THINK DIFFERENTLY
TO GET DIFFERENTIATED RESULTS

CIO Foreword

Picture Bill Gross and Howard Marks, not in their suits, but as seasoned sailors. Indeed, they are modern-day sailors who have successfully navigated markets. Crucially, they recognize that the journey would be long and bumpy.

If Bill Gross' New Normal represented the era of easy money, then Howard Marks' Sea Change* 15 years later marks (pardon the pun) the end of easy money. The era of easy money was so long that many investors took that to be the norm. As markets shift from one regime to another, investors cannot count on making money the same way as before. Even if one changes tack (pardon me for overdoing the sailing analogy), that is not enough.

We will still go through storms that create uncertainty and doubt. But imagine how nauseating it would be if one were to focus on every rocking wave rather than the destination on the horizon. As for the bumps along the way, be thankful for the lessons, in particular, if you did not lose a fortune to learn about markets' universal truths: greed and fear.

Another thing is for sure, so long as one perseveres with the journey, it is never a case of if, but when. At the current juncture, I cannot help but sense the stars are increasingly aligned for our investors.

Alvin Goh

Chief Investment Officer

*New Normal refers to a regime of low rates and lower investment returns following the 2008 GFC. Sea Change refers to a transformation in markets where incumbent rules no longer apply, leading to new challenges and opportunities.

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Market Outlook 2024: A Window of Opportunity

Executive Summary

As we wave goodbye to the 'easy money' era, investors likely pondering, "What's next?" The journey ahead calls for both historical wisdom and a keen eye for future trends. The low-interest rates that fueled unprecedented growth have receded, ushering in a new regime for investors.

2022 marked the year when the market took a hard look in the mirror. Both equity and bonds declined, grappling with inflation that topped the list of investors' concerns. As interest rates rose from historic lows, our strategic moves away from long-duration bonds cushioned us against the harshest blows. Fast forward to 2023, which was mostly a year of tug-of-war between soft and hard landing until investors got more clarity at the end of the year that soft landing is the base case going forward.

The stage is set for 2024 to be a good year for different types of investors. Cash, once yielding close to nothing, now offers a refuge for those who are satisfied with low single-digit returns. For fixed-income investors: bonds have transformed from a "search for yield" to a "yield-rich" haven. And equities? They continue to offer the highest return potential in the long term, but in today's higher interest rate environment, investors will need to dig deeper to invest in segments with better risk/reward.

Indeed, what looks like a victory in the war on inflation has set the stage for a much-needed normalization across economies and markets. We may currently be in a good window of opportunity for undervalued, higher-growth markets like US small-caps and Europe equities to lead the recovery. There are also interesting *Emerging Opportunities* (a new theme for 2024!) that have presented themselves within the Emerging Markets, alongside China equities which retain good rebound potential on the back of their low valuation and washed-out sentiment. Of course, amid late-cycle dynamics, investors should favour higher-quality segments that still offer strong recovery potential.

The end of the interest rate hike cycle also means that bonds are back. Government bonds are shedding their tarnished reputation, reclaiming their shield-and-yield status in investors' portfolios. As interest rates are set to decline, we are also capitalizing on today's attractive rates by positioning in higher-yielding markets that can provide a good buffer to their higher volatility profile.

MARKET REVIEW

The end of easy money
As markets transition out of the era of easy money, the inevitable question would be "what do I do next?" Well, to figure out the future, one needs to understand the past.

The era of easy money was prompted by events 15 years ago, as central banks lowered interest rates during the 2008 Global Financial Crisis to avoid a depression.

Low rates led to an era of extraordinary growth. There were some side effects such as massive increase in debt. But so long as there was asset inflation, it did not matter: Markets got addicted to these low rates.

Bitcoin was the poster child for this era of free money, but it was not alone. Capital was being thrown at anything with a promise (rather than a real premise). The music played on...until it stopped.

A hard road...
In 2022, inflation started to bite, hurting the consumer in many ways. Central banks did what they had to do: start raising rates to contain inflation.

Equities and bonds reacted in textbook-fashion, with bonds experiencing their worst-ever performance in the face of the most aggressive hikes ever. We managed the immediate impact of rate hikes fairly well by avoiding long-duration bonds, benefitting from the unwind of years of easy money policy.

