Global Market Wrap-up

Ahead of central bank week

Multi-assets

Global

- US stocks slump as weak earnings reports and escalating Middle East tensions trigger market risk-off sentiment. Fed is likely to pause given the tightening financial condition.
- Ultra-weak yen puts pressure on BOJ's monetary policy, prompting bond purchasing operation to control JGB yield. We are of the view that BoJ will lift the YCC band by 50bps to be “pre-emptive”.
- CSI300 fall to lowest level since 2019, while government continue to introduce counter-cyclical measures to stabilize confidence and counter decline.

CUIRS Insight

US stocks slump as weak earnings reports, while better-than-expected economic data and escalating Middle East tensions impact market sentiment. US stocks slump as companies reported weaker-than-expected earnings, causing a sell-off in the market. US retail and industrial output data for September surpassed expectations, driven by increased summer spending. The 10-year US Treasury yield hit 5.0% in earlier this week but soon slid from the peak. In our view, we see 5% as the line in sand given strong demand when reaching the level, which can be proved by recent bill auction. However, Mid-east tension and US fiscal policy concern have also contributed to mixed environment on yields.

Weak yen piles pressure on BOJ’s monetary policy and BOJ announced bond purchasing operation to control JGB yield. Ultra-weak yen puts pressure on BOJ to adjust its monetary policy, as USDJPY broke the 150 level, which add more concern on MoF intervention. BOJ also announced bond purchasing operation to control JGB yield. The significant upward pressure on JGB yields and the imported inflation concern by yen could prompt BoJ to be cautious and adjust YCC band by 50bps next week to weigh benefits against the risk.

UK faces stagnation risks and ECB hold policy rate unchanged. The UK faces stagnation risks highlighted by declining retail sales, factory orders, and the Services PMI, indicating weak demand and a cooling job market. As expected, ECB hold its policy rate unchanged amid a slowdown in price gauges and the risk of a recession due to costlier loans. In our view, the further hike by ECB require upside surprise on inflation, which is likely to result from energy price spike, similar to what we saw in early 2022.

APAC economies still subject to China recovery concern, while some central banks gear to off-cycle hike. Chinese government has implemented counter-cyclical measures, but challenges remain especially in real estate sectors. Factors such as FX depreciation, supply shocks, and fiscal policy developments are influencing the monetary authority decision-making process, hence more hawkish tone among the APAC central banks are expected.

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CONTENT

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US: Stocks slump amid better-than-expected economic data

US equity took a downturn

US Stocks tumbled, with Nasdaq index futures losing about 1%, as corporate earning calls overall show weaker-than-expected earnings, which disappoints the market.

Meta Platforms Inc. sank as much as 4% in US pre-market trading after saying it's at the whim of an uncertain economic environment. Alphabet Inc. lost 1.8%, extending a selloff on Wednesday on disappointing cloud figures. Amazon, which reports results after the bell, slid 1.2%. Earnings missteps at the biggest US tech companies — which have already seen $200 billion wiped off their market value — are causing ructions in equity markets as investors rethink sky-high valuations against a backdrop of rising Treasury yields. While the Nasdaq 100 has been seemingly immune to pessimism, with the index still up 31% this year, there's now growing concern about its vulnerability in a wider stock market selloff.

US economic data outperform the market consensus

The United States released better-than-expected retail and industrial output data for September, driven by a surge in summer spending on travel and entertainment, leading to unsustainable real GDP growth in the third quarter. Both service and manufacturing PMI exceeded expectations, indicating positive economic conditions. Mortgage rates remain low with a 5% variable rate and a typical 30-year term.

However, the tightening cycle of the Federal Reserve is expected to hit real economy, resulting in higher mortgage rates, increased credit-card debts, and business-loan defaults, which could affect growth in the current quarter. It is important to note that a significant portion of the economic strength was influenced by temporary factors such as blockbuster summer releases and concert tours, as well as retail inventory buildup, which may not necessarily reflect underlying economic strength. We expect US growth momentum will slow down in Q4 given still-elevated inflation, high interest rates and the resumption of student loan repayment.

