CIO Insights 2Q25

Build Resilience Amid Tariffs.

Recession Fears

Growing risk of a US recession as uncertainty mounts from a tariff war and wavering consumer confidence over DOGE and immigration policies.

IG Credit to Benefit

IG bonds with A/BBB credit ratings to benefit from deeper rate cuts as the Fed responds to a potentially sharp economic slowdown.

Catalysts in China & Europe

While we stay overweight on US tech equities for secular growth, opportunities abound in China following DeepSeek and in Europe after Germany's policy shift from fiscal restraint to largesse.

Alts in a Sweet Spot

Gold continues to be well-bid amid Trump 2.0 uncertainties. Hedge fund strategies to benefit from heightened market volatility, and private asset strategies from alpha sources of return.

DBS

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Executive Summary

Dear valued clients

After two consecutive years of outsized returns in excess of +25%, US equities hit a speedbump with heightened volatility during the first quarter of 2025.

Growing concerns around President Trump's tariffs, coupled with immigration policies and the Department of Government Efficiency's (DOGE) efforts to cut federal employee headcount have dampened consumer confidence. This has also stoked growth fears for the economy.

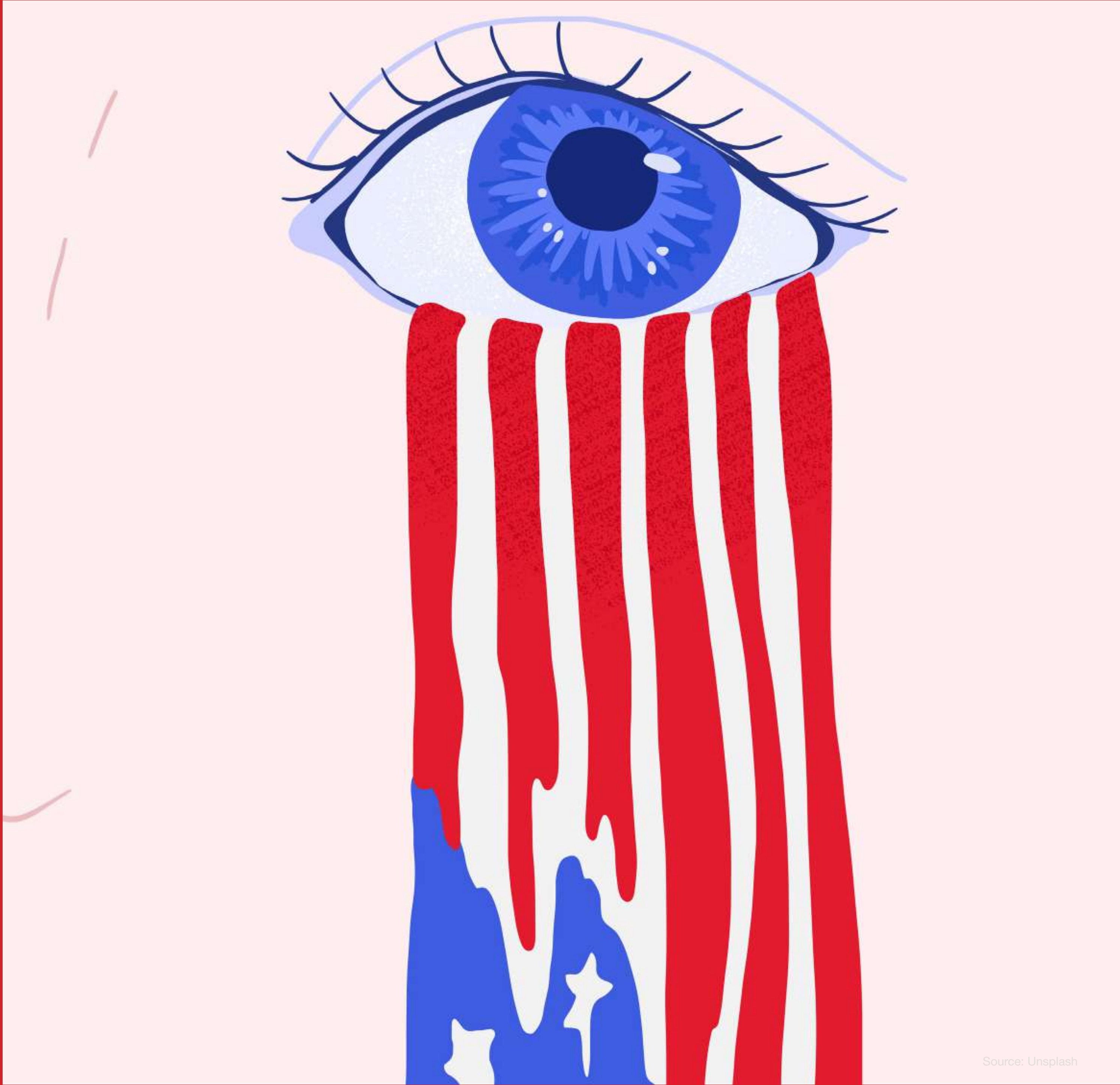
Such ongoing uncertainties have heightened stock market volatility and lowered Treasury yields as investors anticipate a sharp slowdown and potentially deeper rate cuts by the Fed.

Amid Trump's policy flip-flops, I want to reinforce the importance of embracing a portfolio approach to build resilience. For example, our barbell portfolio strategy, which embraces income-generating assets and risk diversifiers in addition to growth equities, has held up well as investment grade bonds rallied +2% and gold +15% (as of 24 Mar).

For this coming quarter, we turn constructive on the European industrial sector, given Germany's decision to end fiscal conservatism and unleash strong stimulus. We maintain a constructive view on China on the back of DeepSeek's technological breakthrough, alongside the country's steep valuation discount to the US. Meanwhile, we remain overweight in US technology for the secular growth play, as well as the asset class of alternatives, namely in gold, private assets, and hedge funds.

Hou Wey Fook, CFA

Chief Investment Officer



Source: Unsplash

The Age of Disruption

Asset Allocation 2Q25

The notion of "US exceptionalism" has waned as policy chaos introduced financial and stagflation risks to the system. While staying overweight in US tech for secular growth plays, seek opportunities in Europe and China. For bonds, stay up in quality with A/BBB with a duration barbell.

Investment Summary 2Q25

Macro Policy

US exceptionalism faces challenges as stagflation risks rise. Near-term economic weakness is prompting markets to price in more cuts. Further monetary easing expected in China and Europe. Japan to continue hiking.

Economic Outlook

As US tariffs on major trade partners escalate, markets are underestimating the impact on growth and inflation. Stimulus spending could pose upside surprise to growth in Europe and China.

Equities

On a 3-month basis, pivot US overweight to Europe on rising defence spending. Maintain overweight on AxJ amid China's tech revival while staying invested in US tech for secular growth.

Credit

Prioritise A/BBB and be selective with BB only in the 1-3Y segment. Portfolio duration should remain in a barbell, overweighting 2-3Y for certainty of good income, and 7-10Y to capitalise on curve rolldown.

Rates

High-yielding status of dollar rates is eroded vs G3 peers due to growth concerns in the US. Increased military expenditure in Europe and persistent inflation worries in Japan to drive up their bond yields.

Currencies

Reduced USD bullishness as US exceptionalism fades and tariffs evolve into a growth risk, but no expectation of a sustained, multi-month USD pullback.

Alternatives

Uncertainty remains the biggest immediate driver of gold under Trump 2.0. Achieve effective portfolio diversification by maintaining a balanced mix of public and private assets including hedge funds.

Commodities

Commodities have registered positive YTD returns due to stockpiling and supply squeezes. However, tariff threat remains as growth drag and demand destruction to creep in over time.

Thematics

Trump's "drill, baby, drill" mantra and the collective push-back on ESG has put the spotlight back on energy, in particular, oil & gas. Oil majors and services companies to benefit.

Theme: Energy – Opportunities Amid Uncertainty

With US energy dominance and security as one of the key pillars of Trump 2.0, the energy sector looks set for gradual production gains as restrictive policies get rolled back.

Against this positive policy backdrop and the continued structural relevance of oil & gas, energy remains a relatively safe space for investors who are seeking play on the robust long-term fundamentals of the sector.

01. Asset Allocation.

Hou Wey Fook, CFA
Chief Investment Officer

Dylan Cheang
Strategist

2025 couldn't have started off in a more dramatic fashion with President Trump wasting no time in unleashing his policy agenda. From startling remarks on taking over Gaza and turning it into the "Riviera of the Middle East" to the announcements of tariffs on China, Mexico, and Canada, Trump is acting on his campaign promises at warp speed. Across the Atlantic, the long-standing foundation of the US-Europe relationship received a severe jolt as European leaders came to the cold realisation that the western alliance is now in severe meltdown.

Not only is Europe denied a seat at the table in the discussion to end the Russia-Ukraine war but the US will also no longer be the "primary guarantor" for the region's security in future. Further strain in ties was evident at the Munich Security Conference with Vice President Vance openly questioning if they still share a common agenda today. The open spat between Trump and Zelensky at the Oval Office, perhaps, perfectly sums up the acrimonious state of affairs between the US and her former allies.

And just like that, the Transatlantic Alliance and postwar American foreign policies are thrown into turmoil. Europe, however, is not sitting back. Led by UK and France, Europe has since put together a "coalition of the willing" to draw up a peace plan for Ukraine. The biggest paradigm shift, perhaps, is Germany's "whatever it takes" moment as Chancellor-in-waiting Friedrich Merz pledged to ease the country's fiscal conservatism to unleash the largest economic stimulus since the end of the Cold War.

This is a water-shed moment signalling Germany's (and by extension, Europe's) entry into massive stimulus mode at a time when policy uncertainties are engulfing the US and the very notion of "US exceptionalism". To ride the new geopolitical realities, we are making two key portfolio switches for the quarter:

1. Downgrade US equities to 3-month underweight while maintaining 12-month overweight; Maintain conviction view on US technology and healthcare
2. Upgrade Europe equities to 3-month overweight while maintaining 12-month underweight; Seek opportunities in Europe industrials (defence sub-sector) and financials

Meanwhile, we believe the following factors will dominate market narratives in 2Q25 and they are:

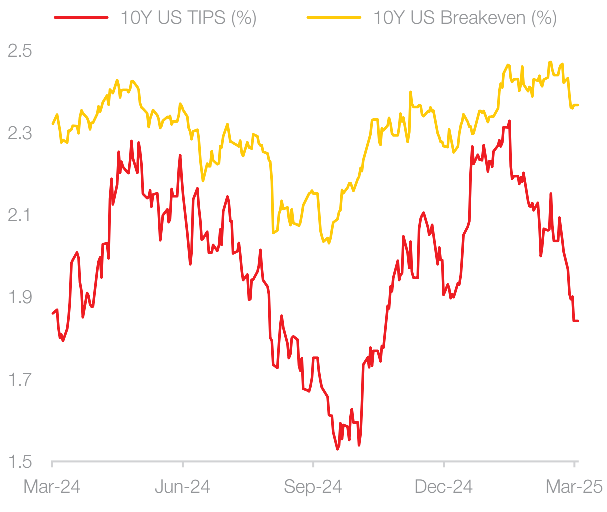
- Revival of growth fears
- Enhancing diversification and downside protection
- Commoditisation of AI

Revival of growth fears

Since the initial market euphoria post-Trump's election victory, risk assets have undergone a reality check with the S&P reversing its gains while US Treasury yields and greenback both headed south. The downshift in Treasury yields is driven predominantly by falling real yields as opposed to lower inflation expectations.

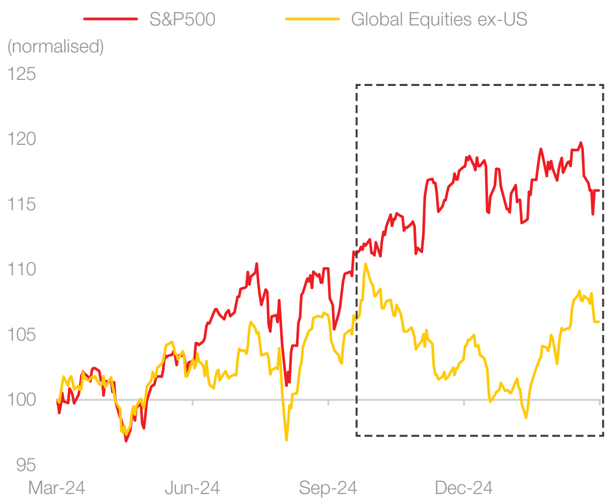
There are two reasons behind the sentiments shift. One, the drawdown reflects an unwinding of popular trades from a flow perspective. To put things in context, the S&P 500 has vastly outperformed global equities since late 2024 as the US market was widely perceived as the “only game in town” following Trump’s election victory. A large part of the gains was in fact driven by the “Magnificent 7” (Mag 7) and this trade is currently being unwound as investors seek opportunities beyond this space.

Downshift in UST yield led by real yields as opposed to inflation expectations



Source: Bloomberg, DBS

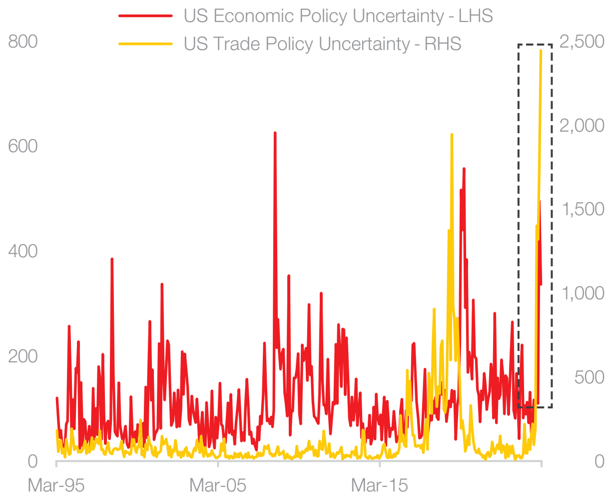
US equities were a consensus long post-Trump’s election victory



Source: Bloomberg, DBS

The other, perhaps bigger, reason for the risk off lies in the revival of growth fears as the double whammy of rising policy uncertainties and weakening growth momentum take hold. Indeed, based on data from Baker, Bloom, and Davis, US trade policy uncertainties have surged to 2,446 and this vastly exceeds the previous peak of 1,947 seen in Aug 2019 during Trump’s first trade war. Given the difficulty in pricing policy risks, it is no surprise that portfolio allocators trimmed their bets on winning trades and adopted a wait-and-see strategy.

US policy uncertainties have hit an all-time high...



Source: Bloomberg, DBS

...while macro data continues to surprise on the downside

Source: Bloomberg, DBS

US macro momentum, meanwhile, is starting to show early signs of moderation. Retail sales, for instance, fell 0.9% in January – the sharpest in two years while consumer confidence plunged 7 points to 98.3 in February – the biggest decline since Aug 2021. Whether these datapoints prove to be the proverbial canaries in the mines for further economic contractions ahead remain to be seen. But the recent slew of policies unleashed by the new administration suggests that things could get worse before they get better, with the key headwinds being:

- New immigration policies: The Trump administration has unleashed a series of new immigration policies as it sought to reduce the number of undocumented migrants in the country. According to Brookings Institute, this will reduce GDP growth in 2025 by 0.1-0.4 %pts.

- Aggressive job cuts by DOGE: The Department of Government Efficiency (DOGE) is slated to cut about 300,000 federal employees. These cuts, coupled with corresponding reduction in private sector contract staff, will translate to weaker consumer confidence and consumption.

- Sticky inflation and weak affordability: US headline inflation has surged to 3% in January, complicating the picture for Trump who has made combating inflation a central piece of his re-election campaign. The political optics of Trump inflicting tariffs at a time of resurgent inflationary pressure will not be palatable for the American people.

Enhancing diversification and downside protection

Despite the revival of growth fears amid policy uncertainties, we believe that the equity up-cycle stays intact. The likelihood of a US recession remains moderate at 25% and this underpins our base-case soft-landing assumption as tariff-related economic headwinds are expected to be offset by tax cuts and deregulation. Based on consensus forecast, global corporate earnings are still expected to grow by 9% this year (+8% for DMs and +14% for EMs), indicating that the sudden occurrence of a bear market is a low probability event – for now.

But investors should not get complacent. From a timeframe perspective, the positives from Trump's policies (such as deregulation and increase in efficiency) will take a longer time to become evident in the economy. On the other hand, the negatives from trade tariffs and slashing of federal workforce is almost immediate. Above all, consumer and business confidence have certainly taken a dent with recent developments. This will translate to weaker consumption and capex in the near term. Under such conditions, investors are advised to:

- Diversify from crowded trades
- Gain exposure to alternatives for downside protection

Diversification from crowded trades: The prevalence of "US exceptionalism" and buying frenzy on AI have led to huge concentration risk in US tech. Just last year, the Mag 7's total return of c.67% has far superseded the 25% gain registered by the S&P 500. But after such robust outperformance, it is no surprise that we are starting to witness a shift in 2025:

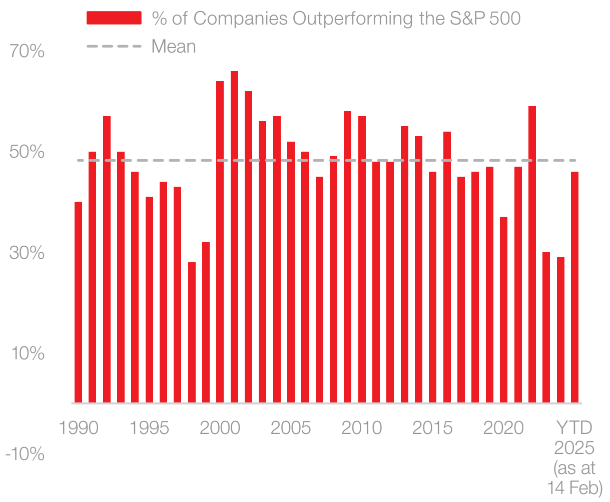
- S&P 500 ex-Mag 7 (proxied by the Bloomberg US Large Cap ex-Magnificent 7 index) has outperformed Mag 7 by c.11 %pts (as of 28 Feb)
- 50% of S&P 500 companies are outperforming the index, a stark contrast to the 29% level seen in 2024

These datapoints suggest that investors are searching for opportunities beyond Mag 7 and such portfolio switches are backed by fundamentals:

1. Narrowing earnings gap: The earnings growth gap between Mag 7 and S&P 500 ex-Mag 7 stood at c.57 %pts in 2024. However, this is expected to narrow to c.20% this year, suggesting that earnings momentum for S&P 500 ex-Mag 7 is on the rebound
2. Valuation discount: On valuation, the forward P/E for S&P 500 ex-Mag 7 is trading at c.28% discount to Mag 7 and this connotes substantial relative value

Despite our positive view on US technology, on balance, we believe that the rotation of portfolio exposure beyond Mag 7 is a healthy development as it reduces concentration risk while enhancing the overall resilience of the market.

Rising percentage of companies within S&P 500 outperforming the index



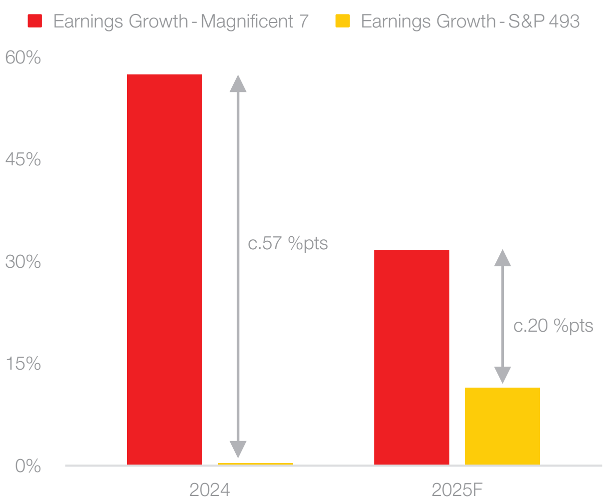
Source: Bloomberg, DBS

Apart from portfolio allocators diversifying beyond Mag 7 within US equities, from a global equities' perspective, we are also seeing signs of investors diversifying beyond US to other DMs (particularly within Europe). Fund flows data from EPFR Global validate this point.

On a 3-month moving average basis, weekly fund inflow to US has moderated by c.35% compared to the start of the year. In contrast, Europe is seeing weekly inflows of USD185mn, a significant shift from the net redemption seen at the start of the year. This trend suggests renewed enthusiasm for Europe equities, and we see opportunities in the following sectors:

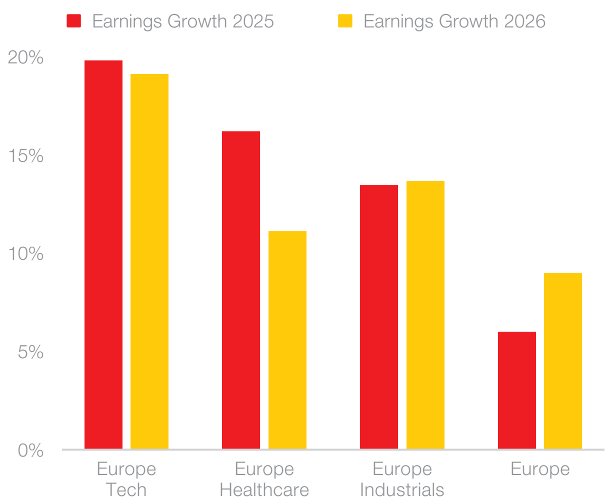
- Industrials: Defence companies (within the industrials sector) are poised to benefit from increased military spending among European

Equity rally broadening across sectors in 2025



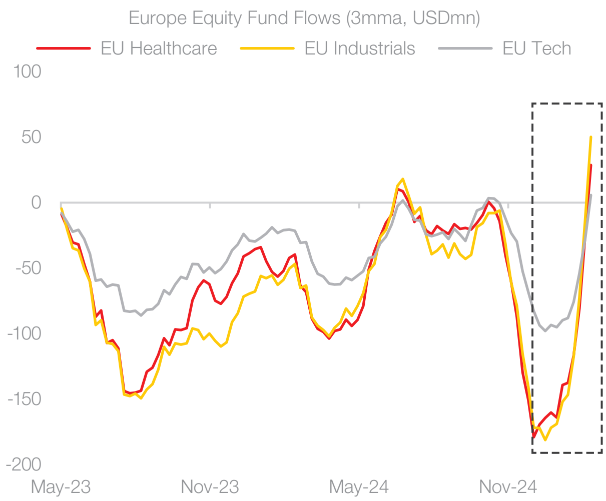
Source: Federal Reserve Bank of St. Louis, DBS

Strong earnings momentum for European tech, healthcare, and industrials



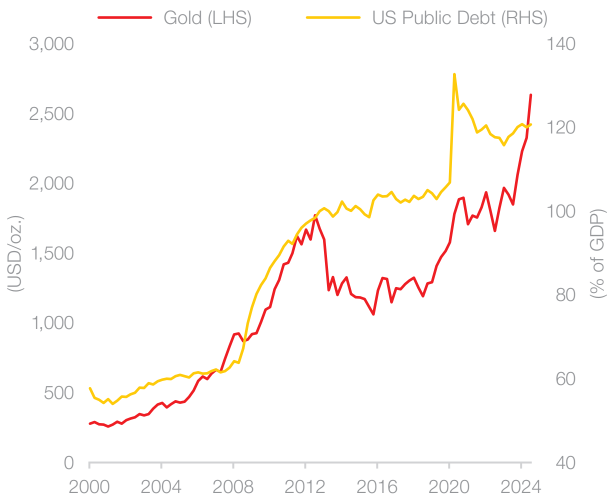
Source: Bloomberg, DBS

Funds flows on the rebound



Source: EPFR Global, DBS

Relationship between gold and US indebtedness



Source: Bloomberg, Federal Reserve Bank of St. Louis, DBS

nations, which will potentially rise from 2% to 2.5%-3.5% of GDP

- Healthcare: Healthcare stands to benefit from the aging population in Europe. According to the European Commission, the population of older people is expected to increase to 32.5% by 2100
- Technology: Europe is expected to invest heavily in semiconductor manufacturing to boost self-sufficiency

Gain exposure to alternatives for downside protection. As global trade tension continues to simmer in the coming quarters, investors are advised to double down on their downside protection through exposure to gold and private assets.

Gold price has been on a tear as concerns on US fiscal condition and rising de-dollarisation risk propelled prices of the precious metal higher. Yet, after last year's robust returns, the inevitable question is: Can gold rally higher? We believe so.

Having reproduced a study done by the World Gold Council, our gold strategist concluded that the primary driver of gold over prolonged periods is nominal GDP with global equity/bond market capitalisation as an offsetting factor. Based on this framework, gold is expected to register annualised returns of c.6.2% over a timeframe of 10-15 years.

On a portfolio basis, we have, in a previous analysis, concluded that a 40/30/30 portfolio (40% equities, 30% bonds, and 30% alternatives) experienced substantially shallower drawdowns compared to a traditional 60/40 portfolio during periods of financial stress. Analysing drawdown data from Dec 2007 through Sep 2023, a 40/30/30 portfolio registered annualised volatility of 9.3% (vs 11.4% for a 60/40 portfolio).

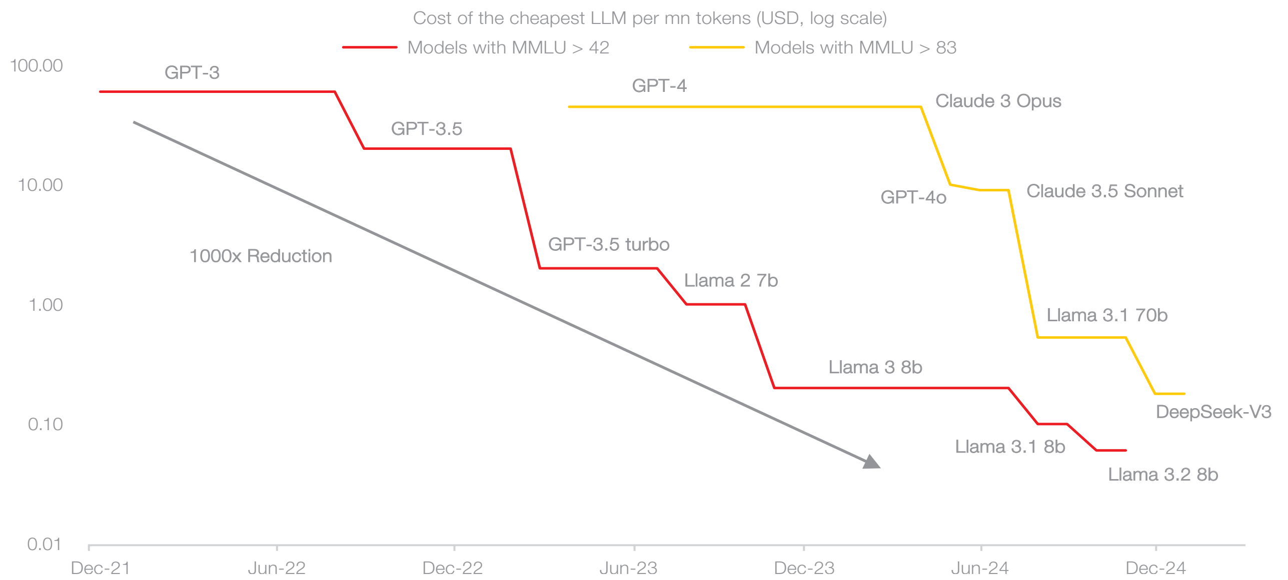
Commoditisation of AI

Implications of DeepSeek's arrival. DeepSeek released DeepSeek-R1, an open-source reasoning model capable of solving complex problems, in Jan 2025. The release sent ripples through the industry as its performance is comparable to leading models like OpenAI's ChatGPT-4o (despite being allegedly developed at a fraction of the cost). DeepSeek's release triggered a tech sell-off as the breakthrough in AI training efficiency raised the following concerns:

- Threat to Big Tech's dominance and profitability: DeepSeek asserts that its V3 model is trained using over 2,000 Nvidia H800 chips and at an exceptionally low cost of USD5.6mn – a fraction of Big Tech's expenditure. This development translates to lower barriers of entry for smaller players and may pose potential headwinds for Big Tech's dominance and high profitability (as a reference, Mag 7's operating margin stands at 24% vs 14% for S&P 500).
- Potential reduction in capex: As AI training and inferencing become more cost-efficient, hyperscalers may cut back on their capex for high-end chips. A slowdown in spending by hyperscalers will weaken the demand for advanced semiconductors and put pressure on the profitability of industry leaders (as a reference, Nvidia's operating margin stands at 62% vs S&P 500's 14%).

Glass half full rather than half empty. While DeepSeek's arrival caused short-term volatility, we believe that it will ultimately benefit the broader economy. Jevons' Paradox suggests that greater efficiency fuels higher demand, and in AI, this means faster adoption. EY projects rapid GenAI adoption to boost GDP growth by 0.5 %pts annually over the next decade.

Cost of Large Language Model (LLM) decreasing over time



Source: a16z, DeepSeek, DBS

Above all, DeepSeek's open-source reasoning model will accelerate demand for inferencing which requires significantly more computational power. According to MarketsandMarkets, the inference market is expected to grow at a 19.2% CAGR, from USD106bn in 2025 to USD255bn by 2030 and this is beneficial to chipmakers.

2Q25 CIO Asset Allocation (CIO AA) – Defensive shift

Categories	Indicators	Score Range	Equities				Bonds		
			US	Europe	Japan	AxJ	DM Govt	DM Corp	EM Bonds
Fundamentals	PMI	-1 to +1	0	0	0	0	0	0	0
	Economic surprise	-1 to +1	0	1	0	1	0	0	0
	Inflation	-1 to +1	-1	0	0	0	-1	-1	-1
	Monetary policies	-1 to +1	0	1	0	0	0	0	0
	Forecasted EPS growth	-2 to +2	1	0	0	0	-	1	0
	Earnings surprise	-2 to +2	1	0	1	0	-	0	0
Valuation	Forward P/E	-2 to +2	-1	0	0	1	-	-	-
	P/B vs ROE	-2 to +2	0	-1	-1	0	-	-	-
	Earnings yield - 10Y yield	-2 to +2	-1	-1	-1	1	1	1	0
	Free Cashflow yield	-2 to +2	-1	0	1	1	-	-	-
	Credit spread	-2 to +2	-	-	-	-	-	0	-1
Momentum	Fund flows	-2 to +2	0	1	0	0	1	1	0
	Volatility	-1 to +1	-1	0	0	0	0	-	-
	Catalysts	-2 to +2	-1	1	0	-1	0	0	0
Raw Score			-4	2	0	3	1	2	-2
Adjusted Score*			**-0.19**	**0.10**	**0.00**	**0.14**	**0.09**	**0.13**	**-0.13**

*Note: The "Adjusted Score" is calculated using the "Raw Score" divided by the maximum attainable score for each category.

Source: DBS

Cross Assets – Bonds remain in play amid rising uncertainties. The latest scoring on our CIO AA framework suggests a preference for bonds over equities.

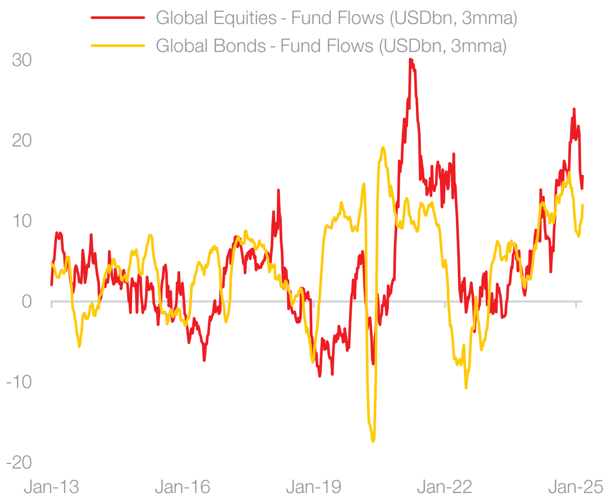
Fundamentals: While US economic momentum has displayed remarkable resilience, recent data suggests that a slowdown is on the cards as incoming retail sales and consumer confidence data surprises on the downside. Given heightening fears on a trade war and impending job losses, we expect confidence to deteriorate further and be a drag on domestic consumption. Essentially, the prevalence of a trade war and shrinkage of federal workforce could potentially offset the benefits from tax cuts and deregulation.

On corporate earnings, the potential negative effects from Trump's policies have yet to be fully incorporated into analysts' forecasts as the situation remains fluid under Trump's transactional style of policy making. On balance, the street remains upbeat on US earnings with an estimated growth of 14% this year, buoyed by an expected 3.7 %pts increase in EBIT margins. Similarly, analysts' outlook for Asia ex-Japan is robust with earnings growth expected at 12%. But the sanguine earnings view will change if trade tensions deteriorate further from here.

Valuation: The gap between US earnings yield and UST 10Y yield has deteriorated to -0.27% as at 5 Mar 2025 and this reinforces our cautious stance on equities relative to bonds.

Momentum: Fund flows data from EPFR Global continues to suggest indifference in investors' asset allocation flows as equities and bonds registered broadly similar inflows of USD136bn and USD137bn QTD (as at 26 Feb 2025). This marks a continuation of the trend in 2024 as USD712bn and USD615bn entered equities and bonds respectively.

Equity and bond flows rising in tandem



Source: EPFR Global, DBS

Equities: Diversifying exposure beyond S&P 500; Seek opportunities in resurgent Europe. The initial enthusiasm surrounding fiscal easing under Trump 2.0 faltered fast as the S&P 500 has since exhausted its post-presidential election gains. On a YTD basis, US lost 0.4% (as at 5 Mar), led by sharp losses in the technology and consumer discretionary sectors. Europe, in contrast, surged 14.7% while Japan and Asia ex-Japan were relatively subdued during the quarter. For the upcoming quarter, we advise investors to avoid "crowded trades" in US and our cautious stance is premised on the following factors:

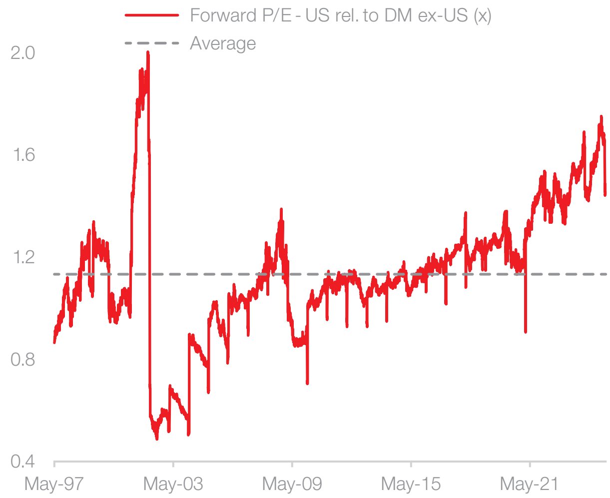
- Revival of growth and policy headwinds: The escalation of trade tensions will weigh on consumer and business confidence, driving domestic consumption and business capex lower. This is coming at a time when US data is already showing early signs of weakness. Yet, the prevalence of sticky inflation will mean that the Fed's hands are tied on the monetary policy front. While tax cuts and deregulation may mitigate some of these headwinds, the macro environment will nonetheless stay challenging for US equities.

- Crowded trade and valuation premium: As the "US exceptionalism" theme faces incremental headwinds in the coming months, the market will find it tough to sustain its valuation premium relative to other DMs, particularly when analysts start to revise down their earnings forecast to factor in rising macro and policy uncertainties. On a forward P/E basis, the US trades at 46% premium to DMs (excluding US).

In spite of our near-term cautious view on US, we continue to stay positive on US technology given secular growth tailwinds. In other developed markets, we are upgrading Europe to 3-month overweight while retaining our neutral weight on Japan. Our positive view on Europe is premised on:

- Rising defence and infrastructure spending: The shifting geopolitical winds with US adopting an "America First" policy will see European nations spending more on defence in the coming years. This is best exemplified by Germany's "whatever it takes" moment as Chancellor-in-waiting Friedrich Merz pushed for the end of fiscal conservatism to create a EUR100bn fund that will unleash the largest economic stimulus since the end of the Cold War. According to Kiel Institute, GDP growth could increase by 0.9-1.5% per year if nations (a) increase defence spending to 3.5% of GDP (vs NATO's target of 2%) and (b) purchase weapons manufactured domestically in Europe.

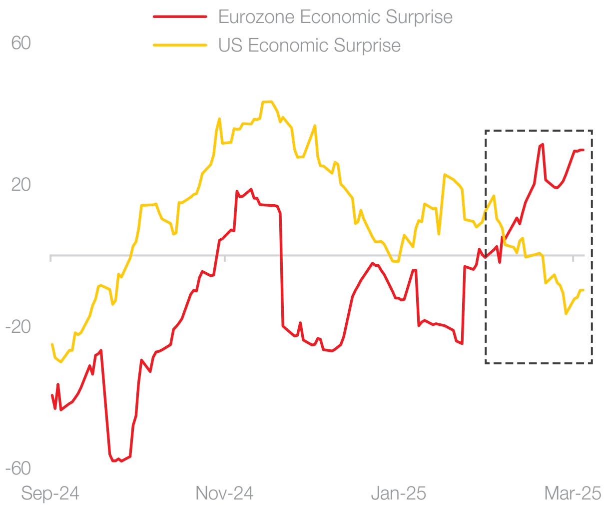
US trades at a huge premium to other DMs



Source: Bloomberg, DBS

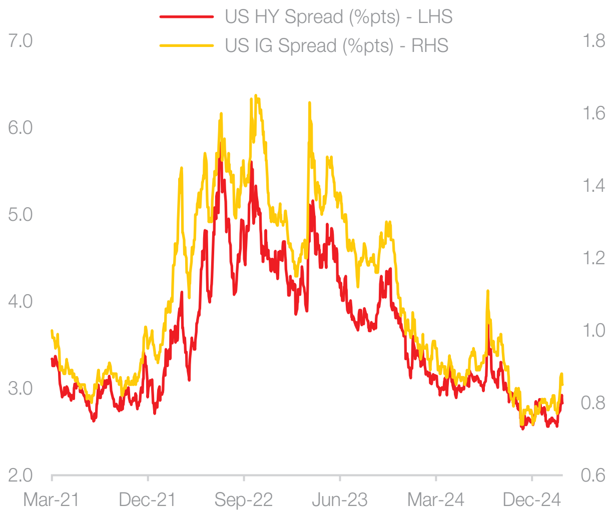
- Improving relative macro momentum and extreme valuation discount: Since the start of the year, economic surprises for the Eurozone have been on a recovery trajectory while the US was trending south. This suggests Europe's macro momentum is outperforming US on a relative basis. Yet, the region continues to trade at an extreme discount to the rest of the developed markets. We believe downside momentum for macro weakness has been sufficiently priced-in and Europe connotes value at this juncture.

