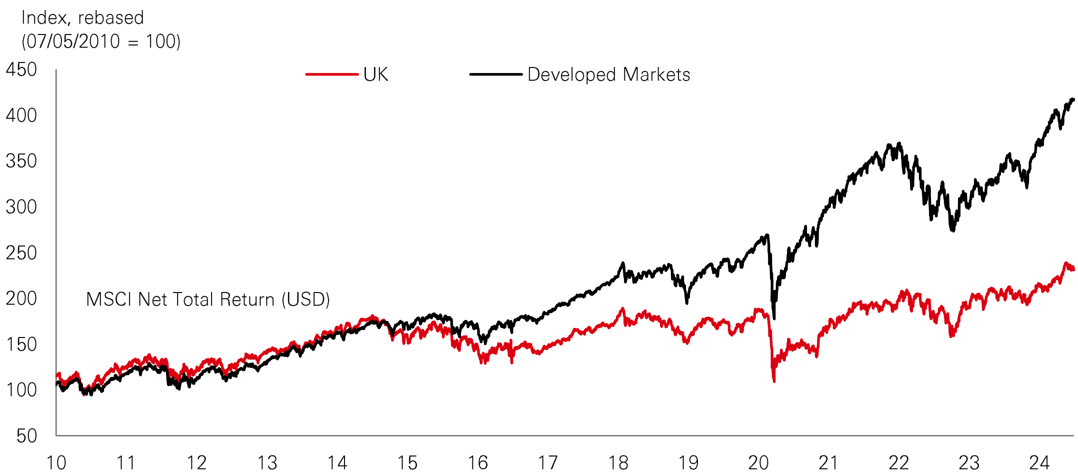
HSBC

Investment Weekly

8 July 2024

Chart of the week – UK stocks over the past 14 years



Last week's victory by the Labour Party in the UK general election marks the end of an era in British politics after 14 years of Conservative rule. During that time, investors have navigated a series of big macroeconomic and political events such as post financial-crisis austerity and eurozone turmoil, Brexit, the Covid pandemic and Russia's invasion of Ukraine. Through the twists and turns in the market, investors in UK equities have done reasonably well, with a net total return of 130% for the MSCI UK in dollar terms, even if this pales into comparison versus gains in overall developed market stocks.

What next for the UK stock market? The Labour Party will face a daunting task in its attempts to boost UK growth and productivity. Like elsewhere in the western world, public finances are stretched after the pandemic and 2022 energy shock, constraining public investment and demand-stimulus measures. Bond market investors are watching closely. And services inflation remains a bit sticky – perhaps due to structural issues such as long-term sickness.

Also, like European markets, the UK is a value play, an investment style that has not fared well over the past 18 months – growth and tech stocks remain en vogue. But as global profits broaden out and the UK economy recovers from last year's slump, there may be a reversal in fortunes. UK big caps can also benefit from a backdrop of resilient global growth. **And crucially, valuations matter for the longer run.**

Market Spotlight

India's bond boost

India's sovereign bonds finally joined the widely-tracked GBI-EM Global Diversified Index in the previous week. They will be phased in over the next 10 months, eventually achieving a maximum weight of 10%. It's an important move for both India's bonds and the rupee because it is likely to boost long-term capital flows.

It comes at a time when the country's external balance is in good shape, with an improving current account that was largely in balance at the end of Q1. But it wasn't always like this. Five years ago, India's FX reserves relied mainly on portfolio inflows, and persistent current account deficits meant its net external position was often on the backfoot. It meant the Reserve Bank of India spent a lot of time building FX reserves to defend the rupee against market volatility. More recently, India has been successfully building 'good quality' reserves. And its external vulnerabilities have been declining too.

