

Vantage Point

A WEEKLY PUBLICATION FROM THE FUND MANAGERS AND ANALYSTS OF PHILEQUITY MANAGEMENT, INC.

MARKET OUTLOOK: CAUTIOUS

SECTOR PICKS: TELCOS, LOW VALUATION STOCKS WITH STRONG EARNINGS GROWTH POTENTIALS FOR 2021

TECHNICALS: SUPPORT AT 5700 FOLLOWED BY 5000, RESISTANCE AT 6500 FOLLOWED BY 6800

After correcting sharply on the announcement of MECQ, note that the market shrugged off the above forecast 16% contraction in 2Q20 GDP. Despite headlines of this contraction being the worst on record, the stock market did not fall as much. This indicates that despite the Philippines officially entering a recession in 2Q20, this was expected and is largely in the price. Some companies which reported 2Q20 earnings which were below forecast also showed surprising strength instead of dropping. As we see in global markets, investors seem to be writing off 2020 and looking forward to 2021.

Moreover, now that we are halfway through MECQ, it seems that an extension is unlikely. A prolonged MECQ will have a debilitating effect on both the economy and capital markets. Once MECQ is lifted, sentiment should also improve.

On the global front, we still see rising COVID cases, but 2 news items will likely drive markets. One is the escalation of the US-China conflict, with Trump recently ordering a ban on Tiktok and Wechat. With Trump up for reelection in November and currently trailing in polls, we may see more anti-China rhetoric from him in as we head into November. Second is the failure of US Congress to pass more stimulus measures. This may be a sign that even the US is hesitant to continue giving dole-outs to the unemployed as the gargantuan fiscal deficit will grow even larger. This mirrors the same policy by the economic team here which is battling for a smaller stimulus package. Too large a fiscal deficit may result in a credit rating downgrade, higher borrowing costs and a depreciating peso - all of which are big negatives for our economy.

With markets already up significantly from their March lows, it is likely that the next leg higher will be driven by the development of an effective vaccine. This is the single biggest catalyst for stocks. Even if a vaccine is not developed this year, we believe that any significant positive news will cause markets to rise sharply even prior to the vaccine's actual distribution.

Philippine Stock Exchange Index (PSEi) 1-year chart



TRADING STRATEGY



With the PSEi correcting last week due to the declaration of MECQ, we took the opportunity to tilt the portfolio's allocations. We have started reducing the portfolio's defensive tilt in favor of cyclical stocks as it seems that the worst is over for the economy.