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Spinning Around

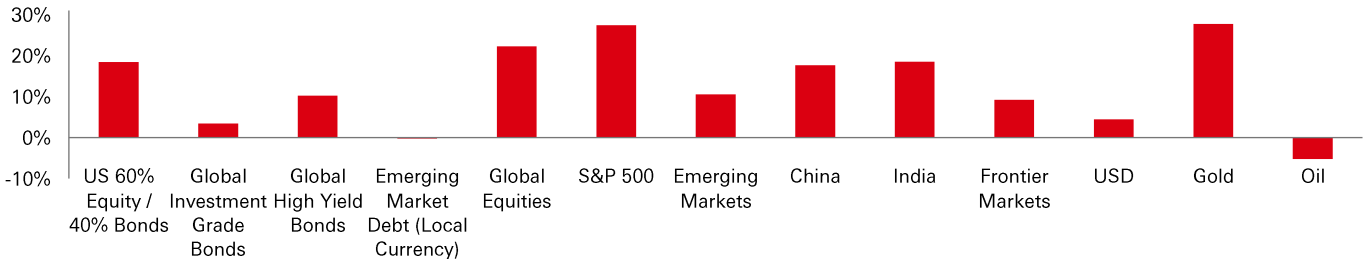


2025 Global
Investment Outlook

What's happened in 2024?

Declining inflation, resilient economic growth and improving corporate profits sum up the positive developments that have characterised the year. And with inflation down from prior sky-high levels, central banks have been able to start pivoting their policies, initiating a global interest rate cutting cycle in the latter half of the year. All of this has culminated in relatively good returns for investors.

Market returns (USD total return)

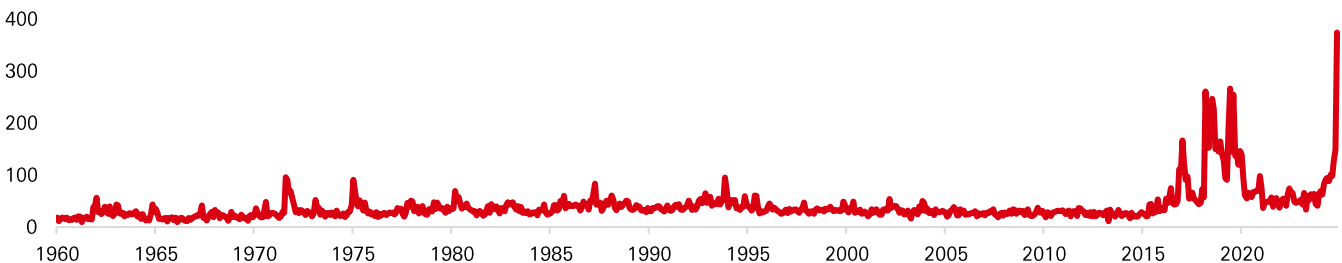


Source: HSBC Asset Management, Bloomberg, December 2024.

Looking forward

We are now in a 'multi-polar world' of economic fragmentation and competing trade blocs. Higher and more unpredictable inflation than we were used to in the last decade is a likely result — we are already seeing supply chains rerouted to higher cost locations. Plus, we know geopolitical tensions can spill over into commodity prices. These challenges reflect the evolving nature of economies and why we see continued rotations in market drivers.

Trade policy uncertainty has spiked and could rise further (trade policy uncertainty index)



Source: HSBC Asset Management, Macrobond, November 2024.

Past performance is no guarantee of future returns.

Any views expressed were held at the time of preparation and are subject to change without notice.



Revolving economies

Globally, growth patterns are shifting.

US growth is now moderating and expected to cool further in 2025, signalling a potential end to its post-pandemic 'exceptionalism'.

