UOB HOUSE VIEW

3Q2022

GLOBAL MACRO

With the Fed accelerating its rate hike cycle, more central banks including those in Asia are following suit as inflationary pressures globally are putting policymakers in a bind. Various factors have held back some Asian economies from normalizing monetary policies but it will be increasingly challenging for central banks in the region to keep to their accommodative stance as the Fed accelerates its pace of tightening, thus widening the rate differentials to detrimental effects.

ASSET ALLOCATION

The shift in asset allocation for 3Q reflects a less favorable policy mix of rising prices, tighter monetary policy and slowing growth. Given the cyclical dynamics, we shifted to an overweight in fixed income in 3Q, while the allocation for equities has been maintained at neutral but the regional allocation is tilted more towards Asia. We are neutral on commodities and alternatives and underweight on cash in the third quarter.

EQUITIES

Under the current monetary tightening environment, we expect equities to trade in a volatile fashion over the next 6 to 12 months, with modest gains on average. Equity markets will struggle to sustain gains until recession concerns ebb on the back of a less hawkish Fed when US/global inflationary pressures peak. With valuations reset lower, the outlook for equities will largely hinge on the performance of earnings.

FIXED INCOME

Fixed income should return a focus on quality with the anticipated move by the Fed to restrain the economy. However, as front-end rates have priced in an aggressive Fed, all-in yield for intermediate maturity investment grade credits are now relatively attractive. The Fed will likely hike and flatten the yield curve which suggest relative less upside risk on long end rates.

COMMODITIES

Supporting the on-going strength in crude oil price is a whole series of supply issues. We raise our Brent crude oil forecast further to USD 130 / bbl for 3Q, 4Q22 and USD 120 / bbl for 1Q, 2Q23 and continue to warn of elevated volatility with risks tilted to the upside. As for gold, we note that there are near term headwinds against gold due to the stronger USD. As such, we trim our positive forecast for gold to USD 1,900 / oz for 3Q, 4Q22 and USD 2,100 / oz for 1Q, 2Q23.

FX & INTEREST RATES

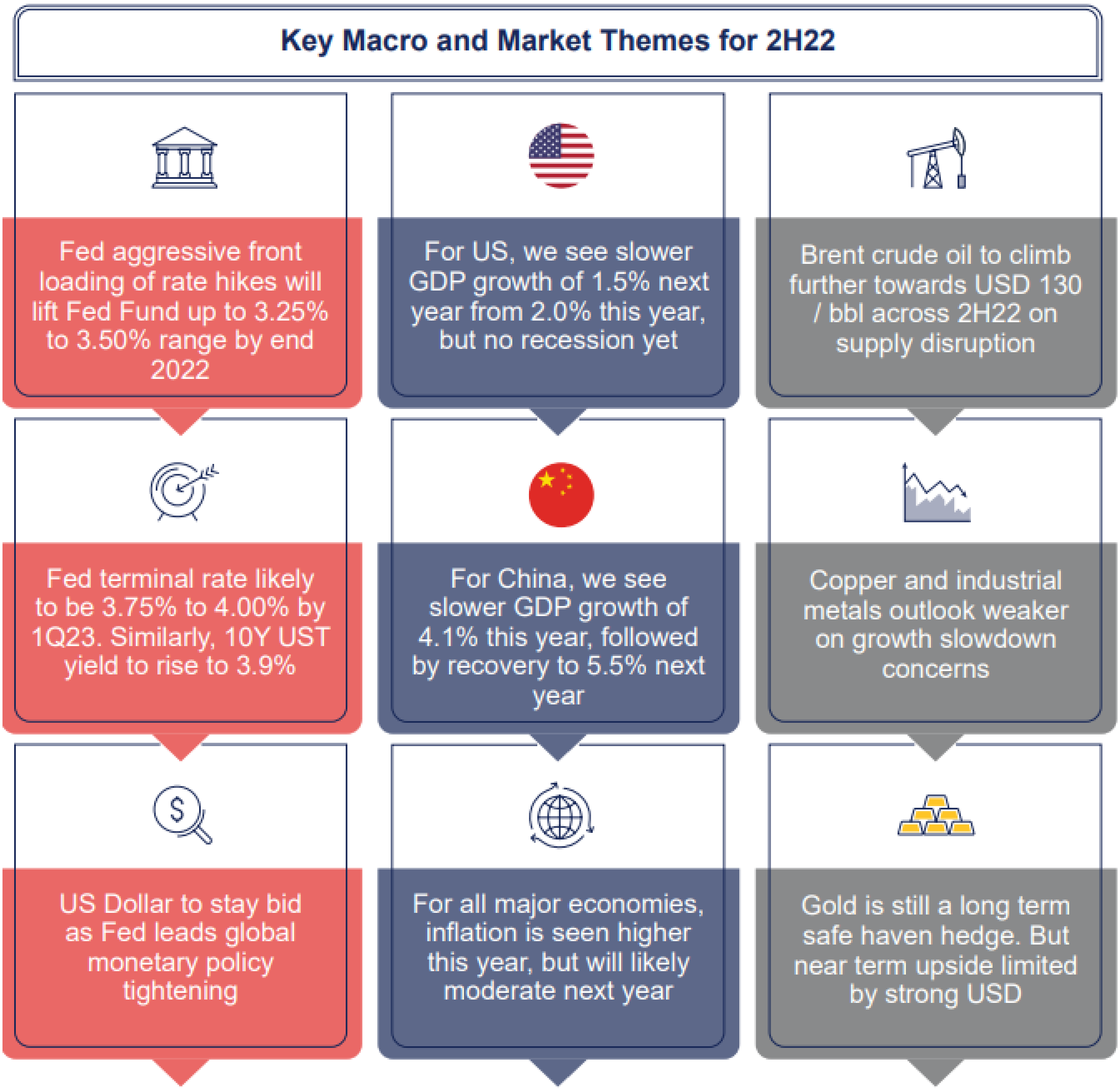
The Fed has lived up to the conviction to front-load its monetary tightening considerably in a bid to tame its soaring inflation. This has helped to underpin the USD strength, together with a slew of global growth downgrades which accentuated the safe haven appeal of the USD. On the back of our higher Fed Funds Target Rate (FFTR) forecast update, we have also recalibrated our yield expectations for the rest of the curve higher. We now see 10Y UST and SGS at 3.80% and 3.40% respectively at the end of 2022.

