

Investment Monthly

Short-term USD and US equity weakness will likely persist

May 2025



Key takeaways

- ◆ Despite the 90-day tariff reprieve, investors and corporates continue to face elevated policy uncertainty and rotate into more defensive markets, sectors and currencies. Short-term USD and US equity market weakness will likely linger, but a US recession is not our base case (although the risk is higher). We prefer multi-asset diversification and quality assets and remain overweight on gold.
- ◆ The Eurozone looks more promising with fiscal support, more EU cooperation and lower-than-perceived earnings exposure to US tariffs. Our more positive view on Germany also supports an upgrade of Europe ex-UK equities to overweight. Japan's high export exposure to the US and a strong yen lead to a downgrade of Japanese equities to neutral. We focus on domestically oriented companies in Asia.
- ◆ With only 3% of earnings derived from US exports and more policy stimulus to support AI adoption, consumption and private companies, we expect Chinese equities to stay resilient and await tactical opportunities from mispricing caused by the tariffs to capture structural growth opportunities. We favour the internet, consumption, financial and industrial leaders, as well as quality SOEs paying high dividends.



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Asset class	6-month view	Comment
Global equities	▶	Global tariff escalation and growth uncertainty have led to broad-based market sell-offs. While volatility will likely persist in the short term, we continue to look for opportunities across sectors and markets with a focus on diversification and quality.
Government bonds	▶	The appeal of US Treasuries has recently declined but they offer some value for long-term investors. We prefer UK gilts and European government bonds over US and Japanese government bonds.
Investment grade (IG) corporate bonds	▶	Credit spreads are tight compared to current equity volatility levels, but overall yields remain attractive. We continue to see quality bonds as a good portfolio diversifier and avoid companies with direct exposure to tariffs.
High yield (HY) corporate bonds	▶	Spreads are tight in spite of high volatility, but overall yields are attractive. We remain selective in high yield bonds with a shorter duration preference for 3-5 years.
Gold	▲	Gold price should continue to break records amid persistent global uncertainty, fears of US stagflation and a softer USD. Central bank buying remains supportive.

▲ "Overweight" implies a positive tilt towards the asset class, within the context of a well-diversified, typically multi-asset portfolio.

▼ "Underweight" implies a negative tilt towards the asset class, within the context of a well-diversified, typically multi-asset portfolio.

▶ "Neutral" implies neither a particularly negative nor a positive tilt towards the asset class, within the context of a well-diversified, typically multi-asset portfolio.

Icons: ↑ View on this asset class has been upgraded; ↓ View on this asset class has been downgraded.

Talking points

Each month, we discuss 3 key issues facing investors

1. Will the reciprocal tariffs lead to a US recession?

- ◆ Although the 90-day tariff reprieve and the exemption of certain electronics have provided some temporary positive impact on sentiment, US companies still face rising tariff-related costs on almost all of their imported goods, which hurt their margins. We think Q1 consensus earnings forecasts will fall further. However, we remain of the view that economic weakness should be short-lived, and a US recession is not our base scenario, although the risk has increased, because long-term structural drivers such as AI and tech revolution and onshoring of jobs remain intact. For now, we will continue to see investors rotate into more defensive markets, sectors and currencies.
- ◆ The recent spike in Treasury yields reflects that the asset has somewhat lost its appeal as a safe haven, while some investors have a liquidity need for margin calls (due to losses elsewhere) when equity markets plunged. As uncertainty persists, we expect the yield curve to move down or with some mild steepening. We remain neutral on US Treasuries, focusing on medium-to-long maturities.
- ◆ Given policy uncertainty and downside revisions to economic growth, we expect further underperformance of US equities and USD assets in the short term, but still prefer the communications, industrials, financials and healthcare sectors. We focus on multi-asset diversification and quality assets and remain overweight on gold.

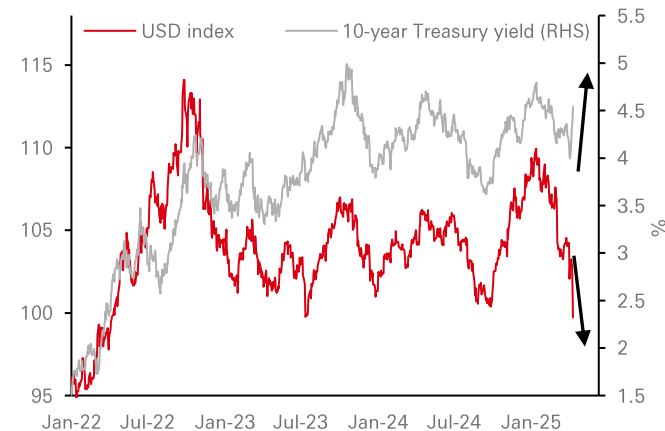
2. Where do we see better or worse opportunities?

