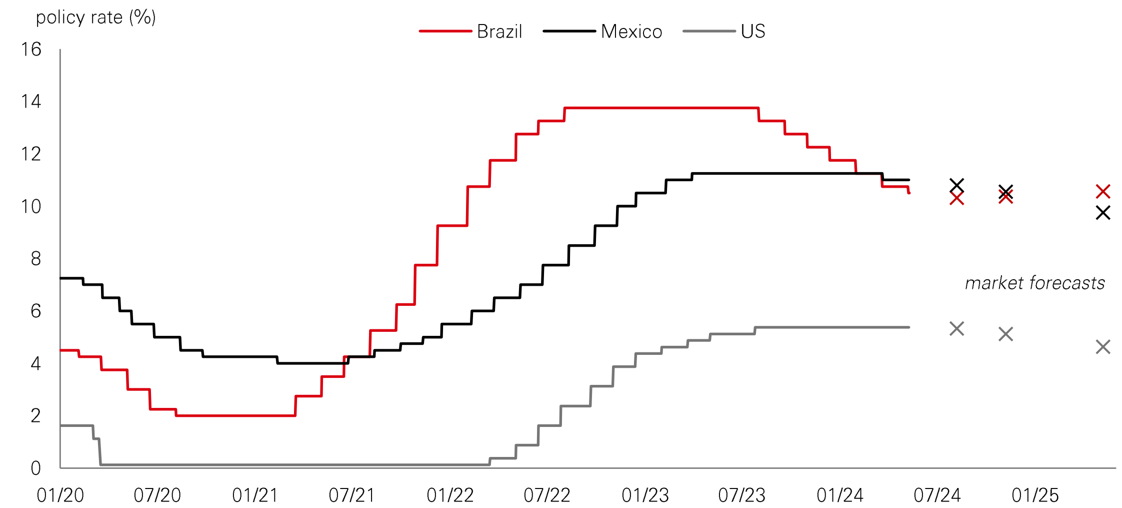
Investment Weekly

13 May 2024

Chart of the week – Fed to EM spillovers



EM central banks were ahead of the curve in the global fight against inflation, and many have already started to cut rates. But last week's central bank meetings in Mexico and Brazil highlighted a more cautious approach. Although Banco Central do Brasil cut rates for the seventh consecutive meeting, the 0.25% reduction was lower than the usual 0.50%. Meanwhile, Banco de Mexico kept rates on hold following a 0.25% cut in March, its first in the easing cycle.

Growing hesitancy to ease may reflect domestic factors. This includes strong labour markets which are keeping wage growth elevated. **But the recent shift in Fed rate expectations is also having an impact**. Front of mind have been concerns over currency weakness and the implications for imported inflation. The Brazilian real is down 4% year-to-date and concerns about capital outflows are likely to have been an issue.

Markets now expect little further easing in Brazil and Mexico over the next year, while the schedule for monetary easing in emerging Asia has been pushed back. This weighs on the outlook for EM growth and near-term EM asset class performance too. Brazil's earnings momentum has been slipping. But the good news is many EM economies are better insulated against tight external financial conditions than in the past. EM asset class valuations remain relatively cheap, providing a margin of safety for investors. Bond traders will benefit from high-for-a-bit-longer interest rates too. And **once the Fed does ease, the investor narrative and the EM policy stance can change quickly**.

Chinese Equities →

Exploring China's recent stock market rebound

US Dollar Outlook →

Understanding the bearish signals for the US dollar

Sell in May? →

Why investors may need to be cautious going forward

Market Spotlight

Stock markets and social unrest

For many countries around the world, the annual May Day holiday is a traditional celebration of workers' rights dating back to the 1900s. Over time – and particularly in periods of economic stress – it has been the focal point for strikes, demonstrations, rallies, and riots.

From an investment perspective, serious social unrest – driven by politics or socio-economics – can upset confidence, hurt growth, and damage stock prices. To understand this better, IMF research has explored the consequences for both economies and markets. One study found that countries experiencing unrest saw GDP remain on average 0.2 percentage points below the pre-shock baseline after 18 months.

Another study examined 156 events and found that while trading volumes often spike, the impact on stock markets was negligible in countries with open and democratic institutions. But for those with more authoritarian regimes, it was damaging, with returns falling on average by 2% within three days, and by about 4% over the following month. Overall, the research supports the view that social unrest can disrupt economies, but markets in countries with more open institutions are better at looking past them.

Source: HSBC Asset Management. Macrobond, Bloomberg. Data as at 11.00am UK time 12 May 2024.

