Discovering Opportunities
in a Remodelled World

Market Outlook 2021

UOB

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Editorial

Editorial

I believe I speak for many when I say that 2020 was a year that we wish to forget – a year that saw economies, businesses, societies and individuals deeply impacted by a global pandemic that emerged without warning. Countries went under lockdown, and we have all had to adapt to very different ways of living and working. With the US elections over and the promising developments on the COVID-19 vaccine front, the world is looking forward to a return to normalcy. However, it bears noting that this "normal" will be vastly different from the one in the days pre COVID-19.

Even as the world anticipates the day when COVID-19 is no longer a global threat with effective vaccines readily available, the reality is that the way we work and socialise will likely have changed permanently. Business meetings will be a hybrid of face-to-face interactions and those conducted via online collaboration platforms such as Zoom and Microsoft Teams, reducing the need for business travel and further enabling work-from-anywhere arrangements.

Digitalisation is now a business necessity and is likely to continue. E-commerce will thrive on the back of new entrants and brick and mortar shops reinventing themselves by offering online shopping options. People movement will be reduced as work from home arrangements become more common among workers – benefitting the logistics industry that delivers food and products to people.

The global supply chain will also evolve: Many countries have become dependent on cheap manufacturing centres such as China, Vietnam and Mexico. But the pandemic has caused governments and companies to start building resilience into their supply chains. This may bring about higher costs to businesses and customers in the future.

As the world heals and remodels itself after this pandemic, this gives rise to investment opportunities if we remain at the forefront of new developments. We broadly categorise these into the following three themes:

Recovery

With a working vaccine on the horizon, investors will look toward a reopening of the global economy. However, the recovery will be uneven:

Countries that have managed the COVID-19 crisis better and sectors that have benefitted from the pandemic, will recover faster. Identifying the economies and sectors that have the potential to perform better is important when making decisions on your investment portfolio.

Technology

The United States (US) and China are locked in a race for technological supremacy. Artificial Intelligence and cloud computing are the new engines of economic growth. 5G networks and massive data centres are the infrastructure required to power these engines and new technology development will provide opportunities for investors to ride on this growth.

Sustainability

The US, Europe and China are leading the charge in embracing environmentally-friendly projects to address climate change. The widespread use of social media has raised awareness on socially-acceptable corporate behaviour, including control and governance issues. Sustainable investing is also entering the mainstream: Investors are increasingly realising the impact their investments can have on the world they live in while recognising that investing responsibly does not mean having to compromise on returns.

Alongside the opportunities we see, there remain investment risks that we need to keep an eye on: The production and distribution of COVID-19 vaccines could face hiccups along the way, hampering economic recovery as a result. US-China tensions will likely continue as the US seeks to contain the rise of China. With its new administration however, the US may perhaps strike a more moderate tone than the past four years. Last but not least, government debt has risen by 78% this year in advanced economies alone[1], increasing the burden on public finances which could eventually impact financial markets.

As we look forward to stepping out of COVID-19's shadow in 2021, the expected recovery will provide the tailwind for markets, setting the stage for us to revisit our investment ideas and tap onto new and sustainable opportunities as we work towards our financial goals. It will be an exciting year ahead, and I wish you success in your investing journey.

Abel Lim
Singapore Head, Wealth Management Advisory
Deposits and Wealth Management
Personal Financial Services

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1 International Monetary Fund, World Economic Outlook Database, October 2020

Review of 2020

Asset Class Review

Equities

Despite the challenges that COVID-19 brought to equity markets, global equities have recovered from the March 2020 lows and closed the year on a positive note.

Central banks injected liquidity into the global economy, and governments all over announced aggressive support packages to prevent irreparable damage to their economies. These measures kept asset prices afloat.

The top performing region was Asia ex-Japan, as Asian countries had managed the COVID-19 pandemic better and reopened their economies earlier than developed markets. This was followed by the US, where “lockdown” stocks such as Technology, E-commerce and Online Services companies soared as they were still able to deliver growth whilst the world’s economies almost grinded to a halt.

At the other extreme, Europe’s continued struggles with containing the pandemic and weak economic data have put its equities under pressure.

The worst performing global sectors were the energy and financial sectors (-33.0% and -7.0% respectively) due to weak global demand and low interest margins. The best performing sectors were technology (+36.4%), followed by consumer discretionary (+29.8%), where Amazon.com alone takes up almost a quarter of the sector.

Fixed Income

The very-low interest rate environment in 2020 has been beneficial for fixed income markets. The fear and uncertainty over COVID-19 has seen safer assets, such as US government bonds and investment grade (IG) bonds, gain the most. Aggressive central bank intervention to support bond markets has also made high yield (HY) bonds favourable. Emerging market debt were indirect beneficiaries, but were deemed less attractive as Latin America and Central Europe struggled to cope with COVID-19.

Currencies and Commodities

The US dollar (USD) spiked in March 2020 due to adverse reactions in the financial markets to the pandemic. It has weakened since then due to the US Federal Reserve’s aggressive easing measures. Comparatively, the European Central Bank was not able to be as aggressive, which led to the Euro (EUR)’s strong appreciation relative to the USD. The Japanese Yen (JPY) remains a safe-haven asset, and thus strengthened as pandemic uncertainties grew and persisted. China’s early reopening led to gains in the Renminbi (CNY) and the Australian Dollar (AUD), as China was one of the few engines able to continue supplying to the global economy.

Unsurprisingly, the global slowdown, the resultant drop in demand and large injections of money into the financial system, sent crude oil prices falling and gold prices soaring. However, the increase in copper prices indicated that actual manufacturing activity has recovered rather significantly.

Asset Class Review

Key Market Events

January
23 January
COVID-19 infections rise. China quarantines the greater Wuhan area.

March
3 March
FED cuts rates to zero.

11 March
WHO declares COVID-19 a pandemic.

27 March
US Congress passes USD 2 trillion stimulus.

May
1 May
Trump threatens new tariffs against China.

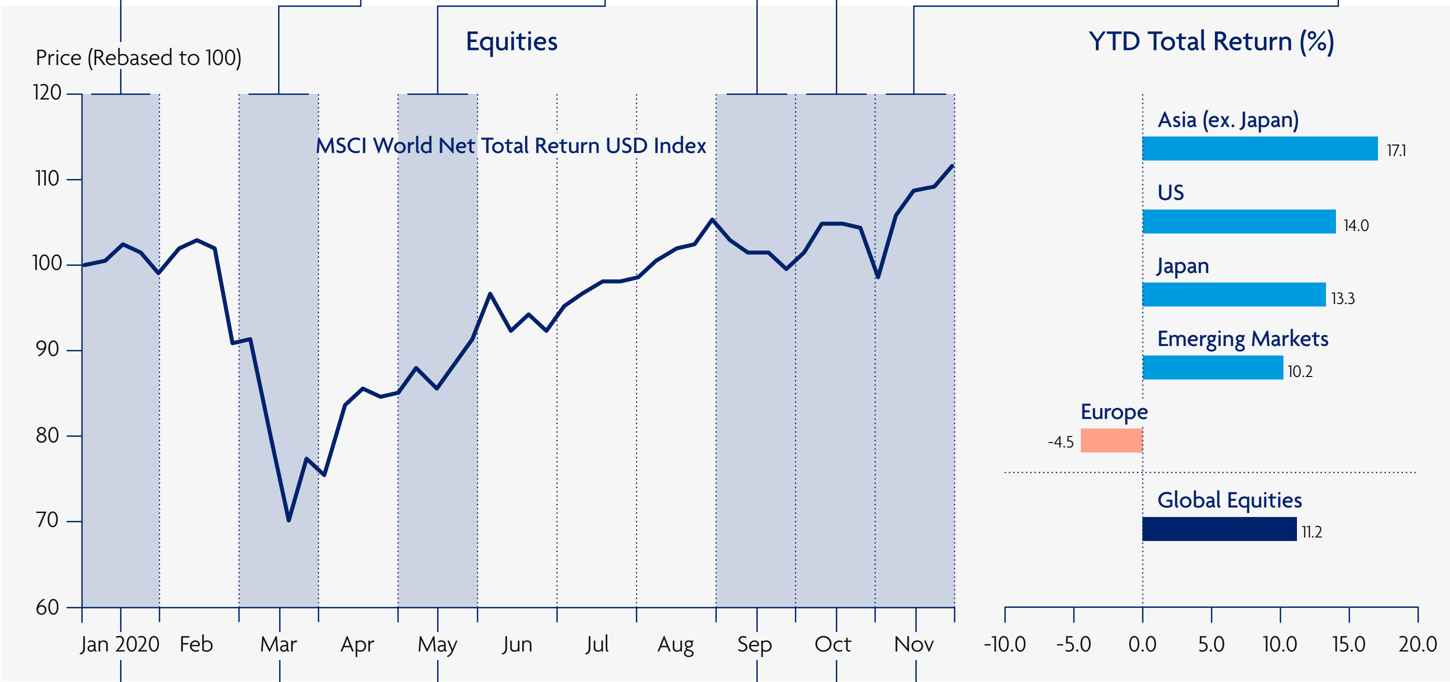
September
4 September
US Tech stocks undergo a serious of pullbacks due to high valuations.

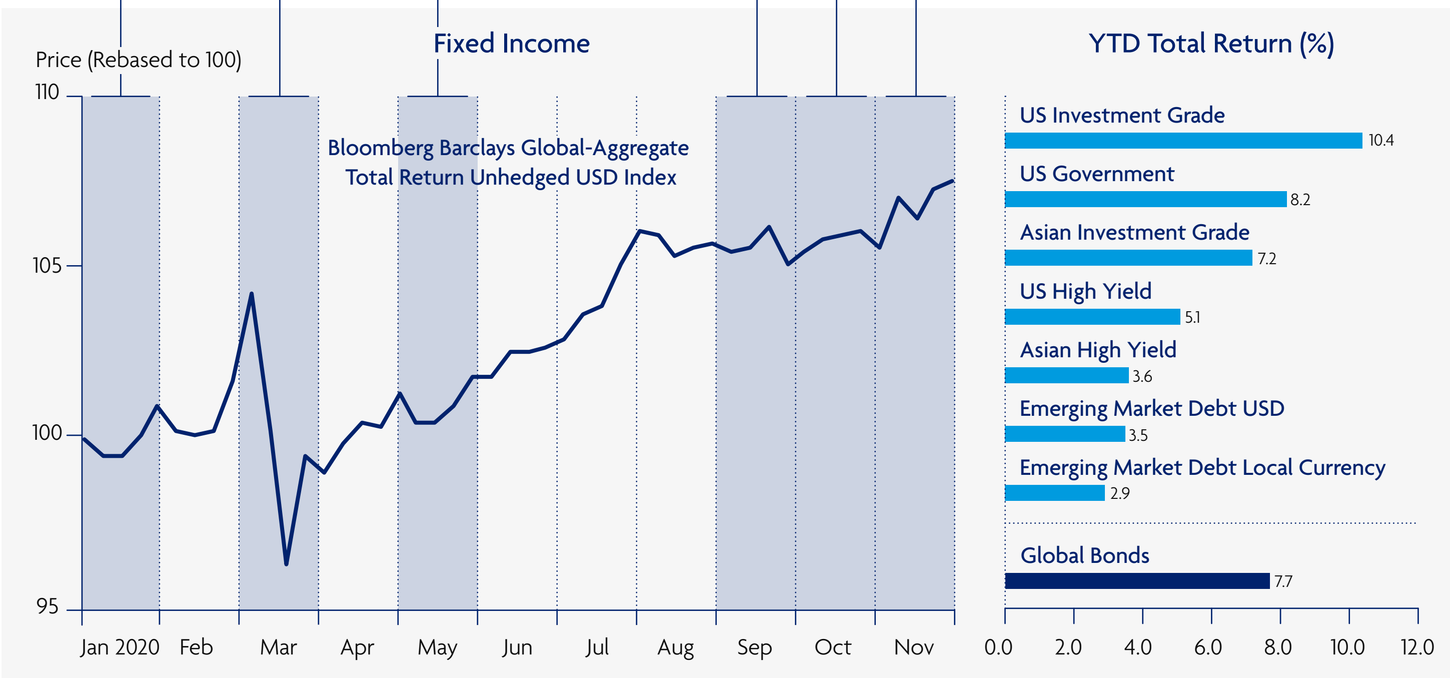
October
Throughout
US stimulus talks begin but remain stalled ahead of elections.

November
7 November
Joe Biden wins US presidency.

9 November
Pfizer/BioNTech announce very successful vaccine trial results.

11 November
China announces new guidelines to curb monopolistic behaviour.





Source: Bloomberg. All percentages shown are expressed in their respective local currency terms, and reflect the total returns from 1 January till 30 November 2020.

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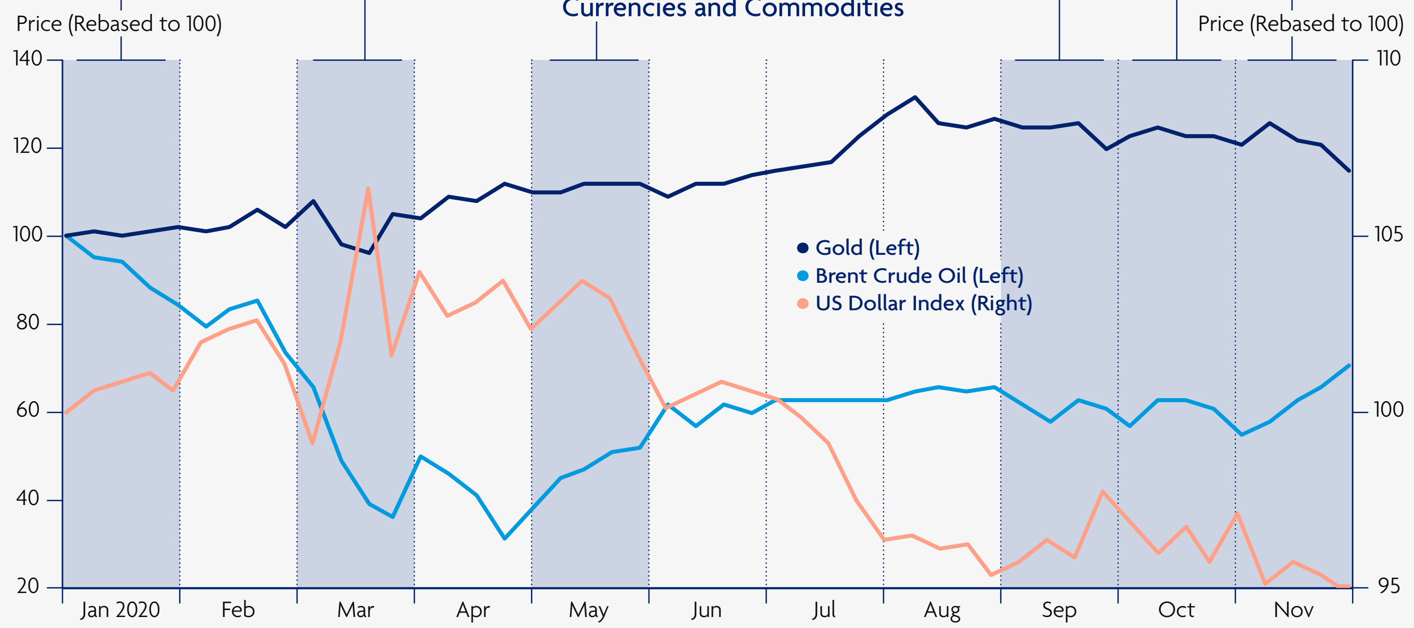
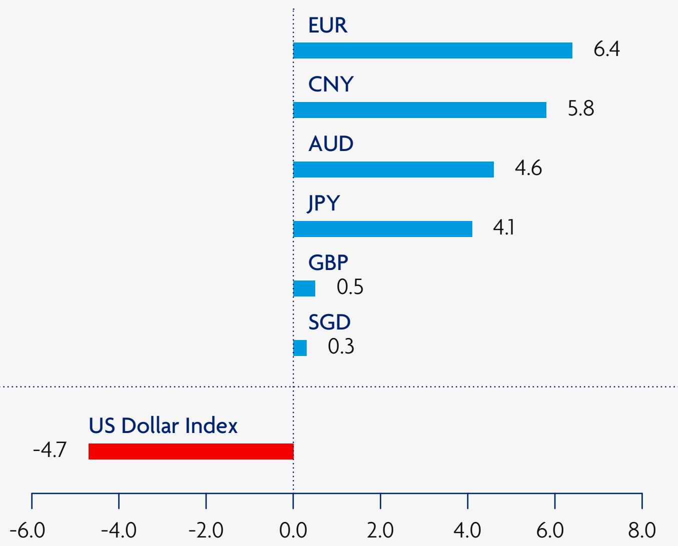
Currencies and Commodities



