INVESTMENT INSIGHT OCT 2023

Investment Services Department

Altruist®

Altruist Financial Group Limited
進邦滙理有限公司

INTEREST RATE

“HIGHER - FOR - LONGER”

U.S. & CHINA

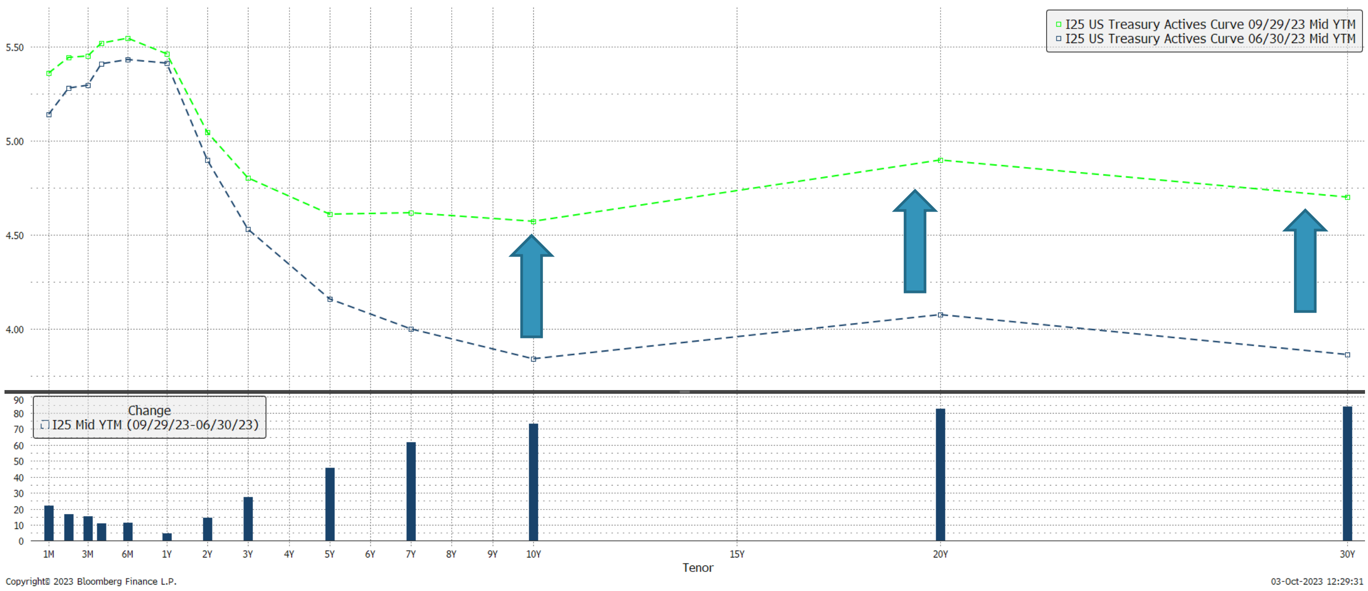
“DRIFT FURTHER APART”

KEY MARKET HIGHLIGHTS IN THE THIRD QUARTER OF 2023

Sometimes, good economic news could be the bad news for the investment markets. The U.S. economy remains robust with strong consumer spending while the unemployment rate is near historical low with stable job growth every month. The chance of soft landing of the U.S. economy is increasing and the previous expectation of recession seems unlikely to happen in the near future. The most aggressive rate hike of the U.S. Fed in the past one-and- a-half year has not cooled down the economy, the Fed maintained its hawkish stance as the current inflation rate is still far away from the 2% target. According to the latest projection from Federal Open Market Committee (“FOMC”) members, the Fed Funds Rate will be “higher-for-longer”, it is expected that the Fed will have one more rate increase this year and the median rate in 2024 of the latest projection is 5.125% as compared to 4.625% of the last projection in June.

The new “higher-for-longer” U.S. interest rate expectation has a big negative impact towards the bond market. The yields of medium-to-long term treasury bonds have rallied over 70 basis points in the past 3 months and the 10-year U.S. treasury yield has even risen above 4.6% which was the highest since 2007 while the short-term rate only had little changes. The rise of medium-to-long term treasury yields has caused the drop of major bond benchmark index. The Bloomberg U.S. Aggregate Index and Bloomberg Global Aggregated have fallen 2.31% and 3.59% respectively in the 3rd quarter and their year-to-date performance also turned to negative.

