

# Balancing the risks

## Global Market Outlook (In-brief)

August 2019

# Investment strategy

## Balancing the risks

- Our Global Investment Committee continues to see the current slowdown as a temporary soft spot, but acknowledges rising risks of a deeper downturn. Therefore, we take a balanced, barbell-like view across equities and bonds.
- We have a preference for credit and other multi-asset income strategies in what may be a renewed 'search for yield'. Within credit, we prefer Emerging Market (EM) USD government bonds.
- Within equities, we maintain our preference for the US. We still see gold as a good way to hedge downside risks.

### Markets remain worried about the growth outlook

Equities pared some of their H1 gains as renewed trade tensions introduced new clouds over the growth outlook. Since June 30, global equities fell -2.4%, while G3 government bonds rallied +2.2%. For investors, the key question remains whether global growth is merely experiencing a temporary slowdown or is at the start of a deeper downturn, as investment implications differ dramatically under each scenario.

### Trade, yield curve negatives, but lead indicators positive

We refresh our framework to compare the current situation with prior slowdowns (1995/98) and recessions (2001/07). In our H2 outlook, we noted that only two of the six factors were negative, a significantly better situation than prior to 2001/07.

Since then, the intensity of these two negative factors has increased. The US economic situation, represented by the US job market, which continued to tighten, and the 10-year-2-year part of the yield curve has also inverted following a prior inversion of the 10-year-3-month curve (see the Perspectives section to know why this is a key recession, but not a timing, indicator). Meanwhile, geopolitics also worsened amid a rise in the number of risks that hold the potential to create a negative growth shock – the renewed rise in US-China trade tensions is well-known, but rising Korea-Japan trade tensions also pose a threat to North Asian

Figure 1

**Our framework argues this remains a temporary slowdown, but risks have risen**

Factors influencing risk assets over 12-24 months – our assessment

Medium-term factors	Current signal	Prior to mid-cycle rate cut (1995/8)	Prior to recession rate cut (2001/7)	Guide
Valuations	↔	↓/↔	↓/↓	S&P500 P/E; deviation from trend
US unemployment rate	↓	↑/↑	↓/↓	Level relative to business cycle range
US monetary policy settings	↔	↓/↓	↓/↔	Policy rate vs. estimates of neutral level
Inflation expectations	↑	↓/↑	↓/↓	Expectations relative to 2% 'target' (lower=positive for risk assets)
Geopolitics	↓	↑/↑	↑/↑	Current/impending financial market or supply side crisis
Financial excesses	↔	↔/↔	↓/↓	Excesses similar to mortgage debt (2007) or dot-com bubble (2001)

Source: Standard Chartered



## IMPLICATIONS FOR INVESTORS

We now have a balanced view between equities and bonds broadly. Gold is a good way to hedge downside risk

Within global equities, we prefer the US. Within Asia ex-Japan equities, we prefer onshore China

We prefer EM USD government bonds. Credit and other multi-asset income strategies likely to outperform government bonds

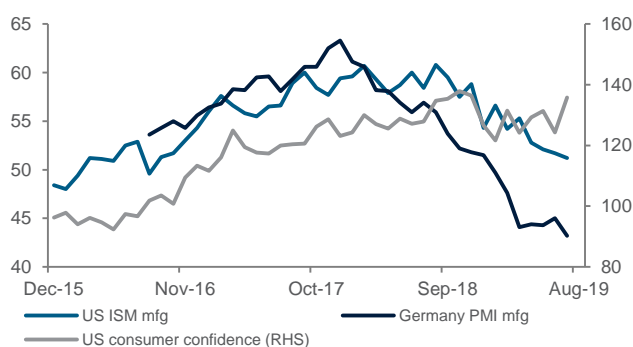
markets and the electronics manufacturing sector. In the UK, the risk of a no-deal Brexit has risen, posing a threat to UK and Euro area growth. Finally, political uncertainty remains elevated in Hong Kong.

However, other factors in our framework have not changed, with the lack of inflation pressure and/or financial excesses being particularly important. On balance, therefore, we believe the case for the current environment being a temporary slowdown remains in place. Having said that, the risks have clearly risen – in our assessment, US recession risks have risen to 40%, from 35% mid-year.

Figure 2

**Manufacturing continues to be very weak, but most so in Europe, while consumer confidence is holding up well**

US and Euro area manufacturing PMIs and US consumer confidence (RHS)



Source: Bloomberg, Standard Chartered

## Diversification more important than ever

The rise in risks – whether from our view of increased US recession risks or from a potential geopolitical shock – causes us to take a more balanced, barbell-like approach across equities and bonds, alongside a preference for gold.

Indeed, the last two months have been a lesson in the value of diversification. While many risky assets weakened, government bonds helped partially offset this as the significant fall in yields meant prices rallied. A barbell-like approach can help ensure investment allocations are not concentrated to benefit from one single scenario alone.

## Favour credit and other income assets

Within bonds, we have a strong preference for credit (ie. bonds that offer a yield premium over US Treasuries, including EM USD government bonds and corporate bonds) and, more broadly, multi-asset income assets.

This preference may appear somewhat odd, given our view of rising risks and an increasingly balanced allocation. However, we see two specific advantages of credit and multi-asset income strategies. First, a still reasonably attractive yield means investors are paid to wait while the global growth outlook plays out.

Second, credit (and income assets more broadly) also offers exposure to a third possible growth scenario – one of slow, but not recessionary, growth. European financials offer a valuable parallel – since end-2014, the steadily deteriorating growth outlook has meant that returns on financial sector equities have been negative. However, subordinated financial sector credit has ended up offering very strong positive returns. Arguably, while equities require growth to perform, credit can continue to do well as long as the ability to repay exists, even in the absence of significant growth.

Within credit, we continue to prefer EM USD government bonds as we see greater value here than in corporate bonds. Asian USD corporate bonds continue to rank second in our preference order for their relative stability.

## Region selection key in equities

Within equities, we continue to see a number of opportunities within each asset class. We prefer the US, which is clearly one market where higher frequency growth data remains noticeably stronger than other regions. US equities also have a track record of largely outperforming other regions in the late stages and at the end of the US business cycle.