- ◆ Europe is benefitting from investors looking to reduce excessive US equity allocations. We are more positive on Germany, in particular, as the post-election boost to German stocks was retraced in the recent sell-off, providing room for a rebound. The coalition agreement for the new government is also in place. As a result, we upgrade Europe ex-UK equities from neutral to overweight. The outlook for Mexico has also improved thanks to its exemption from the reciprocal tariffs and ongoing USMCA negotiations.
- ◆ We remain positive and diversified into Asia, where domestic growth opportunities and markets with less exposure to tariff risks, such as India and Singapore, remain supportive. Our focus on domestically oriented companies is even more important than ever. The UAE also presents a strong structural growth story.
- ◆ A flight to safe-haven assets has strengthened the Japanese yen, which may start to affect Japanese earnings negatively. Moreover, Japan's high reliance on exports to the US also warrants our downgrade of Japanese equities from overweight to neutral.

3. What supports our positive view on Chinese equities?

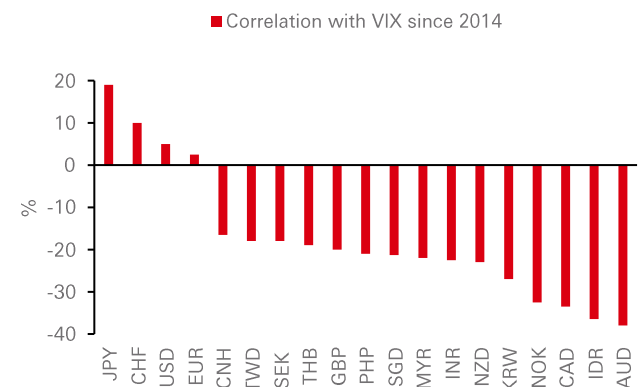
- ◆ Despite high two-way US-China tariffs, Chinese equities only derive 3% of earnings from US exports and are much more domestic than investors appreciate. Nevertheless, we expect the Chinese authorities to further ramp up fiscal stimulus to boost domestic consumption and provide policy support for the private sector to navigate downside growth risks. In addition to further policy rate and RRR (reserve requirement ratio) cuts this year, the PBoC has also allowed the RMB to weaken.
- ◆ Moreover, foreign investors are not holding too much Chinese assets in their portfolios, so there is little selling pressure. Chinese stocks continue to trade at a substantial discount.
- ◆ We remain overweight on Chinese equities and await tactical opportunities from mispricing caused by the tariffs to capture structural growth opportunities from AI innovation. We favour the internet, consumption, financial and industrial leaders, as well as quality SOEs paying high dividends.

Chart 1: Investors shun US assets, requiring higher yields and pushing USD down



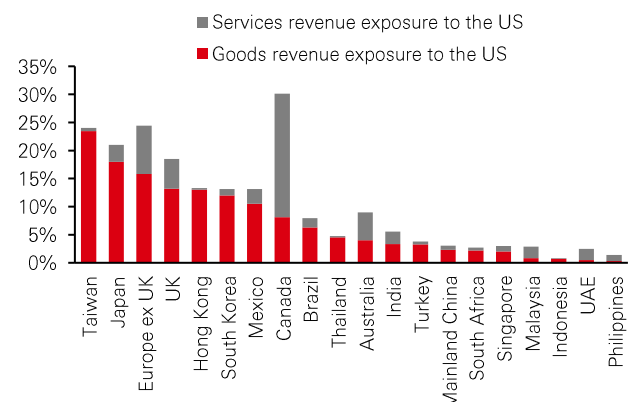
Source: Bloomberg, HSBC Global Private Banking and Wealth, as at 14 April 2025. Past performance is not a reliable indicator of future performance.

Chart 2: Japanese yen benefits from safe-haven flows in times of volatility, but not USD currently



Source: HSBC Global Research, HSBC Global Private Banking and Wealth, as at 14 April 2025. Past performance is not a reliable indicator of future performance.

Chart 3: Mainland China has only limited goods revenue exposure to the US



Source: HSBC Global Research, HSBC Global Private Banking and Wealth, as at 14 April 2025.

