

# CHALLENGING DRIVE



2019 OUTLOOK & STRATEGY

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# Our 2018 Review

## A Turbulent Year Has Passed...

**Without exception, 2018 was a challenging year as almost all asset classes delivered negative returns.** The year started off well for equity markets as the tailwind from synchronised economic growth in 2017 saw markets having one of the best starts in recent years. Asian stock markets rose by between 5-10% in January alone.



However, rising interest rates negatively impacted bonds and hence fixed income funds early in the year. There were concerns that the strong economic growth would force the US Federal Reserve to raise interest rates more aggressively. Overall financial market conditions deteriorated soon after as the US triggered trade tensions with China and the rest of the world.

As a result, Asian equity markets peaked in 1Q2018 and dropped for much of the year. Negative news flow from the US-China Trade War was compounded by a noticeable slowdown of the economy in China as the government sought to bring shadow banking and the bubble of unregulated peer to peer lending under control.

Fixed income markets saw a double whammy of higher interest rates leading to interest rates on the benchmark 10 year Treasuries breaching the critical 3.0% levels from just 2.25% at the start of 2018. Credit spreads for bonds also widened significantly due to the US-China Trade War and slowing Asian economies.

### KEY HIGHLIGHTS FOR 2019

1. Slower global growth from 3.3% in 2018 to around 3.0% in 2019;
2. Inflation to remain tame
3. USD strength to moderate in 2019
4. Oil prices to remain low in the range USD 50-70/bbl
5. Interest rates: 10-year UST to trade between 2.5-3.25% in 2019
6. Yield curve: UST curve to remain flat in 1H19 but could steepen in the front end from 2H19
7. ECB and BOJ to remain accommodative
8. China to implement marginal easing measures
9. No negative surprises for Indonesia and India elections

### KEY RISKS FOR 2019

1. Negative surprises for elections in Indonesia, India
2. Hard landing in China
3. Credit spreads blow out in US and Europe
4. US economic data remains strong, prompting FOMC to be more aggressive in rate hikes
5. US-China trade tensions to find meaningful resolution
6. Oil prices to trade above USD 80/bbl
7. Geopolitical risks in the Middle East and Europe



# OUR 2019 OVERALL INVESTMENT STRATEGY

On a risk-reward basis we would tilt it towards fixed income for 2019.

On a risk-reward basis we would tilt it towards fixed income for 2019. With the higher interest rates and wider spreads, yields for Asian investment grade bonds are attractive at between 4.5-6.0% (from just 3.3% in 2017). These returns are decent bearing in mind the likely risks investors will have to face in 2019. For investors who are able to take currency risks, local currency bonds in India and Indonesia will be preferred.

Peaking US interest rates will mean that Asian central banks will face less pressure to raise domestic interest rates. In fact, given the lack of inflationary pressures there is some flexibility to reduce interest rates. In addition, peaking US rates will also mean the possibility of stronger Asian currencies as investors have less reason to move money to the US. Therefore, an investor in Asian local currency bonds will enjoy the high prevailing yields and may benefit from lower domestic interest rates plus a gain from the currency appreciation.

Yields for Asian investment grade bonds are attractive.



Asian stocks are cheap, trading at a forward PER of just 11x and at a 20-30% discount.

For equities, Asian stocks are cheap both on an absolute and relative basis, trading at a forward PER of just 11x and at a substantial 20-30% discount to US valuations. The headwinds of slower growth will cap upside as corporate earnings may disappoint in 2019. However, with the extremes of valuation we feel that downside is limited so long as the US does not fall into recession. We also note that should the trade wars resolve amicably, Asian equities could recover sharply given the trough valuations. We like REITs as the likely pause of interest rates in 2019 and continued economic growth (albeit slower) will be positive for high dividend yielding stocks.

Just like for bonds, we would favour ASEAN equities. ASEAN countries are more domestically oriented especially Indonesia and Philippines and therefore are less exposed to the Trade Wars.

