UOB House View 2Q 2024

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Global Macro

Amidst the "bumpy" ride in inflation and the latest string of stronger-than-expected US macro figures like the Mar ISM, investors have started to question whether the Federal Reserve (Fed) is indeed able to start rate cuts in June and whether it will be able to deliver the three cuts this year as signaled by the latest Dot Plot. We keep to our existing forecast of 3 x 25 bps cuts from the Fed this year starting from Jun but the risk on balance is increasingly skewed towards lesser.

Asset Allocation

We have raised equities to Overweight in our asset allocation. As we expect market gains to broaden out, we recommend investors to diversify outside of the US mega-caps for better upside potential. Our bond allocation has shifted to Neutral but the relative shift from fixed income does not reflect a bearish view, instead should be seen as better short-term opportunities in selected sectors within equities. Cash remains an Underweight and allocation to alternatives remains an Overweight too.

Equities

Against a benign macro backdrop, we recommend an increase in the allocation to equities given falling inflation and supportive growth. We have increased allocation to emerging Asian equities, funded out of a reduction in the relative weight of US equities. We maintain an overweight on Japan's equities while Europe's equity exposure has been upgraded to neutral.

Fixed Income

For Developed Markets (DM), we remain Overweight on DM USD IG and stay Underweight on DM USD HY as credit spread compression between IG and HY and rising tail risks from an acceleration in defaults lead us to be cautious of the asymmetric risk-reward. We stay Overweight EM Asia IG and continue to advocate investors to buy on dip. We remain Neutral on EM Asia HY and emphasize selectivity and favor selected ASEAN infrastructure, Indonesian utility and property developers.

Commodities

The positive drivers for gold have not changed. There is specifically strong central bank allocation into gold. Thereafter, once the Fed does cut rates, investment demand for gold, possibly via ETFs will likely increase providing impetus for further gold strength. We take this opportunity to raise our positive gold forecast further to USD 2,300 / oz for 2Q24, USD 2,350 / oz for 3Q24, USD 2,400 / oz for 4Q24 and USD 2,450 / oz by 1Q25. Amidst rising geopolitical risk, Brent crude oil price has recovered strongly in the past month. We expect energy benchmark to trade higher to reflect rising geopolitical risk premium and we keep our positive Brent forecasts at USD 85 / bbl in 2Q24 & 3Q24 and rising to USD 90 / bbl in 4Q24 & 1Q25.

FX & Interest Rates

Overall, we maintain our view of a softer USD going forward with short term rates and longer-term yield easing in the months ahead as the Fed is projected to cut rates starting in Jun. We expect 3M compounded in arrears Sofr and 10Y US Treasuries yield lower to 4.73% and 3.70% respectively by 4Q24.

Right By You

Global Macro & Markets Strategy

Will the Fed be able to start rate cuts in June?

It has been a bumpy start to the year as we ended 1Q24. Top of the mind amongst many investors is the slowdown in China's economy. Adding to this challenging setting is the slowdown in Eurozone economy which narrowly averted a technical recession as Russia's invasion of Ukraine now enters its third year. Further clouding the global economic outlook is the increasing push back by the US Federal Reserve (Fed) to cut interest rates. While investor worries persist, in its latest quarterly World Economic Outlook (WEO) update, the IMF raised its global growth projection for this year by 0.2% point to 3.1% and noted reassuringly that "the risks to global growth are broadly balanced and a soft landing is a possibility". What are the risks and positives for the key economies as we enter 2Q24?

On China's outlook, economic activities picked up in the first two months of the year and the PMIs (Purchasing Managers Index) rebounded further in March with the official manufacturing PMI turning expansionary for the first time in six months. However, real estate market indicators remain negative and together with the high local government debt, continue to be a major drag on the recovery. Private consumption and employment outlook is still lackluster at this point, contributing to concerns of deflation. In Jan-Feb, the headline inflation was flat while core inflation averaged 0.8% y/y. Factoring in the expected easing of food price deflation in the coming months, we expect the headline inflation to average 1.0% in 2024 from 0.2% in 2023. We estimate China's 1Q24 GDP growth at 1.7% q/q SA, 4.9% y/y compared to 1.0% q/q, 5.2% y/y in 4Q23. Our full-year 2024 GDP growth forecast is at 4.5%.

It is no surprise that the PBOC intensified its monetary policy easing. After a 50 bps cut in financial institutions' Reserve Requirement Ratio (RRR) in early Feb, the PBOC followed up in late Feb with a larger-than-expected 25 bps cut in the 5Y Loan Prime Rate (LPR) in support of the government's overall push to stabilize the property sector. We still expect the PBOC to moderately increase monetary policy support this year with the 1Y LPR likely falling to 3.20% by end-4Q24 from 3.45% while the 5Y LPR may stay on hold at 3.95% through the rest of 2024. Officials also suggested room to cut banks' RRR further.

Beyond China, the Eurozone economy is not performing much better. The Eurozone may have narrowly averted a technical recession at the end of last year as 4Q23 GDP surprised with a flat showing after a 0.1% contraction in 3Q23. However, the stagnation in Eurozone economy continues into 1Q24, amid ongoing falls in output in Germany and France. Manufacturing PMIs in these key economies continued to experience deeper contractions in Mar.

Given the more pronounced economic slowdown in the Eurozone, and with inflation falling faster than expected, the ECB may well be more open to immediate rate cuts compared to the Fed. However, the ECB's hands are similarly tied as risks to inflation and concerns about services inflation remain to the upside. While ECB President Christine Lagarde opened the door to a rate cut in Jun, she was very cautious in saying that the ECB "needs more evidence, more data". We now expect the ECB to begin cutting rates in Jul, just after the Fed.

