

HSBC Global Private Banking – QIO Q3 2023 View**Willem Sels**

Following a very challenging 2022, global equity markets have rebounded and already retraced about 50% of last year's fall, while bonds markets have also performed well. So, it has paid, so far, not to sit on too much cash.

Now, what has been driving this market rebound? First and foremost, the fall in US inflation – the big bugbear in 2022 – and the good news is that inflation will continue to come down. That has already allowed some central banks to end their rate hikes, and the others should stop soon. Earnings have also been more resilient than people feared because companies have skilfully protected their margins. Tech has outperformed because of that earnings power, lots of exciting innovation and the imminent end of the rate hikes. And sustainable investing, which tends to overweight growth-style and quality stocks and under-allocate to oil and gas, is enjoying these biases now, because they are working in its favour.

Now, the bears will argue that there are some major risks ahead. Developed market growth is slowing, banks are tightening their lending standards and markets are worried about commercial real estate. But banks are generally well-capitalised and loan delinquencies are low, so we do not foresee a systemic crisis. As for real estate, delinquencies tend to take time to materialise, so we see this as a slow burn rather than a wildfire. So, while these are valid downside risks, a US recession is not a done deal, and the negatives are balanced by several other key factors. Falling inflation gives consumers more breathing space, and labour markets remain strong, so consumption which is the largest part of GDP, should remain healthy. Peak interest rates are another positive. And while the West is slowing, Asia's rebound comes to the rescue. So, the picture is much more balanced than some fear – and G7 economies should see slow but still positive economic growth. And the good news is that current earnings estimates already factor in that economic picture.

So, let's talk about Asia, because we look Eastwards to look upwards, both in terms of the Asian economy and Asian stock and bond markets. China's reopening is boosting consumer spending and services, and the data have so far have actually surprised to the upside. This should continue and translate into better earnings and market performance, because beyond the reopening, China's renewed focus on growth should stabilise activity in the property sector, and boost areas related to self-sufficiency and the net-zero transition. Meanwhile India is benefiting from strong investor interest, rising wealth and the upswing in global tech.

Now to think about the global investment environment in a more intuitive way, we identify 6 key forces. First, the economic cycles are unsynchronised, as we have discussed with Asia in an upswing, while the west is slowing. More structurally, we are moving to a world with more strategic competition, lots of disruptive technology and societal changes. And as we are falling behind on the path to net zero, the urgency of that mission becomes even more urgent every day.

So what does this mean for investors? The unsynchronised cycle favours Asia, while peak rates help bonds. The cyclical divergence and our multi-polar world argue for continued USD weakness. And peak rates combine with technological disruption and societal changes to support our positive view on technology. Finally, the complex world we live in and the cyclical uncertainties highlight the importance of diversification and the potential for volatility trades. So, we adopt a mild risk-on tone, with an underweight in cash, an overweight in quality bonds, a neutral stance on equities with a preference for Asia and the US, and an overweight in hedge funds.

But these 6 key forces also drive our investment themes and our four Top Trends. Now, there is an interesting video by Fan Cheuk Wan, our Asia CIO, that discusses our Asian themes in detail. Under our second trend, we focus on companies with resilient earnings, which also points to opportunities in

infrastructure. And we look for income in quality bonds and on dividend stocks. The digital transformation benefits from a structural tailwind, but also from short term support due to peak in interest rates and rapid innovation in areas like AI and automation. Sustainable investing remains key for us, both in the core portfolio and in the satellite themes. Governments are providing huge support to companies in this space because they see it as an area where they want to capture market share.

So, to conclude, what are our main priorities? First, to capture Asia's upturn, both in credit and equity markets, in consumer-related activities as well as priority sectors. Secondly, as markets like to anticipate and inflation continues to come down, bond yields could drop at any point and we want to lock them in ahead of this move. Thirdly, the volatility and dislocations that we are seeing present many opportunities for active strategies, diversified portfolios, volatility strategies and hedge funds. And lastly, we think there remains strong short-term and long-term potential in those tech companies with strong proven earnings, as they will make their corporate clients more profitable, and all of our lives more interesting.