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VIDEO TRANSCRIPT

2016 FIXED INCOME OUTLOOK

MODERATE VALUE AMIDST SPECTRE OF RATE HIKES

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Q1. In your view will the Federal Reserve still raise interest rates and how will it affect your outlook going into 2016?

If you recall, this time last year, markets were pricing in a Federal Reserve ‘lift-off’ in the third quarter of 2015 and our expectations were for a 25bps hike in the fourth quarter of this year.

We see this as a distinct possibility for December although this is a difficult call as 2015 as you would know, has been a year of volatility and general pessimism. Worries of an emerging market growth crisis have been the focus of financial market attention, and this was exacerbated by a number of China’s policy missteps in an effort to maintain market stability, particularly, stock market stability.

As for Latin America, there was great concerns amid the downward spiral of commodity prices and also, as you know, in countries like Brazil, there was deteriorating country fundamentals.

Such considerations would have been on the minds of the Federal Reserve when they decided to leave policy on hold in September; global factors and downward pressures on inflation were cited as their near term concerns. While we note the prevailing bearish market sentiments, we are inclined to take a more optimistic view.

US economic growth has been on a moderate upward trajectory with diminishing labor market slack, and steady improvements in consumer sentiment and as well as, in the domestic housing market. Eurozone economies have also been expanding at a fairly healthy clip as you can see from the rising Purchasing Manager's Index (PMI).

In emerging market Asia, concerns have been mainly over the outlook for China. We anticipate that the ongoing stabilisation of China’s property market, the government pursuing a moderately expansionary fiscal policy and consumer spending holding up well would enable the economy to see growth strengthening into 2016.

In this environment of a moderate global recovery, the Federal Reserve, we feel, can afford to pick up the pace of its tightening in 2016, although the gradient of rate increases is likely to be fairly moderate.

Against this benign macro backdrop, Asian bond markets should be able to mitigate the negative impact of measured rate increases albeit with some near term volatility, this is because it is helped by attractive bond carry.

Q2. What do you see as the main risks and opportunities for Asian bonds in the new year?

We view a sharp deceleration in global growth as a potential key risk, which could result in severe market volatility for emerging market and Asian assets. What have been ailing global capital markets in 2015, particularly for emerging market, has been the weak oil and commodity price outlook.

Depressed energy prices, we feel, cannot be sustained for an extended period as these cheap levels should invigorate consumption. If our expectations for a moderate global recovery come to pass, we should see global growth strengthening further which will lead to a potential turnaround in commodity prices.

This could usher then, a 6 -12 month period where Asian emerging market bond markets and currencies see a period of recovery from the battering it took in 2015. Apart from global bond carry, gains in Asia local currency bond markets could be supported by better currency performance. Asia currency valuations have significantly improved following the steep corrections seen this year.

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In Asia, hard currency bonds also offer value because credit spreads have widened in the third quarter of 2015. And this would bring about good opportunities for investors.

A hard landing in China is often seen as another key worry, but as I've mentioned, this is not our central view. Overall, Asia continues to be well-placed in terms of macro fundamentals relative to the rest of the emerging markets, and they will benefit from a moderate global growth backdrop.

Nevertheless, return expectations need to be weighed against the impact of a less favorable interest rate cycle in the US. Fragilities do remain in the region and close attention to their developments is warranted to assess their impact on our base-case scenario.

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