BCT
銀聯集團

BCT Market Outlook

Apr 2019

Investment Markets	BCT's Investment Views
Equities	**Neutral**
US	Neutral
Europe	Neutral
Japan	Neutral
Asia ex. Japan	Neutral
China & HK	Overweight
Global Bonds	**Neutral**
Government Bonds	Neutral
Credit	Overweight

Scales of weighting: Underweight, Neutral & Overweight.

US Equities

U.S. Equities continued their expansion in March, backed by accommodative monetary policy from Central Banks, albeit on a more timid note. The Federal Reserve surprised to the upside by announcing an early end to its balance sheet roll-off by September, and lowering its "dot plot" projections for the Fed Funds rate. Lower growth and inflation projection pressured 10-year yields down, leading to an inversion of the 3-month and 10-year yield curve. On the trade front, positive declarations from China officials early in the month kept sentiment afloat. The S&P 500 posted a +1.8% return for March, while the Tech-heavy NASDAQ delivered a solid +2.6%. The Russell 2000, an index of mid- and small-caps, underperformed large-cap indices, with a negative monthly return of -2.3%. At sector level, the best performers were Real Estate (+4.9%) and Utilities (+2.9%), while cyclicals like Industrials (-1.1%) and Automotive (-3%) underperformed. The VIX Index, a measure of aversion to risk, decreased nearly 1 point from 14.8 at end-February to 13.7 at end-March, further in below-average territory.

In the U.S., the first signs of a slowdown are emerging. We are likely to be at an inflection point for the market after the strong rally in Q1. The market is exposed to deteriorating economic momentum, and to noise arising from U.S. fiscal policy, with the debate on the U.S. debt ceiling expected to resume in the short term. We could see an extension of the rally in case of improving or not further deteriorating fundamentals, or a correction in case of further earnings deceleration. Inflation should remain contained, thanks to a moderation in energy prices. An issue to pay attention to is the tight labor market, with almost all of the indicators posting stronger growth. We expect the U.S. market to continue to outperform other equity markets in terms of profit growth, even if its outperformance could slow in 2019. However, the climax of the U.S. cycle is an obstacle to a P/E ratio uptrend, so the market should perform in line with EPS growth. **We are cautiously neutral on U.S. Equities. Due to the low visibility at this stage, we take a more prudent view on the market.**

European Equities

European Equities extended their early-year gains in March, owing more to dovish monetary policy and trade relief than domestic fundamentals, with the Stoxx 600 gaining +1.7% this month. The ECB adopted a more dovish tone than expected, with a new round of TLTROs announced, as well as slashed forecast for growth and inflation, questioning the resilience of Europe's economy. Manufacturing PMIs remain in contraction territory (below 50) for the most part. On the U.K. front, Prime Minister May's deal proposal was rejected twice on March 12th and March 29th. An extended negotiation period was granted however by E.U. members, until April 12th, thus avoiding the March 29th deadline. Due to both Brexit uncertainty and the mixed economic data, the Bank of England remained on hold throughout the quarter, despite rising wage pressures. Sentiment indicators sent mixed signals in March, as Manufacturing PMIs are still in contraction territory for the most part, whereas Services PMIs seem to display more robustness. At sector level, this month's outperformers were Retail (+6.9%) and Basic Resources (+6.2%), whilst the relative underperformers were the Insurance sector (-0.2%) and the Banks Sector (-3.7%).

European equities confirmed their weak start in 2019, with below-expectations growth and external risks weighing on the economy. The outlook for inflation is benign. We believe Eurozone growth will gradually recover from its lows by the end of the year, mainly driven by household consumption, albeit not as strongly as at the end of 2017. Political uncertainty is set to remain high, with an uncertain Brexit outcome and E.U. elections, and will weigh on confidence. Another risk for European equities is potential tariffs on the Auto sector. Valuations are not discounted as they were at the beginning of the year, but they are not expensive either.

