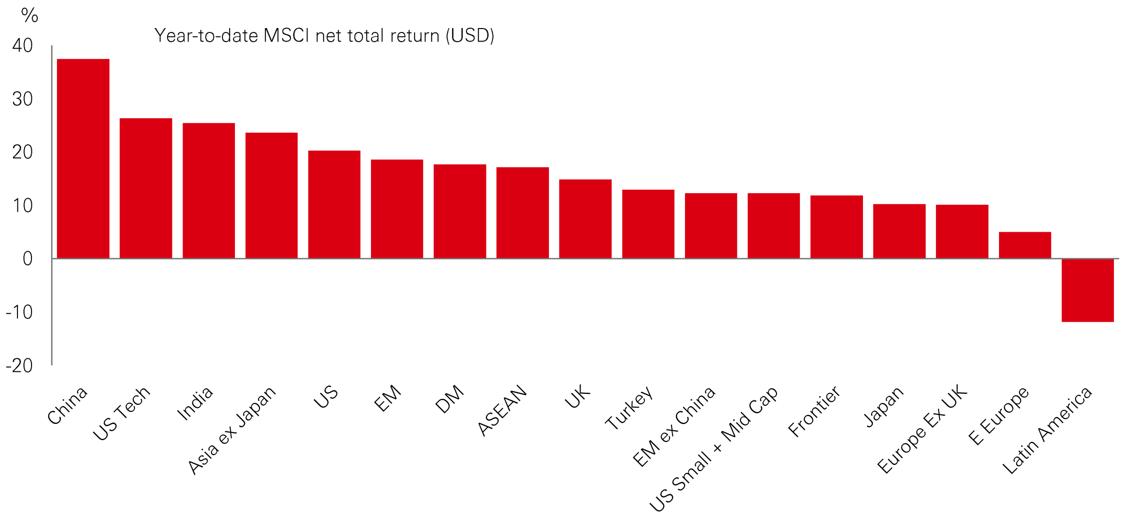
HSBC

Investment Weekly

7 October 2024

Chart of the week – Emerging markets are back



There were some remarkable twists and turns in the macro and market environment in Q3, and one of the biggest was the recent Politburo-endorsed package of support in China. That sparked a stunning rally in the country's stocks, which reversed China's laggard status this year, and put the **overall performance of emerging market stocks at +19% year-to-date, slightly ahead of developed markets**.

Policy was a major focus during the quarter, with the Fed finally joining the global easing cycle with a 0.5% rate cut. The backdrop to that move is that the economy remains on course for a soft landing. Despite some bumps, inflation continued its retreat, but growth also cooled, with mixed employment data causing volatility at times, particularly in early August.

In markets, a 'great rotation' in leadership was a strong theme. In developed markets, the 'Magnificent 7' were robust – rising around 4%, but there were more signs of a broadening out of returns and profit growth expectations across sectors and markets. Japan, Europe, and UK indices largely outperformed the US. And in the US itself, the small-cap Russell 2000 beat the S&P 500. Meanwhile, emerging market regions accelerated on a weakening US dollar and anticipation of rate cuts, with Asian regions setting the pace (see Market Spotlight), but Latam markets continued to lag. Across other asset classes, high quality fixed income performed as the global easing cycle progressed.

Market Spotlight

Emerging Asian assets lead in Q3

Stocks in mainland China and Hong Kong set the pace in Q3 – with a remarkable rally late in the quarter delivering gains of 23% and 24% respectively for MSCI indices. But even before that, weakness in the US dollar as Fed policy easing got started (and rate expectations were repriced) sparked a pick-up in the performance of EM Asian markets. ASEAN was notable, with the region's MSCI index up 19% in Q3. That was driven by a rebound in foreign inflows in response to the favourable FX environment, regional monetary easing, and a resilient macro backdrop. Thailand, the Philippines, and Malaysia led the gains. **Year-to-date, China, India, and Asia (ex-Japan) now lead global performance**.

