The Way We See It

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INSIDE THIS ISSUE

1. Review of Developments
2. Market Outlook
3. The Way We See It

Will 2023 Shine? So Far So Good, But…

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 and Asia Pacific leading and coincident economic data continued to show that major economies are growing, but at a relatively subdued pace. In G7 nations, goods prices have seen a welcome mild decline (until OPEC recently announced a cut in oil supply). However, wages' inflationary pressures in the low-skilled services sectors persisted, thus continuing to keep both headline and core inflation rates higher than desired.

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 (including higher mortgage costs), 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 rising wages bill and to deal with the persistent shortage of low-skilled 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.

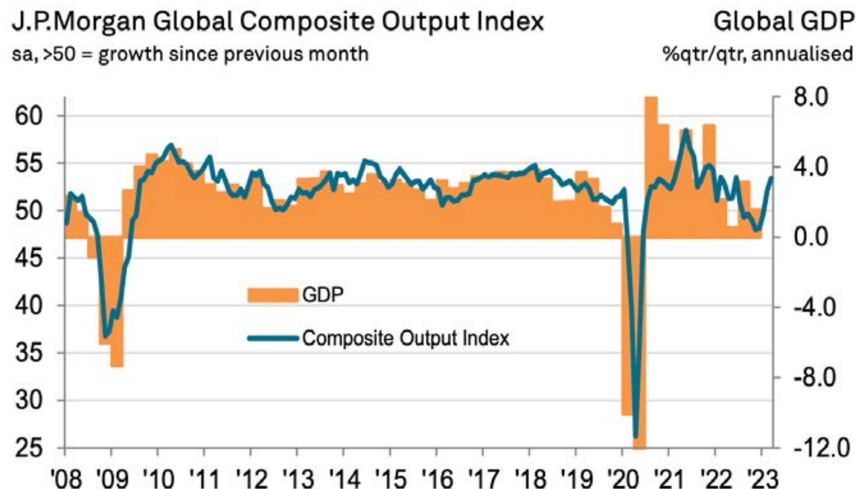
Negative newsflows include the recent turmoil in the U.S. and global banking sector, a threat which we consistently highlighted in our recent monthly reports. The announcement of defaults and shutdowns of a number of banks around the world, starting with the well-publicised collapse of two U.S. regional banks, Silicon Valley Bank and Signature Bank. This was immediately followed, in Switzerland, by the forced purchase of the collapsing Credit Suisse by UBS. As a result of a concerted and swift rescue operation by the US and Swiss governments and their monetary authorities, a US and global banking crisis was averted. The bitter memories and subsequent lessons of the 2008-09 GFC are fresh in everyone's mind.

For months we have been saying "financial accidents can happen".

Other adverse newsflows during the month include the continuing tightening of monetary policy by G10 nations (except Australia), despite the threat of the pervasive global banking crisis. It is interesting to note that while the US Fed and other OECD central banks continued to emphasise that their domestic core inflation remains too high, which thus should have negated any hope of rate cuts this year, the market thinks differently: the latter already started to price in rate cuts, starting from August onwards. They reason that the current threat of a global banking crisis, together with decelerating inflation and a low-growth economy, will force a change of direction by the Fed and its OECD counterparts.

The last macro risk is geopolitical: the continuing war between Russia and Ukraine, and the potential eruption of geopolitical and semiconductor chips' trade tensions between the U.S. and its partners against China into something broader and more damaging.

J.P.Morgan Global Composite PMI™



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

- Global Markets

After a weak February, the month of March saw a more confident and bullish investor. As a result, we saw a solid rally in risky and economic-sensitive assets (including long-dated bonds).

The lower-than-expected US inflation data in February, together with the effective and rapid backstopping and supply of liquidity to their troubled banks by the U.S. and Swiss governments and monetary authorities, prompted investors to think that a pause in the tight U.S. monetary policy is close at hand.

Most asset classes rebounded in March, amid turmoil in banking sector.

In Global Equities, the U.S. led, boosted by investors' renewed interest in the dependable high-growth Technology, Semiconductors and Social Media/ Internet sectors. Other equity markets, including Asia, HK-China and other Emerging, also participated in the global positive investment environment.

Global Fixed Income markets performed well. They were positively supported by the decelerating inflation trend and the hope that the Fed and other G7 central banks are close to implementing a pause in their interest rate hiking cycle. Cash under-performed bonds.

Despite favourable growth data coming out from China, the Commodities complex again ended the month lower in March (the announcement of a cut in oil production by OPEC was made in April).

The US Dollar fell over the month. It was affected by the market belief that the Fed is close to pause its rate hiking cycle, and that it will cut rates in the second half.

Near-term performance of various asset classes

as at 31/3/2023

Asset Class	US Equities	Global Equities	GEM Equities
Index	MSCI USA	MSCI World	MSCI EM
1 month	3.55%	3.16%	3.07%
3 months	7.73%	7.88%	4.02%
YTD	7.73%	7.88%	4.02%
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	2.78%	2.89%	2.54%
3 months	3.50%	3.00%	2.96%
YTD	3.50%	3.00%	2.96%
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	3.70%	3.16%	-0.78%
3 months	3.08%	3.01%	-3.61%
YTD	3.08%	3.01%	-3.61%
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	3.51%	4.52%	0.08%
3 months	4.39%	4.71%	6.07%
YTD	4.39%	4.71%	6.07%
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. Unless there is a sudden change in the Fed's monetary policy, the second half may feel the adverse impact of past monetary tightenings and a potential normalisation of consumption to a more modest growth path.

