

4Q2020 **OUTLOOK & STRATEGY**

Cloudy Vision **20/20** >>



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3Q2020 ASIA EX-JAPAN MARKET REVIEW

The stimulus-driven rebound continued through to most of 3Q2020 but with some correction in equity markets in September. **Government stimuli have exceeded the amounts seen during the Global Financial Crisis in 2008, providing relief to economies that were forced to shut down to contain the COVID-19 virus** (chart 1). Ever-rising COVID-19 cases in the US and second wave fears elsewhere (e.g., Hong Kong, Australia) were counterbalanced by seemingly good progress of vaccines under development (Chart 2) as well as expectations of the extended stimulus.

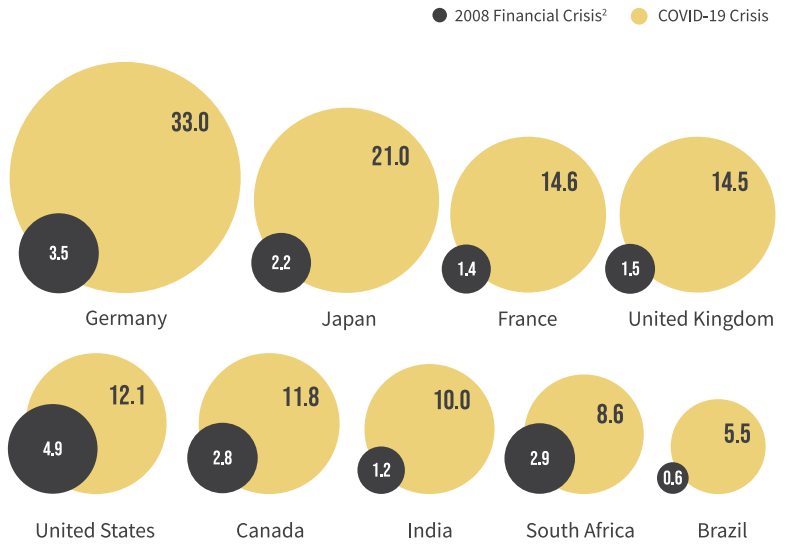
The rally was also aided by a weaker USD coupled with expectations that US rates would remain ‘lower for longer’ as the Federal Reserve (Feds) adopted a more relaxed inflation target. US-China tensions continued to simmer with additions to the Huawei-affiliated blacklist, US sanctions on senior Chinese/Hong Kong government officials and the TikTok ban, amongst others.

Following a stellar run in markets and given elevated valuations, equity investors took some profit off the table in September. Amidst recovery hopes, **there were some rotation from COVID-19 beneficiaries (e.g., tech, healthcare) into beaten-down COVID-19 losers (e.g., industrials, hospitality). Sentiment also turned more cautious given the risks of a disputed outcome in the upcoming US Presidential election in November that increasingly appear ‘too close to call’.** In addition, there were concerns that the US economic recovery might still be some time away as stalled negotiations between Democrats and Republicans on another round of COVID-19 aid diminished hopes that such relief would be soon forthcoming.

Similar to the equity markets, Asian USD Fixed Income also continued its strong recovery from 2Q2020 into 3Q2020 but lost some steam in September. For 3Q2020, the JP Morgan Asia Credit Index (JACI) delivered about 2% in total returns, with 1.90% from investment grade and 2.3% from non-investment grade bonds. The weakness during September was mainly from

non-investment grade bonds, which peaked at 5% total returns during the quarter in the first week of September but lost more than half the returns to end at 2.3% for 3Q2020. For YTD ending September, JACI was up 4.3% with investment grade bonds driving majority of the returns (+5.5%) while non-investment grade bonds underperformed with total returns less than (1%).

