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Tech Talk

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Speakers

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Presentation

Jose Rasco

Hi everyone. Thanks for joining us today and we have an awful lot to discuss. A lot going on with markets and the global economy, and certainly the pandemic and coming back. But before we get started, let me just do some housekeeping here. I have to read a quick disclosure.

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So, on that cheery note, thank you for joining us and we're going to do Tech Talk today. As you know, this year has a big year. 2021 is a year of recovery and growth, hopefully, and we've seen a lot of both. And so, we see that vaccines continue to mitigate the COVID risk. The COVID risk isn't gone but it's being mitigated in many places, and we see that the next waves up are very muted relative to prior waves once vaccination rates hit certain levels, and in the US, we're already seeing that play out as well.

So, what are we look for as a bank, globally? Our views are basically pro-cyclical, risk-on, and what we're seeing is that with fiscal policies being very accommodative and monetary policies being extremely accommodative as well, what do we see? We see policy rates that are low, yield curves that are low and flat, for the most part, and Central Banks that are out there helping to stimulate the economy while watching out for inflation.

So, we're looking for growth out of Asia. Asia has always been a central growth hub for the global economy, and with the reinvigoration of the Chinese economy, we see more of that coming, and as well as a lot of intraregional trade. We are very positive on China and Singapore, for example.

Now, in addition, we're seeing some growth in Europe. And in Europe, we're seeing countries like the UK with its emergence from Brexit and COVID looking a lot better. Germany and France, very pro-cyclical economies that can do well for the consumer, as well as the business sector. We see some upside in the European economy and in European markets as well, and we're actually overweight in all three of those countries in our equity allocations.

And then last but not least, the Western hemisphere, Latin America, just like India, lagging behind in terms of COVID, vaccination rates, and therefore, we're not all that enthusiastic yet in terms of those financial markets. But we do see opportunity in the credit space where there are corporate credit opportunities.

Now, in the US, clearly a story of very rapid growth, much above trend, a lot of fiscal stimulus we've seen. If everything works out like President Biden wants it to, it would be about 9.4 trillion in stimulus over the next year or so, and of course, some of that in the infrastructure side would be delayed over eight years, but 9.4 trillion in spending is about 45% of GDP and that is far in excess of the 40% that FDR spent on the new deal in the 1930s. So, these are big numbers. And so, clearly, it's going to be a growth story.

Now, the thing that is coming out of this is, what are we seeing? We're seeing that we have a base effect. Last year, inflation went down, so therefore, any normal trajectory to inflation is going to look higher, so we have this base effect in inflation for the next three, four months.

In addition, like any business cycle, we have supply and demand aren't really in sync, because usually, you'll slow down your production rates during a recession. In this one, many factories were completely shuttered for months at a time. So, as a result, we have to take into account that these factories need to get back, and inventories were depleted before went into COVID, now they're very low, at all-time low levels according to the ISM indicators. So, manufacturing inventories are extremely low. And if you remember during COVID, we had trouble getting toilet paper and tissues and paper towels. In addition to – look at the home prices we saw today, home prices were up 13, 14% depending on the indicator you look at. That is a very strong number. Why? And one factor is there's a lot of money out there. The other one is there aren't a lot of homes for sale, so we need to see building continue to improve.

So, we need to rebuild inventories, that's a big part of the growth story and we saw it play out in technology with semiconductors, and we're going to talk about that in a moment.

In addition, two other things we see that are very important is the move towards sustainability. ESG investing, sustainability, impact investing, call it what you will, there is a huge movement on the part of many, many groups to focus on the environment, on social criteria, as well as corporate governance, and we are seeing that, increasingly, these groups are very, very active. They're activist, and they are out there using their capital to not just buy goods but to buy securities as well. So, this *Activist Alpha*, I'm calling it, is something that we think is going to affect the markets, and we've seen that play out already a little bit this year, but look for more of that as we go forward.

And last but not least is the role of technology. Technology can be a very cyclical sector as it's capital intensive, so when interest rates are lower, technology can do better, and there are also secular components to it, so long-term themes. We are at the beginning of a long-term multiyear theme we believe in terms of technology investing opportunities. This is not a US story, it is a global story. 5G is just the beginning. We are building a superhighway on which we are going to transport many, many goods, and many, many services, and this is a great opportunity for you folks as investors.

