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Q3 2024 Market Outlook

Positioning for lower rates

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Q2 2024: Market Recap

Risk assets continue to rise in a benign macro environment

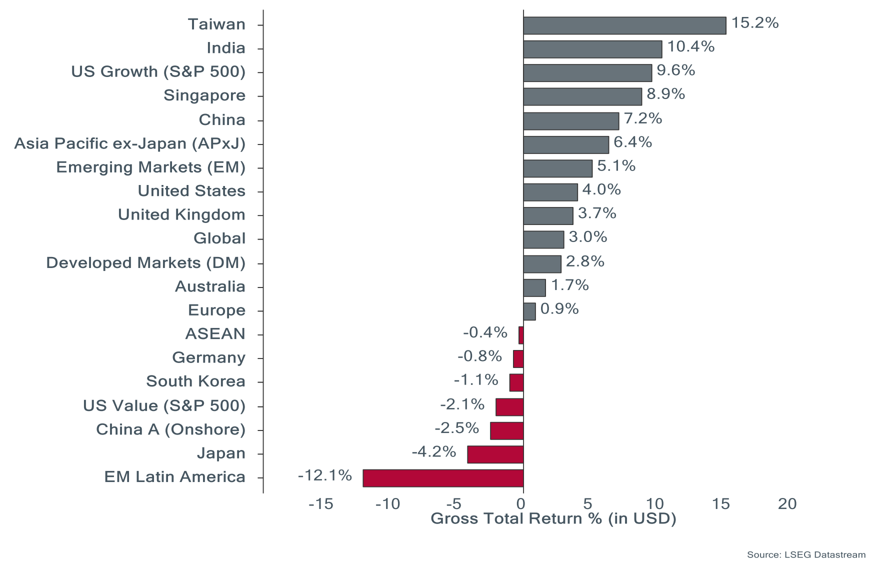
Equities

In the second quarter of 2024, the global equity markets rose, buoyed by strong corporate earnings, continued AI interest, and still decent economic growth momentum. US CPI inflation data showed some signs of easing, following a reflationary first quarter. US equities rose by 4.0%, with the S&P 500 and Nasdaq hitting record closing highs. Emerging Markets (EM) surged by 5.1%, outperforming the Developed Markets (DM) which gained 2.8%. Within EM, Taiwan rallied 15.2%, benefitting from continued AI optimism and investor interest while Latin America (-12.1%) disappointed, weighed by Brazil and Mexico. The ASEAN markets (-0.4%) lagged the broader Asia Pacific ex-Japan (6.4%) and EM markets, dragged by underperformances from Indonesia and the Philippines.