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 ledger, the market consensus believes that the threat of a US recession developing in the second half remains high. This risk is compounded by the recent U.S. banking turmoil, continuing tight monetary policy, shortage of low-skilled workers in the services sector, and the escalation of trade tensions between the U.S. and allies against China (semiconductor chips, other technology-related sectors). Lastly, the recent spike in energy prices, which result from the OPEC oil production cut, is a tax on consumers and businesses.

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 has and is likely to continue to cause unexpected financial crises and/or recessionary conditions. The world economy, in our opinion, remains fragile (financial accidents have and can continue to happen !).

The world economy remains fragile.

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.

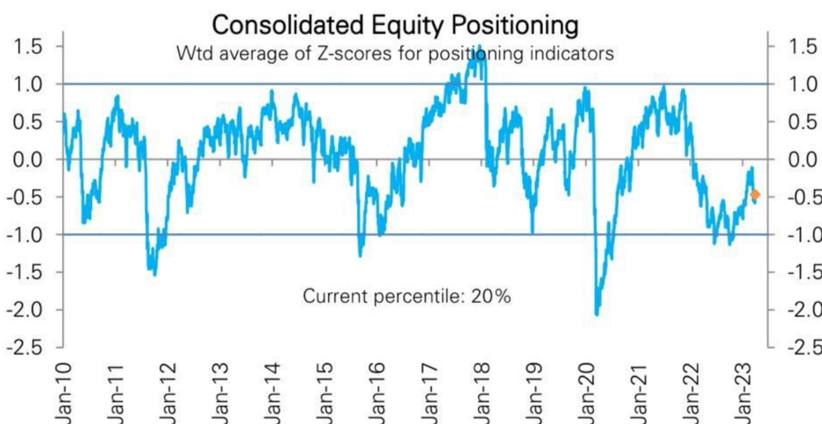
GOJI's view - sensible to adopt a neutral-risk strategy.

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

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 been increasing 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.

Consolidated Equity Positioning



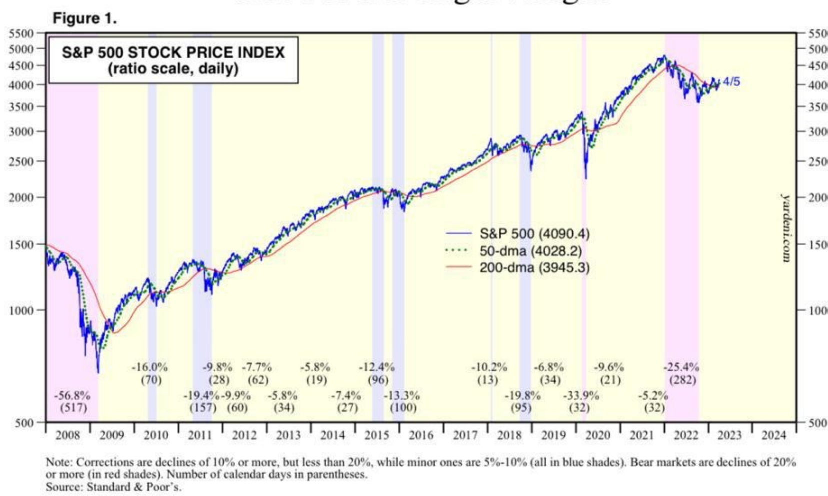
Source: Deutsche Bank Asset Allocation

In this month, we wish to continue to share 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

S&P 500 Moving Averages



Source: Yardeni Research, Inc.

US:SPX | Simple Moving Average EDIT × | Volume × | MACD EDIT ×

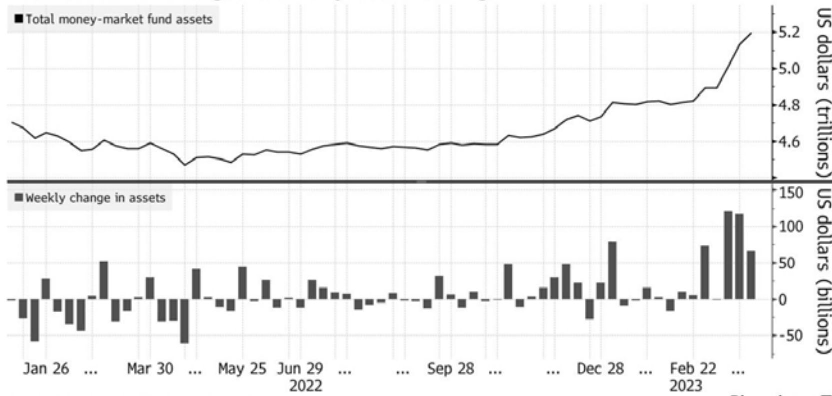
DISPLAY TOOLTIP

SMA(50,200)

Source: MarketWatch.com

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

When Uncertainty Grows, Where the Money Goes?



Source: "*Money-Market Fund Assets at Record $5.2 Trillion as Rates Beckon*", Bloomberg.com, 31 March 2023.

Massive inflow into MMFs - for better return, and for safety.

When uncertainty grows, investors put their money into money market funds for safety, and that is exactly what is happening now.

This massive inflow into money market funds aims to not only achieve a higher return than bank deposits, but also greater safety. This applies particularly to those money market funds which only invest in Treasury bills.

The inflow into money market funds appear to be coming out from bank deposits. Should this phenomenon continue unabated, there is a greater risk that even large systematically important banks can encounter liquidity issues. The only solution is thus for the Fed to either resort to QE again, and/or cut rates significantly and implementing QE simultaneously.

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 neutral-risk and quality-focused investment strategy should remain the foundation of risk-averse investors.

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