INVESTMENT INSIGHT JAN 2022

Investment Services Department

Altruist Financial Group Limited
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LIVING WITH VIRUS & INFLATION IN 2022

2021 Q4 MARKET HIGHLIGHTS

- *The Covid-19 Omicron variant is promptly spreading around the world, the global daily new infected cases climb to a new high.*
- *Escalating inflation now is a global phenomenon.*
- *While the U.S. and European equities rallied in 2021, the Hong Kong Heng Seng Index and Heng Seng China Enterprise Index were the 2 worst performing major global stock market indexes.*

On 26 November, the World Health Organization named a new Covid-19 variant as Omicron. Since then, the Omicron variant has been spreading around the world and the global daily new infected cases promptly surged to pandemic high again. However, the outbreak did not affect the overall investment sentiment of the global stock markets. Mainly contributed by the strong performance of U.S. and European equities, the MSCI World index closed at near record high level at the end of 2021 and gained over 22% for the full year. Unlike the bullish momentum in the Western world, the Hong Kong stock markets were at the darkest period in recent years, the Heng Seng Index and Heng Seng China Enterprise Index even were the 2 worst performing major global stock market indexes in 2021.

2021 was a bumper year for many investors as investment trends were obvious. By only getting rid of Chinese and Hong Kong stocks and bond markets, investors had a big chance to achieve a considerable investment return. Looking forward in 2022, the global investment markets may become more complicated since many uncertainties arose after a strong economic rebound in 2021 and perhaps the market trends and concerns listed below may have big impact towards the future investment direction.

WHAT TO WATCH IN 2022?

ESCALATING INFLATION AND THE SHIFT OF CENTRAL BANK MONETARY POLICIES

Escalating inflation and the shift of monetary policy of major global central banks are the major threats to the investment markets in 2022. Because of supply chain disruption and rebound of demand after substantial fiscal and monetary stimulus, inflation is escalating globally. The inflation rate in the U.S. surges to 40-year high and it is at the record high level in the Eurozone as well. The problem in the emerging world is even more serious. Like Turkey, the annual inflation rate has soared to 36%. To counter the accelerating inflation, the U.S. Federal Reserve ("Fed") has announced a faster pace of tapering in December and interest rate hike will likely happen earlier than previous projections. The shift of monetary policy of major global central banks is almost certain in 2022, but if inflation keeps on soaring, they may inevitably adopt more aggressive measures. It will be a dilemma over how to tighten monetary policy and slow down inflation without killing off the vulnerable global economic recovery. Besides, a rising interest rate will cause the bond yields move up which is unfavorable to those risky assets.

COVID-19 VARIANT

It seems that the pandemic is far from over. The Omicron variant has driven daily new Covid-19 infected cases to record high in many different countries and it is difficult to rule out more virus variants. Even though vaccination can avoid serious illnesses and we gradually get used to live with the virus, the wide spreading of the virus still affects economic activities in different aspects and increases economic downside risk.

GROWING U.S.- CHINA TENSIONS

The relationship between the U.S. and China has deteriorated in recent years as both countries have conflicts in different areas including economics, politics, technology, military and etc. Since they are the two biggest economies in the world, their policy directions would have big impacts to the rest of the world. Looking ahead, it is anticipated that the U.S.- China tensions are hard to ease and changes in the relationship between the two countries also increase volatility to global investment markets.

HIGH VALUATION OF U.S. STOCK MARKET

The U.S. S&P 500 and Nasdaq Composite Index have climbed 130% and 118% respectively since the pandemic low in March 2020. The valuation of those big-name companies is skyrocketing. Take APPLE as an example, its market capitalization has surpassed USD 3 trillion which is roughly equal to the gross domestic product of Britain or India. Although those companies still have good earning prospects, their high valuations may easily trigger market correction if any unfavorable event occurs.

THE CHINESE GOVERNMENT POLICY

In 2021, new regulations and more stringent monitoring imposed by the Chinese Government for sectors ranging from property development, gaming and entertainment, technology to education bought a huge volatility to the investment markets. Looking ahead, the Chinese Government policy will still be the market focus in 2022. It is obvious that "Common Prosperity" which aims at reducing the inequality between the rich and poor and creating a more balanced type of economic growth would be the most important objective of the country in the coming years. Besides, since the Chinese economy is now facing the risk of economic slowdown after a sharp rebound in the first half of 2021, unlike the U.S., it is expected that the People's Bank of China ("PBoC") will impose a looser monetary policy this year so as to create a more stable economic environment. In addition, investors should also pay attention to the 20th National Congress of the Chinese Communist Party which will be held in Autumn this year as it will determine the new Chinese Government leadership in the next 5 years.

