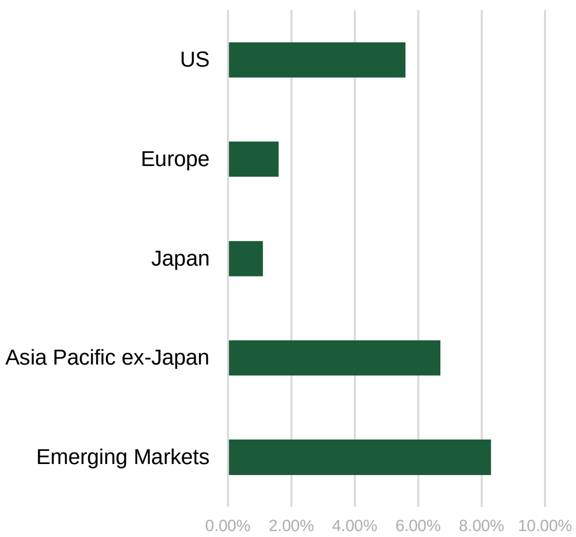
Monthly Commentary

All data as at 31 January 2018 February 2018

MARKET REVIEW

Global Equities +5.6% (USD)



Source: Bloomberg

Asia Pacific ex Japan +6.7% (USD)

Emerging Markets +8.3% (USD)

Hong Kong's Hang Seng Index surged to an all-time high, carried by the financials and information technology sectors. Though expectations for Asia's tech giants were high going into the earnings season, they were still largely achievable - Samsung announced a record $11.2 billion net income in Q4, in line with expectations.

Russia and Brazil contributed significantly to Emerging Markets returns, each gaining more than 10% when measured in USD. Oil prices have been supportive for these resource-heavy countries, stabilising above $68 (Brent Crude) after some volatility earlier in the month. Iron ore and base metals retreated from recent highs as demand growth in China paused for the winter.

US +5.6% (USD)

'FANG' stocks continue to rally alongside the tech sector – Amazon (+24%), Netflix (+40%), Google (+12%) all contributed meaningfully. Cheaper value stocks continue to lag with the exception of financials, which gained 6.5%. Economically-sensitive financials, where we recently initiated an active position, have benefitted from positive tailwinds such as rising interest rates. Despite being the main beneficiary of tax cuts, the more richly-valued small caps have continued to underperform.

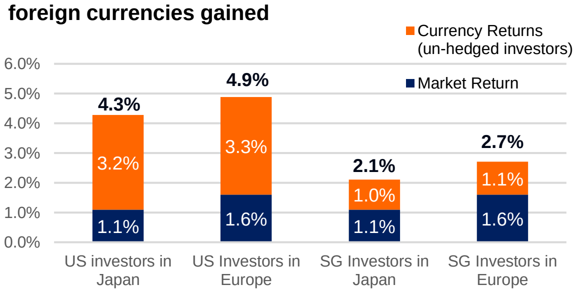
Europe +1.6% (EUR)

Our euro-exposure benefitted strongly the past month as EUR reached 1.24, boosting returns in USD terms (4.9% vs 1.6% in local currency terms). Lack of an equivalent 'FANG' in Europe gave way for financials to take centre stage, and contributing significantly to overall market returns. On a country basis, Italy is a stand-out performer – markets have so far been unconcerned about the upcoming Italy election in March, which is a potential source of risk.

Japan +1.1% (JPY)

A strong yen came into play for USD investors, who gained an additional 3.18% as the dollar weakened. The negative correlation between Japanese equities and currency – previously weakening – disappeared in January, as both equities and yen gained. Most of these gains can be attributed to the information technology and industrials sectors.

Higher returns for SGD and USD investors as foreign currencies gained



Source: Bloomberg

Sovereign bonds fell globally, driven by the rise in US treasury yields (bond yields and prices go in opposite directions) - ten-year yields rose above 2.7% for the first time since 2014. There have also been expectations that the extremely accommodative monetary policies taken by the European Central Bank (ECB) and Bank of Japan (BoJ) would not last for much longer. These expectations have the additional effect of boosting the euro and yen versus the US dollar. Surging equity prices also exerted downward pressure on sovereign bonds.

