Quarterly Investment Strategy
Third Quarter 2016

LATE CYCLE UNCERTAINTIES

ASSET ALLOCATION

Equities reduced to Underweight,
Fixed Income raised to Overweight,
Commodities reduced to Underweight,
Cash raised to Overweight

EQUITY

Remain Overweight Developed Markets,
Remain Underweight Emerging Markets

FIXED INCOME

Remain Underweight Developed Markets,
Emerging Markets raised to Neutral

COMMODITIES

Overweight Energy and Gold,
Underweight Base Metals and Bulk Commodities

UOB Asset Management
大華資產管理

As one of the thought leaders in asset management, UOBAM regularly produces topical investment research articles and publications to help our clients stay on top of financial market developments.

Webcast – Asset Allocation Strategy for Q3 2016

In our quarterly webcast, Mr Tony Raza, Head of Multi Asset Strategy Unit, will share our asset allocation strategy, as well as discuss key issues driving developments in global markets.

View the webcast on the homepage of our website at uobam.com.sg.

INVESTMENT STRATEGY SUMMARY

In the first five months of 2016, most asset classes delivered positive returns but with large levels of volatility. The year started nearly in a panic as global investors were concerned about a new recession in the US and a downturn in the China economy. By the second quarter, those concerns had eased as US and China data suggested sustained, though sluggish, economic growth.

Near the end of the second quarter, risk assets such as equities, commodities and high-yield fixed income had recovered to positive year-to-date returns. At the same time, gold and Group of Seven (G7) government bonds had also performed. The first part of the year saw the odd situation of both risk-free assets and risk assets simultaneously performing, though Britain's vote to leave the European Union (EU) at the end of June caused some dislocation with equity markets falling while safe haven assets like gold outperforming.

As we enter the third quarter, it seems clear that the simultaneous performance of both risk-free assets and risk assets cannot continue. There are legitimate growth concerns that will hurt equities, commodities and high-yield fixed income, or growth will be sufficient to avoid a global weakness and that will cause risk-free assets like government bonds to weaken.

We continue to expect that global growth and expansion will continue albeit at a moderate pace. If the global economies are not approaching a new recession, we would expect that risk assets will eventually outperform risk-free assets. However, in the near term, we note that resolving the asset class inconsistencies is likely to be a volatile process.

We therefore start the third quarter with a more cautious outlook as it appears that most paths lead to near-term weak performance. If economic growth is sustained, then there is a risk of asset class volatility as rate expectations will get repriced. Conversely, if economic risks increase, then risk assets will also perform poorly. In addition, there are several global risks such as Britain's vote to leave the EU and the presidential election in the United States (US) that could trigger market weakness as well.

We think the most likely path is that growth will continue and risk assets will eventually provide better performance. However, in the near term we expect some weakness as rate expectations increase and investors watch the unfolding political developments in Britain and the EU. We expect there to be better opportunities to raise equity levels at a later time and will continue to monitor macro developments to find the right time to make those investments.

John Doyle
Chief Investment Officer
Equities & Multi-Assets

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Chief Investment Officer
Fixed Income & Structured Investments

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GLOBAL ASSET ALLOCATION SUMMARY

We start the third quarter of 2016 with an underweight on equities and an overweight on fixed income. This asset allocation stance was revised after the United Kingdom (UK) voted in a referendum on 23 June 2016 to leave the European Union (EU), roiling financial markets in the immediate aftermath of the vote. Previously when we first held our quarterly strategy meeting in early June, we had downgraded equities to a neutral and upgraded fixed income similarly to a neutral. We expected global growth to continue and policy to be supportive around the world but saw risks rising and insufficient catalysts for equities to break out of the trading range they had been in for the past year. Following the UK referendum, markets have been highly volatile and at the time of writing[1], there are many uncertainties about how this will impact Britain, the European Union – and indeed the global economy and expectations on interest rates. This prompted us to take an even more cautious view on risk assets.

Investment markets have been volatile in 2016 as global investors grapple with issues of global growth and risks from lower oil prices, deflation and a China slowdown. We think that economic growth continues to be moderate but improving, without strong inflationary pressures. Lower oil prices are supportive of better global growth but also lead to lower energy investments and capital expenditure which can give the appearance that growth indicators are slowing. These trends could lead to new highs in equities, but we expect that it will not be until the fourth quarter before these trends and earnings growth become more convincing. Developments in Britain and the EU, which are still unfolding, could also throw a spanner in the works, increasing risks to the global economy.

Global Asset Allocation*	--	-	N	+	++
Equities	○	●	◄	◄	○
Fixed Income	○	►	►	●	○
Commodities	○	●	◄	○	○
Cash	○	►	►	●	○

Notes:
*Three to six months horizon
The weights are relative to the respective benchmark(s).
'- -' denotes maximum underweight, '-' slight underweight, 'N' neutral, '+' slight overweight, '+ +' maximum overweight; arrows show change from last quarter.

Equities – Downgrade to Underweight

Global equities have been stuck in a range since the middle of 2015 and it is not clear that there are sufficient catalysts to break out of that range positively. There are also some growing risks such as Britain's vote to exit the EU, US rate increases and the US elections that add uncertainties to the market. We downgrade equities from an overweight position to underweight until we see more evidence of sustained economic and corporate profit growth. Our positioning within equities is to favour lower beta positions to reflect increased risk aversion.

Fixed Income – Upgrade to Overweight

We upgrade fixed income from underweight to overweight. In an environment of slow growth, fixed income has been a stable performer. We expect that global markets need more catalysts before expectations of stronger growth become more convincing. If growth improves, rising inflation could put pressure on rates to rise. However, for the next quarter we expect that slow growth and tail risks will continue to be an overhang on markets and fixed income will be a comfortable investment. Within fixed income, we are defensive with a preference for high quality corporate credit.

Commodities – Downgrade to Underweight

Most commodities have rallied in the first half of 2016 from deeply oversold levels. However, factors such as a structurally strong US dollar (USD), slowing China demand, and a period of seasonal weakness, has made the commodities asset class less attractive after the recent rally. We downgrade commodities from neutral to underweight, with a preference for gold as a relative safe haven in the midst of heightened risk aversion.

Cash – Upgrade to Overweight

In a period of low growth with rising uncertainties, we believe that higher cash levels could prove useful for us to deploy when there is greater certainty on growth and risks. We raise cash from an underweight to an overweight position.

[1]The contents of this report were updated as at June 2016 and relevant portions were revised on 28 June 2016.

GLOBAL INVESTMENT STRATEGY
LATE CYCLE UNCERTAINTIES

Fundamentally, we maintain a positive outlook on the sustainability of global growth over the second half of 2016. However, we think that caution is warranted over the next quarter. Equity markets have been stuck in a trading range for the past year and it is not clear that there are enough catalysts in economic growth or corporate earnings for equities to break out of their range positively. In addition, there are growing risks relating to Britain's vote to exit the EU, rising rates in the US and increasing uncertainties in the US presidential election.

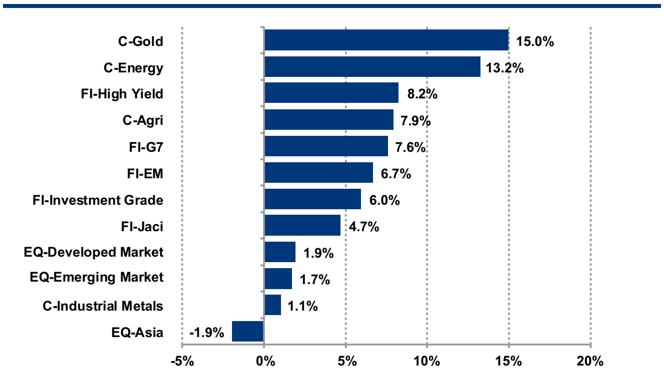
Investment markets have proven highly volatile over the past three quarters with two major corrections of over ten per cent occurring in global equities and additional volatility in credits, high-yield bonds and commodities. Investors have been concerned about the potential of slowing global economic growth. While we think the global economy has been growing at a similar slow pace compared to the previous three years, we believe that markets are getting more nervous about slowing growth as the economic cycle continues. It has been seven years since the last recession and expectations are increasing that one should occur at some point.

How long until the next recession?

There have been several uncertainties in the past 12 months that have contributed to market volatility such as interest rate hikes, fears over China's growth deceleration, falling oil prices and fears of a US economic slowdown. At the heart of it, we think the biggest issue is that this economic expansion has been going on for seven years and many investors are thinking that the world is due for another recession. In addition, with the memory of painful losses from 2008 where global equities declined by 50 per cent, investors are eager to reduce exposure before the next recession.

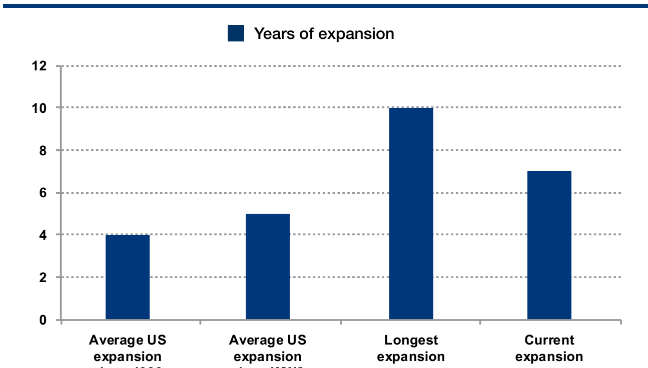
Over the past century, economic expansions from the end of the preceding recession in the US (country with the longest data series and the greatest impact to the world) have averaged four years. However, expansions have become slightly longer averaging five years since World War II. The longest expansion was ten years and occurred from 1991 to 2001. Looking at historical data, investors may have some idea of what to expect on the duration of an expansion.

Year-to-date Asset Class Performance (USD)



Source: Bloomberg, UOBAM, 27 May 2016

Expansion cycles in years



Source: National Bureau of Economic Research (NBER), UOBAM, 3 June 2016

The last recession ended in June 2009 and the expansion through June 2016 marks the seventh year of this expansion. Thus, the current expansion is two years past the average but three years short of the longest expansion. Most investors have observed that we must be closer to the end than the beginning of this expansion. Hence, it might be reasonable to expect that in this last stage of the cycle, equities are likely to have a higher degree of volatility and many investors may be overly quick to reduce exposures at the first hint of trouble.

What is particularly surprising about this cycle is that though we are in a longer-than-average expansion, there is wide-spread acceptance that the global recovery has been sub-par with many structural problems in housing, labour and government debt. One driver of the speed (and length) of a cycle lies in the inflation level. High inflation results frequently from overheating as all of an economy's resources are put to use. In the current world of low inflation where unemployment is still fairly high in many parts of the world and capacity utilisation is still fairly low, it is difficult for an economy to get overheated and for inflation to pick up.

Our estimates are that there are likely two to three years remaining in this economic expansion. This estimate is based on a forecast of when excess capacity may reasonably be expected to be used up and overheating affects some major markets. Another measure we use to estimate the expansion is how long it will take for the yield curve to invert. This can also be thought of as how long it will take central banks like the US Fed to raise short-term rates so that they match or surpass the level of the ten-year rate. This is a condition we have seen before in the previous five recessions and we estimate that it will take two to three years.

