Global Market Outlook macro strategy | 02 March 2015

This reflects the views of the Wealth Management Group

Equities get a lift from central banks

The two months since the publication of our Outlook 2015 have been eventful, led by unexpected policy easing in many countries, while US economic data has remained strong

These events reinforce our conviction in equities and income assets. European equities, in particular, are likely to be key beneficiaries of the European Central Bank's (ECB) quantitative easing (QE) programme. Income assets are also likely to stay well-supported, particularly high-dividend-yielding equities and Chinese and Indian local currency bonds.

- **Central banks ease, intensifying divergence.** While this is long-term USD-positive, the ECB's QE, in particular, is a key support factor for global and European equities. The focus now shifts to the likely timing of a Fed rate hike following strong jobs market data – we believe this is likely to happen over the summer, but markets are not convinced. Greece-related negotiations are a risk, but it appears increasingly likely an agreeable middle ground will be reached.
- **Volatility is likely to continue for longer.** This has been a rising trend across equity, bond and currency markets since late last year. However, (a) this is not unusual in the run-up to a Fed rate hike, and (b) this is not necessarily negative for asset markets. We believe, instead, that volatility throws up its own set of investment opportunities, such as covered calls.

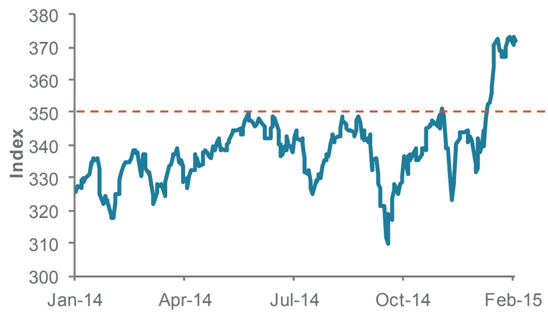
Implications for investors

- **Equities likely to remain well-supported.** We remain in a seasonally strong period for equities, and continued global liquidity is a key source of support. European equities (FX-hedged) currently have the most positive catalysts. We remain bullish on US equities over the next 12 months, but see fewer tailwinds than we do in Europe, given short-term concerns over US earnings growth and a likely move to less-supportive US monetary policy settings. We expect positive returns in Asia and are bullish on four markets: China, India, Taiwan and Thailand.
- **Use any volatility to your advantage.** For equity investors, this would mean using pullbacks to buy, while both equity and currency investors can use rises in implied market estimates of future volatility to generate attractive yields.
- **Income basket performance likely to continue.** Covered calls, high-dividend-yielding equities and China/India local currency bonds look particularly attractive today.

Contents

European equities have broken above their trading range following ECB QE

Euro Stoxx 50 index



Source: BCA Research, Standard Chartered

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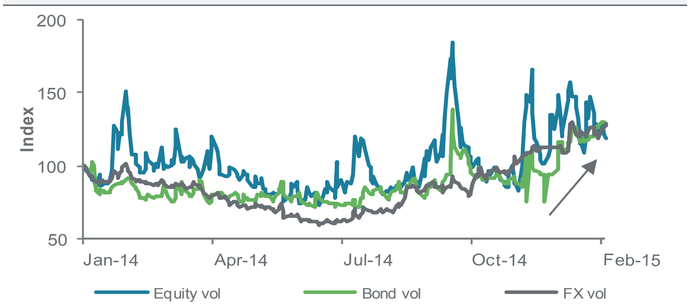
Volatility has been trending up across asset classes

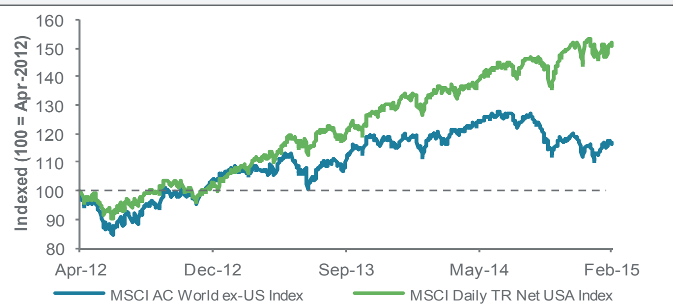
VIX, MOVE and JPMorgan Global FX Volatility indices



Source: Bloomberg, Standard Chartered

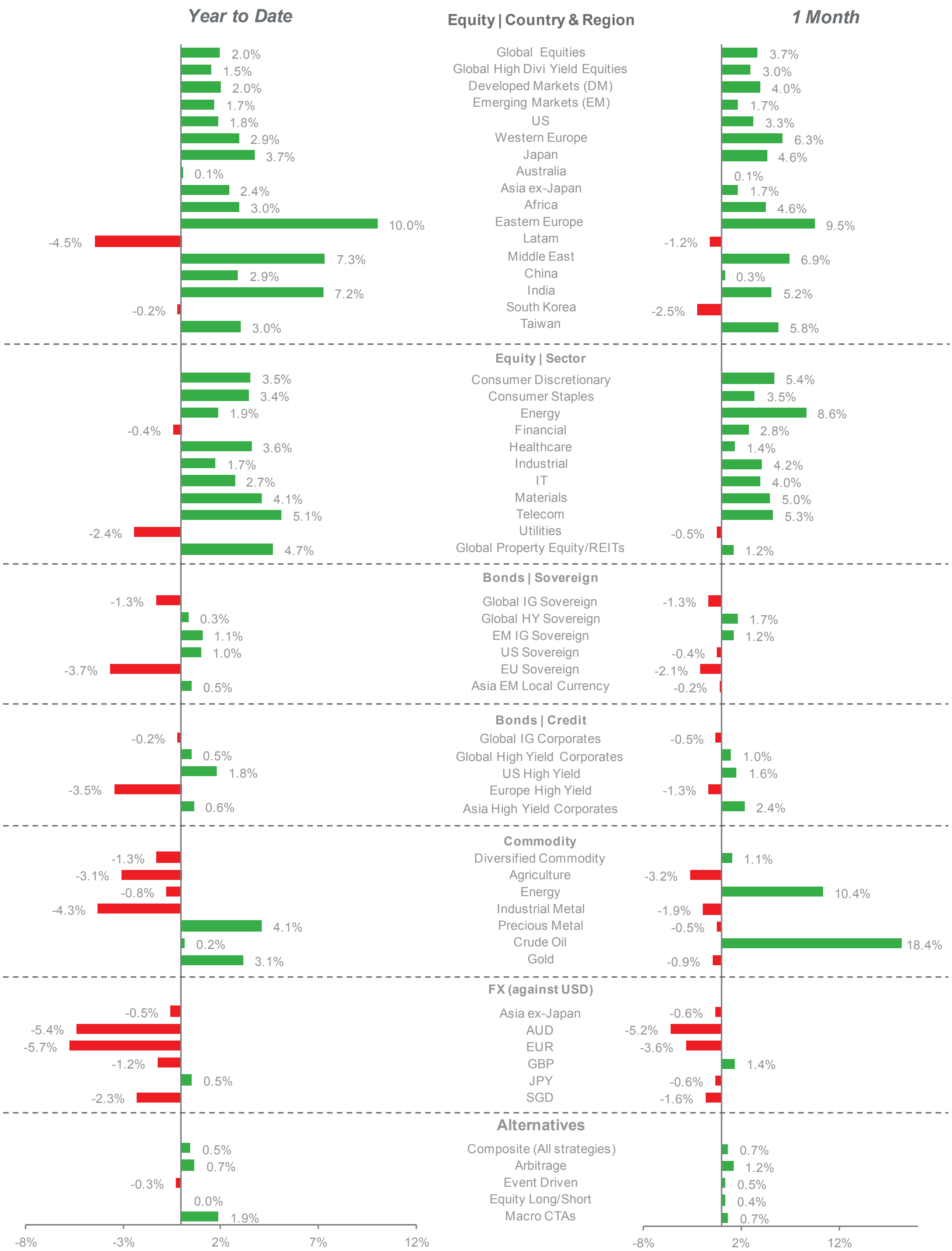
US equities have outperformed since we went Overweight