Now, the markets have been battling reflation versus reopening, and technology has been left by the wayside. Technology has not performed like it did in the past couple of years and so people are concerned. Did I make a mistake? Should I buy more or should I begin to unload my technology shares? We feel – and there's no one right answer here, obviously, it depends on many, many issues – but our overarching view at HSBC Private Banking, globally, is that we like technology. It is one of our fundamental themes. We have four pillars of investing. One is growth, especially focused on Asia. The other one is investing in a low yield world. Number three is sustainability. And number four is technology, and technology, as George Gilder once said, can sometimes give the economy that kick in the butt that it needs and lift productivity and profitability. And so, we feel we're at the beginning of that with this 5G and this new very wide road that we're going to see many products and services that are going to lift productivity and profitability.

So, I am very fortunate to be joined today… so, one of my jobs as the CIO of the Private Bank here in the Americas is to make sure that we bring good content to our clients. And so, this one was easy. I had this one in-house, so I pulled it out of my hat. Brett Mitstifer, if you could join me. Brett Mitstifer is the Head of our Investment team, as well as the CIO of our Discretionary Group, and so he wears many hats, just like I do, and so Brett, you and I have worked together for, what, 10.5 years, I believe, and we're not just interested in the markets, we're also big technology fans. So, welcome, and I'll be asking you a couple of questions.

Brett Mitstifer

Thanks, Jose.

Jose Rasco

Good to have you. So, the first thing is, I think, we need to focus on is where are we going in terms of tech. Now, obviously, you can invest in technology in many ways. You can invest in concepts, you can be an angel investor, a friends and family round, you can buy into private equity, you can buy into a public company, or an IPO, or SPACs as we know today are out there. And then there's a lot of M&A opportunities. So, as an investor, there are many vehicles you can use in which you can invest.

One of the key things that we think is going to happen this year as a bank, is that given the potential for a new tax regime next year in the US, we think there's going to be a fair amount of M&A brought forward into this year, because don't forget, valuations are high in many sectors, and companies have a lot of cash. So why not do it now when you already know what the tax ramifications would be.

So, as a professional investor in the technology sector, Brett, what role do you think M&A could play in technology in terms of valuations this year?

Brett Mitstifer

Yes, thanks, Jose. M&A has always been a big part of the technology landscape. Companies sometimes can develop the technology in-house, and other times, they need to reach out into the private market or to the public market where there are more innovations and disruptors live, so that you, as a big company, can pull in the most state-of-the-art technology that's developed in private markets where you certainly don't have the same pressures to produce quarterly earnings results. You have a longer time horizon for investing your capital and developing new products and cutting-edge products. So, I think M&A has always been a part of the tech landscape, will continue to be so.

If there is a change in tax code, it could be an impetus for owners of private companies or major owners in public companies to sell, sell earlier rather than waiting just because there's a more advantageous tax code around that. There's also, the liquidity in the markets is very high right now, whether it's measured in savings rates, or M2, or the bond market liquidity that's provided by the Fed, there's massive liquidity in the markets right now. So, the ability to fund and to finance M&A activity right now is very, very strong. So, people who want to make moves will be making moves, and we've seen some activity recently, some relatively big deals and there's more in the pipeline. So, I think that's a very important part of the future and always will be.

Jose Rasco

So, not just the traditional M&A in terms of acquiring new tech, but you think this potential change in the tax regime could, in fact, exacerbate those trends in the short-term, right?

Brett Mitstifer

Absolutely. Entrepreneurs and investors always look at the landscape and say, "What decisions should I be making today based on the future potential, future tax code, future regulation?" and if entrepreneurs think that the tax code is going to change substantially and go against them, they will act and they will make adjustments and move their timeline forward.