UOB

GLOBAL MACRO & MARKETS STRATEGY

A Volatile And Rocky 2H22 As Fed Hikes Aggressively
"*We are not trying to induce a recession now. Let's be clear about that*." Fed Chair Jerome Powell, replying to a reporter's question at the post FOMC press conference on 15 Jun 2022, after the Fed hiked by 75 bps.

It has been a rather volatile and tumultuous past quarter for global markets where key asset classes were sold off aggressively across the board as global central banks and investors alike play catch up with further unwelcomed steep rise in inflation. There appears to be nowhere to hide as the recession / stagflation vs runaway inflation debate picked up intensity. Needless to say, it is easy to get carried away by the fear of this potential sharp rise in interest rates in the months ahead. However, there are several key takeaways to watch out for as objective goal posts for the economy and markets for the remaining months of the year.



US Federal Reserve To Lift Fed Fund Rates Up To As High As 4% By 1Q23: In terms of monetary policy, the US Federal Reserve (Fed) has led the race by global central banks to hike rates and tighten liquidity. The Fed in an attempt to contain the runaway inflation narrative, further ramped up their aggressive front loading with a 75 bps rate hike at the recently concluded Jun FOMC and reinforced widespread fears that they will continue to hike aggressively to potentially 3.25% to 3.50% range by end of this year. Overall, we now see Federal Funds Target Rate (FFTR) rising to an eventual terminal rate of 3.75% to 4.00% range by 1Q23. Similarly, we see 10-year US Treasuries yield rising to 3.9% by 1Q23. Kindly refer to Central Bank Policy Focus: When The Fed Aggressively Hikes, How High Can The Asian Central Banks Go? for more details of our updated Fed hiking trajectory outlook.

This front loading of aggressive rate hikes is seen across key central banks as well. Specifically, the European Central Bank (ECB) is expected to finally start hiking in Jul and lift rates above negative in Sep to about 1.00% or higher by 1Q23. Both the Bank of England (BoE) and Reserve Bank of Australia (RBA) are also expected to hike to 2.25% by 1Q23 as well. The odd one out in the

G7 space remains that of the Bank of Japan (BoJ) with Governor Kuroda stubbornly sticking to easy monetary policy and fighting to keep 10-year Japanese Government Bond (JGB) yields glued to an unrealistic 25 bps amidst the race higher in global benchmark yields.

Global Growth To Slow Down Further As Runaway Inflation Starts To Bite: With respect to the macroeconomy, there is widespread and elevated fears of recession or stagflation amidst further rise in inflation. This is especially so when previous high-flying parts of the US economy, particularly in the tech and crypto industry have started to announce widespread job cuts. Needless to say, our updated quarterly forecasts call for slower growth and higher inflation in the major economies that we cover.

