HSBC Private Banking

Video Transcript

HSBC IO 2021 – Q4 Review
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It's clear that the pace of economic growth is slowing around the world, and in our view, we are entering the mid-cycle stage.

But investors should not be overly concerned about this. Growth naturally slows after a V-shaped recovery.

And we still forecast very respectable growth rates in the U.S., Europe and Asia. The cycle should be extended as consumers will want to spend some of their accumulated savings.

Companies will need to rebuild inventories, and governments are starting large infrastructure projects.

So, in fact, we think that somewhat slower growth will help the Fed to stick to its very gradual policy and to its view that inflation will come down in coming quarters.

Some easing of demand will give the supply side time to catch up and reduce the inflationary bottlenecks.

So we should continue to have a healthy combination of continued growth and only very slow policy normalization, which supports our overweight in equities, high yield and emerging market bonds.
We have a broad based equity overweight across regions, but the U.S. remains our most significant overweight whilst in Asia we take a long term approach focusing on secular growth opportunities.

In fact, the mid-cycle stage has historically been positive for equities as earnings continue to grow, even as valuation multiples come down somewhat. And indeed the recent earnings season has been very strong, causing equity analysts to catch up and upgrade their forecasts.

But the speed of the equity market rally may well slow, and we have reduced our exposure to early cyclicals such as industrials and materials. In the mid-cycle stage it also typically makes sense to start to focus more on quality stocks with strong margin power and business models and to tilt towards large caps.

And in the low yield environment we continue to be in we look at dividend strategies to complement the income we can get from high yield and emerging market bonds. Yield differentials should continue to be a mild positive for the U.S. dollar against the euro.

So we think that somewhat slower, is in fact, relatively good for stocks and bonds.

But what is not ensured is a steady economy or a steady market performance. We think consumption will be solid, but the uncertainty around the Delta variant is bound to lead to some fits and starts and some market volatility.

And the current supply bottlenecks and inflation pressures may also take time to be resolved and therefore continue to create some volatility.

So we put more emphasis on building resilient portfolios, by looking at quality stocks, by managing duration, and by actively looking for diversification.

With so much hinging on the Fed outlook, equity markets are currently highly correlated with bond markets, and hence investors need to look at opportunities across asset classes, regions and within alternative assets to appropriately diversify.

That will be the best way, in our view, to create portfolio performance that is a steady as possible.

I mentioned that a somewhat slower economy is not detrimental to the market environment, but where slow is obviously a very bad idea is in our fight against climate change.

The IPCC report has warned us that the situation is much worse than many expected and that urgent action needs to be taken.

So we expect more concrete initiatives from governments at the COP 26 meeting in Glasgow in November, more regulation, more disclosure from companies and more pressure from consumers and investors.

Governments are likely to invest in both mitigation and adaptation and our investment theme reflects this. And outside of climate change we're also seeing broadening interest in social aspects of ESG.

And we've launched a new investment theme related to this covering diversity and inclusion and the delivery of sustainable health care for the long term.

All of our long term themes including sustainability, the digital transformation and Asia's new growth path, allow investors to be somewhat less sensitive to the short term uncertainties and help create more resilient portfolios.

So in summary, the move to the mid-cycle stage does not signal the end of the economic cycle nor the end to the equity market rally.

So we remain invested in equities High yield and emerging market bonds, but we look more actively for quality as well as opportunities in alternative assets to create resilient portfolios.

As returns are likely to slow somewhat it's even more important o try to ensure that those returns are steady as possible.