

## AUGUST 2016

### Asia – The sun rises from the East

The bright spots in the world radiate from Asia as investors look for growth.



Asia, the name of the continent, possibly derived from the Ancient Greek word Ἀσία, which means the east bank of the Aegean Sea. Some researchers have suggested it could have Semitic root “Asu”, which means “**rising**” or “**light**”, a directional referring to the sunrise. Asia has since taken on the meaning of the ‘**Eastern Land**’ – in relation to Greece.

Asia is home to 4.4 billion people or 60% of the world’s population but only accounts for about 30% of Earth’s total land area.

Asia is more a geographic term than a homogeneous continent. Asia is subdivided into 48 countries, two of them (Russia and Turkey) having part of their land in Europe.

Asia varies greatly across and within its regions with regard to ethnic groups, cultures, environments, economics and government systems.

Source: [www.wikipedia.org](http://www.wikipedia.org)



Source: [www.pinterest.com](http://www.pinterest.com)

#### Interesting Facts

Asia has both the highest and the lowest points on the surface of Earth, has the longest coastline of any continent, is subject overall to the world’s widest climatic extremes, and, consequently, produces the most varied forms of vegetation and animal life on Earth.

Source: <https://global.britannica.com/place/Asia>

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Should you have any queries, please contact your UOB Banker for more information.

## The growth engine of the world ►►

Asia has risen steadily over the decades to become the largest contributor to world GDP from Y2005. See Fig 1. As of 2016, the largest economies in Asia are China, India, Japan, Indonesia and South Korea.

Japan was the main contributor of Asia's growth since post-World War 2. The period of rapid economic growth between 1955 and 1961 paved the way for the "Golden Sixties," the second decade that is generally associated with the Japanese economic miracle.

Economic growth in Asia since World War II to the 1990s, besides being largely concentrated in Japan, has also benefitted South Korea, Taiwan, Hong Kong and Singapore, otherwise known as the **Asian Tigers**. They have now all received developed country status and boasting one of the highest GDP per capita in Asia.

Source: Rise of Japan and 4 Asian Tigers from "emergingdragon.com"

### India and China Rising

It is forecasted that India will overtake Japan in terms of nominal GDP by 2020.

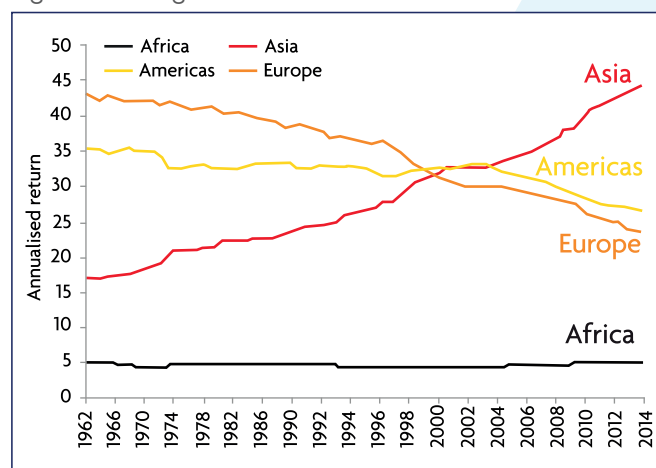
Goldman Sachs reports that China will have the largest economy in the world by 2027.

Source: Commonwealth Business Council-Asia". Archived from the original on 28 July 2007

#### Interesting Fact

In 1965, Japan's nominal GDP was estimated at just over \$91 billion. Fifteen years later, in 1980, the nominal GDP had soared 12 fold to a record \$1.065 trillion.

Fig 1: Percentage share of world real GDP



Source: www.worlddeconomics.com

Table 1: GDP of selected Asian Countries in Purchasing Power Parity terms

| Rank | Country        | GDP (Millions of Int\$) by PPP |
|------|----------------|--------------------------------|
|      | <b>World</b>   | <b>113,523,500</b>             |
| 1    | China          | 20,853,331                     |
|      | European Union | 19,205,364                     |
| 2    | United States  | 18,558,129                     |
| 3    | India          | 8,642,758                      |
| 4    | Japan          | 4,901,102                      |
| 8    | Indonesia      | 3,010,746                      |
| 13   | South Korea    | 1,848,518                      |
| 15   | Turkey         | 1,665,332                      |
| 18   | Iran           | 1,439,295                      |
| 19   | Australia      | 1,138,085                      |
| 20   | Thailand       | 1,108,111                      |

Source: IMF "Report for Selected Country Groups and Subjects (PPP valuation of country GDP)". IMF. Retrieved June 13, 2016.

