Still climbing the 'wall of worry'

Equity markets held up reasonably well despite the 'mini-tantrum' in bonds and gyrations in the US Dollar. We would stay invested, use any volatility to average in, and deploy excess cash holdings in covered call strategies, CNY bonds and unconstrained fixed income.

A surge in German Bund yields and the US Dollar pullback led market volatility. However, global equity market weakness was limited to just over 2% (peak-to-trough). Chinese equities, meanwhile, remained largely flat. We believe equity markets are likely to continue climbing the 'wall of worry' despite Greece, 'sell-in-May' fears and recently weak US data.

We would not be excessively concerned about 'sell-in-May' effects. While we may well see such seasonal volatility, trying to time such a pullback carries a number of pitfalls, which we discuss in more detail on page 4.

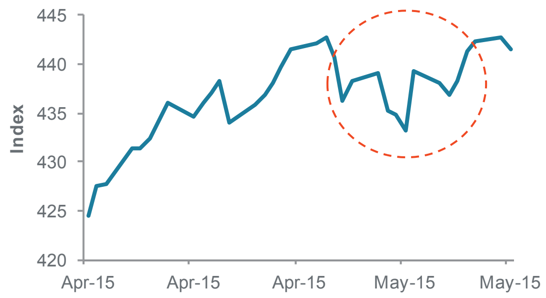
Implications for investors:

- **Our 9-12 month views remain unchanged.** We expect equity markets to outperform bonds, diversified income to generate positive returns and alternative strategies to offer significant diversification benefits.
- **Prepare for greater near-term volatility.** Stay invested, but be prepared to use any temporary volatility to your advantage by averaging in. Excessive cash holdings could be deployed to covered calls, CNY bonds and unconstrained fixed income as they are generally less correlated to equities
- **Maintain regional equity market preferences.** Europe and Japan are likely to stay well-supported by improving growth momentum. In China, the potential for MSCI index inclusion could hold positive short-term implications.
- **Income investing remains a valid approach.** While rising US interest rates may provide headwinds at some point over the summer months, low bond yields relative to their long-term history are likely to keep the search for yield intact. We increase our allocation to CNY bonds and covered calls at the expense of REITs and DM Investment Grade (IG) USD bonds.
- **USD may be bottoming.** Key here is the outlook for interest rate differentials. With European yields about as low as they can go, US interest rate expectations are key.

Contents

Early May equity market weakness was very short-lived

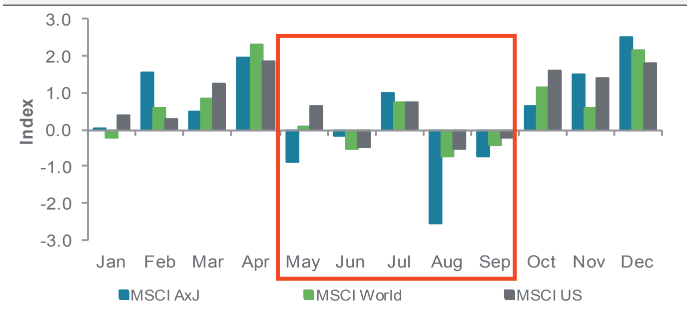
MSCI World Index



Source: Bloomberg, Standard Chartered

History may not repeat, but it seems to rhyme

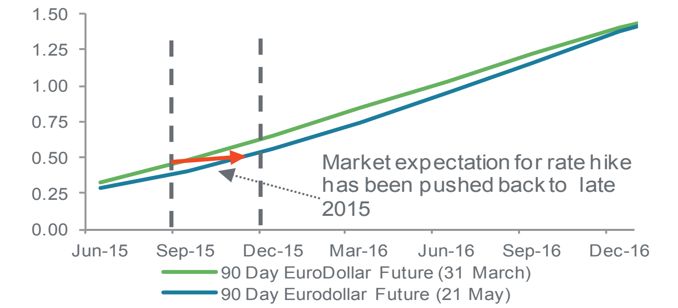
Average USD returns since 1995 (m/m)



Source: Bloomberg, Standard Chartered

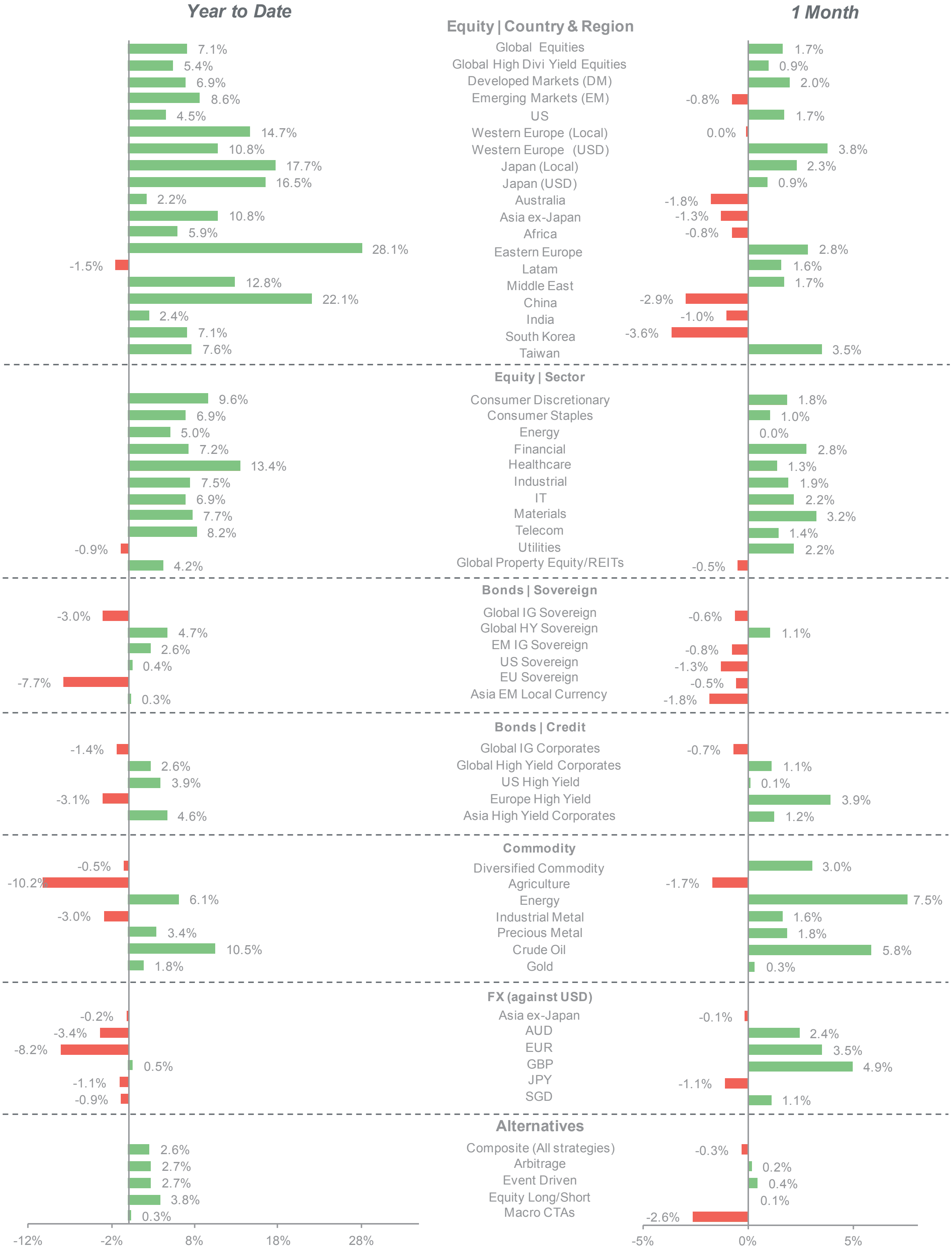
Markets pushed out their first Fed rate hike view to end of the year

