Investment Outlook

Q3 2023

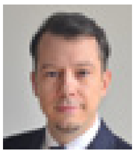
Eastwards and Upwards

HSBC

Global Private Banking

Contributors

Global Chief Investment Officer
Willem Sels
willem.sels@hsbcpb.com
+44 (0)207 860 5258



Head of Asset Allocation
Stanko Milojevic
stanko.milojevic@hsbcpb.com
+44 (0)207 024 6577

Director, Global Market Strategist and Managing Editor
Neha Sahni
neha.sahni@hsbcpb.com
+44 (0)207 024 1341

Regional Chief Investment Officers

Chief Investment Officer, Asia
Cheuk Wan Fan
cheuk.wan.fan@hsbcpb.com
+852 2899 8648

Chief Investment Officer, North Asia
Patrick Ho
patrick.w.w.ho@hsbcpb.com
+852 2899 8691

Chief Investment Officer, Southeast Asia
James Cheo
james.cheo@hsbcpb.com
+65 6658 3885

Chief Investment Officer, China
Desmond Kuang
Desmond.kuang@hsbc.com.cn
+86 21 38881020

Chief Investment Officer, EMEA and Switzerland
Georgios Leontaris
georgios.leontaris@hsbcpb.com
+41 (0)58 705 5746

Chief Investment Officer, UK & CI
Jonathan Sparks
jonathan.sparks@hsbcpb.com
+44 (0)20 7860 3248

Chief Investment Officer, Americas
Jose Rasco

Global Head of Fixed Income
Laurent Lacroix
laurent.lacroix@hsbcpb.com
+44 (0)207 024 0613

Global Head of Equities
Kevin Lyne Smith
kevin.lyne-smith@hsbc.com
+44 (0)207 860 6597

Currencies and Commodities Strategist
Rodolphe Bohn
rodolphe.bohn@hsbcpb.com
+44 (0)203 359 1177

Senior Fixed Income Credit Specialist
Elena Kolchina
elena.kolchina@hsbcpb.com
+44 (0)207 860 3058

Director, Global Equities
Bryan O'Carroll
bryan.ocarroll@hsbcpb.com
+44 (0)203 268 4220

Global Market Analyst, Real Estate Investment
Guy Sheppard
guy.r.sheppard@hsbc.com
+44 (0)207 024 0522

Senior Product Specialist, Private Market Investments
Jorge Huitron
jorge.emilio.huitron@hsbc.com
+44 (0)203 359 7040

Head of European Hedge Fund Research
Alex Grievson
Alex.grievson@hsbc.com
+44 (0)203 359 7065

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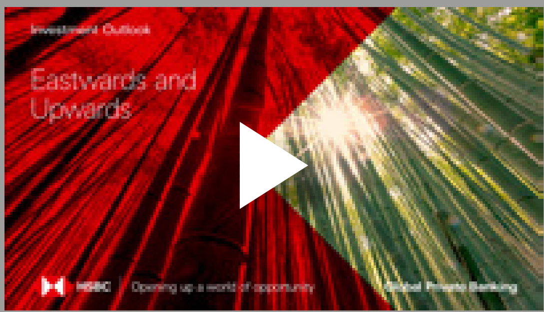
Eastwards and Upwards



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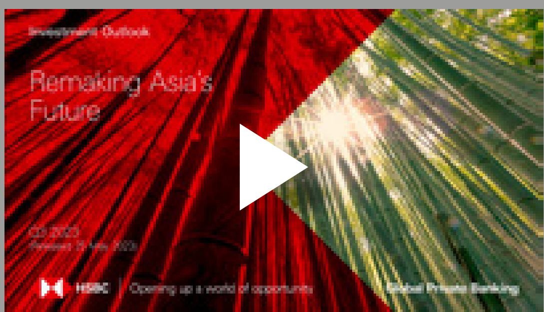


Welcome

Dear client

The financial news tends to focus a lot on the negatives and the risks around us, such as recession fears, banking turmoil and geopolitical challenges. Yet equity markets have rallied and diversified portfolios have already retraced more than half of their 2022 fall.

Investors who focus too much on the risks may fail to recognise the opportunities. They may also confuse the risk scenarios with the core scenario. We think that the core scenario is actually relatively constructive, for several reasons. First and foremost, we are close to the peak in the US policy rate, and this should remain the number one source of support for equity and bond markets.

The economic slowdown in the West is a headwind, but a less important driver, in our view: the slowdown is more gradual than expected, and economists are in fact upgrading old forecasts that now look too low. More importantly, GDP growth matters less than earnings, which continue to surprise to the upside, as companies protect their margins through cost control and with investments that raise productivity.

So while many investors are sitting on cash, we don't. Some investors want cash because it provides flexibility and USD cash currently earns close to 5%. But we think bond markets, blue chip dividend stocks, volatility strategies and hedge funds, to name a few, will outperform cash in the next 6-12 months. As for flexibility, trying to time the market is fraught with difficulty. Markets tend to look forward and could start to price in more rate cuts if inflation continues to fall. As for stocks, we think the wave of earnings downgrades is easing and markets could start to look towards a re-acceleration of profits in coming months.

Asia is responsible for much of our constructive global view and is also the area where many of the opportunities lie. It is in part because of China's consumption led recovery and India's growing wealth and tech upswing that we think the world economy cannot go into recession. We expect Asian earnings to accelerate, which should support the local equity markets and eventually lead to more inflows. In Asian credit too, we find attractive carry opportunities.

Of course, we don't ignore the risks but as we don't think they will cause a systemic crisis, we try to find ways to manage them rather than making them a big part of our core strategy. For example, we stay in the senior part of banks' capital structure, and we have an underweight position in REITs – especially those with large commercial real estate exposure.

Our priorities in the current environment are fourfold:

1. Capturing Asia's upturn: because Asia's acceleration contrasts with the slow growth in the West, and Asia's equity and credit valuations are cheap.

2. Locking in yields of quality credit: because yields are still high but markets could start to incorporate more rate cuts at an unforeseen moment.

3. Exploiting dispersion and dislocations through active strategies: because the unsynchronised cycles and volatility lead to opportunities that nimble investors can exploit via managed strategies, hedge funds, volatility strategies and private markets.

4. Seeking growth from profitable tech: because peak policy rates are supportive of growth-style stocks and we foresee strong earnings growth in areas such as AI & Automation and capex in advanced manufacturing.

In addition to these priorities, we of course continue to invest in our High Conviction Themes that capitalise on our Top Trends. And here again, we find that Asia can offer opportunities to find better growth than in the West, while capitalising on structural trends such as the Digital Transformation and Sustainability.

So yes, we think Asia is in a good spot, both in the short term and for the longer term, and we think globally diversified portfolios will benefit from adding to Asian assets. By going Eastwards, we believe we go Upwards – towards higher growth and higher returns.

Willem Sels,
Global Chief Investment Officer
25 May 2023

Our Portfolio Strategy

We maintain a mild risk-on approach, with our underweight in cash funding our overweight positions in high quality bonds and hedge funds. This is because our outlook is somewhat more positive than consensus: we think peak policy rates will provide a continued tailwind, while economic growth and earnings in developed markets may not be as bad as many fear. We believe it's Asia's turn to see strong market performance and cyclical economic momentum, while many structural opportunities in Asia are also at a pivotal point. In this environment, USD should continue to weaken.

Cash: underweight

Fixed Income: overweight

Focus on high quality borrowers

Medium duration

Equities: neutral

Mild overweight in US

Full overweight in Asia; mild overweight in Latin America

Underweight in EM EMEA and Switzerland

Bias towards quality

Alternatives: overweight

Overweight in Hedge Funds

Keep core allocations to Private Markets and Real Estate

It is easy to be negative, amid high rates, uncertainties around the path of inflation, recession risks, several US bank failures, EM bond defaults and restructuring, commercial real estate challenges, the ongoing Russia-Ukraine war, US-China strategic competition and complex geopolitics. Yet sitting on cash has not been a good strategy in the year to date. So far this year, the expectation of peak rates has led to asset price inflation amid falling CPI inflation. This is the exact opposite of 2022, where we had a broad-based fall in asset prices amid rising CPI inflation. So while in 2022 cash was king, 2023 is a year to be invested.

We think there are five key drivers of markets:

1. The imminent policy rate peak in the U.S. We expect the Fed to hike once more in June, by 0.25%, and then keep rates unchanged throughout 2023. Markets are arguably a bit too dovish, as they price in some US rate cuts before year end. Bears will see this as a negative, but we think that risk sentiment will focus on the positive side of the equation, which is that the hikes will soon be behind us. There is more clarity on this point because inflation has continued to fall in the US, and the base effects from oil and utility costs will very rapidly start to cause a fall in Eurozone and UK inflation in coming months. Reduced uncertainty can help lower risk premia, which should be good for risk assets, including equities, IG credit and EM assets.

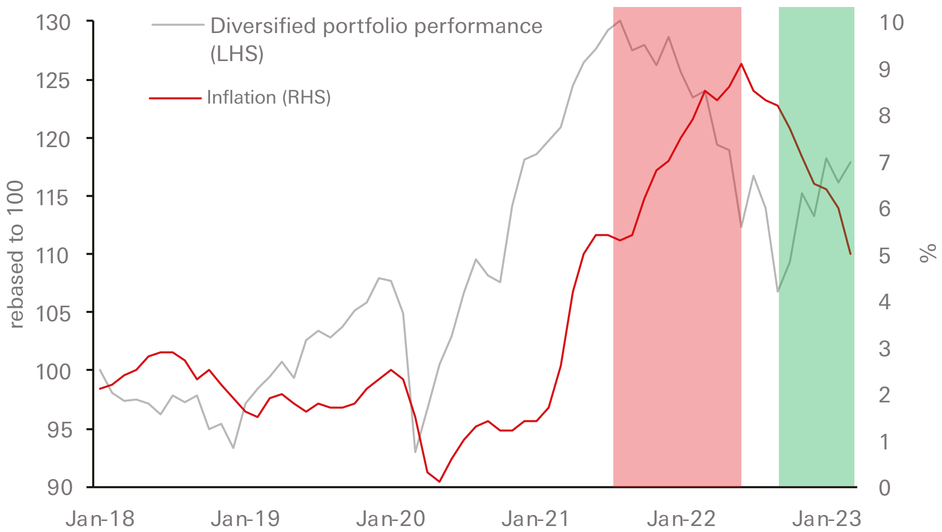
2. If a US recession occurs at all, it should be mild. With all the risks around us, we cannot rule out a recession, but it is not our base case. Bears rightly mention that banks are tightening their lending standards due to the US banking sector turmoil. Surveys indeed show that lending conditions are already tightening, but this is part of the expected transition mechanism of higher rates, and mainly those rate hikes rather than much wider credit spreads. Delinquencies remain very low (even for commercial real estate) and banks of course need to continue to lend in order to earn the lucrative net interest margin between short-term deposits and long term loans. So while small or weak companies may find it hard to find funding, the typically large cap and better quality companies in benchmark equity indices should be less affected. Companies may find funding in private markets too. And while the US economy is indeed clearly slowing, strong consumer demand and solid labour markets create a good starting point, which means a recession – if it occurs – could be delayed. Both in the US and in Europe, in fact, economists have been upgrading their forecasts for Q1 and Q2, because they had been too pessimistic.

3. Earnings matter more than GDP, and they are more resilient than expected. Analysts had become so negative on Q1 earnings that companies beat expectations to a bigger degree than usual. We think companies could beat expectations again in Q2. This is in part because CPI (a proxy for prices charged) is falling less rapidly than PPI (a proxy for input costs), which helps margins. Cost cutting is a priority and wage increases are slowing. Equities may find it hard to rally sharply as earnings growth expectations remain negative in Q2, but as earnings recover in Q3 and Q4, we could see more upside in H2. We are encouraged by the apparent bottoming in global PMIs and business surveys, which often signal a bottoming of earnings momentum.

4. Asia's growth acceleration provides significant encouragement for the region and the world. We're bullish on Asia's growth and asset performance for three reasons. Firstly, China's consumption-led recovery should be sustainable, as we've already seen from continued rebound in services activity and GDP. Considerable household savings accumulated during the COVID period will increasingly be put to work as confidence rises, so we expect retail sales to grow 12% this year versus a slight contraction last year. Secondly, China's focus on growth extends beyond this short-term reopening period, as a stabilisation in property sector activity is much needed, and private sector growth is required to create jobs and bring down youth unemployment. So we think policy support will focus on delivering at least 5% real GDP growth (we think it will reach 6.3%). Lastly, we think some of the structural opportunities in Asia are at pivotal points. The net zero transition receives a great focus, while technological self-sufficiency is leading to huge investment. The long-term rise in middle-class purchasing power is coupled with the current 'revenge spending' (due to the reopening). And sentiment towards India has been boosted considerably as India's population recently overtook China's, and global tech demand benefits India. All of the above make Asia stand out, especially when compared to the current malaise characterising the west.

5. A myriad of risks should create continued volatility, but no systemic crisis. Equity markets have faced considerable challenges, but nevertheless have continued to progress in recent months. This is principally because none of the risks is seen as systemic, and because falling inflation, the end to the rate hikes and stronger Asian growth are bailing us out, just at the right moment. That doesn't mean that we should ignore the risks, but instead manage them. For example, it is prudent to prefer investment grade credit over high yield as the cycle slows and credit standards tighten. And even though the banking sector turmoil has eased, we prefer senior bank bonds over subordinated bonds or stocks. Moreover, to manage some of the real estate risk (which we see as a slow burn rather than a wildfire) we hold an underweight view, specifically on real estate stocks (REITs) and offices, which are most affected by the regional banking crisis. The risk that inflation remains higher for longer (though not our core case) is one of the reasons why we like hard assets such as infrastructure (including renewables) and keep exposure to gold (in spite of the high price level). Geopolitical risks are very hard to manage, but some exposure to commodities, as well as portfolio diversification should help. We fully expect to see continued volatility and think this will help hedge fund performance. Importantly though, investors should not confuse risk scenarios with the core scenario, and our biggest calls are based on our core beliefs around rates, inflation, growth and earnings.

In 2022, returns fell while inflation jumped, and cash was king. 2023 has so far been a mirror image, with returns jumping and inflation falling.



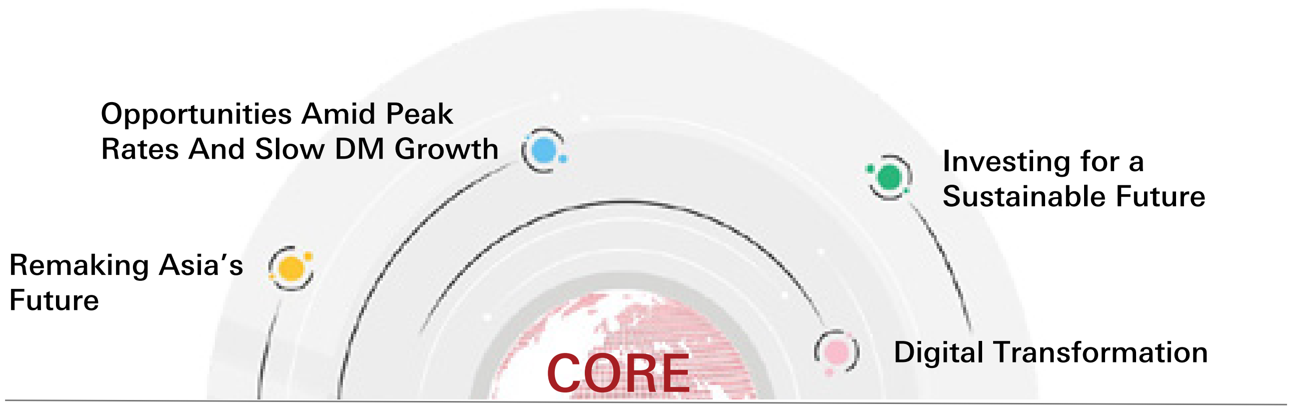
Source: Bloomberg, HSBC Global Private Banking as at 24 May 2023. Past performance is not a reliable indicator of future performance.

In addition to our core views highlighted above, and the four investment priorities listed in the table on the right, we continue to highlight interesting thematic investment opportunities. In Asia, we exploit China's recovery opportunities driven by consumption recovery and policy stimulus. We also see more structural opportunities in Asia's rising tigers, which include ASEAN as well as India. The Digital Transformation continues unabated and we think peak rates as well as strong earnings growth should continue to support performance – especially for themes such as AI & Automation. Sustainability remains key to our investment process, and many of the themes are helped in the short term by the relative outperformance of growth and momentum stocks, and the fading momentum of oil and gas stocks. Apart from these structural themes, we also position for the current slow growth in DM and peak rates. Many of the themes under this trend are represented in our core strategy too, but investors with a particular geographical focus, or a need for income or hard assets may find inspiration here. We discuss all of these Top Trends and High Conviction Themes in more detail in the following chapters.

