

Summary

- ▶ The Fund recorded a positive gain and outperformed the index due purely to stock selections
- ▶ Country allocation detracted, as the positive from the underweight in Indonesia was outweighed by the underweight in Korea. Sector allocation was also negative to relative performance, mainly due to the underweight position in healthcare, a sector which had a great run during the month
- ▶ We have conviction in opportunities among alternative energy in China and India, regional automobile components manufacturers and Chinese textile

Market overview

MSCI Asia ex Japan Small Cap Net index posted a 1.4% gain in US dollar terms during the month, boosted by China as the country signaled that it has scope to do more to support economic growth. In particular it announced policies supportive of the property market.

The China Securities Regulatory Commission (CSRC) announced on 27 March 2015 that newly established domestic mutual funds in mainland China will be allowed to invest in Hong Kong stock market through Shanghai-Hong Kong Stock Connect without Qualified Domestic Institutional Investor (QDII) quota. The announcement is an important catalyst to H-shares and other HK-listed stocks. After a rally of the A-share market from Q4 2014, the offshore H-share market is trading at big discount to its domestic counterparts. Meanwhile, inflation data in the region remains benign. Korea surprised the market with a 25 basis point (bp) rate cut to 1.75% while the Reserve Bank of India (RBI) in India cut the repo rate by 25bps to 7.5%. Thailand also cut rates. Other regional central banks appear in the region appear to have scope to cut rates further or retain already low rates.

China and Korea were the best performing markets in March on the back of supportive comments on growth from the former and a rate cut in the latter. On the other hand, Thailand was the worst performing market, followed by Indonesia and Malaysia. On a sector level, healthcare gained ground and outperformed, while telecommunication services retreated and lagged the market.

Portfolio strategy

The Fund recorded a positive gain and outperformed the index due purely to stock selections. Country allocation detracted, as the positive from the underweight in Indonesia was outweighed by the underweight in Korea. Sector allocation was also negative to relative performance, mainly due to the underweight position in healthcare, a sector which had a great run during the month.

Overall stock selection was positive for the Fund. Selection in Hong Kong contributed significantly, mainly due to the Fund's overweight positions in consumer discretionary companies, namely Century Sage Scientific and Man Wah. On a sector level, selection in industrials was a major driver of positive relative performance, with China Eastern Airline being a notable contributor. The stock rallied during the month, given the company benefited from the falling oil price, the strengthening of traffic growth and as it was trading at a deep discount to its A-share counterpart.

Outlook

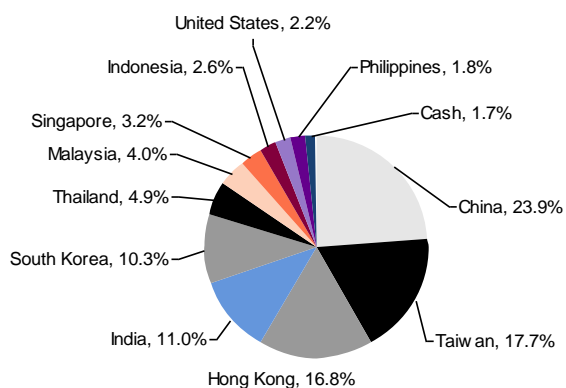
The overall inflation outlook in the region is also subdued, which will give policy makers room to move on rates as needed. The oil price, despite stabilizing recently, remains at relatively low levels which is a net benefit to Asia ex Japan. We also see positive trends in terms of fiscal consolidation in markets that are winding back energy subsidies and increasing infrastructure spend such as India, Malaysia and Indonesia. China's recent policy announcements to support growth are also a positive for regional markets.

There are also other potential positive catalysts on the horizon around economic and structural reforms. In China, Premier Li Keqiang covered a wide range of key reform areas for 2015 at the recent National People's Congress, including financial, fiscal/tax, State-Owned Enterprises (SOE) and hukou reforms and laid out key growth strategies. He also addressed key topics around pollution and anti-corruption. The government's strong intent to maintain stable growth and its focus on reforms could help ease concerns about China's growth outlook, earnings prospects and credit risk, and support the financial markets in the near term, amid a more supportive macro policy backdrop.

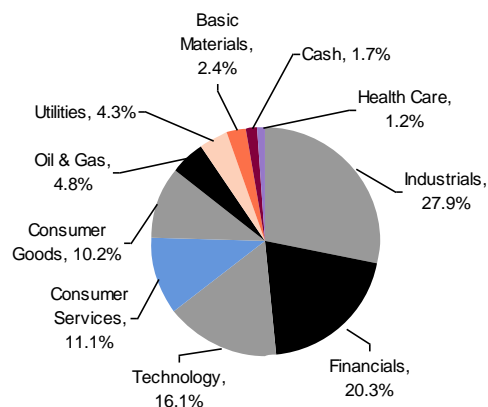
India's commitment to fiscal consolidation, tax reform and infrastructure spend in its February budget is also a positive sign for markets. Looking forward, we expect India's GDP to recover from three years of below trend growth and accelerate further on the back of some structural reforms as and when initiated. The passage of the Land Acquisition bill, a key reform agenda for the government, in the coming session of the Indian Parliament will be closely watched by the market.

We continue to find pockets of attractive stocks within the small cap markets. In particular, we have conviction in opportunities among alternative energy in China and India, regional automobile components manufacturers and Chinese textile. We are also positive on sectors and companies that will be the potential beneficiary of lower oil prices.

Country allocation¹



Sector allocation¹



Top 10 holdings¹

Name	Weight (%)
China Resources Land	2.9
Man Wah Holdings	2.5
Ezion	2.4
Panin Financial TBK PT	2.2
Nexteer Automotive	2.2
Hyundai Development	2.2
China Eastern Airline	2.1
WT Microelectronics	2.1
VST Holdings	2.0
KCE Electronics	2.0

Performance²

%	Class AD in USD terms				Annualised		
	1 mth	3 mths	6 mths	1 yr	3 yrs	5 yrs	Inception (21 November 1997)
NAV	2.7	7.3	-1.8	6.2	17.0	11.6	10.5
NAV*	-2.7	1.7	-6.9	0.6	14.9	10.4	10.1
BM	1.4	5.6	0.2	5.0	7.2	4.5	8.6

Source: 1. HSBC Investment Funds (Hong Kong) Limited as at 31 March 2015. Data shown is for illustrative purposes only and does not constitute investment recommendation to buy or sell in the above-mentioned sectors, countries or securities.

2. HSBC Global Asset Management & Morningstar, Inc. as at 31 March 2015, dividend reinvested in USD terms.

*Net of sales charges. BM (Benchmark) = MSCI Asia ex-Japan Small Cap Index. With effect from 1 November 2008, the benchmark has been changed to the MSCI Asia ex-Japan Small Cap Index. The new benchmark will ensure that the Fund's performance is measured against a benchmark more suited to its strategy. Past performance is not indicative of future returns.

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