

# 2022 Singapore Equity Outlook: Focusing on sustainable growth

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## Summary



- We expect the recovery theme to continue supporting the Singapore economy in 2022. We see broader growth within Singapore's key economic engines in 2022, with a sharper recovery expected in the services sector as the economy reopens.
- Interest rates are likely to rise in 2022 as we see greater pressure from macro policy tightening due to higher inflation and business costs. Inflation might not be as transitory as expected, and rising wages and business costs might pose as a policy headwind in 2022.
- As such, we see a gravitation towards companies with quality of earnings growth and potential defensive growth moats that can sustain and defend returns. With the spectre of rising inflation, we also favour stocks with strong pricing power in an inflationary environment.
- We are positive on alpha opportunities in 2022 and we believe greater bifurcation in growth will lead to opportunities in stock selection. We favour the financials, industrials, consumer and technology sectors and are more cautious on the telecommunications and property sectors.

## Looking ahead to 2022

The Singapore economy is on a road to recovery. Although the economy has already rebounded sharply in 2021, we expect the recovery theme to remain intact and continue supporting the Singapore economy in 2022. We see a broadening of growth within Singapore's key economic engines in 2022, with a sharper recovery expected in the services sector as the economy reopens.

Interest rates are likely to rise in 2022 as we see greater pressure from macro policy tightening due to higher inflation and business costs. Inflation might not be as transitory as expected, and rising wages and business costs might pose as a policy headwind in 2022. With rising inflation and wage costs and slowing revenue growth momentum, the outlook for margins and corporate earnings appears more challenged in 2022. We emphasise the importance of investing in quality and sustainable growth franchises, which we believe will outperform in the current macro environment.

Equity returns could moderate from the double-digit returns achieved in 2021. We believe the opportunity in 2022 will come from stock selection and higher bifurcation opportunities in the Singapore market. We favour financials, industrials, consumer and technology sectors most while we view the telecommunications and property sectors with caution.

### Singapore poised for continued recovery

Looking back, 2021 has been a good year for the Singapore equity market. The Straits Times Index (STI) returned 12.5% on a total return basis (as of 3 December 2021), which has more than reversed its loss of 8.1% in 2020. A strong revival in trade and manufacturing exports helped catalyse a sharp rebound in corporate earnings in 2021, which together with accommodative policy and attractive valuations, helped drive strong double-digit returns for the Singapore stock market and catapulted Singapore to one of Asia's top equity performers in 2021.

We expect recovery to remain a predominant theme in 2022, similar to 2021, during which the economy, equity markets and corporate earnings all recovered to the pre-COVID levels of 2019. For the year to Q3 2021, Singapore's GDP has already risen by more than 7%, which is higher than its pre-pandemic levels in 2019. What is also impressive about this recovery is that in Q3 2021, Singapore was the only ASEAN-6 economy with real GDP growth (seasonally adjusted) above its Q4 2019 level.

Looking forward, we expect economic expansion in Singapore to build on the 7% year-on-year GDP growth expected in 2021 and rise by another 3-5% year-on-year in 2022, thanks to tailwinds from the region's economies reopening and the normalisation of supply disruptions. We also expect growth in 2022 to become more balanced with services moving more in equilibrium with manufacturing. Manufacturing and export-oriented sectors, undoubtedly the stars of the economy in 2021, could see their growth momentum taper off in 2022 but should remain resilient as global demand continues to be healthy. We believe the service sector should recover and provide most of the incremental growth for the Singapore economy as we head into 2022. Wholesale retail trade, transport and storage and services could surprise positively as the country moves towards a new normal in which COVID-19 becomes endemic. Transport services, traditionally a key contributor to the Singapore economy, could be poised for a strong recovery in 2022 as the travelling resumes.

### Growth and quality should start to outperform

In the recently concluded biannual macroeconomic review, the Monetary Authority of Singapore (MAS) said that it is watching closely for signs of inflation, as it sees the risk of inflation becoming more persistent as opposed to a transitory bottleneck caused by the pandemic. This also prompted the MAS to tighten its monetary policy setting in October 2021 to address the rise in consumer prices and inflationary pressure caused by supply disruptions and higher wages.