Moreover, Indonesia and Philippines are more sensitive to interest rates as both countries run twin deficits (budget and current account deficits). With peaking US interest rates, the Central Banks in Indonesia

and Philippines will have more leeway to support the domestic economy. Lastly, Indonesia and Philippines are oil importers and muted oil prices will reduce the pressure on the current account deficit.

So in summary, we expect a challenging year in 2019 but there will be opportunities given the attractive valuations for Asian fixed income and equities. We would like thank you for your support amidst the difficult market environment. At Maybank Asset Management, we will continue to work hard to obtain the investment returns for our customers and also provide investment solutions, both new and existing products that would meet the individual needs of our clients.

# OUR 2019 OVERALL INVESTMENT STRATEGY

## CHALLENGING DRIVE

Themes	Our Assessment	Market Implications & Strategy
<b>Growth Slows</b>	<p>We expect to see slower global growth in 2019. The reasons for slower global growth are manifold. Financial conditions are tighter and the US-China trade war has dampened confidence and increased uncertainty thereby stalling corporate decision making and investment. In addition, export growth is likely to be muted on subdued demand and as a result of prior front-loading of exports (ahead of tariff implementation) in 2018.</p> <p>While China may struggle, as a managed economy, we believe it will succeed in maintaining GDP growth at c.6%. Similarly in Asia, we expect trend or slightly below-trend growth in most economies.</p> <p>US growth momentum will slow as the effects of past fiscal stimulus fade. We do not expect a recession in 2019, albeit that remains a possibility in 2020 (as implied by the inversion of the US yield curve).</p> <p>We expect policy makers, in general, to be more pro-active in boosting the domestic economy. More populist policies may be introduced in countries with upcoming elections in 2019 (e.g., Thailand, Indonesia, India). The Chinese government may respond to the threat of slower growth by relaxing its stance on various issues (e.g., RMB depreciation, property cooling, deleveraging/financing) and increasing fiscal spending. Note that much of the growth slowdown in China can be attributed to the government's various regulatory clampdowns in recent years which has unfortunately now coincided with the trade war.</p>	<p>Neutral for equities and mixed for fixed income (positive government bonds, less so for credits).</p> <p>Favour ASEAN over North Asia for equities and local currency fixed income.</p> <p>Prefer Asian credits with high carry.</p> <p>Favour domestic-oriented names / defensives over cyclical.</p>
<b>INFLATION MUTED; LOWER OIL PRICES</b>	<p>We expect inflation to remain muted in 2019. While there may be a bounce in oil prices in the short term (off the current low base), overall we would expect lower oil prices in 2019 as US shale supply comes on stream. In addition, food inflation should remain benign barring weather shocks.</p> <p>Slower global and capex growth will also weaken commodity demand and prices. The US-China trade war may also prove to be deflationary outside the US. China-made goods will be cheaper with a weaker RMB and China could divert (i.e., dump) its goods to other countries. In contrast, the trade war may increase inflation pressures in the US given more costly imports of consumer goods. Given excess capacity in most of the region, we see little price pressure stemming from capacity constraints.</p>	<p>Negative on most oil plays.</p> <p>Lower oil prices positive for India, Indonesia, the Philippines and Thailand.</p>