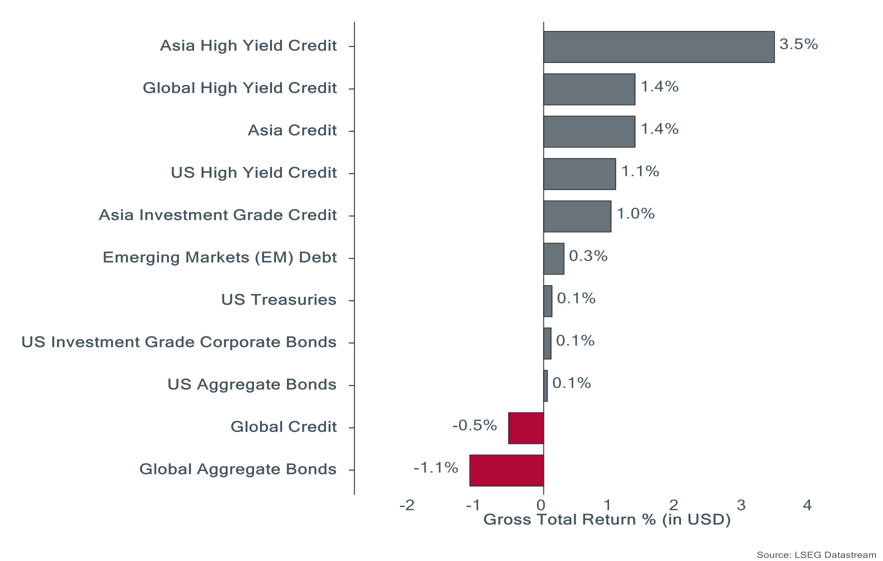
Fixed Income

During the quarter, yields on US Treasuries drifted moderately higher, with the 10-year yield up by 16 bps to end June with 4.36%. On the monetary policy front, the Bank of Canada and the European Central Bank became the first G7 central banks to cut rates. Global aggregate bonds, as proxied by the Bloomberg Global Aggregate Index, declined 1.1%, while US Treasuries, as represented by the Bloomberg US Treasury Index, returned 0.1%, amongst the best sovereign performers. In US credits, US investment grade corporate bonds (ICE BofA US Corporate Index) and US high yield bonds (ICE BofA US High Yield Index) gained 0.1% and 1.1% respectively. The JP Morgan Asia Credit Index (JACI), which proxies the Asia credit market, rose 1.4% on the back of positive gains from both investment grade and high yield issuers.

Global Equities: Q2 2024 Performance



Global Fixed Income: Q2 2024 Performance



Data source: Eastspring Investments; MSCI; LSEG Datastream. Equity returns are referenced by the respective MSCI market indices quoted in USD (gross total returns). Exceptions are the "US Growth (S&P 500) and US Value (S&P 500), which are represented by the S&P 500 Growth (TR) Index and S&P 500 Value (TR) Index, respectively. "DM Equities" is represented by the MSCI World Index. The fixed income markets are represented as follows: "Asia High Yield Credit": J.P. Morgan Asia Credit Non-Investment Grade Index, "Global High Yield Credit": ICE BofA Global High Yield Index, "Asia Credit": J.P. Morgan Asia Credit Index, "US High Yield Credit": ICE BofA US High Yield Constrained Index, "Asia Investment Grade Credit": J.P. Morgan Asia Credit Investment Grade Index, "Emerging Markets (EM) Debt": J.P. Morgan EMBI Global Diversified Index, "US Treasuries": ICE BofA US Treasury Index, "US Investment Grade Corporate Bonds": ICE BofA US Corporate Index, "US Aggregate Bonds": Bloomberg US Aggregate Index, "Global Credit": ICE BofA Global Credit Index, and "Global Aggregate Bonds": Bloomberg Global Aggregate Index. ASEAN is made up of Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand and Vietnam. G7 is made up of United States, United Kingdom, Canada, France, Germany, Italy and Japan.

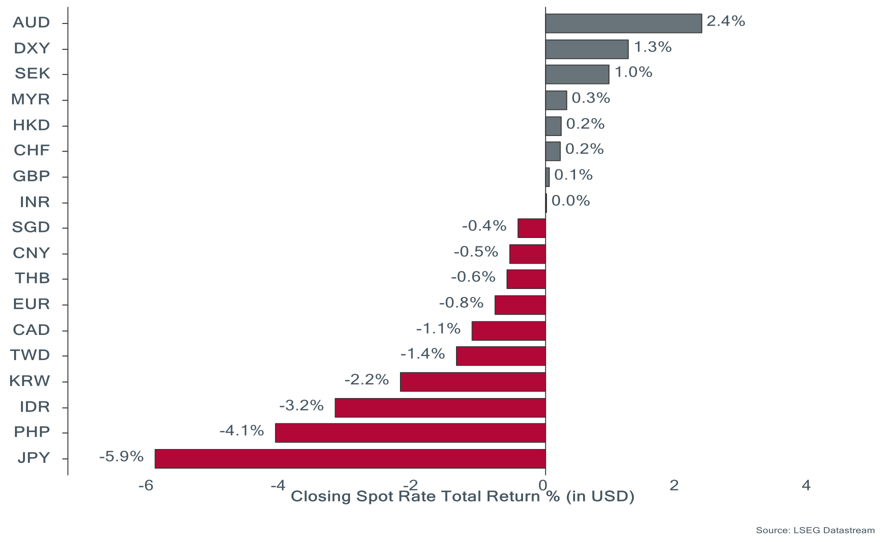
Currencies

Policy divergence, and relatively higher US yields, amongst other factors, supported the USD during the second quarter. The Australian dollar (AUD) appreciated significantly against the US dollar due in part to divergent monetary policies, with the Reserve Bank of Australia (RBA) adopting a less dovish stance compared to other major central banks. The Japanese yen, a big laggard amongst the major DM currencies, continued to weaken against the USD amid still wide interest rate differentials. The Brazilan real continues to rank amongst the worst performers, partly owing to the uncertain outlook for the country's fiscal situation.