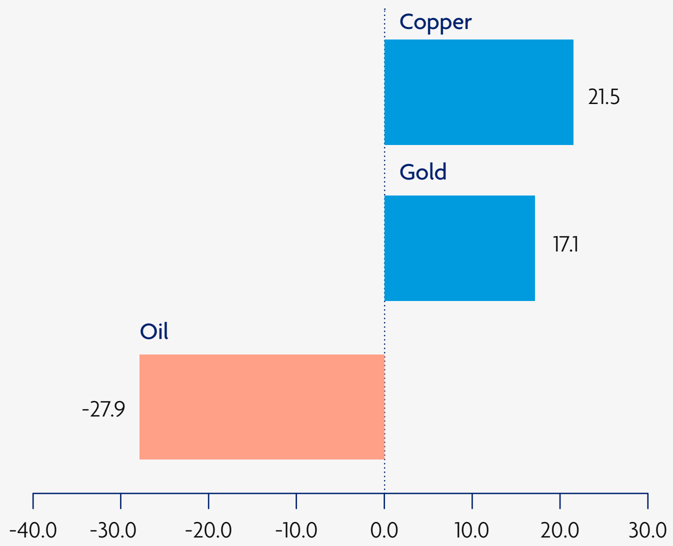
Currencies

YTD Movement Against the US Dollar



Commodities

YTD Total Return (%)



Source: Bloomberg. All percentages shown are expressed in their respective local currency terms, and reflect the total returns from 1 January till 30 November 2020.

Tactical Calls Review

Open Calls

Despite the challenging economic environment, our market calls delivered strong returns and have broadly outperformed the global equity benchmark's return of +11.2%.

Asia ex-Japan equities were our best-performing high conviction call, as the region contained the pandemic more effectively than the developed markets. Its economic growth was also driven by a recovering China. Global equities with high quality factors held up well as their quality shone amid the uncertainty brought by COVID-19. US consumer staples remained defensive as investors sought shelter from market volatility, while benefitting from increased demand during the lockdown period.

Among our Megatrend ideas, Artificial Intelligence (AI) and Innovation equities remained at the top, reflecting their strong growth potential demonstrated by the enabling of work and social activities via digital means amid lockdowns. China has also delivered strong returns as its earlier economic reopening and recovering domestic demand had softened the impact to corporate earnings. Healthcare continues to remain an important focus amid the pandemic. Although Healthcare continues to be driven by vaccine progress in the near-term, new developments in AI and a pipeline of new drugs to cure more diseases create strong longer-term potential for the sector.

We have initiated a new Megatrend idea – Sustainability, focusing on Environmental, Social and Governance (ESG) factors – which is rapidly gaining traction among professional investors for its emphasis on responsible investing that does not compromise on, but instead provides longer-term sustainability in investment returns.

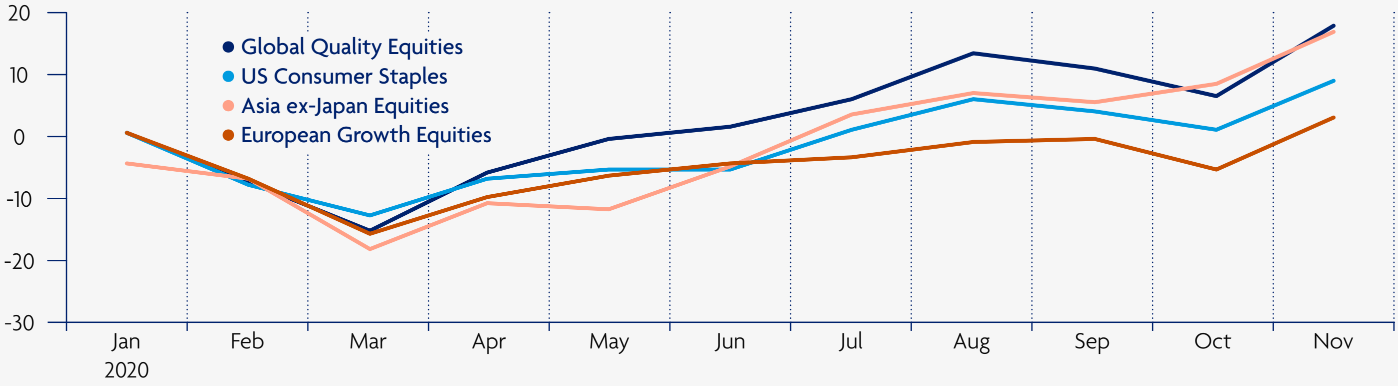
Closed Calls

Our high conviction call on US high-yield (HY) bonds was closed after barely four months as spreads had compressed significantly. During that period, US HY bonds rose by 7.1%, but the likelihood of further upside seemed limited. Investors may want to consider reallocating to one of our Megatrend calls to participate in longer-term growth drivers.

Tactical Calls Review

High Conviction Calls

Cumulative Total Return (%)

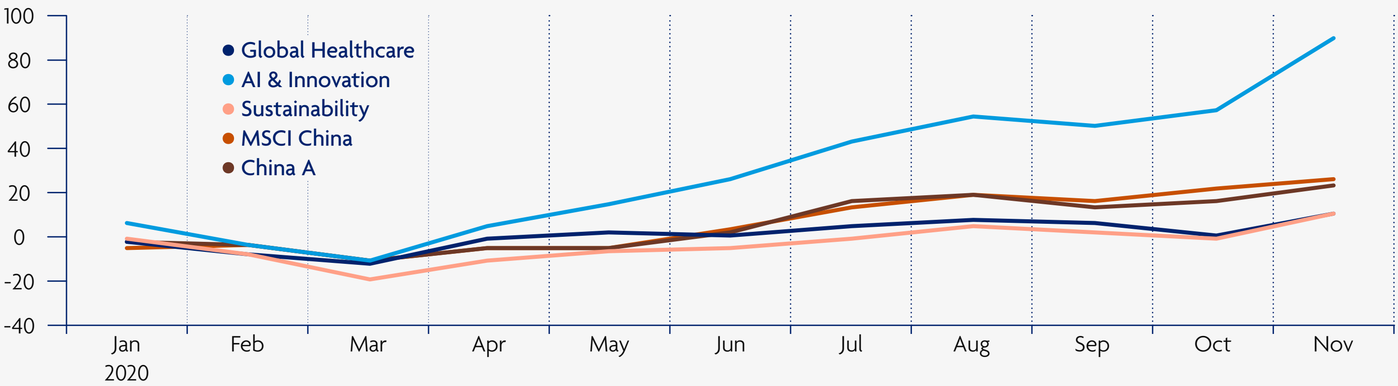


● Since Start^ ● 2020 Year To Date+

Call	Call Start	End Date	Since Start^	2020 Year To Date+
Global Quality Equities	1-Apr-17	Ongoing	76.9%	17.9%
US Consumer Staples	1-Sep-19	Ongoing	14.5%	8.8%
Asia ex-Japan Equities	4-Jun-20	Ongoing	25.8%	25.8%
European Growth Equities	10-Oct-20	Ongoing	1.1%	1.1%
Emerging Markets Equities	31-Dec-17	3-Jun-20	-9.7%	-10.7%
US High Yield	1-Jun-20	9-Oct-20	7.1%	7.1%

Megatrends

Cumulative Total Return (%)



● Since Start^ ● 2020 Year To Date+

Call	Call Start	End Date	Since Start^	2020 Year To Date+
Global Healthcare	1-Jan-17	Ongoing	66.7%	10.1%
AI & Innovation*	1-Jan-19	Ongoing	145.0%	90.1%
Sustainability	1-Oct-20	Ongoing	8.6%	8.6%
China Equities (H-Shares)	1-Jan-19	Ongoing	55.6%	26.0%
China Equities (A-Shares)	1-Oct-18	Ongoing	50.7%	23.6%

* Performance of Allianz Global Artificial Intelligence Fund is used as the proxy for artificial intelligence and innovation equities due to the unavailability of a suitable benchmark index.
^ Source: Bloomberg. All percentages shown are expressed in their respective local currency terms, and reflect the total returns from call start date to 30 November 2020 or call end date, whichever is earlier.
+ Source: Bloomberg. All percentages shown are expressed in their respective local currency terms, and reflect the total returns from 1 January or call start date, whichever is later, to 30 November 2020.

Macro Outlook for 2021

Macro Outlook

Strong global recovery supported by continued government stimulus and the possible widespread availability of COVID-19 vaccinations in H2 2021.

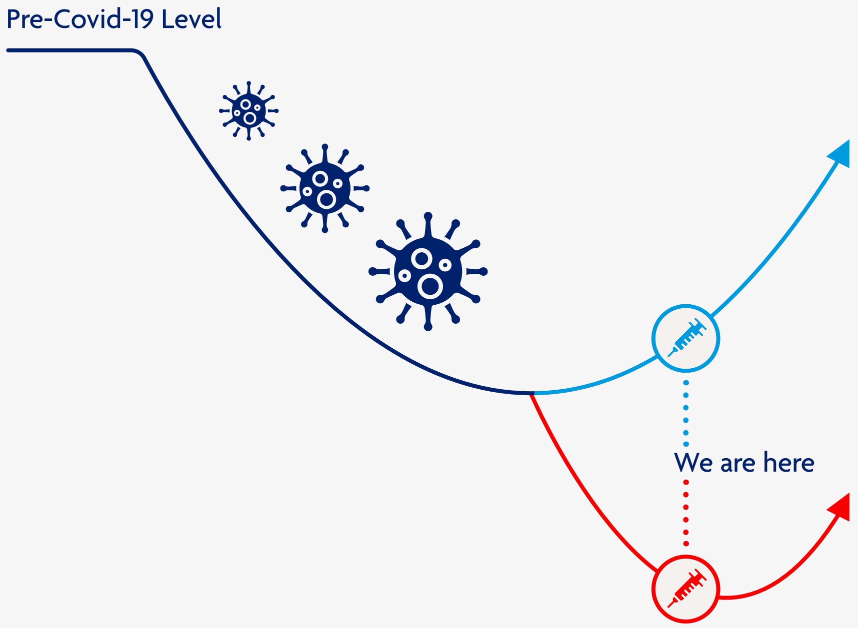
A multi-speed recovery, dependent on vaccines and spending

With the pandemic continuing to impact global economies, we expect a K-shaped recovery (Figure M1), differentiating industries and regions that have emerged quicker and in better shape from the recession. This favours countries such as China, Taiwan and South Korea, and sectors like E-commerce, Electronics, Software and Pharmaceuticals. These 'winners' will outperform regions that were worse hit by COVID-19, such as India and Latin America, as well as sectors related to Travel, Tourism and Hospitality.

Figure M1. We expect a K-shaped recovery due to the differentiation in recovery speeds between regions and sectors that have been impacted by the pandemic.

K-shaped Recovery

The diverging paths of how economies (Emerging Markets and Developed Markets) and Industries / Sectors have been performing.



Positive Performance

Economies on the recovery path

- United States
- China
- South Korea
- Vietnam

Industries thriving amid COVID-19

- E-commerce
- Technology
- Gaming apps / Services
- Electronics
- Pharmaceuticals

Negative Performance

Economies facing challenges on the recovery path

- India
- Indonesia
- Thailand
- Japan
- UK (+Brexit)

Industries impacted by Covid-19

- Tourism-related
- Airlines
- Travel & Hospitality
- Entertainment

As we approach the middle of 2021, COVID-19 cases are expected to fall as widespread vaccination takes place across the world. Governments can then gradually reduce business and personal restrictions, allowing for economic recovery to accelerate in the latter part of 2021. This will give a boost to all segments of the economy, including the pandemic-afflicted sectors.

In the meantime, governments will continue to provide much-needed economic support. Fiscal spending in the US, for example, is expected to increase under a Biden presidency through infrastructure funding, though a Republican Senate will likely block more aggressive spending plans. The US will likely continue to pressure China strategically to curb its growth, especially in technology, where China is expected to expand its own capabilities (link to china megatrend). This ongoing technology race between the rival economic superpowers will create investment opportunities to tap on.

In continental Europe, the European Central Bank (ECB) will continue injecting money into the economy, while government spending plans will tap on the EUR 750 billion Next-Generation EU (NGEU) Fund. The fund is expected to prioritise green projects, which will be a boon for the environment. In the UK, post-Brexit trade restrictions will leave the UK government with little choice but to spend in order to help buoy the domestic economy.

Macro Outlook

The fiscal outlook for Emerging Markets is mixed. With limited coffers, Latin American governments will face greater spending constraints in supporting the economy. Conversely, most Asian economies are better equipped to provide ongoing economic support due to their earlier recoveries and generally more responsible fiscal discipline.

