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WM Chief Investment Office
11 February 2021

Weekly Market View

From the Rat to the Ox

After a disruptive year of the Rat, the year of the Ox brings hope. The Ox also symbolises hard work. We acknowledge that this year will be a hard grind for economies to recover from a recession and for businesses to return to earnings growth to justify elevated valuations. We remain hopeful that both will surprise positively, benefitting risk assets

Equities: The re-emergence of the reflation theme is positive for our preferred US cyclical sectors, such as Financials, Industrials and Materials

Bonds: While we remain constructive on US High Yield bonds, we believe Asian High Yield bonds currently offer better value

FX: We would continue to average into the EUR on expectation of further USD weakness in 2021

+

What will be the focus of China and Hong Kong equities after the holidays?

Is the USD bounce already over?

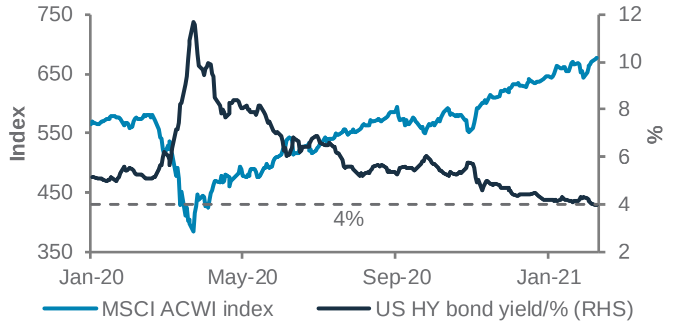
Should we be worried about China's property sector High Yield bonds?

Important disclosures can be found in the Disclosures Appendix.

Charts of the week: Will fundamentals justify valuations?

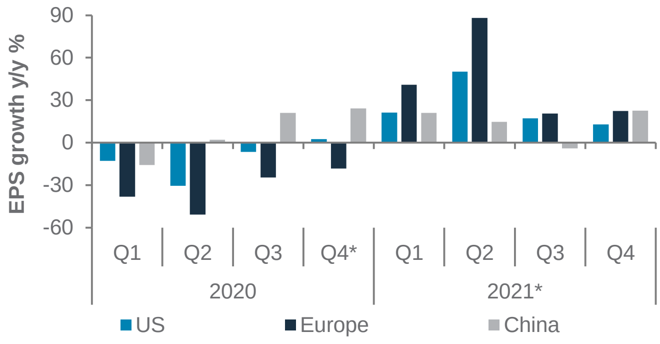
We expect a solid revival in corporate earnings this year, helping justify elevated valuations

MSCI All Country World index and the yield on US High Yield (HY) bonds



Source: Bloomberg, Standard Chartered

MSCI US, Europe and China earnings growth; *Q4 20 and Q1-Q4 21 are consensus estimates



Source: MSCI, FactSet, Refinitiv, Standard Chartered

Editorial

From the Rat to the Ox

We are no astrologers at Standard Chartered, but we could not ignore the significance of the shift in the Chinese zodiac for our investment outlook. Last year was the year of the Rat. The new year is the year of the Ox. While the Rat is a symbol of wealth and abundance, it is also predisposed to disruptions. Meanwhile, the Ox is a symbol of hard work and positivity. As hundreds of millions across Asia usher in the Lunar New Year, perhaps few symbolisms better reflect the unfolding economic and financial landscape.

After a historically disruptive year, we see the next 12 months as the year of hope. For investors, 2021 is the year when the hard work of policymakers and mass vaccinations help lift the global economy out of one of the deepest recessions in history, helping justify valuations that investors have been paying up for over the past year.

Our admittedly brave call to dip back into risk assets during the depths of the COVID-19 crisis in H1 20 has been well rewarded. Global equities have recovered from Q1 20's steep losses, breaking to record highs, and US HY bond yields have dipped below 4% for the first time.

The view we bought into then was that the troika of aggressive policymakers, resourceful scientists and imaginative businesses would pull us out of the crisis sooner than many expected. The setbacks in controlling the pandemic (which has sadly cost millions of lives) notwithstanding, we have been positively surprised by the turn of events. Wherever we look, economies, led by China, have bounced back faster than what economists had forecast a year ago. The upgrades to 2020-21 global growth estimates and corporate earnings forecasts reflect the positive surprises.