Within Asia, we also maintain our focus on onshore China equities. While broader Asian equities may be at risk from any further escalation in trade tensions, onshore Chinese markets are likely to disproportionately benefit from any policy stimulus measures, in our assessment.

## Scaling back our bearish USD view

One of the risks we identified to our modestly bearish USD view was a resurgence of US-China trade tensions. With this risk indeed rising, as best illustrated by the rise in USD/CNY above 7.00, we scale back our view on the USD to a more balanced one given the USD peaking process is likely to complete only after current tensions abate.



# Perspectives on key client questions



## Should we be concerned about the inversion of the 2-year and 10-year US Government bond curve?

On 14 August, **the yield on the 10-year US Government benchmark rate dipped below that of the 2-year benchmark rate** (an event commonly referred to as yield curve inversion). It is the first time since the Global Financial Crisis (GFC) of '08-09 that this has happened, and **it follows other parts of the yield curve that had already inverted** earlier in 2019. (Figure 3)

Historically, yield curve inversions have largely preceded economic recessions in the US. We respect the importance of such a signal. However, the time gap between an inversion and a recession can be very wide, making it a somewhat less-than-perfect indicator over specific time periods. For example, 3 out of 10 inversion episodes were not followed by a recession in the subsequent 2 years.

### What is different this time around?

Our assessment of broader US economic data suggests that the US economy is in better shape than a yield curve inversion alone would indicate. (See the macro section for more). Other distortions this time around (eg. quantitative easing, negative term premium and a large pool of negative yielding debt globally) may decrease the efficacy of this indicator. Lastly, **there tends to be a long lead time between inversions and ensuing recessions (between 8 and 22 months).**

In previous business cycles, yield curve inversions have mainly been caused by the Federal Reserve **rapidly raising short-term rates** to cool down an overheating economy. At present, the inversion has, instead, been **led by the fall in long-term rates** as investors react to prospects of lower global growth and increased momentum in a flight to safety on the back of escalating trade tensions. Of the three times that the inversion of this part of the yield curve gave a false recession warning, two were characterised by falling long-term yields. One argument against an imminent recession is that this is the precise path being mirrored in today's markets.

Figure 3

**Inversion of the 2-year and 10-year Treasury notes yields has been a signal historically correlated with looming recessions. Will this time be different?**

Difference in yields between tenors of the US government yield curve expressed in basis points (bps)



Source: Refinitiv, Standard Chartered



The signalling power of the yield curve may be weaker than it has been historically due to changes in supply/demand dynamics of government bonds given the increasing pool of negative yielding debt across the globe. (c. USD16trn)

The current inversion has been preceded by weaker-than-expected economic data from not only the US, but also from Europe, pushing the German 10-year bund yield into record negative territory (-0.71% at time of writing). Newer studies also show that flatter yields in other Developed Markets (DM) do pose downward pressure on US bond yields.

Moreover, the Fed's past years of asset purchases may have substantially depressed long-term US bond yields. A Fed research paper suggested that quantitative easing (QE) might have reduced the term premium (ie, the additional return investors can expect to hold a 10-year government bond instead of rolling over a short-term Treasury bill for the entire decade) by 100bps, which indicates a flatter yield curve than the past for a similar economic outlook.

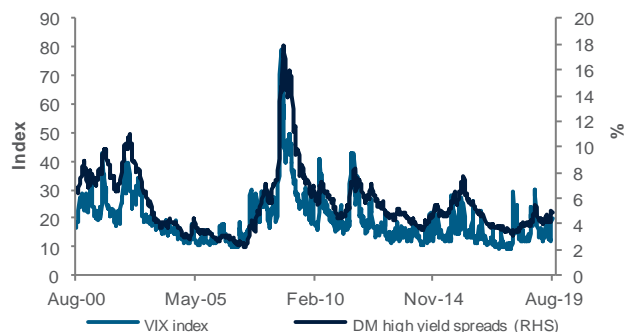
#### What are the implications of this phenomenon?

**Historically, each inversion of the 2-year and 10-year Treasury curve has been followed by a cut from the Fed in the ensuing 24 months.** However, looking forward, the key is whether the Fed actions will be enough to stave off a more pronounced inversion.

Figure 4

**DM HY yield premia have not increased materially despite the yield curve inversion and heightened equity market volatility**

Developed Market (DM) yield premium (RHS), VIX index (LHS)



Source: Bloomberg, Standard Chartered

If long rates continue to fall persistently below short rates, it will become increasingly unprofitable for banks to borrow money in the form of short-term deposits and lend to companies and individuals over longer periods. This would potentially curtail bank lending, tightening financial and credit

conditions, and eventually lead to a recession and a peak in equity markets.

**One aspect we find interesting is that HY yield premium (Figure 4) have not increased materially on the back of the recent inversion and heightened volatility.** In addition, the health of the consumer sector remains robust as indicated by fair household debt levels, positive consumer sentiment and robust consumption data; these give support to a balanced view of the health of the US economy.

While our committee's estimated odds for a US recession in the next 12 months have increased to 40% (see the Macro section), in our assessment, the investment picture warrants a more balanced approach between bonds and equities (see the Investment Strategy section).

#### What are the pros and cons of equities exposure at this stage of the cycle?

We recently scaled back our view on global equities and now expect them to perform in line with bonds, a shift from our view since early 2017 that equities would outperform bonds (barring a short-lived reduction in early 2019). This is not the same, though, as turning bearish on equities – below, we lay out both the positives and negatives of equity exposure at this stage of the cycle. This debate leads us to what is essentially a balanced view on equities relative to bonds.

On the negative side, we see a risk of 2020 earnings estimates being revised lower, hurting a key driver of equity performance. Valuations are above the long-term average, creating a risk of multiples contraction should there be negative growth surprises. Moreover, studies point out that a buy-the-dip strategy becomes less effective when economic indicators (such as PMIs) are negative and/or falling.

