Maybank Investment Strategy

2nd Quarter of 2023

Summary

Risk assets endured a choppy March after the collapse of Silicon Valley Bank and the turmoil at Credit Suisse triggered fears of a financial crisis. Notably, bond market volatility spiked to an all-time high with escalating concerns on the banking sector.

Despite the heightened market volatility, global equities managed to climb with MSCI All-Country (AC) World Index returning 3.2% in March. Notably, investors were pricing in less aggressive monetary tightening, which lent support to the market. Technology and growth stocks also outperformed.

Meanwhile, global bonds witnessed positive returns amid the reduced rate hike expectations. In particular, the U.S. Treasuries (UST) benefitted from a flight-to- safety with the 10-year yield dipping below 3.5%. In addition, gold prices rallied 7.8% and broke above USD 2,000/ounce briefly.

Macro Outlook and Investment Strategy

We remain wary of the downside risks related to the banking sector stress with the tighter credit conditions expected to weigh on overall growth. Still, policymakers stand ready to respond swiftly to limit contagion risk. Central banks may also exercise flexibility in their monetary policies though they are unlikely to pivot and ease aggressively given the sticky inflation outlook.

In view of the above, our base case for a mild recession in the U.S. and Europe remains although the risk of a severe downturn could keep markets volatile. As such, it remains critical for investors to stay prudent and nimble.

Asset allocation wise, we maintain a defensive stance by overweighting cash and fixed income over equities. We continue to favour UST as an effective hedge against recession while seeking quality carry through high grade credits. We would however be more selective towards Additional Tier-1 (AT1) bonds given the banking doldrums.

Meanwhile, we retain our cautious stance on overall equities but are positively biased towards China given the market's attractive risk reward. Further evidence of earnings recovery and potentially corporate restructuring should propel China stocks higher. In contrast, we see further downside for U.S. corporate earnings that may become more apparent in the upcoming reporting season.

Tactical Asset Allocation			
Asset Class *		Sector *	
Equity	-	U.S.	-
		Europe	-
		Japan	=
		Asia ex-Japan	=
Bonds	+	Sovereigns	+
		Developed Markets (DM) Investment Grade (IG)	+
		Developed Markets (DM) High Yield (HY)	-
		Emerging Markets (EM) Bonds	-
Alternatives	=	Hedge Funds	=
		Gold	=
Cash	+		

Source: Maybank Wealth Management Research

* Overweight: +, Neutral: =, Underweight:-

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Asset Class	Changes to date (in USD currency)		
	1M	3M	12M
Equity			
MSCI USA	3.6%	7.7%	7.7%
MSCI Europe	2.5%	10.7%	10.7%
MSCI Japan	4.1%	6.4%	6.4%
MSCI Asia ex-Japan	3.5%	4.4%	4.4%
China	4.5%	4.7%	4.7%
Hong Kong	1.2%	-2.4%	-2.4%
Taiwan	3.1%	14.8%	14.8%
South Korea	4.9%	9.7%	9.7%
India	1.2%	-6.3%	-6.3%
Singapore	5.0%	7.1%	7.1%
Malaysia	1.0%	-3.6%	-3.6%
Indonesia	4.0%	6.5%	6.5%
Thailand	4.4%	-1.6%	-1.6%
Philippines	2.7%	2.7%	2.7%
Bonds			
U.S. Treasuries	3.7%	3.1%	3.1%
Barclays Global IG	3.2%	3.0%	3.0%
Barclays Global HY	0.9%	3.1%	3.1%
Barclays EM Bonds	1.2%	2.1%	2.1%
Alternatives			
Hedge Funds	-1.4%	-0.2%	-0.2%
Gold	7.8%	8.0%	8.0%
WTI Crude	-1.8%	-5.7%	-5.7%
Dollar Index (DXY)	-2.3%	-1.0%	-1.0%

Source: Bloomberg | 31 March 2023

Summary - BONDS

Credit default spreads jumped across the board in 1Q due to concerns over the U.S. banking system and the chaos in bank subordinated bond market. The rates market was also volatile, with 10-year UST retreating from a quarter- high of 4.09% to 3.47% (Figure 3) as at end-March amid bets that the Fed will cut rates in 2H due to growing recession risks.

In the U.S., while core and headline Consumer Price index (CPI) are showing signs of easing, the overall inflation remains elevated and that is posing a challenge for the Federal Reserve's (Fed) objectives – price and financial stability. Consequently, the Fed had little option but to deliver a 25 basis points (bps) rate hike at the March policy meeting.

