
Investors will be roused into action by the crow of several investment opportunities

10 investment eggs to hatch in 2017

Don't be caught sleeping this Year of the Rooster and start sitting on these golden investment eggs; but as with any investment idea, these eggs are best taken with a grain of salt.

With global growth set to accelerate in 2017 and the new United States administration looking to embark on an infrastructure binge, investors will be roused into action by the crow of several investment opportunities. *Singapore Business Review* rounded up the most promising of the bunch based on investor outlooks, including key sectors like biotechnology that promise solid earnings potential and currency plays that anticipate a stronger US dollar.

1. Healthcare and technology stocks

For stock market investors, the healthcare and technology sectors are promising bets in 2017. Most indices climbed higher following the outcome of the US elections, and there is limited potential for indices in aggregate to appreciate further, says **Christian Nolting,** global chief investment officer at Deutsche Bank Wealth Management. This presents an opportunity to concentrate on income strategies and sector themes.

"The earnings outlook remains positive ahead," he says, noting that Deutsche Bank has upgraded the global healthcare sectors to overweight. "As expected, S&P 500 quarterly earnings are now growing again for the first time on a year-on-year basis since the third quarter of 2015, and the outlook remains positive – although we still believe consensus estimates for 2017 may be too high."

Don't be tempted to change your asset allocation if your investment goal or risk tolerance has not changed.

Investors should start loading their baskets with biotechnology stocks, says Nolting. The fundamentals of this subsector remain intact as research and development spending continues to grow. Healthy cash positions and positive earnings will also support biotechnology stocks.

Technology stocks can also be great picks in the face of stronger global growth and fiscal spending into infrastructure, which should drive demand, earnings, and stock prices across the sector.

2. US infrastructure sector

US infrastructure will be another hot sector in 2017 due to a renewed focus to boost infrastructure spending as outlined in the proposals of president-elect Donald Trump. "We are going to fix our inner cities and rebuild our highways, bridges, tunnels, airports, schools, hospitals," said Trump in his acceptance speech. "We're going to rebuild our infrastructure – which will become, by the way, second to none. And we will put millions of our people to work as we rebuild it," he remarked. Nolting reckons the US needs an estimated infrastructure spending of US$3.6t until 2020, and the markets will be rallying behind this growth story.

"Markets are starved for growth," says **Charles Himmelberg**, head of global credit strategy at Goldman Sachs. "This is plainly visible in the eagerness with which markets seized on Trump's growth-focussed message." He adds, "It is also our sense that Trump does intend to prioritise an aggressively pro-growth fiscal agenda of tax cuts, deregulation, infrastructure spending, and defense spending."

Goldman Sachs sees the US fiscal stimulus as a welcome growth and reflationary impulse, especially in a weak global growth environment where the scope for lowering real policy rates remains constrained by low inflation and the zero lower bound on nominal rates.

3. Navigate higher yields

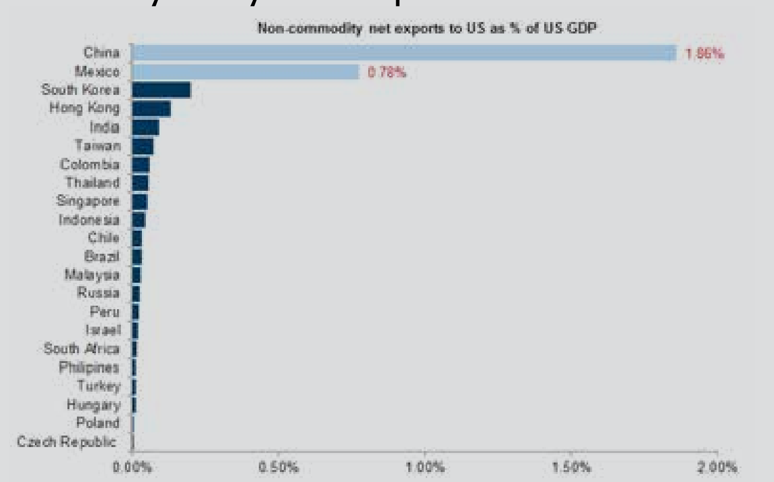
Whilst higher US interest rates and a lack of alternatives should support global demand for US Treasuries, expectations of higher growth and higher inflation rates may create an upwards pressure on yields, says Nolting. Global growth forecasts seem rosier for 2017. Nolting expects global growth to accelerate to 3.5% in 2017 from 3.1% in 2016. He foresees US growth to pick up to 2.2% in 2017 from 1.5% in 2016, which will likely support labour market strength.

