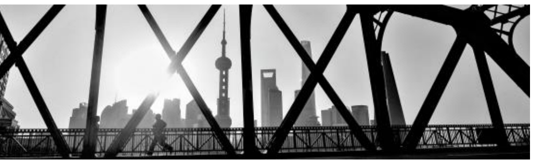


CIO Weekly

28 November 2022

Key Points

- Equities: Fed slowdown hopes see global equities up for the week, led by DM outperformance
- Credit: US HY credit provides insufficient compensation for risks ahead
- FX: EUR to correct lower from the top of 1.0220-1.0480 range; Cautious on GBP after the rise above 1.20 for the first week since 12 August
- Rates: All eyes on payrolls due on Friday; Reasonable chance for NFP to weaken in coming months
- Thematics: Semiconductor industry - Chip manufacturers in China most impacted; expect no immediate impact on equipment, software
- The Week Ahead: Keep a lookout for US Change in Nonfarm Payrolls; Japan Industrial Production Numbers

GLOBAL CROSS ASSETS

Returns of cross assets around the world

Index	Close	Overnight	YTD
DJIA	34,347	0.4%	-5.5%
S&P 500	4,026	0.0%	-15.5%
NASDAQ	11,227	-0.5%	-28.2%
Stoxx Europe 600	441	0.0%	-9.6%
DAX	14,541	0.0%	-8.5%
CAC 40	6,712	0.1%	-6.2%
FTSE 100	7,487	0.3%	1.4%
MSCI AxJ	599	-0.4%	-24.1%
Nikkei 225	28,283	-0.4%	-1.8%
SHCOMP	3,101	0.4%	-14.8%
Hang Seng	17,574	-0.5%	-24.9%
MSCI EM	941	-0.5%	-23.6%
UST10-yr yield*	3.6776	-1.5	216.8
JGB 10-yr yield*	0.25	0.6	18.5
Bund 10-yr yield*	1.971	12.4	215.3
US HY spread*	4.35	-1.0	152.0
EM spread*	400.44	-6.6	70.2
WTI (USD)	76.28	-2.1%	1.4%
LMEX	3777.2	-0.5%	-16.1%
Gold (USD)	1754.93	0.0%	-4.1%

Source: Bloomberg

* Changes in basis points

Equities: Global equities up as Fed signals step down in rate hikes

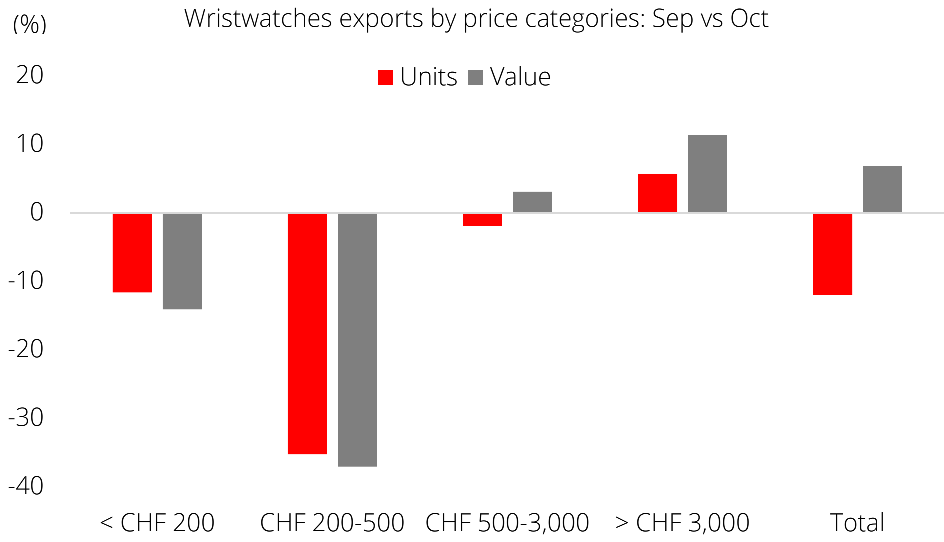
Dovish signals from Fed edge DM equities higher. Global equities rose for the week (ended 25 November) as minutes from the Fed's November meeting suggest a slowing of rate hikes through the end of the year. Global equities were up 1.5% for the week, with Developed Markets gaining 1.7% and Emerging Markets dipping 0.2%.

