BCT MARTKET OUTLOOK

As of January 2022

FED SHIFTS TO INFLATION BATTLE AND SPEEDS UP TAPER

Investment Markets	BCT's Investment Views	Summary
Equities	▬	
US	▬	We are neutral on U.S. equities. We remain selective, believing that value should be preferred but Gross Domestic Product (GDP) deceleration, rate hikes and inflation pressure balanced our view.
Europe	▬	We are neutral on European equities. Our overall stance is biased towards normalization, but we continuously assess the impact of inflation and the evolving COVID-19 situation on corporate margins beyond the short term.
Japan	▬	We are neutral on Japanese equities. This new short-term uncertainty about the new COVID-19 variant temporarily overshadowed the increasingly positive outlook for Japan, as we continue to expect a rebound in private consumption in the Q1 to drive the overall economic recovery.
Asia ex Japan	▬	We are neutral on Asian equities. Vaccination rates rise in Asia and some government will provide access for booster shots. However, some central banks have tightened policies, such as Korea and New Zealand central banks have raised interest rates.
China & HK	▼ / ▬	We are cautious on Chinese equities. We believe China presents selective opportunities, but the short term outlook is blurred by uncertainty over the extent of the slowdown in areas such as construction, regulations and policy for zero COVID-19. We are neutral on Hong Kong equities. Unemployment rate further improved to 4.1% in November, as number of COVID-19 cases were low and economic activities gradually recover. However, due to Omicron outbreak, social distance measures have tightened and hence hindered economic recovery and border re-opening process.
Global Bonds	▬	
Government Bonds	▼	We are cautious on government bonds. Recent hawkish overtures from the Fed reinforce our negative view.
Credit	▲	We remain positive on credit. In Europe, amid continued recovery and hopes of improving credit fundamentals, we believe investors should look for high-quality names.

Scales of weighting	▼	▬	▲
	Underweight	Neutral	Overweight

U.S. EQUITIES

U.S. equities rose in December in the month driven by strong corporate earnings and resilient economic growth, despite the spread of the Omicron variant contributed to slow the growth momentum and added uncertainty. Looking at December, the S&P 500 achieved an all-time high on 30th December at 4808.9 points and closed the month with a gain of +4.5%. Stocks ended the year with a +28.7% return. The U.S. unemployment rate dropped significantly in December to 3.9%, close to the pre-pandemic levels. U.S. core inflation is at its highest level since 1990, driven by strong wage growth as the labour market recovers. At the same time, the buoyant housing market is driving up house prices and rents. December U.S. Manufacturing Purchasing Managers' Index (57.7 points, down from November's 58.3) signals some moderation of activity, still at historically high levels. Central Bank: the tone of the 14th and 15th December Federal Open Market Committee (FOMC) minutes was hawkish as the Federal Reserve (Fed) recognized that inflation could continue to be higher and more persistent than what was expected and the labor market will soon reach maximum employment.

We expect real GDP growth to progressively decelerate in 2022, stabilizing above trend first and eventually converging to potential in 2023. Progressively less fiscal and monetary policy accommodation will drive this normalization. Inflation is also expected to abate, although only gradually, while remaining above 3% until summer. As transitory drivers fade, still resilient demand, rents and wage growth will help supporting core inflation at higher than pre-crisis levels. The December FOMC minutes suggest that the Fed is likely to move early and more aggressively to tighten monetary policy with a first hike in March and a quantitative tightening starting in Q3 or even earlier. The Fed will accelerate tapering in light of elevated inflation pressures and the strengthening labour market. The pace of tapering will be doubled to $30 billion per month in January, to end in March. We are neutral on U.S. equities. We remain selective, believing that value should be preferred but Gross Domestic Product (GDP) deceleration, rate hikes and inflation pressure balanced our view.

