BCT MARKET OUTLOOK

As of Jan 2021

BCT 銀聯集團

Bull market returns, stock market is expected to rise

Investment Markets	BCT's Investment Views	Summary
Equities	Overweight	
US	Neutral	We are neutral on the U.S. equities. Looking ahead, economic recovery in 2021 and earnings improvement should be supportive. However, investors should be mindful of excessive valuations and explore rotation towards quality value and cyclical stocks.
Europe	Neutral	We are neutral on European equities. We stay mildly optimistic as a vaccine rollout should support normalisation of the economy. However, investors should remain focused on businesses with potential for long-term earnings growth and resilient business models.
Japan	Overweight	We are positive on Japanese equities. The pro-cyclical market, with a large share of industrials and consumer discretionary sector, should benefit from an economic rebound as well as close trade linkages with China.
Asia ex Japan	Overweight	We are positive on Asian ex-Japan equities. We remain constructive in light of potential large-scale vaccine availability and as investors put more money to work away from low remunerating assets.
China & HK	Overweight	We are slightly positive on China equities. Fundamentals are favorable for stocks thanks to robust earnings growth, targeted policy supports and positive development of COVID-19 vaccine. We are neutral on Hong Kong equities. We do not expect Hong Kong market to outperform as COVID-19 restrictions are still in place, which may dampen the local consumption and economic activities.
Global Bonds	Overweight	
Government Bonds	Neutral	On government bonds, we are now neutral. We expect the upward movement in yields to continue due to tactical factors. The sell-off will remain limited as fundamentals still point to low levels of rates. On corporate bonds, we are positive. The hunt for yield remains supportive of credit and peripheral debt, even if the extra returns seem limited.
Credit	Overweight	

Scales of weighting	Underweight	Neutral	Overweight

U.S. EQUITIES

Lifted by the U.S. elections and the rise in interest rates, the S&P 500 returned positive in December, with +3.8%, closing the year at +18.4%. December U.S. Purchasing Managers' Index (PMI) signaled a marked improvement in operating conditions across the U.S. manufacturing sector with the reading moving to 57.1 in December. Manufacturers reported a strong end to 2020 although slowing as post-election exuberance has been challenged by the recent rise in new COVID-19 cases and related restrictions. December reading for unemployment was 6.7%, which was stable compared to November data. On the inflation side, although in November the Consumer Price Index remained stable at +1.2%, the recent rebound in energy prices and the rollout of vaccinations against the COVID-19 is fueling expectation for higher reading in December. Asset purchases at the current monthly pace of 120 billion US dollar will continue until substantial further progress has been made towards maximum employment and price stability goals.

With unemployment expected to reach 4.2% and inflation at 1.9% at the end of 2022, a gradual asset purchase tapering could start in 2022. We see policy rates remaining at the zero lower bound until 2024. Jerome Powell warned that it would take time to get to an overshoot of inflation given significant disinflationary forces. After an extraordinary GDP rebound in Q3, we expect a significant deceleration in the last quarter, which will also be influenced by the new rise in COVID-19 cases. However, the potential weakness in Q1 2021 could be partially offset by the implementation of the new fiscal package which, along with expansionary monetary policy, will provide a key support to economic growth in 2021. The "blue wave", with the Democrats taking control of the Senate should further support the rotation towards value themes. It has to be monitored for the potential effects on taxation and legislation on big corporations. We are neutral on the U.S. equities. Looking ahead, economic recovery in 2021 and earnings improvement should be supportive. However, investors should be mindful of excessive valuations and explore rotation towards quality value and cyclical stocks.

EUROPEAN EQUITIES

European bourses ended the year on a positive note, with the MSCI Europe up +2.2%, posting +10.3% on a year-to-date basis. December Eurozone PMI improved and moved to 55.2. The Eurozone manufacturing finished the year on an encouraging tone, with an acceleration of the production growth thanks mainly to the demand for German goods, which drove most of the increase in Eurozone. Employment continued to be cut with higher forecast for the unemployment numbers. On the inflation side, the Eurozone annual inflation was -0.3 % in the last November release, which was stable compared to October. The package delivered by the European Central Bank (ECB) combined an increase in and nine-month extension of the Pandemic Emergency Purchase Programme (PEPP) and an extension to the Targeted Longer-Term Refinancing Operations with a broader scope and confirmed favourable terms. The European Union (EU) signed with China the EU-China Comprehensive Agreement on Investment, a treaty offering safeguards to EU companies offering production to China and insuring EU and Chinese investors a better access to both regions.

