## Principal Islamic Asset Management (Ireland) (PLC)

# Islamic ASEAN Equity Fund

I Class August 2023

## Market Review

The Dow Jones Islamic ASEAN was lower this month -2.97% mom, reversal from last month's strong performance. The weaker market performances were seen across markets - Singapore (-7.24%), Philippines (-6.56%), Malaysia (-3.92%), Indonesia (-2.53%) and Thailand (-0.33%), and. Notable macro developments were:

1) Singapore's July manufacturing PMI continued to edge higher from 49.8 in July to 49.9 in August - still contractionary but suggesting stability. July headline inflation further eased to 4.1% yoy from 4.5% yoy and 5.1% yoy, in June and May respectively. While core inflation also ended lower at 3.8% yoy from 4.2% yoy last month. Singapore's GDP print ended at 0.5% yoy in 2Q23, marginally higher than 0.4% yoy in1Q23. MTI narrowed its forecast to 0.5% - 1.5% for full year amidst weak external outlook.
2) Indo's PMI continued to strengthen in August at 53.9 from 53.3 in July, marking the 24th month of expansion. Indonesia's headline CPI picked up again in August to 3.5% yoy from 3.1% yoy in previous month, while core CPI ended lower at 2.2% yoy, down from 2.4% yoy previously. August trade surplus reversed higher to $3.12b from $1.31b due to larger than expected drop in imports. BI kept policy rate unchanged at 5.75% and expects no further rate hike for the rest of the year.
3) Malaysia's August PMI was unchanged at 47.8 same as previous month - still contractionary as export orders fell. July headline inflation ended at 2.0% yoy trended lower from 2.4% yoy in June. While core inflation ended at 2.8% from 3.1% yoy in June. BNM kept OPR at 3.0% during the July MPC meeting and with no further hikes expected for the rest of the year as the current monetary policy stance is accommodative and remains supportive of the economy. The GDP forecast is expected to slow to 4.0-5.0% in 2023 but to accelerate again in 2024.
4) Thailand August manufacturing PMI slipped into contraction to 48.9, after declining to 50.7 in July from 53.2 in June. August headline inflation ticked higher again to 0.9% yoy from 0.4% yoy in July, whilst core inflation ended lower to 0.8% yoy from 0.9% yoy month ago. BoT raised rates again by another 25bps to 2.25% in their August meeting. BOT is forecasting GDP growth to be at 3.6% in 2023 and higher at 3.8% in 2024. The government target for tourist arrivals to range between 25-30m foreign arrivals in 2023, still shy of 40m pre-pandemic.
5) The Philippine's August manufacturing PMI contracted to 49.7 from 51.9 previously, falling into contraction for first time in two years from slower demand. Headline inflation in August trended higher to 5.3% from 4.7% yoy in July from higher rice and fuel prices. While core inflation in August ended lower at 6.1% yoy from 6.7% yoy previously. BSP paused rates at 6.25%, with no further hike expected in 2023 unless inflation gets out of control. BSP expect inflation to average 5.6% yoy and 2.9% yoy for 2023/24. Trade deficit ended higher in July at US$4.20bn from US$3.94 in June as exports declined.

Malaysia, Thailand and Philippines reported weaker than expected GDP growth largely driven by external factors and slower government spending. Meanwhile, domestic consumptions remained quite resilient. There is a concern that inflation could make a comeback due to the rice export ban by India because ASEAN nations are major consumers of rice. Hence, the sharp sell down of Philippines Peso. Srettha Thavisin, a member of Pheu Thai, was officially endorsed by the King to be Thailand's 30th Prime Minister. The coalition consists of 10 parties with 314 seats and pushed Move Forward Party as opposition. Whilst Malaysia concluded their 6 states election with a status quo results.

For the month of August, consensus earnings were revised upward in Philippines and Indonesia driven by financials, whilst Malaysia saw a downgrade largely due to commodities and healthcare related.

Foreigners turned net sellers except for Malaysia equities. After the conclusion of the 6 states election, Malaysia market saw buying interest from the foreigners, hence, we expect the same for Thailand market as well. USD rebounded after releasing stronger than expected inflation and GDP growth led to concerns of further tightness financial conditions. Phil Peso was hit the hardest (-3.00%), followed by Msia Ringgit (-2.83%), Thai Baht (-2.24%), Sing Dollar (1.60%) and Indo Rupiah (-0.98%).

