QUARTERLY INVESTMENT STRATEGY
THIRD QUARTER 2022

Taming inflation at all costs

UOB Asset Management

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Summary

Inflation has not improved as the world reopened in 2022 and in fact has gotten worse. Central banks have been committed to do "whatever it takes" to tame inflation. These words have helped markets in the past, but have become a significant overhang in 2022. This is likely to remain so until we see some relief in inflation trends.

In our 2Q Quarterly Investment Strategy report, we noted that growth shocks from the war in Europe and sharp interest rate rises had dented our previously healthy economic growth outlook, and had caused us to turn more cautious. That trend is now putting even more pressure on central banks to raise rates and cool the economy.

As such, similar to our views in the second quarter, we believe in the need to stay cautious with both our equity and fixed income investments. Slowing growth will be a headwind for equities and rising rates will be a near term headwind for fixed income. We overweight cash, gold commodities and alternatives.

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Global Investment Strategy

"Whatever it takes", used to be a helpful phrase that central bankers employed to help address periods of financial stress. Now the phrase is striking fear in markets.

In a strange twist of events, over the next few months central banks will not be working to stimulate economic growth. Rather, they must do whatever it takes to tame persistent inflation. This includes engineering a controlled slowdown in growth. Their success lies in the balance.

For a while, the outlook for global growth and global corporate earnings was positive. But then inflation started to run too high and broadened to more sectors, threatening to become persistent. Now central bankers have run out of time to see if supply chain bottlenecks can improve. They need to tame inflation before it becomes entrenched into long term expectations.

Against this backdrop, we need to stay cautious in the near term. However, we recognise that longer-term opportunities are forming. Given that markets are likely to remain volatile in the coming quarter, we are underweight both equities and fixed income and overweight alternatives, commodities and cash.

But we don't think investors need to be overly bearish when thinking about the one-to-two year outlook. While growth will slow in coming quarters, we don't think the slowdown has to be very deep, and there is scope for a strong recovery in the medium term.

A complicated macro world

To many investors, the investment markets have seemed rather crazy in recent years. In the midst of the pandemic, when half the global economy was shut down, global equity markets were making new highs. Now in 2022, just as the world is reopening and global GDP appears strong, both stock and bond markets are mired in bear market conditions. Not surprisingly, some investors have thrown up their hands in frustration and given up trying to find rational explanations for markets. Our view, however, is that markets continue to be rational, it is just that these are very complicated markets to explain.

In order to do so, it is necessary to take into consideration forward pricing, monetary policy, valuations, geopolitical risks and inflation regimes. There are all important conceptual issues, but we will focus on monetary policy and inflation, as we believe these to be the biggest market drivers this quarter.

The inflation problem

At the start of the year, we argued for a firmer global economy amid global Covid re-openings. A rebound in inflation after a decade of disinflation was not necessarily a bad thing, especially as most of the inflation numbers were driven by supply chain issues that should improve over a short period of time.

But the supply chain issues were in fact slow to improve. The war in Ukraine added fuel to the fire by spiking energy and food pricing, while the China lockdowns delayed the reopening theory. Inflation not only failed to ease but in fact broadened to more sectors. With inflation expectations starting to influence wages and service sectors, the risks are growing that high prices will become deeply entrenched and hard to reverse.

There is much debate as to what is causing this spike in inflation. While some blame Covid fiscal policies, others point to the decade of easy monetary policy, alongside structural forces such as deglobalisation and environmental degradation. We remain convinced that current inflationary pressures are primarily supply-led anomalies related to the more-difficult-than-expected unwinding of Covid restrictions.

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Global demand as measured by consumer spending appears to be on a steady trendline that is aligned to pre-Covid trajectories. However, the make-up of spending has changed. In 2020 and 2021, there was a rapid increase in spending on goods, while services spending declined sharply. In 2022, that trend has reversed, with spending on services at elevated levels whereas goods spending is more flat.

