UOB

UOB House View 4Q 2023

Monday, 09 October 2023

The Team
Global Economics & Markets Research
Private Bank

Global Macro

3Q23 was characterized by global investors' expectations that the US Federal Reserve is at or near the tail end of its rate hiking cycle. And while Sep delivered the expected pause, the Fed has not taken a Nov hike off the table and has reinforced the "higher for longer" mantra for interest rates. Going forward, we believe three key event risks may inject renewed volatility into rates and currencies, higher crude oil prices, unwinding of BOJ's Yield Curve Control and China slowdown.

Asset Allocation

From a tactical perspective, we have reduced equities in a mixed asset portfolio to a slight underweight, reflecting near-term challenges. We advocate investors to remain diversified with an anchor to high-quality bonds and short-term money market which pay attractive yields alongside some diversification into private assets with a focus on private credits.

Equities

In our view, names in defensive sectors (healthcare/consumer staples) could hold up better on resilient earnings. We are also constructive on selected cyclicals like the energy sector amidst tight crude supply putting a floor on crude prices and utilities stocks riding on the theme of renewable transition. We remain Neutral on US equities, stay Underweight on European equities, stay Overweight on Japanese equities and remain Neutral on EM Asian equities.

Fixed Income

For Developed Markets (DM), we remain Overweight on DM USD IG, with the view to lock in yield carry without sacrificing credit quality and stay Underweight on DM USD HY as funding and liquidity conditions are set to tighten on the higher-for-longer rates narrative, with potential for credit spreads to widen further on rising default rates. For EM Asia IG, we remain Overweight given their role as portfolio stabilizers and stay Neutral on EM Asia HY as sentiment in this space could be largely affected by Chinese policy measures and the outlook on its property sector and continue to advocate caution, selectivity and diversification in this space.

Commodities

Our view is that positive drivers have intensified and Brent is now ready to test the USD 100/bbl headline resistance. We raised our Brent price forecast by yet another USD 5/bbl to USD 95/bbl in 4Q23/1Q24 and to USD 100/bbl in 2Q24/3Q24. We forecast gold at USD 2,000/oz in 4Q23/1Q24, followed by USD 2,100/oz in 2Q24/3Q24. We maintain our mild negative outlook for Copper, forecasting USD 8,000/MT for 4Q23/1Q24, thereafter USD 7,000/MT for 2Q24/3Q24.

FX & Interest Rates

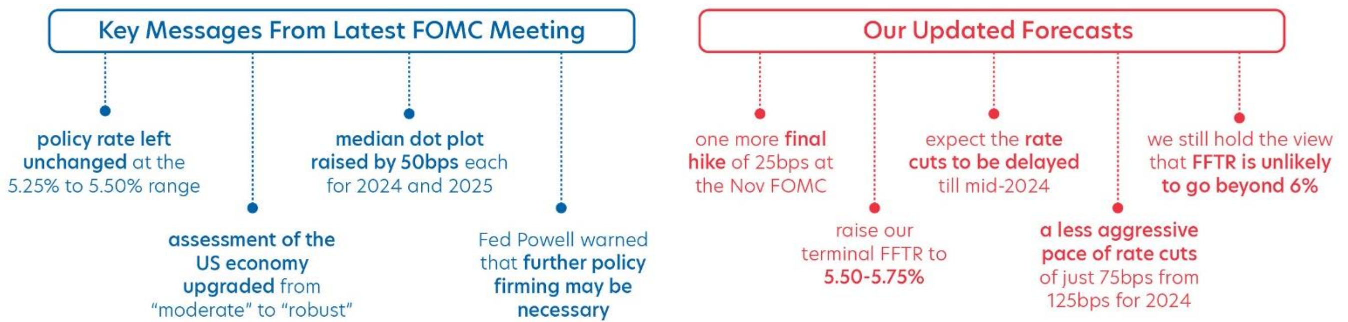
With "higher for longer", there is likely a last hurrah for the USD in the near term even as we keep a long-term bearish view on the USD against DM peers. Meanwhile, our updated Fed view now calls for one more 25-bps hike in Nov with projections for rate cuts pushed back till mid-2024. We expect 3M compounded SOFR and 10Y US Treasuries yield would stay elevated above 5% and 4% respectively till 3Q24.

Right By You

Global Macro & Markets Strategy
Interest Rates To Stay Higher For Longer

"Interest rates are to asset prices what gravity is to the apple." - Warren Buffett

The third quarter of 2023 was characterized by global investors' expectations and hopes that the US Fed is at or near the tail end of its rate hiking cycle. At the latest FOMC meeting on 21 Sep, the Fed left its policy rate unchanged, but renewed their hawkish stance on interest rates. Hereafter is a quick glance at the key messages from the meeting and our updated forecasts.