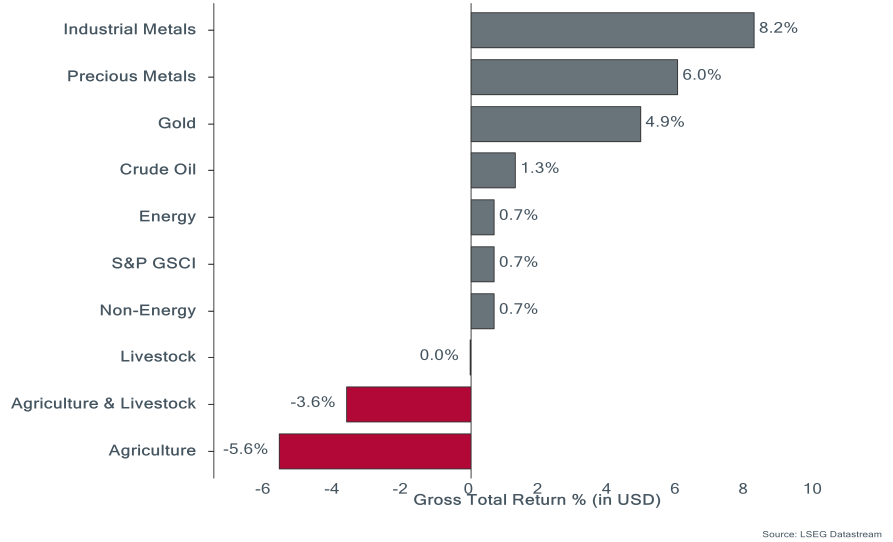
Commodities

During the second quarter, the S&P GSCI experienced a modest increase of 0.7%. The top-performing sectors were industrial metals and precious metals, which saw gains of 8.2% and 6.0%, respectively. The industrial metals sector was bolstered primarily by a strong performance in zinc. Conversely, the agriculture sector was amongst the weakest performers, with a return of -5.6%.

Currencies (vs. USD): Q2 2024 Performance



Commodities: Q2 2024 Performance



Source: LSEG Datastream; S&P Global. For the "Currencies (vs. USD)" chart, with the exception of the U.S. Dollar Index (DXY), the returns for the other respective currencies (against the USD) are based on the closing spot rates calculated by Refinitiv. For the "Commodities" chart, please note the following. Crude Oil: S&P GSCI Crude Oil Index, Energy: S&P GSCI Energy Index, Livestock: S&P GSCI Livestock Index, Gold: S&P GSCI Gold Index, Precious Metals: S&P GSCI Precious Metals Index, Agriculture & Livestock: S&P GSCI Agriculture and Livestock Index, Non-Energy: S&P GSCI Non-Energy Index, Agriculture: S&P GSCI Agriculture Index, and Industrial Metals: S&P GSCI Industrial Metals Index.

