6 - 10 January 2025

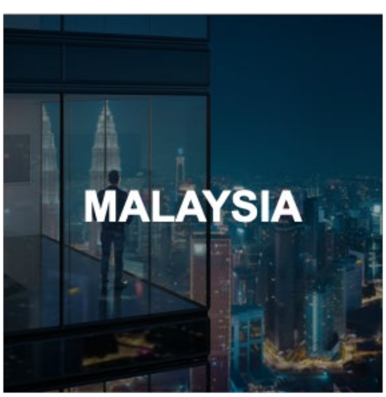
WEEKLY MARKET REVIEW

A brief on global markets and investment strategy

Key Highlights

- The S&P 500 declined by 1.94%, driven by stronger-than-expected U.S. jobs data, with non-farm payrolls adding 256,000 jobs and unemployment falling to 4.1%.
- The ISM Services Index highlighted inflationary pressures in the service sector, reinforcing concerns about tighter financial conditions.
- The Biden administration's proposal to restrict high-end NVIDIA chip exports to Tier 2 nations, including China, heightened uncertainty in the tech sector.
- Treasury yields surged, with the 10-year U.S. Treasury yield rising to 4.77%, strengthening the U.S. dollar and dampening risk sentiment across global markets.

- The MSCI Asia ex-Japan Index fell by 1.85%, with Chinese tech stocks declining after Tencent and CATL were added to the U.S. military-linked entity list.
- Despite Tencent and CATL denying military ties, the designations fueled investor caution and dampened sentiment amid rising geopolitical tensions.
- Market participants remain cautious ahead of the National People's Congress (NPC) in March, where potential economic stimulus measures are anticipated.



- The KLCI Index declined by 1.66% last week amid broader regional pullbacks and U.S. policy concerns impacting the tech sector.
- The US proposed data centre restrictions could challenge Malaysia's ambition to be a regional data hub, though ongoing hyperscaler projects remain unaffected.
- The Johor-Singapore Special Economic Zone (JS-SEZ) agreement was signed, marking a milestone for bilateral economic collaboration.
- Penang's RM10 billion Mutiara Line LRT project was officially launched, enhancing connectivity and boosting investment potential in the region.

Global & Regional Equities

The S&P 500 declined by 1.94% last week, reflecting a weak start to the year across global markets. The broad-based decline was primarily driven by external factors, particularly stronger-than-expected U.S. jobs data, which pushed the 10-year U.S. Treasury yield close to 4.77%. The sharp rise in yields weighed heavily on both emerging and developed markets, impacting multiple asset classes and contributing to investor caution.

The December non-farm payrolls report highlighted the resilience of the U.S. labour market, with 256,000 jobs added—significantly exceeding market expectations of 165,000 and surpassing November's 227,000 increase. Job gains were broad-based, with contributions from the healthcare, government, retail, and leisure and hospitality sectors. Additionally, the unemployment rate declined by 0.1% to 4.1%, defying expectations of a stable reading of 4.2%.

Wage growth provided mixed signals: the year-over-year increase slowed to a three-month low of 3.9%, suggesting some easing, but the monthly increase was firmer than anticipated, indicating persistent stickiness in labour costs. This data reinforces concerns about inflationary pressures, particularly in the service sector.

The ISM Services Index further added to inflationary concerns, with stronger-than-expected service sector activity. The rise in the "prices paid" component highlighted ongoing inflationary pressures, dampening market hopes for near-term rate cuts. The combination of robust employment data and rising service sector prices contributed to a steepening of the U.S. Treasury yield curve, with longer-term yields rising sharply. The stronger U.S. dollar and softening equity markets underscore growing concerns among investors about tighter financial conditions.

Geopolitical developments also added external pressure on markets. The Biden administration's proposal to restrict exports of high-end NVIDIA chips to Tier 2 nations—countries not allied with the U.S.—dampened sentiment in the tech sector. This policy aims to limit access to advanced computing technology, primarily targeting nations such as China and Russia. However, the broader scope of the policy has raised concerns about its impact on emerging markets like Malaysia and India. Consequently, tech stocks faced renewed selling pressure, weighing on portfolio returns for some technology-related assets.