Compared to the economic challenges facing China and the near stagnation in growth for the Eurozone, there is one particular bright spot, i.e. ASEAN remains a global safe haven for economic growth. Our UOB macroeconomic team forecasts that growth for the ASEAN-6 countries climbing strongly from 3.7% last year to 4.6% this year. The region is poised to continue its consistent and steady growth path, supported by a recovering tourism sector, robust domestic spending, rebounding external trade sector and sturdy Foreign Direct Investments (FDI) into the region. Of late, there are some concerns over the on-going weakness in domestic currencies like the MYR and THB. It is likely that domestic currency weakness is exacerbated by a backdrop of USD strength. Nonetheless, we would expect ASEAN currencies to strengthen anew later this year once the Fed starts to cut interest rates.

As for US Fed outlook, crossing into the second quarter of 2024, while the main narrative is still that of a June start to rate cuts, some investors have begun to question whether this is indeed possible. Following the March FOMC and the latest monthly PCE update (whereby core PCE eased marginally to 2.8% y/y in Feb, 2.9% y/y in Jan), Fed Chair Powell did not fight the prevailing desire of a June cut. But he reiterated that he still needs "more good inflation readings" and explained that he continues to expect "inflation to come down on a sometimes bumpy path to 2%". This is the case for other Fed officials as well, with their latest comments continuing to signal patience and highlighting that there is no immediate urgency to cut rates.

Right By You

On top of the latest "sticky" inflation data, the recent growth and activity macroeconomic figures for the US have turned out to be stronger-than-expected as well. Specifically, US manufacturing ISM rose by a larger-than-expected amount, to 50.3 in Mar from 47.8 in Feb. In addition, the New Orders ISM component also rose strongly to 51.4 in Mar from 49.2 in Feb. Furthermore, the Prices Paid ISM component also gained momentum, to 55.8 in Mar from 52.5 in Feb. Concurrently, China's official manufacturing PMI bounced back above the 50.0 level, to a one year high of 50.8 in Mar, from 49.1 in Feb.

On one hand, these stronger PMI figures raised hopes that there is a nascent recovery in manufacturing for both US and China. On the other hand, the rebound in PMI figures suggested that US economy is on firmer footing than the prevailing "soft landing" narrative. Indeed, following the stronger-than-expected ISM figures, the swaps implied odds of a Jun start to rate cuts have been pared down to below 50. Another development that may "spoil" the Fed's start of rate cuts in June is the recent rebound in crude oil prices.

Our macroeconomic team is keeping to existing forecast of 3 x 25 bps cuts from the Fed this year starting from Jun. However, the macroeconomic team notes that given the abovementioned cumulation of stickier inflation amidst stronger growth outlook, the risk on balance is increasingly skewed towards fewer than 3 cuts for this year.

Subsequent inflation and labour market figures for the months of Apr and May will be critically important in terms of data dependency as to whether the Fed will indeed start rate cuts in Jun and will deliver three cuts in total. The upcoming FOMC on 30 Apr / 1 May is also shaping out to be of increasing importance to provide any final messaging or hints as to whether the Fed will indeed start its easing cycle at the subsequent 11/12 Jun FOMC.

Closer to home, domestic inflation trend amongst Singapore's key import partners (China, US, EU27, Malaysia and Taiwan) has softened since peaking in 3Q22 owing to the successive tightening of monetary policies in their respective economies (except China). In the case of China, weakness in its property sector continues to weigh on business and consumer sentiment, keeping a lid on demand-side inflationary pressures. Even with a possible "slight" slope reduction by the MAS in the Apr 2024 MPS, the non-zero (positive) slope of the S$NEER policy band will continue to facilitate an ongoing gradual appreciation of the S$NEER which helps to anchor the transmission of imported inflation into domestic prices.

However, the adjustment of Singapore's core inflation back to equilibrium could remain challenging in the quarters ahead given that domestic cost pressures (as proxied by unit labour and business costs) remain significantly above historical norms, albeit moderating. Overall, we assess that the door is open to MAS' policy normalization via a slight slope reduction (by 50bps) but we now ascribe a lower 30% probability for this to happen in Apr. Therefore, we have shifted our base case for the commencement of policy normalization to the Jul 2024 MPS (70% probability) in light of the still elevated domestic cost pressures and further evidence that core inflation is receding nearer to equilibrium.

FX Strategy: Heading into a pivotal quarter for the USD

The USD finished 1Q24 on a positive note, with the US Dollar Index (DXY) gaining 3.1% to 104.5. The gains came despite dovish rhetoric from Fed's chair Jerome Powell and the FOMC keeping to expectations of three 25 bp rate cuts this year in its latest Dot Plot. We maintain our expectation of a weaker USD across 2024 as the Fed is likely to lead most major central banks in the monetary easing cycle. We argue that the conditions for a sustained USD rally are still absent despite the USD grinding higher across 1Q24, especially when rate spreads of Major FX pairs have not widened materially in favor of the USD in the last couple of months. For major DM FX against the USD, our updated forecasts for EUR/USD, GBP/USD, AUD/USD and USD/JPY are 1.11, 1.32, 0.68 and 144 respectively for 4Q24.

Despite underperforming in 1Q24, we keep to our view of an Asia FX recovery this year, driven by renewed USD weakness from the Fed beginning its rate cut cycle while we expect Asian central banks to largely hold rates steady. Other supportive tailwinds include robust Asia GDP growth profiles relative to the US and regional exports returning to growth. For Asia FX, our updated forecasts for USD/CNY, USD/KRW, USD/THB, USD/MYR, USD/IDR, USD/VND and USD/SGD are 6.95, 1,280, 35.20, 4.55, 15,200, 24,100 and 1.31 respectively for 4Q24.

Rates Strategy: To cut or not to cut

Although our US macro team's base case remains unchanged and they are still looking for US monetary policy easing to kick off this year, recent data does shift the needle towards the possibility that there may be fewer cuts delivered rather than more cuts. Notwithstanding the shifting balance of risk, based on our projected timeline for a Jun cut, monetary policy

easing dynamics should begin to reassert themselves. Short term rates are expected to drift lower across 2024 in tune with our expectations of 75 bps rate reductions from the US Federal Reserve.

