Q2 / 2022

HSBC Jade Perspectives

Shaping your investment portfolio

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HSBC Jade

Contents

HSBC Jade Perspectives is a publication specifically created for our Jade clients.

It explores the key global themes relevant to today's investors, while explaining their diverse implications.

Enhancing portfolio resilience to capture opportunities

We welcomed 2022 with expectations of continued economic growth. More parts of the world gradually re-opened, and strong corporate earnings boosted market sentiment. Many policy makers were also prepared to support the economy until Covid-19 would fade.

Yet as inflationary pressures accelerated, the central banks shifted to a “hawkish” tone and led investors to feeling mixed. Escalated geopolitics also profoundly changed our assumptions and the near-term economic outlook. Inflation has risen due to concerns over the global energy supplies shock. This may hit consumer and business sentiment, leading to lower growth and spending.

As for the pandemic, developed markets with high vaccination penetration are cautiously adopting to “life with Covid”. But as Omicron makes a disruptive comeback in some geographies, it is a timely reminder that the pandemic-related risks remain.

So what does all this mean for investors?

High inflation, rising interest rates and geopolitics are driving financial markets. Despite this, we still don't expect a recession, especially for the US in the next 12 months where fundamentals are strong.

These top-of-mind issues mean that investors not only need to weather volatility, but also stay the course on longer-term objectives. Diversifying with a multi-asset approach and exercising selectivity are recommended to build up portfolio resilience.

We still favour equities and high quality bonds. The current environment will benefit sectors such as energy, financials and materials (to name a few). Quality continues to be key at this stage of the cycle, placing the focus on companies with robust balance sheets, sustainable profits and dividend pay outs.

We see good economic momentum in Asia, particularly in Southeast Asia which is the only region with a stronger GDP forecast than last year. Structural factors such as the Regional Comprehensive Economic Partnership should drive attractive consumer demographics, competitive supply chain dynamics and a shift to radical decarbonisation.

ESG factors are becoming more resonant around the world and we see more sustainable investing opportunities arising. Sustainable investments also lead to quality and corporate resilience. Companies with strong ESG practices tend to provide greater transparency and shape a business model that is better adapted to the future, ultimately benefiting profits and share prices.

In conclusion, in spite of the factors weighing down growth, we still have an appetite for riskier assets in the next 6 months. Diversification, exercising selectivity and staying invested in a resilient portfolio are the important measures to prepare for market volatility and to capture the rebound when it materialises.

Have a safe and fruitful investment journey.

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At a glance

A summary of Q2 2022 HSBC Jade Perspectives

Investment themes

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Be selective and balanced with sectors

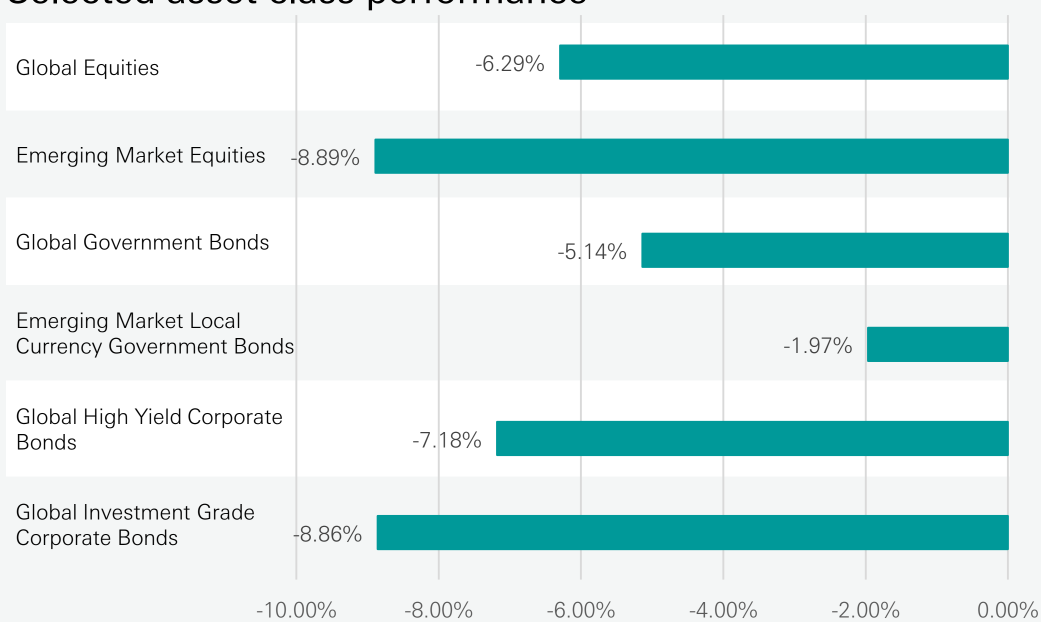
Investment views summary

Bonds	House View (6-months)
Developed Market Government Bonds	▼
Emerging Market Government Bonds (local currency)	▶
Global Investment Grade Corporate Bonds	▲
Global High Yield Corporate Bonds	▲

