# Fullerton Fund Management Investment Views – 2Q2019

We expect stabilisation of global growth and policy easing to provide further support for asset markets in the coming quarter. We had been of the view that markets were overly pessimistic on the global growth outlook at the start of the year. Strong gains in risk assets and the evolution of data and policy developments have since validated our stance. From here, we expect that risk assets, especially Asian equities and credits, should continue their outperformance.

## Executive Summary

- Risk assets, especially Asian equities and credits, are expected to continue their outperformance.
- A continued de-escalation of US-China trade tensions, which remains our base case, will contribute towards a further reduction of market uncertainty and reduced risk premia.
- Shift in central bank rhetoric, led primarily by the US Federal Reserve, has been one of the most important developments last quarter.
- The move towards a more patient approach to rate hikes, and an earlier than expected end to quantitative tightening, neutralises central bank balance sheet contraction as one of the key headwinds for asset markets this year. The global liquidity cycle is thus turning more supportive for risk assets.
- Earnings revisions are likely to be more supportive for Asian equities. We remain focused on disciplined stock selection, with an emphasis on growth stocks.
- Asian credit metrics have improved – credit profiles are also in a good position to weather any potential disappointments in earnings.

**Stabilising global growth and recovering liquidity**

Global growth is still on a slowing path; however, recent data suggest a stabilisation of activity, if not a potential upturn. In particular, the global trading and manufacturing cycles have been abnormally weak. Green shoots in activity are still tentative, but upticks in higher frequency Asian export data as well as Chinese economic data are notable.

Data in the US have also stabilised and expectations of an imminent recession have receded further, and rightly so in our view. The US labour market and consumer remain in a healthy state, and our expectation is still for trend-like rates of growth in the US. More importantly, a continued de-escalation of US-China trade tensions remains our base case. This will contribute towards a further reduction of market uncertainty and reduced risk premia.

One of the most important developments last quarter was a marked shift in central bank rhetoric, chiefly led by the US Federal Reserve. The shift towards a more patient approach to rate hikes, and an earlier than expected end to quantitative tightening, has important ramifications for the evolution of global liquidity. This neutralises central bank balance sheet contraction as one of the key headwinds for asset markets this year. The global liquidity cycle is thus turning more supportive for risk assets.

For additional information, please contact:

Fullerton Fund Management Company Ltd
3 Fraser Street #09-28 DUO Tower, Singapore 189352
T +65 6808 4688 E info@fullerton.com.sg

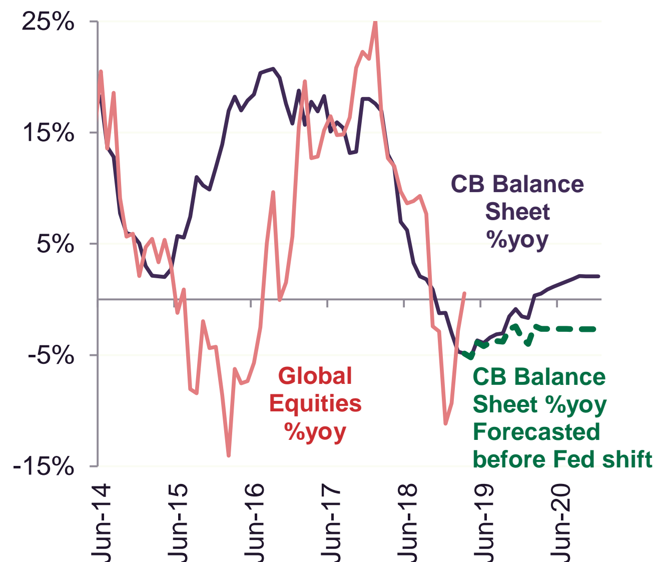
fullertonfund.com

Inflation remains a key risk. So far, inflationary pressure has remained muted and central bankers have leeway to be patient on rates. Monetary policy can respond to growth concerns or allay financial market volatility. We remain watchful for signs of greater inflationary pressure, especially in the US, as this would pose a serious challenge to the benign liquidity environment underpinning risk assets.

**Green shoots in data, such as Chinese economic sentiment**

Source: Fullerton, Bloomberg, Apr 2019

**Change in central bank rhetoric and balance sheet policy neutralises a key headwind for risk assets**




Source: Fullerton, Bloomberg, Apr 2019

**Favour Asian Assets**

We remain positive on risk assets, in particular Asian equities and Asian credits. Whilst year to date gains in Asian assets have been impressive, the environment remains supportive for further gains. In addition to positive fundamentals, we do not believe that positioning or sentiment is overly stretched.

