February 2017

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FROM THE EQUITY DESK

Monthly Outlook

Summary

- Asia ex-Japan (AxJ) equities returned 6.2% in US Dollar (USD) terms, outperforming MSCI World. Singapore, Hong Kong and Chinese equities outperformed while Indonesia, Malaysia and Thailand lagged. Asian currencies generally strengthened against the USD over the month.

- Singapore stocks were buoyed by better-than-expected fourth-quarter GDP growth, while the Hong Kong index was underpinned by financial stocks on the improving outlook for margins from higher global interest rates.

- Meanwhile, MSCI China gained 6.8% in USD terms, led by the industrials, materials and internet sectors. Producer price inflation increased, while manufacturing PMI remained in expansion territory.

- Conversely, demand for Thai and Indonesian equities was muted following their solid performance in 2016. Softer coal prices and lingering asset quality concerns across major banks dampened sentiment towards Indonesia's larger stocks.

- As inflation picks up across a number of countries, we try to look for companies that stand to benefit from a reflationary environment. Meanwhile, valuations for AxJ remain relatively attractive, while earnings revisions have started to trend up.

- We maintain an overweight to China, with a preference to sectors such as internet, tourism and healthcare, and continue to favour India, where companies have witnessed limited impact from the government's de-monetisation policy. Conversely, we remain selective in developed Asia and ASEAN.

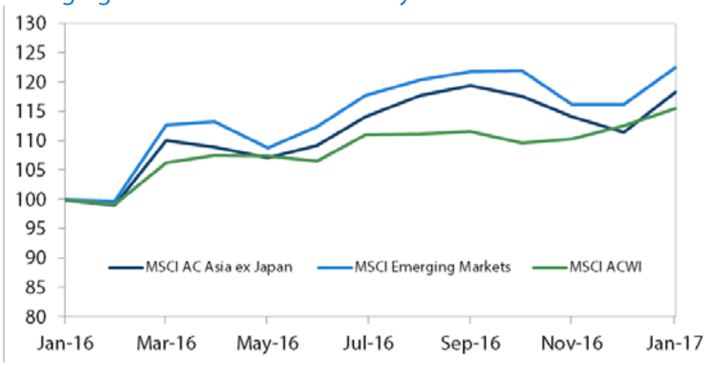
Asian Equity

Market Review

- Asia ex-Japan equities rose in January

Asian equity markets started the year on the front foot with the MSCI AxJ Index up 6.2% in USD terms. Returns bettered MSCI World's 2.4% gain during the month. Equity gains contributed 4.9% while Asian currency appreciation relative to the USD added a further 1.3%. Singapore, Hong Kong and Chinese equities outperformed while Indonesia, Malaysia and Thailand lagged. From a sector standpoint, technology and materials continued to witness strong demand while traditional defensive sectors, utilities, staples and healthcare underperformed. Markets were driven higher by better economic data across the region, higher materials prices and the anticipation of policy led stimulus emanating from the US.

1-Year Market Performance of MSCI Asia ex Japan versus Emerging Markets versus All Country World Index



Source: Bloomberg, 31 January 2017. Returns are in USD. Past performance is not necessarily indicative of future performance.

MSCI Asia ex Japan versus Emerging Markets versus All Country World Index Price-to-Earnings

Source: Bloomberg, 31 January 2017. Returns are in USD. Past performance is not necessarily indicative of future performance.

- Singapore buoyed by growth data; Hong Kong by financial stocks

The MSCI Singapore index returned 8.3% in USD terms for the month of January. A slew of much better economic data for the fourth quarter saw analysts and market participants more optimistic that the economy has passed through the lows of the cycle. Fourth quarter GDP rebounded to 1.8% year-on-year against expectations of only 0.3% growth. This was led by stronger exports and industrial production, in particular within the technology sector. MSCI Hong Kong also finished the month strongly, up 7.7%, although this was led by financial stocks on the improving outlook for margins from higher global interest rates.

