

EQUITY

Global Equities

The risk-on rally in the first half of August unwound as warnings from senior Federal Reserve (Fed) officials attempting to push back against the markets' benign expectations on inflation and rates sank in. Market movements: US (-4.1%), Hong Kong (-1.0%), Shanghai (-1.6%), Japan (+1.0%), Korea (+0.8%), Taiwan (+0.6%), Eurozone (-5.1%), Singapore (+0.3%), Thailand (+4.0%), Indonesia (+3.3%), and Malaysia (+1.3%).

US

The decidedly hawkish speech by Chairman Powell at Jackson Hole signalled the resolve of the Fed to keep financial conditions tight and that more easing in labour market demand is necessary before the current interest rate cycle will bottom. Powell warned interest rates would need to stay high next year to keep curbing inflation rather than being cut quickly again and risk renewed increases in consumer prices, highlighting that failure to restore price stability would lead to far greater pain in the future. This is especially as consumer demand has remained robust even in the face of certain price increases implemented over 2Q22. On the corporate side, firms have notably begun to consider recessionary scenarios ahead more actively, while continuing to prioritize margins and exercise pricing power.

Europe

Outside of the US, the economic cycle in Europe is showing signs of slowdown. Policymakers continue to struggle with tackling decades-high inflation while faced with ongoing threats to economic growth and inflation, in the form of new disruptions to Russian energy supply especially through the key Nord Stream 1 pipeline, which have resulted in Europe gas prices fluctuating wildly. These disruptions, on top of hurting sentiment, will also pressure the European Central Bank (ECB) to tighten policy more aggressively.

China

Risks to global growth have also increased slightly over the past month due to the continued weakness emanating from China, as fresh lockdowns to achieve zero-Covid cases have set back the economy's reopening. The latest Caixin manufacturing PMI reading of 49.5 showed that China's manufacturing activity shrank in August after two months of expansion in June and July, highlighting the ongoing challenges from the country's battle to limit the spread of Covid-19 as well as power supply disruptions due to extreme heat. Chinese policymakers are continuing to gradually ease monetary and fiscal policy, with the latest measure being the further cuts to the 1-year and 5-year Loan Prime Rates.

Asia

The FBMKLCI rose by 1.3% over the previous month, as energy outperformed on the back of strengthening crude oil prices while healthcare remained the biggest laggard on the back of the glove names facing continued margin compression. Foreign equities recorded RM2.0 billion net inflow during the month, representing a sizeable chunk of the net inflow of RM6.3 billion year-to-date. Market sentiment was boosted by the strong 2Q 2022 GDP growth of 8.9% over the year, as domestic demand strengthened, and positive 2Q earnings season, with corporate earnings broadly in line with expectations. The relatively positive tone of corporate results mainly came from sectors exposed to discretionary spending. Going forward, however, we expect the recovery momentum to weaken due to the growing inflationary pressure as well as the diminishing impact from all the stimulus measures i.e. the special EPF cash withdrawal, that were rolled out earlier in 1H 2022. Speculation around the timing of the general election has also flared, following the announcement that Budget 2023 will be tabled three weeks earlier on 7th October.

General View

The higher rates and weaker growth outlook form a challenging backdrop for risk assets. The ride ahead will continue to be bumpy as policymakers try to bring inflation down through a mix of rate hikes and quantitative tightening, even at the expense of greater pain for businesses and households. We maintain our Neutral stance on local equities as limited earnings visibility continues to plague investors. Unveiling of Budget 2023 will be a key event to monitor closely, with handouts, incentives and other pump-priming initiatives, while positive for sentiment, being constrained by the lack of fiscal headroom. We will continue employing a tactical lookout for names with strong longer-term recovery prospects and attractive valuations, while trimming or exiting exposures that may be affected by the impending economy slowdown.

FIXED INCOME

US Treasuries

US Treasury yields rose, led by shorter maturities, as US Federal Reserve (Fed) rhetoric continued to lean hawkish. Chairman Powell, in his speech at the Fed's Jackson Hole conference, emphasized his commitment to fighting inflation, setting the stage for another outsized rate hike at the upcoming September meeting, pushing back against market expectations for rate cuts in early 2023. Fed funds futures are now pricing-in a 50% chance of a 75 basis points (bps) rate hike in September 2022. Economic data published in August were positive with surprisingly strong non-farm payrolls print of 528,000 jobs created in July while inflation seems to have passed its peak as CPI increased 8.5% year on year in July, down from 9.1% in June. The yield curve shifted higher in view of the Fed's hawkish rhetoric with the 2-year and 10-year yields accordingly rose 62bps to 3.49% and 3.19% respectively, resulting in another month of curve inversion of -30bps.

Malaysian Bond Market

On the domestic front, the MGS yield curve mirrored a bull steepening trend as the shorter end of the curve enjoyed strong buying support from foreign investors while onshore accounts remained cautious with light selling interest into strength. Yields were initially higher on the back of higher US rates but despite the spike in US yields, Ringgit rates had proven resilience by moving only a tad weaker in comparison to US Treasuries. The Fed's leadership of a hawkish global policy wave sent the greenback higher, and the Ringgit weakened consequently. Despite weakness on the currency front, economic releases have been very resilient with the economy growing at its fastest annual pace in a year in the second quarter. The second quarter GDP surged 8.90% from a year earlier boosted by expansion in domestic demand and resilient exports. Meanwhile, the Consumer Price Index for July accelerated by 4.4% year-on-year, its highest in 14 months due to higher food and beverage prices. Despite the uptick in inflation, Bank Negara Malaysia is expected to remain gradual and accommodative in its current rate hiking cycle. Government auctions continued to chart encouraging demand with BTC ranging from 2.04x-2.74x for the 3 auctions conducted namely the 5-year MGS re-opening followed by the 20-year GII and 15-year MGS re-opening. Over the month, the 3-year MGS declined 19bps to 3.30% while the 10-year rose 10bps to 3.98%.

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