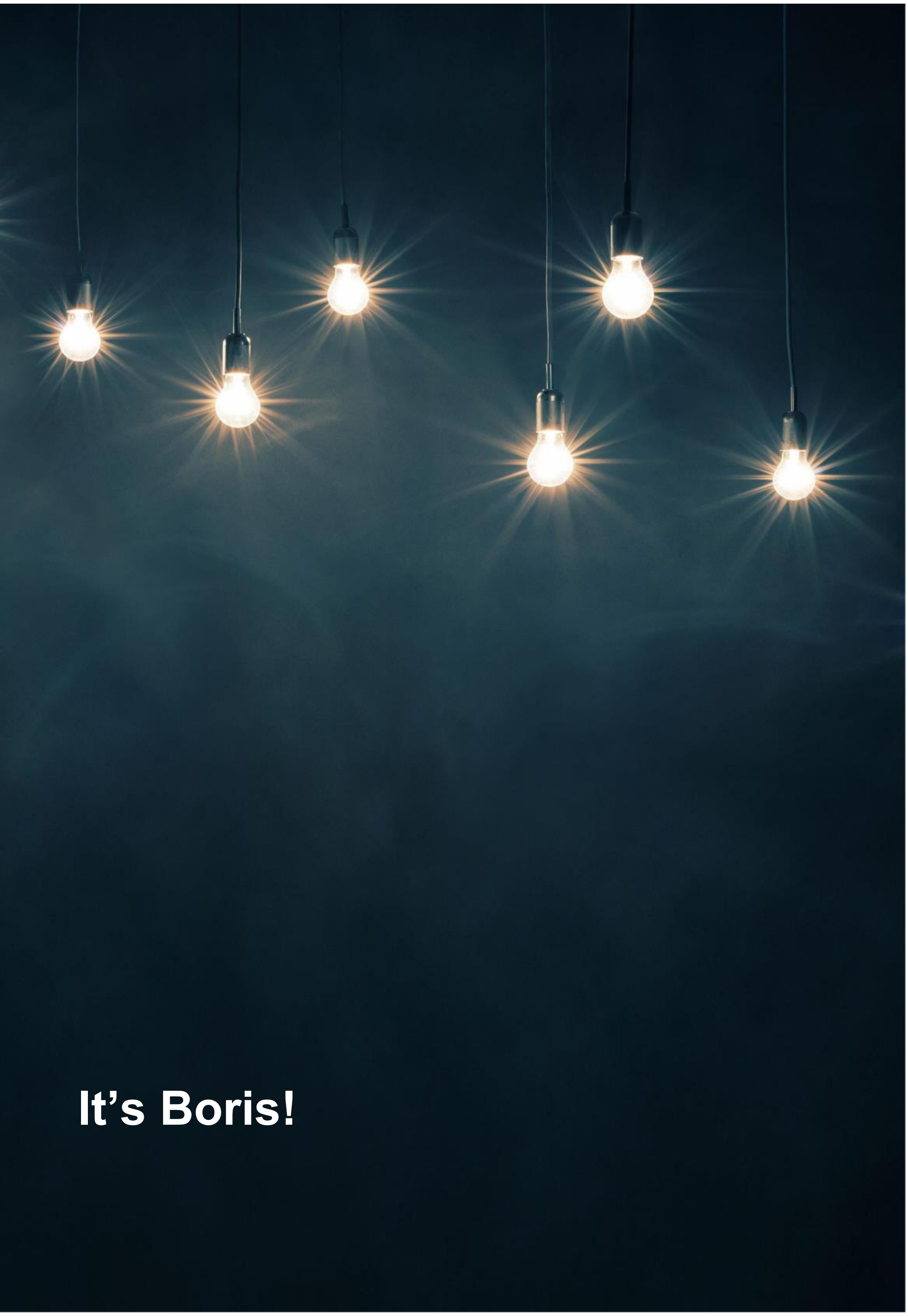
Macro Strategy | 13 December 2019

Weekly Market View



It’s Boris!

