ARECA CAPITAL

FLASH

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For distribution to Areca Capital's Valued Investors

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AIMING AT THE BULL'S EYE

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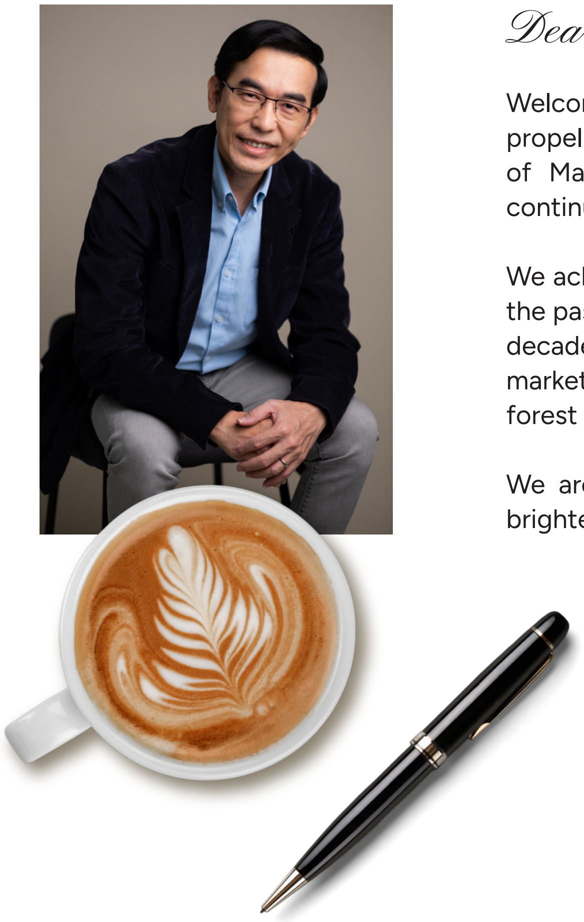
CEO's NOTE



Dear Valued Investors,

Welcoming the new year, Areca Capital anticipates a positive turn, propelled by the prospect of US rate cuts and the appealing valuations of Malaysian equities. As for the potential geopolitical shifts, we continue to stay agile while maintaining an appropriate asset allocation.

We acknowledge that it has been a challenging time in the market over the past few years. But if one's investment period stretches years, if not decades, it's important to not be overly reactive to the whims of the market – especially during times of market downturn. Don't miss the forest for the trees. Investing is for the long term.

We are looking and positioning ahead for our funds in view of the brightening outlook. Here's to a prosperous 2024 for us all!

Best Regards,

Danny Wong,
Chief Executive Director
Areca Capital Sdn Bhd

EQUITY

MARKET OUTLOOK & REVIEW

EQUITY

Market Outlook & Review

by Danny Wong,
Chief Executive Director

Reflecting on 2023 and Charting a Bullish Course for 2024

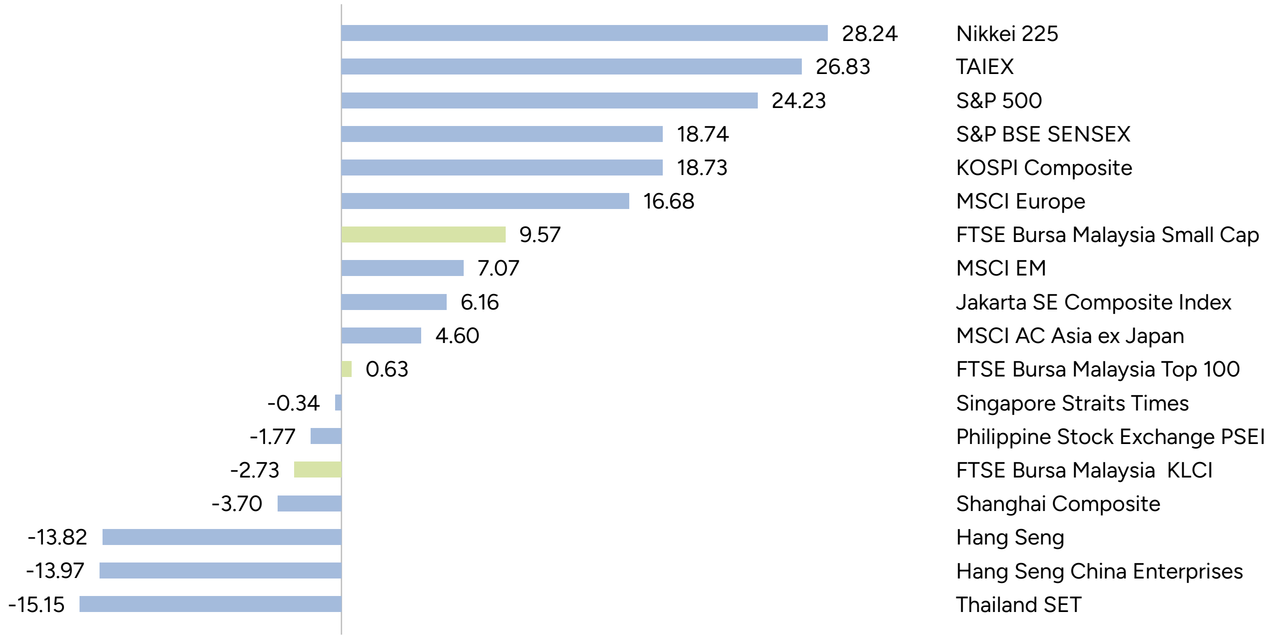
Q How would you sum up 2023 in terms of the equity markets?

