CIO Weekly

21 October 2020

Equities: Significant COVID-19 containment in China

Key Points

- Equities: COVID-19 cases were well contained in China, down to less than 30 average daily cases since April, setting the stage for a meaningful recovery in capital markets.
- Credit: Long duration credits have underperformed in the recovery
- FX: Consolidation on the cards for CNY after strong appreciation and amid growth fears from Europe
- Rates: Breaking down 10Y UST yield movements as US elections approach
- Thematics: Hong Kong residential property sector resilient amid the storm
- The Week Ahead: Keep a lookout for US change in initial jobless claims; Singapore inflation numbers

COVID-19 cases effectively controlled. China saw a spike in cases between 27 January and 14 February, where an average of 4,000 new cases were reported daily. Total confirmed cases were subsequently contained at 90,000 range since the start of September, with the mortality rate kept at 5%.

China, being early among the countries to report COVID-19 cases, is also among the first to show success in containment. During this period, stringent restrictions were implemented, with strict measures taken to lock down cities and towns, limit people's movements, implement contact tracing, and speed up treatment of patients. The measures have borne results. Since the start of April till now, daily average cases were controlled at less than 30, with further improvement seen starting July till now (Table 1).

Table 1: Daily average cases:

27 Jan – 3 Mar	1 April – now	July – now	October – now
3,000	29	27	21

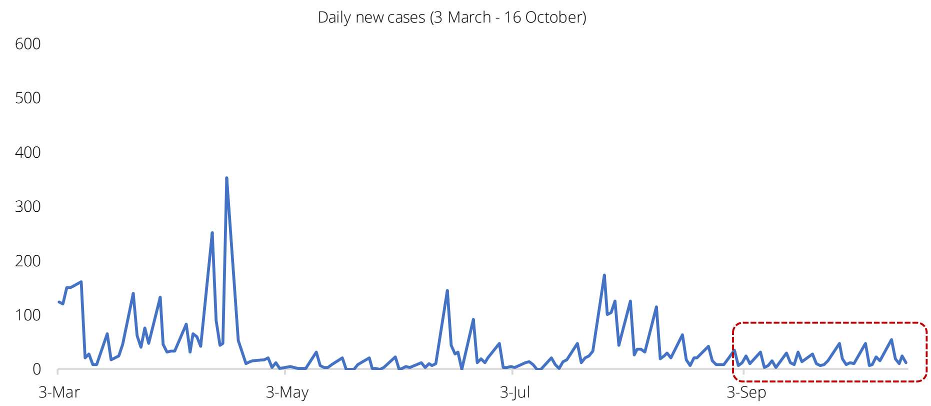
From the beginning of March, daily new cases started to trend down and stayed within control (Figure 1), enabling the authorities to reopen the domestic economy. The spike in daily cases during the end of July was counter-measured by immediate lockdown and mass testing. The situation was contained within weeks.

Makeshift hospitals closed. Notably, during this period, two makeshift hospitals and 14 makeshift health centres were constructed to treat the COVID-19 patients, armed with more than 40,000 medical personnel from all over the country. As new cases subsequently subsided and came under control, 14 of the total 16 makeshift hospitals and centres around Wuhan area have been shut down.

Lives getting back to normal. Being among the first to reopen local activities, China's manufacturing output and domestic consumption have resumed to normalcy. This was shown in the 3.2% growth in 2Q GDP, a striking turnaround from the 6.8% decline in 1Q during the height of the COVID-19 outbreak. 2020 full-year growth is projected at 2.1% before further expanding to 8% in 2021.

