New Growth Engines for a Changing World

Investment Outlook

Q1 2025

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Q1 2025.

Issued on 21 November 2024

Investment Outlook

Discover domestic resilience in an evolving Asia

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Welcome

Dear client

The past few months were dominated by US election uncertainty, which left investors in limbo but still allowed equity markets to rally. Markets are happy that they know the result and can now plan ahead. And although the new administration's policies bring uncertainty on the domestic policy, trade and fiscal front, the result is seen as positive for US risk assets. On other fronts, we have more clarity too. Most notably, it has become clear that the US is not on course for a recession: its steady GDP print resembles a super tanker that will be difficult to blow off course.

Risks to the world's second biggest economy (China) are now tilted to the upside thanks to a big pivot towards fiscal and monetary stimulus (even though the path is complicated by the risk of higher tariffs). The world's most populous country (India) meanwhile benefits from strong cyclical and structural growth. It is also clear that the major Western central banks are all on a rate cutting path that should continue, while lower inflation gives consumers some breathing space. And corporate earnings have continued to surprise to the upside, proving that many companies have benefited a lot from innovation, and have suffered less from high rates than many expected.

Clarity is good for investors as it can reduce risk premia and support valuation multiples. In our view it will also help trigger more investment by the private sector, which should be a key engine of growth. Many companies are sitting on cash which they will be happy to put to work, while others will take advantage of lower borrowing costs to invest. More M&A and more share buybacks will boost shareholder value and support stock markets.

Most governments do not have the healthy balance sheets of the corporate sector, but they share the view that they must innovate and invest to grow in a competitive world. Many of them have therefore formulated detailed and ambitious industrial policies with fiscal support and deregulation as the main instruments. We see this as a second important engine for growth and investment opportunities. Manufacturing and advanced technologies tend to be a priority for those industrial policies as they are viewed as strategic and even a matter of national security – they should therefore be a key area of opportunities for investors. They will also require investment in infrastructure, especially in digital and electricity.

All of these growth engines power opportunities under our thematic trends, including Disruptive Technologies, Climate Action and Evolving Society. Moreover, the continued global economic momentum and the multiple engines create many opportunities in both public and private markets.

Following two years of solid returns for well-diversified portfolios, we think there is further scope for attractive returns. We therefore continue to keep cash balances in our model portfolios at a minimum. We continue to see better opportunities in the US than in Europe, due to relative levels of current growth, innovation and policy support. Despite increased trade uncertainty after the US elections, we expect Asian growth to stay resilient in 2025 with the support of robust domestic growth in India and ASEAN, together with China's widening policy stimulus. We focus on resilient domestic leaders in Asia, where we hold overweight positions in India, Japan and Singapore's stock markets. We think a positive cyclical course has been set, and attractive structural trends are in place. The increased clarity will be reassuring for investors, we believe, supporting investment flows and asset returns. Our four priorities going into 2025 are:

1. Capture earnings tailwinds from policy priorities and innovation
2. Fight falling cash rates with multi-asset and active fixed income strategies
3. Build out core allocation to private markets and hedge funds
4. Discover domestic resilience in an evolving Asia

Willem Sels,
Global Chief Investment Officer

21st November 2024

Our Portfolio Strategy

We believe the global risk environment is constructive: we are at a favourable point in the global growth cycle, developed market central banks continue to cut rates, and companies successfully use innovation and cost control to grow earnings. What's more, additional engines of growth including industrial policies, AI applications, M&A and Chinese stimulus should add to the market momentum and to the opportunity set in 2025. So, we maintain our mild overweight on global equities, while continuing to build our allocation to alternative assets. We believe equities will outperform bonds, and bonds will outperform cash. Sitting on excess cash is likely to once again be a drag on performance.

Cash: Underweight

Fixed Income: Mildly underweight

Neutral on most of the global bond markets

Underweight on Japanese government bonds

Equities: Mildly overweight

Overweight US, UK, Japan, India and Singapore

Underweight Europe ex-UK, EM EMEA and Latin America

Alternatives: Overweight

Overweight hedge funds and gold

Core allocations to Private Markets and Infrastructure

The world around us: cyclical and structural picture

To assess the market outlook for 2025, it's important to first examine the state we are currently in. Economists have time and again been too cautious on US economic growth, overestimating the value of economic indicators (such as yield curve inversion or the Sahm rule) and underestimating both the US consumer and technological innovation. While the US growth rate is clearly off the peak, it should remain close to 2% and well out of recession territory. Tax cuts and deregulation under President Trump should be a further boost to consumption and investment.

Meanwhile in China, there is a clear realisation that exports can no longer be a reliable growth engine given the headwinds from trade tensions and tariff risks under the new US administration. Monetary and fiscal stimulus will continue to be ramped up to boost domestic demand and mitigate those trade challenges. Further policy stimulus will put a backstop to Chinese growth and create potential upside when more decisive demand-side stimulus is delivered. India meanwhile continues to see strong growth, while the reflation trend in Japan continues. So even with the diverging outlook in Europe (where the UK's resilience contrasts with a weak Germany), the global cycle looks healthy.

Central bank actions add to the tailwinds. In developed markets, inflation is now close to target, so interest rates can continue to be normalised from the current restrictive levels to a more neutral setting (balance sheet reduction can slow too). In turn, the Fed cuts should give more breathing space for emerging market central banks to also cut where their local inflation picture allows it. If there is any risk here, we think it is the potential for stronger-than-expected US data (further boosted by tax cuts and deregulation) to cause markets to flip-flop between the 'soft landing' and 'no landing' scenarios: this would lead to volatility in the rate expectations and hence the need for a tactical and active investment approach. It is also worth monitoring the effect of changes to immigration policies, tariffs and fiscal spending on the Fed's policy, but we don't think the Fed will halt or reverse rate cuts till at least mid-2025.

As we try to paint a picture of the world around us, we also need to incorporate some structural forces in addition to the cyclical ones. This is where our top trends come in, which we hope most

Multiple engines boost growth and create a wide opportunity set

How we see the world	Engines of growth	Investment implications
Low global recession risk	Industrial policies support manufacturing	Excess cash should be a drag on performance
Rate cuts and mild inflation in developed markets	Fiscal spending prioritises critical investment	Equities should outperform bonds
More clarity post US elections: a Republican clean sweep	AI enables accelerated innovation	Data-driven bond market requires an active investment approach
Increased focus on national security	M&A and buybacks lift shareholder value	Balance cyclicals and defensives, favour GARP
Healthy corporate and household balance sheets versus high government debt	Real income growth boosts consumption	We focus on domestic leaders in Asia to withstand trade uncertainty
Disruptive technologies trend	China stimulus reboots domestic growth	Rich opportunities in hedge funds, private markets and infrastructure
Climate action trend	Tariff overhang accelerates Asia's intra-regional trade and investments	
Evolving society trend		

readers are familiar with. We discuss our 'Disruptive technology', 'Climate action' and 'Evolving society' trends in the following chapters. The practical investment implications are developed in our high conviction themes.

Two more forces will be key in 2025. First, the complex geo-politics, ranging from outright conflict to challenges for the old globalised and multi-lateral model. Countries are increasingly focused on national security – whether that be the protection of their manufacturing base, energy security or physical security. Second, the build-up of debt on the government side, which contrasts with the private sector's healthy balance sheets and has profound implications. It means that governments need to focus on limited strategic priorities if they don't want to wake up the bond vigilantes, while households and corporates have much more scope to spend and invest, which we think they will.

Rebooting the growth engines

As our table on the previous page illustrates, this picture of the world helps discover how the different economic players are likely to act in 2025.

With the US elections just behind us, there is a lot of focus on government policy, in terms of domestic and trade-related industrial policy, and in terms of fiscal priorities. Following the election of Mr Trump as the next US President, with control of Congress, the US priorities are likely to include trade protectionism, re-onshoring, technological leadership, deregulation and energy independence. Manufacturing activity is hugely competitive around the world and is going to be best supported in countries where there are strong industrial policies. This includes the US, Japan, China and also India, which is surging as a new manufacturing hub. By comparison, the lack of a coordinated industrial policy in Europe and its failure to cut the red tape to unlock the necessary funding will be an obstacle to manufacturing in the EU.

To support manufacturing and boost re-onshoring, infrastructure investment has become more of a strategic focus, as the US Inflation Reduction Act and the recent UK budget illustrated. Electricity is a priority in many countries, given the energy-intensity of our data-led world, and because energy independence is seen as a national security imperative. As more governments borrow to invest, we see this as an additional growth engine in the coming years.

Corporates will welcome tax breaks and other incentives that help them innovate. We think AI will continue to cause a wave of small incremental innovations in almost every company, and a smaller number of big innovations across sectors. AI is not just about chips, but also about the enablers and the applications. Corporates will also use their cash balances and their ability to borrow at cheaper rates to create shareholder value through increased buybacks and M&A. All these actions have the potential to further increase earnings per share and support equity markets.

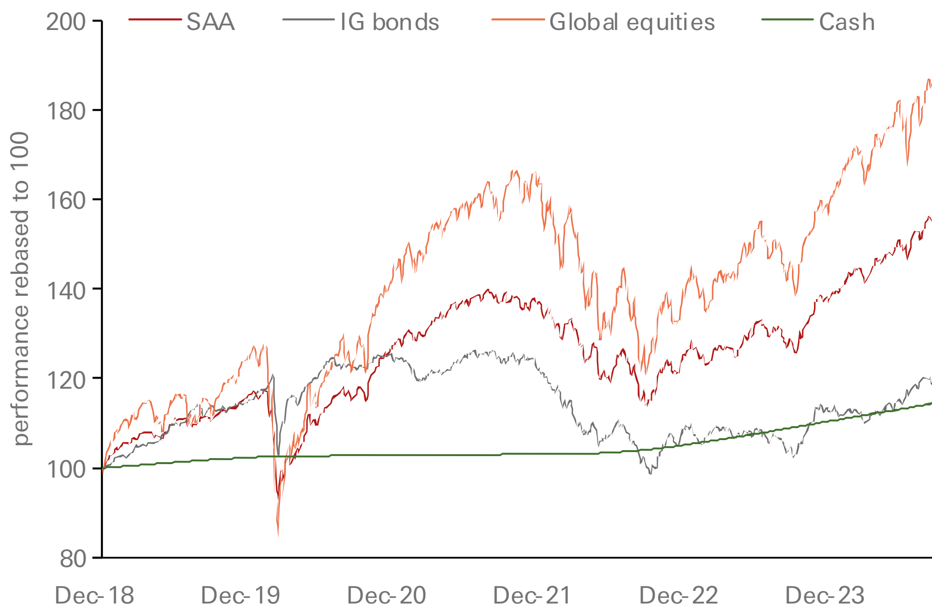
Last but not least, consumption growth should be healthy, as the fall in inflation boosts real consumer incomes. A period of price stability should lead to improved consumer confidence, while falling mortgage rates, rising house prices and stock markets should all help too. Lower-income consumers will remain discerning and price sensitive, but many households should have more to spend, including the retired population, which is responsible for an interesting 'Silver economy'.

Investment implications

Given the healthy cyclical starting point and the many growth engines that should boost and broaden earnings growth, equities should do well. Excess cash should once again be a drag on performance, especially as rate cuts should continue. We think bond performance will be in between cash and equities: attractive yields can still be locked in, but price gains may be mild, given that the markets already price in Fed rate cuts to 3.75% by end-2025.

That's not to say that investors don't face challenges or uncertainties. In fact, we think investors face three known challenges but believe we can turn them into opportunities. Geopolitics remain complex, but we think we know the industrial and fiscal policies governments will adopt to the new world order. So, we like industrials in the US and Asia but not in Europe, while we see continued growth in IT around the world. In Asia, we favour resilient domestic leaders which are expected to outperform exporters and offer safe havens to withstand trade uncertainty and tariff risks under Mr. Trump's presidency. In China, we favour quality industry leaders which are expected

Diversified portfolio strategies have outperformed cash in 2024 and we think this will continue in 2025



Source: SAA = performance of our moderate risk strategic asset allocation, in USD terms. Bloomberg, HSBC Global Private Banking as at 20th November 2024. Past performance is not a reliable indicator of future performance.

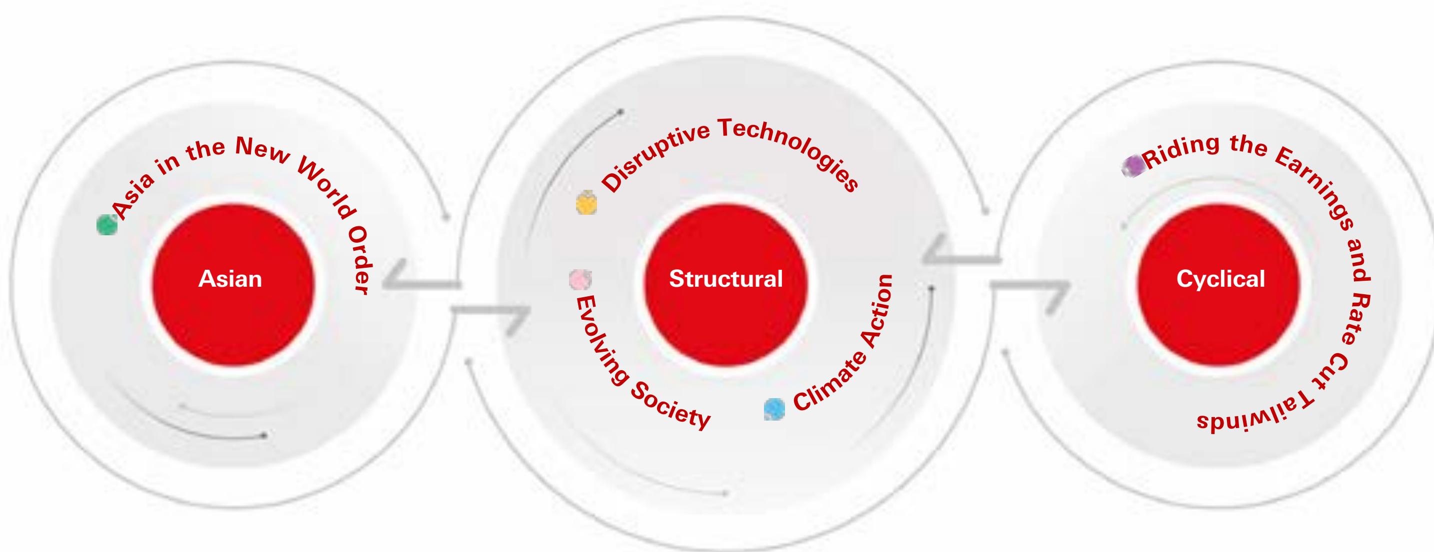
to benefit from further policy stimulus to reboot domestic growth and bolster the high-end manufacturing sectors. And across the world, governments will welcome the involvement of private investors in infrastructure as there is a big need and government funding is limited.