Our four investment priorities this quarter

1. Capturing Asia's upturn
As developed markets struggle with slow growth and recession fears, Asia's upturn stands out. China's reopening and renewed focus on sustained growth should benefit the region. Asia's equity and credit markets are relatively cheap, adding to the attraction. We think earnings and economic growth will be better than consensus forecasts, which should bring investors back, and boost market performance. We are overweight equities in mainland China, Hong Kong, India and Indonesia.
2. Locking in yields of quality credit
As inflation continues to fall in the West, the policy rate peak is imminent, and bond yields have most probably already peaked. We want to lock in the current high bond yield levels because they could fall when markets start to anticipate more future policy rate cuts. We focus on quality credit amid the economic slowdown, across developed and emerging markets, and on senior bonds when investing in financials. We position in medium duration with 5-7 years maturities.
3. Exploiting dispersion and dislocations through active strategies
The unsynchronised economic cycles, uncertainty around macro variables and market fears will continue to lead to volatility, dispersion and dislocations. This can be exploited through multi-asset strategies, active management, hedge funds, private markets and volatility strategies. We prefer to manage risks through managed and diversified strategies rather than to sit on cash and flee from the risks.
4. Seeking growth from profitable tech
Tech and other growth-style stocks are benefiting from the prospect of peak policy rates. In addition, rapid innovation (e.g. AI and Automation) and the drive towards self-sufficiency creates opportunities for earnings growth that far exceed GDP growth rates. That said, we look for companies with strong current cash flows and avoid unproved business models.

Top Trends and Q3 high conviction themes



Remaking Asia's Future

- Asia's Rising Tigers
- China's Recovery Opportunities
- Asia's Green Transformation
- Asian Quality Credit

Opportunities Amid Peak Rates And Slow DM Growth

- American Resilience
- Defensive Positioning Across DM Financial Bonds
- Durable Dividends
- Infrastructure
- Opportunities in Quality Credit
- Asia Through DM
- European champions

Digital Transformation

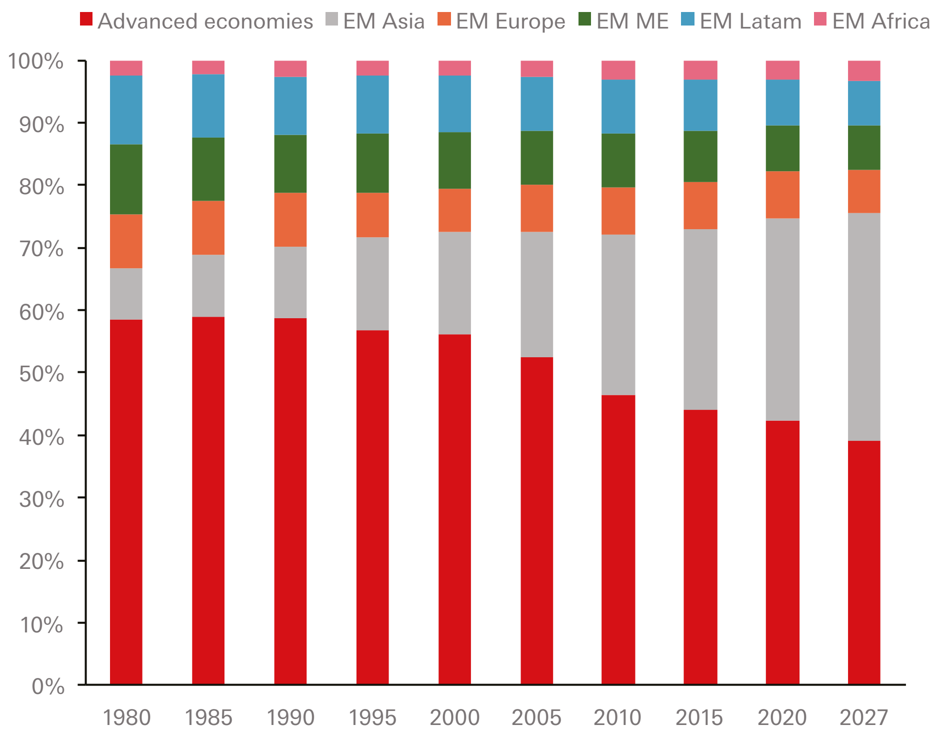
- Smart Mobility
- AI and Automation
- Aerospace

Investing for a Sustainable Future

- Energy Transition and Independence
- Investing in Biodiversity
- Sourcing Income in a Sustainable Way
- Social Empowerment and Well-being

Source: HSBC Global Private Banking as at 24 May 2023.

Asia already accounts for more than a third of global GDP, and that share continues to grow



Source: IMF, HSBC Global Private Banking as at 24 May 2023.

Signs of Improvement in Sentiment

Our Global Composite Sentiment Indicator offers a comprehensive overview of investor, business, and consumer surveys, as well as market positioning. By consolidating data from 70 different surveys, this indicator provides a comprehensive summary of economic expectations and market confidence. It currently reveals a trend towards improved sentiment, while positioning is still below average. That suggests a potential for continued bullish market conditions. We note that possible downside risks related to recent bank failures have had a limited impact on the overall sentiment readings. Our number-crunching has also discovered an uptick in an unexpected place: global trade. Contrary to the much-discussed de-globalisation trend, it seems that China's reopening and other factors should soon lead to a cyclical upswing in trade activity.

Improvements in sentiment despite heightened volatility

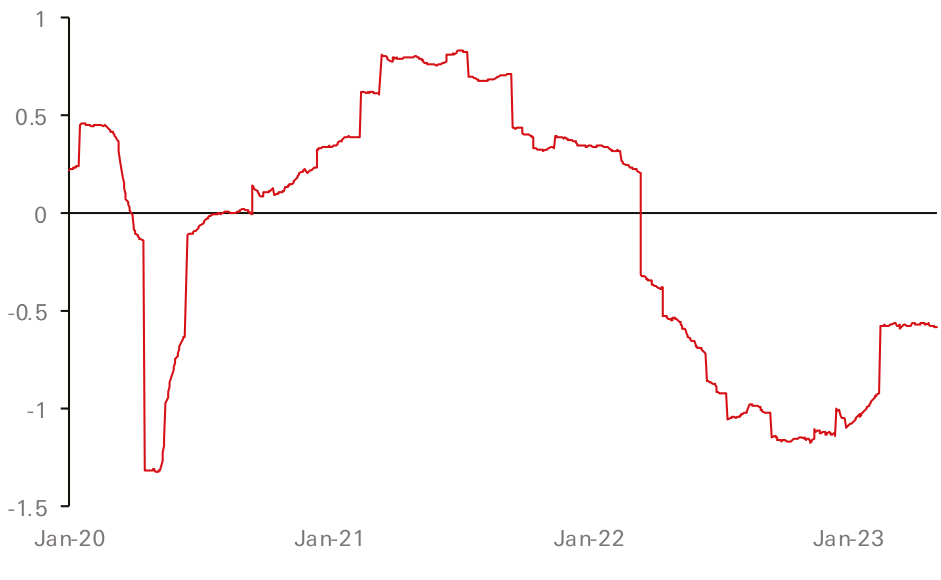
Recent developments across the surveys and indicators we monitor showcase a notable improvement in sentiment in 2023. All four underlying sentiment components (Investor, Business, Consumer, and Positioning) have shown a robust recovery from their low points in 2022 with little fluctuation.

Our **investor sentiment** indicator has showed the strongest improvement in the past two months and moved earlier than the other sentiment indicators (starting in mid-November last year). The more bullish readings in Intelligent Investor and AAII investor surveys, together with improvements in stock market expectations in Germany led the recent positive change in the group. Over the last two months, Street Confidence Index and Asia-ex Japan indicators have improved too. The collective positive shifts across various important investor surveys paint a more optimistic picture than the readings observed just months ago.

Business sentiment bottomed at the end of November 2022, and the uptick in this group has recently been driven by diverse regions too. Despite minimal notable changes in business surveys in the last month, the primary improvements over the past two months include Richmond shipment expectations, China's non-manufacturing business activity expectations, UK business optimism and IFO demand expectations. Although some other surveys contributed negatively, their impact has been comparatively minor.

Early signs of improvements in **consumer sentiment** have been visible since late July 2022. While there

Global Composite Sentiment Indicator



Source: Refinitiv Datastream, HSBC Global Private Banking as at 24 May 2023.

is lack of a strong trend in the last month, good news regarding future employment expectations in China, thanks to the grand reopening, has been the main positive contributor in the past two months. China's overall consumer expectations, followed by improvements in the UK Ipsos Primary Consumer Sentiment Index, as well as other US indicators such as IDB/TIPP Economic Optimism Index, and vacation plans intended by airplane in the next 6-months have also contributed to the positive outlook in the group. Conversely, consumer expectations and future employment expectations in the US have seen minor negative moves. However, the strongest movers have led to an overall positive outlook in consumer sentiment despite negative contribution from some surveys.

Positioning: Compared to the other sentiment groups, positioning appears to be more negative in both 1-month and 2-month timeframes. While single equity options positioning has displayed some positive signs and the Inverse CBOE Put/Call ratio has witnessed an upward shift, it hasn't been sufficient to counterbalance the broader outlook driven by the index derivatives positioning and a slight decrease in EM & HY mutual fund flows over the past month.

Positioning usually moves in line with investor surveys with a 2-month lag. We believe it is reasonable to expect to see a disconnect between what investors say and what they do. Cognitive biases can contribute to delayed market reaction and inconsistent adherence to stated preferences. Nevertheless, if the other indices continue to improve, we think positioning would need to follow. There seems to be more upside to positioning if other sentiment components continue to improve.

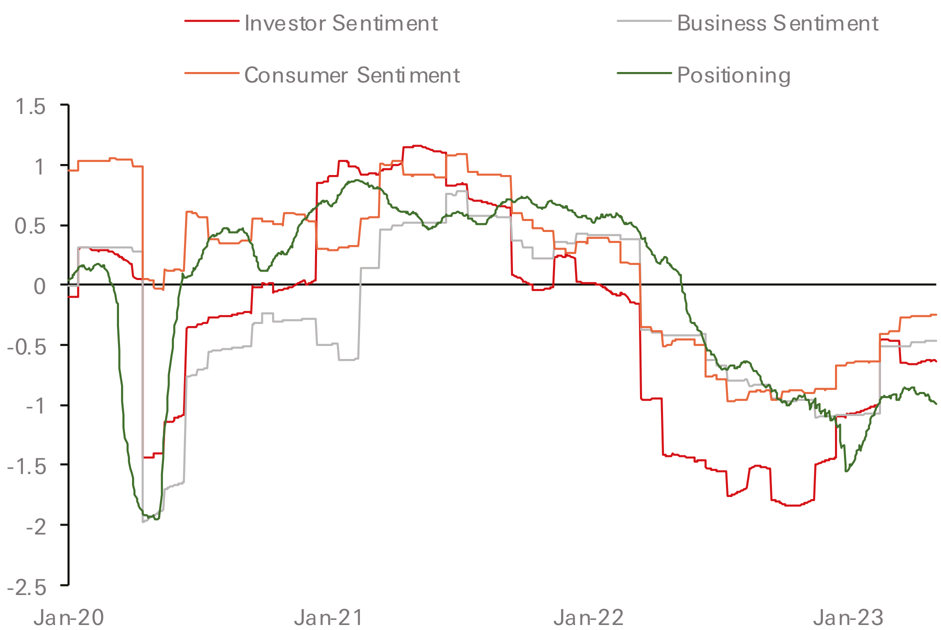
A comment on global trade

The remarkable upturn in both consumer and business sentiment in China is signaling optimism for future economic growth and trade activity. Although the current rebound in China is more driven by services than in the past, heightened business activity expectations in China could be a contributing factor to positive prospects for future trade activity. This appears to be further supported by healthier economic expectations from other regions in the world.

The outlook for shipment expectations in the US has also shown signs of improvement. Improving new export orders reflected in the ISM survey also indicate a growing traffic for shipments for the world's largest importer. Germany, a key player in global trade and Eurozone's largest economy, joins the fray with encouraging demand expectations reflected in the IFO Business Climate Index.

A somewhat weaker US dollar adds another supportive argument that the following months might be better for global trade. The Baltic Exchange Dry Index (BDI) fell substantially from October 2021, but has been showing some more resilience since February 2023. This could be a sign for increasing demand for goods in the world at historically reasonable shipping costs across the globe. A further compelling reason comes from recent outperformance of the Nasdaq Global Semiconductor Index (GSOX), which can be considered important for global trade prospects as the demand for semiconductors typically reflects the broader economic activity.

Sentiment Indicator Components



Source: Refinitiv Datastream, HSBC Global Private Banking as at 24 May 2023.

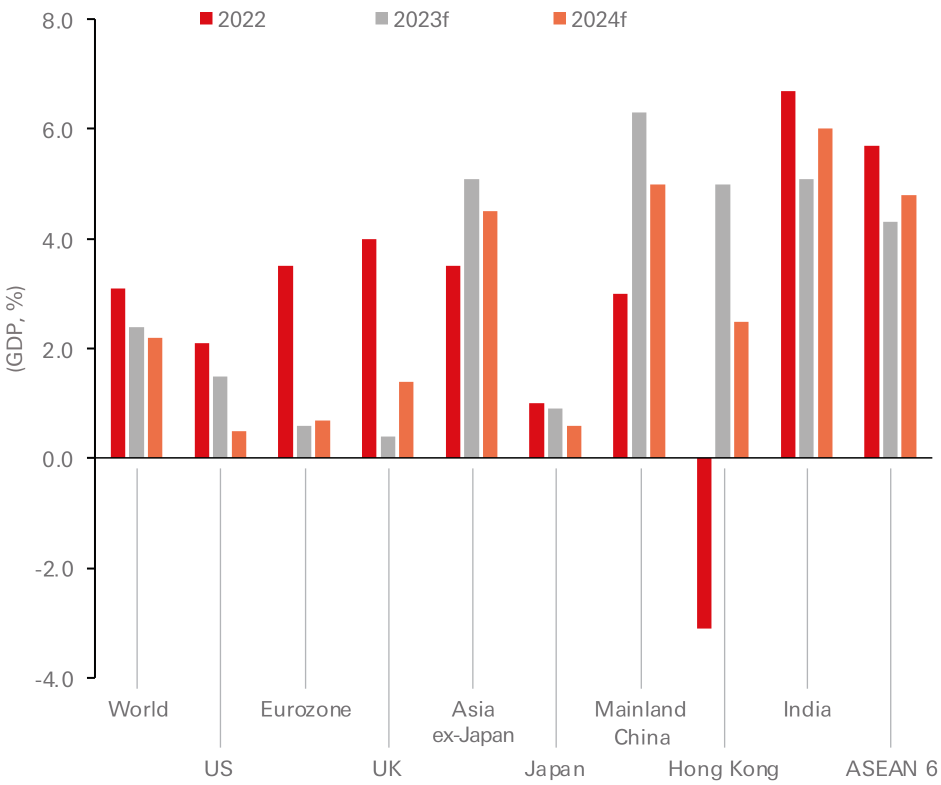
Remaking Asia's Future

Our four high conviction themes

1. China's Recovery Opportunities
2. Asia's Rising Tigers
3. Asia's Green Transformation
4. Asian Quality Credit

Amid the global economic downturn, Asia stands out as a bright spot delivering resilience and growth, supported by China's robust consumption-led recovery and policy stimulus. China's growth recovery and resilient growth in India and ASEAN should help maintain Asia's economic momentum in spite of weakened global demand and credit tightening in the US and Europe. Easing inflation further provides breathing space to the Asian central banks and consumers, allowing policymakers in most Asian economies to end the monetary tightening cycle swiftly ahead of the Fed and ECB. We expect the Bank of Korea to start cutting policy rates in Q4 2023, followed by India, Indonesia, Hong Kong and the Philippines in 2024.

Asia's growth acceleration versus DM slowdown



Source: CEIC, HSBC Global Research forecasts, HSBC Global Private Banking as at 24 May 2023. Forecasts are subject to change

Much stronger-than-expected China Q1 growth led us to raise our China 2023 GDP growth forecast from 5.6% to 6.3%. We expect China's consumption revival, and the resilient growth in India and ASEAN to support a respectable 5.1% GDP growth in Asia ex-Japan this year. Defying the broad-based decline in global manufacturing PMIs, India and the ASEAN registered moderate expansion in their manufacturing sectors due to resilient domestic demand and benefits of supply chain reorientation amid geopolitical uncertainty. In contrast to the economic slowdown in the developed world, Asia will be the only region where we project a notable growth acceleration to 5.1% in 2023 from 3.5% in 2022. We maintain our full overweight position on mainland China equities and hold a mild overweight view on Hong Kong, Indian and Indonesian equities to capture both the tactical and the structural opportunities.

Taking into account that the most significant incremental impact from China's reopening has already played out in the past six months, we have repositioned our theme on Asia's Reopening Winners into a new High Conviction Theme on **China's Recovery Opportunities**. We expect China's cyclical upswing to expand into a broader and more balanced recovery path in H2 2023 with support of further

fiscal and monetary stimulus. China has recorded four consecutive months of robust expansion in the services sector, thanks to unleashing of strong pent-up consumer demand and support of USD1trn in accumulated excess household savings. The Labour Day Golden Week holidays (29 April to 3 May) achieved a record

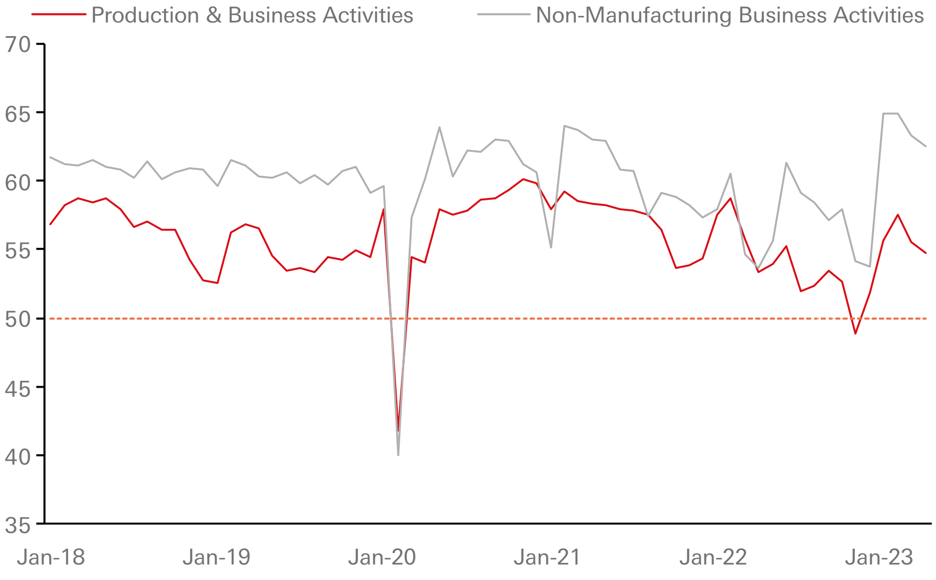
number of 274m domestic holiday trips, 19% above pre-pandemic 2019 levels. Total domestic tourism spending made a healthy 0.7% recovery to RMB148bn, surpassing the 2019 numbers.