EXHIBIT 1: The yields of medium-to-long term U.S. treasury bonds rallied in the 3rd quarter



Source: Bloomberg (as at 30/09/2023)

The hawkish stance of the U.S. Fed has also driven the U.S. dollar to the strongest level since November last year. Due to the divergence in monetary policy, the Japanese Yen ("Yen") and Chinese Renminbi ("RMB") are two of the weakest major currencies. The Yen has fallen to about 150 per USD, near the lowest level since October 2022 while the RMB has also depreciated to about 7.3 per USD which was at 16-year low. In addition, most of the equities markets retreated in the last quarter since the strong U.S. Dollar and rising bond yield have reduced the attractiveness of equities investments.

EXHIBIT 2: The U.S. Dollar Index always moves inversely with global equities

Source: Bloomberg (as at 30/09/2023)

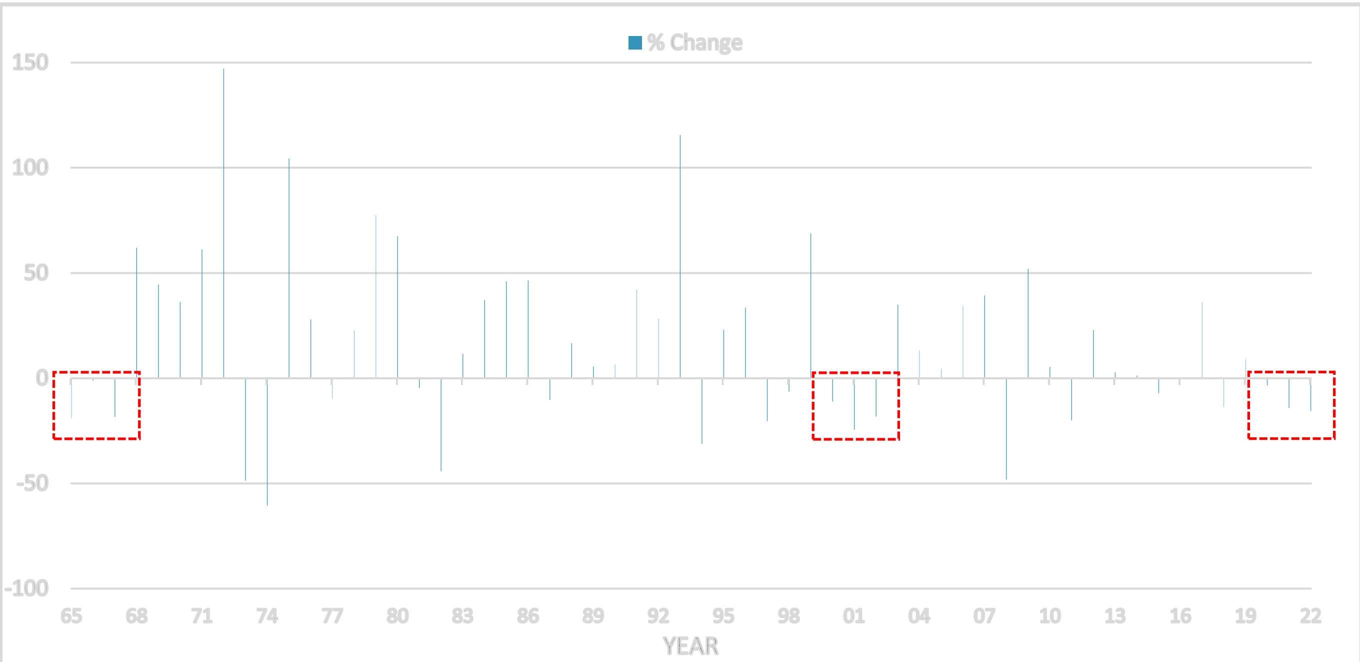
Apart from the Fed's monetary policy stance, the relationship between China and the west is also the market focus as they are drifting further apart. Tensions keep on rising, from tit-for-tat trade tariffs to tech rivalry and spying allegations.

Besides, the post-pandemic economic recovery in China is uneven, big-band stimulus has not been seen and the weakness of the indebted property sector has added further worries. The pessimistic sentiment has greatly affected the stock markets. The Hong Kong and China equities markets have suffered from a record USD 12 billion foreign investor selling in August. The average trading turnover of the Hong Kong stock market fell to about HKD 112 billion in the first 8 months of 2023.

In addition, according to Deloitte's September report on the Mainland China's and Hong Kong's IPO market performance, Hong Kong surprisingly slid to 8th place for IPOs, with 44 IPOs listed in the past 3 quarters. The raised amount of HKD24.7 billion has marked a decline of nearly 14% year-on-year. Out of the past 13 years, Hong Kong has ranked as the world's top IPO venue for 7 years and has never fallen out of the top five in the other years.

