Singapore Market Focus
Singapore Monthly

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DBS Group Research . Equity

9 Jan 2019

Handshake or cold stare?

- STI rangebound at 2960-3190 pending outcome of US-China trade talks
- Adding a Bull-case scenario of STI at 3500
- Transiting to mid-contraction phase - SembCorp Industries, Netlink
- S-REITs still in favour as FED turns dovish - CMT, MCT, MLT, FLT MAGIC
- Sticking to defensives - ST Engineering, Yangzijiang, ComfortDelgro, CMT, MLT, Netlink Trust, UOB

US-China trade talks in focus this month. With the 90-day truce approaching the halfway mark, attention is on the outcome of the mid-level US-China trade talks this week and possibly another between Trump and the Chinese Vice President at the World Economic Forum on 22-25 January. We see rangebound trade for the STI at between 2960 and 3190 pending the outcome of these events.

Adding a Bull-case scenario to the Base and the Bear. A more dovish FED and the possibility (albeit small now) that the US-China trade war could end, have led us to consider a third bull case in addition to our base (still our preferred) and bear scenarios. Our bull case calls for STI recovery to 3500 pegged to 12.6x (-0.5SD) FY20F PE if the following conditions are met (1) US-China trade tariff stops/reverses, (2) FED hikes rates just once or none this year, (3) Asian currencies see their lows against the USD.

Transiting to mid-contraction phase. These signs are telling us that the economy is about to transit from the early contraction (started in 2H18) to mid-contraction phase (i) consumer staples and telco outperformed since 3Q18, (ii) commodity prices (CRB Index) tumbled 15.4% in 4Q18. Utility sector tends to outperform during mid-contraction phase. Our picks are **SembCorp Industries** and **Netlink Trust**.

S-REITs remain in favour as FED turns dovish The sector should continue to garner investors' interest as bond yields stay pressured by the FED turning more dovish. Sector yield spread of 4.2% is above the 10-year average of 3.8%. Giving the uncertain macro growth environment, we prefer the more resilient retail and industrial (warehouse and business parks) sub-segments given their domestic focus and relatively stickier demand respectively. Our picks are **CMT**, **MCT**, **MLT**, **FLT** and **MAGIC.**

Sticking to defensives We continue to adopt a more guarded stance as more companies could sound the caution bell at the upcoming the FY results season and the earnings recession trend may extend for at least two more quarters. We continue to prefer stocks with earnings visibility as well as yield plays with growth. Our picks are **ST Engineering**, **Yangzijiang**, **ComfortDelgro**, **CMT**, **MLT**, **Netlink Trust** and **UOB**.

STI : 3,122.94

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Key Indices

	Current	% Chng
FS STI Index	3,122.94	0.6%
FS Small Cap Index	335.09	0.4%
SGD Curncy	1.35	-0.8%
Daily Volume (m)	1,295	
Daily Turnover (S$m)	865	
Daily Turnover (US$m)	642	

Source: Bloomberg Finance L.P.

Market Key Data

(%)	EPS Gth	Div Yield
2018	7.6	4.4
2019F	7.2	4.5
2020F	6.7	4.2

(x)	PER	EV/EBITDA
2018	13.9	14.2
2019F	12.9	13.6
2020F	12.1	13.1

STOCKS

	Price S$	Mkt Cap US$m	12-mth Target S$	Performance (%) 3 mth	12 mth	Rating
CapitaLand Mall Trust	2.32	6,298	2.44	7.9	10.5	BUY
Mapletree Commercial Trust	1.71	3,637	1.80	6.9	2.4	BUY
Mapletree Logistics Trust	1.30	3,434	1.50	6.6	(3.7)	BUY
Frasers Logistics & Industrial Trust	1.04	1,544	1.20	0.0	(10.9)	BUY
Mapletree North Asia Commercial Trust	1.16	2,705	1.45	2.7	(7.9)	BUY
Sembcorp Industries	2.65	3,482	3.70	(12.0)	(16.1)	BUY
NetLink NBN Trust	0.78	2,224	0.87	(1.3)	(7.2)	BUY
ST Engineering	3.55	8,155	4.15	(0.3)	6.3	BUY
Yangzijiang	1.27	3,694	1.82	0.8	(15.9)	BUY
ComfortDelGro	2.17	3,459	2.56	(8.4)	6.4	BUY
UOB	25.17	30,886	29.50	(3.2)	(6.5)	BUY

