2025 Market Outlook

Balancing global dynamics

Macroeconomic analysis

The US economy stands out among developed markets, but the gap is narrowing

The global economy in 2025 is expected to show a slower growth in developed markets compared to 2024, while emerging markets are expected to perform slightly better than in 2024. However, there are some differences within developed markets: the U.S. economy may slow down more significantly than the current market consensus estimate (with the year-on-year growth rate for all four quarters still above 1.9%). In other regions, although the recovery in the Eurozone and the UK in the second half of 2024 was weaker than expected, the trend of year-on-year growth is still improving. It is expected that the overall performance in 2025 will still lag behind the U.S., but the gap is narrowing. In China, the market is currently focused on whether the Central Economic Work Conference in December can propose effective fiscal "stimulus" policies; otherwise, achieving 5% economic growth in the future remains challenging.

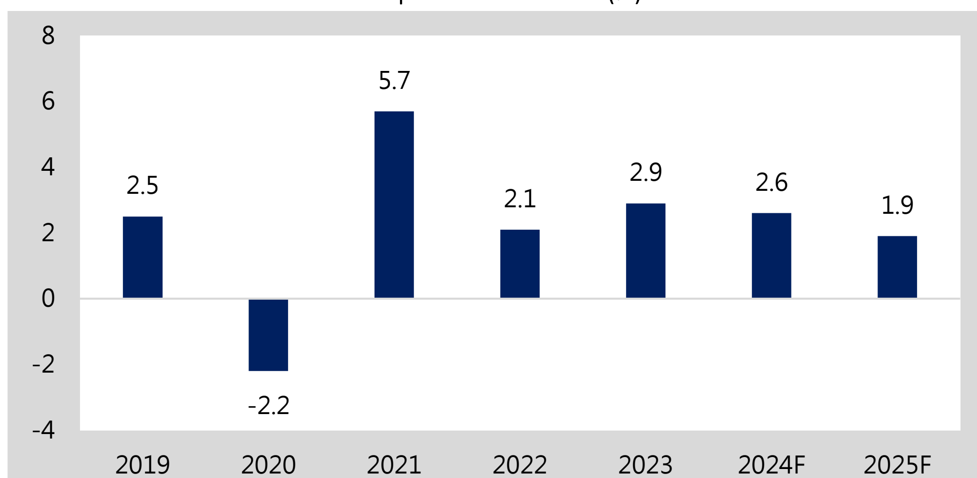
From an industry perspective, global manufacturing performance is sluggish. In the U.S., the recovery since the second half of 2023 has been weak and unclear, mainly due to overall weak capital expenditure (contrary to the general impression of strong AI investment). As for the service sector, U.S. services have shown unexpectedly strong performance, which has been key to the U.S. economy outperforming other mature markets over the past six months. However, with declining savings rates and increasing financial burdens, credit consumption momentum will weaken, so the U.S. economy is expected to decline in 2025.

The biggest change comes from the impact of Trump's re-election as president. Currently, its economic impact is difficult to determine, but it may adversely affect inflation. Trump's four major policies—tax cuts, increased tariffs, immigration restrictions, and financial deregulation—have an uncertain execution order, but start from restrictions on immigration and the implementation of tariffs are visible, although the tariffs are likely to be introduced in phases (by country and rate). Therefore, throughout the year, the four policies mentioned above may be announced in the first half, which will increase the volatility of financial markets. However, from the perspective of the actual impact of these policies, higher economic risk for the United States is still in the second half of the year, and whether there will be improvement in the fourth quarter depends on the policy changes at that time.

With the cooling of U.S. inflation and the labor market, the economy has returned to a roughly balanced dual-risk target of employment and inflation. Inflation in housing and core services remains too high, and the process of cooling core service inflation is slow, with core inflation expected to continue declining in 2025. However, Trump's increased tariffs and anti-immigration policies could lead to a resurgence in goods and services inflation, posing a risk of rising inflation again in 2026.

The labor market has returned to a state of full employment, with the unemployment rate for non-temporary jobs slowly rising, which may affect the currently strong consumer spending. The lagging impact of high interest rates on the economy in 2025 remains unresolved, coupled with the impact of Trump's trade policies on the economy, posing further downside risks to the labor market. Overall, the Federal Reserve will gradually cut interest rates to reduce restrictive rates, while inflation is expected to fall to the target. In November 2024, the policy rate was cut by 25 basis points to 4.75, and further cuts of 75-100 basis points are expected. This rate-cutting cycle will reach a low point of 3.75-4.0% in 2025, with the possibility of rate hikes resuming in 2026.

Graph 1: The U.S. GDP (%)



Source: Bloomberg, Prepared by KGI

The EPS of the S&P 500 is expected to have mid-to-high single-digit growth

In terms of U.S. stock investment, after two consecutive years driven by the AI wave, the overall U.S. stock market is no longer cheap. However, we see opportunities for sector rotation in the future, mainly reflected in estimated earnings improvements, particularly in finance, materials, industrial, and healthcare sectors. Overall, we estimate that U.S. stocks' S&P 500 earnings in 2025 will still grow in the mid to high single digits, with an estimated annual return of 6-12%, down from the previous two years. From a timing perspective, we believe the positive post-election stance can be maintained in the first quarter, but starting in the second quarter, the risks of Trump's policies and economic downturn expectations will be reflected, causing market volatility; risks will further increase in the second half, with the first half overall better than the second half.