Figure M2a. GDP Growth

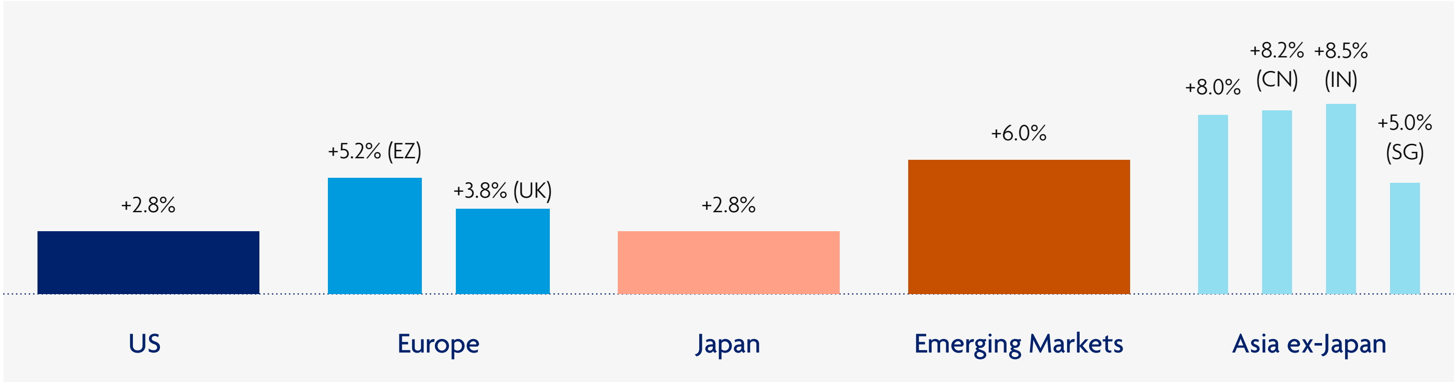
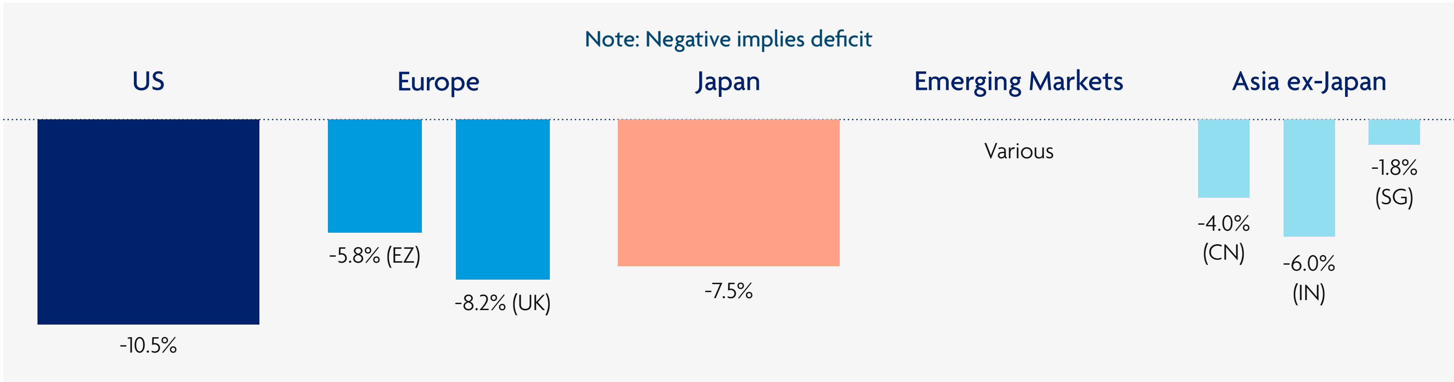


Figure M2b. Fiscal Balance



Sources: UOB Global Economics and Markets Research (4 December 2020), Bloomberg (30 November 2020), IMF World Economic Outlook (October 2020).

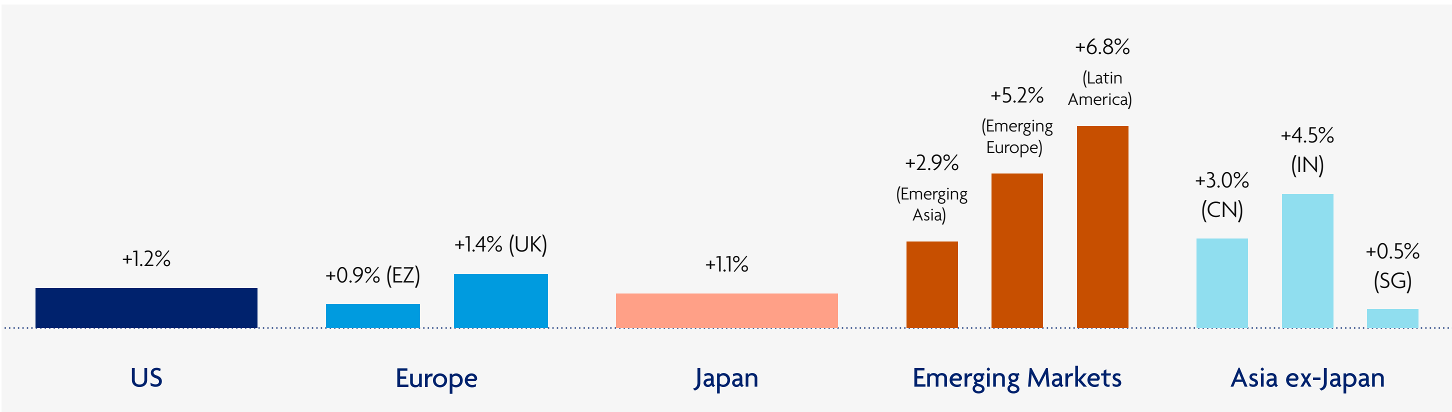
Low interest rates over the coming years will prove to be a key catalyst for a global recovery – assuming inflation remains mildly positive.

Muted inflation and accommodative central banks

With so much government spending anticipated, central banks will generally want to keep monetary policy loose for fear of stunting the recovery. The gradual recovery of demand should keep inflation positive but muted, thus avoiding a deflationary environment.

Against this backdrop, global central banks will more likely take the lead from the US Federal Reserve to accommodate above-average inflation – for example, above 2.0% – for the next three years or so, before considering hiking rates.

Figure M2c. Inflation



Sources: UOB Global Economics and Markets Research (4 December 2020), Bloomberg (30 November 2020), IMF World Economic Outlook (October 2020).

Macro Outlook

As COVID-19 restrictions gradually ease, travel and consumer spending will take off, boosting earnings for companies and supporting a faster recovery. However, the Healthcare, Industrials and Technology sectors may potentially face new policies headwinds that will hamper their growth. per their growth.

Cautious optimism for corporate earnings growth

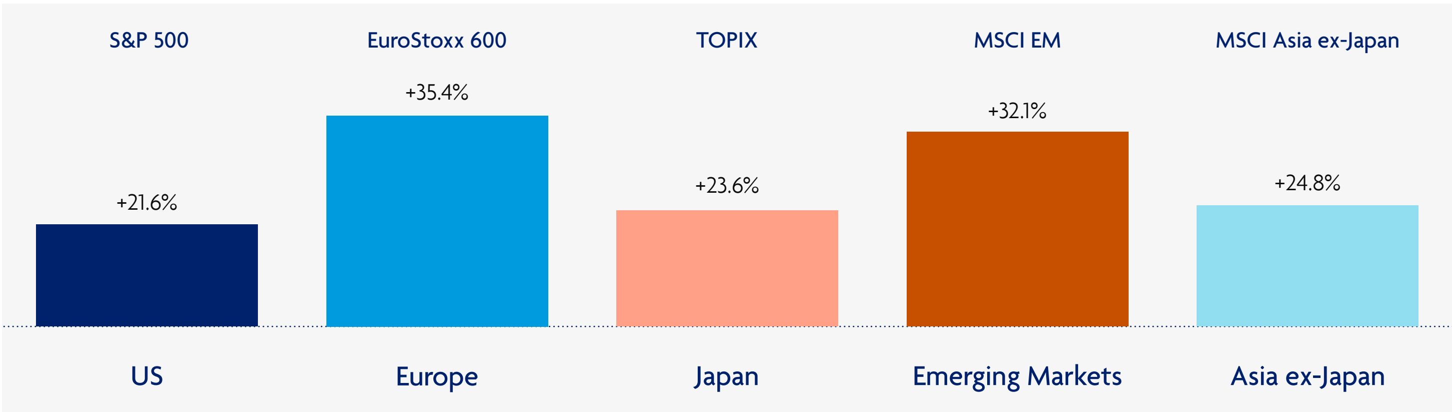
With a low interest-rate and higher-growth environment, corporate earnings are expected to rebound from 2020 levels. The Industrial and Materials sectors will benefit from a Biden infrastructure plan, although the Senate may resist a large package. High-growth companies such as those in the Technology space will likely continue their outperformance, although increasing scrutiny from US regulators might hamper their growth potential.

The Healthcare sector faces the risk of similar regulatory and profitability pressures with any expansion of the Affordable Care Act (aka Obamacare) due to greater oversight and price restrictions set by the US government, but healthcare technology developments will increase the overall sector's growth potential.

Potential tax increases in the US would dent net profitability for many corporates, but improving economic data and increased government spending should cushion any negative impact.

A relatively bright outlook awaits the Travel and related industries, but only when widespread vaccination is available and takes place. Companies that depend on consumer discretionary spending will likely see healthy earnings growth as employment and wages improve.

Figure M2d. Earnings Growth Forecast (EPS)



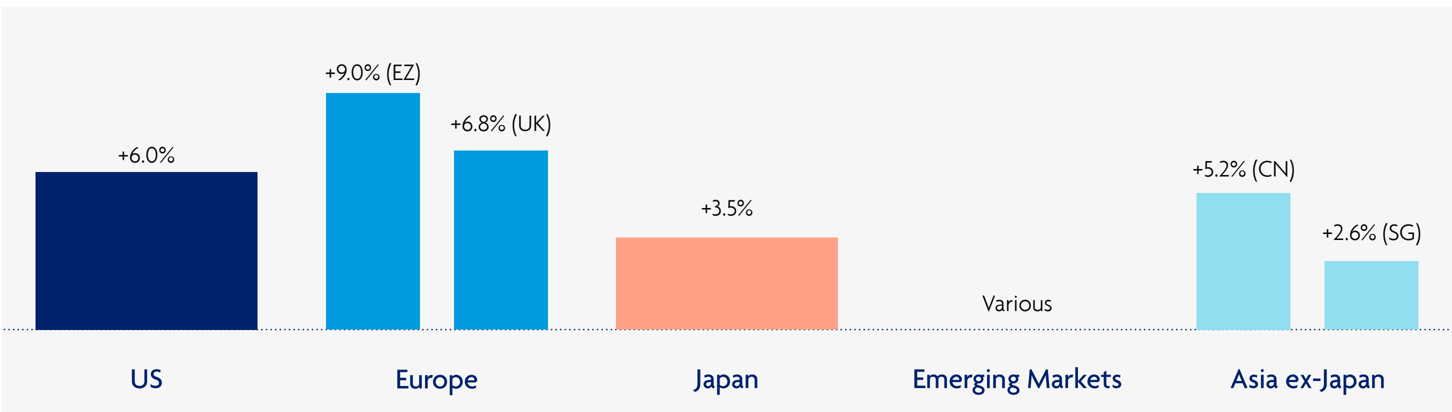
Sources: UOB Global Economics and Markets Research (4 December 2020), Bloomberg (30 November 2020), IMF World Economic Outlook (October 2020).

Consumer spending will rise as job seekers experience an uptick in hiring, and consumers embrace post-COVID freedom.

Renewed optimism to spur consumer spending

With hiring expected to pick up as the economy recovers, families will benefit from higher levels of disposable household income. Pent-up demand suggests that discretionary spending in areas such as travel and leisure, dining out and luxury goods, will likely improve amid easing COVID-19 measures and the economic recovery gathering momentum. Spending on consumer staples like groceries and daily necessities are likely to remain constant, therefore limiting any upside for this sector.

Figure M2e. Unemployment Rate



Sources: UOB Global Economics and Markets Research (4 December 2020), Bloomberg (30 November 2020), IMF World Economic Outlook (October 2020).

Sustainability – doing well while doing good

In a bid to improve business practices, Environmental, Social and Governance (ESG) factors have become an important long-term trend that will also shape sustainable investment themes and processes.

A company's desire to "do good" for society no longer has to come at the expense of profit. Amid efforts by organisations in all sectors to act and behave sustainably (Figure M3) in line with public opinion, they can now do so while still remaining profitable.

In particular, heightened expectations of consumers and shareholders are creating pressures that drive higher ESG standards. Companies that embrace this approach stand to gain from greater social standing and more sustainable revenue streams.

Figure M3. ESG covers a wide range of aspects where sustainability is increasingly important

Environmental Conservation of the natural world	Social Consideration of people & relationships	Governance Standards for running a company
• Climate change and carbon emissions • Air and water pollution • Biodiversity • Deforestation • Energy efficiency • Waste management • Water scarcity	• Customer satisfaction • Data protection and privacy • Gender and diversity • Employee engagement • Community relations • Human rights • Labour standards	• Board composition • Audit committee structure • Bribery and corruption • Executive compensation • Lobbying • Political contributions • Whistleblower schemes

Source: CFA Institute

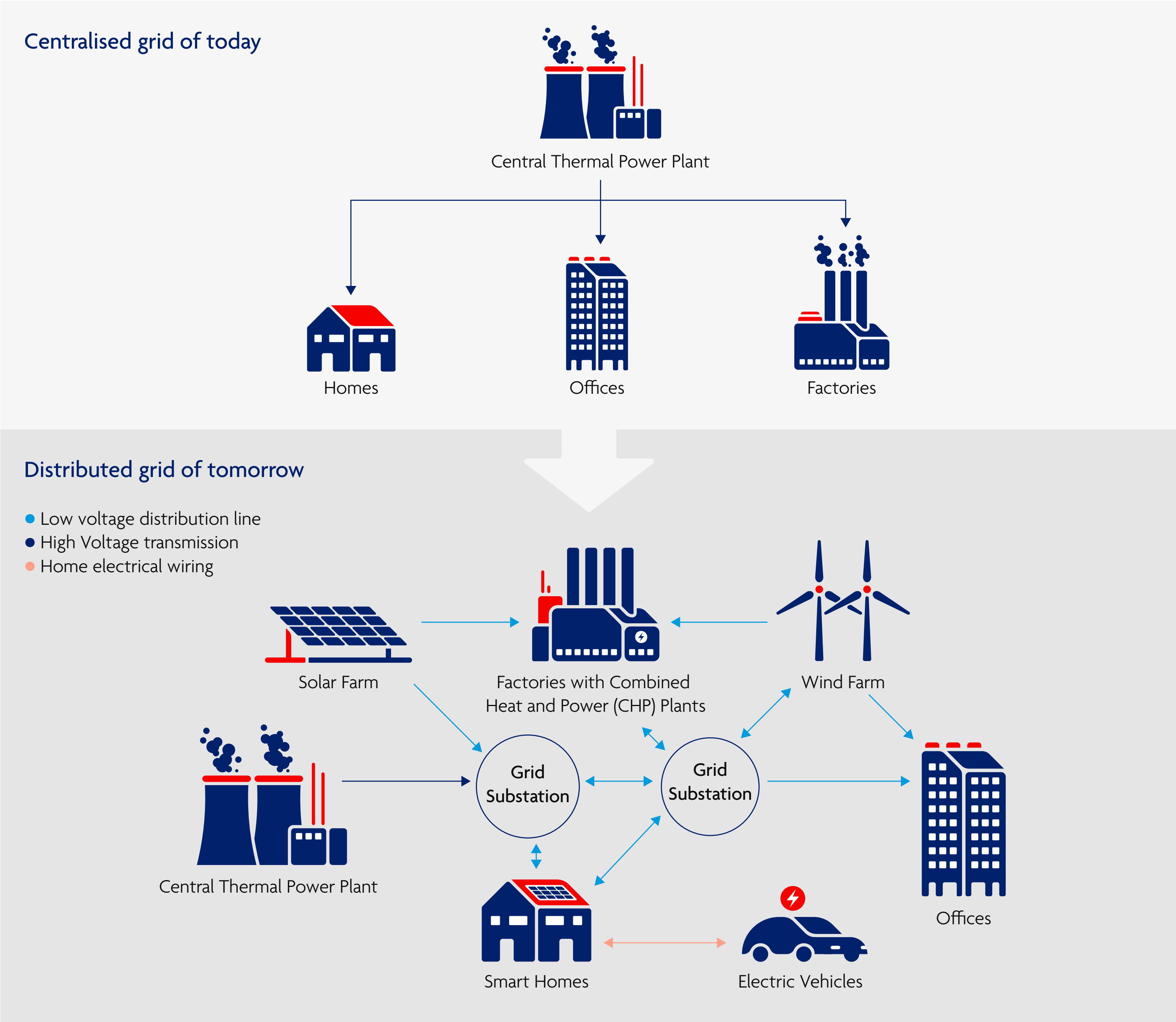
These dynamics are here to stay because of several complementary reasons. Firstly, it makes good business sense to incorporate sustainability into business practices. Reducing resource wastage in manufacturing or services creates cost savings and thus improves profitability. Such companies also tend to emphasise customer and staff satisfaction, resulting in greater customer and worker loyalty that helps to drive their growth.

