
Source: AFP Photo

CIO Weekly

8 November 2022

Key Points

- **Equities:** Potential slowing of rate hikes stoke DM equity rally; Hong Kong and China markets slide on negative sentiments.
- **Credit:** US IG issuers most insulated against rising rates; we continue to advocate an up-in-quality stance in credit.
- **FX:** Greenback failed to get a boost from the rise in US Treasury yields; EM currencies breathed easier on softer USD and better risk appetite.
- **Rates:** Spikes in 2Y and 5Y yields to fade if CPI beats expectations; but potential long end UST underperformance to persist with 10Y heading to 4.50%.
- **Thematics**: Physical stores to make a comeback as consumers shift back to pre-Covid purchasing habits .
- **The week ahead:** Keep a lookout for US Initial Jobless Claims; China CPI y/y.

GLOBAL CROSS ASSETS

Returns of cross assets around the world

Index	Close	Overnight	YTD
DJIA	32,827	1.3%	-9.7%
S&P 500	3,806	1.0%	-20.1%
NASDAQ	10,564	0.9%	-32.5%
Stoxx Europe 600	418	0.3%	-14.2%
DAX	13,533	0.5%	-14.8%
CAC 40	6,416	0.0%	-10.3%
FTSE 100	7,299	-0.5%	-1.1%
MSCI AxJ	559	1.8%	-29.1%
Nikkei 225	27,527	1.2%	-4.4%
SHCOMP	3,077	0.2%	-15.4%
Hang Seng	16,595	2.7%	-29.1%
MSCI EM	897	1.4%	-27.2%
UST10-yr yield*	4.21	5.5	270.3
JGB 10-yr yield*	0.25	0.1	18.7
Bund 10-yr yield*	2.34	4.9	252.3
US HY spread*	4.53	-9.0	170.0
EM spread*	420.07	-14.4	89.8
WTI (USD)	91.79	-0.9%	22.0%
LMEX	3,689.10	-1.6%	-18.1%
Gold (USD)	1,675.63	-0.4%	-8.4%

Source: Bloomberg

* Changes in basis points

Equities: Dual hikes snap DM win-streak

Global equities close lower, led by US decline. Central banks were in focus this week as the US Federal Reserve and Bank of England continued their tightening campaigns with 75 bps hikes. Global equities dipped -1.4% for the week; Developed Markets fell -2.1% while Emerging Markets rallied 4.7%.

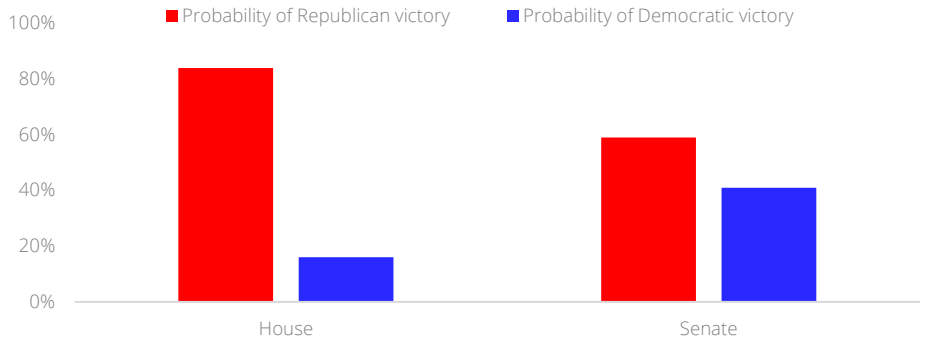
In US, nonfarm payrolls data beat expectations as 261,000 jobs were added in October. However, further rate hike fears fuelled a week-to-date decline for major indices; the S&P 500 and Nasdaq fell 3.3% and 5.6% respectively. Europe closed the week in green on the back of positive corporate earnings. The Stoxx 600 was up 1.5% and FTSE 100 gained 4.1% for the week. Asia equities rose on speculation of easing Covid policies in China; the Hang Seng, HSCEI, and SHCOMP added 8.7%, 9.0% and 5.3% respectively.

Topic in focus: US midterm election to have limited impact on equity markets. After months of intense campaigning in the primaries, the US midterm election is heading down to the wire. Despite initial ground gained by the Democrats in the wake of the Supreme Court's reversal of Roe vs Wade, the Republicans have since regained the lead and forecasts from FiveThirtyEight.com suggests an 84% chance of the Grand Old Party (GOP) regaining the House. However, the Senate race remains a toss-up. According to FiveThirtyEight.com, the Republicans have a marginal lead here with 59% chance of winning while Democrats hold 41% chance.

