

Kenanga Investors

Date: 14 January 2019

THE DECEPTIVE TRADE CONFLICT TRUCE

Focus Malaysia (12 January 2019)

By Ismitz Matthew De Alwis

- Trump must act more cohesively to settle the US-China trade dispute
- Other challenges to a global equity market rebound in 2019



f there is one wish the global investment fraternity has for 2019, it has to be for US president Donald Trump to act in a more gentlemanly manner in his decision-making process, particularly on issues with major global impact. Last year witnessed how the eccentric behaviour of the leader of the world's biggest economy brought about numerous rollercoaster rides time and again across equity markets worldwide. The global economic climate has been besieged with uncertainties of sorts in recent times with Trump's notoriety in declaring a 'deceptive' 90-day trade conflict truce — his most recent market-adverse stunt. On Dec 3, the already sluggish Dow Jones Industrial Index rebounded 250 points soon after Trump and his Chinese counterpart Xi Jinping agreed to a 90-day ceasefire in the trade war that has weighed heavily on global stock markets since mid-2018. But the joy was

short-lived as Wall Street's enthusiasm for the US-China trade truce vanished 24 hours later (the Dow plunged 799 points or 3.1%) following Trump's costly tweet labelling himself as a "Tariff Man" in addition to the surprise and controversial arrest in Canada of Huawei's chief financial officer Meng Wanzhou at the behest of US authorities.

Prior to the truce, both economic giants had already been embroiled in tit-for-tat counterblows with China reciprocating every trade action initiated by the US, i.e. by releasing last August a list of American goods worth US\$60 bil (RM246.66 bil) that Beijing intends to hit with tariffs in retaliation for Trump's plan to impose duties on US\$200 bil in Chinese imports.

DOUBLE-EDGED SWORD

Given his reputation as a businessman extraordinaire – the first billionaire president in US history - Trump would be better off leveraging his business flair to rally economic growth, spread wealth or share prosperity across the globe. Instead, his key messages tend to circle around the usurping of American wealth by foreign economic forces. Ditching much of the legacy of his predecessor Barack Obama, the US has disassociated itself from the 11-member Trans-Pacific Partnership (TPP) which came into effect on Dec 30 with economic powerhouses in the likes of Japan, Canada, Mexico and Australia.

In line with his "America First" agenda to shrink the US trade deficit and overturn "decades of unfair trade deals that sacrificed our prosperity," Trump is adamant in re-negotiating free trade agreements at all costs to safeguard the US economy. China aside, Trump has also waged trade wars on all fronts vis-à-vis free trade animosity with neighbours Mexico and Canada (a revised North American Free Trade Agreement



Kenanga Investors

was sealed on Nov 30) as well as the European Union (with whom Trump declared the scale of hostility was "almost as bad as China, just smaller").

The trade conflict situation is now akin to a double-edged sword. If it worsens with the Trump administration expanding tariffs, the global economy - emerging markets are not spared - is likely to be harmed given the huge size of the US trade with China. On the contrary, there are valid reasons for financial markets worldwide to rejoice if the dispute can be resolved soonest - or at least managed with utmost precaution.

RECORD-BREAKING FEATS

In all fairness, Trump should not be faulted as the sole protagonist for the under-performing global stock markets throughout 2018. On Dec 20, the Federal Reserve raised its benchmark interest rate for the fourth time in 2018 by a quarter-point to 2.5% but lowered its projections for future hikes to two in 2019. Then there was a downward revision to third-quarter gross domestic product numbers (by a mere 0.1% to 3.4%) as business spending weakened. Amid such developments, there were escalating concerns over continued signs of economic slowdown in both Europe and China that many investors feared would ripple over into the US. For the record, all three key barometers ended in the red in 2018 with the Dow retreating 5.6%, the S&P 500 (-6.2%) and the Nasdaq Composite (-4%). It was the worst year for stocks since 2008 and only the second year the Dow and S&P 500 fell in the past decade.

