Maybank Investment Strategy

Third Quarter 2022

Summary

- It remained a challenging environment for risk assets in 2Q22. Inflation continued to surprise on the upside leading to more aggressive monetary tightening that is weighing on growth. Notably, recession fears are on the rise amid lingering geopolitical uncertainties including the Russia-Ukraine conflict.

- Unsurprisingly, global equities, as represented by MSCI All-Country (AC) World Index retreated 15.5% in 2Q, with Taiwan and South Korea leading the retreat. However, China rebounded in June on the back of improving macro data and supportive government policies, and ended the quarter on a positive note.

- Meanwhile, the 10-year U.S. Treasury (UST) yield surged to a high of 3.5% before retreating to current levels of 3.0%. Credit spreads also widened, reflecting the rising concerns on growth and potential default. The economic uncertainties also dampened the upward surge in oil prices but limited the fallout in gold that was affected by the higher Treasury yields and a stronger dollar.

Asset Allocation

- We remain cautious on the macro outlook. While inflation may peak in the coming quarter, it will likely take time to normalise. As such, central banks around the world, including the U.S. Federal Reserve (Fed), will have to remain hawkish to combat inflation.

- The tightening financial conditions will no doubt negatively impact growth and risk causing a recession. With diminishing prospects of a soft landing, we see further downside to the global economy as well as corporate earnings. In view of the above, we maintain a prudent stance in our asset allocation.

- On equities, we remain underweight with Europe as our least preferred market. As for fixed income, we continue to prefer the more defensive Investment Grade (IG) bonds to High Yield (HY) credits with the latter being more vulnerable in a downturn. While we remain neutral on sovereign bonds, the risk reward is no doubt improving relative to the start of the year.

- We expect gold to trade range-bound but would maintain some exposure in the precious metal as a hedge against the growth uncertainties. In comparison, while oil prices may remain supported by supply constraints, the upside will likely be capped by a weaker economic growth and oil demand recovery.

3Q22 Outlook			
Asset Class *		**Sector ***	
Equity	-	U.S.	=
		Europe	-
		Japan	=
		Asia ex-Japan	=
Bonds	=	Sovereigns	=
		Developed Markets (DM) Investment Grade (IG)	=
		Developed Markets (DM) High Yield (HY)	-
		Emerging Markets (EM) IG	=
		Emerging Markets (EM) HY	-
		Asia IG	+
		Asia HY	=
Alternatives	=	Gold	=
		Oil	=
		Hedge Funds	=
Cash	+		

Source: Maybank Group Wealth Management Research
* Overweight : +, Neutral : =, Underweight : -

Asset Class	Changes to date (in USD currency)		
	Month	Quarter	Year
Equity			
MSCI USA	-8.3%	-16.8%	-21.1%
MSCI Europe	-9.9%	-14.2%	-20.4%
MSCI Japan	-7.9%	-14.6%	-20.1%
MSCI Asia ex-Japan	-4.4%	-8.9%	-16.1%
China	6.6%	3.5%	-11.2%
Hong Kong	1.2%	-1.1%	-2.9%
Taiwan	-14.0%	-19.6%	-24.8%
South Korea	-17.0%	-20.8%	-28.3%
India	-6.7%	-13.5%	-15.1%
Singapore	-7.5%	-16.8%	-18.2%
Malaysia	-8.2%	-12.8%	-11.1%
Indonesia	-9.2%	-8.8%	0.2%
Thailand	-8.4%	-10.5%	-6.7%
Philippines	-13.6%	-19.4%	-17.5%
MSCI EM	-6.6%	-11.3%	-17.5%
Bonds			
Barclays US IG	-2.8%	-7.3%	-14.4%
iBoxx US HY	-6.7%	-9.8%	-14.2%
Commodity			
Gold	-1.6%	-6.7%	-1.2%
Oil	-7.8%	5.5%	40.6%

Source : Bloomberg | 30 June 2022

Maybank Investment Strategy

Third Quarter 2022 - Bonds

Summary

- Total returns for global bonds were negative in June and for the quarter, weighed down by rising yields (Figure 3) and widening credit spreads. Notably, the Fed has pivoted several times with its policy guidance, leading to elevated market volatility.

- With U.S. consumer price index jumping 8.6% year-on-year (YoY) for the month of May, inflationary pressure has shown little sign of moderation. Consequently, the Fed had no choice but to raise rates by 75 basis points (bps) in June – the biggest increase since 1994 - and vowed to forcefully tackle inflation.

- According to the latest Fed's "dot plot", the central bank's median projection is now signalling policy rate at 3.375% and 3.75% by the end of 2022 and 2023, respectively (Figure 4). This implies another 175 bps of tightening this year and 38 bps next year.