The Conservative party’s decisive win in the UK and a likely partial US-China trade deal support our bullish view on risk assets

Equities: A trade deal would be particularly positive for US (especially the technology sector) and Euro area stocks

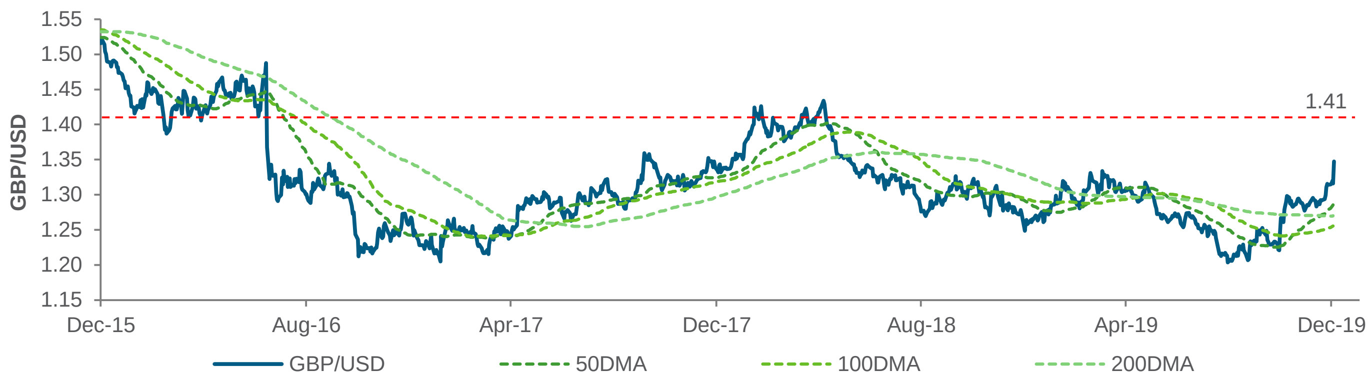
Bonds: A benign Fed and partial US-China trade deal would be a tailwind for Emerging Market bonds

FX: GBP is likely to get a boost from the UK election; next target is at 1.41

Contents

Chart of the week: GBP/USD's next major target is 1.41

GBP/USD and the next major technical resistance



Source: Bloomberg, Standard Chartered

Editorial

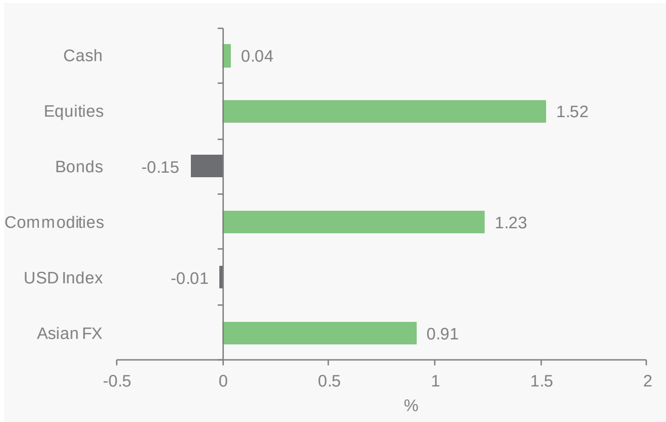
It's Boris! And a US-China trade deal too

The decisive victory by PM Boris Johnson's Conservative Party in the UK elections and US President Trump's approval of a partial trade deal with China are major positives for the global risk assets rally, in our view. Johnson's majority means he should be able to swiftly steer the Brexit deal he agreed with the EU through parliament. While the focus turns to agreeing on a trade deal with the EU by the 31 December 2020 deadline, the vote clears the way for an orderly Brexit. This is bullish for GBP and European assets (see page 5).

The so-called "phase-one" trade deal approved by Trump, if also agreed by China, is likely to avert a new round of tariffs that are due to go into effect on 15 December. The key to watch whether the US rolls back existing tariffs, a condition that China has insisted on before. A partial trade deal is likely to revive global business confidence and support our bullish 6-month view on equities, especially in the US (particularly the technology sector) and Euro area, and Emerging Market (EM) bonds. Having said that, we would not downplay the risk of a short-term pullback, given stretched market positioning.

