INVESTMENT INSIGHT APR 2023

Investment Services Department

Altruist Financial Group Limited
進邦滙理有限公司

A SERIES OF BANK FAILURES IN THE U.S. AND EUROPE

RISKS ARE SEEN IN THE NEAR-TERM, BUT OPPORTUNITIES MAY BE IN THE FUTURE

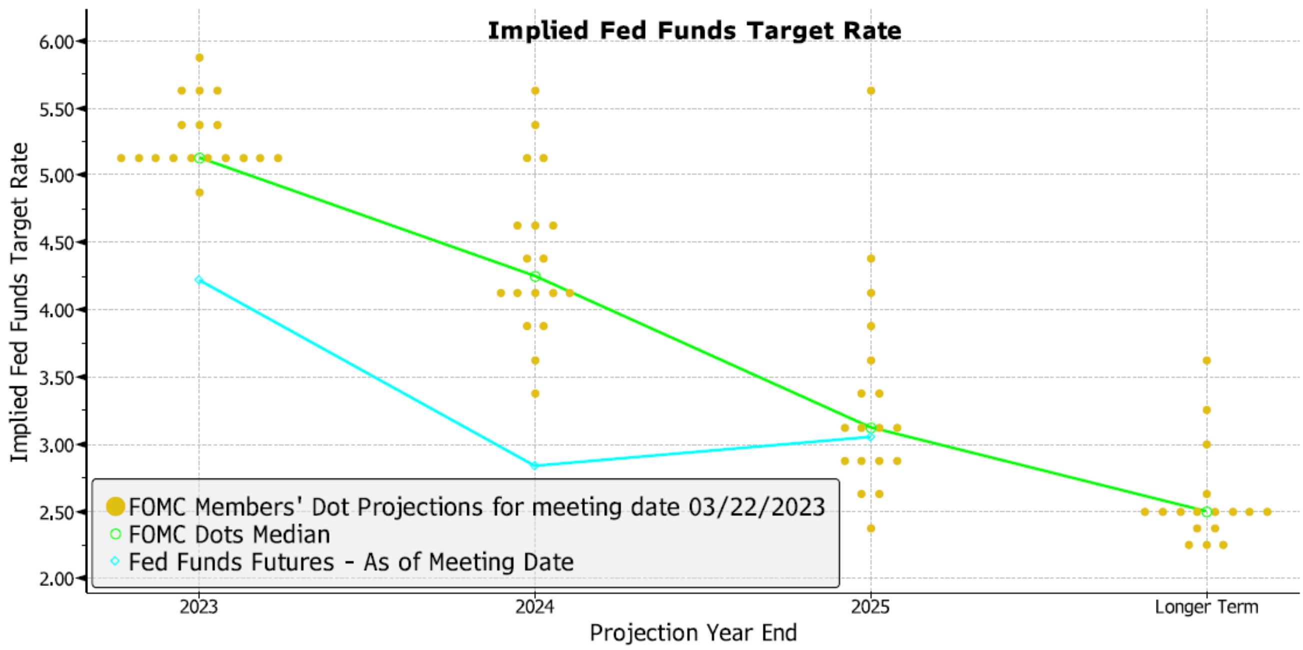
KEY MARKET HIGHLIGHTS IN 2023 Q1

The financial markets have been full of drama in the first quarter of 2023. In January, almost all asset classes rallied as the market anticipated that the global central banks will slow down the pace of interest rate hike and the reopening of the Chinese economy after the Covid pandemic may also stimulate global economic growth. However, the optimistic sentiment was short-lived and had a U-turn afterward.

In the second week of March, Silicon Valley Bank and Signature Bank which were heavily exposed to the tech startup financing and cryptocurrency sector failed respectively and their collapses marked the second and third bank failures in the history of the U.S. To avoid further deterioration, The Federal Reserve ("Fed"), Department of Treasury and Federal Deposit Insurance Corporation reacted quickly, they pledged that all depositors' money in the two banks were 100% protected and additional liquidity was injected into the market. Unexpectedly, a week later, Credit Suisse, the second largest bank in Switzerland, also was at the edge of bankruptcy as the bank recently recorded the biggest loss since the 2008 financial crisis and revealed that it had identified "material weaknesses" in their internal controls over financial reporting for the year 2021 and 2022. With the assistance of the Swiss central bank and financial regulator, the failed Credit Suisse was quickly rescued and acquired by UBS but the Swiss regulator's decision of write down Credit Sussie's USD 17.49 billion AT1 bond to zero greatly surprised the market and triggered frustration among related bondholders.