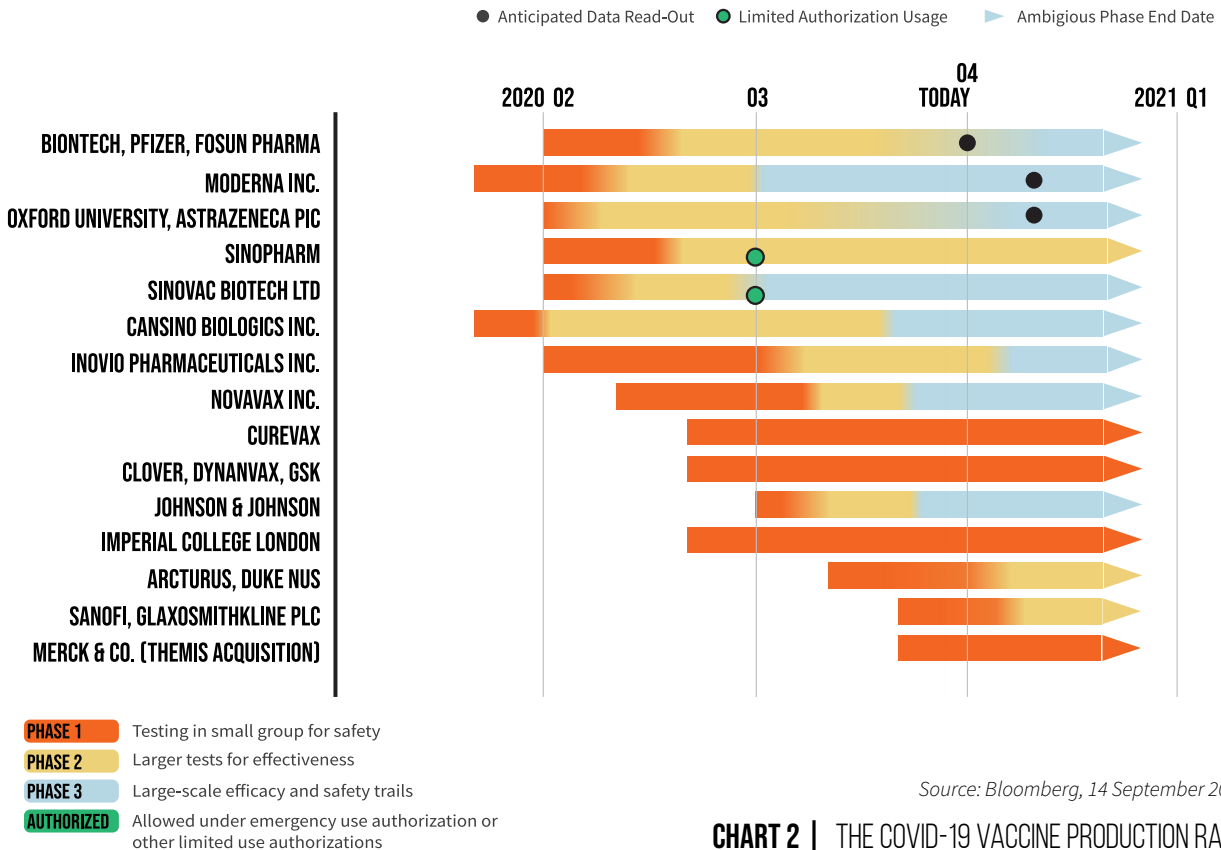
Bond markets started experiencing volatility from the second half of August onwards. **Markets were disappointed with the lack of further stimulus from the government on top of the lack of evidence that the Feds would be implementing any yield curve control.** Long end Treasuries sold-off and credit spreads widened. At the **September Jackson Hole meeting, the Feds announced the change from inflation target of 2% to targeting average inflation of 2%.** This meant that the Feds is willing tolerate higher inflation in the future. **The Fed Dot Plot also suggested that there would be no interest rate hike until end of FY2023.** While this anchored short end rates, long end bonds continued to trade weak as markets focused on inflation fears. During September, Trump continued to attack China and caused credit spreads to widen. Both China and India high yield bonds sold off.



Source: McKinsey & Co, IMF, June 2020.

CHART 1 | ECONOMIC STIMULUS AS A % OF GDP

Long end Treasuries sold-off and credit spreads widened. At the **September Jackson Hole meeting, the Feds announced the change from inflation target of 2% to targeting average inflation of 2%.** This meant that the Feds is willing tolerate higher inflation in the future. **The Fed Dot Plot also suggested that there would be no interest rate hike until end of FY2023.** While this anchored short end rates, long end bonds continued to trade weak as markets focused on inflation fears. During September, Trump continued to attack China and caused credit spreads to widen. Both China and India high yield bonds sold off.



