

HSBC Think Wealth CIO Exchange

Willem Sels, Global Chief Investment Officer, HSBC Private Bank and Premier Wealth and **Wei Li**, Global Chief Investment Strategist, Blackrock

Willem Sels

Thank you, Wei, for sitting down with me for this CIO Exchange. And the first topic we want to address, of course, is AI, where the markets have been flip-flopping between enthusiasm for the winners, but also worries about how AI will affect the incumbents in software, but also in different sectors.

Now our view is that AI boosts earnings potential, so that's a good thing overall. But of course there will be winners and losers and where that's most difficult for clients, they can go across the ecosystem, such as semiconductors, data centres and electricity as well.

How do you address these winners versus those losers and sort of that opportunity versus the challenges from AI?

Wei Li

Well, thanks Willem for having me, and I would observe that earlier in the year, markets were nervous about the unprecedented CapEx spending pace of these hyperscalers. But now you see revenues starting to ramp in an unprecedented way as well.

Earnings are very strong for the hyperscalers, and the revenue ramp for model builders such as Anthropic is unprecedented. And because of that markets are feeling a bit better. And we continue to be overweight the AI ecosystem and the AI theme.

But the big risk, I would say, is that the big spenders not ending up as the ultimate winners. We think that they will, you know, like we look at the model builders and you look at the data centre providers, we believe in them strongly.

But there is a risk, that as we think about potentially compute becoming a commodity, could the owners of IP, patents and data become the winner? So the big question of how the revenue will be divided is still unclear; the jury is still out.

Willem Sels

The other question that clients ask us is the impact on the global economy and in particular on inflation and rates. So on the one hand AI should boost productivity – there are some signs of that, and that should cap inflation. At the same time, all of this investment is going to boost growth, so no need for interest rate cuts.

We end up with a Fed view of no rate changes over the next two years. Where do you stand on this?

Wei Li

We also don't think that the Fed is going to do much. I think markets are right to price out earlier cuts at the beginning of the year. Before AI becomes disinflationary, the demand for raw materials for build-out means that it will be inflationary first, before it becomes disinflationary.

And what's happening in the Middle East, and the broader supply chain disruption further adds to inflationary pressures. I think markets are right to keep the Fed kind of where it is for the next two years.

And some other central banks, like the ECB, Bank of England, and Bank of Japan actually hiking a little bit in the coming quarters.

Willem Sels

What that means for bonds of course is no gains, in terms of bond price appreciation. And so we need to think about how you diversify portfolios.

Bonds have also not worked very well during the conflict, because of those inflation pressures. So you know, we still clip coupons in bonds. And think that's important, but we also diversify through hedge funds, through infrastructure, which also gives that income.

How do you construct portfolios with that rate outlook?

Wei Li

I think this is a golden age for income from bonds. Five years ago, to earn 4–5% investors had to take significantly more risk.

So, we think, bonds are providing meaningful income and relative to losing diversification benefit it is giving portfolio income, which is a good thing. Having said that, portfolio diversification needs to be revisited as well.

Depending on the driver of market volatility, there is no diversifier "one-size-fits-all" solution. It has become a lot more tactical. Traditional diversification hasn't worked in recent episodes.

So, for us, we have an investment theme called "Diversification Mirage". Instead of trying to diversify from core conviction, actually just think about what convictions you want to have in portfolios.

One cannot get away with not having a conviction in the age of AI one way or another. So instead of accidentally having those convictions, own those convictions, because investment decisions made in the name of diversification may end up being big active bets, so own them.

Willem Sels

So diversification is obviously important, but don't do bad investments simply for the sake of diversification. That brings me to the dominance of US assets in portfolios, and especially because of AI, because of that big tech sector in the US, US assets and US dollar tend to dominate portfolios.

We look for diversification in Asia, where we see opportunities in tech at cheaper levels. Also, diversification within Asia, all different countries have different cycles and drivers. And then on top of that we have hedge funds, we have private assets.

How do you deal with that dominance of US assets and the US dollar in portfolios?

Wei Li

I think concentration is a feature of our environment, not necessarily a bug. We're overweight US equities, but we're also overweight emerging market equities.

But if you look at the depth of capital market, energy advantage, you look at the advantage in frontier models, they all point to the US still keeping and maybe even extending its lead. So we are very positive about the US outlook.

But to your point around global opportunities, this is where the emerging markets overweight comes in. We also see opportunities in selective private credit, infrastructure, equity, we like industrial cyclicals over consumer cyclicals.

So there are granular opportunities that we would definitely add to portfolios, but we also believe in a TPA approach. Total Portfolio Approach - look through asset-class labels and focus on the fundamental macro drivers of portfolios.

Willem Sels

So looking for those convictions that you have and then looking across sectors, across geographies as well. Thank you so much for sharing your insights and having that optimistic tone as well.

Wei Li

Thanks for having me.