Market expectations of Fed policy rates



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 21 May 2015 and 1-month performance from 21 April to 21 May 2015*

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

Investment Strategy

- **The manner in which equities powered through event risks and the bond yield spike in early May illustrates the importance of maintaining a focus on long-term investment views without getting too distracted by temporary volatility.**
- **A renewed Fed conversation on rate hikes risks raising volatility over the next few months. We believe an allocation towards less risky or less equity-correlated assets is a better approach when preparing for such an outcome, instead of trying to sell and re-enter equities. See page 4 for more details.**
- **Stay invested in our W.I.D.E.N. theme that favours equities, diversified income and alternative strategies amid an improving growth outlook in major economies and further policy support in Europe and China.**

Equity weakness was fleeting, despite the jump in yields. Higher European inflation expectations, low liquidity and extreme positioning likely contributed to the jump in long-dated bond yields and a fall in the USD. Despite this, equity market weakness was fleeting in nature. In our view, this illustrates the importance of maintaining a focus on long-term investment allocations without getting too distracted by volatility that is expected to be temporary.

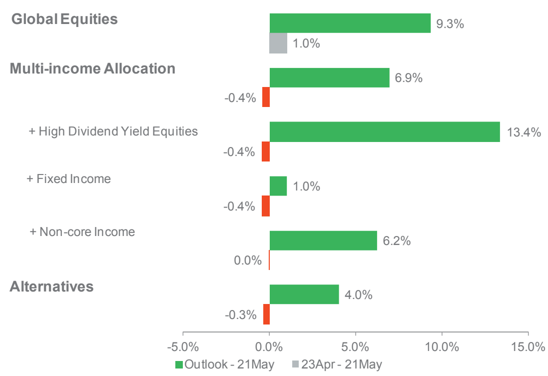
Fed rate signals and policy support outside the US are key to the outlook. Markets have delayed their expectations for the Fed's first rate hike to year-end. This may be a bit excessive and could raise volatility temporarily should the Fed hike rates sooner. But the growth outlook in Europe and Japan is improving, the ECB is 'front-loading' quantitative easing (QE) purchases and China may ease policy further. These positives stand in favour of using any temporary volatility to average into our W.I.D.E.N. theme.

Implications for investors:

- **Stay invested.** History does not favour attempting to time temporary volatility. Strong equity market momentum and supportive policy and growth are short- and long-term positives. Use any weakness to average into our W.I.D.E.N. theme or use excess cash to add less risky assets (see page 4 for details).
- **Maintain currency hedges on Europe, Japan equities.** The temporary pullback in the USD already appears to be drawing to a close. Interest rate differentials continue to favour the USD. We would not remove currency hedges, especially at these levels.
- **Favour offshore (H-share) China equities in Asia.** Further policy easing, the valuation gap with onshore (A-share) stocks and China's potential inclusion in MSCI indices are likely to be key supporting factors.
- **Renewed USD strength, capped yield gains favour alternative strategies.** The recent weakness is likely to prove temporary as yield gains fade and the USD pullback draws to a close.

Bullish W.I.D.E.N. themes have performed well so far

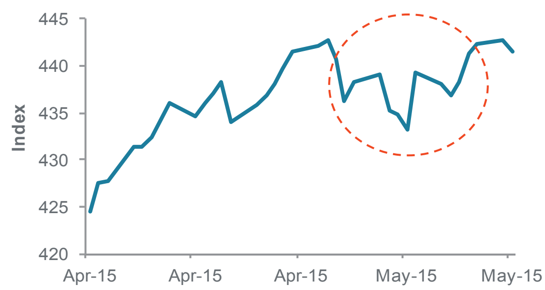
W.I.D.E.N. performance since Outlook 2015 was published and since last Global Market Outlook***



** For the period 12 December 2014 to 21 May 2015*
Source: Bloomberg, Standard Chartered
*** For the period 23 April 2015 to 21 May 2015*
** Income basket is as described in the Outlook 2015: A Year to W.I.D.E.N. Investment Horizons, Figure 60*

Early May equity market weakness was very short-lived

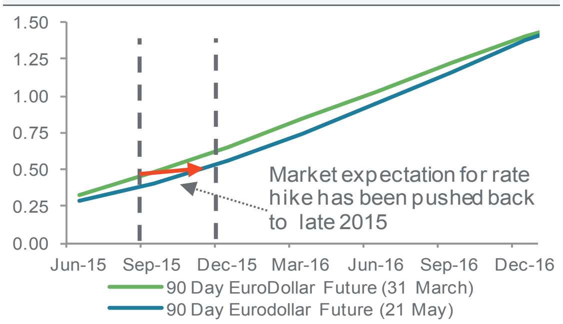
MSCI World Index



Source: Bloomberg, Standard Chartered

Markets have pushed out their expectation of the first rate hike to year-end, which may be excessive

Market expectations of Fed policy rates



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*

Investing ahead of increased volatility

- **Equity market momentum has overwhelmed seasonality concerns. We expect this to continue in the very near term, with global equities hitting new highs. For those with significant cash on the sidelines, our preferred areas are covered call strategies, CNY bonds and unconstrained FI.**
- **An alternative approach would be to wait for a pullback before investing in global equities and diversified income.**

The challenges with 'Sell in May'

You only need to turn on CNBC, Bloomberg or local financial news stations to hear one analyst or another talking about the likelihood of increased volatility. What action to take is usually left open to the listener, but it is easy to infer that you should reduce your allocation to equity markets, or better yet, sell all your holdings. We disagree.

We believe there are several risks to such a strategy:

1) A pullback does not occur, which means you miss the ensuing rally
2) You sell too early or too late
3) You buy back too early or too late

It is interesting to note that **one of the highest consensus views in financial markets is that we will see greater volatility** in the months ahead. A contrarian would argue this suggests a gradual grind higher in equity markets is more likely.

Even if your view proves correct, timing is absolutely critical to the success of this strategy. It is also extremely hard to get right, even for professional investors who monitor market indicators all day. Last year, should you have sold global equities on the 30 April close (true to the 'Sell in May' mantra) and bought back at the closing price on 30 September (October is the start of a seasonally strong period), then, excluding transaction costs, you would be 1.7% worse off than just holding on through the summer months.

For an investor trying to time the market, it may be interesting to note that global equities fell 5% between 6 October and 16 October, but by the end of October, these losses were more than fully recovered (up 7% from the low). The conclusion we draw from the above is that if professional investors struggle to consistently get this right, then individual investors will struggle as well.

So, how do we approach investing over the summer?