Government Debt →

Why public finances are back in focus for investors

Alternative Assets →

Value opportunities in real estate and infrastructure

Trade Tensions →

What a rise in protectionist policies means for markets

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

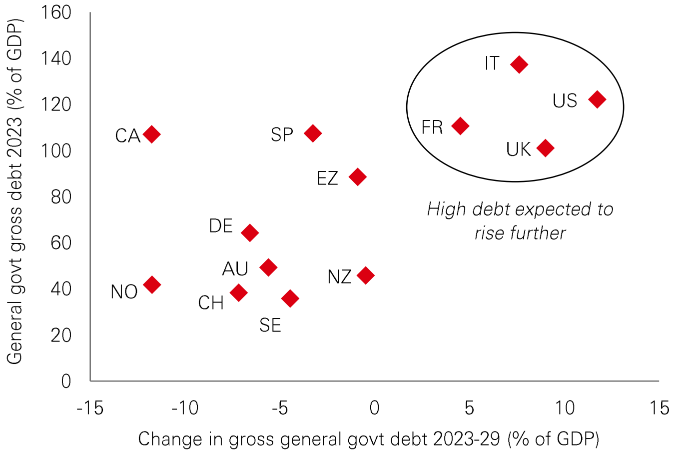
Lens on…

Debt sinners and saints

The French election has put the country's public finances back on investors' radar. Mooted policy proposals among challenger parties could mean fiscal loosening that would raise an already uncomfortably high debt burden. France is not alone in facing rising policy uncertainty against a backdrop of undesirable debt dynamics. The US goes to the polls later this year, while there is still some uncertainty surrounding the new UK government's fiscal plans.

Meanwhile, although Italy is not facing an election, it too stands out as having general government gross debt exceeding 100% of GDP which, according to the IMF, is expected to rise further over the remainder of the decade.

But what of other developed economies? Typically, they either have lower debt ratios or are forecast to see debt decline – many have both characteristics. This highlights that taking account of country-specific dynamics could play an increasingly important role in the higher interest rate environment. **It also emphasises the need for a diversified investment approach**.

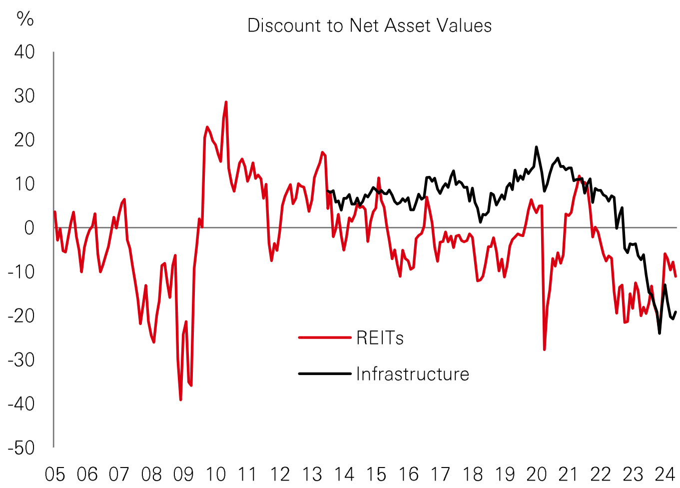


Time to get real

Higher rates in recent years have been tough on alternative asset classes like listed real estate and infrastructure. But with inflation easing, and central banks pivoting, there are signs that valuations will bottom out in 2024 – with activity and returns in both sectors poised for a pick-up.

In listed real estate (REITs), elevated rates have driven down property values and caused investment activity to slow, in part because of the higher costs of debt funding. Likewise, listed companies that develop, or invest in, major infrastructure projects have suffered. That's despite the sector benefiting from exposure to significant government spending in areas like energy transition.

But with both sectors trading well below their published net asset values (NAVs), **a valuation gap relative to global stocks has opened up**. Some alternative asset class specialists believe this could offer an attractive entry point for investors. Importantly, real estate and infrastructure can play a useful diversifying role in portfolios, offering defensive traits, inflation protection, and potentially attractive yields – but **careful stock and sector selection are key**.

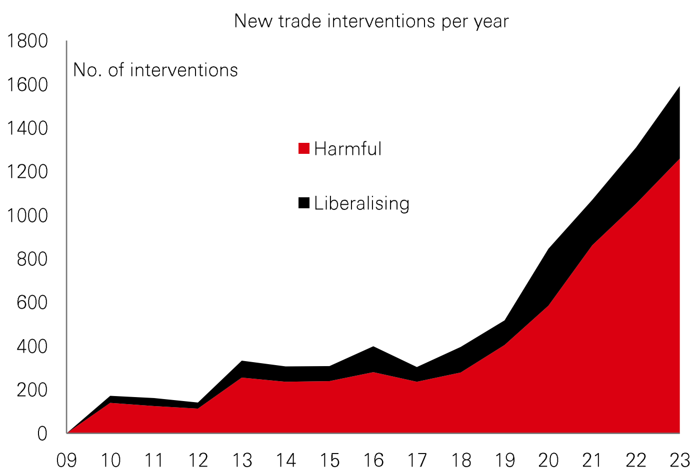


Multipolar world

It has been hard to disentangle economics from geopolitics in 2024, with signs that **the world is becoming increasingly multipolar**. One area we see this in evidence, is in global trade barriers and other protectionist walls, which are being thrown up at a remarkable rate. Data shows a surge over the past few years in trade-distorting measures – so-called 'harmful' trade interventions – such as tariffs and export bans.