It is believed that a series of bank failures in the U.S. and European are not coincident, and the aggressive monetary tightening of global central banks in the past year have already weakened the normal banking operation. Before the recent bank failures, the number one task of global central banks would be taming the inflation, but now their focus may have switched to stabilize the entire financial system. According to the latest projection of Federal Open Markets Committee ("FOMC") members, the median of Fed Fund Rate would be at 5.125% at the year-end of 2023 which only one more rate hike is expected this year. At the same time, based on the latest figure of Fed Fund Futures, the market even anticipated the interest rate will be cut to 4.25% from the current 4.75% to 5% range at the year-end.

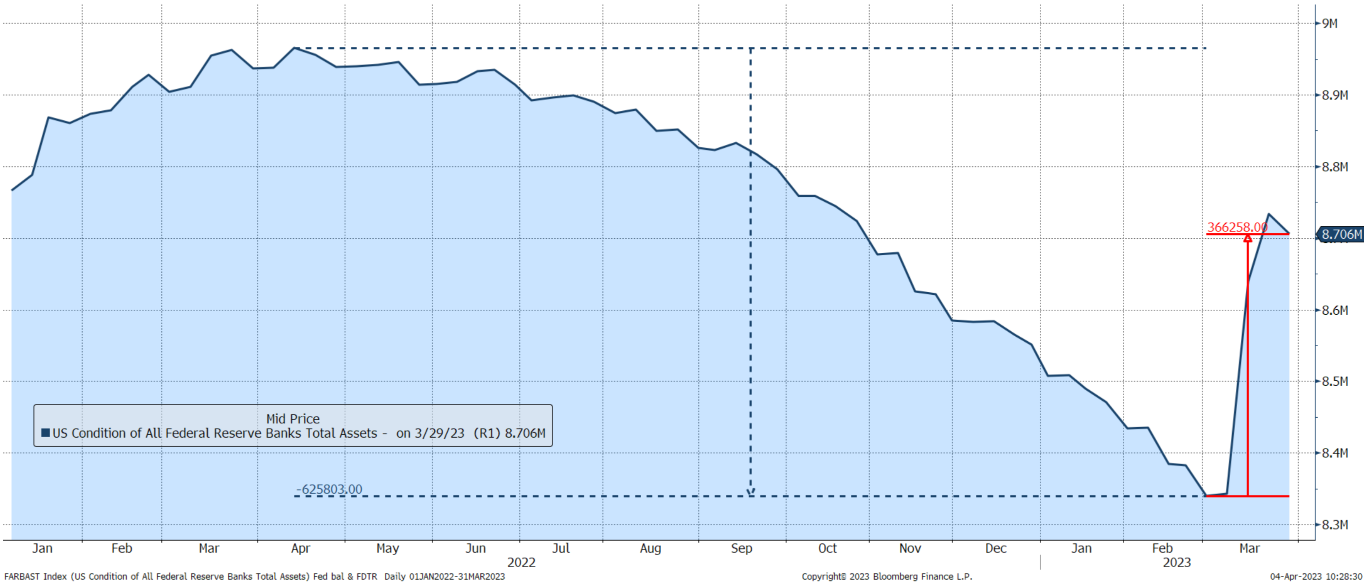
EXHIBIT 1: FOMC members' projection and indication of the Fed Fund Futures



Source: Bloomberg (as at 31/03/2023)

Meanwhile, although the Fed is now targeting to reduce its balance sheet at the pace of USD 95 billion per month, it recently has also injected liquidity into the market through the discount window lending and the newly launched Bank Term Funding Program to avoid the spread of the current banking crisis. In March, the Fed balance sheet has added about USD 363 billion which was more than a half of the asset reduced since the quantitative tightening started in April 2022.