However, it is important to note the following key points. Specific to the US economy, while we see growth slowdown to 1.5% next year, from 2.0% this year, we do not yet see a widespread recession on the horizon although the risk of a 2023 recession has risen in tandem with the overtly hawkish shift of Fed tightening. For China, while we see minimal growth of 1.0% for 2Q this year, growth is expected to recover from 4.1% this year back up to 5.5% next year. In addition, while our updated forecasts all call for higher inflation this year, our macroeconomic team do see inflation moderating next year.

FX STRATEGY - Don't Fight The Fed And The USD: While it is a less clear-cut case to be a USD bull compared to three months ago as more Major central banks joined in the global tightening bandwagon and is catching up on the Fed's rate hike momentum, the key drivers of USD strength remain intact. The strong US labour market and above-trend US GDP growth gave the Fed the conviction to front-load its monetary tightening considerably in a bid to tame its soaring inflation. So far, the Fed has lived up to its credibility and delivered the markets' expectation of rate hikes. This has helped to underpin the USD strength, together with a slew of global growth downgrades which accentuated the safe haven appeal of the USD. Overall, within the Major FX space, we continue to be bullish USD against the EUR and JPY which will keep the DXY tethered near recent highs. Specific to the EUR, the threat of Eurozone fragmentation where the effects of ECB's tightening aren't felt the same way across the Eurozone may overtake rate differential as the key driver of EUR/USD in the near term which is likely to skew the currency to the downside in the near term. For now, we expect further weakness of EUR/USD towards 1.03 by year end before a rebound next year to 1.06 by 2Q23. While both AUD and GBP have weakened anew over the past quarter, we maintain our modest constructive outlook on both currencies against the USD.

Weighed by the dual headwinds of an aggressive Fed rate hike cycle and a slowing Chinese economy, the Asia Dollar Index (ADXY) fell for a second straight quarter in 2Q22 and is on track for the worst performing quarter in four years. The CNY led losses within the region, falling as much as 7.5% with the quarter to 6.81/USD in May as the 2-month Shanghai lockdown exacerbated growth concerns. The abrupt weakness in the CNY also triggered a repricing in some of the more resilient Asia FX such as the MYR and IDR. Both currencies weakened to 2020's lows against the USD even as fundamentals remain sound. With Fed pressing on with its front-loaded rate hikes in 2H22, the selloff in Asia FX is far from over. A repeat of the 2018 playbook could see Asia FX subject to portfolio outflows as the Fed hike rates and conduct QT at the same time. Furthermore, concerns about a China slowdown and rising global recession risks will also keep the pressure on Asia FX. We stay negative on Asia FX and downgrade our various forecasts particularly for CNY and SGD further to 6.90 and 1.41 respectively against the USD by 1Q23. Kindly refer to our latest 3Q 2022 FX Strategy for more details of our currencies outlook.

RATES STRATEGY - Inflation Proving To Be A Formidable Opponent: The US Fed delivered on market expectations with a 75bps hike to the Fed Funds Target Rate (FFTR) in June. Guidance for July's FOMC is that another 75bps remains on the table, which is a reversal of Chairman's Powell's previous stance that 75bps wasn't being actively considered. The updated June Dot plot was shifted higher, and the gap between peak FFTR and long-term neutral FFTR was widened. The updated Dot plot more clearly aligns with the FOMC members' narrative of expeditiously tightening above neutral. On the back of our US macro team's FFTR forecast update, we have also recalibrated our yield expectations for the rest of the curve higher. Overall, we now see 10Y UST and SGS at 3.80% and 3.40% respectively at the end of 2022. Bond yield gains should begin to taper off into 2023 alongside the peak in monetary policy tightening. We have 3M compounded SOFR and SORA at 2.99% and 2.30% respectively for 4Q 22.

Specific to Singapore, if the next couple of core inflation prints were to run hot, we expect that the market narrative will increasingly be focused on the key question of whether the next tightening move by MAS will materialize in October's semi-annual meeting or come in the form of yet another off-cycle move on top of the one that took place in January this year. Two off-cycle moves by MAS in a year will be unprecedented, but no more unprecedented than the outsized monetary policy actions undertaken by a host of major developed market central banks this year. Overall, inflation outcomes in 2Q have increased the possibility of further tightening by MAS this year. If inflation print continues to come in hot over the next couple of months, we think that this will also raise the possibility of another off-cycle tightening move by MAS. Kindly refer to our latest 3Q 2022 Rates Strategy for more details of our rates outlook.