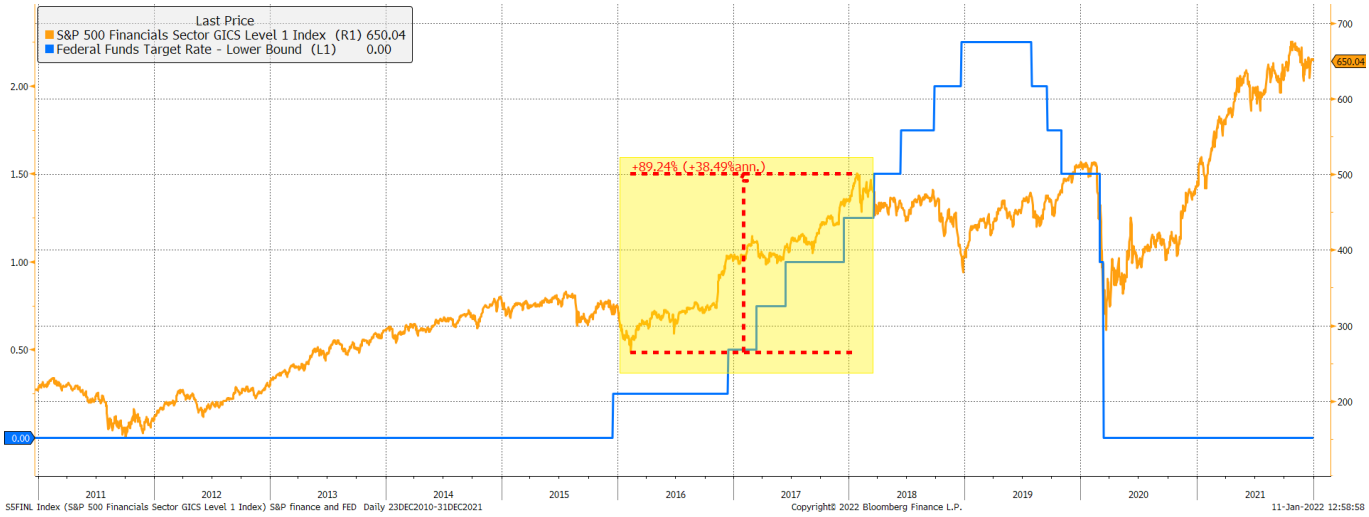
SAME GOAL OF COMBATING CLIMATE CHANGE

Despite of the conflicts between the U.S. and China, to combat climate change is their common goal. The U.S. and China currently target to achieve carbon neutrality in 2050 and 2060 respectively. In the coming decades, it is believed that there would be a strong demand on the development renewable energy, energy saving and other related sectors in order to reduce carbon emission and it may be one of the most important investment trends in the future.

THE OPPORTUNITIES OF SECTOR ROTATION

Monetary tightening of the U.S. Fed is quite certain in 2022. Although it may be unfavorable to growth stocks, the rising interest rate environment would benefit those old economy, cyclical and value stocks. It is believed that financial sectors would be one of them since the profitability of those financial institutions such as banks, insurance companies will improve due to a wider net interest margin income.

EXHIBIT 1: S&P 500 financial sector rose about 90% in the early stage of last interest rate hike cycle