On the positive side, consensus earnings growth still points to double-digit global earnings growth for 2020, while return on equity (ROE) sits at a healthy 14%. Moreover, professional surveys indicate that investors are very overweight cash; historically, high cash levels have proved to be a good contrarian buy indicator for equities. Lastly, as bond yields fall across the globe, a global equities dividend yield of 2.8% becomes increasingly attractive.

Therefore, while history (what we call the outside view) tells us that equity returns in the late stages of the business cycle can be attractive, the current debate (the inside view), in particular the geopolitical landscape, points to an increasingly balanced picture for global equities. We believe the best way for investors to position between positive and negative drivers is to adopt a balanced, barbell-like approach that still allows for a focus on opportunities within equities and bonds (see page 13 for how this translates into specific weights).



### Will the global manufacturing slowdown spill over into the services sector?

The current global economic slowdown would become more worrying if it were to spill over to the services sector; our assessment shows us this risk may not be imminent.

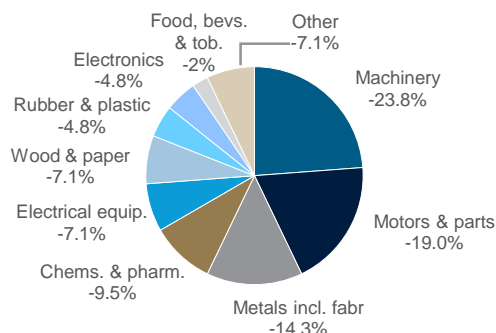
A recent study shows that the manufacturing sector in advanced economies has gone through a downturn six times since the mid-1990s. However, service sector activity only fell considerably in 2000-01 and 2008-09 following the dot-com crash and housing bubble burst, respectively, which had direct effects on jobs, wealth and ultimately the demand for services.

Moreover, service sector slowdowns since the 2008-09 global financial crisis were influenced by other factors outside of the manufacturing sector. In 2011-12, the Euro-zone crisis, and in 2015, the significant tightening of financial conditions were other drivers. We would argue that financial conditions are much looser at present.

Figure 5

#### Most of the global slowdown in manufacturing has come from industries with smaller supply chain links to the services sector

Percent contribution to the slowdown in y/y manufacturing growth in G4 economies (Q4 17-Q2 19)



Source: Refinitiv, CEIC, OECD ICIO, Standard Chartered

Looking at the past, the study links the possibility for spillovers to two direct channels. The first is through supply chain linkages, while the second is through labour market contagion.

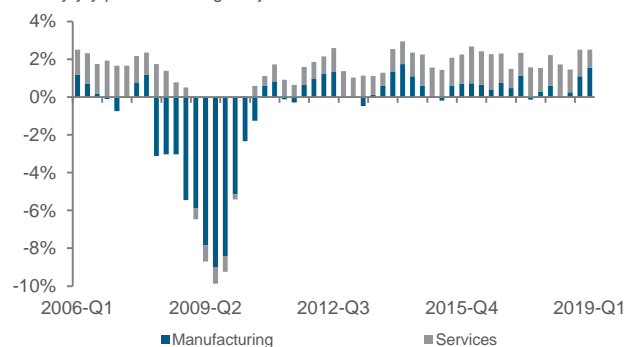
With regards to supply chain linkages, among different manufacturing industries, Food & Beverages and Chemical & Pharmaceuticals – the two largest – have the biggest direct supply chain links according to Capital Economics. However, the industries that have suffered the most during the contraction over the past year and a half have smaller linkages to services, such as Machinery and Motor & Parts. (Figure 5).

With regards to the second link, while manufacturing jobs generally make up a small share of total employment in advanced economies, the analysis shows there needs to be a dramatic loss of employment in the manufacturing sector to have a big impact on the overall labour market to cause the ensuing drop in demand for services. (Figure 6)

Figure 6

#### A sizeable loss of jobs in manufacturing could be very damaging to global growth. Data does not indicate such conditions

Quarterly y/y percent change in jobs for G7 economies



Source: OECD Statistics, Standard Chartered

One way the downturn could seriously drag the services sector down would be if corporate income in the manufacturing sector falls significantly enough for firms to struggle to service existing debt. However, for the time being at least, there are few signs of this feedback loop developing. That said, the risk rises if the US pursues high tariffs on autos later this year, while escalating its tit-for-tat trade tactics against China, and the manufacturing slowdown deepens further across the globe.

# Macro overview

## More stimulus to counter slowdown

- **Core scenario:** Global trade tensions have hurt growth, especially in Europe, Japan and China, but the US economy remains relatively resilient. Our Global Investment Committee sees increased chances of monetary and fiscal stimulus worldwide, which could soften the downturn and extend the economic cycle.
- **Policy outlook:** The Fed cut rates for the first time in a decade; we see 1-2 more cuts in 2019, with possibly more cuts in 2020. We also expect the ECB, BoJ and PBoC to ease policy. Europe is increasingly likely to ease fiscal policy.
- **Key risks:** Global trade and geopolitical tensions remain the main sources of risk, followed by Euro area tensions (around Brexit, Italy). Monetary and fiscal stimulus has the potential to deliver positive surprises to the outlook.

### Core scenario

Global growth expectations have softened since our H2 Outlook amid escalating US-China trade tensions. The uncertainty has led to a sharp downturn in key trade-dependent European economies, such as Germany and Italy, and the more open economies in Asia. There is a growing concern reflected in the bond markets that the slowdown – primarily focused on the manufacturing sector – could spill over to the services sector, dragging down the consumer-driven US economy, which has remained relatively resilient thus far. Our Global Investment Committee acknowledges the risks (our US recession probability over the next 12 months has risen to 40%, from 35% in June). However, with inflation subdued, we believe major central banks, led by the Fed, are preparing to ease monetary policies further. There is also the rising prospect of Europe relaxing its tight fiscal spending rules – this could deliver significant positive surprise to both Europe's and the world's growth outlook.

