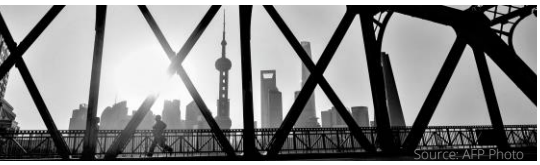

Source: AFP Photo

CIO Weekly

15 December 2020

Equities: S&P 500 to start 2021 on a firm footing

Key Points

- **Equities:** S&P 500 to start 2021 on firm footing amid positive vaccine news and robust earnings momentum
- **Credit:** European credit performance undergirded by negative-yielding sovereign bonds
- **FX:** Risk rally that undermined USD has frozen; SNB meeting this week crucial for the trajectory of CHF
- **Rates:** UST curve bull flattened as risk appetite wobbled; concerns over US fiscal stimulus and Brexit dominated sentiments
- **Thematics:** Singapore REITs riding the winds of change
- **The Week Ahead:** Keep a lookout for US change in initial jobless claims; Singapore non-oil domestic exports

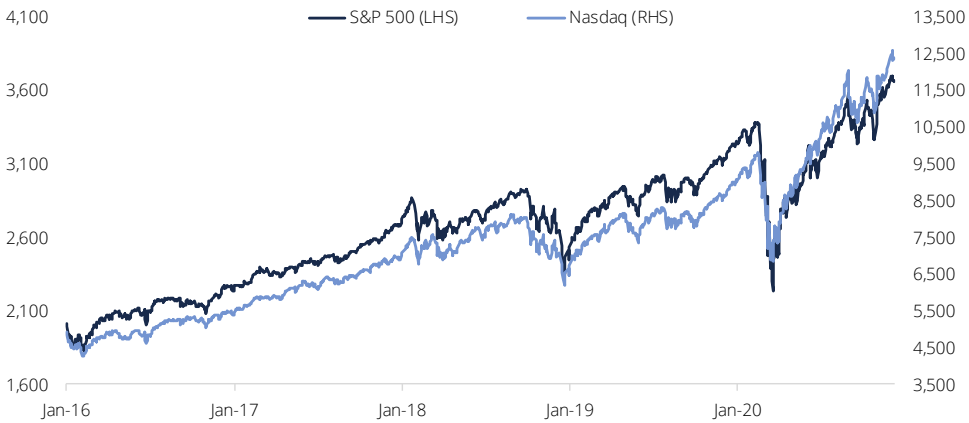
US Equities: Embracing 2021 with hope and optimism. The acute selldown in the S&P 500 Index on the back of the COVID-19 pandemic has proved to be a transitory event as the bulls took charge by late March and drove the index higher. On a year-to-date basis, the S&P 500 has rallied 13.4% while the Nasdaq Composite Index notched up stronger gains of 38.0% (as of 11 December 2020). As we head into 2021, there are many reasons to be optimistic on the collective outlook for the new year. The catalysts are:

- Fiscal Stimulus: Down, but not out. High probability of a "divided government" in the US has dampened the likelihood of robust fiscal easing to boost the US economy. But things may not be as dire as feared. It was last reported that US Treasury Secretary Steven Mnuchin has made a surprising U-turn and returned to the negotiation table for a pandemic relief fiscal package.
- Vaccine Discovery: Driving funds rotation to Value stocks. With the imminence of mass vaccination for COVID-19, activities that require face-to-face human interaction will return to normalcy and this will provide significant boost to the economy, in particular the leisure and tourism-related segments. Positive news on the vaccines front has buoyed "bombed out" sectors in the Value space and we expect the momentum to persist in the coming year.
- Earnings Growth: The next engine of growth for S&P 500. The up move in the S&P 500 was driven predominantly by valuation multiple expansion this year as investors "priced forward" the plausibility of an eventual economic rebound. But come 2021, market up moves will be powered by corporate earnings. Currently, market consensus is expecting S&P 500 earnings to grow 21.9% next year. We see significant room for upward revisions in earnings growth as the economic recovery gathers momentum.