Europe sees stronger macro momentum than US



Source: Bloomberg, DBS

Credit spreads have remained range bound despite macro and economic uncertainties



Source: Bloomberg, DBS

Bonds: Tariff fears are triggering inflows to safe havens; Maintain overweight on bonds. Last quarter, we cautioned that the notion of higher bond yields under Trump 2.0 may not necessarily pan out as the new administration needs to hike tariffs to partially fund its tax cuts. Resultant economic stress arising from a global trade war will weigh on bond yields, which was exactly what happened. Since its peak in 14 Jan, the 10Y US Treasury yield has plummeted as tariff fears took hold.

US IG and HY credit spreads, meanwhile, have remained stable despite the resurgence of policy uncertainties and we believe that the overall tranquillity can be attributed to three factors:

1. Healthy corporate fundamentals: US corporate balance sheets have remained healthy with low risks of defaults. Companies are, in general, managing their debt and cash levels well while corporate profitability has been strong this year.

2. Attractive overall yield: On the demand side, the overall yield for corporate bonds remains attractive and this has sustained fund flows into the credit space. Data from EPFR Global shows USD36bn entering DM corporate bonds this year (as at 26 Feb) and this is broadly similar to the amount seen over the same period in 2024.

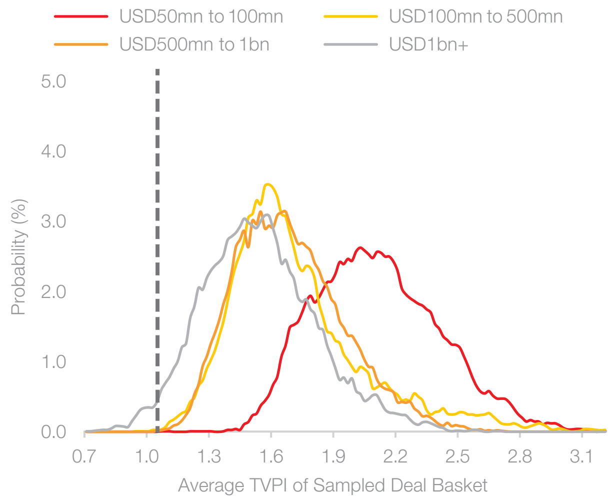
3. Low probability of Fed hike: The Fed currently sees its policy as “restrictive” and hence there is low likelihood of policy tightening despite inflationary risks posed by the escalating tariff war. Moreover, the imposition of tariffs represents a supply shock and historically, policy rate hikes are not effective in such situations.

In terms of credit selection, we advocate investors to stay with quality in the A/BBB segment while taking selective picks in HY BB segment (1–3Y duration). In terms of portfolio duration, maintain a barbell approach with 2-3Y and 7-10Y segments (overall 5-7Y portfolio).

<u>Alternatives</u>: Gold – a geared beneficiary of Trump 2.0. Gold benefits either way in Trump 2.0. On one side of the equation, Trump's taxation cuts and deregulation will only serve to exacerbate longer-term concerns of monetary debasement in the US. But on the other end of the equation, the unleashing of trade tariffs and policy shocks will only drive bond yields lower and trigger the flight to safe havens like gold. It is, therefore, not a surprise that central banks' demand for gold surged to 1,045 tonnes in 2024, a level which is significantly higher than the c.473 tonnes average seen during 2010-21.

In private assets, we advise investors to seek opportunities in middle market buyouts and growth private equity. Middle market companies possess lower purchase multiples, providing room for larger future value expansion. Besides, the requirement for lower leverage in middle market deals auger well for their outlook in a high-interest rate environment.

Strong upside for middle market PE buyout funds



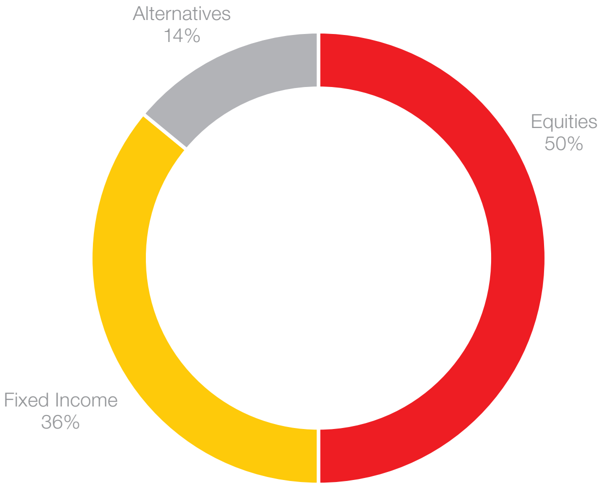
Source: Pitchbook, DBS

2Q25 CIO Asset Allocation (CIO AA)

	3-Month Basis	12-Month Basis
Equities	**Neutral**	**Neutral**
US Equities	Underweight	Overweight
Europe Equities	Overweight	Underweight
Japan Equities	Neutral	Neutral
Asia ex-Japan Equities	Overweight	Overweight
Fixed Income	**Overweight**	**Overweight**
Developed Markets (DM) Government Bonds	Overweight	Overweight
Developed Markets (DM) Corporate Bonds	Overweight	Overweight
Emerging Markets (EM) Bonds	Underweight	Underweight
Alternatives	**Overweight**	**Overweight**
Gold	Overweight	Overweight
Private Assets & Hedge Funds	Overweight	Overweight
Cash	**Underweight**	**Underweight**

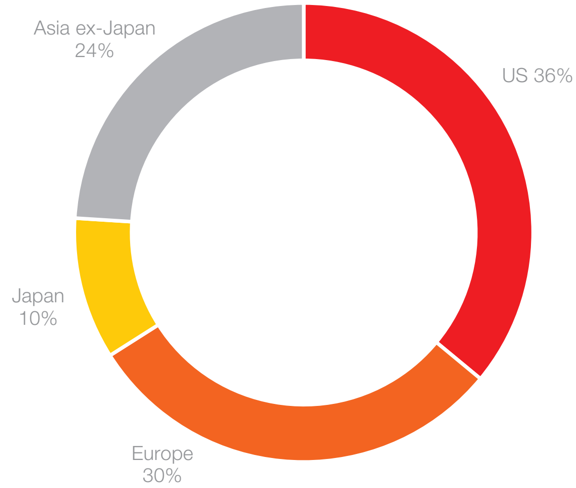
Source: DBS

CIO AA breakdown by asset class (Medium Risk)



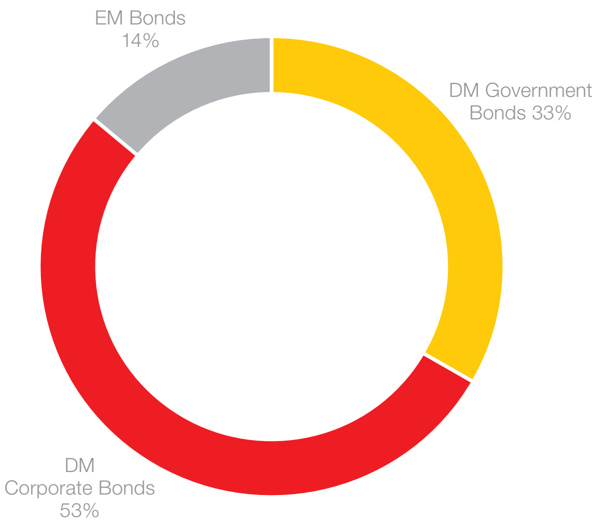
Source: DBS

CIO AA breakdown by geography within equities (Medium Risk)



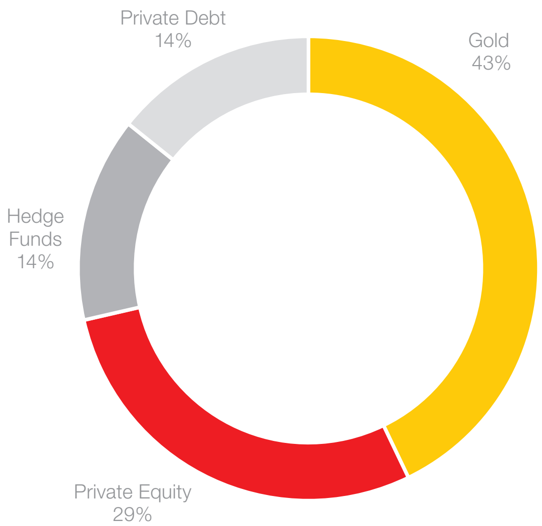
Source: DBS

CIO AA breakdown by bond types within fixed income (Medium Risk)

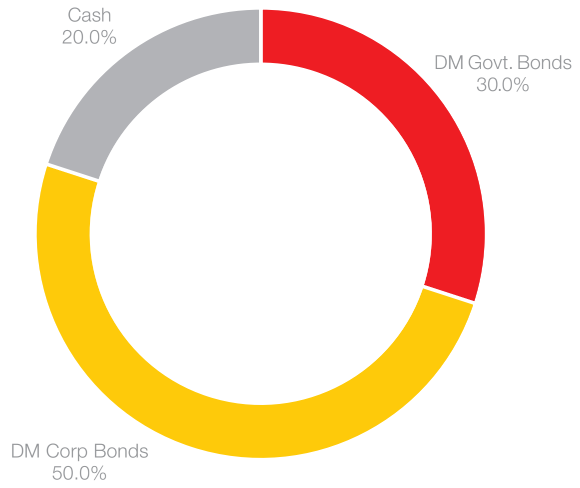


Source: DBS

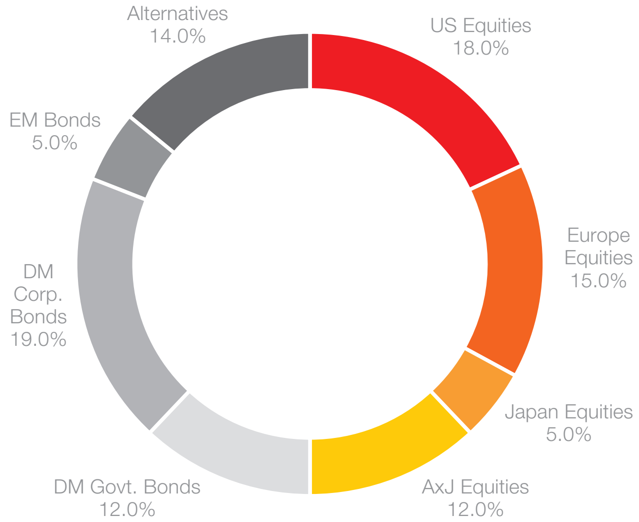
CIO AA breakdown by segments within alternatives (Medium Risk)



Source: DBS



Source: DBS



Source: DBS

Low Risk

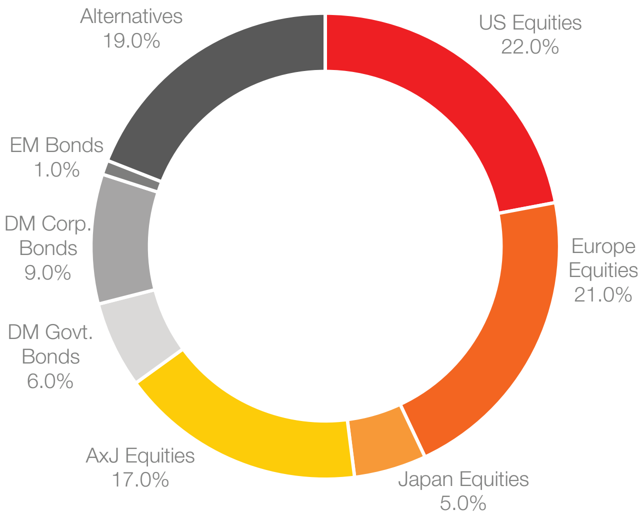
	CIO AA	SAA	Active
Equities	**0.0%**	**0.0%**	
US	0.0%	0.0%	
Europe	0.0%	0.0%	
Japan	0.0%	0.0%	
Asia ex-Japan	0.0%	0.0%	
Fixed Income	**80.0%**	**80.0%**	
Developed Markets - Government	30.0%	30.0%	
Developed Markets - Corporate	50.0%	50.0%	
Emerging Markets	0.0%	0.0%	
Alternatives	**0.0%**	**0.0%**	
Gold	0.0%	0.0%	
Private Assets & Hedge Funds*	0.0%	0.0%	
Private Equity	0.0%	0.0%	
Hedge Funds	0.0%	0.0%	
Private Debt	0.0%	0.0%	
Cash	**20.0%**	**20.0%**	

*Only P4 risk rated UCITs Alternatives

Medium Risk

	CIO AA	SAA	Active
Equities	**50.0%**	**50.0%**	
US	18.0%	25.0%	-7.0%
Europe	15.0%	10.0%	5.0%
Japan	5.0%	5.0%	
Asia ex-Japan	12.0%	10.0%	2.0%
Fixed Income	**36.0%**	**35.0%**	**1.0%**
Developed Markets - Government	12.0%	10.0%	2.0%
Developed Markets - Corporate	19.0%	15.0%	4.0%
Emerging Markets	5.0%	10.0%	-5.0%
Alternatives	**14.0%**	**10.0%**	**4.0%**
Gold	6.0%	5.0%	1.0%
Private Assets & Hedge Funds*	8.0%	5.0%	3.0%
Private Equity	4.0%	2.4%	1.6%
Hedge Funds	2.0%	2.0%	
Private Debt	2.0%	0.5%	1.5%
Cash	**0.0%**	**5.0%**	**-5.0%**

*Only P4 risk rated UCITs Alternatives



Source: DBS

High Risk

	CIO AA	SAA	Active
Equities	**65.0%**	**65.0%**	
US	22.0%	30.0%	-8.0%
Europe	21.0%	15.0%	6.0%
Japan	5.0%	5.0%	
Asia ex-Japan	17.0%	15.0%	2.0%
Fixed Income	**16.0%**	**15.0%**	**1.0%**
Developed Markets - Government	6.0%	4.0%	2.0%
Developed Markets - Corporate	9.0%	7.0%	2.0%
Emerging Markets	1.0%	4.0%	-3.0%
Alternatives	**19.0%**	**15.0%**	**4.0%**
Gold	6.0%	5.0%	1.0%
Private Assets & Hedge Funds*	13.0%	10.0%	3.0%
Private Equity	6.0%	4.9%	1.1%
Hedge Funds	4.0%	4.0%	
Private Debt	3.0%	1.1%	1.9%
Cash	**0.0%**	**5.0%**	**-5.0%**

*Only P4 risk rated UCITs Alternatives

Notes:
1. The above are based on three-month views.
2. Asset allocation does not ensure a profit or protect against market loss.
3. “CIO AA” refers to “CIO Asset Allocation”. “SAA” refers to “Strategic Asset Allocation”.
4. The investor type classification for the portfolio has no direct relationship with the Financial Needs Analysis customer risk profile types and the portfolios are not assigned any product risk rating based on the bank’s proprietary risk rating methodology.

Tariff Storm

Macroeconomics
2Q25

Volatile decision-making by the US authorities have upended Trump trades. Europe seeks to boost growth and security defences in a difficult geopolitical environment. Supply chain reconfiguration and firmer growth prospects are supportive of Asia's outlook. Oil price may be close to a bottom.

Source: Unsplash

02. Macroeconomics.

Taimur Baig, PhD
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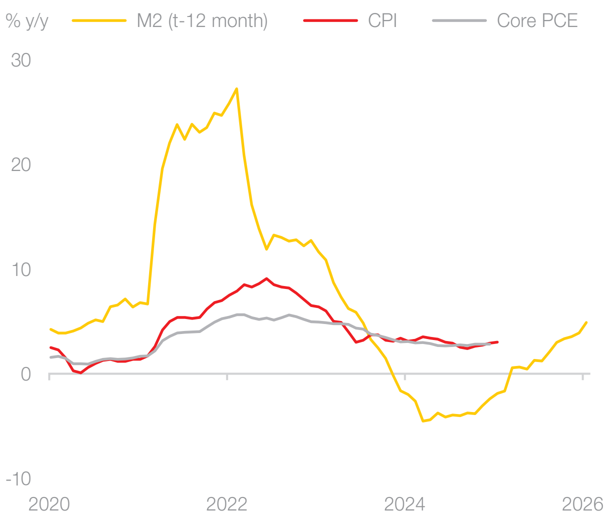
Economist

Suvro Sarkar
Analyst

US

Can US exceptionalism last? Are stagflation risks rising? The game of tariffs, as expected, has intensified. The US government is in the process of imposing and threatening substantial tariffs on imports from Canada, Mexico, and China. Many more such measures are forthcoming against a wider range of countries. We believe that there will be an element of brinkmanship. Tariff threats on products and countries will be issued, and then, withdrawn upon successful extraction of a concession. We also expect retaliatory measures by trading partners, especially toward products with their origins in Republican-run (or red) states. Noise and lobbying over trade policy are expected to spike. We think markets are complacent in pricing in the downside risk to growth and upside risk to inflation from such measures.

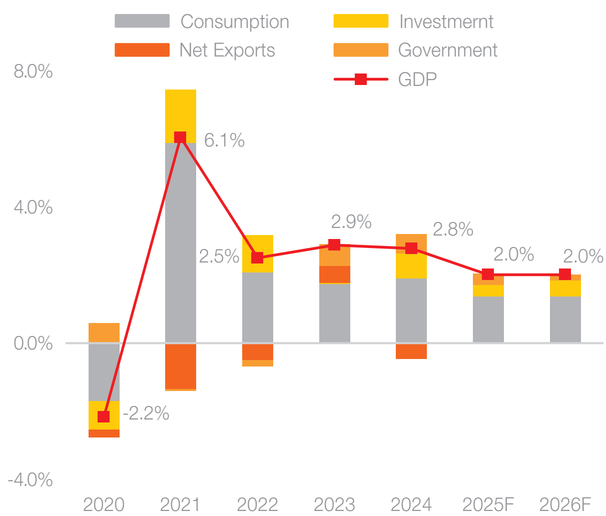
Money and inflation



Source: CEIC, DBS

In thinking through the ramification of tariffs, whether threatened or actual, we should begin with the premise that time for price cuts or passing on savings to customers from productivity gains is over, at least for the time being. Businesses, facing a tight labour market and a still-strong demand environment, would pass on tariff-induced costs readily. Given the types of goods heavily traded between US, Canada, and Mexico, we see an immediate upside to autos and gasoline. Also, demand for US exports would be affected as retaliatory measures are implemented.

US GDP and its components



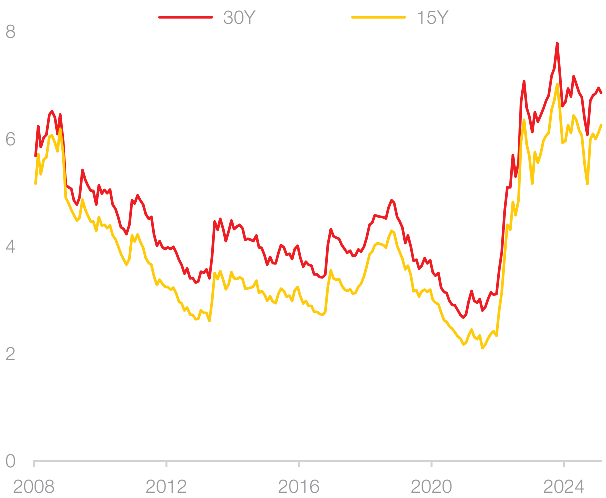
Source: CEIC, DBS

Mexico's export sector, currency, and price level could be destabilised severely; Canada will also likely face considerable damage. Chinese exports, particularly those that have done well lately through the direct-to-consumer delivery model, would likely suffer the most.

The myriad goals of President Trump (e.g. scaling back multilateralism, downsizing the government, reducing the oversight of tech and financial sectors, scaling back immigration, pushing through tax cuts, encouraging fossil fuel production, among others) do not lend themselves to macro stability in the near term. This, in turn, could have the effect of paralysing the Fed from acting as forecasts become harder in the cacophony of policy noise.

Given the strong momentum in the US economy seen through end-2024, we ought to forecast 2.5%+ growth for 2025 and 2026, but we would peg our forecast to around 2% instead after incorporating heightened policy noise as a factor. Beyond tariffs, immigration tightening measures, along with the consolidation of public sector payrolls and spending that would be growth-negative, offsetting supportive measures like deregulation and tax cuts are in our view. Already, consumer and business confidence markers are showing deterioration which is understandable, given the heightened noise around decision-making.

Mortgage rates



Source: CEIC, DBS

Inflation has already been stalling long before settling at the Fed's target of 2%. With tariffs and tax cuts in play, we see headline and core inflation in the 2.5-3% range over the next two years. Inflation expectations have begun rising as per consumer surveys and market-based indicators. Unless there are major financial stability related concerns and a sharp downshift in economic growth momentum, the Fed would find it hard to carry out substantial accommodation. We see 4% as the terminal rate in this cycle, barring the scenario of Trump forcing the Fed into cutting rates.

Eurozone

A confluence of politics, fiscal big bang out of Germany, trade tensions with the US, and efforts to lift the bloc out of stagnation will dominate developments this quarter and the year ahead.

The German elections held in Feb 2025 saw CDU/CSU win the poll with 28.6% of the vote, keeping on track to form the next coalition government. A coalition would be necessary to go past the required 50% of the seats in parliament. A favourable outcome would be a coalition with SPD, even if they are marked by internal policy differences. The far-right AfD party expanded its presence, emerging as the second most popular party. While mainstream parties have rejected cooperation with the AfD to form the next government, its strong showing might undermine investor confidence. Passage of France's 2025 budget avoided the imminent fall of the government, but involved few concessions, including a slower pace of fiscal consolidation.

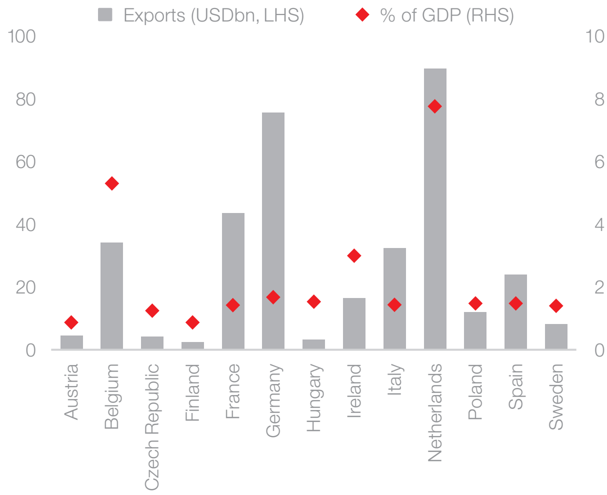
Europe finally readies the ground to increase fiscal spending. German leaders have signalled a marked shift in policy by announcing plans to introduce a special fund for infrastructure investments worth EUR500bn over the coming decade. Incoming

Chancellor Merz also announced an agreement to change the constitutional fiscal debt brake to allow for higher defence spending. These proposals still need the vote in Bundestag, with plans to get it past the outgoing government to expedite the process, as the new coalition will take time to form. Europe's plans to kickstart defence spending depends on evoking the national escape clause of the Stability and Growth Pact, which effectively allows countries with higher deficits (>3% of GDP) to also participate. While plans are favourable, a few things require clarity, including the need for member countries to potentially reorientate existing spending to accommodate the new expenditure requirements (which will dictate extent of growth boost), potential increase in deficits/debts in already highly indebted countries, and bond market reaction to these plans as borrowing costs may rise.

Higher spending was also partially spurred by the need for Europe to assume a bigger role in the region in light of worsening relations between the US and Ukraine. The European Defence Agency estimated EU defence spending at EUR326bn in 2024, up from EUR279bn the year before. Press reports cite discussions of an immediate delivery of air defence systems and deep-precision strike missiles as part of the EUR20bn military package in the works. France and the UK are reportedly spearheading efforts for a one-month peace plan for Ukraine, while the region mulls a military coalition.

On the trade front, the threat of US tariffs linger over the Eurozone. The US was one of the larger destinations for EU exports of goods in 2023 and the second largest partner for EU imports of goods. Of the proposed measures thus far, the most consequential for the zone are the upcoming 25% tariffs on cars, aluminium and steel, semiconductors, and pharma. Reciprocal tariffs in early April are also a risk, although contours of the proposed structure and

Exports to the US by member countries and weightage



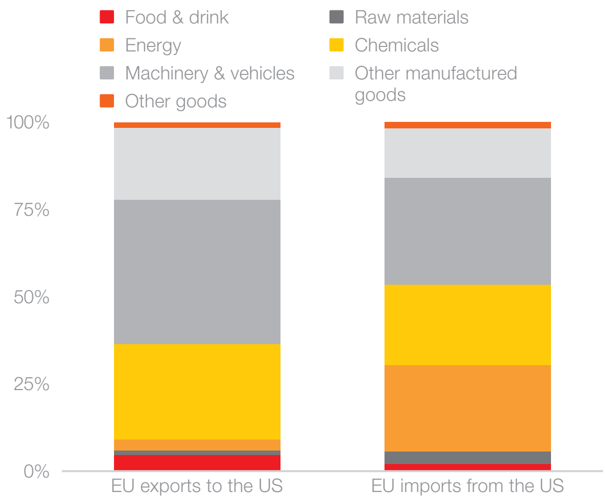
Source: US Census Bureau, DBS

its reach are still unclear. Among the EU members, Netherlands, Germany, France, Belgium, and Italy have the highest exports to the US. Netherlands, Belgium and Ireland signal the highest exposure as a percentage of their GDP.

Among multiple proposals outlined by the US, we see the impact of sectoral action and/non-tariff barriers (VAT) as being more material than reciprocal action. Pharma, machinery and motor vehicles, and energy make up more than a third of EU's exports to the US. For instance, the economic consequence for Netherlands will be significant, given the proposed action on steel and aluminium, cars, pharma, and semiconductors with its rate differentials also wide vs the US.

While the impact on sectors might be material, the risk of reciprocal tariffs is lower as the tariff differential between the US and EU is not as pronounced as it is with Asian economies. For instance, the simple average of the Most Favoured Nation (MFN) trade weighted rate on imports from the US is 1.3% (of the top EU trading partners) vs exports to the US at 1.9%. With the VAT being mentioned as a non-trade barrier and the EU VAT being amongst the highest in the region, that differential will be negative for the bloc.

EU trade with the US - % share (2023)



Source: Eurostat, DBS

We keep 2025 growth projection at 1.0% y/y, from 0.7% y/y in 2024. Household disposable incomes are expected to fare better in the first half of the year, backed by a pick up in real wages and low unemployment rate. The saving rate for households, however, continues to rise, signalling underlying caution. Investment growth remained subdued, while net exports contributed to the headline. Germany's headwinds might receive some support from fresh government spending plans.

The pace of disinflation has, meanwhile, moderated on sticky services. However, this is unlikely to deter the ECB from lowering rates further in 2025. For the ECB, we retain our call for another 50 bps in cuts this year (after 150 bps reduction since 2024), keeping an eye on guidance from Chief Lagarde on whether the Council prefers a pause at the next review to take stock of the recent fiscal developments.

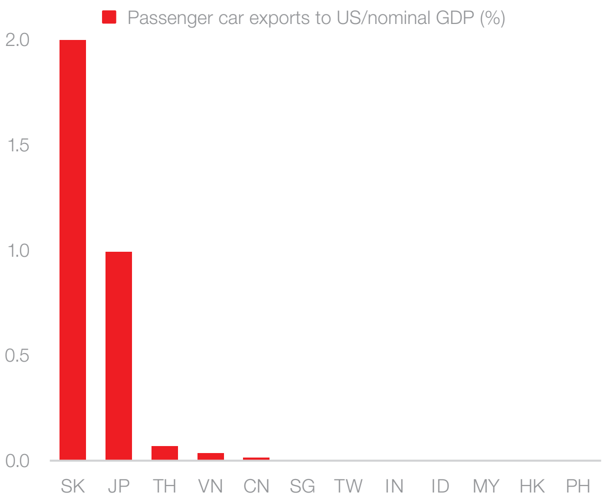
Japan

We maintain our forecast for Japan's economy to grow by 0.9% this year, with modest downside risks. Externally, Japan faces the threat of automotive tariffs from the US as passenger cars are the top product imported by the US from Japan. Japan is the US' second-largest source of car imports, after Mexico. From a macroeconomic perspective, passenger car exports to the US account for c.1% of Japan's GDP. A 25% tariff could reduce Japan's GDP growth by 0.2 %pts due to potential substitution effects from increased US domestic car production.

The reciprocal tariff may not pose the primary challenge. Japan ranks as the US' seventh largest source of trade deficit in 2024, amounting to USD68.5bn. However, Japan's simple average tariff rate for MFN was 3.7% in 2023, almost identical to the US rate of 3.3%. Furthermore, Japan has reduced tariffs on US agricultural and industrial goods under the 2019 Japan-US trade agreement. Japan's VAT is 10%, higher than the US but lower than many European countries. According to the US Treasury's 2024 findings, there is little evidence that Japanese authorities have intervened in the foreign exchange market to weaken the yen.

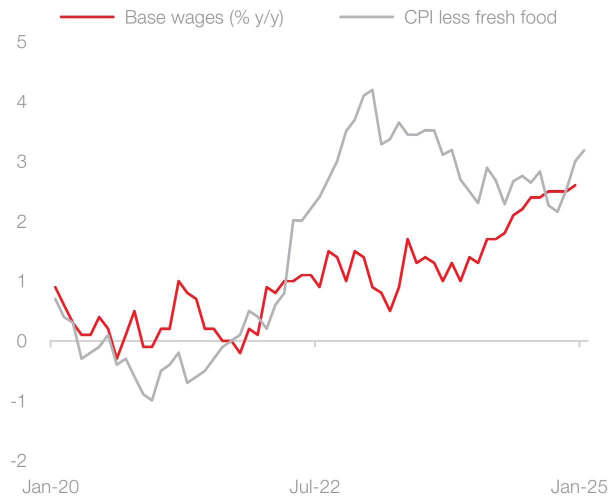
Domestically, consumption is expected to remain weak in 2Q. Japan's largest labour union, Rengo, has secured a 5.46% wage increase during this year's Shunto which includes both the annual scheduled wage increase and base pay rise, similar to last year's initial reading of 5.28%. We estimate that macro-level base wages will rise by 2-2.5% this year, similar to last year's 2.1% increase.

Japan's automobile exports to the US are significant



Source: US Census Bureau, CEIC, DBS

Real wage growth remains negative



Source: CEIC, DBS

Inflation and core inflation are expected to hover around 3% in 2Q before easing to 2% in the second half of the year. Food prices, including vegetables and rice, continue to rise sharply due to domestic supply disruptions and higher costs of raw materials, logistics, and labour. Despite the government's reinstatement of energy subsidies, the lagging effects of yen depreciation are likely to keep imported inflation elevated in 2Q. As a result, real base wage growth is expected to remain negative this quarter, constraining consumer purchasing power.

We maintain our forecast for the BOJ to raise rates by 25 bps to 0.75% in 3Q25. The results of the Shunto wage negotiations and inflation data are likely to fuel expectations for faster BOJ rate hikes in 2Q. However, the weakness in real consumption and real GDP growth will likely discourage the BOJ from acting prematurely. Additionally, the anticipated escalation of tariff threats from the Trump administration in April could further deter the BOJ from raising rates too soon.

Asia

How are China and India managing the noise from the US? China's economy remains under pressure from the property sector which is beset with large unsold inventory, weak transaction volumes, struggles by real estate developers to service their loans, and still-weak sentiments about the price outlook. Despite concerted monetary, fiscal, and regulatory measures to restructure and stabilise, we do not expect the real estate sector to support growth in the near term. However, news about industrial and tech developments, export performance, and market outturn suggest all is not lost in China.

Debt-deflation risks need to be countered with large monetary cushions; the Chinese authorities appear to be providing that. Steady cuts in interest rates and liquidity injection have pushed down borrowing costs and helped narrow corporate spreads. Latest data show green-shoots in the corporate lending space, a prerequisite to a trough.

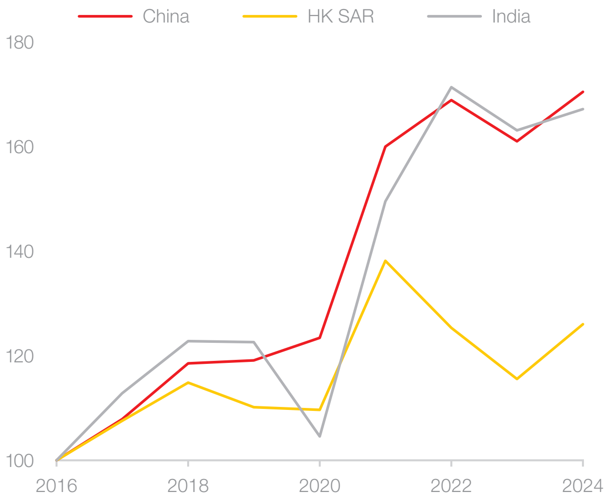
Exports did well in 2024 (+5.9% y/y), hitting a record. The nation's relentless investment in green transition, semiconductor manufacturing, and AI is paying off, forming a high value-added industrial base for the future. Though these take time, the new year has brought a plethora of welcome developments. From Chinese EV and battery manufacturers capturing headlines with ever-widening product offerings and rising sales to local DRAM producers becoming a material player in the global chip market, sentiment around innovation has improved. This was most startlingly portrayed by January's release of DeepSeek's R1 LLM which sent shockwaves through the western AI ecosystem.

China's stock markets have turned ebullient. Hang Seng China Enterprises Index and the Shenzhen Composite Index have marched upward this year. Most striking is the gains of Alibaba, the tech giant which five years ago, stood at the pinnacle of China's corporate hierarchy before undergoing a dramatic fall from grace as a result of regulatory actions. With Jack Ma appearing in public alongside President Xi in recent times and the company announcing strides in several AI-related initiatives, Alibaba is back on the scene.

With Trump 2.0 at the fore, along with an assortment of tariff measures, China will have its hands full externally. Shoring up domestic demand, supporting home-grown industrial capabilities and innovation, and remaining open to international business (ex-US) are China's defensive options.

What about India? After an exuberant summer, India's economy and markets ended 2024 on a soft patch. The three years of robust post-pandemic recovery have lost some of its momentum recently. Spiking food prices muddied the inflation picture, while financial markets took a breather. The rupee has slid in recent months, reflecting an unease over the external outlook.

Exports (2016=100)



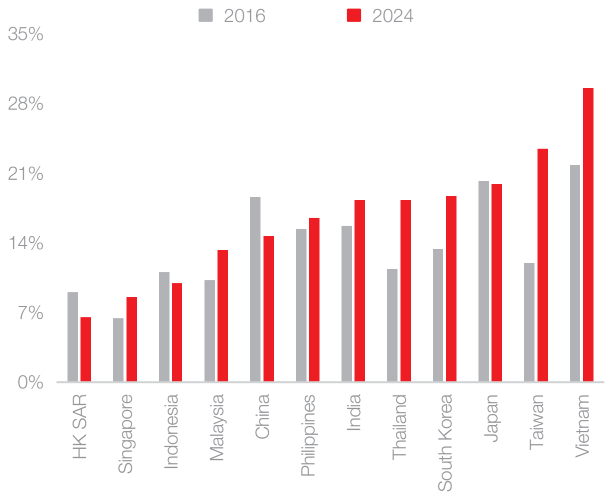
Source: CEIC, DBS

India's post-pandemic recovery has been robust, yet leaves room for improvement. On a real per capita GDP basis, the slide from the pandemic shock has yet to be made up with projections suggesting the gap between pre-pandemic trend and post-pandemic path would persist through the end of this decade.

We see three strategies in motion to address the cyclical weakening:

First, fiscal-monetary easing. The FY25-26 budget contained measures to support producers by improving the ease of doing business and lowering regulatory impediments, along with tax relief for consumers and initiatives to boost employment in the medium-term. The RBI carried out its first rate cut in nearly five years (in Feb 2025). There may not be room for substantial additional stimulus, but the reforms and measures are going in the right direction in our view.

Exports to the US as a share of total exports



Source: CEIC, DBS

The second strategy is vis-à-vis China. The two nations have had a challenging relationship with border disputes, unbalanced trade, and investment access issues creating friction. However, India appears to be displaying a degree of pragmatism in recent times. The movement of capital, technology, and people has gained some momentum lately and we welcome this.

Finally, India has taken a pre-emptive and constructive stance in its dealing with the mercurial Trump administration. By cooperating on undocumented migrant repatriation and reducing tariffs on select US goods in the latest budget, it is clearly signalling its willingness to play ball with the US. Domestic and external challenges may be cause for concern, but India has a clear playbook in place.

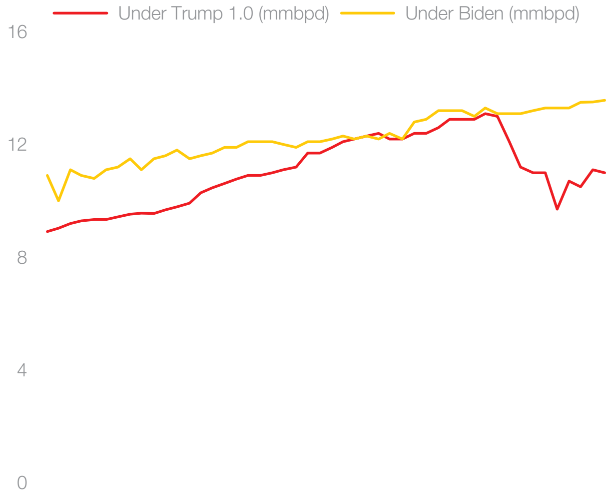
Oil weathers mixed cues under the new Trump era

Oil prices falter after a good start to the year. After a better-than-expected start to the year (i.e. when Brent crude oil prices moved up sharply to above USD80/bbl in early 2025), prices have now settled in the USD70-75/bbl range as of writing which is more in line with our expectations. The upward momentum was largely driven by tighter US sanctions on Russia by the outgoing Biden administration in the US. New sanctions targeting Russia's shadow tanker fleet have the potential to disrupt Russian oil exports to China and India, the biggest buyers of Russian oil. Russia exports around 4-5mmbpd of oil currently and up to 1.5mmbpd of exports could be affected by the sanctions in the coming months unless alternate routes are found. In addition, the unofficial flows of oil from Iran to China are coming under greater scrutiny with the Trump administration at the fore. Without these developments, we would expect Brent crude oil prices to be rangebound at USD70-75/bbl in the near-to-medium term with strong downside support at USD70/bbl.