The second challenge for investors is the data-dependency of markets, which may continue as the US economy is on the cusp between the soft-landing and no-landing scenarios. This means a tactical, active or hedge fund approach can help. We also overweight on gold as a diversifier and a tail risk hedge, as our multi-polar world leads some investors to look for alternatives to the USD. We don't think the dollar will be displaced, however. In fact, we hold a bullish view on the greenback, and also see it as a way to manage volatility: history tells us that USD often does well when economic growth is either on the strong or on the weak side (the 'USD smile' feature).

Lastly, we recognise that valuations are not cheap. That's true in the credit space where spreads are tight in high yield but still fair for investment grade. In equities, US valuations are well above average and stocks' upside will thus mainly depend on EPS growth. So we look for companies that can innovate and be well-positioned for structural trends, through our high conviction themes. We also adopt a GARP approach (Growth At a Reasonable Price) as growth stocks should do well, but investors don't want to overpay. As public market valuations rise, we should see more exits in private equity, allowing for more distributions back to limited partners (LPs) and causing more of the dry powder to be put to work. Finally, we continue to look at opportunities to complement our overweight in US stocks with some selective growth leaders in Asia and the UK that offer attractive valuation appeal.

Top Trends for 2025 and High Conviction Themes

Our Top Trends are well established, with three structural trends complemented by a number of themes focused on Asian opportunities, and a shorter-term set of opportunities exploring thematic ways to benefit from earnings potential and rate cuts. The following pages discuss our High Conviction Themes in more details.



Global High Conviction Themes

Asia	Structural			Cyclical
Asia in the New World Order • Asia's Domestic Leaders • Power Up Asian Shareholder Returns • Rise of India and ASEAN • High Quality Asian Credit	**Disruptive Technologies** • Aerospace & Security • Digital Infrastructure • Intelligent Automation & AI • NextGen Medicines	**Climate Action** • Energy Transition • Biodiversity and Circular Economy	**Evolving Society** • Social Empowerment and Well-being • Silver Economy & Demographics	**Riding the Earnings and Rate Cut Tailwinds** • American Vitality • North American Re-Industrialisation • Income Through Active Credit Selection

Source: HSBC Global Private Banking as at 20th November 2024.

Our four investment priorities for Q1 2025

1. Capture earnings tailwinds from policy priorities and innovation

Why? Following the run-up in equity market valuations and with moderate global growth, we need to look for companies with above-average earnings growth potential. We see industrial and fiscal policies, as well as AI innovation as powerful engines of earnings growth.

What? Industrials in the US and Asia should benefit from strong industrial policies. AI-led innovation should boost the global technology sector and themes such as Intelligent Automation & AI and NextGen Medicines. The resulting data-led economy requires much more electricity, supporting our Energy Transition theme. And all of this requires more infrastructure, where we see strong opportunities for investors. To balance the potential for growth with reasonable valuations, we like to take a GARP approach in the US and Asia.

2. Fight falling cash rates with multi-asset and active fixed income strategies

Why? As most major central banks continue to cut interest rates, we think cash will underperform bonds, equities and alternative assets as lower rates help support valuations across assets. Moreover, multi-asset strategies benefit from a strong opportunity set, given the many growth engines for equities, low equity/bond correlations and big dispersion between stocks. Navigating increased rate volatility, active fixed income strategies can generate diverse alpha sources across markets and sectors by tactically adapting to changing market conditions.

What? We take a global approach as we want to limit investors' home bias and tap into the varied range of opportunities in the US, UK, Japan and rest of Asia. Active strategies which use rebalancing and / or active stock and bond selection can benefit from the headline-related volatility we are likely to continue to see under Trump 2.0.

3. Build out core allocation to private markets and hedge funds

Why? More than 85% of US companies with revenues above USD100m are private companies that are not quoted on the stock exchange. As companies stay private for longer, investors need to have private market exposure to capture that attractive growth spurt. Private credit markets tend to generate relatively stable and attractive returns through the cycle, especially compared to public credit markets. Hedge funds have an attractive opportunity set, as volatility and dispersion should remain elevated.

What? We build our allocation to private equity and private credit to add to opportunities that are not available in public markets, add alpha and diversify. We take broad exposure to hedge funds with strong manager selection and a preference for discretionary macro, systematic equity market neutral, Asian equity long/short, multi-strategy and multi-PM managers.

4. Discover domestic resilience in an evolving Asia

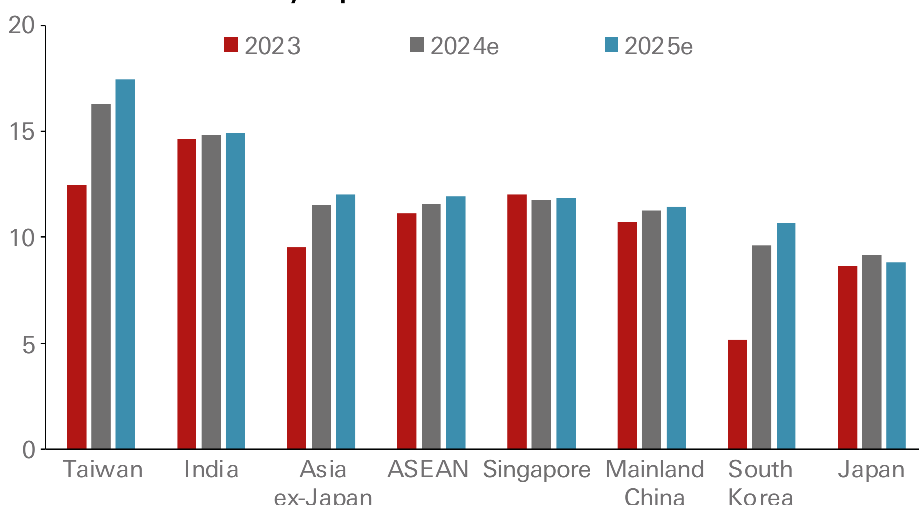
Why? We expect Asia ex-Japan to see 4.4% GDP growth in 2025 despite trade uncertainty, thanks to robust domestic growth in India and ASEAN, coupled with China's broadening policy stimulus. Asia's resilient domestic leaders should outperform exporters, thanks to monetary and fiscal stimulus. The tariff overhang also adds momentum to Asia's intra-regional trade and investments, offering growth opportunities to high-end manufacturing leaders with global competitiveness. Finally, Fed rate cuts create more room for Asian central banks to lower rates that should bode well for quality bonds in the region.

What? Our newly launched theme on Asia's Domestic Leaders focuses on the domestic industry champions which are well positioned to withstand the tariff risks with support of robust domestic growth drivers. In our overweight markets in Japan, India, and Singapore, we find attractive alpha generation opportunities from the domestic growth leaders, which are also captured by the theme on the Rise of India and ASEAN which attaches stronger focus on domestic consumption. We identify beneficiaries from China's policy stimulus, including internet and consumer leaders which can benefit from policy support to boost domestic consumption. Our new theme on Power Up Asian Shareholder Returns positions in quality companies that improve ROE by paying high dividends and increasing share buybacks. To capture the best quality Asian credit opportunities, we stay focused on Asian USD IG corporate bonds, Indian and Indonesian local currency bonds, and Indonesian quasi-sovereign and corporate IG in USD.

Asia in the New World Order

To navigate increased trade uncertainty after the US elections, we focus on discovering domestic resilience and diversification opportunities in Asian equity and credit markets. Our thematic approach identifies winners from durable domestic growth, improving shareholder returns and the structural upswing of India and ASEAN.

Broad-based and steady improvement of Asian markets' ROE in 2023-2025



Source: Bloomberg, HSBC Global Private Banking as at 20th November 2024.

Our Four High Conviction Themes	
1. Asia's Domestic Leaders	We favour Asia's quality companies which rely on domestic demand and have limited exposure to the US market. In mainland China, Hong Kong and Japan, we find attractive alpha generation opportunities from the domestic leaders with strong competitive position and earnings potential that's above their sector average. In China, we like quality internet stocks, select domestic travel plays, and consumer leaders.
2. Power Up Asian Shareholder Returns	This theme looks for resilient and defensive equity returns by positioning in quality companies that enhance ROE by paying high dividends or increasing share buybacks. Consensus estimates forecast Asia ex-Japan's return on equity (ROE) will rise from 11.5% this year to 12% in 2025.
3. Rise of India and ASEAN	We find promising domestic-driven opportunities in India and ASEAN, riding on the secular tailwinds from young demographics, rising middle-class consumers, and technology boom. We attach a stronger focus on domestic consumption winners to mitigate tariff risks.
4. High Quality Asian Credit	Continued Fed rate cuts will create room for Asian central banks to lower rates in coming months. We favour Asian USD IG bonds, Asian financials, Indian and Indonesian local currency bonds, Indonesian quasi-sovereign IG bonds in USD, and select Macau gaming bonds and Chinese TMT issuers.

4.4%

We forecast Asia ex-Japan GDP growth of 4.4% in 2025, well above the global average

59%

59% of Chinese consumers expect an economic recovery within the next 2-3 months

12%

Asia ex-Japan ROE is on steady uptrend from 9.5% in 2023 to 12% in 2025%

6.5%

India and ASEAN economies are should achieve 6.5% average per-capita GDP growth over 2023-2026

Source: McKinsey ConsumerWise Survey, Bloomberg, HSBC Global Research forecasts, HSBC Global Private Banking as at 20th November 2024.

Navigating the fast-evolving geopolitical landscape after the US elections, Asia should sustain resilient economic performance in 2025 with support of multiple growth engines. We believe that robust domestic growth drivers in India and ASEAN, together with China's widening policy stimulus, will drive durable Asia ex-Japan GDP growth of 4.4% in 2025, well above the global average of 2.6% growth. Lingering trade uncertainty under the Trump administration may trigger more demand-side stimulus from China in 2025 to mitigate the external challenges. India and ASEAN continue to benefit from structural tailwinds of young demographics, rising middle-class consumers, strong foreign and domestic private investment flows, and the technology boom.

Our newly launched theme on Asia's Domestic Leaders focuses on regional industry champions which rely on domestic demand and have limited exposure to the US market. Asian companies with high exposure to intra-regional trade and cross-border investments are better positioned to mitigate the US tariff risks in the months ahead. In mainland China, Hong Kong and Japan, we find attractive alpha generation opportunities from the domestic leaders with strong competitive position and above sector average earnings potential to withstand trade headwinds.

In China, we favour domestic leaders with a strong national brand franchise, healthy balance sheets and a competitive edge, as they are poised to benefit from policy stimulus. We like quality internet stocks, select domestic travel plays, and consumer leaders. According to McKinsey's latest ConsumerWise survey, 59% of Chinese consumers expected their economy will recover within the next 2-3 months (compared with just 41% in the US and 30% in the UK). In Japan, the sustained reflation trend and bumper wage hike bode well for domestic consumption companies. These resilient Asian domestic leaders should act as relative safe havens to withstand tariff risks, and they are expected to outperform exporters that focus on the US market

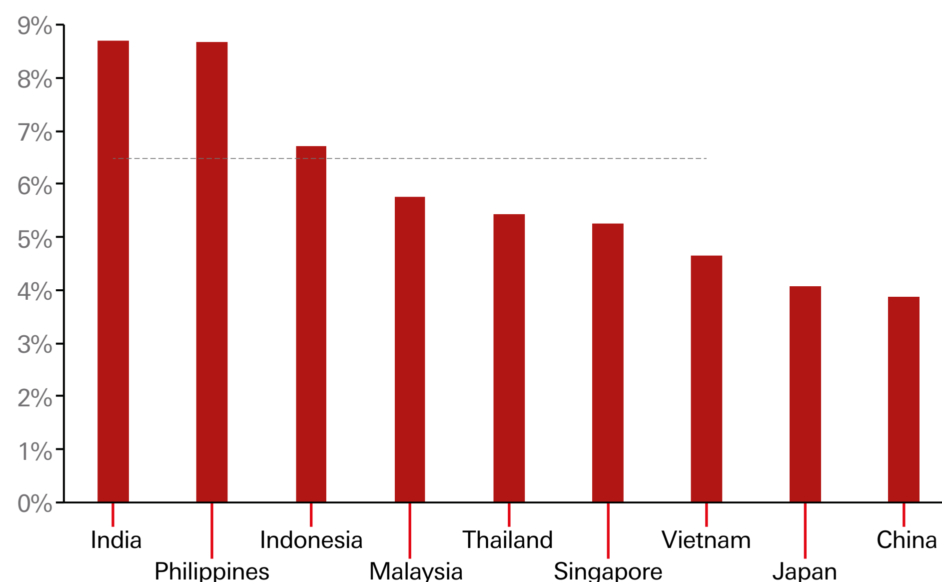
Positioning for an uncertain external environment, our new theme on **Power Up Asian Shareholder Returns** seeks for resilient and defensive equity returns by positioning in quality companies which enhance ROE by paying high dividends and increasing share buybacks. Consensus estimates forecast Asia ex-Japan return on equity (ROE) will rise from 11.5% this year to 12% in 2025, led by Taiwan at 17.5%, India at 15%, ASEAN at 12% and mainland China at 11.5%.

