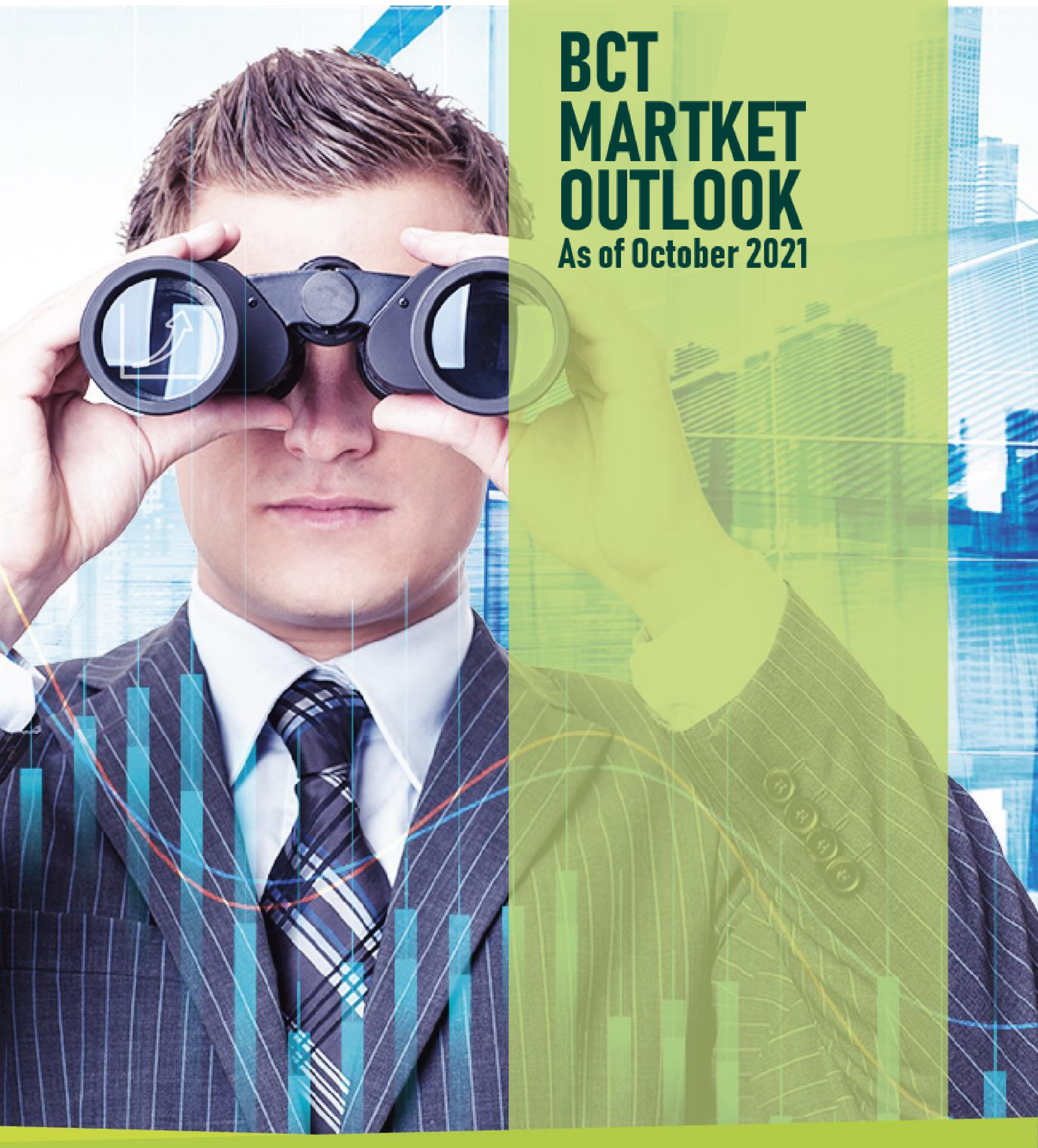
BCT MARTKET OUTLOOK

As of October 2021



THE FED IS ABOUT TO TAPER, WHILE PLAYING DOWN RATE HIKES

Investment Markets	BCT's Investment Views	Summary
Equities	▬	
US	▬	We are neutral on U.S. equities. We think the supply chain shortages and pressures on labour markets should ease later in 2021 and next year. But valuations are extreme in certain segments and hence there is an increasing need to be selective and focus on relative value.
Europe	▬	We are neutral on European equities. Europe continues to emerge from the crisis with expectations of growth peaking later this year. But inflation (energy and food) seems to be getting strong amid the transition towards clean energy.
Japan	▬	We are neutral on Japanese equities. The Bank of Japan left policies unchanged at its September monetary policy meeting, noting that some exports and production have been affected by supply-side constraints.
Asia ex Japan	▬	We are neutral on Asian equities. Purchasing Managers' Index (PMI) data across emerging market Asia rebounded. Lockdown restrictions eased. Vaccination rates across Asia have accelerated, although parts of the region continue to lag behind. Economies are gradually reopening.
China & HK	▬	We are cautious on Chinese equities. We are downgrading our growth forecasts and do not expect growth to recover to trend in Q4 2021. We are neutral on Hong Kong equities. Hong Kong property sector was hard hit as there was news that central government officials had requested Hong Kong developers to help solve the housing problem. This raises concern about more regulations and policies towards this sector.
Global Bonds	▬	
Government Bonds	▼	We are cautious on government bonds. With the recent 'less dovish' stance of CBs, U.S. and core Europe curves staying active, we maintain a steepening view as we await the peak of growth.
Credit	▲	We remain positive on credit. We believe it will rely more on selection as it offers better risk/reward profiles versus A-rated debt.

Scales of weighting	▲ Underweight	▬ Neutral	▼ Overweight

U.S. EQUITIES

September's U.S. manufacturing was 60.7 down from July's 63.4 and August's 61.1. Activity experienced a deceleration in its growth pattern although growth remained solid and dynamic. The rise in production was strong but eased due to material and labour shortages. The manufacturing sector was being affected by supply chain disruptions and input shortages, which had held back activity, as firms were unable to cope with very strong demand. During the quarter, inflation remained relatively high but momentum in U.S. inflation began decelerating with last Consumer Price Index (CPI) reading in line with expectation at 5.3% year-on-year (July 5.4%). Price indicators pointed to significant persistence of inflationary pressures: supply chain bottlenecks remained significant, the labour market was healing fast and wage growth was picking up and diffusing more broadly. In terms of monetary policy, in light of these fresh inflationary pressures, the Federal Reserve (Fed) moved to upgrade their inflation forecasts once again in September and signalled a faster taper than anticipated, which is to start in November, potentially completing the pandemic-related bond buying by June 2022. Interest rate projections rose more than the consensus expected with the Fed looking increasingly confident that it would start raising rates towards the end of 2022 or early 2023, with a pace of three to four hikes per year.

