) will stay pat at 3.25% this year for the above reasons. Inflation may accelerate to 2.0% yoy in 2019 (January-November 2018: 1.0%), but with an expected negative output gap, there is no urgency to recalibrate monetary policy settings. A pause by the Fed implies no urgency for BNM to hike, and a rate cut would require the Malaysian Ringgit (MYR) to tread a firmer path against the USD. As such, government bond yields had been relatively stable throughout 2018 and are likely to sustain in 2019.

The MYR should stabilise and strengthen against the USD by end-2019. This is predicated on the expectation that the USD may be eroded by fading US growth outperformance and a more cautious Fed. However, this has to be weighed against the softer oil prices.

In summary, 2019 is not expected to be a walk in the park as global and regional growth prospects are expected to further slow down. Key external risks remain the US–China trade war and uncertainties pertaining to the speed of China's growth slowdown. Policy intentions have turned more accommodative in many countries, so the question is whether this would suffice to ward off a sharper slowdown in major economies like China. That said, the fairly benign and stable global/regional growth forecasts may not translate into financial market stability as investor confidence remains shaky. However, with the possibility of a pause or a slower pace of rate hikes for the Fed, there could be significant respite for EM including Asian economies.

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