"FOMO" and a broadening rally. The initial rebound on S&P 500 since the trough in March was met with scepticism and this was not surprising. Concerns over pandemic second waves, coupled with US election uncertainties, have resulted in investors sitting on the side lines and staying in cash. But with US equities hitting new highs, investors are expected to increasingly deploy these funds to "chase the market"; a popular strategy has been to "buy the laggards" within the Value space. Essentially, this translates to a "broadening" of the market rally, setting the stage for the S&P 500 to start 2021 on a firm footing.

Dylan Cheang | Strategist

Figure 1: US equities to start 2021 on a firm footing



Source: Bloomberg, DBS

Global cross assets

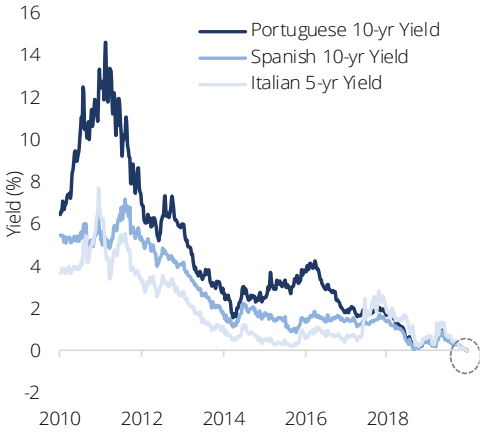
Returns of cross assets around the world

Index	Close	Overnight	YTD
DJIA	29,861.55	-0.6%	4.6%
S&P 500	3,647.49	-0.4%	12.9%
NASDAQ	12,440.04	0.5%	38.6%
Stoxx Europe 600	391.85	0.4%	-5.8%
DAX	13,223.16	0.8%	-0.2%
CAC 40	5,527.84	0.4%	-7.5%
FTSE 100	6,531.83	-0.2%	-13.4%
MSCI AxJ	814.50	-0.5%	18.3%
Nikkei 225	26,732.44	0.3%	13.0%
SHCOMP	3,369.12	0.7%	10.5%
Hang Seng	26,389.52	-0.4%	-6.4%
MSCI EM	1,250.45	-0.6%	12.2%
UST 10-yr yield*	0.89	-0.4%	-102.4
JGB 10-yr yield*	0.01	-30.0%	2.7
Bund 10-yr yield*	-0.62	-2.7%	-43.3
US HY spread*	3.82	-0.5%	46.0
EM spread*	337.22	-0.5%	59.8
WTI (USD)	46.99	0.9%	-23.0%
LMEX	3,455.40	0.4%	21.5%
Gold (USD)	1,827.35	-0.7%	20.4%

Source: Bloomberg
* Changes in basis points

Credit: European credit performance undergirded by negative-yielding sovereign bonds

Figure 2: European negative-yielding debt saw new members last week



Source: Bloomberg, DBS

The European Central Bank announced a slew of supportive measures last week (ended 11 December) following the December Governing Council meeting, with (a) an extension of the duration and size of the Pandemic Emergency Purchase Programme (PEPP) by nine months and EUR500b, respectively, and (b) extending terms for Targeted Longer Term Refinancing Operations (TLTRO) – a means of targeted lending – by one year till mid-2022 (with borrowing rates as low as -1%). Core inflation projections were notably weak; the figure expected to only touch 1.2% by 2023. The dovish guidance pushed new members into the negative-yielding sovereign debt club – the Portuguese 10-year, Spanish 10-year, and Italian 5-year yields printed below zero last week for the first time in recorded history.

