News Release

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HSBC Private Banking Mid-Year 2017 Investment Outlook: Synchronised Growth, Feeble Dollar

Entering the second half of 2017, HSBC Private Banking believes that synchronised global growth, earnings improvement, a weaker US dollar and gradual tightening of the Federal Reserve would continue to support riskier assets. Constructive cyclical drivers are expected to outweigh political tail risks. In anticipation of a sustained and broadening global economic recovery and weakening of the US dollar, HSBC Private Banking stays overweight equities, riskier credit and alternatives and underweight government bonds under a risk-on investment strategy. It maintains overweight allocation to US and emerging market equities, USD credit and emerging market hard currency and local currency bonds. Within Asian equities, it holds an overweight view on China, India and Singapore. It manages geopolitical tail risks through global diversification and overweight in alternatives and gold.

HSBC Private Banking highlights five positive factors in support for riskier assets in the second half of 2017:

(1) Almost all OECD leading indicators are pointing upwards, with a strong upward move in Europe, Russia and Brazil. HSBC economists forecast positive economic growth in 2017 for all countries under their coverage and expect global GDP growth to accelerate to 2.7% in 2017 and 2.8% in 2018 from 2.3% in 2016. China GDP growth is projected to sustain at 6.7% in 2017 and 2018.
(2) Earnings expectations are drifting up in all regions of the developed and emerging markets, and analysts have upgraded far more of their price forecasts than they have downgraded after the first quarter earnings season.
(3) Monetary policy: Although economic data continues to improve, inflation pressure remains subdued, causing the Federal Reserve to adopt a very gradual approach in tightening interest rates and unwind its balance sheet.
(4) China's growth stabilisation, recovery of commodity prices, improved global demand outlook and a weak US dollar are all positive for emerging market equities and bonds. Structural reforms and growth supportive policies should boost growth prospects in Emerging Asia and Latin America.
(5) European cohesion: One of the most important tail risks has been drastically reduced as a result of the election of Mr Emmanuel Macron to be the French President, supporting recovery of global risk appetite.

HSBC Private Banking's Mid-Year Investment Outlook highlights four investment themes that will move the market's direction and shape its investment strategy for the remainder of 2017.

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(1) Synchronised global growth

Latest leading indicators suggest that global economic growth will continue and broaden in the next 12 months. In fact, this is the most synchronised global recovery since the end of the global financial crisis in 2008, and this should make the recovery more sustainable as well.

"Analysts had been particularly cautious on emerging markets and Europe until recent months, but the synchronised recovery now forces them to make a U-turn, causing quick earnings upgrades in these regions," said Cheuk Wan Fan, Head of Investment Strategy and Advisory, Asia at HSBC Private Banking. "If investors grow confident that the expansion will become more durable, we think that even valuation multiples may increase somewhat further from the current levels," said Fan.

HSBC Private Banking continues to see multiple tail risks from geopolitical uncertainty, but policy makers have provided safety nets: central banks' accommodative policies reduce the potential for financial contagion, and they should continue to be generous if the economic outlook were to deteriorate. In China, credit growth is being managed carefully to avoid either a bubble growing, or a bubble bursting.

(2) Mining for income

One fundamental need for most private investors is the quest for income. HSBC economists expect the Federal Reserve to raise interest rates by 25 basis points again in December after the widely expected hike on 14 June. But even after a total of three rate hikes in 2017, Fed funds rate will only rise to 1.50% which remains at historically low level and still below the inflation level.

"At the end of 2017, HSBC expects 10-year US Treasury yield to come down to 1.90% due to structurally low global productivity and inflation, coupled with continued ample global central bank liquidity in search for yield," said Fan.

HSBC Private Banking sees attractive carry in emerging market hard currency and local currency bonds, global mining and energy credit and USD high yield credit. The bank also finds high dividend stocks and share buybacks as interesting alternative to the bond market for investors looking for income.

(3) China: Innovation and global integration

At a time of lingering global concerns about trade protectionism, China strategically strives to build a new sustainable growth model through technological innovation and global integration. HSBC Private Banking favours China's New Economy stocks in the IT, healthcare, new energy, media, financial services, outbound travel, education services and consumer discretionary sectors, as they are expected to benefit from supportive government policies to promote economic rebalancing towards the services and consumption sectors.

"Technological innovation is driving China's transformation from the 'world's factory' to the 'world's innovator'. With 731 million internet users, China is the world's number one digital market with strong growth potential," said Fan.

At the Belt and Road Forum in May, China outlined plans to invest over USD 800bn in the next five years to finance infrastructure projects under the Belt and Road initiative (BRI) in order to stimulate investment and trade along the New Silk Road.

China's ambitious BRI is expected to improve infrastructure connectivity for 63% of the world's population and 30% of global GDP. HSBC Private Banking sees opportunities in China's infrastructure, railway construction, building materials and construction machinery companies. Other potential beneficiaries include Asian infrastructure companies and financial institutions with large exposures to the Belt and Road projects and emerging market commodities producers which will gain from rising Chinese infrastructure investment.

China's accelerating capital market reforms will drive continued integration of its equity, bond and currency markets with the global financial markets. HSBC Private Banking believes the likelihood of the inclusion of A-shares in the MSCI has increased on the basis of the Stock Connect market access framework. China is planning to launch the China-Hong Kong Bond Connect before the end of 2017. In anticipation of likely inclusion of Chinese onshore bonds in the global indexes, HSBC expects foreign ownership in the Chinese onshore government bond market to expand from around 2% today to 10% in the next two years. Potential beneficiaries of China's capital market reforms include stock exchange, insurers and brokers. It expects rising Chinese demand for overseas asset diversification would drive sustained robust southbound inflows into the Hong Kong market, offering a positive liquidity driver for Hong-Kong listed Chinese shares and Hong Kong blue chip stocks.

(4) Industrial Revolution 4.0

Following the earlier Industrial Revolutions of the Steam Engine (1.0), Mass-Production with Assembly Lines (2.0), and Factory Automation (3.0), the Industrial Revolution 4.0 (IR 4.0) is now in full swing. Like its predecessors, HSBC Private Banking expects the IR 4.0 to create substantial productivity gains and support global economic growth. Aside from the utilisation of Big Data and Artificial Intelligence (AI), the IR 4.0 combines automation with remotely-connected computer systems and machine learning algorithms (artificial intelligence).

Clearly, IR 4.0 has many broader economic and social consequences. For many companies, it creates the potential to raise productivity, control costs and grow margins.

"To capture structural growth opportunities from the rapid development of new world technology, we favour industry leaders focused on Big Data, AI, cloud computing, robotics and system security. Higher productivity may benefit margins, but not wages, in our view. As automation could cause job growth to slow, it is possible that inflation as well as interest rates could thus stay low for even longer," added Fan.

Investors should note that investments in the emerging markets may be extremely volatile and subject to sudden fluctuations of varying magnitude due to a wide range of direct and indirect influences. Such characteristics can lead to considerable losses being incurred by those exposed to such markets. Furthermore, investors should beware of the highly speculative nature of products involving hedge funds. These products are generally intended for experienced and financially sophisticated investors who are willing and able to bear the associated risks.

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