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ASIAN EQUITY OUTLOOK

May 2018

Summary

- The MSCI AC Asia ex Japan (AxJ) Index gained 0.7% in USD terms. Trade jitters receded following China's commitment at the Bo'ao Forum to further open up the economy to foreign businesses. Subsequent firm inflation readings in the US and rising oil prices placed downward pressure on global markets.

- Singapore outperformed AxJ peers on the back of strong bank earnings and private home prices growth. India placed second as a tech rebound drove the broader index. Despite ending the month flat, China posted strong 1Q18 GDP growth. Elsewhere, Hong Kong and South Korea outperformed on the back of strong corporate earnings. Conversely, Taiwan ended the month lower.

- Indonesia underperformed despite a Moody's upgrade as rate hike concerns weighed on the index. Similarly, Malaysia was down in USD terms due to currency weakness. Philippines continued to lag due to concerns over accelerating inflation and an overheated economy.

- Despite recent increased volatility, higher earnings growth at relatively attractive valuations in the Asian region provides opportunities for patient investors. By and large, risk premia for these markets have declined on the back of improved monetary and fiscal management and lower private sector debt.

- We maintain an overweight to Chinese stocks, with a preference for structural growth sectors. Meanwhile we remain invested in long-term sustainable franchises offering reasonable risk-reward trade-offs in India. We continue to focus on niche sectors in Technology in Korea and Taiwan and maintain our underweight to ASEAN.

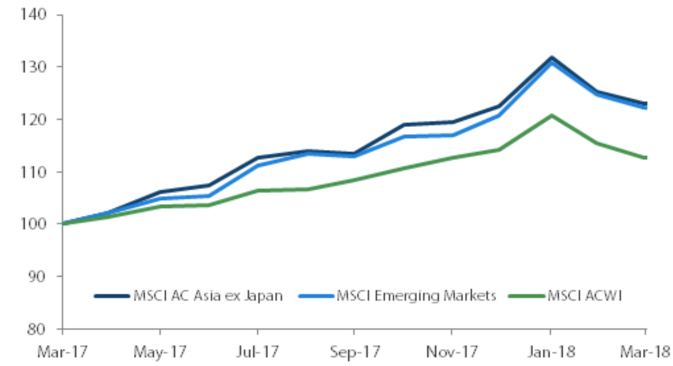
Asian Equity

Market Review

Asian equities rose in April

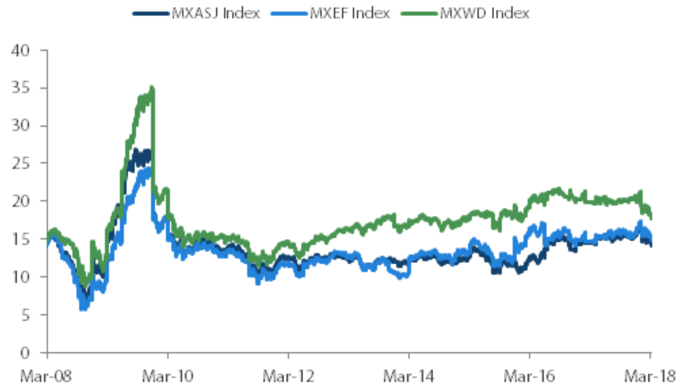
The MSCI AC Asia ex Japan (AxJ) Index rose 0.7% in USD terms in April. Trade jitters between the US and China receded during the month following Chinese President Xi Jinping's commitment at the Bo'ao Forum to further open up the economy to foreign businesses, allowing markets to re-focus on macro data. Subsequent firm inflation readings in the US, combined with rising oil prices, triggered concerns the Federal Reserve could accelerate monetary policy tightening. This pushed US Treasury yields to break above 3%, placing downward pressure on global markets.

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



Source: Bloomberg, 30 April 2018. Returns are in USD. Past performance is not necessarily indicative of future performance.

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



Source: Bloomberg, 30 April 2018. Returns are in USD. Past performance is not necessarily indicative of future performance.

Singapore and India outperformed AxJ peers

Singapore outperformed AxJ peers and rose 6.2% in USD terms, as banks posted robust earnings and private home prices grew more than expected in 1Q. Advance estimates for GDP growth improved to 4.3% in 1Q18, from 3.6% in 4Q17, supported by manufacturing and services sectors. The Monetary Authority of Singapore (MAS) also raised the slope of the SGDNEER policy band "slightly" while keeping the width of the policy band unchanged. India was the second best performing market, up 4.1% in USD terms. Strong earnings from Tata Consultancy Services (TCS) led the rebound in the tech sector, driving strength in the broader index. Meanwhile, agriculture, consumption and rural-related stocks also received a further boost from forecasts that the monsoon would be normal this year.