# OUR 2019 OVERALL INVESTMENT STRATEGY

## CHALLENGING DRIVE

Themes	Our Assessment	Market Implications & Strategy
<b>MONETARY POLICY CONTINUES TO TIGHTEN BUT CLOSER TO THE END; A WEAKER USD</b>	While we expect the Fed to continue to hike in 2019, we believe the rate hike cycle is largely coming to an end in 2019. Normalization will continue as US core inflation remains close to 2% but mounting growth concerns will eventually lead to a pause in hikes.	Prefer US government bonds and Asian local currency government bonds.
	With the flattening US yield curve and given growth risks, we expect the USD to be weaker and correspondingly most Asian currencies to be stronger in 2019. With the exception of China which will ease in order to support its slowing economy, we expect monetary policy to be neutral in most of Asia.	Favor REITs and high dividend yielding stocks.
	We see less pressure on Asian central banks to hike rapidly given a benign inflation environment and less currency pressure from a weaker USD.	Favor Asian currencies over the USD. Favor beneficiaries of weaker USD
<b>MORE VOLATILITY; GEOPOLITICS MATTER</b>	We expect markets to remain volatile in 2019 given the uncertainty and risks to growth. For fixed income, we expect continued refinancing pressure.	
	Binary outcome of US-China trade war will require nimble trading to capture opportunities or preserve capital. The US-China trade war is not just about the economics of trade but increasingly seems to be about containing the rise of China which makes any meaningful resolution difficult.	More tactical trading. High cash allocation from time-to-time.
	While general elections in India, Indonesia and Thailand are likely to see the incumbents returned to power (albeit with an uncertain majority), there is always the risk that the unexpected could occur.	Once election uncertainty is out of the way, India and Indonesia might rally.
	Other sources of geopolitical risks include Brexit; elections in Europe (namely, in Germany and Italy); ECB tapering and Middle East tensions.	
<b>GLOBAL TRADE / SUPPLY CHAIN REFORM</b>	With the US-China Trade War, companies will diversify their production bases. Some MNCs and local Chinese companies have already begun relocating their production from China which could benefit some ASEAN countries. These activities to diversify production bases will accelerate. However, this process may take some time depending on the availability of associated supply chains and infrastructure.  Restructuring of the global trading architecture. The Multilateral system of trade has underpinned the global trading system and was represented by the WTO. The multilateral system worked by getting consensus from all countries. It was generally fair imposing the same tariffs across all countries with certain concessions given. This has broken down given the lack of support from the US and as world has become more complex world it is now hard to get agreement amongst all countries. Countries now prefer to pursue bilateral FTAs.	Favor selected exporters that benefit from production shifts away from China.

# OUR 2019 ASIA EX-JAPAN OUTLOOK

## EQUITIES

**Post the 2018 market sell-off, Asian equities are looking more attractive from a valuation perspective.** Asian equities are trading at 11.2X forward P/E (versus historical average of 12X) and at a 26% discount to US equities (versus historical average of 14%). Coupled with the prospect of the Fed ceasing its rate hike cycle in 2019, expectations for a weaker USD and benign inflation, we expect Asian equities to outperform developed markets in 2019. We see Asia as a beneficiary of fund inflows as investors rotate from developed markets into emerging markets.

We expect markets to be volatile in 2019, thereby necessitating more tactical trading and high cash holdings from time-to-time. We also see value in having some defensive names and high dividend yielding stocks as a portfolio hedge.



**Key risks in 2019 include the outcome of the US-China trade war** (which could move either way – resolution or escalation); a possible US recession in 2020 (as implied by the inversion of the US yield curve); and geopolitical risks. In the event of a US market correction (perhaps driven by US recession fears), Asian equities will not remain unscathed but may decline less given their relative underperformance in 2018 and the relative valuation gap.

**We would favour the more domestic-oriented ASEAN markets over North Asia** given expectations of slower global growth and US-China trade war risks. In addition, lower oil prices would benefit most ASEAN countries, with the exception of Malaysia. Twin-deficit ASEAN countries such as Indonesia and the Philippines should also see less currency pressure given a weaker USD and consequently less need for rapid rate hikes. With Indonesia and the Philippines being some of the biggest beneficiaries of the aforementioned factors and given relatively better earnings growth versus regional peers, we would overweight both Indonesia and the Philippines. The upcoming elections in Indonesia should also be positive from the standpoint of boosting consumption (given pre-election spending) and removing political uncertainty (barring a shock election result).