Global equities hit a new record-high as the US and China moved towards a trade deal; reduced risk of a hard Brexit after the UK elections is likely to remove a key risk facing Euro area assets

Benchmark market 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 05 December 2019 to 12 December 2019

Trade deal hopes, Fed keep the mood-music upbeat

President Trump's sign-off on a partial trade deal with China, which if also approved by China, would remove a key uncertainty hanging over risk assets, in our assessment. Reports suggest the proposed deal includes China agreeing to buy more US farm products. It is not clear whether the US has agreed to roll-back existing tariffs. Nevertheless, a partial agreement could avert the introduction of a new round of tariffs on critical consumer goods imports from 15 December. A partial deal would also signal a de-escalation of trade tensions which have undermined global business confidence and risk assets since 2018.

The Fed's latest policy statement also appears positive for risk assets in the medium term, in our assessment. The US central bank signalled rates are likely to be on hold (and moderately below inflation) through 2020 and omitted a key concern around "uncertainties about (the) outlook". We believe this highlights its increased confidence that the economy is stabilising after this year's slowdown. Continued strength in the job market (with stronger-than-expected job creation in November) and solid consumption remain the drivers of the economy, although investments and exports remain weak amid global trade uncertainty.

Underlying inflation also remains subdued, as confirmed by data this week, with no signs of previous China import tariffs filtering through to US goods inflation. This benign economic backdrop and the expectation of an accommodative monetary policy through 2020 support our positive stance on global equities and EM bonds.

Watching US politics

US politics remains a risk to this constructive outlook, especially with the House of Representatives likely to vote next week to impeach President Trump. While we see low chances of the Senate passing a similar vote, given Republican majority (an impeachment is required by both Houses to remove a sitting President), increased political pressure could lead President Trump to turn more hawkish on foreign policy.

China data raises pressure on policymakers to ease

China's latest data on credit growth, factory gate inflation and exports support our view that policymakers will likely pick up the pace of fiscal and monetary stimulus in the coming months to meet growth targets for 2020. Aggregate credit growth (y/y) fell to a seven-month low of 10.8% in November, money supply growth (a measure of economic activity) remained subdued, producer prices continued to contract for the fifth straight month and exports contracted for the fourth month in a row.

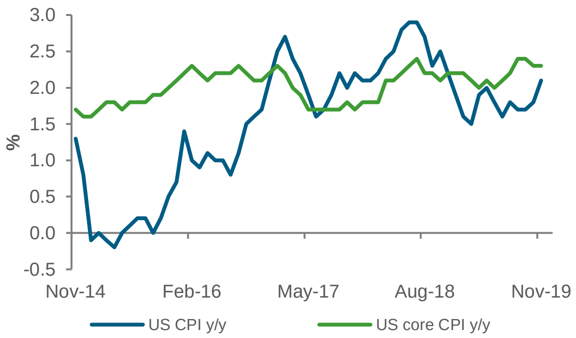
We have started to see relaxation in property market regulations in some cities. The government has also accelerated bond issuance plans for local governments to fund infrastructure investments early on in 2020. We expect more such policy measures, including PBoC rate cuts and lower bank reserve requirements, in the coming months. Although confirmation of a US-China trade deal would be a key driving factor, we believe compelling valuations of China offshore market relative to Asia ex-Japan support the positive case for China equities.

EUR gets a lift from ECB and UK elections

EUR/USD initially broke above 1.1175 resistance after ECB President Lagarde highlighted nascent signs of a mild inflation uptick in the Euro area. The UK election results added further support for the EUR as Brexit uncertainty fades. We remain bullish on EUR/USD on a 6-12 month horizon as we expect regional growth in the Euro area to pick up. The next target is 1.1250, followed by 1.1400.

US underlying (core) inflation remains close to the Fed's 2% target, despite the recent pickup in energy prices

US CPI and core CPI



Source: Bloomberg, Standard Chartered

China's monetary indicators continue to signal subdued economic activity, raising the prospect of more stimulus measures

China's M2 money supply growth

Source: Bloomberg, Standard Chartered

Euro area survey indicators signal further recovery in economic growth expectations and investor confidence amid signs of stabilisation in global trade tensions

Sentix Investor Confidence index and ZEW Survey of economic growth expectations

Source: Bloomberg, Standard Chartered

What does this mean for investors?

