Date: 5 October 2024

NAVIGATING GLOBAL MARKET LANDSCAPE

StarBiz 7 (BizWealth, 5 October 2024)

As global markets face unprecedented challenges and opportunities, several key themes are shaping the investment landscape. In this column, we explore these themes and their implications for investors worldwide.

What are the current key themes driving the markets today, both globally and regionally?

We see four key themes driving the markets today.

Theme 1: Slowdown in US growth and rising unemployment.

The US economy, which has shown resilience in recent years, is now expected to face slower growth. US gross domestic product (GDP) growth is projected to decelerate from 2.5% in 2024 to 1.7% by 2025, driven in part by weakening labour market conditions. Rising unemployment will likely reduce consumer spending and corporate investment, which could weigh on corporate earnings and lead to greater market volatility.

Nonetheless, consensus still expects a soft landing in the United States, as household balance sheets remain healthy and the recent Federal Reserve (Fed) cut of 50 basis points (bps) should help offset any slowdown in growth.

Theme 2: Interest-rate down cycle and Fed easing. The Fed has recently shifted from a period of rate hikes to the start of an easing cycle, with a 50 bps cut already implemented. Market expectations suggest that interest rates could further drop to around 3% by the end of 2025, down from the current 5%.

This easier monetary policy could change the investment landscape, benefitting sectors such as bonds, housing (as mortgage rates fall) and long-duration growth stocks. Additionally, emerging markets (EMs) are likely to gain from capital flows redirected due to the narrowing interest-rate differentials.

China remains a significant factor in the global market outlook. As US rates fall, EM central banks also have more room to cut their own rates with lesser concerns over currency depreciation, providing an additional boost to these economies.

Theme 3: China's stimulus and economic rebound.

The Chinese government has recently rolled out a series of stimulus measures, signalling its intention to do more to support the economy. For now, these include rate cuts, liquidity injection, easing of housing policy and measures to support the equity mark. While these steps alone may not be sufficient to guarantee a sustainable rebound, they are important in signalling a more aggressive supportive stance by the government.

Given the Fed's easing of monetary policy, the People's Bank of China now has more leeway to ease with lesser worries of currency depreciation. Hence, more aggressive actions may follow. Overall, further stimulus and a rebound in Chinese economic activity could be positive for the global economy.

Theme 4: Technological growth, particularly in AI.

Outside of traditional macro- economic factors, the rapid development of artificial intelligence (AI) is a significant theme driving markets.

The race to build AI infrastructure, including data centres, is benefitting tech companies which include the Asian supply chain. Firms involved in the supply chain, such as semiconductors, memory and software, are likely to see increased demand as AI adoption accelerates globally.

How are factors like inflation, central bank policies and geo- political tensions impacting investor sentiment, especially in South-East Asia, and what sectors do you believe will benefit the most from these trends?

EM investors have long anticipated the loosening of monetary policy by central banks in developed markets (DM), given normalising global inflation. The expansion in liquidity means potentially more money flows into EM, thus generally improving currency values against the US dollar and lifting asset prices.

However, as evidenced by the reaction to the Fed's 50 bps rate cut in September, market optimism is tinged with caution as investors also assess risks of a global economic slowdown and geopolitical tensions, such as those from the Middle East conflict or the upcoming US elections.

Given this backdrop, in the near and medium term, we see beneficiaries in companies that are domestically focused, are net importers (benefitting from a stronger ringgit against the US dollar) and/or are rate-sensitive via leverage. This includes sectors like consumer, finance, construction, property, utilities and healthcare.

That said, in the longer term, we still see trade diversion beneficiaries as winners of the structural supply chain diversification and offshoring trends, particularly in the industrials, technology and manufacturing sectors.

Given the current market environment, where do you see the best investment opportunities?

We think South-East Asia is in a sweet spot now. After the Fed started its rate-cut cycle, more funds have been flowing into EMs, especially South-East Asia.

The region's currencies had been under pressure since the Fed rate-hike cycle in 2022 due to the wide interest-rate differential. However, the start of the Fed's rate-cut cycle has narrowed the interest-rate differential with South-East Asia, which boosted inflows into these markets and led to the currencies' appreciation against the US dollar.

The South-East Asian region is generally viewed as a domestic consumption play and is less leveraged to the US growth sector (i.e. technology). It has also benefitted as a foreign direct investment (FDI) destination on trade diversion from China due to US-China trade tensions.

Hence, this region is a defensive play on the back of a potential US economic slowdown. Sectors that could generally benefit from fund inflows and/or lower interest rates include banking, construction/infrastructure, property, real estate investment trusts, telecommunications and utilities.

How should investors approach asset allocation in this economic climate? Should investors focus on diversification across asset classes or geographic regions?

Diversification is always the key for successful investing and an essential part of risk management. In a lower interest rate and slow growth environment in the United States, investors tend to focus on bonds, defensive stocks, EMs, commodities and aforementioned sectors.

How do you view the potential risk of recession in DMs and could that spill over into Asean?

We view the risks of a DM recession as controlled but real. Investors are paying close attention to the US labour data, as softness in headline unemployment has emerged since early 2024. Indeed, current markets price in as much as ~30% recession probabilities for both the United States and the European Union over the coming year.

If there is a DM recession, Asean cannot escape some impact as it is both a net exporter to, and net FDI recipient from, DM. However, increasing robust- ness in Asean's economies means that growth may be more sheltered and resilient than the rest of the world. For example, during the global financial crisis when the United

States recorded -2.6% GDP growth in 2009, Asean managed to maintain a positive figure of +1.5%.

Are there specific sectors that look overvalued or particularly vulnerable?

In the United States, while the tech and healthcare sectors might look expensive on a headline basis, we think this is justified due to high earnings growth and improved prospects from the adoption of AI (for the tech sec- tor). Additionally, the recent correction in this space has also brought valuations down to more reasonable levels.

What role does environmental, social and governance (ESG) play in your current investment strategy?

We integrate ESG considerations into our investment process and decision-making framework. We believe that by managing both the opportunities and risks associated with ESG factors, we can generate better long-term returns and build resilient portfolios for our clients.

Beyond financial performance, we recognise our responsibility to drive positive social and environmental impact, ensuring that our investments contribute to a more sustainable future, along- side delivering value to our stakeholders.

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Source:

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Navigating global market landscape

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LEE SOOK YEE
Chief investment officer at Kenanga Investors Bhd

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■ Markets driven by expected US slowdown, interest-rate downcycle, China's rebound and AI growth

■ South-East Asia is in a sweet spot with sectors such as banking, property and utilities to benefit

■ Strengthening Asean economies suggest their growth may be more resilient than the rest of the world

How are factors like inflation, central bank policies and geopolitical tensions impacting investor sentiment, especially in South-East Asia, and what sectors do you believe will benefit the most from these trends?

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This advertisement has not been reviewed by the Securities Commission.

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