The recovery path has been uneven so far, with April manufacturing PMI declining into modest contractionary territory due to weaker global demand and domestic labour market pressure. China's Politburo addressed this in its meeting in late April, setting a decisively pro-growth policy tone to highlight that the growth recovery would remain the top priority of the government this year. Supportive policies should be expected, especially in light of the global headwinds (banking turmoil and weaker external demand). We therefore anticipate more proactive fiscal stimulus and targeted monetary and credit policy easing, and this should set the stage for a more balanced economic recovery ahead. There are initial signs that business confidence is picking up, as indicated by the China PMI business expectations indices of both manufacturers and service producers.

We continue to see the strongest earnings recovery potential in China's services sector. Riding on the strong consumption recovery momentum, we have revised up our China retail sales growth forecast from 8.5% to 12% in 2023, compared to a contraction of 0.2% last year. This should bode well for quality leaders in both the consumer discretionary and staple sectors. The broadening consumption recovery should also support Chinese internet leaders in various business lines, such as online advertising. A more market-friendly regulatory environment and improved growth outlook should reduce the significant policy risk premium in the Chinese internet stocks versus their global peers.

As an integral part of China's strategic pivot towards a high-quality growth model, the reform of State-Owned Enterprises (SOEs) should result in new motives for large SOEs to improve their profitability and ROE. We expect quality SOE leaders in banking, infrastructure, telecom, energy and property to see the most re-rating potential on the tack of those reforms. More proactive fiscal stimulus will be financed through increased special local government bonds issuance, and should create 5% growth in infrastructure and manufacturing investment this year. The subdued inflationary backdrop will enable the PBoC to provide further monetary easing in the form of liquidity support, such as a further 25bp cut in the RRR in Q2, more targeted credit support and ongoing open market operations. On housing, Beijing's policy

Business expectations in China stay at elevated levels



Source: China National Bureau of Statistics, Bloomberg, HSBC Global Private Banking, as at 24 May 2023.

stance remains accommodative and we expect more property policy relaxations to be deployed in top-tier cities.

Looking beyond opportunities from China's recovery, we further expand the theme on ASEAN Tigers into a broader new High Conviction Theme on Asia's Rising Tigers to capture promising secular growth opportunities in India and Southeast Asia. The Indian and ASEAN economies enjoy demographic tailwinds as they have the youngest populations in Asia. The median age of populations in India and ASEAN is at around 28 years old and 33 years old, respectively, which compares favourably to the median age of over 40 in many developed countries. The demographic dividends offer strong driver for domestic consumption in India and Southeast Asia.

In contrast with the slowdown in the west, India and the ASEAN stand out as the exceptional outperformers delivering modest expansion in their manufacturing PMIs. We expect India to remain on track to sustain 5.1% GDP growth in 2023 and deliver 6.5% growth per annum during 2023-2032, which could double the economy's size in a decade.

In India, we focus on opportunities from two emerging growth industry groups – the high-skilled exports sectors (IT software services and pharmaceuticals) that are gaining global market share, and the fast booming digital ecosystem. Indian digital start-ups are attracting significant foreign direct investment inflows, thus contributing to job creation, new investment opportunities and growth. We recently upgraded Indian equities to a mild overweight view to reflect the market's improved valuations, resilient domestic-oriented earnings and a favourable policy backdrop after the Reserve Bank of India paused its rate hikes.

The ASEAN economies offer a balanced regional mix and diversity to weather global macro uncertainty, with Indonesia and the Philippines being more driven by domestic demand, while Singapore, Malaysia and Thailand are more exports-oriented. We see attractive opportunities in consumption leaders in the ASEAN markets as they benefit from an expansion of middle class consumers and China's reopening. We also like ASEAN banks and infrastructure companies as they can ride on solid domestic consumption and tailwinds from the supply chain relocation into Southeast Asia.

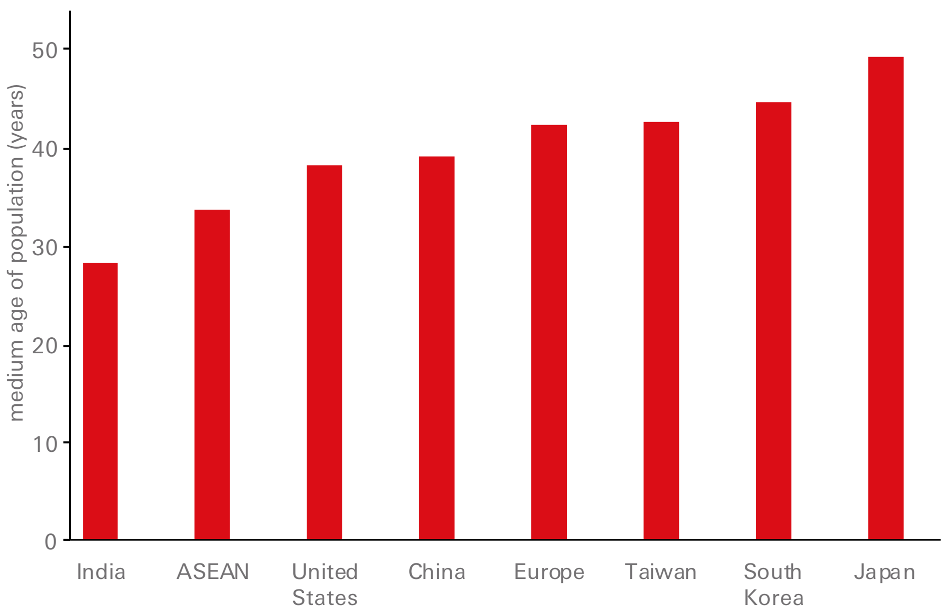
Asia's Green Transformation continues to focus on opportunities from the energy transition and independence, green infrastructure development and innovation of new energy vehicles technologies in the region. According to McKinsey, the addressable market size for green businesses in Asia is expected to reach between USD4trn and 5trn by 2030, as sustainability is increasingly valued by various stakeholders, including investors, customers and employees.

China's transition towards renewable energy and Electric Vehicles (EV) is well underway, backed by strong policy support and catalysed by the global energy crisis. We expect China's annual solar installations to increase at a 13% CAGR to 125GW in 2025. We see promising opportunities in China's energy storage sector, with its 12-month forward earnings growth to stay strong at over 20%. In India, the government set the target of renewable energy contributing 50% of total energy supplied by 2030. Notably, 96% of net incremental power capacity addition in India year-to-date has come from green energy.

Despite near-term headwinds from the price war initiated by Tesla, we see attractive medium-term growth opportunities for China's booming EV supply chain. China's EV penetration rate should stay well above global average in the next decade due to favourable policy support, strong consumer preference and increasing model supply. We forecast EV penetration in China to reach 50% in 2025 and 88% in 2030, well ahead of global average of 27% and 52%, respectively. Nearly 80% of the world's fast-charging stations and 60% of normal charging stations are currently in China, which also controls over 80% of global battery recycling capacity.

Positioning for the peak in US rates, the investment outlook for the **Asian credit market** becomes more constructive. We are bullish on our theme on Asian Quality Credit, as we believe this is an opportune time to switch from time deposits into high quality credits to lock in yields at compelling levels. We add Asian financials to the opportunity set under this theme, focusing on Japanese and Korean banks and life insurers, and select banks in Australia, Hong Kong, Singapore and Thailand. We capture the attractive yield pick-up, which is in part

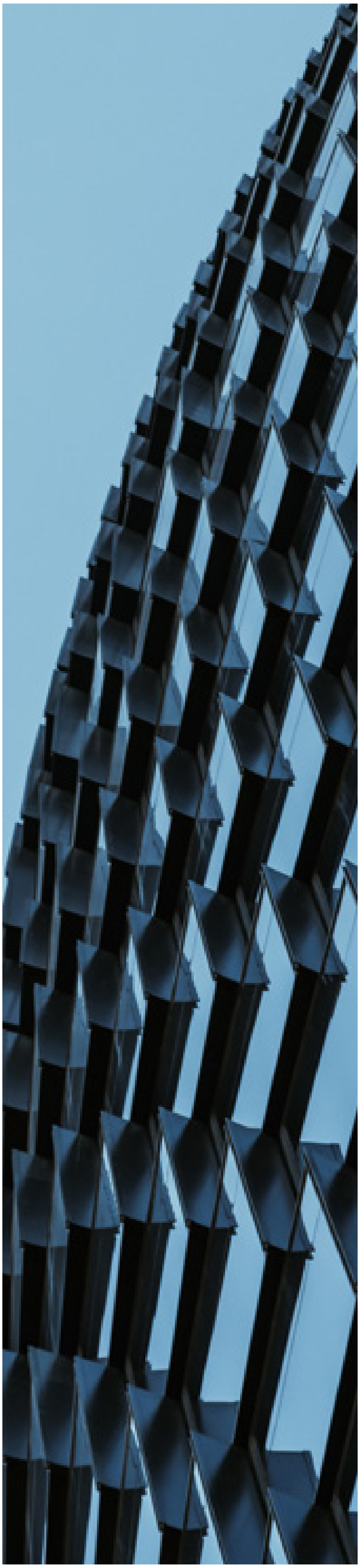
India and ASEAN enjoy demographic dividends that support economic growth



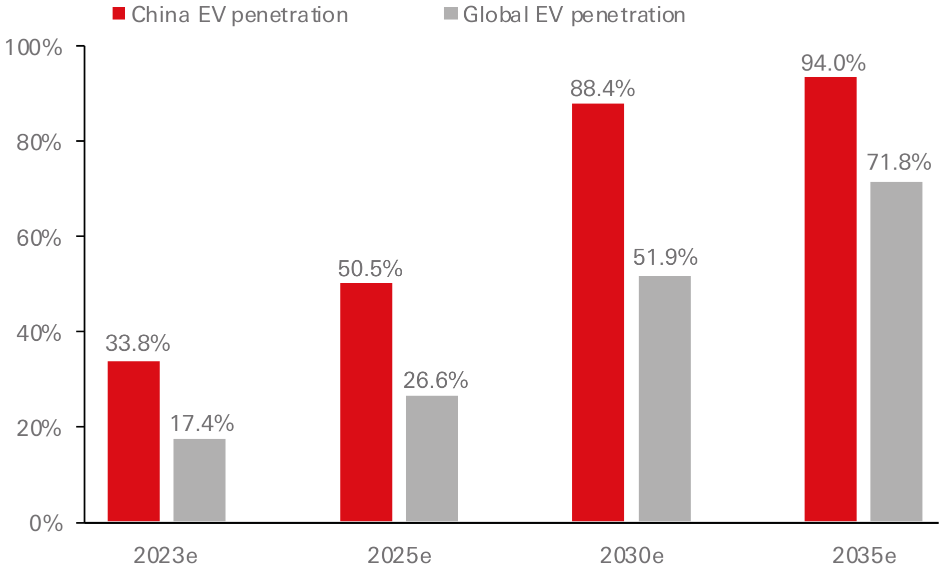
Source: United Nations, Department of Economic and Social Affairs, Population Division (2022), HSBC Global Private Banking as at 24 May 2023.

driven by the banking turmoil in the US and Europe, but has unfairly dragged down prices of high-quality Asian financial bonds. Asian banks have strong capital ratios and the sector is well supported by more pro-growth Asian central banks.

As we expect the recovery momentum in Hong Kong to stay strong, we favour income opportunities from high quality local credits in the retail and property sectors. In the Chinese real estate sector, we maintain our cautious positioning and stay focused on quality SOE property issuers. We continue to like Indonesian quasi-sovereign IGs, thanks to the strong domestic fundamentals supported by rising domestic consumption and resilient exports.

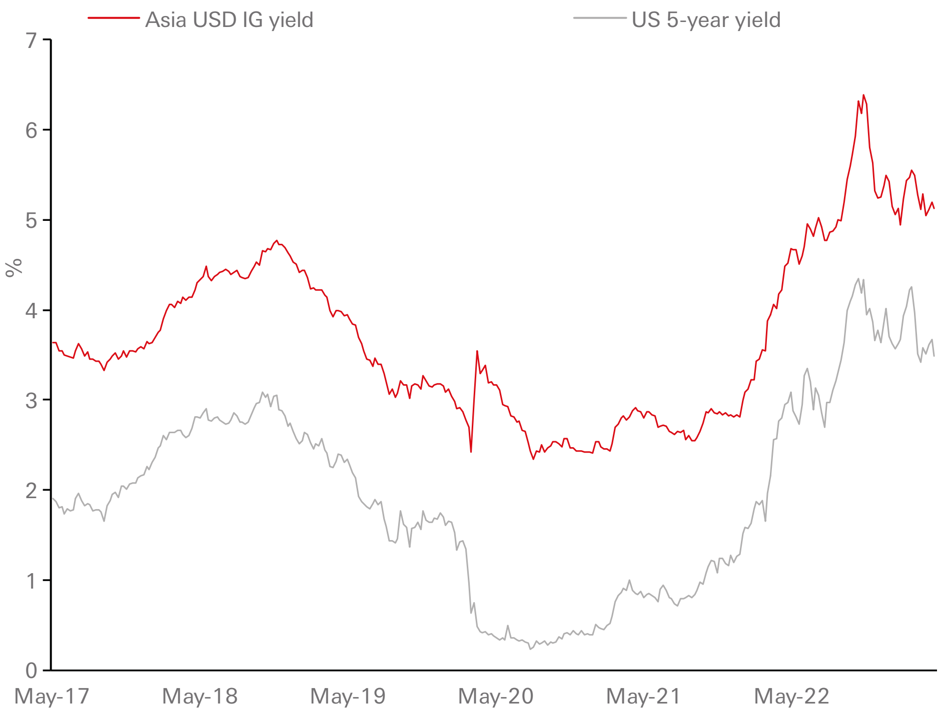


China's EV penetration rate is expected to stay well above the global average in the next decade



Source: United Nations, Department of Economic and Social Affairs, Population Division (2022), HSBC Global Private Banking as at 24 May 2023.

Asian IG bonds offer an attractive yield pickup



Source: Bloomberg, HSBC Global Private Banking as at 24 May 2023. Past performance is not a reliable indicator of future performance.

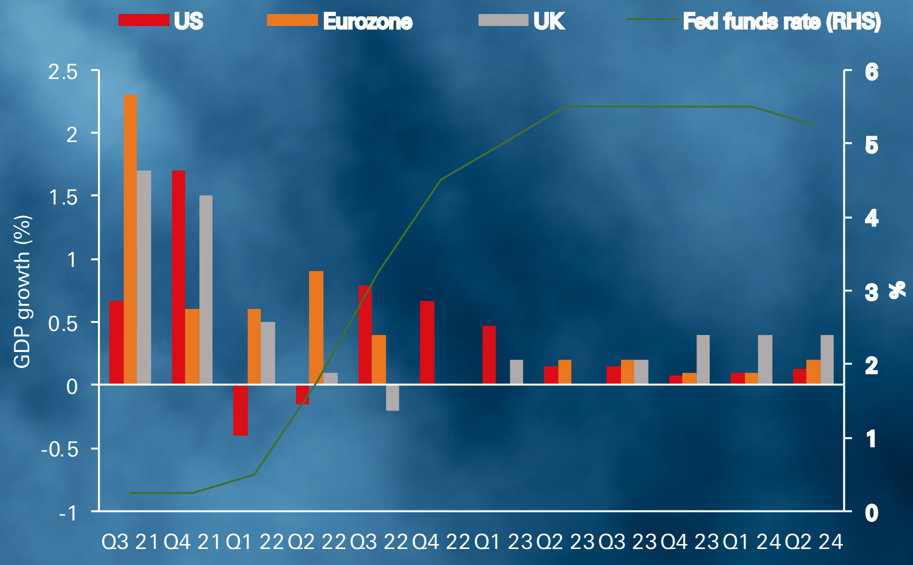
Opportunities Amid Peak Rates And Slow DM Growth

We are close to the policy rate peak in developed economies, and markets even think that the Fed has already completed its final rate hike. This steers us towards bonds, and towards equities that generate income, including dividend strategies. The flipside is that economic growth is slowing, which means that we look for quality and high ratings when investing in bonds, and for earnings resilience in equity markets (e.g. infrastructure). The earnings season illustrated though, that there are plenty of companies in the US and Europe that have strong enough market positions to protect their local earnings and sales. Other companies benefit from the pick-up in Asian demand. Many of these topics are already incorporated in our core portfolio strategy but they can be added as satellites as well.

