

# MARKET COMMENTARY

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## CONTRIBUTOR:

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Short term volatility aside, we envisage a more benign equity environment going into the second half of 2016.

We remain cautious but yet optimistic that any weakness in the equity market may present us with opportunities to build on our equity position.

## OUR HOUSE VIEW

### Stability, the Product of US Normalization No More?

- The incremental consensus view for US Fed rate hike this year has come down from four to two, possibly less? Hopefully, the market shifts away from this fixation on interest rates. While the US economy has not picked up as much traction as anticipated, recessionary concern is also not likely.
- Market volatility has been accentuated by large moves in currencies, making equity investors pay undue attention to their economic impact and that of corporate earnings. Our view is that a more stable economic environment will lend stability to Asian currencies, allowing economic and corporate fundamentals to come to the fore.
- As concerns over US Fed rate hike eased, Korea Central Bank has moved to cut interest rate. We expect fellow Asian Central Banks to follow suit. The combination of easier monetary conditions and fiscal stimulus should help support Asian economies.
- The Malaysian Ringgit went from the best-performing emerging Asian currency in the first quarter of 2016 to the worst this quarter. We view that the Ringgit to remain volatile in the short-term. Thus, we are still maintaining our cautious stance in relation to the market overall direction.



CARTOON BY: HEDGEYE

## PERFORMANCE OF KEY INDICES

FIGURE 1

	AS AT 31.05.16	1 MTH (% change)	YTD 2016 (% change)	PER 2016
D. JONES	17,787.2	0.1	1.0	16.8
NASDAQ	4,948.1	3.6	-2.3	30.0
DAX	10,262.7	2.2	-4.5	20.7
KLCI	1,626.0	-2.8	-4.0	18.1
USD / MYR	4.13	5.7	-3.8	-

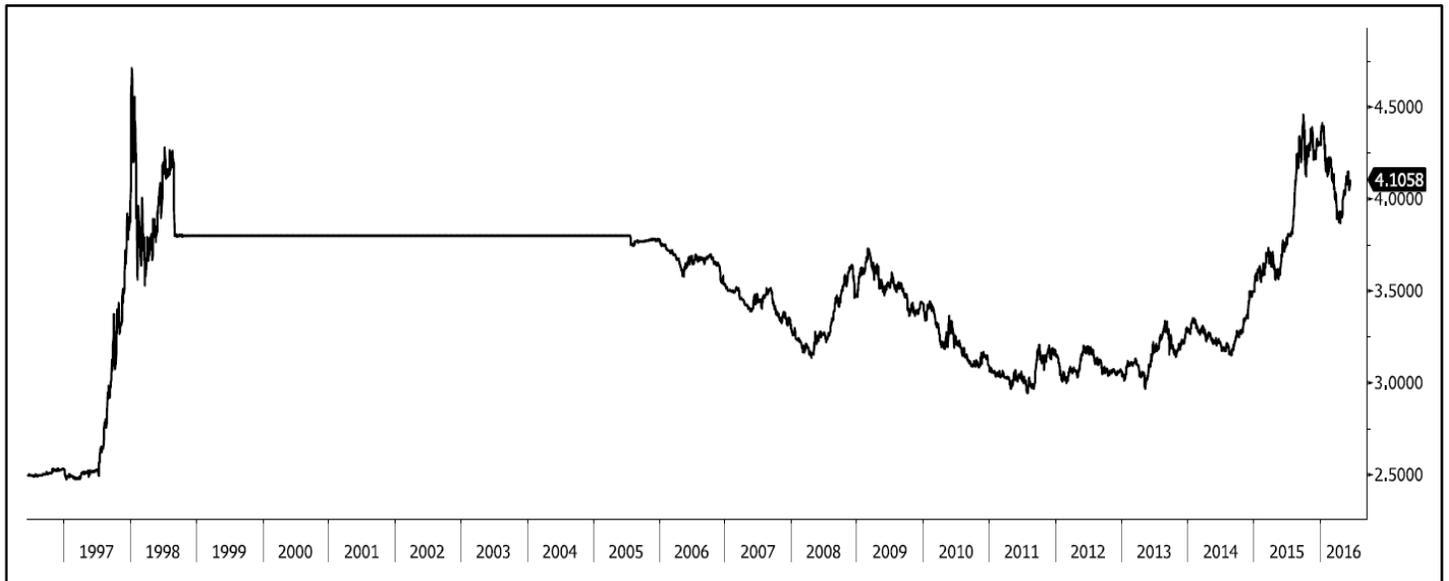
SOURCE: BLOOMBERG (AS AT 31/05/2016)

## REFOCUSING ON FUNDAMENTALS

### Entering a Period of Ringgit Stability?

In the last year and a half, many equity investors, including ourselves, have become fervent ‘currency readers’. As a result, the equity market exhibited huge swings and rotational positioning between US Dollar strength beneficiaries (e.g. exporters who sell their products in US Dollars) and Malaysian Ringgit strength beneficiaries (e.g. domestic oriented industries that benefit from cost savings) as macro positioning triumphed over specific corporate fundamentals.

**FIGURE 2: USD/MYR X-RATE (1996-2016)**



SOURCE: BLOOMBERG (AS AT 13/06/2016)

The Malaysia Ringgit may be primed for short term volatility amid US Fed’s hawkish tone and BREXIT risks. However, our view for a stable Malaysian Ringgit emanates from our view (read cover page) of a more benign global economic environment in the second half of 2016, and consequently, a more stable currency outlook as well.