Q4 is set to print a new GDP contraction, as new rises in COVID-19 cases have pushed Eurozone governments to implement new lockdowns. The vaccination campaign should lift sentiment, but herd immunity will likely be reached only from the second half of 2021, when we expect pent-up demand to be released and support above potential growth. Inflation should remain subdued in the near term before moving gradually higher, but will remain significantly below target. The recent increase of energy prices should be reflected in the next inflation reading. A longer-than-expected extension of the PEPP into Q1 2022 looks consistent with both the size and duration of the stimulus. The ECB will maintain favourable funding conditions for the time needed for economic growth to recover from the pandemic crisis. We are neutral on European equities. We stay mildly optimistic as a vaccine rollout should support normalisation of the economy. However, investors should remain focused on businesses with potential for long-term earnings growth and resilient business models.

JAPANESE EQUITIES

The MSCI Japan advanced by +3.1%, on hopes of the vaccination programme and an economic recovery. Despite extreme market conditions over the year, Japanese stocks ended the year higher, posting +8.8%. The Bank of Japan (BoJ) extended its special programme to support financing till September 2021. The programme combines the quota for purchases of Commercial Paper and corporate bonds into a total of 15 trillion yen, and removes the upper limit of 100 billion yen on special lending provided by financial institutions to each counterparty. Furthermore, the Government approved an additional spending budget of 30.6 trillion yen in fiscal spending, which will be funded by the third extra budget and the initial budget for fiscal 2021. The package includes a two-month extension of special measures, aiming to boost financial assistance to firms impacted by worsening business conditions during the pandemic; help local governments cover losses suffered by restaurants and financial support for medical institutions.

The winter pandemic outbreak has prompted us to downgrade Japan's GDP growth forecasts for the next quarters. However, we don't expect the economy to fall into outright contraction again, given the relatively low infection rate and limited deterioration in mobility data. We are not forecasting its economy to return to its pre-COVID level until the end of 2022. The deep negative output gap will keep inflation at a subdued level. The BoJ will review its monetary easing to ascertain whether it is effective and sustainable, and will release the results in March 2021. But there will be no change of the "Quantitative and Qualitative Easing with Yield Curve Control" framework. We are positive on Japanese equities. The pro-cyclical market, with a large share of industrials and consumer discretionary sector, should benefit from an economic rebound as well as close trade linkages with China. In general, the high operating leverage of businesses in Japan should be positive for profit margins as a result of higher sales in 2021.

ASIA EX-JAPAN EQUITIES

As investors were in a risk-on mood over the month, Asian equities were positive and the MSCI Asia ex-Japan advanced by +6.0%, in local currency terms. The Asian region was leading the pack this year, with the index displaying +22.4%. South Korea was the top performer, benefiting from an increase of technology demand, and its strong vaccination programme. The economy showed an accelerating momentum in its export industry, with the export orders PMI advancing to 54.6 – the highest level since March 2011. It was followed by Taiwan, driven by the technology sector as well. On 4 December the Reserve Bank of India (RBI) decided to keep its policy repurchase rate unchanged at 4.0%, together with an accommodative stance for as long as necessary, in order to support the economy.

The Indian inflation outlook was revised upwards, with headline inflation within the central bank target soon. While the official short-term inflation outlook is coherent with our internal forecasts, we do expect an overall higher inflation (between 5.5%-6.0%), and no further easing by the RBI. In Indonesia, in the near term, we do expect some volatility, especially with the recent stricter social restriction imposed on certain regions of the country. In Singapore, we believe that the country's strong fiscal position will be able to tide the economy over. We consider that Asian growth could outperform other regions in the first half of 2021, offering selective opportunities. In the mid-to-long term, we remain constructive on the region despite 2020 strong performance, and we aim to play laggards. We are positive on Asian ex-Japan equities. We remain constructive in light of potential large-scale vaccine availability and as investors put more money to work away from low remunerating assets.

