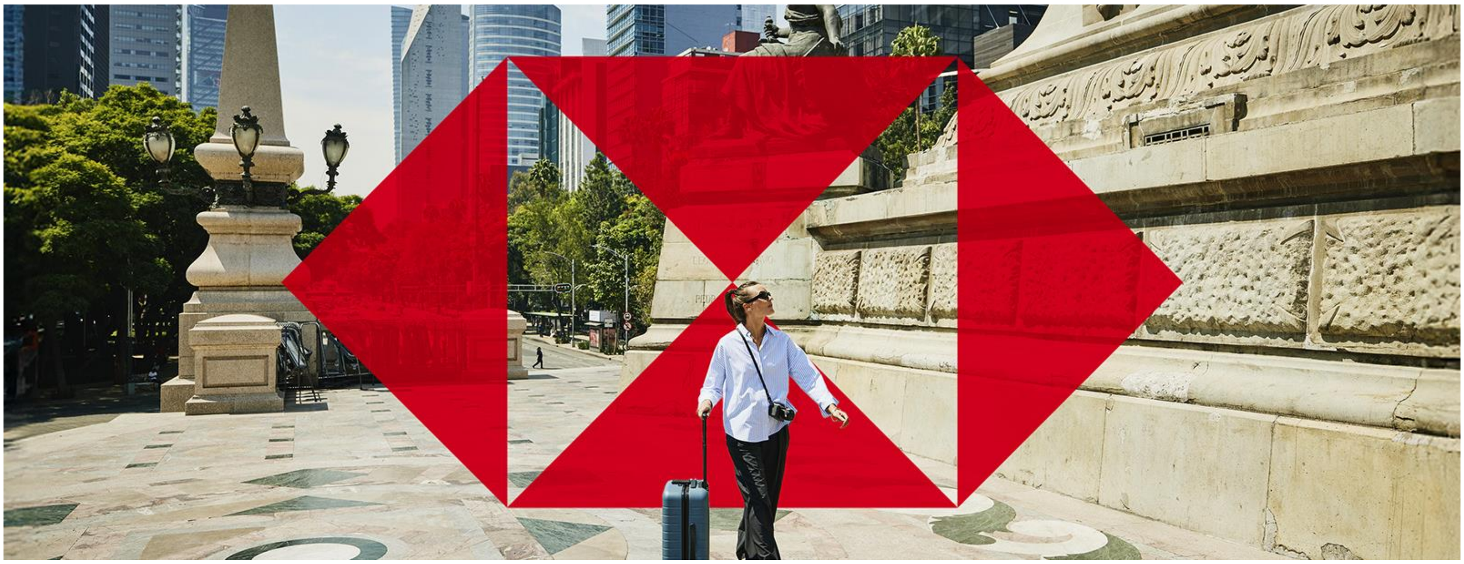
Investment Monthly

Positive drivers boost market optimism amid progress on trade deals

August 2025



Key takeaways

- The higher fiscal deficit concerns caused by the One Big Beautiful Bill, which included significant tax and spending cuts, and broad policy shifts, will likely be offset by expectations of Fed rate cuts and benign inflation. Meanwhile, solid Q2 earnings growth reinforces our US overweight positions in IT, Communications, Industrials and Financials as they benefit from the bill and structural trends. More regulatory clarity (e.g., GENIUS Act) is also a positive.
- Following the US-Japan trade deal, which lowered Japanese tariffs to 15%, the US and the EU also announced a 15% tariff rate on most EU goods sold to the US, plus additional investments in US energy products and military equipment. These deals have de-escalated global trade tensions substantially. We maintain a risk-on stance and mitigate uncertainty through multi-assets, including quality bonds (e.g., UK gilts) and gold.
- While China's 5.2% GDP growth for Q2 has raised hopes of reaching the government's full-year target of around 5%, economic data remain mixed. The Chinese authority has introduced supply-related measures to address the deflationary pressures caused by overcapacity in the areas of solar, steel, auto, lithium batteries, etc., which boosted market sentiment. In Asia, we remain overweight in China, India and Singapore, and neutral in Japan following the loss of its ruling coalition's majority in both parliamentary houses.