Figure 7

### Central banks worldwide have turned decisively dovish

Region	Growth	Inflation	Benchmark rates	Fiscal policy	Comments
US	●	●	●	●	The Fed is likely to cut rates 1-2 times more in 2019 to offset the impact of the trade war. We do not expect a recession in the next 12 months
Euro area	○	●	●	●	The ECB is likely to ease policy, perhaps as soon as in September, amid rising impact from global trade tensions and risks from Brexit and Italy
UK	○	●	●	●	PM Johnson has raised hard Brexit risks, although political constraints could lead to elections
Japan	○	●	●	●	The BoJ is increasingly likely to ease policy further as external risks mount with global trade tensions
Asia ex-Japan	●	●	●	●	Escalating US-China trade tensions and the Fed's dovish policy U-turn implies further policy easing by China and other Asian central banks
EM ex-Asia	●	●	●	●	The Fed's dovish shift paves the way for EMs to cut rates; Mexico seen cutting rates most in Latam

Source: Bloomberg, Standard Chartered

Legend: ● Supportive of risk assets ○ Neutral ○ Not supportive of risk assets



## IMPLICATIONS FOR INVESTORS

The Fed to cut rates 1-2 more times in 2019, with growing prospects for further cuts in 2020

The ECB and BoJ to ease further over the next 12 months, with growing prospects for renewed bond buying by the ECB

China's revision of benchmark rates has set the stage for further easing of monetary policies; targeted fiscal easing to continue supporting consumer-driven growth

# Bonds

## Preference for credit

- Bonds remain a core holding. The recent spike in trade tensions reaffirmed their diversification value. Our base case of a further extension in the business cycle and the sharp decline in bond yields lead us to prefer credit (bonds offering a yield premium over government bonds) over government bonds.
- Heightened trade tensions, global growth concerns and our expectation for 1-2 more Fed rate cuts in 2019 lead us to believe the yields are likely to remain anchored around the current low levels over the next 6-12 months. The 10-year US Treasury yields are likely to be range-bound around 1.50%-1.75%. A swift resolution of trade tensions is the key risk that may result in higher yields.
- Emerging Market (EM) USD government bonds are a preferred area within bonds as cheap valuations (higher than average yield premiums), easier Fed policy and a heightened search for income-generating assets are likely to help them outperform global bonds. Asian USD bonds rank second in our preference order given their high credit quality and defensive characteristics, though increasing US-China trade tensions are a risk.
- Our view the USD could see more support than we earlier expected may pose a headwind to EM local currency bonds. Developed Market (DM) High Yield (HY) and Investment Grade (IG) corporate bonds are a core holding given we prefer credit. Lastly, the sharp decline in government bond yields tempers our enthusiasm for DM IG government bonds, which are least preferred.
- We favour hedging FX exposure for DM IG bonds to reduce currency volatility. For USD-denominated bond investors, we prefer to maintain a short (3-5 years) average maturity profile.

Figure 8

### Bond sub-asset classes in order of preference

Bond asset class	View	Rates policy	Macro factors	Valuations	FX	Comments
EM USD government	▲	●	●	●	NA	Attractive yields, cheap valuations; escalation in geopolitical tensions is a risk
Asian USD	◆	●	●	●	NA	High credit quality, low volatility is positive. Increased risk from US-China trade tensions
DM HY corporate	◆	●	●	●	●	Attractive yields, short maturity profile; risk of higher default rates due to low oil prices
EM local currency	◆	●	●	●	●	Attractive yields, easier EM central bank policy; FX volatility a risk
DM IG corporate	◆	●	●	●	●	High credit quality and improving rating trajectory balanced by low yield and high interest rate sensitivity
DM IG government	▼	●	●	NA	●	Easier monetary policy balanced by recent decline in yields

Source: Standard Chartered Global Investment Committee

Legend: ● Supportive ○ Neutral ○ Not supportive ▲ Preferred ▼ Less preferred ◆ Core holding



## IMPLICATIONS FOR INVESTORS

US 10-year Treasury yield likely to remain anchored around 1.50%-1.75% over the next 6-12 months

EM USD government bonds are most likely to outperform global bonds.

Asian USD bonds remain second ranked despite increasing risks from US-China trade tensions

Figure 9

### Where markets are today

Bonds	Yield	1m return <sup>#</sup>
DM IG government (unhedged)	0.77%*	3.0%
EM USD government	5.30%	0.5%
DM IG corporates (unhedged)	2.04%*	2.2%
DM HY corporates	6.15%	-1.5%
Asia USD	3.70%	1.6%
EM local currency government	5.44%	-3.0%

Source: Bloomberg, JPMorgan, Barclays, FTSE, Standard Chartered

# 29 July to 29 August 2019

\*As of 26 August 2019



# Equities

## Equities – reduced to core holding

- We now see global equities as a core holding. Earnings growth is being impacted by trade tensions, while elevated valuations are a risk. We anticipate global equities moving in a +/-5% range in the coming 6-12 months.
- The US remains our preferred market. Asia ex-Japan, the Euro area and Emerging Markets (EM) ex-Asia are core holdings. The UK and Japan are less preferred. The relative preference for US equities reflects our view that the market is more defensive compared to Developed Market peers.
- Asia ex-Japan has been reduced to a core holding from preferred. China offshore equities have also been reduced to core holding from preferred, although onshore equities remain preferred. The cumulative effect of the US-China trade war and the Japan-Korea trade dispute is weighing on sentiment and leading us to take a more cautious stance.
- Euro area equities remain a core holding with prospects for monetary and fiscal stimulus offsetting trade war risks in terms of the outlook, in our view.
- EM ex-Asia is a core holding. Slower global growth is a concern for these markets. However, they may also be a beneficiary of the US-China trade war. Import tariffs on US soya and oil may nudge Chinese companies to look for alternative sources for these goods; Brazil and Russia are major producers.
- Risks to our equity views: prolonged US-China trade war, weakening Chinese growth and significant USD strength.

