HSBC World Selection Portfolios (AC)

Fund update

31 March 2024

Latest developments

- Global equities delivered another month of strong returns in March; supported by encouraging economic data, sustained enthusiasm for Artificial Intelligence, and the prospect of interest rate cuts. Fixed income markets also experienced a positive month, with government bonds, corporate bonds and high yield bonds all rising in value.
- Within equities, developed markets outperformed emerging markets. The UK was the standout performer over the month, driven by positive GDP growth in January and the latest business sector survey in expansionary territory. European stocks also delivered strong returns, as inflation continued to fall and business confidence data remained firm. Japanese equities gained over the month as the Bank of Japan ended their negative interest rate policy after eight years.
- In the bond markets, US Treasuries rose modestly, supported by dovish comments from Chairman Powell. In the UK, Gilts also experienced a modest rally following a softer than expected inflation print. Conversely, Japanese bond markets slipped marginally lower in March as the Bank of Japan removed their negative interest rate and yield curve control policies.
- The US dollar rallied over the month, driven by upward revisions in the US growth rate and some increase in support for interest rate cuts from other central banks. The Euro fell against the dollar given the relative strength of the US economic data and the persistent weakness in manufacturing data in the Eurozone. Sterling was flat against the dollar over the month.
- In the commodity markets, Gold rallied to all-time highs, driven by the prospect for rate cuts while Oil pushed higher, on elevated geopolitical tensions.

Impacts on the portfolios

- All major asset classes experienced positive returns during March, which resulted in positive absolute returns across all of the World Selection portfolios, with higher risk profiles outperforming lower risk profiles.
- The World Selection portfolios are actively positioned against a long-term asset allocation. During March, our active positioning added value. The biggest positive contribution came from our allocation to alternative asset classes, including Trend Following Hedge Funds and Gold. In addition, our tilt towards Spanish equity and the banking sector in Europe also added value. Conversely, our tilt away from Global High Yield and our preference for Brazil and India equity lost some value, while our tilt towards US Quality sector also detracted slightly.

Any performance information shown refers to the past and should not be seen as an indication of future returns.

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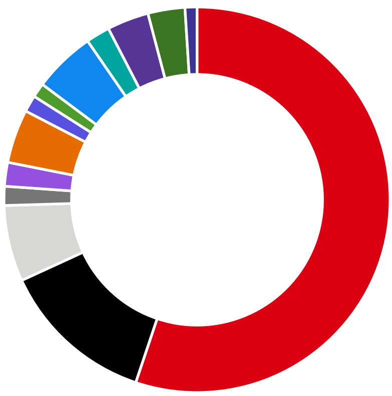
Asset class weightings % (HSBC World Selection 3)



Investment Team Views and Portfolio Positioning

Recession concerns easing

- We are increasingly confident that Western economies can avoid a recession and are now neutrally positioned in equity. The US economy looks particularly strong, providing further support for equity markets. We are conscious that some downside risks still remain; as such, we maintain a preference for higher quality companies that are likely to remain resilient in case of persistent inflation or risks to the growth outlook. We are tilted away from High Yield bonds and Property, as we believe the full impact of higher borrowing costs has yet to be priced in for these asset classes.

The rate cuts are coming…

- We expect major central banks to start cutting interest rates in the second half of 2024 as inflation continues to ease. This encourages us back into government bonds, which are (for the first time in almost a decade) delivering an appealing stream of income for investors. We are focusing our bond exposure on the regions where we believe rate cuts are most likely, for example the US and in March we introduced an exposure to German bonds. Conversely, we have reduced our holdings in Japanese bonds where we expect monetary policy to remain tight.
- We are holding Gold, which has historically benefited as interest rates fall, and is a useful hedge against geopolitical risk. We are holding increased exposure to the Norwegian Krona and Polish Zloty as inflation remains elevated in these markets, and we expect to continue receiving high interest payments on these currencies as their respective central banks delay cutting interest rates.

