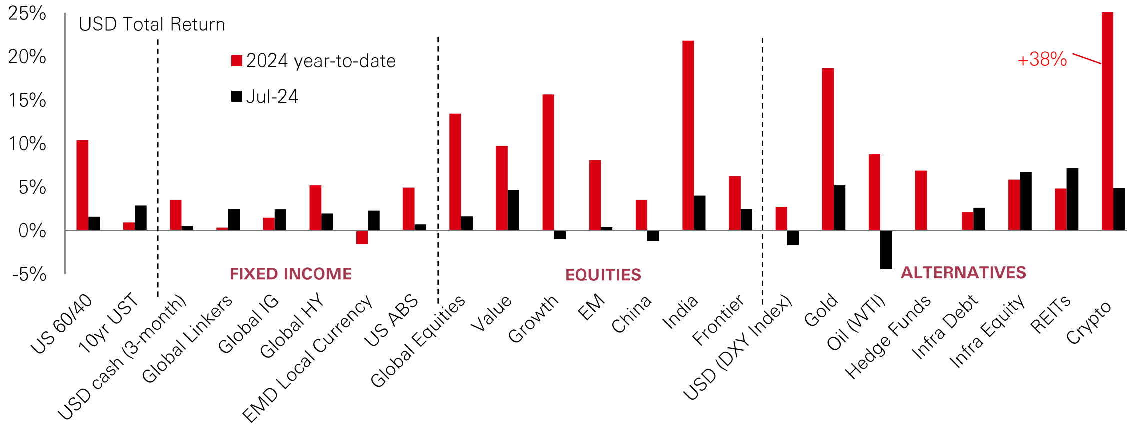
HSBC

Investment Weekly

5 August 2024

Chart of the week – July in review



From the aeroplane window, the ground below can look flat, at least until you start the descent. So it goes in investment markets in July – global stocks are little changed for the month. But, when you get closer, there has been a lot going on.

First, there has been the material correction in the US tech sector. The Philadelphia Semiconductor Index plunged -11% from its peak during the month, with the sell-off extending into August. And the closely-watched Magnificent Seven (Mag7) stocks slipped, with stretched valuations, uncertain profits guidance, and geopolitical tensions all bothering investors. That had consequences for tech-sensitive markets in Asia, too, with prices falling in Japan, Taiwan, and South Korea.

Second, while most momentum trades faltered (except India and gold), unloved value and small-cap stocks rallied. Other defensive sectors, like infrastructure and real estate, also benefitted. This rotation – a broadening of market performance – is a healthy development for the stock market. But it will need to keep going to cover the lost Mag7 index points.

Third, encouraging news on disinflation, a renewed prospect of interest rate cuts in H2, and the soft landing coming into view, suggest the sector rotation story can continue. Equally, the rally in US government bonds helps bolster equity risk premia across the board. And while tech valuations are stretched, they are not historically-extreme.

A number of developments are set to create a more volatile ride in markets during H2. Nominal growth is slowing, and could slow faster – something that has weighed on China's stocks in July. Geopolitical stresses and US elections will matter too.

Market Spotlight

Securitised credit outperforming in 2024

Securitised credit has been one of the best-performing areas of the fixed income universe over the past two years – and that's expected to continue through 2024. Pivotal to its outperformance is that it's a floating-rate asset class. That means income returns have been bolstered by higher central bank policy rates. Resilient economic conditions have played a part too, with falling spreads driven by robust credit fundamentals proving ideal conditions for capital growth.

Despite expectations of near-term US rate cuts – and the Fed easing could start from September – securitised credit should still hold appeal. Some investment specialists expect US policy to gradually shift towards a terminal rate of around 3.5%, a level where income from the asset class would remain high. Plus, there are added advantages for portfolios. Over the long term, securitised credit offers low correlation and low volatility versus other fixed income sub-asset classes. It also has a lower correlation to US equities than corporate bonds, making it an attractive diversifier for multi-asset investors.

Central Banks →
The timetable for Fed rate cuts and a soft landing

Currencies →
What the latest policy moves mean for the Japanese yen

Equities →
Exploring market reaction to Q2 earnings season

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Source: HSBC Asset Management. Macrobond, Bloomberg. See page 8 for details of asset class indices. Data as at 11.00am UK time 05 August 2024.

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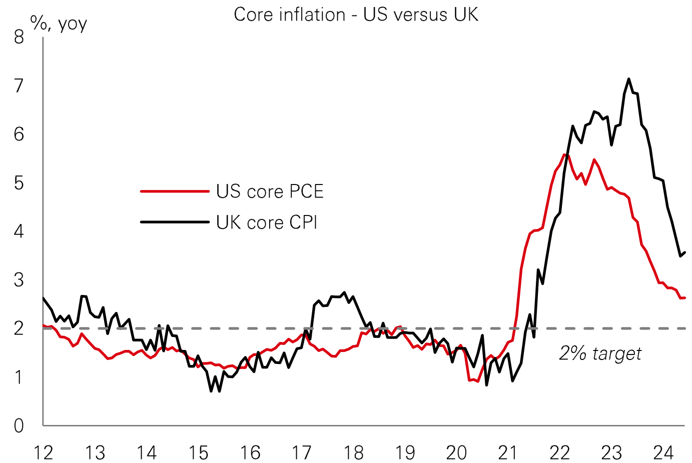
No time to waste

Both the Fed and the Bank of England (BoE) did what markets expected at their latest policy meetings – the Fed standing pat and the BoE cutting by 0.25%.