US equities vs. global equities ex-US, indexed total returns



Source: 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 December 2014 to 12 February 2015 and 1-month performance from 12 January to 12 February 2015*

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

Investment Strategy

- **Many central banks outside the US unexpectedly eased policy. We believe this is supportive of risk assets in general and European equities in particular.**
- **Policy divergence is likely to intensify as the Fed rate hike debate becomes more active, which is expected to lead to increased volatility. This will likely create opportunities for buying equities on dips or strategies involving taking advantage of volatility spikes to enhance yields in both equity and currency markets.**
- **Policy divergence is also likely to drive the USD higher over the medium term, although it is over-extended short term.**

Central bank easing, particularly the European Central Bank's (ECB) much-awaited start to quantitative easing (QE), is a key positive for risk assets. This announcement is likely to provide European equities with the catalyst they need to begin outperforming, particularly since the weaker EUR has a significantly positive impact on earnings. Also, a combination of QE efforts from both the Bank of Japan (BoJ) and the ECB mean global liquidity is likely to remain ample even if the Fed starts raising rates, a key positive for global equity markets outside Europe as well.

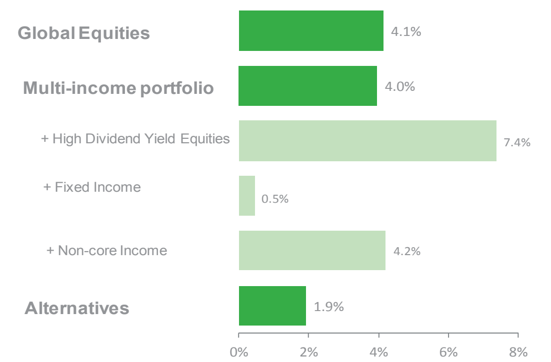
Central bank actions intensify divergence, which is USD-positive. A number of central banks outside the US have unexpectedly eased policy since the beginning of the year. This is set to intensify divergence in policy as the focus shifts increasingly towards the likely timing of a Fed rate hike. The USD is likely to benefit, short-term pullbacks notwithstanding.

Implications for investors:

- **We remain in a seasonally strong period for equities.** We are mindful that some indicators of short-term stress for US equities have strengthened; however, this contrasts with the fact that we are in a seasonally strong period for equities and that bouts of volatility are often difficult to time and can be short-lived. Seasonality and liquidity are also likely to support Asian equities and we are bullish on four markets: China, India, Taiwan and Thailand.
- **European equities attractive.** While the long-term supports for European equities remain in place, we believe ECB QE will act as a catalyst. We remain Overweight on a currency-hedged basis. We remain bullish on US equities as well, but see fewer tailwinds than we do in Europe.
- **Divergence, loose monetary policy offer opportunities for income generation.** Key beneficiaries from recent market and policy action include covered calls, high-dividend-yielding equities and Chinese and Indian local currency bonds.
- **Use any volatility to your advantage.** Equity investors could use pullbacks to buy, while both equity and currency investors can take advantage of volatility spikes to enhance yields.

Bullish W.I.D.E.N. themes have had a decent start to 2015

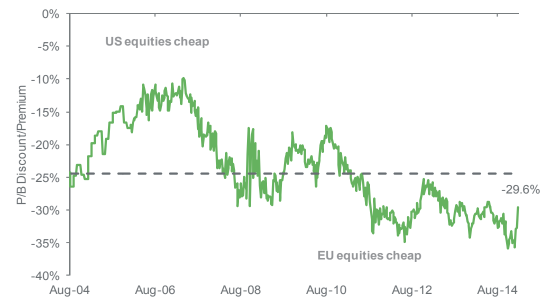
*W.I.D.E.N. performance since Outlook 2015 was published**



** For the period 12 December 2014 to 12 February 2015*
Source: Bloomberg, Standard Chartered
** Income basket is as described in the Outlook 2015: A Year to W.I.D.E.N. Investment Horizons, Figure 60)*

European equities still offer significant value relative to US equities. ECB QE may provide the catalyst

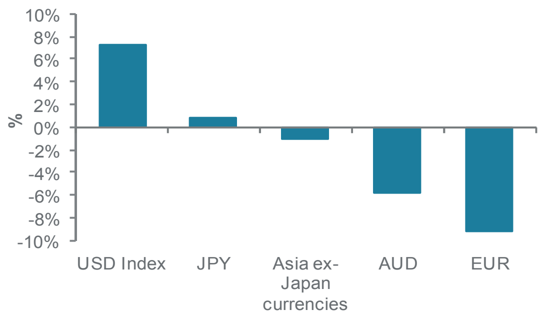
US vs. European equities relative valuation



Source: DataStream, Standard Chartered

USD has strengthened considerably since we published our Outlook 2015

Key currencies vs. USD



Source: Bloomberg, Standard Chartered

Asset Class	Relative Outlook	Start Date
Cash	UW	Feb-12
Fixed Income	UW	Jan-11
Equity	OW	Aug-12
Commodities	UW	Dec-14
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	OW	Dec-14
	DM HY	N	Jul-14
	EM HY	N	Dec-14
Equity	US	N	Feb-15
	Europe	OW*	Jul-13
	Japan	OW*	Nov-14
	Asia ex-Japan	UW	Dec-14
	Other EM	UW	Aug-12
Commodities		UW	Dec-14
Alternatives		OW	Jun-13

**Currency-hedged*

Economic and policy outlook

More than a dozen central banks have eased policy this year. The European Central Bank (ECB) is set to execute its unprecedented bond purchase plan from March. We expect more easing in China, Japan, India, and possibly in Canada and Australia. The Fed stands out – we expect it to start raising rates this summer.