Source: Bloomberg, 14 September 2020

CHART 2 | THE COVID-19 VACCINE PRODUCTION RACE

OUR 2020 INVESTMENT THEMES

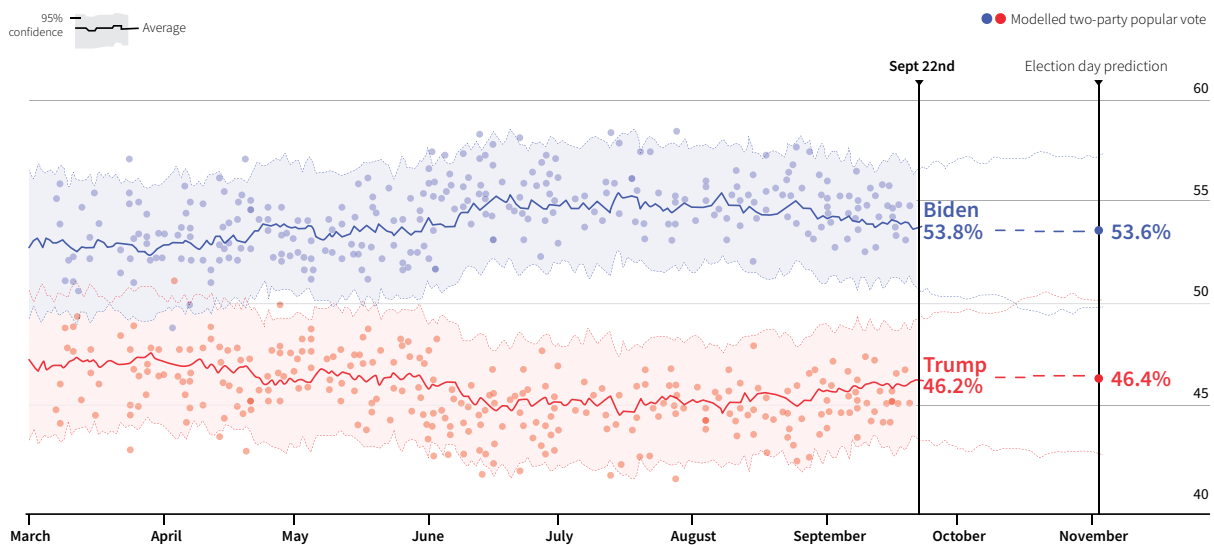
KEY THEMES	OUR ASSESSMENT	MARKET IMPLICATIONS & STRATEGY
Global Growth Uncertainty	<ul style="list-style-type: none"> • A recession in 2020 with growth picking up in 2H2020 as lockdowns end. • Growth uncertainty to persist with COVID-19, politics and trade policy being unpredictable swing factors. • Policy makers look to boost their domestic economies via fiscal spending. • Positive factors: supportive monetary/fiscal policy. • Negative factors: corporate decision- making/ investment slows as consumption decelerates (on diminished confidence and cash preservation). 	<ul style="list-style-type: none"> • Favour a trading-oriented/tactical stance. • Favour fixed income over equities on better risk- reward. • Expect dividend cuts. • Focus on structural themes that are less dependent on global macro- economic conditions e.g., 5G, technology change/ trends, policy beneficiaries. • Favour Asian currencies and gold over USD.
Continuing Trade Tension and Tech War	<ul style="list-style-type: none"> • US protectionist trade stance and global trade tension to remain an overhang. • Meaningful US-China trade war resolution unlikely as underlying issues extend beyond the economics of trade. • Ongoing US-China tech war to continue given US/ China rivalry, national security and intellectual property concerns etc. • Corporates hedge against the risk of rising trade friction by reconfiguring regional supply chains. • Risk of trade friction broadening out to other countries (e.g., on currency manipulation accusations, re-routing of trade flows to circumvent tariffs). 	<ul style="list-style-type: none"> • Favour a trading-oriented/ tactical stance. • Favour beneficiaries of production shifts away from China. • Focus on more domestic demand stories as it will be less exposed to global supply chain disruptions from the US-China tensions.
Accommodative Monetary Policy	<ul style="list-style-type: none"> • Monetary policy to remain accommodative globally amidst benign inflation as governments focus on stimulating growth and preserving jobs. • Interest rates expected to remain low for longer. • Expect a weaker USD. We are bearish on USD from a medium term perspective as Fed's Balance sheet expansion will continue till 2021. • Negative output gaps (given excess capacity) and economic worries (weakening demand) to keep inflation subdued. 	<ul style="list-style-type: none"> • Markets are unlikely to re- visit the drastic sell-off levels in March given supportive liquidity environment. • Bullish on duration for fixed income. • Favour long-end sovereign and quasi-sovereign bonds. • Prefer selective Asian currencies over USD like THB, SGD, IDR and INR • We like gold as an asset class due to very low to negative rates globally and higher fiscal stimulus across the globe.
More Volatility; Geopolitics Matter	<ul style="list-style-type: none"> • Markets to remain volatile given uncertainty thereby requiring nimble trading. • Sources of geopolitical risk include, amongst others: US Presidential elections, US-China tensions, North Korea, Brexit, Latin America/Middle East political instability etc. 	<ul style="list-style-type: none"> • Bullish on duration for fixed income. • Favour long-end sovereign and quasi-sovereign bonds.