For end 2Q24, we see the 3M compounded in arrears Sofr and Sora at 5.22% and 3.67% respectively. Thereafter, short term rates are then expected to drift lower across 2024 in tune with our expectations of 75 bps rate cuts from the Fed. Eventually the 3M compounded in arrears Sofr and Sora could drop to 4.73% and 3.46% respectively by 4Q24.

For the longer end of the curve, we peg the 10Y UST and SGS yields at 3.90% and 2.85% respectively by end 2Q24. Our forecasts have been tweaked higher by 0.10% from the previous month given that scenario probabilities have shifted towards fewer Fed rate cuts. Our forecast assumes that the long-term relationship which governs the process of SG rates adjusting by a lesser degree to US rate changes will continue to hold into 2024 as well as to persist across the whole US rate cut cycle. Fundamentally, we think that the potential for significant SGS outperformance is limited because the SGD NEER is starting from a position of strength and we do not expect the MAS to tighten monetary policy further. Across 2024, the 10Y UST and SGD yields are forecasted to progressively decline and may touch 3.70% and 2.70% respectively by end 4Q24

Commodities Strategy: Raising our positive gold forecast further to USD 2,450 / oz by 1Q25

The drivers for our positive forecast for gold have not changed. These are specifically strong central bank allocation into gold, especially that of EM and Asian central banks and particular strong purchases from People's Bank of China (PBoC) as well. Further out into second half of the year, once the Fed does cut rates, investment demand for gold, potentially via various investment products including ETFs, will likely increase providing the impetus for further gold strength. Over the near term, rising geopolitical risk has triggered stronger inflows into gold and that is evident via rising futures related positioning. This latest leg of the rally in gold higher is interesting because the precious metal has shown resilience against USD that has stayed strong in 1Q24. This worth watching closely and may suggest a regime change whereby other key drivers for gold strength now come into play. Overall, we raise our positive gold forecast further to USD 2,300 / oz for 2Q24, USD 2,350 / oz for 3Q24, USD 2,400 / oz for 4Q24 and USD 2,450 / oz by 1Q25. Prevailing spot reference rate is USD 2,280 / oz.

The recent renewed rise in crude oil price following escalating geopolitical risk adds to unease, and is also another development that may "spoil" the Fed's start of rate cuts in Jun. Over the past month, amidst rising geopolitical risk, Brent crude oil price has recovered strongly from USD 82 / bbl to USD 88 / bbl. The rise in geopolitical risk can be attributed to two fronts. First, Ukraine has started to target Russia's energy and refinery facilities. Second, the conflict between Israel and Hamas now risk escalating to implicate Iran, which has become a key energy producer.

We have argued since the start of the year when Brent crude oil was trading around the USD 80 / bbl, that the energy benchmark should trade higher nearer to USD 90 / bbl to reflect rising geopolitical risk premium. Unfortunately, in recent weeks, our warning turned out to be true, whereby Brent crude oil price has indeed traded higher on rising geopolitical risk. And the consequence of rising energy price is the renewed rise in inflation expectation which may complicate the Fed's anticipated rate cut in June. For now, market is sanguine to this risk as Chair Powell has said previously that the Fed does not yet see much risk of sustained pass through of rising costs from this latest renewed rise in energy price.

We expect energy benchmark to trade higher nearer to reflect rising geopolitical risk premium and we keep our positive Brent forecasts at USD 85 / bbl in 2Q24 & 3Q24, and rising to USD 90 / bbl in 4Q24 & 1Q25.

Asset Allocation

The Fed wants to ease but timing likely constrained by resilient economy and stickier than expected inflation

The year started with strong gains in most asset classes. In the latest FOMC meeting, the Fed confirmed its intent to cut interest rates, most likely starting from the June meeting but the timing is now a question mark given the resilient US economy and stickier than expected inflation outturns. Importantly, Fed Chair Powell also lowered the bar to ease by raising its GDP forecast for end-2024 to 2.1% and the core PCE Price index to 2.4%. The Fed's long-run policy rate remains unchanged at 2.5%.

The US economy has stayed resilient with the housing market showing signs of a recovery despite high mortgage rates. The other interest rate-sensitive sectors such as the autos are modestly affected. With strong corporate earnings, the equity market will likely stay supported even though market valuations have trended above historical averages. However, excluding the effects of mega-cap stocks, as proxied by the S&P 500 equal-weighted index, the US equity market is valued at 17.5x 12-month forward earnings, which is in line with its long-term history (Fig. 1).

Whilst the "Magnificent 7" names have been driving much of the outperformance since 2023, most of the gains can be attributed to higher earnings. **As we expect market gains to broaden out, we recommend investors to diversify outside of the mega-caps for better upside potential.** Artificial Intelligence (AI) has been the principal market driver for the technology sector, with Nvidia now valued over USD 2tn. Looking ahead, the economic benefits of AI will broaden out from semiconductors to infrastructure companies including cloud service providers. AI will bring forth innovation and productivity growth for the broader economy.

For the US market, we recommend that investors build some exposure in the more value-oriented sectors such as energy and financials. These cyclical sectors are expected to benefit from a rebound in the manufacturing activity.

Meanwhile, the Bank of Japan (BOJ) has finally ended its unconventional policy of 17 years by hiking its policy rate to 10bp and officially ending the yield curve control (YCC). Despite the surprise move, BOJ's communication was carefully crafted to avoid unwanted rates and FX volatility, thereby culminating in further JPY weakness.

The policy set-up remains supportive for Japan's equity prices as inflation will spur a new cycle of lending and investments in the coming years. Improving corporate governance should also pose as a tailwind for stocks. **We maintain our positive view and recommend investors to keep the JPY unhedged in the event of a sudden shift in monetary policy**. South Korean equities could also benefit from a Japan-styled "value-up" initiative by reducing its material discount.