Secondly, governments around the world are increasingly introducing legislation to combat climate change. ESG-compliant companies will have an advantage over companies lagging in this aspect, and will likely face lower reputational and financial risks or penalties by avoiding ESG-related violations.

Sustainability – doing well while doing good

Thirdly, greater demand by investors for ESG considerations has accelerated green initiatives. For example, the circular economy ensures products are designed to be durable, repairable, reusable and recyclable. Electricity grids are also decentralising towards a distributed, web-like grid to connect multiple sources of renewable energy to various users, thereby providing for more alternative power sources in case one or more fails, whilst reducing pollution (Figure M4).

Figure M4. Renewable energy requires a more web-like power grid, which provides more redundancies in the event of a failure in part of the grid.



Source: Allianz Global Investors, January 2020

Finally, the Sustainability sector is a job creator. The transition to a greener economy requires new skills for both existing and newly-created jobs. For example, renewable energy is expected to increase the total Energy sector employment from 58 million today to 100 million by 2050[2], while every USD 1 million investment in ecosystem restoration projects created 31.5 jobs directly and indirectly[3].

Ultimately, there is a compelling case for ESG investing as we highlight via our Sustainability Megatrend call.

2 OECD, International Renewable Energy Agency (IRENA), October 2020
3 OECD, February 2016

Dealing with ballooning government debt

Governments must drive domestic economic rebounds to reduce unprecedented debt levels created by the fiscal and monetary response to the pandemic. However, markets and investors will need patience, given that this will take time.

The scale of handouts required to address the economic shutdowns due to COVID-19 has inevitably led to government debt levels not seen since World War II (Figure M5). While these handouts reduce the negative economic consequences, it brings future challenges for governments and investment opportunities.

Implications of this growing government debt include higher taxes for future generations to help reduce the debt levels so that governments can provide healthcare and social security for older generations. In turn, this will likely reduce monies available for corporate investments and reduce productivity growth.

The ballooning deficit is already complicating policy choices as governments deliberate on more support packages, while managing growing debt levels. Yet, for as long as investors are willing to buy new debt issues, this cycle can continue.

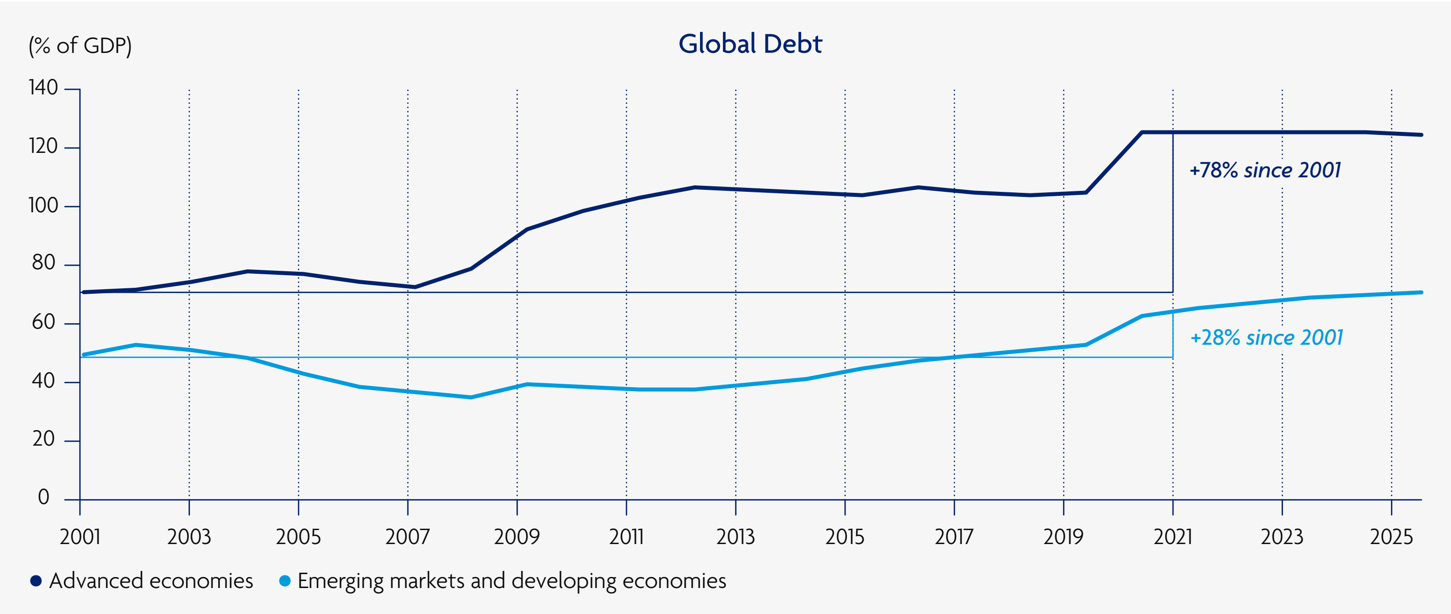
Low interest rates have been helpful in making it less costly for governments to borrow money. This makes it easier for governments to continue to roll over their debt and spend more if needed.

Governments have a number of options to reduce debt levels in a post-COVID world, namely

- Growing the economy faster than the growth in debt; as the US did after World War II
- Reducing government spending and increasing taxes, although timing is key – higher taxes enacted too soon could disrupt the recovery
- Introducing taxes on the digital economy to tap on its growth
- Closing tax loopholes to stem losses in potential government income

Regardless of these or any other measures, reducing debt levels to lower – and healthier – levels will take years. In the meantime, governments need to tread carefully and slowly to avoid potentially derailing economic recovery.

Figure M5. Government debt has been increasing over the years, but has spiked in 2020.



Source: IMF World Economic Outlook Database, October 2020

Key Drivers and Risks

Drivers

Vaccine-driven recovery plus loose monetary and fiscal policies	Further digitalisation and technological advances	Resetting diplomatic relationships
• Central banks and governments will maintain their supportive economic stance. • Widespread vaccine availability towards mid-2021 will boost confidence.	• Accelerated digitalisation brought about by COVID-19 will continue and further enhance efficiency and productivity and in turn propel economic growth. • Workers who up-skill or re-skill can take on higher-value jobs, thereby improving their wages and livelihoods.	• A return to a more diplomatic, collaborative and multi-lateral approach by incoming US President Joe Biden to address key global issues such as growth and climate change.

Risks

Vaccine delays or poor efficacy	Continued global economic deterioration	Further protectionist measures
• Delays in vaccine development and/or overall effectiveness will prolong economic uncertainty. • The subsequent need for further government support will increase debt burdens in the short term and potentially interest rates moving forward.	• The possibility of companies failing and governments' inability to inject further stimulus – regardless of a vaccine – will result in increased unemployment, which will in turn reduce global demand and hamper recovery.	• Similar to China's dual circulation approach amid its rift with the US, more countries may begin to look inward and focus on stimulating domestic recovery, rather than trade internationally.

Strategy

The world that emerges from COVID-19 will be different from the world we left behind pre-pandemic. The economic recovery post-COVID-19 will be broad-based, but certain trends will thrive better than others. For example, digitalisation has become the norm for social and professional interactions, while travel may never be the same again.

Uncertainties will likely remain over how this new world will be like. Yet, several long-term Megatrends remain intact: China is placing more emphasis on its domestic economy, Artificial Intelligence (AI) adoption continues to be a key engine of the new economy, and technological advances continue to open up new possibilities, particularly in Healthcare.

Increased attention towards ESG factors is a key pivot. Both governments and companies will be increasingly differentiated by their willingness to act and behave sustainably. The substantial spike in government debt in 2020 requires policymakers to tread carefully so as not to upset the economic recovery.

Looking ahead, investors should continue to tap on these long-term drivers identified, and adhere to these time-proven investment practices:

- Know your own risk appetite and do not invest beyond your risk thresholds.
- Maintain a diversified portfolio with an appropriate mix of core and tactical investments to minimise possible drawdowns due to unforeseen market events.
- Invest regularly in tranches and avoid timing the market.
- Review your portfolio periodically with your UOB Advisor, or upon recent significant life events, as your financial objectives may have changed.

Key Events Calendar 2021

• Political • Central Banks • Major Event

January

20 January
US Presidential Inauguration

21 January
ECB Meeting

25 — 29 January
World Economic Forum, Digital Davos

February

12 — 17 February
China Spring Festival Golden Week

March

11 March
ECB Meeting

16 — 17 March
US FOMC Meeting (+ Summary of Economic Projections)

April

22 April
ECB Meeting

May

13 — 16 May
World Economic Forum Special Annual Meeting in Singapore

June

10 June
ECB Meeting

15 — 16 June
US FOMC Meeting (+ Summary of Economic Projections)

July

22 July
ECB Meeting

23 July — 8 August
Summer Olympics in Tokyo, Japan

September

9 September
ECB Meeting

21 — 22 September
US FOMC Meeting (+ Summary of Economic Projections)

October

1 October
World Expo in Dubai, UAE

22 October
Japan General Elections

24 October
Germany Federal Elections

28 October
ECB Meeting

November

1 — 12 November
UN Climate Change Conference in Glasgow, Scotland

December

14 — 15 December
US FOMC Meeting (+ Summary of Economic Projections)

16 December
ECB Meeting

Asset Classes and Strategy

Using VTAR to identify ideas

Our award-winning framework focuses on analysing large volumes of financial data in the four components of Value, Trend, Activity and Risk (known as VTAR). This framework provides a holistic view of financial markets and identifies investment opportunities across asset classes, sectors, geographical regions, and time periods. The UOB Personal Financial Services Investment Committee examines these insights, in tandem with key risks, and comes to a consensus to determine the attractiveness of each potential investment idea.

Purpose
Identifying investments with attractive valuations and earnings potential.

Common Indicators
- Price-to-Earnings Ratio (P/E Ratio)
- Earnings Growth (EPS Growth)
- Option-Adjusted Spreads (OAS)

Purpose
Understanding the trend of the investment.

Common Indicators
- Simple Moving Averages (MAs)
- Relative Strength Indicator (RSI)
- Fund flows

Purpose
Understanding the macro environment and business activities that may affect performance.

Common Indicators
- Central bank policies
- Composite Purchasing Managers Index (PMI)
- Industrial Production (IP) and Retail Sales

Purpose
Identifying key markets risks and potential mitigating factors.

Common Indicators
- Geopolitical events
- Industry- or region-specific events
- News flows

Asset Class Views

Financial markets have turned optimistic, driven by COVID-19 vaccine developments. We have upgraded to a positive view on equities and remain slightly positive on fixed income. However, investors should be prepared for uncertainty in the path of economic recovery and possible policy changes due to new political developments.

Equities

We are currently neutral on the US as valuations appear stretched, with corporate earnings recovery and growth being reliant on further fiscal stimulus. We see selective opportunities within Europe, given a watershed fiscal agreement (EU Recovery Fund). However, COVID-19 infections need to be managed well for Europe's recovery to be stronger. We remain negative on Japan despite greater political stability, as it remains heavily reliant on a pickup in global demand.

In Emerging Markets, we are not optimistic on Latin America, Eastern Europe and the Middle East, all of which either have less room for more stimulus given unsustainable deficits, or may be too reliant on commodity prices for growth. A better control of the COVID-19 situation could lead to an upgrade on this outlook.

Asia ex-Japan, especially China, is where we think the best opportunities lie, especially with more attractive valuations (P-E Ratio: 15.5x) than developed markets (P-E Ratio: 20.6x). With better virus control throughout Asia, coupled with China's economy recovering, exports and earnings are expected to improve in the region, supported by the signing of the Regional Comprehensive Economic Partnership (RCEP).

Fixed Income

Central banks are likely to keep their monetary policies loose to support economies as companies adapt and remodel. This implies that interest rates are likely to stay low for longer. We are slightly overweight on fixed income, but investors have to be selective as not all segments present great value.

We are negative on government bonds as yields remain low and unattractive, and they remain vulnerable to unexpected spikes in inflation. Corporate investment grade (IG) bonds will be supported by easy monetary policies, and we prefer Asian investment- grade (IG) bonds for their relatively higher yield of 2.0% to 2.5% and wider spreads than the broader global bond index. As for high yield (HY) bonds, we turned neutral as the current yields may not compensate for the possibility of higher defaults should economic conditions continue to weaken.

We are neutral on Emerging Market bonds as yields and spreads are now less attractive and could widen if COVID-19 infections remain uncontrolled, causing global trade to take longer than expected to recover.

Currencies and Commodities

The US dollar is likely to gradually weaken against both developed market and Asian currencies as the Fed continues its easing programmes and as US interest rates remain low for longer.

The pick up in global demand and OPEC+ production cuts will likely push oil prices to USD 55/bbl by Q3 2021. We expect Gold prices to remain supported on the back of central bank easing, rising to USD 2,000/oz by Q4 2021.