COMMODITIES STRATEGY - Brent Crude Oil Continues Strong Rally As Supply Crunch Persists: Supporting the on-going strength in crude oil price is a whole series of supply issues. Russian crude oil supply has now been effectively taken off the "mainstream" energy market and will remain so now that the European Union has decided to ban seaborne Russian crude. In addition, OPEC does not seem to be in a hurry at all to step into the supply vacuum. While OPEC has raised its monthly production modestly, Saudi Arabia has negated the move by also hiking immediately thereafter by a large amount its Official Selling Price (OSP) for its crude oil shipments. As a result, global crude oil supply remains tight with clear evidence that inventory levels continue to drop. Therefore, Brent crude oil remains in strong backwardation with the crack spread rallying further to a new historic high. These are indicative of strong price support at current level. Hence, we raise our Brent crude oil forecast further to USD 130 / bbl for 3Q, 4Q22 and USD 120 / bbl for 1Q, 2Q23 and continue to warn of elevated volatility with risks tilted to the upside.

Gold has had a difficult past quarter, with various attempts to rally limited by the strong USD strength. This is especially so when the Fed further ramped up its rate hiking cycle with an outsized 75 bps hike at the recently concluded June FOMC. Overall, we stay positive on gold due to on-going strong safe haven demand. Positioning in global gold ETFs remain strong as well. Possible loosening of Covid-19 distancing measures across China may also lead to higher physical gold jewellery demand in 2H22.

However, we note that there are near term headwinds against gold due to the stronger USD. As such, we trim our positive forecast for gold to USD 1,900 / oz for 3Q, 4Q22 and USD 2,100 / oz for 1Q, 2Q23.

LME Copper experienced some weakness, pulling back to the USD 9,500 / MT level. This retreat in LME Copper price makes perfect sense given the on-going Covid-19 related social distancing measures and lockdowns in key cities across China that resulted in a temporary shutdown in manufacturing activity. In fact, given the sharp correction in some macroeconomic indicators like industrial production across the month of April, the witnessed correction in LME Copper price can be said as mild. Despite the slowdown in industrial activity in China across 2Q22, one of the key supportive factors for LME Copper is the on-going tightness in inventory. This is a similar supportive factor for many commodities across 2Q22 as well. Overall, in line with the increasing challenges to global economic growth, we now turn cautious in our outlook for LME Copper and forecast USD 9,000 / MT in 3Q, 4Q22, followed by USD 8,500 / MT in 1Q, 2Q23. Kindly refer to our latest 3Q 2022 Commodities Strategy for more details of our crude oil, copper and gold outlook.

Rising Credit Risk Is Now A Growing Concern As Rate Hikes Start To Bite: Previously, during the onset of Covid-19 in the early months of 2020, the global economy was spared widespread credit default as every government stepped up fiscal support of their respective economies. It is no longer realistic to expect such fiscal support going forward as key economies (with the exception of China) have reopened their borders and removed the Covid-19 related distancing measures. As such, there is now a growing and widening credit risk as the weaker parts of the economy is unable to adjust to the sharp rise in interest rates from zero just as recently as a year ago.

There are two key related credit spreads that are worth watching. First is the credit spread between high yield and investment grade benchmarks in the US. Second is the spread between Italian and German Bund 10-year benchmarks. The former credit spread is a proxy of the health of non-investment grade in the US and its further rise bears closer scrutiny for potential default risk in weaker industry sectors. While the latter spread is strictly a yield spread, it is a key proxy of debt issues in Italy and fragmentation risks in the Eurozone. Overall, there has been a clear rise in both spreads, although both have yet to surpass the high last seen in 1Q20 during the onset of Covid-19. Along with the stagflation/recession risks mentioned earlier, this is yet another space that warrants close monitoring, as funding costs rise in tandem with central banks' continuing policy tightening spree in 2H of this year.

ASSET ALLOCATION

The shift in asset allocation for the third quarter reflects a less favorable policy mix of rising prices, tighter monetary policy and slowing growth. Despite these headwinds, real consumer spending has held up well and corporate profit margins stayed resilient. However, as the Fed continues to tilt its forward guidance towards more restraint until evidence of inflation moving close to its 2% target while growth outlook deteriorates, the balance of risk for risky assets is to the downside.

While fundamental developments are self-evidently negative, there remains pockets of opportunities. China is recovering from its self-imposed "zero-COVID" policy, the fallout of its deleveraging campaign in the real estate sector and a regulatory crackdown of the internet sector. With depressed valuations and light investor positioning, a vigorous rebound from the March lows even as incremental news-flow turns positive. Asian equities and emerging markets in general have also outperformed developed markets to date.