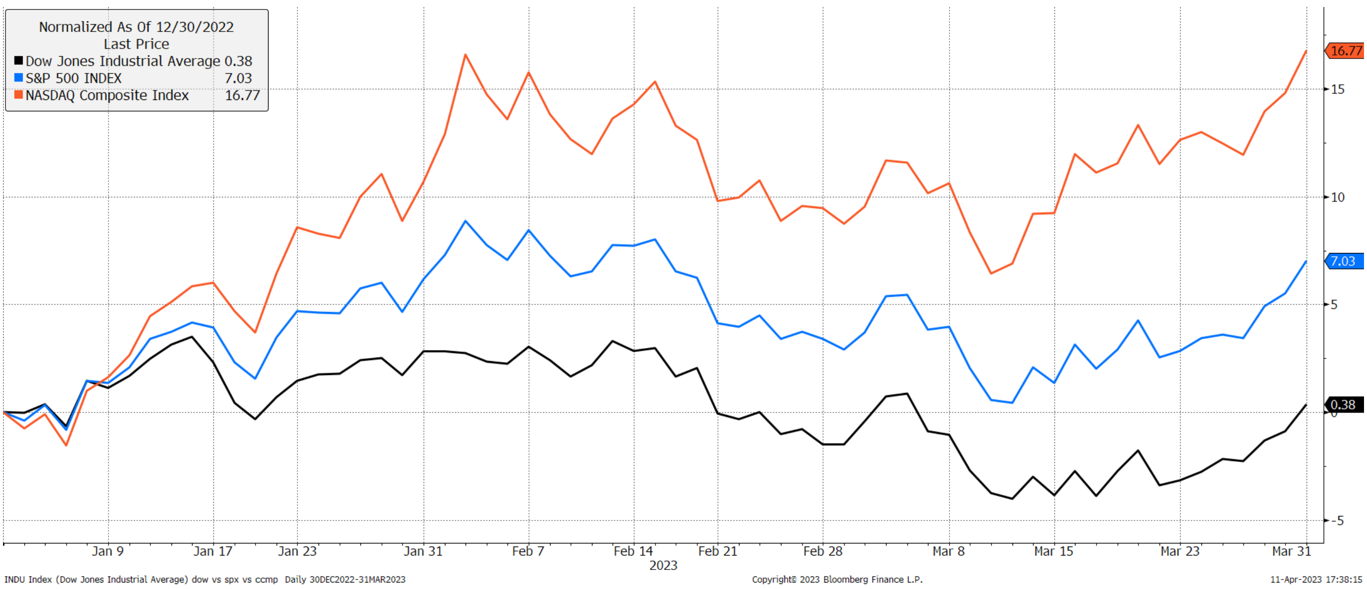
EXHIBIT 2: The Fed balance sheet added about USD 363 billion in March 2023



Source: Bloomberg (as at 31/03/2023)

As those major central banks and regulators reacted promptly after the failures of U.S. and European banks, the financial markets only had a very short-term shocks, and most of the asset classes rebounded in late March. Among all, the Nasdaq Composite Index outperformed and posted 17.05% gain in the first 3 months of 2023 which was its best quarterly gain since the second quarter of 2020 as the markets expect the pace of rate hike will be slowing down and the falling treasury yield may benefit those growth stocks.

EXHIBIT 3: The Nasdaq Composite Index outperformed in the 1st quarter



Source: Bloomberg (as at 31/03/2023)

TABLE 1: Global Stock Markets Performance (% In local currency)

Indexes	2023 Q1	2022 Full Year
S&P 500	7.48	-18.13
Nasdaq Composite	17.05	-32.51
STOXX Europe 600	8.58	-9.88
DAX	12.25	-12.35
CAC 40	13.39	-6.71
Nikkei 225	8.45	-7.35
Hong Kong Hang Seng	3.51	-12.56
Hang Seng China Enterprises	3.94	-15.63
Shanghai Stock Exchange Composite	5.94	-12.81
Shanghai Shenzhen CSI 300	4.67	-19.83
Singapore Straits Times	0.79	8.36
Korea KOSPI	10.76	-23.20
Taiwan TWSE	12.51	-18.83
India SENSEX	-2.87	5.77
Indonesia JCI	0.73	6.97
Thailand SET	-2.71	3.51
Russia RTS	2.97	-32.02
Brazil IBOV	-7.16	4.69
S&P Pan Arab Composite	-0.47	-5.68
MSCI World	7.88	-17.71