A Democratic clean sweep will translate to greater passage of measures from Biden's fiscal agenda and a more elevated path for policy rates. Conversely, a Republican victory in both the House and Senate will lead to an opposite outcome. A divided congress, meanwhile, will result in limited passage of fiscal measures during Biden's remaining Presidential term. In any case, we believe the overall impact from the US midterms will be limited. Instead, the bigger drivers for equity markets at this juncture are corporate earnings, recession risks, and Fed policy path.

Dylan Cheang | Analyst
Goh Jun Yong | Analyst

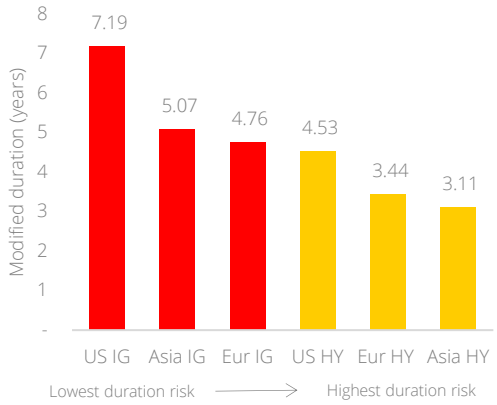
Figure 1: Forecast on US midterm election



Source: FiveThirtyEight.com

Credit: US IG issuers most insulated against rising rates

Figure 2: US IG issuers have locked in prior low rates for longer



Source: Bloomberg, DBS

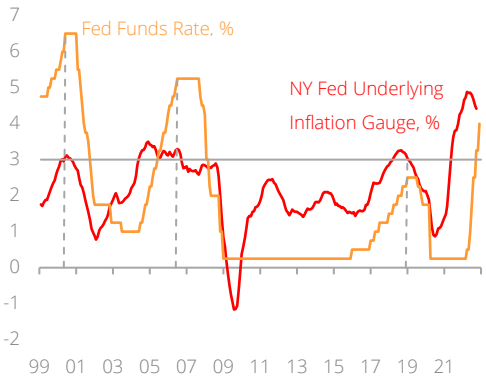
With the latest Fed rhetoric suggesting they "still have some ways to go" in making rates "sufficiently restrictive" we continue to advocate an up-in-quality stance in credit. In view of the impact on interest and debt servicing burdens, higher rates are likely to have the most significant impact on the most leveraged parts of the economy. Mindful of this environment fraught with volatility, we conducted a risk assessment to identify where pockets of weakness could first potentially arise as rates continue their upward trajectory.

Our assessment of various factors reveals that US IG corporates are best positioned to weather this rising rate environment. A key factor analysed was duration risk, or how long companies have locked in interest rates for, since companies that do not have debt maturing in the near term are expected to have lower refinancing needs and hence be relatively insulated against rising rates. Based on our analysis, issuers in US IG appear most robust in terms of duration risk (Figure 2). Within US IG, even sectors with highest duration risks (Financials and Consumer Discretionary) boast a duration upwards of five years, as most US companies seized the opportunity in 2020 to lock in extraordinarily low rates for a longer period. These insights continue to validate our emphasis on high quality credit in today's environment, given that loss avoidance is key for outperformance in a credit portfolio.

Daryl Ho | Strategist

FX: Currencies gaining traction on risk appetite

Figure 3: Real US rates turning positive soon



Source: Bloomberg, DBS

The US mid-term elections are in play. DXY depreciated a second session by 0.6% to 110.19, its lowest close since 26 October. Investors viewed Democrat losses as unfavourable for the USD and Republican gains as positive for equities. Although the US economy exited its technical recession in 3Q22, American voters are upset with the significant increase in the cost of living. Many expect the Republicans to regain control of one or both houses of Congress and render US President Joe Biden a "lame duck" in the next two years. The Grand Old Party (GOP) will revive brinkmanship with the White House over the federal debt limit, which needs to increase next year.