Asset Class Views

Our latest house view on various asset classes

Asset class	6-month view	Comment
Global equities		
Global	▶	Global tariff escalation and growth uncertainty have led to broad-based market sell-offs. While volatility is likely to persist in the short term, we continue to look for opportunities across sectors and markets with a focus on diversification and quality.
United States	▶	Rising concerns over tariffs, inflation and earnings will likely weigh on US equities in the short term but long-term structural themes, including technology revolution, job onshoring and US re-industrialisation continue to offer plenty of opportunities.
United Kingdom	▶	We see signs of economic resilience, but weak business sentiment, modest consumption and potential government spending cuts continue to weigh on the economic growth outlook. The tariff impact is relatively mild though.
Europe ex-UK	▲↑	Fiscal support, more EU cooperation and increased investor flows into the region lead to an upgrade to overweight. The economic outlook for Germany has improved thanks to its infrastructure-driven stimulus and improved political stability.
Japan	▶↓	Despite favourable wage momentum and corporate governance reforms, we downgrade Japanese equities to neutral due to the country's high export exposure to the US and a strong yen.
Emerging Markets (EM)	▶	The EM growth outlook has been increasingly clouded by tariff risks. We favour EM Asia the most for its diverse growth opportunities, overweighting China, India and Singapore.
EM EMEA	▼	While we see attractive opportunities in the UAE, some economies in the region remain vulnerable to external headwinds and geopolitical uncertainty. Turkey's political climate is causing some risk aversion among investors.
EM LatAm	▶↑	We are more positive on Mexico given its exemption from US reciprocal tariffs for now and its long-term trade partnership with the US. The USMCA re-negotiations are also underway. Brazil's rate hikes remain a headwind.
Asia ex Japan equities		
Asia ex-Japan	▲	Despite high reciprocal tax rates, AI innovation, domestic policy support and improved earnings visibility warrant a positive outlook for Asia. We prefer domestically oriented companies with resilient cash flows and strong brand positions.
Mainland China	▲	We expect more domestic stimulus to boost innovation and consumption and prefer the internet and software leaders, select consumer companies, and quality SOEs paying high dividends.
India	▲	Stabilised earnings expectations, less demanding valuations and improved international flows remain positive drivers for Indian equities. We prefer large-cap stocks in the financials, healthcare and industrials sectors.
Hong Kong	▶	Property market overhang and muted retail sales remain headwinds for Hong Kong equities. We prefer quality developers and undervalued high dividend stocks in the insurance and telecom sectors.
Singapore	▲	Our positive outlook for Singapore equities is backed by the country's defensive merit and attractive dividend.
South Korea	▶	South Korea is not benefitting from the accelerating AI adoption trend due to its higher exposure to semiconductors and hardware companies. Reciprocal and auto tariffs will weigh on earnings growth.
Taiwan	▶	Taiwan is hurt by its high-tech exports to the US, and the impact on semiconductor manufacturing is subject to further clarity on chip tariffs. We maintain a neutral position for now.
Government bonds		
Developed markets (DM)	▶	The appeal of US Treasuries has recently declined but they offer some value for long-term investors. We prefer UK gilts and European government bonds over US and Japanese government bonds.
United States	▶	US Treasury yields have been volatile with short-term inflation expectations and real yields rising sharply. A liquidity need for margin calls also increases selling pressure. We believe the sell-off of long-dated bonds should fade soon.
United Kingdom	▲	Attractive yields, favourable tax conditions and broader economic uncertainty are tailwinds for UK gilts.
Eurozone	▲	Recent Euro strength and lower energy prices should bolster the ECB's confidence in keeping inflation close to its 2% target level. We expect the ECB to cut rates further to prioritise growth and believe Bund yields should remain anchored.
Japan	▼	Given the prospect of a lower global rate environment and weaker domestic growth, we expect the Bank of Japan to adopt a less aggressive normalisation cycle. We remain underweight on Japanese government bonds, with a 3-5-year positioning.
EM (Local currency)	▼	Fiscal expansion in China and a globally challenged risk appetite are headwinds for emerging markets local currency debt.
EM (Hard currency)	▶	We remain selective and generally focus on quality. The USD weakness is expected to persist in the short term.
Corporate bonds		
Global investment grade (IG)	▶	Credit spreads are tight compared to current equity volatility levels, but overall yields remain attractive. We continue to see quality bonds as a good portfolio diversifier and avoid companies with direct exposure to tariffs.
USD investment grade (IG)	▶	US corporates still enjoy strong fundamentals, but their credit metrics will deteriorate. Credit spreads may remain choppy but all-in yields remain attractive. We prefer quality banks, insurance and technology issuers.
EUR investment grade (IG)	▲	Valuations are tight but carry makes total yields attractive. European corporates are not as directly exposed to a US growth slowdown as their US peers while European authorities have expressed willingness to support tariff-impacted sectors.
GBP investment grade (IG)	▲	GBP bonds are under-owned by international investors but offer similar yield levels to the USD market and a better risk-adjusted return trade-off.
Asian investment grade (IG)	▶	Global trade uncertainty and continued disinflation should support a more accommodative policy stance by central banks. We prefer Asian financials, Indian local currency debt, Chinese hard currency bonds in technology, financials and SOEs.
Global high-yield (HY)	▶	Spreads are tight in spite of high volatility, but overall yields are attractive. We remain selective in high yield bonds with a shorter duration preference for 3-5 years.
USD high-yield (HY)	▶	USD high yield provides a substantial overall yield, but equity volatility often feeds through into higher HY bond volatility.
EUR high-yield (HY)	▶	In line with our global high yield view, we remain selective on EUR HY bonds and stick to a 3-5-year positioning.
GBP high-yield (HY)	▶	We have a neutral view and short duration exposure on GBP high yield as spreads are below their long-term average.
Asian high-yield (HY)	▶	The property market remains an overhang in China. We prefer quality issuers in selective areas, such as Macau gaming.
Commodities		
Gold	▲	Gold price should continue to break records amid persistent global uncertainty, fears of US stagflation and a softer USD. Central bank buying remains supportive.
Oil	▶	Oil prices are being hit by slowed demand expectations and excess output. US tariff exemptions on oil products may limit downside risks for now.