Solid earnings growth is forecast to drive over 7% growth in dividends in Asia ex-Japan and 9% in Japan in 2025, thanks to positive progress of corporate governance reforms in Japan, China and South Korea. Dividend yields in Singapore and Indonesia at 4.2%; Hong Kong and Malaysia at 3.9% look compelling versus 1.8% globally. We favour quality mainland China SOEs, Hong Kong insurance, telecom and property stocks paying high dividends. Share buybacks in Asia are growing at a record pace, particularly in Japan, mainland China and Hong Kong markets. Notably, the PBoC launched a special relending facility in mid-October for commercial banks to facilitate share buybacks by listed companies and major shareholders. China A-share buybacks hit a record high in 2024, more than double of 2023's total.

Our theme on the **Rise of India and ASEAN** shifts its focus more towards domestic consumption to add resilience against the tariff overhang. The recent pullback in Indian equities presents an attractive opportunity to add exposure as the market remains well supported by 17% 2025e earnings growth, high ROE, and strong inflows from domestic investors. As such, we prefer Indian large caps over small and mid caps due to their relatively attractive valuations and better earnings profile. Within ASEAN, we prefer Singapore equities as the country has a modest trade deficit against the US, making it a defensive play under tariff risks as compared to other regional peers, especially with support of its compelling dividend yield. We see opportunities in financials, consumer, real estate, infrastructure and communication services stocks in India and Southeast Asia.

Continued Fed rate cuts will create more room for Asian central banks to lower rates, which should bode well for quality bonds in the region, supporting our theme on **High Quality Asian Credit**. To capture the best Asian credit opportunities, we stay focused on Asian USD investment grade corporate bonds, Asian financials, Indian and Indonesian local currency bonds, Indonesian high quality quasi-sovereign IG bonds in USD, and select Macau gaming bonds and Chinese TMT issuers.

India and ASEAN economies should achieve 6.5% average per-capita GDP growth over 2023-2026

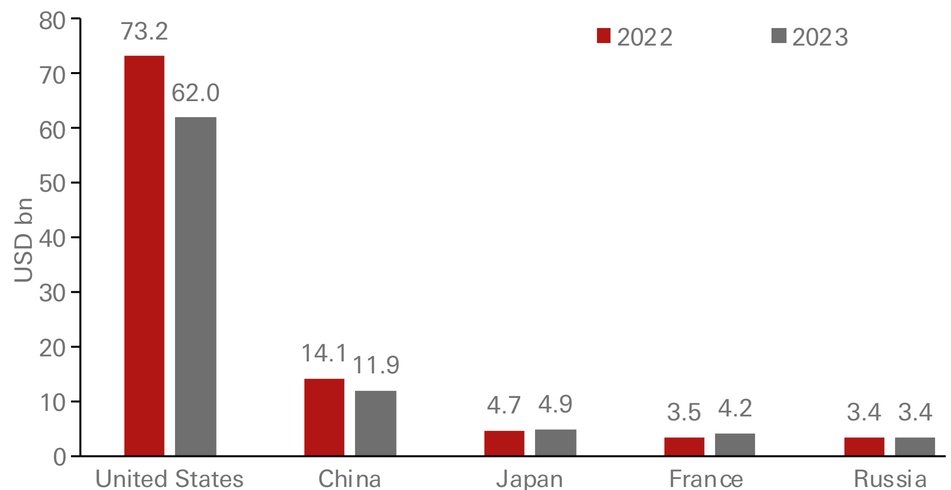


Source: : CEIC, HSBC Global Private Banking as at 20th November 2024.

Disruptive Technologies

Innovation and leading-edge technologies are driving productivity gains, re-shaping the security industry, addressing unmet medical needs causing completely new businesses segments to emerge.

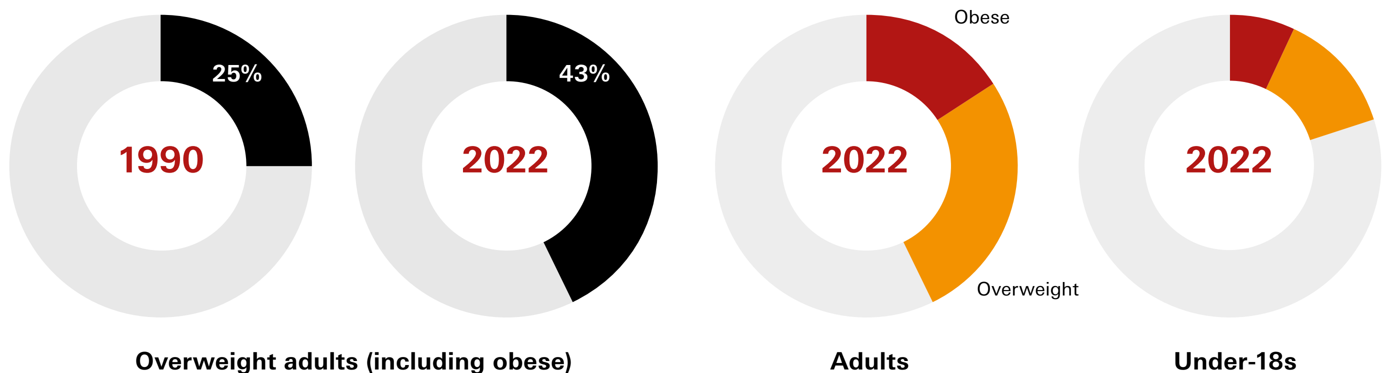
Government expenditure on space programmes



Source: Visible Alpha, HSBC Global Private Banking, 20th November 2024.

Our Four High Conviction Themes	
1. Aerospace & Security	The pace of development is astounding in satellite, space vehicle, rocket and other aerospace technologies. In parallel security concerns are rising in areas such as IP, software, physical and digital infrastructure.
2. Digital Infrastructure	Digital infrastructure capacity is seeing strong demand-driven growth with cloud, data centres, network providers, semiconductor suppliers and equipment manufacturers set to benefit.
3. Intelligent Automation & AI	Companies are racing to embed AI capabilities in products and services to expand their capabilities and boost performance. Enhanced visual and sound recognition systems have multiple applications.
4. NextGen Medicines	Highly targeted new therapies including mRNA vaccines, gene therapies and CAR-T therapies combined with the latest diagnostic and scanning technologies are leading to better patient outcomes and often lower costs.

NextGen Medicines address a weighty worldwide problem



Source: World Health Organisation, 2022; HSBC Global Private Banking as at 20th November 2024.

Adopt & Adapt or Risk Decline

A wave of innovations is reshaping business models, leading industries to rapidly adopt and adapt to the new commercial landscape.

Aerospace & Security

The aerospace renaissance is taking off with advances in satellite, space vehicle, rockets other aerospace technologies all gaining momentum due to various factors. Rockets and unmanned aerial vehicles are receiving particular attention due to recent technological advancements and the accompanying greater capabilities. The commercial aircraft segment has seen less innovation as there a few competitors. In contrast, there have been several ambitious new entrants to the space market as the technologies and costs have become more accessible.

Unsurprisingly, new technologies bring opportunities but also risks. The rise of digitalisation and inter-connectivity has brought new risks particularly relating to security. Commercial and state espionage is an ongoing threat in areas such as intellectual property (IP), software, physical and digital infrastructure where malefactors not only seek information but also control and influence. Recent targeted attacks include government elections; energy infrastructure; hospitals and research establishments.

With this investment theme, we focus on the companies providing these essential equipment and services to these agencies

Digital Infrastructure

This investment theme focuses on the networks, data centres, platforms and technologies that enable the digital revolution. Its importance cannot be overstated. While new technologies are central to the evolutionary process, their transformation capabilities cannot reach their full potential without robust digital infrastructure. Whether that is roving 6G AI-enabled mobile devices or autonomous machines or remote medical robots, all require digital highways, data processing and memory capacity on a global scale to be effective.

For example, an electric vehicle manufactured in China or USA can be sold anywhere in the world. These vehicles often require interconnectivity with digital infrastructure for consumers to fully benefit from all the services and capabilities of its car.

Intelligent Automation & AI

Over the last two years, large language models (LLM) and other AI models have proliferated, and their capabilities have advanced tremendously. The diffusion phase is already well underway with AI software integrated into products and services to provide new and greater capabilities. Commercially, intelligent automation offers potential productivity gains together with safer operating environments for employees. Intelligent automation can provide non-stop continuous service at a consistently high level. As with the ecommerce revolution, those early adopters that fully embrace the potential of AI and deploy it effectively into their operations, products and services will potentially recognise the greatest benefits and competitive advantage. Our investment theme looks to capitalise on these developments and the companies that are well positioned to benefit most from them.

For example, the technology can be used to improve automated telephone answering services; smarter mobile telephones and search engines; expanding use of connected healthcare devices; recycling centre sorting of waste; vehicle driver behaviour change.

NextGen Medicines

The spiralling cost of healthcare in most developed countries is a major cause for concern as the affordability weighs on both government and tax-payers.

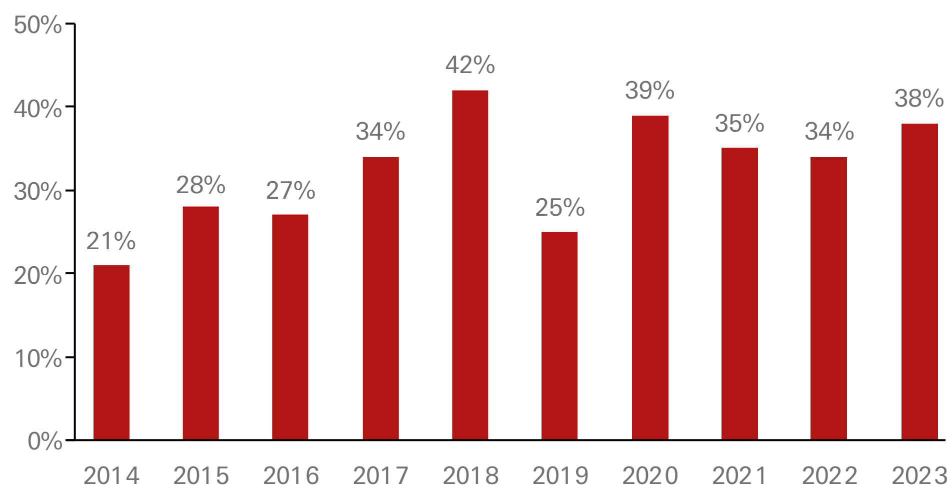
In the US, the world's large healthcare market, YoY costs increases have accelerated with medical plans expected to rise on average by 7.5%-8% YoY in 2025 (source: PWC), well ahead of inflation and salary rises.

This escalating crisis needs radical solutions, and a new generation of treatments may provide part of the solution.

For example, since 1990, human adult obesity has doubled with an estimated 890m people or 1 in 8 classified as being obese and 1.6 billion classified as overweight (source: WHO, 2022). Glucagon-like peptide-1 (GLP-1) drugs are the first mainstream product to offer a treatment for obese patients. While these treatments tend to be expensive, the drug's costs need to compared to the expense of treating the multiple ailments an obese person is more prone to suffer. These include diabetes, cardiovascular disease, high blood pressure and ongoing hospital and ambulatory care over their lifetime.

Similarly, there is substantial scope for mRNA vaccines, gene and CAR-T therapies to transform lives and lower overall long-term medical costs.

Personalised medicines as a percentage of FDA approved new molecular entities

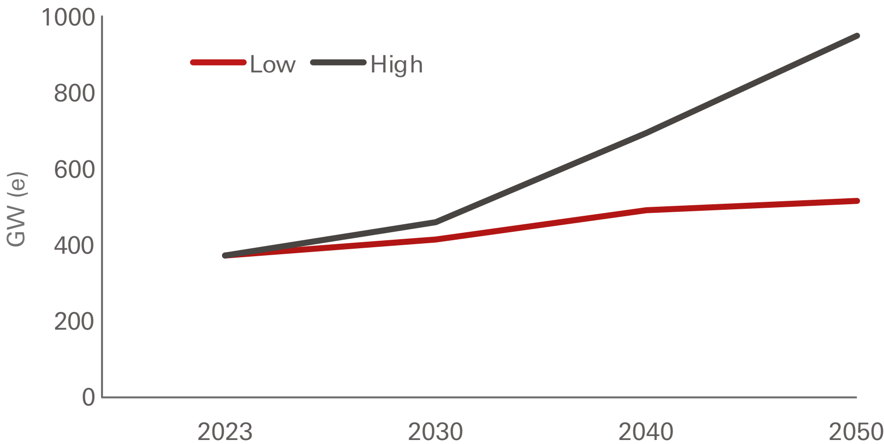


Source: Statista, HSBC Global Private Banking as at 20th November 2024.

Climate Action

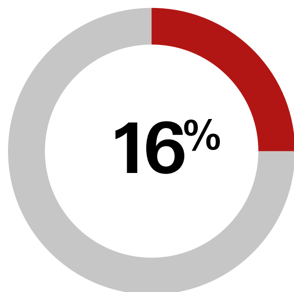
The demand momentum for sustainable or zero carbon products and services continues to present investment opportunities. Recent announcements of nuclear energy deals for energy hungry AI companies shows that sustainability is a key driving force in corporate spend.