Outperformance in eastern and emerging markets

- The economic backdrop in markets such as India, Japan and Brazil is very strong, monetary policy settings are accommodative and there is room for fiscal support. We maintain a number of positions to gain access to the specific opportunities we see in these markets:
  - Japan versus developed market equity, given appealing valuations, strong flows from foreign investors, improved corporate governance, and weakening Yen supporting exports
  - Indian equity and government bonds: India remains one of the fastest growing economies globally, is making steady productivity improvements, has high foreign direct investments, and favourable demographics
  - Brazil versus emerging market equity given the country’s positive momentum, strong macroeconomic backdrop, and attractive fundamentals. We trimmed this position in February.
  - Mexican peso currency positioning, given the currency is benefitting from the strong growth story in Mexico and is attractively valued against developed markets currencies
  - Japanese Yen against Swiss Franc, given Japan's stronger inflationary pressure and potential for interest rate policy

In March, we entered a position in Chinese government bonds. We expect the central bank to continue the interest cutting cycle to boost growth, which should benefit bond prices.

Source: HSBC Asset Management, as at 31 March 2024.
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What’s next?

- The likelihood of Western economies avoiding a recession this year is increasing although markets remain ‘priced for perfection’, and disappointment remains a key risk. We are cognisant that geopolitical uncertainty, upcoming elections and fiscal constraints might impact markets later in the year. Economic performance remains divergent in emerging economies. India will be the fastest growing economy in 2024, while the China outlook remains challenged by several growth headwinds.
- We expect the first interest rate cut from the Fed during the second half of 2024, and the ECB and Bank of England are likely to follow. Lower government spending looks set to be a slight drag on growth in 2024 in Western economies, but we do not expect a return to 2010s-style austerity measures. We anticipate that Emerging market central banks will continue monetary easing, with cuts in Latin America and Emerging Europe. Asia central banks are likely to start cutting interest rates during second half of 2024. Government support in China remains measured and targeted.
- In light of the above, portfolios currently sit at a neutral risk setting. We remain selective within our equity exposure, holding a bias towards companies with earnings resilience. Fixed income yields are at attractive levels, and we are focusing our bond exposure on regions we expect to be first movers in monetary easing e.g. Europe and the US. We hold gold given its safe heaven properties and as an inflation hedge. Finally, given the brighter economic outlook, our portfolios are tilted towards select Eastern and Emerging markets, including Japan and India.

Key risks

The value of an investment in the portfolios and any income from them can go down as well as up and as with any investment you may not receive back the amount originally invested.

- **Counterparty Risk**: The possibility that the counterparty to a transaction may be unwilling or unable to meet its obligations.
- **Credit Risk**: A bond or money market security could lose value if the issuer’s financial health deteriorates.
- **Default Risk**: The issuers of certain bonds could become unwilling or unable to make payments on their bonds.
- **Derivatives Risk**: Derivatives can behave unexpectedly. The pricing and volatility of many derivatives may diverge from strictly reflecting the pricing or volatility of their underlying reference(s), instrument or asset.
- **Emerging Markets Risk**: Emerging markets are less established, and often more volatile, than developed markets and involve higher risks, particularly market, liquidity and currency risks.
- **Exchange Rate Risk**: Changes in currency exchange rates could reduce or increase investment gains or investment losses, in some cases significantly.
- **Interest Rate Risk**: When interest rates rise, bond values generally fall. This risk is generally greater the longer the maturity of a bond investment and the higher its credit quality.
- **Investment fund risk**: Investing in other funds involves certain risks an investor would not face if investing in markets directly. Governance of underlying assets can be the responsibility of third-party managers.
- **Investment Leverage Risk**: Investment Leverage occurs when the economic exposure is greater than the amount invested, such as when derivatives are used. A Fund that employs leverage may experience greater gains and/or losses due to the amplification effect from a movement in the price of the reference source.
- **Liquidity Risk**: Liquidity Risk is the risk that a Fund may encounter difficulties meeting its obligations in respect of financial liabilities that are settled by delivering cash or other financial assets, thereby compromising existing or remaining investors.
- **Operational Risk**: Operational risks may subject the Fund to errors affecting transactions, valuation, accounting, and financial reporting, among other things.

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Important information

For Retail Clients

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GD 0769. EXP 30/06/2024