Market Outlook

- The pace of policy tightening will remain intense over the coming months. Even the European Central Bank (ECB) is catching up with other central banks and will likely raise interest rates in July for the first time in 11 years. Should U.S. inflation stay higher-than-expected, markets will also have to adjust their Fed rate expectations higher again.

- In view of the above, the path to a soft landing has become more challenging and the re-inversion of the 2-year and 10-year UST yield curve in June – a recession indicator - is flashing warning signs.

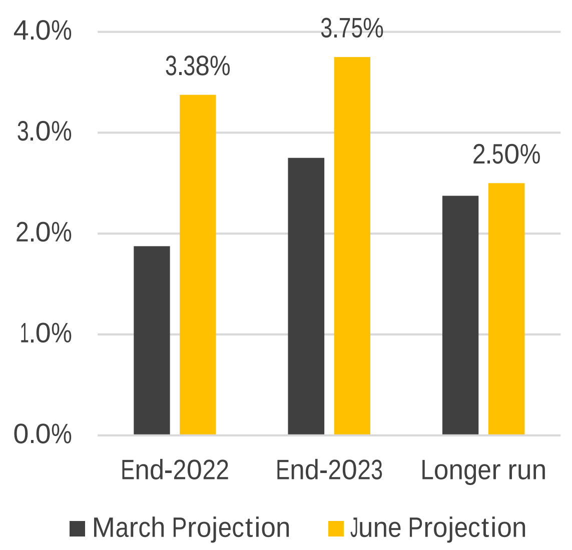
- For now, investors will continue to focus on inflation and the hawkish Fed policy, leading to upward pressure on the Treasury yields. Still, we expect growth concerns to increasingly dominate towards the latter part of the year, hence putting a lid on the yields.

- Taking into consideration of the latest dot plot and growing recession concerns, we revise our 10-year UST yield forecast range to 2.75% - 3.25% by end-2022. While we acknowledge the increasing attractiveness of sovereign bonds, we remain wary of the near-term downside risk and hence stay neutral for now. Meanwhile, the tightening financing conditions could trigger credit constraints and hence higher default rates. Corporate credit spreads, especially in the HY segment, would likely widen given the weaker macro outlook.

Figure 3: 10-year U.S. Treasury yields continue to climb in 2Q

Source: Bloomberg I 30 June 2022

Figure 4: Fed's median forecasts for the federal funds rate



Source: Bloomberg I 30 June 2022

Market Outlook- cont'd

- We turn underweight on Developed Market (DM) HY credit as the risk reward has become unattractive. Despite the recent widening of credit spreads, we believe current valuations have not fully reflected the elevated recession risks, particularly in a protracted downturn scenario. While credit fundamentals are starting from a relatively strong point, rising funding costs and weaker earnings suggest lower quality issuers will be more vulnerable in this rate hike cycle.

- In contrast, we maintain a neutral view on DM IG credit as nominal yields have become more attractive given the year-to-date rise in interest rates and widening of credit spreads. However, there is scope for spreads to widen further as investors start to price in recession risks, providing some cause for caution.

- We are neutral on Emerging Market (EM) IG credit given the balanced risk reward, with robust credit fundamentals and supportive technicals mitigating macroeconomic concerns. Notably, EM IG credit metrics are expected to improve in 2022 amid higher commodity prices. Limited issuance of new EM corporate bonds is also a positive. In contrast, we are underweight EM HY as the segment is fundamentally weaker and would be more vulnerable to interest rate hikes stemming from higher inflation.

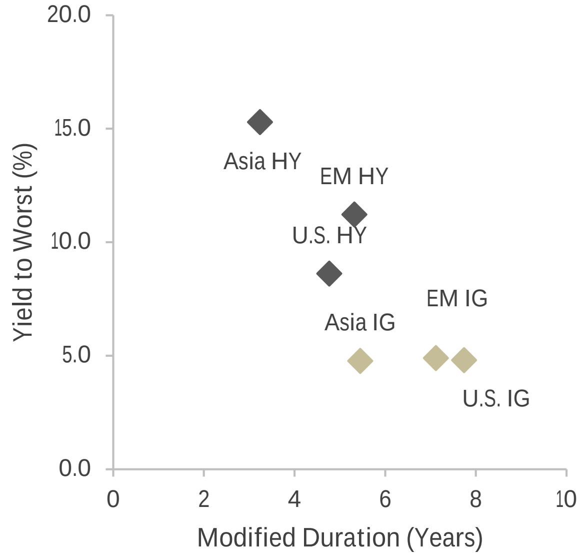
- In Asia, we prefer Asia IG over HY credit in an up-in-quality stance as the former offers resilient carry and lower default risk. China's increasingly pro-growth policies should also support the fundamentals of China IG credit which has a significant weighting in the Asia IG universe. Notably, Asia IG credit offers a higher carry relative to its U.S. peers despite having a shorter duration.

