CIO Weekly GLOBAL MULTI-ASSET

3 June 2024

Key Points

- **Equities:** Worries over higher-for-longer rates negatively impacted global stock markets
- **Credit:** Strong US households imply that the mortgage market is healthy despite widening spreads. MBS a unique opportunity for government-backed yields
- **FX:** Stay vigilant of downside risks in the USD in June; EUR/USD to break above 1.08-1.09 range if ECB delivers hawkish interest rate cut at 6 June meeting
- **Rates:** Steepening for US 2Y/10Y curve is still at play; Expect ongoing steepening of CGB curve alongside commencement of CNY1tn ultra-long special sovereign bond issuance
- **The Week Ahead:** Keep a lookout for US Change in Nonfarm Payrolls; China Trade Balance

GLOBAL MULTI-ASSET RETURNS

Index	Close	Overnight	YTD
DJIA	38,686	1.5%	2.6%
S&P 500	5,278	0.8%	10.6%
NASDAQ	16,735	0.0%	11.5%
Stoxx Europe 600	518	0.3%	8.2%
DAX	18,498	0.0%	10.4%
CAC 40	7,993	0.2%	6.0%
FTSE 100	8,275	0.5%	7.0%
MSCI AxJ	671	-0.8%	4.5%
Nikkei 225	38,488	1.1%	15.0%
SHCOMP	3,087	-0.2%	3.8%
Hang Seng	18,080	-0.8%	6.1%
MSCI EM	1,049	-0.9%	2.5%
UST10-yr yield*	4.50	-4.8	61.9
JGB 10-yr yield*	1.06	0.5	45.6
Bund 10-yr yield*	2.66	1.2	64.2
US HY spread*	3.08	-2.0	-15.0
EM spread*	316.82	20.1	-2.1
WTI (USD)	76.99	-1.2%	7.5%
LMEX	4,362.90	-1.3%	16.0%
Gold (USD)	2,327.33	-0.7%	12.8%

Source: Bloomberg
* Changes in basis points

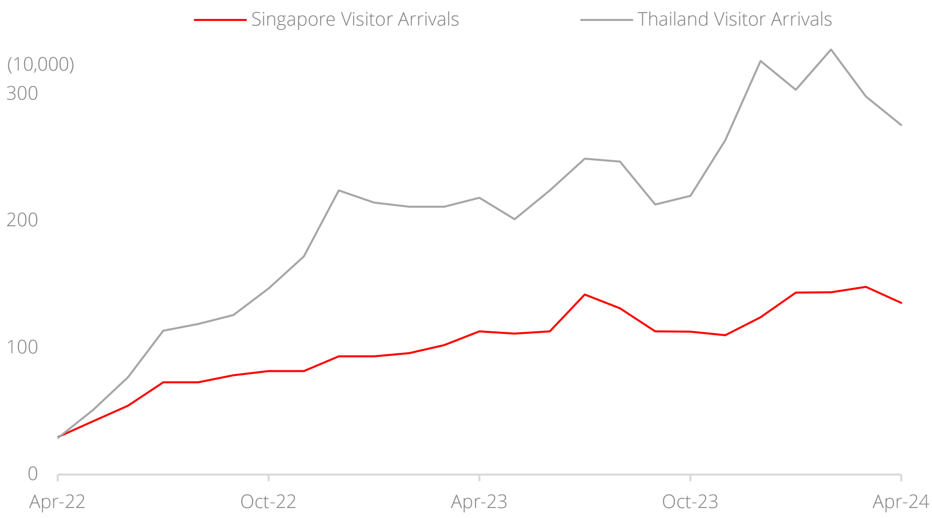
Equities: Global equities decline on fears of higher-for-longer rate

Hawkish Fed rhetoric affected global equity markets. The Dow Jones, S&P 500, and the NASDAQ dropped 1.0%, 0.5%, and 1.1%, respectively for the week. Technology stocks did not perform well, while US 10Y Treasuries hit a recent high. Even though inflation data was in line with market expectations, hawkish comments from US Minneapolis Federal Reserve (Fed) President Neel Kashkari cast a pall over markets. Higher-than-expected inflation in Europe also dragged markets lower. The Stoxx 600 and the FTSE both retreated 0.5% for the week. The Nikkei 225 dropped 0.4% amid news that Japan's industrial output fell in April. The HSI fell 2.8%, but Hong Kong markets might have retraced due to profit taking after the sharp increase in the beginning of the month. The SHCOMP dipped 0.1% as China's PMI fell to 49.5 in May.

