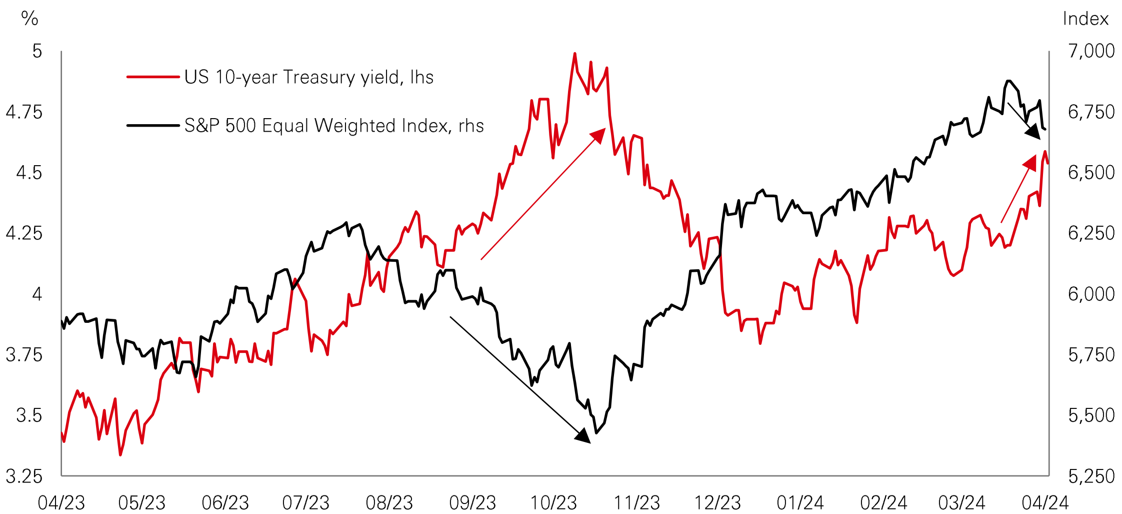
Investment Weekly

15 April 2024

Chart of the week – Higher bond yields pressuring stocks



US Treasury yields have risen markedly since the start of the year, with the 10-year yield jumping above 4.5% last week for the first time since mid-November. Market repricing of 2024 Fed rate cuts has been a big driver of the move. This has come amid upside inflation surprises – including last week's March CPI release showing broad-based stickiness in services inflation – and ongoing economic resilience, not least previous week's bumper payrolls print. And it has revived the 'higher-for-longer' investor narrative that was such a key feature of market action last autumn.

Despite yields creeping higher, year-to-date gains across the risk asset universe have been impressive. But there are signs that risk markets are beginning to wobble under the strain of higher risk-free rates.

With valuations in pockets of the market looking stretched, **a further leg up in bond yields could present a major challenge to risk asset pricing**. High uncertainty regarding the level of the neutral interest rate means longer-dated yields lack a credible anchor. This makes them sensitive to cyclical developments, or movements in commodity prices.

Most worrying would be if yield moves are driven by sticky inflation or supply-side concerns in the oil market, rather than strong activity.

Asian Stocks →

Looking at the strong performance in Asian equities in Q1

FX Volatility →

How diverging rates policies could cause currency market volatility

Fiscal Outlook →

The US fiscal policy outlook and what it means for multi-asset investors

Market Spotlight

Q1 results season – show us the earnings!

S&P 500 Q1 results season kicked off in earnest last week with big financials dominating the calendar early on. Full year 2024E consensus EPS growth stands at 10% overall, with profit growth of 3% in Q1 rising to 17.5% in Q4.

With the index on a hefty 21x price-earnings (PE) ratio, and rates still elevated, further significant multiple expansion looks challenging, with investors now demanding to see progress on earnings after a muted 2023.

Tech and communication services EPS growth remain at the top in Q1 (c. +20% y-o-y). Base effects are anticipated to boost Utilities. Five sectors are expected to decline including the cyclicals that rode the recent broadening-out rally, including Industrials, Energy and Materials as investors look beyond Q1. Any upside surprises here could support further market gains. In Financials, it looks more mixed with Banks weakest and Insurance strongest.

Analysts expect the costs of oil, shipping, transport and finance to fall back, even if wages are likely to remain a material headwind. Therefore, we will be closely monitoring outlook statements for signs that the expected H2 recovery in margins – baked into estimates – can materialise. Lastly, previous excitement over AI could also shift to more practical talk of near-term costs.

Source: HSBC Asset Management. Macrobond, Bloomberg. Data as at 11am UK time 12 April 2024.

Lens on...

