Principal®

Market Commentary October 2021

In alliance with CIMB

Global Outlook

Global markets retreated in September 2021 with developed markets having declined more than the Asia-Pacific bourses. Among the markets that outperformed in September were Japan 4.9%, India 2.7%, and Indonesia 2.2%. The United States (U.S.) and Europe bourses declined by 4.8% and 3.4% respectively. Bond indices performed lower by -1.4% to -1.8%.

The U.S. Federal Reserve (Fed) Chairman indicated that quantitative easing (QE) tapering could start towards the end of 2021. It was stressed that there is no direct link between tapering and the timing of interest rate hikes, with the latter assessed on substantially more stringent criteria. Market is now expecting the U.S. 10-year bond yields to end 2021 at 1.50-1.80% after the latest news flow.

We continue to prefer Asian equities on a long-term basis with focus on quality companies that are long term winners or benefit from structural changes in their respective industries through market share gain. We also prefer companies with pricing power to overcome cost pressures and quality growth companies.

General outlook of the two capital markets: Fixed Income & Equity

Region: Developed economies

1. Our view – neutral.
2. PMIs (Purchasing Managers' Index) in the U.S. and European Union (E.U.) continued to remain above 60, which indicates the positive outcome of greater vaccine roll-out, re-opening of economies and large stimulus packages. .
3. The Fed indicated that QE tapering could start towards the end of 2021. It was stressed that there is no direct link between tapering and timing of interest rates with the latter assessed on more stringent test.

1. Our view – positive.
2. PMIs in the U.S. and E.U. continued to remain above 60, which indicates the positive outcome of greater vaccine roll-out, re-opening of economies and large stimulus packages.
3. Remain Overweight on U.S., E.U. & Japan.

Region: Regional (Asia-Pacific ex-Japan)

1. Our view – neutral.
2. Pockets of opportunity in local Asian currencies and Chinese credits as yields remain relatively attractive.
3. We forecast Asian bonds to provide a return of 3.25% to 3.75% in 2021.

1. Our view – positive.
2. Asian economies especially China & North Asia continued to post healthy data which would translate into actual growth.
3. Portfolios are positioned for cyclical recovery and long-term growth drivers such as financials, e-commerce, internet of things, cloud computing and electric vehicles.

Region: China

1. Our view – neutral.
2. Net supply of bond in July 2021 declined to RMB360 billion from RMB480 billion the month before. Excluding financials, the overall trend indicated the private sector has held up better than the State-Owned Enterprises (SOEs).
3. The default rate in July 2021 rose to 1.41% from 1.39% the month before. It was driven by a medium size private developer defaulting its repayment.

1. Our view – neutral.
2. The manufacturing PMI for Sept 2021 dropped to 49.6 from 50.1 the previous month while the Non-manufacturing PMI recovered to 53.2 from 49.6 in Aug 2021. This is owing to the resurgence of COVID-19 cases in the period.
3. The Chinese Communist Party (CCP) Politburo meeting in end July, highlighted the that current growth is unbalanced and yet to solidify. This is likely a signal of the end of the current policy tightening cycle.

Region: Domestic (Malaysia)

1. Our view – neutral.
2. Based on the potential of yield curve steepening and wider credit spreads in the fourth quarter of 2021 owing to primary market repricing, we are defensive on risk taking. Cash holding could increase.
3. Portfolio duration is maintained at 1.05x. Private credits are preferred over government bonds. Names with stronger fundamentals and liquidity are preferred.

1. Our view – positive.
2. Corporate earnings (excluding glove companies) remained on the recovery path with 2022 growth projected at 20%.
3. We turn positive on Malaysia owing to the easing of the movement control order which has paved the way for various sectors to be reopened. The sectors we prefer include financial, consumer discretionary, basic materials and selective transport and technology.

Our Strategy

We continue to prefer equities over fixed income.