Brent crude oil prices moderate after a strong start to the year in 2025

Source: Bloomberg, DBS

US oil production trends under recent presidents



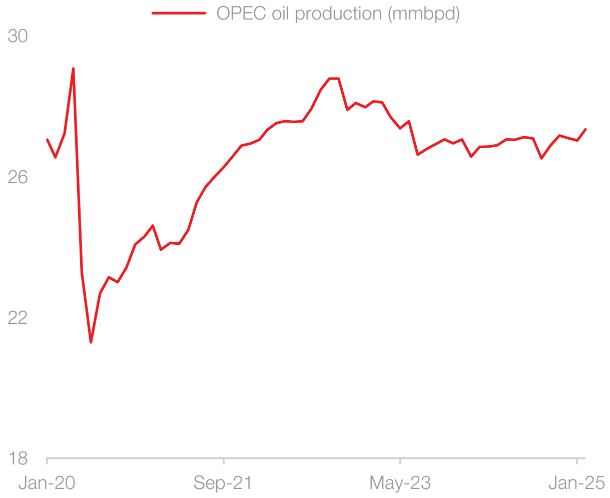
Source: Bloomberg, DBS

Impact of Trump 2.0 on the oil market not so straightforward. A second Trump presidency could significantly impact the oil market, but the effects are not straightforward. Trump's focus on American energy dominance is well-known, for example, withdrawing from the Paris Agreement and declaring a "national energy emergency" to expedite fossil fuel projects. This aligns with his past "drill, baby, drill" campaign promises and plans to loosen regulations on the US energy industry. However, it is not as simple as more drilling. While reduced regulations could boost US oil production, the industry primarily reacts to market forces instead of depending solely on government policies. We have already seen significant increases in US shale oil production under President Biden. Therefore, while a Trump administration might create a more favourable environment for production growth, massive increases are not guaranteed. Oil companies will ultimately base their decisions on market demand and profitability.

Geopolitical risk premium lower but uncertainties remain. The Israel-Hamas ceasefire in January (which preceded Trump's return to office) presented the first signs of conflict resolution and possible return of peace in the Middle East. It could be a significant turning point in the 15-month saga in the Gaza strip. While the jury is still out on whether these de-escalation moves will eventually be successful, the risks of the Middle East flashpoint exploding are on the backburner for now, removing a key upside risk for oil. Meanwhile, Trump's potential efforts to de-escalate the Russia-Ukraine conflict could lead to the lifting of sanctions on Russian oil, easing the pressure on global supply chains. Conversely, tougher sanctions on Iran could tighten the global oil market, potentially helping OPEC+ to restore supplies gradually without creating a huge surplus. In short, expect price volatility as these mixed cues play out.

OPEC+ will have to bite the bullet and slowly start to increase supplies from April. OPEC+ has delayed restoring the voluntary cuts, totalling 2.2mmbpd, several times in the last few months. As of early Mar 2025 however, OPEC+ has decided to go through with its production increase starting Apr 2025, adding around 0.14mmbpd per month; its first step towards unwinding the cuts by Sep 2026. This is the first output hike by OPEC+ since 2022. However, the OPEC+ supply response will continue to remain flexible depending on market conditions. If oil prices fall below the USD70/bbl mark for an extended period, output hikes may be paused in our opinion. We reckon the group (led by Saudi Arabia and Russia) would prefer to ensure market stability—meaning higher oil prices—at the continued cost of market share for OPEC+.

OPEC+ supplies will increase from hereon for the first time since 2022



Source: Bloomberg, DBS

We maintain our forecast of a moderate oil price environment. Brent crude oil prices are likely to moderate overall from the 2024 average of USD80/bbl as demand-side risks have risen, supplies from OPEC+ are set to gradually return, and the risks of crises in the Middle East and Russia-Ukraine theatres have diminished. We maintain our conservative base-case for Brent crude oil price forecast of USD70-75/bbl in 2025, owing to the prevailing demand risks. We introduce our 2026 Brent crude oil price forecast at USD67-72/bbl, slightly weaker than 2025, given the expected higher quantum of supply increase from OPEC+ in 2026.

Quarterly average oil price forecast 2025/26 – DBS base case view

(USD per barrel)	1Q25	2Q25F	3Q25F	4Q25F	1Q26F	2Q26F	3Q26F	4Q26F
Average Brent crude oil price	75.0	72.0	74.0	75.0	71.5	69.0	70.0	67.0
Average WTI crude oil price	72.0	69.0	71.0	72.0	68.5	66.0	67.0	64.0

Source: DBS

GDP growth and CPI inflation forecasts

	GDP growth, % y/y						CPI inflation, % y/y, ave					
	2021	2022	2023	2024	2025F	2026F	2021	2022	2023	2024	2025F	2026F
China	8.1	3	5.2	5	5	4.5	0.9	2.2	0.2	0.6	1	1.5
Hong Kong SAR	6.3	-3.5	3.3	2.5	2.5	2.5	1.6	1.9	2	1.5	1.5	1.5
India	10.3	7.2	8.7	6.5	6.5	6.5	5.1	6.7	5.7	4.9	4.1	4
India (FY basis)*	9.7	7.6	9.2	6.5	6.4	6.4	5.5	6.7	5.4	4.7	4.2	4
Indonesia	3.7	5.3	5.1	5	5.1	5.1	1.6	4.2	3.7	2.3	2	2
Malaysia	3.3	8.9	3.6	5.1	4.8	4.6	2.5	3.4	2.5	1.8	2.8	2.3
Philippines	5.7	7.6	5.6	5.6	5.8	5.6	3.9	5.8	6	3.2	2.6	2.4
Singapore	9.8	4.1	1.8	4.4	2.8	2.5	2.3	6.1	4.8	2.4	1.3	1.7
South Korea	4.6	2.7	1.4	2	1.7	2.2	2.5	5.1	3.6	2.3	2	2
Taiwan	6.7	2.7	1.1	4.6	3	2.4	2	2.9	2.5	2.2	1.9	1.7
Thailand	1.6	2.6	2	2.5	2.6	2.4	1.2	6.1	1.2	0.4	1.2	1.5
Vietnam	2.6	8	5	7.1	6.8	6.6	1.8	3.2	3.3	3.6	3.5	3.3
Eurozone	5.3	3.5	0.5	0.7	1	1.2	2.6	8.4	5.5	2.3	2.2	2
Japan	2.7	0.9	1.5	0.1	0.9	0.6	-0.3	2.5	3.3	2.7	2.7	1.8
United States	5.9	2.1	2.5	2.8	2	2	4.7	8	4.1	3	2.6	2.5

*2020 represents Fiscal 21; ending Mar 21

Source: CEIC, DBS

Policy interest rates forecasts, eop

	1Q25	2Q25	3Q25	4Q25	1Q26	2Q26	3Q26	4Q26
Mainland China*	3.1	2.95	2.8	2.8	2.8	2.55	2.55	2.55
India	6.25	5.75	5.75	5.75	5.75	5.75	5.75	5.75
Indonesia	5.5	5.25	5.25	5.25	5.25	5.25	5.25	5.25
Malaysia	3	3	3	3	3	3	3	3
Philippines	5.75	5.25	5.25	5.25	5.25	5.25	5.25	5.25
Singapore**	2.88	2.88	2.73	2.63	2.63	2.63	2.63	2.63
South Korea	2.75	2.5	2.5	2.5	2.5	2.5	2.5	2.5
Taiwan	2	2	2	2	2	2	1.875	1.875
Thailand	2	2	1.75	1.75	1.75	1.5	1.5	1.5
Vietnam***	4.5	4.5	4.5	4.5	4.5	4.5	4.5	4.5
Eurozone^	2.5	2	2	2	2	2	2	2
Japan	0.5	0.5	0.75	0.75	0.75	1	1	1
United States	4.5	4.5	4.25	4	4	4	4	4

*1-yr Loan Prime Rate; ** 3M SORA OIS ; *** Refinancing Rate; ^ Deposit Facility Rate

Source: CEIC, DBS

Exceptionalism Challenged

US Equities
2Q25

The pursuit of an ”America First” agenda and ensuing policy chaos weigh on business confidence and economic activities. Yet, inflation stays stubbornly high, restricting the Fed’s ability to cut rates. Maintain US tech for secular growth and add healthcare for defensive plays.

03.
US Equities.

Dylan Cheang
Strategist

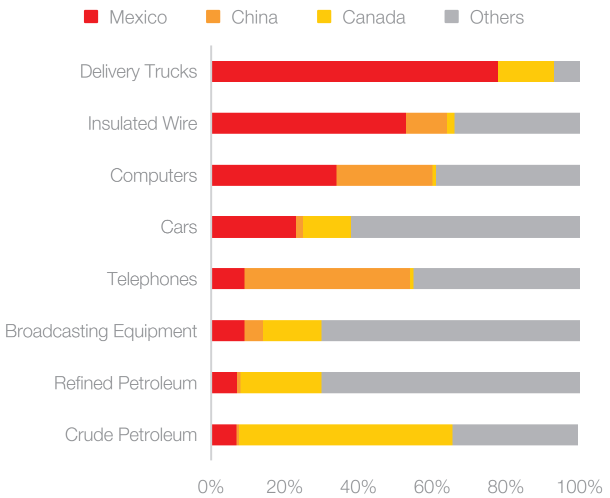
Policy chaos and the demise of US exceptionalism. The story of US equities is a curious case of "self-inflicted pain". Just when the S&P 500 was basking in the glory of being the "only game in town" following Trump's election victory, the market gave up all its gains and started heading towards correction territory. The abrupt turnaround in fortunes lies squarely on the surge in policy uncertainties with the new administration unleashing a global tariff war and reshaping the world order with its "America First" agenda. The ensuing chaos is starting to weigh on business confidence and economic activities. ISM Manufacturing, for instance, fell to 50.3 in February and edged closer to contractionary territory while forecast from Atlanta Fed's GDPNow is pointing to a -2.4% decline in GDP (vs a growth of 2.6% at the start of the year).

US consumers, meanwhile, are stuck between a rock and a hard place. Weakening macro conditions and looming job cuts coincided with plunging consumer confidence – which saw a 7-points dip to 98.3 in February, the biggest decline since Aug 2021 – while retail sales similarly corrected by 0.9% in January, the sharpest in two years. Yet, despite the dire consumption outlook, inflation remains stubbornly high and will only get worse if the tariff war escalates from here. Trump's imposition of tariffs on Mexico, China, and Canada will affect a wide range of goods from delivery trucks and cars to petroleum – a strangely ironic situation considering Trump had made combating inflation the central rethoric of his re-election campaign. The political optics of the new administration inflicting tariff pains at a time of resurgent inflation will not go down well with the American consumer.

Policy chaos dimming US economic outlook

Source: Bloomberg, DBS

US imports affected by tariff war



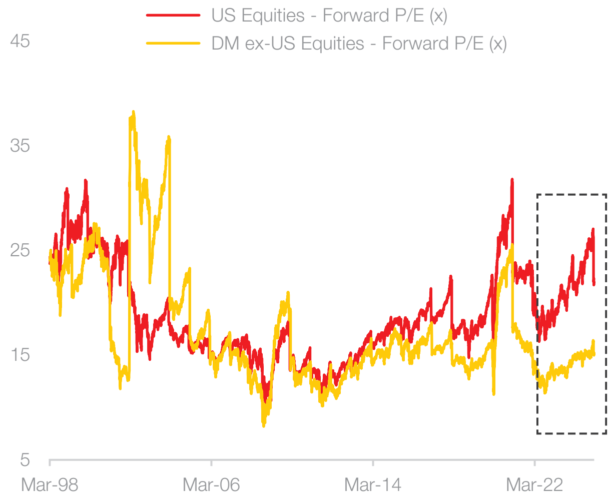
Source: Bloomberg, DBS

When the unthinkable becomes reality – Investors "de-risking" from US equities. The acute correction on the S&P 500 and Nasdaq says it all. Investors are actively switching out of US equities to fund their positions in Europe and China. The very notion of "de-risking" from US equities, unthinkable just a month ago, is now becoming a reality. Under the "America First" policy agenda, the very rule-based global system that has served America so well for decades is crumbling. And with Trump announcing that this is "just getting started", we see no immediate end in sight for the portfolio shifts away from the US.

Funds are pre-emptively switching out of the US based on expectations of a darkening economical and geopolitical mood. The change in sentiments, unfortunately, is coming at a time when US equities are trading at huge valuation premiums relative to the rest of the world. A "priced for perfection" market will need to see substantial unwinding before the negatives are fully priced-in and this is just only getting started. Forecasted earnings for the S&P 500 suggest that the downside has yet to be reflected in analysts' forecasts and we anticipate more weakness ahead when downward earnings revisions begin.

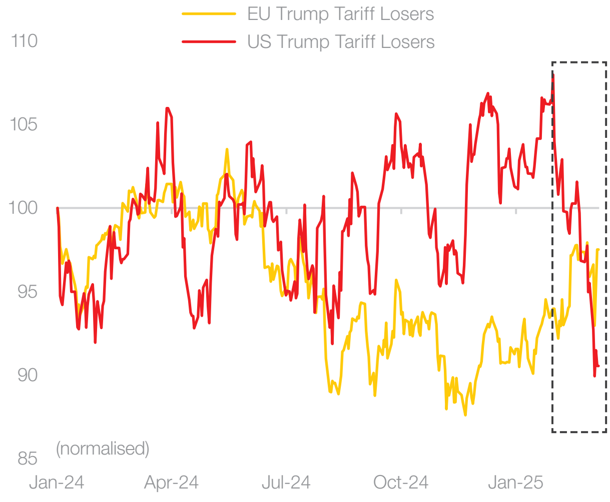
Meanwhile, if the new administration thinks that they are "winning" this trade war, anecdotal evidence is suggesting otherwise. The "US Trump Tariff Losers" thematic basket, which tracks the performance of US stocks negatively exposed to Trump's tariffs, has seen sharp correction since late-January while its European counterpart remains on a gradual uptrend. This suggests that the tariffs are hurting US companies more than their European peers.

US trades at a valuation premium compared to other developed markets



Source: Bloomberg, DBS

The tariffs war is hurting US companies more than the European ones



Source: Bloomberg, DBS

2Q25 US Sector Strategy – Defensive shifts

Changing times call for changing strategy. Policy chaos means that businesses will hold back on their investment decisions until further clarity emerges. Similarly for consumers, purchases of big-ticket items will be postponed until the economic fog is lifted. Under such conditions, the US economic momentum will moderate, necessitating a recalibration of our US sector strategy. A more defensive tilt is necessary with the recent performance of US sectors already reflecting this new reality.

On a YTD basis, “crowded trades” like technology and consumer discretionary have lost 8.7% and 10.2% respectively (as at 6 Mar) while defensive sectors like healthcare (+8.6%) and consumer staples (+6.9%) have outperformed. For 2Q25, the key switches that we are making to our US sector allocation are:

- <u>Upgrade consumer staples to overweight:</u> Should economic conditions moderate from here, we expect consumer staples to outperform consumer discretionary as the former provides essential goods. Demand for consumer staples tends to be more inelastic and resilient to economic headwinds. Companies providing “value” goods selling at more affordable price points will see greater demand from consumer down trading.

  In the hypermarts space, companies with a stronger focus on private labels will benefit as the latter enhances customer loyalty and offer higher gross margins. Additionally, in an era of rising trade tension, we also favour companies that rely less on overseas suppliers. Walmart, for instance, has reduced its exposure to Chinese suppliers from 80% in 2018 to 60% in 2023 with further reductions expected.

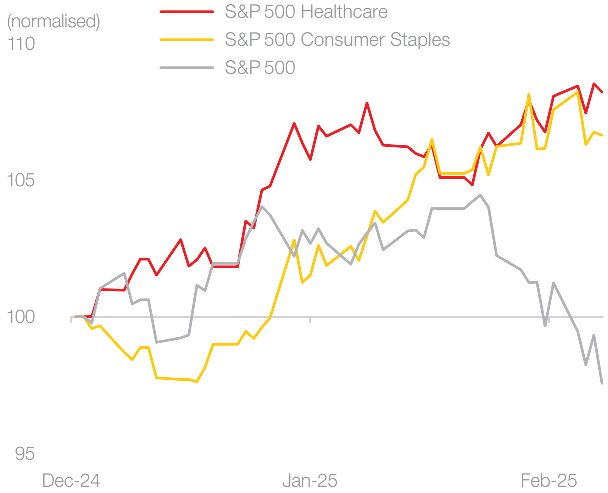
- <u>Upgrade utilities to neutral:</u> Demand for utilities tends to be very resilient during economic slowdowns due to its provision of necessities like electricity, water, and gas. However, investment merit is partly offset by policy headwinds arising from the new administration’s approach to energy transition. Its withdrawal from the Paris Climate Agreement and the suspension of offshore wind power leases could all translate to higher equipment and material costs for renewables companies. Hence a neutral rating is warranted.

- <u>Downgrade consumer discretionary to underweight:</u> US domestic consumption is expected to face substantial headwinds from (1) new immigration policies that will drive down the number of undocumented migrants in the country, (2) aggressive job cuts by the Department of Government Efficiency (DOGE), and (3) the prevalence of sticky inflation and weak affordability. In such an environment, non-essentials within the consumer discretionary space will experience weaker demand.

  Following Trump’s election victory, our initial assumption is for the consumer discretionary sector to be boosted by taxation cuts. But given recent policy chaos and the plunge in consumer confidence, this thesis is now off the table as we expect the negatives arising from policy uncertainties to supersede the positives from lower taxes.

- Downgrade energy to neutral: We are downgrading the energy sector to neutral given the absence of catalysts. Brent crude oil prices are expected to moderate from 2024's average price of USD80/bbl to between USD70-75/bbl in 2025 given (1) rising demand risks, (2) gradual increase in supply from OPEC+, and (3) diminishing geopolitical risks on the Middle East and Russia-Ukraine front.

Boring is good – healthcare and consumer staples are leading the way in the US



Source: Bloomberg, DBS

US Sector Allocation – 2Q25

	Overweight	Neutral	Underweight
US Sectors	Technology	Industrials	Real Estate
	Comm. Services	Utilities	Materials
	Healthcare	Energy	Cons. Discretionary
	Financials		
	Cons. Staples		

US Sector Key Financial Ratios

	Forward P/E (x)	P/Book (x)	EV/EBITDA (x)	ROE (%)	ROA (%)	OPM (%)
S&P 500 Index	21.3	4.9	15.8	18.3	4.1	14.4
S&P 500 Financials	16.7	2.4	7.9	14.0	1.7	20.3
S&P 500 Energy	14.1	2.0	7.9	13.3	6.4	11.0
S&P 500 Technology	35.0	11.9	26.5	29.8	12.7	26.3
S&P 500 Materials	21.4	2.9	12.5	11.5	4.9	12.5
S&P 500 Industrials	22.5	6.2	16.3	24.1	6.7	12.5
S&P 500 Cons. Staples	22.8	7.0	17.3	24.7	7.6	7.3
S&P 500 Cons. Discretionary	25.1	8.8	17.2	30.2	7.9	11.4
S&P 500 Comm. Services	19.1	4.8	13.6	20.0	8.2	21.9
S&P 500 Utilities	17.2	2.2	12.6	11.1	2.8	21.1
S&P 500 Real Estate	37.8	3.1	20.0	7.6	3.2	23.2
S&P 500 Healthcare	18.3	5.2	17.1	14.4	4.9	6.8

Source: Bloomberg
* Data as at 6 Mar 2025


Source: Unsplash

From MAGA to MEGA

Europe Equities
2Q25

Eurozone growth remains weak despite easing inflation and ECB rate cuts. Manufacturing and consumer spending struggle, but the defence sector outperforms. Germany's proposed fiscal expansion could drive a historic shift and boost sentiment. Upgrade Europe to overweight amid positive momentum.

04. Europe Equities.

Joanne Goh
Strategist

Europe has been the strongest-performing region YTD, with an uplift of its 12-month forward P/E to 14.5x. Equity risk premium has compressed to a 10-year low due to these factors: -

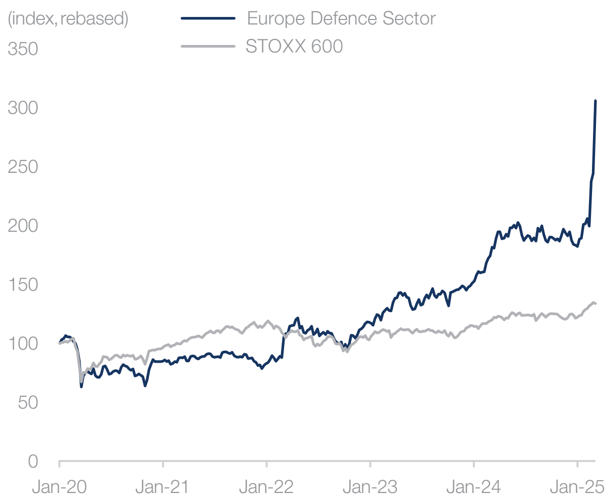
1. Rotation from growth to value, as Europe trades at half of US' valuations;
2. Re-rating of global banks, including Eurozone's "higher-for-longer" narrative
3. Speculation of a potential Ukraine peace deal
4. Outperformance of Europe's defence sector amid discussions on increased defence spending in Germany and across the bloc

The European defence sector continues to be a crucial industrial pillar, particularly in Germany, and is outperforming amid shifting geopolitical dynamics. With a newly elected government focused on economic expansion, the sector appears well-positioned for further gains, potentially boosting the STOXX 600 index.

Germany's incoming Chancellor, Friedrich Merz, has proposed a EUR500bn infrastructure fund and signalled a significant increase in defence spending, with projections suggesting fiscal expansion of up to 5.5% of GDP. This bold move has also prompted discussions within the EU about loosening fiscal constraints.

Despite lingering challenges and skepticism, if these measures are implemented, they could mark a historic shift for Europe's traditionally cautious fiscal stance. Given this positive momentum, we are upgrading our European outlook to overweight.

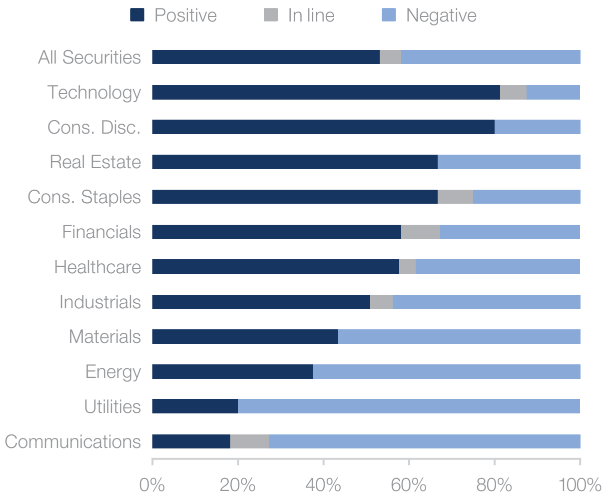
Outperformance in defence sector



Source: LSEG, DBS

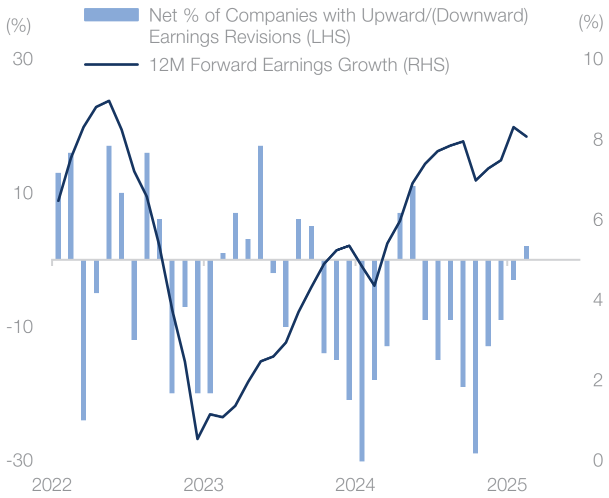
Slower-for-longer growth. While Eurozone inflation has eased, growth remains subdued. Despite lower borrowing costs, manufacturing remains in recession, consumer spending is weak, and investments are constrained by trade war fears. The ECB has cut rates six times since Jun 2024 and may need to cut further. France's economy contracted last quarter, and German retail sales stagnated, reinforcing signs of economic inactivity. We maintain the 2025 GDP growth projection at 1.0% y/y, up from 0.7% y/y in 2024, as an increase in Germany's defence spending is likely to have a positive but insignificant impact on the region in our view.

4Q earnings beat for STOXX 600 companies



Source: Bloomberg, DBS

No earnings upgrades despite earnings beat



Source: LSEG, DBS

Mixed earnings signals. 4Q24 earnings have been relatively strong, with >54% of companies beating expectations. Key highlights include:

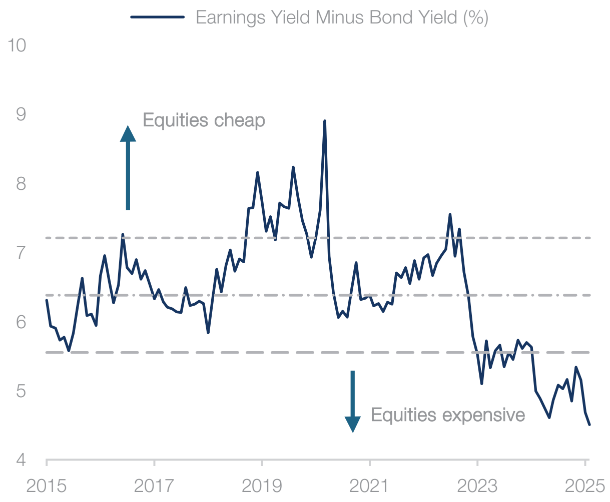
- **Positives:** Strong order books and cloud momentum in tech (SAP, ASML), resilient healthcare earnings, and company-specific outperformance in consumer discretionary, (Adidas, Burberry, Hermès, Richemont). software, healthcare, and real estate saw positive revisions.
- **Negatives:** Beverages/Cognac players cut guidance on destocking and China tariffs. Autos faced tariff headwinds, with Porsche issuing a profit warning due to weak BEV demand.
- **Mixed:** Banks showed strong capital returns but lacked guidance upgrades; cost containment varied across players like ING and Deutsche Bank.

Despite the earnings beat, only 1.5% of companies have seen upward revisions, with 2025 earnings growth forecasts steady at 7.2%. Basic resources, autos, and chemicals – sectors vulnerable to global trade risks – have seen the sharpest downgrades.

Valuations and trade risks. European equities trade slightly above their 10-year average P/E, yet appear expensive relative to bonds due to high bond yields. Even after multiple ECB rate cuts, the yield curve has steepened as sovereign risks remain elevated due to high fiscal deficits.

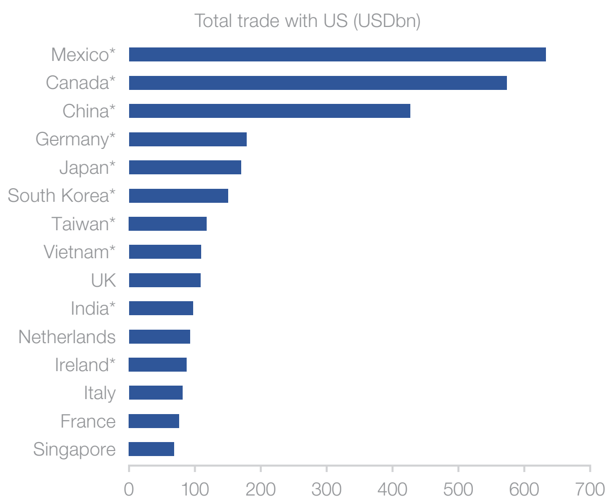
While a potential Ukraine peace deal could lower energy costs and boost economic confidence – benefitting banks, energy, industrials, and defence – the outcome is uncertain. Additionally, Europe's large trade surplus with the US makes it a likely target for tariffs. While tariffs themselves matter, broader trade uncertainty could weaken investment sentiment and economic growth. Key export sectors – machinery/ equipment, pharmaceuticals, and chemicals—are particularly exposed. Germany, Ireland, Netherlands, Italy, and France are among the most vulnerable economies. Europe also has a high exposure to China, adding another layer of risk.

Eurozone's equity risk premium (earnings yield – bond yield) compressed to a 10-year low



Source: LSEG, DBS
Note: Bands are average and +/- one standard deviation lines

Trade tariffs likely to hit Europe



Source: LSEG, DBS
*Denotes top 10 countries with trade deficits with US

Stay with quality global leaders. While not spared from macro uncertainty and tariff risks, globally competitive businesses with strong moats remain well-positioned. Preferred sectors include:

Defence & Aerospace: Structural growth and policy shifts

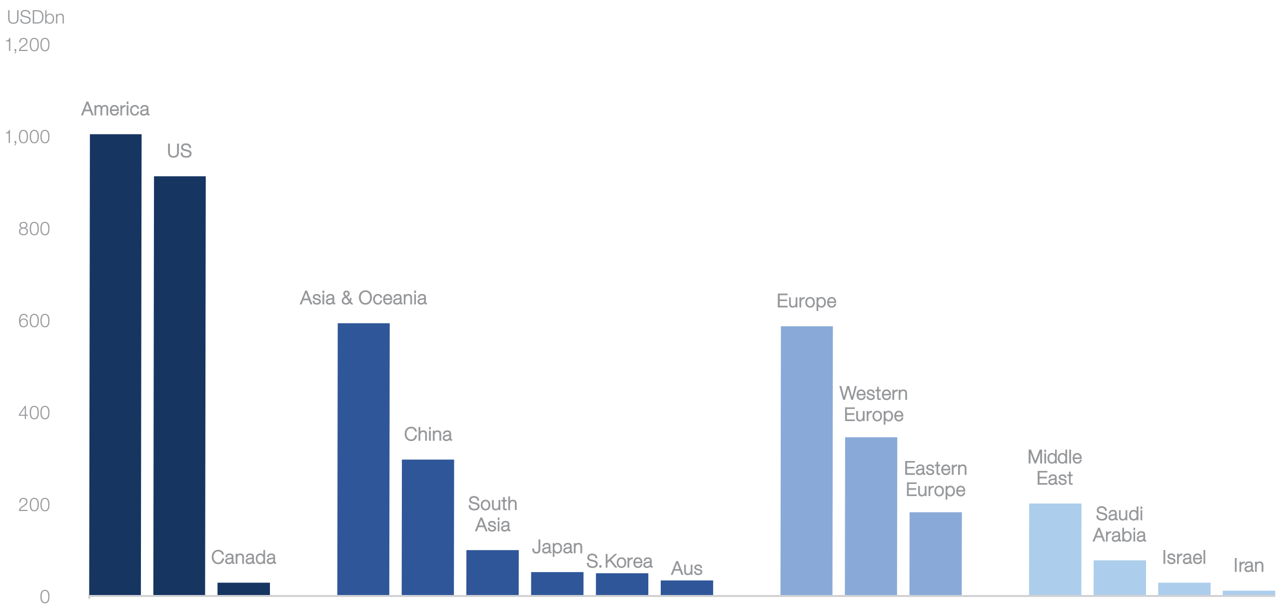
The EU faces a growing need for structurally higher defence spending, driven by geopolitical tensions and evolving security threats. With increasing concerns over regional stability, European nations are reassessing their military budgets to enhance defence capabilities and reduce reliance on external allies.

A key development is the potential increase in NATO's defence spending target for EU countries. Currently set at c.2% of GDP, discussions are emerging about raising it to 3%. If implemented, this would translate to a significant 50% increase in defence budgets across the Eurozone compared to 2024 levels. Such an uplift would accelerate investments in advanced weaponry, cybersecurity, space defence, and modernisation of military infrastructure.

However, uncertainty remains, particularly regarding geopolitical developments such as a potential ceasefire in Ukraine. A de-escalation of conflict could lead to shifts in defence priorities and spending allocations. Additionally, the US Department of Defence (DoD) has signalled potential budget cuts, which may impact transatlantic defence collaborations and procurement plans for European allies.

Despite these variables, the structural push toward stronger defence and aerospace investments in Europe is likely to persist. Companies operating in

Global defence spending breakdown by region



Source: SIPRI , DBS

the sector could benefit from increased government contracts, expanded R&D funding, and growing demand for next-generation defence technologies.

Health & Wellness

Europe's health and wellness sector is set for long-term expansion, driven by demographic shifts and rising healthcare needs. A key factor is the aging population, as the global senior population is projected to double to 1.6bn by 2050. This demographic shift will place increasing demand on healthcare services, pharmaceuticals, and wellness-related products, creating sustained opportunities for companies operating in the sector.

However, potential risks remain, particularly regarding drug pricing pressures, as governments and regulators push for cost containment in healthcare.

To navigate these challenges, investors may focus on companies with strong fundamentals and resilient demand. These include:

1. Pharmaceutical companies with a strong growth pipeline of innovative drug portfolio and ongoing R&D investments;
2. Leaders in medical technology and diagnostics, which should continue to see strong demand for healthcare solutions, supported by long-term contracts and hospital investments
3. Companies with essential and recurring sticky consumer demand which can offer stability in the face of pricing pressures. Their products remain indispensable as aging populations prioritise wellness, vision care, and nutrition

Secular Winners: Key themes driving long-term growth

Europe is witnessing a structural shift across key industries, positioning certain sectors as secular winners amid technological advancements, infrastructure upgrades, and sustainability goals.

1. **Electrification: Modernising aging power grids**

   With 40% of Europe's distribution grids over 40 years old, the region faces an urgent need for modernisation. Aging infrastructure is increasingly unable to support growing electricity demand from industries, households, and the expanding adoption of EVs. To meet future energy needs and integrate renewable sources, grid capacity is expected to double by 2030. This transition will drive significant investment in power transmission, smart grids, and energy storage solutions, benefitting companies involved in electrical infrastructure, automation, and digital energy management.

2. **Leading-Edge Technology: Semiconductor race for innovation**

   The global demand for advanced semiconductor chips continues to rise as nations and industries compete to lead in AI, automation, and digital transformation. Europe is investing heavily in semiconductor manufacturing to reduce reliance on foreign supply chains and enhance technological self-sufficiency. Governments and corporations are supporting initiatives to develop leading-edge semiconductor technology, focusing on high-performance computing, 5G, and AI-driven applications. Companies in the semiconductor equipment and materials supply chain are well-positioned to benefit from this long-term trend.

3. **Clean Energy & Water Scarcity: Addressing critical needs**

   As Europe accelerates its transition toward clean energy, investment in renewable sources such as solar, wind, and hydrogen is set to rise. However, with increasing industrial and urban demand, water scarcity has emerged as a growing concern. The need for efficient water management, desalination, and wastewater recycling solutions is becoming a priority. Companies specialising in water treatment, infrastructure modernisation, and sustainable resource management are expected to play a vital role in addressing this challenge.

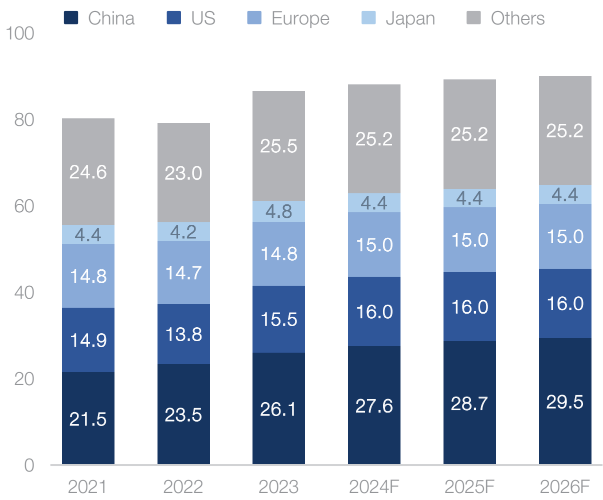
Sector preferences

Our sector preferences are guided by key structural trends, including electrification, semiconductor advancements, clean energy, healthcare demand, and defence spending. These long-term shifts present strong investment opportunities in industries with sustained growth potential. Based on these factors, we recommend focusing on sectors with enduring secular tailwinds while exercising caution in areas facing near-term challenges and structural downturns.

Within the consumer discretionary sector, we maintain a strong preference for the luxury segment, particularly brands that are aligned with quiet luxury, while remaining cautious of the autos sector. The share of luxury purchases tied to tourist spending has rebounded from 30% in 2023 to 35% in 2024 and is expected to normalise around 40% in 2025. Additionally, global tourism is set to expand by approximately 12% y/y in 2025, surpassing 1.6bn arrivals and exceeding pre-pandemic levels. Quiet luxury brands are well-positioned to capitalise on this trend, as affluent consumers increasingly prioritise understated elegance and superior craftsmanship over conspicuous wealth, supporting sustained long-term growth.

Conversely, the outlook for European OEM carmakers remains uncertain. While recent earnings were largely in line with expectations, with solid cash flow generation across the board, investor focus has shifted toward management guidance, which has been mixed at best. Foreign automakers continue to lose market share in China and face stiff competition from Chinese brands locally, while rising political uncertainty in Europe is complicating the region's EV transition. In key markets like Germany and France, government support for EV adoption is waning, with policy reversals further clouding the outlook. As a result, OEMs will likely face margin pressures, as reduced state incentives will force companies to invest more in carbon credits to offset emissions, increasing production costs and weighing on profitability.