Despite ongoing volatility in equity markets, we maintain a positive outlook on the fixed income space due to attractive yields. The 10-year U.S. Treasury yield has risen to 4.77%, reflecting a 55 basis point increase since the end of December and 17 basis points year-to-date. At current levels, we see value in the 3- to 7-year segment of the yield curve, where government bonds are offering yields of approximately 4.3%.

With near-term rate cuts largely priced out, markets are now only pricing in one potential rate cut as early as June 2025, with another projected for 2026. This cautious outlook suggests that while inflation remains a concern, the opportunity to lock in attractive yields within this segment of the curve provides a compelling case for selective exposure to high-quality fixed income assets.

Global & Regional Equities *(cont')*

In Asia, the MSCI Asia ex-Japan Index declined by 1.85%. Apart from the impact of rising U.S. Treasury yields, another key driver of the decline was renewed concerns around China. The U.S. Department of Defense added Tencent Holdings and Contemporary Amperex Technology Co., Limited (CATL) to its list of companies allegedly linked to China's military, causing a sharp selloff in Chinese tech stocks. Tencent's share price, in particular, dropped by around 10% following the announcement, while CATL—a global leader in EV battery manufacturing—also saw a decline in its share price amid increased market anxiety.

Although the designation is largely symbolic, with no immediate operational impact on either Tencent or CATL, it has heightened geopolitical tensions and cast a shadow over investor sentiment. Tencent has denied supplying any technology to the Chinese military and stated its intention to appeal the decision in hopes of being removed from the list. CATL has similarly distanced itself from any ties to the Chinese military, emphasizing its focus on global partnerships with automakers such as Tesla and BMW.

On the outlook for Chinese markets, we expect trading activity to remain subdued until after the National People's Congress (NPC) meeting in March, where more details on potential economic stimulus measures are expected to be announced. Additionally, both market participants and the Chinese government appear to be adopting a cautious stance, waiting to see how U.S. policy toward China evolves amid ongoing geopolitical tensions.

Given the current environment of elevated Treasury yields and lingering uncertainty, we believe that Chinese equities are unlikely to see significant upside in the near term. China equities expected to stay range-bound until there is greater clarity on both U.S. policy direction and domestic stimulus announcements.

Updates on Malaysia

The KLCI Index declined by 1.66% last week, reflecting cautious sentiment amid regional pullbacks.

The most significant market-moving news was the Biden administration's proposal to restrict server capacity for Tier 2 and Tier 3 nations, including Malaysia. According to The Edge Malaysia, the restrictions aim to limit AI computing power for nations like Russia and China but have broader implications for Malaysia's growing data centre sector.

Ongoing data centre projects by hyperscalers such as Google and Microsoft are expected to remain unaffected. However, future expansion pipelines could face headwinds, impacting the sector's long-term growth prospects. Companies may need to secure "Validated End User" (VEU) status by meeting stringent U.S. security and compliance requirements to access higher computing power. Without effective mitigation, the restrictions could challenge Malaysia's ambition to become a regional data centre hub.

Updates on Malaysia *(cont')*

In domestic news, the Johor-Singapore Special Economic Zone (JS-SEZ) agreement was officially signed last week, marking a significant milestone. The JS-SEZ will consist of nine flagship zones, each specialising in key sectors. For instance, Johor Baru City Centre will focus on finance, while Pengerang will continue as a key oil and gas hub. The government also announced a RM28 billion infrastructure fund to support the development of critical projects within the zones, aiming to bolster economic growth and attract investments.

Another notable event was the official groundbreaking of the Penang Mutiara Line Light Rail Transit (LRT) project. This RM10 billion initiative marks Penang's first rail-based transit system. Spanning 29.5 km with 21 stations, including a provisional stop at Penang South Reclamation Island-A (PSR-A), the Mutiara Line aims to enhance connectivity, stimulate high-value investments, and foster new industries. The market largely anticipated this development, resulting in muted reactions to related thematic plays.

