

HSBC Investment Outlook – Q2 2025 (Issued 13 March 2025)**Willem Sels, Kevin Lyne-Smith and Emma Cory****WillemSels**

I'm here with Kevin Lyne-Smith and Emma Cory to discuss how key trends are impacting the opportunities in both public and private markets. Kevin, it's fair to say that the development of powerful AI models that are cheaper to operate are going to create a lot of opportunities for AI adopters. Where do you see the main beneficiaries?

Kevin Lyne-Smith

Well, I think everyone benefits from more diverse sources of AI innovation, also greater competition. This should, in theory, lead to greater innovation and more acceleration of developments together with lower costs. But do not forget, not all models suit all tasks, or all applications.

In our Intelligent automation and AI investment theme, we concentrate less on the software models themselves. But focus on the adopters, such as utilities, that are using AI to optimise electricity distribution, and healthcare companies for both drug discovery and smart device development.

Similarly, our American re-industrialisation theme identifies industrial companies that are onshoring production to US factories and using automation, AI and other smart technologies to boost productivity to offset higher labour costs. Altogether, this provides enhanced supply chain security and greater manufacturing flexibility.

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Now all of this will need investment in infrastructure and I imagine mainly around telecom and electricity.

Kevin Lyne-Smith

Indeed, communications services is our favourite sector due to its track record of delivering strong sales and earnings growth, especially in the media and entertainment companies. Clearly, these and other businesses are increasingly dependent on digital infrastructure to deliver their products and services.

In the latest earnings season, several large IT companies identified insufficient data centre capacity as the obstacle that is responsible for their slowing growth. Powering all these technologies requires increasing supplies of reliable energy, which is a topic of our energy transition theme, where companies are turning to wind, solar and nuclear energy generation to secure supplies and assure a degree of independence, whilst at the same time also minimising their carbon footprint.

Willem Sels

I'm glad you mentioned infrastructure Kevin because in the private markets too, we continue to invest in infrastructure. So let me turn to you Emma, around the world, governments are announcing these investments in data centres, in electricity to feed those data centres. So this is all about countries wanting to be leaders in our data led economy and AI, isn't it?

Emma Cory

Yes, definitely, but of course, they welcome private capital as well because the investment required is enormous. And what this can provide for private investors is stable cash flows, exposure to the underlying cloud assets, but also inflation adjusted returns. So this can be attractive for portfolio construction but also to add diversification.

Willem Sels

Couldn't agree more. What else is going on in private markets?

Emma Cory

Well for private equity a number of stars are aligning. You have the resilient economic backdrop and also increased innovation boosting investor confidence in the space. You also have somewhat lower borrowing costs and increased capital markets activity, which should mean more deals coming through.

You also have given the AI opportunities, a lot of private markets participating, and some of these companies could do really well. Some may need to acquire the expertise as well. This should lead to more dry powder being put to work, more deal activity, increasing valuations which should increase private equity returns.

So investors may be interested to look at private equity. But also they can look at private credit. Public credit spreads are tight. In the private credit markets, they are more attractive. Some investors may be concerned in the higher for longer interest rate environment. And defaults are rising, but they still remain low. And this can be mitigated by collateral and appropriate management. And of course as always for alternatives, manager selection is key as the dispersion of returns in this space is very high.

Willem Sels

Thanks, Emma and Kevin. And I think it's interesting to see that both across the public and private markets, we can exploit the strong themes and trends starting, of course, with the disruptive technologies which create opportunities across the whole AI eco-system, which in turn requires a rapid energy transition and creates new business models across sectors.

The US is a strong player in all of this, supporting our American themes and US stock picks, but it's also clear that China has strong capabilities creating domestic leaders and boosting the prospects for returns in the region.