Europe auto sales volume



Source: S&P Mobility, DBS

Europe Sector Allocation – 2Q25

	Overweight	Neutral	Underweight
Europe	Technology	Cons. Discretionary*	Real Estate
	Industrials	Financials	Materials
	Healthcare	Utilities	Cons. Staples
		Energy	Comm. Services

*Overweight luxury, underweight autos

Valuation table

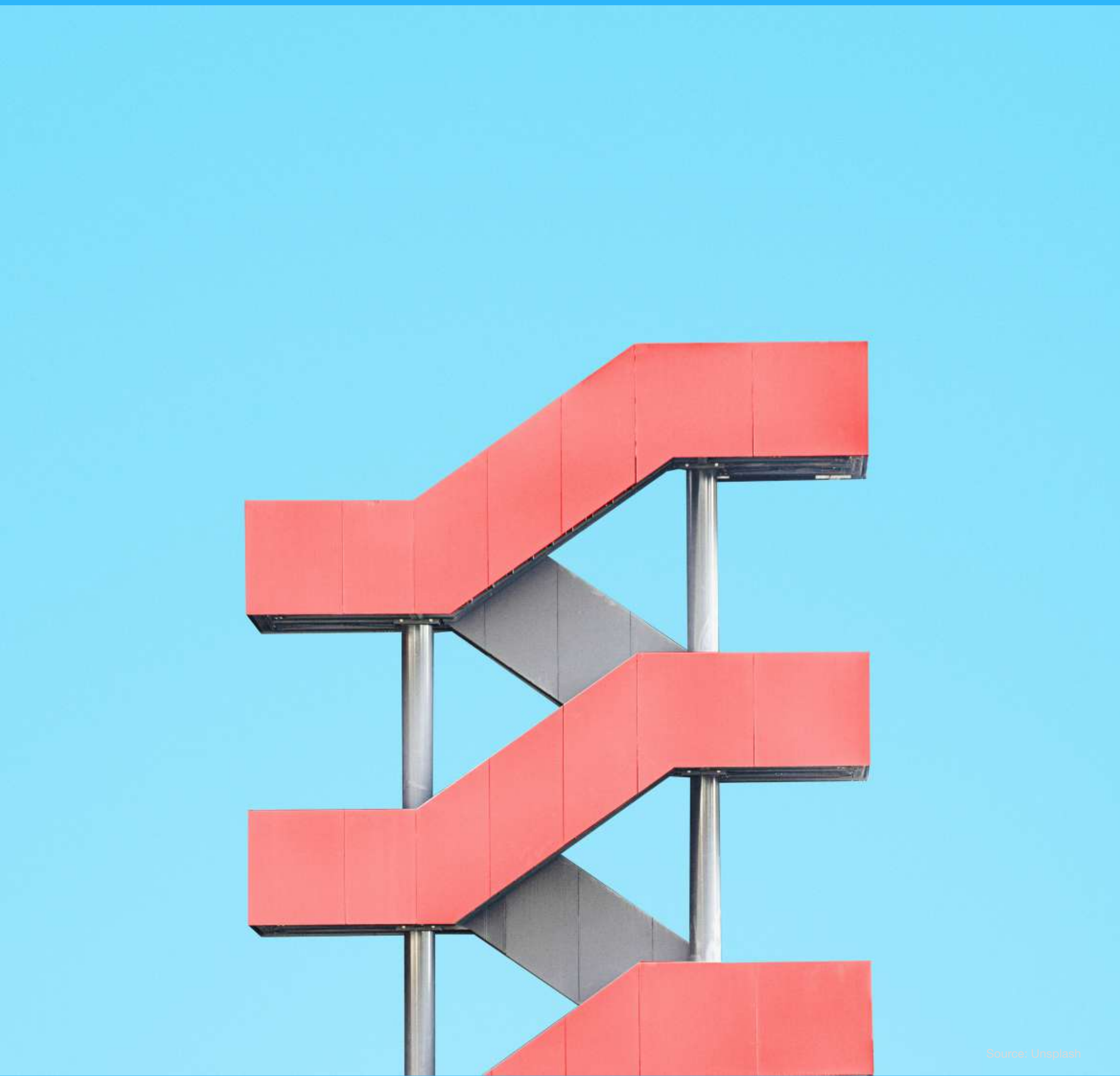
	Forward P/E (x)	P/Book (x)	EV/EBITDA (x)	FW ROE (%)	ROA (%)	OPM (%)
Europe	14.6	2.1	10.5	13.2	1.5	12.9
EU Financials	10.5	1.3	-	12.2	0.7	17.3
EU Energy	8.6	1.1	3.9	12.4	3.3	10.0
EU Technology	27.3	5.1	21.3	16.0	6.8	16.0
EU Materials	16.1	1.8	9.5	10.0	2.9	7.9
EU Industrial	20.9	3.8	12.3	16.5	5.0	10.6
EU Cons. Staples	15.9	3.1	11.6	17.7	5.0	10.8
EU Cons. Discretionary	17.2	1.9	7.3	10.7	4.3	9.5
EU Comm. Services	19.0	1.7	7.4	9.4	1.9	14.1
EU Utilities	11.0	1.6	8.1	12.5	2.7	13.4
EU Real Estate	13.4	0.8	-	2.9	-1.1	-18.1
EU Healthcare	16.0	3.8	14.8	17.8	5.3	16.7

Source: Bloomberg, DBS

Upward Momentum

Japan Equities
2Q25

BOJ is set to continue gradual policy normalisation after its January rate hike, supported by sustained inflation, strong wage growth, and resilient earnings. Alongside ongoing corporate reforms, this would boost market sentiment, despite a stronger yen.



Source: Unsplash

05. Japan Equities.

Joanne Goh
Strategist

Domestic transformation gains momentum. Japanese equities have underperformed YTD, weighed down by three key concerns: (1) the risk of additional tariffs under Trump 2.0, (2) uncertainty in a higher interest rate environment amid BOJ policy normalisation, and (3) heightened volatility of the yen. However, we believe that these headwinds will subside, paving the way for the market to regain its upward momentum.

Japan's ongoing domestic transformation, driven by corporate governance reforms, economic policy shifts, and structural improvements, is expected to sustain market strength into the second half. This period will further underscore the resilience of Japanese companies, as management teams continue to execute reforms and adapt to evolving economic conditions, reinforcing a strong bottom-up growth story.

Tariff resilience. Japan is likely to be less impacted by potential US tariffs compared to other countries, and relative to the first Trump administration. In 2015, Japan ranked third globally in its trade surplus with the US, but by 2023, it had improved its position to fifth by curbing surplus growth and increasing direct investments through expanding auto manufacturing production within the US and more. Japan has further room to narrow its trade surplus by boosting imports of US energy-related products. Additionally, Japan's limited trade exposure to Canada and Mexico, which are subject to US tariffs alongside China, reduces its vulnerability to broader tariff policies.

Current reforms trailing the "Abenomics" era – paused for now

Source: LSEG

Strengthening economic ties. Defence spending is another key focus in Trump 2.0, where Japan has already taken proactive steps. Under its five-year plan initiated in 2022, Japan is doubling its defence budget as a percentage of its GDP. To maintain a favourable US-Japan relationship, Japan is increasing LNG procurement from the US and expanding US-bound investments by Japanese corporations, mirroring strategies seen under the first Trump administration.

While broad US tariffs on sectors like autos and pharmaceuticals would impact Japan, the latter is not a major export category. The auto sector, Japan's largest export to the US, has strategically mitigated risks by ramping up local production. In 2023, Japanese automakers produced over 3.2mn vehicles in the US, while direct imports from Japan stood at approximately 1.3mn. If Trump's tax cuts are reinstated, Japan's US-based car production is likely to benefit.

While tariffs may create near-term challenges, Japan's long-term strategy of diversifying investments and strengthening economic cooperation with the US, positions it well to navigate potential policy shifts.

Steady normalisation amid yen strength. The BOJ is expected to continue its gradual monetary policy normalisation following its rate hike in January. Several factors including sustained inflation, robust wage growth, a strong current account surplus, a more balanced Federal Reserve stance, and resilient corporate earnings, have strengthened the BOJ's confidence in advancing its policy shift.

This growing confidence should support market sentiment toward BOJ policies, even as the yen appreciates. The latest Tankan survey indicates that Japanese companies are operating with an assumed exchange rate of 146 yen per dollar, suggesting that further yen strength is manageable without significantly disrupting economic activity. A stronger yen would also help mitigate imported inflation, particularly in energy costs, while exerting downward pressure on the US dollar which could potentially benefit global markets outside the US.

Additionally, the dominance of yen carry trades, a key driver of yen weakness over the past two years, is likely to fade as the yen loses its status as the primary funding currency following rate cuts in Europe. As a result, the long-standing inverse correlation between a weak yen and strong Japanese stock market should diminish. We believe that Japan's equity markets will remain resilient despite the appreciation of yen, easing concerns that a stronger currency could weigh on market performance.

Ultimately, interest rate hikes driven by economic normalisation should have a net positive effect on Japan's economy and equity markets, reinforcing confidence in the country's structural transformation.

Domestic reforms gaining traction. Amid heightened market uncertainty, Japan's corporate landscape is undergoing a fundamental shift, with management capabilities and reforms taking centre-stage from a bottom-up perspective. This transformation is evident across both private and public markets, signalling a broader effort to unlock value and enhance corporate governance.

- ***Private Market: Acceleration of corporate restructuring and deal momentum***

  Corporate restructuring in Japan is gaining momentum, as seen in several high-profile cases. Notable examples include:

  1. The takeover battle for Seven & i by the Canadian convenience store giant Alimentation Couche-Tard, known for operating Circle K
  2. The futile Honda-Nissan merger, reflecting ongoing industry consolidation
  3. The blocked acquisition of US steel by Nippon Steel, highlighting geopolitical sensitivities in cross-border M&A
  4. The bidding war for Fuji Soft, with KKR and Bain vying for control

Private equity interest in Japan is also rising. According to Preqin, Japan-focused funds accounted for 15.8% of the total USD47bn raised in APAC in 2024—more than double the five-year historical average of 6.4%, despite an overall decline in fundraising. Japan also contributed to 30% of total deal activity, well above its 21.9% historical average. So far this year, 77 buyout deals have been announced, totalling USD4.2bn. Major transactions include:

1. Bain Capital's USD3.3bn buyout of Mitsubishi Tanabe Pharma from Mitsubishi Chemical Group
2. MBK Partners' bid for Nagano-based semiconductor firm FICT

The real estate sector, hospitality in particular, remains a dynamic private market, driven by surging inbound tourism which fuels demand for hotel assets and commercial properties.

- ***Public Market: Shareholder returns and structural shifts***

In the public markets, Japanese corporations have emerged as the largest equity buyers, repurchasing JPY7.9tn (USD50bn) worth of domestic stocks in 2024—a record amount. This surge in buybacks comes as the Tokyo Stock Exchange pressures listed firms to enhance shareholder value and improve capital efficiency.

While Japanese institutional and individual investors were net sellers taking profits amid the yen carry trade unwind and record-high stock market levels, long-term global investors are increasingly drawn to Japan. Notably, legendary investor Warren Buffett increased his stakes in Japanese trading houses, citing attractive valuations and strong corporate fundamentals.

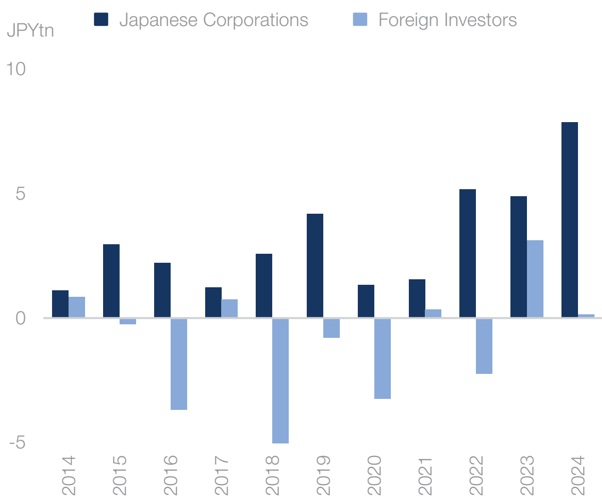
- ***Key catalysts driving corporate reforms***

We believe significant value remains in Japanese equities, supported by:

1. An aging demographic with succession challenges, leading to business divestitures
2. The unwinding of cross-shareholdings as companies restructure non-core assets to boost transparency and governance
3. Undervalued and underperforming stocks which present opportunities for strategic realignment
4. The rising influence of activist investors that push for reforms and better capital allocation

Two years into this reform-driven shift, we are seeing tangible results that are reflected in corporate re-ratings and strong TOPIX gains. Japan's domestic transformation is no longer just a narrative; it is actively reshaping its financial markets and corporate culture.

Japanese corporate buybacks at a record high

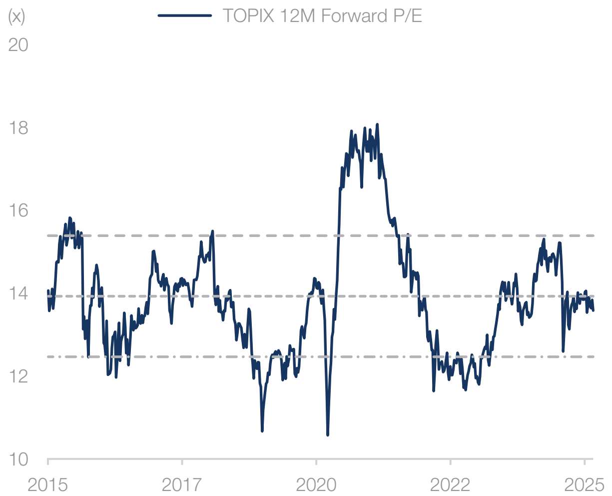


Source: Bloomberg, Tokyo Stock Exchange, DBS

Upward valuations and earnings outlook. Japanese equities are currently trading at 14x P/E, in line with their historical average. Despite a 50% rally in the broader index over the past two years (2023-24), valuations remain compelling, supported by robust corporate earnings and aggressive share buybacks.

Looking ahead, Japanese companies are projected to achieve annual earnings growth of c.9.2% over the next three years. With valuations at historical norms, we anticipate the market to grow in tandem with earnings, barring a US recession.

TOPIX 12-month forward P/E valuations hovering at average levels



Source: LSEG, DBS
Note: Bands are average and +/- 1SD

Steady macro outlook. We expect a benign macro environment for Japan in 2025, with a GDP growth of 0.9% (compared to just 0.1% in 2024). Inflation is forecasted to average 2.7% for the year, supporting a 2% increase in macro-level base wage. We anticipate the BOJ's policy rates to rise gradually, reaching a neutral rate of 1% by 2Q26. In addition, we expect the yen to remain at current levels (subject to updates).

This outlook provides a favourable environment for bottom-up opportunities in the following sectors:

- **Overweight Financials:** With the ongoing BOJ interest rate normalisation, the financial sector is poised to continue benefitting from a higher-for-longer interest rate environment, which should support higher NIMs. We believe this environment will also stimulate loan growth and encourage increased capital expenditures as companies put their idle balance sheets to work. Given Japan's relatively low debt ratios, we expect credit costs to remain minimal in this cycle.

Banks benefitting from high interest rates

Source: LSEG, DBS

- **<u>Overweight Industrials and Technology:</u>** Japan's strengths in robotics, semiconductors, precision engineering, EV technology, AI, and IoT positions its industrials and technology sectors at the core of global digital transformation. As the various industries embrace automation, connectivity, and smart solutions, Japanese innovation will remain a key driver of technological progress. Japan's increased defence spending should support and stimulate its industrials sector, particularly companies involved in high-tech manufacturing, infrastructure development, and defence-related innovation.

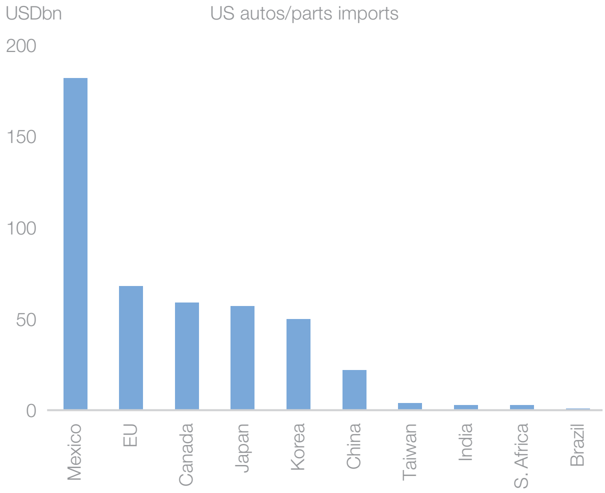
- **<u>Overweight Real Estate:</u>** We see significant value in Japanese real estate companies, which should be unlocked as reflation takes hold. Policy and structural tailwinds, including government-backed urban redevelopment projects in major cities like Tokyo, Osaka, and Fukuoka, are expected to drive property value growth. Additionally, inbound tourism will continue to benefit hotels and retail property firms through increased tourist spending. The ongoing aging population and urbanisation trends also support strong demand for senior housing and high-quality residential units.

Still undervalued in a reflationary environment with low interest rates

Source: LSEG, DBS

- **<u>Neutral Autos:</u>** We take a non-consensus stance in recommending positions within the Japanese autos sector (under Consumer Discretionary) as the market may be overestimating the risks associated with tariffs. Leading companies in this space are strong in hybrid car sales and pioneering hydrogen fuel cell technology. Moreover, ongoing sector consolidation that enhances global competitiveness should create value-unlocking opportunities within the industry.

US imports more autos from Mexico, EU, and Canada than from Japan



Source: LSEG

Note: Four-quarter sum till 3Q24

Japan Sector Allocation – 2Q25

	Overweight	Neutral	Underweight
Japan	Technology	Cons. Discretionary	Materials
	Financials	Cons. Staples	Healthcare
	Real Estate	Energy	Utilities
	Industrials	Comm. Services	

Valuation table

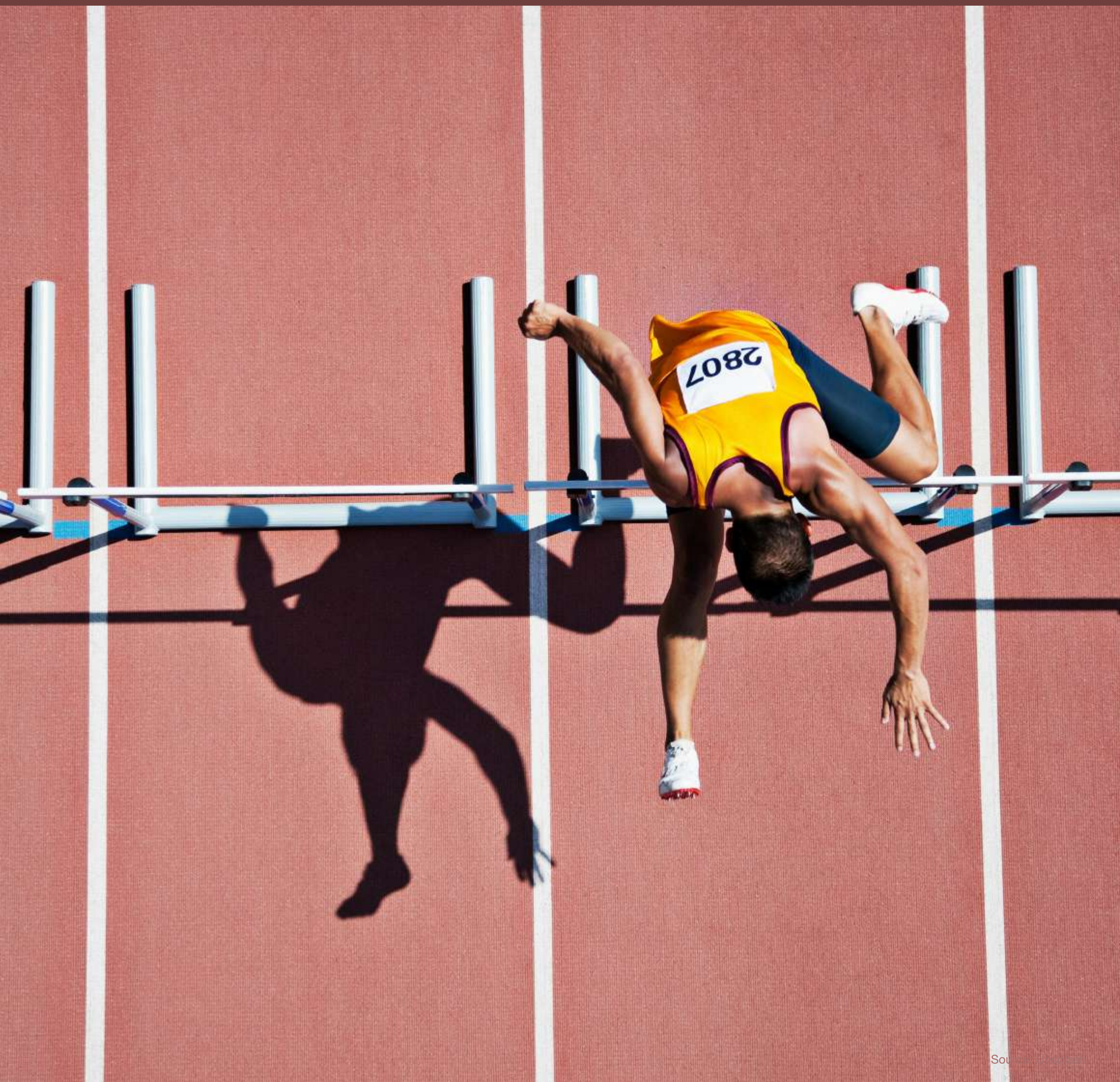
	Forward P/E (x)	P/Book (x)	EV/EBITDA (x)	FW ROE (%)	ROA (%)	OPM (%)
Japan	14.9	1.5	6.5	9.1	1.5	9.6
JP Financials	12.1	1.1	-	8.1	0.5	14.4
JP Energy	7.6	0.7	4.7	7.8	3.4	6.2
JP Technology	20.8	2.6	12.9	10.8	6.2	11.7
JP Materials	13.8	1.1	7.2	7.2	3.8	7.6
JP Industrial	13.5	1.6	11.4	10.8	4.8	7.1
JP Cons. Staples	23.2	1.9	9.9	7.1	2.9	6.5
JP Cons. Discretionary	14.1	1.4	7.7	8.8	3.9	8.2
JP Comm. Services	22.9	2.0	9.3	8.3	2.8	19.9
JP Utilities	9.5	0.6	8.2	7.3	2.6	6.2
JP Real Estate	13.1	1.3	13.6	8.9	3.1	13.2
JP Healthcare	17.6	2.1	13.3	8.5	4.5	12.5

Source: Bloomberg, DBS

Navigating Trade Tariffs

Asia ex-Japan
Equities
2Q25

Corporate earnings in tech-focused markets to be robust, fuelled by AI-driven growth on the back of DeepSeek's rise. The region's attractive valuations, earnings growth, and dividends make it a strong investment opportunity despite ongoing trade risks.



06.
Asia ex-Japan Equities.

Yeang Cheng Ling
Chief Investment Officer, North Asia

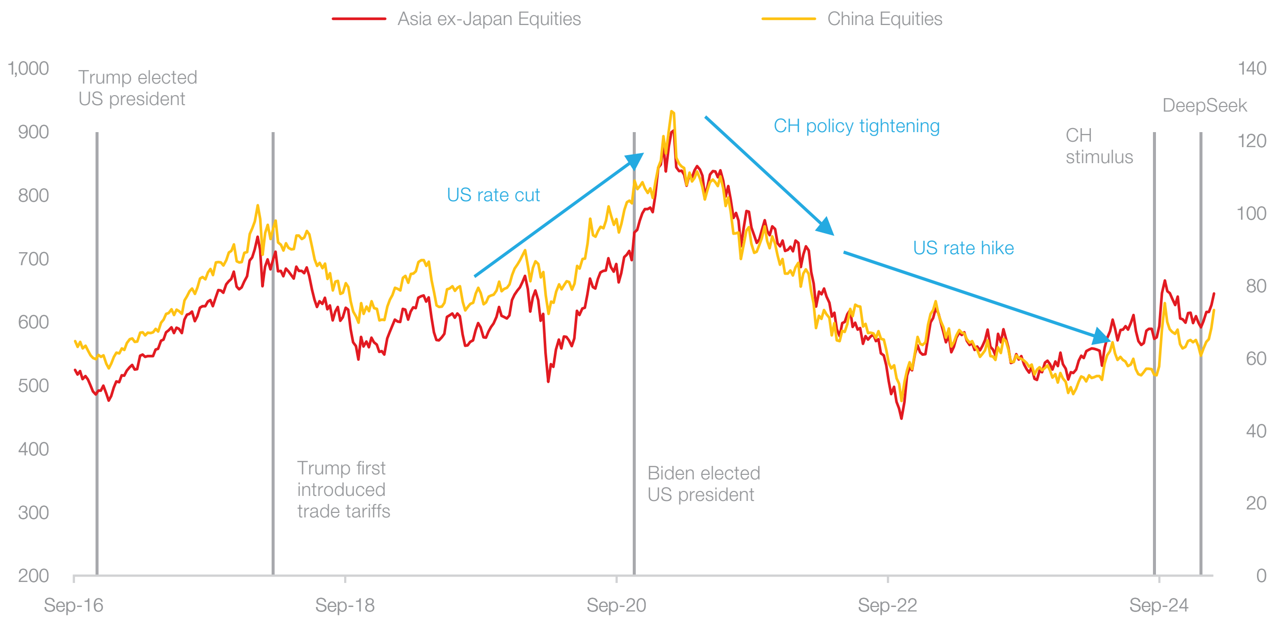
Joanne Goh
Strategist

The region started 2025 with a blistering rally as the emergence of DeepSeek sparked optimism across the region, led by the exuberance surrounding China's technological advancements. Since the start of the year, Asia ex-Japan equities experienced a notable turnaround in outlook and sentiment, driven by several key developments that have caused a surge in investor confidence, particularly in China.

DeepSeek's unexpected rise as a leader in AI innovation has boosted confidence over the region's ability to drive growth, especially in the technology sector. At the same time, concerns over potential US tariffs on Chinese goods have eased due to a combination of diplomatic efforts, economic resilience, and the strategic diversification of trade relationships and supply chains. This positive shift is further supported by the improving outlook for corporate earnings.

While the protectionist policies of the current regime in the US continues to pose a threat to Asia – by prolonging trade frictions – stimulus measures in China and beyond are leading to a revival of growth and mitigating the effects of tariffs. Within Asia, industry leaders are now better positioned to weather headwinds having diversified supply chains, production bases, and end markets.

Impact of interest rate, policies, stimulus, and DeepSeek



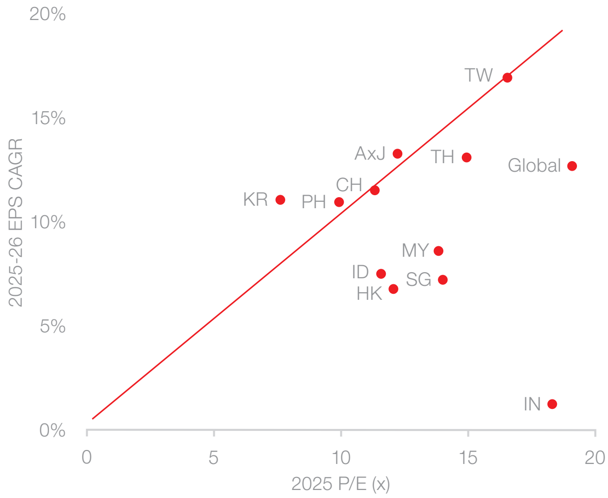
Source: Bloomberg, DBS

We are constructive on Asia ex-Japan based on the following factors: upward earnings revisions, supportive valuations, and appealing dividend income. The region is trading at a forward P/E of 10x-11x based on the 2025-26 earnings CAGR of 13%, offering a PEG ratio of less than 1x.

Although the valuation divergence between Asia ex-Japan and developed markets is likely to persist, we expect the gap to gradually narrow as the impact on trade balances and corporate earnings appears to be milder than feared.

The performance of Asia equities will be supported by double-digit earnings growth in 2025 and 2026, light investor positioning, improving confidence for China stimulus, and the collateral benefits for regional trade partners. Notably, corporate earnings are projected to remain robust across technology-focused markets as their supply chain and innovation capabilities enable them to ride the AI wave.

Heavyweight markets across Asia are trading at compelling valuations



Source: Bloomberg, DBS

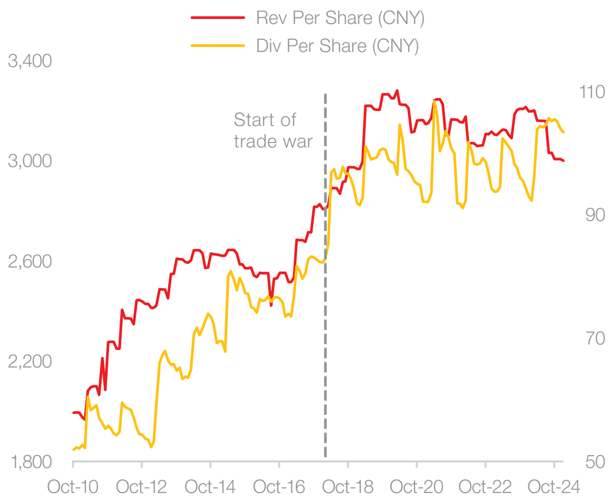
Meanwhile, ASEAN stands to benefit from Trump 2.0 due to shifting trade flows. This is due to outbound direct investment (ODI) from China moving to the region as companies expand their footprints.

Select countries in ASEAN are the main recipients of capital investment flows under the ‘China + 1’ wave, with China being the main contributor. This trend positions ASEAN for strong economic growth and investment opportunities given its proximity to China, favorable demographics, and trade openness. This will also lead to the development of a nascent data centre industry, leading to additional demand for electricity.

These encouraging developments further reinforce our constructive outlook. This can be viewed through our barbell investment approach; on the growth side, anchor with companies that are in the semiconductor, platform, game development, and tourism industries, as well as the beneficiaries of a revival in consumption. On the income side, we maintain our conviction on large banks and REITs for their appealing and stable yields.

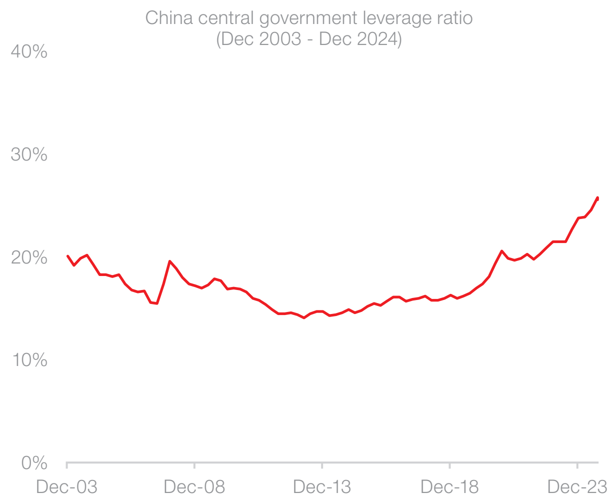
A bulwark against tariffs. China’s resilience remains evident as it has adapted well to external trade pressures, having faced tariff challenges for over eight years. As mentioned, investors have been warming up to Chinese equities thanks to DeepSeek’s technological breakthrough. More notably, the revenue and dividend per share of Chinese companies have remained stable since the start of the trade war. This indicates the limited direct impact of tariffs on corporate earnings and fundamentals as China’s deflationary environment works in favour of its export competitiveness.

Income remains resilient against headwinds



Source: Bloomberg, DBS

Sufficient room for government leverage

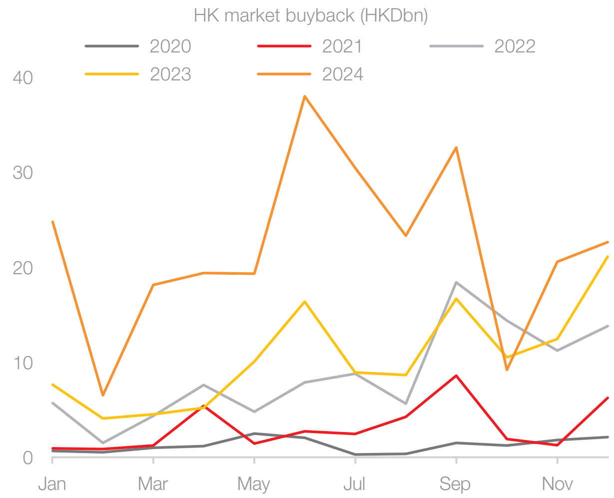


Source: WIND, DBS

Additionally, even after boosting local consumption, China's central government still has significant fiscal flexibility thanks to being leveraged at just 25% of GDP, well below the G20 average of 75%. This provides ample room for an increase in debt ratio, which can further fund government-led stimulus. We expect China to prioritise domestic demand through a mix of cyclical and structural measures, such as consumer goods trade-in programs, increased pensions, and raises in civil servant pay; complemented by spending on infrastructure, welfare, and housing. As external shocks like tariffs put pressure on growth, China will continue to pivot towards sustainable domestic growth, backed by expedited fiscal spending and leverage to drive economic stability and consumption.

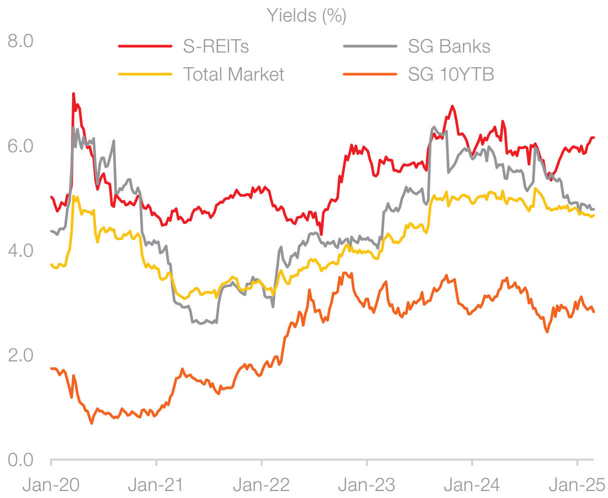
Stabilising the markets. Buyback activities have gained momentum since 2022 as corporates accelerate capital management to enhance shareholder returns. This trend is expected to persist and broaden as corporates are committed to improving capital efficiency and rewarding shareholders. The growing emphasis on buybacks, supported by the PBOC's relending and swap facilities, will add to liquidity flows and stabilise the market, boosting confidence. Global precedents show that consistent buyback activity has a proven track record of boosting market confidence and driving investment returns, resulting in the potential for a market re-rating.

Stepping up share buybacks



Source: WIND, DBS

Shelter for yields



Source: LSEG

Bright spots in the region

Singapore: Banks lead, REITs seek stability. Singapore was the top performer in the region in 1Q, driven by strong bank earnings and high dividends. We expect further upside, supported by 1) higher-for-longer interest rates, sustaining net interest margins, 2) resilient fee income amid steady economic growth, 3) attractive capital returns, including buybacks and dividends, and 4) MAS initiatives to enhance the equity market, benefitting banks.

S-REITs are stabilising, with lower rates easing funding costs. Notably, the 1M SORA has fallen to 2.7% (100 bps y/y), mirroring Fed rate cuts. If sustained, lower borrowing costs could trigger a re-rating from historically low valuations. Concerns around occupancy rates, FX volatility, and taxes remain but may be offset by cost efficiencies and rental growth.

Indonesia: Defensive stance amid external risks. We stay defensive on Indonesia as foreign inflows remain weak, pressured by US trade risks and high global rates. Markets have also been disappointed by weak FY24 results and muted FY25 guidance (especially from banks and telcos). Earnings downgrades are likely post-FY24 results in March. Given the near-term caution, we focus on: 1) defensive plays with stable earnings amid volatility, 2) value recovery from opportunities post-correction, and 3) dividend stocks for yield support.

Consumer names should remain resilient, backed by festive spending. Domestically, markets are watching policy shifts under the new government. These include the launch of a sovereign wealth fund “Danantara”, which aims to accelerate GDP growth from c.5% to 8% by unlocking SOE asset value.

Thailand: SET Index plunge spurs buybacks. The SET Index dropped 13% in early 2025, driven by broad-based foreign selling, except in banks (+4.0%), which benefitted from strong 4Q24 results and yields of 4.3%-8.5%. Sharp stock price corrections have led to aggressive share buybacks from cash-rich firms, improving EPS and ROE and providing downside protection. Government stimulus, including digital wallet handouts and Easy E-Receipt incentives, should boost domestic consumption.

The tourism sector remains a bright spot, with hotel operators posting strong 4Q24 results. International arrivals in 2024 neared or exceeded pre-pandemic levels, with the exception of Chinese tourists, which have only seen a c.60% recovery. Thailand’s global exposure is expected to increase following the latest season of the HBO hit *White Lotus*, which was filmed on its beaches and could boost travel interest.

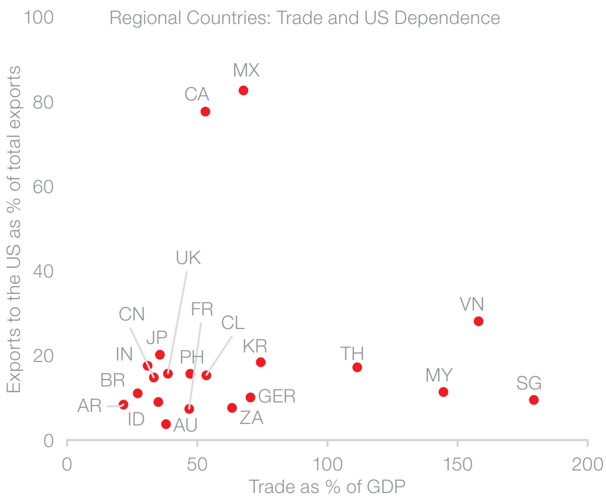
Malaysia: Supported by government policies. Malaysia’s economy remains on track for 4.8% GDP growth in 2025, supported by government policies including NSS (National Semiconductor Strategy), NIMP (National Industrial Master Plan), NETR (National Energy Transition Roadmap) and a stable monetary stance. Key investment themes include: 1) banks – benefitting from economic resilience, 2) healthcare – driven by medical tourism, 3) construction – supported by policy-driven infrastructure projects.

India: Poised for 2H recovery. India’s equities declined 17% from last year’s high due to an economic slowdown and tighter monetary conditions. The slowdown was largely cyclical, driven by post-elections consumption and a decline in investments. Rising food inflation caused by weather disruptions and a hawkish central bank maintaining rates despite US Fed cuts further tightened monetary conditions. However, 4Q GDP growth rebounded strongly on higher government and consumer spending, confirming the slowdown was temporary. With the April-January fiscal deficit at 74.5% of the full-year target, there is room for additional stimulus to boost growth in 2H25.

Economic conditions are expected to improve in 2H25, driven by: 1) tax relief in FY26 budget, supporting consumption and employment, 2) improved liquidity aiding capital markets, 3) easing food inflation stabilising spending, 4) increased infrastructure investment, and 5) potential RBI rate cuts lowering borrowing costs. Additionally, the RBI has reduced risk weights on bank loans to NBFCs and microfinance institutions, partially reversing 2023’s macroprudential tightening. This move aims to unlock funds and improve credit availability.

India and China are key markets in Asia ex-Japan and EM. A shift in sentiment toward China could lead investors to use India as a funding source. After its correction, India now trades at slightly below +1 SD, while its valuation premium with China has narrowed to average levels. While not cheap, its domestic-driven economy offers resilience against US tariffs. India has taken a proactive stance on China (trade, border issues) and the US (tariffs, migration), reinforcing stability. With supportive policies and structural growth drivers regaining momentum, India remains attractive amid global uncertainty. We maintain a neutral stance with focus on banks as a beneficiary of monetary easing.

