



Global Market Outlook

Are we there yet?

→ Equities and bonds faced a challenging April as the Fed continued to guide rate hike expectations higher.

However, as global central banks embark on policy tightening, the main question facing investors is whether we are approaching the bottom in risky assets.

→ Our still-benign recession checklist gives us confidence that equities can outperform bonds and cash once the Fed stops guiding rate expectations higher.

We continue to prefer Asia ex-Japan equities, even if COVID-19 lockdowns in China delay the recovery.

→ Bond yields could rise further before topping out. We favour EM USD government, Asia USD and US/European High Yield bonds where attractive valuations are a support; private credit and floating rate loans also offer an attractive risk/reward.

We maintain our preference for commodity currencies.

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What can we learn from prior episodes of quantitative tightening?

Is it time to start adding exposure to bonds?

Are earnings reports supporting the case for equities?

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Investment strategy and key themes

Steve Brice

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Our foundation allocation preferences over a 12-month horizon

- Prefer Global Equities and Gold
- *In equities:* Asia ex-Japan
- *In bonds:* DM HY, Asia USD, EM USD govt
- *In FX:* Bearish USD; bullish EUR, GBP, AUD, NZD, CAD, CNY

Longer-term (3-5-year) themes

- The Winds of Climate Change
- Embracing a Digital Future
- China's 'Common Prosperity'

Sector preferences over a 12-month horizon

- *US:* Energy, Financials, Healthcare
- *Europe:* Financials, Energy, Industrials, Healthcare
- *China:* Energy, Industrials, Financials

Are we there yet?

- Equities and bonds faced a challenging April as the Fed continued to guide rate hike expectations higher. However, as global central banks embark on policy tightening, the main question facing investors is whether we are approaching the bottom in risky assets.
- Our still-benign recession checklist gives us confidence that equities can outperform bonds and cash once the Fed stops guiding rate expectations higher. We continue to prefer Asia ex-Japan equities, even if COVID-19 lockdowns in China delay the recovery.
- Bond yields could rise further before topping out. We favour EM USD government, Asia USD and US/European High Yield bonds where attractive valuations are a support; private credit and floating rate loans also offer an attractive risk/reward. We maintain our preference for commodity currencies.

The Fed guides rate expectations higher, and markets lower

While April is usually a positive month for equities from a seasonality perspective, 2022 is proving to be different. Since the end of March, global equities have fallen over 6%, with Chinese equities falling about 9%. In the US, the Fed's efforts to guide rate hike expectations higher was one driver, leaving the 10-year US government bond yield almost 50bps higher, the USD about 5% higher and gold slightly lower over the past month.

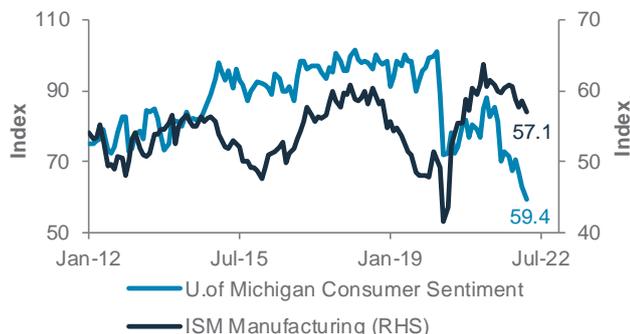
On the back of a hawkish Fed guidance amid rising inflation expectations, we revise our own views and now expect the Fed funds rate at 2.25% (slightly below market expectations) and the 10-year US government bond yield in the 2.50%-2.75% range by the end of 2022.

Are equities close to a bottom, with a fairly aggressive Fed hiking cycle already priced in? The next Fed meeting in early May is likely to see a 50bps rate hike and the start of Quantitative Tightening (QT; where the Fed starts to reduce its bond holdings). Given this and our view that growth and inflation are likely to slow in H2, we are likely approaching the point where the Fed limits how much higher it guides policy expectations. Markets already expect policy rates to reach the Fed's estimated 'neutral' level by year-end and the majority of indicators on our 'recession checklist' remain at healthy levels. This constructive outlook could change if the Fed feels a need to push the economy into recession to contain inflation expectations, but at this time we believe that is unlikely if growth and inflation slow in H2, as we expect.

China's COVID-19 policies and any wide-ranging European embargoes on Russian oil and gas are risks to global growth and inflation should they create new supply shocks.

Fig. 1 US consumer sentiment has softened, but manufacturing business confidence remains robust

US consumer sentiment and manufacturing confidence



Source: Bloomberg, Standard Chartered

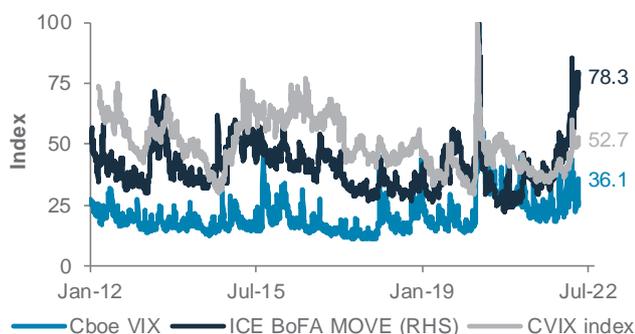
Should I start buying bonds?

It is logical to ask whether today's bond yields offer an opportunity for long-term investors to accumulate bonds. As we noted last month, we would argue it does, but very selectively where risk/reward is justified by a range of drivers. EM USD government bonds are one example of where we do see an increasingly attractive opportunity, given credit spreads have also weakened significantly. High Yield bonds are another, both in US/Europe, where credit quality is holding up, and in Asia, where valuations remain close to extremes.

It is possible bonds start looking attractive more broadly at some point, especially if economic growth starts to slow towards or below trend. However, bond yields could go higher near term as central banks stay hawkish. Hence, we would wait for Fed guidance to assess whether the market repricing of rate hikes is done. This could possibly mean the 10-year US government bond yield rises modestly above 3.00% first.

Fig. 3 Volatility has risen across most asset classes recently, most notably in bonds and currencies

Equity, bond, FX volatility; 100=max value in last 10 years



Source: Bloomberg, Standard Chartered

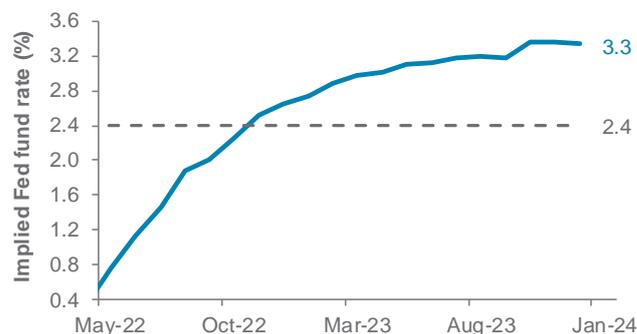
Taking advantage of volatility

One outcome of the rapid repricing of Fed rate expectations over the past month has been an extended period of volatility, not only in equities, but also in bond and currency markets.

For currencies, the continued rise in yields has meant the USD rally has extended for longer than we expected. Having

Fig. 2 Markets expect Fed rates to cross the 2.4% 'neutral' estimate, but this appears a risk more for 2023

Market pricing of Fed funds rate over next two years



Source: Bloomberg, Standard Chartered

said that, we continue to believe that once US rate hike expectations are fully priced in and expectations start to catch up elsewhere (most notably in Europe), the USD is likely to reverse. To take advantage of the volatility, we continue to prefer the AUD, CAD and NZD, where rate hikes by the respective central banks offer a good hedge against the risk the Fed rate hike repricing is not yet complete.

In equities, we also believe the relatively high volatility offers several opportunities. From a 6-12-month perspective, we continue to expect equities to outperform bonds and cash, especially with elevated inflation supporting nominal earnings. A US recession is likely to be the main risk to this view, but as our recession checklist from last month demonstrates, most indicators are not flashing a warning sign as yet. We would also note that, with the current market expectation of Fed rate hikes, policy rates would only approach the Fed's estimated 'neutral' level by year-end. This means worries of a tight Fed policy should be more of a concern for 2023 or later, not this year.

What about China?

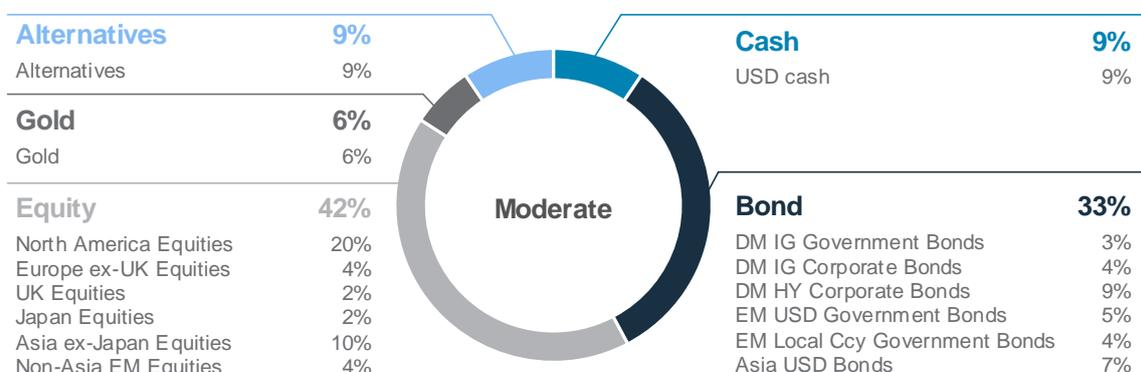
The economic shock from the continued lockdown is proving to be a dominating factor for Chinese equities, bonds and currency markets. Given the widespread restrictions on economic activity, it is possible the market weakness extends until the most acute phase of the lockdowns is over. This makes timing a bottom in Chinese equities very difficult.