Source: DBS Bank, Bloomberg Finance L.P.
Closing price as of 8 Jan 2019

DBS
Live more, Bank less

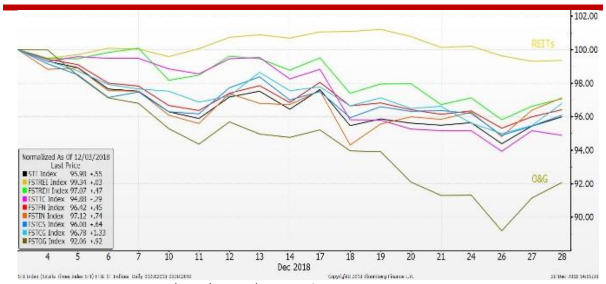
ed: TH/ sa: YM, CW, CS

January Market Outlook

Downbeat December concludes a year to forget

- The Straits Times Index (STI) ended December 2018 down 2.1% on the heels of a larger tumble in US equity market indices and oil price. The STI fell 10% y-o-y, down 16% from its YTD high
- REITs performed the best as US 10-year bond yield fell 22bps to 2.77%
- O&G stocks underperformed amid a near 10% decline in Brent crude to US$53pbl
- Average value of shares on the SGX in 2018 stood at S$1.173bn/day, +2.2% y-o-y

FTSE ST Indices

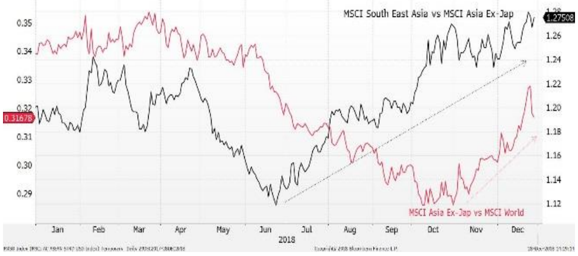


Source: DBS Bank, Bloomberg Finance L.P.

Asia markets outperformed as US stocks slumped

- Asian stocks took the near-10% December decline in the S&P500 Index in their stride → Asian stocks had fallen earlier and trading at a lower valuation
- Asia stock markets outperformed Developed markets since November
- Within Asia, Southeast Asia stock markets have outperformed since July
- US markets trade at 15x (average), Asia Ex-Japan at 11.6x (between -0.5SD and -1SD) and STI at 11.7x (between -1.5SD to -1SD) 12-month forward PE
- Relative outperformance can continue as the FED turns dovish and the USD weakens

Relative strength of World, Asia and South East Asia



Source: DBS Bank, Bloomberg Finance L.P.

US-China trade talks in focus this month

- US delegation to hold mid-level trade talks in Beijing on the 7 January week to discuss trade
- Trump may hold high-level trade talks with Chinese Vice President at the World Economic Forum in Davos from 22-25 January (source: SCMP) → Developments closely watched as 90-day truce ends on 1 March
- We think US equity market's sharp post-Christmas rebound may not sustain as the outcome of trade truce remains uncertain
- FOMC meeting – FED likely to hold rates steady at 2.5%

Key events

Date	Event	Comments
Week of 7 Jan	US-China trade talks in Beijing	US delegation to hold mid-level talks in Beijing on 7 Jan week to discuss trade (source: Bloomberg)
22-25 Jan	World Economic Forum	Trump may hold high-level trade talks with Chinese Vice President (source: SCMP)
29-30 Jan	FOMC meeting	FED is likely to hold rates steady, dot plot points to 2 hikes this year

Source: DBS Bank

Rangebound pending outcome of 90-day truce

- Straits Times Index started 2019 at 3068 or 11.7x (between -1.5 to -1SD) 12-month forward PE
- Conditions currently tilt towards our base-case scenario
  (1) Truce to trade war: 90-day truce ends 1 March
  (2) FED stops at two hikes: Latest dot plot points to two hikes this year (previously three) this year
  (3) Asian currencies stabilise: Bloomberg JPM Asia Dollar Index (ADXY) recovered moderately from 103.2 to 105.2
- January could see rangebound trade between 2960 and 3190

Straits Times Index (Daily)

Source: DBS Bank, Bloomberg Finance L.P

Transiting to mid-contraction phase

- Signs that say the economy is about to transit from early to mid-contraction phase
  (1) Early contraction phase started in 2H18 when the STI began its downtrend
  (2) Consumer staples (e.g. **Dairy Farm, Sheng Siong**) outperformed and telco (e.g. **Starhub, SingTel**) outperformed since 3Q18
  (3) Commodity prices tend to fall sharply – CRB Index tumbled 15.4% in 4Q18
- Utility sector tends to outperform during mid contraction phase (e.g. **SembCorp Industries, Netlink Trust**)

