

Looking past the abyss  
穿越市場陰霾

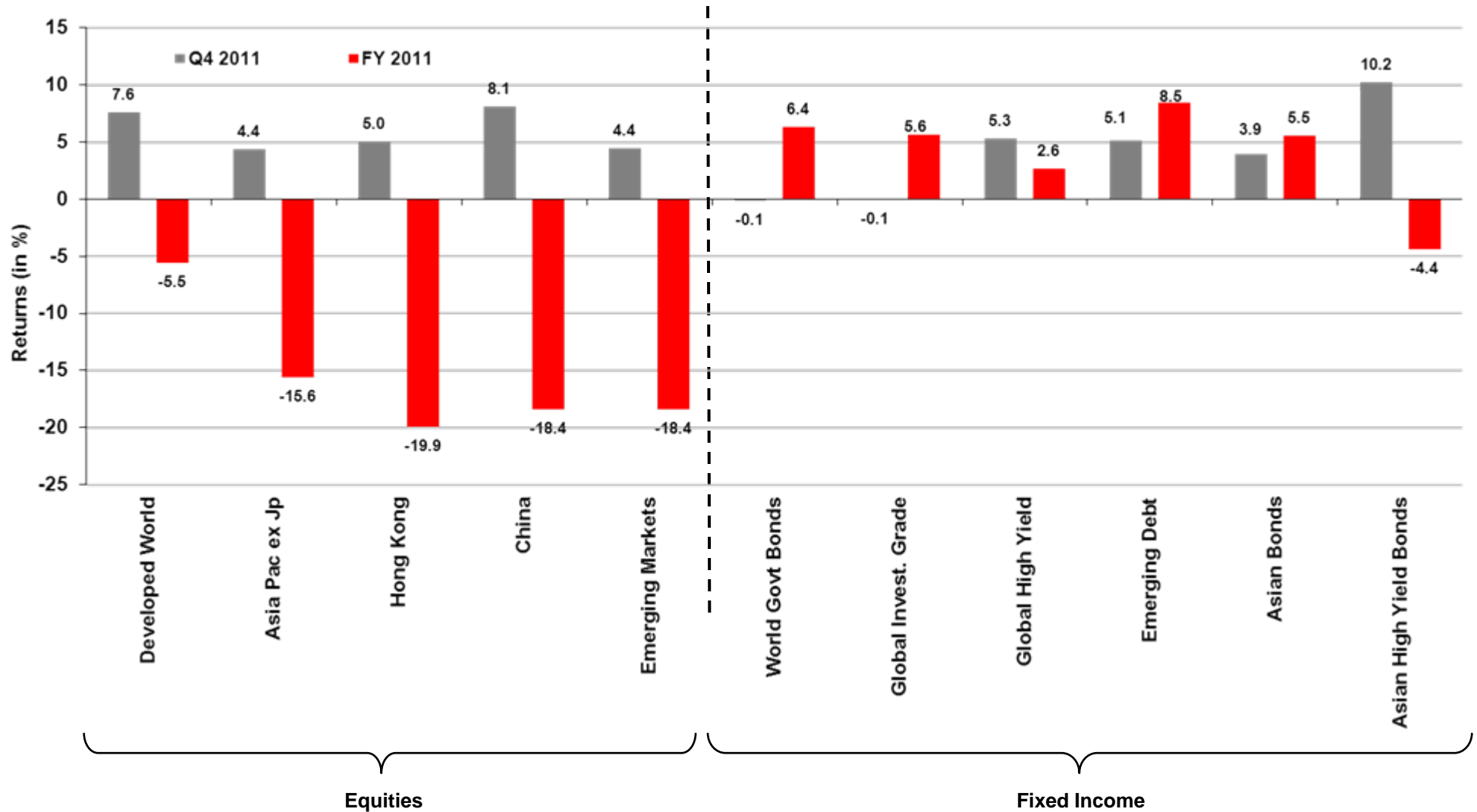
-- 2012 Outlook



# Market Overview



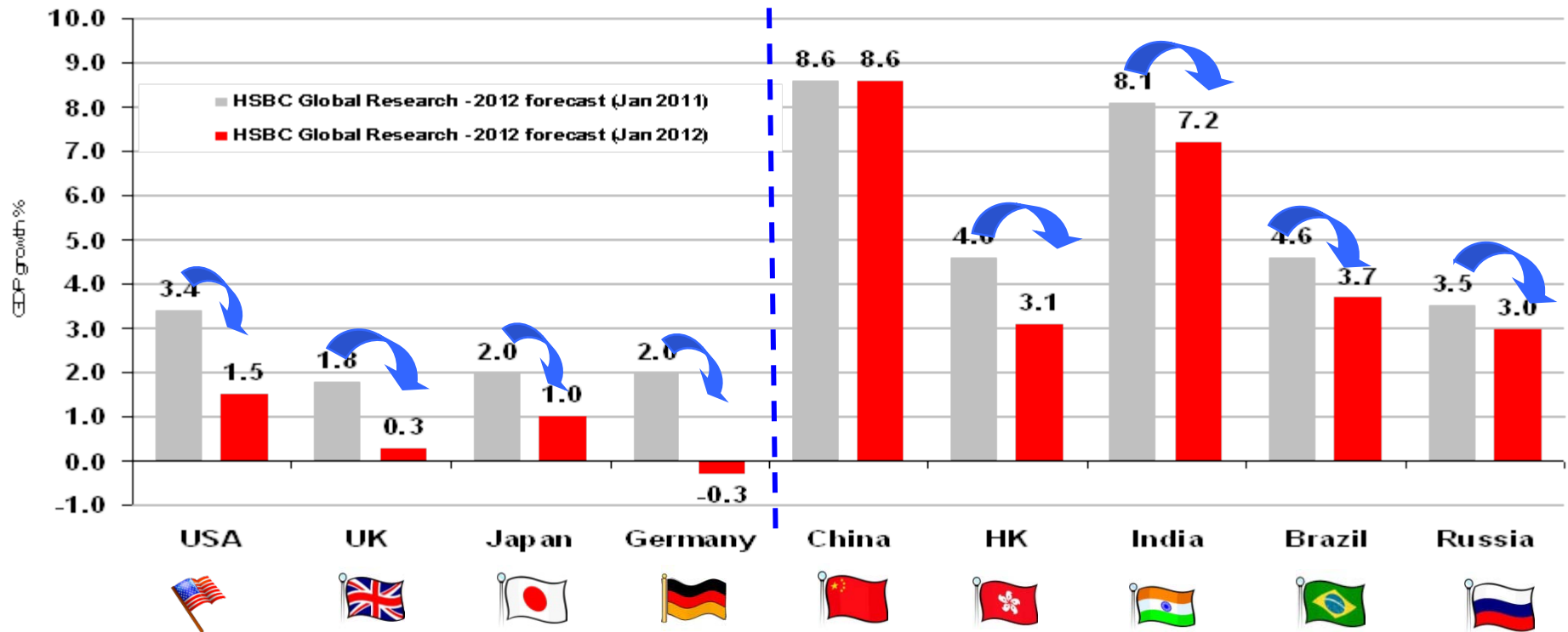
# Market performance in 2011



Source: Morningstar and Bloomberg. Data as at 31 December 2011. Total Returns in USD