In contrast, Eurozone growth is expected to slow to 1.3% in 2017 from an estimated 1.6% in 2016. Nolting reckons Eurozone yields will also rise, but will likely be lower than US yields, with the former being pushed up by gradually increasing inflation, some priced-in political risks not materialising, and expectations of European Central Bank (ECB) tapering.

The slower rise in Eurozone yields assumes that the ECB will continue to buy for the time being. The two regions also have differing inflation outlooks with Eurozone headline inflation expected at 0.2% yoy for 2016 and 1.4% for 2017, whilst the US inflation is expected at 1.4% in 2016 and 1.9% in 2017.

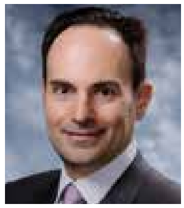
Given the potential of higher inflation and rising bond yields, investors should adjust their fixed income portfolios, says **Zal Devitre**, head of investments at Citibank Singapore. "Bond investors should consider shortening the duration of their holdings and should

Trade relations with China (and to a lesser degree Mexico) will receive heavy scrutiny under Trump

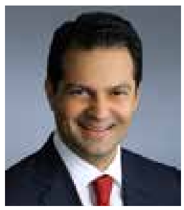


Sources: UNCTAD, Goldman Sachs Global Investment Research

Christian Nolting



James Martielli



Zal Devitre

Roger Crook

avoid developed market government bonds. Inflation-linked investments, including Treasury Inflation Protected Securities, are likely to outperform in this environment," he says.

Devitre projects the 10-year US Treasury yield to reach 2.25% by end 2016 and 2.6% by end 2017, as the Fed tightens monetary policy amidst rising inflationary pressure. "Donald Trump's victory in the US Presidential election has triggered an inflection across multiple asset classes, from equities to fixed income, currencies to rates. Given presidential-elect Trump's commitment to tax cuts and a large infrastructure spending program, we expect interest rates to continue to rise in 2017, driving the US dollar (US$) higher," he says.

4. Buy US$ over EUR and JPY

The US$ is gathering strength and will continue to rise against both the euro (EUR) and Japanese yen (JPY) in 2017 as the US domestic growth accelerates, opening a chance for US$ investors. "We see further US$ strengthening. We expect the US$ to reach parity against EUR by end 2017 and US$-JPY 115," says Nolting. "This is in part due to monetary policy divergence."

The US$ has been rising against the EUR since Trump won the US elections, and many analysts say the two currencies could be trading one-for-one in 2017. Nolting reckons the Fed is expected to move "low and slow" with a maximum of three hikes (25bps each) by the end of 2017 to achieve inflation target and "full" employment.

Meanwhile, the ECB is anticipated to extend quantitative easing until September 2017, and to announce gradual tapering around mid-2017. Nolting reckons US growth will continue to outstrip European growth.

In Japan, the next 12 months will likely see 10bps cut in the policy rate and a further increase in the Quantitative and Qualitative Easing programme. "Diverging growth fundamentals will also drive divergent exchange rates via increasing rate differentials," says Nolting.

5. Position for strong US$, US growth

Whilst strong economic growth will be a positive for US equities, not all sectors are expected to outperform in this environment. Devitre expects cyclical sectors such as financials to shine brighter than defensives such as food and tobacco. He also points to domestically-focussed companies that sell most of their goods in the US to do better than their export-oriented peers. The strengthening US$ will create greater profit headwinds for such exporters.