Republican full control may adversely affect bond market

As for bond investment, economic cooling and declining inflation would typically be favorable for bond investment, but Republican full control may adversely affect bond investment. For example, worsening fiscal deficits will increase bond issuance costs, rising inflation will lead to higher yields on medium- and long-term bonds, and poor fiscal discipline and long-term inflation risks will push up neutral interest rates and bond term premiums. Therefore, medium- and long-term government bonds are less favored in 2025, while some short-term government bonds or high-credit-quality corporate bonds, with relatively higher yields, can provide good interest income. Overall, 2025, with increased inflation risk and potential monetary policy reversal, is not a favorable time for bond investment.

Global strategies

Core strategy - ACE

Alternatives: Gold and cryptocurrencies — assets with lower correlation to traditional stocks and bonds.

Credit Selection: Prioritize high-rated bonds, focusing on opportunities in corporate bonds.

Elite Stocks: Prefer U.S. and Japanese stocks, maintain a preference for large-cap over small-cap, and pay attention to sector rotation.

Preference in developed markets: The U.S. > Japan > Europe

With Trump's election and the Republican Party taking control of both the House and Senate, creating a "red wave," historical data since World War II shows that the S&P 500 index's average return under a red wave is lower than the overall average. Fundamentally, the current S&P 500 stock risk premium remains low, with a P/E ratio (around 27 times) more than 1.5 standard deviations above the 30-year average, indicating it is not cheap.

Currently, the overall the U.S. economy is doing well. Although interest rates have started to decrease, they remain restrictive, the likelihood of an economic slowdown continued to follow. Additionally, the red wave may increase stock market volatility next year. In the second half of 2024, we have noticed signs of sector rotation. The revenue growth of AI giants (Microsoft, Google, Amazon, and META) has not kept pace with the rise in capital expenditures. Stocks with a high proportion of overseas revenue have seen their advantages diminish, and subsequent stock prices may fluctuate at high levels. However, the U.S. AI-related and large companies hold a unique position globally. Investing regularly (fixed amount and frequency) may be more ideal, while also paying attention to the overall portfolio weighting.

Some industries may benefit from Trump's policy of bringing manufacturing back to the US. For example, domestic manufacturing may benefit from further tax cuts to 15%. Currently, we prefer the financial, materials, industrial, and healthcare sectors. The market expects an increase in the fiscal deficit, which generally benefits the performance of materials and industrial stocks. Capital goods within the industrial sector often experience a honeymoon period after presidential elections due to expectations of increased construction. Additionally, if the economy maintains a soft landing scenario, growth stocks (especially non-essential consumer goods and technology) are more favorable. Conversely, if the economy significantly deteriorates and the risk of a hard landing increases, defensive sectors such as essential consumer goods, healthcare, and telecommunications may be more ideal.

"Trump trade"

With Trump's election and the Republican Party taking control of both the House and Senate, the following industries have become market focus:

1. Traditional Energy: Prioritizing the development of traditional energy, with the importance of green energy decreasing.
2. Financial: Easing financial regulations, including for traditional financial institutions and virtual assets like Bitcoin.
3. Non-Essential Goods: Implementing tax reduction policies that may stimulate consumption.
4. Defense: Requiring allies to pay for their own defense expenses, stimulating demand for weapons.

However, the above "Trump trades" have already seen significant gains following the election results. To transition from short-term "trades" to medium- to long-term "investments," subsequent policies need to be implemented to support the fundamentals, which could help to sustain the upward trend.

The U.S. large caps vs. small caps

In the large-cap vs. small-cap style, it is generally recognized that small-cap stocks perform better than large-cap stocks after interest rate cuts. During Trump's first term, small-cap stocks indeed had better returns. However, we believe that the advantage of small-cap stocks may be difficult to replicate in his second term. Currently, the economy may slow down due to high interest rates, which is different from Trump's first term when the economy was recovering from a low point. We expect mid- to large-cap stocks to remain relatively favorable, as the interest rate cut cycle can practically improve the refinancing costs for mid- to large-cap stocks. The S&P 500 equal-weight index holds relatively fewer giant companies and more mid- to large-cap stocks, with a P/E ratio of about 20 times, slightly higher than the 30-year average of 19.3 times. The sector composition includes more industrials (16%) and financials (15%).

Maintaining a positive view on Japanese domestic consumption stocks

With Shigeru Ishiba re-elected as Prime Minister, his coalition does not hold a majority in the House of Representatives. This gives smaller parties, which favor expansionary policies, greater influence. Policies supporting the economy are expected to continue, and the new parliament shows potential for consensus on individual issues, reducing political uncertainty.

Over the past two years, the Nikkei index has performed well, with a high proportion of export stocks benefiting from a weak yen, which has contributed significantly. Overseas investors have seen good returns after hedging against the yen. However, the continued weakness of the yen has imported inflation. In 2024, the end of negative interest rates and Yield Curve Control (YCC) may see the Bank of Japan intervening to support the yen. In the same year, the spring wage negotiations in Japan resulted in the highest wage increases in nearly 30 years, with real wages on an upward trend. This supports consumption, and wage growth is expected to drive inflation towards the 2% target. With real interest rates remaining low, the Bank of Japan may have more room to raise rates. Stable wage growth is favorable for domestic demand stocks (such as food and beverage, retail sales), and attention should also be paid to the effectiveness of corporate reforms in Japan. The yen is expected to appreciate in the medium to long term, making non-hedged categories more favorable.

