Allianz

Market Review and Outlook

May 2023

Market Review

In May 2023, global equity markets experienced a correction with the MSCI World Index falling 1.25% mom, being hampered by stubbornly high core inflation in US and Europe which gave rise to the spectrum of prolonged peak policy rates. Apart from inflationary concerns, US' Dow Jones Index which dropped 3.49% mom was also dragged by the debt ceiling deadlock between the Democrats and Republicans throughout May. On the other hand, from an economic standpoint, its April 2023 core consumer inflation rate was 5.5%, -0.1 ppt mom and generally in – line with expectations. Housing starts in April 2023 was also up +2.2% mom as compared to the expectation of a 1.4% mom contraction. In addition, May's preliminary reading of the S&P Global US Composite Purchasing Managers Index (PMI) was 54.5 versus 53.4 in the previous month. In line with market expectations, the Federal Reserve raised the Fed Fund Rate by yet another 25 bps to its latest target range of 5.00 – 5.25% but ceased posturing that more policy firming might be required to achieve its 2.0% inflation target. In Europe, the Stoxx 50 Index also plummeted 3.24% mom as its core Consumer Price Index (CPI) had an April preliminary reading of +5.6% yoy which was comparable to the +5.7% yoy reading for the previous month. Eurozone's March unemployment rate improved to 6.5%, -0.1 ppt mom and was slightly better than consensus expectation of 6.6%. To counter the persistent inflationary situation, the European Central Bank (ECB) raised its deposit rate by 25 bps to 3.25% but also noted a possible slowing of the pace of hikes. China's Shanghai Composite Index also declined by 3.57% mom as its April Caixin China PMI Manufacturing Index reported a contractionary reading of 49.5 as compared to 50.0 a month ago. Its April Industrial Production only grew by +5.6% yoy which fell short of consensus' expectation of +10.9% yoy. The People's Bank of China (PBOC) opted to keep its 1 – year and 5 – year Loan Prime Rates stable at 3.65% and 4.30% respectively in May 2023, for the 9th straight month.

During the month under review, Brent oil decreased by 8.6% mom to USD72.66/ bbl. It was troubled by weaker oil demand outlook which depressed market sentiments. Crude palm oil (CPO) also weakened by 17.3% mom to RM3255/ MT in May as the US Department of Agriculture issued 2023/34 bumper crops estimates which led to a correction of oil seed and other vegetable oil prices. In addition, China and India had also slowed down their imports of CPO during the month.

Over in the ASEAN countries, the Stock Exchange of Thailand inched up +0.29% mom on account of positive market sentiments stemming from its general election results on 14 May 2023. The Thai equity market had rallied on a MTD basis prior to the election but gave up some of its gains after it emerged that the Move Forward Party (MFP) was the biggest winner and this gave some investors pause due to their people – centric policies such as an approx. 30% minimum wage hike. It should be worthwhile noting that the Thai coalition government would only be properly determined later, up to 60 days post – election. The Thai economy held up well with its 1Q23 GDP growth coming in at 2.7% yoy, +1.3 ppt qoq and above consensus expectations. Malaysia's FBMKLCI fell 2.04% mom to 1387.12 due to concerns surrounding the global economic slowdown and US debt ceiling impasse. Foreign net equity outflow in May 2023 amounted to RM728.2m, which led to a YTD net outflow of RM2.8b. The Ringgit had also weakened to RM4.6130: USD1.00 from RM4.4622: USD1.00 in April 2023 despite the Monetary Policy Committee (MPC) of Bank Negara Malaysia's (BNM) decision to raise its Overnight Policy Rate (OPR) by 25 bps to 3.00%. That said, Malaysia was still on sound economic footing with 1Q23 GDP growth reported at +5.6% yoy which was above consensus expectations and a March Industrial Production growth of +3.1% yoy which was also ahead of expectations. The Straits Times Index (STI) of Singapore had also experienced a drop of 3.42% mom following a Non – Oil Domestic Export (NODX) contraction of 9.8% yoy, its 7th consecutive month of decline while it also experienced an April Industrial Production contraction of 6.9% yoy, -2.7 ppt mom. Lastly, the Indonesian Jakarta Composite Index (JCI) tumbled 4.08% mom as it recorded an April export contraction of 29.40% yoy which worsened from an 11.33% contraction in March and was below consensus expectations. It was also pulled down by weakening commodity prices in the month as coal and nickel dropped 26.4% mom and 12.1% mom respectively.