Equities

What are the implications of a possible US-China trade deal and the Fed staying on hold in 2020? A US-China partial trade deal would defuse a major risk factor facing global equities. Although details are sketchy, a roll-back of existing tariffs is likely to allay trade tensions that have undermined global business confidence. This is likely positive for trade-dependent markets such as Europe and Asia and sectors such as US technology.

US Fed Chair Powell's guidance this week that interest rates will likely remain on hold until inflation rises was welcomed by the equity market, with the S&P500 rising on the day of the announcement. Lower-for-longer interest rates are good for market valuations because they imply the current attractiveness of equities relative to bonds is unlikely to reverse due to rising bond yields. In the US, we prefer financials and technology sectors – the latter is the top-performing sector YTD.

As we head into 2020, investors are reviewing the 'Dogs of the Dow' theory that proposes that the next year's best performers will be this year's worst performers. Energy is the worst performer in 2019 which, based on the theory, will be the best performer in 2020. While the sector has risen in recent weeks as oil prices rose, we view the sector as a core holding as fundamental drivers, including the outlook for global growth, is positive, but not so much as to expect substantially increased energy demand in 2020. We also note that this theory is not foolproof; energy was the worst performing US sector in 2018 too.

Bonds

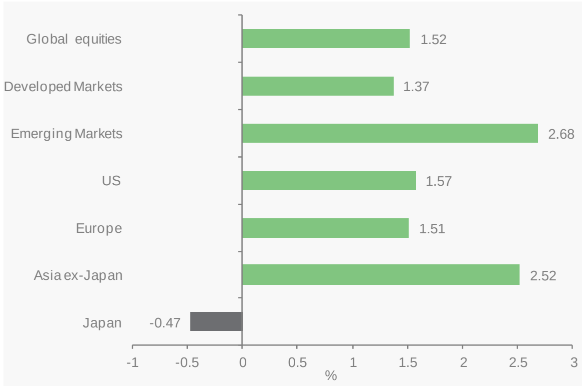
What is the implication of the latest Fed policy on your Emerging Market bond view? The bond market responded positively to the Fed, with Treasury yields initially moving lower across the board, and bonds most sensitive to changes in Treasury yields (such as EM USD government bonds) emerging among the biggest gainers this week. Any US-China partial trade agreement would be an additional tailwind for our continued positive view on Emerging Market (EM) bonds, which is driven by (1) more rate cut signals from EM central banks, such as RBI and, (2) a relatively stable macroeconomic and geopolitical environment, and (3) attractive valuations.

In Asia, Asia High Yield (HY) USD bonds underperformed other major EM markets over the past week amid concerns about potential China HY bond defaults. However, we note the spillover from defaults in the onshore market to the USD-denominated offshore market remains limited. Almost 75% of the asset class comprises of relatively higher quality Investment Grade (IG) bonds and the market has a dedicated regional investor base, providing the asset class with relative stability. We remain comfortable with our preferred view on Asia USD bonds.

FX

Do you expect further declines in USD/CNH? Following positive reports of a partial US-China trade deal, USD/CNH broke below the psychologically important level of 7.00. While details are still awaited, a partial agreement would reduce a key risk facing China's economy and businesses. A deal would mean December tariffs are put on hold. Any roll-back of existing tariffs is likely to push the USD/CNH pair lower towards support at 6.93, followed by 6.85. Resistance at 7.00 to 7.02 should hold if a trade deal is officially announced.

