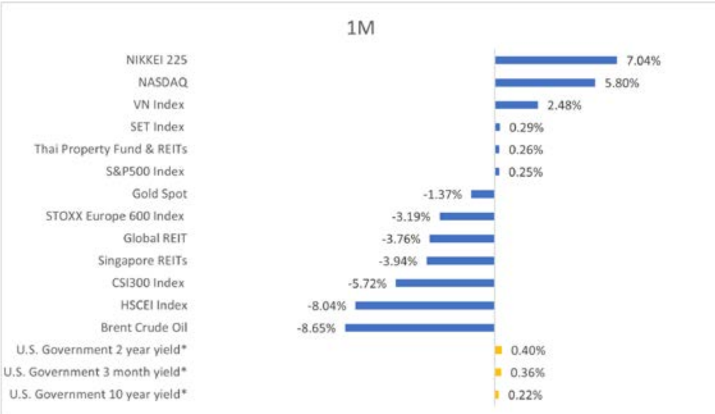
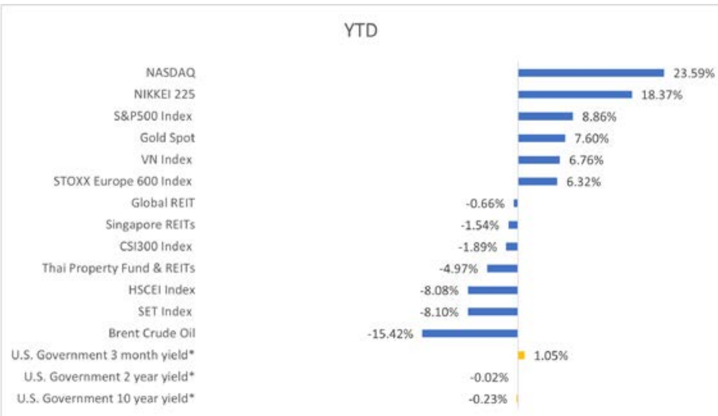
Principal Asset Management

Monthly Report

May 2023

Global Markets Performance in May 2023





Note*: This shows a change in yield not price return.

Source: Bloomberg as of 31 May 2023

Market Review for May 2023

US stock market slightly increased although an issue of US debt ceiling made the market volatile throughout the month. However, the senate successfully passed a bill to raise the debt ceiling before the deadline. EU stock market went down after the manufacturing sector was still weak and ECB continued to raise its interest rates to fight with inflation while China stock market was under pressure from worse-than-expected economic data and geopolitical conflict between the US and China. Vietnam stock market rose as State Bank of Vietnam (SBV) decided to cut interest rates by 0.50% to boost growth and retail sales remained resilient, reflecting strong domestic consumption. Global and Singapore REITs dropped significantly as US 2-year treasury yield increased and Gold decreased slightly after President Biden signed legislation to raise the debt ceiling into 2025. As a result, investors decreased their exposure of Gold as a safe asset.

US Stock Market: S&P500 Index rose slightly by 0.25% in May 2023 although the debt ceiling impasse between Democrats and Republicans caused the market concerned throughout the month. However, a deal allowing the US to borrow more money passed the House of Representatives by a vote of 314-117 and was signed into law by President Joe Biden by 5 June 2023 or the so-called X date. Regarding economic data, the services flash PMI for May increased to 55.1 above the market expectation of 52.6 but the manufacturing PMI was 48.5, signaling a contraction in activity. US inflation rose by 4.9% in April YoY, down from March's 5% increase while core CPI increased by 5.5% from a year earlier, due to persistently high shelter costs. Nevertheless, the main reason why S&P500 Index performed very well since the beginning of this year was strong earnings reports of large tech companies in particular. Therefore, the earnings announcement for Q2 23 and inflation will be the key factors in determining the performance of the market going forward.

EU Stock Market: STOXX Europe 600 Index dropped by 3.19% in May 2023 because of continuously weak manufacturing sectors and stubbornly high inflation. The eurozone manufacturing PMI in April was at 44.6, signaling a further decline in the health of the manufacturing sectors, while the eurozone services PMI remained above the 55 level, indicating expansion. Regarding Eurozone inflation data for April, CPI was up to 7.0% YoY in line with the market forecast, driven by 13.6% increase in food prices and core CPI increased by 5.6% YoY, also in line with consensus forecast. However, although inflation remained high ECB has changed its monetary policy to a slower pace of hikes in response to uncertainty of economic outlook and a further tightening of credit standards.