Case	Assumption / Risk	Market Implications & Strategy
● <b>BAD CASE</b>	<ol style="list-style-type: none"> <li>1. Weaker-than-expected economic growth.</li> <li>2. Further trade war escalation.</li> <li>3. Negative inflations surprise.</li> <li>4. Heightened geopolitical tension.</li> </ol>	<ul style="list-style-type: none"> <li>• MSCI Asia ex-Japan target 570, based on 10.5X 2020E EPS of 54 (-5%).</li> </ul>
● <b>BASE CASE</b>	<ol style="list-style-type: none"> <li>1. Slower global growth but no US recession nor China hard landing.</li> <li>2. Trade war continues without severe escalation.</li> <li>3. Muted Inflation; lower oil prices.</li> <li>4. The Fed continues to hike but rate hike cycle comes to an end in 2019. In Asia (ex-China), monetary policy is neutral.</li> <li>5. Weaker USD, stronger Asian currencies.</li> <li>6. No severe geopolitical incidents.</li> </ol>	<ul style="list-style-type: none"> <li>• Overweight: India, Indonesia, Philippines.</li> <li>• Underweight: Hong Kong, Taiwan, Korea, Thailand.</li> <li>• Neutral: Others.</li> <li>• Favour ASEAN over North Asia.</li> <li>• Favour domestic-oriented names / defensive over cyclicals.</li> <li>• MSCI Asia ex-Japan target 640, based on 11.6X 2020E EPS of 55 (+6%).</li> </ul>
● <b>GOOD CASE</b>	<ol style="list-style-type: none"> <li>1. Better-than-expected economic growth.</li> <li>2. Easing of trade tensions.</li> </ol>	<ul style="list-style-type: none"> <li>• MSCI Asia ex-Japan target 680, based on 12X 2020E EPS of 57 (+13%).</li> </ul>

Based on MSCI Asia ex-Japan Index closing price of 602.10 on 14 December 2018.

# OUR 2019 ASIA EX-JAPAN OUTLOOK

## LOCAL CURRENCY FIXED INCOME & CURRENCY

We expect global GDP growth to slow from around 3.3% in 2018 to around 3.0% in 2019. The key driving forces for slower GDP growth will be a late-cycle US economy, Trump's 2018 tax cuts wearing off, end of QE, and the slowdown in global trade. Growth in China is expected to slow from 6.5%–6.6% in 2018 to 6.0%–6.1% in 2019, which brings EM Asia GDP growth to below 6.0%. Despite slower growth in the coming years for Asia, we are cautiously optimistic on Asian local government bonds and currencies as USD strength is likely to abate due to a pause in Fed hikes and lower crude oil prices. Additional factors that are helpful towards EM Asian local currency (LCY) bonds and FX include light positioning, cheap valuations, high real yields and tame inflation in EM Asia in 2019.



Slower global GDP growth by 0.3%.

**"Recovery begins from the darkest moment."**

- John Major, Former British Prime Minister.

We had highlighted previously that the biggest threat to Asia LCY and FX markets was the perception of synchronised tightening by the G3 central banks. While only the Fed had hiked rates over 2018, the impact of liquidity withdrawal had caused EM currencies to weaken considerably. However, as we are writing this, the market seems to be having a rethink about the trajectory of Fed rate hikes as yields have declined from October's high and given the inversion in the front end of the yield curve. Indeed, for 2019, our base case is for the Fed to hike probably twice through 2019 if economic data remains firm. However, we should provide for the possibility that the Fed may only hike one time if trade tensions escalate. Meanwhile the ECB and BOJ are expected to remain accommodative at least through 1H19, with latest macro data leaning on the weaker side.

### ASIAN LCY GOVERNMENT DEBT AND FX: PICKS AND PANS FOR 2019

Government Bonds (LCY)	-2	-1	0	+1	2	FX	-2	-1	0	+1	2
China			•			China			•		
India				•		India				•	
Indonesia				•		Indonesia					•
Korea				•		Korea		•			
Singapore				•		Singapore			•		
Malaysia			•			Malaysia		•			
Taiwan			•			Taiwan		•			
Thailand			•			Thailand			•		
Philippines				•		Philippines				•	

# OUR 2019 ASIA EX-JAPAN OUTLOOK

## LOCAL CURRENCY FIXED INCOME & CURRENCY

We still like the LCY debt markets in Indonesia and India from both carry and currency appreciation perspective.