Rising risks

There are several risks in the next few months which we would like to highlight. At the top of our list are:

1) Britain's vote to exit the EU,
2) how markets will digest potentially rising rates and
3) the risks of rising uncertainties from the US presidential election.

On 23 June, Britain voted by referendum to leave the European Union (Brexit), sending financial markets into a turmoil with the Sterling pound falling by about 10 per cent against the US dollar in a day to a 30-year low. Expectations are for Britain to invoke Article 50 of the 2007 Lisbon Treaty to set the terms by which it withdraws from the EU in accordance with its constitutional requirements. However, developments are unfolding as we write[2] and the medium to long term impact of the UK vote are still difficult to quantify. Outgoing British Prime Minister David Cameron has indicated that the UK will not invoke Article 50 until the governing Conservative Party selects a new leader and the new Prime Minister, which will delay the formal two-year exit negotiations between Britain and the EU. This will prolong the uncertainty with a lack of clarity on trade and economic relations between the UK and Europe weighing on business investment decisions into the UK. Already credit rating agencies have lowered the UK's sovereign rating with Standard & Poor's downgrading it to AA (Negative) from AAA, citing the risk of a less predictable and effective policy framework, while Fitch cut its rating by one notch to AA from AA+ and Moody's lowered its outlook to negative from stable albeit maintaining its sovereign rating at Aa1. Beyond the impact on the UK, there are also likely implications for the European Union, such as the possibility of other EU member states calling for their own referendums, potentially leading to structural changes to the grouping. The UK is also a significant contributor to the EU's overall budget and extricating the UK's share and reallocating it to other member states will likely be a politically delicate process. All in, we think the near-term impact of Brexit is sharply negative for risk assets with the protracted period of uncertainty having negative implications on growth prospects for the UK and potentially for the region.

Our main concern with US rates is that the US bond markets have assumed a very low level of interest rate increases and inflation. US Federal Reserve (Fed) Fund futures imply the market only expects one rate hike in 2016 and the US Treasury (UST) ten-year bond yield at below two per cent implies a low level of expectations for future hikes as well. US consumer economic data trends and improving levels of inflation warrant further rate hikes. The US Fed governors have been publicly articulating that the market is being too complacent regarding rate hikes. The risk is that if rate expectations increase and the UST ten-year yield rises, then markets are likely to be volatile during that period, much like the 2013 period when UST ten-year yields climbed to three per cent on the back of then-Fed chairman Ben Bernanke's announcement of a winding down of quantitative easing (QE). Similar to that period, we do not need to be structurally bearish about rising rates for near-term volatility to rise.

US election years are generally positive for equity markets and they have historically been able to perform well under both Democratic and Republican administrations. US stock markets tend to rise by a median return of 8.3 per cent during election years. They have also risen by 10.5 per cent during the course of Democratic administrations and four per cent during Republican administrations.

[2]The contents of this report were updated as at June 2016 and relevant portions were revised on 28 June 2016.

S&P Annual Stock Market Price Returns From 1880

	MEDIAN RETURN	YEARS
All Years	8.0%	136
Presidential Election Years	8.3%	34
During Democratic Presidencies	11.0%	63
During Republican Presidencies	4.0%	72

Source: Macro Research Board (MRB) Research, UOBAM estimates, 25 April 2016

The concern with this election is that uncertainties are rising by a greater extent than what we have seen in the past. Republican candidate Donald Trump's policies are not very clear but his views on trade, foreign policy and fiscal policy have generally not been market-friendly. It is not clear what his specific actions will be if he is elected president but we think it is fair to say markets will price in rising levels of uncertainty. On the Democratic side, Hillary Clinton, who was expected to be more of a status quo candidate who would continue President Obama's policies, has been forced to change views on trade and financial reform due to the nomination process against Bernie Sanders. It is increasingly less clear on which direction both candidates will be pulled and we are cautious about this level of uncertainty for markets.

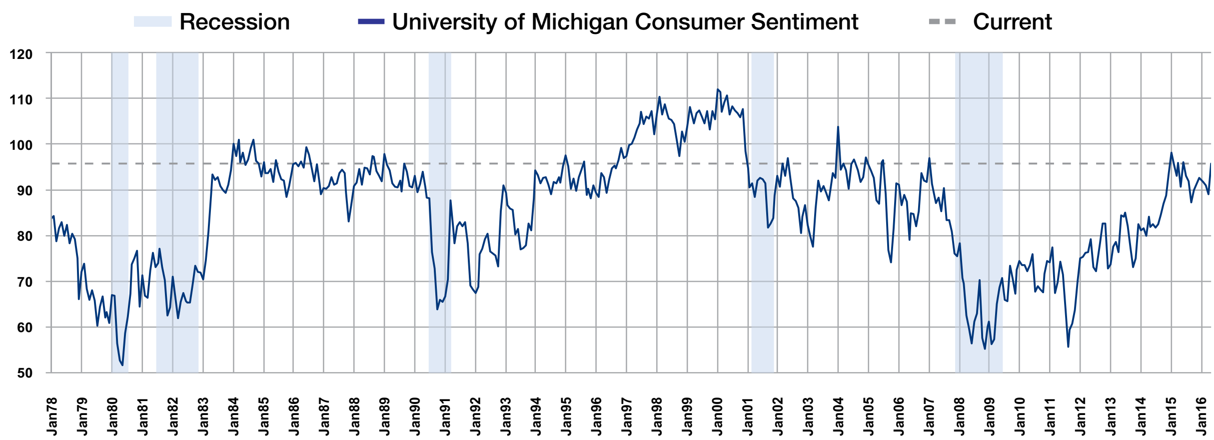
Upside risks

While we have sounded a note of caution regarding risks, we would be quick to highlight that there are upside risks as well. One of the most encouraging global trends is the health of the US consumer. Consumption drives the majority of the US economy and the US economy is in turn a key support for the global economy. We suspect many investors have overlooked this underlying strength because of the broad perceptions of household weakness following the 2008 financial crisis and the impression raised by angry voices in politics that partially explain the rise of candidates like Donald Trump. However, on an objective basis of monitoring job gains, wage gains, hours-worked gains, consumer confidence, savings rates, petrol pump prices, and mortgage rates, it is hard to find a period in the last 20 years where the US consumer has looked as strong as he does now.

Employment opportunities are a key starting point for assessing the consumer. The official unemployment rate is down to 4.7 per cent which is in line with the US Fed's assessment of full employment (allowing for a certain amount of continuous transition of labour). The country has been growing the total number of jobs by about two per cent per year over the past four years. The average annual wage increase is 2.4 per cent. Indications from the Job Openings and Labour Turnover Survey (JOLTS) show that job openings are at the highest levels in more than a decade.

Consumer confidence is also tracking at levels in line with the highest cyclical levels reached since the 1970s with the exception of the dot.com bull market from 1997 to 2000. This confidence is further supported by the fact that petrol pump fuel prices for US drivers have been in their lowest sustained range for over a decade. Mortgage rates at three to four per cent across most of the country are effectively near or at all-time lows. Finally, the savings rate has been higher through this expansion and at six per cent, remains higher than that seen since the mid-1990s.

University of Michigan Consumer Sentiment



Source: Bloomberg, June 2016

There are many headlines about the difficult situation of the US consumer. However, tracking the key economic data points that affect the US consumer, there is a strong case to be made that the US consumer has not looked this healthy since the late 1990s. If that confidence spills over into more confident spending patterns, then there is significant room for both economic trends and equity markets to surprise on the upside.

Assessment and outlook

In summary, we think that the fundamentals of the global economy and global equity markets remain positive, albeit unexciting. At the same time, we are tracking a number of risks including developments in Britain and Europe, US rate rises and the US presidential election. In addition, we note that global markets have been range-bound for the past year and we do not see near-term catalysts to support breaking out to new highs. At this point, we think that the risks outweigh the potential returns and thus tactically recommend a more cautious outlook for risk classes.

The current expansion has continued for seven years, which is already higher than the average of five years. Over the next few years, we would expect investors to become more anxious as this expansion gets close to the historic expansion of ten years. Our models based on when inflation trends will trigger interest rate hikes, which slow down the economy, point to at least another two years of expansion.

While there are many risks, we also would highlight that there are upside risks as well. The US consumer drives the US economy. This in turn drives the global economy, which looks surprisingly healthy as measured by employment, wage gains, confidence; savings rate levels, mortgage rates and petrol prices. If the US consumer's confidence finally translates into better spending, then there is room for economic and equity market upside.

In conclusion, we reduce equities to an underweight, raise fixed income to an overweight position, reduce commodities to an underweight position, and raise cash to an overweight position.

EQUITY STRATEGY

GLOBAL EQUITY

SECTOR ALLOCATION	--	-	N	+	++
Consumer Discretionary	○	○	●	○	○
Consumer Staples	○	○	●	○	○
Energy	○	▶	▶	●	○
Financials	○	○	●	◀	○
Healthcare	○	○	○	○	●
Industrials	○	●	○	○	○
Materials	○	●	○	○	○
Information Technology	○	○	○	●	◀
Telecommunications Services	●	○	○	○	○
Utilities	●	○	○	○	○

Notes:
The weights are relative to the benchmark – MSCI AC World Index.
'- -' denotes maximum underweight, '-' slight underweight, 'N' neutral, '+' slight overweight, '+ +' maximum overweight; arrows show change from last quarter.

We have a positive outlook on global equities in the longer term, underpinned by continued growth in the advanced economies, modest earnings growth outlook and strong corporate profitability.

Given the years of underinvestment following the Global Financial Crisis, we believe that technology companies should benefit from rising corporate expenditure on technology hardware, software and business solutions. Hence, we are overweight on the information technology sector. We are also overweight on the healthcare sector given its strong cash generation and dividend yield. The sector continues to benefit from recent merger and acquisition activities and strong earnings growth momentum from the biotech sub-sector. We also have an overweight position in energy as we believe that the demand-supply fundamentals in the sector have improved considerably in recent months amid attractive valuations.

Our strategy continues to be underweight on materials given the sub-par growth of the global economy. We have also adopted a more cautious stance on interest rate-sensitive sectors such as utilities and telecommunications which could be impacted adversely by expectations of the US Fed tightening policies in the coming quarters.

REGIONAL ALLOCATION	--	-	N	+	++
DEVELOPED	○	○	○	●	○
US	○	○	○	●	○
EUROPE	○	●	◄	○	○
JAPAN	○	○	●	○	○
CANADA	○	○	●	○	○
AUSTRALIA	○	○	●	○	○
EMERGING	○	●	○	○	○
Asia Ex-Japan	○	○	●	○	○
LATAM	○	●	○	○	○
EMEA	○	●	○	○	○

Notes:
The weights are relative to the benchmark – MSCI AC World Index.
'- -' denotes maximum underweight, '-' slight underweight, 'N' neutral, '+' slight overweight, '+ +' maximum overweight; arrows show change from last quarter.

