Investment Monthly

Market rotation reinforces diversification across the AI ecosystem

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Key takeaways

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- Market concerns over AI overspending have led a rotation from semiconductor and hardware stocks to hyperscaler and software stocks. We maintain exposure across the AI ecosystem to avoid being caught by rapid shifts in momentum. We remain optimistic about the long-term AI trend, which supports broadening earnings growth within and beyond the IT sector, including Energy, Materials, Communications and Financials across regions.
- Despite elevated energy prices amid ongoing geopolitical uncertainty, the macro backdrop and corporate fundamentals remain favourable for equities. Bonds are driven by the fragility of the US-Iran peace agreement, surging AI investments and a more hawkish Fed Chair. Within bond markets, we prefer investment grade credit, given its higher quality and attractive valuations, with coupon income continuing to be the primary driver of total returns.
- The UK's new Prime Minister, Andy Burnham, is prioritising easing cost-of-living pressures, decentralising decision-making and increasing investment in public services, signalling that fiscal policy could become more expansionary. Gilt yields have moved higher and remain sensitive to fiscal policy and government borrowing. We expect the Bank of England to keep the Bank Rate unchanged this year. While the FTSE 100's exposure to energy and defensive sectors provides resilience, limited catalysts for a more positive overall equity outlook warrant a neutral stance on UK equities.

Asset class	6-month view	Comment
Global equities	▲	While global equity opportunities remain attractive, driven by AI-fuelled earnings growth and rising productivity across sectors, a selective and diversified approach remains critical to navigate ongoing market volatility.
Government bonds	▶	Inflation uncertainty and geopolitical risks support our preference for medium duration bonds across major developed markets.
Investment grade (IG) corporate bonds	▲	Global investment grade credit continues to offer attractive carry and diversification benefits. Near-term returns should favour coupon income over capital gains.
High yield (HY) corporate bonds	▶	While macro risks remain elevated and spreads are tight, risk appetite is supportive and all-in yields remain attractive.
Gold	▲	USD strength is a risk, but gold should still benefit from central bank purchases and diversification flows. We see potential upside towards year-end.

▲ "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.
Chinese equity views herein are from HSBC PB and Wealth Global Investment Committee

Talking points

Each month, we discuss 3 key issues facing investors

1. Is AI a sustainable investment theme following recent volatility?

- Market concerns over potential AI overspending have led to money moving out of semiconductors into hyperscaler and software stocks. We view this as profit-taking and repositioning rather than a loss of confidence in the AI theme.
- As markets continue to assess AI opportunities and their impact, we expect volatility and rotation to persist. Meanwhile, AI-driven earnings growth is broadening within and beyond the technology sector, with consensus forecasts for US earnings growth reaching 24% y-o-y in 2026. Initial Q2 earnings results are encouraging, particularly in Energy, IT and Materials. Valuations are now more balanced than it was at the start of the year.
- We maintain exposure across the AI ecosystem to avoid being caught by rapid changes in market momentum. While we remain positive on the IT sector due to the long-term AI trend, we also favour Energy, Materials, Communications and Financials across regions.

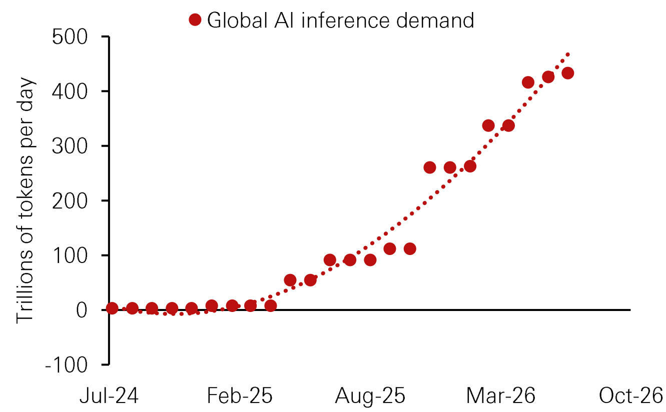
2. How are markets responding to ongoing geopolitical uncertainty?

- Renewed geopolitical tensions in the Middle East have recently pushed oil prices higher, putting pressure on margins and inflation, although tensions have moderated somewhat following a pause in US strikes against Iran. We don't believe the uncertainty will trigger broad-based downward revisions to global earnings expectations, as the macro backdrop and corporate fundamentals remain supportive of equities. Our overweight on the energy and materials sectors can help cushion the impact of energy-driven inflation.
- Bond markets are driven by the fragility of the US-Iran peace agreement, the macro implications of surging AI investments and a more hawkish Fed focused on taming inflation under Chair Warsh.
- We maintain a neutral stance on government bonds across major developed markets and prefer investment grade credit for diversification, given its quality and more attractive valuations. New US investment grade credit gross issuance reached USD1.2 trillion in H1 (+30% y-o-y), led by tech companies financing AI capital expenditure. In the near term, coupon income should remain the primary driver of total returns rather than capital gains, and we continue to be selective in emerging markets.