UST yield: Tug of war

On October 19th, Powell gave a speech at the New York Economic Club, implying that there would be no interest rate hike in November, but that interest rates could remain for a longer period of time. The 10-year US Treasury yield hit a new high of 5.0% in the session, reaching a new high since 2007. Yields later slid from the peak, accelerating after billionaire investor Bill Ackman said he was ditching his bearish bet on long-term Treasuries. Stronger than expected US retail sales, labour market and inflation data in recent weeks have helped push yields higher, despite the over 500bps hike delivered by the Fed over the past 18 months.

At the same time, the situation in the Middle East continued to escalate. From the evening of the 25th to the early morning of the 26th, the Israeli Defense Forces launched a large-scale ground attack on the Gaza Strip. The increasing risk aversion sentiment then pressure the yields lower.

Growing concerns over the US government's near $2tn annual budget deficit, exacerbated by Fitch Ratings' decision in August to lower the US credit rating, have also added to upward pressure on yields. There are also some bearish statements on US yield: "There is too much risk in the world to remain short bonds at current long-term rates," Ackman posted on X, formerly known as Twitter, saying that growth in the US was weaker than the mainstream data suggests.

Fig. 1: Consumer contribute more than half of Q3 GDP growth

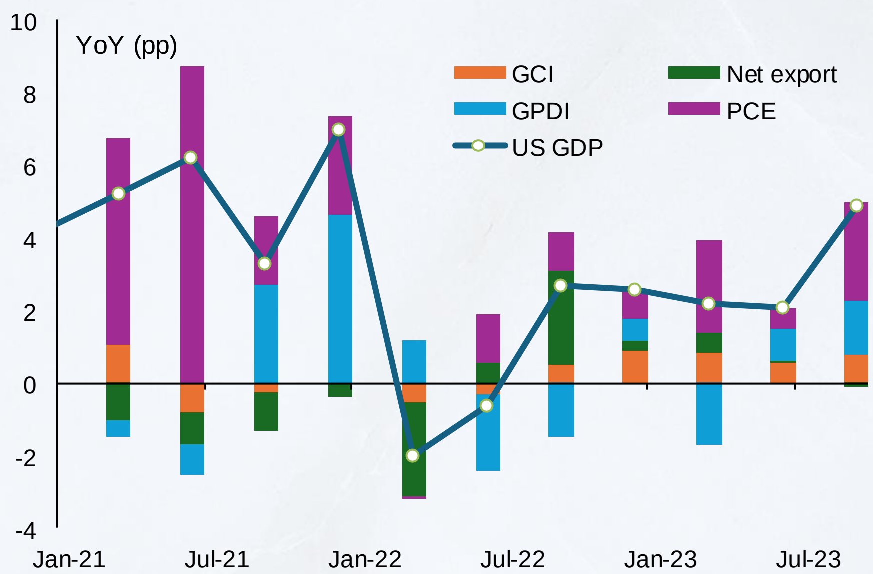
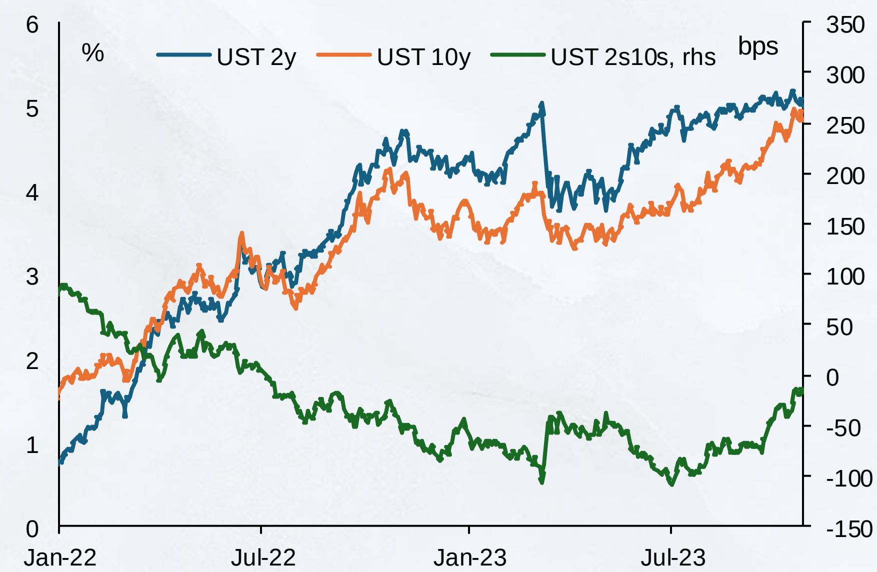