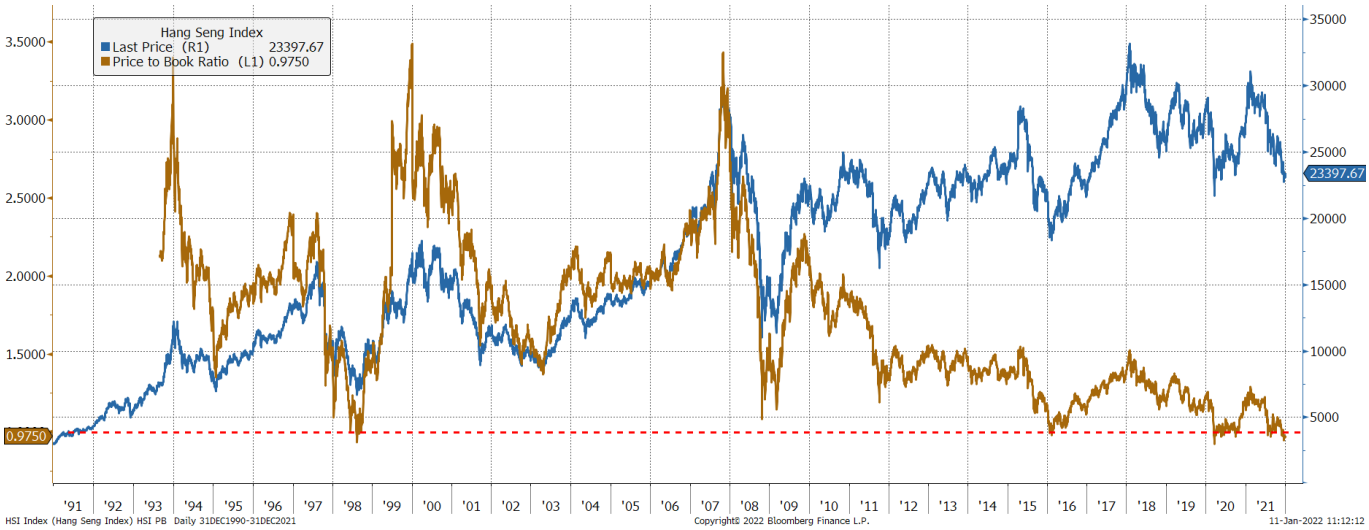


Source: Bloomberg (as at 31/12/2021)

LOW VALUATION OF HONG KONG AND CHINESE STOCK MARKETS

The Hang Seng Index and Hang Seng China Enterprise Index were the two worst performing major global equity indexes in 2021. After the correction last year, their valuations look attractive. Like the Hang Seng Index, the current P/E ratio is about 10 times and its price-to-book ratio is even below 1 which is almost at the cheapest level in more than 30 years. If investors believe investment cycle, it may be a good timing to take it as a long-term investment.

EXHIBIT 2: The Price-to-Book ratio of Hang Seng Index is almost at the lowest level in 30 years



Source: Bloomberg (as at 31/12/2021)

We went through Covid-19 lockdown, mass vaccination, economy reopening and the arrival of Omicron variant last year. In 2022, we may still have to get used to the virus and rising cost of living will also affect our daily lives.

There are full of investment challenges this year, it would be better to adopt a prudent investment approach as a whole. At the same time, taking advantage of current relative value opportunities at both regional and sector level may also be a good strategy.

TABLE 1: Global Stock Markets Performance

	2021 Q4 Return		2021 Full Year Return	
Indexes	**Local Currency**	**USD**	**Local Currency**	**USD**
S&P 500	11.02%	11.02%	28.68%	28.68%
Nasdaq Composite	8.47%	8.47%	22.21%	22.21%
STOXX Europe 600	7.64%	5.92%	25.82%	17.19%
DAX	4.09%	1.79%	15.79%	6.61%
CAC 40	9.86%	8.10%	31.88%	22.83%
Nikkei 225	-2.14%	-5.32%	6.62%	-4.42%
Hong Kong Hang Seng	-4.84%	-4.69%	-11.84%	-12.33%
Hang Seng China Enterprises	-5.74%	-5.60%	-21.25%	-21.69%
Shanghai Stock Exchange Composite	2.06%	3.49%	7.05%	9.93%
Shanghai Shenzhen CSI 300	1.61%	3.03%	-3.51%	-0.91%
Singapore Straits Times	1.75%	2.61%	13.55%	11.34%
Korea KOSPI	-2.95%	-3.44%	4.15%	-4.79%
Taiwan TWSE	7.74%	8.29%	26.92%	28.85%
India SENSEX	-1.32%	-1.65%	23.23%	20.84%
Indonesia JCI	5.00%	5.38%	12.46%	10.65%
Thailand SET	3.40%	4.48%	17.70%	5.81%
Russia RTS	-8.96%	-8.96%	21.73%	21.73%
Brazil IBOV	-5.55%	-7.28%	-11.93%	-18.10%
S&P Pan Arab Composite	1.34%	1.34%	32.66%	32.66%
MSCI World	7.86%	7.86%	22.38%	22.38%

Source: Bloomberg (as at 31/12/2021)

TABLE 2: Major Currencies Performance (In terms of USD)

	Change in 2021 Q4	Change in 2021
Currencies	**In terms of USD**	
Euro	-1.81%	-6.93%
British Pound	0.43%	-1.01%
Japanese Yen	-3.29%	-10.28%
Hong Kong Dollar	-0.13%	-0.56%
Chinese Renminbi (CNY)	1.40%	2.69%
Australian Dollar	0.50%	-5.60%
New Zealand Dollar	-1.06%	-4.98%
Singapore Dollar	0.64%	-1.99%
South Korean Won	-0.42%	-8.63%
Taiwanese Dollar	0.60%	2.25%
Indian Rupee	-0.13%	-1.71%
Indonesian Rupiah	0.42%	-1.42%
Thai Baht	1.27%	-10.34%
Russian Ruble	-2.58%	-0.36%
Brazilian Real	-2.38%	-6.77%

