PP14767/09/2012(030761)

Thursday, July 09, 2015

3Q15 US Economic Outlook

"First Interest Rate Adjustment Soon"

US Economic Forecast

	2012	2013	2014	2015F	2016F
IMF	2.8%	1.9%	2.4%	3.6%	3.3%
US Federal Reserve				2.3%-2.7%	2.3%-2.7%
World Bank				3.2%	3.0%
OECD				3.0%	3.0%
Bloomberg Consensus				3.0%	2.8%

Source: Various, M&A Securities

Positive catalysts:

1) Full employment and robust housing market
2) Appreciation of USD: cheaper importation cost
3) Economic re-acceleration (Fed 2014 GDP: 2.4%; Fed 2015F GDP: 2.3%-2.7%)
4) Sluggish global commodity prices: less pressure on cost of living and inflation

Negative catalysts:

1) A series of policy rate hike
2) BOP imbalance to continue
3) Rapid capital inflow: USD may get too strong

US is on the road to full recovery, underpinned by full employment and steady housing market. The strength of USD will pave the way for consumers spending to be sizzling. Blessed by increasing shale oil deposits, the US is unperturbed by the prolong weakness of oil prices and hence, we predict the US will have no qualms of adjusting its interest rate this year, its first adjustment since the last 6 years. Admittedly, hedge funds had turned nervous as borrowing cost will elevate and has started pulling back their capital, steadily and at time robustly. The victims so far have been the global commodity producers and also emerging countries as can be witnessed in heighten currency volatility, albeit moving down south. Despite suggestion by the World Bank for the US to start adjusting its Federal Funds Rate (FFR) only next year but we think that the key to that decision will hinge on a few factors, including 1) the strength of its labor and housing market 2) the outlook of oil and hence, inflation and 3) the strength of USD.

The US cannot take lightly the possibility of runway inflation as monetary weapon would usually take a few months to take effect. Give that the US will be dead serious to adjust the rate before things get out of control. This we predict will be in earnest in 2H15, albeit in small dose of 25-50 basis points before steadily elevating to reach the normalize level of 4%++ by 2017. Hence, there could be at time sharp adjustment to the tune of 50 basis points for each FOMC meeting. The US have known to adjust (note: cut or increase) their FFR during recession or economic prosperity within 2 years and we think it may be the case this time around. A word of caution: although the FFR may seems to be heading skywards but we need to issue a disclaimer that there could be adjustment or cut or pause on FFR depending on the strength of the US economy. Therefore, it is not cast in stone.

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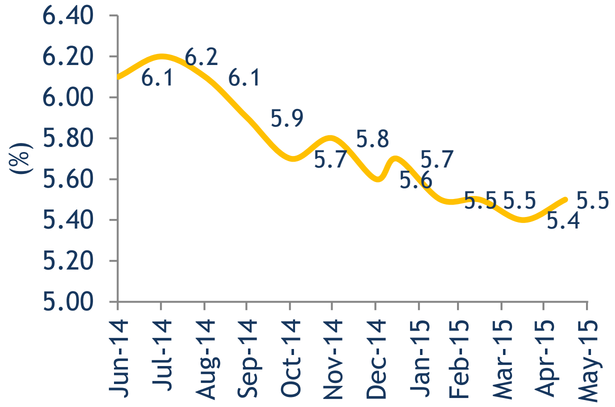
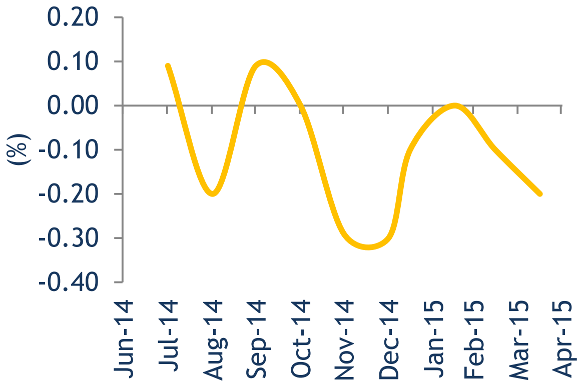
All in all, the US economy is on full mend and finally grows within its capability. As a backlash, however, the strength of USD may weigh on its export potential and likely to result in bigger trade imbalance. The strength of USD will be juxtaposed and precursor for import to elevate if one is to look at the US big spending appetite. Nonetheless, it will not be a big issue as the US economy is 80% oil by consumers spending. Meanwhile, the soft global commodity prices will be a blessed for the US economy as it will put less pressure on inflation. As it turns out to be, the US will be the global locomotive to global economy amid economic headwinds in Japan and the Eurozone.

