



Global Market Outlook

Looking beyond the taper

'Talking about tapering' is now well underway and we expect the Fed to announce bond purchase tapering by end-2021. This could create temporary volatility, but strong economic and earnings growth and rock-bottom policy rates mean we retain a preference for equities over bonds.

China's regulatory tightening may continue for some time, though. We prefer gaining exposure to China via Asian USD bonds, given increasingly attractive valuations.

Fed tapering is likely to result in moderately higher bond yields, but that should not stand in the way of a weaker USD. This leads us to retain a preference for Value-style equities and a regional preference for Europe and the US.



What should be expected from the Fed's tapering plans?

What are the charts saying about China's internet sector and the USD?

Why does the UN IPCC report on climate risks matter?

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Investment strategy and key themes

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Investor implications on a 12-month horizon

- Global equities over bonds and cash
- In equities: US, Euro area, UK favoured
- In bonds: Asia USD, DM HY, EM USD preferred
- In FX: USD likely to fall against EUR, GBP, AUD, CAD, NZD

Key themes

- Ready, Steady, Rotate
- Race for Income
- USD to slump in 2021
- Disruptive Innovation
- Climate change
- A world of yield-free risk

Looking beyond the taper

- 'Talking about tapering' is now well underway and we expect the Fed to announce bond purchase tapering by end-2021. This could create temporary volatility, but strong economic and earnings growth and rock-bottom policy rates mean we retain a preference for equities over bonds.
- China's regulatory tightening may continue for some time, though. We prefer gaining exposure to China via Asian USD bonds, given increasingly attractive valuations.
- Fed tapering is likely to result in moderately higher bond yields, but that should not stand in the way of a weaker USD. This leads us to retain a preference for Value-style equities and a regional preference for Europe and the US.

Markets tread water, but China slumps

For many Developed Markets (DMs), August was characteristic of a relatively slow summer month. Most major equity and bond markets remained in tight ranges, with an ongoing debate on when, and at what pace, the Fed tapers its bond purchases remaining a key source of uncertainty. The USD rose 1% over the past month.

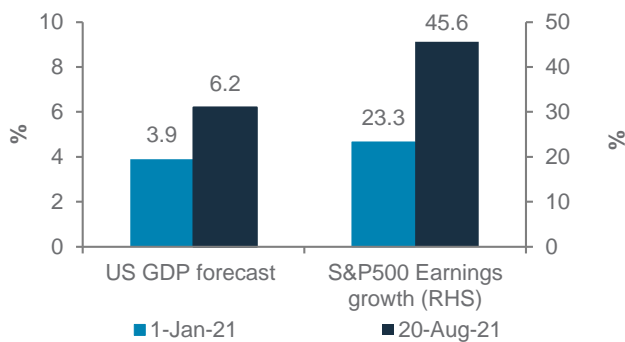
Chinese markets, though, faced anything but a quiet August. Regulatory tightening remained an ongoing concern, causing the MSCI China index to log another month of negative returns, taking the decline from this year's peak to -29.2%.

To taper or not to taper?

Public statements by Fed governors over the past month have made it clear that there is a lot of 'talking about tapering' bond purchases. With transitory inflation likely to leave the headline CPI slightly above 2% next year, the Fed's inflation mandate is appearing less of a hindrance to a policy shift. From a labour market perspective, a continuation of current trends would lead to a sub-5% unemployment rate by the end of 2021. Economic surprises have turned negative, but the still-strong level of most growth data suggests this is just a case of expectations being excessively lofty rather than something to be really concerned about. We do not believe another COVID-19 flare-up will lead to widespread lockdowns as broadening vaccinations reduce the severity of infections, enabling societies to "live with COVID-19".

Fig. 1 Any slowing of growth expectations likely to occur from very high levels

US 2021 full-year consensus expectations; Jan vs today



Source: Bloomberg, Standard Chartered

Unlike the infamous 2013 ‘Taper Tantrum’ episode, any Fed tapering action this time should not come as a surprise to markets. A number of investor surveys show a majority expect the Fed to announce a taper of asset purchases before the end of 2021, consistent with our own expectations – see *Perspectives on Client Questions* for more.

For investors, this difference from 2013 is crucial. This, combined with the fact that growth and earnings data is levelling-off at a very high level across DMs, gives us confidence in our continued preference for equities and riskier corporate bonds. However, some sentiment or positioning adjustment could still occur in the near term.

In equities, we maintain a preference for Europe (including the UK) and the US. Value-style equities are also expected to start outperforming Growth-style equities once again as growth confidence, and a Fed move towards the tapering of quantitative easing, help government bond yields rise.

China: Bonds over equities

In Asia, China’s financial assets face a very different backdrop. From a monetary policy perspective, we expect more easing as policymakers seek growth stability ahead of the annual Party Plenum in October. However, there are scant signs of recent regulatory tightening coming to an end. Historically, tightening regulatory policy has rarely been short-lived and recent measures have been framed as being consistent with longer-term policy objectives.

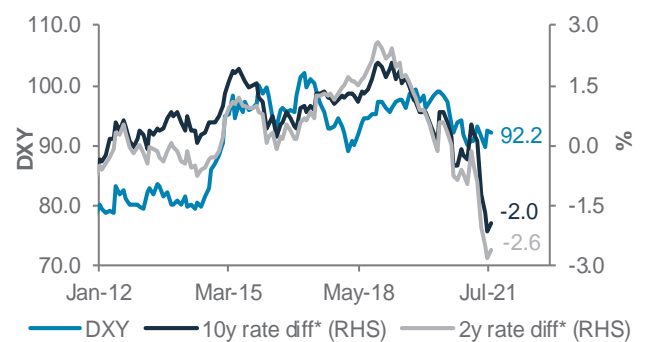
We believe Chinese equities are likely to perform broadly in line with global equities over the next 12 months. Like other risks, regulatory concerns are likely to be fully priced in at some point. However, for now, we favour two approaches to gaining exposure to Chinese assets.

First, we continue to prefer the energy and industrial equity sectors in China along with technology sub-sectors consistent with our Disruptive Innovation theme. These are likely to be less sensitive to further regulatory tightening.

Second, we favour Asia USD bonds, especially those offering higher yields, alongside Emerging Market (EM) USD

Fig. 2 Relative bond yields still favour a much weaker USD

USD Index (DXY) vs real (net-of-inflation) yields

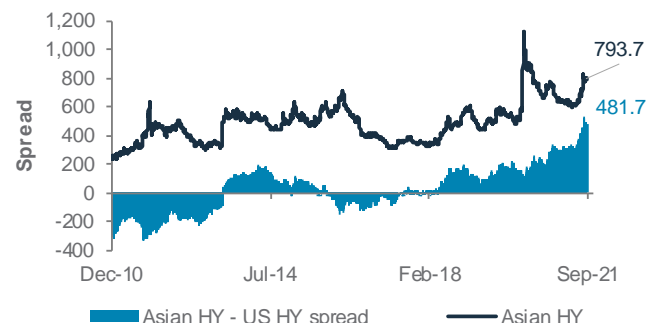


Source: Bloomberg, Standard Chartered; *yields deflated by CPI

government and US/European HY bonds. Valuations of Asian USD HY bonds are now at the cheapest levels since the peak of the COVID-19 crisis, relative to both the asset class’s own history as well as to its US and European peers. Timing a trough in valuations remains difficult, but Asian HY bonds now pay investors a very attractive yield to wait for an upturn in sentiment, in our view.

