UOB

In collaboration with:
J.P.Morgan ASSET MANAGEMENT

UOB Investment Insights

Market PowerBar

MARCH 2023

A LOOK AT THIS MONTH

Key Topics	What Investors Should Know
1  Maintaining our case for Asia ex-Japan	**Global stock markets have rallied on the back of China's reopening and expectations of a possible turnaround in the Federal Reserve's rate hike cycle.** ▶ Investors should remain cautious on developed markets amid risks of an economic slowdown and more aggressive rate hikes than expected. ▶ Chinese stock valuations are still attractive, while the ongoing reopening in China can continue to benefit Asia ex-Japan markets.
2  Unintended spillover effects of China's reopening	**China's reopening could have both positive and negative effects on the global economy.** ▶ Chinese demand for goods and services should cushion against an economic slowdown, while supply chain bottlenecks should dissipate and global inflation could trend lower. On the other hand, greater import demand for commodities can also push inflation up. ▶ Investors with the appropriate risk appetite can benefit from adding Chinese stocks given that the A-share market is less correlated with global indices and may not be affected as much by a slowdown in developed markets.
3  ASEAN markets could continue to perform in 2023	**ASEAN economies stand to benefit from China's reopening.** ▶ Recent weakness in exports to the West could be offset by rising Chinese demand. ▶ The recovery in tourist arrivals to ASEAN countries has some way to go and could support jobs in the services sector, as well as consumption.

Upcoming Event

China "Two Sessions": National People's Congress (NPC) and Chinese People's Political Consultative Conference (CPPCC)

Keep an eye on China's policy announcements, especially its official post-COVID growth target.

Speak to your UOB Advisor today to find out more.

Topic 1

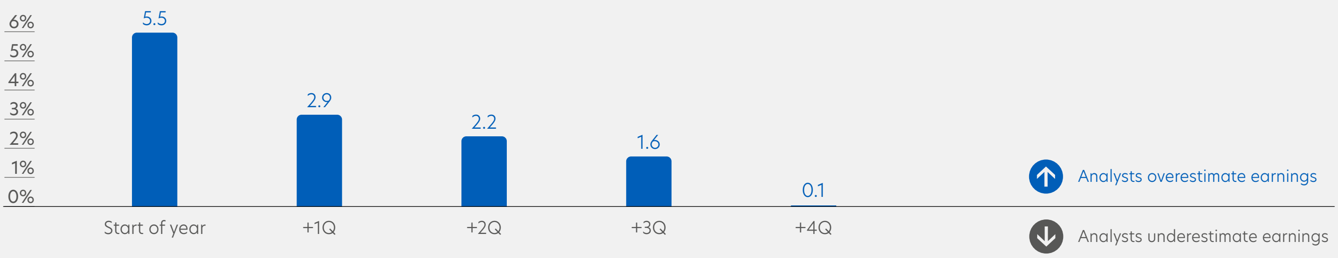
Maintaining our case for Asia ex-Japan

Markets rallied in January, especially with developed markets reporting stronger-than-expected growth data, and this has eased fears about a deep recession. However, markets turned cautious in February following strong labour market and inflation data. We continue to believe that the risk of a short and shallow recession in developed markets remains high. As such, we favour Asia ex-Japan, as the region stands to benefit from China's ongoing reopening.

Figure 1A

Earnings expectations are typically overstated at the start of the year

Average analyst over/underestimate of annual earnings (S&P 500, pro-forma EPS, 1996 – 2021)



