global **market outlook**

This reflects the views of the Wealth Management Group

macro strategy | 05 August 2014

Volatility likely to remain low for a while

We expect volatility to remain low in the coming months given high visibility on economic growth, earnings growth (especially in the US) and inflation. At some point, rising US inflation and interest rate expectations may lead to a temporary increase in volatility, but we are likely some months away from this. Global equities remain our preferred asset class in both the short term (next 3 months) and the medium term (12 months).

Favoured asset classes:

- **All major equity regions expected to generate positive returns.** We believe all major equity regions (Europe, US, Asia ex-Japan, Japan and non-Asia Emerging Markets [EM]) will generate positive returns over the next 12 months. We have a slight preference for Europe and the US, but we prefer a diversified global equity allocation.
- **Momentum strengthening in Asia.** Three key drivers of potential equity returns (economic momentum, monetary policy and valuation) have improved in Asia, led by China. The clearest shift has been in economic growth expectations, which are starting to reverse the downgrades seen over the past two years.
- **EM bonds favoured.** We continue to find greater value in Asian bond markets. From a local currency perspective, we like CNY, CNH bonds as well as a diversified exposure to Asian local currency bonds. From a USD bond market perspective, we like EM High Yield (HY) government bonds, as valuations are not as stretched as Developed Market (DM) corporate HY (see below).

Changes from last month:

- **Cut DM HY bonds to Neutral from Overweight:** Since we turned OW on DM HY (September 2011), this asset class has generated absolute returns of approximately 41%, outperforming global bonds by around 35.4%. However, increasing corporate leverage has led to a deterioration in creditworthiness, in our opinion. Given stretched valuations, we believe now is a good time to reduce exposure. Within an income portfolio, we would increase our allocation to CNY, CNH bonds and leveraged loans (see page 12)
- **Raise India equity allocation to Overweight** as two of the three criteria we identified as drivers of our allocation decision are flashing green (see page 7).

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Risk indicators still supportive of equity markets

S&P 500 red flag checklist

Market indicators	June	July
Valuations at 17x forward P/E		
Unsustainable pace of appreciation		
Domestic outperfoming global		
Defensives outperforming cyclicals sectors		
Treasury rally	x	x
Global indicators	**June**	**July**
Negative surprises from Europe/Japan		x
Significant slowing in EM growth	x	
Reversal of Manufacturing recovery		
Significant USD strength		
Domestic Indicators	**June**	**July**
Fading employment momentum		
Stalled housing recovery		
Policy wildcard		

Source: BCA Research (indicators), Standard Chartered (views)
Note: Xs mark events that have occurred or could soon occur

Steve Brice	*Chief Investment Strategist*
Manpreet Gill	*Head, FICC Investment Strategy*
Adi Monappa, CFA	*Head, Asset Allocation & Portfolio Solutions*
Audrey Goh, CFA	*Investment Strategist*
Victor Teo, CFA	*Investment Strategist*
Tariq Ali, CFA	*Investment Strategist*

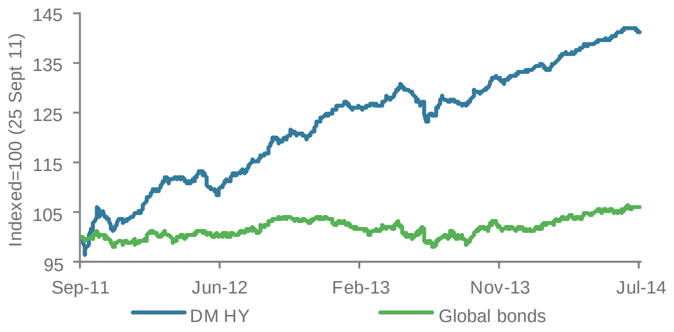
Asia economic growth gathering momentum

Consensus Asia ex-Japan 2014 GDP growth forecasts

Source: Bloomberg, Standard Chartered

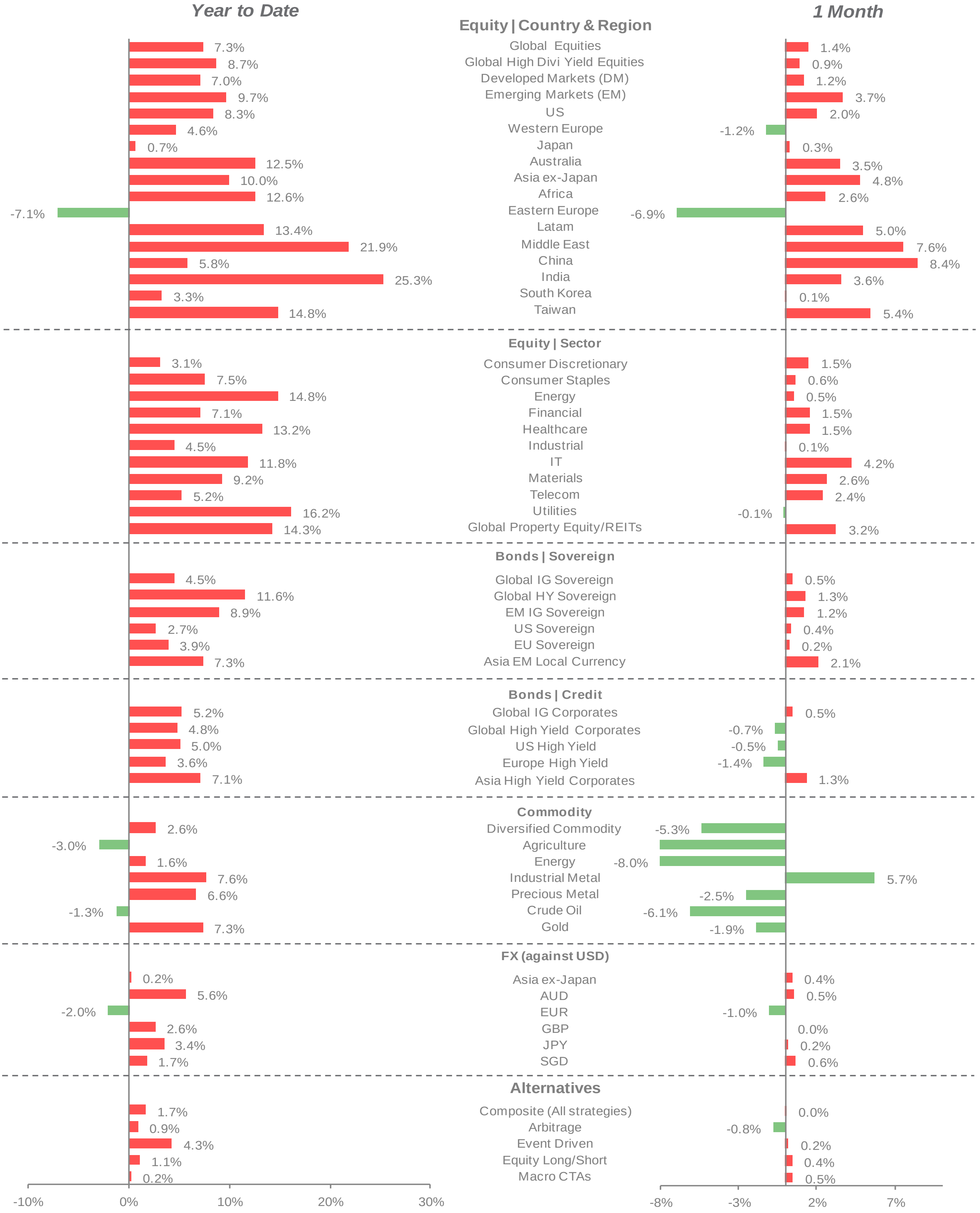
Close the DM HY bond Overweight stance

Performance of DM HY since we turned OW vs. global bonds



Source: Barclays Capital, Citigroup, Bloomberg, Standard Chartered

Market Performance Summary (Year to Date & 1 Month)*



** All performance shown in USD terms, unless otherwise stated.*

**YTD performance data from 31 Dec 2013 to 24 July 2014 and 1-month performance from 24 June to 24 July 2014*

Sources: MSCI, JP Morgan, Barclays Capital, Citigroup, Dow Jones, HFRX, FTSE, Bloomberg, Standard Chartered