Source: Bloomberg (as at 31/03/2023)

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

Currency	2023 Q1	2022 Full Year
Euro	1.25	-5.85
British Pound	2.10	-10.71
Japanese Yen	-1.31	-12.23
Hong Kong Dollar	-0.61	-0.06
Chinese Renminbi (CNY)	0.36	-7.86
Australian Dollar	-1.88	-6.20
New Zealand Dollar	-1.45	-6.97
Singapore Dollar	0.65	0.71
South Korean Won	-2.79	-6.05
Taiwanese Dollar	0.87	-9.88
Indian Rupee	0.67	-10.15
Indonesian Rupiah	3.82	-8.45
Thai Baht	1.19	-3.47
Russian Ruble	-4.55	1.32
Brazilian Real	4.29	5.59

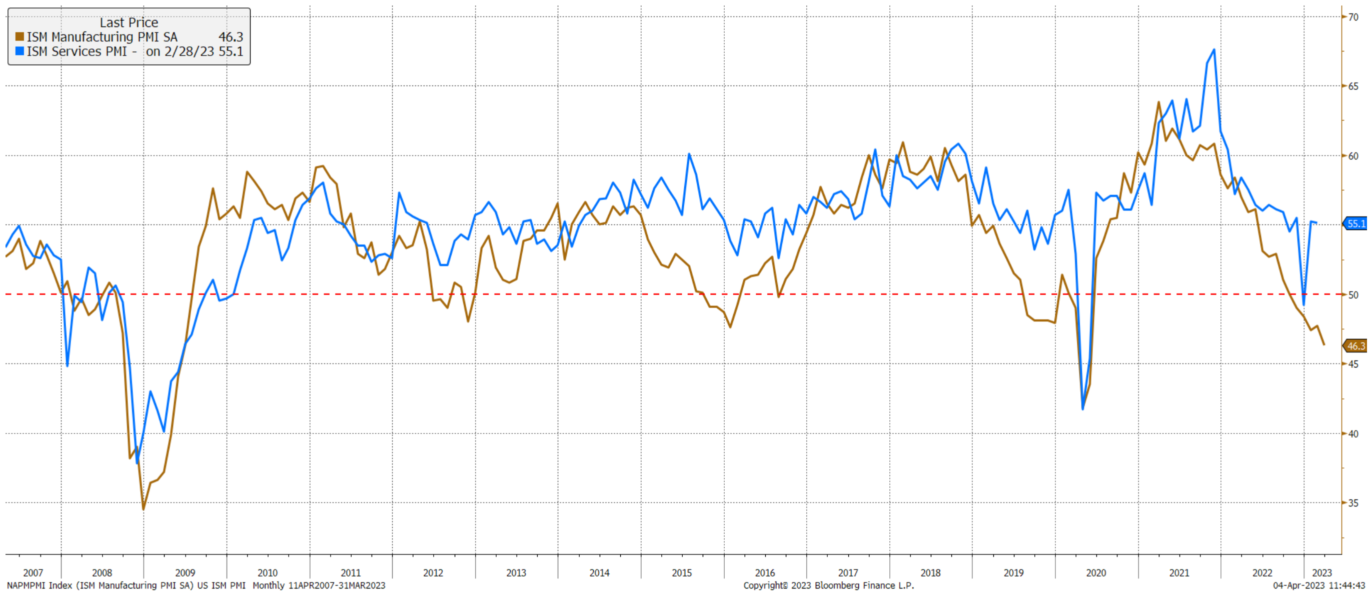
Source: Bloomberg (as at 31/03/2023)

WHAT'S AHEAD FOR THE REST OF 2023?