- **The ECB's stimulus plan helps revive confidence.** The central bank's government bond purchase plan starting in March allows it to potentially keep buying government and private sector bonds until inflation returns close to its 2% target. We believe the plan will further weaken the EUR, in the process boosting exports and inflation expectations, the latter by driving up the cost of imports.
- **Japan is likely to add stimulus as inflation expectations remain subdued.** Although the economy is likely to have returned to growth in Q4 2014 and nominal wages rose, real wages after adjusting for inflation declined last year. We expect the Bank of Japan (BoJ) to add to its bond purchase targets as inflation expectations remain subdued.
- **Falling inflation allows Emerging Markets (EM) to ease policy.** China, India, Russia, Turkey and Singapore all eased monetary policy this year, joining the Euro area, Canada and Australia. We expect further easing in most EMs as low inflation allows central banks to focus on boosting growth.
- **The Fed is likely to start raising rates by the summer.** A sustained pace of strong job creation suggests that pressure is growing on the Fed to start raising rates from record-low levels. Although a strong USD is weighing on exports, consumers are benefitting from improving job prospects and lower energy costs. We expect the Fed to start raising rates by September.

US: Strong job market, low energy costs boost consumption

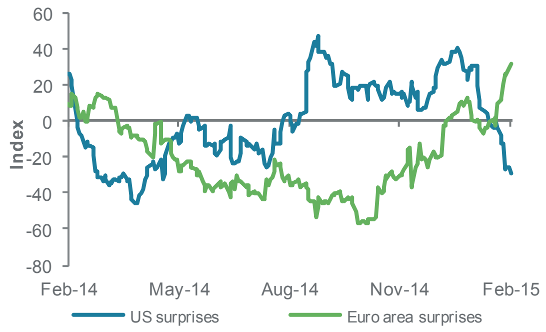
- **Robust US hiring in January.** US employers added 257,000 jobs in January, and a million over the past three months, helping sustain last year's fastest pace of hiring since 1999. Job openings are at a 14-year high, suggesting strong job creation in Q1 2015.
- **Wage growth picks up.** Although the unemployment rate rose marginally in January from a 6-1/2-year low, average hourly earnings rebounded, suggesting the labour market is tightening. Rising wages are attracting more Americans to return to the job market, limiting further acceleration in wage pressures for now.
- **Strongest consumer confidence since 2007.** The robust job market and decline in energy prices have helped boost household income and consumer confidence. This is driving sales of big-ticket items, such as autos and homes, to multi-year highs.
- **Strong USD weighing on manufacturers**. A decline in orders for capital goods and waning confidence, reflected in a survey of manufacturing sector purchasing managers, albeit from high levels, suggest the USD's gains may be starting to hurt exports.
- **Fed likely to lift rates by the summer due to wage pressures.** We believe the robust job market will put upward pressure on wages, setting the stage for a rate hike by September.

Europe: ECB's stimulus package positive for growth, inflation

- **Euro area sentiment improves.** Investor sentiment, business confidence and confidence of purchasing managers in the services sector have started to improve after slumping through H2 2014. This is also visible in improving consumer sentiment – Euro area retail sales rose in December at its fastest pace since 2007. However, the manufacturing sector confidence remains subdued, weighed by excess capacity and falling producer prices.

Euro area economic data surprise positively while US data fall below expectations

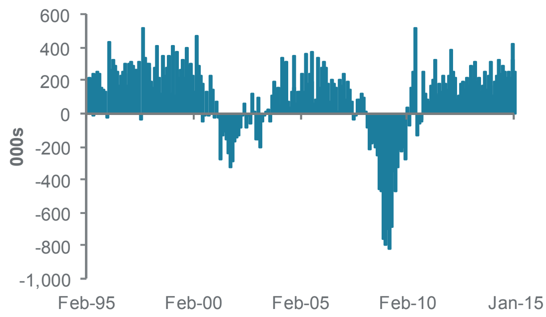
Citigroup economic surprises index for US and Euro area



Source: Citigroup, Bloomberg, Standard Chartered

US job creation continues at a robust pace

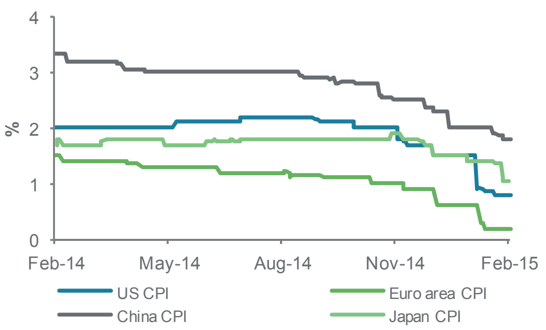
US monthly net non-farm payrolls ('000s)



Source: Bloomberg, Standard Chartered

Consumer inflation expectations decline globally

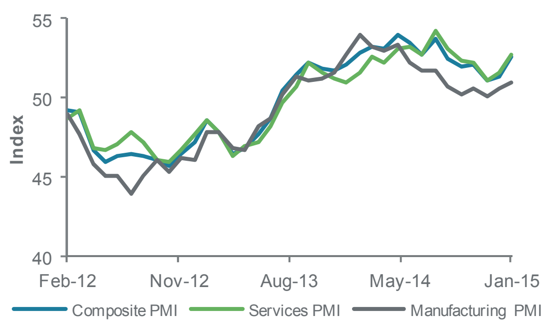
Consensus CPI forecasts for 2015 (%, y/y)



Source: Bloomberg, Standard Chartered

Euro area PMIs are turning around

Euro area Composite, Manufacturing and Services PMIs



Source: Bloomberg, Standard Chartered

- **Germany driving Euro area revival.** The Euro area's largest economy reported a record current-account surplus in 2014, aided by exports, which are benefitting from the sharp decline in the EUR. Strong growth is boosting German wages, helping boost local consumption. However, business confidence in other major Euro area economies, such as France and Italy, remain subdued.
- **Inflation continues to decline.** Euro area consumer prices contracted for the first time since 2009, while producer prices have been contracting since 2013 due to falling commodity prices, high unemployment and excess capacity.
- **ECB stimulus likely to revive inflation, growth.** The government bond purchase programme, which starts in March, potentially allows unlimited purchases until inflation moves close to the ECB's 2% target. We believe this will be achieved through a weaker EUR, by making imports more expensive. A weaker EUR is also likely to boost exports. Strong exports and record-low borrowing costs are expected to revive growth in the Euro area.
- **Greek bailout extension likely.** Euro area policymakers are likely to extend Greece's bailout programme, allowing for a postponement of debt repayments. Talks in Brussels point to a compromise by German policymakers as well as Greece's willingness to meet a majority of its bailout conditions.

Japan: Further easing by the Bank of Japan (BoJ) likely in H1

- **Falling real wages subdue inflation expectations.** Although nominal wages in Japan rose last year, real wages (adjusting for inflation) fell 2.5%. Falling real wages are weighing on household consumption and suppressing inflation expectations.
- **We expect further BoJ easing to drive the JPY lower,** helping exporters and reviving inflation expectations. Governor Haruhiko Kuroda has said there is scope for the BoJ to increase its government and corporate bond holdings further, if needed.