For the global suppliers of goods and services, this has been a challenging period. During the pandemic, goods producers had to manage factory lockdowns and uncertain future forecasts, but were also forced to ramp up deliveries to meet surprisingly strong orders. Employment for goods production, sales and deliveries were strong. Now in the 2022 post-pandemic era, a large number of workers are suddenly needed in service sectors like restaurants, recreation and travel. The reallocation has been tricky to manage, and the inability of these industries to meet such big shifts in demand has resulted in pricing pressures on goods and upward wage pressures.

The good news about supply-driven inflation is that it is less structural and therefore more addressable. The Fed was proved incorrect in calling this inflation “transitory” but they are probably not wrong that it is not likely to persist over the very long term. For example, cars in the US are a big driver of inflation. In the decade prior to Covid, the US averaged car sales of about 17.5 million per year. As of May 2022, the seasonally-adjusted car sales annual trend rate was 12.5 million cars. Car dealers are reported to have many customers but no cars to sell. As a result, new car prices are up and even more so for used car prices.

However, it is reasonable to assume that the US will be able to produce 17.5m cars again next year and that existing production problems can be resolved before too long. After all, the US has sustained this volume of car sales for decades. If indeed supply can normalise by 2023, then a lot of the current inflation problems can be expected to dissipate.

The monetary policy challenge

The downside to supply-led inflation is that central bank policy cannot do a lot to improve supply. The ability to raise interest rates and reduce liquidity are blunt tools because they only have the effect of reducing demand rather than increasing supply.

The US Fed has similarly articulated the view that current inflation is supply-led and should improve over time. But they are concerned that inflation has been too slow to improve, and is getting entrenched into expectations. Having waited for months for an improvement in supply, time is running out, and the Fed has now committed to do “whatever it takes” to tackle inflation.

The investment implications of this commitment are troubling for both the equity and bond markets. Since global supply issues do not look like they will be quickly resolved, most economists are ominously concluding that “whatever it takes” will be a meaningful slowdown in demand. This has cast dark clouds over equity markets as equities usually struggle to perform when the outlook is for slow or negative growth. Meanwhile, fixed income markets are unlikely to benefit despite their safe haven status. Unlike previous moderations in growth, it may take unusually high rates for the Fed to orchestrate enough of a slowdown to bring down inflation.

Hard or soft landing?

At this point, most investors seem to have accepted that growth must slow. But investors are yet to agree on the shape that the slowdown will take, and in particular, whether a full-blown recession is on the cards. If the economy contracts to negative growth in the coming year and unemployment rises significantly, then investors would perceive this as a “hard landing”. However, if growth only moderates without a significant rise in unemployment, then investors would welcome this as a “soft landing”.

Looking back at other soft landings periods, it is estimated that equity markets typically correct by between 10 to 20 percent and drawdowns typically last less than a year. The drawdowns for hard landings are deeper, ranging between 20 to 40 percent. While there are a large number of risks and uncertainties, we at UOBAM think the case for a soft landing is more compelling.

Economic growth in the developed markets since the start of the year remains healthy with employment at historically high levels, strong consumer spending was and positive manufacturing indicators. Additionally, both consumer and corporate balance sheets are still healthy. In particular, consumers were fairly prudent during the Covid period, causing savings rates to increase, while net worth is at high levels.

Faced with a slowdown, both consumers and corporates look likely to manage without needing to make deep cuts. Also, as inflation is largely due to shortages of goods like cars, a hard landing scenario, including significant reductions in production, closed production lines and worker lay-offs would not solve the problem. Rather, what central banks need is for companies to keep producing enough to meet demand, and most businesses appear to realise this. As such, we don't expect a very sharp slowdown, and our base case remains for a soft landing.

Rising long-term opportunities

Our base case for the next quarter is for caution and to be underweight equities and fixed income. But it is important to be aware that the long-term expected returns for both equities and fixed income have improved significantly in 2022.

Fixed income markets are having one of their worst years in history with broad global fixed income benchmarks suffering double digit declines in 2022. Central banks are expected to keep hiking rates through the coming months. As a result, many investors appear to have soured on fixed income as an asset class.