In the latest March Fed's "dot plot", the projected median Fed funds rate was left unchanged for end-2023(Figure4) at 5.1%, and this implies an additional of 25 bps of rate hike for this year. For end-2024, Fed's projection was revised upwards from 4.1% to 4.3%, implying a lower rate cut of 75bps instead.

BONDS – Market Outlook

While lingering worries on inflation remains, Fed officials are wary of the unintended consequences to financial markets given their aggressive rate policy stance over the past one year. The collapse of some U.S. regional banks and the subsequent contagion effects to global banking peers, have exacerbated fear of interconnected domino effect during a credit crunch.

While several major central banks have maintained their rate hikes in March, we expect them to continue exercising flexibility in their monetary policies. Meanwhile, we expect the Fed to deliver one more 25bps rate hike in 1H and pause for the rest of the year. With the rate hike cycle peaking, our 10-year UST yield forecast remains unchanged at 3.0% by end-2023.

In addition, we do not expect the Fed to aggressively ease in 2H given the sticky inflation outlook and still resilient labour market. Notably, in the Fed's latest Summary of Economic Projections, the 2023 unemployment and core PCE inflation projections were left unchanged at 4.5% and 3.6%, respectively.

Given our base case for a mild recession, we continue to overweight fixed income and maintain our preference for sovereign bonds to credits.

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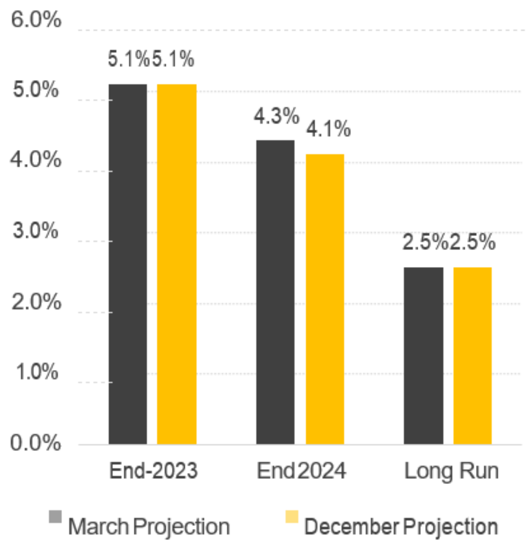
Figure 3: 10-year UST yieldfell in 1Q as recession fear mounts

Source: Bloomberg I 31 March 2023

Figure 4: Median forecasts for the Fed funds rate based on the Fed's "dot plot"



Source: Bloomberg I 31 March2023

BONDS - Market Outlook Cont.

For credits, given the ongoing concerns over recession risk and negative repercussions from tightening financial conditions, we maintain our cautious stance with a preference for Investment Grade (IG) over High Yield (HY) bonds.

We maintain an overweight stance on Developed Market (DM) IG credit which should benefit from a flight-to- quality in an event of a recession. In contrast, we maintain an underweight stance on DM HY credit as the risk reward profile remains unattractive. Furthermore, rising recession risk amid the banking sector stresses could drive credit spreads and default rates higher from current levels.

The European bank capital sector has repriced following the Swiss decision to write down CHF16 billion of Credit AT1 bonds ahead of equity capital. While the authorities including the European Central Bank, Bank of England, Monetary Authority of Singapore, and Hong Kong Monetary Authority, have publicly stated that they would respect the capital structure hierarchy, investors will still demand a higher risk premium for investing into AT1 bonds in the short-term. As such, the asset class could remain volatile amid a recalibration of AT1 risks. Investors should remain selective and consider reducing concentrated positions within the European banking sector.

We are underweight Emerging Market (EM) bonds, with a preference for higher quality IG bonds given the uncertain market outlook. We are underweight EM HY credit as the weaker corporates will be more affected by the higher interest rates and their access to debt capital markets may be undermined amid heightened risk of fund outflows.

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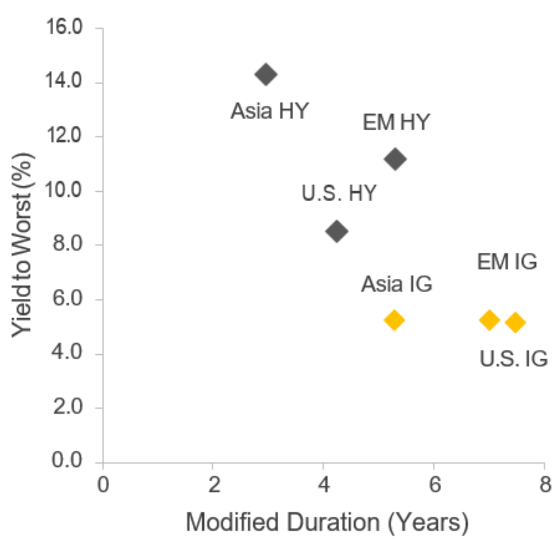
BONDS - Market Outlook Cont.