We see the risk of inflation rising further as we enter 2022. Based on the gap between consumer and producer prices, companies and corporates appear to be bearing a greater brunt of the cost pressure in prices and this could ultimately flow into consumer prices in 2022. Against this backdrop, we believe the MAS is likely to stay guarded against inflation and tighten policy when needed. As the economy gradually reopens, domestic price pressures could further add to existing supply side pressures caused by supply chain bottlenecks. Should inflation continue to move above 2.0%, we expect the MAS will further tighten at the next April 2022 policy meeting.

Tighter policy is also likely to have an impact on equity markets. Tapering could start at the end of 2021 in the US with the Federal Reserve scaling back on asset purchases until mid-2022. Should domestic inflation be less transitory and more permanent, cost pressure on businesses will inevitably rise, and it would be prudent, in our view, to favour companies with growth and quality. Our belief is that growth and quality typically perform better during times of growth scarcity and when higher interest rates, rising cost drivers and slowing revenue momentum introduce greater uncertainty on earnings.

In 2022, we expect companies with quality and sustainable growth in returns to outperform the broader market, and prefer them over companies that rely purely on cyclical growth, momentum or value. Growth will become scarcer in

2022—investors are likely to pay more for earnings growth visibility and certainty in stock and sector selection. As such, we see a gravitation towards companies with quality of earnings growth and potential defensive growth moats that are able to sustain and defend returns. With the spectre of rising inflation, we also favour stocks with strong pricing power in an inflationary environment. Again, we expect quality and growth moats to feature well in performance during times of inflation.

### The return of alpha as growth slows and policy normalises

We expect equity returns to moderate in 2022 following strong double-digit gains in 2021. This is typical when sharp economic recovery phases descend into moderate growth periods typical of a mid-cycle economic expansion. Against the backdrop of rising rates, market valuations are also looking less attractive. This could dampen overall market returns (beta) in 2022 where the market has less room for price-to-earnings expansion and more uncertainty on overall earnings growth.

We are positive on alpha opportunities in 2022 and we believe greater bifurcation in growth will lead to strong opportunities in stock selection. We also believe sectors that offer a more sustainable growth profile at reasonable valuations could attract higher valuations due to scarcity premiums. With this stronger focus on growth and returns, we prefer sectors which offer continued growth in earnings trajectory in 2022, and those that have growth buffers to offset earnings weakness. In this category, we like technology, industrials and consumer discretionary and staples where we see good potential of incremental growth in earnings revisions in 2022.

We like utilities and industrials as we see rising energy prices as a tailwind and the continued push towards sustainability investment as a growing theme. Rising oil and commodity prices should support earnings in select industrials. We also continue to have a constructive view of renewable energy opportunities and transition stories where we identify positive change in a company's sustainable returns.

We are more positive on consumer discretionary in 2022, especially in Singapore companies with exposure to the growth in ASEAN consumerisation. We expect ASEAN consumption to recover in 2022, as we believe the region is poised to play catch up and accelerate faster than most other Asian economies. We also favour consumer staples and see the sector as a good inflation hedge. Valuations are more attractive after the recent price correction and we see better relative earnings growth from higher commodity prices as we head into 2022. We particularly favour companies within the sector in which we identify distinct positive change, such as efforts to improve environmental, social and governance areas of materiality.

We also like technology hardware and see a potential re-rating in the sector once we overcome the current supply chain disruptions. Lockdowns imposed by governments and component material shortages have caused significant impact on the global supply chain, and the alleviation of these bottlenecks through government relaxation and private initiatives to improve supply chain issues should allow tech companies to ride on the broader reopening and the capex recovery in manufacturing and trade. We also believe most of the tech hardware companies in Singapore are trading at attractive valuations, from a historical perspective and also compared to their peers in the region.

We like select financials and believe banks will continue to be a beneficiary of rising interest rates. We also see banks benefitting from financing opportunities with the resumption of trade agreements in the region. While we also like communication services such as e-commerce for their attractive growth proposition in next few years, we are more cautious on their valuations. We have a cautious view of telecommunications due to more lacklustre growth prospects and are also relatively cautious on property and REITs, due to rising interest rates and a tightening liquidity environment.