- While Asia HY credit is offering much higher than historical average spread, we retain our neutral stance given the still elevated default concerns in China property credit. Chinese authorities have started to introduce supportive policies, but the measures have yet to provide meaningful relief to distressed developers amid lacklustre contracted property sales and liquidity. The sector still needs more time to bottom-out, as such the upside will likely be capped for now.

Key Risks

- Persistent inflation leading to accelerated tightening.
- Escalating political uncertainties in emerging markets.

Figure 5: Yield-to-Worst and modified duration of bond sub-asset classes



Note: The above indices are based on Bloomberg Barclays bond indices.
Source: Maybank Group Wealth Management Research I 30 June 2022

Maybank Investment Strategy

Third Quarter 2022 - Equities

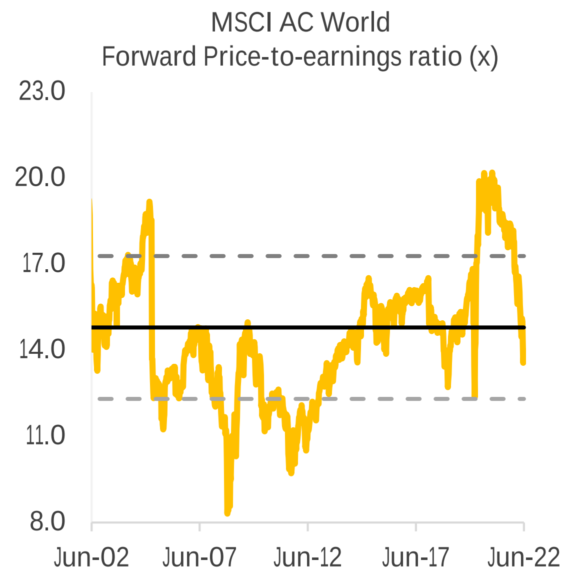
Summary

- While global equities have retreated to historical average valuation (Figure 6), the performance may remain subdued with corporate earnings vulnerable to further downgrade on slower revenue growth and lower margins.
- Overall, we prefer to position defensively with active selection playing an increasingly important role at current juncture. Notably, quality stocks, including those with lower earnings risks and stronger balance sheet, are more likely to outperform as they are better positioned to navigate the current headwinds.
- Markets wise, we are neutral on both the U.S. and Asia (including both China and Japan) but retain our positive tilt on Indonesia. We also turned neutral on Taiwan on valuation grounds and Thailand on the improving macro and tourism outlook. In contrast, we remain negative on Europe and India.
- Sectors wise, we prefer the likes of Consumer Staples and Healthcare that have historically outperformed during a recession given their more stable earnings profile. Staying invested in dividend stocks could also help generate steady income returns for the portfolio.

Market Outlook

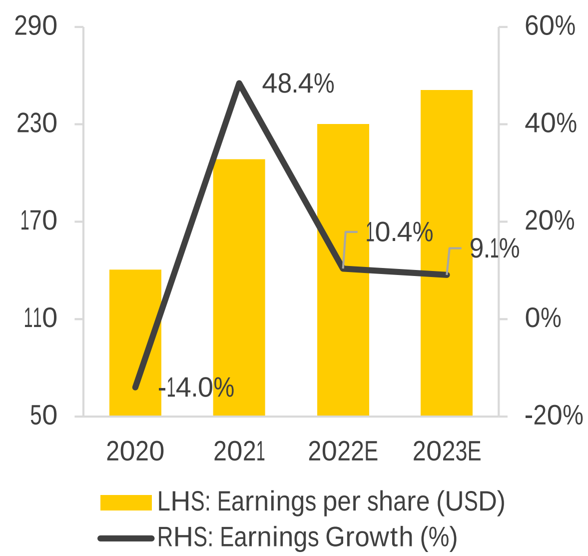
- Persistent inflation has pushed the Fed to front-load its interest rate hikes more aggressively this year. The heightened pace of tightening has resulted in rising fear of a recession as growth momentum is slowing down rapidly. However, consensus is still projecting S&P 500 earnings to grow at 10.4% for 2022 (Figure 7). We believe the forecasts may be overly optimistic and see downside risks to earnings particularly profit margins in view of the rising cost inflation. Still, with the market now trading below its historical average valuation, the longer-term downside may be more limited. Hence, we maintain our neutral stance on U.S. equities.
- Eurozone's manufacturing and services activities have deteriorated further for the month of June (Figure 8). It highlights the region's elevated recession risk especially if Russian gas supply were to be shut off completely. Unfortunately, the soaring inflation is forcing the ECB to tighten more aggressively, which will undoubtedly weigh on economic and earnings growth. While the market is undemandingly valued, it will likely underperform as the negatives may not have been fully priced in.