Figure 1 – US market outside of the mega-caps looks reasonably priced

Source: Bloomberg, UOB Private Bank

While Chinese equities have rebounded 16% from their recent lows, further gains are likely to be capped without more material stimulus or measures to resolve the liquidity crisis in the real estate sector. Direct measures to support consumption also remain absent. Having said that, the external sector should stabilise alongside the global manufacturing rebound.

The recently announced government spending on infrastructure will also provide some fiscal support. **With the Chinese equity market trading at depressed valuations, downside risk from current levels is likely limited.** Meanwhile, some upside potential remains as the government could step up its policy action. **Overall, we view that the 5,000 level on the HSCEI acts as a key confidence barometer that the Chinese government would like to hold (Fig. 2).**

Figure 2 – Yield gap is at historic high - risk-reward is attractive but a catalyst is needed for a bull phase

Source: Bloomberg, UOB Private Bank

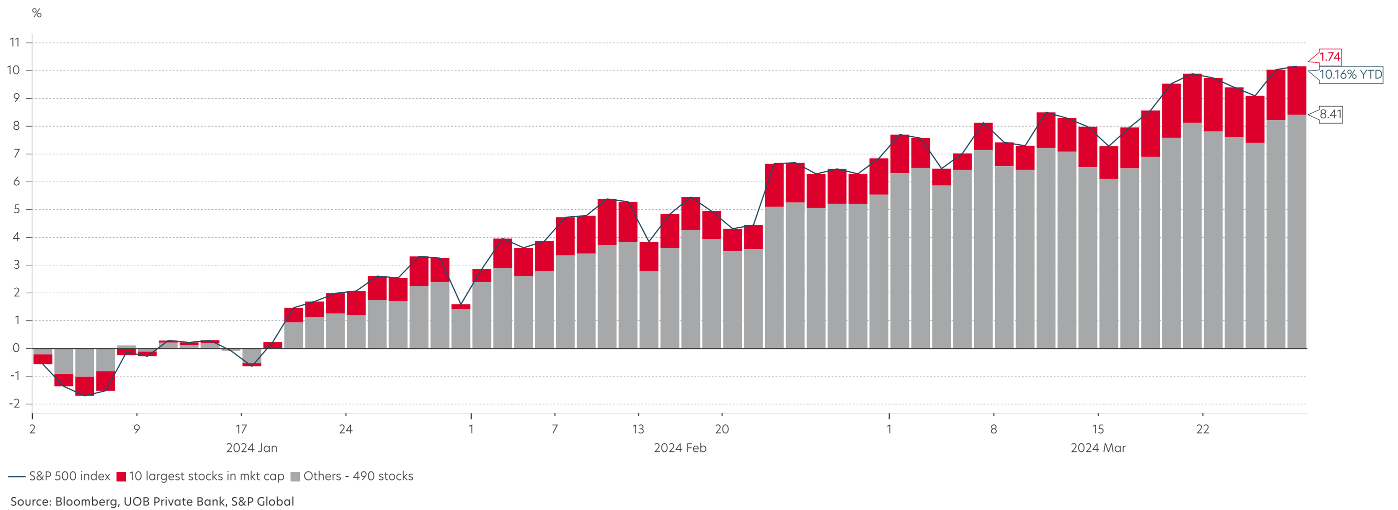
Source: Bloomberg, UOB Private Bank

Against a benign macro backdrop, we recommend an increase in the allocation to equities given falling inflation and supportive growth. While the broad US equities are overbought and no longer cheap by historical standards, they are more reasonable outside of the top mega-caps. **We recommend clients to take some profit and switch into the more value-oriented sectors, equal-weighted indices and small and mid-cap sectors that will benefit from declining rates (Fig. 3).**

Regionally, **we have increased allocation to emerging Asian equities**, funded out of a reduction in the relative weight of US equities. In emerging Asia, China remains a tactical trade. We stay constructive in most ex-China economies such as South Korea, India and the ASEAN region. We maintain an overweight on Japan's equities while Europe's equity exposure has been upgraded to neutral.

Figure 3 – The US market breadth has improved

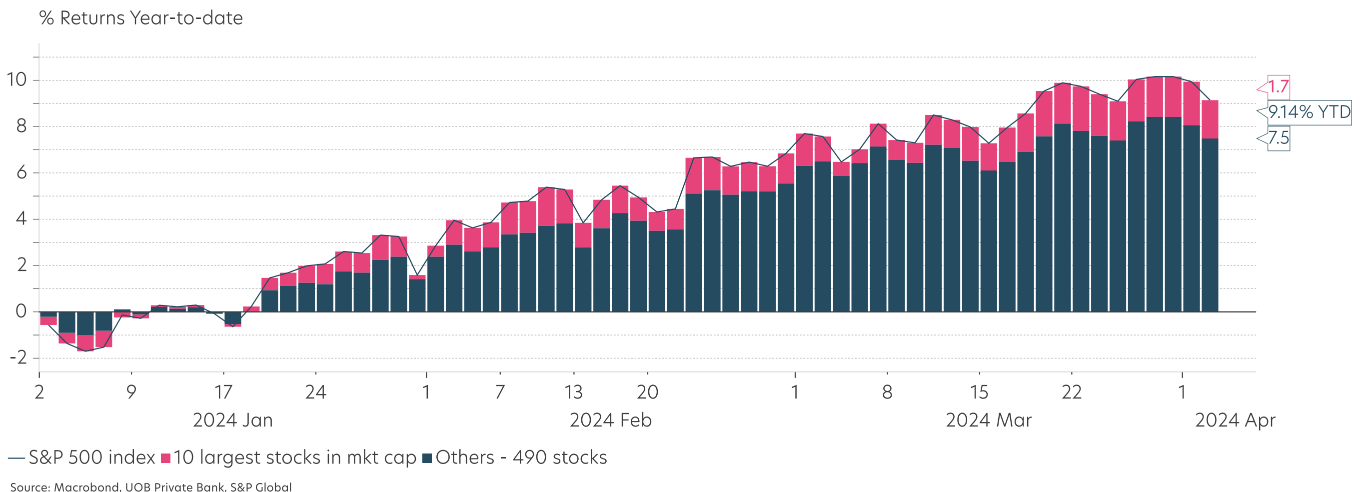
Source: Bloomberg, UOB Private Bank



The relative shift from fixed income does not reflect a bearish view but better short-term opportunities in selected sectors within equities. We continue to advocate an allocation to fixed income which will also benefit from the tailwind of falling rates. To date, emerging market bonds have outperformed treasuries. Credits have outperformed government bonds while high-yield debt have outperformed investment-grade bonds. **We maintain a positive view on alternative assets** given their diversification benefits and returns potential under current macro conditions.

