2024 Market Outlook

Time for a bracing breeze

December 2023

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Contents

A review of 2023

As we expected, 2023 proved to be a challenging year for most Asian equity markets, with a number of uncertainties unfolding during the period.

The year started on a strong footing, given investors' high expectations of the re-opening boost to the Chinese economy, which were deemed to be positive for the entire Asian region. However, the optimism faded quickly as the ongoing debacle in the Chinese property sector, despite some supportive measures being announced by the government, continued to dent consumer confidence and drag on the overall economy.

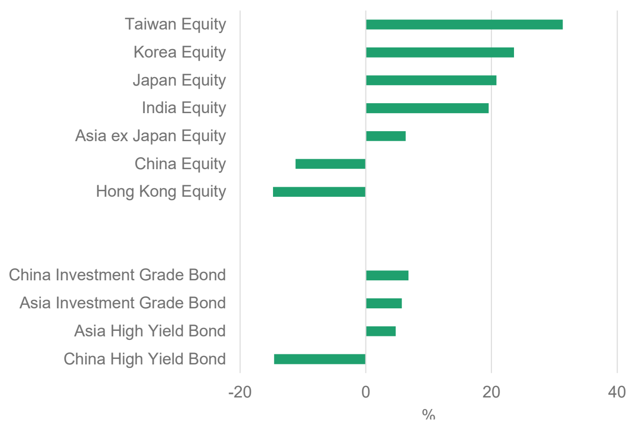
This also led to a dreadful high yield bond market in Asia, which at the beginning of the year continued to remain highly exposed to Chinese real estate developers in spite of several defaults in 2022. Similar to equities, with an upbeat market at the start of the year, the Asian high yield bond market started to correct in the second quarter as Chinese property sales remained low even after the economy had re-opened. The market then deteriorated further as, towards the end of the year, one of the largest privately owned developers which was considered "financially sound", also went into default. While the Chinese government announced further supportive measures, fragile investor confidence meant that markets remained volatile for the remainder of 2023.

From a macroeconomic perspective, persistent inflationary pressure across different regions led to one of the fastest and strongest monetary tightening cycles globally, from the US and Europe to most of Asia, including Japan, which had been enduring deflation for a long time. The US Fed was the most aggressive in its tightening, which resulted in a large appreciation of the US dollar. This constrained China in terms of its flexibility to conduct further easing to support the economy, given the risk of further downward pressure on the renminbi. On the other hand, the escape from a "deflationary trap" for Japan helped its equity market to become among the best-performing equity markets in Asia (in JPY terms). This rising interest rate cycle also has implications for fixed income, as higher bond yields resulted in rather lackluster returns for investment grade bonds, whereas demand for money market and short-maturity investments skyrocketed.

From a geopolitical standpoint, the Sino-US relationship remained delicate, as the US continued to add further investment restrictions on China, while the previous Covid disruption resulted in some corporates reorganising their supply chains to include South Asia. This has seen some equity markets, such as India, delivering strong performance in 2023 despite already high valuations.

Another "market changing" development was the rapid adoption and prevalence of artificial intelligence (AI) with the launch of ChatGPT-4, which has started to revolutionise how things are done for many different businesses. This has also led to a significant increase in demand for technology hardware, which helped both the Taiwan and Korean equity markets deliver double-digit returns, given their large exposure to the technology supply chain.

Year 2023 Performance of different Asia asset classes



Source: Bloomberg, as of December 2023. Currency in USD. Refer to the MSCI Index return as region equity's performance.

The global and regional macroeconomic and geopolitical factors which had significant influences on Asian assets in 2023, will continue to drive markets in 2024, but in different ways. We expect a gradual change of direction in the wind, with the tailwind that propelled some markets and assets in 2023 to fade, whilst the resistance from significant headwinds for others to reduce – resulting in some mean-reversion for 2024.

Asia investment outlook

The aforementioned global and regional macroeconomic and geopolitical factors which had significant influences on Asian assets in 2023, will continue to drive markets in 2024, but in different ways. We expect a gradual change of direction in the wind, with the tailwind that propelled some markets and assets in 2023 to fade, whilst the resistance from significant headwinds for others to reduce – resulting in some mean-reversion for 2024.

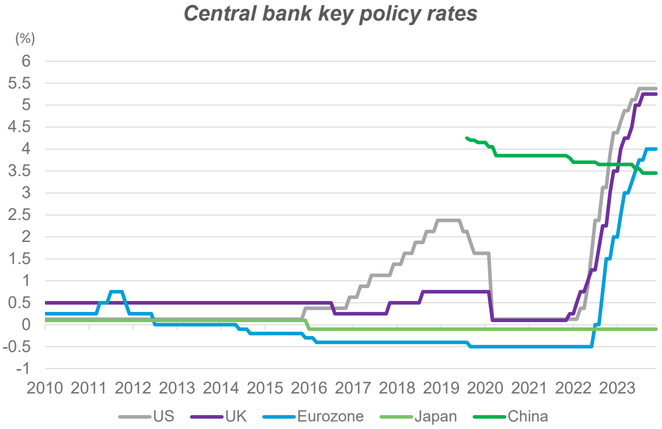
Key Investment Themes – Time for a Bracing Breeze

1) Inflation and Monetary Policy - from headwind to tailwind for Asia

While Covid might seem like a distant memory, the lingering effect of the pandemic remains significant, especially on the economy and inflation. However, the good news is that we are now close to the “beginning of the end” and finally a return to “normal”.

Globally, inflationary pressures have eased gradually, and the downward trend will likely continue into 2024. In the final FOMC meeting of 2023, the US Federal Reserve (the Fed) confirmed that the central bank has finished interest rate hikes and could look to cut interest rates by up to 75bps in 2024, as shown in its dot-plot projection. It is likely that we could see similar moves by other major central banks, such as the European Central Bank (ECB) and the Bank of England (BOE). The exception probably remains the Bank of Japan (BoJ), given that the country is at an earlier stage of the monetary cycle.

