BEA 東亞銀行 | PRIVATE BANKING 私人銀行

4th Quarter 2022

BEA Asset Navigator

Investment Themes

Strong US dollar is the number one factor affecting the performance of all asset classes

- Core CPI is much higher than the Fed's 2% target, which points to another potential 50 to 75 basis points interest rate hike coming in Nov and Dec. The pace and scale of rate hikes by the Fed is overwhelming other central banks, which means the US dollar is expected to remain strong this quarter.
- Growing foreign exchange risk is affecting non-US denominated bond prices, while rising credit default swap (CDS) indexes also reflect the fact that the risk of defaults is likely to trigger another round of selloffs in the bond markets, especially in Europe.
- Overly strong US dollar is dampening investor demand for riskier assets, e.g. equities, derivatives, and commodities.

Global recession risk replaces the pandemic as a leading role in the investment world

- The end of COVID is in sight, as indicated by the WHO in September. The release of pent-up demand as conditions return to normalcy is still the key driver in many economies, although the impact is diminishing with time.
- However, investors now expect a global recession, starting in the first half of next year. Risk averse strategies are the norm for this quarter, i.e. decreasing portfolio risk, increasing cash holdings, underweighting cyclical assets, overweighting defensive assets, etc.
- A technical rebound in risky assets can be expected after a major selloff, especially in the equity markets. Important to be nimble and decisive, because this opportunity will only be available for a limited time.

Political developments in the US and China will impact investment sentiment in the near term

- The US midterm elections will be held on 8th Nov, and the result will determine the political balance of power for the second half of the Biden administration. The stock market tends to perform well during midterms despite the uncertainty.
- Xi Jinping is set to have his third presidency term confirmed at the twentieth National Congress of the Chinese Communist Party (NCCCP). Investors are paying great attention to likely appointments and policy directions. The policy-driven economic momentum will lead to a shifting of investment between various sectors in Hong Kong and the A-share market.
- Geopolitical tensions will continue to change the global investment landscape in the long run, especially for northeast Asia.

Asset Class Overview

↑ Outperform → Neutral ↓ Underperform

Asset Class	Quarterly View	Commentary
Equities		
United States	↑	Indexes have yet to price in the rate hike effect and potential recession. Technical rebound is an optimistic scenario, with around a 10% upside.
Europe	→	Energy consumption this winter, rather than fuel supply, will be the key factor determining whether a potential recession becomes reality.
Asian ex-Japan	↓	Strong USD is absorbing liquidity in Asia, undermining economic growth and the equity market. It is still questionable whether China's economy has returned to normal.
China	↓	Economic policy of China's new politburo after the twentieth NCCCP is a key factor determining sentiment. Disappointed investors are still looking for signs of normalcy.
Hong Kong	↓	Sectors closely correlated with China's economy cannot benefit from the reopening policy and new policy address. Tech sector performance will be driven by the indexes.
Bonds		
US Government	→	Pressure of potential rate hikes is offset by risk-averse demand for US govt. bonds. Key factor going forward will be the frequency of rate hikes.
USD Investment-grade	→	Credit spread of investment-grade bonds is improving, but the downturn is clouding market sentiment regarding cyclical sectors.
Global High-yield	→	CDS rate for EU high-yield bonds is approaching that of the European Debt Crisis, but a big selloff can lead to a short-lived technical rebound.
US High-yield	↑	Credit spread for high-yield bonds is improving due to potential risk appetite in the equity market. Strong US dollar is also attracting liquidity from overseas.
Asian Pacific Investment-grade	↓	Surging CDS rate reflects a significant risk of defaults in Asia compared to previous quarters. Strong USD is another risk factor.
Commodities		
Gold	↓	Gold prices are being boosted by geopolitical tensions but cooled by rate hikes – forecast to hover within a 10% range of $1,700 per ounce.
Crude Oil	↑	Supply cuts by OPEC+ have been overridden by plummeting demand amid a looming recession, natural gas shortages, and the US's replenishment of its energy reserves.
FX		
AUD	→	Commodity prices are driving Australia's export economy and boosting the overall performance of the AUD.
NZD	→	RBNZ's hawkish stance on interest rate hikes and stable export prices for dairy products may help the NZD to stay resilient.
EUR	↓	Economic woes and the potential energy crisis in the eurozone may lead to a recession, which will weigh on the EUR.
GBP	↓	High inflation and economic weakness in the UK, together with policy uncertainty from the new government, will put the GBP under pressure.
JPY	↓	Government intervention has failed to reverse the weakness of JPY. The currency will fall further as long as the BOJ sticks to a loose monetary policy.
CNH	↓	Repeated Covid outbreaks in China will lead to continuous economic weakness, putting pressure on the RMB in the short term.

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%
		US Investment-grade	US Corporate	0.8%	Asian-Pacific Investment-grade	Asian-Pacific Aggregate	0.9%
		Global High-yield	Global High-yield	1.8%			
Commodities	S&P Goldman Sachs Commodity	Gold	Spot Gold	4.1%	Crude Oil	WTI Futures	2.8%
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%

* A quarterly figure within the threshold positive and negative percentages is rated as "neutral". A figure over the threshold is rated "outperformance", while a figure under the threshold is an "underperformance".