SEP 2024

# Investment Navigator
## Asia Edition

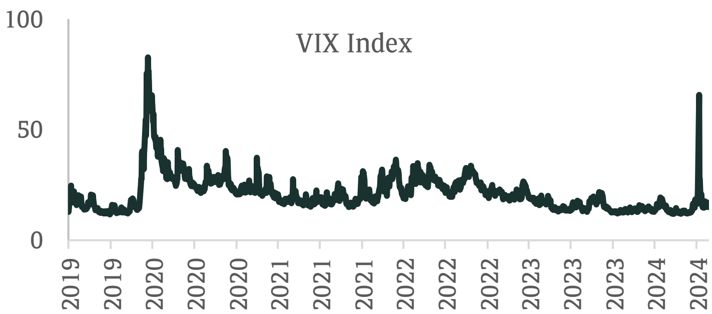
# How to ride on the exacerbated volatility?

## Global markets suffered from a "double whammy" in early August

Global markets saw heavy sell-offs in early August 2024 due to (1) unwinding of carry trades following a hawkish Bank of Japan (BoJ) and (2) growing recession risk as the Sahm rule is triggered. Volatility was heightened to 65 on 5 August 2024, a level only recently seen during Covid. After the "Black Monday", equity markets rebounded and volatility has normalised as yen stabilised after the BoJ said they will not hike rate when markets are unstable.

We believe around 70% of carry trades have been unwound and hence, the worst of positioning unwinding is likely behind us.

**VOLATILITY JUMPED TO 2020 COVID HIGHS ON "BLACK MONDAY"**




*Source: Bloomberg, BNP Paribas (WM), as of 3 September 2024. Past performance is not indicative of current or future performance.*

### What is Sahm rule?

It is a recession indicator which states that when the 3-month moving average of the national unemployment rate is 0.5 ppt above its low over the prior 12 months, it signals the beginning of a recession.

## US soft-landing remains our base case scenario

On the US, economic data in recent weeks indicates a soft-landing scenario, instead of any imminent recession. For example, ISM Services rose to above 50, the Senior Loan Offices Survey shows improvement in US credit demand, mortgage applications increased, US retail sales beat consensus and US consumer confidence reached a 6-month high.

**Moreover, we have never seen a recession when US real wage growth remains positive.** The Atlanta Fed GDPNow (a real GDP growth forecast for 3Q) is currently at 2.0%.

**Sahm rule if applied to US initial jobless claims is not signalling a recession.** Claudia Sahm, a former Fed economist who created the Sahm rule, also said the US is not in a recession.

Prashant BHAYANI
Chief Investment Officer
Asia
BNP Paribas
Wealth Management

Grace TAM
Chief Investment Adviser
Hong Kong
BNP Paribas
Wealth Management

Dannel LOW
Investment Adviser
Asia
BNP Paribas
Wealth Management

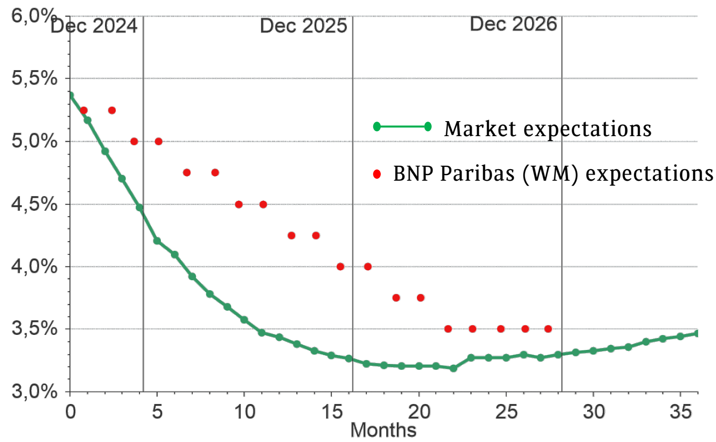

## Market expects aggressive cuts in the coming months. Is it overdone?

With inflation slowing and labour market softening, rate cut in September 2024 is almost a done deal. The question is whether it is a 25bp or 50bp cut.