Citigroup revealed 11 **Global Growth Generators ("3G")** countries; 9 came from Asia. See Table 2.

Developing Asia and Africa will be fastest growing regions until 2050, driven by population and income growth, so all of 3G countries came from the both continents (Asia by 9 countries and Africa by 2 countries) and none from the other continents.

Source: "Global Economics View/Global Growth Generators: Moving beyond 'Emerging Markets' and 'BRIC'" (PDF). 21 Feb 2011.

Note: Bigger index means better conditions. GDP per capita measured at 2010 PPP USD. Average growth is average growth in forecast of real GDP per capita measured at 2010 PPP USD.

Source: [https://en.wikipedia.org/wiki/3G\\_\(countries\)](https://en.wikipedia.org/wiki/3G_(countries))

Table 2: Global Growth Generators (3G) countries 2010–2050

| Country     | 2010 GDP/Capita | % of US GDP/Capita | % Av. Growth | 3G Index |
|-------------|-----------------|--------------------|--------------|----------|
| Vietnam     | \$3,108         | 7                  | 6.4          | 0.86     |
| China       | \$7,430         | 16                 | 5.0          | 0.81     |
| India       | \$3,298         | 7                  | 6.4          | 0.71     |
| Indonesia   | \$4,363         | 10                 | 5.6          | 0.70     |
| Mongolia    | \$3,764         | 8                  | 6.3          | 0.63     |
| Philippines | \$3,684         | 8                  | 5.5          | 0.60     |
| Iraq        | \$3,538         | 8                  | 6.1          | 0.58     |
| Bangladesh  | \$1,735         | 4                  | 6.3          | 0.39     |
| Egypt       | \$5,878         | 13                 | 5.0          | 0.37     |
| Sri Lanka   | \$4,988         | 11                 | 5.9          | 0.33     |
| Nigeria     | \$2,335         | 5                  | 6.9          | 0.25     |

## The case for Asia ►►

### 1. Growth

- In the latest IMF World Economic Outlook Update (released 19 July 2016), it is highlighted that Brexit causes 'substantial' increase in economic, political and institutional uncertainty.
- As such, global forecast for Y2017 is reduced by 0.1 percentage point, to 3.4 percent. **However, there is negligible impact to Asia because of limited trade and financial links with UK.**

Source: IMF World Economic Outlook Update, 19 July 2016.

- Except for Vietnam, Malaysia and Singapore, most parts of Asia are less vulnerable to Brexit. See Fig 2.

### 2. Asian Equities are attractively valued and under-owned.

- Asian equities had underperformed developed market equities over recent five years. MSCI Asia Pacific ex-Japan equities have been trading range-bound for the last 5 years, as earnings failed to advance.
- This also resulted in an underweight position in Asian equities from global funds over this period. At the same time, global funds piled on to Developed Market equities, making this a relatively crowded trade. See Fig 3.
- Asian equities are priced at an attractive forward price-to-earnings at 12.4 times, relative to S&P500 17.2 times (as at 30 June 2016).

### 3. Asian Credit offered a potentially less volatile journey (over the last 2 years).

- Asian credit had delivered the best returns with a relatively stable path since January 2014. See Fig 4.
- The reasons for this include a period of less defaults and a relatively lower corporate leverage ratio – a key lesson from the pains of the Asian Financial Crisis.
- With many of the developed nation bonds (especially European credit) offering ultra-low yields of less than 1 percent, investors have already started allocating to Asia – in particular **Asian Investment Grade Credits**. We feel this trend will continue in the medium term.