Now that the "uncertainty" regarding the Fed's monetary policy outlook is mostly out of the way, this does not mean that the coast is clear for the global economy and financial markets going forward. US Treasuries were sold off anew post FOMC and the US Dollar is decidedly stronger as well. Going forward, we believe that there are three key event risks that may inject renewed volatility into respective underlying interest rates and related currencies. These are namely higher crude oil prices, unwinding of BOJ's Yield Curve Control (YCC) and China's on-going economic slowdown.

BACKDROP

When Saudi Arabia first announced their intention for production cuts, there were widespread skepticism as to whether they are able to achieve any stability in crude oil prices given the fragile global growth outlook. However, US economic growth turned out to be much stronger than expected and China's energy demand stayed robust despite its economic uncertainties.

As a result, Brent crude oil price found a floor at USD 80/bbl and duly recouped all of its year-to-date losses across 3Q23 and more. Since then, Saudi Arabia has kept up the supply squeeze and exacerbating it further by extending it till end of this year. At the moment of writing, Brent crude oil price has rallied to USD 95/bbl. The global supply squeeze is real and we update our forecast for a test of USD 100/bbl in 1Q2024.

BACKDROP

The BOJ is now the only major central bank that still maintains negative benchmark rate in the front end at -10 bps in the money markets.

To the BOJ's credit, Governor Ueda has been doing his best to highlight the risk of BOJ's imminent normalization of monetary policy and potentially unwinding of "Yield Curve Control" (YCC). At a recent candid interview with the Yomiuri Shimbun, Governor Ueda spoke of his desire for "a quiet exit" to easy monetary policy.

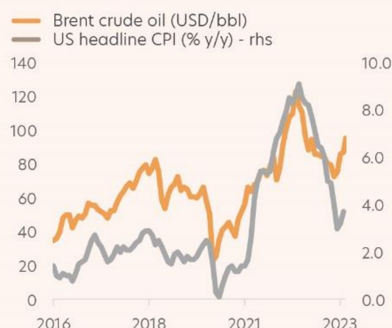
Indeed, our view is that the BOJ is poised to lift front end benchmark rates above zero in 1Q24 and thereafter gradually normalize YCC by lifting the 10Y Japanese Government Bond (JGB) yield progressively above 1.0% across 2024.

BACKDROP

China's announcement late last year that it is exiting "zero-Covid" was greeted with much initial enthusiasm. However, the anticipated post-Covid recovery across 2023 fell flat and did not materialize. Externally, China's exports continued to contract amidst difficult external trade environment, ongoing US-China tensions, and supply chain shifts. Domestically, consumption and spending failed to pick up as retail sentiment stayed weak. Amidst both external and domestic challenges, China's property sector continues to grapple with its large debt load with key developers teetering near default as they struggle with their refinancing.

Although a full recovery is far from certain, we believe that various fiscal stimulus and monetary policy easing will help China's economy to stabilize across 2024 and sustain GDP growth just above the critical 5% handle in 2023.

Will climb in crude oil price back to USD 100/bbl trigger renewed inflation?



IMPACT

Needless to say, this renewed rise in crude oil and energy prices comes at a rather inconvenient time when the global economy is just about to get inflation under control.

Major central banks like the Fed and European Central Bank (ECB) are just reaching the tail end of their synchronized rate hiking cycle.

This renewed rise in Brent prices back up towards the USD 100/bbl handle runs the risk of keeping inflation sticky and potentially prolonging the rate hiking cycle and weighing down on global economic recovery in 2024. At the very least, renewed strength in energy prices reinforces the consensus expectation that global rates will stay "higher for longer".

What happens after 10Y JGB yield crosses 1%?

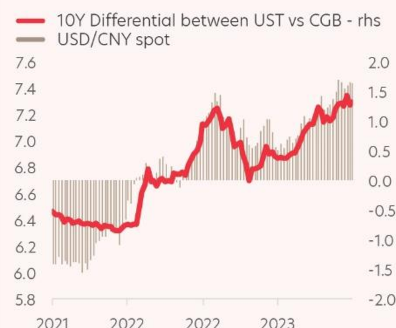
IMPACT

Since late last year, investors have been anticipating and positioning for the unwinding of BOJ's Yield Curve Control.

In fact, alongside the climb in 10Y JGB yields, the forward looking swap rate has been targeting the 1% handle. The concern here is that the BOJ may not be able to effect an orderly normalization or "quiet exit", and JPY rates may jump instead, injecting renewed and unwelcomed volatility into the global financial markets.

If JBG yield and JPY rates do jump, this may trigger renewed strength in the JPY, causing the unwinding of the JPY carry trade and this may consequently affect global risk asset prices negatively.

CNY weakens in line with rising 10Y yield differential for the USD



IMPACT

As a result of the PBOC's easing cycle to address China's economic weakness, the CNY has been losing critical interest rate support.

Specifically, the 10Y yield differential for USD/CNY deteriorated against the CNY to more than 1.5% in the USD's favor. This together with increasing worries of China's economic slowdown resulted in USD/CNY shooting higher above 7.30 across 3Q23. This excessive CNY weakness has the effect of prolonging USD strength, weighing down on both key Asia and ASEAN FX.

