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Special Coverage

To Buy or Not to Buy?

Xian Chan
Global Head of Wealth Insights
HSBC Wealth and Personal Banking

Key takeaways

- We expect volatility to persist and remain "tactically neutral" on equities.
- Emerging Markets and Asian equities are long-term opportunities, but investors should be prepared for short-term market challenges.
- High-yield bonds - Asia, in particular - have become more attractive but liquidity issues and potential corporate defaults make us cautious. We are Neutral for now but Overweight for the long-term.

Investment View Summary

Bonds	Tactical view (1-3 months)	Strategic view (>12 months)
Developed Market Government Bonds	▼	▼
Emerging Market Government Bonds (local currency)	▲	▲
Global Investment Grade Corporate Bonds	▶	▼
Global High Yield Corporate Bonds	▶	▲

Equities	Tactical view (1-3 months)	Strategic view (>12 months)
Global	▶	▲
United States	▶	▲
Eurozone	▶	▲
United Kingdom	▶	▲
Japan	▶	▲
Emerging Markets	▲	▲
Central & Eastern Europe and Latin America	▶	▶
Asia (excluding Japan)	▲	▲

▲ "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.

Tactical view: Short-term view over 1-3 months that may differ from the long-term strategic asset allocation.

Strategic view: Long-term (>12 months) asset allocation to meet an investor's risk and return objectives.

Source: HSBC Global Asset Management, as of 1 Apr 2020.

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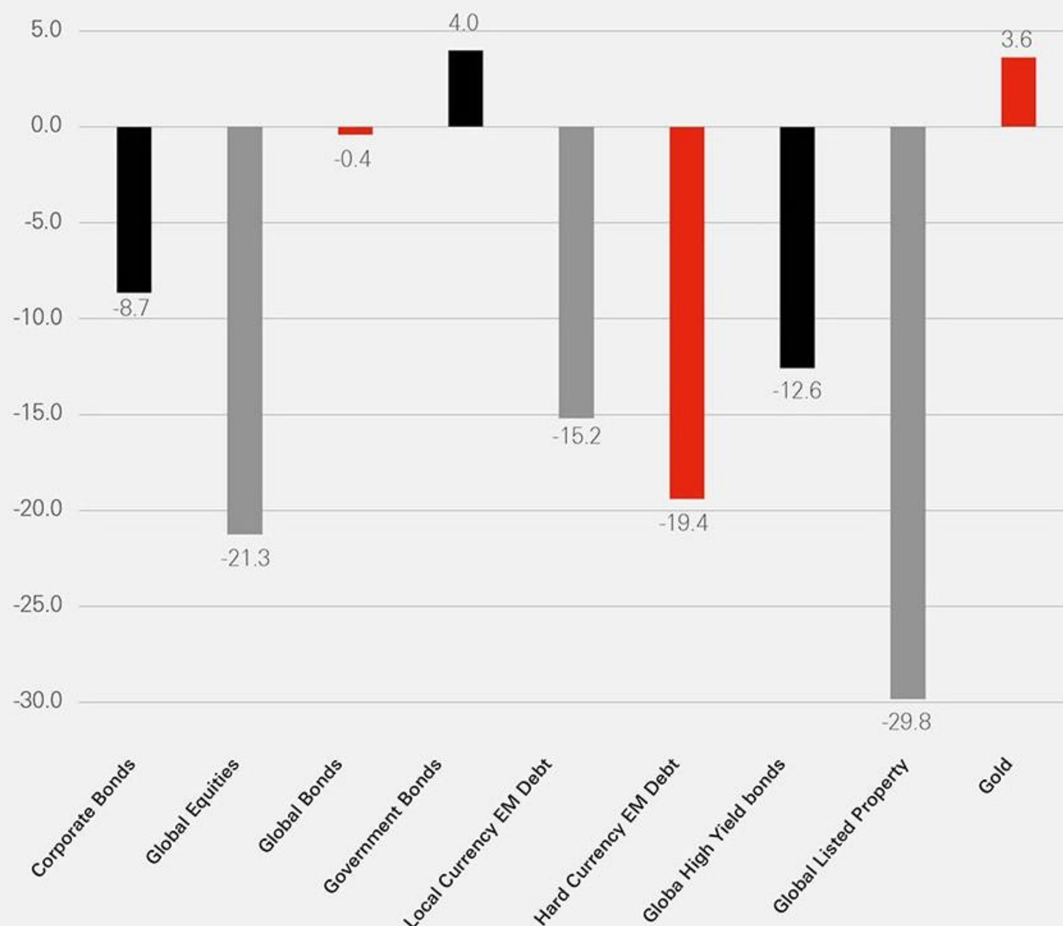
Finding direction in unprecedented times

To buy or not to buy? That is the question bolder investors are starting to ask. And who could blame them? After all, most asset classes are now priced more cheaply than at the start of the year. Global equities are down more than 20% (Chart 1) while the riskier types of fixed income investment have also sold off significantly.