Fig. 2: UST 2s10s steepener trade is still working



Japan: Chance for BoJ to lift YCC band by 50bps

Weak yen piles pressure on BOJ's monetary policy

USDJPY has been pushed up to 150 level, raising the risk of government intervention in the currency market and piling pressure on the Bank of Japan to adjust monetary policy. The weakness has also been noted by BOJ officials, who must decide whether to tweak the policy that has weighed on the yen for years on next week.

"The yen's persistent weakness also adds pressure on the BOJ's policy settings, whether or not to raise the ceiling for yield-curve control, remove YCC or end the negative policy rate," said Koji Fukaya, a fellow at Market Risk Advisory in Tokyo. He added that the yen is probably hemmed in for now with intervention risk limiting further losses and the yield gap preventing a recovery. Officials neither confirmed nor denied whether they propped up the yen at that time. Japan's top currency official Masato Kanda has said Japan will take appropriate steps if excessive moves are seen in FX markets.

In our view, the USDJPY quick drop (from 150.7 to 147.6) on Oct 3rd NY trading time is not likely the direct intervention conducted by Japanese authorities. In contrast, the drop suggests that the market is getting sensitive at the level and nervous about the potential intervention. Moreover, the direct intervention will only smooth the trajectory of Yen depreciation. A material rebound of JPY should require lower US yields, which we anticipate to see in Q4 when the US economy slows down with the aforementioned factors.

Significant upward presure on JGB yield, Central bank to seek balance

On Oct 24, BOJ announced an unscheduled bond purchasing operation, as it sought to smooth the JGB yields upward pressure that had brought them to fresh decade highs. Following the BOJ's announcement, the 10-year JGB yield declined 0.5 basis points to 0.855%.

Possible reasons for the upward pressure on JGB yields should include 1) The structural upward revision of US yields, resulting in widening rates differential; 2) Improvements in Japan's inflation fundamentals contributing to the upward pressure; 3) The ultra-weak JPY and rising import inflation risk; 4) Active fiscal spending, as indicated by a new stimulus package, increases bond supplies; 5) Japanese lifers have not yet shifted focus back from USD bond, despite reports of potential changes in asset allocation. Data suggests they are waiting for higher JGB yields to enter the market.

The central bank probably wants to give itself enough flexibility to keep YCC to withstand until NIRP exits. If the current 1% band is hit either by strong hiking expectations or beta to overseas rates, BoJ would need to buy up huge quantities of JGB, adding downward pressure on JPY, in turn adding more imported inflation risk. We hence see a strong rationale for BoJ to act preemptively by raising the ceiling further to 1.5% on Oct 31st.

But BoJ still wants to avoid a sharp rise in long-term interest rates. The policy maker may worry that a 100bps hike of the upper band will send hawkish signals to the market, which may further be seen as a stronger indication that BoJ may conduct policy normalization sooner than originally expected, in turn selling more JGBs. But a reactive approach will only make matters worse, therefore there's 50/50 chance for BoJ to conduct the further band lift as it must weigh on benefits against the risk.

