BCT銀聯集團

BCT Market Outlook

December 2014

US Equities

Latest Fed minutes showed the FOMC was concerned with the possibility of a downward movement in longer-term inflation expectation. Same as September, the October CPI rose by 1.7% from the previous year. Furthermore, the overall economic growth momentum continued. The ISM Manufacturing Index rebounded from 56.6 in September to 59 in October, indicating an acceleration in manufacturing expansion. What's more was the revised 3Q annualised GDP grew by 3.9% from the last quarter, higher than the preliminary figure of 3.5%.

Inflation is still below the Fed's 2% target, which favours the maintenance of the low rate policy. The decline in oil prices also weighed on the inflation expectation. On the other hand, improvement in employment and manufacturing continued to provide support to a US recovery, which is likely to fuel the strength of USD. As for the timing of the interest rate hike, in addition to employment situation, the focus has now shifted more to inflation. Although the inflation may be below the target for an extended period, we maintain the next rate hike to come at around mid-2015, due to a recovery and an improvement in the labour market. Our SLIGHTLY POSITIVE outlook for the US remains unchanged.

European Equities

The ECB announced the buying of ABS in November, urging to up-hold inflation, and will act further if necessary. The October CPI in the Eurozone increased by 0.4% from the previous year, which remained a far distance from the 2% target. On the other hand, the fundamentals were still sluggish. Eurozone's advanced 3Q GDP only rose by 0.2% from the previous quarter; while September's retail sales declined by 1.3% from the previous month, a reversal of August's 0.9% increment. Moreover, the Eurozone's Manufacturing PMI stood at 50.6 in October, lacking positive momentum.

In our view, the ECB must act with caution when buying into ABS. They need to strike a balance between moral hazard and the effectiveness in stimulating credit. Furthermore, the ECB may purchase sovereign bonds in 2015, but the action may not be effective as the bond yields are already at low levels. The possibility of unemployment and disinflation in the Eurozone remain as concerns, and the key to improve is whether the credit condition can be stimulated as expected under the easing policies. Euro depreciated further on ECB's policy stance which may support inflation, export and corporate earnings. The policy enhancement is likely to benefit the equity markets in the short term, but may suffer on the currency side. We maintain our NEUTRAL stance.

Japanese Equities

Prime Minister Abe dissolved parliament and announced a national election in December, and use the issue of delay in consumption tax hike (to Apr 2017 from 8% to 10% which was originally scheduled for October 2015) as the re-election theme. The preliminary GDP in 3Q declined by 1.6% on a quarter-on-quarter basis and was the 2nd consecutive quarter of slippage, entering into recession technically. Moreover, October's consumer confidence index dropped further from 39.9 in September to 38.9.

Abe's bet on delaying the consumption tax hike is likely to gain support from the public, but at the same time also reflects doubt in the effectiveness of Abenomics. In addition, the plan to increase equity holdings by Japan's Government Pension Investment Fund ("GPIF") favours equity markets overall, but the total return may be partly cancelled out by the weakness in yen under accommodative policy. Also, investors should also be cautious on the potential reversal of yen's weakness if Ebola and geo-politics environment worsen. Moreover, the rapid depreciation of yen may hurt imports more than benefiting on the export side. We remain NEUTRAL on the Japanese market.

Asia ex-Japan ex-Hong Kong Equities

The recent enhancement of ECB's and BoJ's accommodative monetary policies supplied abundant liquidity to the markets, while valuation continued to be a spotlight for the region. The MSCI Asia Pacific ex-Japan Index was traded at 13.3 times estimated earnings, lower than 17.2 times for the US S&P 500 Index. For specific countries, in addition to anticipated reforms from Jokowi's new Indonesian government, Indonesia's cut of fuel subsidies also favours market sentiment. Meanwhile, Malaysia will remove the energy subsidies in December, and it was reported that the borrowing cost of public housing fund in Korea will be lowered.

Certain countries acted to stimulate their economies through monetary and fiscal means, or to undergo reforms, which supported the equity markets. However, the strength of USD should persist on the back of sound US fundamentals and rate hike expectation, posting obstacles to potential upsides to Asian currencies or equities. Although political tension and the worsening of epidemic may trigger rapid and large-scaled money outflows, it should provide buying opportunities for medium to longer terms. We are SLIGHTLY POSITIVE in the region due to favourable economic prospects and attractive valuation.

China & Hong Kong Equities

The PBOC surprised the market by cutting the interest rate asymmetrically with lending rate cut more than savings rate, hoping to improve the sluggish credit condition and resist disinflation. Economic figures were not satisfactory. The October year-on-year growth of fixed asset investment, retail sales and industrial production all slowed down from September. Besides, as a leading indicator for CPI, October's PPI was down by 2.2% from the previous year, deepened from September's -1.8%, while the year-on-year growth of the CPI maintained at 1.6%. On the other hand, the sales of residential buildings in October dropped 3.2% which narrowed from September.

The recent rate cut is highly indicative of the weakness in the economy, it is beneficial to equity markets in the short-term, especially for property, insurance and RMB debt-intensive sectors; but the net interest margin (NIM) of banks may suffer. Also, further rate cuts are possible due to relatively high real (inflation adjusted) interest rate, but is believed that more targeted RRR / interest rate reductions and short-term liquidity injections are preferred actions that could avoid asset bubbles better. On the Shanghai–HK Stock Connect ("SHSC"), although current market showed little interests in participating, approval from offshore regulatory jurisdictions such as Luxembourg to allow local funds to invest through SHSC will increase the trading volume. We have changed to a SLIGHTLY POSITIVE stance for China and Hong Kong.

Global Bonds

Enhanced easing policies from ECB and BoJ favoured global liquidity and bond performance, especially those under the asset purchasing programme and high-yield bonds. Besides, the inflation outlook was dampened by the weakness in oil prices and favoured bond prices. Besides, further depreciation of euro and yen on monetary easing stance from ECB and BoJ is expected, hurting the total return from a currency prospective although yields of euro and yen denominated bonds benefited. The RMB weakened on PBOC's rate cut.

Further enhancement of major central banks' easing policies is likely to support bond performance and the yield spread might narrow further. The persistence in USD strength will hurt the performance of non-USD-denominated bonds from a currency prospective, neutralising certain gains from yield decline. In addition, the rally of USD plus PBOC's rate reduction may hinder the upside of RMB, but due to relatively high real interest rate of China, RMB is still having a relative rate advantage over other major currencies. We hold a SLIGHTLY NEGATIVE view for bonds overall due to the limited room for rate reduction, but we are slightly positive for RMB bonds on the potential upside of the RMB.

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