Topic in focus: ASEAN – A growth engine for the global economy. ASEAN's economic recovery is expected to continue in 2024, underpinned by resilient domestic demand and the easing of supply chain disruptions. While monitoring China's growth is prudent given its links with the region, ASEAN's growth outlook remains positive, supported by trade-oriented economies, recovery in the electronics cycle, and tailwinds from travel and tourism. The robust 4.7% GDP growth forecast and bottoming exports provide fundamental support. Urbanisation, demographics, and integration tailwinds also bode well for businesses expanding in ASEAN, cementing its status as a major global growth engine. Longer-term, we see opportunities in supply chain reconfiguration beneficiaries and critical infrastructure providers, particularly for commodities and steel.

Key investment themes include consumer and telecom sectors in Indonesia; Thailand's tourism and industrial names that will benefit from the visa waiver and resurgence in FDI applications; and Singapore banks, as well as retail and hospitality REITs benefitting from events. Bright spots also include Malaysia's construction industry and Vietnam's potential re-rating due to rapid growth, low urbanisation, and possible index inclusion.

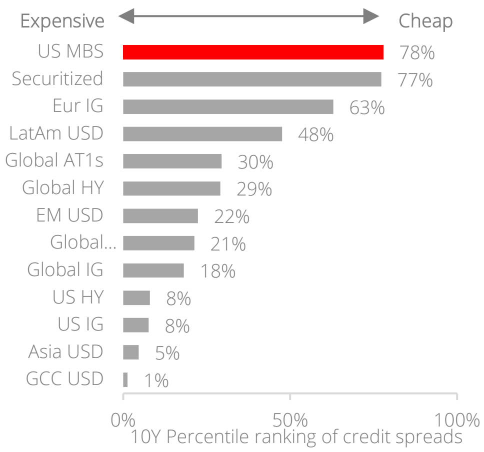
Figure 1: Tourism trends in ASEAN are on the rise



Source: Bloomberg, DBS

Credit: Value remains in US MBS

Figure 2: US MBS remains cheap on spread terms



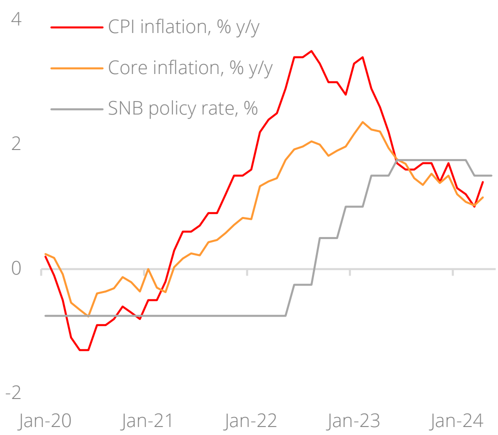
Source: Bloomberg, DBS

US households as pillars of support. The strength of US households remains one of the engines of the dominant US economy. Unlike during the 2008 Global Financial Crisis – when leverage was high – household balance sheets today have remained healthy, which has allowed greater bandwidth to tolerate the Fed-induced higher rates environment. Moreover, the US is relatively unique in its issuance of long-dated mortgages – households who had financed their home purchases in the low-rate years of 2020-2021 are insulated from the effects of the hiking cycle. Given such, we would be remiss not to mention one of the largest asset classes in the US bond market – agency mortgage-backed securities (MBS), as an attractive opportunity in fixed income.

Strong households would not default on their mortgages. Moreover, prepayment risk has declined as most US homeowners had refinanced their mortgages in the low rates years of 2020-2021. At present, more than three-quarters of the index have coupon rates below 3.5%; homeowners would unlikely prepay these mortgages given the prevailing rates of c.7%. Even so, MBS spreads are trading at some of their cheapest levels in history, likely due to (a) the Fed running off their MBS holdings under quantitative tightening, and (b) peripheral concerns on commercial MBS given the weakness in the commercial real estate sector. We believe agency MBS to be a unique opportunity for government-supported yields given their undemanding spread valuations and precedence as a Fed policy toolkit in times of severe distress.