# 2012 GDP growth forecasts remain positive for all major economies, despite recent downward revisions

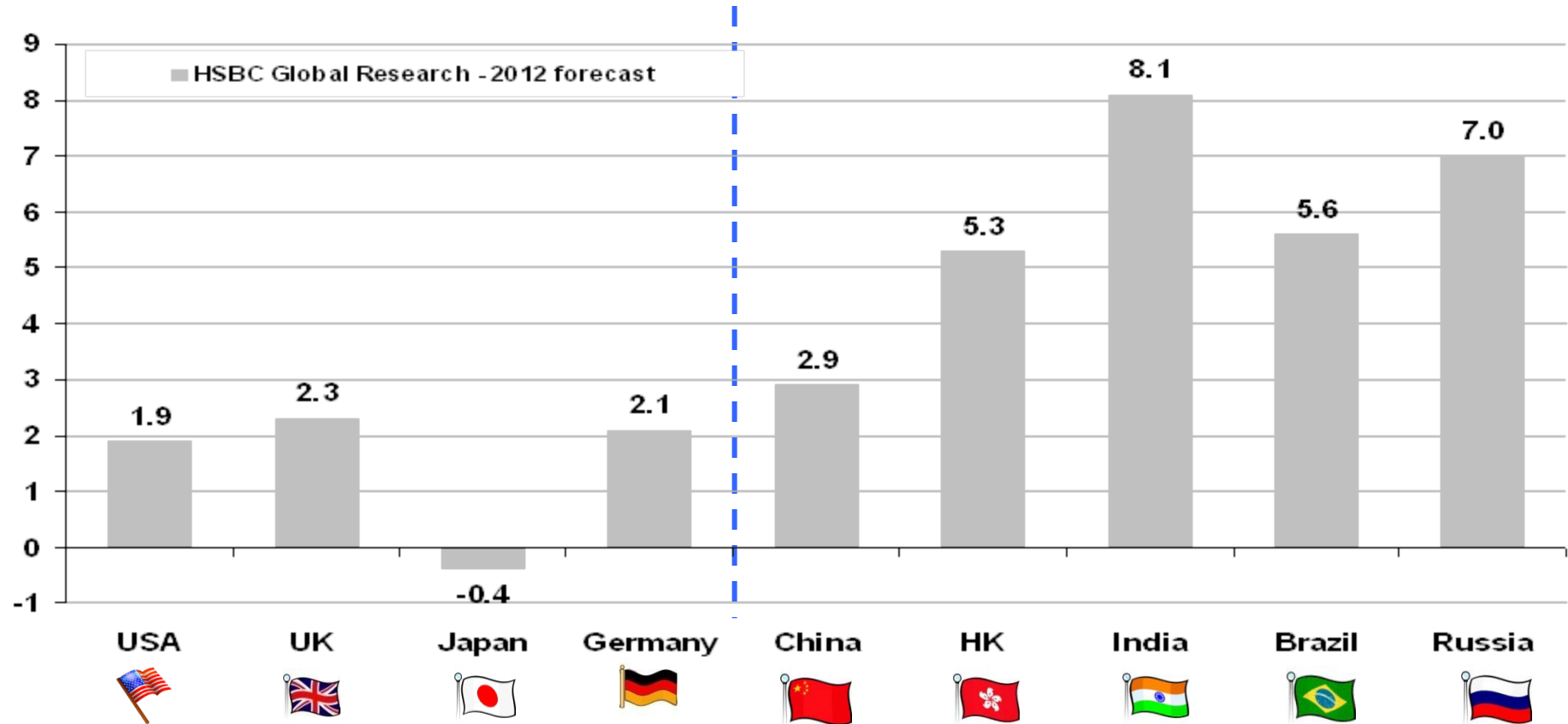
2012 GDP growth forecasts (%) – Jan 2011 vs Jan 2012



Source: HSBC Global Research. Data as of 3 January 2012.