Investment Strategy:

- **Little reason to expect volatility to increase near term**
- **Remain bullish on global equities in both the short and medium term**
- **We cut Developed Market High Yield (DM HY) to Neutral from Overweight, reallocating to CNY, CNH bonds and leveraged loans in an income portfolio**

Volatility expected to remain low in the coming months. More and more market commentators are calling for an increase in equity market volatility (read: equity market weakness). Equities are generally a volatile asset class and, therefore, short-term weakness is always possible. However, we would make three points:

- **Any weakness is expected to be short term, with any losses likely to be being quickly recouped.**
- **Increasing volatility is not necessarily the same as equity market weakness.** Volatility can increase in a rising equity market, as happened between 1995-97.
- **Low volatility is likely to extend.** Increased volatility usually occurs during periods of greater uncertainty surrounding the economic, earnings or inflation outlook. The trigger for such a near-term increase in uncertainty is unclear. At some point, increasing US inflationary pressures could lead to greater uncertainty, but we appear some months away from this.

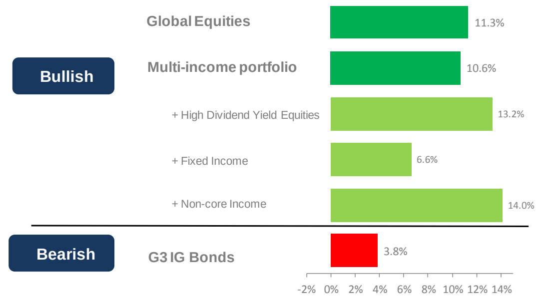
Implications for investors:

- **Stay the course.** We do not believe in selling equity holdings to take advantage of any short-term weakness. Indeed, we would advocate moving towards an Overweight equity position for those who have yet to do so. We prefer a diversified equity allocation rather than one that is focused in one or two regions or sectors.
- **Generating upfront premia to remain challenging near term.** A favoured strategy amongst many investors is to sell FX or equity put options to generate an upfront return. While we believe this is a perfectly valid strategy, the current low volatility environment makes it difficult to generate attractive returns.

DM HY bonds reduced to Neutral. We have closed one of our longest standing Overweights, namely DM HY bonds. Since we initiated this OW (September 2011), this asset class has generated returns of approximately 41%. However, a slight deterioration in balance sheet strength and stretched valuations make this a good time to close this stance, in our opinion (see page 6 for more details).

A.G.I.L.E. themes have performed reasonably well

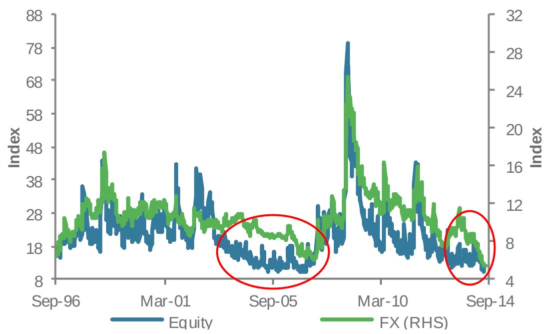
*AGILE performance since Outlook 2014 was published**



** For the period 16 December 2013 to 24 July 2014*
Source: Bloomberg, Standard Chartered
** Income basket is as described in the Outlook 2014: A Year to be A.G.I.L.E., Figure 53.*

Volatility is low and could remain low for an extended period

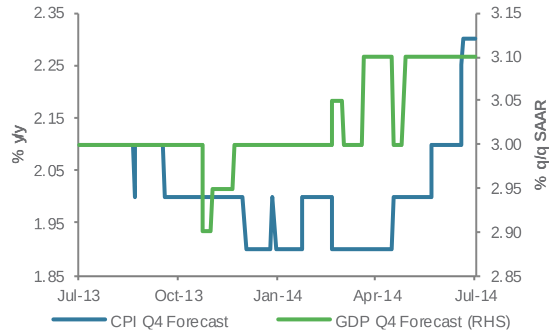
Equity and FX volatility measures



Source: VIX, JP Morgan, Bloomberg, Standard Chartered

Economic uncertainty contained: Growth expectations increasing, but so is inflation

Consensus US growth and inflation forecasts for 4Q 14



Source: Bloomberg, Standard Chartered

Asset Class	Relative Outlook	Start Date
Cash	UW	Feb-12
Fixed Income	UW	Jan-11
Equity	OW	Aug-12
Commodities	N	Nov-13
Alternatives	OW	Jun-13

Legend
Start Date - Date at which this tactical stance was initiated
OW - Overweight N - Neutral UW - Underweight
DM - Developed Markets
EM - Emerging Markets

Source: Standard Chartered

	Sub-asset Class	Relative Outlook	Start Date
Cash		UW	Feb-12
Fixed Income	DM IG	UW	Jan-11
	EM IG	N	Feb-14
	DM HY	**N**	Jul-14
	EM HY	OW	June-14
Equity	US	OW	Apr-12
	Europe	OW	Jul-13
	Japan	N	Apr-13
	Asia ex-Japan	N	Apr-14
	Other EM	UW	Aug-12
Commodities		N	Nov-13
Alternatives		OW	Jun-13

Economic and policy outlook

US hiring picks up as growth rebounds; China stabilises

- **US** companies are hiring at the fastest pace since 1999 as the economy recovered from a harsh winter. The strengthening jobs market has boosted consumption of big-ticket items such as homes and cars. However, Fed policymakers remain divided on the likelihood of a resurgence in inflation. We believe the robust job market could translate into higher wages by year-end, forcing the Fed to raise rates in H1 15, ahead of market expectations.
- **European** economic indicators were mixed over the past month. Germany reported declines in industrial production and investor confidence, while its manufacturing sector continues to face deflationary pressures. However, the latest pan-Europe business confidence survey showed a marked improvement.
- In **Emerging Markets (EM)**, **China's** economy recovered slightly to post a 7.5% expansion in Q2, indicating that targeted policy easing is helping to stabilise growth even as the government pursues broad-based reforms. **India's** inflation continued its downtrend, raising prospects for a monetary policy easing down the line. **Indonesia** elected Joko Widodo as its next president, although he faces a divided parliament.

US: Strengthening job market points to wage pressures ahead

- **Fastest pace of hiring since 1999.** The US economy created almost 1.4m net new non-farm jobs in H1, the fastest pace of hiring since H2 99. The improving job market was corroborated by a small business survey, which showed it was becoming increasingly difficult to fill open positions.
- **The robust job market is encouraging big-ticket consumption**. Existing home sales rose to an eight-month high in June, while auto sales rose to an eight-year high. We believe this is yet another sign that consumers, after years of paring down debt, are gaining confidence about the economic outlook.
- **Jobs rebound likely to fuel wage inflation.** Consumer price inflation was unchanged at 2.1% in June, after accelerating for three straight months. Although labour participation remains depressed, we believe ongoing hiring, especially by small businesses, is likely to cut slack in the labour market, forcing companies to raise salaries and fuelling inflation by year-end.