Have yields bottomed out?
10-year treasury yields rose, sending bond prices down

Source: Bloomberg

Investment Grade (IG) bonds fell, as tightening spreads were not enough to offset the overall rise in yields. Euro-area bonds declined as investors sought to move away from negative yielding bonds to higher yielding products elsewhere.

Asian bonds corrected, in line with trends in the global bond markets. USD-denominated sovereign and investment grade corporates fell. Asian high yield bonds were slightly positive, aided by tightening credit spreads. India's ten-year yields continued to rise in January, reaching 7.6%. Ample bond supply, expectations of higher inflation (especially with higher oil prices), and wider deficits were contributing factors for the bond sell-off in India.

Emerging market debt fell marginally. Argentine credits were the weakest performer, as the peso fell by about 3%. Peso weakness was driven by the central bank's two interest rate cuts in January. Venezuela bonds were a stand-out performer the past month, returning double digit returns. Venezuela bonds had previously collapsed (yields rose to around 50%) as the country failed to pay back their debt obligations - investors are betting the worst may now be over.

High Yield (HY) bonds saw positive returns, escaping the broader sell-off in fixed income. Relatively higher carry (coupons) in HY bonds, managed to offset the negative impact of rising interest rates. Higher oil prices also contributed to the positive returns in the high yield segment.

OUTLOOK AND STRATEGY

Global equity markets surged for most of January, before giving back some towards the end of the month. The 5.5% gain over one month is not typical behaviour; already representing one-quarter of last year's total returns. Growth stocks largely continued to outperform value globally, especially as the usual growthier tech suspects – Amazon, Netflix, Alibaba, Tencent, etc. – have continued to perform in line with their high expectations. Going forward, a sustained increase in interest rates (correspondingly bond yields) may dampen the attractiveness of equities – we saw a two-day rout in equities as US ten-year yields breached 2.7% towards the end of the month. Close attention is being paid to the performance of value stocks, which may benefit more from rising interest rates.

In a move widely anticipated by the markets, the **US** Fed left interest rates unchanged at their recent meeting, while setting the stage for another rate hike in March. Current expectations are for three rate hikes in 2018. That said, any signs of quickening inflation could lead to even higher rates than what has already been priced in; and risk catching the market off-guard. US small caps underperformed, even though our growth-tilt has provided some additional gains. The recent re-allocation of some small-cap exposure into financials has worked out well so far. We are on the look-out for slowing price momentum within the small-cap growth space, before deciding if a complete move away is warranted.

Our euro-unhedged positions have continued to gain as **European** investors ready themselves for a plausible start of tightening by the ECB. This is supported by a strong euro-zone economy, whose 2017 GDP reached 2.7% - even higher than the 2.5% reported in the US. In the meantime, the still accommodative monetary policy should continue to be supportive for equities, barring any political risks that may manifest in the region.

Earnings in corporate **Japan** have continued to grow in line with expectations, and should support the stock market rally. BoJ has remained committed in maintaining their ultra-accommodative monetary policy, even going as far as to boost their government bond purchases over the last week of January. This is supportive for bond prices in the shorter-term; dampening yields (and the yen) while also being positive for equities.

Equities in **Asia ex Japan** have room to climb, as long as corporate earnings and GDP growth continue to meet expectations. However, the recent strong surge in equity prices is not sustainable at its current pace; and it would not be so surprising to see a technical price correction down the road. Supportive fundamentals, and still realistic valuations should limit the magnitude of any such price declines.

Oil prices have traded near 12-month highs as the OPEC-led effort to curb oil production have managed to control supply, even as we see increasing output from the US shale oil players. Commodity prices remained firm despite pulling back from their highs in recent weeks. This is supportive for the resource-heavy **Emerging Markets**; such as Russia, South Africa and Brazil.