OUR 4Q2020 ASIA EX-JAPAN EQUITY OUTLOOK & STRATEGY

As mentioned in our 3Q2020 outlook, there appears to be a disconnect between financial markets and economic reality with markets rallying despite a weak economy, thanks to fiscal and monetary policy support from governments and central banks. Markets have largely ignored concerns such as rising COVID-19 cases and heightened US-China tensions, resulting in the MSCI Asia ex-Japan index recovering to pre-pandemic levels. The pace and quantum of the equity market rebound had been remarkable considering

that the global economy remains weak albeit with some recovery in economic activities post-lockdowns.

Given the rally, **Asian equities are now trading at an elevated 15X forward P/E (versus historical average of 12X). From a fundamental standpoint, we would view the risk-reward as being unattractive considering the geopolitical risks.** While Biden is leading the polls for the moment (See Chart 3), there have been concerns that Trump supporters have been



Source: *The Economist*, 22 Sept 2020

CHART 3 | FORECASTING THE 2020 US PRESIDENTIAL ELECTIONS

avoiding polls therefore rendering current polls an inaccurate gauge of the upcoming elections. In the event of a Biden win, equity markets would likely to react negatively as corporate tax rates would rise thereby crimping earnings. We believe markets will be volatile in the run-up to the US Presidential elections in November. **We are neutral on equities despite the concerns as stimulus will provide support on**

Asian equities but still prefer to have more cash (i.e, c.10%-15%) in our portfolios. We favour more domestically- oriented stocks as well as those with structural drivers beyond COVID-19. Now we are also looking at selected stocks that have been hit hard by COVID-19 but which, would recover in 2021 once a vaccine is found (e.g., travel-related stocks).

OUR 4Q2020 ASIA EX-JAPAN FIXED INCOME OUTLOOK & STRATEGY

As we enter 4Q2020, we can identify several key political risks that will cause volatility to the financial markets. We have the continued US-China cold war, the upcoming US Presidential Election as well as the risk of a no-deal Brexit by end-2020. This is on top of the pandemic that we are still facing globally and whether we can continue to open the economy gradually as we enter the winter season.

In the face of these risks that occupy headlines on a daily basis, it is very easy to forget that there are some basic fundamentals that anchor well for bond investments currently.

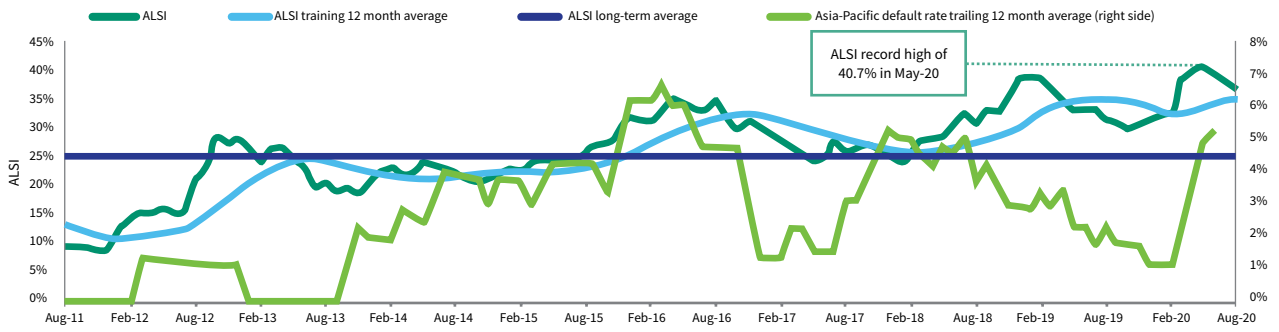
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First, **bond returns are generally affected mainly from interest rates and credit spreads.** Due to the likely prolonged weakness in growth caused by the global pandemic lockdowns, the US Federal Reserve has committed to keep interest rates low for the next three years till end FY2023. As for inflation, we believe that the risks are low, given that the inflationary pressures in the past few months were due to supply chain disruptions, rather than demand. With increasing job losses and uncertainties on when economies can fully re-open, we are not confident consumer spending (demand) would increase anytime soon. **Low interest rates and low inflation would be positive for bond investments.**