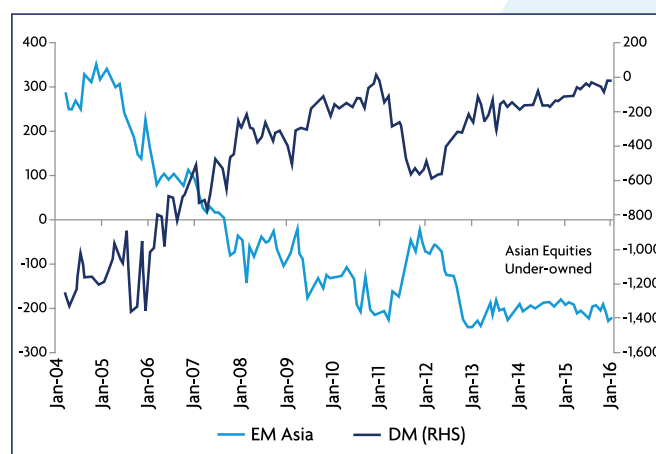
Fig 2: Asian Vulnerability to Brexit



Source: BloombergBriefs.com

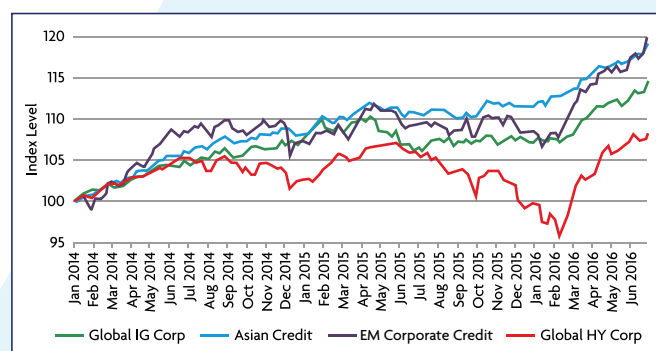
Fig 3: Asia ex-Japan equities are under-owned

Yet a rich investment universe of over 16,000 listed companies  
Global funds positioning (OW/UW vs. MSCI AC World, in bps)



Source: Goldman Sachs, February 2016

Fig 4: Asian credit offered a less volatile journey



Source: Blackrock Aladdin, June 2016.

Index levels are rebased to 100 on January 2014. Asian Credit: JPM Asian Credit Index; Global IG Corp: Barclays Global Corporates (USD Hedged); EM Corp Credit: JPM Corporate EMBI; Global HY Corp: Carclays High Yield Corporates (USD Hedged)

## What it means for investors ►►

### Recap of last month's call

- Last month, our central theme was centered on uncertainty and had advocated to remain defensive as markets seek clarity from post-Brexit.
- Within equities, we were positive on Asia ex-Japan. We were more constructive towards bonds, especially towards the higher quality issuers.

|              |   |
|--------------|---|
| Equity       | <u>Hold</u> higher quality equities. Gradually <u>add over time</u> through regular investment scheme |
| Fixed Income | <u>Add</u> higher quality bonds   |
| Alternative  | <u>Hold</u> unconstrained alternative investment strategies to lower portfolio volatility             |
| Currency     | <u>Reduce</u> GBP and EUR<br>AUD and NZD range bound<br>SGD to be well supported                      |

Source: UOB Investment Insights – July 2016

### Review of last month's strategy

- We were cautiously positioned in July, being underweight in equities. However, we were surprised with the rebound of global equities, led by Japanese and Asian equities.
- Our overweight in Fixed Income delivered positive performance as investors continue to chase yields.
- Our caution on GBP and EUR was warranted as pressure builds on these two currencies.

### Investment Perspective - August

- This month, we continue to advocate a defensive stance.

