Quarterly Investment Outlook
First Quarter 2018

MARKET REVIEW

Global stocks extended the year's rally in the final quarter of 2017. Equity investors were well rewarded the past year as global economic growth picked up more convincingly. In a first since the establishment of the MSCI World equity index in 1987, there were equity gains in every single month as volatility plumbed record lows throughout the year. Cyclical sectors outperformed defensive ones as risk appetite picked up. Our growth bias in US and Europe benefitted from an underweight in utilities, particularly in December when the rate-sensitive sector fell further as the Fed raised interest rates. Global bonds also did well the past year. The combination of improved growth outlook, benign inflation, and modest tightening of monetary policies, have pushed fixed income valuations higher alongside equities. We are cognizant of a more challenging market environment in 2018, and expect potential inflection points that would create opportunities for our asset allocation strategy.

The **US** S&P 500 index gained 6.6% in Q4, led by the more cyclical (economically-sensitive) sectors – tech, consumer discretionary, and financials all contributed strongly. More recently, energy was supported by stable oil prices, and financials by the continuation of monetary policy tightening. The passing of the highly anticipated tax reform bill did not move markets meaningfully, as expectations were already priced in previously. While growthier tech stocks continued to outperform, a bout of volatility in December signalled potential market rotation away to relatively less expensive sectors. Utilities fell out of favour as interest rates rose, and exacerbated by potential legal costs arising from the California wildfires.

Europe eked out small gains in Q4. Commodity-related stocks were the main contributors on the back of strong metal and oil prices - Glencore, Royal Dutch Shell, and BP all surged more than 10%. Utilities fell together with the global utility index, declining more than 3% in December. Stock returns continue to be meaningfully affected by currency movements. Our currency-unhedged positions benefitted as the EURUSD pair gained 1.6% over the fourth quarter, adding to returns.

Japan equities surged in the fourth quarter, gaining 8.5%. The prevailing inverse equity-currency relationship weakened - the Japanese yen advanced together with equity prices; rising 3.6% and 19.7% over the year, respectively. This can be attributed to the depreciating dollar, as well as improving corporate fundamentals. The latter can be seen as more structural than transitory, and may be the catalyst for the Bank of Japan (BoJ) to finally scale back on their accommodative monetary policy.

Asia Pacific ex Japan returned 33.5% in 2017, and did so with persistently low volatility (between 8-10%) not seen in the last 30 years. Return drivers were also concentrated: Out of 647 stocks in the index, the top four gainers - Tencent, Alibaba, Samsung, and Taiwan Semiconductor – all within the Information Technology sector, contributed to one quarter of the region's gains for the entire year. While low levels of volatility do not necessarily portend market crises, they do indicate market confidence (even complacency?) in future outcomes. Disappointment in growth (as embodied by the tech giants) is expected to reverse such optimism.

Emerging Markets gained 7.1% in Q4, benefiting our overweight in the region. Energy commodities and industrial metals picked up momentum towards the second-half of the year, supporting the commodity-related markets. Brazil and South Africa both gained more than 20% in 2017. Crude oil (WTI) prices rose above $60 for the first time since 2015 on firm demand and expectations that the OPEC oil cartel will continue to support prices.

Sovereign bonds in the major markets continued their steady gains through the year, though short-dated US bonds started to grind down on the back of monetary policy tightening. The US Fed raised rates by another 0.25% in December, bringing the target range of Fed Funds rate to 1.25% - 1.50%. In Europe, the ECB announced it would halve its bond-buying program in its Quantitative Easing (QE) from €60bn to €30bn a month starting from January. Inflation-linked government bonds outperformed on expectations of higher inflation in the medium term, especially in the Euro area.

Within **Investment Grade bonds,** corporate debt outperformed sovereigns. Credit spreads tightened on favourable corporate earnings and low corporate default rates. Large corporate issuance was absorbed with little problem. Energy-related debt rallied (spreads compressed on the lower perceived risks) over the quarter as oil prices trended upwards.

Emerging Market bonds gained in the quarter, driven by improving fundamentals in Russia and Brazil. Stronger commodity prices and low inflation was supportive for their economies. Despite record issuance and hard currency debt supply from both the sovereign and corporate sectors, strong demand was able to contribute positively to returns.

Asia bond gains were in line with expectations; similarly supported by improving fundamentals and economic growth. Inflationary pressures remained muted in Asia, which was positive for the bond markets. On the back of steady capital inflows, South Korea and Malaysia registered strong positive returns as their currencies rallied strongly against the US dollar. In line with the general positive environment for credit products, hard currency (USD) Asian bonds also saw positive returns.

