# February Outlook – Diverting Attention to Geopolitics

## SUMMARY

- **The US Fed Reserve has become more "data & market" dependent in policy path ahead while being flexible in its balance sheet run-off vs auto-pilot.** Negative trade war effects are spreading in Asia while the Eurozone's Composite PMI fell in Dec-18 to a four-year low. Separately, when President Donald Trump withdrew the US from a long-standing nuclear weapons treaty with Russia on Feb. 1, his actions set the stage for what many fear could be a new arms race between the global superpowers.
- **Both the Malaysian business & consumer sentiment index sank below the 100pts threshold in 4Q18**. MIER forecast business conditions are expected to moderate in 1Q19, but consumers will remain prudent in their shopping. In Jan-19, the ringgit debt instruments reported outflows of RM2.3bn while equity market saw RM1bn inflow, bringing total portfolio outflows to RM1.3bn, narrowing from –RM3.3bn in Dec-18.
- **Malaysia equity market was the only market in negative territory in Jan-19 while bond continued rallied as the Fed turns dovish.** With global market rallying in Jan-19, we saw spillover positive trading sentiment to our local market by positioning in bashed down small- and mid-cap stocks. However, our KLCI closed marginally lower MoM while the rest of the regional peers were up 2-10%. On the other hand, the local bond market rallied with MGS yields trending lower MoM especially at the belly of the curve. Despite a net supply of RM13bn govvies in Jan-19 coupled with foreign selling activity, govvy yields fell and well supported by local investors as the Fed went on a dovish pivot at its 1$^{st}$ FOMC meeting on Jan 30$^{th}$.
- **Macro – Tightening financial conditions in Advanced Economies.** Changes in financial condition are partly a reflection of global developments. Current trend reflects tighter monetary policies in advanced economies toward 2H18 whilst temporary easing in FCI in Jan-19 post the dovish Fed's statement on flexible balance sheet run-off while turning more data dependent ahead. Increased leverage in the Chinese economy over the past 10 years. Fortunately, onshore borrowing costs in China has been on the declining trend, which is supportive of corporate expansion. Whereas borrowing costs in Advanced Economies had been rising from 2003 to 2006, which attributed to the global financial crisis in 2008.
- **Equity – We are still adopting a defensive and trading stance with limited exposure in the near term.** With global market rallying in Jan-19, we saw spillover positive trading sentiment to our local market by positioning in bashed down small- and mid-cap stocks. As long as global market is sustainable and there is no negative outcome from the US-China trade war by Mar. 1, then we may see small- and mid-cap stocks continue their rallies into Feb- and Mar-19, which is more of liquidity driven rather than long term fundamental buy.
- **Fixed Income – Bullish outlook for the Malaysian govvies.** In view of the recent dovish statement by the Fed, we have revised our year-end MGS yield targets lower from our previous projections. We now foresee that there will be no hike by the Fed this year as opposed to 2x hike previously as the US and global growth is expected to see a slowdown amid ongoing trade tensions, US government shutdown and continued weakness in the European economies. Additionally, we see a return of foreign funds due to the attractive real returns as MYR strengthens.

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