1) **Stay invested.** Investors should avoid trying to time selling global equities and then look for an opportunity to re-enter, given the challenges outlined above.
2) **Use volatility to your advantage:** Investors could average into global equity and diversified income investments over the coming months. This has the benefit of taking advantage of any weakness, but also ensures participation in the rally should no weakness occur.
3) **Deploy excess cash to less risky or less equity-correlated assets:** Investors with significant cash on the sidelines could consider investing in asset classes that either have a lower risk profile or a low correlation with equities:
   – Equity covered calls (which give up some of the upside, but also earn a premium to offset some of the downside risks),
   – CNY bonds, which historically had low correlation to equities and avoided losing money during the 2013 'taper tantrum'
   – Unconstrained fixed income (which may be less sensitive to rising interest rates)

'Sell-in-May' history is mixed

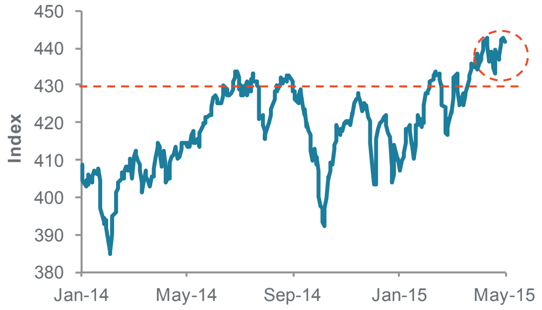
Returns and maximum drawdowns over May-Sep period (%)

Year	Sell in May returns	Peak to trough
2000	-4.8	-8.0
2001	-18.4	-26.4
2002	-23.3	-25.7
2003	13.3	-3.8
2004	2.2	-5.9
2005	10.8	-2.5
2006	0.3	-12.3
2007	6.2	-11.3
2008	-22.3	-26.3
2009	28.9	-7.6
2010	0.3	-13.0
2011	-20.5	-21.7
2012	2.1	-11.2
2013	4.5	-8.6
2014	1.7	-5.2
Average	**-1.3**	**-12.6**
Median	**1.7**	**-11.2**

Source: Bloomberg, Standard Chartered

Equity market momentum has overwhelmed seasonality concerns

MSCI AC World index



Source: Bloomberg, Standard Chartered

Multi-income update

- **The multi-income allocation has performed well YTD. The twin objectives of this allocation (generating a stable income stream, protecting income by considering total return potential) remain unchanged.**
- **Keeping these two objectives in mind, we have tweaked our allocation this month in anticipation of an environment of increased volatility in the months ahead.**
- **Specifically, we look to reduce rate-sensitive assets, improve portfolio diversification and monetise equity market volatility. We do this by reducing allocation to Developed Market (DM) Investment Grade (IG) bonds and REITs and raising allocation to leveraged loans, CNY bonds, covered calls and non-core assets outside of REITs.**

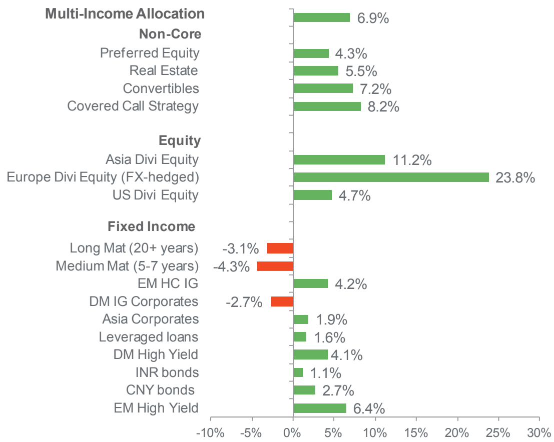
The multi-income allocation has performed well (up 6.9%) since our Outlook 2015 publication, led by dividend equity performance. The two guiding principles for our multi-income allocation, as outlined in Outlook 2015, remain unchanged: 1) generation of a stable income stream, and 2) protection of income by considering the total return potential of asset classes. These twin objectives remain valid.

As we have outlined on page 4, we are mindful of the risk of near-term volatility. Given our two objectives (particularly the second), we rebalance by moving to assets that protect against rising rates, provide diversification and monetise volatility, without significantly sacrificing the yield component.

1. **Reduce rate-sensitive assets** – We reduce our allocation to DM IG assets (paltry yields and interest rate risks) and REITs, both of which may be challenged in a rising rate environment. In their place, we look at the following:
   - **Adding to leveraged loans**: The asset class offers an attractive yield of around 4.76%. Incrementally stronger investor protection in the event of a default and a floating rate (lower interest rate risk) arguably bring a more defensive risk profile to the income portfolio.
   - **Rotating within non-core income**: We reduce our allocation to REITs in favour of other non-core income assets, such as convertible bonds and preferred stock. REITs have been a steady performer in the non-core income bucket. However, a market environment focused on rising rates might create challenges for the asset class. In the 2013 'taper tantrum', this asset class saw a drawdown of -15.88%.
2. **Improve portfolio diversification by adding to CNY bonds** – Chinese onshore bonds provide an attractive yield of around 4.71%, while maintaining a low correlation with other asset classes. This allows an investor to continue to benefit from income during periods of heightened uncertainty. One risk is the chance of a currency depreciation, which we believe is limited given China's ambition to have the yuan included in IMF's Special Drawing Rights (SDR) currency basket.
3. **Monetise equity market volatility through increased covered call allocation** – Equities have had a strong start to the year. While we continue to expect positive returns from this asset class going forward, incremental returns may be generated in a period of increased volatility. Under these circumstances, we prefer to increase our allocation to covered calls, which give us exposure to the equity market while slightly reducing downside risks.

Performance of 2015 multi-income allocation

Inception to date total return performance (%)*



** For the period 12 December 2014 to 21 May 2015*
Source: Bloomberg, Barclays, JPMorgan, Citigroup, MSCI, FTSE, CRISIL, Standard Chartered

Adjusted weights for 2015 multi-income allocation

All figures are in percentages

Asset Class	Sub-Asset Class	Weight
Fixed Income	EM High Yield	**4.0%**
	CNY bonds	**5.0%**
	INR bonds	**3.0%**
	DM High Yield	**5.0%**
	Leveraged loans	**5.0%**
	Asia Corporates	**2.0%**
	DM IG Corporates	**5.0%**
	EM HC IG	**8.0%**
	G3 Sovereigns	**7.0%**
	- Mid Mat (5-7 years)	5.0%
	- Long Mat (20+ years)	2.0%
Sub-total		**44.0%**
Equity	US Divi Equity	**12.0%**
	Europe Divi Equity (hedged)	**15.0%**
	Asia Divi Equity	**11.0%**
Sub-total		**38.0%**
Non-Core	Covered Call Strategy	**6.0%**
	Convertibles	**5.0%**
	Real Estate	**2.0%**
	Preferred Equity	**5.0%**
Sub-total		**18.0%**
Total	**Multi-Income Allocation**	**100%**

Source: Standard Chartered

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 5-7y 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, S&P 500 Covered Call index, CRISIL Composite Bond Fund Index, JP Morgan EMBI Global Diversified, FTSE EPRA/NAREIT Developed North America REITs TR Index, FTSE EPRA/NAREIT Europe REITs TR Index, FTSE EPRA/NAREIT Asia REITs TR Index, JACI Investment Grade Corporates, JACI Non-Investment Grade Corporates, Barclays EM Local Government Asia

Economic and policy outlook

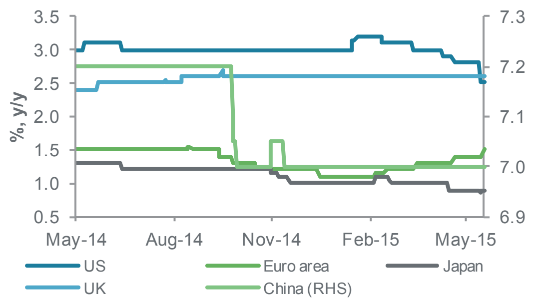
A temporary US slowdown is likely to delay a Fed rate hike to September or possibly later. European growth is broadening, but extremely low inflation implies the ECB bond purchases are likely to continue well into 2016. Japan is accelerating, but China continues to slow, raising the prospect for more stimulus.

