July Outlook – A triple shock warrants seatbelts

SUMMARY

- **Risk of trade war amplified.** US equities closed flat whist the European and most Asian stocks declined in June on escalated global trade war concerns. More hawkish tone from DM central bankers where the Fed Dots guides for a potential 2 more hikes in 2H18 while the ECB president reiterated that the euro-area economy is strong enough to overcome increased risk, outlining the ECB's plans to complete QE purchases by end 2018. Over to China, in response to current headwinds, both internally and externally, the PBOC announced 50bps RRR cut that will unleash 700bn yuan in liquidity.
- **Malaysia now in policy sweet spot with steady growth and benign inflation.** BNM under the helm of new governor is expected to hold the OPR steady at 3.25% during Jul-18 MPC meeting, despite the policy tone might be dovish-biased amid external uncertainties. On the other hand, domestic economic fundamentals remain steady despite signs of moderation. Headline manufacturing PMI deteriorated at a slower pace in Jun-18 while distributive trade surged to 3-month high in Apr-18.
- **Foreign selling in equity intensified in June but slowed down in bond markets.** We saw continuous daily foreign net sell in equities, ranging from RM200m to RM500m, on the back of flight to safety, weakening ringgit and domestic policy uncertainties remain. However, FBMKLCI was the most resilient market in South East Asia while China Shanghai SE was the worst performing index in the region. Over to the local bond market, bargain hunting was seen in the short-end govvies while the long-end quasi-govvy space was well bid.
- **Macro – Financial markets volatility leads to economic turbulence or vice versa.** The global economic plane is still cruising at decent altitude. If you would go simply by the headlines, you may have thought it had already lost an engine. Not exactly. There is still plenty of thrust that is pushing Asia's economies ahead. On the other hand, financial markets have been jitters of late as uncertainties have piled up. So now, are we facing a financial market crisis or economic crisis is ahead? Fundamentals in emerging Asia remain relatively steady and robust but certainly, financial assets are not immune from the threats of a triple shock, namely: 1) tighter US financial conditions; 2) higher oil prices; and 3) trade wars.
- **Equity – Trade wars and "currency crisis" to dominate headline news in July.** If neither of the 2 happens severely, we expect foreign outflow from Malaysia to taper down, if not turn back into inflow instead. As a result, once foreigners stop selling, we expect our market to at least have a technical rebound. Also, once investors see the weak CNY to stabilise at circa USDCNY6.60-6.70, which was guided by the PBoC governor, we shall see investors regain certain degree of confidence in Asian markets. On the other hand, if we assume the market only has 2017's foreign inflow amount to unwind, we probably still have another RM5bn mark to go.
- **Fixed Income & FX – The good, the bad and the ugly.** According to estimates by the IIF, investors have cut allocations to EM debts considerably since late-April to Underweight. This is a major shift from the period between Mar-17 and Apr-18 when investors were mostly positive. We thought this development is positive as short-term investors have cleared position. In 2H18, the govvy auctions will be well supported with only RM4.8bn net issuance. This is also coupled with the lower supply of GG and corporate bonds as the government reprioritizes large infrastructure projects. Over to FX market, an upbeat Fed means an upbeat USD. A note of caution is likely to be sounded regarding the risks of a global trade war but here too the implications for the USD are largely positive where the mood is likely to be predominantly "risk off" in July.

Disclaimer:

This document has been prepared by Etiqa Insurance Berhad (ELIB) solely for informational purposes and shall not be construed as the basis for making investment, financial or other decisions. Past performance is not indicative of future results and no representation or warranty is made regarding future performance. ELIB makes no representation or warranty of any kind, express, implied or statutory regarding, but not limited to, the accuracy of this document or the completeness of any information contained or referred to in this document. This document is distributed on the express understanding that, whilst the information in it is believed to be reliable, it has not been independently verified by ELIB. ELIB and any of its related affiliates accepts no liability and will not be liable for any loss or damage arising directly or indirectly (including special, incidental or consequential loss or damage) from your use of this document, howsoever arising, and including any loss, damage or expense arising from, but not limited to, any defect, error, imperfection, fault, mistake or inaccuracy with this document, its contents or associated services, or due to any unavailability of the document or any part thereof or any contents.