The futures market is currently pricing in a 100bp Fed rate cuts by end-2024. The pace and depth of expected cuts is almost equivalent to a recession scenario. We believe this looks overdone.

> We expect a 25bp cut in September and another 25bp cut in December this year if economic data continues to point to a soft-landing scenario.

**WE EXPECT 2 FED RATE CUTS BY END-2024, LESS THAN MARKET EXPECTATIONS OF 4 CUTS**




*Source: Datastream, BNP Paribas (WM), as of 3 September 2024.*

Hence, we expect yields to rebound when we see more resilient US data in the coming months. **Our 3-month target for US Treasury 10-year yield is 4.25% and 12-month target at 4%.**

**In the short-term, we tactically move our positive stance on US government bonds to neutral, although we remain constructive on the asset class strategically in the medium term.** We intend to upgrade the asset class to positive again with better entry point if 10-year yields bounce back above 4%. **We continue to be positive on short duration US investment grade bonds** as yields remain attractive and credit spreads could tighten further as economic growth and investor demand persist.

## Accumulate bonds when yields rebound

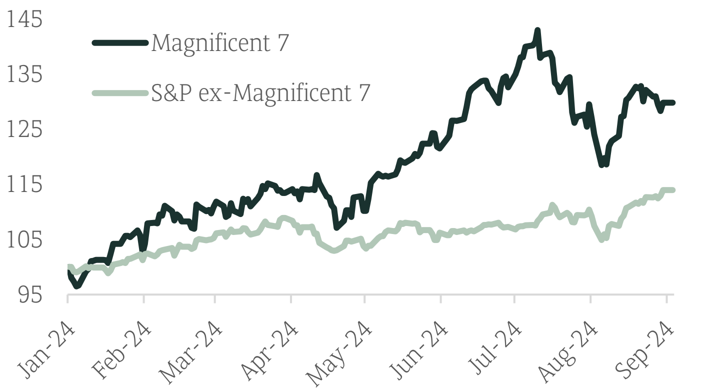
Bonds tend to perform well in a rate cut cycle, and they can also serve as a hedge to the recession risks. The bond rally in August 2024 is a remainder of how sensitive the bond market is over fears of a recession.

Furthermore, historical data shows that yields were down 3 months and 6 months after the first rate cut in both soft-landing and hard-landing scenarios.

### Laggards are catching up

One interesting fact to note about the strong equity rally after the "Black Monday" is market breadth has been broadening. Magnificent 7 stocks saw a strong rebound but only recovered around half of their losses during the crash, while S&P ex-Magnificent 7 stocks reached fresh record highs in anticipation of a rate cut environment.

### NON-MAGNIFICENT 7 US STOCKS HAVE BEEN CATCHING UP




*Source: Bloomberg, BNP Paribas (WM), as of 3 September 2024. Past performance is not indicative of current or future performance.*

Apart from the US non-tech sectors, we also have been seeing rebound in laggards such as UK and Eurozone equities. We still believe there is plenty of room for the laggards to catch up. Investors should diversify their exposure to sectors such as healthcare and financials.

## AI: Don't miss the forest for the trees

Despite the recent losing momentum in the AI-related stocks, we do not think it is a "game over" for the AI investment theme. We believe we are still at the early stage of the AI revolution. Hence, corrections are buying opportunities.

Furthermore, Nvidia and semiconductor stocks are only the tip of the iceberg, and there are still plenty of opportunities in other areas such as software, data centre, hardware and cybersecurity. It is also widely believed that AI is likely to drive operating margin expansion for most of the industries, consumer services, financials, media and entertainment and healthcare to just name a few.

**KEY RISKS**

- US economy deteriorates quickly and raises the recession probability.
- Uncertainty over US election outcome whether there would be inflationary policies that deters the Fed from continuing rate cuts.

## Strategies on equities, bonds, currencies & commodities

**EQUITIES:** We remain positive on global equities in the medium term, as a rate cut environment and improving liquidity should be supportive to the asset class if the soft-landing scenario remains intact. Lingering fear over recession, the upcoming US elections and seasonality headwinds may see rising market volatility in the autumn period. Nevertheless, any short-term weaknesses would be buying opportunities.