High yield bonds performed well over the year in a favourable macro environment. Rising commodity prices have also been positive for the high yield sector. After posting strong gains for most of 2017, and with spreads close to their historical lows, there was some profit taking as reflected in widening of spreads. Consequently, high yield bonds underperformed investment grade bonds over the last quarter.

OUTLOOK AND ASSET ALLOCATION STRATEGY

GLOBAL ASSETS

Global Assets	--	-	=	+	++
Equity			▲		
Fixed Income			▲		

Note:
--: Underweight | -: Slight Underweight | =: Neutral | +: Slight Overweight | ++: Overweight

Equity: Neutral

Global equities have continued to surge upwards, pushing valuations closer to their historical highs. Earnings expectations continue to be optimistic, though still supported by strong earnings. While we would not rule out a continuation of the rally, earnings will need to continue to grow convincingly for equities to remain in favour. We stick to our neutral stance on equity relative to fixed income.

Looking past the current inflated asset prices, the investment landscape has continued to look positive. Monetary policy is still largely accommodative in a low inflationary environment, and global economic activity has continued to pick up. We favour areas of the market which may thrive in the current landscape, and where valuations are more attractive.

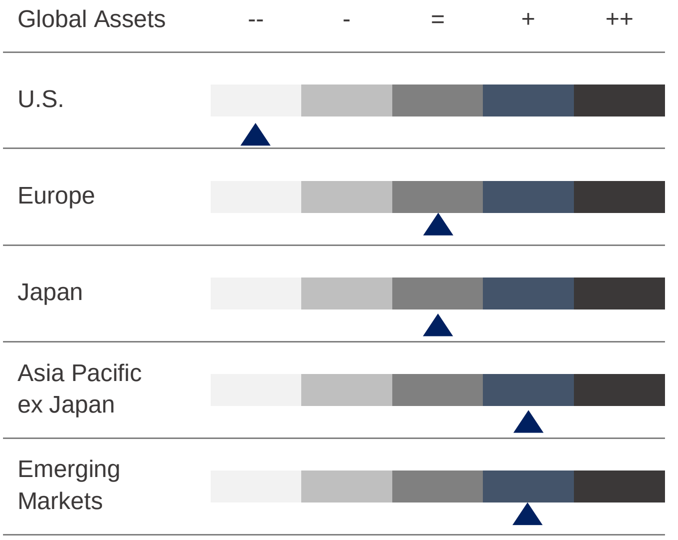
Fixed Income: Neutral

Default risks remain low as corporate fundamentals continue to improve. Demand for loans should continue to be supported as economic activity picks up.

Inflation has been elusive, spurring demand for longer dated bonds and keeping the bond bears at bay. That said, declining unemployment in the major markets putting pressure on wages, and rising commodity prices can create an upside surprise on inflation that is not priced in. This cycle is not favorable for fixed income assets – we have observed gains starting to moderate over the past few months.

Our underweight in duration will help reduce the sensitivity to interest rate movements, while focusing on extracting returns from coupon. Within the different segments, we favor emerging markets with fundamental tailwinds and where valuations are less stretched.

EQUITY



Note:
--: Underweight | -: Slight Underweight | =: Neutral | +: Slight Overweight | ++: Overweight

United States: Underweight

The Fed raised rates in December, citing the stronger economy and low unemployment rates. Continued growth amid gradual tightening should continue to be supportive for US equities.

The tax reform bill is positive for equities in the long run - a reduction of the corporate tax rate would benefit companies that have paid a higher tax rate. Our bias to small cap growth companies would benefit, though their historically high valuations could tamper gains going forward.

In view of these stretched valuations, we reduce our exposure to the small cap growth sector, and initiate a position in the financial sector where valuations have more room to run. Financials are also expected to benefit from a reduction in corporate taxes, and from higher interest rates.

Japan: Neutral

Japanese stocks look increasingly promising on improving corporate fundamentals. A re-election of Shinzo Abe assured the continuation of “Abenomics”, which bodes well for equities market.

There is a sense of dependency on the BoJ, who is the majority holder of Japan’s equities through their purchases of the ETF market. Though unlikely, the central bank could surprise by announcing an early withdrawal of their stimulus programme, and risk halting the current rally. Valuations are not expensive, but in our view not compelling enough to overweight the region relative to other opportunities.