Having said that, we believe the four factors we outlined in recent months behind our positive 6-12 month view on Asia ex-Japan equities remain valid: supportive China policies, the pessimistic outlook already priced in, Asia ex-China's gradual emergence from COVID-19 and several Asian markets' correlation to a global recovery. Chinese policy support for the economy remains a key assumption, but we are likely to see greater fiscal support once lockdowns are eased, given this is when the impact on demand is likely to be greater.

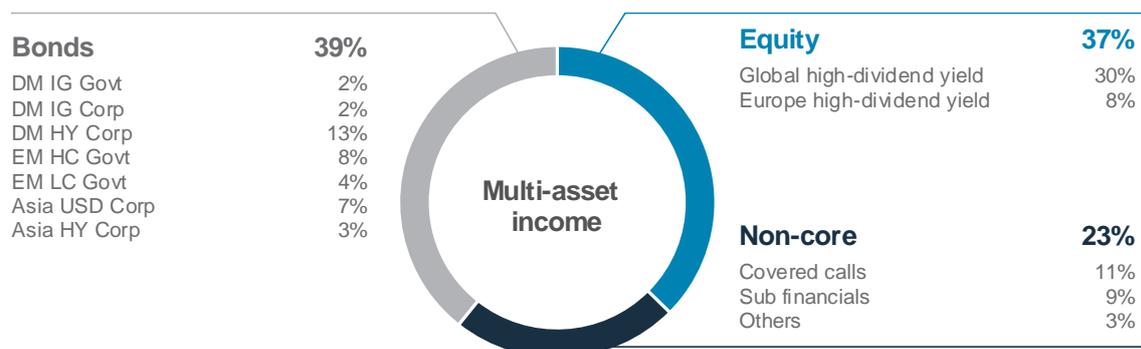
Closing bond yield differentials between US and Chinese government bonds could place further downward pressure on the CNH in the short term. However, this is likely to fade if the USD does peak, as we expect.

Tactical asset allocations

Global* allocation for a moderate risk profile



Multi-asset income allocation for a moderate risk profile



	View	Detail
USD cash	◆	+ Safety, ability to invest opportunistically - Very low yield
Bonds		
DM Govt	▼	+ High credit quality, rising yields - Outperformance difficult due to low yield level
DM IG Corporate	▼	+ High credit quality - Very sensitive to rising US bond yields, expensive
DM HY Corporate	▲	+ Attractive yield, low rate sensitivity - Falling credit quality
EM USD Govt	▲	+ Attractive yield, attractive value - Sensitive to rising yields
EM Local Ccy Govt	◆	+ Moderate yield, USD weakness over 6-12 months - Rising policy rates in some EMs
Asia USD	▲	+ Moderate yield, low volatility - Default contagion risks
Equities		
North America	◆	+ Above-trend growth, earnings rebound - Faster Fed tightening, rising cost pressures
Europe ex-UK	◆	+ Above-trend growth, policy support - Ukraine crisis impact, rising cost pressures
UK	◆	+ Attractive valuation - Policy tightening risk, Brexit-related uncertainty
Japan	▼	+ Global economic recovery, policy support - China slowdown, structural deflation
Asia ex-Japan	▲	+ Earnings rebound, China policy support - COVID-19 risk, regulatory tightening
Gold	▲	+ Weak USD, equity volatility hedge - Return of risk appetite, short-lived inflation
Alternatives	◆	+ Diversifier characteristics - Equity, corporate bond volatility

Source: Standard Chartered Global Investment Committee; *See page 17 for our Asia-focused allocations

Legend: ▲ Most preferred | ▼ Least preferred | ◆ Core holding

Perspectives on key client questions

Audrey Goh, CFA
Senior Cross Asset Strategist

Hannah Chew
Portfolio Strategist

Twin tightening – a double whammy for risk assets?

The US Fed began its rate hiking cycle last month with a 25bps rate hike. Markets are now pricing a Fed rate of 2.75% (from just 0.80% estimated in January) by the end of the year. Meanwhile, the Fed's meeting minutes suggest quantitative tightening (QT) is likely to start in May. The Fed is expected to reduce the size of its bond holdings eventually by USD 95bn/month, marking the second time it will hike rates and reduce its balance sheet concurrently. This would make it one of its most aggressive policy tightening cycles in recent decades. Against this backdrop, the volatility of major asset classes has spiked: bond volatility approached 2020 recession highs, while equity volatility hit levels above the end-2018 levels when the Fed last undertook twin tightening. We look to the prior episode of twin policy tightening (rates and balance sheet) to see which asset class did well or poorly when both policy tools were tightened together, and how investors might prepare their investments against this backdrop.

Faster pace of tightening today, but level not necessarily tighter

The Fed is expected to start contracting its balance sheet in May after delivering the first interest rate hike in March. While the pace of asset reduction is almost double that of four years ago (USD 95bn/month vs USD 50bn/month), the underlying economic conditions are vastly different.

Inflation and economic growth are much higher and labour markets much tighter today, compared with 2017 (see figure 4). The real (net-of-inflation) 10-year government bond yield was 50bps at the start of twin tightening in 2017 (vs -10bps now) and hit 115bps by the end of 2018, driving market volatility higher and triggering the 2018 repo crisis.

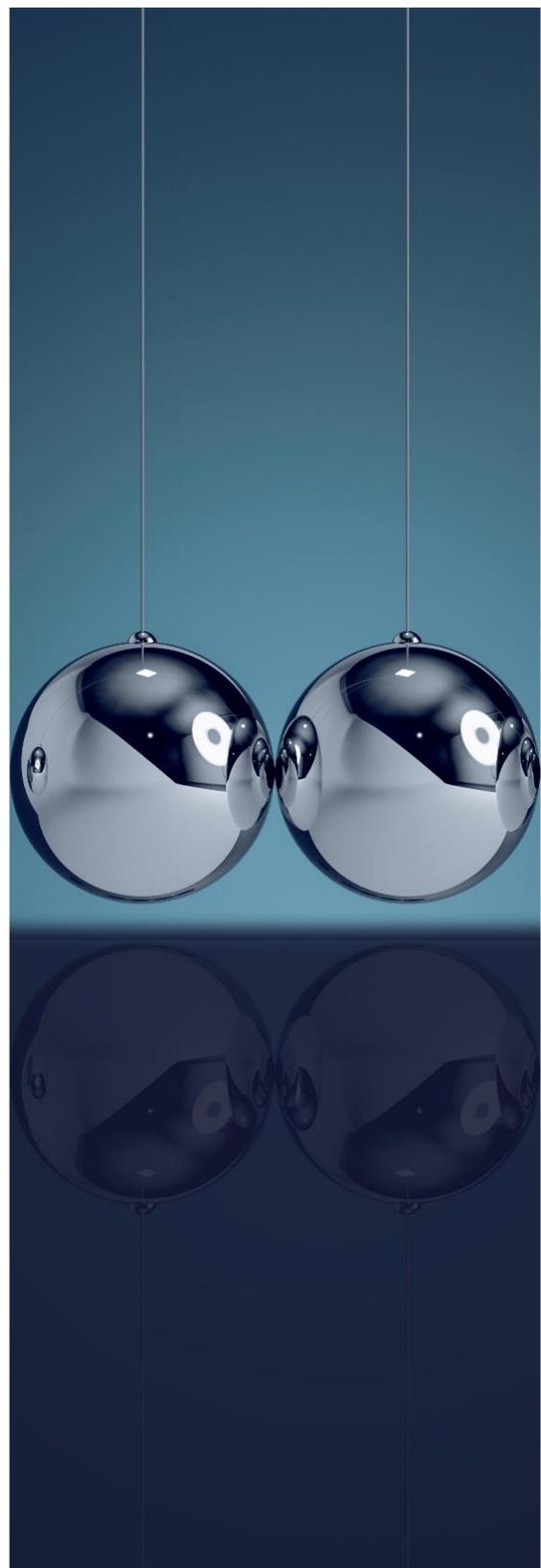
Financial conditions are arguably looser today, despite a much tighter labour market and higher inflationary concerns. Therefore, it probably makes sense for the Fed to tighten more aggressively now to play catch-up.

