EQUITY ADVISORY ASIA

Equity Perspectives

HK / China ▪ United States ▪ Europe / UK

Second Issue, 2025

BNP PARIBAS
WEALTH MANAGEMENT

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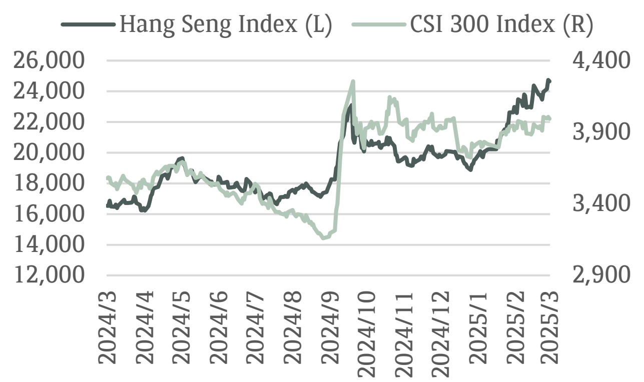
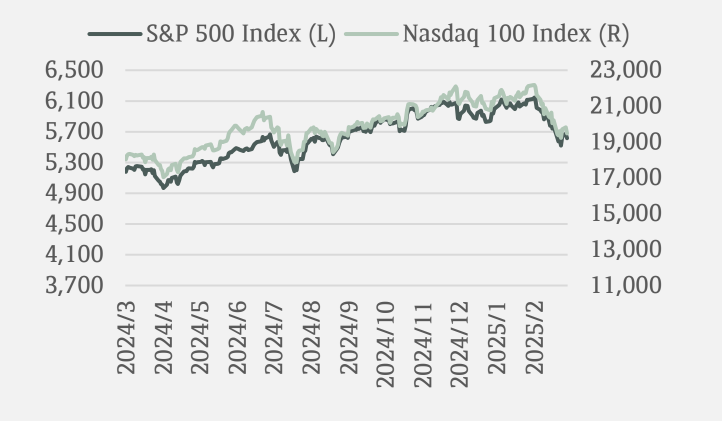
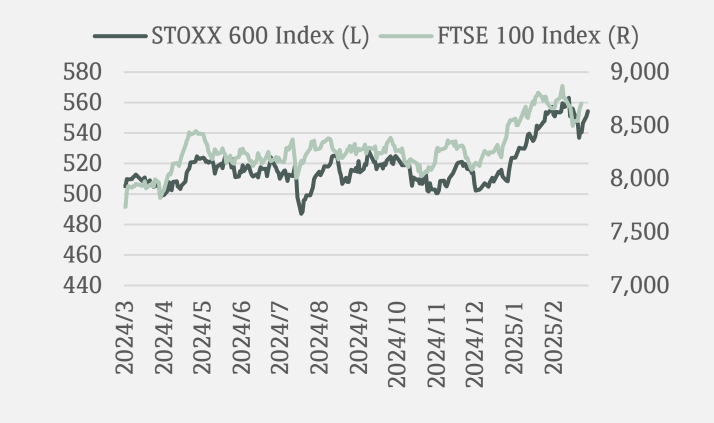
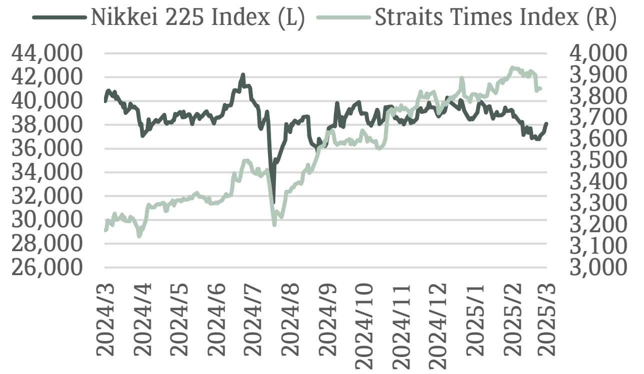
Major indices performance at a glance









Source: BNP Paribas, Bloomberg, as of 18 March 2025
Past performance is not indicative of current or future performance

MARKET SNAPSHOT

Since mid-February 2025, US stocks pulled back as trade uncertainties and a softening economy weighed on a market that had been "priced for perfection." Valuations have now eased, although volatility is likely to remain for some time. We favour a more prudent asset allocation approach within the country as we await more clarity, seeing value in sectors such as financials, health care, and industrials.