- China also ended the month higher

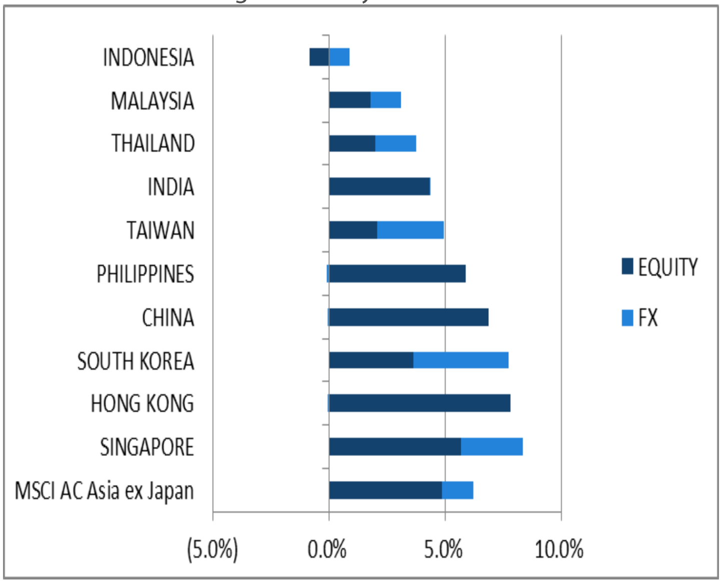
Chinese equities also had a strong month with MSCI China up 6.8% in USD terms, led by industrials, materials and internet sectors. Producer price inflation (PPI), the price of goods coming out of the factory gate, increased by 5.5% in December and the manufacturing Purchase Managers' Index (PMI) remained in expansion territory at 51.4. Public Private Partnership (PPP) projects and higher commodity prices gave rise to a more optimistic earnings outlook for industrial and material stocks. The internet sector was driven by Alibaba which reported better than expected results on the back of better cloud revenues and strong core e-commerce growth. Revenues were up 54% year on year.

- Conversely, Indonesia and Thailand lagged

Some of last year's better performing markets started off 2017 on a weaker note with MSCI Indonesia up only 0.1% in USD terms while MSCI Thailand was up 3.7%. A softening in coal prices and lingering asset quality concerns across major banks meant subdued demand for some of Indonesia's larger stocks. Demand for Thai equities was also muted given their strong performance last year.

MSCI AC Asia ex Japan Index

For the month ending 31 January 2017

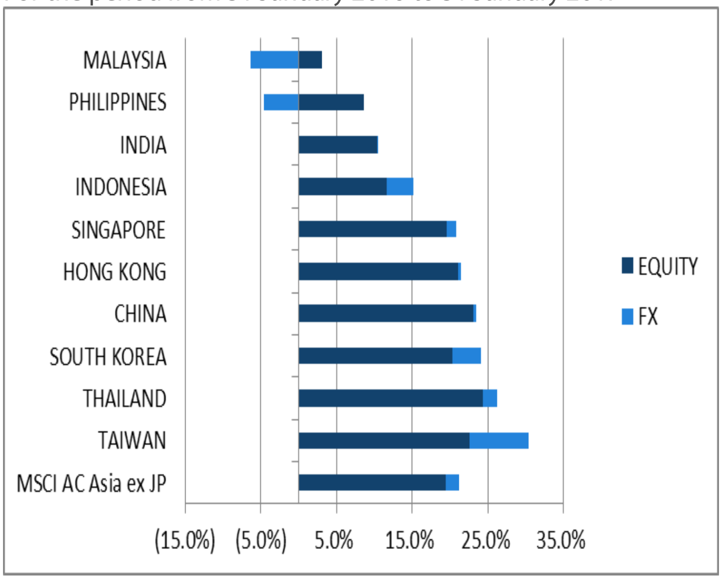


Source: Bloomberg, 31 January 2017

Note: Equity returns are single country MSCI indexes and are in local currencies while FX and MSCI Asia ex Japan returns are in USD. Returns are based on historical prices. Past performance is not necessarily indicative of future performance.

MSCI AC Asia ex Japan Index

For the period from 31 January 2016 to 31 January 2017



Source: Bloomberg, 31 January 2017

Note: Equity returns are single country MSCI indexes and are in local currencies while FX and MSCI Asia ex Japan returns are in USD. Returns are based on historical prices. Past performance is not necessarily indicative of future performance.