We believe there is uncertainty related to the timing and the amount of infrastructure plans and tax hikes. On the other hand, corporate margins and price pressures remain. However, economic reopening continues and real rates are still negative. Thus, while we are vigilant as the exceptional earnings performance this year will be difficult to repeat, we think this is not a time to be negative on equities. Instead, investors should look for company-specific factors and value names with a more domestic focus (such as banks) and less on cyclical value, as we highlighted earlier. In addition, we look for companies with a sustainable earnings potential and we focus on buybacks/ dividend opportunities. However, we are cautious on bond proxies and would avoid expensive growth and distressed value. We are neutral on U.S. equities. We think the supply chain shortages and pressures on labour markets should ease later in 2021 and next year. But valuations are extreme in certain segments and hence there is an increasing need to be selective and focus on relative value. Investors should also keep in mind the potential tax hikes and stay away from names that could be hurt due to regulations brought in to deal with tax avoidance.

EUROPEAN EQUITIES

The MSCI Europe was up +0.5% in local total return terms for Q3 and was down -3% in September. In Europe, inflation continued to grow in September: on a year-on-year basis, the Eurozone's consumer prices jumped +3.4% in August according to a flash estimate, up from +3% a month earlier (and +2.2 in July) and it was the highest level since September 2008. Higher energy costs were a big part of this upsurge. After a positive surprise in Q2, the Eurozone economy is expected to post another strong Q3 gross domestic product (GDP), although high-frequency indicators now point to flattering levels still below pre-crisis ones. Recovery in the service sector is still lagging, like services consumption. The Eurozone's Purchasing Managers' Index (PMI) moved from 62.8 in July to 58.6 in September, slightly lower from the earlier flash estimates of 58.7 points. Expansions were still strong, but the manufacturing growth slowdown continued in September. The drop was driven by new orders and output. From a monetary perspective, the European Central Bank (ECB) announced a slowdown in bond purchases, but in contrast to the Federal Open Market Committee (FOMC), it was keen to stress that this was not the beginning of a process of tapering purchases down to zero. The ECB is continuing its monetary support but it is recalibrating its flexible program as recovery is well underway and financing conditions have improved.