"Given the likelihood of increased infrastructure spending paired with corporate and individual tax cuts, we are likely to see a medium-term boost to US economic growth," says Devitre. "This economic growth should drive corporate earnings in the United States."

6. Selective IG bonds for US, Europe, and EM

Investment grade (IG) bonds on both sides of the Atlantic and emerging markets (EM) will also draw attention due to their convincing valuations and strong demand. Nolting says the outlook on European IG credit is positive as the corporate sector purchase programme remains a major driver for tighter spreads. Investors are now focussed on volatility in rates and macro risk instead of concerns about the European banking system.

"We are also constructive on US IG credit, as spreads are expected to tighten despite possible periods of increased volatility," says Nolting. "Demand is exceeding supply and valuations remain compelling." He also retains a constructive view on EM credit given improved EM growth outlook, stabilising commodity prices, positive reform climates in several countries, and a favourable demand-supply picture.

7. Japan equities

With modest economic growth in the cards in 2017 and notable improvements in consumer and business sentiments as well as labour market conditions, Japanese equities are starting to become attractive for investors. More importantly, in the near term, a weaker JPY is likely to support Japanese equities, says Nolting, and the economic outlook is brightening due to improving industrial production in the third quarter of 2016 which was slightly better compared to the first half of 2016 and the year of 2015.

"Note also that the Japanese economy could prove resilient to US anti-free trade rhetoric: exports to the US account for just 3.4% of GDP. We think that the Bank of Japan (BoJ) will continue with its yield curve management strategy for two implicit objectives – to increase inflation and to provide relief to financial sector earnings," he explains.

Meanwhile, a Bank of America Merrill Lynch report says the sustained JPY weakness is likely to lift US$/JPY to 120. The investment bank maintains its view that weaker JPY bodes well for equities.

8. Hedge with RMB

Alongside positioning for a stronger US$, investors should also prepare for a weaker Chinese renminbi (RMB) in 2017, according to Goldman Sachs. "Our forecasts – US$/CNY at 7.30 in 12 months – call for a depreciation that is well beyond forward market pricing, thereby implying positive gains even accounting for the negative carry. And beyond the usual reasons for wanting to hedge exposure to 'China risk', we think it will also hedge the risk of a 'Trump trade tantrum,'" says Himmelberg.

Three main factors will convince investors to hedge with RMB, foremost of which is how China's management of its currency remains vulnerable to the destabilising effect of sharp devaluations against the US$. "Whilst the Chinese authorities have clearly communicated a shift in focus to a trade-weighted currency basket, thus de-emphasising the signal, it is still the case that the only signal that matters is US$/CNY," he says.

"We think higher fixings still run the risk of encouraging capital outflows as households and firms anticipate a faster pace of depreciation," explains Himmelberg. "Whilst the shift to a trade-weighted regime makes sense, China has historically had a bilateral exchange rate, which means that fixing US$/CNY weaker is not as easy as it sounds," he adds.

A second factor is that RMB has a "bias to depreciate," with Goldman Sachs research pointing to an asymmetry in the response of the US$/CNY fix to the dollar. Since March, the US$/CNY fix has risen 0.60% for every 1% rise in the dollar, whilst the US$/CNY fix has fallen only 0.38% for every 1% drop in the dollar. "There is therefore clear evidence of asymmetry in how the RMB responds to dollar moves, which in our minds is evidence of an underlying bias to weaken the currency and supports our bearish view on the RMB," says Himmelberg.

Finally, investors could choose RMB in their quest to find an effective hedge against the key downside risk to the Trump administration, namely if the aggressive effort to renegotiate US tariff and trade agreements ends badly. "Whilst we think Trump will most likely pursue trade agreements that are less radical than his protectionist rhetoric, we nonetheless acknowledge that his negotiations could be more aggressive and hence more risky. China is likely to be a primary focus of these efforts," he adds.