Jose Rasco

Now, one of the questions that we've been asked, because we've had some people already send in some questions in advance, and it's a question that's on everybody's mind, let's be honest, tech stocks did really well last year as a sector. What is a tech stock? It's an interesting question. We'll get to that in a minute. So, if you look at valuations, and one of the problems we have in the market today is that certain parts of the economy are really humming along and earnings have really picked up already, and those multiples look pretty good. Other parts of the economy, we're seeing the price has taken off in anticipation of future earnings. Investors are discounting those future cash flows back.

Now, the question is, and it's a simple formula, price divided by earnings. Earnings in the tech sector, or based on the Bloomberg consensus numbers we've seen, are about to truly take off in the next two years. This year and next year, they are basically set to almost double, if you look at the sector, of just technology. So, that would, what we call, normalize earnings. So, earnings have been not that great for many parts of the tech sector for a variety of reasons, but prices have risen in advance of that, and therefore, we see multiples that are a little stretched in certain parts of the sector. And we can break it down to the hardware, software, services, as well as semiconductors.

Brett Mitstifer

I think your question is about, should we be concerned about P/E multiples and what do we think about P/E multiples in this kind of market environment, and it's an excellent question. It's normal in an economic cycle, when you're coming out of a recession, that P/E multiples will certainly look high coming out of a rebound, or out of a recession because earnings are depressed. So, P/E multiples can look high, but what normally happens is earnings catch up with prices. And we think that that's a key theme for 2021. Earnings are going to be up anywhere - 25-40% depending on the sector or the estimates. But we don't think the markets go up that much. We think the markets have a good year, but they don't go up as much as earnings. So, the earnings catch up to the prices and so you have a natural process of bringing down P/E multiples throughout the year. And as this extends out into 2022 and to 2023, you have a clear path to how P/E multiples will probably continue to come down even though stock prices do quite well.

Now, the other side of that is, what is the discount rate you're going to place on those P/E multiples, given interest rates as low as they are today. So, it's not unusual to have higher than average P/E multiples in a very, very low interest rate environment. And that's where we are as well. We're definitely in that kind of environment that P/E multiples should be high, because frankly, the earnings yield on the bond market is extremely high, so the stock market should be as well.

Jose Rasco

And if you look, Brett, and we've talked about different sectors in the economy, consumer discretionary, and there are a series of sectors that have been hammered by the COVID pandemic and recession, and clearly, you see a great illustration of that normalization of earnings. And tech, even though everybody thinks tech did great, and it did last year during COVID, certain pockets did really well, there is a normalization process of earnings as we begin to build out the economy in this new business cycle that – in agreement with what you just said – we think valuations may actually come in as you see the market and earnings go up a heck of a lot more than the market might. So, I think that answers that question, which is a good one.

We talked about a potential higher tax regime next year. One of the reasons for that potentially higher tax rate structure, both for the individual and corporate sector, is infrastructure spending. Now, as an economist by training, everybody knows, infrastructure is the free lunch. If you spend money on infrastructure and you're building homes and facilities and railroad tracks, that tends to be a good multiplier. It creates jobs, lifts productivity, improves logistics, and creates wealth. And then it creates a wealth effect in the market, which feeds back to the consumer. So, it creates a very positive feedback loop.

So, in China, Brett, we have seen that the Chinese Government has come out and said they want to basically create a virtuous cycle like we have in the US, where you have a technology sector that is creating technology and creating disruption and innovation, and on the other side of it, you have consumers who are going to go work in those technology jobs and then become the consumers of those products. So, you create this virtuous cycle, and we're lucky we already have that, to a large degree, in the US. And so, therefore, China is spending a ton of money on 5G and on developing that middle class to help create that cycle.

In the US, the Biden administration has proposed 2.3 trillion in spending and the three categories they focused on is physical infrastructure, digital infrastructure, and what they're calling social infrastructure. In other words, getting a segment of society that has been somewhat left behind in the digital age and bringing them up to speed in terms of their ability to learn and get the proper logistics in place so they can truly function in this new digital world.

So, if we could just talk about infrastructure for a second it's a major theme for the bank, globally. I actually wrote the reports for Infrastructure 2.0, the virtuous cycle of future growth. Can you talk to us about how that plays out in terms of physical, digital, and social in terms of the concepts behind portfolio construction, and how infrastructure is going to be a long-term play, just like the tech multi-year rollout that we see. How could they go hand in hand, Brett, in terms of portfolio creation?

