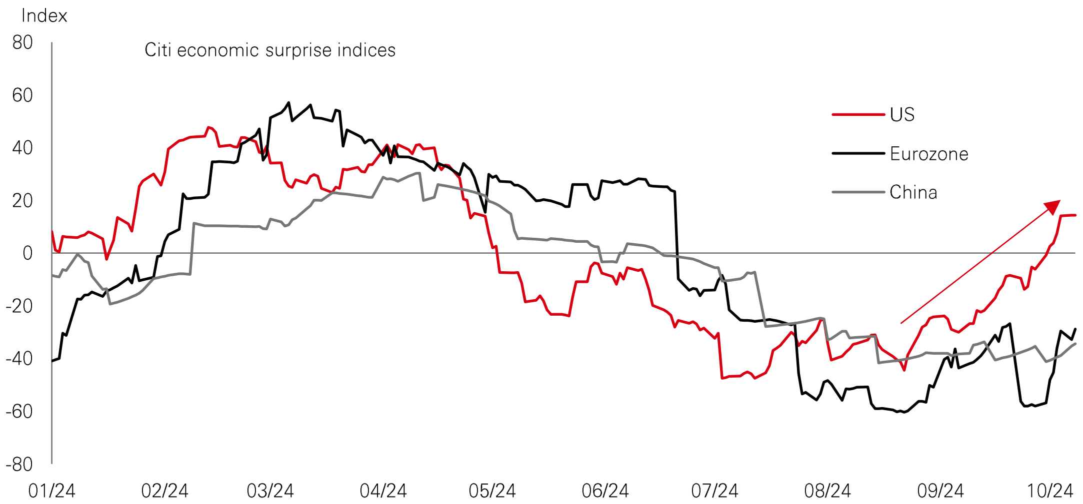
HSBC

Investment Weekly

14 October 2024

Chart of the week – US economic data holding up



September's strong US employment report, with non-farm payrolls up 254k (versus 150k expected) and the unemployment rate unexpectedly edging lower to 4.1%, was good news for those hoping for a soft landing for the world's largest economy. The recent run of better-than-expected economic data (see chart) also coincides with an underlying trend of disinflation – despite September's stronger-than-expected CPI print. Leading indicators point to a further moderation in price pressures, including the shelter component which is contributing to high services inflation.

August's market wobble – partly triggered by a weak July payrolls number – now seems like a distant memory. US stock markets are notching up fresh all-time highs and the US 10-year Treasury yield is back above 4%.

A soft landing is good news for global risk assets. But markets are likely to remain volatile as investors grapple with uncertainty over the economic outlook. Rates remain restrictive and the US election has the potential to usher in policy shifts. And despite better US macro news, **some labour market data suggests cooling ahead**. The October payrolls report could be weak again. **Earnings could also disappoint** – doubly bad news given stretched valuations.

Market Spotlight

Chinese markets take a pause for breath

It was a bumpy week for Chinese stocks as investors digested the recent surge in prices and the National Development and Reform Commission's (NDRC) announcement that it would accelerate bond issuance to support the economy.

A pause for breath last week isn't surprising given the extremity of recent market moves – the MSCI China had gained around 26% in the 10 trading days leading up to the Golden Week holiday. Investor expectations around the speed and scale of incoming fiscal support may have become too optimistic.

Despite the lack of details on potential fiscal stimulus offered by the NDRC, it is likely that Chinese authorities will still unveil a meaningful fiscal package in the coming weeks. The Ministry of Finance held a press briefing on 12 October, while another opportunity for action comes at the National People's Congress standing committee meeting later this month.

Earnings Season →

What lower expectations mean for profit growth in Q3

Frontier Markets →

Why policy easing is a plus for frontier equity valuations

Fixed Income →

Exploring strong investor demand for IG credit

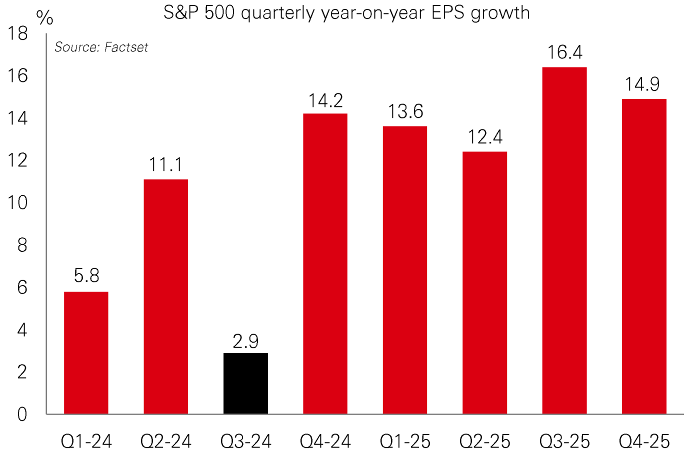
Source: HSBC Asset Management. Macrobond, Bloomberg. Data as at 11.00am UK time 11 October 2024.