China stock market: Chinese stocks, both H-Shares and A-Shares, dropped by 8% and 5.7% respectively in May 2023, as the Chinese economy recovered more slowly than what markets expected. The PMI index for both the manufacturing and service sectors in May was below expectations, with 48.8 and 54.5 points respectively. Additionally, the inflation rate turned negative at -0.1% MoM in April, indicating deflation. Similarly, new loan applications saw a sharp decrease, totaling 718.8 billion yuan, compared to the previous month. These factors indicate a decline in confidence within the private sector, and the liquidity problem in the real estate sector has not been fully resolved. Furthermore, there is an increasing risk of tension between the US and China. Looking ahead, we expect both the government and the People's Bank of China will introduce additional stimulus measures to address liquidity issues and boost consumer spending. This will serve as a supportive factor for the growth of the Chinese economy.

Japan stock market: NIKKEI Index rose significantly by 7.04% in May 2023 but the market is not famous for investors as there are several main problems affecting Japan economy negatively like aging society, deflation, a sluggish economy and export dependence. However, when the Fed and ECB raise their interest rates Japan is only the one of developed countries which could keep its interest rate at very low level of -0.1% together with injecting a lot of liquidity continuously and implementing yield curve control. To adopt all of the policies Japan is required to spend large amounts of money. As a result, Japanese Yen has depreciated significantly since the beginning of this year. Nevertheless, its impact has turned to be positive in that some companies which are listed not in Japan can gain profit from exchange rates and valuation of the market is more attractive in an eye of foreign investors. Besides, although Japan needs to import most of its energy, a risk of incoming recession makes energy prices drop which can be considered as a factor in an improvement of import.

Thai stock market: SET Index increased by 0.29% in May 2023, with Thai stock market initially rising to a peak of 1,569 points before the Thai election day. However, after that the market experienced a decline due to concerns over the difficulty in electing the prime minister and the potential negative impact of the leading parties' policies on the capital market. Additionally, Thai exports in April contracted by -7.6% YoY, which was below the market's expectation of -2%. These factors caused Thai stock market to decline and close at 1,533 points at the end of May. Since the beginning of this year, Thai stock market has experienced an 8% drop, which is considered underperforming compared to global stock markets. However, the fundamentals of Thai listed companies over the next 6-12 months remain strong, and the forward P/E ratio is slightly below average. This presents an attractive investment opportunity for medium to long-term investors.

Vietnam stock market: VN Index rose by 2.48% in May 2023, despite concerns about potential power shortages. This rise can be attributed to a decrease in inflation in May to 2.43% YoY, which was lower than the previous month's rate of 2.8% YoY. As a result, the Central Bank of Vietnam decided to cut interest rates by 0.5% to reach 5%. Additionally, there was a positive rebound in industrial production, with a growth of 0.1% YoY, indicating improvement compared to the previous month's negative growth. Moreover, retail sales showed a strong increase of 11.5% YoY, providing support for the upward trend in the Vietnamese stock market. However, investors should closely monitor the economic growth in Vietnam, as the manufacturing purchasing managers' index dropped to 45.3 points, indicating contraction for the third consecutive month.

Fixed Income Market: US 10-year treasury yield increased from 3.4% at the end of April to 3.6% at the end of May as the likelihood of a further rate hike of the Fed has been significantly increasing to 75% from 48% over a week ago, according to CME

FedWatch Tool. Meanwhile, Thailand 10Y bond yield slightly increased to around 2.55% as the Bank of Thailand (BOT) raised the key interest rates by 0.25% in line with the market expectations. Although the Thailand inflation rose 2.67% YoY in April, it tends to increase slightly in the second half of the year due to a recovery of the tourism sector.

REITs: Thai REITs slightly increased by 0.26% in May 2023, driven by an more interest in high dividend yield compared to the government bond yield. The government bond yield tends to increase slightly due to Thai inflation decreasing along with energy prices. In contrast, Singapore REITs and Global REITs sharply declined by -3.94% and -3.76%, respectively, in May 2023. The declines were mainly due to an increase in 2-year US bond yields from 4.1% to 4.4% in the previous month. As a result, investors sold off both assets while awaiting clarity on the Federal Reserve's monetary policy in terms of potential interest rate cuts for this year.