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Asset class	6-month view	Comment
Global equities	▲	The recent tariff announcements and optimism about AI adoption have boosted global sentiment. We maintain our risk-on strategy by diversifying across multi-assets and sectors that combine quality fundamentals and structural tailwinds.
Government bonds	▶	We hedge against US trade policy and growth uncertainties by focusing on 7-10-year duration for DM sovereign bonds (except Japan) and maintain our preference for US gilts over Treasuries and Bunds.
Investment grade (IG) corporate bonds	▶	We continue to use quality bonds to manage growth, tariff and geopolitical headwinds. Credit spreads are relatively tight as investors may prefer investment grade credit over Treasuries.
High yield (HY) corporate bonds	▶	Spreads are tight as risk appetite is high while equity volatility is low. We hold a shorter duration bias of 3 to 5 years.
Gold	▲	Gold remains a key diversifier amid market uncertainty although the uptrend may ease. Central bank buying continues to provide support.

▲ "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.

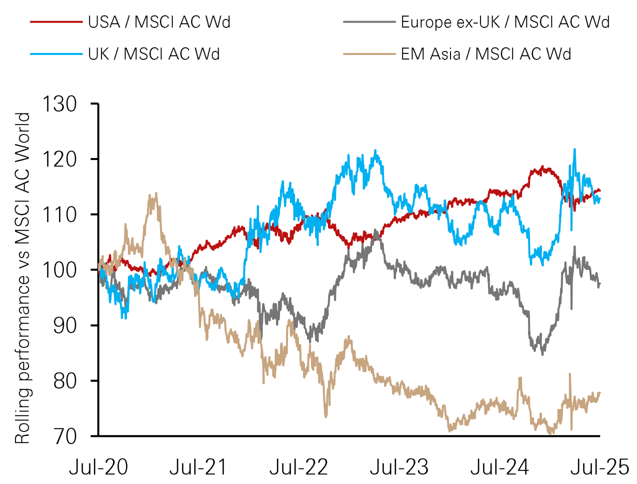
Talking points

Each month, we discuss 3 key issues facing investors

1. What is driving the US equity rally?

- The US Congress passed the One Big Beautiful Bill on 3 July, which introduced significant tax changes and spending cuts, new border security funding, and broad policy shifts across Energy, Healthcare, and more. In addition to ensuring the 21% corporate tax rate, it also included individual tax cuts (eliminating federal taxes on tips and overtime pay), a rising cap on state and local tax deductions, and a deduction for automotive loan interest.
- Market concerns over a higher fiscal deficit weigh on bond prices and elevate borrowing costs but should be offset by rising expectations of Fed rate cuts and benign inflation, as well as multiple positive drivers.
- Given the low bar, Q2 earnings results surprised to the upside, led by IT, Communications, Industrials and Financials. We stay overweight on these sectors, which should benefit from the Bill and structural trends. We think the AI-led equity outperformance will continue, although valuations have risen but are still below prior peaks. The Guiding and Establishing National Innovation Act (GENIUS) is expected to motivate more companies to use digital assets, benefitting the IT and related areas, such as communications, media and infrastructure. Our US overweight position since May has worked well and will stay on course.

Chart 1: Tech leadership is helping the US equity market's continued rebound since May 2025

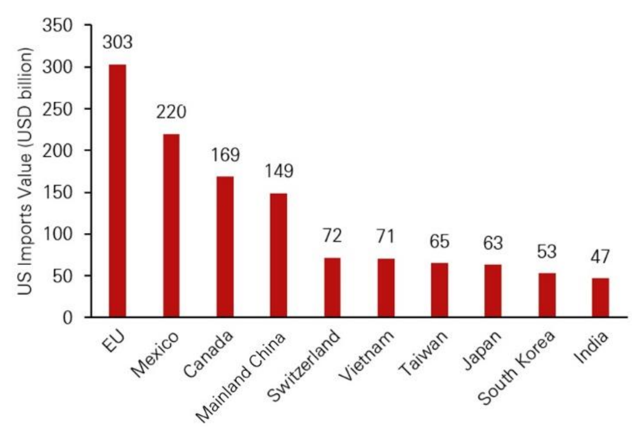


Source: Bloomberg, HSBC Private Bank and Premier Wealth as at 22 July 2025. Past performance is not a reliable indicator of future performance.

