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FROM THE EQUITY DESK

Monthly Outlook

Summary

- Asia ex-Japan (AxJ) equities returned -2.0% in US Dollar (USD) terms, underperforming MSCI World and MSCI Emerging Markets (EM). Currencies across AxJ generally weakened against the dollar following the Federal Reserve's (Fed's) decision to hike rates. Meanwhile, Gold declined 2.2% while oil jumped 8.66% month-on-month.

- China and Hong Kong ended the month down 4.1% and 6.4% in USD terms respectively. The Chinese government announced an adjustment to the composition of the trade-weighted CNY index.

- Meanwhile, MSCI South Korea posted a marginal 0.6% gain in USD terms on the back of a depreciating Korean Won (KRW), the ongoing impeachment of President Park, and a downward revision of 3Q16 GDP growth.

- MSCI India declined -0.1% in USD terms, while various economic sectors were negatively impacted by Modi's demonetisation exercise. The Monetary Policy Committee (MPC) also surprised by leaving interest rates unchanged.

- Within ASEAN, Indonesia emerged as the best performer while Singapore underperformed peers. Thailand continued its growth momentum with a 2.1% gain.

- Recent developments in China, such as the change to the trade-weighted CNY Index, acceleration of Public-Private Partnerships and the Shenzhen-Hong Kong Stock Connect appear encouraging. Meanwhile, we remain cautious in Korea on the back of political scandal and potential strains in Sino-Korean trade. Elsewhere in Taiwan, we continue to be selective, preferring companies in niche sectors with sustainable earnings.

- Asian EMs offer better growth and more attractive valuations than developed markets. Despite near term headwinds as a result of the demonetisation initiative, India remains one of our preferred equity markets. We remain selective in ASEAN, while maintaining zero weight in Malaysian Equities.

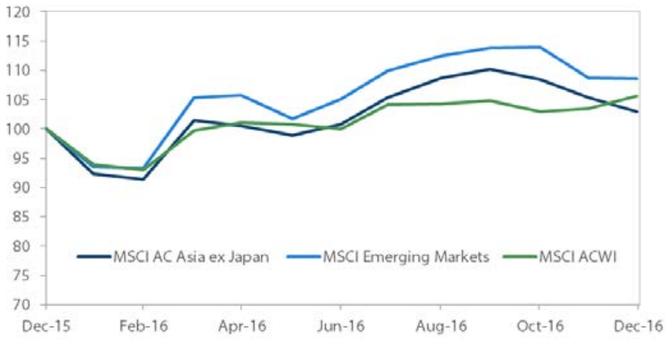
Asian Equity

Market Review

- Asia ex-Japan equities declined in December

The AxJ equity market ended 2016 slightly higher despite several unexpected global events throughout the year. Year-to-date (YTD), the MSCI AxJ benchmark index was up 5.2%. For the month, the index finished down 2.0% in USD terms, lagging MSCI World and MSCI Emerging Markets (EM) which returned 2.4% and 0.2% respectively. Following the Fed's decision to raise its rate by 25 basis points (bps) in mid-December, currencies in AxJ generally weakened against the dollar, led by the Korean Won (KRW). Gold closed down -2.2%, while oil rose 8.66% on a monthly basis.

1-Year Market Performance of MSCI Asia ex Japan versus Emerging Markets versus All Country World Index



Source: Bloomberg, 31 December 2016. Returns are in USD. Past performance is not necessarily indicative of future performance.

MSCI Asia ex Japan versus Emerging Markets versus All Country World Index Price-to-Earnings

Source: Bloomberg, 31 December 2016. Returns are in USD. Past performance is not necessarily indicative of future performance.

- **North Asia remained weak**

MSCI China and MSCI Hong Kong finished down 4.1% and 6.4% in USD terms respectively. Chinese stocks were initially impacted by the sharp bond market correction following stringent monetary policies, but continued to trade sideways as the market remained uneventful heading towards the year-end. China also announced an adjustment to the composition of the trade-weighted CNY index. Effective 1 January, 2017, USD/G3 currency weights will be reduced while more EM currencies will be included.

MSCI Korea posted a 0.6% gain in USD terms on the back of a weakening KRW. The National Assembly passed a bill to impeach President Park and this bill will now be reviewed by the Constitutional Court. Additionally, the Bank of Korea revised down 3Q16 GDP estimates to 2.5% quarter-on-quarter (QoQ) growth.