One challenge we often get is whether this means all the good news is already priced in. For sure, there are ample sources of potential disappointments. A mutation of the virus or other factors could cause the vaccination drive to falter. Many technical indicators appear stretched, leaving risk assets vulnerable to a short-term pullback.

Nevertheless, our considered view is that these are precisely the uncertainties that are currently holding back risk assets. We continue to place our calculated faith in policymakers (taking the view they will not pull the plug too early on accommodative policies), scientists (in using the past year's learnings to get ahead of the virus) and innovative businesses and consumers (in overcoming challenges). These factors, combined with contained energy costs and a weakening USD, should keep global financial conditions supportive for risky assets.

In this environment, holding a diversified allocation across stocks (with a tilt towards Value equities), bonds, gold and other alternative assets, and taking advantage of market dips, remain critical. Nevertheless, we see the redoubtable Ox climbing the wall of uncertainty to deliver investors in equities and riskier bonds a respectable return that beats cash, high quality bonds and, importantly, inflation. We also believe an allocation into longer-term structural themes tied to technological breakthroughs, such as 5G, Internet of Things, e-vehicles and e-medicine, and the global push towards an environmentally sustainable world, remain attractive.

The weekly macro balance sheet

Our weekly net assessment: On balance, we see the past week's data and policy as positive for risk assets

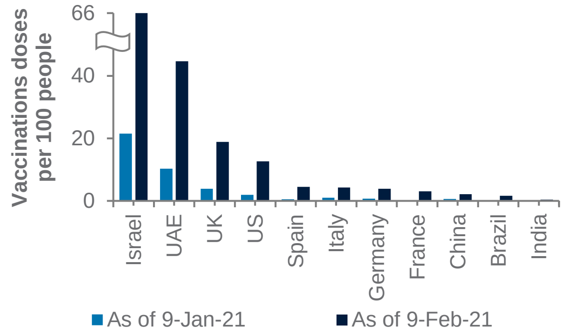
(+) factor: Falling COVID-19 cases, US stimulus progress

(-) factor: Weak US and Euro area data, tighter China liquidity

	Positive for risk assets	Negative for risk assets
COVID-19	• New cases continued to decline worldwide • The US plans to boost weekly vaccine shipments to states to 11m	• The pace of vaccinations in the EU remain 'too slow', leading some German lawmakers to propose buying vaccines at a national level
	Our assessment: Positive – declining new cases worldwide, partly offset by slow EU vaccination pace	
Macro data	• US's Yellen said the economy could return to full employment in 2022 if Congress approved the USD 1.9trn stimulus • US job openings rose unexpectedly • German m/m exports rose unexpectedly and consumer inflation accelerated • China's producer prices accelerated, allaying concerns about deflation	• US job creation fell below expectations and previous job numbers were revised lower • Largest annual US trade deficit since 2008 • China's M2 money supply y/y growth rose less than expected • Euro area Sentix Investor Confidence declined unexpectedly • German industrial output rose less than expected
	Our assessment: Negative – weak US job creation, China's tighter money supply, Euro area confidence	
Policy developments	• US President Biden pushed for the USD 1.9trn stimulus, saying latest job report showed the risk of doing too little • Fed's Powell, ECB's Lagarde and BoE's Bailey pledged to keep policy easy for an extended period	
	Our assessment: Positive – US stimulus progress	
Other developments		• US, China warships face-off in east Asia
	Our assessment: Negative – US-China tensions belie expectations of a rapprochement	

Vaccinations are progressing worldwide, but Europe has a lot of catching up to do

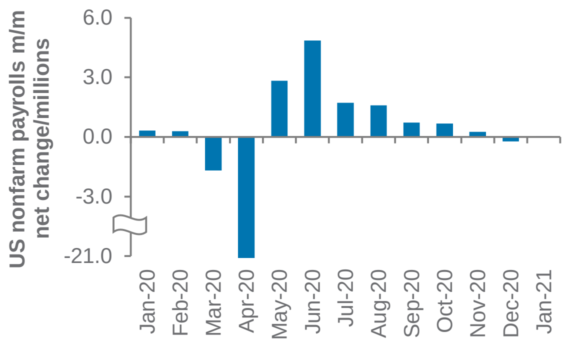
Number of COVID-19 vaccine doses administered per 100 people vs a month ago



