News Release

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HSBC PRIVATE BANK 2017 INVESTMENT OUTLOOK: GO WEST OR EAST

Bond Yield to Come Down, Focus on Growth Opportunities in the US & Asia

Following a surprising and turbulent 2016, global financial markets will continue to be driven by political events and policy uncertainty, setting the new year against an equally challenging backdrop. Underpinned by global political uncertainty and prolonged market volatility, domestic factors and structural growth will be the main performance drivers in 2017, with the most attractive growth opportunities present in the US and in Asia, according to HSBC Private Bank's 2017 Investment Outlook report.

HSBC Private Bank believes global diversification and a balanced portfolio strategy will be crucial for Asian investors who seek for stable returns with controlled risk. HSBC Private Bank expects a moderate improvement in global growth outlook in 2017, driven by more expansionist fiscal policies under the Trump administration, sustained growth stabilisation in China and recovery of the oil producers in emerging markets. Global GDP growth is forecast to accelerate to 2.5% in 2017 from 2.2% in 2016, driven by better growth in the US and emerging markets. Within the global equity portfolios, HSBC Private Bank is overweight on US and Asian equities as it sees better growth opportunities in the two markets as compared to Europe which is plagued with structural challenges and political uncertainties.

"Investors are confronted with two major structural challenges in 2017: the political uncertainty in Europe and the UK, and the increasingly uncertain global trade environment. To mitigate the lingering effects of these risk factors, a disciplined and selective investment approach will be necessary. Besides US equities, we are overweight equities in China, India and Indonesia, which are expected to outperform the regional peers due to their domestic-demand driven growth, positive progress of structural reforms and supportive policies," said Fan Cheuk Wan, Head of Investment Strategy, Asia, HSBC Private Bank. "We believe that their resilient domestic fundamentals and structural growth drivers would contain the potential damage from growing trade protectionism under the new US administration."

HSBC Private Bank highlights four themes that will move the market's direction and shape its investment strategy for 2017.

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(1) Bond yields to come down again

Financial markets have enthusiastically priced in the potential reflation of the US economy under the Trump presidency, but the danger is that the aggressive price action may get ahead of fundamentals. HSBC Private Bank believes the current yield level is unsustainable and forecasts US 10-year Treasury yield to come down again after peaking in the first quarter of 2017, as the all-time high US government debt levels could push the costs of debt servicing to unsustainable levels. The strengthening USD has already led to an overall tightening of financial conditions, thus limiting the need for any rapid interest rate hikes in the US.

"We expect US 10-year Treasury yield to edge down after the first quarter of this year and then move towards 1.35% by the end of 2017. In our view, medium to long-term structural drivers, including global economic challenges, quantitative easing in Europe and Japan, elevated debt levels globally, should constrain the scope of the Federal Reserve to raise interest rates," said Fan. HSBC economists expect only two 25-basis point rate hikes by the Federal Reserve in 2017, followed by one rate hike in 2018. "We also maintain our positive view on US investment grade and high yield bonds and emerging markets hard currency bonds as we believe any reversal of US yields after the first quarter of 2017 should support the global search for yield and recovery of the credit market," Fan added.

To achieve portfolio risk diversification, HSBC Private Bank stays overweight on gold, which offers an effective investment instrument to hedge against political risks and inflation threat. The recent correction in gold price should provide a good strategic entry point when investor fears of rapid US rate hikes ease in the coming months.

(2) Asia's structural growth

In a low growth and low return environment, Asia offers attractive growth opportunities underpinned by strong domestic demand, positive structural reform progress, monetary and fiscal easing and favourable demographics. Asia is in a reasonably strong position to withstand global headwinds from Brexit and a potential increase in trade protectionism, given ample policy ammunition of Asian policymakers to ease monetary conditions and introduce fiscal stimulus to support GDP growth.

HSBC Private Bank stays positioned in Asian companies exposed to structural growth and reforms as they are resilient to withstand cyclical volatility in the global economy and impact of trade protectionism. "In China, increased risk of trade protectionism under the Trump presidency will likely accelerate China's economic rebalancing to transition from export-oriented growth to domestic consumption-led and services-driven growth," Fan suggested. HSBC economists expect China GDP growth to sustain at 6.5% in 2017, down slightly from 6.7% projected for 2016 to reflect the challenging outlook for global trade.