### Asia shines as a bright spot for investments.

|              |   |
|--------------|---|
| Equity       | <u>Overweight</u> Asian equities. <u>Hold</u> higher quality equities. Gradually <u>add over time</u> through regular investment scheme |
| Fixed Income | <u>Add</u> Asian bonds and higher quality bonds   |
| Alternative  | <u>Hold</u> unconstrained alternative investment strategies to diversify risks and therefore lower portfolio volatility                 |
| Currency     | <u>Reduce</u> GBP and EUR<br>AUD and NZD range bound<br>Bullish on USD  |

### Strategy for month of August

- We continue to advocate a defensive stance, seeking quality assets and to be diversified in an investment portfolio.
- Asian equities and bonds are our tactical focus.
- We feel that Asia will be least impacted by the uncertainty surrounding Brexit. In particular, the post-Brexit performance in both the Asian Investment Grade bonds and Asian equities outperform their global counterparts.

|                                | YTD          | Post Brexit  |
|--------------------------------|--------------|--------------|
| <b>Bonds</b>                   |              |              |
| Global Investment Grades       | 8.23%        | 0.04%        |
| <b>Asian Investment Grades</b> | <b>7.28%</b> | <b>1.96%</b> |
| <b>Equities</b>                |              |              |
| Global Equities                | 4.36%        | 1.01%        |
| European Equities              | -3.92%       | -4.28%       |
| <b>Asian Equities</b>          | <b>7.90%</b> | <b>6.10%</b> |

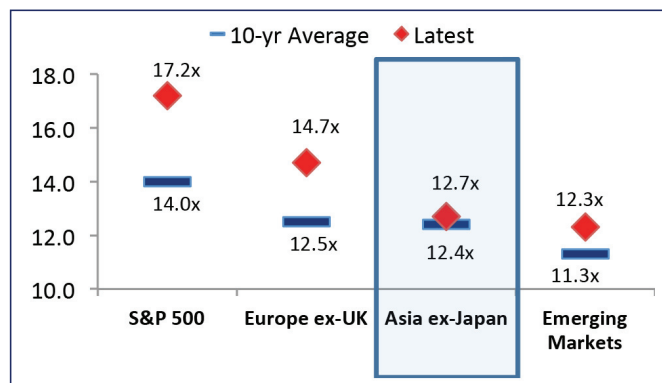
Source: Bloomberg, Barclays as at 27 July 2016. All in US Dollar.

## Equities

### Asia ex-Japan equities are attractively valued.

- We are positive on Asia ex-Japan equities.
- Asia ex-Japan equities are valued relatively cheaper compared to developed markets like US and Europe. It is also at the least overvalued versus own historical 10 year average.

Asian equity valuations are relatively attractive – Price to Earnings (Forward P/E ratios)



Source: FactSet, MSCI, Standard & Poor's, J.P. Morgan Asset Management. Guide to the Markets Asia 3Q 2016 - 31 Jul 2016. P/E ratios are in local currency terms.

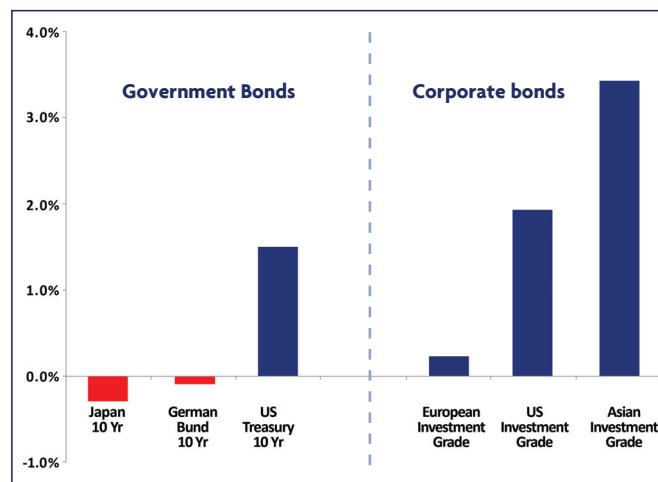
- Asian governments and central banks have recently embarked on tools to accelerate growth e.g. South Korea unveiled an US\$8.5 billion (\$11.44 billion) economic support package. Such policies should improve corporate profitability and increase shareholder value.

## Fixed Income

### Asian Fixed Income – Search for yields in a low interest world

- Asian bonds are benefitting and should continue to be well-supported by investment flows in search for yields.

Asian investment grade bonds stand out by offering higher yields than other global bonds.