Exporting countries are vulnerable



Source: LSEG, DBS

Valuation table

	Forward P/E (x)	P/Book (x)	EV/EBITDA (x)	FW ROE (%)	ROA (%)	OPM (%)
AC ASIA EX JAPAN	14.9	1.7	10.8	11.7	1.9	12.2
AxJ Financials	9.2	1.1	N/A	11.9	1.0	23.3
AxJ Energy	11.1	1.1	4.9	10.3	4.3	7.4
AxJ Technology	16.2	3.1	9.9	17.1	19.7	10.9
AxJ Materials	22.5	1.2	9.0	5.3	1.9	6.0
AxJ Industrial	13.4	1.3	8.7	9.8	2.5	9.0
AxJ Cons. Staples	21.1	2.9	11.5	14.0	5.7	9.2
AxJ Cons. Discretionary	16.3	2.4	11.0	13.1	5.6	8.3
AxJ Comm. Services	21.2	3.3	13.0	14.0	6.1	19.7
AxJ Utilities	12.4	1.4	8.6	10.8	3.2	14.1
AxJ Real Estate	14.0	0.6	12.5	4.5	1.8	16.8
AxJ Healthcare	40.5	3.1	18.5	7.4	3.9	6.7

Source: Bloomberg, DBS

We are overweight on the following Asia ex-Japan sectors:

- Technology – Asia is known for its pole position in leading-edge semiconductor contract manufacturing. The rising demand for AI-embedded devices and chipsets will undoubtedly highlight the essential role fulfilled by this sector
- Consumer discretionary – We are constructive on platform companies which have strong moats around the online and e-commerce ecosystems. The ongoing development of AI functions, algorithm architectures, and cloud penetration will sustain investment attractiveness
- Communication services – Asia is at the forefront of the cloud and gaming industries, leveraging technological innovation and vast consumer bases. With a growing middle class, AI developments, and a thriving eSports ecosystem, the region's internet sector is poised for continued growth
- Financials – The sustained dividend yields of state-owned and large quality banks with strong balance sheets have consistently rewarded investors with attractive returns. Strong loan growth continues in the ASEAN market and there is the potential for stable NIM in a less dovish rate environment
- Real estate* – Our neutral position reflects a balanced view, underpinned by a positive outlook on Singapore REITs as reliable income generators, while maintaining a cautious stance towards China real-estate developers due to prevailing market uncertainties

AxJ Geographical Allocation – 2Q25

Overweight	Neutral	Underweight
China#	Hong Kong	South Korea
Taiwan	India	Philippines
Singapore	Indonesia	
Thailand	Malaysia	

Including China stocks listed in Hong Kong

AxJ Sector Allocation – 2Q25

Overweight	Neutral	Underweight
Technology	Energy	Consumer Staples
Consumer Discretionary	Real Estate*	Materials
Financials	Utilities	Industrials
Communication Services	Healthcare	

Rethinking US Exceptionalism

Global Rates
2Q25

US growth worries are eroding the yield premium of US Treasuries over G3 peers. Increased military expenditure and persistent inflation worries are driving up German and Japanese yields respectively.

Source: iStock

07. Global Rates.

Eugene Leow
Strategist

Samuel Tse
Strategist

Rethinking US exceptionalism? The US economy has proven to be an outperformer in recent years but we wonder if a rethink is at hand. From a rates perspective, the strength of the US economy has allowed US Treasury yields to be elevated relative to the other large economies (i.e. Eurozone, Japan, and China). However, we wonder if the balance of risks is now tilted the other way as dynamics within the large economies shift, leading to a cyclically smaller yield premium for the US.

First, we think that a cyclical slowdown in the US may be a material consideration. Amid tariff uncertainties and funding freezes, investments in the US may cool. Moreover, as DOGE-related job cuts extend, this could be a headwind for the labour market in the short term. Lastly, there may be some frontloading of consumption ahead of tariffs that could translate into slower growth later down the line. Taken together, a less rosy outlook in the near term could weigh on US yields, structural fiscal concerns notwithstanding.

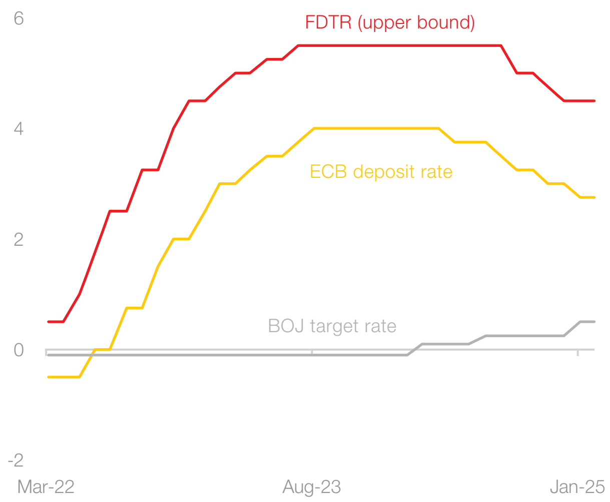
Second, long-end EGB yields are buoyant despite aggressive ECB cuts amid a weak economy. This may be due to a shift in fiscal outlook as the bloc faces pressures to up military spending. Germany, in particular, might need to loosen purse strings to pull its economy out of a recession. While a conservative-led coalition government in Germany may not be formed until April, there is some optimism that the worst for the Eurozone may be behind us.

Third, JGBs have been relentlessly selling off. Inflation appears to be sustained with labour cash earnings and recent CPI prints surprising on the upside. With CPI hovering above 3% y/y, it is clear that the BOJ has considerable room to hike rates (current target rate stands at 0.5%). However, the pace of rate hikes that is tolerable may be around 50-75 bps a year. Until the BOJ becomes more serious about tackling inflation, medium to long-term yields will still see upward pressures.

Fourth, Chinese stock markets have gotten an AI-related boost and CGB yields are also sharing in some of the optimism that the worst may be over for the Chinese economy, threats from tariffs notwithstanding.

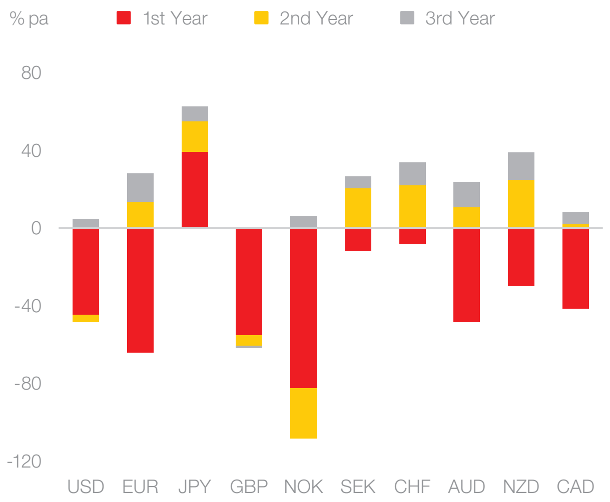
With the outlook of other major economies improving and that of the US likely to face challenges, we could see the yield premium of USTs erode over peers in the coming months.

Further fine-tuning across the G3



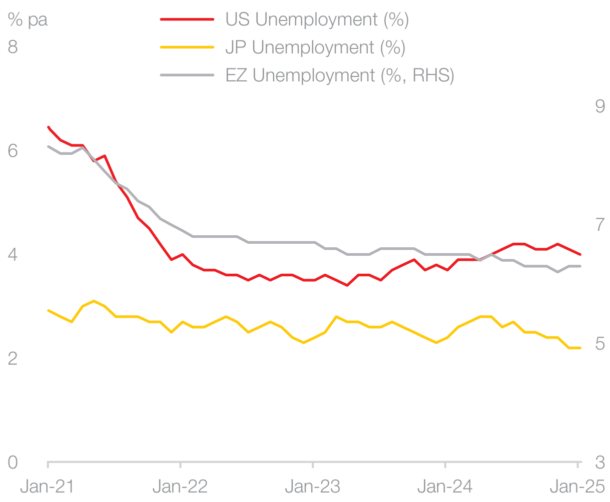
Source: Bloomberg, DBS

Mixed picture across the G10



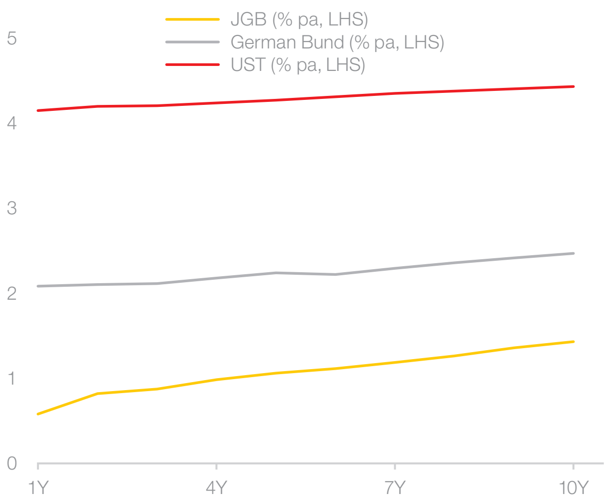
Source: Bloomberg, DBS

Unemployment stays low across the G3



Source: Bloomberg, DBS

Flattening curves



Source: Bloomberg, DBS

Asia Rates

CNY rates: Limited upside in CGB yields

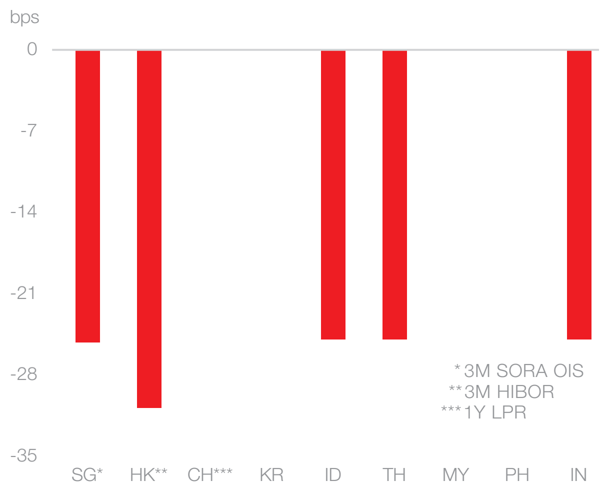
CNY rates have rebounded significantly on improving data prints. M1, which includes cash for spending and investment, has returned to growth since Dec 2024. Total social financing and New Yuan Loans growth has accelerated on the back of stabilising corporate credit demand and government bond issuance. CPI also shows signs of stabilisation. Meanwhile, the higher fiscal deficit target and local government bond issuance set in the Two Sessions have fuelled the growth optimism. The outperformance of the equity market and rebound in property transactions have boosted the money demand. Against this backdrop, investors have been taking profit from previous long CGB trades.

That said, the upside could be restrained. The prolonged weak inflation and sustained recovery in economic activities require further easing. The renewed trade tension against the US may also prompt the Chinese central bank to return to easing. The steady CNY exchange rates, in tandem with JPY and other Asian currencies, also leave room for liquidity injection. The PBOC will cut the 1Y LPR by 15 bps in 2Q with a total of 30 bps this year. We expect the PBOC to resume government bond buying and inject an extra CNY2tn through a 100 bps RRR cut this year. Curve-wise, a "moderately loose" monetary policy implies a flattening curve.

IDR rates: Rate cut and fiscal developments

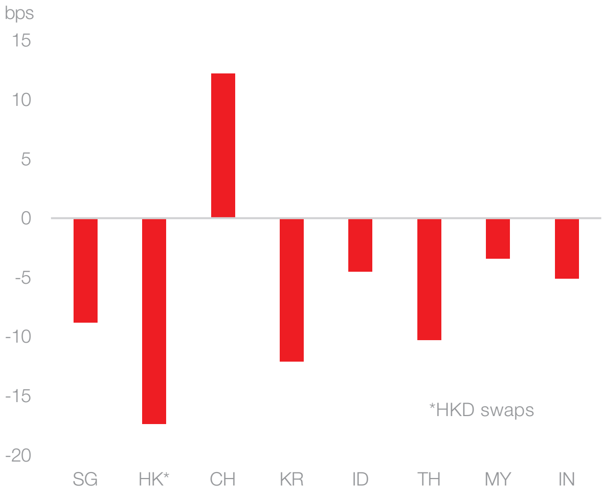
Despite elevated UST yields and a strong dollar, BI is on course with rate cuts, thereby adding downward pressure to IndoGB yields. Spreads against UST counterparts will likely compress further. On the monetary front, recent CPI prints have undershot BI's target of 1.5-3.5% due to policy measures amid weakening consumption sentiment. The elevated real rate (benchmark rate – inflation) is currently at around 500 bps. Meanwhile, the overall growth could be dragged by negative fiscal impulse. The new administration is set to finance social programs partially with spending cuts worth IDR306.7tn (8% of total spending; 1.2% of GDP). Hence, monetary easing and rate cuts will take a bigger role in stimulating growth. For instance, BI plans to support the government in borrowing programs to fund a housing stimulus plan. However, the BI's share of government local bonds is the highest as compared to its Asian peers (at around 25%), and this is discomforting. The monthly OMO has increased from around IDR500-600tn in the first half of 2024 to around IDR750-900tn of late. Meanwhile, BI will also lower the reserve requirement for banks that extend mortgage loans. Curve-wise, steepening could return if rate cuts stay on schedule. Short-end rates such as SRBIs will remain in check due to policy easing.

Change in policy rates YTD



Source: Bloomberg, DBS

Change in 10Y government bond yields YTD



Source: Bloomberg, DBS

INR rates: Further downside on IGB yields

We see further downside risk on IGB yields amid rate cut expectations. The RBI will likely cut the benchmark rate by another 50 bps in the first half of 2025 after a 25 bps reduction in February. The US' "Fair and Reciprocal Plan" could be a key headwind as the US' trade deficit against India doubled during 2015 and 2024. India's MFN trade-weighted average tariff rate in 2023 stood at 12% vs 2.2% in the US (general not bilateral). Domestically, retreating consumption sentiment and slower wage growth warrant concern. Inflation is also edging down to the 4% target. Equity markets have also seen strong foreign portfolio outflows due to high valuation and earning concerns.

Rate cuts aside, the RBI is prompt in easing liquidity conditions to facilitate policy transmission as evidenced by the narrowing spread between the O/N MIBOR and the policy rate. The central bank has net injected INR1,388bn through open market operations YTD. Curve-wise, we continue to see a steepening bias as long-end bond supply will remain abundant with over 75% of total borrowings in tenors over 10 years.

KRW rates: Rate cuts and supplementary budget

Short-term KTB yields will see mild downward pressure this year alongside one additional cut from the BOK in 2Q25. The stabilising Korean won leaves room for the cut, thanks to the relative stabilisation in the political landscape and temporary retreat in USD rates. Domestically, economic growth could slow from 2.0% in 2024 to 1.7% in 2025. CPI should also stay moderate at around 2%, suggesting the real rate is still beyond neutral at 0.8%. Meanwhile, slower loan growth and weak home prices call for further easing. On the external front, tariff risks are on the rise. While South Korea may not be a priority target for reciprocal tariffs due to KORUS FTA, it remains vulnerable to automobile tariffs. South Korea is the US' third largest source of passenger car imports (after Mexico and Japan) with automobile exports to the US accounting for around 2% of its GDP. In contrast, long-term KTB yields will likely be lifted by the higher debt-to-GDP ratio and a potential supplementary budget of KRW30tn. As a result, the KTB yield curve is expected to slightly steepen.

MYR rates: Steady MGS yields in 1H25

MGS yields will remain anchored for the rest of 1H25. Our expectations for an extended pause by BNM into 1H25 will also keep the MGS yields stable. Thus far, the Malaysian economy grew by 5.1% in

2024 with inflation remaining moderate below 2% y/y over the past six months. Looking ahead, the average headline inflation should be manageable at 2.8% in 2025, given the contained global commodity prices and domestic price pressures, though with upside risks from RON95 subsidy rationalisation. That said, heightened geopolitical tensions and potential negative spillovers to Malaysia's growth could prompt BNM to consider rate cuts in 2H. Note that Malaysia is particularly vulnerable to the proposed 25% US tariffs on semiconductors as US semiconductor imports from Malaysia account for approximately 4% and 5% of Malaysia's GDP and total goods exports (in 2024) respectively, well above the ASEAN-6 average.

Meanwhile, a narrowing fiscal deficit will also keep MGS yields in check. Federal government expenditure is budgeted to grow at a slower pace of 3.3% compared to 5.5% for revenue in 2025. The joint efforts by Malaysian policymakers and government-linked entities to encourage inflows alongside BNM's extended rate pause will also cushion the adverse impact from elevated USD rates.

PHP rates: Compressing spreads against UST

PHP rates should fall in tandem with the upcoming 50 bps of policy rate cuts in 2Q25. While the BSP kept the benchmark rate unchanged in February amid rising external uncertainty, the domestic economic condition allows for further easing. GDP growth undershot the central bank's expectations at 5.6% last year due to extreme weather conditions. Meanwhile, the rising yet manageable inflation leaves room for further cuts. With inflation remaining steady below 3%, the real interest rate should stay restrictive at 2.85%. Aside from rate cuts, the banks' reserve requirement ratio was cut in February by 200 bps to 5%, greasing liquidity conditions. Curve-wise, steepening should be at play amid the upcoming cuts. The spread against the UST yields should compress.

SGD Rates: Flush liquidity

SGD rates will likely be held low for the foreseeable future amid very flush liquidity conditions. Judging by SORA fixes and the cut-offs in MAS and T-bills, it does appear that the institutional space may be shifting demand towards these short-term instruments. We note that downward pressure on SGD rates is persisting despite no imminent Fed cut pricing and a flatter SGDNEER slope. At current levels, we suspect that SGD rates are probably too low and may not have much room to shift lower even if the Fed delivers further calibrated easing.

THB rates: Domestic and external headwinds call for cuts

Downside risks on THB rates are emerging. The BOT unexpectedly cut its policy rate by 25 bps to 2% during its first meeting of 2025. The downside growth risks and subdued inflation call for further easing ahead. The potential reciprocal tariffs by the US could also dent Thai exports performance. Note that the US accounted for almost 20% of Thailand's goods exports, and Thailand is the US' 11th largest goods trade deficit partner. Meanwhile, tight financial conditions from credit deterioration also prompted the BOT to ease rates. Lower interest rates and weaker THB could support the recovery of inbound tourism. We expect the BOT to cut the benchmark rate by another 25 bps to 1.75% in 2025. Outstanding government bonds increased by THB199bn between Jun and Dec 2024. Strategy-wise, Thai government bonds (govvies) yields will likely fall further with steepening as the core theme.

Rates forecasts

		2025				2026			
		1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q
US	3M SOFR OIS	4.38	4.38	4.13	3.88	3.88	3.88	3.88	3.88
	2Y	4.25	4.20	4.15	3.90	3.90	4.00	4.10	4.10
	10Y	4.30	4.20	4.20	4.50	4.60	4.70	4.75	4.80
	10Y-2Y	5	0	5	60	70	70	65	70
Japan	3M TIBOR	0.65	0.65	0.90	0.90	1.00	1.15	1.15	1.15
	2Y	0.70	0.80	0.90	0.95	1.00	1.10	1.10	1.10
	10Y	1.15	1.25	1.35	1.50	1.60	1.60	1.70	1.70
	10Y-2Y	45	45	45	55	60	50	60	60
Eurozone	3M EURIBOR	2.70	2.20	2.20	2.20	2.20	2.20	2.20	2.20
	2Y	2.20	2.15	2.15	2.15	2.15	2.20	2.30	2.40
	10Y	2.70	2.80	2.90	3.00	3.10	3.20	3.25	3.25
	10Y-2Y	50	65	75	85	95	100	95	85
Indonesia	3M JIBOR	6.35	6.10	6.10	6.10	6.10	6.10	6.10	6.10
	2Y	6.35	6.15	6.20	6.20	6.20	6.25	6.25	6.25
	10Y	6.55	6.45	6.45	6.45	6.45	6.55	6.55	6.55
	10Y-2Y	20	30	25	25	25	30	30	30
Malaysia	3M KLIBOR	3.50	3.50	3.50	3.50	3.50	3.50	3.50	3.50
	3Y	3.45	3.40	3.40	3.40	3.45	3.45	3.45	3.45
	10Y	3.85	3.80	3.85	3.90	3.95	4.00	4.00	4.00
	10Y-3Y	40	40	45	50	50	55	55	55
Philippines	3M NDF implied yield	5.25	5.00	5.00	5.00	5.00	5.00	5.00	5.00
	2Y	5.75	5.50	5.50	5.55	5.60	5.60	5.60	5.60
	10Y	6.00	5.80	5.80	5.85	5.90	5.90	5.90	5.90
	10Y-2Y	25	30	30	30	30	30	30	30
Singapore	3M SORA OIS	2.88	2.88	2.73	2.63	2.63	2.63	2.63	2.63
	2Y	2.95	2.90	2.85	2.70	2.70	2.80	2.90	2.90
	10Y	2.90	2.80	2.80	3.10	3.10	3.20	3.25	3.25
	10Y-2Y	-5	-10	-5	40	40	40	35	35

Units -
Interest rates: %, eop
Interest rates spreads (10Y-2Y / 10Y-3Y): bps, eop
*swap rates

Source: CEIC, Bloomberg, DBS

		2025				2026			
		1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q
Thailand	3M BIBOR	2.15	2.15	1.90	1.90	1.90	1.65	1.65	1.65
	2Y	1.85	1.65	1.55	1.55	1.35	1.25	1.25	1.25
	10Y	2.10	1.95	1.90	1.90	1.75	1.70	1.70	1.70
	10Y-2Y	25	30	35	35	40	45	45	45
Mainland China	1Y LPR	3.10	2.95	2.80	2.80	2.80	2.55	2.55	2.55
	2Y	1.35	1.25	1.10	1.10	1.05	1.00	1.00	1.00
	10Y	1.70	1.65	1.50	1.50	1.45	1.40	1.40	1.40
	10Y-2Y	35	40	40	40	40	40	40	40
Hong Kong, SAR	3M HIBOR	3.80	3.80	3.60	3.40	3.40	3.40	3.40	3.40
	2Y*	3.75	3.75	3.75	3.55	3.50	3.60	3.70	3.70
	10Y*	3.60	3.55	3.60	3.95	4.00	4.10	4.15	4.20
	10Y-2Y	-15	-20	-15	40	50	50	45	50
Korea	3M CD	2.85	2.60	2.60	2.60	2.60	2.60	2.60	2.60
	3Y	2.50	2.40	2.40	2.50	2.55	2.60	2.60	2.60
	10Y	2.80	2.70	2.70	2.85	2.90	2.95	2.95	3.00
	10Y-3Y	30	30	30	35	35	35	35	40
India	3M MIBOR	7.00	6.65	6.65	6.65	6.65	6.65	6.65	6.65
	2Y	6.35	6.00	6.00	6.00	6.05	6.10	6.10	6.10
	10Y	6.55	6.45	6.50	6.55	6.60	6.65	6.65	6.65
	10Y-2Y	20	45	50	55	55	55	55	55

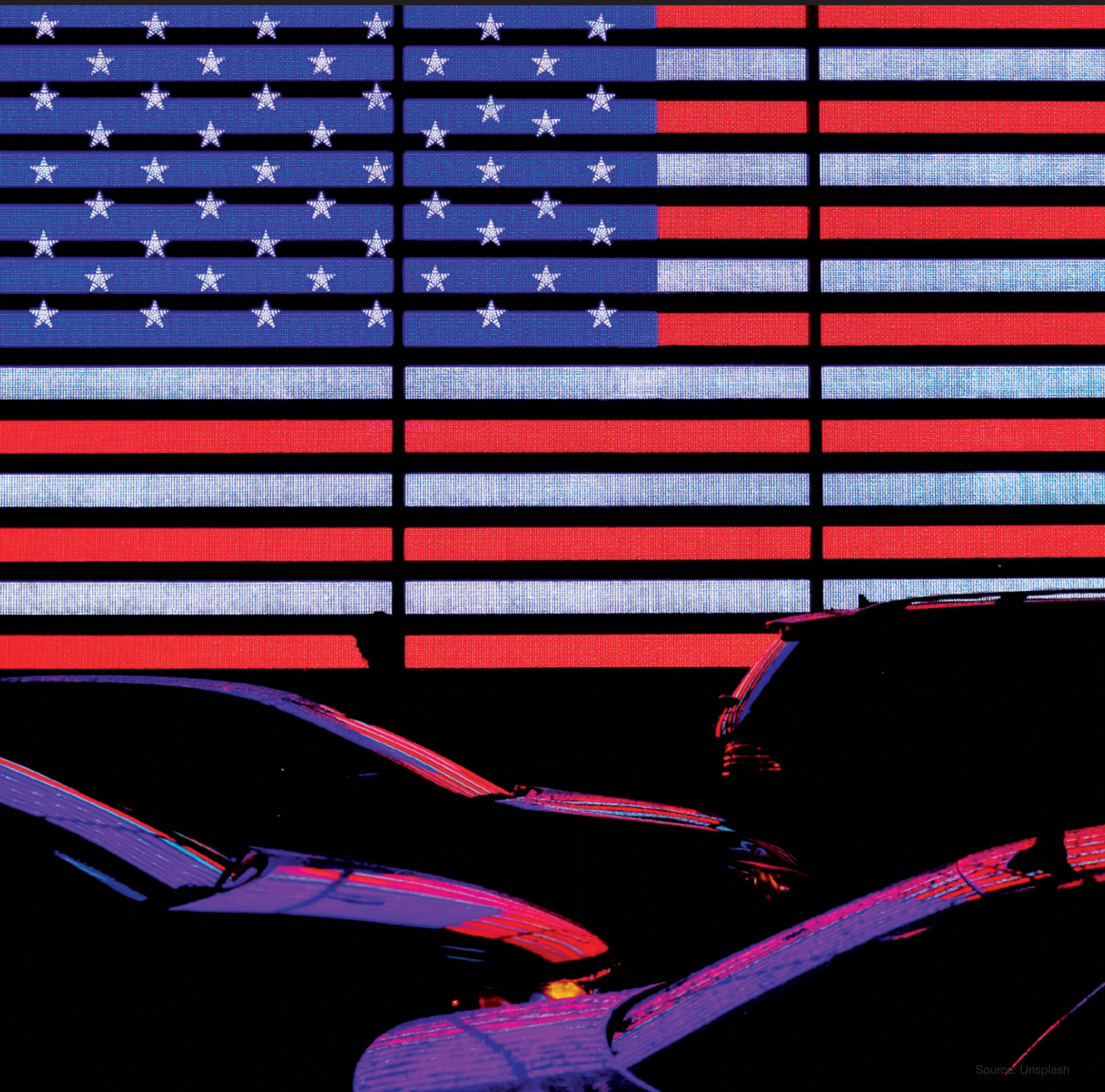
Units -
Interest rates: %, eop
Interest rates spreads (10Y-2Y / 10Y-3Y): bps, eop
*swap rates

Source: CEIC, Bloomberg, DBS

Why Trump Needs Lower Yields

Global Credit
2Q25

The transition into a tighter fiscal/easier monetary policy stance spells tailwinds for bonds. Prioritise A/BBB and be selective with BB only in the 1-3Y segment. Portfolio duration should remain in a barbell, overweighting 2-3Y for certainty of good income, and 7-10Y to capitalise on curve rolldown.



Source: Unsplash

08. Global Credit.

Daryl Ho, CFA
Strategist

Elijah Tan, PhD
Analyst

It is difficult to be a bond strategist these days. To illustrate, one simply needs to think about the number of core concepts in fixed income that have been overturned in just the last three years alone. Firstly, the concept of "safety" in bonds was called into question in the bear market of 2022, where double-digit losses were not uncommon following the most aggressive Fed hiking cycle in decades. To add insult to injury, correlations with equities rose, throwing 60/40 risk diversification practices out the window.

Secondly, geopolitical fragmentation has given sovereign wealth funds and FX reserve managers – some of the biggest players in international fixed income markets – pause in holding developed market debt as reserve assets, seeing as such debt (a) can be seemingly printed with abandon and (b) unilaterally sanctioned out of use at the debtor's discretion.

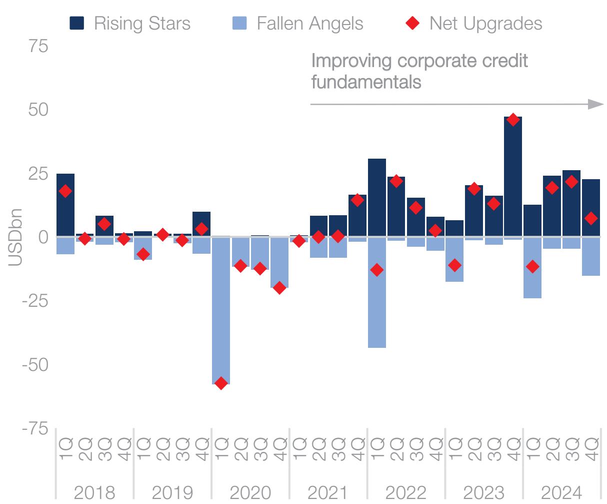
Thirdly, longstanding assumptions around the "risk-free" rate have been thrown into disarray as the fiscal trajectory of the US remains on an unsustainable path, with investors quickly learning that the sky's the limit for the US debt ceiling, and not in a good way. The inevitable downgrade of US debt ratings from AAA to AA+ in 2023 certainly begs a question that never needed to be asked before – does the riskless rate have risk?

Lastly – and on a related note – notions of credit risk have also been turned on its head with companies like Microsoft and Johnson & Johnson retaining their AAA ratings – a notch above the same US government that can theoretically "never default" on its dollar obligations. The key observation is that private sector corporates have on aggregate

"Risk-free" government bonds showing more risk than corporates

Source: Bloomberg, DBS

Spread tightening supported by improving credit fundamentals

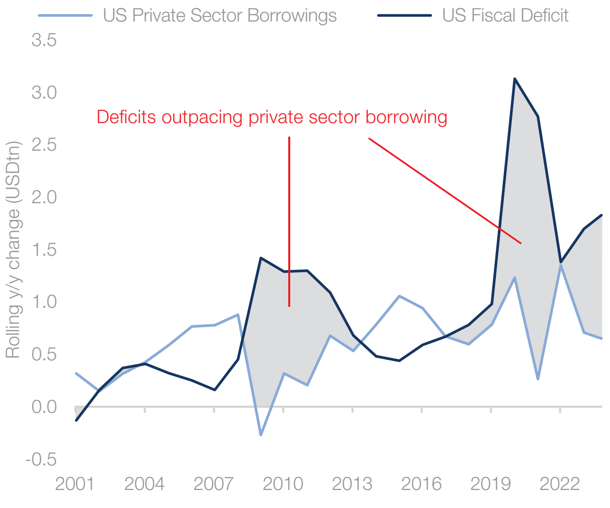


Source: Bloomberg, DBS

continued to demonstrate financial prudence (unlike governments), resulting in an extended period of spread tightening despite inverted yield curves and other recessionary warnings.

Nevertheless, we have to try. There is a paradigm that adequately explains the quirks and kinks that we observe in the bond markets today, and it is in the notion of fiscal dominance. Fiscal dominance occurs when deficits become equally or more important than private sector lending and/or monetary policy in driving economic activity. When a country's debt/GDP remains above 100%, monetary policy becomes ineffective at controlling inflation; on the contrary, persistently high interest rates can exacerbate deficits, prolonging inflation instead.

Government has "crowded out" the private sector over the last two decades

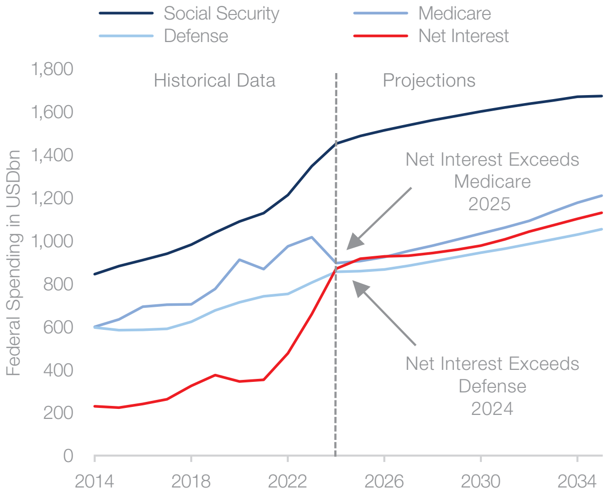


Source: FRED, Department of the Treasury, Bureau of the Fiscal Service, DBS

The impotence of monetary policy. Signs of this phenomenon are already around us. In concept, the rapid 525 bps of rate hikes should have ground the economy to a halt, yet growth remains strong, labour markets at full employment, and inflation sticky above the 2% Fed target. This is because high rates will not deter governments from spending; congressmen after all measure success more in the return of voters than the return of dollars. Moreover, at least domestically in the US, the private sector has over several decades migrated towards asset-light models of operations. The offshoring of capex-heavy fixed asset operations outside the US has limited the need for domestic borrowings to finance said assets; borrowings which are more sensitive to Fed policy.

Move (rates) fast, break things. Not only have rate hikes not slowed the economy; they can conversely bring about the unintended consequence of being economically stimulative in a regime of Fiscal dominance – which goes against prevailing thought. Aggregate savings in the private sector have been channelled into banks, money market funds, pensions, and other asset managers, which are recycled into bills and other "high quality" debt instruments of the US government, now generating high rates of return thanks to the Fed. These interest payouts function like a liquidity injection (stimulus cheques getting their own stimulus cheques), which continue to build private sector surpluses like a snowball. It is no surprise at all, that net interest payments by the US government have exceeded defence spending in 2024 and are slated to exceed Medicare within a year's time.

Net interest continues to exceed other critical budgetary items



Source: Congressional Budget Office, DBS

All this conflicts with Trump's economic agenda. No doubt, the ills of fiscal dominance would have to be addressed under a second Trump administration. Fortunately, there appears to be a narrow solution that kills both the birds of (i) Trump's "America first" agenda and (ii) the alleviation of the US debt spiral with one stone – and that is lower interest rates. In illustrating this outcome, we hope to be able to propose a non-consensus but credible credit strategy for bond investors to adopt as we embark on a second Trump term.

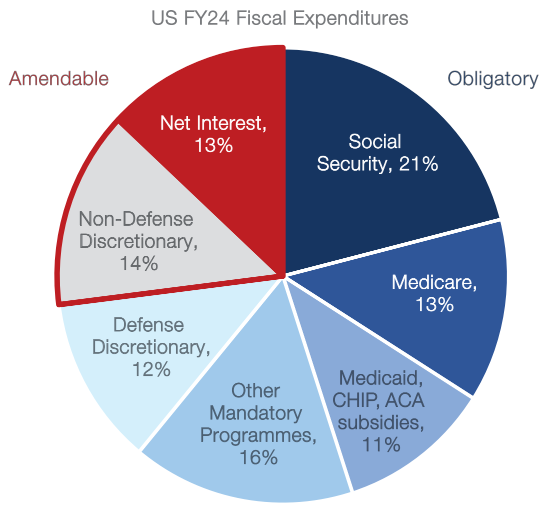
Tariffs are an imperfect solution. Crucially, this will be President Trump's final term to cement his legacy in "making America great again", perhaps one last hurrah in promoting a US manufacturing renaissance for American workers. Creating manufacturing jobs in the US can happen chiefly in one of two ways, requiring either (a) high import tariffs or (b) substantial dollar depreciation. Obviously, President Trump's first few weeks in office suggest that he favours the former, in line with his antithetical mantra to "carry a big stick, speak loudly and swing it at others". The tariff experience of 2018, however, tells us that this results in two particularly undesirable outcomes for the Trump administration, namely (a) negative sentiment for businesses and investors, and (b) a strong USD that ultimately hurts the export competitiveness of US multinationals, the very entities they seek to reshore.

We think that a better option to achieve the same outcome is to devalue the USD by lowering rates. This would increase US export competitiveness without the negative sentiment towards businesses, and most importantly, it has a historical precedent. The Plaza Accord of 1985 was signed for this reason – back when it was still classy to be diplomatic – to devalue the dollar and rectify the US trade deficit with their trading partners after the Volcker era. To do this today, the US would have to bring down levels of real interest rates from a 17-year high, which would not only (a) weaken the USD, but also (b) reduce the ever-climbing net interest expense that the Treasury continues to add to the deficit. Would other trade partners cooperate given that their own economies are on shaky ground? We think that gradual strengthening of domestic currencies is a lesser evil than a tariff shock, given that (a) it is optically more palatable as a bilateral agreement and can be reversed with negotiation (think Louvre Accord in 1987), and it also (b) provides cover to decumulate USD reserves, which appears to be an alignment of interest.

Shift from easy fiscal/tight monetary to tight fiscal/easy monetary policy. Admittedly, cutting rates and weakening the USD amid a strong economy and large deficits risks inflation expectations becoming unanchored and bond vigilantes reenacting a "Liz Truss moment" for US Treasury bonds. Therefore, to maintain the trajectory of a soft landing, the US administration needs to thread the needle in switching from an easy fiscal/tight monetary policy stance to a tight fiscal/easy monetary policy stance – delivering concessionary fiscal cutbacks to prevent the economy from overheating. We believe this is in part why President Trump signed an executive order to create the Department of Government Efficiency (DOGE), in recognition that fiscal cutbacks are critical for longer-term sustainability under his policy priorities. Curiously, of the c.27% in annual fiscal expenditures we consider "amendable" by the administration, around half of it could be under the purview of DOGE (non-defence discretionary), while the other half is related to net interest costs which could be alleviated by looser monetary policy.

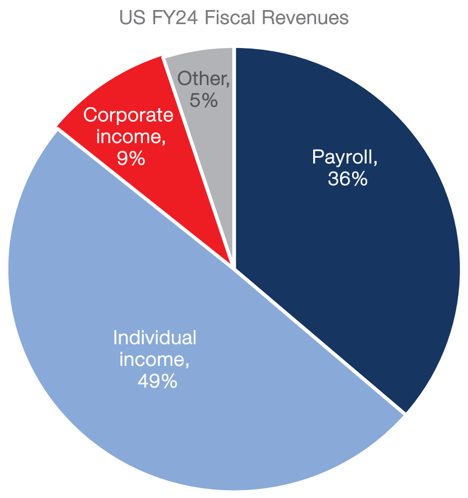
Would expansionary tax cuts negate DOGE? Common sense supposes that revenues would decline under President Trump's plan to cut corporate taxes. However, it is too simplistic to look at this issue purely from a numerical (15% is less than 21%) dimension. Firstly, corporate tax receipts are a smaller component of fiscal revenues (c.9% in FY24), and secondly, the ultimate objective to reshore manufacturing capacity implies that there could be other avenues to recoup revenues from foreign income of US multinationals. The 2017 Tax Cuts and Jobs Act (TCJA) came with certain provisions, such as (i) exemptions for most dividends received by US multinationals from their foreign affiliates, and (ii) exemptions of portions of foreign income from tax and a reduced tax rate under the Global Intangible Low Taxed Income (GILTI) regime. Such concessions could be simultaneously rolled back with the proposed tax cuts, to ultimately entice such US multinationals to "come home". Lower interest rates would also once again help in the calculus, for such entities to borrow and build out manufacturing capacity in the US.