The Heng Sang Index has dropped 6.83% this year as at the end of the 3rd quarter. If there is no any exciting good news, it is likely that the index would record negative return this year. It would be its fourth consecutive year of making loss which has never happened since its inception in 1964.

EXHIBIT 3: Heng Sang Index has never recorded 4th consecutive yearly loss before



Source: Bloomberg (as at 30/09/2023)

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

Index	2023 Q3	2023 YTD
S&P 500	-3.27	13.06
Nasdaq Composite	-3.94	27.11
STOXX Europe 600	-2.03	9.24
DAX	-4.71	10.51
CAC 40	-3.43	13.38
Nikkei 225	-3.36	24.34
Hong Kong Hang Seng	-4.19	-6.83
Hang Seng China Enterprises	-2.03	-5.01
Shanghai Stock Exchange Composite	-1.40	3.33
Shanghai Shenzhen CSI 300	-2.93	-2.50
Singapore Straits Times	2.14	3.33
Korea KOSPI	-3.86	10.76
Taiwan TWSE	-1.72	19.58
India SENSEX	2.05	9.43
Indonesia JCI	4.43	5.12
Thailand SET	-1.40	-9.54
Russia RTS	3.14	8.56
Brazil IBOV	-1.29	6.22
S&P Pan Arab Composite	-1.49	3.64
MSCI World	-3.36	11.56

Source: Bloomberg (as at 30/09/2023)

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

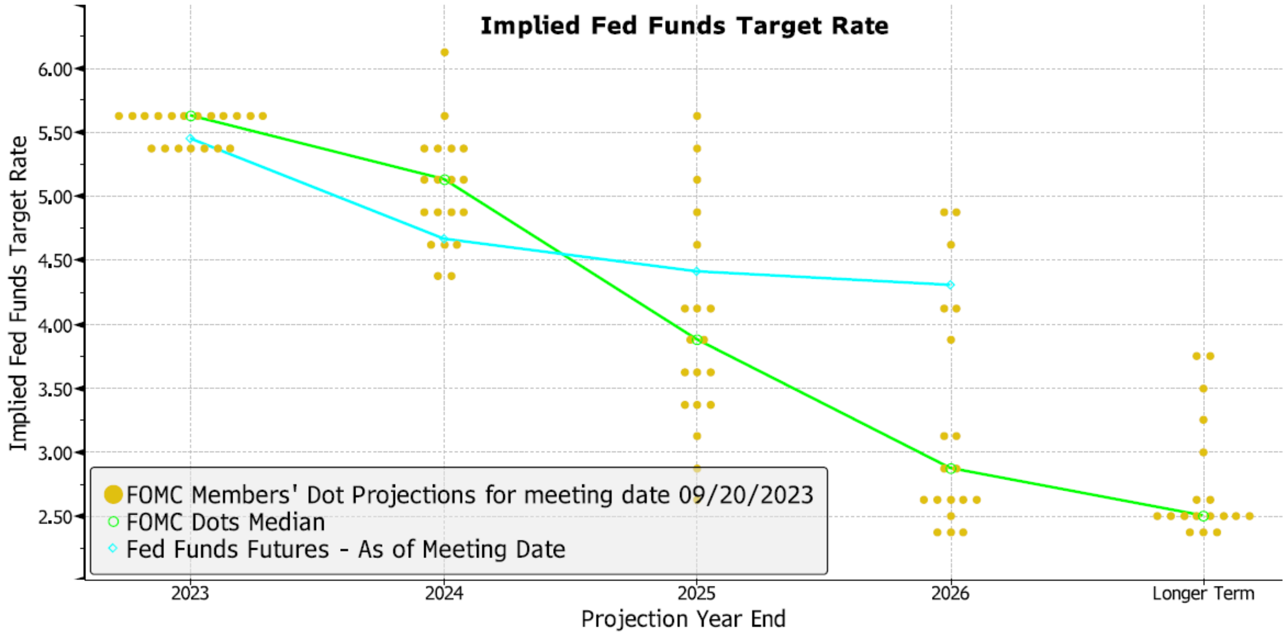
Currency	2023 Q3	2023 YTD
Euro	-3.08	-1.23
British Pound	-3.97	0.96
Japanese Yen	-3.39	-12.22
Hong Kong Dollar	0.08	-0.37
Chinese Renminbi (CNY)	-0.61	-5.47
Australian Dollar	-3.44	-5.55
New Zealand Dollar	-2.07	-5.54
Singapore Dollar	-1.01	-1.95
South Korean Won	-2.35	-6.22
Taiwanese Dollar	-3.52	-4.83
Indian Rupee	-1.2	-0.37
Indonesian Rupiah	-2.99	0.73
Thai Baht	-2.63	-4.96
Russian Ruble	-8.44	-23.95
Brazilian Real	-4.94	4.89

Source: Bloomberg (as at 30/09/2023)

Will the U.S. interest rate go higher-for-longer?