### Corporate restructuring in new Singapore

We remain positive on the corporate restructuring theme in Singapore. In 2022, we expect corporate restructuring beneficiaries to feature more in companies that have embraced innovation to better compete in a post-pandemic economy, as well as companies making positive transitions in their journeys towards sustainability. We believe successful execution in their respective corporate restructurings will raise the potential of overall sustainable returns and provide a re-rating in valuations.

We are more upbeat on reopening beneficiaries in 2022 and expect companies that have restructured to be well-placed for the transition to an endemic new normal. An example would be in private healthcare operators, where companies have stepped up to support government efforts to provide testing and vaccinations, even as their primary hospital

business suffered. Today, this restructuring has positioned them well in Singapore's new norm of "test, trace and vaccinate", and the business for healthcare services has doubled from pre-pandemic levels. Also, vaccination rates rising to levels that allow economies in the ASEAN region to reopen borders and resume travel could mean a strong revival of foreign medical tourism in Singapore, as more foreign patients return for elective procedures and the requirements for testing drives continued growth in healthcare services.

The energy transition story in renewables also presents an exciting area of growth and transformation for Singapore Inc. We see this as particularly relevant in the industrials sector, notably in infrastructure and utilities where there are growing opportunities to invest in sustainability. We also favour companies well placed in the energy transition towards renewables, where companies have demonstrated clear and aggressive plans to grow their renewables portfolio through decarbonisation initiatives, tapped green financing and accelerated capital recycling for growth. We also see this expansion in renewable energy happening at a time when ASEAN governments are also accelerating plans to decarbonise. With good execution, we believe this could see companies improving on their sustainable returns and re-rating with higher valuation multiples.

### Increased focus on dividend growth

We believe dividend investing remains relevant in a time of rising interest rates and slowing growth. Against the backdrop of growth deceleration in 2022, capital preservation and sustenance of returns will become even more important as a source of returns. We continue to be constructive in dividend investing and expect greater focus on high and rising dividend stocks in the current macro backdrop.

We believe the backdrop of rising yields would not necessarily weaken the prospects of high-yielding dividend stocks, but rather underline the importance of dividend growth. In Singapore, we also continue to find that the spread for dividend yields against bond yields remains attractive, despite rising bond yields. This spread will remain supportive for high-yielding dividend companies. The strategy in dividend investing for 2022 will increasingly focus on dividend growth rather than dividend yields, as we expect dividend growth opportunities could be scarcer amid a rising interest rate environment. As such, we see the potential for companies with high and rising dividend growth profiles to be re-rated with higher valuations during a time where broader earnings growth moderate.

We also see quality and sustainable returns featuring as a key driver of performance in dividend investing. We like selected financials, industrials and technology companies that are well positioned to deliver and increase dividends in 2022. We also see selective retail REITs and logistic REITs outperforming in 2022. We see retail REITs as a beneficiary of the reopening trade in Singapore, and logistic REITs benefitting from Singapore's rising role as a regional manufacturing hub in technology, transportation and financial services.

### Key themes of recovery, rates and returns in 2022

In summary, we expect the growth story in the Singapore economy to continue into 2022, where we see a greater contribution from the recovery in the service sector. This continued recovery will also underpin growth in corporate earnings for the Singapore equity market. 2022 will also see the spectre of rising inflation and interest rates. In our opinion, we believe companies with quality and sustainable growth will outperform during a time of slowing earnings growth and rising cost pressures. Finally, against the backdrop of ebbing liquidity and policy support coupled with slowing global growth momentum, we expect overall equity market returns to moderate in 2022. However, we remain positive on alpha opportunities in Singapore. We believe the moderation of earnings growth and tighter policy headwinds will lead to greater dispersion in earnings growth across sectors and higher bifurcation in stock returns. This will favour stock pickers, in our view. We favour financials, industrials, consumer and technology sectors most in 2022.

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