GLOBAL MACRO DEPARTMENT
SOUTH EAST ASIA REGIONAL MARKET REPORT

NUS INVESTMENT SOCIETY

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Abstract

Poised to be the next emerging market region, Southeast Asia has shown great promise in the recent times. On a holistic view, with facets of political stability, strategic diversification in industrial sectors, coupled with rich and vast natural resources, along with a highly favorable geographical location - Southeast Asia is slowly becoming a top-notch hub for companies to move their operations to.

As such, this section seeks to delve deeper into the broad-market outlook of this region, with focus set on Singapore, Malaysia and Indonesia. Synergizing macro-economic theories, technical analysis and recent events & news, we aim to critically analyze the situation as it is today, and how it would be in the near

Singapore

Economy in Brief

Singapore is a highly trade-oriented economy. As a member of many regional, multilateral and bilateral free trade agreements, Singapore's total exports and imports exceeding 3 times that of its annual Gross Domestic Product (GDP) and amounting approximately to a combined sum of 1 trillion in Singapore Dollar. Besides export trades, Foreign Direct Investment (FDI) inflow has been another significant driver of its economy due to its low-corruption, pro-business and low-tax environment. Given its small population and lack of natural resources, Singapore purchases many of its raw goods externally and considers human resource as a vital issue for its economic development. Consequently, the Singaporean economy is highly sensitive to external shocks, especially to its key trading partners.

News & Events

China Market Crash, Economic Slowdown and Yuan Devaluation

China is Singapore's largest export partner and hence activities in China has a substantial impact on the Singaporean economy. In 2015, 3 major events occurred.

China has experienced double-digit growth rates for many years but this is set to change with the Chinese leadership implementing new economic reforms to restructure the economy to be more reliant on consumer spending and services. After quarters of slowing growth, China's GDP growth was said to be 6.9% for Q3 2015, the first time it broke the 7% level since 2009. While the accuracy of this data may be questionable, weak industrial and investment data certainly supports the notion that China is experiencing an economic slowdown.

With a slowing economy, Chinese consumers experience lower income growth and hence are more likely to cut back on spending, inclusive of those on foreign imports. From Singapore's perspective, a decrease in exports demanded by China would have a detrimental effect on its growth. Additionally, with China attempting to reposition its economy, it creates serious questions about Singapore relying on Chinese demand as a long term driver of economic growth.