Fed: Divided on inflation outlook

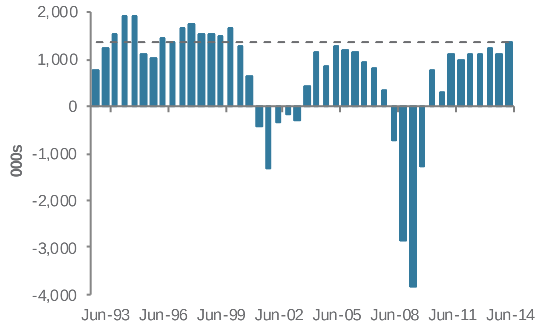
- While Fed minutes showed members agreed on ending quantitative easing by October, opinions were mixed on when the Fed should raise rates to ward off inflation. Fed Chair Yellen maintained that 'significant slack' remains in the labour market, keeping wage growth muted, while Regional Fed presidents Fisher and Bullard argued for raising rates as soon as in Q1 15, if not earlier. **We believe rising wages could force the Fed to raise rates in H1 15, ahead of market expectations.**

Europe: Germany falters, raising hopes of further policy easing

- **Europe's economic indicators are weakening**. Europe's largest economy, Germany, had remained robust. However, recent data showed industrial production and factory orders declined in May from the previous month and investor confidence fell for the seventh month in July. That said, consumer confidence is on an uptrend across the Euro area on the back of a still buoyant services sector, and the latest Euro area business confidence survey was more upbeat.

US hiring in 1H was the strongest since 1999

US total half-yearly non-farm payrolls ('000s)



Source: Bloomberg, Standard Chartered

US auto and home sales resume uptrend

US auto sales, existing home sales (m SAAR)

Source: Bloomberg, Standard Chartered

US inflation and wage pressures subdued for now

US CPI (%, y/y), hourly private sector earnings (%, y/y)

Source: Bloomberg, Standard Chartered

German firms face persistent deflationary pressures

German producer price index

Source: Bloomberg, Standard Chartered

- **Further ECB easing may be necessary.** The ECB, after cutting the benchmark rate to a record low and the deposit rate to negative, plans to introduce a long-term bank lending programme from September. With high unemployment across the Euro area, we believe stronger action may be needed over the next 12 months to reverse the ongoing weakness and reignite inflation. This could include quantitative easing aimed at weakening the EUR and bolstering exports. The recent slowdown in Germany could persuade policymakers there to back such a plan.

EM: Asia appears to have turned the corner

China: Economy stabilises after directed policy easing

- **Targeted measures boost China Q2 growth to 7.5%**. After two consecutive quarters of deceleration, China's growth nudged marginally higher in Q2, indicating the measures directed at rural and certain priority sectors were helping stabilise the economy. A measure of manufacturing activity rose to an 18-month high in July, while retail sales growth in June remained robust at 12.4%.
- **Easing inflation creates room for further easing.** We do not expect broad-based policy easing, given the authorities' ongoing efforts to shift the economy's drivers away from investment and towards consumption. However, subdued consumer inflation and deflationary pressures at the factory gate should allow policymakers to continue their targeted easing measures. The uptrend in new bank loans for the second straight month in June indicates the authorities' willingness to support growth.

Other Asia: Indian inflation declines; Indonesia elects Jokowi

- **India's consumer price inflation fell to 7.3% in June,** continuing its decline since peaking at 11.2% in November. Inadequate monsoons could reignite food inflation. However, we believe this is likely to be temporary. Falling inflation, combined with the new government's pledge to cut the budget deficit over the coming years, sets the stage for the central bank to consider easing monetary policy. Lower borrowing costs are essential for reversing three years of growth slowdown. India's trade deficit, which widened in June, needs to be watched closely.
- **Indonesia's Joko Widodo (Jokowi) needs to win over a divided parliament.** Although Jokowi's election as President has been contested by the opposition candidate, we believe his margin of victory should be sufficient for the court to reject the challenge. Jokowi's main test would be to win over an opposition-controlled parliament to push through tough reforms such as cutting subsidies. Investors will also look for Jokowi's stance on mineral exports and his ability to attract foreign investments.

Japan: Economy stabilises after April tax hike

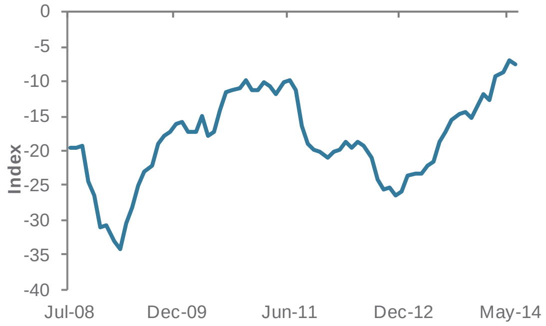
- **Japan's growth appeared to stabilise** following a sharp decline in April after the sales tax rise. The official Tankan survey showed large manufacturers and services providers were upbeat about the outlook on the economy (although smaller companies were less so). Bank lending in June accelerated for the second straight month while the current account surplus rose. We believe the central bank is likely to assess growth and inflation trends over the coming months before deciding on further policy action.

Conclusion:

The strong pickup in US hiring, if sustained, could cut the slack in the labour market and ignite wage pressures, forcing the Fed to raise rates by H1 15. The Euro area data is mixed, which could lead the ECB to embark on quantitative easing over the next 12m. China's economy appears to be stabilising after targeted policy easing.

Euro area consumers are on the mend as service sector remains healthy

Euro area consumer confidence index



Source: Bloomberg, Standard Chartered

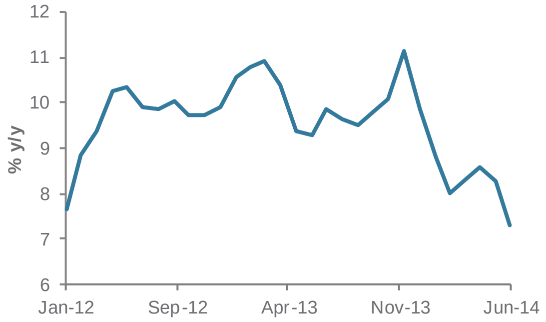
China's economy turns the corner

China economic surprises index

Source: Citigroup, Bloomberg, Standard Chartered

India's consumer inflation decelerates sharply

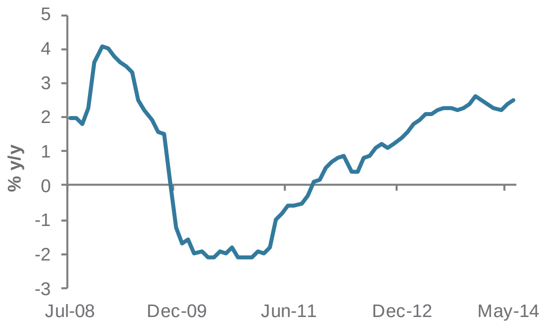
India CPI %, y/y



Source: Bloomberg, Standard Chartered

Japan bank lending accelerates for the second month

Japan bank lending (excluding Trust banks) (%, y/y)



Source: Bloomberg, Standard Chartered

Fixed Income – Underweight

- The risk of a shift in the Fed's stance remains a key factor behind our Underweight on G3 government bonds
- Our preferred bond asset classes are CNY or CNH, Asia local currency and Emerging Market High Yield (EM HY) sovereigns
- We cut Developed Market High Yield (DM HY) to Neutral (from Overweight earlier) due to a deteriorating risk/reward trade-off

G3 and EM sovereign bonds:

- **US Treasury yields have remained capped.** One likely reason for this is falling German Bund yields, which have increased demand for relatively attractive US Treasuries. However, we believe low yields are likely to be temporary. A flattening of the yield curve normally occurs at this point in the economic cycle via rising short-maturity yields. Instead, today we are witnessing falling long-end yields. In our opinion, this is inconsistent with an economy where growth and inflation risks are both increasing.
- **The timing of the first Fed rate hike remains key.** If markets are correct in fully pricing in a Fed rate hike only by October 2015, yields may rise much more gradually than we expect. However, if the Fed does indeed hike rates much earlier, as we expect, then yields may rise more rapidly.
- **We remain Overweight EM HY government bonds.** Key factors supporting this view include (i) attractive absolute yields (just under 7%), (ii) attractive value relative to DM HY, as spreads are not nearly as tight, and (iii) continued comfort with diversified exposure from a credit risk perspective. Key risks include Ukraine (though an IMF support programme is well underway) and Argentina (where risks are very well known).