We now see USD turning lower only in 1Q24. Needless to say, persistent USD strength adds to offshore debt burden for Asian corporates and may slow down the anticipated economic recovery.

FX Strategy: "Higher For Longer" Buys Time For The USD

While we maintain a long-term bearish view on the USD against developed economies (DM) peers, there is likely a last hurrah for the USD in the near term. Resilient US data gives the Fed the runway to keep US rates restrictive and elevated for awhile longer, supporting the USD. Our macro team has also pushed back the timing of the Fed's first rate cut to 2Q24 from 1Q24 previously, in line with market expectations. The trimming of near-term rate hike expectations of other central banks such as the European Central Bank (ECB) and Bank of England (BOE) meant that the USD will get to keep its interest rate advantage over its DM peers awhile longer before the Fed's rate cut cycle narrows the advantage. Overall, we expect the USD to hold its strength against most Major FX peers (except JPY) in 4Q23 before weakening starting 1Q24 as Fed's rate cut speculation intensifies. As such, our updated forecasts for EUR/USD, GBP/USD and AUD/ USD for 3Q24 are 1.14, 1.34 and 0.69 respectively.

Most Asia FX fell against the USD in 3Q23 as the CNY fell to 7.35 /USD, the weakest since late 2007. Chinese authorities have responded with further interest rate cuts and other policy measures to boost domestic demand, stabilize the property market, and address the local government debt risks. Despite the signs of stabilisation, the CNY is not likely to rebound strongly as yet until the wide monetary policy divergence between the Fed and PBOC starts to narrow next year when Fed's rate cut speculation intensifies. Going forth, we expect USD/Asia and USD/CNY to peak in 4Q23 as China's sentiment

and macro data stabilise further, followed by trading lower across 2024 as broad USD weakness start to exert again. As for the SGD, as the CNY stabilises and regains footing, the SGD is expected to bottom and rebound as well, albeit in a modest way as the Monetary Authority of Singapore (MAS) is unlikely to raise the pace of the appreciation of the S$NEER further in Oct. Overall, our updated forecasts for USD/CNY and USD/SGD for 3Q24 are 6.90 and 1.31 respectively.

Rates Strategy: It Is Largely A Waiting Game Now

Accounting for Sep FOMC, our US macro team expects one further rate hike in Nov 2023 for a peak Fed Funds rate of 5.75% in this tightening cycle. The Fed Funds rate is expected to stay at this plateau for the rest of 2023. Thereafter, we expect a US easing cycle to kick off in 2024 and extending into 2026. Our updated Fed view is less dovish than the previous iteration and while we still anticipate the cycle turning lower, this rate easing view is based on the prevailing policy rate level being restrictive and does not assume a severe retrenchment in economic growth. In the event of a meaningful negative growth shock, the policy rate will probably undershoot deeper into accommodative territory. As it stands, we have factored in 75bps of rate cuts across 2024 while futures market pricing as of 21 Sep is also similarly priced with around 70bps baked in. Over the full cycle, we have a more dovish profile for Fed Funds compared to prevailing market pricing. Specifically, our easing cycle bottom for Fed Funds sits at 3.25% which is 75bps lower than the futures market price of around 4.00%.

Overall, given our updated FFTR forecast of 5.25% in 3Q24 (from the previous forecast of 4.25%), we have updated our entire suit of interest rate forecasts. Specifically, we now see 3M compounded SOFR at 5.23% in 3Q24 (from the previous forecast of 4.23%) and we have also raised the forecast for 10Y US Treasuries yield to 4.10% (from the previous forecast of 3.45%). Consequently, it is important to note that we now see 3M compounded SOFR and 10Y US Treasuries yield staying above 5% and 4% respectively in the coming 4 quarters till 3Q24. Similarly, for SG rates, the forecast for 3M compounded SORA and 10Y SGS yield has been raised to 3.80% and 3.35% respectively for 3Q24. Details in updated table hereafter.

Commodities Strategy: Supply Squeeze Triggers Strong Rebound In Brent Crude Oil In 3Q23

In early Sep, we raised our price forecast for Brent crude oil by USD 5 / bbl to the USD 90 to 95 / bbl price range. This was after Saudi Arabia surprised by extending their unilateral production cut of 1 mio bpd to the end of the year. This action from Saudi Arabia contributed to further supply squeeze which will propel Brent crude oil price higher towards USD 95 / bbl. For more details, kindly refer to Commodities Strategy note: "Brent To Climb Further To USD 95/bbl As Saudi Arabia Keeps Up Supply Squeeze" dated 06 Sep 23. Since then, over the past month, Brent crude oil has climbed confidently beyond USD 90 / bbl to trade above the USD 93 / bbl level. The key positive drivers that we have mentioned previously remained in force and in some cases have intensified. Firstly, Saudi Arabia and OPEC+ have kept up the supply squeeze. Secondly, US economy has performed better-than-expected with stronger GDP growth of nearer to 3% now seen this year. Thirdly, the concurrent crude oil inventory drawdown in the US has intensified amidst evidence of stronger economic growth. Overall, our view is that the abovementioned positive drivers have intensified, and Brent is now ready to test the USD 100 / bbl headline resistance. We therefore raise our price forecast by yet another USD 5 / bbl to the USD 95 to 100 / bbl range. We now forecast Brent price at USD 95 / bbl in 4Q23 and 1Q24, followed by USD 100 / bbl in 2Q24 and 3Q24.

