

Phillip 3Q24 Singapore Strategy

Seizing the yield

SINGAPORE | STRATEGY

Review: Singapore's equity market rose 3.4% in 2Q24, the best performance in six quarters. Banks registered another commendable quarter. Attractive dividend yield and recovery in fee income drove share prices (Figure 1). Yangzijiang chalked up a stellar performance (Figure 2), with container freight rates surging 75% over three months. Seatrium's share price was spooked (Figure 3) by new investigations related to Brazil. This was despite securing multiple new contracts, including two FPSO contracts worth S\$11bn. REITs remain a major laggard (Figure 4), weighed down by rising interest expenses. US equities, namely technology, continue to outperform against major asset classes (Figure 5).

Outlook: Economic momentum in the US is slowing. Consumer spending on discretionary items, such as auto sales (Figure 6) and electronics (Figure 7), is slowing down. US government deficits are cooling off (Figure 8), and savings rates (Figure 9) need to creep up from exceptionally low levels. In the US Presidential elections, betting averages now give Trump a clear lead of 54% against Biden's 19%. The lead widened by almost 20% after the recent presidential debate. If Trump uses tariffs for political leverage, at risk will be ASEAN with its surging trade surplus with the US (Figure 10).

Our base case on interest rates is one rate cut in December. We have a Federal Reserve ready to cut rates. Its recent economic projections show that core PCE inflation is not expected to hit its 2% target until 2026. Nevertheless, the Fed expects to still project an interest rate of 3% by 2026, or 2.25% points lower than the current level. Core PCE inflation of 2.6% is already below its projection of 2.8% (Figure 11).

We believe the Singapore economy is also lacklustre and drifting sideways. Exports, the PMI survey, industrial production, loans, and retail are all trending sideways and returning to pre-pandemic levels. Sectors with stronger momentum are tourism, building materials (Figure 12), shipping (Figure 13), and oil and gas (Figure 14). Residential sales this year have been horrendous. New home sales this year until May are down 48% YoY (Figure 15). A delay in approvals for new launches has raised the risk for developers. It likely contributed to a recent land sale with no bidders.

Recommendation: We believe REITs have become a more attractive relative bet. Most REITs hedge their interest rates on a three-year basis. We are entering the second year of rate hikes after the Federal Reserve's first rate hike in March 2022. The headwind of surging interest expenses will largely end by this year. So, rental growth can begin to outpace interest expenses. The first cut in interest rates will also signal its peak, providing clarity for real estate investors and sparking more transaction activity. We favour Cromwell REIT [BUY, TP EUR1.91] as the European Central Bank turns more aggressive in loosening monetary policy. The narrative has moved to two additional rate cuts this year. OUE REIT [BUY, TP S\$0.33] pays an attractive 8% yield with a portfolio of Singapore assets trading at a discount of 50%. CapitaLand Investment [BUY, TP S\$3.38] will benefit from increased real estate transaction activity and improve the performance of the six REITs it manages. On semiconductors, we expect another set of weak 2Q24 results but believe an inventory replenishment cycle can drive recovery later this year. We believe a better way to gain exposure to semiconductors is through their US counterparts [Figure 16]. The listed SGX semiconductor company customers are equipment makers that have a virtual monopoly in their respective equipment sectors. Alternatively, an index of diversified semiconductor names is less volatile and lowers company-specific risk. Banks remain an attractive bet with a yield of 6%. Any upside surprise will come from higher dividends and strong fee income. We removed Thai Beverage [BUY, TP S\$0.63] from our model portfolio. The share price took another leg down due to higher alcohol duties proposed in Vietnam. Our BUY recommendation is unchanged as valuations have turned attractive at 11x PE and consumption in Thailand is recovering over the past few months. We are overweight Banks, Defence, REITs, and Telecommunications.