Fig. 4 Economic conditions are vastly different now, driving a faster pace of policy normalisation, compared with 2017

	2017–2018*	2022 - ?**
US consensus GDP growth (annual YoY)	2.2%	3.5%
US unemployment rate	4.3%	3.8%
US jobless claims	260k	171k
US CPI inflation	2.2%	8.5%
Fed balance sheet size prior to QT	USD 4.42trn	USD 8.90trn
Pace of QT	Gradual phase in over 12 months, with a peak of USD 50bn per month	QT to reach USD 95bn per month within the first 3 months from start
QT initiation since the first hike	2 years after the initial rate lift-off	1 FOMC meeting after initial rate lift-off
Pace of rate hikes	225bps increase in 37 months	Markets expect Fed rate to end 2022 at 2.75%

Source: Bloomberg, Standard Chartered

*Data at the start of QT unless otherwise stated; ** Data as of 28 April 2022

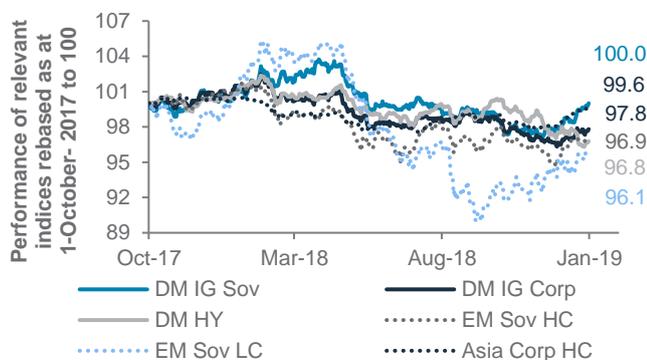


Poor returns on bonds during Fed tightening

Bonds delivered zero to negative returns, with elevated volatility, when QT and higher rates occurred simultaneously in 2017-2018. While bonds were rangebound initially, they fell subsequently on renewed expectations of tighter monetary policy and higher real yields. Long maturity assets, such as DM Investment Grade government bonds sold off, while EM local currency bonds were also impacted by a stronger USD. The performance of bonds only started to improve once real and nominal yields peaked in November 2018, and the Fed turned decisively dovish in 2019. TIPS (Treasury inflation-protected securities) bonds were flat and only China government bonds delivered positive returns in this period.

Fig. 5 Challenging for bonds to perform until real rates or inflation peak

Performance of bond assets during twin policy tightening*



Source: Bloomberg, Standard Chartered

*Twin policy tightening refers to the Fed conducting both rate hikes and Quantitative Tightening measures concurrently

Strategies for bond investors: Rising yields have been a challenge for fixed income assets over the past two years.

Bonds remain least preferred, particularly DM IG Sovereign and Corporate bonds. We retain a neutral duration stance, given upside risks to inflation. That said, higher rates tend to slow economic growth and it is possible that bonds, particularly long-tenure bonds, could start looking more attractive, especially if growth starts to slow going into next year. Hence, removing exposure to rate sensitive assets entirely may also not be an optimal decision. At higher levels of bond yields, possibly when US 10-year government bond yield rises modestly above 3%, some exposure to higher quality bonds may be warranted to help mitigate risk late in the cycle.

Investors can also consider Chinese government bonds, with authorities embarking on an easing cycle, and to some extent, US Treasury inflation-protected securities (TIPS). However, if the Fed is successful in lowering inflation expectations, then regular bonds will likely outperform TIPS.

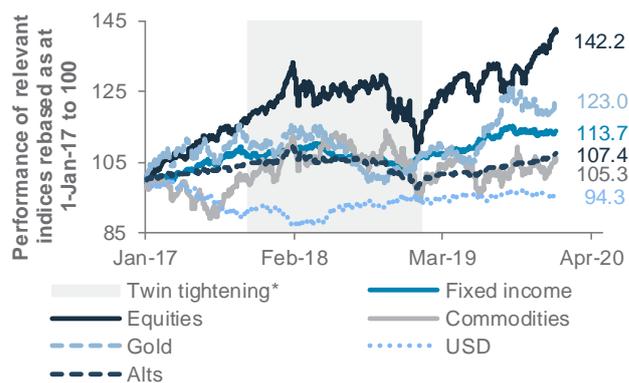
Equities went up then down in 2018

Equities did well in the initial part of twin policy tightening, but eventually, performance started to diverge as volatility picked

up on the back of growth concerns. Investors would have been better off overweighting risk assets in the early part of the twin tightening and reverting to a neutral/underweight positioning by late 2018. Within equities, the US, Japan and the commodity sector were the clear standouts, outpacing other key regions in the first 12 months of twin tightening.

Fig. 6 Equities did well initially, but struggled to deliver returns against a hawkish policy backdrop

Performance of assets during twin policy tightening*



Source: Bloomberg, Standard Chartered

*Twin policy tightening refers to the Fed conducting both rate hikes and quantitative tightening measures concurrently

Ample liquidity this time

While it is unclear how much liquidity is considered as ample, the starting point of the Fed's balance sheet is much larger at USD 8.5trn (vs 4.5trn in October 2017). The rate of balance sheet tightening is expected to run at c.12% per annum of the initial balance sheet size vs c.13% in 2017. Bank reserves and other forms of money are also more plentiful this time.

Should there be a liquidity squeeze due to QT, there are tools institutions can access via Fed's new standing repo facility or through existing swap lines with other central banks, which can help mitigate a liquidity fallout like that of late-2018. The flip side is this may well embolden the Fed to be more aggressive on its tightening plan than it otherwise would have been. Hence, we retain a less preferred stance on bonds.

Strategies for equity investors: We continue to prefer equities and expect volatility to stay elevated. Lower real yields and global equities having already fallen c.11% YTD mark two key differences with the prior start of QT, suggesting a lot of tightening concerns may now be priced. A rise in the chances of a recession is a key risk; hence, we would consider exposure to risk hedges such as gold or holding a greater cash (USD) buffer alongside as tightening becomes more advanced. Gold's performance was lacklustre during 2017-2018, which is not entirely surprising as it tends to do poorly during periods of tightening. Given the war in Ukraine, though, gold and other commodity-based assets may potentially serve as good hedges this time, especially if a long-drawn conflict prolongs commodity shortages and supply chain disruptions.

Our thematic ideas

Hannah Chew
Portfolio Strategist

A brief overview of our currently open thematic ideas, coupled with some recent highlights

 Key themes	
Embracing a digital future	<p>Our 5G/Internet of Things (IoT) and Cybersecurity themes have performed well relative to global equities, despite recording negative returns since the start of 2022. The strong price performance for Cybersecurity, especially since the Ukraine invasion, highlights the growing demand tailwind stemming from the war. We continue to prefer the Cybersecurity theme amid strong earnings upgrades, which in turn supports its rich valuations (12-month forward P/E of 33.0x). IoT valuations have fallen considerably and look attractive compared with global equities after accounting for their strong growth expectations (21.2x vs 15.2x, respectively).</p> <p>Government spending on digital infrastructure remains pivotal in sustaining the long-run sustainability of the theme. For instance, a breakdown of the Australian Federal budget shows AUD 130.1m will be spent over 2022-2025 as part of the Digital Economy Strategy to drive digital transformation. Over the longer term, the International Data Corporation expects spending on computer and storage infrastructure to deliver a compound annual growth rate (CAGR) of 12.6% between 2021 and 2026, reaching USD 133.7bn. The investments channelled towards reshaping and sustaining a safe digital environment confirm the growing importance and longevity of this theme. Hence, we continue to see the potential for these themes to outperform the broader market over a long-term horizon of 3-5 years.</p>
The winds of climate change	<p>Climate-related themes have fallen since last month's update. Most notably, Electric Vehicles (EV) are the worst hit, down c.22% since their peak in January. Precious metals used in EV batteries, such as lithium, nickel and aluminium, have seen a sizeable uptick in prices since 2020. With demand for lithium-ion batteries surging, there are concerns that the EV sector could face challenges in terms of a looming supply shortage for batteries, especially with the ongoing Ukraine war and Russia being a major exporter of key materials.</p> <p>Earnings revisions are trending lower across the board. However, valuations have also dropped slightly since our last update (12-month forward P/Es of Clean Tech, EV, Water and Green Infrastructure at 28.4x, 17.2x, 22.0x, and 19.3x, respectively).</p> <p>Although the energy transition narrative has been boosted by the recent push for energy security (especially in Europe), the shift towards green energy further exacerbates metal shortages as clean technologies require significant amounts of metals and supply chain disruptions are likely to persist in the near term. However, renewable energy developers are adapting and learning to source from alternative suppliers. This supply constraint is also giving rise to concepts such as the circularity of materials used in renewable energy, including EV batteries. While this is a near-term headwind, we continue to view more positively on the future outlook for climate investing, given its importance in global mandates of combating climate change.</p>
China's 'Common Prosperity'	<p>China's 'Common Prosperity' theme has been greatly challenged with the hard-tech manufacturing and green renewable themes down over 30% each since the start of 2022. China's Omicron wave and its zero-COVID policy leading to lockdowns in Shanghai and other regions have weighed negatively on investor sentiment. However, the authorities are beginning to introduce measures to resume production and mitigate disruptions to industries affected by the lockdowns. Additionally, valuations for high-tech manufacturing and renewables (12-month forward P/E of 18.5x and 13.8x, respectively) continue to fall, ie, they appear increasingly attractive against both the global and Chinese equity market (12-month forward P/E of 15.2x and 9.7x, respectively).</p> <p>Nonetheless, China's commitment to 'net zero' climate goals was reconfirmed in its recent announcements. According to the National Development and Reform Commission, China will add 140 gigawatts of capacity from clean energy resources, which is more than the rest of the world combined in 2020. We also see these efforts at utilising renewable energy to meet energy demands as positive for domestic Chinese hard-tech and semiconductors businesses, as the latter are key for China to adopt clean technology.</p> <p>Moreover, more than half of China's recent USD 2.3trn infrastructure plan will be directed to support the manufacturing and service industries. This emphasis also reflects China's commitment to ensuring its dominant share in global manufacturing, especially in areas such as EV, renewable energy and microchips. Thus, we remain convinced that this investment theme has plenty of room to run in the coming years.</p>