Figure 10

### Equity market drivers and our assessment of their outlook

	View	Valuations	Earnings	Corporate margins	Economic data	Bond yields	Fund flows	Geo-politics	Context
US	▲	●	●	●	●	●	●	●	Preferred view driven by lower bond yields that are supportive of elevated valuations. Market less exposed to trade war compared to peers
Asia ex-Japan	◆	●	●	●	●	●	●	○	Core view reflects potential for China stimulus offsetting part of the trade war risks. Easier US monetary policy implies easier Asian financial conditions
Euro area	◆	●	●	●	○	●	●	●	Core view reflects potential changes to ECB rates on bank excess reserves as well as supportive bond yields and valuations
EM ex-Asia	◆	●	●	●	●	●	●	○	Core view reflects fair valuations and relative insulation from trade war. Lower commodity prices a risk
UK	▼	●	●	●	●	●	○	○	Less preferred view reflects Brexit risks and the impact of lower commodity prices. Political outlook increasingly uncertain, despite a new Prime Minister
Japan	▼	●	●	●	●	●	●	●	Less preferred view reflects uncertainty over tax and wage growth outlook, outweighing supportive valuations and low bond yields

Source: Standard Chartered

Legend: ○ Not supportive ● Somewhat supportive ● Balanced ● Supportive ● Very supportive ▲ Preferred ▼ Less preferred ◆ Core holding



## IMPLICATIONS FOR INVESTORS

Global equities are a core holding, with a preference for US equities

Asia ex-Japan, Euro area and EM ex-Asia are core holdings. UK and Japan are less preferred

Prefer Chinese onshore equities within Asia ex-Japan

Figure 11

### Where markets are today

Market	P/E ratio	P/B	EPS	Index level
<b>US (S&amp;P 500)</b>				
17x	3.1x	8%		2,925
<b>Euro area (Stoxx 50)</b>				
13x	1.4x	8%		3,411
<b>Japan (Nikkei 225)</b>				
12x	1.1x	2%		20,461
<b>UK (FTSE 100)</b>				
12x	1.5x	6%		7,184
<b>MSCI Asia ex-Japan</b>				
13x	1.3x	9%		602
<b>MSCI EM ex-Asia</b>				
10x	1.4x	9%		1,300

Source: FactSet, MSCI, Standard Chartered. Note: valuation and earnings data refer to 12-month forward data for MSCI indices, as of 29 August 2019

# Alternative strategies

## Modest opportunity in Alternatives

- Expectations for higher volatility are balanced against potentially higher correlations across certain asset classes
- This backdrop supports a more moderate opportunity set across the board for alternatives strategies

### Performance review of alternatives strategies

In August, our alternatives allocation delivered a small positive performance of 0.2%, as positive returns in Event Driven and Global Macro were largely offset by negative returns in Equity Hedge and Relative Value. Global Macro has been the best-performing strategy recently, being the only strategy to deliver positive returns in each of the last three months.

This month, all four strategies remain as core holdings. While market volatility is expected to rise, correlations may rise as well across certain asset classes, which would reduce performance dispersion and shrink the opportunity set for alternatives. In addition, risk sentiment has dialled back to a more neutral stance.

In our view, Global Macro remains attractive as a diversifier in an uncertain global policy environment, as shifts in central bank policy and geopolitical risks continue to be key drivers for markets.

We adjust our alternatives allocation to: Equity Hedge 29% (from 32%), Relative Value 26% (from 25%), Event Driven 26% (from 25%) and Global Macro 19% (from 18%). For more information on the allocation, please refer to *Outlook 2019*.

Figure 12

#### Traffic light framework alternatives strategies

	Description	View	Drivers for strategies to perform		
Substitutes	Equity Hedge	In essence, buying undervalued stocks and selling overvalued stocks	◆	<ul style="list-style-type: none"><li>• Positively trending equity markets</li><li>• Rising equity market dispersion</li></ul>	<div>●</div> <div>●</div>
	Relative Value	Looking to take advantage of differences in pricing of related financial instruments	◆	<ul style="list-style-type: none"><li>• Falling interest rates/cost of funding</li><li>• Narrowing credit spreads</li></ul>	<div>●</div> <div>○</div>
	Event Driven	Taking positions based on an event such as a merger or acquisition	◆	<ul style="list-style-type: none"><li>• Positively trending equity markets</li><li>• Rising mergers and acquisitions</li><li>• Narrowing credit spreads</li></ul>	<div>●</div> <div>●</div> <div>○</div>
Diversifier	Global Macro	Looking to exploit themes, trends and asset class relationships (correlations) at a global level, generally with leverage	◆	<ul style="list-style-type: none"><li>• Rising volatility and credit spreads</li><li>• Increasing cross asset dispersion</li><li>• Clear market trends (up/down)</li></ul>	<div>●</div> <div>●</div> <div>●</div>

Source: Standard Chartered

Legend: ● Supportive ○ Neutral ○ Not supportive ▲ Preferred ▼ Less preferred ◆ Core holding



## IMPLICATIONS FOR INVESTORS

Diversified approach preferred to alternatives allocation, given our outlook on volatility and late-cycle dynamics

All strategies remain core holdings

Global Macro remains an attractive diversifier

Figure 13

#### Where markets are today

Alternatives	YTD	1m return
Equity Hedge	6.5%	-0.5%
Relative Value	4.5%	-0.1%
Event Driven	3.1%	0.4%
Global Macro	5.9%	1.3%
Alternatives Allocation	5.2%	0.2%

Source: Bloomberg, Standard Chartered

Note: YTD refers to 31 December 2018 to 29 August 2019; 1m return refers to 1 August 2019 to 29 August 2019



## USD neutral as weaker currencies buffer escalating tariffs, slower trade

- The Fed's pivot towards lower rates has triggered a broad rush to ease monetary policy and generate a weaker currency buffer against slower trade and growth.
- The JPY is likely to strengthen on escalating trade and geopolitical tensions, as BoJ faces challenges to ease monetary policy relative to global interest rates.
- The GBP is pricing in an increasing risk of hard Brexit, but remains structurally undervalued. We continue to see attractive risk/reward in the GBP.

