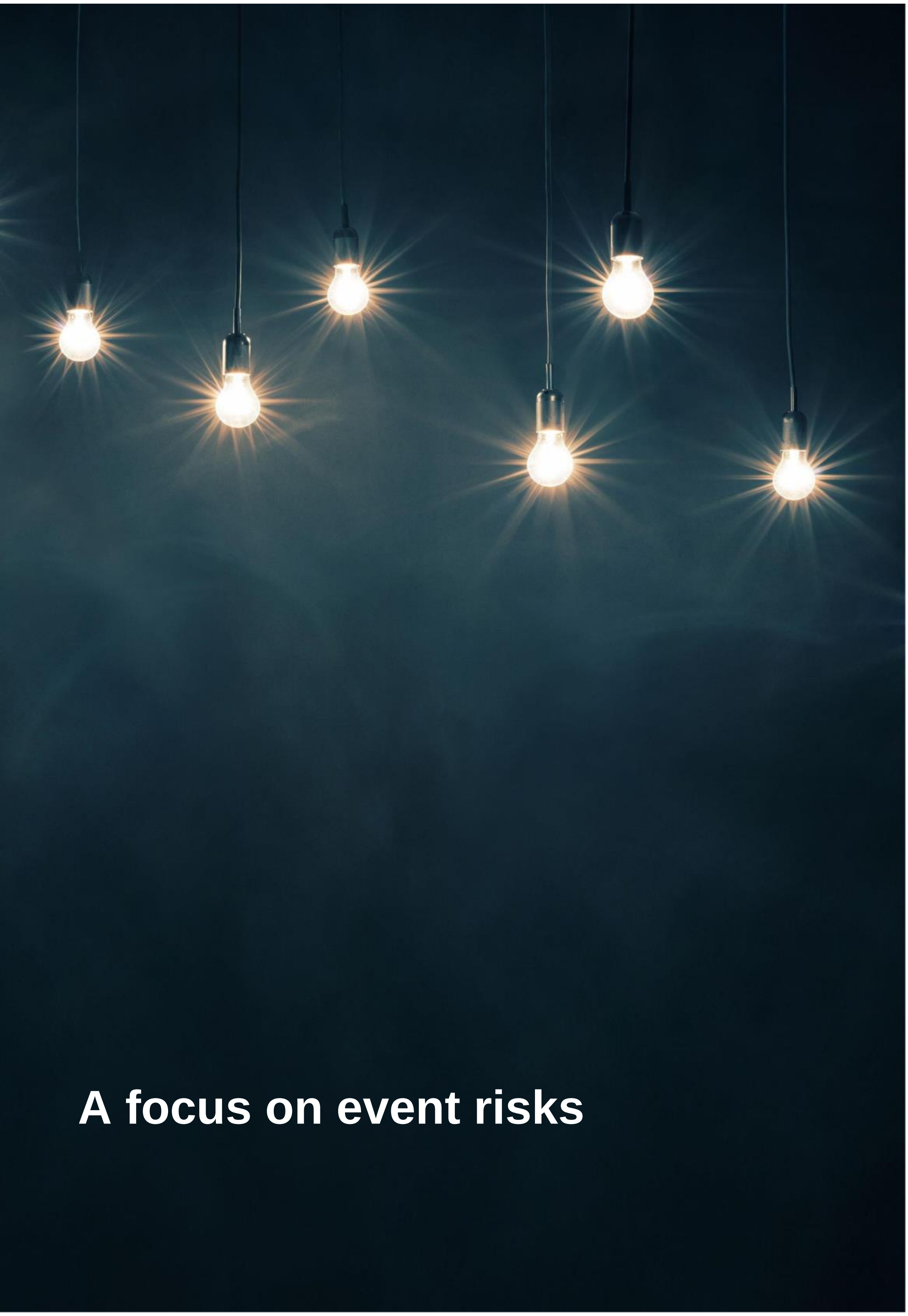
Macro Strategy | 11 October 2019

Weekly Market View



A focus on event risks

US-China trade talks, Brexit and US Q3 earnings next week are potential catalysts for global equities to break out of this year's range

Equities: The US Q3 earnings season starts next week. Expectations are weak, but any upside surprise could prove to be a positive catalyst

Bonds: Liquidity-boosting Fed balance sheet expansion may have little impact on bond yields, but could reduce upward pressure on the USD

FX: We see attractive risk/reward on the GBP ahead of a key week for Brexit

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Chart of the week: Can key events break equities out of their range?

