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2024 Market Outlook &
Investment Strategy
March Version





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2024 Market Outlook & Investment Strategy March 2024

Core views

- **Global economy** | Against the backdrop of consistent cooling of inflation, the US economy did not weaken, but continued to show signs of recovery in numerous aspects. Although the US inflation is steadily approaching the policy target, there is no immediate urgency for the Fed to lower interest rates. According to statements made at the FOMC meeting in January, the Fed is seeking more data to bring greater confidence that inflation has sustainably come down to its 2% target. Therefore, there is a low chance for the Fed to start an interest rate cut in March, and the market has maintained its basic expectation of only three interest rate reductions in 2024. Despite the potential “soft landing” or even “no landing” scenarios of the US economy as evidenced by numerous economic data, there are undercurrents in the US financial system, especially the risks of insufficient credit provisions in the commercial real estate sector for small and medium-sized banks. In addition, according to the Fed’s Chairman Jerome Powell and the US Secretary of the Treasury Janet Yellen, they both acknowledged the severe impact imposed by surging vacancy rates and refinancing costs on the commercial real estate and the banking industries’ exposure to related credit risks. In case that the US economy is truly healthy and will move upward from now on, then the current inversion of the US bond yield curve should return to normal on a bearish path, but such scenario has never occurred in history. Whether it will be a different case this time round, the market will wait and see. Furthermore, the market is paying closer attention to the inflation and economic conditions in the Eurozone to deduce the timing of the ECB’s interest rate cut. With respect to the inflation, the CPI and the core CPI in the Eurozone slowed to 2.8% and 3.3% respectively year-over-year in January, and the overall inflation gradually moved towards the ECB’s target level. From the economic aspect, the Eurozone GDP was flat quarter-over-quarter in Q4, 2023, thus avoiding a technical recession, but its economic growth in 2023 reached only 0.5%, slightly lower than the EU’s forecast in November 2023. The composite PMI in the Eurozone rose to a 6-month high in January, but still failed to escape from the trend of contraction. In the near term, the market is still undergoing the adjustment period for the timing of interest rate cuts, and whether the inflation can further fall back to the ECB’s target has become a crucial factor in adopting interest rate cuts. On February 15, the data released by the Office for National Statistics of the UK showed that the UK economy grew by 0.1% year-over-year in 2023, lower than the market’s expectations. On the supply side, the output of the three major industries all experienced declines. In particular, the service industry, manufacturing industry and construction industry declined by 0.2%, 1.0% and 1.3% respectively. On the demand side, net exports, household spending and government consumption experienced declines. Nevertheless, the capital investment growth driven by business investment has offset part of the economic declines, and provided a buffer for the economic downturn. Since 2024, amid expectations of interest rate cuts, the UK economy has shown signs of recovery. Driven by the recovery of the consumer confidence and the rebound of the real estate and service industries, and coupled with the low base effect in Q4, 2023, the UK economy is expected to achieve a quarter-over-quarter growth of 0.2% in Q1, 2024. In China, the demands still showed no signs of improvement in January. The PBOC lowered its RRR, highlighting its policy stance on stabilizing growth. China’s manufacturing PMI reached 49.2 in January, and the non-manufacturing PMI amounted to 50.7, whereas the composite PMI reached 50.9. The recovery on the production side remained better than that on the demand side, and China has experienced accelerated recovery in external demands. In January, the CPI fell by 0.8% year-over-year, and the core CPI rose by 0.4% year-over-year, hitting a record low since July 2023. The PPI fell by 2.5% year-over-year, and maintained the trend of declines month-over-month. China’s CPI is still dragged down by food prices year-over-year. Moreover, the year-over-year increase in core CPI has narrowed, indicating that consumer demand remains weak. The scissors gap between the PPI and the CPI in January narrowed by 0.7 percentage points from the previous month. It is expected that the recovery of corporate earnings will remain unchanged. Since January, the authority has stepped up efforts in rolling out macroeconomic policies. Taken together, China’s domestic fundamentals are still recovering moderately, but the strength of recovery is still weak. Due to the consistent introduction of macroeconomic policies to stabilize growth, China’s economic growth will be supported, but it will take time to restore market confidence. In case that subsequent economic data underperform compared with the market’s expectations, there is still the chance of further intensification of policy efforts.



- **Stock market** | Since early 2024, the US stock market continues to experience a rally. The market has reached a consensus about the Fed's interest rate cuts, and the discrepancy of perception only exists in terms of timing and pace. As such, the outlook on future monetary policy constitutes a driving force rather than a hindrance to the US stock market. In addition, investors expect that the US economy would be able to avoid a recession and maintain strong growth, and corporate earnings will enter into the phase of upward movements at an accelerated pace. This is confirmed by the US economic data at the macro level as well as the financial reports of enterprises at the micro level, thus bolstering the valuation of US stocks and lowering the risk premiums. Nevertheless, the US employment data continued to slow down, and average working hours unexpectedly dropped to a record low since 2020. Moreover, the US stock market has become more dependent on the bolstering effects of AI and chip-manufacturing related stocks. The rally of the US stock index only relies on the contribution of a small number of stocks. In addition, there were more companies with a negative guidance on earnings than a positive one in Q1, 2024. Coupled with a horrific financial report from New York Community Bancorp, depositors may move their deposits once again away from banks, thus triggering a new round of bank runs. Moreover, the long-term US treasury yields have not risen to a significant extent, indicating that the market did not give up hedging against the risks of economic recession. With respect to European stocks, the Stoxx Europe 600 Index tested historical highs in February. The ECB is likely to start its cycle of interest rate reductions, thus supporting the tech stocks to rise by more than 10% since early 2024. Closer attention shall be paid to the ECB's progress of the rate-hike cycle. When the actual process of interest rate cuts differs from the market's expectations, it may lead to market adjustments in stages, which will bring favorable opportunities for investors to arrange asset allocation into European stocks. At present, the market expects the ECB to remain on hold in March. Given that the ECB may start to cut interest rates sooner, the depreciation of the EUR/USD is likely to benefit large companies with a higher proportion of overseas revenue. In addition, the moderate growth of the global economy will benefit large companies that are mainly export oriented. Nevertheless, closer attention shall be paid to the adjustments in expectations for interest rate cuts, which may lead to stock market volatility. With respect to the China A-share market, Chinese mainland's PMI rose slightly, and the Chinese economy experienced a rebound. Commodity supply and sales inventories increased in tandem, and the growth of supply has accelerated. The aggregate financing to the real economy (AFRE) in January was the highest during the same period. Against the backdrop of intensified efforts made by the financial sector to support the capital demands of the real economy, the effects of market stabilization and the Fed's cycle of interest rate hikes may still disturb the China A-share market, which is expected to rise steadily in March. With respect to the Hong Kong, China stock market, the domestic economy continued to experience a weak recovery. The PMI data recovered to some extent, but remained slightly lower than the market's expectations. Moreover, the US economy has shown evident resilience. In particular, the number of new nonfarm payrolls in January exceeded the market's expectations. In the mid-to long-term, there are higher expectations for overseas interest rate cuts. Coupled with Chinese mainland's new round of reserve requirement ratio cuts, the liquidity pressure is likely to ease, thus providing liquidity support for Hong Kong, China stocks to bottom out amid stabilization. However, due to the complex international situation and geopolitical tension, and judging from the domestic economic recovery and policy intensity that were less than expected, the performance of Hong Kong, China stocks may still suffer from a negative impact. With respect to the Japanese stock market, Japanese stocks continue to rise since early 2024, and are close to an all-time high. The stock market rally is mainly attributable to three major factors, namely, compensatory gains, structural reforms of enterprises by the government, and the expected end of the policy of negative interest rates. Japan is at the crossroads of comprehensive transformation, as evidenced by the compensatory gains in the stock market. Moving forward, the sustainability of the stock market rally would depend on factors including the all-round improvement of labor productivity, the ability of enterprises of grasping the industrial trend through their decision-making, the sustainability of profits of listed companies, and the resilience of the Japanese society subsequent to the JPY's appreciation. With respect to Asian stock markets, driven by the moderate growth of the global economy and China's supportive policies, the MSCI AC Asia ex Japan Index bottomed out and experienced a rebound. The Indian stock market outperformed compared with other markets, but closer attention shall also be paid to the consistent net outflow of funds. Due to the launch of the "Enterprise Value Enhancement Plan" by the South Korean government in mid-February, the market starts to associate it with the stock market reform plan launched in Japan in 2023, attracting a large net inflow of funds. The valuation of Korean stocks has been consistently low. In case that the plan is in line with the market's expectations, it could lead to a rally in the Korean stock market. The valuation of Asian stocks is at a discount compared to the US stocks. Driven by the implementation of the aforementioned reform measures, it could enhance the attractiveness of the stock market performance.