We still like the LCY debt markets in Indonesia and India from both carry and currency appreciation perspective. **The valuation in terms of real yield and real effective exchange rates are highest in these two countries.** We expect inflation in both countries to remain muted and fall due to lower oil prices. Also we expect the Fed to pause next year which will be positive for these economies as they will be able to ease monetary policy by the end of 2019. In terms of growth, India is expected to return to its longer term growth rate of 6.5-7.5%, compared to 6.2% in 2017 as it exits from the impact of demonetisation. Indonesia is also expected to grow between 5.0-5.5% in 2019.

Meanwhile for the Philippines, growth is expected to remain strong due to infrastructure investment and consumption while inflation expectations have been held in check after the BSP raised rates by 150 bps from 1H18 to 4.75%. Furthermore, November's headline inflation has also slowed to 6.0% from 6.7% earlier and looks likely to decline even further given lower oil prices. For 2019, we also like Philippines as we expect inflation in the Philippines to gradually come down in 2019 due to declining oil prices and the 150 bps of aggressive hikes by BSP in 2018.

In anticipation of slowing growth and reduced inflationary pressures, Singapore's MAS is likely to keep its SNEER exchange policy stable in 1H19.

**For Malaysia, our call of MYR outperforming EM Asia FX has panned out,** with USDMYR recording a YTD loss of 3% vs. -13% for USDINR, -8% for USDIDR and -6% for USDPHP. While the MYR remains cheap in the long run, we think low oil prices and slowing trade will impact balance of payment prospects, preventing the MYR from appreciating further.

**Despite the outlook for a volatile year, fundamentals of many Asian currencies remain challenging** as they grapple with an environment of high debt, worsening demographics and sluggish productivity. The pickup in growth in EM Asia in 2018 was more due to external demand from DM and less from domestic demand. However, we expect this to reverse in 2019 as we expect domestic-driven South East Asian economies to do well and export-driven North Asian economies to weaken. We expect South East Asian currencies with high real yield to outperform North Asian currencies. The risk to this outlook is a quick resolution of US-China trade tensions.

While country allocation remains important, local currency bond returns in 2019 will come from carry, modest FX appreciation and duration gains. The expectations of a Fed pause and weaker USD will be most favourable for South East Asian countries after a dismal 2018.

### Malaysia

MYR stable for now.

### Singapore

Strong SNEER exchange policy.

### India

Growth rate to return to 6.5-7.5%.

### Indonesia

Expected to grow 5-5.5% in 2019.

### Philippines

Inflation to come down.

# OUR 2019 ASIA EX-JAPAN OUTLOOK

## USD CORPORATES

**We are projecting a total return of 3% to 5% for JACI in FY2019.** We think interest rates can go up by between 20 to 60 basis points but this can be easily absorbed given current JACI yield of 5.22% (as of 20 Dec 2018). We think that current yields are attractive and there is no need to take on too much risk for additional return.

**Our recommendation is** to have the majority (i.e., 50%) of the fund be invested in stable investment grade five year bonds, 10% in long end investment grade quasi-sovereigns, 20% in high yield with 20% in cash for trading opportunities.