Equities	House View (6-months)
Global	▶
United States	▲
Eurozone	▼
United Kingdom	▶
Japan	▶
Emerging Markets	▶
Asia (excluding Japan)	▲

Note:
Views presented have a **6-month time horizon** on asset classes for a tactical asset allocation.
▲ "Overweight" implies a positive tilt towards the asset class, within the context of a well-diversified, typically multi-asset portfolio.
▼ "Underweight" implies a negative tilt towards the asset class, within the context of a well-diversified, typically multi-asset portfolio.
▶ "Neutral" implies neither a particularly negative nor a positive tilt towards the asset class, within the context of a well-diversified, typically multi-asset portfolio.
Source: HSBC Global Investment Committee, as of 17 March 2022.

Selected asset class performance



2022 Year-to-Date

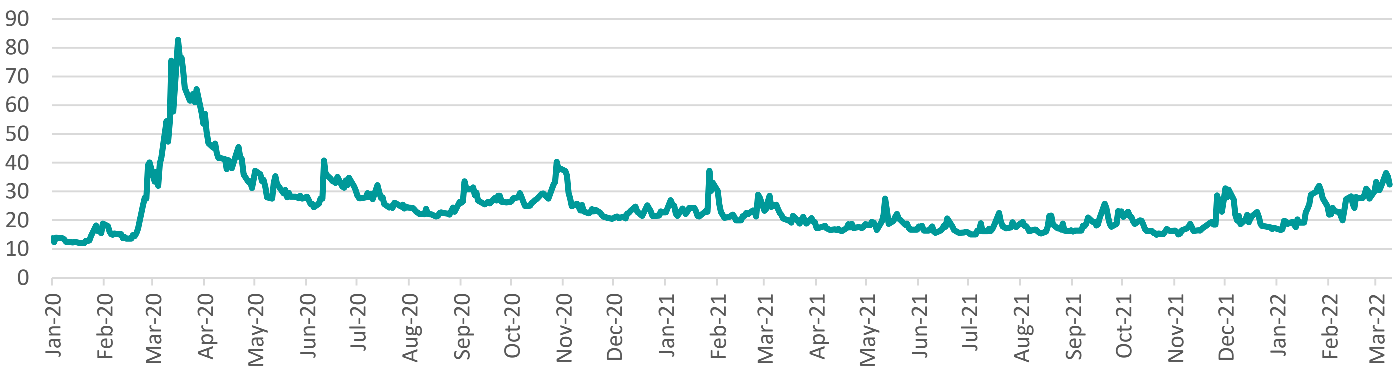
Source: Refinitiv Datastream, data as of 22 Mar 2022.

Note: the chart shows total returns of asset classes in USD dollar (USD). Asset class performance is represented by different Indices – Global Equities: MSCI ACWI Net Total Return Index (USD); Global Government Bonds: Bloomberg Barclays Global Aggregate Treasuries Total Return Index (Hedged, USD); Global High Yield Corporate Bonds: Bloomberg Barclays Global High Yield Corporate Total Return Index (Hedged, USD); Global Investment Grade Corporate Bonds: Bloomberg Barclays Global Aggregate Corporate Total Return Index (Hedged, USD); Emerging Market Equities: MSCI Emerging Net Total Return Index (USD); Emerging Market Local Currency Government Bonds: Bloomberg Barclays Emerging Market Local Currency Government Total Return Index.

Key charts to watch

Despite rising market volatility, it is trending lower than at the onset of Covid-19

The CBOE VIX Index



Source: Refinitiv Datastream, data as of 22 Mar 2022.