Growth dynamics in Asia are likely to stabilise or improve. We observe green shoots in Asian activity and expect that Chinese policy stimulus will remain supportive for Chinese growth and the wider Asian region. For China, we had expected that both fiscal and liquidity easing would buffer growth. Our positive expectations have so far been validated by an uptick in the total social financing data and leading economic indicators of activity.

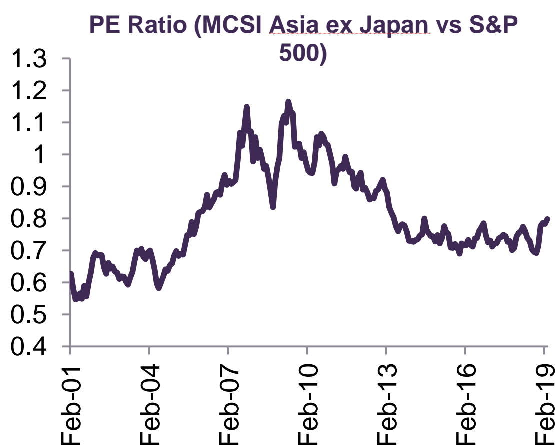
The global liquidity cycle also translates into a loosening of financial conditions for Asia. With a less hawkish Fed and earlier end to quantitative tightening, liquidity in Asia is likely to remain positive for financial assets. A stable USD environment also poses less pressure on Asian currencies, and central banks in the region have tilted monetary policies towards a more dovish stance. Coupled with fiscal policy easing, this creates a benign environment for Asian risk assets and supports portfolio flow to the region, and reinforces the momentum for asset allocation towards the region.

From a bottom-up perspective, we expect the worst of Asian equity downward earnings revisions to be past. Earnings revisions are likely to be more supportive for Asian equities. Moreover, despite the strong gains year to date, valuations remain at close to long term averages and trading at reasonable levels both on an outright and relative basis. Within Asian equities, we also observe that stock correlations have recently fallen, emphasising the value of stock picking. We remain focused on disciplined stock selection with an emphasis on growth stocks. We have overweight positions in India and Singapore, and in the Technology sector. We are also positive on Chinese A shares as we expect earnings to pick up toward the middle of the year, following the uptick in economic data and monetary easing. We believe that policymakers will favour a slow bull market as part of wider economic policymaking. The rise in margin balances bears scrutiny as excessive leverage is likely to be discouraged, but levels remain manageable so far.

Within the Asian credit space, we note that credit metrics have improved. Credit profiles are also in a good position to weather any potential disappointments in earnings. In line with the more benign global growth and liquidity environment, there has also been strong regional support for Asian credits. We are cognisant that the low level of US government bond yields poses duration risks.

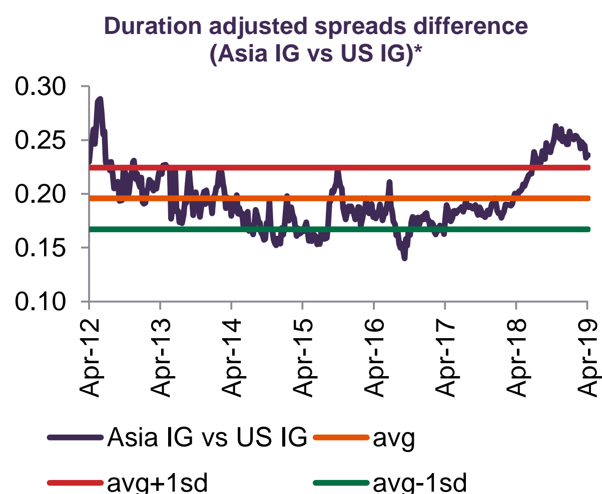
Given stabilisation in growth and the mature and very benign pricing of the Fed, we will actively manage overall duration risks in bond portfolios. Nevertheless, we note that absolute yield levels in Asian credits still remain attractive and provide a sufficient cushion against increases in US interest rates. Particularly on a relative value basis, Asian credits still offer attractive spreads versus US credits. Our emphasis on bottom-up credit selection remains, and we see opportunities in well-structured investment grade perpetuals and in the BBB space.

**Asian equity valuations still attractive versus US**




Source: Fullerton, Bloomberg, Apr 2019

**Asian credit valuations are also attractive versus US**




Source: Fullerton, Bloomberg, Apr 2019.
*JACI Investment Grade Index versus Bloomberg Barclays US Aggregate Credit Index

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