1. The risk of recession in the U.S. is rising but it may be short and mild if it happens

The monetary tightening of major central banks has already weakened the financial system and the economic activities have also seen downside pressure. The latest U.S. ISM Manufacturing Purchasing Managers' Index ("PMI") in March has declined to 46.3, the lowest since May 2020. In the past 70 years, whenever the ISM manufacturing PMI dropped below 45, recession occurred on 11 out of 12 occasions (exception was in 1967) according to the research from BoFA. The ongoing economic slowdown has already weakened demand while high inflation has also squeezed corporates' profit margin. According to the latest forecast of Wall Street Analysts, the S&P 500 companies is facing the sharpest drop in profits in the first quarter of 2023 since the pandemic.

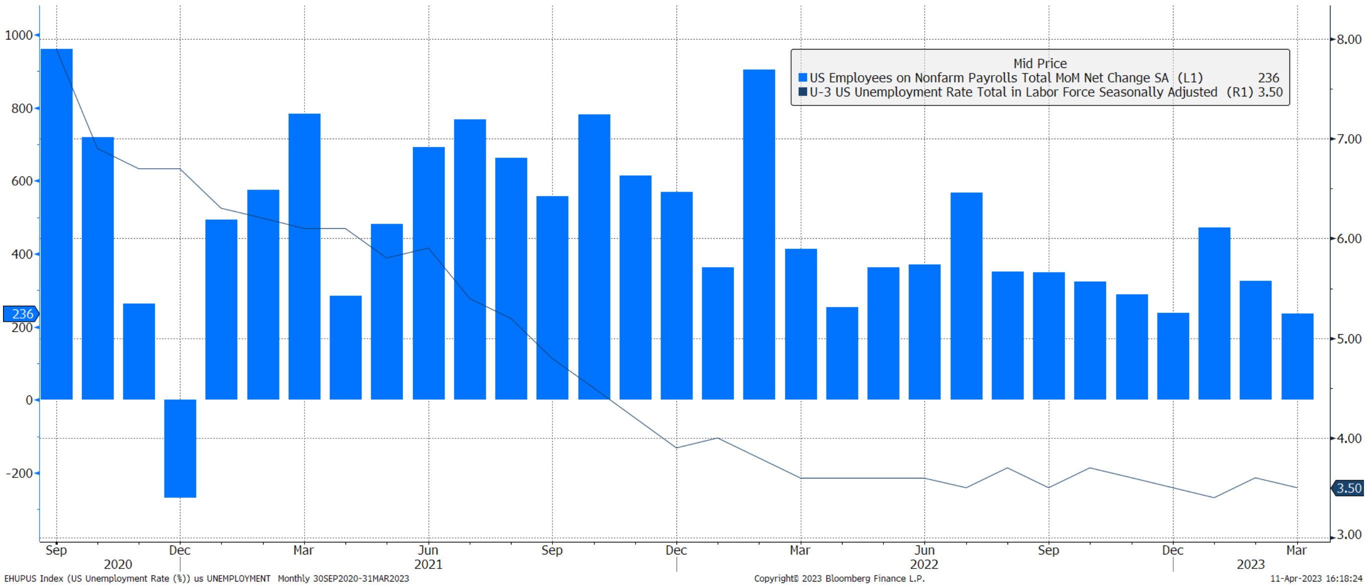
EXHIBIT 4: The U.S. ISM Manufacturing PMI has fallen into the contraction zone



Source: Bloomberg (as at 31/03/2023)

However, the U.S. labor market was still robust. Although only 236,000 jobs were added in March which was the smallest monthly gain since December 2020, it was still above the pre-pandemic monthly average of 183,000 gain between 2010 and 2019. At the same time, the unemployment rate was at 3.5%, near the 50- year low of 3.4% recorded in January this year.