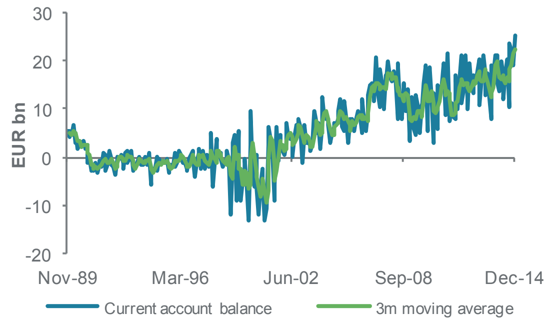
China: More policy easing expected as growth, inflation slow

- **Sharp import contraction portends further slowdown in Q1.** China's imports contracted almost 20% in January, adding to the slowdown in the manufacturing and services sectors. Meanwhile, falling commodity prices have dragged down consumer inflation to a five-year low. Producer prices have been falling since 2012.
- **We expect more policy easing in H1.** This is likely to include further cuts to bank reserve requirements and lower interest rates, adding to the easing measures implemented since September, as growth is likely to slow to 7% in 2015.

Other EMs: Further rate cuts in India depend on budget, inflation

- **India focuses on the 28 February budget.** Although the central bank cut rates in January, it reiterated that further cuts will depend on the government's ability to reduce the budget deficit by curbing subsidies to fund infrastructure spending. The new government has approved USD 100bn of infrastructure and mining projects, which were held back on environmental grounds.
- **Emerging Markets (EM) and commodity producers ease policy.** Central banks in China, India, Russia, Turkey and Singapore have eased policy this year, joining counterparts in Canada and Australia. We expect falling inflation to allow central banks to ease policy further this year.
- **Brazil raises rates to fight inflation.** Brazil was an exception as it raised its key rate for the third time since October 2011 to counter rising inflation, which soared above 7%. We expect inflation to rise further as the economy stalls and the currency trades at a 10-year low, raising the cost of imports.

Germany reported a record current account surplus
German Current Account Balance (EUR bn)

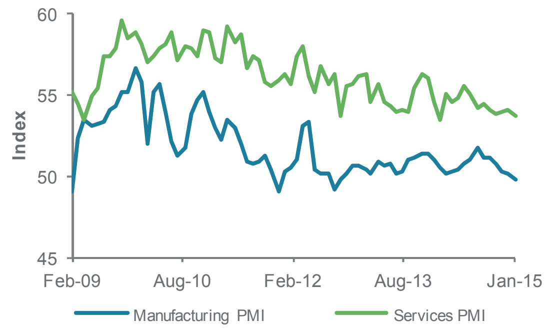


Source: Bloomberg, Standard Chartered

Japan's real wages contracted last year, hurting sales
Japan real wages (%, y/y); retail sales (%, y/y)

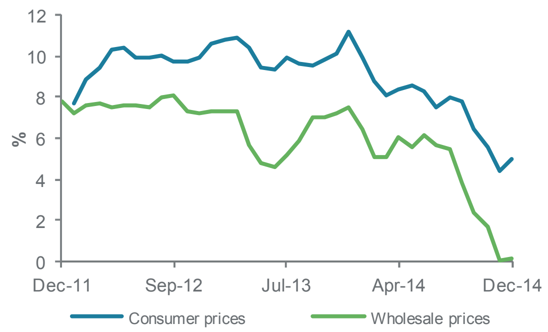
Source: Bloomberg, Standard Chartered

China's manufacturing sector contracted while the services sector continued to slow down
China's manufacturing and non-manufacturing PMIs



Source: Bloomberg, Standard Chartered

India's inflation has slowed significantly since last year
India's consumer and wholesale price indices (%, y/y)



Source: Bloomberg, Standard Chartered

Fixed Income – Underweight

- We continue to prefer corporate bonds over sovereigns and favour an unconstrained approach to bonds.
- CNY, CNH and INR local currency and Emerging Market (EM) Investment Grade (IG) sovereign bonds remain our preferred bond asset classes. CNY and CNH bonds offer an opportunity to add, given recent FX weakness.
- Rising inflation expectations likely led US Treasury yields higher. Total returns are likely to be capped despite the European Central Bank's (ECB) quantitative easing (QE).

G3 and EM (USD) sovereign bonds

- **Rebound in US inflation expectations led to a rise in Treasury yields.** The increase in commodity prices, especially of oil, along with strong US employment data, caused inflation expectations to move higher. Over the past month, markets have also started assigning a higher probability to an earlier-than-expected rate hike by the Fed. Together, these factors drove yields higher.
- **The ECB's sovereign bond-buying is likely to cap the rise in US Treasury yields.** While the rising probability of a Fed rate hike is likely to place upward pressure on US Treasury yields, very low yields in Europe and potentially high demand for bonds are likely to restrict the magnitude of the increase due to the relative attractiveness of US Treasury yields.
- **In the USD space, we continue to prefer EM IG government bonds over EM High Yield (HY) government bonds.** EM IG government bonds have been one of the top-performing bond asset classes year-to-date and continues to offer value at current spreads, in our view. EM HY government bonds also appear inexpensive, but we remain cautious due to higher concentration risk, the high exposure of these countries to commodities and idiosyncratic risks in Venezuela and Ukraine.

Asian local currency bonds

- **Attractive opportunity to buy CNY and CNH bonds.** Given that we do not expect the CNY to weaken significantly further (please see page 11 for currency views), we believe the recent currency weakness offers a buying opportunity for CNY and CNH bonds. They continue to offer attractive yields and potential for capital gains if China eases monetary policy further.
- **We continue to like INR bonds.** They continue to offer attractive yields with the potential for capital gains through policy-easing. While bond prices have increased since our recommendation, we still see room for further gains. We expect strong capital inflows as well as a strong reserve position to support the INR.

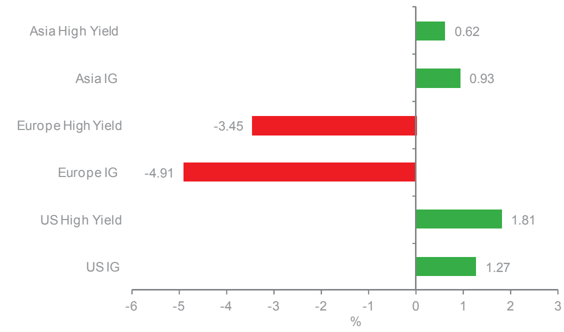
Corporate credit (USD)

- **Developed Market (DM) HY spreads continue to widen.** The spike in yields of US energy sector bonds and lower US Treasury yields were two key drivers of wider spreads. However, valuations are only now around long-term averages.
- **Cap total exposure to HY bonds to benchmark levels.** We believe capping the total exposure to c.10% of total allocation (for the 'moderate risk' investor-class) is the best way to balance the risk/return. However, we continue to monitor HY bonds closely should an attractive entry point present itself.