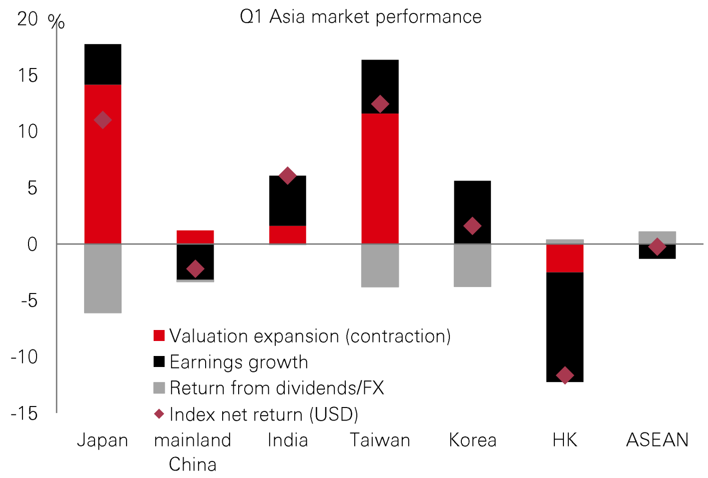
Promising run for Asia stocks

Asian stock markets enjoyed a good run in Q1. And although Japan was the regional outperformer, **Asia ex Japan outperformed both LatAm and EMEA**.

Amid the upswing in the semiconductor cycle, Taiwan notched up double-digit gains, beating Korea. But Korea's recently announced 'Value Up' programme – which aims to boost valuations and shareholder returns – will be a key area of investor focus.

Indian stocks extended last year's stellar run. By contrast ASEAN equities finished the quarter flat on a lacklustre growth outlook. But there are some interesting prospects within the bloc. The Philippines, for example, is gaining investor attention given cheap valuations, a healthy earnings outlook, and the prospects of big rate cuts by the central bank over the next year.

Perhaps the key move in Q1 was **in mainland China, where policy measures finally appear to have put a floor under prices**. Domestic growth and property sector headwinds persist.



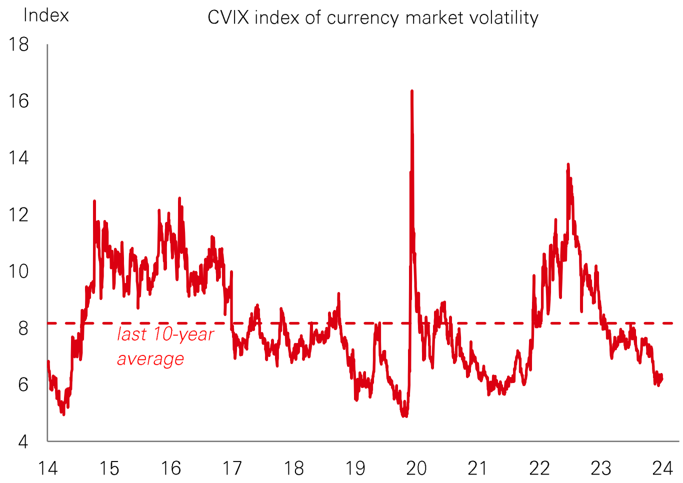
Fed affects FX

For a while now, currency market volatility has been very subdued. This echoes very low levels of implied equity market volatility as measured by the VIX index.

This may reflect growing investor confidence in the 'soft landing' narrative of resilient growth and disinflation across economies, and the idea that global central bank cutting cycles will be fairly synchronised.

The last week's US CPI data throws this scenario into doubt. Mounting evidence of sticky US services inflation contrasts with better progress on disinflation in Europe and in many parts of the EM universe. This raises the possibility of growing policy divergence, even if anxieties about FX-driven inflation pressures constrain how much easing outside of the US can be introduced.

As the inflation path becomes bumpier and disinflation becomes more dependent on domestic rather than global factors, there is a good chance currency volatility reignites in the coming months.



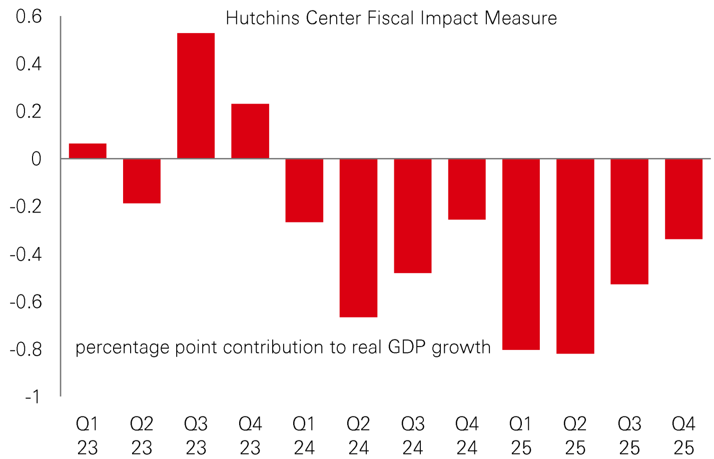
Don't forget about fiscal

The strength of private sector balance sheets explains a big part of why the US economy has been so resilient to the fastest policy tightening cycle since the 1980s. But fiscal policy has also helped.