US ended the week in green ahead of thanksgiving with all three major indices recording gains; the S&P 500, Nasdaq and Dow Jones were up 1.5%, 0.7% and 1.8% respectively. Europe markets too extended their winning streak on Fed slowdown hopes; the Stoxx 600 and FTSE 100 rose 1.7% and 1.4% for the week. Asian equities again saw mixed performance. Malaysian stocks closed the week up 2.6% after Anwar Ibrahim was announced as the country's next prime minister; Hong Kong and China markets fell amid fresh Covid lockdown worries; HSCEI and Hang Seng were down 2.5% and 2.3% respectively.

Topic in focus: Luxury is not a proxy for the general economy. Companies in the luxury goods segment continue to beat expectations with strong sales posted in the latest results season. Appetite for luxury goods sales continues to rise as "revenge shopping", a weak euro, and easing of Covid-related lockdowns helped fuel growth for the sector despite a looming recession, sharply higher interest rates, and widespread inflation. These goods are sought after and regarded as new luxury by the Millennials, who are now in their prime spending years, as an expression for individuality, social status, and aspirations.

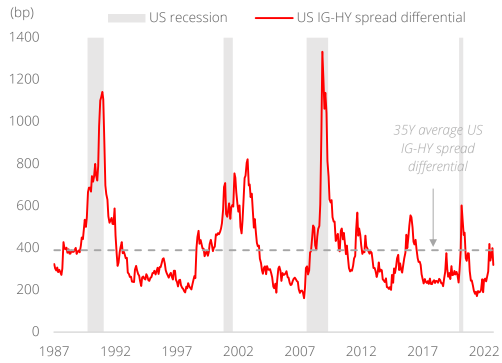
This trend in luxury sales is confirmed by the October exports data for Swiss watches. Notably, i) total exports have already surpassed 2019 pre-pandemic levels since last year, and grew another 10% year-to-date; ii) items in the higher price category (>CHF 3000) generated most of the growth; iii) steady growth is seen in high share markets such as the United States (+16.7%), Japan (+9.9%), and Singapore (+29.0%), while China (-18.1%) recorded negative growth; iv) over half the growth came from watches made from precious metals (+11.0%). Hence, the outlook is for luxury sales to climb higher when China further eases Covid lockdowns.

Figure 1: Stronger export growth seen in higher priced items



Source: Federation of the Swiss Watch Industry, DBS

Figure 2: Past recessions saw peaks in IG-HY spread differential



Source: Bloomberg, St Louis Fed, DBS
Dates of US recessions as inferred by NBER GDP-based recession indicator

Credit: US HY provides insufficient compensation for risks ahead

As a challenging year soon comes to a close with tightening financial considerations around the world feeding concerns regarding a deteriorating growth outlook, we continue to advocate an up-in-quality stance in credit, favouring Investment Grade (IG) over High Yield (HY). Although various economic indicators in the US appear resilient, we are mindful that we are now in the thick of the Fed's most aggressive rate hiking cycle in decades. With increasing pressures on corporate balance sheets, lagging economic indicators could have some catching up to do before the impact of elevated rates works its way through the system.

As illustrated in Figure 2, although the credit spread differential between US IG and HY has widened considerably since the start of this year, this differential remains below its long-run average. Considering a worsening economic environment in the cards, this suggests that US HY is offering investors insufficient compensation for its additional risks over IG. Our analysis of past data shows that that all recessions over the past 35 years were accompanied by spikes in this differential as investors demanded additional compensation for HY credit in periods seeing heightened default risks. This suggests that should the macroeconomic environment deteriorate, a similar widening would likely come to pass, causing HY to underperform IG. This reiterates our preference for high quality credit in light of the looming macro uncertainties.

