Wealth Management Chief Investment Office
14 October 2022

Weekly Market View

Keeping at it, for now

- The Fed is likely to 'keep at it', tightening policy despite growth expectations falling across Developed Markets

- The Fed's focus is expected to remain on raising interest rates through the end of the year. However, some FOMC participants indicated heightened economic and financial uncertainty may require the pace of policy tightening to be calibrated at some point

- We believe the rise in bond yields is creating an attractive entry point for investment grade bonds and multi-asset income strategies. Meanwhile, we expect USD-JPY to sustainably break through the 1998 high before the Bank of Japan considers intervening again

What is your take on the sector impact of the new US policy on semiconductor sales to China?

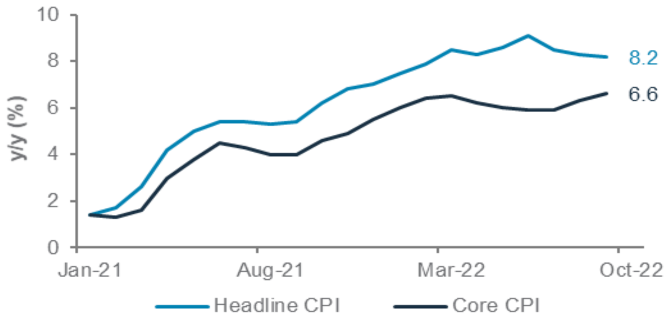
What are your thoughts on the Q3 22 US earnings season?

Will GBP/USD breach parity?

Charts of the week: What does it take for the Fed to pivot?

The Fed is keeping at it in the face of persistent inflationary pressures; geopolitics hits the semiconductor sector

US core inflation hits a 40-year high in September



Semiconductor sector stocks hit by US stance on China sales

Source: Bloomberg, Standard Chartered

Editorial

Keeping at it, for now

The Fed is likely to 'keep at it', tightening policy despite growth expectations falling across Developed Markets (DM). Until this changes, we would view equity market bounces as bear market rallies. Spikes in yields, though, likely offer attractive entry points for high-quality bonds and multi-asset income strategies. We retain a bearish short-term outlook for the GBP.

Consensus growth forecasts continue to dip across DMs: 2023 consensus GDP growth forecasts are 0.7% in the US and 0.2% in the Euro area, while the UK is seen experiencing a full year recession. The IMF downgraded global growth projections, especially in the Euro area, and now forecasts Germany and Italy will experience a full year recession.

Despite this, DM central banks continue to tighten policies aggressively. Minutes from the latest Fed policy meeting showed policymakers were more concerned about taking too little action than too much. This week's inflation data, with core inflation rising to a new 40-year high, is only likely to reinforce these concerns. Meanwhile, the strength of the labour market, with the unemployment rate falling to cycle lows once again, is likely to keep the Fed focused on raising interest rates through the end of 2022 at least – a fourth consecutive 75bps rate hike is likely in early November. Some FOMC members indicated heightened economic/financial uncertainty may require the pace of policy tightening to be calibrated at some point, but the inflation data may push that discussion to 2023.

The narrative for mainland China is very different. While the IMF downgraded its 2023 growth forecast here as well, it still expects policy easing to support a recovery in 2023, and new loans data this week reaffirmed the stimulus is starting to feed through to the economy. However, the US's decision to require companies to obtain licenses to export semiconductor chips to mainland China is a significant development. Chinese authorities will likely see this as an attempt to limit its economic development and double-down on its plan to reduce reliance on foreign technology. Semiconductor stocks have pummelled the world over. We would be cautious about adding here, though the sharp sell-off and spike in volatility may offer attractive income-generating opportunities via structured strategies.

Last week, we indicated markets were overestimating the probability of a near-term pivot in monetary policy. Since then, US 10-year government bond yields have risen sharply, testing 4% once again. We see this as an opportunity to add to bond portfolios – we prefer Investment Grade (IG) corporate bonds in the US and Asia – and multi-asset income strategies.