Given the cyclical dynamics, the asset allocation into the third quarter has shifted to an overweight in fixed income. The repricing of fixed income yields has resulted in a sharp correction in bond prices to date. As growth prospects in the developed world continue to deteriorate in the coming months and with a hawkish Fed dot-plot been duly discounted in front end rates, intermediate duration high quality fixed income would be appropriate. Into a potential recession (in 2023), fixed income can also be an effective portfolio stabilizer as rates eventually peak. Allocation to high yield should be more prudent and selective as a downturn usually lead to a repricing of credit spreads.

Our allocation to equities has been maintained at neutral but the regional allocation is tilted more towards Asia given more favorable output gap and tailwind from pandemic reopening. In China, the policy cycle has decidedly turned for the better while valuations are close to historic lows.

Finally, on alternatives, preferences should be tilted towards non-directional 3rd party hedge funds over base metals. The recent price weakness in Gold could ease as both real rates and the US dollar have moved higher given the Fed's agenda.

Global Asset Allocation For 3Q 2022

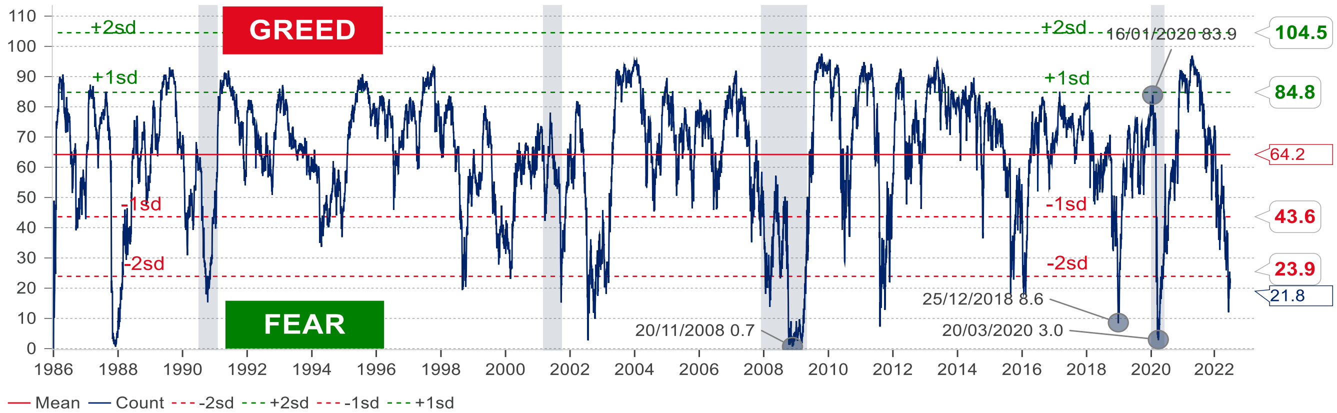
	Underweight	Neutral	Overweight
Equities		•	
Fixed Income			•
Commodities		•	
Alternatives (hedged strategies)		•	
Cash	•		

EQUITIES

Under the current monetary tightening environment, we expect equities to trade in a volatile fashion over the next 6 to 12 months, with modest gains on average. Equity markets will struggle to sustain gains until recession concerns ebb on the back of a less hawkish Fed when US/global inflationary pressures peak.

For now, oversold technical conditions (example given in the S&P 500 below) and light investor positioning imply that equities do have some potential upside.

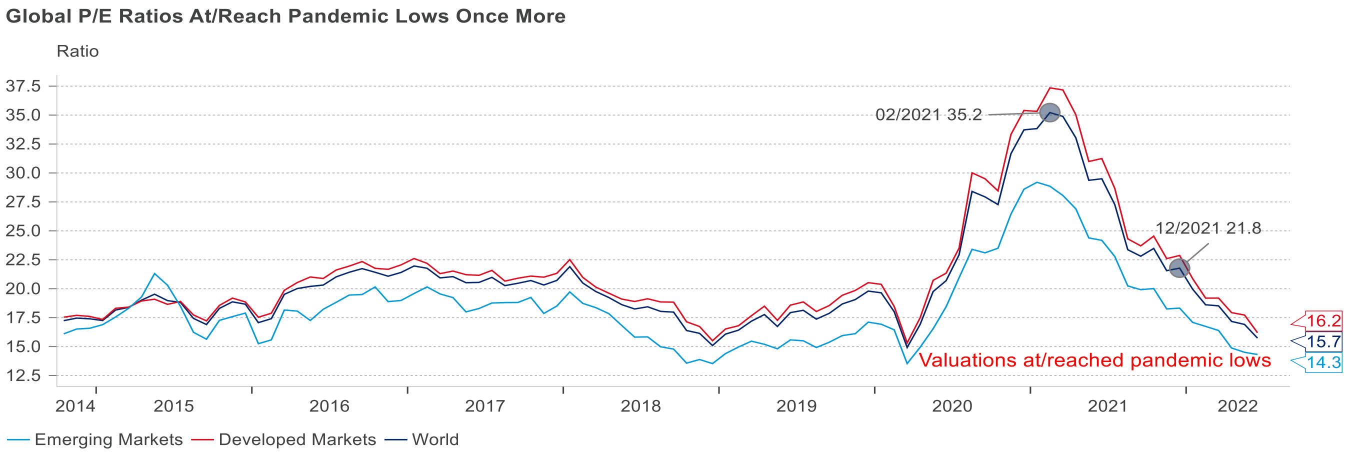
% Share of S&P 500 Members With Price > 200dma Reaching Levels During Start Of COVID-19 Pandemic



