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Economic and Investment Insights 經濟和投資分析

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3Q Investment Outlook: Equity rebound may continue as global economic recovery picks up

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Q: Is the global economy bottoming out from the recession already?
A: Indeed, as we can see from some leading economic indicators, the global economy has stabilized gradually in the second quarter. Assuming the return-to-work strategy moves us forward and not take us a step back, the global economy should start to recover in 3Q'2020. Even if the recovery is not a "V-shaped", likely the economy is still heading in a positive direction. However, it will take several quarters for the global economic output to recover to the pre-COVID level.

Q: Do you think the market rebound that happened in the second quarter will continue into the third quarter?
A: We think it will. The largest positive factor is still the economic support from the global fiscal and monetary policies. The global central banks are continuing to loosen their policies which provides support for the financial conditions to rebound close to their easiest level ever. The ample liquidity flow is acting as a strong backstop for equities to continue the uptrend. The technical position of the equity market appears to be overbought in the short run but it still looks positive with the longer-term indicators.

However, volatility will continue as fundamental risks are ever present. The overall valuation of the stock market is comparatively high, meanwhile the expected earnings are facing downward adjustments. Investors also should not neglect risk factors such as a resurgence of COVID-19 infections and an exacerbation of an already strained US-China relationship.

Q: How should equity assets be allocated?
A: We are slightly bullish on equities in the third quarter. Among them, we are slightly positive on U.S. and China, while neutral on Asia and Japan. Europe is slightly negative, and Hong Kong is negative.

With all the risk factors ahead, it is still possible that the market will experience some short but sharp corrections again. However, we do not anticipate a new bear market in a short term while and certainly a re-testing of the market lows seems unlikely.

Q: Valuations in the U.S. market have been persistently high, why is it still worth looking into?

A: The valuations of U.S. stocks are relatively expensive and especially for the growth and large cap stocks. There is also a possibility that when economic activities resume, the confirmed cases of COVID-19 may accelerate again in the U.S. However, the U.S. is indeed one of the few major regions that has implemented large-scale fiscal and monetary policies. In fact, with the coordination of policies, some of the U.S. data has already outperformed market expectations in the second quarter. If the strength of the policies continues, it will help limit the downside risks of the U.S. stocks.

Q: Why are we slightly bullish on China but bearish on Hong Kong?

A: Out of all the major regions, China's economic situation is exceptional. Although the external demand was weak, the epidemic was under control relatively early which allowed the production facilities in China to reopen and be the first to rebound from the COVID-19 in the second quarter. At the same time, China still has room for further fiscal and monetary easing compared to some parts in Europe, U.S. or emerging economies. Of course, the tension between U.S. and China has become the biggest uncertainty when investing in China, especially right before the U.S. presidential election.

Hong Kong is struggling to recover from the recession that began last year and any intensification of the political situation will hinder the recovery further. It is almost certain that the Hong Kong economy will continue to decline this year. In the short term, local stocks are still facing considerable challenges.

Q: How should bond assets be allocated in this low rate environment?

A: In general, we are slightly optimistic on bonds. Among them, we prefer Investment-Grade corporate bonds as supported by the FED's corporate bond-buying programs. With the expectation that rates are going to stay low for a longer period, sovereign bonds may not generate meaningful return and therefore our view is neutral.

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