In 2023, bond markets did not fare as badly as they did in 2022, but it was tough anyway. In the first 10 months, bond investors were still not making any money. It was only in the last 2 months that bonds rallied to close the year up 7%. Where 2022 was the shock response, 2023 was the tussle as markets tried to figure out what next.

The secondary impact of the rate hikes was harder to call. For most of 2023, it was a tug-of-war between hard and soft landing. At the start of the year, there were already concerns that the pace of rate hikes, coupled with "structural" inflationary pressures, would lead to a hard landing and market crisis. The banking crisis in March essentially shifted the odds in favour of the hard landing camp.

..to a soft landing
Clarity only started emerging at the end of 2023 as it was clearer that the war on inflation was being won as inflation slowed from 9% to 3%, with positive signals from the Fed. This paved the way for a soft landing, and much-needed normalization of markets. We mentioned earlier that bonds rallied strongly in Q4, but they were not alone. Markets that were sidelined before such as EM credit and small caps showed their potential, rallying 12% and 21% respectively as the soft-landing scenario gained traction.

Risks and opportunities in the new era
The end of easy money means that many investors now find themselves in an unfamiliar world: high interest rates, a top-heavy market, potential unraveling of indebtedness.

Yet amid these risks, 2024 is shaping up to be a good year. This is not just us being hopeful. The Sea Change has led to a much more conducive environment across the range of asset classes.

Cash: "Return-free risk" to "Risk-free return"
On one end of the spectrum, interest rate markets have gone from "Return-free risk" back to "Risk-free return". With the normalization of interest rates, investors who only want minimal returns can finally get low single-digit return on their cash.

Bonds: "Search for yield" to "Spoilt for yield"
For income investors, they have gone from the "Search for yield" to being "Spoilt for yield". A wide range of credit markets now offer high single to double-digit yields, with potential for capital appreciation.

Equity: Broad-based growth to specific growth
On the other end of the spectrum, equities have tended to offer the highest return. But investors can no longer bank on making money the same way as before. Without low interest rates to push broad-based growth, equity investors need to dig deeper to get return from areas that offer specific growth.

We cover these risks and opportunities in greater detail in the following sections.

Bonds: Bloomberg Global Aggregate, Credit: Bloomberg Emerging Markets High Yield, Small cap: Russell 2000 from 20/10/23-29/12/23

EQUITY: SOFT-LANDING RECOVERY

As years' worth of Quantitative Easing (QE) experiments by the US Fed unraveled in 2022, it also signaled the start of a different regime for equity investors.

Just as in nature, there are also seasons or cycles in financial markets. Investors will need to carefully evaluate if the winners of the past decade can continue to do well in the next part of the investing journey.

One example of a prominent winner in the past decade would be the 'FAANG' group of stocks, or the more recent 'Magnificent 7' stocks[1] that rallied spectacularly in 2023 alongside the AI frenzy; leaving other parts of the market in the dust. What are the odds that a narrow group of stocks continue to lead the way in 2024 and beyond? Consider the following observations from history:

1. Narrow leaderships are rare, happening only 3 times in the past 50 years.
2. Narrow leaderships are followed by a broadening of leadership to other market segments.

Another point to evaluate is their valuations: high valuations act as a ceiling to returns going forward. If so, investors should consider the possibility that such investments may fall under the 'past winner' basket and may not suffice as the sole drivers of your investment performance as the market season changes.

The following research and chart done by Capital Group also reinforces this point.

The takeaway is clear: return leadership tends to change into a new regime, and investors should have the flexibility to venture outside the popular market segments did well during the previous broad-based growth.

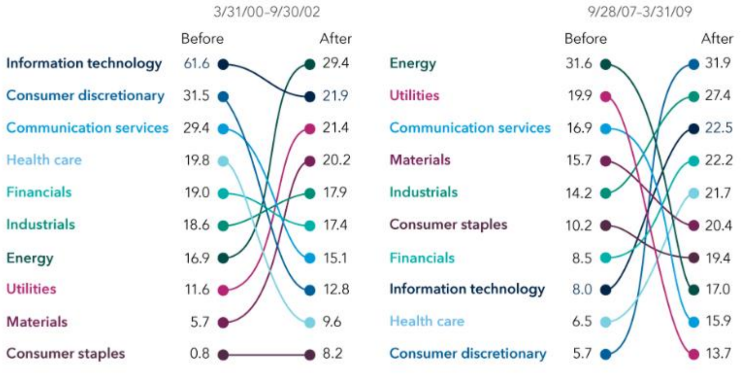
Within equities, two themes offer their unique brand of growth and stand a good chance to grow into tomorrow's winners.

