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Use market churn to diversify equity portfolios

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Although risk assets have been resilient in the run-up to the 9 July deadline for the US re-evaluation of reciprocal tariffs, it would be premature to breathe a sigh of relief. The next few weeks till 1 August, when elevated tariffs are set to take effect, could remain fraught and potentially volatile. Investors would however do well to view this as an opportunity to ensure that the FX exposure of their portfolios is well-diversified. Those looking to reduce excess USD exposure in equities should consider our selection of favored equity markets and segments.

Financial markets have so far taken the tariff turbulence in their stride. Just last week the S&P 500 hit another all-time high with the USD (DXY index) also bouncing off a 40-month low and holding comfortably above that. Does that mean investors should ignore the potential for tariff escalation?

We think a little bit more caution and longer-term strategizing is warranted. The unexpected announcement of 25% of tariffs on US imports from Japan and South Korea, and subsequently a 50% tariff on US copper imports highlight the potential for unforeseen twists in how the policy environment develops. Additionally, there is the difficulty in figuring out how markets might react, and whether this reaction might turn out to be correct. Case in point: It is still hard to ascertain ahead of time just how correct the markets are in being as sanguine as they are about the potential economic damage from the announced tariffs.

An elevated level of uncertainty and volatility will be hard for investors to avoid, over the coming weeks at least. With attention likely to be on US trade policy amid the ongoing tariff tensions, our focus area of de-dollarization is likely to remain in the limelight. It might thus be advantageous for investors to be on the lookout for volatility to unearth opportunities to diversify portfolios. While we continue to recommend that investors diversify their excess USD cash holdings (mainly

to the EUR and AUD), this would also apply to excess USD exposure in equities. Below we highlight our favored options for diversifying equities allocations in portfolios.

Look for quality European equities. The quality investment style tends to work well in volatile, slow growth periods, and in the later stages of business cycles. Besides this, the European Quality style has underperformed MSCI Europe in total return terms since its relative peak in October 2020 compared to an outperformance of 2 percentage points per year on average over the last 35 years, with lower volatility. Notwithstanding a possible near-term pause in the EURUSD's 13% year-to-date rise, we continue to expect that as the most liquid alternative to the USD, the EUR is likely to remain a key beneficiary of the erosion of confidence in the USD. Also, fiscal measures in Germany and increased European defense spending will likely be supportive for the EUR. We expect the EURUSD to climb towards 1.20 by June 2026.

Tech story in Asia – Mainland China, South Korea and Taiwan. Technology remains a preferred sector across regions, with China's tech sector being a key expression of this in Asia. The risk-reward profile for China's tech sector is improving, supported by the (albeit uneven) de-escalation in Sino-US tensions, robust AI innovation, and attractive valuations. Although many of the key stocks in this sector might be denominated in HKD, they would still benefit from CNY appreciation (against both the USD and HKD) as their revenues and earnings would be largely in CNY. We thus maintain our Attractive preference on China tech despite remaining Neutral on the broader market.

We also see Taiwan's equities as Attractive and believe they are well positioned to benefit from global tech demand and capital rotation, given Taiwan's leadership in AI and technology hardware. Within Korea, we remain bullish on the memory producers and value-up beneficiaries. Tariff-related volatility might provide some buy-on-dips opportunities for some key semiconductor names in South Korea and Taiwan. These are boosted by strong structural drivers such as resilient AI capex and the ongoing monetization. Structured solutions may also offer an alternative avenue to gaining exposure amid heightened volatility. We also see further upside in both the KRW and TWD against the USD over the coming 12 months.

India and Singapore offer domestic resilience. India equities also remain Attractive in our eyes, offering resilient domestic demand and strong technology exports. On the tariff tensions, we still expect US-India tariff discussions to lead to an in-principle approval early, although a more formal agreement may only be reached around year-end or even later. Accommodative monetary policy meanwhile should also support outperformance by Indian equity markets. Case in point, the Reserve Bank of India (RBI) announced bigger-than-expected easing in June, cutting the repo rate by 50bps to 5.5% and the cash reserve ratio (CRR) by 100bps in four stages. Notwithstanding its shift to a "neutral" stance, we still see scope for another RBI cut before the year-end.

We recently upgraded Singapore equities from Neutral to Attractive as the market offers a defensive bulwark against the ongoing geopolitical uncertainty. Key positives include a stable currency, generous dividend yields, and a steady earnings outlook. Ongoing equity market reforms also provide additional catalysts in the form of an SGD 5bn capital injection and potential value-up initiatives to unlock shareholder value. We see the USDSGD moving down to 1.25 by June 2026, despite the likelihood of some near-term USD resilience.

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