Our seven high conviction themes

1. American Resilience
2. European Champions
3. Durable Dividends
4. Infrastructure
5. Asia through DM
6. Opportunities in Quality Credit
7. Defensive Positioning
   Across DM Financial Bonds

We foresee slow growth, but a deep recession is unlikely. Peak policy rates should support markets.



Source: Bloomberg, HSBC Global Research forecasts, HSBC Global Private Banking as at 24 May 2023. Forecasts are subject to change

American Resilience: The US economy is slowing and although Fed Chair Powell, like us, thinks a recession may be avoided, we need to look for companies with resilient earnings. Key overweight sectors for us include consumer discretionary and industrials, which are the focus of this theme. This can be complemented with our Digital Transformation themes (see next chapter), which include many US companies with strong earnings prospects as well.

European Champions: Europe has demonstrated remarkable economic resilience since the Ukraine war, thanks to the easing of energy prices, fiscal support and resilience in the consumer sector. A diverse set of global leaders from sectors spanning pharmaceuticals, clean energy, semiconductors, industrial automation and luxury should offer investors exposure to both higher demand from Asia but also from longer term trends such as automation, energy transition, smart buildings etc.

Durable Dividends: Dividends can substantially add to total returns, especially when the potential for sustained upside in equity markets is somewhat limited. Of course, as the cycle slows, it is important to select companies that have sufficiently strong cash flows to make those dividends durable. But dividend expectations remain healthy and we do not think that banks will substantially cut them. From a style perspective, dividend stocks tend to have a quality bias and often qualify as 'low volatility' stocks, which should help as market uncertainty remains substantial.

Infrastructure: Although inflation should continue to come down, it will remain higher than in the past decade, and investors will continue to look for partial hedges. One option is infrastructure stocks, as many of them benefit from a link (often set by the regulator) between their input costs and the prices they charge, which protects their profits. We also like infrastructure's predictable nature of cash flows in the context of a slowing economy.

Asia Through DM: We are bullish on the Asian economy and Asian assets, but recognise that many investors still worry more about policy risk and geopolitics than we do. A good indirect way to tap into Chinese, Indian and other Asian short-and long-term opportunities is through DM companies that cater to Asian consumption. Many European and US consumer brands are loved in Asia.

Opportunities in Quality Credit: Our overweight of high-rated bonds in our core portfolio is also reflected in our high conviction themes. We continue to focus on investment grade, because we think high yield spreads are somewhat too tight and sensitive to the growth slowdown. We see opportunities in better quality EM hard currency corporate bonds as well. We are comfortable with medium durations (5-7 years) and think that floating rate notes are now less attractive as we are already at – or near – the policy rate peak in developed markets.

Defensive Positioning Across DM Financial Bonds: As sentiment in the banking sector remains fragile, we focus our exposure to the most senior part of the capital structure. That said, capital ratios for the sector are well above the minimum regulatory requirements, interest income is strong and loan delinquencies are low. In addition, spreads are attractive when compared to non-financials. We also find opportunities in insurance and are more willing to select some subordinated bonds there.

Digital Transformation

The digital revolution has been underway for some time, but it is now entering a particularly interesting phase as several key technologies converge and interoperability is becoming essential.

Our three high conviction themes

1. Smart Mobility
2. AI & Automation
3. Aerospace

Smart Mobility

In simple terms, smart mobility includes the integration of intelligent technologies in transportation. In the broader context, the theme also embraces governments, companies and individuals making smart decisions and policies about the choices of mobility given the environmental and demographic challenges. The Paris Agreement, the COP27 and the IPCC climate study give an even greater sense of urgency to the adoption of zero-emission technologies, especially in transportation. Electricity, hydrogen, biofuels and ammonia are potential zero-emission or green fuels that should help reduce these emissions.

The recent advances in smart mobility are most evident in Electric Vehicles (EV) where purchases reached 10.7 million or 1-in-7 vehicles last year driven by strong growth in China and Europe, according to BloombergNEF. Purchases are accelerating with new models and manufacturing capacity expanding rapidly. Battery charging infrastructure remains patchy though, with only an estimated 2.7 million charging points globally. But expansion initiatives are finally gaining some momentum. Battery technology continues to advance benefiting from increased R&D budgets and soaring applications.

Complementing the advances in vehicle electrification technologies has been the timely rollout of 5G telecom networks that are supporting newer in-vehicle services while connecting vehicles seamlessly to the surrounding environment providing high quality real time data. Services include everything from software updates, livestreaming of events to the infotainment system, to immersive maps with weather and traffic information. In our view, transportation is undergoing its biggest revolution since the introduction of commercial air travel.

Governments' environmental stimulus packages in several major economies should also provide additional financial impetus. Our smart mobility investment theme focuses on new energy vehicles, 5G, sensors, batteries and infrastructure technologies.

AI & Automation

The last 12 months has seen the long promised potential of Artificial Intelligence (AI) finally becoming a reality. The catalyst was the public unveiling and subsequent release of OpenAI's ChatGPT chatbot, which led to a cascade of technology titans revealing their own AI initiatives. ChatGPT represents a step change in capabilities and applications for AI and has potentially game changing implications for governments, businesses and the consumer. We look to capture this potential in our AI & Automation investment theme.

In particular, the marriage of AI and automation offers considerable potential to expand capabilities and therefore its applications for automation. For example, in the financial services sector, intelligent automation offers more potential with respect to client facing services including more complex investment advice, improved credit and insurance screening and automated secure client recognition.

Similarly, there are numerous healthcare applications including monitoring patients, tracking samples, continuously monitoring real-time patient data, x-ray and NMR scan analysis and automated sample testing.

This is increasingly important in many markets as demographic trends, rising labour costs and labour shortages are making returns on investments in automation even more attractive. The number of operational robots reached 3.5 million units in 2022, with an estimated value of USD15.7bn (source: IFR, February 2023).

In tandem, automation is also benefiting from other technological developments including miniaturisation and advances of sensors, cameras, batteries, software, that together are increasing their capabilities and uses. For example, agriculture is embracing automation from GPS controlled tractors and harvesters, to soil and crop management using drones and AI, livestock feeding and milking.

AI is particularly strong at identifying patterns in complex data sets from various sources including consumers, traffic, weather, financial markets etc. and generating scenarios and outcomes. When this is combined with the increasingly capable automation hardware and improved connectivity (5G mobile, cable and low earth orbit satellite networks) the potential seems almost limitless.

Aerospace

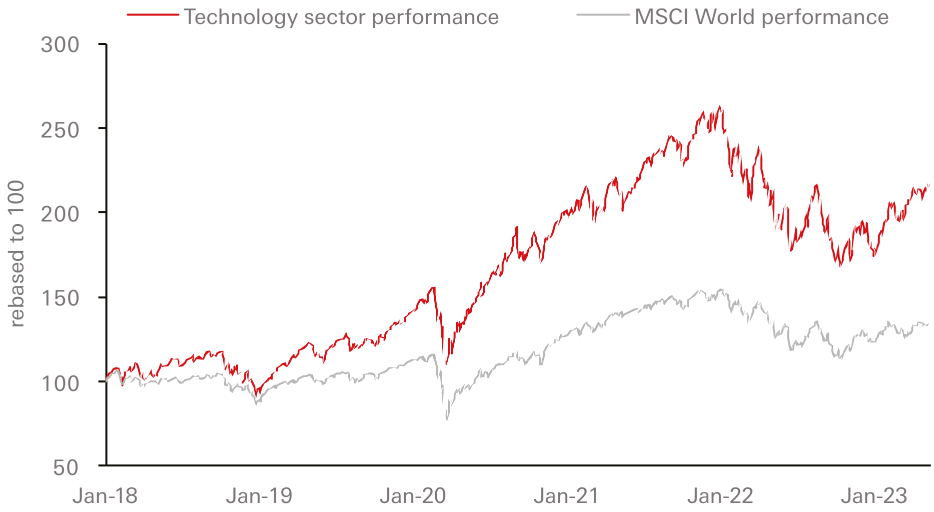
The post-pandemic rebound in air travel is well underway with several major airlines placing very large aircraft orders with manufactures in the last few months. Aerospace manufacturers already had strong order books and significant backlogs, even as COVID restrictions eased, due to persistent labour and supply chain issues. In addition, many governments are increasing their defence spending putting further pressure on manufacturing capacity and supply chains. These factors are helping lift companies in the sector and create investment opportunities.

Aerospace companies are also successfully pursuing the new commercial opportunities in the space economy. Normally the preserve of governments, private companies have already demonstrated viable rockets and space vehicles with some receiving government contracts. The rising demand for data and interconnectivity has created a commercial opportunity for companies to deploy networks of low earth orbiting satellites that can provide full geographical coverage. This has been a key source of growth for the small satellite industry.

In 2022, small satellites represented 95% of spacecraft launched. Small satellite launches are up 18x in 6 years. Small satellites include microsats (100kg-10kg) and nanostats (weighing less than 10kg) which include cubesats that typically are only 10 cm across. Small satellites are a fast-growing segment of the business. They are very cheap to manufacture and a single space flight can carry tens of satellites in a single payload due to their small size and low weight. This enables networks of satellites to be quickly, easily and cheaply deployed, and it has opened up the market to new entrants and new applications.

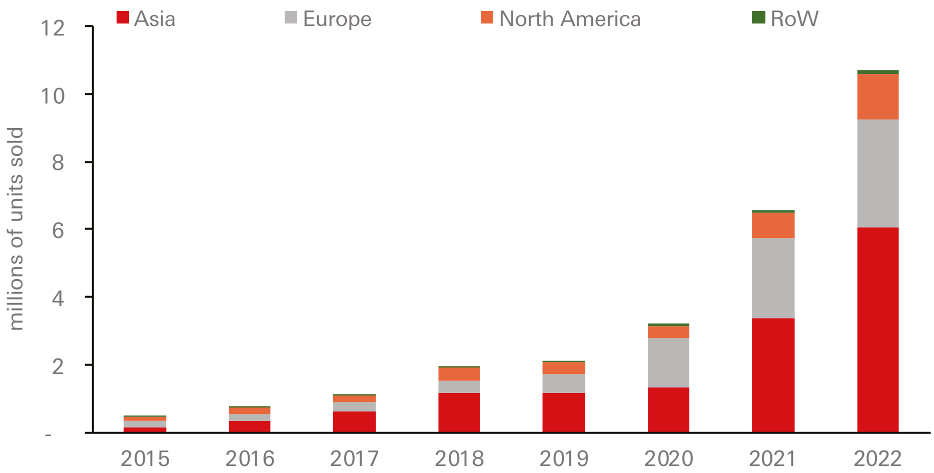
Through our Aerospace investment theme, we identify investment opportunities to this rapidly evolving industry.

Digital Transformation related themes are benefiting from the recovery in the tech sector



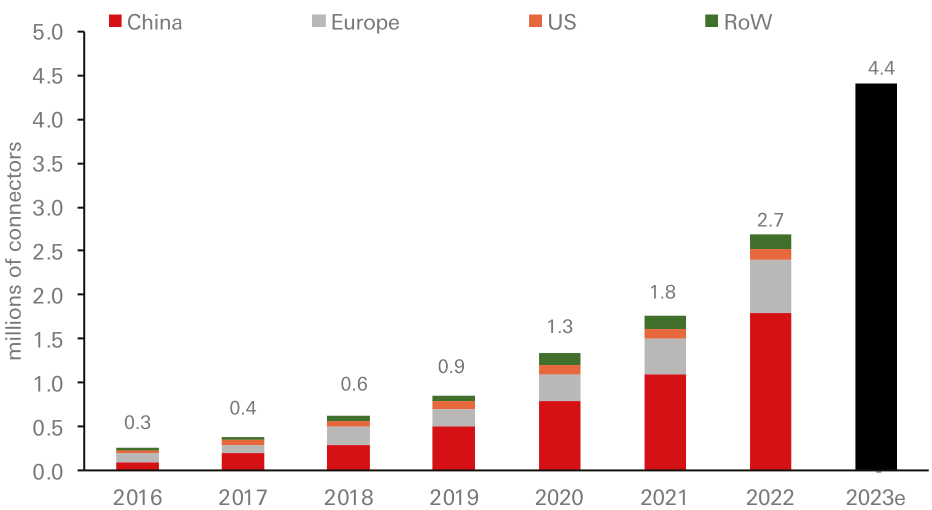
Source: Bloomberg, HSBC Global Private Banking as at 24 May 2023. Past performance is not a reliable indicator of future performance.

Electric Vehicle Unit Sales by Region



Source: Bloomberg, HSBC Global Private Banking, as at 24 May 2023

Cumulative Public EV charging connectors by country

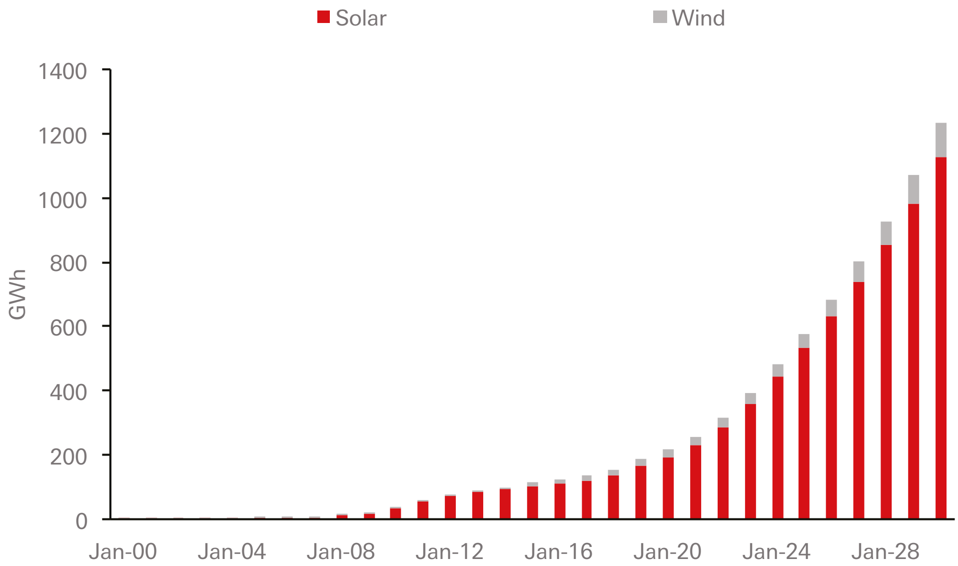


Source: BloombergNEF, Eco-Movement, , HSBC Global Private Banking, as at 24 May 2023

Investing for A Sustainable Future

We are very much in the foothills of a sustainable future. The goal is now known (which has not always been the case) and it is now widely accepted that we need to keep emissions and pollution to a minimum wherever possible. This is driving a sea change across policy, investing opportunities and across the everyday products and services that are needed within the global economy. For companies, sustainability must be a feature of their future. Any companies having long term strategies that don't account for sustainability are in a precarious position with investors. Today, the risk of ignoring sustainability in corporate strategy outweighs the reward, and that is a meaningful change in corporate norms.

Europe's solar and wind capacity growth



Source: Bloomberg Finance L.P. HSBC Global Private Banking, as at 24 May 2023

Our four high conviction themes

1. Energy Transition & Independence
2. Investing in Biodiversity
3. Sourcing Income in a Sustainable Way
4. Social Empowerment and Wellbeing.

Energy Transition & Independence

Europe is at the epicentre of the energy transition as the shift in demand away from Russian oil intensifies the effort to develop alternate, domestic sources of energy. It is estimated that by 2050 Europe will need an investment of $32 trillion to reach its net zero goals. This creates a lot of investment opportunity. Clean power and electrification are the key sources of emission reductions with BNEF estimating up to 78% of future reductions in emissions will come from those two pillars. Solar and Wind capacity has been experiencing high growth in recent years and we expect this to continue to 2030.

The transition to lower emission energy production and greater energy independence is not just a European story of course; the US and Asia are also progressing quickly in these themes. The drivers are somewhat different but encouragingly, economics are a driver in all regions as renewable strategies can often offer better economics when it comes to new capacity.

The combination of economic, societal and political demand, technological progress and the desire for energy independence make our Energy Transition and Independence theme an attractive opportunity.

Investing in Biodiversity

Biodiversity is quickly becoming one of the greatest areas of interest when it comes to sustainability. A big part of the credit for this goes to the Kunming-Montreal Global Biodiversity framework unveiled at the COP15 in December 2022 (even though momentum had long been building). Over 99% of humanity's food and over 60% of our medicines are reliant on nature which makes it all the more surprising how much risk we have placed on ignoring sustainable biodiversity. A major problem has been our inability to value biodiversity, and how to attribute and distribute that value. The Global Biodiversity Framework is now trying to address those issues. As a result, new mechanisms to value, manage and attribute credit appropriately will create an economy around protecting and promoting biodiversity, which is a significant step towards sustainable management. It is estimated that c.$830 billion will need to be invested in this by 2030, which presents a large opportunity for investors. Our theme of 'Investing in Biodiversity' seeks to reflect some of this.

Sourcing Income in a Sustainable Way

Investors have remained relatively cautious in 2023 and many are looking for more stable investments that can deliver consistent income rather than relying on a valuation expansion. Through our theme of Sourcing Income in a Sustainable Way, we have identified solutions that have a stable foundation at the business level and can deliver an attractive dividend, but, they do so in a sustainable way. This way investors can get the benefits of an attractive investment approach which is aligned to their income needs while at the same time supporting a sustainable future.