- **Bond market** | The peak of the Fed's interest rate is basically certain, but the expectations of a rate cut in Q1, 2024 could be disappointed. The rebound in short-term US treasury yields is likely to provide an opportunity for arranging asset allocation into US bonds. In addition, the expectations of an interest rate cut by the ECB are likely to provide opportunities for investing in European bonds in 2024. At the moment, investors holding sovereign bonds are able to hedge against the risks of recession, which can provide a rather attractive minimum yield. Therefore, European sovereign bonds are likely to have greater advantages in the near term. Against the backdrop of restoration of weak fundamentals, China's bond market needs both constantly easing credit policies to boost demands, and constantly loosening monetary policies to lower nominal interest rates. Coupled with the peak season of institutional asset allocation in Q1, 2024, there is little risk of rising interest rates in China's bond market in March. With respect to the Chinese USD bonds, it is recommended to prioritize asset allocation into long-term investment-grade bonds. Emerging markets are subject to the impact of fluctuations in the USD exchange rate to a significant extent, and pressure in the short term would not affect investment opportunities in the long term.
- **Commodities** | Looking forward to March 2024, the price of gold is likely to become increasingly volatile in the near term due to changes in the interest rate environment driven by the expectations of an interest rate cut by the Fed. Closer attention shall be paid to the US economic data and the pace of the Fed's interest rate reductions. In the mid-to long-term, crucial elections will take place in numerous economies in 2024. The rising risks in the banking sector may prompt the Fed to lower interest rates. The gold purchase demands of central banks are becoming a strong support for gold prices. On the supply side of the crude oil market, the output of the OPEC bloc is expected to remain at a low level in Q1, 2024, but there is a low chance for the OPEC to further increase production cuts, leading to a bearish trend for oil prices. On the demand side, although slower global economic growth leads to lower level of oil demands, demands from developing countries such as China and India have increased, thus bolstering crude oil prices.
- **Foreign exchange** | As mentioned in our previous monthly commentary, the foreign exchange market mainly revolves around the timing and amplitude of the first interest rate cut. As the latest US inflation data experienced a rebound once again, and the employment data was still not bad, there is a lower chance for the Fed to cut interest rates in May. Moreover, there is a lower chance for the Fed to cut interest rates by 75 bps in total throughout the year 2024, thus leading to the strengthening of the USD in February and the weak performance of non-USD markets. Looking forward to March, the market is still expected to focus on the trend of core data. With respect to specific currencies, US dollar: USD is likely to strengthen amid oscillations in the near term due to the dual resilience of inflation and employment data. Euro: EUR is unlikely to be bolstered for the time being due to weakening fundamentals and delayed interest rate cuts. British pound: GBP may hardly achieve ideal performance amid the BoE's slower pivot towards a more dovish stance. Japanese yen: JPY's weakness in the near term will not alter the perception about its strengthening in the medium term. Canadian dollar: CAD has certain potential for upward movements during oscillations amid consolidation. Australian dollar: AUD may become increasingly volatile due to the loosening of hawkish policy stance. Renminbi: RMB is expected to operate within a reasonable range against the backdrop of rather negative factors overseas and mixed performance of domestic economic data.



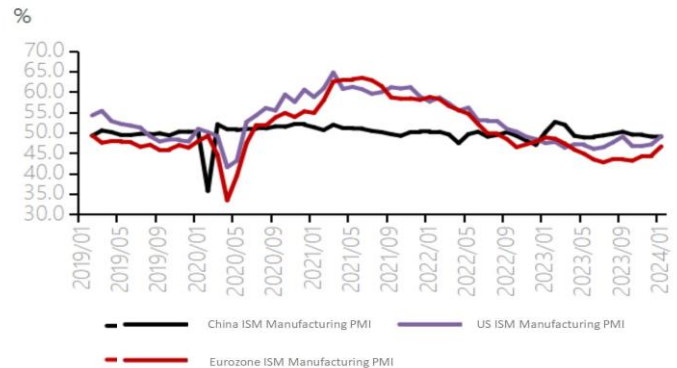
Global Economy

Fig. 1: Monthly CPI YoY (As of January 31, 2024)



Source: Wind, BOC Investment Strategy Research Center

Fig. 2: Monthly Manufacturing PMI YoY (As of January 31, 2024)



Source: Wind, BOC Investment Strategy Research Center

US: Interest rate cuts are unlikely to take place in March, and the financial sector is faced with the threats of undercurrents

Over the recent period, against the backdrop of constantly cooling inflation, the US economic data did not weaken. Instead, it has shown signs of recovery in numerous aspects. First, the real GDP growth in Q4, 2023 reached 3.3% on an annualized quarter-over-quarter basis, far exceeding the expected growth of 2%. Second, the non-farm payrolls in January unexpectedly went up by 353,000, nearly twice the expected number of 185,000. In addition, the employment in December 2023 was revised upward to 333,000, thus breaking the pattern of frequent downward revisions to data in 2023. Finally, soft data verified the recovery of hard data. In January, the IHS Markit Manufacturing PMI and Services PMI both exceeded the market's expectations. The manufacturing PMI reached 50.3, hitting a new high since October 2022. The services PMI reached 52.9, also hitting a record high over the past seven months. The Consumer Sentiment Index of the Chicago Fed rose to the level of 114.8 in January, higher than the expected level 114.5 and the previous value of 110.7.

Against the backdrop of rising economic momentum, Although the US inflation is steadily approaching the policy target, there is no immediate urgency for the Fed to lower interest rates. according to statements made at the FOMC meeting in January, the Fed is seeking more data to bring greater confidence that inflation has sustainably come down to its 2% target. Therefore, there is a low chance for the Fed to start an interest rate cut in March, and the market has maintained its basic expectation of only three interest rate reductions in 2024. Nevertheless, the federal funds rate futures differ from with the Fed's policy guidance, and are still pricing in 5.5 times of interest rate cuts, thus confusing numerous investors. In fact, the expectations implicit in the pricing of interest rate futures do not accurately predict when and how much the Fed will cut interest rates, but shall rather be interpreted as hedging against the risks of economic recession/or financial crisis. This is likely to generate a premium because once the risk incidents break out, the market may force the Fed to cut interest rates at a quicker pace.

Despite the potential "soft landing" or even "no landing" scenarios of the US economy as evidenced by numerous economic data, there are undercurrents in the US financial system. As the financial results of the New York Community Bancorp (NYCB)(with loan loss provisions ten times higher than expected as well as dividend cuts), the share price plunged back to the level in 1997. In addition, the Fed removed the wording that "the US banking system is sound and resilient" from its policy statement seen in each of the FOMC meetings, which has intensified the market's concerns especially about the risks of insufficient credit provisions in the commercial real estate sector for small and medium-sized bank. In addition, according to the Fed's Chairman Jerome Powell and the US Secretary of the Treasury Janet Yellen, they both acknowledged the severe impact imposed by surging vacancy rates and refinancing costs on the commercial real estate and the banking industries' exposure to related credit risks. Although they said that the US regulators were working to ensure that the financial system could cope with the situation, the Fed also said so in 2007 that the subprime mortgage crisis was under control. Nevertheless, one of the worst financial crises in history still took place in 2008. In case that the US economy is truly healthy and will move upward from now on, then the current inversion of the US bond yield curve should return to normal on a bearish path, but such scenario has never occurred in history. Whether it will be a different case this time round, the market will wait and see.