Analysts spooked

Q3 results season kicks off this week with 8% of the S&P 500 (by market cap) reporting, and 60% expected by Halloween. Annual consensus profits growth is 10% for this year, and 15% for 2025. But on a quarterly year-on-year basis, analysts have slashed forecasts for Q3 to just 2.9% – down from 10.2% a year ago. So, what has spooked them?

Economically-sensitive sectors like materials, consumer discretionary (autos/retail), and industrials have seen some of the biggest cuts. Soft economic data over the summer are likely to blame, and lower oil prices hit energy names. But from Q4, that changes. Five quarters of growth averaging 14% (double the long-run average) suggests a rosier outlook.

Technology is set to be the fastest growing sector in Q3, while analysts expect energy to be the weakest. Financial stocks, which are among the first to report, are anticipated to slow. Overall, a low growth bar could offer scope for above-average beats for Q3. But with the market already trading on a relatively high PE of 21x, **a soft landing and giddy profit growth from Q4 onwards appear to be priced-in**, just as momentum in tech earnings is starting to slip.

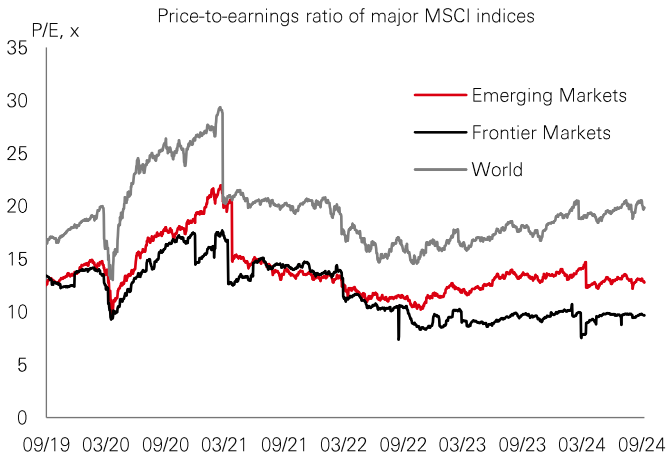


Value at the frontier

Many Frontier and smaller emerging market countries were relatively quick to respond to the post-Covid inflation surge, hiking rates faster than the US. With real rates now significantly positive, they have room to cut – and stimulate growth – without pressuring their currencies. We've seen recent cuts in countries like Iceland, Kenya, Pakistan, and Serbia. It's a trend that should act as a tailwind for Frontier valuations.

It comes as valuation discounts between Frontier and both DM and EM regions remain well above their 5-year averages. Frontier markets are currently trading at a price-earnings ratio of 9.7x – a 51% discount to DMs (at 19.9x) and a 24% discount to EMs (at 12.8x).

Yet, **Frontier offers superior earnings growth and higher dividend yields**, plus the diversification benefit of low correlation with other asset classes. This is largely being driven by structural trends like the relocation of manufacturing hubs, re-routing of supply chains, social and economic reforms (especially across Gulf Cooperation Council countries), and digitisation.

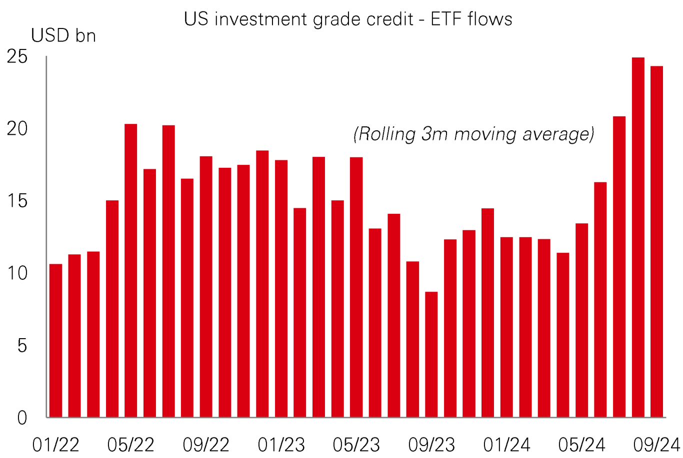


'All in' appeal of US IG

Growing expectations of a soft economic landing bode well for US investment grade (IG) debt. With Fed policy easing expected to continue at a cautious pace, and recent jobs data mitigating recession worries, 10yr Treasury yields have risen, which has improved the attractive all-in yields that IG debt offers.

