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Wealth Management Chief Investment Office
3 June 2022

Global Market Outlook

The income opportunity

→ A strong equity rebound since mid-May brightens the near-term outlook, but it is natural to question whether this is the start of sustained gains (our base scenario) or just a bear market rally.

→ Nevertheless, earning attractive yields from income strategies has become much easier. Multi-asset income strategies offer an attractive opportunity to earn yields last seen at the peak of the 2020 sell-off. They are also a route to gain exposure to our preferred bond asset classes through a well-diversified allocation.

→ Within equities, Asia ex-Japan offers an opportunity to diversify away from the US-centric recession debate. Financial and energy sectors should benefit in the current macro environment.

Gold remains an attractive diversifier, especially if the USD is close to peaking.

+

How to hedge against a further rise in inflation?

What are the macro factors to watch in the coming weeks?

Is the USD finally turning?

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Investment strategy and key themes

Steve Brice
Chief Investment Officer

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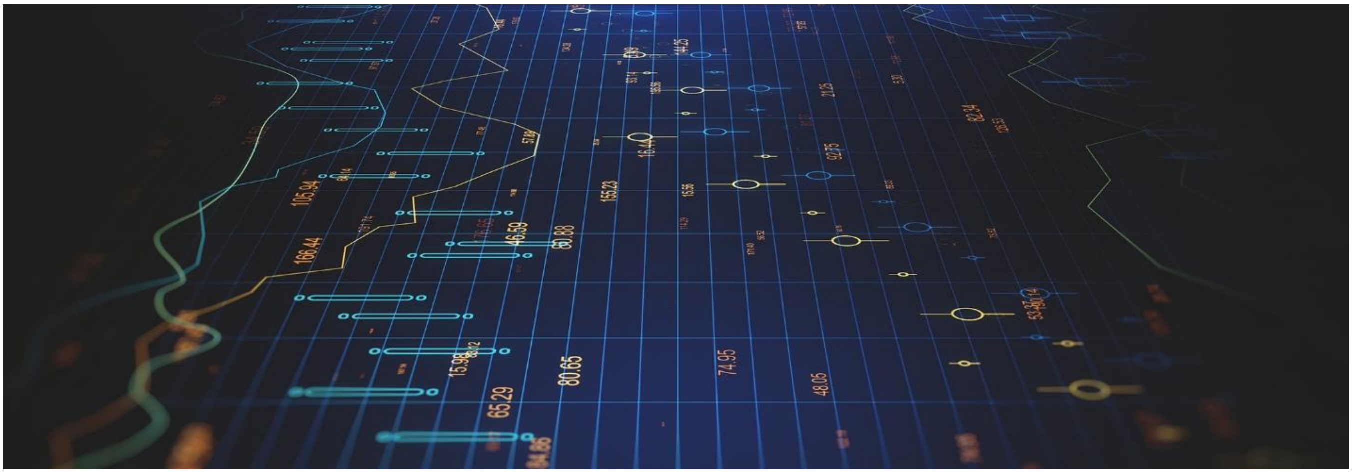

Our preferences (12-month view)

Foundation allocation preferences

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

Longer-term themes

- The Winds of Climate Change
  - Clean Technology, Electric Vehicles, Water Scarcity, Infrastructure/ Green Capex
- Embracing a Digital Future
  - Internet of Things and 5G, Cybersecurity
- China's 'Common Prosperity'
  - Hard Tech/Semiconductor, Renewables

Sector preferences

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

The income opportunity

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- Nevertheless, earning attractive yields from income strategies has become much easier. Multi-asset income strategies offer an attractive opportunity to earn yields last seen at the peak of the 2020 sell-off. They are also a route to gain exposure to our preferred bond asset classes through a well-diversified allocation.
- Within equities, Asia ex-Japan offers an opportunity to diversify away from the US-centric recession debate. Financial and energy sectors should benefit in the current macro environment. Gold remains an attractive diversifier, especially if the USD is close to peaking.

After the round trip, the scenarios

After a downbeat April, May offered investors some relief. Global equities staged a 7% rebound from mid-May to end the month approximately where they started. Bonds delivered slightly higher total returns as yields took a turn lower, while gold lagged.

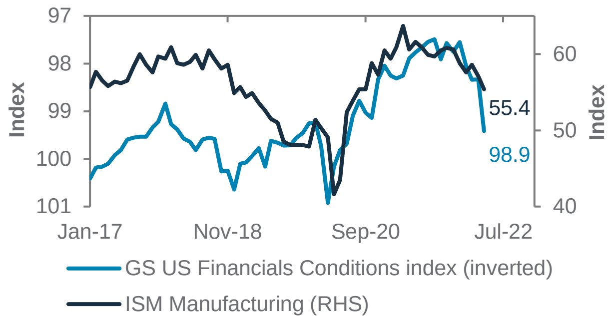
May's relief rebound notwithstanding, the key question remains: is this simply a temporary bear market rally or the start of more sustained gains? A combination of macroeconomics and market history could help offer some guidance.

US history shows equity markets do well in non-recessionary years. Global equity market valuations have dipped and yields have risen this year. This combination means long-term expected returns are starting to look more attractive than a year ago. Our own assessment shows a simple buy-on-dips strategy has worked well in recent decades, while another study noted that 3-12-month gains were usually strong after a 6% or greater weekly return.

The main caveat, of course, is that these conclusions hold in non-recessionary years. Therefore, as we illustrate in more detail in the *Perspectives* section, it may be helpful to think in terms of scenarios. Our base case scenario continues to assume no US recession within the next 6-12 months as US inflation eases in H2, enabling the Fed to turn its focus from fighting inflation to supporting growth. The lack of any new warning signals on our recession checklist and easing market inflation expectations in recent weeks support our base scenario.

Fig. 1 **Fed rate hike expectations have tightened US financial conditions, raising growth risks**

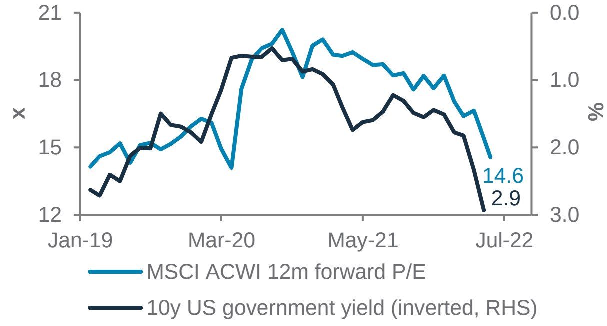
US financial conditions vs ISM manufacturing sentiment



Source: Bloomberg, Standard Chartered

Fig. 2 **Equity market valuations off the boil; the path of bond yields is key to where multiples go from here**

S&P500 12m P/E ratio, 10y US govt bond yield (inverted)



Source: Bloomberg, Standard Chartered

The main risk scenario, in our view, is one where inflation fails to peak as quickly as we expect and the market's inflation expectations return to, or exceed, recent highs. Besides continued supply disruptions, a further jump in oil prices is one way such a scenario could pan out. In this scenario, the Fed will be encouraged to 'overtighten' even if growth weakens. Nevertheless, we believe a data-driven Fed is likely to reverse course on signs the economy is weakening sharply.