The global bond market saw another volatile month in May. US Treasuries (UST) weakened with yields rising by 19 – 33 bps mom in a flattening manner. The sell – off was due to the confluence of factors that included the US debt ceiling concerns, stubbornly high inflation and the heightened probability of another rate hike. The US Treasury Department, constrained by the need to raise or suspend the debt ceiling, announced unchanged coupon auction sizes for the May – to – July quarter. With US cash resources dwindling, investors avoided Treasury bills maturing during the first half of June, causing short tenured yields nearing maturity to briefly exceed 7% before an agreement to temporarily suspend the debt ceiling was reached to avoid a default. On 2 June 2023, the US Congress approved a deal to lift the country's borrowing limit which brought some relief to the markets. The agreement suspended the debt ceiling and the spending limit set by Congress that determines how much money the government can borrow, until 1 January 2025. Earlier on 25 May 2023, Fitch placed the US "AAA" rating on "rating watch negative", signaling that it could downgrade US debt if lawmakers do not agree on a bill that raises US Treasury's debt limit. As of end – May, the market – implied expected peak was higher at 5.285% in July (end – April was 5.033%) compared to a +36.4% probability of a rate hike in June (previously +21.1%) and +46.5% in July (previously rate cut probability of 23.2%).

The Malaysian Government Securities (MGS) yield movements in May were rather resilient compared to the UST movements, even after BNM surprised the market by raising the OPR by 25 bps to 3.00%. Mom, MGS yields shifted between -4 bps to +9 bps with the 7 – year MGS and 10 – year MGS attracting the most interest. The 10 – year MGS closed 3 bps lower at 3.70%. However, market players also traded cautiously ahead of the US Congress decision to lift the country's borrowing limit to avoid a default.

Market Outlook

Though there are several exo – and endogenous risks that appear to plague the global as well as our domestic economy, there are nascent signs of recovery. The US Senate has recently approved a bipartisan debt ceiling bill which should thankfully avert the first – ever US debt default and also the central banks appear to have begun to ease back on the momentum of rate hikes required to curtail the burgeoning inflation issue. However, we are cognizant that there still are risks at large such as the Russia – Ukraine war, the reemergence of new Covid outbreak and the success of the economic reopening of China. The inflationary environment may also prove to be more stubborn than anticipated with the latest US May Non – Farm Payrolls (NFP) rising by 339k which surpassed market expectation of 190k. Closer to home, several states will be soon undergoing state elections which could, to some degree, serve as a litmus test as to the people's approval of the Unity government. Nevertheless, the results would not likely have any immediate effect on the stability of our federal government and hence, we believe that rollouts of their policies would continue unabated.

For equities, we would continue to adopt a prudent yet sensible posture towards our equity market's longer term growth trajectory and, where opportunities arise, would channel monies into fundamentally good investments. Nonetheless, we may at times adjust our stance to adapt to any market environment flux which may necessitate an investment direction shift. Otherwise, there may also be times where we could engage in a modicum of trading activity to take advantage of any prevailing market volatility.

In 2023, bond yield volatility in the fixed income market is expected to persist due to fears of a potential banking crisis and the sticky inflationary data although the threat of a US default has diminished. Fed's 'dot plot' is at 5.1% for this year-end, while the market implied rate is pricing in at least one rate cut to 4.908% by year-end (narrowed from a minimum of two rate cuts last month at 4.474%). Locally, BNM in its latest assessment cited that with the OPR level now at 3%, the monetary policy stance is slightly accommodative and remains supportive of the economy. With the latest 25 bps hike on 3 May, BNM has withdrawn the monetary stimulus intended to address the economic disruption caused by the Covid – 19 crisis. Despite the improved risk – reward of MGS, external and internal factors could still contribute to bond market volatility that may affect local yields. However, we will continue to accumulate bonds at favorable valuations while prioritising good quality names.

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