The greenback did not get a boost from the rise in US Treasury yields. The US Treasury 2Y yield increased 6.5 bps to 4.72%, a new year's high. The 10Y yield firmed 6 bps to 4.22%, keeping the yield curve inverted at -51 bps. Although consensus expects Thursday's US CPI inflation to slow to 7.9% y/y in October from 8.2% the previous month, we see the Fed lifting its 2023 rate forecast above the 4.6% projected in September. Unless inflation surprises strongly, we see the Fed moving towards smaller rate hikes from December. After the fourth 75 bps hike to 4%, the gap between the Fed Funds Rate and the New York Fed's underlying inflation gauge has narrowed significantly. The case for a Fed hike pause will increase when real rates turn positive.

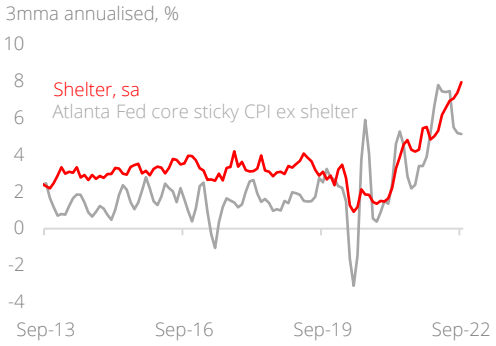
GBP appreciated 1.2% to 1.1514, on top of last Friday's 2% gain. The UK Budget Statement on 17 November is shaping up as a positive event. Chancellor Jeremy Hunt should deliver GBP60b of tax hikes and spending cuts to plug the fiscal gap. Hunt expects the Office for Budget Responsibility (OBR) to project government debt as a falling proportion of income. The 10y Gilt yield has eased to 3.64% from 4.50% after the mini budget was dismantled. GBP is trying for the second time since 26 October to break above 1.15. While the odds have improved from the 20-day moving average (MA) cutting above the 50-day MA around 1.1350, GBP still needs to clear the major resistance at 1.1680 or its 100-day MA.

Emerging Asian currencies breathed easier on a softer USD and better risk appetite. As witnessed in the Developed Markets, players appear to be buying back the weakest currencies in Asia too. The USD's retreat was evident in the price-taker USD/SGD which fell near 1.40 for the first time since 12-13 September. For the first time since 6 October, USD/INR closed below 82 while USD/KRW neared 1,400. Pay close attention to the traction USD/KRW has in pushing below 1400. After its plunge from 38 last Friday, USD/THB might test 37 soon. Thailand is approaching its target of attracting 10m foreign visitors this year. Despite China's Covid Zero policy, other foreign travellers, especially Indians and Malaysians, have been attracted to Thailand due to the weak exchange rate. USD/VND stabilised around 24,850 after the second 100 bps rate hike on 25 October. The two aggressive hikes and the widening of the USD/VND trading band should help the country to tackle rising inflation with a less volatile exchange rate without a sharp drawdown in foreign reserves.

Philip Wee | Strategist

Rates: Working around upcoming CPI figures

Figure 4: Alternative measure of US inflation



Source: Bloomberg, DBS

While keeping an eye on the US mid-term elections, we will focus more on US CPI figures due this Thursday 10 November (consensus: 0.6% m/m sa, 7.9% y/y). Note that these figures still appear high, but the Cleveland Fed's Nowcast points to an even higher figure of 0.78% m/m sa (8.1% y/y). While the headline figure may surprise on the upside, we think that the focus should be on the Atlanta Fed's sticky inflation less shelter measure to remove the lagged impact of the rental component. On a three-month annualised basis, this measure is running at about 5% (still uncomfortably high but with no signs of acceleration). We would also keep an eye on the New York Fed's underlying inflation gauge which takes into account non-price variables and the Cleveland Fed's trimmed mean measure which removes the outliers.

Data is clearly important, but forward guidance has returned with Fed Chair Powell suggesting that a downshift (a slower pace of hikes) may be appropriate. The price action around post firm NFP figures last Friday also point to possible exhaustion in selling of short-dated USTs in response to labour market strength. On a related note, implied volatility in Treasuries finally fell meaningfully. There are a couple of ways to interpret the fall in volatility. With the Fed signalling a smaller pace of rate hikes, it intuitively makes sense that the range of probable yield movements should be smaller. Second, the Fed is getting much closer to the terminal rate where a pause seems most likely. In the absence of runaway inflation or the sudden onset of a hard landing, a period of more stable yields may be in store. Tactically, spikes in 2Y (around 4.8%) and 5Y yields (4.45-4.50%) should be faded if CPI beat expectations. We are more worried about long end UST underperformance and still see 10Y upside perhaps out to 4.50%, representing considerable upside risks to our forecast.