Brett Mitstifer

So, infrastructure is very interesting and exciting. It's something that we haven't invested in fully for a long time, but we have been investing in our technology infrastructure, but we have to take it to a new level, because one of the things that we've discovered in the pandemic is there's a bit of a supply chain issue in our infrastructure, and some of our manufacturing turns out to be too far away from home, we need to bring it back home. Companies are bringing their manufacturing facilities back to the US, and opening new plants. Those new plants are going to be heavily technology-driven – automated manufacturing, state-of-the-art technology in inventory management, etc. So, there's going to be a lot of money spent to make sure that that infrastructure for all that new manufacturing facility is up to snuff. And that will be heavily about building out the 5G network, so that we can have smart warehouses, and goods and services can be transported around the country.

We're going to see a big shift in the semiconductor space. Manufacturing of semiconductors is going to be moving more and more back to the US, because that infrastructure is critical, on the digital infrastructure perspective, to have enough chips close to home so that we don't have the shortages that we're seeing now in the manufacturing sector, specifically the auto sector, where there's a shortage of chips because there's too much manufacturing too far away from home. And we need to have more of that security, infrastructure, and supply chain security closer to home.

The CapEx cycle is going to be heavily tech driven, tech jobs are the key to the future of job growth and wealth creation in the country. Yes, we need to get everybody back to work. We need to get restaurant works and everybody back to work, but the big driver of wealth and job growth in the US is going to be skilled jobs, higher-skilled jobs in the manufacturing sector that are going to be heavily tech [audio].

Jose Rasco

So, in other words, we're going to see this play out in multiple ways in the tech sector. Now, you talked about infrastructure in terms of physical, digital, and then on what the President is calling social infrastructure, I'm assuming there are a lot of opportunities there in terms of education, lifetime learning, things like that, retraining. Even closing the digital divide, which has a hardware and software component to it. Even those, I think, are included. So, some other opportunities for investors.

Brett Mitstifer

Getting broadband more broadly out across the entire country, improving – get 5G further out into the country opens up the gamut for things, like you said, education, remote education, remote work. There's lots of opportunities that we will see in reducing that divide. If you can push out the technology further into society, it creates more opportunity for everyone.

Jose Rasco

Now, one of the obvious opportunities in this digital – or this infrastructure rollout, and we've seen it play out in a meaningful way in the past month, gas prices are now national average, I think over $3 a gallon, is security. And we have a new theme where we're focused on total security, which again is very focused on physical and digital. So, can you talk to us about, again, in the construction of portfolios, in your views, Brett, we view it as a major theme for the bank globally, and not just in terms of physical security and personal security, but as records go public in healthcare, and financials, and education becomes more digital, like you said, these are very personal issues and those need to be secured. So, can you talk to us about, again, that convergence between physical and digital in the security space?

Brett Mitstifer

Yes, cybersecurity is an extremely important issue in our society, because as you say, access to someone's personal records… there have been very high-profile hacks of our personal data from retailers, a major credit rating company was hacked and personal data got out there. So, from a personal perspective, cybersecurity is critical that people can't get access to our data and our personal information as we move more and more online.

And cybersecurity, you don't have to go past the Colonial Pipeline mess to realize how much of a tech related economy we are, and how important cybersecurity is. If ransomware can shut down the gasoline supply to the entire East Coast, what would happen if that happened with the electric grid. We don't have storage facilities for electricity like we have storage facilities for gasoline. That is critical to our society and the smooth running of our economy is that we protect and guard our systems from cyberattacks.

It's not new, but the most recent case shows how truly vulnerable we are and that we have to spend a lot of time and effort to secure our economy, both physically and digitally in the future. And supply chain security is the same kind of thing. Manufacturing facilities have to have cybersecurity. Everybody has to have a cybersecurity veil to protect themselves from either ransomware, or intellectual property theft, or personal information theft. It is very important.

