June 2017

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FROM THE EQUITY DESK

Monthly Outlook

Summary

- MSCI Asia ex Japan (AxJ) gained 4.7% in USD terms, outperforming the MSCI AC World and MSCI Emerging Markets Indices. The results of the French presidential elections buoyed sentiment and outweighed patchy economic growth data.

- South Korea was the best-performing market in the region, following the election of president Moon Jae In and easing geopolitical tension between China and Korea.

- China also did well, despite Moody's downgrade of its sovereign credit rating and a growth slowdown. The central Bank's clarification that financial deleveraging is not monetary tightening eased market fears.

- India, Malaysia and Thailand lagged the regional benchmark. India was weighed down by weaker-than-expected GDP growth. In Thailand, corporate earnings disappointed, while heavy rainfall, a weak household balance sheet, and a slowdown in fiscal spending curbed domestic consumption.

- Valuations across AxJ remain reasonable despite the recent re-rating, and should be well supported by earnings upgrades across major sectors following a decent reporting season.

- We maintain an overweight to China, with a preference to sectors such as Internet, Tourism, Healthcare and Consumer. We also continue to favour India as we expect increased government tax revenues to be redeployed into infrastructure development. Meanwhile, we remain constructive on Korea, Taiwan and Indonesia, while reducing our exposure to Thailand.

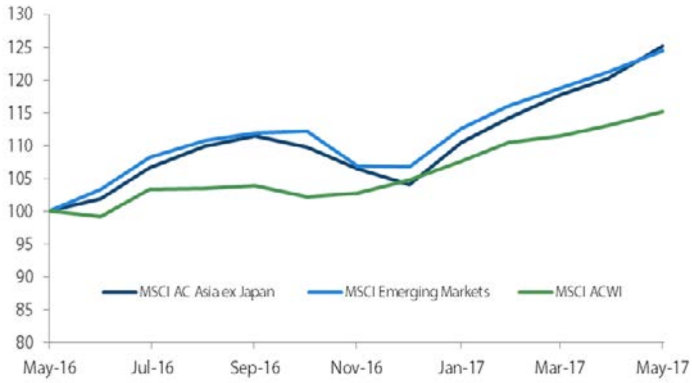
Asian Equity

Market Review

- Asia ex-Japan equities continued to rise in May

Asian equities continued their upward trajectory, with the MSCI Asia ex Japan (AxJ) Index rising by another 4.7% in US dollar (USD) terms and outperforming both the MSCI AC World and MSCI Emerging Markets (EM) indices. Year-to-date (YTD) returns now tally a respectable 20.9%; it is not surprising therefore that this rally has started to attract sizeable inflows into EM and Asian equities. Results of the French presidential elections buoyed sentiment early in the month, and seemed to give markets enough impetus to overlook patchy growth data. Asian currencies were largely stable with the exception of the KRW, MYR and THB which rallied 1.5-2.0% against the USD. Gold was lacklustre, and oil continued to slip.

1-Year Market Performance of MSCI Asia ex Japan versus Emerging Markets versus All Country World Index



Source: Bloomberg, 31 May 2017. Returns are in USD. Past performance is not necessarily indicative of future performance.

MSCI Asia ex Japan versus Emerging Markets versus All Country World Index Price-to-Earnings

Source: Bloomberg, 31 May 2017. Returns are in USD. Past performance is not necessarily indicative of future performance.

- South Korea outpaced its regional counterparts

South Korea (up 8.1% in USD terms) was the best performing market in the region. In local currency terms, the domestic KOSPI Index posted its highest monthly gain in the past five years. The election of President Moon and his nomination of top-level officials demonstrated the new government's hawkish stance on chaebols (family-run conglomerates); consequently, the large holding companies were the key beneficiaries with rising market speculation of a potential restructuring event. Easing geopolitical tension between China and Korea also proved a tailwind for markets. The KRW's 1.7% appreciation against the USD gave a fillip to USD returns.

- China outperformed despite Moody's downgrade

MSCI China gained 5.3% in USD terms. The market shrugged off Moody's one-notch downgrade of China's sovereign rating, as well as a slowdown in growth. The People's Bank of China (PBoC)'s clarification that financial deleveraging is not monetary tightening eased market fears, and the CNY's 1% appreciation in the month dampened depreciation concerns. Technical factors also contributed, with mutual market access (MMA) southbound flows rising 50% month-on-month (MoM) and EM seeing inflows of USD11bn (China is 27% of MSCI EM). Growth is slowing from its 1Q17 high; the producer price index (PPI) peaked at 7.8% over a year ago (oya) in February and was 6.4% in April, and credit growth has been decelerating for five consecutive months now.