Conclusion:

Prefer Asian local currency bonds (CNY, CNH and INR) and EM IG sovereigns. Cap total exposure to HY across DM and Asia.

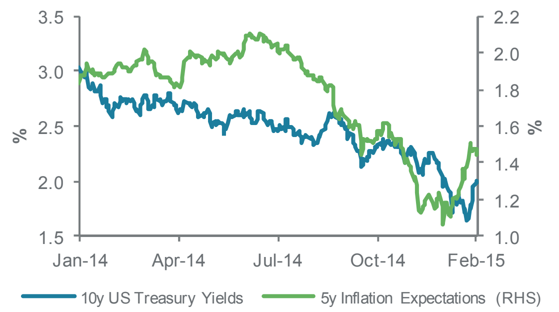
Performance of fixed income YTD* (USD)



** For the period 31 December 2014 to 12 February 2015*
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

Inflation expectations likely behind yield rise

US 10-year Treasury yield vs. market expectations of 5-year inflation



Source: Bloomberg, Standard Chartered

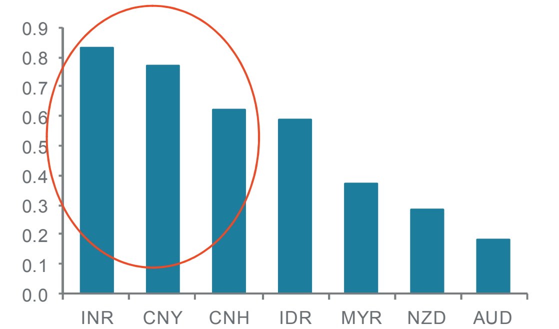
EM investment grade sovereign bonds continue to look attractive

EM IG spread is still above the long-term average

Source: Barclays, Bloomberg, Standard Chartered

CNY, CNH and INR continue to deliver superior volatility-adjusted returns

Despite the recent pickup, CNY volatility remains low relative to other currencies



Source: Bloomberg, Standard Chartered

Equity – Overweight

- **We remain bullish on equities, but leadership may change.** We remain bullish on the US market, expecting a total return of 6% in 2015. However, we believe European equities have the strongest potential to outperform given the ECB's stronger than expected monetary policy response and as earnings accelerate.
- **Bullish on Europe and Japan.** We remain bullish on Europe and Japan on a currency-hedged basis. This strategy worked well in January, with both markets outperforming the US.
- **Remain Underweight Asia ex-Japan.** There is no change in our Underweight Asian view. Nevertheless, it is important to note that we expect positive returns in the region and are bullish on four markets: China, India, Taiwan and Thailand.

We remain bullish on the 12-month outlook for US equities

- **We remain positive on the US.** We remain fundamentally positive on the outlook for the US economy and equity market. Three factors drive our positive view on the US:

  1) **Earnings:** After stripping out the negative impact of the plunge in oil prices on the energy sector, S&P 500 earnings rose 9% in Q4.

  2) **Valuations:** Currently, 17x 2015 forecasts are elevated, but remain below levels observed when inflation was at similarly low levels historically.

  3) **Growth:** The US economy continues to gain traction, as reflected in the January jobs report.

USD strength creates headwind for earnings

- **Q4 US EPS growth 10% excluding currency impact.** Dollar strength has been a factor weighing on Q4 US earnings. It is estimated that a 1% annual appreciation in the USD reduces EPS growth by 0.4%. This implies US Q4 EPS growth could have been 10% stripping out USD strength, as opposed to the reported 6.4%.
- **Hedging reduces negative impact.** Balancing concerns of the negative impact of USD strength is the effect of hedging, both financial and natural, via matching overseas sales and costs. Hedging helped mitigate the impact of USD strength on the technology sector's earnings – 14% EPS growth in Q4.

Oil price decline hurts short-term earnings outlook

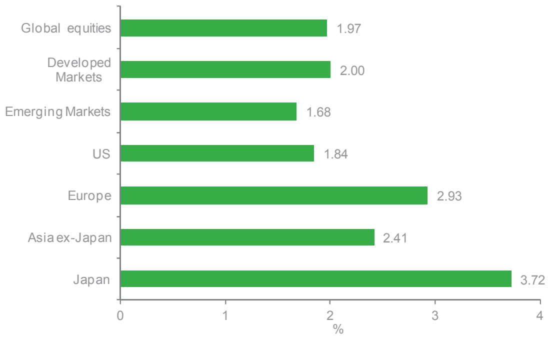
Energy sector Q4 earnings cut 52%. Consensus forecasts for Q4 earnings of the US energy sector fell 52% between October and January. While this cut is understandable, given the 60% peak-to-trough decline in oil prices, analysts have yet to factor in the positive effect on sectors expected to benefit from lower energy prices.

- **US consumer to see USD 833 windfall from oil-price drop.** Following the decline in US petrol prices from the average USD 3.34 in 2014 to the current USD 2.20, US households are expected to benefit from a USD 833 windfall.
- **Higher consumer spending.** This windfall is already finding its way into the US economy, with evidence of an uptick in families taking mini breaks, increasing spending on eating out and higher demand for pick-up trucks.

European equities surge

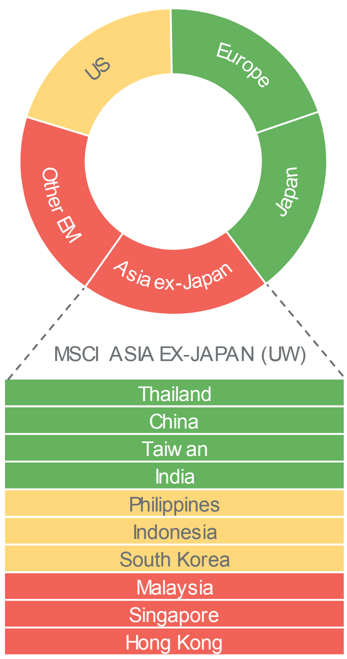
- **European markets rose 8% in January.** The strength of the rally took some by surprise given the election of euro-sceptic Syriza party in Greece. The ability of markets to put aside developments in Greece reflects a belief that widespread contagion is unlikely even if Greece exits the Euro area.