Meanwhile, global and US equities have made new 2022 lows, and the VIX equity market volatility index is close to 2022 highs. Against this backdrop, equities may temporarily recover even if the data improves only modestly. However, we would still view any such bounce as a temporary bear market rally until the Fed shifts focus to supporting growth.

On FX, markets are likely to test the Bank of Japan's desire to intervene again by pushing USD/JPY sustainably above the 1998 high of 147.65. In the UK, the focus is on whether the Bank of England can extricate itself from the provision of emergency liquidity measures as well as any potential government policy reversal regarding its mini-budget. We believe 1.14-1.16 will offer strong GBP-USD resistance, before a test of 1.05-1.07.

Next week, the focus will be on US housing market data. Mortgage rates have surged, hitting activity and sentiment hard – although house prices are still rising strongly. Housing starts is the most important release, and the consensus is for a decline after August's bounce. We also have a series of Fed speakers who will have the opportunity to tweak their messaging after this week's disappointing inflation data.

— Steve Brice

The weekly macro balance sheet

Our weekly net assessment: On balance, we see the past week's data and policy as negative for risk assets in the near term.

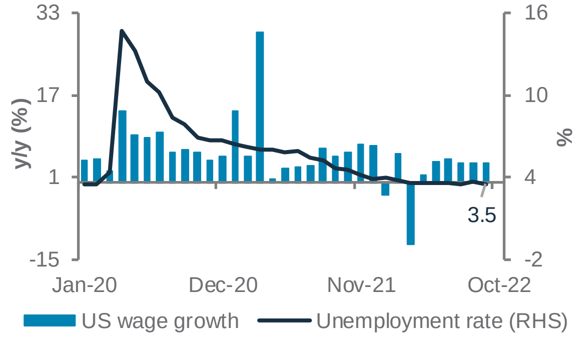
(+) factors: Strengthening China new loans data

(-) factors: Hawkish Fed, strong US services data, OPEC output cut

	Positive for risk assets	Negative for risk assets
COVID-19		• Shanghai COVID-19 cases hit three-month high, leading to school closures
	Our assessment: Negative – Cases rising again, though outside of China, policymakers are not reacting	
Macro data	• US labour market continues to generate strong jobs growth • US small business confidence rose slightly, as did consumer credit • US consumer one-year forward inflation expectations fell further • China new loans rose more than expected in September • Euro area industrial production expanded more than expected	• US core inflation hits a 40-year high • US participation rate fell in September, leading to tighter labour market • Household incomes expected to slow to 6% (NY Fed consumer survey) • Euro area investor confidence fell more than expected • UK industrial production declined and wages accelerated, both more than expected
	Our assessment: Negative – Still elevated inflation pressures to encourage further aggressive tightening in the US	
Policy developments	• FOMC minutes talk about the potential calibration of monetary policy tightening amid heightened economic and financial uncertainty • UK looks set to backtrack on 'mini' budget	• FOMC minutes show Fed focused on fighting inflation • ECB's Holzmann indicates shallow recession will not get in the way of policy tightening • BoE aims to remove liquidity support this week
	Our assessment: Negative – Fed, ECB firmly focused on fighting inflation, even at the cost of growth	
Other developments		• US tightens controls over semiconductor chip exports to China
	Our assessment: Negative – US semiconductor policy is only likely to intensify 'strategic competitor' narrative	

Tight labour market keeping the Fed on the offensive for now

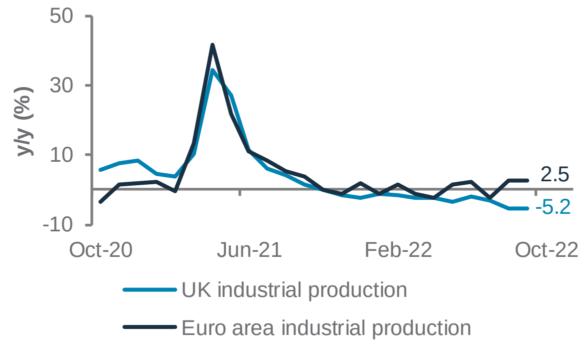
Unemployment rate falls back to cyclical lows while wage growth remains elevated