Macro Outlook

Moderating global growth and disinflationary forces pave the way for a Fed pivot

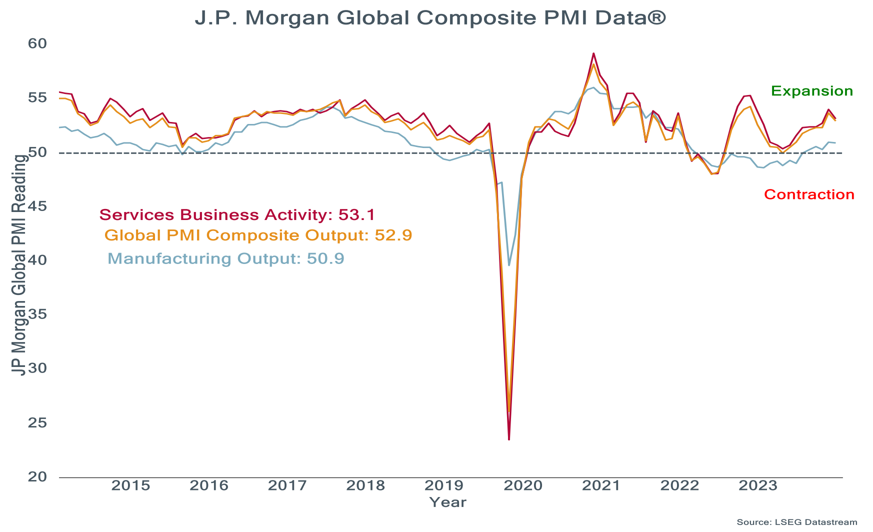
Growth

The global economy has been expanding steadily for the past eight months, as shown by the J.P. Morgan Global Composite PMI Output Index. However, this momentum showed signs of easing in June where the PMI for new export orders, which proxies export demand, fell into the contractionary territory, below 50. Economic data also disappointed (relative to expectations) across the US and Europe, reflecting the lagged effects of higher rates and reduced fiscal tailwinds. Perversely, weakening economic data continues to support the "bad news is good news" narrative, as market participants hope that the Fed will eventually pivot to a rate cut. For now, the US continues to support global demand, maintaining its global economic leadership position while China remains challenged by a deflationary backdrop and lack of meaningful stimulus.

Inflation

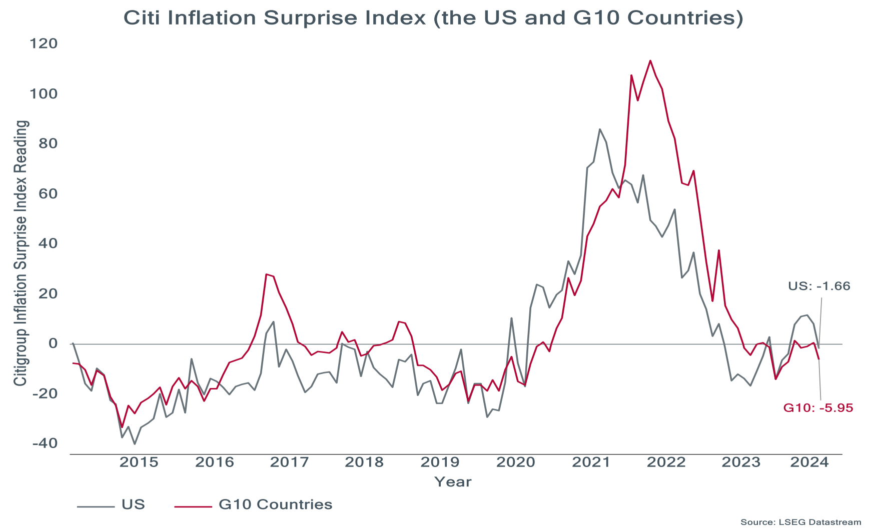
Inflation in the US showed signs of easing in the second quarter. Both headline and core Consumer Price Index (CPI) readings softened, leading to a decline in the Citi Inflation Surprise Index. This contrasts with the reflationary trend seen in the first quarter. Shelter inflation, which has a significant weighting in the CPI basket, increased by a modest +0.2% monthly, contrasting with the earlier consecutive +0.4% monthly increases. In June, the US labour market showed signs of normalising. The three-month average for payroll gains decreased after significant revisions, and average hourly earnings—a crucial gauge of wage inflation—also moderated. A weakening labour market and decelerating consumer spending in the US reaffirm our belief that disinflationary forces remain in play for the rest of 2024, paving the way for the Fed to eventually pivot.

Global Purchasing Managers' Index (PMI)



Source: J.P. Morgan; LSEG Datastream. 14 June 2024

Citi Inflation Surprise Index (US, G10)



Source: LSEG Datastream; Citigroup. 28 June 2024.

