Overview

US
• The month started with some risk-off sentiment in global markets with a US drone strike on 3 January that killed a senior Iranian military commander, but dissipated over the next week as Iranian military retaliation did not result in any US casualties.
• Global risk-on sentiment resumed in the run-up to and following the signing of the US-China Phase 1 Trade deal on 15 January.
• In the third week of the month global markets swung back to risk-off mode and continued to the end of the month, as concerns grew on the seriousness of the coronavirus outbreak that began in Wuhan, China and spread to more than 20 countries and regions.
• By month-end the futures market had begun to price in a US Fed rate cut by as early as the 10 June FOMC meeting (at 65.6% probability on 31 January versus only 27.4% probability on 24 January), despite the US Fed maintaining a firmly neutral stance at its 29 January meeting where policy rate was kept unchanged.
• Advanced reading of 4Q2019 GDP at 2.1% annualized QoQ beat consensus expectation of 2.0% (3Q2019: 2.1%) as strong Net Exports due to contraction in imports contributed 1.48% to growth, masking weaker Personal Consumption contribution of 1.20% (3Q2019: 2.12%) and contracting Gross Private Investment for a third quarter in-a-row with contribution of -1.08% (3Q2019: -0.17%).

EU
• As expected, the European Central Bank (ECB) kept its Deposit Facility Rate unchanged at -0.5% and maintained net asset purchases at EUR20b a month at its 23 January meeting. The ECB still saw growth risks “tilted to the downside”, while inflation is expected to hover around current levels of 1.3% YoY (December 2019) but with expectations “ticked-up slightly” in the medium-term.
• The ECB’s strategic review was formally launched, also on 23 January to conclude by end-2020.
• Flash estimate for 4Q2019 GDP at 0.1% SA QoQ (3Q2019: 0.3% SA QoQ) significantly disappointed consensus forecast of 0.2% SA QoQ; dragged down by unexpected contraction from Italy and France, but with likely expansion from Germany which releases its 4Q GDP number later.

Malaysia
• Bank Negara Malaysia (BNM) cut policy rate by 25bps to 2.75% on 22 January 2020, surprising consensus expectation of policy rate remaining unchanged. BNM states that the cut is “a pre-emptive measure” which we see as signaling flexible policy stance, although with a dovish bias.
• Headline foreign reserves printed at USD103.7b at 15 January 2020 (31 December 2019: USD103.6b), continuing to rebuild since end-November 2019 providing some resilience for the ringgit against speculation.
• External trade performance for November 2019 disappointed expectations with trade surplus of RM6.54b (consensus expectation: RM11.00b, October 2019: RM17.33b) with export growth contracting -5.5% YoY (October 2019: -6.7% YoY) and import growth contracting -3.6% YoY (October 2019: -8.7% YoY).
• Industrial Production (IP) growth normalized in November 2019, at 2.0% YoY (consensus expectation: 1.1% YoY) after dip to 0.3% YoY in October 2019. In general, IP YoY growth remains in a declining channel that it has been in since 2Q2018.
Equities

GLOBAL EQUITIES

The market uptrend continued into early 2020 on stronger-than-expected economic data readings from the US and China. While sentiment turned cautious on rising global tension, risk-on momentum returned as concerns over the US and Middle East tensions receded. The rally in the market was also supported by the signing of Phase 1 trade deal between the US and China as well as positive corporate earnings releases.

Sentiment, however turned negative following the outbreak of coronavirus, triggering a sell-off in the equity market, on uncertainty over its impact to Chinese and global economy. Initially identified in Wuhan City, China in Dec 2019, the virus was carried abroad by residents and visitors, spreading across 28 countries and had the World Health Organization declare a global health emergency on 30 January 2020.

Dow Jones Industrial Index slipped 0.99% in January while Euro Stoxx 50 Price was down by 2.78%. The weaker economic data coming out during the month from Germany also contributed to the negative sentiment.

Brent crude oil price dropped 11.9% MoM to close at USD58/bbl on fear of coronavirus outbreak.

ASIA PACIFIC EQUITIES

More impact was felt in the North Asia equity market, with Hang Seng Index declining by 6.66%. Shanghai Stock Exchange Composite Index fell by 2.41% as market was closed for Lunar New Year. Taiwan's TAEIX Index and South Korea’s KOSPI Index depreciated by 4.18% and 3.58% respectively as concerns over disruption to global supply chain following extension of the Lunar New Year holiday break unsettled investors.

Investors have turned risk-off on concerns over falling growth on the back of the coronavirus outbreak. We are staying defensive with investments tilting towards big capitalization and high dividend stocks which tend to be more resilient, while selectively position into stocks with strong fundamentals and stable year-on-year earnings growth to add value to the performance.