Source: Bloomberg, Standard Chartered

Macro overview at a glance

Rajat Bhattacharya
Senior Investment Strategist

Zhong Liang Han
Investment Strategist



Key themes

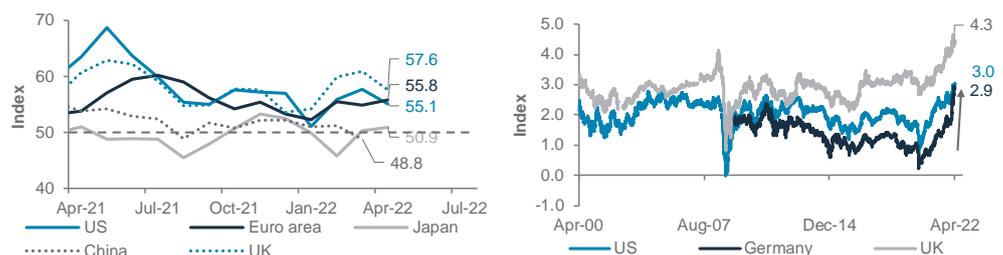
- We have further raised our end-2022 Fed policy rate expectations to 2.25%, 25bps higher than that anticipated a month ago. The revision is based on four main factors: (i) a sustained rise in US 10-year inflation expectations towards 3% as oil prices stay close to USD 100/bbl; (ii) the broadening of near-term inflation from goods to services; (iii) a tighter job market lifting wages; and (iii) robust business confidence data. Our end-2022 Fed rate call is below market estimates of c.2.75% since we expect the Fed to slow the pace of rate hikes in H2 as inflation decelerates. Our economic monitors continue to indicate a low probability of a US recession in the next 6-12 months, despite the decline in economic output in Q1 due to one-off factors.
- The continuation of the Russia-Ukraine conflict has led to downgrades in consensus global growth estimates, especially for Europe. However, we still expect the European economy (like the US) to grow above its pre-pandemic trend this year amid still-accommodative monetary policies and new fiscal spending on defence and energy. We believe above-trend growth will enable the ECB to pursue its plan to end bond purchases in Q3 and start rate hikes as it tackles inflation. Meanwhile, China remains on the opposite end of the policy spectrum to the US and Europe – its restrictive COVID-19 policies have heightened growth risks. Hence, we expect policymakers to continue easing fiscal and credit policies to revive growth.



Key chart

While business confidence indicators remain robust in the US and Europe, long-term inflation expectations have broken higher, forcing central banks to singularly focus on taming prices

Fig. 7 The Fed, ECB and BoE turned hawkish as inflation expectations broke higher
Business confidence (PMIs) in major economies; US, Germany, UK inflation expectations*



Source: Bloomberg, Standard Chartered; *Based on breakeven rates from 10y inflation-protected bonds

Macro factors to watch

The outlook for global growth and inflation has turned more uncertain due to the Russia-Ukraine conflict, even as the impact of the pandemic starts to fade. In this fast-changing world, we plan to watch the following drivers to assess underlying fundamentals and anticipate policy decisions:

1. **US, Europe activity indicators:** Although the US GDP contracted in Q1 as surging imports detracted from strong consumption and private investment, underlying business indicators (PMIs) remain robust both in the US and Europe, pointing to above-trend growth this year. We expect services to drive growth as economies normalise after the pandemic by H2 and goods consumption slows.
2. **Inflation expectations, Ukraine war and oil prices:** The breakout in US and European inflation expectations in the past month was triggered by the Ukraine war, which led to a surge in commodity prices. Any escalation (which halts Russian energy supplies) could fuel inflation further. In the US, inflation pressures were already building, with the acceleration in wages, shelter and services sector

costs. The tight US job market is another inflation catalyst. As COVID fades, we expect more workers to return to jobs, alleviating wage pressures. We expect US inflation and inflation expectations to peak in H1, partly also due to base effects, as long as the Ukraine war does not spiral. This should allow the Fed to turn less hawkish in H2, even if inflation remains well above its 2% target.

3. **China's policy measures:** China's zero-COVID policy has led to more than 50 cities going into some form of lockdown. The resulting downward pressure on growth is keeping a lid on global commodity prices, but it also means Beijing will need to stimulate the economy further to achieve its ambitious 5.5% growth target. The PBoC has already cut the bank reserve requirement and fiscal and credit impulse have turned positive. The upcoming Politburo meeting could signal more stimulus. We expect local governments to fast-track infrastructure spending. The restart of factory production in Shanghai is likely to ease supply bottlenecks. Further easing of COVID-19 restrictions should enable faster transmission of policy easing measures across the economy in H2.

Bonds at a glance

Abhilash Narayan
Senior Investment Strategist

Cedric Lam
Senior Investment Strategist



Key themes

- Tighter monetary policies and rising inflation remain headwinds for bond investors for now. Bond yields rose over the past month following hawkish Fed comments; there is a risk bond yields have not topped out yet. However, with markets now pricing in a Fed rate of about 2.75% by end-2022 and US core CPI showing tentative signs of decelerating, we expect the 10-year US Treasury yields to return a range of 2.50%-2.75% over 6-12 months.
- Developed Market (DM) High Yield (HY) and Asian USD bonds remain our preferred areas within bonds as we continue to view valuations as attractive for the risk on offer. We also like their low sensitivity to rising interest rates.
- We continue to prefer Emerging Market (EM) USD government bonds. Elevated commodity prices should remain beneficial to many EM net commodity exporters. We believe inexpensive valuations should offset their high sensitivity to bond yields.

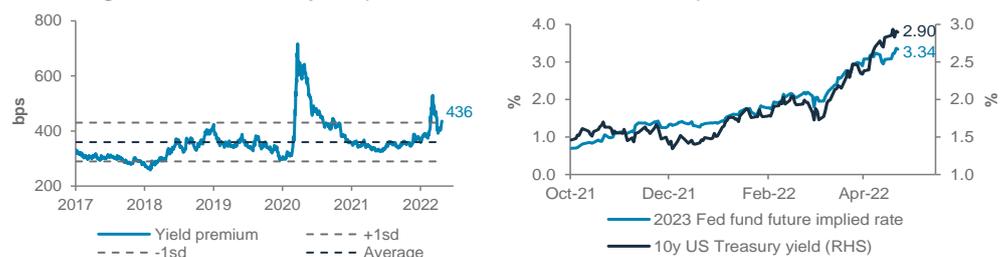


Key chart

EM USD government bond yield premium is at a multi-year high; recent hawkish Fed comments have raised rate hike expectations, with about 240bps of hikes priced till end-2022

Fig. 8 Attractive valuation on offer in EM USD government bonds; monetary tightening expectations have been front-loaded

EM USD government bonds yield premium; Fed Fund Futures implied US interest rate



Note: As of 25 April 2022. Source: Bloomberg, Standard Chartered.

Factors to watch in our preferred bond assets

Elevated March inflation data and more hawkish-than-expected Fed comments have driven government bond yields higher. However, the rise in bond yields could represent an attractive entry point for bond investors considering rebalancing, or adding to our preferred areas within bonds, ie, EM USD government or High Yield (HY) bonds.

DM HY bonds have extended their negative return since the beginning of the year. In the US, rising Fed policy tightening expectations have raised concerns about growth, especially the Fed's ability to achieve a "soft landing". In Europe, the Ukraine conflict persists, raising inflation risks. The yield on DM HY bonds has surged to over 7%, a multi-year high. Asia USD bonds, similar to their DM counterparts, have seen yields rise to a multi-year high of 5.5% owing to a COVID-19 wave spreading across China.

However, it is notable that this surge in yields has been largely driven by the rise in US government bond yields. Yield premiums, which measure the risk premia of credits over risk-free US government bonds, have been fairly contained, rising c.80bps and c.55bps for DM HY and Asia USD bonds, respectively, YTD.

We believe most factors supporting our preference for DM HY and Asian USD bonds should remain intact in the next 6-12 months. In DM HY, we see corporate fundamentals remaining strong, with recent Q1 earnings continuing the post-pandemic recovery, while sharply higher oil prices benefit the HY energy sector. In addition, we expect defaults to remain close to historical lows of roughly 1% for the rest of 2022, given the backdrop of still above-trend economic growth.

In Asia, Chinese authorities have been measured in easing policy. However, with lockdowns further impacting the outlook, we expect more stimulus measures to follow. Meanwhile, Asia ex-China USD bonds continue to see broad-based improvement in their credit fundamentals post pandemic, in line with their US and European counterparts.

EM USD government bonds have been among the worst-performing bond asset classes YTD, with rising government bond yields negatively impacting returns due to their relatively high interest rate sensitivity. However, we view EM USD government bonds as preferred since we believe current bond yields largely price in aggressive Fed rate hike expectations. We also expect EM commodity-exporting economies to benefit from elevated prices.

