HSBC World Selection® Portfolio
Review and Outlook

Using a "swoosh-onomics" lens to assess the recovery

Key takeaways

- HSBC World Selection Portfolios posted positive gains over the third quarter.
- Economic activity has picked up quickly from exceptionally depressed levels.
- After the initial surge, growth is now set to moderate as economies enter the next phase of the recovery—the "flattening of the swoosh."
- Monetary and fiscal policies continue to support household incomes and businesses.

Q3 review and outlook

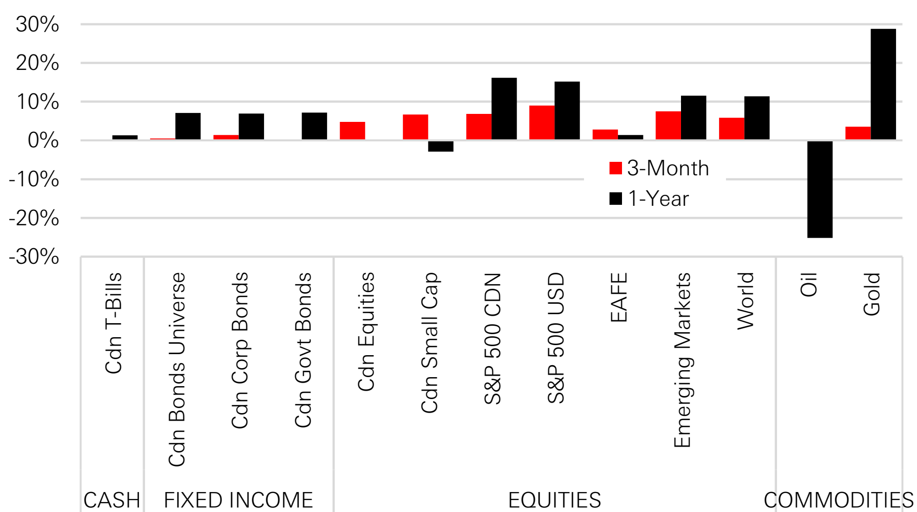
The HSBC World Selection Portfolios (the Portfolios) posted positive gains over the quarter as the global economy continued to improve. For full details of Portfolio performance, please refer to your quarterly statement.

The strong growth in the third quarter continued, albeit at a more modest pace than the second quarter. This is in keeping with our most likely scenario of a "swoosh-shaped" recovery for the global economy. Economic activity has picked up quickly from exceptionally depressed levels. After the initial surge in growth, it is now set to moderate as economies enter the next phase of the recovery—the "flattening of the swoosh."

Strong third-quarter data supports this view. Monetary and fiscal policies continue to support household incomes and businesses. But the growth trajectory is now set to flatten out amid abnormally high unemployment, low consumer and business confidence, and high savings rates.

In the third quarter, US equities gained 6.83%, international equities were up 5.85%, and emerging markets gained 7.45%. Closer to home, Canadian equities underperformed their US counterpart delivering a 4.73% return. The bulk of the return was driven by the industrials and utilities sectors.

Index returns



Sources: RIMES and Bloomberg Canada as at September 30, 2020. All returns in Canadian dollars, except where specified. Past performance is not indicative of future performance. All returns are gross. For illustrative purposes only. One-year performance: September 30, 2019, to September 30, 2020. Indices represented are: FTSE Canada 91 Day T-Bill Index (Cdn T-Bills), FTSE Canada Universe Bond Index (CAD) (Cdn Bonds Universe), FTSE Canada Universe All Corporate Bond Index (Cdn Corp Bonds), FTSE Canada All Government Bond Index (Cdn Govt Bonds), S&P/TSX Capped Composite Index (CAD) (Cdn Equities), S&P/TSX Small Cap Index (CAD) (Cdn Small Cap), S&P 500 Total Return Index (CAD) (S&P 500 CDN), S&P 500 Total Return Index (USD) (S&P 500 USD), MSCI Europe, Australasia a nd Far East (EAFE) Net Index (CAD) (EAFE), MSCI Emerging Market Net Index (CAD) (Emerging Markets), MSCI World Net Index (CAD) (World), Crude Oil Futures (CL1 Comdty) (Oil), Gold Future (GOLDS Comdty) (Gold).

- After a strong rally in North American equities since the lows in March, we trimmed our exposure and redeployed the proceeds to Canadian bonds to provide a cushion against volatility as we entered the fall.
- Based on our analysis, we see market valuations as broadly reasonable at this point
- Our outlook currently points to a recovery that will take 18-24 months to return activity to pre-COVID levels.
- Our investment philosophy remains unchanged and the Portfolios will maintain their broadly diversified investment approach.
- We will continue to use market volatility as a potential opportunity to improve the risk-return profile of the portfolios.

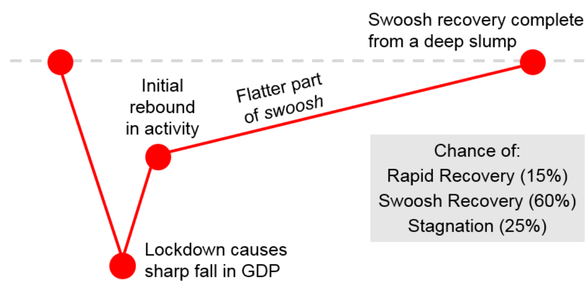
After a strong recovery, we have made adjustments entering the fall

Amid this ongoing uncertainty, we adjusted the portfolios in late August to reduce exposure to US and Canadian equities to a slightly overweight tactical position regionally. We also increased our underweight position in global real estate equities and redeployed the proceeds to Canadian bonds. Although prospective returns for Canadian bonds are lower than riskier asset classes, they provide a cushion against volatility. We are closely balancing potential asset class returns against the ongoing risks in the market and continue to look for investment opportunities.

Investors questioning the "rally in everything"

While we appear to be past the worst, the situation is far from normal. Many investors have commented that there is an "eerie vibe" in markets due to the worry that the "rally in everything" might be on shaky foundations.

Is this "rally in everything" disconnected from economic fundamentals? Our analysis says no, and we do not see any irrational exuberance in market pricing. The markets are forward looking. Pricing in many markets now discounts a swoosh-style recovery. Based on our analysis, that seems like an acceptable baseline scenario, and it means we see market valuations as broadly reasonable at this point.



For illustrative purposes only. Source: HSBC Global Asset Management, Macrobond, September 2020. Any views expressed were held at the time of preparation and are subject to change without notice. While any forecast, projection or target where provided is indicative only and not guaranteed in any way. HSBC Global Asset Management (UK) Limited accepts no liability for any failure to meet such forecast, projection or target.

A recovery forecasted to take 18-24 months

Our outlook currently points to a recovery that will take 18-24 months to return activity to pre-COVID levels. The forecast assumes a continuation of aggressive policy measures, a gradual reopening of the global economy and for there to be a widely available vaccine at some point in 2021.

In the near term, there is upside potential, linked to better news and momentum, while the downside risks are around the US election, the continuing re-emergence of the virus, policy error that leads to a reduction of monetary or fiscal support, or long-term damage to economies. We view these competing pressures as roughly balanced.

Continuing to maintain diversification in the face of market volatility

As the global economy continues to face a challenging environment, we recommend a well-diversified approach across asset classes and geographies. Our investment philosophy remains unchanged and we will continue to use market volatility as a potential opportunity to improve the risk-return profile of the portfolios.

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