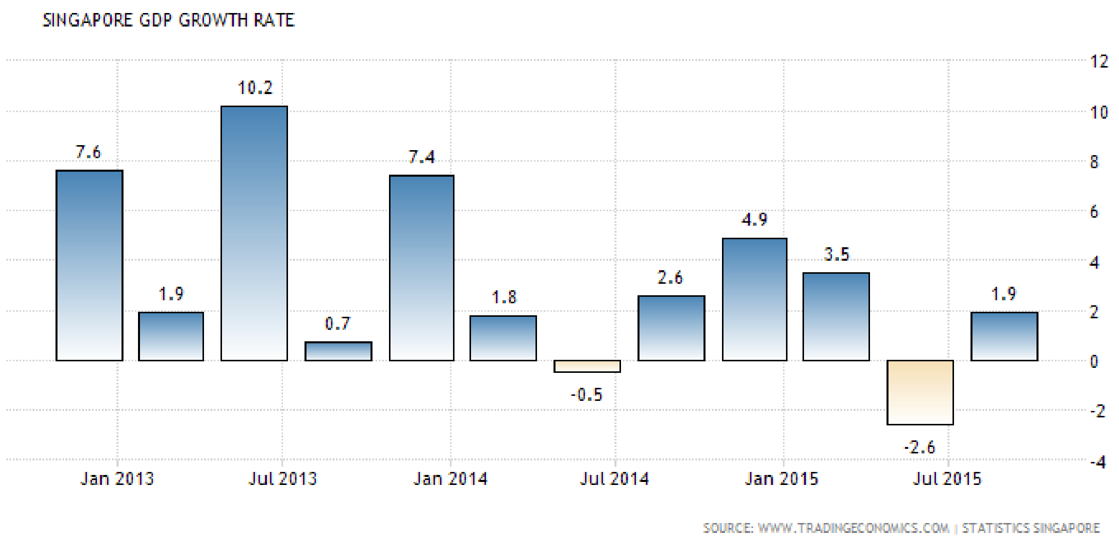

Figure 1: Singapore Q3 GDP YoY Growth Rate

As can be seen, the China economic slowdown has played a huge part in the sluggish GDP performance of Singapore this year (Figure 1), with manufacturing contracting for successive quarters and construction and services both slowing.

Another huge event that occured in 2015 was the Chinese stock market crash. Encouraged by easy borrowing, Chinese retail investors poured money into the stock market, driving the Shanghai Stock Index up 150% in the span of less than a year. However, the spike was independent of fundamental strength and created a huge bubble that popped on 12th June 2015 (Figure 2).

Figure 2: Shanghai Class A Index - The Rise and the Fall

Despite the Chinese government's aggressive counter-measures, the stock market would go on to lose more than 40% of its value to wipe out the year's gains. However, despite the gloom of the Chinese stock market, the Straits Times Index (STI) was less adversely affected, sliding about 5% from 12th June to 11th August (before the devaluation).

The less significant impact of the Chinese stock market crash was due to the fact that foreign share of the Chinese stock market was a paltry 1.5% and hence there was unlikely to be a direct impact on Singapore portfolios. Nonetheless, the market crash still did hit investor confidence and portrayed a grim outlook of future economic prospects which caused the decline.

The most significant event, however, was the double surprise devaluation of the Yuan. The People's Bank of China (PBOC) cut the Chinese Yuan by 1.9% on 11th August 2015 and again on 12th August 2015 by 1.6%. As a result, the STI gapped down by about 2% on the 12th August open and coupled with an already bearish market sentiment, would go on to slide by another 10% before rebounding (Figure 3).

A weaker Yuan relative to the Sing dollar causes Singaporean exports to be less competitive and attractive. With lower export levels to China, Singapore's biggest export partner, it would no doubt hurt Singaporean GDP and economic growth.

Figure 3: STI Performance in 2015

Key Forecasts

China has faced economic slowdown in recent years and with the Politburo dedicated towards shifting economy reliance towards consumer spending, the slowdown would likely continue into 2016 as China continues to go through the transition period. While the Singaporean government has every means of repositioning the economy in the long run to take advantage of this shift, this is less likely in the near future with Singaporean economic performance more likely to be closely linked to Chinese growth and hence demand. Should the Chinese economy continue to stutter, it is possible for Singapore's economy to continue to be sluggish.

As for the CNY/SGD relationship, Figure 4 below may be indicating an end to the uptrend. A double top pattern may be forming with the price twice testing the red resistance area but failing to move as high on the third, most recent, try. This gives rise to the possibility of a reversal which will cause relative strengthening of the SGD which would have a detrimental effect on Singaporean economy. While the Monetary Authority of Singapore (MAS), could easily counter the weakening of the Yuan with exchange policy of their own, they may not do so as it would be at the expense of higher interest rates. Resistance can be expected around 0.2260 while support can be expected around 0.2100 to 0.2120.

Figure 4: 1-Year Trend of CNY/SGD

As such, if the CNY/SGD does in fact move into a downtrend and Chinese economic growth continue to be sluggish as predicted, the Singaporean economy is likely to continue to struggle. Resistance for the STI may be found around 3153 while support may be found around 2738, at the depth of the downtrend at October 2015.

Malaysia

Economy in Brief

From an economy dominated by the production of raw natural resource materials, such as tin and rubber, Malaysia today has a diversified economy and has become a leading exporter of electrical appliances, electronic parts and components, palm oil, and natural gas. The dominant sector is services, which accounts for more than 50% of the GDP. The economy of Malaysia is the 3rd largest in Southeast Asia, after the much more populous Indonesia and Thailand. Malaysia's economy is one of the most competitive in the world, ranking 14th in 2015.