The latest development continued to validate our bullish call on European High-Yield (HY) for 4Q20 (please refer to "New dawn for European HY", 28 Sep 2020). As at 11 December, European HY returned 8.3% (in USD terms) quarter to date – handily outperforming most other risky credit markets. In terms of Developed Markets comparisons, the return on European HY also trounced USD HY returns of 5.5% in the same period by 280 bps, again confirming our outlook that Europe was preferred over US in DM HY exposure (please refer to "Europe over US in DM HY", 7 Aug 2020). We believe credit will remain supported as central banks err on the side of dovishness as long as the economy remains some distance away from a complete recovery.

Daryl Ho | Strategist

FX: Risk rally that undermined USD has frozen

Figure 3: SNB meeting in focus

Source: Bloomberg, DBS

Wall Street on lockdown. New York City Mayor Bill de Blasio warned that the city could return to a full lockdown to break the second wave of coronavirus infections. The Dow and S&P 500 were lower for the fourth straight session by 0.6% and 0.4%, respectively, on Monday (14 December). Unlike last Wednesday, the Dow did not close marginally but more than 100 points below the key 30,000 level.

Until Congress puts aside their bipartisan differences, a US stimulus bill is still not in sight before Christmas. Apart from an imminent government shutdown this Friday, millions of Americans will lose their unemployment compensation benefits under the CARES Act when they expire on 26 December, and face eviction when a federal eviction moratorium expires on 31 December. With the US economy facing more downside risks in the short-term, **the risk rally that undermined the USD has also frozen**.

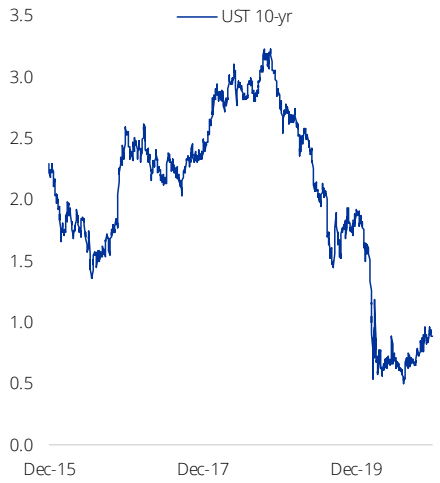
The US Treasury Department's semi-annual Currency Report could get released before Joe Biden's inauguration on 20 January. Newswires have been highlighting that Switzerland is at risk of being flagged as a currency manipulator. The Swiss National Bank (SNB) reported three months ago that interventions have amounted to CHF90b in 1H or 12% of gross domestic product (GDP) (above the 2% mark) to counter the flight to safety into the CHF during the COVID-19 outbreak. Current Account surpluses have been consistently above the 2% of GDP criteria; consensus expects them to exceed 8% in 2021 and 2022. America's bilateral trade deficit with Switzerland totalled USD79b in the first ten months, well above the USD20b threshold.

CHF players should pay close attention to the SNB meeting on Thursday. The SNB is set to publish data on forex operations which it has pledged to do so on a quarterly basis instead of annually. Although EUR/USD has yet to reach its 1.25 peak seen in 1Q18, CHF has surpassed its 2018 highs against USD and EUR, at 0.92 and 1.20, respectively. USD/CHF and EUR/CHF ended Monday at 0.8868 and 1.0772, accordingly. Taking the overall exchange rate situation into consideration, **the SNB is unlikely to change its guidance to not rule out deeper negative interest rates and stronger interventions to curb excessive CHF strength.**

Philip Wee | FX Strategist

Rates: Still a grind

Figure 4: Persistent uncertainties



Source: Bloomberg, DBS

The US Treasuries (UST) curve bull flattened modestly as risk appetite wobbled. Ten-year yields closed just below 0.90% as market participants worried about US fiscal stimulus and persistent uncertainties over Brexit talks. On the fiscal front, despite encouraging signs that the Democrats and the Republicans are closer to a deal, differences on State aid prevented an agreement from taking place. Instead, a one week stop gap bill was signed to prevent a government shutdown from taking place. It probably does not help that Brexit talks have hit an impasse, dragging down German and UK yields in the process. Interestingly, demand for longer tenor bonds appeared to have returned in the recent 30Y UST auction, suggesting that yields of around 1.70% is sufficient to entice investors.