In sum, the global community have to face the fact that the US will be go ahead with its plan to adjust interest rate this year. With so much policy space in hand and so much to lose if inflation turns skyward, the US will not waste time to make the best for the country. In order to avoid catastrophic volatility, we think that the adjustment will be in small dose at first before proceeding to be in full force then after. In our view, the period of volatility could last until end of 2016.

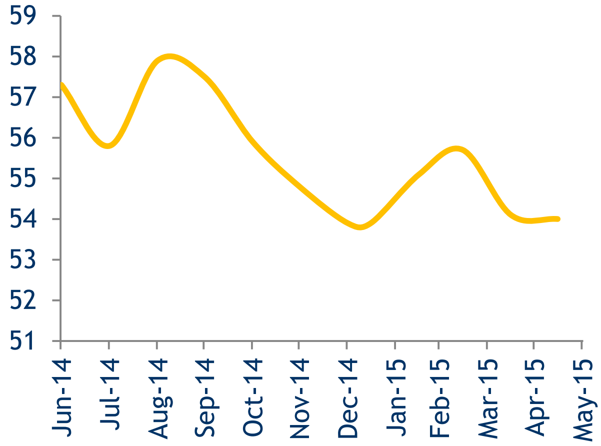
US Unemployment Rate
(June 2014 - May 2015)



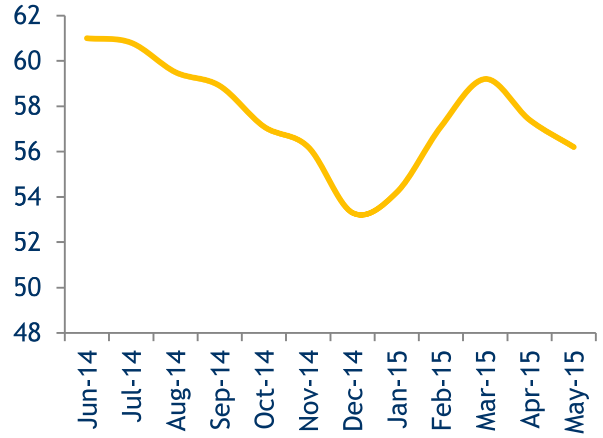
US Inflation Rate
(June 2014 - May 2015)



US PMI Manufacturing
(June 2014 - May 2015)



US PMI Services
(June 2014 - May 2015)



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M&A Securities

Market Access

STOCK RECOMMENDATIONS

BUY — *Share price is expected to be ≥+10% over the next 12 months.*
TRADING BUY — *Share price is expected to be ≥+10% within 3-months due to positive newsflow.*
HOLD — *Share price is expected to be between -10% and +10% over the next 12 months.*
SELL — *Share price is expected to be ≥-10% over the next 12 months.*

SECTOR RECOMMENDATIONS

OVERWEIGHT — *The sector is expected to outperform the FBM KLCI over the next 12 months.*
NEUTRAL — *The sector is expected to perform in line with the FBM KLCI over the next 12 months.*
UNDERWEIGHT — *The sector is expected to underperform the FBM KLCI over the next 12 months.*

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