MSCI AC World with key technical support and resistance

Source: Bloomberg, Standard Chartered

Editorial

A focus on event risks

Financial markets largely treaded water over the past week, as investors awaited the outcome of major political and economic events. The US and China were holding talks at the time of writing. Reports suggest the likelihood of achieving a significant trade deal is low, though we believe low expectations create considerable room for an upside surprise should an agreement that staves off a US tariff rise on October 15 be achieved. Meanwhile, next week contains crucial dates for the Brexit process – the European Council is set to meet on 17-18 October, following which the UK Parliament is set to hold a special session on 19 October. We continue to expect policymakers to avoid a no-deal Brexit.

Outside of these event risks, markets are also likely to focus on the US Q3 earnings season, which kicks off next week. Although the consensus is for a small contraction in earnings y/y, led by the energy sector, a continuation of the recent record of upside surprises would be a positive. Any guidance on corporate margins is likely to be key.

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Can the US and China reach any agreement on trade?

US and Chinese trade representatives are meeting this week, restarting stalled trade talks ahead of a planned rise in US tariffs on USD 250bn worth of Chinese imports on 15 October. Expectations from the talks appear low, especially after the US imposed sanctions on specific Chinese officials and technology firms ahead of the talks. Reports suggest the issue of forced technology transfer remained a key hurdle, though the possibility of a currency pact and Chinese purchase of US agricultural goods are positives.

We continue to believe a trade truce, or a 'mini-deal' of some sort, remains the most achievable outcome. President Donald Trump is likely to be incentivised to avoid a recession-inducing breakdown ahead of Presidential elections next year, while continued weakness in Chinese growth data (most recently, the unofficial PMI index and producer prices) is an incentive from a Chinese point of view. However, a positive outcome is far from certain. As we discuss on page 5, global equities have been relatively range-bound for a large part of this year, admittedly after a very strong start, and we continue to monitor trade discussions as one possible catalyst for either a positive, or negative, breakout.

Can earnings offer any guidance on the market outlook?

A second event likely to capture market attention next week is the start of the US Q3 earnings season. Expectations remain low, with consensus currently looking for -3.2% y/y earnings growth. However, a recent pattern of managing expectations lower ahead of earnings, followed by positive surprises, suggests the final outcome could be more positive. Any guidance on the 2020 outlook, especially related to corporate margins, is likely to be key. See page 4 for sector details.

Meanwhile, minutes of the September Fed meeting showed those favouring the September rate cut viewed it through a risk-management lens, but 'several' participants favoured leaving rates unchanged unless economic data weakened sufficiently. Recent data highlights the Fed's dilemma – although US labour market data disappointed relative to expectations, one-off factors, such as strikes at large corporations, could have been a factor. Soft consumer and producer prices illustrated that inflationary pressure remains weak. We continue to expect another Fed rate cut this year. However, whether manufacturing PMIs rebound from here is key to higher equity prices and bond yields, in our assessment.

Crunch time for Brexit and the GBP, or another extension?

The coming week is key for the Brexit process. The European Council meeting is scheduled for 17-18 October, and the UK Parliament will hold a special session thereafter on Saturday, 19 October – the first in 37 years. This session is likely to be key, as any decision on a potential Brexit agreement, or possible extension request, would likely be agreed to at this session. We believe the GBP offers an attractive risk/reward at current levels, given the only conviction expressed by the UK Parliament thus far has been the avoidance of a no-deal Brexit.

What we are watching

US-China trade talks; Brexit talks; US Q3 earnings, Fed comments.