**BONDS:** We continue to like investment grade bonds. Any rebound in yields are good opportunities to accumulate bond exposure to lock in the attractive yields ahead of the Fed rate cut cycle. Bonds also act as a hedge to any hard-landing fears.

**CURRENCIES & COMMODITIES:** We expect the USD to consolidate in the near term after the recent sharp move, which provides good entry points for non-USD currencies, as we still see USD weakness in the medium term. We continue to favour gold and copper. Investors should buy on dips.

**MONETISE VOLATILITY:** Investors can take advantage of rising volatility to get asset class exposure via structured solutions that potentially capture the upside while managing the downside risk.

# Overview of our CIO Asset Allocation for September 2024

| | Views Current | Views Prior | Constituents | We like | Comments |
|---|---|---|---|---|---|
| EQUITIES | + | + | Markets | UK, Japan, Eurozone, Brazil, China, South Korea, Singapore & Indonesia | ■ We maintain our **positive view on non-US equities**.<br>■ We are **positive on developed markets Small Caps**. |
| | | | Sectors | Healthcare, Materials, Industrials | ■ We also like EU financials & technology. |
| | | | Styles/ Themes | Megatrend themes | ■ Circular economy, electrification, security, deep value & income themes. |
| BONDS | = | = | Govies | US inflation-indexed bonds | ■ We **tactically move US Treasuries to neutral**<br>■ Our 12-month target for the US 10-year Treasury yield is revised down to **4.0%**. |
| | + | + | Segments | Investment grade, Emerging markets (EM) bonds (USD + local currency) | ■ We remain **positive on US** (short maturity) **and Euro** (up to 10-year maturity) **investment grade corporate bonds**. |
| CASH | - | - | | | |
| COMMO-DITIES | + | + | | Gold<br>Base metals | ■ **Gold - positive**: target of $2600/oz in 2025<br>■ **Oil - neutral**: Brent's target range $75-85.<br>■ **Base metals – positive** |
| FOREX | | | USDJPY | | ■ **USDJPY** 3- and 12-month targets at **145 and 140 respectively**. |
| ALTER-NATIVE | + | + | | Hedge funds (event driven, long-short equities, relative value) | ■ **Neutral on global macro** |

Note: + Positve / = Neutral / - Negative

## GDP & CPI Forecasts

| | | GDP (YoY%) | | | CPI (YoY%) | | |
|---|---|---|---|---|---|---|---|
| | | 2023 | 2024f | 2025f | 2023 | 2024f | 2025f |
| Developed | US | 2.5 | 2.5 | 1.9 | 4.1 | 2.9 | 2.3 |
| | Japan | 1.8 | -0.4 | 0.7 | 3.3 | 2.7 | 2.6 |
| | Eurozone | 0.6 | 0.9 | 1.6 | 5.4 | 2.3 | 2.0 |
| | UK | 0.1 | 1.0 | 1.3 | 7.3 | 2.6 | 2.2 |
| North Asia | China | 5.2 | 5.2 | 4.3 | 0.2 | -0.1 | 1.2 |
| | Hong Kong* | 3.2 | 2.9 | 2.7 | 2.1 | 2.3 | 2.3 |
| | South Korea | 1.4 | 2.5 | 2.0 | 3.6 | 2.5 | 2.1 |
| | Taiwan* | 1.4 | 3.1 | 2.7 | 2.5 | 1.9 | 1.6 |
| South Asia | India | 8.2 | 6.9 | 6.7 | 5.4 | 4.7 | 4.3 |
| | Indonesia | 5.1 | 5.0 | 5.1 | 3.7 | 2.7 | 2.7 |
| | Malaysia | 3.7 | 4.9 | 4.3 | 2.5 | 2.1 | 2.8 |
| | Philippines* | 5.6 | 6.2 | 6.2 | 6.0 | 3.6 | 3.0 |
| | Singapore* | 1.1 | 2.1 | 2.3 | 4.8 | 3.0 | 2.5 |
| | Thailand | 1.9 | 2.8 | 3.1 | 1.3 | 0.7 | 1.7 |

