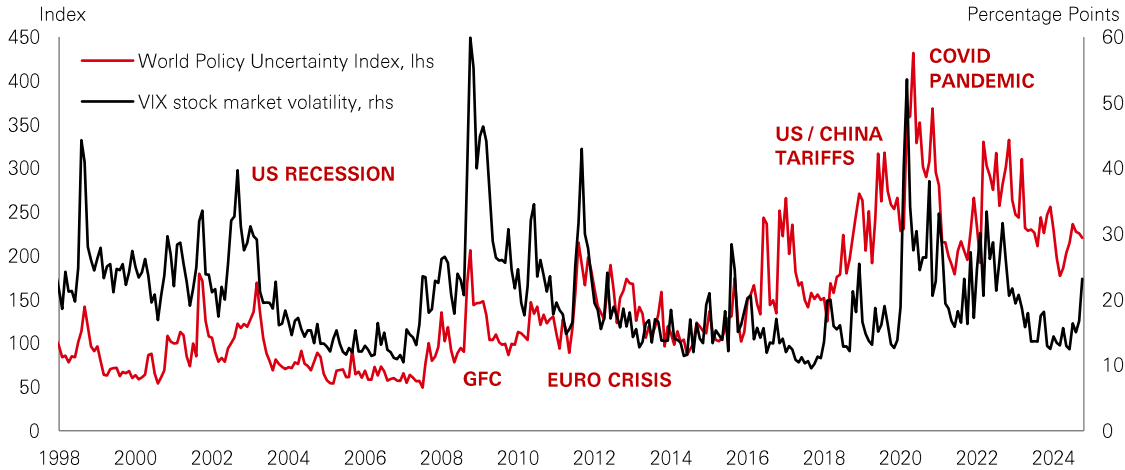




Investment Weekly

2 December 2024

Chart of the week – Will rising policy uncertainty push market volatility higher in 2025?



Rising uncertainty over economic and trade policy has been hanging over global markets in recent weeks. It's the kind of anxiety that typically goes hand-in-hand with higher stock market volatility. So far, most of the volatility has been in rates markets. And that's hardly surprising given uncertainty over the inflation outlook, particularly in a year when bond pricing has been hyper-sensitive to macro data.

Meanwhile, US stocks remain in a strong uptrend. But with market multiples pricing perfection (the S&P 500 hit another new high last week), bond yields still elevated, and growth cooling into 2025 – can calm conditions last?

In a "multi-polar world" of economic fragmentation and competing trade blocs, the most significant consequence for investors is a higher and more unpredictable inflation regime. This could constrain central bank policy easing, weighing on growth and corporate profits. Fixed income returns may still depend on yield income to support returns, and government bonds may not be a dependable hedge for portfolios. With geopolitics potentially disrupting underlying investor assumptions on the growth, profits, and inflation outlook, **market volatility could easily pick up, should the global news flow deteriorate - and the most expensive parts of the market could be vulnerable.**

Market Spotlight

Going private

Private credit has been a popular portfolio diversifier with investors in recent years – helped by an era of elevated rates that enhanced returns. But with central banks pivoting in the second half of 2024, a shift to lower rates has raised questions about whether that will change.

Yet, demand for private credit has remained robust. One explanation is that, while rates are on their way down, they are unlikely to fall to the very low levels experienced during the last decade. If rates begin to normalise at around 3%, it should leave room for private credit assets to deliver still-attractive all-in yields – particularly when compared to fixed-rate bonds. In fact, private credit premiums could potentially deliver a cushion as floating-rate yields decline. Another attraction is that private credit doesn't rely on an exit market to fund the distributions given that loans are repaid after a fixed period. This has been an important differentiator to private equity markets, where a weaker exit environment recently has led to lower distributions back to investors.

Despite recent growth, private credit only accounts for around 6% of corporate lending in the US – which is one of the most mature private credit markets.

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Source: HSBC Asset Management. Macrobond, Bloomberg. Data as at 7.30am UK time 29 November 2024.