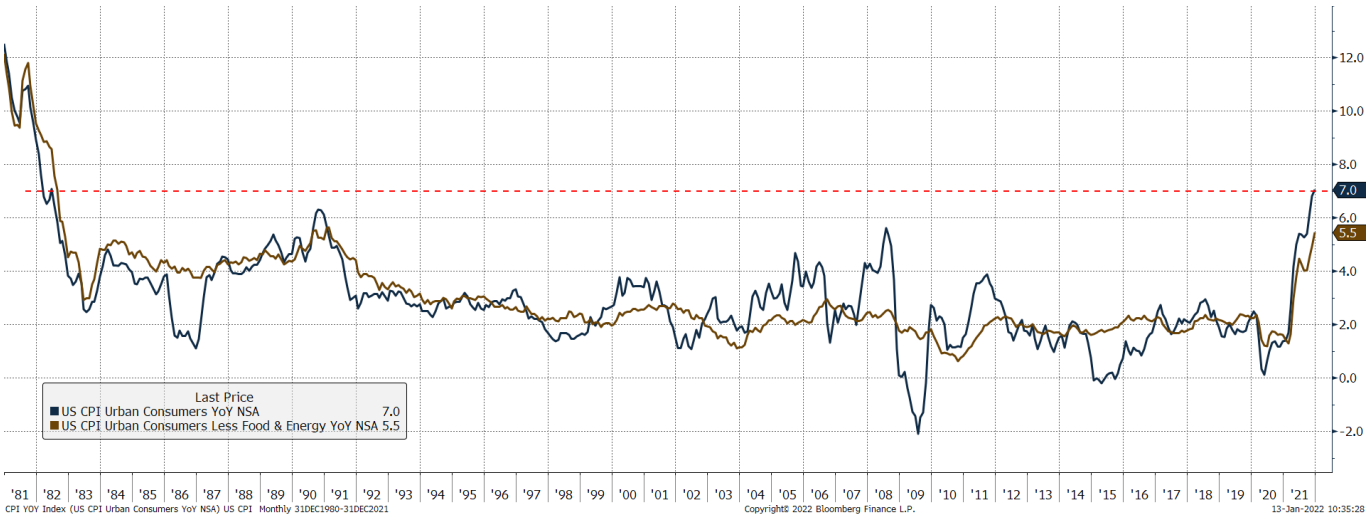
Source: Bloomberg (as at 31/12/2021)

Review Highlights and outlook around the globe

United States

- The U.S. inflation accelerated the most in 40 years. The consumer price rose to 7% in December and the core figures, which exclude volatile food and fuel costs, also climbed to 5.5% year-on-year.

EXIBIT 3: The U.S. consumer price grew at the fastest pace since 1982



Source: Bloomberg (as at 31/12/2021)

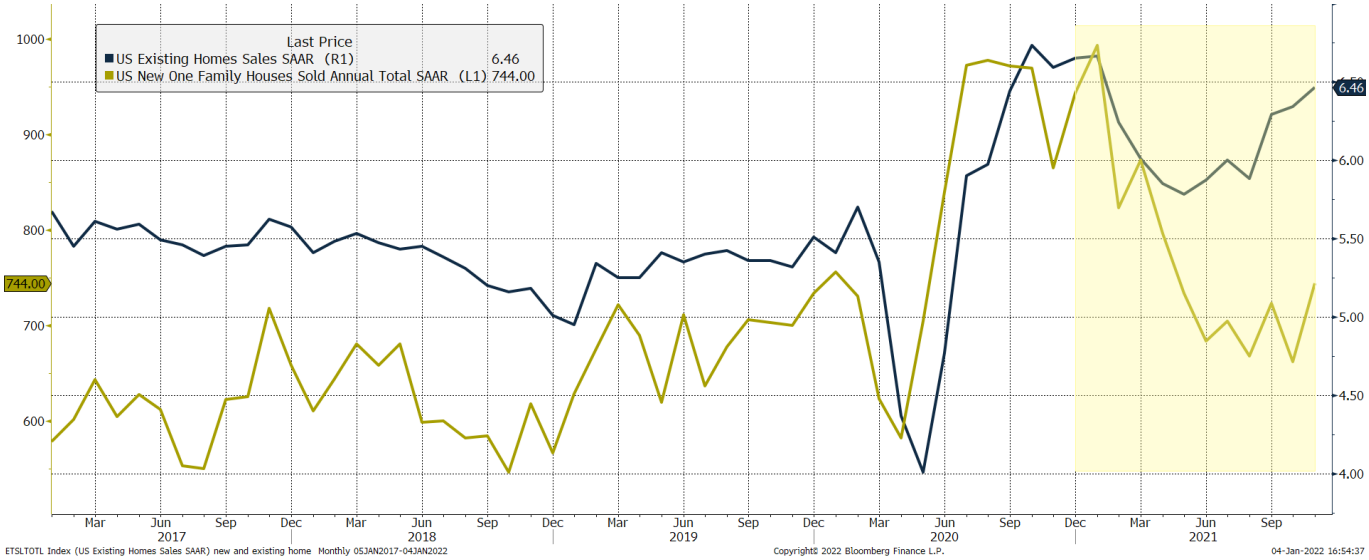
- According to the data from the Labor Department, the unemployment rate fell to 3.9% in December, a new pandemic low despite the economy only added 199,000 jobs in that month. Job growth averaged 537,000 per month in 2021 and nonfarm employment has increased by 18.8 million since April 2020 but it is still about 3.6 million jobs short of its pre-pandemic level.

