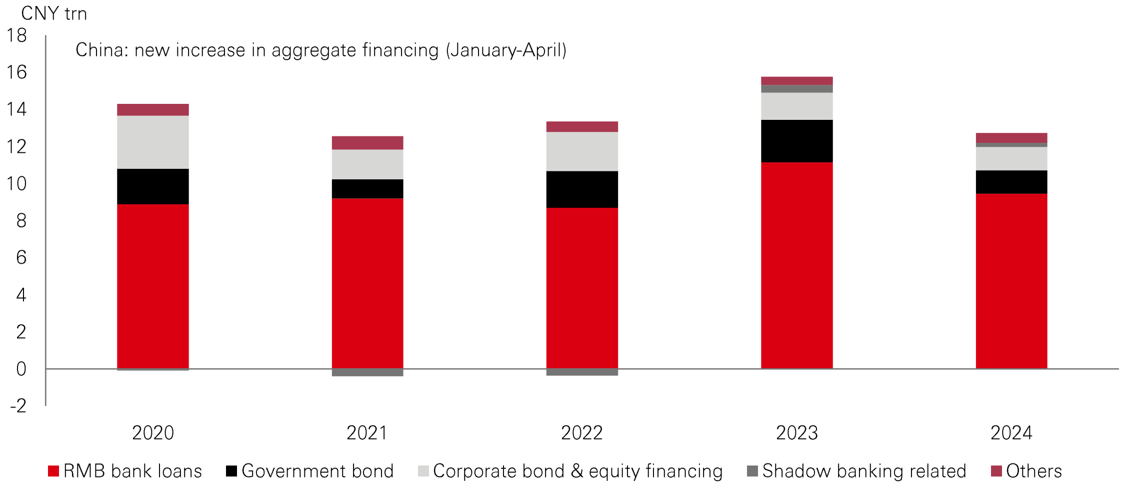
Investment Weekly

20 May 2024

Chart of the week – China's ultra-long bond boost



Policy support from Chinese authorities to boost economic momentum has been building for months. This week saw the latest, and potentially most potent of those moves, with confirmation of a new CNY1 trillion (USD140 billion) ultra-long government bond issuance.

Starting 17 May, and running to mid-November, the sale includes tenors of 20, 30 and 50-year bonds. Assuming auctions are a success, early details suggest the central government will allocate CNY500bn to itself and another CNY500bn to local governments to ease financial constraints and deleveraging pressures at the local level. After a slow start for bond issuance this year (see chart), the move could be a stabilising force for credit growth for the rest of 2024.

While not quite the policy 'bazooka' unleashed in the 2008 financial crisis, it's nonetheless a significant effort to ensure the government's 5% GDP growth target is met. While the precise usage is unknown, investments are expected to target longer-term projects in areas like technology, regional development, and agriculture and energy security.

Overall, it marks a notably different approach to European policymakers, who in the past have resolutely resisted leveraging low rates to issue ultra-long bonds as a source of fiscal expansion. **And the measures may help maintain China's year-to-date stock market outperformance.** That said, ongoing deflationary pressures and unbalanced growth are likely to mean that even more support will be needed in the coming months.

European Equities →

How rate cuts could affect stock market momentum

Corporate Bonds →

Why a brighter outlook could boost European IG

Real Assets →

Exploring the opportunity in listed infrastructure

Market Spotlight

Full circle in markets

April was a bad month for US equities and bonds with hot growth and inflation data leading markets to price in a greater probability of a 'no landing' scenario and more hawkish Fed policy. However, mid-way through May and we've come full circle with the 10-year US Treasury yield heading lower while the S&P 500 has hit a new high.

Jerome Powell triggered the turnaround at his May press conference when he pushed back against the idea that the next move in Fed funds could be up. This was followed by a softer-than-expected April payrolls print and the lowest core CPI print of the year.

While July remains a stretch for the first Fed rate cut, the cooler inflation and labour market data keep September on the table. Indeed, with a wider selection of US activity and survey data now surprising on the downside – the April retail sales print was a case in point – a softening of activity may be the next story to emerge.

Source: HSBC Asset Management. Macrobond, Bloomberg. Data as at 11.00am UK time 17 May 2024.