Across regions, we have a preference for Developed Markets (DM) over Emerging Markets (EM). This is due to the divergence in growth trajectories, the effects of capital flows from EM, and perceived risks to earnings expectations from shifting revenue and cost trends. Within DM, we remain overweight on the US. Our view is that the dollar strength which was previously a headwind to overseas corporate profits will subside in the coming quarters due to base effect. Meanwhile, the tightening labour force will result in higher wage inflation but the higher disposable income along with lower gasoline prices will support the retail sector, which remains a larger part of the economy. We retain the view that the economy remains on a strong recovery trajectory, and the US remains attractive for selective value plays.

We hold an underweight position in Europe despite the potential for further economic recovery. A weaker euro has helped to lift confidence and boost economic activities. The region also has significant operating leverage to an upturn in economic activity with profit margins currently at trough levels. However, heightened political risks arising from the UK's vote by referendum to exit the European Union creates an overhang on the region.

Concerns continue to linger over the long-term efficacy of Japan Prime Minister Abe's 'third arrow' economic policy. However, we see opportunities arising from beneficiaries of Japan's QE. Economic data remains mixed but we believe that the Bank of Japan (BoJ) will remain accommodative, which would help to support the market. Despite disappointments on policy and the anaemic economic backdrop, there are some positive developments in corporate governance and corporate performance. Hence we retain our neutral position in Japan.

We retain our underweight position in EM. Challenges are expected to persist due to domestic imbalances and the build-up of excess credit in the period following the Global Financial Crisis. The slowdown in China continues to weigh heavily on the demand and prices of resources. The abrupt shift in the resources sector has dampened investments and growth in much of the developing world. We believe that the EM still present good multi-year opportunities from a structural and macro standpoint but face challenges from a cyclical standpoint. Growth is falling short of expectations and corporate earnings could face further downward pressures unless productivity levels can continue to rise. There are interesting bottom-up opportunities and stock selection is increasingly critical.

ASIA PACIFIC EQUITY

SECTOR ALLOCATION	--	-	N	+	++
Consumer Discretionary	○	○	○	●	○
Consumer Staples	○	○	●	○	○
Energy	○	○	▶	▶	●
Financials	○	○	●	◀	○
Healthcare	○	○	○	○	●
Industrials	○	●	○	○	○
Materials	○	●	○	○	○
Information Technology	○	○	●	◀	◀
Telecommunications Services	●	○	○	○	○
Utilities	○	●	○	○	○

Notes:
The weights are relative to the benchmark – MSCI Asia Pacific Index.
'- -' denotes maximum underweight, '-' slight underweight, 'N' neutral, '+' slight overweight, '+ +' maximum overweight; arrows show change from last quarter.

Our strategy is currently overweight on the energy, healthcare and consumer discretionary sectors. We have increased our weights in the energy sector recently given the strong demand response resulting from low oil prices and improving demand-supply balance globally. We are also overweight on the healthcare sector given its strong cash generation and dividend yield. We remain positive on the longer-term trend for the consumer sector as it provides exposure to the continued strong growth of domestic demand. We have reduced our position in the technology sector to neutral as the sector is currently facing headwinds arising from slowing revenue growth. However, we remain positive on the longer term trend.

The strategy is underweight on the materials sector due to concerns on China, which is experiencing slower growth. The country is also currently in the midst of implementing reforms.

REGIONAL ALLOCATION	--	-	N	+	++
Asia Ex-Japan	○	○	○	●	○
Japan	●	◀	○	○	○
Australia & NZ	○	○	▶	●	○

Notes:
The weights are relative to the benchmark – MSCI Asia Pacific Index.
'- -' denotes maximum underweight, '-' slight underweight, 'N' neutral, '+' slight overweight, '+ +' maximum overweight; arrows show change from last quarter.

Across regions, the current positioning of the Asia Pacific strategy is to be overweight on Asia ex-Japan, Australia and New Zealand. The position is funded from an underweight position in Japan. This is a result of bottom-up securities selection and does not necessarily reflect a view on the respective regions.

For example, the overweight position in Asia ex-Japan is due mainly to the relative attractiveness of Indonesia and India financials against the rest of the region. Similarly, the underweight position in Japan reflects our concern on the operating prospects of Japanese financial and material companies.

ASIA EX-JAPAN EQUITY

COUNTRY ALLOCATION	--	-	N	+	++
China	○	○	●	◄	○
Hong Kong	○	●	○	○	○
India	○	○	●	○	○
Indonesia	○	○	○	●	○
South Korea	○	○	○	●	○
Malaysia	○	►	●	○	○
Philippines	○	►	●	○	○
Singapore	○	○	●	○	○
Taiwan	○	●	○	○	○
Thailand	○	○	○	●	○

Notes:
The weights are relative to the benchmark – MSCI Asia ex-Japan Index.
'- -' denotes maximum underweight, '-' slight underweight, 'N' neutral, '+' slight overweight, '+ +' maximum overweight; arrows show change from last quarter.

SECTOR ALLOCATION	--	-	N	+	++
Consumer Discretionary	○	●	◄	○	○
Consumer Staples	○	○	●	○	○
Energy	○	►	●	○	○
Financials (Ex Re)	○	○	●	◄	○
Real Estate	○	○	●	○	○
Healthcare	○	○	●	○	○
Industrials	○	●	○	○	○
Information Technology	○	○	○	●	○
Materials	○	●	◄	○	○
Telecommunications Services	○	○	●	○	○
Utilities	○	○	○	●	○

Notes:
The weights are relative to the benchmark – MSCI Asia ex-Japan Index.
'- -' denotes maximum underweight, '-' slight underweight, 'N' neutral, '+' slight overweight, '+ +' maximum overweight; arrows show change from last quarter.

The outlook for growth in Asia remains challenging due to the slowdown in China. Expectations for the US Fed to resume rate hikes in the second half of 2016 (2H16) could present headwinds for Asian currencies. Although inflation remains low, central banks will have less room to cut interest rates as the risk to currency stability and capital outflows need to be balanced against growth concerns.

China remains in a conundrum of rising debt and slower growth. There have been marginal improvements in economic data but it remains to be seen whether the recovery is sustainable. We continue to stay cautious on China's economy but expect growth to stabilise as a result of earlier monetary loosening, government spending and a property market pick-up. Structural challenges in terms of overcapacity and high debt levels remain, but on a positive note, we see that economic rebalancing is accelerating.

We have reduced our position in China to neutral. We are also underweight on Hong Kong due to the challenging outlook for the property sector, which faces the headwinds of a slowing China and potentially higher interest rates. In Taiwan, we are more constructive on the technology sector due to improving inventory and product cycles. We are overweight on Indonesia as we expect lower interest rates to flow through to increased spending and investment. We are also more optimistic on India as moderate inflation and rising incomes could boost consumption.

Asian equity valuations are currently attractive at around one standard deviation below the mean level on a price-to-book basis – a level that was last seen during the 2008 Global Financial Crisis.

Asia's mostly favourable demographic trends and rising incomes underpin the long-term fundamental growth potential of the region, making it an attractive investment destination. We see investment opportunities in niche segments relating to the new economy. Rising internet and smartphone penetration will accelerate technological disruption across various sectors including retail, financial services, travel and transportation. This trend presents bottom-up investment opportunities across the whole ecosystem of e-commerce including information technology services and financial technology sectors.

ASEAN EQUITY

COUNTRY ALLOCATION	--	-	N	+	++
Singapore	○	○	▶	●	○
Malaysia	○	●	○	○	○
Indonesia	○	○	○	▶	●
Thailand	○	●	◀	◀	○
Philippines	○	●	○	○	○

Notes:
The weights are relative to the benchmark – MSCI South East Asia Index.
'- -' denotes maximum underweight, '-' slight underweight, 'N' neutral, '+' slight overweight, '+ +' maximum overweight; arrows show change from last quarter.

In ASEAN, domestic demand continues to be the primary driver for growth as external demand remains weak. In the early part of the year, the strength of the USD had moderated, removing a headwind for ASEAN currencies and allowing central banks room to ease monetary policy. Going into 2H16, we think ASEAN markets could see increased volatility as expectations rise for the US Fed to resume rate hikes.

The ASEAN strategy is most overweight on Indonesia where the market has corrected to attractive levels and we expect lower interest rates to translate into increased spending and investment. The passing of the Tax Amnesty Bill could boost confidence.

We have raised Singapore from neutral to overweight. Despite the global growth slowdown and oil price volatility posing risks to the economy, valuations are supportive and we think the government has policy tools to support growth. The strategy has reduced the overweight position in Thailand after the market's strong performance over the last six months as we expect the country's economic outlook to moderate in 2H16.

We remain underweight on Malaysia overall due to near-term headwinds from disappointing corporate earnings. However, we expect a recovery in oil prices to bolster the economy and ease pressure on the currency. In the Philippines, political conditions have stabilised after President Duterte's strong win. Economic fundamentals remain robust, however, we view valuations as expensive.

FIXED INCOME STRATEGY

GLOBAL FIXED INCOME

FIXED INCOME	--	-	N	+	++
DEVELOPED	○	●	○	○	○
DM Government	●	○	○	○	○
DM Credit	○	●	○	○	○
EMERGING	○	▶	●	○	○
EM Government	○	○	●	○	○
EM Corporate	○	▶	●	○	○
EM Local Currency	○	●	○	○	○
Duration	○	○	●	○	○
Yield Curve*	○	○	●	○	○
Asia	○	○	●	○	○
Latin America	○	○	●	○	○
CIS/EE	○	○	●	○	○
Middle East/Africa	○	○	●	○	○

Notes:
The weights are relative to the appropriate benchmark(s).
'- -' denotes maximum underweight, '-' slight underweight, 'N' neutral, '+' slight overweight, '+ +' maximum overweight; arrows show change from last quarter.
*'+' denotes Steepener and '-' denotes Flattener.

Our overall fixed income strategy is to stay defensive. In the developed regions, we remain underweight on government debt as we view them to be expensive. We are generally positive on investment grade (IG) corporate credits for carry while keeping duration neutral compared with the benchmark. We remain cautious on high yield credits. We also remain defensive and selective in our credit selection.

In the emerging region, we have upgraded our call to neutral. We remain neutral in USD-denominated EM sovereigns and corporate credits. We remain neutral on all EM regions, as we believe performance will be driven largely by country-specific factors. We remain slightly underweight on EM local currency credits selectively.

DEVELOPED MARKETS

Review

After the first rate increase in years in December 2015 by the US Fed, US Treasury bond yields were struggling to rise as risks in the global financial markets were compounded by concerns such as geopolitical tensions, oil price volatility and the health of the Chinese economy. The US Fed March meeting minutes showed that the projections from the Board members for the median Fed funds rate by end 2016 was revised down by 0.5 to 0.9 per cent, compared to earlier projections taken at end-2015. The market's downward revisions of projections in the number of rate hikes this year also kept a lid on the yield curve. The USD weakened before bottoming out in April.

