Manulife Investment Management

News Release

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Manulife Investment Management: Emerging Markets move into a more challenging regime, but opportunities remain in 2022

- Select emerging Asia equities and fixed income markets are in a better position to withstand potential macro headwinds
- ASEAN markets likely to benefit from favourable government policies and play the role of key growth drivers
- Sustainable Asian credits see a better year ahead given rising concerns over ESG issues

HONG KONG / SINGAPORE – As we head into 2022, a year dominated by a long list of known unknowns, namely rising US inflation and rate-hike expectations, geopolitical tensions, spike in COVID-19 cases and appearance of new variants. Such a long list of macro headwinds implies that the first half of 2022 may look challenging: Price pressures look as though they might ease, but inflation could remain uncomfortably high for the first few months of the year. However, prospects for the second half of 2022 look better, as inventory rebuilds and the unwinding of supply chain disruptions are expected to fuel a more sustainable recovery than the pent-up rebound of 2021.

An improved growth picture and slower inflation are likely to bring global markets back to a Goldilocks regime, which should be far better for market returns and general risk assets.

Sue Trinh, Head of Macro Strategy, Asia, Manulife Investment Management, said: "Once inflationary and growth pressures ease, we expect global central banks to make a dovish policy pivot, which should create conditions that will allow for an extension of the economic growth cycle. While we expect uncomfortably high levels of inflation in the first half of 2022, they are likely to be driven by global supply issues, which can't be addressed with interest-rate policy. With the Fed's plan to reduce its asset purchasing program, potential volatility in the USD and U.S. interest rates may weigh on global liquidity – an element that's crucial to Asian growth."

"We think emerging Asia's equities and fixed income will be supported by accommodative monetary policy stances and are in a better position to withstand the Fed's taper risks relative to 2013, thanks to stronger external positions, lower reliance on external funding, and better-balanced positioning. While inflation will likely pick up further, large output gaps will help keep underlying price pressures in check. In the event global supply bottlenecks worsen upside inflation pressures, Asia is likely to escape the worst of the global inflationary shock, particular versus other emerging markets."

"Cyclically, macro conditions are expected to be more favourable for the reopening or recovery in Taiwan, Japan, and some of the ASEAN markets this year. Structurally, the Asia region has a lot of work to do to recoup lost output due to the pandemic. The biggest concern remains weak consumer demand which will be exposed by the looming downturn in export growth. On the other hand, Asia's milder inflation expectation comes down to one simple factor – trade surpluses. Maximising export production remains the marginal growth driver through the pandemic. At the same time, re-opening and pent-up demand pressure has not been as strong, while household consumption growth has rebounded much faster in other regions compared to Asia."

"For the Asia region as a whole, we expect to see policy normalization will be at a much slower pace and of lower magnitude relative to previous cycles and other emerging markets."

Asian Equities: Southeast Asian markets as the key growth drivers

The emergence of the Omicron variant, China's regulatory tightening cycle and central banks' actions further impacted the growth in Asia heading into 2022. **Ronald Chan, Chief Investment Officer, Equities, Asia ex-Japan, Manulife Investment Management** considers these developments and assesses their potential impact on the regional economic landscape over the year ahead.

"Some of the macro factors that we would highlight for 2022 are the COVID-19 variant, the US Taper and China's growth pattern, all of which represent growth headwinds for Asia. However, their impact is expected to be felt differently in North Asia compared to Southeast Asia. As such, we expect GDP growth in China to slow from 8% in 2021 to around 5% in 2022, which is lower than the growth projection for Southeast Asia. Our positive outlook for Southeast Asia is further propelled by the 6%–7% expected growth momentum in India. In addition, our positive view towards the sub region is further reinforced by the higher real yields in major economies, namely Indonesia and India, which are attracting capital flows."

"Given the previous tensions between China and the US, we believe that Southeast Asia will be a strategic beneficiary, at least over the medium term, as there may be foreign direct investments in specific sectors. These include battery suppliers in Indonesia, auto companies in Thailand, and IT supply chain in Malaysia."

