2025 Investment Outlook – Asia Fixed Income: Investment Grade

November 2024

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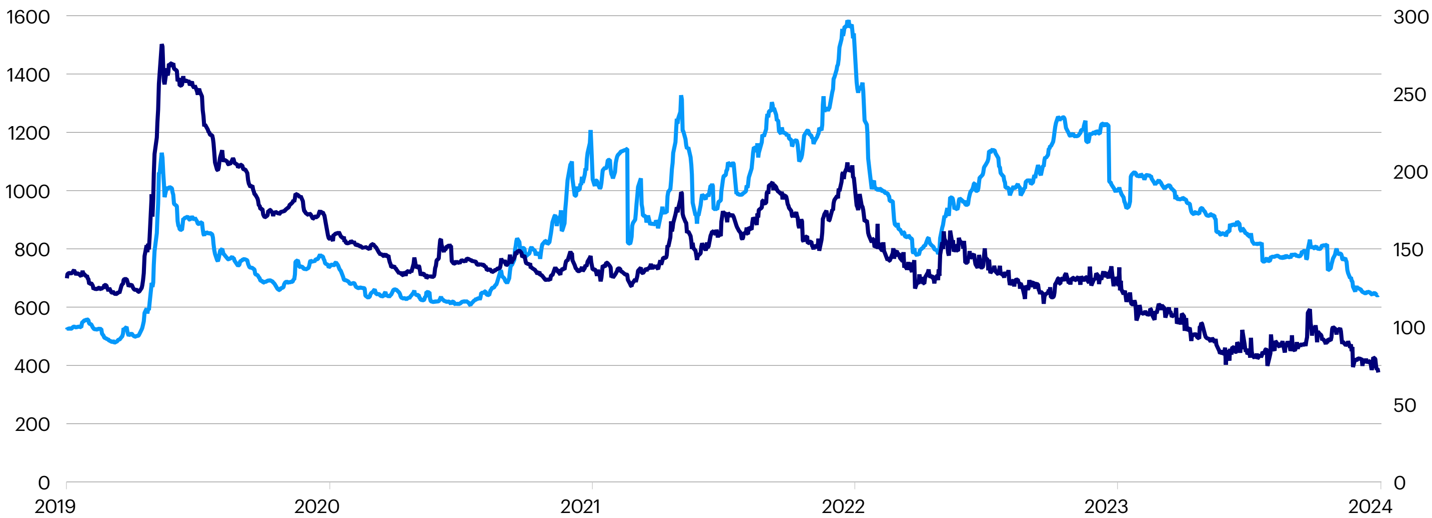
Global macro events continued to dominate the market in recent months. Both the surprise 50 bps cut by the US Federal Reserve (Fed) at the September Federal Open Market Committee (FOMC) and China's easing announcement have been constructive for Asian credit. Nonetheless, the repricing of the Fed policy path and the US election have greatly increased uncertainty and volatility. Despite the massive sell-off in US rates, Asia investment grade (IG) still recorded a decent return year-to-date as spreads traded at historical tights.

Recently strong US macro data has reset a less dovish path for expected Fed policy. The president-elect Trump's victory and a likely Republican sweep is expected to push US rates higher as all of his major policy initiatives (tariffs, fiscal policy, immigration) are inflationary and the fiscal deficit is set to materially widen. At the latest November FOMC, Fed Chair Powell declined to comment on Trump's policy agenda and the appropriate Fed response. He reiterated that the Fed's policy decisions would be data dependent, and the current economy still supports further easing as the labor market and wages have cooled and inflation has been trending toward the Fed's target.

The market has significantly pared down rate cut expectations since Trump won the presidential election. Beyond January, heightened policy uncertainty may lead the Fed to move more slowly than it otherwise would. The Fed Fund futures market is now implying less than 100bps of cumulative easing through 2025.

Asia IG spreads continued to tighten in Q4 despite the sell-off in US rates. JP Morgan Asia Credit Index (JACI) IG spreads have tightened -27bps to 70 basis points (as of Nov 8, 2024) from +97bps (as of Aug 16, 2024). Nonetheless, Asia credit investors are comfortably holding onto bonds despite rich valuations and escalated rates volatility. With stable fundamentals and low default rates, Asia credits appear attractive from all-in yield perspective.

Figure 1 - JACI Investment Grade versus JACI High Yield (November 2019 – November 2024)



	Mid Price
JACINGSW Index (J.P. Morgan JACI Non-Investment Grade Strip Spread to Worst (%)) (L1)	641.56
JACIIGSW Index (J.P. Morgan JACI Investment Grade Strip Spread to Worst (%)) (R1)	70.48

Source: Bloomberg, data as of 8 November 2024. **Past performance does not guarantee future results.**
An investment cannot be made directly in an index.