Asia local currency bonds:

- **CNY or CNH bonds and Asia local currency bonds still attractive.** The big positive surprise over the past month has been the rebound in Asian currencies, which has supported returns in Asia local currency bonds. Nevertheless, we continue to believe local currency bonds in both China and the region, more broadly, remain attractive due to a combination of attractive yields (c.4%), a stable outlook on currencies and a likely lack of broad-based policy tightening in the region.

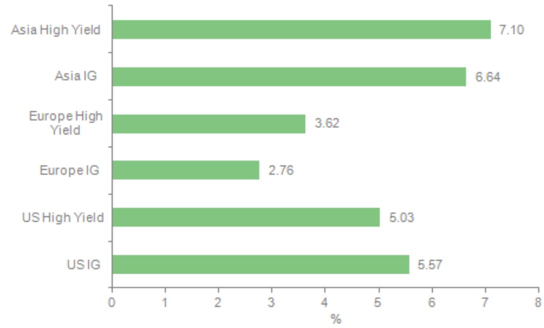
Corporate credit (USD):

- **Cut DM HY to Neutral (from Overweight).** Spreads are not far from historical tights, illustrating just how expensive the asset class is, aggregate corporate credit quality is now deteriorating and anecdotal evidence warns of a slight rise in default rates. While still-loose lending conditions argue against a significant widening of spreads, we believe the risk/reward trade-off no longer supports an Overweight view.
- **DM HY Overweight has performed strongly since inception of the call.** Since we initiated our Overweight in late September 2011, total returns have been very strong (c.41%), compared with just 5.6% for global bonds.

Conclusion

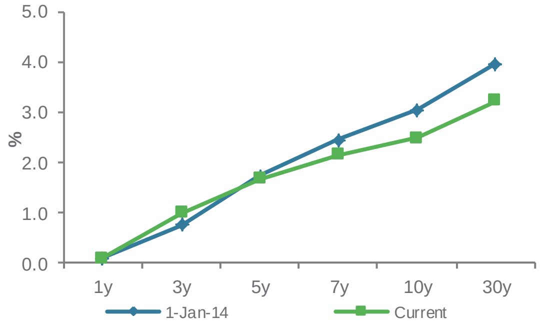
We cut DM HY to Neutral due to a deteriorating risk/reward profile. CNY, CNH, Asia local currency bonds and EM USD HY sovereigns remain our preferred bond asset classes, in order of preference. Our G3 sovereign bond Underweight remains unchanged on expectations of higher US Treasury yields in 2H 14.

Performance of fixed income YTD* (USD)



** For the period 31 December 2013 to 24 July 2014*
Source: Barclays Capital, JPMorgan, Bloomberg, Standard Chartered. Indices are Barclays Capital US Agg, US High Yield, Euro Agg, Pan-Euro High Yield, JPMorgan Asia Credit Index

US yield curve has flattened, mainly due to falling long-end yields
US Treasury yield curve (today vs. January 2014)



Source: Bloomberg, Standard Chartered

Risk-reward for DM HY bonds is deteriorating
DM HY score card

	US	Europe
Lending conditions	✓	✓
Expected defaults	✓	✓
Repayments	✓	✓
Valuations	✗	✗
Corp credit quality	✗	✗

Source: Bloomberg, Standard Chartered

CNY (onshore) bonds continue to perform well
S&P China corporate bond index (USD)

Source: S&P, Bloomberg, Standard Chartered

Equity – Overweight

- We remain Overweight equities, with Europe as our top regional pick. We expect markets to move higher steadily over time and expect volatility to remain low in the coming months.
- Early indications from the earnings season in the US and Europe are positive, which is providing some support to the asset class. We expect positive absolute returns across all regions in the coming 12 months and recommend investors diversify their allocations to minimise the impact on their portfolio of any potential short-term weakness in an individual market.
- Increasingly constructive on Asia ex-Japan on the back of stabilising Chinese data and supportive election results.
- We upgrade Indian equities to Overweight from Neutral, as two of the three catalysts we identified last month have led to the anticipated consolidation in the market. We cut Taiwan to Neutral.
- We retain our bias towards US large-cap stocks. US small cap is expected to continue to underperform as a result of less attractive valuations and monetary conditions over the next 12 months.
- Asian political uncertainty is reducing, while global political uncertainty remains elevated.

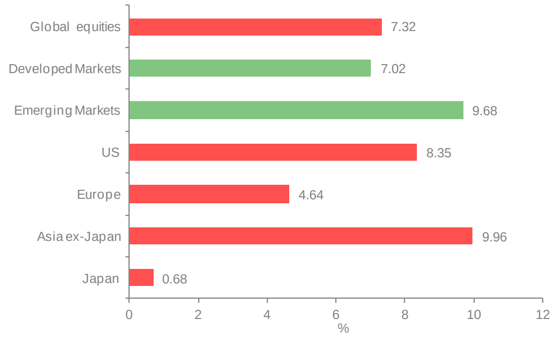
Developed Markets (DM) – EU/US earnings season constructive

- **Remain Overweight European and US equities**. We continue to be Overweight European and US equities based on our estimated returns for the two regions. Europe continues to be our preferred region, offering the highest returns. We are neutral Asia ex-Japan; however, we are becoming progressively more constructive on the region.
- **Early indications from US and EU 2Q earnings are positive.** Of the 217 companies that have reported Q2 earnings in the US, almost 80% have beaten expectations. The trend, at this early stage in the earnings season, is observable across all sectors, except consumer staples. While no clear pattern is observed in European corporate earnings, we note that consensus earnings expectations are more optimistic, forecasting a 12m forward EPS growth of 14.5%, compared to 10.5% in the US.
- **We remain biased towards US large cap.** Small cap valuations remain elevated in absolute and relative terms to large cap. Small cap has tended to outperform during times of low volatility. While it may be early to call an end to small caps' run of outperformance, the steady rise in small cap/large relative valuations, suggest the risk-reward is not compelling.

Emerging Markets (EM) – China data turning supportive

- **We are increasingly constructive on Asia ex-Japan,** one of the few remaining regions offering attractive valuations. Improving global growth is expected to support Asia's exports and earnings, which have disappointed over the past three years. The stabilisation of relative earnings between EM (c.70% from Asia) and DM may continue to support Asia's recent outperformance. The upcoming China H1 14 earnings season in August will be critical.
- **Asia's economic surprise index, a proxy for data surprises relative to market expectations, continued to improve over the month.** The index has clearly recovered and is on the verge of becoming positive driven by an improvement in Asia's trade data and China's economic data.

