

Asia high yield shines amidst reopening recovery

Recent banking concerns in Europe and the US have highlighted the risks of rapid policy tightening following a prolonged period of low interest rates. While Western economies face an increased risk of recession under a restrictive monetary policy this year, Asian economies are beginning to recover as they reopen post-pandemic. Given the likelihood of stronger growth in Asia relative to the West, the case for investing in Asian bonds is compelling. The reopening of China and the structural improvements seen in ASEAN countries could give crucial support to economic growth throughout the region, thus providing a more positive backdrop for the Asian high-yield market.

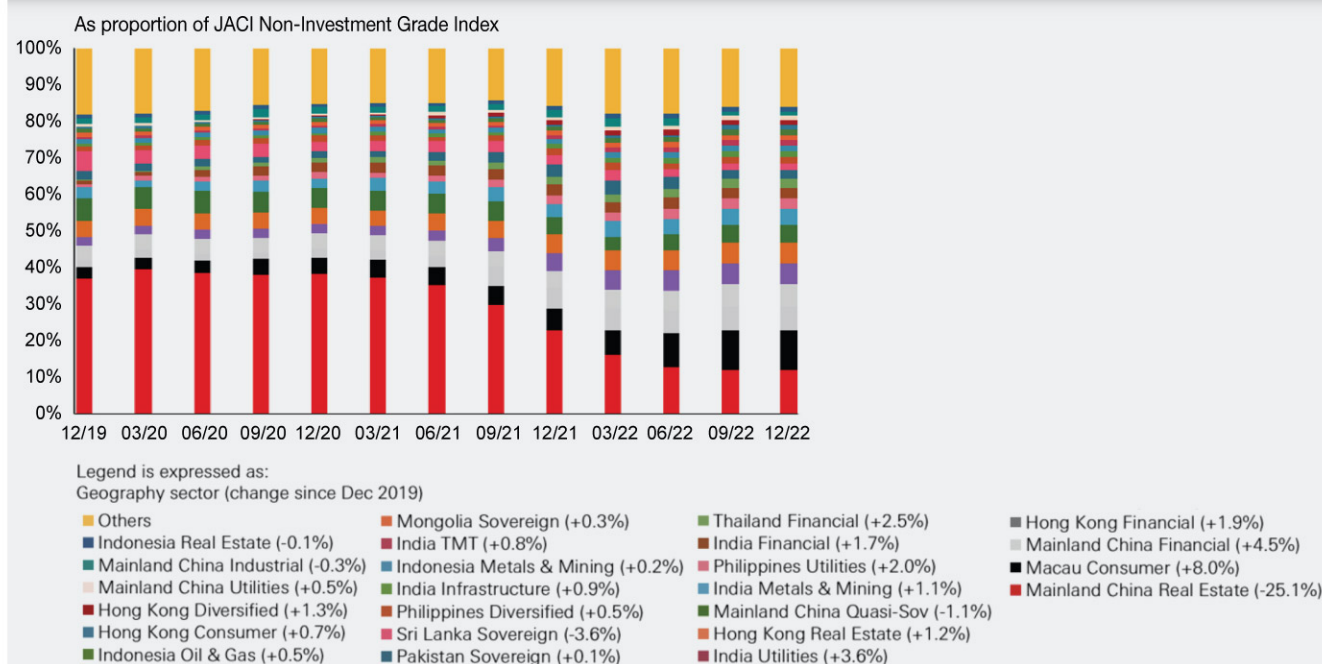
Balanced and diversified universe with attractive yield

According to the JACI Non-Investment Grade Index, the Asia high-yield market covers a diverse range of issuers from various

regions and sectors, and includes bonds with different durations and credit ratings.

Geographically, mainland China remains a significant segment in the Asia high-yield market. However, the market also comprises other rapidly growing economies such as India, Indonesia, Singapore, the Philippines, and Thailand. In terms of sector, investors have observed significant shifts in the past year. The China property sector, which used to dominate the Asia high-yield market, has shrunk considerably, and now accounts for only around 10% of the Asia high-yield universe (Chart 1). Other sectors such as finance, consumers, and utilities have gained growing importance, resulting in a more balanced and diversified investment universe.

Chart 1: Evolution of the Asia high yield bond market



Source: JP Morgan, HSBC Asset Management, 31 December 2022. For illustrative purpose only.