1. Recovery

With the end of the rate tightening cycle and soft-landing as the current base case; there is a good window of opportunity for undervalued, higher-growth markets to lead the recovery. Our investors would know that **US small-caps** fit the bill, with their valuations currently trading at wide discounts to large-cap names not seen since 1999. According to Morningstar Research, '2024 will be the first year that both the disruptions from the pandemic and all the subsequent dislocations [high rates, contraction]...will be behind us', setting the stage for small-caps to outperform. Of course, given late-cycle dynamics, investors should retain a preference for higher-quality names within this segment.

Recovery tailwinds have also been building for **Europe equities.** We reduced exposures here in April 2023 ahead of meaningful slowdowns in the economy. Similarly, we are adding back slightly today on early indications that the slowdown has finally bottomed out. Europe's industrial base puts it in a good position to benefit from a recovery brought about by a soft landing.

Market Leadership: Returns % Before & After Bear Markets



Source: Capital Group. For the tech bubble the dates represented are December 31, 1996, to March 31, 2000 (before bear market), and September 30, 2002, to December 30, 2005 (after bear market). For the global financial crisis the dates represented are December 31, 2003, to September 28, 2007 (before bear market), and March 31, 2009, to December 31, 2013 (after bear market).

[1] https://money.com/faang-magnificent-seven-tech-stocks

EQUITY: EMERGING OPPORTUNITIES

2. Emerging Opportunities

This is a new theme being introduced in our portfolios. The end of easy money, and shift from broad-based growth to specific growth means that investors need to focus on high-growth markets driven by their distinctive economic trajectories and coupled with attractive valuations.

The volatility in the past few months has also presented interesting opportunities within **Emerging Markets** at lower valuations and attractive technical.

For one, **Vietnam** is one Emerging Market that has been under the radar but presents an interesting opportunity to investors. Long-time seasoned investors who had invested during Vietnam's boom-bust cycle in the 2000s may associate the market with unpredictable and large price swings; perhaps not so surprising given the smaller economy and 'frontier' status it had back then. But when it comes to Vietnam, it does seem to be a case of 'this time is different'.

Vietnam is a key beneficiary of US-Sino decoupling, fueling its export-led economy. As such, the economy has climbed from 85th in 2010 to 36th largest globally in 2022 (CEBR). It is a different country and market today than before, and one of strategic importance to major economies of the world.

There is strong government support, as well as an attractive demographic profile. Vietnam's 100-million population, of which the middle class is forecasted to double by 2026 (OECD), provides strong growth tailwinds for the economy.

The icing on the cake? Despite being an emerging market, Vietnam equity performance has kept pace with developed market equities over the past decade.

Source: whitehouse.gov

China: For a long while, Chinese equity markets had a nice combination of economic growth that underpinned an upward trajectory, and recurring market cycles that rewarded tactical asset allocation. **This has not been the case in recent times, with the pace of recovery disappointing us. Going forward, we are approaching China from a more opportunistic standpoint.**

What was different this time was that the Chinese government decided to employ some tough love in a determined drive to rid the system of some of its excesses. This surprised markets with some of its unprecedented policies including:

- Willing to let property developers fail where before they tended to be bailed out
- Clipping the wings of national technology champions such as Ali Baba and Tencent
- Eliminating entire industries such as for-profit education literally overnight

To be clear, China still retains immense potential for the long-term investor. The US-Sino tensions are precisely due to the rise of China as a global industrial and financial superpower. The US knows because that is how it displaced the UK. China has increased its sphere of economic influence all the way from Asia to Europe to Latin America. As an example, China is poised to dominate the global automotive sector after years of building up an entire supply chain in EVs.

While the worst is over, there remains a market overhang as sentiment remains at rock bottom. As Bill Gates said, "We always overestimate the change that will occur in the next two years and underestimate the change that will occur in the next ten."

