HSBC

Investment Monthly

Moving cash to bonds ahead of Fed rate cuts

September 2025

Key takeaways

- Weaker-than-expected US payroll numbers, an elevated real policy rate and Fed Chair Powell's comments at Jackson Hole reinforce market expectations for rate cuts to resume in September. Investors are likely to move cash to bonds to lock in higher yields. The falling correlation between stocks and bonds also means that quality bonds are better diversifiers against equity market volatility. We upgrade Global and US investment grade to overweight.
- In the US, the headwinds of growth moderation, tariff-driven goods inflation and elevated valuations should be offset by Fed rate cuts and AI-led innovation, with tax cuts and deregulation providing further support for equities. We remain overweight on global equities, with a preference for the US and Asia, and maintain diversification through multi-asset strategies.
- In addition to the high US tariffs of 50%, India is also facing short-term cyclical headwinds, leading to slowing earnings momentum and continued foreign investment outflows. We therefore downgrade Indian equities to neutral and prefer China and Singapore in Asia. Government support for AI adoption and domestic consumption, along with a renewed focus on addressing the overcapacity issue, is boosting market optimism for Chinese equities. Defensive qualities and an attractive dividend yield bode well for Singapore's equity market.

Willem Sels

Global Chief Investment Officer, HSBC Private Bank and Premier Wealth

Lucia Ku

Global Head of Wealth Insights, HSBC International Wealth and Premier Banking

Asset class	6-month view	Comment
Global equities	▲	The combination of Fed rate cuts, resilient earnings growth and accelerating AI adoption supports our mildly risk-on strategy, diversifying across regions and sectors, with a preference for the US and Asia.
Government bonds	▶	While fiscal deficits are a concern, benign inflation should lead to more rate cuts. We prefer a 7-10-year duration for DM sovereign bonds (except for Japan) and favour UK gilts over US Treasuries.
Investment grade (IG) corporate bonds	▲↑	Easing inflation pressure and lower interest rates should benefit quality bonds, which offer an attractive hedge against equity market volatility. We upgrade Global IG credit to overweight for its attractive value in anticipation of rate cuts.
High yield (HY) corporate bonds	▶	Spreads are tight as risk appetite is high while equity volatility is low. We hold a shorter duration bias of 3 to 5 years.
Gold	▲	Although the uptrend may ease, gold remains a key diversifier against tariff-related policy concerns, USD depreciation and geopolitical uncertainty.

▲ "Overweight" implies a positive tilt towards the asset class, within the context of a well-diversified, typically multi-asset portfolio.
▼ "Underweight" implies a negative tilt towards the asset class, within the context of a well-diversified, typically multi-asset portfolio.
▶ "Neutral" implies neither a particularly negative nor a positive tilt towards the asset class, within the context of a well-diversified, typically multi-asset portfolio.
Icons: ↑ View on this asset class has been upgraded; ↓ View on this asset class has been downgraded.

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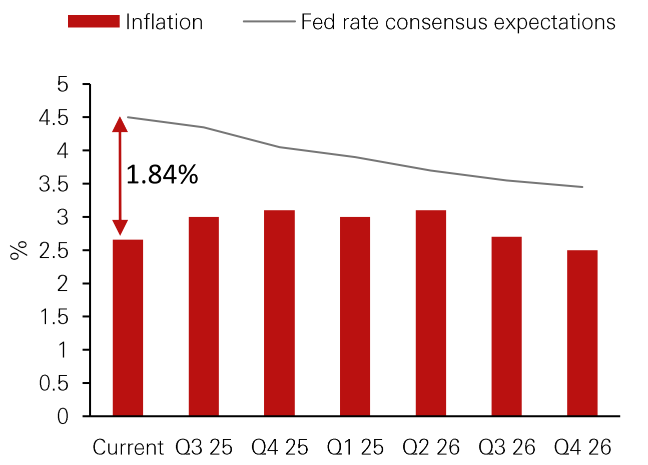
Talking points

Each month, we discuss 3 key issues facing investors

1. How should investors position their portfolios for Fed rate cuts?

- Following the release of July's weaker-than-expected payroll numbers, and Fed Chair Powell's comments at Jackson Hole that the economic situation 'may warrant' policy changes, the market now expects the Fed to shift its focus from tackling inflation to growth moderation.
- In fact, the real policy rate is quite elevated, and is much higher than in other Western markets, offering scope for the Fed to cut rates. We have been forecasting the restart of rate cuts in September, followed by further cuts in December and next March.
- This means that investors will likely move cash to bonds to lock in higher yields for now. Adding to it is the falling correlation between equities and bonds. They moved in the same direction when inflation fight was prioritised, but it is no longer the case. This has improved the diversification power of bonds, making quality bonds a good hedge against equity market volatility. As the balance sheets of many US corporates remain strong and IG bond yields are attractive, we upgrade Global and US investment grade credit to overweight, aligning it with those in EUR and GBP, as well as UK gilts. Our preference for a 7-10-year duration lies in its best risk-adjusted value along the curve.