Fig. 3 Asian HY USD bond valuations cheap vs history and vs US HY peers

Asia HY bond yield premium over US Treasury yield and relative to US HY bond yield



Source: Bloomberg, Standard Chartered

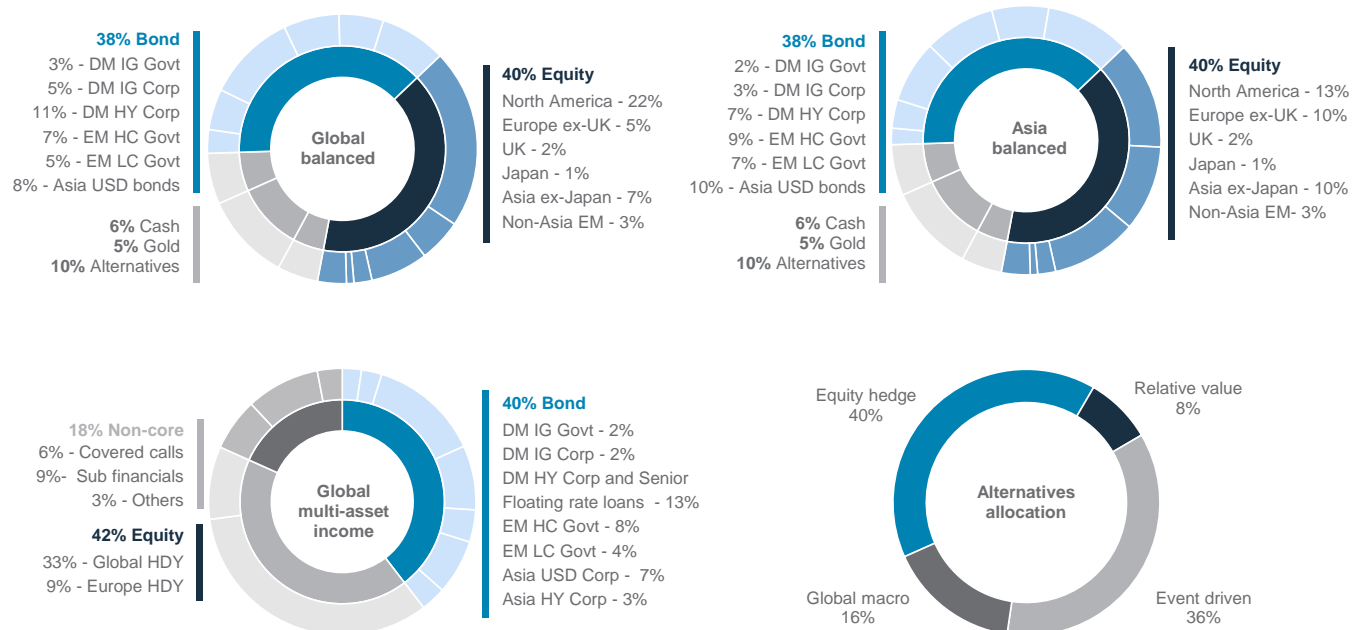
The yield catch-up

It is valid to question if Fed tapering implies further USD gains via higher bond yields. However, the still wide disconnect between relative yield differentials and the USD, combined with the USD Index (DXY) being at key resistance, tilts the balance in favour of a weaker USD, in our view. Against this backdrop, we continue to prefer European and commodity currencies. The latter undoubtedly face short-term headwinds from a COVID-19 resurgence and commodity price pullbacks, but recent central bank comments suggest this is unlikely to completely derail monetary policy tightening plans.

Gold is also likely to rise and close the gap with real bond yields, although there is a risk that rising yields could become a headwind in the longer term, unless USD weakness takes the baton as a driver of gold prices.

Our 12-month tactical asset allocation

12-month tactical asset allocations for investors with a moderate risk profile (numbers may not add up to 100% due to rounding)



Summary of our key asset class views


View	Detail
USD cash	▼ + Safety - Negative real (net-of-inflation) yield
Bonds	
DM Govt	▼ + High credit quality, policy support - Very sensitive to rising US bond yields
DM IG Corporate	▼ + Policy support - Very sensitive to rising US bond yields
DM HY Corporate	▲ + Attractive yield, low rate sensitivity - Valuations, risk of rising defaults
EM USD Govt	▲ + Attractive yield, attractive value - Sensitivity to rising yields, USD rebound
EM Local Ccy Govt	◆ + Moderate yield, weak USD view - Rising local policy rates, USD rebound
Asia USD	▲ + Attractive yield, attractive valuations - China regulatory tightening, default risks
Equities	
North America	▲ + Earnings growth, policy support - COVID-19 wave, potential tax rise
Europe ex-UK	▲ + Vaccinations, Value rotation, policy support - Renewed COVID-19 wave
UK	▲ + Attractive valuation, Value rotation, Vaccinations - Policy risk, strong GBP
Japan	▼ + Global economic recovery - China slowdown, structural deflation
Asia ex-Japan	◆ + Earnings rebound, China monetary easing - China regulatory headwind, COVID-19
Gold	◆ + Weak USD, equity volatility - Treasury yield rebound, Return of risk appetite
Alternatives	◆ + Diversifier characteristics - Equity, corporate bond volatility

Source: Standard Chartered Global Investment Committee

Legend: ▲ Most preferred | ▼ Least preferred | ◆ Core holding || Green: upgrade from prior view | Red: downgrade from prior view

Other themes

Below we provide a brief overview of our currently open thematic ideas, coupled with some recent highlights. For further details, please read our Thematic Investing H2 2021 Update published on 2 July 2021.

 Other themes		
Structural Themes	Disruptive Innovation	<p>We retain a structural preference for the Disruptive Innovation theme, favouring 1) Fintech, 2) eGaming, 3) Electric Vehicles (EVs), 4) 5G/Internet of Things (IoT), and 5) Medical Technology.</p> <p>Of these sub-themes, those benefitting from fiscal policy tailwinds, such as EVs and IoT, continue to see more upward earnings revisions estimates relative to downgrades, thus justifying rich forward valuation multiples (12-month forward P/Es of 28x and 27x, respectively). Noticeably, however, the eGaming sub-theme has come under pressure recently due to China regulatory tightening concerns. For now, we look through this short-term weakness, but continue to monitor regulatory developments.</p>
	Time for Climate Investing	<p>The UN Intergovernmental Panel on Climate Change (IPCC) recently released their sixth assessment report that highlights the severe impacts of global warming exceeding the 1.5°C threshold (refer to page 9). Global policymakers are looking to further accelerate their efforts to reach a carbon-free economy in view of the urgency to combat the threat of climate change.</p> <p>Although valuations have picked up, with the clean energy sector trading at a 12-month forward P/E of about 65.1x, solar at 37.8x, wind at 30.1x and water at 33.2x, we continue to see growing opportunities for future investments in this space as climate action is likely to increase. Greener and more sustainable infrastructure might also be key to withstanding extreme weather changes.</p>
	In a world of “Yield-Free” risk	<p>Government bond yields remain near multi-decade lows, while DM corporate bond yield premiums are also near record lows even as the Fed prepares to taper bond purchases. While bond yields are moderately higher than a year ago, they remain low relative to history and are likely insufficient to provide protection against any equity downside.</p> <p>We continue to believe investors will need to take additional risks, make prudent use of leverage and/or explore alternative, less-liquid assets, such as hedge funds or private investments, to capture opportunistic sources of diversification, income and returns.</p>
Cyclical Themes	Ready, Steady, Rotate (Value to outperform Growth)	<p>At the onset of 2021, we argued that Value's unprecedented underperformance against Growth-style equities during 2020 would experience a reversion to longer-term means. However, repeated COVID-19-induced growth scares and the recent drop in US bond yields have paused the rotation towards Value stocks in recent months.</p> <p>Year-to-Date (YTD), global Value equities returned 15.1% vs 13.5% for global Growth equities. As relative valuations remain clearly in favour of Value from a historical perspective, and as we expect bond yields to face upward pressure as the Fed begins its tapering plans, we believe the catalysts for Value to outperform Growth over the coming 12 months are still in place.</p>
	USD to slump in 2021	<p>Our cyclical theme of USD weakness has suffered delays and setbacks thus far in 2021. The USD Index (DXY) has rebounded on short-term uncertainty and as short-USD positioning has been unwound. However, we still expect the USD to decline long term, reflecting relative economic fundamentals, once near-term monetary and fiscal uncertainty eases and global growth broadens.</p>
	Race for income	<p>Absolute returns across the income spectrum tend to be substantially higher in an environment where growth and inflation expectations are rising, compared with other growth/inflation scenarios. To capture more yield, investors are encouraged to go beyond traditional fixed income assets and add exposure to high dividend equities and hybrids. While credit assets remain a core holding in our global diversified income allocation, investors might want to consider tilting towards parts of the bond market that are less sensitive to higher rates as the Fed prepares to taper. We continue to prefer Asia USD (including HY), DM HY and EM USD government bonds.</p>

Source: Bloomberg, Standard Chartered; Performance data as of 26 August 2021.

Perspectives on key client questions

Marco Iachini, CFA
Cross Asset Strategist

Q What to expect from the Fed's tapering plans?

