Market Watch

A growth scare?

Summary

Equity indices fell amid growth concerns. The S&P500 fell 3.2% with European and Japanese stocks, as well as oil prices, falling alongside.

Policy rate hikes, growth worries remain key market concerns. The Fed's Kashkari noted bringing inflation lower could take longer than expected, though a Fed survey did show 1-year inflation expectations slowed slightly.

US inflation, Chinese policy efforts, technicals are key signposts. Yesterday's market move weakens the near-term technical picture slightly, but whether US inflation has peaked is likely to be a key focus this week.

Background

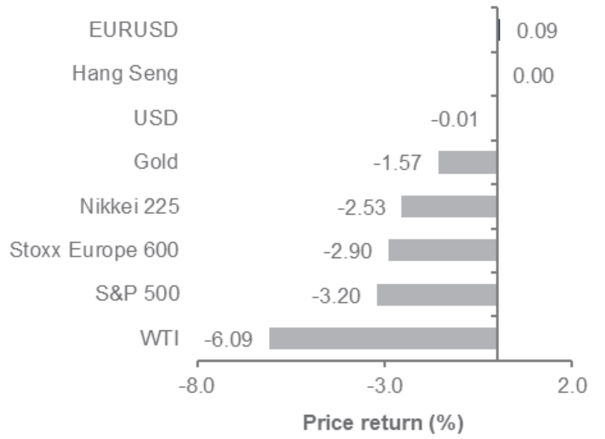
Equity markets had a volatile start to the week, after what was already a tumultuous past week. US equities led the weakness, with the S&P500 and Nasdaq falling 3.2% and 4.3%, respectively. The energy sector led the decline following a 6.1% fall in WTI oil prices. Equities outside the US also declined, led by Japanese and European indices, though by smaller magnitudes than the US. Gold fell and the USD Index (DXY) was flat. Bond yields initially rose, but then fell.

Impact of policy tightening on growth remains a concern. Concerns about how much Fed tightening is likely in the pipeline, and what impact it may have in terms of slowing growth, remains an ongoing narrative. Minneapolis Fed President Kashkari said that he was confident inflation would return to normal, but noted it would take longer than expected with the Fed unable to influence supply constraints. On the positive side, a Fed survey showed consumer inflation expectations over the next year fell to 6.3%, a 0.3% decline from March.

Chinese data was likely an additional factor yesterday. A slowing of headline export growth to 3.9% y/y raised questions about economic growth in major economies. Meanwhile, ongoing Covid lockdowns have meant markets have questioned the growth outlook in China domestically, and its implications for commodities demand.

US, European and Japanese equities fell, alongside oil prices, amid growth concerns

1-day price return (%) on 4 May



Source: Bloomberg, Standard Chartered

China's export growth slowed to 3.9%, weakest pace since June 2020

China export growth data y/y

Source: Bloomberg, Standard Chartered

What does this mean for investors?

S&P fall still well within pullback territory, though correlations remain a challenge. The S&P500 is now down about 17% from its most recent peak. On its own, this remains within the 10-19% pullbacks witnessed six times within the broader 2009-2020 equity bull market.

However, what has made the current market environment far more painful is there have been few places to seek refuge. Bonds have sold off alongside equities because a repricing higher of Fed rate expectations has been a key common factor, leaving commodities as one of the few areas to seek shelter. The good news is increased focus on the potential growth consequences of monetary policy tightening could lead the bond-equity correlation to become negative once again – meaning equity losses would be offset, at least to some degree, from bond market gains (and vice versa).

Inflation data, Fed pricing, China policy key from here. The key to this outlook in the near term is US CPI inflation data later this week, with the consensus expectation being for a slight fall to 8.1%. While this is still high, it could raise hopes that last month's number marked a peak.

As we noted in our *Global Market Outlook*, it is possible we are approaching the point where the Fed limits how much higher it guides policy expectations. This would also be consistent with the message from the Fed's financial stability report, which noted that a sharp increase in interest rates could pose risks to financial market trading conditions and a decline in economic activity. The Bank of England's warning on recession risks recently offers a similar message. However, this likely needs greater confidence that inflation pressures are at least not getting worse.

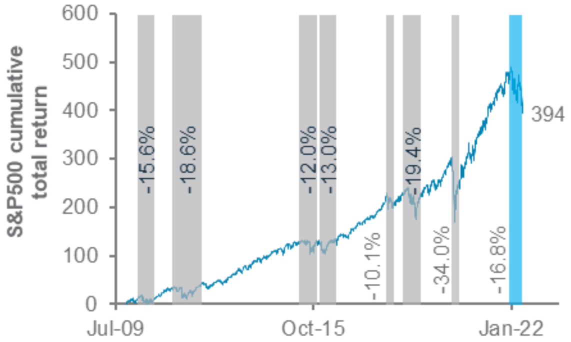
Energy, financials and China remain opportunities. Within equities, yesterday's pullback in the energy sector may have created an opportunity to add, given supply concerns are unlikely to abate soon given ongoing European discussions on curtailing Russian oil supply. Financials are also a potential hedge against higher bond yields. Longer-term, we continue to see Asian equities and Asia USD bonds as opportunities given still-beaten up valuations across both. The fact that yesterday's equity market weakness was accompanied by a fall in bond yields also gives us a little more confidence in taking advantage of higher yields across income asset classes, including EM USD government bonds.

Technicals: The S&P500 broke below technical support in late-February and May lows as well as the 100WMA. This brings 3950 and 3875 into focus as the next key areas of potential support. Yesterday's move in the US 10-year government bond yield is also consistent with our view that 3.26% likely marks a cap in the near term.

— **Manpreet Gill,** *Head FICC Investment Strategy*

10%+ equity market sell-offs are not uncommon; there were six in the last bull market, each presenting a buying opportunity

S&P500 marked with prior 10% pullbacks



Source: Bloomberg, Standard Chartered

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