China was flat as the Tech sector led decline

Returns for MSCI China were flat in USD terms. The People's Bank of China (PBoC) announced a surprise 1% cut in the reserve requirement ratio for most banks, with the exception of policy lenders. The move was largely aimed at freeing up funding for small firms. The cut also came after the release of strong 1Q18 GDP, which saw the economy beating expectations and grow 6.8%. Meanwhile, Chinese tech stocks fell after the US banned ZTE from buying key American technology for seven years.

Hong Kong and Korea outperformed; Taiwan fell

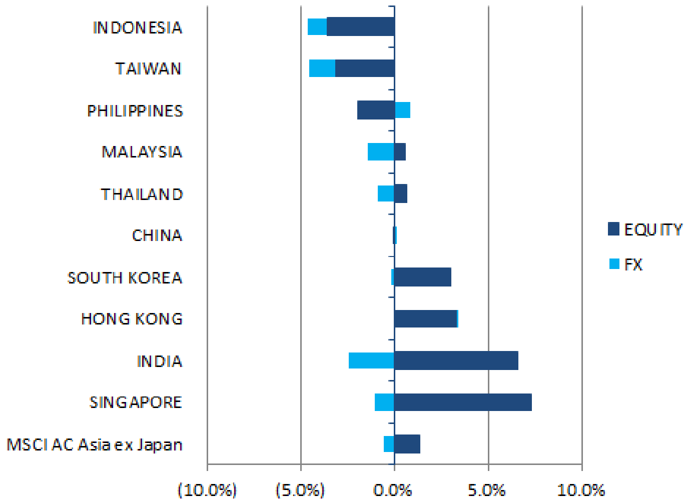
Hong Kong rose by 3.3% in USD terms. Financials were supported by strong earnings and intervention by the central bank to prop up the HKD for the first time since 2015, after the currency slipped to its weakest level since 2005. Elsewhere in North Asia, Korea gained 2.7% in USD terms amid better-than-expected earnings from Samsung Electronics and the prospect of improved inter-Korean relations. Conversely, Taiwan declined 4.6% in USD terms. TSMC trimmed its full-year revenue estimate on weaker smartphone demand, sparking concerns about potentially sluggish 2Q earnings within the tech sector.

Most of ASEAN lagged

Most of ASEAN lagged. Indonesia returned -4.6% in USD terms despite an upgrade of its sovereign rating by Moody's. Mixed earnings results, limp consumer debt and a weakening rupiah which stoked rate hike concerns weighed on the index. Malaysia was down 0.9% in USD terms due to currency weakness. The market, however, was up in local currency terms, underpinned by stronger commodity prices and the upcoming 14th General Election in May. Philippines declined 1.2% in USD terms as accelerating inflation led to concerns of an overheated economy.

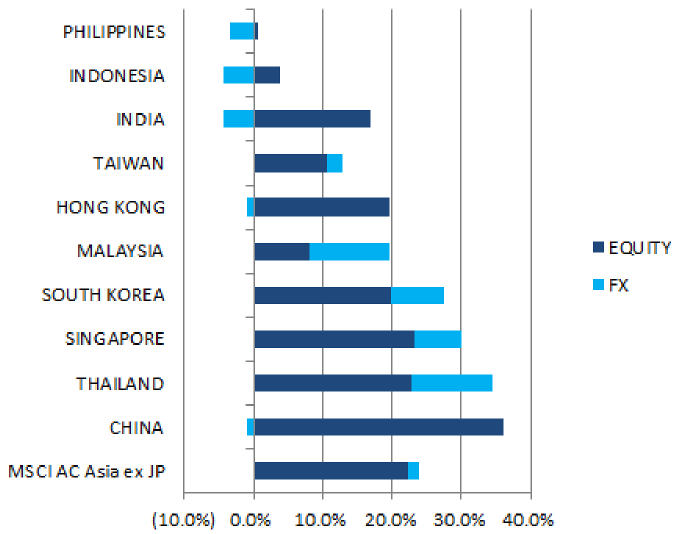
MSCI AC Asia ex Japan Index[1]

For the month ending 30 April 2018



Source: Bloomberg, 30 April 2018

For the period from 30 April 2017 to 30 April 2018



Source: Bloomberg, 30 April 2018

[1]Note: Equity returns refer to MSCI indices quoted in local currencies while FX refers to local currency movement against USD. Returns are based on historical prices. Past performance is not necessarily indicative of future performance.