- **Weak recovery likely to delay a Fed rate hike to September, at the earliest.** Economists have cut Q2 growth forecasts after a disappointing Q1. While the job market picked up pace in April, consumer sentiment remains subdued. A weaker-than-expected recovery in Q2 may delay a Fed rate hike to September or later.
- **Low inflation means sustained ECB bond purchases, despite broad-based growth upturn.** Growth picked up in France, Spain and Italy, offsetting a slowdown in Germany and helping end a four-month decline in consumer prices. However, low inflation implies ECB bond buying is likely to continue well into 2016.
- **Greece has weeks to reach a bailout agreement or default**. Greece failed to make progress in talks with the EU leaders at Riga aimed at unlocking bailout funds. However, the ECB has continued with its emergency loans to Greek banks so far. German Chancellor Angela Merkel said that Greece has until the end of May to reach an agreement.
- **Japan's accelerating growth raises the hurdle for more BoJ easing.** Q1 growth accelerated to an annualised 2.4%, from 1.1% in Q4, powered by corporate investments. As growth picks up, the BoJ has pushed back the deadline for reaching its inflation target to Q3 16, from March. While inflation remains low, accelerating growth has lowered the chances of more policy easing.
- **China's continued slowdown points to further policy easing**. The economy continued to slow down for the second straight quarter in Q2. We expect more policy easing, including cuts in bank reserve requirements and interest rates. India faces headwinds from the rebound in oil prices and a delay in key policy reforms. Weak exports are likely to keep Asian central banks accommodative.

US: Weak recovery suggests Fed may not hike until September

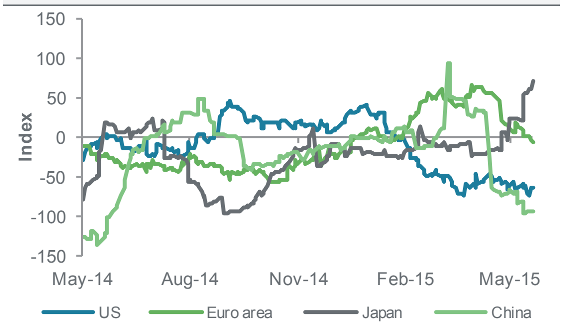
- **Q2 growth forecasts downgraded.** Consensus estimates for Q2 growth have been cut to an annualised 2.7% (from 3.1%) over the past week. This follows a sharp slowdown in growth in Q1 (0.2%) as yet another harsh winter hurt retail sales, while a stronger USD and weaker oil price hurt exports and energy investments.
- **Job market recovers, but consumers hold out**. US job creation rebounded in April after a sharp decline in March. However, retail sales stalled in April after a recovery in March, while consumer sentiment weakened to a six-month low in May. A recovery in consumption, which accounts for 70% of the economy, would be critical for sustained growth. A pick-up in housing starts in April to a seven-year high is encouraging following the winter blip.
- **Wages starting to pick up.** Average earnings growth ticked up to 2.2% in April, while broader measures of labour costs showed bigger increases in Q1. This indicates wage pressures are rising as unemployment drops closer to the Fed's 5.0-5.2% target. As wages rise, we expect a consumer-driven recovery in H2.
- **Cautious Fed likely to delay hike until September or later.** Fed Chair Janet Yellen has indicated her unease about financial bubbles and warned that 'bond yields could see a sharp rise' when the Fed raises rates. However, other officials have highlighted the risk of tightening too soon. We believe a weaker-than-expected recovery in Q2 is likely to delay a rate hike to September or later.

US growth forecasts have been cut, Euro area forecasts upgraded over the past month
Consensus 2015 GDP growth forecasts (%)



Source: Bloomberg, Standard Chartered

Japan data have surprised positively, while data from China and the US continued to underwhelm
Economic surprise indices for major economies

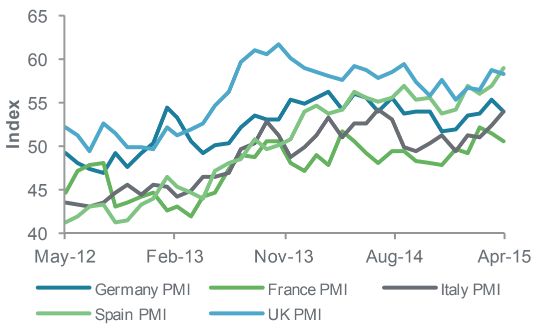


Source: Citigroup, Bloomberg, Standard Chartered

US unemployment declined further as the job market recovered in April, but consumption stayed subdued
US retail sales (%, m/m); unemployment rate (%)

Source: Bloomberg, Standard Chartered

European recovery broadened, helping offset a slowdown in Germany
PMIs for major European economies



Source: Bloomberg, Standard Chartered

Europe: Growth broadens, but low inflation implies sustained QE

- **France, Spain, Italy join the recovery.** Acceleration in three of the Euro area's four-largest economies helped offset a slowdown in Germany in Q1. The broadening of growth has led economists to upgrade Euro area consensus growth forecasts for 2015 to 1.5% (from 1.1% in February), matching the ECB's revised target.
- **Deflation concerns fade, but inflation remains low.** Euro area consumer prices were unchanged in April after four months of y/y declines, easing concerns about prolonged deflation. However, consensus inflation estimates for 2015 (0.15%) remain significantly below the ECB's 2% target.
- **Low inflation implies sustained ECB bond buying**. The ECB inflation target looks challenging even for 2016, given the substantial slack in the economy. As inflation stays low, the ECB is likely to continue with its bond purchases well into 2016. The ECB's plan to front-load bond purchases this summer indicates its commitment to its unprecedented stimulus programme.
- **ECB backstops, economic recovery likely to shield the Euro area from a Greek default**. We believe other peripheral Euro area economies have reformed substantially over the past two years and are now relatively immune to any fallout from a Greek default, if it were to happen. The ECB has also set up several liquidity backstops to protect any spillover from such uncertainty.

Japan: Accelerating growth raises hurdles for more BoJ easing

- **Growth accelerates in Q1.** The pickup in growth to a higher-than-expected 2.4% annualised, from 1.1% in the previous quarter, suggests the economy is steadily recovering from the impact of last year's sales tax rise. While the recovery has so far been driven by corporate investments and improving trade balance, the BoJ expects a moderate rise in wages and lower energy prices to trigger a rebound in consumer spending.
- **Growth pickup raises the hurdle for more BoJ easing**. The BoJ has pushed back the deadline for achieving its 2% inflation target by six months to September 2016. Although inflation remains well below target, the acceleration in growth provides the BoJ another reason to delay any further policy easing.