Weak eurozone economy

The Eurozone's economic growth is relatively weak, with markets and official institutions continuously lowering GDP forecasts for next year. The number of bankruptcies in Germany and France is rising, and earnings estimates for European companies in 2025 have been downgraded. The performance of European and the U.S. stock markets has diverged more clearly after the U.S. election. In addition to internal political risks, Europe also faces potential risk factors such as the U.S. tariffs and a slowdown in China's economic growth. Even if the European Central Bank cuts interest rates faster than the US, it is due to the region's weak economy rather than inflation reaching its target. Comparatively, Switzerland and the UK, with their more defensive characteristics, are relatively ideal within the region.

Trump preferred weaker dollar, interest rate differentials could be the key consideration

Generally, a strong dollar is unfavorable for asset prices, and weaker non-US currencies put pressure on Asian markets. Currently, the US Dollar Index is above 105. Considering the strong momentum of the dollar, we expect it to remain relatively strong in the first quarter of 2025. However, Trump has repeatedly mentioned his desire for a weaker dollar to support the U.S. manufacturing and reduce the trade deficit.

Traditionally, a strong dollar negatively impacts the U.S. domestic manufacturing but benefits countries that rely on exports. The U.S. manufacturing has been in long-term decline, currently accounting for about 10% of overall GDP. The latest US ISM Manufacturing PMI for November is 46.5. Since the tightening of monetary policy in 2022, the PMI reflects continued weakness in the U.S. manufacturing, with recovery hampered by high interest rates and weak capital expenditure. However, before the COVID-19 pandemic, the manufacturing PMI was in the expansion range. Lower interest rates and a weaker dollar may help mitigate the decline in manufacturing, while stronger currencies of trade partners could increase their attractiveness for setting up factories and investing in the US.

Looking back at 2017 to 2020, before the pandemic, despite Trump imposing tariffs on multiple countries during his previous term, the nominal amount of the US trade deficit continued to increase, while the trade deficit as a percentage of GDP remained around 2%. Between the US and China, the main impact of the trade war was a narrowing of the US trade deficit with China, with the annual trade deficit in 2019 shrinking by 18% compared to the previous year, as import sources shifted from China to other regions. After the pandemic outbreak, the U.S. bond yields rose to multi-year highs, the dollar strengthened, and the trade deficit widened, reaching about 3.2% of GDP in 2023. A weaker dollar could help improve the trade deficit.

A weaker dollar may support exports and manufacturing, which the Trump administration might welcome. In 2017, the first year of Trump's presidency, the US Dollar Index fell by about 10% for the year. At that time, the Eurozone economy was performing well, with GDP growth of 2.6% for the year. Currently, the Eurozone economy is hovering on the brink of recession, with a more aggressive rate-cutting pace than the US. Among developed markets, the US economy is relatively stable. If a weaker dollar is desired, narrowing the interest rate differentials with other currencies may be necessary, making the pace of the U.S. rate cuts crucial.

More tariff increases in the second half of 2025

After the "trade war" broke out in 2018, US inflation did indeed rise slightly, with the overall CPI increasing from 2.1% at the beginning of the year to 2.8% in June. From July 2018 to March 2020 (pre-pandemic), core services inflation only rose moderately (core CPI averaged 2.2%, peaking at 2.4%). However, the strengthening of the dollar in 2018 may have offset some of the impact of rising tariffs. In 2018, the US sanctioned Iran, causing WTI oil prices to rise from an average of $54 per barrel in 2017 to $71 per barrel in 2018, contributing more to overall inflation than other policies.

Although the US achieved an energy trade surplus in 2020, shocks to energy supply can push up inflation (as seen with the Russia-Ukraine war in 2022). How the Trump administration will implement Trade War 2.0 remains uncertain. Energy prices can fluctuate due to geopolitical events, and policies towards oil-exporting countries like Russia and the Middle East will significantly impact the U.S. inflation prospects.

The impact of tariffs on inflation will depend on which goods and countries are taxed, as well as the details of exemption clauses. Trump may aim to use tariffs to reach agreements and increase investment from trade partners in the US, while avoiding increased tariff barriers that could lead to a decline in the U.S. exports, further appreciation of the dollar, and higher inflation. Additionally, a stronger dollar would offset some of the tariff impacts.

Excluding the effects of trade policies and tariffs, the continuous decline in the U.S. labor voluntary quit rates and employment costs, which lead to core services inflation, suggests that core services inflation is still on a downward trend. The market expects core PCE to return to 2.3% by the end of next year (down from 2.7% in September 2024). With inflation on a downward trend, policies to increase tariffs in the second half of 2025 may slow the rate of inflation decline or even cause it to rise.

The red wave may slow the pace of disinflation

In 2024, the US entered a rate-cutting cycle, with the Federal Reserve shifting its focus to balancing the labor market and inflation. In the fourth quarter of 2024, the U.S. employment and other economic data continued to exceed expectations, and Treasury yields rebounded from low levels, with recession concerns nearly disappearing.

The extension of the Tax Cuts and Jobs Act (TCJA) mentioned by Trump is expected to reduce the U.S. government fiscal revenue. When locking in long-term bond yields, the market may demand a higher term premium as compensation, which is one reason for the rise in the U.S. long-term bond yields in the fourth quarter of 2024. Policies mentioned by Trump before the election, such as deporting illegal immigrants, increasing trade restrictions, and tax cuts, could also exacerbate inflation. This poses a risk of rising medium- to long-term bonds yield and could push up the dollar. However, this contradicts the desire for a weaker dollar to support

exports, and excessive restrictions could also drag down the US economy. We believe Trump tends towards "pragmatism," balancing the impacts of "America First" and "inflation stability" when implementing policies.