Benchmark (USD) equity market performance w/w*



Source: MSCI, Bloomberg, Standard Chartered
*Week of 05 December 2019 to 12 December 2019

US and Euro area equity market technicals are positive

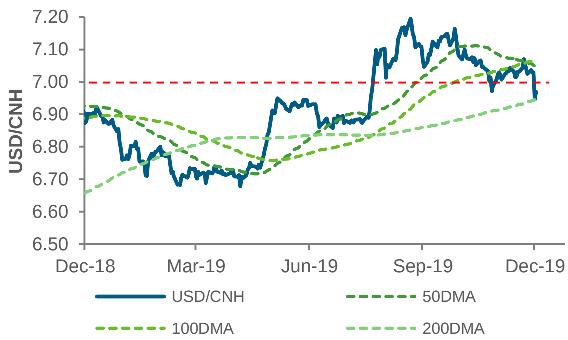
Technical levels of key markets as of 12 December 2019

Index	Spot	1st support	1st resistance	Short-term trend
S&P 500	3,169	3,068	3,210	↑
STOXX 50	3,706	3,630	3,788	↗
FTSE 100	7,273	7,130	7,440	↘
Nikkei 225	23,902	22,700	23,600	↗
Shanghai Comp	2,916	2,860	2,950	↘
Hang Seng	26,994	26,000	27,910	↗
MSCI Asia ex-Japan	663	640	669	→
MSCI EM	1,071	1,031	1,075	↑
Brent (ICE)	64	60	67	↗
Gold	1,466	1,445	1,485	→
UST 10Y Yield	1.93	1.68	2.00	↗

Source: Trading Central, Standard Chartered
Note: Arrows represent short-term trend opinions

USD/CNH broke through the psychological 7.0 mark amid expectations of a partial US-China trade deal; the next support is around 6.93, followed by 6.85

USD/CNH



Source: Bloomberg, Standard Chartered

Top client question

What are the implications of the UK election?

PM Johnson and the Conservative party appear to be heading for a parliamentary majority of 74 seats (Conservative lead vs the combined total of other parties). This would be the largest win since Margaret Thatcher's in 1987, and the worst result for the opposition Labour party since 1935. This projected result importantly provides markets with clarity and this should broadly support currency and asset markets in both the UK and Europe.

Johnson should have the parliamentary and party support to "Get Brexit Done" – at least the initial Withdrawal Agreement part – by the end of January 2020. Thereafter, Britain would enter a transition period (where the current EU membership rules continue to apply) during which a new trade agreement and relationship with the EU is negotiated. Although the current "deal" allows this transition period to be extended as far as end-2022, Johnson has targeted to complete these talks and fully depart from the EU by the end of 2020.

We believe that Johnson can now focus on securing the best EU deal, rather than fulfilling election pledges. The projected election result does include one potential headache for Johnson, as the SNP is on course to win more than 50 seats and it will almost certainly seek another referendum on Scottish independence. Johnson's ability to delay this may depend upon achieving a comprehensive trade deal with the EU that would also solve any customs border issues for Northern Ireland. In addition to securing a trade deal with the EU, Johnson has said that 80% of the UK's external trade will be covered by free trade agreements within 3 years, with prioritisation for the US, Australia, New Zealand and Japan.

We expect that the new government will also propose a new budget in February that increases spending on the health, education and police sectors, and may also include plans for increased broad infrastructure spending. As the economy is likely to receive a boost from the election result, we also think that the Bank of England will be closely monitoring inflationary pressure and may be more prone to hike interest rates, especially if fiscal spending rises quickly.

We remain bullish on GBP/USD with a longer-term expectation of 1.41. Some short-term consolidation is likely, but we expect support between 1.30 and 1.3150 to now provide a strong base. Technical signals are slightly overbought near-term, but once these have cleared, we expect GBP/USD to test 1.3650 in the coming days. Brexit clarity should also help EUR/USD maintain a firmer footing, with the pair breaking above the 200-day moving average and previous high at 1.1180 and testing the next resistance levels at 1.1250 and 1.1400.

UK equities are also likely to rally in the near-term as confidence is restored. MSCI UK price-to-earnings ratio (PE) is trading in line with historical averages and the dividend yield of almost 5% is nearly twice the global average. GBP strength implies domestically-focused sectors, including consumer services, retail and homebuilders, are likely to outperform internationally-focused sectors such as energy and healthcare. This trend will be reinforced by fiscal stimulus in early 2020 and a pick-up in investment as Brexit uncertainty is resolved. UK equities are a core holding.