ASEAN EQUITIES

ASEAN equities were not spared from the global market sell-down, ending the first month of 2020 with a 5.5% MoM decline in US Dollar terms. All ASEAN markets closed the month in the red with the Philippines suffering the most as it slumped 8.2% MoM in US Dollar terms. It was followed by Thailand (-8.0% MoM) and Indonesia (-4.8% MoM) while Vietnam was the least hit, down 2.7% MoM followed by Singapore (-3.6% MoM) and Malaysia (-3.8%). With the exception of Rupiah (+1.6% MoM), other ASEAN currencies closed weaker against the US dollar. Thai baht was the worst performer, depreciating by 4.9% MoM followed by the Singapore dollar (-1.4% MoM) and the Philippines peso (-0.5% MoM).

Meanwhile, Malaysian ringgit and Vietnam dong closed only marginally weaker against the greenback; both were down 0.2% MoM.

In terms of forward P/E multiples, Thailand remains to be the most expensive and is now the only ASEAN market trading above its 10-year mean at +1 S.D. Other ASEAN markets are now trading below their respective 10-year average P/E multiples amid the recent sell-down. Singapore (-1.2 S.D) continues
to be the cheapest in the pack, followed by the Philippines (-1.1 S.D), Indonesia (-0.6 S.D) and Malaysia (-0.4 S.D), while Vietnam (-0.1 S.D) is trading slightly below mean valuation.

We maintain our Neutral calls on all ASEAN markets with the exception of Vietnam on which we have an Overweight call given its strong growth and attractive country profile. As we expect the markets to continue to be volatile, we maintain our defensive stance and prefer defensive and high-yielding stocks. We will watch the development of the coronavirus outbreak closely to seek any opportunity to buy quality stocks that are undervalued while realizing profits on those we think have reached their potential.

MALAYSIAN EQUITIES

The KLCI started 2020 with a loss of 3.6% MoM, in tandem the weak regional market performance. The bearish sentiment was most prevalent in small cap segment where the FBMSC Index plunged 6.3% MoM.

The US Federal Reserve held its benchmark funds rate in a range between 1.5% to 1.75%. US 10-year treasury yield collapsed 41bps to close at 1.51%, causing slight yield curve inversion of 3bps against 3-month treasury yield driven by pessimism stemming from the coronavirus outbreak.

Foreign institutional investors made net purchase of RM100m worth of Malaysian equities in January 2020. Sector wise, property, plantation and energy were the worst performing sectors, dropping between 7.2 to 8% MoM. The healthcare sector benefited from the coronavirus outbreak to gain 9.8% MoM.

The top three gainers in KLCI components stocks were Top Glove (+24.5%), Hartalega and Press Metal; while the worst performing stocks were Petronas Chemical (-15.8%), Malaysia Airports and Genting Bhd.

**Strategy**

The year 2020 started off with high volatility, as the global markets were not only affected by the ongoing uncertainties but exacerbated by the coronavirus outbreak in January. The actual impact of the outbreak to the global economy will be difficult to quantify, but in the short term it will definitely make a dent on the already slowing global growth. Despite the ongoing uncertainties, Dow Jones continued to outperform the global markets as corporates in the US have been posting better-than-expected profits.

Although the local market registered a small positive in foreign fund flows in the first month of the year, the market performance was lackluster. Concerns related to the coronavirus outbreak have caused a sell down in the tourism and consumer related companies but was partially neutralized by the run-up in the gloves and healthcare players. Rolling into the month of February, all investors will be focused on the 4Q2019 results reporting season. We will reassess our alpha picks while searching for new ideas.

As we remain defensive, we believe the local market can show improvement in 2020 due to 1) recovery in corporate earnings due to the low base effect in the previous year and 2) after back-to-back lackluster performance of the past 2 years, there is a higher probability for the local market to make a comeback. Our sector preference remains in plantation, consumer (non-discretionary), oil & gas players involved in maintenance, selective construction and technology players and REITs.
Fixed Income

ASIAN BOND MARKETS

The Asian dollar high yield bonds’ pace of return accelerated for a second month in-a-row at 1.59% MoM in January 2020 from 0.88% MoM in December 2019, as global risk-on sentiment took hold premised on continued positive developments with the US-China Phase 1 Trade Deal (agreed in principle in December 2019 and subsequently signed on 15 January 2020). The Investment Grade space also saw a jump in positive return of 2.09% MoM from 0.21% MoM return in December 2019. By country, the top three gainers were the Philippines (+2.57% MoM), Malaysia (+2.47% MoM) and Indonesia (+2.44% MoM). For the month, all markets under our coverage saw significant positive return with Thailand (+2.28% MoM), Hong Kong (+2.10% MoM), Singapore (2.07% MoM), South Korea (+1.82% MoM), China (1.79% MoM) and India (+1.79% MoM).

