CIO Weekly
GLOBAL MULTI-ASSET

29 May 2023

Key Points

- Equities: Tech run-up on Thursday not enough to prevent another losing week for global equities
- FX: Upcoming US jobs data vital to extend the DXY's uptrend in upper half of 101-106 range; EUR weakness persist amid technical recession in Germany
- Rates: USD rates space turned decidedly hawkish amidst optimism over debt ceiling, removal of imminent banking sector worries and resilient data
- Thematics: The improving global auto market and rising EV sales of foreign OEMs in China prove to be positive on the auto parts company sector
- The Week Ahead: Keep a lookout for US Change in Nonfarm Payrolls; Japan Industrial Production Numbers

GLOBAL MULTI-ASSET RETURNS

Index	Close	Overnight	YTD
DJIA	33,093	1.0%	-0.2%
S&P 500	4,205	1.3%	9.5%
NASDAQ	12,976	2.2%	24.0%
Stoxx Europe 600	461	1.1%	8.6%
DAX	15,984	1.2%	14.8%
CAC 40	7,319	1.2%	13.1%
FTSE 100	7,627	0.7%	2.4%
MSCI AxJ	625	0.9%	0.9%
Nikkei 225	30,916	0.4%	18.5%
SHCOMP	3,213	0.4%	4.0%
Hang Seng	18,747	0.0%	-5.2%
MSCI EM	973	0.9%	1.7%
UST10-yr yield*	3.80	-1.9	-7.7
JGB 10-yr yield*	0.41	-0.7	0.1
Bund 10-yr yield*	2.54	1.6	-2.8
US HY spread*	4.46	-7.0	-23.0
EM spread*	400.62	3.1	26.4
WTI (USD)	72.67	1.2%	-9.5%
LMEX	3,654.70	1.5%	-8.3%
Gold (USD)	1,946.46	0.3%	6.7%

Source: Bloomberg
* Changes in basis points

Equities: Markets mixed as US reaches debt ceiling deal

Global equities ended mixed amid debt ceiling negotiations. Markets were once again weighed down last week (ended 26 May) by US debt ceiling negotiations and the worsening economic outlook in Europe as Germany slips into recession for 1Q. Global equities were down 0.5% for the week, with Developed Markets and Emerging Markets losing 0.5% and 0.4% respectively.

US equities rallied higher last Thursday (25 May), after higher-than-expected forecasts from Nvidia triggered a frenzied run up in the technology-heavy Nasdaq composite, which was up 2.5% for the week and +24% YTD. S&P 500 and Dow Jones ended the week up 0.3% and down 1.0% respectively. Europe closed lower for the week as optimism weakens after its largest economy, Germany fell into recession after reporting -0.3% GDP growth for 1Q; the Stoxx 600 and FTSE 100 lost 1.6% and 1.7% respectively. China equities closed lower across the board with industrial output, retail sales, and fixed asset investments all growing at weaker than expected pace, prompting investors to question if the post-pandemic recovery is losing momentum; the SHCOMP and HSCEI lost 2.2% and 3.9% respectively.

Topic in focus: **Favour China State-owned Banks**. China financials have delivered good performance since the conclusion of China's Party Congress in end October 2022 where regulators strengthen oversight of the USD60t financial system. Since 2017, deleveraging campaigns pushed by regulators meant that Chinese banks have healthier balance sheets and higher liquidity. YTD, China's banking index has returned c.22% gains driven by:

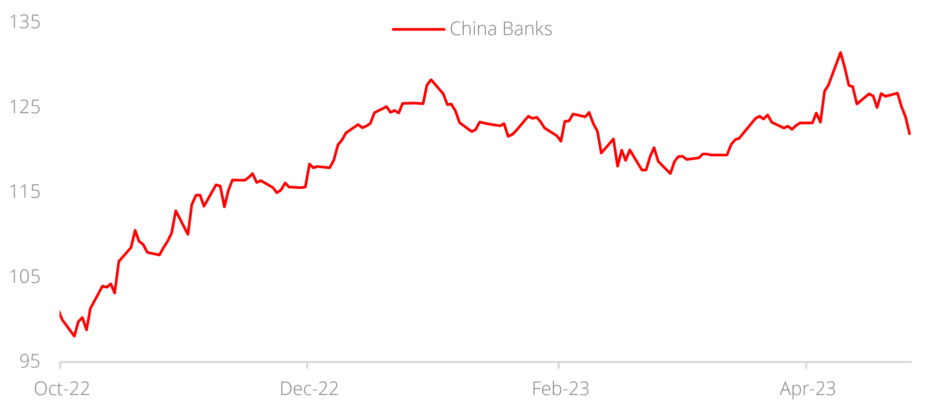
i. Expectations of US rate hikes coming to an end. This development should reverse the yield compression between China large banks and bonds