Yeang Cheng Ling | Strategist

Figure 1: COVID-19 cases well contained



Source: Bloomberg, DBS

Global cross assets

Returns of cross assets around the world

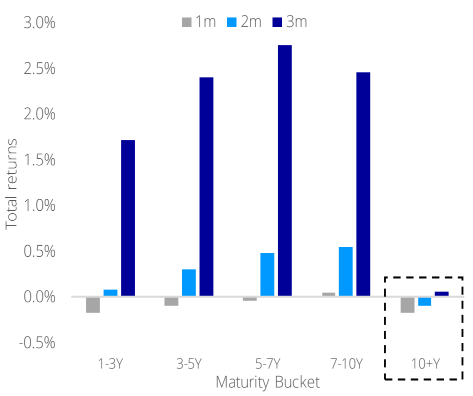
Index	Close	Overnight	YTD
DJIA	28,195.42	-1.4%	-1.2%
S&P 500	3,426.92	-1.6%	6.1%
NASDAQ	11,478.88	-1.7%	27.9%
Stoxx Europe 600	366.81	-0.2%	-11.8%
DAX	12,854.66	-0.4%	-3.0%
CAC 40	4,929.27	-0.1%	-17.5%
FTSE 100	5,884.65	-0.6%	-22.0%
MSCI AxJ	743.80	0.3%	8.1%
Nikkei 225	23,671.13	1.1%	0.1%
SHCOMP	3,312.67	-0.7%	8.6%
Hang Seng	24,542.26	0.6%	-12.9%
MSCI EM	1,127.28	0.3%	1.1%
UST 10-yr yield*	0.77	3.1%	-114.9
JGB 10-yr yield*	0.02	23.5%	4.1
Bund 10-yr yield*	-0.63	1.1%	-44.1
US HY spread*	4.68	-0.6%	132.0
EM spread*	376.99	0.0%	99.6
WTI (USD)	40.83	-0.1%	-33.1%
LMEX	3,058.00	0.4%	7.6%
Gold (USD)	1,904.08	0.3%	25.5%

Source: Bloomberg
* Changes in basis points

DBS Live more, Bank less

Credit: Long duration credits underperformed in the recovery

Figure 2: Global credit returns - Long duration has underperformed



Source: Bloomberg, DBS

Risk appetite was conducive for much of the third quarter on a rebound in economic data, vaccine progress, as well as a building consensus of a Democratic "blue wave" post-elections and the corresponding anticipated ease of fiscal stimulus passage with a united Congress. This has resulted in a steepening of the US Treasury curve, as the market-built expectations of upward global growth and inflation trajectories in the long-end.

While these factors were positive for risk assets, not all asset classes benefitted from the positive shift in sentiment. Global long duration corporate credits – measured as those with more than 10 years to maturity – naturally underperformed in the period of curve steepening (over the last one, two, and three month horizons), as low absolute yields and large supply technicals saw weak demand for the long-end. This has panned out in accordance with our expressed caution for duration risk (please refer to "New Fed framework favours HY over IG", 31 Aug 2020), and we continue to think that investors are better rewarded for additional yield taking credit risk (via High Yield credit) than extending duration while the recovery remains intact.

Daryl Ho | Strategist

FX: Deal or no deal?

Figure 3: CNY consolidation on the cards

Source: Bloomberg, DBS

The USD Index (DXY) held above 93.2 during the US session. Republicans and Democrats remain far apart on a stimulus bill before the US elections on 3 November. The 48-hour deadline set by House Democrats for a deal expires one day before Republican-held Senate's vote on a smaller USD500b bill on Wednesday. Looking ahead, investors favour a Blue Sweep at the elections because the Democrats would be more united in delivering its larger USD2.2t bill. While there is confidence that Democratic candidate Joe Biden will oust President Donald Trump from the Oval Office and maintain the Democratic Party's majority in the Lower House, the Senate race is still considered too close to call. DXY is as deadlocked as stimulus talks within a tight 93 to 94 range in October.

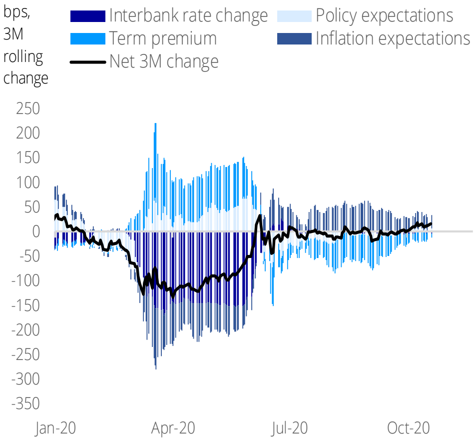
GBP could not hold above 1.30 on Monday (19 October). GBP initially rallied to a high around 1.3020 on the European Union (EU) making some concessions to restart and intensify Brexit talks. The UK was, however, unconvinced that the EU's position has shifted sufficiently for talks to achieve the compromises needed for a deal between two sovereign equals. As things stand, both sides will need to strike a deal between end October and early November for EU leaders to ratify at the EU Parliament meeting on 23-26 November. Despite hopes for a Brexit breakthrough, GBP could not shake off the volatility related to the elusive US stimulus bill. **GBP/USD is still seen holding a 1.27 to 1.30 range in the short term.**