3. What is the outlook for the UK after Burnham takes office?

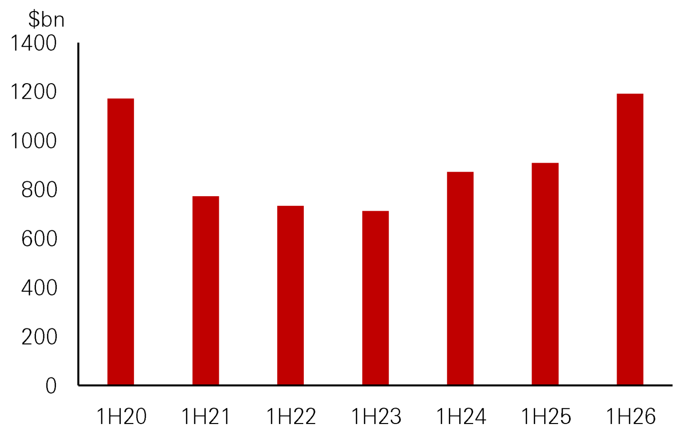
- The UK's new Prime Minister, Andy Burnham, has pledged a 'new economic model' aimed at easing cost-of-living pressures, decentralising decision-making and increasing investment in public services. Whether these goals can be achieved without undermining the UK's fiscal credibility remains a market concern.
- Burnham's comments about being flexible with government borrowing and spending rules suggest that fiscal policy could become more expansionary, pushing gilt yields higher across the curve. Sterling has also weakened as investors demand a higher premium for holding UK gilts. With the government relying more heavily on shorter-dated gilt issuance, a larger proportion of debt will require more frequent refinancing.
- UK gilts are likely to remain sensitive to fiscal policy and government borrowing. We remain neutral on gilts and expect the Bank of England to keep the Bank Rate unchanged this year. We continue to favour GBP investment grade credit for its attractive risk-adjusted returns. While the FTSE 100's exposure to energy and defensive sectors provides greater resilience than more domestically focused equity markets, limited catalysts for a more positive overall equity outlook support a neutral stance on UK equities for now.

Chart 1: Exponential structural demand growth for AI



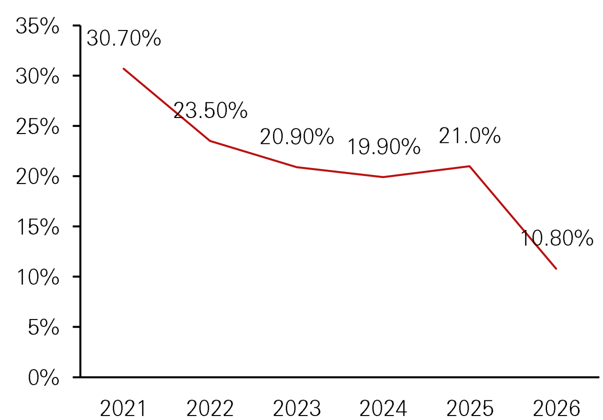
Source: Bloomberg, HSBC Private Bank and Premier Wealth as at 14 July 2026.

Chart 2: Elevated US investment grade supply is being well absorbed



Source: Bloomberg, JP Morgan, HSBC Private Bank and Premier Wealth as at 14 July 2026. Past performance is not a reliable indicator of future performance.

Chart 3: Share of long-term gilts in the DMO's Autumn debt issuance plan trends lower



Source: UK DMO, HSBC Private Bank and Premier Wealth as at 21 July 2026.