News & Events

Oil's Sharp Decline

Just a year ago in December, oil stood at above $70 per barrel. Fast forward to 2015 December, oil has lost over 50% of its value, standing at a 7-year-low. With Malaysia's economy heavily dependent on the export of oil, the tumbling of prices has thinned national income. With exports of oil amounting to RM87.6 billion (US$24.1 bil) per year, such plummeting has considerable detriment to the economy. Oil-dependent companies, of course, was hit the worst. Notably, one of the largest oil & gas company, Sapurakencana Petroleum Berhad dipped from a share price of RM 2.95 in early February to RM 1.78 in December, with many other oil companies following suit. The oil decline also brought about an adverse impact of the ringgit depreciation, which will be discussed further below.

Amidst the oil decline, the stock market undoubtedly was affected, with a broad-based sell-off during the period of stark and panic selling of oil in the months of May to late August, highlighting the significance of oil prices on the market sentiment of investors in Malaysia.

Figure 5: Kuala Lumpur Composite Index performance in May to September

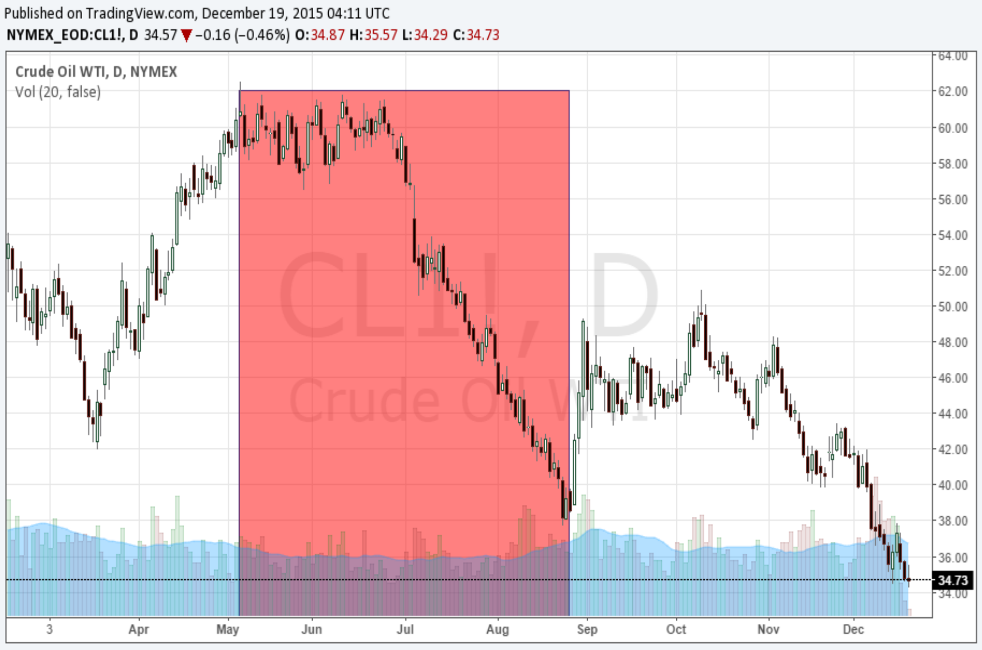

Figure 6: Oil prices in May to September

Ringgit Depreciation

The Ringgit depreciation has been so severe that it drew reminiscence of the Asian Financial crisis in 1998. Mirroring the oil price slump in May to August, the MYR/USD skyrocketed from 3.53 to an unprecedented 17-year high of 4.45 , a 25% depreciation in a short span of 4 months. Attributed to the falling oil prices, a weakening economy and growing political instability, the ringgit was subject to panic selling during these months.

Figure 7: Ringgit Depreciation from May to late September

1MBD and Political instability

Figure 8: Prime Minister Najb's saga on embezzlement of $700million USD

The polarization of Malaysia's political environment intensified recently, as both the Prime Minister and the opposition ramped up efforts to entrench their positions. In the aftermath of Wall Street's article on Najib embezzlement of $700 million, an atmosphere of mistrust looms over the political landscape - prompting and fuelling the peaceful demonstrations of Bersih 4.0.