What has dominated the headlines for the past year has been externally driven. The US Federal funds rates continued to climb through 2023 (albeit much more marginally compared to 2022) as the strength of the US economy continued to confound expectations. Interest rates are now in the 5.25% to 5.50% range. Furthermore, geopolitical tensions have come to the fore with the latest war between Palestine and Israel. Closer to home, the bond default by one of China's largest property developers, i.e., Country Garden, also put further pressure on China's property sector, weighing on economic growth and investors' sentiment as real estate has been a significant contributor to China's GDP.

Combined, what has happened in 2023 has bludgeoned the appetite for risk-taking, especially in Asian equity markets. Nevertheless, calls for a dovish Fed turning increasing louder towards the year-end, did support some markets to close stronger.

Market Performances Across The Globe (YTD as at 31 December 2023)

Market Performance in Respective Currencies



Source: Lipper, Data up to 31st December 2023

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For Malaysian equity, what is Areca Capital's outlook for year 2024, and why?

We had expected a rate pause or rate cut scenario to have taken place last year, but unfortunately, this looks to have been postponed and delayed to 2024 instead. With the US central banks' latest indication, a rate cut scenario in 2024 is finally within sight. This bodes well, as historical analysis has shown that Asian equities tend to perform when US interest rates are no longer at their peak or when interest rate cuts take place. This will help to lift positive sentiment in the market.

We hope this will drive flows back to Malaysia. Sentiment, rather than fundamental, could be the missing piece to the puzzle. Fundamentally speaking, Malaysian companies are in the right place at the moment. Valuations for Malaysian equity are attractive at the moment; close to a negative 1.5x standard deviation from its long-term mean.

In a nutshell, we are bullish for the brand-new year.

What are the sectors and themes in Malaysia that the funds would be positioned in?

In terms of thematic, we think the pump-priming sectors such as construction and property will do well in view of the higher development budget and potential announcement of major infrastructure projects such as the MRT 3 and High-Speed Rail (HSR). For value play, we like some of the bank, consumer and tourism names as proxies to economic recovery and revival. Larger-cap stocks will be the main beneficiaries if foreign funds come back in a bigger way in 2024.

For other sectors, we like selected segments of the technology and industrial. These are in line with some of the national agendas and major policies announced, such as the New Industrial Master Plan (NIMP) and National Energy Transition Roadmap (NETR). We also like some of the turnaround plays, like healthcare and transportation.

What are your thoughts on foreign markets?

Broadly speaking, a reduced strength in the greenback stemming from interest rate cuts in the US will have a huge impact on fund flows. We believe that funds may gravitate towards laggard markets with growth potential such, as Asia.

For China, we believe that economic data are bottoming. At this point in time, sentiment is still fragile on the ground, despite the regulation on technology and the property clampdown subsiding from their peak levels. The strength of the market's recovery will come from the direction of the policies that the government takes. We will take a very active hand in managing the China technology portfolio to navigate the volatility. The portfolio is currently diversified between the larger matured companies for their stability and on the other hand, their relatively smaller counterparts to position for growth.

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Q For an investor, how should we position ourselves?

One would still need to keep an eye out on the geopolitics front, i.e.: US-China relations, and monitor any risks of the blow-up to the conflicts we've currently been seeing in Palestine, Ukraine, and the Red Sea. Besides, we will be watching two key elections – Taiwan and the US – that might have broader implications affecting other nations.

Once your strategic asset allocation is in place, e.g.: 60% Equity with remaining 40% in Bonds, this allocation should be maintained for the long term. It's a risk to have sudden or big drastic moves, especially when the market swings.