Eurozone: The market is at the period of adjustments for the timing of the ECB's interest rate cuts

The market is paying closer attention to inflation and economic conditions in the Eurozone to deduce the timing of the ECB's interest rate cuts. With respect to the inflation, the CPI and the core CPI in the Eurozone slowed to 2.8% and 3.3% respectively year-over-year in January. In addition, according to the latest consumer expectations survey from the ECB, consumers expect the Eurozone inflation to drop to 3.2% in the next 12 months. This is the third consecutive month of declines and the lowest level since early 2022. Overall inflation is gradually moving towards the target set by the ECB. From the economic aspect, the Eurozone GDP was flat quarter-over-quarter in Q4, 2023, thus avoiding a technical recession, but its economic growth in 2023 reached only 0.5%, slightly lower than the EU's forecast in November 2023. However, other leading indicators pointed to a slight improvement in the Eurozone economic outlook. Although the Eurozone services PMI went down to 48.4 in January, falling within the contraction range for the sixth consecutive month, the manufacturing PMI rose to 46.6 and hit a 10-month high. The constant increase in new orders has improved the conditions of the manufacturing sector and offset the impact imposed by further declines in the services sector. As such, the composite PMI in the Eurozone rose to a 6-month high in January, but still failed to escape from the trend of contraction.

At present, there is still divergence between the ECB's stance and the market's expectations about interest rate cuts. As expected by the market, the ECB kept interest rates unchanged at the FOMC meeting in January. According to the ECB's President Christine Lagarde, the Governing Council believed that it was premature to discuss an interest rate cut, but it also maintained its comment that an interest rate cut could take place in the summer. However, many members of the Governing Council maintained a hawkish stance, and showed divergent views on the timing of interest rate cuts. In addition, the market has seen changes in the timing of interest rate cuts. According to the Bloomberg interest rate futures, the market's expectations that the ECB would lower interest rates at the policy meeting in April have dropped from more than 100% in early 2024 to less than 60% at present. In the near term, the market is still undergoing the adjustment period for the timing of interest rate cuts, and whether the inflation can further fall back to the ECB's target has become a crucial factor in adopting interest rate cuts.

UK: The economy has entered into a mild technical recession, and is likely to recover in 2H, 2024

On February 15, the data released by the Office for National Statistics of the UK showed that the UK economy grew by 0.1% year-over-year in 2023, lower than the market's expectations. The UK economy declined by 0.3% in Q4, 2023, marking two consecutive quarters of declines and entering into a mild technical recession. On the supply side, the output of the three major industries all experienced declines. In particular, the service industry, manufacturing industry and construction industry declined by 0.2%, 1.0% and 1.3% respectively. On the demand side, net exports, household spending and government consumption experienced declines. Nevertheless, the capital investment growth driven by business investment has offset part of the economic declines, and provided a buffer for the economic downturn. Since 2024, amid expectations of interest rate cuts, the UK economy has shown signs of recovery. Driven by the recovery of the consumer confidence and the rebound of the real estate and service industries, and coupled with the low base effect in Q4, 2023, the UK economy is expected to achieve a quarter-over-quarter growth of 0.2% in Q1, 2024.

In early February, the BoE kept its benchmark interest rate unchanged at 5.25%. The central bank removed the wording about further tightening its monetary policy at its policy statement, indicating that the cycle of interest rate hikes has come to an end. Moreover, the BoE estimated that the fall in oil and gas prices could temporarily bring the overall inflation in the UK back to the 2% target in the near term, and more evidence is still needed to support interest rate cuts. The BoE's market guidance for cautious interest rate reductions is in line with the moves of the Fed and the ECB. The inflation rate reached 4% in the UK in January, the same as in December 2023 and lower than the market's expectations of 4.1%. As can be seen, the Red Sea incident did not impose a direct impact on the British economy. The average weekly earnings growth in the UK from September to November 2023 amounted to 6.6%, lower than the growth of 7.9% in the previous three months. Inflation continued to fall, and the job market cooled to some extent, providing greater support for the BoE to cut interest rates. The British government is expected to announce a series of tax cuts in its spring budget on March 6 to bolster public support. Both monetary and fiscal easing measures are likely to boost the British economy in 2H, 2024.



China: Overall demands remained low, and the RRR cut by the central bank highlighted the policy stance towards stabilizing growth

In China, the manufacturing PMI in January reached 49.2, an increase of 0.2 from the previous month, but it has been below the boom-bust line for four consecutive months. The non-manufacturing business activity index in January reached 50.7, an increase of 0.3 from the previous month. The composite PMI output index in January reached 50.9, an increase of 0.6 from the previous month. Among the varying components of the manufacturing PMI, the production index rose by 1.1 to 51.3, and the new orders index went up by 0.3 to 49. Furthermore, the new export orders rose by 1.6 to 47.8. The restoration on the production side remained better than that on the demand side, and China has experienced accelerated recovery in external demands.

In January, the CPI fell by 0.8% year-over-year, and the decline expanded by 0.5 percentage points from the previous month. The CPI went up by 0.3% from the previous month, and the increase expanded by 0.2 percentage points from the previous month. In January, the core CPI went up by 0.4% year-over-year, and the increase narrowed by 0.2 percentage points from the previous month, reaching a record low since July 2023. China's CPI is still dragged down by food prices year-over-year. Moreover, the year-over-year increase in core CPI has narrowed, indicating that consumer demand remains weak. It is expected that from February, the year-over-year CPI growth will return to the positive range. In January, PPI dropped by 2.5% year-over-year and 0.2% month-over-month. PPI continued to decline month-over-month. It is expected that PPI will turn positive year-over-year until Q2, 2024. The scissors gap between the PPI and the CPI in January narrowed by 0.7 percentage points from the previous month. It is expected that the recovery of corporate earnings will remain unchanged.

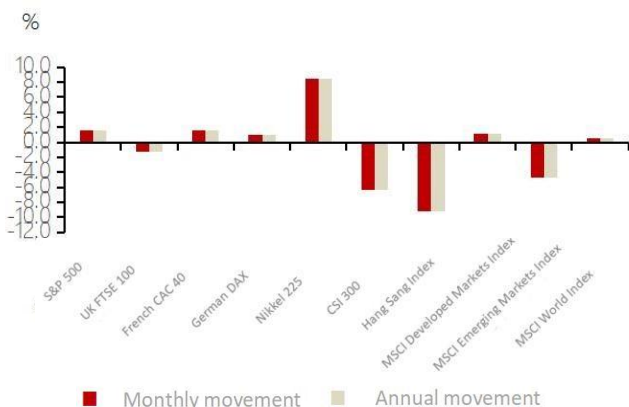
Since January, the authority has stepped up efforts in rolling out macroeconomic policies. On January 24, the PBOC announced a cut of required reserve ratio by 0.5 percentage points, releasing about RMB 1 trillion in long-term funds. The timing and intensity of the RRR cut exceeded the market's expectations, revealing the central bank's intention to strengthen management of expectations. Moving forward, it is expected that subsequent efforts of countercyclical adjustments in monetary policy will not subside, and there is still the chance of targeted adjustments to LPR in subsequent stages. On January 25, according to the statements made by the officials from the National Administration of Financial Regulation at a press conference of the State Council Information Office, "the real estate sector has a long industrial chain and covers a wide range of areas. It could impose a crucial impact on the national economy, and is closely related to the livelihoods of the people. Hence, the financial sector undoubtedly has the responsibility to support the real estate sector". On January 26, the National Administration of Financial Regulation and the Ministry of Housing and Urban-Rural Development held separate meetings to promote the implementation of the urban real estate financing coordination mechanism. Since then, Guangzhou and other municipalities have gradually relaxed restrictions on home purchases.

Taken together, China's domestic fundamentals are still recovering moderately, but the strength of recovery is still weak. Due to the consistent introduction of macroeconomic policies to stabilize growth, China's economic growth will be supported, but it will take time to restore market confidence. In case that subsequent economic data underperform compared with the market's expectations, there is still the chance of further intensification of policy efforts.