FX: USD to extend its weakness into June

Figure 3: SNB will refrain from a back-to-back cut in June



Source: Bloomberg, DBS

Stay vigilant of downside risks in the USD in June. The Fed's narrative to be patient on interest rate cuts has become more bark than bite without the backing of US data. At next week's Federal Open Market Committee meeting, we expect the Fed to set a high hurdle for a rate hike and to stay the course for later and fewer rate cuts. With the US economy moving from exceptional growth towards a soft landing, the Fed will expect inflation to cool in 2H24, more so if Friday's US nonfarm payrolls (NFP) hold below 200k for a second month. More importantly, the EU and the UK economies have exited their technical recession in 1Q24. Other global central banks have also become more aligned with the Fed's patience on rate cuts.

Potential movement in EUR on hawkish cut. EUR/USD to break above its 1.08-1.09 range if the European Central Bank (ECB) delivers a hawkish interest rate cut at its 6 June meeting. The ECB will not pre-commit to another cut after consumer price index (CPI) inflation increased to 2.6% y/y in May, higher than the 2.5% consensus and 2.4% in the previous month. Core inflation also increased to 2.9% in May vs the consensus for it to stay unchanged at April's 2.7%. Last week, ECB Chief Economist Philip Lane said the governing council will follow a data-dependent and meeting-by-meeting approach.

USD/CHF remaining below 0.92. USD/CHF is more likely to break below its two-month range of 0.90-0.92 than above it. Two events hijacked the only attempt to push above 0.92 on 1 May. First, Fed Chair Jerome Powell said on 1 May that the Fed did not see the next interest rate move as a hike. Second, Switzerland's CPI inflation release on 2 May rebounded from 1% y/y in March to 1.4% y/y in April, slightly below the Swiss National Bank's (SNB) policy rate of 1.4%. On 6 June, another surprise in CPI inflation should end the odds for a back-to-back rate hike at the SNB meeting on 20 June. Last week, SNB President Thomas Jordan warned of upside risks to the central bank's inflation forecast from the CHF's weakness and an R star (natural rate of interest) that could be higher than the present estimate of 0%.

USD/CAD to move in narrow band. USD/CAD has been confined to a 1.36-1.38 range since mid-April. The Bank of Canada (BOC) is widely expected to lower its overnight lending rate by 25 bps to 4.75% at its 5 June meeting. On 28 May, Finance Minister Chrystia Freeland fuelled rate cut bets with her comments that the federal budget presented in April would create the conditions for inflation to fall and the BOC to bring rates down. Last Friday, the Canadian economy also disappointed. Apart from growing by an annualised 1.7% q/q saar in 1Q24, slower than the 2.2% consensus, 4Q23's GDP growth was revised to 0.1% from its preliminary 1% estimate.

Rates: Steepening at play

Figure 4: US 2Y/10Y curve

Source: Bloomberg, DBS

Dropping UST yields. UST yields across tenors retreated last Friday on a mildly cooling data print. Personal Consumption Expenditure (PCE) and core PCE inflation, the preferred inflation measures of the Fed, stalled at 2.7% y/y and 2.8% in April respectively. On a sequential basis, core PCE moderated from 0.3% m/m to 0.2%. The relatively modest inflation was underpinned by slower personal income growth. This pointed to a more balanced labour market condition. Note that the employee-compensation saw more apparent easing compared to passive income such as interest and dividend income. Against this backdrop, personal spending growth eased from 0.8% to 0.2%. Meanwhile, the downward revision of 1Q GDP figure (from 1.6% q/q saar to 1.3%) and the PCE sub-component (from 3.1% to 2.8%) also attested the moderating consumption sentiment. Strategy-wise, steepening is still at play. Notably, the 2Y/10Y segment of the curve has yet to test the resistant level -30bps. Should the labour market data including NFP and job openings fall further as expected this week, the short-end yield could stay rich in the near-term.