1 July 2024

2Q24 performance

Figure 1: Another positive quarter for banks

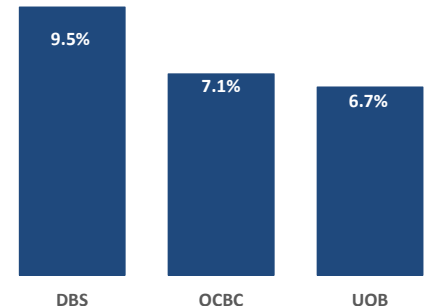


Figure 2: Cyclical bets returning

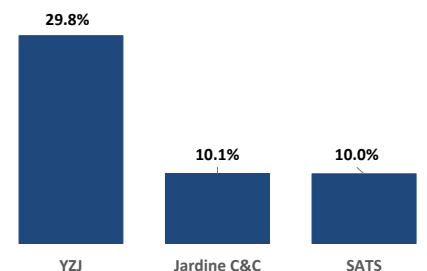


Figure 3: Consumer stocks a drag

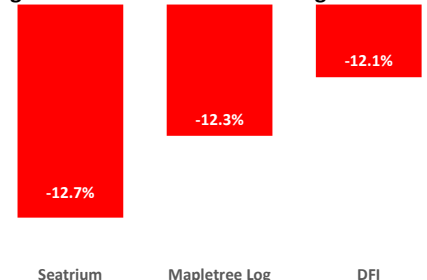
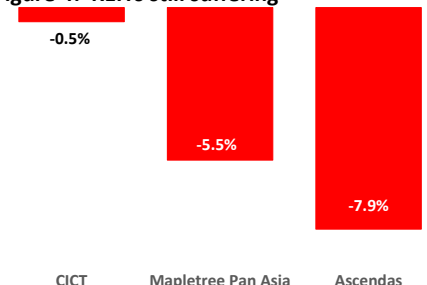


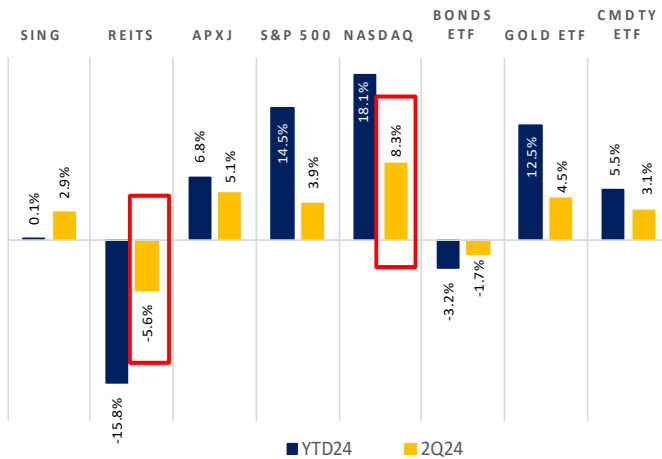
Figure 4: REITs still suffering



Source (Fig 1-4): PSR, Bloomberg, 28Jun24

Paul Chew (+65 6212 1851)
Head of Research
paulchewk@phillip.com.sg

Figure 5: US tech remains in the lead, while REITs suffer



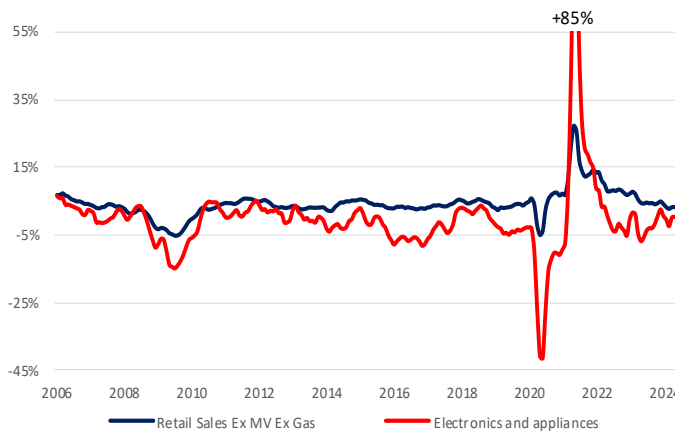
Source: PSR, Bloomberg, performance in USD terms