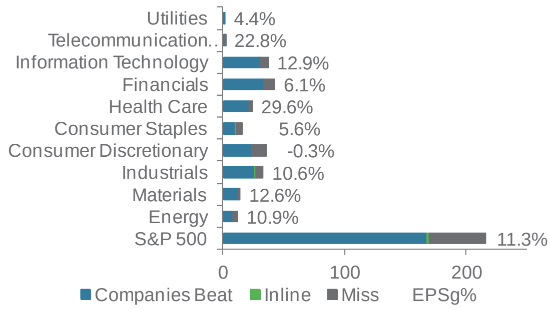
Performance of equity markets YTD* (USD)



** For the period 31 December 2013 to 24 July 2014*
Source: Bloomberg, Standard Chartered. MSCI Indices are USD total return

US 2Q earnings have exceeded expectations so far

S&P 500 2Q earnings surprises (by number of companies) and earnings growth (by sector)



Source: Bloomberg, Standard Chartered

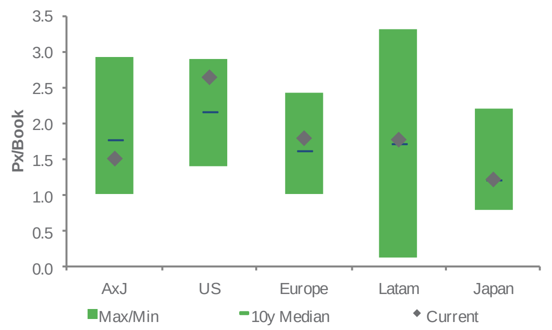
Large-cap stocks have outperformed YTD

Ratio of MSCI US and Europe large vs. Small cap

Source: MSCI, Bloomberg, Standard Chartered

Valuations for Asia ex-Japan are attractive relative to other regions

Forward P/B ratios by regions (current vs. median)



Source: MSCI, Bloomberg, Standard Chartered

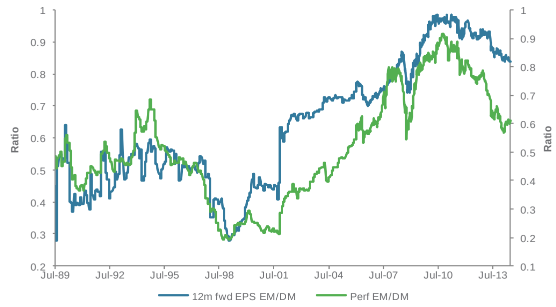
- **Raising India to Overweight.** At the time of our last Global Market Outlook, we flagged a potential future change in our India allocation from Neutral. We cited three catalysts that would lead us to review the recommendation. The three factors we cited were: a rise in oil prices, a budget disappointment and signs of local net buying. The latter two factors have been triggered, leading us to increase our allocation to the market to Overweight.
- **Taiwan reduced to Neutral.** We are reducing our allocation to Taiwan to Neutral from Overweight to compensate for the increased allocation to India. Taiwan has outperformed Asia ex-Japan by approximately 4.5% since we initiated our call in mid-February this year. We continue to like Taiwan and, particularly, the technology sector. Nevertheless, valuations have become stretched and there is a risk that investors may reduce allocations to Taiwan in favour of other markets which offer more attractive relative valuations. These could see a catch up in their relative performance in 2H 14.
- **Asian political uncertainty reducing.** The announcement by the Indonesian election commission that Jokoo Widodo won a clear victory in the Presidential election, capturing 53% of the vote compared to 47% by his rival Prabowo Subianto, should help ease uncertainty in the country. Add in positive sentiment towards the BJP's victory in India, and political uncertainty in the region has clearly decreased.
- **Global political uncertainty remains elevated.** While uncertainty in Asia is reducing, uncertainty at the global level remains elevated. Developments in Ukraine and in Syria/Iraq continue to have the potential to increase global uncertainty and cause a spike in risk aversion. Further, key EM elections in the coming 12 months include Turkey on 10 August and Brazil in October 2014. It is clear that politics continues to have the potential to cause upsets for markets. Of the four events we are monitoring, the expansion of the Islamic State of Iraq and Syria (ISIS) in Syria/Iraq has the greatest potential to upset markets. In contrast to Russia, which has become more willing to seek a solution in Ukraine possibly due to the threat of increased sanctions, the world community has no such leverage over ISIS.

Conclusion

We remain Overweight equities, with Europe forecast to generate the highest returns globally in the coming 12 months. We remain neutral on Asia ex-Japan, albeit with an increasingly constructive view. Within Asia, we have increased India to Overweight from Neutral and reduced Taiwan to Neutral

Earnings growth differential appears to be stabilising between DM and EM

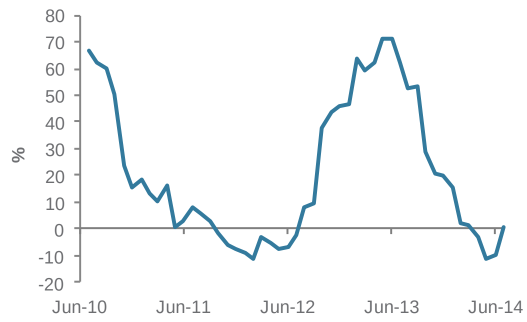
MSCI EM vs. DM – 12m forward EPSg and performance



Source: MSCI, Bloomberg, Standard Chartered

Positive credit growth could support Chinese equities

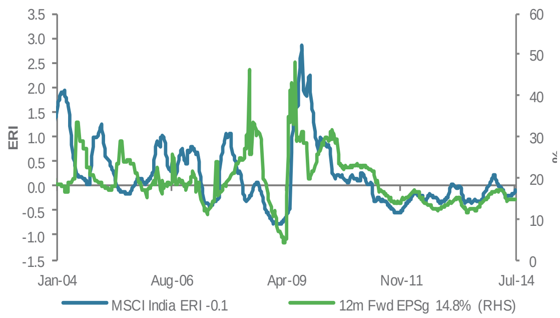
China total social financing, y/y % (12mma)



Source: Bloomberg, Standard Chartered

Earnings revisions are turning positive

MSCI India earnings revision index and 12m EPS growth



Source: MSCI, Bloomberg, Standard Chartered

Commodities – Neutral

- We maintain a Neutral view on commodities.
- While we remain cognisant of the upside risks of inflation to gold, we believe an end to Fed QE purchases and an eventually stronger USD are negative for gold.
- Energy remains our preferred sub-asset class. Oil prices have fallen to the bottom of their recent range, improving their risk/reward trade-off.

We remain Underweight gold. The precious metal's lack of response to the bounce in equity volatility and geopolitical risks remains disappointing. While the chart on the right illustrates some evidence of a correlation (albeit limited) with a rise in volatility, we believe the rising opportunity cost of holding gold (a non-yielding asset) in the face of continued positive returns in equity and bond markets is likely to be the dominant force.

The one risk we are monitoring more closely is from rising inflation. As we highlighted last month, there is some evidence rising inflation expectations could pose upside risks for gold. We do not believe the magnitude is sufficient as yet to be a source of concern, but we are watching this closely.

We remain Overweight energy. Brent oil prices have dropped back sharply to the bottom of a USD 104-111 sideways range due to the lack of escalation in key geopolitical risks. The violence in Iraq has not spread to the oil-producing south so far, while Libya surprised to the upside by re-opening energy-exporting terminals.

The fall back in energy prices means the risk/reward profile has now improved, in our view. Downside risks are likely limited to the bottom of the range, while continued demand growth and uncertainty in many key oil-supply regions (including Russia; due to Ukraine-related risks) mean upside risks remain present. Current prices offer attractive levels to build exposure, in our opinion.

We remain Neutral on industrial metals. The normalisation of market positioning for many key metals may now lead to a significant rise in long net positions. We believe this poses the risk of prices overshooting to the upside in the short term; however, given positioning is now not far from levels usually signifying a peak, we believe any further upside is likely to be limited.