In response to the COVID-19 pandemic crisis, the Fed undertook its fourth - and largest ever - Quantitative Easing (QE) programme of US government and mortgage bond purchases. Given the recovery in growth and inflation expectations, the Fed is now debating when and how it should wind down these purchases. As we write, the Jackson Hole Economic Policy Symposium is under way, and investors will look for clues about QE tapering plans by Fed Chairman Jerome Powell and his team.

Whether we see detailed plans, or indications for a future tapering announcement, we expect the impact on markets to be limited in both duration and magnitude. We still expect the Fed to announce tapering plans before the end of 2021 and begin the actual reduction of its bond-purchasing programme by the first quarter of 2022.

Learning from the past – Fed edition

In 2009, the Fed began the reduction of its QE1 programme immediately after its tapering announcement, while for QE2, it had set a pre-defined deadline for the end of its balance sheet policies. However, it was the QE3 taper episode that earned the infamous nickname of “Taper Tantrum” due to markets’ reaction to the Fed Chairman Bernanke’s surprise mention of tapering plans during a Q&A session following the May 2013 FOMC meeting. The sell-off in US government bonds that ensued temporarily spilt over to equity markets, hurting investor sentiment and fuelling concerns about the impact to the real economy.

At the June 2013 policy meeting, the Fed formally announced a tapering of some of its QE policies contingent upon continued positive economic data. While Bernanke did not announce an interest rate hike at that time, he introduced inflation and employment targets as preconditions for raising policy rates, sending equity markets lower in the aftermath of the announcement. The Fed subsequently decided to hold off on its tapering plans in September, following a couple of negative employment data surprises. At last, at the December 2013 meeting, the Fed announced that it would begin to scale back its bond purchases, concluding what would eventually be considered a template of communication missteps to avoid in the future.



Fig. 4 Fed tapering history

QE Period	QE start	Taper announcement	QE taper start	QE end	Comments
QE1	25 Nov 2008	12 Aug 2009	12 Aug 2009	1 Mar 2010	First tapering experience. No advance warning
QE2	3 Nov 2010	N/A	N/A	30 Jun 2011	QE ended as scheduled (no taper)
QE3	13 Sep 2012	22 May 2013	18 Dec 2013	29 Oct 2014	“Taper tantrum” episode
Balance sheet normalisation	N/A	14 Jun 2017	1 Oct 2017	N/A	Balance sheet reduced by USD 700bn until Aug 2019
QE4 (COVID-19)	15 Mar 2020	<i>By end of 2021</i>	<i>Q1 2022</i>	?	Greater tolerance of inflation under Fed's new AIT* policy

Source: Federal Reserve, Standard Chartered; *AIT = Average Inflation Targeting policy; Italics reflect SCB WM CIO expectations

Unlike 2013, we believe that the Fed now approaches its tapering decision from a position of strength. GDP growth is expected to hit 6.5% this year and over 4.0% in 2022 and inflation targets have been largely achieved. Lastly, the current pace of job gains suggests that employment targets could be achieved next year, with the Fed expecting the unemployment rate to fall to 4.5% by end-2021 and to 3.8% by end-2022.

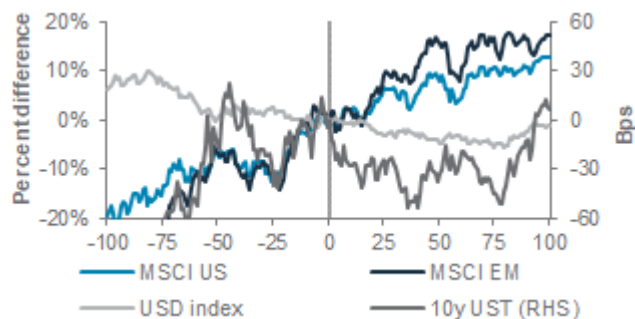
Recent surveys of professional money managers indicate that more than 80% of investors expect the Fed to announce its tapering plans by year-end (of that number, a majority expects an announcement by the September FOMC meeting). Likewise, in another survey done by the Federal Reserve Bank of New York, more than 75% of respondents expect the tapering to start in Q1 2022 – in line with our expectations. This indicates that a taper announcement and its official start should not be a shock to investors and markets.

Learning from the past – Markets edition

While the Fed will try to avoid a repeat of 2013, we look at previous tapering announcements to understand the reaction of assets to the announcement.

Fig. 5 Equities better digested the 2009 taper as they continued to rebound from the GFC trough

Change in select assets pre- and post- 2009 taper announcement on 12 August



Source: Bloomberg, Standard Chartered; T = work days

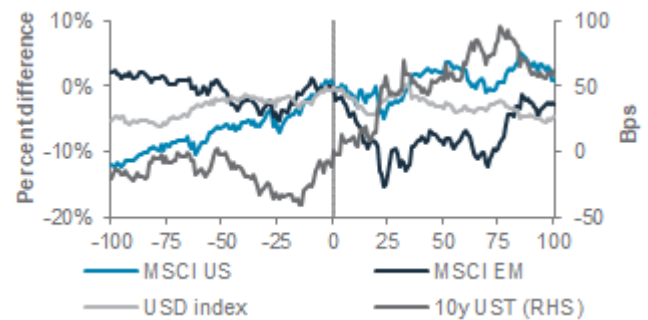
Somewhat reassuringly, tapering has not been a major issue for US equities in the past. In 2009, the MSCI US Equity index traded well throughout tapering. It behaved similarly in 2013, going into the announcement – only to display a benign 5% correction shortly after the June FOMC meeting. EM equities withstood the 2009 tapering better than US equities. However, they underperformed in the immediate weeks following each FOMC meeting during the 2013 “Taper Tantrum” period, causing them to eventually lag US equities over a medium-term horizon.

US government bond yields have typically risen in anticipation of tapering announcements before trading largely sideways following the actual start of tapering. In 2013, in particular, the 10-year Treasury yield spiked roughly 140bps from their low

in May until the December taper start due to the surprise effect caused by the Fed’s (mis)communications. Across all episodes, the USD declined between 1% and 5% in the months following either taper announcements or taper starts.

Fig. 6 Tapering surprises are more a risk for equities outside the US than for US equities

Change in select assets pre- and post-2013 taper announcement surprise on 22 May



Source: Bloomberg, Standard Chartered; T = work days

Given the above analysis, and considering that investor positioning today is less stretched than at the start of the summer (especially for the USD and US bonds), we believe that a tapering announcement will not constitute a significant drag to risky assets – particularly DM equities. Meanwhile, we expect bonds to start pricing a taper announcement more aggressively, thus putting upward pressure on yields.

All the while, the Fed continues to telegraph its intentions clearly and slowly to the investor community. This backdrop leads us to believe that an upcoming taper announcement may have a smaller impact on financial assets than in the past.

Q Will the USD finally head lower once the Fed embarks on its QE reduction?

Admittedly, our bearish long-term USD view has yet to materialise.

Our thesis of downward pressure on the USD from US twin-deficits and the economic recovery radiating to the rest of the world outside the US has suffered various setbacks. The USD has regularly found itself playing the role of a “safe-haven”, driven by repeated COVID-19 growth scares, skewed positioning, geopolitical risks, China’s regulatory crackdown and the slow vaccination progress in EMs.

While we hold a short-term (three month) neutral view on the USD, drivers of USD weakness over the coming 12-month period remain in place and are likely to cascade once the global economy re-opens more broadly and risk sentiment improves. These drivers include the Fed’s greater tolerance for inflation under its new AIT monetary policy, ample USD liquidity, capital outflows from full-priced US assets and the weight of the US twin deficits.

Why the IPCC report matters

The UN Intergovernmental Panel on Climate Change (IPCC) Report

The UN IPCC is a body of scientists who assess and provide governments with scientific data that can be used to develop policies on climate matters. It publishes assessment reports every six years and recently issued its sixth report on climate change.

With better data collection and modelling capabilities, the sixth assessment delivered a sober report on how temperatures are likely to keep rising, with increased occurrences of extreme weather events attributed to human activity. We can expect an increase in heat waves, longer warm seasons and shorter cold seasons under a 1.5°C warming scenario. The patterns could intensify if global warming exceeds 2°C.

As global warming accelerates, the risk of historically unprecedented climatic events rises. Thankfully, there is an increased urgency of climate action that is likely to result in policymakers accelerating measures to combat the risks highlighted in the report and these, we believe, would lead to potential investment opportunities.