Sector outperformers at various phases of economic cycle

Economic Phase	Sector Outperformers	*Examples	Comments
Late contraction	Financials	UOB, OCBC	1Q 2017 to 3Q 2017
	Property	CityDev, UOL etc.	
	Technology	Sunningdale, Hi-P, Venture	
Early Expansion	Industrials	Yangzijiang	
	Transportation	CAO, SATS, SIAE	
	Construction	Tat Hong, Yong Nam, Lian Beng	4Q 2017 to 2Q 2018
Middle Expansion	Capital Goods	SembCorp Marine	
	Basic Materials	Asia Enterprise, Hupsteel	
Late Expansion	Commodities & Energy	Olam, CPO	
	Consumer staples	Dairy Farm, Sheng Siong	3Q 2018 till current
Early contraction''	Consumer Services	ComfortDelgro	
	Telco	SingTel, Starhub	
Mid contraction	Utilities	SembCorp Industries, Netlink Trust	1Q/2Q 2019 onwards?

* These are examples and do not constitute a recommendation

Source: DBS Bank

Adding a Bull-case scenario to the Base and the Bear

Our base and bear scenarios for the Singapore market this year remain valid with the former being the preferred outcome (refer to report titled '2019 Outlook and Strategy: Pitch on Value' dated 26 November 2018). The following developments in recent weeks have led us to consider a third Bull-case scenario in addition to the prior two:

1. The FED has turned much more dovish – The FED dialled back its 2019 rate hike projection to just two (previous 3-4 hikes) at the December 2018 FOMC meeting. Last Friday, Jeremy Powell raised the odds that rate hikes might pause this year, saying that the FED is not on a pre-set path to raise rates and the committee will be patient to watch how the US economy evolves
2. DBS Research lowers rate hike forecast – Our chief economist also recently lowered his rate hike projections to two from four previously, citing the FED's change of stance.
3. Developments in US-China trade talks – At the G20 summit on 1 December 2018, a 90-day truce was announced. US tariffs on China imports have paused at 10% (previous intention was 25%) on US$200bn of Chinese imports and a further 25% on US$50bn worth of imports pending the outcome of trade talks during this 90-day period. Mid- and high-level talks are expected this month.

Bull case – Low seen at 2850, recovery to 3500

Condition 1: Trade war stops
- US tariffs on China stop at current 25% on US$50bn imports and 10% on a further US$200bn imports
- Added bonus if US-China gradually rolls back tariffs on each other's measures)

Condition 2: FED hikes once or none
- US inflation stable at around 2%
- FED hikes rates once or even none this year, FED funds rate of 2.75% at end-2019
- US 10-yr yield already peaked at 3.25% in 4Q18, stays below 3.1% this year

Condition 3: Asian currencies strengthen
- Asian currencies seen major low in 4Q18, recovers against USD, ADXY (currently 105.6) bottomed at 103.2 in 4Q18
- USDCNY capped below 7, USDSGD peaked at 1.39 in 4Q18

Straits Times Index
- Correction ended at 2955 in late Oct last year at 11.41x (-1.5SD) 12-mth fwd PE
- Recovery towards 3500 pegged to 12.6x (-0.5SD) FY20F PE as trade war halts, fewer rate hikes and Asian currencies recover

Straits Times Index Bull case - Low seen at 2955, recovery towards 3500

Source: DBS Bank

Base case preferred view – Low at 2850, recovery to 3250

Condition 1: Truce to Trade War

- US tariffs on China stop at 25% on US$250bn imports
- US-China trade hostilities do not degenerate into an all-out trade war (i.e. 25% tariffs on all imports upon each other and China introduces qualitative measures)

Condition 2: FED stops at 2, max 3

- US inflation stable at around 2%, upward wage pressure stabilises
- FED hikes rates twice, at most three times next year that lifts the FED funds rate to an anticipated 3.00-3.25% and pauses
- US 10-yr yield peaks at/before 3.6%