The onshore CNY closed below 6.70 per USD for a second session. CNY reference rate was set on Monday at 6.7010 per USD, its strongest level since April 2019. The National Bureau Statistics reported that China's recovery picked up to 4.9% y/y in 3Q from 3.2% in 2Q. The momentum was, however, less impressive in quarter on quarter terms. Real GDP growth moderated to 2.7% q/q seasonally adjusted in 3Q from 11.7% in 2Q. CNY was also supported by expectations of inflows, namely, the dual listing of the Ant Group initial public offering in Shanghai and Hong Kong whose shares are expected (as per a Straits Times article) to start trading a few days after the US elections. A Biden presidency in the US is considered positive for China and the global economy. Mr Biden has pledged to reset "America First" policy if he wins the election by immediately re-joining the Paris climate accord and the Iran nuclear deal, keeping the US inside the World Health Organization and repairing strained diplomatic relations around the world. **Having appreciated more than 7% since May, CNY may consolidate** now that it has returned to the 6.70 levels, especially if global growth fears from Europe start to weigh on investors.

Philip Wee | FX Strategist

Rates: Breaking down 10Y UST yield movements as US elections approach

Figure 4: Breakdown of changes in 10Y UST yield



Source: Bloomberg, DBS

The movements on 10Y US Treasury (UST) yields can be broken down into components and analysed as we head closer to the US elections. While there are quite a few possible outcomes, they can be broadly classified into three scenarios – a clear Biden victory with Democrats holding both houses, thereby increasing the odds of another sizable fiscal stimulus; contested elections where the outcome may not be known for several months (leading to risk aversion); and a mixed house – with either Trump or Biden as president (which could be viewed as largely status quo). Taking neutral 10Y yields at around 0.70-0.75%, we think 10Y yields can rise 10-15 bps in the first scenario, fall by 10-15 bps in the second scenario, and rise modestly in the third scenario as election uncertainties ease.

We noted that 10Y US yields have been held down by three unresolved issues – US elections, stalled fiscal stimulus, and lack of vaccine approval. However, the past few weeks saw a repricing higher in longer-term yields. As Biden widens his lead over Trump, the market is now putting Biden victory as the core scenario (and putting the prospect of stimulus back into play). We suspect that more than 50% of this is already reflected in the rates space with more election clarity translating into a marked reduction in term premium (see chart). The other aspects of the yield curve have been largely stable as market participants do not expect the Federal Reserve to act in the coming few years. Moreover, we also flagged that inflation expectations (as proxied by the 10Y breakeven) already normalised into the 1.6-1.7% range several months ago. In short, term premium has been reduced, steepening the UST curve in the process. Further steepening could occur, but we probably have to cross the election hurdle first, and subsequently, the vaccine hurdle (we still expect a vaccine(s) to be approved by year end).

Eugene Leow | Rates Strategist

Thematics: Hong Kong residential property sector resilient amid the storm

- Solid support from end-users
- Stable outlook amid challenges
- Most property developers exhibit strong earnings visibility
- Current sector valuation priced in > 30% property price decline