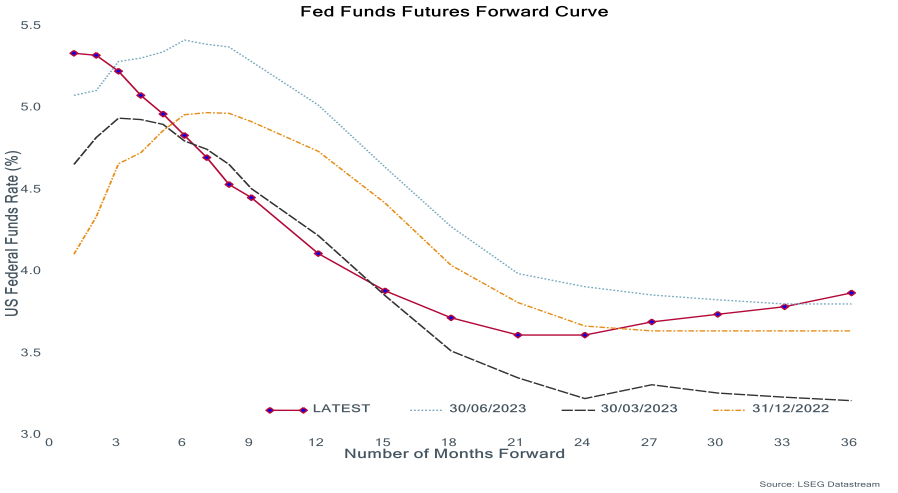
Monetary Policy

Amid slowing growth and easing inflation, central banks in developed countries are signaling potential rate cuts. The Swiss National Bank has already implemented two cuts in 2024, while the Bank of Canada and the European Central Bank recently delivered a rate cut each in June. Meanwhile, given the relatively resilient US economy, the Fed has kept its policy rate steady, at least for the time being. Compared to early 2024, current market expectations for US rate cuts indicate a more gradual easing path. Initially, concerns about persistent inflation led the Fed to be cautious, causing investors to reduce expectations of aggressive rate cuts. However, softer US CPI data in the second quarter and potential softening of the labour market (which could ease wage inflation), may now prompt the Fed to start cutting rates soon. The Fed seeks to avoid being too slow to cut rates in order to maintain policy credibility. Otherwise, it risks inadequate rate cuts during a meaningful growth slowdown, potentially leading to a recession.

Looking Ahead

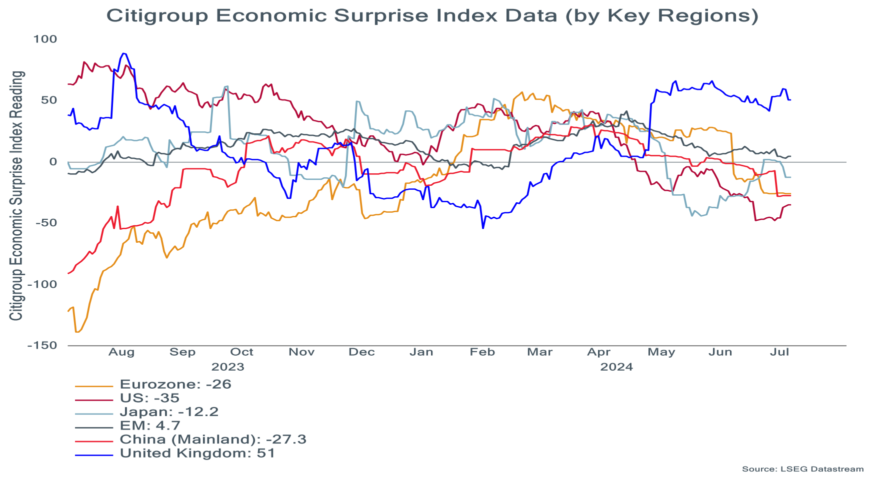
In the second half of 2024, we anticipate continued moderating inflation, decelerating (but still positive) growth, and easier monetary policy overall. US consumer spending momentum, a key driver of global growth/demand will be hampered by a combination of decelerating wage growth, fading pandemic excess savings, and tighter bank lending standards, amongst other key factors. US consumers can still support global demand in the near term as long as US wage inflation continues to outpace US headline inflation. Although we believe that the risk of either a "soft landing" or a recession is being better balanced, the data-dependent Fed has room to cut interest rates to mitigate any shocks if a meaningful growth slowdown occurs. In our view, the continued disinflationary backdrop will allow the Fed to cut rates at least once or twice later this year.

U.S. Federal Funds Futures Forward Curve



Source: LSEG Datastream. 19 July 2024.

Citigroup Economic Surprise Index



Source: LSEG Datastream; Citigroup 22 July 2024.