The European Central Bank (ECB) at its March meeting cut the deposit facility interest rate deeper into negative territory by ten basis points (bps) to -0.4 per cent, and also made the decision to include investment grade euro-denominated bonds in the list of eligible assets for regular purchases in the expanded asset purchase programme. A series of targeted longer-term refinancing operations (TLTRO II) will also be launched at a quarterly frequency from June 2016 to March 2017.

Outlook and Strategy

US Fed officials had recently been taking a more hawkish tone in preparing the market for the gradual removal of monetary accommodation in the coming months. Despite this, the US Treasury ten-year yield has traded lower than where it started this year. In the G10 world of diminishing positive-yielding government securities, the US holds the highest weight of around 60 per cent. The US was thus an attractive destination for investors looking for positive returns with large inflows from Japan. We think the inflows and narrowing of spread advantage is likely coming to an end.

We expect the ECB to focus on the implementation of measures announced in March and monitor the market reaction before calibrating further actions. Even before the start of the Corporate Sector Purchase Programme (CSPP) in June 2016, credit spreads of investment grade euro-denominated bonds were declining, with those of CSPP-eligible bonds narrowing more than those which are ineligible. Core European government bond yields also moved lower, creating an easier financing environment in the Eurozone.

The UK electorate's vote by referendum to leave the EU caught the markets off-guard. While there was bearishness priced into the pound prior to the vote, both the pound and euro weakened significantly after the results showed a win for the "Brexit" camp.

Japan has put off the planned consumption tax increase scheduled for April 2017 after considerable delay on fears that the economy is too fragile to withstand any weakening in consumption. Another package of fiscal measures to bolster the economy is expected to be announced later this year. However, the delay is an obstacle in the path towards fiscal consolidation and will test the country's debt sustainability, risking a downgrade to its sovereign rating.

In Canada, the fire-related halt to oil production in Alberta is expected to slow the economy in the second quarter but we expect it to pick up in the third quarter as oil production resumes. With the outlook for the oil price expected to increase gradually – positive for the Canadian economy, the Bank of Canada is expected to hold a neutral stance in monetary policy

The Reserve Bank of Australia unexpectedly cut the cash rate by 25 bps with another reduction of 25 bps this year priced into the futures market. The stabilisation of the labour market did not deter the central bank from easing as the falling inflation into a multi-year low level pushed it into action.

We have a neutral duration call for the G7 government bonds as the diverging but still largely easing bias compresses yields. We have a slight long duration slant for Australian government bonds.

EMERGING MARKETS

Review

Emerging Markets (EM) had a good quarter for the three months to 30 May 2016, as EM bond yields fell from 6.28 per cent to 5.81 per cent. The recovery that had started in early February continued at a strong pace until the middle of April, as the rally stabilised and bond yields traded sideways. We think that a little too much bad news had been earlier priced in and financial markets were oversold – and as the tide subsided, bond prices, equities and currencies staged a recovery.

Outlook and Strategy

Some of the factors that had caused EM bonds to trade poorly in prior periods have faded. An example is oil. Having traded below USD30 per barrel early this year, oil staged a recovery over the past three months, closing near to USD50 per barrel. This has taken the pressure off some EM oil-exporting countries and also lifted the outlook for inflation, avoiding a deflationary scare. Asset prices have been highly correlated with oil of late and thus the bounce helped to lift EM bond prices. Stability in the Chinese currency as well as an injection of stimulus in China also helped to avoid expectations of a collapse in EM growth. Lastly, expectations of interest rate moves by the US Fed have reversed. In the last few months of 2015, the markets were increasingly hawkish, pricing in as much as four 25 basis point rate hikes in 2016. Since February this year, those rate hike expectations have almost completely been priced out as US growth expectations were also reduced.

Looking ahead, we think that further price increases in EM bonds will be limited. While the worst case scenario – a collapse in China and commodity markets, and interest rates hikes – has been avoided, we find little reason for sustained improvements. EM growth is still lacklustre, with no signs of a recovery in trade as global growth remains sluggish at best. Leverage in EM has not decreased which will make growth increasingly precarious over time. As we added risk in early 2016 (with the view that markets were pricing in a little too much bad news), we are now reducing risk in our portfolio, keeping a small positive slant but much closer to neutral.

In a broader context, we like EM bonds for the long term. Over the course of the last decade, we have seen EM bonds recover ever stronger through different economic and financial crises. The asset class has matured and economies are better managed with economic and financial safety buffers at hand to battle global headwinds. Our strategy for 2016 has been to ‘buy the fear’. This asset class trades with global risk sentiment, and being able to buy bonds at attractive prices during a sell-off or correction presents a good opportunity to lock in attractive yields over the long term.

ASIA

Review

Asian hard currency bonds registered a positive year-to-date 2016 return of 4.7 per cent in USD terms, of which the first two months of the second quarter (2Q16) contributed 1.1 percentage points. Unlike the previous quarter where total return was held up by the rally in underlying US Treasuries, the superior performance in 2Q16 was the result of credit spread tightening while UST gave up some of its earlier gains. Overall, positive risk sentiment was the main driver for the tightening in Asian credit spreads during the recent two months.

The market focus this quarter was largely on the trend in oil prices. Despite the failure to reach an agreement to reduce oil output at the Doha Summit in April, oil prices continued to climb higher due to supply outage and talks of oil supply deficit in the next few years. WTI crude oil futures were on a one direction march towards the USD50 per barrel level. The absence of negative macroeconomic news, talk of a US recovery and the stabilisation of the Purchasing Managers' Index (PMI) across Asia also boosted risk sentiment. On top of these, the smaller-than-expected bond issuances had also forced investors to buy the available supply so as to deploy cash. For the first two months of 2Q16, the ten-year UST yield rose by eight bps from 1.77 per cent to 1.85 per cent while the JP Morgan Asia credit composite spread tightened by about 21 bps from 287 bps to 266 bps.

Outlook and Strategy

Although the recent economic data suggests the removal of a hard landing scenario in China or a slowdown in the US, there remain many challenging issues that global central banks need to tackle. Any mishandling may create potential crises which could exacerbate the existing weak global economy. On the corporate front, we expect more negative outlook revisions and defaults especially from industries with excess capacity such as steel and mining. In terms of valuation, Asian credit spreads are back at the levels seen before the sell-off in early August 2015. As at end May, the average Asian credit spread stood at about 266 bps which is about 23 bps narrower than its five-year historical average of 289 bps. At this stretched level, we expect any effort to extend this rally further to be exhausted.

Moving ahead, we are still maintaining our neutral position with a cautious stance as we believe that investors will continue to prefer 'defensive carry' with a consistent focus on credit differentiation. The negative interest rate environment coupled with slow global growth and a lack of inflationary pressures will continue to push investors to search for yield and stay invested in credit bonds. We prefer to hold high single-digit cash levels so as to participate in any near-term sell-off or attractive new issuances.

SINGAPORE

Review

The Singapore economy grew 1.8 per cent year-on-year (yoy) in the first quarter of 2016, unchanged from the previous quarter and in line with advance estimates. In terms of sectors, manufacturing contracted less (negative one per cent), construction picked up (6.2 per cent), while the moderation in services (1.4 per cent) was attributed to wholesale trade. Headline inflation stayed negative for the 18th consecutive month in April 2016 and came in at negative 0.5 per cent whereas core inflation edged up to 0.8 per cent. The Singapore Dollar (SGD) ended the month of May 2016 at 1.3777, weakening 2.5 per cent from end-April on the back of broad USD strength against most Asian currencies.

The SGD corporate bond primary market picked up in March (after the lull in January and February) with the pipeline dominated by REITs, property developers and financial issuers. There were also foreign regulatory capital issuances, such as from ABN Amro Bank, Societe Generale, National Australia Bank, and even Manulife Financial Corp. The supply was much welcomed by investors and post-secondary performance of these new issuances was strong as unallocated investors continued to add to positions.

Outlook and Strategy

The Ministry of Trade and Industry maintained the 2016 growth forecast for Singapore GDP at one to three per cent. Downside risks remain due to softening economic conditions, continued sluggishness in global trade and moderate growth in services. The Monetary Authority of Singapore expects headline inflation to remain negative throughout 2016 and average negative one to zero per cent for the whole year. Core inflation is expected to pick up gradually over the course of the year and will likely be in the lower half of the 0.5 to 1.5 per cent forecast range. However, the increase in core inflation will be mild, given the weak external price outlook, subdued economic growth prospects and a reduction in labour market tightness.

On the currency front, we expect SGD to remain in the lower half of the SGD Nominal Effective Exchange Rate (NEER) policy band on the back of softer economic fundamentals. As we continue to expect the SGD to weaken, short-end interest rates will rise as investors demand higher interest rates to compensate for a weaker currency. Therefore, we continue to be underweight on the short end of the Singapore Government Securities (SGS) curve and remain neutral on the long end.

After a flurry of new SGD bond issuances since March, we expect supply to moderate in June during the summer break. Nevertheless, we expect issuers to tap the market opportunistically on the back of improved risk sentiment and to possibly front-load issuance in anticipation of a US rate hike in the second half of 2016. In addition, we are likely to see more foreign issuers tapping the SGD bond market as they seek diversification for their funding needs.

COMMODITIES STRATEGY

COMMODITIES	--	-	N	+	++
Agriculture	○	○	●	○	○
Base Metals	○	●	◄	◄	○
Bulk Commodities	●	◄	○	○	○
Energy	○	○	►	●	○
Gold	○	○	○	●	○

Notes:
The weights are relative to the appropriate benchmark(s).
'- -' denotes maximum underweight, '-' slight underweight, 'N' neutral, '+' slight overweight, '+ +' maximum overweight; arrows show change from last quarter.

Overview

We move to a slight underweight position for the overall commodities sector. The decision by the US Fed to delay further US interest rate increases caused the USD to weaken in 1H16. This was beneficial for the commodity sector, given the strong negative correlation between commodity prices and the USD in recent quarters. Sentiment was also helped by supportive policy action in China, an improvement in Chinese economic data, as well as sizeable fund inflows into Chinese commodity futures. However, improving US economic data has increased the probability that the US Fed will raise interest rates again in the coming quarter, triggering an upward move in the USD. This, together with the probability of a normal seasonal downturn in Chinese economic data, could create short-term headwinds for the commodity sector. Some near-term price volatility can also be expected as investors focus on demand concerns stemming from lacklustre industrial production (IP) and manufacturing PMI data. While cautious on immediate prospects, we note that continued supply curtailments point to a sustainable recovery in commodity prices over the medium term.

Agriculture

We remain at a neutral weight on agriculture commodities. Grain prices have been relatively stable in recent months, in the absence of any weather events. This supports the argument that grain prices are close to bottoming. As previously noted, analysts estimate that corn, wheat and soybean prices are close to average production costs, even after factoring in lower energy costs and other input reductions. While the 2015-16 El Niño weather event has now ended, this creates the potential for a La Niña event, producing reduced rainfall in North and South America. Brazil, Argentina and the United States are all major soybean producers, and soybean prices will strengthen if there is below average rainfall. This would also be positive for Crude Palm Oil (CPO) prices, given that CPO is the main substitute product for soybean.