Equity at a glance

Daniel Lam, CFA
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Senior Investment Strategist



Key themes

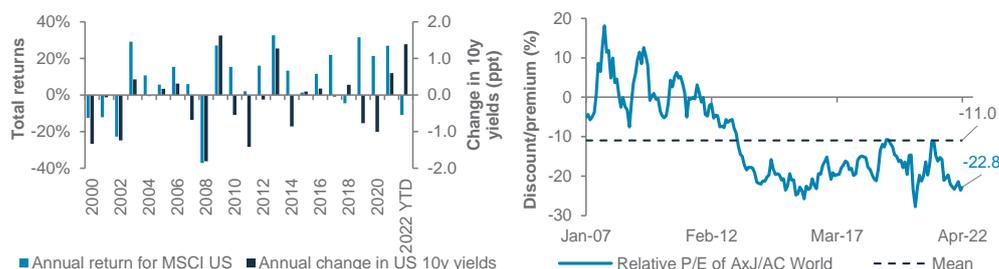
- Global equities remain a preferred asset class on a 12-month horizon. While earnings growth in 2022 is likely to slow significantly from 2021's extraordinary recovery, we believe equities remain attractively valued relative to other major asset classes such as bonds.
- Asia ex-Japan continues to be our most preferred equity market – the region's valuation is relatively undemanding. Geopolitical challenges have eased somewhat in China, compared with our update last month, but China has been combating the spike in Omicron cases, which clouds its earnings outlook in the short term. However, we continue to believe that Chinese equities are still likely to outperform global equities in the long term due to policy support and relatively cheap valuation.
- US equities continue to be a core holding. While the Fed has been increasingly hawkish, the Q1 2022 earnings season has been robust so far, and the pace of Fed policy tightening could slow in H2 2022.



Key chart

Fig. 9 Since 2000, US equities have registered positive returns in seven out of the eight years the US 10-year government bond yield rose; MSCI Asia ex-Japan is near a trough in terms of relative valuation vs the MSCI All-Country World index

Annual returns for MSCI US vs annual change in US 10-year government bond yield; relative valuation of MSCI Asia ex-Japan vs MSCI All-Country World indices



Source: MSCI, FactSet, Bloomberg, Standard Chartered

With an aggressive Fed rate hiking cycle likely priced in, we see potential for equities to reclaim ground over the rest of the year. Asia ex-Japan equities continue to be cheap and supported by China's policy easing

Higher yields do not equal bearish equities

The key development since our last update has been the increasingly hawkish tone from the Fed. This is reflected by the sharp rise in US bond yields, with the US 10-year government bond yield rising to close to 3%. However, is such a sharp rise in bond yields bearish for equities?

Not according to our historical review. Since 2000, US equities delivered positive annual returns in seven out of the eight years in which the US 10-year government bond yield rose. So far this year, US equities are down about 11%, while US 10-year yield has risen by over 130bps. We believe the market may have priced in Fed rate hikes too aggressively for the rest of this year given our expectation that inflation will slow later this year. Hence, our Global Investment Committee expects the US 10-year yield to retreat to 2.50%-2.75% later this year.

A peak in bond yields should alleviate concerns about the impact of higher rates on equity valuations. Thus, we believe there is room for equities to turn higher for the rest of the year.

More broadly, we believe equity fundamentals remain positive. 2022 EPS growth expectations have been revised up over the last four months. For example, US EPS is expected to grow at 9.4% in 2022 now, compared with 7.8% at the start of the year. Expectations have similarly risen for the Euro area (from 4.9% to 9.3%) and the UK (from 1.5% to 15.2%).

The revision in earnings growth remains relatively lacklustre in Asia ex-Japan (from 7.6% to 7.8%). Part of this could be attributed to the COVID-19 lockdowns in China. However, policies remain relatively supportive, compared with the US – for example, there has been monetary easing in China over the last few weeks, with more likely to come. Valuations in Asia ex-Japan equities remain very attractive vs the rest of the world, with Asia ex-Japan trading at a 23% discount.

Thus, we believe risk/reward favours staying invested in and adding to equities where appropriate by taking advantage of current market weakness. We also see the currently elevated equity market volatility as a source for generating income.

FX at a glance

Francis Lim
Senior Quantitative Strategist

Nataniel Tang
Investment Strategist



Key themes

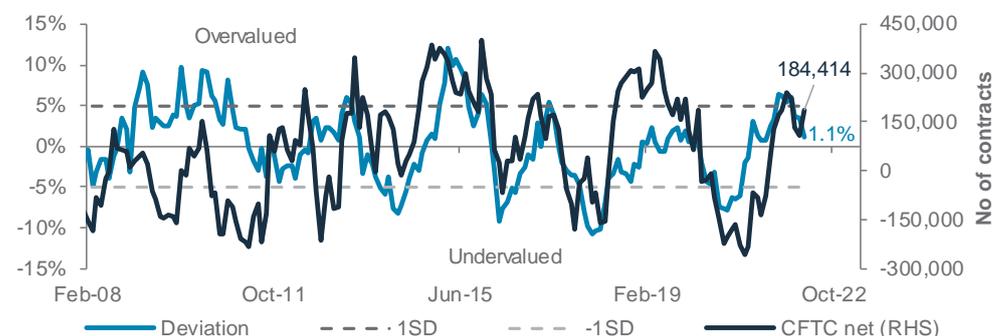
- Our 6-12-month USD view is bearish. We expect the USD to peak in Q2 as: i) Fed policy expectations reach peak hawkishness as growth eases along with inflation data; ii) global monetary policy continues to shift towards normalisation at varying speeds; iii) capital flows rotate away from the US towards more attractively valued assets; iv) steady de-dollarisation continues; and v) uncertainty rises around US politics and future policy direction. The speed and timing of the USD reversal, though, is likely to be driven by the evolution of the Ukraine war and China's zero-COVID policies.
- Technicals are nearing key levels. We expect the USD index (DXY) resistance around the 2017 high near 104 to contain any final push higher, notwithstanding even more Fed hawkishness or geopolitical escalation. We also expect the EUR and the JPY to begin at least a corrective rally after what has been a period of heavy selling. Commodity currencies should continue to be underpinned and the bifurcation of energy exporter currencies versus importers is likely to continue by varying degrees.
- Key risks for further USD strength are: i) a rise in US household and business credit expansion despite rising interest rates that exacerbates inflation and prompts the Fed to "chase" at a faster rate to subdue inflation and ii) depressed risk sentiment that weighs on the global economy and reduces the attraction of USD alternatives. Above 104 in the DXY targets 109 next.



Key chart

Our proprietary DXY valuation model uses real yields, equity prices, inflation, current accounts and commodities as inputs. A significant deviation from 0% implies potential USD misvaluation. Despite the recent USD rise, it is less overvalued but long positioning is rising again

Fig. 10 Our model suggests the USD is approaching fair value; long positioning rising
Deviation of DXY value vs our model; CFTC net USD positioning



Source: Bloomberg, Standard Chartered

A transitioning USD

We believe the Fed will not hike rates as many times as the market currently expects, and non-US central banks have room to turn more hawkish. Nominal yield differentiation, which has supported the USD should fade. There is potential for USD selling to gain traction through the summer as the focus shifts to US mid-term elections and rising policy uncertainty. We expect a "two-tier" USD to continue even as we anticipate a broad USD peak. Commodity exporter currencies with hawkish central banks (AUD and CAD) should continue to outperform commodity importer currencies with dovish central banks (EUR and CHF).

Two uncertain variables could determine the USD peak. Firstly, the Ukraine war, where any eventual de-escalation should lead to improved risk sentiment, and inflationary pressure could still prompt the ECB to move quickly to normalise monetary policy while the window is open.

Secondly, China may claim victory against COVID-19 as the summer nears and cases naturally peak, allowing targeted fiscal stimulus to be deployed during economic re-opening. Both events would support a rebound in global growth and add momentum to a sustained USD reversal.

We continue to prefer the AUD, CAD and NZD as commodity prices should remain elevated and their respective central banks are focused on countering inflation. The EUR should be an eventual key beneficiary of a USD peak. We continue to believe that the JPY is undervalued, oversold and ripe for a surprise reversal. Any sign of the BoJ acknowledging rising inflation expectations could trigger the relaxation of yield curve control and a sudden move to unwind carry trades. Finally, USD/CNH has rallied sharply, but we expect resistance above 6.70-6.80 to slow the rise as Covid lockdowns eventually end.

Gold, crude oil at a glance

Manpreet Gill
Head, FICC Strategy

Nataniel Tang
Investment Strategist



Key themes

- We believe gold continues to be an attractive portfolio diversifier and is likely to trade back above USD 2000/oz, with the potential to achieve a new all-time high. Extreme Fed hawkishness, which placed upward pressure on real (net-of-inflation) bond yields, triggered the recent correction, but we expect technical support around 1,875 to 1,900 to hold. Gold should perform well once, as we expect, the Fed raises rates by a little less than markets expect and the USD peaks. Gold's core "risk-off" safe-haven status, physical demand from India and China and rising reserves allocation are also supportive.
- We expect oil prices to remain underpinned by potential supply risks and/or strong demand as COVID-19 restrictions in Asia = ease and global growth picks up pace. The Ukraine war may reduce in intensity but sanctions are unlikely to ease quickly; European restrictions on Russian energy imports could rise and OPEC and US shale production increases take time and are subject to constraints. Geopolitical tension in and around the Middle East is also an ongoing risk. A negative shift in risk sentiment or strong demand destruction are the main risks to this view.