On the flipside, HK/China equities leapfrogged to become one of the best performing major market year to date* (YTD), boosted by optimism on the country's AI innovations and a potential consumer revival. We remain positive on HK/China stocks, seeing a structural shift in sentiment with valuations still undemanding versus peers. The current narrow market breadth should first widen, however, to underpin a healthy bull market

European shares also performed well YTD on hopes of government stimulus and a luxury revival. Valuations are undemanding, especially in UK equities as its defensive merits remain favourable in our view.

**as of 18 March 2025*

LATEST MARKET UPDATE

HK / China: Tide Turns

The Chinese economy is well prepared for a de-coupling from the US. What was perceived as risks in the past may be becoming moats.

What happened?

The rise of low-cost artificial intelligence (AI) models in China despite Graphics Processing Unit (GPU) constraints have reinvigorated enthusiasm towards Chinese technology & internet sectors. Top government officials' pro-growth tone during the Two Sessions in March 2025 reinforced market expectations for more stimuli and less regulatory scrutiny. The Hong Kong stock market shrugged off worries over escalated US-China trade tensions and imminent deflation risks in mainland China. Nonetheless, it is astonishing that Hong Kong has outperformed most other major stock markets year-to-date.

In our August 2024 publication, we highlighted that international investors could enhance risk-adjusted returns via having exposure to HK / China stocks. The case still holds true whilst Hang Seng Index (HSI) and CSI 300 Index demonstrate weak-to-moderate correlations with global stock markets (please see Chart below).

CORRELATION MATRIX OF WEEKLY PERFORMANCE OF STOCK MARKET INDEXES FOR THE PAST 2 YEARS

	HSI	CSI300	S&P500	TOPIX	STOXX600	MSCI World
HSI	/	0.71	0.33	0.32	0.47	0.42
CSI300	0.71	/	0.22	0.22	0.22	0.26
S&P500	0.33	0.22	/	0.57	0.67	0.97
TOPIX	0.32	0.22	0.57	/	0.47	0.62
STOXX600	0.47	0.22	0.67	0.47	/	0.78
MSCI World	0.42	0.26	0.97	0.62	0.78	/

Source: Blomberg, BNP Paribas as of 12 March 2025

Our thoughts

The stock market rally in Hong Kong so far is very AI-centric. As of 12 March 2025, only 23 out of the 83 Hang Seng Index constituents outperformed the index since the release of DeepSeek R-1 on 20 January 2025. The top five outperformers are all AI-related. We think the narrow market breadth should widen to underpin a healthy bull market. Therefore, we expect active sector rotations with a range-bounded market index in the second quarter of 2025.

How to play the game?	
Everything AI	Low-cost AI models spawn numerous new business opportunities in other industries. Many companies have trumpeted to leverage on AI, however not everyone has tech-DNA in our view. We prefer companies with good track record of using technologies to enhance their products.
US tariffs	Be selective with companies in industries that have high sales exposure to the US market, such as solar panel manufacturers. Excess capacity across the industries will inevitably lead to thinning profit margins.

Notable Developments in Selected Sectors

- **Consumer:** Premier Li placed "vigorously boost consumption" at the top spot of the Chinese government's agenda in his 2025 Government Work Report, rising from the third place in 2024. The State Council followed up with a thirty-point action plan for boosting consumption. Provincial governments are expected to roll out a vast array of stimulative policies in the coming months.
- **Low-cost AI:** China's DeepSeek-R1 is perceived as a game-changer for the global AI race whereby hardware requirements and development costs for AI-models could be significantly lower than previously thought. Falling inference costs of open-source AI-models will incubate innovative ideas that address AI-use cases for numerous smaller audience groups. An exponential growth in the number of AI-applications, that each may need a little more computation power, in turn requires sizable increase in hardware infrastructure capacity. Blossoming AI-applications may also trigger consumer upgrade to AI-capable smartphone and gadgets.