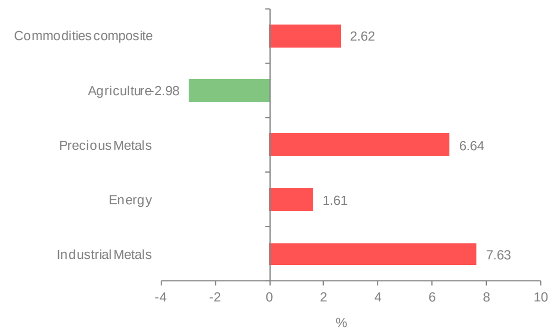
Longer term, our focus remains on signs of strengthening demand, particularly in China (which is still largely lacking) and onshore Chinese inventories (which remain elevated), both of which support our Neutral stance.

We remain Neutral on agricultural commodities. Prices continued to slump over the past month amid a lack of upside triggers. Our focus remains on the potential effect of El Nino weather patterns. While early indications, such as Monsoon rains in the Indian subcontinent, have been somewhat encouraging, we remain on watch for potentially greater volatility in agricultural prices over the next few months.

Conclusion

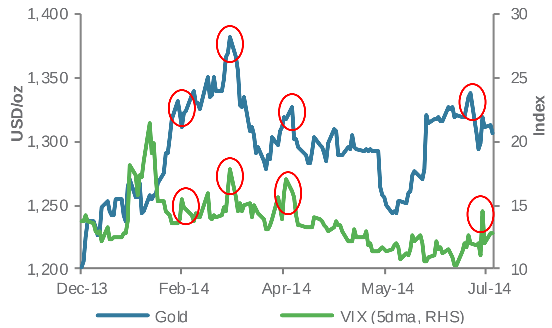
We retain our Neutral stance on commodities. We continue to believe gold prices have room to fall further from here. Oil offers an attractive risk/reward trade-off at current levels. Chinese policy and onshore inventories remain key to the outlook on industrial metals.

Performance of commodities YTD* (USD)



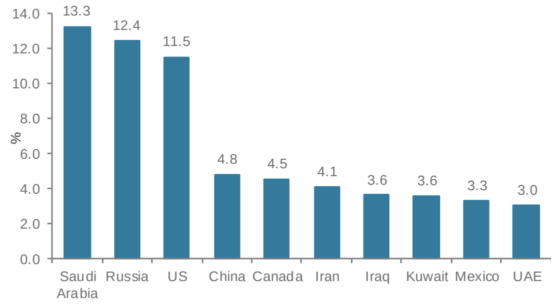
** For the period 31 Dec 2013 to 24 July 2014*
Source: DJUBS, Bloomberg, Standard Chartered
DJUBS, DJUBS Agri, DJUBS Precious metals, DJUBS Energy, DJUBS Industrial metals

Rise in equity volatility is not helping gold much
Gold spot vs. VIX index



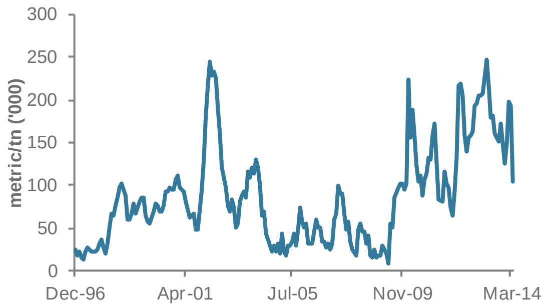
Source: Bloomberg, Standard Chartered

Iraq remains a key oil producer in a global context
Top 10 crude oil producers (% of 2013 global production)



Source: BP Statistical Review 2014, Standard Chartered

China onshore copper inventories have eased somewhat, but still remain elevated
Shanghai Copper inventories, '000 metric tons



Source: Bloomberg, Standard Chartered

Alternative Strategies – Overweight

- We remain Overweight alternative strategies, as they offer exposure to equities, our preferred asset class.
- We believe alternative strategies may be especially attractive in an environment where volatility is low and equity markets have now risen for a long period without any meaningful pullback. A diversified approach offers attractive exposure by itself, but equity long/short offers an alternative way of gaining exposure to equities, our preferred asset class.

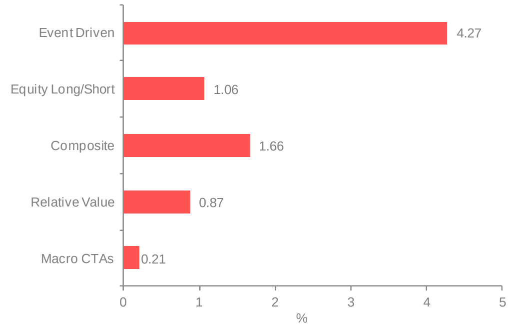
We continue to see equity long/short strategies as attractive for investors who are uncomfortable with accepting the volatility associated with long-only exposure. These strategies can be interesting for investors wanting to raise their equity exposure to benefit from what we view to be an attractive long-term trend but are uncomfortable with the volatility associated with a long-only position. Recent performance has been along expected lines: correlation with global equities has been positive, but volatility has been lower.

Protection against any equity volatility, stock correlations and acquisitions activity are key factors leading to our Overweight. We continue to expect equities to outperform over the next 12 months. However, we believe alternative strategies can help offer some protection against any short-term volatility. We also note stock correlations remain low, suggesting a more positive environment for equity long/short strategies. Sharply rising number of merger and acquisitions (M&A) activity is also positive both for alternative strategies more broadly, and for equity long/short strategies, in particular.

Conclusion

We maintain our Overweight on alternative strategies. We favour diversified exposure and equity long/short strategies to ensure portfolio diversification and lower volatility relative to long-only equities.

Performance of alternative strategies YTD* (USD)



** For the period 31 December 2013 to 24 July 2014*
Source: HFRX, Bloomberg, Standard Chartered
HFRX global hedge, HFRX equity hedge, HFRX event driven, HFRX relative value, HFRX macro/CTA

Foreign Exchange

USD: We expect appreciation over the medium term

We expect the USD to continue to appreciate, although we expect most of this strength to come against the EUR and JPY. Continued improvement in US labour market data is likely to push the Fed to hike rates earlier than current market expectations, in our view. While interest rate differentials, one of the major drivers of USD strength, have just begun to turn in favour of the USD, we believe they will become more pronounced once higher US interest rate expectations are priced in. In addition, USD undervaluation against most major currencies is also likely to provide a supportive backdrop.

EUR: We expect depreciation over the medium-term

We expect the EUR to continue to trend lower on the back of monetary policy divergence with the US. Recent economic data suggests activity remains lacklustre at best, though business confidence rebounded following the most recent ECB easing. We believe there is a reasonable likelihood this may push the ECB to ease more aggressively. The EUR continues to trade higher than interest rate differentials imply as a result of capital flows and external balances. We expect these to be less supportive going forward, as European debt becomes less attractive.