The Fed Fund futures, one of the most widely used tools for hedging short-term interest rate risk, indicated that the interest rate will fall to 4.66% in 2024 which will be lower than the 5.125% projections from the FOMC members.

EXHIBIT 4: Fed Fund Futures vs FOMC member projections

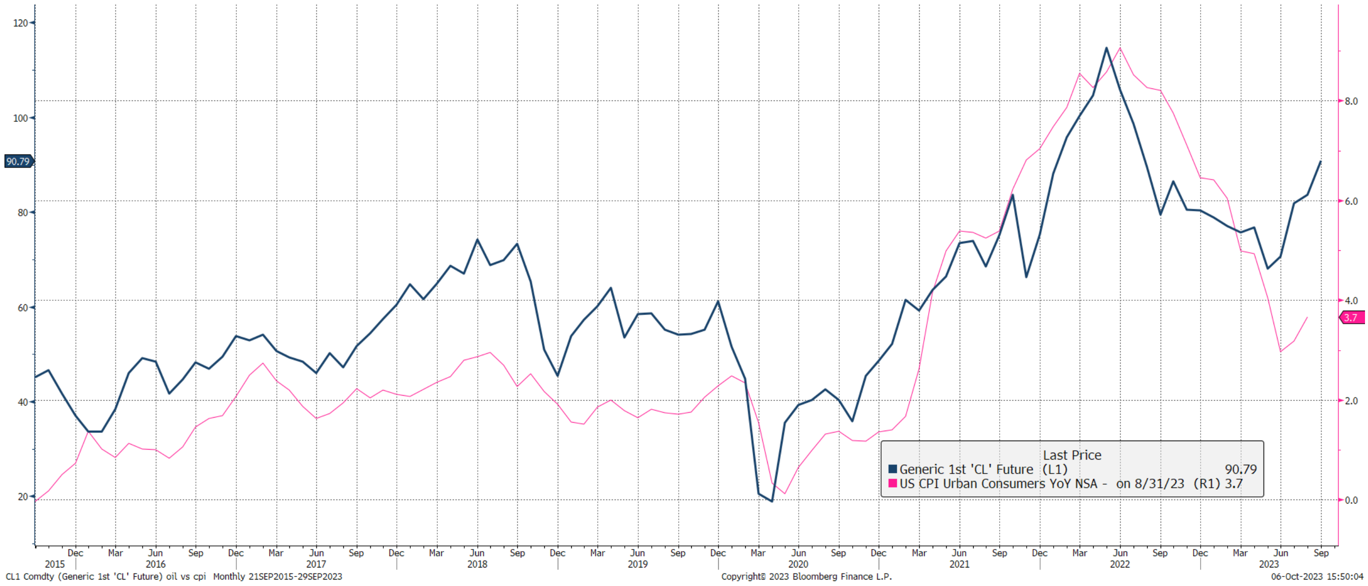


Source: Bloomberg (as at 30/09/2023)

Whether the U.S. interest rate will go higher-for-longer, there are many variables and oil price would be one of the most important influential factors. In the 3rd quarter, the oil price has risen over 30% to about USD 90 per barrel due to the oil production cut of Saudi Arabia and Russia. Will the production cut continue? Will the coming Winter in the Northern Hemisphere be colder than expected? Or will the global geopolitical tension be heightened further? Crude oil is a major economic input, those uncertainties may trigger the surge of energy price and elevate inflation pressure.

Besides, in the past decades, the western world has enjoyed the benefit of globalization by importing lot of cheap manufacturing goods from China. However, driven by the government policy, many critical manufacturing works are now returning to the U.S. due to strategic reasons. The change will increase cost and higher price will be transferred to the consumer and it may be hard for the inflation to be cooled down.

EXHIBIT 5: The U.S. CPI has moved closely with the oil price



Source: Bloomberg (as at 30/09/2023)

How should investors position if the U.S. interest rate go higher-for-longer?

