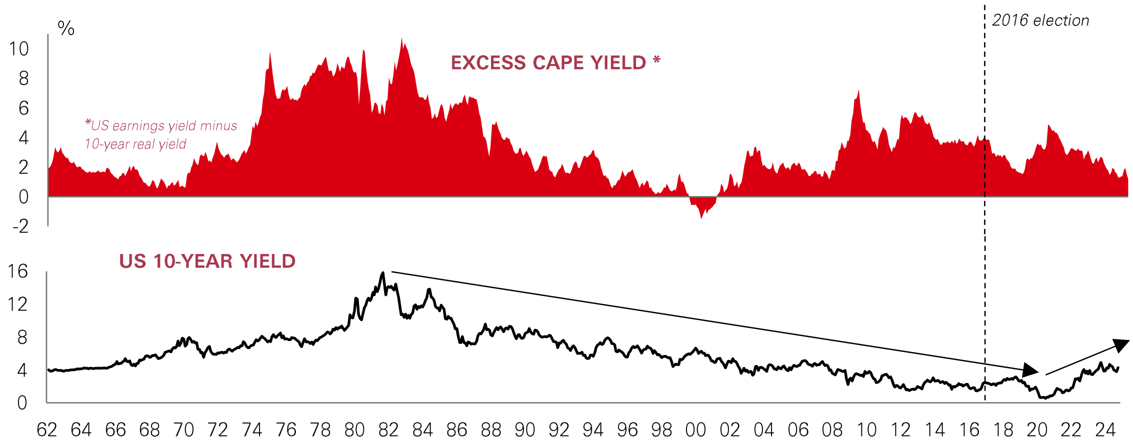
Investment Weekly

25 November 2024

Chart of the week – A difficult starting point for US stock valuations



Over the previous week, risk markets have paused for breath. US stocks have unwound some of their big post-election gains, high-yield credit spreads have picked up from multi-year lows, and commodity prices have lost ground.

We think recent market action reflects a new reality facing investors. There is a "tug of war" between enthusiasm around significant aspects of the US policy outlook – mainly deregulation and tax cuts – versus concerns about the potentially stagflationary effects of loose fiscal policy and an acceleration of the trend in US isolationism.

US 10-year yields are hovering just below April's year-to-date highs despite the Fed now in easing mode and inflation in a holding pattern, with room for more disinflation in 2025. This is because there is now much greater uncertainty around the inflation outlook, reflected in the recent pick-up in the US term premium.

Structurally higher inflation and interest rates pose many challenges for investment markets. It weighs on the growth and earnings outlook. And it makes stock valuations less attractive versus bonds. The most expensive parts of the stock market such as US mega-cap tech – which look priced for perfection – could be vulnerable.

Market Spotlight

High flying assets

Four years after being badly hit by Covid travel restrictions, air traffic has finally caught up with 2019 levels – but the global aviation industry's cyclical and structural growth drivers are changing.

A new research explores the sector's investment outlook – with a focus on airports, which are a key part of the infrastructure asset class. Overall demand looks robust, but new trends in the traveller 'mix' and geographic growth are emerging. While business travel continues to decline, demand from cohorts travelling for leisure and 'visiting friends and relatives' is growing quickly. And in terms of regional demand, industry forecasts suggest that fast-growing developing nations will contribute 85% of the industry's growth over the next 20 years – with Asia Pacific expected to be a powerhouse.

For airport investors, post-pandemic challenges are giving way to new opportunities, with wealth and demographic trends expected to drive above-GDP growth rates for the industry. Together with offering a wider range of travel destinations, there are opportunities for airports to enhance returns with a wider range of premium services.

Q3 Earnings →

The latest on profits 'beats' and 'misses' in US stocks

Asian Equities →

Why stock buybacks are on the rise in Asian markets

Currencies →

How FX moves post-US election compare to 2016

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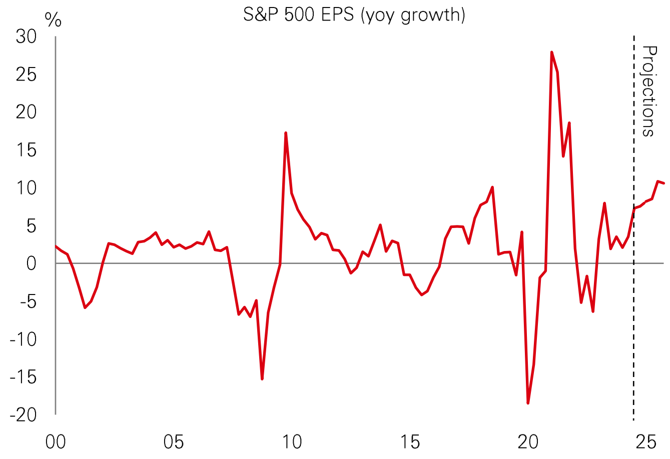
Source: HSBC Asset Management. Macrobond, Bloomberg. Data as at 7.30am UK time 22 November 2024.

