

UOB Investment Insights

Market PowerBar

OCTOBER 2022

A LOOK AT THIS MONTH

Key Topics

What investors should know

1



In developed markets, inflation has been a key driver of central bank policy decisions and market action, while in Asia, concerns over China's growth and slower pace of reopening has kept inflation more manageable.

The policy divergence is worth noting. In particular, Asia's relatively looser monetary policy could lend support to stocks.

- ▶ Asian central banks are likely to deliver smaller rate hikes compared to their developed market counterparts.
- ▶ In particular, the People's Bank of China's (PBOC) monetary policy has been more accommodative amid headwinds related to COVID-19 lockdowns and property market woes.

2



As recession risks rise across developed markets, investors are turning to Asia as its economies gradually reopen.

Ride on Asia's recovery.

- ▶ Asian equities have performed relatively well year-to-date and still offer attractive valuations.
- ▶ Asian economies with a greater reliance on domestic demand are expected to better withstand developed markets' slower growth.

3



Even as China's growth continues to be challenged by COVID-19 lockdowns, property sector woes and weather disruptions, much of these negative news has likely been priced in.

Investors who can stomach short term volatility and keen on China may focus on the valuations and trends of sectors taking up bigger weights in the benchmark index.

- ▶ Chinese stock markets are trading below their 15-year price-to-earnings average.
- ▶ Larger sector weights are supported by less regulatory headwind, improving fundamentals, and relatively attractive valuations.

Upcoming Events



European Central Bank (ECB) Meeting

- ▶ Watch for any change in the ECB's rate hike trajectory.

20th Congress of the Chinese Communist Party

- ▶ Watch for China's economic development and potential revision of its zero-COVID policy.



Speak to your UOB Advisor today to find out more.

Topic 1

Policy Divergence

High inflation in the developed markets has been a key driver of central bank policy decisions and market action this year. The inflation problem in the developed markets is a bigger one than in Asia. In Asia, a combination of growth concerns in China and a slower pace of reopening has kept inflation more manageable.

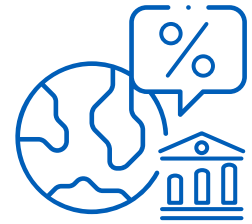
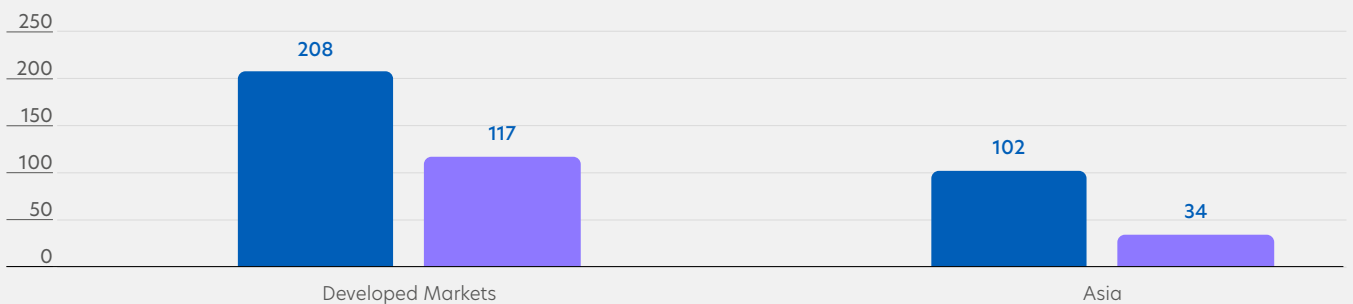


Figure 1A

Average Cumulative Central Bank Policy Rate Changes (bps)

Bps since 31 December 2021

Basis Points



Source: Forecast from J.P. Morgan Economics as of 30 September 2022.

Developed Markets include United States, United Kingdom and Euro Area.

