Market Review and Outlook

May 2022

Market Review

May was a volatile month with the global economy being continually impacted by the monetary policy tightening measures of several central banks to rein in inflation, the prolonged Russian – Ukrainian conflict and the lockdown of parts of the Chinese economy as part of its dynamic zero Covid policy. Consequently, the global equity market as evinced by the MSCI World Index continued its decline by easing 0.16% mom. In the US, the Dow Jones Index was flattish, with a meagre +0.04% mom increase. This was despite its Federal Reserve (Fed) decision to raise its Fed fund rate by 50bps during the month as it had already provided ample signalling in prior months. April 2022 headline inflation in the US was still elevated at +8.3% yoy which prompted the Fed Chair to state that he could not guarantee a so – called 'soft landing' for the economy in his efforts to tamp down inflation which would remain his top priority. On the employment front, the US unemployment rate was maintained at 3.6% in April which is the lowest level post – Covid and comparable to levels prior to the pandemic.

In Europe, the Stoxx 50 Index fell 0.36% mom as the Russian – Ukrainian conflict continued unabated with attempts at diplomatic solutions appearing to bear little fruit. Instead, the European Union (EU) decision to ban 70% of imports of Russian oil by ship and up to 90% by the year's end could have further impact on their own economies as Russia has supplied as much as circa 40% of the European Union's energy needs. To fill in the energy supply void, Europe would have to source alternatives from the existing supplies from the global market which could worsen inflation. On that note, May 2022 Monetary Union Index of Consumer Prices flash inflation in the European Union (EU) surged to a new record high of +8.1% yoy, which was 4x the European Central Bank's (ECB) target of +2%. yoy. To that end, the ECB, which is already lagging its US and British peers, has flagged for rate hikes to begin in 3Q22. On the other hand, the Shanghai Composite Index rebounded +4.57% mom. Unlike the broader world, China continued to struggle with the proliferation of the Covid – 19 Omicron variant. Throughout the month, Beijing, Shanghai and Tianjin imposed stringent pandemic curbs which inadvertently hampered economic growth. To counter the weak loan demand due to Covid lockdowns and a property slump, the People's Bank of China (PBOC) reduced its 5 - year Loan Prime Rate (LPR) to 4.45% from 4.60%, its largest reduction since 2019.

During the month, Brent oil maintained its relentless upward trajectory with a +12.3% mom surge to USD122.84/ bbl on the back of the aforementioned moves by the EU to cut off Russian crude. Palm oil price instead fell by 14.0% mom to RM6607/ MT as the Indonesian government lifted a temporary ban on palm oil exports that it enforced in late April to lower the prices of domestic bulk cooking oil. There was also an increase in Malaysia's palm oil inventory by +11.5% mom to 1.64m MT in April 2022.

Over in the ASEAN region, equity markets were somewhat lacklustre during the month under review. Malaysia's FBMKLCI corrected 1.90% mom as investors were surprised by Bank Negara Malaysia's (BNM) move to raise the Overnight Policy Rate (OPR) by 25bps to 2.00% as global inflationary pressures have increased sharply. That said, BNM also iterated that growth was on firmer footing, driven by strengthening domestic demand amid sustained export growth. On our economic front, 1Q22 GDP growth recorded a +5.0% yoy growth which was ahead of consensus expectations, being driven by sustained recoveries in private consumption as well as services sectors. Nonetheless, April 2022 Consumer Price Index (CPI) came in at 2.3%, which was well within BNM's inflation forecast for 2022.

Net foreign equity inflow in May 2022 amounted to RM77.3m, -90.6% mom. Singapore's Straits Times Index also tumbled 3.71% mom as 1Q22 GDP growth momentum decelerated to +3.7% yoy from +6.1% yoy in 4Q21. Its April 2022 Non – oil Domestic Exports (NODX) grew by +6.4% mom, -1.3 ppt mom and was also slightly below consensus estimates as the impact of China's Covid – 19 city lockdowns kicked in to disrupt global supply chains. Singapore's inflation level was also disconcerting with its April 2022 CPI All Items stubbornly high at +5.4% yoy, the same as March 2022 and at levels last seen in 2012. In Indonesia, the Jakarta Composite Index dropped 1.11% mom despite 1Q22 GDP growth coming in within consensus expectations at +5.01% yoy but -0.96% qoq. The Bank of Indonesia elected to keep its key 7 – day reverse repurchase rate stable at its low of 3.5% in May 2022 but adjusted its reserve requirement ratio (RRR) from 5.0% against IDR deposits to 9.0% by September 2022. Lastly, the Stock Exchange of Thailand slid 0.24% mom on the back of the abovementioned China Covid – 19 driven economic slowdown, expectations of Fed rate hikes and supply chain disruptions caused by the Russia – Ukraine conflict. Apart from that, its 1Q22 GDP growth was +2.2% yoy and ahead of consensus expectations.