### FY2019: LIGHT AT THE END OF THE TUNNEL

Key themes	Maybank AM Assessment	Positions
<b>Value has emerged in Bonds</b>	<p>Bond yields have risen by 100bps to 300bps in FY2018.</p> <p>Investment grade bonds at 4.5% and high yield bonds at 8%; bonds offer attractive value given historical volatility of less than 2%.</p> <p>Higher yields provide a buffer against a mild sell-off in interest rates.</p>	<ul style="list-style-type: none"> <li>• Bond portfolios gradually move from cash to bonds.</li> <li>• Balanced portfolios overweight bonds versus equities.</li> </ul>
<b>Fed to pause late FY2019/ early FY2020</b>	<p>The ongoing trade war during FY2018 weighed heavily on business sentiment, hindering future growth.</p> <p>US is already at a mid/late growth cycle.</p> <p>Inflation remains benign. Oil price peaked in October 2018 and has fallen over 30% from the peak.</p>	<ul style="list-style-type: none"> <li>• Yield curve remains flat. Prefer to buy less than 5-year bonds for carry.</li> <li>• Selectively buy into investment grade corporate perpetual bonds with high resets for higher carry.</li> <li>• Opportunistically trade long end quasi-sovereign bonds.</li> </ul>
<b>Growth to Slow but No Recession</b>	<p>US to avert a recession in FY2019 as Fed pauses after 1 to 2 hikes.</p> <p>China to continue to roll out targeted easing measures to support growth as they try to counter growth headwinds from both domestic deleveraging and external stress from the trade war escalation.</p> <p>Credit fundamentals to remain stable and bond defaults to remain low as China implements new policies to support the private sector such as introducing credit insurance, mandatory loan quota to the private sector, targeted cut in banks' reserve requirement ratio etc.</p>	<ul style="list-style-type: none"> <li>• Selectively add high yield exposure.</li> <li>• Access to funding is key. Prefer liquid balance sheet such as property sector.</li> <li>• Prefer Indonesia and China as risk-reward is attractive.</li> </ul>
<b>Volatility to remain</b>	<p>While fundamentals look attractive for bonds, technical factors such as fund flows and supply pressure can overwhelm.</p> <p>Continued equity weakness can dampen risk appetite for credits despite attractive yields.</p> <p>Geopolitical headwinds continue, from US-China trade war, elections, Brexit, ECB tapering, Middle East tensions.</p>	<ul style="list-style-type: none"> <li>• Keep 50% of the funds in 5-year investment grade bonds for attractive stable carry of 4% to 5%.</li> <li>• Keep 20% in short dated high yield and 10% in long end quasi-sovereigns.</li> <li>• Maintain 20% in cash for opportunistic trading.</li> </ul>

2019

# OUTLOOK

SINGAPORE



# SINGAPORE 2019

## EQUITIES

### OUR OUTLOOK

**We are positive on the outlook for Singapore equities in 2019.** The market correction this year has made valuations attractive. The forecast 2019 Price to Earnings ratio for the Singapore market is about 11x, which is not expensive relative to other stock markets. Trading at 1.5 standard deviations below its historical mean, it is also cheap relative to history. In other words, the market has priced in a fair bit of bad news. If 2019 turns out to be better than expected, the equity market could perform very well.

**There are two notable points about our 2019 outlook.** First, the range of possible outcomes is wider than usual as the key risk is geopolitical. While our base case is for the US and China to reach a negotiated deal on trade, it is also possible that negotiations could break down, relationships could deteriorate and tit-for-tat measures could spiral out of control. We are aware of a small but existent tail risk of a negative outcome for the global economy.

Second, we do not expect 2019 to be as good as 2018. Even if a deal on trade is reached, there has been some damage done on supply chains. Tariffs are economically equivalent to a tax on international trade which leads to economic inefficiency and output loss.

Therefore, it is likely that global trade next year would be negatively affected by the ongoing trade war between the US and China. As a small open economy, Singapore's exports would not be immune from the global trade downturn.



The market is below its historical mean, it is also historically relatively cheap.

The banking sector remains healthy and we expect mid-single digit loans growth in 2019.

**Major economies such as the US and Europe are seeing slightly slowing growth.**

China's economy may slow more than expected given its deleveraging campaign domestically and the trade war internationally. In response to the slowdown, we expect an end to quantitative tightening in 2019. We expect the US Fed to pause its rate hikes in 2019 to ease financial conditions and avoid a hard landing as growth slows. Growth may slow more if US trade policy continues to prioritise dividing the economic pie rather than growing it. We also expect China to announce more policy-easing to support the domestic economy especially the small and medium sized enterprises.