Issuance of bonds to steepen CGB curve. Meanwhile, we see ongoing steepening of the Chinese Government Bonds (CGB) curve alongside the commencement of a CNY1tn ultra-long special sovereign bond issuance. We think there will be further stimulus from the central government down the road, given a relatively healthy debt level. Note that the central government's debt-to-GDP ratio was less than 25% last year, compared to over 70% of the G20 average. In fact, public spending by the central government went up by 10.5% y/y YTD in April, outpacing the 2.6% of local governments. A stronger growth momentum and stimulus could add upward pressure on long-end yields. Meanwhile, shorter-end yields may continue declining on expectations of reserve requirement ratio cuts. The weaker-than-expected NBS Manufacturing PMI data indicated a stronger need of monetary stimulus. Sustained recovery requires further monetary easing, and the modest CPI inflation leaves room for policy rate cuts. Overall, further steepening of the yield curve is likely.

Thematics: Global Pharmaceuticals – Surviving the patent cliff challenge

- Intensified competition from generic versions of patented drugs after patent expiry is a major risk for global pharma sector in the next three years
- Eight out of 13 global pharma players would have at least 30% of sales facing patent expiry
- One name has the highest exposure to patent expiry among peers, making its sales more vulnerable
- Another name faces relatively low exposure, at only 15% of its sales, with new drug approvals providing possible share price catalysts in the next 12 months

Global pharmaceutical players are facing risk of a patent cliff. When a drug's patent expires, generic versions of that drug enter the market at lower prices, capturing market share from the original drug manufacturer. This is known as a "patent cliff". Sales loss for the original drug maker can be huge, as illustrated in the case of Roche's drug Avastin. After its patent expired in 2019, Avastin's annual sales plunged 75% from USD7.1bn (2019) to USD1.8bn (2023). Research and development firm IQVIA predicts the total loss of sales in the US for patented drug makers from patent expiry will more than double from USD67bn (2018-23) to USD145bn (2024-28). Of the 13 giant players that make up 55% of the global pharmaceutical sector's market cap, eight of them would have 30% or more of their sales facing patent expiry in the US by 2026, a huge uncertainty to earnings. Based on our analysis, one name has the highest exposure, with 68% of its sales subject to this risk posed by six of its patented drugs, with numerous players having already announced plans to produce generic versions of all six.

One name faces low risk of patent expiry and visible catalysts ahead. Among the four players with less than 20% of its sales exposed to patent cliff risks, one name has the highest potential in terms of share price catalysts over the next 12 months, given the company has five new drugs in the pipeline for approval or new clinical data readouts vs the other three. This company may release positive clinical data, or get approval for the launch of its treatments, for diabetes, Alzheimer's disease, atopic dermatitis, and atherosclerotic cardiovascular disease. In China, a company with new capacity to produce key materials for a product to be launched by the aforementioned name will likely benefit from the launch in mid-2024.

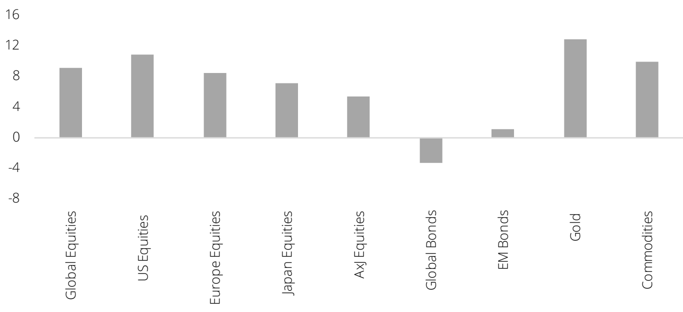
Figure 5: Portion of sales facing patent expiry in the US

Company	Stock code	% of sales from US (2023)	% of sales facing potential competition from generic versions in US (est)*			
			2023	2024	2025	2026
Eli Lilly	LLY US	64%	12%	12%	12%	15%
Novo Nordisk	NOVOB DC	59%	24%	24%	24%	24%
J&J (pharm rev**)	JNJ US	57%	23%	27%	35%	35%
Merck	MRK US	44%	5%	7%	7%	9%
AbbVie	ABBV US	77%	31%	31%	31%	31%
Novartis	NVS US	38%	10%	10%	39%	39%
Roche (pharm rev**)	ROG SW	48%	20%	30%	41%	46%
AstraZeneca	AZN LN	42%	5%	15%	31%	37%
Amgen	AMGN US	68%	3%	8%	30%	34%
Pfizer	PFE US	46%	6%	6%	9%	33%
Sanofi	SNY US	40%	10%	10%	10%	12%
Bristol Myers Squibb	BMS US	70%	2%	7%	11%	68%
Gilead	GILD US	71%	<8%	<8%	<8%	8%