Hence, while China continues to be an emerging opportunity, the timing of the catalyst is less visible. As global investors, we maintain a reduced overweight to China 'A' equities today: still maintaining good exposures to take advantage of potential rebounds on the back of attractive valuations, but at the same time aware of other more timely opportunities that are available to our investors today. We remain alert to developments in China and expect to make further adjustments as opportunities (or risks) arise.

BONDS ARE BACK

Some readers may recall our comic series where we highlighted the risks of easy money, referring to government bonds as the 'shield that yields'.

This was because with cash yielding next to nothing, investors were not getting any return, while running a risk that the defensive properties of government bonds would not manifest during market stress. Effectively, this was return-free risk.

This turned out to be true as the government bonds, conventionally the flight to safety assets, not only dropped with equities in 2022 but registered their largest losses ever.

While we were not immune from losses, our decision to avoid government bonds then helped reduce the downside from what was a very obvious risk.

Avoiding obvious risks is crucial. While no one will expect to identify all the downside risks, one should heed the signs wherever they are evident. Yes, it means sometimes we leave the party early but it also means we avoid the panic crush at the exits. Ask anyone who got crushed at the exits and they will tell you they wished they got out sooner.

In many ways, investing success is about having the longevity to fight the next battle. Having faced challenges such as unprecedented rate hikes, it is nice to see that the battles ahead are more subdued, if not outright attractive. As we transition out of the era of easy money, bonds have become more attractive than they were in a low-rate world.

Interest rates: "Return-free risk" to "Risk-free return"

The suggestion that government bonds were attractive would probably be met with skepticism after the huge declines in 2022 and the volatility of 2023. But this is the type of flushing out and reset that is needed in any market that became too overbought.

Government bonds are now the shield with yield, serving two roles. First, they offer better yield for the first time in a long while. Second, they resume their place in a portfolio to buffer against riskier assets such as equities.

Credit: "Search for yield" to "Spoilt for yield"

During the era of easy money, demand for income amid a sea of liquidity resulted in low (even negative) yields. It was indeed an ongoing search for yield. In such an environment with little upside and plenty of downside, it was not practical (maybe even irresponsible) to run an income strategy.

Today, traditional credit markets offer two attractive features for income investors with the risk tolerance.

1. Lock in high rates

Amid historically attractive bond yields, it makes sense to lock in higher yields for a longer period. This reduces the reinvestment risk into lower-yielding opportunities as future bond issuance will likely be at lower rates.

2. Exposure to capital appreciation

While there will be interim volatility, we are beating the crowd before the line starts forming at the velvet rope as cashed-up investors find themselves pressured to take some risk and push bond prices up.

At the same time, there are risks. The domino effect of higher interest rates is still playing out. Certain markets such as government bonds, public credit, and real estate have already borne the brunt of the rate hikes, and reset to more attractive levels.

Yet, there are segments where the impact remains to be seen. Such risks exist in high-yield markets especially where companies struggle to generate cash flows to service an increasingly high cost of debt. This does not mean we avoid the high-yield segment in its entirety as it would mean throwing the baby out with the bathwater. But we are focusing on segments of higher quality issuers with lower default risks to get the high income.

As much as opportunities in traditional income markets are the best they have been in years, our alternative income strategy stood out in 2023, providing stable double-digit income while not being affected by the volatility in traditional markets. The prospects have not diminished as we see attractive yields even in 2024.

HOW ARE WE POSITIONED?

Equity (Green) **Bonds (Blue)**

Key Themes	
Positioning for Recovery With the end of the rate tightening cycle and soft-landing as the current base case; there is a good window of opportunity for undervalued markets to lead the recovery. Maintain a preference for higher quality segments that still offers strong recovery potential.	**US small-cap equities** **Europe equities**
Emerging Opportunities Financial markets operate in cycles. The end of the easy money era means looking beyond popular markets that did well during the previous broad-based growth to find tomorrow's winners. Focus on high-growth markets driven by their own distinctive economic trajectories and coupled with attractive valuations.	**China 'A' equities** **Emerging Market equities, Vietnam equities**
Late Cycle Stability With interest rates remaining at higher levels compared to the past decade, there continue to be signs that economies and businesses are adjusting to the new regime. e.g. tight labour markets and slower growth. The current late-cycle dynamic means that high quality investments play an important stability role in portfolios in case of negative surprises.	**Healthcare equities** **Government and Investment Grade bonds**
Capturing High Yields The combination of high interest rates with the end of the Fed interest rate tightening cycle means that bonds should place prominently on investors radars. Position in higher yielding markets that can provide a good buffer to their higher volatility profile.	**Asian High-Yield bonds** **Emerging Market bonds**