Figure 4 – The largest stocks drive more than 65% of S&P 500's returns in 2023

Source: Macrobond, UOB Private Bank, S&P Global



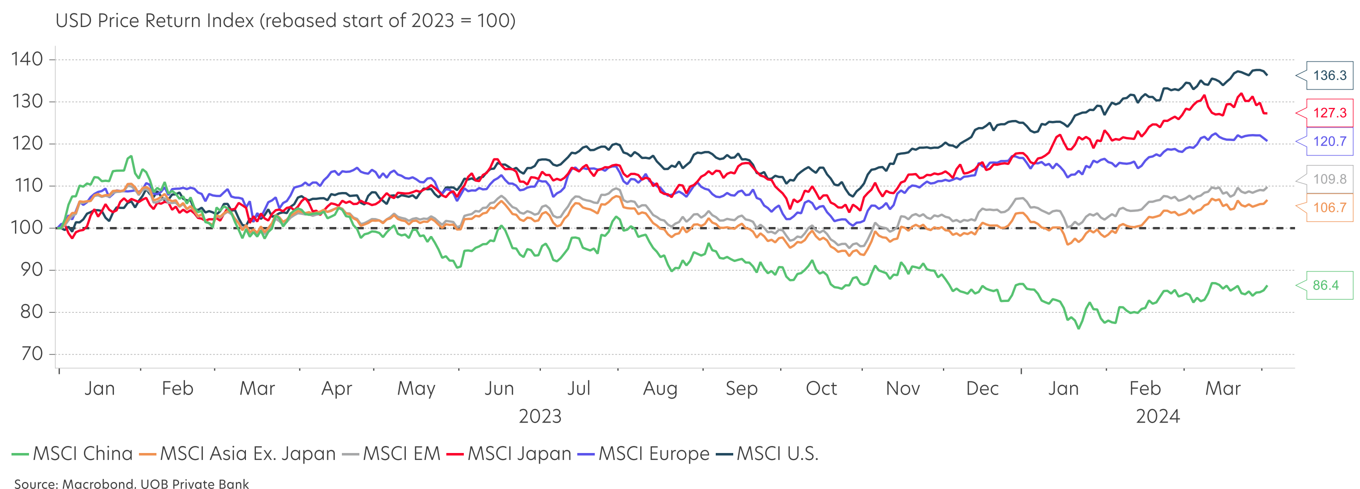
Asset Allocation Table (2Q 2024)

Asset Classes	U/W	N	O/W
Equities		○ →	●
United States	●	← ○	
Europe	○ →	●	
Japan			●
EM Asia		●	
Fixed Income		●	← ○
DM IG			●
DM HY	●		
EM IG			●
EM HY		●	
Alternatives			●
Hedge Funds			●
Private Markets		●	
Crude Oil			●
Base Metals		●	
Precious Metals		●	
Money Market	●		

Equities

Equity Performances

Source: Macrobond, UOB Private Bank, Federal Reserve



Source: Macrobond, UOB Private Bank

MSCI USA (+10.0% in USD terms) outperformed all other regional markets except Japan year-to-date (as of 31 Mar 2024). This came on the back of a better-than-expected goldilocks outcome fast becoming the market consensus and the halo effect Generative AI has on many US stocks. Equity positioning has steadily risen alongside crowding into the Momentum factor, culminating in market dislocations across global equities over the past year. Notably, US "Magnificent 7" continued to drive a disproportionate share of returns amidst sustained positive earnings revisions whilst the small-cap names lagged.

On economy, data point to resilient US growth, continued disinflation and a bottoming manufacturing PMI. Despite a recent uptick in US "supercore" inflation, Fed Chair Powell reiterated that price pressures will continue to ease, and lower rates will likely be appropriate at some point in 2024. He also clarified that expected policy easing will not be affected by a strong labour market going forward.

Importantly, the Fed has lowered the bar for its planned policy easing by lifting both inflation and GDP projections for 2024. All these point to a dovish Fed policy tilt. Finally, the business cycle outlook remains supportive albeit moderate headwinds including fading fiscal thrust and diminishing savings could limit growth.

On markets, investor complacency can be observed from several indicators; this could persist as long as the odds of strong inflation or recession stay low. Following an overextended equity rally, the uptrend could enter a more volatile phase with increased sensitivity to the macroeconomic outlook. Fed rate cuts without an economic or financial crisis would spur the next up leg in risk assets, including a potential mania in mega-cap stocks. A caveat would be the Fed could use its massive room for maneuvre to drag its heels on rate cuts. Overall, the cyclical bull market is still intact, but the risk of near-term correction has risen.

Given that higher volatility can be expected in the near term, investors could look to buy on pullbacks or engage defensively via structured products. Diversification is key. As the US market breadth broadens, investors may consider opportunities outside of the "Magnificent 7", for instance, in value-oriented sectors including Energy and Financials. Small- and mid-cap sectors can also benefit from declining rates. Prudent investors should take some profits.

Overall, **we downgrade US equities to Underweight from Neutral**.

MSCI Europe (+4.6% in USD terms) continued to trail behind the US and Japan year-to-date (as of 31 Mar 2024). Valuation re-rating more than offset the slight downward earnings revisions as well as EUR depreciation against the USD, culminating in the single-digit positive USD returns. Rising expectations for policy rate cuts from the Fed and ECB have bolstered risk sentiments. Having said that, euro area's corporate earnings outlook warrants caution given weak exports demand amid tepid Chinese recovery.