Market Outlook

The new "normal" and relatively attractive valuations provide opportunities for patient investors

The Trump Presidency has certainly made for greater volatility that starkly contrasts against an extended period of abnormally low volatility that preceded it. The new "normal" provides opportunities for patient investors. In our view, the economic impact of the "trade war" is small and not enough to derail other longer term drivers. While the term "trade war" sells more papers, it is important to realise that none of this is policy as yet. There is a two-month window during which affected parties can negotiate, and our base case remains that backroom deals that are palatable to all parties are likely to be worked out.

Earnings growth in the region is higher than in developed markets while relative valuations are much more attractive compared to previous points when markets corrected sharply. Emerging markets' recoveries started in 2015-16, which was two to three years after the US and the Eurozone. Growth is still early-mid cycle and, hence, inflationary pressures are low. By and large, most markets have lowered their reliance on foreign currency funding, have better fiscal balances and have more flexible exchange rate mechanisms. Thus susceptibility to external shocks has been much reduced. Coupled with declining private sector debt to GDP ratios, risk premia associated with these markets have declined.

Continue to favour structural growth sectors in China and Hong Kong

China's longer term growth outlook continues to be supported by the country's efforts to rein in excesses in the financial sector in conjunction with ongoing supply side reform. China has one the lowest correlations of GDP with trade growth among all the AxJ countries, and this has been decreasing over time. The ongoing supply side reform in Chinese manufacturing will further diminish the urgency and importance of related US trade investigations. Progress on the key initiatives highlighted by President Xi, in both the National People's Congress (NPC) as well as at the Bo'ao Forum, will be keenly watched. MSCI's inclusion for the A-share constituents later this quarter will also be noteworthy. Our preference continues to be for structural growth sectors – Tourism, Healthcare, and Insurance. In Hong Kong, the prospect of higher interest rates resulting from tighter coupling with USD LIBOR augurs well for banks.

Remain constructive on India long term but are more selective amid potential headwinds

India's economic growth is likely to rebound in the second half of 2018, recovering from the adverse impact of demonetisation and the introduction of the GST last June. Politics, however, can no longer be taken for granted, with elections, both state and national, being held in the next 12 months. The ruling Bharatiya Janata Party's (BJP's) showing in these elections could dramatically impact the risk premium in what is seen as a rather expensive equity market. High, and still rising, oil prices as well as a tighter global interest rate environment are expected to be headwinds to the Indian economy. Bearing these risks in mind, we are more selective, preferring sustainable franchises offering reasonable risk-reward trade-offs.

Focus on niche Technology stocks in Korea and Taiwan

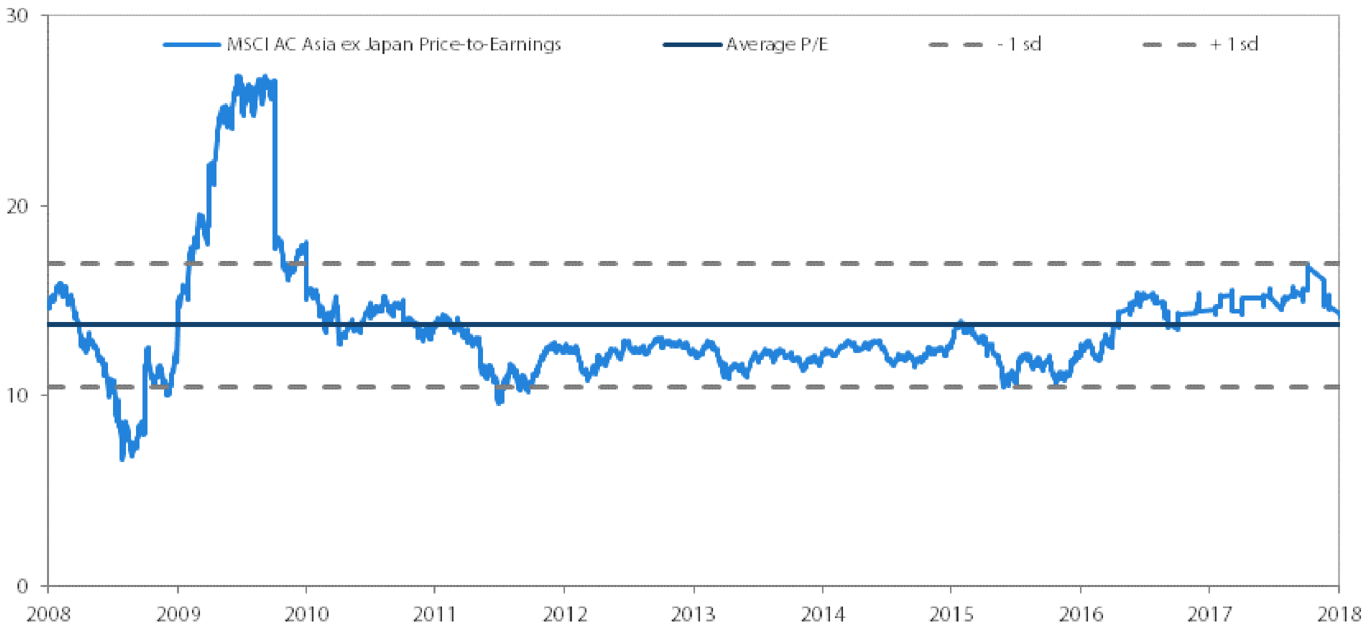
We remain selective in Korea and Taiwan, notwithstanding the recent thawing of relations between the two Koreas as well as China. The stronger won, particularly when compared to the yen, affects export competitiveness. Taiwan's technology sector is heavily dependent on demand for Apple products, and is also susceptible to potential disruption from "trade wars". Hence, we focus on stocks exposed to niche areas, namely electric vehicles and display solutions.