Figure 3: Rangebound

Source: Bloomberg, DBS

FX: Not underestimating the USD this week

DXY consolidated between 105.3 and 108 over the past fortnight after its sell-off from a high of 113.2 on 3 November. Although markets see a smaller 50 bps hike on 14 December, the US Treasury 10Y yield ended last week (ended 25 November) at 3.68%, beneath the 3.75-4% Fed Funds Rate. Given the Fed's intention to target a higher 2023 rate above the 4.6% set in September, Fed Chair Jerome Powell will need to sound hawkish when he discusses the economy and labour market on 30 November. If Powell successfully lifts the 10Y bond yield, the DXY could recover some of this month's losses.

Although US Consumer Price Index (CPI) and core inflation slowed to 7.7% y/y and 6.3% respectively in October, the readings were too high above the 2% target for the Fed to lower its guard. The same can be said for the lower readings expected in Thursday's October Personal Consumption Expenditures' deflator (6% consensus) and core inflation (5% consensus). On Friday's jobs report, the fewer 200k nonfarm payrolls consensus expects for November will be high relative to pre-Covid levels. November's CPI inflation readings, which come a day before the Federal Open Market Committee meeting, could surprise on the upside.

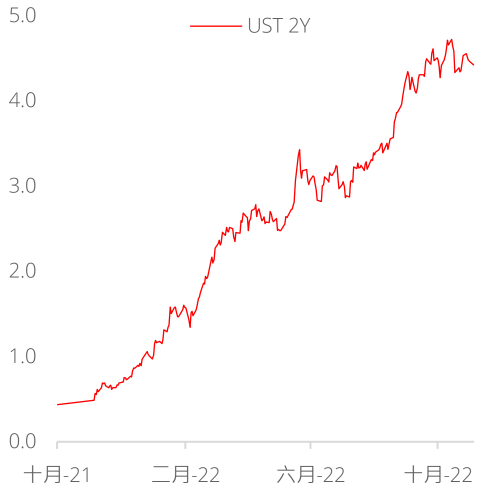
EUR could correct lower from the top of its 1.0220-1.0480 range of the past fortnight. The European Central Bank (ECB) believes that monetary policy is not restrictive enough to lower double digit inflation to its 2% target. On 30 November, consensus sees CPI inflation slowing to 10.4% y/y in November from 10.7% in October and core inflation unchanged at 5%. Unfortunately, the Eurozone is entering a technical recession in 4Q22 and 1Q23. Hence, the ECB is leaning towards a smaller 50 bps hike on 15 December after the jumbo 75 bps hike on 27 October. At the same meeting, the governing council will discuss the "key principles" of quantitative tightening without announcing a start date. Expect Bundesbank President Joachim Nagel to push the ECB to reduce its bond holdings at the start of 2023. Nagel and ECB President Christine Lagarde are speaking on 28 November and 2 December.

We are cautious about GBP after it rose above 1.20 for the first week since 12 August. GBP is well above its pre-mini budget level of 1.13 and has rebounded 17% from its new all-time low of 1.0350 on 26 September. Although the Conservative Party has dismantled the minibudget and elected a new prime minister, inflation continued to double-digit levels, with the UK economy falling below pre-Covid levels. The bets for more rate hikes by the Bank of England will exacerbate the UK recession, also feeling the drag from fiscal spending cuts. There is no guarantee that the downturn will not extend beyond the expected four quarters into 2Q23. In September, consensus first predicted - 0.2% growth in 2023, an outlook that has deteriorated to -0.4% in November and -0.8% last week. Not surprisingly, Commodity Futures Trading Commission data showed the GBP's recovery from unwinding short positions instead of accumulating long positions. In short, GBP is vulnerable if the USD regains some composure this week from the Fed and US data.