Emerging Market Credit →

What potential trade tensions mean for EM bonds

Asian Equities →

Q3 sector winners and losers in Asian markets

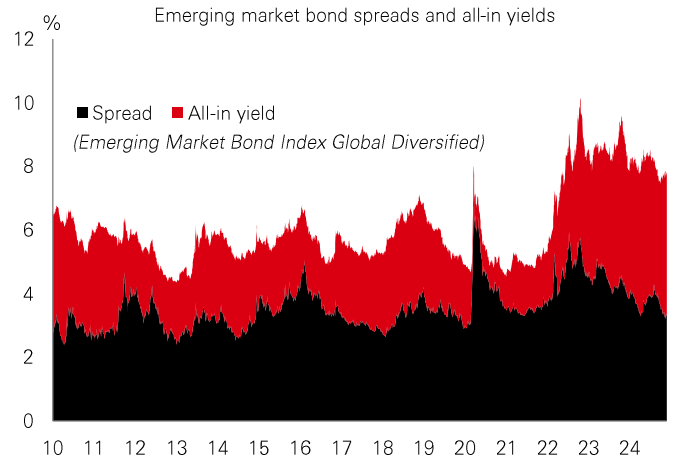
Currencies →

Why the euro is under pressure on multiple fronts

Upbeat on EM credit

Investor sentiment towards emerging markets (EM) has been cautious in the wake of US elections and growing concerns about tariffs. EM sovereign bonds (tracked by the EMBI index), for instance, are a high-duration asset class with a structurally improving average credit-rating outlook. If bond yields gradually grind lower globally, EM sovereigns could be well-placed to perform given their historically high all-in yields. **Spreads have compressed but are expected to remain well-behaved, thanks to a structural improvement in credit quality.**

That said, global risks remain high, which could impact the asset class. Worries about inflation and more active fiscal policy mean markets are pricing a shallower path for US monetary easing. And tariffs are unlikely to leave many EMs unscathed, with risks of a strong US dollar tightening global financial conditions. For EM investors, country sensitivity to these headwinds will depend on factors like existing free trade agreements, relationships with the new US administration, and the degree of trade exposure that they have to the US.



Asia's solid earnings

Asian stock markets have delivered decent performances this year, with mainland China and India setting the pace. But as Asia's Q3 earnings season rolls on, we've seen regional variations in terms of sector winners and losers.

Technology-led markets in South Korea and Taiwan are still the region's profit engine. **Strong demand in industries like semiconductors and hardware has been potent, particularly in South Korea, which has seen a strong rebound in profits growth.** In Japan, Q3 has also been solid, with financial stocks the big driver on improving margins. But its discretionary stocks have lagged, with profits falling among automakers. In mainland China, financial stocks (particularly insurance firms) have underpinned robust Q3 profits growth, and firms in hardware and e-commerce have been strong too.

By contrast, profits in India have surprised to the downside. But weak macro momentum in the quarter is expected to recover, and sectors like financials, healthcare, and real estate have performed well. Overall, some specialists continue to see **fair valuations across the region, as well as solid growth and appealing economic diversification.**



Euro woes

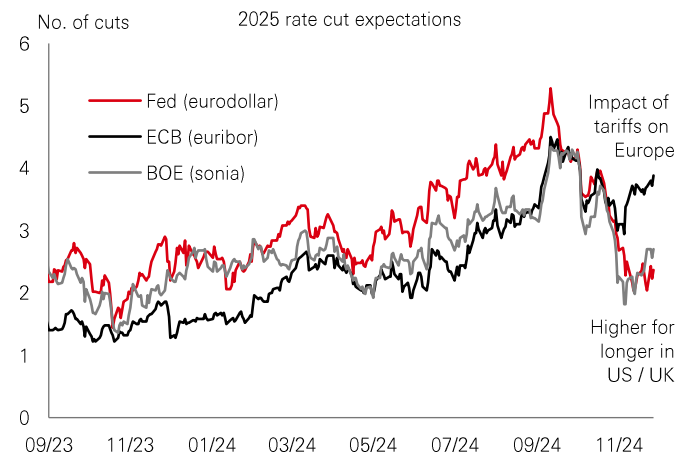
In addition to concerns about potential changes to US trade policy next year, the Eurozone is already dealing with its own fair share of problems – much of which are weighing on the euro.