Jose Rasco

For example, one interesting part of this whole total security package, believe it or not, is food security. So, one of the things we saw play out during COVID, during the pandemic and the lockdowns, not just in the US, across the globe, was food insecurity became a major issue in many countries. And not just in poor countries, in many developed countries as well, and not just in urban areas, but even in some rural areas. In the US, we have food deserts where in major cities, people had to travel 30 minutes across town just to get to a supermarket. So, the concept of food security has become a major issue, and I know, I believe it's China and Australia actually have it as part of their defense budget, Brett. Because if you think of the concept of the food production function, right, it used to be you had a farmer in the field with a pitchfork trying to get the hay onto the wagon, today, you're using robotics and drones and iPads and chemicals to secure the crops, or if you have organic food, you have other issues you have to worry about. But the automation of the American farm, or the global farm has created vulnerabilities in terms of security and the ability to get these products to market.

Everything from the right software to refrigeration trucks that can get it to market. Is that something you're looking at as well, Brett?

Brett Mitstifer

Yes, automated farming is a huge issue. But again, if we can't get the product to market in the right places in the country, that's a big problem. We're flying drones on Mars, but we can't figure out how to stop food waste in our world, so there is a lot of work to be done there, but technology is going to help that. Without technological advance, we wouldn't be growing as many crops as we are right now, and as cheaply as we can. So, we don't have a food cost problem, we have a distribution problem and we need to make sure that that works better.

Jose Rasco

Absolutely. I remember reading a book, God, long ago, called *Snow Crash,* by a guy named Neal Stephenson, and in it, he defined an American economy that was run by the mob and all we did was deliver pizzas to one another by bicycle. He was clearly wrong, because now we're going to be doing it using autonomous vehicles. And speaking of autonomous vehicles, we see pizza delivery by autonomous vehicle and all these drones that are being used by some of the logistics companies that are out there. clearly, that's another great example of how you need to integrate the physical and the digital, because you can't have an autonomous car if you don't have the lines on the road paved and painted, right.

Brett Mitstifer

And you have to have the 5G network, and you have to have the semiconductor chips, and you have to have all that hardware to run it. You can't autonomous vehicles in a serious way without 5G, because the speed and the amount of data that needs to be analyzed quickly is critical. I think we're almost there on the software and on the semiconductors and the processing chips, but the 5G network is going to be the next big thing to really go to autonomous vehicles.

Now, we're going to move to electric vehicles, the EV market is going to explode, but the next, next phase of that should be the autonomous side of the equation.

Jose Rasco

Now, you raised an interesting point in terms of autonomous vehicles. Long ago, in the 90s, I actually wrote a report called the ABCs of Digital Media. It was access, broadband, content, and services. And so, if you look at today, it's hardware, software, and digital services is essentially the corollary in today's market, and one of the things we're seeing is that, like you talked about security, there's a component in each one. Hardware, software, and services. Now, interestingly enough, think back to the 90s revolution in tech, in the 80s, we were just introducing personal computers, and they were all green screens, remember that, and very, very simplistic stuff. Pong was a very advanced game for the time. So, today, as you mentioned, we are very far advanced, and technology has managed to – using the process of creative destruction – technology has managed to diffuse throughout the economy.

And one client asked, which I think is an excellent question and leads us right into the next part of what we want to talk about. in the past, we talked about technology as a certain group of companies have made either hardware or software, that was it. Today, we really have to look at not just investing directly in technology companies, but indirectly, by sector, in the companies that are best putting to use the hardware, the software, and the emerging services that are converging together to create that profitability and productivity. So, can you talk to us about that and the concept of convergence and diffusion and how tech companies are really being redefined. Today, a healthcare company is just as much of a tech company as some semiconductor companies, in many ways.

Brett Mitstifer

Yes, we look at the digital world much more broadly than just technology companies *per se*. FinTech is revolutionizing how we transact our financial lives, how we invest, how we save, how we borrow, how we lend. It's changing dramatically what currencies look like. And the healthcare world is also in the middle of the transformation.

The future of life sciences is about computational data as much as it is about biology or chemistry. It's about analyzing the human genome, people's genetics, crunching numbers, big data, artificial intelligence, to customize solutions to individuals for their treatments, and that's the future of life sciences and the industry. And the pharmaceutical industry is living and dying off of data that they can collect and analyze on how things work, on how medical breakthroughs work and how humans interact with those medical issues.