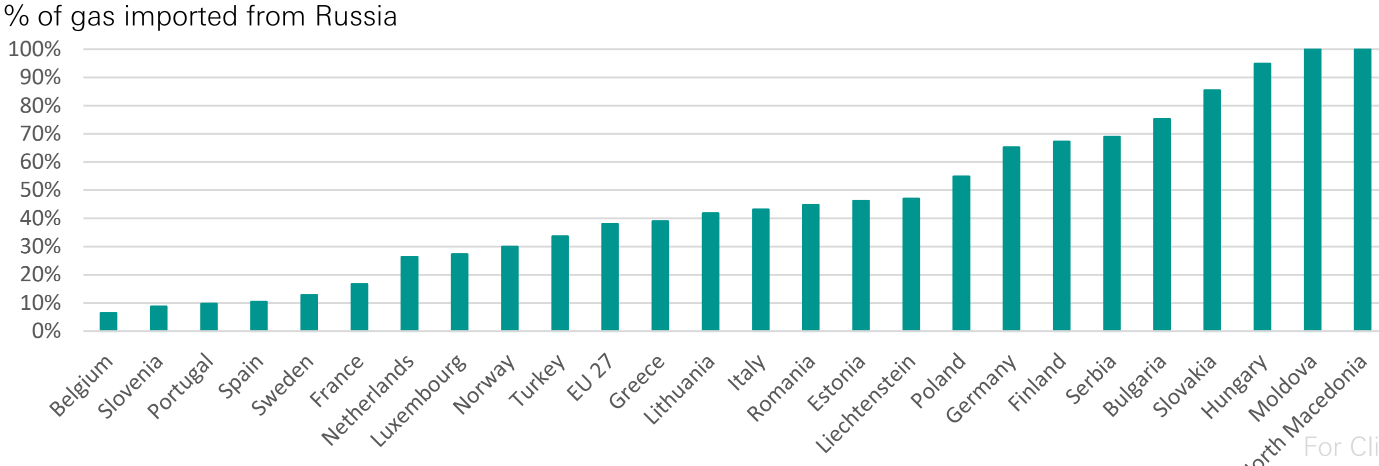
Structural policies favour growth prospects for Asian economies

	GDP		Inflation	
	2021f	**2022f**	**2021f**	**2022f**
Global	5.8	3.5	3.8	6.5
Asia	6.2	4.6	2.0	3.1
Mainland China	8.1	5.6	0.9	2.1
US	5.7	3.4	4.7	6.9
Eurozone	5.3	2.6	2.6	6.5
UK	7.5	4.3	2.6	7.6

Source: HSBC estimates as of 22 Mar 2022. Note: Aggregates are based on nominal GDP weights (GDP) and PPP-weights (inflation).

European economies are largely dependent on Russian natural gas

% of gas imported from Russia



Source: Refinitiv Datastream, Eurostat, data as of end 2020.

Four investment themes to help shape your portfolio

1 Build resilience in your portfolio

We don't anticipate a recession thanks to strong economic and earnings fundamentals, especially in the US. However, high inflation, tighter monetary policy, geopolitics and new waves of Omicron remain as risks. Short-term volatility is expected to continue.

The Russia-Ukraine conflict may edge inflation even higher over energy supply disruption. In key markets where policy normalisation has started, we are forecasting rate hikes of 1.75% by the Federal Reserve and 0.75% by the Bank of England, in total for 2022. We also forecast that the European Central Bank to raise rates of 0.5% up through to March 2023.

Building portfolio resilience is paramount in times of uncertainty. Investors should focus on quality companies with robust balance sheets and dividends as income sources. We're still positive on risky assets and prefer US, Canadian and Southeast Asian stocks. Fundamentals remain supportive in these markets who are home to sectors that benefit from current conditions (e.g. financials, energy and commodities). A multi-asset approach that incorporates high-quality bonds can help weather bouts of market volatility. Short-dated high yield bonds offer the best risk-reward profile against an uncertain rate environment.

Over the next 6 months, we prefer the following asset classes:

- **US, Canadian and Asian equities**
- **Global, US, European, UK and Asian investment grade and high yield bonds (particularly short-dated bonds)**

2 Capture strong growth in Asia

Southeast Asia's growth and attractive valuations are a standout: it is the only region with a stronger GDP forecast at 5.2% (vs 3.6% from 2021).[1] Economic re-opening is a dominant theme, with consumption expected to persist as markets embrace "living with Covid". Recovery will also benefit from higher commodity prices and the RCEP trade agreement.