Eugene Leow | Strategist

Thematics: Asean e-commerce players hit stop on discounts

- E-commerce players are discouraging small basket purchases in pursuit of profitability
- This is likely to benefit physical stores
- We prefer mass grocery retailers in Singapore

Consumers might switch back to physical stores. E-commerce players are charging higher delivery rates from consumers in view of mounting logistics costs. In addition, product prices on e-commerce sites have also gone up as e-commerce players are charging higher commissions from merchants as well. This encourages users to visit physical stores for 10-30% savings on smaller basket sizes. Cashback vouchers, used to offset delivery charges earlier, have also largely ceased as e-commerce players pursue profitability.

E-commerce growth is slowing down, physical retailers likely to see recovery in 2023. According to eMarketer, Southeast Asia e-commerce sale is expected to grow by 20.6% in 2022 to USD89.7b. This is far below the 58% growth seen in 2020 and 26.1% growth in 2021 during the pandemic. Going forward, eMarketer projects 13.5% e-commerce sales CAGR over 2022-24, less than one-third of 41% seen over 2019-2021. We see downside risks to these projections as e-commerce players lower discounts sharply while logistics costs have also gone up significantly.

Offline stores in Southeast Asia are likely to witness sales CAGR of 6% over 2022-24. According to our estimates using eMarketer data, offline stores witnessed flattish growth in 2021 and are likely to see 7.9% growth in 2022 due to revenge shopping post-pandemic. With consumers shifting to pre-Covid purchasing habits, coupled with lower discounts from e-commerce players, offline stores are expected to make a comeback. Based on eMarketer data, we estimate offline stores in Southeast Asia will register 6% CAGR over 2022-24 to reach an estimated sales figure of USD1.1t in 2024.

Among the physical stores, we like mass grocery retailers in Singapore. They are likely to experience a second wind in their sail with the shift towards home dining on rising cost of living. In Indonesia, we like retailers that target the middle to upper income earning consumers as they are more resilient against inflation.

Sachin Mittal | Analyst

Andy Sim | Analyst

Cheria Christi Widjaja | Analyst

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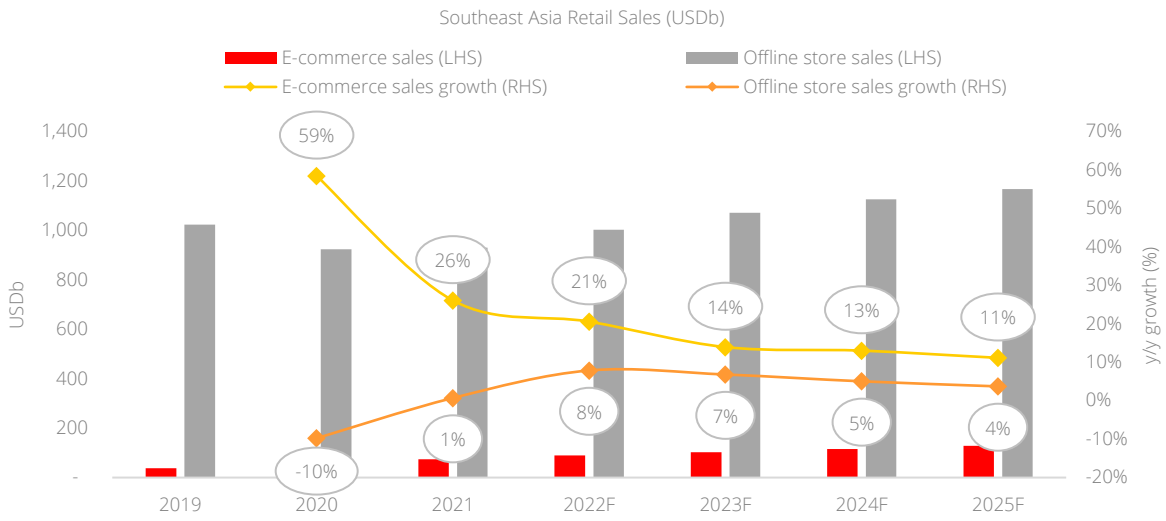
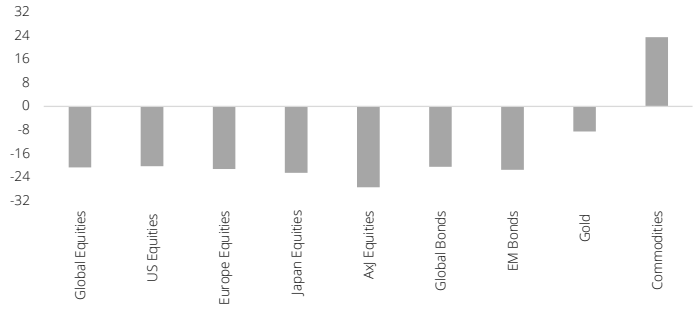
Figure 5: Offline stores sales are expected to register a CAGR of 6% over FY22F-24F



