July Outlook – Macro & Risk-Asset Disconnection

SUMMARY

- **Rising monetary easing prospects.** While the Fed left their key policy rate unchanged, they dropped a reference in their statement to being “patient” on borrowing costs and forecast a larger miss of inflation target this year. Also, a statement from the ECB president which said “additional stimulus will be required” if the economic outlook does not improve. Dovish central bankers’ stance is largely due to weakening manufacturing activity amid trade tensions but on a brighter note, the US and China agreed at the G20 summit to restart trade talks.
- **World Bank lowers Malaysia's 2019 growth on global economic volatility.** The World Bank has downgraded Malaysia's economic growth this year to 4.6% from 4.7%. Malaysia’s Nikkei Manufacturing PMI eased further in Jun-19 and it has been in the contraction region for the 10th consecutive months while inflation remained low at 0.2% YoY for the third straight month in May. Positively, broad money (M3) growth rose for the second straight month in May-19, largely driven by higher demand from the private sector and a slower decline in funds for foreign operations.
- **Local equity fell before recovering while bond market continued to charge ahead.** Domestic equity market sentiment was dragged by negative trade war news in 1H June but came 2H June, we saw investors concentrated buying on few key heavyweights rather than across the board. Over to fixed income market, local govvies continued to rally in Jun-19 with yields lowering across benchmarks, tracking the global trend as central banks become increasingly dovish on uncertain growth outlook.
- **Macro – Disconnect between macro trend and financial assets performance.** Tariffs themselves have a real economic impact where the second-round effects on financial market conditions and uncertainty cascade through investment, employment, consumption, and growth to compound the impact. Notably, the expansion in manufacturing activity is cooling fast to the slowest pace since Sep-16, according to the BoJ’s Tankan Survey and true enough, the latest PMIs in Jun-19 ticked down again as the global new export orders have been contracting for 10 months now. However, both the high- and low-risk asset prices are currently all rallying, premising on high expectations of concerted easing monetary policy path globally which is led by the Fed.
- **Equity – Time to act local after thinking global**. With trade war event temporary being put aside, this gives room for investors to focus back on the fundamentals of our local market, starting with the construction sector which has been receiving many news flow of contract awards across small to big construction companies. Despite having all these temporary relief rallies, investors should always be on the guard of trade war developments as Trump always has the tendency to ‘flip flop’. For July, we have upgraded the technology sector to Market Weight and downgraded the rubber glove sector to Market Weight.
- **Fixed Income – The Fed rate cut in Jul-19.** The Fed’s dovish statement in the June FOMC statement suggests that a rate cut is imminent with market expecting as much as 3 cuts this year. We expect that the Fed to deliver a 25bps cut in Jul-19 as opposed to our earlier estimates of a cut in Sep-19 as a pre-emptive measure amid continued trade tensions alongside bearish outlook on global growth. We have therefore, revised our year-end MGS yields lower from our previous estimates 6 months ago where the assumptions then did not include an OPR cut (which happened in May) and the Fed’s dovish stance.

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