PM Johnson's Conservative party is set to win the biggest majority since the days of Margaret Thatcher in the 1980s

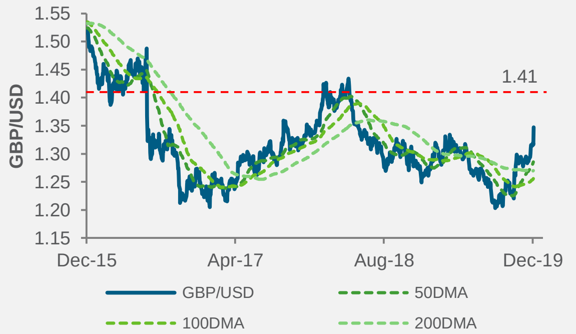
UK election results, with 642 out of total 650 seats declared for 2019 at the time of publishing

	No of Seats	
Party	**2017**	**2019**
Conservative	318	358
Labour	262	203
SNP	35	48
Liberal Democrat	12	11
DUP	10	8
Others	12	14

Source: Bloomberg, Standard Chartered

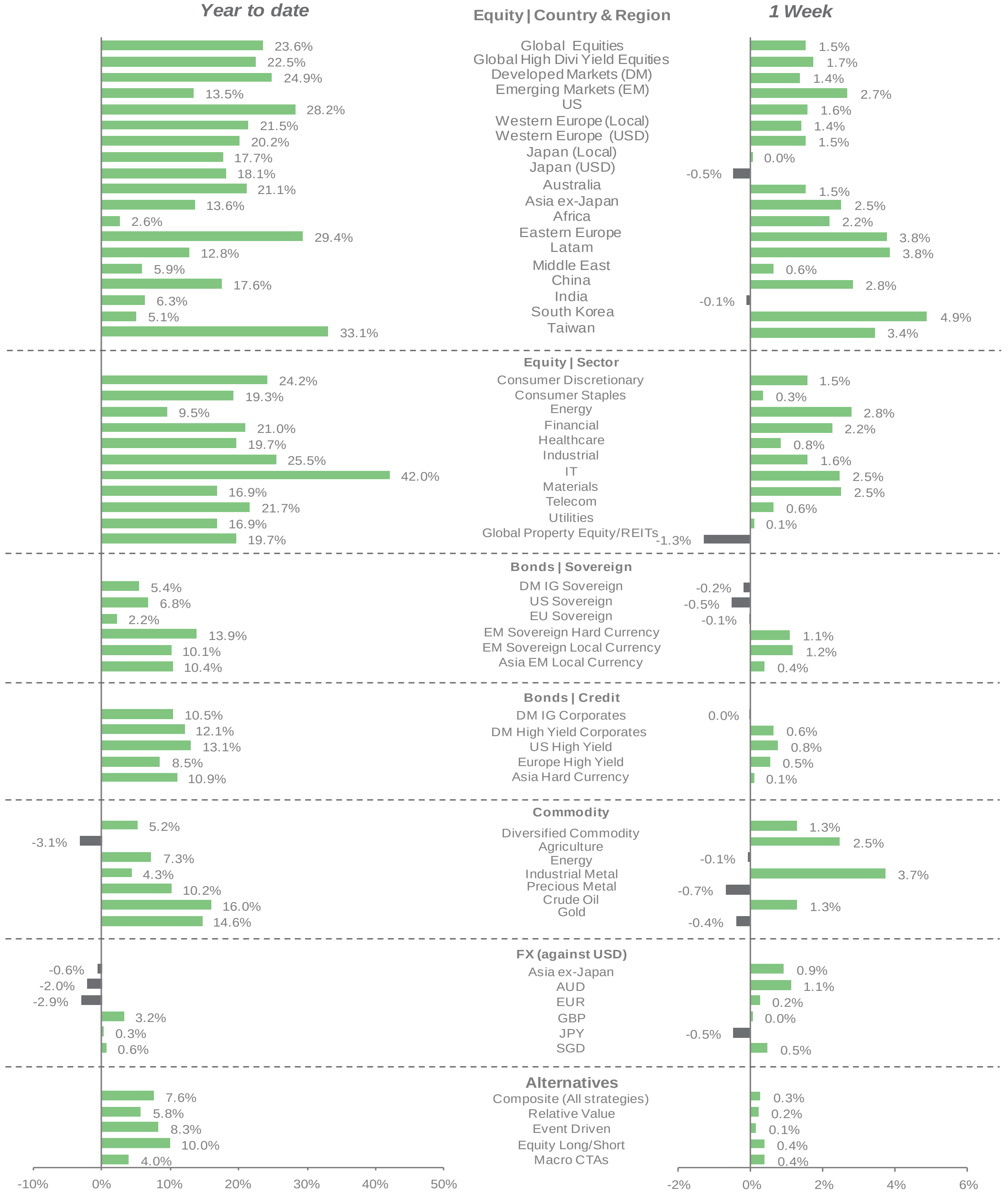
GBP/USD faces next resistance at 1.41, almost 5% above current levels