While our view is also cautious for the coming quarter, over a one to two-year period, we believe that fixed income will provide healthy returns. The improved outlook is primarily due to the simple fact that bond yields are much higher than they were a year ago. As of the middle of June, 10-year US Treasury bond yields reached about 3.25 percent and the average investment grade credit spread is 1.6 percent. Thus, the average yield for most bond funds is approaching 5 percent. At this level of yield, further increases in interest rates will not have the same effect as in recent months. It is possible therefore for fixed income funds to generate positive returns over the next year even if rates rise further.

Furthermore, if and when economic growth slows, slowing inflation will ease the pressure on bond yields. A more significant growth slowdown in the coming year will lead to falling bond yields and the potential for fixed income returns to reach high single digit levels. Hence, while we still advise near-term caution, opportunities are forming in fixed income markets over the medium term.

Equity markets' long term returns are heavily influenced by risk premiums and valuations. So far in 2022, earnings for listed companies has continued to grow while valuations have declined sharply, making the multi-year outlook more healthy for equities than at the start of the year. Furthermore, if our views about a soft landing are correct, then the market correction appears overdone, and equities have the potential to trend up from these levels.

Overall, we think it is important to balance the view of near-term market volatility with positioning for a recovery over the longer term. We recommend that investors with a longer time horizon stay invested, and those who have exited the markets to re-enter gradually over time.

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Global Asset Allocation

For the third quarter of 2022 we are underweight equities, slightly underweight fixed income, overweight cash, overweight commodities, and overweight alternatives.

Within equities we are overweight Asia which we expect to be less affected by the turmoil in Europe and have better valuations. Within fixed income we are cautious on government bonds and high yield, and prefer investment grade credits.

Sector	View	Notes
Equities	–	**Rationale:** We were optimistic at the start of the year for equities, but the dual risks of inflation plus the war in Ukraine have added too much uncertainty. As such, we keep our recommendation to underweight after downgrading in the second quarter. Growth may yet prove resilient by the end of 2022, but for 3Q22 we recommend caution until there is better clarity on the global growth outlook. **Risks:** Slowing growth momentum, hawkish Fed policy, Russian retaliation against the West, China's slowing growth and inflation are all meaningful risks to global equities.
Fixed Income	–	**Rationale:** We expect bond yields to continually rise through the rest of 2022. Bond yields already rose significantly in 1Q22 and we think the pace of further rises will continue. We expect the 10yr UST yields to range between 3.0 to 3.75 percent in the second half of the year. Fed rate hikes and bond yield rises will be a headwind for fixed income markets. **Risks:** Inflation and the hawkish Fed remain downside risks for fixed income. On the other hand, geopolitical risks could trigger a rally in safe haven assets like bonds and thus could "wrongfoot" the fixed income underweight.
Commodities	+	**Rationale:** Commodities will face intense shortages due to the conflicts in Ukraine as both Ukraine and Russia are major suppliers of many major commodities. In particular, sanctions on Russia will limit global supply of oil and the global risks are putting upward pressure on gold prices. **Risks:** Fed hawkishness could drag down both growth-related commodities and the gold outlook.
Alternatives	+	**Rationale:** Broad market upside is more limited after a strong rally but opportunities remain in stock and sector picks. The availability of stock picking alpha opportunities tend to be a healthy environment for alternative assets including market neutral hedge fund strategies, hence our overweight alternatives. **Risks:** The rotations in assets have proved unpredictable and investment strategies may get wrongfooted.
Cash	+	**Rationale:** Short term yields are improving and big uncertainties in core asset classes like equities and fixed income imply cash and other liquid instruments should be a good place to hide. **Risks:** If global growth proves resilient and inflation can be tamed, then other asset classes could outperform and cash returns will be too low.