DBS Currency Forecasts

CCY pair, eop	25 Nov	4Q22	1Q23	2Q23	3Q23	4Q23
USDCNY	7.1650	7.25	7.20	7.15	7.10	7.05
USDHKD	7.8134	7.85	7.84	7.83	7.82	7.81
USDINR	81.686	82.3	81.6	80.9	80.1	79.4
USDIDR	15,673	15,300	15,120	14,930	14,750	14,560
USDMYR	4.4843	4.70	4.65	4.60	4.55	4.50
USDPHP	56.695	60.0	59.0	58.0	57.0	56.0
USDSGD	1.3768	1.43	1.42	1.42	1.41	1.40
USDKRW	1,324	1,430	1,390	1,360	1,330	1,300
USDTHB	35.737	39.0	38.4	37.8	37.1	36.5
USDVND	24,802	23,880	23,820	23,760	23,700	23,640
AUDUSD	0.6751	0.63	0.64	0.66	0.67	0.68
USDCAD	1.3380	1.35	1.34	1.32	1.31	1.30
EURUSD	1.0395	0.96	0.98	1.00	1.02	1.04
USDJPY	139.19	150	145	141	136	132
NZDUSD	0.6247	0.59	0.60	0.61	0.63	0.64
USDCHF	0.9459	1.00	0.99	0.98	0.97	0.96
GBPUSD	1.2092	1.11	1.13	1.15	1.16	1.18
DXY Index	105.96	115.0	112.8	110.6	108.4	106.2

Figure 4: Peaked?



Source: Bloomberg, DBS

Rates: NFP watch

US Treasuries have rallied significantly this month. This was led by the long end with 10Y and 30Y yields down by 53 bps and 59 bps respectively from their respectively peaks in early November. Fundamentally, there has only been a single clear trigger – this miss in headline CPI. While a single better CPI print should not be viewed as a trend, market participants are perhaps more sensitive to downside risks. Couple that with Fed forward guidance that have decisively turned less hawkish, the market is no longer trying to push the terminal rate above 5%. It probably does not help that liquidity appears to be poor as attention shifts to the World Cup.

Ultimately, large moves in this period might turn out to be more noise than signal. This week (ending 2 December), all eyes will be on payrolls due on Friday. As inflation and the Fed show tentative signs of downshifting, it is the resilient labour market that is preventing a further fall in 2Y UST yields. We think that there is a reasonable chance that that NFP will weaken in the coming months. Announced layoffs (especially in the tech space) might take some time before hitting NFP figures and higher rates need time to filter into the real economy.

Thematics: Semiconductor – How will the chip war play out?

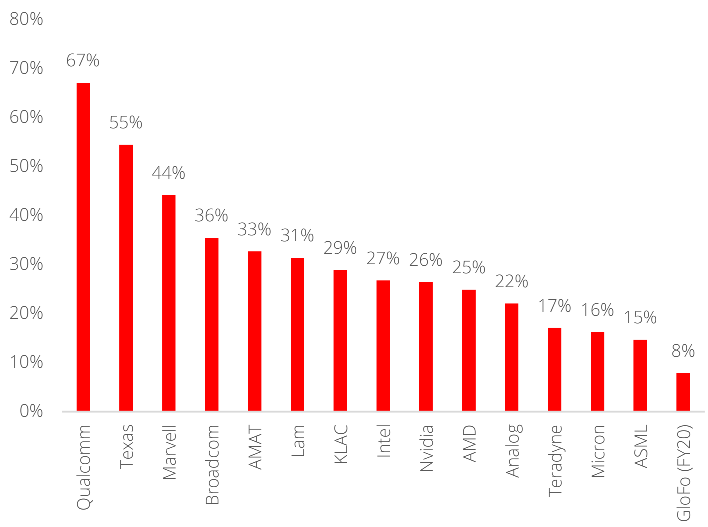
- Chips at the centre of the US-China tech war, chip manufacturers in China most impacted
- Expect no immediate impact on equipment, software
- Global companies are not spared but various mitigating factors to safeguard their businesses
- We explore bull, base and bear case of this development and possible impact

Chip manufacturers in China most impacted. Among Chinese companies, we see the most impact on chip manufacturers (Integrated Device Manufacturer/fabrication-less), followed by foundries. We do not expect a material impact to equipment manufacturers and software developers, as China's current technology is way behind the thresholds mentioned in the latest curbs.