EM Asian credits were also strong during the quarter, with Asia high yield a leading performer globally. In part, that was driven by well-performing names in markets like India and Indonesia. And from here, some specialists believe the default outlook is favourable with good funding access, strong balance sheets and a resilient macro backdrop for a vast majority of Asian companies.

Chinese Stocks →

How policy stimulus propelled Chinese markets

Rates Outlook →

Is Brazil's recent rate hike a warning for the Fed?

European Stocks →

Exploring the earnings outlook for European stocks

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

Lens on...

China's breathtaking rally

Recent stimulus announcements have sparked a dramatic recovery in China's stock market – making it the top-performing global market this year… and perhaps the strongest example yet of the great rotations we've seen in markets in 2024.

The gains are impressive. But the starting point was one of serial underperformance, connected to concerns about nominal growth. On valuation measures like 'earnings yield', there had been a large 'China discount', which gave stocks room to move sharply on better-than-expected news. It meant the stimulus was 'doubly good' for the market because investor sentiment had been so bad.

After a rally of historic proportions, some short-term caution is probably warranted. But the comprehensive liquidity measures mean that the 'policy put' is back. Further fiscal and credit stimulus will be crucial to make the market recovery sustainable, but China's policy stimulus, combined with Fed jumbo cuts, improves the odds that the global economy will stick to a soft landing.

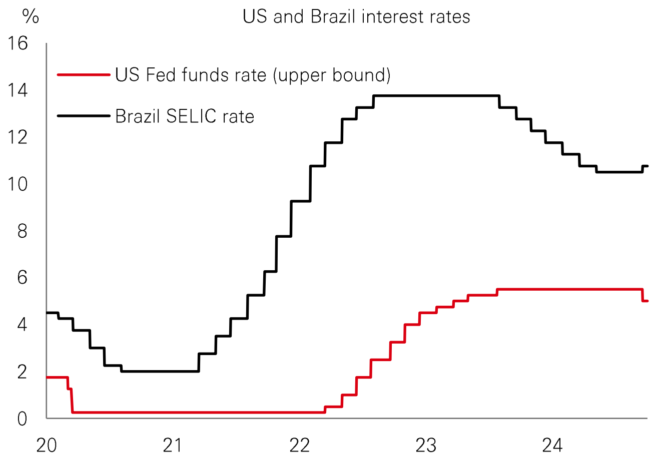
Brazil – a warning for the Fed?

Back in March 2021, Banco Central do Brasil (BCB) became one of the first major central banks to start hiking rates in response to the pandemic surge in inflation. As a global leader in the policy cycle, could September's BCB rate hike be a cautionary tale for the Fed, just as it kicks off its easing cycle?

Brazil's recent switch to policy tightening came a year after the country's leadership launched a public spending spree that fuelled domestic demand. Tight labour markets, a pick-up in wage growth, and a weaker Brazilian real have since proved inflationary.

For some onlookers, there are similar risks lurking in the US. November's US presidential election could result in a sizeable fiscal boost and shift tariff rates higher, while the US dollar remains on a weakening trend.

The comparison is off the mark. The fiscal boost wouldn't come until 2026, and the labour market and wider economy is cooling. But the potential shift in policies could mean a higher-than-expected endpoint for rates in this policy easing cycle, with consequences for longer-term investors.

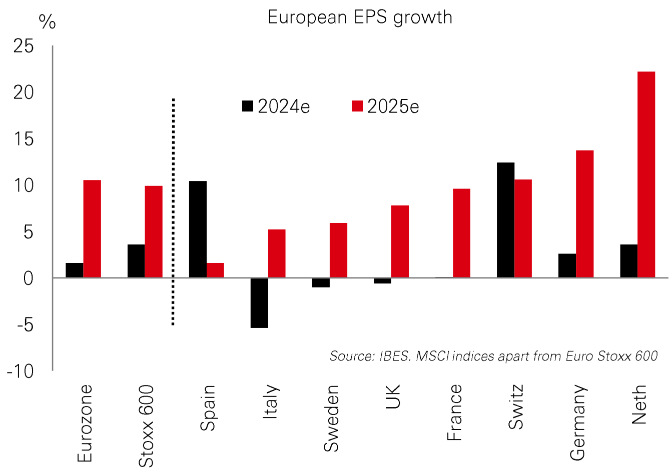


Conflicting signals for European profits

European stocks outperformed their US peers in Q3, helped by the 'broadening out' trade and their strong exposure to China, with investors seeking value outside the US. However, there is an intriguing disconnect between country-level macro data and profit growth expectations.