China: Expect more policy easing as growth decelerates

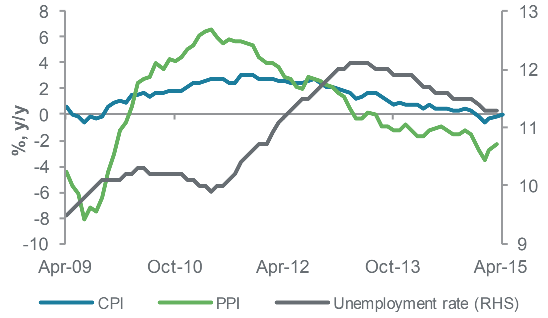
- **Growth may slow for second straight quarter.** Continued weak data for April suggests China is likely to slow for the second straight quarter in Q2 even after several rounds of cuts in interest rates, bank reserve requirements and targeted easing. With forward-looking indicators staying weak, we expect further reductions in bank reserve requirements and interest rates.
- **Plenty of room for further easing**. Although the PBoC cut interest rates in May for the third time in six months, the benchmark lending rate of 5.1% still remains high compared with consumer inflation of 1.5%. Given the government's 3% inflation target, the PBoC has sufficient capacity to cut rates further.

Other EMs: India faces headwind from oil rebound, reform delays

- **The RBI faces rate cut hurdle as oil prices rebound**. Although India's consumer inflation has fallen below the RBI's target, the rebound in oil prices and chances of a weak monsoon threaten to revive inflation expectations. Meanwhile, key tax reform and land acquisition bills have been stalled in the parliament.
- **Asian central banks likely to stay accommodative as exports slump**. Most Asian economies have reported continued contraction in exports in April. The weak external sector and low inflation are likely to keep monetary policies accommodative.

Substantial slack remains in the Euro area, justifying the prolonged period of easy monetary policy

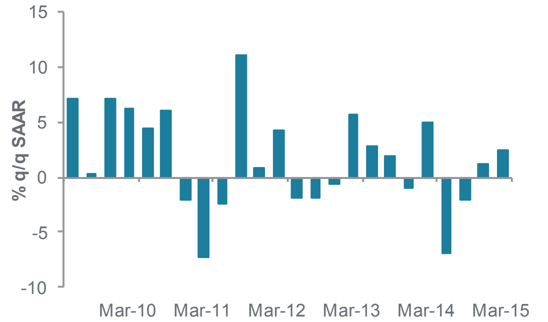
Euro area CPI and PPI (%, y/y); Unemployment rate (%)



Source: Bloomberg, Standard Chartered

Japan's economy accelerated in Q1 on corporate investment and trade surpluses

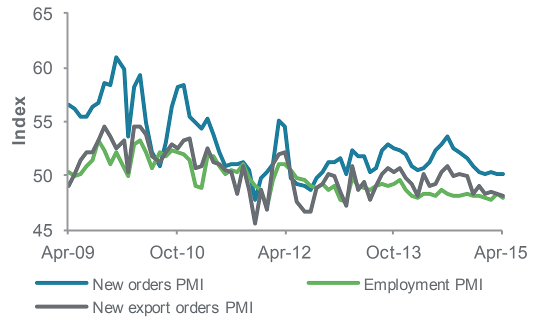
Japan's GDP growth (%, q/q SAAR)



Source: Bloomberg, Standard Chartered

China's economic data remained weak, pointing to more policy easing measures

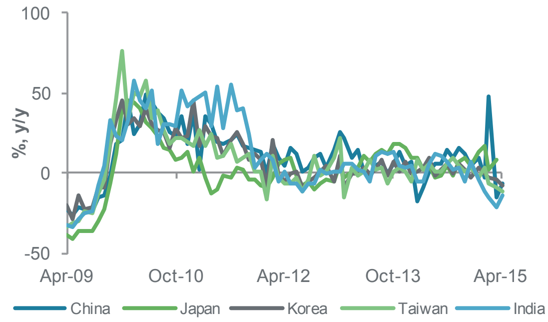
PMIs for new orders, new export orders and employment



Source: Bloomberg, Standard Chartered

Most Asian exports continued to contract in April

Export growth (%, y/y)



Source: Bloomberg, Standard Chartered

Fixed Income – Underweight

- We expect the rise in yields to remain capped. We continue to favour corporate bonds over sovereign debt, with an equal preference for Asia and Developed Market (DM) corporate credit.
- The CNY, CNH and INR local currency and Emerging Market (EM) Investment Grade (IG) sovereign USD bonds remain our preferred bond asset classes.

G3 and EM (USD) sovereign bonds

- **German Bunds led US Treasury yields higher**. US Treasury yields have risen sharply due to a combination of a sharp rise in German yields, rising inflation expectations and low market liquidity.

  However, we believe the rise in the yields will remain capped and the recent increase in the difference between 2-year and 10-year yields should reverse. Hence, we continue to prefer a moderate maturity profile in USD bond portfolios.
- **We continue to like EM USD government bonds, with a preference for IG**. We believe little has changed over the past month and view the recent soft performance as nothing more than a catchup with other bond asset classes.

Asian local currency bonds

- **We maintain our preference for INR bonds.** The recent currency depreciation is not surprising as it is unrealistic for the INR to remain stable given how other Asian currencies have weakened YTD. However, the high yield on offer and scope for capital gains mean bond returns should more than offset currency depreciation.

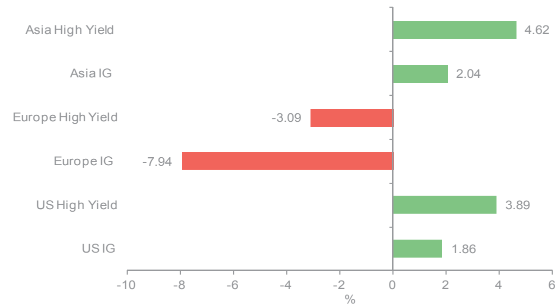
  We believe the recent increase in yields due to concerns around a weak monsoon and higher oil prices is overdone. We remain comfortable holding INR bonds as the supportive fundamental factors still remain in place.
- **We continue to like CNY and CNH bonds.** In particular, CNY and CNH bonds' low correlation with other asset classes means that they continue to offer an exceptional diversification option.

Corporate credit (USD)

- **We prefer benchmark exposure to Asian corporate credit**. While regional bonds offer lower yields compared with other major EMs, we believe a neutral stance relative to non-Asia EM and DM corporate credit is justified:
  - Valuations are fair and remain near their historical average. Values, relative to other major regional credit markets, are also within their usual ranges.
  - Asian growth expectations are arguably more positive than those of the rest of the EMs.
  - Asian credit has been less volatile than other EMs.
  - Asian corporate default rates are expected to be lower than the overall EM universe, justifying a lower yield premium.

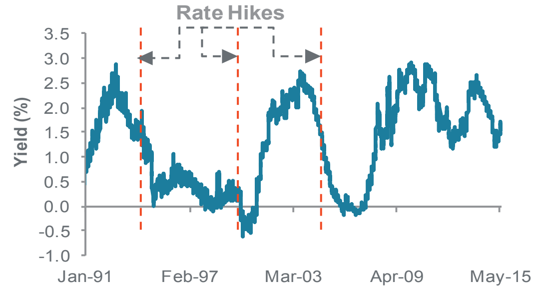
  While this paints a relatively positive picture, macro concerns and still-tight monetary conditions in China prevent us from being more positive. Hence, we prefer Neutral or benchmark exposure to Asian IG and High Yield (HY) corporate credit.
- **Do not chase the DM HY rally**. We believe that the recent rally is largely momentum driven, a catchup after the soft performance earlier this year. However, fundamentals are still on a deteriorating path. We still believe benchmark exposure best balances the yield and risks, which is consistent with our preference for corporate credit over sovereign bonds.