Estimated global nuclear energy capacity growth to 2050

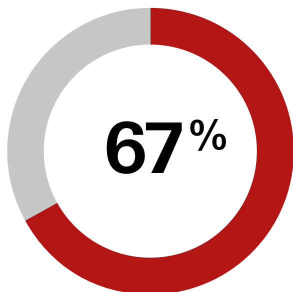


Source: International Atomic Energy Agency. HSBC Global Private Banking, as at 20th November 2024.

Our Two High Conviction Themes	
1. Energy Transition	There has been a marked rise in the desire of global economies to move to lower carbon energy production while also increasing the independence of their domestic energy production. These forces are driving major changes in the energy mix which are also resulting in major changes across grid infrastructure resulting in a global energy transition.
2. Biodiversity and Circular Economy	International bodies have recently developed appropriate quantitative frameworks and measurement tools to measure the impact and exposure of individual companies on natural capital and biodiversity. This is creating a new lens through which investors can identify risks but also seek out opportunity.

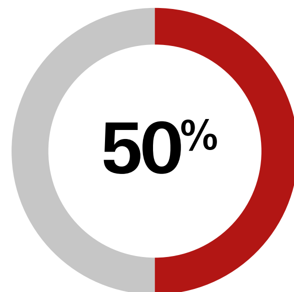


16% of current US electricity demand is related to AI



Renewables and nuclear will account for 54-67% of global electricity production by 2050

Wildlife populations have declined by 73% since 1970



50% of global GDP is connected to natural capital

Source: Forbes, WEF, IEA, Living Planet Index, HSBC Global Private Banking as at 20th November 2024.

The case for sustainability is a relatively clear one when it comes to both the need and the desire for solutions.

Recent natural disasters, abnormal weather conditions and the growing problem of unmanaged waste in water systems and oceans have served to remind us that the need for sustainable offerings is as high as it has ever been. Likewise, though, we are seeing an expanding "want" for sustainable solutions. The arrival of AI this year also brought with it a huge appetite for energy and the companies consuming this energy are looking to zero emission solutions to provide it - with nuclear getting particular interest. Nuclear has grabbed the headlines in recent months as major AI and cloud companies announced partnerships with nuclear energy providers as part of their strategy to obtain carbon free energy to meet their AI energy demand. This energy is available from non-sustainable sources, but they are looking for long term sustainable solutions to meet the need, because their customers demand it.

Energy Transition

Global investments in the low-carbon energy transformation have been rising and topped $1.8trn in 2023. Still, much more investment is needed. The reinvigoration of Nuclear as an option in a sustainable future has opened a path for some major energy consumers to expand investment in this area to add to the energy mix.

Renewable energy adoption has seen a steep rise over the past couple of decades, thanks to rising awareness and policy push but if we were to remove the policy support now, renewable energy would be on course to represent 50% of electricity generation by 2030 according to Bloomberg New Energy Finance. The acceleration of adoption has a compounding effect on technological progress too which can be seen across the space and needs to be accounted for when forecasting the future. The hurdles for a sustainable future are high but they are coming down with every technological step.

Lithium-Ion batteries, for example, integral to mobile phones, laptops, electric vehicles and grid storage fell 90% in cost per kilowatt hour between 2010 and 2023 and they halved in price since 2017, according to BloombergNEF.

Small modular nuclear reactors are another technology being developed that could significantly advance the sustainability agenda. They are designed to be cost effective, portable, easier to manage and quicker to launch. They present an attractive solution for energy hungry industry that wants zero carbon emissions and can't wait for a full-scale nuclear plant. Some of the designs being touted also have hydrogen as an offshoot of the process.

Energy grids will need to be adapted to a more sustainably sourced energy future where the sources of that energy are more disparate and need to be connected.

Biodiversity and Circular Economy

Biodiversity funds have seen their inflows grow over 5X in the last 4 years according to a recent Morningstar report and yet, it is still only early days for the sector. The climate fund market, by comparison, is c.$530bn on a global basis.

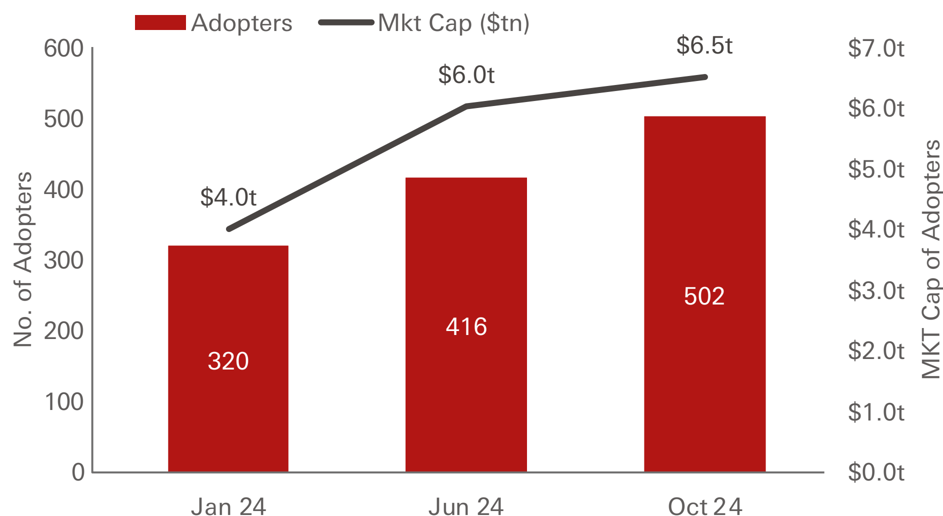
Interestingly, the report highlights three types of funds, ones with companies focused on reducing the risk of biodiversity loss, funds seeking companies that provide solutions to biodiversity loss and funds that are a mix of the two. It is the solution-focused funds that are growing most in 2024.

The Living Planet Index report was also recently updated and it makes for grim reading with an estimated 73% average decline in wildlife populations since 1970. This is often linked to the destruction of habitats where the waste of a linear economy is a major culprit. Circular solutions are needed.

The World Economic Forum has estimated that 50% of global GDP is connected to natural capital but because nature has always been free and its use has not been managed it has led to issues such as overfishing, or river pollution, damaging its value for future generations.

The Taskforce on Nature-related Financial Disclosures developed a set of disclosure recommendations for companies to assess, report and act on their nature-related dependencies, impacts, risks and opportunities. The number of adopters is rising quickly, and this disclosure of companies' biodiversity exposure presents opportunities for investors.

Global growth in adopters of TFND

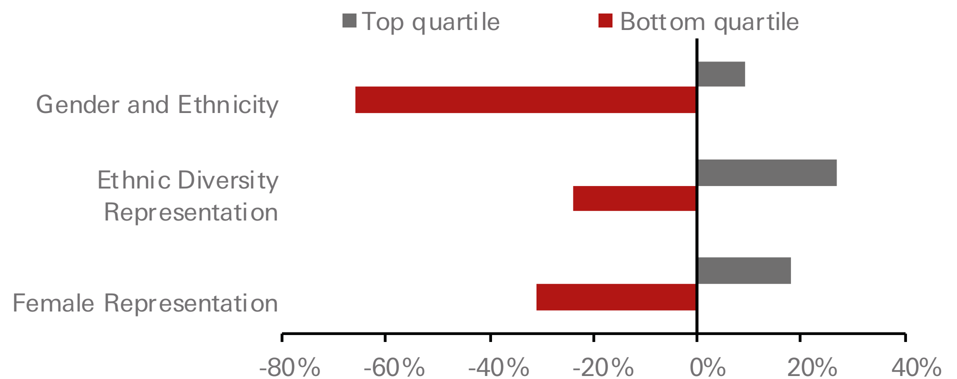


Source: Taskforce on Nature Related Financial Disclosures, HSBC Global Private Banking, as at 20th November 2024.

Evolving Society

Demographic shifts, technological innovation and changes in the way people want to live is driving an evolution of our societies. Our themes reflect two aspects which we think are both durable and have strong investment potential.

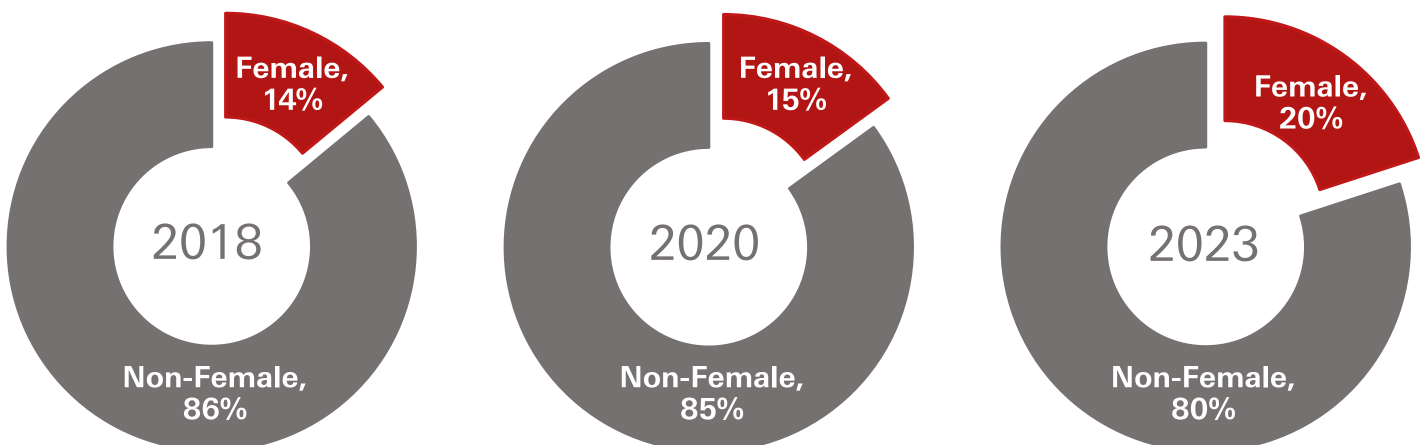
Likelihood of financial performance based on diversity performance



Source: McKinsey, HSBC Global Private Banking as at 20th November 2024.

Our Two High Conviction Themes	
1. Social Empowerment and Well-being	Our theme focuses on gender equality, diversity, female workforce participation, access to quality education and healthcare. This is not just because investors and consumers care about these topics, but also because studies have shown that more diverse organisations tend to perform better.
2. Silver Economy & Demographics	The theme focuses on the investment opportunities that look set to benefit as the world gets older. Demand for health and personal care, assisted living, mobility, security and leisure products and services like travel is in an upward trend that is set to continue for several decades.

Average female representation on executive teams across 23 countries



Source: McKinsey, HSBC Global Private Banking as at 20th November 2024.

Society is evolving across many strands. The age demographics of most societies have been changing for years as birth rates have been falling, while at the same time, people are living longer. Although this change is occurring over a long period of time, the ramifications on society and its economics will be deep and wide. Older people are the richest people in society in aggregate but they have very different savings and consumption patterns.

Society is also changing at the fundamental levels of work, local commute and international travel. Technology and the COVID-19 pandemic have moved a large portion of office work to be remote or partially remote. Society is also driving for workplaces that are more diverse and better representations of all ethnicities. Progress is slow but evident and research suggests that more diverse organisations are more robust to the challenges of business.

Our high conviction themes under the Evolving Society trend will shift over time, but we present two of them here including our new theme focusing on the opportunities available to investors from aging populations.

Social Empowerment and Well-being

Empowering diversity and inclusion in organisations is an important trend for society but we believe it should also be a consideration for investors looking for resilience in their portfolios. Shifts in the demographics of major corporations bringing better balance to gender representation and to ethnicity representation are creating opportunities and research is showing that it may be linked to corporate profitability.

Studies done by universities of Leicester and Glasgow show that companies with more than 30% female executives tend to outperform.

Similarly, McKinsey calculates that companies in the top quartile for gender diversity on executive teams are 18% more likely to be more profitable than the bottom quartile set of companies (see graph on previous page). Top quartile companies for ethnic diversity have a 27% greater chance of outperforming companies in the bottom quartile. Companies in the bottom quartile for executives on both gender and ethnic representation are 66% less likely to outperform top quartile companies.

What's more, unsurprisingly, research suggests that workplaces with senior management and executive teams that are more diverse across gender and ethnicity are more likely to have workforces that have better diversity which in turn leads to more robust decision making and financial outcomes.

This is a key investment trend for the future and our theme aims to reflect the best opportunities available within it.

Our theme of **Silver Economy & Demographics** is designed to capture the best opportunities resulting from an aging, wealthy, population with much different saving and spending habits than younger working people.

Opportunities in this space are likely to present themselves in a variety of places. New retirement lifestyles of fitter, more able retires that are keen to travel, supported by a high purchasing power, are fuelling the Silver Economy.