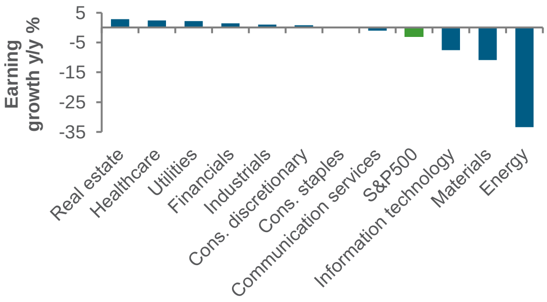
Any potential US-China currency pact could limit further gains in the USD

Trade-weighted US Dollar Index

Source: Bloomberg, Standard Chartered

Energy sector the biggest drag on US Q3 earnings expectations

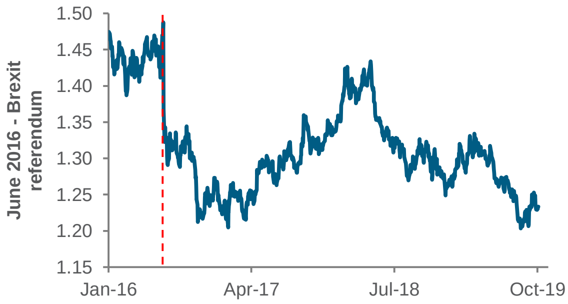
Q3 19 earnings expectations by sector



Source: I/B/E/S, Refinitiv, Standard Chartered

GBP is back close to post-Brexit vote lows; we see attractive risk/reward at these levels

GBP/USD



Source: Bloomberg, Standard Chartered

What does this mean for investors?

Equities

What is the outlook for the US Q3 earnings season? Market consensus is for S&P500 Q3 earnings to contract by -3.2% compared to the same period a year ago. This has echoes of Q2 earnings expectations, which were similarly negative heading into the reporting season, creating the potential for a positive 'surprise'. Companies prefer to under-promise and over-deliver, as research has shown that companies beating earnings expectations witness a 'pop' in their share price in the days following the release. US banks will be among the biggest sector to report in the week of 14 October, with analysts expecting the financial sector, within which banks are the largest industry group, to report +1.4% earnings growth. The energy sector is expected to be the main drag – the consensus is for a -33% decline in earnings, as oil prices in Q3 '19 were, on average, 20% below levels witnessed in Q3 '18.

We are comfortable with our preferred view on US equities and see financials as a less preferred sector and energy as a core holding.

How has consumption spending fared over the Chinese 'Golden Week' holiday? Overall, revenue from retail and dining during the period rose 8.5% y/y to CNY 1.52trn, according to data from China's Commerce Ministry, helped by higher sales of white goods and increased spending on domestic tourism and entertainment. This was one key source of support for both Hong Kong and China equity markets this week, despite rising expectations that Hong Kong's economy is likely to tip into a technical recession following the recent political unrest. We believe the trend for rising domestic consumption in China is sustainable on the back of supportive government measures and reduced overseas travelling amid a softer CNY. The consumer sector remains our preferred sector within China equities.

Bonds

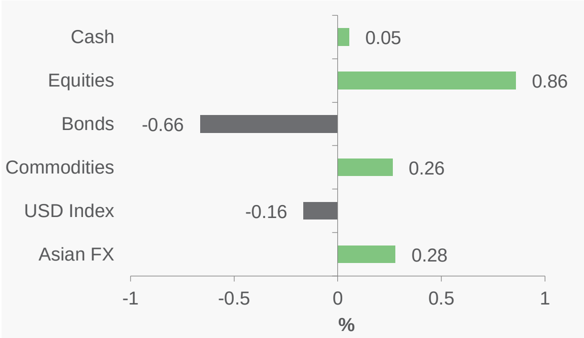
Is the Fed plan to expand its balance sheet significant for bonds? Fed Chair Jerome Powell said the Fed would start expanding its balance sheet 'soon', most likely by purchasing T-bills, in an effort to support short-term liquidity. While we await details, we do not view this as another quantitative easing (QE) programme and see little significant impact on Treasury yields, a bond asset class we continue to see as least preferred. However, where it could have a more significant impact is by improving global US Dollar liquidity which, in turn, could reduce upward pressure on the currency.