*Source: BNP Paribas Group Economic Research, BNP Paribas Global Markets forecasts as of 30 August 2024*
** IMF data and forecasts as of 30 August 2024*

### GROWTH

- **US soft-landing remains our base case scenario.** Our US GDP growth forecast is 2.5% for 2024, and 1.9% for 2025. The Sahm rule (recession indicator) is triggered in US unemployment rate. However, if Sahm rules is applied to US initial jobless claims, there is no signs of a recession.
- Recent economic activity numbers in China correspond to GDP growth of below 5% this year. We expect acceleration in special local government bond issuance, while faster renewal of equipment and consumer goods trade-ins will help to nudge up growth in the coming months.

### INFLATION

- Recent inflation numbers in the US, Eurozone and UK show that the disinflation trend continues, giving room for the major central banks to cut rates in September 2024.
- In Japan, Tokyo core inflation accelerated for a fourth straight month by 2.4% YoY in August 2024, above the central bank's 2% target. We expect the Bank of Japan to hike rate further in 4Q 2024.
- China's inflation remained muted, couple with the Fed starting to cut rate soon, this will give more room for domestic easing measures to achieve the country's growth and inflation targets.

## Equities

POSITIVE NEUTRAL NEGATIVE

| OVERALL GLOBAL: POSITIVE | | |
|---|---|---|
| Positive | Neutral | Negative |
| **COUNTRY** | | |
| UK<br>Japan<br>Emerging Mkt<br>Eurozone | US | - |
| **SECTOR** | | |
| Healthcare<br>Materials<br>Industrials | Energy<br>Comms.<br>Real Estate<br>Technology<br>Financials<br>Utilities | Consumer Staples<br>Consu. Discre. |

| OVERALL ASIA: POSITIVE | | |
|---|---|---|
| Positive | Neutral | Negative |
| **COUNTRY** | | |
| China<br>Singapore<br>South Korea<br>Indonesia | Taiwan<br>India, Thailand<br>Malaysia<br>Philippines | - |
| **SECTOR** | | |
| Comms.<br>Consu. Discre.<br>Consumer Staples<br>Technology | Energy<br>Materials<br>Real Estate<br>Financials<br>Healthcare<br>Utilities | Industrials |

- Markets were quick to recover from the "Black Monday" in early August 2024. However, the Mag7 failed to reached new highs during the rebound, while non-Mag7 US Index hitting fresh highs.
- Markets tend to double dip after huge spikes in the VIX Index. This coincides with seasonal headwinds as the 2nd half of September tends to be the weakest period of the year and US election years often experience a correction in October.
- While the short-term outlook may look bumpy, the long-term backdrop of falling rates in a non-recessionary environment still looks encouraging for equities. **We would see any short-term weakness as buying opportunity, especially in our favoured markets such as EU, UK Equities, Japan and Small Caps.**

