December Outlook – Synchronised Asian Growth Moderation

SUMMARY

- **Temporary lift from trade-war truce**. US equity rebounded in Nov-18 on a more dovish signal by the Fed's Powell and as the US agrees to delay any further tariff increases on China, subject to successful negotiations in 90 days. However, the European market declined in Nov-18 on slower growth data, albeit ECB's Draghi expects the end of bond buying to still happen in Dec-18. Meanwhile, some Asian economies are showing moderating GDP growth in 3Q18.
- **Moderating GDP growth while OPR remains unchanged in Malaysia.** BNM expects the economy to remain on a steady growth path for the remainder of the year, after recording a GDP growth of 4.4% YoY in 3Q18. As such, the OPR maintains at 3.25% for the fifth consecutive meetings since Jan-18. Separately, Budget 2019 announced GDP forecast of 4.8% in 2018 and 4.9% in 2019. Despite global economic landscape uncertainty, improving growth forecast to be cushioned by domestic consumption as well as the expected recovery in both agriculture and mining sectors.
- **Recovery in global markets MoM after closing so red in Oct.** For Nov, the Asian markets had led the global markets' rallies after huge retracements in Oct following trade war concerns. Malaysia KLCI, on the other hand, was still down -1.7% MoM due to kitchen sinking by some of the corporates. Over to the local bond market, we have seen more safe haven flows in Nov-18, thus, lifting the whole MGS term structure higher, where the 5y MGS benchmark suffered the most, but the corporate bond segment was relatively steady without much movements.
- **Macro – Turning point in growth and policy rates.** We foresee economic and market views are increasingly divergent going into 2019 especially the political and market headwinds tend to add to policy complications. As such, our 2019 investment thesis is based on synchronised GDP growth moderation in emerging Asia, the end of rates hiking cycle which will eventually lead to weakening USD and for Malaysia, the sovereign rating outlook and government finances will be the main focus. EM Asia policy rate has, on average, been trailing US Fed fund rate path to the upside so far. As the US policy rate reaches hiking cycle peak, EM Asia policy rate hikes should follow through to come to an end.
- **Equity – Minimum spending, maximum impact; introducing KLCI target for 2019 at 1,700**. Although we expect window dressing activities since it is the last month of the year, we believe GLCs will only dress up when the timing is right. And, we think these targeted stocks would include those where their share prices have been recently bashed down and have low liquidities. For Nov-18, we have upgraded 2 sectors to Overweight, namely Financial and Rubber Glove sectors. We see more downside risk of consensus earnings forecast for 2019 at this junction. As a result, we take a more conservative view with the 2019 KLCI target of 1,700. Consensus on the other hand has diverse KLCI targets between 1,600 and 1,900.
- **Fixed Income – Mildly bearish MGS Curve in 2019**. The outlook for 2019 appears rather gloomy for the domestic bond market against a backdrop of weaker GDP growth expectations amid ongoing uncertainties on trade war and oil prices. We forecast 2019 Malaysian GDP growth to moderate to 4.6-4.7% vs the official forecast of 4.9%. In the meantime, inflation is expected to edge up with the reintroduction of SST and targeted fuel subsidy. As such, we expect the 10Y MGS to range between 4.20% and 4.30% in 1H19 on subdued macro data and rising uncertainties on sovereign rating outlook and net supply dynamics before whittling down to end the year at 4.20% due to refinancing needs on larger maturities towards 4Q19.

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