Some small tactical allocations may be warranted here and then. A long-term investor can consider to increase their equity invested levels now to take advantage of the market lows.

FIXED INCOME

MARKET OUTLOOK & REVIEW

FIXED INCOME

Market Outlook & Review

by Edward Iskandar Toh,
Chief Investment Officer (Fixed Income)

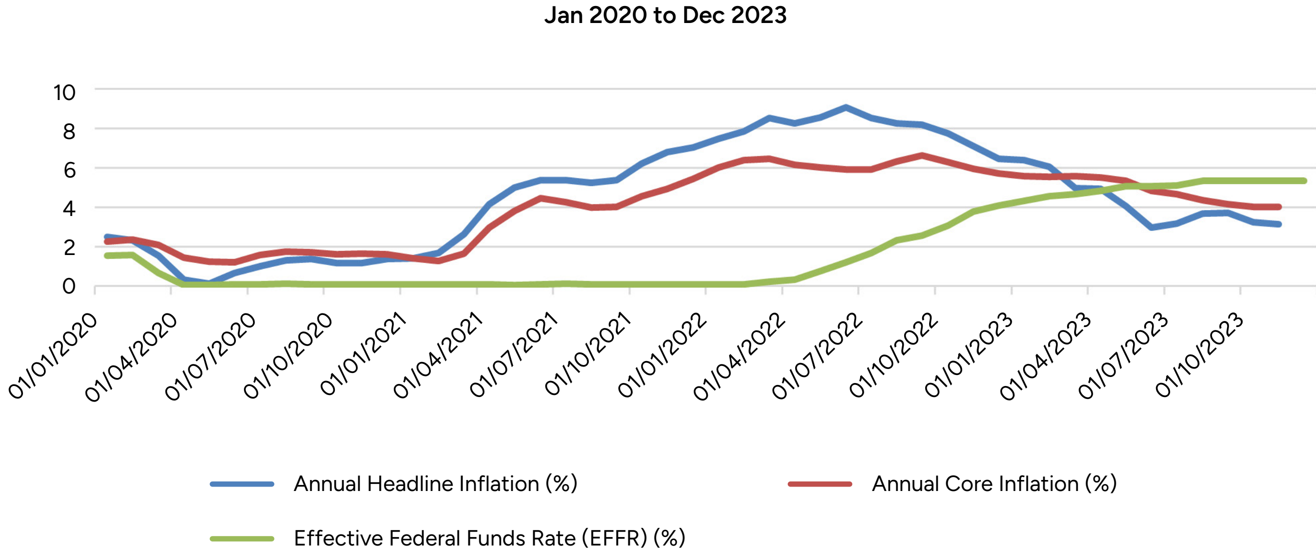
Favourable Outlook for 2024

Q How would you sum up 2023 in terms of interest rates?

Towards the end of 2023, the Federal Reserve (Fed) seemingly appeared victorious in its war against inflation. Its policymakers decided to leave interest rates in the 5.25% to 5.50% range at its last 3 meetings of the year while signalling that its aggressive hiking campaign is over. To put it into perspective, the Fed increased its Effective Federal Funds Rate (EFFR) by 525 basis points (bps) over 21 months, an average of 25 bps increase per month.

This rate hike cycle has been the most aggressive and fastest over the past 35 years. At the start of the cycle, March 2022, the annual headline inflation rate was 8.54%. Subsequently, it peaked at 9.1% in June 2022 and started falling, ending at 3.14% in November 2023. Similarly, annual core inflation cooled from its peak of 6.6% in September 2022 to 4.01% in November 2023.

United States Annual Headline & Core Inflation vs Effective Federal Funds Rate (EFFR)



Source: Bloomberg

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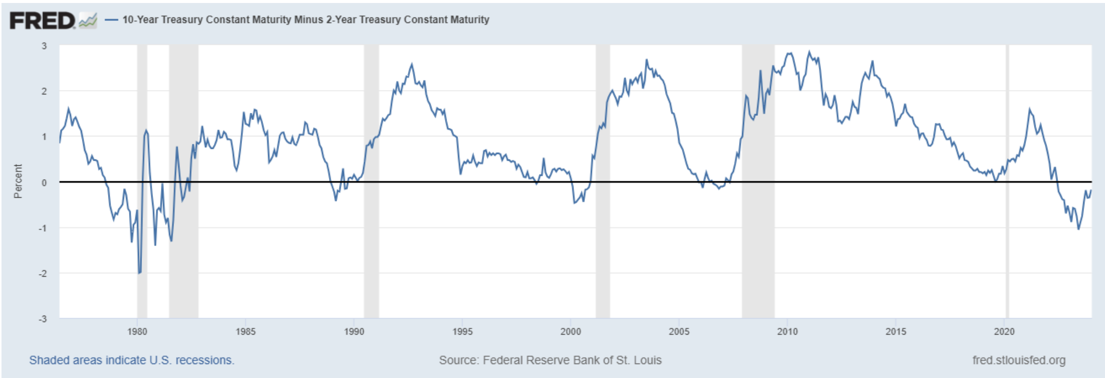
Q What is Areca Capital's outlook on interest rates for 2024, and why?