Preference for short-term bonds

We expect bond yields to fall to 3.7-4.2% in the first half of 2025. With more tariffs and tax cuts likely in the second half of 2025, the economy may transition from a soft landing to no landing, increasing the chances of inflation rising again, which could push bond yields up once more. If the neutral rate rises to 1.0-1.25% and long-term inflation rises to 2.5%, the federal funds rate will fall between 3.5%-3.75%. With unstable fiscal revenue and economic growth expectations, the yield spread between long and short bonds could rise to 100 basis points, and the 10-year bond yield could exceed 5%, although this level may not occur during next year's rate-cutting cycle.

The pace of inflation decline may slow, and medium- to long-term bond yields may remain relatively high. Consider increasing short-term bonds or shortening the duration of the bond portfolio. Since the economy may still slow down in the first half of 2025 and we are in a rate-cutting cycle, medium- to long-term bonds may still gain in price. However, attention should be paid to inflation and economic growth expectations in the second half of the year, which may drag down the performance of medium- to long-term bonds.

Maintain preference for high-rated corporate bonds

In 2020-21, under the low-interest-rate environment of the pandemic, the U.S. companies issued a large amount of corporate bonds, making them more resilient to subsequent monetary tightening. This year, the total issuance of the U.S. investment-grade corporate bonds reached about $1.7 trillion, an increase of about 40% from last year's $1.2 trillion. After 2025, more companies will need financing and will be forced to finance in the current high-interest-rate environment, with average corporate financing costs continuing to rise. The economy may be cooling in the first half of 2025, making investment-grade corporate bonds with lower credit risk still an ideal strategy.

De-dollarization promotes gold price increase

Historically, gold prices have been negatively correlated with the U.S. real interest rates, but this has decoupled in recent years, with both rates and gold prices rising. The Russia-Ukraine war has spurred a global de-dollarization trend, with central banks reducing dollar assets and increasing gold reserves, especially in emerging countries. Among the top 10 gold reserve countries, Russia and China have seen the highest increases in reserves. The trend of U.S.-China power divergence continues, and increased gold holdings by emerging countries may further support gold prices. According to the International Monetary Fund, the U.S. still holds the highest gold reserves globally, and rising gold prices are also beneficial for the U.S..

The red wave may slow the pace of disinflation, and with the Republican administration potentially increasing the fiscal deficit, traditionally beneficial to real assets like gold, market turbulence has historically supported gold prices. However, improved geopolitical risks may put downward pressure on gold.

Trump administration's positive attitude towards cryptocurrencies

The Trump administration has a positive attitude toward cryptocurrency assets. Trump's victory has significantly supported the trend of cryptocurrencies, with Bitcoin once rising close to $100,000 per coin before falling back. In 2024, more the U.S. legislation may promote or relax regulations on Bitcoin and cryptocurrencies overall, but specific legislation for Bitcoin as a reserve asset is still pending.

Although a series of related assets (spot ETFs, futures, etc.) provide liquidity for investors, institutional investors (especially trend-following algorithms) can increase Bitcoin's volatility. Additionally, the SEC's approval in October for Bitcoin spot ETFs to trade options may increase market maker hedging transactions. In the short term, we believe Bitcoin's volatility may remain high, and it is not advisable to hold too much in an overall portfolio. Countries using it as a reserve must bear significant risks. Over the past 10 years, Bitcoin has experienced three periods with maximum drawdowns exceeding 70%.

China macroeconomic

Tariffs and policy : 2025 sees test of China's confidence

Looking back at the first three quarters of the year, the Chinese economy grew 5.3% YoY in Q1, beating the expected 4.8%, but the momentum slowed down afterward. In Q2 and Q3, the growth rates came in at 4.7% and 4.6% respectively. This brought GDP growth for the first three quarters to 4.8%, below the government's target of around 5%. China's economic growth has been trending down quarter by quarter, indicating strong downward pressure on its economy. Hence the Chinese government has introduced a package of counter-cyclical policies in recent months, which include not only monetary policies such as reducing reserve requirement ratios (RRRs) and interest rates but also a relatively large-scale debt-swap program to ease the stress on local governments' budgets, to release the resources for supporting the economy.

More incremental policies from the Chinese government

Take debt relief as an example. At the Standing Committee of the National People's Congress (NPC) meeting on November 8, China proposed a RMB10 trillion debt alleviation quota (or RMB12 trillion if the hidden debt for shantytown reconstruction is included and repaid according to the original contract). The Ministry of Finance (MOF) promptly issued the RMB6 trillion debt quota to local governments the following day and strengthened its policy guidance. In addition, the MOF announced in mid-November that the proceeds from the issuance of ultra-long-term special national bonds to support the large-scale equipment replacement and consumer goods trade-off, amounting to RMB300 billion, had been delivered.

Benefiting from the effects of existing policies and the anticipation of new policies, China's economic data for October has improved. In particular, retail sales growth accelerated to an eight-month high of 4.8% YoY, which reflects a further strengthening of consumption recovery. A closer look at the latest domestic demand situation reveals that the tick-up was mainly due to:

- The largest and most extensive "Singles' Day" has significantly driven demand for consumer goods
- Continued efforts in home appliance and automobile subsidy policies have further promoted related consumer goods
- Apparent property demand pick-up in October

Going forward, as income subsidies targeting specific groups of people increase, the unemployment rate remains low, downward expectations of housing prices lessen, and consumer good subsidies expand, the propensity to consume is forecast to rise marginally. If consumption tendency returns to the pre-pandemic level, retail sales growth is expected to climb to over 6%, which should help stabilize the overall economy.