Maximum Overweight: ++ Slight Overweight: + Neutral: ■ Slight Underweight: – Maximum Underweight: ––

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Global Equity Outlook
(Regional Strategy)

The global economic slowdown is expected to coninue to weigh on equity market perromance in the coming quarter. Regionally, the calls are tricky to make. We come down on the view that the inflation and rate challenges in the developed markets are going to hurt those markets more.

We would expect Asia to outperform in this environment. Admittedly, this is a challenging call to make when the trend is for developing markets to underperform developed markets during global economic slowdowns.

However, we note that Europe faces the headwind of the conflict in Ukraine. The US faces the headwind of having the most hawkish central bank. Asia, on the other hand, appears to be on a bit of a counter trend to what is happening elsewhere. The region continues to reopen more whereas other markets are already open. Asia also has structurally higher growth that can operate better in higher interest rate environments.

As such, we are neutral on the US and positive on Asia.

Country	View	Notes
US 	■	**Rationale:** US equities are relatively more expensive and the US is the epicentre of the interest rate hiking environment that will weigh on US corporates. But the US corporate environment has proved more resilient to economic weakness in prior downturns. During periods of economic slowdowns, the US dollar and US markets tend to perform relatively better. These mixed issues lead us to be neutral on US equities. **Risks:** The US Fed has turned more hawkish than central banks in other major regions and the US could face a greater slowdown than other regions. Also, valuations are high and could face deratings.
Europe 	-	**Rationale:** European growth is at risk due to the conflict in Ukraine. The sanctions against Russia are likely to slow growth in Europe as a whole, given the relatively high reliance on Russian energy and other imports. **Risks:** European earnings growth forecasts are lower than other major regions. Europe has struggled to maintain periods of better performance in the past and may disappoint again in 2022.
Japan 	■	**Rationale:** Japan will likely be seen as a relative safe haven from the conflicts in Europe, and growth was set to rebound from the heavy pandemic restrictions in 2021. **Risks:** Even in a world of rising inflation, Japan has not been able to shrug off deflation. Deflation contributes to weak investment and stagnant growth.
Asia 	+	**Rationale:** Asia's lower valuations make it less vulnerable. The underperformance from last year implies more upside potential. And it is out of the way of the direct conflict in Europe. **Risks:** Smaller-than-expected/delayed fiscal and monetary support measures in China, as well as prolonged and/or elevated underlying core inflation in Asia represent downside risks.

Very Positive: ++ Positive: + Neutral: ■ Negative: - Very Negative: --

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Asia Equity (Country Strategy)

The outlook for Asia equities market is mixed in the near term amid an uncertain global macro environment.

Downward revisions to growth expectations due to supply shocks in food commodities and fossil fuel is playing out. In addition, corporates' profitability remain susceptible as consumer sentiment turns increasingly fragile against a slowing global growth backdrop, despite signs that the region's inflation momentum may be slowing ahead. These uncertainties underscore our continued defensive tilt towards energy, materials and financials, as well as a value bias in our positioning.

Country	View	Notes
Mainland China	■	**Rationale:** Valuations may have bottomed after earnings downgrades. Potential economic growth turnaround in 3Q from further macro and targeted fiscal support measures to counter growth slowdown. **Risks:** Earlier than expected easing supply chain disruptions, faster than expected recovery in domestic real estate sector. Potential upside from lifting of US trade tariffs.
Hong Kong	–	**Rationale:** Further downside risks to an already lacklustre GDP growth outlook owing to its zero-Covid policy. **Risks:** Earlier-than-expected borders reopening, improved China/HK political relationship.
India	–	**Rationale:** Earnings outlook is tepid due to the ongoing squeeze on margins and against an already elevated inflationary environment. **Risks:** Corporate earnings outlook improves, oil price normalises.
Indonesia	+	**Rationale:** GDP growth accelerating on back of domestic reopening boost. Country is a good hedge against stagflation risks as a net commodity exporter. **Risks:** Collapse in commodity prices, weak Rupiah.
Malaysia	+	**Rationale:** Reopening to sustain earnings momentum. Better placed to benefit from higher oil prices as an energy exporter country. **Risks:** Slower-than-expected domestic economy recovery, election/political noise, sharp drop in oil prices could weaken MYR.
Philippines	–	**Rationale:** Pace of domestic economy recovery will continue to trail regional peers, against a backdrop of fiscal lull in the near-term post local elections. **Risks:** Faster-than-expected recovery in tourism, earlier-than-expected normalisation in economic activities
Singapore	■	**Rationale:** Beneficiary of global re-opening but its exports are vulnerable to global growth slowdown. **Risks:** Sharper-than-expected growth slowdown in China/major trading partners.