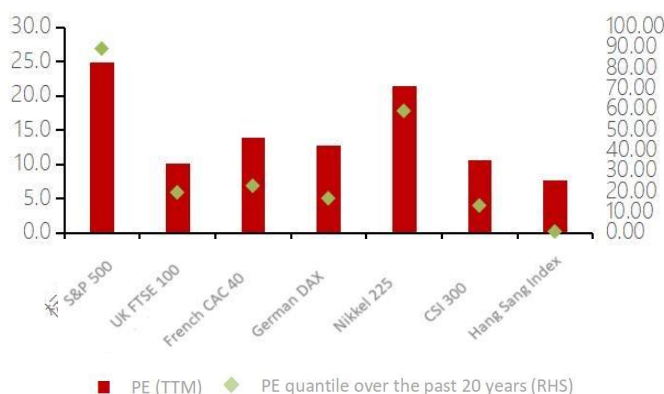
Stock Market

Fig. 3: Stock Index Movements (as of January 31, 2024)



Source: Wind, BOC Investment Strategy Research Center

Fig. 4: Stock Index Valuation (as of January 31, 2024)



Source: Wind, BOC Investment Strategy Research Center

US: The S&P 500 Index hit new highs, and risks of distortion could exist

Except for the declines in the first week, the S&P 500 Index has risen every week since the beginning of the year 2024, and it seems to be only a matter of time before it breaks through the threshold of 5,000 points. Against the backdrop of the consistent slowdown in inflation, the market has reached a consensus about the Fed's interest rate cuts in the next step, and the discrepancy of perception only exists in terms of timing and pace. As such, the outlook on future monetary policy constitutes a driving force to the US stock market, reversing the suppression of stock valuations caused by tightening monetary policy and rising interest rates over the past two years. Varying economic data in the US have risen over the recent period, thus lowering the expectations about the pace of interest rate cuts. Furthermore, the entire US bond yield curve has risen compared with previously. Nevertheless, investors in the US stock market showed no concerns about rising interest rates, and US stocks continue to hit record highs. The key reason is that investors expect US economy would be able to avoid a recession and maintain strong growth, and corporate earnings will enter into the phase of upward movements at an accelerated pace. This is confirmed by the recently strengthening US economic data at the macro level as well as the financial reports of enterprises at the micro level, thus bolstering the valuation of US stocks (one-year forward PE ratio of the S&P 500 Index rose to 20 times) and lowering the risk premiums.

However, the real situation may not be a truly rosy picture. First, there are concerns behind the "strong" economic data. For instance, the employment data (without seasonally adjusted) dropped by 2.635 million in January, but the seasonally adjusted data was raised by 3 million. As long as there is an error of 10% in the seasonally adjusted data, the data could turn negative. The ADP employment continued to slow down, and the new employment based on household surveys continued to show negative growth. The average working hours unexpectedly dropped to a record low since 2020. Second, the breadth of the stock market rally once again decreased. In particular, the YTD return of the S&P 500 Equal-weighted Index only rose by 0.37%, and the Russell 2000 Index even fell by 3.73%. Moreover, the US stock market was more dependent on the bolstering effects of AI and chip-manufacturing related stocks, whereas cyclical stocks and small-cap stocks remained weak. Among companies that have released annual reports, an increasing number of companies have issued negative guidance for financial results in Q1, 2024. In addition, the financial report released by New York Community Bancorp (NYCB) once again sounded the alarm, and the impact of the gray rhino of commercial real estate sector is likely to loom large on the balance sheets of banks. While short-selling forces still exist, depositors with potential concerns are likely to transfer their bank deposits to avoid risks, which might trigger a new round of risk. Finally, in the face of strengthening economic data and investor optimism, the long-term US treasury yields have not risen to a significant extent, and the yield curve remained inverted, indicating that the market did not give up hedging against the risks of economic recession. Before the yield curve returned positive, there is still the chance for cyclical risks to be released in the US stock market.



Europe: Declines of the EUR supported the performance of large companies

The market's expectations have cooled for short-term interest rate cuts by the ECB and the Fed, but the rebound in economic data has increased the chance of a soft landing, thus bolstering the Stoxx Europe 600 Index to test its historical high in February. As the inflation gradually fell back to the target level, and the cycle of interest rate cuts is expected to begin, the downward trend in bond yields has been established, which continued to bolster the performance of the European tech sector. As of the time of writing, the Stoxx Europe 600 TECH Index has risen by more than 10% since early 2024. From the aspect of inflation, it is expected that the ECB will enter into a cycle of interest rate cuts within the year, and it is just a matter of timing. Moving forward, the growth stocks dominated by tech stocks are likely to remain supported in the general direction. Closer attention shall be paid to the timing of arranging asset allocation into the market. When the actual process of interest rate cuts differs from the market's expectations, it may lead to market adjustments in stages, which will bring favorable opportunities for investors to arrange asset allocation into European stocks.

In March, investors shall pay closer attention to the policy statements made by the European and US central banks. Regarding interest rates, the market is now almost certain that central banks will remain on hold. However, due to earlier expectations of interest rate cuts, the EUR/USD has depreciated since the beginning of the year. Given that the income of many large European enterprises mainly comes from overseas, they will benefit during the declines of the EUR. Since January 2024, the EUR/USD has fallen from the level of 1.10. The MSCI Europe large-cap index has always performed better than the small-cap index. Coupled with the mild recovery of the global economy, in case that the demands for new orders continued to rise, it will also support the growth of large export-oriented companies. However, closer attention shall be paid to the potential fluctuations of the stock market subsequent to a rally due to adjustments in the expectations of interest rate cuts.

China: The A-share market bottomed out amid a rebound, and investors shall remain cautious for Hong Kong, China stocks in the short term while paying closer attention to the enhanced cost-effectiveness in the mid to long-term

The China A-share market experienced a rebound amid consolidation in February. The market bottomed out amid a rebound in mid-to-late January, then fell back and bottomed out in February. The ChiNext Index experienced a slight correction at the end of January, then fell slightly and rose back in February. With respect to industry, the majority of sectors experienced declines. In particular, the banking, non-banking finance and household appliances sectors have led the market, and comprehensive, light manufacturing and leisure services sectors have declined the most.

Looking forward to March, the China A-share market may experience the trend of steady upward movements. At the macro level, the PMI rose slightly to 49.2% in January, thus putting an end to the downward trend for three consecutive months, and the level of economic prosperity has rebounded. At the market level, the commodity index went up by 0.4 percentage points from the previous month, and supply, sales, and inventory data all showed an upward trend. In particular, the supply growth has accelerated to a significant extent. With respect to liquidity, RMB 6.5 trillion worth of aggregate financing to the real economy (AFRE) was added in January, hitting a record high in the same period in history, and financial support for the real economy remained at a high level. With respect to risks, the uncertainties in the trend of US interest rates, the direction of the geopolitical tension and the actual effectiveness of market stabilization measures will all impose an impact on the China A-share market in March.

Global stock markets continued to rise in January, and Hong Kong, China stocks underperformed to some extent. With respect to industrial performance, only the energy and telecommunications sectors rose, whereas all other sectors experienced declines. In particular, the healthcare and the consumer discretionary sectors were the top decliners. In February, Hong Kong, China stocks continued to fluctuate amid adjustments.

Moving forward, investors shall remain cautious for the short-term trend of the Hong Kong, China stock market, but shall also take note of the enhanced cost-effectiveness of asset allocation into Hong Kong, China stocks in the mid to long-term. On the one hand, although the PMI data in January recovered, it is still slightly lower than the market's expectations, and Chinese mainland's economy continued to experience a weak recovery. On the other hand, the US economy has shown evident resilience. The number of new non-farm payrolls in January exceeded the market's expectations once again, and there has been an increasing trend for higher overseas interest rates and a stronger USD. In the mid to long-term, there will be increasing expectations for the overseas interest rate cuts. Coupled with Chinese mainland's new round of reserve requirement ratio cuts, the liquidity pressure is likely to ease, thus providing liquidity support for Hong Kong, China stocks to bottom out amid stabilization. With respect to the risk factors, the international situation is complex, and the geopolitical tension is apparent at the moment. Closer attention shall be paid to the potentially inadequate measures of policy easing, which will affect the overall performance of the Hong Kong, China stock market.