On the macro front, Europe is expected to grow in 2025, but recent activity data for Germany and France has been weak, with manufacturing PMIs well below 50. Germany's auto sector is struggling in particular. By contrast, the same industrial confidence surveys in Spain have been more positive. Meanwhile, the big drivers of wider European profit growth – which is expected to jump from 2-3% this year to around 10% in 2025e – are pencilled in as Germany and France. Both are forecast to move from low single digits in 2024e to 10-13% next year. But Spanish EPS growth is set to fall.

This apparent contradiction in the macro outlook and expected earnings growth implies scope for surprises.



Past performance does not predict future returns. This information shouldn't be considered as a recommendation to buy or sell specific sector/stocks mentioned. Any views expressed 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 October 2024.

Key Events and Data Releases

Last week

Date	Country	Indicator	Data as of	Actual	Prior
Mon. 30 September	CN	Official Manufacturing PMI	Sep	49.8	49.1
	US	Fed Chair Powell Speech at NABE Annual Meeting			
Tue. 01 October	JP	Tankan Business Conditions Manufacturing Index	Q3	13.0	13.0
	US	ISM Manufacturing Index	Sep	47.2	47.2
	US	JOLTS Job Openings	Aug	8.04mn	7.71mn
	BR	S&P Global Manufacturing PMI	Sep	53.2	50.4
	EZ	HICP, Flash (yoy)	Sep	1.8%	2.2%
Wed. 02 October	KO	S&P Global Manufacturing PMI	Sep	48.3	51.9
	MX	S&P Global Manufacturing PMI	Sep	47.3	48.5
	EZ	Unemployment Rate	Aug	6.4%	6.4%
Thu. 03 October	US	ISM Services Index	Sep	54.9	51.5
Fri. 04 October	US	Change in Non-Farm Payrolls	Sep	-	142k

The week ahead

Date	Country	Indicator	Data as of	Survey	Prior
Mon. 07 October	GE	Manufacturing Orders (mom)	Aug	-2.5%	2.9%
Tue. 08 October	US	NFIB Index of Small Business Optimism	Sep	91.7	91.2
	GE	Industrial Production (mom)	Aug	0.7%	-2.4%
Wed. 09 October	BR	CPI (yoy)	Sep	4.5%	4.2%
	MX	Headline Inflation (yoy)	Sep	4.6%	5.0%
	IN	RBI Repo Rate	Oct	6.50%	6.50%
	NZ	RBNZ Official Cash Rate	Oct	4.75%	5.25%
Thu. 10 October	US	CPI (yoy)	Sep	2.3%	2.5%
Fri. 11 October	KO	Bank of Korea Base Rate	Oct	3.25%	3.50%
	US	PPI (mom)	Sep	0.1%	0.2%
	US	Univ. of Michigan Sentiment Index (Prelim)	Oct	70.5	70.1
	IN	Industrial Production (yoy)	Aug	1.3%	4.8%

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Market review

Heightened geopolitical concerns weighed on risk markets, with oil prices climbing on rising supply worries. The US dollar DXY index was little changed. Core government bonds were mixed, with US Treasuries weakening on comments by Fed Chair Powell that there was no urgency to ease policy. Bunds rallied on dovish ECB comments. Global equities softened, with US stocks falling across the board, and the small-cap Russell 2000 faring worst. The Euro Stoxx 50 fell on growing concerns about the eurozone's economic outlook, while Japan's Nikkei 225 was little changed despite a weaker yen following comments by new LDP president Ishiba on monetary policy. In emerging markets, the Hang Seng rallied further, Korea's tech-driven Kospi index weakened, and India's Sensex index also lost ground in a holiday-shortened week. Copper and gold both consolidated following recent rallies.

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