Market Outlook

- Focus on beneficiaries of reflationary environment

Globally investors seem transfixed by policy rhetoric and "tweets" from the newly sworn in President Trump. This has distracted from otherwise improving economic conditions in the US and a pick-up in trade across the Asia region towards the end of 2016. In today's new anti-globalisation world, the question remains whether traditional export orientated economies will benefit as much as they may have done in past cycles. We see a greater role for China in this equation, especially if the US remains focused on a protectionist/anti-trade agenda. As inflation picks up across a number of countries, we try to look for those companies that stand to benefit from a reflationary environment. MSCI AxJ trades on a 1.4 times forward price-to-book (P/B) multiple compared to a 2.2 times P/B multiple for MSCI World, while earnings revisions have started to trend up.

- Maintain overweight to China

Economic data from China continues to improve despite the rise in domestic interbank rates and a plethora of policy actions to contain capital outflows. The government continues to push PPP programs to encourage greater investment in the near term while the rise in PPI should help ease some pressure at mining and industrial companies. Of note during January was the announcement by the Chinese Steel and Iron Ore Association that it will be clamping down on all illegal operating capacities with a view to eliminate 50 million tonnes per annum (mtpa) of steel capacity (or 6% of Chinese production) by June 2017. We maintain an overweight stance to Chinese stocks with a preference for new economy sectors including internet, tourism and healthcare.

- Continue to favour India

India also remains a key overweight and with the reporting season well under way, we note many companies have witnessed limited impact from the government's de-monetisation policy. Private banks experienced large low cost deposit inflows which should structurally lower funding costs for the sector. Corporate orientated banks continued to show high credit costs which we believe is evidence that they are finally acknowledging and providing for problem assets in their legacy books. China's move to curtail illegal steel production has lifted prices globally and this should ease what has been a big problem sector for Indian banks. The upcoming budget session is likely to produce incremental hand-outs for the rural community, particularly in light of the disruption caused by de-monetisation.