Singapore's 2022 Budget reflects confidence in its growth trajectory in a post-pandemic world. The local stock market is skewed towards financials that offer attractive dividend yields and leverage into the domestic economy. We also see growth in Indonesia driven largely by consumption. As Southeast Asia's largest economy, it is supported by infrastructure expansion and abundant natural resources, including materials for electric vehicle components.

The National People's Congress sets a more accommodative tone in monetary policy, targeting growth and consumption recovery in Mainland China. A range of sectors are expected to benefit, including technology, manufacturing, infrastructure and a shift to green transformation. The structural factors provide economic support in the longer term.

Over the next 6 months, we're Overweight in Singaporean, Indonesian, Thai and Taiwanese equities, but remain Neutral on Chinese equities.

1 HSBC estimates as of 22 Mar 2022. Note: Aggregates are based on nominal GDP weights (GDP).

3 Seize the opportunities of net zero

According to the UN climate science body, human-induced climate change is causing widespread adverse impact. Some of such changes are irreversible, as human and natural ecosystems are beyond their ability to adapt.[2]

The risks of climate change grow with rising temperatures, and so will pressures mount for governments and corporates to live up to net zero pledges. Emissions removal requires acceleration of green innovation and resilient standards to prevent further vulnerability. We advocate investors to find opportunities in sectors such as power generation and infrastructure, transportation, buildings and industrials. The current supply shock that has pushed energy prices up highlights the need for diversification and affordability of sources, paving way to renewables.

Companies with robust ESG practices also tend to provide greater transparency and maintain longer-term shareholder values. Investors are increasing demand for clear and comprehensive climate disclosures to make informed investment decisions. Incorporating ESG metrics can also enhance portfolio resilience while generating long-term capital growth.

Focus on investment themes and companies exposed to renewable power, green infrastructure, clean transportation, energy-efficient construction materials and emissions reduction for industrials.

4 Be selective and balanced with sectors

We hold a balanced view between cyclical and defensive stocks, in anticipation of further softening of economic momentum and volatility from geopolitical tensions. We've recently upgraded defensive sectors like Healthcare to Overweight in the US and Consumer Staples globally to Neutral to add defensiveness to equities allocations.

Globally, energy remains our top pick as we expect prices to stay high, while financials will stand to benefit from rising rates. Rising commodity prices have also been a good tailwind for the materials sector, particularly in the metals and mining industry. In spite of recent volatility, we prefer technology as the world adjusts to a more convenient, digitally-empowered way of living. Selection, however, is tilted towards innovation such as online education, communications, e-commerce, entertainment and cybersecurity.

Over the next 6 months, we like the following global sectors:

- **Communications – increased data usage as more activity shifts online**
- **Energy (including renewables) – supply shortages continue to drive prices higher**
- **Financials – higher interest rates providing a more favourable environment**
- **Materials – commodity prices helping to drive the sector outlook**
- **Technology – the "new normal" generates further demand**

2 UN IPCC "Climate Change 2022: Impacts, Adaptation and Vulnerability", February 2022

▲ Asia (excluding Japan)

Relative to the US and Europe, the inflation pressures in Asia are less pronounced, allowing most central banks to hike rates much more slowly or keep them unchanged. We are Overweight in Asian stocks, particularly in the Southeast Asia sub-region. Singapore is well-positioned to benefit from global economic growth, while Indonesia's economy is supported by domestic consumption.

We also like Taiwanese stocks as they benefit from global demand in tech, 5G and semi-conductors.

We are Neutral on Mainland China and see that the market has attractive longer-term potential, especially in light of expected stimulus.

Over the next 6 months, we like:

- **The following sectors in Asia:** energy, financials and technology
- **Singaporean, Indonesian, Thai and Taiwanese equities**
- **Asian investment grade and high-yield bonds**
- **Mainland Chinese local currency bonds**

Regional market outlook

Japan

We hold a Neutral view in Japan in spite of relatively cheap valuations. The pandemic and supply chain issues have been holding back the economy, and although recent indicators are improving somewhat, those issues are not yet fully behind us and consumption is likely to remain muted. The expected global economic slowdown will be a headwind for Japan's exports and stock market, but some of its technology, machinery and engineering businesses could benefit from global business investment and the drive towards automation.

Our Neutral stance on Japan as a whole remains unchanged, as its economic growth is structurally weaker than that of its Asian neighbours.

United States

The latest earnings season is evidence that many domestic companies continue to generate good profits, even as costs increase. In times of stress, the US equity market benefits from its size and liquidity, especially as investors like holding USD-denominated assets.