Ironically, Wall Street also achieved a few feats in 2018. Both the Dow and S&P 500 broke an all-time record of 26,828.39 points on Oct 3 (Dec 31: 23,327.46) and 2,930.75 points on Sept 20 (Dec 31: 2,506.85) respectively. The Dow also surged 1,086.25 points at the close on Boxing Day, presumably as a year-end window dressing exercise – the first time the benchmark index ever ended on a four-digit note in a single day. But 2018 will be remembered for its extreme volatility. The VIX volatility index spiked while the CNN Business' Fear & Greed Index has been stuck in "Extreme Fear" throughout much of the year. The Dow has swung 1,000 points in a single session only eight times in its history, and five of those took place in 2018. Across the Atlantic, there is a high likelihood of Brexit triggering chaos in the UK with an adverse spillover effect on global financial markets.

Back in October, S&P Global Ratings warned that a "hard" Brexit would trigger a deep and lengthy recession in the UK – and the outlook increasingly points to such a no-deal scenario as the European Commission rolls out contingency plans and embattled Prime Minister Theresa May struggles to get the votes for the deal she negotiated.

LOCAL CHALLENGES

Back home, external concerns will continue to undermine investor sentiment in 2019 with the dearth of domestic drivers making it difficult for the Malaysian equity market to shine amid already pricier valuation vis-à-vis comparable developing peers.

Those uncertainties are further heightened by the volatility in crude oil prices (Brent crude closed 2018 at US\$53.80/barrel after touching a four-year high of US\$86.29/barrel on Oct 3), potentially weaker external sector and limited ability to pump prime domestically due to a commitment towards fiscal prudence. On the other hand, downside pressure on US economic growth stemming from waning fiscal stimulus and rising inflation, coupled with a potential reversal in the greenback's strength, could encourage the outflow of funds – potentially in the second half of 2019 – into Asian markets that boast stronger growth prospects, both in terms of economy and corporate earnings. Regardless of pricier valuation, foreign investors are poised to nibble selectively into undervalued blue chips and fundamentally solid big and mid-cap plays as the earnings growth is expected to gain momentum in 2020.





Kenanga Investors

Given the mixed signals, investors are advised to maintain a defensive view of the local equity market and probably pursue a bottom up strategy in 2019. Amid the anticipation of moderating growth for the Malaysian economy with minimal prospect of broad-based growth in the local stock market, an active management strategy with decent stock picking skill can spell success for investors. In the context of unit trusts, a little readjustment of one's portfolio, i.e. switching from an FBM KLCI index-linked fund to a small sector fund may just do the trick. This is given the spread between the FBM KLCI and FBM Small Cap is trading at levels not seen in more than five years, suggesting an attractive valuation for the small cap sector in comparison with the benchmark index.

After registering superior returns in 2017 (+15.9%), the local small cap sector had reversed all its previous gains by posting 34% losses in 2018 in tandem with a bearish sentiment that had impacted equity markets locally, regionally and globally. Above all else, a bluer sky can be expected in the days ahead with the government having lined up various measures to strengthen the nation's finances, and its structural reforms to address past shortcomings and boost competitiveness should be viewed in a positive light by investors.

Despite closing 5.91% lower at 1,690.58 points in 2018 (2017: 1,796.81) and posting a total foreign net outflow of RM11.65 bil (the largest yearly foreign net outflow since RM19.49 bil in 2015) as tracked by MIDF Research, the local bourse was Asia-Pacific ex-Japan's fifth best performer behind India's SENSEX (+6.02%), New Zealand's NZX (+4.92%), Jakarta Composite Index (-2.54%) and Sri Lanka's Colombo Stock Exchange All Share Index (-4.97%).

