# Fund managers on investment themes for the second half

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Fund managers share their views on what they think are the investment themes for the second half of this year:

**Gan Eng Peng**

Head, equity strategies & advisory

Affin Hwang Asset Management Bhd

**What would be some of your investment themes for the second half of 2016?**

Clearly the global economic growth environment has become anaemic. Sentiment is weak and cautious across the board. Despite easy and cheap money globally, capitalist animal spirit is missing.

Such conditions make equity investing difficult. Equity investing depends highly on growth, the lack of which limits its upside. On the other hand, cheap money has propped up all financial assets valuations, making things expensive even in the context of slow growth.

Our strategy to navigate such a low growth low rate environment is to anchor a large portion of the portfolio into resilient cashflow high dividend stocks. This strategy benefits from further interest rate cuts and capital gains are made from yield compression.

When markets are flat to downward biased, and poor economics create more disappointment, I think it makes sense to have more concentrated holdings. The more positions you own, the higher your chances of getting hit. More positions mean more unintended risk taking. Hence, besides our core dividend income strategy, we run a concentrated stock selection where only intended risks are taken. This also makes sense in an environment of high valuations and limited stock selection choice – we should buy more of what we like when we find them.

Specifically for Malaysia, we think the following themes are worth keeping an eye on:

1. We continue to like yield driven stocks as discussed. This constitutes 30%-40% of our portfolios. When we buy yield stocks, we are looking for those that some semblance of growth, which is the primary driver of capital gains. Hence returns come from yield compression, the actual yield, and capital gains on the growth.

2. The anaemic economic condition in Malaysia is likely to lead to an interest rate cut in the later part of this year. Malaysia has one of the higher rates among developing Asian countries. We think it will join the rest of Asia in dropping rates. This is of course good for yield stocks.

3. We will be keeping an eye out for the PNB group of companies. Potential change in leadership there could lead to restructuring of long underperforming assets.

4. We do not think the syariah segregation of EPF monies will have a big impact, but this needs to be monitored in case the take-up for syariah funds are stronger than expected. If that is the case, it will create further syariah stocks premium.

5. After Pan-Borneo Highway contracts for Sarawak, we think it will move towards the Sabah leg, with its own set of beneficiary companies.

6. The by-election results and implosion of opposition parties could lead to talks of early general election in 2017.

7. The rise of the massive Bandar Malaysia project as more details are released. This project, if it takes off, will change the property landscape of the Klang Valley for the next decade.

**What sort of stocks would you look at?**

Our strong cash flow yield strategy has led us to quite a few utilities and infrastructure stocks, which is their basic characteristic. We have positioned a large portion of our portfolio into yield stocks to benefit from potential yield compression.

The balances of the portfolio are being run on a concentrated basis on higher conviction ideas.

We also have various exposures to Bandar Malaysia construction beneficiaries, companies that could benefit from Pan Borneo Sabah contracts and PNB group of companies.

**What are the issues that will continue to mar the second half of the year?**

On the global front, the balance of slow growth versus rising rates continues. As long as this balance is maintained, markets can continue to chug along. If growth becomes too weak, markets could sell off. If it becomes too strong and rate expectations comes back strongly again, markets will also sell off. How this pans out will also determine US dollar strength and hence emerging market foreign flows.

Brexit is a clear and present danger for global markets.

The rising popularity of president-elect Donald Trump and his controversial policies will shake markets

Unwinding of hedge funds due to redemption has driven many market returns in the first half of 2016. This was due to short covering of their positions. We believe Malaysia was one of the beneficiaries. This trend needs to be monitored further for its impact.

**Will returns be hard to come by again?**

The investing world is clearly settling on a lower standard of returns for all asset classes. Low growth low rates and high valuations just do not allow strong returns to be generated without taking excessive risks.

Markets are driven by growth and positive forward expectations, the lack of which curtails its upside.

Domestically, we think there are limited catalysts to drive the market beyond 5% from these levels. Ample investment liquidity and willingness to support it also means the market is unlikely to fall in a big way.

**Is volatility the order of the day? Will returns be bifurcated or concentrated, say only on the big caps?**

Markets are volatile as it is a discounting machine. Markets are a function of future expected events – growth, risks, rates etc. When the outlook is murky, gyrations become common as scenarios changes frequently. Combined with tons of liquidity in the system and efficient information flow, fund flows exaggerate the situation further.

The key attribute for investing in the above environment is about quick adaptability. Macro conditions changes and strategies and portfolio positioning needs to change with it quickly. Failing which, portfolios get hurt and left behind.

**Do you foresee more inflows into bonds or equities in this part of the world?**

Emerging market flows has been weak. It is also inherently hard to predict. We keep an eye on it for its impact on markets but do not use it as a predictive tool for future market directions.

**Bashar Al Natoor**

Fitch Rating's global head Islamic finance.

**What would be some of your investment themes for Islamic Finance for the second half of 2016?**

As we have expected, issuance from sovereigns has picked up early in the year and is now followed by banks and corporates. Various factors have supported this trend, such as the recovery in oil prices – although still on the weak side, along with declining Gulf Cooperation Council (GCC) sovereign reserves, liquidity in financial systems, and moves by issuers to tap the capital markets before the next Fed rate hike.