2. What are the implications of recent trade deals?

- The US and Japan have concluded a deal to reduce US reciprocal tariffs on all Japanese products from 25% to 15%. Additionally, Japan also agreed to invest USD550bn in the US and open its markets to US automobiles, rice and agricultural products.
- Following this, the US and the EU also announced a 15% tariff rate on most EU goods sold to the US, including automobiles. Moreover, the EU will purchase US energy products and chips (USD750bn) and make additional US investments (USD600bn) as part of the deal. While this is welcome by the market, some sectoral tariffs are still not clear and muted demand for autos, agriculture and pharmaceuticals continues to weigh on the region's Q2 earnings growth. Nevertheless, we see pockets of opportunity in Financials, Industrials and Utilities. The recent trade deals have de-escalated global trade tensions substantially.
- While tariff impacts may linger in the US, we do not expect inflation to surge due to accelerating tech-led productivity gains and anticipated rate cuts. As equity markets remain resilient, we maintain a risk-on stance and manage uncertainty through diversification across multi-assets, including quality bonds (e.g., UK gilts) and gold.

Chart 2: The trade deal between the two largest economies is expected to bring stability

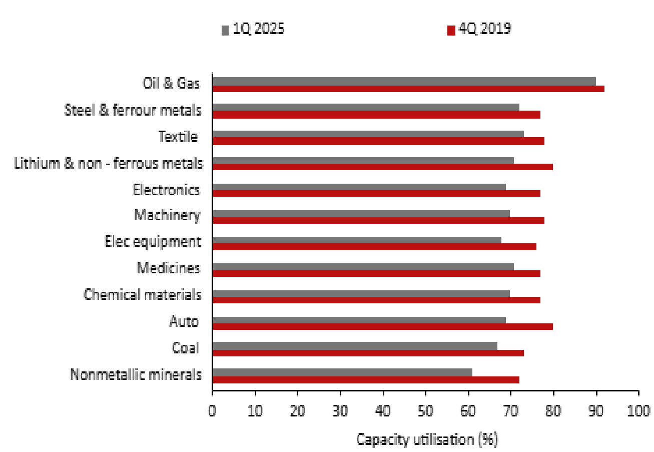


Source: Bloomberg, US Census Bureau, HSBC Private Bank and Premier Wealth as at 28 July 2025.

3. Will China's Q2 GDP growth boost a more bullish outlook for Asia?

- China's GDP growth of 5.2% y-o-y for Q2 slightly exceeded market expectations, raising hopes of reaching the government's full-year target of around 5%. While industrial production showed strength due to robust exports and retail sales were somewhat solid, fixed asset investment and the property sector continued to be sluggish.
- To address the deflationary pressures caused by overcapacity that weighs on margins and earnings, the Chinese authority has called for supply-related measures for the solar industry, followed by steel, auto, lithium batteries, etc. Although the actual reduction in capacity will take time, the commitment is a clear positive for market sentiment.
- Elsewhere in Asia, while the US-Japan trade deal supports global sentiment, the loss of the majority in both parliamentary houses will likely push Japan's ruling coalition to become more expansionary, leading to continued uncertainty. We remain positive yet selective in Asia, downgrading Industrials to neutral after strong YTD returns lifted valuations above the five-year average, while upgrading Healthcare to overweight due to attractive valuations and catalysts such as renewed funding in China and AI-driven innovation. We prefer China, India and Singapore and remain neutral in Japan.

Chart 3: Capacity utilisation rates are low, highlighting a clear overcapacity problem



Source: HSBC Global Investment Research, HSBC Private Bank and Premier Wealth as at 22 July 2025.

