

EQUITY

Global Equities

The rally staged by risk assets towards the end of July reflected hopes by some investors that the end of the rate hiking cycle could be in sight. Persistent inflation and tighter financial conditions are starting to bite in developed markets, as evident in the latest US GDP numbers for 2Q 2022 that showed that the US economy entered a technical recession. Market movements: US (+4.6%), Hong Kong (-7.8%), Shanghai (-4.3%), Japan (+5.0%), Korea (+5.1%), Taiwan (1.2%), Eurozone (+4.4%), Singapore (+3.5%), Thailand (+0.5%), Indonesia (-0.2%), and Malaysia (+3.3%).

US

Towards the end of July, the US Federal Reserve (Fed) raised its Fed funds rate by 75 basis points (bps) for a second straight month, taking its target to 2.25-2.50%. This came at a time when the US economy unexpectedly contracted for a second quarter in a row in 2Q 2022, meeting the criteria for a 'technical' recession, though the economy is not yet experiencing a broad-based, sustained contraction in activity. The US earnings season is also well underway, with corporate results somewhat mixed though beating earnings per share (EPS) estimates on average. However, firms are undoubtedly facing macro headwinds, which is translating into concerns such as potential capital expenditure cuts and elongated sales cycles.

Europe

In Europe, early 2Q 2022 results point to a beat relative to expectations on sales but a miss on EPS, exemplifying the growing cost pressures and trickier margin backdrop corporates are facing. New disruptions to Russian energy supply are weighing heavily on sentiment after Russia's Gazprom said that gas flows to Germany through the key Nord Stream 1 pipeline would fall by half of the already-reduced flows from 27th July on claims that Western sanctions had caused difficulties in maintenance of the infrastructure. This threat of gas disruption is certainly fuelling inflation that is pressuring the European Central Bank to tighten policy more aggressively.

China

China's economy is starting a gradual, though bumpy and still fragile, recovery. Latest reading of the Caixin manufacturing purchasing managers' index (PMI) of 50.4 showed that China's manufacturing activity expanded for a second straight month in July 2022, though declining from 51.7. However, the official manufacturing PMI published by the National Bureau of Statistics fell to contractionary territory at 49.0 in July from 50.2 in June. A higher pace of recovery is seen in non-manufacturing activity, mainly services, which continued to expand in July 2022 with a PMI reading of 53.8, from 54.7 in June 2022. The July Politburo meeting concluded with a call for incremental easing and this should be indicative of an easing policy bias for China.

Asia

The FBMKLCI recorded a strong performance of 3.3% over the previous month, led by the Technology, Telecommunications and Financials sectors. Only the Energy and Transportation sectors recorded monthly declines on recessionary concerns. The month of July saw Bank Negara Malaysia (BNM) raising the Overnight Policy Rate (OPR) by 25bps which is the bank's second consecutive hike this year. Inflation continued to rear its head in the economy with the release of the June CPI data indicating a 0.6% increase over a month ago and 3.4% over a year ago. During the month, the first reading of the Tobacco Product and Smoking Control Bill 2022 was held, which included the much-anticipated generational endgame law for those born in 2007 and after. The Dewan Rakyat also passed the proposed anti-party-hopping law.

General View

Moving further into the second half of 2022, slowing growth and recession risks are a top concern for investors. With inflation still uncomfortably high in most major economies, the aggressive stance by central banks risks a hard landing for the global economy, which would be detrimental to corporate earnings and ultimately weigh on risk asset prices. We maintain our Neutral stance on local equities as we look out for clearer visibility of next year's earnings. Presently, positive economic recovery, on the back of reopening of international borders and robust private consumption, may be curtailed by risks of stagflation, weaker Ringgit, dampening business and consumer sentiment and political uncertainty amid the upcoming election. We will also employ 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

It was a volatile month for Treasuries with the 10-year US Treasury benchmark initially spiked back up to 3.00% in early July before rallying towards the end of the month to settle at 2.65%. The Federal Reserve (Fed) raised its policy rate by 75 basis points (bps) for the second month in a row but left guidance intentionally vague regarding any planned moves when it meets next in September. The recent softness in economic readings provided ammunition for yields to move lower and has deepened the month-long inversion of the 2-year/10-year Treasury yield curve. Meanwhile, the advanced estimate of 2Q 2022 GDP validated the market's concern of a technical recession with the economy showing a second quarter-on-quarter (QoQ) contraction at -0.90%. Over the month, despite the sequential 75bps hike in the Fed funds rate, the 2-year yield widened by only 5bps to 2.88% while the 10-year yield declined 23bps to 2.65%.

Malaysian Bond Market

Locally, government bonds saw strong buying support with yields edging lower by 24-38 bps across the curve, trending in line with the rally seen in US Treasuries alongside global rates. The yield curve mirrored bull flattening movements with outperformance in the 30-year segment with better buying interest for duration. Meanwhile Bank Negara Malaysia (BNM) delivered its second consecutive 25bps OPR hike to further adjust the "degree of monetary accommodation" amid better growth prospects for the Malaysian economy. Despite interest rate hikes, bond yields moved lower with better buying interests following lower UST yields as market were encouraged by the prospect of the Fed pausing its hiking cycle by December and BNM's gradual and measured approach to policy normalization. Buying interests spilled over to the auction markets which garnered strong BTC ratios of 2.4x-3.1x for the three auctions conducted during the month. In July, the 3-year yield was marginally higher by 3bps to 3.49% while the 10-year declined by 33bps to 3.89%.

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