# Rate of inflation is expected to stay high in emerging markets

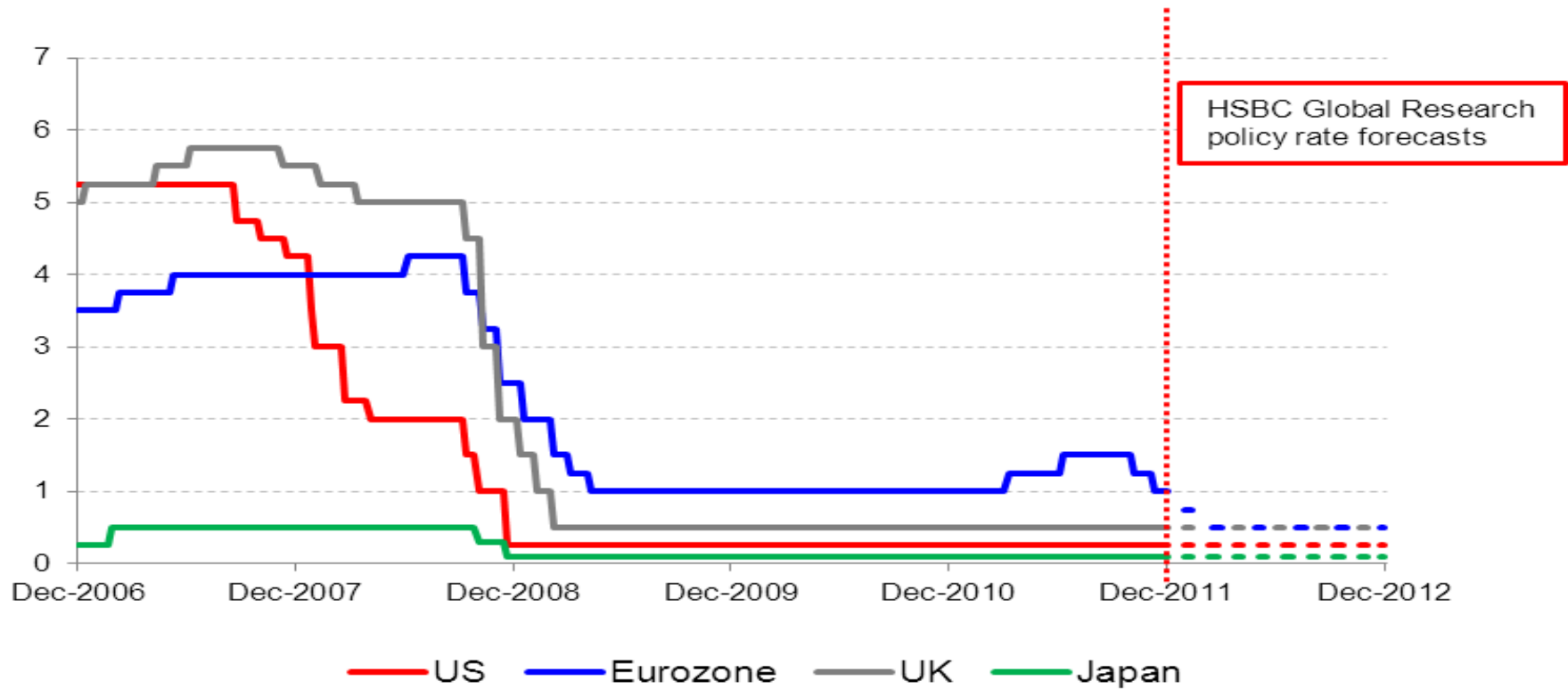
2012 Inflation forecasts (%)



Source: HSBC Global Research. Data as of 3 January 2012. Any forecast, projection or target contained in this presentation is for information purposes only and is not guaranteed in any way. HSBC accepts no liability for any failure to meet such forecasts, projections or targets. For illustrative purpose only.

# Interest rates expected to stay low

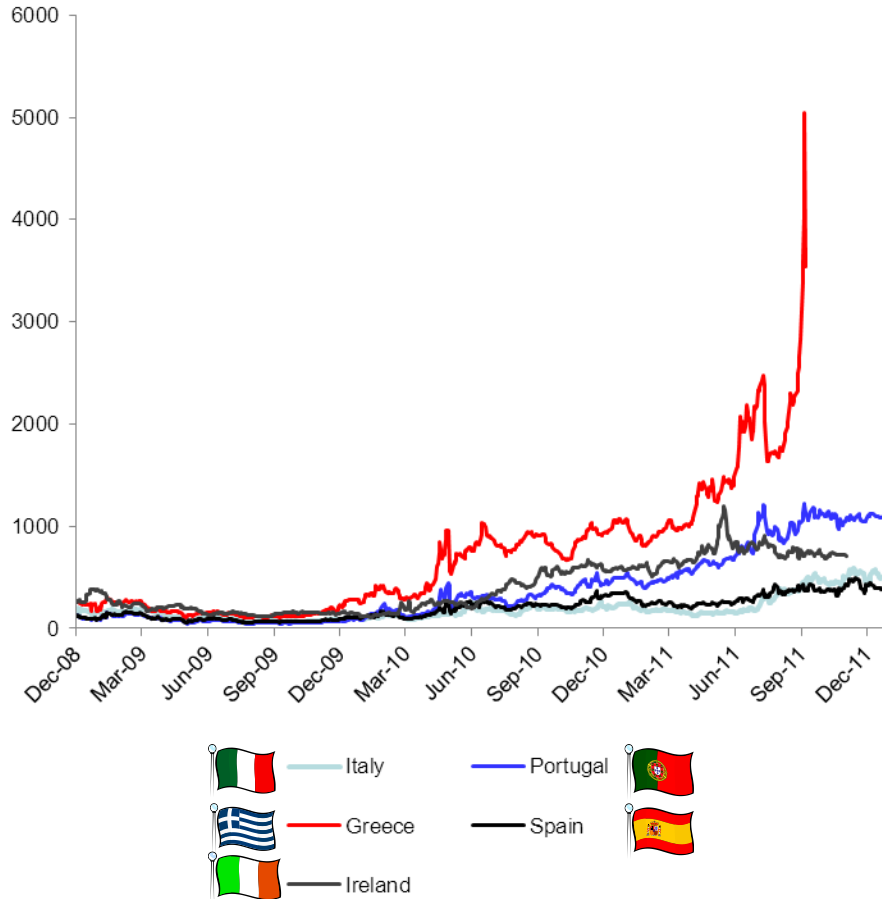
Developed market policy rates and forecasts<sup>(1)</sup>



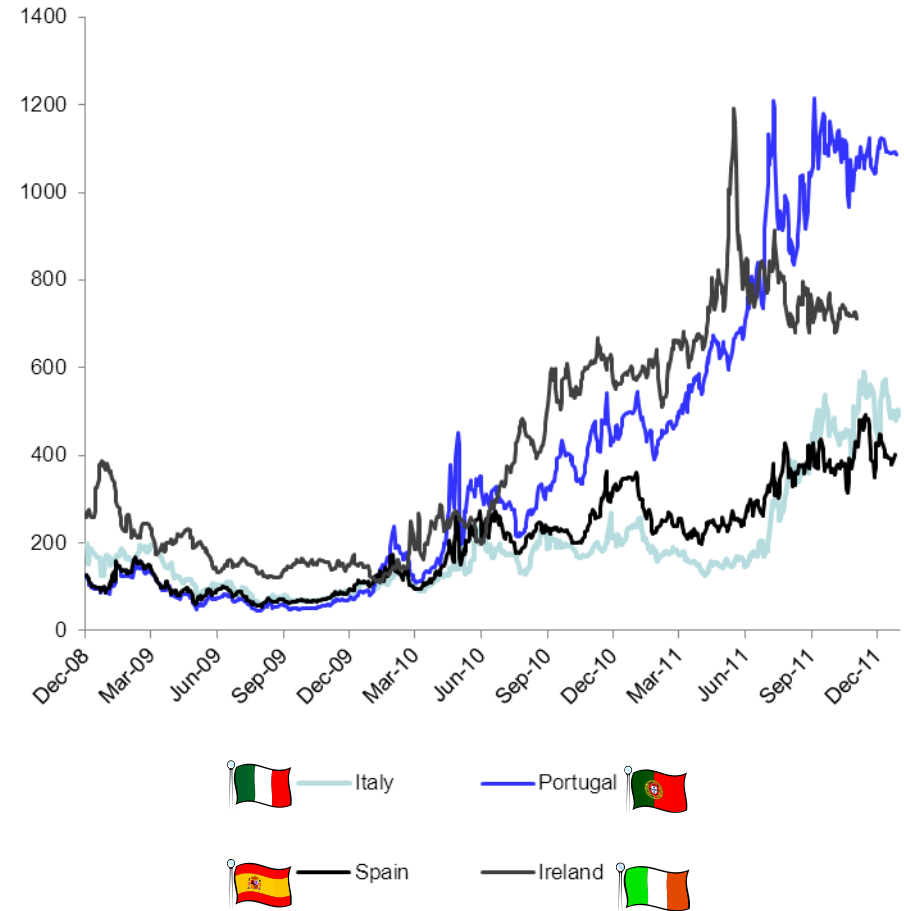
Source: HSBC Global Research and Bloomberg. Data as at 31 December 2011. Any forecast, projection or target where provided is indicative only and is not guaranteed in any way.