In Asia USD bonds, Investment Grade (IG) yield premiums surprisingly widened by more than those for High Yield (HY) bonds. Although US-China trade uncertainty may have been one driver, a surge in new bond issuance may also have been at play. We continue to view Asian USD bonds as a preferred holding.

FX

Is the EUR set to rise? Although recent Euro area economic data has remained weak and Brexit is an overhang, EUR/USD appears to be making a renewed attempt to push above resistance at 1.10, a move that could gain momentum if the USD peaking process gathers pace.

Benchmark (USD) performance w/w*



Source: MSCI, JP Morgan, DJ-UBS, Citigroup, Bloomberg, Standard Chartered (Indices used are JP Morgan Cash, MSCI AC World TR, Citi World Big, DJ-UBS Commodity, DXY and ADXY)

*Week of 3 October 2019 to 10 October 2019

Equity market technicals have turned mostly negative

Technical levels of key markets as of 10 October 2019

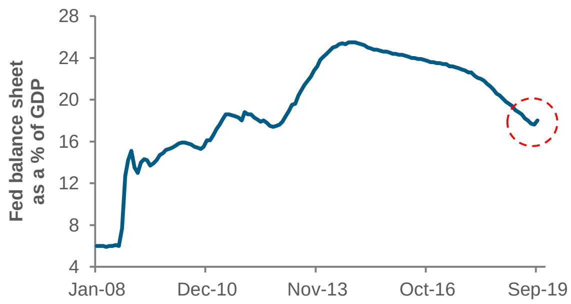
Index	Spot	1st support	1st resistance	Short-term trend
S&P	2,938	2,855	3,028	→
STOXX 50	3,494	3,395	3,545	↘
FTSE 100	7,186	6,970	7,305	↘
Nikkei 225	21,552	21,100	21,750	↘
Shanghai Comp	2,948	2,874	2,978	↘
Hang Seng	25,708	25,300	26,350	↓
MSCI Asia ex-Japan	614	601	625	↘
MSCI EM	996	972	1,010	↘
Brent (ICE)	59	54	63	↓
Gold	1,494	1,483	1,519	→
UST 10Y Yield	1.66	1.43	1.8	↘

Source: Trading Central, Standard Chartered

Note: Arrows represent short-term trend opinions

Fed balance sheet is expanding again; we expect the modest expansion to support short-term liquidity

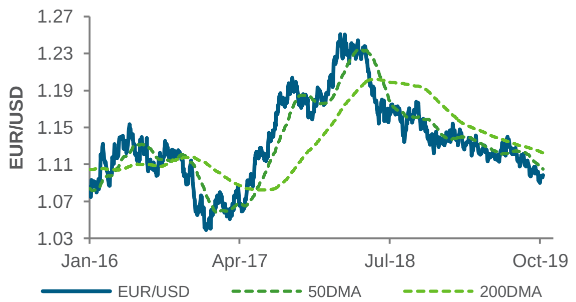
US Fed balance sheet as a percentage of GDP



Source: Bloomberg, Standard Chartered

EUR would gain from a peaking USD

EUR/USD



Source: Bloomberg, Standard Chartered

Top client question

Global equities seem caught in a range. What are the key technical levels that could signal a breakout is occuring?

Since early 2018, global equities (the MSCI All Country World index) have repeatedly tested stiff resistance at a horizontal trendline at 533, but has failed to break higher.

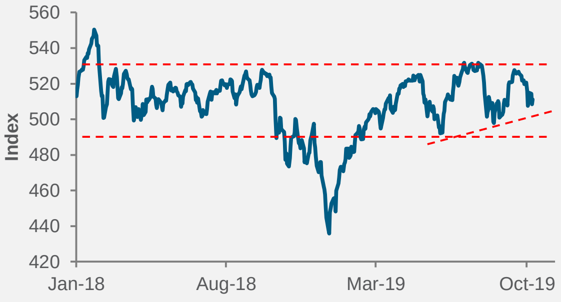
The index is now approaching a strong support area: a slightly upward-sloping trendline (now at about 500; 2.7% from Thursday's close) and a horizontal trendline at about 492 (4.3% from Thursday's close). We view this support as quite strong, suggesting a rebound is likely if the fundamental backdrop for equities remains supportive going into the Q3 earnings season.

