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HSBC IO 2022 Q1

The Big Reset – Willem Sels Video

When we look into 2022 there are a number of things that remain unchanged, some that undergo a gradual transition and a few big structural changes, which we have called the Big Reset.

Looking at continuity first, the good news is that economic growth still remains above normal in the mid-cycle stage and we will also still be in a very low interest rate environment.

And of course, this combination is bullish for equities, where we maintain our overweights in US and Europe whilst we search for carry in the bond markets. But following the rally, we become more selective and position in those areas that are best suited to the changes that we are seeing.

It's clear that a transition in monetary and fiscal policy has already started, and the triggers for this can be found in the pandemic. COVID 19 was not just a health crisis, but also led to supply chain disruptions and adjustments in the labour markets, which have boosted inflation to which central banks are now starting to react.

The pandemic also led to increased inequality and record government spending, which is now requiring some changes in fiscal policy. The transition in central bank policies will lead to uncertainty, but should be gradual and led by the Fed. And that, of course, will support the US dollar and also leads us to prefer EM hard currency over local currency bonds. Bond investors will also need to manage duration and because inflation may remain high for a number of months and taxes are rising, we need to pick companies with strong margin power.

But governments will still continue to spend on some priorities, including infrastructure and health care, where we see opportunities. And a final consequence of this transition is more market volatility, which should allow hedge funds to take advantage of relative value opportunities.

Now on to the Big Reset, and of course, the most dramatic reset relates to sustainability, which has seen a leap in interest from investors and has become key to any company's strategy.

The visible triggers for this are increased ESG awareness and activism, the much discussed COP26 meeting dramatic climate change around us, rapid biodiversity loss and the recent spike in energy prices, which has made clean energy even more competitive.



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So portfolios need a big reset on sustainability to integrate ESG opportunities and risks and pick the winners of the sustainability revolution for the long run.

In the thematic space, the energy transition will continue to see very strong government and business investment and innovation, and that will lead to lots of funding activity in the capital markets and opportunities to get income in a sustainable way. And let's not ignore the social aspects of sustainability because more and more investors want to address the increased inequality, in part simply because fair societies and companies typically perform better in the longer term.

A big reset is going on in Asia as well as the region is remaking its future. And one of the triggers is the sustainability revolution that we just talked about, as it will have a huge impact on Asia and is part of China's focus on stability and sustainability of growth. The common prosperity goal can also be seen in this context.

And the US-China relationship and global supply chain disruption are some of the reasons for China's tech self-sufficiency goal and a trend to more regional integration.

Now, for investors, these changes lead to some continued short-term uncertainty, and hence we maintain our neutral stance on Chinese equities and hard currency bonds for now. But at current valuations, we see good opportunities when we align ourselves with those structural trends and policy priorities, including China's Green Revolution and the next generation Asian tech leaders.

Wealth and disposable income growth across Asia remain considerable, and we therefore expect to see a real consumer revival.

Now it won't come as a surprise that our last element of the Big Reset is going back to the enabler of a lot of innovation, namely the Digital Transformation. And when we look around us, recent triggers of this reset include a much increased digital use and literacy that was forced upon us during the lockdown, and digital access is now much broader due to new work patterns.

Data continue to multiply and AI and increased computer power enable new innovations. And on the medical front, genome technology opens new opportunities for treatment, while global collaboration on vaccine development during the pandemic creates the hope of more international breakthroughs.



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So this revolution creates a number of opportunities for investors relating to data security, but also in automation and AI and smart mobility. Companies' spending on IT and R&D has already picked up, and they are investing some of their considerable cash piles.

And finally, technological innovation intersects with governments' priority to spend on health care and with people's longevity to support our theme of biotech genomics and devices.

So we've gone through the elements of continuity, the policy transition and the areas where we see a Big Reset, and that allows me to summarize our Top Ten Takeaways for 2022.

As the cycle continues and rates remain low, we remain invested with an overweight in US and European stocks while we focus on high yield and emerging market hard currency bonds in fixed income. The transition of central bank and fiscal policies should lead to mild further strength in the US dollar and causes us to be more selective and we focus on areas with strong fundamentals.

Due to the increased volatility we expect, we manage duration in fixed income and overweight hedge funds. And as for the Big Reset, we have discussed three structural trends. Sustainability should be incorporated throughout the portfolio, and investors should not shy away from investing in Asia, especially in areas aligned with the long term policy priorities.

We continue to like many growth stocks linked to the digital transformation. And beyond hedge funds, we also see opportunities in private markets as some interesting companies do not trade in public markets, and a long term approach can be very well adapted to position for the Big Reset.