Asset Class Views

Our latest house view on various asset classes

Asset class	6-month view	Comment
Global equities		
Global	▲	While global equity opportunities remain attractive, driven by AI-fuelled earnings growth and rising productivity across sectors, a selective and diversified approach remains critical to navigate ongoing market volatility.
United States	▲	The US is resilient to the energy shock and is well exposed to AI-related upside, supporting earnings momentum to broaden beyond mega-cap stocks. Reshoring and the reindustrialisation of the US economy remain long-term structural growth drivers.
United Kingdom	▶	While markets are looking for greater clarity on spending priorities and borrowing plans under the new Prime Minister, modest domestic growth and still-above-target inflation continue to weigh on market sentiment.
Europe ex-UK	▼	The region remains sensitive to energy dynamics and uneven earnings momentum. We adopt a selectively cautious approach and see longer-term opportunities in defense, aerospace and security, which benefit from structural or policy support.
Japan	▶	The market has performed strongly year-to-date, but valuations remain elevated while earnings upgrades have been limited. We maintain a neutral stance for now, with a preference for the technology and financials sectors.
Emerging Market (EM)	▶	USD strength will exacerbate growth dispersion within the region. We see better opportunities in EM Asia, particularly in the technology-led markets of North Asia.
EM EMEA	▶	A permanent resolution to the Middle East conflict remains elusive, posing a headwind to regional growth, while South Africa benefits from a bullish outlook for gold.
EM LatAm	▶	Elections present two-way risks, but stronger commodity prices and trade flows with China remain supportive. Mexico should continue to benefit from greater access to the US economy than other emerging-market peers as the USMCA remains in force.
Asia ex-Japan equities		
Asia ex-Japan	▲	We take a selective approach to tapping into the region's diverse growth opportunities, with North Asia particularly well-positioned to benefit significantly from AI momentum.
Mainland China	▲	Attractive valuations, policy support and bottom-up opportunities remain supportive. We prefer the onshore to offshore Chinese market due to its higher exposure to AI hardware, semiconductors, robotics and manufacturing leaders.
India	▼	The fundamental backdrop remains challenging given higher valuations and limited exposure to the AI investment cycle, while elevated energy prices and El Niño concerns may add further inflationary pressures. Financials and Industrials are preferred.
Hong Kong SAR, China	▲	While retail sales growth should remain positive in H2, it is likely to moderate somewhat. We prefer banks, insurance, telecoms and utilities for their stable income, as well as quality developers with strong balance sheets and market positions.
Singapore	▲	Singapore equities are favoured for their defensive profile and attractive dividend yields.
South Korea	▲	Despite recent volatility linked to profit-taking in semiconductors, AI-driven earnings momentum, attractive valuations and corporate governance reforms remain positive drivers. Private consumption and exports are showing strong momentum.
Taiwan China	▶	Despite AI-led demand for advanced semiconductors, valuation concerns remain.
Government bonds		
Developed markets (DM)	▶	Inflation uncertainty and geopolitical risks support our preference for medium duration bonds across major developed markets.
United States	▶	Amid elevated inflation limiting the scope for easing and the need to monitor incoming macro data, we expect the Fed to keep the federal funds rate target range steady at 3.50%–3.75% throughout 2026 and 2027, although upside risks have increased.
United Kingdom	▶	With the Bank of England now putting rates on hold while maintaining a hawkish bias amid geopolitical risks and higher oil prices, gilt markets are likely to remain sensitive to incoming inflation and fiscal developments.
Eurozone	▶	While recent inflation data do not signal broad-based second-round pressures, risks are skewed to the upside amid elevated oil and gas prices. We now expect a rate hike at the ECB's September meeting.
Japan	▶	Wage growth and corporate sentiment may support a gradual tightening path by the Bank of Japan. We expect one more hike by year-end, but the risk of an earlier move has increased due to concerns about yen weakness and higher inflation.
EM (Local currency)	▶	A stronger USD and a more hawkish Fed mean upside is limited, and we no longer see a strong case for EM local currency bonds to outperform high yield.
EM (Hard currency)	▶	While both USD strength and attractive yields are supportive, we remain selective and generally focus on quality.
Corporate bonds		
Global investment grade (IG)	▲	Global investment grade credit continues to offer attractive carry and diversification benefits. Near-term returns should favour coupon income over capital gains.
USD investment grade	▲	While supply remains elevated, it is being well absorbed by robust investor demand seeking attractive yields.
EUR investment grade	▲	We continue to prioritise carry and income through EUR investment grade credit with a medium-to-long duration bias.
GBP investment grade	▲	We favour GBP investment grade credit to build portfolio resilience while maintaining a medium duration stance (5-7 years).
Asian investment grade	▲	Asian credit has shown resilience and continues to offer attractive yields, supporting our income-led approach. We prefer Australian IG bonds, Asian financials and Chinese hard currency bonds.
Global high yield (HY)	▶	While macro risks remain elevated and spreads are tight, risk appetite is supportive and all-in yields remain attractive.
USD high yield	▶	While risk appetite remains strong, we see better value in investment grade bonds, especially with increased supply in high-grade IT issuers.
EUR high yield	▶	We adopt a selective approach with a short-to-medium (3-5 years) duration preference for now.
GBP high yield	▶	A weaker currency and softer growth outlook temper enthusiasm for risk assets. We remain neutral on GBP high yield.
Asian high yield	▶	We maintain a neutral position to align with our global high yield allocation, reflecting our focus on quality.
Commodities		
Gold	▲	USD strength is a risk, but gold should still benefit from central bank purchases and diversification flows. We see potential upside towards year-end.
Oil	▶	Oil prices are likely to remain volatile in the near term as markets can reprice quickly in response to geopolitical uncertainty.