For gold, we maintain our view of an eventual sustained break above USD 2,000 / oz. Gold remains a key diversifier of portfolio risk and current headwinds of strong USD and higher long-term yield should reverse next year, turning into key tailwinds for renewed rise in gold price. We forecast gold at USD 2,000 / oz in 4Q23 and 1Q24, followed by USD 2,100 / oz in 2Q24 and 3Q24. For Copper, at the risk of stating the very obvious, there is no price cartel for Copper, like in crude oil to curtail supply. As such, Copper is vulnerable to near term downside risks ahead of the stabilization of growth outlook for China over the medium term in 2024. As such, we maintain our mild negative outlook for Copper, forecasting USD 8,000 / MT for 4Q23 and 1Q24, thereafter USD 7,000 / MT for 2Q24 and 3Q24.

Asset Allocation

Most risky assets consolidated in the third quarter although the magnitude of sell-off was modest. The MSCI World index corrected 3.3% after rising over 15% in 1H 2023. The US Treasury 10-year yield traded above 4.5%, bringing the total return for a Treasury index to negative. This represents the third year of negative return for US Treasuries, a phenomenon not seen in the past 50 years. On a more positive note, Chinese equities traded broadly in line during the recent quarter despite a lack of policy support. The USD index traded higher against most currencies while the commodity complex stayed firm, led by the energy sector.

The key economic trend in 2023 was US exceptionalism. Despite being the first developed economy to raise interest rates, the US economy has outperformed most advanced economies and averted a much-anticipated recession in 2023. Moreover, inflation has managed to trend lower despite a strong labor market.

Such an outcome is exceptional by historic standards; one should caution against the conclusion that a goldilocks economy is in the making. US economic strength was partly contributed by strong fiscal impulse led by the Inflation Reduction Act and the Chips Act. Going into 2024, these effects are likely to fade at a time where the tight monetary policy will wield the most restraint (Fig. 1). On the inflation front, several one-off events contributed to a faster-than-expected decline. This may result in inflation print inflecting higher before returning to the Fed's target rate of 2%.

Figure 1 – US 10Y Real Yields Have Broken Out

Source: Macrobond, UOB Private Bank, Federal Reserve

Over in China, despite policy disappointment, equities have paused its underperformance in the third quarter. This may be a first sign that bearish selling has reached a nadir. Even without meaningful support, the Chinese economy appears to be stabilizing, led by the manufacturing sector.

Meanwhile, **the property sector is still challenged on multiple fronts amid a liquidity crunch**. The lack of state support may reflect the Chinese government's agenda to eventually downsize the industry. Given the sizeable contribution of the real estate sector to the real economy, China may face continued growth headwinds.

However, the short-term cycle may be inflecting with global manufacturing activity recovering. Against a backdrop of depressed valuations, there could be a window of short-term outperformance for Chinese risk assets.

The inevitable slowdown of the US economy suggests that the prospective risk-adjusted returns for both the short-end and long-end fixed income markets are attractive. I**nvestors should use the current elevated long-term rates to build positions in high-quality bonds.** These assets will prove useful in a growth slowdown as Fed policy rates peak.

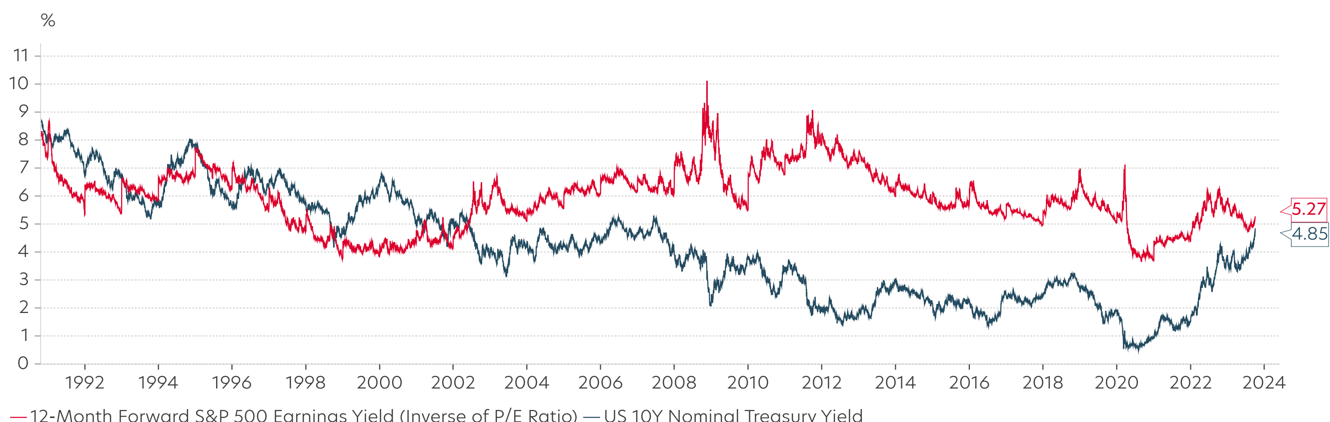
In the light of high risk-free returns, equities will have a higher wall to scale (Fig. 2). The AI-led rally may have room to run but positioning has become incrementally crowded. Hence, **markets may peak in the short term as valuations both on earnings and against bond yields are no longer attractive.**