LATEST MARKET UPDATE

US: Balancing Act Between Risks and Returns

What happened?

Following the most recent all-time high in the S&P 500 index achieved on 19 February 2025, we have seen some pullback in US equities, which has brought valuations from this year's peak multiple of 22.6x forward price/earnings (P/E) to more palatable levels of ~18.6x forward P/E, which is approaching the index's 10-year historical average of ~17.7x (estimates as of 11 March 2025).

Our thoughts

The start of 2025 has already seen prior expectations of elevated market volatility playing out as investors recalibrated their risk appetites with increasing uncertainties and risks perceived from ongoing trade and policy reviews prioritised by the new Trump administration, while previous hope for tailwinds such as potential tax cuts, deregulation and more business-friendly policies now look likely to come at a later stage. As a result, we have recently downgraded US equities to Neutral, favouring a more prudent asset allocation stance as we await more clarity from the frequent radical and unpredictable shifts in US government's trade policies.

For FY25E and FY26E, consensus forecasts for MSCI US index's earnings per share (EPS) growth are currently for 12.1% and 14.4% respectively, which remain higher than World equities' EPS growth forecast at 10.3% and 13% respectively (estimates as of 3 March 2025). Should earnings delivery hold up and tariff uncertainties ease in the coming months, we see potential for market bounces ahead which could open new opportunities for tactical investors.

On sectors, we continue to favour financials (banks, insurers), industrials and healthcare sectors. For banks, we expect deregulation and enhanced Merger & Acquisition (M&A) activities to be supportive of earnings. Areas that may face headwinds include tariff-exposed stocks or those related to the climate movement such as renewables, where future executive actions could favour some rollback of green policies.

Despite near term profit-taking pressures, we remain constructive over the medium term on the AI theme which we view as a multi-year structural theme. Within the wider technology sector, we continue to advise diversification beyond hardware and semiconductors to software picks which offer limited direct tariff risk exposures and future growth prospects in AI-enabled product innovations. Key industrials ideas are maintained in view of continued reshoring tailwinds expected. We continue to see opportunities in healthcare's defensive-growth merits, while AI also has the potential to transform the industry, reducing costs and improving savings in the long run. Other investment themes favoured include clean water, gold and copper miners.

How to play the game?	
Areas on our radar	Trade policy uncertainties, earnings and economic growth trajectory, AI investment
Investment implications	To favour a more prudent asset allocation approach while ensuring diversification

Notable Developments in Selected Sectors

- **Industrials:** The manufacturing sector should see tailwinds from higher industrial activities, data centers and AI-driven infrastructure build-up, while demand for capital goods such as machinery should also improve, helped by pro-growth policies and lower interest rates ahead.
- **Healthcare:** Sector stocks have made a strong start to 2025, benefiting from market volatility and a rotation out of higher-beta sectors. President Trump's new healthcare department appointees are viewed as potential industry disruptors, which may add some uncertainty. However, we still see opportunities in healthcare's defensive-growth merits, while AI also has the potential to transform the industry, reduce costs and improve medical outcomes.
- **Information Technology:** Recent volatility stems from concerns regarding AI spending sustainability, competitive pressures, and macro developments. The confluence of factors has triggered a market correction. While short-term jitters are evident, this has led to valuation adjustments within key AI enablers, resulting in a more nuanced valuation landscape. We maintain a constructive medium-term outlook as fundamental growth drivers within the theme remain robust.

LATEST MARKET UPDATE

Europe/UK: Europe's Leading the Way

What happened?