Consequently, PM Najib Razak's government implemented security measures that strengthen both the roles within and the powers of the government and the National Security Council, of which Najib is the head - which many see it as a form of clinging onto more power and authority. Disapproval of the PM has spread since, even from the members of his own party, as on 7 December, the deputy leader of United Malays National Organization publically called for scandal-ridden Razak to step down.

Such political instability has caused many foreign funds to pull their investments out of Malaysia, in fear of riots breaking out and social unrest threatening business operations and property damage, further compounding on the downward spiral of the Ringgit.

Key Forecasts

KLCI

Figure 9: Technical Analysis on KLCI

In recent months of October to December, it seems to be a consolidation period - with prices loitering and moving between price levels of 1720 and 1620. With slight bias towards the downside, Relative Strength Index showing that price has been on the lower zone of 20 - 40, price action below 100 SMA (green line) and 50 SMA (red line), and the prominent presence of large down days, the slide is expected to continue if it breaches the near term support of 1620. Rallies have to close above the key zone levels of resistance at 1690 and 1740 for a signalling of a possible reversal above the "neckline" of a prolonged inverted head and shoulders pattern.

While short term rebounds can be expected, the macro-environment does not bode well for Malaysia. With oil prices continuing to decline, coupled with the ringgit depreciation expected to further deteriorate and the increasing uncertainty of political stability, investors, particularly foreign funds, will be more prudent in their selection of capital investment. The situation in Malaysia do not seem favourable. Constrained by the rise in interest rates in US, foreign funds are expected to flow out of the Malaysian market, causing a further spiral in the stock market in Malaysia - unless stimulus arrives to support the market (though highly unlikely due to the burgeoning Malaysia's external debt of RM700 billion). The focus next will be more on tangible assets such as gold, property and even, the USD - asset classes which are likely to lead the market next year.

Indonesia

Economy in Brief

Indonesia is the largest economy in South East Asia. Crude oil and natural gas are Indonesia has the largest economy in Southeast Asia and is one of the emerging market economies of the world. As of 2014, Indonesia's GDP in PPP terms was a staggering US$2.685 trillion. Its economy is eighth largest in terms of GDP (PPP), making it an extremely attractive place for businesses to thrive.

The industry sector is the economy's largest and accounts for 46.4% of GDP (2012). Naturally, Crude oil and natural gas are Indonesia's most valuable natural resources. Relying it as a major source of export revenue, their main trading partners are the United States, China, Singapore, Japan and South Korea. Another industry which plays a huge part is agriculture, which provides employment for more than 40% of the labor force.

News & Events

Impact of oil price decline

Decreased oil prices have resulted in lost potential revenue of almost 253 trillion Indonesian rupiahs, or $20.24 billion, in the 2015 state income projection. However, the lowered state projection for oil and gas production of 8% also accounted for this loss. In addition, the low price of crude oil will cause a decrease in Indonesia's export commodity prices. This trend will suppress revenue from Indonesian exports, as about 60% of Indonesian exports are in the form of commodities.

Interestingly however, the decrease of oil prices have encouraged the improvement of Indonesia's current account deficit. A Ministry of Trade press release on March 17 stated that "the export total for the month of February 2015 reached USD 12.3 billion while imports reached USD 11.6 billion. Therefore, a USD 738.3 million was achieved."

The fall in world oil prices encouraged the Indonesian government to recalculate the amount of subsidized fuel prices. In its new policy, the government revoked the fuel subsidy for premium fuel and provided a subsidy fixed at 1,000 rupiahs per litre for diesel fuel. This policy is considered a win-win option for the government and the public. With the reduction in fuel subsidies, the government can maximize its spending on productive sectors. On the other hand, the public can enjoy lower fuel prices, which move in accordance with the market price.