EXHIBIT 5: The U.S. Job market remains robust



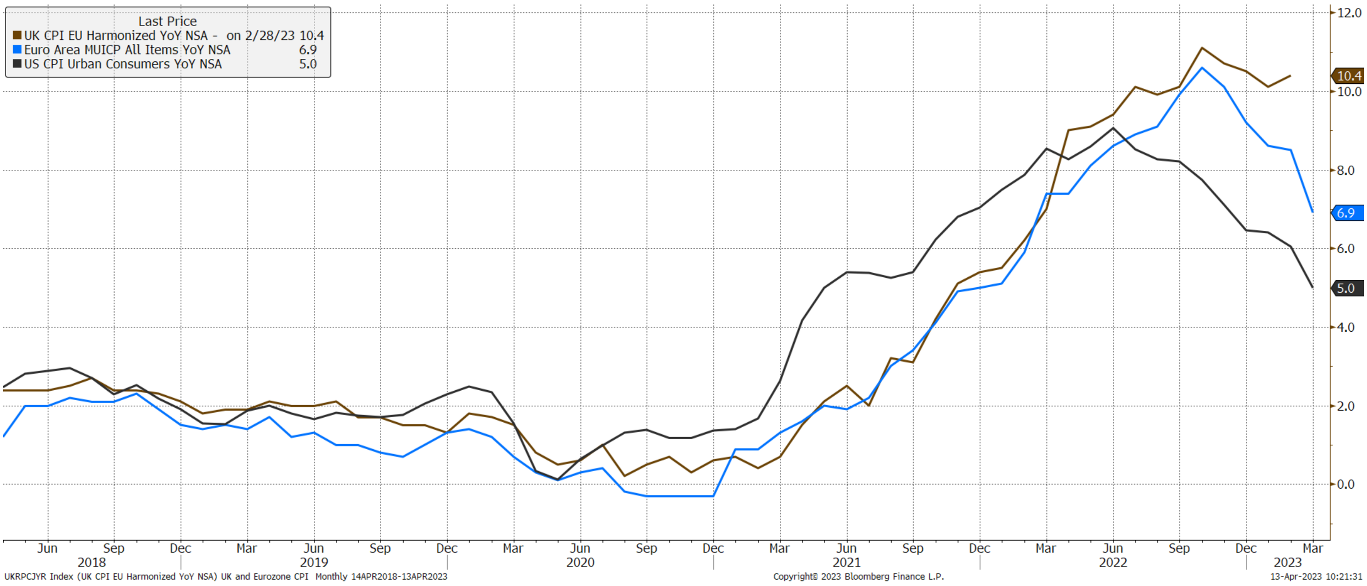
Source: Bloomberg (as at 31/03/2023)

Although the risk of recession in U.S. is rising, if recession happens, it may be different from the previous and it will likely be short and mild since it is believed that the labor market may only have slight deterioration.

2. A period of disinflation likely on the way

Although the price level is still high in the U.K, the inflation rate in the U.S. and Eurozone has decelerated in recent months, the Consumer Price Index of the U.S has even dropped to 5% in March which was the lowest since May 2021. The inflation is still far from the Fed's 2% target, but the weaker inflation together with the recent failures of regional banks may let the Fed reconsider its current interest rate policy and as mentioned earlier, the recent Fed Fund Futures have already indicated the interest rate will be peaked this summer and rate cut may happen in Autumn this year.

EXHIBIT 6: Inflation pressure is easing in the U.S.