CHINA & HONG KONG EQUITIES

In December, the MSCI China advanced by +2.6%, but the performance was capped by the continuity of the U.S.-China tensions. However, the index progressed by +28.1% in 2020. Chinese exports and industrial production growth was more resilient than expected. The domestic recovery is broad-based and increasingly driven by private demand and the services sector. The headline CPI was dragged down by declining pork prices. Core inflation had bottomed out and held positive. Trump administration blacklisted China's top chipmaker,SMIC, and about sixty more Chinese firms, arguing that those companies exploited U.S. technology for negative purposes. In addition, China's antitrust measures against large internet companies tightened up. China's regulator launched an investigation into Alibaba, which was suspected of monopolistic acts. The MSCI Hong Kong went up in December (+5.0%) and in 2020 (+5.4%). As the local pandemic situation remains challenging, the government announced an extension of social distancing measures. The vaccination campaign should start in February. Hong Kong CPI remains in deflation territory and fell by -0.2% year-over-year in November. The labour market improved, with seasonally adjusted unemployment rate eased slightly to 6.3%.

Solid November data and the reported surge in electricity demand in Southern China in December suggest that Q4 GDP growth is tracking higher than our forecast of 5.5% year-over-year. The headline CPI should stay transitorily negative until March 2021. The annual Central Economic Work Conference suggests that China will continue its policy normalisation in 2021, but avoid an abrupt exit from policy stimulus. Money supply and aggregate social financing will grow "in line" with nominal economic growth. We do not expect any immediate rate hike in 2021. Assuming largely stable macro leverage ratio, we expect total social financing growth to slow from 13.7% at end-2020 to 11.6% end-2021. We are slightly positive on China equities. Fundamentals are favorable for stocks thanks to robust earnings growth, targeted policy supports and positive development of COVID-19 vaccine. We are neutral on Hong Kong equities. We do not expect Hong Kong market to outperform as COVID-19 restrictions are still in place, which may dampen the local consumption and economic activities.

GLOBAL BONDS

Despite rising infection rates and a new variant of the COVID-19 virus emerging, financial markets ended 2020 on an optimistic note. This optimism was driven by the rollout of COVID-19 vaccine programmes and expectations for a U.S. fiscal stimulus. Against this backdrop, corporate bonds outperformed government bonds. The U.S. curve steepened with the main move seen in the belly of the curve: the U.S. 2-year yield fell approx. -0.03% from end-November. Further on the curve, the U.S.-10 year yield finished the year at +0.92% after having moved to +0.84% at the end of November. Having started the month at -0.57%, the German 10-year remained stable until the end of the year. Over the month, the German 2-year yields rose approx. +0.03% to -0.72%. The JPM Emerging Markets Bond Index Plus Composite generated a positive performance during the month appreciating by +2%.

The Q3 rebound in GDP numbers was stronger than expected, but renewed lockdowns due to the second wave of COVID-19 infections could affect economic activity in the first quarter of 2021. On the vaccine front, a large-scale rollout and accommodative policies, as put in place by the ECB at its latest policy review meeting, should drive a recovery in global GDP in the second part of the year, providing a supportive environment for risky assets. However, in credit, there is a wide gap between valuations and fundamentals. So, we recommend investors to balance their search for yield with quality credit through strong research and selection. On government bonds, we are now neutral. We expect the upward movement in yields to continue due to tactical factors. In our central case scenario, the sell-off will remain limited as fundamentals (central bank's stance, growth outlook) still point to low levels of rates. On corporate bonds, we are positive. The hunt for yield remains supportive of credit and peripheral debt, even if the extra returns seem limited. We favour investment grade names as supported by purchasing programs. The expected tightening is very limited, but we recommend to maintain the exposure for carry purposes.

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