The valuation of the Asia credit market is compelling. In the high-yield space, investors can see yields reaching double digits for Chinese bonds, and 8.6% and 10.5% for Indonesian and Indian credits, respectively (Chart 2). In comparison to similar types of

bonds in the US and European markets, Asia high yields offer higher yields with lower durations, making them an attractive asset class at this juncture.

Chart 2: High yield sectors outside of China also offer yield - Indonesia and India stand out



Using JPMorgan Asia Credit Index (non investment grade).

Source: JPMorgan, HSBC Asset Management as of 17 March 2023.

Investment involves risks. Past performance is not indicative of future performance. For illustrative purpose only.

Looking forward to the second half of 2023, with the easing of energy prices from the peak last year, inflationary pressures in the US are expected to subside, potentially benefiting the bond market as a whole. Moreover, as the risk of recession and uncertainty in Western developed markets continues to grow, investors see a more constructive macroeconomic outlook characterized by favorable growth prospects in Asia. As such, investment in Asia high-yield bonds could become all the more attractive.

China to continue supportive measures for real estate sector

In recent years, the mainland China property sector has constrained performance in the Asia high-yield market. However, additional supportive measures and the relaxation of COVID policies by the Chinese government have bolstered its recovery.

In last November, the Chinese authorities announced a 16-point plan to support the housing market, leading to larger credit lines being granted by the major Chinese banks to 17 property developers. These measures provided relief to the sector's liquidity issues and contributed to the significant rally in the property sector. Furthermore, the Chinese government has continued to announce additional supportive measures, including relaxed escrow account control and the resumption of equity financing. These actions demonstrate the government's commitment to restoring market confidence. With China signaling the end of the deleveraging cycle for the sector, the focus is likely to shift towards addressing the credit transmission gap. Investors are likely to see a recovery of contracted sales as China's economy continues its reopening.

While the macroeconomic situation has improved, investors should remain mindful of the potential risks in the China property sector. Weaker property developers may still be at risk, and defaults are expected to continue. Moreover, property sales continue to face challenges as China transitions from a COVID-restricted world to a post-pandemic era. Economic data may take time to reflect improvements, and housing sales recovery is linked to economic recovery, so a rebound in the physical market may require more time. Investors should be selective in bonds investment in the mainland-China property sector.

On a separate note, with positive market sentiment due to consumption recovery and industrial production, investors remain overweight on China industrials high yield and Macau gaming industry, as the market see stronger-than-expected visitor arrivals and pent-up demand from the premium mass. The resumption of group tours and e-visas for mainland-China residents is improving Macau's economic recovery and strengthening the sector's performance.

Constructive outlook on selected India and Indonesia sectors

Apart from China, ASEAN countries have made significant improvements in their macroeconomic fundamentals. Along with the recovery of their tourism industries and China's reopening, ASEAN issuers' strong access to local funding has also helped keep the overall default rate at manageable levels.

Therefore, investors also favor the commodity sector in India and the coal sector in Indonesia. It is expected that the strong demand for commodities and energy will support prices and, in turn, benefit these sectors. Similarly, investors also favor the Indonesia property sector as it could benefit from further improvement in the local economic conditions. In India, investors remain optimistic about the renewable energy sector and believe that global investment in sustainability could support the industry.

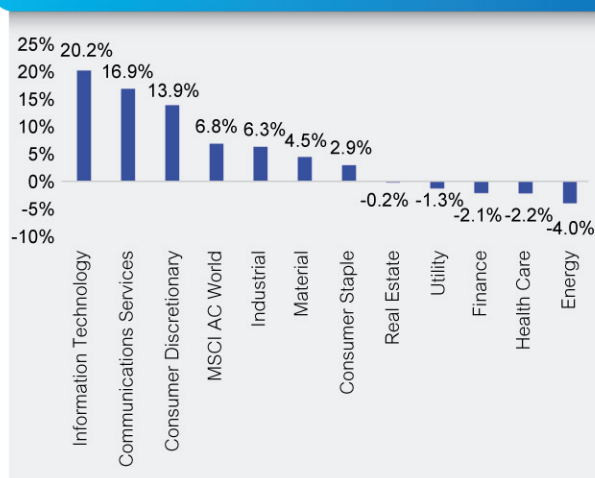
Overall, as the risk of a recession in the US and European economies remains, market volatility is likely to persist. However, as seen in recent market developments, the global monetary tightening cycle could come to an end soon. Together with the cyclical weakening of the US dollar, they could be important drivers for emerging market bond performance. Asia, in particular, finds itself in a "parallel world" with the West due to the region's strong growth momentum and lower inflation. Investors can thus turn to Asian bonds for higher growth prospects.