However, any break below the support area could trigger a 'head-and-shoulder' pattern – the left shoulder at the May high, the head at the July high and the right shoulder at the September high. A head-and-shoulders pattern is typically a bearish pattern, implying a break of support could trigger a drop towards major support at the December low of 435 (15% from Thursday's close).

As we discussed on page 3 and 4, event risks may define whether markets will rebound or break lower. A positive outcome would likely involve the US and China moving closer or achieving a truce or a 'mini-deal' together with continued upside surprises in the US Q3 earnings season. However, a collapse in the trade talks and/or significant disappointments in the upcoming US earnings season would likely raise the risk of a downside break.

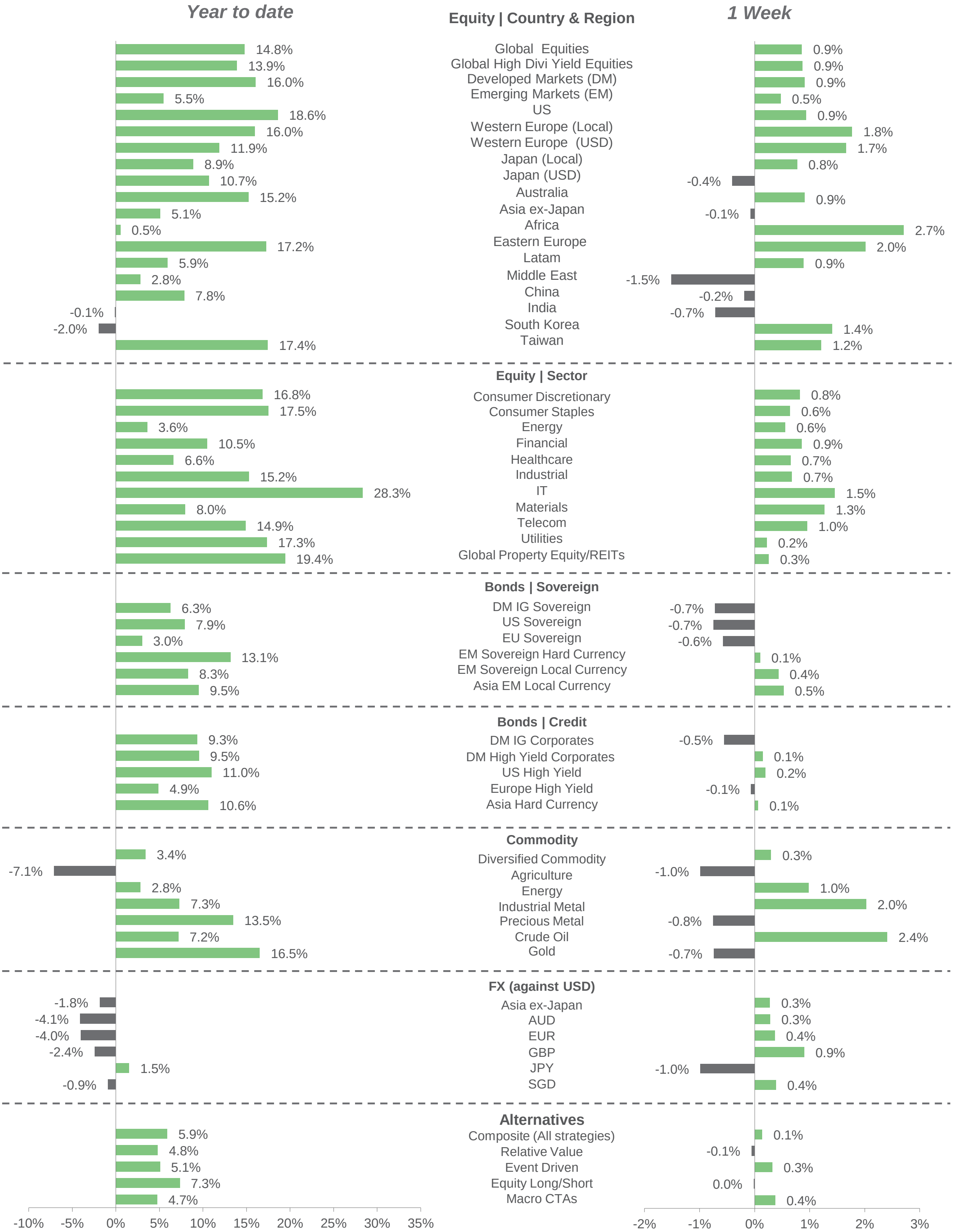
Global equities have remained rangebound recently; we are mindful of the risk from a potential head-and-shoulders pattern