# Eurozone worries to continue

Credit default swap spreads – Eurozone peripherals



Credit default swap spreads – peripherals w/o Greece



Source: Bloomberg. Spreads based on 5 years CDS, data as at 31 December 2011.

# What's ahead?

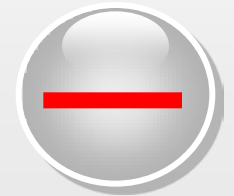
## Opportunities

- Global recovery continues at an uneven pace
- Equity valuations are reasonable
- Corporate earning growth has been strong
- Continued policy support

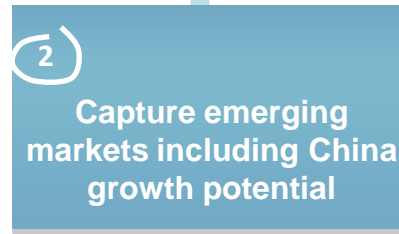


## Risks

- Uncertainty with Eurozone debt crisis
- Swinging investor sentiment
- Slowdown in global economic growth



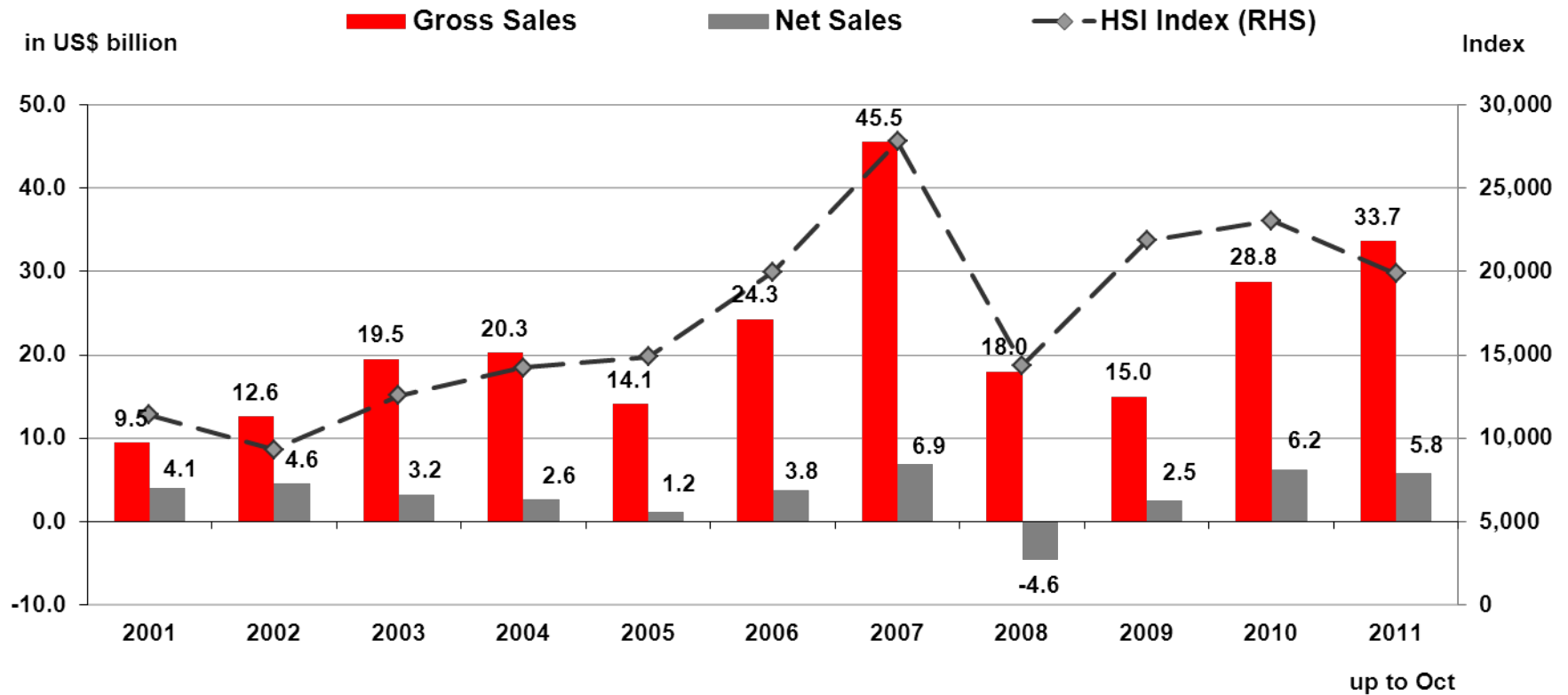
## Investment Themes



# 1Q Investment themes

# Customer behavior trend – gross & net sales

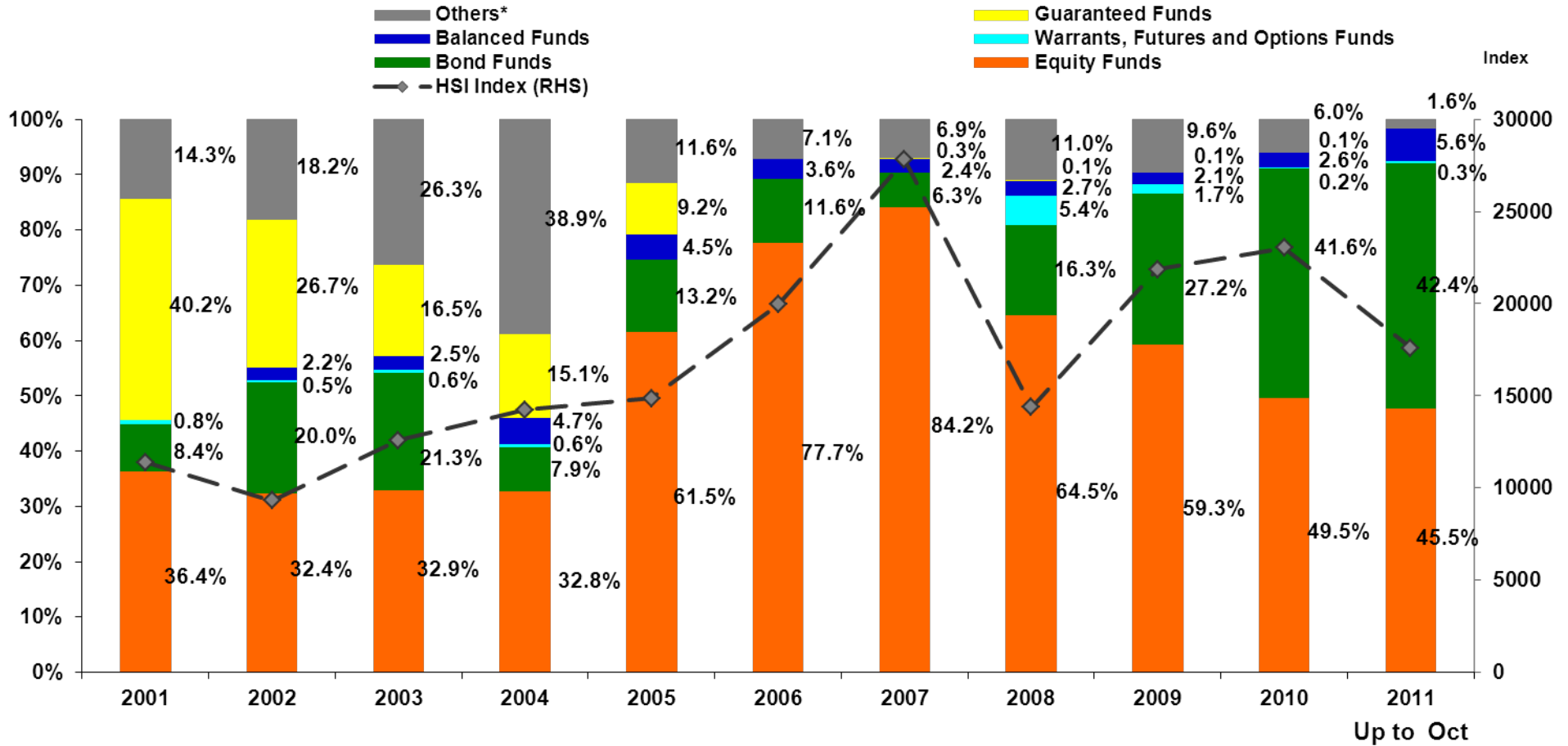
## Hong Kong Retail Fund Gross & Net Sales



Source : Bloomberg and Hong Kong Investment Funds Association (IFA). Data as of Oct 2011.

# Customer behavior trend – by fund categories

## Gross Sales Breakdown by Major Fund Categories



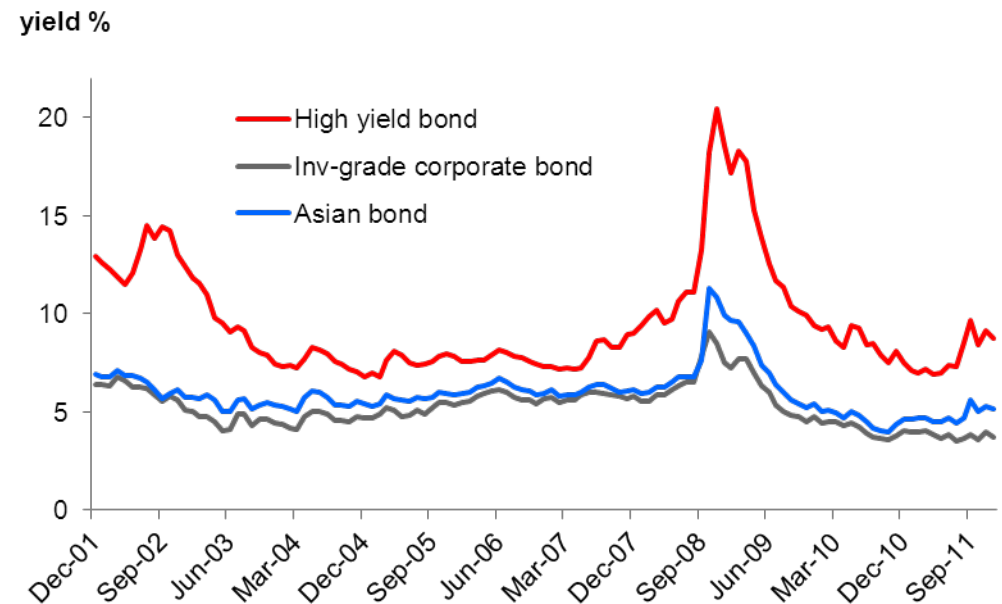
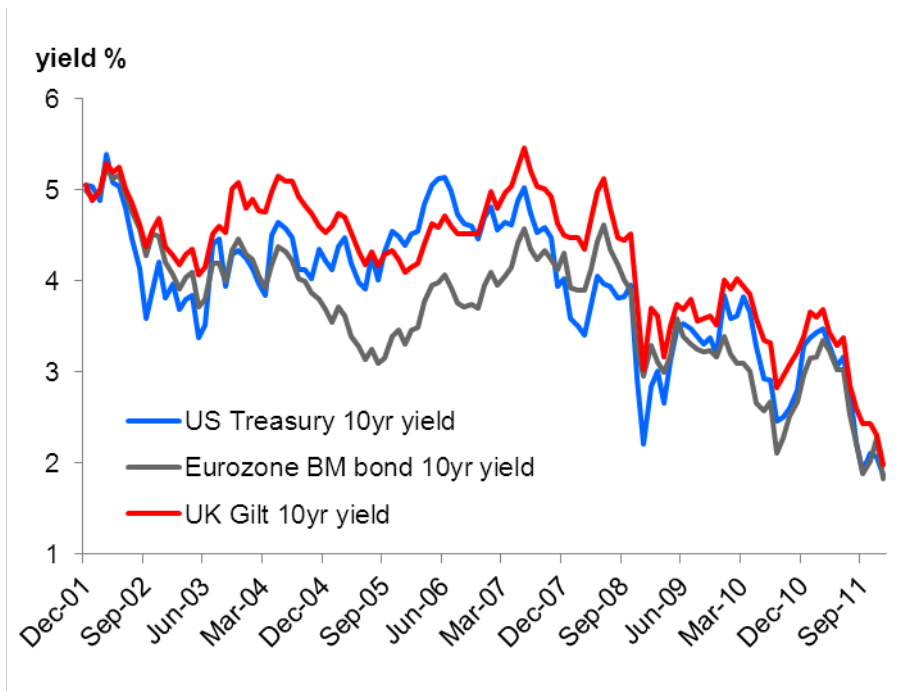
\* Include Money Market Funds / Liquidity Funds, Equity Index Funds, Fund of Funds, Hedge Funds and Other Funds.