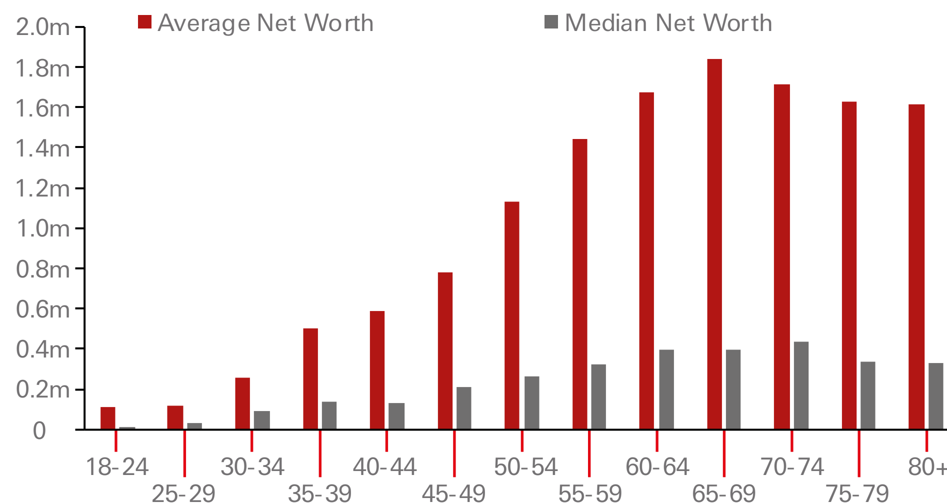
The typical industries we think of, such as pharmaceuticals; healthcare, assisted living and mobility equipment should also have hotels, cruise liners, airlines, consumer goods and specialist financials considered alongside them.

The over 60's also have the highest average net worth in society having spent a lifetime building up wealth, typically in their home equity which is often downsized, releasing capital. Retirees also have more time to spend and will typically do so with experiences, travel, leisure, hospitality.

Technology also has a major role to play and older societies such as Japan are already using robotics and technology to service older consumers. AI should also create new opportunities to service an aging population.

This is a global trend that is set to persist for the very long term and society is still adjusting to meet the demands revealing themselves. As the beneficiaries span across sectors and geographies, a bottom-up stock picking approach is needed.

Average and Median Wealth Levels in the US by Age Groups

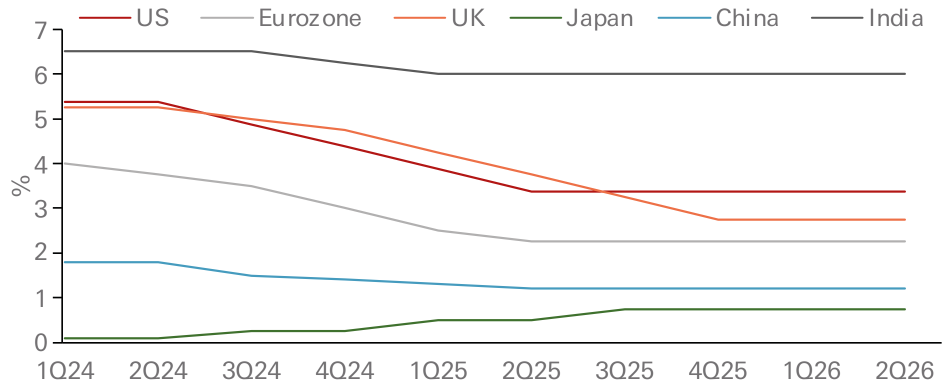


Source: Federal Reserve Survey of consumer Finances 2022, HSBC Global Private Banking as at 20th November 2024.

Riding the Earnings and Rate Cut Tailwinds

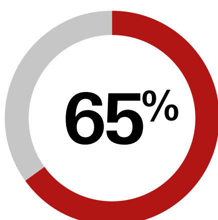
Cyclical support for portfolios should principally come from broad-based earnings growth and continued rate cuts. We look for the most attractive places to capture that earnings growth in equities and selectively lock in attractive yields in quality credit.

Many central banks are cutting rates, with the notable exception of Japan

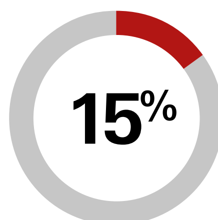


Source: HSBC Global Research forecasts, HSBC Global Private Banking as at 20th November 2024. Forecasts are subject to change

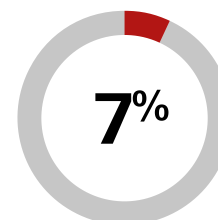
Our Three High Conviction Themes	
1. American Vitality	Many of the engines of global growth are in a higher gear in the US than elsewhere, creating resilient growth for the economy and corporate earnings. Our American Vitality theme takes a broad sector approach but emphasises the sectors we like that are not yet represented in our other themes. This includes financials, which are benefiting from loan growth and capital market activity, and consumer discretionary stocks which benefit from the likely extension of tax cuts, rate cuts and resilient labour markets.
2. North American Re-industrialisation	The desire for re-industrialisation is one of the few things that both Presidential candidates agreed on, illustrating the strong support for this trend. The desire to produce locally is illustrated by the government's plans to raise tariffs, while companies like to bring production closer to home to make the supply chain more reliable. Our theme taps into both the companies that benefit from producing locally, and companies that facilitate the re-onshoring (factory automation, logistics etc.).
3. Income Through Active Credit Selection	Bonds' stable income stream can provide an important contribution to returns, as well as a source of diversification. While markets already incorporate the bulk of the rate cuts that we foresee in the West, we think it is important to lock in the attractive yields on offer. As we rate investment grade, high yield and emerging market bonds neutral we take a bottom-up approach, with a medium-maturity target. A selective and active approach can also take advantage of the rate volatility we may still see.



65% of what the US Federal government buys has to be produced in the US



15% of the US government's revenues is spent on net interest payments



US companies' interest payments are just 7% of operating surplus, a 60-year low

Source: Buy American Act, Federal Reserve, HSBC Global Private Banking as at 20th November 2024.

Multi-asset portfolios did well in both 2023 and 2024, driven by cyclical forces. Better-than-expected growth (especially in the US), coupled with the opportunities created by innovation, led to solid earnings growth, which increasingly spread from IT to other sectors. And when inflation started to fall, the prospect of rate cuts not only boosted bond performance but also allowed equity valuation multiples to appreciate.

We think that those cyclical forces remain in place, and this is what we try to exploit with the three themes under this short-term trend.

American Vitality

The US economy currently has good momentum behind it, growing by a higher-than-expected 3% in Q2 2024 and 2.8% in Q3 2024. From here, we see continued broad support from most GDP components, including consumption, private and government investment.

Technological innovation is a key growth engine, which we tap into through our themes under the 'Disruptive Technologies' trend. Our overweight in industrials is aligned to the 'North American Re-industrialisation'. In addition to those, we see reasons for attractive returns in consumer discretionary stocks and financials as well.

The new administration wants to extend many of the tax breaks for households, which should help consumer spending. This is in addition to the fundamental support coming from resilient labour markets, falling inflation, lower rates and the wealth effect from improving housing markets. Financials have generally shown better-than-expected results, disproving some investors' fears that falling net interest income would weigh on earnings. For many banks, strong capital markets and increased loan growth have helped support earnings. Delinquencies remain low, thanks to resilient growth, and the fact that many borrowers locked in borrowing costs before rates started to rise.

Our **North American Re-industrialisation** theme taps into the very well documented re-onshoring trend, which itself results from the supply chain issues during the pandemic, and companies' desire to be less exposed to geopolitics in our multi-polar world.

As we have discussed, manufacturing is facing strong global competition, and countries with strong industrial policies are likely to have an advantage. The US is one of them, in our view. The Biden administration put in place strong fiscal support for re-onshoring with the CHIPS & Science Act and the 'Build America, Buy America' Act. And although the specific incentives may change under the new administration (including more tariffs for example) the focus remains.

Beneficiaries of the re-industrialisation should include engineering companies, and those that help with the automation and optimisation of manufacturing processes. Logistics specialists will see more business too.

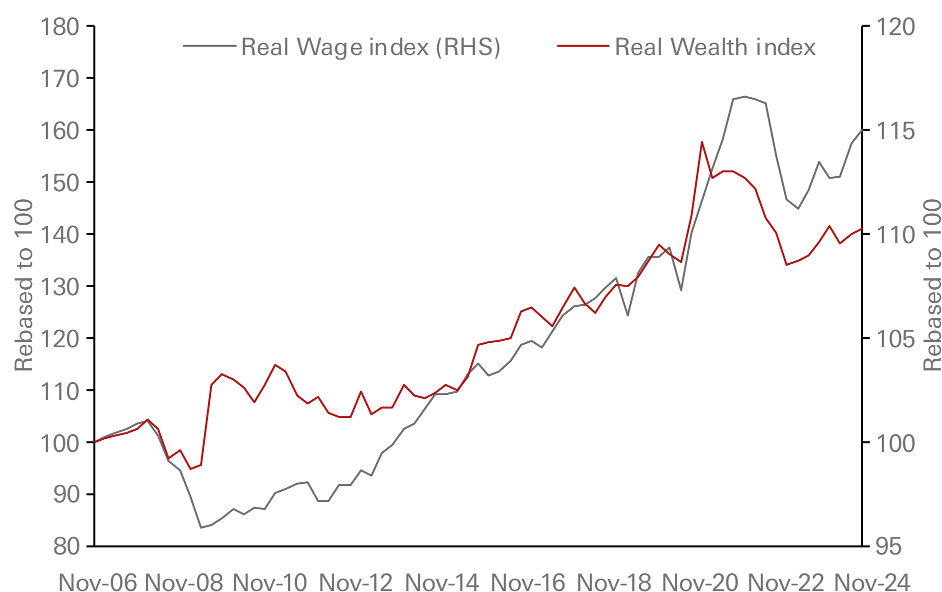
As new clusters of industrial activity form in the US, further boosted by tech-led innovation and the infrastructure build-out, we think the US will attract even more companies and investment. In turn, this should help the manufacturing sector's competitiveness and profitability.

Income Through Active Credit Selection

We like to lock in yields on quality credit as cash rates are falling and we believe investors will increasingly put some of their high cash balances to work in bonds. Of course, markets already price in the bulk of the likely rate cuts, but holding bonds can help offset equity losses in a scenario of weaker-than-expected growth. That's because the Fed has shifted its focus from fighting inflation more towards fighting any potential weakness in labour markets. Conversely, when economic data surprises on the upside, as has been the case lately, the rise in yields provides a tactical opportunity for investors to lock in those attractive yields.

In fact, we like 1) an active approach to adapt to changes in the macro-economic data, and 2) a bottom-up approach to pick the best opportunities across the market. That's because while we have a neutral allocation to most parts of the credit spectrum, we see selective opportunities in all geographies and parts of the credit spectrum. We like to tap into that broad credit opportunity set, but try to achieve an acceptable average credit rating, and currently prefer an average duration of 5-7 years.

After two difficult years, US households' income and wealth are growing again in real terms, which should support consumption



Source: Federal Reserve, US Department of Labor, Bloomberg, HSBC Global Private Banking as at 20th November 2024.

Equities

The monetary policy easing cycle remains on track, which should be accretive to earnings and provide a tailwind for global equities. Fiscal stimulus under the new US administration should be pro-cyclical and therefore provides another tailwind. While US stocks trade at much higher multiples than other markets, this is warranted by superior earnings growth, strong US innovation, and their high exposure to many of our high conviction themes. Across markets and sectors, there is high dispersion in valuations and return expectations, which may require recalibration throughout the year and argues for an active approach. For now, the US remains our principal overweight, together with the UK, India, Singapore and Japan. We remain overweight on technology but continue to diversify into communication services, financials, industrials, healthcare, and utilities.

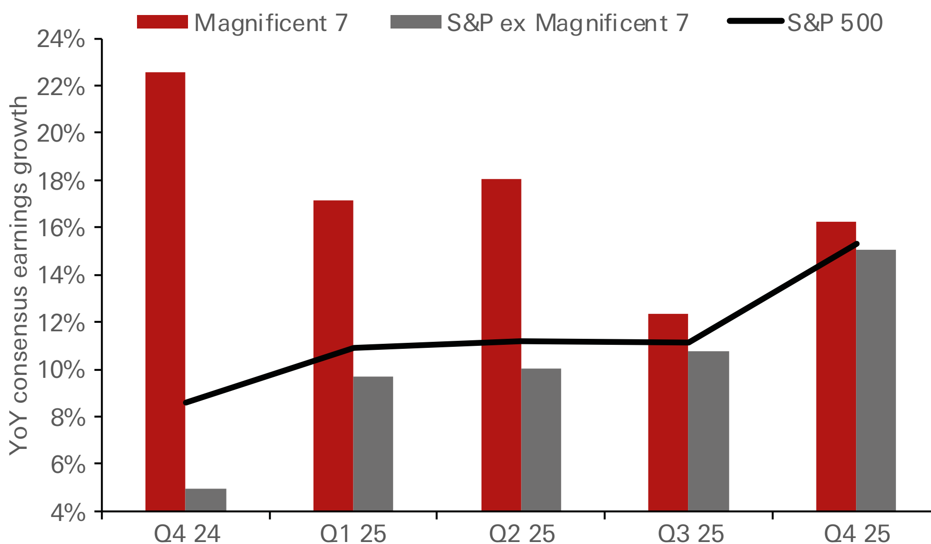
US profit power

The bull market in the US should continue as monetary policy easing, fiscal stimulus and deregulation should drive up earnings. While valuations have expanded, they are nowhere near all-time highs and given the strength in the future earnings outlook, companies look reasonably valued. S&P earnings are expected to rise 9% in 2024 and in excess of 15% in 2025. These are pre-election numbers, therefore the prospect for lower corporate and household taxes has not yet been factored in. The Magnificent 7 will continue to lead technological change but we look for broader market participation as the “Forgotten 493” are expected to post better earnings well into 2025. Moreover, the technology revolution is just beginning which should continue to improve productivity and earnings. The technology and growth imperatives are clear and companies that participate will benefit. From a sector perspective, we continue to favour technology and communication services. Due to the reindustrialisation of the US and the increased demand for energy, we continue to like the industrials sector. Finally, healthcare innovation is impressive and the demographic need for healthcare causes us to remain positive on the sector. As investors recalibrate the new political reality in the US, we diversify investments to navigate any potential sources of volatility. US equities remain our preferred overweight globally, and the fundamentals look quite attractive as we head into a new year.

