REGIONAL MARKETS UPDATE

US MARKET (2.0 STARS – UNATTRACTIVE)

- ISM Manufacturing PMI came in at 58.8 in Aug 17, down from 56.3 in Jul 17
- ISM Non-Manufacturing came in at 55.3 in Aug 17, up from 53.9 in Jul 17
- Nonfarm payrolls rose by 156,000 in Aug 17, after a downward-revised 189,000 gain in Jul 17
- Private payrolls rose by 165,000 in Aug 17, after a downward-revised 202,000 increase in Jul 17
- Unemployment rate at 4.4% in Aug 17 from 4.3% in Jul 17
- Factory orders fell -3.3% m-o-m in Jul 17, after an upward-revised 3.2% gain in Jun 17
- Advance retail sales fell -0.2% m-o-m in Aug 17, after a downward-revised 0.3% m-o-m rise in Jul 17
- Excluding autos and gas, retail sales fell -0.1% m-o-m in Aug 17, after a 0.5% m-o-m rise in Jul 17
- Industrial production fell -0.9% m-o-m in Aug 17, after an upward-revised 0.4% m-o-m rise in Jul 17
- Leading index posted a 0.4% m-o-m increase in Aug 17, after a 0.3% increase in Jul 17
- Housing starts registered a 1.118 million annual rate in Aug 17, after an upward-revised 1.19 million annual rate in Jul 17
- Building permits registered a 1.3 million annual rate in Aug 17, after an upward-revised 1.23 million rate in Jul 17
- Existing home sales fell -1.7% m-o-m in Aug 17 to a 5.35 million annual rate, after a -1.3% m-o-m decrease in Jul 17
- Consumer confidence index at 119.8 in Sep 17, down from a downward-revised 120.4 reading in Aug 17
- Based on the S&P/Case-Shiller Composite 20, US home prices rose 5.81% y-o-y in Jul 17, after a 5.65% increase in Jun 17
- Fed Funds Rate: 1.00% – 1.25%

MARKET OUTLOOK

Earnings estimates of US companies (as represented by the S&P 500 Index) on aggregate saw little change over the month of September. 2017's estimated earnings were revised -0.1% lower, while 2018's estimated earnings were lowered -0.3% over the month (as of 25 September 2017). Year-to-date, 2017's estimated earnings were upgraded 0.3%, while 2018's and 2019's earnings estimates were revised -0.5% and -0.9% respectively. Breaking down by sectors, US information technology (IT) companies once again saw earnings upgrades, with 2017's earnings of the sector bumped up 1.1%. Financials saw slight earnings downgrades as a whole for both their 2017's and 2018's earnings, while the consumer staples sector saw broad-based earnings upgrades. This month round, the energy sector did not see downgrades to 2017's earnings estimates (2018's estimated earnings still saw downgrades), while the materials sector saw a -2.4% downgrade in 2017's earnings. Year-to-date, the IT sector enjoyed the most earnings upgrades, buoyed by secular digitisation trends and a cyclical upturn in the semiconductor industry.

With regards to recently-released economic data from the US, the ISM Manufacturing PMI came in at 58.8 in August, up from a prior 56.3 and beating consensus estimates of 56.5. Readings of new orders and new export orders fell, while employment and backlogs rose from the previous month. On the other hand, the services (ISM Non-Manufacturing) reading came in at 55.3 in August, rebounding from a prior 53.9 but falling short of the consensus forecast of a 55.6 reading. Readings of new orders, new export orders, and employment rose from the previous month. Both manufacturing and services in the US remain robust, which should continue to support growth momentum as global economic momentum continues to accelerate. In terms of employment numbers, August's nonfarm payrolls print came in at 156,000, down from July's downward-revised 189,000 and falling short of consensus estimates (180,000). Manufacturing payrolls continue to surprise on the upside, while construction rose the most since February. Wages, as represented by average hourly earnings, rose 0.1% month-on-month, down from a prior 0.3% gain (wages rose 2.5% year-on-year in August). The US labour remains robust, and we expect the pace of job creation to gradually moderate lower moving forward as the business cycle matures in the US.

