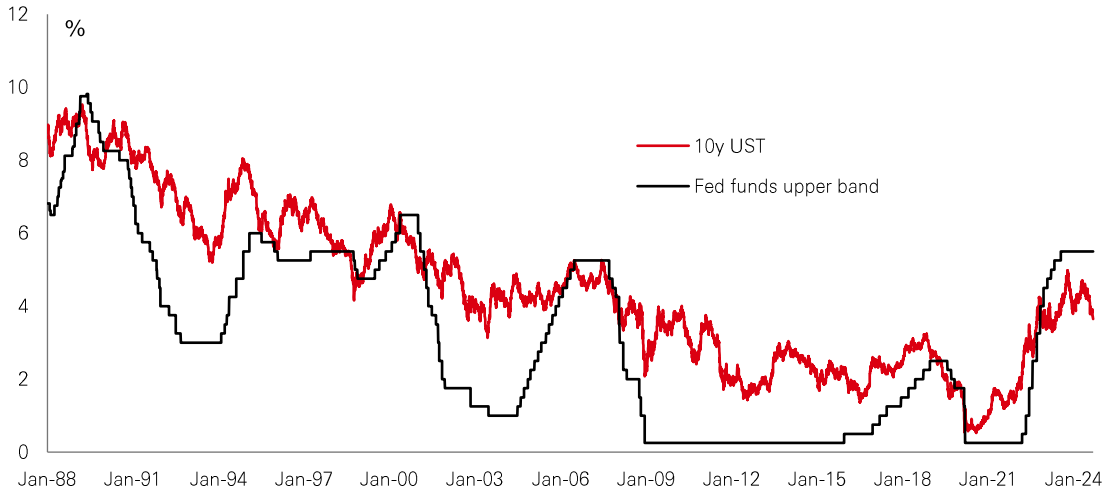


Investment Weekly

16 September 2024

Chart of the week – Treasuries and the Fed policy cycle



Markets are pricing in an approximate 40% chance of a 0.50% Fed cut on 18 September. This is despite an unexpectedly strong August core inflation print of 0.3% month-on-month. Shelter costs were the main culprit behind the upside surprise. Excluding shelter, core inflation is running at only 1.1% on a six-month annualised basis, suggesting that price pressures are under control and allowing the Fed to put more weight on the labour market leg of its mandate.

Here, the August data were mixed; unemployment ticked down, having jumped in July, but payrolls were softer than expected. Overall, a broad swathe of data suggests the labour market is continuing to cool, but relatively gradually, which helps explain why the overwhelming consensus among economists is for a 0.25% cut. However, the funds rate is at restrictive levels and, based on current market pricing, is only likely to return to a neutral stance around mid-2025.

Given policy acts with a lag, the risk that labour market cooling turns into labour market freezing will remain elevated for some time to come. **This alone is likely to lead to further bouts of volatility in markets.** And if those risks then crystallise, the Fed will be forced to cut aggressively. So, while Treasury yields have fallen markedly of late, **they can still play an important role in hedging portfolios against downside growth scenarios.**

Small Caps →

Why valuations could appeal to multi-asset investors

Currencies →

Exploring recent moves in the Mexican peso

Market Spotlight

UK stocks breaking out

Since the 16 July peak of the S&P 500, there has been a significant rotation in performance within the global equity space. Previous winners such as US tech have been lagging, while unloved regions and sectors – value, defensives, EM, and small caps – have taken the lead. For developed markets, this reversal of fortune for UK equities has been particularly striking.

Some analysts think as part of the wider broadening-out story, UK stocks can continue to be a relative winner. The market remains unloved and cheap, with the MSCI UK trading at a significant valuation discount versus its own 10-year average 12m forward PE. The UK market is also defensive, with significant weights in consumer staples and healthcare that can better withstand a deterioration in global economic conditions. And although a stronger pound might be a headwind to export-oriented firms – especially in the large-cap space – this can be offset by cheaper input costs from abroad. **With EPS growth expected to jump into double-digits for 2025, the overall profits picture also looks good.**