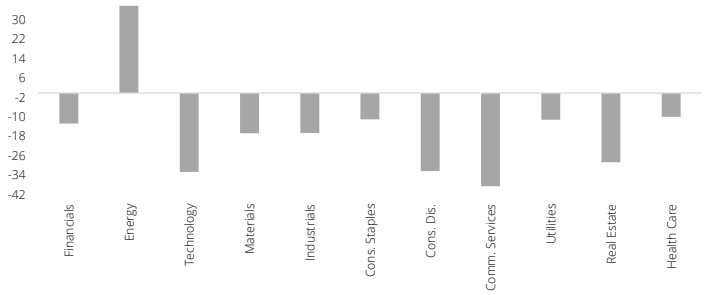
Source: eMarketer, DBS

CIO Markets Watch

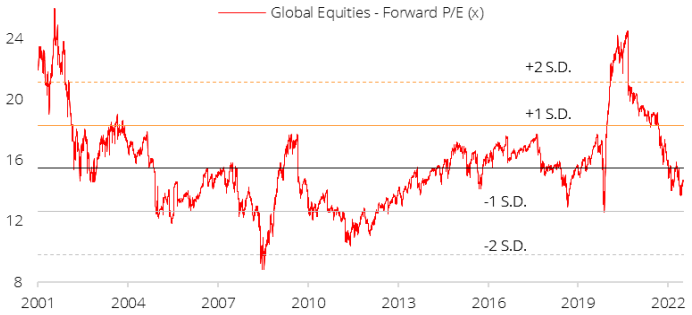
Global Cross Assets YTD Returns



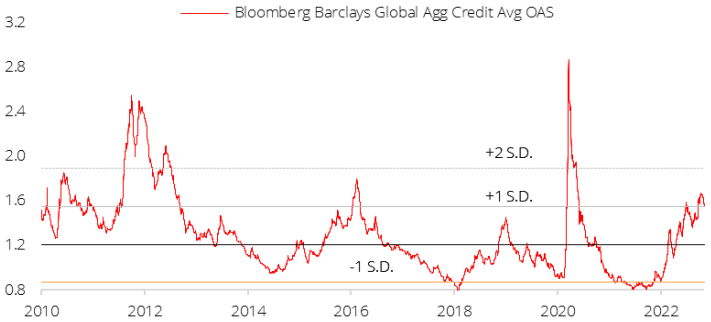
Global Sector YTD Returns



Global Equity Valuation



US Corporate Spreads



INDEX RETURNS

	1 week	MTD	QTD	YTD
Equities				
S&P 500	-1.7%	-1.7%	6.2%	-20.1%
NASDAQ	-3.9%	-3.9%	-0.1%	-32.5%
Russell 2000	-2.0%	-2.0%	8.7%	-19.4%
Euro Stoxx 600	1.5%	1.5%	7.9%	-14.2%
Nikkei-225	-0.2%	-0.2%	6.1%	-4.4%
MSCI WORLD	-0.6%	-0.6%	6.5%	-21.6%
MSCI ACWI	0.1%	0.1%	6.1%	-22.2%
MSCI Asia ex-Japan	6.8%	6.8%	0.3%	-29.1%
MSCI EM	5.8%	5.8%	2.5%	-27.2%
HSCEI	14.1%	14.1%	-4.7%	-31.6%
SHCOMP	6.4%	6.4%	1.8%	-15.4%
Hang Seng	13.0%	13.0%	-3.6%	-29.1%
STI Index	1.6%	1.6%	0.4%	0.6%
Fixed Income				
Barclays Global Aggregate	-0.1%	-0.1%	-0.7%	-20.5%
Barclays US Aggregate	-0.6%	-0.6%	-1.9%	-16.3%
Barclays US High Yield	-0.6%	-0.6%	1.9%	-13.1%
Barclays Euro Aggregate	-0.7%	-0.7%	-0.6%	-16.7%
Barclays Euro High Yield	0.3%	0.3%	2.3%	-13.1%
JPM EMBI Global	0.9%	0.9%	1.0%	-21.5%
JPM EMBI Global Diversified	-0.1%	-0.1%	0.3%	-24.6%