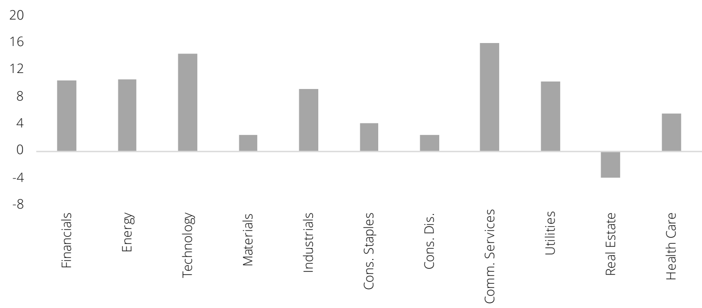
*Based on 2023 sales figures, representing sale of drugs that are facing patent expiry during 2024-2026 or with expired patents, divided by total sales
**For J&J and Roche, instead of total sales (which include sale of medical devices), total drug sales were used
Source: Company data, Google, Bloomberg, DBS

CIO Markets Watch

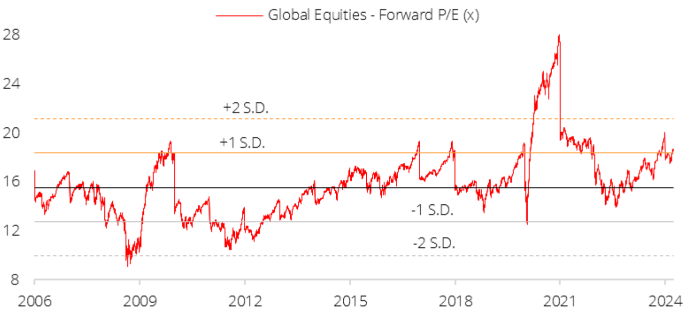
Global Cross Assets YTD Returns



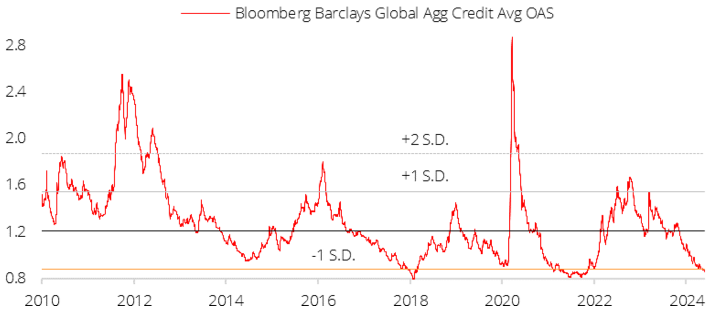
Global Sector YTD Returns



Global Equity Valuation



US Corporate Spreads



Source: Bloomberg, DBS

INDEX RETURNS

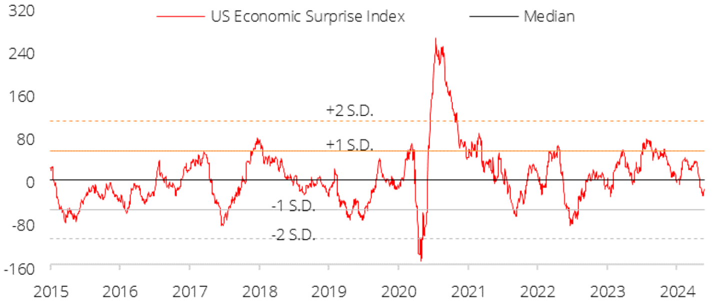
	1 week	MTD	QTD	YTD
Equities				
S&P 500	-0.5%	4.8%	0.4%	10.6%
NASDAQ	-1.1%	6.9%	2.2%	11.5%
Russell 2000	0.0%	4.9%	-2.6%	2.1%
Euro Stoxx 600	-0.5%	2.6%	1.1%	8.2%
Nikkei-225	-0.4%	0.2%	-4.7%	15.0%
MSCI WORLD	-0.5%	4.2%	0.2%	8.7%
MSCI ACWI	-0.8%	3.8%	0.3%	8.1%
MSCI Asia ex-Japan	-3.0%	1.3%	2.4%	4.5%
MSCI EM	-3.1%	0.3%	0.6%	2.5%
HSCEI	-3.2%	1.9%	10.0%	10.8%
SHCOMP	-0.1%	-0.6%	1.5%	3.8%
Hang Seng	-2.8%	1.8%	9.3%	6.1%
STI Index	0.6%	1.3%	3.5%	3.0%
Fixed Income				
Bloomberg Global Aggregate	-0.1%	1.3%	-1.2%	-3.3%
Bloomberg US Aggregate	0.0%	1.7%	-0.9%	-1.6%
Bloomberg US High Yield	0.0%	1.1%	0.1%	1.6%
Bloomberg Pan Eur. Agg.	-0.2%	0.0%	-1.2%	-1.5%
Bloomberg Pan Eur. High Yield	0.1%	1.0%	0.9%	2.8%
JPM EMBI Global	-0.1%	1.8%	-0.2%	1.2%
JPM EMBI Global Diversified	-0.1%	1.8%	-0.4%	1.1%