Asset Class Views

Equities

• Positive • Neutral • Negative

Subclass	VTAR	Negative	Slightly Negative	Neutral	Slightly Positive	Positive
US	V T A R			●		
Europe	V T A R				●	
Japan	V T A R		●			
Asia (ex-Japan)	V T A R				●	
Emerging markets (ex-Asia)	V T A R			●		

Fixed Income

• Positive • Neutral • Negative

Subclass	VTAR	Negative	Slightly Negative	Neutral	Slightly Positive	Positive
Developed market (DM) government bonds	V T A R		●			
DM investment grade bonds	V T A R			●		
Global high yield bonds	V T A R			●		
US-dollar emerging market (EM) debt	V T A R			●		
Local-currency EM debt	V T A R			●		

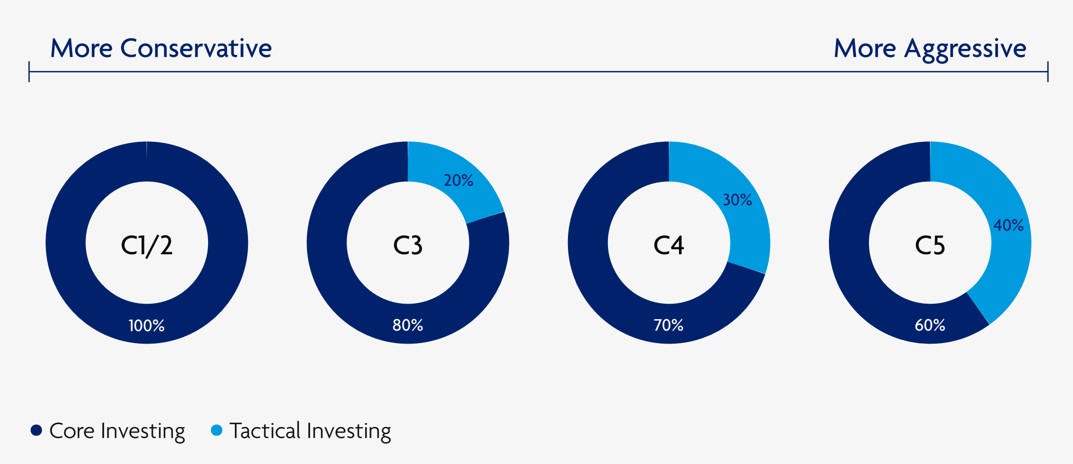
Currencies and Commodities

Subclass	Negative	Slightly Negative	Neutral	Slightly Positive	Positive
Gold				●	
Oil				●	
US dollar		●			
Singapore dollar				●	

Strategy Summary

UOB Risk-First Approach

The dual-track K-shaped recovery is expected to be uneven, which can result in market volatility even as economies reopen. Our proprietary Risk-First approach can help smoothen the ride for our clients – depending on their risk profile, portfolios are constructed with a maximum of 20%, 30% or 40% allocated to Tactical investing (which has higher risk), and the remainder in Core investing.



Core Investing

Relatively lower risk in nature, yet able to generate reasonable returns that tend to be less volatile than the broader market in order to meet most clients' financial goals. An allocation to Core solutions helps to lower downside volatility – a much-needed outcome in such a challenging period.

Short- to medium-duration investment grade bonds

The defensive nature of these liquid bonds enables them to weather heightened volatility, giving investors greater portfolio stability. This asset will also experience lower drawdowns should central banks abruptly reverse their low-rate stance due to an inflation spike.

Asian investment grade bonds

This asset class offers a good balance between defensiveness and yield. With relatively higher yields (2.0%—2.5%), compared with the broader global bond index (0.9%), and with spreads near their historical average (166 basis points), these bonds will benefit from the region's earlier resumption of economic activity from the COVID-19 pandemic.

Global multi-asset strategies

These strategies offer a flexible and diversified asset allocation to capture opportunities in a variety of market conditions and across various asset classes – including equities, bonds and alternatives. They can provide a mix of both income (historical 12-month yields of 4.5%—5.4%) and capital growth to meet an investor's financial goals.

Tactical Investing

Tactical strategies are identified using our award-winning VTAR framework, which focuses on analysing financial data in the four components of Value, Trend, Activity and Risk (VTAR). The framework aims to provide a holistic view of financial markets and identify investment opportunities across asset classes, sectors, geographical regions and time periods.

Megatrends (3 to 5 years)

- Sustainability
- China
- Global Healthcare
- AI & Innovation

High Conviction Calls (6 to 12 months)

- Asia ex-Japan Equities
- Global Equities with High Quality Factors

Sustainability

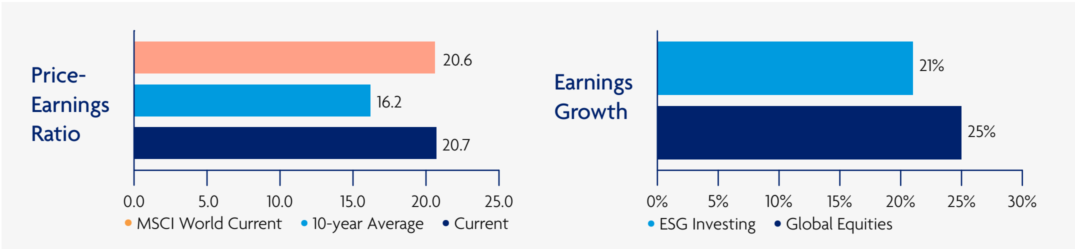
VTAR Rating
- Positive
- Neutral
- Negative
- Not Applicable

Sustainable investing has attracted significant attention from investors as a way to achieve sustainable long-term returns. This interest is likely to accelerate, with total ESG managed assets expected to grow more than five times by 2036.

Three key factors are used to measure the sustainability and societal impact of investing in a company – Environmental, Social and Governance, or ESG. By incorporating ESG factors into investment decisions, portfolios can potentially better manage downside risk and generate higher risk-adjusted returns over time.

Companies that embrace ESG tend to gain a more loyal customer following. For example, customers are more likely to buy from companies that recycle waste materials to make new goods, in order to reduce their individual carbon footprint. These companies also tend to avoid issues that may result in reputational damage, drawn-out lawsuits and fines that come from ESG-related violations, which are risks that can impact shareholders' returns.

Investor interest in ESG factors has grown rapidly since the COVID-19 outbreak. For example, 71% of institutional investors[4] globally plan to integrate ESG into their investment process by 2030. This heightened interest has led to ESG-strong companies becoming expensive, but this valuation continues to remain supported by a clear technical uptrend.



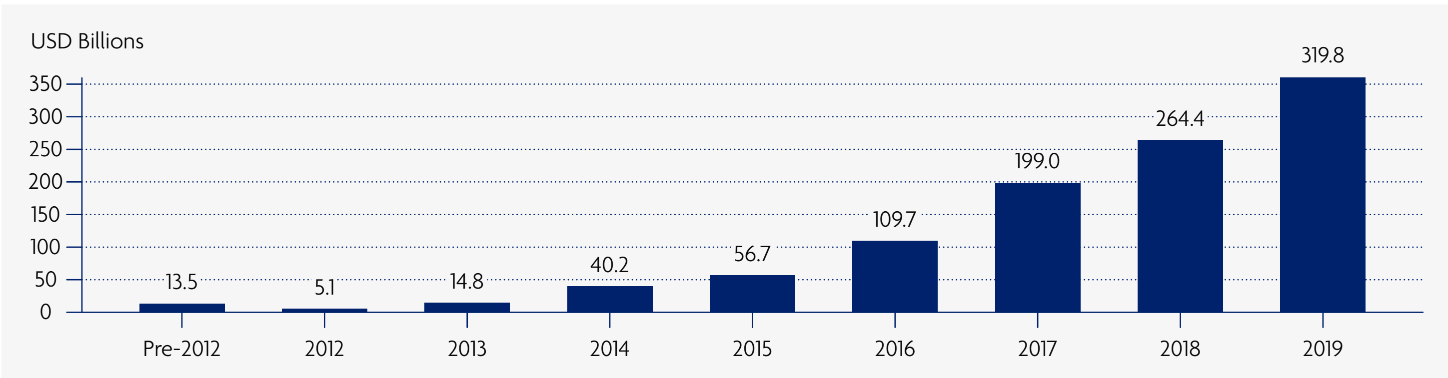
This interest is likely to lead to ESG-related managed assets growing from an estimated US$30 trillion in 2020 to US$160 trillion by 2036[5] and a significant increase in sustainable debt issuance (Figure C1) – both of which will likely accelerate as interest grows.

There are risks that investors should be aware of, however. For example, while there are genuine ESG-strong companies, there are also those that may conduct 'greenwashing' – providing misleading information on the friendliness of their environmental policies. In addition, companies that embark on the ESG path might need to invest significantly in the near term – this will impact their immediate cash flow and profitability, in order to benefit over the longer term.

While Europe and the US are more advanced in ESG investing and regulations, Emerging Markets such as China, Brazil and India are rapidly catching up. Companies that adopt ESG business practices early will likely benefit as governments are likely to implement more stringent climate-friendly regulations over time.

There are also clear financial benefits of this trend for long-term investors. For example, green bonds can be issued at a slightly lower yield than comparable bonds, giving companies with strong ESG practices access to cheaper funds. Such companies will also gain the attention of investors through their responsible practices, thus attracting greater investor interest.

Figure C1. Sustainable debt issuance has increased significantly in the past five years alone.



Source: Bloomberg New Energy Finance

4 Allianz Global Investors "Institutional Investor Survey", April 2019
5 Deutsche Bank, Global Sustainable Investment Alliance, Financial Times, September 2019

Megatrend
China

VTAR Rating
- Positive
- Neutral
- Negative
- Not Applicable

China's government is committed to developing its domestic market. This effort will expand and accelerate opportunities for investors who are already focused on various onshore sectors and themes.

China's growth story remains a compelling investment case.

As tensions between the US and China are likely to persist, albeit in a more subtle manner under a Biden presidency, the Chinese government's strategy to bolster the domestic economy is gathering pace.

By opening its market wider, China seeks to improve competitiveness, and obtain scientific collaboration with new partners to counter the US's attempt in restricting China's access to the global technology supply chain. These goals are aligned with a domestic desire for higher standards of living, which will in turn lead to increased demand for higher quality education, better healthcare and other social services.

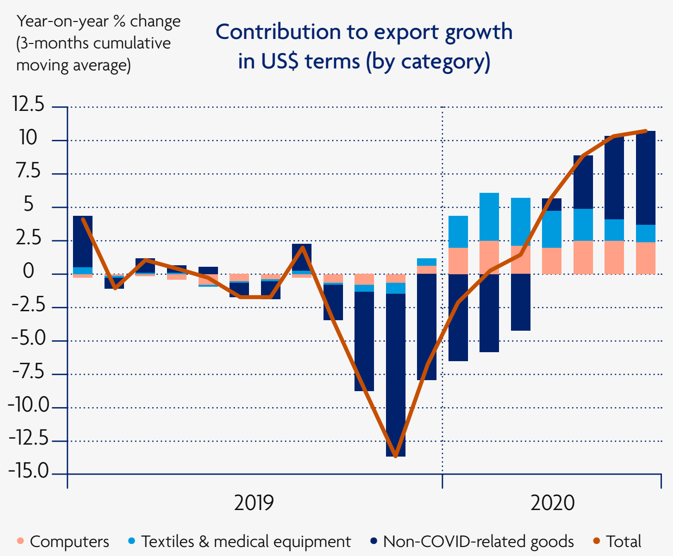
While current P-E ratios are slightly elevated for China A shares (14.6x), they are cheaper than those in developed markets (20.6x). Notably, valuations for China A shares are nowhere near the historical highs seen in 2010 (24.3x) and 2015 (18.6x). Furthermore, corporate earnings are expected to grow by 18% in 2021.

A potential risk is that both US political parties want to restrain the rise of China, suggesting tensions might remain or escalate. In addition, any resurgence in COVID-19 cases will affect global demand for China's exports. Encouragingly, China's exports have seen some recovery and have shifted from pandemic-related goods (e.g. medical supplies, computers) to regular consumption goods (Figure C2), and will grow further following the signing of the Regional Comprehensive Economic Partnership (RCEP).

With the above challenges, China has initiated its "dual circulation" economic approach (Figure C3) to prioritise domestic-led growth. This underscores the potential of the "Made in China 2025" ambition to reduce its dependence on foreign technology.

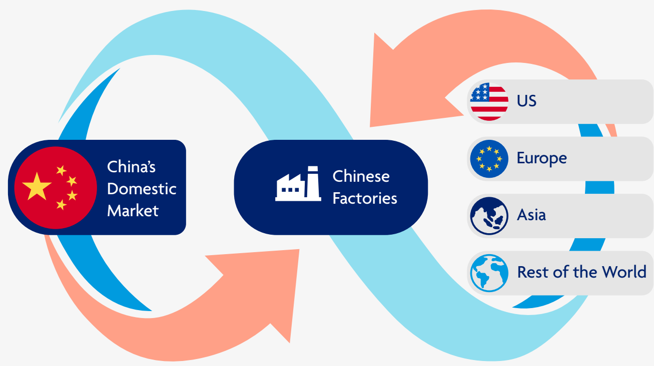
To help drive this ambition, a stimulus plan was announced in April 2020 to enhance communications networks and use Big Data and Artificial Intelligence (AI). The goal is to fuel China's next phase of infrastructure development – this includes large-scale data centres and 5G networks – to compete technologically with the US. With these, China remains a growth market too big for investors to ignore.

Figure C2. China's export surge is broadening beyond COVID-related goods



Source: GaveKal Dragonomics/Macrobond, October 2020

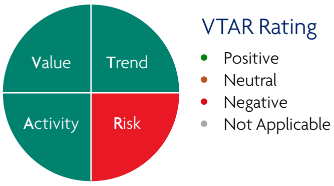
Figure C3. "Dual circulation" emphasises domestic growth to reduce reliance on external demand.



Growing the domestic market to balance its reliance on external trade.

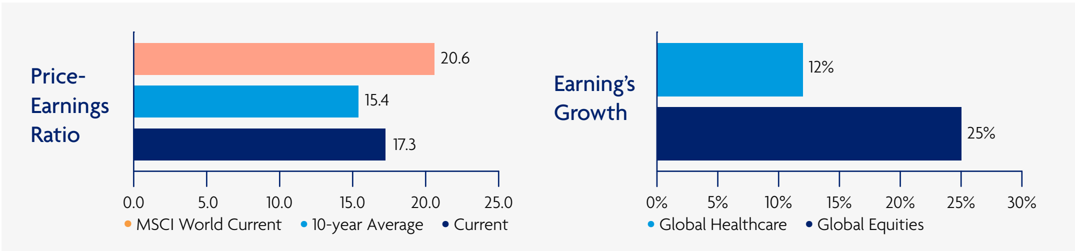
Megatrend

Global Healthcare



The combination of COVID-19 and technological innovation harnessing the power of computing and Artificial Intelligence (AI) has made healthcare more important and accessible. This makes the Healthcare sector an attractive investment theme.

COVID-19 has thrust the importance of healthcare into the spotlight for investors globally. Current P-Es for the sector are high (17.3x), but still lower than that of global equities as a whole (20.6x). Expected earnings growth of 12% in 2021 reflects the upward trend, with momentum picking up steadily.



Consistent fund inflows have followed greater public awareness of the Healthcare sector, spurred by the race for a COVID-19 vaccine.