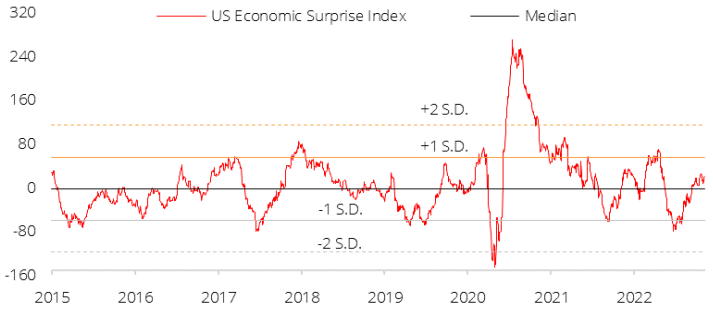
PRICES & SPREADS

	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	4.22	3.83	3.02	2.34
Japanese Govt. Bond 10-yr	0.25	0.24	0.23	0.21
German Bunds 10-yr	2.34	2.11	1.33	0.55
Spreads				
US Agg Corporate Spread	1.49	1.59	1.55	1.16
US Corporate HY Spread	4.53	5.52	5.69	3.25
Euro Agg Corporate Spread	2.13	2.25	2.15	1.31
EM USD Agg Spread	3.90	4.03	4.04	3.13
Currencies				
US Dollar Index (DXY)	110.1	112.1	104.7	98.3
EUR/USD	1.00	0.98	1.05	1.11
USD/JPY	146.6	144.7	135.7	121.7
USD/CNY	7.2	7.1	6.7	6.3
Commodities				
WTI Oil	92	79	106	100
London Metal Exchange (LMEX)	3689	3541	3879	5174
TR/CC CRB Commodity	287	268	291	295
Gold	1676	1661	1807	1937

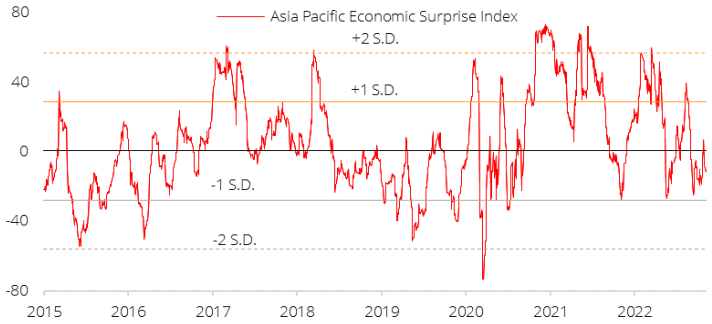
DBS

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)	10-Nov	05-Nov	220k	217k
CPI m/m (US)	10-Nov	Oct	0.60%	0.40%
U. of Mich. Sentiment (US)	11-Nov	Nov	59.5	59.9
MBA Mortgage Applications (US)	09-Nov	04-Nov	--	-0.50%
Wholesale Inventories m/m (US)	09-Nov	Sep	0.80%	0.80%
CPI Ex Food and Energy m/m (US)	10-Nov	Oct	0.50%	0.60%
Monthly Budget Statement (US)	11-Nov	Oct	-$92.5b	-$429.7b
Continuing Claims (US)	10-Nov	29-Oct	1481k	1485k

MACRO CALENDAR

	Date	Period	Survey	Prior
Asia				
CPI y/y (CN)	09-Nov	Oct	2.40%	2.80%
BoP Current Account Balance (JP)	09-Nov	Sep	¥250.0b	¥58.9b
PPI y/y (JP)	11-Nov	Oct	8.80%	9.70%
PPI y/y (CN)	09-Nov	Oct	-1.50%	0.90%
Money Supply M2 y/y (CN)	09-Nov	Oct	12.00%	12.10%
Money Stock M2 y/y (JP)	10-Nov	Oct	3.20%	3.30%
Money Stock M3 y/y (JP)	10-Nov	Oct	2.80%	2.90%
New Yuan Loans CNY (CN)	09-Nov	Oct	800.0b	2470.0b

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