Asia’s variety is its edge

In Asia, equity market leadership has shifted to India and Japan. Japan is benefiting from a mild pickup in growth, the inflation pickup boosting earnings power, and a focus on shareholder value. Investors like it also because of its low correlation to other markets. We think rate hikes will remain mild and gradual, therefore do not pose a major risk to stock performance. India remains an

Earnings of the forgotten 493 are expanding



Source: Bloomberg, HSBC Global Private Banking as at 20th November 2024.

economically diversified equity market with very positive demographics and above-trend economic growth and earnings. The market is not cheap, but India has traditionally sold at a premium to many of its regional peers, which has now contracted somewhat due to the recent consolidation in Indian equities. In Asia, Singapore is another country which benefits from the global changes in supply chains and the Asian regionalisation.

The return potential of China's very cheap valuations will probably only be unlocked when government stimulus is deemed sufficient by markets to create a sustained upward trend in growth and earnings. The measures announced to date are quite significant, but the debt overhang and US tariffs continue to cloud future prospects. We maintain neutral positions on mainland China and Hong Kong equities and focus on domestic stocks amid the complex trade relationships.

Europe trying to find its place

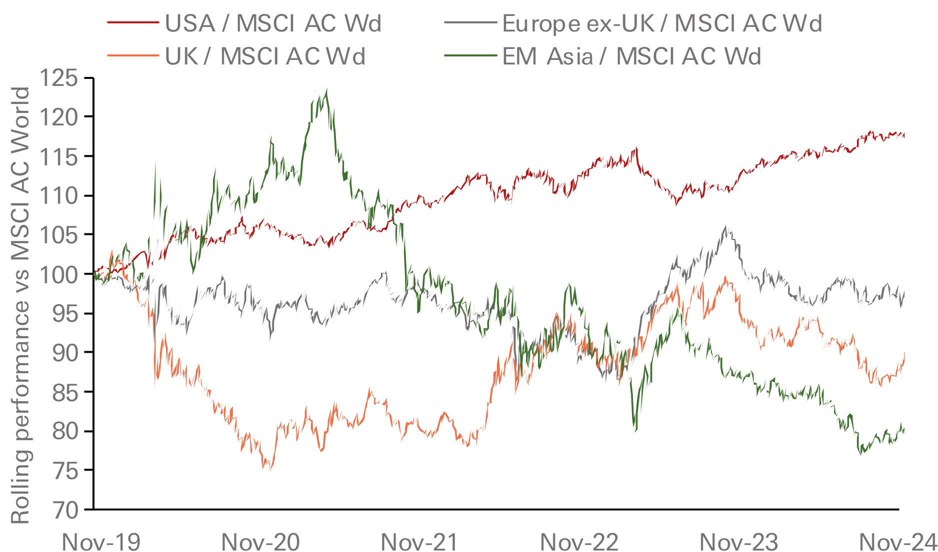
A lack of European leadership to formulate a clear industrial strategy is hurting its manufacturing base and continues to weigh on economic growth. The deceleration in global economic growth adds to the challenges for very open and global European equity markets. European equity markets did relatively well given the domestic economic conditions as their global footprint has enabled them to benefit from growth in other parts of the world. But following the US elections and the prospect of more tariffs, we downgraded our view on both Germany and the Eurozone to mildly underweight. Tariffs could adversely affect the consumer discretionary sector while the luxury companies continue to search for the Asian consumer who has not yet returned in full.

The UK equity market is in a better place, as political stability is a positive and signs of improving economic data give us some cause for cautious optimism moving forward. In addition, the UK does not have a trade surplus with the US, which could insulate it from potential tariff impacts. Its global companies are trading at very low valuations and the market's defensive nature adds to the appeal for investors looking to diversify US-heavy or tech-heavy portfolios.

Sticking with equities

We maintain our mildly overweight view on global equities as returns should exceed those of the other asset classes, especially as monetary policy normalisation unfolds. Clearly, political uncertainty and geopolitical conflicts, as well as the mild global slowdown create challenges, but earnings have enough momentum and diversity to push markets up further.

The US has continued to outperform global equities, but the UK and Asia too are showing improvement



Source: Bloomberg, HSBC Global Private Banking as at 20th November 2024. Past performance is not a reliable indicator of future performance.

Fixed Income

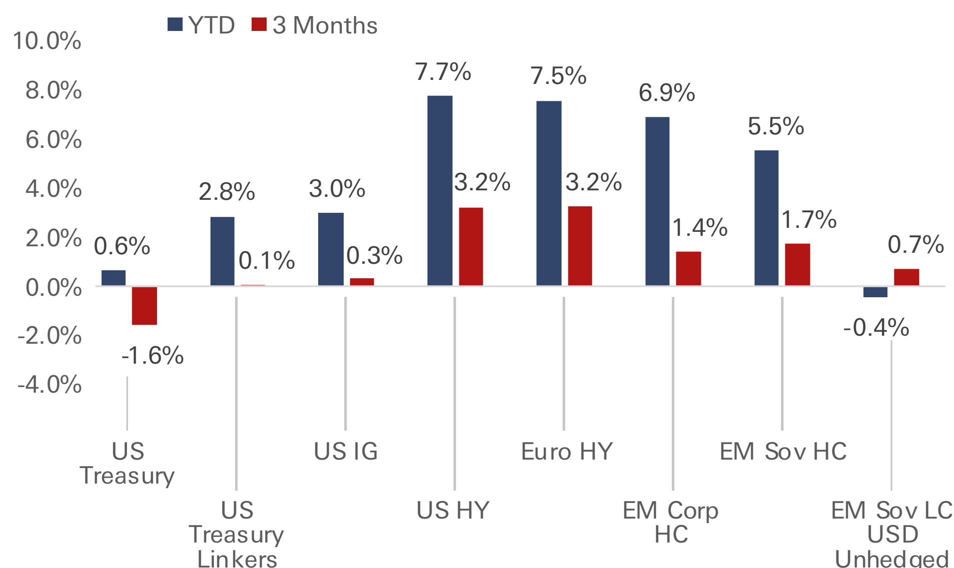
The clear outcome of the US elections makes us more confident about the performance of risk assets. As such, we decided to pare back our allocation to USD Investment Grade (IG) and EM HC corporate bonds to a neutral stance, as we find better opportunities in the US equity market.

We therefore have a neutral stance across almost all bonds' segments, apart from the Japanese government bonds, where we retain an underweight position. However, we continue to see corporate credit, including USD IG bonds and Global High Yield (HY) as a good way of diversifying multi-asset portfolios and generating income by locking in elevated yields.

Expectations of a Republican "clean sweep" pushed DM government bond yields higher and hurt the performance of duration assets, while Global HY benefited the most from the surge in risk appetite.

Following the swift outcome of the US Elections, we decided to pare back our allocation to USD IG and EM HC corporate bonds to a neutral stance, as we find better opportunities in the US equity market. As USD IG credit spreads are at their tightest levels since 1997, the largest contributor to expected returns - the rate component - may continue to exhibit volatility and will be sensitive to any new political developments.

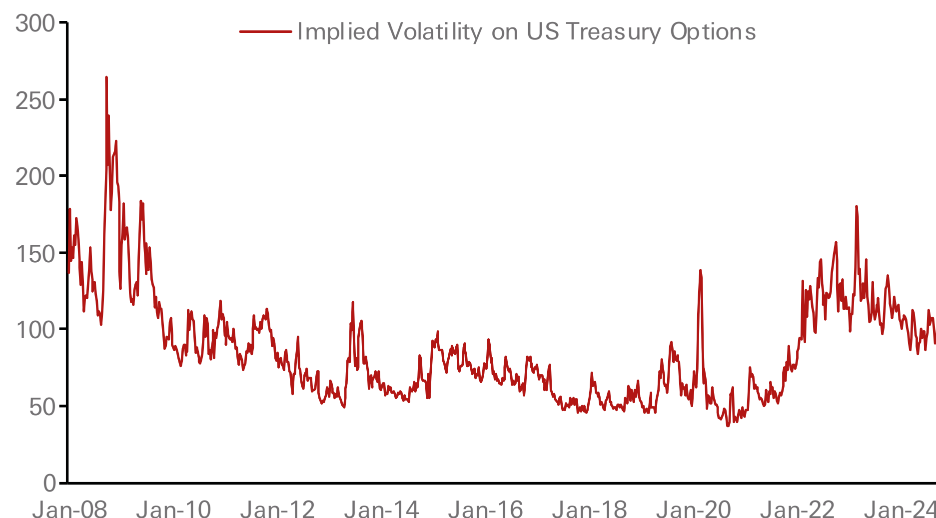
The US Elections outcome has been detrimental to duration assets' performance, such as DM government bonds



Source: Bloomberg, HSBC Global Private Banking as at 20th November 2024. Past performance is not a reliable indicator of the future performance

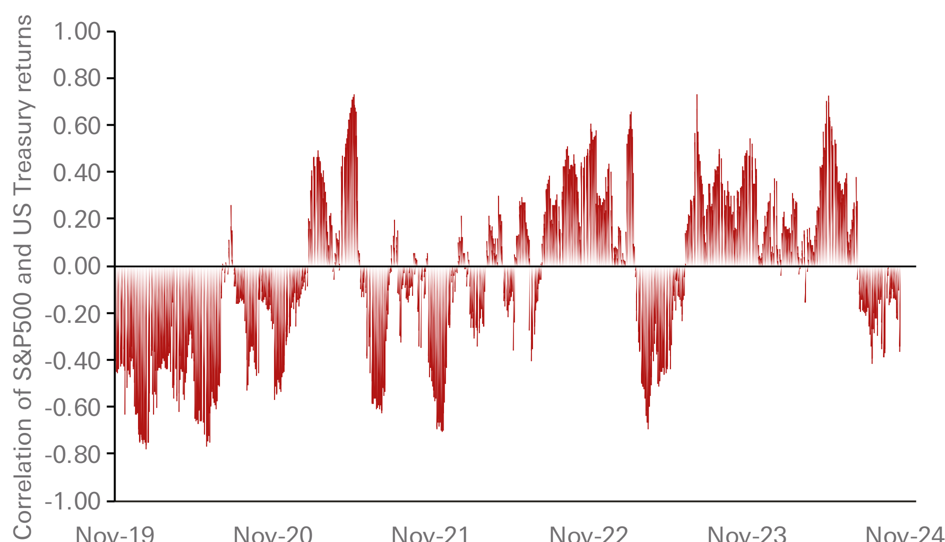
We believe, however, that a large part of the expected fiscal stimulus and tariff measures under the new Trump administration are already priced in US Treasury yields. This is evidenced in yields having risen quite significantly a month before the elections, and almost by as much as what we saw a month after the 2016 election. In addition, there is a chance that any fiscal measures initiated by the new administration in 2025 may be diluted by Congress, as opposition from fiscal hawks in Mr Trump's own party could result in a compromise on tax cuts. As for tariffs, they may not be universal, and it may

Rate volatility may remain elevated in 2025



Source: Bloomberg, HSBC Global Private Banking as at 20th November 2024. Past performance is not a reliable indicator of future performance

A negative correlation between equities and fixed income strongly supports diversification strategies



Source: HSBC Global Private Banking, Bloomberg as at 20th November 2024. Past performance is not a reliable indicator of future performance

take months before we see the effects in inflation measures. All in all, we expect the Fed to carry on with its easing policy and its data-dependency, as highlighted by Fed Chairman Powell on 7 November 2024. This should remain supportive of the bond markets.

While we now have a neutral stance across almost all bond segments, apart from Japanese government bonds, where we retain an underweight position, we continue to see corporate credit, including USD IG bonds and Global HY, as a good way of diversifying multi-asset portfolios and generating income by locking in elevated yields. As exhibited in the above chart, bonds and equities have recently moved back to an environment of negative correlation. Therefore, a well-diversified portfolio should be able to thrive during "risk-on / risk-off" periods.

Considering elevated volatility across US Treasuries, we keep our focus on 5-7 year maturities overall, but slightly shorter for Global HY and EM HC debt (3-5 years on average). Credit selection becomes even more relevant considering the uncertainty around the upcoming US administration's policy measures. For example, some companies may be better positioned to navigate a potential escalation in tariffs and their resulting impact on the economy. We believe that financials, especially banks, could fare relatively well amid deregulation.

We are conscious however, that current credit spreads in general do not fully compensate for default risk. As a result, we not only focus on companies prioritising bondholder-friendly policies, with sound leverage ratios and low short-term refinancing needs, but also the ones with robust supply chains and no geographical mismatches, which would make them less vulnerable to US tariffs. This is valid not only for developed markets but also for emerging market companies, and across the IG and HY ratings spectrum.

The risk to our strategy is that large unfunded tax cuts implemented by Republicans could trigger a repricing of the term premium and push US Treasury yields much higher in anticipation of higher budget deficits and Treasury issuance. This scenario was witnessed after the UK mini-budget announcement in October 2022. Fortunately, the US dollar's status of the global reserve and trade currency structurally supports its government bond market. In addition, the Treasury has some much needed flexibility in its financing options, even in consideration of a looser fiscal path. It may lean on more bills supply to fund higher deficits, while keeping coupon issuances steady. We therefore believe this scenario has a very low probability of materialising.

Across EM debt, we have turned more cautious on Mexican assets, due to the country's close trade ties with the US, but we remain broadly neutral on EM across the board. Fiscal stimulus from the US and China could well support global economic growth and therefore risk appetite for EM debt. We favour countries that are net importers of US goods and services, and companies from sectors which may be less exposed to potential US tariffs.

Additionally, we believe that long-term factors such as demographics can help justify lower rates. Other factors may play a more immediate role, however, such as geopolitical risks and monetary policies.