At its September meeting the ECB announced the recalibration of its pandemic emergency purchase programme for the remainder of the year, postponing to December any decision on 2022 quantitative easing. The only "moderately lower" path is likely to mean a slowdown in Q4 to higher levels than in Q1, probably close to a 70 billion euro monthly. A lower level of purchases versus Q2 and Q3's 80 billion euro would be consistent with the combination of current financing conditions and the improved macro picture. We expect the ECB to keep its dovish stance and its stimulus beyond March next year, mainly by increasing the size of asset purchase programme (APP). We stay balanced and continue to believe in economic normalisation and reopening. We think investors should look for value names, as implied expectations in these areas remain attractive. Investors should avoid distractions from short-term noise and focus on non-disrupted businesses that deliver sustainable earnings. We are neutral on European equities. Europe continues to emerge from the crisis with expectations of growth peaking later this year. But inflation (energy and food) seems to be getting strong amid the transition towards clean energy. In this environment, we reiterate the rotation towards value, but recommend investors to broaden this to include names displaying strong quality and dividend characteristics. Overall, the focus should be on selection and pricing power.

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JAPANESE EQUITIES

From a geographic perspective, Japan was among the best equity performer in September, and it saw the largest advances in Q3. In September, both indices returned great performance, with the TOPIX up +4.2% and the Nikkei up +5.4% in total return terms. In Q3, the TOPIX and the Nikkei grew +5.2% and +2.8% in total return terms respectively. The Delta variant and supply chain constraints disrupted Japan's recovery in Q3. The state of emergency has been extended, causing falls in mobility and household confidence, while the auto sector has had to cut production due to component supply bottlenecks. Inflation readings remained negative, due to the one-off rebasing and previous change in mobile phone charges. That said, the outlook has brightened up as reopening moves closer. The country is on track for a 75% full vaccination rate in October, paving the way for a lift of social distancing rules.

In terms of monetary policy, the tilt towards tightening, though, is not unanimous: we expect more inconsistency in the pipeline. The Bank of Japan (BoJ) left policies unchanged, as expected, at its September meeting, noting that exports and production have been affected by supply-side constraints. We are neutral on Japanese equities. We expect the BoJ to remain on put while other developed market (DM) central banks forge ahead with tapering later this year. It is too early for BoJ to start the discussion on policy normalisation, since Japan's economic recovery has been slower than other DMs, and inflation remains negative. It is projected to rise gradually in the medium term but is still a long way from reaching the 2% target.

ASIA EX-JAPAN EQUITIES

It was a mixed story in Asia with regional disparities in terms of overall performance. In India, the Sensex and the Nifty 50 grew respectively +2.7% and +2.8%. Indian growth is proving robust after the reopening and inflation is decelerating with dynamics returning within the central banks ranges. The Stock Exchange of Thailand (SET) rallied 8% month-on-month. Towards the end of the month, Thailand's infection rate started to decline. Vaccination rollout continues to accelerate with 450,000 doses per day, covering 33% of the population with 1 dose and 11% fully vaccinated. The Philippines Stock Exchange Index (PSEi) gained +2.4% month-on-month. In the beginning of September, daily COVID-19 cases hit a record high of 26,000, but subsequently declined towards the end of the month. More than 80% of the adult population received at least one dose. The Indonesian Jakarta Stock Price Index (JCI) recorded gains of +2.2% month-on-month. The gains were due to the strong energy sector performance. As of end September, 30% of the population received their first vaccine dose. The Singaporean Straits Times Index (STI) crept up +1% month-on-month due to the real estate sector. At the end of the month, Singapore reported record daily cases of 2,478 and the government advised senior citizens to stay at home and plan for a booster shot.

In Singapore, towards the end of September, the government implemented tighter restrictions such as reducing group gatherings, extending home based learning to 7 October and requiring work from home for at least a month. Despite the short term noise with rising daily cases, the reopening theme is still on track over the medium term. In Indonesia, as daily cases are declining, the worst is behind us. We anticipate the reopening of economic activities towards the final quarter of the year. In Thailand, it has seen fewer virus cases and has started to loosen its curbs, the recovery story remains on track as the accelerating inoculation rate is leading to easing restrictions in Thailand. In the Philippines, restrictions has relaxed as vaccination continues to roll out, together with mobility easing, the recovery theme is on track. In Malaysia, the first domestic travel bubble was launched on 16 September, while the government continues to explore other tourism spots. Vaccination rate continues to inch higher at 83.7% of the adult population. With mobility restrictions easing the recovery theme is on track moving into Q4. We are neutral on Asian equities. PMI data across emerging market Asia rebounded. Lockdown restrictions eased. Vaccination rates across Asia have accelerated, although parts of the region continue to lag behind. Economies are gradually reopening.