Asian Equities →

Diversification benefits of emerging Asian stocks

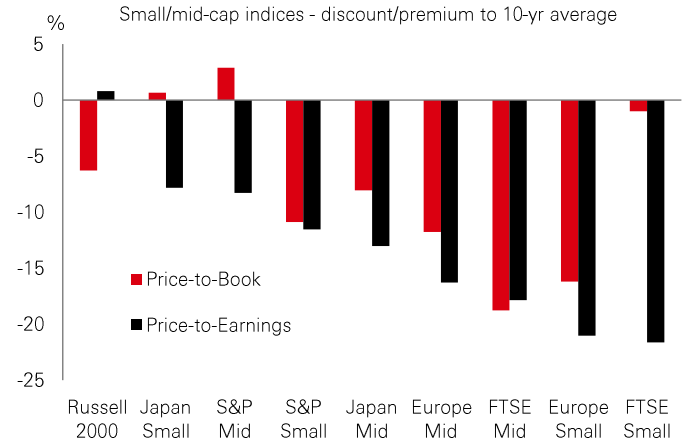
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Small cap value

When volatility hit global stocks in August, and mega-cap tech firms sold off sharply, small-caps proved to be a surprise winner. And while the rally in smaller firms has since cooled, it gave us an insight into how quickly small cap value can react to steady growth and the prospect of rate cuts.

Currently, there are deep valuation discounts between smaller caps and large caps (and their own history). Most developed market indices show small- and mid-cap stocks trading 10-25% below their 10-year average measures like price/earnings (PE) and price/book. By contrast, the S&P 500 currently trades at a 30% premium to its 10-year average 12m forward PE. Selection is key.

Europe and Japan look particularly unloved, with the former expecting rate cuts and the latter an eventual return to inflation, boosting nominal profit growth.

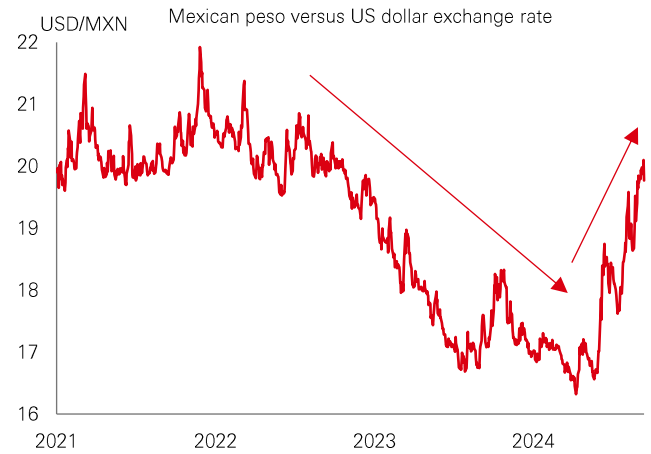


What happened to the super peso?

The Mexican peso has been one of the strongest performing EM currencies in recent years. This has come on the back of proactive central bank policy, a solid fiscal position, and strong economic ties with the outperforming US economy. Other more structural factors such as continuing growth in remittances and supply chain 'nearshoring' have also played a role.

Against a backdrop of elevated interest rate differentials, the peso has also seen interest from international investors engaging in 'carry trades' (where traders borrow in low rate currencies and buy higher rate assets). But this summer's rapid unwinding of popular carry trades has put significant pressure on the currency, just as factors like domestic politics and the imminent US election have pushed uncertainty higher.

After the recent retreat, it now seems likely the so-called super peso may settle in a new range. *Happy Independence Day to our Mexican readers!*

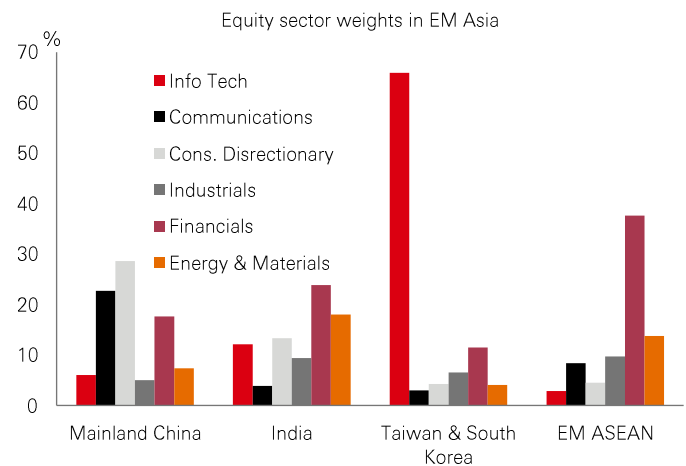


Emerging and diverging in Asia

While global technology stocks have suffered badly in recent bouts of market volatility, analysts are upbeat on the sector in emerging Asia. Profit growth expectations have recently picked up on solid international demand for semiconductors and positive profits figures from mainland Chinese tech heavyweights.