"For one, levying tariffs on Mexico would require repealing North American Free Trade Agreement (NAFTA), which we see as unlikely. Moreover, in contrast to the large bilateral trade deficit that the US runs with China, trade is nearly balanced with Mexico," says Himmelberg. "We think tariffs on Chinese imports represent the clearest risk of Trump's trade policy, and we prefer to use the RMB to hedge this risk."

9. Alternative finance

In 2017, alternative finance will step into the spotlight and will further increase in importance in Singapore and the rest of Southeast Asia, promising a sweet investment ride for those that buy into its potential to satisfy SMEs with no access to bank loan financing. "I think alternative finance is a fast developing, big investment opportunity," says **Roger Crook**, CEO at Capital Springboard. "The rising interest

Stocks in the healthcare and technology sectors are promising bets in 2017

Alternative finance enables investors to diversify their investment portfolio and risks

amongst institutional investors towards alternative finance is an indication that large financial companies will become more engaged in the sector going forward."

He reckons alternative finance is emerging as a mainstream option in Asia that addresses the rising entrepreneurial needs in the region. China, for example, has become the world's largest peer-to-peer lending market by transaction volume with US$101.7b in 2015, accounting for almost 99% of the total volume in the Asia-Pacific region.

"Asia remains a lucrative market which is attracting alternative finance options from diverse parts of the world," says Crook. "Meanwhile, the local market remains optimistic, and will sustain – if not increase – the demand for short-term loans; however it is to be seen what regulatory bodies will do to ensure the prolonged health of the lending space," he adds.

Despite Singapore being the wealthiest country in the region per capita, a recent study by Deloitte highlighted that 40% of local SMEs – which contributes to around 47% of the country's GDP – didn't have access to a bank loan. "Whilst SMEs are hungry for capital, banks are not willing to lend as quickly," says Crook. "The immediate addressable opportunity currently stands at US$3.3t, compared to the already exploited early stage investing market of US$300b."

"Alternative finance is reaching a tipping point from which it will launch into a mainstream financing option and explode in growth rate and high value to become a foundation for global finance," he adds.

Crook reckons that 2017 will see an uptick of entrants in all countries across Southeast Asia, and alternative finance will be attractive for investors because it can help diversify their portfolio amidst these uncertain times.

"Whether it's accredited, institutional, or retail consumers, whether it's trade, invoice trade financing, whether it's SME lending, all segments of peer-to-peer will grow and it will continue to be a very exciting market," says Crook. "With the continuous search for yield in this present market, alternative finance enables an investor to diversify their investment portfolio and risks and at the same time achieve good returns," he adds.

10. ETFs

For investors that are looking to build a low-cost, broadly diversified portfolio, exchange-traded funds (ETFs) may be the simplest way to go, says **James Martielli,** head of portfolio review, Asia at Vanguard. "Many of these products are low cost, offer broad diversification, and are easily accessible with a brokerage account on an exchange," he says.

"As our founder John C. 'Jack' Bogle often said, instead of trying to find the needle in the haystack, just buy the whole haystack instead," adds Martielli. Providing a more general investment strategy, he reckons that predicting which stock, sector, or currency will outperform is always a difficult task since markets are often surprising and unpredictable over the course of a short-term period like a year.

But following four timeless principles – goals, balance, cost, and discipline – improves the chance for investment success. "First, start by aligning your asset allocation with your investment goals. As a rule of thumb, the longer your time horizon, the more you should be able to allocate to riskier assets like stocks," explains Martielli.

He says the next thing they do is encourage investors to maintain balance in their portfolio by having a diversified mix of stocks, sectors, countries, and asset classes. Martielli adds, "Costs is one of the few things in investing that you can control. The less you pay, the more of the investment return you keep."

"Finally, maintaining discipline is easy to say, but harder to do in practice," stresses Martielli. Here is his advice to investors: "Do not be tempted to change your asset allocation if your investment goal or risk tolerance has not changed."

We forecast continued depreciation of RMB against US$

Sources: Bloomberg, various news sources; annotated by Goldman Sachs Global Investment Research