Source: Macrobond, UOB Private Bank

From a P/E angle, valuations have corrected significantly from their earlier highs, with the Factset World Index P/E multiple declining to 15.7 from 21.8 in Dec 2021 and a peak of 35.2 in Feb 2021, showing that most of the valuation excesses of recent years have been unwound. As such, there is the potential for stocks to rebound, led by non-US equities, should global economic growth conditions remain resilient, and assuming interest rate expectations and bond yields calm in 2H2022.

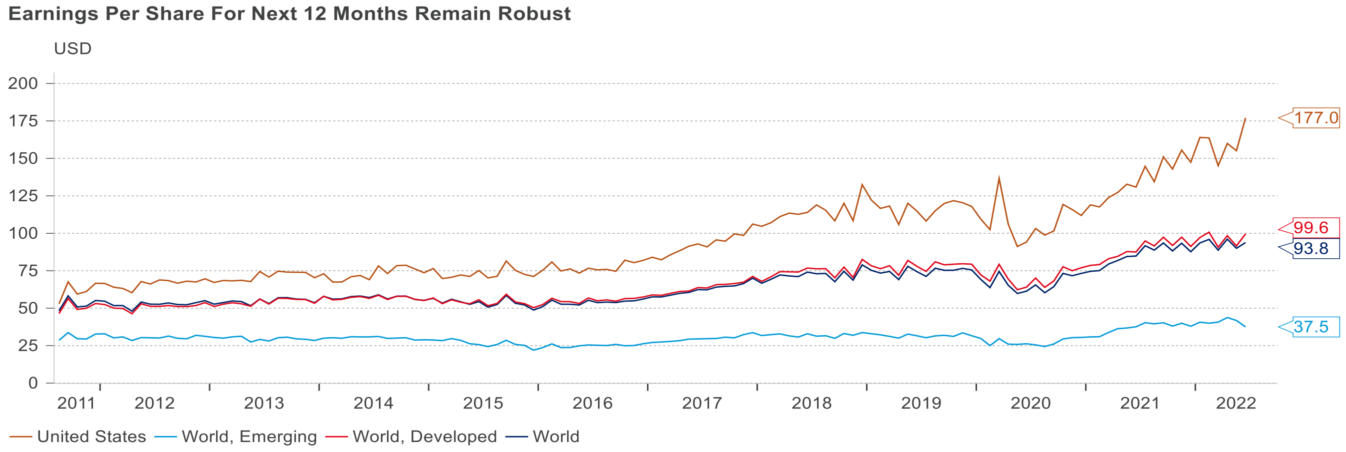
Global P/E Ratios At/Reach Pandemic Lows Once More



Source: Macrobond, UOB Private Bank

With valuations reset lower, the outlook for equities will largely hinge on the performance of earnings. Corporate profits in most markets remain resilient. The 12-month forward earnings for across developed and emerging equity benchmarks remain in an uptrend. More importantly, the US continues to be a standout performer, with underlying forward earnings at a new high. While there were some notable disappointments during the recently completed Q1 earnings reporting season, overall results were solid, with most US companies beating bottom-line expectations.

Earnings Per Share For The Next 12 Months Remain Robust



Source: Macrobond, UOB Private Bank

Given the increased uncertainty about the global economic growth outlook, ongoing supply chain issues, and cautious corporate commentary and guidance, downgrades to global earnings estimates are possible in the months ahead.

This also means that year-on-year earnings growth will slow, consistent with a moderation in global economic growth momentum. As growth decelerates and some profit downgrades play out, investors could become more nervous about the earnings outlook, especially given the elevated nature of profit margins, thus resulting in additional selling pressure on equities. These dynamics underpin our view that equity performance will remain choppy before stocks find a durable bottom.