Sector Views

Global and regional sector views based on a 6-month horizon

Sector	Global	US	Europe	Asia	Comment
Consumer Discretionary	▼↓	▼↓	▼↓	▲	We downgrade the sector based on increasing signs of US consumer weakness and disappointing earnings results from European companies. In contrast, Asian consumer sentiment continues to improve as valuations remain attractive relative to their history and other regions. Western autos remain battered by dislocated strategies and expensive products. Luxury goods sales declined in Q1 and are not expected to recover until H2. Both industries may also be targets of tariffs.
Financials	▲	▲	▲	▲	US Financials reported strong results for Q1. Net interest income is likely to remain elevated as inflation remains stubbornly high. Trading activity has been particularly strong and is likely to persist in the near term. In Asia, we remain positive on China's economy and improving sentiment in the region.
Industrials	▲	▲	▲	▲	Industrials have started the year modestly but have pulled back on tariff concerns even as company guidance was upbeat with many segments (machinery, construction, aerospace, trucks, trains and freight) expecting solid YoY growth from robust order books. Digital infrastructure and essential physical infrastructure related businesses seem set to benefit from a pick-up in capital spending.
Information Technology	▶↓	▶↓	▶↓	▶	We downgrade the IT sector with the negative news flow regarding the impact of tariffs on hardware and semiconductors, and uncertainties regarding future data capacity requirements. We remain constructive on software and services. In the medium to long term, the sector presents significant growth opportunities as AI models proliferate, and AI capabilities become embedded in most products and services.
Communications Services	▲	▲	▶	▲	In the US, the media and entertainment industry is forecast to have above-average sales and earnings growth for 2025, even after its stellar performance over the past two years. In Europe, the outlook for the telecom services sector is plagued by strong competition, low investment returns and a lack of pan-European scale. In Asia, the sector is more balanced with attractive valuations and easing regulation.
Materials	▼	▼	▼	▼	The demand outlook is expected to remain weak amid a challenging pricing environment. Persistently high energy and feedstock costs will likely squeeze margins and profits. Mining and chemical stock valuations are undemanding, but growth is likely to remain elusive. Tariffs remain a significant risk and are hurting sentiment. Refining, processing and chemical stocks remain unappealing in the short term.
Real Estate	▶	▶	▶	▶	The sector appears to have stabilised except in China where some uncertainty remains. Retail space and older offices are particularly challenged as alternative consumer purchasing channels evolve and refurbishment costs are high. New office developments and housing are experiencing better supply-demand dynamics. The re-routing of supply chains is driving demand for new facilities in developed and some emerging markets.
Consumer Staples	▶	▶	▶	▶	Strong competition and consumers trading down have created a weak pricing environment for companies in many markets. Limited potential for sales growth and margin expansion, combined with high valuations relative to other sectors (in line with history), makes the sector unattractive. Consumers are trading down and seeking lower cost alternatives when purchasing goods.
Energy	▶	▶	▶	▶	Unfavourable supply-demand dynamics are expected to lead to lower oil prices in the next 12 months, although the relatively higher cost of shale gas production may limit output and, therefore, oversupply-induced price declines. Gas demand will likely remain buoyant, albeit volatile, due to seasonal demand impacting prices. Low valuations, strong cash flows and high dividends somewhat offset the sector's speculative nature.
Healthcare	▲	▲	▲	▶	At the end of last year, the market overreacted to negative news flow and uncertainty regarding US healthcare policy. The sector has now started to recover. In Asia, the sector is seeing improving market dynamics and strong earnings growth expectations for this year. In the US, we expect earnings growth to be among the highest of the sectors with new and recently launched products driving earnings. European healthcare stocks have a more mixed outlook.
Utilities	▶	▶	▶	▶	Energy demand trends remain very supportive as many economies undergo electrification of transportation, expansion of digital infrastructure, and rising affluence driving demand for air conditioning, freezers, etc. Utilities are already operating close to capacity, so substantial capital investments are required to upgrade generation capacity and transmission infrastructure. Valuations are undemanding.

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