"While physical ASEAN integration is not satisfactory as expected, digital integration within the bloc is more encouraging. Currently, over 30 big-tech unicorns are due to go public, and this process is expected to extend to fintech, logistics providers, and e-commerce players. These companies share two features – the business lines of unicorns which will adapt more readily for regionalisation, and ASEAN governments' fewer regulations on industries like e-commerce, internet and e-gaming."

"The near-term outlook for ASEAN is expected to improve as economies reopen, with most of the bloc's countries relaxing movement and travel restrictions, albeit gradually. Strategically, Southeast Asia should play an important post-pandemic role in Asia's economic trajectory. The "China Plus One" initiative has encouraged multinational companies to diversify their business lines and production bases into regional markets."

Asian Fixed Income: High-yield credits and sustainable bonds are poised to growth

Asian fixed income markets experienced a challenging 2021. Regional economies gradually recovered from the COVID-19 pandemic, while regulatory changes and idiosyncratic risk in some markets contributed to a divergence in performance between investment-grade and high-yield credits. **Murray Collis, Deputy Chief Investment Officer, Fixed Income, Asia ex-Japan, Manulife Investment Management** highlights the significant opportunities in the Asia fixed income space.

"We believe that Asian high-yield bonds offer particularly attractive valuations, with bond yield spreads well above historical averages, providing significant opportunities this year. Overall, we see global liquidity to remain relatively accommodative from a historical perspective for Asian credits in 2022. We believe that some credits, especially in the high-yield segment, are excessively priced to the downside. Indeed, price dislocations, particularly in the China real estate sector, that were experienced in 2021 do not reflect the underlying fundamentals of higher-quality developers."

In 2021, supply and demand on the ESG front has proven that there has been a growing popularity of sustainability-linked bonds. On the Asian sustainable bond market, Murray added:

"In the Asia-Pacific region (excluding Japan), around one in five new bond issue deal was an ESG bond. In what we consider to be a positive development, we're beginning to see growth of another kind – diversification in issuers in terms of breadth (sectors) and geography in both the credit and sovereign space. We expect the issuance of ESG bonds in Asia to continue to grow in 2022, as focus shifts from declaration of intent to actual implementation post COP26 summit."

"While we look at the challenges Asian credit has faced throughout 2021, there's every reason for investors to remain cautious, as the recent upheaval has taken out the froth in the Asian bond market. The J.P. Morgan Asia Credit Index, which is widely used as a proxy for the market, lost around 3% in 2021.[1] The way we see it, the repricing of risk brought about a valuation reset. This is particularly true in the high-yield space where asset prices have fallen to a level not seen in years, relative to their peers in Europe and the US. In our view, this has created a compelling opportunity in Asia's sustainable fixed-income market, particularly in light of the increasingly urgent search for yield in an environment that, despite talks about monetary tightening, continues to be characterized by historically low interest rates."

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About Manulife Investment Management

Manulife Investment Management is the global wealth and asset management segment of Manulife Financial Corporation. We draw on more than a century of financial stewardship and the full resources of our parent company to serve individuals, institutions, and retirement plan members worldwide. Headquartered in Toronto, our leading capabilities in public and private markets are strengthened by an investment footprint that spans 17 markets. We complement these capabilities by providing access to a network of unaffiliated asset managers from around the world. We're committed to investing responsibly across our businesses. We develop innovative global frameworks for sustainable investing, collaboratively engage with companies in our securities portfolios, and maintain a high standard of stewardship where we own and operate assets, and we believe in supporting financial well-being through our workplace retirement plans. Today, plan sponsors around the world rely on our retirement plan administration and investment expertise to help their employees plan for, save for, and live a better retirement.

As of September 30, 2021, Manulife Investment Management's assets under management and administration, including assets managed for Manulife's other segments, totaled CAD $1.1 trillion (US $835 billion). Not all offerings are available in all jurisdictions. For additional information, please visit manulifeim.com.

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[1] Bloomberg, as of 17 January 17, 2022