Central bank key policy rates

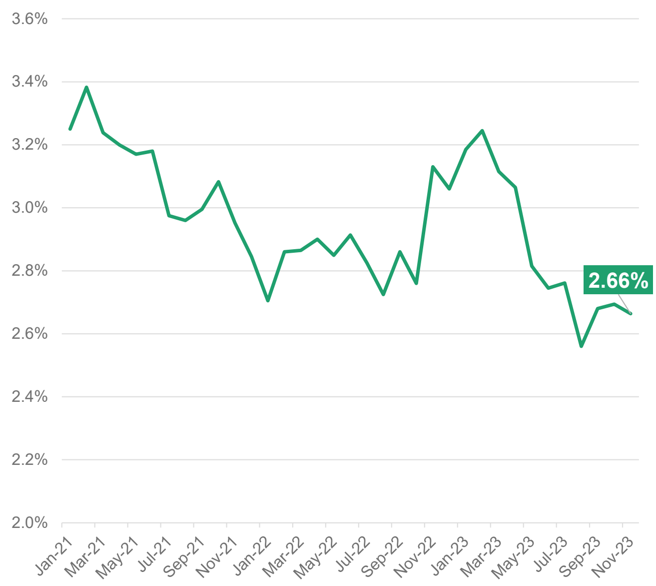


Source: Bloomberg. 1-year Loan Prime Rate (LPR) is used to represent short-term interest rates for China.

This change from monetary headwind to tailwind will likely be supportive of risk assets. We believe that Asia could benefit the most as this paves the way for stronger easing from central banks in the region, particularly for China. In 2023, monetary tightening and the disappointment from the economic recovery in China created depreciation pressure for the renminbi, which constrained the People’s Bank of China’s (PBoC) flexibility in providing further monetary stimulus to support the economy. Similarly, for the rest of Asia, central banks also needed to maintain a prudent stance and conduct some tightening to manage inflationary and currency depreciation risks.

As the cycle starts to turn with the US dollar’s strength weakening, central banks in Asia will have ample room to loosen monetary policy. This is particularly true for China, as recent data suggest that its economy is facing the risk of deflation, and therefore, further easing is needed and expected as an acyclical measure. We believe further required reserve ratio (RRR) and loan prime rate (LPR) cuts, as well as other forms of easing to improve financing and monetary conditions, will happen in 2024, potentially in the first half of the year, given the rising risk of a further slowdown as indicated by recent data.

10-year China Government Bond yield remains at a low-level



Source: Bloomber, as of November 2023.

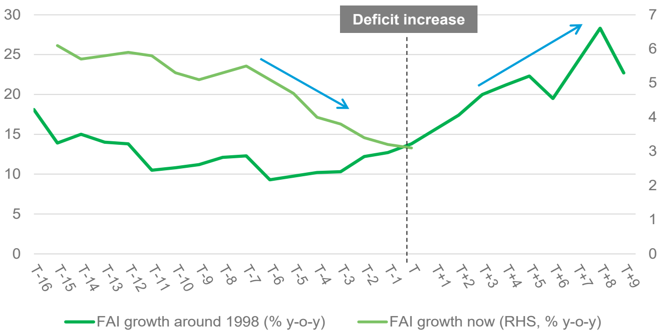
Monetary conditions remain accomodative, albeit with a weak demand

Source: Bloomberg, as of November 2023.

2) Economic Growth – China's recovery is delayed, not derailed

The initial excitement post-reopening in early 2023 quickly faded, due to weaker macro readings after the first quarter. On a positive note, the rollout of policy support measures accelerated after July, underscoring Chinese policymakers' commitment to economic growth. In addition to interest rate and RRR cuts, a slew of easing and supportive measures were announced to help the economy. These included an unexpected RMB1 trillion central government bond issuance, announced in October 2023, which widened the central budget deficit from 3.0%to 3.8% (of GDP).

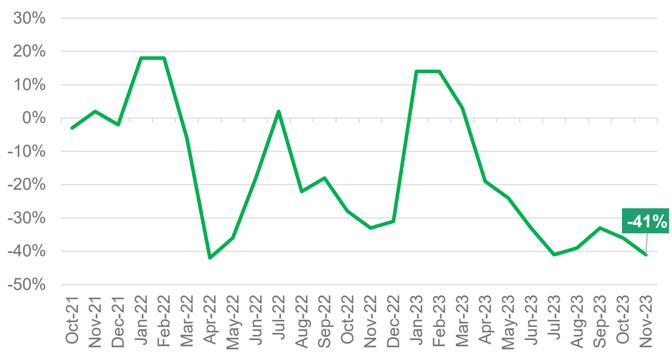
Historic experience suggests Fixed Asset Investment (FAI) growth could accelerate after a mid-year increase in budget deficit



Source: Wind, CLSA, as of October 2023.

However, a prolonged weakness in the property market, which accounts for nearly 25% of China's GDP when the market's affiliated upstream and downstream industries are included, may continue to be a drag on market sentiment. We believe that slow new home sales could extend into the near term, consequently affecting the wealth effect and consumer demand. For 2024, it is therefore critical to watch whether the government will implement further policy support for the ailing property market, particularly concrete measures directed towards easing the pressure on developers facing funding difficulties. We believe a stabilising of China's property market is vital for the sustainable revival of consumer confidence and a further rebound of economic growth momentum.

New home sales value versus 4-year average



Downward property price pressure has intensified

Source: NBS, JP Morgan, as of November 2023.

We also expect to see more progress with the government's comprehensive packages to resolve the ongoing local government debt issue, which has been another major market concern during the past year. This could come in the form of a package of measures, such as debt restructuring of local government financing vehicles (LGFV), debt swaps with the central government, and/or debt restructuring/refinancing at a lower interest rate with a longer duration. Here, it is key to monitor whether the central government would leverage up and shoulder the greater debt burden of local government. Further details may be revealed in the Party's forthcoming key economic conference, including the 'third plenum' of the Party Congress.

Overall, we expect China's economy to follow a U-shape recovery and to see more support from the central government.

3) Divergence from Convergence – identifying the right sectors and strategies

In 2023, global markets, including Asia's, were characterised by one dominant investment theme – AI and technology. The launch of ChatGPT-4, as well as many more AI models and applications, were the key drivers of both growth and market returns. Meanwhile, the divergence in the global economies, with desynchronised growth and inflationary dynamics, as well as monetary policy, caused significant return dispersion among markets, sectors, and investment styles.

With the aforementioned convergence of macroeconomic trends, we expect market breadth to improve and the force of mean-reversion to drive the divergence of sector and strategy returns.