GBP/USD



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 12 December 2019, 1 week period: 05 December 2019 to 12 December 2019

Economic and market calendar

	Event	Next Week	Date	Period	Expected	Prior
MON	JN	Jibun Bank Japan PMI Composite	16-Dec-19	Dec P	–	49.8
	FR	Markit France Composite PMI	16-Dec-19	Dec P	–	52.1
	GE	Markit/BME Germany Composite PMI	16-Dec-19	Dec P	–	49.4
	EC	Markit Eurozone Composite PMI	16-Dec-19	Dec P	–	50.6
	US	Markit US Composite PMI	16-Dec-19	Dec P	–	52.0
TUE	UK	Average Weekly Earnings 3m/y/y	17-Dec-19	Oct	–	3.6%
	US	Housing Starts	17-Dec-19	Nov	1340k	1314k
	US	Building Permits	17-Dec-19	Nov	1405k	1461k
	US	Industrial Production m/m	17-Dec-19	Nov	0.8%	-0.8%
WED	GE	IFO Expectations	18-Dec-19	Dec	–	92.1
	UK	CPI y/y	18-Dec-19	Nov	–	1.5%
THUR	UK	Retail Sales Ex Auto Fuel y/y	19-Dec-19	Nov	–	2.7%
	UK	Bank of England Bank Rate	19-Dec-19	19-Dec	0.8%	0.8%
	JN	BOJ Policy Balance Rate	19-Dec-19	19-Dec	–	-0.1%
FRI/ SAT	US	Core PCE q/q	20-Dec-19	3Q T	–	2.1%
	US	Personal Income	20-Dec-19	Nov	0.3%	0.0%

	Event	This Week	Date	Period	Actual	Prior
MON	GE	Exports SA m/m	09-Dec-19	Oct	1.2%	1.5%
	EC	Sentix Investor Confidence	09-Dec-19	Dec	0.7	-4.5
	CH	Aggregate Financing CNY	09-Dec-19	Nov	1750.0	618.9b
TUE	CH	CPI y/y	10-Dec-19	Nov	4.5%	3.8%
	CH	PPI y/y	10-Dec-19	Nov	-1.4%	-1.6%
	FR	Industrial Production y/y	10-Dec-19	Oct	-0.2%	0.2%
	EC	ZEW Survey Expectations	10-Dec-19	Dec	11.2	-1.0
	US	NFIB Small Business Optimism	10-Dec-19	Nov	104.7	102.4
WED	US	CPI Ex Food and Energy y/y	11-Dec-19	Nov	2.3%	2.3%
	US	Real Avg Hourly Earning y/y	11-Dec-19	Nov	1.1%	1.1%
THUR	US	FOMC Rate Decision (Upper Bound)	12-Dec-19	11-Dec	1.75%	1.75%
	JN	Core Machine Orders y/y	12-Dec-19	Oct	-6.1%	5.1%
	EC	ECB Main Refinancing Rate	12-Dec-19	12-Dec	0.0%	0.0%
	US	PPI Ex Food and Energy y/y	12-Dec-19	Nov	1.3%	1.6%
FRI/ SAT	JN	Industrial Production y/y	13-Dec-19	Oct F	-7.7%	-7.4%
	US	Retail Sales Ex Auto and Gas	13-Dec-19	Nov		0.1%

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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