5% GDP growth for 2025 facing lingering challenges

Yet it is important to note that although market confidence is somehow uplifted by various policy measures, which led to the recent improvement in economic data, the global environment remains dauntingly complicated and the overall domestic economic momentum is still fragile. We are of the view that in the next stage, macroeconomic regulation and control needs to be stepped up while investment and consumption have to be bolstered further.

In fact, although the debt relief program mentioned above looks sizable, fiscal "stimulus" is lacking. China needs fiscal policy along with stimulus measures that are large and direct enough to make a difference in the medium to long term. China's economy is in a structural predicament, as evidenced not only by the low growth rate of the Chinese economy compared to its own past, but also indirectly by the lackluster performance in recent years of countries that used to be dependent on China (e.g. Australia) and of the resources that China needs (e.g. metals in raw materials).

Large and direct fiscal stimulus required

From our perspectives, even if China introduces more policy stimulus, but if it is not "direct" enough (e.g. a fiscal policy package that directly helps you spend, rather than just "encourages" you to spend), the effects will not be apparent. This is evidenced by the prevailing monetary policy, where people are reluctant to borrow money despite the low interest rates. This shows a lack of confidence in the market after the real estate bust. Fortunately, at two press conferences held on October 12 and November 8 respectively, Finance Minister Lan reiterated that counter-cyclical adjustments are definitely not limited to the latest debt relief package and commercial bank capital injection and that there will be ongoing fiscal policy objectives:

- actively utilizing the room for raising deficit;

- expanding the scale of issuance of specialized bonds, broadening the areas of investment, and increasing the proportion of proceeds to be used as capital;
- continuing to issue ultra-long-term special national bonds to support major national strategies and security capacity building in key areas;
- increasing efforts to support large-scale equipment renewal, and expanding the variety and scale of consumer goods trade-in;
- broadening the scale of transfer payments from the Central Government to local governments and stepping up the protection of inputs in key areas such as science and technology innovation and people's livelihood.

We are expecting that China will continue to advance its medium-term policy stimulus (more rate cuts and other individual measures are possible by year-end; any large-scale incremental fiscal program might have to wait until after next year's Two Sessions). Moreover, the upcoming focus will be December's Central Economic Work Conference (CEWC), at which the policy setting for next year will be determined.

Increased pressure on China's economy due to red wave

Investors are particularly concerned about the impact of Trump being re-elected as President of the United States on China-US relations and the Chinese economy. Compared to areas such as diplomacy, finance, and technology, tariffs have been the recent focus of the market. If Trump insists on raising tariffs on all Chinese imports to 60%, the impact on China's trade and economy will be significant; however, a number of variables are here, including 1) the final tariff rates; 2) the pace of the increase (gradual or across-the-board); and the scale of tariffs exemptions. In short, China's economy next year will be driven by two opposing forces: U.S. policy and stimulus efforts of the Central Government.

In sum, as confidence is yet to be restored, the goal of boosting domestic demand and consumption, which has been emphasized over the past years, is harder to achieve than expected. This might have to do with China's not-yet-returned animal spirits. In addition, the continued sluggish employment performance has led to the limited growth in wages (especially for new employees). All this is making people reluctant to spend like they did in the past. Given such stubborn structural problems, we believe that achieving a 5% economic growth rate in China in 2025 will be challenging.

For reference, the International Monetary Fund (IMF) projected a 4.5% GDP growth rate for China in 2025 (this forecast, however, did not factor in the possible effects of earlier or potential future fiscal stimulus packages announced by the Chinese government).

HSI forecast for 2025

Review of FY24：The index finally breaks its trend thanks to favorable policies from China

As of November 29, 2024, the Hang Seng Index (HSI) has demonstrated a robust year-to-date increase of 22.3%, positioning it among the leading markets in the Asia-Pacific region (measured in U.S. dollars). Notably, the trajectory of the index this year has diverged from trends observed over the past four years, as it not only reached its intra-year peak in the first quarter but also recorded significant highs of 19,706 points on May 20 and 23,242 points on October 7. However, following these peaks, the index began to weaken under the influence of a myriad of adverse factors, including policy support falling short of expectations, a potential reduction in the number of interest rate cuts by the U.S. next year, and escalating geopolitical risks.