- At the same time, a record number of Americans, more than 4.5 million people, voluntarily left their jobs in November. The highest rates of people leaving their positions were in sectors where remote work is not an option as Covid-19 risks were rising again. Healthcare, retail and restaurants are facing big labor shortages. For example, there were 1.8 million job openings in healthcare and social assistance in November, but only about 6,100 workers were added.

- The December ISM Services PMI Index fell to 62 from November's all time high of 69.1. The 7.1-point decline was the sharpest since April 2020 and may suggest that the Omicron variant is beginning to take a toll on providers of in-person services like travel, dining out and entertainment. At the same time, the ISM Manufacturing PMI in December fell to 58.7, the lowest level since January 2021. According to the ISM, the demand was still strong but supply chain constraints continued due to shortages of critical lowest-tier materials, high commodity prices and difficulties in transporting products.

- The U.S. new-home sales advanced to seasonally adjusted annual rate of 744,000 in November from a revised 662,000 in the prior month, the sales were at 7-month high but 14% below last year's level. The existing home sales increased for a third straight month in November to a seasonally adjusted annual rate of 6.46 million units. Tight supply and elevating house prices hindered the U.S. home sales in 2021. Comparing to the end of 2020, the latest median sales price of both existing and new home surged about 14%.

EXHIBIT 4: The U.S. home sales fell in 2021



Source: Bloomberg (as at 31/12/2021)

- Supported by the accommodative fiscal and monetary policy as well as strong corporate earnings, 2021 was another stellar year for the U.S. equity markets. The Dow, S&P 500 and Nadsaq Composite Index gained 20.95%, 28.68% and 22.21% respectively in 2021, which were their third straight winning years. However, the overall condition may have some changes in 2022 and it is anticipated that market volatility will increase this year. Persistent inflation may speed up the pace of the monetary tightening shift of the Fed. Besides, the high stock market valuation may also easily trigger significant market correction if any unfavorable event occurs.

Europe

- The IHS Markit Eurozone Composite PMI stood at 53.3 in December 2021, which was below the previous month's 55.4. The latest figure signaled the weakest expansion in private sector activity since March, as services output growth slowed to an eight-month low amid a resurgence of Covid-19 infections, while the manufacturing expansion remained subdued due to supply chain disruptions.

- Driven by the skyrocketing energy cost, the inflation rate of the Eurozone rose 5% in December as compared to last year and hit its highest record. Unlike the Fed, the European Central Bank ("ECB") believes that the inflation will peak soon as they expect energy prices to stabilize throughout the year and supply bottlenecks to ease and the dovish stance of the ECB is likely to remain unchanged in the near term. The divergence between the policy stance of the Fed and ECB may lead the Euro to weaken further this year after about 7% depreciation against the USD in 2021.

EXHIBIT 5: The Euro depreciated about 7% against the USD in 2021

Source: Bloomberg (as at 31/12/2021)

- The STOXX Europe 600 advanced more than 25% in 2021, but there are still several good reasons to support the positive investment outlook of European equities. Firstly, the monetary policy of ECB is more accommodative as it is believed that the central bank will only cautiously unwind its stimulus package. Secondly, as global investors increasingly incorporate ESG (Environment, Social, Governance) factors into investment decisions, European equities may attract money inflow since European companies generally have a strong commitment on ESG issues. In addition, if sector rotation is the key investment theme this year, European equities is expected to benefit since Europe market possesses a higher proportion of value and cyclical stocks than its global peers.