Base Metals

We move to a slight underweight on base metals given the probability of seasonally weaker demand in the coming quarter. Near-term supply has also been unusually buoyant for some metals, with significantly lower disruption from weather events, mining problems or industrial action. Capital investment in new production remains at depressed levels, and means future supply growth may lag behind reserve depletion and mine closures. However, these medium-term factors are unlikely to produce high prices in the coming quarter.

Bulk Commodities

We continue to hold an underweight position in bulk commodities. The strong rebound in iron ore and steel prices in the early part of this year was driven by restocking, but pricing is already starting to roll over. New low-cost iron ore production continues to enter the market from Australia and Brazil, and should put downward pressure on prices in 2H16. The recent law suit filed by US Steel against Chinese steel producers is a potential concern, since this will allow investigation of both direct shipments into the United States, as well as possible transhipments via other countries. This could potentially put downward pressure on Chinese steel production, and reduce demand for steel input materials. High production levels and environmental pressure continue to depress thermal coal markets.

Energy

We move to a slight overweight position in energy. There are increasing signs that the supply-demand balance for crude oil is moving back to neutral, from the oversupplied conditions that existed in early 2016. Supply data is becoming more supportive as US onshore domestic oil production continues to fall, with aggregate non-Organization of the Petroleum Exporting Countries (OPEC) production now expected to decrease in both 2016 and 2017. There have also been press reports that the new Saudi Minister of Energy, Industry & Mineral Resources Khalid Al-Falih and Deputy Crown Prince Mohammad bin Salman are targeting a crude oil price of approximately USD60 per barrel, in order to support the potential privatisation of key Saudi energy assets. Global demand continues to grow, with the US now into its summer driving season, which typically results in elevated levels of gasoline consumption.

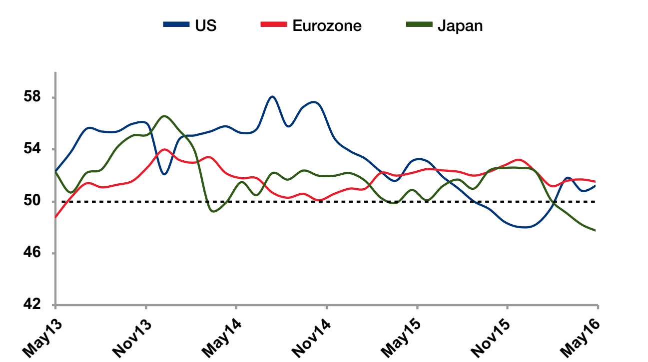
Gold

We remain in an overweight position in gold despite the possibility of higher US interest rates and an upward movement in the USD. The upward trend in US inflation rates suggests that US real rates may stay negative, even with a rate increase of 25 bps. The gold price is also being supported by continued gold exchange-traded fund (ETF) inflows, with aggregate gold ETF holdings close to 2,000 tonnes, some 30 per cent higher than at the start of 2016. The surprise result of the UK referendum to leave the EU also raised risk aversion, boosting demand for gold. The strong gold ETF inflows suggest nervousness among investors, given ongoing problems with the EU and political uncertainty in the run-up to the US presidential election in November 2016. Central banks remain the aggregate net buyers, with the People's Bank of China (PBoC) and Russia's central bank making sizeable official gold purchases for eleven consecutive months. Retail demand from China and India is also at record levels.

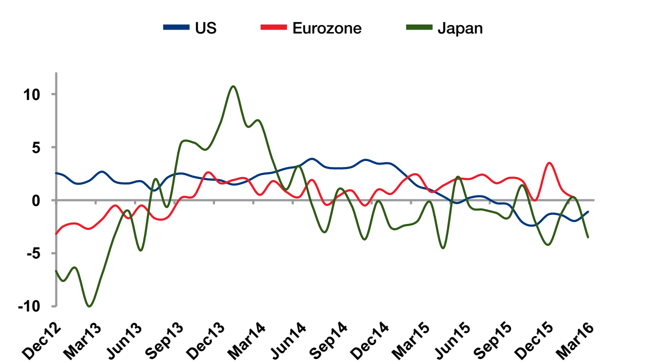
APPENDIX
ECONOMIC INDICATORS

DEVELOPED ECONOMIES

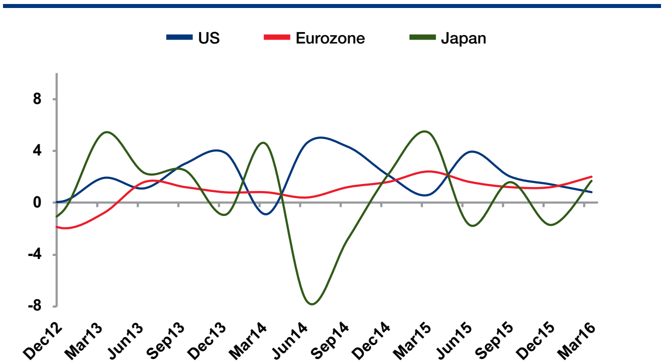
Purchasing Managers' Index



Industrial Production Growth (YoY%)

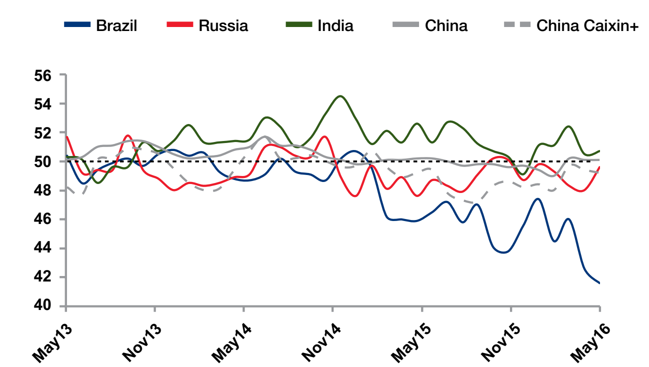


Real GDP growth (QoQ%, saar)*

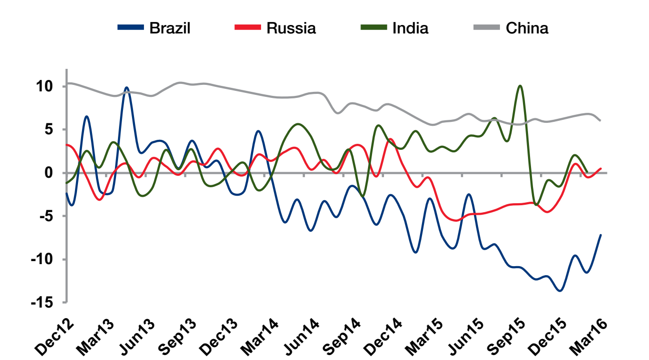


EMERGING ECONOMIES

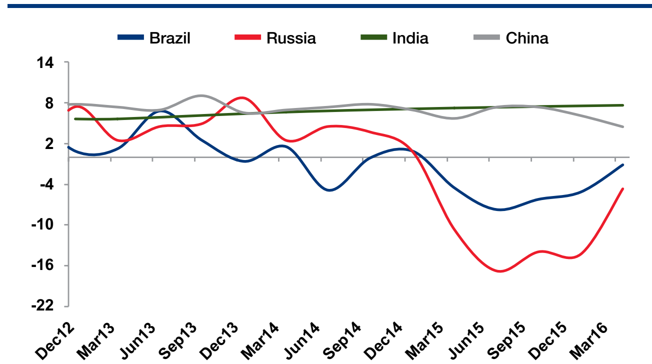
Purchasing Managers' Index



Industrial Production Growth (YoY%)



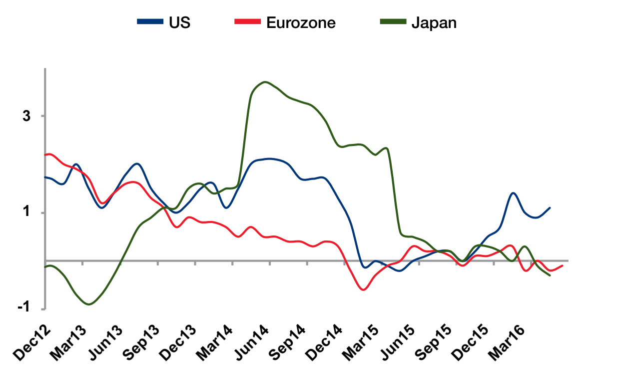
Real GDP growth (QoQ%, saar)*



*For some economies, annualised GDP data are estimates by UOBAM. For India, data are in year-on-year percentages (YoY%).
+ China Caixin PMI was previously known as HSBC PMI (effective July 2015).
Note: All data are sourced from Bloomberg, Datastream and UOBAM unless otherwise stated, as at 6 June 2016.

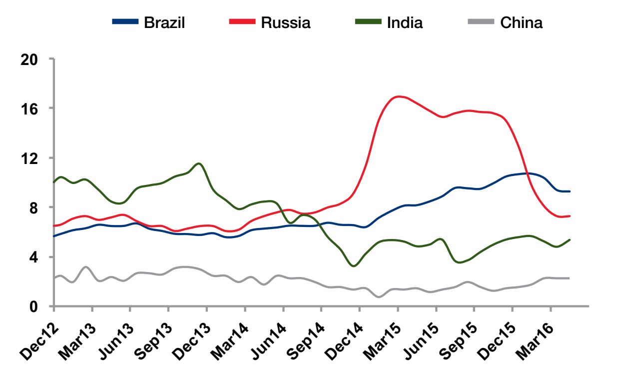
DEVELOPED ECONOMIES

Inflation - CPI (YoY%)



EMERGING ECONOMIES

Inflation - CPI (YoY%)



Note: All data are sourced from Bloomberg, Datastream and UOBAM unless otherwise stated, as at 6 June 2016.