Performance of fixed income YTD* (USD)



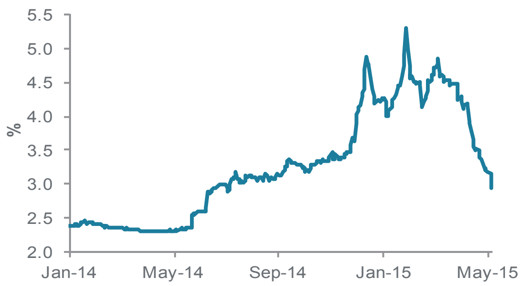
** For the period 31 December 2014 to 21 May 2015*
Source: Barclays Capital, JPMorgan, Bloomberg, Standard Chartered. Indices are Barclays Capital US Agg, US High Yield, Euro Agg, Pan-Euro High Yield, JPMorgan Asia Credit Index

US yield curve likely to resume its flattening
Differential between 10-year and 2-year US Treasury yields (10-2 yield curve)



Source: Bloomberg, Standard Chartered

CNH liquidity is improving
3-month CNH Libor rate



Source: Bloomberg, Standard Chartered

Asian corporates offer a premium over global corporates
BarCap GlobalAgg Corporates, JPMorgan Asia Credit Index spreads

Source: Bloomberg, Standard Chartered

Equity – Overweight

- Equity markets are likely to remain buoyant in the coming weeks given the ECB's liquidity backstop. China may benefit from a positive announcement on the inclusion of A-shares in the MSCI Emerging Markets (EM) indices.
- The ECB's commitment to frontload quantitative easing (QE) in the summer months is negative for the EUR and positive for export-orientated sectors in Europe, including auto, capital goods and consumer staples.
- MSCI will announce its decision on whether it will include domestic China shares in its indices on 9 June. We believe inclusion in the MSCI EM Index would be in a 2-5% range.
- We have become more cautious about the short term outlook for India and Thailand. Concern over valuations, earnings disappointment and policy setbacks, specific to India, have led to recent underperformance.

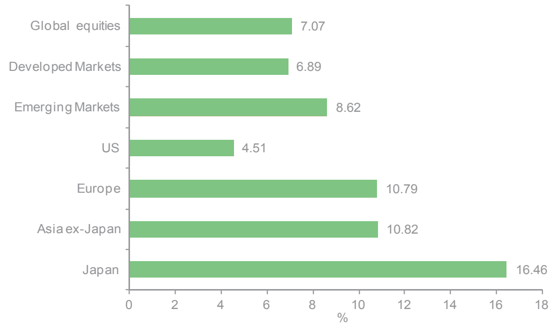
Climbing a wall of worry

- Equity investors have had to navigate a path through a series of negative developments over the past month, including:
  1) Expectations of negative earnings in the US and flat growth in Europe
  2) Disappointing Q1 GDP growth in the US, which averaged 0.2% q/q annualised compared with the 1% forecast growth.
  3) Greece's cash crunch, which has led to expectations that it may exit the Euro area as early as June
- The markets' strength in the face of these negative developments, higher bond yields and currency volatility reflects the ability of investors to successfully climb the 'wall of worry'. This feature of market sentiment usually witnesses one of two eventual outcomes: an accumulation of negative news that grows too big to ignore, shattering investor confidence and leading to a significant correction. An alternative outcome sees a positive turn in news flow, justifying investor optimism.
- The willingness of the central banks in Europe and Japan to provide liquidity to the financial system implies that markets are likely to retain their positive bias over the medium term. Setbacks are inevitable, possibly related to the end game for the Greek crisis over the next month and/or the first rate rise by the Fed over the next six months. Nevertheless, expectations of a steady recovery in earnings imply markets stand a good chance of recovering from any setback and pushing ahead to record new highs.
- Timing the correction is never easy. We continue to prefer Europe and Japan equities on a currency hedged basis, as we believe that they have the highest potential for further gains. We remain Neutral on US equities.

ECB frontloads QE

- The ECB has pre-empted the risk of increased volatility in European asset markets over the summer months by announcing it will 'frontload' (i.e. accelerate purchases in May and June) its EUR 60bn monthly bond buying programme. The ECB's decision to increase its bond buying signals that there is a liquidity backstop in place, should markets be rocked by events in Greece.
- The ECB's announcement had an immediate positive impact on European government bonds, partially reversing the sell-off that started in mid-April. The decline in bond yields helped weaken the EUR against the USD, which has been tightly correlated to the US/German two-year yield spread.

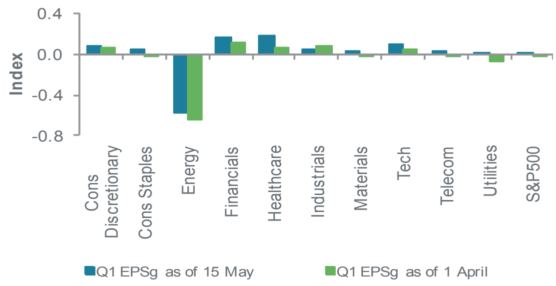
Performance of equity markets YTD* (USD) update



** For the period 31 December 2014 to 21 May 2015*
Source: Bloomberg, Standard Chartered. MSCI Indices are USD total return

S&P500 Q1 earnings move into positive territory

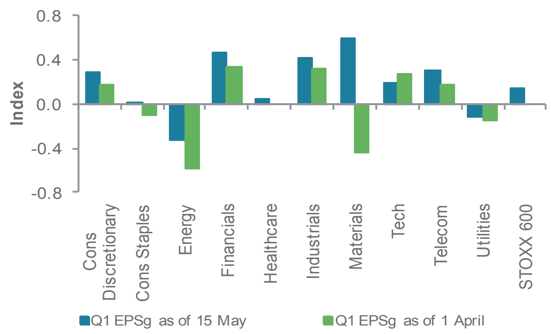
S&P500 Q1 sector earnings forecasts on 1 April and 15 May



Source: Datastream, IBES, Standard Chartered

Q1 energy sector earnings in STOXX 600 recover between April and May

STOXX 600 Q1 sector earnings forecasts on 1 April and 15 May



Source: Datastream, IBES, Standard Chartered

US/German yield spread moves back in favour of the EUR

US/German yield spread (inverted) and EUR/USD

Source: Bloomberg, Standard Chartered

* The decline in the EUR has provided a fillip to export-orientated sectors in Europe, including the auto, transport and consumer staples sectors. While these sectors had performed well in Q1, they weakened following the recovery in the EUR since mid-April. Between mid-April and the day before the ECB's announcement on 18 May, the STOXX 600 index underperformed the S&P500 by 7%. If the recent reversal in the EUR is the start of a new trend, European equity markets may start to outperform the US once again.

MSCI decision on including China A-shares in its indices

* MSCI will announce its decision on whether or not to include China A-shares in its indices on 9 June. MSCI-managed indices are widely used by active (mutual fund) and passive (exchange-traded fund) managers globally. An estimated USD 9.5trn of assets are benchmarked to their indices worldwide.
* Currently, only overseas-listed China shares and Shenzhen- and Shanghai-listed B-shares are included in the MSCI indices. This is despite the fact that domestically listed China stocks, or A-shares, account for 11% of global market capitalisation.
* The barriers to investing in A-shares have slowly been coming down, with quotas for foreign institutional investors, which enabled them to trade A-shares. In November 2014, the introduction of the Stock Connect permitted individual investors to trade A-shares. The launch of the Stock Connect is a potential game changer and increases the likelihood of a positive decision on 9 June.
* Market expectations of the initial weight of China in the MSCI EMs Index ranges from 2% to 5%. If China A-shares are to be included, they would only be included from February 2016, with final weight only achieved over a two-year period, possibly in increments of 0.5-1% every six months. This incremental approach is designed to give institutional investors time to adjust their holdings. As A-share quotas are increased, we would expect China's weight in EM indices to increase. Assuming all quotas were removed tomorrow, the weight of A-shares in the MSCI EMs index would be 16%.