Assessment of Key Risks – Global Elections in Focus

Risk Areas of Concern	Likelihood	Magnitude of Negative Impact
Global elections slated for 2024, and notably the US presidential election cycle will feature prominently in the headlines and potentially introduce heightened volatility over the next 3-to-12-month horizon.	High	Medium
Limited impact (and untimely implementation) of meaningful stimulus measures from China pose a risk that China's disinflationary environment will continue to hamper global growth. The absence of any meaningful stimulus announced in the 3rd Plenum exacerbates this notion.	Medium	Medium
Developed markets recession risk remains (e.g., US, Europe) as the impact of the concerted global central bank monetary tightening is felt. For example, the Fed's action or rather its timing to cut rates, is crucial as the it wants to avoid being "behind the curve".	Medium	High
Inflation and growth persisting for longer remains a possibility, though the recent softening of US CPI data and forward-looking US labour market indicators seemingly suggest the disinflationary trend should remain intact for 2024. To this end, US labour market conditions and the US wages trajectory continue to be key watchpoints.	Low	High
Geopolitical tensions (e.g., the Russia–Ukraine, Iran–Israel and Gaza-Israel conflicts) still loom in the background and can have significant impacts on investor sentiment, though we generally view these as transitory in nature. A further broadening of Middle East tensions, for example, may cause further energy-driven inflation and potentially increase global trade costs in the event of supply disruptions.	Low	Medium

Datesource: Eastspring Investments (Singapore) Limited, July 2024. The information provided here is subject to change at Eastspring's discretion without prior notice.

Asset Allocation Views

Runway for risk assets remains intact (for now)

Over the shorter-term tactical horizon, gradually moderating inflation and benign (yet still positive) growth can continue to support risk assets, with US equities being our favoured equity position, as it continues to benefit from relatively strong earnings. In our view, US consumer spending, which is a key driver of US and global growth will eventually slow more meaningfully as tailwinds like excess savings from the pandemic, wage income and consumer credit growth fade. To this end, the team is prepared to be more defensive on equities over the 12-month horizon.

In the second half of 2024, we expect moderating inflation, decelerating growth and an easier (or less restrictive) monetary policy. With regard to bond yields, we believe that disinflationary forces will ultimately prevail and keep yields on a general downward trend. Such a backdrop will be supportive of government bonds, namely US Treasuries. As such, and when considering the attractive current yield levels, we have begun entering into long duration government bond positions in our multi asset portfolios. We will look to scale into a larger position if and when there is more compelling evidence of a further slowing in the US economy.

Asset Allocation Views

● Underweight ● Neutral ● Overweight

↑↓ Upgrade/downgrade in view from previous quarter – No change

Asset	3m		12m		Rationale
Global Equities	● (Overweight)	–	● (Underweight)	–	We recognise that equity valuations are currently elevated, making the asset class susceptible to potential sell-offs in response to any negative surprises, or declining corporate profits. With global economic activities expanding at the margin and the markets likely to reward any economic weakness (as this allows the Fed to cut rates), we remain tactically constructive over the 3m horizon. There is still scope for further upside as money from money market funds finds its way into equities. Over the 12m horizon, US and global growth momentum will slow more meaningfully as excess savings from the pandemic fade and the labour market softens. This would weigh on equity valuations, in line with late cycle dynamics.
Government Bonds	● (Overweight)	↑	● (Overweight)	–	As the broader disinflationary trend continues, we see value in positioning for the decelerating global growth outcome now. As such, we have begun entering into long government bond positions in our multi asset portfolios (where applicable), mostly via US Treasuries. In line with our more risk-off, defensive positioning over the 12m horizon, we believe that US duration stands to benefit over the medium-term given slowing growth and disinflationary trends, in addition to the typical “flight-to-safety” responses.
US Inv. Grade Credit	● (Underweight)	–	● (Neutral)	–	US investment grade credit spreads remain tight amid market expectations of a potential “soft landing” scenario, while being supported by decent corporate fundamentals. To this end, over the 3m horizon, the short-term overweights in risk assets (e.g., global equities, US high yield bonds) across our multi asset portfolios are typically being funded out of holdings in US investment grade bonds. Over the 12m horizon, we maintain a neutral stance on US investment grade bonds. Compared to US high yield bonds, investment grade bonds can benefit from potential price appreciation amid declining US yields.
Cash	● (Neutral)	–	● (Overweight)	–	Our cash positioning remains neutral over the short-term given our “risk-on” tactical positioning. Cash remains a constructive position over the 12m horizon given our defensive, risk-off outlook.