Chart 1: US policy rates are well above inflation. The elevated real yield gives the Fed ample scope to cut

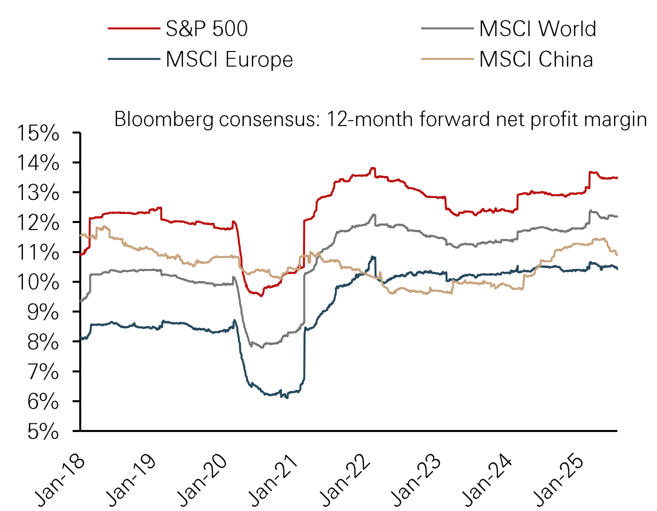


Source: Bloomberg, HSBC Private Bank and Premier Wealth as at 26 August 2025. Note: Red bars denote the market's inflation expectations.

2. Are equities losing momentum?

- Supported by multiple positive drivers, we maintain our mildly risk-on stance towards global equities, with the biggest overweight position in the US, where Q2 earnings growth surprised on the upside, led by IT and Communications.
- We believe the headwinds of growth moderation, trade tariffs leading to some goods price inflation and elevated valuations should be offset by Fed rate cuts, AI-led innovation and long-term structural trends (e.g. re-industrialisation), while tax cuts and deregulation from the One Big Beautiful Bill Act are additional drivers for equities.
- While we remain overweight on Technology in the US, which represents a significant weight in equity indices, as well as on Communications, Financials and Industrials, we downgrade Consumer Discretionary to underweight. It is because consumer stocks are negatively affected by the weakening labour market and rising goods prices. Outside the US, Asia remains attractive for its robust fundamentals and diverse opportunities, particularly in Consumer Discretionary, Communications, Financials and Healthcare. We remain neutral in the Eurozone and the UK, but see opportunities in Industrials, Financials and Utilities. We continue to adopt multi-asset strategies to balance growth opportunities and market uncertainty.

Chart 2: US companies are expected to remain the most profitable



Source: Bloomberg, HSBC Private Bank and Premier Wealth as at 5 August 2025. Forecasts are subject to change.

3. Will India's short-term headwinds drag on Asia?

- The US tariffs of 50% on Indian goods, which are among the highest in Asia, are likely to impact the country's economic growth and affect market sentiment negatively.
- More importantly, India is facing some cyclical headwinds and a lack of confidence from foreign investors, leading to continued investment outflows. Earnings momentum is expected to slow down significantly in 2025. The government is stepping up support for exporters, such as lower interest loans, and is committed to undertaking economic reforms. While we remain optimistic on India's longer-term fundamentals, we think it is prudent to move Indian equities to a neutral position for now.
- Within the region, the economic outlook for China remains positive thanks to government support for AI adoption and domestic consumption. The renewed focus on addressing the overcapacity issue is welcomed by the market. Additionally, we favour Singapore for its defensive qualities and attractive dividend yield. Overall, we think the growth story of Asia remains intact.

Chart 3: India's earnings growth expectations have been on a downward trend

Source: Bloomberg, HSBC Private Bank and Premier Wealth as at 28 August 2025. Forecasts are subject to change.