ASSET ALLOCATION STRATEGY

-- Underweight – Slight Underweight = Neutral + Slight Overweight ++ Overweight

Equity: Regions

United States

US Small-caps as relative valuations are attractive and expected to benefit as economies recover. **Healthcare** as earnings are more stable and less dependent on broader economic cycle.

Europe

Europe's pro-cyclical industrial base to benefit from economic recovery as it becomes clearer a severe recession is not on the cards.

Japan

Maintaining no exposure as they are less attractive compared to other opportunities. Valuations have also become less attractive, with the prospect of a stronger JPY posing a risk to Japanese equities.

Asia Pacific ex Japan

Slight China 'A' overweight as the deleveraging cycle has taken its course. Tailwinds steadily building up in the form of improving credit conditions and economic activity.

Emerging Markets

Preference for high-growth markets at attractive valuations i.e. Vietnam

Fixed Income

Global

Focus on currency-hedged government bonds to buffer portfolio volatility during periods of stress.

Investment Grade Corporate

Maintaining no exposure as we run a barbell strategy combining defensive government bonds and high income credit.

US High Yield

Maintaining no exposure due to relative poorer valuations and risk of defaults as economies remain late-cycle.

Asia

Attractive yield across major fixed income markets with room for capital appreciation and better fundamentals.

Emerging Markets Debt

Hard currency bias to focus on return from credit while limiting exposure to emerging market currencies.

MARKET INDEX RETURNS

Equity Regional	MTD	YTD	10Y	20Y
Global	4.83	22.81	8.51	8.14
United States	4.53	26.26	12.02	9.69
Europe	5.50	20.48	5.09	6.79
Japan	4.99	19.30	5.45	4.83
Asia Pacific ex Japan	4.65	7.36	3.94	7.31
Emerging Markets	3.87	10.12	3.01	7.17

Equity Markets	MTD	YTD	10Y	20Y
Australia	11.00	14.25	6.53	9.73
Brazil	6.79	33.09	2.39	6.62
China "A"	-1.28	-11.73	4.54	8.18
China "H"	-1.41	-10.84	-2.64	3.97
Hong Kong	0.16	-10.56	0.30	5.04
India	8.06	19.57	11.18	11.60
Indonesia	3.97	11.32	5.57	11.98
Korea	5.84	17.27	2.62	7.58
Malaysia	1.88	-2.75	-2.38	5.91
Russia	-0.27	25.30	3.49	7.94
Singapore	6.97	6.33	3.62	7.48
Taiwan	5.35	31.99	11.35	10.26
Thailand	5.87	-11.45	3.62	7.60

Equity Sectors	MTD	YTD	10Y	20Y
Gold	1.17	10.60	5.25	2.17
Energy	-0.08	-1.42	3.44	8.36
Technology	4.29	53.66	18.63	12.37
Healthcare	4.46	4.27	9.56	9.23
Financials	5.36	12.10	10.00	4.74

Fixed Income	MTD	YTD	10Y	20Y
Global Aggregate	4.16	5.72	0.38	2.40
Global Aggregate (H)	3.20	7.15	2.41	3.42
High Yield	3.89	13.76	4.15	6.41
Asia	3.13	7.39	3.35	2.99
Emerging Markets	4.20	9.09	3.03	5.75

Note: (H) Currency Hedged

Currencies	MTD	YTD	10Y	20Y
SGD/USD	1.28	1.46	-0.44	1.27
EUR/USD	1.39	3.12	-2.17	-0.66
JPY/USD	5.07	-7.04	-2.88	-1.36

Commodities	MTD	YTD	10Y	20Y
Gold	1.31	13.10	5.55	8.34
Oil	-5.67	-10.73	-3.12	4.03

*As of Dec 2023. Source: Bloomberg. **Total return in USD**.*
10 and 20 year returns are annualized.

"In investing, what is comfortable is rarely profitable."

Rob Arnott

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