Allianz

Market Review and Outlook

July 2022

Market Review

For equities, the MSCI World Index rose +7.9% mom to close at 2,746 points for the month of July. Similarly, the Dow Jones Index, propelled by solid earnings from technology and oil companies, increased by +6.7% mom as it reversed last month's loss as it seemingly looked past concerns surrounding high inflation and recession risks. On the US' economic front, retail sales in June increased by +1.0% mom as compared to a decrease of 0.3% mom in May. Its May industrial production grew slower at 0.2% mom versus an increase of +1.1% mom in the previous month. US S&P Composite PMI growth weakened to 52.3 in June as compared to 53.6 in May. Over in Europe, the Stoxx 50 Index gained +7.3% mom during the same period despite a lower Eurozone S&P Composite PMI reading of 52.0 in June as compared to 54.8 in May. Its May retail sales rose +0.2% mom after contracting by 1.3% mom in the previous month. Nonetheless, its industrial production growth grew by +0.8% mom in May as compared to an increase of +0.4% mom in the previous month. Conversely, China's Shanghai Composite Index fell 4.3% mom in July despite an improvement in Caixin China Composite PMI reading of 55.3 in June as compared to 42.2 in May. After cutting its 1-year Loan Prime Rate twice in December 2021 and January 2022 to bolster its economic growth, the People's Bank of China kept it stable at 3.70% in its July 2022 meeting. After a reduction of the 5-year Loan Prime Rate in May 2022, it was also kept stable in its July 2022 meeting.

In July, Brent oil declined further by 4.2% mom to USD110.01/bbl amid concerns on lower demand for gasoline amidst a rising rate environment to combat inflation as well as global recession fears. Crude palm oil (CPO) price also dipped by 14.4% mom to RM4,355/MT after Indonesia lifted its export ban and on the back of concerns that demand may be stifled by high prices.

On the ASEAN front, equity markets closed the month under review with positive performances. Malaysia's FBMKLCI rose by +3.3% mom, partially reversing its 8.0% mom loss in June. July saw net foreign inflows of RM124m, bringing YTD inflows to approximately RM6.2b. From an economic standpoint, Malaysia's May industrial production growth weakened to +4.1% yoy compared to a growth of +4.6% yoy in the previous month. June manufacturing PMI strengthen to 50.4 as compared to 50.1 a month ago. Indonesia's Jakarta Composite Index gained +0.6% mom despite a lower S&P Global manufacturing PMI reading of 50.2 in June as compared to 50.8 in the previous month. The Indonesian central bank held its 7 - day repo rate stable at 3.5% in its June meeting, unchanged since February 2021. Similarly, the Stock Exchange of Thailand increased by 0.5% mom despite a declining S&P Global manufacturing PMI reading of 50.7 in June as compared to 51.9 in the previous month. The Bank of Thailand kept its Benchmark Interest Rate at 0.50%, unchanged since May 2020. Singapore's Straits Times Index surged 3.5% mom despite an 8.5% mom drop in industrial production growth in June as compared to an increase of +10.9% mom in May. Its June PMI reading was also slightly weaker at 50.3 as compared to 50.4 in May and its Non-oil Domestic Exports grew +3.7% mom in June as compared to a growth of +3.2% mom in May.

US Treasury (UST) rallied in July and ended the month lower by 17-36bps mom after the Fed authorized its second consecutive 75bps interest rate hike in July in a bid to stem the swelling inflation mainly arising from the surge in food and fuel prices. This took the benchmark overnight borrowing rate up to a range of 2.25%-2.50%, which was the highest level since December 2018. US CPI surged 9.1% yoy in June 2022 (May 2022: 8.6% yoy) beating the consensus estimate of 8.8%, which was the largest yoy jump since December 1981. US GDP contracted again in 2Q2022 by 0.9% qoq (survey: +0.4% qoq) after the 1.6% qoq decline in 1Q2022 which brings the US economy to a technical recession. Fed's Chairman, Powell however opined that the US economy is not in a recession as central bank has been raising rates to control inflation and the labour market in general remained tight.

Malaysian Government Securities (MGS) yields were mostly lower by 25-42bps mom, largely tracking the UST movements. In the latest World Economic Outlook Update published on 26 July, the International Monetary Fund (IMF) slashed Malaysia's economic growth forecast for 2022 from 5.6% to 5.1%, which is lower than Bank Negara Malaysia's (BNM) estimated GDP growth range of 5.3%-6.3%. The lowered growth projection considered factors that could hamper global trade, including exposure to the ongoing Russia-Ukraine war, global inflation, tighter monetary policies and geopolitical tensions, among others. Malaysia's CPI for June 2022 increased by 3.4% yoy which exceeded consensus expectations of 3.2% yoy and May 2022 figure of 2.8% yoy. The increase was largely due to food inflation which rose 6.1% yoy in June.

Foreign funds net sold Ringgit bond holdings with net outflows of RM3.5b (June: -RM4.1b), bringing YTD outflows to RM6.8b. Foreign share of both MGS and MGS+MGII lowered to 35.5% (June: 36.5%) and 23.3% (June: 23.9%) respectively. Malaysia's foreign reserves climbed marginally by USD0.2b to USD109.2b as of end-July 2022 (June: USD109.0b).

Market Outlook

Globally, markets are expected to alternate between risk-off and risk-on as investors digest the upcoming Fed policy rates and conditions of the economies. The volatility is compounded by the swings in commodity prices due to geopolitical concerns on the Russian-Ukraine conflict and its impact on commodity prices, global inflation and interest rates. Locally, investors will be keeping an eye on Malaysia's 2Q22 GDP and July's CPI figures, as well as the 2Q results season. Investors would also be monitoring newsflows on the possibility of an early 15th General Election in 2022.

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 direct monies into fundamentally good investments. That said, during this period of nascent economic recovery, we would be partial towards robust growth sectors but should remain watchful for any changes in market environment which might necessitate a realignment of investment direction. We might also at times assume a degree of trading bias to take advantage of any market volatility.

Locally, bond yields are expected to remain volatile in tandem with the UST yield movements. Although US has entered into a technical recession, the markets continued to remain jittery over the potential aggressive Fed rate hike path as global inflation remains elevated due to still high commodity prices and supply disruption. The Fed indicated that it is still committed to achieving its targeted inflation rate of approximately 2.0% and economic data will be scrutinized heavily to determine the next rate hike. On the other hand, local monetary policy is expected to remain accommodative to support sustainable economic growth in an environment of price stability as BNM reassured that economic developments and inflationary conditions will be monitored continuously and any rate hike would be done in a measured and gradual manner. Further OPR hike(s) could happen in 2H22, after BNM kickstarted its policy normalization cycle by 25bps during the Monetary Policy Committee (MPC) meeting in May 2022 followed by a second consecutive OPR hike in July to 2.25%.

We think the risk-reward of MGS has improved with the Ringgit rates market well priced for BNM normalisation but we are mindful of the bond market volatility arising from both external and internal fronts, which would impact local yields. The risk remains if domestic inflation surprise on the upside and foreign portfolio outflow accelerate. We would maintain our strategy to accumulate bonds at favourable valuations skewing towards good quality names.