Asset Class Views

Our latest house view on various asset classes

Asset class	6-month view	Comment
Global equities		
Global	▲	The combination of Fed rate cuts, resilient earnings growth and accelerating AI adoption supports our mildly risk-on strategy, diversifying across regions and sectors, with a preference for the US and Asia.
United States	▲	Despite growth and policy uncertainties, we think Fed rate cuts and continued AI-led innovation, along with tax cuts and deregulation provide further support for US equities, particularly in the IT, communications, financials and industrials sectors.
United Kingdom	▶	Fiscal constraints and elevated government bond yields continue to pose challenges to UK equities.
Europe ex-UK	▶	While business optimism is picking up, private consumption remains weak and exporters face headwinds.
Japan	▶	We maintain our neutral position on the back of the continued reflation trend and rising expectations for fiscal stimulus to boost domestic consumption. Technology leaders and consumption related stocks are preferred.
Emerging Market (EM)	▶	Fed rate cuts should allow central banks in emerging markets to follow, while an improved outlook for trade deals and stronger fundamentals reinforce our preference for EM Asia.
EM EMEA	▼	Although the UAE offers structural opportunities, the region remains challenged by lower oil prices, geopolitical concerns and global trade uncertainty.
EM LatAm	▶	The outlook for Mexico is better than Brazil, where exports are challenged by trade tariffs and rate hikes remain a headwind.
Asia ex Japan equities		
Asia ex-Japan	▲	We focus on domestic resilience and structural growth opportunities in Asia, favouring China and Singapore, and believe the AI innovation theme should continue to be a key driver. Shareholder returns also look attractive.
China	▲	Solid earnings growth, reasonable valuations and more policy support for AI innovation and domestic demand bode well for Chinese equities. We prefer technology and internet leaders, domestic consumption plays, and high-dividend SOE stocks.
India	▶↓	While long-term fundamentals remain supportive, slowing earnings momentum and continued investment outflows lead to our downgrade to neutral. The high US tariffs on Indian goods also weigh on sentiment.
Hong Kong	▶	We remain neutral on Hong Kong equities as we look for a sustainable improvement in the fundamental outlook for the economy and corporate earnings. We prefer banks, insurance, telecom, utilities and quality developers.
Singapore	▲	The equity outperformance is supported by the market's strong fundamentals, attractive dividend yield and defensive appeal.
South Korea	▶	The tailwinds of undemanding valuations and expectations for an acceleration of the Corporate Value-Up Programme may already be priced in. Policy execution risks remain.
Taiwan	▶	The high-tech exposure to the US remains a key challenge, with the impact on semiconductor manufacturing subject to further clarity on chip tariffs. Political uncertainty adds to the downside risk.
Government bonds		
Developed markets (DM)	▶	While fiscal deficits are a concern, benign inflation should lead to more rate cuts. We prefer a 7-10-year duration for DM sovereign bonds (except for Japan) and favour UK gilts over US Treasuries.
United States	▶	The slowing US labour market and the Fed's focus on growth suggest that policy easing will start soon. We see more attractive value on the long end of the yield curve and maintain our 7-10-year duration preference.
United Kingdom	▲	The recent UK inflation pick-up is believed to be temporary while the ongoing easing labour market conditions should allow the Bank of England to deliver policy rate cuts towards 3%, supporting our preference for the attractively valued gilts.
Eurozone	▶	As we expect the ECB to keep rates on hold, relative interest rate differentials will start tightening. A further substantial rally from the current levels is limited.
Japan	▼	Political uncertainty and fiscal concerns about policy turning more expansionary will likely keep JPY rates volatile and the term premium in long-end JGBs elevated. We expect the Bank of Japan to initiate a rate hike in Q4.
EM (Local currency)	▶	Falling inflation and a weaker USD offer room for EM rate cuts. Tariff decisions may weigh on corporate margins.
EM (Hard currency)	▶	We still find yields but remain selective and generally focus on quality bonds.
Corporate bonds		
Global investment grade (IG)	▲↑	Easing inflation pressure and lower interest rates should benefit quality bonds, which offer an attractive hedge against equity market volatility. We upgrade Global IG credit to overweight for its attractive value in anticipation of rate cuts.
USD investment grade	▲↑	Solid Q2 earnings growth is supportive of the credit markets, where investment grade issuers are still enjoying healthy balance sheets to withstand potential shocks. A September rate cut should amplify capital inflows from cash into bonds.
EUR investment grade	▲	Despite stretched valuations, credit spreads remain tight. We think EUR investment grade bonds can better compensate for duration risk and still offer attractive yields.
GBP investment grade	▲	GBP bonds are under-owned by international investors but offer attractive yields similar to the USD market. We think there is a good risk-adjusted return trade-off, given our outlook for more policy rate cuts.
Asian investment grade	▶	The Asian credit market should benefit from global diversification flows and strong local demand for resilient income. We favour Japanese and Australian IG bonds, Asian financials, as well as Chinese hard currency and Indian local currency bonds.
Global high yield (HY)	▶	Spreads are tight as risk appetite is high while equity volatility is low. We hold a shorter duration bias of 3 to 5 years.
USD high yield	▶	USD high yield provides a substantial overall yield, but equity volatility often feeds through into higher HY bond volatility.
EUR high yield	▶	In line with our global high yield positioning, we remain selective on EUR high yield bonds and stick to a 3-5-year duration.
GBP high yield	▶	We hold a neutral view and a short-duration exposure on GBP high yield, as spreads are below their long-term average.
Asian high yield	▶	As China's government prioritises boosting consumption and tech innovation, we remain cautious about the property market.
Commodities		
Gold	▲	Although the uptrend may ease, gold remains a key diversifier against tariff-related policy concerns, USD depreciation and geopolitical uncertainty.
Oil	▶	We expect oil prices to remain range-bound due to excess supply.

