Quarterly Strategy

HAMON INVESTMENT

4Q 2023

After the third quarter pullback, the final quarter of the year saw a strong rally in most asset classes and markets, as the investors believed that the US Federal Reserve would cut interest rates sooner in 2024 than previously expected, and data supporting the view that central banks should have reached the peak of their tightening cycles boosted most markets. The end of the "higher for longer" rate fears rallied developed market equities, which outperformed emerging markets amid ongoing worries over China's real estate sector. The MSCI World index was up 11.07% over the quarter, while the MSCI Asia ex Japan index was up 6.12%.

In Japan, the Nikkei followed the global market rally, gaining 11.43% in Q4. Despite weakening quarterly GDP growth, with 3Q GDP down 0.7% QoQ, GDP was still up 1.5% YoY. Governor Ueda of the BoJ hinted that the negative interest rate policy (NIRP) may be removed soon, given he has higher conviction that inflation will gradually increase to the 2% target going into FY2025, and he also mentioned that monetary policies would continue to be accommodative. We therefore believe that interest rates in Japan may begin rising in 2024, albeit at a slower pace initially. This should benefit financial stocks, due to improving earnings outlook for the next few years.

The Hong Kong/China markets continued to be under pressure over the quarter. The MSCI China and Hang Seng Index were down 4.22% and 4.04% respectively during the period, despite the Chinese government announcing a widening of the budget deficit by RMB 1tr to support the economy. While GDP growth was on track to be over 5% for 2023, three consecutive months of negative CPI dampened sentiment, leading to worries about ongoing deflation risks and the sustainability of the economy. This triggered significant outflow of more than US$10bn by active EU and US domicile funds in the HK/China market, alongside US$7.6bn outflow from the China A share market through the Northbound Stock Connect channel over the quarter. As corporates may have a more conservative outlook and guidance during their upcoming results season, we believe this will trigger downward revisions, which in turn would increase the chance of the markets to fall further in the first quarter of 2024. We therefore cut down our exposure in HK/China significantly to reduce the risk, especially in "growth" stocks, and will only look to add high dividend yield stocks gradually for income.

The US 10-year Treasury bond yield dropped below 4% in December, from a peak of almost 5% in October. As investors now expect a "goldilocks" environment, with aggressive rate cuts in the coming year amid expectations of lower inflation, the US market has continued its upside momentum. The S&P Index was up 11.24% over the quarter. We expect the US market may see some consolidation in the near term, especially after the sharp rally in the last two months of 2023, but lower inflation would continue to boost the market. The US November employment report showed solid job growth, with the unemployment rate declining to 3.7%, while non-farm employment increased by 199k, higher than expected. Headline CPI rose slightly by 0.1% MoM, while core CPI rose 0.3% MoM. Consumption continued to hold up, with retail sales gaining 0.3% MoM, while food services spending was strong, rising 1.6% MoM.

As mentioned, the US 10-year Treasury bond yield dropped below 4% in December, due to expectations of rate cuts, and US IG bonds rallied 6.82% over the quarter. While this is positive news, we believe the expectations of a 1.5% cut in interest rates for 2024 seems a bit too aggressive, along with the sudden and drastic drop in bond yields, which may lead to some volatility in the bond market in the near-term. We will therefore continue to closely monitor the bond market, and look to add longer duration bonds only when we see there is some correction.

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Quarterly Strategy (cont'd.)

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We remain positive towards global semiconductors, as we see the that sector has bottomed out. While there may be some bumpiness in the near-term, which is usually the case for sectors at the beginning of an upcycle, inventory issues have been cleared for general servers, PC, and smartphone related components and devices, and we should see positive growth going forward. We continue to favor AI-related names, like Nvidia, Super Micro, and Samsung, as we believe we will continue to see growth and expansion in AI usage.

Memory prices have also bottomed and prices should increase each quarter going forward. As such, we are confident that memory stocks will do well in 2024, and have increased exposure in names, such as Samsung Electronics and Micron, accordingly.

Our portfolio strategy for 2024 is to focus on:

1) AI-related companies in the US;
2) Global semiconductor names;
3) Japanese financials;
4) High dividend yield stocks in HK/China; and
5) Longer duration bonds.

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