Source: Our World in Data, Standard Chartered

Biden's proposed USD 1.9trn fiscal spending package is likely to revive the US job market

US monthly net non-farm jobs created



Source: Bloomberg, Standard Chartered

China's slowing money supply reflects policymakers' focus on financial stability

China's M2 money supply growth

Source: Bloomberg, Standard Chartered

Top client questions

Which US equity sectors are likely to benefit from the re-emergence of the reflation theme?

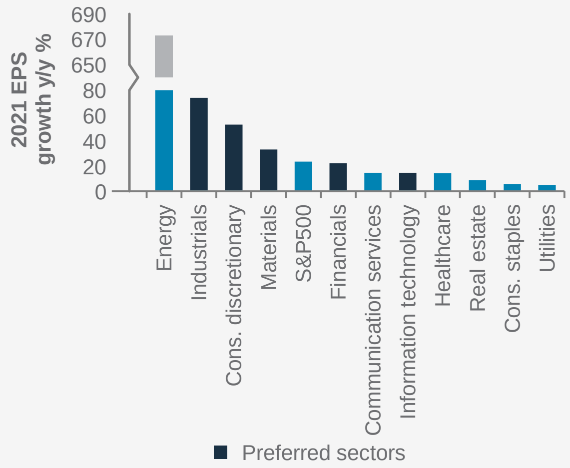
The reflation theme appears to be gaining momentum, with gradually rising market inflation expectations being a key signal. In our assessment, this is consistent with the strong monetary stimulus driving a cyclical recovery.

As this recovery extends with policy support and a vaccine rollout, sectors that have been hit hard in the cyclical downturn can be expected to bounce back strongly in the cyclical recovery. This is one key driver of our preferred view on the industrials, consumer discretionary and materials sectors in the US. While these sectors posted some of the deepest earnings declines in 2020, they are expected to show sharp earnings rebound in 2021. Although the energy sector is expected to have the strongest earnings rebound, we believe this sector will continue to face headwinds as policymakers support a shift towards green energy.

Consistent with the reflation theme, we would also focus on the increasingly steep yield curve (ie. gap between long and short maturity bond yields). This is usually a positive driver for the financial sector as banks earn higher net interest margins on future loans. The US financials sector is preferred.

Our preferred cyclical sectors are likely to lead the US earnings recovery in 2021

Consensus estimates for 2021 earnings growth for various US equity sectors



Source: Bloomberg, Standard Chartered

What is likely to be in focus for China/Hong Kong equities after the holidays?

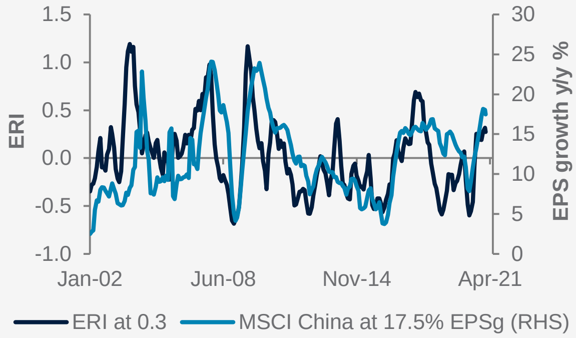
The China and Hong Kong earnings season kicks off in March, making earnings a likely focus after the Lunar New Year holidays. Earnings preannouncements have been net positive to date, suggesting a solid V-shaped recovery. The healthcare and technology sectors have preannounced the biggest earnings recovery so far. The market is expecting 12-month forward EPS growth of 18% for China equities.

We believe the strong earnings preannouncements are constructive for China equities (both onshore and offshore), cementing their status as a preferred market in Asia ex-Japan. We expect a further rerating of the market as earnings estimates are upgraded in the coming quarters amid an economic recovery and still-accommodative government policies, despite the recent tightening measures.