But is now really the time to go bargain-hunting, or is it premature to do so?

The coronavirus outbreak is still a humanitarian tragedy of global proportions. The US has now joined Europe in confronting the full force of the outbreak, while the situation in parts of Asia seems to have improved somewhat in recent weeks.

To control the spread of the virus, populations in many countries are staying home and only venturing out for necessities like food and medical care.

Countless businesses have been forced to shut due to government enforcement or non-existent demand. This has impacted economic growth to the point where everyone now assumes we are in the midst of a global recession. The chart below shows how manufacturing activity – a key indicator of the health of the economy – around the world has already plummeted.

Chart 2: Global manufacturing activity has plummeted

Source: Refinitiv Datastream, Markit, HSBC. Data is as of 31 Mar 2020.

Manufacturing Activity represented by Global PMI Data (50 means no change)

There is speculation as to whether we will experience a “V-Shaped” recovery this year, where the economy bounces back with vigour once the worst is over. The answer no doubt depends on the length and severity of the crisis. The longer, deeper and more persistent the outbreak, the more likely we are to see permanent damage to the economy. On the flip-side, if the virus is successfully contained in the next few months and government measures succeed in supporting businesses and consumers through the worst, it’s entirely possible that things may look much better by year-end.

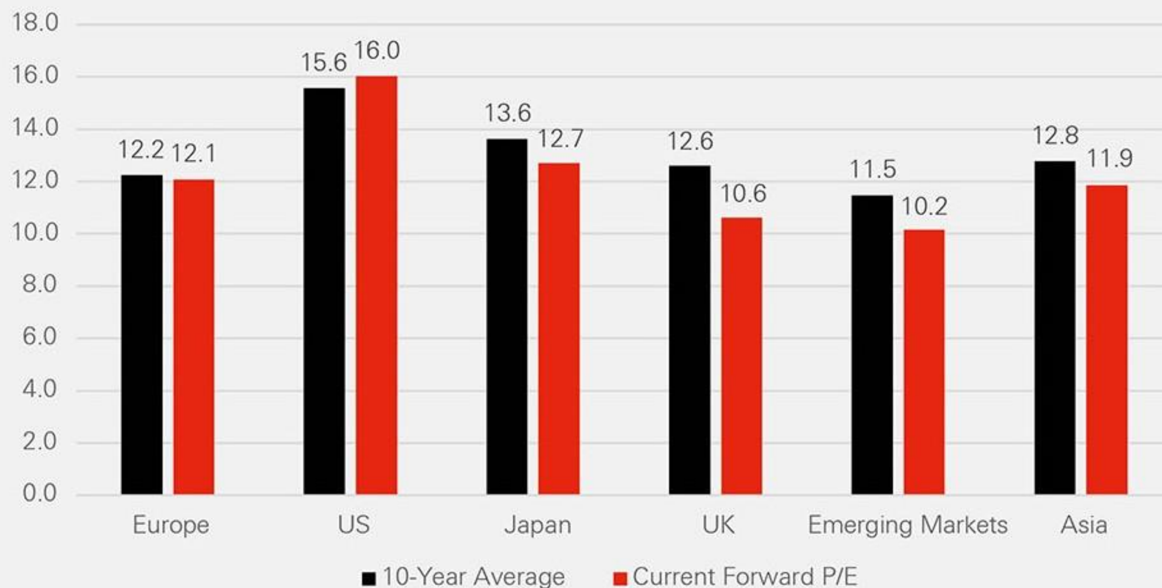
Being guided by the facts

Admittedly, this prognosis contains a lot of “ifs” and “buts”. But the reality is that no-one can yet predict the outcome with any degree of certainty.

So instead, let’s take a look at what we do know:

Firstly, we know that attempting to time the market is notoriously difficult, and we don’t recommend it. Trying to “predict the bottom” during volatile times is also dangerous, because you run the risk of missing out on any significant rebounds that happen in the interim.

Secondly, we know that the price of most asset classes has fallen significantly since the start of the year. Most equity markets have fallen by about 20% and are cheaper than their long-term averages, as illustrated in Chart 3. The valuations of riskier bond classes are also cheaper, with high yield bonds and Emerging Market debt (US Dollar-denominated) now offering double-digit yields over US Treasuries.



Source: Refinitiv Datastream, HSBC, Data as of 31 Mar 2020

Thirdly, we know that over the long-term, a well-diversified investment approach that favours attractively valued assets over less attractive ones, has plenty to recommend it. In particular, it allows investors to benefit from asset price growth over an extended period, while using effective diversification to weather any storms.