Bashar: 'We expect sukuk issuance to remain relatively strong in the second half of the year.'

We expect sukuk issuance to remain relatively strong in the second half of the year, based on the pipeline of deals and the potential for some governments to issue debt to make up for weak oil revenues. It is worth noting that the third quarter is likely to be quieter, due to the combination of the summer break and Ramadan. Overall our expectation is for 2016 sukuk issuance to at least match 2015 issuance.

**Any new development that will see more growth in Islamic finance?**

New sukuk laws in some countries should support issuance by helping to create a standardised structure and improving transparency. The trend of gradually increasing use of syariah-compliant borrowing as more countries create legal frameworks is likely to support issuance, and as issuers attempt to attract a broader investor base, including Islamic finance investors.

**Which regions will Islamic finance see futher progress this year?**

Islamic finance is systemically important in many jurisdictions, including the GCC and Malaysia and is growing in the wider regions of Middle East, Asia and even Africa, where there is significant potential and demand for infrastructure Islamic financing.

**Manu George**

Investment director, Asian Fixed Income

Schroder Investment Management (Singapore) Ltd

**What would be some of your investment themes for fixed income for the second half of 2016?**

We are seeing a cyclical improvement in the global economy but structural concerns, such as high leverage levels and weak productivity, remain. Secondly, uneasy policy truce appears to be at work among global central banks. Third, debt overhang sees policymakers sanction unconventional methods, such as negative interest rates in Europe, to boost economic growth. Fourth, emerging market differentiation is getting more pronounced with fragilities within political and fiscal arenas being exposed. Fifth, economies are awash with liquidity from central banks, but this is not translating to liquidity in financial markets and is therefore increasing the costs of investing.

Manu: ‘Our bias is to hold high quality countries and companies where yields have overshot fundamentals.’

**Will we continue to be in a position where returns are hard to come by again?**

We believe that with US rates still low, European and Japanese bond yields in negative or close to negative territory, the chase for attractive yield will likely encourage investors into emerging markets.

**Will we continue to see low single digit returns in emerging market fixed income in the second half of the year?**

We believe that emerging markets in general – both hard and local currency – are even more attractive today than two years ago. If risk sentiment continues to be positive, we anticipate that emerging markets could end the year with returns in the high single digits. However, a change in risk sentiment or a hawkish US Fed could make it more challenging for investors in the sector.

**Do you see more inflows into fixed income in emerging markets?**

We believe that with indications that the US Fed is likely to stay on hold in June and potentially July, investors will look to emerging markets as a source of opportunity to generate return and yield in their portfolios. So flows may improve in the coming months if the US Fed does not raise rates later this month.

**Do you see the spread widening in Emerging market foreign currency debt?**

We believe that a lot of the spread widening occurred during the second half of 2015 and the first quarter of 2016. So the likelihood of further spread widening will be a function of expectations of a US fed rate hike. This coupled with worsening credit conditions may impact spreads. However, we believe the market was priced last week for this and now looks cheap relative to the anticipated trajectory of the US Fed rate hike given the poor US employment numbers.

**Are you particularly underweight or overweight on any asset class for the second half?**

Our bias is to hold high quality countries and companies where yields have overshot their fundamentals. We tactically prefer Latin America over Asia given that Latin America sold off more than Asia. However, we still find attractive places to invest in the Asian region. Asia for us is generally a defensive allocation within the emerging market universe, and so we will tend to have allocations to select Asian countries where we anticipate further loosening of monetary policy which will benefit bond investors like us and to hedge our risk in the event that the market sentiment turns bearish.

**YVONNE TAN**

General manager, investment services

Eastspring Investments Bhd

**What would be some of your investment themes for the second half of 2016?**

The second half of 2016 will likely be another period of volatility, starting with the US FOMC meeting in June, Brexit referendum on June 23, the higher possibility of a US rate hike and the uncertainty surrounding the US presidential race.

Tan: ‘With so much volatility expected, stick to the basic principles of investing.’

We are cautious on the market but remain on the lookout for any correction to add good fundamental stocks with strong and sustainable business models, healthy balance sheet, management with good track record and preferably with a decent dividend yield. Domestically, depending on the outcome of the upcoming by-elections in Selangor, it may be a pre-cursor to an early general election in 2017.

**What sort of stocks would you look at?**

Stick to the basic principles of investing, with so much volatility expected, and hence uncertainty to follow, stock picking will be the key.

We like companies with strong and sustainable business models, healthy balance sheet, management with good track record and preferably those that give decent dividend yield.

**Will returns be hard to come by again?**

With the level of volatility, and the many variables and outcomes investors have to consider, returns will be harder to achieve.

**I understand we are still in an environment of low interest rates. That has caused a rally in our bond market. Do you see this trend continuing?**

Market expectations are that the US Federal Reserve will resume hiking rates in the near to medium term, although at a gradual pace. Fed chairman Janet Yellen has made public statements in recent weeks reiterating that the Fed funds rate will need to be raised gradually.

However, market expectations on the timing of the first hike have recently been pushed to late 2016. On the domestic front, in its meeting on May 19, Bank Negara stated that the current level of the OPR was appropriate and supportive of the economy but it noted downside risks in the global economic and financial environment and was monitoring their implications to the local economy. –