August Outlook – The Art of Trade War

SUMMARY

- **Escalating US-China trade war while US-EU trade disputes ease.** Both the US and European stocks rose in July as President Trump and the EU's chief executive agreed to work toward eliminating trade barriers on industrial goods. On the other hand, the Fed's commitment to a gradual pace of interest-rate hikes meanwhile was criticized by President Trump, worried of a counteract effect to the latter's economic policies as the US GDP grew at 4.1% rate in 2Q18, fastest in almost 4 years. As trade tensions are on the rise, China further unveiled a package of targeted policies to boost domestic demand.
- **Malaysia's consumer confidence in 2Q18 hit 21-year high.** The MIER consumer sentiments index rebounded above the 100-point optimism threshold in 2Q18, the highest level since 2Q97. This is likely due to the recent change in the political landscape, abolition of the GST and the consumers' expectations of an improvement in the economic welfare. Meanwhile, Jun-18 inflation hit 40-month low as the impact of zero-rated GST kicks in and BNM left the OPR unchanged as largely expected at 3.25%.
- **FBMKLCI gained close to 100 points in July on local support while foreigners started buying on govvies.** Most locals were risk off in the earlier month as they were awaiting for foreigners to finish selling our equity market. Hence, when foreign selling started to slow down, bargain hunting activity returned to look at bashed down and high beta sectors. On the other hand, the local bond market ended July with yields easing MoM on strong buying momentum across all tenures. Meanwhile, auctions for RM9bn local govvies saw strong support with favourable bid covers.
- **Macro – Likelihood, implications and counter measures of trade tensions.** US-China trade spate will remain the main focus in Aug-Sept and we think that trade tensions will escalate further as both countries' leaders have come up with targeted fiscal and monetary policy measures to negate possible adverse economic impacts. If full-blown trade war happens, US GDP growth would be reduced by 0.7% in 2019 while Chinese growth would be 0.8% slower, and global growth would be cut by 0.5%. However, it is not necessary to be so negative to ASEAN economies as trade diversion to ASEAN could eventually be an opportunity for FDI inflows.
- **Equity – All eyes on 2QCY18 results since August is a result reporting month.** Our channel checks tell us that this coming 2QCY18 results would most likely be within expectations although there is risk of potential kitchen sinking activities by some corporates given their poor share price performance. To note, we have upgraded our construction sector back to Market Weight from Underweight as investors turned slightly risk on. However, domestic equity market has not factored in another USD200bn trade tariff imposition but foreign selling temporary takes a breather while waiting for new development.
- **Fixed Income & FX – Value seen in the longer-end bonds.** In 2H18, there will be lesser supply of govvies in the market with net supply of RM2bn in 3Q18 and 4Q18 each and new issuances will be focused at 3-10y tenures. Therefore, we see value in the longer-end govvies due to supply constraint as well as current favourable spreads. Furthermore, positive real returns in domestic market since the beginning of this year should provide room for BNM to cut the OPR as a counter measure if the Malaysian economy suffers from the wrath of intensifying US-China trade war going into 2019. Over to FX, the ringgit is pretty much driven by external factors for now, such as trade tensions which lead to weakening RMB. In view that the US-China trade conflict is going to be escalated in Aug-Sept., we revise our ringgit trading range to USDMYR4.00-4.15 in Aug-18.

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, ordue to any unavailability of the document or any part thereof or any contents.