As the Fed maintains its long-term commitment to reach 2.0% inflation, the question lies on whether the Fed will keep interest rates higher for longer than expected or cut as much as 75bps in 2024, as signalled in its last meeting of 2023. While inflation rates are on a downward trend, both headline and core inflation remained sticky for most of the 2nd half of 2023.

Even so, a global economic slowdown is expected in 2024 as the effects of a high-interest rate environment kick in. Some signs were already showing. The 2-year and 10-year US Treasury (UST) yields remained inverted at -35 bps in December 2023, indicating an economic slowdown in the United States (US). Both new and existing home sales in the US have been on a downward trend, with the former dropping from 662k in July 2023 to 590k units in November 2023, while the latter dropped from 4070k to 3820k units in the same period.

In its October outlook, the International Monetary Fund (IMF) projected a relatively stagnant annual gross domestic product (GDP) growth of 2.1% in 2023 (2022: 2.1%) and a drop to 1.5% in 2024. The Euro Area is projected to see a larger slowdown with a growth rate of 0.7% in 2023 (2021: 3.3%) and 1.2% in 2024.



Source: Federal Reserve Economic Data (FRED)

Q What about the Malaysian economy?

Bank Negara Malaysia (BNM) is expected to take a more measured approach to Overnight Policy Rate (OPR) decisions. However, Malaysia was not dragged into the global race to curtail inflation. Rather, we were spared the impact of higher costs of domestic consumption and expenses. Our domestic policy of subsidising the cost of essential goods has helped keep annual headline inflation in check as it eased to 1.5% in November 2023 (October 2023: 1.8%), a 33-month low, mainly driven by moderation in food prices.

We believe that the current OPR rate, 3.0%, is the neutral rate and any need to cut will largely depend on the inflation rate and gross domestic product (GDP) growth. Upside risks to inflation stem from uncertainty towards the impact of subsidy rationalisation, rising commodity and food prices from further geopolitical tensions, and stronger domestic demand.

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Any cuts in US interest rates by the Fed would see a narrowing interest rate differential with our OPR; enhancing the attractiveness of the undervalued MYR. In turn, there would be a potential capital inflow to Malaysia through investment in assets or foreign direct investment (FDI). This is given that Malaysia remains a favourable investment destination while being underinvested as of end-2023 by historical and regional comparisons. Furthermore, favourable policies on tourism by the Malaysian Government would greatly benefit its service industry in the coming year.

Q What is Areca Capital's strategy for 2024?

All in all, we do not foresee any rush by BNM to cut interest rates. Any potential cuts in foreign interest rates, particularly in the US, would create an environment favourable to fixed-income investments.

Our strategy remains the same. We will continue to hold moderate to long-duration bonds which would enable us to gain from any potential interest rate cuts; or the sentiment of potential interest rate cuts; while also maintaining liquidity on interest rate hike risks. We would also favour stronger credits as opposed to high-yielding ones.

by Areca Capital

BULLETIN BOARD

New Private Trust Services and Refreshed Logo Unveiled

We are delighted to have launched our new private trust services and a refreshed logo in October 2023.

Our new private trust services provide tailored solutions and estate planning for high-net-worth and mass-affluent clients. We believe in making these services accessible to a broad spectrum of clients. By combining wealth and long-term investment management, we offer a holistic approach to help clients grow, preserve, and distribute their wealth through generations.

As for the refreshed logo, it embodies our vision of partnering hand-in-hand with our clients on their wealth management journey. The logo's distinctive elements reflect the stability and trust that Areca Capital has built over the years while embracing a fresh, contemporary look to signify its evolution.

Excited about the future, we remain dedicated to providing innovative financial solutions. The introduction of new private trust services and a refreshed logo mark significant steps towards this mission.

Watch our new brand film by clicking on the play button below to discover what true wealth means to us at Areca Capital. Enjoy!

Areca Capital's Brand Film

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