ii. Narrowing of steep valuation discounts

iii. Resumption in total social financing growth to 11.7%, back to the level last seen in January 2022

We remain constructive on China's state-owned enterprise (SOE) banks as the strong balance sheets and sustainable dividend yields (8.46% in 2023) makes them an attractive income generating building block within the barbell portfolio.

Figure 1: China Banks performance



Source: Bloomberg, DBS

FX: US Debt ceiling vote and monthly jobs data

Figure 2: All eyes on jobs data

Source: Bloomberg, DBS

This Friday's US monthly jobs report will be vital to extend the DXY's uptrend in the upper half of this year's 101-106 range. Interest rate futures priced in a 69% chance for a 25 bps hike to 5.25-5.5% at the Federal Open Market Committee meeting on 14 June. Bloomberg consensus expects US nonfarm payrolls to slip below 200k to 173k in May from 230k in April, as the unemployment rate rises to 3.5% from 3.4%, and average hourly earnings remain unchanged at 4.4%. Last Friday, the PCE deflator rose by a faster rate of 0.4% m/m (4.4% y/y) in April from 0.1% m/m (4.2% y/y) in March. Core PCE deflator was also stronger at 0.4% m/m (4.7% y/y) vs 0.3% m/m (4.6% y/y) in March. On 31 May, Richmond Fed President Thomas Barkin should reaffirm that the US labour market has not cooled enough for the Fed to close the door for more hikes to return inflation to its 2% target.

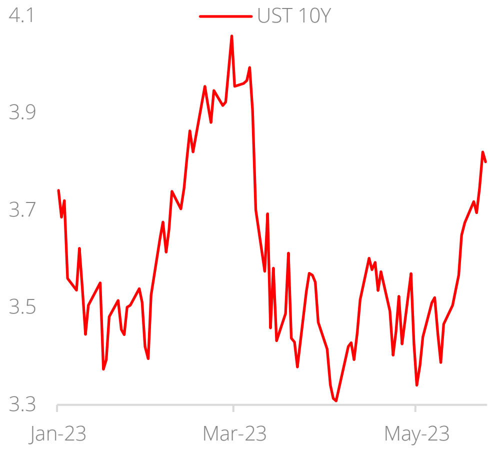
With a US debt default considered extremely negative for the US economy, the Fed will need Congress to pass the weekend's "in principle" agreement between the White House and the Republicans to raise the USD31.4t federal debt ceiling. So pay attention to the vote in the US House of Representatives on 31 May for progress to avert a US debt default on 5 June, the new X-date by US Treasury Secretary Yellen.

EUR depreciated a third week by 0.8% to a two-month low of 1.0723, into the lower half of this year's 1.05-1.11 range. Germany revised 1Q23 GDP growth to -0.3% q/q sa (-0.2% y/y nsa) 1Q23 from its preliminary 0% growth (0.2% y/y nsa) a month earlier and sent Eurozone's largest economy into a technical recession. With the country's ZEW Sentiment Index plunging to -10.7 in May from 4.1 in April and an average of 19.3 in 1Q23, the German government probably regretted last month's decision to upgrade this year's growth forecast to 0.4% from 0.2%. On 31 May, consensus expects Germany's CPI inflation to slow to a preliminary 0.2% m/m (6.4% y/y) in May from 0.4% m/m (7.2% y/y) in April, and a day later, Eurozone's CPI inflation declining to a preliminary 0.2% m/m (6.3% y/y) in May from 0.6% m/m (7% y/y). This week, European Central Bank officials will likely maintain the narrative for the hiking cycle to peak after two more rate increases in June-July.