Figure 14

### Foreign exchange: key driving factors and outlook

Currency	3m View	12m View	Real interest rate differentials	Risk sentiment	Commodity prices	Broad USD strength	Comments
USD	◆	◆	●	●	NA	NA	Growth and rate differentials are key
EUR	◆	◆	●	●	NA	●	Growth to bottom; mix of policy easing is key
JPY	▲	▲	●	●	NA	●	No BoJ policy shift; new fiscal stimulus
GBP	◆	▲	●	●	NA	●	Brexit risk rising; undervalued
AUD	◆	◆	●	●	●	●	RBA expected to maintain easy policy
CNY	◆	◆	●	●	●	●	Tariff outlook still the main driver

Source: Bloomberg, Standard Chartered Global Investment Committee

Legend: ● Supportive ○ Neutral ○ Not supportive ▲ Bullish ▼ Bearish ◆ Range

### USD – Could remain strong for longer as global rates fall

We have turned increasingly neutral on the USD, acknowledging that although the uptrend may be peaking, the USD could simply plateau rather than reverse trend. The shift towards lower US policy rate expectations and US bond yields has quickly prompted many global central banks to join the rush towards easier monetary policies. Weaker currencies could cushion their economies from slowing growth and inflation aggravated by escalating trade tensions.

Global USD liquidity could tighten in the months ahead and capital flows into the US could persist, potentially keeping the USD supported for some time. We are closely watching the outcome of anticipated bilateral US trade talks with China, Japan and the EU for clues to any possible USD trend reversal and its timing. Domestic and global politics are likely to remain a key driver for FX.

The USD (DXY) index has resistance at the August 98.93 high, with a stronger resistance around 100.15-75. Key supports sit at 95.75 and 95.00, where a break would suggest that the USD uptrend may have finally reversed.



## IMPLICATIONS FOR INVESTORS

The USD could plateau at its current elevated level as tariff tensions escalate amid a broader global slowdown

Trigger for EUR strength could be delayed as the ECB likely pursues deeper negative rates.

We still see attractive risk/reward in the GBP, though near-term volatility is likely

The JPY is the most likely currency to strengthen against the USD

Figure 15

### Where markets are today

FX (against USD)	Current level	1m change <sup>#</sup>
Asia ex-Japan	102.39	-2.4%
AUD	0.67	-2.5%
EUR	1.11	-0.8%
GBP	1.22	-0.3%
JPY	106.52	-2.1%
SGD	1.39	1.3%

Source: Bloomberg, Standard Chartered

# 29 July to 29 August 2019

# Multi-asset income

## Decent yield, with reasonable risk

- We continue to believe a yield goal of 4%-5% is achievable for income-focused investors without having to take an unusually high level of risk.
- Downside risk protection has become more critical for income-focused investors. We retain our preferences for Asia USD, Emerging Market (EM) USD government and Developed Market (DM) High Yield (HY) bonds.
- Historical analysis shows there is potential room for outperformance of EM USD government and DM HY bonds over other income assets when both growth and inflation are expected to slow in the next 12 months.

### Key macro drivers supportive of multi-asset income in 2019

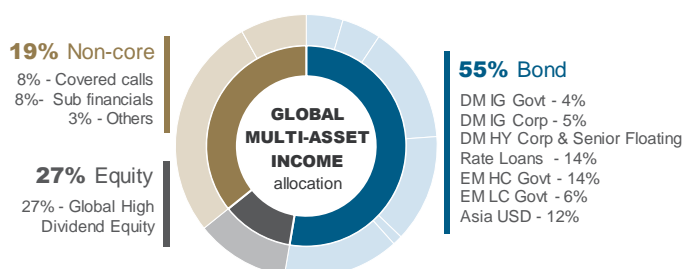
An eventful August - with the yield curve inversion, renewed trade tensions and amplified geopolitical risk in Hong Kong, the UK and Italy - has translated into a total return of -0.7% for our multi-asset income allocation. Since the publication of the 2019 Outlook, our allocation has delivered a total return of 8.4%, of which 3.0% has come from income. The negative August performance was mainly driven by the exposure to risky assets, with high dividend global equities (HDY) and DM HY bonds reporting -2.3% and -1.5% returns, respectively. That said, maintaining exposure towards quality bonds (including DM IG Sovereign and DM IG Corporate bonds) has helped mitigate downside risk in the past month.

Despite the drastic moves in global bond yields recently, pockets of opportunities remain available for investors to achieve their income goal of 4%-5% without taking excessive risks. Our diversified income allocation currently yields 4.5%, against a historical volatility range of 4%-11%, based on our backtesting. (The volatility is a measure of the level of risk income investors will likely take in the next 12 months.)

While diversification in income sources is essential, protection from potential capital loss has become a more important consideration to income investors in this challenging environment. We believe tilting towards credit components (EM USD government, Asia USD and DM HY bonds), while maintaining a reasonable exposure to quality bonds, remains a valid strategy. Our Global Investment Committee believes that we are still in an extended late economic cycle, with moderating growth and inflation. Historical analysis shows that in a similar economic scenario, EM USD government, Asia USD and DM HY bonds were among top performers, delivering positive total returns.

Figure 16

### Breakdown of our proposed multi-asset income allocation



Source: Standard Chartered. Note: Allocation figures may not add up to 100% due to rounding



## IMPLICATIONS FOR INVESTORS

Yield target of 4%-5% is achievable for income-oriented investors

Risk management remains crucial in positioning our multi-asset income allocation in the late stage of the economic cycle

Slowing growth and slowing inflation have historically been positive for income assets

Figure 17

### Allocation performance

Allocation performance	Outlook to date*	1m return**
Multi-asset income	8.4%	-0.7%

