Looking beyond uncertainty

In conversation with Willem Sels, Global CIO, HSBC Global Private Banking and Wealth

Charlotte Kan:
Thanks for joining us. I'm here today with Willem Sels, Global Chief Investment Officer at HSBC Global Private Banking and Wealth, to discuss the investment trends for the third quarter and how investors can adapt to disruption.

Willem, thank you for joining us.

Willem Sels:
Thank you for having me.

Charlotte:
So, Willem, at a time where uncertainty seems to be the norm, how can investors react?

Willem:
Well, they need to react, because governments, corporates and households are reacting. Investors need to react as well to a world which is really fundamentally changing.

So clearly, the world is getting more regionalised from that excessive globalisation that we had. The world is moving more online especially during COVID, obviously, but that will remain with us. There is the question of energy independence, and I would argue that, you know, inflation will probably come down a little bit from here from a cyclical perspective, but it is structurally higher than it was before.

So, you know, the way that we invest in this is through our high-conviction, topical themes, which we will probably talk about, I'm sure.

Charlotte:
So how serious is the threat of stagflation? How much of a problem could it be for global growth, and how do you expect monetary policymakers to react?

Willem:
So stagflation is really the big elephant in the room that the market has been very worried about. You know, so stagflation we define as a recession plus high inflation.

Now, on the growth side, we expect a global slowdown and a broad-based slowdown, but not a recession. You will have some negative quarters of growth in this and that country, but basically not at the same time.

And that saves us to some extent from a global recession. Whilst one is slowing down, the other one is more resilient.

Also, we will need to invest a lot in that transition into bringing some of those supply chains closer to home, that energy revolution and so on. And that will prop up activity.

We do think that inflation will gradually come down – not very sharply – but we may have seen the peak. And investors are actually already pricing in a lot of rate hikes, probably a little bit too much, especially if growth slows down. Central banks may not hike as much as the market currently expects.

Charlotte:
So which geographies currently are proving to be more resilient to all this change we're seeing around us?

Willem:
So whilst Europe and the UK are clearly slowing down, and China may start to see a bottom towards the end of the year, actually, currently the resilient countries are the US – there is a reopening there taking place – and then the countries around ASEAN, in Asia and Hong Kong as well, are reopening.

So they are actually some of our overweights that we have in our equity portfolio as well.

Charlotte:
With a world more focused on protecting critical infrastructure like energy, food or even cybersecurity, where are the opportunities currently?

Willem:
We have a theme which is called 'Total Security', and it's broad-based. So, clearly because of that online shift, you know, all of our data need to be secure. So cybersecurity is very important.

We also have innovation around fintech, and there are a lot of opportunities there.

Then also within the security factor is that energy transition that is happening –

that energy independence that countries want to achieve, not just because of the sustainability revolution, but also geostrategically you want to have your energy supply secured and at a price that is not too volatile.

So there will be investment in renewable energy, also in fossil fuels – hopefully not too much more – and in sustainability, and that will happen around the world.

So opportunities in the US, in Europe and in Asia, in that sense.

Charlotte:
Despite the current global tech rut, digital transformation remains one of your high-conviction themes. Can you explain why?

Willem:
So part of the volatility and the, you know, downward trend in technology stocks is simply due to interest rates, because typically they are growth stocks. And growth stocks tend to be very sensitive to the ups and downs of interest rates.

Now, with, you know, so many rate hikes already priced in, we think that headwind should start to ease.

The reason why we continue to be optimistic is because of that shift towards an online economy. But also all of the potential due to innovation. So AI and 5G, the big gains in computer power, you know, allow a lot of innovation.

So we do think that trend is a structural trend that will continue. And hopefully soon – because those interest rates may stabilise – we will start to see a bottoming of those types of stocks.

Charlotte:
Willem, given the uncertainty currently about the macro outlook, what should be the common thread when picking quality assets?

Willem:
We have kind of redefined how we look at quality. So a company needs to weather obviously the short-term cyclical difficulties, growth and inflation, and it also needs to adapt to those structural changes.

And so when we look at a quality stock, it's first a company that probably has a strong market position to be able to protect its margins.

Secondly, it needs a strong balance sheet to be able to invest, to adapt to all of the structural changes to that supply chain reorientation, making its products cleaner and all of those kinds of things.

And ultimately, it needs to be inventive. We are looking for an innovative CEO and a company with strong human capital to be able to adapt.

So that's our new definition of quality, if you want.

Charlotte:
What have you identified as the key risks to your forecast, both on the upside and the downside?

Willem:
So in the short term, I think the market will continue to really focus on that growth and inflation picture, that stagflation debate that you were talking about, you know, and clearly the two big drivers of that have been, number one, the war in Ukraine, and then number two, COVID-related lockdowns and therefore the supply chain issue.

So, you know, any positive or negative movements on those variables would impact the market quite significantly.

The other important topic, obviously, is what central banks are doing, and they have, I would say, a very narrow landing strip if they want to, you know, achieve that soft landing. And they have to get it just right. So if they go too quickly or too slowly, that would both be negative for them.

Charlotte:
Finally, Willem, what's your message to investors?

Willem:
The correction we've already seen in the bond market and the equity market is ultimately going to lead, obviously, to attractive longer-term opportunities.

Where and when we enter the market is going to be a function of what is the market pricing in and also is there any change in the growth and inflation expectations.

So for the moment, for example, we really like shorter-dated corporate bonds, because we think those lots of interest rate hikes are priced in. And we have hedge funds as our biggest overweight currently because they benefit from that volatility.

And in the equity market, you know, we take some risks through selling options and volatility to generate income. We are also looking at, you know, private equity as a longer-term approach, and those quality stocks that you asked about, which are obviously well positioned for the cyclical and the structural changes.

Charlotte:
Thank you very much.

Willem:
Thank you for having me.