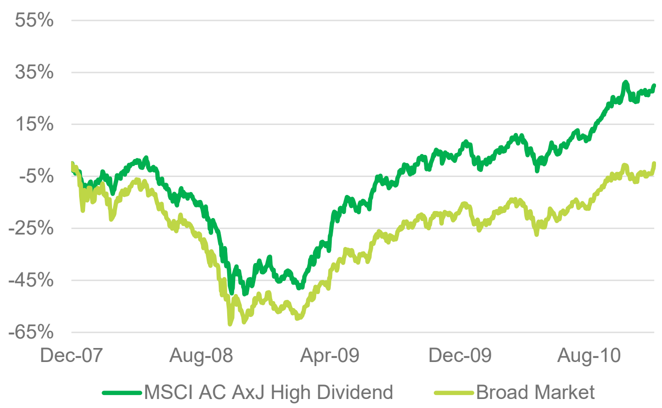
First of all, dividend-focused equity investment strategies are likely to gain from loosening monetary policy. During the period of near-zero interest rates, investors were pushed out on the risk curve to generate yield by allocating to asset classes such as high yield bonds and dividend-yielding equities. These allocations were largely reversed in 2022 and 2023, given the rapid and significant increase in interest rates and bond yields, which saw investors de-risk back into investment grade bonds and money market instruments. Now, the trend will likely begin to reverse as interest rates and yields begin to fall. As such, we expect dividend equity-focused strategies to perform well in 2024. Globally, we believe that Asian equities remain mostly attractive from a valuation perspective. The convergence of economic growth in the region with the rest of the world could result in some mean-reversion on valuation, thus providing further impetus for Asian equity markets to deliver strong returns in the coming year.

Dot-com Bubble Period

	MSCI AC AxJ High Dividend	Broad Market	Outperformance
Net return change	+18.2%	+5.9%	+12.3%

	Dec 2000	May 2002
Federal Funds Target Rate	6.5	1.75

Global Financial Crisis



	MSCI AC AxJ High Dividend	Broad Market	Outperformance
Net return change	+30.0%	-2.0%	+32.0%

	Dec 2007	Dec 2010
Federal Funds Target Rate	4.25	0.25

Source: Bloomberg.

European Debt Crisis

	MSCI AC AxJ High Dividend	Broad Market	Outperformance
Net return change	**+10.2%**	**+1.2%**	**+9.0%**

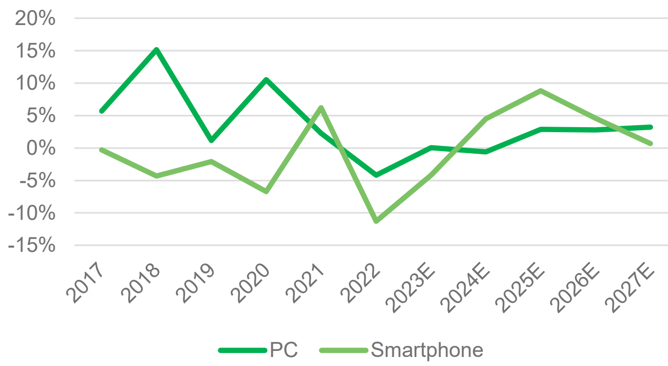
	Dec 2010	Dec 2012
Federal Funds Target Rate	**0.25**	**0.25**

Source: Bloomberg.

Secondly, within the dividend-focused sectors, there are also likely to be some changes in terms of market leadership amid the changing monetary cycle. Rising interest rates have supported financials, such as banks, given the improvement of net interest margin (NIM) over the last two years. Meanwhile, sectors that rely on relatively high leverage, such as REITs and utilities, have suffered, given rising interest costs. The performance of these two sectors could likely see some mean reversion in the coming quarters as monetary easing begins. Similarly, if there is going to be further stimulus in China, consumer spending could potentially improve, which could see some mean-reversion trades in the consumption sector, which significantly underperformed in 2023. Another asset class that investors should watch out for is gold, which has proven to be resilient even in a monetary tightening cycle. Investors should, therefore, take time to consider these potential sector divergences arising from the convergence of macroeconomic trends.

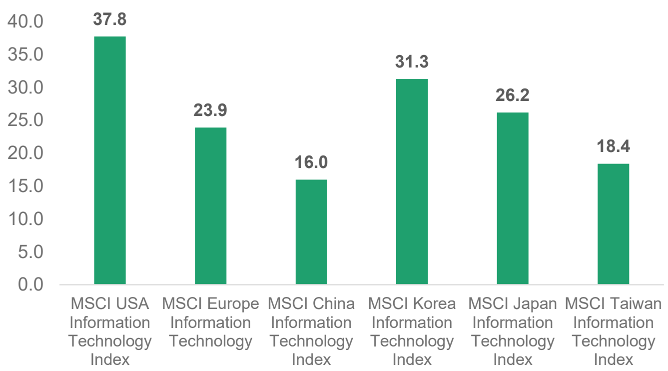
Finally, some of 2023's outperformers could potentially continue to do well in 2024, with technology being the most likely. Lower interest rates are typically supportive of growth equities. While the returns of AI-related stocks pushed valuations higher in 2023, the strong demands from the fast adoption of the technology, now coupled with lower interests and yields, should remain supportive of technology-related stocks in 2024. We have also seen signs of a bottoming out in the consumer electronics cycle, which could add further to potential market returns from the overall sector in 2024. That said, with elevated valuations, volatility is likely to increase, and hence, security selection will be key to capturing opportunities and managing risk.

Global smartphone and PC revenues are recovering from the bottom



Source: Macquarie, IDC, December 2023.

Asian tech sector offers attractive valuations



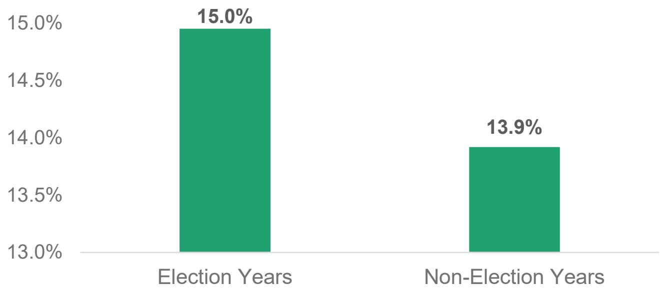
Source: Bloomberg, November 2023.

4) Geopolitics – a continuing source of volatility

Geopolitics have been a continuing source of market volatility for the past few years, from the Ukraine-Russian conflict and Sino-US relations to the recent Israel-Gaza conflict. This trend is unlikely to change, and we should continue to expect volatility from geopolitics in 2024.

While there are a number of elections globally, the most notable is the US presidential election in the second half of 2024. It is expected that issues surrounding the Sino-US relationship will remain a key focus, especially given that a strong stance on China continues to be a bipartisan consensus in the United States. With the US election campaign starting early in the year, we should expect increasing news flows on Sino-US relations, which could trigger some volatility.