Key findings and their impact

Global temperatures are likely to rise 1.5°C between 2030 and 2052

Human activities are estimated to have caused c.1.0°C of global warming above pre-industrial levels already and the past five years have been the hottest on record since 1850. Without immediate and significant emissions cuts, average temperatures could rise by more than 2°C by the end of the century. This could result in around 420m more people being frequently exposed to extreme heatwaves and increase water stress by up to 50%.

Agricultural production is projected to be hit, with yields of major crops in drought areas expected to fall by more than 50% by 2050 and almost 90% by 2100.

Carbon emissions need to decline by about 45% from 2010 levels by 2030 to prevent overshooting 1.5°C rise in temperatures

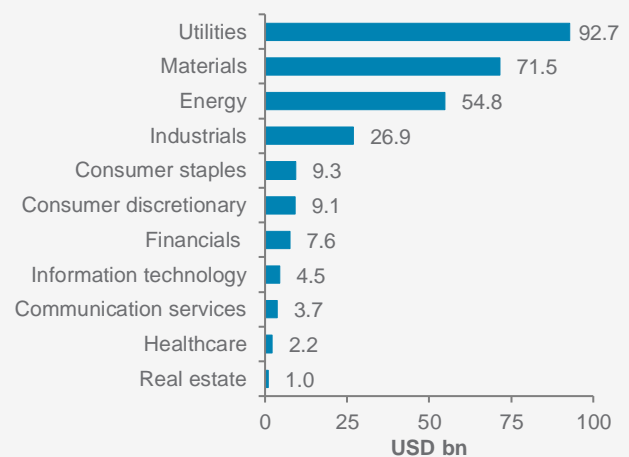
Governments are likely to respond to the findings of the IPCC report and do more to accelerate the transition to a greener economy. Such a transition will entail a cost, including increased regulations, leading to stranded assets and the implementation of carbon pricing mechanisms, increasing the costs for companies, especially for those operating in high-polluting industries and laggards in adopting carbon reduction measures.

The Financial Times estimated potential stranded assets at around USD 900bn, equivalent to about one-third the value of big oil and gas companies.

According to S&P Global, global companies face up to USD 283bn carbon pricing costs, with 13% of their earnings at risk by 2025, under a high carbon price scenario.

Fig. 7 Carbon earnings at risk under a high carbon price scenario

Based on companies listed on the S&P Global 1200



Source: S&P Global Trucost, Standard Chartered

The growing importance of carbon pricing has also led to an increase in companies utilising internal carbon prices for corporate accounting. The setting of an internal charge on the amount of carbon dioxide emitted from assets and investment projects has provided an additional lens to determine how emissions could affect income and senior management decisions. For instance, French company Danone reported that its carbon-adjusted earnings per share (EPS) using an internal carbon pricing had seen a 12% growth compared with the headline EPS growth of 8.3% in 2019 as a result of a 9% reduction in carbon emissions.

Extreme weather and rising sea levels

Extreme heat waves are expected to occur once every decade, compared with once every 50 years because of global warming, while downpours and droughts have also become increasingly frequent. We have seen such events in the past few months – from Greece's wildfires and a record 48.8°C temperature in Europe to floods in China and Japan.

Extreme weather events have a huge impact on the level of GDP. In Asia, the probability of being exposed to a lethal heat wave at least once in the decade could increase to 80%. This

translates into about USD 2.8trn to USD 4.7trn of GDP annually being put at risk by 2050 from an effective loss of outdoor working hours because of increased heat and humidity.

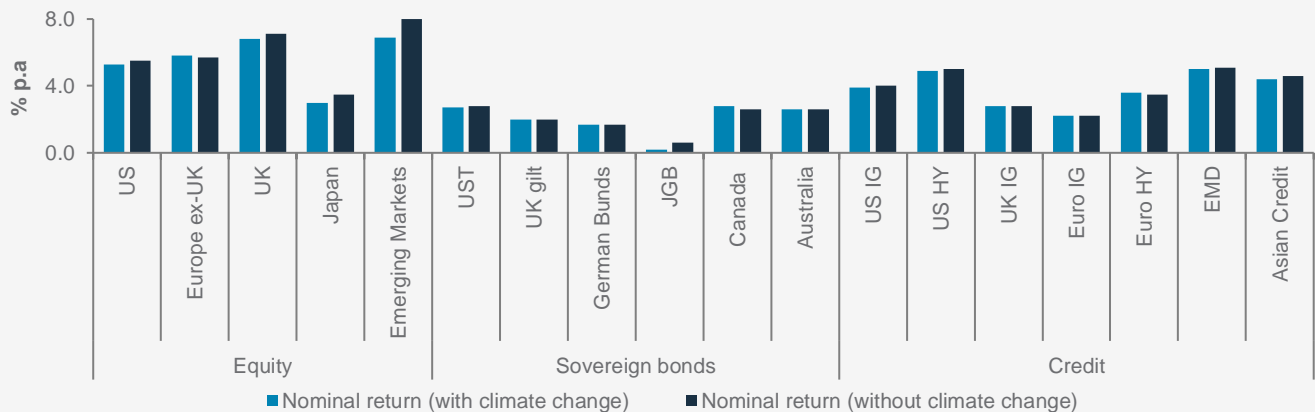
Physical risks of climate change due to rising sea levels have also been highlighted through research by Scientific Reports,

which mentioned that coastal flooding could damage assets of about USD 14.2trn by 2100.

These findings can be translated into asset class returns forecast and risk management adjustments from a portfolio perspective that clients can consider.

Fig. 8 Climate change impact on equity and fixed income returns

30y return forecast between 2021 and 2050



Source: Schroders Economics Group, Standard Chartered

Climate change and the portfolio effect

Traditional asset classes and forecasted returns

Physical and transition risks related to climate change generally lead to higher costs and lower productivity across countries. A study by Schroders Economics Group demonstrates the impact of climate change on asset classes – the impact is mostly negative for broad asset classes, compared with a scenario that assumes policies have already been implemented and no further climate-related impact occurs. Risk assets, such as equities, tend to be more sensitive to climate change compared with fixed income.

Climate change risk management

The economic cost of climate policy for the market to absorb by 2030 is estimated at c.USD 8trn by Mercer. Uncertainty posed by the policy is expected to impact portfolios, accounting for as much as 10% of overall portfolio risk for a representative portfolio of a traditional asset mix. Mitigating climate risks will, therefore, require investors to think differently from an asset allocation perspective, diversifying across traditional asset classes and sources of risks. Sustainability factors, such as leveraging on sustainability ratings of issuers, could support investors in making more informed decisions on companies and investment products. Companies that are responding to climate policy and taking appropriate measures to reduce their climate risks, in turn, could help investors reduce climate risk exposure.

Opportunities that benefit from the transition story

The EU Commission has proposed that at least 25% of EU expenditure will contribute to climate action during 2021-27 in

its next long-term budget. While Biden's USD 1trn infrastructure package recently passed by the Senate has been watered down, it still includes USD 1bn of spending into infrastructure to support the charging and procurement of EVs and USD 55bn of investments to improve access to clean drinking water.

Apart from government efforts, the International Energy Agency (IEA) also estimates that technologies focused on removing carbon dioxide could amount to USD 2bn in 2021, providing additional opportunities in this energy transition story.

Although most renewable energy sectors (solar, wind, clean energy) have underperformed global equities in recent times, (with the exception of water and EVs), the increasing evidence of the effect of climate change on the social and economic landscape challenges policymakers to speed up their transition to a low-carbon economy. This should eventually lead to macroeconomic and capital market adjustments and ultimately lift corporate profitability. We thus see this as a key driver of asset class returns in the future.

The management of carbon risks in clients' portfolios is therefore important in ensuring that, beyond being climate resilient and recognising the impact of climate change on their assets, there is an opportunity to enact real changes as well.