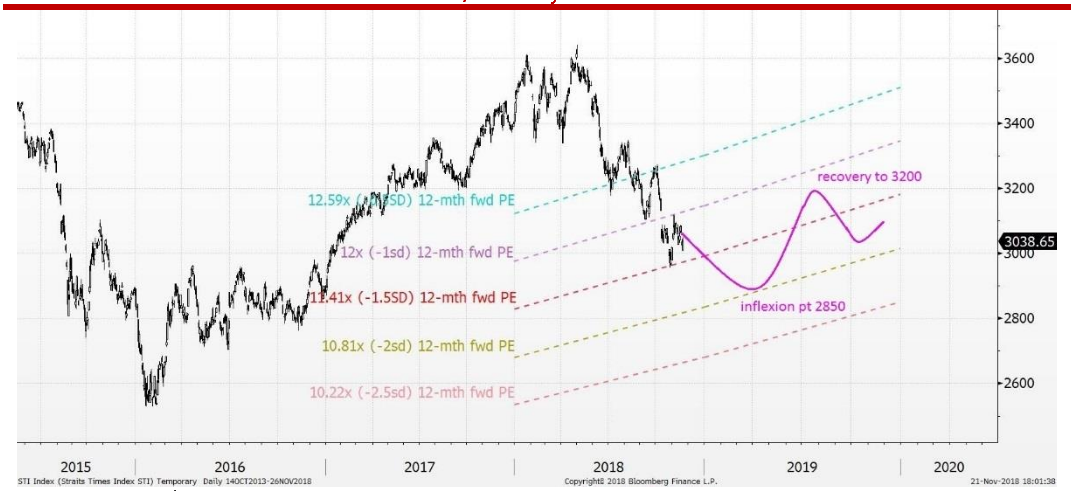
Condition 3: USDCNY peaks at 7.2

- USDCNY does not extend beyond the 7.2 ceiling in 2Q forecasted by our currency strategist
- Subsequent USDCNY pullback sees recovery in Asian currencies, including the SGD

Straits Times Index

- 7% downside from 3050 to an inflexion point at 2850 in CY1Q19 pegged to 10.81x (-2SD) FY19F PE
- Followed by a recovery towards 3250 pegged to 12x (-1SD) blended FY19/20F PE on an oversold valuation trade, attractive yield and investors look beyond trade disruption to diversion

Straits Times Index Base case - Low at 2850, recovery towards 3250



Source: DBS Bank

Bear case – Down to 2600

Condition 1: All-out trade war

- US and China impose 25% tariffs on all imports upon each other
- China further retaliates with qualitative measures, making it harder for US companies to compete in China
- Qualitative retaliation can be more uncertain than tariffs because it is "open-ended"

Condition 2: FED goes 4

- US inflation rises beyond 2.5% driven by upward wage pressure and tariff impact even as global growth slows
- Our Chief economist's above-consensus forecast of 4 rate hikes next year comes true, FED funds rate at 3.5% by end-2019
- US 10-yr yield goes beyond 3.6%

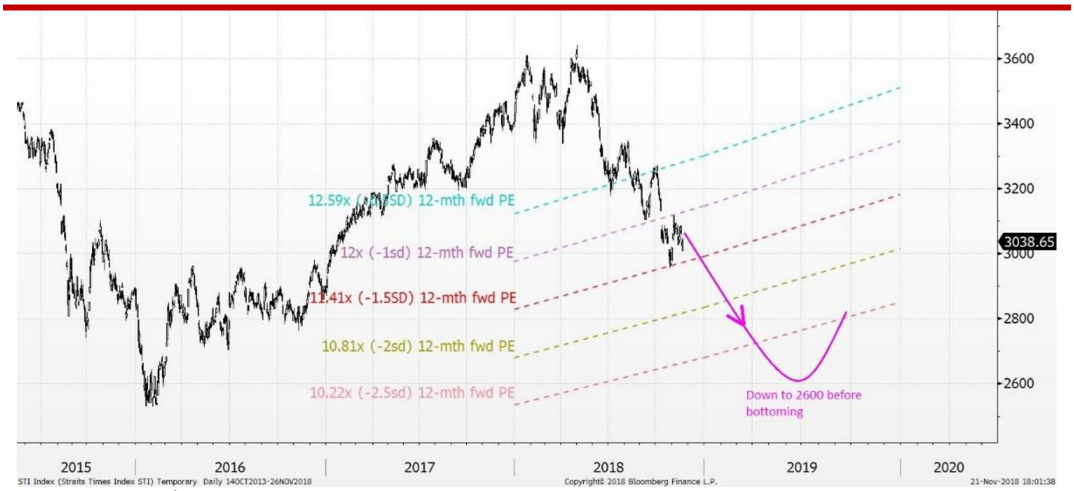
Condition 3: USDCNY rises beyond 7.2

- USDCNY rises beyond the 7.2 ceiling in 2Q forecasted by our currency strategist
- USDCNY weakness further drags down Asian currencies, USDSGD goes beyond our currency strategist's forecast of 1.44 by 2Q19

Straits Times Index

- Another 15% downside from 3050 to 2600 pegged at 9.8x (-3SD) blended FY19/FY20F PE before recovery
- 'Extreme' -3SD valuation peg coincides with GFC low

Straits Times Index Bear case – Down to 2600



Source: DBS Bank

Strategy

S-REITs remain in favour as FED turns dovish

S-REITs was the second best performing sector (after healthcare) in 2H18 and should continue to garner investors' interest as bond yields are still pressured by the FED turning more dovish. The FED's latest dot plot points to two (previously three) rate hikes this year that lifts the FED funds rate to 3%. FED Chairman Powell even hinted of a pause in rate hikes following his latest comments that with muted inflation readings, the FED will be patient and watch how the economy evolves.