Figure 6: Equity valuation may remain depressed amid earnings uncertainties



Source: Bloomberg | 30 June 2022

Figure 7: Consensus expects 2022 earnings to grow by 10.4% despite challenging environment



Source: Factset | 24 June 2022

Market Outlook- cont'd

- Japan's economic growth has been supported by improving consumer activities with the pandemic coming under control. However, there are increasing downside risks to its growth outlook given Japan's export-oriented economy. Hence, corporate earnings estimates may be susceptible to further downgrade. Still, the inexpensive market valuation, coupled with a dovish Bank of Japan as well as potential fiscal stimulus, may offer some support to the market.

- We are encouraged by the improvements witnessed in China's economy as well as equity market as the COVID lockdown restrictions were gradually eased. Positive signs are also accumulating on the property and regulatory front. Notably, the scope of property easing is spreading to top-tier cities while the regulatory tightening of the technology sector appears to be coming to completion. However, we do not anticipate a quick turnaround and expect the recovery to remain bumpy especially given the global headwinds. In addition, the government will likely stick to its stringent zero-COVID policies which could lead to renewed lockdowns from time to time and disrupt the recovery. As such, we retain our neutral stance on China.

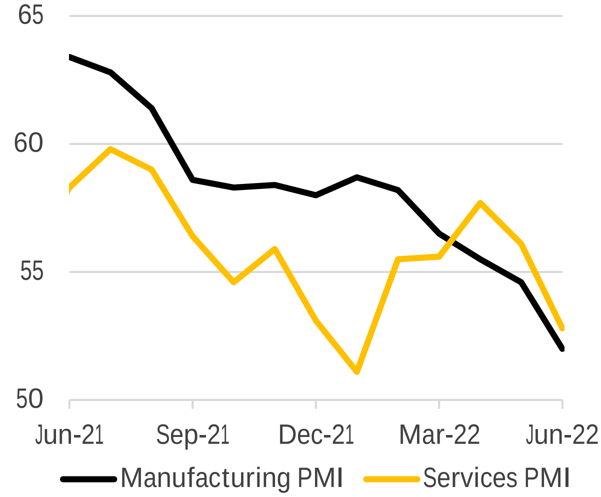
- We continue to underweight India. Retail investors, a strong pillar of the market since 2021, could start shifting away from equities and towards more traditional saving instruments with the expected increase in bank deposit rates. In addition, India's equity risk premium does not fully reflect the risks to growth and earnings, leaving the market vulnerable to a sell off.

- To-date, the South-East Asian markets have held up relatively better than global peers. However, they will not remain unscathed in a downturn. For now, we retain our preference for Indonesia with support from the robust domestic demand recovery potentially mitigating the risks of peaking commodity prices and a weaker currency. Meanwhile, we retain our neutral stance on both Malaysia and Singapore as the inexpensive valuations should limit the downside risks for both markets.

Key Risks

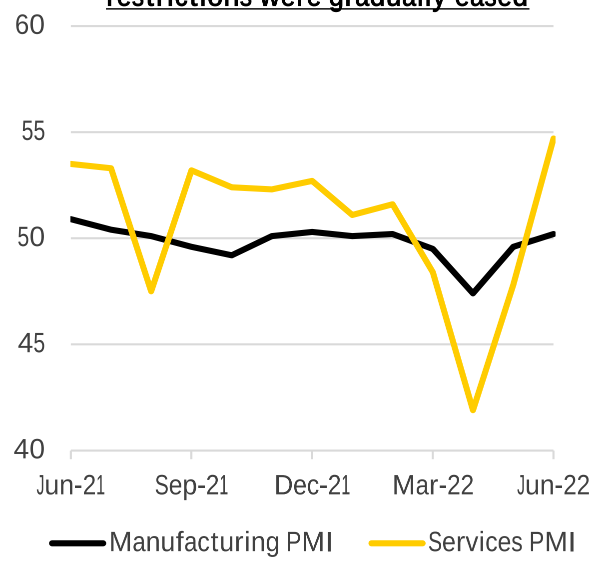
- Runaway inflation leading to more aggressive monetary tightening and global stagflation.
- Worse-than-expected deterioration in corporate earnings.
- Escalation in geopolitical uncertainties.

Figure 8: Eurozone manufacturing and services Purchasing Managers' Index (PMI) data surprised on the downside



Source : Bloomberg | 30 June 2022

Figure 9: China's manufacturing and services PMI improved in June as lockdown restrictions were gradually eased



Source : Bloomberg | 30 June 2022

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