Europe: Neutral

Stock market returns in terms of the local currency have been dampened by a strengthening euro. Our currency-unhedged position means that we have benefitted from gains in foreign currency. Domestic small cap stocks could be one to watch out for, as they have been exhibiting some resilience to a stronger euro. However, the recent run-up has made a potential entry point less attractive.

The euro-zone economy has improved considerably, as reflected by strong manufacturing numbers in December. Political risks continue to plague the region, even if they have somewhat faded from the forefront. Negotiations for Brexit are set to continue in Q1. The risk of populism in Europe will continue to loom in 2018.

Asia Pacific ex Japan: Slight Overweight

The stellar run so far has been supported by earnings growth, and less on valuation re-rating. 2018 could be another good year for equities, if the region is able to at least match its forecast GDP growth of 6.2%, and consensus earnings growth of more than 15%.

The outlook on tech companies is still positive, but their valuations are 29% higher than the broader market, whereas both had similar valuations in 2015. Our Chinese A-share exposures are a safer way to play the Asian growth theme, as valuations remain low on a historical basis.

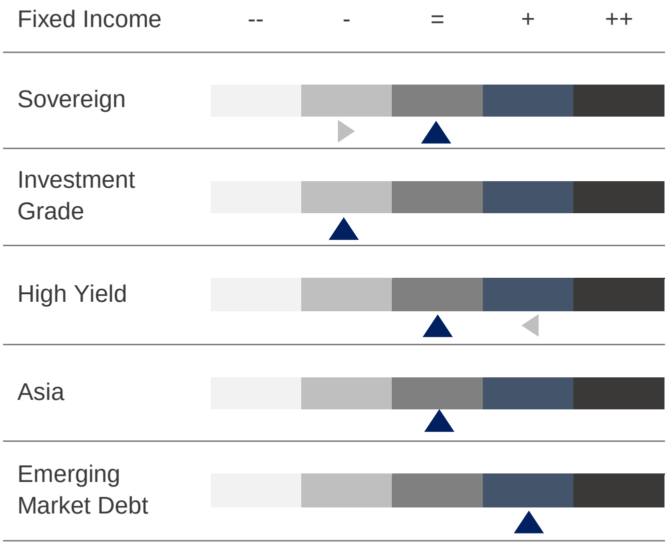
Considering strong earnings growth, and valuations – far below the peak of 2007 -, we maintain our slight overweight.

Emerging Markets: Slight Overweight

The macro landscape looks favourable for EM equities. Commodities, which are one of the main drivers in the region, have seen prices increase on strong demand. OPEC’s commitment to curb oil production has been supportive for oil prices. Geopolitical tensions in the Middle East could also disrupt oil production in the region.

China’s plan to tackle issues such as shadow banking, over-leverage, and over-capacity, is positive for growth in the long term. GDP growth has expanded at a healthy 6.5%, which would be supportive for commodities.

FIXED INCOME



Note:
--: Underweight | -: Slight Underweight | =: Neutral | +: Slight Overweight | ++: Overweight

Sovereign: Neutral

Sovereign bond yields will be driven higher by tightening of monetary policy by the Fed and ECB, two of the most influential central banks in the world. The portfolio's equity exposures are expected to benefit from the gradual rate hikes, while the rest of the fixed income portfolio is positioned more defensively.

What could derail all these is disappointment in global growth which is unable to justify current valuations. By bringing the slight underweight in Sovereign bonds back to neutral, we expect the portfolio to be more buffered against any unforeseen risk that may cause a material downturn in the markets.

Investment Grade: Slight Underweight

Strong capital investment is expected to continue, as global economies embark on a synchronized growth path. Large issuances of investment grade bonds are expected to fund these capital investments.

In this low yielding environment, investors will still continue to search for yield. However, given the tight credit spreads over sovereign bond yields, there is little room for corporate bonds to compensate the potential losses from rising sovereign bond yields. We therefore maintain our slight underweight stance.

High Yield: Neutral

High yield bonds have had a good run over the past two years. Strong macroeconomic growth, general healthy corporate earnings, low default rates, and the preference by investors to search for higher yielding instruments were the main supportive factors.

While fundamentals broadly remain supportive, we are increasingly cautious. High yield spreads are near historically tight levels. The pace of spread tightening has moderated, coupled with bouts of volatility. The tight spreads offer a small buffer to compensate for the potential price losses from rise in yields. Therefore, we want to lock in profits by trimming the slight overweight to neutral.