- **India weighed down by demonetisation exercise**

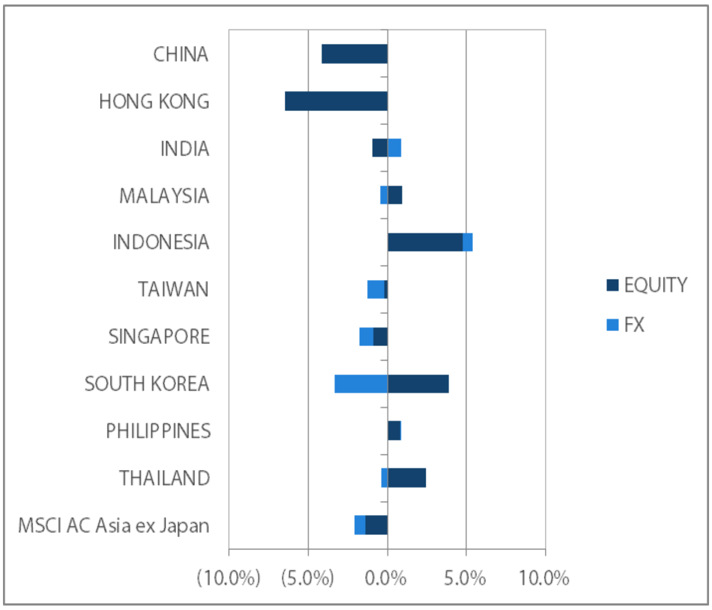
The MSCI India Index ended down 0.1% in December. However, that belies the intra-month volatility which saw the Nifty Index trading within a 5% range. This reflected the muddled impact of demonetisation across various sectors as consumption declined, manufacturing PMI contracted (a first in 12 months) and bank rates dropped further on tepid loan growth even as G-Sec yields recouped some of their November losses. On top of that, markets were given little to cheer about when the winter session of Parliament concluded without any progress on the GST bill, as the Opposition protested the Government's move. Meanwhile, the MPC surprised by leaving interest rates unchanged, citing macroeconomic uncertainty as its key reason.

- **ASEAN ended the month mixed**

Within ASEAN, Singapore reversed last month's outperformance to finish at the bottom of the pile, returning -1.7% in USD terms. Conversely, Indonesia rebounded strongly, becoming the best performing Asian market with a gain of 5.4% in USD terms. This comes as Bank Indonesia kept rates unchanged; the Board of Governors was of the view that the economy will recover in 2017, supported by improving performance of the corporate sector and increased financing. Fitch also revised Indonesia's outlook to Positive. Elsewhere, Thailand also posted a 2.1% gain in USD terms, continuing its resilience.

MSCI AC Asia ex Japan Index

For the month ending 31 December 2016

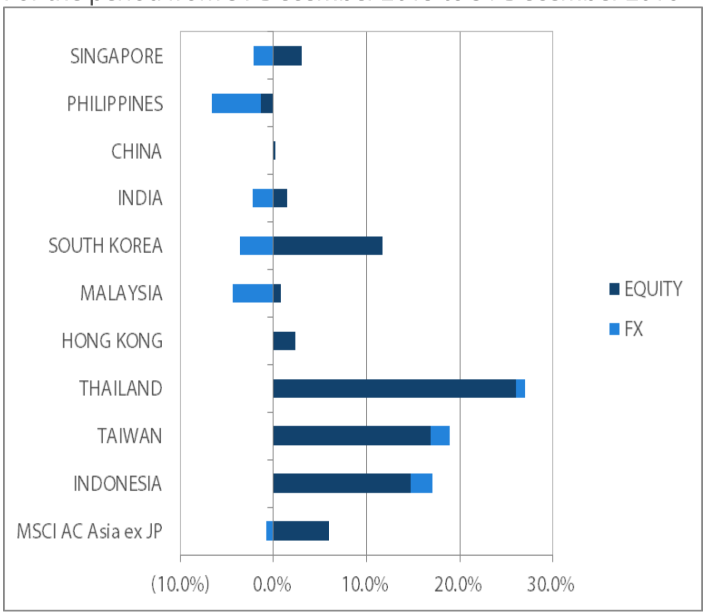


Source: Bloomberg, 31 December 2016

Note: Equity returns are single country MSCI indexes and are in local currencies while FX and MSCI Asia ex Japan returns are in USD. Returns are based on historical prices. Past performance is not necessarily indicative of future performance.

MSCI AC Asia ex Japan Index

For the period from 31 December 2015 to 31 December 2016



Source: Bloomberg, 31 December 2016

Note: Equity returns are single country MSCI indexes and are in local currencies while FX and MSCI Asia ex Japan returns are in USD. Returns are based on historical prices. Past performance is not necessarily indicative of future performance.