Regional local currency sovereign bonds in US dollar terms registered significant gains, also benefiting from the trade deal driven risk-on flows out of DM to EM markets. Indonesia led the pack with a gain of 3.35% MoM followed by Malaysia at 2.73% MoM and with China-onshore and Thailand markets tying at third place with returns of 1.72% each.

While the risk-on DM to EM flows drove strong returns for Asian bonds for the month, the coronavirus outbreak and escalation that emerged at the end of the month is likely to be a drag on return into February and March. At present traders appear to be generally differentiating between economies that are more vulnerable to coronavirus-driven slowdown in activity and those that are more resilient. The 10Y govvies on Japan, Australia, Hong Kong, South Korea, Singapore, the Philippines and Indonesia were bearish for the week to 6 February 2020, while Malaysia, the Philippines, India, Indonesia and Thailand are bullish for the week. China’s 10Y govvies yields were bullish in this first week of February, likely on domestic risk-off asset reallocation flows.

The forex market remains subdued as the US further signals a weak dollar policy, with the Commerce Department finalizing new regulation allowing it to impose duties on countries with undervalued currencies without depending on the Treasury Department to make the assessment. In this risk-off period, the US dollar should remain subdued, while other hard currencies could see some strengthening bias.

However, the low-yield environment in DM markets should continue to mitigate strength in hard currencies and continue to provide resilience to Regional High Grade bonds in markets deemed less economically vulnerable to the current coronavirus outbreak.

MALAYSIAN BOND MARKET

Malaysian bond markets entered 2020 with positive momentum amidst the whirlwind of predominantly risk-off global headlines hitting the press during the first month of the year; and the ample liquidity ready to be deployed as the New Year started.

The assassination of prominent Iranian military leader, Qasem Soleimani, on 3 January was the first event that threw dampener on global markets’ optimism for improved trade and growth prospects. While further military escalation was eventually averted, the event served as reminder the wide array of factors that could rapidly roil the markets. The official signing of US-China phase-1 trade deal on 15 January and the commencement of Trump impeachment trial, were easily overshadowed by the escalation of the novel coronavirus outbreak later in the month.
With global growth prospects thrown into doubt again, risk-off sentiment resumed dominance, sending US Treasury yields falling. During the month, 10-year US Treasury yield fell all the way from ~1.90% to end the month at ~1.50%. Locally, MGS/GII markets continued the strength that had started in December, with yields in the long end falling >10 bps in the first few weeks of trading.

While major central banks (US FED, ECB, and BOJ) kept their respective policy rates unchanged, as widely expected; locally, BNM delivered a policy surprise.

On 22 Jan 2020, BNM announced a 25bp cut of the OPR from 3.00% to 2.75%, providing extra boost for the MGS/GII market. Although the rate cut had already been priced in previously, yields plunged 8-18 bps across the curve in the hours after the rate decision. Apparently the market does not see the “pre-emptive” cut a measure sufficient to stave off economic slowdown, but rather a confirmation of more dovish policy actions to come.

The bullish sentiment in the bond market was also reflected in the strong MGS/GII auction results, with the 7-year MGS, 15-year GII, and 3-year MGS garnering bid-to-cover ratios of 2.5x, 3.4x, and 2.2x respectively. Corporate bond issuance similarly received overwhelming demand from investors. Among the issuers that priced their bonds during the month, Aeon Credit Service (M) Bhd and Hong Leong Assurance Bhd, with respective RM500m and RM300m issue size, recorded bid-to-cover ratios of >8.0x and >5.0x respectively.

We maintain our bullish view on the bond markets. While the stellar performance in 2019 may not repeat, we note the appeal of bonds as an asset class amidst the brewing risks and uncertainty (both economic and political), and the vulnerability of late-cycle growth prospects. Meanwhile, we are also keenly aware of the factors that may send short-term setbacks to local bank markets, among which the FTSE Russell review decision due in March 2020.

**Strategy**

**Market Outlook**

While we did not expect an OPR cut at the January MPC, we had called for a rate cut in early 2020 and our funds were positioned accordingly with portfolio duration overweight against benchmark. Moving forward, market conditions still point towards sustained bullish market conditions with flushed domestic liquidity, lack of new primary bonds supply and a strengthening Ringgit to attract higher foreign inflows. Economic growth concerns and benign inflation will continue to keep interest rates low and bond yields supported.

**Portfolio Duration**

We are maintaining duration overweight relative to benchmark as liquidity in the market remains ample and yields are not expected to spike up sharply. Due to growth concerns arising from the coronavirus in China and its impact on the global economy, market is gradually expecting BNM to cut the OPR by another 25 bps in 2020.

**Security Selection**

Our strategy remains ie overweight duration vs benchmark with focus on Corporate bonds for yield pick-up. In view of the sharp compression on government bond yields, we will trade on government bonds on relative value along the yield curve and anticipation on any steepening or flattening.
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