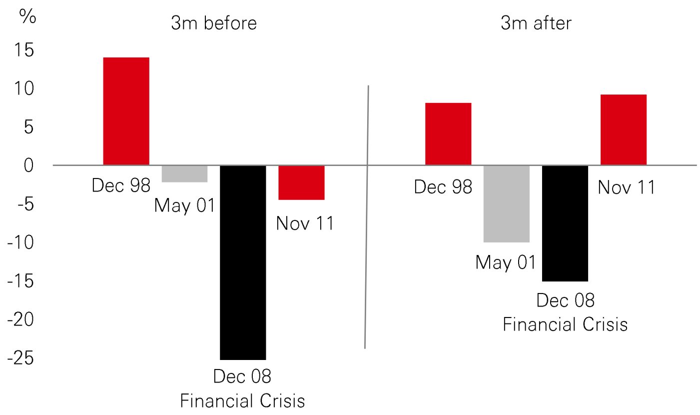
What eurozone rate cuts might mean for stocks

For investors in European stocks, the old adage that 'it's better to travel than arrive' could ring true this year. An improving economic backdrop, broadening market momentum and expectations of an ECB rate cut as soon as June, have driven eurozone equities higher. But could a rate cut affect the rally?

In the months before and after previous first cuts by the ECB – notably the 2001 tech bubble and 2008 financial crisis – eurozone stocks performed poorly. But in both cases, valuations and leverage were excessive, triggering recessions. By contrast, equities were strong either side of the ECB's 1998 rate cut to defend against a global slowdown in what was otherwise, a non-recessionary, mid-cycle backdrop. And it's there that we see similarities to today.

Despite evidence of earnings growth and strong recent momentum, European stocks continue to look unloved. The DJ Stoxx 600 has lagged US and DM equities for the past five years and still trades near record lows versus the US (on a 12m forward price-earnings ratio). With rate cuts on the horizon, some tactical selling could be expected, but the case for selective stock picking in Europe remains.

DJStoxx 600 performance around first ECB cut



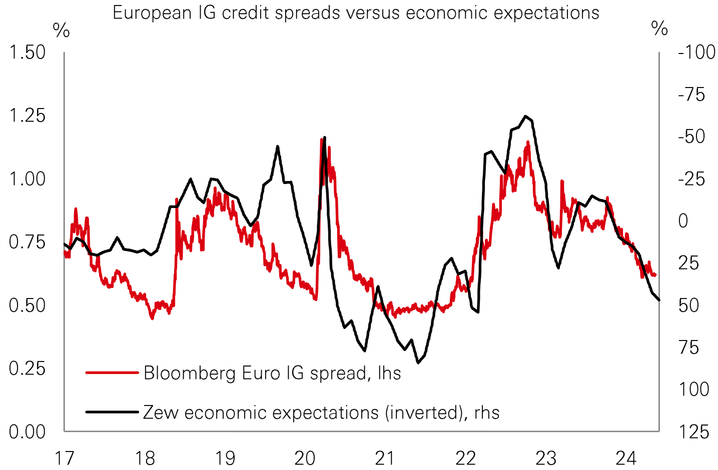
Putting cash to work in European IG credit

Signs that the global growth outlook is broadening out could bode well for risk assets outside the US. In particular, European investment grade credit, which has been trading at a discount to US credit for some time, could begin to close the valuation gap.

The impetus has been a steady recovery in economic surveys, including in Germany where the continent's manufacturing slump has been keenly felt. Positive March PMI data and a 0.3% quarter-on-quarter rise in GDP in Q1 2024, suggest the eurozone's slump is over. And despite still-high policy rates, sentiment has lifted on growing expectations of a June rate cut from the ECB, given the relatively benign inflation outlook for the eurozone.

For credit, it means a reduced risk of spread widening despite spreads being close to historic lows.

European IG credit spreads versus economic expectations



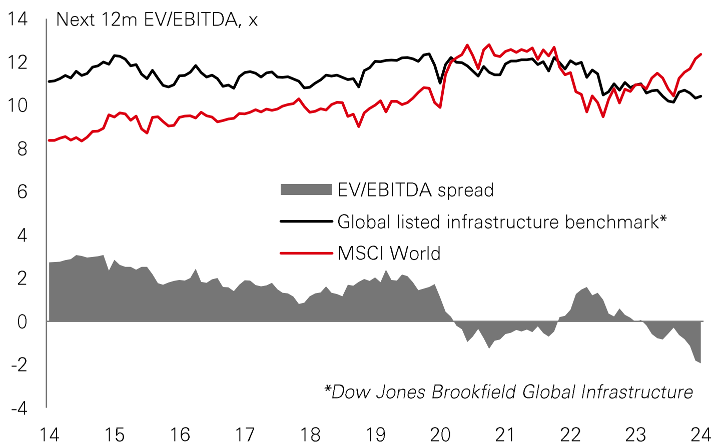
Infrastructure opportunity

Global listed infrastructure is popular in portfolios for its defensive traits and dependable cashflows. But over the past two years, elevated real rates have dragged on valuation multiples and left it underperforming global equities. Yet, with rate cuts on the horizon, that could now present an opportunity.