Focus on the rebound

Regardless of the ultimate scenario, a near-term extension of the current equity rebound is likely. History shows buying-the-dip when 12-month returns turn negative (as they did for the S&P500 index at the end of April) was a strategy that delivered attractive benchmark-beating returns over time. Even under a recessionary/bear market scenario, history shows us that bear market rallies can be sizeable (averaging about 10-25% and lasting 21-58 days over the last 6 recessionary bear markets).

Within this bigger picture, there are three additional steps investors can take to diversify their risk while gauging recession risks. First, by continuing to hold gold, which we view as a preferred asset alongside equities. Second, through equity sector exposure. On a 6-12 month horizon, we continue to prefer the energy and financial sectors globally, healthcare sector in the US and Europe and industrial sector in China. We expect these sectors to be the most likely beneficiaries of our base case macro environment.

China offers diversification

A third way to diversify risk is through a varied regional allocation. Our scenarios offer a very US-centric view of the world. While this remains key for most major financial markets, China's economy and policy are at a different point in the economic cycle. This offers a way to diversify exposure from US-centric scenarios. China's weak economic data is well known, and arguably well priced, given the deep discount of Asian equities relative to global stocks and the large yield premiums on Asia USD bonds. However, China's gradual easing of tight COVID-19 restrictions and a noticeably greater policy emphasis on supporting economic growth are two positive catalysts that could support Asian equities from here.

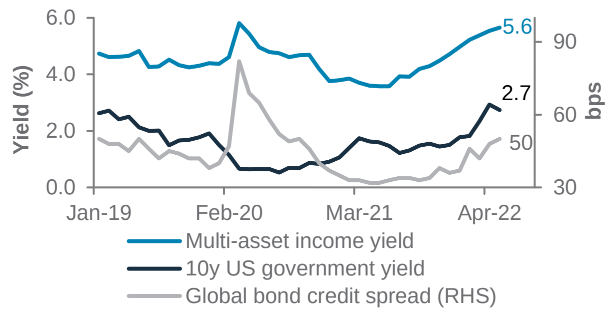
The income opportunity

This equity market debate notwithstanding, one opportunity that is relatively less debatable is today's increasingly attractive income yields. Our multi-asset income strategy now offers a yield of 5.6%, considerably higher than the sub-4% on offer for much of 2021 and not far from the 2020 sell-off peak.

Allocations to income strategy today benefit from both wider yield premiums and higher government bond yields. This strategy also offers a way to gain exposure to our preferred bonds – Developed Market High Yield bonds, Asia USD bonds and Emerging Markets USD government bonds – but within a well-diversified strategy that also incorporates high dividend-paying equities and non-core income assets such as REITs.

Fig. 3 **Multi-asset income yield not far from 2020 peak, benefiting from higher bond yields and yield premiums**

Multi-asset Income yield, 10y US govt bond yield, global corporate bond yield premium over Treasuries



Source: Bloomberg, Standard Chartered; As of 27 May 2022

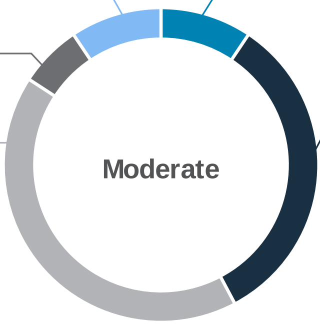
Has the USD peaked?

Recent narratives have increasingly questioned whether the ECB and other major central banks have room to catch up with the Fed. This raises the question of whether the USD has peaked (our base scenario). We continue to expect the USD to weaken over the next 6-12 months. We favour the commodity currencies (particularly the AUD) as one way to gain exposure, especially as their central banks continue to hike rates, offering a buffer against any short-term re-test of recent peaks in the USD or US government bond yields.

Foundation: Tactical asset allocation

Global* allocation model for a moderate risk profile

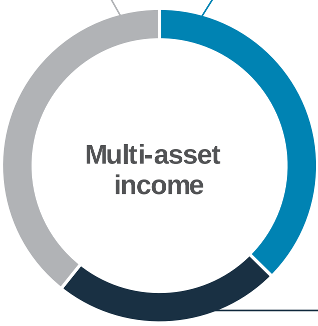
Alternatives	**9%**
Alternatives	9%
Gold	**6%**
Gold	6%
Equity	**42%**
North America Equities	20%
Europe ex-UK Equities	4%
UK Equities	2%
Japan Equities	2%
Asia ex-Japan Equities	10%
Non-Asia EM Equities	4%



Cash	**9%**
USD cash	9%
Bond	**33%**
DM IG Government Bonds	3%
DM IG Corporate Bonds	4%
DM HY Corporate Bonds	9%
EM USD Government Bonds	5%
EM Local Ccy Government Bonds	4%
Asia USD Bonds	7%

Multi-asset income allocation model for a moderate risk profile

Bonds	**39%**
DM IG Govt	2%
DM IG Corp	2%
DM HY Corp	13%
EM HC Govt	8%
EM LC Govt	4%
Asia USD Corp	7%
Asia HY Corp	3%



Equity	**37%**
Global high-dividend yield	30%
Europe high-dividend yield	8%
Non-core	**23%**
Covered calls	11%
Sub financials	9%
Others	3%

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

Source: Standard Chartered Global Investment Committee; *See page 16 for our Asia-focused allocations

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

Perspectives on key client questions

Audrey Goh, CFA
Head of Asset Allocation and Thematic Strategy

Hannah Chew
Portfolio Strategist

Inflation – The big picture

Global bonds and equities have witnessed one of the sharpest sell-offs in recent years, falling 12.7% and 12.3%, respectively, YTD. A key driver of this weakness has been persistently high inflation, which triggered concerns that the Fed could overtighten policy, causing slowing growth or even recession, while inflation remains elevated. Market volatility notwithstanding, the question on many investors' minds continues to be about whether they should hedge against inflation.

There are signs that the worst of inflation may be behind us, with the latest US headline CPI moderating to 8.3% in April from 8.5% in March and inflation expectations having eased significantly. In our base case, we expect US inflation to peak in H1 2022 before falling gradually to 5% by year-end.

However, there are several risks to our base case. First is higher oil and gas prices due to the return of Chinese oil demand after COVID-19 lockdowns end and as a result of the EU's recent partial ban on Russian oil imports. Second, higher wages and rental costs in the US may be 'sticky', sustaining recent rises. Third, China's COVID-19 restrictions could exacerbate supply chain disruptions. If any of these risks play out, it could mean inflation does not moderate quite as fast as we expect. In a pessimistic scenario, inflation could make new highs. Here, we explore possible asset classes that we believe can help hedge against such an outcome.