Less negative on global companies, with mitigating factors in play. Temporary licenses, relatively smaller contributions from advanced chips and related equipment from China, as well as companies exploring options to bypass the US ban such as the modification of chips and production processes have made us less negative now. Our bear case scenario, though less likely, assumes an extension of the ban, such as to include less advanced chips. This could even affect the entire technology value chain, including material and component suppliers and packaging and assembly divisions.

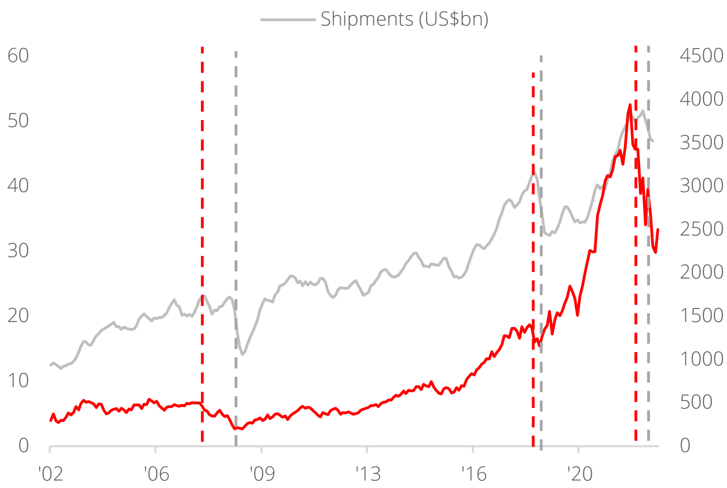
Stock market moves ahead of industry. DBS expects the semiconductor industry to trend lower in the next few months, with worldwide semiconductor shipment growth to dip further and enter negative growth territory. We prefer stocks with technology leadership and trade diversification to ride on China's semiconductor localisation trend.

Figure 5: Last FY % Revenue Contribution from China



Source: Bloomberg, DBS

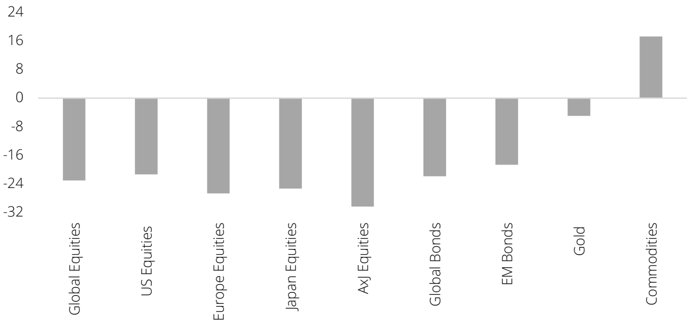
Figure 6: SOX vs. global semiconductor shipments