So, technology is not just about tech stocks, it's about healthcare, it's about FinTech, it's about consumer behavior, it's about a lot of things, and it's going to permeate our entire … it's about pipelines, right, amazingly. Technology is reaching out to the real estate, how real estate is managed and functions as well is a lot about technology.

Jose Rasco

So, as we go forward, smart cities, smart grids, all these smart products we have, and the Internet of Things, all these things require the hardware, the software, and the value-added services as we go forward.

Now, if you look… another very well-known fan of technology investing, Cathie Wood at Ark talked about the five sectors that she likes going forward. DNA sequencing, robotics, energy storage, AI, and Blockchain. Now, Brett, if you had to list five things that you're focused on in tech development today, this diffusion concept, what would be those five? If you had to pick five sectors. Because I know you – and I'm sort of cheating here because I read your report this morning that you posted on LinkedIn, and for those of you who haven't seen it, Brett wrote on his views on tech investing, and he did list five sectors. So, can you talk to us about those and where those advancements will take us?

Brett Mitstifer

Yes, so we are talking about FinTech, healthcare tech, digital services, digital infrastructure, and digital consumer. Those are kind of broad categories. They're not industries, they're not sectors, they're just broad categories that capture a lot of things that are going on and how digital services will be adapted. A lot of the digital infrastructure is what we talked about in terms of 5G and semiconductors and things like that, but digital services is what you alluded to earlier about education, about gaming in the place. E-commerce is in digital consumer, it is changing rapidly in terms of how we order food and how we have food delivered and how we book our vacations, and how we work from home, lots of things there.

And the FinTech side is exploding in terms of new ways to manage our personal financial health in terms of insurance and mortgages, lending, and deposits, and investments. And then lastly, as I mentioned, healthcare is just exploding in terms of not only the data side, but digital solutions to help us on our day-to-day health issues, whether they be sleep apnea related issues, or blood pressure, and diabetes, all of these things are unfolding as a revolution in how we deal with our healthcare issues.

So, there's been some high-profile companies about telehealth, which is great, but it’s going to go much further than that in terms of our day-to-day lives.

Jose Rasco

Now, Brett, one of the issues that we've been asked a lot about has been digital currencies, and I don’t want to focus on the world of unregulated currencies, which we don’t really want to touch on due to the volatility, but if you look at the concept, there are proposals being floated in Governments all over the planet to create digital currencies or virtual currencies at a national – some of them even at a state and city level. What role do you think… and you can talk about that if you want. And another question we had was on Blockchain. Blockchain, obviously, is not going to take over the world of Visa one to one transactions at the counter, in terms of getting medical supplies or something, but Blockchain is going to take on a major role in terms of contracts and other things. Could you talk to us about where there are opportunities in the Blockchain space?

Brett Mitstifer

Blockchain is all about a distributed ledger of keeping track of transactions or information or assets or anything that you want to talk about. The next time you buy… at some point in the future when you buy a house, you won't have to register your deed in the county, it will be held in Blockchain and it will be very secure. So, the key issue to Blockchain is security of those records and control of those records so that they can't be stolen, or lost and there's a very strong record – centralized record for all of these types of transactions. And secure, the key issue is keeping everything secure. So, Blockchain is going to roll out in a lot of ways, regardless of the current trends today in currencies and crypto currencies. I think Blockchain is a major thing for us.

The other question – I don’t want to get into the whole crypto currency thing at all.

Jose Rasco

It’s not something we recommend at this point, that we talk about, so no point in dealing with it.

Brett Mitstifer

But electronic transactions are key. The security… anything that we can create to make electronic transactions over the internet between whether it’s B2C, B2B, C2B, however we’re transacting over the internet between ourselves and businesses and making that more secure in an electronic transaction is very important and is critical.