The China-U.S. relationship as the foremost risk factor for 2025

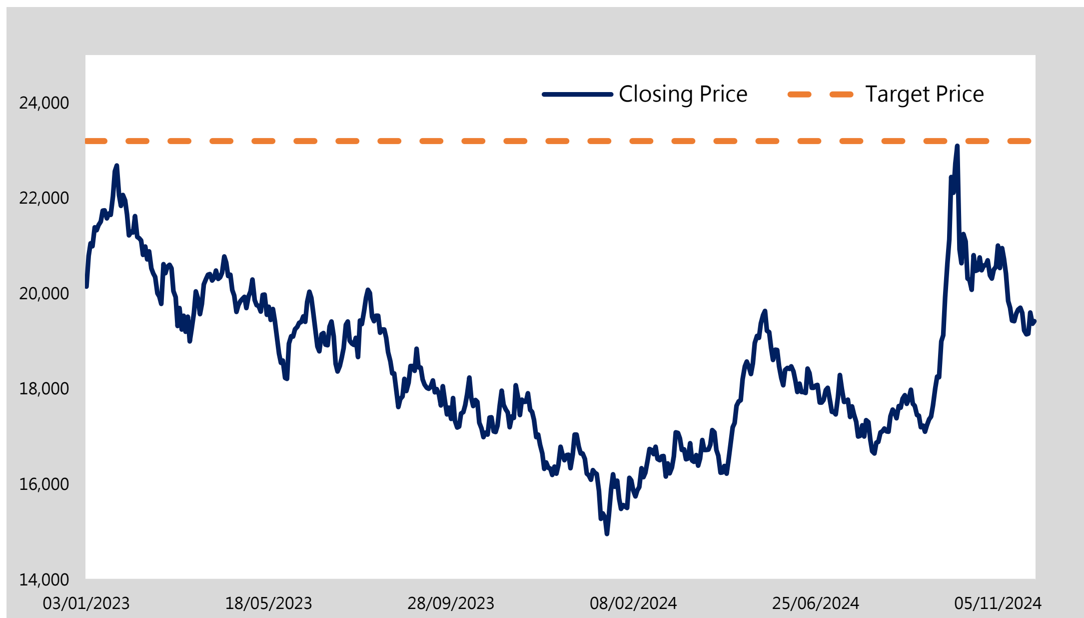
Looking ahead to 2025, the primary uncertainty for the Hong Kong and China markets is anticipated to stem from a resurgence of the China-U.S. trade war. Should the U.S. impose tariffs of up to 60% on imported goods from China, this would effectively signal a hard decoupling of China and the U.S., potentially leading to a low-to-mid-single-digit decline in Chinese exports in the first year. In response, it is anticipated that the Chinese government may shift its focus to stimulating domestic consumption to mitigate the economic impacts arising from the downturn in exports. We believe that the HSI will be significantly volatile next year.

Target price for the HSI in 2025: 23,200 points

While the China-U.S. relationship is poised to be the primary risk factor for the Hong Kong stock market in 2025, from an optimistic perspective, the declaration by President Trump regarding a potential 60% tariff on Chinese imports may serve as a part of bargaining strategy, leaving the final tariff rates and their scope uncertain. Additionally, considering that the Ministry of Finance has indicated that further economic stimulus measures are yet to be introduced, our outlook for the market remains cautiously positive. Considering the unusually exuberant market sentiment during the HSI's recent decline from the peak, when daily trading turnover exceeded HK$600bn at once, we believe that the index has the potential to return to the 23,200 points in 2025. In terms of market valuation, the market forecasts EPS of HK$2,210 for 2025, reflecting a YoY growth of 5.1%. Thus, the forwarded P/E corresponding to the 23,200-point level would be 10.50x, slightly above the 10-year average of 10.26x. Should the index close at 19,700 points by year-end, this would indicate a potential upside of approximately 17.8%.

This scenario is based on the following key assumptions: (i) the scale of economic stimulus measures aligns with expectations and focuses on private consumption, (ii) EPS growth for the HSI maintains >5%, and (iii) the China-U.S. conflict is confined to trade-related issues only.

Graph 2: Hang Seng Index



Source: Bloomberg, Prepared by KGI, As of 29 November 2024

3 Investment themes for 2025

Theme 1: Benefiting from new policies

The Chinese government is currently actively nurturing the capital market. Since September, the PBOC has introduced structural monetary policy tools that allow eligible financial institutions to use less-liquid assets as collateral in exchange for highly liquid assets such as treasury bonds and central bank bills. Through this tool, they can secure funds for investment in the stock market. These initiatives aim to stabilize the stock market and enhance investor confidence, particularly benefiting the relatively undervalued Hong Kong and A-share markets.

China Merchants Bank (3968): Although CMB recorded an annual decline in both net interest income and non-interest income during the first three quarters, its wealth management income continues to show improvement. The number of Golden Sunflower and above clients reached 5.0657 million, reflecting a 9.16% increase compared to the end of the previous year. The Company's balance of AUM of these clients amounted to RMB11.7 trillion, marking an 8.15% growth from the end of last year. Additionally, the number of private banking clients increased by 7.22% compared to the end of the previous year. When customer investment sentiment strengthens, China Merchants Bank's leading position in wealth management positions it well to benefit from an increase in risk appetite among mainland citizens.

Ping An Insurance (2318): Ping An Insurance reported revenues of RMB861.81bn in 9M24, reflecting an 8.7% YoY increase. The company's three core businesses, namely life and health insurance, property and casualty insurance, and banking, continued to show stable growth. The new business value (NBV) for life and health insurance reached RMB35.16bn, up 34.1% YoY. The increase in both the number of agents and per capita productivity indicates a growing momentum for its core business. Overall, the quarterly results exceeded expectations, indicating improvement in the profitability of life insurance. Additionally, factors such as the improvement in the mainland real estate and A-share markets are favorable for its prospects.

Theme 2: Low geopolitical sensitivity

With Donald Trump re-entering the political arena, investor attention is shifting back to U.S.-China relations. At the same time, Trump's cabinet picks signal tough stance on China, prompting markets to reassess potential changes in the business environment of China, particularly regarding tariffs and restrictions on China's technological development. Investors may consider companies with a more domestic focus to mitigate geopolitical risks.

China State Construction (3311): The Group has continued to promote the application of MiC technology in the mainland market in recent years. At the same time, it has a leading position in the construction market of Hong Kong and Macao, so it can benefit from the development of the northern metropolitan area of Hong Kong. The management has clear guidance for the future, including increasing its dividend payout ratio from "approximately 30%" to "not less than 30%" in 2024, with more than double-digit growth in net profit margin, and newly signed contracts reaching HK$210 billion. Looking forward, operating cash flow will continue to improve, and the dividend payout ratio may also gradually increase. Overall, the prospect visibility is high.