EUROPEAN EQUITIES

European equities indices rose in December the MSCI Europe posted a + 5.1% in local total return in December whilst the MSCI EMU and the Euro Stoxx 50 did relatively worse finishing the quarter with a return of +4.9% and +5.8% respectively. Inflation in the Eurozone accelerated to its highest level since the single currency was introduced in 1999. The consumer prices rose an annualized 4.9% rate in November, up from 4.1% in October and 3.4% in September, as energy costs surged. From a monetary perspective, the European Central Bank (ECB) left policy unchanged at its December meeting. It also said it would end its emergency asset purchase program in March but temporarily increased its Asset Purchase Program to smooth the transition. In Europe the Capital Market Union (CMU) is moving forward as the European Commission announced a package of measures to improve the ability of companies to raise capital across the EU.

In Europe, we believe peak growth is now past and that the impact of Omicron and some new restrictions will translate into a deceleration of sequential growth entering into 2022, further delaying the recovery in consumer spending and in the service sector, facing the headwinds of higher energy prices and supply bottlenecks. Consumers and businesses were already facing the headwinds of rising energy prices and supply bottlenecks. Inflation is also acting as a drag on domestic demand and consumption and is not yet being compensated by higher wage growth. From mid-2022 we expect the current gap between core and headline inflation to narrow with inflation stabilizing to somewhat higher than pre-crisis levels, yet within target in 2023. We are neutral on European equities. Our overall stance is biased towards normalization, but we continuously assess the impact of inflation and the evolving COVID-19 situation on corporate margins beyond the short term.

JAPANESE EQUITIES

In Japan, the Nikkei 225 declined for -2.2% in Q4, with a positive 3.49% return in December. The pace of economic recovery undermined sentiment with the Q3 GDP, released in December, below expectations (-0.8% quarter-on-quarter) and overseas coronavirus concern weighing on the markets. With the yen was generally weaker in the quarter. Japan inevitably imported its first known case of Omicron in December, but overall infection rates remain remarkably low, as they had throughout 2021. The Bank of Japan (BoJ) decided to partially extend COVID-19 supports. It will end purchases of corporate bonds and commercial paper at the end of March, but will continue to provide interest-free loans to banks aiding pandemic-hit SMEs by another six months till the end of September.

The Bank of Japan's own Tankan survey, released in December, contained no real surprises, although the overall tone was reasonably upbeat. There was some evidence of a slight pick-up in corporate inflation expectations over the next two years. Meanwhile, the current inflation rate crept back into positive territory as several one-off factors begin to drop out, but there still seems little chance of Japan experiencing a short-term inflation spike as seen elsewhere. Japan, which has been a laggard in the recovery so far and is trading at attractive relative valuations, should benefit from increased external demand as supply issues are resolved, fiscal stimulus and a weaker yen. This includes direct cash handouts to households in an effort to kick-start a consumption recovery in the first half of 2022. We are neutral on Japanese equities. This new short-term uncertainty about the new COVID-19 variant temporarily overshadowed the increasingly positive outlook for Japan, as we continue to expect a rebound in private consumption in Q1 to drive the overall economic recovery.

ASIA EX-JAPAN EQUITIES

In Asia, returns were generally positive in December. The market seems to have recovered slightly from its board market sell-off following the emergence of the Omicron, which investors had feared could derail the global economic recovery. Among the best performers, there are the Stock Exchange of Thailand (SET) (+5.7%) and the South Korea Composite Stock Price Index (KOSPI) (+4.9%) for vaccination across Asia have broadly accelerated. Followed, we have the Singaporean Straits Index also posted positive performance with a +2.7% return after its underperformance index market last month. Investors continued to track developments surrounding the new COVID-19 variant and whether existing vaccines would prove to be less effective. In Taiwan, positive economic data and a rise in exports boosted investor confidence, with chipmakers performing well hence Taiwan Stock Exchange Corporation Index (TWSE) also returned positively.

