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Farewell, 2023, and Greetings to 2024!

In 2023, notable events unfolded, such as the Regional Banking Crisis in March and the subsequent suspension of the US Debt Ceiling in late May/early June. In China, substantial growth challenges, particularly in the property sector, emerged, marked by Country Garden's missed coupon payment. This prompted significant government stimulus in Q3 and Q4, including an additional RMB 1 trillion bond issuance. Toward the year's end, the US 10-year Treasury reached a 16-year high, and the Israel-Hamas Conflict contributed to global market weakness. However, the Federal Reserve's less hawkish tone in November/December resulted in a shift toward positive market sentiment.

We all know markets hate uncertainty and thrive on clarity. A clearer understanding of the future direction may provide additional room for a rally. However, **Five notable factors** are believed to shape the outlook for 2024.

The Big Questions for 2024

Are we in a new regime of higher global real rates?

Are there still geopolitical threats?

What to do with Global Tech and AI?

Can we escape a global slowdown?

Where is China landing?

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First and foremost, are we in a new regime of higher global real rates?

We think fears of dramatically higher real rates are overdone and we are near the end of the tightening cycle. The interest rate futures market is currently anticipating a potential rate cut as early as March 2024.

CME FEDWATCH TOOL - MEETING PROBABILITIES

MEETING DATE	300-325	325-350	350-375	375-400	400-425	425-450	450-475	475-500	500-525	525-550
1/31/2024					0.0%	0.0%	0.0%	0.0%	14.5%	85.5%
3/20/2024	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	11.9%	72.7%	15.4%
5/1/2024	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	11.5%	70.8%	17.2%	0.5%
6/12/2024	0.0%	0.0%	0.0%	0.0%	1.1%	17.0%	65.8%	15.7%	0.4%	0.0%
7/31/2024	0.0%	0.0%	0.0%	1.0%	15.5%	61.4%	20.2%	1.8%	0.0%	0.0%
9/18/2024	0.0%	0.0%	0.9%	14.2%	57.3%	23.9%	3.5%	0.2%	0.0%	0.0%
11/7/2024	0.0%	0.5%	9.0%	40.4%	37.0%	11.5%	1.5%	0.1%	0.0%	0.0%
12/18/2024	0.4%	7.3%	34.2%	37.7%	16.5%	3.5%	0.4%	0.0%	0.0%	0.0%

Source: CME Fedwatch Tool, 27 December 2023

Nevertheless, if developed markets (DM) continue to adopt a "higher for longer" interest rate regime, It could present a variety of challenges to emerging market (EM) assets, including reduced capital inflows, currency depreciation, and higher debt-servicing burdens for EM nations.

Secondly, are there still geopolitical threats?

Since the onset of US-China trade war, China is losing US import share, with Vietnam and Mexico emerging as key manufacturing hubs through "friend-shoring" and "near-shoring. Deglobalisation and onshoring are reshaping the global manufacturing landscape while India had also received influx of FDI in the recent years.

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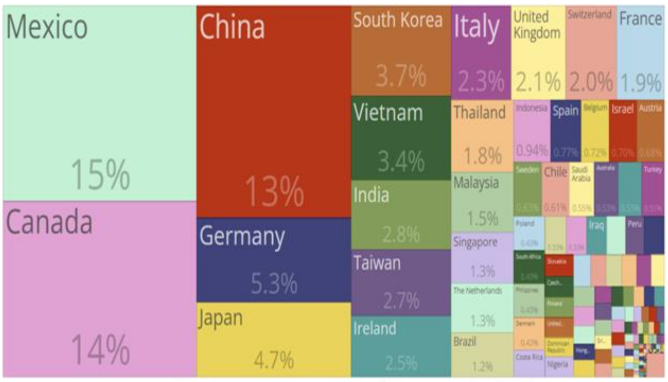
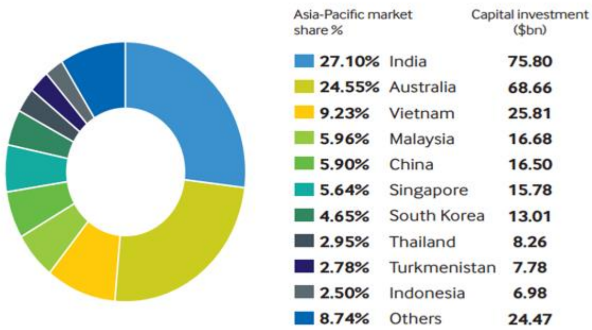
Geopolitics: The rewiring of globalisation

US Importing more than Mexico and Canada than China for the first time since 2003

ALL BY COUNTRY
TOTAL: 1.26T



In 2022, India led Asia Pacific in FDI capital investment



Source: Forbes, 11 July 2023 (Left); The fDi Report 2023, 16 May 2023 (Right)

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Separately, geopolitical risks, including the Middle East conflict and Taiwan's election, introduce uncertainties in 2024. Finally, the potential return of President Trump post-2024 could heighten international tensions, trade tariffs, and fiscal concerns, complicating global markets.

Thirdly, what to do with Global Tech and Artificial Intelligence (AI)?

If it weren't for the outstanding performance of the tech sector this year, the S&P would be showing little to no growth. Some analysts argue margins could face additional downward pressure next year as inflation falls, wages remain high, and interest expense resurges. However, a steep acceleration in TECH+ profits should offset this broader weakness. AI is playing an important role in innovation and efficiency, as it matures into a general-purpose technology, AI's impact on productivity could be relatively swift from here given its broad business applicability and low complementary investments needs. Yet, the true scale of economic payoffs will be shaped by its interplay with labour markets dynamics and demographic challenges.

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Fourthly, can we escape a global slowdown?

The answer remains uncertain, as the market is acknowledging certain potential risks, including declining corporate profits, low savings rates, sluggish industrial loan growth, high valuations, and lingering concerns about a recession. Valuations and risk premiums are notably high, with persistent worries about an economic downturn. On a separate note, global trade, responsible for nearly half of the growth slowdown since spring, continues to contract. About 30% of this decline is attributed to the tech sector, but there are indications of improvement, particularly in memory prices.

Finally, where is China landing?

China's GDP has now recovered back to its pre-Covid trend. According to IMF, China was projected to grow 4.2% in 2024 in the Oct projections, but was revised to 4.6% in 2024 in Nov. The revision is attributed to China's stronger-than-expected growth in the third quarter and a series of recently released policies. Separately, we observe a mix of economic signals, with improved retail sales and lending activities, contrasted by a slowdown in manufacturing and property sales. In the longer run, some market participants express concerns about challenges related to high debt, an aging population, and the erosion of labour cost advantages (leading to the relocation of production to lower-cost regions such as ASEAN).

All of these pose risks for 2024. At the same time, risks may also imply opportunities. We reaffirm our belief that there are still opportunities in the market, and we maintain a discerning approach in choosing high-quality stocks for our portfolio. However, it is crucial to exercise caution and carefully select investment options to ensure the best risk-adjusted returns. By taking a vigilant and discerning approach, investors can potentially reap the benefits of the current market opportunities while minimising risks.

Our investment portfolio focuses on quality companies that possess strong fundamentals, including stable earnings and a promising future outlook, and are led by capable management teams. Please click on the link to learn more or email us at phillipmutual@phillipcapital.com.my if you require any further information.