Compared to China offshore, we believe China onshore equities offer more exposure to the cyclical recovery and are usually less impacted by geopolitical tensions and internet sector regulatory risks. Healthcare and technology sectors remain preferred in China amid a robust earnings outlook. Consumer discretionary is also preferred on expectations of strong domestic consumption growth and product upgrades.

China's corporate earnings estimates have been revised higher in recent weeks

MSCI China 12-month forward earnings estimates and earnings revisions index*



Source: MSCI, FactSet, Standard Chartered; *A comparative measure of upward vs downward revisions in earnings estimates

Top client questions (cont'd)

Do recent defaults raise risks for China HY property sector bonds?

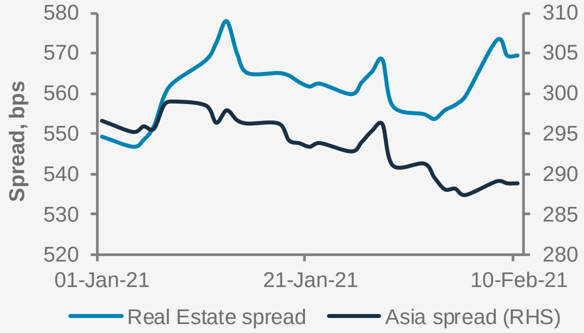
An individual missed loan repayment by a Chinese real estate company has negatively impacted China High Yield (HY) property sector bonds. Despite a revival in default concerns, we believe regulatory policies are unlikely to ease following comments in the PBoC's Q4 20 monetary policy report that stated the financing policy for the property sector will remain focused on continuity, consistency and stability.

In our view, refinancing worries are likely to be an ongoing concern for Chinese HY property sector bonds. A greater focus on the quality of fundamentals means the market could also increasingly differentiate on the basis of debt sustainability.

Having said that, the recent volatility was largely triggered by (and thus far limited to) an individual event. Therefore, we believe the impact to the China HY property sector is likely to be temporary, especially for the HY sub-category. This gives us comfort in our preference for Asia HY bonds, of which the China HY property sector is a significant component. We would be comfortable taking advantage of this pullback to add exposure where appropriate.

We would take advantage of the pullback in Asian HY bonds as China's property sector default risks remain contained

Yield premium (spread) on Asia USD bonds and Asia real estate sector bonds vs Treasuries



Source: Bloomberg, Standard Chartered

Are record low US HY bond yields a concern?

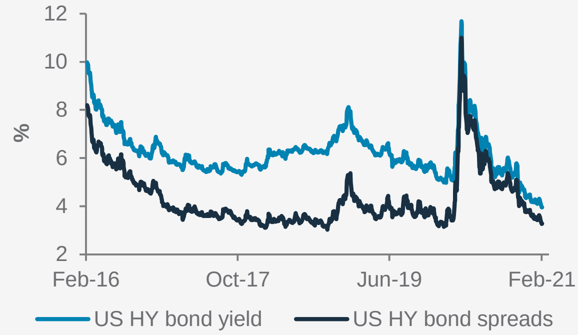
Yields on US HY bonds fell below 4% for the first time ever amid lower US Treasury yields and a sharp decline in yield premiums. The yield premium (a measure of valuation), at 3.27%, is approaching 2018's 11-year low of 3.16%.

Fundamentally, the yield decline does not come as a surprise as the ongoing economic recovery, a strong US earnings season and ample liquidity have helped fuel the search for yield globally. Despite elevated corporate leverage in the sector, low borrowing costs have meant that the aggregate debt servicing ability of HY corporates has been resilient. While we are monitoring some signs of frothiness in the CCC-rated segment, the expected decline in default rates could continue to support market optimism. Thus, while we acknowledge that the risk-reward offered by US or Developed Market (DM) HY bonds has reduced, we still view them favourably compared to Investment Grade (IG) corporate and government bonds, which are trading at even lower yields.

For investors seeking to add exposure today, Asian HY bonds present an attractive alternative as their yield pickup (and absolute yield), relative to their US counterparts, is substantially above the historical average.

US HY bonds compare favourably with IG peers, despite the sharp decline in yields

Yields offered by US HY bonds and their yield premium over Treasuries



Source: Bloomberg, Standard Chartered

Top client questions (cont'd)

Is the USD bounce already over?