For the bond market, despite reaching year-to-date highs in the first two weeks of May, most US Treasuries (UST) yields ended the month stronger as investors steered away from equities and sought shelter in bonds. Fed Chairman Jerome Powell continued to assert that Fed would continue raising rates until inflations show signs of retreat thereby reinforcing expectations that the Fed would continue its 50bps hikes in upcoming Fed meetings.

Back at home, the 11th May Monetary Policy Committee (MPC) meeting, as mentioned, BNM surprised the bond market with a pre-emptive 25bps hike, lifting the OPR off the record low of 1.75% which had been maintained since July 2020. With the domestic growth now on a firmer footing, the MPC decided to begin reducing the degree of monetary accommodation. It mentioned that global inflationary pressures have increased sharply due to a rise in commodity prices, strained supply chains and strong demand conditions, particularly in the US. However, despite the surprise OPR hike, the local government bonds staged a rally post-MPC as yields rallied 3-32bps mom across the curve as investors sought safety in bonds.

Foreign funds turned net buyer in May with a purchase of RM0.5b of Ringgit bond holdings (April: -RM2.2b), bringing YTD inflow to RM0.9b. Foreign share of both MGS and MGS+MGII decreased to 37.4% (April: 37.6%) and 24.7% (April: 25.0%) respectively. Foreign reserves increased by USD0.3b mom to USD112.8b as of end-May 2022.

Market Outlook

We believe that investors would keep a keen eye on how the Fed's and other central banks' upcoming rate hike decisions could effectively suppress the burgeoning global inflation concerns. Furthermore, there are heightened geopolitical risks emanating from the Russia – Ukraine conflict which if allowed to prolong, might further strain the already stretched global supply chains. Over in China, global investors would be monitoring the progress of their dynamic zero Covid – 19 policies in controlling the recent outbreaks and its impact on their economy. Domestically, there could be political concerns brewing on the horizon as the 15th General Election (GE15) which must take place before the end of July 2023 might be pushed back to 2H22, as the Pakatan Harapan's Memorandum of Understanding (MoU) of Transformation and Political Stability with the government is only valid till end July 2022. In addition, our government has begun posturing for the gradual removal of blanket fuel subsidies and its eventual replacement by a more targeted system as it has become prohibitively expensive for the government should oil price hover above USD100/ bbl.

For equities, we maintain our prudent yet sensible posture towards our equity market's longer term growth trajectory and, where opportunities arise, would direct monies into fundamentally good investments. We are also inclined to engage in some trading activities should market volatility present us with good opportunities. We are partial towards sectors exhibiting robust growth prospects but remain cognizant for signs that market volatility might dictate a shift of investment direction.

Locally, bond yields are expected to remain volatile in tandem with the UST yield movements. The markets have been jittery over the aggressive Fed rate hike path as upside risks to inflation persist, while there are simultaneous downside risks to growth as the ongoing Ukraine conflict is set to further worsen the global supply chain constraints. BNM mentioned at the recent MPC meeting that any rate hike would be done in a measured and gradual manner, ensuring that monetary policy remains accommodative to support sustainable economic growth in an environment of price stability. Hence, further OPR hike(s) could be expected in 2H22, after BNM kickstarted its policy normalization cycle in May 2022.

We think the risk-reward of MGS has improved with the Ringgit rates market well priced for BNM normalisation. We would remain cautious of the bond market volatility arising from both external and internal fronts, which would impact local yields. Moreover, we would maintain our strategy to accumulate bonds at favourable valuations skewing towards good quality names.