JPY: We expect depreciation over the medium term

The JPY has continued to trade in an extremely tight range for the past few months. This raises the risk that any breakout of this range is

Short term

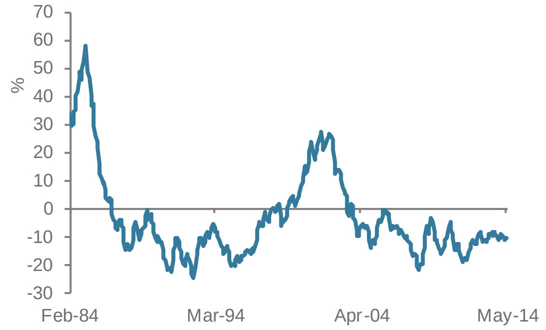
refers to a horizon of less than 3 months

Medium term

refers to a time horizon of 6 to12 months

USD undervalued by about 10% with respect to dollar index constituent currencies

USD over/under-valuation



Source: Bloomberg, Standard Chartered

likely to be disproportionate in size, in our view. We believe any such breakout is more likely to be in favour of JPY weakness. The US-Japan 10-year yield differential has been largely flat over the last few months. However, a rise in US rates means the differential will likely move in favour of the USD, highlighting that JPY weakness is not dependent on further Bank of Japan (BOJ) easing alone, as monetary policies are still likely to diverge considerably.

GBP: We remain medium-term Neutral

We remain neutral on the GBP as we believe most of the positives may have been priced in its recent rally. Most UK economic indicators have surprised to the upside over the past year, while the recent statement by the Bank of England (BOE) governor indicates increased willingness to consider policy tightening. However, we do not see interest rate differentials being supportive of further GBP gains if US rates rise as well. The August inflation report will be key, in our view.

Given the risks, we prefer to take exposure on the GBP against the EUR, where monetary policy divergence is more visible in relative interest rates (see chart below).

AUD: We remain medium-term Neutral

We remain medium-term Neutral and expect the currency to trade in a broad range. While the AUD continues to trade higher than that implied by interest rate differentials and commodity prices, demand for Australia's AAA-rated bonds and low volatility continue to support the AUD. As a result, portfolio inflows are likely to offset any outflows from declining direct investment. However, recent statements by Reserve Bank of Australia (RBA) policy makers suggest a low tolerance for an elevated currency level, although it is likely the AUD would have to rise significantly for the central bank to take concrete action.

SGD: We remain medium-term Neutral

We expect the SGD to remain range-bound medium term. Recent economic activity and inflation seems to have cooled somewhat. However, given a pickup in the global economy and trade, we do not see significant downside risk. Monetary authorities are likely to maintain a tightening bias, though we expect most SGD strength to come against non-USD currencies in Singapore's trade basket.

Other Asia ex-Japan: we remain medium-term Neutral

We expect further appreciation in the CNY. Policymakers are likely to be increasingly comfortable with gradual currency strength given (i) the band widening has succeeded in raising volatility and discouraging speculators, and (ii) improvement in economic data. A continued pick-up in exports and reserve accumulation should be supportive of a stronger currency, in our view.

Elsewhere in Asia ex-Japan, we remain Neutral but prefer currencies strongly linked to improving global growth and strong balance of payment fundamentals. In this regard, KRW and TWD continue to stand out. Improving growth prospects in China further provide a favourable backdrop for these currencies.

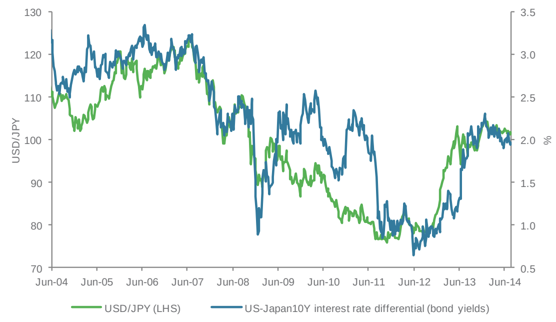
We are also increasingly constructive on the INR following sharp improvements in external balances and FX reserves. Widodo's Presidential election win in Indonesia is also reform-positive, though prospects of a hung parliament, large foreign holding of debt as well as a sizeable current account deficit make the IDR more susceptible in case of any major Emerging Market currency sell-off.

Conclusion

We remain medium-term bullish on the USD and CNY and remain bearish on the JPY and EUR. We favour KRW and TWD in Asia.

JPY: increase in US 10-year rates may drive USD/JPY higher

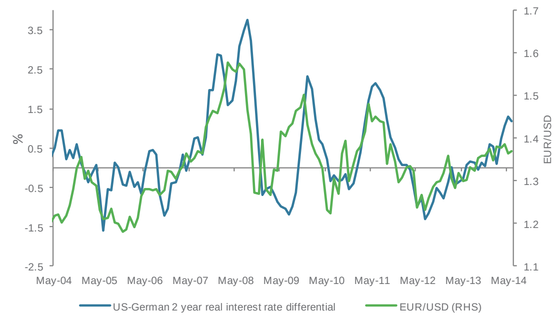
US-Japan 10-year interest rate differentials



Source: Bloomberg, Standard Chartered

EUR: real interest rate differentials to fall as US yields increase

US-German 2-year real interest rate differentials and EUR/USD



Source: Bloomberg, Standard Chartered

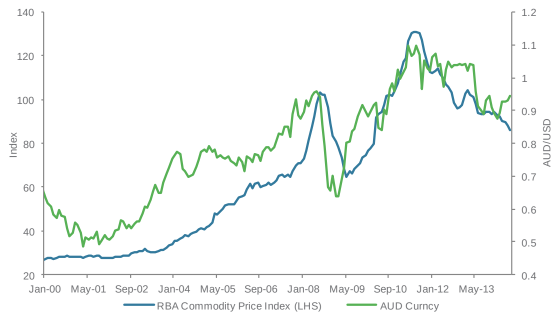
GBP: monetary policy differential between UK and the EU reflected in GBP strength vs. EUR

UK-EU 2-year interest rate differentials vs. GBP/USD

Source: Bloomberg, Standard Chartered

AUD: declining commodity prices to cap AUD strength

RBA Commodity price index and AUD/USD



Source: Bloomberg, Standard Chartered

Investing for Income Generation: An update on the multi-income portfolio

- We continue to believe a diversified approach to income investing remains a key theme
- Income investors should remain vigilant about interest rate risk as discussion around the first Fed rate hike takes centre stage
- We stay A.G.I.L.E in our income portfolio by reducing allocation to DM HY in favour of CNY corporate bonds and leveraged loans

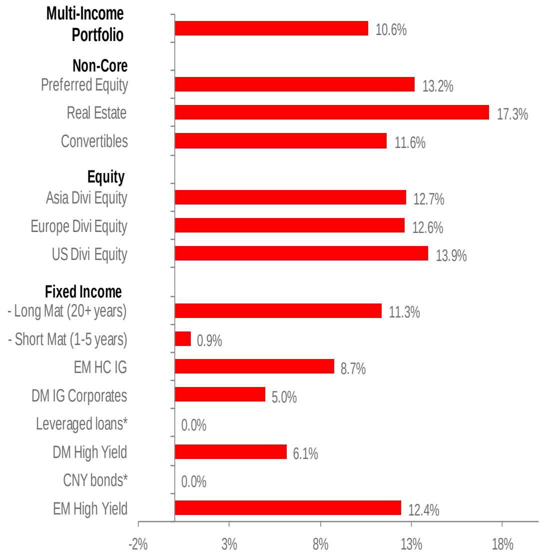
In our 2014 Outlook publication, we highlighted multi-income investing as a key theme. Given the low-interest-rate environment, investors were urged to explore a diversified portfolio of income-generating assets that included investments beyond traditional fixed income. Accessing multiple sources of yield would provide the income stability, much prized by this class of investors. We also highlighted the importance of being A.G.I.L.E with income-related assets. Given we are slightly past the halfway mark in the year, it is a good time to evaluate the relative attractiveness of assets in the income portfolio and make changes as necessary.

