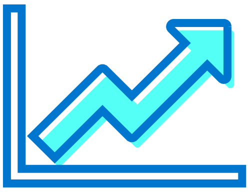
Principal

Market Commentary July 2022

In alliance with CIMB

Global Outlook



In June 2022, global markets dropped across board, with continued concerns over the possibility of a US recession and inflation outlook. During the month only the Shanghai Composite and Chinese H-shares listed in Hong Kong recorded an increase 6.7% and 3.4% respectively. Korea, Taiwan and the S&P500 posted the largest drop of 13.2%, 11.8% and 8.4% respectively. Bonds indices dropped ranging from 3.1% to 3.2% for the month.[1]

On the monetary policy front, it is likely that the central banks will refocus on the risks to growth, on top of the inflationary risks. The latest U.S. Federal Reserve (Fed) statement reinforced earlier guidance on interest rate trend to contain inflation. The Fed's balance sheet shrinkage started in June 2022 at a run-off rate of USD47.5 billion before projected to rise to USD95 billion in September.[2]

We turned slightly positive on Asian equities underpinned by China's re-opening and visible policy stimulus. We continue to focus on quality companies with earnings visibility, robust balance sheet, long term winners, market share gainers and with pricing power.

We remain neutral on equity markets for developed economies.

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

Region: Developed economies

1. Our view – least preferred
2. Developed Markets economic fundamentals remained sound with improving employment. There is downside risk to growth & earnings should geopolitical uncertainties persist.
3. The Fed reinforced guidance on interest rate trend and signalled balance sheet shrinkage started in June 2022.[2]

1. Our view – neutral.
2. Developed Markets economic fundamentals have shown signs of weakening. There is downside risk to growth & earnings should inflationary pressures persist.[3]
3. We remain neutral on the United States (U.S.), European Union (E.U.) & Japan on concerns over economic growth, inflation, higher interest rates and the geopolitical uncertainties.

Region: Regional (Asia-Pacific ex-Japan)

1. Our view – neutral.
2. Pockets of opportunities in local Asian currencies and Chinese credits as yields remain relatively attractive.
3. We forecast Asian bonds to provide a return of 4.00% to 5.00% in 2022.[4]

1. Our view – positive.
2. We added exposure to China underpinned its re-opening and visible stimulus policy.
3. We continue to focus on quality companies with earnings visibility, robust balance sheet, market share gainers and with pricing power.

Region: China

1. Our view – neutral.
2. Net supply of bond in April 2022 rose by 15% month-over-month (MoM) to RM318 billion. The jump in supply is driven by the private sector while the State-Owned Enterprises (SOEs) recorded a drop of RM24 billion.[3]
3. The default rate in April 2022 eased to 0.49% from 0.55% driven by State-Owned Enterprises (SOEs). The private sector default rate edged up to 3.9% from 3.8% the month before.[3]

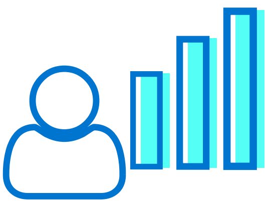
1. Our view – positive.
2. China has provided better visibility of its policy to support growth. In addition, the lockdown is being cautiously lifted to enable economic activities to resume.
3. The manufacturing PMI (Purchasing Managers' Index) for June 2022 recovered to 50.2 from 49.6 while the Non-manufacturing PMI rose to 54.7 from 47.8 previously. The rebound reflected the impact from the cautious re-opening by China.[5]

Region: Domestic (Malaysia)

1. Our view – neutral.
2. Bank Negara Malaysia (BNM) raised the Overnight Policy Rate (OPR) by 25 basis points (bps) to 2.25% in July 2022. S&P Global Ratings revised Malaysia's outlook to stable from negative previously.[6]
3. Portfolio duration is revised to 1.10x +/- 0.20 from 1.05x +/- 0.20 previously. The move is to take advantage of potential yield falling in anticipation of stronger market support. Still prefer credits over government bonds.

1. Our view – neutral.
2. We continue to adopt a balanced approach between value and growth while having sufficient diversification.
3. We still prefer consumer discretionary, and commodities but turned cautious on commodities. We are also relooking at financials and technology after the recent sell-off.

Our Strategy



We maintained our Neutral recommendation for developed markets. This is owing to concerns over geopolitical tensions, inflation, and economic growth on the back of rising interest rates. Within bonds, we prefer local and regional to global developed market fixed income. We are mindful of the various risk scenarios that are developing and are focused on ensuring that our portfolio construct has a sensible risk profile.

We turned slightly positive on Asian equities. This is supported by China's move to loosen the lockdown and allow economic activities to resume. In addition, Chinese policymakers have announced highly visible stimulative measures to support growth. Markets are likely to be focused on quality firms with unique growth drivers, pricing power and reasonable valuations. China and ASEAN offer such ideas that can do well regardless of broad market performance.

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

- Be aware of risks to ride out volatilities arising from geopolitical tensions, policy normalisation, inflationary issues and Covid19 variant.
- Focus on quality growth offered by the developed markets and seek value opportunities within the Asia-Pacific region.
- Position for sustainability themes including renewables, alternative energy, and food sustainability.

Our Fund Options

1. Universal Funds

Low → High

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 Fund • Principal Lifetime Enhanced Bond Fund
Moderate	• Principal Lifetime Balanced Income Fund • Principal Islamic Lifetime Balanced Fund
Mildly aggressive	• Principal DALI Global Equity Fund • Principal Asia Pacific Dynamic Mixed Asset Fund • Principal Asia Pacific Dynamic Income Fund • Principal ASEAN Dynamic 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

2. Islamic Funds

Low → High

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

3. EPFMIS Universal Funds

Low → High

Risk Scale	Fund Options
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
Aggressive	• Principal Asian Equity Fund • Principal Greater China Equity Fund

4. EPFMIS Islamic Funds

Low → High

Risk Scale	Fund Options
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
Aggressive	• Principal Islamic Asia Pacific Dynamic Equity Fund • Principal Islamic Enhanced 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**.

Sources:

[1]Bloomberg, 30 June 2022

[2]Federal Reserve Board, 4 May 2022

[3]JP Morgan, 31 May 2022

[4]JP Morgan, 5 July 2022

[5]S&P Global, 30 June 2022

[6]Bank Negara Malaysia, 6 July 2022

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