FULLERTON FUND MANAGEMENT

THE FULLERTON WEEKLY

09 January 2017

Our Views on Asian Fixed Income and FX in 2017

2017 will see rising interest rates in the US as the Federal Reserve begins to normalise interest rates. The Fed has guided for steeper borrowing costs in 2017, with most Fed officials projecting three potential rate hikes for the year, versus two previously. With markets having priced in a shallower rate hike cycle versus the Fed, US Treasuries are likely to be volatile due to the divergence in rate hike expectations.

In Asia, the region as a whole is likely to be impacted by rising US rates and potentially protectionist US policies, albeit to varying degrees. We expect regional policymakers to stay vigilant in the face of downside risks, and most Asian countries have taken measures to reduce macro vulnerabilities. However, central banks have less leeway to ease rates. We expect to see selective monetary easing, as policymakers are constrained by tighter external financial conditions. Instead, governments are likely to pursue fiscal pump-priming instead.

We believe the risk of increased US trade protectionism under President-elect Trump has risen. In such a scenario, Hong Kong, Singapore, Taiwan and Korea are most at risk to US trade protectionism, in terms of export growth sensitivities to the US. On the other hand, India and Indonesia are structurally positive stories, and the progress on government-led reforms has been encouraging. Their large domestic-oriented economies are also less vulnerable to downside growth risks from potential shifts in US trade policies. On China, we also expect policymakers to prioritize growth and stability given the need for political renewal in 2017.

From a currency standpoint, we believe the USD is likely to strengthen further against most currencies, with USD strength supported by the rising interest rate environment in the US. Against the backdrop of sustained USD strength, we expect Asian currencies to generally weaken against the USD in 2017. We believe that a stronger USD will have differentiated impact amongst Asian currencies. With increased likelihood of US trade protectionism, low yielding Asian currencies with greater sensitivities to US export growth sensitivities, (such as the KRW and the SGD) are more vulnerable to currency weakness against the USD. Conversely, we expect the more domestic consumption driven, higher yielding currencies, such as the IDR and INR, to perform better, given their relatively higher levels of insularity against the vagaries of global trade. In addition, India and Indonesia continue to offer the highest real yields in the region, which offers a relatively better buffer against rising US interest rates.

On credits, we hold the view that Asian credits continue to offer attractive carry for income. We expect Investment Grade (IG) credit spreads to remain stable in 2017, supported by lower expected net supply and continued strong participation from the region's domestic investor base. Given our views of sustained USD strength in 2017, we expect USD bonds to outperform local currency bonds. Notwithstanding this, we believe that both Indonesia and India local currency bonds will continue to provide positive returns from a total return standpoint, despite the negative impacts from rising US rates and USD strength.

	Value	% wow Change
Equities		
Dow Jones Indus. Avg	19,963.8	+1.0
S&P 500 Index	2,277.0	+1.7
MSCI AC Asia Pacific	138.4	+2.5
S&P/ASX 200 Index	5,755.6	+1.6
Hang Seng Index	22,503.0	+2.3
Ho Chi Minh Stock Index	679.8	+2.2
Jakarta Composite Index	5,347.0	+0.9
FTSE Bursa Malaysia KLCI	1,675.5	+2.1
KOSPI Index	2,049.1	+1.1
Karachi 100 Index	49,038.2	+2.6
S&P BSE Sensex Index	26,759.2	+0.5
Shanghai SE Composite	3,154.3	+1.6
Stock Exch Of Thai Index	1,571.5	+1.8
Straits Times Index	2,962.6	+2.8
Taiwan TAIEX Index	9,372.2	+1.3
TOPIX Index (Tokyo)	1,553.3	+2.3
Bonds / Currencies		
US 10YR Treasuries	2.4193	-3 bps
EUR/USD	1.0532	+0.1
USD/JPY	117.0200	+0.1
GBP/USD	1.2287	-0.4
Commodities		
Gold (Spot)	1,179.2	+1.7
Crude Oil (WTI)	54.0	+0.5
RJ/CRB Commodity Index	193.5	+0.5

Source: Bloomberg (last trading price for week ended 06 January 2017)

Disclaimer

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