| | | 1-month (%) | YTD (%) | 2023 (%) | Forward PE (x) | Trailing PB (x) | Dividend Yield (%) 2024f | EPS Growth (%) 2024f | EPS Growth (%) 2025f | ROE (%) 2024f |
|---|---|---|---|---|---|---|---|---|---|---|
| Developed | US | 2.3 | 18.0 | 25.0 | 21.4 | 4.9 | 1.5 | 10.0 | 15.5 | 18.2 |
| | Japan | -2.8 | 15.6 | 25.9 | 14.4 | 1.5 | 2.1 | 17.4 | 7.2 | 9.0 |
| | Eurozone | 1.6 | 8.2 | 16.0 | 12.8 | 1.8 | 3.2 | 2.2 | 10.6 | 13.0 |
| | UK | 0.2 | 8.2 | 3.3 | 11.9 | 1.9 | 3.6 | 0.5 | 8.4 | 13.6 |
| | Asia Ex-Japan | 1.8 | 9.8 | 3.6 | 12.5 | 1.7 | 2.6 | 28.2 | 15.7 | 11.7 |
| North Asia | China | 0.5 | 1.9 | -12.8 | 8.9 | 1.1 | 3.4 | 15.1 | 11.0 | 11.3 |
| | China A-shares | -3.5 | -3.2 | -11.4 | 11.2 | 1.4 | 3.6 | 10.8 | 10.4 | 11.1 |
| | Hong Kong | 5.3 | -8.1 | -17.8 | 11.6 | 0.9 | 4.4 | 10.6 | 9.3 | 7.1 |
| | South Korea | -5.1 | 0.4 | 23.9 | 8.7 | 1.0 | 2.1 | 119.7 | 29.9 | 10.3 |
| | Taiwan | 0.5 | 31.5 | 26.7 | 17.1 | 3.2 | 2.4 | 32.6 | 18.6 | 15.8 |
| South Asia | India | 1.1 | 23.0 | 20.3 | 24.1 | 4.5 | 1.1 | 10.0 | 17.2 | 15.4 |
| | Indonesia | 4.4 | -0.8 | 2.2 | 13.1 | 2.4 | 4.6 | -0.3 | 7.5 | 16.2 |
| | Malaysia | 3.1 | 14.2 | -3.2 | 14.1 | 1.5 | 3.6 | 14.7 | 6.0 | 8.0 |
| | Philippines | 5.9 | 8.9 | 1.1 | 12.0 | 1.9 | 1.9 | 14.3 | 9.4 | 13.6 |
| | Singapore | -1.8 | 8.2 | -3.9 | 12.2 | 1.5 | 5.4 | 10.0 | 3.8 | 10.6 |
| | Thailand | 3.0 | -2.3 | -13.8 | 15.8 | 1.7 | 3.1 | 11.6 | 13.6 | 10.0 |

*Source: MSCI indices in local currency terms, Bloomberg, Datastream, BNP Paribas (WM), as of 30 August 2024*

## Fixed Income

POSITIVE NEUTRAL NEGATIVE

| OVERALL GLOBAL: NEUTRAL | | |
|---|---|---|
| POSITIVE | NEUTRAL | NEGATIVE |
| EMD (LC)<br>EMD (HC)<br>IG | ▼ UST<br>High Yield | - |

| OVERALL ASIA (USD): NEUTRAL | | |
|---|---|---|
| POSITIVE | NEUTRAL | NEGATIVE |
| Japan | Korea<br>India<br>Philippines<br>Singapore<br>Indonesia | Hong Kong<br>China |

| | | Total Return (%) 1-Month | YTD | 2023 | Yield-to-Worst (%) |
|---|---|---|---|---|---|
| Asia | Asia USD Bond | 1.3 | 4.9 | 7.3 | 5.0 |
| | Asia Local Currency Bond | 5.4 | 4.0 | 7.2 | 4.1 |
| | China | 1.0 | 5.3 | 5.0 | 5.2 |
| | Hong Kong | 1.2 | 4.9 | 7.7 | 4.9 |
| | India | 1.3 | 7.4 | 9.5 | 5.7 |
| | Indonesia | 2.6 | 3.3 | 9.9 | 5.0 |
| | Singapore | 1.0 | 3.8 | 6.6 | 4.5 |
| | South Korea | 0.9 | 4.2 | 6.6 | 4.6 |
| | Philippines | 2.1 | 3.5 | 8.3 | 5.0 |
| Other Regions | US 10-year Treasuries | 1.5 | 3.0 | 3.8 | 3.8 |
| | US Investment Grades (IG) | 1.4 | 3.1 | 5.5 | 4.4 |
| | US High Yield (HY) | 1.6 | 6.3 | 13.4 | 7.3 |
| | Emerging Market USD Bond | 1.3 | 5.4 | 7.1 | 5.5 |

*Source: Barclays indices, Bloomberg, BNP Paribas (WM) as of 30 August 2024*

| US Treasury 12-month Yield Targets (%) | 2Y | 5Y | 10Y | 30Y |
|---|---|---|---|---|
| | ▼ 4.00 | ▼ 4.00 | ▼ 4.00 | ▼ 4.25 |