Asia ex-China: The outperformance of Japanese stocks is likely to continue, and varying measures are taken to increase the attractiveness of Asian stocks

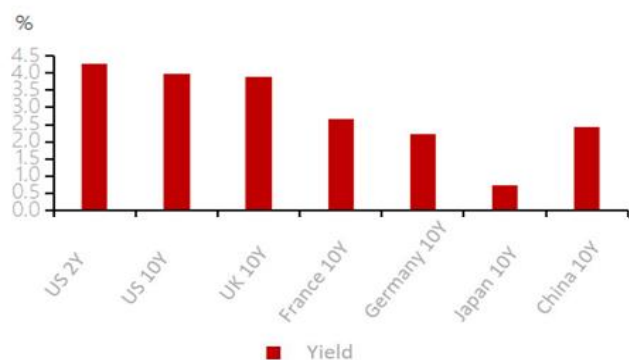
The Nikkei 225 Index has been on a constant rally since the beginning of the year, and reached the level of 38,000 points, which is one step away from the record high of 38,975.44 points hit 34 years ago. Despite the rises, Japanese stocks are still in the stage of compensatory gains. In case that no major changes take place, there is a high chance that Japanese stocks could break through historical highs within the year. Three major factors have bolstered the performance of Japanese stocks. First, as the global economy recovers and technological innovation regains vitality, Japanese stocks will inevitably experience compensatory gains. Second, Japan is undergoing extremely drastic structural reforms from top-level political design to the boards of directors of enterprises. Medium-sized listed companies are competing with each other to increase dividends, buy more treasury stocks, and either proactively or passively adjust the structure of board of directors. The economic benefits and value of Japanese enterprises may experience a turnaround, thus injecting vital impetus to the long-term rally of Japanese stocks. Third, the policy of negative interest rates is expected to come to an end, and the central bank is likely to start the normalization of interest rates. Since then, prices have experience a moderate growth of inflation, and corporate earnings have increased to a significant extent. During the spring wage negotiations, wages have increased by more than 4%, and capital expenditures of listed companies have also increased evidently. Furthermore, corporate and personal wealth have both increased to a significant extent. In addition, the government has expanded the coverage of the tax exemption system for small investments, and encouraged citizens to transfer their bank deposits into holdings of stocks of blue chip companies, which is expected to bring tens of billions of funds to the stock market.

Japan is at the crossroads of comprehensive transformation, as evidenced by the compensatory gains in the stock market. Moving forward, the sustainability of the stock market rally would depend on factors including the all-round improvement of labor productivity, the ability of enterprises of grasping the industrial trend through their decision-making, the sustainability of profits of listed companies, and the resilience of the Japanese society subsequent to the JPY's appreciation.

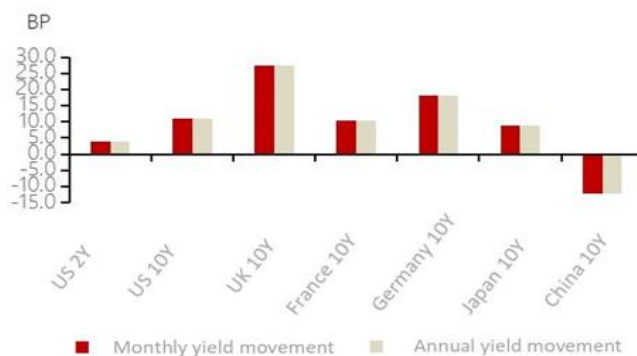
Driven by the moderate growth of the global economy and China's supportive policies, the MSCI AC Asia ex Japan Index rebounded from a low of about 594 points in mid-January and rose above the 200-day moving average of about 621 points in early February. Although the Indian stock market outperformed and hit a historical high, it shall be noted that according to Bloomberg's observations on capital flows, the Indian stock market has recorded net capital outflows for four consecutive weeks in the week ending February 2. On the contrary, due to the announcement by the South Korean government that it would launch the "Enterprise Value Enhancement Plan" in mid-February, the market starts to associate the plan with the stock market reform plan launched in Japan in 2023. As of the time of writing, although the details of the plan had not yet been disclosed, it attracted a net inflow of nearly 25% of the net capital inflows for the whole year of 2023 in the week of February 2, thus stimulating the MSCI Korea Index to rise sharply by more than 5% on February 1 and 2. Korean stocks have long been plagued by the issue of low valuations. In case that the details of the plan could truly increase enterprise value as expected by the market, it may become one of the catalysts for the rise of Korean stocks. The valuation of Asian stocks is at a discount compared to the US stocks. Driven by the implementation of the varying reform measures, it could enhance the attractiveness of the stock market performance.

Bond Market

Fig. 5 and Fig. 6: Government Bond Yields (as of January 31, 2024)



Source: Wind, BOC Investment Strategy Research Center



Source: Wind, BOC Investment Strategy Research Center



Developed markets: The rebound in bond yields is expected to provide opportunities for asset allocation into US bonds, and European sovereign bonds may have greater advantages in the near term

US bonds: At the FOMC meeting in February, the Fed continued to keep interest rates unchanged, and basically confirmed that interest rates already peaked. However, according to the Fed's Chairman Jerome Powell, the Fed is unlikely to cut interest rates in March. Hence, the market's expectations for an interest rate cut in Q1, 2024 were not fulfilled once again. At present, the market expects that the interest rate cut would be postponed to May or June. After a round of oscillations of bond yields, the US 10-year treasury yield has risen again to 4.15%, close to the high level in the year. The overly optimistic market sentiment about the interest rate cut recovered to some extent. Furthermore, it is expected that the interest rate dot plots released at the FOMC meeting in March will bring a clearer direction to the market. From the aspect of supply and demand, although the US Treasury Department signaled in its latest quarterly refinancing statement that it would increase the scale of bond issuance again from February to April, it is expected that the scale of bond issuance would not need to be increased once again for at least the next few quarters. With respect to the repurchase plan of the US treasuries, the US Treasury Department also announced that it would start to engage in small-scale repurchase operations in April, and planned to announce details of a formal plan on regular repurchase in May. The operations by the US Treasury Department are expected to bring certain support to the US treasuries from both the supply and demand sides. In the mid-to long-term, even though the exact timing of interest rate cuts remains to be determined, as inflation continues to fall and moves closer to the target level, set by the central bank, interest rate cuts will eventually take place. In the general direction, there is still a high change for the US bond yields to move downward, and a rebound in bond yields will provide opportunities for arranging asset allocation into US bonds. Furthermore, it is recommended to properly increase the duration of the bond portfolio so as to capture the potential opportunities arisen during the start of the cycle of interest rate cuts.

European bonds: According to the statement made at the ECB's policy meeting in January, it is too early to discuss interest rate cuts at the moment. Since the inflation rate in the Eurozone rebounded in December 2023, the inflation rate in January only dropped slightly by 0.1% from a month earlier, and the rate of cooling inflation was slower than that in December 2023. As generally expected by the market, the ECB is unlikely to lower interest rates in March, thus causing the German 2-year and 10-year treasury yields to rebound from the lows of about 2.39% and 2.02% at the beginning of the year to about 2.64% and 2.33%, an increase of 25 bps and 31 bps, respectively. Despite this, falling inflation is still the general direction, and the GDP growth in Germany, the largest economy in the Eurozone, shrank by 0.3% quarter-over-quarter in Q4, 2023, indicating that the Eurozone economy is facing hidden concerns. Such trend prompted the market to believe that the ECB would still cut interest rates during the year, bolstering the performance of European bonds. Whenever bond yields experience a rebound, it would provide an opportunity for investors to enter into the market. At present, the minimum yields on the Bloomberg Barclays Pan-European Aggregate Sovereign Bond Total Return Index and the European Investment-grade Bond Total Return Index amount to 3.27% and 3.06%, respectively. Both yields are higher than their respective average minimum yields of 1.1% over the past decade, which are attractive to some extent. Nevertheless, against the backdrop of consistent uncertainties in the European economy, holding sovereign bonds may be more advantageous in the near term as they provide a hedge against recession risks and offer rather attractive minimum yields.

Emerging markets: There is little risk of rising yields in China's bond market, and investors may increase the duration of Chinese USD bonds, whereas long-term opportunities continue to exist in emerging markets despite the pressure in the short term

China's bond market: The pattern of weak recovery is still evident in China's economic fundamentals. The manufacturing PMI in January reached 49.2%. Although it rebounded by 0.2% from December 2023, it was still below the boom-bust line. In addition, due to the high base effect, the CPI in January fell by 0.8% year-over-year, and the PPI fell by 2.5% year-over-year. The constant trend of negative inflation rate has raised the real interest rate of the entire society, which is not favorable for the recovery of the real economy. Against such backdrop, on the one hand, loose fiscal credit policies are required to consistently stimulate and drive demands. The financial data in January reflected the increase in credit. Moreover, the increase in the aggregate financing to the real economy (AFRE) in January amounted to RMB 6.5 trillion, an increase of RMB 506.1 billion year-over-year. The monthly increase hit a record high. RMB loans went up by RMB 4.92 trillion in January, an increase of RMB 16.2 billion year-over-year, and also set a historical record high for a single month. In particular, the data in January changed the situation in the previous two months where government financing was stronger than corporate and residential financing. In January, residential financing improved to a significant extent, and corporate financing was not weak either. On the other hand, loose monetary policies are also required to consistently lower nominal interest rates. Although the reserve requirement ratio was cut on February 5, the current mortgage interest rates are still relatively high. According to the "2023 Q4 China Monetary Policy Execution Report" released in early February, the PBOC has made it clear that during the next stage of monetary policy execution, it would maintain reasonable growth in the total volume of financing and money supply, and the market's expectations for further monetary easing are not low.



