The Way We See It

March 2023
Issue 14

Goji Consulting Limited

enquiry@goji-consulting.com

INSIDE THIS ISSUE

Will 2023 Shine? Probably, but watch the Fed and corporate earnings revisions.

A brief update report which serves to review the recent market development and to offer our outlook for the rest of the year and beyond.

Review of Developments
- Global Economies

Key US, European, Japanese and Chinese leading and coincident economic data showed that major economies are likely to continue to grow, albeit at different speeds, and supported by different sectors. In G7 nations, goods prices have seen a welcome mild decline, but wages' inflationary pressures in the services and manufacturing sectors persisted, exerting pressure on both headline and core inflation data.

The overall global macroeconomic setting shows a mixed picture.

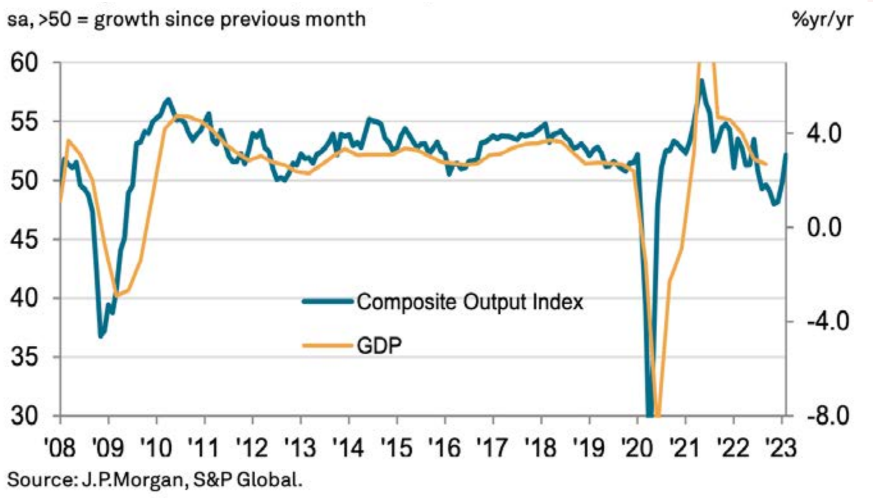
First, from a growth perspective, boosted by solid employment and wage gains which are partially offset by a higher cost of living, consumption growth trends in G7 nations appeared to be normalising and heading towards their long-term equilibrium growth path. On the capital expenditure side, one should expect a mild pick-up of activity as companies are likely to spend more on A.I. and automating their workflow process, in order to reduce their fast-rising wages bill and to deal with the persistent shortage of workers.

Second, China's more relaxed Covid measures, together with its economic reopening and a less restrictive policy towards the property sector, have resulted in a modest pick-up in economic activity.

Market panics and projects a higher Fed fund rate.

Negative newsflows include a much higher US January inflation and growth data, released in the month of February. Hence, investors again fretted about the persistently high cost of living, a hawkish US Federal Reserve and other G7 central banks (Fed fund rate is projected to be raised by 25-50bps in their March FOMC meeting to 4.75-5.25% p.a.), continuing downgrades in global GDP and corporate sales and earnings, and no let up in the war between Russia and Ukraine.

J.P.Morgan Global Composite PMI™



Source: J.P.Morgan, S&P Global

- Global Markets

The month of February saw a correction in risky and economic-sensitive assets (including long-dated bonds), following a strong rally in the previous month.

As investors bought heavily in January to re-balance their underweight positioning in risky assets, the higher-than-expected US inflation and growth data forced a re-thinking of the optimistic interest rate and equity scenario. Taking the new data into account, some investors (particularly those in the Fundamental camp) took some profit in both equity and bond asset classes.

In Global Equities, profit-taking in China and Emerging Markets sent these markets down to a larger extent than the US and other developed markets.

Global Fixed Income markets also suffered from some profit-taking, impacted by the stronger macroeconomic data, as discussed above. Cash out-performed bonds.

Despite favourable growth data coming out from China, the Commodities complex ended the month lower, following other risky and economic-sensitive assets down.

The US Dollar bounced back modestly, boosted by the more cautious sentiment of global investors, as well as the widening interest rate spread, in favour of the U.S.

All major asset classes pulled back in the month of February.

Near-term performance of various asset classes

as at 28/2/2023

Asset Class	US Equities	Global Equities	GEM Equities
Index	MSCI USA	MSCI World	MSCI EM
1 month	-2.39%	-2.37%	-6.48%
3 months	-2.08%	0.17%	-0.45%
YTD	4.04%	4.57%	0.92%
FY 2022	-19.46%	-17.73%	-19.74%

Asset Class	US Corporate	US Treasury	US Aggregate
Index	Bloomberg US Corporate	Bloomberg US Treasury	Bloomberg US Agg
1 month	-3.18%	-2.34%	-2.59%
3 months	0.26%	-0.41%	-0.04%
YTD	0.70%	0.11%	0.41%
FY 2022	-15.76%	-12.46%	-13.01%