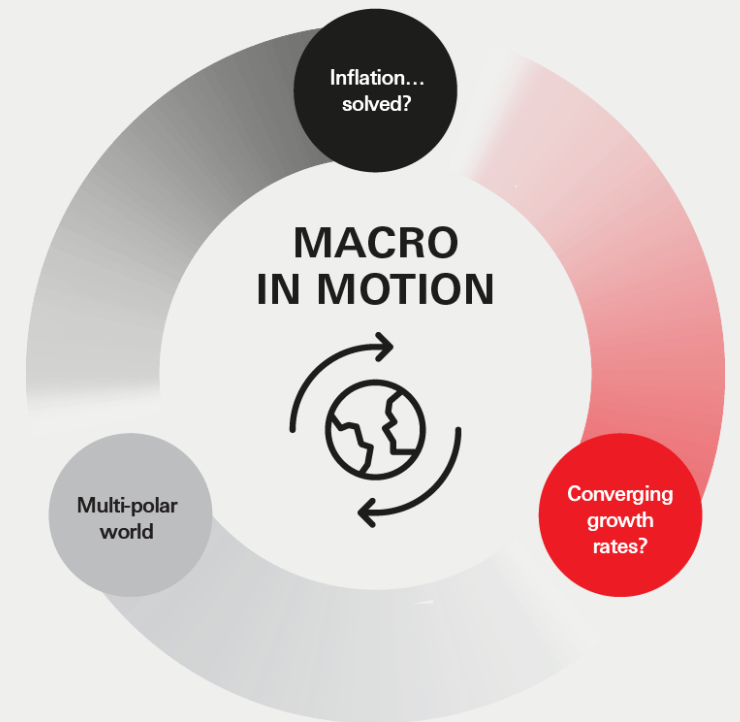
Meanwhile, low levels of productivity growth and a weak manufacturing sector are hobbling Europe's rebound, where economies largely remain 'in the slow lane' in their recovery path.

Emerging and frontier markets are projected to experience premium growth rates, with China benefiting from policy support and India maintaining its status as the fastest-growing large economy.

Importantly, expansion of the emerging markets growth premium – or economic growth in excess of developed markets – usually drives outperformance in emerging market assets.

Economies in motion

- The US is likely to secure a soft landing – where growth slows but remains positive – and this slower, but steady growth allows inflation to continue to moderate.
- As US growth cools, it will look less exceptional versus the rest of the world.
- But uncertainty around economic and trade policy across countries is rising. With the world becoming more 'multi-polar', this will create varying opportunities and challenges for individual economies.



Source: HSBC Asset Management, December 2024. Any forecast, projection or target where provided is indicative only and not guaranteed in any way. HSBC Asset Management accepts no liability for any failure to meet such forecast, projection or target. The views expressed above were held at the time of preparation and are subject to change without notice.



Shifting to new opportunities

Our expectations for economic and corporate profit growth to converge in advanced economies suggests that investment markets outside of the US have room to perform.

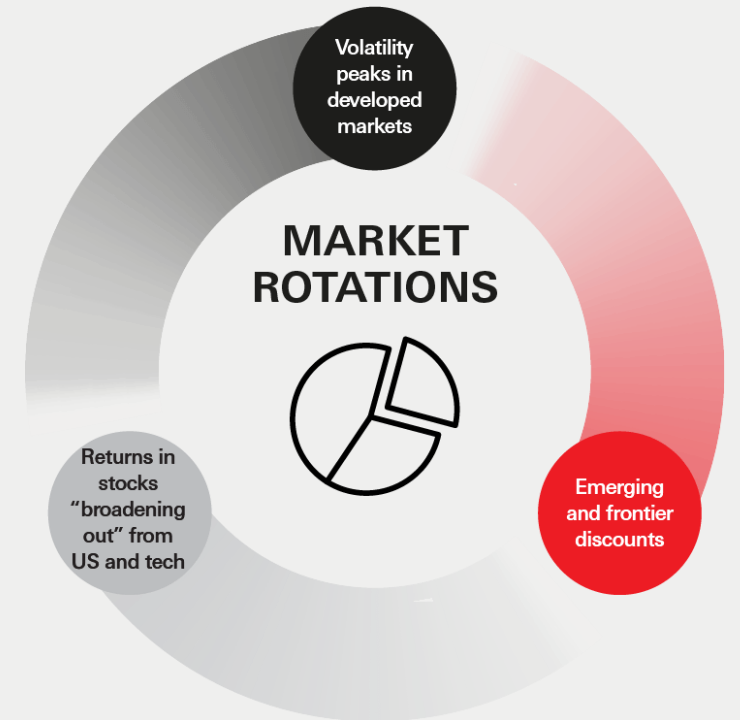
Neglected parts of global stock markets, such as less growth-oriented 'value' stocks, have an opportunity to catch up. In faster growing emerging markets — especially those less reliant on exports to the US — we could see outperformance on the back of cheaper valuations today.