The short-term USD rally that we expected (see *Weekly Market View* dated 15 January) materialised but has been modest. Our strategy was to "average in" to the EUR, the AUD and the GBP versus the USD at various support levels in anticipation of medium-term USD weakness. Since publication, EUR/USD traded to a 1.1950 low, triggering two entry levels, AUD/USD to a low near 0.7560, triggering one level and GBP/USD only declined to 1.3565.

This price action supports our 12-month bearish USD view. Investors appear to be "looking through" possible near-term US economic outperformance from stimulus and faster vaccinations and focusing on likely USD risks, including inflationary pressure and large budget and trade deficits.

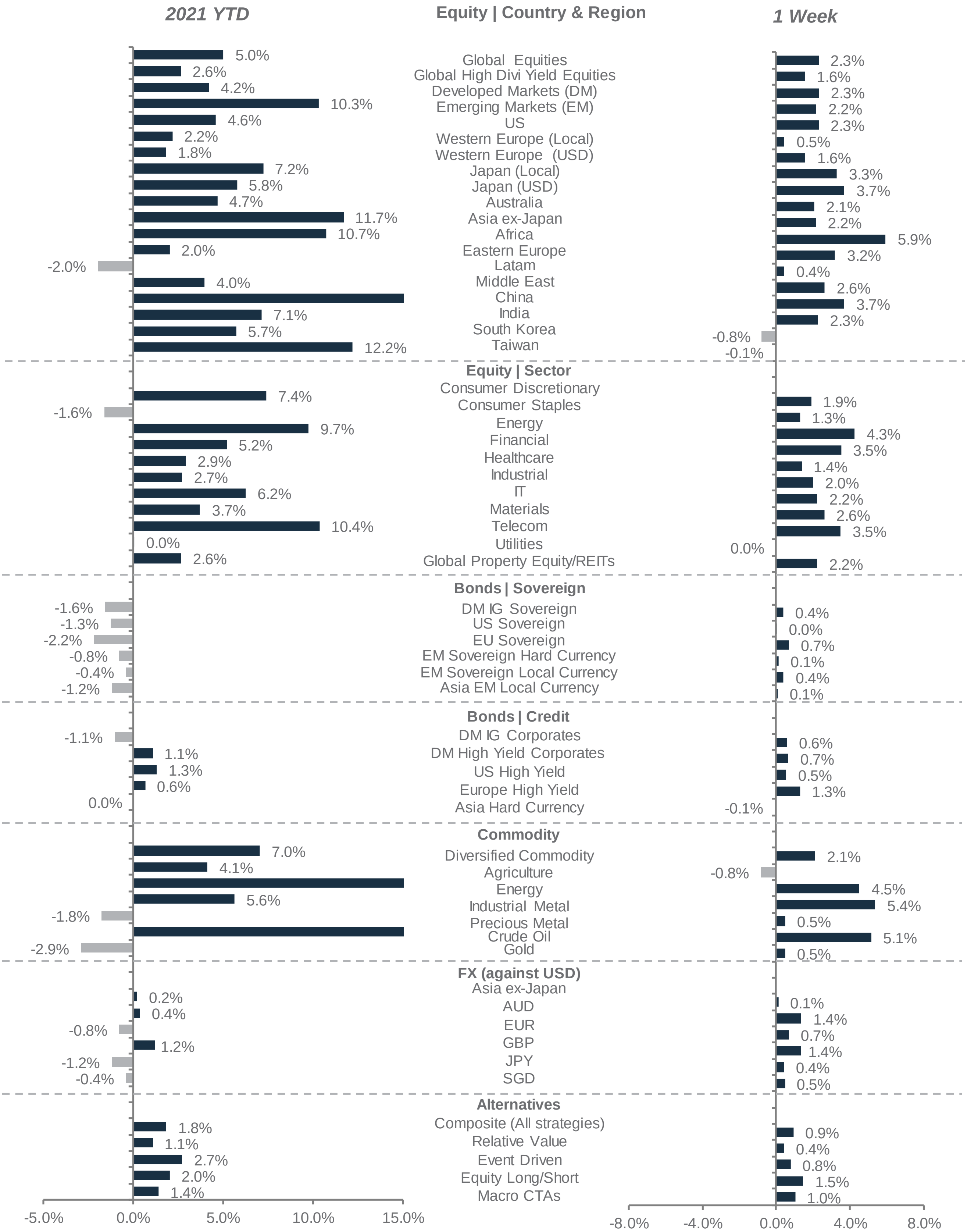
We believe our January strategy remains optimal, but the levels require updating. If EUR/USD holds below the technical resistance at 1.2200, support at 1.1950 would offer an initial entry point. While the AUD/USD January high at 0.7820 remains unbroken, there may still be an opportunity to enter around 0.7560. GBP/USD has rallied strongly with relatively minor corrections. We look for another dip towards 1.3570 as an initial entry level.