Singapore's domestic economy is likely to perform modestly in 2019. Although underlying demand is strong, the property sector is being restrained by the government's cooling measures, which is likely to be effective in stopping the en-bloc collective sale cycle, thereby limiting both price and volume growth. The banking sector remains healthy and we expect mid-single digit loans growth in 2019.

# SINGAPORE 2019

## EQUITIES

### OUR STRATEGY



We would advocate Overweight positions on REITs, Gaming; Neutral positions on Financials, Telecommunications; and Underweight positions on Property Developers.

**In 2019, we will focus our stock picks on quality companies with attractive valuations.**

Market valuations have fallen meaningfully and this represents a good opportunity to invest in the Singapore equity market. We expect volatility to remain high, and would suggest investors remain nimble in the view of potential changes to the macroeconomic and geopolitical landscape.

We would advocate Overweight positions on REITs, Gaming; Neutral positions on Financials, Telecommunications; and Underweight positions on Property Developers.

Our most favoured sector is the REITs, as they benefit from a stable interest rate regime. We think that the US Fed is close to the end of its rate hike cycle in 2019.

We also like the fact that Office spot rents continue to rise, Chinese tourist arrivals continue to grow, and occupancy in the Retail sector continues to be high. Furthermore, the business model of REITs is relatively resilient to the trade war.

We also like the Gaming sector as results continue to be good but valuations have fallen to attractive levels, creating an opportunity to accumulate.

We are neutral on Financials, as their share prices may have priced in an expected benefit from rising interest rates that may not materialise in a slow growth environment.

For the Telecommunication sector, we are not overly pessimistic as we note that share prices have fallen to attractive levels, and a fair bit of bad news has been priced in. Incumbent telecom operators are taking action to prepare themselves for the new operating environment.

We are underweight on the Property Developers, due to the restrictive regulatory regime currently in place. Although valuations are not expensive, we remain concerned with a lack of catalysts for stock price performance going forward.

# SINGAPORE 2019

## FIXED INCOME

### OUR OUTLOOK



Singapore's economy is expected to grow by 1.5% to 3.5% in 2019, core inflation forecasted at 1.8%.

Singapore's economy grew by 2.2% YoY in the third quarter of 2018, below second quarter's 4.1% rise and the market's expectation of 2.4%. For 2018, the Ministry of Trade and Industry (MTI) expects growth to range 3.0-3.5%, near the higher end of its earlier forecast range of 2.5-3.5% in August. Along with other Asian countries, domestic inflation picked up slightly in 2018, with CPI-All Items inflation and MAS Core inflation expected at 0.7% and 1.7% respectively.

**Looking into 2019, the impact of the ongoing trade conflicts between the US and its major trading partners will likely continue.**

The impact from trade tensions and being in the late stage of the growth cycle is slow economic expansion. US growth should moderate in 2019, as the effect of the fiscal stimulus fade and monetary policy continues to tighten, mitigated with healthy private consumption and strong labour market conditions.

**In Asia, China's growth is also projected to moderate to low-6.0% in 2019 from mid-6.0% in the previous years'.** This is due to the government's de-leveraging efforts, the slowdown in the real estate market and further reduction in trade. There have been some signs of the government loosening restrictions on home purchases and deleveraging in late 2018 and we believe such piecemeal measures will continue into 2019. Outside of China, growth in the key ASEAN economies is expected to ease or remain unchanged in 2019, supported by resilient domestic demand and lower oil prices, despite slowing export growth.

**Hence, the external demand outlook for Singapore's economy slightly weakens in 2019, adding pressure to export-oriented sectors.** However, the service sector should remain resilient, supported by robust demand for IT and digital solutions. We also expect an improvement in the construction sector as a pickup in contracts translates into activities. Singapore's economy is expected to grow by 1.5% to 3.5% in 2019, while headline and core inflation is forecasted to come in at 1.5% and 1.8% respectively.

**SGS curve shifted higher with a flattening bias in 2018 in line with USTs.** Yields at the front end part of the curve increased by 15-30bps to reflect FOMC rate hikes, while the intermediate to long end increased by only 0-10bps. The SGD had outperformed its regional peers in 2018, depreciating 2.6% against the USD while the JP Morgan Asia Dollar Index has depreciated 4.64% against USD.