ENDS

Ismitz Matthew De Alwis is the executive director and CEO of Kenanga Investors Bhd and president of the Financial Planning Association of Malaysia (FPAM).



kenanga

Kenanga Investors

Article Source:

Focus Malaysia (12 January 2019)

columns

FocusM Jan 12-18, 2019

The deceptive trade conflict truce

- more cohesively to settle the US-China trade dispute
- Other challenges to a global equity market rebound in



If there is one wish the global investment fraterally has for 2019, it has to be for US president Donald Trump to act in a more gentlemanly manner in his decision-making process, particularly on issues with major global maser.

Last year witnessed how the eccentric behaviour of the leader of the world's biggest economy brought about numerous roller-

brought about numerous roller-counter risks time and algi-mater stees time and algi-across equily markets worklyshe. The glorial economic climate has been besieged with uncer-tainties of sorts in recent items with Trump's notarities in declara-ing a 'decopality' sp-day target conflict trace - his most recent market adverse stant. On Dec 1, the already singlish.

On Dec 3, the almosty singlish Down Jones Industrial Index rebounded 250 points soon after Throug and this Citisese conflier part 30 jumping agreed in a 90-stay consolire in the frade wer than weighted beavely on glotal stock market strine mid-2018. Sint the Joy was short-freed as Wall Street's enthusiasm for the US-China trade times varietised 24.

US-China trade trace variabled 24 hours later the Dow pinning of 700 points or 3.0% following Trump's costly tweet abeling introsel as a Trait's Man' in addition to the samptes and controversial arrest in Camada of Hunswel's chief financial officer Meng Warution at the behavior of US without like.

francial officer Meng Warnhouse at the behest of US mitherities. Perior to the truce, both economic garness had already been embredied in 16-16-14 counter, but he will be the membrane and the membrane with China reciprocaling every trade action installed by the US, i.e. by releasing last August 12 that of American goods worth the China reciprocaling and August 12 that of American goods worth USSo bil (collection in the August 12 that of American goods worth the China and to retaliation for Trump's plan to impose duties on US\$200 bil in Chinese imports.

Double-edged sword Given his reputation as a busi-nessman extraordinaire — the first initionaire president in the history - Tramp would be better off leveraging its bestness fair to rally economic growth, spread wealth or store prosperity across the since.

wealth or sture prosper to the globe. Instead, his key messages tend to circle around the usurp-ting of American wealth by deeign economic forces. Disching much



of the legicy of this predecessor intrack Oburna, the US has disessorbated fixed from the unmember. Trans-seath Partnership (TVP) which came that effect on the content powerhouses in the likes of Japan, Canada, Mexica and Australia.

In time with this "America.

of jajon, Cimani, Medoca and Australia.

In time with his "America Firm? agonda to shrinsk the US frande of unifar trade deals that sacrificed our prosperity," Promp-ies adormant in re-negolitating free trade agreements at all conts to safestard the US contently.

China aside, Trump has also waged trade wars on all fronts waged trade wars on all fronts with meighbours Mexico and Carnada a revised North American Free Trade Agreement was sealed on Nov 30 ja swell as the European Union potth whom Trump declared the scale of free Trump declared the scale of free

or at least managed with utmost precantion.

Record-breaking feats

In all fairness, Trump should not be familed as the sole protagonist for the under-performing global

for the under-performing global stock markets throughtant zook. On Doc 20, the Federal Reserve raised its benchmark interest rate for the fourth time in 2008 by a quarter-point to 2.5% but towered its projections for future filters to two in 2019. Then there was a downwent provident to

but nowered he presidents in the finite billion to boo in 2019. Then there was a downseard revision to third-quarter gross domestic product numbers by a more 0.0% to 1.4% as business spending seakened.

And such developments, there were escalating concerns over continued sighs of economic slowdown in both Europe and Chies that many investors foured would ripple over into the US.

For the record, all three key barounders ended in the red in 2018 with the Dow retreating 5.6% the Self 900-(4-20) and the Saday Composite (-4%). It was the worst year for stocks since 2008 and only the second year the Dow and Self 900 801 in the part decade.