Market Outlook

- Asian markets now offer more attractive valuations and fundamentals

Notwithstanding the headwinds posed by a stronger USD, Asian EMs offer better growth than developed markets, and at more attractive valuations. Currently, MSCI AxJ trades on a 1.4x forward P/B multiple compared to a 2.2x P/B multiple for MSCI World.

Fundamentally, Asia is also in better shape than the period leading up to the taper tantrum in late 2013. This is primarily due to the significant adjustments that Asian countries have made. More notably, China has indicated a willingness to adopt a more flexible stance vis-à-vis the Chinese yuan (CNY), India has introduced the GST bill and demonetisation in a bid to combat corruption and increase electronic transactions, while Indonesia has also strengthened its fiscal position by cutting oil subsidies and implementing the tax amnesty programme.

- Favour India while selectively overweight in ASEAN

Despite a near term impediment to growth as a result of Modi's demonetisation exercise, India remains one of our preferred equity markets as we believe it still offers the best structural growth profile in Asia over the medium and long term. Ultimately, the demonetisation initiative can also be viewed as the government's willingness to introduce non-populist reforms. Furthermore, the MPC's decision to leave rates unchanged suggests that the new Reserve Bank chief is not easily swayed by external pressures.

- Recent initiatives in China prove promising

Recent developments in China have been encouraging. The change to the trade-weighted CNY Index indicates a more flexible stance towards managing the currency. In addition, the government has accelerated its Public-Private Partnerships to encourage private participation in public projects so as to quicken the pace of economic growth in the next few quarters. In our view, the Shenzhen-Hong Kong Stock Connect is also a game changer relative to the Shanghai-Hong Kong Stock Connect as the former offers a wider scope and greater depth of financial instruments.

- Remain cautious on Taiwan, Korea and developed Asia

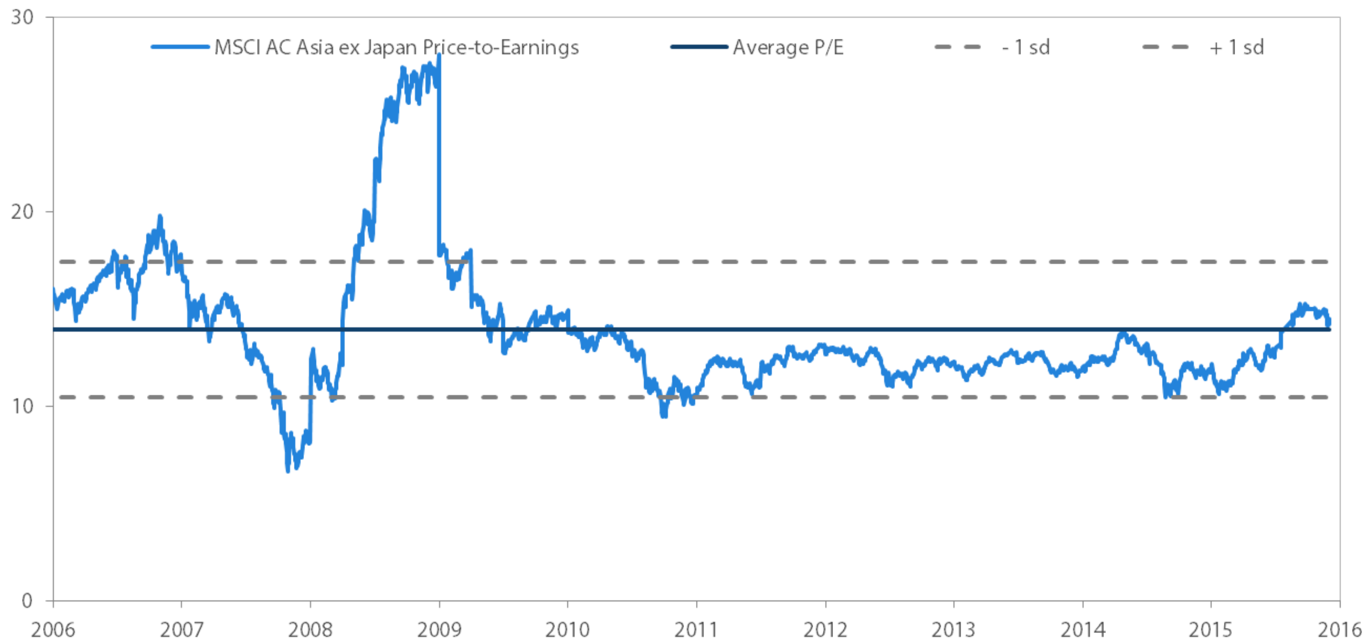
We remain selective in Taiwan, preferring companies in niche sectors with sustainable earnings. The outlook is mixed, with policy makers mulling a potential increase in business tax. If these taxes are approved, it could hurt manufacturers' earnings. Across in Korea, Sino-Korean trade could remain affected by the country's commitment to deploy the Terminal High Altitude Area Defense system in conjunction with the US, at least in the near future. The debacle that has plagued Park's government has led to investigations into the government's dealings with multiple companies, suggesting that we have not seen the last of this development. Hence, we remain cautious in Korea.