Fig. 3: Carry disadvantage continue to pressure JPY

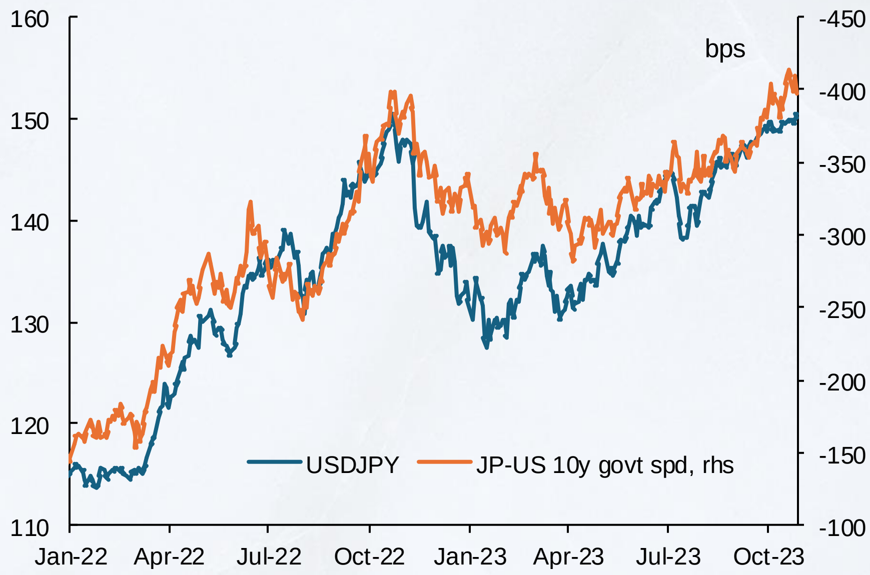
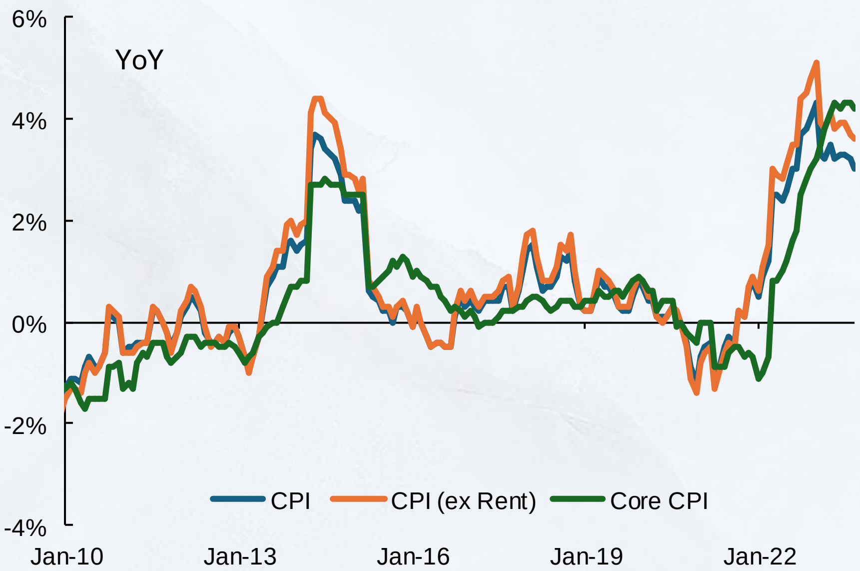


Fig. 4: BoJ need to seek balance between tightening and keep sustainable inflation



UK: Stagnation risks remain

Data published on Tuesday by the Office for National Statistics showed that the unemployment rate rose to 4.2% in the three months to August, up from 4% in the previous quarter, while the employment rate fell 0.3% to 75.7% in the same period. However, the agency warned that these estimates should be treated as "experimental" since they were derived from tax records and benefits claims, rather than the usual labor force survey.

The ONS was unable to publish the usual set of figures due to worsening problems with its survey. The response rate to the survey has fallen since the pandemic, reaching levels where its results are no longer reliable. This has led to a divergence in recent months from other data sources. The lack of reliable figures means policymakers will lack key information on the true state of the jobs market at a critical turning point for the economy.