The Fed's rate hike in March suppressed market concerns that inflation was potentially becoming long-term. The tech sector and other growth stocks have experienced a headwind from rising interest rates, but with six more rate hikes (for the rest of 2022) already priced in by markets, we believe that this headwind should start to ease. As a big energy producer, the US is less sensitive than Europe to high energy costs, and its energy, infrastructure and banking sectors tend to benefit from high oil prices.

Over the next 6 months, we like:

- US equities in general, particularly the following sectors: communications, energy, financials, healthcare, materials and technology
- US investment grade and high yield corporate bonds

Eurozone and UK

The Eurozone stock market has underperformed and we maintain our Underweight view due to the region's proximity to Ukraine, and sensitivity to energy supply disruptions. That said, we do not expect a recession or financial crisis, due to the low rate environment and generous liquidity provisioning by the European Central Bank.

The Bank of England has become more "hawkish" on monetary policy, although there are indications that they may take growth risks into account over the coming months.

Over the next 6 months, we like:

- The following European & UK sectors in particular: energy, financials and materials
- European & UK investment grade and high-yield bonds

EM EMEA and EM Latin America

Political uncertainties, viral spread and the uneven path to economic recovery are our primary concerns for Emerging Markets in both EMEA and Latin America.

We hold an Underweight position in EM EMEA for the next 6 months, as the region is furthermore impacted by a refugee crisis and higher energy prices. Business and consumer confidence are likely to remain very weak, weighing on economic activity and investor sentiment.

As for EMs in Latin America, whilst broader fiscal and macroeconomic challenges remain, higher commodity prices are likely to bring in greater revenues for Brazil. **We therefore upgrade our view on EM LatAm to Neutral for the next 6 months.**

Notes:
Views presented have **a 6-month time horizon** on asset classes for a tactical asset allocation. For a full listing of HSBC's house views on asset classes and sectors, please refer to our Investment Monthly issued at the beginning of each month.

"Overweight" implies a positive tilt towards the asset class, within the context of a well-diversified, typically multi-asset portfolio.

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HSBC Perspective

Transitioning to a circular economy

Travis Tucker
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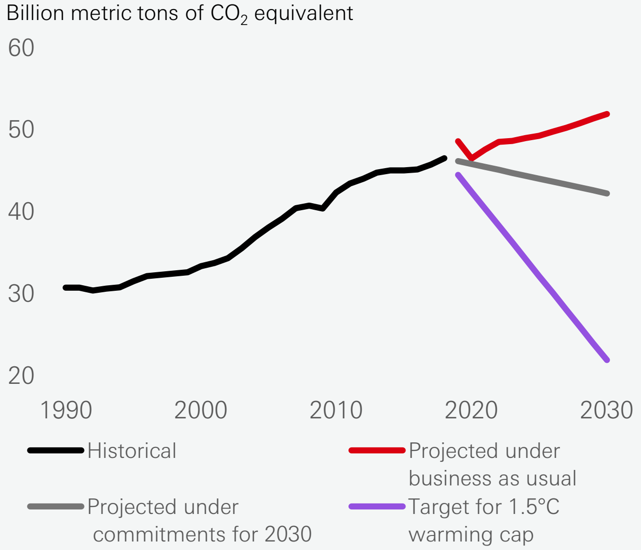
Geopolitics have exacerbated existing pressures on global energy supplies, pushing prices to new heights. To compensate, some governments have resorted to reopening coal plants, arguably one of the worst contributors to carbon dioxide (CO_2) emissions.

In the long run, this trend should accelerate investments into the renewable energy transition. After all, a locally-generated energy source means less reliance on other countries for supply. However, burning 'dirtier' fossil fuels in the near term only moves us further away from limiting global warming to a level that would avoid severe consequences.

Figure 1 – Total greenhouse gas emissions



Source: IMF, Climate Change Indicators Dashboard (October 2021)

At scale solutions beyond renewable energy are urgently needed. Transitioning to a more circular economy has as big a potential impact as any, and will drive much broader sustainability benefits.

What is a circular economy?

A circular economy refers to extending the lifecycle of products we use, and reusing materials to reduce resource consumption and waste. According to a report, the global rate of circularity, or recovered materials as a percentage of materials used, is currently less than 9%.[1] Accordingly, 70% of greenhouse gas emissions are directly linked to the extraction, transportation and use of materials. Doubling the circularity rate would reduce our global carbon footprint by 40% versus current trajectories.