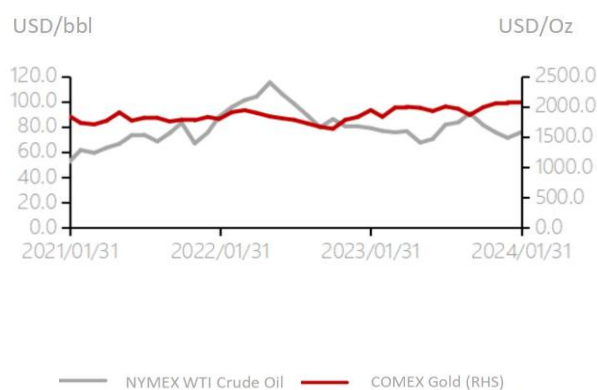
Furthermore, Q1 is typically the peak season for institutional asset allocation. The 10-year government bond yield has dropped to a historical low of around 2.4%, and periodic pressure of profit-taking also needs to be taken into account. Nevertheless, the bond market is still expected to maintain its strength in March with greater support compared with bearish signs, and there is little risk of rising yields in the near term.

Chinese USD bond market: The Fed's latest employment report for January far exceeded the economists' expectations. The US economy added 353,000 jobs in January, and the unemployment rate reached 3.7%. In addition, the US CPI went up by 3.1% year-over-year in January, and was expected to increase by 2.9%. The CPI in January increased by 0.3% month-over-month, and was expected to increase by 0.2%, setting the largest increase over the past four months. Given that the labor market remained strong, and that the inflation did not show a real and convincing decline, investors are not recommended to bet on an utterly aggressive pace of interest rate cuts from the Fed in 2024. According to Bloomberg, the chance of an interest rate cut in March is only 2%, and the market has maintained expectations for about 4 or 5 interest rate cuts throughout the year. Nevertheless, it is estimated that the final number of rate cuts could be fewer, with about 2 or 3 interest rate reductions. The US 10-year treasury yield has been hovering between 3.8% and 4.2% in January. For Chinese USD bonds, it is recommended to purchase long-term, high-rated bonds when the bond yields are rather high, and adopt a wait-and-see approach. Subsequently, investors may start to take profits when the central bank starts to cut interest rates in 2H, 2024.

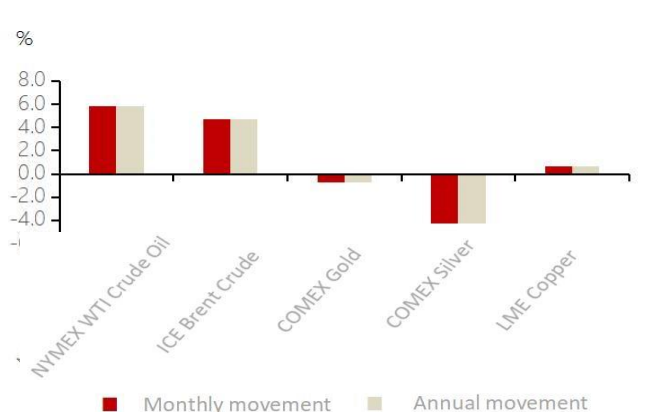
Global emerging bond markets: The USD has risen by about 2.8% year-to-date as the market expects the Fed to cut interest rates in later stages. Such trend has imposed short-term pressure on the emerging bond markets, which have recorded net outflows of approximately USD 2.4 billion year to date. In addition, the Bloomberg Barclays Emerging Markets Investment grade Bond Total Return Index declined by 1.28%. Nevertheless, the Fed is expected to start the cycle of interest rate cuts within the year. This will help increase the room for interest rate reductions in emerging markets, and enhance the attractiveness of returns in emerging bond markets. At present, the minimum yield of the Bloomberg Barclays Emerging Markets Investment-grade Bond Total Return Index is about 5.48%, which is approximately plus 2 standard deviations from the 10-year average, and the valuation seems rather attractive. A correction in emerging bond markets is likely to provide investment opportunities.

Commodities

Fig. 7 and Fig. 8: Commodity Prices (as of January 31, 2024)



Source: Wind, BOC Investment Strategy Research Center



Source: Wind, BOC Investment Strategy Research Center

Gold: The gold market is likely to experience oscillations, and it is recommended to purchase gold after corrections

The Fed once again decided to suspend interest rate hikes at the FOMC meeting in January, and many FOMC members did not believe that interest rates would start be cut in March. Due to the Fed's policy stance, gold prices experienced a fall. Subsequently, the US released a series of strong economic data as well as the data on non-farm payrolls that exceeded the market's expectations. The strong performance of the US economy and employment has strengthened the market's expectations that the Fed would not lower interest rates for the time being, and gold prices immediately entered into a period of adjustments.

Looking forward to March 2024, the Fed has a high chance to keep interest rates unchanged on March 20. The price of gold is



likely to become increasingly volatile in the near term due to changes in the interest rate environment driven by the expectations of an interest rate cut by the Fed. Moreover, we remain bullish on gold in the mid-to long-term, and it is recommended to purchase gold after corrections. In the mid-to long-term, the timing of the Fed's start of interest rate cuts in 2024 has been postponed from Q1 to Q2. Nevertheless, from the aspect of the whole year of 2024, it becomes increasingly clear that the Fed will start the cycle of interest rate reductions. The constant declines in nominal interest rates and real interest rates are expected to support the rally of gold prices. As elections will be held around the globe in 2024 and 2025, governments of varying countries are expected to increase public spending to stimulate the economy, and central banks may adopt interest rate cuts in 2H, 2024. In addition, due to the recession in the commercial real estate sector, there have been declines in the financial results and share price of the New York Community Bancorp, thus revealing the rising credit risks of commercial real estate sector in a high interest rate environment. Repricing has led to the heightened pressure of debt repayment, and defaults of commercial real estate loans have led to risks for small and medium-sized banks. Furthermore, financial risks have been transmitted to credit risks. The aforementioned situation is likely to push the Fed to start the cycle of interest rate reductions, thus driving up gold prices. In addition, the gold purchase demands of central banks around the globe are expected to provide support for gold prices. According to the IMF and relevant public data, official gold reserves around the globe went up by 28 tonnes in December 2023, and the total volume of gold purchases (41 tonnes) in the same month exceeded the total volume of gold sold (12 tonnes).

Crude oil: The center of oscillations is expected to move up

In February, the US oil prices continued to fluctuate around the level of USD 70. The trend was rather strengthening with upward movement of the center of oscillations. This was mainly attributable to geopolitical conflict. The market was concerned that the conflict in the Middle East might escalate. In the near term, although geopolitical factors have imposed an impact on the crude oil market, supply and demand are still the core disturbing factors for oil prices.

Looking forward to March, crude oil prices are expected to remain volatile, but the center of oscillations is likely to move upward. At present, there are two major risks in overseas energy markets that are worthy of attention. First, the concern about the escalation of the geopolitical conflict in the Middle East. Second, the concern about certain small systemic risk incidents in the US. Huge uncertainties exist in the risk events in the above two directions. For oil prices to break through the current level and continue to move upward, all-round improvements are needed, and the issues could not be addressed by marginal progress or improvements merely at the level of expectations. On the supply side of crude oil, judging from the implementation of previous plans of production cuts, although the implementation rate of OPEC+ production reductions continued to decrease, the policy of production cuts will not be adjusted in the near term, thus providing support for crude oil prices. In addition, the growth rate of US shale oil may slow down in 2024. On the demand side, the incremental demand for crude oil in 2024 will mainly originate from developing countries. According to the data of the EIA, China's oil demands will reach 15.94 million tons per day in 2023, and China's gasoline demands may reach the peak in 2024. India is the world's third largest energy consumer, and its demands for imported crude oil will continue to increase.