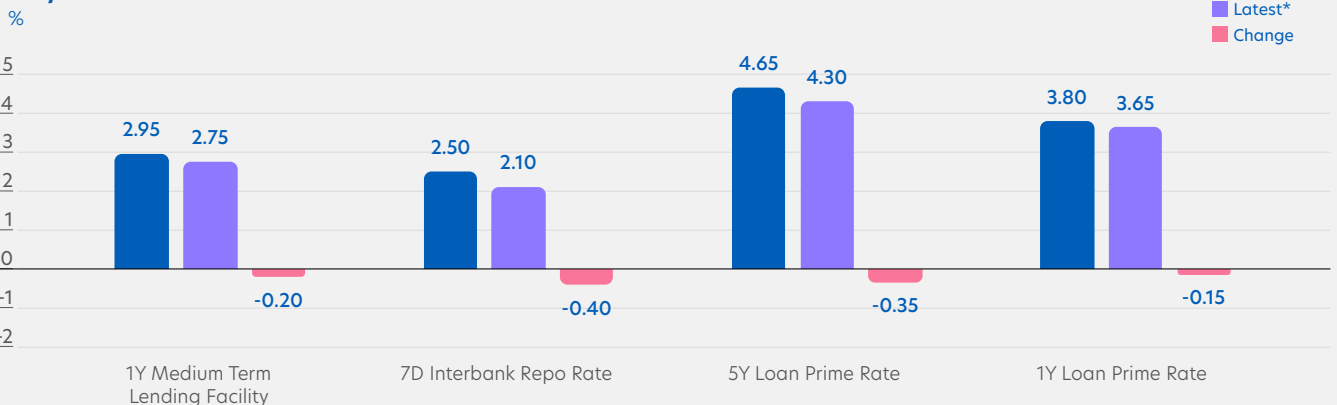
Asia includes Australia, Philippines, South Korea, India, Taiwan, Malaysia, Thailand, Indonesia, Japan and China.

Key takeaways

1. Year-to-date, Asian central banks have hiked slightly less than half the average number of basis points compared to developed market central banks (Figure 1A). For the rest of the year, developed market central banks are expected to make fighting high inflation a priority and hike an average of 125 basis points more. In Asia, we expect less than a third of rate hikes till year end compared to the developed world, given the region's more muted inflationary pressures and a slowdown in global demand.
2. China's monetary policy is on a different path from the developed world's and most of Asia's. While most economies have increased rates to some degree, China is one of the few to have cut policy rates this year.
3. The People's Bank of China's (PBOC) has taken an accommodative monetary policy to battle growth headwinds related to COVID-19 lockdowns and property market woes. It has cut key interest rates in order to maintain conditions conducive for growth (Figure 1B), including reducing the 5Y loan prime rate twice this year to kickstart recovery in the real estate sector.

Figure 1B

Key Chinese Interest Rates



Source: Bloomberg.

*Data reflected as of 30 September 2022.



In summary

- Policy divergence between developed markets and Asia, particularly China, is worth noting. More accommodative monetary policy in this region can lend support to stocks. On the other hand, aggressive monetary policy in the developed world has led to stock market volatility.

Topic 2

Asia's recovery

Asia is not experiencing as rough a time as the Euro area or US yet. Except for China, more countries are slowly shifting to living with COVID-19 and welcoming foreign travellers again. Inflation is on the rise, but there are fewer signs of overheating compared to the US. Asia also does not face energy supply issues to the same extent as Europe.



Figure 2A

MSCI Asia ex-Japan valuations

MSCI Asia ex-Japan (AXJ) - MSCI World (MXWO) Index 15Y Relative Next 12 Months' Price-to-earnings Ratio



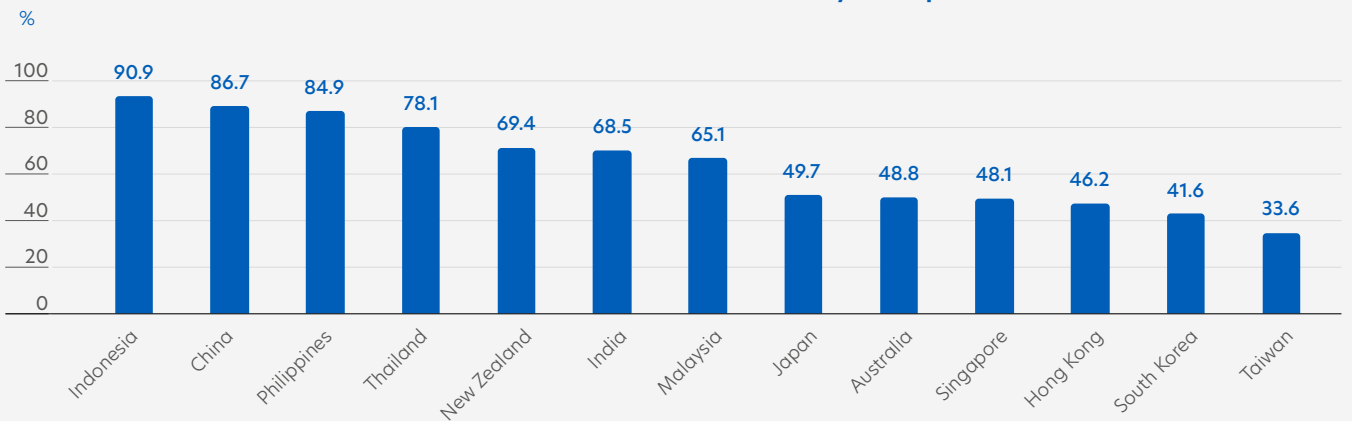
Source: FactSet, MSCI, J.P. Morgan Asset Management. Data reflected as of 30 September 2022.