Asia: Neutral

Fundamentals remain supportive for Asia bonds. In 2017, there was large issuance of high yield bonds from the Chinese real estate sector. In 2018, we expect overall issuance in the Asia bond space to be high as borrowers take advantage of the low interest rate level to lock in cheap funding. Deleveraging in the Chinese corporate financial sector could weigh on the weaker tiers of banks, but the impact on the big four banks should be more limited.

Given that yields are lower than emerging markets, general tight spreads, large issuance versus favorable fundamentals, we maintain our neutral stance.

Emerging Market Debt: Slight Overweight

We expect EM debt to be supported as the favourable macro and technical backdrop exhibited in 2017 remain intact. Better outlook for commodity prices are filtering into the real economies. While there are nascent signs of rising inflation, overall pressure remains muted. Furthermore, EM central banks have more room to manoeuvre in terms of economic stimulus.

Stronger economic growth in 2018 is likely to bring about an improved balance of payments in general. Spreads continue to tighten and have more room to do so compared to other segments of fixed income. We remain slight overweight in this asset class.

RETURNS AS AT 31 DECEMBER 2017

Regional Equity	MTD	QTD	YTD
Global	1.5%	5.4%	21.6%
US	1.0%	6.1%	19.4%
Europe	0.6%	0.3%	7.7%
Japan	1.4%	8.5%	19.7%
Asia Pacific ex-Japan	2.9%	7.5%	33.5%
Emerging Markets	3.4%	7.1%	34.3%

Fixed Income	MTD	QTD	YTD
Global Investment Grade	0.3%	1.1%	7.4%
High Yield	0.2%	0.2%	6.8%
Asia	0.3%	0.5%	5.4%
Emerging Market Debt	0.4%	0.6%	8.2%

Currencies	MTD	QTD	YTD
USD/SGD	-0.9%	-1.6%	-7.7%
EUR/SGD	0.0%	0.0%	5.5%
JPY/SGD	-1.0%	-1.7%	-4.1%

Commodity	MTD	QTD	YTD
Gold	2.2%	1.8%	13.1%
WTI Crude	5.3%	16.9%	12.5%

Source: Bloomberg.
All returns in index currency terms.

Country	MTD	QTD	YTD
Australia	1.6%	6.8%	7.0%
Brazil	6.2%	2.8%	26.9%
China “A”	0.6%	5.1%	21.8%
China “H”	2.0%	7.3%	24.6%
Hong Kong	2.5%	8.6%	36.0%
India	2.7%	8.9%	27.9%
Indonesia	6.8%	7.7%	20.0%
Korea	-0.4%	3.0%	21.8%
Malaysia	4.6%	2.3%	9.4%
Russia	0.4%	1.6%	-5.5%
Singapore	-0.9%	5.7%	18.1%
Taiwan	0.8%	2.5%	15.0%
Thailand	3.3%	4.8%	13.7%

Sector	MTD	QTD	YTD
Gold equity	4.6%	2.1%	12.2%
Energy equity	4.7%	5.3%	-3.8%
Technology	-0.1%	8.1%	36.9%
Healthcare equity	-0.1%	0.6%	18.0%
Financial equity	1.8%	8.1%	20.0%

Important Notice & Disclaimers

This publication shall not be copied, or relied upon by any person for whatever purpose. The information herein is given on a general basis without obligation and is strictly for information only. This publication is not an offer, solicitation, recommendation or advice to buy or sell any investment product, including any collective investment schemes or shares of companies mentioned within. Although every reasonable care has been taken to ensure the accuracy and objectivity of the information contained in this publication, finexis advisory Pte Ltd and its employees cannot be held liable for any errors, inaccuracies and/or omissions, howsoever caused, or for any decision or action taken based on views expressed or information in this publication. The information contained in this publication, including any data, projections and underlying assumptions are based upon certain econometric assumptions, forecasts and analysis of information available as at the date of this document and reflects prevailing conditions and our views as of the date of the document, all of which are accordingly subject to change at any time without notice. finexis advisory Pte Ltd does not warrant the accuracy, adequacy, timeliness or completeness of the information herein for any particular purpose, and expressly disclaims liability for any errors, inaccuracies or omissions. 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. Nothing in this publication constitutes accounting, legal, regulatory, tax or other advice. The information herein has no regard to the specific objectives, financial situation and particular needs of any specific person. You may wish to seek advice from a professional or an independent financial adviser about the issues discussed herein or before investing in any investment or insurance product. Should you choose not to seek such advice, you should consider whether the investment or insurance product in question is suitable for you.