Figure 6: Signs of discretionary spending pulling back
US: Auto sales (3MMA YoY)



Source: PSR, CEIC

Figure 7: Electronics sales growing sub 1%
US: Retail Sales (3MMA YoY)



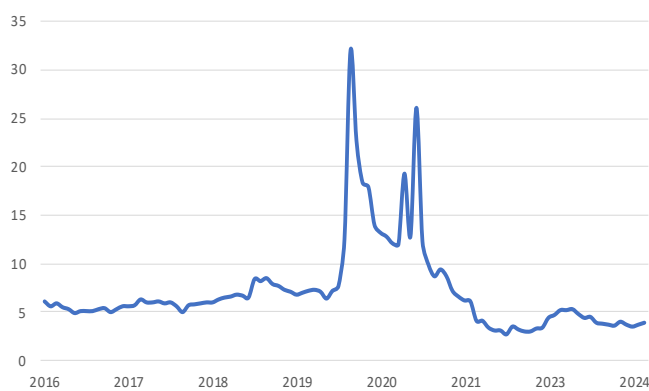
Source: PSR, CEIC

Figure 8: Government stimulus normalising
US: Government Deficit (12M YoY)



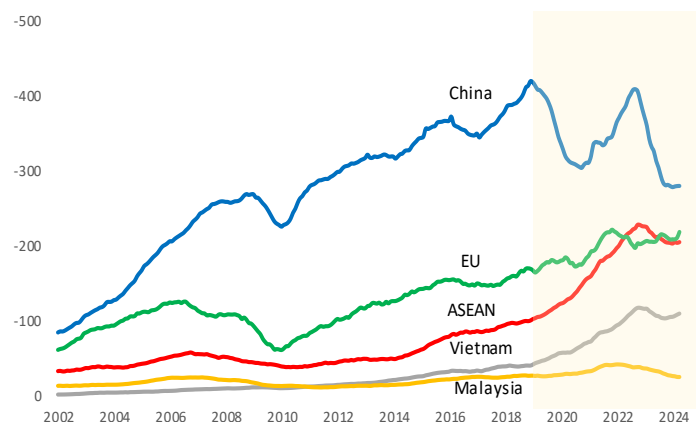
Source: PSR, CEIC

Figure 9: Savings rate at record lows against pre-pandemic 8%
US: Personal saving rate (%)



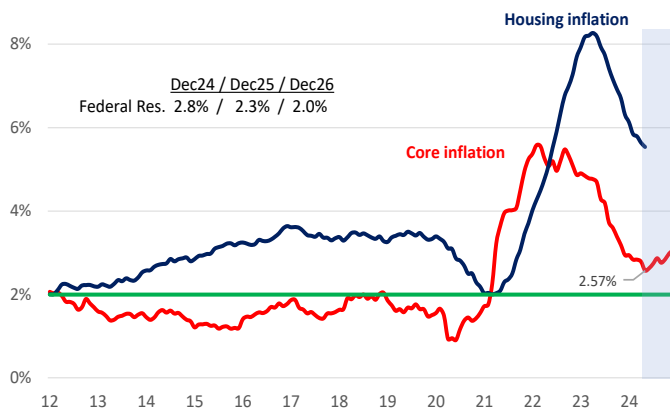
Source: PSR, CEIC

Figure 10: EU and ASEAN should worry about tariffs
US: Trade Deficit (Rolling 12 months US\$bn)



Source: PSR, CEIC

Figure 11: Inflation now below Fed target
US: Core PCE Inflation (YoY)