Against this backdrop, we believe that a combination of a sensible outcome of the Brexit situation coupled with the continued delivery of earnings growth is needed to justify meaningful further upside. **We remain neutral on European equity markets as valuations don't appear as discounted as earlier this year and risks remain tilted to the downside.**

Japanese Equities

Japanese Equities ended flat this month, in contrast to the continued rally in the U.S. and Europe, with the Nikkei 225 losing -0.03%, driven by small caps (-0.9% for The Nikkei Mid & Small Caps Index). In sector terms(1), Real Estate (+6.9%), Information Technology (+3.4%) and Industrials (+1.7%) were the best performers, while Energy (-4.16%) and Healthcare (-3.4%) underperformed. Although three quarters of corporate executives worry about the state of the Chinese economy, exports to, and machine-tool orders from, China have recently bottomed out. Exports in general remain precarious. Yet, shipments to the U.S. continue to grow while those to the E.U. are surprisingly resilient. On the domestic economy front, the government is accelerating disaster restoration projects, infrastructure investment and urban development for the 2020 Tokyo Olympic Games.

Macroeconomic data is highlighting dampened domestic demand on the back of weaker exports. The economy is also suffering from global economic deceleration, which is impacting primarily the corporate sector. In the meantime, the government revealed a blueprint for economic stimulus, showing a strong determination to avoid any setback in the economy. Japanese equity market participants remain extremely cautious of a potential global economic slowdown, trade disputes and rising operating costs. Downward revision in earnings estimate has outnumbered upward revision since last September. The median forecast of recurring profits for FY18 is now submerging 7% YoY. **We have moved our stance on Japan back to neutral. Should there be no resolution in the U.S./China trade negotiations, the Japanese market could underperform due to a strengthening Yen, which usually acts as a safe-haven asset.**

Asia ex Japan Equities

Asian equities performed well on more than expected dovish Fed, positive news around trade talks and China's fresh stimulus, with MSCI Asia Pacific ex Japan posting +1.3% return for March. India (+9.2%) was the best performing market, supported by several drivers: positive macro variables (benign inflation, accommodative monetary policy), dissipating uncertainties around the upcoming National Elections, as a Modi-led National Democratic Alliance (NDA) government looks like the most likely outcome, a better trend on earnings consensus and strong net equity inflows from foreign investors, while Korea was hit again (-3.1%) on the back of a disappointing earnings season amidst the global growth slowdown. The full set of GDP releases for Q4 2018 confirmed some resilience in the region, driven mainly by domestic demand. The first two months of 2019 confirmed very weak export dynamics across the region. The region's inflation figures remained very benign. Oil and food prices pushed inflation to levels lower than expected. In the Philippines, February inflation finally went down within the Bangko Sentral ng Pilipinas' (BSP) range, at 3.8% YoY. Overall, CBs in the region are in a wait-and-see mode before shifting towards a more dovish stance, thanks to a more favorable global financial environment. India cut its policy rates by 0.25%. In Thailand, House of Representatives elections have been held. 95% of the votes have been counted, while the remaining 5% is under investigation for irregularities. Currently, no parties or alliances (as per the information available) have any majority. Final results will be announced after the 9th of May.

Overall, our main scenario remains that growth should stabilize in the region, while expected earnings look reasonable and achievable. We continue to think that improvement in capital expenditure discipline, the lack of major macroeconomic imbalances and increasing pay-out ratio, should help reduce economic and profit volatility. Potential headwinds such as a strong US dollar and deteriorating US-China trade relations have eased and might support additional growth for equities. We suggest a more cautious stance on countries with higher valuations and political risk (like Thailand, with the upcoming elections, and valuations that are not as discounted as they were before 1Q rally). From a fundamental perspective, earnings per share growth consensus expectations stabilized later in the month. Earnings revisions are bottoming out. The focus continues to be on stock picking, as valuation dispersion remains significant. **We are neutral on Asia ex-Japan. Even though we remain constructive on this asset class, we see a pause in the upside in the short term.**

China & Hong Kong Equities

Picking up on their year-to-date momentum, Chinese Equities are posting strong returns for the month, with the Shanghai Composite Index gaining +5.1% and Hong Kong's Hang Seng up +1.5%. Investors also welcomed an above expectations Manufacturing PMI index for February (49.9 vs 48.5) and the announcements that accompanied the National People's Assembly. Positive feedback on trade negotiations between US representatives and Chinese Vice Premier Liu He pushed up risk assets over. This was by offset in part by rising tensions in some emerging countries with current account deficits and underwhelming imports in March. The authorities have formalized GDP growth targets for 2019, between 6% and 6.5%, a slight decline from the +6.6% in 2018. They also announced a fiscal stimulus plan with tax cuts representing just over 2% of estimated GDP for 2019. The budget deficit will rise from 2.6% of GDP in 2018 to 2.8% this year. Beijing has also confirmed its desire to further open its markets to international players.