Within Asia, we have a neutral view on Asia IG credit given fair valuations. That said, the strong credit quality and relatively shorter duration in Asia IG bonds provide resilience amidst market volatility. Meanwhile, we are neutral on Asia HY credit as supportive policy measures suggests a more balanced risk reward outlook. Nevertheless, the risks related to China's property market remain as contracted sales have yet to show a sustainable recovery and homebuyer confidence are not fully restored

Key Risks

- A deeper and protracted economic downturn.
- Escalating geopolitical tensions.

Figure 5: Yield-to-Worst and modified duration of bond sub-asset classes



Note: The above indices are based on Bloomberg Barclays bond indices.

Source: Maybank Group Wealth Management Research I 31 March 2023

Summary – EQUITIES

Financial cracks have emerged as a result of aggressive monetary policy tightening over the past year. The failure of two U.S. regional banks and the collapse of Credit Suisse have triggered some panic selling in March.

Positively, the policy responses from central banks have been swift and powerful, helping to prevent the banking crisis from spreading. Consequently, some calm has returned to the equity markets, with the CBOEVIX index retreating around 22% from year-to-date high.

Looking ahead, we are still wary of downside risks as major stresses remain and European banks' credit default spreads continue to stay elevated. As such, we maintain our underweight stance on equities, with the U.S. and Europe being our least preferred markets.

Defensive sectors including Consumer Staples and Healthcare may outperform in current environment given their resilient earnings profile. Selected defensive technology companies which are still able to grow even in difficult economic environments may outperform too.

EQUITIES - Market Outlook

The recent bank turmoil has increased the risk of a U.S. recession and the re-steepening of the 10-year / 2-year UST yield curve from trough suggests an imminent recession (Figure 6). Yet, the strong labour market is keeping inflation elevated, complicating the outlook for the Fed as it sought to balance price stability with financial stability.

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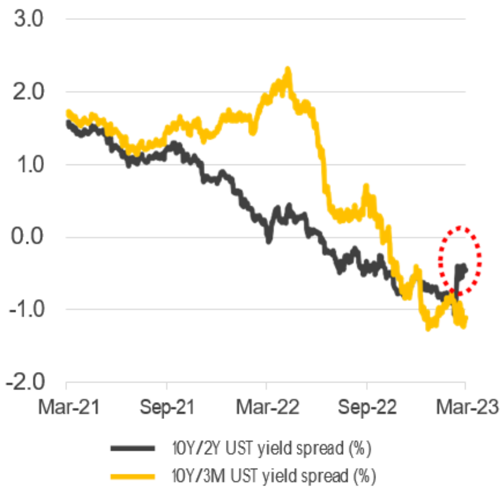
EQUITIES – Market Outlook Cont.

Meanwhile, we continue to see downside risks to the U.S. earnings and more downgrades could occur during the 1Q reporting season. Analysts are still projecting an earnings growth of 1.5% (Figure 7) and revenue growth of 2.0% for 2023. Given the many uncertainties and with the S&P500 still trading at unattractive forward price-to- earnings ratio of 17.7x, we maintain our underweight stance on U.S. equities.

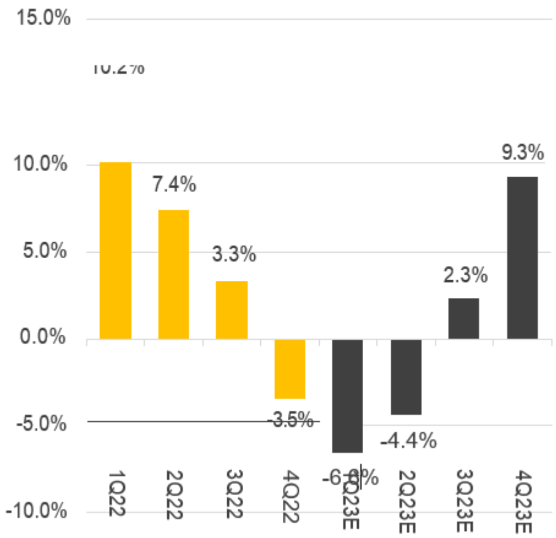
We continue to underweight Europe despite the jump in Eurozone Composite Purchasing Managers' Index (PMI) to 54.1 in March from 52.0 in February. The full impact of the monetary tightening is likely to start to be felt. Meanwhile, the wave of uncertainty triggered by Credit Suisse has not settled yet and we are bracing for continued volatility ahead.