Meanwhile, Singapore and Hong Kong face multiple headwinds in the form of higher US interest rates, anemic or potentially negative growth and a possible correction in property prices. Furthermore, Hong Kong also faces political uncertainty as the Hong Kong Chief Executive election is scheduled to be held in mid-2017.

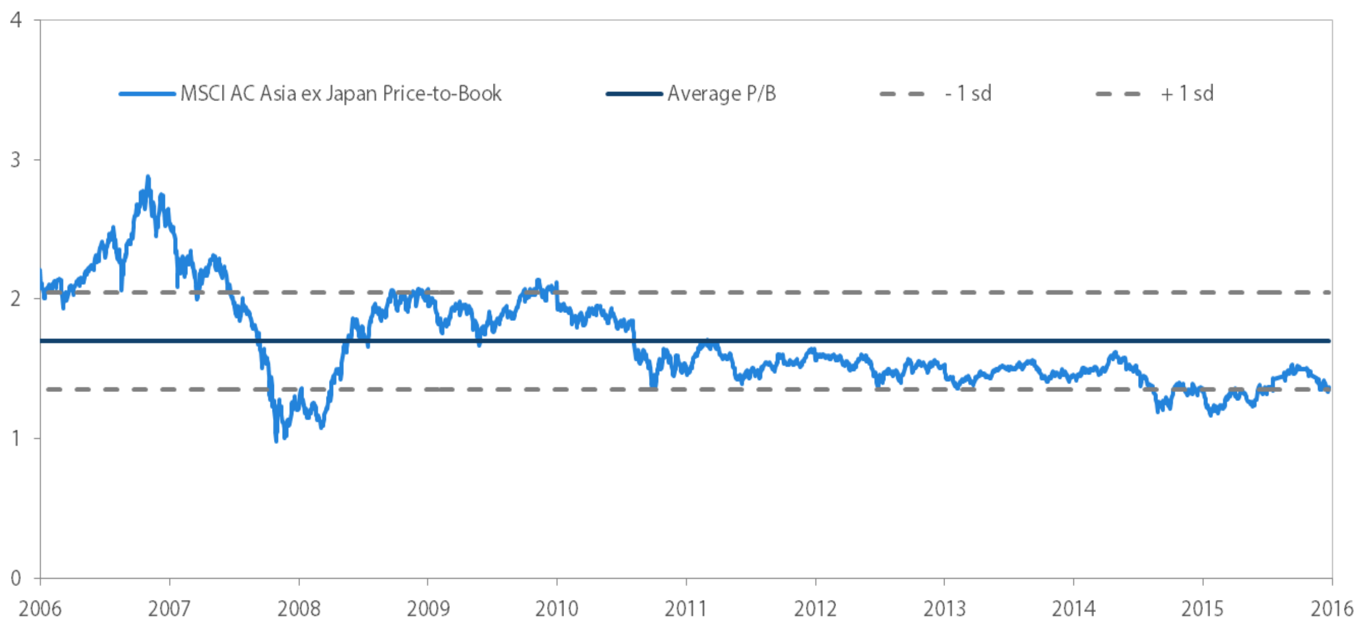
Meanwhile, we remain selectively overweight in ASEAN, favouring underappreciated and strong franchises in Indonesia and Thailand which are focused on domestic demand and infrastructure. Conversely, we continue to avoid the Malaysian equity market altogether.

Appendix

MSCI AC Asia ex Japan Price-to-Earnings



MSCI AC Asia ex Japan Price-to-Book



Source: Bloomberg, 31 December 2016. Ratios are computed in USD. The horizontal lines represent the average (the middle line) and one standard deviation on either side of this average for the period shown. Past performance is not necessarily indicative of future performance.

Important Information