Broadening profits growth could also produce a rotation within US equities towards neglected or defensive sectors that stand to benefit from policy actions, such as financials and industrials. Financials would benefit from potential deregulation and increased M&A, while some industrials may benefit from tariffs, even with higher input costs.

Additionally, less globally exposed companies may be shielded from trade policy impacts, which could continue to support recent resilience in small-cap stocks.

Market rotations

- Policy uncertainty means that investors need to be prepared for market volatility.
- Markets are primed to rotate:
 - higher-for-longer interest rates can have knock-on effects
 - stock laggards can become leaders
- Emerging and frontier markets trade at a significant discount, and have potential to deliver bumper returns.



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Turning to new diversifiers

A higher-for-longer interest rate environment also challenges traditional portfolio constructs.

With geopolitics potentially disrupting assumptions on the growth, profits, and inflation outlook, market volatility could easily pick up — leaving the most expensive parts of the market vulnerable.

Government bonds could struggle to protect against stock market downturns in an environment where interest rates stay elevated. This strengthens the need to incorporate alternatives into portfolios — those like private credit and real assets, along with the uncorrelated returns of hedge funds.

Likewise, asset-backed securities can help. They benefit from a higher-for-longer scenario given that they are floating rate instruments — meaning their coupon payments will rise if interest rates do. And today, they have high starting income levels alongside their low correlations to traditional fixed income — making them a useful portfolio diversifier.

Always an alternative

- A shallow rate cutting cycle creates opportunities in floating-rate private credit and asset-backed securities, with compelling yields on offer
- Equity strategies focusing on real assets provide a defensive route into the market
- Hedge funds and other alternatives become more important diversifiers in this new market regime



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Being active in emerging markets

Fed cuts and China stimulus, alongside a starting point of hefty valuation discounts, has meant a good 2024 for a broad range of emerging market asset classes.

Still, they remain unloved and under-owned by international investors, reflected in relatively cheap valuations. This means that any positive developments can lead to strong market reactions, as seen recently in China.

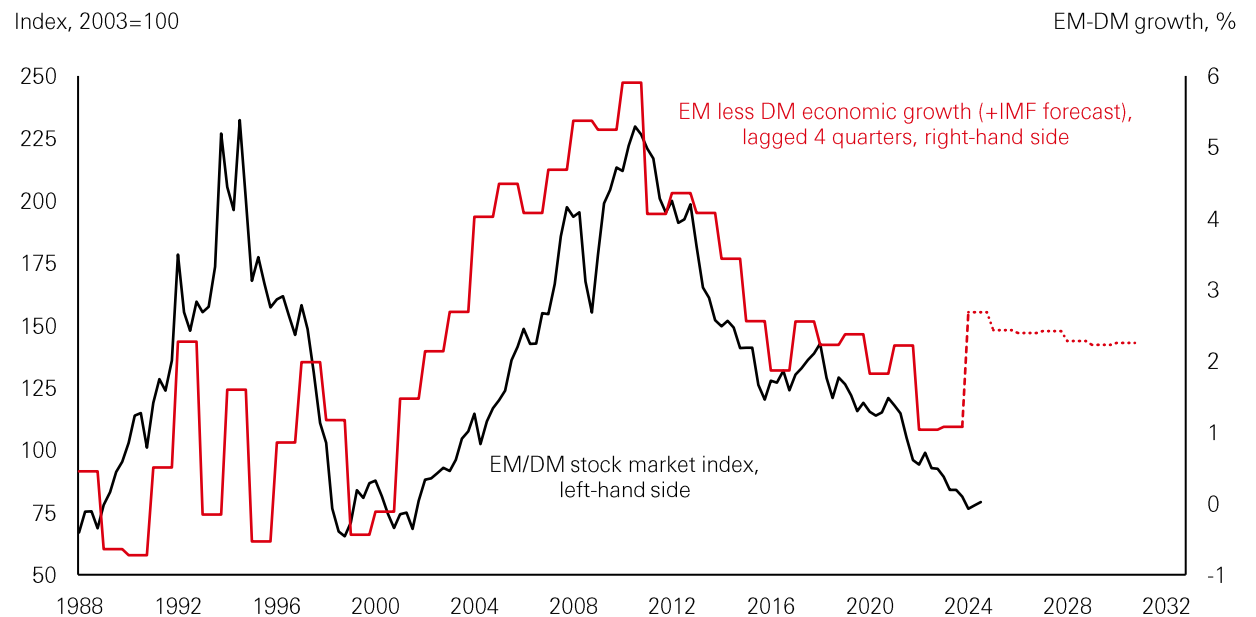
Unique prospects within emerging market countries also contribute to diversification benefits. However, given regions are performing so differently, and are facing different challenges, investors must do their homework when allocating to them.