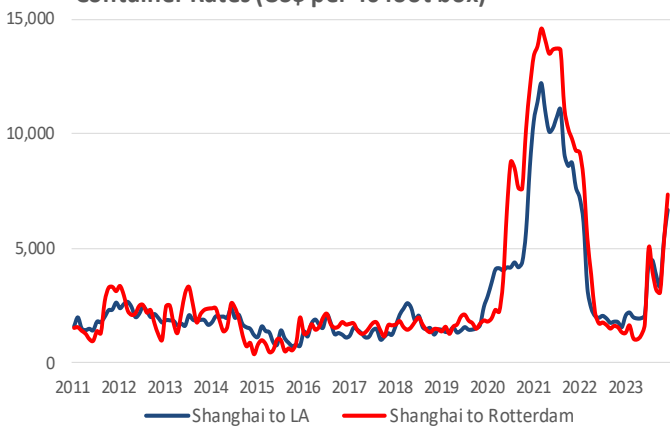
Source: PSR, CEIC

Figure 12: Robust construction demand support building materials
Ready Mixed Concrete Demand (3MMA % YoY)



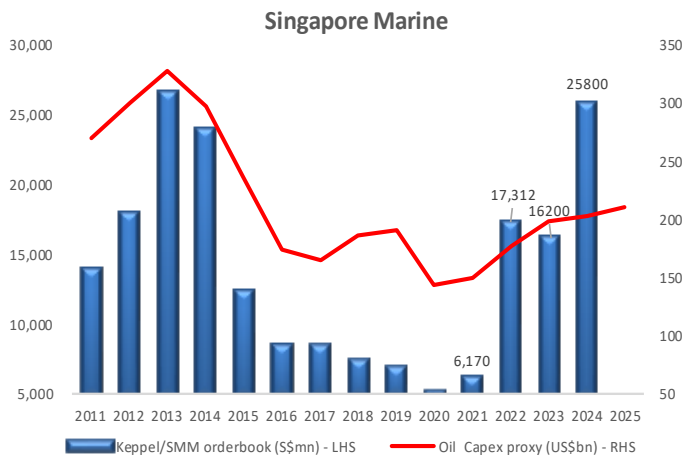
Source: PSR, CEIC

Figure 13: Tripled this year
Container Rates (US\$ per 40 foot box)



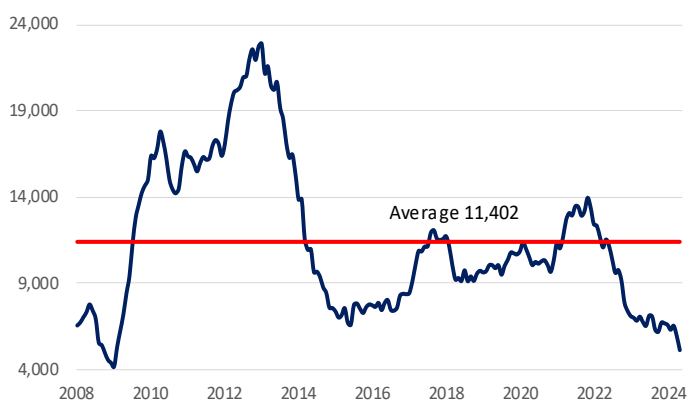
Source: PSR, Bloomberg

Figure 14: Record order books boosted by renewables



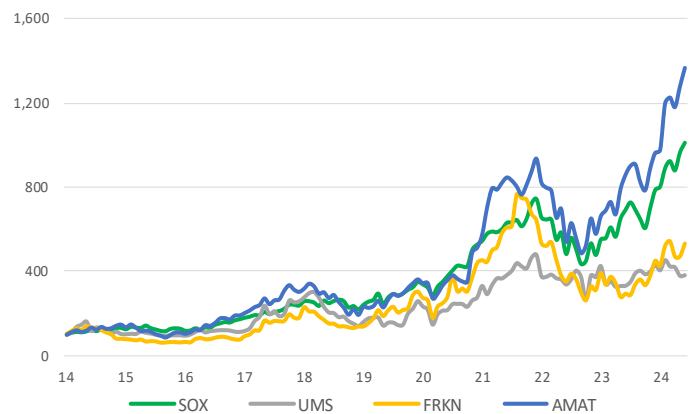
Source: PSR, CEIC

Figure 15: Close to global financial crisis lows
SG: Primary Residential Sales- Excl. EC (12M Total)