GBP depreciated by 0.8% to 1.2344 a third week, back inside the first quarter's 1.18-1.2450 range. Although the IMF stopped predicting a UK recession, the economy could still stumble into one. CPI inflation finally declined to 8.7% y/y in April after seven months of double-digit readings, allowing the Bank of England to join the Fed in downsizing hikes to "normal" 25 bps in March and May. Unfortunately, inflation is still well above the 2% target, made worse by core inflation hitting a 31-year high of 6.8% in April. With food prices at 41-year highs, the Tory government plans to cap basic food prices at supermarkets. Chancellor of the Exchequer Jeremy Hunt supported more hikes to lower inflation even at the expense of a recession. However, higher borrowing costs add to the government's debt interest bill and consumers' mortgage payments. In late May, an Ipsos poll showed two out of three Britons expect the opposition Labour Party to win the most seats at the general elections due in January 2025. We cannot rule out Prime Minister Rishi Sunak facing Tory rebellion like his predecessors.

Rates: Market shifts hawkish

Figure 3: 10Y UST Yield heads above crisis range



Source: Bloomberg, DBS

The USD rates space turned decidedly hawkish over the past week amidst a combination of optimism over the debt ceiling, removal of imminent banking sector worries, and resilient data. Over the weekend, a tentative deal was also reached between the White House and the Republicans which would see the debt ceiling suspended through January 2025 in return for capping spending (ex defence). A vote is being set up for Wednesday, a few days before the new X-date of 5 June.

Keeping these developments in mind, we lay out some thoughts below. First, we think that the rates space has already factored in a fair amount of good news from the debt ceiling lifting. It probably also helps that the spending cuts appear modest. There might be another pop higher in yields when the US bond market reopens on Tuesday (30 May), but we think room for more optimism to be priced might be limited. Second, the market has pared banking sector worries. Banking stocks appeared to have stabilised, deposit outflows have cooled, and banks are not borrowing as much from the Fed's discount facility. This is reflected from 2Y and 10Y yields firmly breaching above their respective banking sector ranges and are now back at levels consistent to a hawkish Fed back in early March. Third, we note that implied 1Y and 2Y real yields are near cycle highs (very tight by recent standards). Interestingly, market stresses appear minimal.

Overall, the market has switched from downside worries (pricing in imminent Fed cuts) to upside worries (pricing in a high chance of a hike by July). Our 2Y yield forecast looks low compared to spot as we see the Fed on hold and also factored in some recession risk premium in Treasuries. While we acknowledge that the risk of another Fed hike has risen, downside risks appear to have faded and data has proven generally resilient. It may well come down to whether the Fed needs to see labour market weakness, not just cooling inflation. We get another reading of NFP this Friday. Meanwhile, 10Y yields are closing in on our forecast of 3.90%. We will be watching for signs of exhaustion in UST selling after the sizable yield adjustments. In addition, we will watch for signs of stresses in financial conditions or when 2Y/10Y segment of the curve gets to -80 bps to gauge for overextension. We reiterate our receive bias, especially for the longer tenors (10Y and 30Y).

Thematics: China Auto Sector – A shake-up in foreign brands' EV strategy

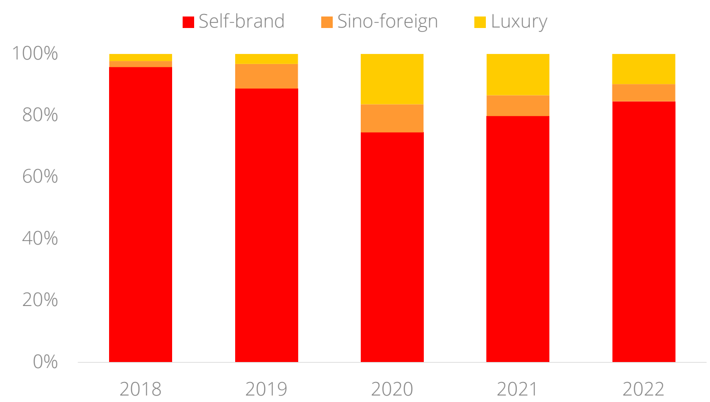
- Foreign brands sharpening EV strategy with faster new EV launches to strengthen market position; positive on parts producers
- Western OEMs ahead in EV penetration compared to Asian OEMs currently
- Expect foreign brands' EV market share to expand in medium term; but Chinese brands will still dominate