Overall economic activity looks to slow further in Q1, while policymakers have reaffirmed their supportive stance. The annual National People's Congress (NPC) sent a clear signal that growth is the top priority this year. The fiscal package came out larger than widely expected, with confirmation of a meaningful corporate VAT cut and heavier issuance of local government special bonds. While exports are suffering and the property sector is softening, drag from the Auto sector is becoming smaller, and the state has begun stabilization efforts, helped by policy supports. Overall credit growth seems to be bottoming out. U.S./China trade negotiations remain a key uncertainty. Recent signs have shown meaningful progress, with planned tariff increases being postponed for now. Stress in RMB and capital outflows have remained under control, helped by a more dovish Fed and a softer dollar, as well as improving market sentiment. We therefore see an unchanged RMB on a 12-month horizon, as the currency appears fairly valued, with low risk-adjusted carry. **We are positive on China & Hong Kong, as valuations still stand at attractive levels and a trade deal looks more likely after recent positive developments.**

Global Bonds

With economic data still coming in relatively weak, the bond market enjoyed a great month in March with significant falls in yields in most global markets, leading to positive returns over the quarter. The U.S. curve (10-year minus 3-month) inverted in March, sending out a signal that a US recession could be a reality in 12 months' time. In European fixed income markets, it was much the same story, but with less action at the short end of the yield curve compared to the U.S. Increasing signs of slowing growth in Europe were evident in lower PMI's and other economic data, whilst inflation remains a problem for the ECB – headline inflation fell from 1.5% to 1.4% and core inflation fell from 0.9 to 0.8%, and is stubbornly showing no signs of accelerating. German 2-year yields actually rose 0.01% to -0.61%, 10-year yields fell 0.31% to -0.08% and 30-year yields also fell 0.3% to 0.57%. The spread between 10-year German Bunds and 10-year Italian BTP's was quite volatile, spiking in early February to a high of 2.87% before falling back to a low of 2.37% in mid-March. The JPM Emerging Markets Bond Index had a great quarter, appreciating 6.16% as investors embraced the asset class against the backdrop of the U.S. central bank signaling that interest rates are on hold. Although credit markets also participated in the on-going "risk-on" mood in Q1, there has been some fatigue setting during March.

The Federal Open Market Committee paused its policy rate normalization process (we don't expect any interest hike this year) and is messaging patience and data dependence with respect to future policy rate moves. We expect the Fed will conclude the balance sheet normalization by the end of the third quarter, which would be earlier than the market is expecting. At current valuations, investors should be more cautious on U.S. bonds. Euro fixed income received strong support from the ECB's new accommodative measures. This should benefit the peripheral bond market, favored in the search of income. We maintain a slightly short duration view in Europe. E.U. credit (peripheral financials in particular) is the main beneficiary of the new TLTRO round. We still see room for spread compression, as the search for yield will be particularly aggressive in Europe. In U.S. credit, given the recent spread tightening, we have become more cautious regarding IG corporates. Although EM momentum has recently deteriorated, the continued dovish stance by the world's major CBs might still play in favor of EM debt markets. Nonetheless, we keep a watchful eye on any negative surprise. We remain constructive on EM hard currency debt and we tend to favor those countries with cheap valuations. On EM bonds in local currency, we expect extra-carry returns from high-yield countries (Indonesia). **Overall, we are Neutral on Government Bonds (Neutral on U.S. and European Treasuries), and Positive on Credit (Positive on EM and European Credit, and Neutral on U.S. Credit) i.e. Neutral on Global Bonds.**

[(1)] Sectors of the S&P 500 (U.S. Equities), Stoxx 600 (European Equities, Topix (Japanese Equities), MSCI China (Chinese Equities) indices.

Investment involves risks. Past performance is not indicative of future performance. The value of constituent funds may fall as well as rise. For further information about the risks involved, please refer to the principal brochure of BCT (MPF) Pro Choice and BCT (MPF) Industry Choice.
The information contained in this document is provided for information purpose only and does not constitute any solicitation and offering of investment products. Potential investors should be aware that such investments involve market risk and should be regarded as long-term investments.

"BCT"	– BCT Financial Limited (Plan Sponsor) – Bank Consortium Trust Company Limited (Trustee & Administrator)

Issued by BCT Financial Limited
The content of this Market Outlook is contributed by Amundi Hong Kong Limited.