Reducing Thailand and India to Neutral

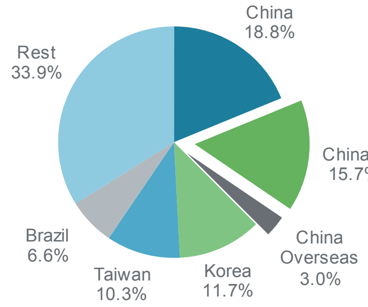
We have become less bullish in the near term towards markets in India and Thailand. Factors driving this decision centre on concerns over valuations - both markets trade almost 15% above long-term average valuations of 15x and 11x consensus forecast earnings, respectively. Earnings revisions for both markets are among the lowest in the region, and there have been policy setbacks in India, which have disappointed investors. We remain constructive on both markets long term, but believe upside may be capped in the near term. Following these reductions, our preferred Overweights are China and Taiwan.

Conclusion:

Investors have successfully climbed a wall of worry over the past month. Looking ahead, the ECB liquidity backstop and a potential positive announcement on China A-shares' inclusion in the MSCI EMs Index are factors that could propel indices to new highs. Disappointment over US growth and the end of the road for negotiations between Greece and its European partners are potential negative catalysts.

Hypothetical weight of China A-shares in the MSCI Emerging Market (EM) Index

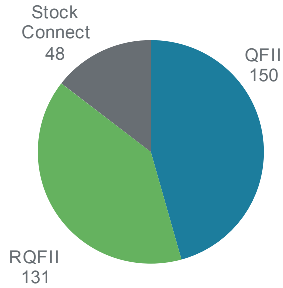
Pro forma country weights in MSCI EM



Source: MSCI, Standard Chartered.

Access to China A-shares is restricted

Breakdown of China A-share quota



Source: MSCI, Standard Chartered

Commodities – Underweight

- We expect gold to remain range-bound in the short term, but to weaken longer term
- The recent oil and industrial metal price rally is unsustainable, in our view

We remain Underweight commodities. We believe commodities as a group are likely to weaken further over a medium-term horizon. Although commodities, especially energy and base metals, have rallied substantially over recent months, we believe this has been driven primarily by shorter-term factors that do not affect the longer-term fundamental outlook.

- **We remain Neutral on energy.** We believe the current rally in oil prices is unlikely to sustain. In our view, the fundamental outlook, both with respect to supply and demand, does not favour a substantial pickup. On the supply side, OPEC production continues to grow, while non-OPEC production is only marginally lower as major producers have not scaled back production significantly. At the same time, crude and petroleum product inventories, both in the US and OPEC countries, have continued to grow. In addition to this, we estimate the USD 60-65/bbl region allows a large number of shale producers to become profitable. Hence, any increase in prices to these levels may encourage increased production, and ultimately put further pressure on prices.

  On the demand side, we believe the recent surge in demand was driven more by seasonal factors, as well as a build-up of some strategic reserves demand by China. However, at a more fundamental level, demand growth remains weak. Therefore, while oil prices are likely to be higher than current levels in the longer term, prices may actually turn lower over the short term.

- **We remain Neutral on gold.** We expect gold to remain weak in USD terms and trade in a broad range in the short term. From a demand-supply perspective, we do not see major changes on either side. On the demand side, investor interest in gold continues to decline. Evidence from Gold ETF holdings show a sharp fall in total investor holdings in May. On the supply side, gold inventories remain largely unchanged.

  From a macroeconomic perspective, the overall environment continues to favour risky assets. Potential interest rate hikes by the Fed and a stronger USD remain major headwinds for gold. In the short term, some buying interest may be seen as Europe grapples with Greek debt concerns. However, we believe this will have limited spillover effects as policy makers are likely to prepare an effective response.

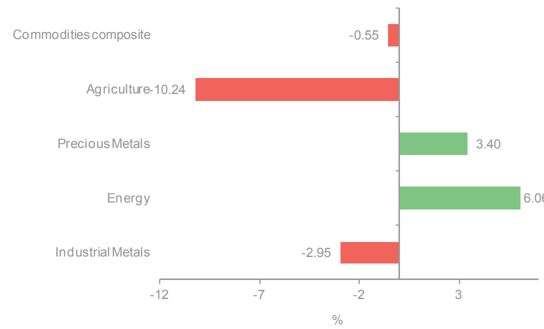
- **We remain Neutral on base metals.** We do not expect the recent rally in base metal prices to continue. Demand from China is likely to remain low, as both residential and business investment remains weak, while supply remains elevated.

  In our view, a weaker USD, China policy easing and temporary shortages of recycled copper were the main factors behind the recent rally. We believe none of these factors are likely to support copper over the longer term.

  Similarly, we see the recent rally in iron ore prices to be driven by shorter-term factors, including seasonal demand, but we do not see the longer-term drivers to have improved substantially.

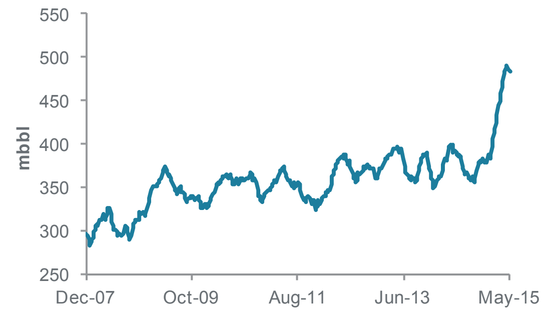
  With respect to both aluminium and zinc, recent data suggests a substantial increase in refined production in China, which is likely to increase oversupply and put pressure on prices.

Performance of commodity markets YTD* (USD)



For the period 31 December 2014 to 21 May 2015
Source: Bloomberg, Standard Chartered. MSCI Indices are USD total return

US crude oil inventories only marginally lower from record levels
US total crude oil inventories



Source: Bloomberg, Standard Chartered

Gold likely to remain range-bound short term
Gold price

Source: Bloomberg, Standard Chartered

Recent copper rally likely to be temporary
Copper price

Source: Bloomberg, Standard Chartered

Alternative Strategies – Overweight

- We remain Overweight alternative strategies. Our supportive themes – policy divergence, clearer market trends and demand for protection against volatility – remain very much in place.
- Countertrend moves in the USD and bond yields were likely key factors behind macro strategies' poor performance over the past month. However, these are already showing signs of reversing.
- Our favoured strategies remain equity long/short, macro/CTA and event-driven strategies.

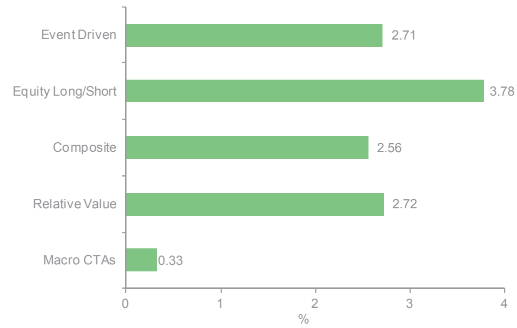
USD consolidation and the sharp move in bond yields hurt macro strategies. The rapid pace of the countertrend move likely worked against the divergence and trend-following nature of the strategy. However, we believe the weakness is likely to be temporary. The USD is already showing signs of reversing, and we expect bond yields to remain capped. Trend-following strategies will likely need time to adjust. Divergence is likely to re-emerge once fundamentals regain dominance after extreme positioning begins to normalise.