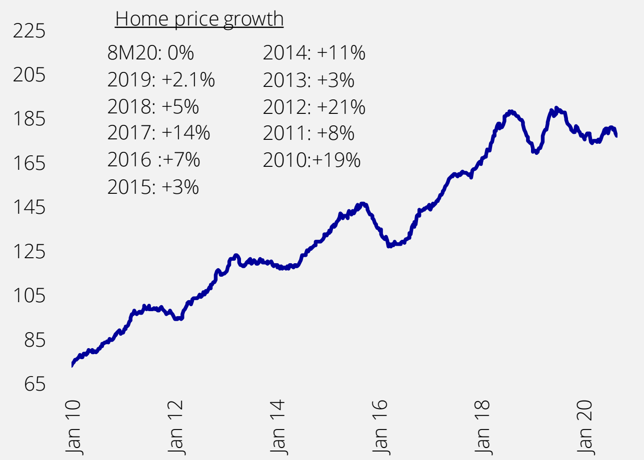
Solid support from end-users. Despite the COVID-led economic downturn, Hong Kong's residential sector, especially mass market, has exhibited strong resilience thanks to solid local end-user demand. Unlike the previous economic downcycle, DBS Group Research has not seen any major forced selling in the secondary market partly due to a benign interest rate environment which should have strengthened the holding power among existing owners. Therefore, home prices have stayed broadly stable year-to-date. Mass market projects have outperformed their luxury counterparts, which has been affected by a lack of mainland buyers due to travel restrictions and quarantine measures. Selected developers are now adopting a more flexible pricing strategy to expedite luxury home sales.

Stable outlook amid challenges. Given intermittent sales disruption led by the pandemic, we expect property developers to launch more new projects when the window of sales opportunities emerges. While a benign interest rate environment and favourable new supply outlook continue to support the residential market, potential migration wave, intensifying US-China tensions and the prolonged economic downturn should remain as an overhang on housing demand. Overall, we forecast home prices to remain steady over the next nine months, with mass market projects continuing to outperform.

Most property developers exhibit strong earnings visibility. The property developer sector is trading at 49% discount (as of 15 September 2020) to our appraised current net asset value on a weighted average basis, >1 standard deviation below its 10-year average. The current valuation has priced in >30% fall in property prices across the board which seems less likely given the benign interest rate environment. Thanks to encouraging project presales, most property developers, such as Sun Hung Kai Properties (16 HK) and Sino Land (83 HK), have strong earnings visibility which is overlooked by the market. This leads to our view that residential developers should continue to outperform office or retail landlords. Consistent good sell-through rates should improve the sentiment on the sector.