Near-term US economic conditions are going to prove challenging. The labour market recovery has stalled amid a surge in coronavirus cases. Initial jobless claims and continuing claims surged to 853k and 5757k, respectively, much higher than what consensus had expected. A fiscal bridge is needed to tide the economy through before mass vaccinations can take place. While vaccine approvals can take place as early as this week (ending 18 December), it would still be months before herd immunity gets achieved. We are neutral on 10Y US yields at current levels, noting that the tight 0.80-1.0% range has held over the past few weeks. In the absence of fresh impetus, it might prove difficult for a breakout. On the upside, 1% is proving to be a tough hurdle to cross given still tough economic and COVID-19 conditions. On the downside, 10Y yields closer to 0.80% would present opportunities to pay as we await economic normalisation in 2021.

Eugene Leow | Rates Strategist

Duncan Tan | Rates Strategist

Thematics: Singapore REITs riding the winds of change

- Bulk of income disruption to be confined to 2020 as economy mends
- Nearly 60% of S-REITs projected to deliver above pre-COVID-19 distributions in 2021, supporting a further rally
- Yield spreads at more than 1SD provides sufficient buffer against a steepening yield curve
- Balanced approach in our picks; focus on names with sustainable growth and pipelines

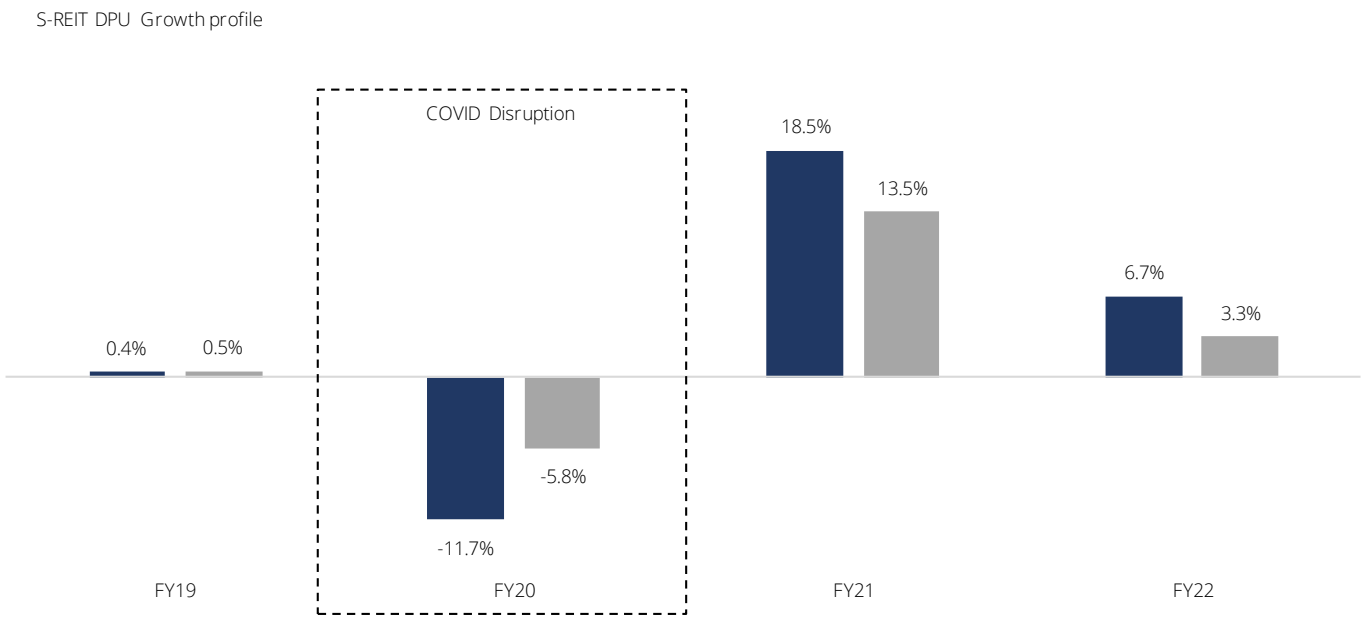
Leaving the pandemic behind; 60% of S-REITs under coverage to surpass pre-COVID-19 distributions. The income disruption to Singapore real estate investment trusts (S-REITs) caused by the COVID-19 pandemic has been unprecedented but should be largely confined within 2020. While we see new secular real estate trends emerging post-COVID-19 (e.g. greater adoption of online and flexible working arrangements, and disruption to selected industries), we believe that S-REITs, through strategic merger and acquisition (M&A) activities in 2020, will remain resilient. With the Singapore economy on the mend, we project S-REITs to deliver a c.19% (c.13% ex-hospitality) y/y distribution per unit (DPU) growth in 2021, with c.60% of S-REITs under DBS Group Research's coverage projected to deliver DPUs higher than pre-COVID-19 (as of FY19) levels.