Key chart

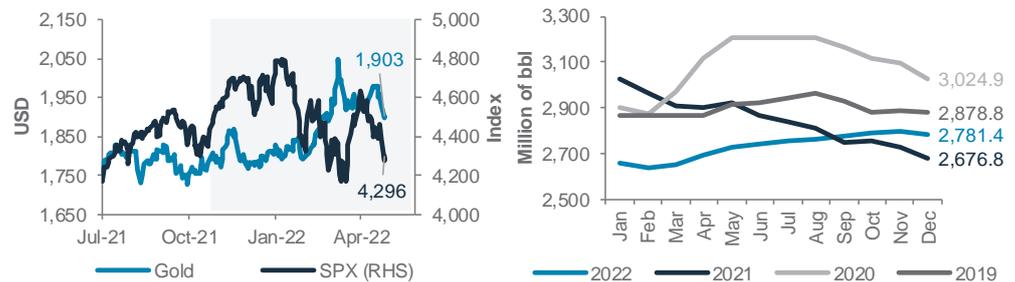
Gold offers an attractive hedge if inflation proves to be higher, or longer-lasting, than we expect. A modestly weaker USD is also a boon for the precious metal

US shale producers are less likely to respond to higher oil prices relative to pre-COVID-19 times due to higher capex discipline

Fig. 11 Gold has been an effective hedge against equity market drawdowns; OECD crude oil and liquid fuel inventory is likely to remain at a 4-year low through most of 2022

LHS chart: Gold vs S&P500 Index*

RHS chart: OECD crude oil and liquid fuel inventory from 2019 to 2022F**



Source: Bloomberg, Standard Chartered

*Shaded area is from 22 October 2021, when we upgraded gold to most preferred; **US Dept of Energy

The outlook for gold and oil

Increasingly hawkish Fed expectations have been a headwind for gold's expected advance. In our view, Fed rate hikes may run into constraints of financial market and housing market volatility, which could initially keep real rates subdued, but eventually weigh too heavily on aggregate demand. If the Fed wavers from policy tightening, an inflationary impulse should support gold. The Fed may alternatively witness a deflationary impulse if China's COVID-19 lockdowns extend and/or the Ukraine war escalates. This will lean against Fed tightening initially, and as US interest rate headwinds abate, gold may get a boost from both a peaking USD and slowly improving economic growth in India and China, both important sources of physical gold demand. Geopolitical risks are likely to stay elevated with multiple potential flashpoints, a traditionally supportive backdrop for gold demand. In addition, given financial sanctions and the strategic leveraging of commodity

supplies, gold could significantly outperform as a safe-haven asset.

Oil prices are likely to remain underpinned by uncertainty over potential disruptions in supply as geopolitical tensions stay elevated and the weaponisation of currencies and financial systems spreads to commodities. This is particularly true of Russia, but Iran and the Middle East may also be vulnerable to both planned and unplanned supply constraints. US shale production may rise, but this usually happens with a lag. Fossil fuel underinvestment is still a supply overhang. Demand for oil from Asia is likely to rise when pandemic-related barriers recede.

Quant perspective

US market risk model – upgraded equity risk, but...

Francis Lim

Senior Quantitative Strategist

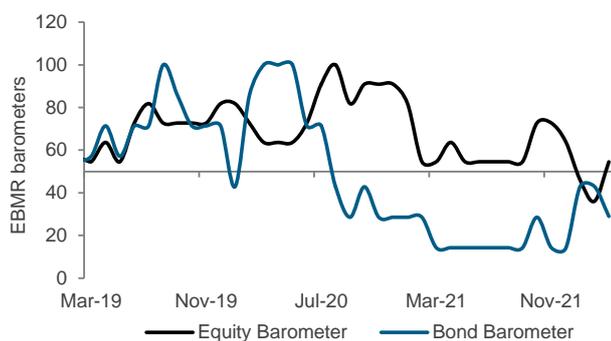
Be cautious of model's upgrade to equity risk

Our US Equity-Bond Market Risk (EBMR) models the downside risks in US equities and the 10-year US Treasuries. It uses 11 economic and market factors to create equity and bond risk barometers. If the value of a barometer falls below 50, it signals higher downside risks and vice versa.

The US EBMR model shifted back to Stage 3 in April after staying in Stage 4 for two months. This means the model remains against taking on excessive risk in US government bonds but is now in favour of taking on US equity market risk. However, we view this shift to be of lower quality than usual as the equity barometer improvement is primarily driven by modestly positive equity momentum signals that have been quite volatile. These signals have also deteriorated intra-month.

Fig. 12 EBMR turned bullish on equities

US equity and bond market risk barometers



Source: Standard Chartered

Furthermore, all rate factors, such as US 10-year government, corporate AAA and 90-day commercial paper yields, are currently negative factors in the equity barometer as the model views higher rates to be detrimental to equity market risks under a high inflation environment. Still supportive factors for the barometer are US money supply and housing starts, but with the former only slightly supportive as it has turned less and less bullish since the Fed-tapering in Nov-21.

Meanwhile, our bond barometer has deteriorated to 29 from 43, marking the 20th straight month of bearish signal for bond market risks. Over this period, the US 10-year government bond yield rose by c.215 bps (bond price falls as yield rises). Among factors that are depressing the bond barometer are high commodity prices and low US jobless claims. While industrial activity remains expansionary, as measured by US manufacturing PMI, these factors together signal room for the Fed to hike rates aggressively.

Our model's projections remain skewed towards Stage 3 over the coming months, but the probability of Stage 4 has noticeably increased to around 20+%, which is high compared with the past. This implies US equities could still outperform over the longer time frame, but this view carries a higher degree of uncertainty.

Implications on global assets

Data since 1999 suggest gold is the most preferred in Stage 3, which is consistent with the inflation narrative. The model's preference for the asset is based on its long-term relationship with the market cycle, which favours gold as an inflation-hedge under Stage 4.

Fig. 13 Scenarios over the coming months till August 2022 vs December 2021 (Outlook 2022) projections

Probability of the evolution of financial market risk cycle from the current Stage 3 and preferred assets

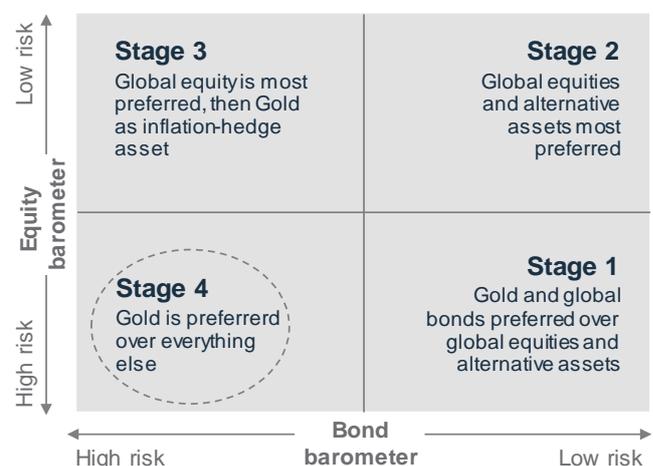
Model's estimated probabilities in December 2021

Stage	Dec-21	Jan-21	Feb-22	Mar-22
1	0%	0%	0%	0%
2	0%	0%	0%	0%
3	100%	100%	100%	99%
4	0%	0%	0%	0%

Model's estimated probabilities in April 2022

Stage	May-22	Jun-22	Jul-22	Aug-22
1	0%	1%	3%	2%
2	1%	4%	10%	12%
3	70%	73%	69%	73%
4	29%	22%	18%	12%

Source: Standard Chartered



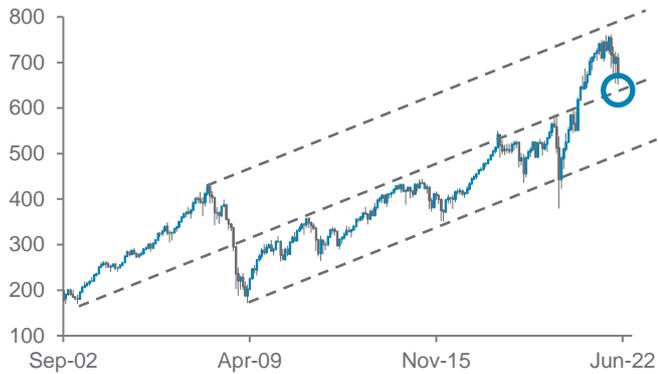
Technicals

Manish Jaradi

Senior Investment Strategist

Fig. 14 Global equities: Range view intact

MSCI All Country World index monthly chart with MACD



Source: Refinitiv, Standard Chartered

The range view articulated in last month's Technicals section remains unchanged. The lower end of the range is the middle line of the channel (now at 641) and the top end of the range is the January high of 761. Only a break below the middle line would imply that the broader upward pressure has faded.