**For 2019, we believe the SGS curve can continue to experience flattening pressures.** As mentioned in our AxJ Local Currency Fixed Income & Currency outlook, our base case is for Fed to potentially hike once or twice through 2019. The projected hikes will likely put upward pressure on the front part of the UST yield curve which then feeds through to SGS. Meanwhile, we expect Singapore inflation to be tame, resulting in low term premium which keep the yield curve flat.



The service sector should remain resilient, supported by robust demand for IT and digital solutions.

# SINGAPORE 2019

## FIXED INCOME



We have a neutral to slightly positive view for SGD.

**For our FX outlook, MAS should keep its SNEER exchange policy stable in 1H 2019**, in anticipation of slowing growth and reduced inflationary pressures. We have a neutral to slightly positive view for SGD, as we expect USD strength to abate due to a pause in Fed hikes and lower crude oil prices and expect SGD to hover between 1.32-1.36 in 2019.

2018 has been a volatile year for the credit market. We have seen SGD bond defaults from CW Advanced Technologies, Pacific Radiance and Hyflux. Away from the distressed space, investment grade rated SGD bonds had experienced sharp sell-off too, where spreads of 5-year A and BBB rated bonds widened by 20-60bps. The spread widening is due to: (1) Weaker risk appetite in a year of geopolitical volatility and equity sell-off as the USD strengthened (2) New bond issues came cheaper progressively in USD space, causing the secondary market to reprice with the impact reflected in the SGD space.

**Gross SGD bond issuance (ex-SGS & MAS bonds/bills & CDs) reached SGD 22.6bn** as of 20th December 2018, slightly below the issuance amount last year of about SGD 25.2bn. Around 30% of them came unrated, ranging from airlines, commercial services to entertainment. Among rated issues, the majority remained investment grade, with financial and real estate issuers comprising 83% of the total rated issues.

**In the upcoming year, risk-aversion and valuation pressure from new issues should keep the secondary market weak** in 1Q of 2019. However, as valuation for SGD has become attractive after the sell-off in bonds, we are likely to turn more positive from 2Q 2019 if Fed continues its recent dovish stance and market stabilises.

Case	Assumption / Risk	Market Implications & Strategy
● <b>BAD CASE</b>	US economic data remain strong, prompting FOMC to be more aggressive in rate hikes US-China trade tensions continue to weigh on international trade Oil prices spike up toward USD 100/bbl Inflation expectations move higher	Rates curve shift higher and may experience bear steepening Asian currencies to weaken vs USD Risk-off and credit spreads widen
● <b>BASE CASE</b>	Federal Open Market Committee (FOMC) to continue its hikes in 2019 (1-2 hikes), ECB and BoJ to remain accommodative through 1H 2019 Slowing growth and reduced inflationary pressure in Asia Oil prices to remain low (USD50-65/bbl)	Curve to remain flat Continue to prefer credit over government bonds Expect MAS to keep its SNEER exchange policy stable in 1H 2019 SGD to partially recover its weakness vs USD, hovering between 1.32-1.36
● <b>GOOD CASE</b>	US economic data moderates, FOMC does not hike in 2019 Soft landing in China after marginal easing measures from the government	Yield curves likely to steepen in the front end Credit spreads tighten following better funding conditions and stabilizing economy, prefer credit over government bonds. Asian currencies to appreciate vs USD

# SINGAPORE 2019

## FIXED INCOME

### OUR STRATEGY

**Rates:** Curve likely to remain flat and may shift marginally higher following US Fed's hiking path. Prefer short-end in general but to pick up good quality longer tenor bonds selectively to lock in at higher yield levels.

**Credit:** Broadly stable with tightening potential if macro data stay within expectation and rates stay supportive. Currently stay cautious but look to add after some stabilisation in the market, potentially starting from 2Q or 2H of 2019.

**Currency:** SGD to partially recover its weakness.





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