BCT
銀聯集團

BCT Market Outlook

As of Jul 2019

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

Scales of weighting: Underweight, Neutral & Overweight.

US Equities

After bad performances during the previous month, US shares gained and the S&P 500 set a new record high at 2,941.76 (+7.1% in June). The outcome of the G20 Summit was a little more favorable than expected: negotiations would resume without a new deadline (that could have crystallized tensions again in the near future) and the tail risks of an escalation in tariff was averted in the short-term. However the truce did not represent a game changer. The most complex issues (intellectual property rights and technology transfers) were not addressed at the G20. The confrontation between the US and China will therefore return to the forefront sooner or later, the prevalent protectionism will not disappear from the radar screens. The end result in markets during June was a uniform rebound, with 7.5% increase on the NASDAQ Composite Index. The Russell 2000, an index of mid- and small-caps, was in line with the performance of large-cap indices, with a monthly return of 7.1%. At sector level (1), Materials, Energy, and IT outperformed (respectively +11.7%, +9.3% and +9.1%) and recovered their loss of June while Utilities and Healthcare were the month's underperformers (respectively -2.1% and -1.2%). The VIX Index, a measure of aversion to risk, slowed down to stabilize around 16, reflecting the end of the stress on markets from May.

The equity rally was capped early in May on renewed concerns about US tariffs, but after the pullback, the equity market quickly recovered, staying close to all-time highs. Earnings downgrades have no reason to stop, in line with some global growth moderation. So the outlook for the market is broadly unchanged. There are stock-specific opportunities in quality and growth. We see value in companies linked to infrastructure/cloud/data center and selective Financials such as insurance brokers, auto and home insurance. In order to have a strong performance in the value sector, we need reflationary conditions which are not visible in the current phase in the cycle. Among our strongest convictions, we believe that “bond proxies” stocks are extremely overvalued (e.g. Consumer Staples and Utilities stocks). Healthcare sector still provides a stable profit outlook at far lower valuations than bond proxies. **We remain cautiously neutral on US equities after the strong year-to-date rally, with sector/stock selection being the main strategy to approach the market.**

European Equities

European equity markets made strong gains in June as investors remained hopeful that the US President, Donald Trump, and the Chinese President, Xi Jinping, would move closer to a trade deal at the G20 Summit. The Purchasing Managers' Index (PMI) hit a seven-month high in June at 52.1. A PMI of above 50 suggests economic expansion. Growth was driven by the Services component which saw its sharpest rise since the end of 2018. In the UK, Theresa May resigned as the leader of the Conservative Party and therefore as the UK prime minister, taking a caretaker role as of 7 June. The Conservative Party began the process of selecting its new leader, who will also become prime minister. The Euro Stoxx 600 delivered +4.5% this month. At country level, the MIB of Italy was the biggest winner (+7.5%). France and the UK shares also performed well with increases of the CAC 40 at 6.8% and the FTSE 100 at 4.0%. At sector level (1), Basic Resources (+9.5%), Chemicals (+8.4%) and Auto (+7.3%) outperformed, while Real Estate (-3.4%) underperformed.

European equities could offer interesting entry points after the European Union elections, should the economic outlook improves in the second half of the year and domestic demand remains resilient, as we expect. The current features of the market (increasing valuations dispersion and lower sectoral correlation) fit a stock picking approach. We continue to see selective opportunities in the cyclical part of the market (but with less conviction than one month ago), while the defensive part is expensive. We like high-quality Industrials with strong balance sheets, some of which discount very negative outlooks, and we see opportunities in Healthcare as well. On Banks, we believe a cyclical rebound has to be confirmed to see a convincing repricing opportunity. **We are neutral on European equities. Geopolitical factor could ease somewhat, with the EU election behind us. Valuations are attractive. Potential market entry points could materialize in the coming weeks in the market.**

Japanese Equities

Japanese equity market rose during the month of June with a total return of 3.4% for the Nikkei 225. Global macroeconomic and political factors were again dominant. In sector level (1), almost all sectors were positive, with Materials on the top (+7.2%) and only one negative sector: Utilities (-2.1%). The Yen strengthened against other major currencies, reflecting its perceived safe haven status, which tended to add downward pressure on equity prices. Economic data was mixed, with the largest positive surprise coming in real GDP growth for the first quarter of 2019. This showed that real GDP grew at an annualized rate of 2.1% during the quarter when consensus expectations were for a decline. Macroeconomic indicators for the period, however, were mixed with consumer price inflation lower in May, as was manufacturing in June.

We continue to maintain a neutral stance on Japanese equities, where conflicting factors are at play: The earnings momentum for Japanese equity indexes are weak compared to the world stock indexes; Yen is not so supportive for the equity at the moment: the stock market benefits from a weaker Yen, but the uncertainty of global growth, plus risks on the trade side, could lead to some strengthening of the currency. Among the supporting factors, valuations are attractive on historical basis and relative to other developed markets. Also if the hike of the value added tax planned for October this year was postponed in the last minute (after the Senate election on 21 July at the earliest), we could see a positive market reaction. However, the main reason to postpone would probably be worsening of the ongoing international manufacturing. In other words, this argument may be positive for the Yen and indirectly weigh on the Japanese market. **We are neutral on Japanese equities. Opportunities could be found at the stock picking level.**

Asia ex Japan Equities

The MSCI Asia ex Japan Index recovered (+6.4%) in June as trade talks between the US and China restarted after the Chinese President, Xi Jinping, and the US President, Donald Trump, held a meeting at the G20 Summit in Osaka. Most countries ended up in strong positive performance, with the exception of flattish India (-0.5%). Thailand (+6.8%) and Singapore (+6.5%) were the key performers. Cyclical sectors were the best performers (Consumer Discretionary and Communication Services) while Defensives (Healthcare and Energy), relatively lagged. In Thailand, the strong rally in equities was driven by the reduction of political risk sentiment, with the news that the new government would be ready by mid-July, policy support optimism and light investor positioning. Indian equities saw a small correction after hitting all-time highs in early June, as investor focus shifted from the Modi Government victory to upcoming events like the Union Budget and high-frequency economic growth indicators. The region's inflation figures have remained very benign. Food prices have been pushing up the cost of living quite broadly on the back of agricultural products prices, which have increased lately. Having said that, the Central Bank's targets are not at risk for the time being.