Source : Hong Kong Investment Funds Association, Bloomberg. Data as of Oct 2011

## Theme 1: Yield Enhancement

### Unattractive valuations for developed market government debt

- ▶ Government bonds look unattractive with the prospect of negative real long-term returns
- ▶ Corporate bonds could offer better value with solid balance sheet and low default rates in low interest rate environment



Source: Bloomberg. Data as of 31 Dec 2011. High yield bond = BarCap Global High Yield. Inv-grade corporate bond = BarCap US Aggregate Corporate Bond. Asian Bond = CS Asian bond. Information above refers to the past and should not be seen as a guide to the future.

# Solid Asian economic fundamentals lead to rating upgrades

- ▶ Solid economic progress has been rewarded by credit rating upgrades in recent years
- ▶ Default rates, which are indicator of health in corporate bond sector, have continued to remain low

## Asia credit ratings continue to see upgrades since 2010

Countries / Regions	Ratings since 2010	Current ratings
Hong Kong	AA+	AAA
Singapore	AA+	AAA
China	A+	AA-
Indonesia	BB	BB+
Philippines	BB-	BB

Source: Bloomberg and Standard & Poor's as at 21 Dec 2011. Based on foreign currency long term ratings.

## Default risks of bonds with different credit ratings\*

Credit rating	Characteristics	Default risks*	Average yield *
AAA	Investment grade	0.01%	2.48%
AA			2.92%
A			3.67%
BBB	Non-investment grade	0.20%	4.70%
BB			6.95%
B			8.60%
CCC and below	Extremely speculative	7.9%	14.01%

\* Default risks are dependent on technical factors such as availability of funding and credit downgrades.  
Source: Bloomberg and Standard & Poor's as at 21 Dec 2011. Based on foreign currency long term ratings.

## Local currency bonds benefit from FX outlook

- ▶ Local currency denominated sovereigns can selectively offer higher yields than their USD equivalents, as well as currency upside
- ▶ In longer term, Asian currencies are well placed to appreciate, reflecting their long-term structural advantages, although policy actions may slow down the process

### Asian currencies expected to appreciate against USD

Currencies	Current levels <sup>1</sup>	Q4 2012 forecast <sup>2</sup>	Potential upside <sup>2</sup>
Malaysia ringgit	3.17	2.88	10.0%
Thai baht	31.55	28.80	9.5%
Taiwan dollar	30.28	28.00	8.1%
South Korean won	1152.45	1070.00	7.7%
Philippine peso	43.84	41.00	6.9%
Chinese renminbi	6.29	6.15	2.4%

Source of data: <sup>1</sup> Bloomberg. Data as at 31 Dec 2011. <sup>2</sup> HSBC Global Research. Data as at Dec 2011.

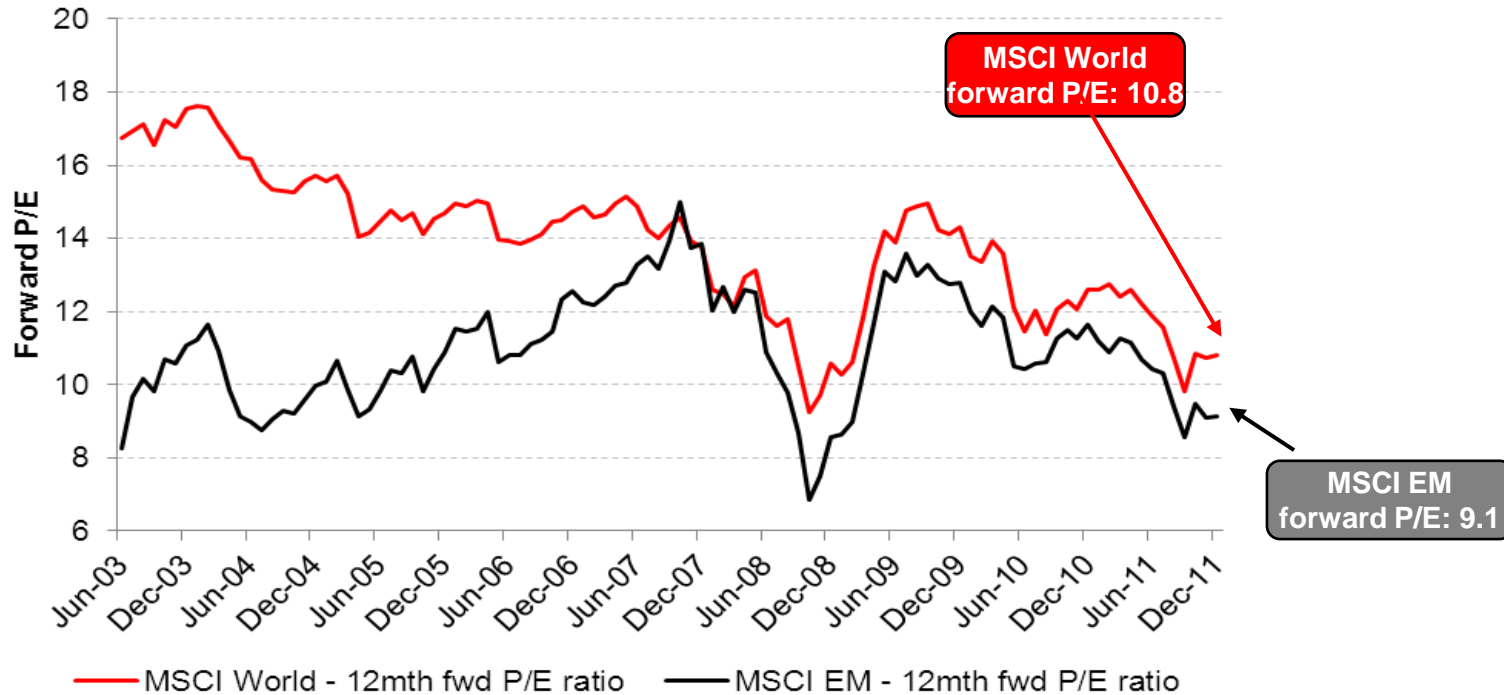
## Theme 2: Capture emerging markets including China growth potential