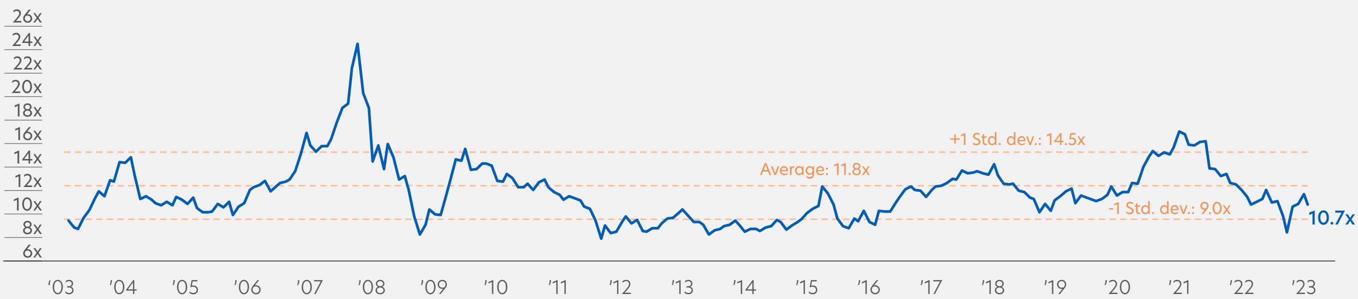
Source: Compustat, FactSet, Standard & Poor's, J.P. Morgan Asset Management.
Historical EPS levels are based on annual operating earnings per share. Earnings estimates are based on estimates from Standard & Poor's and FactSet Market Aggregates. Past performance is not indicative of future returns. Data reflect most recently available as 31 January 2023.

Key takeaways

1. The rally across developed markets in January has been driven by economically sensitive sectors. Some of the triggers that point to a sustainable market recovery are already in play: Inflation is easing, expectations of a Federal Reserve pivot are rising and the US dollar (USD) looks like it has peaked. However, sentiment has changed following stronger-than-expected labour market and inflation data in the US.
2. We remain cautious about an economic slowdown and impending recession. Earnings expectations tend to be overly optimistic at the start of a new year (Figure 1A). Stubbornly high inflation and a strong labour market in the US could result in further policy tightening. If that goes too far, central bank policy mistakes could derail any economic recovery.
3. Meanwhile, Asia ex-Japan markets have been driven by China's recovery. This is ongoing and more sustainable in our view than continued improvement across developed markets. Asia ex-Japan markets could rally further as investors have yet to fully factor in the Chinese economy returning to normal. China's valuations are still slightly below average even after the recent rally (Figure 1B).

Figure 1B

MSCI China valuation remains attractive despite the recent rally



Source: FactSet, MSCI, J.P. Morgan Asset Management. Price-to-earnings ratio based on next twelve months earnings estimates. Data reflect most recently available as 27 February 2023.

In summary

- The US has not avoided a recession yet. We still expect further deceleration in growth as companies are slowing investments and households appear to be saving less and borrowing more.
- The end of lockdowns in China and possible end to the Fed rate hike cycle favour Asia ex-Japan and Chinese markets over developed markets for now.

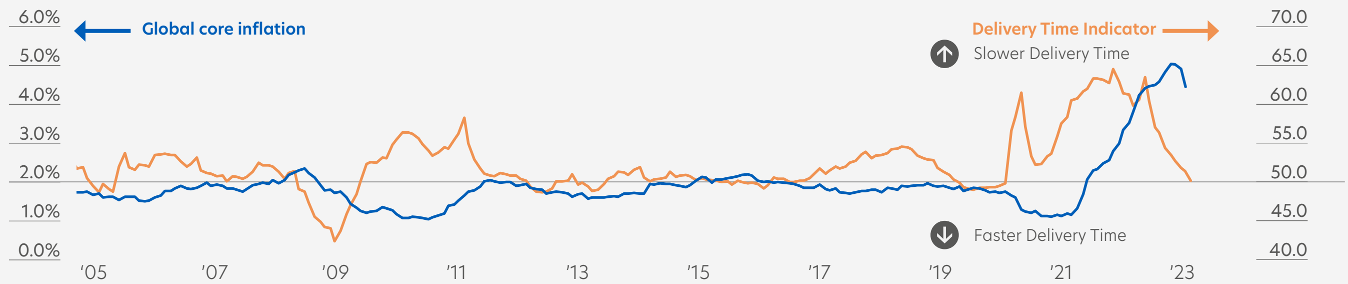
Topic 2

Unintended spillover effects of China's reopening

China is reopening faster than expected, which is a positive development for both the global economy as well as stock markets. The most obvious benefit to the world is the return of Chinese demand for goods and services, in addition to the easing of supply chain bottlenecks. However, we should be aware that not all these spillover effects are positive.