Performance of equity markets YTD* (USD) update



** For the period 31 December 2014 to 12 February 2015*
Source: Bloomberg, Standard Chartered. MSCI Indices are USD total return

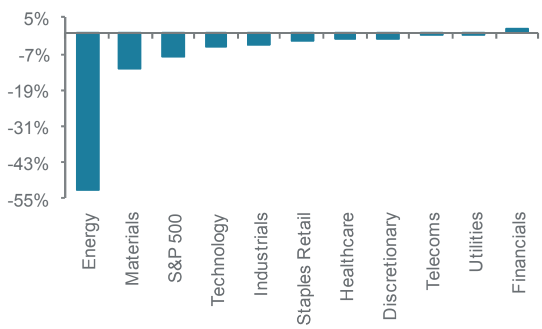
Our GIC view on equity markets



Source: Standard Chartered

Analysts reduce energy sector earnings growth estimates, but no increase in sectors that benefit from lower oil prices

Changes in S&P 500 sector earnings growth estimates



Source BCA Research, Standard Chartered

- **Bigger-than-expected QE.** The European Central Bank (ECB) announced a EUR1.1trn quantitative easing (QE) package in January, which, combined with negative deposit rates, has boosted optimism that Europe can shake off its malaise.
- **European earnings season off to a good start.** The European earnings season starts later than the US, but is off to a good start with 58% companies reporting earnings above analysts' expectations. Consensus expects Q4 EPS to rise 24%.

Asia ex-Japan in easing mode

- **Positive returns forecasts in Asia ex-Japan (AxJ).** We expect AxJ to post positive total returns in dollar terms in 2015. Nevertheless, volatility is likely to be elevated at the time of the first US rate hike and in the immediate aftermath.
- **Policymakers across Asia have eased policy.** Year to date, policymakers in China, India and Singapore have moved to ease monetary policy. The rate cut in India came sooner than expected, while the reserve requirement cut in China was inevitable once weak January data started to emerge.
- **Bullish on India.** The Indian equity market performed well in January, rising 7%. However, it is likely to consolidate in the near term, following the Bharatiya Janata Party's (BJP) loss in the New Delhi state election.
- **China, Taiwan and Thailand also stand out.** We are also bullish on these markets based on 1) the likelihood of further easing in China, 2) the impact of a US recovery on demand for tech hardware in Taiwan, and 3) a pickup in investment in Thailand.
- **Challenges remain.** We retain our Underweight stance on AxJ due in part to high levels of leverage that could weigh on performance as we approach the first rate hike by the Fed.

Risks to consider

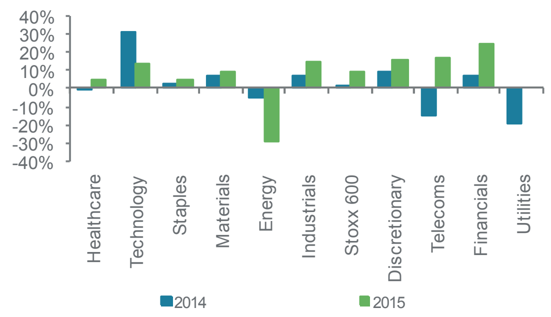
- **Greece –** The market is sanguine about the impact of Greece's demands for a debt write-off. If negotiations between Greece and its Euro area partners break down, the ambivalence of investors to a Greek exit from the Euro area would be severely tested.
- **Oil –** WTI oil prices have bounced off the USD 44 low in January. The consensus is for a USD 40-60 price range in H1 2015. This is dependent on OPEC maintaining output. If OPEC were to cut output, oil prices would surge, undermining the nascent recovery in many market sectors, including airlines.
- **Fed –** The Fed has made it clear that it remains 'patient' in terms of raising rates. However, the January jobs report in combination with an improvement in Euro zone lead indicators may test this patience in the coming months. A change in expectations for the timing of a rate hike would lead to increased volatility.
- **China –** The anti-corruption campaign in China has been widened to the banking sector with the CEO of Minsheng Bank recently resigning. In targeting banks, there is a risk of a slowdown in credit supply if loan officers undertake greater due diligence in granting loans. This in turn could lead to a reassessment of China's growth prospects in 2015.

Conclusion:

We remain positive on equities, anticipating they will outperform other asset classes over the next 12 months. Concerns over the impact of dollar strength need to be balanced with the positive effect of lower oil prices. Risks of a short-term correction have increased as markets reach 52-week highs amid elevated volatility. We would be buyers of selected markets on weakness.

Stoxx full-year earnings growth

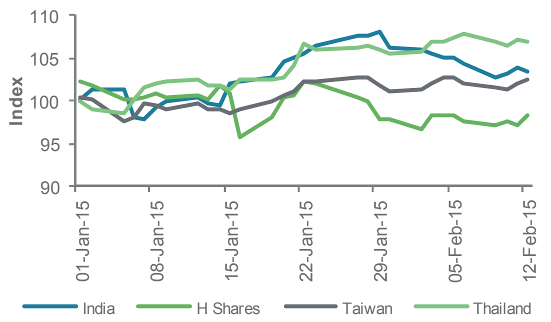
Consensus forecasts 2% growth in 2014, 9% in 2015



Source: Reuters, Standard Chartered

Thailand is a top performer among our Asian overweights YTD

Performance of our overweight calls: 1 January 2015 = 100



Source: Bloomberg, Standard Chartered

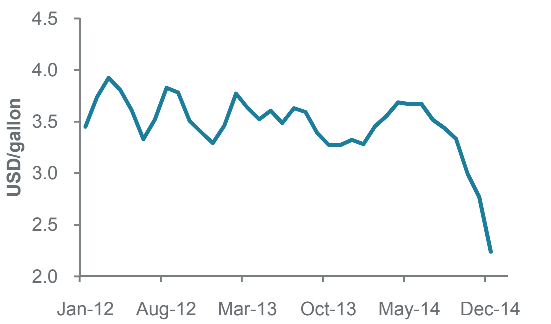
ECB balance sheet forecast to increase to EUR 3trn

ECB balance sheet

Source: Bloomberg, Standard Chartered

US petrol prices have declined by 50% since July

US average pump prices for one gallon of unleaded fuel



Source: Bloomberg, Standard Chartered

Commodities – Underweight

- We remain Underweight commodities with the strength of the USD and a weak Chinese economy being key headwinds. We expect gold prices to weaken moderately amid rising US interest rates and a stronger USD. However, Europe-related concerns may limit downside.
- Oil prices may have witnessed most of their weakness, but varying supplier incentives to curtail production may sustain considerable near-term volatility.

We turn Neutral on gold (from Underweight earlier). While we are moderately bearish on gold, we believe a number of factors may limit significant downside despite a stronger USD. Concerns of a Greek exit from the Euro area and geopolitical concerns in Ukraine are generally supportive for gold. The pace of weakness from current levels is likely to be more modest, in our opinion.

We also believe the global macro environment does not favour a gold rally. First, deflationary risks have increased markedly recently, reducing demand for gold as an inflation hedge. Second, expectations of rising US yields amid Fed rate hike expectations will likely increase the cost of holding gold. Third, the latest round of easing measures, particularly QE by the ECB, is likely to increase risk-taking sentiment and undermine demand for safe-haven assets. Finally, a strong USD is also likely to be an additional headwind for gold.