Source: PSR, CEIC

Figure 16: Apart from AEM, most have consistently underperformed
Semiconductor: US vs SG (USD excl. dvd)



Source: PSR, Bloomberg

Phillip Absolute 10

Our model portfolio was up 1% during the quarter, underperforming the Singapore market's 3.4% gain. The weakest names in the portfolio were Keppel Ltd (-11.6%), Thai Beverage (-8.2%) and China Aviation (-5.0%). Outperformers were Valuetronics (+11.3%), DBS (+9.5%), and Singtel (+8.7%). Keppel Ltd reported limited monetisation gains. Thai Beverage's share price was hurt by plans to raise alcohol taxes in Vietnam. We remain positive about China Aviation. Outbound passenger travel in China is still surging.

3Q23 - Add: **Thai Beverage**; Remove: **DBS**

4Q23 - Add: **ST Engineering, Singtel**; Remove: **CDL, SGX**

1Q24 - Add: **Valuetronics, China Aviation Oil**; Remove: **CapitaLand Ascott Trust, PropNex**

2Q24 - Add: **DBS, Cromwell European REIT**; Remove: **OCBC, Frasers Centrepoint Trust**

3Q24 - Add: **OUE REIT**; Remove: **Thai Beverage**

Strategy commentary: We are looking to seize or capture yield in our portfolio. Our focus is on high yield dividend names and adding more REITs as the macro backdrop is a slowing economy and a Federal Reserve ready to cut rates.

Changes to model: We removed Thai Beverage due to the overhang from higher alcohol duties. We do see a rebound in beer and alcohol consumption, but the stock's de-rating persists. We added OUE REIT due to its attractive dividend yield of almost 8% and 50% discount to book on its Singapore assets. The REIT has an investment-grade credit rating.

Figure 17: Monthly movements

	Absolute 10	SING
Jan24	-0.9%	-2.7%
Feb24	-0.9%	-0.4%
Mar24	0.7%	2.6%
Apr24	1.5%	2.1%
May24	-0.2%	1.3%
Jun24	-0.3%	-0.1%
Jul24		
Aug24		
Sep24		
Oct24		
Nov24		
Dec24		
YTD	-0.2%	2.9%
Out/(Under)perf.		-3.0%

Source: Bloomberg, PSR, Performance is for illustration only and excludes brokerage fees, dividends and monthly rebalancing costs.

Stock commentaries

Company	Comments
1. Cromwell REIT	Divestment and redevelopment strategies to drive organic growth and stable capital. We expect a forward dividend yield of c.10%. More ECB rate cuts will come after the 25bps cut on 6th June to directly benefit the REIT.
2. DBS	There is an upside to dividends as DBS has no cap on the dividend payout ratio (OCBC / UOB 50%). Stable NIMs, low-single-digit loan growth, and double-digit growth in fee income will sustain earnings momentum.
3. OUE (New)	Heavily discounted investment-grade REIT with a 0.43x P/NAV and attractive dividend yield of 7.8%. We expect rental reversion of 10% in FY24e for office and retail and the hotel variable component to increase by 4.7%.
4. China Aviation	China's international flights are still rocketing upward. In May 24, China's international air passenger traffic was up 2.6x YoY to 5.1mn. The company's aircraft refuelling in Shanghai Pudong Airport will be a major beneficiary.
5. ST Engineering	ST Engineering is enjoying multiple growth drivers backed by a record order book of S\$27.7bn. Earning growth is supported by aircraft MRO, passenger-to-freighter conversion and increased defence spending.
6. Valuetronics	It is turning around its operation with its new customers. Valuations remain attractive with their cash pile of HKD1.16bn (or S\$200mn) or around 80% of the market capitalisation and pay a yield of 6%.
7. CapitaLand Inv.	Fee-related business (FRB) revenue continues to grow (+7% YoY in 1Q24). We expect the return of event-driven fees and the robust lodging business to underpin further growth in FRB revenue. The target is to double funds under management to S\$200 billion in five years.
8. ComfortDelGro	Earnings growth is still underway, led by higher platform fees and commission charged by Zig Singapore, margin improvement from UK bus re-contracting and expansion, and increased taxi fleet size in China.
9. Singtel	Share price drivers for Singtel are S\$200mn p.a. cost-down efforts in Australia and Singapore, a S\$300-400mn EBITDA opportunity in GPU-as-a-Service, and planned asset disposals of S\$6bn.
10. Keppel Ltd	Share price catalysts remain asset monetisation. Keppel targets to monetise a further S\$5-7bn of assets by 2026. It has S\$12.6bn worth of assets on its balance sheet that can be disposed.

