

DEAR INVESTOR,

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FUND MANAGER'S LETTER
DECEMBER 1ST WEEK, 2022

Equity

Will there be a December Rally in stocks?

Large number of investors are expecting the index will perform well at the end of the year. This is correlated with the fact that in the past 10 years, December has been very kind to Indonesian stock market. JCI Index was up on average +3.01% in December for the past 10 years. December was also the month with the highest average increase in a year. Even during US recessionary periods, December consistently booked high positive results during the past 15 years for JCI Index. We see a slightly different results for US stock markets which in some years December recorded negative results and generally continued to January.

As any other phenomenon in the stock market, to act on certain phenomenon we, in Avram, need to understand the underlying reason of the phenomenon in the first place and take it with a grain of salt.

December rally is first well-known in US market as the Santa Clause Rally. Investopedia defined the Santa Clause rally as a sustained increase in the stock market that occurs in the week leading up to December 25 and could continue until January 2.

Theories that support Santa Claus rally including increased holiday shopping, optimism derived from seasonal spirit, and institutional investors try to settle their position before going on vacation. Whilst, many try to connect the December rally in Indonesian stocks to the window dressing phenomenon. It happens when portfolio manager sells stocks with large losses and purchases high-flying stocks near the end of the quarter or the year and include the new bought stocks into the fund's holdings. In Indonesia, this phenomenon is deemed not only causing the December rally but also continued to January and caused the January Effect. Stocks with big market capitalization were the ones that normally moved the markets during this period.

As investors, it will make our life easier if this phenomenon is a constant and we can follow the strategy blindly. Unfortunately, similar to any other phenomenon, we need to dig deep into the root cause of the phenomenon and ensure whether the causes are still valid or not, specifically in Indonesia case. I think window dressing assumptions for the cause of December rally is something logical and addressed to the FOMO part of the investors. Yet, for the December rally to become reality this year, I would need more than just the expectation that others will repeat their actions this year and aggressively buy big-caps to push the index higher. It means we are back to catalyst and risk that are in the markets.

From US, declining rate of US inflation could provide a catalyst for the markets.

US Core PCE inflation in October which showed increase of 4.98% YoY or consistently below its highest reading of 5.4% in February supported market's expectation that the Fed will start to temper down its tightening move. Other inflation indicators like US CPI YoY and Core CPI YoY which are also in declining trend aid to this argument. Encouraging US Inflation report data on December 13 could give rationale for a year-end rally.

From global, China's latest move to relax their strict Covid rules are considered to be one of big catalyst for the markets. China's economic reopening is expected to drive up China domestic consumption and support the global economic growth.

Dollar index declined to 105 and broke MA 200 level is seen to be supportive for Emerging Markets which benefited from weak US Dollar. Yet, from domestic side, the deteriorating price one of big tech companies in Indonesia limit the upside for the index to rally this end of year.

Overall, we maintain our defensive stance on our portfolio and like good quality companies that have pricing power during this inflationary environment. While, we are on the lookout for opportunity to enter more cyclical names when the markets conditions approve us to do so.

Fixed Income

The US Federal Reserve may scale back the pace of its interest rate hikes in December, Fed Chairman Jerome Powell said on Wednesday in a speech at the Brookings Institution. "It makes sense to moderate the pace of our rate increases as we approach the level of restraint that will be sufficient to bring inflation down. The time for moderating the pace of rate increases may come as soon as the December meeting". Still, Powell added that "terminal rate," is likely to be "somewhat higher" than the 4.6% indicated by in the September projections. Powell suggested that it may be appropriate to slow the pace of interest rate increases as soft economic data hinted that its aggressive policy is taking effect on the economy.

The Federal Reserve raised the target range for the federal funds rate by 75bps to 3.75%-4% during its November 2022 meeting, marking a sixth consecutive rate hike and the fourth straight three-quarter point increase, pushing borrowing costs to a new high since 2008.

The yield on the US 10-year Treasury note consolidated around 3.6%, a level not seen since September, as the narrative started to change from inflation and tightening to slowing growth and a policy pivot.

The yield rose above the 3.6% last Friday, mark from the two-month low of 3.5% on December 1st, as a stronger-than-expected US jobs report added to Federal Reserve's leeway to continue tightening monetary policy. The US economy added a net 263 thousand jobs during November, well above market forecasts of 200 thousand and showing further evidence that the labor market remains tight. On top of that, average hourly earnings surpassed expectations and grew 0.6% on the month, adding to the central bank's room to fight inflation.

From domestic, Indonesia's annual inflation rate fell to a three-month low of 5.42% in November of 2022 from October's of 5.71%, the inflation number is below market consensus of 5.5%.

However, the inflation rate was still above the upper limit of the BI's 2-4% target for the sixth straight month. Indonesia's trade surplus on the other hand, edged down to USD 5.67 billion in October of 2022 from USD 5.74 billion in the same month of the previous year, beating market expectations of a surplus of USD 4.5 billion. During the first ten months of the year, the trade surplus widened sharply to USD 45.52 billion from USD 30.90 billion in the corresponding period in 2021.

Foreign exchange reserves in Indonesia marginally decreased to USD 130.2 billion in October of 2022, following USD 130.8 billion in the previous month, the lowest amount since May 2020, which was mainly influenced by the payment of the government's external debt.

The official reserve assets were equivalent to 5.6 months of imports and servicing government's external debt and remained adequate, supported by the stabilized and solid domestic economic outlook.

Global indicators showed supportive sentiment toward lower SUN yields. The UST 5-year yield curve fell 21bps from the end of the previous week to 3.65%, while the US 10-year yield curve registered a 19bps decline to 3.49%. From the risk perspective, Indonesia's 5-year CDS recorded a 9bps decline.

This downtrend in CDS indicates that investors' risk averseness is dissipating. Based on the Rupiah Value Stability Indicator Development report by Bank Indonesia, transaction data for 28 November – 1 December 2022 shows a net-buy by foreign investors of IDR9.64 trillion consisting of IDR8.76 trillion net buys in the SBN market and IDR0.88 trillion net buys in the stock market. Transaction data Monday-Thursday in the previous week showed that foreign investors recorded a net buy of IDR 11.71 trillion. The Rupiah recorded an appreciation of 1.58% against the US Dollar on a week-on-week basis.



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