The justification for a stable Malaysian Ringgit extends beyond the relative argument that the US Dollar strength may have ran its course but also premised on what we observed to be improving domestic conditions.

### What Drives Our Ringgit View!

In numerous issues of our newsletter, we have repeated highlighted that in the short-term, the Malaysian economy remains vulnerable to a phase of slower growth. Nonetheless, it is also our view that the Malaysian Ringgit movements have also been overtly driven by unprecedented political turmoil and the country’s tenuous capital position.

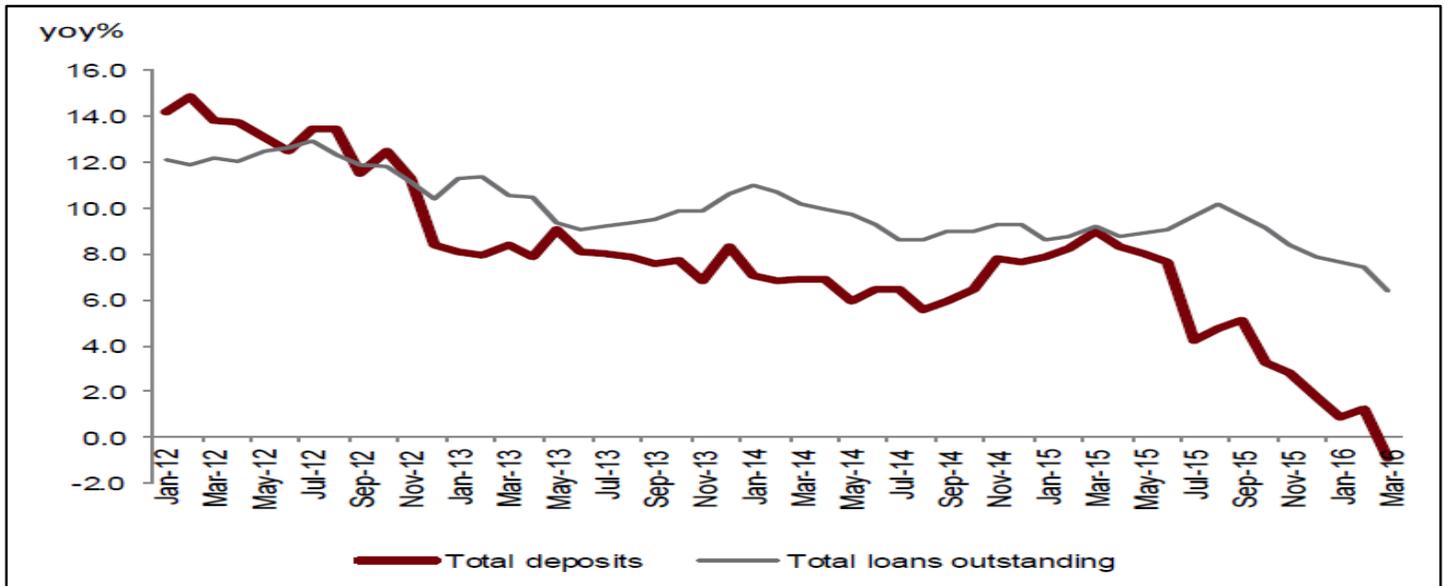
As political uncertainty eased (evidenced by BN’s dominance at the recently concluded Sarawak state elections), the debt burden from 1MDB removed (the sale of power assets and Abu Dhabi’s guaranteed step-in on interest payments for 1MDB debt), and an improved fiscal position from the recovery in oil price (budgeted at USD 30-35 per barrel against the current market price of USD 50 per barrel), the issues pressuring the Ringgit are no longer the thorns in the flesh.

### A Range Bound Malaysian Ringgit; Not Necessarily A Bad Thing

We expect the Malaysian Ringgit to trade in a band. This is not a bad thing considering the heightened volatility we have experienced in recent times.

We have laid out the positive factors (see above) that set the floor for the Malaysian Ringgit. On the flip side, we also see limited upside for the Malaysian Ringgit as we anticipate the possibility of an interest rate as well as what we evidenced by opportunistic capital shift out of the country on any recovery in the currency (total deposit growth has been on a declining trend since March 2015 coinciding with the period when the Malaysian Ringgit started to unravel).

**FIGURE 3: TOTAL DEPOSITS DECLINED YOY**



SOURCE: BANK NEGARA MALAYSIA

### **Strategy For Second Half 2016**

Our strategy has remained largely unchanged through the course of the year to date. Rather than following the momentum of herd investing and risk getting whipped-sawed, we remain fundamentally focused, paying particular attention to quality companies with industry leading positions and strong management track records.

Our two key themes for the portfolio are (1) Shariah beneficiaries and (2) domestic consumption names with growth potential. Please refer to our Newsletter Issues 6 and 7 for the complete stories.

### **SELECTED HOLDINGS**

**FIGURE 4**

STOCKS	BLOOMBERG TICKER	PRICE (RM)	PER 2016	EPS (\$) 2016	GROWTH (%) 2016	P/BVPS 2016	DY (%) 2016
TAKAFUL	STMB MK EQUITY	3.90	18.31	0.21	11.52	4.24	1.90
SPRITZER	SPZ MK EQUITY	2.33	11.65	0.20	20.48	1.40	2.16

SOURCE: BLOOMBERG CONSENSUS DATA (AS AT 14/06/2016)

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