MSCI AC World and technicals



Source: Bloomberg, Standard Chartered

Market performance summary*



Sources: MSCI, JP Morgan, Barclays Capital, Citigroup, Dow Jones, HFRX, FTSE, Bloomberg, Standard Chartered

*Performance in USD terms unless otherwise stated, YTD period from 31 December 2018 to 10 October 2019, 1 week period: 3 October 2019 to 10 October 2019

Economic and market calendar

	Event	Next Week	Date	Period	Expected	Prior
MON	CH	Exports y/y	14-Oct-19	Sep	-2.9%	-1.0%
	CH	Imports y/y	14-Oct-19	Sep	-6.0%	-5.6%
TUE	CH	CPI y/y	15-Oct-19	Sep	2.9%	2.8%
	CH	PPI y/y	15-Oct-19	Sep	-1.2%	-0.8%
WED	US	Retail Sales Ex Auto and Gas	16-Oct-19	Sep	0.3%	0.1%
THUR	US	Building Permits	17-Oct-19	Sep	1340k	1425k
	US	Housing Starts	17-Oct-19	Sep	1320k	1364k
	US	Industrial Production m/m	17-Oct-19	Sep	-0.1%	0.6%
FRI/SAT	JN	Natl CPI Ex Fresh Food, Energy y/y	18-Oct-19	Sep	–	0.6%
	CH	Industrial Production y/y	18-Oct-19	Sep	4.9%	4.4%
	CH	Retail Sales y/y	18-Oct-19	Sep	7.8%	7.5%
	CH	GDP y/y	18-Oct-19	3Q	6.1%	6.2%
	EC	ECB Current Account SA	18-Oct-19	Aug	–	20.5B
	US	Leading Index	18-Oct-19	Sep	0.1%	0.0%

	Event	This Week	Date	Period	Actual	Prior
MON	GE	Factory Orders WDA y/y	07-Oct-19	Aug	-6.7	-5.0%
	EC	Sentix Investor Confidence	07-Oct-19	Oct	-16.8	-11.1
TUE	CH	Caixin China PMI Services	08-Oct-19	Sep	51.3	52.1
	CH	Caixin China PMI Composite	08-Oct-19	Sep	51.9	51.6
	GE	Industrial Production WDA y/y	08-Oct-19	Aug	-4.0%	-3.9%
	US	NFIB Small Business Optimism	08-Oct-19	Sep	101.8	103.1
	US	PPI Ex Food and Energy y/y	08-Oct-19	Sep	2.0%	2.3%
WED						
THUR	JN	Core Machine Orders y/y	10-Oct-19	Aug	-14.5%	0.3%
	GE	Exports SA m/m	10-Oct-19	Aug	-1.8%	0.8%
	US	CPI Ex Food and Energy y/y	10-Oct-19	Sep	2.4%	2.4%
FRI/SAT	IN	Industrial Production y/y	11-Oct-19	Aug	–	4.3%
	US	U. of Mich. Sentiment	11-Oct-19	Oct P	--	93.2

Source: Bloomberg, Standard Chartered; key indicators highlighted in blue
Previous data are for the preceding period unless otherwise indicated
Data are % change on previous period unless otherwise indicated
P - preliminary data, F - final data, sa - seasonally adjusted
y/y – year-on-year, m/m - month-on-month

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