Very Positive: ++ Positive: + Neutral: ■ Negative: – Very Negative: ––

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Country	View	Notes
South Korea	■	**Rationale:** Still modest non-tech domestic consumption should provide some offset to a potential slowdown from export-dependent sectors. **Risks:** Semis cycle rebounding earlier-than-expected, Weak non-tech consumption growth, Geopolitical risks (US, Japan, China)
Taiwan Market	–	**Rationale:** Moderating global end-demand for tech hardware, alongside headwinds from disruption in supply chain, is likely to weigh on its near-term growth trajectory. **Risks:** Better-than-expected personal consumption spending, Worsening cross-straits relationship.
Thailand	■	**Rationale:** Steady uptrend in earnings recovery is largely discounted. **Risks:** Delayed revival in tourism sector, resurgence in political unrests.

Very Positive: ++ Positive: + Neutral: ■ Negative: – Very Negative: ––

Export markets look vulnerable

We see the balance of risks skewed more favourably to South Asia as the underlying recovery trends from reopening broadens out. On the contrary, export-oriented North Asia is more vulnerable to the global growth slowdown.

While we maintain our negative view on North Asia, **we have upgraded China to neutral.** We have turned more positive as China's equity market valuation appear to have bottomed after recent earnings downgrades. The recent enhancements in macro policy support and implementation of targeted fiscal measures should help drive an earnings turnaround in the third quarter. Also in the near-term, we expect China to see a bounce in economic activities on the back of reopening activities assuming no major resurgence of Covid infections.

In contrast, we downgrade Taiwan from overweight to underweight. Moderating global end-demand for tech hardware and supply chain disruptions are likely to put a dampener to its near-term growth trajectory.

We remain neutral on Korea as still modest non-tech domestic consumption growth should help offset a potential slowdown from export-dependent sectors.

Hong Kong remains an underweight given downside risks to an already lacklustre GDP growth due to its zero-Covid policy and against moderating exports and investments backdrop.

We continue to underweight India given a tepid earnings outlook due to the ongoing margin squeeze and amid an already elevated inflationary environment.

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Within ASEAN, we continue to overweight Malaysia and Indonesia as our preferred markets. Malaysia's reopening is likely to sustain corporate earnings momentum and the market is better positioned to benefit from higher oil prices as an energy exporter country. Likewise, Indonesia's GDP is anticipated to accelerate on the back of a domestic reopening boost. As a net commodity exporter country, Indonesia also offers a hedge against stagflation concerns and supply-side constraints.

We remain neutral on Singapore and Thailand. Singapore is a beneficiary of the global reopening but its exports growth is vulnerable to a global growth slowdown. Thailand is seeing a steady earnings recovery but this is largely discounted. Philippines remains an underweight as the pace of domestic economy recovery from reopening is likely to trail its regional peers, against a backdrop of a fiscal lull in the near term, post local elections.

Key risks to our cautiously optimistic positioning include a huge tech rebound and extended above-trend inflation. A drastic global growth slowdown also represents downside risks to our view.

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Global Fixed Income Outlook

(Sector Strategy)

We expect 10-year bonds to trade between 2.85 – 3.60 percent in the coming quarter, and assess that moves towards the top end of the range represents a good opportunity for investors to get back in the market. Given the turbulence in financial markets and widening of credit spreads, we prefer high quality asset backed bonds with attractive valuations.