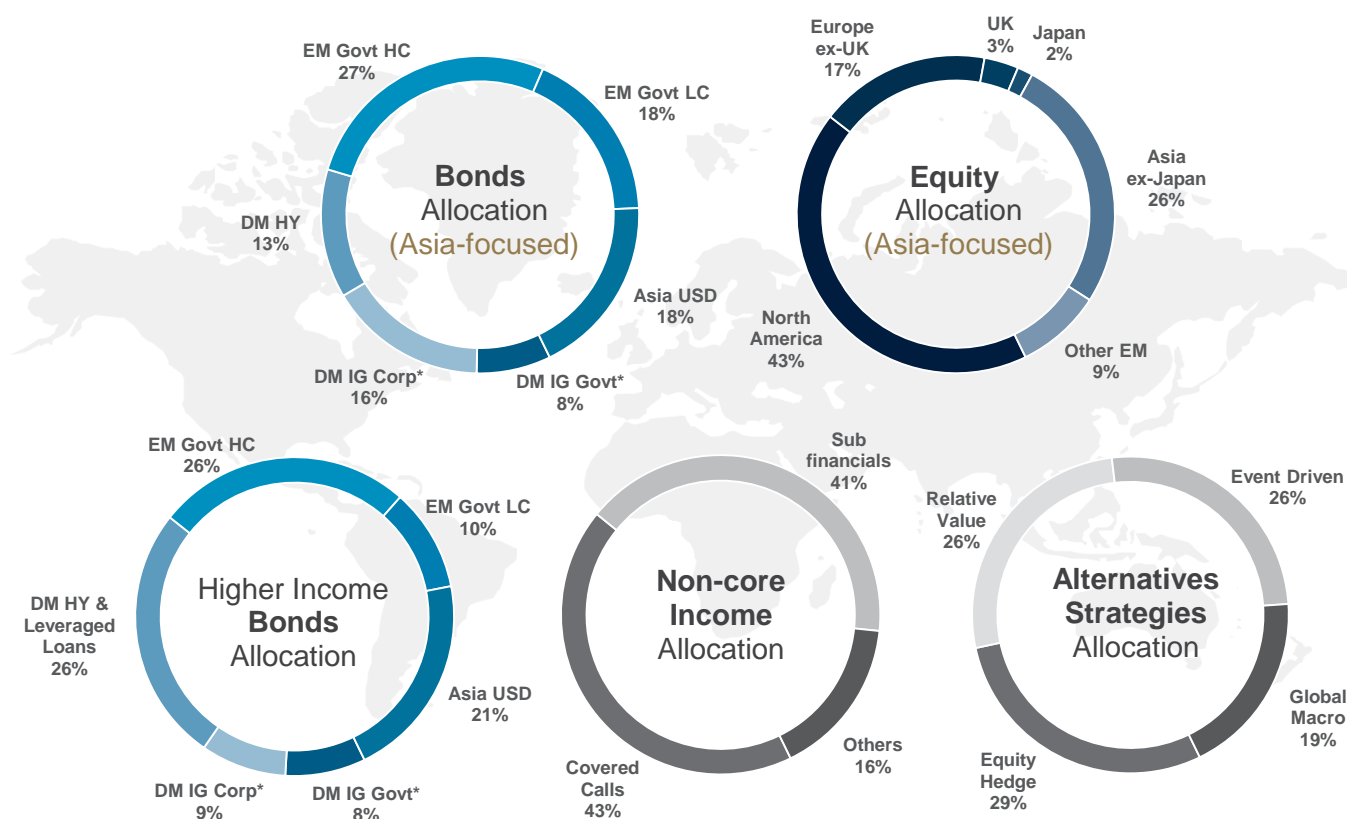
Source: Bloomberg, Standard Chartered

\*Performance from 7 December 2018 to 29 August 2019

\*\*Performance from 31 July 2019 to 29 August 2019



# Our recommended allocations



## Tailoring a multi-asset allocation to suit an individual's return expectations and appetite for risk

- We have come up with several asset class "sleeves" across major asset classes driven by our investment views
- Our modular allocations can be used as building blocks to put together a complete multi-asset allocation
- These multi-asset allocations can be tailored to fit an individual's unique return expectations and risk appetite
- We illustrate allocation examples for both Global and Asia-focused investors, across risk profiles

Bonds Allocation (Asia-focused)	Higher Income Bond Allocation	Equity Allocation (Asia-focused)	Non-core Income Allocation	Alternatives Strategies Allocation
For investors who want a diversified allocation across major fixed income sectors and regions  Asia-focused allocation	For investors who prefer a higher income component to capital returns from their fixed income exposure  Includes exposures to Senior Floating Rate bonds	For investors who want a diversified allocation across major fixed income sectors and regions  Asia-focused allocation	For investors who want to diversify exposure from traditional fixed income and equity into "hybrid" assets  Hybrid assets have characteristics of both fixed income and equity  Examples include Covered Calls, REITs, and sub-financials (Preferred Shares and CoCo bonds)	For investors who want to increase diversification within their allocation  Include both "substitute" and "diversifying" strategies

Note: Allocation figures may not add up to 100% due to rounding. \*FX-hedged

# Asset allocation summary

Tactical Asset Allocation - (12m). All figures are in percentages.

Summary	View	ASIA FOCUSED				GLOBAL FOCUSED			
		Conservative	Moderate	Moderately Aggressive	Aggressive	Conservative	Moderate	Moderately Aggressive	Aggressive
Cash	▼	10	4	2	0	10	4	2	0
Fixed Income	◆	75	53	41	11	75	53	41	11
Equity	◆	15	31	46	80	15	31	46	80
Alternative Strategies	▼	0	12	12	8	0	12	12	8
Asset class									
USD Cash	▼	10	4	2	0	10	4	2	0
DM Government Bonds*	▼	6	4	3	1	8	6	4	1
DM IG Corporate Bonds*	◆	12	9	7	2	17	12	9	3
DM HY Corporate Bonds	◆	10	7	5	1	14	10	7	2
EM USD Government Bonds	▲	20	14	11	3	15	11	8	2
EM Local Ccy Government Bonds	◆	13	9	7	2	10	7	6	2
Asia USD Bonds	◆	14	10	7	2	11	7	6	2
North America	▲	6	13	20	34	10	20	29	51
Europe ex-UK	◆	3	5	8	14	1	2	4	6
UK	▼	1	1	2	3	0	1	1	3
Japan	▼	0	0	1	1	0	0	1	1
Asia ex-Japan	◆	4	8	12	21	2	5	7	13
Non-Asia EM	◆	1	3	4	7	1	2	4	6
Alternatives	▼	0	12	12	8	0	12	12	8
		100	100	100	100	100	100	100	100