Key drivers of our alternative strategies' Overweight remain in place. A renewed conversation around a Fed rate hike is likely to return the focus to policy divergence, favouring macro strategies. Meanwhile, short-term volatility should allow long-short strategies to outperform.

Conclusion:

Remain Overweight 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 21 May 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 6-12 months

Foreign Exchange

- We view the recent pullback in the USD is likely over and expect it to gain against the EUR, JPY, AUD and SGD
- We like the GBP against non-USD currencies, including the EUR, JPY, AUD and SGD

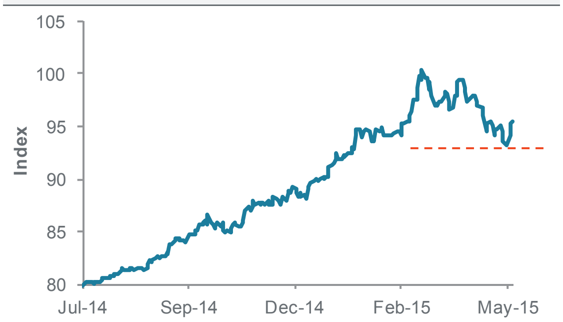
USD: We expect modest medium-term appreciation

We expect USD to be strong over the medium term and believe the recent pullback in the USD is over. Also, we believe the recent weakness in US economic data is temporary and expect acceleration in US growth in the coming quarters. Furthermore, we expect the Fed to hike interest rates in September, which is likely to further enhance the yield advantage of US debt assets and stimulate demand for the currency. A major risk to our USD view remains a substantial delay in a Fed rate hike if economic fundamentals continue to weaken.

EUR: We expect medium-term depreciation

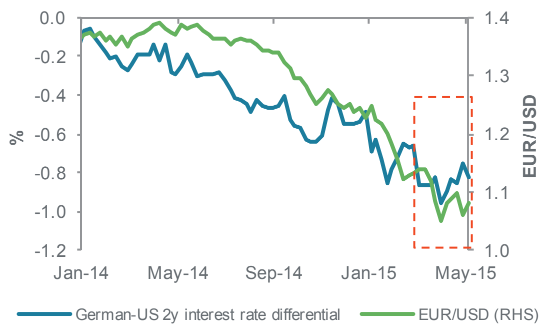
We expect the EUR to weaken over the medium term. In our view, the recent pickup in Euro area growth and inflation are unlikely to change the course of the current policy. We believe the ECB is likely to continue favouring an extremely loose policy until substantial progress is made in reviving long-term inflation expectations. As a result, we believe investors are likely to continue seeking higher yielding assets outside the Euro area. This may be further exacerbated as the Fed hikes interest rates and further expands the yield advantage in US debt assets. We expect the yield differential to be the dominating driver of the EUR over the medium term, despite a large current account surplus and marginally improving economic data.

USD likely bottomed short term
US Dollar Index



Source: Bloomberg, Standard Chartered

EUR: Recent bounce in German-US interest rate differential unlikely to sustain
German-US 2-year interest rate differential and EUR/USD



Source: Bloomberg, Standard Chartered

JPY: We expect medium-term depreciation. We expect JPY depreciation over the medium term although range-bound movements are likely to continue in the short term. Policy divergence in 2015 continues to be key to our medium-term negative outlook on the JPY. While some improvements are visible in Japan's macro indicators following the quantitative easing (QE), we do not believe these are sufficient to warrant a retraction in the easing stance. On the contrary, further easing by the BoJ is possible should inflation expectations fall. In the short term, a lack of any major catalyst is likely to keep the JPY range-bound.

GBP: We remain medium-term Neutral. We do not see further upside in the GBP following the recent rally. We believe Fed rate hikes will curtail GBP strength as interest rate differentials between the US and UK debt continue to expand. At the same time, we believe the BoE will be the first major central bank to raise interest rates after the Fed. The recent Inflation Report highlighted current low inflation to be temporary with economic slack expected to be eliminated in about one year. In this regard, we see the UK to be fundamentally stronger than its peers and, hence, expect medium-term appreciation against the EUR, JPY, CHF and AUD but not the USD.

AUD: We remain bearish on the AUD

We expect further weakness in the AUD over the medium term. In our view, the recent rebound is temporary and may reverse in near-term. We believe the recent bounce in iron ore prices is unlikely to sustain, which undermines Australia's export competitiveness and mining investment. Furthermore, we expect the RBA to further cut interest rates if local economic conditions deteriorate further. This, in our view, will further reduce the yield advantage Australia enjoys over the other G10 countries. We also expect currency volatility to pick up around the time the Fed hikes interest rates, which may further undermine AUD carry trades.

SGD: We expect modest SGD depreciation medium term

We expect modest medium-term weakness over a 12-month period. We believe Fed rate hikes and the accompanying weakness in Singapore's major trade partners' currencies, to which the SGD is benchmarked, will drive the SGD modestly lower. In addition, the domestic economic outlook seems lacklustre at best. In our view, further deterioration in the domestic inflationary scenario and housing prices may compel policy makers to ease monetary policy.

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

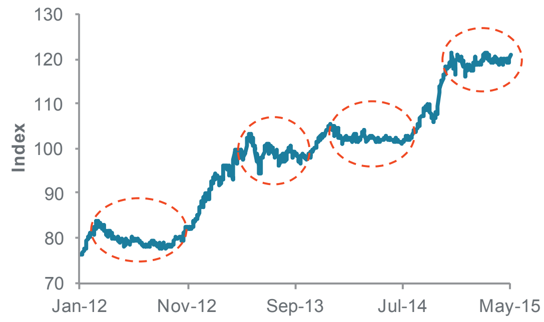
We remain overall Neutral on Asia ex-Japan currencies as a whole, but prefer the CNY and INR on a relative basis. We expect the THB and KRW to underperform relatively amid policy concerns on rich currency valuations. We are Neutral on the IDR, MYR and TWD.

With respect to the CNY, we believe the authorities are likely to prioritise long-term reform over short-term benefits of a weaker exchange rate. In our view, China will continue to favour a stable CNY as it seeks greater internationalisation of the currency (including its inclusion in IMF's Special Drawing Rights [SDR] currency basket). With restricted two-way capital flows, we do not believe the recent weaker macroeconomic data and easing monetary policy are negative for the CNY. With respect to the INR, we do not see significant weakness from current levels. In our view, the RBI is likely to intervene to support the currency in case of a sharp selloff. Longer term, however, the RBI is likely to prefer a gradual depreciation to foster export competitiveness.

We have also revised our outlook lower on the THB and KRW. In both cases, the trade-weighted currencies remain significantly overvalued relative to history. While policy makers have surprised on further monetary easing, we believe further policy easing or direct intervention to further currencies remains a possibility for the two export-dependent economies.

USD/JPY: Likely to break higher with a Fed rate hike

USD/JPY



Source: Bloomberg, Standard Chartered

AUD: Markets underestimating potential for another RBA rate cut

Australia 2-year government bond yield

Source: Bloomberg, Standard Chartered

KRW and THB: Both export-driven currencies (trade weighted) have risen significantly

KRW and THB nominal effective exchange rate

Source: Bloomberg, Standard Chartered

Disclosure Appendix

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