Gold: Gold prices dropped by -1.37% in May 2023, pressured by a rise in US 2-year and 10-year bond yields, along with the passage of a bill to increase the debt ceiling by the US Congress. These factors caused investors to alleviate their concerns and reduce their exposure to gold as a safe asset.

Market Outlook and Investment Strategy for the next 3-6 months

- US tech stocks referring to Nasdaq Index rose dramatically in May 2023 and Fed decided to hit pause on interest rates hikes for June meeting as expected. However, the latest dot plot indicated that another two quarter percentage point moves are on the way which may begin in the next meeting. Meanwhile, ECB raised interest rates by 0.25% to 3.5% as expected and signaled more hikes are on the cards.
- As the Fed kept up hawkish calls in the latest meeting, credit conditions of banks in the US have tightened and US stocks may face the risk of more downward earnings revisions, slightly underweight rating is given to global equities but we still prefer China and Asia stock markets after People's Bank of China (PBOC) cut key policy rates such as seven-day reverse repurchase rate or one-year medium-term lending facility (MLF) loans to support economy and Chinese officials are considering further stimulus measures to stimulate domestic consumption and the property sector. Regarding Japan, if Bank of Japan (BOJ) keeps ultra-low interest rates, earnings of Japanese companies are likely to be upgraded as a result of the yen's depreciation.
- We keep our slightly overweight exposure to fixed income (prefer global fixed income) due to attractive yield and US recession probability. Currently, PIMCO GIS Income Fund, the master fund of **Principal Global Fixed Income Fund (PRINCIPAL GFIXED)** has a YTM of 7.12% as of 31 May 2023.
- Overall, we still recommend investing in quality-growth stocks because uncertainties tend to happen during the rest of this year, and we think investors should pay attention to an importance of asset allocation to create a proper portfolio by diversifying each asset class based on their risk appetites.

Portfolio Adjustment

- As in May 2023 Japan stock market rose significantly but this kind of the rise usually is not sustained, we have exposure of Japanese stocks slightly more than the benchmark. Similarly, Tech stocks have also increased drastically since the beginning of this year. Therefore, at the moment we focus on investing in mega cap stocks with high cash and stable income. From our point of view, the strategy can help reduce volatility of the portfolio resulting from the risk of incoming recession.

- We maintain high exposure of ESG stocks because in the long-term perspective they tend to deliver a good return. Big institutional investors continue to support environmentally friendly companies and such companies have a lower risk of corruption.
- Clear stimulus packages are still the hope of China stock market. However, for the time being the market expects the measures are not strong enough to improve the economy as forecast and geopolitical risks also put pressure on the market. As a result, we have only small exposure of China stocks.
- Our exposure of Thai stocks is equal to the benchmark. We select companies which are almost not affected by global recession and are not related to political issues because of the uncertainty of electing the prime minister.
- We have higher exposure of global fixed income than the benchmark. If the Fed stops raising rates, this will positively impact on global fixed income. Meanwhile, we have same exposure of Thai fixed income as the benchmark, focusing mainly on gaining holding period return.

Note:

- Fed stands for Federal Reserve, US central bank.
- ECB stands for European Central Bank
- REIT stands for real estate investment trust
- YoY stands for year-over-year, which is a way of measuring how a number has changed compared to the same period a year earlier.
- CPI stands for consumer price index, a key indicator to measure inflation.
- PMI refers to the Purchasing Managers Index, a measure of economic health in the future.
- Overweight refers to a larger portion of an asset class compared to a benchmark.
- Neutral refers to the same portion of an asset class as a benchmark.
- Underweight refers to a smaller portion of an asset class compared to a benchmark.
- H-Shares stands for stocks of Chinese mainland companies that are listed on the Hong Kong Stock Exchange.
- A-Shares stands for stocks of mainland China-based companies that trade on the two Chinese stock exchanges, the Shanghai Stock Exchange and the Shenzhen Stock Exchange.
- Hawkish refers to an aggressive stance of the central bank that prioritizes keeping inflation low by raising interest rates.

Investment Strategy Team

Supakorn Tulyathan, CFA – Chief Investment Officer

Thaned Lertpetchpun – Investment Strategist

Mintra Juntavitchaprapa – Investment Strategist