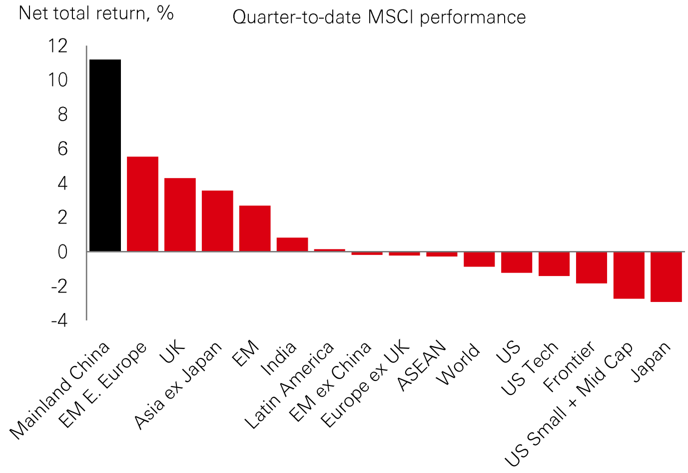
Lens on…

Mainland China's stock rebound

In recent weeks, there's been a reversal of fortune for Chinese stocks, outperforming indices across both developed and emerging markets. Crucially, **policy measures have shored up confidence**, with the Politburo signalling ongoing assistance on both the monetary and fiscal fronts.

Targeted measures have also been ramped up. Plans for "high quality" development of capital markets promise better protection for investors. Authorities are looking to reinforce Hong Kong's position as a financial hub, and support technology firms and the troubled real estate sector. And there have been efforts to encourage firms to boost share buybacks and dividend payouts.

Despite the turnaround, challenges remain, primarily property sector weakness and soft domestic demand. Deflationary pressures weigh on the profit outlook, but valuations remain very attractive, so there is still a good chance that piecemeal policy action continues to boost investor sentiment. In terms of earnings prospects, high-tech firms and high-quality state-owned enterprises look to be the bright spots.

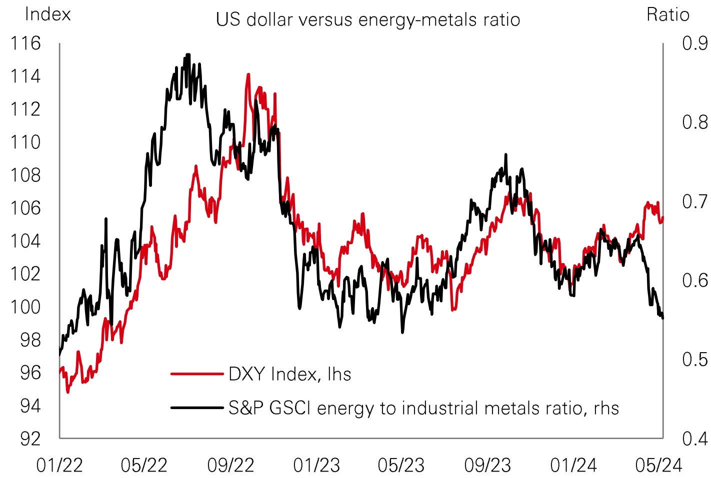


Commodities and the dollar

As one would expect, the repricing of US rate expectations has boosted the US dollar. The DXY index is up about 4% year-to-date.

Asian and European trade and survey data suggest a turnaround in the global manufacturing cycle, which benefits export powerhouses Europe and Japan. This may translate to a more hawkish-than-expected policy trajectory for the ECB and BoJ over the coming quarters. A Fed cut in September could shift the narrative away from high-for-longer US rates.

Commodity markets also point to a possible shift in the relative fortunes of the dollar. Since early April, the ratio of energy to industrial metals prices has fallen, which should result in a weaker dollar. This is because a lower ratio – which this time around reflects a combination of falling energy prices and rising metals prices – is disproportionately better news for Europe and Japan which are big energy importers and more sensitive to improvements in the global cycle (which higher metals prices potentially signal).

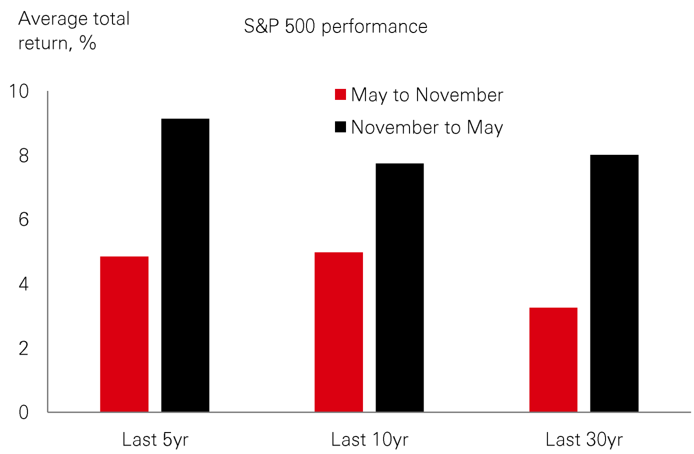


Sell in May and go away?