Core inflation is much closer to the target in the US than the UK and wage growth is more clearly moderating, which are consistent with a wide range of indicators showing that the US labour market is cooling. Moreover, the Fed has a dual mandate – inflation at target and full employment – whereas the BoE targets only inflation.

Looking ahead, the Fed may need to avoid further delaying rate cuts if it wants to secure the much talked of 'soft-landing'. Gradual US slowdowns – such as those are seen at present – can morph into sharper slowdowns with little warning, and by that time, it is too late for policy makers to rescue the situation. The BoE, however, needs to stick to its guidance that it "will not cut rates too much or too quickly" given inflation is proving stickier in the UK than elsewhere.

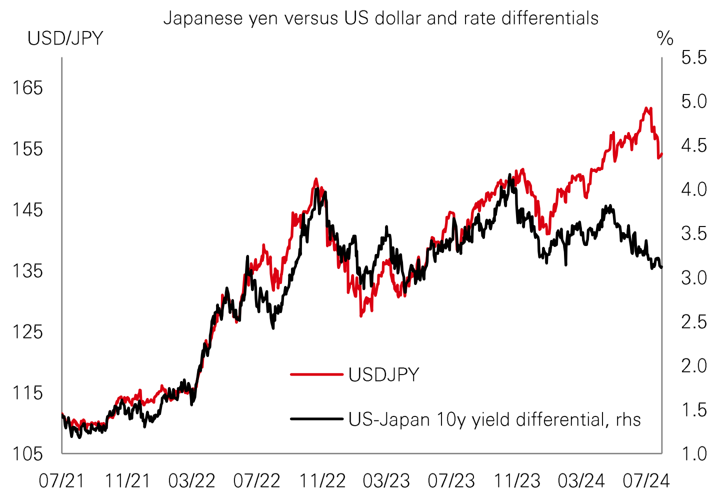


Yen spillover

The recent sharp recovery in the Japanese yen is a big development for markets. The yen has been a major funding currency for carry strategies in recent years (where traders borrow yen to invest in higher-yielding currencies). But a strengthening yen – amid intervention by Japanese authorities – undermines the profitability of these trades, thus seeing them unwind. These carry trades may have also funded positions in other risk assets, possibly exacerbating the recent global tech sell-off. And a stronger yen potentially weakens domestic corporate profits, which is one reason why Japanese stocks sold off sharply last week.

While the pace of the yen rally looks unsustainable, there are good reasons to expect further recovery in the coming months.

The Bank of Japan's gradual policy normalisation is important. But the more meaningful propulsion for the yen is likely to come from continued global disinflation. This could see interest rate differentials falling further in favour of the yen. 2024 promised to a be a good year for the yen – but maybe it'll just be the second half?

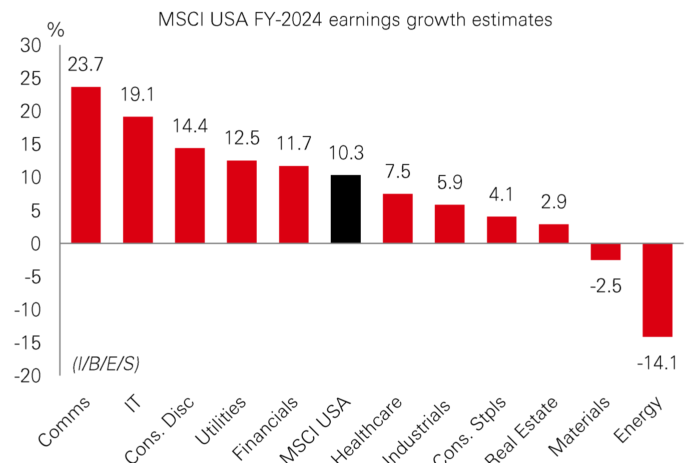


Q2 earnings – great expectations

The Q2 earnings season continues in the US, and the broad picture so far is positive. Profits across the largest stocks are on course to grow at an annual rate of 10% this quarter. Further out, the consensus view is that there will be similar growth for the year as a whole. Those sectors reporting the strongest growth last quarter include communication services, IT, financials, and healthcare.

But there have been some disappointments. 'Big tech' sectors are set to drive the bulk of profits growth this year. Yet, stocks on high valuations – like many in the tech sector – have been battered on any hint that blistering profits growth is at risk. That's extended to some Magnificent Seven stocks – which have wobbled at times.

More broadly, restrictive rates and signs of economic stress – particularly in the consumer sector – are causing pain in places. Consumer staples has been lacklustre in Q2, and when you adjust-out the influence of Mag7 stocks, the same goes for consumer discretionary, too. The cooling growth and weary consumers could pose a risk to profits in places near-term.