Listed infrastructure covers stocks exposed to everything from power networks and airports to communication towers and utilities. While the sector's performance correlates negatively to rate movements, its underlying fundamentals have been solid, with profit growth and income both resilient over the past decade. That's being helped by secular tailwinds, with rapid investment spending in areas like urbanisation, digitisation, and the energy transition.

With the asset class trading at an unusually wide discount to global stocks (based on the valuation of forward enterprise value to EBITDA), the sector could be good value. It also has a notably higher dividend yield, which could become more attractive when rates begin to fall.

Valuation of listed infrastructure versus global equities



Past performance does not predict future returns.

Source: HSBC Asset Management. Macrobond, Bloomberg. Data as at 11.00am UK time 17 May 2024.

Key Events and Data Releases

Last week

Date	Country	Indicator	Data as of	Actual	Prior
Sat. 11 May	CN	CPI (y-o-y)	Apr	0.3%	0.1%
Mon. 13 May	IN	CPI (y-o-y)	Apr	4.8%	4.9%
Tue. 14 May	US	NFIB Business Confidence Survey	Apr	89.7	88.5
	US	Fed Chair Powell speaks	May		
Wed. 15 May	EZ	Employment	Q1	0.3%	0.3%
	US	CPI (y-o-y)	Apr	3.4%	3.5%
	US	Retail Sales (m-o-m)	Apr	0.0%	0.6%
Thu. 16 May	US	Housing Starts (m-o-m)	Apr	5.7%	-16.8%
	JP	GDP (q-o-q)	Q1 (P)	-0.5%	0.0%
Fri. 17 May	CN	Retail Sales (y-o-y)	Apr	2.3%	3.1%
	CN	Industrial Production (y-o-y)	Apr	6.7%	4.5%

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

The week ahead

Date	Country	Indicator	Data as of	Survey	Prior
Mon. 20 May	EZ	Q1 Earnings			
	CN	Loan Prime Rate (1yr)	May	3.45%	3.45%
Wed. 22 May	NZ	RBNZ Interest Rate Decision	May	5.50%	5.50%
	UK	CPI (y-o-y)	Apr	2.1%	3.2%
	US	Existing Home Sales (m-o-m)	Apr	-0.7%	-4.3%
	US	May FOMC meeting minutes			
Thu. 23 May	IN	S&P Global Composite PMI	May (P)	-	61.5
	EZ	Eurozone HCOB Composite PMI	May (P)	51.6	51.7
	US	Composite PMI	May (P)	-	51.3
	TY	Turkish Central Bank Interest Rate Decision	May	50.00%	50.00%
	KO	BoK Interest Rate Decision	May	3.50%	3.50%
Fri. 24 May	JP	Nationwide CPI ex fresh food & energy (y-o-y)	Apr	2.5%	2.9%
	US	Durable Goods Orders (m-o-m)	Apr (P)	-0.7%	0.9%

P – Preliminary, Q – Quarter **EZ – Eurozone, CN – China, NZ – New Zealand, IN – India, TY – Turkey, KO – Korea, JP – Japan**

Source: HSBC Asset Management. Data as at 11.00am UK time 17 May 2024.

Market review

Reassuring US CPI data supported risk appetite last week. Core government bonds rallied with investors now pricing in two 0.25% Fed rate cuts by year-end. The US Dollar DXY index weakened on downward US data surprises. In equities, the S&P 500 and Nasdaq reached new all-time highs, outperforming the eurozone Stoxx 50 index as the Q1 earnings season comes to an end. Despite disappointing Q1 GDP data, Japan's Nikkei 225 index posted strong gains led by momentum in technology shares. In EM, the Shanghai Composite weakened on disappointing Chinese data. India's Sensex index rallied, continuing its recent favourable trend. In commodities, energy prices were stable as the International Energy Agency trimmed its forecast for 2024 oil demand ahead of June's OPEC+ meeting. Gold rose towards historic highs on improving US rate sentiment, with copper also performing strongly.

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