HP WEALTH MANAGEMENT

February 2025

INVESTMENT STRATEGY FEBRUARY 2025

CIO THOUGHTS

Trade War 2.0 has begun, with tariffs set on China, steel, and aluminium, while those on Mexico and Canada have been delayed. The scope, timeline, and escalation potential of these tariffs remain uncertain. We, therefore, recommend a well-diversified portfolio with strategic hedges to withstand policy shifts, sudden reversals, and potential volatility spikes. We see Financials, US Energy, and gold benefiting from reshoring, inflation hedging, and a stronger US dollar, while Consumer, Tech, and Auto stocks face valuation compression risks.

Michael Foo
CIO and Partner

ASSET CLASSES

Equities

Updates:

- **Market Impact:** Rising costs, margin pressures, and uncertainty from tariffs on major US trading partners drive P/E compression, lowering valuations for multinational stocks.
- **Winners & Losers:** Gold, US Financials, and Energy may gain as inflation hedges, while consumer stocks (low pricing power) and industrials (tariffs exposure) face losses.

Our View:

- **US:** Neutral, tariff concerns mitigated by continued US economic and corporate exceptionalism.
- **Japan:** Overweight, with reflation trajectory remaining strong. Concerns on BoJ policy and currency weakness should subside.
- **Europe:** Underweight, due to weak economic and earnings growth coupled with vulnerability to tariffs.
- **Asia ex-Japan:** Neutral, tariff concerns and trade policy uncertainties may be balanced by a stronger recovery in China.

Credit

Updates:

- US tariffs introduce risks to corporate fundamentals and global trade.
- Corporate spreads remain tight but are supported by strong fundamentals, low default rates, and attractive yields. This should persist under a pro-growth, deregulation-focused US policy environment.

Our View:

- IG preferred to HY, given evolving risk landscape.
- Remain Neutral on Emerging Market Debt, given fiscal divergences and exposure to trade risks.

FX / Gold

Updates:

- **US Dollar:** strong US economic data (particularly solid payrolls) and tariff concerns continue to reinforce Dollar strength. The Dollar remains the best hedge against ongoing trade risks, with further upside likely if tariffs persist or escalate.
- **Gold:** surged to a record high of $2,942 on February 11, fueled by tariff concerns, Chinese demand, and market structural factors.

Our View:

- **USD:** best hedge against ongoing tariff risks, with further upside likely if tariffs persist or escalate.
- **Gold:** remains an attractive hedge against US policy uncertainty, supported by central bank demand, despite short-term volatility. Maintain allocations.

MACROECONOMIC OUTLOOK

"The US economy remains strong, giving the Fed reason to pause rate cuts. The labour market remains robust, with consumers worrying about tariff-driven inflation. Moderate tariffs should have a limited impact, but a severe escalation could significantly raise prices. In Europe, stable growth and lower inflation have allowed the ECB to continue easing rates.

Edwin Chan

Senior Portfolio Manager

US

- **Labour Market:** Non-farm payrolls rose by 143k, with a net upward revision of +100k for prior months. Unemployment dropped to 4.0%, but the average workweek fell to a cycle low of 34.1 hours. Nominal labour income grew close to 5% annualized.
- **Manufacturing Strength:** The ISM manufacturing index moved into expansionary territory for the first time since 2022, driven by new orders and reshoring trends, supporting Fed caution on rate cuts.
- **Consumer Confidence Drop:** February's University of Michigan survey showed a sharp decline, driven by rising inflation expectations, likely tied to tariff concerns.

China

- **Measured Response:** China's counter-measures to the US 10% tariff hike include targeted tariffs on US oil, LNG, agricultural machinery, and rare-earth mineral export controls. This is much narrower in scope than expected and a sign that China is aiming to avoid a severe trade war escalation.
- **De Minimis Rule Impact:** If the US eliminates the de minimis rule, tariffs could rise by 2%, affecting 8% of US imports from China.
- **Limited Short-Term Impact:** The 10% tariff hike has minimal near-term effects, but higher permanent tariffs would bring considerable pain.
- **Long-Term Risks:** A 60% tariff could cut China's exports by 80%, reducing GDP by 2.3%.

Europe

- **Economic Recovery:** Euro area composite PMI has improved, led by Germany, with steady consumer spending. However, growth forecasts remain cautious due to US trade policy uncertainty.
- **Inflation:** January inflation data confirms disinflation progress, with core inflation at 1.8% annualized, largely driven by cooling core services prices.
- **ECB Rate Cuts:** With inflation improving and moderate growth, markets expect the ECB to cut rates to 1.75% in 2025.
- **Market Impact:** Lower rates have boosted European risk assets, which have performed well in early 2025.