Social Empowerment and Wellbeing

Social issues such as equality, opportunity, quality of education, clean water, nutrition and sanitation are all growing in importance as society demands more of their stakeholders. The pandemic played a significant role in bringing the social element of corporate behaviours to the fore. Inflation has caused worker bodies to ask for better pay and conditions, and strikes have continued. Opportunities for empowerment through technology and increased access to online education are growing too. Similarly, healthcare has seen major changes through the use of technology and is allowing more remote access to consultations in recent years. For investors, some companies will be better positioned than others to navigate the mounting pressures and potential risks of these issues. Governments, shareholders, employees, consumers and activists are increasingly demanding that companies integrate all social aspects in their business strategy and those that do are likely to benefit in the long run.

Equities

Global equities deserve a neutral allocation, in our view. The global economy is slowing, and some fear a recession, triggered by a contraction in bank lending or other risks. But this should be offset by the tailwind coming from the end of the interest rate hikes, and our observation that sentiment (investor positioning and consensus earnings forecasts) are already quite conservative. The earnings season has shown that even in a slowing economy, there are many companies that can maintain their margins, and we continue to focus on those. In addition, equities' total return can be enhanced by selecting companies with solid dividend payouts. We pay close attention to sector bets and like technology, communications, industrials and consumer discretionary, but this remains a stock-pickers' market. Geographically speaking, Asia remains our largest overweight, but we also maintain a US overweight and a neutral exposure to Europe.

Asia is our largest equity overweight

Asian equity valuations are attractive, with China showing a much bigger discount versus its 5-year average, than other countries do. In addition, we think that Asian earnings should start to see some meaningful upgrades. The positive economic momentum in Asia contrasts with that in the West, and we expect to see the same geographical contrast in earnings momentum in coming months. On the risk side too, Asia arguably looks better than the Western markets. Asian banks are generally well-capitalised, and interest rate policy is not seeing the tightening observed in the West.

Some foreign investors are still overestimating the risk of a U-turn regarding China's reopening and China's renewed focus on growth. For them, there are indirect ways of investing in greater China through ASEAN countries, or through European and US exporters. Our view however is that China's policy change will be sustained, and as growth and earnings continue to pick up, this will translate into better market sentiment, which will bring back investment flows. Hard data already shows that the consumption recovery continues to gather momentum, and we think that with time, the reopening will also bring more job growth and rising wages, which should keep the consumption story going.

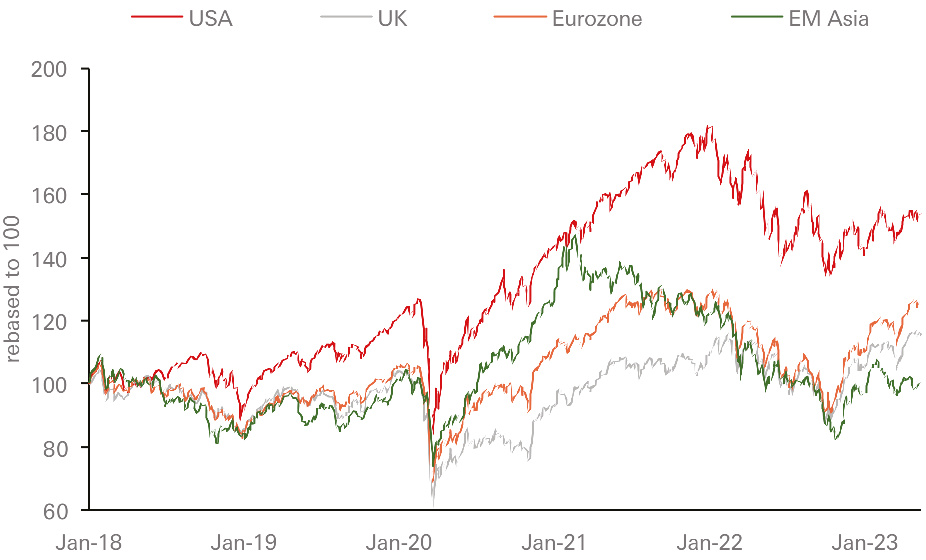
In India, the technology industry has been gaining share throughout, and after the global pandemic. Expectations are that the diffusion of new technologies throughout the old economy should lift growth, productivity and return on capital.

Throughout Asia, key structural trends such as automation, disruptive technologies, the Net-Zero Transition, China's technological self-sufficiency goal and the global supply chain reorientation remain drivers of growth and profitability.

Resilient US

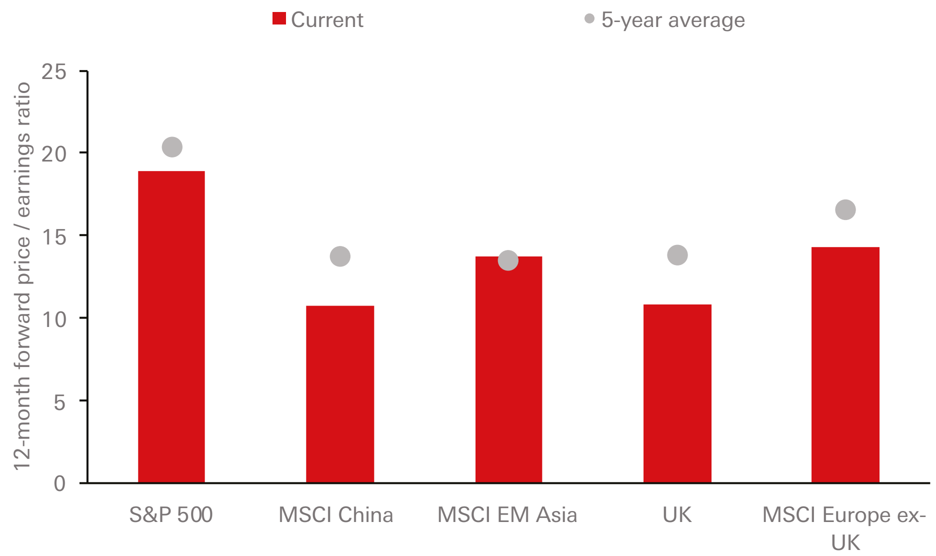
Despite the most aggressive Fed tightening policy since the Volker era, the US labour market remains healthy, the unemployment rate is low, and wages are growing at double the pace of the last business cycle. A growing consensus that the Fed is close to the rate peak – or has already reached it – has boosted equity market valuations and risk appetite. Markets love to look forward, and if inflation continues to fall, as we expect, it would not be surprising that the market starts to factor in more rate cuts, which would be positive for equities. One sector that should perform quite well as rates peak is IT (and, more

Europe has performed well as the economy has avoided a recession



Source: Bloomberg, HSBC Global Private Banking as at 24 May 2023. Past performance is not a reliable indicator of future performance.

Equity valuations are actually not that stretched



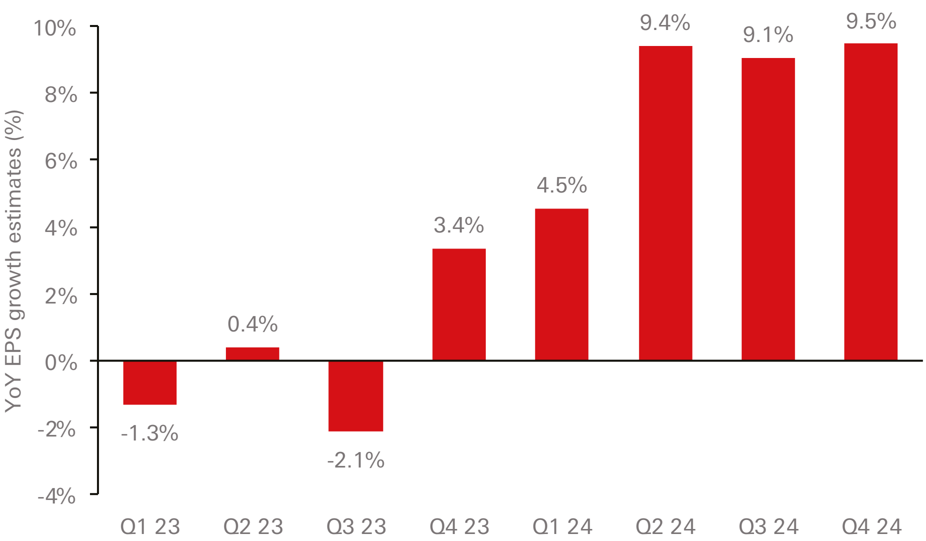
Source: Bloomberg, HSBC Global Private Banking as at 24 May 2023.

generally, growth-style companies), which should also benefit from the increased levels of spending on next-generation technologies that promise to lift profitability and returns on invested capital. Given the large share of tech in the US compared to other markets, this is a clear positive for the US market.

Listed real estate companies on the other hand have gone through many challenges in recent years, and market concern has become even more pronounced lately, so we are underweight on the sector. High interest rates, tighter financial conditions and a weaker economy should keep prospects for real estate muted. The office space in particular suffers from high vacancy rates (22%), which however contrasts with healthier areas such as logistics (closer to 3%). So while we do not believe a systemic crisis is imminent, further mark-to-market risks have led us to reduce exposure to the sector and remain very selective with regard to the specific exposure.

In summary, current valuations seem warranted and the upside to US stocks will probably mostly come from earnings. In the short term, some downward revisions are still possible, but we think earnings will rebound in H2, which should support performance later in the year. As a result, we stick to companies that can best deliver that earnings growth through strong market positions, productivity growth or cost cutting.

S&P500 earnings are set to rebound in 2H 2023 and 2024



Source: Bloomberg consensus estimates, HSBC Global Private Banking as at 24 May 2023.

Europe better than expected

Europe averted a recession and an energy crisis last winter due to better weather. Inflation has remained a bugbear and the ECB continues to sound hawkish. That said, inflation is on its way down, which should give consumers some breathing space, and the pickup in Asian demand is a positive for Europe as well. We hold a neutral stance on the Eurozone but see the potential for more differentiation, with the core (Germany and France) outperforming the periphery (Italy and Spain). This is due to the risk of more stringent bank lending which would hit the periphery more, while Germany and France are well positioned for stronger Chinese and Asian demand.

When comparing Europe to the US, we find it a close call, and while we continue to prefer the US, the gap between our positions has narrowed. The US benefits from a large tech sector, which is doing well, and the fact that it has many quality-style companies (i.e. with dominant positions). Europe on the other hand has lower valuations, and the strengthening euro can add to returns. While the US regional banks pose a risk to performance, the larger US banks have been doing very well and we do not consider the US banking crisis as systemic.

In the UK, we have upgraded our position to neutral allocation. Economic data seem to have bottomed. UK economic surprise indices have been rising recently, and consumer confidence is improving. Moreover, as we get close to the end of the rate hikes, this should support valuations, which are particularly cheap in the UK in our view.

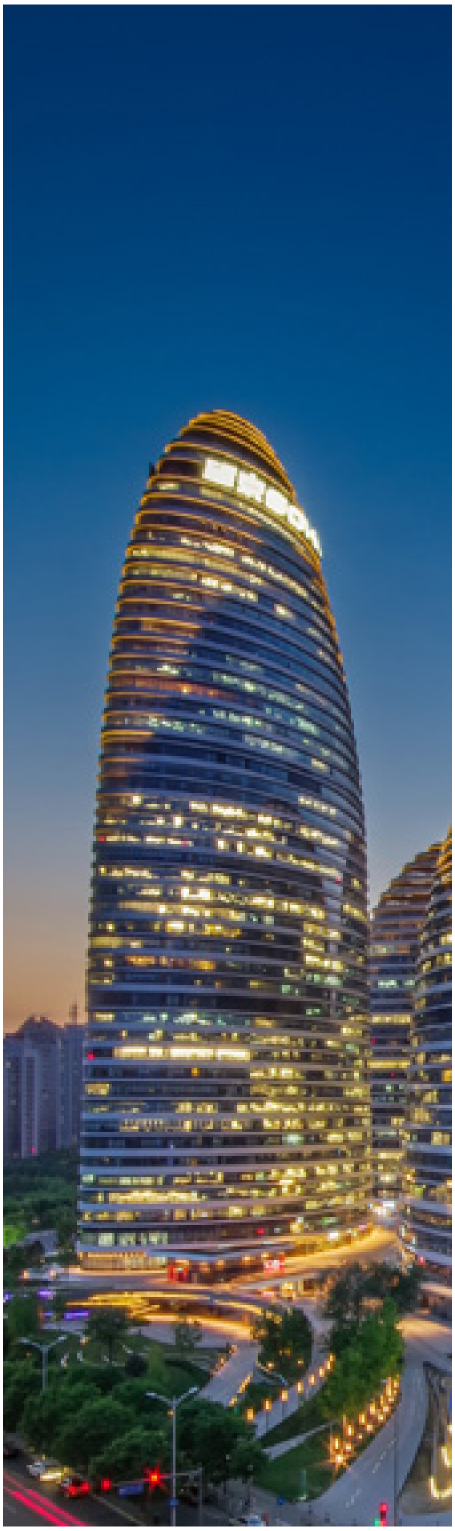
Fixed Income

Markets have been relatively resilient over the past few weeks despite continued concerns surrounding US Regional Banks and tightening DM credit conditions. Rate market volatility has stabilised, albeit at high levels, and low equity volatility has offered a favourable environment for credit markets, especially for High Yield. However, we expect credit spread volatility to pick up in the coming months due to tightening credit conditions, stretched valuations and weakening growth trends. Therefore, we continue to focus on quality corporate credit, mostly in Global Investment Grade (IG) markets and at the "belly" of the yield curve (i.e. medium maturities of 5-7 years). We are selective on EM corporate debt and focus on quality credit and global players. Fixed Income remains our asset class of predilection, on a risk-adjusted basis.

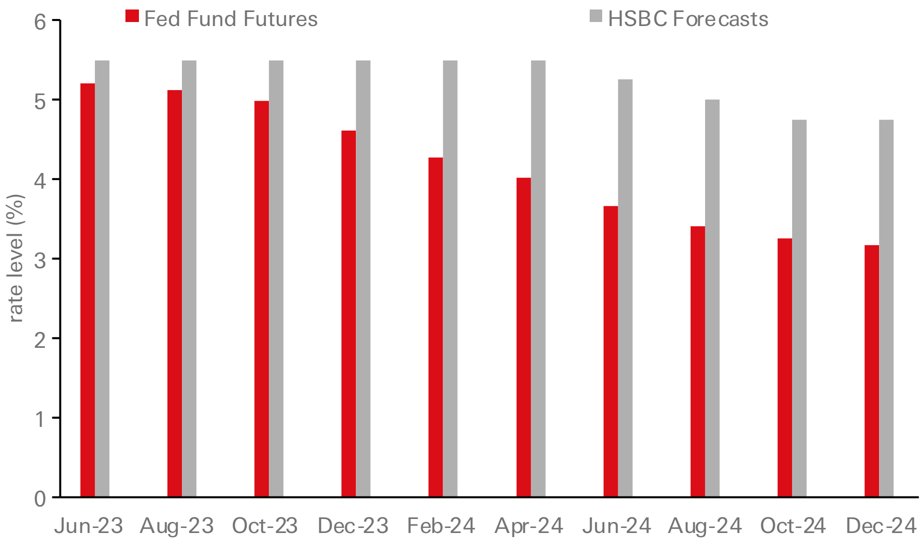
The evolution of the bond market over the past quarter has been twofold:

i. A flight to quality caused by distress in the US and European banking sectors, which pushed down bond yields and tamed policy rate hike expectations.

ii. Improving sentiment since April, as we agree with the consensus that recent credit events in the banking sector should be idiosyncratic and not systemic.



The market is too negative on growth in our view, and therefore prices in rate cuts too early



Source: HSBC Global Private Banking, Bloomberg as at 24 May 2023.

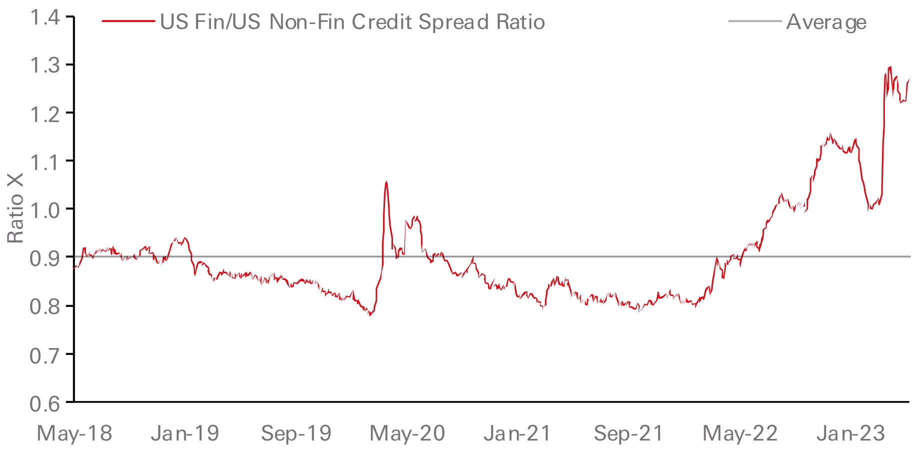
The mild-risk on tone has helped Global High Yield and EM Local Currency debt to perform quite well, while DM bond yield have remained at the bottom of their recent trading ranges. Investors are trying to assess how DM central banks, such as the Fed, will be able to balance their fight against sticky core inflation, while also lending their support to financial stability.