This shift away from trade integration towards protectionism is fuelled in part by geopolitical and national security concerns. But it's also down to strategic competitiveness and underscores a wider move towards 'slowbalisation'. While there can be advantages, it's a trend that risks raising costs, disrupting trade, and restricting market access. And **for investors, that raises uncertainty**.

More broadly, we see a risk that trade interventions are one of a number of geopolitical events that could start to 'stack up' and affect the economic outlook. For investors, it could pay to be prepared for policy, political and geopolitical uncertainties that makes for a bumpier ride in markets in the second half of the year.



Past performance does not predict future returns.
Source: HSBC Asset Management. Macrobond, Bloomberg. Data as at 11.00am UK time 05 July 2024.

Key Events and Data Releases

Last week

Date	Country	Indicator	Data as of	Actual	Prior
Sun. 30 Jun	CN	Official NBS Manufacturing PMI	Jun	49.5	49.5
	FR	First round of French lower house elections	Jun		
Mon. 1 July	JP	BoJ Tankan Large Manufacturers Business Confidence	Q2	13.0	11.0
	CN	Caixin Manufacturing PMI	Jun	51.8	51.7
	US	ISM Manufacturing Index	Jun	48.5	48.7
Tue. 2 July	EZ	Consumer Prices (y-o-y)	Jun (P)	2.5%	2.6%
	PT	ECB Forum on Central Banking	Jul		
Wed. 3 July	CN	Caixin Services PMI	Jun	51.2	54.0
	US	ISM Services Index	Jun	48.8	53.8
	US	June FOMC minutes published	Jun		
Thu. 4 July	UK	General Election	Jul		
Fri. 5 July	US	Monthly Change in Non-farm Payrolls (000s)	Jun	-	272

P – Preliminary, Q – Quarter **CN – China, FR – France, JP – Japan, EZ – Eurozone, PT – Portugal**

The week ahead

Date	Country	Indicator	Data as of	Survey	Prior
Sun. 7 July	FR	Second round of lower house elections	Jul		
Tue. 9 July	MX	CPI (y-o-y)	Jun	4.9%	4.7%
	US	Fed Chair Powell testifies to the Senate Banking Committee	Jul		
	US	NFIB Business Confidence Index	Jun	89.0	90.5
Wed. 10 July	NZ	RBNZ Interest Rate Decision	Jul	5.50%	5.50%
	CN	CPI (y-o-y)	Jun	0.4%	0.3%
	BR	IPCA Inflation Index (y-o-y)	Jun	4.4%	3.9%
Thu. 11 July	KO	Bank of Korea Central Bank Interest Rate Decision	Jul	3.50%	3.50%
	US	CPI (y-o-y)	Jun	3.1%	3.3%
Fri. 12 July	CN	Trade Balance ($ bns)	Jun	83.7	82.6
	IN	CPI (y-o-y)	Jun	4.8%	4.7%
	IN	Industrial Production (y-o-y)	May	4.9%	5.0%
	US	University of Michigan Consumer Confidence Index	Jul (P)	67.0	68.2

P – Preliminary, Q – Quarter **FR – France, MX – Mexico, NZ – New Zealand, CN – China, BR – Brazil, KO – South Korea, IN – India**

Source: HSBC Asset Management. Data as at 11.00am UK time 08 July 2024. The views expressed above were held at the time of preparation and are subject to change without notice.

Market review

Dovish comments from Fed Chair Powell boosted risk markets. Core government bonds were range-bound as investors mulled uncertainty over the upcoming Presidential election and weak US data. US equities were mixed: the S&P500 reached an all-time high but the Russell 2000 lost ground. The Euro Stoxx 50 index rebounded, led by French equities. The spread between 10yr French and German bonds narrowed ahead of the second round of lower house elections in France. Japan’s Nikkei 225 reached record levels, aided by the yen’s continued weakness against the US dollar. EMs saw a mixed performance, with China’s Shanghai Composite index weakening on lingering growth concerns. India’s Sensex index moved higher, while Brazil’s Bovespa index rose on better fiscal news. In commodities, oil prices rose on improving summer demand. Gold consolidated, while copper was steady.