On economy, the two largest EU economies, Germany and France, continued to contract in March. In contrast, EU peripherals including Spain have been growing at a solid pace relative to expectations. Broadly, services drove private-sector activity higher but the gauge for manufacturers fell and surprised on the downside. With Germany likely entering recession after a 4Q23 contraction on manufacturing drags, Europe's industrial sector is set to be a weak spot. In this regard, China's lacklustre consumption recovery and excess capacities need to be resolved for EU industrial exports to see a meaningful uplift. A silver lining is that the underlying price pressures have been diminishing alongside slowing wage growth. As the threat to inflation expectations recedes, the ECB could begin easing at mid-year.

On markets, MSCI Europe has trailed behind regional DM peers given its relatively sizeable underweight on the Tech sector (which has outperformed) in 1Q24. With Industrials comprising the largest part (i.e., ~17.5%) of the MSCI Europe equity basket, this relative underperformance could start to reverse when Europe's industrial exports strengthen on a sustained pick-up from China's manufacturing activity.

Looking ahead, there remain pockets of opportunities in MSCI Europe; selected stocks riding on the macro theme of rising military defense expenditure, or the structural theme of renewables transition could still perform well. Finally, the slump in commercial real estate and rising energy prices will be key risks to watch.

Taken together, selectivity still needs to be emphasized amid rising rate-cut expectations. We remain on watch for a sustained Chinese manufacturing rebound which would bode well for European industrial exporters at large. Quality large-cap names as well as dividend stocks with a solid track record of stable payout remain favoured as core holdings.

Overall, **we upgrade Europe's equities to Neutral from Underweight**.

MSCI Japan (+10.2% in USD terms) outperformed all other regional markets (as of 31 Mar 2024) despite a weak yen. Within equities, our sole overweight call on Japan has panned out well. Investors continued to reprice the potential for a major and transformative economic shift as inflation takes hold following long periods of deflation. Markets remained optimistic

that higher wage growth will promote a healthy level of inflation and spur higher consumption. With momentum and earnings per share (EPS) upgrades supporting bullish sentiments, any near-term pullbacks are expected to be short-lived.

On economy, the core CPI inflation has begun to roll over with the yen consolidating near 150 against the US dollar. To this end, Japan's inflation trajectory mainly reflects its currency situation. Some market participants argued Japan could be in for a wage-price spiral following a strong increase in negotiated wage of late. However, negotiated wage has never been a good predictor of the actual nominal wage growth. This is because most of the small and medium-sized enterprises usually do not engage in wage raises advocated by the labour unions.

Separately, Bank of Japan's (BOJ) removal of negative interest-rate policy and the suspension of yield curve control (YCC) can be seen as dovish policy adjustments; the cautious moves are unlikely to upset Japan's strong equity rally and resilient economic performance.

On markets, Japan's easy money and weak currency continued to boost nominal corporate earnings. The reversal in price expectations encourages capital investments and leverage given still-negative real interest rates. Meanwhile, earnings momentum remained favorable.

While MSCI Japan now trades at a more demanding valuation (i.e., 17x 12MF P/E) relative to history, the rerating is well-sustained amidst robust foreign inflows. Continued corporate governance reforms are expected to support improvement in shareholder returns. Beyond any technical pullbacks, the outlook for Japan's equities remains ebullient.

Against this backdrop, investors should consider keeping the yen unhedged in Japanese equity portfolios to defend against any abrupt shifts in BOJ's monetary policy. Investors can gain defensive exposure via structured products, with quality companies leveraged to domestic consumption recovery, corporate reforms and AI/tech manufacturing as underlying securities.

Overall, **we remain Overweight on Japan's equities**.

MSCI Asia ex-Japan (+2.0% in USD terms) clocked a slight positive return year-to-date, dragged by MSCI China (-2.3% in USD terms) which began the year with a sharp correction (as of 31 Mar 2024). Sentiments towards China have stayed pessimistic; the latest fund managers' surveys suggest shorting China is still one of the most popular trades. Looking ahead, a decisive technical breakthrough backed by substantial Chinese government stimulus support will likely be required for capital flows to return, and to propel the Chinese equity rally beyond a "dead cat bounce". Having said that, the downside potential is likely to be limited from current levels.

On economy, latest indicators point to China's intention to "meander through", i.e. to maintain economic resilience without much policy support. China's 2024 government budget suggests a modest increase in fiscal thrust relative to last year, while financial conditions have eased since the start of the year.

Looking ahead, China's economy could stay sluggish for a while amid fragile domestic confidence and continued property woes. On a more positive note, Chinese manufacturing exports are recovering while the broad deflationary pressure has eased. Excavator sales also point to warming construction activity.

On markets, Chinese equities are still hovering at an undershoot extreme with practically no multiple expansion. The discount between China and their global as well as EM peers remains at record levels. Looking ahead, any positive catalyst could drive Chinese equities higher given depressed expectations.

Notably, the government's attempt to boost foreign business confidence via the "Invest In China" campaign could pave the way for structural reforms. While the effectiveness of the campaign remains to be seen, the top leadership in China has at least recognized the importance of privately owned sectors as well as foreign businesses in driving the country's economic development.

Against this backdrop, the odds of a sustained Chinese equity valuation rerating remain small despite an improvement in China's economic outlook. With a view that the downside potential for Chinese stocks is limited, investors can consider engaging defensively via structured products.

Across emerging Asia, China remains a tactical trade. We reiterate preference for stocks in South Korea, India and ASEAN region; investors can gain exposure to them via diversified vehicles like funds.

Overall, **we remain Neutral on EM Asia's equities**.