Currencies and Commodities

As we anticipated, the US dollar is well-supported in Q4 by elevated US Treasury yields, stronger-than-expected US economic data and lingering global uncertainties. The post-election reaction was also positive, as a strong USD is one of the typical features of the 'Trump trade'. Emerging market (EM) currencies initially edged higher thanks to positive risk appetite but sold off after the election.

As we enter 2025, we believe the market will be looking at the direction of yields, economic momentum and risk sentiment to determine currencies' relative performance. While global policy rates are expected to drift down, the US dollar will remain one of the higher yielding currencies, which makes it attractive. The US economy's outperformance may be another source of support. And as tariffs add to uncertainty in our multi-polar world, the US dollar may continue to see some support from its safe haven status.

In our view, currencies offering attractive carry or those with relatively hawkish guidance from the central bank will remain supported as many other countries are cutting rates. In the US, a lot will depend on how the Fed navigates fiscal changes as we enter a new US presidency. Tax cuts will come with higher debt, and some concerns that potentially higher inflation might limit the room for the Fed to cut rates. Although we think the Fed remains on its rate cut path for now, we think USD should remain well supported, also thanks to the encouraging economic outlook. Outside of the US, we will watch how the new tariff and trade policies affect risk appetite, which is already fragile due to geopolitical conflicts.

With that in mind, we consider USD as one of the most attractive currencies given steady high US yields, and supportive US economic policies. On the other hand, we consider EUR, CHF, JPY, and NZD as most vulnerable and see limited upward risks in the coming months. The Eurozone's political concerns have risen lately, due

Bullish
In G10: USD Other: INR, IDR, PHP, and ZAR Commodities: Gold
Neutral
In G-10: GBP, CAD and AUD Other: SGD, RMB, KRW, THB, BRL and TRY Commodities: Silver, and Oil
Bearish
In G10: EUR, CHF, NZD and JPY Other: MXN

The gold price has been rising in line with higher US debt, and we believe this trend will continue

Source: Bloomberg, HSBC Global Private Banking as at 20th November 2024.
Past performance is not a reliable indicator of future performance.

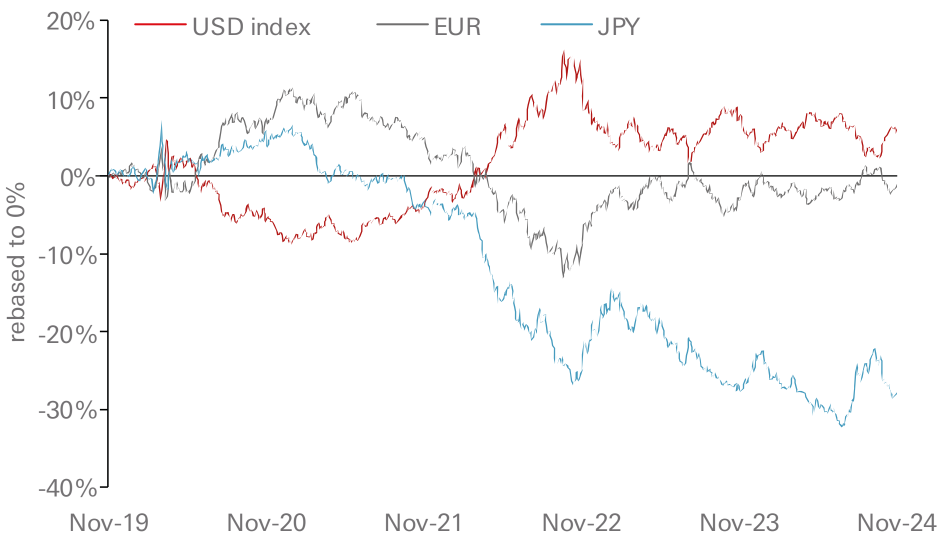
to tariff risks and Germany facing an election amid sluggish growth. JPY and CHF remain vulnerable to low yields compared to the US, although further easing from the Fed could curb this trend. New Zealand's economic context is a concern for NZD, while more generally, high-beta and commodity currencies could be at risk given the moderate regional growth outlook.

In EM, China is one of the key targets of US trade tariffs. However, we believe the People's Bank of China will play a key role in containing FX volatility and hence see limited downside risks to the currency. Nevertheless, we prefer ASEAN currencies including IDR and PHP. Current conditions maintain strong upward pressure on high yielding currencies, but even with increasing international trade uncertainties, investment and trade inflows could spread through the region and support domestic economies. We also maintain a constructive outlook on INR, thanks to high yields, strong domestic momentum, and further inflows as more Indian bonds get included in Global bond indices.

Although the year-to-date performance has been great, Gold had a negative post-election reaction on the back of a strong USD and higher US yields. But in a context of higher US debt from fiscal expansion policies, potential higher inflation, and global uncertainties, we see gold edging even higher in the coming months. Some investors seem to be looking for active diversification or an alternative to the US dollar in our multi-polar world and a hedge against geo-political tail risks. That said, the current high valuation could eventually limit the overall demand for the metal or boost scrap supply.

Oil prices have been quite resilient to the high level of uncertainties in the Middle East, but we see the price sensitive to changes in the supply/demand balance. We acknowledge downside risks if US output is substantially increased and global demand is undermined by soft ex-US growth.

USD has outperformed EUR and JPY over the past five years – a trend which we expect to persist



Source: Bloomberg, HSBC Global Private Banking as at 20th November 2024.
Past performance is not a reliable indicator of future performance.

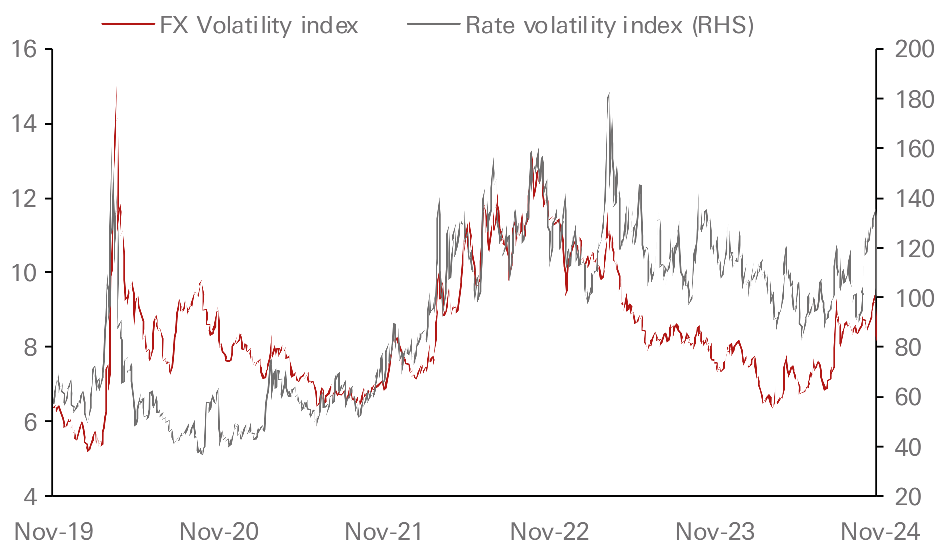
Hedge Funds

Hedge funds have been benefiting from a rich opportunity set and although some big risk events are now behind us, we think volatility and dispersion in equities, fixed income and currencies will continue be substantial. This should benefit long/short and active strategies and underscores the importance of hedge funds as portfolio diversifiers. As a result, we maintain our overweight on hedge funds. We are most positive on discretionary macro, systematic equity market neutral, Asian equity long/short, multi-strategy and multi-PM managers.

Some major events benefited smart hedge fund managers in H2 2024. Those managers who anticipated the September Fed cut early with long bond positions benefited, especially if they later reversed those when growth figures picked up and pushed yields higher. In Asia the dramatic initial response by equity markets to the multi-faceted Chinese policy announcements increased volatility and caused large and variable changes in the relative performance of the region's stock markets. Finally, the US elections and economic data flow caused many ups and downs in relative performance of sectors and styles as many fund managers moved closer to their benchmark to reduce binary election-related risks.

However, recent trading periods represented difficult times for managed futures as trend selection strategies were buffeted by whipsawing equity markets, a meandering path for fixed income and fluctuations in currency markets. In contrast event driven strategies delivered healthy positive performance driven by fundamental equity sub-strategies and credit-based allocations. Macro managers enjoyed strong returns propelled by interest rate trading while credit specialist allocations also delivered. Both market neutral and multi-strategy funds made gains recently.

Relatively high currency and rate volatility create opportunities for hedge funds



Source: Bloomberg, HSBC Global Private Banking as at 20th November 2024. Past performance is not a reliable indicator of future investors.

Looking ahead, we remain positive on the opportunity set for discretionary macro managers. Volatility in interest rates should continue, while the different central bank rate paths should create opportunities in foreign exchange markets that can be monetised. In particular, the Japanese yen should continue to see volatility, which also affects the Nikkei, which managers can exploit. And as US economic data may keep the 'soft landing vs no landing' debate going, the Fed rate cut path will also continue to be repriced, impacting rate differentials. In short, we see conditions of persistent volatility across asset classes and global divergence in macro-economic performance supporting macro managers' returns over the coming quarters.

Within CTA's the Yen carry unwind near the beginning of Q3 followed by the sell-off in the Nikkei represented two hits for trend followers. In addition, the surprise policy announcements by China created challenges for short China equities and short macro-related commodities positioning such as copper. Furthermore, hurricane Helene's impact on natural gas prices hurt a long-held short positioning in the strategy. As the world remains uncertain but some major risk events are behind us, we hold a neutral outlook on the performance credentials of CTA's going forward. In contrast, given our constructive view no global equities, we have a neutral/ positive view on systematic equity market neutral strategies.

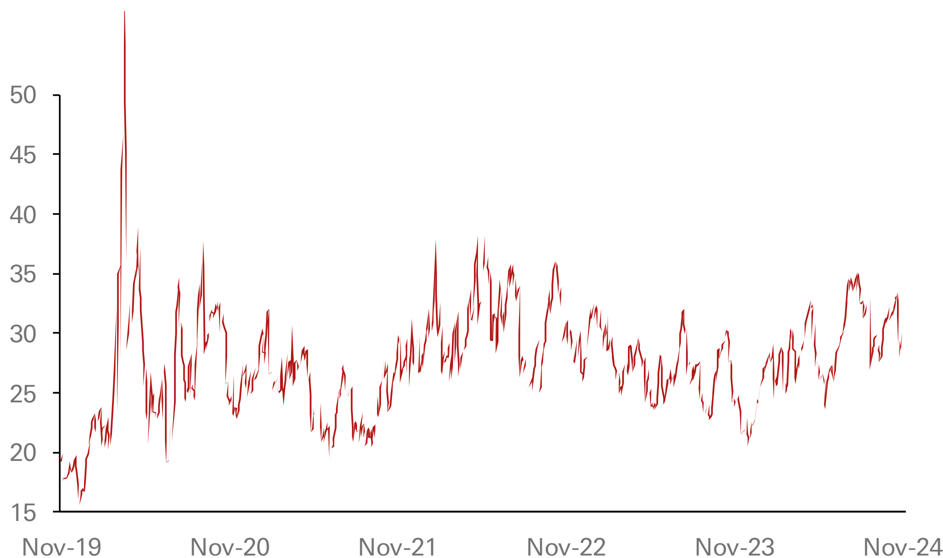
In light of the significant policy support measures in China we have upgraded our outlook for Asian equity long/short to outright positive. This reflects the significant improvement in momentum and sentiment that previously held us back from shifting beyond neutral/ positive and our view that valuation differentials with the rest of the world will tighten.

We maintain our outlook at neutral for event driven strategies. While valuations in US equity markets look full, corporate activity in the form of announced take-overs continues to tick up year on year. We believe that decision-making by corporate management will be catalysed after the US elections, causing them to engage in further transactions. Meanwhile activist campaigns abound as managers continue with new campaign announcements. One area of potential concern with event driven strategies is that of potential crowdedness in special situations. There is an element of commonality here, albeit with dispersion in terms of investment approaches.

Our neutral outlook for credit long/short strategies is maintained. From a pricing perspective, valuations are slightly rich, but carry is still interesting. The relative bright spot in terms of dispersion both across and within sectors is maintained and supportive for credit long/short managers. Within distressed there continues to be a non-meaningful increase in filings - we remain neutral on the outlook for the strategy. Finally, we continue to favour structured credit within the wider opportunity set of alternative credit strategies.

We maintain our positive view on the operating environment for Multi-Strat and Multi-PM managers, which have continued to deliver positive performance.

Markets expect relatively high dispersion of stock returns within the S&P500, which should benefit equity-focused hedge fund strategies



Source: CBOE S&P500 dispersion index, Bloomberg, HSBC Global Private Banking as at 20th November 2024. Past performance is not a reliable indicator of future investors.