In September's Federal Open Market Committee (FOMC) meeting, the Fed announced that it will begin to normalise its balance sheet amount in October – a move which was widely expected by markets given the thorough communication by Fed members throughout 3Q 17. The Fed will trim reinvestments in US Treasuries by USD 6 billion per month and in mortgage-backed securities (MBS) by USD 4 billion per month. No specifics were given as to when the normalisation process will end. Acknowledging that household spending "has been expanding at a moderate rate, and growth in business fixed investment has picked up in recent quarters", the Fed also added that they do not expect the adverse impacts of the recent hurricanes to derail growth momentum in the US. The US central bank also made no changes to the benchmark Fed Funds Rate, and the 'Dot Plot' forecast was almost unchanged, indicating that policy-makers are expected to hike the benchmark rate one more time in December and by another three times in 2018. Consequently, markets have also repriced the odds of a rate hike by the year's end (from a 53.2% probability to a 63.8% chance). We reiterate that the Fed is taking a gradual approach in normalising policy, and that guidance is still data-dependent, giving them leeway to respond depending on how economic conditions change moving forward.

Over the month of September, the S&P 500 index made new highs and punched above the 2500 level, rising 1.2% (as of 25 September 2017). Some of the top performing stocks include energy-related players such as the likes of Helmerich &Payne, Andarko Petroleum, Chesapeake Energy, Marathon Oil and Halliburton, while Allergan, Regeneron Pharmaceuticals, Mattel and Carnival Corp were some of the bottom performers over the month. Consequently, the US equity market trades at 19.2X, 17.3X and 15.7X 2017's, 2018's and 2019's estimated earnings, at premium to its fair PE ratio of 15.0X. **The potential upside of the US market is now the lowest among the markets that we cover, and as such, we maintain our rating of 2.0 Stars "Unattractive" for the US.** Despite our view on the equity market, we are not pessimistic on economic prospects, as the US economy remains robust and leading indicators continue to point to growth at this juncture. Additionally, while lower than before, expectations remain for Trump's administration to deliver fiscal expansion (either in the form of corporate tax cuts or infrastructure spending), which if implemented successfully, could provide strength to domestic growth in the US. However, there is still an element of uncertainty regarding the new administration's attitude and possible policies regarding trade relations with emerging markets like Mexico and in Asia.

REGIONAL STAR RATINGS

US (2.5 Stars – Neutral)

Why we like it

1. Economic Fundamentals Robust, Lending Support To Corporate Earnings Growth
    - Economic momentum remains robust, manufacturing has picked up since 3Q 16 while consumption is expected to be the key driver for GDP, supported by a robust labour market and still relatively subdued energy costs
    - In an environment of positive economic growth, earnings are forecasted by consensus to grow by a 12.8% annualised rate by end-2019 (as of 25 Sept 2017)

2. Strong Brands, Global Reach And Importance
    - Many US companies possess strong branding power; 9 out of the 10 most valuable brands of the world are US companies (according to Forbes' 2016 study)
    - A large proportion of the largest US companies derive significant proportions of revenue from overseas, allowing such companies to benefit from global growth rather than being fully dependent on the domestic economy
    - Leading US companies still remain global leaders in various fields like technology (Apple, Google, IBM), finance (JP Morgan, Citigroup), energy (Exxon Mobil, Chevron), consumer-orientated (P&G, Coca Cola, Amazon, Walt Disney) and even healthcare (Johnson & Johnson, CVS Health)

3. Domestic Growth Drivers And Trends
    - Other than a normalisation of the residential housing market, unparalleled access to cheaper energy prices – via the shale energy revolution – should provide a competitive advantage for US manufacturing and companies
    - The Trump administration is expected to roll some form of a fiscal stimulus package (either via corporate tax cuts or infrastructure spending) which will lend support to domestic growth
    - The US remains a key player in the global innovation scene, leading the way in digitisation

What we don't like

1. Valuations Remain Elevated, Resulting In Lower Potential Returns
    - On several valuation metrics, valuations of the US equity market remain relatively stretched at this current juncture. The forecasted annualised return of US equities by end-2019 is the lowest among the markets we cover

2. Earnings Growth Vulnerable To A Contraction Of Corporate Profit Margins
    - Profit margins of US companies remain high relative to historical averages (approximately 6.0%), may contract if labour costs increase and the Fed continues on its monetary tightening stance as the US economy enters the later stages of the business cycle
    - Earnings growth prospects will be affected if margins decline and sales growth do not increase

3. Selected Areas Of "Excesses" And "Frothiness"
    - Signs of over-optimism have manifested in selected areas of the market – the recent IPOs of new technology companies with no profits calls to mind the more "bubbly" period of the stock market in the late 1990s
    - Relatively-stretched valuations in some areas in small caps, certain technology sub-sectors and the defensive sectors (healthcare, utilities) are also areas of concern