Fixed Income

Developed Markets Investment Grade Credits

DM Investment Grade (IG) proxied by US Corporate IG (Bloomberg US Corporate Bond Index) delivered a -0.4% total return year-to-date (in USD terms, as of 31 Mar 2024). This was driven by a pair of offsetting effects: modest credit spread tightening (~9bps year-to-date) and negative US treasury (UST) returns. Notably, UST yields climbed, and UST curve steepened on the back of US economic resilience.

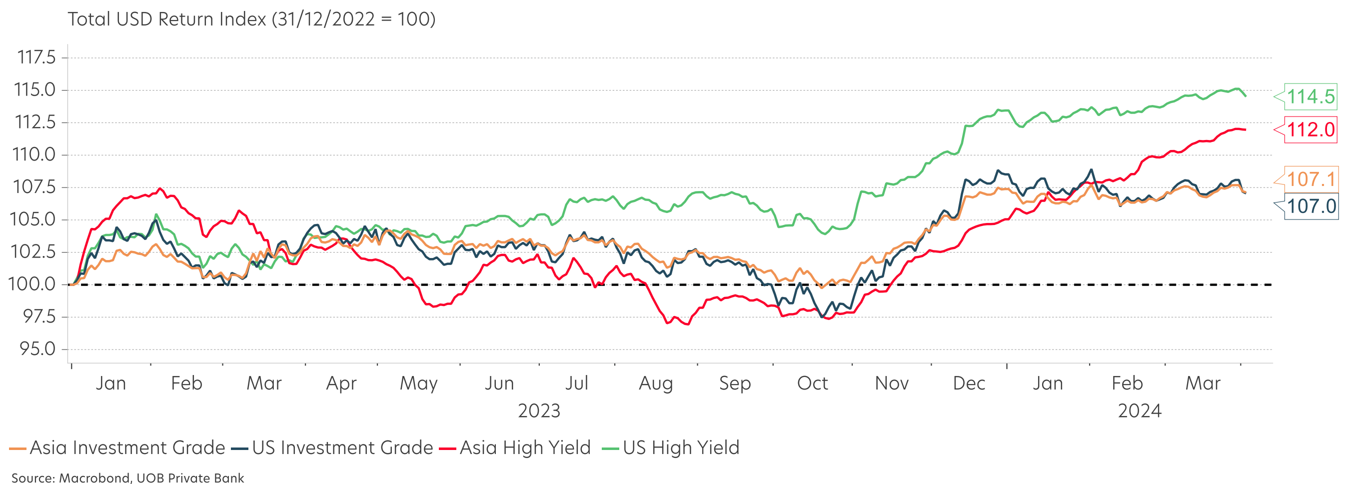
The concoction of resilient US economic growth, Fed rate-cut expectations, looser financial conditions, and relentless US equity markets renders it a conducive environment for credit spreads to tighten. As such, credit spreads for high-quality issuers will likely stay supported; if not, credit spreads should grind tighter in the absence of material rates move.

Current credit valuations may appear stretched but all-in-yields remain attractive from a historical perspective. As such, any excess returns for the rest of 2024 will likely be driven by credit selection; the avoidance of adverse credit events will prove paramount. We continue to advocate a bottom-up approach in selecting fundamentally robust credits to secure income over a longer horizon.

Overall, **we remain Overweight on DM USD IG**.

Fixed Income Year-to-date Performances

Source: Macrobond, UOB Private Bank



Developed Markets High Yield Credits

DM High Yield (HY) outperformed its IG counterpart as US Corporate HY (Bloomberg US Corporate High Yield Index) returned +1.5% year-to-date (in USD terms, as of 31 Mar 2024). Default rates are projected to inch higher but have thus far been relatively manageable and pose no systematic risk.

Against this backdrop, HY credit spreads outperformed by tightening ~18bps year-to-date, and continue to be a source of excess return via elevated credit carry (301bps average OAS on index level).

The credit spread compression between IG and HY as well as rising tail risks from an acceleration in defaults lead us to be cautious of the asymmetric risk-reward.

Therefore, **we remain Underweight on DM USD HY**.

US IG and HY Corp Bonds Average OAS

Source: Macrobond, UOB Private Bank

Emerging Markets Investment Grade Credits

EM Asia Investment Grade (IG) delivered a +0.3% total return year-to-date (in USD terms, as of 31 Mar 2024) at the index level (Bloomberg EM Asia USD Credit High Grade Index). IG credit spreads were ~17bps tighter year-to-date and notably touched historical tights of 91bps on 27 Mar 2024.

Against a supportive macro backdrop, favorable demand-supply dynamics, and lower volatility (relative to the US and global credits), EM Asia IG remains an effective portfolio stabilizer during events of market dislocations.

Our preference within EM Asia IG are Asia (incl. Japan and Korea) financials, select Asia-focused insurers, quasi-sovereigns/strategic state-owned enterprises, and TMT.

Taking a diversified approach to duration risk management by targeting an average modified duration of 5 to 8 years will provide investors with the opportunity to lock in yields over a longer horizon. US Treasury (UST) returns, led by the Fed's pace and magnitude of easing, will be an important contributor to total returns through 2024.

We continue to advocate buying on dips and reiterate our Overweight on EM Asia IG.

Emerging Markets High Yield Credits

EM Asia High Yield (HY) was a standout performer as the EM Asia HY index (Bloomberg Asia USD High Yield Bond Index) delivered +6.6% total returns year-to-date (in USD terms, as of 31 Mar 2024).

While the removal of defaulted China property developer contributed to base effects, it was the combination of recovery from Macau gaming sector and several special situations events (i.e., Vedanta, Sri Lanka, Pakistan, and select China/HK developers) that drove returns.