Before the release of May's inflation data, the narrative was that of peak inflation - as long as headline inflation does not exceed 8.50 percent, fixed income markets should chug along just fine. However, May's print of 8.50 percent put paid to that notion. The Fed reacted by hastening the pace of Fed rate hikes, with the terminal rate touching four percent at one point.

As such, fixed income has suffered another wobble. However, the growth/inflation trade off means that during risk off periods, bonds saw renewed demand, which kept the 3.50 percent level in 10-year yields intact.

Sector	View	Notes
Developed Markets (DM)	■	**Rationale:** While upside is limited, high quality DM bonds will offer attractive carry in any downturn. **Risks:** All bets are off if US CPI breaches the 9 percent mark.
DM Government	■	**Rationale:** Even with elevated inflation, current govies offer very attractive carry, even in the shorter tenors. **Risks:** Continuing inflation prints at 8-9 percent may led to another bond selloff.
DM Credit	+	**Rationale:** DM IG bonds are at very attractive valuations. With most of these bonds being asset backed, there should be no question of debt repayment. **Risks:** Continuing volatility in financial markets may cause credit spreads to widen out.
Emerging Markets (EM)	+	**Rationale:** Valuations of EM debt are far more attractive than in the DM space, especially within the investment grade credits. **Risks:** Not all sectors should be treated equally. We favour the commodities sector.
EM Government	■	**Rationale:** EM hard currency debt metrics are not yet at distressed levels and we see ample opportunities in certain spaces. **Risks:** A rising USD could cause some debt servability issues in certain EMs.

Very Positive: ++ Positive: + Neutral: ■ Negative: – Very Negative: ––

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Sector	View	Notes
EM Corporate	+	**Rationale:** EM IG bonds are far more attractive than their DM counterparts in terms of valuation, even if the risk is greater. **Risks:** We cannot rule out the increase in non-performing loans should a global recession occur.
EM Local Currency	–	**Rationale:** EM local currencies are set to face more headwinds with a rising USD and could see more outflows to come. **Risks:** If US Treasury yields stops rising, money could yet return to this sector.
Duration	■	**Rationale:** Rationale: We remain neutral. Given the flatness of the curve, there is not much incentive to extend duration in the current environment. **Risks:** The belly of the curve could spike higher if markets price out the terminal rate that is currently priced into several regional markets.
Yield Curve	–	**Rationale:** The yield curve is set to stay flat given that we are closing in on to the tail end of the economic cycle. **Risks:** We can only see curve steepening if economic prospects improve.

Very Positive: ++ Positive: + Neutral: ■ Negative: – Very Negative: ––

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Emerging Market Fixed Income
(Regional Strategy)

Sector	View	Notes
Latin America	–	**Rationale:** Political risks remain in several countries due to shifts towards populist parties, amid the toll exacted by the pandemic. Higher social spending may raise fiscal concerns and lead to increase in debt levels. **Risks:** Stronger than expected GDP growth data may lead to change in attitude of citizens in countries heading for elections.
CIS/EE*	■	**Rationale:** The low yield assets will remain susceptible to higher UST yields, while Turkey remains unpredictable. **Risks:** If rates remain low for an extended period, it may lead to higher demand for the low yielders which have become cheaper after the selloff in early 2021.
Middle East (ME)	■	**Rationale:** Middle East credits have been sturdy due to ample liquidity and strong oil prices which may be topping out soon. **Risks:** Oil prices could continue to surge above $80.
Africa	+	**Rationale:** The extension of the G20 DSSI programme to end-2021 has allayed fears of debt sustainability for now, while rising oil prices remains a strong tailwind for several countries. **Risks:** If more countries sign up for the G20 Common Framework, which calls for equal treatment of private and public bondholders.
Asia	+	**Rationale:** Post pandemic credit fundamentals have improved with the rating trajectory is positive. Having underperformed DM and EM peers, it offers value on a relative basis supported by positive fund flows. We like the frontier countries and expect spreads to tighten after lagging in 2020 while IG credits continue to face supply risks. **Risks:** Worsening of the Covid-19 situation; negative headlines from defaults, restructuring of asset management companies, re-rating and other idiosyncratic events tend to have a knock-on impact on the sector.
Singapore	■	**Rationale:** Low carry makes SGD bonds a less attractive proposition even though a strengthening SGD would be a boon. **Risks:** SGD bonds could follow if US yields make a surge lower.