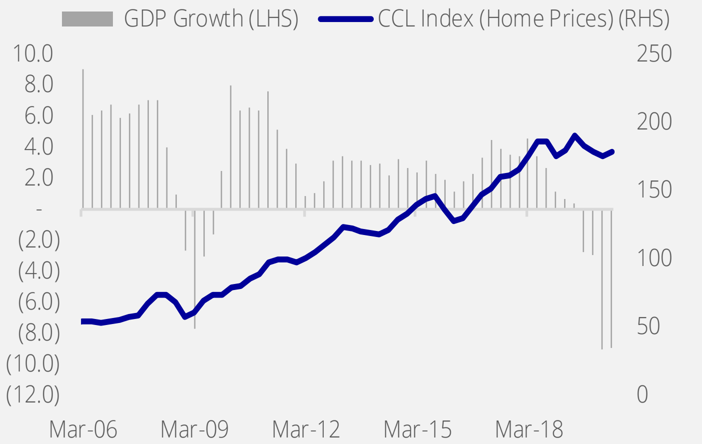
Jeff YAU | Analyst

Figure 5: Centa-City Leading Index



Source: Centaline Property Agency

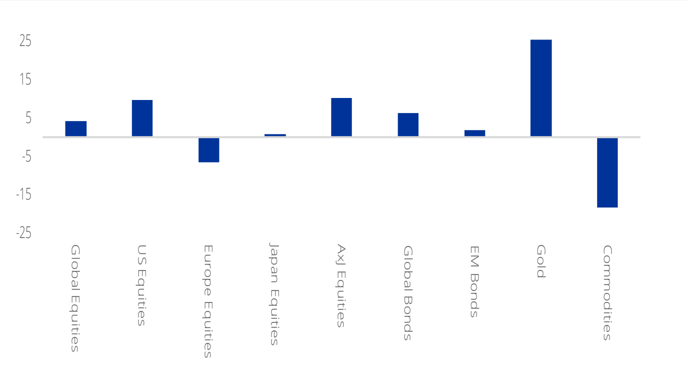
Figure 6: GDP growth vs home prices



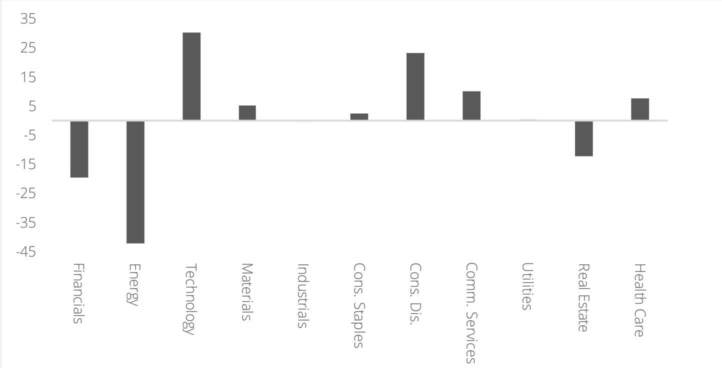
Source: Census and Statistics Department, Centaline Property Agency

CIO Markets Watch

Global Cross Assets YTD Returns

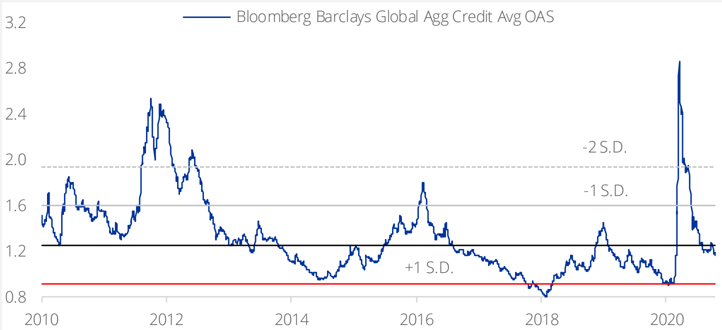


Global Sector YTD Returns



Global Equity Valuation

US Corporate Spreads



Index Returns

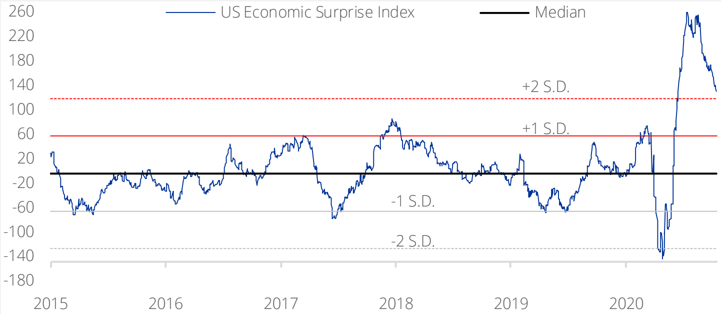
	1 week	MTD	QTD	YTD
Equities				
S&P 500	-3.0%	1.9%	1.9%	6.1%
NASDAQ	-3.3%	2.8%	2.8%	27.9%
Russell 2000	-2.1%	7.0%	7.0%	-3.3%
Stoxx Europe 600	-1.7%	1.6%	1.6%	-11.8%
Nikkei-225	0.5%	2.1%	2.1%	0.1%
MSCI WORLD	-2.4%	2.1%	2.1%	2.5%
MSCI ACWI	-2.2%	2.4%	2.4%	2.4%
MSCI Asia ex-Japan	-0.9%	4.4%	4.4%	8.1%
MSCI EM	-0.9%	4.2%	4.2%	1.1%
HSCEI	1.0%	6.2%	6.2%	-10.7%
SHCOMP	-1.4%	2.9%	2.9%	8.6%
Hang Seng	-0.4%	4.6%	4.6%	-12.9%
Straits Times	-0.3%	3.1%	3.1%	-21.1%
Fixed Income				
Barclays Global Aggregate	0.2%	0.6%	0.6%	6.3%
Barclays US Aggregate	0.2%	-0.1%	-0.1%	6.7%
Barclays US High Yield	0.1%	1.5%	1.5%	2.1%
Barclays Euro Aggregate	0.3%	0.8%	0.8%	3.6%
Barclays Euro High Yield	-0.1%	1.1%	1.1%	-2.4%
JPM EMBI Global	0.0%	1.4%	1.4%	1.7%
JPM EMBI Global Diversified	0.1%	1.6%	1.6%	2.1%