Fig. 4 **We see inflation easing somewhat in our base scenario, but the inflation outlook remains the key variable**

Possible macroeconomic scenarios with likely policy and market implications over the next 6-12 months

	Optimistic scenario (Low probability)	Base scenario (Our view: high probability)	Pessimistic scenario (Low but rising probability)
Inflation	• Inflation falls back towards **2-3%** levels • **Long-term inflation expectations fall back below 2.5%** as oil prices fall well below USD100/bbl	• **Inflation peaks in H1** and falls gradually to **5%** by end of 2022 • **Long-term inflation expectations stay below 3%** even as oil prices stay elevated	• Inflation continues to set **new record highs** • **Long-term inflation expectations rise above 3%** as oil prices continue to climb
Fed Policy	• **Fed pauses rate hikes in H2**, while continuing with a more moderate pace of quantitative tightening than currently projected	• Fed sees less of a need to tighten monetary policy as much as markets expect • **Fed slows down the hiking cycle after July**; keeps current pace of quantitative tightening • Fed policy rate ends at **2.25%** at end-2022	• Fed sees a need to tighten more aggressively than current market expectations • **Fed accelerates the hiking cycle and tightens beyond its 2.4% neutral rate estimate** by end-2022 and accelerates the pace of quantitative tightening
Economic Growth	• **Growth slows down towards pre-pandemic trend** • **Job markets remain robust**.(US jobless rate stays below the Fed's 4% target)	• **Growth slows down but remains above 3%**, well above the pre-pandemic trend of c.2% • Economy **avoids a recession**	• Growth decelerates sharply • Economy **enters recession within the next 12 months**
Financial Markets	• Both equities and credit rebound sharply • Gold underperforms	• Equities rebound and outperform credit, which outperforms government bonds • Gold outperforms on still-elevated inflation	• Equities and credit decline further • Government bonds outperform while Gold shines as a hedge

Source: Standard Chartered

Very high inflation regimes are positive for real assets and commodities

We segmented US CPI inflation into different regimes and focused particularly on the very high inflationary periods. Under this scenario, commodities were a standout performer, but private real estate, global REITs and gold also delivered some of the best returns. Real assets, such as global REITs, tend to capture the upside from inflation through greater income growth due to higher rents.

Equities were the clear underperformers in these high inflation regimes, particularly Developed Market equities, delivering negative returns across the board. This comes as increased borrowing and labour costs eat into their profit margins, weighing on the bottom line.

Bonds, counterintuitively, performed well, delivering positive returns. This is likely due to a high starting point in yields. Historically, when inflation was very high, Developed Market government bonds outperformed due to their safe-haven nature as investors were likely to rotate into the asset class while anticipating an economic downturn stemming from tighter financial conditions and inflationary pressures.

Fig. 5 **Gold, commodities and private real estate historically outperformed in high and very high inflation regimes***

Average 12m returns under high and very high inflation regimes (since index inception to April 2022)

	High inflation	Very high inflation
From 1977		
Gold	5.1%	11.6%
Commodities	1.6%	9.8%
Private real estate	8.9%	9.6%
From 2002		
Global bonds	2.6%	3.3%
Global equities	4.6%	-9.0%
US equity	4.0%	-10.1%
Euro area equity	5.0%	-7.9%
Asia ex-Japan equity	10.2%	-0.7%
DM govt bond	2.5%	4.0%
DM corp bond	3.8%	1.7%
DM HY	7.2%	-1.0%
EM USD	9.5%	1.7%
EM local	6.3%	3.9%
Asia USD**	7.2%	2.9%
Leveraged loans	3.6%	-3.1%
TIPS	2.5%	1.3%
Global REITs**	12.5%	5.7%
Natural resources equities	5.9%	-10.1%
Global infrastructure	11.3%	-4.3%

Source: Standard Chartered * High inflation regime is defined as CPI levels between 3-4%; very high inflation regime is defined as CPI levels above 4%. ** Asia USD index data since 2005 and Global REITs index since 2008

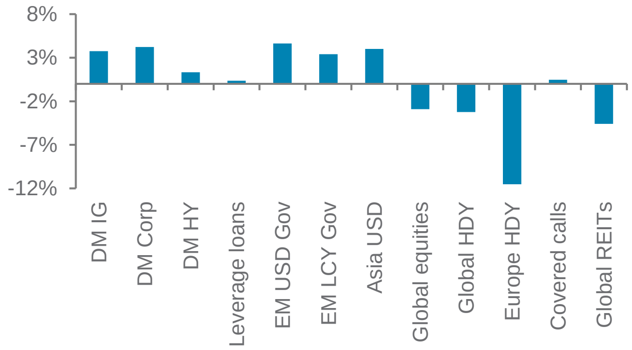
How to position a portfolio if inflation remains elevated

Against the current economic backdrop, the following strategies can help offer a hedge against scenarios where inflation remains elevated or ticks higher:

- **Have exposure to gold, private real assets, global REITs and commodities** – in our view, this is an important step towards getting an investment allocation 'inflation ready'. History shows these assets consistently outperformed during high inflation scenarios.
- **Consider increasing exposure to quality government bonds** – we maintain a neutral maturity profile stance (around five years to maturity) given upside risks to inflation. That said, higher rates tend to slow economic growth, and long-tenure bonds can start looking more attractive especially if growth slows or the economy enters a recession. At today's somewhat higher levels of bond yields, some exposure to high quality bonds may provide a good portfolio hedge against recession risk. Bonds with floating rate characteristics can also help.
- **Diversifying equity exposure** – global infrastructure and natural resource equities performed well alongside commodities this year. These assets have historically delivered positive returns under high inflation regimes – albeit up to a point until inflation reaches very high levels, causing all equities to fall sharply.

Fig. 6 **Credit assets were more resilient under rising inflation regimes**

Average 12m returns of various asset classes under a global growth falling and inflation rising economic scenario* (2005-2021)



Source: Bloomberg, Standard Chartered.
*Economic scenarios are identified by BCA research data across business cycles.

Therefore, assets, such as private real estate, commodities and gold, can help hedge against any adverse scenarios of still-high or rising inflation. While the performance of some of these hedges could turn lower under more optimistic scenarios where inflation falls more quickly than we expect, these assets should nevertheless enable investors to build diversified allocations prepared for a range of scenarios.

Our thematic ideas

Hannah Chew
Portfolio Strategist

We provide a brief overview of our currently open thematic ideas coupled with some recent highlights below.

Key themes	
Embracing a digital future	Technology stocks, especially our cybersecurity theme, continued to face pressure from rising bond yields. The impact can also be seen where earning revisions have turned down sharply, with consensus expectations for both Internet of Things (IoT) and cybersecurity-related earnings turning negative. While performance has been extremely challenged for cybersecurity, our IoT sub-theme performed in line with global equities since the start of May till date. We remain cautious in the near term given that certain communications-related companies have missed earnings expectations due to pressures from rising inflation and interest rates. Nonetheless, from a longer-term perspective, a study by Grand View Research Inc still provides a positive outlook: global 5G infrastructure is estimated to reach a market size of c.USD 96bn by 2030, with a compound annual growth rate of 34.2% from 2022 to 2030. With proper infrastructure in place, future deployment costs for 5G service providers are likely to decline, even as demand for their services rise. Therefore, we still see potential for the theme to deliver positive returns over the next 3-5 years.
The winds of climate change	The performance of climate-related themes has been weak, with Water and Electric Vehicles (EV) declining by c.17% since the start of 2022. Valuations across the board have trended up this month and earning revisions have deteriorated, with most sub-themes seeing only marginally positive revisions. However, all our sub-themes have outperformed global equities since the start of May against the backdrop of improving overall investor sentiment in recent weeks. We believe this rebound is also attributed to potential oil supply constraints that is leading to a renewed focus on alternative energy. Moreover, EU leaders' decision to partially ban Russian oil imports highlights the urgent need for alternative sources of energy to be made readily available. While we acknowledge that geopolitics remains a near-term headwind, we believe the outlook for renewable energy sources remains positive, given that European countries are likely to double down on efforts to become energy independent to hedge against oil supply disruptions. Thus, we retain our conviction in this theme over a 3-5 year horizon.
China's 'Common Prosperity'	2022 continues to be a challenging year for Chinese equities and our China-related themes continue to see losses of over 20% YTD. Valuations have become slightly more expensive for our high-tech manufacturing and renewables sub-themes, which are trading at a 12-month forward P/E of 22.5x and 16x, respectively. To mitigate the impact of soaring energy prices and geopolitical instability caused by the Russia-Ukraine war, China has announced plans for 169 new and expanded coal projects that would potentially reduce the country's chances of meeting short-term climate targets. However, China has also recently tripled its investments in solar power projects amounting to USD 4.3bn in the first four months. This puts the nation on track to install record amounts of new clean energy capacity. Although China remains reliant on coal in the interim, we view these parallel efforts to develop renewable energy capacity as a strong commitment towards meeting China's net zero goals. While the near-term outlook appears challenged due to seemingly conflicting decisions, we believe that strong political willpower will tide the country through in the long term in achieving both its economic and environmental targets.