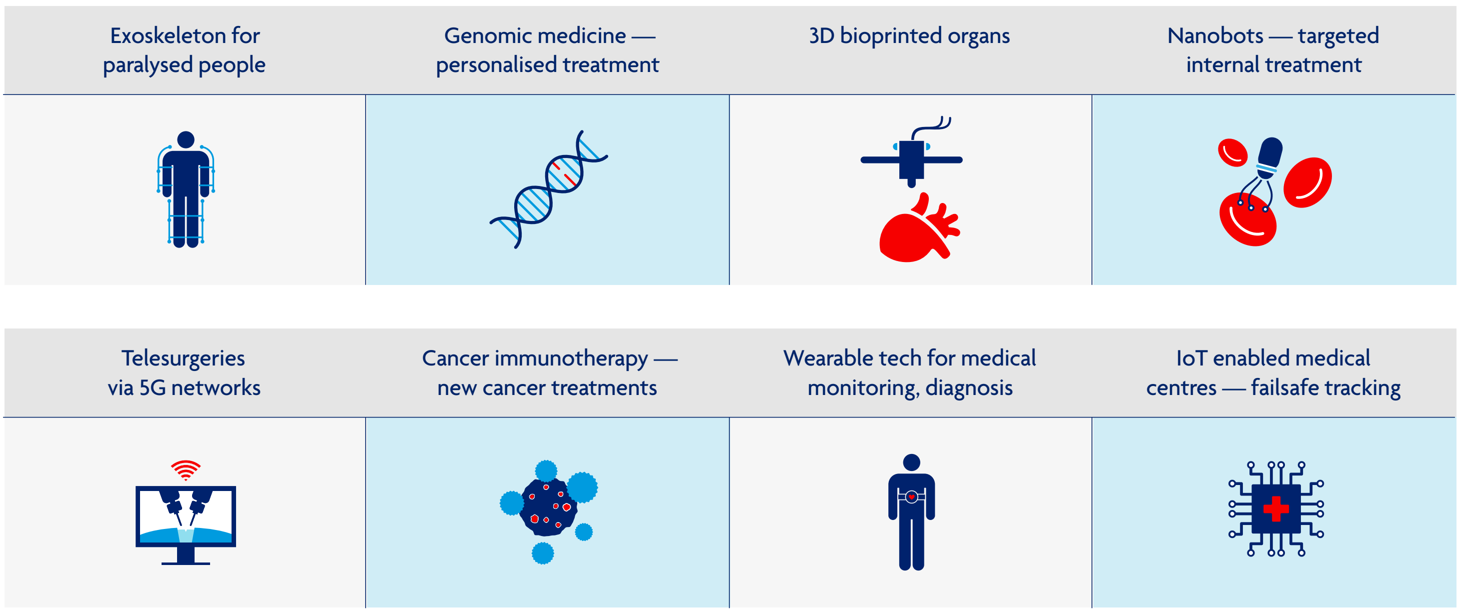
A possible Democratic sweep following the US senatorial elections in January 2021 poses regulatory risks – it can lead to a push to expand Obamacare, which will in turn limit the profitability of healthcare companies by placing caps on drug prices and services. However, growing demand for healthcare goods and services will sustain the Healthcare industry amid periods of economic disruption or policy changes.

At the same time, the pace of progress on potential COVID-19 vaccines highlights the scope to adopt new and emerging technologies (Figure C4). These benefit areas such as biopharmaceuticals and medical technology; and allow healthcare providers to achieve greater efficiencies and provide new methods of service and care.

One example is the use of cloud computing and machine learning in developing gene therapy. Gene therapy requires significant computing power to identify and reverse the effects of a defective gene, and creates the potential to treat almost 100 devastating diseases, including Alzheimer's Disease, diabetes, cancer and HIV/AIDS. Meanwhile, ongoing trials demonstrate the potential of Artificial Intelligence (AI) to predict and diagnose diseases more quickly than even the most experienced medical professionals. AI can also be effective in supporting the daily needs of patients, helping to ensure dementia patients take their medication regularly, or keeping them engaged via virtual interactions.

Acceleration in digitalisation has also increased the demand for new services like telemedicine. This is expected to grow by 21% annually to USD 176 billion by 2026.[6] These exciting developments in the Healthcare sector are key reasons why it deserves a place in long-term investment portfolios.

Figure C4. New technologies benefit many areas, such as biopharmaceuticals and medical devices and healthcare providers.



6 Source: Capital Group, Statista. Forecast includes impact of COVID-19.

Megatrend

Artificial Intelligence (AI) & Innovation

VTAR Rating
- Positive
- Neutral
- Negative
- Not Applicable

The pandemic boosted the adoption of Artificial Intelligence (AI) and related technologies, both at work and home. With innovation increasingly being implemented to offload menial tasks and increase efficiency, companies will be looking to tap on this area of growth to enhance shareholder returns.

As an engine of the digital economy, AI & Innovation received a significant boost as a result of the COVID-19 outbreak. Global lockdowns forced individuals and companies to embrace digitalisation – many businesses believe that AI will transform their organisations within the next three years (Figure C5).

Big Data is fuelling the ability for AI to improve its capabilities. Daily interactions with 'smart assistants' such as Alexa, Siri and Google Assistant, for example, create exponential amounts of data, with an estimated 100 million voice-based smart speakers sold worldwide[7], while improvements in computing power support the more sophisticated algorithms.

Governments are fostering initiatives to research, develop and integrate new technologies into their economies to fuel growth. China, Japan, France, Canada, Germany, India, Sweden, the UK and the US all have targeted AI strategies.

In a world of 'smarter' cities, autonomous electric vehicles can determine optimal travel routes from AI-enabled traffic monitoring, on top of reducing pollution and the need for car ownership. Buildings can become more energy and water efficient, saving both money and resources.

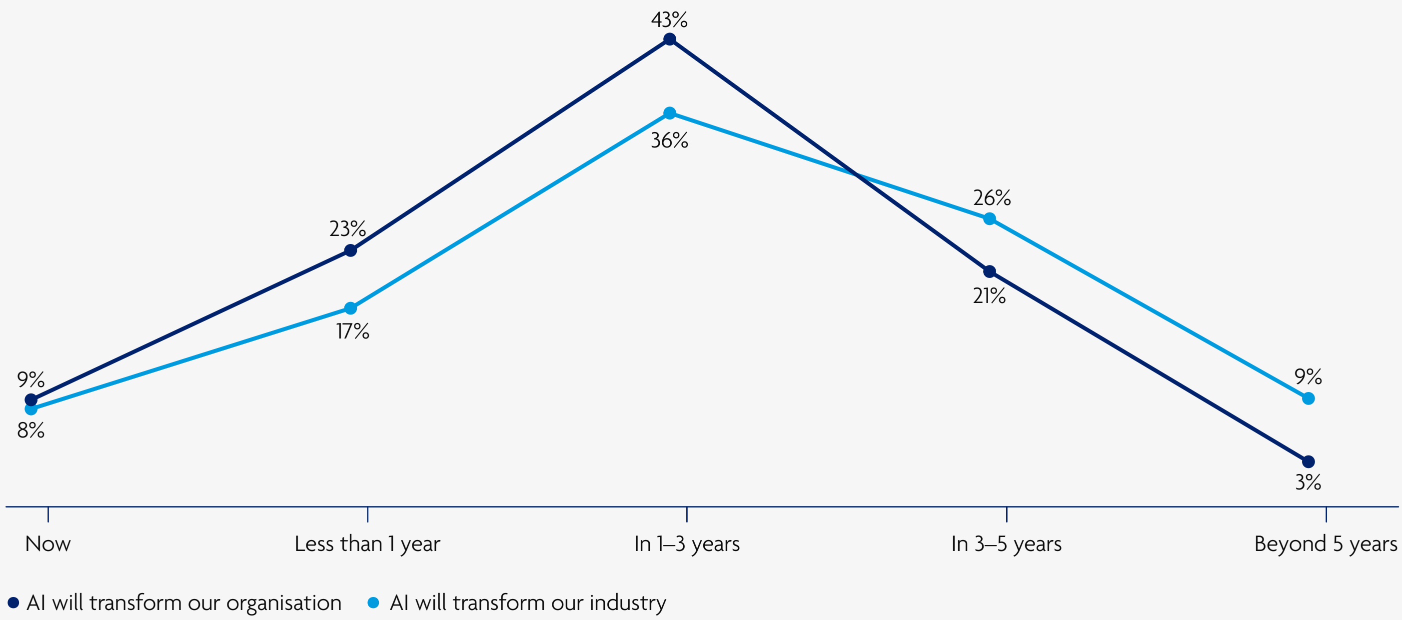
A possible pitfall is the risk of enhanced regulatory oversight. Excessive or inappropriate policies may slow the adoption of new technologies, specifically, policy controls over how technology companies store and use the data they collect. Digital taxes, on the other hand, may create headwinds for global tech giants or emerging AI players.

Yet the momentum of innovation is strong. In financial services for instance, Bank of America now uses predictive analytics to alert customers up to seven days in advance on whether their spending habits will potentially reduce their account balance to zero. Meanwhile, Citibank integrates AI into its fraud detection processes.

UOB, for its part, uses AI to detect suspicious transactions and connected parties to combat money laundering and financial crime. It also employs AI to analyse transaction data, turn that information into meaningful insights and provide guidance on the most suitable financial solutions for its customers via its mobile banking app UOB Mighty.

Ultimately, new opportunities from Big Data and technology tools application are already apparent via 5G, augmented reality, Internet of Things (IoT) and cloud computing, providing a long-term trend which investors can tap into.

Figure C5. Many believe AI will transform their organisations and industries



Note: Percentages may not total 100 percent due to a small number of respondents who answered "Don't know."

Source: Deloitte, July 2020

7 Canalys, August 2018

High Conviction Call

Asia ex-Japan Equities

VTAR Rating
- Positive
- Neutral
- Negative
- Not Applicable

Countries in Asia are emerging from COVID-19 in much better shape; economically and socially; when compared to other parts of the world. This gives the region an advantage for growth, championed by China.

Asia showed impressive levels of preparedness and control in dealing with COVID-19. In 2021, the region is projected to recover quicker and grow faster than the rest of the world (Figure C6).

With stronger domestic appetite in Asia, particularly from China, Asian countries have increased trading with one another (Figure C6). We also see a strong demand in technological products from Taiwan and South Korea, which aids these export-led countries.

A potential risk is Asia's heavy reliance on demand from China. Potential escalation in US-China tensions might dampen regional growth momentum. Furthermore, India continues to struggle with COVID-19 infection rates, impairing its recovery efforts.

However we are encouraged by the Asian governments' ongoing commitment to monetary and fiscal support to limit any downward pressure on growth. The recent Regional Comprehensive Economic Partnership (RCEP) will facilitate intra-Asia Pacific trade and be an additional growth pillar for the region.

Even at valuations higher than its 10-year average (15.5x vs 12x), Asia ex-Japan equities remain cheaper than their developed market peers (20.6x). Their appeal is further boosted by growth expectation in corporate earnings for 2021 which will further improve its valuations.

This will underpin the region's broader, longer-term upward trend.

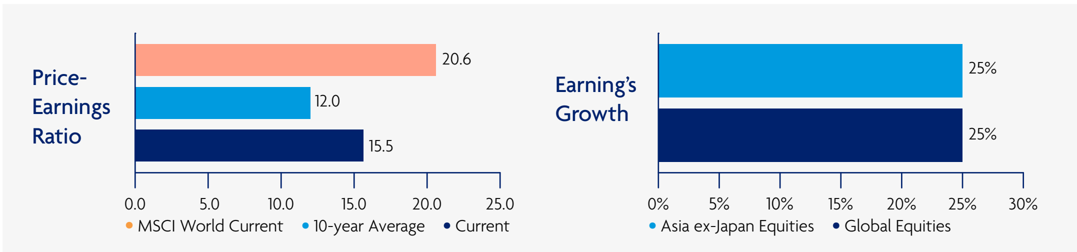
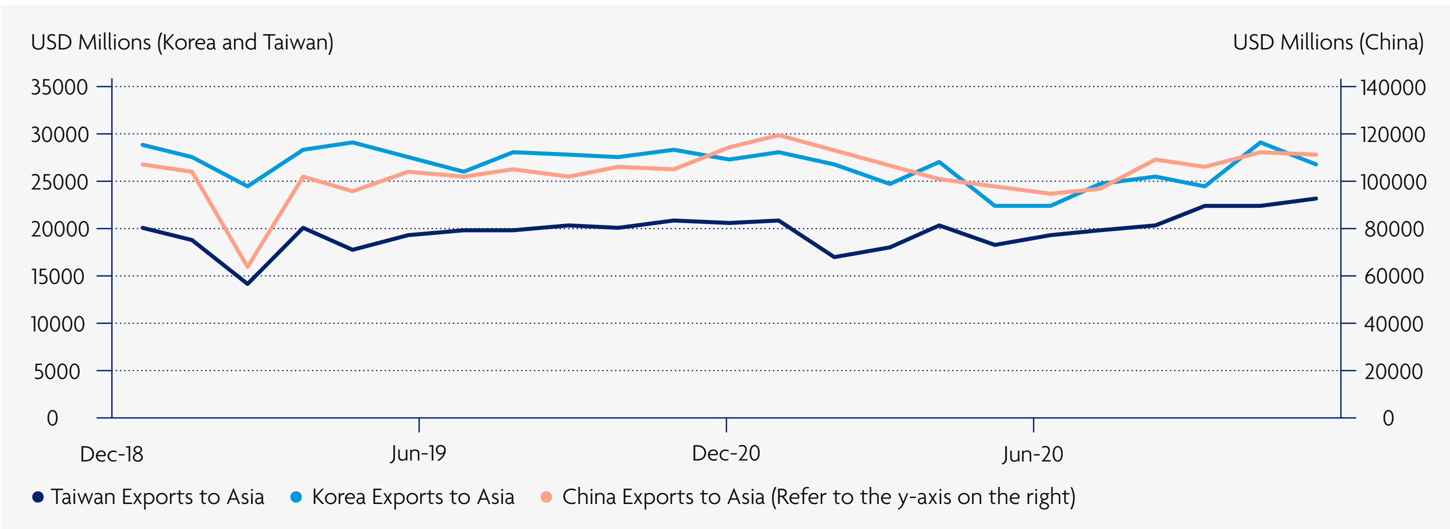
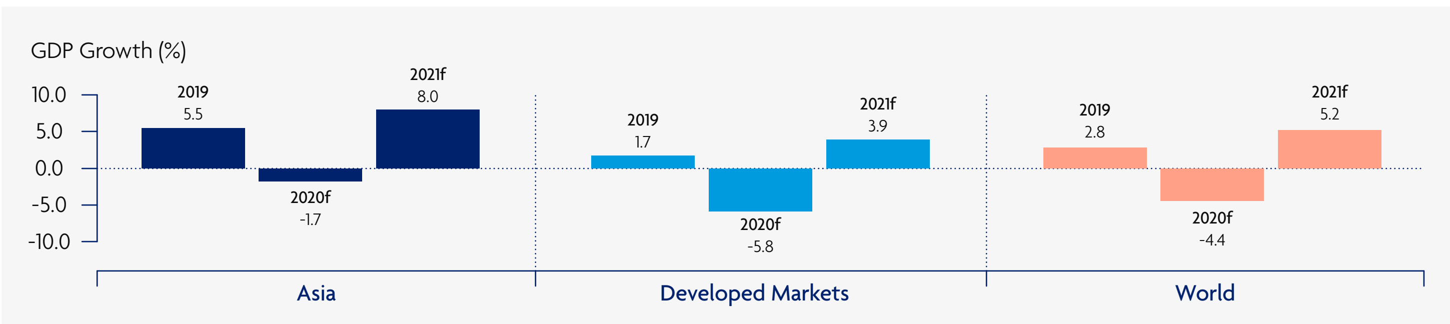


Figure C6. China, Korea and Taiwan exports within Asia have increased this year, while Asia leads in economic growth.