Asset Class Views

Our latest house view on various asset classes

Asset class	6-month view	Comment
Global equities		
Global	▲	The recent tariff announcements and optimism about AI adoption have boosted global sentiment. We maintain our risk-on strategy by diversifying across multi-assets and sectors that combine quality fundamentals and structural tailwinds.
United States	▲	Despite policy uncertainty and elevated valuations, US equities are well supported by solid earnings growth, potential tax cuts and deregulation, AI-led innovation and other structural trends such as nearshoring and re-industrialisation.
United Kingdom	▶	Sticky inflation and mixed political signals remain headwinds. Elevated government bonds yields are also obstacles. The US-UK trade deal provides some comfort but is not enough to shift our neutral view for now.
Europe ex-UK	▶	Despite the EU-US trade deal, some sectoral tariffs are still not fully clear. A stronger euro and relatively weaker earnings momentum compared to the US support a neutral stance. We favour the industrials, financials and utilities sectors.
Japan	▶	While the recent trade deal and the continued reflation trend support Japanese equities, rising expectations of fiscal stimulus to boost domestic consumption raise fiscal concerns. We prefer technology leaders and consumption stocks.
Emerging Markets (EM)	▶	Lower inflation is positive for some emerging markets while an improved outlook for trade deals reinforces our preference for EM Asia, in particular.
EM EMEA	▼	The region faces weak growth and monetary and geopolitical uncertainties, except for the UAE, which offers attractive structural opportunities.
EM LatAm	▶	Within the region, Brazil's exports are challenged by US trade tariffs while elevated policy rates remain a headwind.
Asia ex Japan equities		
Asia ex-Japan	▲	We prefer strong domestic players who can handle tariff risks and protect margins. The AI and tech sectors continue to benefit from supportive policies and structural trends. China, India and Singapore stand out for their stronger fundamentals.
Mainland China	▲	We expect China to maintain a pro-growth stance and accelerate tech self-sufficiency and economic rebalancing. We continue to favour industry leaders exposed to AI innovation, mass consumption, and quality SOEs paying high dividends.
India	▲	Domestic resilience and a favourable monsoon season support our GDP growth forecast upgrade for 2025 and 2026. We prefer large-cap stocks in the consumer discretionary, financials, industrials and heathcare sectors.
Hong Kong	▶	While equity outperformance is supported by liquidity inflows, underlying fiscal and retail weakness remain. We prefer banks, insurance, telecom and utilities for dividend income, as well as selected quality developers.
Singapore	▲	The market's defensive appeal and compelling dividend yield support its robust equity performance.
South Korea	▶	Strong YTD performance is driven by undemanding valuations and expectations of an acceleration of the Corporate Value-Up Program. However, these positives may have been priced in, while policy execution risks remain.
Taiwan	▶	The high-tech exposure to the US remains a key challenge, with the impact on semiconductor manufacturing subject to further clarity on chip tariffs. Political uncertainty adds to the downside risk.
Government bonds		
Developed markets (DM)	▶	We hedge against US trade policy and growth uncertainties by focusing on 7-10-year duration for DM sovereign bonds (except Japan) and maintain our preference for US gilts over Treasuries and Bunds.
United States	▶	Given the scale and liquidity of US Treasuries, we believe the concerns over fiscal debt and trade tariffs are overdone. We hold the view that the next Fed rate cut will occur in September and maintain our 7-to10-year duration preference for now.
United Kingdom	▲	UK gilts are challenged by near-term inflation uncertainty and heightened fiscal concerns. Nevertheless, weak UK economic growth, expectations of ongoing rate cuts and attractive valuations still warrant an overweight position.
Eurozone	▶	As we expect the ECB to remain on hold for the foreseeable future, relative interest rate differentials will start tightening. A further substantial rally from the current levels is limited.
Japan	▼	We expect the key opposition parties to call for further increases in JGB issuance to finance more aggressive fiscal stimulus. Concerns about fiscal sustainability will likely keep JPY rates volatile and the term premium in long-end JGBs elevated.
EM (Local currency)	▶	Falling inflation and a weaker USD offer room for EM rate cuts. Tariff decisions may weigh on corporate margins.
EM (Hard currency)	▶	We still find yields but remain selective and generally focus on quality bonds.
Corporate bonds		
Global investment grade (IG)	▶	We continue to use quality bonds to manage growth, tariff and geopolitical headwinds. Credit spreads are relatively tight as investors may prefer investment grade credit over Treasuries.
USD investment grade (IG)	▶	Given ongoing uncertainty around debt sustainability, the Fed rate outlook and tariff impacts, we maintain our preference for quality bonds. Spreads remain choppy but their all-in yields, fundamentals and liquidity are still attractive.
EUR investment grade (IG)	▲	Despite tight credit spreads, we believe EUR investment grade bonds can better compensate duration risk and offer attractive yields.
GBP investment grade (IG)	▲	GBP bonds are under-owned by international investors but offer yield levels similar to those of the USD market and a good risk-adjusted return trade-off given our outlook for more policy rate cuts.
Asian investment grade (IG)	▶	We continue to focus on quality Asian credit in Asian financials, Indian local currency bonds, and Chinese hard currency bonds in the technology, media and telecom sectors for their attractive carry.
Global high-yield (HY)	▶	Spreads are tight as risk appetite is high while equity volatility is low. We hold a shorter duration bias of 3 to 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. Delinquencies and debt levels bear monitoring, but non-performing loans remain below their five-year averages.
EUR high-yield (HY)	▶	In line with our global high yield view, we remain selective on EUR high yield 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)	▶	Although policy expectations have improved market sentiment somewhat, we remain cautious about China's property market, as the policy focus remains on boosting consumption and tech innovation.
Commodities		
Gold	▲	Gold remains a key diversifier amid market uncertainty although the uptrend may ease. Central bank buying continues to provide support.
Oil	▶	We expect oil prices to remain range-bound as excess supply limits the upside and geopolitical risk de-escalates.

