Video Transcript

HSBC Global Private Banking – February 2024

Zooming In: Episode 1 – Reasons to stick with US stocks
Willem Sels and Nicole Inui

Willem:

Welcome, everyone, to our new video series called Zooming In, where we are going to focus on a burning topic for investors.

And today we wanted to talk about the US equity market, which has continued to outperform other markets. And the same can be said about the US economy. And we remain overweight on US stocks and see many opportunities there.

So, to dive into this, I've invited Nicole Inui, who is Head of Americas Equity Strategy at HSBC Global Research.

Nicole, welcome and thanks for joining us.

Now, one key area of strength of the US economy has been the consumer. And with wage growth still relatively high and inflation falling, this should be a good environment for consumer related stocks, isn't it Nicole?

Nicole:

So for 2023, the surprise was the US consumer. The US consumer was much more resilient than we had initially anticipated. And part of this is the strong labour market and this is something we continue to see into 2024.

But also it was the impact that higher rates had on the US consumer. So initially we thought with higher rates this would really impact consumer spending. But what we saw is the US consumer had locked in those low fixed rate mortgages. So as interest rates went up, it really had less of an impact on consumer spending than we initially thought.

Now, looking into 2024, it's a little bit different. So we are starting to see some impact of higher rates in certain aspects of the consumer. So the low- and middle-income consumers are experiencing a higher delinquencies on credit cards and auto loans. So we could start to see a trade down of the middle consumer to lower brand of products. For the higher income consumer, we think consumer spending will still stay pretty resilient. The high-end consumer has excess savings and they are feeling the wealth effects of higher home prices and of course, a higher stock market, as you had mentioned.

Willem:

So what does that mean in terms of strategy within the consumer related stocks, Nicole?

Nicole:

So we think you should really take a barbell approach. So focus on those stocks that are focused on a low income consumer, because you will see these middle income consumers trading down. So you'll see demand there. And on the higher end, that consumer spending will stay resilient.

We think the focus will be on experiences and that will take a larger share of the consumer wallet.

So those companies focused on that should perform well through the year.

Willem:

Now, in one of your recent reports, you actually talk about the US elections, which we can't avoid as a topic. And you say that historically the consumer area as well as industrials have done well in a year of an election. Can you explain why that is?

Nicole:

So, yes, we looked over the past election cycles to try to see which sectors outperform on a relative basis. And consumer discretionary and industrials are two sectors that we have noticed tend to outperform during an election year.

So why is that? What we've seen during election years, usually consumer confidence picks up and we're actually seeing that today in the US. If you look at the consumer confidence data for December and January, it is on an uptick and that tends to support consumer discretionary stocks. It's an important leading indicator. And on the industrial side, I usually see some sort of announcements or expectations of announcements of additional fiscal spending in the form of infrastructure, which tend to support industrial stocks.

Now, we do have the election this year, but we have another very important event – the Fed pivot. So we expect the Fed to start cutting rates in June and lower rates tend to be positive for cyclical sectors such as consumer discretionary and industrials.

Willem:

It seems that when I think about the election, both top Presidential candidates are eager to bring manufacturing back to the US, and to some extent this has already kicked off with the CHIPS & Science Act and then the Inflation Reduction Act, which is expressed in our investment theme around North American Re-Industrialisation. What do you see on the ground around this topic?

Nicole:

So yes, this is a very important topic. We've had three very important pieces of legislation that have passed over the past few years. The Infrastructure Investment Act, the CHIPS Act, the Inflation Reduction Act. And combined, these three pieces of legislation represent about $2 trillion of additional federal spending that we'll see over the next ten years.

And if you look at the data, we are already starting to see some impact of this additional spending. We took a look at US construction, non-residential construction spending, and it's booming.

So it's up around 20% year over year. And this is despite the fact that we're in a higher rate environment.

Willem:

Now, of course, we have to talk about AI and technology. And the question we often get from clients is how far can these stocks rally further clients is how far can these stocks rally further after the rally that we've already seen?

Nicole:

Yes, we cannot avoid the discussion on AI and tech. If you look at tech and specifically companies with exposure to the AI theme, they have really driven the stock market returns over the past year, even over the past month. So right now, these stocks are trading at a pretty hefty premium on a valuation basis compared to the overall market.

But also these companies are reporting very strong earnings growth and very high profitability when we look at profit margins and look on the returns over equity.

So we see this excitement over AI that we saw in 2023. We see that continuing into 2024. It will be very interesting to see sectors discussing how they will monetise these efforts surrounding AI. And we think investors will start to focus on the early AI leaders. So as always, stock picking will be key.

Willem:

Indeed, it will be. And to conclude, clearly there are opportunities in technology, but also in other sectors such as consumer discretionary and industrials, which is very much in line with our strategy at the Private Bank, which is to broaden sector exposure in the US: for example, through thematic ideas like North American Re-Industrialisation and American Resilience.

So to all our clients, I hope you enjoyed this video.

And Nicole, thank you for your insights.

Nicole:

Thank you for having me.