Source: Bloomberg, Standard Chartered

Macro overview at a glance

Rajat Bhattacharya
Senior Investment Strategist

Zhong Liang Han
Investment Strategist

Key highlights

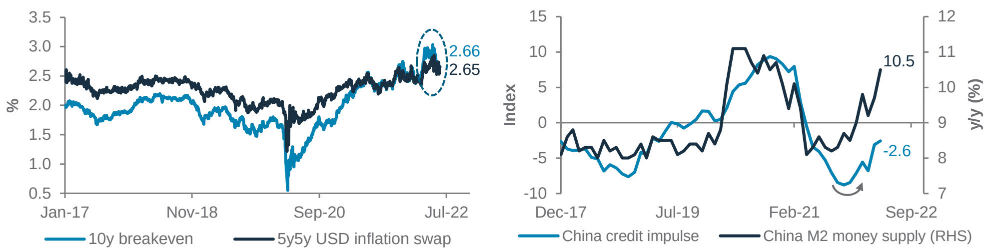
- US long-term inflation expectations appear to have peaked for now. We believe a sustained peak in inflation expectations is required for the Fed policy to turn less aggressive, the USD to ease and global risk sentiment to recover. As inflation expectations peaked, market expectation of the Fed policy rate for end-2022 has eased to around 2.80%, from a peak of 3% in early May. The market's expectation, which includes two 50bps rate hikes in June and July, is still above our end-year estimate of 2.25% - we expect the Fed to slow the pace of rate hikes in H2 as inflation decelerates. Our economic monitors continue to indicate a low probability of a US recession in the next 6-12 months.
- China's economy appears to have bottomed as authorities relax COVID-19 lockdowns and accelerate fiscal and monetary stimulus. Business confidence indicators point to a slower pace of contraction in May vs April. Meanwhile, the credit cycle is turning. In recent weeks, authorities have cut a key five-year interest rate linked to mortgages and infrastructure lending, while Premier Li Keqiang urged local governments to revive infrastructure spending. China's recovery is likely to provide support to Europe, where domestic sentiment remains subdued due to the Ukraine war, while a surge in energy-driven inflation erodes purchasing power. We see rising chance of the ECB lifting rates above zero in H2 to curb inflation pressures.

Key chart

A peak in US inflation expectations should enable the Fed to turn less hawkish in its policy stance in H2. China's credit cycle recovery portends a rebound in economic activity in H2.

Fig. 7 US inflation expectations have likely peaked, while China credit is picking up

US inflation expectations*; China's money supply growth and pace of change in credit growth



Source: Bloomberg, Standard Chartered; *Based on 10-year inflation-protected bonds, inflation swaps

Macro factors to watch

1. **Slowing activity indicators, rising wages:** Business confidence indicators (PMIs) continued to slow in the US and Europe in May, but output and employment indicators remained robust. Forward-looking indicators, such as new orders, still point to above-trend growth in the coming months. Rising input costs and delivery times remain a drag in the US, while wage pressures and rising interest rates emerge as areas of concern. We expect more lower income workers to return to the workforce in H2 as savings dwindle, especially with the rising cost of living. This is likely to put a lid on wages. We also expect the engine of growth to shift to services from goods consumption in H2 as economic activity normalises after the pandemic.
2. **Peak Inflation expectation, rising oil prices, Europe's Russian oil ban:** Although US inflation expectations have peaked for now, crude oil prices, which are a key driver of those expectations, have steadily risen in recent weeks, approaching February's high. Europe's partial ban on Russian oil could tighten global oil markets, even though Russian oil continues to flow into Asia and OPEC agreed to boost output. Europe's ban would also raise the risk of retaliation from Russia, including a possible stoppage of natural gas exports to Europe. Russia's response to Finland's and Sweden's plans to join NATO is another geopolitical risk. We do not expect Russia to cut off gas to Europe or engage with NATO as these moves are likely to severely impact Russia's economy.
3. **China's reopening:** The extent of China's relaxation of COVID-19 lockdowns ahead of November's Party Congress remains uncertain. Nevertheless, a gradual relaxation and increasing policy stimulus are likely to slowly lift domestic sentiment as well as business confidence across Emerging Markets and Europe in H2. The transmission of China's policy stimulus needs to be monitored closely, especially in the residential property and household consumption sectors where demand remains depressed. Meanwhile, the restart of activity in China is likely to ease global supply chain bottlenecks, potentially offsetting the inflationary impact of higher oil and commodity prices as China reopens.

Bonds at a glance

Abhilash Narayan
Senior Investment Strategist

Cedric Lam
Senior Investment Strategist

Key highlights

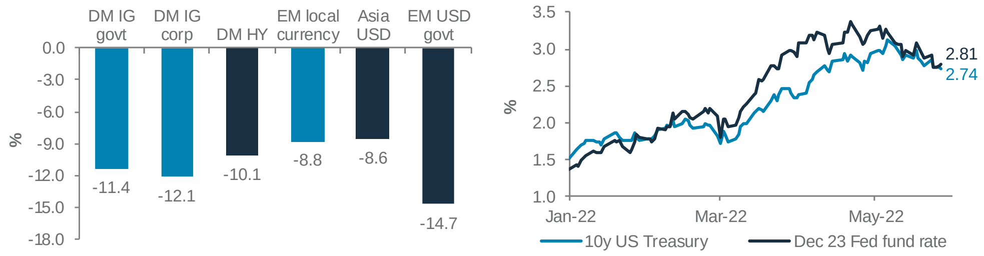
- Bond yields, especially in the US, declined in May, marking a welcome period of consolidation after the incessant sell-off since the start of the year. Tentative signs of peaking US inflation, Fed officials guiding towards rate hikes in line with market expectations and increasing risks of slowing global growth lead us to stick with our below-consensus forecast for Fed rate hikes and the 10-year US government bond yield. We continue to expect 10-year US government bond yields to trade in the 2.50%-2.75% range over the next 6-12 months, although a retest of 3-3.25% over the next few months remains likely.
- Our preferred areas – DM High Yield and Asian USD bonds – have delivered negative returns, but outperformed the global bond benchmark in 2022 YTD. As we assign low probability to a recession over the next 12 months, we view the recent increase in credit yield premiums as an attractive opportunity to add exposure. EM USD government bonds remain a preferred asset class as well, as we like the attractive yield and cheap valuations despite the idiosyncratic risks.

Key chart

An easing of the market's Fed rate hike expectations has been a key contributor to the recent fall in US government bond yields.