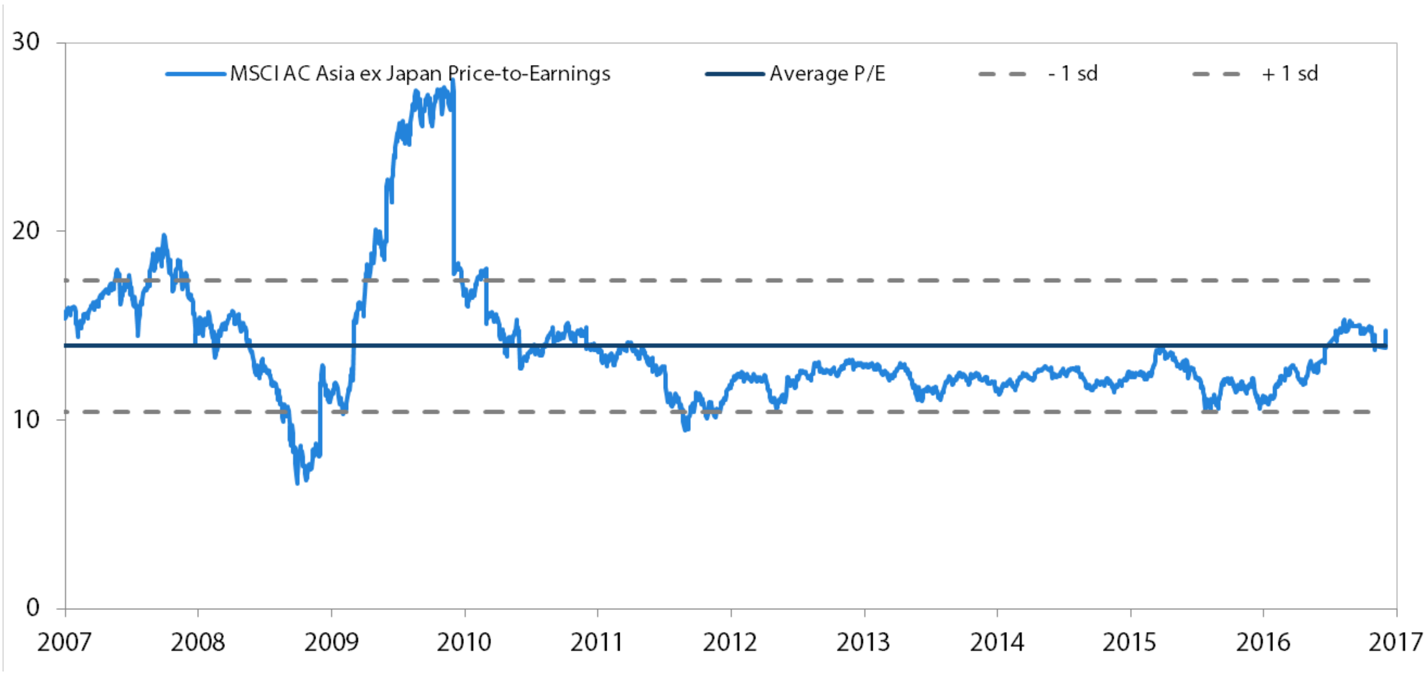
- Remain selective in developed Asia

We have become more constructive on more developed Asian market financial stocks owing to the potential improvement in profitability brought about by a pick-up in the global interest rate environment. We do not, however, believe this applies to all, and differentiate according to our views on outstanding asset quality issues and the negative impact of higher rates on domestic growth.

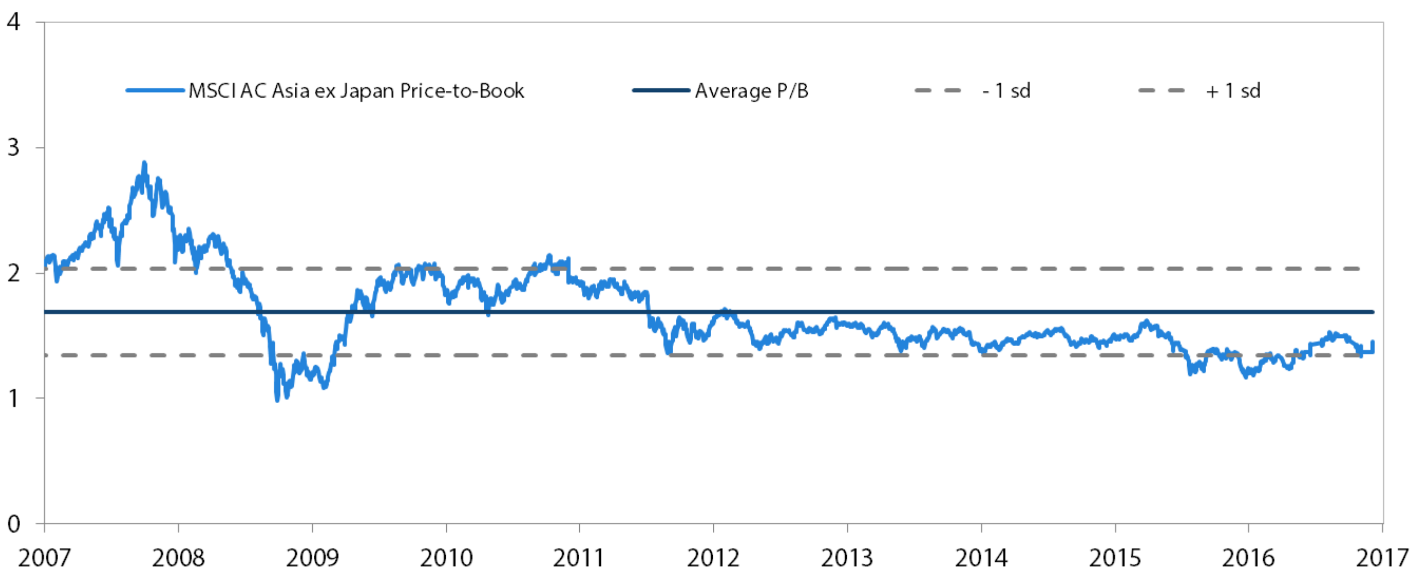
We remain very selective across the traditional export orientated economies of Taiwan, Korea and Singapore, preferring companies in niche sectors with sustainable earnings. While the technology sector has been a key driver of better export numbers thus far, we are wary of each country's sensitivity to US demand and as potential losers from any trade spat between the US and China as has already been evidenced by Korea's agreement to let the US install a Terminal High Altitude Area Defense.

Appendix

MSCI AC Asia ex Japan Price-to-Earnings



MSCI AC Asia ex Japan Price-to-Book



Source: Bloomberg, 31 January 2017. Ratios are computed in USD. The horizontal lines represent the average (the middle line) and one standard deviation on either side of this average for the period shown. Past performance is not necessarily indicative of future performance.

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