## Fund Review

The Fund eased in August by -2.30% mom but performed better than the benchmark index which was down by -2.97% mom. For the month, at the country level, the outperformance was attributed by the stock selection in Malaysia and Thailand but Indonesia was a drag on performance. At the sector level the contributors to better performance were Consumer Discretionary, Staples and Industrials while the Materials sector in particular Vale Indonesia was the main detractor. Since the fund's inception, the Fund outperformed the benchmark by 6.17%.

## Portfolio Outlook and Strategy

Tight US Federal Reserve policies are offset by an increasingly supportive monetary and fiscal policies from China given the different economic conditions. It's now a consensus view that the US economy has a soft landing as economic growth and labor markets are faring better than expected. Positive news on US inflation means policy rates have peaked but could remain elevated into early 2024. The US consumers are resilient as employment is plentiful, the housing market is robust, and the equity market is strong. As such, the US economy is not slowing down fast enough to warrant a Fed rate cut. With higher Treasury issuance in 2H2023, we expect US monetary policy to remain relatively hawkish for the next few months. While it remains above the Fed's target of 2%, inflationary pressures are easing (July CPI +3.2% yoy) despite the strength of the economy.

China's policy stance has turned decisively dovish with actions to address the property sector, ease financial conditions and support private sector confidence. Mortgage rates were cut and downpayment ratios have been reduced. An urban renewal (called "Urban Village Renovation") program worth about 0.8-2.3% of GDP p.a. is expected to be announced. The PBoC has also cut lending rates, albeit by only 20bps this year. Local governments have also been encouraged to raise special bonds to facilitate repayment of arrears to private enterprises. Finally, regulatory headwinds against internet companies have abated. The challenge confronting China is not one of financial meltdown – as Government debt is reasonable vs global comparisons and credit remains available through state-owned financial intermediaries - but one of economic stagnation brought on by a crisis of confidence amongst individuals and corporates. As such, we will be acutely sensitive to Chinese policies which are pro-cyclical, bring forth tangible cash flow or monetary benefits to the private sector, and which encourage risk-taking and capital investments.

We expect moderate returns on risk assets for the remainder of 2023 but a more constructive outlook for 2024 - contingent on impactful, synchronous and broad policy actions over the next 6 months by China.

MSCI ASEAN corrected and is currently trading at 12.9x forward 12 months Price-to-Earnings Ratio, which is below the 5-year historical average of 14.3x

**Table 1: Foreign fund flows**

| FF Nett Flows (USD'mil) | Malaysia | Indonesia* | Philippines~ | Thailand | Vietnam^ | Total |
|---|---|---|---|---|---|---|
| Aug23 | 30.6 | (1,263.1) | (131.1) | (442.9) | (110.4) | (1,916.9) |
| YTD22 | (632.0) | (709.9) | (379.7) | (4,647.4) | (177.0) | (6,546.0) |
| 2009 - YTD23 | (5,992.3) | 6,719. 3 | 2,385.0 | (23,713.4) | 1,655.0 | (18,946.4) |

*[1] There were approximate inflows of $4 billion in 2019 due to BDMN acquisition by MUFJ and MAPA IPO.
*[2] There were approximate inflows of $1.4 billion in May 2020 due to Bank Permata acquisition by Bangkok Bank.
^ A consortium led by KKR invested $650 million of Vinhomes in June 2020.
~ KKR acquired $192 million stake in First Gen Corporation in late June 2020 and JERA bought $1.58 billion stake in the Aboitiz Power.

*Source: Bloomberg*

We believe ASEAN equities continue to provide investors a combination of recovery plays and long-term structural themes. Hence, we have adopted a barbell approach of cyclicals and growth. As reopening progresses further in ASEAN, we focus on quality companies in cyclical sectors such as financials, consumer, real estates, and tourism-related sectors, for sustained recovery backed by positive long-term growth outlook, with sustainable dividend yield as an added positive. We also continue to like structural growth themes of ASEAN internet and technology & supply chain shift, with a focus on quality growth companies at reasonable valuation. Our strategy continues to aim to capture these ASEAN opportunities of strong fundamentals, taking advantage of the volatilities of external global market sentiments.

# Risk Considerations

Investing involves risk, including possible loss of principal. Past Performance does not guarantee future return. All financial investments involve an element of risk. Therefore, the value of the investment and the income from it will vary and the initial investment amount cannot be guaranteed.

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