Source: Bloomberg; Standard Chartered

Euro area on the verge of a recession despite a rebound in industrial production

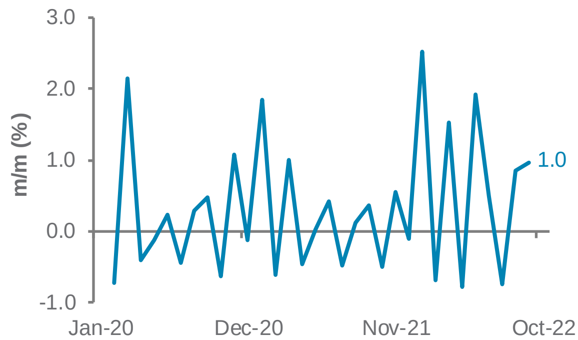
Euro area and UK industrial production, % y/y



Source: Bloomberg, Standard Chartered

China stimulus feeding through in new loans

China new loans, 12-month moving average, % m/m



Source: Bloomberg, Standard Chartered

Top client questions

What is your take on the recent news surrounding the semiconductor sector?

Semiconductor stocks have fallen in recent weeks due to concerns about a cyclical slowdown and further geopolitical impediments to sales. Firstly, on the cyclical slowdown, a major PC chip supplier warned of lower Q3 22 revenues due to a sharp deterioration in the PC market and an inventory correction. Data centre chip demand remains resilient, but could be at risk from a further economic slowdown. Secondly, on geopolitics, the US government announced new restrictions on the sale of advanced chips to Mainland China. This is likely to undermine revenue opportunities into 2023 for leading chipmakers and semiconductor equipment vendors in the US that generate up to 30% of their sales from Mainland China.

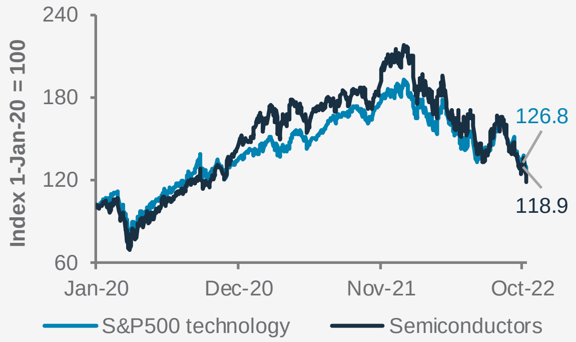
In our view, semiconductor equities have already priced in a lot of negative news, and we see selectively attractive value over the longer term. Risk management is paramount in volatile markets, and semiconductor stocks could test new lows. The Philadelphia Semiconductor index has corrected by 46% from its peak, but remains over 70% higher from pandemic lows. However, we believe long-term drivers for semiconductors remain in place, with the digitalisation trend, in particular, accelerated by COVID-19. Heightened volatility, though, means structured strategies have become increasingly attractive, in our view.

— **Fook Hien Yap,** *Senior Investment Strategist*

Semiconductor stocks have fallen 46% from the peak in December 2021, but continue to be over 70% above the pandemic low

S&P500 Technology and Philadelphia Semiconductor (SOX) indices

Rebased to 100=1-Jan-2020



Source: Bloomberg, Standard Chartered

What are your thoughts on the Q3 22 US earnings season?

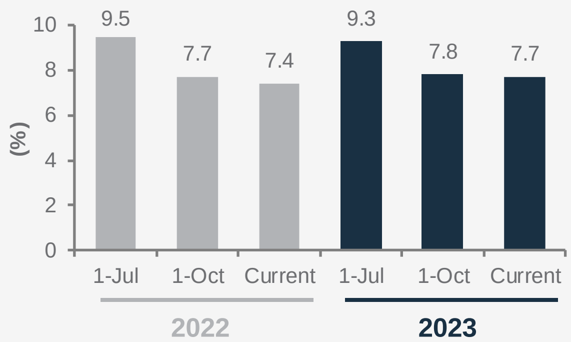
Q3 2022 consensus earnings growth for S&P500 is 4.1% y/y – the lowest this year. Expectations have been moving lower gradually from over 11% at the beginning of July. The inflationary environment, particularly in terms of raw material costs and wages, impacts the cost of doing business, and aggressive Fed rate hikes are likely to lead to a dampening of demand. This macro environment is likely to dominate over individual company fundamentals for now until there is more room for optimism on inflation.