India is set to maintain its position as the fastest growing major economy. Yet beyond India, the 'multi-polar world' presents opportunities for many Asian economies to exploit a restructuring of global trade patterns, as production is relocated to 'partner' countries.

While emerging markets should not be treated as one bloc, the US dollar outlook will play a role across all. Should US dollar strength at least moderate, this supports further potential for emerging market assets.

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Emerging market – developed market relative growth historically translates to stock market performance



Source: Bloomberg, HSBC Asset Management, November 2024.



Portfolios taking shape

Benefit from yields

Fewer interest rate cuts from the US Federal Reserve, and more issuance of Treasuries as government debt continues to grow, will put upward pressure on bond yields. This means fixed income investors can continue to benefit from relatively high yields available, but material capital appreciation will only arise if economic growth surprises to the downside and interest rate cuts become more aggressive. However, this is not our central scenario going into 2025.

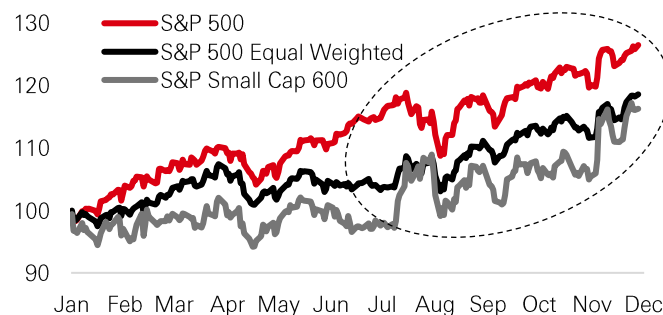
For this reason, we think bond segments less sensitive to interest rates — like asset-backed securities — look interesting. Their floating rate nature and high starting income levels make them stand out as portfolio options today. Additionally, low correlations to traditional fixed income reinforces their diversification appeal.

There are favourable options from high yields elsewhere in corporate bonds, with company balance sheets solid amidst a resilient global economy, but many segments are 'priced for perfection'. This leaves little buffer against any downturn in credit quality and increase in default risk.

Rotations in equities

Profit growth should be less concentrated in the US in 2025. This supports the case for non-US developed and emerging markets. Starting from low valuations, any good news can unlock performance. Within the US, returns have started to broaden from the tech sector.

Broadening out of returns within US equities

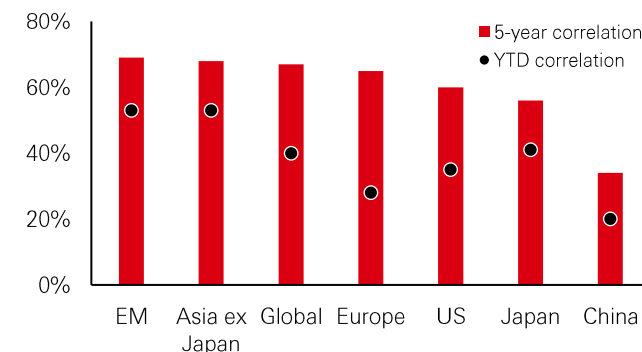


Source: Macrobond, HSBC Asset Management. 1 December 2024.

Broadening returns can help emerging markets, where there are compelling opportunities. However, risks such as a stronger US dollar and geopolitical uncertainties could impact sentiment, making us selective. Still, unique market characteristics offer diversification.

The below chart presents an example, showing a decoupling of India's markets from other major markets.

India equity correlation with respective markets



Source: MSCI, HSBC Asset Management, as of 16 September 2024.*

Always an alternative

Alternative assets can offer valuable resilience within multi-asset portfolios. Hedge funds, for instance, which are designed to deliver uncorrelated returns, have proven particularly useful during market downturns. Other options include private credit, where investors can benefit from high yields in floating-rate instruments, enhancing resilience amidst interest rate uncertainty.

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