Tencent (700): In 3Q24, Tencent benefited from game-driven growth, including titles such as "Valorant," "Honor of Kings," "Peacekeeper Elite," and "Dungeon & Fighter: Origin." At the same time, advertising revenue beat expectations. Looking ahead to 2025, Tencent has a rich pipeline of games, and its advertising monetization capabilities are also promising.

China Mobile (941): As capital expenditure gradually decreases, it is expected that the annual free cash flow will achieve good growth. The company values shareholder returns and has committed to increasing the dividend payout ratio to 75% over the next three years starting from 2024. China Mobile has high growth visibility and attractive dividends, and the industry is highly defensive, making it suitable for income generation.

Theme 3: Actively expanding business overseas

Despite growing at a faster pace than developed countries, China's economic growth has slowed compared to its previous rapid expansion. Many Chinese companies are actively seeking new overseas opportunities to expand their business footprint and sustain profit growth.

Trip.com (9961): Over the years, Trip.com has expanded its footprint through both organic growth and acquisitions, managing a diverse portfolio of brands, including Ctrip, Qunar, Trip.com, and Skyscanner. Currently, it stands as the leading one-stop travel platform in China and has gained significant recognition globally. With the increase in international flight availability and relaxed visa rules, its overseas operations are poised to benefit from a rebound in market demand. Additionally, there is a notable shift in the travel preferences of Chinese tourists, particularly among the younger generation, who increasingly favor customized travel experience. This explains the growing reliance on online travel agencies (OTAs) for travel planning and bookings.

BYD (1211): In 3Q24, BYD reported revenues and profits of RMB201.12bn and RMB11.6bn respectively, representing YoY increases of 24% and 11.5%. The GPM improved by 3.2 ppts sequentially to 21.89%, driven by economies of scale and increased sales contributions from models equipped with DM5.0 technology, which lead to higher average selling prices and per-unit profits. As of now, BYD's NEV have entered multiple countries, including Brazil and Thailand. As a global leader in NEV, BYD's overseas sales volume reached 329,073 units in 10M24, grew by nearly 90%.

Table 1：Top Picks

Name	Target Price
Benefiting from new policies	
CMB (3968)	43.0
PAI (2318)	57.5
Low geopolitical sensitivity	
CSCI (3311)	11.9
Tencent (700)	507.0
China Mobile (941)	80.9
Actively expanding business overseas	
Trip.com (9961)	625.3
BYD (1211)	319.1

Taiwan market

We are optimistic that Taiwan's stock market in 2025 will continue the bullish trend observed in 2023 and 2024. This optimism is primarily based on the steady global economic expansion and the AI arms race, which is expected to sustain strong momentum in technology stock earnings. Additionally, active participation by domestic investors in Taiwan's stock market and interest rate cuts by the Federal Reserve are likely to ease the pressure of international capital outflows, further enhancing market risk appetite.

Given that generative AI is gradually being integrated into more end-user applications, leading global cloud service providers are expected to continue expanding their AI investments in 2025. This will drive the AI server market to maintain its high growth momentum and support a 23% earnings growth for Taiwan's tech stocks in 2025, following a 35% increase in 2024. Besides the AI boom benefiting tech stocks, non-tech stocks are expected to gain from the stabilization of China's economy, with an anticipated earnings growth of about 5% in 2025. Overall, we estimate that Taiwan's stock market will see an overall earnings growth of 18% in 2025, following a 36% increase in 2024.

While we remain optimistic about the continuation of the bullish trend in Taiwan's stock market in 2025, the annual gains may not surpass the impressive performances of the past two years. The current AI-driven surge has already resulted in a significant increase of over 90% for the Taiex, with the forward price-to-earnings ratio reaching as high as 21 times. Compared to previous bull markets driven by technological paradigm shifts, the current gains and valuations are approaching historical peaks. Following a 28% increase in 2023, Taiwan's stock market has once risen nearly by 30% in 2024.

We expect Taiwan's stock market in 2025 to generally follow a U-shaped trend, with a bullish bias in the first and fourth quarters and potential corrections in the second and third quarters. In particular, Trump's entry into the White House could increase market volatility due to his aggressive economic and trade policies.

Singapore market

Opportunities and challenges coexist

In 2024, Singapore is capitalizing on the global wave of artificial intelligence, which is driving up demand for semiconductors and related electronic components, fueling notable growth in its electronics and machinery manufacturing sectors. The financial services industry, especially wealth management, is thriving, bolstered by rising risk asset prices. Robust demand for housing has spurred a steady recovery in construction activity, while the increase in MICE (Meetings, Incentives, Conferences, and Exhibitions) events has reinforced tourism, making it a strong contributor to economic growth.

Looking ahead to 2025, significant changes are anticipated in the global macroeconomic landscape, with the U.S. expected to overhaul key policies related to international trade, foreign affairs, immigration, and more under Trump's administration. Rising

tensions among major economies are likely, yet Singapore, with its strategic position as a trade, logistics, and wealth hub, is well-positioned to navigate these shifts. Since the onset of the trade war in 2017, Singapore has leveraged its strengths and geographical advantages, achieving consistent growth. As we move into the coming year, Singapore is poised to face both new challenges and fresh opportunities.