Navigating past a steepening yield curve; wider-than-average yield spreads supports further yield compression. While the yield curve (10Y-2Y) is expected to steepen in 2021/2022 in line with stronger economic growth, we do not see this as a major hurdle for S-REITs. This is due to (i) its gradual steepening (25 bps over two years) and, (ii) a lower base effect. In fact, we believe that the wider-than-average FY21 yield spreads of c.5.0% (+1.0 standard deviation (SD)) coupled with robust growth rates and an extended low interest rate environment, will be catalysts to support a further rerating.

Venturing out for alpha in the new year. Our earlier call of preferring a more "risk-on" approach has worked (please see Singapore REITs: Turn of the tide, 1 Sep 2020). Looking ahead, we take a balanced approach in our picks of S-REITs in 2021, with a focus on growth and ability to deliver pre-pandemic DPUs in 2021. Logistics S-REITs, such as Mapletree Logistics Trust (MLT SP), are possible "vaccine plays" on demand for warehouse storage; while we believe retail S-REITs like Frasers Centrepoint Trust have the ability to deliver pre-COVID-19 DPUs, supported by dominant malls and possible pipeline injections. Commercial landlords with a diversified Grade A and suburban business park assets, such as Keppel REIT, will remain resilient despite possible shifts in office demand. Lastly, we continue to favour hospitality S-REITs like CDL Hospitality Trusts (CDREIT SP) for their robust DPUs growth as borders reopen.

Derek TAN | Analyst
Dale LAI | Analyst
Rachel TAN | Analyst
Geraldine WONG | Analyst

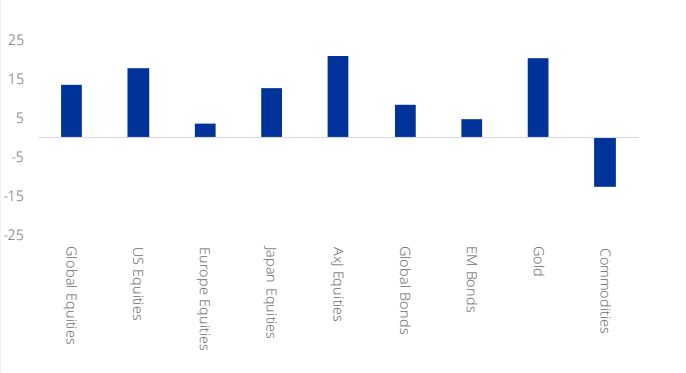
Figure 5: Growth profiles by subsector in 2021