The Bank of England believes that wage pressures created by a shrinking workforce are one of the main reasons high inflation has persisted in the UK. Chancellor Jeremy Hunt has made tackling inactivity a priority. However, the ONS currently cannot provide figures on the reasons for stubbornly high rates of economic inactivity. The recent data release also lacked details on people's working hours, the extent of self-employment or part-time work, and any sectoral breakdown.

In addition to the ONS data, other indicators point to challenges in the UK economy. The Confederation of British Industry's monthly retail sales balance plummeted to -36.0 in October 2023, indicating that retailers reduced their orders to suppliers and anticipate doing the same in November. The total order book balance from the Confederation of British Industry's Industrial Trends Survey also declined sharply, signaling the most significant monthly drop in factory orders since January 2021. Furthermore, the UK Services PMI fell to its lowest level in nine months, reflecting weak client demand across the real estate sector and other factors.

Lastly, the number of employees on the books declined by 11,000 in September, further indicating a cooling jobs market. These various indicators demonstrate the challenges and uncertainties facing the UK economy, particularly in terms of employment and consumer spending.

Euro Area: We are at the plateau already

Following 10 back-to-back increases, European Central Bank leave the deposit rate at 4% on Thursday, in line with analysts' consensus surveyed by Bloomberg. The pause would follow a further slowdown in the two main gauges of euro-area prices and a worsening backdrop for the 20-nation economy, which faces the risk of a recession in the second half of 2023 as costlier loans squeeze households and firms.

ECB officials have signaled that borrowing costs will remain elevated for a prolonged period to pull inflation back toward the 2% goal. While several warn of further monetary tightening should Middle East tensions spill over into energy prices, some analysts warn rate cuts may be needed before next fall, as markets are pricing now.

The HCOB flash eurozone composite purchasing managers' index, a measure of activity at companies across the 20-country bloc, fell to a 35-month low of 46.5 after contraction of activity in both the services and manufacturing sectors. On the positive side, consumer-price gains slowed more than expected last month to 4.3% — less than half their double-digit peak about a year ago. Lagarde told top European Union officials this week that the fight against inflation is going well, according to people familiar with the matter.

Even so, alongside any potential spike in energy prices amid the fighting in the Middle East, a weaker euro also poses an upside risk to the outlook. The plateau is here, we argued. The further hike would require upside inflation surprise, which is likely to be triggered by an energy price spike due to more intense geopolitical tension. Furthermore, the sufficient LNG reserve could alleviate the bite on European economy, if any.

With the high external uncertainties and slowing economy, the risk titled to downside for EUR. We then continue to favor EUR as funder and recommend short EURMXN (Current: 19.13, Target: 18.19, Stop loss: 19.40) to position the EU weakness and US exceptionalism.

China: Bearish equities amid gradual fundamental recovery

Chinese A-shares decline amid challenges

Chinese shares have tumbled to their lowest level since before the Covid-19 pandemic, driven by a combination of factors including slowing economic growth, a liquidity crisis in the property sector, and geopolitical tensions.

The CSI 300 index, which tracks large and liquid Shanghai- and Shenzhen-listed stocks, fell as much as 1.3% on Monday, reaching its lowest level since 2019. Global fund flows have also been affected by deteriorating relations between the US and China, with asset managers facing pressure from Washington over investments in certain Chinese companies. Offshore investors using Hong Kong's Stock Connect program have sold a net RMB169bn (USD23bn) worth of shares since August, significantly reducing net inflows for the year.

Government employs measures to regain market confidence; More room for rates cut but view remains

To address the growth momentum, the Chinese government has taken measures such as issuing RMB1trn in supplementary bonds for disaster relief and infrastructure enhancement. The issuance of these bonds, planned to be completed in the fourth quarter, aims to support economic growth and counter expectations of decline. Given the timing of issuance, we expect it to take no effect to 2023 but further boost 2024 growth rate, which also signals for government's strong ambition to boost the economy.