But a catch for the region's tech players is a potential slowdown in global growth. While firms in markets like Taiwan and South Korea have enjoyed years of strong demand, recent sector weakness has revealed some vulnerability to external headwinds and downside growth risks in the US.

The good news for investors is that while tech is expected to remain a profit engine for the region, emerging Asian markets also offer broad sector diversification. Against a backdrop of uncertain global growth, domestically-focused markets like mainland China, India, and ASEAN – where tech has a relatively small overall sector weighting – are less reliant on external demand.



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Key Events and Data Releases

Last week

Date	Country	Indicator	Data as of	Actual	Prior
Mon. 09 September	MX	Headline Inflation (yoy)	Aug	5.0%	5.6%
	CN	CPI (yoy)	Aug	0.6%	0.5%
Tue. 10 September	US	NFIB Index of Small Business Optimism	Aug	91.2	93.7
	BR	CPI (yoy)	Aug	4.2%	4.5%
	UK	Unemployment Rate, ILO	Jul	4.1%	4.2%
	CN	Trade Balance (USD)	Aug	91.0bn	84.7bn
Wed. 11 September	UK	GDP Estimate (mom)	Jul	0.0%	0.0%
	US	CPI (yoy)	Aug	2.5%	2.9%
Thu. 12 September	EZ	ECB Deposit Rate	Sep	3.50%	3.75%
	IN	CPI (yoy)	Aug	3.7%	3.6%
	IN	Industrial Production (yoy)	Jul	4.8%	4.2%
Sat. 14 September	CN	Industrial Production (yoy)	Aug	4.7%	5.1%
	CN	Retail Sales (yoy)	Aug	2.50%	2.7%

MX - Mexico, CN - China, US - United States, BR - Brazil, UK - United Kingdom, EZ - Eurozone, IN - India

The week ahead

Date	Country	Indicator	Data as of	Survey	Prior
Tue. 17 September	US	Retail Sales (mom)	Aug	-0.2%	1.0%
Wed. 18 September	US	Housing Starts	Aug	1.31mn	1.24mn
	US	Fed Funds Rate (upper band)	Sep	5.25%	5.50%
	BR	Banco de Brazil SELIC Target Rate	Sep	10.75%	10.50%
	ID	Bank Indonesia Rate	Sep	6.25%	6.25%
	UK	CPI (yoy)	Aug	2.2%	2.2%
Thu. 19 September	US	Existing-Home Sales	Aug	3.88mn	3.95mn
	JP	CPI excluding fresh food and energy (yoy)	Aug	3.0%	2.8%
	UK	BoE MPC Base Rate	Sep	5.00%	5.00%
	NW	Norges Bank Sight Deposit Rate	Sep	-	4.50%
Fri. 20 September	TY	CBRT 1 Week Repo Lending Rate	Sep	50.00%	50.00%
	JP	BoJ Policy Rate	Sep	-	0.25%

US - United States, BR - Brazil, ID - Indonesia, UK - United Kingdom, JP - Japan, NW - Norway, TY - Turkey

Source: HSBC Asset Management. Data as at 11.00am UK time 15 September 2024. This information shouldn't be considered as a recommendation to buy or sell specific sector/stocks mentioned. Any views expressed were held at the time of preparation and are subject to change without notice.



This week

Risk markets rebounded ahead of the US Fed's FOMC meeting this week, with rising expectations of a possible 0.50% cut. Core government bonds rallied, with US Treasuries faring better than German Bunds. The European Central Bank delivered a 0.25% cut in the deposit rate, with ECB president Lagarde reiterating that future cuts would remain "data dependent". The US dollar DXY index fell to a 2024 low. US equities saw a broad-based rally, led by tech stocks, with the Euro Stoxx 50 and Japan's Nikkei 225 also on course to finish the week higher. In emerging markets, the tech-dominant South Korea Kospi index posted modest gains and India's Sensex index resumed its upward trend. Ongoing disinflation worries pushed China's Shanghai Composite index close to 2024 lows. In commodities, oil prices stabilised late last week, after falling sharply on supply concerns. Gold reached fresh historic highs.

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