Macro overview – at a glance

Rajat Bhattacharya
Senior Investment Strategist



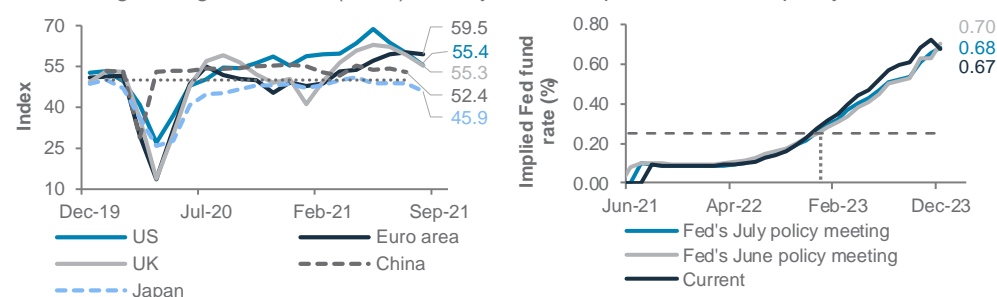
Key themes

The COVID-19 vaccination leaders - Europe and the US - continue to lead the global economic recovery from the pandemic, while low vaccination rates across Emerging Markets (except for China) delay the return of normalcy. A resurgence in infections in the US and Asia could cause a brief slowdown in activity, but we believe rising vaccinations worldwide and the growing comfort among citizens to “live with COVID-19” after vaccinations portend a cyclical global recovery by next year. We expect economic growth in the US and Europe to remain above trend in 2022 as businesses rebuild inventory to meet pent-up demand, while consumers pare excess savings. The US could gain from c.USD 4trn in new fiscal spending on infrastructure, environment and social benefits if a budget is approved by the Congress this year. China is the only major economy that is likely to grow at a slower pace in 2022 vs pre-pandemic levels, but Beijing is likely to relax policies to stabilise growth. Inflation has started to normalise, notably in the US, as supply bottlenecks and job dislocations ease. This should allow the Fed to taper bond purchases from early 2022, although a rate hike is unlikely next year. The ECB and BoJ are likely to stay highly accommodative for longer.

Key chart

Business confidence in the vaccination leaders - Europe and the US - remains strong. Monetary policy is also likely to stay loose over the coming year as the Fed is expected to hike rates only in early 2023, while the ECB and BoJ remain very accommodative

Fig. 9 Business confidence high in vaccination leaders; Fed rate hike long way off
Purchasing managers' indices (PMIs); money market expectation of Fed policy rate



Source: Bloomberg, Standard Chartered

Monetary Policy	Macro factors positive for risk assets	Macro factors negative for risk assets
US ▽ ◆ ▲	+ 50% fully vaccinated; above-trend growth + Jobs, excess savings to lift consumption + Business restocking, infrastructure boost + Fed rate on hold; still-high fiscal support	– Proposed tax hikes, fiscal drag from 2022 – COVID-19 revival; precautionary savings – Slowing goods demand; supply bottlenecks – Weak lending; early/faster Fed tapering
Euro area ▽ ◆ △	+ 55% fully vaccinated; above-trend growth + Excess savings pared; robust industry + ECB easy; Recovery Fund pay-out in H2	– COVID-19 variants risk; slowing vaccinations – Precautionary savings; high jobless rate – Supply constraint; Recovery Fund delays
China ▼ ◆ △	+ 55% fully vaccinated; consumption boost + Strong industry, exports; infrastructure lift + PBoC policy easing to support growth	– Regulatory tightening; COVID-19 lockdowns – Global goods-to-service shift to hit exports – Precautionary savings; geopolitical risks
Japan ▽ ◆ △	+ Strong export growth, pent-up demand + Vaccination rates to improve in Q4 + More fiscal stimulus likely amid slowdown	– COVID-19 lockdowns; precautionary savings – Global goods-to-service shift to hit exports – Structural deflationary forces
UK ▽ ◆ △	+ 62% fully vaccinated; above-trend growth + ‘Living with COVID’ strategy to lift consumption + Infrastructure boost; longer pandemic aid	– COVID-19 variants risk; precautionary savings – Brexit-related job market & supply disruptions – High inflation; tighter monetary policy risk

Source: Standard Chartered Global Investment Committee

Legend: ▲ Tighter policy | ▼ Easier policy | ◆ Neutral policy

Bonds – at a glance

Abhilash Narayan
Senior Investment Strategist

Cedric Lam
Senior Investment Strategist



Key themes

Bond yields continue to be depressed as the increased hawkishness from the Fed appears to have been balanced by heightened concerns around rising COVID-19 cases. Nonetheless, at current levels, the 10-year US Treasury yield appears too low and we expect it to recover towards recent highs of around 1.75%-2.0% over the next 12 months. In the current environment, we still believe corporate bonds, with low interest rate sensitivity and reasonable yield, offer the best risk-reward to investors.

We continue to like DM HY bonds, as they are direct beneficiaries of vaccination-driven growth rebound (and higher corporate profitability). Asian USD bonds, particularly HY bonds, have been hit by rising regulatory concerns. However, the markets are pricing in an extremely high default rate, which is unlikely to materialise in our assessment. Hence, we retain our preference of Asian USD bonds, with HY bonds preferred over Investment Grade (IG) rated bonds.

Key chart

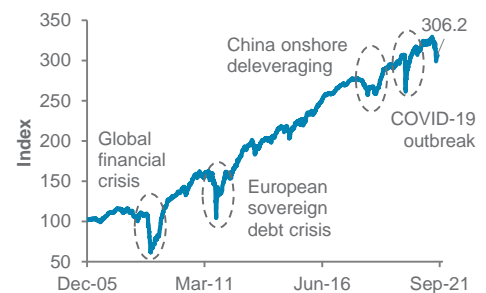
Historically, sell-offs in China HY bonds have proven to be good buying opportunities

Fig. 10 Corporate and EM USD bonds continue to offer attractive risk-reward balance

Historical credit spread ranges and current spread percentiles since 2000 (or since data is available); China HY USD bonds total return index

	Current spread	Min	Max	Percentile
US IG Corp	85	70	545	11%
US HY	307	233	1,971	7%
DM HY	381	221	1,804	23%
EM USD	353	157	906	53%
Asia USD	224	153	472	49%
– Asia IG	137	119	326	12%
– Asia HY	795	240	1,130	97%

Source: Bloomberg, Standard Chartered



	The bullish case	The bearish case
Asia USD	<ul style="list-style-type: none"> + Strong credit fundamentals + Increasing foreign demand + Attractive valuations relative to the US 	<ul style="list-style-type: none"> – Risk of higher defaults in China – Lower yields vs other EM bonds
DM HY corporate	<ul style="list-style-type: none"> + Balance sheet improvement in 2021 + Default rates have declined sharply + Low interest rate sensitivity 	<ul style="list-style-type: none"> – Expensive valuations – Increase in supply
EM USD government	<ul style="list-style-type: none"> + Higher commodity prices + Cheaper valuations vs US IG/HY bonds + EM growth rebound 	<ul style="list-style-type: none"> – High interest rate sensitivity – Low vaccination rate. Risk of renewed lockdowns
EM local currency	<ul style="list-style-type: none"> + Higher commodity prices + Improvement in EM FX reserves + Moderately attractive yield 	<ul style="list-style-type: none"> – Tighter EM monetary policy – Risk of outflows due to Fed tapering – Higher volatility due to FX exposure
DM IG corporate	<ul style="list-style-type: none"> + Strong credit fundamentals + Attractive hedged yield for foreign investors 	<ul style="list-style-type: none"> – Expensive valuations – High interest rate sensitivity – Low absolute yield
DM IG government	<ul style="list-style-type: none"> + High credit quality + Fed, ECB unlikely to hike rates at least in the next 12 months 	<ul style="list-style-type: none"> – Improvement in growth and/or inflation – Large net issuance increase – Fed likely to begin tapering in Q1 22

Source: Standard Chartered Global Investment Committee

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

Equity – at a glance

Daniel Lam, CFA
Senior Cross-asset Strategist

Fook Hien Yap
Senior Investment Strategist



Key themes

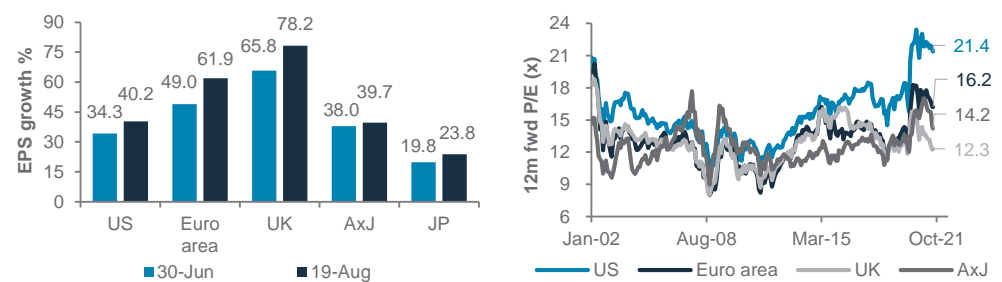
We expect global equities to continue outperforming other asset classes on a 12-month time horizon, with earnings growth expected to be the primary driver of returns. The Euro area is at the top of our preference order. It has become a “global vaccination leader”, which bodes well given increasing concerns over the Delta variant’s spread. It is also relatively under-owned, compared to the US. US equities remain preferred, with fiscal stimulus and the premium it commands from its innovation leadership. This is partially offset by the rebound in yields, which may hurt valuations in Growth stocks. The UK is also preferred, with a strong EPS rebound and still reasonable valuation. In Asia, regulatory concerns continue to weigh on China, while Japan remains less preferred with its relatively weaker earnings trend. The key risk to our global outlook is a sharp surge of hospitalisations in countries with high vaccination rates as this would undermine the “vaccinate and live with it” strategy.