We continue to favour a moderate pro-growth investment stance, with overweight in EM equities, particularly China, from the expected policy divergence with the developed markets. Mild reflationary macro policies and reduced regulatory pressures on internet-platform companies as the National Party Congress approaches in November will likely be supportive of Chinese risk assets.

Elevated relative valuations in US equities keep us neutral on a 6-12 month horizon. At the sector level, we favour financials, industrials, materials, and energy. Financial earnings are still poised to outperform over the coming year as central bank rate hikes and expanding loan balances lift bank net interest incomes, and credit quality is supported by the healthy corporate profit environment and low unemployment. Meanwhile, even as global economic growth momentum slows, we expect the industrial sector's relative earnings to surprise to the upside given the large order backlogs for capital equipment, increases in defense spending, and improving demand for commercial aircraft as air travel normalizes. Selectively, there are opportunities in the growth space as some of the big tech names have been sold off together with negative market sentiments.

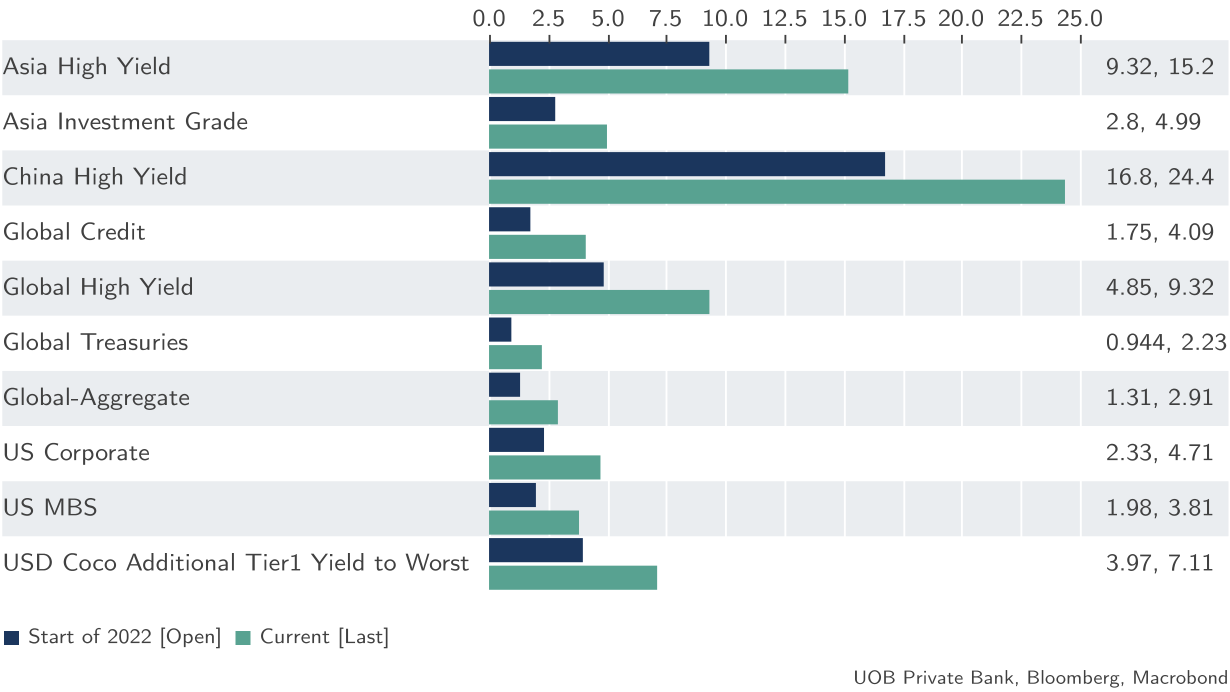
FIXED INCOME

Fixed income should return a focus on quality with the anticipated move by the Fed to restrain the economy. Presently, US investment grade fundamentals have measured up well with ratings upgrades outpacing downgrades. Credit spreads have widened to 150bp, while fair, has yet to price in a recession. However, as front-end rates have priced in an aggressive Fed, all-in yield for intermediate maturity investment grade credits are now relatively attractive. The Fed will likely hike and flatten the yield curve which suggest relative less upside risk on long end rates.

The fundamental picture in US high yield is not too different. In fact, credit metrics have shown resilience including leverage, interest-cover. Overall upgrade to downgrade supported the same view. However, as high yield spreads widen into growth slowdowns and as a key driver of total return, high yield bond prices will invariably be more volatile. Overall, we retain a cautious stance.