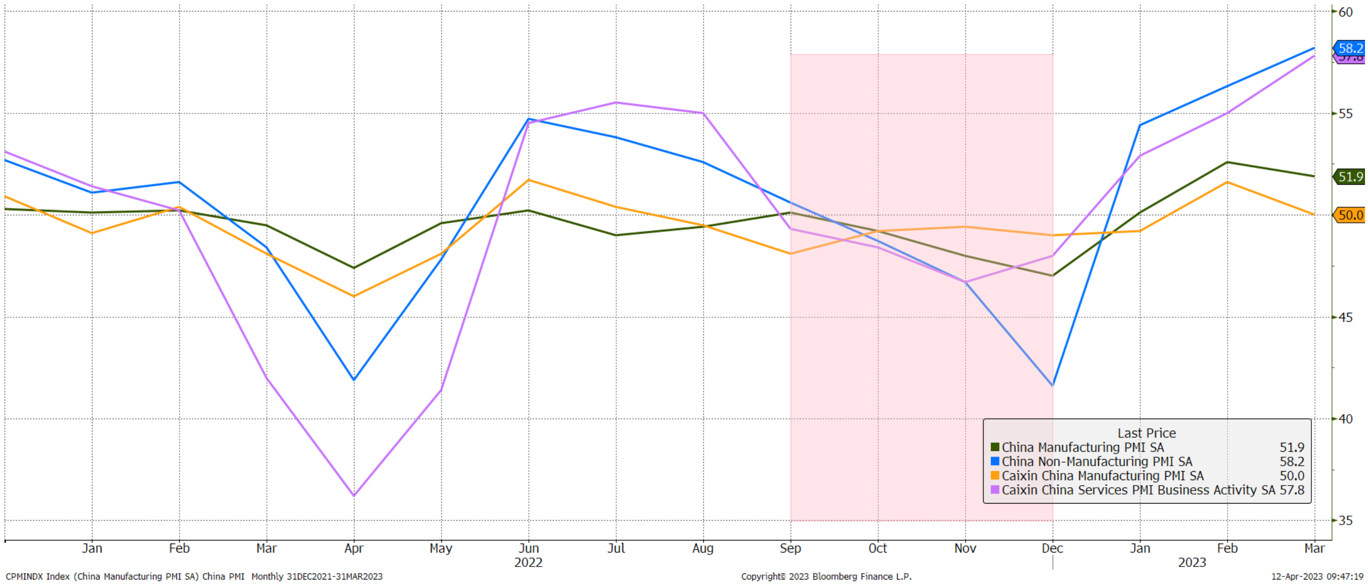


Source: Bloomberg (as at 31/03/2023)

3. The recovery of the Chinese economy

China's economic activities picked up gradually after the government started to abandon Covid-19 control in late 2022. Although the growth in the manufacturing sector was relatively moderate due to weak oversea demand, the expansion in the services sector accelerated. In March, the official non-manufacturing PMI soared to 58.2, marking the best level since 2011 while the Caixin China General Services PMI also rose to 57.8, which was the third consecutive monthly expansion and the highest reading since November 2020. The services sector is crucial to the Chinese economy as it accounts for 55% of GDP and 48% of employment.

EXHIBIT 7: The service sector in China accelerated in the 1st quarter of 2023



Source: Bloomberg (as at 31/03/2023)

The economic recovery of China is good news to the declining global economy, and it is believed that Asia, especially the ASEAN region, will benefit the most. Since ASEAN is the largest trading partner of China, the rebound of Chinese domestic demand will stimulate the export of the region. Also, they would also be benefitted from China's border reopening, as Thailand, Vietnam and Singapore are the top three travel destinations in Southeast Asia that are most favored by the mainland Chinese tourists.