Key chart

Earnings growth continues to be the primary driver of equity returns, offsetting valuation risks

Fig. 11 Earnings growth estimates in the US and Europe have been upgraded after a strong Q2 earnings season; UK remains the cheapest market in terms of valuations

Consensus 2021 EPS growth (left); consensus 12m forward P/E ratio (right)



Source: MSCI, FactSet, Standard Chartered

The bullish case		The bearish case	
Preference order ↑	Euro area equities ▽ ◇ ▲	+ Cyclical sector heavy, Value play + Relatively uncrowded + Vaccination leader	- Lower ROE vs other markets - Fiscal stimulus lags the US
	US equities ▽ ◇ ▲	+ Strong earnings + Fiscal stimulus + Innovation factor	- Expensive valuations - Yield rebound hurting technology - Peaking growth momentum vs peers
	UK equities ▽ ◇ ▲	+ Sharp EPS rebound + Rotation to Value + Inexpensive valuations	- Stronger GBP holding back gains - Monetary policy may tighten - Post-Brexit trade frictions
	Asia ex-Japan equities ▽ ◆ ▲	+ Growth and vaccination converge with DM + Undemanding valuations + China - targeted stimulus	- Regulatory pressure in China - Growth slowdown in China - Firmer USD
	Within AXJ	South Korea equities ▲	India equities ▲
	Japan equities ▼ ◇ ▲	+ Cyclical sector heavy + Valuation attractive + Better earnings revisions vs EM	- Slow vaccination progress - Pause in global economic momentum
			China equities ◆

Source: Standard Chartered Global Investment Committee

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

FX – at a glance

Manpreet Gill

Head, FICC Investment Strategy

DJ Cheong, CFA

Investment Strategist



Key themes

We continue to expect a weaker USD against European and commodity currencies over the next 6 to 12 months. The global economic recovery, delayed by recurrent bouts of the COVID-19 pandemic, should broaden as vaccinations rise worldwide. We also expect other bearish USD drivers, including the Fed's greater tolerance of inflation under its new monetary policy (AIT), ample USD liquidity, capital outflows from US assets and the weight of the US twin deficits to play out. Key risks are further pandemic setbacks, policy mistakes, regulatory surprises and geopolitical tensions that support safe-haven demand.

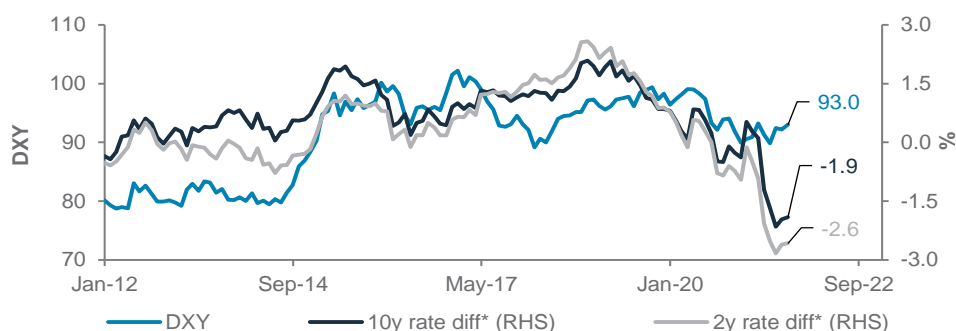
The next one to three months may see continued range-bound trading as markets await clarity from the Fed over tapering of bond purchases. Other risk events include the Delta variant's impact, the German election outcome and another round of major central bank policy meetings. Positioning has now turned from USD-bearish at the start of 2021 to bullish, and this trend could push the USD 1%-2% higher towards key technical resistance before the cyclical USD downtrend reasserts.

Key chart

DXY has held up well so far due to near-term uncertainty and short-USD positioning that has now been unwound. Once fears of higher US yields recede and global growth broadens, we expect a USD decline on the back of weaker fundamentals, including a negative real interest rate spread

Fig. 12 Real interest rate differentials suggest an eventual USD decline

USD Index (DXY), with 2y, 10y real rate differentials* between US and peers



Source: Bloomberg, Standard Chartered; *Government bond yields deflated by CPI inflation indices

Fig. 13 Summary of major currency drivers

12-month outlook	The bullish case	The bearish case	12-month outlook	The bullish case	The bearish case
USD (DXY) ▼	+ Rising US yields; US exceptionalism + Safe-haven demand rises	– Global growth and rate differentials – Capital outflows & high twin deficits	USD/JPY ◆	+ Rising nominal US Treasury yields + Weak safe-haven demand for JPY	– Favourable real yield differentials – Elevated short JPY positioning
EUR/USD ▲	+ Fiscal spending drives EA growth + Germany raises fiscal stimulus	– Dovish ECB policy continues – China slowdown spills over impact	USD/CNY ◆	+ China policies too tight; slow growth + Renewed US-China tensions	– Rising global trade and exports – Continued CNY investment inflows
GBP/USD ▲	+ Vaccination-led growth recovery + Hawkish BoE as economy expands	– A resurgence of COVID-19 cases – Post-Brexit risks	USD/CAD ▼	+ Commodity price vulnerability + Faster growth may be priced in	– Global/US growth positive for trade – Hawkish BoC ahead of the Fed
AUD/USD ▲	+ Global growth and commodity prices + COVID policy re-set underpins growth	– More dovish RBA; slow vaccinations – Weaker Chinese demand	NZD/USD ▲	+ Domestic growth up; Hawkish RBNZ + Terms of Trade; Higher milk prices	– “Zero-Covid” policy; slow vaccinations – Vulnerability to China demand

Source: Standard Chartered Global Investment Committee

Legend: ▲ Bullish | ▼ Bearish | ◆ Rangebound

Technicals

Manish Jaradi

Senior Investment Strategist

China internet: Slide could pause

The CSI Overseas China Internet USD sector index could be about to pause as it approaches strong support area – an uptrend line from 2015 and the 2020 low. The pace and the extent of the fall and deeply oversold conditions also support this view. For a pause to be confirmed, at a minimum, the index needs to break above immediate resistance at the 10 August high of 7,367 (6% from the 26 August close).

Looking beyond a pause, a break above the 50-DMA (now at 8,028; 16% from the 26 August close) is needed for the short-term trend to change to rangebound from down – the last time the index was above the average was in March. A medium-term trend reversal (to an uptrend) could take a while to unfold. For instance, it took months of base building in 2019-2020 before the index gathered renewed upward momentum.

Europe financials: Looking to break out

The European financials sector index is yet again showing signs of renewed momentum after being in a sideways range for years. That is revealed by 1) a hold last year above the 2011 lows, 2) a near 100% retracement of the February-March 2020 slide, 3) the capitulation-type sell-off last year (which typically tends to signify the end of a downtrend).

However, in order to conclude that this time it is indeed different, the index needs to break crucial converged resistance at the top end of the channel and the 2020 high (rebounds since 2016 have been capped at similar resistance). A final confirmation would be a break above the 2015 high, which could open way for a multi-year uptrend, potentially towards 120 (90% from the 26 August close).