Central Banks Interest Rates

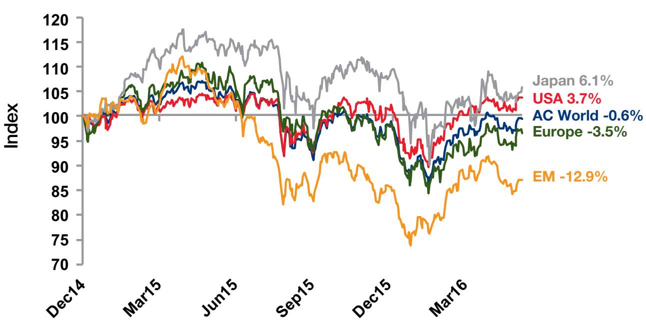
Country	Interest Rate	Current Rate (%pa)	Latest Meeting	Change at Latest Mtg (bp)	Last Change	Next Meeting
		6-Jun-16				
United States	Fed Funds Target Rate US	0.500	27 Apr 2016	—	16 Dec 15 (+25bp)	16 Jun 2016
Eurozone	Refinance Rate	0.000	2 Jun 2016	—	10 Mar 16 (-5bp)	21 Jul 2016
Japan	BOJ Overnight Call Rate	-0.046	—	—	3 Jun 16 (-0.9bp)	—
United Kingdom	UK Official Bank Rate	0.500	6 Jun 2016	—	5 Mar 09 (-50bp)	16 Jun 2016
Brazil	Brazil Selic Target Rate	14.250	27 Apr 2016	—	29 Jul 15 (+50bp)	8 Jun 2016
Russia	Russia Refinancing Rate Announcement	8.250	13 Sep 2013	—	13 Sep 12 (+25bp)	—
India	Repurchase Rate	6.500	7 May 2016	—	6 Apr 16 (-25bp)	—
China	1 Year Benchmark Lending	4.350	6 Jun 2016	—	26 Oct 15 (-25bp)	—
South Africa	South Africa Repo Avg Rate	7.000	6 Jun 2016	—	17 Mar 16 (+25bp)	21 Jul 2016

Source: Bloomberg, updated as of 6 June 2016

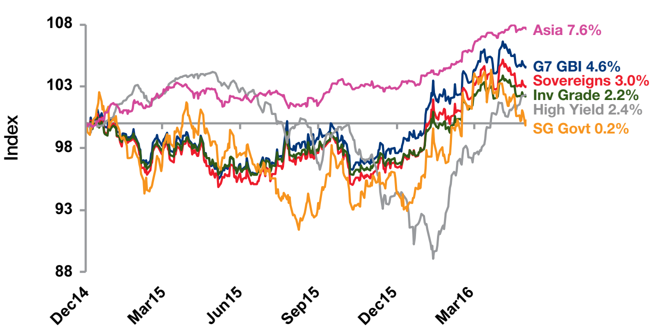
MARKET PERFORMANCE

DEVELOPED MARKETS

Equity Indices
(Rebased 100 on 31 December 2014)



Fixed Income Indices
(Rebased 100 on 31 December 2014)



Commodity Indices
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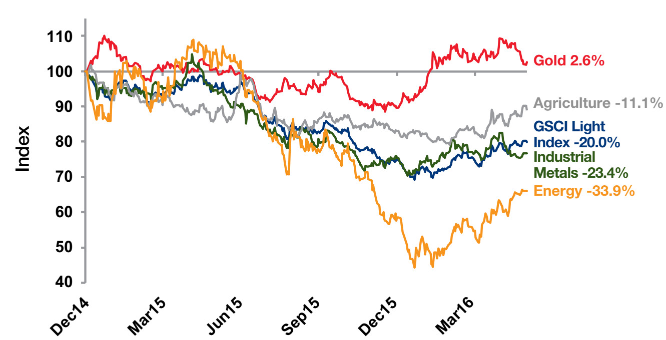
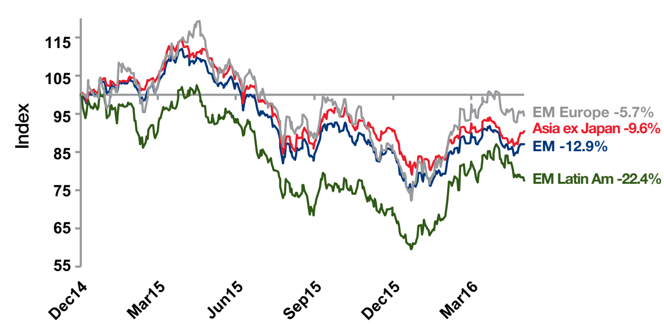
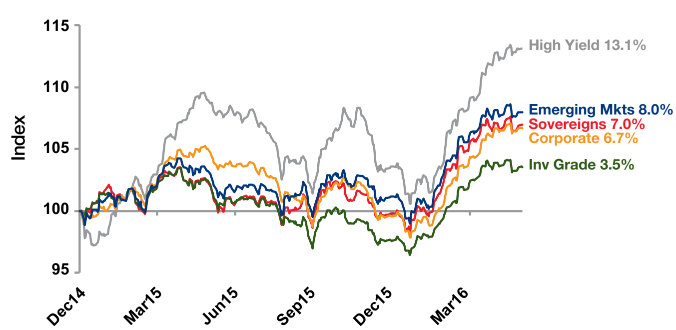


EMERGING MARKETS

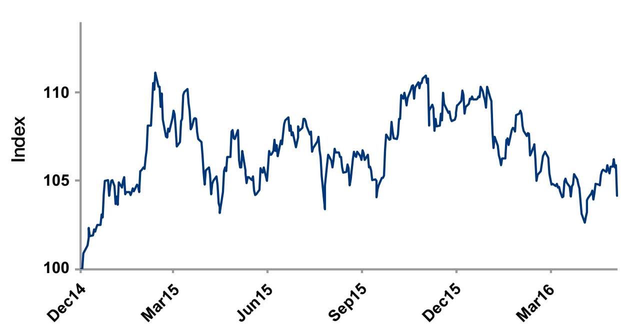
Equity Indices
(Rebased 100 on 31 December 2014)



Fixed Income Indices
(Rebased 100 on 31 December 2014)



Dollar Index Spot
(Rebased 100 on 31 December 2014)

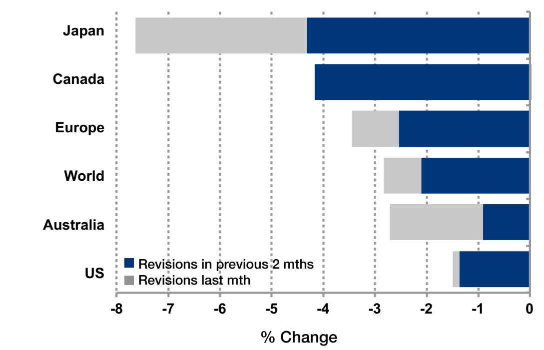


Note: All data are sourced from Bloomberg, Datastream and UOBAM unless otherwise stated, as at 6 June 2016.

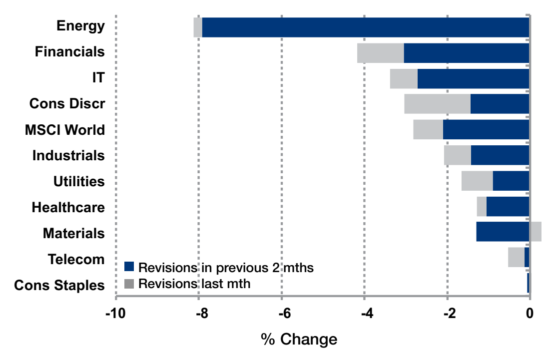
EQUITY MARKET INDICATORS

DEVELOPED MARKETS

Earnings Revision by Regions for FY2

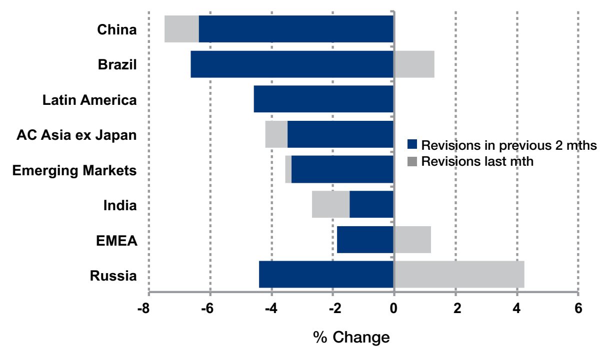


Earnings Revision by Sectors for FY2

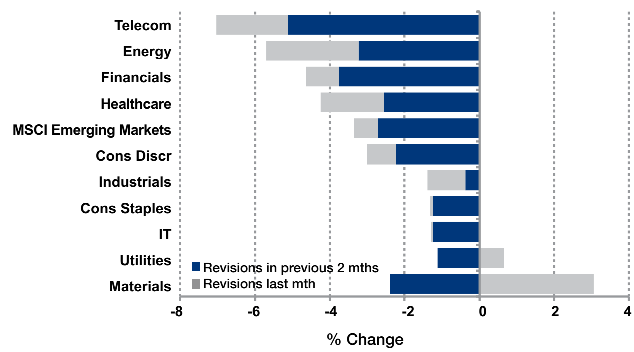


EMERGING MARKETS

Earnings Revision by Regions for FY2



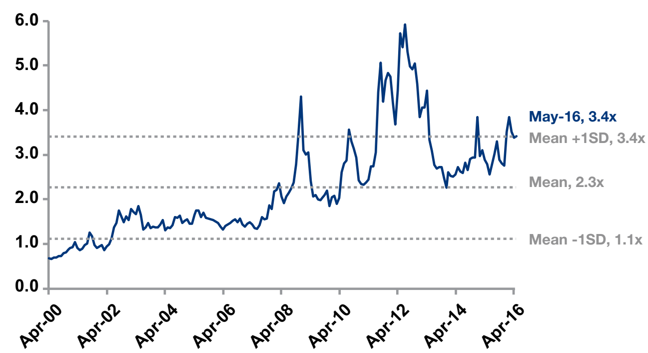
Earnings Revision by Sectors for FY2



Note: All data are sourced from Bloomberg, Datastream and UOBAM unless otherwise stated, as at 6 June 2016.

VALUATION

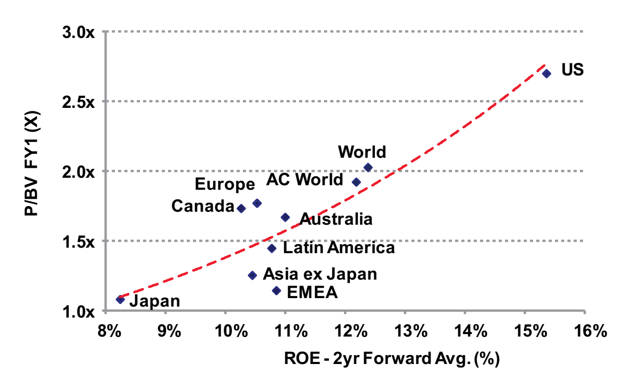
Developed Markets Earnings Yield Ratio*



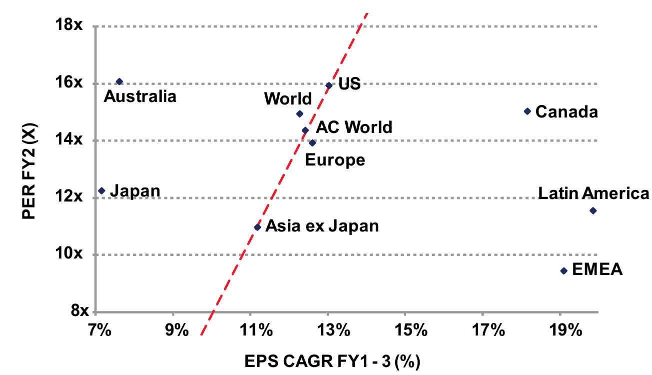
*Mean and SD are based on data from 1999.