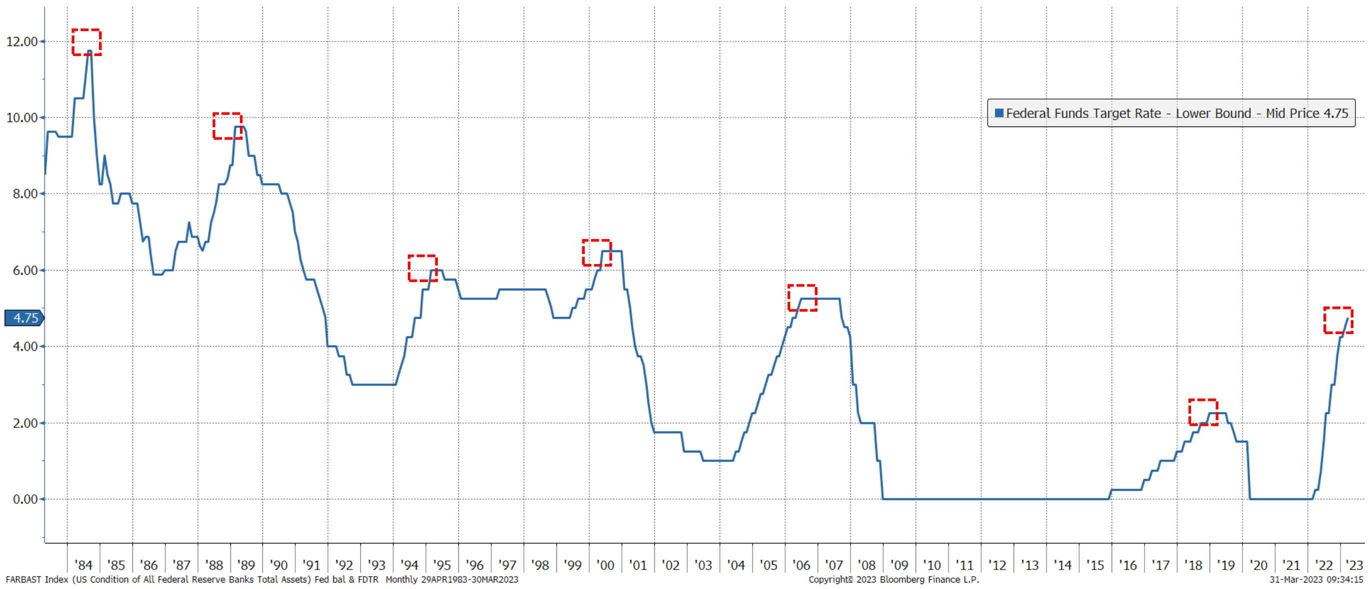
4. Global Geopolitical tension

Global geopolitical tension remains as one of the key risks to the global economy. The Russia-Ukraine war has lasted for more than 1 year, we still do not see any sign of ending. The conflict between the U.S. and China also heightened in different areas including trade, technology, military, national securities, South China Sea and Taiwan Strait. The persistent global geopolitical risk discourages globalization, disrupts supply chain and adds investment market uncertainty and volatility as well.

INVESTMENT IDEA – IF THE U.S. INTEREST RATE IS NEAR THE PEAK

The overall inflation rate in the U.S. is on a downtrend even though it may stay at the current high level for a while, but it is widely expected the Fed Fund Rate may be near the peak after more than one-year interest rate hike of 4.75% rate increase which was the Fed's most aggressive monetary tightening in the past 40 years.

EXHIBIT 8: The U.S. Interest rate cycle in the past 40 years



Source: Bloomberg (as at 31/03/2023)

Table 3: The 1, 2, 3-year performance of U.S. Equities and bond after the Fed Fund Rate peaked

The month that the Fed Fund Rate at peak	Performance in 1 year (%)		Performance in 2 year (%)		Performance in 3 year (%)	
	Equities*	Bond#	Equities*	Bond#	Equities*	Bond#
31/8/1984	18.22	24.15	64.47	51.73	121.23	53.91
28/2/1989	18.89	12.74	36.24	26.52	57.97	42.72
28/2/1995	35.57	12.51	69.87	18.25	129.30	30.51
31/5/2000	-10.55	13.12	-22.94	22.28	-29.15	36.44
30/6/2006	20.57	6.12	4.83	13.68	-22.65	20.55
31/12/2018	31.47	8.72	55.65	16.88	100.29	15.08
Average	19.03	12.89	34.69	24.89	59.50	33.20
Average (removing the best and the worst year)	22.29	11.77	40.30	20.98	64.21	32.55

Source: Investment Services Department of Altruist Financial Group and Bloomberg (as at 31/03/2023)

** S&P 500 Index* *#Bloomberg US Aggregate Bond Index*

If the U.S. interest rate cycle is near the end, it may be a favorable environment to both fixed income and equities investment. Excluding the current one, we have experienced 6 different U.S. interest rate hike cycles in the past 40 years and it is found that both S&P 500 and Bloomberg U.S. Aggregate Bond Index achieved remarkable returns in the coming 1 to 3 years when the interest rate is peaked.

We understand the global economy is still very fragile, there are a lot of different market uncertainties which may adversely affect investment sentiments. Under the current scenario, it is believed that high quality bond would be a more prudent investment choice. After more than one-year rate hike, bond prices have fallen significantly, and attractive bonds yields are seen, especially those short-term bonds. Like the 6-month and 1-year U.S. treasury, they are now providing about 4.7% and 4.4% yields respectively. In addition, the default risk of high quality or investment grade bonds is much lower, and they would be more resilient during economic downturn cycle.