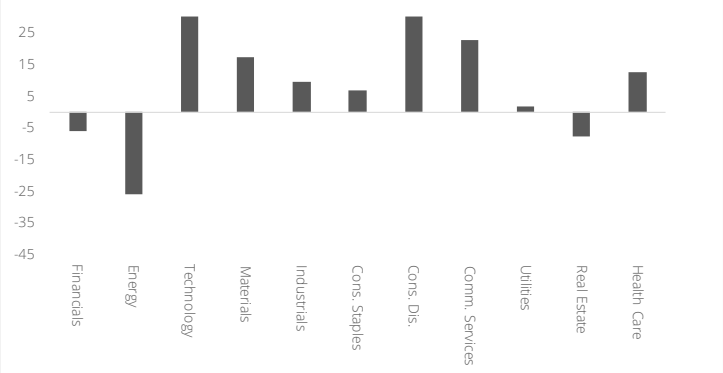
Source: Companies, DBS

CIO Markets Watch

Global Cross Assets YTD Returns

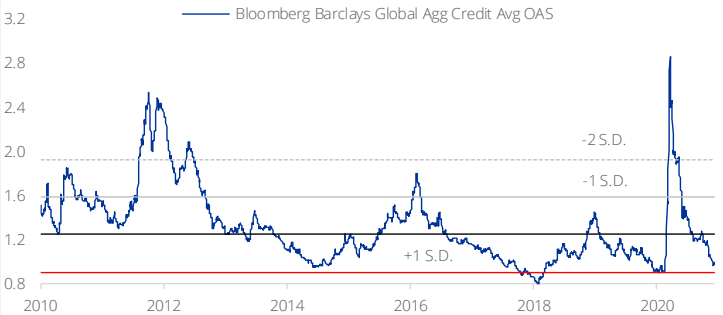


Global Sector YTD Returns



Global Equity Valuation

US Corporate Spreads



Index Returns

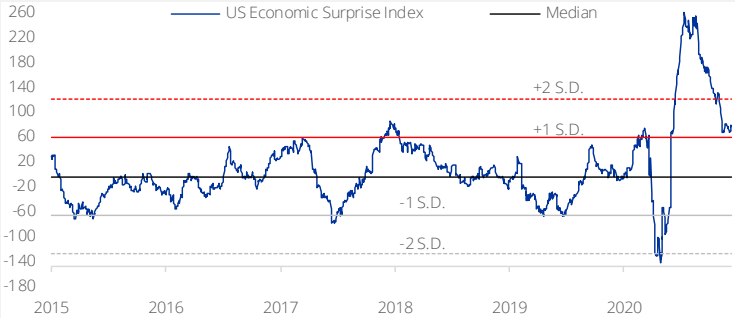
	1 week	MTD	QTD	YTD
Equities				
S&P 500	-1.2%	0.7%	8.5%	12.9%
NASDAQ	-0.6%	2.0%	11.4%	38.6%
Russell 2000	1.2%	5.2%	26.9%	14.7%
Stoxx Europe 600	-0.3%	0.6%	8.5%	-5.8%
Nikkei-225	0.7%	1.1%	15.3%	13.0%
MSCI WORLD	-0.6%	1.4%	10.7%	11.1%
MSCI ACWI	-0.6%	1.7%	11.3%	11.3%
MSCI Asia ex-Japan	-0.3%	3.0%	14.3%	18.3%
MSCI EM	-0.2%	3.8%	15.6%	12.2%
HSCEI	-0.3%	-1.0%	11.1%	-6.5%
SHCOMP	-1.4%	-0.7%	4.7%	10.5%
Hang Seng	-0.4%	0.2%	12.5%	-6.4%
STI Index	1.2%	1.9%	15.9%	-11.3%
Fixed Income				
Barclays Global Aggregate	0.2%	0.7%	2.6%	8.5%
Barclays US Aggregate	0.2%	-0.1%	0.4%	7.2%
Barclays US High Yield	0.1%	1.1%	5.6%	6.2%
Barclays Euro Aggregate	0.3%	0.4%	1.5%	4.3%
Barclays Euro High Yield	0.0%	0.5%	5.0%	1.4%
JPM EMBI Global	0.3%	0.9%	4.5%	4.9%
JPM EMBI Global Diversified	0.2%	0.7%	4.2%	4.8%