IG debt has a high correlation with government bonds. So, if risk appetite falters, IG should be a defensive play as the widening in credit spreads is likely to be, at least partially, offset by the fall in government bond yields.

The fundamental backdrop for IG has also been positive. Corporate profits have been resilient, and the net issuance outlook is expected to remain favourable. Above all, investor demand remains upbeat. There have been strong flows for much of this year into US IG exchange traded funds and the unwinding of popular carry trades during the summer did little to dent investor enthusiasm. The experience suggests that the marginal spread-widening required to attract buyers is smaller than it was in the past.



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Key Events and Data Releases

Last week

Date	Country	Indicator	Data as of	Actual	Prior
Tue. 08 October	US	NFIB Index of Small Business Optimism	Sep	91.5	91.2
Wed. 09 October	BR	CPI (yoy)	Sep	4.4%	4.2%
	MX	Headline Inflation (yoy)	Sep	4.6%	5.0%
	IN	RBI Repo Rate	Oct	6.50%	6.50%
	NZ	RBNZ Official Cash Rate	Oct	4.75%	5.25%
	US	FOMC Minutes	Sep		
Thu. 10 October	US	CPI (yoy)	Sep	2.4%	2.5%
	FR	2025 Budget			
Fri. 11 October	KO	Bank of Korea Base Rate	Oct	3.25%	3.50%
	IN	Industrial Production (yoy)	Aug	-	4.8%
	US	Univ. of Michigan Sentiment Index (Prelim)	Oct	-	70.1

US - United States, BR - Brazil, MX - Mexico, IN - India, NZ - New Zealand, FR - France, KO - South Korea

The week ahead

Date	Country	Indicator	Data as of	Survey	Prior
Sun. 13 October	CN	CPI (yoy)	Sep	0.7%	0.6%
Mon. 14 October	US	Earnings	Q3		
	CN	Trade Balance (USD)	Sep	89.8bn	91.0bn
Tue. 15 October	UK	Unemployment Rate, ILO	Aug	4.1%	4.1%
Wed. 16 October	ID	Bank Indonesia Rate	Oct	6.00%	6.00%
	UK	CPI (yoy)	Sep	1.9%	2.2%
	PH	Central Bank Policy Rate	Oct	6.00%	6.25%
Thu. 17 October	US	Retail Sales (mom)	Sep	0.2%	0.1%
	EZ	ECB Deposit Rate	Oct	3.25%	3.50%
	TY	CBRT 1 Week Repo Lending Rate	Oct	50.00%	50.00%
	CH	Banco Central de Chile Policy Rate	Oct	5.25%	5.5%
	US	Industrial Production (mom)	Sep	-0.1%	0.8%
Fri. 18 October	JP	CPI (yoy)	Sep	2.5%	3.0%
	CN	Retail Sales (yoy)	Sep	2.5%	2.1%
	CN	GDP (yoy)	Q3	4.6%	4.7%

CN - China, US - United States, UK - United Kingdom, ID - Indonesia, PH - Philippines, EZ - Eurozone, TY - Turkey, CH - Chile, JP - Japan

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Market review

Risk markets were firm ahead of Q3 earnings season in the US. Core government bonds fell on an upward surprise in September's employment report. US CPI data also came in stronger than expected. Bunds continued to fare better than US Treasuries as investors priced in a 0.25%, rate cut at October's ECB Council meeting. In stocks, the US S&P 500 touched a new all-time high, the Euro Stoxx 50 index traded sideways, and Japan's Nikkei 225 inched higher. Emerging market equities weakened as investors awaited further details on potential fiscal stimulus for the Chinese economy. The Hang Seng fell sharply, with China's Shanghai Composite also weakening after the Golden Week holiday. The Korean Kospi rebounded, with India's Sensex little changed. In commodities, geopolitical tensions are supporting energy prices. Copper weakened, while gold was on course to finish the week flat.

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