Figure 2A

Global inflation could trend lower given the faster delivery times after China normalises



Source: Standard & Poor's, J.P. Morgan Asset Management.
Participants in Standard & Poor's PMI business surveys, conducted in 44 countries, are asked: "Are your suppliers' delivery times slower, faster or unchanged on average than one month ago?". Index includes the manufacturing and construction sectors. PMI score reflected above is 100 – PMI report by Standard & Poor's. A reading of 50 = no change, <50 = faster delivery time, >50 = slower delivery time.
Data reflects most recently available as of 10 January 2023.

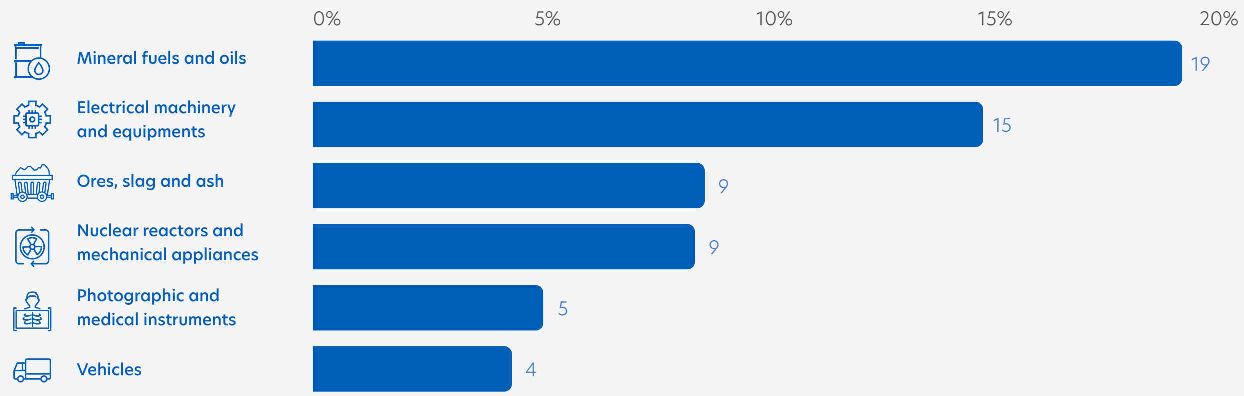
Key takeaways

1. China's reopening presents several benefits to the global economy. If growth continues to slow down in developed markets, China's revival can help to cushion against the downturn. As China normalises, supply chain bottlenecks in manufacturing and shipping activities should also dissipate, which will help push global inflation down (Figure 2A).
2. However, there could be unintended negative consequences as well. Should Chinese demand for commodities pick up, this could worsen supply issues and push prices higher. Figure 2B shows China's top imported goods, representing categories where we might see some price pressure. This is hardly good news at a time when inflation is still a major concern. However, these inflationary forces could be partially offset by a decline in demand from the US and Europe.

Figure 2B

Inflationary pressure may persist over China's top imported goods

Share of total gross goods import value, 2019



Source: OECD TiVA database; J.P. Morgan Asset Management.
Data reflects most recently available as of 31 January 2023.

In summary

- Despite the recent rally in Chinese stocks, we remain positive on China on the back of its recovery and supportive policies.
- Spillover effects like rising commodity prices might push global inflation higher and continue to weigh on global economic growth. Investors with the appropriate risk appetite can benefit from adding Chinese stocks to their portfolios, given that the A-share market is less correlated with global indices and may not be affected as much by a slowdown in developed markets.