We remain Neutral energy. Brent oil prices have rallied after briefly falling to USD 47-48/bbl. However, we cannot conclude that the recent upturn is the beginning of a major recovery trend. In our view, the steep fall in oil prices since mid-2014 is driven, on balance, by supply-side factors. As the ability and willingness of producers to alter production might vary considerably, timelines on how quickly the supply-demand imbalance can correct remain uncertain. We believe oversupply is unlikely to correct immediately, particularly as OPEC attempts to regain market share from US shale producers and other non-OPEC countries.

Similar situations in the past have shown that oil prices can remain depressed for some time. As the adjacent chart shows, weak prices persisted over 1986-1989 as OPEC producers refrained from cutting production in a likely bid to gain market share. We believe volatility in oil markets will remain elevated and do not rule out further weakness. At the same time, we acknowledge that demand is likely to strengthen, particularly in the short term.

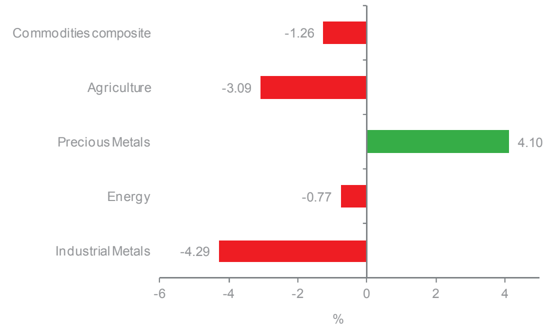
We turn Neutral on industrial metals (from Overweight earlier)

With the majority of the weakness likely behind us, we believe the lack of significant demand catalysts amid a largely oversupplied market will limit any major gains. Demand fundamentals in China remain weak amid a sluggish housing market and falling investment. On the supply side, elevated inventories and an expansion of production capacity, particularly in iron ore, will likely keep prices depressed.

Longer term, our focus remains on signs of strengthening demand, particularly in China, and a revival of investment cycles elsewhere. With this still lacking and inventories generally elevated, we prefer to turn Neutral.

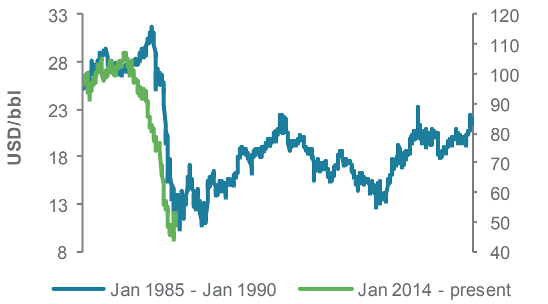
We remain Neutral on agricultural commodities. 2014 was a relatively benign year with respect to weather-related events, and we see stocks remaining at elevated levels. However, we expect some marginal appreciation in prices this year, as consumption picks up with low price levels. Gains may be more pronounced where the supply situation is tighter (sugar) while soft commodities (coffee) remain vulnerable to weather conditions.

Performance of commodities YTD* (USD)



** For the period 31 December 2014 to 12 February 2015*
Source: DJUBS, Bloomberg, Standard Chartered
DJUBS, DJUBS Agri, DJUBS Precious metals, DJUBS Energy, DJUBS Industrial metals

An echo from history; oil prices can remain low for extended periods
WIT crude oil prices



Source: Bloomberg, Standard Chartered

Gold prices may edge lower, but majority of the weakness is likely over
Gold prices

Source: Bloomberg, Standard Chartered

Industrial metal prices continue their downtrend
Iron ore and copper prices

Source: Bloomberg, Standard Chartered

Alternative Strategies – Overweight

- We remain Overweight alternative strategies as divergence in central bank policy, clearer macro and market trends and rising demand for protection against volatility offer support.
- Our favoured strategies remain equity long/short, macro/CTA and event-driven strategies.
- Asset class returns have been encouraging since we published our Outlook 2015. However, within the strategy, macro strategies have outperformed, while equity long/short strategies have underperformed.

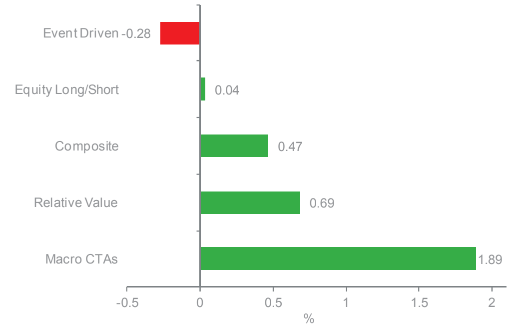
Macro strategies' outperformance likely to continue. This asset class likely benefited from the secular rise in the USD since late last year. We expect central bank easing outside of the US to directly support this asset class because it intensifies divergence, a key driver for macro strategies. We expect this outperformance to continue, especially if the Fed's focus remains on the likelihood of a rate hike. Rising correlation across asset classes is a near-term risk.

Equity long/short and event-driven strategies have underperformed. Long/short strategies may have suffered from reducing value dispersion within US equity markets. However, sector performance dispersion remains high, suggesting there is room for the strategy to perform. We also value the strategy's lower volatility as short-term stress indicators for US equity markets rise. Event-driven strategies have also reported somewhat subdued returns thus far, but we are encouraged by rising global mergers and acquisitions volume.

Conclusion:

Stay Overweight on alternative strategies, favouring diversified exposure. Within the asset class, we favour equity long/short, event-driven and macro/CTA strategies.

Performance of alternative strategies YTD* (USD)



** For the period 31 December 2014 to 12 February 2015*
Source: HFRX, Bloomberg, Standard Chartered
HFRX global hedge, HFRX equity hedge, HFRX event driven, HFRX relative value, HFRX macro/CTA

Short term

refers to a horizon of less than 3 months

Medium term

refers to a time horizon of 6 to12 months

Foreign Exchange

- We remain bullish on the USD, and expect the EUR and the JPY to weaken further. We also expect further weakness in the AUD and NZD. We expect the GBP to remain largely stable.
- We are overall neutral on Asia ex-Japan currencies, but prefer the CNY, INR, IDR, THB and PHP over the KRW, TWD and MYR.

USD: We expect medium-term appreciation

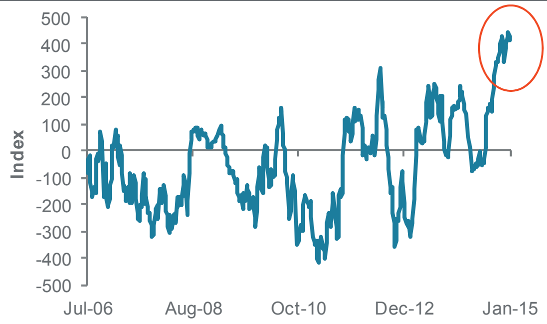
We expect continued USD strength on the back of Fed tightening and monetary policy divergence. As policy easing by other major central banks may now be largely priced in, we believe Fed rate hike expectations will be the next key catalyst for additional USD strength. A pick-up in US yields will further expand interest rate differentials and support the USD, in our opinion.