Emerging Markets Earnings Yield Ratio*

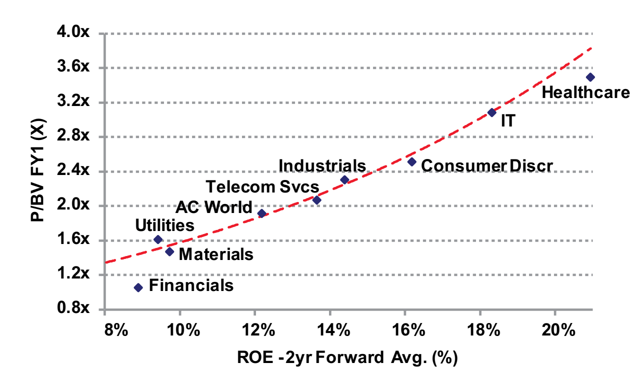
P/BV vs ROE by Region



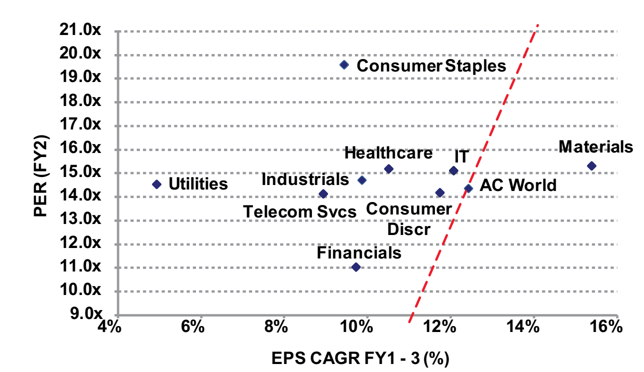
P/E vs Growth by Region



P/BV vs ROE by Sector



P/E vs Growth by Sector^



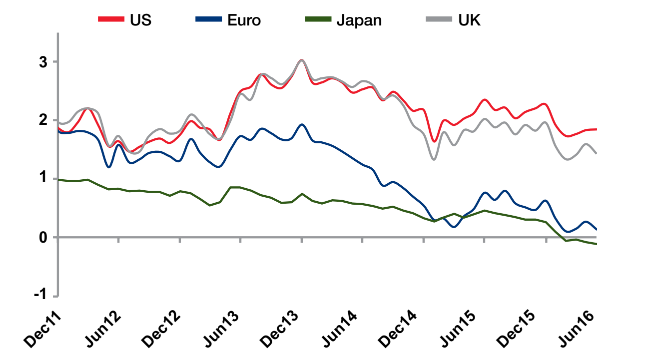
^Energy sector is not shown in the chart.

Note: All data are sourced from Bloomberg, Datastream and UOBAM unless otherwise stated, as at 6 June 2016.

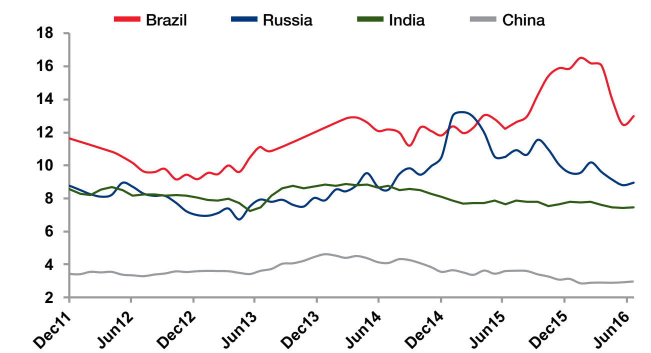
FIXED INCOME MARKET INDICATORS

SOVEREIGN

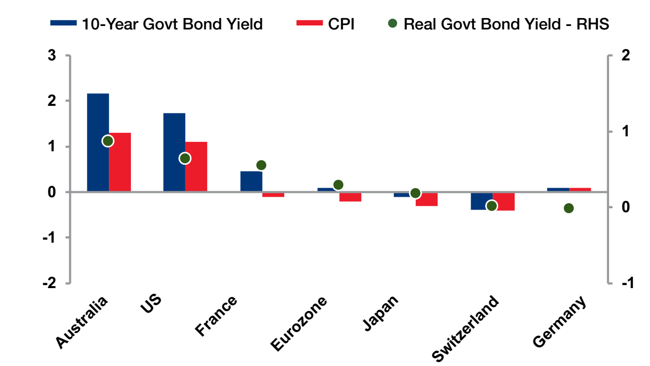
Developed Markets 10-Year Government Yield (%)



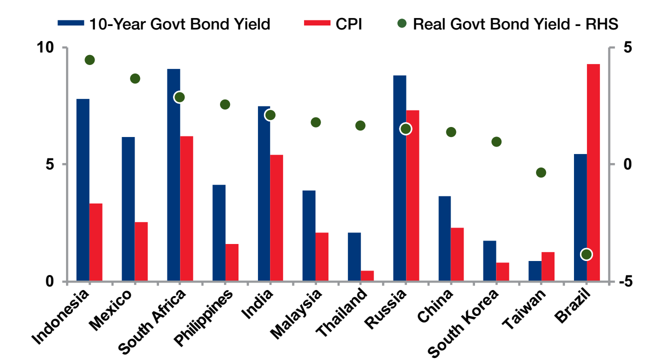
Emerging Markets 10-Year Government Yield (%)



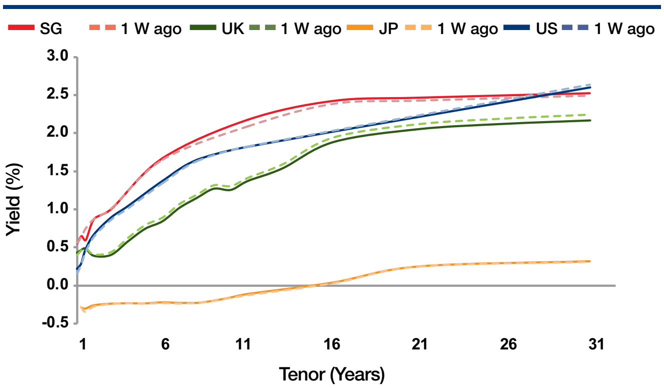
Developed Markets Real Government Yield (%)



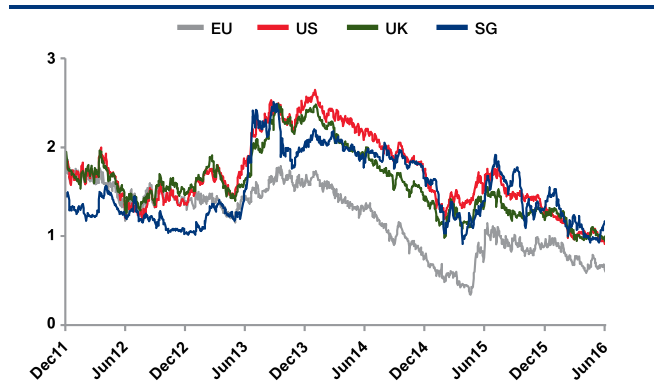
Emerging Markets Real Government Yield (%)



Nominal Yield Curve (%)



Yield Curve Steepness (10Y – 2Y) (%)

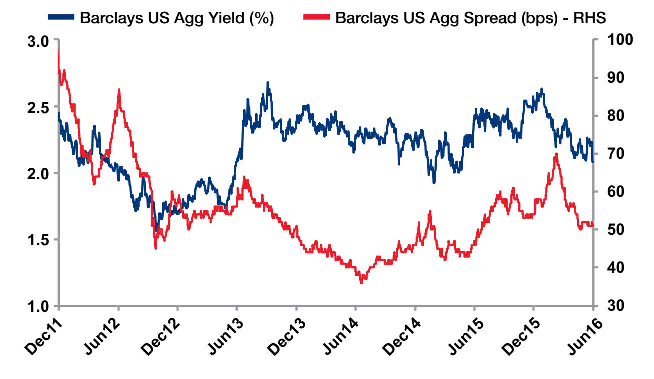


Note: All data are sourced from Bloomberg, Datastream and UOBAM unless otherwise stated, as at 6 June 2016.

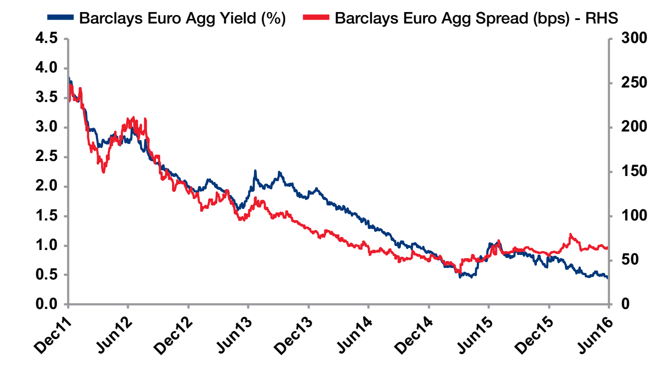
FIXED INCOME MARKET INDICATORS

CREDITS

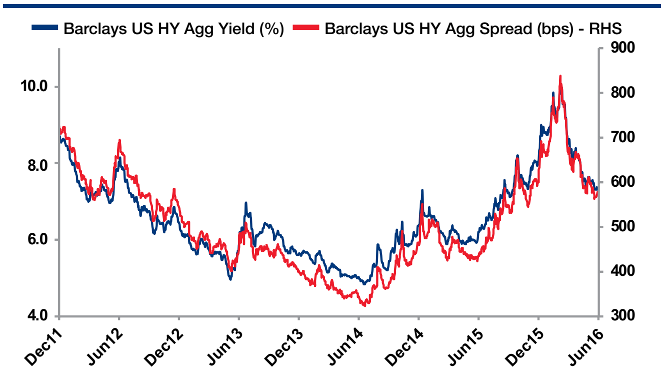
US Markets (USD) Yield and Credit Spread



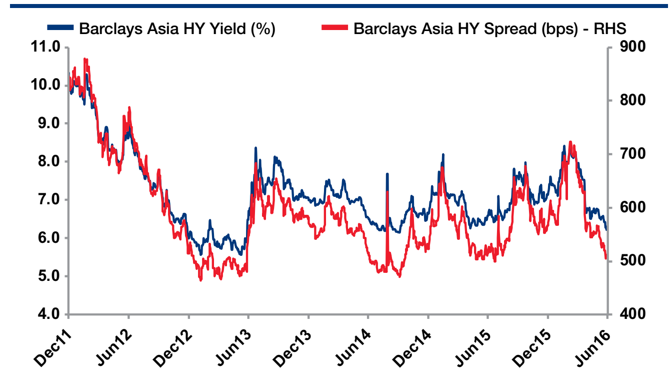
Euro Markets (USD) Yield and Credit Spread



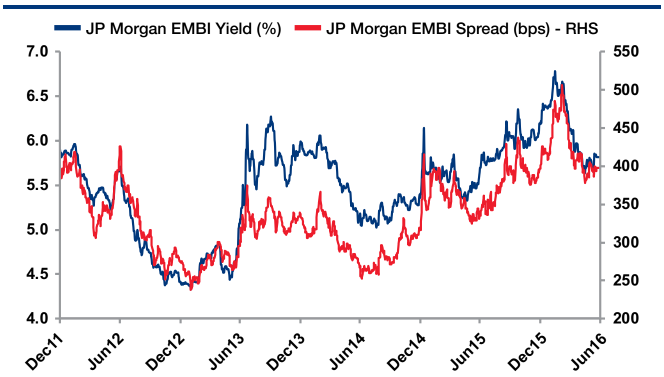
US Markets (USD) HY Yield and Credit Spread