- India, Malaysia and Thailand lagged

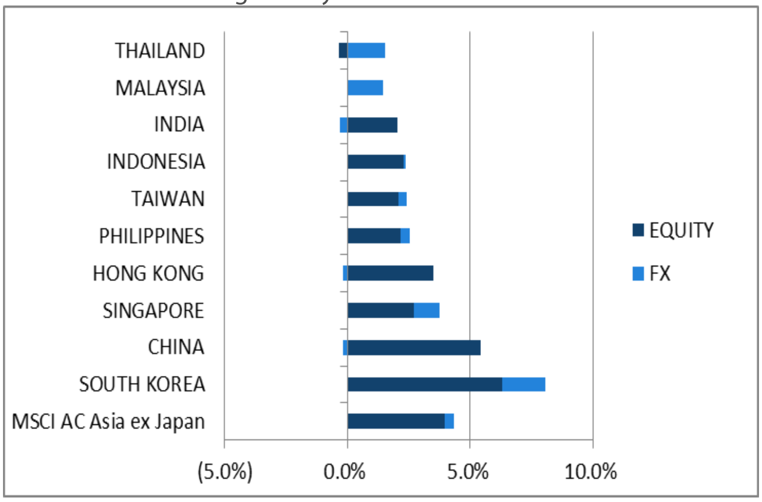
India (up 1.8% in USD terms) lagged the regional benchmark. Q4FY17 GDP growth surprised sharply to the downside and economic data points remain weak. Purchasing managers' index (PMI) and industrial production (IP) trends softened in April and are still below pre-demonetisation levels. Sector performance was divergent. Consumer Staples & Discretionary outperformed, led by solid earnings and positive guidance, while Healthcare was the key underperformer, as steep pricing declines in the US generic markets weighed on the earnings outlook.

Elsewhere, Malaysia and Thailand were flat in local currency terms. Thai corporate 1Q17 earnings generally disappointed.

Heavy rainfall, a weak household balance sheet, and a slowdown in fiscal spending have started to weigh on domestic consumption. Concerns on corporate capital calls also affected market sentiment.

MSCI AC Asia ex Japan Index

For the month ending 31 May 2017

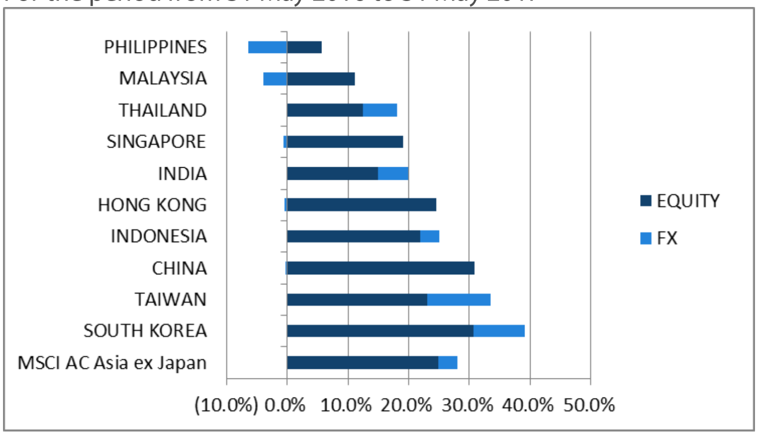


Source: Bloomberg, 31 May 2017

Note: Equity returns refer to MSCI indices quoted in local currencies while FX refers to local currency movement against USD. Returns are based on historical prices. Past performance is not necessarily indicative of future performance.

MSCI AC Asia ex Japan Index

For the period from 31 May 2016 to 31 May 2017



Source: Bloomberg, 31 May 2017

Note: Equity returns refer to MSCI indices quoted in local currencies while FX refers to local currency movement against USD. Returns are based on historical prices. Past performance is not necessarily indicative of future performance.

Market Outlook

- Valuations remain reasonable and should be supported by earnings upgrades

Although valuations across AxJ have re-rated this year following a broad-based rally, they are still not excessive, and should be well supported by earnings upgrades across major sectors following a decent reporting season. The MSCI AxJ Index trades on a 1.5x forward price-to-book (P/B) multiple compared to a 2.2x P/B multiple for the MSCI World Index.

- Maintain overweights to China and India

China's economy has positively surprised year-to-date despite the market's ongoing preoccupation with persistent stringent financial regulations. This will likely lead to some moderation in the near term as slower loan growth and receding producer price inflation filters through to the broader economy. However, this should be largely offset by rising domestic demand ahead of the 19th National Congress scheduled for November this year. The government continues to push public-private partnership (PPP) programmes as a means of attracting private capital. We remain overweight Chinese stocks, with a preference for new economy sectors such as Internet, Tourism and Healthcare. We have also recently added positions in the Consumer sector.