- We add one Fed rate cut to our forecast for this year on the back of deteriorating labour market in the US. Hence, **we now expect two 25bp rate cuts in 2024 (September and December) and four cuts in 2025.**
- We expect US bond yields to increase in the short term. We thus **tactically move to Neutral from Positive on US government bonds.** We intend to re-enter the asset class with a better starting yield in a few months as we remain constructive on US Treasuries strategically.
- We revise down the 12-month yield targets for the whole US Treasury yield curve, with 10-year yield target down to 4% from 4.25%.
- **We continue to favour high quality assets such as investment grade corporate bonds** as yields remain attractive and credit spreads could tighten further as economic growth and investor demand persist. WE prefer short maturities in the US and up to 10 years in the Eurozone.
- In Asia, we are positive on Japan. BoJ's rate normalisation, corporate governance reforms and high operational efficiency position banks and insurers for growth in interest income and investment returns. There are also abundant AA-rated quasi-sovereign names available in Korea.

## Forex & Commodities

POSITIVE NEUTRAL NEGATIVE

### 12-MONTH FOREX VIEW

| Positive | Neutral | Negative |
|---|---|---|
| JPY INR AUD CAD | USD CNY EUR SGD GBP PHP NZD KRW | IDR MYR THB |

### COMMODITIES

| Positive | Neutral | Negative |
|---|---|---|
| Gold Base metal | Oil | - |

- EUR: The bigger and faster Fed rate cuts expectations pushed the dollar lower. In the short-term, the USD could rebound as the repricing looks extreme. Hence, we change our 3-month target for EURUSD to 1.10. Our long-term outlook suggests more rate cuts in the US over 2025-26 compared to the ECB, and we keep our 12-month target at 1.12.
- JPY: We expect the BoJ will hike rates in every quarter until the nominal rate reaches about 1%, and then slow down the hiking pace thereafter. We change our USDJPY 3-month target to 145 and keep our 12-month target at 140.
- GOLD: **We keep our positive view and our 12-month target at $2600/oz.** The downside risk seems limited as central banks continue their strategic purchases, geopolitical risks remain elevated, real yields decline and USD weakens.
- OIL: **We turn neutral and expect Brent to trade in the $75-85 range** as Chinese demand remains weak, US recession fears linger and the OPEC+ is looking to taper its voluntary productions cuts from December.
- BASE METALS: A rebound in manufacturing PMI is needed for base metals to fully recover, but we remain positive as inventories for example for copper outside of China are low. The medium-term outlook remains bright due to structural demand for infrastructure, decarbonisation, defense and AI.

## Forex Forecasts

| | | Spot | 3-month | | 12-month | |
|---|---|---|---|---|---|---|
| | | As of 30 Aug 2024 | View | Target | View | Target |
| Developed | USD Index* | 101.70 | = | 101.8 | = | 100.0 |
| | Japan | 145.6 | = | 145 | + | 140 |
| | Eurozone | 1.107 | = | 1.10 | = | 1.12 |
| | UK | 1.314 | = | 1.31 | = | 1.30 |
| | Australia | 0.679 | = | 0.68 | + | 0.70 |
| | New Zealand | 0.627 | - | 0.60 | = | 0.63 |
| | Canada | 1.348 | + | 1.32 | + | 1.30 |
| Asia Ex-Japan | China | 7.088 | - | 7.20 | = | 7.20 |
| | South Korea* | 1,336 | - | 1,390 | = | 1,360 |
| | India | 83.87 | + | 82.0 | + | 82.0 |
| | Indonesia* | 15,455 | - | 16,300 | - | 16,200 |
| | Malaysia* | 4.323 | - | 4.82 | - | 4.76 |
| | Philippines* | 56.15 | = | 57.6 | = | 57.3 |
| | Singapore* | 1.303 | - | 1.36 | = | 1.34 |
| | Thailand* | 33.85 | - | 37.2 | - | 36.3 |

*Source: BNP Paribas (WM) as of 30 August 2024*
**BNP Paribas Global Markets forecast as of 30 August 2024*

Note: + Positve / = Neutral / - Negative

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