PRICES & SPREADS

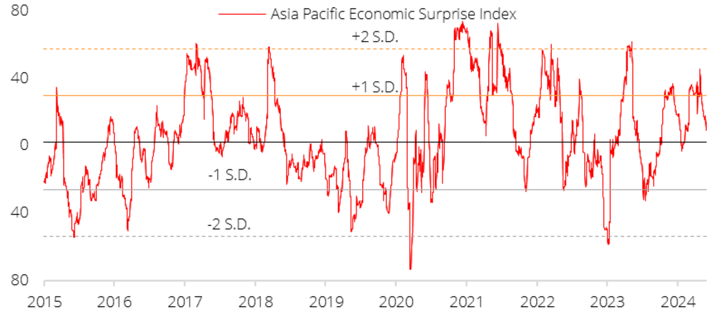
	Spot	1Q24	4Q23	3Q23
Rates				
Fed Funds Target	5.50	5.50	5.50	5.50
ECB Main Refinancing Rate	4.50	4.50	4.50	4.50
BOJ Policy Balance Rate	0.10	0.10	-0.10	-0.10
US Treasury 10Y	4.50	4.20	3.88	4.57
Japanese Govt. Bond 10Y	1.06	0.72	0.61	0.76
German Bunds 10Y	2.66	2.30	2.02	2.84
Spreads				
US Agg Corporate Spread	0.85	0.90	0.99	1.21
US Corporate HY Spread	3.08	2.99	3.23	3.94
Euro Agg Corporate Spread	1.08	1.14	1.37	1.54
EM USD Agg Spread	2.48	2.60	2.94	3.13
Currencies				
US Dollar Index (DXY)	104.7	104.5	101.3	106.2
EUR/USD	1.08	1.08	1.10	1.06
USD/JPY	157.3	151.4	141.0	149.4
USD/CNY	7.2	7.2	7.1	7.3
Commodities				
WTI Oil	77	83	72	91
London Metal Exchange (LMEX)	4363	3811	3762	3717
TR/CC CRB Commodity	290	290	264	285
Gold	2327	2230	2063	1849

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)	07-Jun	May	190k	175k
Initial Jobless Claims (US)	06-Jun	01-Jun	220k	219k
ECB Main Refinancing Rate (EU)	06-Jun	06-Jun	4.25%	4.50%
ISM Manufacturing (US)	03-Jun	May	49.6	49.2
ECB Deposit Facility Rate (EU)	06-Jun	06-Jun	3.75%	4.00%
Durable Goods Orders (US)	04-Jun	Apr	0.70%	0.70%
GDP SA q/q (EU)	07-Jun	1Q	0.30%	0.30%
HCOB Eurozone Manufacturing PMI (EU)	03-Jun	May	47.4	47.4

MACRO CALENDAR

	Date	Period	Survey	Prior
Asia				
Retail Sales y/y (SG)	05-Jun	Apr	2.20%	2.70%
Trade Balance (CN)	06-Jun	May	$69.80b	$72.35b
Exports y/y (CN)	06-Jun	May	5.10%	1.50%
Imports y/y (CN)	06-Jun	May	4.50%	8.40%
Purchasing Managers Index (SG)	03-Jun	May	--	50.5
Monetary Base y/y (JP)	03-Jun	May	--	2.10%
Caixin China PMI Services (CN)	04-Jun	May	52.5	52.5
Caixin China PMI Composite (CN)	04-Jun	May	--	52.8

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