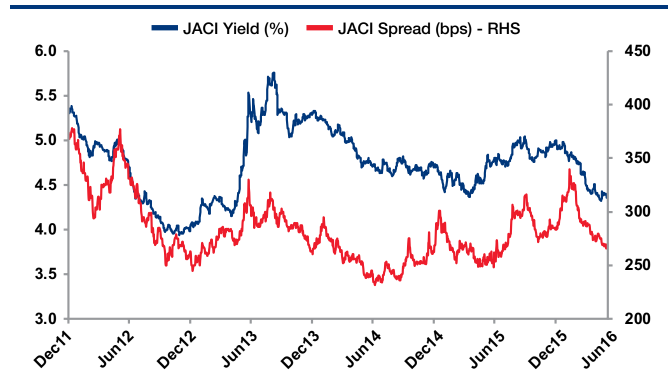
Asia Markets (USD) HY Yield and Credit Spread



Emerging Markets (USD) Yield and Credit Spread



Asia Markets (USD) Yield and Credit Spread



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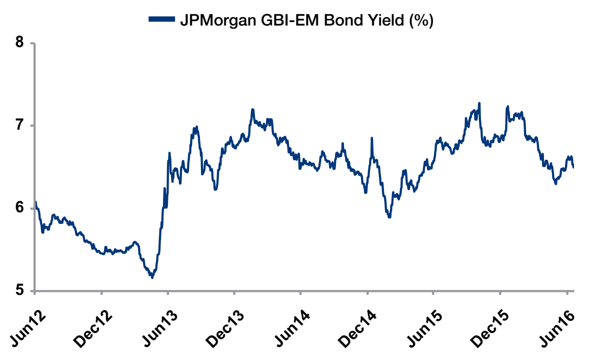
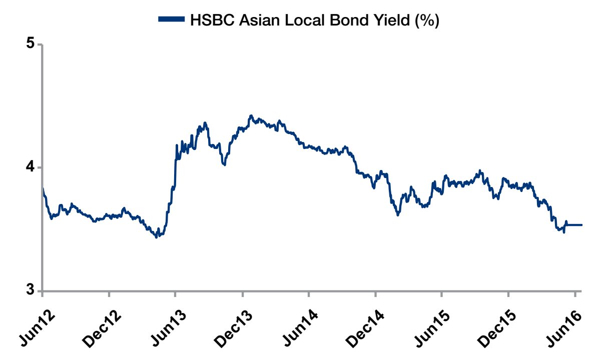
CREDITS

Emerging Markets (Local Currency) Bond Yield

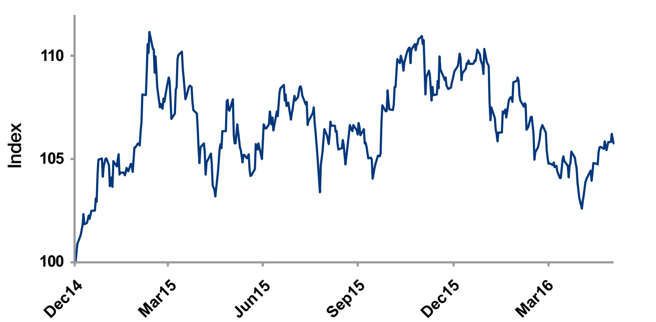


Asia (Local Currency) Bond Yield

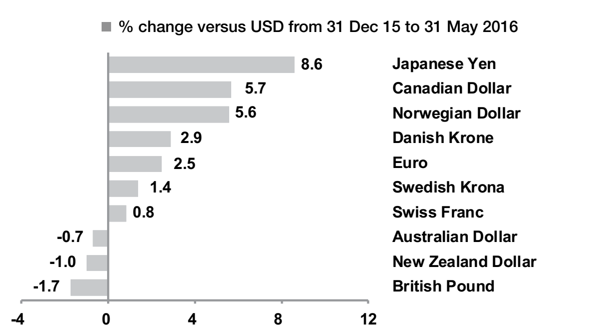


CURRENCIES

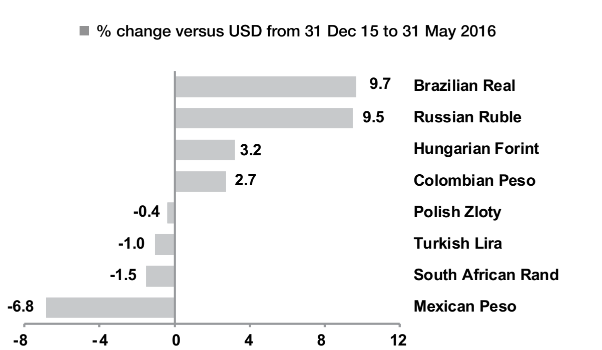
Dollar Index Spot (Rebased 100 on 31 December 2014)



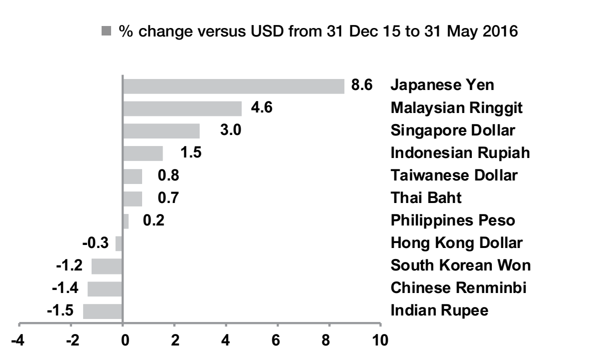
G-10 FX against US Dollar



Emerging Markets FX against US Dollar



Asia FX against US Dollar



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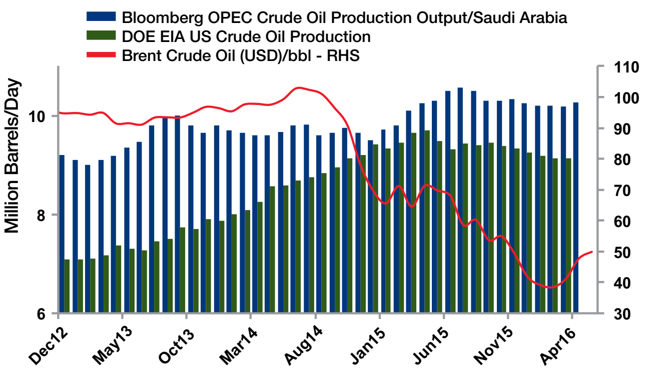
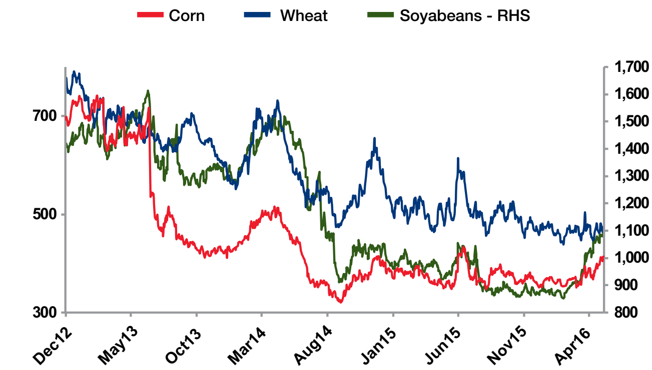
COMMODITY MARKET INDICATORS

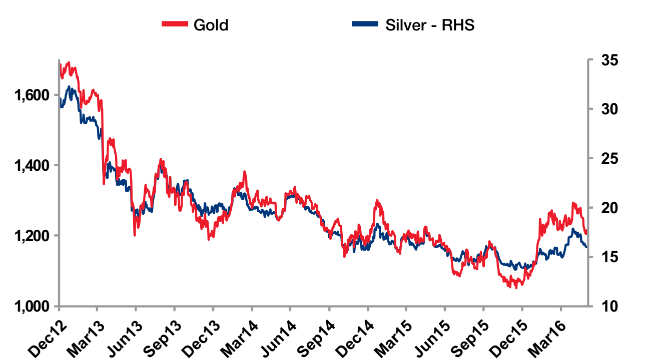
Brent Crude Oil Price and Production



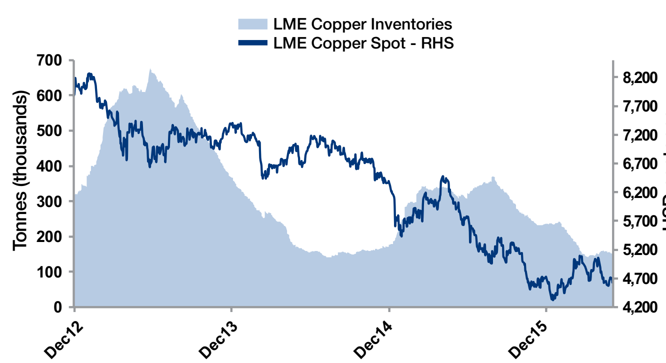
Agriculture Price (USD)



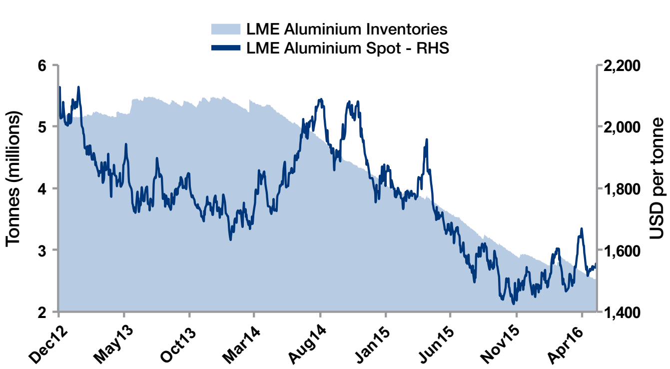
Precious Metal Price (USD)



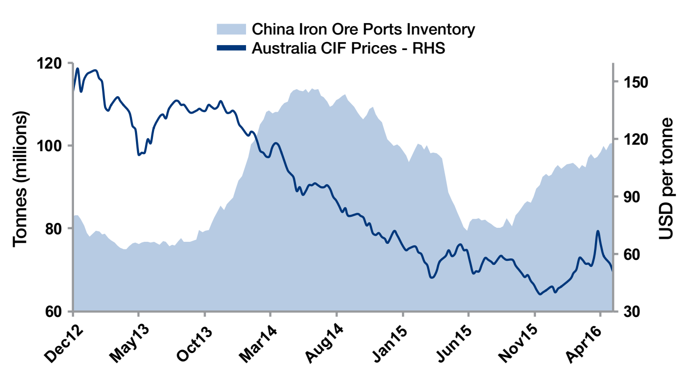
Copper Price (USD)



Aluminum Price (USD)



Iron Ore Price (USD)



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UOB Asset Management Ltd Co. Reg. No. 198600120Z