Topic 3

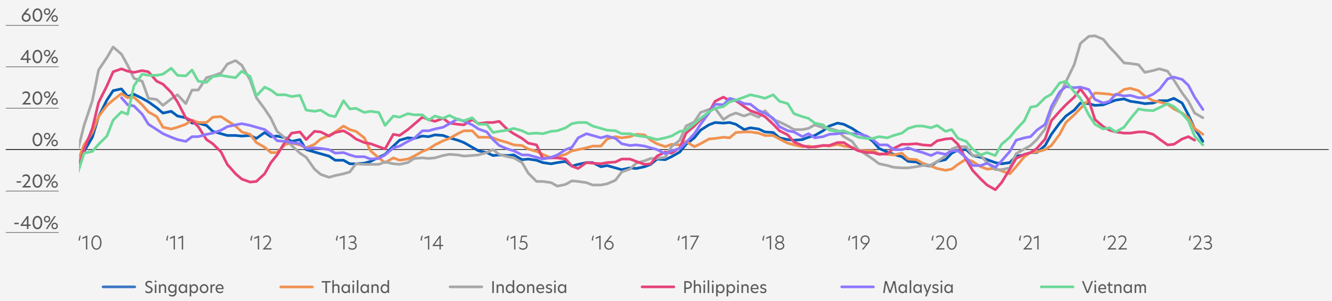
ASEAN markets could continue to perform in 2023

While global stocks fell 18% in 2022, ASEAN stocks were a relatively bright spot, outperforming global markets by close to 12%. This was due to resilient exports to the West and the reopening of borders supporting overall economic recovery. With developed markets poised for a slowdown, can ASEAN stocks continue to perform in 2023?

Figure 3A

Slowing export activities in ASEAN due to weaker demand in the West

Year-over-year change, 6-month moving average



Source: FactSet, J.P. Morgan Asset Management; Data reflect most recently available as 28 February 2023.

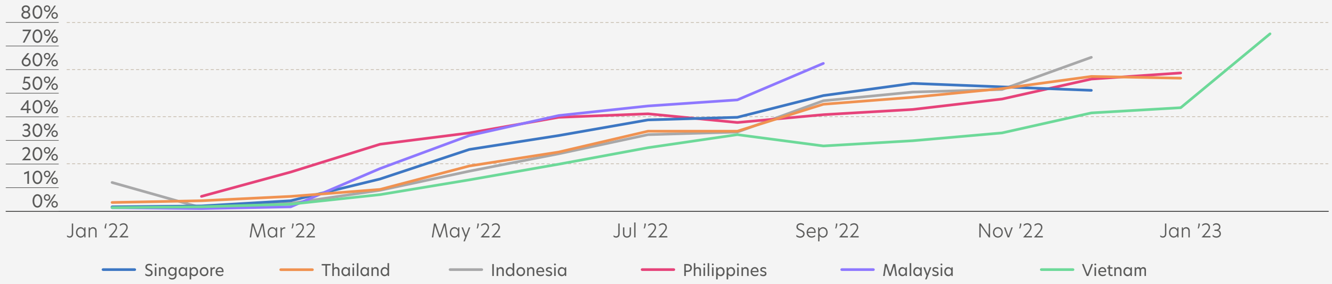
Key takeaways

1. Export growth has been adversely affected in ASEAN (Figure 3A) as demand has started to slow in the West given the impact of tight monetary policy. As China continues its accelerated reopening in 2023, the weakness in export demand from the developed West could be offset to a certain degree by the Chinese recovery.
2. It is crucial to understand which countries have a larger exposure to Chinese final demand, especially since the Organisation for Economic Co-Operation and Development (OECD) estimates that around 26% of China's imports are intermediate goods and services not consumed within China.
3. Singapore, Thailand and Vietnam are more exposed to China's final demand than to final demand from the US and European Union combined. These three ASEAN countries therefore stand to benefit more from an uplift in Chinese economic activity.

Figure 3B

Tourist arrivals in ASEAN only rebounded to around 60% of their pre-COVID level

Relative to respective month in 2019



Source: CEIC, J.P. Morgan Asset Management. Data reflect most recently available as 28 February 2023.

In summary

- ▶ Just as importantly, the tourism recovery in ASEAN has some way to go. The region's tourism arrivals last year only improved to about 60% of pre-COVID levels (Figure 3B). The continued recovery in tourism will go a long way in lifting domestic employment, especially in the services sector, and that in turn will help to support consumption and overall sentiment.
- ▶ Taken together, we believe that China's recovery this year can be sustained, and will have a positive impact on ASEAN from both trade and tourism perspectives.

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