Q3 earnings scorecard

With Q3 earnings season drawing to a close in the US, last week saw results from the market's most closely-watched technology giant, NVIDIA. Like the rest of the S&P 500's 'Magnificent 7' tech stocks, NVIDIA's quarterly profits were ahead of analyst forecasts for the quarter. Indeed, with more than 90% of companies in the index having reported, around 75% of them have beaten profit expectations.

However, the scale of index-wide profits beats – averaging about 4.3% above estimates, according to Factset – is roughly half that of their 5-year average. Firms may be finding it harder to beat forecasts. And given the index trades on a price-to-earnings ratio of 22.3x (versus its 15-year average of 16.4x), prices could be vulnerable if future earnings disappoint. The communication services, IT and healthcare sectors have seen the largest (aggregate) beats, while energy and materials have seen the largest (aggregate) misses.

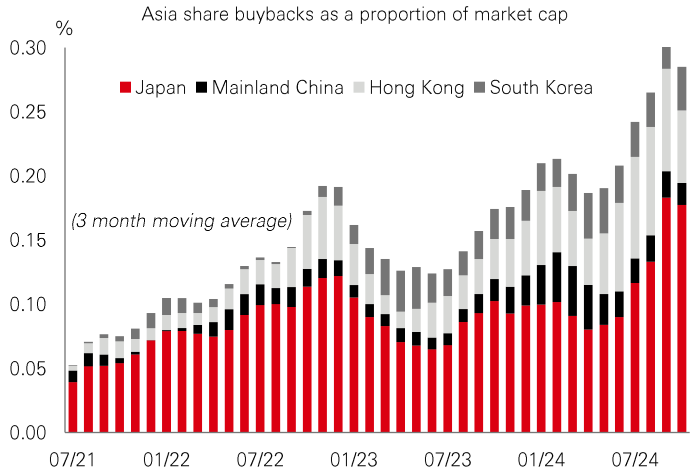
From here, profit growth expectations remain high into 2025. **But against a backdrop of policy uncertainty and a cooling economy, any weakness could lead to heightened volatility.**



Asia's buyback boost

US stock buybacks have boomed in recent years as companies looked to boost earnings-per-share, buoy their valuations, and allocate cash to reward shareholders. Against a backdrop of falling rates – dampening returns on cash holdings – this popularity should persist. But this isn't just a US phenomenon – Asia stock markets have seen a buyback boost too.

A key difference in Asia is that buybacks have been driven by regional efforts to improve corporate governance. Governments have called on firms to be more investor-friendly and improve their valuations. Japan is a prime example, and is now seeing a third consecutive year of record buybacks in 2024. A similar move in South Korea – the 'Value-Up' programme – saw a 25% rise in buybacks in H1-24 from H1-23. Mainland Chinese authorities have also demanded action on profitability and shareholder returns. Share repurchases there are on course to break domestic records this year, with September's stimulus measures including a RMB300bn relending facility earmarked specifically for share buybacks.

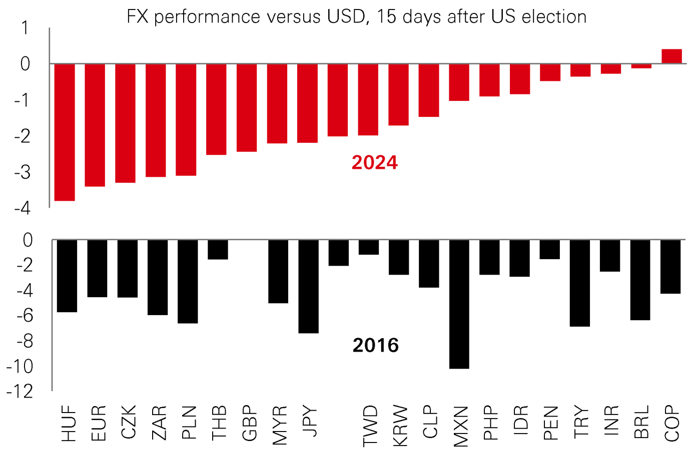


FX moves versus 2016

Recent action with the US dollar looks to be following the 2016 playbook. The DXY index or "dixie" is up around 3-4% since the US election, about the same as in the 15 days following the 2016 poll.