Fig. 8 **Bond yields likely to consolidate after a torrid start to the year**

YTD performance of key bond asset classes; 10-year US government bond yield and Fed Fund Futures implied US interest rate



Note: As of 30 May 2022. Source: Bloomberg, Standard Chartered.

"What now?" after a painful start to the year

Global bond markets have had the worst start to a year since the availability of our benchmark data more than two decades ago. YTD, global bonds are down by more than 10%. Till now, the worst start of the year saw negative returns of c.3.5% in 2013, when yields rose sharply due to taper tantrum.

As painful as the sell-off has been, it is important for investors to not succumb to recency bias and let past returns influence their forward-looking investment decisions. There are two key factors that are worth considering for bond investors:

1. We have been highlighting for the past few months that we viewed the run-up in yields and rate hike expectations as excessive given that we expected growth and inflation to slow down in H2. The recent decline in US government bond yields has been closely correlated with the repricing of rate hike expectations.

   While the Fed is still likely to hike rates by 50bps in June, we believe the market has potentially seen a peak in rate expectations, consistent with our expectation the 10-year US government bond yield is likely to trade in the 2.50-2.75% range in 6-12 month's time, though we do not rule out a near-term spike.
2. Over the past decade, low bond yields have been a key challenge for bond investors, which gave rise to terms such as TINA (There Is No Alternative). However, today, with yields across most areas in bonds close to multi-year highs, investors have a viable alternative to equities.

In China, greater urgency among policymakers to ease COVID-19 restrictions, the roll out economy-supportive measures and the improvement in the credit impulse are supportive for Chinese economic growth. Recent measures to support property developers' access to onshore funding and boost property demand should also help stabilise the real estate sector. When we combine that with cheap valuations and low net supply this year, we believe Asian USD bonds have a high probability of outperforming global bonds.

In DM HY bonds, we see the cheap valuations at odds with low default rate and improving corporate credit quality. Higher oil prices should also be supportive for energy sector bonds. Hence, the current yield of over 7.5% on offer looks extremely attractive to us, even after we factor in the risks from potential slowdown in US growth over the next 6-12 months.

Equity at a glance

Daniel Lam, CFA
Head, Equity Strategy

Fook Hien Yap
Senior Investment Strategist

Key highlights

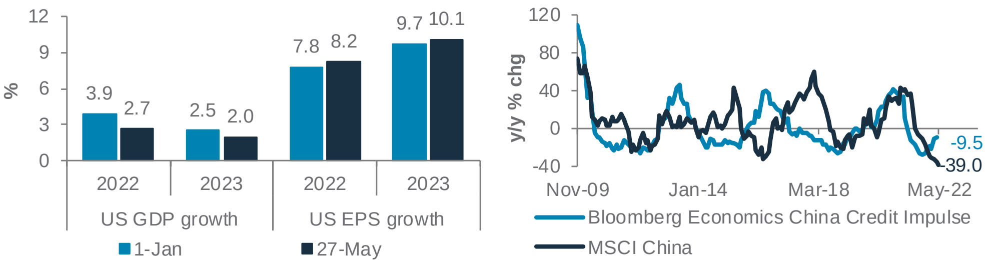
- Global equities remain a preferred asset class on a 12-month horizon. The pressure on global equities has eased lately as US government bond yields pulled back after hitting resistance around 3.2%. Earnings growth remains robust, especially in the US. Key technical support levels were held in May's drawdown, with good volume buying interest near support levels.
- Asia ex-Japan remains our most preferred market – the region's valuations are relatively undemanding, with its 12-month forward P/E ratio at an 18% discount to global equities. China has stepped up policy support in recent weeks. Significant easing of COVID-19 lockdowns should provide a tailwind for China and Asia ex-Japan equities to outperform in the coming months.
- US equities remain a core holding. Technically, the market has overcome the downtrend in place since March 2022. We believe there is room for a gradual recovery in US equities over the next 6-12 months as inflation data eases, enabling the Fed to turn less hawkish, compared with market expectations.

Key chart

The robust earnings growth should continue to support US and global equities. Meanwhile, policy easing in China should provide an impetus for Asia ex-Japan equities to outperform.

Fig. 9 **Consensus US earnings growth estimates have been revised higher since the start of the year even as GDP growth estimates were downgraded; we expect China equities to respond positively to stimulus measures and a rebound in credit impulse**

Consensus US GDP growth and MSCI US EPS growth estimates; Bloomberg Economics China Credit Impulse and MSCI China index



Source: MSCI, FactSet, Bloomberg, Standard Chartered

Crouching dragon, taming US inflation

Policymakers in the US and China are fighting two different battles now. The US is looking to reduce inflation, while China is seeking to revive growth. Our base case remains that US inflation can be tamed without a recession. This, combined with the policy stimulus in China, should spur global equities to outperform other asset classes over the next 6-12 months.

Facing high inflation, the US Fed is raising interest rates and removing pandemic-era monetary stimulus. The Fed's action has already contributed to consensus downgrades for US GDP growth since the start of the year. Cost inflation is also worrying as it could squeeze profit margins, reducing corporate earnings.

However, US equity valuation has already derated since the start of the year, with the 12-month forward P/E multiple falling c.19%. If inflation is controlled in H2 2022 as we expect, we are unlikely to see aggressive interest rate hikes, sparing US stocks from further valuation derating. US earnings have also remained resilient, with consensus EPS growth upgraded slightly since the start of the year. Higher inflation and commodity prices are boosting earnings in some sectors, while higher interest rates support banks' earnings and digitalisation continues to drive growth in the technology sector. These are likely to offset the negative impact of inflation and a slower economic growth. We expect earnings growth to continue supporting US equities, enabling them to perform in line with global equities over the next 6-12 months.

Meanwhile, China equities remain 47% below their peak in February 2021 amid stringent COVID-19 lockdowns. We believe the market has not priced in policy stimulus measures, such as the reduction in interest rates and taxes, easing of property financing rules and infrastructure spending. Such stimulus is likely to be more effective once lockdowns end. Sentiment is still poor, but we expect China's easing policies to support Asia ex-Japan equities to outperform global equities over the next 6-12 months, with China performing in line with Asia ex-Japan.