2

Secondly, **default rates may have peaked and are trending lower.** International rating agency Moody's predicted in April that the default rates for Asia would increase to 6% for FY2020 from below 2% previously. This is lower than their forecasted default rates for US and Europe and 13% and 7%, respectively. While we are aware that default risks are higher, we are able to manage this risk by investing in higher rated bonds and avoiding weak rated bonds (majority of the defaults occur in single B rated issuers or below). In addition, central banks in the US, Europe and India have rolled out supportive financing programs such as bond purchasing programs and government standby guarantees for loans to private companies. These programs have injected the much-needed liquidity boost to private businesses during this highly stressful period. Moody's monitors liquidity stress as one of the main triggers for defaults. While liquidity stress has increased for Asia during 2Q2020, they observed that the Asian Liquidity Stress Indicator "ALSI" (dark green line) peaked in May and has been on a down trend since June through August. With liquidity stress diminishing as economies reopen, default rates (light green) may have peaked and could trend lower going forward.



Note: Long-term average is from 1 September 2010 to 31 August 2020. Source: Moody's Investors Service

CHART 4 | ASIAN LIQUIDITY STRESS INDICATOR

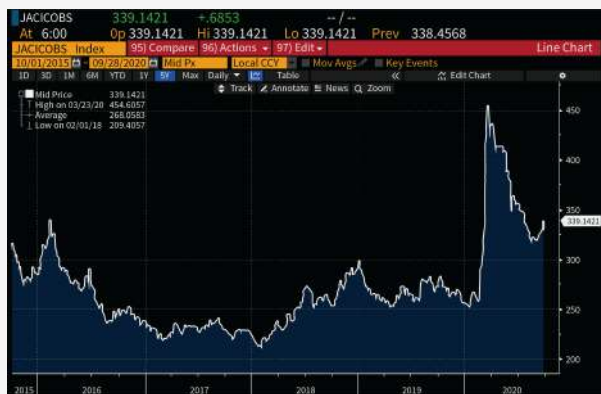
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Thirdly, **while default rates are expected to be higher, we are being compensated to manage this risk.** Bond spreads are currently wider than the five-year average. As we get past this quarter of US Presidential Election and Brexit risks, and as economies continue to re-open more next year, with hopefully a successful vaccine and treatment in place, credit spreads should tighten in again towards the average and bond prices could rally.

Relative to the US and Europe, Asia “High Yield” (HY) are currently trading at higher yields with lower default rates as predicted by Moody’s highlighted under the second key risk. **Therefore, under a risk-adjusted basis, we are being paid more to take on risk in Asian USD credit bonds.**

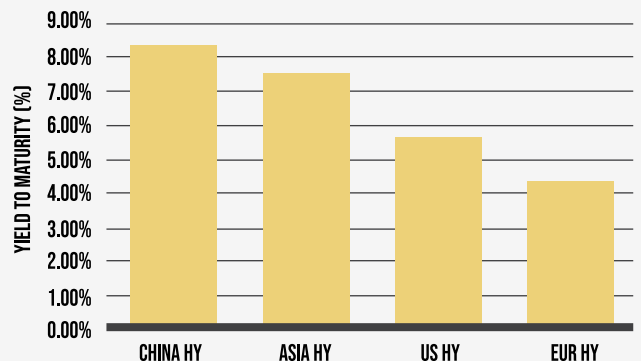
We still expect higher volatility going into the last quarter of FY2020. However, we do not expect to revisit the magnitude of sell-offs experienced in March this year due to the global COVID-19 lockdowns. **The macro fundamentals are supportive for bond investments for the next few years and we continue to expect 4% to 5% returns annualised, which is attractive for investors in the current low rate environment.**

Asian bonds are also offering higher yields for lower expected default rates relative to US and Europe. Therefore, we encourage Investors to remain invested as we expect a more stable environment in FY2021.



Source: Bloomberg as at 28th September 2020

CHART 5 | CREDIT SPREADS SHOULD NARROW TO AN AVERAGE LEVEL OF 270BPS BY FY2021



SOURCE: BOXX, YIELD BOOK, MORGAN STANLEY RESEARCH

Source: Bloomberg as at 28th September 2020

CHART 6 | ASIA HY AND CHINA HY YIELD ARE THE WIDEST IN GLOBAL CREDIT

ASIAN LOCAL CURRENCY GOVERNMENT BONDS & FX

On another note, Asian local currency bonds did well and returned about 3.52% mainly from yield compression and FX gains.