Growth has weakened again, with manufacturing PMIs in France and Germany in the low 40s and services failing to do enough to produce positive growth. Then there is political uncertainty, with general elections in Germany in February and ongoing instability in France.

These risks have led to a sharp repricing in the relative outlooks for growth and monetary policy. Markets have priced in more aggressive monetary easing by the ECB, just as Fed rate cuts have been priced out.

The result is the euro has weakened in the face of a strengthening US dollar – and the next few months could be challenging.

The good news is a weaker euro supports domestic exporters, despite near-term caution on the profits outlook. Likewise, ECB rate cuts should boost both the macro outlook and government bonds.



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Key Events and Data Releases

Last week

Date	Country	Indicator	Data as of	Actual	Prior
Tue. 26 November	US	Consumer Confidence Index, Conference Board	Nov	111.7	109.6
	US	S&P Case-Shiller 20 House Prices (mom)	Sep	0.2%	0.3%
	US	FOMC Minutes	Nov		
Wed. 27 November	US	PCE Price Index (yoy)	Oct	2.3%	2.1%
	NZ	RBNZ Official Cash Rate	Nov	4.25%	4.75%
	US	GDP, 2nd Estimate (qoq annualised)	Q3	2.8%	2.8%
	EZ	Comments by ECB Executive Member Isabel Schnabel	Nov		
Thu. 28 November	KO	Bank of Korea Base Rate	Nov	3.00%	3.25%
Fri. 29 November	JP	Tokyo CPI excluding food and energy (yoy)	Nov	1.9%	1.8%
	EZ	HICP, Flash (yoy)	Nov	-	2.0%
Sat. 30 November	CN	NBS Composite PMI	Nov	-	50.8

US - United States, NZ - New Zealand, EZ - Eurozone, JP - Japan, KO - South Korea, CN - China

The week ahead

Date	Country	Indicator	Data as of	Survey	Prior
Mon. 02 December	US	ISM Manufacturing Index	Nov	47.5	46.5
	BR	S&P Global Manufacturing PMI	Nov	-	52.9
	MX	S&P Global Manufacturing PMI	Nov	-	48.4
	CN	Caixin Manufacturing PMI	Nov	50.6	50.3
Tue. 03 December	US	JOLTS Job Openings	Oct	7.51mn	7.44mn
	BR	GDP (qoq)	Q3	0.7%	1.4%
Wed. 04 December	US	ISM Services Index	Nov	55.5	56.0
Fri. 06 December	US	Change in Non-Farm Payrolls	Nov	200.0k	12.0k
	IN	RBI Repo Rate	Dec	6.50%	6.50%
	US	Univ. of Michigan Sentiment Index (Prelim)	Dec	73	71.8

US - United States, BR - Brazil, MX - Mexico, KO - South Korea, IN - India

Source: HSBC Asset Management. Data as at 7.30am UK time 02 December 2024. For informational purposes only and should not be construed as a recommendation to invest in the specific country, product, strategy, sector or security. Any views expressed were held at the time of preparation and are subject to change without notice.



Market review

Risk markets were stable, with the US dollar index correcting lower amid rising trade tensions. Core government bonds rallied as investors digested the latest appointments to the forthcoming US administration. Rising budget concerns prompted a wider 10yr yield spread between French and German government bonds. US equities posted modest gains in a holiday-shortened week, whereas the Euro Stoxx 50 index softened, led by a weakness in French stocks. Japan's Nikkei 225 reversed earlier gains last week as the yen rebounded versus the US dollar. Emerging market equity performance was mixed. China's Shanghai Composite and India's Sensex advanced, while Korea's KOSPI index dropped on lingering worries over domestic macro outlook and geopolitical risks as the BoK delivered a surprise rate cut. In commodities, oil and gold consolidated. Copper edged higher.

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