Portfolio cash levels increased slightly last week, although we remain highly invested. We also took profits in the construction and utilities sectors to lock in gains.

Fixed Income Updates & Positioning

The credit primary market had a robust start last week, with year-to-date issuances in the APAC US dollar space reaching approximately USD 30 billion. We actively participated in a diverse range of deals across markets.

In the US dollar space, notable issuances included Hong Kong Airport Authority, CLP Power Hong Kong Limited, a China State-owned Enterprise (SOE), Dai-ichi Life Holdings, Inc., and China Hongqiao Group Ltd, a Chinese aluminium producer. In the Australian dollar space, we took part in Australia and New Zealand Banking Group's (ANZ) Tier 2 issuance. In the euro market, we were involved in Deutsche Lufthansa AG's bond deal, while in the Singapore dollar space, we participated in Saudi National Bank's issuance.

Performance-wise, credit spreads tightened across most issuances, reflecting healthy demand; however, prices have softened due to a broader rate sell-off.

In the secondary market, we executed portfolio rebalancing to create room for primary market allocations. This involved taking profit on select CNH (offshore Chinese yuan) positions and reallocating into US dollar bonds.

Additionally, we increased our exposure to Prosus N.V., the Dutch investment firm that holds a 24% stake in Tencent Holdings Limited, following spread widening to 6.4% after Tencent was added to China's Unreliable Entity List by the US Government. This designation imposes restrictions on companies' critical imports and exports. While the restrictions were anticipated, the announcement heightened investor caution, initially causing Prosus bonds to weaken before staging a partial

Fixed Income Updates & Positioning *(cont')*

recovery. Interestingly, Tencent bonds demonstrated greater resilience compared to the company's equities, with spreads widening by 15 basis points immediately after the news but narrowing to 5 basis points by the end of the week.

Back home, the local bond market remained supportive last week despite movements in US Treasury yields. The 7-year Malaysian Government Securities (MGS) stood out as the sole exception, with its yield rising by 3 basis points (bps) to 3.79% due to new supply. In contrast, the rest of the benchmark curve either remained unchanged or declined by 2 bps. Notably, most of the buying flows came from domestic players, particularly the banking sector. By the end of last Friday, the 3-year MGS was at 3.45%, the 10-year MGS stood at 3.82%, and the 30-year MGS was steady at 4.18%.

The first government bond auction of the year saw a robust response. The 7-year MGS benchmark auction recorded a bid-to-cover (BTC) ratio of 2.8 times for an issuance size of RM 5 billion. Incoming bids totalled RM 14 billion, significantly surpassing the 2024 average of RM 10 billion for 7 to 10-year tenors. We participated in this issuance, reflecting our confidence in the demand dynamics.

Looking ahead, the upcoming 15-year Malaysian Government Investment Issues (MGII) auction will have a total issuance size of RM 4 billion, with RM 3 billion available for public markets and RM 1 billion privately placed by Bank Negara Malaysia. We anticipate strong demand from domestic institutional investors, given the attractive long-duration offering.

From a technical standpoint, with a fiscal deficit target of 3.8% for 2025, the gross government bond supply is expected to decline to RM 164 billion compared to the RM 175 billion issued in 2024. Additionally, total maturities for the year are projected to fall to RM 84 billion, down from RM 93 billion in 2024. This reduced supply is expected to remain supportive of the market, particularly given sustained demand from domestic institutional investors.

Foreign funds continued to pare down their holdings in Ringgit-denominated bonds for the third consecutive month in December, with a monthly outflow of RM 1.4 billion. This brought the total fourth-quarter outflow for 2024 to approximately RM 14 billion. However, for the full year of 2024, foreign inflows remained positive at RM 4.8 billion, although significantly lower than the RM 23.6 billion inflow recorded in 2023. By December 2024, foreign holdings in MGS stood at 32.3%, a drop from 34.4% at the end of 2023.

Our current portfolio duration ranges between 4.8 years and 6 years. We have been gradually buying into the secondary private debt securities (PDS) market to add exposure by taking a selective approach.