Net interest remains a large but amendable portion of fiscal expenditures



Source: Center on Budget and Policy Priorities, DBS

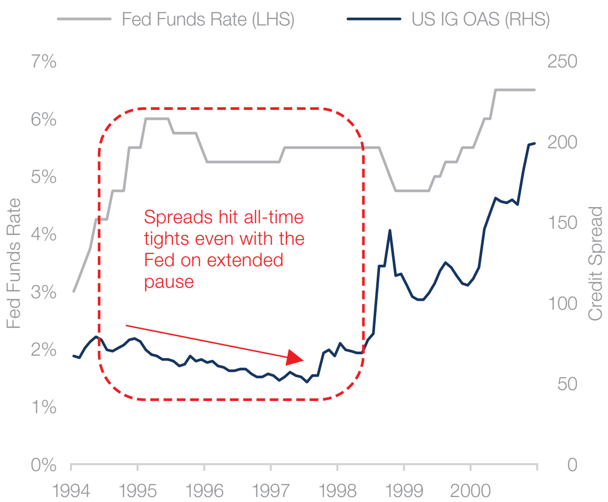
Corporate tax cuts may not substantially affect fiscal revenues



Source: Center on Budget and Policy Priorities, DBS

What does this mean for credit? On paper at least, the above outcomes of fiscal prudence, a strong and stable US economy, and an extended pause on Fed rates with expectations of looser monetary policy are hallmarks of a mid-1990s America under President Clinton. This bodes very well for credit investors, if history is any guide. While it is hard to believe that bonds would do well under an extended policy pause, the mid-90s analogue shows that spreads remained on a multi-year trend of tightening, resulting in strong returns even without the help of the Fed.

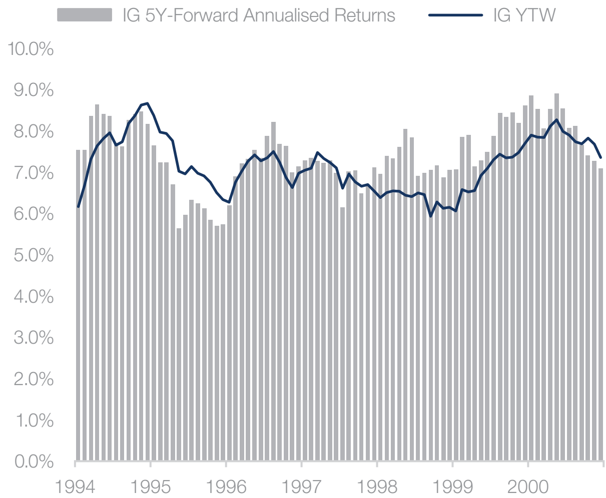
Credit spreads on a multi-year tightening trend in the 90s



Source: Bloomberg, DBS

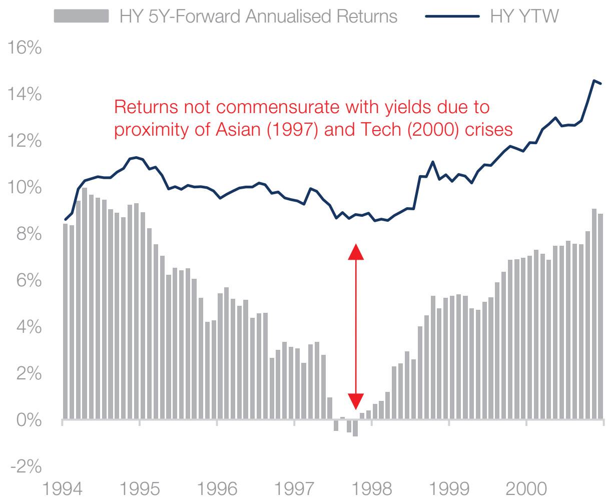
Quality remains key. This is most evident with IG credit. We looked at the annualised returns over a five-year forward period between the years 1994 and 2000 and compared it to the starting yields-to-worst (YTW), and found that investors basically got what they purchased in yield terms. This is intuitive, as capital gains are unlikely with the Fed not on an

IG credit annualised returns were commensurate with their starting yields…



Source: Bloomberg, DBS

…while higher yields could not save HY returns



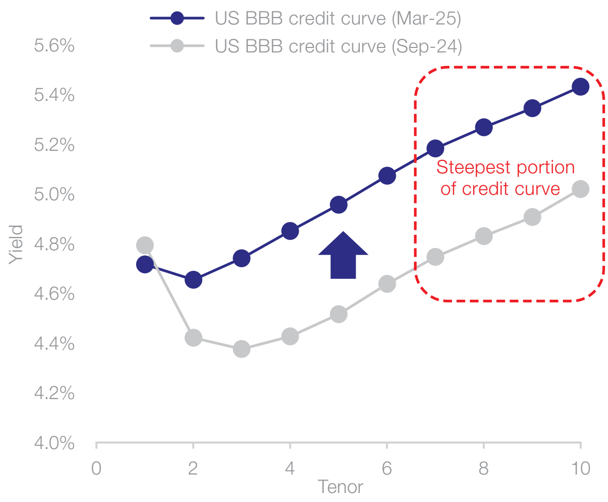
Source: Bloomberg, DBS

aggressive cutting cycle. HY credit, however, paints a different picture. Due to the proximity of major risk events such as the Asian (1997) and Tech (2000) crises, spread widening and capital losses ultimately overshadowed the higher yields on offer. Investing in HY just before the Asian crisis, for example, gave negative annualised returns over the whole five-year period. For that reason, despite expectations of a soft landing, we think that investors in HY should remain defensively in the BB-bucket around the 1-3 year duration segment to prepare for the unexpected.

Duration barbell remains optimal. While the ills of fiscal dominance remain, we continue to think that the 2-3 year duration bucket offers good income with low sensitivity to positive economic surprises. However, the steepening of the yield curve under expectations of expansionary Trump policies presents an opportunity for investors to extend duration, given that President Trump's "shoot first, ask questions later" approach to tariffs as leverage implies that negative headlines can still ultimately cloud the blue-sky narratives of tax cuts and economic expansion; an outcome that finds precedence in his first term. Value has emerged in the 7-10 year portion of the curve, with potential roll-down benefits.

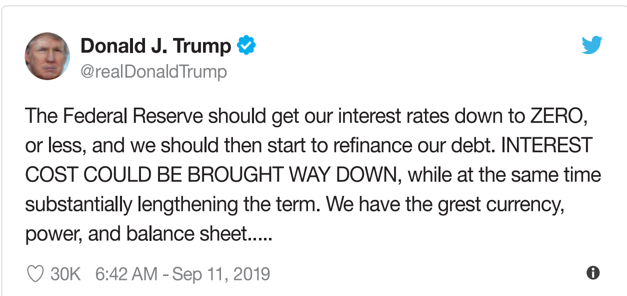
Spoiler alert – Trump does not like high rates. Moreover, newly appointed Treasury Secretary Scott Bessent has spoken of his 3/3/3 rule (targeting 3% real GDP growth, 3% annual budget deficit/GDP, and raising US energy production by three million barrels of oil per day) which represents a slowing of growth, reduction of fiscal spending and decrease in inflationary pressure (increased oil supply). Explicitly, he had even vocalised a preference for lower 10Y

Steep credit curve means that investors are now better compensated for duration



Source: Bloomberg, DBS

rates. Adding to this the initial analysis that President Trump's policies are congruent with a lower rates and weaker dollar environment, potentially transitioning to a tighter fiscal/easier monetary policy stance, there appears to be no shortage of tailwinds for the asset class of fixed income. Most notably, President Trump himself is cognisant of the ills of fiscal dominance, judging from his earlier tweets on how to fix America's debt problem with lower rates.



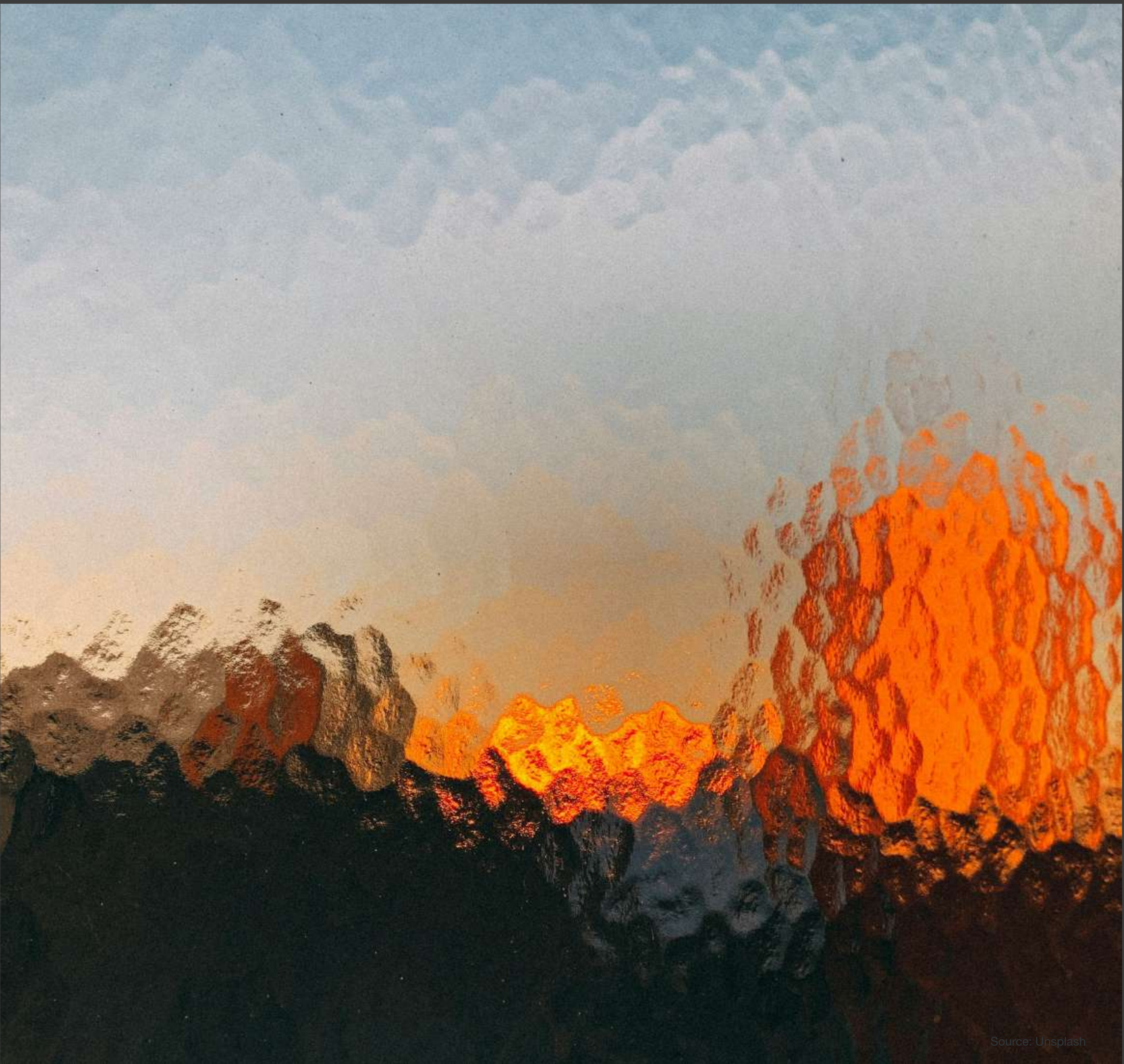
Source: X (formerly known as Twitter, Inc.)

In summary, we think that fixed income could be buoyed by a lower rates regime that supports President Trump's "America First" agenda, contrary to popular opinion around tariffs leading to inflation leading to higher rates. With tariffs introducing greater uncertainty, growth no longer benefitting from pro-cyclical fiscal stimulus, and rates allowed to finally descend, bonds could catch a tailwind. Investors should stay up in quality with A/BBB credit, and only make selective picks in the better quality HY BB segment in the 1–3 year duration segment. Portfolio duration should remain in a barbell of 2-3 year and 7-10 year segments (resulting in an overall 5-7 year portfolio), although steeper curves now present an opportunity to extend duration. As inflation today has been driven by profligate government spending, we believe that this generation's "Paul Volcker" needs to come in the form of a President – not a Fed chair – who can put the brakes on the runaway train of fiscal spending and slay this inflationary wyvern. Yes, there is a difference between what should be done and what will be done, but we are quietly hopeful that they could be one and the same under President Trump's swansong.

Reduced USD Bullishness

Global Currencies
2Q25

Reduced USD bullishness as US exceptionalism fades and tariffs evolve into a growth risk. Too early to switch to a multi-month USD-negative view as it still draws support from elevated yield spreads and shaky risk sentiment.



Source: Unsplash

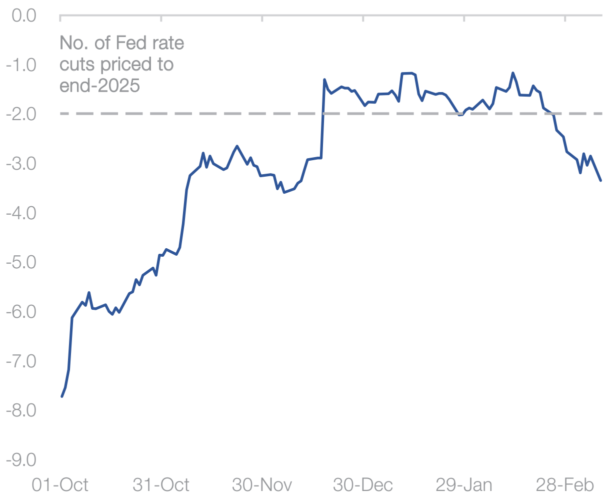
09. Global Currencies.

Terence Wu
Strategist

Carie Li
Strategist

FX in review. In 1Q25, we laid out a USD-positive thesis built on a less dovish Fed and the threat of additional tariffs. This thesis held up well through to mid-February before coming apart as US macro exceptionalism, which afforded the Fed room to slow down rate cuts, started to unravel. We now note pockets of US data weakness, and 1Q25 may see a contraction in the US economy. On tariffs, there has been a shift in focus towards their growth risks, rather than their inflation risks. This change in the market's view on the US economy (and by extension, the USD) is best illustrated in its expectations of Fed rate cuts. After having priced in around one to two Fed rate cuts in 2025 up to mid-February, the market has since turned more dovish. By mid-March, the market is expecting around 3.5 cuts in 2025, significantly more than the Fed's official communication.

The market priced in more than two Fed rate cuts since mid-February



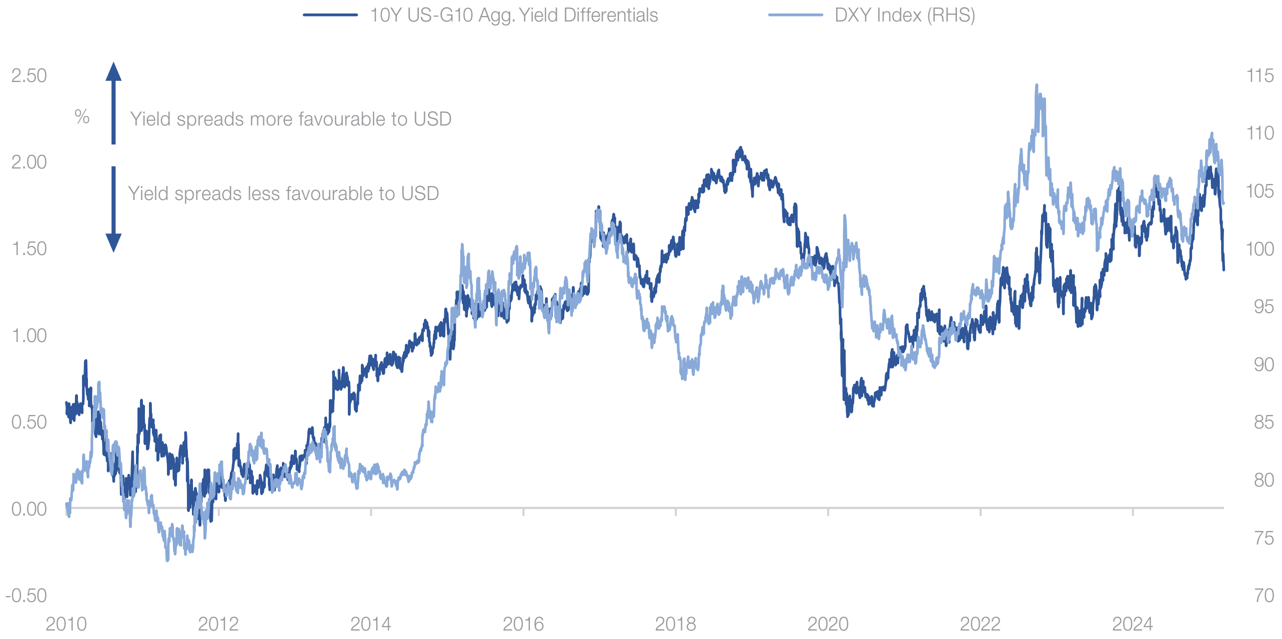
Source: Bloomberg, DBS

Reduced USD bullishness. Taken together, these developments have triggered a sharp USD drawdown, which could overflow into early 2Q25. There is cause for us to temper our USD-bullish view, but it is premature to revert to a multi-month USD-negative posture. We continue to expect the USD to draw strength from its still-elevated yield advantage and a worsening risk sentiment.

The USD's yield advantage has reduced… The UST yield curve is lower YTD, triggered first by the Fed's reluctance to project a more hawkish stance in the face of tariff-driven inflation risks, then by the spreading US growth weakness. Given that inflation expectations have also risen during this period, what we saw was a yield compression against the USD both on nominal and real terms. The 10Y UST-G10 yield spreads have compressed around 50 bps YTD. It is unsurprising that it should lead to some immediate USD downside.

…but spreads will remain supportive of the USD. Nevertheless, there should be limited downside for UST yields from current levels. The Fed should curtail excessively dovish expectations, thereby providing support for UST yields. Moreover, from a longer-term perspective, the compression comes off a very elevated UST yield baseline. Prior to the YTD compression, the 10Y UST-G10 yield spreads were standing at six-year highs. Even at the current levels, the yield spread is still more in favour of the USD now, compared to more than 70% of the time over the past 15 years. Thus, the USD's yield advantage is still present, albeit softer relative to multi-year highs. This yield advantage is unlikely to go away unless the US falls into a deep recession, something that is currently not our baseline expectation.

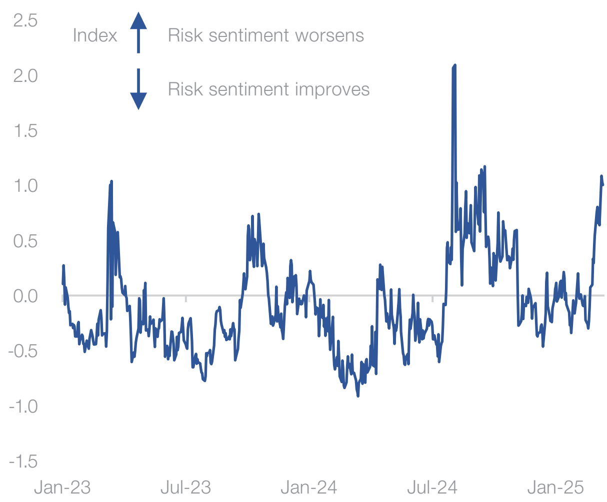
Yield spreads remains firmly in favour of the USD



Source: Bloomberg, DBS

Jittery risk sentiment may trigger USD's haven flows. As the growth risks posed by tariffs gain market attention, we have noted a worsening of market risk sentiment. This is mostly clearly illustrated in the US equities space, where the S&P 500 has retreated off highs and the VIX is on a steady climb since mid-February. The USD tends to outperform on haven flows in periods of market stress – this has admittedly not materialised yet, but we could see this dynamic coming into play in 2Q25, when the tariff narrative will likely step up upon the conclusion of the trade reviews mandated under the "America First Trade Policy" memorandum.

Market sentiment has taken a turn for the worse

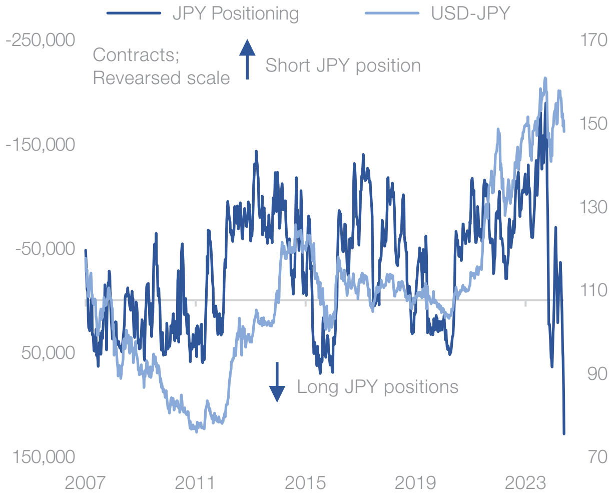


Source: Bloomberg, DBS

EUR driven by a regime change in German fiscal policy. The EUR faces a major idiosyncratic positive. German Chancellor-in-waiting Friedrich Merz announced fiscal plans in early March that could unleash a wave of government spending on defence and infrastructure. In fiscally cautious Germany, this is a regime change. The scale of the anticipated fiscal spending could materially alter the growth outlook of Germany and the Eurozone. It also coincides with a period where Eurozone data outcomes and equities are outperforming the US, reinforcing the relative attractiveness of European assets. We expect this to have an immediate positive flow through to the EUR-USD, at least in the tactical horizon. Thus, we could see the EUR-USD staying elevated in early 2Q25, before reverting lower in the multi-month horizon.

JPY to outperform against non-USD majors. Beyond the EUR, the other major currencies are susceptible to the above-mentioned USD cues. In discussing the USD trajectory, we outlined an environment of moderating US growth and rising risk-off sentiment. These conditions strengthen the case for the traditional safe havens. The flat-to-lower yield environment also makes carry trades less attractive, with the subsequent unwinding further favouring the low-yielding funding currencies. Taken together, these global dynamics are strong JPY-positives. Domestically, rising expectations of BOJ rate hikes drove JGB yields higher, and allowed the long-absent positive correlation between JGB yields and the JPY to re-emerge. Domestic cues could further strengthen if this year's shunto negotiations conclude with another round of outsized wage increases. Thus, the JPY has several positives going for it into 2Q25. This leaves us with the view that the JPY should strengthen against non-USD major currencies. Take caution though, as these JPY-positives have been well-noted by the market, and long-JPY positions are now near historical extremes. The risk of a sharp unwinding of JPY-longs, and its negative impact on the JPY, is non-negligible.

Long JPY positions are at historical extremes



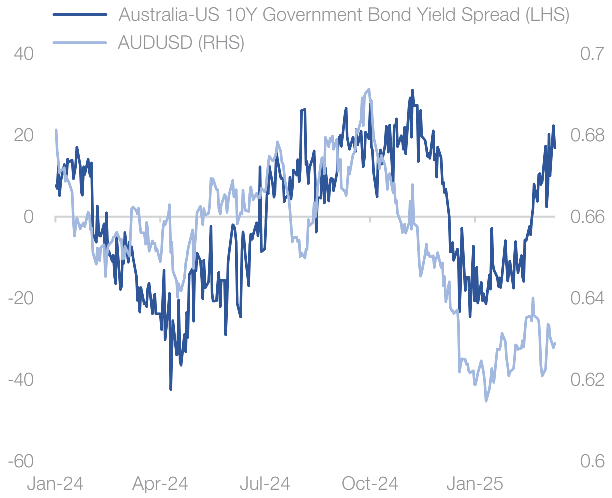
Source: Bloomberg, DBS

CHF less attractive than the JPY: Being a fellow safe haven and funding currency, the CHF faces similar positive dynamics as the JPY. However, domestic and EU-specific cues are not as positive for the CHF. Switzerland may be facing deflation again soon, compelling the SNB to adopt a dovish stance. We do not rule out the SNB cutting policy rates to zero by this year. Furthermore, with EU growth looking on the up, there is risk of a rotation out of CHF towards EUR. These idiosyncratic CHF-negatives is likely to offset the risk-related positive drivers to keep the CHF soft.

AUD disadvantaged by its role of a proxy for the RMB. Expect the AUD to still be driven more by global cues than domestic drivers. We continue to detect China-specific risks for the AUD, namely the still-weak domestic demand and housing market, and the threat of further tariffs. So long as these China-specific risks do not alleviate in a convincing manner, it is difficult to construct a sustained AUD-positive argument. On the domestic front, even though the RBA tries to project a patient stance, market expectations of RBA rate cuts continue to increase. Thus, do not expect domestic drivers to be an AUD-positive for now. Even with the USD looking impinged in the near-term, we do not expect the AUD-USD to be breaching YTD highs in 2Q25. In contrast, expect the AUD-USD to trade in a sideways to heavy tone.

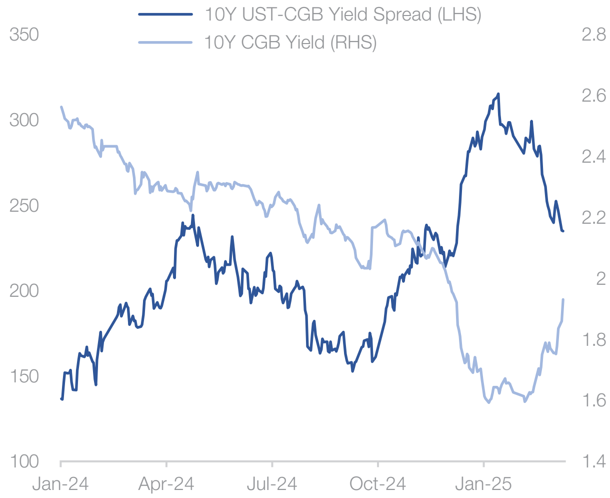
RMB outlook is better than expected. Despite tariff risks, the RMB's decline against the USD has been well managed YTD. This is attributable to the PBOC's insistence in setting USD-CNY fixing rate below the 7.2000 handle, which effectively caps the USD-CNY below 7.3500. As such, the USD-CNH also finds it difficult to breach the 7.4000 locus. Another reason is the measured retaliation to Trump's new 20% tariffs, which signalled China's preference to avoid a tit-for-tat tariff war. In addition, China has seen several positives this year that have supported sentiment around China. This ranges from the emergence of Chinese tech (best represented by DeepSeek), to President Xi's appearance at a private sector symposium, to the ambitious GDP growth target set out in the Two Sessions. This has spurred optimism on a Chinese recovery and

AUD benefitted little from its yield advantage



Source: Bloomberg, DBS

10Y UST-CGB yield spread narrowed



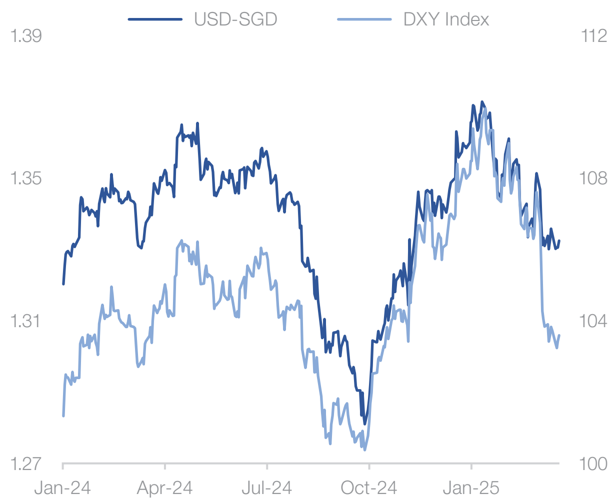
Source: Bloomberg, DBS

provided support for the RMB. Note that CGB yields have reverted higher after a multi-year decline to record lows. This narrows the UST-CGB spread, a longstanding RMB-negative. These developments suggest that we should resist calls for excessive RMB weakness. Expect the USD-CNY to be capped below 7.3500.

Also contain excessive RMB optimism. The sharp rally of RMB between Sep and Oct 2024, and its equally fast reversal is a cautionary tale. It reminds us to be cautious about being too quick to turn too optimistic about China's growth outlook and the RMB's upside prospects. Unless there is a sustained material alleviation in China's domestic challenges, and persistent tech sector positives, the recent China optimism may fade.

SGD: Asian currencies in general are facing divergent drivers. Tariff risks are still real (negative for Asian currencies), but the US moderation should allow a softer USD posture (positive for Asian currencies). The SGD will also be susceptible to these cross-currents. Expect USD-SGD volatility as the market shifts its focus between these divergent drivers. For now, with China coping well with the additional tariffs, the focus looks to be on the US moderation. This could allow the USD-SGD to search lower in the near-term. However, on a multi-month basis, tariff risks may reassert, leaving the USD-SGD higher towards the end of 2Q25. Furthermore, the SGDNEER Index continues to look elevated relative to its estimated mid-point. This gives scope for the SGD to weaken against the basket of currencies. Thus, we should resist chasing any near-term USD-SGD downside, with expectation that the pair could recover towards the 1.3700 handle by end of 2Q25.

USD-SGD tracking the DXY Index lower

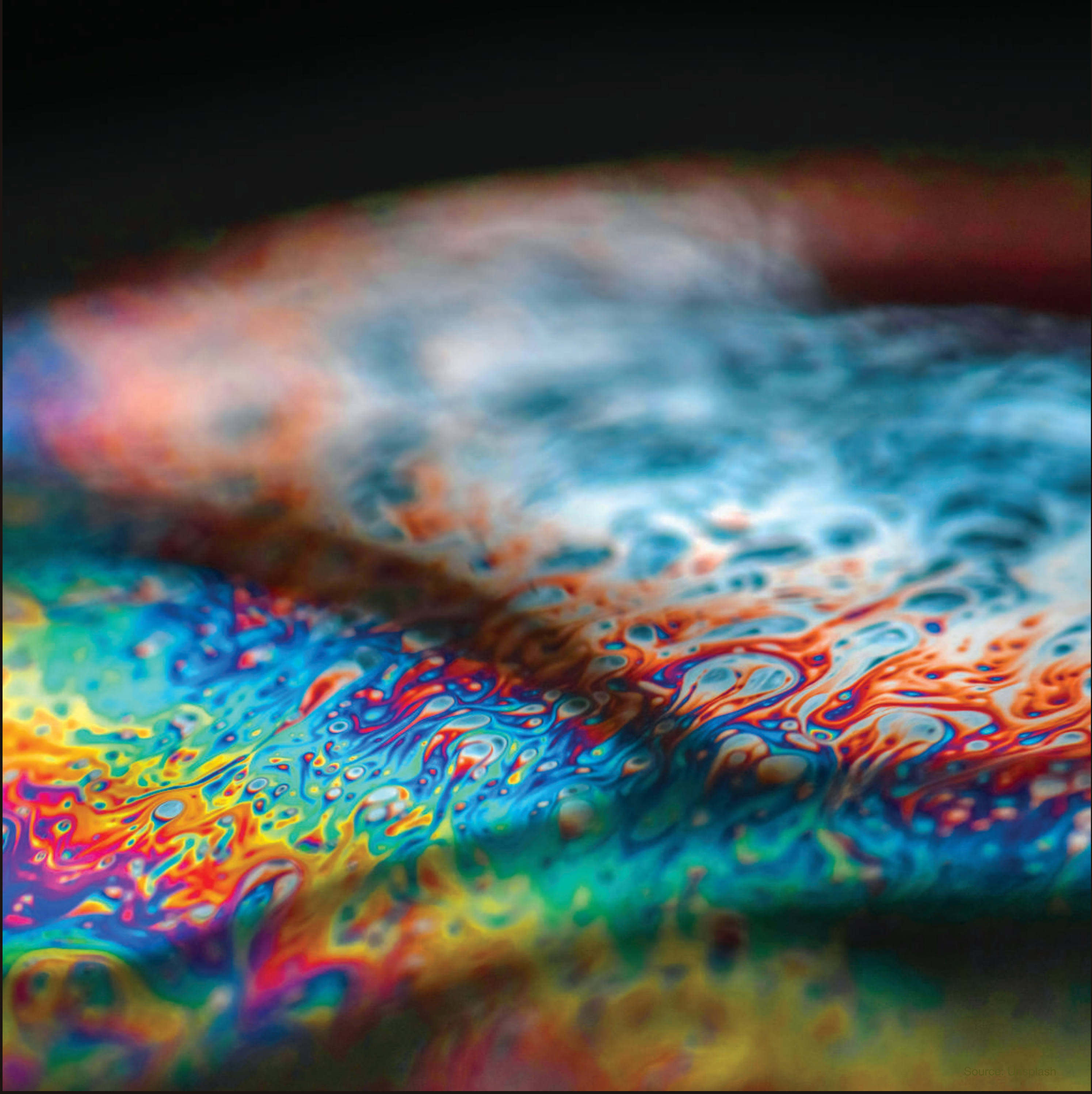


Source: Bloomberg, DBS

DBS currency forecasts

Exchange rates, eop	11 Mar	1Q25	2Q25	3Q25	4Q25	1Q26	2Q26	3Q26	4Q26
China	7.2479	7.26	7.34	7.32	7.29	7.27	7.25	7.22	7.20
Hong Kong	7.7684	7.77	7.80	7.79	7.79	7.79	7.78	7.78	7.77
India	87.315	87.6	88.8	88.7	88.5	88.4	88.3	88.1	88.0
Indonesia	16437	16450	16500	16430	16370	16300	16230	16170	16100
Malaysia	4.4320	4.45	4.52	4.49	4.47	4.44	4.41	4.39	4.36
Philippines	57.390	57.7	59.0	58.9	58.8	58.7	58.5	58.4	58.3
Singapore	1.3336	1.34	1.37	1.36	1.36	1.35	1.34	1.34	1.33
South Korea	1458	1460	1480	1475	1470	1460	1455	1450	1445
Thailand	33.908	34.1	35.0	34.8	34.5	34.3	34.1	33.8	33.6
Vietnam	25489	25520	25650	25620	25600	25570	25540	25510	25480
Australia	0.6272	0.62	0.60	0.61	0.61	0.62	0.62	0.62	0.63
Canada	1.4436	1.45	1.46	1.46	1.45	1.45	1.45	1.44	1.44
Eurozone	1.0847	1.08	1.04	1.05	1.06	1.07	1.08	1.09	1.10
Japan	147.03	148	151	149	148	146	144	143	141
New Zealand	0.5690	0.57	0.55	0.55	0.56	0.56	0.57	0.58	0.58
Switzerland	0.8795	0.89	0.92	0.91	0.91	0.91	0.90	0.90	0.89
United Kingdom	1.2886	1.28	1.23	1.24	1.25	1.26	1.28	1.29	1.30
United States	103.85	105.0	110.0	109.2	108.3	107.5	106.7	105.8	105.0

Australia, Eurozone, New Zealand, and United Kingdom are direct quotes.



Good Start to the Year

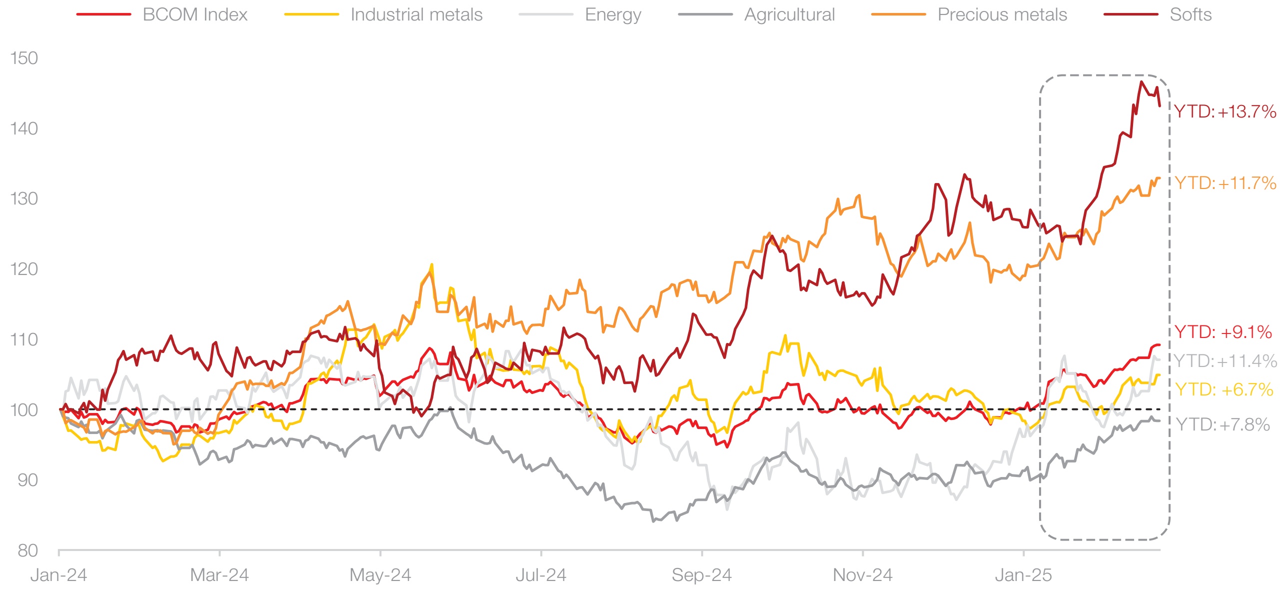
Commodities
2Q25

Commodities surprised on the upside, registering positive YTD returns due to supply squeezes and pre-emptive stockpiling. Nonetheless, caution is warranted as growth drag and demand destruction from tariffs work their way through the global economy.

10. Commodities.

Goh Jun Yong
Strategist

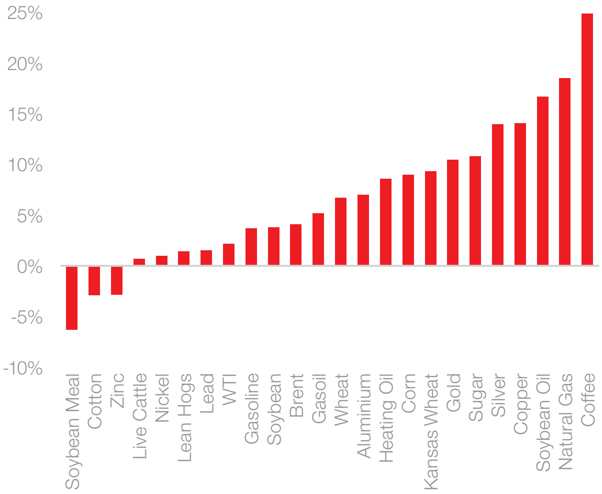
Commodities have regained some lost ground from last year



Source: Bloomberg, DBS. Data as at 21 Feb

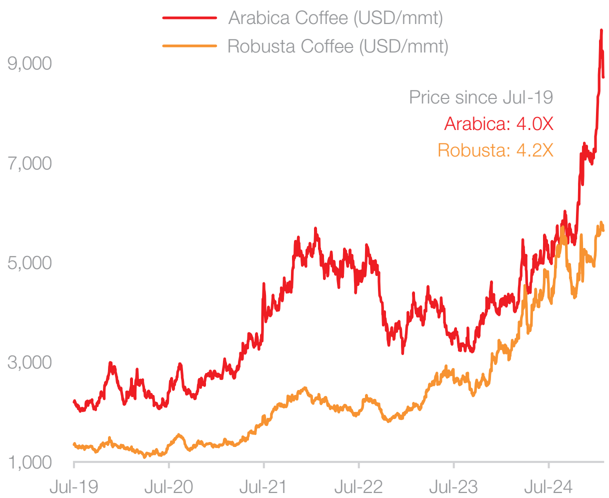
Positive YTD flows despite an uncertain backdrop. Commodities have registered positive flows thus far in 2025 after flatlining for the last year or so. This came as somewhat of a surprise considering the macro environment has remained tepid (economic growth has been somewhat resilient, with no major surprises to the upside), and uncertainties abound in the newly minted Trump 2.0 era. Elevated rates, a strong USD, and tariff risks add further headwinds for the asset class. Nonetheless, commodities had a good start to the year, with the BCOM index up 9.1% YTD (as at 21 Feb) and all subsectors in the green. Softs were a standout performer, registering a 13.7% gain on the back of rising coffee prices. Precious metals and energy followed closely behind with 11.7% and 11.4% respectively, buoyed by heightened uncertainty and tariff risks under Trump 2.0. The sector closest to the secondary economy in the form of industrial metals performed the worst, rising 6.7% YTD.