Source: Bloomberg, Barclays as at 27 July 2016

- The stabilization of Chinese economic data and commodity prices are supportive of investment sentiments in Asian assets.
- We like Asian high quality bonds because their prices tend to hold up well in times of market stress.
- In addition, emerging market bonds are also attracting investors' fund flows. However investors who are not willing to accept the inherent higher risks should consider investing in Asia high quality bonds instead.
- We stress the importance of stringent credit selection and a tactical nimbleness for this opportunity.

## Currencies

### GBP and EUR still under pressure.

- We expect both GBP and EUR to remain under pressure against the USD.
- The Bank of England had cut interest rates of 25 basis points (bps) to 0.25% with a series of monetary stimulus on 4 August 2016. The Monetary Policy Committee indicated more easing is to come.
- The spill over effect of a UK recession is projected to lower Euro area growth by between 0.5-1.0 percentage point.
- Our target is for GBP/USD pair to reach 1.28 by end 3Q16 and further down to 1.24 by year-end. Our target for EUR/USD is 1.07 by year-end.

### AUD and NZD to trade range bound.

- We think that both AUD and NZD are likely to trade within a range.
- The Reserve Bank of Australia (RBA) lowered official cash rate by 25bps to 1.50% at its most recent August meeting. This move likely marks the end of further actions for some time.
- Reserve Bank of New Zealand (RBNZ) has cited weaker growth and look to possibly ease rates in August.
- However, similar to AUD, the NZD remains resilient on the back of positive carry.

### Bullish on the USD

- While the Fed kept rates unchanged in July, it commented that the labour market strengthened and near-term risks to the economic outlook have diminished.
- This brings back a revival of Fed rate hike expectations back to markets.
- We expect the Fed will hike rates at least once by year end, at the 13/14 December meeting.
- This should give rise to USD strength and we target USDSGD at 1.38 by year end.

## Alternatives

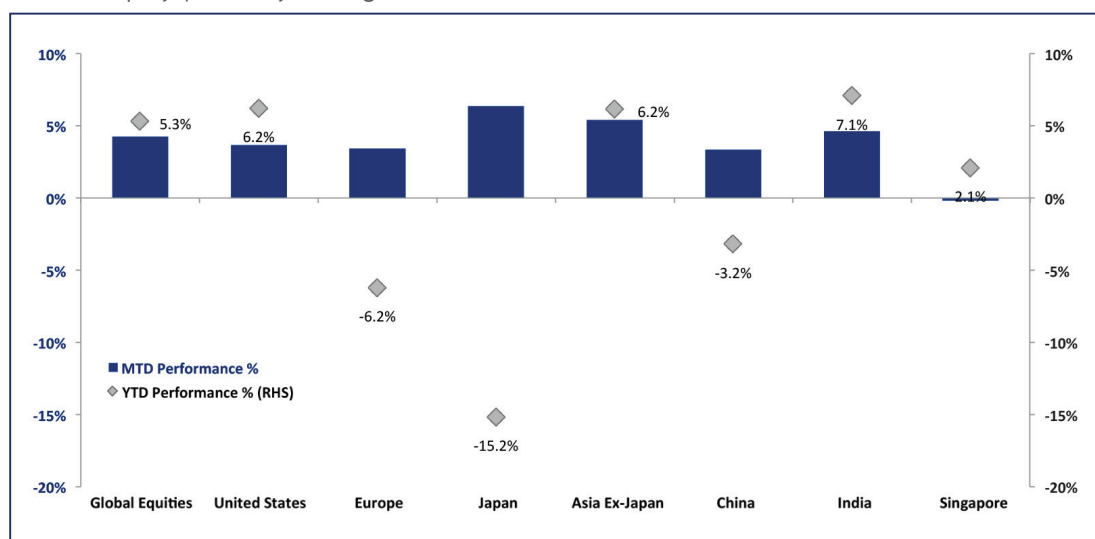
### Unconstrained strategies help to reduce overall portfolio volatility, whilst benefiting from global macroeconomic trends

- Unconstrained strategies aim to generate positive performance in varying market conditions by seeking out opportunities in times of market dislocations or volatilities.
- These strategies tend to have low correlations to traditional asset classes like equities and bonds. This helps to diversify portfolio risks efficiently.