Sector Views

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

Sector	Global	US	Europe	Asia	Comment
Consumer Discretionary	▼	▶	▼	▶	Company margins have been squeezed by higher energy and labour costs, combined with softening demand and a weak pricing environment. In the US, there are early signs of a recovery in consumer demand across some segments, reflecting the continued strength of the US economy. Elsewhere, the combined effects of the Middle East conflict and record temperatures are driving sales of solar panels, batteries, EVs and air conditioners. Growth in the luxury goods segment remains challenging following years of unsustainable price rises.
Financials	▲	▲	▲	▲	Financial market volatility is challenging for the sector, but overall quarterly results have remained very strong. US financials continue to trade at a premium to their global peers due to their superior growth. Trading continues to see strong order flow, with corporate advisory (M&A and IPOs) and debt issuance businesses also booming. Sector momentum is showing some signs of stalling, but this may be transitory. The outlook for the insurance sector is more mixed, given the rise in weather-related and other catastrophic events.
Industrials	▲	▲	▲	▶	Industrials are benefitting from the multi-year roll-out of new technologies, including infrastructure (energy, digital and AI), aerospace, defence, electric transportation, automation and robotics. Order books continue to grow, with companies committing capital to new and upgraded production. Limited excess capacity is providing a supportive pricing environment.
Information Technology	▲	▲	▲	▲	Higher investment spending continues to weigh on sentiment and the sector's performance, despite strong quarterly results and growth forecasts that exceed the broader market. Valuations remain attractive, with the sector now trading slightly above the broader equity market rather than at its historical premium. Demand for AI software, related hardware and semiconductors is driving robust growth as companies across every sector deploy AI-enabled products and services. Earnings visibility continues to improve in Europe.
Communications Services	▲	▲	▲	▲	Media and entertainment segments continue to report above-average sales and earnings growth, combined with undemanding valuations, although consumer demand may be affected by rising energy prices and other costs. Asia remains attractive, although relative valuations are less compelling. The telecom services segment has attractive defensive qualities, with improving fundamentals, low valuations, high dividend yields and low exposure to tariffs.
Materials	▲	▲	▲	▲	Miners continue to benefit from a supportive macroeconomic backdrop, steady demand and sustainable price rises. Construction materials are seeing early signs of improvement. In contrast, margins in the chemicals industry are under pressure from higher energy and feedstock prices. Speciality materials/miners, including rare earth metals used in high technology products, are seeing robust demand.
Real Estate	▶	▶	▶	▶	The uncertainty regarding interest rate policy and the direction of potential changes is weighing on sentiment. Demand for high-quality office space and high-tech facilities, including data centres and specialist manufacturing, remains solid. Retail real estate remains challenged. The US market is particularly benefitting from reshoring trends and an improving residential market.
Consumer Staples	▼	▼	▼	▼	Sentiment is weak as margins are squeezed by rising costs (including energy, labour, and soft commodities). The pricing environment remains challenging as inflation is changing consumer demand patterns. Valuations reflect the sector's limited growth potential.
Energy	▲	▲	▲	▲	Oil and gas supply remains tight, with prices remaining elevated as the Middle East conflict continues. Global energy supply chains, together with damage to energy infrastructure, may delay a swift return to normality. Energy producers and refiners are likely to continue benefitting from elevated energy prices over the next several quarters. Valuations, free cash flow and dividend yields remain attractive for now.
Healthcare	▶	▶	▶	▲	The US government's healthcare policies remain in flux, posing a potential risk to sales and profits. M&A activity has picked up as companies look to offset pricing pressure on older medicines with new innovative products. Healthcare companies in Asia, particularly in China, are benefitting from new product launches, improving demand dynamics and relatively low valuations. New technologies in drug discovery, testing, patient records and diagnosis are set to transform the sector.
Utilities	▲	▲	▲	▶	Utilities are managing a multi-year surge in demand for electricity as many segments of the economy transition away from fossil fuels, while IT-related demand for electricity continues to soar. With limited spare capacity, substantial capital investment is required to upgrade generation capacity and transmission infrastructure. Valuations and yields remain attractive.

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