FX at a glance

Manpreet Gill
Head, FICC Strategy

Francis Lim
Senior Quantitative Strategist

Key highlights

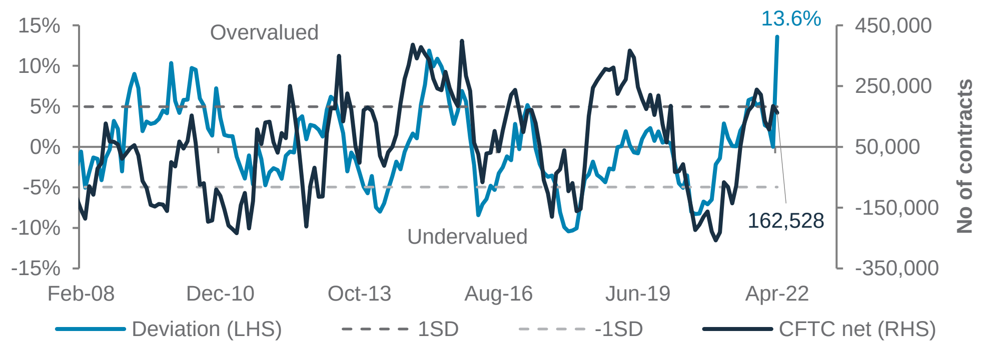
- Our 6-12-month USD view is bearish. We expect the USD to peak in Q2 as i) Fed policy expectations reach peak hawkishness as growth eases along with inflation data; ii) other central banks, including the ECB and eventually the BoJ, continue to normalise monetary policy to avert currency weakness that amplifies inflation; iii) capital flows rotate away from the US towards more attractively valued assets; iv) steady de-dollarisation continues, and v) uncertainty rises around US politics and future policy direction. The USD has already priced in significant Fed hikes, slower global growth and considerable safe-haven risk. The timing of the USD reversal will likely be driven by the speed of global monetary policy convergence, the easing of China's zero-COVID-19 policies, alongside robust stimulus and some kind of resolution to the Ukraine war.
- Technicals suggest the USD index (DXY) may have peaked at 105 in May, although a sustained break below 101 would add confidence that another new high can be avoided. We also expect the EUR and the JPY to continue to see a slow strengthening after a period of continuous heavy selling. Commodity currencies, particularly the AUD and CAD, should continue to be underpinned and the bifurcation of energy exporter currencies versus importers is likely to continue by varying degrees.
- Key risks for further USD strength are: i) a rise in US household and business credit expansion, despite rising interest rates, that exacerbates inflation and prompts the Fed to "chase" inflation-fighting at a faster rate; ii) further degradation in the global economy that reduces the attraction of USD alternatives, and iii) a continuing decline in global risk sentiment as political and geopolitical tensions rise. A DXY index breach above 105 resistance would open up the next target of 109.

Key chart

Despite the recent USD decline, it is now overvalued, driven largely by a fall in relative rate differentials.

Our proprietary DXY valuation model uses real yields, equity prices, inflation, current accounts and commodities as inputs. A deviation from 0% implies a potential USD mis-valuation.

Fig. 10 Our model suggests the USD is significantly overvalued and positioning is long
Deviation of DXY value vs our model; CFTC net USD positioning



Source: Bloomberg, Standard Chartered

The USD may finally be turning

We believe the Fed will not hike rates as many times as the market currently expects, and non-US central banks will continue to pivot to more hawkish stances. Nominal yield differentiation, which has supported the USD, should fade. There is potential for USD selling to rise through the summer as the focus shifts to US mid-term elections and policy continuity concerns. Commodity exporter countries with hawkish central banks (AUD, CAD) are likely to continue to outperform commodity importer currencies with more dovish central banks (EUR, CHF).

Two uncertain variables could determine the USD peak. Firstly, the Ukraine war, where any eventual de-escalation should lead to improved risk sentiment, even as inflationary pressure still prompt the ECB to normalise monetary policy while the window is open. Secondly, China may claim victory against COVID-19 as the summer nears and cases naturally peak, allowing targeted fiscal stimulus to be deployed during economic re-opening. Both events would support a global growth rebound and add momentum to a USD reversal.

We continue to prefer the AUD, CAD and NZD as commodity prices should remain elevated and their respective central banks stay focused on countering inflation. The EUR should be an eventual beneficiary of a USD peak. We continue to believe that the JPY is undervalued, oversold and ripe for a surprise reversal. BoJ policy remains easy but rising inflation expectations could trigger relaxation of yield curve control and a sudden unwinding of carry trades in the coming months.

Gold, crude oil at a glance

Manpreet Gill
Head, FICC Strategy

Nataniel Tang
Investment Strategist

Key highlights

- We continue to favour gold as we believe it remains an attractive portfolio diversifier. Gold prices have fallen from last month, and it has been trading between USD 1,790 and 1,870/oz. However, we believe that gold has the potential to rise towards USD 2000/oz as geopolitical tensions remain elevated. A peaking USD, resilient consumer and central bank demand and rising gold ETF investment demand continue to provide tailwinds for the precious metal.
- We remain bullish on oil prices as fears of a disruption in global supply continue to plague the market. Following the recent EU embargo on most Russian oil imports and the ban on EU companies' insurance of Russian oil shipments anywhere in the world, we expect global crude supplies to tighten further, even as OPEC+ agreed to ramp up oil production by 650k/bpd in the next two months. US crude stockpiles continue to draw down and global demand for oil could potentially pick up as China begins to ease its lockdown measures. There may also be ramifications for global inflation and growth if oil prices rise too sharply, and if Russia retaliates further by restricting the supply of gas.

Key chart

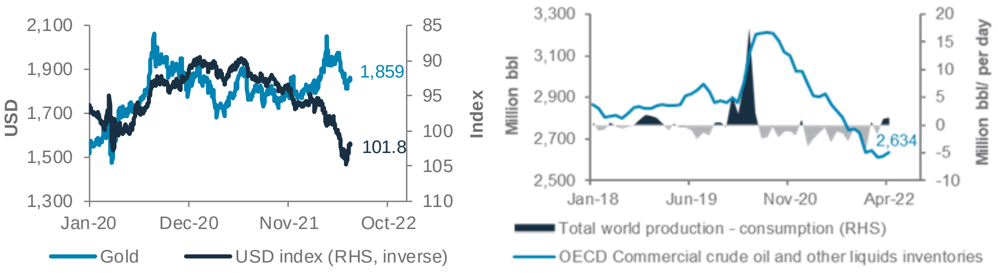
Gold offers an attractive hedge against geopolitical risk; a peaking USD is also a boon for the metal.

EU sanctions against Russia pose significant upside risk for oil; reduced COVID-19 lockdowns in China could also boost demand.

Fig. 11 **Gold has performed as a safe-haven asset and a peaking USD would add support for high gold prices; OECD crude oil inventory have been diminishing, while global oil consumption has exceeded production from June 2020 and for most of 2021**

LHS chart: Gold vs USD Index (DXY)

RHS chart: OECD crude oil and liquid fuel inventory vs Global net oil production*



Source: Bloomberg, EIA, Standard Chartered
*Grey area represents global net oil production (production minus consumption)

A brighter future for gold?

Gold has experienced headwinds from rising interest rate expectations and a strong DXY that reached a high of 105 (a level last seen in 2002). However, following a recent dovish tilt in the Fed's FOMC May meeting minutes, we believe that hawkish interest rate expectations may be largely priced into markets. As such, we do not expect bond yields to constrain gold and our view of a peaking USD is likely to lend tailwinds to gold in the long term. Also, our proprietary Equity-Bond Market Risk model continues to signal a high risk of moving to Stage 4, a stage usually consistent with gains in gold.

Investment demand for the precious metal remains solid. Robust demand for gold ETFs continues as investors look to hedge risk amid the uncertain geopolitical backdrop. Consumers are also turning to physical gold to protect the real value of their wealth as stagflation fears increase. Gold has the potential to continue outperforming as a safe-haven asset.

What is the outlook for oil?

Oil prices are likely to remain elevated. The EU's sanctions on Russian crude supply, not only directly to Europe but also on global shipments that would previously have been insured by European companies, could restrict total global supply. There is uncertainty around how this shortfall will be offset. OPEC's decision to increase output by 650k/bpd in the next two months should alleviate some of the shortfalls.

Global oil inventories continue to draw down and remain at a four-year low, while global consumption has exceeded production for nearly half of 2020 and 2021. OPEC+ has also struggled for months to keep up with their quota increases as members remained plagued by capacity concerns. Additionally, demand is forecast to increase as China could potentially ease its COVID-19 lockdown policy. A key risk to our view is strong demand destruction or slowing global growth.