Prices & Spreads

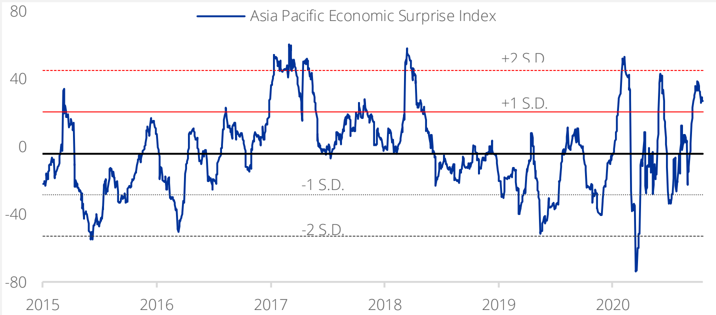
	Spot	2Q20	1Q20	4Q19
Rates				
Fed Funds Target	0.25	0.25	0.25	0.25
ECB Main Refinancing Rate	0.00	0.00	0.00	0.00
BOJ Policy Balance Rate	-0.10	-0.10	-0.10	-0.10
US Treasury 10-yr	0.77	0.69	0.66	0.67
Japanese Govt Bond 10-yr	0.02	0.01	0.02	0.01
German Bunds 10-yr	-0.63	-0.52	-0.46	-0.47
Spreads				
US Agg Corporate Spread	1.24	1.36	1.50	2.72
US Corporate HY Spread	4.68	5.17	6.26	8.80
Euro Agg Corporate Spread	1.18	1.23	1.53	2.41
EM USD Agg Spread	3.18	3.34	3.93	6.19
Currencies				
US Dollar Index (DXY)	93.4	93.9	97.4	99.0
EUR/USD	1.18	1.17	1.12	1.10
USD/JPY	105.4	105.5	107.9	107.5
USD/CNY	6.7	6.8	7.1	7.1
Commodities				
WTI Oil	41	40	39	20
London Metal Exchange (LMEX)	3058	2968	2682	2335
TR/CC CRB Commodity	152	149	138	122
Gold	1904	1886	1781	1577

CIO Economics Watch

US Economic Surprise Index



Asia Pacific Economic Surprise Index



Macro Calendar

	Date	Period	Survey	Prior
United States & Eurozone				
Initial Jobless Claims (US)	22-Oct	Oct	870k	898k
MBA Mortgage Applications (US)	21-Oct	Oct	--	-0.70%
New Home Sales (US)	26-Oct	Sep	1010k	1011k
Markit Eurozone Manufacturing	23-Oct	Oct	53	53.7
Markit US Manufacturing PMI (US)	23-Oct	Oct	53.5	53.2
Housing Starts (US)	20-Oct	Sep	1465k	1416k
Existing Home Sales (US)	22-Oct	Sep	6.30m	6.00m
Leading Index (US)	22-Oct	Sep	0.60%	1.20%

Macro Calendar

	Date	Period	Survey	Prior
Asia				
CPI y/y (SG)	23-Oct	Sep	-0.30%	-0.40%
Jibun Bank Japan PMI Mfg (JP)	22-Oct	Oct	--	47.7
Natl CPI y/y (JP)	22-Oct	Sep	0.00%	0.20%
Industrial Production y/y (SG)	26-Oct	Sep	--	13.70%
Natl CPI Ex Fresh Food y/y (JP)	22-Oct	Sep	-0.40%	-0.40%
Jibun Bank Japan PMI Composite	22-Oct	Oct	--	46.6
Jibun Bank Japan PMI Services (JP)	22-Oct	Oct	--	46.9
Machine Tool Orders y/y (JP)	20-Oct	Sep	--	-15.00%

DBS Live more, Bank less