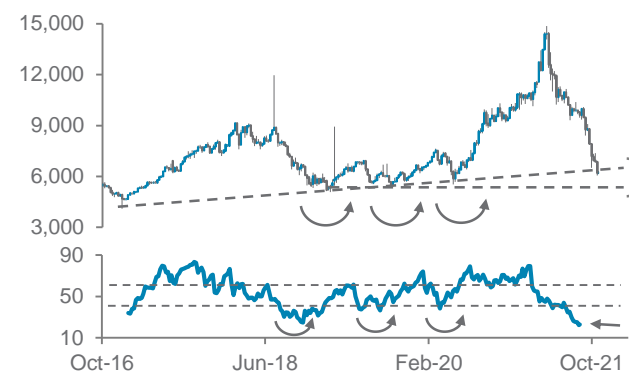
USD index: Stiff resistance ahead

The USD index (DXY) faces tough hurdles ahead, which could make it difficult for the greenback to rise meaningfully from current levels. To put this into context, the 2021 rebound is not surprising given the index had fallen to a strong support level at the 2018 low of 88.25.

However, the hold of a support on its own would not necessarily imply a reversal of the trend – it could well imply a pause. In this case, the feeble/choppy nature of the rebound since last year raises the prospect of a pause in the downtrend and the index could find it tough to break above the resistance cluster at 93.80-94.80.

Fig. 14 China internet: Slide could pause

CSI Overseas China Internet index weekly chart with RSI



Source: Bloomberg, Standard Chartered

Fig. 15 Europe financials: Looking to break out

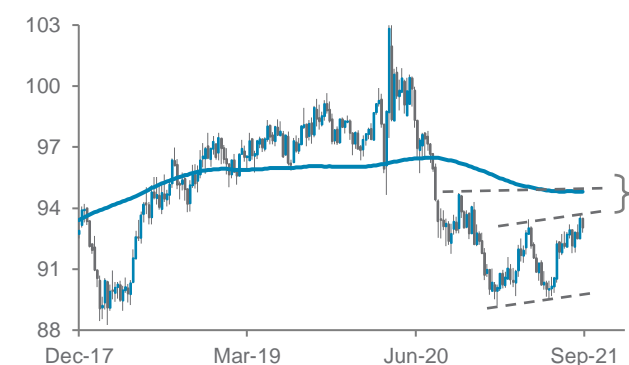
MSCI Europe Financials weekly chart



Source: Bloomberg, Standard Chartered

Fig. 16 DXY: Stiff resistance ahead

DXY weekly chart with 200-WMA



Source: Refinitiv, Standard Chartered

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.

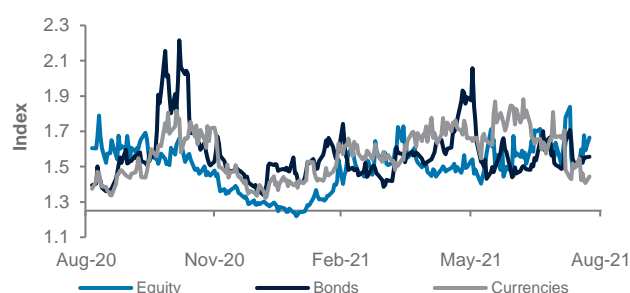
Where is diversity falling or rising this month?

Based on our proprietary diversity indicator, we do not see imminent signs of a price reversal across the assets we track, with exception for natural gas in the commodities basket and some China sectors. Natural gas is up sharply this year. Its recent rally ahead of a warm weather forecast has caused our diversity indicator for the asset to worsen further, signalling that chasing returns comes with increasingly higher risk.

For equities, there is no visible crowding. This includes our overweight calls on US and European equities, which have risen by 19% and 18%, respectively, YTD. Our indicator also shows no significant crowding in Asia ex-Japan equities that could cause a reversal of the recent downtrend.

Fig. 17 Average market diversity score across equities, bonds and FX

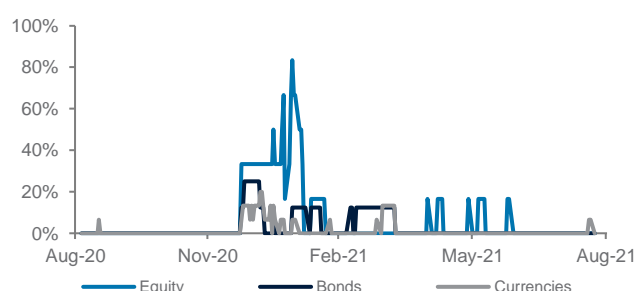
Market diversity is generally healthy



Source: Standard Chartered

Fig. 18 % of assets with diversity score < 1.25

No red flags across key markets



Source: Bloomberg, Standard Chartered

Meanwhile, the recovery in bond returns, especially in DM and EM credits, since the first quarter of this year has not triggered any red flags in our diversity indicator. This suggests the prevailing trends in the bond space are unlikely to be disrupted by any extreme investor views of these markets.

At the sector level, our diversity indicator is signalling hopes for a reversal or a slowdown in the downtrend for China's tech and property-related sectors. Their recent returns, however, remain lopsided, as hopes of policy easing seem inadequate in offsetting the negative sentiment around the recent regulatory clampdown by the government and the slowing economic growth. We would be cautious about forecasting the timing of a reversal in this situation given the risk that regulatory tightening might override any diversity signal.

Fig. 19 Healthy diversity at broad asset class level, but keep an eye on sectors

Level 1	Market diversity	30-day diversity trend
FTSE World Broad IG Bond	●	↑
MSCI All Country World	◐	→
Gold	◐	→
HFRX Global Hedge Fund Index	●	↑
China Sectors		
Communication Services	◐	↓
Real Estate	○	→
Commodities		
Natural Gas	○	→

Source: Bloomberg, Standard Chartered; data as on 23 August 2021

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	▼	14	6	3	0	14	6	3	0
Fixed Income	◆	63	38	28	7	63	38	28	7
Equity	▲	23	40	55	84	23	40	55	84
Gold	◆	0	5	4	4	0	5	4	4
Alternatives	◆	0	10	10	5	0	10	10	5
Asset class									
USD Cash	▼	14	6	3	0	14	6	3	0
DM Government Bonds	▼	3	2	1	0	5	3	2	1
DM IG Corporate Bonds	▼	6	3	2	1	8	5	4	1
DM HY Corporate Bonds	▲	12	7	5	1	18	11	8	2
EM USD Government Bonds	▲	14	9	6	2	11	7	5	1
EM Local Ccy Government Bonds	◆	11	7	5	1	9	5	4	1
Asia USD Bonds	▲	17	10	7	2	13	8	6	2
North America Equities	▲	8	13	18	27	12	22	30	45
Europe ex-UK Equities	▲	6	10	14	22	3	5	7	11
UK Equities	▲	1	2	3	5	1	2	3	5
Japan Equities	▼	1	1	1	2	1	1	1	2
Asia ex-Japan Equities	◆	6	10	14	22	4	7	10	14
Non-Asia EM Equities	◆	1	3	5	7	2	3	5	7
Gold	◆	0	5	4	4	0	5	4	4
Alternatives	◆	0	10	10	5	0	10	10	5