Asia

- Driven by the strong global demand of semiconductor and technology goods, the exports and imports of both South Korea and Taiwan broke new record high in 2021.

EXHIBIT 6: Record High Exports and Imports in South Korea and Taiwan

	2021 Export growth rate (year-on-year)	Export amount in 2021 (USD Billion)	2021 Import growth rate (year-on-year)	Import amount in 2021 (USD Billion)
Taiwan	29.40%	446.45	33.20%	381.17
South Korea	25.80%	644.54	31.50%	615.05

Source: Bloomberg (as at 31/12/2021)

- The Japan economy declined 3.6% in the 3rd quarter year-on-year as a sharp rise in local Covid-19 cases during the period hit private consumption and a global chip supply shortage hurt the sales of cars and electronic goods. However, it is expected that Japan's economy should rebound in the coming quarters since the government just unveiled a record breaking USD 480 billion stimulus package to boost the economy.

- The manufacturing activities in China accelerated in December. The official manufacturing Purchasing Managers' Index (PMI) rose to 50.3 from 50.1 in November while the Caixin manufacturing Purchasing Managers' Index (PMI) rose to 50.9 in December - its highest level since June. The overall business sentiment in the non-manufacturing sector also rebounded. The December official non-manufacturing PMI rose to 52.7, up from 52.3 in November while China Caixin services PMI, which focuses on small companies, rose to 53.1 in December from 52.1 in November.

- China posted a record trade surplus in December and 2021, as exports outperformed expectations during a global pandemic. The trade surplus hit $676.43 billion in 2021, the highest since records started in 1950, up from $523.99 billion in 2020. The surplus with the U.S. rose 25.1% in 2021 over a year earlier to $396.6 billion. The strong trade balance data reflected strong foreign demand and China's important role as a manufacturing center in global supply chain.

- Although the manufacturing activities remained strong, there is no sign of recovery in the property market. In November, the residential property sales and the area of new housing started by developers both dropped about 20% from a year ago. In addition, the new home sales price fell 0.3% month-on-month, which was the biggest decline since February 2015 and only nine of 70 cities tracked by the Chinese statistics bureau saw monthly price gains.

- To avoid economic slowdown, the People's Bank of China ("PBOC") cut the Reserve Requirement Rate ("RRR") for banks by 50 basis points in mid of December. It was the second move last year and released 1.2 trillion RMB in long term liquidity. At the same time, the PBOC also raised the foreign exchange RRR by 200 basis points to 9% from 7%. The move would force banks to set aside more of their foreign currency deposits, and it is widely believed the decision intended to slow down the yuan's recent rapid appreciation.

EXHIBIT 7: The Renminbi appreciated rapidly since May 2020

Source: Bloomberg (as at 31/12/2021)

- We have witnessed significant performance divergence of Asian stock markets in 2021. While the Hong Kong Heng Seng Index lost over 10%, the Indian Sensex and Taiwan stock Exchange Weighted Index gained more than 20%. The poor performance of Hong Kong stock market was mainly due to China's regulatory crackdown in different aspects of the economies and the sanctions or restrictions imposed by the U.S. SEC to those U.S. listed Chinese companies. Whether the Hong Kong stocks can have reversal in 2022, it still depends on the Chinese Government policy to a certain extent. Currently, the valuation of Heng Seng Index is almost at the cheapest point in more than 30 years, it may be worth increasing the exposure, but probably policy- driven stock selection would be crucial.