Average Annualized Realized Market Volatility of S&P 500 (1986 - 2023)



Source: Value Partners, Bloomberg, based on monthly returns, as of December 2023.

Within Asia, there are also some important elections investors should watch out for, notably in Taiwan (January 2024), Indonesia (February 2024), South Korea (timing not confirmed yet) and India (June 2024). All of these, depending on the outcome of the elections, could result in changes in policy direction, international relations, and the relationships between China and ASEAN and other North Asian countries. All of these outcomes could potentially trigger some volatility for Asian assets. As such, whilst we remain optimistic overall on the outlook for the region in 2024, we also believe that it is important to keep a keen eye on risk management to navigate the increasingly complex investment landscape and the geopolitical environment in 2024.

We expect dividend equity focused strategies to perform well in 2024. Globally, we believe that Asian equities remain most attractive from a valuation perspective. The convergence of economic growth in the region with the rest of the world could result in some mean-reversion on valuation, thus providing further impetus for Asian equity markets to deliver strong returns in the coming year.

Asia investment outlook

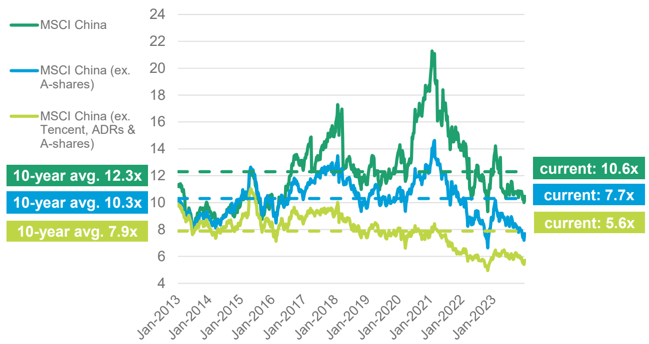
Asian equities outlook

At a high level, while growth has been patchy in China in 2023, the country has shown some signs of stabilsation in the near term, driven by additional policy support and an easing of tensions with the US. In other parts of Asia, select opportunities remain, supported by strong domestic markets, which make them more resilient against some of the wider global headwinds. Overall, stock selection remains crucial, in our opinion, especially as we expect markets to remain uneven going into 2024.

Below is our more detailed outlook for the various equity markets in Asia:

China equities: We are cautiously optimistic on Chinese equities, with the expectation that the market could experience a more significant recovery in the second half of 2024. Near-term economic challenges remain, but as the monetary cycle turns, we expect stronger policy support, which would result in a gradual "U-shaped" recovery in the coming years. We also believe that the low valuations offered by the market are attractive and could potentially see some mean-reversion to help further drive returns in 2024.

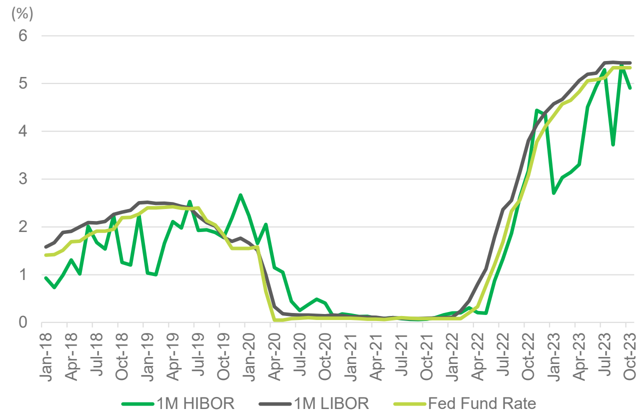
China market PE (x)



Source: Bloomberg, CICC, as of December 2023.

Hong Kong equities: As with Chinese equities, we are cautiously optimistic on Hong Kong equities. We should, however, note that the economic challenges facing Hong Kong equities could potentially be more difficult to resolve. High property prices and rents, as well as labour costs, continue to weigh on businesses. These issues are likely to take longer to resolve. The market is also more exposed to international capital and could experience higher volatility should geopolitical risks remain heightened. That said, the reverse could happen. Should there be a cyclical recovery in China, this supports Hong Kong equities, as international capital could re-enter the market quickly to capitalise on related opportunities. Like Chinese equities, valuations for Hong Kong equities are at a depressed level and, therefore, should provide long-term investors with an attractive entry point, as well as providing a cushion against further significant downside risks.

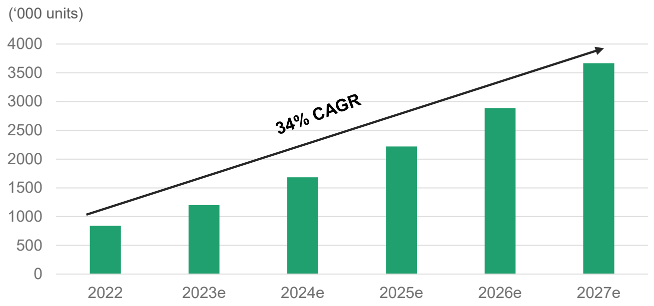
High interest rates have been a key drag to Hong Kong, but this may improve ahead



Source: Wind, CLSA, as of October 2023.

Taiwan equities: Taiwan was one of the better-performing Asian equity markets in 2023, bolstered by the positive momentum of AI and other new technologies, including autonomous driving and electric vehicles (EVs), and augmented and mixed reality (AR/MR) devices. We believe these trends could continue to drive new business opportunities for Taiwan's technology companies. Coupled with a potential turnaround of the consumer electronics downcycle, especially the demand for PCs and smartphones, these trends support the potential for the Taiwan market to continue to perform well in the year ahead. However, investors need to closely watch geopolitical events – particularly the forthcoming Taiwan elections and the wider Sino-US relations, inflationary pressures, and interest rates – that may all have an impact on Taiwan and could lead to volatility.

Strong demand for AI-related hardware bodes well for Technology companies in Taiwan

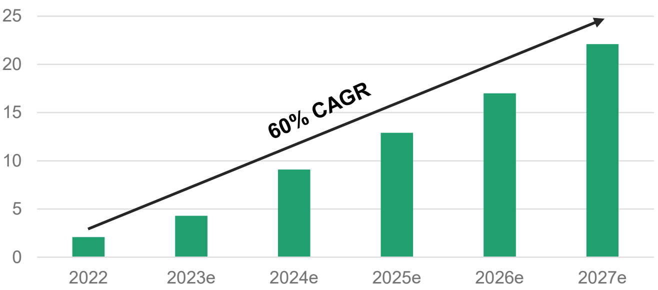


Source: Bloomberg Intelligence, CLSA, Trend Force, August 2023.