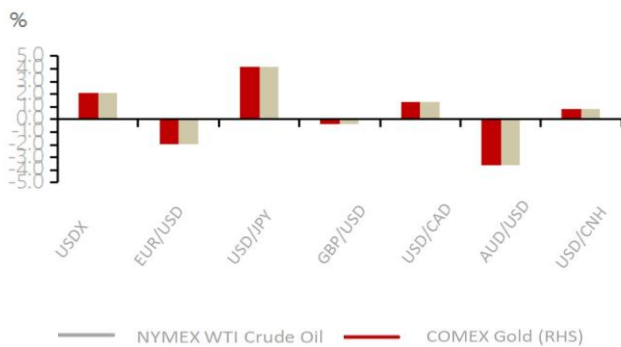
Overall, member countries of the OPEC+ bloc are still insisting on lowering production, and the rising geopolitical risks in the Middle East have also made it harder for oil prices to fall to a significant extent. It is expected that oil prices at the current position will most likely continue to fluctuate within a range. Driven by a series of sudden bullish factors in the near term, the center of oscillations is likely to move up.

In a nutshell, on the supply side, voluntary production cuts are likely to be implemented by the OPEC+ bloc, thus bolstering the oil prices. Nevertheless, the Fed does not plan to start an interest rate cut immediately, and the rate cut may not be as deep as originally expected by the market. The global economy is facing downward pressure, the overall macroeconomic environment tends to be rather gloomy, imposing pressure on the crude oil prices. Given that the prevalent contributing factor of the crude oil prices has once again returned to the mutual game between fundamentals and bearish macroeconomic signals, the oil market is likely to consistently fluctuate sideways amid a weak pattern.

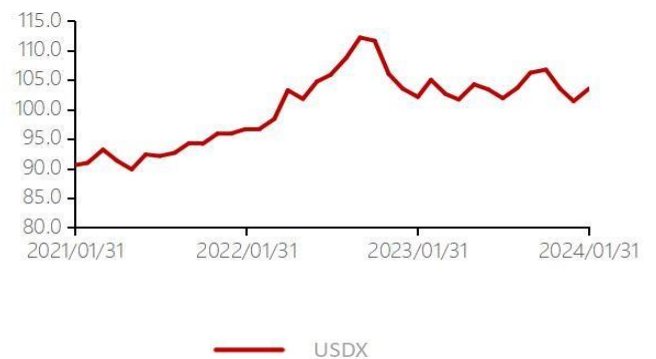


Foreign Exchange

Fig. 9 and Fig. 10: Foreign Exchange Prices (as of January 31, 2024)



Source: Wind, BOC Investment Strategy Research Center



Source: Wind, BOC Investment Strategy Research Center

U.S. dollar: USD is likely to strengthen amid oscillations in the near term due to the dual resilience of inflation and employment data

The market focus tends to be placed on the FOMC meeting in mid to late March. Given that the inflation and employment data released so far in 2024 have shown resilience, coupled with the statements made by the Fed's Chairman at the FOMC meeting in early February, the market does not have too much expectations for an interest rate cut in March. Bolstered by the likelihood of maintaining higher interest rates for a longer period of time, the USD index exceeded the level of 104.9 in mid-February. The market has reached the consensus to keep interest rates unchanged at the FOMC meeting in March, but it is more important to observe the changes in the dot plots of interest rates. According to the dot plots updated in December 2023, there is a chance for the Fed to cut interest rates by 75 bps in 2024. Driven by the official statements that cooled down expectations of interest rate cuts over the recent month, and the resilience of the job market, the revised dot plots are unlikely to show interest rate cuts with an accumulative amplitude of greater than 75 bps. On the contrary, two scenarios are more likely to take place. First, the Fed may maintain a 75-bp rate cut. Second, the Fed may adopt interest rate cuts of less than 75 bps. In case that the second scenario becomes a reality, the expectations for higher interest rates in a longer period of time may push up the USD index, which has already priced in the expectations of three interest rate cuts. Moreover, there is a chance for the USD index to return to the mid November high of about 106, or even reach a higher level. Although the second scenario is possible, the first scenario is actually more likely. The interest rate dot plots also point to the possibility of a 75-bp rate cut. The market focus will be placed on the Fed's expectations of inflation and economic data. Given that the Fed is highly vigilant against a rebound in inflation, it is expected that its policy stance will not be too dovish unless the inflation rate and employment data released in March clearly point to the target level, which could prompt the market to expect earlier interest rate cuts. Otherwise, the USD index is likely to hover at a rather high level in March.

Euro: EUR is unlikely to be bolstered for the time being due to weakening fundamentals and delayed interest rate cuts

Despite lower expectations for interest rate cuts, the EUR was not bolstered in February. Instead, the currency hit a low of around 1.07 once reached in mid-November 2023. Given that the European economy is not as resilient as the US economy, even if the president of the ECB signaled that the interest rates would not be cut in a hurry, the market still expects the ECB to reduce interest rates earlier than the Fed. The expected sequence of interest rate cuts in Europe and the US has been reflected in the weakening EUR. With respect to the economy, although certain economic data in the Eurozone have improved, the PMI still fell within the contraction territory. In addition, the European Commission lowered its economic growth forecast for the years 2024 and 2025 to 0.8% and 1.5% in mid-February. As can be seen, even if there is no pressure to lower interest rates, there is actually a need to do so. Moreover, even if the EUR may experience a rebound, its rally will be limited. The market is paying closer attention to the ECB's forecast of future economic growth at the policy meeting in March. Since the ECB's policy meeting will be held earlier than the FOMC meeting, if the expected economic prospects do not disappoint the market, the EUR is still likely to rebound from a low level within a narrow range.



British pound: GBP may hardly achieve ideal performance amid the BoE's slower pivot towards a more dovish stance

On a technical front, the risk for GBP-USD looks tilted to the downside, especially after the pair broke downside of 1.26 – 1.28 range and managed to hold for nearly two months. Although less acute, GBP softness is also likely against the USD in the months ahead. The main driver of said weakness is, the slow but clear pivot by the Bank of England towards a more dovish stance. February's Monetary Policy Committee (MPC) meeting delivered the first steps in this direction. Importantly, there was the removal of hiking bias together with notably lower inflation forecast for 2024. On the cautious side, two members continue to vote for a hike and Governor Bailey advises treating inflation with caution. As such the path to a full pivot lengthens. Looking ahead, if the expected softer sequential inflation and wage prints materialize alongside stagnating growth, it will make it very difficult for the Bank of England to be a hawkish outlier within the G10.

Japanese yen: JPY's weakness in the near term will not alter the perception about its strengthening in the medium term

Amid the general trend of a stronger USD, the exchange rate of the USD/JPY has strengthened to some extent, rebounding to above the level of 150. The estimate of the timing and frequency of the Fed's rate cuts in 2024 will determine the trend of short-term US treasury yields, while imposing an impact on the USD/JPY through the overall changes in the USD index. At present (as of the close of February 16), the federal funds rate futures contracts imply that there is merely a chance 38.4% for the Fed to start cutting interest rates in May, and the chance of four or more interest rate cuts in 2024 drops to only 64%. In Japan, there is limited new information that could affect market trends, and the Japanese economy fell into a technical recession in Q4, 2023. From our perspective, the Fed is already at or very close to the peak of interest rate hikes, and the BoJ is no longer likely to further ease its monetary policy. As such, the next step in adjusting monetary policies for both the Fed and the BoJ will be conducive to narrowing the interest rate gap between the USD and the JPY. Therefore, we maintain our bearish view on the trend of the USD/JPY.

Commodity currencies:

Canadian dollar: CAD has certain potential for upward movements during oscillations amid consolidation

According to the minutes of the latest policy meeting held by the Bank of Canada, due to the persistence of underlying inflation, the central bank still needs to be cautious about prematurely lowering the interest rates. On the one hand, although wage growth has slowed down to a slight extent, the issue of overheating and inflation still exist. On the other hand, according to the latest report released by the Statistics Canada, the unemployment rate fell for the first time in nearly six months as driven by the increase in part-time work. The employment data that exceeded the market's expectations reflected the strength of economic fundamentals and the lower urgency to cut interest rates, thus bolstering the CAD. With respect to crude oil prices, on the supply side, major oil-producing countries have generally reduced their oil production. On the demand side, during the recovery of the global economy, crude oil supply tends to tighten as demands continue to grow. The gap between supply and demand still exists, and the center of oscillations for oil prices is expected to remain high. Overall, based on the performance of economic fundamentals, expectations of monetary policies, and forecasts on crude oil prices, there are gradually increasing favorable factors for the CAD. Moving forward, it is expected that the CAD has certain potential for upward movements during oscillations amid consolidation.