Fig. 15 Asian equities: Still searching for a low

MSCI Asia ex-Japan index monthly chart

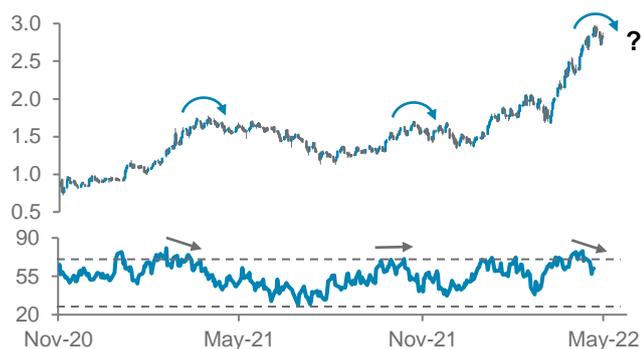


Source: Refinitiv, Standard Chartered

The index is testing crucial support at 716. The break of a key pivot in the past has, at the very least, led to a multi-month range (the most recent break occurred in January). Hence, this month's close will be crucial. A decisive break below the support could pave way towards 560 (16% below Thursday's close).

Fig. 16 US government bond: Close to an interim top?

US 10-year Treasury yield daily chart with RSI

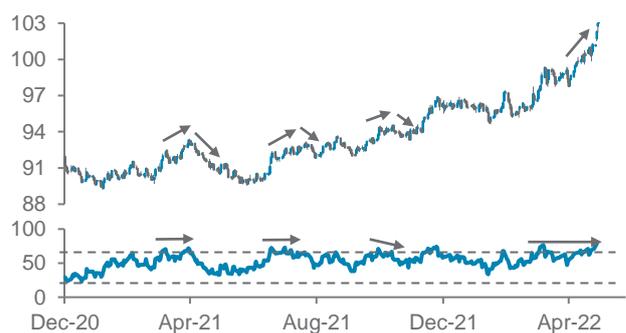


Source: Refinitiv, Standard Chartered

A negative divergence (rising yields associated with declining momentum) suggests the yield rally is showing signs of fatigue. Put together, since the target of the reverse head & shoulder pattern of 3.0% (highlighted in the 2022 outlook) has been met, the bar for an imminent bullish break above major resistance at 3.26% is now higher.

Fig. 17 USD: Signs of rally fatigue

DXY daily chart with RSI



Source: Refinitiv, Standard Chartered

As in the bond yield chart, there is a negative divergence in the DXY chart, just as it tests strong resistance at 103-104 (highlighted last week). Faltering momentum at major resistance levels often reduces the likelihood of an imminent bullish break. Moreover, any break below 99.40-99.60 would confirm that the upward pressure has faded.

Tracking market diversity

Francis Lim
Senior Quantitative Strategist

About our market diversity indicators

Our market diversity indicators help to identify a potential change in short-term trends due to a fall in market breadth across equities, credit, FX and commodities. When market diversity falls, it implies either buyers or sellers are dominating, leading to a rapid rise or fall in asset prices. This is usually unsustainable and is likely to be followed by a slowdown or a reversal. Our diversity indicator is based on a statistical index called fractal dimension; a value below 1.25 serves as a guideline that prices are rising or falling too fast.

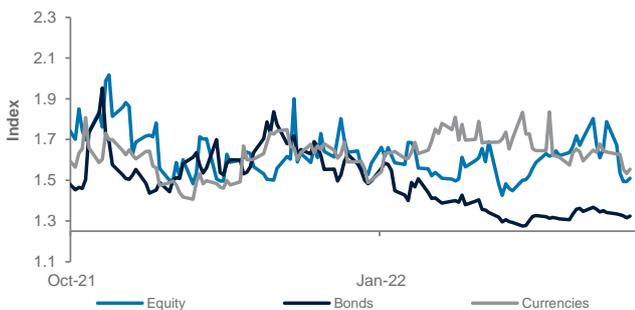
Where is diversity falling or rising this month?

Since March, investor diversity has broadly narrowed, but it remains high for equities as they trade in a range amid elevated market volatility. For bonds, diversity remains depressed – we see our indicators continuing to point towards a reversal risk in DM bonds.

However, as we mentioned in March, any reversal risk in DM bonds is more dependent on market expectations of Fed rate hikes as monetary policy is currently the key driver behind the negative momentum in these assets. This means our diversity indicator for DM bonds could remain stretched for some time, until there is a material shift in Fed hike expectations.

Fig. 18 Diversity of bonds remains stretched

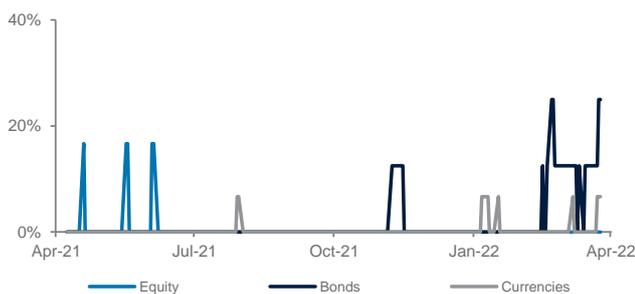
Average market diversity score by asset class



Source: Standard Chartered

Fig. 19 Red flags in bonds, but a lot depends on policy

Percentage of assets with diversity score <1.25



Source: Bloomberg, Standard Chartered

In currencies, we are also seeing some significant shift in market diversity due to a strong USD. Most notable is the diversity on USD/JPY (+11.3% since February) – the diversity value is now significantly below the threshold of 1.25, indicating heightened risk of a reversal. GBP/USD and USD/MYR are two other USD-based pairs to watch due to significant USD strength as their diversity values are edging towards 1.25. The GBP/USD has fallen 4.9% since February, while USD/MYR has risen 3.7% over the same period.

Among equity sectors, investor diversity in the China IT sector is approaching the 1.25 threshold. The sector has been affected by policy crackdown and poor investor confidence. We also flagged the US energy sector last month, but its diversity has improved since due to a 9% correction in the past week.

Fig. 20 Diversity across key assets/sectors

Level 1	Market diversity	30-day diversity trend
FTSE World Broad IG Bond	○	→
MSCI All Country World	●	→
Gold	●	↑
HRFX Global Hedge Fund Index	●	↑
US Sectors		
Information Technology	●	→
Energy	◐	↑
EU Sectors		
Information Technology	●	→
Energy	◐	↑
China Sectors		
Information Technology	◐	→
Energy	●	↑
Commodities		
WTI	●	↑

Source: Bloomberg, Standard Chartered; as on 25 April 2022

Legend: ○ Very low ◐ Low/moderate ● High

Asset allocation summary

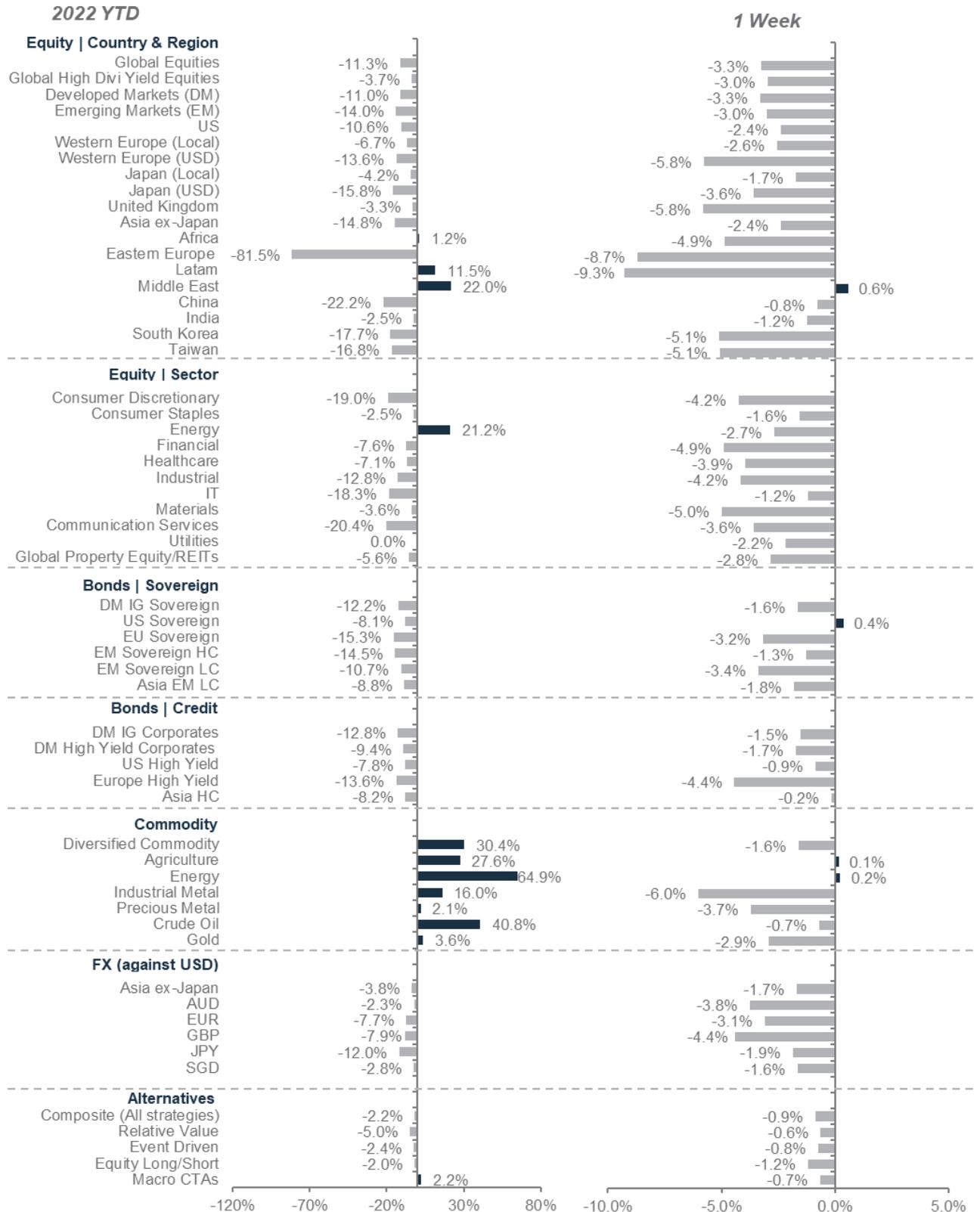
Summary	View	ASIA FOCUSED				GLOBAL FOCUSED			
		Conservative	Moderate	Moderately Aggressive	Aggressive	Conservative	Moderate	Moderately Aggressive	Aggressive
Cash	◆	21	9	4	0	21	9	4	0
Fixed Income	▼	56	33	23	6	56	33	23	6
Equity	▲	23	42	57	84	23	42	57	84
Gold	▲	0	6	6	6	0	6	6	6
Alternatives	◆	0	9	9	4	0	9	9	4
Asset class									
USD Cash	◆	21	9	4	0	21	9	4	0
DM Government Bonds*	▼	4	2	2	0	5	3	2	1
DM IG Corporate Bonds*	▼	5	3	2	1	7	4	3	1
DM HY Corporate Bonds	▲	11	6	5	1	16	9	6	2
EM USD Government Bonds	▲	12	7	5	1	9	5	4	1
EM Local Ccy Government Bonds	◆	10	6	4	1	8	4	3	1
Asia USD Bonds	▲	15	9	6	2	12	7	5	1
North America Equities	◆	6	12	16	23	11	20	27	40
Europe ex-UK Equities	◆	5	9	12	17	2	4	6	9
UK Equities	◆	1	2	3	4	1	2	3	4
Japan Equities	▼	1	1	2	3	1	2	2	3
Asia ex-Japan Equities	▲	8	15	20	29	5	10	14	20
Non-Asia EM Equities	◆	2	4	5	8	2	4	5	8
Gold	▲	0	6	6	6	0	6	6	6
Alternatives	◆	0	9	9	4	0	9	9	4