Very Positive: ++ Positive: + Neutral: ■ Negative: – Very Negative: ––

* Commonwealth of Independent States and Central and Eastern Europe

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Global Currencies Outlook

Never have conditions been so conducive for USD strength, with all its stars lining up nicely.

There is an increasing growth disparity between Europe and the US, and this has helped the USD break all manner of technical resistance in the run up to its current highs. The USD is also considered a high yielder in the G7 space, with the Fed set to hike even more going forward. Finally, turbulence in financial markets have also helped the USD gain strength on its traditional status as a safe haven.

Currency	View	Notes
US Dollar (USD) **US$**	++	**Rationale:** Everything is in favour of US strength, including carry, technicals, fundamentals and safe haven status. **Risks:** USD could suffer if the Fed suddenly turns dovish.
Euro (EUR) **€**	–	**Rationale:** Europe faces a multitude of problems, including structural supply side problems and widening peripheral spreads. **Risks:** Should the Russia/Ukraine war end, the EUR could spike higher.
Japanese Yen (JPY) **¥**	–	**Rationale:** The BoJ is resolute with its yield curve control measures and remains the sole low yielder in a high yielding world. **Risks:** The JPY could spike higher if the BoJ abandons their YCC policy.
Singapore Dollar (SGD) **S$**	■	**Rationale:** SGD is incomparable against the USD for the reasons quoted above, but its NEER (nominal effective exchange rate) is actually trading strongly, which means it is currently outperforming regional peers. **Risks:** SGD might see some softening if inflation gets out of control.
China Renminbi (CNY) **CNY**	–	**Rationale:** China's zero-covid policy has resulted in growth forecasts being continually revised lower, which has caused the CNY to pay the price. **Risks:** The CNY could spike higher if China truly reopens.

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Global Commodities Outlook

We expect most of the major commodities to benefit from both structural trends and the impact of the war in Ukraine.

As other asset classes are more adversely affected by geopolitics, commodities provide a good diversifying effect. Typically, commodities benefit from forces that are negative for other asset classes. Real assets like commodities have also historically outperformed during periods of high inflation.

Sector Allocation	View	Notes
Commodities	+	**Rationale:** We like commodities as a beneficiary of the inflationary environment. It has a cyclical and a structural outlook that is positive. Russia and Ukraine are key suppliers of energy, metals and agricultural commodities and due to the war and sanctions, commodity shortages are likely to push up prices Structurally, many commodities such as base metals are seeing increased demand as they are increasingly used as part of the solution to shift away from carbon-based energy. **Risks:** If the US FED overtightens, it could both slow growth and raise real rates. This would be negative for both the cyclical commodities and the safe haven metals.
Gold	+	**Rationale:** Gold will retain its role as a valuable hedge if war risks rise or inflation continues to pose a threat. It has a dual purpose as a safe haven asset in a period of uncertainty and as an inflation hedge during periods when inflation rebounds faster than expected. **Risks:** In the last cycle, gold started to underperform when the US Fed announced the tapering of its monetary policy support. We expect the Fed to remain hawkish and to continue quantitative tightening in 2H2022.
Base Metals	+	**Rationale:** We think the multi-year outlook will be strong as new and green technologies create fresh demand for many of the metal commodities. **Risks:** Most base metals are very sensitive to global demand and any unexpected slowdown will weaken the outlook.
Energy	+	**Rationale:** Oil is a strong beneficiary of the global recovery, and the supply constraints from the Ukraine conflict. Shale oil appears slow to pick up the slack due to the amount of capital losses in the last cycle making companies reluctant to be quick to reinvest in shale. **Risks:** A setback in the pandemic, or the rise of troubling new variants would undermine the reopening of the global economy and oil prices would be negatively affected.
Others	+	**Rationale:** Demand for other broad commodities such as agriculture are also likely to remain high as the Ukraine conflict continues to disrupt supplies. **Risks:** As always, supply disruptions remain a key risk to the strengths and weakness of many commodities.