A wake-up call for foreign automakers to adopt an offensive EV strategy. The low new energy vehicle (NEV) market share of foreign brands in China is a result of their global electric vehicle (EV) strategy. Based on their FY22 sales mix, all these brands are still relying on international combustion engine vehicles for the bulk of their profits. Hence, they have limited EV products for the Chinese market. However, DBS believes the pace is expected to change, with the American and European automakers speeding up their battery electric vehicle (BEV)/plug-in hybrid electric vehicle (PHEV) development. The Asian automakers such as Toyota, Honda, and Hyundai are going down the fuel cell electric vehicle (FCEV) route as part of their long-term decarbonisation plan while their BEV/PHEV strategy is being shaped up.

Foreign brands' EV market share to scale higher. Following the execution of their EV strategy, the overall EV market share of foreign brands is expected to hit 9-10% in the coming 4-5 years, up from approximately 5.6% in 2022. Luxury original equipment manufacturers (OEMs), led by the German brands, are set to capture a mid-teens share, up from 9.8%. Currently, the German OEMs like Volkswagen are slightly ahead of the Asian OEMs in their electrification pace. Overall, the Chinese brands will continue to dominate.

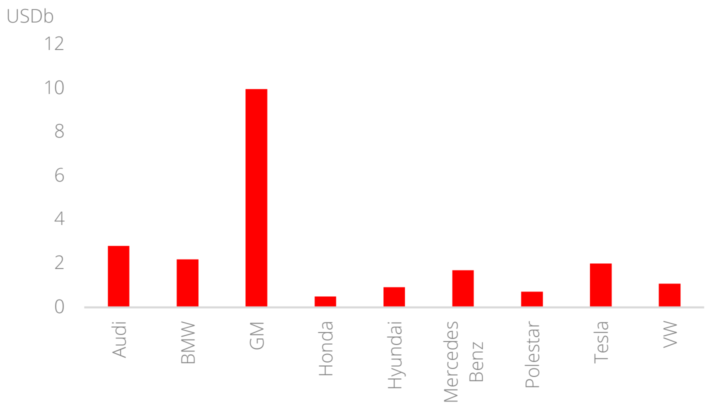
Our recommendation. The global vehicle market has recorded decent expansion in April, with China, Europe, and the US at 80%, 17%, and 9%, respectively. We reiterate that the improving global auto market and rising EV sales of foreign OEMs in China to be positive on the auto parts company sector. We also expect the Chinese PV market to chalk up around 1.8m units in sales in May, given the strong momentum in the first two weeks of the month. To ride on the Chinese market recovery, we continue to like automakers.

Figure 4: NEV penetration by auto brands



Source: CPCA

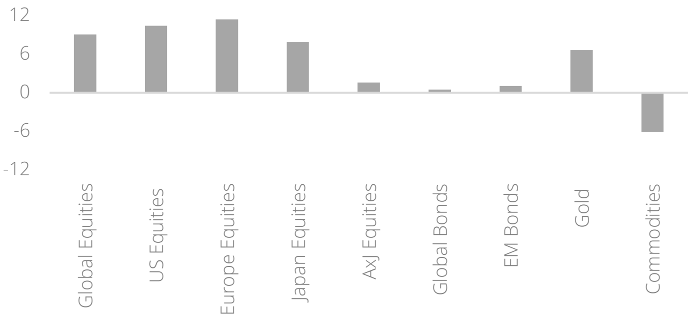
Figure 5: Foreign automakers' EV investment strategy (2023-2027)