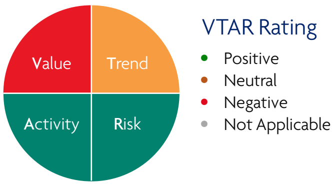




Source: Bloomberg, as at 30 November 2020

High Conviction Call

Global Equities with High Quality Factors



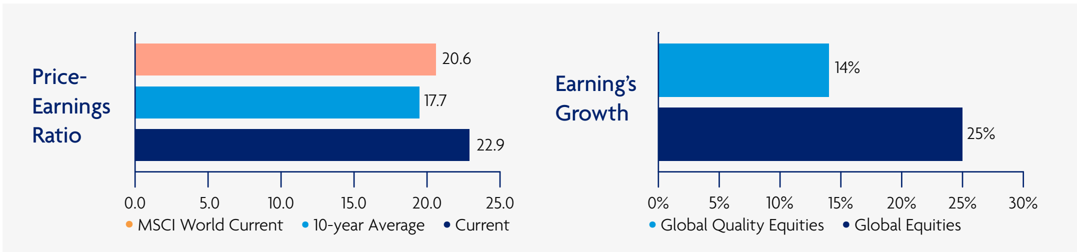
Equities with higher quality characteristics remain attractive. They have proven to be more resilient amid COVID-19 and their growth is likely to accelerate faster than other stocks as economies start to recover.

Higher quality companies continue to stand out, having outperformed the broader MSCI World global equities benchmark (+36.1% vs +27.7%) and generally maintaining a strong upward trend.

Although this momentum has ebbed and flowed in line with localised resurgences of COVID-19, quality equities continue to be driven by multiple themes (Figure C7) and display promising characteristics:

- A high return on equity, which reflects earnings growth potential
- A low debt-to-equity ratio, demonstrating financial discipline in borrowings
- Low variations in earnings, representing consistency

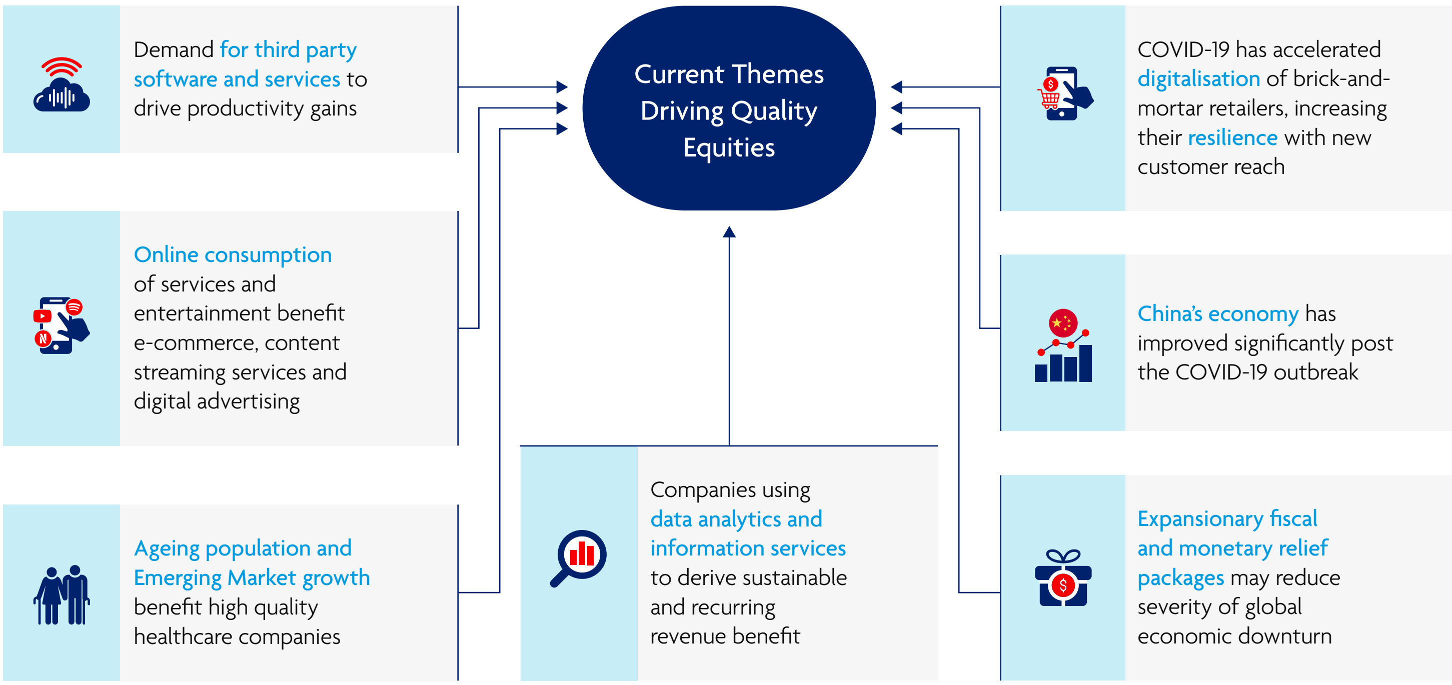
High valuations (22.9x), due to the larger weightage in the technology sector, remain a concern for some investors. Yet earnings are expected to increase in 2021 due to these companies' resilient growth during COVID-19.



Low interest rates and bond yields have also driven valuations higher. Furthermore, trends such as relatively low growth plus low rates are expected to be anchored by the US Federal Reserve for the next three years. Equities with high quality factors tend to be compared with bonds, hence low bond yields will have a positive effect on prices of such equities.

These dynamics should breed investor confidence – high-quality equities that deliver strong growth are appealing alternatives to bonds with low yields. In addition, relatively loose central bank policies and government funding to stimulate domestic economies should support quality equities.

Figure C7. Equities with high quality factors are driven by multiple themes in the post-COVID world



Source: Wellington Management

Country Focus

Singapore

A brighter outlook for Singapore in 2021 will help revive the domestic economy, following significant government spending to cushion the impact of the pandemic. Despite muted tourism-led demand and low oil prices, the recent rebound offers scope for optimism – especially in specific Singapore equity sectors, such as Property Developers, Industrial and Office REITs, and domestic government bond yields relative to US Treasuries.

Amid expected Chinese Renminbi (CNY) gains, the SGD might appreciate against the USD to 1.30 by Q3 2021.

Government spending to spur a steady rebound, countering 2020's record contraction

2020 saw Singapore's worst economic contraction on record, with a forecast of -6.0% for the full year. The Construction and Services sectors have borne the brunt of the decline. However, we expect a U-shaped recovery with a brighter outlook for Singapore in 2021.

The economy is expected to grow by +5.0%, driven by the outsized government spending to support jobs and provide rent relief. This will dampen the potential for the pandemic to create long-term structural damage to the economy.

Lower domestic and tourism-led demand, plus low oil prices, is expected to keep inflation muted. Yet three factors are expected to contribute to Singapore's gradual recovery: The improving COVID-19 situation, with minimal community infections since late August 2020; steady reopening of the economy since the end of the circuit breaker, with the government exploring air travel bubbles to reopen borders to international visitors and trade; and greater support for the biomedical industry amid stronger global pharmaceutical-related demand (Figure R1).

Equities

Singapore equities will likely benefit from global monetary stimulus and generous COVID-19 government support packages. However, the recovery is expected to be uneven. For instance, property developers, industrial and office REITs should be less affected due to their larger cash buffers and longer lease expiries. Meanwhile, banks, along with transport and aviation companies, may underperform due to rising credit risks and delayed recovery in demand respectively.

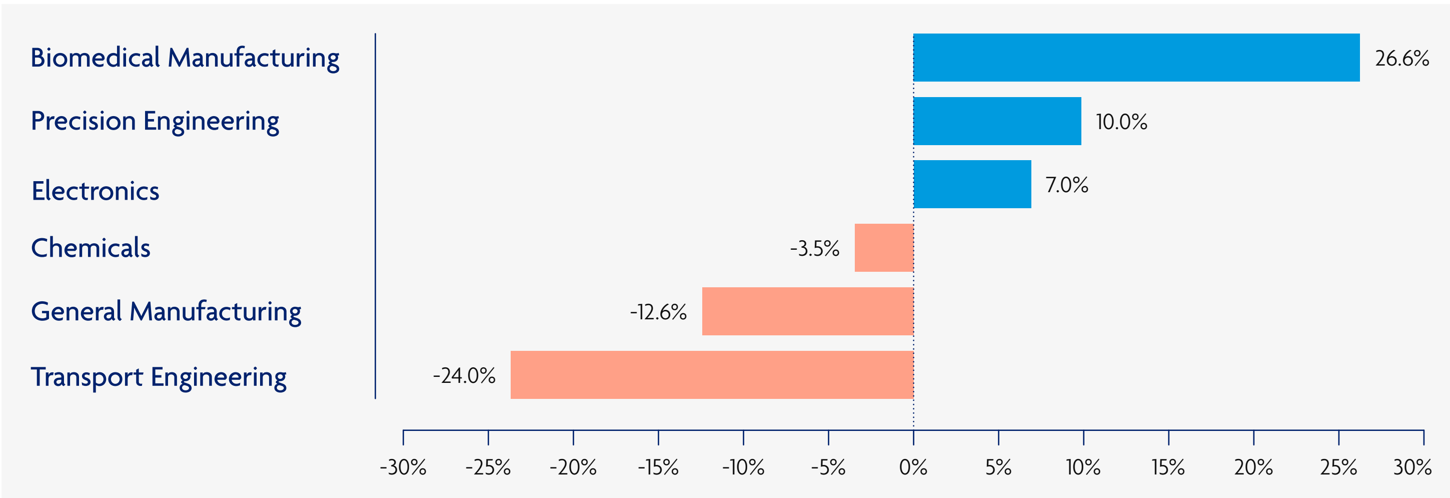
Fixed Income

Domestic government bond yields will likely remain low for 2021, but still trend higher than US Treasury yields. While credit spreads are expected to tighten further in 2020 and early-2021, investment grade (IG) corporate bonds will provide a defensive stance and higher yield pick-up. Inflation for Singapore is expected to remain subdued in 2021.

Currency

Since Q2 2020, the SGD has shown a positive correlation with the Chinese Renminbi (CNY). Given the expected gains in the CNY going forward, there is room for SGD to appreciate against the USD to 1.32 by the end of Q1 2021, and to 1.30 by Q3 2021.

Figure R1. Biomedical manufacturing was the best performing cluster in 2020 and will continue to support the economy in 2021.



Source: Macrobond, UOB Global Economics & Markets Research, September 2020

Malaysia

Initial economic recovery in Malaysia is encouraging, but unlikely to return to pre-pandemic levels until at least 2022. Potential government support could come via a fiscal expansionary approach targeting the sectors most affected by COVID-19.

Bank Negara Malaysia (BNM) is likely to keep its Overnight Policy Rate (OPR) at 1.75% until at least mid-2021.

Although domestic economic recovery is underway, it may be uneven across sectors

Malaysia's GDP is expected to expand to 6.0% in 2021 after an expected contraction of 5.5% in 2020. It is also expected to benefit from the 12th Malaysia Plan (12MP) in January 2021, where the government will likely announce more investor-friendly measures. These could potentially attract more foreign direct investments to further boost the economy.

Key downside risks for the country include it being tied to the global economic recovery pace, the containment of COVID-19 infections and domestic political uncertainties. Moreover, Malaysia has repositioned itself as a manufacturing hub in a bid to be a key player in the global supply chain; it wants to grab a share of the reshoring of manufacturing away from China.

We expect inflation to rise from -1.0% in 2020 to 2.1% in 2021, as the domestic economy recovers and commodity prices stabilise. The MYR is expected to strengthen further to 3.95 against the USD by Q3 2021, whilst BNM is expected to keep its OPR unchanged at 1.75% until Q4 2021.

Equities

With the impact and recovery from COVID-19 likely to be uneven across different sectors, investors need to be selective towards Malaysian equities. Value stocks within the Financial and Healthcare sectors are favoured, as growth equities have massively outpaced value-counters for several years, especially in 2020. Travel-related stocks could continue to face headwinds as long as COVID-19 remains undefeated.

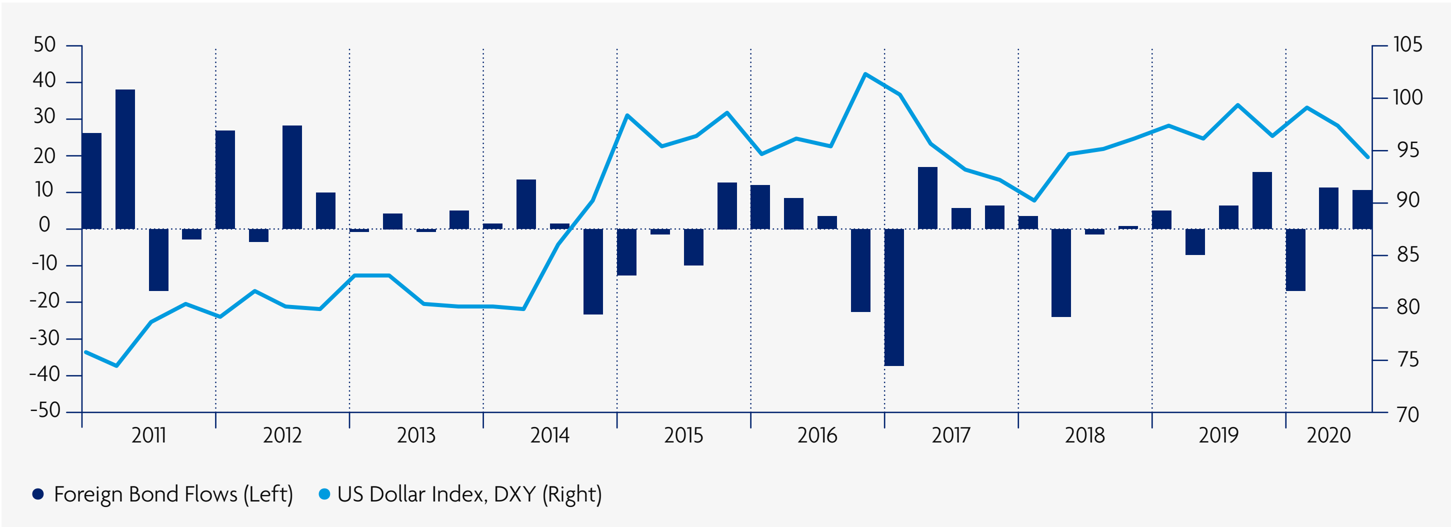
Fixed Income

Based on a weaker USD backdrop and the US Federal Reserve's (Fed's) easing policy stance, the Malaysian bond market could continue to benefit from its relatively more attractive 10-year yield of 2.76% (Figure R2) compared with the developed markets, Singapore's 0.87% and Thailand's 1.31%. However, Malaysia has been on the FTSE Russell watch list for possible exclusion from its World Government Bond Index since March 2019, posing a key risk.