Individual commodity performance YTD



Source: Bloomberg, DBS. Data as at 21 Feb

Green coffee prices have quadrupled in the past five years



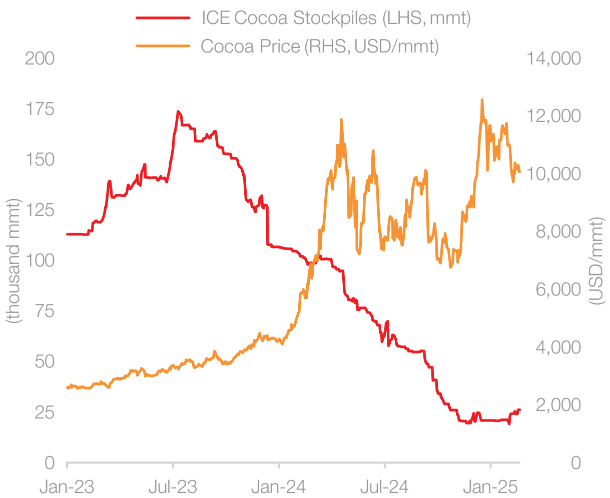
Source: Bloomberg, DBS

Agricultural and Soft Commodities

An expensive caffeine fix. Coffee was the single best performing commodity so far this year with Arabica and Robusta coffee gaining 23.8% and 12.4% respectively. The thesis for coffee remains the same as what we have highlighted in past quarters – growing global demand coupled with supply challenges brought on by global warming. Brazil and Vietnam, the two largest coffee producing nations in the world, continue to see dwindling production due to dry, arid weather. Brazil's National Supply Company (CONAB), released its first report for this year's harvest in January, confirming that supply for this coming harvest year is going to be challenged yet again; 2025/26 production at 51.81mn bags, down 4.4 % compared to 2024/25. This is the lowest production level recorded since 2022/23, when production reached 50.9mn. Additionally, January's International Coffee Organisation monthly report highlighted that certified stocks of Arabica coffee shrank to 0.91mn 60-kg bags, an 11.7% decrease from Dec 2024. Similarly, Robusta coffee has seen three consecutive years of deficits due to drought conditions in Vietnam. While supply may catch up in the coming years, legislation such as the EU's new deforestation law, which prohibits the sale of goods made from commodities grown on deforested land from being sold on the bloc, will present challenges. Additionally, the lack of investment in farming technology and infrastructure, as well as weather-driven volatility, throws further headwinds into the mix.

Cocoa supply remains in a pickle. While cocoa has underperformed on a YTD basis (-13.7%), it remains one of the best performing commodities over the past year; from 1 Jan 2024 to 21 Feb 2025, cocoa returned +135.7%. The outperformance of cocoa is likely to persist in 2025 and beyond as the underlying reasons for the price increase have not been resolved. We previously highlighted that an ongoing deficit in the global cocoa market — driven by resilient demand for cocoa and cocoa products, supply shocks from El Niño, fertiliser shortages, and outbreaks of swollen-shoot disease in Ivory Coast and Ghana (which together account for two-thirds of global production) — was responsible for the price increase.

Exchange cocoa stocks have declined in the past year and a half

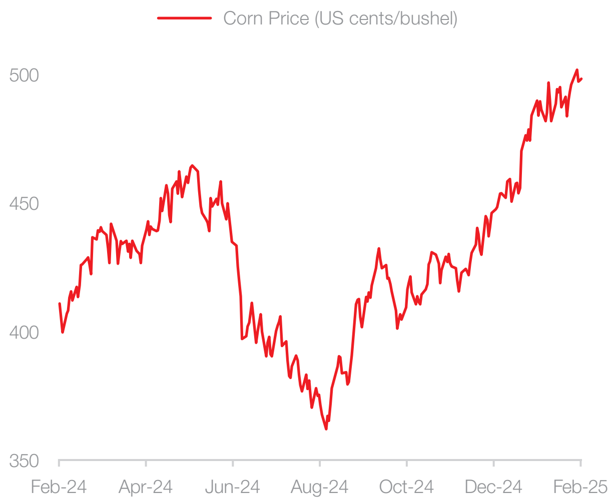


Source: Intercontinental Exchange (ICE), Bloomberg

This continues to be the case as global demand for cocoa products remain robust while supply struggles to keep pace. This can be seen in how cocoa stocks around the world have steadily depleted over the past year and a half; Intercontinental Exchange stocks of cocoa have fallen by more than 80%, from 163,820 tonnes in Sep 2023, to just 26,070 tonnes in February this year. Independent licensed warehouses in New York are also showing concerning stock levels at this time of the year; total stocks are at c.90,000 tonnes.

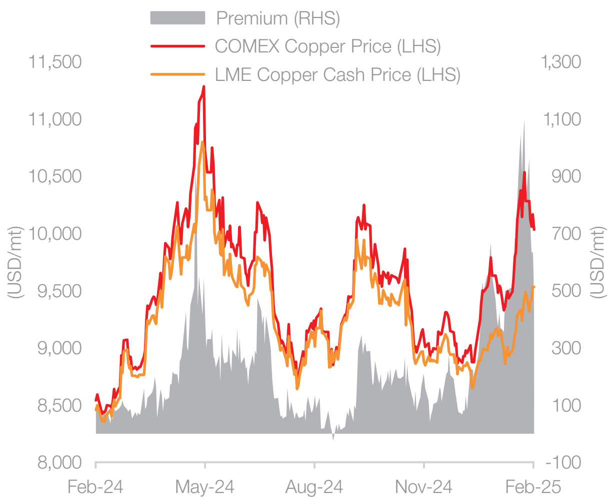
Lower US and Argentina output for corn. In addition to coffee and cocoa, corn prices have also risen this year due to a projected supply squeeze. The US and Argentina, the first and fourth largest producing countries respectively, are expected to see reductions in their 2024/25 harvests. US corn yields were revised downwards from 183.1 bushels/acre to 179.3 bushels/acre from Dec 2024 to Jan 2025, resulting in a net reduction in 2024/25 production from 385mmt to 378mmt. Similarly, Argentina is expecting lower yields this season due to dry and warm conditions; corn in bad conditions was at 22% at the end of January this year, twice as much as it was during the same period last year. As a result, the Buenos Aires Grain Exchange lowered its forecast for Argentina's 2024/25 harvest by 1mmt to 49mmt. On the demand side, corn is expected to stay resilient as global demand was revised slightly upwards thanks to its key role in livestock feed and biofuel production. Corn prices were up 8.7% YTD (as at 21 Feb). While the threat of tariffs remains ever-present, corn prices look to be supported from a fundamental perspective for the coming year.

Corn prices have been on the rise since Aug 2024



Source: Bloomberg, DBS

COMEX copper premium over LME stretched due to tariff worries



Source: Bloomberg, DBS

Industrial Metals

Tariff-induced premiums for COMEX copper. Industrial metals was the worst performing sector in the commodities complex, but still managed a YTD gain of 6.7% (as at 21 Feb) on the back of relatively resilient economic data in both US and China. US manufacturing PMI rebounded over the 50-point mark for January and February while initial jobless claims have been on a downtrend since late last year. In China, 4Q24 GDP growth surprised on the upside at 5.4% y/y, with full-year growth hitting the official 5.0% y/y target. The Caixin manufacturing PMI also managed to stay in expansionary territory for the first two months of the year.

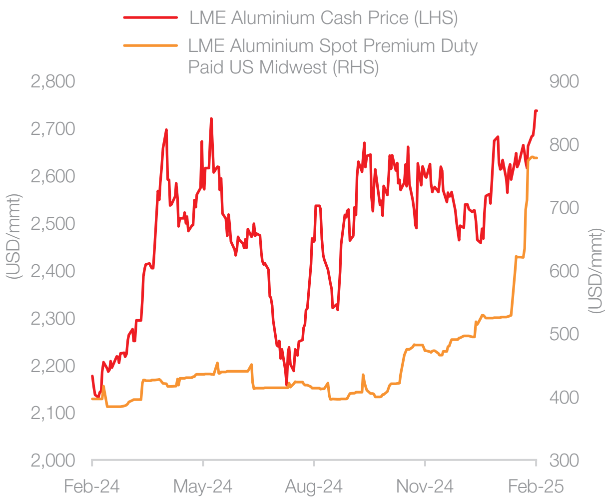
Among industrial metals, copper was the best performing with COMEX copper futures recording a +14.5% performance YTD (as at 20 Feb). There are several reasons for this outperformance. Firstly, China expanded its trade-in programme, extending some subsidies – such as on EVs – while also increasing eligibility on other subsidies, which helped with sentiment around copper demand. Secondly, there was a premium for COMEX copper (over its LME counterpart) due to concerns that the US might impose tariffs impacting metals. The average premium of the front-month COMEX contract over LME cash stood at USD129/mmt on 18 Dec 2024, compared to USD1,099/mmt on 13 Feb 2025. The US copper premium over London fell immediately following Trump's inauguration, as the new administration was silent on tariffs in the first few days post-inauguration. However, as it became clearer towards the end of the month that tariffs would indeed be employed swiftly, the premium grew again. Notwithstanding a positive first quarter performance, our outlook for copper remains cautious; while the first-order effects of tariffs include stock-piling and temporary price increases, second-order effects often involve demand destruction at the margin, which could in turn dampen prices in the medium term.

25% tariffs on aluminium. Aluminium benefitted from the same tailwinds that buoyed the industrial metals complex; economic resilience in the major economies kept demand reasonably supported while worries on the supply side added further upside for the metal in the first two months of 2025.

The first of the two factors impacting supply was the EU's proposal to ban imports of Russian aluminium. EU envoys agreed on a new sanctions package on 19 Feb that includes a ban on primary aluminium imports. How much the ban will impact aluminium prices remains to be seen; circumvention is a perpetual problem that plagues sanctions, not to mention Russian aluminium makes up only about 6% of EU aluminium imports. Further, the ban will not be effective immediately and only comes into force a year from the official adoption of the package.

The second factor was China's removal of its export rebate on aluminium, which could curb the flow of Chinese aluminium abroad, thereby reducing global supply. Another major development that proved to be moderately bullish for short-term aluminium prices was the announcement of 25% tariffs on aluminium and steel by the US on 11 Feb. This resulted in a c.3% increase in LME aluminium cash prices in the week following the announcement, as well as a corresponding 23% rise in US Midwest premiums. In the longer term, however, the outlook is

US Midwest premiums for aluminium soar



Source: Bloomberg, DBS

more bearish as there is likely to be weaker demand from the higher all-in price as well as a possibility of growing US production.

<u>Conclusion</u>

Volatility will reign in the short term. Commodities have surprised on the upside in 1Q25, driven by stronger than expected economic momentum. The tariff threat appears to be limited in its consequence for now. In fact, prices for some commodities have been temporarily boosted due to factors such as stockpiling and supply squeezes. However, we continue to be cautious about impending second-order effects from tariffs, including demand destruction at the margin and a subsequent dampening of sentiment. To that end, we continue to favour commodities that benefit from a secular, rather than cyclical, growth story. While the soft-landing scenario continues to play out, the commodities complex will continue to show selective rather than broad-based outperformance.

Anchor in the Storm

Alternatives 2Q25: Gold & Private Assets

Structural bull market for gold as uncertainty under Trump 2.0 buoys short-term demand while de-dollarisation and higher global nominal GDP growth act as longer-term tailwinds. Diversify into a hybrid portfolio for alpha returns and resilience ahead of market gyrations.

Source: Unsplash

11.
Alternatives: Gold.

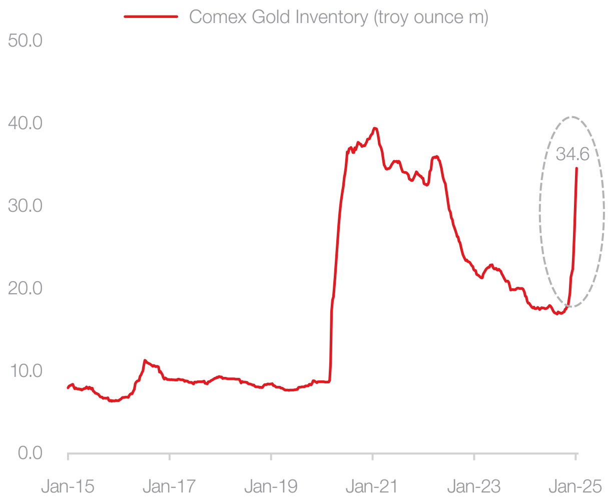
Goh Jun Yong
Strategist

Explaining gold's performance. This quarter, we analyse the reasons for gold's largely unidirectional ascent in the past year and what we can expect from the precious metal moving forward. From immediate factors such as geopolitical turmoil, to medium and longer-term drivers like the widening US fiscal deficit and global GDP growth, this report will endeavour to shed light on them all.

Uncertainty is the biggest immediate driver. In 1Q25, gold hit a series of all-time highs amid global uncertainties; from geopolitical turmoil to trade war worries and fears of resurgent inflation, the past quarter seemed to have it all. On tariff fears specifically, gold staged a strong rally in late January on worries that bullion, which has historically been exempt from import duties, might be tariffed in the future. This resulted in a stockpiling of gold on COMEX, the New York commodity exchange, which saw inventory levels rise 127% since the US election in November last year to reach c.39.7mn troy ounces, or USD115.3bn at current market price (as at 7 Mar). While it is tempting to dismiss such events as a one-off occurrence, or a result of idiosyncratic risk, there is a clear thread tying them together; Trump 2.0 is here to stay for the next four years and it would be prudent to assume a higher level of uncertainty under this regime.

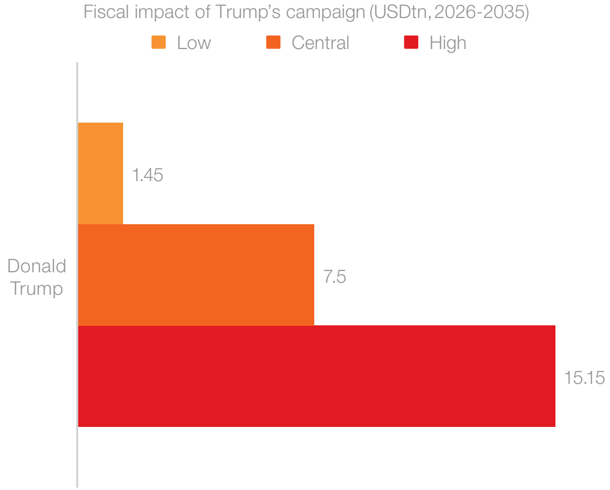
Medium-term drivers – Rising US debt and de-dollarisation. We have spoken at length about monetary debasement and de-dollarisation as structural drivers of gold demand in our past publications. This thesis remains firmly intact. Under Trump, expansionary policies such as tax cuts, increased fiscal spending, and de-regulation are expected to take place, and this will likely exacerbate the US fiscal deficit and prompt an expansion of liquidity in the future; this is positive for gold from a monetary debasement angle. Additionally, the world is expected to become more fragmented from a geopolitical perspective under Trump 2.0, which will continue to drive central bank demand for gold, especially among the BRICS+ nations, which view bullion as their biggest alternative to the dollar.

COMEX gold inventory rose 94% since the US election



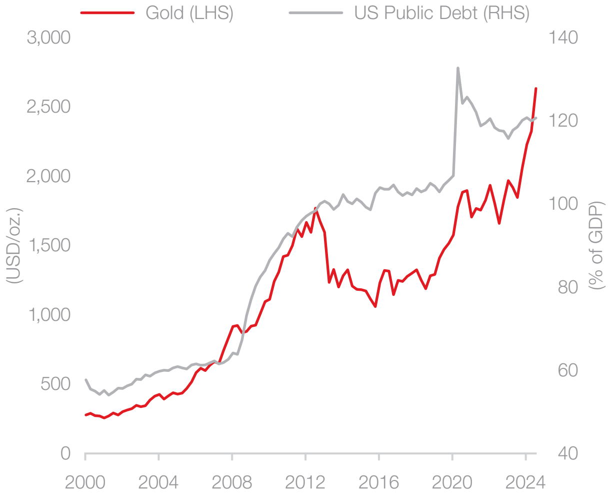
Source: COMEX

US fiscal deficit expected to grow under Trump



Source: Committee for a Responsible Federal Budget, a non-profit that supports lower deficits

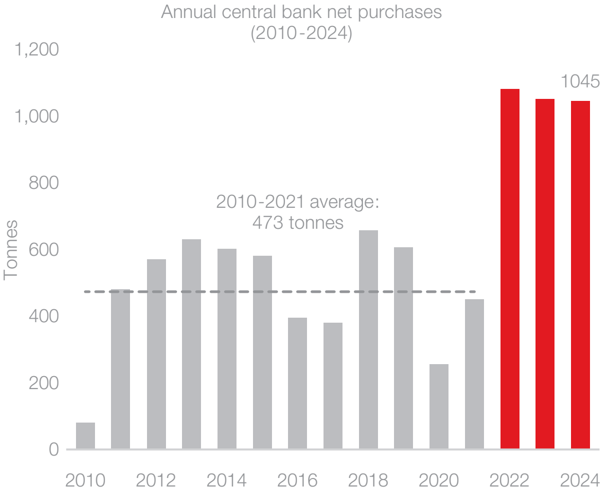
Gold is correlated with US indebtedness, which is expected to rise



Source: Bloomberg, Federal Reserve Bank of St. Louis, DBS

Central bank demand continues to be robust. This trend propelled central bank gold buying to a whopping 1,045 tonnes in 2024. This is the third consecutive year central bank buying exceeded the thousand-tonne mark – significantly higher than the c.473-tonne average between 2010 and 2021. It is also worth noting that de-dollarisation demand is not exclusive to central banks, where more investor classes are beginning to see the merits of buying gold as a hedge against dollar and monetary debasement risk. This is evidenced by robust investment demand for gold, which grew 25% y/y in 2024 to reach 1,180 tonnes, a four-year high. To summarise, fiscal expansion in the US and growing global fragmentation will continue to strengthen the appeal of gold in the medium to long term.

Central bank gold buying remains elevated, reaching 1,045 tonnes in 2024

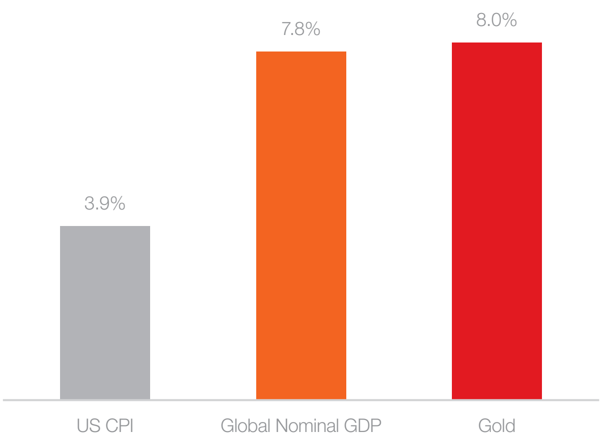


Source: Metal Focus, Refinitiv GFMS, World Gold Council

Long-term – conventional ways of looking at gold are limited. For even longer-term time frames (>10 years), there are two main conventional ways of estimating gold's return. The first is using inflation as a gauge since gold is often deemed as a store of value. The problem of doing so, however, is that gold's empirical returns far exceeds CPI growth. Using US CPI as a proxy, gold's return (8%) over the past 50 years is almost double that of inflation. The probability that this is due to chance is extremely low. The second way is through examining gold production cost and using that as a proxy for marginal gold price. The issue here is that in reality, miners typically react to gold price and not the other way round – higher gold cost means miners are more willing to mine more expensive deposits and vice versa. Additionally, gold cannot be consumed unlike other commodities which have an ever-growing source of supply ready to return to the market in the form of recycled supply, which competes with primary production. In short, conventional ways of estimating gold's long-term return are limited at best.

Gold has outperformed inflation significantly in the last 50 years

Annual growth in US CPI, global nominal GDP, and gold price (1971-2023)



Source: Bloomberg, Federal Reserve Bank of St Louis, LBMA Gold Price PM, World Gold Council

Distilling gold's return into an economic and financial component. Taking into account the different ownership and demand sources of gold, a more holistic way of looking at gold's price/return is through a lens of two distinct components: economic and financial.

- Economic component: Consumer demand (from technology and jewellery) and long-term investment demand (including central bank demand)
- Financial component: Shorter-term investment demand and hedging demand

Economic expansion and opportunity cost tend to impact the economic component of gold's return while risk, uncertainty, and momentum tend to impact the financial component.

GDP growth and global market capitalisation as proxies. We reproduced a study done by the World Gold Council with slightly different parameters and came to the same conclusion that the **primary driver of gold price over an extended time horizon is nominal GDP, with global equity and bond market capitalisation acting as an offsetting factor** (via the substitution effect). A linear regression analysis using annual data from 1971 – 2022, yielded a positive coefficient between global nominal GDP and the price of gold (2.8), and a negative coefficient between global equity and bond market capitalisation and the price of gold (-1.0). More importantly, the analysis produced an R-squared value of 89% (i.e. 89% of variance in gold price can be explained by a combination of nominal GDP and global equity and bond market capitalisation), indicating a strong fit of the dependent and independent variables.

Gold long-term price model (1971 – 2022)

Dependent variable:	Log gold price (USD/oz.)
Log global nominal GDP(1)	2.417
Log global equity(2) and bond(3) market capitalisation	-0.997
Observations	52
R-squared value	89%

Source: Gold price used in this analysis is the LBMA London PM session spot price, sourced from Bloomberg. (1) Nominal GDP, sourced from Federal Reserve Bank of St. Louis FRED database. (2) World equity market capitalisation by World Federation of Exchanges, sourced from World Bank database. (3) World bond market capitalisation proxied by "Amount Outstanding of International Debt Securities for All Issuers, All Maturities, Residence of Issuer in All countries" by BIS, sourced from Federal Reserve Bank of St. Louis FRED database.

Using this framework as a guide, we can predict gold's average annualised return with the help of third-party estimates for nominal GDP and world equity and bond market capitalisation. Using estimates provided by JP Morgan's 29th Long-term Capital Markets Assumptions report, we arrive at an estimated annualised return of c.6.2% for gold over a 10 to 15-year horizon (based on annual nominal GDP growth of 5.0%, and World Government Bonds return of 4.2% and AC World Equity return of 7.1% with a 60/40 weightage). While this is by no means a definitive way of determining the intrinsic value of gold, it certainly gives us some perspective of what its potential long-term return could be.

All that glitters is gold. Regardless of the time frame in question, all signs point to compelling tailwinds for gold as an asset class. In the immediate term, volatility under Trump 2.0 should power safe haven demand for bullion. The latest rumblings about the possible revaluation of the US gold reserves (from a book value of USD42/oz. to market price) add further positive momentum behind the asset class. In the medium to long-term, tailwinds from monetary debasement and de-dollarisation continue to be at play, and over an even more protracted time horizon, gold's return has been empirically shown to outperform inflation and track global GDP closely, putting it in a good position for long-term capital appreciation. Against this tremendously positive backdrop, we maintain our bullish stance on gold and 12M target price of USD3,330/oz. that we established on 7 Feb 2025, which is based on the assumption of a dollar index level of 110.8 and US 10Y treasury yield of 4.4% by 1Q26.

Alternatives: Private Assets.

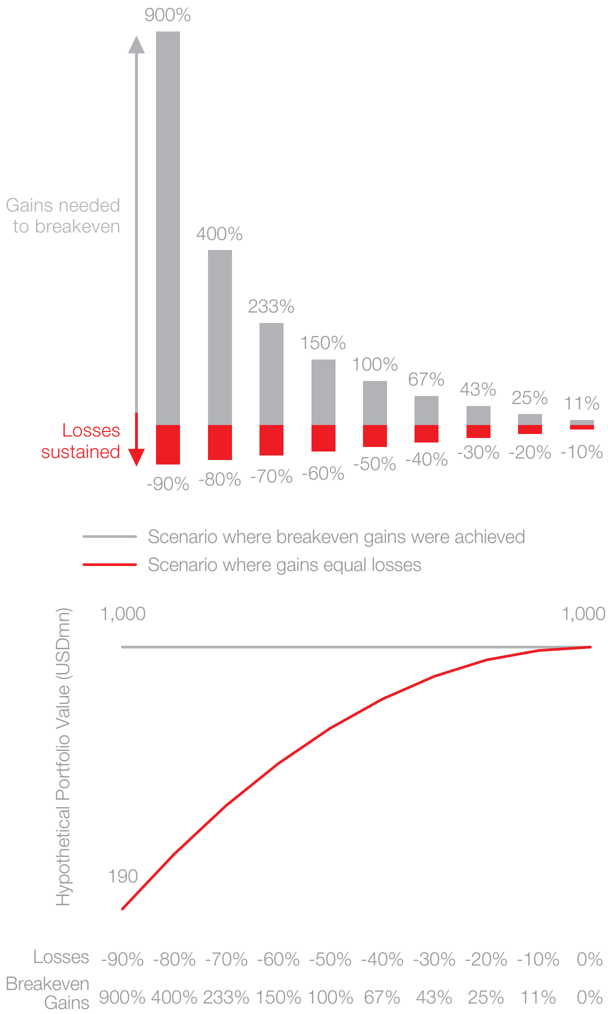
Daryl Ho, CFA
Strategist

Elijah Tan, PhD
Analyst

Diversify, or count your losses. Losses and gains are asymmetric in nature, and recovery is harder than initial loss-making. In volatile markets, a strategy for minimising losses is essential. Diversification, which spreads investments across uncorrelated assets, averages out gains and losses, and minimises overall portfolio drawdowns. However, diversification can also precipitate performance drag. That said, our analyses reveal the loss-hedging benefits of diversification significantly overshadows costs of performance drag over a 10-year horizon, making diversification an indispensable portfolio management tool.

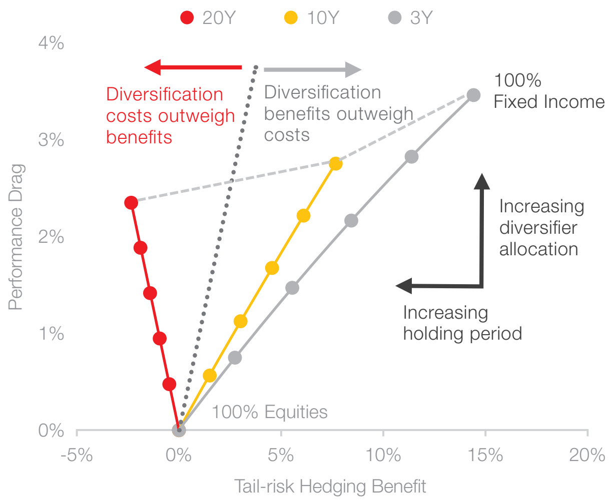
Hedge with an edge. Interestingly, performance drag increases with shorter holding periods. Said differently, too many short-term low-correlating positions in a portfolio can accrue significant diversification costs from performance drag. Therefore, apart from downside protection, effective diversification requires an illiquidity premium to offset these costs. Pursuing illiquidity premium, in turn, warrants a strategy that considers investor's unanticipated liquidity needs. A hybrid portfolio strategy, combining high illiquidity premia of private assets with liquidity of public assets, best exemplifies this. The result can be superior drawdown protection and returns uplift, compared to the 60/40 portfolio.

Every loss requires a greater gain to breakeven



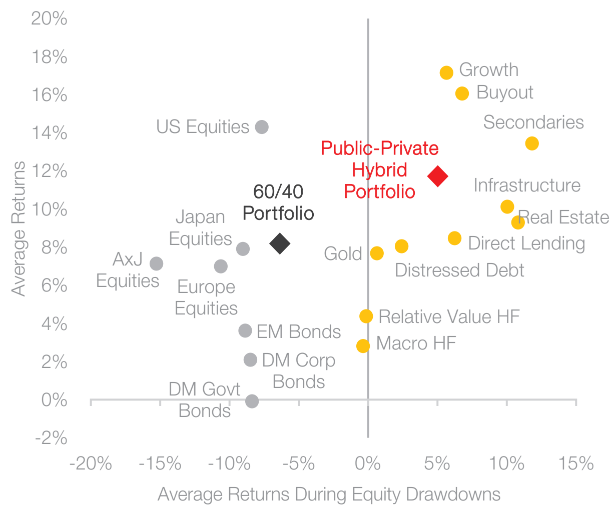
Source: DBS

Diversification benefits outweigh costs over a 10-year horizon



Source: Pitchbook, Bloomberg, DBS

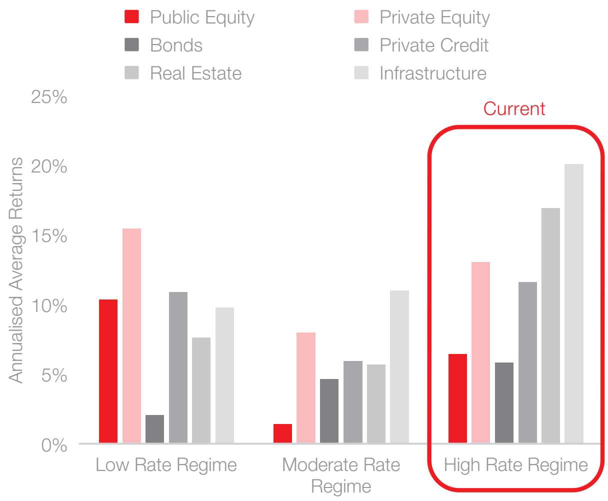
Private assets offer superior returns and hedging benefits over public counterparts

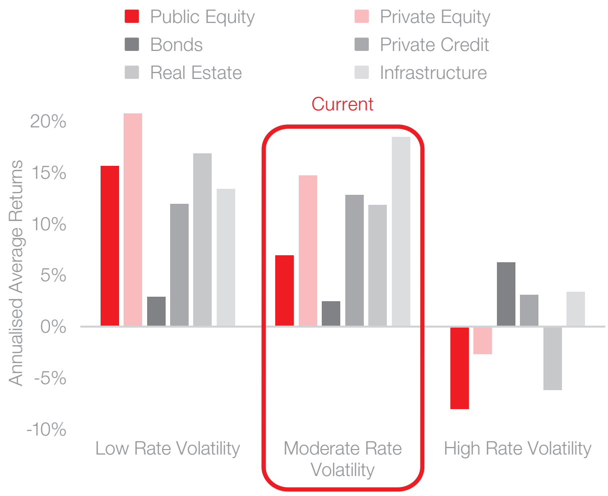


Source: Pitchbook, Bloomberg, DBS

Private assets have consistently provided strong hedging benefits across macroeconomic cycles. Our analyses reveal value and income generators in private markets historically outperformed public counterparts under high-rate regimes. However, rate volatility above 75th percentile can disrupt this dynamic, causing income generators to underperform bonds. Barring sudden quantitative re-tightening, or two standard deviation spikes in Treasury yields, the current high-rate moderate-volatility regime should remain constructive for outperformance.

Private assets outperform public assets under high-rate regime, though rate volatility remains a key risk

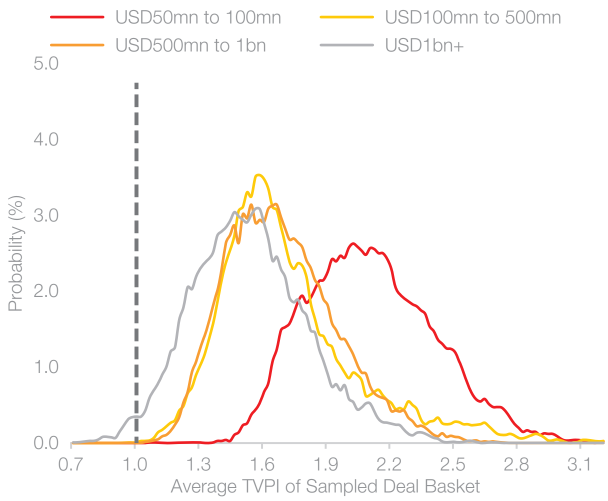




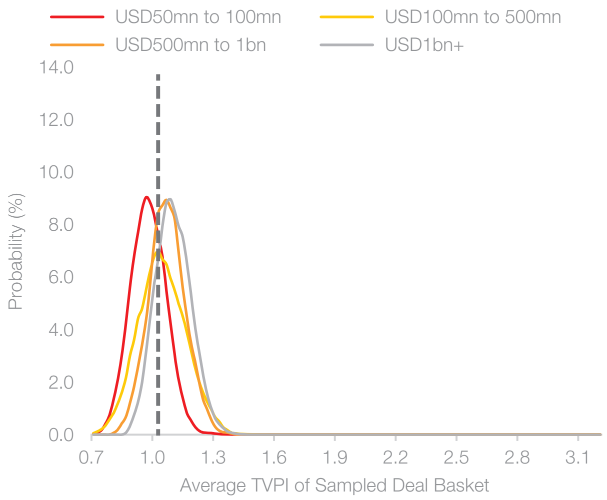
Source: Pitchbook, Bloomberg, DBS

Value in focus. Starting at an earlier stage of the growth cycle and displaying lower purchase multiples, mid-market companies offer greater headroom for value expansion and requires lower leverage. Consequently, mid-market deals are less susceptible to rate stress. A 2024 DealEdge report reveals revenue and profit margin growth drove c.60% of value creation in mid-market deals, compared to 47% for large-cap deals. The focus on profitability, rather than leverage-driven multiples expansion, supports strong mid-market performance under high-rate environments. However, not all mid-market segments offer the same risk-reward, and success depends on manager selection. Empirically, the USD50mn-100mn segment exhibited the greatest probability of upside. Under bottom-quartile managers, this segment displayed the highest likelihood of loss-making (>50%). Finally, the 2022 dip in valuation multiples bottomed out following the Fed's late-2024 rate cuts. With easing set in motion, valuation multiples should see steady uplifts. Recent rate pauses might temporarily suppress multiples, extending the window to capitalise on low entry multiples. Importantly, private equity remains undervalued against public counterparts with a decade-high valuation gap of 3.6x.

Mid-market funds excel under top-quartile managers…

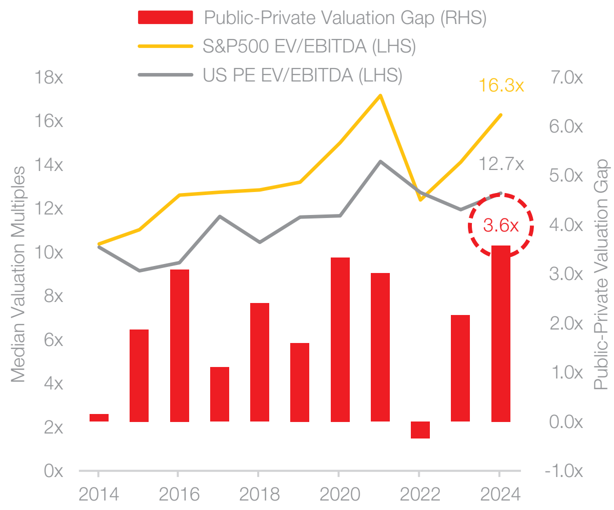


…but see significant downsides under bottom-quartile managers



Source: Pitchbook, DBS

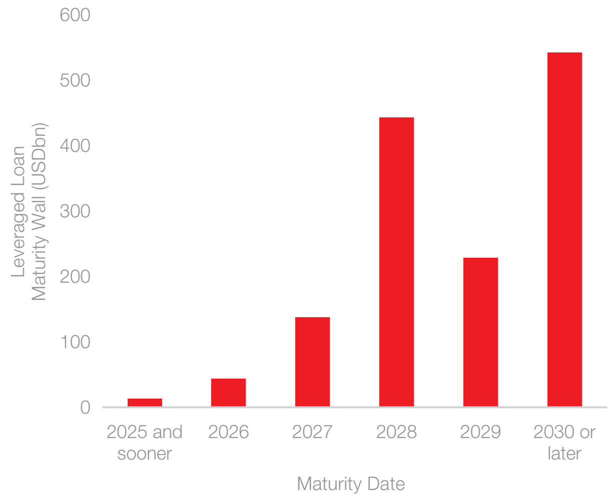
Private equity valuations are at their most attractive relative to public equity in a decade



Source: Pitchbook, DBS

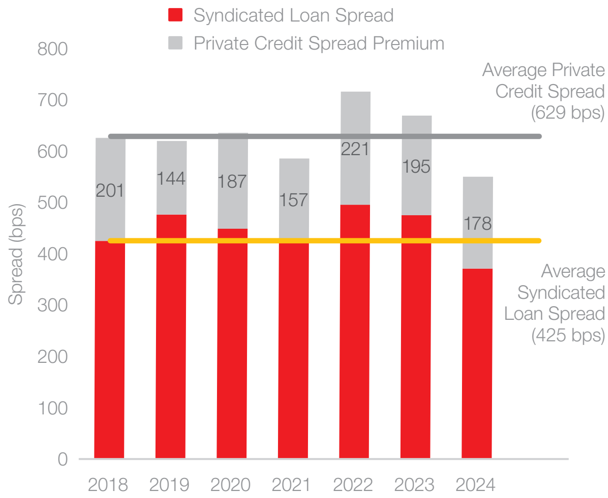
Broadening opportunities. A fundamental shift ensued post-pandemic, with private credit now financing c.61% of private market demands, and bank lending retreating to c.39%. This is driven by borrower demands for flexible financing solutions beyond what banks and public credit markets can offer. The Basel III endgame implementation in 2H25 will intensify this rotation as banks face stricter capital requirements. Meanwhile, c.USD500bn in bank loans will mature in 2028, creating a sizeable refinancing market for private credit to absorb.