The higher-for-longer expectation of the U.S. interest rate has negative impact to bond price, especially to those medium-to-long term bonds and the U.S. 10-year treasury yield has risen to over 4.6% which was the highest since 2007. To a certain extent, they showed attractiveness after the recent correction as investor can lock in a relative high yield for a longer period. Besides, if interest rate falls in the future, investors may also enjoy the opportunity of bond price appreciation. At the same time, the rising bond yields inversely affect equity markets and smaller companies may suffer more as most of them are not cash-rich companies and a higher borrowing cost may weaken their profitability.

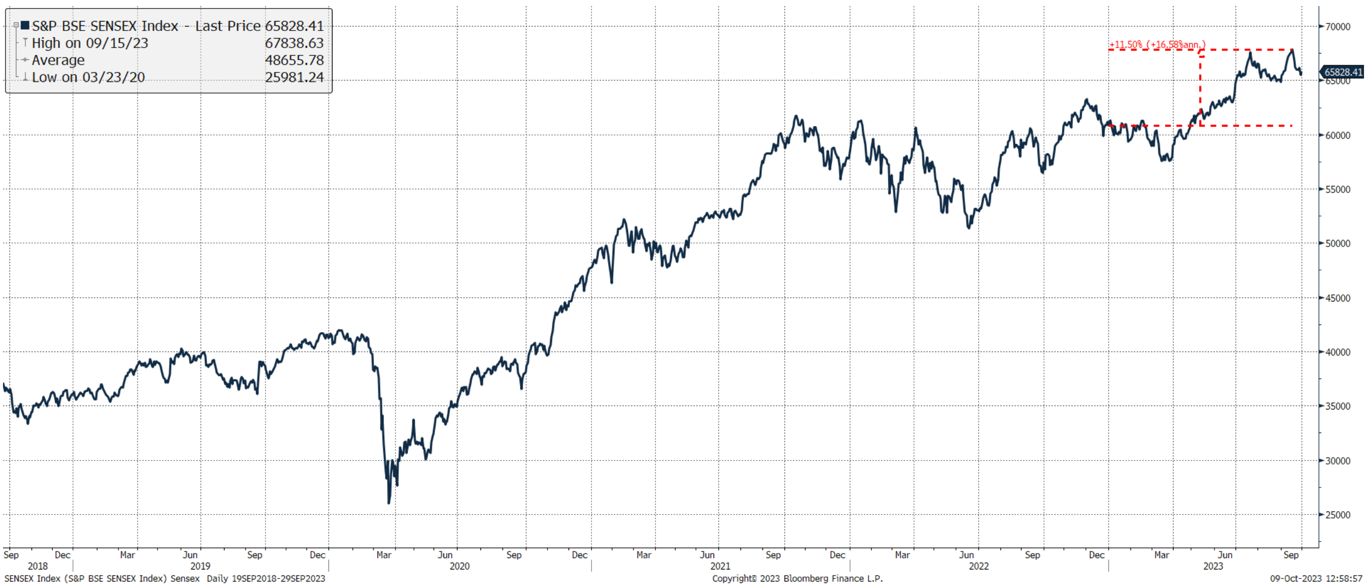
In the short term, to preserve capital and capture the investment opportunity of the current high interest rate environment, investors may consider to overweight short-term U.S. treasury bonds. Their yields within 1-year maturity are over 5.4% and it is believed such investment is almost risk-free since the chance of U.S. Government default in near term is extremely low.

How should investors position if the West and China drift further apart?

In the past few years, the global supply chain has been seriously disrupted by the Covid -19 pandemic and Russia's invasion of Ukraine. A new concept "friend-shoring" has been initiated by the U.S. recently which aims at rerouting supply chains to countries perceived as politically and economically safe or low-risk, to avoid disruption to the flow of business. In other words, it is the idea of reducing the reliance on China. However, according to the data of the US Bureau of Economic Analysis (BEA), the US-China trade in goods has reached a new record in 2022 at USD 690 billion and it is believed that despite the moving trend of reducing import from China, supply chain will not be changed overnight.

Nevertheless, investment opportunities emerge due to the gradually shift of supply chain. Among all, India market may have the greatest potential to compete with China in low cost and large-scale manufacturing due to its large and young population. Cheered by the abundant foreign investment and optimistic economic growth forecast in the coming years, the Indian Sensex Index has hit record high in September, rallied over 10% this year and this bullish trend may further go on.

<u>**EXHIBIT 6: The Indian Sensex Index has hit record high in September**</u>



Source: Bloomberg (as at 30/09/2023)

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