Developed Markets (DM) - Turmoil in the US Regional Banking sector may weigh on economic growth, justifying our view that the peak in DM policy rates is getting closer.

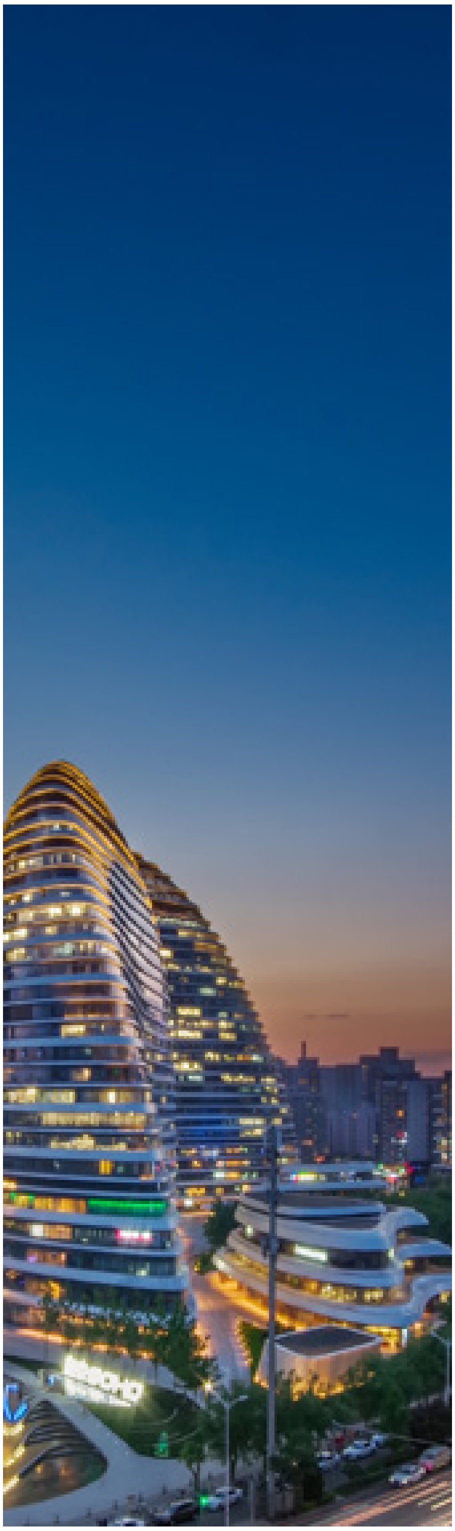
We believe that DM central banks have almost exhausted their rate hike potential, even though core inflation remains sticky and employment generally strong. Central banks cannot ignore the collapse of four US Regional Banks, especially in the context of a slowing economy and already tight financial conditions. Despite the recent low volatility in equity and high yield, investor fear has not dissipated, with concerns focused on US Regional Banks' capital, liquidity and operating models. How Regional Banks realign their business models and how regulation evolves will have a major impact on overall credit formation, and an excessive focus on shoring up liquidity and capital could limit bank lending. In fact, lending was already contracting and the recent Beige Book has confirmed that the banking sector turmoil has made it worse. While a US recession is not our core scenario, we acknowledge that risks have increased.

A recent review led by the Fed following Silicon Valley Bank's demise makes it clear that tighter regulation is coming, with particular focus on managing interest rate and liquidity risks, which

Credit Spread Ratio between Financial and Non-Financial bonds is at post pandemic high



Source: Bloomberg, HSBC Global Private Banking as at 24 May 2023. Past performance is not a reliable indicator of future performance



will affect both sides of banks' balance sheets. Large banks already operate under these regulatory frameworks and the Fed is proposing to extend these rules to smaller banks, with USD 100-700 billion in assets (this would be a reversal of the deregulation applied since 2018-2019). With more than 4,500 regional/small banks in the US, we could expect further sector consolidation, in order to strengthen their capital and achieve sufficient scale. This may result in further tightening of financial conditions for consumers and Small and Medium scale Enterprises (SMEs).

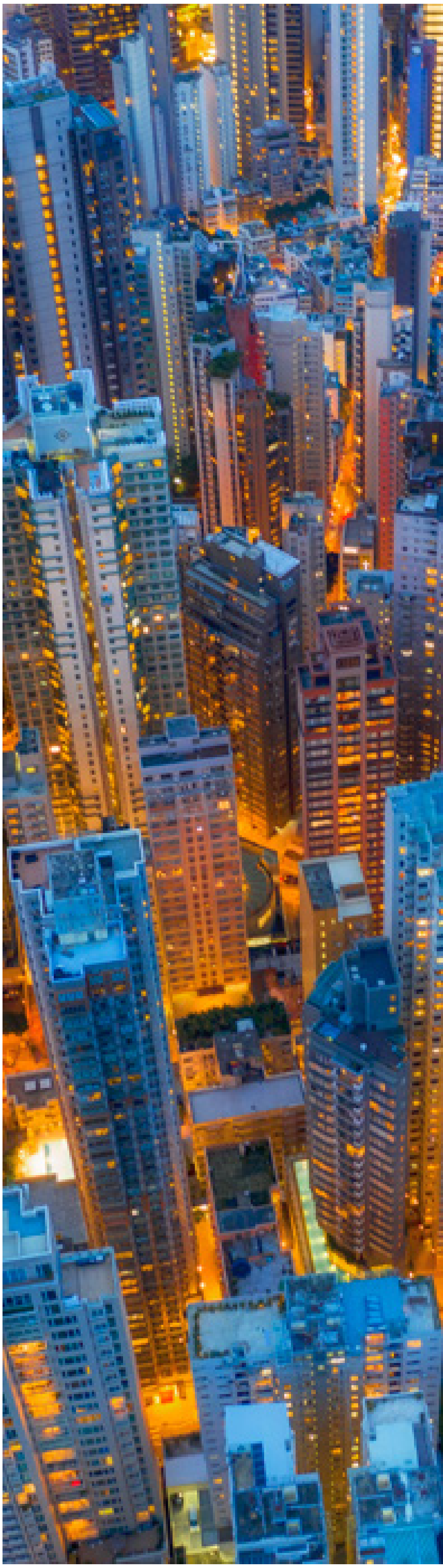
Europe enjoys stronger banking capitalisation and stricter regulations than in the US, even for smaller banks. But the backdrop of tightening credit conditions is similar. The ECB bank lending survey revealed that credit conditions are likely to tighten further due to the magnitude of cumulative rate hikes to date, which will put a brake on loan demand.

Where does it take us in terms of asset allocation across bond markets?

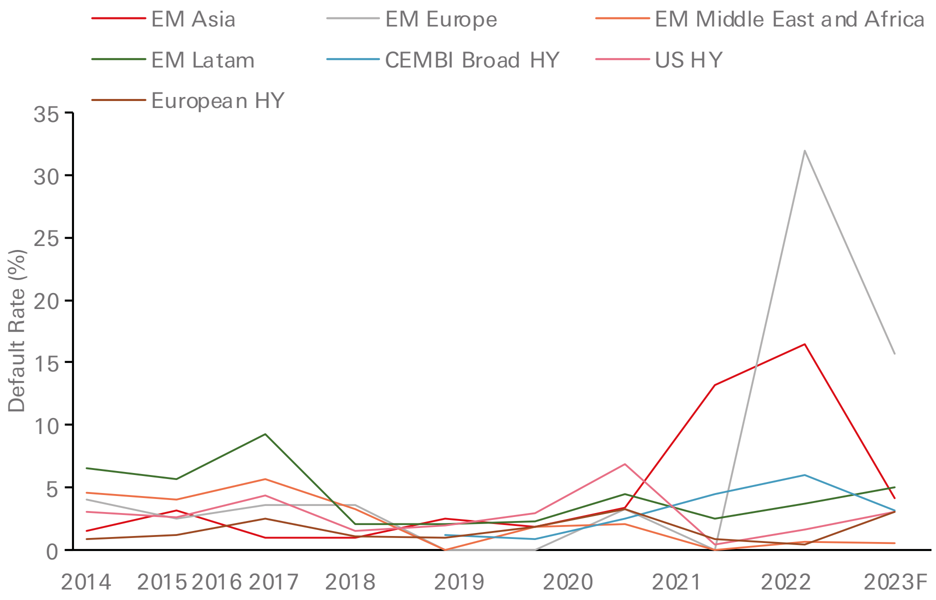
We reiterate our defensive stance by focusing on Global IG markets, at the "belly" of the yield curve (i.e. 5-7 years) and remain selective on EM corporate credit. We increased the average duration target for DM IG credit two months ago, before turmoil in the banking sector triggered risk aversion. That allowed us to lock in attractive yields for a longer period of time and should result in steeper price appreciation if bond yields were to fall in coming weeks or months.

Our call to focus on quality has been put under duress over the past few weeks, as market sentiment has improved and HY has outperformed. We believe, however, valuations in high yield are too tight and do not capture the risk of deteriorating credit conditions and increasing default rates. Thus, we prefer to keep a neutral stance on this sub-asset class.

Sector-wise, we continue to focus on Energy, Technology and Financials. We recognise the banking sector's profitability challenges. However,



EM Corporate HY Default Rate is on track to decline towards US and European levels this year



Source: HSBC Global Private Banking, JP Morgan estimates, 24 May 2023.

this should not materially impact the solid levels of capital and liquidity that the largest DM banks benefit from, as European institutions already comply with the restrictive Basel III Capital Requirements. We believe that subordinated capital instruments (Tier 2, AT1) will remain volatile and subject to idiosyncratic risks in the future. As such, we feel comfortable with financials, mainly the Banks' Senior unsecured debt. Comparing Financial to Non-Financial corporate bonds highlights the attraction of Banks' Senior unsecured securities.

At the corporate level, we continue to focus on quality companies which prioritise bondholder-friendly policies, have sound leverage ratios and lower short-term refinancing needs.

Emerging Markets - A Source of Diversification and Carry

With DM bonds now providing higher yields, appetite for EM bonds has naturally fallen back somewhat. Since the beginning of the year, EM Corporate bonds in Hard Currencies (HC) have slightly underperformed both DM IG and DM HY, providing a total return of 2.4% compared to 3.2% (US IG) and 4.2% (US HY) as of May 8.

Nevertheless, the underperformance was not significant and EM credit fundamentals have remained broadly stable. The EM Corporate HY default rate is estimated at 2.0% as of the end of April. Regionally, the Middle East maintained zero default rates and Asian default rates moderated to only 0.7% given stabilisation among China's property companies. On the negative side, defaults and distressed exchanges have increased among Brazilian issuers, with the default rate for Brazilian corporates reaching 4.1% YTD. This is mainly due to slowing Brazilian growth, still high inflation and tight monetary conditions, which mainly hurts highly leveraged and low margin domestically oriented companies. The credit quality of leading Brazilian companies has significantly improved over the past decade and the majority of Brazilian companies present in the Eurobond market have diversified revenues, positive free cash flows and solid balance sheets. We thus continue to find some select opportunities at current improved valuations.

Overall, we retain an Overweight position in EM corporate bonds in HC, as they provide diversification and good carry for client portfolios. On average, EM corporate bonds have a 7.0% yield, a 4-year duration and an IG rating of BBB. However, our focus is on quality credits mainly from GCC and Asia, where macroeconomic fundamentals are stable or improving. In Latin America, we prefer Mexico for its relative macroeconomic resilience. We see less value at the moment in EM sovereigns and EM LC bonds due to higher potential volatility.

Currencies And Commodities

While Q1 saw a largely directionless USD, the greenback was on a downward path in Q2. Factors that had supported the USD – such as the Fed's policy tightening and global uncertainties – lost their impetus. Indeed, falling inflation has reduced uncertainty and the risk of further rate hikes: we think the Fed is at or close to its rate peak and markets even foresee some rate cuts in coming months. As we move into Q3, we foresee further USD weakness. A narrowing of monetary policy gaps between the Fed and other central banks, coupled with the relatively more hawkish tone of the European Central Bank and the Bank of England, will add negative pressure to the greenback. Additional factors are the softer US economic outlook, the bottoming of global business sentiment and the mild improvement in global risk appetite.

Bullish

In G-10: EUR, GBP, JPY and AUD

In EM: BRL

Neutral

In G-10: CHF, CAD and NZD

In DM and EM: RMB, SGD, INR, IDR, THB, PHP, ZAR, and MXN

Commodities: Gold, Silver, and Oil

Bearish

USD, TRY

Currencies

We believe USD will continue its move down in Q3. Some improvement in the global environment amid reduced risks of persisting inflation is undermining USD. Although the market has long been expecting the Fed to cut rates this year, some stronger-than-expected economic figures (improving PMIs and higher-than-expected nonfarm payrolls) only had a marginal positive impact on USD. In contrast, softer inflation data triggered a sharp sell-off in USD. These reactions indicate that like us, the market is resolutely bearish USD and any renewed weakness in economic figures would weigh on USD. From a monetary perspective, the market is expecting a dovish Fed later this year and even prices rate cuts. By comparison, it sees further hikes in the EU and in the UK. While we think those US rate cuts are premature, these market expectations should weigh on USD and favour EUR and GBP which have long suffered from this USD-positive monetary gap. Besides benefitting from a narrowing monetary gap, we believe EUR and GBP will also benefit from resilient economic drivers and the overall softer greenback.

Meanwhile, China's economic landscape continues to improve despite a soft manufacturing sector and weak global demand. Services and local demand remain strong and GDP growth expectations are encouraging. Still, risk appetite has so far only seen a mild pickup, in part because global investors remain relative absent. Nonetheless, regional peers and trade partners could benefit from this restart as it could improve tourism industries and/or external balances. For instance, we remain constructive on AUD and JPY. We also believe that the monetary policy will be key for JPY as a change in the yield curve control will likely push government yields higher and therefore support JPY.

Although we see only a mild risk-on environment in Q3, we believe countries where we see positive surprises could see some FX appreciation, especially as we have gone through a long period of uncertainty. Therefore, instead of turning bullish on the whole EM region, we are selective on EM and believe currencies offering high yield opportunities still have strong upward potential - hence our bullish outlook on BRL.

Commodities

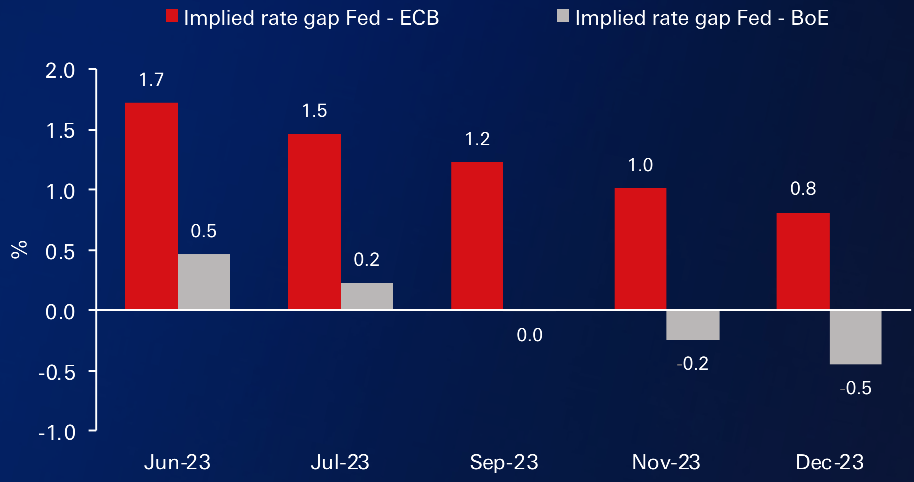
Gold is currently trading at high levels, and has benefitted from the retreat in USD, as well as softer yield expectations. On the other hand, falling inflation and the improved market environment limited physical and investment demand. We believe the gold price will continue to trade sideways, as it is helped by the imminent end of rate tightening in developed markets, but undermined by global yields lingering at high levels.

We expect Silver's physical supply/demand deficit to widen in the coming months, due to stronger demand from the industrial sector. However, like for Gold, we believe non-yielding assets are still going to suffer from high global yields.

The oil market meanwhile is broadly balanced, as OPEC+ is keeping its options open to unwind supply cuts if demand were to increase (e.g. on higher Chinese demand). This should keep the price contained, although the current sector conditions are slightly more tilted to a shortage in supply.

As a result of these points, we maintain our neutral view on gold, silver and oil.

The market expects the rate gap between the Fed and the ECB & BoE to fall, triggering further USD weakness

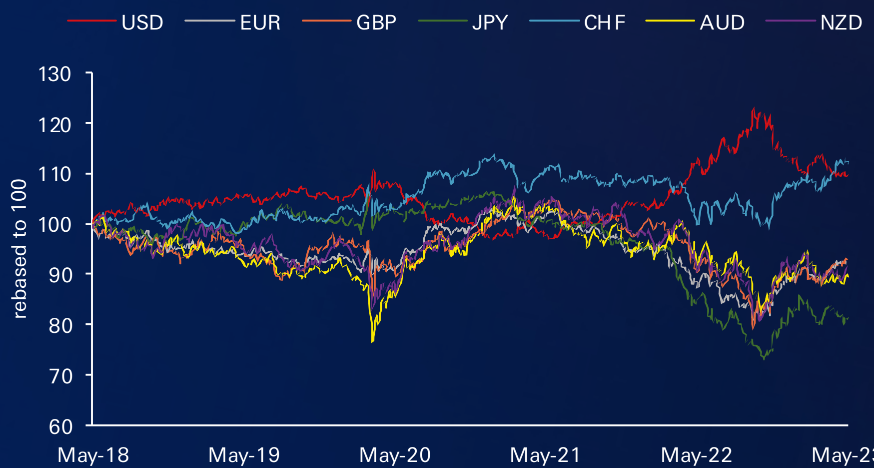


Source: Bloomberg, HSBC Global Private Banking as at 24 May 2023.