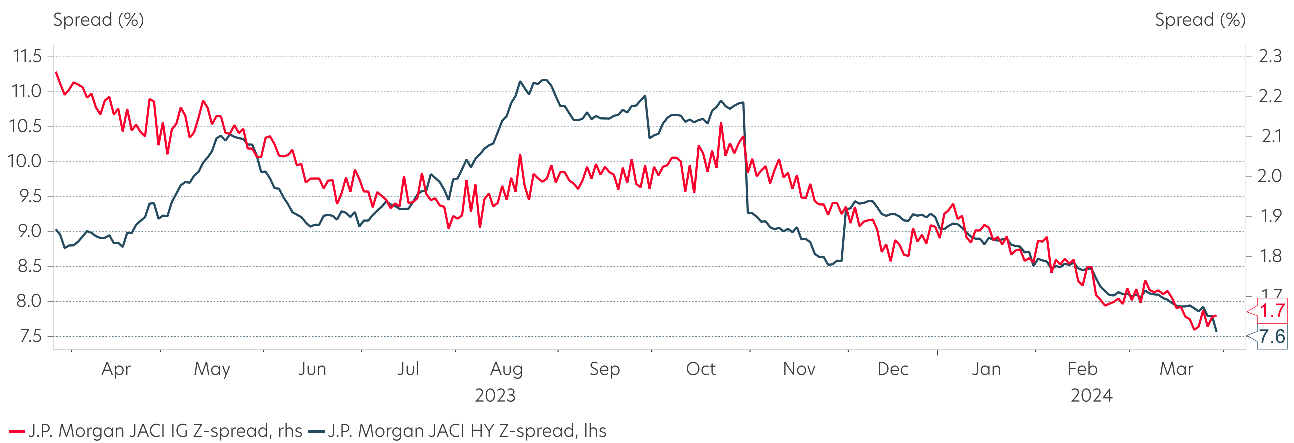
Going forward, we remain cautious on China property sector due to lacking sector policy initiatives. Additionally, positive restructuring outcomes in this space are becoming increasingly difficult to manifest as outright liquidation possibilities have been gaining traction (i.e., Evergrande and Country Garden).

We emphasize selectivity and favour selected ASEAN infrastructure, Indonesia utility and Indonesia property developers.

Overall, **we remain Neutral on EM Asia HY**.

JP Morgan JACI IG and HY Corp Bond Z-spread

Source: Macrobond, UOB Private Bank



FX, Interest Rate & Commodities Forecasts

FX	02 Apr	2Q24F	3Q24F	4Q24F	1Q25F
USD/JPY*	152	149	146	144	142
EUR/USD*	1.08	1.09	1.10	1.11	1.12
GBP/USD*	1.26	1.28	1.30	1.32	1.34
AUD/USD*	0.65	0.66	0.67	0.68	0.69
NZD/USD*	0.60	0.60	0.61	0.62	0.63
DXY*	104.76	103.2	102.1	101.2	100.1
USD/CNY*	7.23	7.15	7.05	6.95	6.85
USD/HKD	7.83	7.80	7.80	7.80	7.80
USD/TWD*	32.07	31.8	31.4	31.0	30.5
USD/KRW*	1,350	1,320	1,300	1,280	1,270
USD/PHP*	56.36	55.8	55.3	54.8	54.3
USD/MYR	4.75	4.70	4.60	4.55	4.50
USD/IDR*	15,924	15,600	15,400	15,200	15,000
USD/THB*	36.64	36.0	35.6	35.2	34.8
USD/VND*	24,970	24,500	24,300	24,100	24,000
USD/INR*	83.38	82.5	82.0	81.5	81.0
USD/SGD	1.35	1.33	1.32	1.31	1.30
EUR/SGD*	1.46	1.45	1.45	1.45	1.46
GBP/SGD*	1.70	1.70	1.72	1.73	1.74
AUD/SGD*	0.88	0.88	0.88	0.89	0.90
SGD/MYR	3.52	3.53	3.48	3.47	3.46
SGD/CNY*	5.35	5.38	5.34	5.31	5.27
JPY/SGDx100*	0.89	0.89	0.90	0.91	0.92

POLICY RATES	02 Apr	2Q24F	3Q24F	4Q24F	1Q25F
US Fed Funds Rate	5.50	5.25	5.00	4.75	4.50
JPY Policy Rate	0.10	0.10	0.10	0.25	0.25
EUR Refinancing Rate	4.50	4.50	4.00	3.50	3.50
GBP Repo Rate	5.25	5.00	4.75	4.50	4.25
AUD Official Cash Rate	4.35	4.35	4.00	3.75	3.50
NZD Official Cash Rate	5.50	5.50	5.25	5.00	4.75
CNY 1Y Loan Prime Rate	3.45	3.20	3.20	3.20	3.20
HKD Base Rate	5.75	5.50	5.25	5.00	4.75
TWD Official Discount Rate	2.00	2.00	2.00	2.00	2.00
KRW Base Rate	3.50	3.50	3.25	3.00	2.75
PHP O/N Reverse Repo	6.50	6.25	6.00	5.75	5.50
MYR O/N Policy Rate	3.00	3.00	3.00	3.00	3.00
IDR 7D Reverse Repo	6.00	6.00	6.00	6.00	5.75
THB 1D Repo	2.50	2.50	2.50	2.50	2.25
VND Refinancing Rate	4.50	4.50	4.50	4.50	4.50
INR Repo Rate	6.50	6.50	6.50	6.25	6.00

INTEREST RATES	02 Apr	2Q24F	3Q24F	4Q24F	1Q25F
USD 3M SOFR (compounded)*	5.35	5.22	4.98	4.73	4.50
SGD 3M SORA (compounded)*	3.68	3.67	3.59	3.46	3.30
10Y US Treasuries Yield*	4.34	3.90	3.80	3.70	3.60
SGD 10Y SGS*	3.16	2.85	2.80	2.70	2.65

COMMODITIES	02 Apr	2Q24F	3Q24F	4Q24F	1Q25F
Gold (USD/oz)*	2,284	2,300	2,350	2,400	2,450
Brent Crude Oil (USD/bbl)	89	85	85	90	90
Copper (USD/mt)	8,991	8,000	8,000	7,000	7,000

Updated on 03 April 2024
Source: UOB Global Economics & Markets Research

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