This more dovish stance has also taken its toll on long bond yields with the US 10-year yield retreating 64bps to 2.59% and the MAS 10-year yield down by 59bps to 2.05% in recent months. This has lifted S-REIT's yield spread to 4.2% that is above the 10-year average of 3.8%.

Giving the uncertain macro growth environment, our REITs analyst prefers the more resilient retail and industrial (warehouse and business parks) sub-segments given their domestic focus and relatively stickier demand respectively. Our picks are **CMT**, **MCT**, **MLT**, **FLT** and **MAGIC**.

S-REITs picks

Company	Price 4 Jan	Target Price	Target Return	Mkt Cap (S$m)	EPS Growth 19 (%)	EPS Growth 20 (%)	Div Yield 19 (%)	Net Debt / Equity 19	P/BV 18 (x)
CapitaLand Mall Trust	2.26	2.44	8%	8,332	5.3	1.9	5.1	0.3	1.2
Frasers Logistics & Industrial Trust	1.03	1.20	17%	2,076	-0.3	2.4	6.5	0.3	1.1
Mapletree Commercial Trust	1.65	1.80	9%	4,766	2.6	2.0	5.7	0.3	1.1
Mapletree Logistics Trust	1.26	1.50	19%	4,520	3.6	2.9	6.3	0.4	1.0
Mapletree North Asia Commercial Trust	1.14	1.45	27%	3,610	-2.5	1.3	6.8	0.4	0.9

Source: DBS Bank

Stock market transition from early to mid-contraction outperformers positive for utilities

If our view that the current early-contraction phase of the economic cycle should come to an end in 1Q and the mid-contraction phase is next, then utility stocks could start to outperform soon. There are not many utility stocks listed but **SembCorp Industries** and **Netlink NBN Trust** are two large caps that come to mind.

Utility stocks

Company	Price 4 Jan	Target Price	Target Return	PER 19 (x)	PER 20 (x)	EPS Growth 19 (%)	EPS Growth 20 (%)	Div Yield 19 (%)	Net Debt / Equity 19	P/BV 18 (x)
NetLink NBN Trust	0.765	0.87	14%	38.5	33.7	55.7	14.3	6.6	0.2	1.0
SembCorp Industries	2.540	3.70	46%	10.9	9.6	41.5	13.8	2.3	1.0	0.6

Source: DBS Bank

Sticking to defensives

We continue to adopt a more guarded stance to our stock preferences even though there is tentative sign of some light at the end of the tunnel for US-China trade relations and interest rates may rise at a slower pace. More companies could sound the caution bell at the upcoming the FY results season and the earnings recession trend could continue for at least two more quarters.

Thus, we continue to prefer stocks with earnings visibility as well as yield plays with growth. Our picks are **ST Engineering** and **Yangzijiang** for the former and **ComfortDelgro**, **CMT**, **MLT**, **Netlink Trust** and **UOB** for the latter.

Defensive picks

Company	Price 4 Jan	Target Price	Target Return	PER 19 (x)	PER 20 (x)	EPS Growth 19 (%)	EPS Growth 20 (%)	Div Yield 19 (%)	Net Debt / Equity 19	P/BV 18 (x)
Yield with growth										
CMT	2.26	2.44	8%	18.3	18.0	5.3	1.9	5.1	0.3	1.2
ComfortDelgro	2.37	2.56	8%	16.3	15.8	7.6	2.9	4.8	cash	1.9
MLT	1.26	1.50	19%	16.4	15.9	3.6	2.9	6.3	0.4	1.0
NetLink NBN Trust	0.765	0.87	14%	38.5	33.7	55.7	14.3	6.6	0.2	1.0
UOB	24.57	29.5	20%	9.6	9.1	8.1	6.2	4.9	0.0	1.1
Earnings visibility										
ST Engineering	3.49	4.15	19%	18.5	16.8	9.7	10.1	4.6	0.3	4.8
Yangzijiang	1.25	1.82	46%	8.9	8.0	-6.4	10.2	3.6	cash	0.9

Source: DBS Bank

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FULLY VALUED (negative total return i.e. > -10% over the next 12 months)
SELL (negative total return of > -20% over the next 3 months, with identifiable catalysts within this time frame)

Share price appreciation + dividends

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