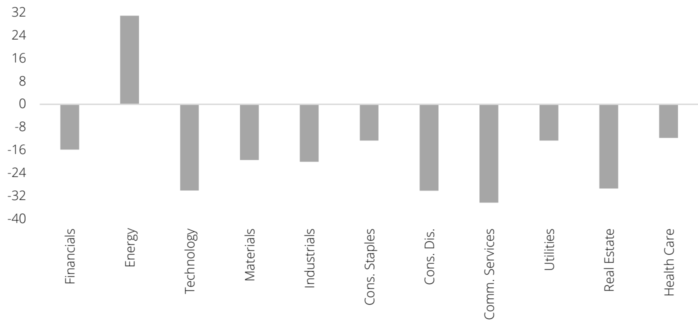
Source: SIA, CEIC, Refinitiv, DBS

CIO Markets Watch

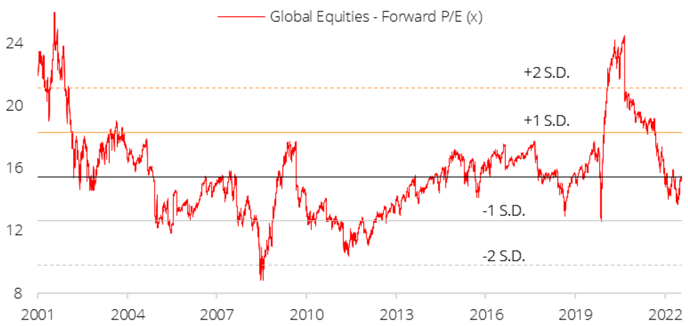
Global Cross Assets YTD Returns



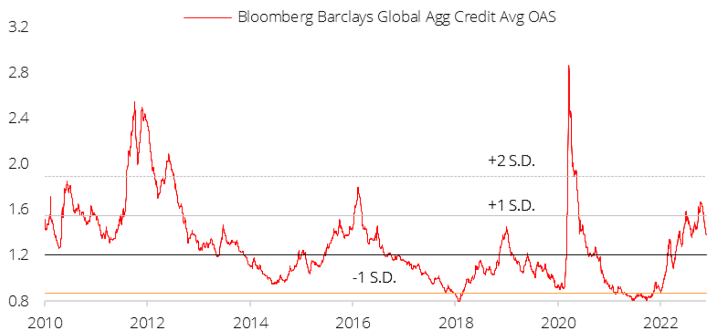
Global Sector YTD Returns



Global Equity Valuation



US Corporate Spreads



INDEX RETURNS

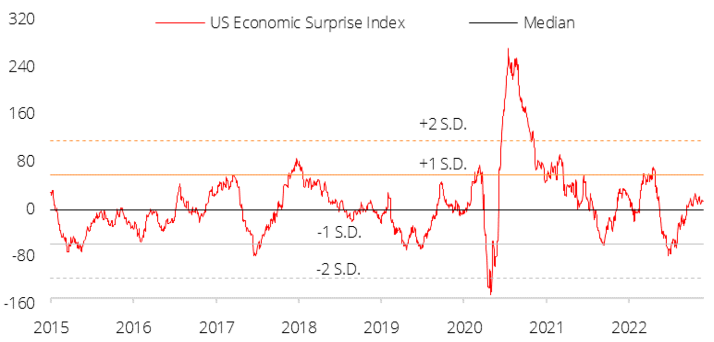
	1 week	MTD	QTD	YTD
Equities				
S&P 500	1.5%	4.0%	12.3%	-15.5%
NASDAQ	0.7%	2.2%	6.2%	-28.2%
Russell 2000	1.1%	1.2%	12.3%	-16.8%
Euro Stoxx 600	1.7%	6.9%	13.6%	-9.6%
Nikkei-225	1.4%	2.5%	9.0%	-1.8%
MSCI WORLD	1.7%	6.1%	13.7%	-16.3%
MSCI ACWI	1.5%	6.6%	13.0%	-17.2%
MSCI Asia ex-Japan	-0.4%	14.4%	7.4%	-24.1%
MSCI EM	-0.2%	10.9%	7.4%	-23.6%
HSCEI	-2.5%	20.9%	1.0%	-27.5%
SHCOMP	0.1%	7.2%	2.6%	-14.8%
Hang Seng	-2.3%	19.7%	2.0%	-24.9%
STI Index	-0.8%	4.9%	3.7%	3.9%
Fixed Income				
Barclays Global Aggregate	0.9%	5.0%	4.3%	-16.5%
Barclays US Aggregate	1.1%	3.5%	2.1%	-12.8%
Barclays US High Yield	1.1%	2.2%	4.8%	-10.6%
Barclays Euro Aggregate	0.5%	2.2%	2.3%	-14.2%
Barclays Euro High Yield	1.3%	3.7%	5.8%	-10.2%
JPM EMBI Global	1.5%	6.2%	6.3%	-17.4%
JPM EMBI Global Diversified	1.6%	6.2%	6.6%	-19.9%