Key takeaways

1. In face of uncertainty in developed markets, investors have turned to Asia. Asian equities have performed relatively well year to date, and valuations are still attractive. MSCI Asia ex-Japan price-to-earnings ratios are still low in comparison to their 15-year history against the MSCI World index (Figure 2A).
2. Recession risks are rising across developed markets, and Asia, despite being in a promising recovery, is not immune to these risks. However, although earnings are driven to an extent by exports, they are also supported by large domestic demand (Figure 2B). Asian markets that are more reliant on domestically sourced revenues may outperform those in the US and Europe, should the slowdown in developed markets continue.

Figure 2B

Revenue derived from domestic demand of each country's respective MSCI index



Source: FactSet, MSCI, J.P. Morgan Asset Management. Data reflected as of 30 September 2022.

In summary

- ▶ As Asia is not uniform, there will still be divergence in performance within the region even with less exposure to energy supply issues like in Europe or overheating like in the US.
- ▶ Local policy action, the region's own geopolitical concerns, and a slowing macro landscape remain as key risks.
- ▶ Overall, economies with a higher share of activity generated by domestic demand are expected to be more resilient in weathering developed markets' slower growth.

Topic 3

China Update

After a grueling year of tighter regulations for certain sectors such as Technology, Consumer Discretionary, and Communication Services in 2021, growth in China continues to be challenged by COVID-19 related lockdowns, real estate sector woes and weather disruptions. Much of this negative news is likely to have been priced in. Both onshore (MSCI China A) and offshore (MSCI China) Chinese stock markets are trading below their 15-year price-to-earnings (PE) average, much lower than developed markets' (Figure 3A).

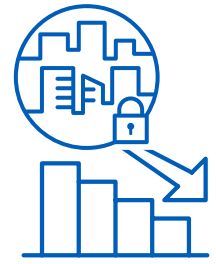


Figure 3A

MSCI China and MSCI China A valuations have derated significantly



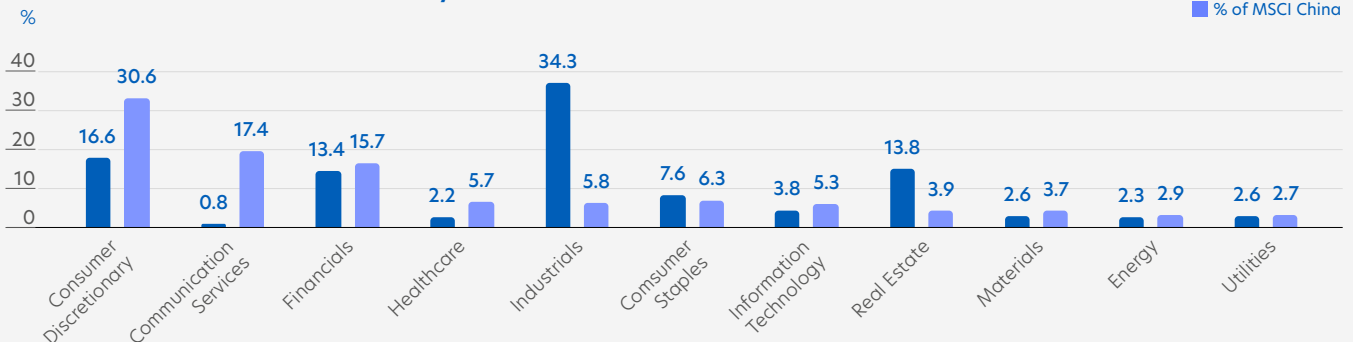
Source: FactSet. Data reflected as of 30 September 2022.

Key takeaways

1. Until the Chinese Communist Party's 20th Congress in mid-October, it is unlikely that we will see wider scale relaxation of its zero-COVID policy. However, rising vaccination rates among the elderly (above 60 years old) will give the government more comfort in embracing more sustainable reopening towards the end of this year.
2. As for the property crisis, the percentage of loans related to incomplete properties is still relatively small. The central government's decisive action to set up a fund (approximately RMB300 billion) that troubled developers can tap on to complete the projects is a step in the right direction to prevent widespread decline in confidence.
3. The economy is not always an accurate representation of stock markets. For example, while the real estate sector is the third-largest contributor to overall Chinese GDP at around 14%, the sector's weight within MSCI China representing offshore markets is only 3.9% (Figure 3B).

Figure 3B

Markets are not the economy



Source: Bloomberg, Haver. Data reflected as of 30 September 2022.



In summary

- Larger sector weights such as Consumer Discretionary, Communication Services, and Technology are supported by diminishing regulatory headwinds, improving fundamentals and relatively attractive valuations. Investors who can stomach short term volatility and keen on China may wish to focus on valuations and the trends of these bigger sector weights.



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