Although harder to spot, opportunities do exist

So what does this mean for our investment strategy?

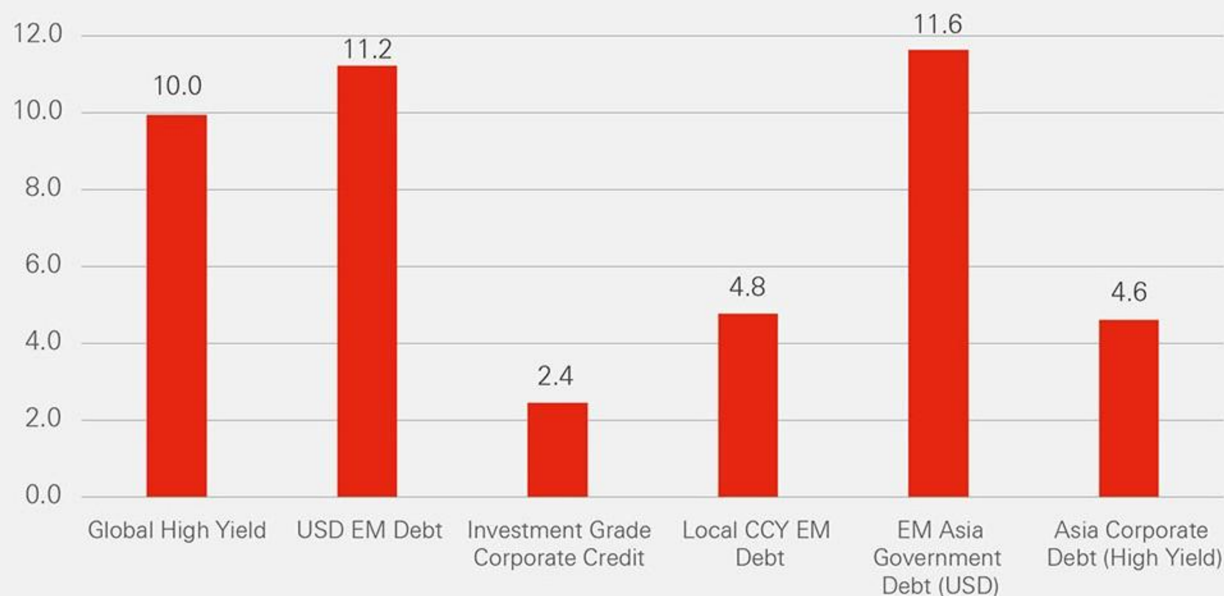
It's important to emphasise that for the reasons discussed above, we intend to err firmly on the side of caution in the coming months. Corporate earnings are likely to be weak, with a consequent effect on the stock market. Strong portfolio diversification will therefore be especially important.

However, while it may not suit the more cautious investor, we'd be remiss not to acknowledge that attractive pockets of opportunity do exist right now in the market.

We've already mentioned the attractiveness of equities. Within this asset class, Asian equities are our pick of the bunch. The continent's structural growth trend is still in play, and in the near term Asian countries, compared to many developed western markets, more arguably have ammunition to support their economies during tough times – in particular through monetary and fiscal policy.

On top of this, we are already starting to see signs that life in some Asian counties – China, for example – is starting to return to normal. If this continues it will be a huge boon for their economies.

In the case of fixed income, high yield bonds are an asset class that is starting to look attractive, as current valuations suggest investors are now getting compensated for the inherent risks. The chart below shows how currently these bonds may even provide double-digit yields over US Treasuries.



But here's the caveat. In volatile times, liquidity for these instruments can be challenging, meaning that the price advertised for high yield bonds isn't necessarily the price you can transact at. This lack of liquidity can have a detrimental impact on portfolio performance, which is why we're staying cautiously neutral over the next three months.

Nonetheless, the time is no doubt fast approaching when investors should consider going overweight high yield bonds – i.e. when things start returning to normal and liquidity returns. Our preference, as ever, is to seek out higher-quality spectrum, while staying clear of lower-quality companies which may struggle to survive in the current environment. As with equities, our preference right now is for Asian high yield bonds.

Translating insight into action

In summary then, it's well worth considering the longer-term opportunities out there. Having an investment plan, and drip-feeding some, but not all of your money into some of these assets may prove fruitful in the long run, providing it's done in a systematic, diversified manner.

But it's also worth repeating that, with renewed volatility expected in the short term, this approach is probably not for the faint of heart. For those who prefer a sound night's sleep, a more defensive approach to navigating the coming volatility may be more appropriate.

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