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CHINA & HONG KONG EQUITIES

The MSCI Hong Kong went down in September (-6.09% in USD terms, including net dividend). Hong Kong's headline CPI growth was 1.6% year-on-year in August. Hong Kong's unemployment rate dropped from 5% in August, to 4.7% as the number of COVID-19 cases was mainly low and economic activities gradually recovered. "First in / first out" applies to China, which is now facing another inflection point. The view that "2021 growth can print above 8% anyway" explains why Beijing is not backing off from regulatory tightening, notwithstanding the one-off overnight liquidity injections to preserve financial stability. From a monetary point of view, the People's Bank of China (PBoC)'s Open market operations (OMO) size to an eight-month high rolled over the Municipal Liquidity Facility (MLF) by the full amount in September and increased before the Mid-Autumn Festival. In China, growth numbers have broadly surprised on the downside in Q3, with exports being the only exception. Policy tightening, self-imposed restraints (zero tolerance COVID-19 policy and decarbonisation policies), and the global chip shortage have all contributed to the slowdown.

While the long-term outlook remains solid, we see more negative catalysts than positive ones on a six-month horizon. This would call for a prompt return to policy easing. The reserve requirement ratio (RRR) cut alone will not do much to lift growth, given the prevailing constraints on sector credit allocation and the push to lower energy intensity towards year-end, but the authorities have been reluctant to ease more. We expect policy rates to hold unchanged, coupled with targeted easing programme for small and medium-sized enterprises. We are cautious on Chinese equities. We are downgrading our growth forecasts and do not expect growth to recover to trend in Q4 2021. August's producer price index (PPI) surprised on the upside again and is likely to stay high for longer, due to supply constraints. CPI inflationary pressures remain subdued as services consumption has been hit hard. We are neutral on Hong Kong equities. The total number of vaccinations reached 8.68 million, with 4.18 million people fully vaccinated. Hong Kong property sector was hard hit as there was news that central government officials had requested Hong Kong developers to help solve the housing problem. This raises concern about more regulations and policies towards this sector.

GLOBAL BONDS

At the September FOMC meeting, Powell signalled that the reduction in asset purchases could begin as early as November, and to end the program by mid-2022. It is expected to reduce its purchases at a rate of $15 billion per month until June. In addition, median interest rate projections by FOMC members rose more than expected. It is increasingly confident that it will start raising rates towards the end of 2022 or early 2023, at a pace of three to four hikes per year. Inflation forecasts have been revised upwards. Inflation is likely to be the determining factor in the timing of the first rate hike and the pace of further rate hikes. In the ECB, the implementation of the Next Generation European Union (NGEU) plans will support above-potential growth leading to a faster recovery to pre-pandemic levels (by mid-2022). Inflation will keep rising across the Eurozone, receiving a further boost from gas and energy prices, especially as the winter season approaches. Overall, the J.P. Morgan Economic and Monetary Union Government bond indices had slightly negative returns over the quarter, as yield generally rose: both the 3-5 year Index and the 5-7 year Index fell -0.03% whilst in September the former limited the loss to -0.3% against a fall of -0.7% for the 5-7 year Index.

The macroeconomic backdrop remains positive amid strong growth figures and easy financial conditions, but we are witnessing weakening momentum in the U.S. and China. On the other hand, uncertainty remains elevated amid the above Central Banks (CBs)-target inflation, the increase in the cost of shipping, distribution bottlenecks, and pressures to 'de-globalise' supply chains. We believe it is a constructive environment to play inflation and credit with a selective approach to identify 'rising stars' amid a better default environment. We are cautious on government bonds. With the recent 'less dovish' stance of CBs, U.S. and core Europe curves staying active, we maintain a steepening view as we await the peak of growth. Euro-peripheral debt is supported by a better economic outlook, but we think political risks must be monitored. Unsurprisingly, inflation is elevated in the U.S. and Europe, even if there was some indication of a peak in the U.S. We remain positive on credit. We believe it will rely more on selection as it offers better risk/reward profiles versus A-rated debt. In addition, we play the 'compression' theme by focusing on bottom-up analysis (improving credit metrics), short-/mid-term maturity debt, and Environmental, Social, and Governance (ESG). Default outlook in credit is benign, we believe investors should avoid areas where risks are asymmetric and show a diminishing returns trend as we move across the quality spectrum.

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