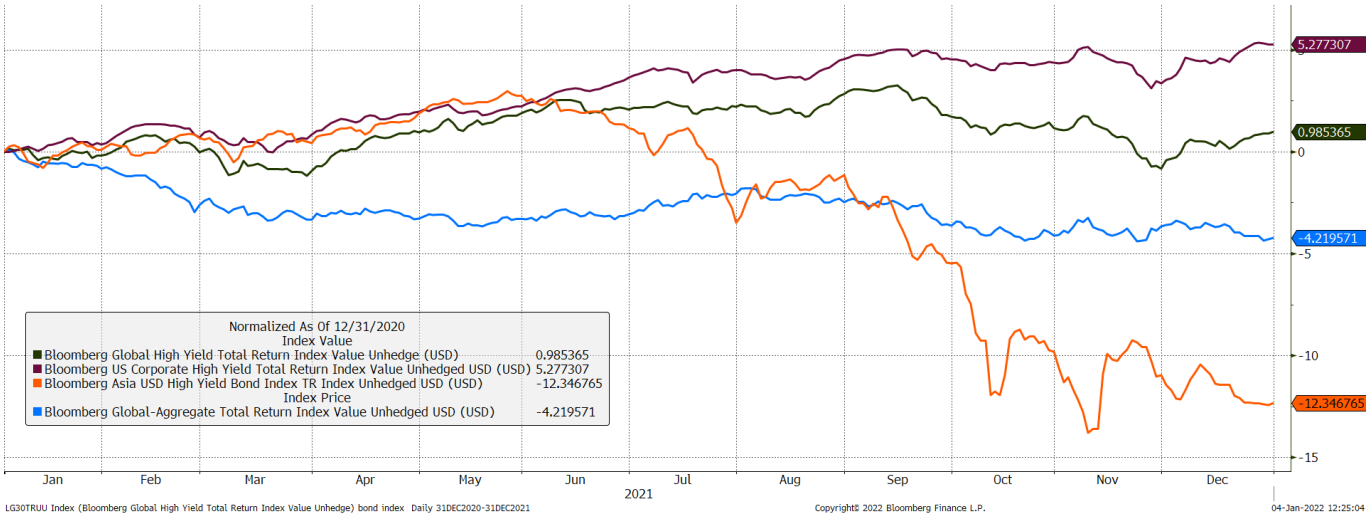
EXIHIBIT 8: The Asian equity markets diverged in 2021

Source: Bloomberg (as at 31/12/2021)

Fixed Income

- Because of the robust recovery of the U.S. economy and strong U.S. dollar, the U.S. corporate high yield bond outperformed other fixed income sectors in 2021. On the other hand, due to the Evergrande default crisis, the Asian high yield bonds tumbled, and the Bloomberg Asia USD High Yield Bond Index lost over 12% last year.

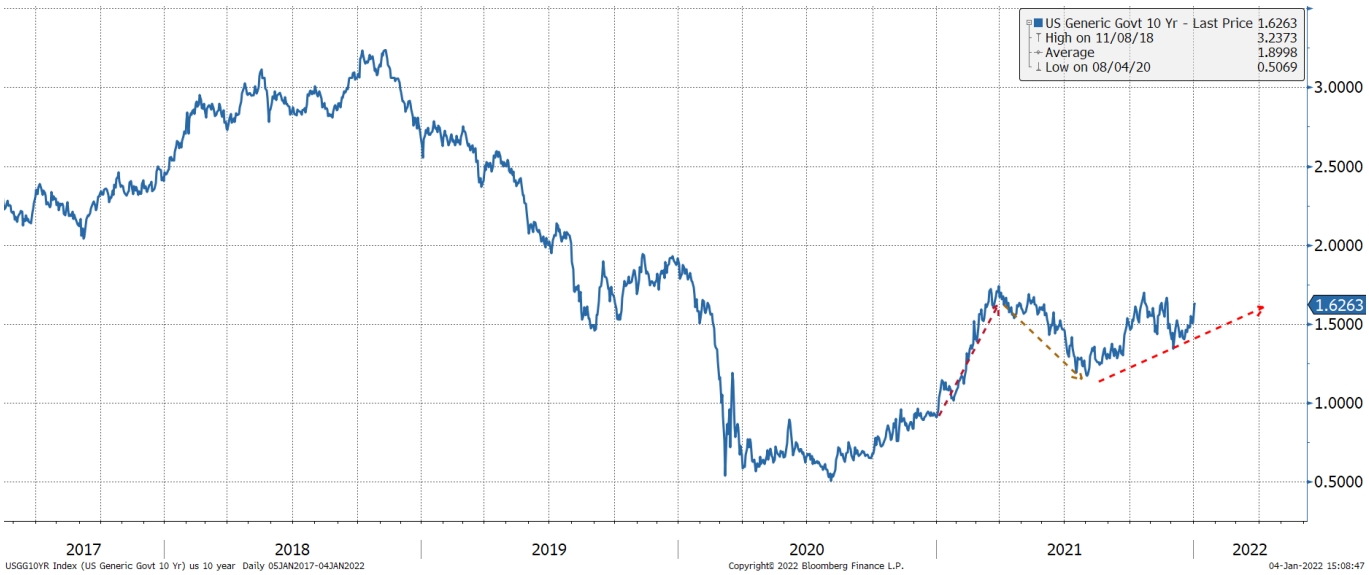
EXHIBT 9: The U.S. corporate high yield bond outperformed other fixed income sectors in 2021



Source: Bloomberg (as at 31/12/2021)

- During the last meeting in December, the Fed decided to double the pace of its tapering to USD 30 billion per month and the asset purchases program will end in March 2022. Besides, according to the latest Federal Reserve's dot plot, it showed that the officials expected to raise the Fed fund rates 3 times in 2022 and another 3 times in 2023. Since the Federal Reserve has turned to be more hawkish, it is believed that the benchmark 10-year treasury yield may continue its upside trend and move higher in 2022 which may be unfavorable to the overall investment sentiment.