In Asia, we believe investors start to think that COVID-19 is becoming endemic. As vaccines and treatment options improve, we expect periodic sprouts in new infections across the region, with well-managed treatments and lower hospitalisation rates allowing the global economy to normalize. In Singapore, there were also fears that the government might have to scale back some recently relaxed curbs on activities. In Indonesia, its momentum is improving on the back of the recent reopening and continuous vaccination rollout. After being very subdued in 2021, inflation dynamics should trend higher in 2022, moving towards the upper part of the target. We are neutral on Asian equities. Vaccination rates rise in Asia and some government will provide access for booster shots. However, some central banks have tightened policies, such as Korea and New Zealand central banks have raised interest rates. In Australia, the Reserve Bank of Australia (RBA) has tightened prudential regulation on new mortgages. A gradual tightening of monetary policy and the slow fiscal consolidation expected.

CHINA & HONG KONG EQUITIES

In China, Shanghai Composite Index was a positive performer with a growth of +2.1% in December. Though Chinese economy continued to suffer from zero-COVID-19 policy and Chinese property developers are experiencing a tightening in financial conditions. The broad weakness in the economy has caught policymakers' attention, hence policy easing and other measures are hence on the way to stabilize growth. The Politburo meeting and the Central Economic Work Conference confirm China is moving into monetary easing and will step up policy supports at the turn of the year. Broad monetary easing is already underway with the 0.50% Required Rate of Return (RRR) cut in mid-December and a 0.05% Loan Prime Rate cut on 20 December. In Hong Kong, Hang Seng Index experienced a depreciation of -0.3%. Market sentiment was driven down due to Omicron outbreak in Hong Kong, it is believed to impeded economic activities and put Hong Kong-Shenzhen border reopening on hold again.

On policy side, we expect another 0.05% of rate cut in January. The People's Bank of China (PBoC) has increased its verbal intervention, embedded a depreciation bias in daily fixing and hiked the foreign exchange RRR slightly, to discourage RMB appreciation. However, housing sector deleveraging is most likely to continue, and we do not expect another round of big credit stimulus. We maintain our view that economic growth will rebound sequentially from its dip and then stay slightly below trend in 2022. Inflation will remain comfortably below 3%. We are cautious on Chinese equities. We believe China presents selective opportunities, but the short term outlook is blurred by uncertainty over the extent of the slowdown in areas such as construction, regulations and policy for zero COVID-19. Hence we stay watchful amid the government's desire to propagate common prosperity which should help reduce inequalities in long run. We are neutral on Hong Kong equities. Unemployment rate further improved to 4.1% in November, as number of COVID-19 cases were low and economic activities gradually recover. However, due to Omicron outbreak, social distance measures have tightened and hence hindered economic recovery and border re-opening process.

GLOBAL BONDS

Inflation has continued to surprise on the upside and the recovery in the U.S. labour market is much stronger than expected. The increase in wage is strong for low-wage sectors but generalized to all sectors. In light of the inflationary pressures, the Fed is accelerating its Quantitative Easing (QE) Reduction and longer-term interest rate expectations increased. At the same time, real rates are in very negative territory and demand for U.S. Treasuries remains very strong. At the same time, though more hawkish than expected, the ECB confirmed its much more dovish stance than the Fed and Bank of England (BoE), it will keep an open-ended QE running for all of 2022, calibrating its size to cover for most of next year's net debt issuance.

The evolution of the virus cycle, a deceleration in economic growth, and inflation will determine central banks' responses. We are cautious on government bonds. Recent hawkish overtures from the Fed reinforce our negative view, indicating a mild increase in core yields and bear steepening of the yield curve. However, we believe this will be balanced by maintenance of broad easy financial conditions and investors should stay defensive and flexible. We are cautious on the duration in Europe due to ECB's gradual QE move. We remain positive on credit. In U.S., we are cautious on long-duration IG given their potential to be affected by rising core yields. However, in Europe, amid continued recovery and hopes of improving credit fundamentals, we believe investors should look for high-quality names.

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