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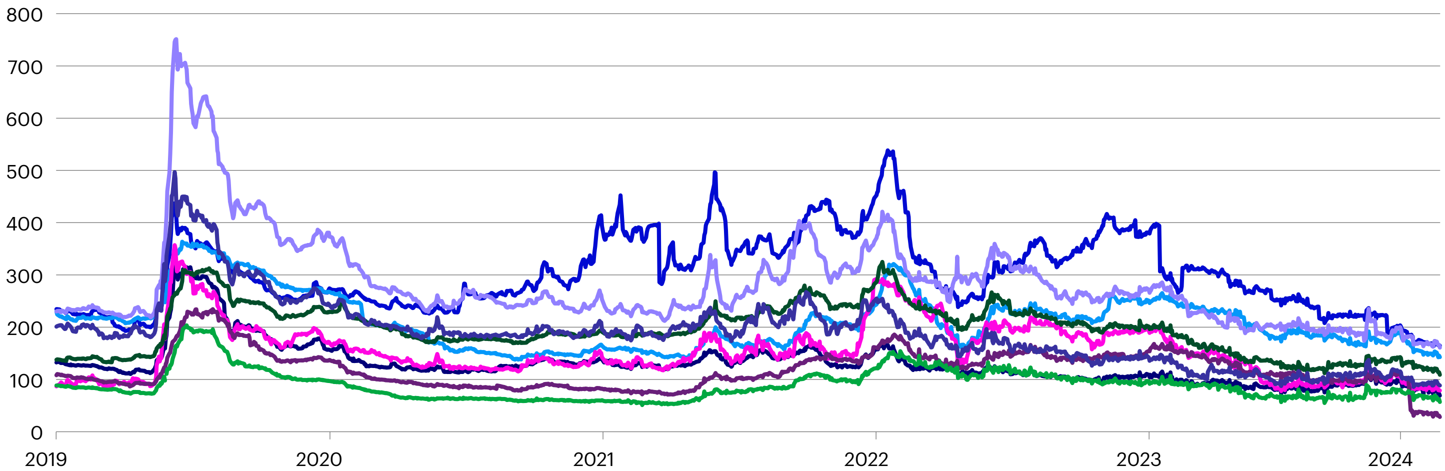
Emerging market (EM) Asia economic growth has been growing at a healthy pace. While exports may remain resilient in the next 1 or 2 quarters on front-loaded shipments, keeping real GDP strong, US tariffs will likely be the key downside risk to growth in 2025. A strong US dollar could pose headwinds and limit the potential room for EM Asia to lower rates even though core inflation is trending down. Despite the potential challenges to the overall EM Asia economies, we believe Asia IG corporates' credit fundamentals may remain largely stable with ongoing deleveraging and sufficient liquidity.

Market technicals continued to be supportive even with a pickup in new supply year-to-date. Negative net supply is likely to remain due to bond redemption and coupons. We expect the primary market to become more active if US rates trend lower later next year. In general, the primary market does present some attractive relative value opportunities. We expect new issue supply to remain strong in 2025 led by financials, whereas sovereign new issuance will continue to lag. We believe the primary market will likely continue to be a focus for investors, and new issue performance and technicals are likely to drive market performance.

Asia IG credit spreads are currently tight relative to historical standards as well as compared to global IG peers. Asian financials, bank tier 2 papers and insurance company subordinated debt are the key areas that look compelling in terms of relative value. We started to see a risk premium at the longer-end of the credit curve post the recent rates sell-off. However, we continue to prefer 5-7years over the longer-end given the potential rates volatility. Despite trade tariff threats, we remain constructive on China IG in the medium term and expect companies to benefit from China's easing policy and stimulus. In addition, we think China IG credits should continue to enjoy strong technicals driven by onshore buying interests. We expect Asian IG credit spreads to broadly remain range-bound for 1H 2025 despite near-term volatility. Asia IG yield offers at 5 to 5.20% low volatility returns appear very attractive. All-in yield buying interests should continue to drive investor flows.

Figure 2 – Asia credit spreads by country over the past five years (Nov 2019 – Nov 2024)



	Mid Price
J.P. Morgan JACI China Strip Spread to Worst (%)	165.59
J.P. Morgan JACI Hong Kong Strip Spread to Worst (%)	145.55
J.P. Morgan JACI Malaysia Strip Spread to Worst (%)	72.83
J.P. Morgan JACI Philippines Strip Spread to Worst (%)	79.78
J.P. Morgan JACI Singapore Strip Spread to Worst (%)	30.84

	Mid Price
J.P. Morgan JACI Korea Strip Spread to Worst (%)	62.30
J.P. Morgan JACI Thailand Strip Spread to Worst (%)	113.66
J.P. Morgan JACI IndiaStrip Spread to Worst (%)	165.85
J.P. Morgan JACI Indonesia Strip Spread to Worst (%)	89.64

Source: Bloomberg, data as of November 8, 2024. **Past performance does not guarantee future results.** An investment cannot be made in an index.

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President-elect Trump's policy will likely set the tone for all asset classes in 2025. However, Asian central banks are expected to respond with policies that will support exports and domestic demand. In the medium term, we believe US inflation will consolidate around current levels. Growth however should continue to slow and justify the Fed's easing cycle. We believe Asia IG credit will continue to deliver solid returns in 2025, mainly supported by the moves in US treasuries. Despite the uncertainties in US policy and the rates path, stable fundamentals and strong technicals in Asian credits should keep spreads tight. Receding rates volatility in 1H 2025 should gradually attract fund flows into Asia IG. While we do not see scope for material spread compression in Asia IG from current levels, we believe the high all-in yields should continue to be supportive for 2025.

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Investment risks

The value of investments and any income will fluctuate (this may partly be the result of exchange rate fluctuations) and investors may not get back the full amount invested.

When investing in less developed countries, you should be prepared to accept significantly large fluctuations in value.

Investment in certain securities listed in China can involve significant regulatory constraints that may affect liquidity and/or investment performance.

Important information