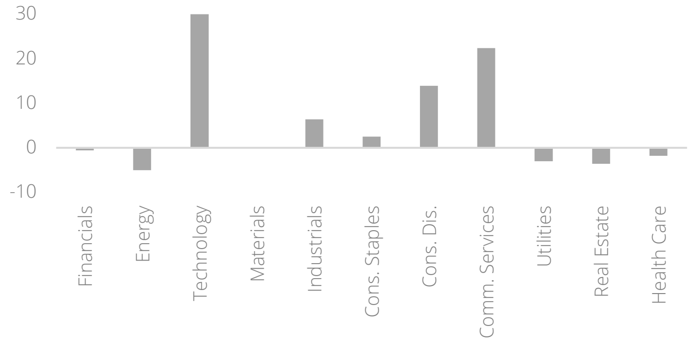
Source: Companies

CIO Markets Watch

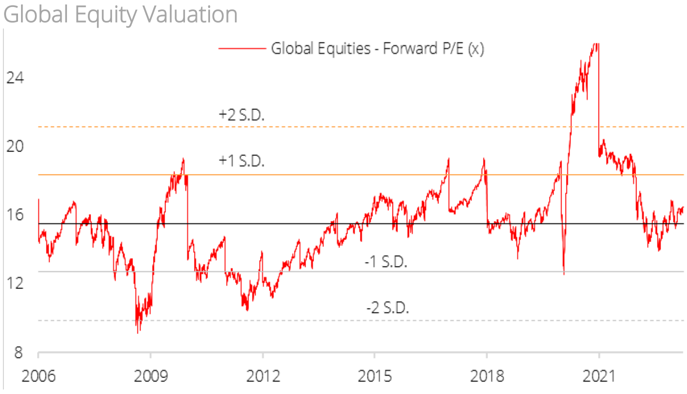
Global Cross Assets YTD Returns



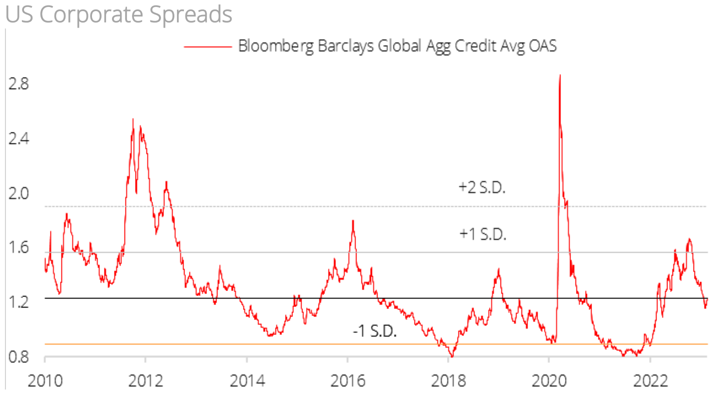
Global Sector YTD Returns



Global Equity Valuation



US Corporate Spreads



Source: Bloomberg, DBS

INDEX RETURNS

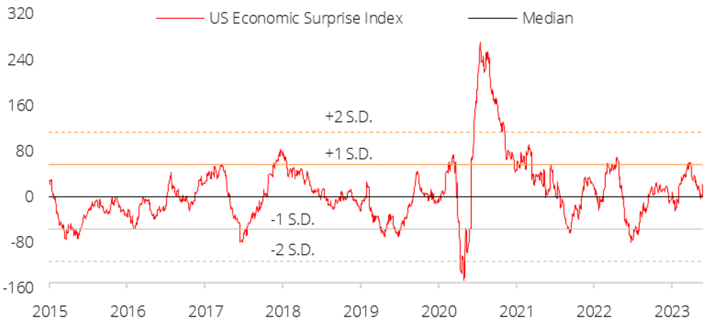
	1 week	MTD	QTD	YTD
Equities				
S&P 500	0.3%	0.9%	2.3%	9.5%
NASDAQ	2.5%	6.1%	6.2%	24.0%
Russell 2000	0.0%	0.2%	-1.6%	0.7%
Euro Stoxx 600	-1.6%	-1.1%	0.8%	8.6%
Nikkei-225	0.4%	7.1%	10.3%	18.5%
MSCI WORLD	-0.5%	-0.3%	1.3%	8.7%
MSCI ACWI	-0.5%	-0.3%	1.0%	7.9%
MSCI Asia ex-Japan	-0.5%	-0.9%	-3.0%	0.9%
MSCI EM	-0.4%	-0.4%	-1.8%	1.7%
HSCEI	-3.9%	-5.5%	-9.1%	-5.5%
SHCOMP	-2.2%	-3.3%	-1.8%	4.0%
Hang Seng	-3.6%	-5.8%	-8.1%	-5.2%
STI Index	0.1%	-1.9%	-1.6%	-1.4%
Fixed Income				
Barclays Global Aggregate	-1.1%	-2.9%	-2.5%	0.5%
Barclays US Aggregate	-0.7%	-2.3%	-1.7%	1.2%
Barclays US High Yield	-0.4%	-1.2%	-0.2%	3.3%
Barclays Euro Aggregate	-0.6%	-1.3%	-1.2%	0.9%
Barclays Euro High Yield	-0.2%	0.5%	1.0%	4.0%
JPM EMBI Global	-0.4%	-1.7%	-1.2%	1.0%
JPM EMBI Global Diversified	-0.5%	-1.5%	-0.8%	1.2%