Yet the importance of a circular economy extends far beyond this. The global population currently consumes 60% in excess of the resources that the planet can regenerate.[2] Beyond diminishing our finite resources, this also weakens nature and its ability to replenish.

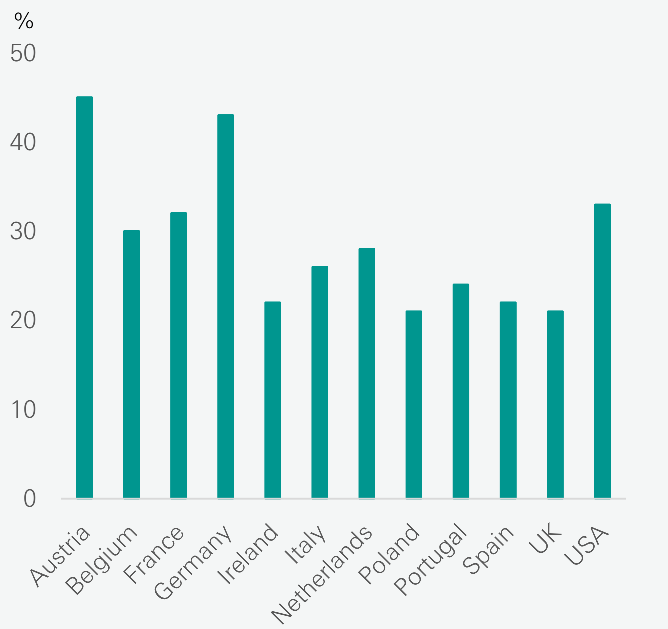
Since the turn of the century, the Amazon rainforest has become less resilient to disturbances such as droughts and land-use changes, with greatest losses in areas that were close to human activities (e.g. logging).[3] Researchers warn that once a critical threshold of vulnerability is reached, rainforests will become grassland. Given their role in storing carbon emissions, generating moisture and rainfall, and providing habitat for much of the world's species, the consequences cannot be overstated. Developing a more circular global economy lies at the heart of future economic and social prosperity.

Fortunately, a combination of sustainability-minded consumers, regulatory action and innovation in the private sector are planting the seeds of change. The European Union has taken the lead in regulating

1 Circularity Gap report, Circularity Gap Reporting Initiative
2 World Economic Forum, October 2021
3 Study by the University of Exeter, Potsdam Institute for Climate Impact Research (PIK) and Technical University of Munich, published in the Nature Climate Change journal, March 2022

disclosure around companies' circular economy contributions, or lack thereof. This is important to support necessary investment in circular activities. The introduction of a plastic tax and proposal for new rules on waste shipments encourage the shift to more circular business models. Consumers are also choosing products with better sustainability credentials, for example taking preference on clothing brands that prioritise the durability and recycling of materials.

Figure 2 – Consumers that are no longer shopping or shopping less with particular retailers (on sustainability grounds)



Source: Company data, Bloomberg Intelligence (November 2021)

A circular economy provides incentives for companies that extend beyond brand loyalty. Implementing circularity in supply chains and production processes can reduce input costs in the long run – the solar energy industry is an example. Currently, more than 4 million tons worth of solar panels are installed globally, accounting for over 40,000 tons of waste. Over the next few decades, we could reach 60 million tons worth of solar panels installed.[4] Recycling those panels can provide USD15 billion worth of raw materials for 2 billion new panels. Furthermore, silicon from solar panel waste can be repurposed for lithium-ion batteries, creating supply for another industry hampered by vulnerable supply chains and volatile input prices – electric vehicles.

Market considerations

Across industries, companies are rethinking business models that are dependent on an abundance of materials, prices of which have risen significantly. Technology has been a facilitator, enabling better engagement with customers across the product life cycle, supporting opportunities for repair and re-use programs. Companies leading change in these areas are building more efficient businesses, while strengthening brand loyalty.

There are also companies that are enabling change, with respect to circular packaging and shipping solutions, conversion of waste into energy and new products, and smart buildings and infrastructure solutions that drive efficiency.

Meanwhile, product sharing platforms are challenging the traditional approach of ownership altogether. This can be seen via the emergence of subscription services in many industries, such as fashion, vehicles or even camping equipment, where traditionally consumers bought and disposed of items, often after limited use.