Additionally, local news points out that the central government might further expand the budget deficit in 2024 and issue additional government bonds, with a view to alleviating pressure on local fiscal expenditures and reducing local debt risks. With these bear in mind, we are of the view that both fiscal and monetary policy will tend to be more expansionary role. Given the additional bond issuance, we expect PBoC to inject liquidity via OMO (reverse repo and MLF), historical record also shows that PBoC will relax monetary policy in the most of time. Hence, we anticipate PBoC to re-engage policy rates and RRR cut again. However, given that PBoC is now draw a line in FX market, we think its monetary operation have been and will continue to be cautious. The tug of war in FX & rates will remain here until external factor turns – specifically the US rates.

Economy indicators recovers, but real estate and exports remain sluggish

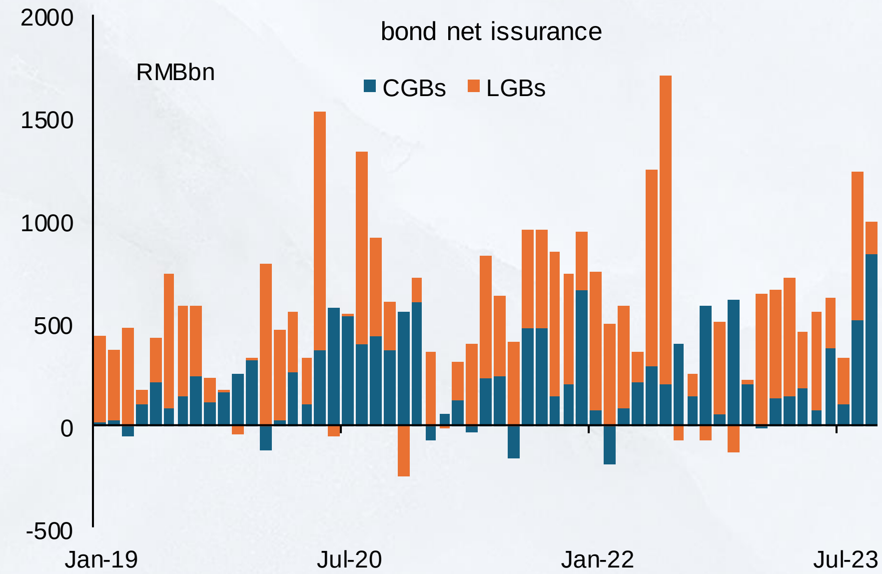
In terms of economic indicators, the third quarter saw a recovery in GDP beyond expectations, with a focus on infrastructure construction and disaster management. Year to date, China's GDP growth has reached 5.2% y/y, hence the 5% target for 2023 is close at hand. While household consumption, manufacturing, and infrastructure investment have shown acceleration, real estate and exports remain weak spots.

Confidence among businesses and individuals is still lacking, with concerns about the continuity of economic stabilization, the real estate market, and the geopolitical situation. In September, total retail sales of consumer goods increased by 5.5% year-on-year, manufacturing investment rose by 7.9%, and investment in infrastructure development increased by 6.8%.

However, the sales area and volume of commercial housing experienced declines, with real estate investment also showing negative growth. New starts, new construction, and completed areas in the real estate sector also saw decreases. These various economic indicators highlight the challenges facing the Chinese stock market and the broader economy, including the need to address slowing growth, manage liquidity issues in the property sector, and navigate geopolitical tensions.

Fig. 5: CSI 300 fell to its lowest level since 2019

Fig. 6: Government bond net issuance has surged since August



China: Property policy struggles persist

China grapples with property policy balance

“China is struggling to strike a balance on its property policy over the past two years — they have been caught between providing too much stimulus or not enough,” said Larry Hu, chief China economist at Macquarie. “They have been muddling through — but the measures they have taken so far have been not enough to ease the developer-related credit risk perceived by homebuyers.”

Property developers still face challenges

The turmoil among property developers is hugely significant for China because construction and real estate has been the motor of much of its growth. Property and related industries have often contributed roughly a quarter of gross domestic product.