Right By You

From a tactical perspective, **we have reduced equities in a mixed asset portfolio to a slight underweight, reflecting near-term challenges**. Having said that, given our expectations for a broadly resilient earnings outlook with the prospect of a mild recession, any sell-off is likely to be moderate; **investors can consider taking advantage of the range-bound trading pattern.**

Figure 2 – What Compensation Over Risk-Free Rate?

Source: Macrobond, UOB Private Bank, Federal Reserve



While Chinese assets are oversold and trade at attractive valuations, a strong catalyst remains absent. As such, stocks are expected to stay range-bound in the near term. In our view, it is difficult to anticipate the timing and scale of any tangible government response. While valuations can support downside risks, **the upside potential is unlikely to be realized until a more forceful breakthrough in Chinese policy support.**

Given these developments, **investors should stay diversified with principally an anchor to high-quality bonds and short-term money market which pay attractive yields and some diversification into private assets with a focus on private credits.**

In the short term, **a non-directional participation in equities may be optimal, be it through selected hedge fund strategies or structured payoffs**. This will solve for a return structure that offers positive real returns and resilience against an economic slowdown going into 2024.

Asset Allocation Table (4Q 2023)

Asset Classes	U/W	N	O/W
Equities	• ←	○	
United States		•	
Europe	•		
Japan			•
EM (Asia)		•	
Fixed Income			•
DM IG			•
DM HY	•		
EM IG			•
EM HY		•	
Alternatives			•
Hedge Funds			•
Private Markets		•	
Crude Oil			•
Base Metals	○ →	•	
Precious Metals		•	← ○
Cash	○ →	•	

Right By You

Equities

MSCI US (+12.2%) has outperformed broad markets year to date (as of 30 Sep 2023). The year-to-date gains have been impressive, catching many investors by surprise amidst an increasingly restrictive Fed policy.

In particular, the US Big Tech stocks have held up well against a backdrop of higher-for-longer Federal Funds Target Rate (FFTR) despite being long-duration assets. This economic resilience can primarily be attributed to the net fiscal thrust led by President Biden's administration over the past two years, higher productivity growth post pandemic-related collapse and a mini manufacturing capex boom related to onshoring.

Having said that, there are several risks.

First, the effect of US fiscal stimulus is likely to fade.
Second, excess household savings have largely been depleted.
Third, monetary policies work with long transmission lags.

US real rates and costs of capital have moved deeper into the restrictive zone at a time when growth risks are mounting against a still-rosy economic picture. Against this backdrop, markets have been adjusting to higher real yields, as in the case through 3Q 2023.

With US equities having rallied primarily on valuation re-rating and elevated bond yields posing as a hurdle for further multiple expansion, **earnings growth will have to do the heavy lifting.** Having said that, fiscal tailwinds which have supported the GDP so far are likely to diminish over time. In this vein, US earnings resilience will be tested. Looking ahead, diversification and selectivity will be key.

On the positives, equity returns have tended to end in the positive region in the final quarter of the year. Positive seasonality effects suggest scope for some upside following market consolidation in 3Q 2023. In addition, US earnings momentum could improve from here following some signs of stabilization.

While we still like selected quality growth stocks for their steady free cash flows and AI productivity gains, we have toned down our bullishness amid elevated real yields and incrementally crowded positions. Defensives like Healthcare still have a role to play as portfolio stabilizers. Finally, we are constructive on selected cyclicals like the Energy sector in which global supply deficit can put a floor to crude prices. Investors can consider tapping on structured payoffs. **We stay Neutral on the US equities.**

MSCI Europe (+5.4% in USD terms) continued to trail behind the US and Japan year-to-date (as of 30 Sep 2023). Our underweight call has panned out well. It is worth noting the euro has more than given back all its gains against dollar through June and July by the end of 3Q 2023.