Sector Views

Global and regional sector views based on a 6-month horizon

Sector	Global	US	Europe	Asia	Comment
Consumer Discretionary	▼↓	▼↓	▼	▲	We downgrade Global and US Consumer Discretionary, due to their full valuations and concerns regarding US consumer spending trends and slowing demand. A weakening pricing environment, after years of aggressive price rises in the luxury and auto businesses, may limit margin and revenue growth potential. Consumer demand in H2 is likely to remain muted and highly selective.
Financials	▲	▲	▲	▲	Global Financials reported stronger-than-expected results for Q2. Net interest income is likely to remain elevated as inflation remains stubbornly higher than expected, keeping interest rates elevated. Trading activity and bond issuance are likely to remain strong in the near term. In Asia, we remain positive on China's economy and the improving sentiment in the region.
Industrials	▲	▲	▲	▶	We are positive on the sector given several major favourable development trends, including electrification, reshoring, supply chain security, digital infrastructure, aerospace, and rising defence spending. However, uncertainty regarding tariffs poses a headwind to investment. Order books remain relatively healthy.
Information Technology	▲	▲	▶	▶	AI demand remains resilient, with new AI-enabled products and services being launched across various industries and sectors. First-quarter results beat expectations, providing a reassuring outlook for software and hardware growth. The roll-out of AI-enabled products and services is gaining momentum, along with embedded AI-enhanced processes. Together, these should fuel additional demand for software, hardware and IT services.
Communications Services	▲	▲	▶	▲	In the US, we remain positive on the media and entertainment segments, which are forecast to have above-average sales and earnings growth for 2025. In Europe, the outlook for the telecom services is plagued by strong competition, low investment returns and a lack of pan-European scale. In Asia, the sector is more balanced with attractive valuations and easing regulation.
Materials	▶↑	▶↑	▶↑	▶↑	We upgrade the sector based on the expectations that fundamentals and commodity prices have bottomed out, and macroeconomic indicators are slowly improving for China and Europe. In addition, oil prices may decline over the next 12-18 months, providing benefits for the chemicals industry. Valuations remain undemanding. Tariffs are a source of risk.
Real Estate	▶	▶	▶	▶	The sector appears to have stabilised except in China, where some uncertainty remains. Retail space and older offices are particularly challenged as alternative consumer purchasing channels evolve and refurbishments costs are high. New office developments and housing are experiencing better supply-demand dynamics. The re-routing of supply chains is driving demand for new facilities in developed and emerging markets.
Consumer Staples	▶	▶	▶	▶	Strong competition and consumers trading down have created a weak pricing environment for companies in many markets. Limited potential for sales growth and margin expansion, combined with high valuations relative to other sectors (in line with history), makes the sector unattractive. Consumers are trading down and seeking lower-cost alternatives when purchasing goods.
Energy	▶	▶	▶	▶	Elevated geopolitical tensions have pushed energy prices higher but rising supply and weakening demand are expected to lead to lower oil prices in the next 12 months, although the relatively higher cost of production for shale gas may limit production. Seasonal demand in the northern hemisphere is likely to support gas prices. Low valuations, strong cash flow and high dividends somewhat offset the sector's speculative nature.
Healthcare	▶	▶	▶	▲	Asian Healthcare should benefit from improving demand dynamics, attractive valuations that are below their five-year average, and rising investor interest in a new wave of innovative medicines. Uncertainties regarding the US government's healthcare policy and potential medicine price reductions are hurting sentiment for both US and European healthcare stocks.
Utilities	▶	▶	▲	▶	European Utilities are benefitting from favourable energy demand trends, positive price trends, and rising spending on energy infrastructure. Many economies are undergoing electrification of transportation and expansion of digital infrastructure, while rising affluence drives demand for air conditioning, freezers, etc. Utilities are already operating at full capacity, so substantial capital investments are required to upgrade generation capacity and transmission infrastructure. Valuations are undemanding.

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