Quant perspective

US market risk model – upgraded equity risk, but …

Francis Lim
Senior Quantitative Strategist

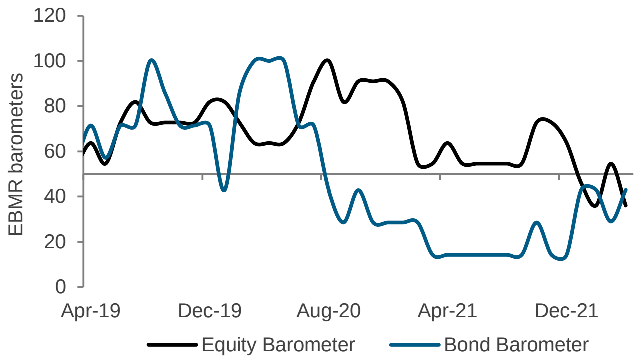
Bearish on equity and bond market risks

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

The US EBMR model shifted back to Stage 4 from 3 in May as we have anticipated last month. In Stage 4, the model is against taking on excessive risks in both US equity and US government bonds. Previously, we have highlighted the model's shift to Stage 3 was of lower quality as the improvement in the equity risk barometer of the model is primarily driven by a volatile equity momentum signal that turned modestly positive and its deterioration intra-month was not captured as the model uses monthly frequency data.

Fig. 12 **EBMR bearish on equity and bond market risks**

US equity and bond market risk barometers



Source: Standard Chartered

The equity barometer is currently sitting at 36, below the 50 mark, indicating a bearish outlook for US equity market risk. The barometer turned lower as both our equity momentum signals over the short- and medium-term horizons turn bearish. Other negative factors include the US 10-year government, corporate AAA and 90-day commercial paper yields as rising interest rates are unsupportive of equity market risks under an inflationary environment. Factors that are still supportive of the equity barometer are money supply and US housing starts, but both have slowed significantly.

Our bond barometer remains bearish but has improved from 29 to 43 in May. The barometer has been bearish on government bond market risk since August 2020 (21 months). Over this period, the US 10-year government bond yield has risen by around c.200bps (bond price falls as yield rises). Factors that continued to remain unsupportive of the bond barometer are high commodity prices, low US jobless claims, still expansionary US Manufacturing PMI and the recovery in US capacity utilisation. Put together, these factors are inflationary in nature, which is negative for bonds.

The model's projections remain skewed towards Stage 3 over the next four months but the probability of moving to Stage 4 has risen significantly. This implies that the base case that US equities will outperform bonds has become more uncertain.

Implications on global assets

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

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

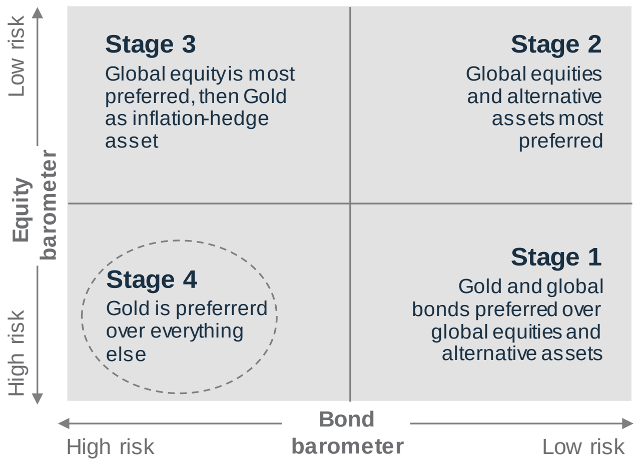
Probability of the evolution of financial market risk cycle from the current Stage 3 and preferred assets

Model's estimated probabilities in December 2021

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

Model's estimated probabilities in May 2022

Stage	Jun-22	July-22	Aug-22	Sep-22
1	38%	7%	13%	11%
2	6%	11%	23%	10%
3	14%	**57%**	**52%**	**68%**
4	**42%**	25%	12%	11%



Source: 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.

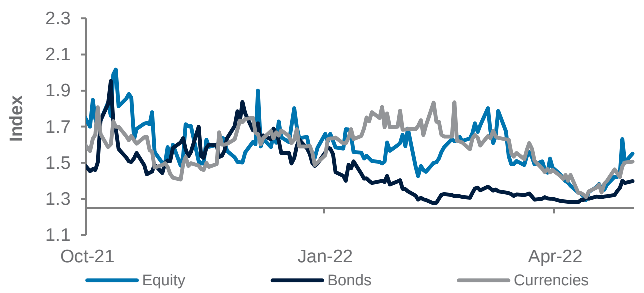
Where is diversity falling or rising this month?

In May, we saw a rare occasion where the number of assets with low diversity jumped in the bond and currency markets (see Figure 4). These included government bonds and credits for DM and EM, and USD/CNY, USD/JPY, GBP/USD and USD/MYR. The diversity of these assets, however, has quickly improved after a reversal, coinciding with a pause in the rise of US 10-year government bond yield and the USD.

In equities, we continue to see levels of diversity above our threshold for reversal despite their weakness, especially in Asia ex Japan and US equities. This is due to the elevated volatility in equities seen this year, which acts as a balancing force for market diversity in these assets. Meanwhile, the diversity of DM government bonds remains depressed, but it has broadly improved across other bond markets as signs of bottoming started to emerge.

Fig. 14 Average market diversity score by asset class

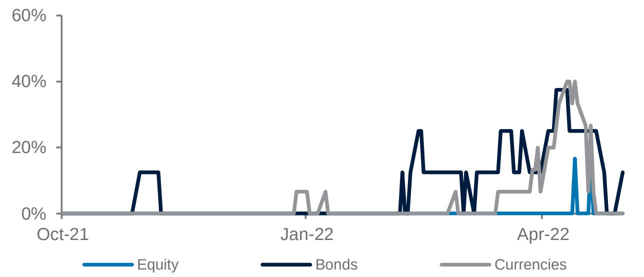
Diversity of bonds started to improve



Source: Standard Chartered

Fig. 15 Percentage of assets with diversity score <1.25

Red flags in bonds started to ease



Source: Bloomberg, Standard Chartered

In currencies, we have previously flagged that the steep rise in USD/JPY is at a heightened risk of reversal as its diversity is below the threshold of 1.25. We also recommended to watch out for GBP/USD and USD/MYR as their diversity was edging dangerously close to 1.25. USD/JPY and GBP/USD have since reversed, while the gains in USD/MYR have also slowed significantly. The diversity of these currencies is now safely above the reversal threshold of 1.25.

None of the key sectors we track has diversity below the critical threshold of 1.25, except for Europe and China real estate due to their prolonged weakness. Meanwhile, the diversity of the energy sector is no longer as stretched as when we flagged it previously. Despite their strong gains this year, the broad-based weakness in equities during April helped balance out the diversity of the energy sector.