Private Markets

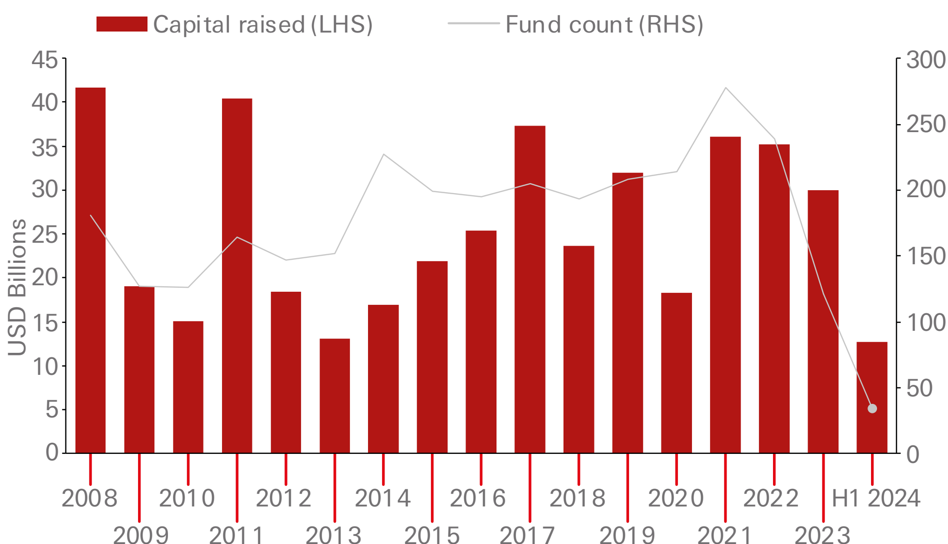
While private equity fundraising remains off its highs, large buyout funds of managers with long-term and proven track records continue to raise substantial funds. The lower and mid-market is increasingly attractive thanks to reasonable valuations and a wide range of future exit opportunities. Dry powder has been falling and we expect increased confidence to lead more managers to close transactions. In private credit, the default and loss rates remain low and the monthly private credit returns have been steady in 2024 in contrast to the public market.

As overall fundraising slowed, Europe-focused funds have seen their share of fundraising hit the highest level in several years. This could be a reflection of the path of interest rates in Europe, which saw the ECB cut rates prior to the Fed, while it may also be due to valuations in Europe, which are more attractive than some other markets. Regardless, activity levels should pick up quite significantly in Europe as these allocations are put to work.

Across global private equity markets, dry powder fell from record levels, which were reached in 2022. With around $1.5tn of dry powder available, fund managers have significant resources for future investments. Nevertheless, many fund managers are exercising caution when it comes to capital deployment and are seeking an attractive entry valuation, which would allow them to maintain historic return levels, rather than simply lower their own return targets.

Unsurprisingly, given the macroeconomic backdrop, many fund managers are cautiously optimistic about global economic growth. This is particularly true in the US, where many managers continue to monitor for pockets of weakness, which might present long-term opportunities. There are also several long-term secular trends playing out, with significant opportunities for private equity managers. These can be found in energy transition, on-shoring or near-shoring of supply chains and the emergence of AI. Each of these trends requires significant volumes of capital spending and with government balance sheets stretched, private equity will have a major role to play in either delivery or configuration of the tools that will enable real progress towards end goals.

PE first time fundraising activity



Source: Pitchbook, as at 20th November 2024.

Inflation is softening and interest rates are gradually coming down from recent peaks – although the exact timing and magnitude can be debated. The direction of travel is what is generally important to investors and fund managers alike. In an environment such as this, fund managers can be more confident in their assumptions and feel better able to make longer-term decisions on investments. They are also likely to be increasingly committed to closing transactions (both buying and selling) over the next 12 months, instead of holding out and waiting for a more stable environment and stronger market, as was the case in the last 12-24 months. This all bodes well for a future increase in activity.

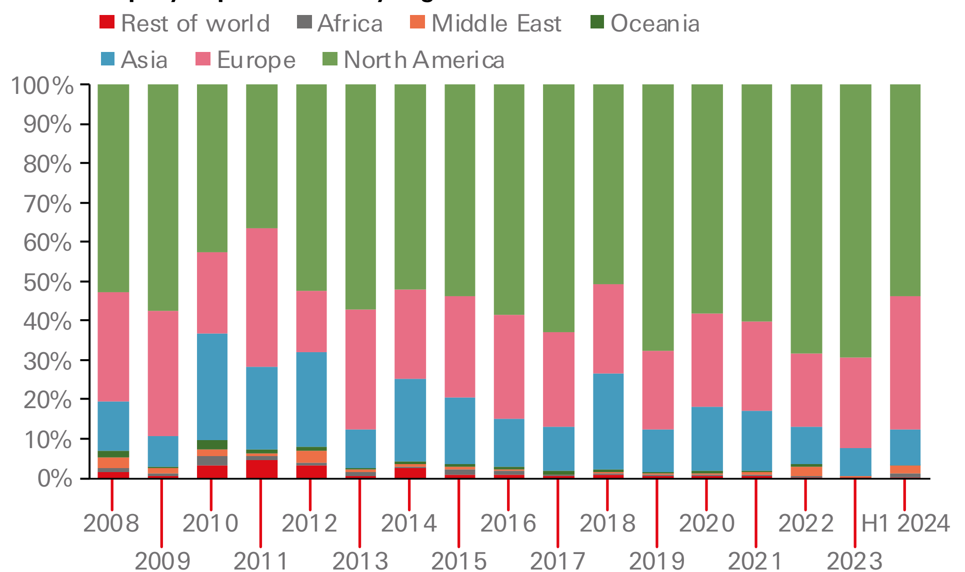
Such an environment should benefit managers with strong value creation capabilities, which will shield them from the impact of interest rates that are still high (both in relative and absolute terms). Such an approach should also allow them to grow assets and achieve future exits without over-reliance on leverage and financial engineering to deliver returns. It is therefore our view that a high-conviction approach – investing with GPs with proven value creation skills – combined with vintage diversification, positions investors to capitalise on emerging opportunities and manage risks effectively.

In private credit, high borrowing costs have resulted in more profit warnings, but the senior secured nature and diversified exposure of portfolios tends to keep default and loss rates low.

US LBO deal volume has started to gain momentum, after a significant slowdown in the past 2 years. Loan spreads, particularly in the upper middle market, have tightened in 2024 as banks reopened to business. But direct Lending continues to generate attractive yields and risk-adjusted returns due to the higher base rate and lower leverage levels for the underlying borrowers.

We expect to see greater performance dispersion across managers in coming quarters, where those with better underwriting standards over the past few years are likely to see lower defaults and losses, and better net returns.

Private equity capital raised by region



Source: Pitchbook, data as at 20th November 2024.

Real Estate

Global commercial real estate value declines have begun to stabilise in 2024. Significant declines are now limited to the office sector, which faces a unique set of headwinds. Geographically, declines have been most significant in Europe and the US. The sharp decline in values and falling interest rates are starting to boost the appeal of real estate, but investment volumes remain subdued for now. That could start to change with further interest rate cuts and post-US election clarity.

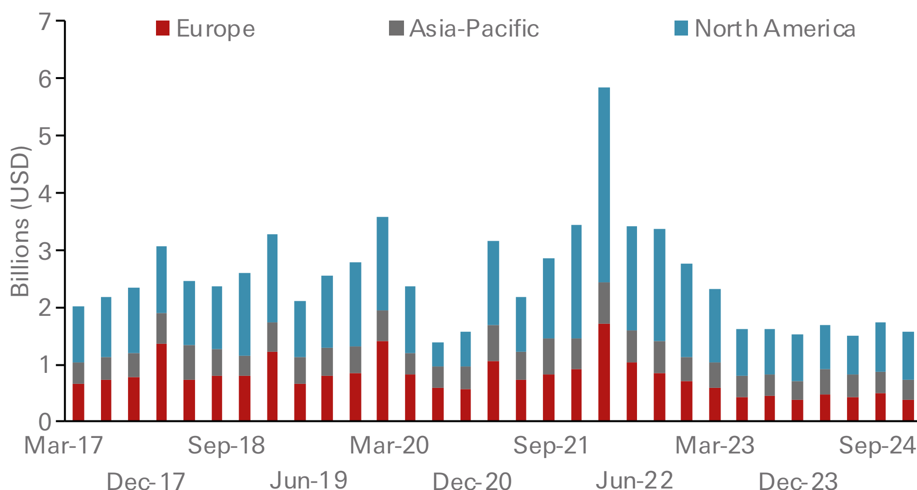
Global commercial real estate value declines have moderated during 2024. Between June 2022 and June 2024, global capital values declined by approximately 15%. However, in Q2 2024 global values declined by just 0.7%, with only the office sector (-2.4%) continuing to experience significant value declines.

Geographically, the most significant declines have been observed in Europe (-19%) and the United States (-18%), while Asia-Pacific has seen a modest overall decrease of just 3.4%, which partly reflects low interest rates in Japan, and less of a spike in valuations in 2021/ early 2022. However, as Japanese inflation has returned and interest rates edge up, property values may begin to fall as property yields come under upward pressure.

As capital values settle, the re-rating of property yields across Europe, North America, and parts of Asia (such as Australia) provides the foundation for an improved outlook for direct property market returns. Further declines in interest rates should also boost the relative appeal of real estate yields versus other asset classes.

Though the relative appeal of real estate has recently improved, investment volumes remain subdued; year-to-date (to September) investment volumes are at their lowest level since 2010. However, there are signs that in markets such as the UK, where values were quicker to correct, liquidity is beginning to pick up again. Some investors delayed investing until after the US elections and further cuts in interest rates.

Global investment volumes for Real Estate are still low but could start to pick up



Source: MSCI, HSBC Global Private Banking as at 20th November 2024.

Another benefit of lower interest rates is the positive impact on future income growth resulting from better-than-expected economic activity, which can potentially boost leasing activity and the ability of landlords to raise rents. Should economic activity pick up, this may boost leasing activity for retail and office properties, whose leasing activity more closely tracks the economic cycle. This contrasts with residential, logistics and non-traditional property types, such as senior housing and data centres, where demand drivers are currently more secular and less cyclical.

Still, the office sector faces major challenges, especially in US West Coast cities, as hybrid working practices have reduced the need for space and shifted demand towards high-quality, sustainable buildings. This has created a significant overhang of older assets that risk becoming obsolete without substantial capital investment. In global gateway cities like London's West End and central Paris, constrained supply has driven prime rents to record highs. And in New York, rents for trophy buildings remain relatively strong despite multidecade-high vacancy rates, highlighting a preference for best-in-class properties.

After years of struggling, the retail sector is in relatively good health, particularly for non-discretionary neighbourhood retail. Yields are elevated after a decade of being out of favour with investors, during which time there has been very little new development. On the occupier side, failing retailers have been cleared out during the pandemic and landlords have successfully re-tenanted empty stores with a more sustainable mix of occupiers. The result is a re-emergence of rental tension and growing investor interest.

Logistics fundamentals have softened in many markets as businesses are focussed on operationalising a significant overhang of space that was leased during the pandemic. Still, any weakness in leasing is expected to be temporary as e-commerce continues to take market share. Moreover, the significant market rental gains over recent years will take time to filter through to incomes, so we believe there is further scope for income growth in the near term.

The residential sector continues to deliver rising income due to a lack of development and stable rental demand, which is benefitting from an affordability advantage for households versus buying. In the US, where there have been pockets of excessive multifamily development, fundamentals are stronger for single-family housing, manufactured housing, and senior housing.

Whilst falling interest rates and improved liquidity may support some yield compression, we would expect income levels and income growth to be the predominant drivers of total returns over the medium term. For core strategies, this means focusing on stable, income-generating assets in resilient sectors. Additionally, the recent sharp declines in value have created pockets of distress, especially in the office sector, which may create opportunities for investors willing to embrace greater levels of risk. Value-added and opportunistic approaches, including acquiring and repositioning distressed assets with targeted asset management strategies, offer potential for capturing higher rents and returns.

HSBC and Sustainability

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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 invest-ment may include, but are not limited to:

Credit risk
Investor is subject to the credit risk of the issuer. Investor is also sub-ject 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 invest-ment 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 spe-cial 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) de-fault 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 in-cur reinvestment and subordination risks. Investors may lose all their invested principal in certain circumstances. Interest pay-ments 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 con-vertible and bail-in debentures are hybrid debt-equity instruments that may be written off or converted to common stock on the oc-currence of a trigger event. Contingent convertible debentures re-fer to debentures that contain a clause requiring them to be writ-ten 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 mecha-nisms (i.e. cotractual 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 mech-anisms (i.e. statutory bail-in) whereby a national resolution au-thority writes down or converts debentures under specified con-ditions 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 princi-pal.

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 sched-ule and/or that the risk on the ranking of the bond seniority would be compromised following nationalisation.

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, liquidi-ty 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 invest-ments 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 estab-lished economies and/ or securities markets. Such risks include (a) the risk of nationalisation 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 set-tlement periods in so far as securities transactions and (h) less strin-gent 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 appli-cable 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 "ESG and sustainable investing" products include investment approaches or instruments which consider environmental, social, governance and/or other sustainability factors to varying de-grees. Certain instruments we classify as ESG or sustainable investing products may be in the process of changing to deliver sustainability outcomes. There is no guarantee that ESG and Sustainable investing products will produce returns similar to those which don't have any ESG or sustainable characteristics. ESG and Sustainable investing products may diverge from traditional market benchmarks. In addition, there is no standard definition of, or measurement criteria for, ESG and Sustainable investing or the effect of ESG and Sustainable investing products. ESG and Sustainable investing and related measurement criteria are (a) highly subjective and (b) may vary significantly across and within sectors.

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An investment which is considered to fulfil sustainable criteria today may not meet those criteria at some point in the future. When we allocate an HSBC ESG and Sustainable Investing (SI) classification: HSBC ESG Enhanced, HSBC Thematic or HSBC Impact (this is known as HSBC Purpose in the UK) to an investment product, this does not mean that all individual underlying holdings in the investment product or portfolio individually qualify for the classification. Similarly, when we classify an equity or fixed income under an HSBC ESG Enhanced, HSBC Thematic or HSBC Impact (this is known as HSBC Purpose in the UK) category, this does not mean that the underlying issuer's activities are fully aligned with the relevant ESG or sustainable characteristics attributable to the classification. Not all investments, portfolios or services are eligible to be classified under our ESG and SI classifica-tions. This may be because there is insufficient information available or because a particular investment product does not meet HSBC's SI classifications criteria.

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