Evergrande itself is still struggling to finalise its own long-planned restructuring, which was derailed last month when it failed to proceed with an offshore debt refinancing due to an unspecified regulatory investigation. Evergrande faces a liquidation hearing in a Hong Kong court on October 30.

Most of the top 10 developers in 2020 have also faced plummeting sales amid waning consumer confidence, compounding developers’ liquidity concerns. There are signs that homebuyers have preferred instead to buy from state-backed developers, seen as less likely to go bust.

The crisis for the real estate sector has yet to feed through into any sharp move for house prices. New home prices, the main gauge of the real estate market in China, have fallen in some major cities but remain buoyant in others.

Beijing's property policies face effectiveness concerns

Analysts argue that many of Beijing’s policy measures towards property have been well-intentioned but ineffective — trying to strike too delicate a balance between offering enough liquidity support and not spurring further speculation in the sector.“Many policies aim to stabilise the home market and provide just about the right amount of liquidity for developers to finish existing units and deleverage,” said Ng. “[But] when there are too many targets, it is a difficult task to ensure everything falls into place.”

Hong Kong: Follower, not a driver

Hong Kong reduces stamp tax to boost market sentiment

The Hong Kong stock market sentiment is depressed, Hong Kong stamp tax rate will be reduced from 0.13% to 0.1% to reduce the transaction cost of investors, in order to boost market sentiment and enhance the competitiveness of Hong Kong stock market by the end of November to complete the legislative process. Since the reduction is not large, symbolic significance is more than practical in our view. However, this highlights the Hong Kong government's willingness to boost market liquidity.

The short-term release of positive signals may improve market sentiment. But the strong rebound on HSI index will be only seen when 1) US rates go lower, alleviating its damage to Hong Kong economy; 2) China’s growth momentum recover is proven to be robust, which boost market confidence.

HKEX scheduled to launch FINI on Nov 22nd, further enhance liquidity in HKD money market

FINI, also known as Fast interface for New Issuance. This is the new IPO process in HKEX, which has been planning since 2021. From the macro perspective, the material change is that the total volume of HKD required for pre-funding will dramatically decline. This will result in reduced amount of interbank transfer of cash, less less liquidity locked (transfer of aggregate balance between Hong Kong banks) and lower HIBOR volatility around the time of IPOs.

According to the HKEX’s study, the new funding process of IPO pipeline can reduce the net cash movement by 72-98%. Looking forward, only the largest IPOs will have a residual impact on HIBOR when the level of aggregate balance remains low.

EM Asia: Further tightening cycle may be needed

Philippines: Pre-emptive action to prevent 2nd round inflation

The Bangko Sentral ng Pilipinas (BSP) raise its target rate to 6.5% effective this Friday. The BSP sees 2024 headline inflation to average 4.7%, much higher than its September forecast of 3.5%. it also flagged that headline inflation will unlikely return to target for the rest of 2023. We believe the off-cycle surprise is partially driven by the weak PHP, which has already been defended at 57 (upper band of DBCC parameters)

Moving forward, we think the BSP will keep its policy rate steady at 6.50% in the November and December Monetary Board meetings. After all, core inflation is still threading downwards, which means the BSP's tight monetary stance is already in the works. That said, if core inflation follows the headline upward trend again, then there's risk that BSP will continue its tightening cycle further.

Thailand: End with hike but concern about inflation

The risk to rate hikes emanates more from the external side as fundamentals (current account deficit & relatively low interest rates) are unsupportive to Thai Baht. Recent Israel-Hama wars add risk to commodity price, which further triggered position on paying Thai rates.