A strong start for the multi-income portfolio

Before discussing changes to the portfolio, it is informative to review portfolio performance. The overall portfolio is up 10.6% since our 2014 Outlook publication. We've seen strong performance from all three major areas within the portfolio – high dividend equities, diversified fixed income and non-core income. While non-core income was included for its diversification benefit and attractive yield, the strong capital gains in this area have provided a welcome boost to performance. Global real estate has been the outstanding asset class in non-core income with an inception-to-date return of 17.3%.

A review of equity and fixed income performance displays some interesting trends. High dividend equity has delivered positive absolute performance, with Developed Markets (DM) outperforming Emerging Markets (EM), in line with our view. We've also seen strong performance from DM High Yield (HY) and DM Investment Grade (IG) corporates (relative to G3 sovereigns), our preferred sectors within the fixed income space. Of particular surprise has been strong performance from EM asset classes, which have outperformed other fixed income assets within our portfolio. The price move could be driven by reducing risks, as highlighted by improving macro indicators such as current account and trade data

Performance of multi-income portfolio



Source: S&P, JPMorgan, Barclay Capital, Citigroup, MSCI, SPDR, FTSE, IShares, Bloomberg, Standard Chartered Bank

Performance from 16 December (date of Outlook 2014 publication release) to 24 July 2014

Indices are Barclays Global HY TR unh USD, JPMorgan EMBI HY, Citigroup WBIG Corp USD, JPMorgan EMBI IG, Citigroup WBIG Sovereigns, Citigroup WBIG 1-5y USD, Citigroup WBIG 20+y USD, MSCI North America High Divi TR, MSCI Europe High Divi USD, MSCI EM Asia High Divi TR, SPDR Barclays convertible ETF, FTSE NAREIT global index TR USD, IShares preferred stock ETF ,S&P/Citic China Corporate Bond, S&P/LSTA US Leveraged loan 100 index

Estimated interest rate sensitivity of fixed income assets
Expected total returns (12m) based on change in yields (%)

	Asia LCY	Asia HY Corp	Global HY	EM HC HY	EM HC IG	G3 Sov	DM IG Corp	CNY bonds Corp	CNH bonds
Yield to Maturity	**3.8%**	**7.1%**	**5.4%**	**8.1%**	**4.8%**	**1.3%**	**2.9%**	**5.9%**	**4.0%**
Duration*	**6.5**	**4.6**	**4.1**	**5.5**	**7.7**	**6.9**	**7.1**	**3.5**	**2.7**
Change in yield -1.50%	13.6%	14.0%	11.5%	16.3%	16.3%	11.7%	13.5%	11.0%	8.0%
-1.00%	10.4%	11.7%	9.4%	13.6%	12.5%	8.2%	10.0%	9.3%	6.7%
-0.50%	7.1%	9.4%	7.4%	10.8%	8.6%	4.8%	6.4%	7.6%	5.4%
0.0%	3.8%	7.1%	5.4%	8.1%	4.8%	1.3%	2.9%	5.9%	4.0%
0.50%	0.6%	4.8%	3.3%	5.3%	0.9%	-2.2%	-0.7%	4.1%	2.7%
1.00%	-2.7%	2.5%	1.3%	2.6%	-2.9%	-5.6%	-4.2%	2.4%	1.4%
1.50%	-6.0%	0.2%	-0.7%	-0.2%	-6.8%	-9.1%	-7.7%	0.7%	0.1%

Source: JPMorgan, Barclays Capital, Citigroup, Bloomberg, Standard Chartered

**Duration is an approximate measure of interest rate sensitivity; LCY = local currency, HC = hard currency*

Staying A.G.I.L.E. within fixed income

As highlighted in the Fixed Income section, we have cut our Overweight on DM HY due to a deteriorating risk/reward profile. Consistent with this view, we reduce our allocation to this asset class within the income portfolio. We re-allocate the proceeds to CNY corporate bonds and leveraged loans. CNY bonds remain one of our preferred asset classes given attractive yields (around 5.9% YTM) and likely currency appreciation. The low correlation with global equities, as highlighted during previous risk-off environments such as the May 2013 “taper-tantrum”, suggests these bonds also help to significantly diversify risk.

We also initiate a small allocation to the leveraged loan asset class. This asset class shares a number of characteristics with DM HY. However, incrementally stronger investor protection in the event of a default, relative to DM HY, and a floating rate arguably brings a more defensive risk profile to the income portfolio.

Interest rate risk a key topic.

As we approach the end of quantitative easing, discussions around the timing of the first Fed rate hike are likely to take centre stage. If markets are correct in fully pricing in a Fed rate hike only by October 2015, yields may rise much more gradually than we expect. However, if the Fed does indeed hike rates earlier, as we expect, then yields may rise more rapidly. Interest rate sensitivity is an issue that cannot be ignored. It is useful to measure the impact of a change in yields on various fixed income asset classes within our multi-income portfolio.

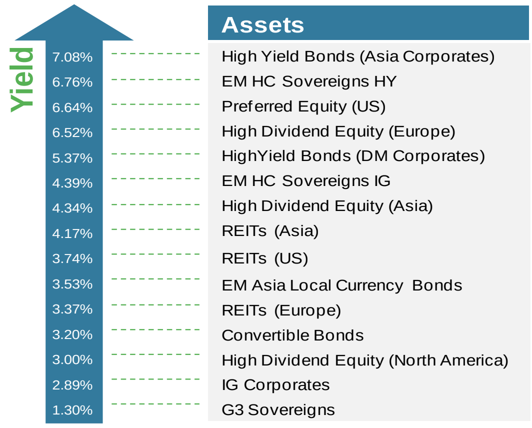
We use a simple analysis combining yield-to-maturity and interest rate sensitivity to understand this impact. The shaded region in the table on page 12 represents the range of probable outcomes, in our opinion. For a number of asset classes, the yield available may not be sufficient to offset the capital loss arising from a rise in yield, resulting in negative total returns.

In the G3 sovereign bond space, the mark-to-market loss might be smaller. However, the lower yield on offer means the buffer against capital loss maybe insufficient. Asset classes, such as EM Hard currency HY and CNY bonds are partially shielded from the rise in yields by their above-average coupon. This yield buffer, combined with continued comfort with the credit risk, leads us to be Overweight on these asset classes.

We continue to believe investors can generate positive total returns by investing in a diversified portfolio of income-generating assets. An approach that focuses on multiple sources of income in key areas such as high dividend equity, diversified fixed income and non-core assets should continue to generate stability of yield for the income investor.

Broaden the mix – a range of yields on offer beyond fixed income

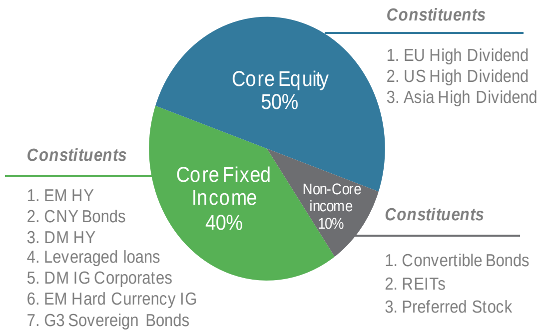
Yield to maturity/dividend yield (%)



Source: JPMorgan, Barclays Capital, Citigroup, SPDR, FTSE, IShares, MSCI, Bloomberg, Standard Chartered

Focus on diversified income sources

Combination of core and non-core income assets



Source: Bloomberg, Standard Chartered

As of 24 July 2014

For illustrative purposes only. This diagram shows a multi-asset income asset allocation for a moderate risk profile only. Different risk profiles may produce significantly different asset allocation results. This example is provided for general information only and does not constitute investment advice, offer, recommendation or solicitation. It does not take into account the specific investment objectives, needs or risk tolerances of a particular person or class of persons and it has not been prepared for any particular person or class of persons.

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