Valuations are still close to fair value, but the positive upside at 12 months horizon disappears due to the positive performance in June. Selectivity is the key. We see, for the next 12 months, a stabilization of earnings growth for emerging Asian markets close to 5%, which is higher than global emerging markets level (2.5%). Earnings revisions are still negative and recent recovery vanished. We saw further deterioration in revisions in Asia. We prefer to be selective about stocks. Some themes are at play: the dividend per share growth increased strongly in global equity market and is expected to further improve. Dividend yield and dividend per share growth expectations can be two good factors to play in a late cycle scenario. These two factors are particularly supportive for some countries like India. Other than that, we still think that China and domestic stories in Asia are attractive. China is going to accelerate fiscal and monetary stimulus and this can be particularly positive for all the areas. But if the trade talks further derail in the coming weeks, we will prefer to play some domestic and insulated stories (like the Philippines and India). **We remain slightly positive on Asia ex Japan equities, given that some domestic demand growth stories are attractive as defensive plays. The evolution of the trade talks will be crucial, not only for China but also markets which are closely linked to the global cycle and, among them, some relevant Asian markets such as Korea and Taiwan.**

China & Hong Kong Equities

Chinese equities gained (+8.0% on the MSCI China Index) on positive trade news while the central government indicated its ongoing support for the domestic market. The People's Bank of China stated that it injected approximately US$108 billion into the market in June to maintain liquidity in the banking system at a "reasonably sufficient level" whereas the Ministry of Finance issued new measures aimed at speeding up infrastructure spending. Macroeconomic data was mixed, Purchasing Managers' Index – a figure that represents current and future business conditions, stayed flat in June with the previous month at 49.4 and retail sales in May were up 2.1% month-on-month. MSCI Hong Kong Index went up in June (+7.0% in US$ terms, including net dividend). The best performing sector were Financials (+11.0%) and Consumer Discretionary (+8.3%). Prices on food and housing remained the key drivers, rising 6.5% and 4.2% respectively. Prices on utilities, durable goods and clothing/footwear stayed sluggish and fell 4.9%, 2.0% and 1.2% respectively.

The Chinese government has multiplied monetary and fiscal stimulus measures over last year, which has helped cushion the shock related to the slowdown in global trade. Negotiations between China and the US will resume following the G20 Summit in Osaka. There is some good news (absence of a deadline and suspension of the prohibition on US companies continuing to provide Huawei). The pressure on global value chains should therefore subside, particularly in the Technology Sector. However, tensions set to return to centre stage sooner or later with regard to strategic issues (intellectual property rights and technology transfer), on which no progress has been made. **We are positive on Chinese equities. We think China's economy could hold up better than last year, as policymakers are better prepared, and local sentiment looks less fragile.**

Global Bonds

During June, the US Federal Reserve reaffirmed its recent dovish pivot (by not increasing interest rates) and opened the door to interest rates cut (potentially as early as July). Meanwhile, the President of European Central Bank (ECB), Mario Draghi, suggested that the ECB might be ready to restart quantitative easing (QE) as it seeks to stimulate the Eurozone economy. As markets responded to these developments, many parts of the corporate bond market had their best month of returns so far this year. The Euro-denominated investment grade market had its best monthly return since July 2016. To some extent, this strong performance reflected an expectation that any resumption of QE by the ECB would include corporate bond purchases. The other key driver of market sentiment was an announcement early in the month that the US would not impose tariffs on imports from Mexico. This reversal of Trumps' unexpected tariff threat provided strong support for bonds.

The scenario of moderate growth and dovish central banks remains supportive for fixed income, in particular for bonds which provide investors with an income – i.e. corporates and emerging market (EM) bonds. However, as these markets are no longer cheap, it is important to "optimize" the carry opportunities across the board (EM debt hard currency, EU investment grade, US corporates that are less exposed to trade disputes). We expect US Treasuries to continue to protect portfolios in case of escalations of trade tensions and other geopolitical risks (resurfacing frictions around the Iran nuclear deal could impact the oil outlook). The price for safe assets is high, with the 10-year US Treasury yield below 2.3% (10-year German Bund yield in negative territory), but it will likely to remain so, as there is strong demand for safe assets and scarce supply. **As we expect the US dollar to stay around current levels in the short term, non US investors could consider gaining exposure to this source of protection and liquidity without a full currency hedging. On credit, we believe that the current dovish central banks' environment still favours credit to exploit the carry but a careful attitude is required. This means investing in quality and focus on favourable fundamentals. We are neutral on government bonds and slightly positive on corporate credit.**

(1) Sectors of the S&P 500 (US Equities), Stoxx 600 (European Equities, Nikkei 225 (Japanese Equities), MSCI China (Chinese Equities) indices.

"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.