The transition to a circular economy is in its early stages. High income countries currently rely on two-fifths of their materials from elsewhere in the world. Demand for those same materials is only growing elsewhere, with consumption from upper-middle-income countries doubling from 2000 to 2017.[5] A more circular economy can be a natural solution to this growing problem. Leaders in this transition have much to gain, generating opportunities for investors.

4 Bloomberg Intelligence, November 2021
5 United Nations Department of Economic and Social Affairs, 2020

Glossary

Alternative investments: a broad term referring to investments other than traditional cash and bonds and may include real estate, hedge funds, private equities and commodities investments, among other things. Some of these investments may offer diversification benefits within a portfolio.

Asset class: a group of securities that show similar characteristics, behave similarly in the marketplace, and are subject to the same laws and regulations. The main asset classes are equities, fixed income, and commodities.

Asset allocation: the allocation of funds held on behalf of an investor to various categories of assets such as equities, bonds and others, based on their investment objectives.

Company fundamentals: the intrinsic value of a company as analysed by looking at its revenue, expenses, assets, liabilities and other financial aspects.

Diversification: often referred to as "not putting all your eggs in one basket", diversification means to invest in a variety of different markets, products and securities to spread the risk of loss.

Fiscal policy: the use of government spending and tax policies to influence macroeconomic conditions such as aggregate demand, employment, inflation and economic growth.

Investment strategy: the internal guidelines that a fund follows in investing the money received from its investors.

Inflation: the rise in the general price levels of goods and services in an economy over a period of time.

Monetary policy: process by which the authorities of a country control the supply of money. This often involves targeting a rate of interest for the purpose of promoting economic growth and stability.

Quantitative easing (QE): also known as large-scale asset purchases, is a monetary policy whereby a central bank buys government securities or other financial assets from the market in order to increase the money supply and encourage lending and investment.

Strategic asset allocation: a practice of maintaining a mix of asset classes which should meet an investor's risk and return objectives over a long-term horizon and is not intended to take advantage of short-term market opportunities.

Tactical asset allocation: an active management strategy that deviates from the long-term strategic asset allocation in order to capitalise on economic or market conditions that may offer near-term opportunities.

Tapering: the reduction of the interest rate at which a central bank accumulates new assets on its balance sheet under a policy of QE.

Volatility: a term for the fluctuation in price of financial instruments over time.

Contributors

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Willem joined HSBC Private Banking in 2009 where his career has spanned Fixed Income, Investment Research, leading the UK Investment Group and most recently the role of Chief Market Strategist. He chairs the Global Investment Committee of the Global CIO Office for Private Banking and Wealth Management. Willem holds an MBA from the University of Chicago and an MSc from the University of Louvain (Belgium).

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Lucia Ku

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Lucia leads the Wealth Insights function with a focus on the development of its content strategy and delivery of key content initiatives to drive Insights consumption across different channels. She is also responsible for leveraging the firm's research capabilities to enhance our Insights offering to wealth management clients in Asia and globally. Previously, she has worked at a number of banks and asset managers, including HSBC Asset Management.

Maria Wu

Senior Wealth Insights Manager, HSBC Wealth and Personal Banking

Maria leads the creation of market insights, thought leadership initiatives and the delivery of an ESG-focused content strategy as part of HSBC's core investment philosophy. Previously, she has launched initiatives for HSBC Jade globally, connecting high net worth clients with tailored multi-channel services, exclusive lifestyle experiences (including client sustainability expeditions) and brand communications.

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Endnotes

Foreign securities carry special risks, such as exposure to currency fluctuations, less developed or less efficient trading markets, political instability, a lack of company information, differing auditing and legal standards, volatility and potentially, less liquidity. International investing including emerging markets involves a greater degree of risk and increased volatility that is heighted when investing in emerging markets. Foreign securities can be subject to greater risks than US investments, including currency fluctuations, less liquid trading markets, greater price volatility, political and economic instability, less publicly available information, and changes in tax or currency laws or monetary policy. Economies in Emerging Markets generally are heavily dependent upon international trade and, accordingly, have been and may continue to be affected adversely by trade barriers, exchange controls, managed adjustments in relative currency values and other protectionist measures imposed or negotiated by the countries with which they trade. These economies also have been and may continue to be affected adversely by economic conditions in the countries in which the trade.

Investors should consider the investment objectives, risks and charges and expenses associated with bonds before investing. Further information about a bond is available in the offering document. The offering document should be read carefully before investing

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