Looming maturity wall in syndicated loans could lead to refinancing opportunities in private credit



Source: Pitchbook, DBS

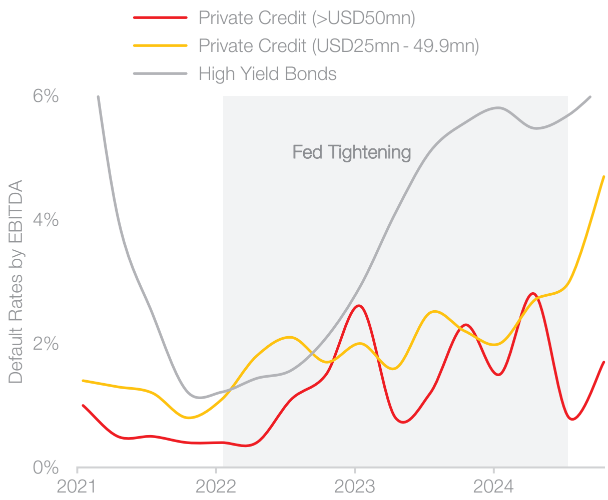
Across rate cycles, private credit exhibits steady premium over syndicated loans



Source: Pitchbook, DBS

In addition to these tailwinds, under the current high-rate regime, private credit's floating rate structure will keep yields high above pre-pandemic levels (current: 10.4%). Importantly, its spread premium has remained consistently above public counterparts (c.204 bps), buffering against rate volatility. As alluded before, barring two standard deviation rate volatility spikes, drawdowns are unlikely, and outperformance should continue. In corroboration with this are default rates which have remained below that of high-yield bonds. Noteworthily, larger borrowers show less defaults than smaller borrowers, making larger deals more appealing.

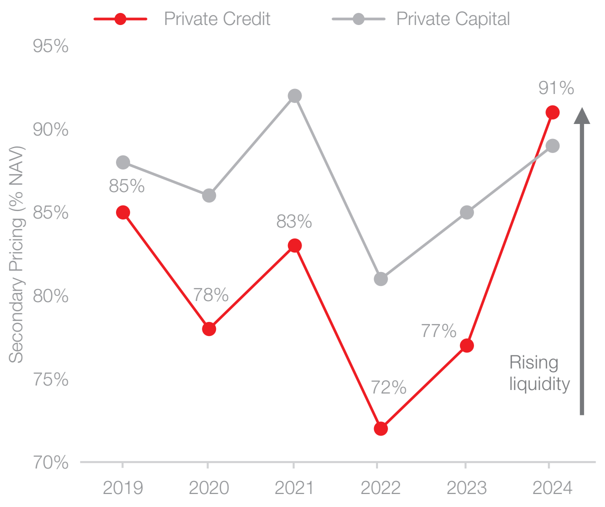
Private credit displayed low default rates despite rate stress, aided by low leverage ratios amongst borrowers



Source: Proskauer, Moody's, DBS

Private credit secondaries are pricing at a record 91% of NAV, up from 77% last year, reflecting improved liquidity. This, supported by primary market tailwinds, presents an opportunity for investors to rebalance and capture excess returns from other higher yielding (but less liquid) strategies. However, investors should be mindful of diversification costs and only rebalance strategically.

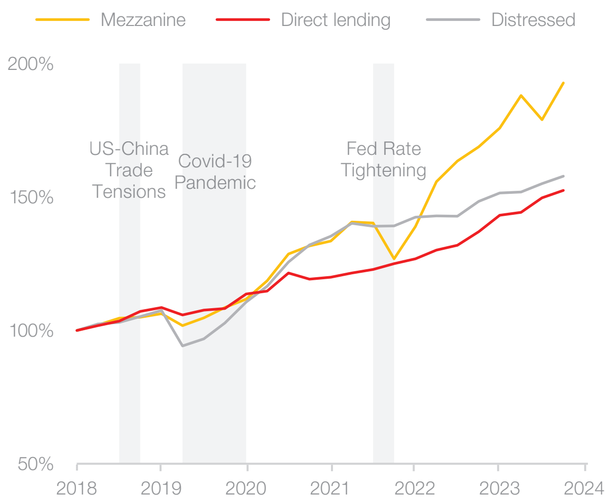
Private credit secondaries surged on the back of retail semiliquid demand



Source: Jefferies, DBS

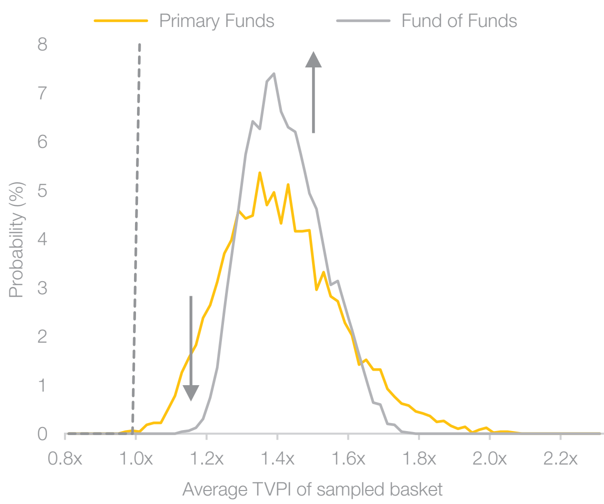
Vehicle selection. Empirically, fund-of-funds displays attenuated downside and greater upside over primary funds. Apart from improved performance, fund-of-funds offer convenience and economies of scale for investors who would otherwise have to source and commit multiple tranches to separate primary funds. Finally, fund-of-funds can be flexibly structured around open-ended vehicles such as

Strategy diversification can help investors capture excess returns



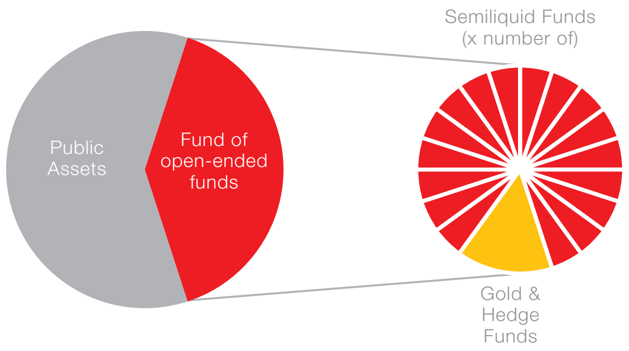
Source: Pitchbook, DBS

Fund-of-funds improves the probability of higher returns



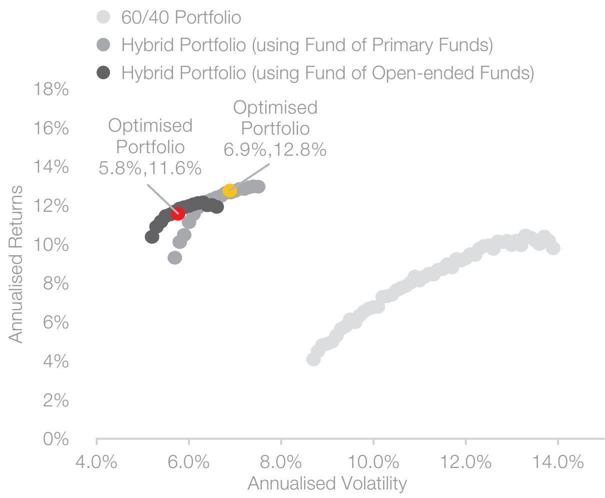
Source: Pitchbook, DBS

Gaining private asset exposure in a hybrid portfolio using a *fund of open-ended funds* model



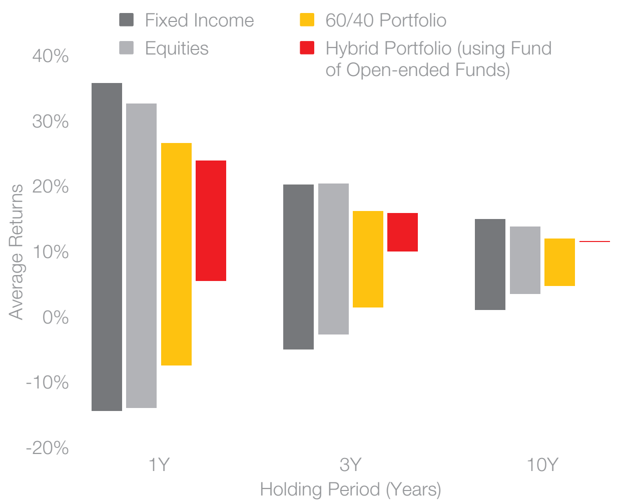
Source: DBS

Hybrid portfolios via the *fund of open-ended funds* approach exhibit the most optimal risk-adjusted returns



Source: Pitchbook, Bloomberg, DBS

Hybrid portfolios offer superior diversification benefits over a 10-year horizon



Source: Pitchbook, Bloomberg, DBS

semiliquids and hedge funds for liquidity and risk management – a trend we believe will gain significant traction. Our analyses show the deployment of a hypothetical fund of open-ended funds in a hybrid portfolio confers immense diversification benefits, helping the portfolio outperform both a pure equity play and 60/40 portfolio over a 10-year horizon, and significantly improving its Sharpe ratio.

Blending liquidity with opportunity. Beyond downside protection, diversification strategies need to offer investors a higher premium for staying invested, while considering their liquidity needs. Although private assets offer high illiquidity premia, the lack of illiquidity management presents an entry obstacle for individual investors. Adopting a balanced mix of private and public assets in a portfolio, and using open-ended vehicles, can help individual investors better capitalise the coming private market surge.

Source: Unsplash

Opportunities Amid Uncertainty

Thematic Strategy 2Q25

Against a positive policy backdrop under Trump 2.0, US production of oil & gas is expected to increase gradually. Long-term beneficiaries of this heightened level oil & gas activity include oil majors, shale plays, and oilfield services.

12. Energy.

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Strategist

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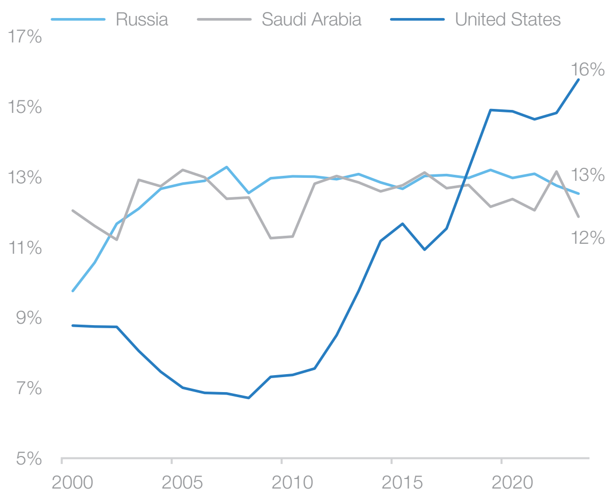
Analyst

Elizabelle Pang
Analyst

US energy dominance a key focus. Energy has been a key pillar underpinning Trump's belligerent moves since he has come back to power in the US. Many of his moves have been aimed at ensuring American dominance in the global energy space, most recently being the establishment of a National Energy Dominance Council to oversee the new administration's pursuit to unleash American energy. As a vocal opponent of platforms like the Paris Agreement to fight climate change, which he perceives to create a competitive disadvantage for the US, Trump withdrew from the pact for a second time in 2025 and has instead signed off on a "national energy emergency" which will purportedly allow the administration to fast-track energy projects in the US. Most of these will be fossil-fuel based projects like gas-fired power plants, pipelines, and other infrastructure. This should come as no surprise given his oft repeated campaign war cry of "drill, baby, drill", promising to remove any regulations which hinder the growth of the US energy industry. Priority will be on lowering the cost of energy to domestic consumers rather than emissions reductions, and we should see renewed focus on oil and gas in the near term.

Oilfield services a potential beneficiary of Trump 2.0. Of course, we do not think that the "drill" part will be taken literally by industry participants. US shale oil production does not really depend on politics as much as market factors, and production has already increased sharply under the Biden administration. Under the new Trump administration, US oil production will have more room to increase with roll back of any restrictive regulations. However, major

Proportion of US oil production to global volume has grown

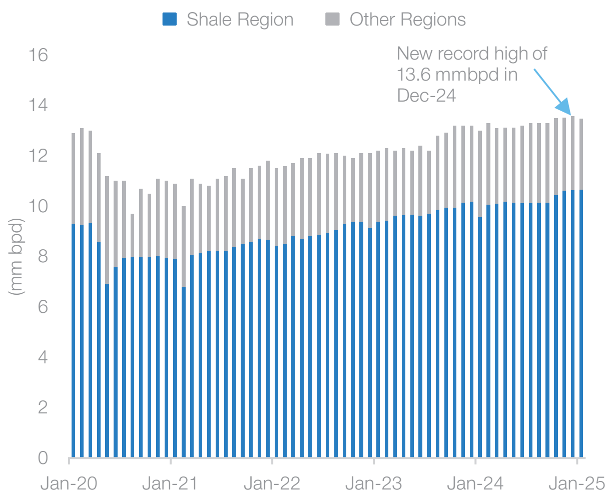


Source: EIA, DBS

production gains are unlikely as oil producers will respond to market conditions rather than policies. As such, we think that US oilfield services players could be among the key beneficiaries of higher oil and gas activities in the US.

LNG and nuclear power set to receive a boost. The natural gas sector will also be among the biggest beneficiaries of Trump's policies, which could herald a golden age for US liquefied natural gas (LNG) dominance. We have already seen reversals of the LNG export permitting pause under the new administration and we could see a revival of LNG export terminal projects. The US' plans for energy dominance will include efforts to launch a nuclear power renaissance in the US, with more funding

US oil production hovering near all-time high levels

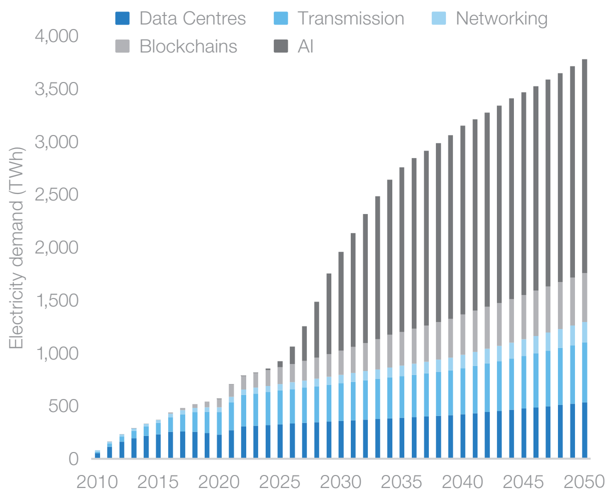


Source: Bloomberg, DBS

available for developing next generation nuclear technology. Natural gas and nuclear energy look best poised to reliably supply the energy requirements of the AI-fuelled data centre boom.

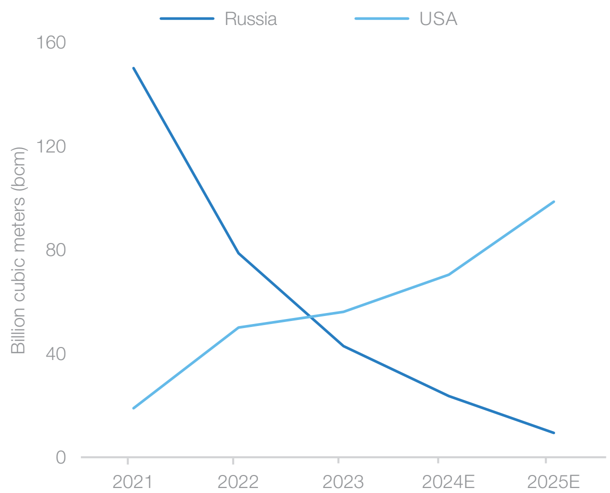
Opportunities amid volatility. Elsewhere, Trump's tariff wars and geopolitical parlays ensure that volatility will be the name of the game as far as energy plays are concerned. Tariffs on Canadian and Mexican energy flows and Chinese solar plans all complicate the pitch for US domestic energy prices, whereas global efforts to defuse the war between Russia and Ukraine could result in lower geopolitical risk premium in oil and gas prices. Meanwhile, stricter sanctions on Iran could provide for tighter demand-supply dynamics in the oil market. Suffice to say, we

AI to drive increasing electricity demand in the US



Source: Energy and AI: the power and the glory, ThunderSaid Energy, Apr 2024. Data from Jun 2024 onwards is forecasted.

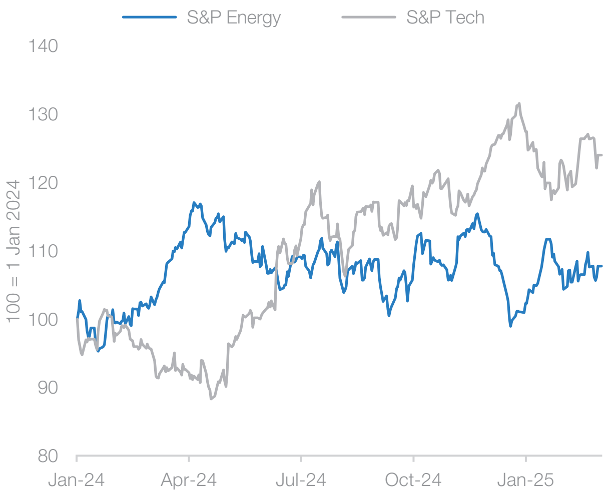
EU natural gas imports



Source: European Commission, IEEFA, Wellington Management. 2024-2025 figures are estimates.

are set for interesting times for the energy market in the near term, and market volatility will continue to offer opportunities to invest in the energy sector, and particularly the oil and gas sector, to play on the robust long-term fundamentals.

Will energy stocks outperform tech again?



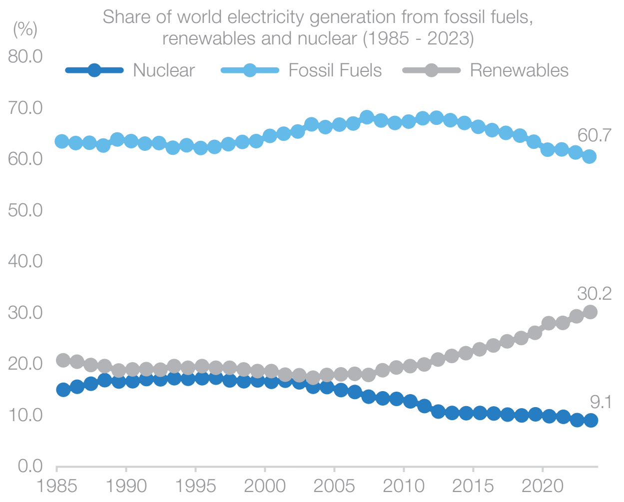
Source: Bloomberg, DBS

The structural case for oil and gas remains strong

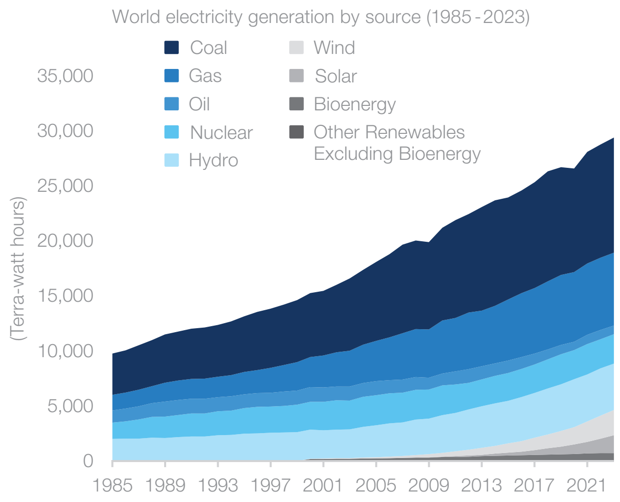
Fossil fuels continue to dominate electricity generation. Despite the aggressive roll-out of renewable energy sources across major world economies, electricity generation continues to be dominated by fossil fuels. As of 2023, c.60% of global electricity generation was produced using fossil fuels, while renewables and nuclear power made up the remaining 30% and 10% respectively. The reasons for the continued prevalence of fossil fuels in electricity generation are largely structural and are expected to persist for some time to come. Coal's share of power generation in Asia remains at c.56% as at 2023, led by China (59%) and India (>70%). This figure is expected to stay high due to the presence of new coal plants that cannot be retired in the short-term. At the same time, natural gas, while emitting c.50% less CO2 emissions than coal when used for power generation, is still a fossil fuel and will ultimately delay the switch to renewables. Additionally, there are currently still plenty of challenges in the adoption of renewables that have yet to be overcome. The complete overhaul in grid infrastructure needed, the relatively lower power densities as well as intermittency in power generation (diurnal and annual for solar, and weather-dependent for wind) and the lack of feasible energy storage options, are compelling reasons that will continue to perpetuate the relevance of fossil fuels in electricity generation globally as a baseload fuel option.

Crude oil will continue to see demand from transport. Electrifying transport has emerged as one of the most promising ways to meet global emissions targets and facilitate the energy transition. However, progress has been slow, even for specific areas of land transport such as motorcycles and cars, which have been shown to be the most promising options for one-to-one EV swaps. Globally, the share of EVs remains insignificant (3.2% as at 2023). Among major economies, China leads the way with 7.6% EV penetration. In terms of new cars sold, trends are more encouraging, but internal combustion engine (ICE) vehicles still make up the majority of sales globally, with EVs comprising just 18% of new cars sold in 2023. With trade barriers acting as a further drag on EV adoption under Trump 2.0, ICE and hybrids are likely to continue to dominate road transport. For aviation and maritime transport modes, electrification has made even less progress and continue to be overwhelmingly dependent on fossil fuels. Accordingly, the demand for crude should remain resilient in the short to medium term, only peaking around 10 to 15 years from now.

Fossil fuels still make up >60% of global electricity generation

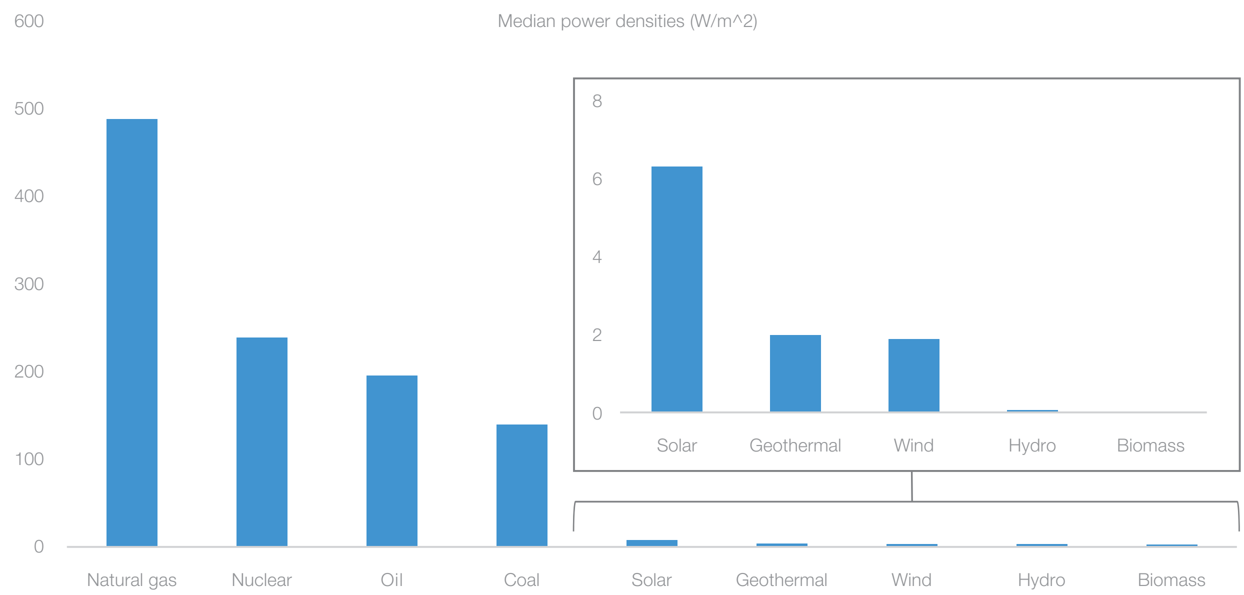


Source: Our World in Data, DBS



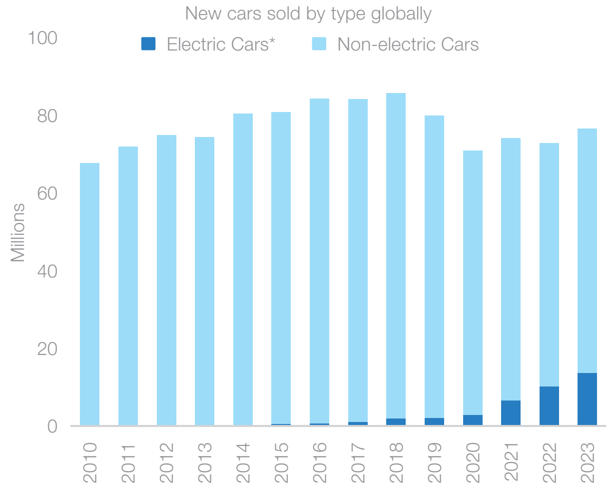
Source: Our World in Data, DBS

Fossil fuels have higher power densities than renewables



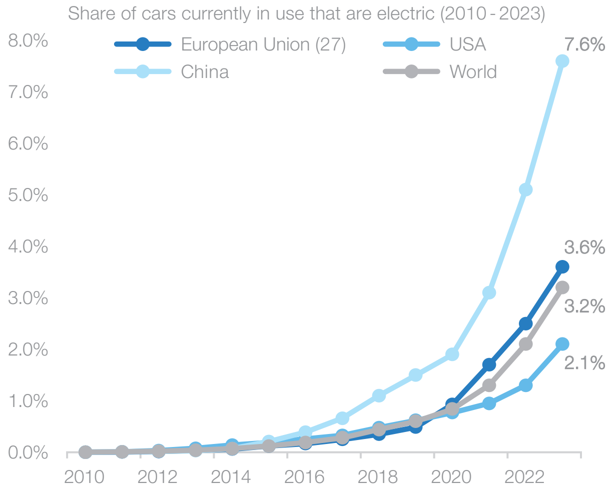
Source: Adapted from Zak and Behrens 2018

ICE vehicles still make up majority of new car sales globally



*Includes battery electric vehicles and plug-in hybrids
Source: Our World in Data, DBS

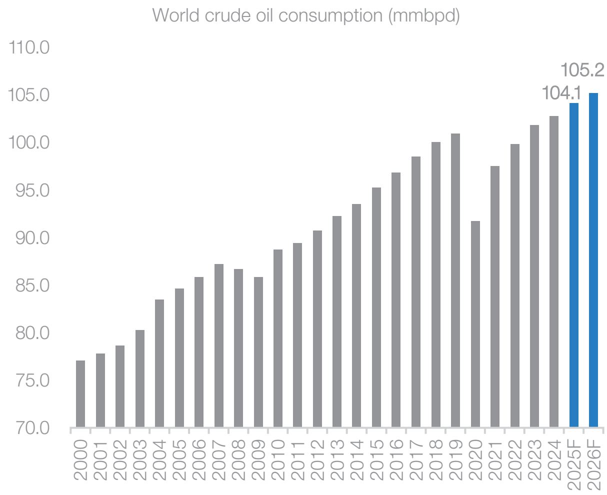
Only 3% of cars in use globally are EVs



Source: Our World in Data, DBS

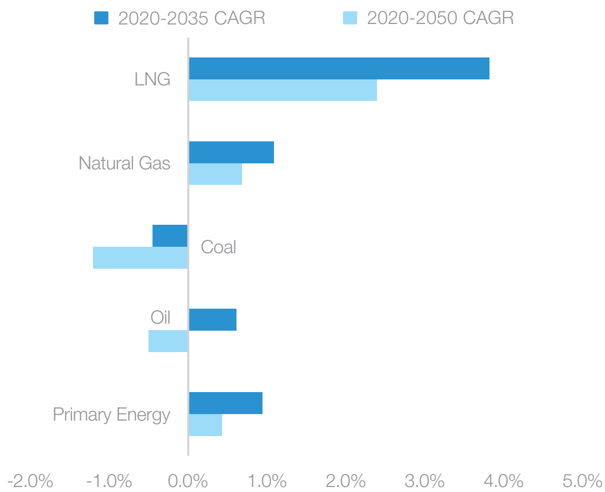
Gradual trajectory of energy transition bodes well for natural gas. Natural gas is the cleanest fossil fuel in terms of CO2 emissions and is expected to have the most resilient demand; it can substitute coal usage in power and heating without substantial restructuring of infrastructure. This makes natural gas an ideal "bridge" fuel between traditional and fully green sources of energy. The outlook for natural gas will largely be determined by two opposing trends: rising demand in emerging economies as they capitalise on the "bridge" status of natural gas to rapidly grow and industrialise, counterbalanced to an extent by the eventual structural shift towards a greater proportion of renewables. The net effect of these two trends will depend on the speed of the energy transition, but as things stand, natural gas is expected to retain its positive demand growth momentum well into the long-term, even as coal and oil peak out earlier sometime in the 2030s and 2040s respectively. For example, LNG will boost natural gas' relevance in the emerging markets of South and Southeast Asia.

Oil demand to remain resilient in the short to medium term



Source: EIA, Bloomberg, DBS

Gas demand set to retain growth under current trajectory

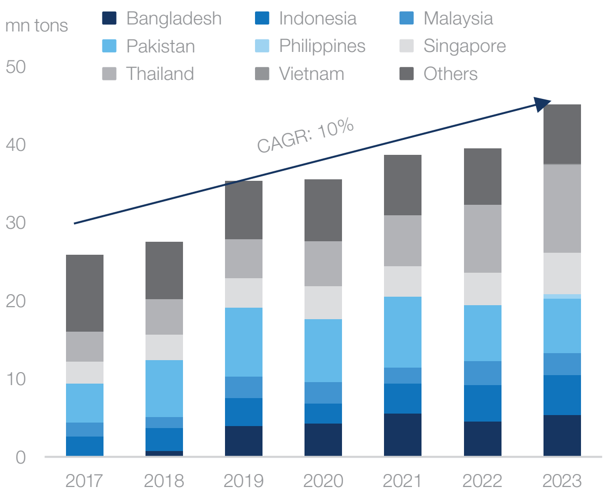


Source: BP, DBS

<u>Playing the long-term fundamentals of the oil and gas sector</u>

Oil majors – Energy security is back in vogue. With the structural case for fossil fuels remaining strong and a sharp resurgence in energy security under Trump 2.0, it appears the stars are aligning for the global oil majors. For US majors, inorganic growth from acquisitions (shale or otherwise) appears to be the latest catalyst while all eyes are on European majors with their strategy reset and return to being more hydrocarbons-focused to drive profitability. To be clear, the recent push-back on lower carbon investments does not mean that oil majors have abandoned all plans for net zero or the clean energy transition. What it does mean is that the capital allocation to low carbon initiatives will be more selective and that return on capital barriers have been raised. This rationalisation of low carbon spending and the resumption of a pragmatic approach towards capex (rather than a policy driven one) should be a welcomed change for both investors and the oil majors themselves.

Asia LNG demand trends: Southeast Asia the new frontier for LNG demand



Source: Bloomberg, DBS

US shale M&A picks up pace, changes competitive landscape

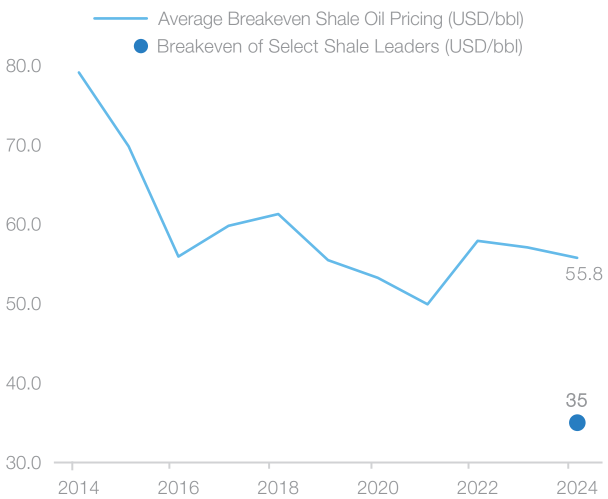
Target	Acquirer	Deal value (USDbn)	Date announced
Pioneer Natural Resources	Exxon Mobil	64.5	Oct 2023
Hess	Chevron	60	Oct 2023
Endeavour	Diamondback	26	Feb 2024
CrownRock	Occidental Petroleum	12	Dec 2023
Earthstone Energy	Permian Resources	4.5	Aug 2023
Black Swan Oil & Gas, PetroLegacy Energy, and Piedra Resources	Ovintiv	4.3	Apr 2023

Source: GlobalData, Companies, DBS

Shifting sands in US shale oil as consolidation gathers pace. Another notable area in the fossil fuels space is the growing dominance of shale oil. With a flurry of announced M&A transactions and possibly more in the pipeline, the face of the US shale oil industry is being fundamentally transformed. The era of drilling and growing at all costs is slowly giving way to a more measured development phase. With private operators being acquired by supermajors, there will be an increased focus on profitability as opposed to a mindless pursuit of production volume. Industry consolidation should also help the combined entities achieve greater economies of scale, thereby lowering production costs and further boosting profitability.

Fossil fuels are here to stay for the foreseeable future. The world's energy needs, whether it is heating, transport, or electricity generation is still very much reliant on fossil fuels. Given the structural nature of the challenges faced by renewable energy sources (intermittency, storage, power density, etc.), we believe that the energy transition will likely be a bumpy one with non-linear progress. Coupled with a renewed drive for energy security and a collective push-back on ESG under Trump 2.0, the case for fossil fuels looks stronger than ever. Amid the volatility of Trump's tariffs and the emergence of DeepSeek, the latter of which has roiled Big Tech stocks and equity markets, energy, and especially fossil fuels, remains a relatively safe space. We expect limited downside for oil at USD70/bbl whereas upside could come from factors like better Chinese demand numbers as well as the continued deferment and moderation of OPEC+ supply. Oil majors, shale plays, and oilfield services should see upside from heightened oil and gas activity and production volume growth against such a backdrop.

Future of US shale driven by falling break-even pricing



Source: Bloomberg, Wood Mackenzie, DBS

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Glossary.

Acronym	Definition
AI	artificial intelligence
ASEAN	Association of Southeast Asian Nations
ASP	average selling price
AT1	additional tier 1
AUM	Assets under management
AxJ	Asia ex-Japan
bbl	barrel
BCOM	Bloomberg Commodity Index
BEV	battery electric vehicles
BNM	Bank Negara Malaysia
BOJ	Bank of Japan
BOK	Bank of Korea
BOT	Bank of Thailand
BSP	Bangko Sentral Ng Pilipinas
bpd	barrels per day
bps	basis points
CAA	CIO Asset Allocation
CAGR	compound annual growth rate
CDU/CSU	Christian Democratic Union (Germany)/ Christian Social Union (Bavaria)
CET1	Common Equity Tier 1
CGB	China Government Bonds
COMEX	The Commodity Exchange
CPI	consumer price index
DM	Developed Markets
dma	day moving average
DOGE	Department of Government Efficiency (United States)
DPU	distribution per unit
DRAM	dynamic random access memory
DXY	US Dollar Index
EBIT	earnings before interest and taxes
EBITDA	earnings before interest, tax, depreciation, and amortisation
EC	European Commission
ECB	European Central Bank

Acronym	Definition
EGB	European Government Bonds
EIA	Energy Information Administration
EM	Emerging Markets
eop	end of period
EPFR	Emerging Portfolio Fund Research
EPS	earnings per share
ESG	Environmental, Social, and Governance
ETF	exchange-traded fund
EU	European Union
EV	electric vehicle
FOMC	Federal Open Market Committee
FRED	Federal Reserve Economic Data
FX	foreign exchange
G3	Group of Three
G10	Group of Ten
G20	Group of 20
GDP	gross domestic product
GILTI	Global Intangible Low Taxed Income
GPT	Generative Pre-trained Transformer
HIBOR	Hong Kong Interbank Offered Rate
HY	high yield
ICE	Intercontinental Exchange
IndoGB	Indonesian Government Bonds
IG	investment grade
IGB	India Government Bonds
ISM	Institute for Supply Management
IT	Information Technology
JGB	Japanese Government Bond
KLIBOR	Kuala Lumpur Interbank Offered Rate
KORUS FTA	United States-Korea Free Trade Agreement
KTB	Korea Treasury Bonds
LBMA	London Bullion Market Association
LGFV	local government financing vehicle

Acronym	Definition
LLM	large language model
LME	London Metal Exchange
LPR	loan prime rate
LVMH	Moët Hennessy Louis Vuitton
M&A	mergers and acquisitions
MAS	Monetary Authority of Singapore
MFN	Most Favoured Nation
MGS	Malaysia Government Securities
MIBOR	Mumbai Interbank Outright Rate
mmbpd	million barrels per day
mmt	million metric tons
MSCI	Morgan Stanley Capital International
NAV	Net Asset Value
NATO	North Atlantic Treaty Organisation
NBFC	Non-Banking Financial Company
NEER	nominal effective exchange rate
NIM	net interest margin
NYSE	New York Stock Exchange
O/N	overnight
OAS	Option-Adjusted Spread
OIS	overnight indexed swap
OMO	Open Market Operations
OPEC+	Organisation of the Petroleum Exporting Countries
OPM	operating profit margin
P/B	price-to-book
P/E	price-to-earnings
PBOC	People's Bank of China
PCE	personal consumption expenditure
PE	Private Equity
PER	price-to-earnings ratio
PMI	purchasing managers' index
PPI	producer price index
R&D	research and development

Acronym	Definition
RBA	Reserve Bank of Australia
RBI	Reserve Bank of India
REIT	real estate investment trust
ROA	return on asset
ROE	return on equity
RRR	required rate of return
SAA	Strategic Asset Allocation
SD	standard deviation
SEA	Southeast Asia
SET	Stock Exchange of Thailand
SGDNEER	Singapore Dollar Nominal Effective Exchange Rate
SNB	Swiss National Bank
SOE	state owned enterprise
SOFR	Secured Overnight Financing Rate
SORA	Singapore Overnight Rate Average
SPD	Social Democratic Party of Germany
SRBI	Bank Indonesia Rupiah Securities
T-bills	Treasury bills
TAA	Tactical Asset Allocation
TCJA	Tax Cuts and Jobs Act (United States)
TOPIX	Tokyo Stock Price Index
TP	target price
TPI	tax and price index
TSE	Tokyo Stock Exchange
TSMC	Taiwan Semiconductor Manufacturing Company
UCITS	Undertakings for Collective Investment in Transferable Securities
UST	US Treasury
VAT	value-added tax
VIX	Chicago Board Options Exchange's Volatility Index
WTI	West Texas Intermediate
YCC	Yield control curve
YTD	year-to-date
YTW	yields-to-worst

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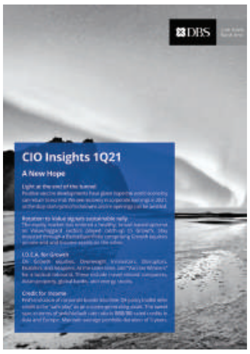

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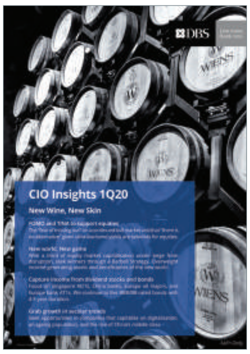

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