However, given the size of the USD rally in a short time, we remain wary of a short-term pull-back. Speculator positioning in the USD is now near extreme levels and a sharp correction to any disappointing news is possible. So far, momentum has dominated while we admit that the USD has outpaced our expectations. Longer term, the main risk to our bullish USD is a significant delay in the Fed hiking rates or significant economic surprises in Europe or Japan.

EUR: We expect medium-term depreciation

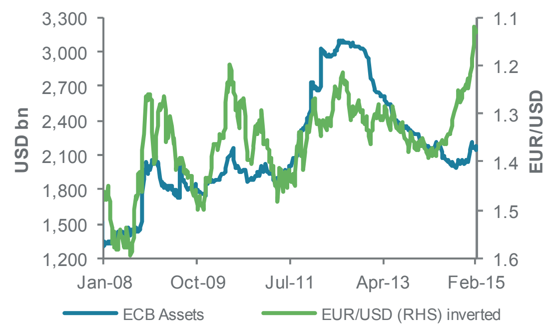
We expect EUR depreciation to continue over the medium term. With the impact of additional easing likely priced in, we believe further weakness will be dependent on additional USD strength. However, we believe three other factors are likely to keep the EUR weak:

USD positioning excessively long, short-term pullback possible
USD net non-commercial futures positioning



Source: Bloomberg, Standard Chartered

EUR: ECB balance sheet expansion may already be priced in; Fed hikes now key to further EUR decline
ECB assets and EUR/USD



Source: Bloomberg, Standard Chartered

1) Increased use of EUR as a funding currency, 2) re-allocation of central bank reserves away from the EUR, and 3) portfolio outflows seeking higher yields. Nonetheless, we caution that speculator short positioning on the EUR is approaching 2012 Euro-crisis levels and could result in a sharp, albeit relatively short-lived, rebound in case of any positive news.

JPY: We expect medium-term depreciation

We remain bearish on the JPY over a 12-month horizon. However, we believe it is likely to consolidate in a broad 116-120 range in the short term, following a sharp rise. Similar periods of consolidation have been observed in 2013 and 2014 (see adjacent chart). We expect the USD/JPY pair to eventually break higher amid an increasing possibility that the Bank of Japan (BoJ) undertakes further easing measures. We believe the BoJ may take additional easing measures if inflation expectations continue to fall. Fed rate hikes, however, still remain key for additional JPY weakness.

GBP: We remain medium-term Neutral

We believe further downside in the GBP is likely to be limited, given recent declines. We are more constructive on the economic outlook and see lower deflationary pressures in the UK compared to the EU and Japan, which is likely to result in a rate hike either later in 2015 or 2016. However, the GBP may remain volatile ahead of UK parliamentary elections in May.

Commodity currencies: We remain bearish on the AUD and NZD

We expect the AUD to depreciate in the medium term. We believe three main factors are likely to keep the AUD under pressure. First, expectations of additional policy easing by the Reserve Bank of Australia (RBA) will further deteriorate the yield advantage the AUD has enjoyed previously. Second, pass-through effects of weaker commodity prices will likely keep terms of trade weak. Third, a pick-up in currency volatility will further undermine AUD-supportive carry trades.

We expect the downtrend in the NZD to continue. Similar to the AUD, we believe a combination of weak commodity prices, declining interest rate differentials and a pick-up in currency market volatility are negative for the NZD.

SGD: We remain medium-term Neutral

We remain medium-term neutral**.** However, we believe the SGD has become more vulnerable to USD strength following the loosening of monetary policy by the Monetary Authority of Singapore (MAS). A further loosening of policy may see more pronounced SGD downside.

Other Asia ex-Japan (AxJ): We remain medium-term Neutral

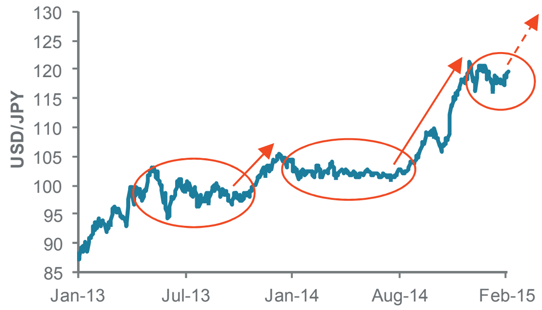
We are Neutral on AxJ as a whole but expect the CNY, INR, THB, PHP and IDR to outperform the KRW, TWD and the MYR in the medium term.

Presently, we do not expect the People's Bank of China (PBoC) to either widen the trading band or drive the daily fixing rate consistently higher. Hence, in our opinion, the CNY will continue to trade in a broad range. We expect strong capital inflows as well as a strong reserve position to support the INR. We expect the THB, PHP and IDR to trade in a broad range from current levels amid supportive monetary policies in their respective countries and a somewhat better growth outlook compared to Korea and Taiwan.

In our view, recent gains in the KRW and TWD are unlikely to be sustained over a medium-term horizon. We expect further weakness in the JPY to compel policymakers to weaken their currencies amid a lacklustre domestic growth scenario. The MYR is likely to remain weak amid USD strength and low commodity prices, in our view.

JPY: May consolidate short term, but eventually break higher on Fed rate hike expectations

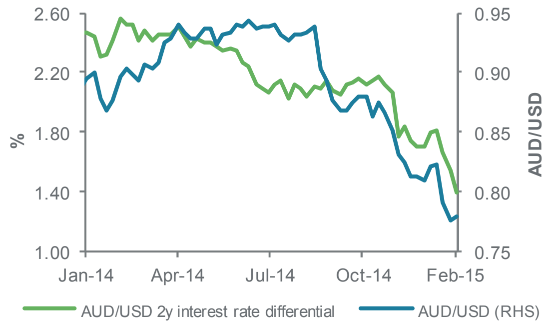
USD/JPY chart



Source: Bloomberg, Standard Chartered

AUD: Fall in interest rate differentials to further weaken the pair

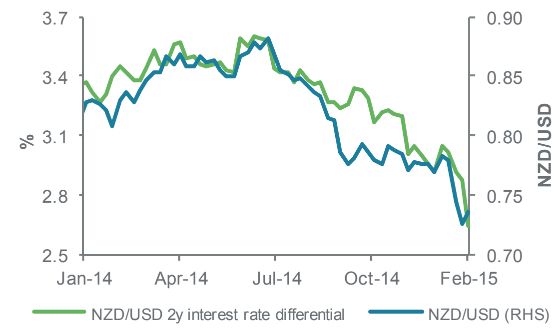
AUD/USD 2-year interest rate differentials (swap rates)



Source: Bloomberg, Standard Chartered

NZD: Decline in interest rate hike expectations has substantially narrowed interest rate differentials

NZD/USD 2-year interest rate differentials (swap rates)



Source: Bloomberg, Standard Chartered

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