Eurozone manufacturing PMIs remain stuck in recessionary zone, pointing to a growth stall. Given China's economic malaise amidst lackluster domestic demand and a property slump, the Eurozone economies can expect no meaningful uplift from its exports to the supposed economic powerhouse. Concerns about Chinese growth and sharp rises in developed market (DM) bond yields fed through to the European equities.

As PMI softness persists and supply chains normalize, corporate pricing power is set to roll over; this is evident in Europe's weakening corporate intentions to raise prices amidst weaker final demand. Finally, the impact of higher corporate borrowing costs is poised to be more pronounced going into 2024.

The latest Eurozone PMIs point to forthcoming earnings downgrades. Stagflation could be a harsh reality for Europe, especially since they have not had the benefit of fiscal expansion or a recovery in productivity. Broadly, **defensive sectors like Utilities and Consumer Staples are expected to hold up better on resilient earnings and relative earnings momentum.**

Investors can consider taking advantage of the recent market consolidation and spikes in volatility using structured notes for better risk-reward. **Selected high-quality growth companies with strong pricing power and steady free cash flows have corrected meaningfully**; these names could be potential candidates for the underlying.

We also like integrated oil majors amidst tight crude supply and Utilities stocks riding on the structural theme of renewable transition. Given the still-lackluster earnings growth outlook as well as ECB's potential monetary overkill, we remain Underweight on European equities.

MSCI Japan (+9.1% in USD terms) has outperformed all regional markets except the US (as of 30 Sep 2023). The year-to-date USD returns have been impressive considering the yen's dramatic depreciation by ~12% since the start of this year.

Japan's equities held up well through 3Q 2023, trading in a range-bound fashion. We have been constructive on Japan's equities given improving manufacturing PMI, yen weakness, ultra-easy monetary policy as well as steadily rising inflation. Equity valuations have trended higher, encouraged by Tokyo Stock Exchange's drive for corporate reforms and share buybacks.

Finally, **Japanese equities have also benefitted from foreign portfolio inflows as institutional funds look to diversify away from China within their Asian equity allocation; we expect this trend to persist.**

Corporate pricing power has been improving as companies continue to pass on rising raw material costs to households. Having said that, it is important to pick firms with staying pricing power as BOJ's monetary policy looks to normalize and global growth slows down.

Meanwhile, overshoots in Japanese banks could persist on expectations for the unwinding of YCC beyond any profit-taking. Finally, **we see selective opportunities in tech following the latest correction cycle**; investors can consider defensive participation via structured products to improve risk-reward. **We remain Overweight on Japanese equities.**

MSCI Asia ex-Japan (-2.4% year-to-date in USD terms) slumped through 3Q 2023, dragged by MSCI China (-9.2% year-to-date in USD terms) which languished after a strong start (as of 30 Sep 2023).

Our view to reduce Chinese positions on stimulus-related relief rallies has panned out well. As mentioned, China's policy reflation efforts have been lackluster given the drip-feed fiscal stimulus. Private-sector firms continued to struggle on weak domestic demand while green shoots in Chinese housing activity are fading. Coupled with chronic household over-saving, the broad outlook is bond-bullish especially as China exports deflationary pressures globally.

The silver lining is the Chinese government recognizes more needs to be done to reinvigorate their economy and has vowed to offer more forceful support. Chinese industrial profits rose in August for the first time in more than a year. Meanwhile, rising import volumes of commodities suggest infrastructure spending is likely to gain momentum. Manufacturing activity has contracted at a slower pace, indicating the economy is showing some signs of stabilization.

With low equity valuations cushioning downside, Chinese equities can continue to trade in a range-bound fashion with potential short-term outperformance. Bright spots are emerging in the consumer sector, with food and travel-related spending rebounding strongly. China's Golden Week will be an important gauge on consumer spending recovery. Overall, **we remain Neutral on EM Asian equities.**

Fixed Income

DM Investment Grade (IG) proxied by US Corporate IG closed flat year-to-date (as of 30 Sep 2023), underperforming its DM High Yield (HY) peer. Although spreads have tightened for the most of this year, DM IG total returns were offset by negative Treasury returns. Despite holding the policy rate at the Sep 2023 FOMC, the US Fed has turned incrementally hawkish.

The Fed's current policy stance reflects their willingness to sacrifice growth to gain conviction that inflation has been tamed. The Fed Dot plot signals one more rate hike in 2023 and that the policy rate could stay above 5% next year. The Fed's higher-for-longer narrative has materially curbed previous expectations for rate cuts in 2024.

Given the macro headwinds, it is essential to lock in yield carry without sacrificing credit quality. We expect one more 25 bps Fed rate hike in Nov 2023 FOMC and an extended pause thereafter. Fed rate cuts are expected to be delayed till mid-2024.