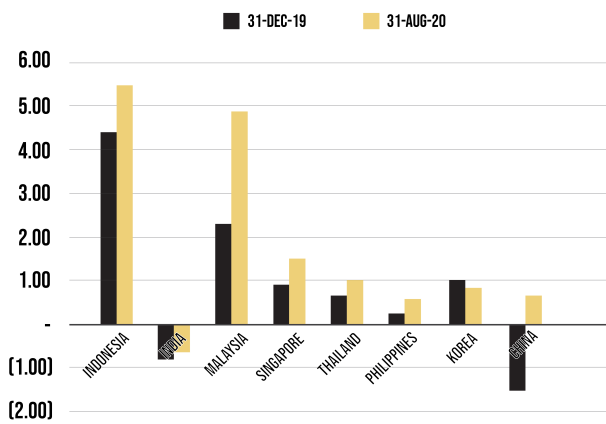
Going forward in the 4Q2020, we do not expect any rally in government bonds. Hence, we stick to short duration mainly for carry and currency appreciation.

We believe that most Asian central banks' rate cut cycle is over and we expect Asian curves to steepen in overall, due to higher fiscal deficit and less room

for further rate cuts. However, given the real yield is still positive across Asia and us expecting Asian currencies to continue its strong performance after the US elections mainly due to weaker dollar, we are neutral on local bonds for 4Q20. We continue to like IDR, CNY, KRW and MYR bonds for their high real yields.

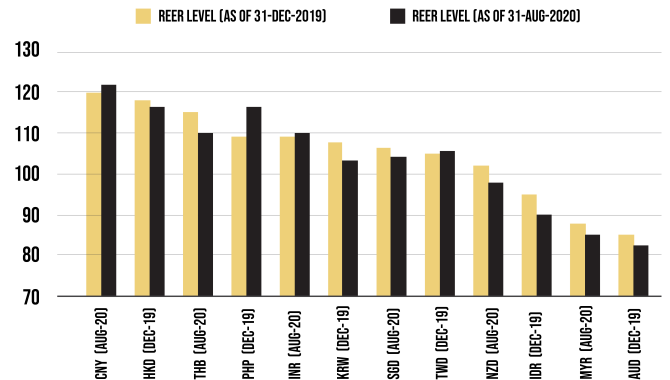
For currencies we prefer IDR, MYR, SGD and CNY from a medium-term perspective.

3Q20: ASIAN LOCAL CURRENCY REAL YIELDS AND REAL EFFECTIVE EXCHANGE RATE CHANGE



Source: Maybank Asset Management, August 2020

CHART 7 | 10 YEAR LOCAL GOVERNMENT BOND REAL YIELD



Source: Maybank Asset Management, August 2020

CHART 8 | REAL EFFECTIVE EXCHANGE RATE CHANGE

SUMMARY ON ASIA LOCAL CURRENCY BOND & FX

	INTEREST RATE	FX
INDONESIA	OVERWEIGHT	OVERWEIGHT
PHILIPPINES	MARKETWEIGHT	MARKETWEIGHT
INDIA	MARKETWEIGHT	MARKETWEIGHT
CHINA	OVERWEIGHT	OVERWEIGHT
SOUTH KOREA	OVERWEIGHT	MARKETWEIGHT
SINGAPORE	MARKETWEIGHT	OVERWEIGHT
THAILAND	MARKETWEIGHT	MARKETWEIGHT
MALAYSIA	OVERWEIGHT	OVERWEIGHT

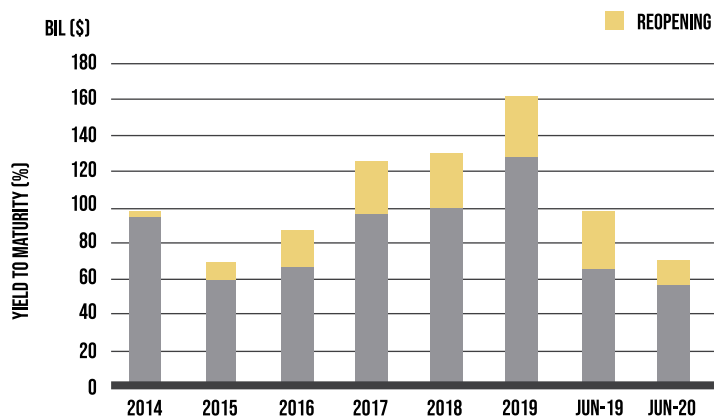


OUR 4Q2020 GLOBAL SUKUK OUTLOOK

Global Sukuk as an asset class outperformed conventional bonds in 3Q2020, with both Dow Jones Sukuk Index and Bloomberg Barclays EM GCC Sukuk returning 2.68% to 2.85% in this period. This contrasts with JP Morgan Asia Credit Index of 2.49% and JP Morgan EMBI MENA sub-index at 2.43%. Market sentiment remained supportive till late August but turned progressively negative over September, given a mix of resurgent COVID-19 cases in Europe, negotiation deadlock on a new US fiscal stimulus, doubts over the pace of economic recovery and the pullback in the equity markets. Still, Global Sukuks managed to return about +0.1% MTD as compared to JACI and EMBI MENA where the returns were at -0.1% to -0.5%, respectively.