As a net importer of oil, Indonesia benefits from falling oil prices. This development provides an opportunity for the country to revise costly policies, such as the fuel subsidy system, and has provided a net benefit to the current account balance despite falling revenues from domestic oil production. Domestic laws, such as the constitutional requirement that the government set fuel prices, limit the scope for future ASEAN-wide cooperation on oil and gas. However, Indonesia's efforts to diversify energy sources, such as through increased biodiesel consumption, open the door to new avenues of cooperation. Though falling oil prices present a challenge to these initiatives, the economic viability of developing new and renewable energy should be ensured by providing attractive incentives. Continued efforts on diversifying energy resources are critical to Indonesia's energy and environmental security goals, and renewable energy and natural gas have important roles to play.

Indonesia's re-entry into OPEC

Many experts consider Indonesia's re-entry to be an unusual move as Indonesia is a net importer of oil and consumes almost double of what it produces, much unlike any other OPEC members.

However, it makes commercial sense for OPEC to invest in Indonesia from a long term perspective as Indonesia's demand for energy is growing faster than most of the other Asian economies. As OPEC members scramble hard to find new markets for its crude oil, Indonesia is slowly but steadily emerging as one of the hottest energy markets in Asia.

OPEC's decision to cut production

Despite favouring lower oil prices, Indonesia wouldn't oppose any call by OPEC to cut crude production "as long as [they do not] get cut," the country's OPEC Governor Widhyawan Prawiraatmadja said in an interview in Jakarta on Tuesday. "We are new, we like to listen, to observe," he said, adding he didn't know what price level would trigger an extraordinary OPEC meet.

The country is talking to fellow OPEC member Iran about long-term crude supplies to feed its growing domestic oil refining industry, Prawiraatmadja said, declining to give details. Indonesia aims to increase its processing capacity by about 40 percent by 2025 to 1.73 million barrels a day. That will require investment of $23.6 billion, including construction of two new refineries, with Indonesia looking to OPEC countries for investments and supplies.

Overall GDP growth

In view of the macro-economic turmoil as aforementioned, Indonesia's market has taken major blows in its net trade, with continuous downward pressure since the end of Q1, as seen in the JCI (Figure 10). Despite a significant comeback during Q3, Indonesia continues to face downward pressure.

Figure 10: Jakarta Composite Index

Indonesia's GDP expanded by 3.21 percent in the third quarter of 2015, slowing from a 3.78 percent growth in the previous three months and below market expectations. A faster increase in private consumption and investment were unable to offset a significant slowdown in government spending and a slight fall in exports.

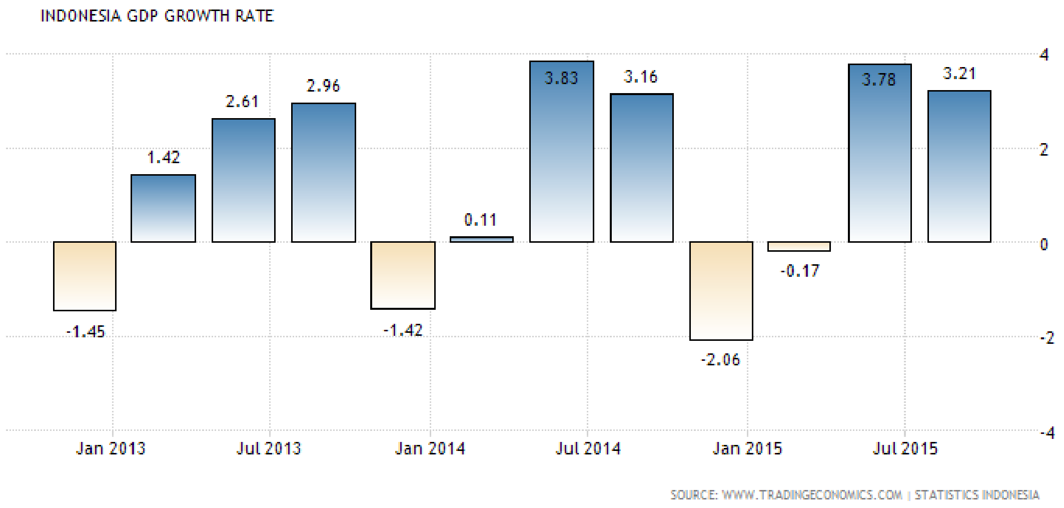

Figure 11: Indonesia GDP growth rate (quarterly)