Four key trends shaping the investment landscape of the global consumer

In Q1 2023, global equities rebounded following the sell-off last year as there were signs that inflation was abating. Within the MSCI AC World index, sectors such as information technology, communications services, and consumer discretionary outperformed the broader market.¹

The United Nations' World Tourism Organization estimates that international tourism in 2022 recovered to 63% of its pre-pandemic levels.² And global sales of sun-and-sea packages rose 75% in 2022 to almost US\$69 billion, according to the World Travel and Tourism Council.³

Chart 1: Q1 2023 Global Equity sector performance



Source: Bloomberg, as of March 31, 2023. **Past performance is not a guide to future returns.**

As many investors anticipate the Federal Reserve pausing rate hikes this year or even cutting rates later, this development would be beneficial for discounted cash flow valuation of growth stocks, where more of their value is attributed to the future. With a sufficient time horizon, there could be room for valuations to improve from here.

It is likely that investors may re-focus on the latest global consumer trends as they reassess the consumer sector's investment landscape. Below are the key trends shaping consumer behavior.

1) In-person experiences after COVID (Travel, Movies, etc.)

During the pandemic, trips to the movies, vacations, and family holidays were put off. Much of the world has developed some immunity to the COVID virus and in-person activities are back on the menu.

As many people now have the ability to enjoy in-person activities again, a massive recovery is seen, in fact the pent-up appetite for some of these activities is leading to record demand for certain experiences.

China, in particular, is undergoing the same unlocking of experiences - with even greater impact given their longer lockdown and huge consumer savings. In fact, China saw strong mobility and consumption recovery after reopening. During the Chinese New Year, passenger trips reached 1.59 billion, a year-on-year increase of 50.5%, recovering to 53.5% of the same period in 2019.⁴ Retail sales jumped 10.6% in March, marking the strongest rebound since June 2021 and signaling that consumer demand is back on the growth track.⁵

Chart 2: China flights returned to 90% of pre-pandemic level



Source: STR, Morgan Stanley Research, as of January 10, 2023.

Many consumer-focused experiences are unique and will continue to drive physical excursions into the future. It is unique to eat in the ambiance of a fine restaurant, gamble and shop in a destination casino, go to a concert or movie theatre, experience a museum, or travel to see unique cultures and sites.

While many of these experiences have been curtailed or reduced during this period of social distancing, they are recovering with great momentum.

2) eCommerce: Becoming everything and everyone

The pandemic lockdowns accelerated the shift to e-commerce, bringing new users to the platforms, and expanding the types of goods people buy online.

But there are very large markets which are still early in their adoption of e-commerce.

Food and consumables which are groceries and staples represent about 1/3 of consumer spending* and despite massive growth during the pandemic, their e-commerce penetration is still early in adoption.

The luxury goods market is expected to grow for years to come, fueled by the emerging middle class across many geographies. This market is also very early in the shift online, although the leading platforms which will own luxury e-commerce in the future have already emerged.

Household durables, like furniture and appliances and other hard-to-ship items, have begun shifting online as well. And the early leaders for autos - buying a car online - have a very long runway of growth in this shift.

All in, these categories represent more than 2/3 of our consumption that is still early in e-commerce adoption.*

New trend - Social commerce is giving e-shoppers a new experience

Social commerce is the use of social media platforms for product promotion and sales. It enhances customer interaction with commenting and liking features, helping shoppers to explore products and exchange information. Meanwhile, AI now enables virtual fitting and try-on, which boosts fashion and cosmetic retail.

US retail social commerce sales could reach US\$79.6 billion by 2028, accounting for 5.2% of total retail e-commerce sale.⁶

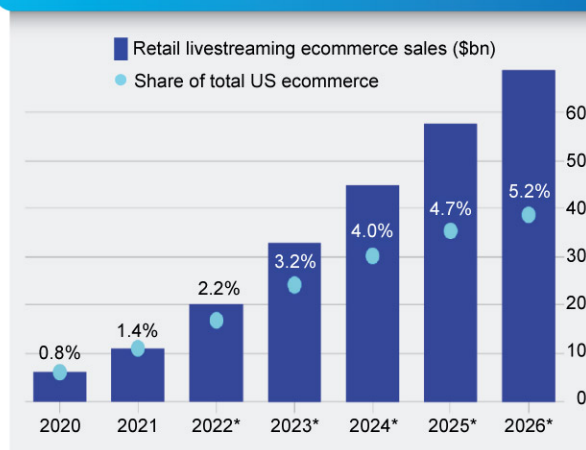
Some e-commerce giants have recently launched their own social commerce platforms with features enabling brands to post their photos and videos, so that customers can be directed to a product page when they click on items of interest.