This speaks of Sukuks’ resiliency given the strong liquidity conditions and pent up demand albeit limited supply growth given in part due to the structural complexity of Sukuks vs conventional bonds. Issuances of sukuku globally in 2020 would likely see a decline compared to the USD160bn seen in 2019. In 1H2020, sukuk issuances totalled to USD70bn, lower than USD 100bn issued in 1H2019. Other than the relative ease of access via conventional debt markets vs Sukuks, GCC banks’ also reduced funding needs in light of COVID-19’s impact. Hence, reduced their need to tap onto the Sukuk markets.

Looking into 4Q2020, we expect heightened volatility in the Sukuk markets due to the US elections and general macro weaknesses. Therefore, **we are neutral on Global Sukuk and we prefer investment grade (IG) over high yield (HY) sukuku.** Credit spreads of GCC investment grade names remain wide relative to EM peers despite the recovery. With the low UST yields environment to persist, Sukuks as an asset class remains attractive for good carry.



Source: S&P Global Ratings, Eikon, Maybank Asset Management Singapore

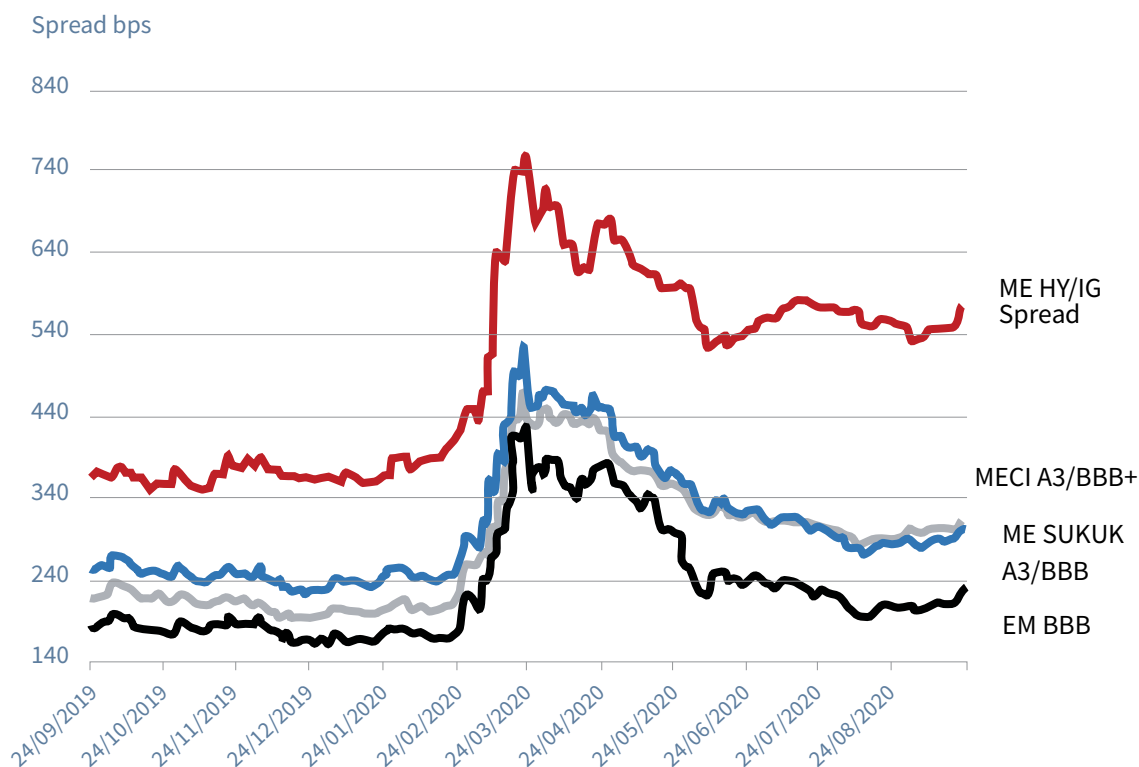
CHART 9 | SUKUK ISSUANCE VOLUME WILL REMAIN DEPRESSED

Generally, we favour IG names over HY. Despite the HY GCC property sukuku enjoying a rebound since March, valuations are now expensive considering the oversupply situation, made worse from the COVID-19's fallout. **In the IG space, we continue to favour financials given high government ownership/support and yet having good spread pick up over the sovereign.**