Korea equities: The Korean market experienced something of a roller-coaster ride in 2023, with the early excitement driven by the upbeat expectation on the technology sector offset by more recent setbacks. Looking into 2024, we are positive about the market on the back of an improving export outlook, mainly led by semiconductors, which should also partly offset the country's weak domestic consumption. However, market volatility will likely remain high, especially considering the government's recently introduced short-selling ban that will last throughout the first half of 2024.

Overall, we see selective opportunities in the Korean market and favor sectors that could enjoy structural growth and the prospect of global expansion, including semiconductor value chains, aesthetics, and autos. Meanwhile, we believe the low valuations of the market – as represented by a low price-to-book (PB) ratio – may offer some downside protection against the risks of geopolitical tensions and higher inflation.

IT companies in Korea - especially in the memory sector - will be bolstered by the rising demand for High Bandwidth Memory (HBM) products

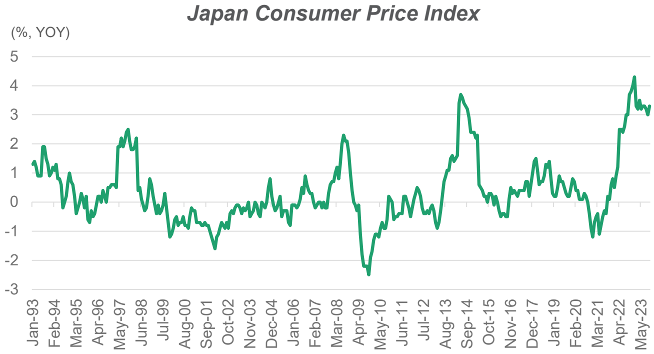


Source: Bloomberg Intelligence, CLSA, Trend Force, August 2023.

Japan equities: We hold a mildly cautious and arguably contrarian view of the Japanese equity market, given the complicated and somewhat contradicting macro conditions. On the one hand, the Bank of Japan (BOJ) has widened the yield curve control (YCC) policy band and committed to maintaining an ultra-easy monetary policy. On the other hand, the roaming fiscal stimulus is looking to reflate the economy further, posing an upside risk to the 2% inflation target (the most recently reported CPI is already around 3%). Hence, we believe the longer the BOJ maintains its negative interest rate policy and YCC, the higher the cost will be for the economy in due course. This would also be Japan's first time facing higher interest rates in more than two decades, posing additional uncertainty for consumers and investors alike. These realities could, in our view, lead to more near-term volatility in both the currency and the stock market.

For the first time in many years, Japan may tighten its monetary policies on high inflation

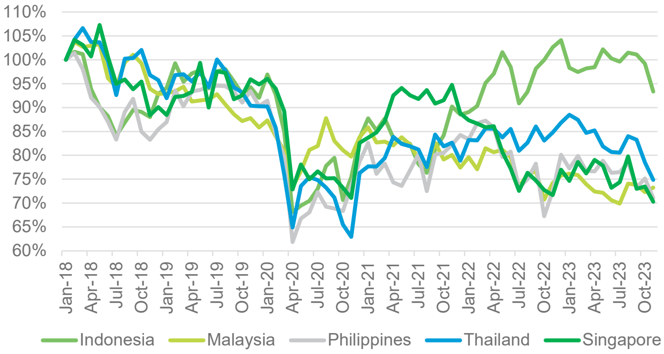
Japan Consumer Price Index



Source: Bloomberg, as of October 2023.

Southeast Asia equities: Southeast Asian markets delivered a mixed and generally lackluster performance in 2023, as the rate hikes in the US and weaker economic growth in China combined to limit their performance. With both factors likely on the mend in 2024, some regional markets could fare better, although the risks posed by geopolitical uncertainties may continue to linger. Amongst the key markets, we prefer Indonesia and the Philippines in the year ahead. Indonesia has a strong fiscal position and healthy credit growth. Further developments in the country's EV supply chain, driven by increasing investments from foreign companies into Indonesia's nickel mining and processing industry, remain growth drivers, along with infrastructure investments and crude palm oil. In the Philippines, we believe corporate investment demand could rise with an easing interest rate environment and stable currency, while consumption is also likely to pick up. Relatively speaking, we have a neutral to cautiously optimistic stance on the Singapore and Malaysian markets, but are more cautious on Thailand, where there is a persistent asset quality issue, and consumption may continue to remain weak.

The ASEAN markets have delivered mixed performance in recent years, and may continue to diverge

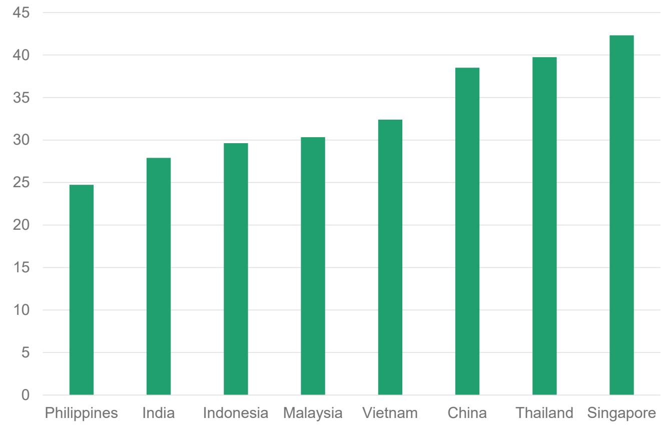


Source: Bloomberg, as of November 2023.

Indian equities: India's market delivered substantial outperformance in 2023, but we remain cautious of its extreme valuations. Currently, the market's forward-looking PE is at a near 80% premium relative to other emerging markets, leaving little margin of safety for investors. In particular, Indian banks are coming out of experiencing peak net interest margin (NIM) and benign credit costs, while IT companies are already witnessing slower revenue growth. The consumption growth pattern is also uneven and is skewed toward high-end discretionary spending. For investors holding a long-term and optimistic view of the Indian market, we would recommend a selective approach, with a particular focus on opportunities in the utilities and energy sectors.

India enjoys many structural tailwinds, like the young population, but also has its challenges and valuations are at the extreme

Median population age by country (2022)



Source: CLSA, UNCTAD, 2022.

The outlook for Asian and Chinese investment grade bond issuers remains solid, with low default rate risk supporting credit spreads. Meanwhile, the landscape of Asian high yield has changed significantly, with fewer constituents from the Chinese property sector, reflecting an increasingly more stable credit quality.