On an annual level, the Indonesian economy grew an annual 4.73 percent in the September quarter of 2015, up from 4.67 percent expansion in the previous period but fractionally below market consensus. A faster expansion in government spending and investment managed to offset a further decline in exports while private consumption was flat.

Figure 12: Indonesia GDP annual growth rate (quarterly)

Key Forecasts

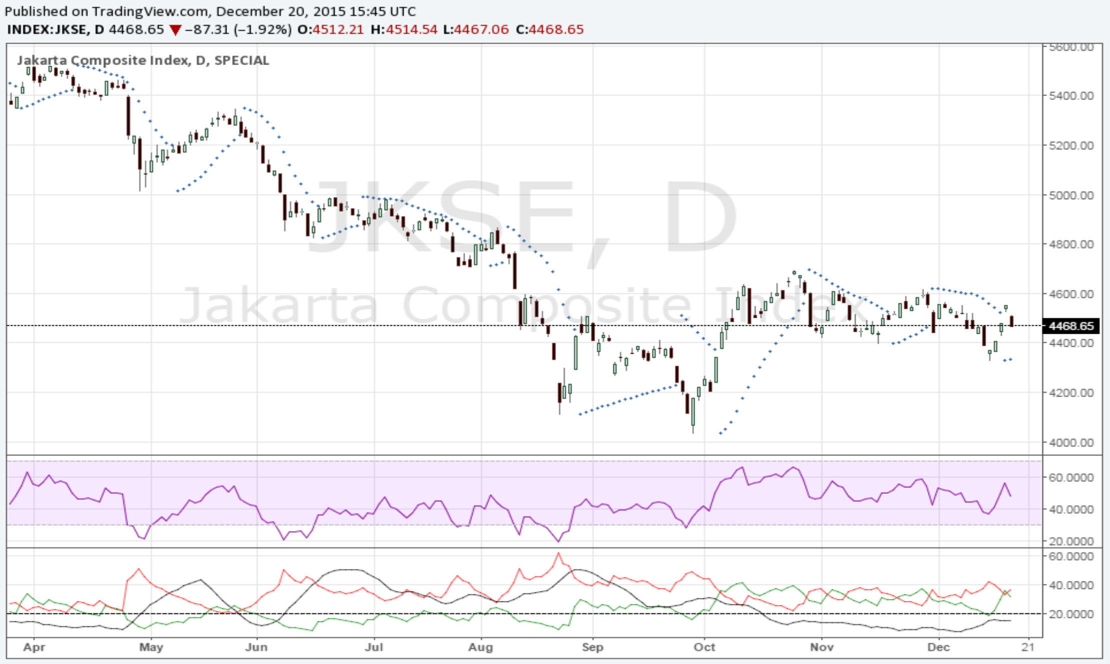

Figure 13: JCI technical analysis

As seen in the chart, the JCI has been ranging between 4600 and 4400 for over a month. The ADX and RSI indicators show weak directional momentum. The RSI ranging between 60 and 40 for the past one month, giving no clear indication of a trend strength. This is also shown in the ADX, hovering below 20 since mid-October, and hence indicating that there is a very weak trend. Given the long standing downward pressure since Q1, and the continued dip, as seen in the most recent low on 14th December, it is expected that the price will continue to move downward through 2015.

In view of the undesirable macro-economic circumstances surrounding Indonesia, GDP growth is likely to be negatively affected. With Indonesia's entry into OPEC and OPEC's call for production cuts, Indonesia may have to manage a new strategy to improve its economy. Oil production cuts may cause oil prices to rise, significantly causing Indonesia's imports to increase, which affects its ability to focus on other developments which it has been doing thus far.

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