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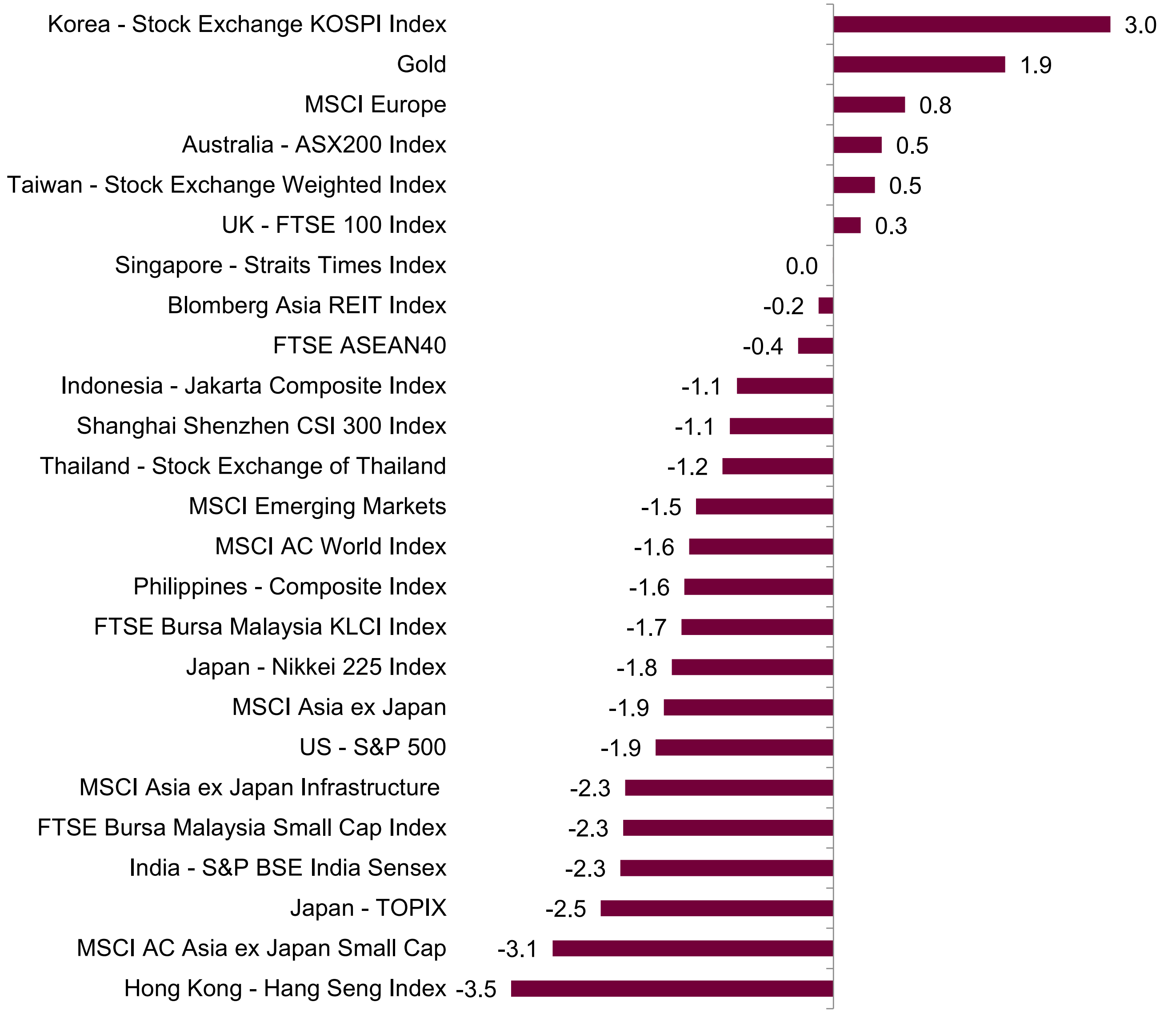
Index Performance | 6 January – 10 January 2025



Index Chart: Bloomberg as at 10 January 2025. Quoted in local currency terms.