Sector Views

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

Sector	Global	US	Europe	Asia	Comment
Consumer Discretionary	▶	▶	▼	▲	Initial Q2 reported sales and earnings have disappointed, particularly in luxury goods and autos. After years of above-inflation price rises and weak sentiment, consumers are switching to cheaper alternatives, creating a challenging environment for the companies. For Q3, consumer demand is likely to remain muted and highly selective.
Financials	▲	▲	▲	▲	Global Financials reported stronger-than-expected results for Q2. Net interest income is likely to remain elevated as inflation remains stubbornly higher than expected, keeping interest rates elevated. Trading activity and bond issuance are likely to remain strong in the near term. In Asia, we remain positive on China's economy and the improving sentiment in the region.
Industrials	▲	▲	▲	▶↓	We downgrade Asian Industrials after a period of outperformance that has seen valuations rise above their five-year average. US tariff concerns continue to weigh on sector sentiment and guidance. Q2 results have been muted so far, but order books remain relatively healthy. Digital infrastructure, aerospace, defence and construction are likely to benefit from a pick-up in capital spending.
Information Technology	▲	▲	▶	▶	AI demand remains resilient, with new AI-enabled products and services being launched across many industries and sectors. First-quarter results have beaten expectations, providing a reassuring outlook for software and hardware growth. The roll-out of AI- enabled products and services is gaining momentum, along with embedded AI- enhanced processes. Together, these should fuel additional demand for software, hardware and IT 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 uncertain outlook for most commodities has been a major headwind for mining stock and chemical stocks. Tariffs remain a risk that is hurting sentiment. Valuations are undemanding and the commodity cycle appears to be troughing, but this is far from certain. Persistently high energy and feedstock costs are likely to squeeze margins and profits. 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 refurbishments 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	▶	▶	▶	▶	Elevated geopolitical tensions have pushed energy prices higher but rising supply and weakening demand are expected to lead to lower oil prices in the next 12 months, although the relatively higher cost of production for shale gas may limit production. Seasonal demand in the northern hemisphere is likely to support gas prices. Low valuations, strong cash flow and high dividends somewhat offset the sector's speculative nature.
Healthcare	▶	▶	▶	▲↑	We upgrade Asian Healthcare due to improving demand dynamics, attractive valuations that are below their five-year average, and rising investor interest in a new wave of innovative medicines. In the US, ongoing government policy uncertainty and rising medicine pricing pressure remain. European Healthcare is trading at a 20% discount to its US peers, but sentiment continues to be negative for the sector.
Utilities	▶	▶	▲	▶	European Utilities are benefitting from favourable energy demand trends, positive price trends, and rising spending on energy infrastructure. Many economies are undergoing the electrification of transportation, expansion of digital infrastructure, and rising affluence, which drives demand for air conditioning, freezers, etc. Utilities are already operating at full capacity, so substantial capital investments are required to upgrade generation capacity and transmission infrastructure. Valuations are undemanding.

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