EXIBIT 10: U.S. 10-year treasury bond yield may move higher in 2022



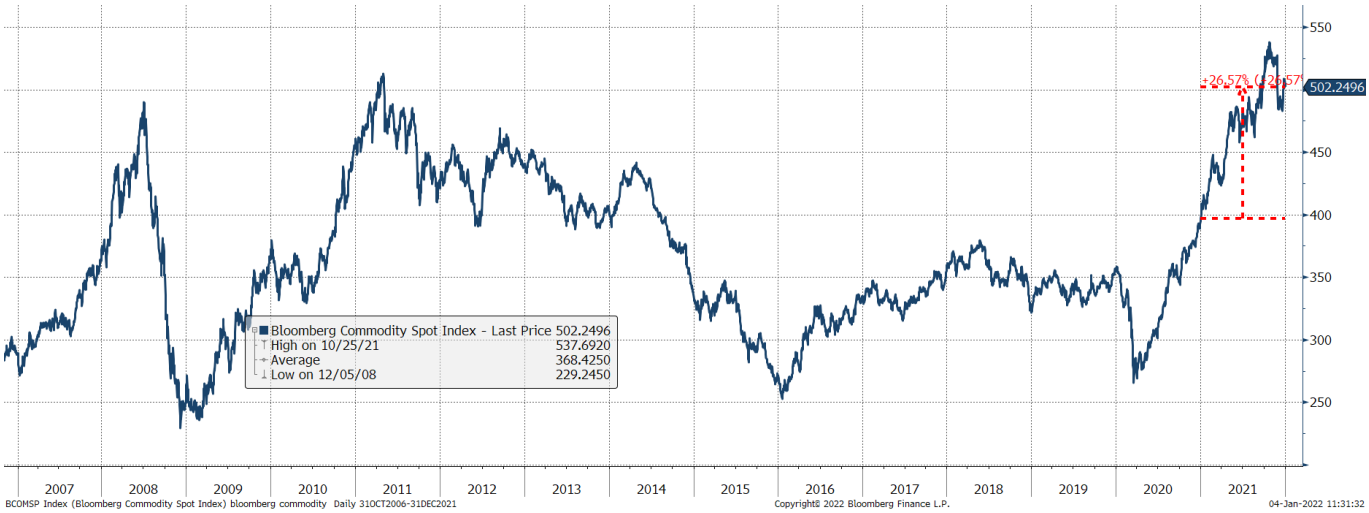
Source: Bloomberg (as at 31/12/2021)

- However, the overall outlook of fixed income investment may not be that pessimistic in 2022 even though the bond yields are expected to move higher. In fact, a steady rising bond yield may not be a bad thing as it also offers a higher reinvestment return for coupons and principals of matured bonds.

Commodities

- The performance of commodities has been very strong throughout 2021, the Bloomberg Commodities Spot Index jumped over 26%. Recovering demand after the Covid-19 lockdown, supply chain disruptions, government policy and adverse weather have all contributed to the stellar performance. In 2022, it is believed that the commodities price growth will become milder as the overall supply chain disruption will improve and the tightening monetary policies of major global central banks also may limit the rise.

EXIHIBT 11: The Bloomberg Commodities Spot Index rallied over 26% in 2021



Source: Bloomberg (as at 31/12/2021)

- The oil price rallied over 50% last year and oil was one of the best performing commodities. Looking ahead, the bullish momentum of oil may continue in 2022 as it is expected that the phenomenon of demand-supply imbalance will still exist in the near term. Although the Omicron variant has pushed the Covid-19 new infected cases to a new peak, it seems that the variant is less severe to the human health. Most of the countries in the U.S. and Europe believed that the impact of Omicron would be short-lived and are reluctant to restore the strict restrictions that hammered the global economy when the pandemic took place in 2020. On the supply side, even though OPEC and its allies agree to increase production, many member-countries actually do not have enough capacity and struggle to meet the target. As a result, the oil shortage may continue to support the strong price.