Economy overview

GDP: In the first three quarters of 2024, Singapore's GDP growth significantly outpaced the same period in 2023, driven by robust manufacturing output, especially in electronics, and a thriving modern services sector. Economic growth is bolstered by steady expansion in key trading partners as global interest rates ease with moderating inflation. However, with Donald Trump re-elected as U.S. president, tensions between the U.S. and China are expected to escalate, potentially impacting Singapore's growth through tariff policies and shifting manufacturing to Southeast Asia. Near-term growth is supported by an upswing in electronics, trade cycles, and favourable financial conditions, with the Monetary Authority of Singapore (MAS) projecting 2024 GDP growth at 2.0% to 3.0%. In 2025, GDP is anticipated to reach S$548.15 billion, with per capita income at S$93,956.

CPI: MAS expects core inflation momentum to remain contained in Q4, which would imply a further slowing in its YoY rate over the next few months. Core inflation is expected to be around 2% by the end of the year, and average between 2.5%–3.0% for full 2024, down from 4.2% in 2023. In 2025, both CPI-All Items inflation and MAS Core Inflation are forecast at 2.0% in 2025.

Labour market: While overall hiring plans have softened, employment growth is expected in manufacturing and services, supported by improved business confidence. The Ministry of Manpower anticipates a tight labour market, aided by festive season hiring and an optimistic GDP forecast. Further income growth is expected in 2025 as economic conditions improve and interest rates fall, narrowing the nominal-real income gap.

Fixed asset investment: In the first half of 2024, Singapore attracted S$5.4 billion in Fixed Asset Investment (FAI) commitments, keeping the Economic Development Board (EDB) on track to meet its annual target of S$8–10 billion. This follows S$12.7 billion in investments in 2023 and a record S$22.5 billion in 2022, largely driven by semiconductor growth. The EDB now seeks to stabilize FAIs at S$8–10 billion annually, with Total Business Expenditure (TBE) between S$5–7 billion and the creation of 16,000–18,000 jobs. By 2025, investment levels may become steadier amid clearer economic conditions following global elections and potential interest rate cuts.

International trade: In September 2024, Singapore's total trade rose 0.5% year-on-year, with exports up by 0.1% and imports by 0.9%. Non-oil domestic exports (NODX) grew by 2.7%, continuing August's strong performance, and reached S$14.9 billion, though below July's peak of S$15.4 billion. Electronics and non-electronics exports both saw gains, with notable NODX growth to the EU 27, Indonesia, and South Korea. Non-oil re-exports (NORX) grew 3.4%, driven by electronic NORX, despite declines in non-electronic re-exports. However, China's ongoing slow economic recovery, alongside potential higher U.S. tariffs, is expected to keep Singapore's trade growth in the single digits through 2025.

Personal disposable income and savings: Personal income growth in 2024 is likely to remain subdued as companies cut jobs and freeze hiring amid economic uncertainties. However, expected U.S. interest rate cuts could improve hiring levels and boost disposable income in 2025.

Housing and rental prices: Year-to-date, private housing prices rose by 1.6%, a moderation compared to the 3.9% increase seen in the first three quarters of 2023. Meanwhile, private residential rentals rebounded by 0.8% in Q3 after a 0.8% decline in Q2. Rentals for non-landed properties increased by 0.5%, and landed property rentals surged by 3.2%, reflecting renewed demand in the rental market. The supply gap remains as newly launched property units cannot catch up with rising demand.

Asia wealth hub

Singapore is currently home to approximately 336 centi-millionaires (individuals with a net worth of at least US$100mn), ranking 6 globally. Singapore's centi-millionaire growth forecast is ranked 9th for the next 10 years, with a projected growth between 100% - 150%. Singapore also ranks 3rd in terms of net inflow of HNWIs, behind UAE and the U.S., with an expected 3,500 HWNI relocating to Singapore in 2024.

Favourable sectors

Banking: Robust profitability, low valuation, and attractive dividend yields.

Real estate investment trust: Upward re-rating amidst the rate cut cycle, and high dividend yields.

Palm oil: Continued depressed palm oil production in Indonesia and Malaysia.

Indonesia market

Catalysts for aiming higher economic growth in 2025

For 2025, we are targeting enhanced economic growth, projecting a 5.5% annual GDP increase, surpassing the 10-year average of 5.1%. This growth will be driven by increased consumption and investment, a rise in civil servant salaries, infrastructure development in the Nusantara Capital City (IKN), and downstream exports, contingent on robust global commodity prices.

The banking industry should play a pivotal role in 2025 by expanding credit distribution to the micro, small, and medium enterprise (MSME) sector. We remain optimistic, as Indonesian fiscal policy has effectively rebounded the economy post-COVID-19 pandemic. Despite upcoming challenges, we anticipate significant improvements in consumer confidence and domestic demand.

Challenges ahead for Indonesia

Strengthening the capital market as a primary funding source for the non-bank financial sector is crucial for enhancing the resilience of the domestic economy and achieving the 5.5% growth target. Currently, capital market investors are predominantly concentrated on the island of Java, where Jakarta is located. To address this, the government needs to increase capital market literacy and broaden the investor base to other islands, such as Kalimantan, Sulawesi, and Sumatera.

One of Indonesia’s significant challenges is the development gap between Java and other islands like Sumatera, Kalimantan, and Sulawesi. The disparity in basic infrastructure and public services between urban and rural areas, especially outside Java, is evident.

Additionally, there are substantial restrictions on foreign participation in the services sector, which should be relaxed. For instance, legal services could benefit from foreign expertise, which does not necessarily need to be sourced domestically.

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