India also remains a key overweight. The crackdown on black money and the recent demonetisation exercise have driven a steady flow of monies into domestic equity funds, which in turn has pushed the local stock market higher. The imminent rollout of government service tax (GST) will create a homogenous domestic market, and drive a structural increase in government tax revenue which will likely be redeployed into infrastructure development. Notwithstanding lukewarm quarterly results and a widening gap between market prices and underlying value, there remain pockets of structural beneficiaries at reasonable valuations. The expectation for a near-normal monsoon augurs well for consumer spending.

- Remain constructive on Taiwan and Korea

We remain constructive on Korea and Taiwan, which are Asia's major tech hubs and key export economies. The election of new president Moon Jae In sets the stage for greater fiscal spending and corporate reform. Despite elevated sabre-rattling by North Korea, or perhaps because of it, the relationship with China appears on the mend. We are optimistic that the improvement in earnings across the majority of Korean companies can continue. In Taiwan we remain selective with holdings spread across niche segments of the technology sector and companies with good long term cross-straits franchises.

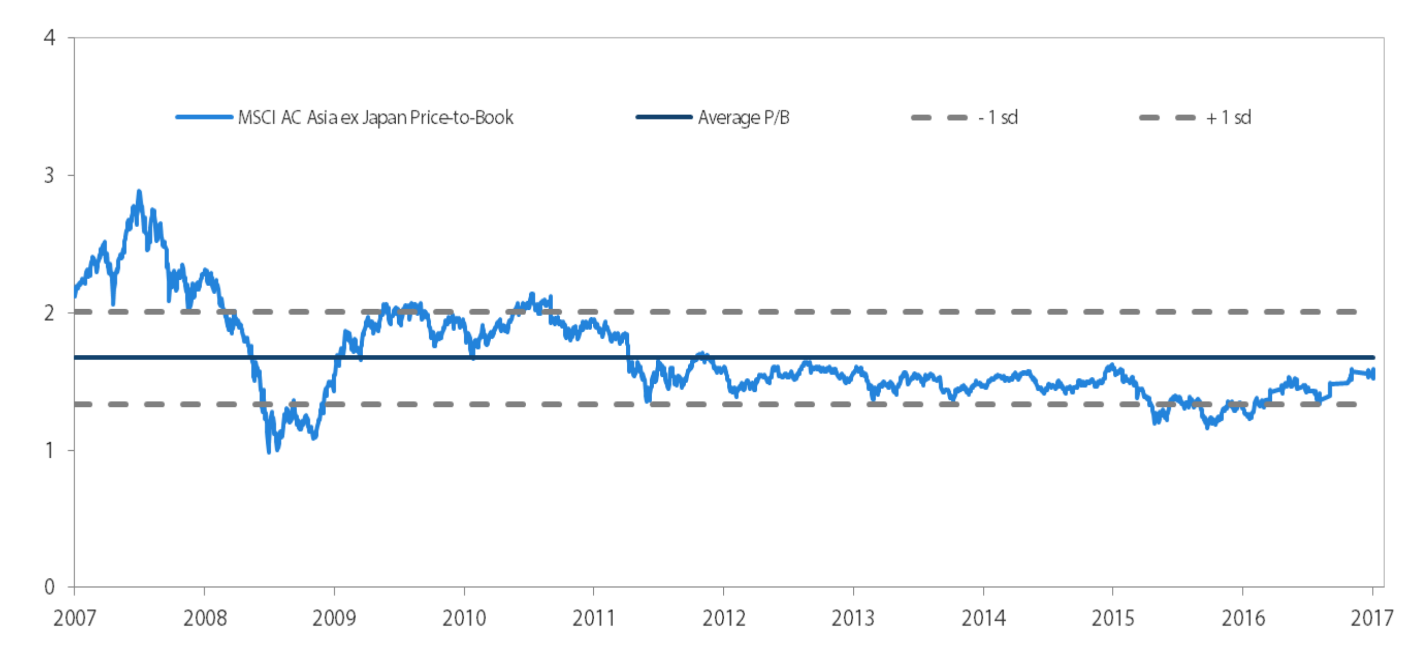
- Favour Indonesia; have reduced exposure to Thailand

Within ASEAN, we have become more constructive towards Indonesia and are looking for opportunities to add to our exposure there. Following the peaceful election of Jakarta's new mayor, we expect a pick-up in domestic activity, particularly infrastructure. Banks appear to be dealing with the credit cycle on the front foot. In Thailand, we find overall economic conditions tepid and await clarity vis-à-vis the new King; we have reduced our exposure here. There is no change in our stance towards the Philippines where we are cognisant of slowing GDP growth and limited progress on infrastructure under president Duterte. We maintain our zero weight to Malaysia.

Appendix

MSCI AC Asia ex Japan Price-to-Earnings

MSCI AC Asia ex Japan Price-to-Book



Source: Bloomberg, 31 May 2017. Ratios are computed in USD. The horizontal lines represent the average (the middle line) and one standard deviation on either side of this average for the period shown. Past performance is not necessarily indicative of future performance.

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