Figure 18: Phillip Absolute 10 for 3Q24

Company	1M	3M	YTD	Rating	Target Px (\$)	Share Px (\$)	Upside	Mkt Cap (US\$m)	Dvd. Yield
Yield									
Cromwell REIT (EUR)	-1.4%	2.2%	-0.7%	Buy	1.91	1.41	35%	848	11.1%
DBS Group	-0.4%	9.5%	18.1%	Buy	38.50	35.86	7%	75,131	4.9%
OUE REIT (New)	-3.7%	-7.1%	-8.8%	BUY	0.33	0.260	27%	1,052	8.0%
Dividend / Earnings Growth									
China Aviation	-1.7%	-5.0%	-1.7%	Buy	1.05	0.86	22%	545	3.2%
ST Engineering	3.8%	8.0%	11.6%	Accumulate	4.90	4.34	13%	9,971	3.7%
Valuetronics	2.4%	11.3%	7.6%	Buy	0.76	0.640	19%	193	3.5%
Re-rating Plays									
CapitaLand Investment	-0.8%	-1.5%	-16.5%	Buy	3.38	2.64	28%	9,744	4.5%
ComfortDelGro	-2.9%	-3.6%	-3.6%	Buy	1.63	1.35	21%	2,154	4.9%
Singtel	10.9%	8.7%	11.3%	Buy	3.00	2.75	9%	33,452	5.5%
Keppel Ltd	-3.4%	-11.6%	-8.2%	Accumulate	7.98	6.49	23%	8,634	5.2%
Average	0.29%	1.1%	0.9%				20%		5.5%

Source: Bloomberg, PSR ^ Dividend yields are historical for all stocks

Head of Research

Paul Chew – paulchewkl@phillip.com.sg
Technical Analyst

Zane Aw – zaneawyx@phillip.com.sg
Credit Analyst

Shawn Sng – shawnsngkh@phillip.com.sg
US Tech Analyst (Digital Entertainment/Semicons)

Jonathan Woo – jonathanwookj@phillip.com.sg
Contact Information (Singapore Research Team)
Property | REITs

Darren Chan – darrenchanrx@phillip.com.sg
Property | REITs

Liu Miaomiao – liumm@phillip.com.sg
US Tech Analyst (Hardware/E-commerce/ETF)

Helena Wang – helenawang@phillip.com.sg
Research Admin

Qystina Azli – gystina@phillip.com.sg
Banking & Finance

Glenn Thum – glennthumjc@phillip.com.sg
US Tech Analyst (Software/Services)

Ambrish Shah – amshah@phillipventuresifsc.in
Contact Information (Regional Member Companies)
SINGAPORE
Phillip Securities Pte Ltd

Raffles City Tower
250, North Bridge Road #06-00
Singapore 179101
Tel +65 6533 6001
Fax +65 6535 6631
Website: www.poems.com.sg
JAPAN
Phillip Securities Japan, Ltd.