Stringent credit selection remains key to portfolio stability; we prefer favorable bond structures from issuers with strong credit fundamentals. **We remain Overweight on DM USD IG.**

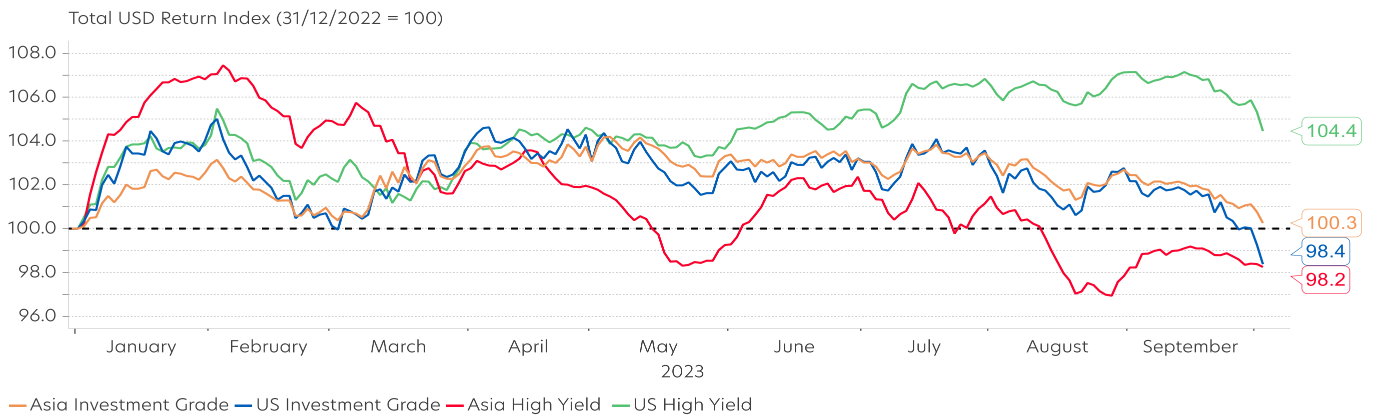
DM High Yield (HY) saw +5.9% USD total returns year-to-date (as of 30 Sep 2023), outperforming all its peers. Despite higher anticipated default rates, HY credits have held up well thus far on resilient US consumer spending. Energy issuers have also benefited from surging crude prices. Spread compression more than offset the negative Treasury returns, culminating in positive total returns through the first three quarters of the year.

Looking ahead, we see growth risks rising as effects of US fiscal thrust fade and excess US household savings diminish. On this note, we can already see meaningful HY spread widening taking its course (blue line, chart on bottom right).

Funding and liquidity conditions are set to tighten from here on DM central bankers' higher-for-longer rates narrative. Given the potential for credit spreads to widen further on rising default rates, **we remain Underweight on DM USD HY.**

Fixed Income Year-To-Date Performances

Source: Macrobond, UOB Private Bank



Source: Macrobond, UOB Private Bank

EM Asia Investment Grade (IG) credits saw +1.1% USD total returns year-to-date (as of 30 Sep 2023), outperforming its EM Asia High Yield (HY) peer. Despite spread tightening since Mar 2023, total returns have largely been offset by the Fed's higher-for-longer interest rates stance.

We remain constructive on EM Asia IG credits given their role as portfolio stabilizers in the event of market dislocations; they can help to cushion drawdowns in riskier assets. Inclusion of Asia IG credits into a balanced portfolio makes strategic sense given the elevated yields against a backdrop of rising uncertainty and market volatility.

We reiterate preference for selected quality credits within Asian Financials, quasi-sovereigns, strategic Chinese state-owned enterprises (SOEs) and Indonesian Utilities.

We continue to emphasize taking a diversified approach in terms of duration management, preferring an average modified duration of 5-8 years at the overall bond portfolio level. In our view, current all-in yield levels are attractive; investors should consider locking them in boldly. As with DM IG, Treasury returns will have to do the heavy lifting in total return contribution given relatively tight spreads at current levels. We reiterate a buy-on-dips stance to lock in higher yield carry at opportune times. Overall, **we remain Overweight on EM Asia IG.**

EM Asia High Yield (HY) saw -1.6% USD total returns year-to-date (as of 30 Sep 2023), underperforming all its peers. Looking ahead, investor sentiment in this space will largely be affected by Chinese policy measures and the outlook on China property sector which remains under huge liquidity pressure.

A silver lining would be that the Chinese government has signaled its intention to offer more forceful policy support. Having said that, we continue to advocate caution, selectivity and diversification while placing emphasis on issuer survivorship. We reiterate preference for selected Indonesian property developers and Indian commodity traders. Overall, **we remain Neutral on EM Asia HY.**