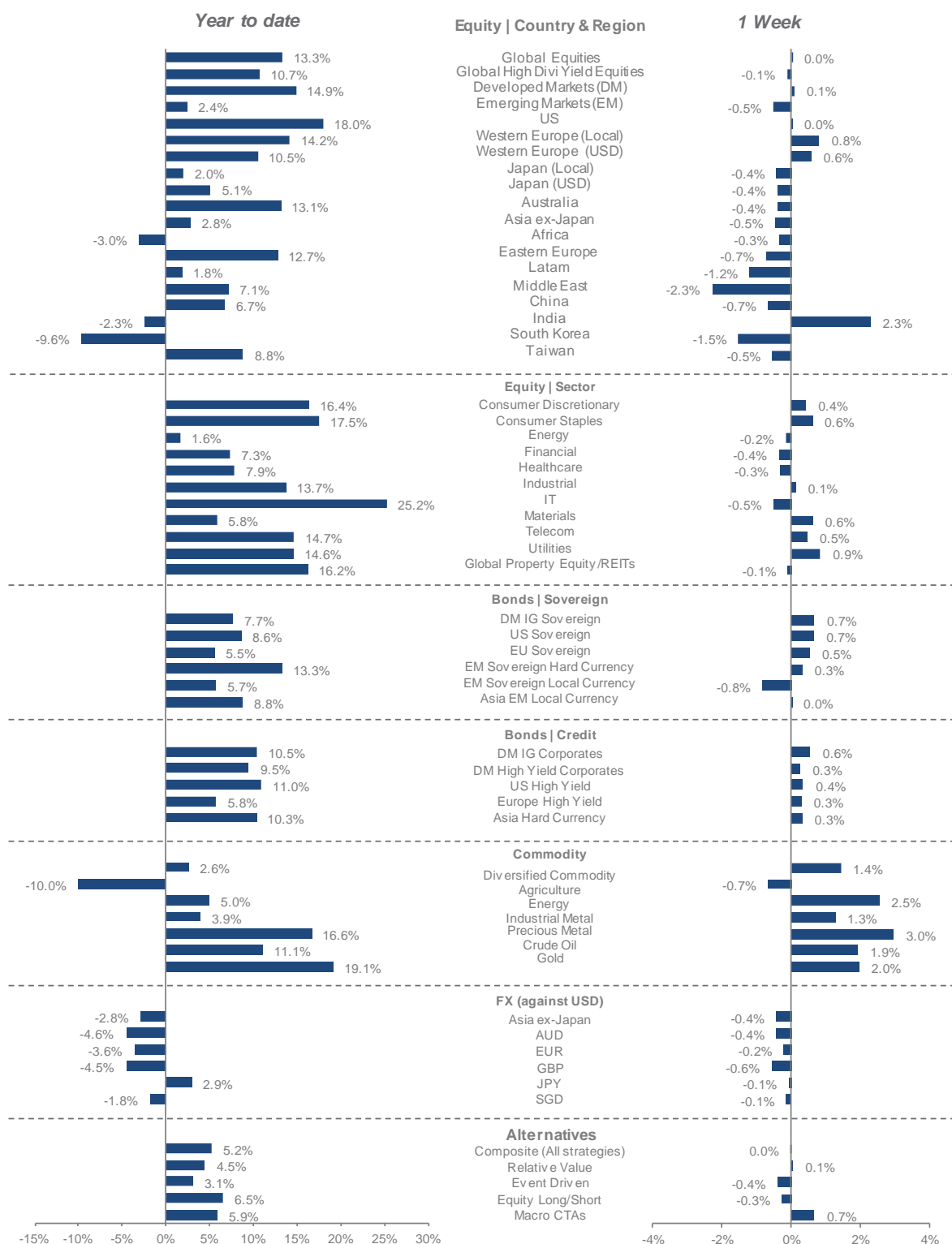
Source: Bloomberg, Standard Chartered. \*FX-hedged

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Note: (i) For small allocation we recommend investors to implement through global equity/global bond product; (ii) Allocation figures may not add up to 100 due to rounding. \*FX-hedged

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 2018 to 29 August 2019 and 1-week performance from 22 August 2019 to 29 August 2019

# Events calendar

## july 2019

X	UK Conservative Party members vote on new Prime Minister
X	China Politburo meeting on economic policy
01	Japan Upper House election
02	RBA policy decision
25	ECB policy decision
30	BoJ policy decision

## august 2019

01	FOMC policy decision
01	BoE policy decision
06	RBA policy decision

## september 2019

03	RBA policy decision
12	ECB policy decision
19	FOMC policy decision
19	BoJ policy decision
19	BoE policy decision
30	US deadline for budget agreement

## october 2019

X	Japan's consumption tax hike scheduled
X	China Politburo meeting on economic policy
01	RBA policy decision
24	ECB policy decision
31	Last day of ECB President Mario Draghi's 8-year term
31	FOMC policy decision
31	BoJ policy decision
31	UK Brexit deadline

## november 2019

X	Japan's Constitutional referendum
X	APEC summit
05	RBA policy decision
07	BoE policy decision
14	US auto tariff decision due

## december 2019

X	China Central Economic Conference
X	China Politburo meeting on economic policy
03	RBA policy decision
12	FOMC policy decision
12	ECB policy decision
19	BoJ policy decision
19	BoE policy decision

## january 2020

23	ECB policy decision
30	FOMC policy decision
30	BoE policy decision

## february 2020

NA

## march 2020

03	US Super Tuesday (Democratic presidential primaries)
10	More US Democratic presidential primaries
12	ECB policy decision
19	FOMC policy decision
26	BoE policy decision

## april 2020

30	FOMC policy decision
30	ECB policy decision

## may 2020

07	BoE policy decision
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## june 2020

04	ECB policy decision
11	FOMC policy decision
18	BoE policy decision

**Legend:** 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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