The gold price is close to its 5-year high as USD has weakened

Source: Bloomberg, HSBC Global Private Banking as at 24 May 2023. Past performance is not a reliable indicator of future performance.

The soft USD is one of the main factors in G-10 currencies' recent appreciation



Source: Bloomberg, HSBC Global Private Banking as at 24 May 2023. Past performance is not a reliable indicator of future performance.

Hedge Funds

Hedge funds proved their value last year as they protected portfolios against deep losses in equities and bonds. As global risk appetite has improved this year, hedge fund returns have bounced too, and a nimble and diversified hedge fund portfolio should continue to do well. We focus on diversification of strategies, and favour 1) discretionary macro managers, 2) equity market neutral strategies, 3) equity / long short strategies with low net exposure or focused on Asia, 4) structured credit and 5) multi-strategy, multi-manager approaches.

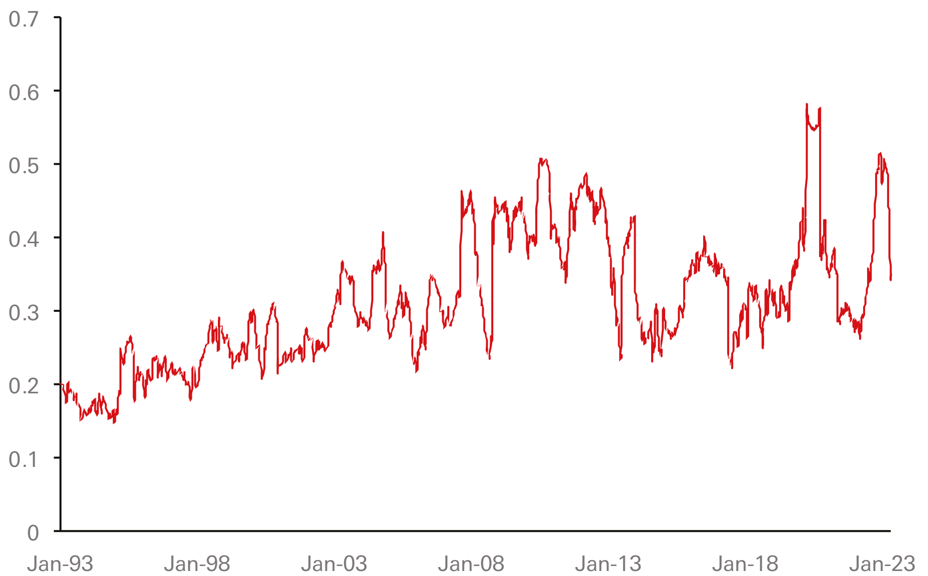
During 2022 hedge funds delivered a close to flat return, but this compared well to bond or equity returns, amid a very challenging market backdrop. The equity rally and improved risk appetite so far this year have boosted hedge funds, while strategy performance leadership has evolved, with equity long/short managers showing marked gains.

The US bank failures, concerns over tightening lending standards, the fall in rate expectations and heightened volatility during the month of March served as a strong reminder that investors need to adjust positions regularly. Discretionary macro managers that were positioned for a hawkish path by the Fed gave back some performance within their rates books. Trend-followers lost money on short positions in fixed income but those managers owning long duration risk assets such as equity long/short strategies with a technology bias enjoyed their day in the sunshine.

What does this all mean going forward for allocators of multi-strategy hedge fund portfolios? Firstly, that strong risk management principles are key, but this was tested with generally satisfactory results within Macro and Multi-Portfolio Manager (PM) strategies. Secondly diversification is also key – both within hedge fund investment solutions and across broader multi-asset investment solutions. This has not gone unnoticed by allocators who added to hedge funds as they saw the value in their portfolios highlighted in 2023.

Our positive outlook for discretionary macro managers is maintained and underpinned by several factors. Continued uncertainty over the interest rate picture, the number of hikes as well as its impact on inflation expectations and growth creates opportunities for managers. While the very elevated fixed income volatility temporarily proved problematic for some macro managers in March, it has since come back down from its highs. Equity market volatility as proxied by a 20-30 range on the VIX continues to be supportive for position taking for the strategy.

Risk on / Risk off indicator



Source: HSBC Global Private Banking, Bloomberg, Refinitiv Datastream, as at 24 May 2023. The correlation indicator measures the strength of the correlations between such assets as equities, credit, rates, FX and commodities.

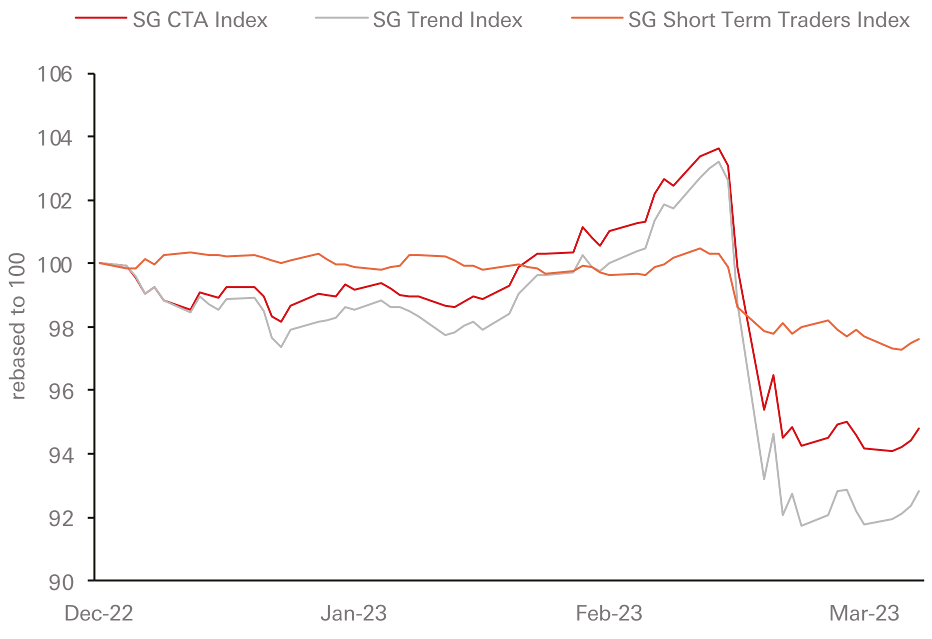
We maintain our views on systematic strategies. For managed futures allocations our neutral outlook is predicated on observations that a prevalence of both long and short-term trend across asset markets is notoriously difficult to predict. Within this strategy set, we maintain a bias towards alternative markets which tend to operate with higher barriers to entry. For equity market neutral strategies our mildly positive view is supported by an acknowledgement of a continuation of higher-than-average stock price dispersion within asset selection. We continue to feel that managers with scale continue to operate with an advantage due to increasing set up costs..

Within equity long/short we delineate our outlook between low net and variable net approaches. By geography we separate out Asia from rest of world reflecting the composition of the underlying universe in the region. Given the prevailing and our forecast market environment for risk assets over the coming 6 months we apply a mildly positive forecast for low net approaches. We are less constructive (mildly negative) on the outlook for variable net strategies. Asia's mildly positive outlook is premised on supportive valuations and a greater degree of freedom for regional monetary/fiscal policy.

Two observable drivers during the first quarter of 2023 which impact the opportunity set for our event driven managers are the evolution of corporate activity over the period and the incidence of activist campaigns. For the former global M&A activity collapsed to 10-year lows during Q1 2023, falling 44% YOY, which is a reflection of hibernating capital markets. This was tempered by a surprising quantum in the number of activist campaigns. Within credit, most sub-components improved during the quarter – particularly loans, but carry still looks interesting. The default cycle is still ahead of us but predictions for the incidence of defaults indicates an opportunity set coming down the track. We maintain our neutral outlook for event driven as a whole and for most credit approaches barring structured credit, where we are mildly positive.

We maintain our positive view for the operating environment for Multi-Strategy, Multi-PM strategies, the majority of which weathered the volatility well during the month of March, delivering positive returns over the first quarter. Looking forward, opportunities in macro and systematic equity market neutral sub strategies may lead returns over the coming quarters.

Trend-Followers whipsawed during Q1 2023



Source: HSBC Global Private Banking, SocGen, as at 24 May 2023. Past performance is not a reliable indicator of future performance

Private Markets

Despite macroeconomic headwinds, we maintain our belief that the Private Equity market remains well positioned for long-term growth and outperformance of public markets. Fundraising remains strong across Europe and larger, high-quality managers are still hitting their full fund allocations amidst more caution and selectiveness from LPs. Exits have slowed in 2023 as GPs remain patient for conditions to improve, but this has helped the secondary market thrive. Despite portfolio NAV markdowns, PE has held a strong outperformance vs public equity markets. Overall, we maintain high conviction for the private equity asset class for investors looking to deploy capital and continue to emphasise the importance of investing with best-in-class managers.

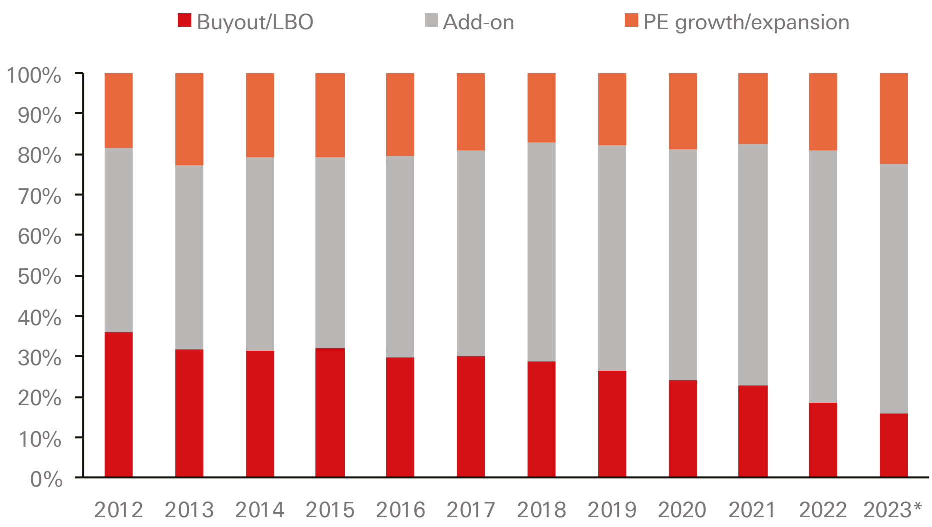
Fundraising has been fragmented in 2023 to date. The story has been positive for Europe so far, but more muted in the US. Many LPs continue to act with caution when making new commitments amidst a market where slower distributions, higher borrowing costs and a continued denominator effect has led to constraints on capital. This is evident when analysing the breakdown of funds raised, as the number of US and European funds that have raised $1bn+ in Q1 2023 has increased by 70.5% when compared with 2022, indicating that investors have been favouring large, high quality, experienced managers.

investors have been favouring large, high quality, experienced managers in Q1 2023

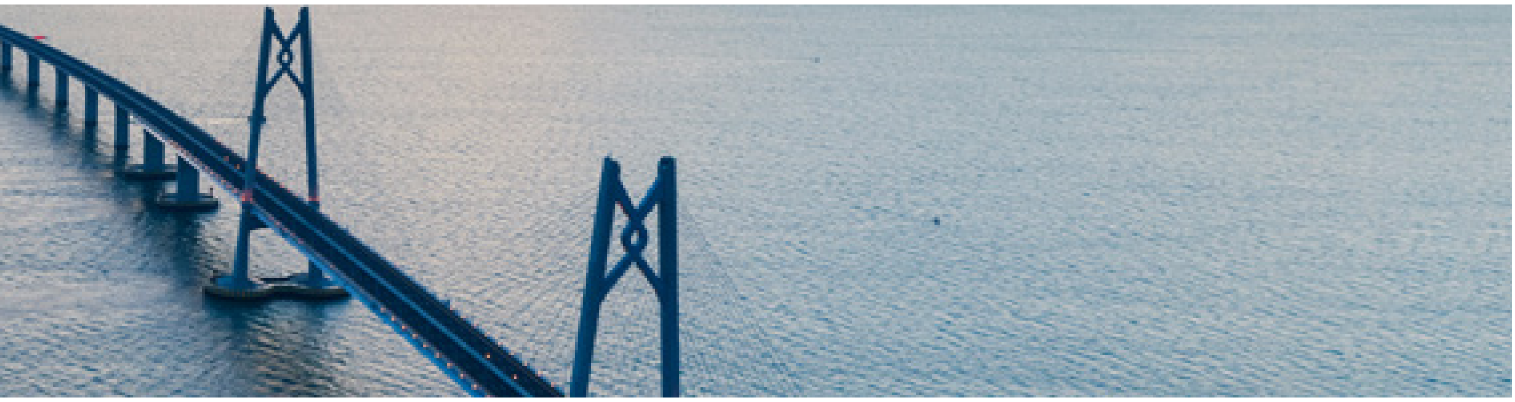
Dealmaking throughout Q1 and Q2 has delivered mixed results so far. In the US market, Q1 2023 deal count was down 9.3% from the last quarter, whereas overall deal value increased by 11.4% from Q4 2022. The story was similar in Europe with Q1 deal value and deal count down by 8.7% and 3.7% respectively, QoQ. A trend across both markets is that PE managers have had to adapt to the more challenging macroeconomic back drop by reducing deal sizes to make them easier to finance and more digestible. At the very top, "megadeals" of $1bn+ have dropped significantly compared with 2022. This trend is consistent when looking at the types of deals that are being executed. Growth equity and add-on transactions, which typically are smaller than Buyouts and LBOs, accounted for 84.1% of US deals in Q1 2023, compared with pre-COVID levels of 73.5%. Looking ahead, though, we believe that the heightened volatility, dislocation and disruption in global markets will provide favourable deployment conditions for opportunistic and distressed manager strategies.

Investors have been favouring large, high quality, experienced managers in Q1 2023

PE Fund count by size (US and EU)



Source :HSBC Global Private Banking, as at 24 May 2023

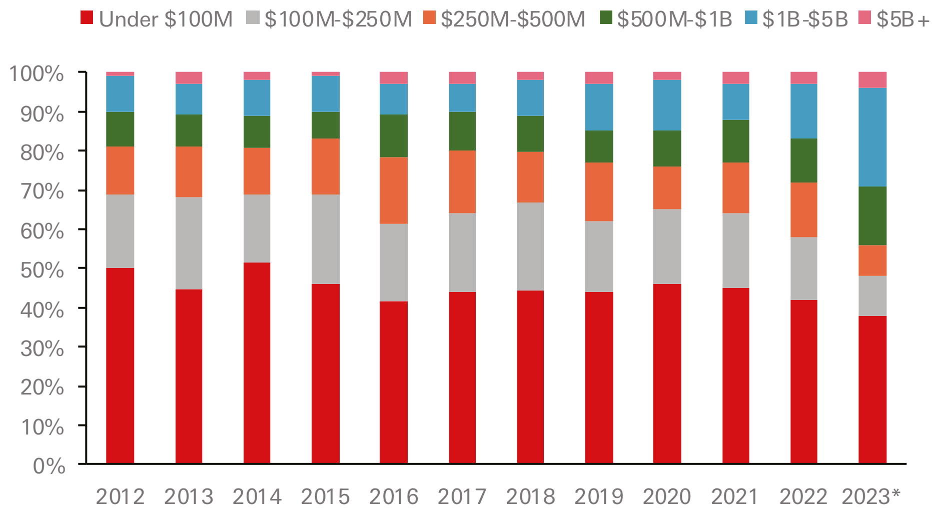


PE **exit** activity has had a quiet start to 2023, particularly in the US market where Q1 2023 has seen both overall exit value and number of exits decline by 31.6% and 30.5% respectively, QoQ. At a global level, GPs have faced adverse valuation adjustments caused by persistent inflation and higher rates creating less favourable sale environment. But a benefit of Private Equity as an asset class is that managers can be flexible with their exit strategies and do not have to become forced sellers. This has held true so far in 2023, with many GPs choosing to hold on to portfolio assets and remaining patient until the exit environment improves.

The **secondary market** is one area that has continued to benefit from the slowdown in primary exit routes, and this comes after two record deployment years. In 2010, just over a decade ago, there was c.$10bn in secondary transaction volume, but this was $132bn in 2021 and $108bn in 2022, and the pace should be similar in 2023. One reason for the increased activity is pricing, with many secondary deals now being agreed at larger discounts to par compared with 2021, as sellers are having to adjust their expectations to include larger risk premiums to factor in volatility and macro uncertainty. Other drivers include an increased need for liquidity from LPs and a desire from GPs that are fundraising to demonstrate distributions, increasing demand for both LP and GP-led transactions.