PRICES & SPREADS

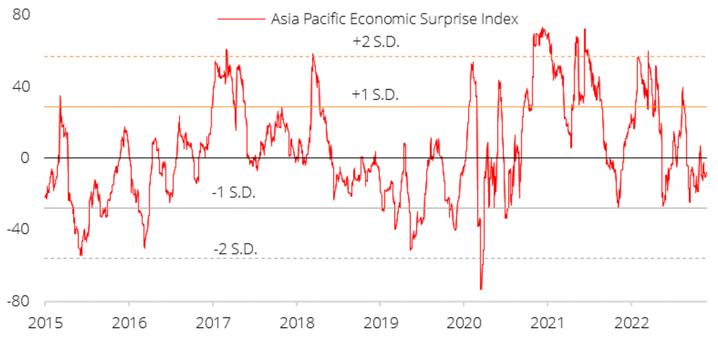
	Spot	3Q22	2Q22	1Q22
Rates				
Fed Funds Target	4.00	3.25	1.75	0.50
ECB Main Refinancing Rate	2.00	1.25	0.00	0.00
BOJ Policy Balance Rate	-0.10	-0.10	-0.10	-0.10
US Treasury 10-yr	3.68	3.83	3.02	2.34
Japanese Govt. Bond 10-yr	0.25	0.24	0.23	0.21
German Bunds 10-yr	1.97	2.11	1.33	0.55
Spreads				
US Agg Corporate Spread	1.30	1.59	1.55	1.16
US Corporate HY Spead	4.35	5.52	5.69	3.25
Euro Agg Corporate Spread	1.84	2.25	2.15	1.31
EM USD Agg Spread	3.60	4.03	4.04	3.13
Currencies				
US Dollar Index (DXY)	106.0	112.1	104.7	98.3
EUR/USD	1.04	0.98	1.05	1.11
USD/JPY	139.2	144.7	135.7	121.7
USD/CNY	7.2	7.1	6.7	6.3
Commodities				
WTI Oil	76	79	106	100
London Metal Exchange (LMEX)	3777	3541	3879	5174
TR/CC CRB Commodity	273	268	291	295
Gold	1755	1661	1807	1937

CIO Economics Watch

US Economic Surprise Index



Asia Pacific Economic Surprise Index



MACRO CALENDAR

	Date	Period	Survey	Prior
United States & Eurozone				
Change in Nonfarm Payrolls (US)	2-Dec	Nov	200k	261k
Initial Jobless Claims (US)	1-Dec	26-Nov	231k	240k
GDP Annualised q/q (US)	30-Nov	3Q	2.80%	2.60%
ISM Manufacturing (US)	1-Dec	Nov	49.8	50.2
Conf Board Consumer Confidence (US)	29-Nov	Nov	99.9	102.5
MBA Mortgage Applications (US)	30-Nov	Nov-25	--	2.20%
S&P Global Eurozone Mfg PMI (EU)	1-Dec	Nov	47.3	47.3
S&P Global US Mfg PMI (US)	1-Dec	Nov	47.6	47.6

MACRO CALENDAR

	Date	Period	Survey	Prior
Asia				
Industrial Production MoM (JP)	29-Nov	Oct	-1.80%	-1.70%
Jobless Rate (JP)	28-Nov	Oct	2.50%	2.60%
Manufacturing PMI (CN)	29-Nov	Nov	49	49.2
Caixin China PMI Mfg (CN)	30-Nov	Nov	48.9	49.2
Jibun Bank Japan PMI Mfg (JP)	30-Nov	Nov	--	49.4
Job-To-Applicant Ratio (JP)	28-Nov	Oct	1.35	1.34
Capital Spending y/y (JP)	30-Nov	3Q	6.40%	4.60%
Purchasing Managers Index (SG)	2-Dec	Nov	49.5	49.7

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