### Emerging markets: Bear / Bull markets

	Dates	% Increase	# of months		Dates	% Decline	# of Months
<b>Bull</b>	01/88 -08/97	619%	116	<b>Bear</b>	08/97 – 09/98	-56%	13
<b>Bull</b>	09/98 – 04/00	114%	19	<b>Bear</b>	04/00 – 10/01	-49%	17
<b>Bull</b>	10/01-11/07	537%	73	<b>Bear</b>	11/07 – 10/08	-65%	12
<b>Bull</b>	10/08 -						
<b>Average</b>		<b>423%</b>	<b>69</b>			<b>-57%</b>	<b>14</b>

Source: Franklin Templeton Investments. Based on 30% changes, average does not take into account bull numbers.

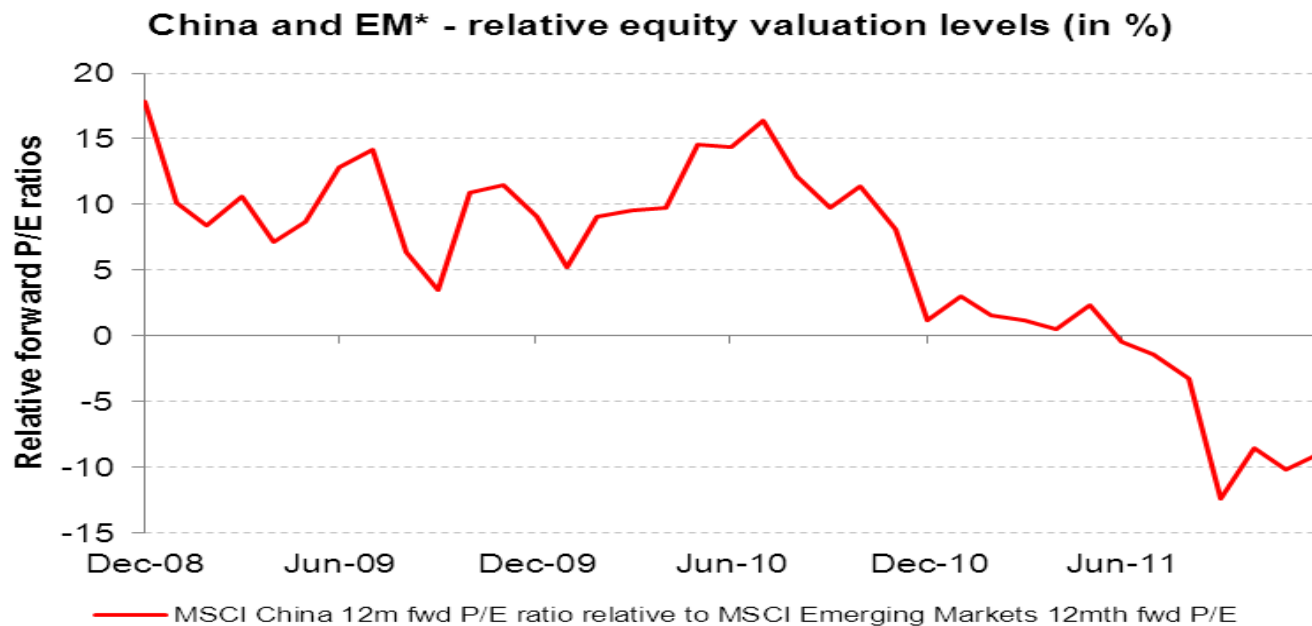
# Current equity valuation levels could offer interesting opportunities



Source: Bloomberg. Data as at 31 December 2011. "MSCI World" consists of 24 developed market country indices, "MSCI Emerging Markets" consists of 21 emerging market country indices. Performance information above refers to the past and should not be seen as a guide to the future.

## Chinese equities are particularly attractive

- ▶ Chinese equities are trading 12-month forward PE at 8.3x, 40% discount compared to 5-year historic average
- ▶ Robust economic growth and slowing inflation rate should have a positive impact on market sentiment
- ▶ Investors with positive view towards China could pave way for upside potential



Source: Bloomberg and HSBC. Data as at 31 December 2011. \*EM = Emerging Markets. "MSCI Emerging Markets" consists of 21 emerging market country indices. Performance information above refers to the past and should not be seen as a guide to the future.