Figure 6: Re-steepening of 10Y/2Y UST yield curve from trough suggests imminent recession



Source: Bloomberg I 31 March 2023

Figure 7: S&P 500 Earnings Growth Year-on- Year (%)



Source: Factset | 31 March 2023

We expect corporate earnings to soften due to the slowdown in the global economy, particularly with rising recession risks in the U.S. and Europe. However, China's stronger economic outlook could mitigate some of the earnings headwinds in the near term. In addition, the Bank of Japan's accommodative monetary policy could provide some support in this challenging environment. As such, we retain our neutral stance on Japan.

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EQUITIES – Market Outlook Cont.

China's economic recovery is on a firmer footing with the latest manufacturing and services PMI (Figure 8) now above the key expansionary threshold. Better corporate and consumer confidence should help to drive higher spending. Notably, China corporates are seeing business momentum picking up and guiding more robust earnings outlook in the latest earnings results. Coupled with an undemanding valuation, at forward price-to-earnings ratio of 10.2x (Figure9), we maintain our overweight stance

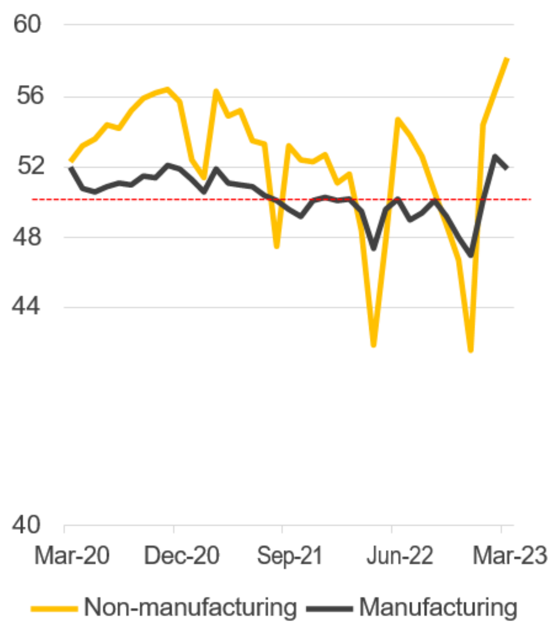
India equities have performed poorly year-to-date, owing to the issues surrounding Adani Group. Meanwhile, India has asked its state-owned banks to focus on stress testing their business models after they were found to have fallen behind on developing comprehensive models that are meant to withstand risks of failure. With Financials constituting a sizeable portion in MSCI India, this could continue to dampen investor's sentiment even though valuations are now more reasonable than in the beginning of the year. Consequently, we retain our underweight stance on India.

In South-East Asia, the banking turmoil in the developed markets has not derailed the financial sector in this region given its limited exposure and more robust fundamentals. However, the region is not immune to a global slowdown, and a defensive positioning is still favoured. While Malaysia is trading at inexpensive valuations, lingering political uncertainties, notably with six state elections to be held in June, will put a lid on its upside potential. Thus, we downgrade Malaysia to neutral from overweight.

Key Risks

- A deeper and protracted economic downturn.
- Worse-than-expected deterioration in corporate earnings.
- Escalation in geopolitical uncertainties.

Figure 8: China's Manufacturing and Services PMIs are above key expansionary levels



Source: Bloomberg | 31 March 2023

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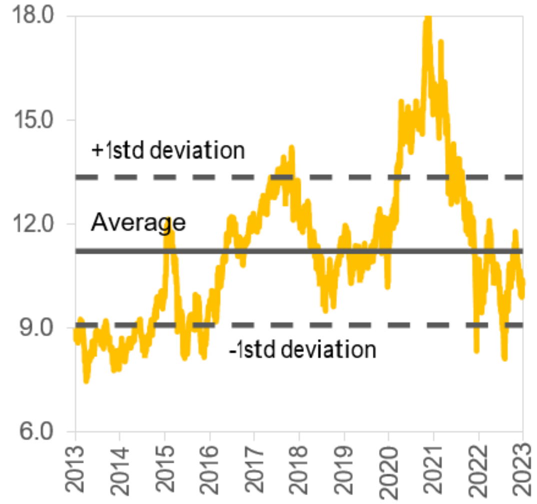
Figure 9: MSCI China is trading at an attractive forward price-to-earnings ratio of 10.2x versus historical average of 11.2x



Source: Bloomberg |31 March 2023

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