2nd Quarter 2023

BEA Asset Navigator

Investment Themes

Recession becomes the global main investment theme

- Rate hike cycle of developed markets will approach its end, and a recession would become the main investment theme among global investors.
- This is not a doomsday scenario but a mild slowdown in the US economy under analysis. The downturn is likely to be higher than minus 1% with a reversal in Q2 to Q3 GDP figures.
- A low-double-digit decline in the US equity market is highly expected, and the IG US bond market may outperform under risk aversion.
- An equity index portfolio is not a good strategy to diversify recession risk in the record, but a balanced portfolio would perform much better.

Sino-US conflict would escalate, and decoupling in different segments is inevitable

- Geopolitical risk in the NE Asia region is escalating, and decoupling between the US and China would accelerate.
- Financial decoupling becomes the key risk in this conflict, in terms of potential delisting, investment ban, and termination of business in the US.
- Tech decoupling will stimulate competition on hardware, from chips to high-tech devices. Fiscal and monetary supports by the government will create potential benefits for both markets but in separated mode.
- Monetary policy divergence between the US and China would polarize the performance of the property market in the US and China. The key risk in the property market is likely expected to be in the commercial or office segment.

"East over West" hypothesis supports and leads by US and China GDP trends

- Official GDP forecasts in China and the US are 5 and 0.4%, respectively, which show the divergence of economic trends between China and the US.
- Arbitrage in fiscal and monetary policies between the two countries provides good investment opportunities in major investment markets.
- Fragmentation and correspondent capital decoupling would apply amid different international groups or organizations, e.g., EU, ASEAN and G7.
- Segregation of capital between regions is one of the key methods of risk diversification under global risk aversion.

Asset Class Overview

↑ Outperform → Neutral ↓ Underperform

Asset Class	Quarterly View	Commentary
Equities		
United States	→	Recession risk is escalating, and defensive stocks will outperform cyclical stocks. A downturn in Q3 earnings forecast will trigger a correction.
Europe	↓	Stagflation is the major risk that could trigger a revaluation of the index. Liquidity may be "tighter for longer" in the US, eroding risk appetite.
Asian ex-Japan	→	The Sino-US conflict increases economic tension in regions. NE Asia's performance would be mixed while the SE Asia has a better prospect.
China	↑	China's reopening heats up economic recovery. Stimulus in fiscal and monetary policies is highly expected, and policy-driven cyclical stocks may be hot picks.
Hong Kong	→	One of the core conflicts between the US and China is financial and currency threats. China-related stocks will outperform the index.
Bonds		
US Government	→	The softening of yield inversion would push up the 10-year treasury yield, and the 25-bps hike in May has already been priced in the market.
USD Investment-grade	↑	Risk aversion due to recession risk is buoying. The end of the current rate hike cycle is highly expected, and capital inflows support these facts.
Global High-yield	↓	Credit risk surged since the banking crisis in US and EU markets. The next epicenter would be expected in HY categories. CDS points north as well.
US High-yield	→	Economic figures defy the downturn sentiment. Investors are cautious about liquidity status. The buoying of CDS implies default risk should not be ignored.
Asian Pacific Investment-grade	↑	Benefit of China's economic recovery and expectation on the end of rate hike cycle in developed markets, along with higher-than-average yield levels and lower-than-average CDS support the current uptrend.
FX		
AUD	↑	China's economic rebound and rising iron ore prices will drive the Australian dollar higher.
NZD	↑	Persistent inflation despite rate hikes calls for a firm stance on raising rates, which will help the New Zealand dollar continue to rise.
EUR	↑	The European Central Bank is expected to continue raising rates to suppress inflation, which is likely to maintain a strong view for the euro.
GBP	↑	It is not easy for the UK to escape from stagflation, but if the US dollar is weakening, it will benefit the pound.
JPY	→	The BOJ is unlikely to raise rates in the short term, but if other central banks slow down their rate hikes, it will be favorable for the performance of the yen.
CNH	↑	Stable economic prospects after the pandemic and narrowing interest rate differentials are expected to give the renminbi an advantage.

Important Note:

Quarterly view of each asset class is benchmarked against a corresponding proxy index

Asset Class	Benchmark	Asset Class	Proxy Index	Threshold*	Asset Class	Proxy Index	Threshold*
Equities	MSCI World	US	S&P500	1.1%	China	CSI300	4.3%
		Europe	STOXX Europe 600	1.6%	Hong Kong	Hang Seng	3.3%
		Asian ex-Japan	MSCI Asia ex Japan	2.8%			
Bonds	Bloomberg Global Aggregate Bond	US Government	US Gov't/Credit	0.8%	US High-yield	US Corporate High-yield	1.5%
		USD Investment-grade	US Corporate	0.8%	Asian-Pacific Investment-grade	Asian-Pacific Aggregate	0.9%
		Global High-yield	Global High-yield	1.8%			
FX	US Fed Trade Weighted Advanced Foreign Economies	AUD	AUD/USD	2.8%	GBP	GBP/USD	2.7%
		NZD	NZD/USD	3.2%	JPY	JPY/USD	3.1%
		EUR	EUR/USD	4.0%	CNH	CNH/USD	2.2%

* **Outperform:** Quarterly performance of proxy index is higher than the positive threshold percentage of corresponding benchmark; **Neutral:** Quarterly performance of proxy index within the positive and negative threshold percentages of corresponding benchmark; **Underperform:** Quarterly performance of proxy index is lower than the negative threshold percentage of corresponding benchmark.