Tactically we would like to recommend an increase in exposure to funds that are focussed on developed markets. This is to participate in the earlier hard re-opening of their economies by developed economies (vis-à-vis emerging economies) as they were able to vaccinate at a faster pace and contain the spread of COVID-19.

The market remained cautious over China after two highly indebted property companies missed payment on their bonds. This came after policymakers announced regulatory changes that impacted the technology, education, and food delivery industries. The divergence in performance between large cap stocks and small and mid-cap stocks in China, nevertheless, continued with the latter outperforming the former. We have a positive view on China's new economic direction and the benefits to earnings.

Note that income is integral for a well-diversified portfolio. In short, investors are advised to focus on:

- Diversifying across the themes of renewal, revitalise and recovery.
- Growth, quality and income while tactically complementing with cyclicals and value.
- Maintaining long-term focus as the next economic upcycle is about to unfold.

Our Fund Options

1. Universal Funds

Low

Risk Scale	Fund Options
Conservative	• Principal Islamic Money Market Fund
Mildly conservative	• Principal Lifetime Bond Fund • Principal Islamic Lifetime Enhanced Sukuk Fund • Principal Islamic Lifetime Sukuk Fund • Principal Islamic Global Sukuk • Principal Lifetime Enhanced Bond Fund
Moderate	• Principal Lifetime Balanced Income Fund • Principal Islamic Lifetime Balanced Fund
Mildly aggressive	• Principal Asia Pacific Dynamic Income Fund • Principal Asia Pacific Dynamic Mixed Asset Fund • Principal DALI Global Equity Fund • Principal Global Real Estate Fund
Aggressive	• Principal Global Titans Fund • Principal Global Millennial Equity Fund • Principal Asia Pacific Dynamic Growth Fund • Principal Greater China Equity Fund • Principal China Direct Opportunities Fund • Principal Greater Bay Fund

High

2. Islamic Funds

Low

Risk Scale	Fund Options
Conservative	• Principal Islamic Money Market Fund
Mildly conservative	• Principal Islamic Lifetime Sukuk Fund • Principal Islamic Global Sukuk Fund
Moderate	• Principal Islamic Lifetime Balanced Fund • Principal Islamic Lifetime Balanced Growth Fund
Mildly aggressive	• Principal DALI Global Equity Fund MYR • Principal DALI Asia Pacific Equity Growth Fund • Principal Islamic Asia Pacific Dynamic Income & Growth Fund
Aggressive	• Principal Islamic Asia Pacific Dynamic Equity Fund • Principal Islamic Small Cap Opportunities Fund

High

3. EPFMIS Universal Funds

	Risk Scale	Fund Options
Low	Conservative	• Principal Islamic Money Market Fund
	Mildly conservative	• Principal Islamic Lifetime Enhanced Sukuk Fund • Principal Islamic Lifetime Sukuk Fund
	Moderate	• Principal Islamic Lifetime Balanced Fund
	Mildly aggressive	• Principal Asia Pacific Dynamic Income Fund • Principal Titans Income Plus Fund
High	Aggressive	• Principal Global Titans Fund • Principal Greater China Equity Fund • Principal Asian Equity Fund • Principal Small Cap Opportunity Fund

4. EPFMIS Islamic Funds

	Risk Scale	Fund Options
Low	Conservative	• Principal Islamic Money Market Fund
	Mildly conservative	• Principal Islamic Lifetime Enhanced Sukuk Fund • Principal Islamic Lifetime Sukuk Fund
	Moderate	• Principal Islamic Lifetime Balanced Fund
	Mildly aggressive	• Principal DALI Asia Pacific Equity Growth Fund
High	Aggressive	• Principal Islamic Asia Pacific Dynamic Equity Fund • Principal Islamic Small Cap Opportunities Fund

You may obtain a copy of the Prospectus/Information memorandum/Disclosure Document and its Product Highlight Sheet (if any) for the above-mentioned funds at our offices, distributors or our website at **www.principal.com.my**.

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