Past performance does not predict future returns. The views expressed above were held at the time of preparation and are subject to change without notice.

Source: HSBC Asset Management. Macrobond, Bloomberg, Datastream. Data as at 11.00am UK time 05 August 2024.

Key Events and Data Releases

Last week

Date	Country	Indicator	Data as of	Actual	Prior
Tue. 30 July	US	Consumer Confidence Index, Conference Board	Jul	100.3	97.8
	EZ	GDP, Prelim (qoq)	Q2	0.3%	0.3%
	MX	GDP, Flash (qoq)	Q2	0.2%	0.3%
Wed. 31 July	US	Fed Funds Rate (upper bound)	Jul	5.50%	5.50%
	JP	BoJ Policy Rate	Jul	0.25%	0.10%
	BR	Banco de Brazil SELIC Target Rate	Jul	10.50%	10.50%
	EZ	HICP, Flash (yoy)	Jul	2.6	2.5
	CN	NBS Composite PMI	Jul	50.2	50.5
Thu. 01 August	US	ISM Manufacturing Index	Jul	46.8	48.5
	MX	S&P Global Manufacturing PMI	Jul	49.6	51.1
	KO	CPI (yoy)	Jul	2.6%	2.4%
	KO	S&P Global Manufacturing PMI	Jul	51.4	52.0
	UK	BoE MPC Bank Rate	Aug	5.00%	5.25%
	EZ	Unemployment Rate	Jun	6.5%	6.4%

Q – Quarter **US – United States, EZ – Eurozone, MX – Mexico, JP – Japan, BR – Brazil, CN – China, KO – South Korea, UK – United Kingdom**

This week

Date	Country	Indicator	Data as of	Survey	Prior
Mon. 05 August	US	Earnings Update	Q2		
	US	ISM Services Index	Jul	51.0	48.8
Tue. 06 August	AU	RBA Cash Target Rate	Aug	4.35%	4.35%
Wed. 07 August	GE	Industrial Production (mom)	Jun	1.0%	-2.5%
	CN	Trade Balance (USD bn)	Jul	98.0	99.1
Thu. 08 August	MX	Headline Inflation (yoy)	Jul	-	5.0%
	MX	Banxico de Mexico, Overnight Lending Rate	Aug	-	11.00%
	IN	RBI Repo Rate	Aug	6.50%	6.50%
Fri. 09 August	BR	CPI (yoy)	Jul	-	4.2%
	MX	Industrial Production (mom)	Jun	-	0.7%

Q – Quarter **US – United States, AU – Australia, GE – Germany, CN – China, MX – Mexico, IN – India, BR – Brazil**

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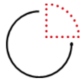

Market review

Global equities endured a sharp sell-off late in the week as markets digested disappointing economic data on US employment and manufacturing. It came after the Fed held rates steady ahead of expected policy easing from September, which triggered a fall in 10-year US Treasury yields. Mixed earnings news also played a part in the market-wide volatility, with 'big tech' stocks under pressure. Globally, the spillover was worst felt in Japan where the Nikkei 225 suffered a sharp reversal from recent all-time highs. Earlier last week, the Bank of Japan raised its policy rate to 0.25%. Elsewhere in Asia, India's Sensex fell for the week, but China's Shanghai Composite managed a modest gain. In commodities, the oil price was on course for its fourth consecutive weekly fall on signs of weak demand. Gold prices rebounded back towards record highs.

Note: Asset class performance on Page 1 is represented by the following indices:
US 60/40: Bloomberg EQ:FI 60:40 Index, Cash: JP Morgan Cash Index (3month), 10yr UST: ICE BofA 10yr US Treasury Index, Global Linkers: ICE BofAGlobal Inflation-Linked Government Index, Global IG: Bloomberg Barclays Global IG Total Return Index unhedged. Global High Yield Index: ICE BoFaUS High Yield Index, EMD Hard currency: US ABS: Bloomberg US ABS Floating Rate Total Return index; Bloomberg Barclays Global Aggregate Treasuries Total Return Index. EMD local currency JP Morgan EMBI Global Total Return local currency. Global Equities: MSCI ACWI Net Total Return USD Index. Value: MSCI Value Index, Growth: MSCI Growth Index, Global Emerging Market Equities: MSCI Emerging Market Net Total Return USD Index. China: MSCI China Index, India: MSCI India Index. Frontier: MSCI Frontier Markets Total Return Index, Alternatives: USD: DXY Index, Gold Spot $/OZ, Oil: WTI crude oil, Hedge funds: Credit Suisse Hedge Fund Index, Leverage Loans: JP Morgan liquid Loan Index, Infra Debt: iBoxx USD Infrastructure Total Return Index, Infra Equity: Dow Jones Brookfields Global Infrastructure Total Return Index, REITS Real Estate: FTSE EPRA/NAREIT Global Index TR USD. *Crypto: Bloomberg Galaxy Crypto Index.

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