Asset Class	Global Govt Bonds	Global Aggregate	Global Commodities
Index	Bloomberg Global TSY	Bloomberg Global Agg	CBR
1 month	-3.56%	-3.32%	-2.97%
3 months	0.12%	0.39%	-3.55%
YTD	-0.59%	-0.15%	-2.97%
FY 2022	-17.47%	-16.25%	19.53%

Asset Class	Asia ex Japan Equities	China Offshore	China A
Index	MSCI AC AxJ	MSCI China	MSCI China A Onshore
1 month	-6.81%	-10.37%	-4.00%
3 months	0.71%	5.40%	7.90%
YTD	0.85%	0.18%	5.98%
FY 2022	-19.35%	-21.80%	-27.09%

Source: GOJI, MSCI, Bloomberg

Market Outlook
- Global Economy

While there are both positive and negative factors operating in the US and the world economy, the potential growth positives are likely to narrowly win out, but not by much, in the first half of 2023. The second half may feel the adverse impact of past monetary tightenings and a potential normalisation of consumption to a more modest growth path.

Tug-of-war remains; positives to win out marginally in H1.

Positives in the first half include: solid employment is likely to continue to boost GDP growth in the US, together with modest increased spending by the government and corporates. In China, the gradual re-opening of its major commercial cities and potential easing of Covid rules, combined with a modest easing of fiscal and monetary policies should help to modestly boost its GDP from 3.5% in 2022 to about 5% this year. In addition, as the majority of countries have started to re-open and encouraged tourists and foreign workers to return, this will add to GDP growth and help to alleviate the shortage of labour in many countries.

On the negative and risk side, should the Fed continue to tighten too aggressively in order to tame inflation within a short time frame, the US economy may not escape a recession scenario in the coming 6-12 months. Other negative factors again focus on still-elevated inflation, still-tight global monetary policy tightening, and continuing selective supply bottleneck issues on certain specific production components, in particular labour. High inflationary pressures are likely to force central banks in major OECD countries to continue to raise rates in coming months. In addition, while supply-side bottlenecks appear to ease a little, the complete suspension of gas and oil exports from Russia to Germany and other European countries could continue to hurt their economies. Lastly, the difficulty in finding workers to fill low-skilled services jobs in major economies continued to cause unfavourable imbalances in demand and supply.

In brief, the world economy is expected to grow modestly in the first half. Having said that, one must acknowledge that, after a decade of almost zero interest rates and trillions of QE and fiscal pumping, the abrupt reversal of these super-easy monetary and fiscal policies could cause unexpected financial crises and/or recessionary conditions. The world economy, in our opinion, remains fragile (financial accidents can happen !).

The Way We See It

- Global Markets and Investment Thematics

The above economic, monetary, and geopolitically unbalanced backdrop is expected to prevail in 2023. Please refer to our 2023 Annual Investment Outlook document for a more comprehensive discussion, analysis and scenario-building.

In the short-term, we continue to think that it would be sensible for investors to continue to adopt a modestly defensive to neutral-risk strategy. This translates into a strong focus on quality and lowly-geared assets that can deliver predictable cash flows, and, until the Fed's Chairman, Jerome Powell, truly pivots from tight to pause/ease, investors could consider holding a mild overweighting in US-dollar-denominated Treasuries and Investment Grade corporate bonds.

GOJI's view remains - modestly defensive to neutral-risk strategy.

In terms of geographical diversification, it appears that it may pay to be neutral in the US versus other global equities. This is based on the differing growth and liquidity trends across the globe, which favour the rest of the world over the US.

From an investor's sentiment and positioning perspective, while they have recently increased their equity' and other risk assets' weighting based on the expectation of peak inflation and interest rates, both Quantitative- and Algorithm-focused and Fundamental investors remain modestly underweight risk assets. Interestingly, a number of Fundamental investors took profit in February, influenced by the higher-than-expected US inflation and growth data.

Discretionary vs Systematic Equity Positioning

*Wtd average of Z-scores for positioning indicators, weights based on explanatory power in regression of equity performance on indicators

Source: Deutsche Bank Asset Allocation

Technical: S&P500 shows a positive signal of "Golden Cross".

In this month, we wish to add a technical chart of the leading risk index in the world, the US-based S&P 500 stocks index. It shows that the index has been gradually rising since October 2022, within a volatile upward-trending trading range. Importantly, the 50-day moving average has crossed the 200-day counterpart on their upward trends, an event which is labelled a 'Golden Cross'. The latter is a positive signal (as long as they trend upwardly), suggesting higher prices ahead on a medium-term basis.

S&P 500 Stock Price Index

Source: Yardeni Research, Inc.

To summarise, it remains our strong belief that a sustainable bull market in equities and corporate bonds will return at some stage. But it would only occur when valuations fall further to reflect the US and global sluggish growth trend, and, more importantly, when the US Fed and other major central banks switch from the current tightening to a pause, or an easing mode. In the meantime, due to continuing macroeconomic uncertainties in the global economy, markets are likely to remain volatile. Consequently, a modestly defensive and quality-focused investment strategy should remain the foundation of risk-averse investors.

GOJI CONSULTING LIMITED

Level 34, Tower One, Times Square
1 Matheson Street, Causeway Bay, Hong Kong

www.goji-consulting.com

enquiry@goji-consulting.com

+852 3951 0359