New trend - Livestream shopping craze sweeping from east to west

Livestream shopping is popular in China given the power of KOLs and limited-time offers. China's total retail sales of consumer goods reached RMB45 trillion in 2021, with about 5% attributed to livestream shopping.⁷

Livestream shopping has huge growth potential in western markets given the massive social media user base. Livestream shopping may account for 5.2% of total e-commerce sale in the US by 2026.⁸

Chart 3: U.S. livestream commerce market size



Source: Financial Times, as of August 11, 2022. *Estimates.

3) Electrification of vehicles

As the world continues to focus on reducing carbon emissions and combating climate change, the future of electric vehicles (EVs) looks bright, as does the potential for high returns on investment as the EV industry continues to grow and mature.

With advancements in battery technology and a growing demand for sustainable transportation options due to concerns about the impact of fossil fuels on the environment, EVs are poised to play a major role in the future of transportation.

In recent years, there has been a significant increase in the number of EVs on the road.

Global electric vehicle sales reached a record of 6.6 million units in 2021, almost double the previous year and accounting for nearly 9% of total vehicle sales.⁹

This trend is expected to continue, with many countries setting ambitious targets for emission cuts and the adoption of EVs. For example, the European Union has set a goal of having 30% of all new car sales be EVs by 2030, while China aims for 20% of its car population to be electric by 2025.¹⁰

4) Video games: mobile and global

The video game industry has been growing for more than a decade, fueled by demographics including a massive generation of millennials and the digital-first generation Z behind them.

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EYE ON THE MARKET

A better business model has evolved, with digital downloads being more convenient for game players and more profitable than selling disks through a store for game developers.

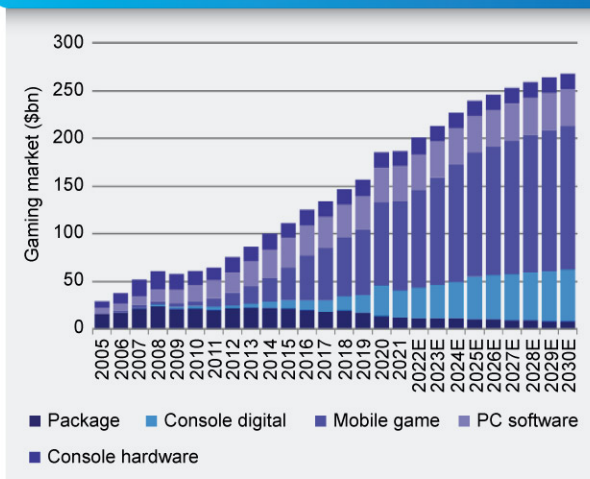
But the big driver is the current market expansion to mobile devices. Mobile devices mean people are connected everywhere they go, all the time, and they can actually create time to spend on leisure activities and consumption.

Today's smartphones have much faster graphics-processing chips than a traditional video game console. This is a powerful factor because the great game franchises of the last 20 years can now be rendered on a mobile device. It is also massively market expansionary as there are roughly six times as many consumers globally with a smartphone than those with a gaming PC or console.

Source:

1. Bloomberg, as of March 31, 2023
 2. Bloomberg, as of February 9, 2023
 3. Bloomberg, as of February 9, 2023
 4. Ministry of Transport of the People's Republic of China as at February 16, 2023.
 5. MarketWatch, as of April 18, 2023
 6. McKinsey & Company, October 19, 2022.
 7. National Development and Reform Commission, as of October 31, 2022.
 8. Financial Times, as of August 11, 2022.
 9. The International Council on Clean Transportation, as of June 29, 2022.
 10. New York Times Chinese, as of September 27, 2022.
- * Invesco, as of December 31, 2022

Chart 4: Video game spending



Source: Game market size – Company data, Goldman Sachs Global Investment Research, as of April 2022.

These trends lead us to believe that two of the world's most powerful drivers (demographics and mobile connectivity) look set to benefit the video game industry for years to come.

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