Global fixed income markets exhibited relatively coordinated movements, characterized by higher interest rates, tighter spreads and a weaker USD. Rising US treasury yields dented the total returns of USD-denominated bonds in January. Oil prices powered higher, benefiting energy issuers. Market volatility increased towards the end of the month as bonds sold off, triggering a decline in equity prices. We are monitoring the speed at which yields are rising, as well as any sustained increase in market volatility that may be harmful for risk assets.

Yields have grinded higher as expectations are for the major central banks to continue (Fed), or even to begin (ECB and BoJ) tightening of monetary policy. This has occurred even as central bankers have communicated an accommodative stance in policy making. After a spectacular run in 2017, the return potential for equities and spread products such as high yield bonds has diminished. Rising interest rates are likely to weigh on returns and may also introduce higher volatility. We maintain a neutral stance in **sovereign bonds** - a safe haven asset class - to cushion potential downside risk.

Fundamentals continue to be favourable for corporate debt in the near-term. That said, **IG** and **HY** bond valuations are high. Their spreads (difference in yields compared to government bonds) are near historical lows, and offer little cushion from rising interest rates. Oil prices are a supportive factor for HY bonds. Although oil prices have risen drastically in recent months, firmer global demand, as well as geopolitical risks out of the Middle East countries (such as Saudi Arabia, Iran, Venezuela, etc.) could limit the downside. Within the high yield segment, we favour the shorter-end of duration to help offset interest rate risks.

Even as growth in Asia has remained robust, we are cautious about the implications of the high levels of leverage on **Asian fixed income** products – ratio of total debt to GDP is currently upwards of 250% in China. China's deleveraging campaign is expected to weigh on lower tiered Chinese corporates and banks. Bond issuance is also likely to remain large as corporates continue to take advantage of the still low interest rates to lock in cheap funding. Indian bonds are increasingly attractive at their current high yields (about 7.6%), though faster inflation and an increasing fiscal deficit could see even higher yields from current levels.

The favourable macro conditions that have acted as a tailwind for **EM debt** are likely to remain intact in 2018. Better trade numbers on the back of higher commodities prices, stronger domestic growth and generally contained inflationary pressure means that EM debt could outperform the other fixed income asset classes. Likewise, we are biased towards short-duration to help mitigate the risk of higher interest rates.

MARKET PERFORMANCE

Regional Equity	MTD	YTD
Global	5.6%	5.6%
US	5.6%	5.6%
Europe	1.6%	1.6%
Japan	1.1%	1.1%
Asia Pacific ex-Japan	6.7%	6.7%
Emerging Markets	8.3%	8.3%

Fixed Income	MTD	YTD
Global Investment Grade	1.2%	1.2%
High Yield	0.3%	0.3%
Asia	-0.5%	-0.5%
Emerging Market Debt	-0.2%	-0.2%

Currencies	MTD	YTD
USD/SGD	-1.8%	-1.8%
EUR/SGD	1.5%	1.5%
JPY/SGD	1.3%	1.3%

Commodity	MTD	YTD
Gold	3.2%	3.2%
WTI Crude	7.1%	7.1%

Source: Bloomberg. All returns in index currency terms.

Country	MTD	YTD
Australia	-0.5%	-0.5%
Brazil	11.1%	11.1%
China “A”	6.1%	6.1%
China “H”	15.8%	15.8%
Hong Kong	9.9%	9.9%
India	5.6%	5.6%
Indonesia	3.9%	3.9%
Korea	4.0%	4.0%
Malaysia	4.0%	4.0%
Russia	8.5%	8.5%
Singapore	3.9%	3.9%
Taiwan	4.3%	4.3%
Thailand	4.2%	4.2%

Sector	MTD	YTD
Gold equity	2.0%	2.0%
Energy equity	3.8%	3.8%
Technology	7.5%	7.5%
Healthcare equity	5.6%	5.6%
Financial equity	6.4%	6.4%

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