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Asset Allocation (cont.)

Asset Allocation Views

Global Equities	3m		12m		Rationale
US	🟢	–	🔴	–	We continue to maintain a constructive outlook on US equities (constituting approximately 65% of MSCI ACWI's total market cap) over the 3m horizon; the US market also continues to deliver strong earnings and sales growth relative to other global markets, alongside market exuberance over the AI story. Over the next 12 months, we expect global growth momentum to slow meaningfully, as the cumulative impact of previous rate hikes take hold, which will eventually lead to an overall decline in equity valuations. Therefore, we maintain an underweight stance on US equities over the 12m horizon.
Europe	🔴	↓	🔴	–	We downgraded Europe to slightly below neutral over the tactical horizon as the region's fundamental economic indicators deteriorated. While European equities remain undervalued compared to the US, the potential for relative outperformance depends on global growth significantly accelerating given Europe's export-dependent economy. As such over the 12m horizon, Europe equities are expected to underperform due to its high sensitivity to the global business cycle.
Emerging Markets (EM)	⚪	↑	⚪	–	Economic data for the EMs are beating expectations compared to other key regions (e.g., U.S., Europe). Hence, we have updated its tactical outlook to a more neutral stance, from a previously bearish stance. Over the 12m horizon, due to the asynchronisation of the business cycle, EM earnings growth has the potential to outpace that of the developed markets (DM) economies, hence our more neutral stance.
Asia Pacific ex-Japan	⚪	–	⚪	–	Given our tactically neutral on EM equities, we are also tactically neutral on APxJ equities as Asia (China, South Korea, Taiwan, etc.) accounts for a sizeable portion of EM. Over the 12m horizon, Asian equities are likely to trade more range-bound, relative to developed market equities. Furthermore, Asia's starting valuations are relatively more attractive than the US'.

Government Bonds	3m		12m		Rationale
US	🟢	↑	🟢	–	Forward-looking indicators of a worsening US labour market imply that growth will continue to deteriorate while wage inflation moderates. We believe in building long US government bond positions in our multi asset portfolios now, where applicable. Over the 12m horizon, we expect US yields to track downwards overall in line with our expectation of a disinflationary environment.
Europe	⚪	–	🟢	–	We maintain our neutral short-term stance. We believe that the ECB rate cut in June was more of a moderation of a restrictive policy, rather than an outright dovish pivot. Over the 12m horizon, a combination of relatively weak economic growth and the lagged effects of rate hikes make Europe government bonds relatively attractive in a potential risk-off market scenario.
Singapore	⚪	–	🟢	–	While the Monetary Authority of Singapore (MAS) is unlikely to ease in the near term, we see the possibility of easing in 2025 especially if manufacturing sector activity continues to slow and the disinflation trend stays intact. As such, we are constructive on Singapore Government Securities (SGS) bonds over the longer term.

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Asset Allocation (cont.)

Asset Allocation Views

Credit	3m		12m		Rationale
US High Yield	🟢	–	🔴	–	US high yield remains attractive at this stage, exhibiting stronger fundamentals than in previous cycles. While spreads are deemed to be expensive, the approximately 8% yield-to-worst remains attractive from an overall total return perspective. Consistent with our view on global equities, we remain tactically constructive on US high yield (versus US investment grade bonds) at this stage, but is cognisant of the risks of a slowing economy pushing spreads wider into H2 2024.
US Investment Grade	🔴	–	⚪	–	Given the current extremely tight US investment grade spreads, we maintain a less constructive stance on the asset class over the 3m horizon. The view becomes more neutral over the 12m horizon, given our defensive preference for government bonds (or higher quality interest rate sensitive bonds that can benefit from falling yields) and cash.
Emerging Markets	⚪	↓	⚪	–	We currently hold a tactical neutral outlook on Emerging Markets (EM) USD bonds given the limited scope for upside from current spread levels. Over the 12m horizon, we remain neutral as higher quality assets (e.g., EM sovereign bonds) may outperform riskier assets along the credit spectrum. That said, DM bonds should still outperform EM bonds in the late cycle.
Asian Credit	🟢	–	⚪	–	We are constructive on Asian credits over the short term as slower, but steady global growth conditions should help stabilise Asian credit fundamentals. We remain constructive on Asia's growth prospects as the region continues to establish an increasingly important position as the world's manufacturing and trade hub. Over the 12m horizon, bond yields in Asia may be more stable as the region's inflation is relatively more subdued, while a strong local investor base can support the asset class.