## Theme 3: Diversification remains key

### Diversification helps you optimize the risk return payoff of your portfolio

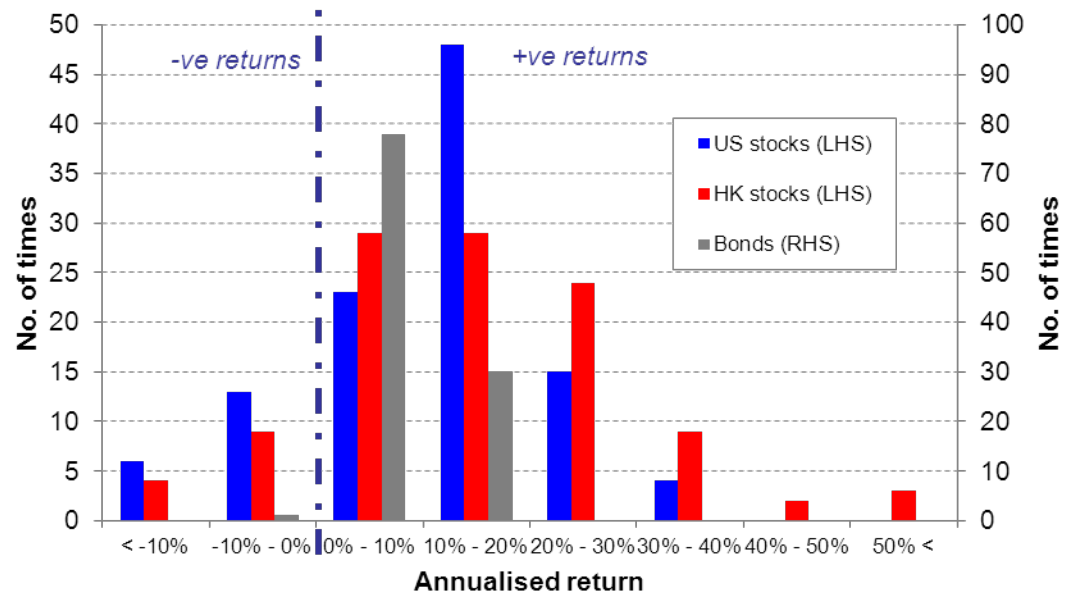
#### Bonds

- ▶ The probability of receiving 0-10% return from investing in bonds for three year is higher than 50%
- ▶ The average return is lower than stocks at around 8.2%, but variations in returns are also much less

#### Stocks

- ▶ The variations of returns on stocks are much wider than bonds, with higher potential gain and loss
- ▶ While HK stocks are “riskier” than US stocks, the average return is also higher (14.9% vs. 11.2%)

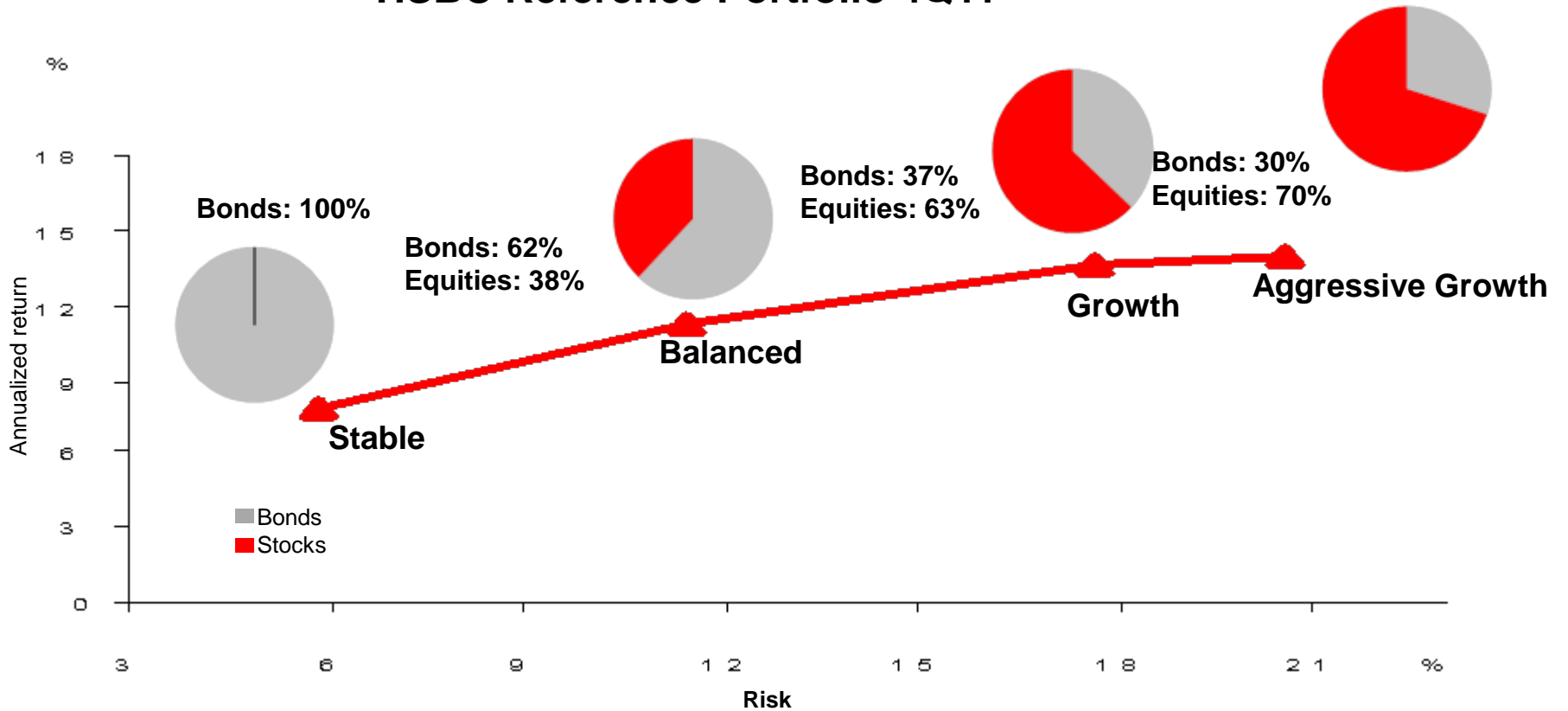
3-year rolling return distributions  
(Q4 1981 - Q4 2011)



Source: Bloomberg and HSBC. Data as of 31 Dec 2011. US stocks = S&P 500 Index, HK stocks = HSI Index, Bonds = BarCap US Treasury Index.

# Different asset mix based on your risk appetite

## HSBC Reference Portfolio 4Q11



Source: Morningstar and HSBC. The figures are not indicative of future performance. The performance of your investments will depend on the performance of the underlying assets chosen by you for your portfolio(s).

## Summary

- ▶ Moderate growth for Developed market and more robust pace for Emerging markets
- ▶ However risks to growth remain
- ▶ Issues around debt sustainability (and not just in the Euro zone) will continue to dominate the news as there is no quick fix and the process will take time and continue to fuel volatility
- ▶ Valuations for risky assets are very attractive
- ▶ Key themes/investment ideas:
  - Seek exposure to equities
  - With unappealing valuations for developed government debt markets, exposure to credit is key
  - Asia has very strong fundamentals, which provide a supportive environment for Asian bonds
- ▶ High level of volatility implies diversification remains key

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