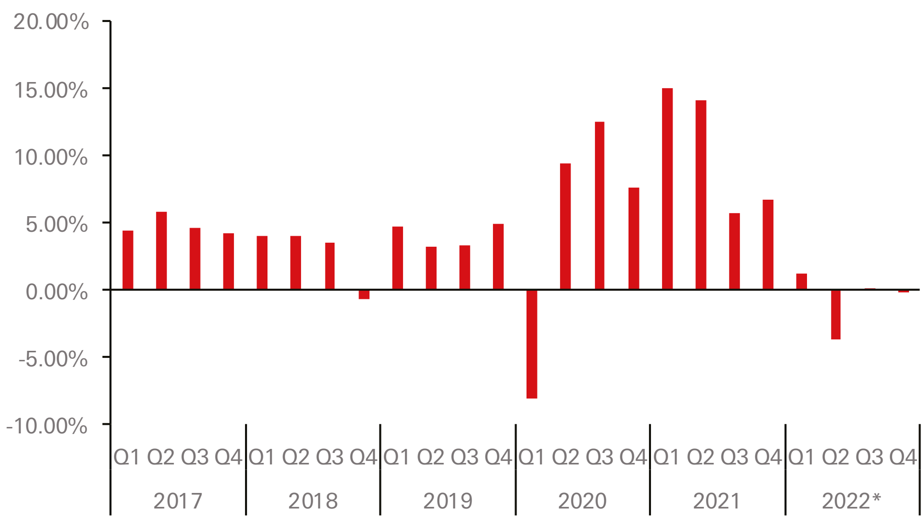
Global PE **performance** was more subdued in 2022 compared with prior years. Preliminary data is estimating -0.2% for Q4 2022 resulting in FY22 performance of 3.1% (including preliminary data for Q4), a notable outperformance of the MSCI World Index which came in at -18.1% for 2022. Factors hindering recent PE performance include increased borrowing costs as well as PE assets being re-rated downward using higher discount factors leading to portfolio NAV markdowns. Geographically, the European PE market has been most resilient, returning 3.3% in 2022, followed by 2.9% in the US and -2.3% in Asia.

Breakdown of PE by transaction type (US): the decline of Buyouts and LBOs



Source: HSBC Global Private Banking, as at 24 May 2023.

Quarterly PE Return (gross IRR) has been subdued in 2022 versus previous years



Source: HSBC Global Private Banking, as at 24 May 2023. Past performance is not a reliable indicator of future performance

Real Estate

Higher interest rates continue to push up property yields and put downward pressure on property values. The gap in price expectations between potential buyers and sellers remains wide. So far, there have been few distressed sellers, though this is expected to increase as a wave of loans require refinancing. Still, property occupier fundamentals remain relatively robust for now (except for the office sector), with high occupancy, limited new supply, and in place rents below market rents in a number of sectors, particularly logistics. Given the long-term importance of income return, we favour sectors with high occupancy and strong thematic demand drivers, including logistics, residential and alternative sectors such as life sciences and self-storage. We maintain our negative view on offices.

The sharp increase in interest rates is pushing up property yields, though unlike other more liquid asset classes, such as equities and bonds, it is taking longer for property yields (and capital values) to adjust. The difficulty in accurately assessing market value reflects real estate's relative lack of liquidity and transparency. Asset valuations are typically based on comparable transactional evidence, but given the wide divergence between buyer and seller price expectations, transactional evidence is in short supply.

Investment activity slowed considerably in the second half of 2022, and this decline in momentum has continued into the early months of 2023 as, for many sectors/geographies, the property yield spread over the risk-free rate of return is historically low. Moreover, with the all-in cost of debt (which includes the lender's margin) higher than property yields, debt investors are not active at current property yield levels. According to data from RCA, global investment in Q1 2023 was the weakest first-quarter figure since Q1 2012. Globally, investment activity in Q1 2023 was 46% below the 10-year average, with the decline most significant in Europe (-58%), followed by North America (-40%) and Asia Pacific (-37%).

For now, there is little distress in the market as tenants pay their rents and landlords make their loan repayments on time. However, as investors look to refinance at significantly higher interest rates than expiring loans, and with lower capital values stretching loan-to-value covenants, a growing number of assets may need to be put up for sale. Still, for now, we do not expect a wave of distressed sales of the same magnitude experienced during the global financial crisis of 2008/09 when the collapse of the subprime mortgage market in the US lead to a freeze in lending. Today loan-to-value ratios are lower and lenders have been willing to work with investors, often extending loans by 2-years, rather than taking back the buildings.

Whilst values have been declining in most markets, the speed of decline has been most notable in the UK. MSCI's UK monthly property index shows that between June 2022 and February 2023, capital values declined by 21%. However, the March data release indicated capital values edged up, albeit by just 0.2%. As a result, from a pricing perspective, the UK looks relatively attractive.

Elsewhere, capital value declines have so far been less significant. MSCI data for the US indicates that values have been marked down by around 10% to the end of Q1 2023, whilst in continental Europe, declines have been between those in the UK and the US. Values have been most resilient in Asia, though this is predominantly due to the ongoing low interest rate environment in Japan. The new governor of the Bank of Japan has suggested this policy will, for now at least, be maintained.

In contrast to investment markets, property occupier fundamentals remain relatively robust for now, except for the office sector, with high occupancy, limited new supply, a positive impact from rental indexation in many markets, and in place rents below market rents in a number of sectors, providing the potential for increases in net income upon lease renewal.

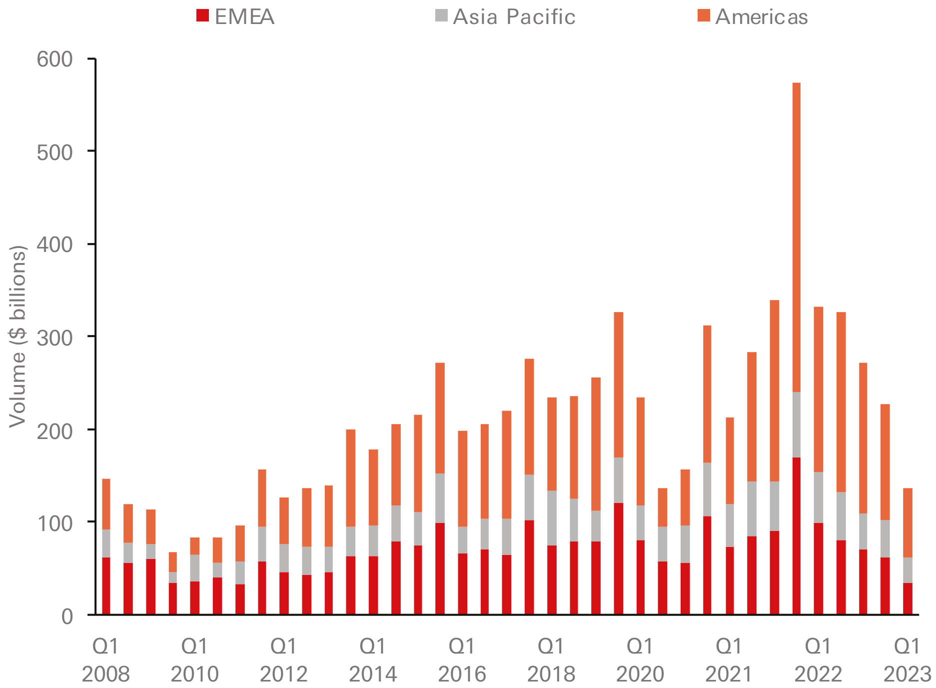
Nevertheless, despite robust occupier fundamentals, we expect further capital value declines as the yield gap between property and government bonds remains historically low – though the wide spread over recent years was artificially widened by quantitative easing. Furthermore, higher interest rates are expected to eventually hit the real economy, which may impact property fundamentals and forward-looking rental prospects.

Whilst the overall outlook for direct real estate is challenging, performance will vary by geography and sector and opportunities are likely to arise for investors able to take advantage of any market dislocation. Moreover, it is important to note the importance of income. For example, in both the UK and the US the income return has accounted for between 65% and 70% of total return over the long run, according to MSCI. Looking ahead, those sectors with the highest occupancy and strongest thematic demand drivers should deliver the strongest returns.

Logistics remains a favoured sector as occupancy remains elevated and, due to recent rental growth, many markets have in-place rents that are significantly below market levels. Other sectors demonstrating high occupancy and thematic tailwinds include residential and alternative sectors such as life sciences and self-storage.

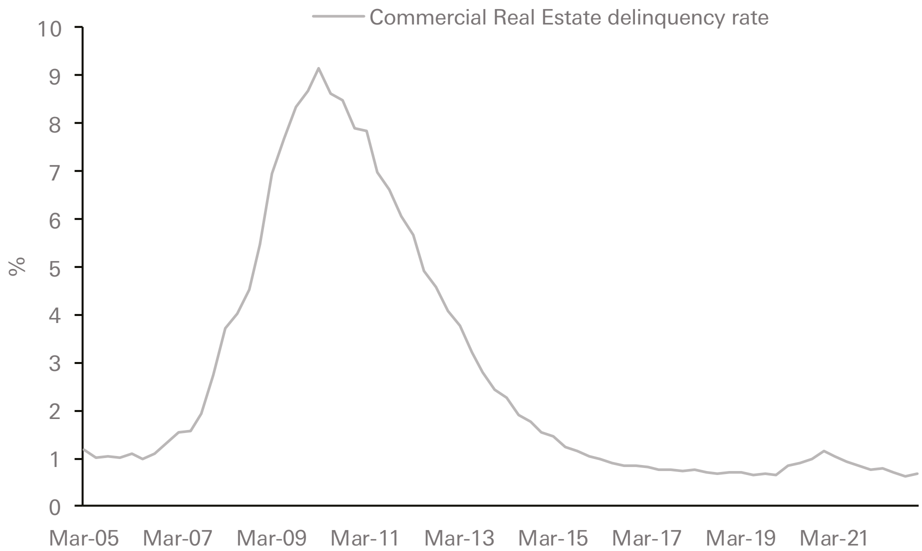
We retain our most negative conviction for offices, as tenants reduce their space requirements due to the shift to remote working, and retrenchment among technology and banking sector occupiers has worsened the situation. Additionally, recent Artificial Intelligence (AI) developments pose a significant threat to white-collar jobs as routine and repetitive tasks increasingly become automated.

Low real estate investment volumes limit price discovery, but we foresee further price downside



Source: RCA, HSBC Global Private Banking as at 24 May 2023.

Although real estate has faced structural challenges for several years, delinquency rates are currently very low



Source: Federal Reserve, HSBC Global Private Banking as at 24 May 2023.

Risk Disclosures

Risks of investment in fixed income

There are several key issues that one should consider before making an investment into fixed income. The risk specific to this type of investment may include, but are not limited to:

Credit risk

Investor is subject to the credit risk of the issuer. Investor is also subject to the credit risk of the government and/or the appointed trustee for debts that are guaranteed by the government.

Risks associated with high yield fixed income instruments

High yield fixed income instruments are typically rated below investment grade or are unrated and as such are often subject to a higher risk of issuer default. The net asset value of a high-yield bond fund may decline or be negatively affected if there is a default of any of the high yield bonds that it invests in or if interest rates change. The special features and risks of high-yield bond funds may also include the following:

- Capital growth risk - some high-yield bond funds may have fees and/ or dividends paid out of capital. As a result, the capital that the fund has available for investment in the future and capital growth may be reduced; and
- Dividend distributions - some high-yield bond funds may not distribute dividends, but instead reinvest the dividends into the fund or alternatively, the investment manager may have discretion on whether or not to make any distribution out of income and/ or capital of the fund. Also, a high distribution yield does not imply a positive or high return on the total investment.
- Vulnerability to economic cycles - during economic downturns such instruments may typically fall more in value than investment grade bonds as (i) investors become more risk averse and (ii) default risk rises.

Risks associated with subordinated debentures, perpetual debentures, and contingent convertible or bail-in debentures

- Subordinated debentures - subordinated debentures will bear higher risks than holders of senior debentures of the issuer due to a lower priority of claim in the event of the issuer's liquidation.
- Perpetual debentures - perpetual debentures often are callable, do not have maturity dates and are subordinated. Investors may incur reinvestment and subordination risks. Investors may lose all their invested principal in certain circumstances. Interest payments may be variable, deferred or cancelled. Investors may face uncertainties over when and how much they can receive such payments.
- Contingent convertible or bail-in debentures - Contingent convertible and bail-in debentures are hybrid debt-equity instruments that may be written off or converted to common stock on the occurrence of a trigger event. Contingent convertible debentures refer to debentures that contain a clause requiring them to be written off or converted to common stock on the occurrence of a trigger event. These debentures generally absorb losses while the issuer remains a going concern (i.e. in advance of the point of non-viability). "Bail-in" generally refers to (a) contractual mechanisms (i.e. contractual bail-in) under which debentures contain a clause requiring them to be written off or converted to common stock on the occurrence of a trigger event, or (b) statutory mechanisms (i.e. statutory bail-in) whereby a national resolution authority writes down or converts debentures under specified conditions to common stock. Bail-in debentures generally absorb losses at the point of non viability. These features can introduce notable risks to investors who may lose all their invested principal.

Contingent convertible securities (CoCos) or bail-in debentures are highly complex, high risk hybrid capital instruments with unusual loss-absorbency features written into their contractual terms. Investors should note that their capital is at risk and they may lose some or all of their capital.

Changes in legislation and/or regulation

Changes in legislation and/or regulation could affect the performance, prices and mark-to-market valuation on the investment.

Nationalisation risk

The uncertainty as to the coupons and principal will be paid on schedule and/or that the risk on the ranking of the bond seniority would be compromised following nationalization.

Reinvestment risk

A decline in interest rate would affect investors as coupons received and any return of principal may be reinvested at a lower rate. Changes in interest rate, volatility, credit spread, rating agencies actions, liquidity and market conditions may have a negative effect on the prices, mark-to-market valuations and your overall investment.

Risk disclosure on Dim Sum Bonds

Although sovereign bonds may be guaranteed by the China Central Government, investors should note that unless otherwise specified, other renminbi bonds will not be guaranteed by the China Central Government.

Renminbi bonds are settled in renminbi, changes in exchange rates may have an adverse effect on the value of that investment. You may not get back the same amount of Hong Kong Dollars upon maturity of the bond.

There may not be active secondary market available even if a renminbi bond is listed. Therefore, you need to face a certain degree of liquidity risk.

Renminbi is subject to foreign exchange control. Renminbi is not freely convertible in Hong Kong. Should the China Central Government tighten the control, the liquidity of renminbi or even renminbi bonds in Hong Kong will be affected and you may be exposed to higher liquidity risks. Investors should be prepared that you may need to hold a renminbi bond until maturity.

Alternative Investments

Hedge Fund - Please note Hedge Funds often engage in leveraging and other speculative investment practices that may increase the risk of investment loss. They can also be highly illiquid, are not required to provide periodic pricing or valuation information to investors, and may involve complex tax structures and delays in distributing important information. Alternative investments are often not subject to the same regulatory requirements as, say, mutual funds, and often charge high fees that may potentially offset trading profits when they occur.

Private Equity - Please note Private Equity is generally illiquid, involving long term investments that do not display the liquid or transparency characteristics often found in other investments (e.g. Listed securities). It can take time for money to be invested (cash drag) and for investments to produce returns after initial losses.

Risk disclosure on Emerging Markets

Investment in emerging markets may involve certain, additional risks which may not be typically associated with investing in more established economies and/ or securities markets. Such risks include (a) the risk of nationalization or expropriation of assets;

(b) economic and political uncertainty; (c) less liquidity in so far of securities markets; (d) fluctuations in currency exchange rate;

(c) higher rates of inflation; (f) less oversight by a regulator of local securities market; (g) longer settlement periods in so far as securities transactions and (h) less stringent laws in so far the duties of company officers and protection of Investors.

Risk disclosure on FX Margin

The price fluctuation of FX could be substantial under certain market conditions and/or occurrence of certain events, news or developments and this could pose significant risk to the Customer. Leveraged FX trading carry a high degree of risk and the Customer may suffer losses exceeding their initial margin funds. Market conditions may make it impossible to square/ close-out FX contracts/options. Customers could face substantial margin calls and therefore liquidity problems if the relevant price of the currency goes against them.

The leverage of a product can work against you and losses can exceed those of a direct investment. If the market value of a portfolio falls by a certain amount, this could result in a situation where the value of collateral no longer covers all outstanding loan amounts. This means that investors might have to respond promptly to margin calls. If a portfolio's return is lower than its financing cost then leverage would reduce a portfolio's overall performance and even generate a negative return

Currency risk – where product relates to other currencies

When an investment is denominated in a currency other than your local or reporting currency, changes in exchange rates may have a negative effect on your investment.

Chinese Yuan ("CNY") risks

There is a liquidity risk associated with CNY products, especially if such investments do not have an active secondary market and their prices have large bid/ offer spreads.

CNY is currently not freely convertible and conversion of CNY through banks in Hong Kong and Singapore is subject to certain restrictions. CNY products are denominated and settled in CNY deliverable in Hong Kong and Singapore, which represents a market which is different from that of CNY deliverable in Mainland China.

There is a possibility of not receiving the full amount in CNY upon settlement, if the Bank is not able to obtain sufficient amount of CNY in a timely manner due to the exchange controls and restrictions applicable to the currency.

Illiquid markets/products

In the case of investments for which there is no recognised market, it may be difficult for investors to sell their investments or to obtain reliable information about their value or the extent of the risk to which they are exposed.

Environmental, Social and Governance ("ESG") Customer Disclosure

In broad terms "sustainable investments" include investment approaches or instruments which consider environmental, social, governance and/or other sustainability factors to varying degrees. Certain instruments we classify as sustainable may be in the process of changing to deliver improved sustainability outcomes.

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