Jose Rasco

And so, one of the other things, you talked about consumer, or e-commerce for the consumer sector in particular, and some of the… as we make this more of a pervasive technology. And if you looked during COVID, what I call the COVID Compression, we had 10 years of change that got rolled into about 10 weeks of opportunity, where we were forced to make some major changes and everybody had to buy bikes for the house and do all kinds of things you didn’t plan on doing last year. One of the things was becoming more of an electronic consumer. At HSBC, our technology research team in London has estimated that, in the US, they feel that ecommerce could reach 50% of retail consumption in the next 15 years. That’s a big number. Part of that will be now, again, the rollout of 5G, continuous consumption, merchants sent… if you and I were going to the mall together in the same car, Brett, you're going to get different ads than I'm going to get, and so that’s one thing.

The other thing is the use of VR and AR (virtual reality versus augmented reality). I don’t know if you want to talk about that, but I know there are opportunities there as well and that consumer space is absolutely monstrous, especially as we see some of these social issues get dealt with, like the wage gap between men and women, you will see, as wages go up for women in the next couple of years to try to close that gap, I think you'll see more opportunities in the e-commerce space. It will be more diversified than people thought, right.

Brett Mitstifer

Absolutely. I know some people think that when the pandemic is going to end, people are going to just go back to the way they were before and all of these trends about e-commerce are going to go by the wayside. But frankly, I don’t think that’s the case. Certainly, there's a bit of a rush to the door at the moment of people rushing out to restaurants and rushing out to do things, and rushing out to go to concerts and do things, and that’s very normal human behavior after being locked down for a year, that people are going to do that.

But on the other side of that, people will then, after that initial surge – we've talked about it, there's a big surge in the economy right now – after that initial surge, people will step back and get back to the normalization of their lives, and there's a lot of things that we did during the pandemic that people will continue to want to do into the future, and that businesses are, in essence, going to force people to do in the future.

You're going to go to… there's no such thing as a ticket for a sporting event, a paper ticket for a sporting event anymore, it will all be electronic. You'll be in a marina, and you'll order your food electronically, there's no reason to go to the concession stand. The things that we developed, people will want to do, because it makes our lives better, more convenient, and people will get back to that.

But right now, yes, there's a bit of a desire to get out into the world and that’s very normal. But the landscape has changed permanently.

Jose Rasco

If you have any questions, raise them in the chat please and we’ll try to answer them like we've been doing, but please try to get them in now, because we’re going to end in the next few minutes.

So, Brett, from our perspective globally at HSBC, we look at the tech sector and we say, we really like it, we like it short-term, we like it long-term. However, we have a couple of problems. Number one is the reopening of the economy, where some sectors that have been depressed are going to have to bounce back, and that bounce back is going to result in money, investors pouring into those sectors because of the increase in earnings that should be rather large in sectors like cruises, hotels, restaurants etc. Now, that doesn't mean we don't like tech, it just means that for the time being, there's a temporary surge to these other sectors as they get rebuilt…

[Technical difficulty]

Brett Mitstifer

It looks like we lost Jose again temporarily. I think the point of his question was going to be how do we deal with this cyclical rebound. Look, I fully agree with the idea of this cyclical recovery, because there is going to be a big cyclical recovery in earnings, cyclical sectors are going to see a rebound, sectors that haven't done well during the pandemic are going to see a big rebound. And so, right now, investor focus has shifted over to that part of the investment world.

But technology is also a bit cyclical. The CapEx cycle is cyclical and we're going to be undergoing a big CapEx resurgence here, so that's going to be helping to drive the technology investment. But also, at the same time that we've seen this cyclical resurgence, we've also had this escalation of inflation fears, and that's weighed heavily on higher P/E stocks.

So, high P/E stocks don't like higher inflation, they don't like rampant inflation, they don't like rampantly rising interest rates. And so, we've had this bit of an inflation scar that may not be over yet, but seems to be diminishing a little bit in the last few weeks. If you look at breakeven spreads on TIPs, they got to very extreme levels, they backed down a little bit. The Treasury yields have backed down a little bit. And low and behold, at the same time, you see that inflation fear pull back a little bit. You see the market go back toward technology names and growth names and things like that.