We would continue to average into the EUR on expectation of USD weakness in 2021

EUR/USD

Source: Refinitiv, 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, 2021 YTD performance from 31 December 2020 to 10 February 2021; 1-week period: 3 February 2021 to 10 February 2021

Our asset class views at a glance

Asset Class			
Equities	▲	**Alternatives**	◆
Asia ex-Japan	▲	Equity hedge	▲
US	▲	Event-driven	◆
Euro Area	▲	Relative value	◆
Japan	▲	Global macro	▼
Other EM	◆		
UK	◆	**Cash**	▼
		USD	▼
Bonds (Credit)	▲	EUR	▲
Asia USD	▲	GBP	▲
Govt EM USD	▲	AUD	▲
Corp DM HY	▲	CNY	▲
Corp DM IG	▼	JPY	◆
Bonds (Govt)	▼		
Govt DM IG	▼		
Govt EM Local	▲		

Source: Standard Chartered Global Investment Committee

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

Economic and market calendar

	Event	Next Week	Period	Prior
MON	JN	GDP Annualized SA q/q	4Q P	22.9%
TUE	EC	ZEW Survey Expectations	Feb	58.3
WED	JN	Exports y/y	Jan	2.0%
WED	US	Retail Sales Ex Auto and Gas	Jan	-2.1%
WED	US	Capacity Utilization	Jan	74.5%
THUR	US	Housing Starts	Jan	1669k
FRI/SAT	JN	Jibun Bank Japan PMI Composite	Feb P	47.1
FRI/SAT	EC	Markit Eurozone Composite PMI	Feb P	47.8
FRI/SAT	UK	Markit/CIPS UK Composite PMI	Feb P	41.2
FRI/SAT	US	Markit US Composite PMI	Feb P	58.7

Source: Bloomberg, Standard Chartered

Prior 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

S&P500 has resistance 0.4% above current level

Technical indicators for key markets as on 10 Feb 2021

Index	Spot	1st support	1st resistance
S&P500	3,910	3,883	3,926
STOXX 50	3,648	3,638	3,662
FTSE 100	6,524	6,499	6,541
Nikkei 225	29,563	28,749	29,970
Shanghai Comp	3,655	3,549	3,708
Hang Seng	30,039	29,422	30,347
MSCI Asia ex-Japan	941	925	948
MSCI EM	1,423	1,399	1,435
Brent (ICE)	61.5	59.7	62.3
Gold	1,843	1,810	1,860
UST 10Y Yield	1.12	1.11	1.15

Source: Bloomberg, Standard Chartered

Elevated risk of short-term reversal in some markets

Our proprietary market diversity indicators as of 09 Feb

Level 1	Diversity	1-month trend	Fractal dimension
Global Bonds	◐	↑	1.49
Global Equities	◐	→	1.26
Gold	◐	↓	1.70
Equity			
MSCI US	◐	→	1.30
MSCI Europe	◐	→	1.37
MSCI AC AXJ	○	→	1.24
Fixed Income			
DM Corp Bond	◐	↑	1.53
DM High Yield	○	→	1.25
EM USD	◐	↑	1.46
EM Local	◐	↑	1.39
Asia USD	◐	↑	1.50
Currencies			
EUR/USD	◐	↑	1.44

Source: Bloomberg, Standard Chartered; **Fractal dimensions below 1.25 indicate extremely low market diversity/high risk of a reversal**

Legend: ● High | ◐ Low to mid | ○ Critically low

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