Australian dollar: AUD may become increasingly volatile due to the loosening of hawkish policy stance

According to the latest statement made by the RBA at its policy meeting, it would keep the cash rate unchanged at 4.35%, which was in line with the general market expectations. With respect to the employment data, the number of people employed rose slightly in early 2024, and the unemployment rate climbed to a two-year high, thus revealing the trend of cooling in the labor market. As such, the RBA has also softened its previously hawkish stance. With respect to the inflation, due to the strengthening of the USD and the slowdown in the economy overall, the quarterly CPI data in Australia released in January showed that annual commodity inflation had declined for five consecutive quarters. Under the dual impact of employment and inflation data, the market's expectations for the RBA's first interest rate cut have been advanced from November 2024 to September 2024, thus prompting the AUD to become increasingly volatile in the short term. From a technical aspect, the main moving average of the AUD experienced declines, indicating that the currency has ushered in a weak pattern. Overall, the AUD is in a weak position in the near term, and closer attention shall be paid to whether it could stabilize above the level of 0.660. Moving forward, the AUD is expected to show its orientation of movements amid oscillations, and may become increasingly volatile in the short term.

Renminbi: RMB is expected to operate within a reasonable range

As of February 9, the CFETS USD/RMB exchange rate closed at the level around 7.19, slightly lower than in January. As mentioned in our previously monthly commentary, the RMB exchange rate should depend on two factors in the short term. First, China's economic data. And second, the pace of overseas interest rate cuts. The results of China's latest economic data released for February were rather mixed. The data on the aggregate financing to the real economy (AFRE) exceeded the market's expectations overall, and the growth of M1 picked up rapidly. Nevertheless, the growth rates of CPI and PPI were still negative. On overseas aspect, the latest data on the US CPI picked up once again year-over-year. The market's expectations for the timing of the Fed's first interest rate cut have been postponed again. Non-USD currencies are still under pressure in the short term. From the policy aspect, the monetary execution report for Q4, 2023 released by the PBOC highlighted the necessity of stabilizing expectations on exchange rates, guarding against the risk of exchange rate overshooting, warding off the formation of self-reinforcing unidirectional expectations and keeping the RMB exchange rate overall stable at a reasonably balanced level. Overall, against the backdrop of coexistence of both bullish and bearish factors in the short term, the RMB is expected to operate within a reasonable range.



Asset Allocation

Fig. 11: Asset allocation recommendations in 2024

Stocks	Underweight			Overweight	
	Bearish	Conservative	Neutral	Recommended	Bullish
U.S. (S&P 500)		●	●		
Europe (DAX, CAC)		●			
U.K. (FTSE 100)		●			
Japan (Nikkei 225)				●	
China A-shares (CSI 300)				●	
Hong Kong, China (Hang Seng Index)				●	
Bonds	Underweight			Overweight	
	Bearish	Conservative	Neutral	Recommended	Bullish
U.S. Treasuries				●	
Chinese Dollar Debt				●	
China: Money Market			●		
China: Rate Securities			●		
China: Credit Debt			●		
China: Convertible Bonds			●		
Precious metals	Underweight			Overweight	
	Bearish	Conservative	Neutral	Recommended	Bullish
Gold				●	
Silver				●	
Crude Oil		●	●		
Copper		●	●		
Aluminum			●		
Foreign currencies	Underweight			Overweight	
	Bearish	Conservative	Neutral	Recommended	Bullish
USD		●	●		
EUR		●			
GBP		●	●		
CAD			●		
AUD				●	
JPY				●	
CNY			●		

Source: BOC Investment Strategy Research Center

Note: The black dot represents the annual view, and the grey dot represents the direction of adjusted configuration at proper time with preset conditions.



Against the backdrop of the macro-theme that “global assets are ushering in the dawn as the USD starts the cycle of interest rate reductions”, we have analyzed the trend of major categories of varying global assets from the aspects of geopolitical structure, macroeconomic policies, economic growth, valuation and liquidity, etc. For the next year. From our perspective, against the backdrop of the fundamentals of “slow global economic recovery and the Fed’s start of the cycle of interest rate cuts” in 2024, we believe the allocation among major asset categories should be in the following order: stocks, gold, commodities and bonds.

With respect to stocks, China’s economy is making progress to promote stability and experiencing a moderate recovery. China continues to facilitate the high-quality development and form new productive forces. Overall, the RMB is strengthening amid neutrality. Given that Chinese assets have the highest cost performance in the world, the Chinese stock market shall be given priority in the allocation of global assets, and overweight shall be given to China’s A-shares (recommended) and Hong Kong, China stocks (recommended). Given that the Fed suspended interest rate hikes for three consecutive times, the market has priced in the timing of the start of the interest rate cuts in advance. Moreover, the US stock market has fully priced in a “soft landing” for the economy. It is recommended to start with a neutral view on US stocks. After the start of the first interest rate cut, investors shall reduce stock holdings on highs and turn to underweight, and then increase holdings during sufficient declines of stock prices and return to a standard allocation. The European economy remains sluggish and the rebound can hardly be sustained. Hence, it is recommended to give an underweight to European stocks. The Japanese economy may emerge from deflation and maintain its trend of recovery, and the stock market is expected to experience a moderate recovery. Hence, an overweight shall be given to Japanese stocks (recommended). Emerging markets have benefited from the easing of global liquidity pressure, and it is recommended to invest moderately in countries that benefit from the restructuring of global industrial and supply chains.

In the bond market, driven by the consistent declines of the US inflation and the Fed’s start of the cycle of interest rate reductions, there is still the chance of a shallow economic recession. At present, it is the best investment stage, and it is recommended to maintain the overweight in US stocks in Q4, 2023 (recommended). As the US bond yields experience a downward trend, Chinese USD bonds are entering into a golden period for asset allocation, and it is recommended to maintain the overweight in Chinese USD stocks in Q4, 2023 (recommended). China’s economy is experiencing a moderate recovery, but its foundation is not solid. The liquidity level is rather loose, and there is still room for the RRR cuts and interest rate cuts. The center of interest rates is expected to constantly move downward. The 10-year government bond yield is likely to fluctuate in the range between 2.45% and 2.75%, and it is recommended to adopt a neutral view.

With respect to the precious metals and commodities, the functions of geopolitical hedging and the long-term logic of currency hedging (role of credit scale) amid the century-old changes continue to evolve, and the value of long-term asset allocation into gold exceeds the previous situation. Coupled with the pattern of rising gold prices during the period from the end of the USD interest rate hikes to the start of the cycle of interest rate reductions (expected declines in the USD real interest rates), it is recommended to maintain the overweight on gold in Q4, 2023 (recommended). The tight balance between crude oil supply and demand is likely to continue, and it is recommended to be conservative first before. It is recommended to be conservative for copper first and then adopt a neutral view. Driven by the alleviation of the oversupply of aluminum, demands are likely to improve, and it is recommended to adopt a neutral view.

With respect to currencies, the cycle of the USD rate hikes is over, and the economy is gradually entering into a recession. It is recommended to maintain an underweight (conservative) during the period when market transactions are expected to ease, and then increase allocation to a standard position when the opportunity arises. The consistent headwinds in the economic environment in the UK can hardly support the GBP. It is recommended to adopt a neutral view on the GBP and adjust to an underweight (conservative) at an opportune moment. In Japan, the trade deficit has narrowed, and the spreads between US and Japanese government bonds have narrowed, whereas the safe-haven attribute of the JPY is expected to resume. It is recommended to raise the standard position of the JPY in 2023 to an overweight (recommended). The economic fundamentals of the Eurozone are not as good as those of the US. In addition, the interest rate cut may be earlier than that of the US with similar magnitude. The comparative advantages of the monetary policies have weakened to some extent, and it is recommended to lower the allocation from the standard position in 2023 to an underweight (conservative). The fundamentals of the Australian economy are favorable, and the comparative advantages of monetary policies still exist. The exchange rate of the AUD/USD will be at a historical low in 2023 and has a need for rebound. It is recommended to increase the standard position of the AUD in 2023 to an overweight (recommended). We maintain our neutral view for the CAD. Given that China’s economy is expected to recover, but exports are weakening due to the sluggish external demands, the RMB is likely to be rather strengthened amid neutrality, and it is recommended to adopt a neutral view.

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