Currency

Broad USD weakness following a shift in the Fed's policy approach, coupled with a firmer CNY and stable oil prices, should provide underlying support to the MYR. It is expected to strengthen to 4.03 against the USD by Q1 2021, and to 3.95 by Q3 2021.

Figure R2. A weaker USD will continue to attract more foreign inflows into Malaysian bonds.



Source: Macrobond, UOB Global Economics & Markets Research

Thailand

Thailand has been cited as a success story in containing COVID-19, yet the economy continues to suffer from limited international tourist arrivals, weak global trade and a plunge in private investment. The sizable government stimulus package to support both households and businesses will likely result in some sectors rebounding in the latter part of 2021, with others expected to take a bit longer.

Key growth drivers of trade and tourism still face headwinds from COVID-19

After an estimated domestic economic contraction of 7.8% in 2020, we forecast an expansion of 6.0% in 2021, higher than the Bank of Thailand's (BOT) forecast of 3.6% (Figure R3). The recovery is slower than previously thought, mainly due to declining Thai merchandise exports and a sharp decline in tourism receipts. Although Thailand had relative success in managing the pandemic, foreign tourism earnings are down significantly. On a brighter note, government spending should soften any further downturn.

Headline inflation is likely to gradually rise in 2021 but stay close to the lower band of the BOT's target range.

Equities

The current headwinds for the equity market mostly stem from tight valuations and the slower-than-expected domestic recovery. But with consensus for forecasted earnings growth in Thailand expected to see a rebound in 2021, the benchmark Stock Exchange of Thailand (SET index) will likely trade between 1,100 and 1,450. We favour a balanced mix between defensive sectors, such as Utilities, Infrastructure and Telecommunication companies, and sectors that benefit from a post-vaccine return-to-normal, such as Tourism, Healthcare and Transportation.

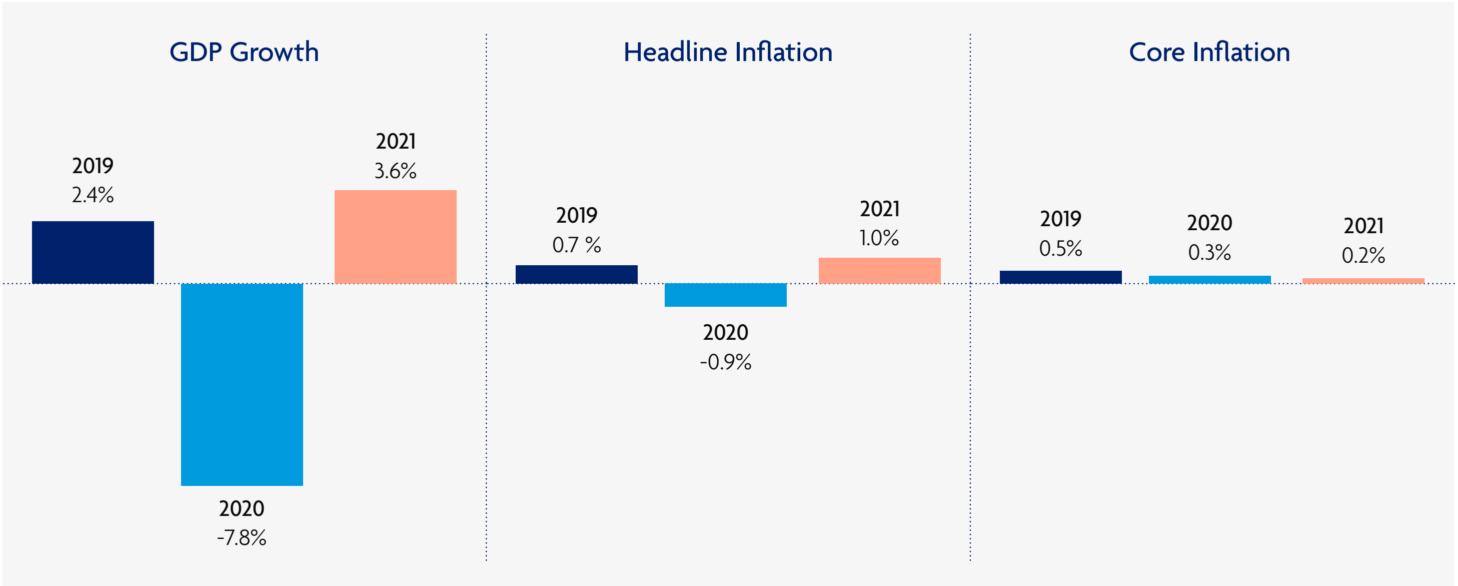
Fixed Income

As the US Federal Reserve continues to keep monetary policy loose for an extended period, we expect the Bank of Thailand (BOT) to stay firm on its policies. This widens the Thai-US rate differential, which in turn attracts more capital inflows and pushes down Thai bond yields.

Currency

We forecast the Thai Baht (THB) to maintain at around 30.5 against the USD in Q3 2021. This reflects internal challenges related to lower tourism-related revenue, declining Thai merchandise exports and the current account being revised downwards. External pressures have come from a second COVID-19 wave and continued US-China trade tension.

Figure R3. Thailand's economy is expected to recover this year, with headline inflation gradually rising.



Source: Bank of Thailand

Indonesia

Indonesia's economic growth is expected to rebound in a more meaningful way in 2021 after a relatively mild contraction in 2020. This is in part due to expansionary fiscal policy that is expected to continue for the foreseeable future.

An optimistic outlook for 2021 following supportive fiscal stimulus

After an economic contraction of -1.5% in 2020, the country's first since the Asian Financial Crisis, we are cautiously optimistic for growth of 4.3% in 2021. This recovery will be based on businesses and individuals adapting better to COVID-19, plus expectations of a vaccine next year. Greater mobility also has the potential to boost non-essential consumption, such as restaurant dining, clothing and apparel and entertainment, amid pent-up demand largely supported by Indonesia's young and increasingly middle-income population.

With continued expansionary fiscal policy in 2021, based on a government target of 5.7% of GDP, the key focus will be towards spending on infrastructure and social safety aid. As of 2019, around 90 out of 245 National Strategic Projects (NSP) had been completed, with the remainder expected in 2021 (Figure R4); after being deferred in 2020 due to COVID-19. The prospect for the pace of economic activity to increase should also lead to higher employment and a general positive outlook for the economy going forward.

Equities

The Jakarta Composite Index is expected to grow by 8.0% to 9.0% in 2021, in line with expectations of a COVID-19 vaccine to restore mobility. We favour Financials, Consumer Goods and Infrastructure in 2021 – the first two being defensive sectors with resilient characteristics, while the latter should prosper from the government refocusing on development after forced delays in 2020.

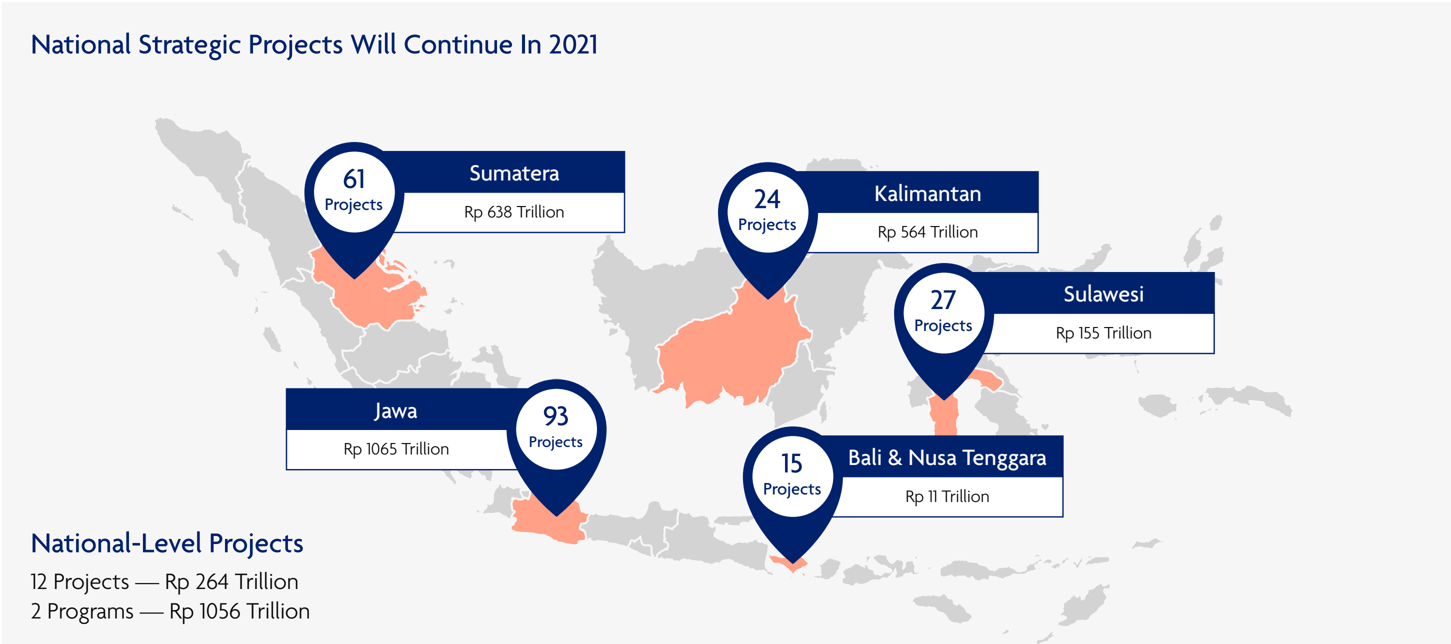
Fixed Income

The combination of negative global yields and low inflation will likely result in yields on domestic government bonds drifting lower. Bank Indonesia (BI) is also projected to slash the benchmark rate a further 25 basis points in 1Q 2021, bringing the seven-day reverse repo rate down to 3.5% by Q1 2021.

Currency

After remaining subdued, we expect the Indonesian Rupiah (IDR) to weaken to 14,300 against the USD by Q1 2021 and 14,400 by Q3 2021, even as low rates might induce capital inflows in conjunction with economic recovery.

Figure R4. Continued government spending on infrastructure will increase the pace of economic activity in 2021.



Source: The Committee for Acceleration of Priority Infrastructure Delivery (KPPIP), UOB Global Economics & Markets Research

China's economy has recovered from COVID-19 quicker than its neighbours, benefitting from a combination of decisive actions to deal with the disease, easing monetary and fiscal measures by the Central Bank and government support. These measures are further boosted by widening interest rate differentials and further financial market liberalisation, which will likely help domestic assets become more attractive to investors.

The CNY is expected to strengthen to 6.35 against the USD moving forward.

China's rapidly recovering economy will lead regional post-pandemic growth

China's economy has taken the lead in recovering from the impact of COVID-19 (Figure R5) and is expected to grow by 8.2% in 2021. Retail sales have shown continuous improvement, with both the manufacturing and service sectors returning to expansionary levels.

Monetary and fiscal policy will remain relatively accommodative, providing support to the economy. However, the People's Bank of China (PBOC) prefers to provide liquidity through structured monetary policy tools such as open market operations instead of broad interest rate cuts. In addition, credit easing will allow companies to access much-needed loans.

At the same time, the economic "dual circulation" policy is expected to be vigorously implemented to drive both domestic growth and external trade. This will further boost domestic consumption, thus helping China's economy to better withstand uncertainty over external demand as a result of the pandemic.

Differentials in economic recovery and widening interest rates compared with developed markets, combined with ongoing financial market reforms, will make Chinese assets more attractive. However, geopolitical risks, such as the continued friction between China and the US, may cause some market volatility.

Equities

Corporate earnings will gradually improve and are expected to grow by 18% in 2021. Relatively cheap valuations are still attracting foreign and domestic investors. A low interest rate environment and controls over the property market have led to inflows into stocks. We expect this trend will continue. Ongoing financial reforms and greater accessibility of China's financial markets to foreign investors also add to the stock market's appeal. New-economy sectors such as 5G and Clean Energy are expected to do well in 2021, while the Healthcare and Consumer Staples sectors may face selling pressure in the near-term due to their strong performance in 2020.

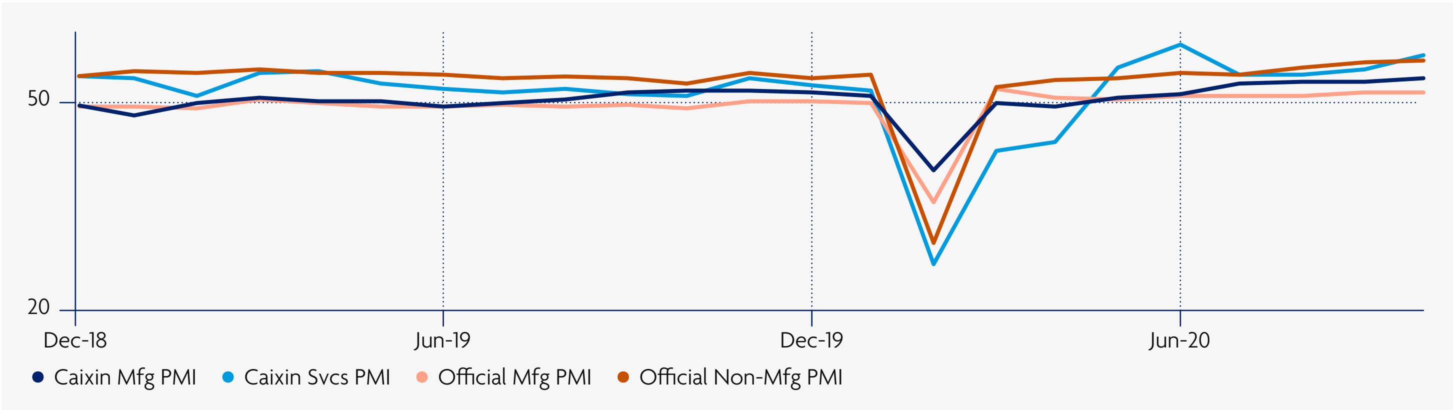
Fixed Income

Expectations of an economic recovery have pushed interest rates up from their lows, putting pressure on the fixed income market. Credit selection and a focus on short- and medium-duration bonds are important to counter the potential risk of widening spreads.

Currency

Widening interest rate differentials between the US and China, plus a strong Chinese economic rebound, have led to continued capital inflows into CNY. These factors have led to the CNY strengthening against the USD. We expect the CNY to appreciate to 6.45 against the USD by Q2 2021, and to 6.35 by Q3 2021.

Figure R5. Chinese sentiment has picked up significantly and has returned to expansionary levels.



Source: Bloomberg

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