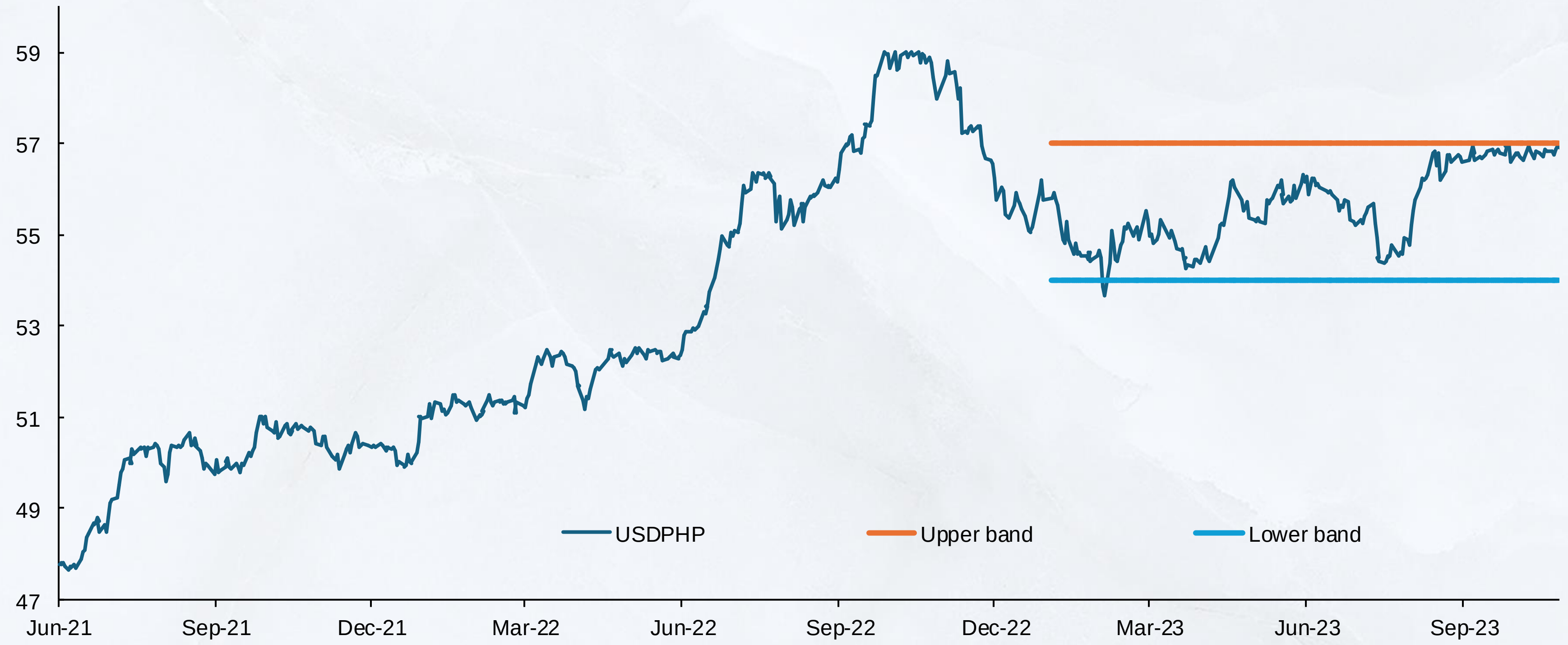
However, The BoT should finish the work already. The BoT had earlier noted that the policy rate should be appropriate to support long-term sustainable growth. However, we do note the risk that the MPC remains concerned about inflation in 2024, with the impact of the government's stimulus and El Nino likely to start becoming visible early. That said, we think with price pressures so low, an increase would still likely keep inflation within BoT's target band of 1-3%, keeping the bar high for more hikes.

Malaysia: 2024 Budget plan add risk to further hike, but depends on the trajectory

Malaysia delivered its 2024 budget on 13 October, aiming to narrow its fiscal deficit to 4.3% of GDP in 2024 (2023: 5.0%). However, this seems to be achieved by higher growth and a broadening in tax revenue, not outright expenditure reduction.

We are waiting for details on the timing of tax hike and the subsidy rationalism, but this could pose upside risk to inflation. Though we believe Bank Negara Malaysia (BNM) has completed its tightening cycle in 2023, close attention on inflation is warranted next year.

Fig. 7: USDPHP has been relatively stable at upper band of 57



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