Fig. 16 Diversity across key assets/sectors

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

Source: Bloomberg, Standard Chartered; as on 31 May 2022

Legend: ○ Very low ◐ Low/moderate ● High

Foundation: Asset allocation summary

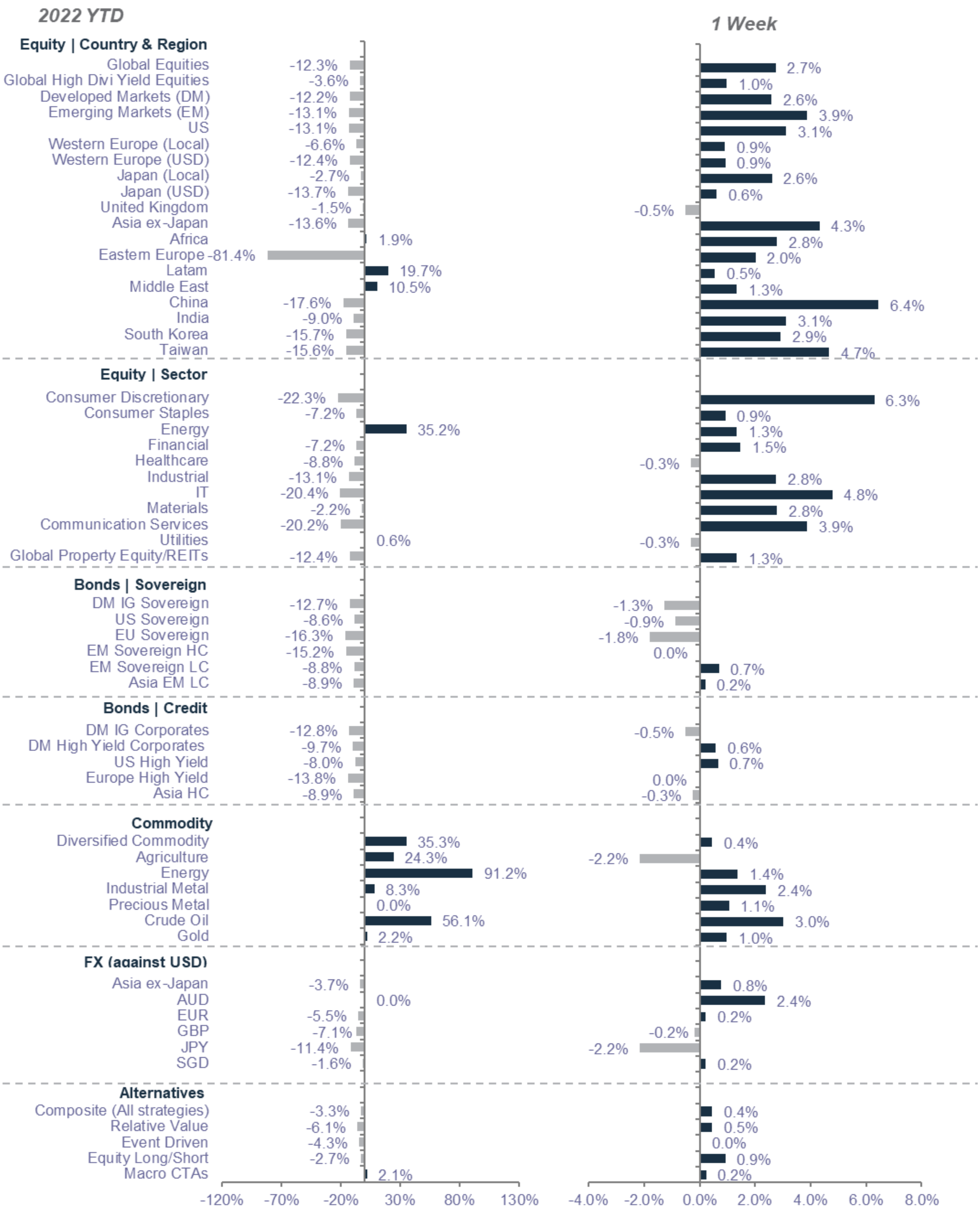
Summary	View	ASIA FOCUSED				GLOBAL FOCUSED			
		Conservative	Moderate	Moderately Aggressive	Aggressive	Conservative	Moderate	Moderately Aggressive	Aggressive
Cash	◆	21	9	4	0	21	9	4	0
Fixed Income	▼	56	33	23	6	56	33	23	6
Equity	▲	23	42	57	84	23	42	57	84
Gold	▲	0	6	6	6	0	6	6	6
Alternatives	◆	0	9	9	4	0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

Source: Standard Chartered; *FX-hedged

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

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

Market performance summary*



Source: MSCI, JPMorgan, Barclays, Citigroup, Dow Jones, HFRX, FTSE, Bloomberg, Standard Chartered
*All performance shown in USD terms, unless otherwise stated
*YTD performance data from 31 December 2021 to 02 June 2022 and 1 week-performance from 26 May 2022 to 02 June 2022

Key events

2022

JUN

- 07 Jun > Australia: RBA holds interest rate meeting
- 09 Jun > ECB policy decision
- 15 Jun > FOMC policy decision
- 16 Jun > BoE policy decision
- 17 Jun > BoJ policy decision
- 25 Jun > Finland: Results of NATO membership discussion due
- 26-28 Jun > Germany: 48th G7 Summit
- 29-30 Jun > Spain: NATO Summit

JUL

- 20 Jul > BoJ policy decision
- 21 Jul > ECB policy decision
- 27 Jul > FOMC policy decision

AUG

- 04 Aug > BoE policy decision

SEP

- 08 Sep > ECB policy decision
- 15 Sep > BoE policy decision
- 21 Sep > FOMC policy decision
- 22 Sep > BoJ policy decision

OCT

- 27 Oct > ECB policy decision
- 28 Oct > BoJ policy decision

NOV

- 02 Nov > FOMC policy decision
- 03 Nov > BoE policy decision
- 08 Nov > US House/Senate elections

DEC

- 14 Dec > FOMC policy decision
- 15 Dec > ECB policy decision
- 15 Dec > BoE policy decision
- 20 Dec > BoJ 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

For more insights

Market views on-the-go (MVOTG)

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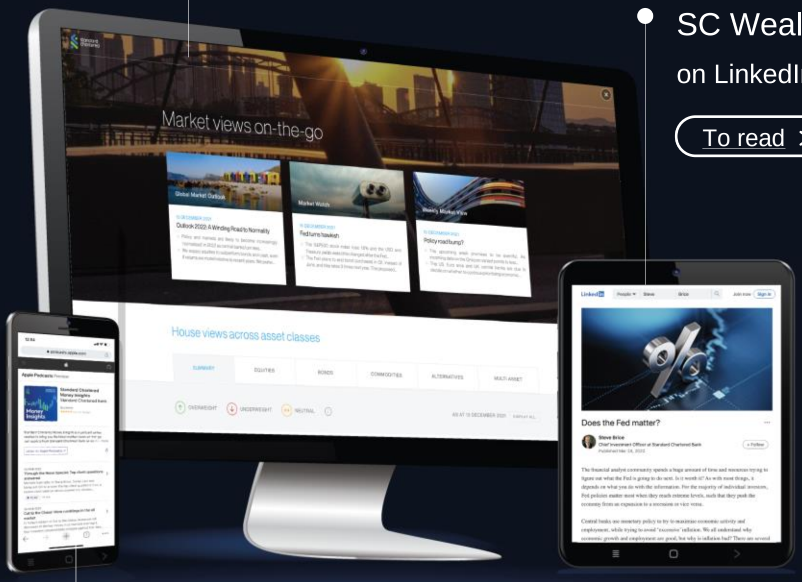

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