FX	3m		12m		Rationale
USD	🟢	–	🟢	–	Strong relative US growth and high real rates may support the USD in the near-term, but we are cognisant that other catalysts are needed to support the upward momentum. Over the 12m horizon, the USD (relative to other key currencies), stands to benefit in a slowing global growth environment, given its counter-cyclical nature.
EUR	🔴	–	🔴	↓	Over the 3m horizon, we maintain a greater preference for the USD (vs. the EUR), given the above-mentioned rationale on the USD. Over the 12m horizon, the EUR, given its pro-cyclical characteristic, will likely underperform the USD in a growth slow-down, late cycle scenario.
SGD	⚪	↑	⚪	–	In the near term, the SGD should remain relatively range bound at current levels as the Monetary Authority of Singapore would likely keep its FX policy status quo for now. We remain neutral over the longer-term as well, as the counter-cyclical USD would likely outperform all major currencies in a decelerating growth environment, consistent with late cycle dynamics.

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Copper: The red metal is poised to rise

Copper is one of the world's top traded commodities, with its popularity coming from its versatility and extensive use in a range of industries. The top five global copper producers are Chile, Peru, Democratic Republic of Congo, China, and the United States. These five accounted for approximately 60% of the global production. Chile has the lion's share at 24%[1]. On the other hand, China accounts for 50% of the global copper demand[2]. China's economic conditions thus greatly impact copper prices.

Copper prices are typically determined by demand and supply considerations, financing and production costs, and climate and geopolitical conditions. Prices have been volatile over the past year on the back of weaker demand from China, which is experiencing a structural change. China's property sector, which once contributed to the bulk of China's copper demand, has now shrunk to approximately 5%. Future copper demand will likely emanate from the green energy transition, with some broker forecasts indicating that green energy will drive ~47% of all copper demand for the rest of the decade.

Green energy aside, high copper demand will come from the rapid growth in Artificial Intelligence (AI). Copper, a key raw material, is used in the construction of datacentres, which AI relies on. According to UBS research, copper demand from datacentres in 2023 was ~1.5% of global demand. Due to copper's high electrical conductivity, it may also be used in the production of semiconductors.

[1] https://www.statista.com/statistics/605533/distribution-of-global-copper-mine-production-by-select-country/

[2] https://www.statista.com/statistics/693466/distribution-of-global-refined-copper-consumption-by-region/

Despite weaker demand from China, copper prices have surged since February of this year as supply disruptions this year created a supply shortage. This supply issue is unlikely to be alleviated in the short run, as underinvestment in the industry in recent years has made it difficult to discover and develop new mines. In fact, it can take up to 15 years to discover and develop a new mine. As a result, global copper inventories remain at multi-year lows, suggesting that the supply issue is unlikely to go away anytime soon.

Source: LSEG Datastream, as of 23 July 2024.

Against this backdrop of growing copper demand, ongoing supply shortage, improving prospects in China and eventual rate cuts, some analysts are bullish on this commodity. Citibank, for example, is of the view that copper prices will hit USD12,000 per tonne (27% upside) over the next 12-18 months. There are a few means to gain exposure to the red metal; invest directly in copper or in copper miners. Copper miners is a higher beta play versus copper as more factors impact a copper miner's share price. The following chart compares the historical total return performances of the London Metal Exchange (LME)-Copper Grade A, based on price in USD per metric tonne, and the Global X Copper Miners ETF (Ticker: COPX).

A diversified exposure to a range of companies that derive the bulk of their revenues from copper mining is less risky than owning single copper mining stocks. The fundamental outlook for copper remains compelling and any pullbacks in price are likely to attract strategic buying (in both copper and copper miners).

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