All figures in %. Source: Standard Chartered

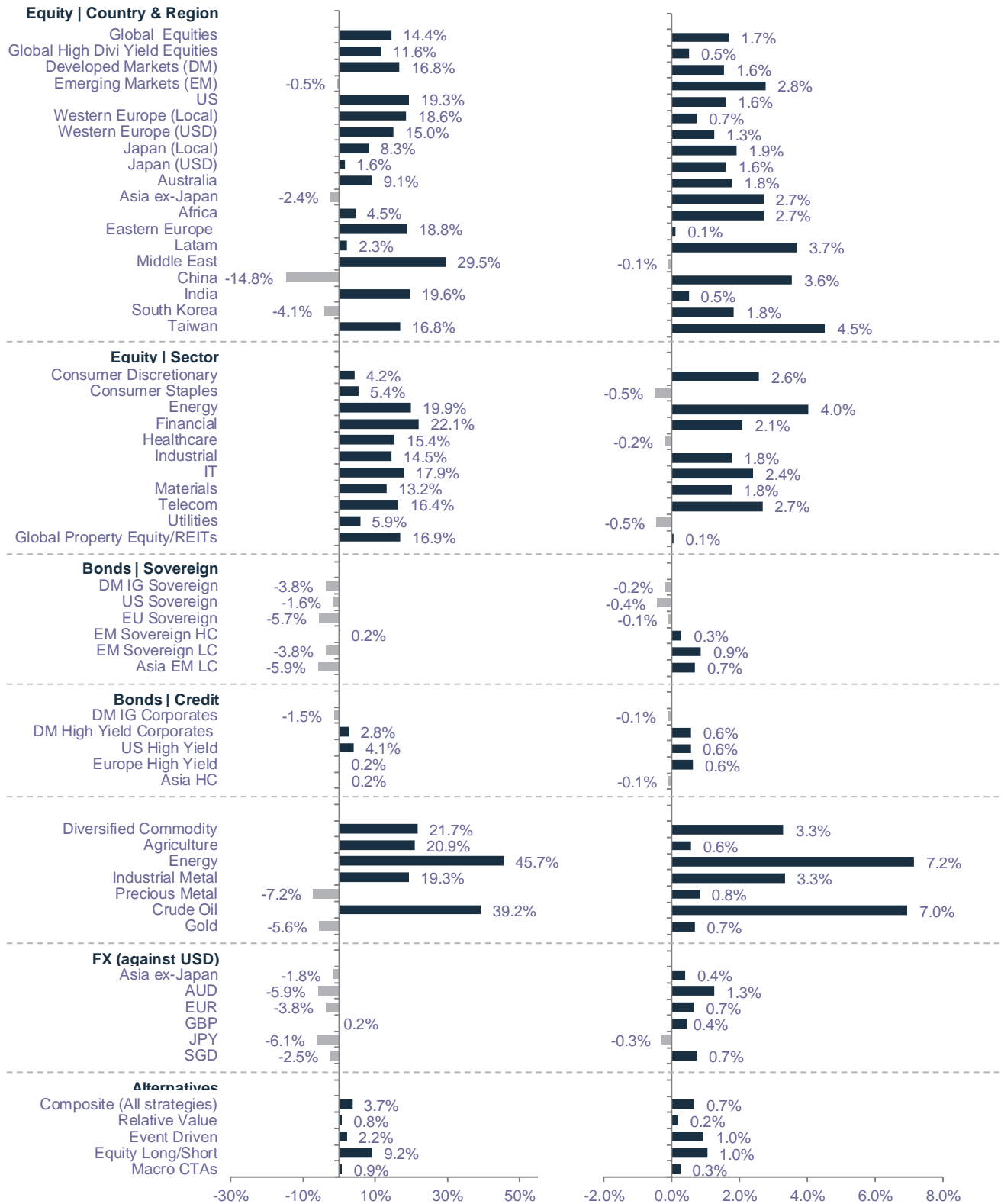
Note: Allocation figures may not add up to 100 due to rounding

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

Market performance summary*

2021 YTD

1 Week



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 2020 to 26 August 2021 and 1 week-performance from 19 August 2021 to 26 August 2021

2021 key events

SEPTEMBER 2021

9	ECB policy decision
22	FOMC policy decision
22	BoJ policy decision
23	BoE policy decision
26	Federal elections in Germany

OCTOBER 2021

22	Deadline for Japan General Elections
28	BoJ policy decision
28	ECB policy decision

NOVEMBER 2021

1-12	UN Climate Change Conference in Glasgow
03	FOMC policy decision
04	BoE policy decision

DECEMBER 2021

Dec	China Annual Economic Work Conference
15	FOMC policy decision
16	BoE policy decision
16	ECB policy decision
17	BoJ policy decision
31	Iran's deadline for the US to end sanctions

JANUARY 2022

20	ECB policy decision
26	FOMC policy decision

FEBRUARY 2022

3	BoE policy decision
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MARCH 2022

Mar	China National People's Congress session
9	South Korea Presidential election
10	ECB policy decision
16	FOMC policy decision
17	BoE policy decision
27	Hong Kong Chief Executive election

APRIL 2022

Apr	France Presidential elections
14	ECB policy decision

MAY 2022

4	FOMC policy decision
5	BoE policy decision

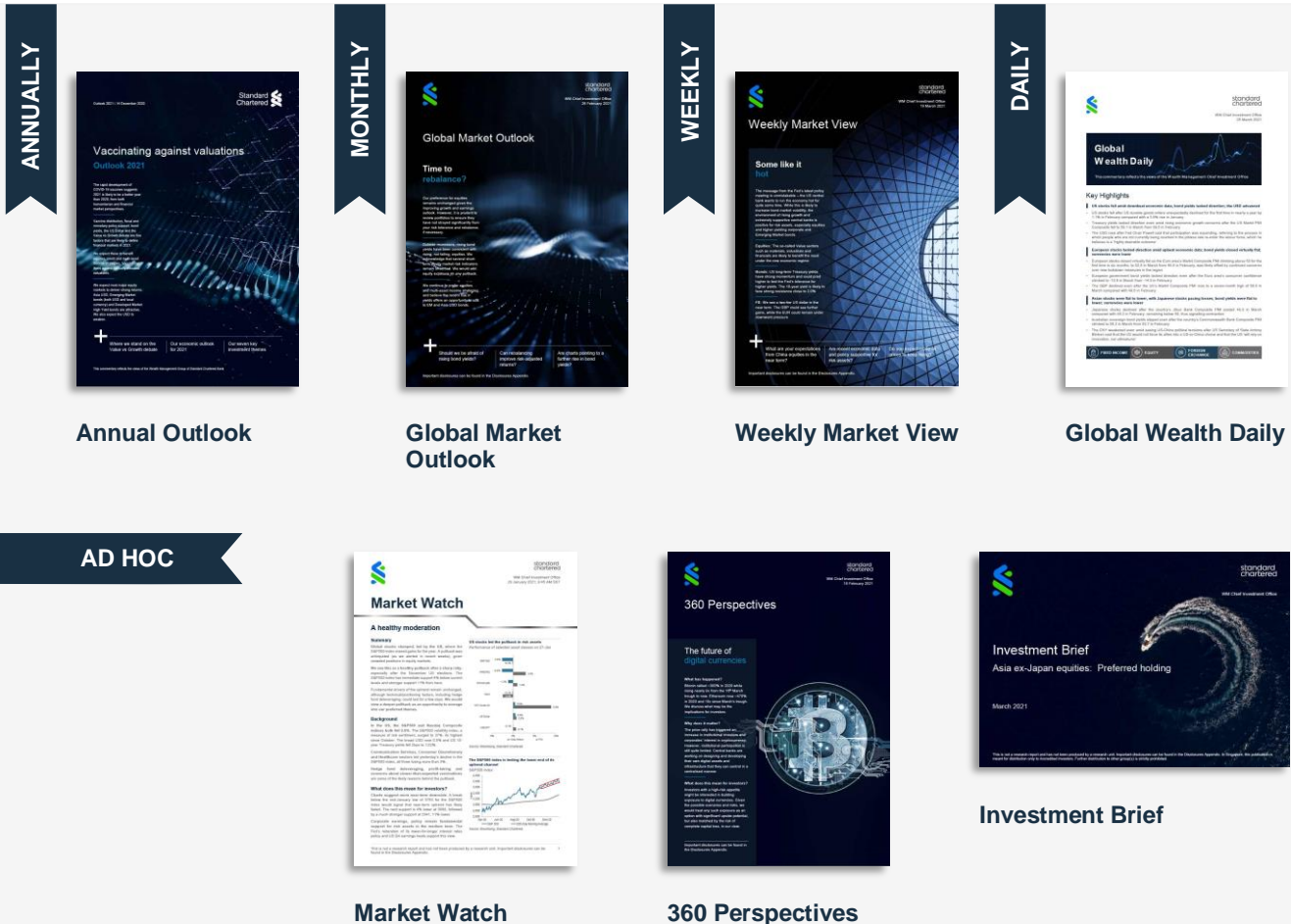
JUNE 2022

9	ECB policy decision
15	FOMC policy decision
16	BoE policy decision

■ 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

Our key advisory publications



Annual Outlook – The Annual Outlook highlights our key investment themes for the year, the asset classes we expect to outperform and the likely scenarios as we move through the year.

Global Market Outlook – Our monthly publication which presents the key investment themes and asset allocation views of the Global Investment Committee for the next 6-12 months.

Weekly Market View – Our weekly publication which provides an update on recent developments in global financial markets and their implications for our investment views.

Global Wealth Daily is an early morning update of major economic and political events and their day-to-day impact on various assets classes the previous day.

Market Watch focuses on major events or market developments and their likely impact on our investment views.

360 Perspectives provides a balanced assessment of the outlook for an asset class. It presents both the positives and negatives of the asset class, as well as the major drivers, instead of offering a specific view.

Investment Brief explains the rationale behind our views on an asset class, incorporating the fundamental and technical drivers.

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