Asia investment outlook

Asia fixed income outlook

At a high level, the outlook for Asian and Chinese investment grade (IG) bond issuers remains solid, with low default rate risk supporting credit spreads. Meanwhile, the landscape of Asian high yield (HY) has changed significantly, with fewer constituents from the Chinese property sector, reflecting an increasingly more stable credit quality. Credit selection and the successful identification of dislocation opportunities remain crucial, and the pace and breadth of corporates' earnings and cash flow recovery remain our key focus. Bond buybacks have also become more prevalent, reducing the refinancing burden for bond issuers and underpinning the technicals for select high yield segments. Given the stabilising credit outlook, improved sector diversification, and expectations of lower default rates, we see a better value proposition in Asian high yield bonds heading into 2024 (Figure 1).

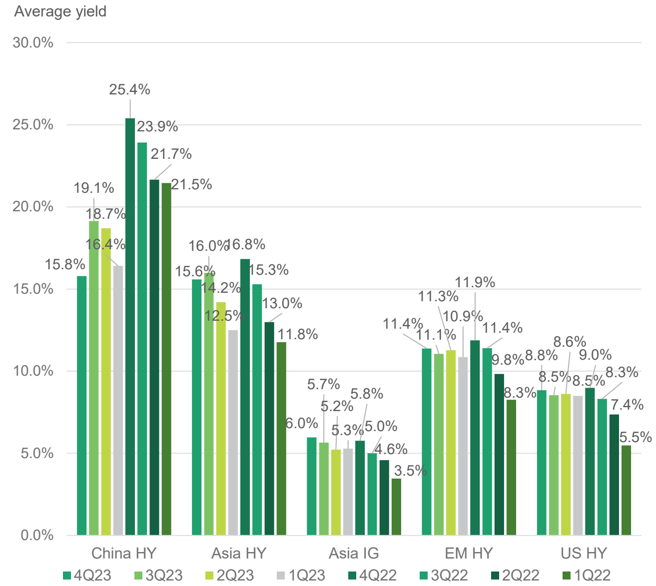
Decent carry also provides downside protection in an overall slowing growth environment. On the technical front (Figure 2), we expect bond supply to only marginally accelerate in the Asian IG space, as onshore funding access remains buoyant. Some issuers could turn opportunistic if the US Treasury yield moderates from the current level. We continue to expect the overall low bond supply in the Asian HY segment.

Given the expected challenging environment in 2024, with largely restrictive US rates and China's patchy growth recovery, we prefer a barbell strategy to balance risk and reward. Asian IG bonds, yielding around 5-6%, provide a decent income choice with a shorter duration than their US peers. We see ongoing opportunities to rotate into longer-term bonds to reduce the re-investment risk when there is a clearer picture of the path for a Fed pivot. The Asian HY space also offers pockets of opportunities for issuers with decent-quality assets and access to onshore capital markets that facilitate their ability to refinance.

Our theme on credit selection is to stay with names that benefit from a consumption-led recovery or deleveraging trend. We also continue to monitor the speed of a fundamental turnaround in China and maintain our strategy of diversifying our exposure into India, Indonesia, Hong Kong, and Macau.

Figure 1: Compelling Asia bond valuations versus peers, with improved sector diversification and default rates stabilising

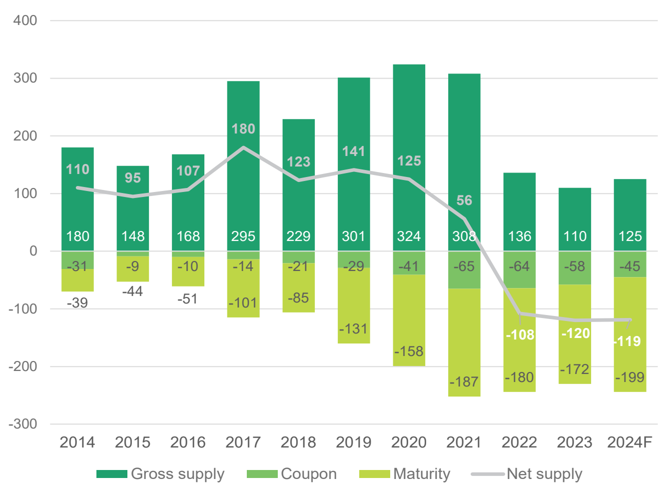
Bond valuation of global credit markets



Source: JP Morgan Asia Credit Index, Bloomberg Index; as of December 2023.

JP Morgan Asia Credit Index Investment Grade ("Asia IG Index") and High Yield ("Asia HY Index") generated 7.0% and 3.9%, respectively, up to 18 December 2023, versus 1.7% and -1.4% up to 9M23.

Figure 2: Lower net bond supply supports select segments in Asia credit market



Source: JPM, Bloomberg, 2023.

Below is our more detailed outlook for the various fixed income markets in Asia:

Onshore China: The China Government Bond (CGB) yield experienced a V-shape move during the third quarter of 2023, with a weaker economic outlook accompanied by a 20bp spike since August lows. Yields also advanced in mid-November as front-end liquidity stayed tight amid increased government bond supply. With property and consumption activities lacking sustainable strength, the risk of a further uptick in CGB yields is controllable, unless there is a rising likelihood of a ramp-up on the fiscal budget, which increases bond supply.

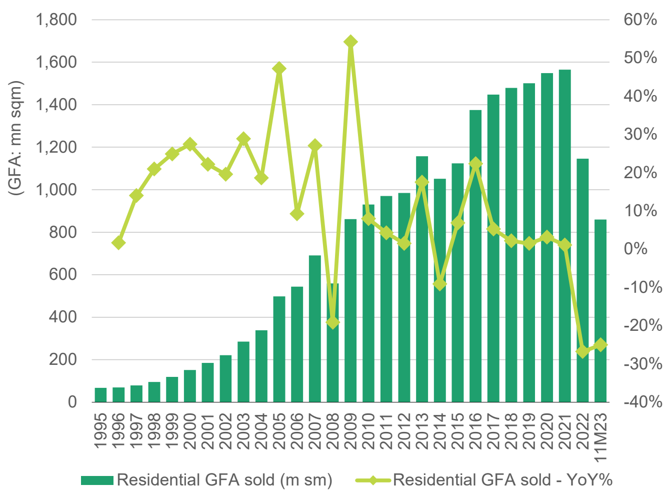
The People's Bank of China will likely exercise caution on policy rate cuts, given their impact on capital outflows, net interest margin (NIM) pressure for banks, and depreciation pressure on the renminbi. The gradual economic rebound should also reduce the need to cut rates. The dollar strength, albeit softening, leads us to believe that the yield gap between US and China government bonds will stay wide in the short-to-medium term.