Source: Standard Chartered; *FX-hedged

All figures in %; Allocation figures may not add up to 100 due to rounding

Legend: ▲ Most preferred | ▼ Least preferred | ◆ Core holding

Market performance summary*

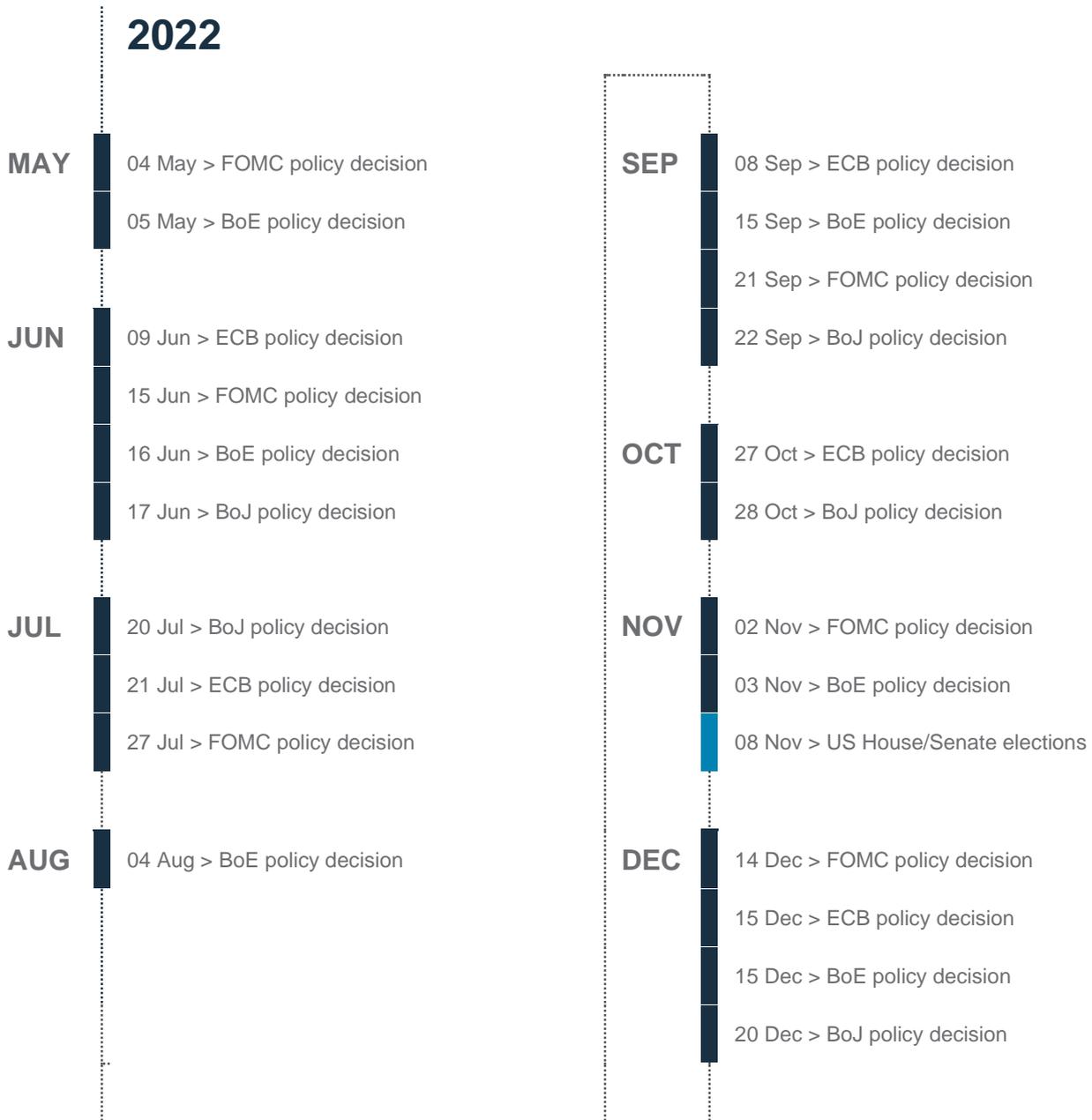


Source: MSCI, JPMorgan, Barclays, Citigroup, Dow Jones, HFRX, FTSE, Bloomberg, Standard Chartered

*All performance shown in USD terms, unless otherwise stated

*YTD performance data from 31 December 2021 to 28 April 2022 and 1 week-performance from 21 April 2022 to 28 April 2022

Key events



■ Central bank policy | ■ Geopolitics | ■ EU politics

X – Date not confirmed | ECB – European Central Bank | FOMC – Federal Open Market Committee (US) | BoJ – Bank of Japan | BoE – Bank of England | RBA – Reserve Bank of Australia

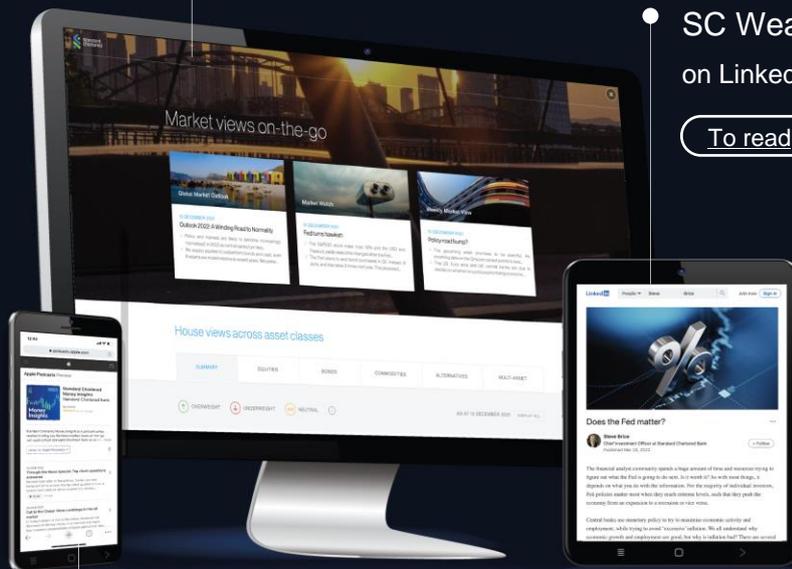
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1. The figures on page 5 show allocations for a moderate risk profile only – different risk profiles may produce significantly different asset allocation results. Page 5 is only an example, provided for general information only and they do not constitute investment advice, an offer, recommendation or solicitation. They do not take into account the specific investment objectives, needs or risk tolerances of a particular person or class of persons and they have not been prepared for any particular person or class of persons.

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