EQUITY

Global Equities

Global equities continued to march higher in the last month of the year as narrative for a potential pivot by the Federal Reserve away from interest rate hikes this year to early cuts next year. Market movements in December (in local currency terms): US (+13.7%), Eurozone (+10.4%), Hong Kong (-0.3%), Shanghai (-3.9%), Japan (+8.4%), Taiwan (+12.0%), Singapore (+5.6%), Thailand (+2.4%) and Malaysia (+1.0%).

US & Europe

After acknowledging that higher UST yields have led to sufficient tightening financial conditions in November, the December Federal Open Market Committee (FOMC) meeting Summary of Economic Projections showed FOMC participants' assumptions of appropriate policy going forward only includes rate cuts. All but two voters indicated that rates would be lower in 2024 and indeed, every single dot was lower by the end of the projection horizon. Continuation of softening in inflation coupled with strong labour market reaffirmed the soft-landing scenario, resulting in further gains in risk assets.

While European Central Bank (ECB) president commented that dynamics in Eurozone favour a "higher-for-longer" environment, European equities gained in December amid steeper drops in inflation. As in the US, this prompted hopes that price pressures may be easing, and interest rate cuts are not far away. UK equities also rose during the month but lagged several other developed countries. Moving forward, Europe itself would have to navigate a tricky balance between slowing growth while walking the geopolitical tightrope between China and the US. Earnings growth is still expected to be muted compared to US, at 6.2% for 2024.

China

In Asia, Japanese shares rallied amid Bank of Japan (BOJ) decision to maintain interest rates, as widely expected by the market. Expectations of stronger Yen, continued corporate reforms, wage growth, and changes in Nippon Individual Savings Account scheme led the momentum in 2H2023 and is expected to continue in 2024. However, Chinese stocks were tepid despite the gains in global shares. In fact, all markets in the MSCI Asia ex Japan Index ended the month in positive territory apart from China, which had continued to struggle. Consensus' earnings estimates for offshore Chinese equities of 14% YoY in 2024 appear to be optimistic and vulnerable to downward revision.

Asia

The KLCI continued its monthly gain and recorded a 1.0% rise over the month of December, closing 2023 with -2.7%. Throughout the years, December 2023 appeared to be unusual with heightened average daily trading value above RM2.3b – December typically is a soft month for the Malaysian market. Foreigners had led the flows with YTL Power remains as the favourite, underpinned by the recent announcement of a partnership with NVIDIA. In addition, fears of Covid had resurfaced during the month which led to a jump in the healthcare sector.

General View

The outlook for equities appears largely favourable in 2024 under our two most likely scenarios of mild recession and soft landing, although in our mild-recession base case the reflationary effects of lower rates will be partially offset by some degree of earnings growth headwinds, and thus a judicious sector and stock selection process will be important. We continue to be positive on local equities as the recent earnings season gives us confidence that earnings delivery should continue to improve, catalysing the depressed equity market supported by the expected reversal in the strong dollar trade alongside promising macro policies.

FIXED INCOME

US Treasuries

A dovish Fed prompted a strong rally in UST as yields declined after the Fed kept rates steady at their 22-year high. The updated economic projections showed lower inflation expectations for 2024 and the Fed discussed the timing of potential rate cuts for the first time. In its policy statement, the central bank tweaked the language that could potentially signal that the officials are done with tightening policy, leaving investors cheering Powell's policy pivot. As a result, the 10-year Treasury yield fell 14 bps in the wake of the meeting on 13 December and ended the month at 3.88%, its first sub-4% close since August. Recent US economic data releases, while pointing to gradual deceleration of growth, have so far not suggested the need for rapid rate cuts. This may result in still heightened level of volatility in the UST yields in the near term as the Dot plot of rate expectations showed 75 bps of cuts next year compared to the more than 150 bps priced in by markets. Over the month, the 2-year yield declined 29bps to 4.25% while the 10-year adjusted down by 31bps to 3.88%, maintaining its inversion at -30 to -37bps range.

Malaysian Bond Market

MYR government bonds ended the year on a strong footing with a total return of 6.4 % despite the 25bps overnight policy rate (OPR) hike by Bank Negara Malaysia (BNM) and a record issuance of government bonds in 2023. Sentiment was boosted by the rally in developed market yields along with strong buying as investors look to build inventory ahead of the new year. Demand for duration was evident as the yield curve bull flattened supported by higher real returns. The annual inflation rate in Malaysia fell to 1.5% in November 2023 from 1.8% in the prior month, less than market forecasts of 1.7%. It was the lowest print since February 2021, with food prices rising the least in near 2 years. Inflation is expected to remain a key theme in 2024 with the rollout of petrol subsidy rationalisation. However, OPR should remain stable at 3% in 2024. The 2024 auction calendar saw similar number of auctions at the count of 37. Long duration supply in 15-30y is expected to increase but is expected to be offset by lower total supply, translating into an auction average range MYR4.6 billion - MYR4.9 billion, a minor reduction from the MYR5.0 billion average in 2023. Going into 2024, the bond market stand to benefit if US rate cut tailwinds gain traction in 2024. Widening of real interest rates should keep demand in check and maintain a supportive backdrop for bonds. Over the month, the 3-year MGS yield declined by 7bps to 3.48% while the 10-year decreased 10bps to 3.87%.

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