European equities have had a robust start to the year and have outperformed US markets, despite mixed macro data, political tensions, and fears that tariffs from a Trump presidency will adversely impact regional profitability. Significantly, Germany's federal election has helped change the investment and political landscape, with the conservative Christian Democratic Union/Christian Social Union (CDU/CSU), led by Friedrich Merz, emerging as the victor. The CDU/CSU and SPD, likely coalition parties, have proposed a EUR500bn special fund for infrastructure spending spread over ten years, as well as finally more financial leeway for the German states. In addition, there was a new defence proposal that "necessary defence spending" above 1% of Gross Domestic Product (GDP) should be exempt from debt brake restrictions, with no upper limit. If approved, this would open up the way for significant broader spending. Separately, the European Commission also announced a EUR800bn plan to increase European defence spending. In addition to the fiscal spending story, European market performance has been driven by stocks aligned with structural themes (e.g., renewable energy and AI), signs of recovery in the luxury goods space, and investment opportunities aligned with a potential end to the Ukraine-Russia war. The European Central Bank (ECB) has lowered the key deposit rate six times since June 2024. Signs of Eurozone inflation easing boosted confidence that the ECB is approaching its 2% target. We expect more cuts in 2025 with a terminal deposit rate at 2% in September 2025. The results season has been modestly supportive, with Banks and Healthcare registering the strongest earnings surprises. However, stocks particularly exposed to tariffs and global trade policy uncertainty have led the downgrades.

Our thoughts

Even after the recent strong market performance, European stocks still trade at reasonable valuation levels (the Stoxx 600's Price to Earnings (P/E) of 14.3x, as of 11 March 2025). We are positive on Healthcare, Industrials, Materials and Financials. In the UK, leading economic data has been more upbeat, in contrast to the more pessimistic tone in markets and the country. The government has taken a pro-growth tone, but the Chancellor may renege on her promises to raise tax, which would be a blow to confidence. Still, a lot of negativity is already reflected in market valuation. The UK still offers value, trading on 12.9x forward P/E for the FTSE 100 and the MSCI UK as of 11 March 2025, with the market's defensive merits remaining favourable.

How to play the game?	
Areas on our radar	Trade policy and geopolitical uncertainties, government stimuli, economic recovery.
Investment implications	To avoid excessive trade policy exposure while favouring sectors with structural tailwinds such as Healthcare, Financials, Materials, and Industrials

Notable Developments in Selected Sectors

- **Financials:** Banks are the best Stoxx 600 performers in 2025 so far (as of 18 March 2025). Broader confidence remains healthy, with the banking sector offering substantial shareholder returns on the back of strong earnings. A potential continuation in regional sector M&A would also be positive, with the sector having seen the most M&A activity since 2020.
- **Materials:** Germany's EUR500bn infrastructure fund and a potential ceasefire in Ukraine are expected to be supportive for the sector. We have upgraded European Chemicals from Negative to Neutral after sizeable underperformance over the last 2-3 years.
- **Industrials:** Supported by increased fiscal spending in Germany, the sector is expected to be a beneficiary of increased capex spending in key structural growth areas, including defence, electrification, industrial automation and renewables. The sector would also benefit if we see a resolution to the Ukraine-Russia conflict and a country rebuild.

Equities Allocation

POSITIVE NEUTRAL NEGATIVE

OVERALL GLOBAL MARKETS: POSITIVE

POSITIVE	NEUTRAL	NEGATIVE
COUNTRY		
UK Japan	US Eurozone	-
SECTOR		
Financials Healthcare Materials Industrials Utilities	Communication Services Real Estate	Consumer Staples Energy Technology Consumer Discretionary

OVERALL ASIAN MARKETS: POSITIVE

POSITIVE	NEUTRAL	NEGATIVE
COUNTRY		
China Hong Kong	-	-
SECTOR		
Communication Services Consumer Discretionary Consumer Staples Technology	Energy Materials Real Estate Financials Healthcare Utilities	Industrials

Note: Orange indicates an upgrade, while red indicates a downgrade

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