Asia Investment Grade: Asian investment grade bonds should offer defensiveness with an attractive all-in yield and favorable technicals. However, we see limited room for further spread compression based on historical averages and when compared to US peers. However, a material widening in the credit spread is not our base case, as US credit spreads should avoid a recession-style selloff. Some consolidation in the US treasury yield will be a key driver for performance in 2024.

The slower and uneven growth in China and high US rates will be key risk factors for Asian credit in 2024. Nevertheless, we expect Asian IG to remain broadly stable, with high-rated credits being the most resilient due to their strong balance sheets and market positions, as well as access to funding. The weight of Asia IG and high-rated credits within the broader index have also increased, with A/AA credits constituting around 44% of the JACI Composite Index, followed by BBB at 41%. This, together with low fallen angel risk and limited bond supply, should bode well for Asia IG to remain resilient in 2024.

China Property: The various easing measures for the sector are yet to provide a game changer on broad-based confidence and demand weakness. Data shows that property sales exhibited a marginal rebound in September despite rounds of measures introduced in August that focused on the recovery of higher-tier cities, indicating the need for more easing measures. We expect sales growth to bottom in 2023-2024 as concerns over job security and income growth remain key hurdles for housing demand, which take time to recover. This view is also predicated on our expectations that the government will maintain a supportive, non-aggressive tone in reviving the sector and a slowing urbanisation rate.

A slow grind in recovery for China's property sector



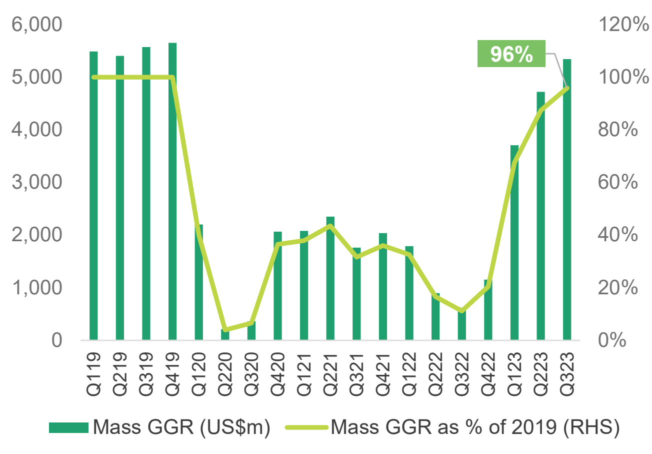
Source: National Bureau of Statistics of China; up to November 2023.

The divergence trend for state-owned enterprise (SOE) and private-owned enterprise (POE) developers will likely be sustained, with the former benefiting from policies supporting higher-tier markets and access to funding. We have a cautious view on a POE sales turnaround, given limited land acquisitions on tight funding, lower new supply, and restrictive property sales escrow accounts that prioritise project delivery.

Overall, we expect nationwide property sales value to have fallen by 10% in 2023, narrowing from the -28% YoY decline in 2022 and maintaining a soft trend in 2024 from about -5% to -10% YoY. New starts will likely decline on a similar scale due to constrained land acquisitions, low sell-through rates, and more resources devoted to project completion, dragging real estate investment (REI) growth. Separately, the government has been promoting the renewal of old urban villages in high-tier cities to revive REI. However, the scale, pace of property price recovery, and funding sources will likely differ from the shanty town redevelopment scheme, which was primarily funded by policy bank loans that resulted in a sector upcycle.

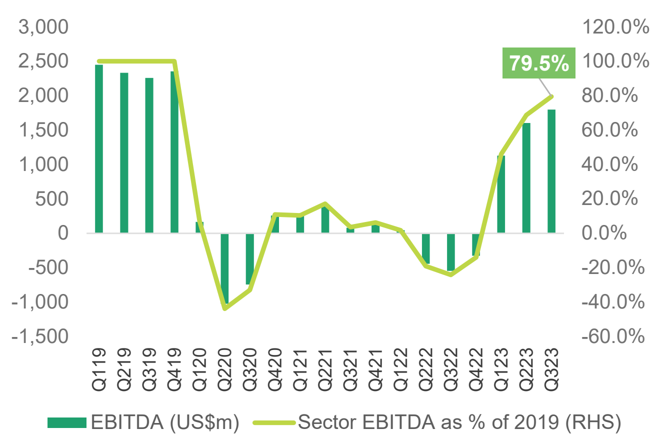
Macau Gaming: Gaming operators have benefitted from a strong recovery in gross gaming revenue (GGR). The latest data shows that market-wide mass GGR has already improved to around 90% of 2019 levels. We believe this mass-driven growth trend will support improvement in operators' credit profiles in terms of EBITDA growth and free cash flow generation on a YoY basis. Industry EBITDA would land in the range of US$6-7 billion in 2023, which more than covers interest costs and capex amounting to US$3-4 billion. This will facilitate deleveraging and prompt more rating upgrade actions. We note that while China's softer growth outlook may impact a mass market recovery, the operators' credit profile will remain stable in the medium term.

Resilient mass GGR recovery gained momentum and back to 2019 levels



Source: UBS; Company data up to 3Q23.

Decent recovery on industry EBITDA



Source: UBS; Company data up to 3Q23.

There is some room for mass demand to ramp up, given more new hotel rooms and improving labor issues. This, coupled with steady margins from operating leverage, should boost EBITDA in 2024. Further outperformance for the sector may drive mass demand to reach 110-120% of 2019 levels. However, this could be a challenging task on expectations of slower growth in China.

With non-demanding bond valuations, limited new supply, and improving fundamental trends, we believe the sector will continue to provide good carry opportunities and diversification benefits within Asian HY.

Indian Corporates: Thanks to its resilient domestic demand and substantial government capex that has boosted investment, India remains one of the growth engines within emerging markets. Despite expectations of a high fiscal deficit to continue, the government's limited external debt position moderates currency and capital flight risk. This should anchor macro stability, and the overall picture should not deviate much with the upcoming general elections in 2024.