Right By You

FX, Interest Rate & Commodities Forecasts

FX	21 Sep	4Q23F	1Q24F	2Q24F	3Q24F
USD/JPY	148	146	140	135	132
EUR/USD	1.07	1.06	1.09	1.12	1.14
GBP/USD	1.23	1.23	1.28	1.32	1.34
AUD/USD	0.64	0.64	0.66	0.68	0.69
NZD/USD	0.59	0.59	0.60	0.62	0.63
DXY	105.48	105.3	102.3	99.6	97.9
USD/CNY	7.30	7.30	7.10	7.00	6.90
USD/HKD	7.82	7.85	7.83	7.80	7.80
USD/TWD	32.15	32.0	31.5	31.0	30.5
USD/KRW	1,337	1,340	1,300	1,280	1,260
USD/PHP	56.78	57.0	56.0	55.0	54.0
USD/MYR	4.69	4.70	4.55	4.48	4.42
USD/IDR	15,388	15,400	15,100	14,800	14,500
USD/THB	36.14	36.3	35.3	34.5	34.0
USD/VND	24,323	24,500	24,000	23,800	23,600
USD/INR	82.92	83.0	82.0	81.0	80.0
USD/SGD	1.37	1.37	1.34	1.32	1.31
EUR/SGD	1.46	1.45	1.46	1.48	1.49
GBP/SGD	1.68	1.69	1.72	1.74	1.76
AUD/SGD	0.88	0.88	0.88	0.90	0.90
SGD/MYR	3.43	3.43	3.40	3.39	3.37
SGD/CNY	5.34	5.33	5.30	5.30	5.27
JPY/SGDx100	0.92	0.94	0.96	0.98	0.99

POLICY RATES	21 Sep	4Q23F	1Q24F	2Q24F	3Q24F
US Fed Fund Rate	5.50	5.75	5.75	5.50	5.25
JPY Policy Rate	-0.10	-0.10	0.00	0.00	0.00
EUR Refinancing Rate	4.50	4.50	4.50	4.25	4.00
GBP Repo Rate	5.25	5.25	5.25	5.00	4.75
AUD Official Cash Rate	4.10	4.35	4.35	4.00	3.75
NZD Official Cash Rate	5.50	5.50	5.50	5.25	5.00
CNY 1Y Loan Prime Rate	3.45	3.35	3.35	3.35	3.35
HKD Base Rate	5.75	6.00	6.00	5.75	5.50
TWD Official Discount Rate	1.88	1.88	1.88	1.88	1.88
KRW Base Rate	3.50	3.50	3.50	3.25	3.00
PHP O/N Reverse Repo	6.25	6.50	6.50	6.25	6.00
MYR O/N Policy Rate	3.00	3.00	3.00	3.00	3.00
IDR 7D Reverse Repo	5.75	5.75	5.75	5.75	5.50
THB 1D Repo	2.25	2.50	2.50	2.25	2.00
VND Refinancing Rate	4.50	3.50	3.50	3.50	3.50
INR Repo Rate	6.50	6.50	6.50	6.50	6.50

INTEREST RATES	21 Sep	4Q23F	1Q24F	2Q24F	3Q24F
USD 3M SOFR (compounded)	5.24	5.43	5.55	5.45	5.23
SGD 3M SORA (compounded)	3.71	3.92	3.95	3.92	3.80
US 10Y Treasuries Yield	4.49	4.30	4.30	4.20	4.10
SGD 10Y SGS	3.41	3.40	3.40	3.40	3.35

COMMODITIES	21 Sep	4Q23F	1Q24F	2Q24F	3Q24F
Gold (USD/oz)	1,925	2,000	2,000	2,100	2,100
Brent Crude Oil (USD/bbl)	94	95	95	100	100
LME Copper (USD/mt)	8,194	8,000	8,000	7,000	7,000

Source: UOB Global Economics & Markets Research Estimates

Disclaimer

This publication is strictly for informational purposes only and shall not be transmitted, disclosed, copied or relied upon by any person for whatever purpose, and is also not intended for distribution to, or use by, any person in any country where such distribution or use would be contrary to its laws or regulations. This publication is not an offer, recommendation, solicitation or advice to buy or sell any investment product/securities/instruments. Nothing in this publication constitutes accounting, legal, regulatory, tax, financial or other advice. Please consult your own professional advisors about the suitability of any investment product/securities/ instruments for your investment objectives, financial situation and particular needs.

The information contained in this publication is based on certain assumptions and analysis of publicly available information and reflects prevailing conditions as of the date of the publication. Any opinions, projections and other forward-looking statements regarding future events or performance of, including but not limited to, countries, markets or companies are not necessarily indicative of, and may differ from actual events or results. The views expressed within this publication are solely those of the author's and are independent of the actual trading positions of United Overseas Bank Limited, its subsidiaries, affiliates, directors, officers and employees ("UOB Group"). Views expressed reflect the author's judgment as at the date of this publication and are subject to change.

UOB Group may have positions or other interests in, and may effect transactions in the securities/instruments mentioned in the publication. UOB Group may have also issued other reports, publications or documents expressing views which are different from those stated in this publication. Although every reasonable care has been taken to ensure the accuracy, completeness and objectivity of the information contained in this publication, UOB Group makes no representation or warranty, whether express or implied, as to its accuracy, completeness and objectivity and accept no responsibility or liability relating to any losses or damages howsoever suffered by any person arising from any reliance on the views expressed or information in this publication.