Within Asian equities, HSBC Private Bank is overweight on China, India and Indonesia for their robust domestically-driven economic growth, structural reform tailwinds and pro-growth policy support. Compared to their Asian and Organisation for Economic Co-operation and Development (OECD) peers, the three countries have a lower-than-average dependency on exports and their strong domestic focus should also make them less vulnerable to potential increase in trade barriers and fluctuations in global risk appetite.

Supportive reform policies should benefit companies in the New Economy sectors, including Internet, IT, healthcare, new energy, travel, consumption and education services, as their stronger structural growth outlook should support the higher-than-market-average valuation. Moreover, China's continued market liberalisation effort, including the recently launched Shenzhen-Hong Kong Stock Connect, will likely bring positive liquidity impact on the Hong Kong market due to strong southbound flows from China driven by rising demand of the Chinese investors for overseas asset diversification amidst the RMB depreciation trend. HSBC FX strategists forecast the RMB to depreciate further, albeit gradually and orderly, to 7.20 against the US dollar by the end of 2017. Potential beneficiaries of southbound flows include quality undervalued Chinese and Hong Kong blue chips with prominent brand names and small-and-mid cap growth stocks listed in Hong Kong. HSBC Global Research forecasts upside potential of the Hang Seng Index to reach 25,000 and the Hang Seng China Enterprises Index to hit 11,000 by the end of 2017.

"We are positive on Asian investment grade and high-yield credits in hard currency with preference for Indian and Indonesian bonds. As we expect US bond yields to come down after peaking in the first quarter, the expected pullback in bond yields and the US dollar should support a recovery of Asian equities and Asian credits going into the second quarter of 2017," Fan said.

(3) US domestic focus

The expansionist fiscal policies, reduced regulatory control and protectionist trade policies under Trump's presidency should benefit domestically oriented companies in the US. Against a largely lackluster global economy, HSBC expects US GDP growth to accelerate to 2.3% in 2017 from 1.6% in 2016 while growth in the Eurozone is projected to decelerate to 1.2% in 2017 from 1.6% in 2016. While the valuations of US stocks are higher than that of European equities, there is room for further widening of the valuation differential between the two regions due to their divergent growth path.

In the US, domestically focused companies are likely to benefit the most under any increases in trade tariffs, especially the small-and-mid cap companies because they are typically more domestically oriented than the multi-nationals. A stronger US dollar potentially hurts corporate profits, but it should hurt domestically-focused companies less than exporters. If the Trump administration could allow US corporates to repatriate foreign profits with a preferential 10% corporate rate, it could provide the corporate sector with plenty of liquidity for mergers and acquisitions activity, share buybacks and increased dividend payments.

(4) Brave new world

Demographic shifts and technological innovation present opportunities even in a low return world with challengers and disruptors likely to emerge as winners in the brave new world. Technology has driven a major cost efficiency through the rapid growth of Artificial Intelligence and its integration with the Internet of Things, from consumer electronics to cars. Computing power and digital technology are evolving into an era where automation is entering a long-term secular growth phase.

Building on these four themes, HSBC Private Bank has identified the top 10 investment ideas for Asian investors in 2017:

1. US 10-year Treasury yield should come down again after peaking in Q1 2017
2. Gold to rise to USD 1,550 per ounce
3. RMB to fall towards USD/CNY 7.20 by the end of 2017
4. US domestically focused stocks
5. Sustainable dividends, M&A and buybacks
6. US and Asian High Yield
7. Support for oil and energy producers
8. Asian reformers: Indian and Indonesian stocks and bonds
9. China’s New Economy stocks
10. Alternatives for risk diversification

Investors should note that investments in the emerging markets may be extremely volatile and subject to sudden fluctuations of varying magnitude due to a wide range of direct and indirect influences. Such characteristics can lead to considerable losses being incurred by those exposed to such markets. Furthermore, investors should beware of the highly speculative nature of products involving hedge funds. These products are generally intended for experienced and financially sophisticated investors who are willing and able to bear the associated risks.

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