Remain underweight ASEAN

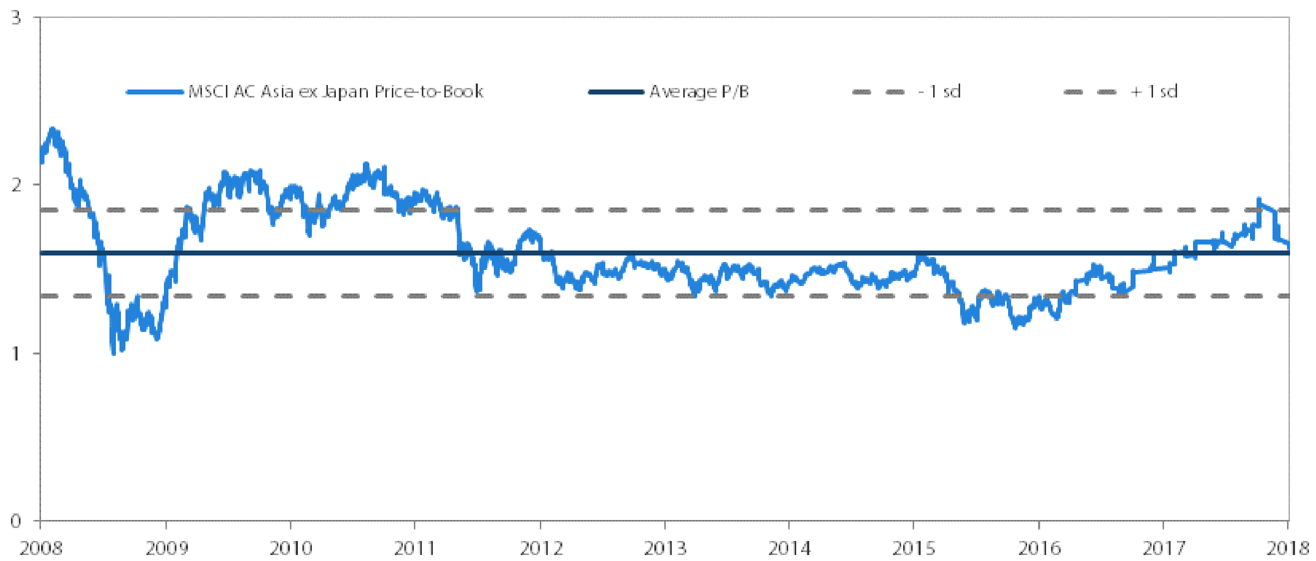
We maintain our underweight stance in ASEAN although with some change in relative preferences. In Thailand, we have added select positions in both Food & Beverage and Healthcare related stocks while we remain well positioned in Singapore given better growth prospects and attractive valuations. There are increasing signs of overheating in the Philippines' economy and capital outflows are pressuring the currency and we thus remain zero weighted. Meanwhile, we maintain select positions in both Indonesia and Malaysia.

Appendix

MSCI AC Asia ex Japan Price-to-Earnings



MSCI AC Asia ex Japan Price-to-Book



Source: Bloomberg, 31 March 2018. 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.

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