For local currency sukuku, we prefer MYR MGII over IDR INDOIS at this juncture. Even though real yields remain positive, **we are not comfortable with the weakness in USD/IDR due to Bank Indonesia's independence and the need to help fund deficits beyond 2020.** Still, the external funding environment remains benign as FX swap points remained stable while spot currency weakened. Hence, we remain positive over IDR in the medium term and we believe offshore investors' interest will return. **We prefer Malaysia as positive real yields remain amidst negative inflation and improved foreigner participation in the domestic bond market.**



For crude oil, we expect prices to continue to range in the USD 40-50/bbl throughout 4Q2020 as softer demand outlook is countered by the expectation of a weaker USD and higher inflation expectations.



Source: Azimut Asset Management, Maybank Asset Management Singapore

CHART 10 | SUKUK CREDIT SPREAD OVER TIME

GLOBAL SUKUKS : RECOMMENDATIONS

Malaysia	<ul style="list-style-type: none"> • Current Account to deteriorate slightly given lower oil prices (USD 40/bbl for 2H2020) and lower trade from COVID. • MYR outperformed in 3Q20 given increased flows and cheap valuations. USDMYR to range 4.10 to 4.20 over 4Q20. • Prefer short end MGII for carry and currency appreciation potential given flat curve; avoid duration given the potential for increased supply. • Market weight on USD Malaysia sovereign, SOE Sukuks, continue to like local currency Sukuk with periodic MYR weakness as an opportunity to add.
Indonesia	<ul style="list-style-type: none"> • IDR to stay 14,500 to 15,000 over Q420 though external funding remains benign. • Prefer short-dated IDR Sukuks for carrying as increased sovereign funding needs may drive domestic yield curve steeper; 10-year yield forecasted at 7.5-7.6% by year-end from 7.10% now. • Inflation is expected to remain stable and IDR real yields remain positive, BI likely done with rate cuts with policy rate now at 4%. • Market weight on both USD and IDR INDOIS Sukuks.
Saudi Arabia	<ul style="list-style-type: none"> • Market weight on KSA Sovereign Sukuks. • Supply of sovereign conventional bonds and Sukuks can be absorbed given JPM Index Inclusion. • Prefer IG over HY Saudi names as an increase in the VAT rate to 15% from 5% effective on July 2020 is likely drag on consumers and corporates.
UAE	<ul style="list-style-type: none"> • Residential real estate market might have bottomed but any recovery is likely to be slow. • Rescheduling of Expo 2020 into 2021 to delay recovery. • In the UAE HY space, overweight bank AT1 for carry given the expectation of profitability and strong capital ratios even as NPLs build up; First Abu Dhabi bank calling their AT1 perp in May gives confidence to this sector in contrast to European bank AT1 sector. • Overweight financials given strong government ownership/support and sovereigns as UAE best positioned to weather this current oil price downturn.
Qatar	<ul style="list-style-type: none"> • Market weight on Sukuks issued by Qatari financials. • Overall Sukuk supply from Qatar should remain limited in 2020.
Oman	<ul style="list-style-type: none"> • Market weight OMAN USD Sukuks despite tight valuations as impending supply should be well absorbed; Government's overfunded position in 1H20 is the main reason for low supply. • Downgrade risks remain high given increased strain to budget on lower oil prices.
Bahrain	<ul style="list-style-type: none"> • Bahrain's sovereign and quasi-sovereign conventional bonds and Sukuks to remain supported despite tight levels for its B+ rating. It has strong support from Saudi and UAE. • Government's fiscal position set to improve given existing reforms in place and USD 10 billion support package from UAE and Saudi. • Overweight on BAHRAIN's USD sovereign Sukuks as yield is attractive for carry. Opportunity to add on weakness.
Turkey	<ul style="list-style-type: none"> • Underweight USD TURKSK Sukuks on tight valuations and high susceptibility to geopolitical risks. USDTRY among the worst performers among EM FX.
Kuwait	<ul style="list-style-type: none"> • Continue to like Kuwaiti Banks AT1 perps for carrying given limited supply vs UAE banks. • Kuwait's credit rating downgrade to A1 Stable by Moody's. Neutral on Kuwait.



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