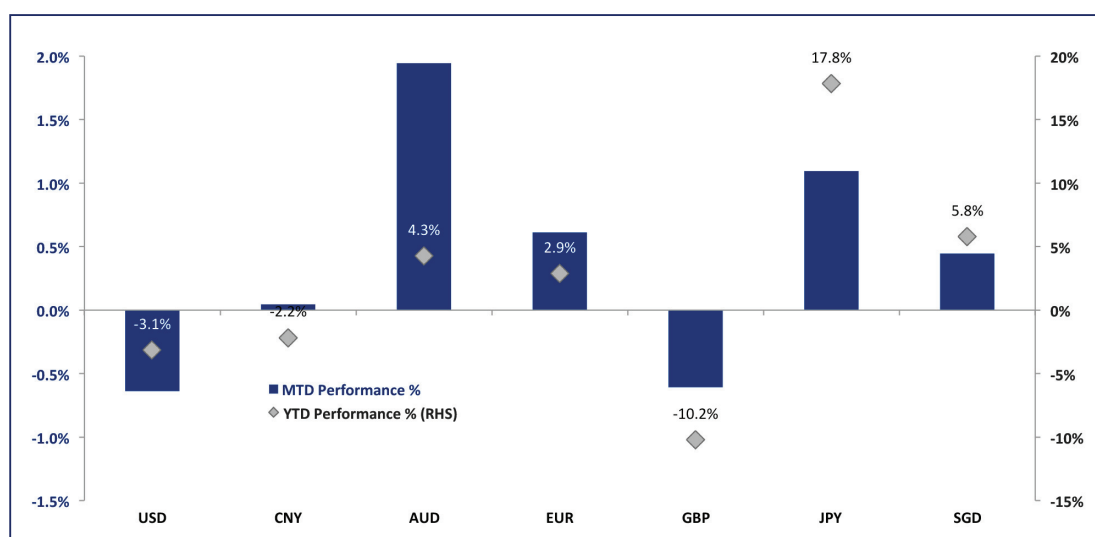
## Global Markets Performance Recap ►►

Chart 1: Equity | Country or Region



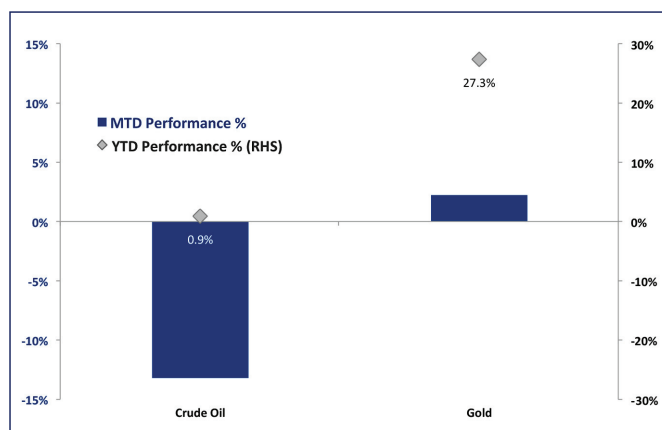
Source: Bloomberg as at 30 July 2016. Equity Indices all from MSCI  
\* 30 June 2016 to 30 July 2016

Chart 2: Currencies



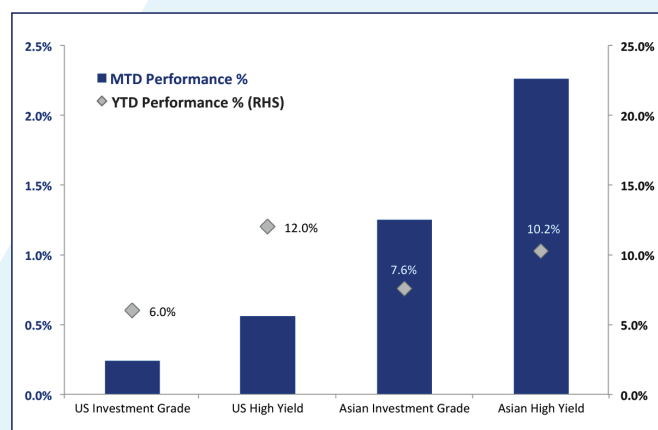
Source: Bloomberg as at 30 July 2016.  
\* 30 June 2016 to 30 July 2016