4-2 Nihonbashi Kabuto-cho Chuo-ku,
Tokyo 103-0026
Tel +81-3 3666 2101
Fax +81-3 3666 6090
Website: www.phillip.co.jp
THAILAND
Phillip Securities (Thailand) Public Co. Ltd

15th Floor, Vorawat Building,
849 Silom Road, Silom, Bangkok,
Bangkok 10500 Thailand
Tel +66-2 6351700 / 22680999
Fax +66-2 22680921
Website: www.phillip.co.th
UNITED STATES
Phillip Capital Inc

141 W Jackson Blvd Ste 3050
The Chicago Board of Trade Building
Chicago, IL 60604 USA
Tel +1-312 356 9000
Fax +1-312 356 9005
Website: www.phillipusa.com
INDIA
PhillipCapital (India) Private Limited

No.1, 18th Floor, Urmi Estate
95, Ganpatrao Kadam Marg
Lower Parel West, Mumbai 400-013
Maharashtra, India
Tel: +91-22-2300 2999 / Fax: +91-22-2300 2969
Website: www.phillipcapital.in
MALAYSIA
Phillip Capital Management Sdn Bhd

B-3-6 Block B Level 3 Megan Avenue II,
No. 12, Jalan Yap Kwan Seng, 50450
Kuala Lumpur
Tel +603 2162 8841
Fax +603 2166 5099
Website: www.poems.com.my
INDONESIA
PT Phillip Securities Indonesia

ANZ Tower Level 23B,
Jl Jend Sudirman Kav 33A
Jakarta 10220 – Indonesia
Tel +62-21 5790 0800
Fax +62-21 5790 0809
Website: www.phillip.co.id
FRANCE
King & Shaxson Capital Limited

3rd Floor, 35 Rue de la Bienfaisance 75008
Paris France
Tel +33-1 45633100
Fax +33-1 45636017
Website: www.kingandshaxson.com
AUSTRALIA
Phillip Capital Limited

Level 10, 330 Collins Street
Melbourne, Victoria 3000, Australia
Tel +61-03 8633 9803
Fax +61-03 8633 9899
Website: www.phillipcapital.com.au
TURKEY
PhillipCapital Menkul Degerler

Dr. Cemil Bengü Cad. Hak Is Merkezi
No. 2 Kat. 6A Caglayan
34403 Istanbul, Turkey
Tel: 0212 296 84 84
Fax: 0212 233 69 29
Website: www.phillipcapital.com.tr
HONG KONG
Phillip Securities (HK) Ltd

11/F United Centre 95 Queensway
Hong Kong
Tel +852 2277 6600
Fax +852 2868 5307
Websites: www.phillip.com.hk
CHINA
Phillip Financial Advisory (Shanghai) Co Ltd

No 550 Yan An East Road,
Ocean Tower Unit 2318,
Postal code 200001
Tel +86-21 5169 9200
Fax +86-21 6351 2940
Website: www.phillip.com.cn
UNITED KINGDOM
King & Shaxson Capital Limited

6th Floor, Candlewick House,
120 Cannon Street,
London, EC4N 6AS
Tel +44-20 7426 5950
Fax +44-20 7626 1757
Website: www.kingandshaxson.com
CAMBODIA
Phillip Bank Plc

Ground Floor of B-Office Centre, #61-64,
Norodom Blvd Corner Street 306, Sangkat
Boeung Keng Kang 1, Khan Chamkamorn,
Phnom Penh, Cambodia
Tel: 855 (0) 7796 6151/855 (0) 1620 0769
Website: www.phillipbank.com.kh
DUBAI
Phillip Futures DMCC

Member of the Dubai Gold and
Commodities Exchange (DGEX)
Unit No 601, Plot No 58, White Crown Bldg,
Sheikh Zayed Road, P.O.Box 212291
Dubai-UAE
Tel: +971-4-3325052 / Fax: + 971-4-3328895

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