So, it's not necessarily over. As Jose mentioned, we're going to see some inflationary numbers as we reopen, as demand is outstripping supply at the moment. But in general, if that's a transitory trend, and we get back to some normalization, ultimately, those inflation fears should subside somewhat.

Jose Rasco

Thanks, Brett. And then the only thing I wanted to ask you, I guess, was if you were stuck in an elevator with everybody on this call, the normalization of earnings, that's a factor, and I think as we see earnings, especially in tech, are set to really do very well, I think we see multiples look a lot more normalized and we could see a real rise in the tech sector going forward, that's the cyclical side. On the secular side, this 5G rollout is going to be a multiyear phaseout, and then you have to diffuse it through the economy, and then you get that convergence of new products and services. And that's really where the rubber meets the road for you, as a manager of portfolios, and the manager of an asset allocation team.

So, if you could just give us a long-term perspective on that diffusion and that creative destruction going on in the economy and how that plays out over the next few years.

Brett Mitstifer

I think in a portfolio you need to have both exposure to current trends and what's happening over the next three to six months, 12 months. And you also have to have exposure in your portfolios of what's going to happen over the next three to five years. And I think that's key.

So, the key to us is, yes, get some cyclical exposure in your portfolio, because we are in a rebound, we're having a recovery, but remember these secular trends of three to five years. The US economy is transforming itself into more of a tech economy. It's going to be driving growth, job creation, wealth, employment, and I think that's the key issue is you need to have that exposure in your portfolio.

So, that's the way we're approaching portfolio construction right now, is have a bit of a barbell, what's going on today and what the secular trends are as well. And your portfolio that you have today, you can shift. In six months, you can shift it a little more. If trends change, you can shift it. But remember, there's some secular growth opportunities out there that you need to invest in for the long-term, and be willing to sacrifice short-term performance for long-term secular trends, that’s critical.

Jose Rasco

And, in fact, a lot of people are saying this is the opportunity to lock in those long-term opportunities, as they have not necessarily performed as well as we thought.

Now, one final question, Brett, before we let you go, and we will let you guys go after this. We had a question from the audience. Let me just read this right. “Will virtual tokens be a more prolific form of digital data security? How does that impact cybersecurity?” What are your thoughts there?

Brett Mitstifer

I think there's a lot of things that are going to be developed over the years to enhance digital data security. It’s such a critical issue that there's lots of opportunities to create new technologies to make us more secure. So, I think that three years from now it’s going to look vastly different than it is today, and so, you have to be on top of what the current trends are.

Virtual tokens, yes, absolutely. All the types of data security that we can come up with we’re going to need to come up with, because there will always be bad actors in the world that are trying to do something, and we have to keep our economy, we have to keep our personal lives safe from that intrusion. So, I think all of that makes a lot of sense.

Jose Rasco

I think that’s a great way to end, because this is an issue for individuals, businesses, and Governments, where they have to securitize physical and digital infrastructure. And the whole point… I learned long ago from a guy who was a legend in the business who said, “You invest in long-term themes and you trade that volatility around that theme”, and that’s really what you just said, if you think about it.

And so, I think this is a perfect illustration of that. Security is a major theme within the cyber, within the whole concept of digital transformation of this economy. And right now, whether it’s tokens, whatever it’s going to be, there are themes that you can trade, in the short-term, that may or may not be in a long-term solution. So, important to keep that conversation going.

For the clients who called in, we want to thank you for your time and we want to remind you that we’re here and we have very, very deep thoughts around these issues, especially when it comes to tech. Keep an eye on the cyclical versus the secular, and keep your mind focused on the fact that these earnings need to be normalized. And as the economy goes back to something more normal than we had during the COVID year, you will see those earnings normalize, and I think you'll see multiples look a little more reasonable. And the growth in tech over the coming two years, in particular, should be rather expansive.

So, we’re optimistic about the future here, and we would recommend that you talk to your relationship managers, your investment counsellors, keep that conversation going, and Brett and I are always available to talk. We do monthly updates with many clients and would love to do so with you if you are so inclined.

So, thank you again for your time, and look forward to speaking with you all soon. Thanks, Brett. Thank you very much.

Brett Mitstifer

Thank you, Jose. Thank you everyone.