But moves in individual FX pairs show some interesting differences versus the 2016 experience. The most striking contrast is the Mexican peso. This was one of 2016's biggest casualties, and although it's down this time around, it is one of the better performers. Other Latin American currencies have held up well too – the Brazilian real and Columbian peso have hardly budged. This resilience could reflect a hawkish tilt to central bank policymaking in the region in recent months.

Moves in Europe have also been quite different. The euro and some Eastern European currencies have been badly hit by the election result. Trade tariffs would come at a very difficult time for the region's manufacturers. But the good news is FX weakness supports external competitiveness for export-dependent firms. In 2025, US-specific factors – policy and inflation trends – are likely to be a big influence on the dollar. But **global economic and political developments will also be key**.



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Source: HSBC Asset Management. Macrobond, Bloomberg, Datastream. Data as at 7.30am UK time 22 November 2024.

Key Events and Data Releases

Last week

Date	Country	Indicator	Data as of	Actual	Prior
Mon. 18 November	JP	BoJ Governor Ueda speech	Nov	-	-
Tue. 19 November	US	Housing Starts	Oct	1.31mn	1.35mn
Wed. 20 November	ID	Bank Indonesia Rate	Nov	6.00%	6.00%
	UK	CPI (yoy)	Oct	2.3%	1.7%
Thu. 21 November	US	Existing-Home Sales	Oct	3.96mn	3.83mn
	JP	CPI (yoy)	Oct	2.3%	2.5%
	TY	CBRT 1 Week Repo Lending Rate	Nov	50.00%	50.00%
Fri. 22 November	IN	S&P Global Composite PMI (Flash)	Nov	59.5	59.1
	EZ	Frankfurt European Banking Congress		-	-
	EZ	S&P Global Composite PMI (Flash)	Nov	-	50.0
	UK	S&P Global Composite PMI (Flash)	Nov	-	51.8
	US	S&P Global Composite PMI (Flash)	Nov	-	54.1

JP - Japan, US - United States, ID - Indonesia, UK - United Kingdom, TY - Turkey, IN - India, EZ - Eurozone

The week ahead

Date	Country	Indicator	Data as of	Survey	Prior
Mon. 25 November	US	Q3 earnings	Q3	-	-
	GE	IFO Business Confidence Index	Nov	86.0	86.5
Tue. 26 November	US	Consumer Confidence Index, Conference Board	Nov	112.5	108.7
Wed. 27 November	US	PCE Price Index (yoy)	Oct	2.3%	2.1%
	NZ	RBNZ Official Cash Rate	Nov	4.25%	4.75%
	US	GDP, 2nd Estimate (qoq annualised)	Q3	2.8%	2.8%
	US	FOMC minutes	Nov	-	-
Thu. 28 November	JP	Tokyo CPI excluding food and energy (yoy)	Nov	-	1.1%
	KO	Bank of Korea Base Rate	Nov	3.25%	3.25%
Fri. 29 November	EZ	HICP, Flash (yoy)	Nov	2.4%	2.0%
Sat. 30 November	CN	NBS Composite PMI	Nov	-	50.8

US - United States, GE - Germany, NZ - New Zealand, JP - Japan, KO - South Korea, EZ - Eurozone, CN - China

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Market review

Risk markets were resilient despite heightened geopolitical tensions, with both oil and gold prices rallying. The US DXY dollar index paused for breath after its recent strong run. Core government bonds consolidated ahead of key US inflation data and mixed comments from Fed officials. US equities saw a broad-based rally as investors digested Q3 earnings. The Euro Stoxx index fell modestly, while Japan's Nikkei 225 weakened as the yen rebounded versus the US dollar. BoJ governor Ueda reiterated his commitment to gradual rate hikes. Emerging market stock markets were mixed. The Shanghai Composite and Hang Seng indices finished the week lower, but the tech-driven South Korea Kospi index performed well. India's Sensex index fell further. In Latin America, Brazil's Bovespa and Mexico's IPC equity indices were on the defensive. Meanwhile, copper was little changed.

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