Prices & Spreads

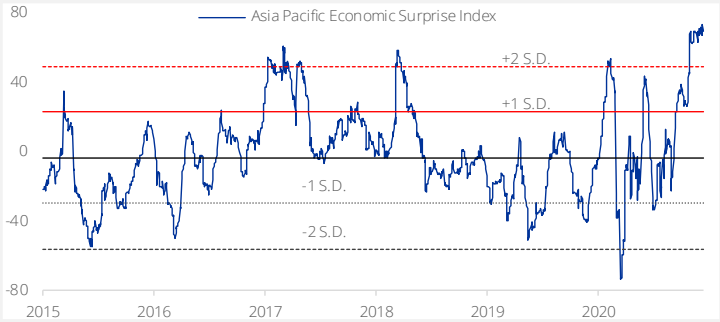
	Spot	2Q20	1Q20	4Q19
Rates				
Fed Funds Target	0.25	0.25	0.25	0.25
ECB Main Refinancing Rate	0.00	0.00	0.00	0.00
BOJ Policy Balance Rate	-0.10	-0.10	-0.10	-0.10
US Treasury 10-yr	0.89	0.69	0.66	0.67
Japanese Govt Bond 10-yr	0.01	0.01	0.02	0.01
German Bunds 10-yr	-0.62	-0.52	-0.46	-0.47
Spreads				
US Agg Corporate Spread	1.04	1.36	1.50	2.72
US Corporate HY Spread	3.82	5.17	6.26	8.80
Euro Agg Corporate Spread	0.96	1.23	1.53	2.41
EM USD Agg Spread	2.77	3.34	3.93	6.19
Currencies				
US Dollar Index (DXY)	90.7	93.9	97.4	99.0
EUR/USD	1.21	1.17	1.12	1.10
USD/JPY	104.1	105.5	107.9	107.5
USD/CNY	6.6	6.8	7.1	7.1
Commodities				
WTI Oil	47	40	39	20
London Metal Exchange (LMEX)	3455	2968	2682	2335
TR/CC CRB Commodity	162	149	138	122
Gold	1827	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)	17-Dec	Dec	815k	853k
FOMC Rate Decision (Upper Bound) (US)	16-Dec	Dec	0.25%	0.25%
CPI y/y (EU)	17-Dec	Nov	-0.30%	-0.30%
MBA Mortgage Applications (US)	16-Dec	Dec	--	-1.20%
Retail Sales Advance m/m (US)	16-Dec	Nov	-0.30%	0.30%
Industrial Production m/m (US)	15-Dec	Nov	0.30%	1.10%
Markit US Manufacturing PMI (US)	16-Dec	Dec	55.9	56.7
Markit Eurozone Manufacturing PMI (EU)	16-Dec	Dec	53	53.8

Macro Calendar

	Date	Period	Survey	Prior
Asia				
Non-oil Domestic Exports y/y (SG)	16-Dec	Nov	0.30%	-3.10%
Jibun Bank Japan PMI Mfg (JP)	15-Dec	Dec	--	49
Natl CPI y/y (JP)	17-Dec	Nov	-0.80%	-0.40%
BOJ Policy Balance Rate (JP)	17-Dec	Dec	--	-0.10%
Natl CPI Ex Fresh Food y/y (JP)	17-Dec	Nov	-0.90%	-0.70%
Trade Balance (JP)	15-Dec	Nov	¥522.5	¥872.9b
Jibun Bank Japan PMI Composite (JP)	15-Dec	Dec	--	48.1
Jibun Bank Japan PMI Services (JP)	15-Dec	Dec	--	47.8