The picture in Asia shows a mixed picture with investment-grade staying resilient with a year to date widening of 45bp or so. High yield bore the brunt of the sell-off given the sector-wide liquidity crisis in the privately owned China real-estate issuers. The Asia high yield blended spread has widened to 1050bp, more than the during the 2008 Global Financial Crisis. With the sector stuck in a stalemate, aggravated by rolling COVID lockdowns and a hesitant state policy, much of the sector is priced at distressed levels. Survivors are likely to be limited to State-Owned-Enterprises (SOEs) or a handful of some of the strongest names in the industry. Hence, investors are advised to be highly selective.

Yields Changes Since Start Of 2022



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FX, INTEREST RATE & COMMODITIES FORECASTS

FX	16 Jun 22	3Q22F	4Q22F	1Q23F	2Q23F
USD/JPY	133	134	135	136	136
EUR/USD	1.05	1.04	1.03	1.05	1.06
GBP/USD	1.23	1.25	1.26	1.28	1.30
AUD/USD	0.70	0.71	0.72	0.73	0.74
NZD/USD	0.63	0.65	0.66	0.67	0.68
DXY	104.04	104.4	104.8	103.3	102.5
USD/CNY	6.70	6.80	6.85	6.90	6.90
USD/HKD	7.85	7.85	7.85	7.85	7.85
USD/TWD	29.73	30.0	30.2	30.4	30.5
USD/KRW	1,289	1,300	1,310	1,320	1,330
USD/PHP	53.44	54.0	54.5	55.0	55.0
USD/MYR	4.40	4.46	4.48	4.50	4.52
USD/IDR	14,768	15,000	15,100	15,100	15,200
USD/THB	35.15	35.4	35.8	36.2	36.2
USD/VND	23,200	23,400	23,500	23,550	23,600
USD/INR	78.08	79.0	80.0	80.5	81.0
USD/SGD	1.38	1.40	1.41	1.41	1.41
EUR/SGD	1.46	1.46	1.45	1.48	1.49
GBP/SGD	1.71	1.75	1.78	1.80	1.83
AUD/SGD	0.97	0.99	1.02	1.03	1.04
SGD/MYR	3.17	3.19	3.18	3.19	3.21
SGD/CNY	4.84	4.86	4.86	4.89	4.89
JPY/SGDx100	1.04	1.04	1.04	1.04	1.04

RATES	16 Jun 22	3Q22F	4Q22F	1Q23F	2Q23F
US Fed Fund Rates (Upper Bound)	1.75	2.75	3.50	4.00	4.00
USD SOFR	0.51	2.05	2.99	3.64	3.91
USD 3M LIBOR	2.03	3.00	3.65	4.10	4.10
US 10Y Treasuries Yield	3.26	3.60	3.80	3.90	3.90
JPY Policy Rate	-0.10	-0.10	-0.10	-0.10	-0.10
EUR Refinancing Rate	0.00	0.75	0.75	1.00	1.00
GBP Repo Rate	1.25	1.75	2.25	2.25	2.25
AUD Official Cash Rate	0.85	1.25	1.75	2.25	2.25
NZD Official Cash Rate	2.00	2.50	3.00	3.50	3.50
CNY 1Y Loan Prime Rate	3.70	3.55	3.55	3.55	3.65
HKD Base Rate	2.00	3.00	3.75	4.25	4.25
TWD Official Discount Rate	1.50	1.63	1.75	1.88	1.88
KRW Base Rate	1.75	2.25	2.50	2.50	2.50
PHP O/N Reverse Repo	2.25	3.00	3.50	3.75	4.00
SGD SORA	0.61	1.53	2.29	2.78	2.96
SGD 3M SIBOR	1.56	2.15	2.75	3.10	3.10
SGD 3M SOR	1.77	2.20	2.75	3.10	3.10
SGD 10Y SGS	3.11	3.30	3.40	3.50	3.50
MYR O/N Policy Rate	2.00	2.50	2.50	2.75	3.00
IDR 7D Reverse Repo	3.50	4.00	4.50	4.75	5.00
THB 1D Repo	0.50	0.50	0.75	1.00	1.00
VND Refinancing Rate	4.00	4.00	4.00	4.00	4.25
INR Repo Rate	4.90	5.65	5.65	5.65	5.65

COMMODITIES	16 Jun 22	3Q22F	4Q22F	1Q23F	2Q23F
Gold (USD/oz)	1,845	1,900	2,000	2,100	2,100
Brent Crude Oil (USD/bbl)	119	130	130	120	120
LME Copper (USD/mt)	9,075	9,000	9,000	8,500	8,500

THE TEAM

Global Economics & Markets Research
Private Bank

All chart data from Bloomberg unless otherwise specified.

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