With the S&P 500 up around 25% since end-October and markets recently regaining momentum following April's drawdown, the stock market wisecrack "sell in May and go away" may hold special significance this year. Over the past 5, 10 and 30 years, index total returns are significantly lower in the six-month period from May to November, and there are plenty of challenges facing investors in the current environment.

Valuations in many parts of the DM risk asset universe look increasingly stretched. The DM growth outlook is hobbled by restrictive monetary policy settings. Tighter-for-longer policy at the Fed could have meaningful effects on global financial stability. And lower inflation is usually linked to weaker corporate pricing power.

For now, resilient economic activity and corporate earnings are bulwarks against big risk asset drawdowns. And Fed cuts – once they come – can help. But elevated macro and geopolitical uncertainty makes it crucial to protect portfolios against adverse scenarios.



Past performance does not predict future returns.

Source: HSBC Asset Management. Macrobond, Bloomberg. Data as at 11.00am UK time 12 May 2024.

Key Events and Data Releases

Last week

Date	Country	Indicator	Data as of	Actual	Prior
Mon. 6 May	CN	Caixin Services PMI	Apr	52.5	52.7
	IN	HSBC Services PMI	Apr (F)	60.8	61.7 (P)
	BR	S&P Global Services PMI	Apr (P)	53.7	54.8
Tue. 7 May	GE	Factory Orders (mom)	Mar	-0.4%	-0.8%
Wed. 8 May	AU	RBA Interest Rate Decision	May	4.35%	4.35%
	SW	Riksbank Interest Rate Decision	May	3.75%	4.00%
	BR	Banco Central do Brasil Interest Rate Decision	May	10.50%	10.75%
Thu. 9 May	CN	Trade Balance (USD bn)	Apr	72.4	58.6
	UK	BoE Interest Rate Decision	May	5.25%	5.25%
	MX	Banco de Mexico Interest Rate Decision	May	11.00%	11.00%
	MX	CPI (yoy)	Apr	4.7%	4.4%
Fri. 10 May	UK	GDP (qoq)	Q1	0.6%	-0.3%
	IN	Industrial Production (yoy)	Mar	5.2%	5.7%

P – Preliminary, F – Final, Q – Quarter **CN – China, IN – India, MX – Mexico, AU – Australia, SW – Sweden, BR – Brazil, GE – Germany**

The week ahead

Date	Country	Indicator	Data as of	Survey	Prior
Sat. 11 May	CN	CPI (yoy)	Apr	0.2%	0.1%
Mon. 13 May	EZ	Q1 Earnings			
	IN	CPI (yoy)	Apr	4.8%	4.9%
Tue. 14 May	US	NFIB Business Confidence Survey	Apr	88.1	88.5
Wed. 15 May	EZ	GDP (qoq)	Q1 (P)	0.3%	0.3%
	US	CPI (yoy)	Apr	3.4%	3.5%
	US	Retail Sales (mom)	Apr	0.4%	0.7%
Thu. 16 May	US	Housing Starts (mom)	Apr	9.0%	-14.7%
	US	Industrial Production (mom)	Apr	0.2%	0.4%
	JP	GDP (qoq)	Q1 (P)	-0.4%	0.1%
Fri. 17 May	CN	Retail Sales (yoy)	Apr	3.8%	3.1%
	CN	Industrial Production (yoy)	Apr	5.4%	4.5%

P – Preliminary, Q – Quarter **CN – China, EZ – Eurozone, IN – India, JP – Japan**

Source: HSBC Asset Management. Data as at 11.00am UK time 12 May 2024.

Market review

Positive sentiment prevailed in risk markets last week, aided by a pickup in US rate cut expectations ahead of key US CPI data. Core government bonds consolidated with 10-year Treasuries hovering around 4.5%. Sweden's central bank, the Riksbank, cut rate by 0.25%, highlighting diverging central bank stances. In the US, the S&P 500 posted decent gains, continuing its rebound from a weak performance in April, but it lagged Europe, with the Euro Stoxx 50 pushing higher on positive Q1 earnings news. Japan's Nikkei 225 edged lower amid hawkish BoJ comments hinting at faster-than-expected interest rate hikes. In EM, the Shanghai Composite continued to see positive momentum amid improving investor confidence, while India's Sensex index weakened on rising political jitters. In commodities, oil prices traded sideways while gold rallied on lower US real yields.