Last year, business investment saw a modest boost from government incentives under the CHIPS and Science Act and Inflation Reduction Act. There was also a rebound in direct spending by federal and state governments.

But 2024 will be different. Fiscal policy is expected to be contractionary; a drag on economic growth. Previous monetary policy tightening may bite with a lag. And 'higher for longer' interest rates may mean that policy-makers risk recession to defeat sticky inflation. This creates some future risks for GDP and profits growth, and stocks too.

The longer-term fiscal arithmetic will be impacted by the outcome of the US elections. And that will be an important event for investors. **But the key point is that fiscal activism is back, and public deficits are likely to remain large**. **We're not heading back to the 2010s, and that has major implications for investors**.



Past performance does not predict future returns.

Source: HSBC Asset Management. Macrobond, Bloomberg. Data as at 11am UK time 12 April 2024.

Key Events and Data Releases

Last week

Date	Country	Indicator	Data as of	Actual	Prior
Tue. 9 April	US	NFIB Business Confidence Index	Mar	88.5	89.4
Wed. 10 April	US	CPI (y-o-y)	Mar	3.5%	3.2%
	CA	Bank of Canada Interest Rate Decision	Mar	5.00%	5.00%
	US	FOMC Meeting Minutes	Mar		
Thu. 11 April	CN	CPI (y-o-y)	Mar	0.1%	0.7%
	MX	Industrial Production (y-o-y)	Mar	3.3%	2.7%
	EZ	ECB Interest Rate Decision	Apr	4.00%	4.00%
Fri. 12 April	CN	Trade Balance (USD bns)	Mar	58.6	39.7
	KO	Bank of Korea Interest Rate Decision	Apr	3.50%	3.50%
	IN	CPI (y-o-y)	Mar	-	5.1%
	IN	Industrial Production (y-o-y)	Feb	-	3.8%
	US	University of Michigan Consumer Confidence Index	Apr P	-	-

P – Preliminary, F – Final **US – United States, CA – Canada, CN – China, MX – Mexico, EZ – Eurozone, KO – Korea, IN – India**

The week ahead

Date	Country	Indicator	Data as of	Survey	Prior
Mon. 15 April	US	Q1 earnings	Apr		
	EZ	Industrial Production (mom)	Feb	1.0%	-3.2%
	US	Retail Sales (mom)	Mar	0.4%	0.6%
Tue. 16 April	UK	Unemployment Rate (3 months)	Feb	4.0%	3.9%
	CN	Retail Sales (y-t-d)	Mar	5.4%	5.5%
	CN	Industrial Production (y-t-d)	Mar	6.5%	7.0%
	CN	GDP (q-o-q, SA)	Q1	1.6%	1.0%
	US	Housing Starts (mom)	Mar	-2.7%	10.7%
	US	Industrial Production (mom)	Mar	0.4%	0.1%
	US	IMF publishes World Economic Outlook	Apr		
Wed 17 April	UK	CPI (y-o-y)	Mar	2.9%	3.4%
	US	G20 Finance Ministers and Central Bank Governors Meeting	Apr		
Thu. 18 April	US	Existing Home Sales (mom)	Mar	-5.1%	9.5%
Fri. 19 April	MX	Retail Sales (mom)	Feb	-	-0.6%
	JP	Nationwide CPI ex fresh food & energy (y-o-y)	Mar	3.0%	3.2%
	IN	Indian People's Assembly Election	Apr		

Q – Quarter **US – United States, EZ – Eurozone, UK – United Kingdom, CN – China, MX – Mexico, JP – Japan, IN – India**

Source: HSBC Asset Management. Data as at 11am UK time 12 April 2024.

Market review

Risk assets took a pause for breath after disappointing US inflation data, with core government bonds weakening amid a re-pricing of US rate expectations. US Treasuries underperformed Bunds as ECB President Lagarde suggested a eurozone rate cut was imminent, probably in June, with a "few members" calling for immediate policy easing. US equities were mixed, with the rate-sensitive Russell 2000 faring worst but large-cap technology stocks recovering some lost ground later in the last week. The Eurostoxx 50 index moved sideways whilst Japan's Nikkei rebounded on a weaker yen. In emerging markets, China's Shanghai Composite index fell amid lingering deflation worries, while India's Sensex reached new highs before selling off later on the US inflation print. In commodities, ongoing geopolitical concerns are underpinning energy prices. Gold reached a new high.

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