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Video Transcript

HSBC Investment Outlook – Q2 2024 (Issued 14 March 2024)
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We've been putting our cash to work and continue to do so. The prospect of US rate cuts starting in June is a clear positive for portfolios. Secondly, it has become increasingly clear that the US economy will not go into recession as it continues to surprise on the upside.

Earnings prospects have also improved as companies benefit from resilient demand whilst cost pressures are easing. So the fundamentals are positive and present a fertile ground for investment returns. In fact, some of the positives are not just cyclical in nature, but structural forces, many of which we already tap into through our investment themes.

For example, in our data-led economy, disruptive technologies have been boosting innovation and productivity for a while. Generative AI should further accelerate this across sectors well beyond the small number of companies that are currently benefiting. Climate action is another trend that is here to stay and requires huge investment in infrastructure.

And as societies age, healthcare services are becoming even more crucial with innovation again being enabled by technological disruption. Our new sports and entertainment theme is at the intersection of changing consumer preferences and innovation in virtual reality. And finally, a new world order is reshaping Asia's supply chains, which also creates a wave of re-industrialisation in North America. So how can we build portfolios that tap into the opportunities created by these cyclical and structural forces? We start by casting a wide net, because we think that there are opportunities in bonds and in stocks, both of which we overweight. We also include alternatives, with clear opportunities in private markets and infrastructure.

But of course, relative valuations and relative fundamentals make us selective. So we continue to prefer US stocks over those in Europe, in spite of the valuation differences, because of much more resilient growth in the US, more US innovation, and higher tail risks in Europe. And for similar reasons, we also believe the US dollar will continue to see mild strength against the Euro and sterling. Our second very conscious choice is to emphasise quality first, and we don't necessarily go for the cheapest option. For stocks, this means a focus on companies with solid earnings power and generally a preference for large cap over small caps.

And for bonds, it means a continued preference for investment grade over high yield. And in financials, the potential for commercial real estate related losses points us to senior financial bonds and away from US regional bank stocks towards the large caps. So while our stance has turned more risk-on since we published our 2024 outlook, we have only made small tweaks to our four key investment priorities.

First, we extend bond duration because of policy easing. Bonds have been volatile so far this year, but they have become more realistic about rate cuts and are now closely aligned with our own rate expectations. We continue to believe that inflation will gradually come down, so we want to lock in the current high bond yields. And we ensure that we have sufficient duration to allow us to benefit from the price gains as those yields come down.

Secondly, we continue to broaden US equity exposure to benefit from the soft landing. The US presidential elections are still some time away and as the outcome may depend on just a handful of states, we instead focus on the solid US fundamentals. We continue to like the tech sector, but acknowledge that many investors will want to lower their average valuations by including other sectors as well. And in fact, we like industrials, consumer discretionary, communication services, financials and healthcare, as well as our themes called 'American Resilience' and 'North American Re-industrialisation'.

Thirdly, we hedge tail risks via alternatives, multi-asset and volatility strategies. Bonds and equities are currently more highly correlated than usual, so we need more active diversification, by including alternatives. Generating a solid income stream can also help stabilise returns, and we like to do this by finding different sources of income.

So in addition to bonds, we include private credit where possible, which is often floating-rate, or infrastructure, which is often linked to inflation. And lastly, we continue to diversify our Asian exposure. The good news is that China's support measures should limit the downside for equities there, but markets may need to see these measures translate into higher earnings growth before we see sustained stock market upside. So in the interim, we continue to diversify within Asia, and there are many opportunities.

We have been highlighting India, Indonesia and South Korea for a while, and during the first quarter we added Japan to that list, because corporate governance is rapidly improving there and Japan is well-placed to benefit from the growth in AI, digitalisation and automation. So yes, there is a fertile ground for investment returns, in many areas.

Our investment approach remains selective but actively diversified to manage volatility and risks while benefiting from the very rich opportunity set.