PRICES & SPREADS

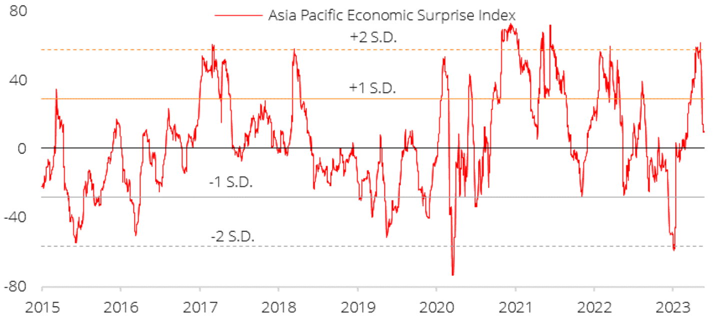
	Spot	1Q23	4Q22	3Q22
Rates				
Fed Funds Target	5.25	5.00	4.50	3.25
ECB Main Refinancing Rate	3.75	3.50	2.50	1.25
BOJ Policy Balance Rate	-0.10	-0.10	-0.10	-0.10
US Treasury 10Y	3.80	3.47	3.88	3.83
Japanese Govt. Bond 10Y	0.41	0.33	0.41	0.24
German Bunds 10Y	2.54	2.29	2.57	2.11
Spreads				
US Agg Corporate Spread	1.37	1.38	1.30	1.59
US Corporate HY Spread	4.46	4.55	4.69	5.52
Euro Agg Corporate Spread	1.68	1.72	1.70	2.25
EM USD Agg Spread	3.44	3.52	3.32	4.03
Currencies				
US Dollar Index (DXY)	104.2	102.5	103.5	112.1
EUR/USD	1.07	1.08	1.07	0.98
USD/JPY	140.6	132.9	131.1	144.7
USD/CNY	7.1	6.9	6.9	7.1
Commodities				
WTI Oil	73	76	80	79
London Metal Exchange (LMEX)	3655	4038	3984	3541
TR/CC CRB Commodity	261	268	278	268
Gold	1946	1969	1824	1661

CIO Economics Watch

US Economic Surprise Index



Asia Pacific Economic Surprise Index



Source: Bloomberg, DBS

MACRO CALENDAR

	Date	Period	Survey	Prior
United States & Eurozone				
Change in Nonfarm Payrolls (US)	02-Jun	May	190k	253k
Initial Jobless Claims (US)	01-Jun	27-May	235k	229k
ISM Manufacturing (US)	01-Jun	May	47	47.1
Conf. Board Cons. Confidence (US)	30-May	May	99	101.3
MBA Mortgage Applications (US)	31-May	26-May	--	-4.60%
HCOB Eurozone Mfg PMI (EU)	01-Jun	May	44.6	44.6
S&P Global US Mfg PMI (US)	01-Jun	May	48.5	48.5
Unemployment Rate (US)	02-Jun	May	3.50%	3.40%

MACRO CALENDAR

	Date	Period	Survey	Prior
Asia				
Industrial Production m/m (JP)	30-May	Apr	1.30%	1.10%
Jobless Rate (JP)	29-May	Apr	2.70%	2.80%
Manufacturing PMI (CN)	30-May	May	49.5	49.2
Caixin China PMI Mfg (CN)	31-May	May	49.5	49.5
Jibun Bank Japan PMI Mfg (JP)	31-May	May	--	50.8
Job-To-Applicant Ratio (JP)	29-May	Apr	1.32	1.32
Capital Spending y/y (JP)	31-May	1Q	5.40%	7.70%
Monetary Base y/y (JP)	01-Jun	May	--	-1.70%

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