Chart 3: Commodities



Source: Bloomberg as at 30 July 2016.  
\* 30 June 2016 to 30 July 2016

Chart 4: Credit



Source: Bloomberg as at 30 July 2016.  
\* 30 June 2016 to 30 July 2016

## Summary of UOB Investment Views ►►

| Asset Class                                    | -- | - | N | + | ++ |
|--|----|---|---|---|----|
| Equities                                       |    |   |   |   |    |
| United States                                  |    |   | • |   |    |
| Europe   |    | • |   |   |    |
| Asia (ex. Japan)                               |    |   |   | • |    |
| Japan  |    |   | • |   |    |
| Eastern Europe, Middle East and Africa (EEMEA) |    |   | • |   |    |
| Fixed Income                                   |    |   |   |   |    |
| Developed Markets Sovereign                    |    | • |   |   |    |
| US Investment Grade                            |    |   |   | • |    |
| US High Yield Bonds                            |    |   | • |   |    |
| Emerging Market USD Bonds                      |    |   |   | • |    |
| Emerging Market Local Currency Sovereign Bonds |    |   | • |   |    |
| Commodities                                    |    |   |   |   |    |
| Gold   |    |   |   | • |    |
| Base Metals                                    |    | • |   |   |    |
| Agriculture                                    |    |   | • |   |    |
| Energy   |    | • |   |   |    |
| Cash   |    |   |   |   |    |

Source: UOB Private Bank – July 2016

### UOB Global Foreign Exchange Outlook

| FX Outlook | 3Q16 | 4Q16 | 1Q17 | 2Q17 |
|------------|------|------|------|------|
| EUR/USD    | 1.09 | 1.07 | 1.06 | 1.05 |
| GBP/USD    | 1.28 | 1.24 | 1.20 | 1.16 |
| AUD/USD    | 0.75 | 0.76 | 0.78 | 0.80 |
| NZD/USD    | 0.72 | 0.73 | 0.75 | 0.75 |
| USD/JPY    | 105  | 106  | 109  | 110  |
| USD/SGD    | 1.37 | 1.38 | 1.41 | 1.42 |

### UOB Regional Asia Foreign Exchange Outlook

| FX Outlook | 3Q16   | 4Q16   | 1Q17   | 2Q17   |
|------------|--------|--------|--------|--------|
| USD/MYR    | 4.15   | 4.15   | 4.10   | 4.08   |
| USD/THB    | 36.0   | 36.5   | 37.0   | 37.0   |
| USD/CNY    | 6.70   | 6.60   | 6.59   | 6.62   |
| USD/IDR    | 13,200 | 13,200 | 13,300 | 13,400 |
| USD/PHP    | 47.0   | 46.0   | 45.0   | 43.0   |
| USD/INR    | 70.0   | 71.1   | 72.2   | 71.1   |
| USD/TWD    | 32.3   | 32.4   | 32.1   | 31.8   |
| USD/KRW    | 1,190  | 1,200  | 1,220  | 1,230  |

Source: UOB Global Economics & Markets Research, 30 Jun 2016





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» For 2016, we recommend investors to S.I.F.T. through a year where global transformations shape our world. «

## **S**elective on Investment Opportunities.

We currently favour Asian equities as the region's growth continues to be amongst the highest in the world and valuations are relatively attractive. In Asia, our preference is China H-shares, India, Indonesia and South Korea.

## **I**dentify Quality and Value.

For equities, Value is preferred over Growth, as evidenced in the past tightening cycles. For fixed income, we prefer Asian higher quality Investment Grade credit over Developed Markets (DM) due to the higher yield over similar rated securities in the DM space.

## **F**ocus on a Risk-Managed Portfolio.

Be prepared for higher bouts of volatility. Build a stable core portfolio. This allows investors to stay anchored amidst the volatility.

## **T**ake note of Consensus Trades.

Momentum reversal can happen quickly. Consensus views such as the recent UK referendum that resulted in Brexit can quickly reverse and surprise the market. However, these risks can also open doors to new opportunities.



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