While Indian HY corporates' fundamentals are broadly on a solid footing with supportive onshore market financing conditions, bond valuations (spanning renewables, commodities, and utilities) appear rich relative to their US peers. That said, the sector should remain well-anchored, given the favorable macro backdrop and the lack of bond supply. We adhere to our view on potential credit spreads widening in the space on a US hard landing scenario, the impact of sustained high oil prices, and the monsoon season's risks to inflation. Any consolidation in this space would provide investment opportunities. We expect the Reserve Bank of India to keep rates unchanged for the rest of FY24 (ending March).

Indonesian Corporates: Indonesia's quick consolidation of its fiscal deficit was supported by the surge in commodity prices and improved domestic economic conditions. On the other hand, slower global and China growth should cool down the country's export and commodity outlook. Nevertheless, Indonesia's prudent fiscal stance and manageable inflation support a resilient macro picture. The country's focus on higher value chain manufacturing and the electric vehicle ecosystem could attract foreign inflows and provide growth alternatives in the long run. The Bank of Indonesia's emphasis on currency stability should avoid a volatile move in the Indonesian rupiah. Overall, we do not anticipate major policy changes post-election in February 2024. We closely monitor if the weaker demand from China will impact commodity prices.

In 2024, we expect new and different risks and opportunities to arise in the markets as a result of the changing macroeconomic environment and geopolitical landscape. We believe investors could capture these opportunities through allocating to assets with more attractive valuations, given the expected mean reversion of returns, but also balance that with some hedges against downside risks.

Summary

Global asset allocation views 2024

Asset class	View	6-12 month views
Equities		
US	▼	• Valuations of US equities are high both on a relative and absolute basis, pricing in most of the expectations of interest rate cuts in 2024. • While strong economic data indicates an increasing probability of soft-landing, the risk of recession and a re-acceleration of inflation remains. This might result in a rather significant correction in the market, given where valuations are.
Europe	▼	• Recession risks in Europe remain high, with some countries already seeing a contraction in their economies. • While inflation has moderated, the current pricing of an interest rate cut by Q2 2024 looks to be aggressive. Should interest rates stay higher for longer, volatility might ensue.
Japan	►	• The tailwind from the weaker Japanese yen is helping company earnings, given their large overseas revenue exposure. The strong focus on improving shareholder returns by the regulator and exchange has sparked an increase in share buyback activities, which is also supportive of the market. • However, inflation and wage pressures are still rising. The Bank of Japan eventually would need to exit from its ultra-easing monetary policy. This might reverse the tailwind enjoyed by Japanese equities, putting the market at risk of a correction.
North Asia (ex-Japan)	▲	• We believe China's economy is nearing its bottom, and its recovery will likely be gradual rather than V-shape. As expectations are very low and positioning is extremely light, we believe the market will recover gradually from here. • For Taiwan and Korea, we believe the positive momentum, driven by artificial intelligence and other new technologies, could continue driving new business opportunities for tech companies. However, investors will need to closely watch geopolitical events and changes in monetary policies that may cause market volatility.

▲ ***Add exposure*** ► ***Remain the same*** ▼ ***Reduce exposure***

Source: Value Partners, December 2023.

Asset class	View	6-12 month views
South Asia	►	• The domestic markets in Asia remain healthy, and inflation concerns are receding. Some countries have room for monetary or fiscal policy easing to support the recovery if needed. However, the slowdown in export orders will cap the upside as developed markets go into a recession. • Within South Asia, we prefer Indonesia and the Philippines. Indonesia has a strong fiscal position and healthy credit growth, while corporate investment demand in the Philippines could rise on the back of the easing interest rate environment and stable currency. • In India, we are cautious about its extreme valuations. Investors holding a long-term and optimistic view of the Indian market will need to be selective. We see opportunities in the utilities and energy sectors.
Other emerging markets	►	• As global growth slows, weaker exports will likely impact other emerging markets. Softer commodity prices are also a headwind for many of these markets. • On the other hand, domestic demand has become healthier, and receding inflationary pressure, as well as a weaker US dollar, are both supportive of some monetary easing, which could prove positive for the markets too.
Bonds		
US Treasury	►	• Treasury yields will likely remain volatile as the timing and the magnitude of rate cuts remain uncertain. • With the increasing budget deficit, the larger supply of Treasuries could keep rates volatility elevated. • With that said, moderating inflation and the risk of recession means that investors should also own some duration for diversification, especially given the higher carry offered by the asset class.
Asian investment grade	▲	• Asia investment grade bonds are yielding around 6%. As demand remains strong while new supply remains tight, there is further room for spread tightening. • Asia investment grade bonds offer defensiveness, especially for short-dated bonds, which remain in a sweet spot with an attractive all-in yield.

▲ ***Add exposure*** ► ***Remain the same*** ▼ ***Reduce exposure***

Source: Value Partners, December 2023.

Asset class	View	6-12 month views
Asian high yield	►	• The landscape of Asia high yield has changed, with fewer constituents from the Chinese property sector as the weaker credits have already defaulted, reflecting a more stable credit quality. • Sentiment has gradually improved as China's economy is nearing its bottom. Macau and China's travel-related bonds remain a bright spot as their recovery remains on track. • As interest rates go down, we are likely to see renewed investors' interest in the asset class in the second half of 2024.
Emerging markets bond	►	• The stabilising US dollar and US Treasury yields support sentiment toward emerging market bonds. Receding inflationary pressure provides room for EM central banks to conduct easing ahead of the US Fed, which could prove positive for the asset class. • However, as global growth slows and recession risk remains, emerging market bonds will likely be negatively impacted, especially as commodity prices become weaker.
Alternatives		
Real estate	►	• The end of the rate hike cycle helps stabilise the real estate sector. • However, as global recession risk remains, the outlook for real estate demand remains uncertain.
Gold	▲	• Gold should continue to be supported as the US rate hike cycle has likely come to an end. • It also remains a robust hedge against heightened geopolitical risks.
Base metals	▼	• Commodity prices will remain weak as recession risks have not been fully priced in. • Although China's economy is expected to recover gradually, demand for commodities will likely remain soft for some time, especially as the property sector needs time to recover.
Oil	►	• Oil prices will likely remain range-bound as the counter-balancing force of reduced demand and production cuts offset each other. • Heightened geopolitical tensions, particularly in the Middle East, may cause short-term spikes in oil prices.
Cash	►	• The current cash yield is attractive, providing a c.5% return. • However, as rates have peaked, there will be a rolling down effect on the return of holding cash.

▲ ***Add exposure*** ► ***Remain the same*** ▼ ***Reduce exposure***

Source: Value Partners, December 2023.

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