Ironically, Wall Street also better to 300 kinds and 5.8% good \$1.000 kinds. The branch of the state of the

and 2,930.75 points on Sept 20 (Dec 3): 1,506.85) respectively. The Dow 200 surgiest 1,636.25 points at the close on isotroli Day, presimably as a year-ond window dressing exercise - the first time the benchmark index ever ended on a four-digit note in a single day.

ars't me the bondmark most vever ended on a barr-digitable in a striple drag. Bit Look will be remembered for its extreme volusibility index spited with the CNN institutes Four of Greed index has been shock in "Botterne-Fear" throughout much of the year. The Dobe has sweng (accoptants in a single session only organized throughout much of the striple of the striple in the striple in the single session only organized throughout much of the office to the striple in the single state in a night likelihood of serval trigger in the single striple in the UK with an adverse apiliower effect on global function in the single striple in the single striple in the single striple in the single striple was single striple warned that a "laure" striple warned that

Back in October, S&P Global statingle warned that a "hard" irrest! would trigger a deep and lengthy recession in the UK. and the outlook increasingly points in south a no-deal scenario as the European Commission rolls out-contingency puts and embodied irrime. Minister Theresa May struggles to giet the votes for the deal she negotiated.

limited ability to pump prime domestically due to a commit-ment lower in fiscal prudence. On the other hand, downside pressure on 15 economic growth stemming from waning fiscal stemming from wanting focus stimulus and rising inflation, compied with a potential reversal in the greenback's strength, could encourage the outflow of funds-potentially in the second half of 2019 - Into Asian markets that boast stronger growth prospects, both in terms of economy and corporate earnings, isogardiess of pricier valua-

segments of pricer valua-tion, foreign investors are potsed to mitrie selectively into under-valued tries chips and fundames-tally solid hig and mid-cap playe as the earnings growth is expected to gain momentum in

Chem the mixed signals, investors are advised to maintain a defense wires of the local entering market and probably pursue a bottom up strategy to cop.

Amid the anticipation of moderating ground for the Malayston comment with mixtural prospect of tread-based grounds in the second stock market, an active management strategy with

in the local stock transfet, an active management strately with decent stock picking skill can spell success for investors.

In the constead or not transfer, as this readplicament of one's portfolio, i.e. a settlething from an Fillia RCG trade. Filmed from the a small section found may just do the brick. This is given the grade abetween the Film KCG and Film Small Can be strated at least 1.

This is diven the spread between the Fank KLGI and Fish Small Cap is trading at levels not seen in more than five years, suggesting an attractive valuation five he small cap sector in comparison with the benchmark back.

After registering superior returns in 2007 (+55%), the local small cap sector had reversed all fix previous glains by poeting 4x%, loses in 2008 in tandem with a bearth a sentiment that had impacted equity market locally, regionally and globally.

Above all else, a thinar sky can be expected in the days should expect the sentiment of the sent that had been sentiment of the sent

deal fibre neglicitated.

Local challenges
lack herne, external concerts will
confilme to underratine investor
sentiment in 2009 with the document
of domestic drivers making it difficult for the Malaystan equity
market to strine smid already
prices valuation vis-3-4% control
prices visceric crusic
times developing neers.

Those uncortainates are further heightensed by the volatility
to crude oil prices silvered crusic
claimed 2018 at 1835;3.80 branel
after twoching is done-year high of
1838.6.9 branel on Oct. 3, potentially weaker external sector and eigh ned outflow of iM-nés the the largiest yearly foreigh net outflow since iMon, politif note, as tracked by MIDP kessearch, the local bearne was Acta-Pacific ex-players fifth best performer behind India's SENSEX (+6.02%), New Zealand's NEX (+6.02%), Jakarta Cormposite Index (-2.54%), Jakarta

How did the US stock markets fare in 2018?

MOEX	BND80 7/01#	SHOWER MERIN	N 1817	SEILING FROM SEWER HIGH
Dose Jorges	3337.45	-55%	257%	-134%
Rescied Composite	46538	-35%	252%	-184%
58/900	290685	-6.2%	19.4%	-148%