Very Positive: ++ Positive: + Neutral: ■ Negative: - Very Negative: --

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Global Alternatives Outlook

Alternatives continue to be an attractive asset class for investors looking to diversify beyond traditional investible classes. These can exhibit high correlation during times of market stress.

Alternatives can also add value to a portfolio in the current environment of low fixed income yields, risk of interest rate appreciation and volatile equity markets. Private equity can provide excess returns during a low interest rate environment with less volatility, while providing access to new opportunities not available in listed markets.

Sector Allocation	View	Notes
Hedge Funds	+	**Rationale:** Stretched valuations and volatile market support is limiting beta exposure and investors are seeking returns from alpha. **Risks:** Continued bull market performance would cause hedged strategies to underperform relatively.
Private Equity (PE)	■	**Rationale:** This asset class has the ability to access companies with superior growth and benefit from disruptions in areas such as technology and healthcare. **Risks:** Valuations are less attractive and selectivity is required.

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Contact Details

Brunei

UOB Asset Management (B) Sdn. Bhd.
Address Unit FF03-FF05, 1st Floor, The Centrepoint Hotel,
Jalan Gadong, Bandar Seri Begawan BE3519, Brunei Darussalam
Tel (673) 242 4806

China

Ping An Fund Management Company Limited
Address 34F, Ping An Financial Center, No. 5033, Yitian Road, Futian District, Shenzhen 518000
Tel (86) (755) 2262 3179

Indonesia

PT UOB Asset Management Indonesia
Address UOB Plaza 42nd Floor, Jalan MH Thamrin Number 10, Jakarta 10230, Indonesia
Tel (62) (21) 2929 0889

Japan

UOB Asset Management (Japan) Ltd.
Address 13F Sanno Park Tower, 2-11-1 Nagatacho, Chiyoda-ku, Tokyo 100-6113, Japan
Tel (81) (3) 3500 5981

Malaysia

UOB Asset Management (Malaysia) Berhad
Address Level 22, Vista Tower, The Intermark,
No. 348 Jalan Tun Razak,
50400 Kuala Lumpur, Malaysia
Tel (60) (03) 2732 1181
Website uobam.com.my

UOB Islamic Asset Management Sdn. Bhd.
Address Level 22, Vista Tower, The Intermark,
No. 348 Jalan Tun Razak,
50400 Kuala Lumpur, Malaysia
Tel (60) (03) 2732 1181
Email UOBAMCustomerCareMY@UOBgroup.com

Singapore

UOB Asset Management Ltd.
Address 80 Raffles Place, #03-00, UOB Plaza 2, Singapore 048624
Tel 1800 22 22 228 (Local toll-free)
(65) 6222 2228 (International)
Email uobam@uobgroup.com
Website uobam.com.sg

Taiwan

UOB Asset Management (Taiwan) Co., Ltd.
Address Union Enterprise Plaza, 16th Floor, 109 Minsheng East Road, Section 3, Taipei 10544
Tel (886) (2) 2719 7005
Email uobam.com.tw

Thailand

UOB Asset Management (Thailand) Co., Ltd.
Address 173/27-30, 32-33 South Sathon Road, 23A, 25th Floor,
Asia Centre Building, Thungmahamek, Sathon, Bangkok 10120, Thailand
Tel (66) (2) 786 2000
Website uobam.co.th

Vietnam

UOB Asset Management (Vietnam) Fund Management Joint Stock Company
Address Unit 01B, 15th Level, the Landmark Building, 5B Ton Duc Thang, Ben Nghe Ward,
District 1, Ho Chi Minh city, Vietnam
Tel (84) 28 3910 3757
Website uobam.com.vn

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