In terms of sectors, only 4 of the 11 are expected to deliver positive earnings growth, with energy leading the pack at 121% y/y. Energy remains a preferred sector across the US, Europe and China. On the other side of the spectrum, communication services are expected to show the biggest earnings decline at 16%. We have recently downgraded the sector to less preferred as the sector's high valuation is likely to be most negatively impacted by rising yields. Financials is also projected to show an earnings decline of 10%, challenged by increasing stress on loans amid an economic slowdown.

— **Daniel Lam,** *Head, Equity Strategy*

Consensus earnings growth in the US has been revised down since mid-2022

S&P500 consensus earnings growth for 2022 and 2023 at various points in time



Source: Refinitiv, Standard Chartered

Top client questions (cont'd)

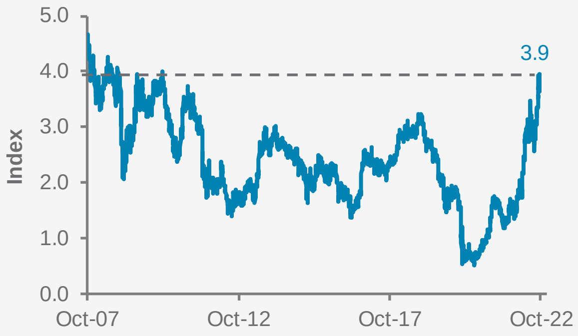
What is your latest view on US Treasuries after the recent US economic data release?

The 10-year US Treasury yield moved higher to 3.92% after the latest US September CPI print. This data and the latest Fed FOMC minutes, which showed policymakers continue to be largely focused on inflation, support our view that it may be too soon to expect a Fed pivot and the US 10-year government bond yields are likely to continue testing the technical resistance at 4%. While brief moves above this level remain probable (we see subsequent technical resistances at 4.14% and 4.34%), historically the resulting rise in recession expectations acts in the opposite direction and is likely to limit yields from moving substantially higher. Hence, we believe any rise in yields should be regarded as an attractive entry point, especially in our preferred high-quality bond asset classes – DM IG corporate bonds and Asia USD bonds.

— **Cedric Lam,** *Senior Investment Strategist*

The 10-year US Treasury yield moved higher after the latest US Sept CPI print, though failed to sustainably hold above 4%

10-year US Treasury yield



Source: Bloomberg, Standard Chartered

How likely is it for GBP/USD to break below parity?

GBP/USD has seen a persistent spike in volatility since the announcement of the UK 'mini' budget on 23 September, with the pair initially declining to a 50-year low around 1.0350 before recovering to 1.1495 following the BoE's intervention to help mitigate margin call risks for pension funds.

Earlier this week, BoE Governor Bailey's announcement that the central bank would end market intervention by 14 October led to concerns of renewed selling pressure on UK government bonds (Gilts). As the 30-year Gilt has declined by over 50% this year, there are concerns that this could mean UK pension funds that had borrowed money to invest in long-term Gilts could face an increased risk of margin calls should prices decline (yields rise) further. However, news reports indicate that UK Finance Minister Kwarteng left IMF talks in Washington early, which has increased market expectations that the new UK government may make a U-turn on the mini-budget, including the corporate tax cut component. This could potentially alleviate market concerns around the UK's fiscal stability and has provided a near-term boost to the GBP.

While upward momentum could see a re-test of 1.14 and even 1.16 over the next few days, we expect GBP/USD to edge lower in the coming weeks, with 1.0700 and 1.0500 as key near-term supports. Disappointment on potential rollback or budget proposals could raise the risk of a test of parity, but we believe GBP/USD may struggle to break below the 1.0500-1.0700 region where it should stabilise.

— **Abhilash Narayan,** *Senior Investment Strategist*

GBP/USD likely to edge lower in the coming weeks, though it is likely to struggle to break below 1.05-1.07

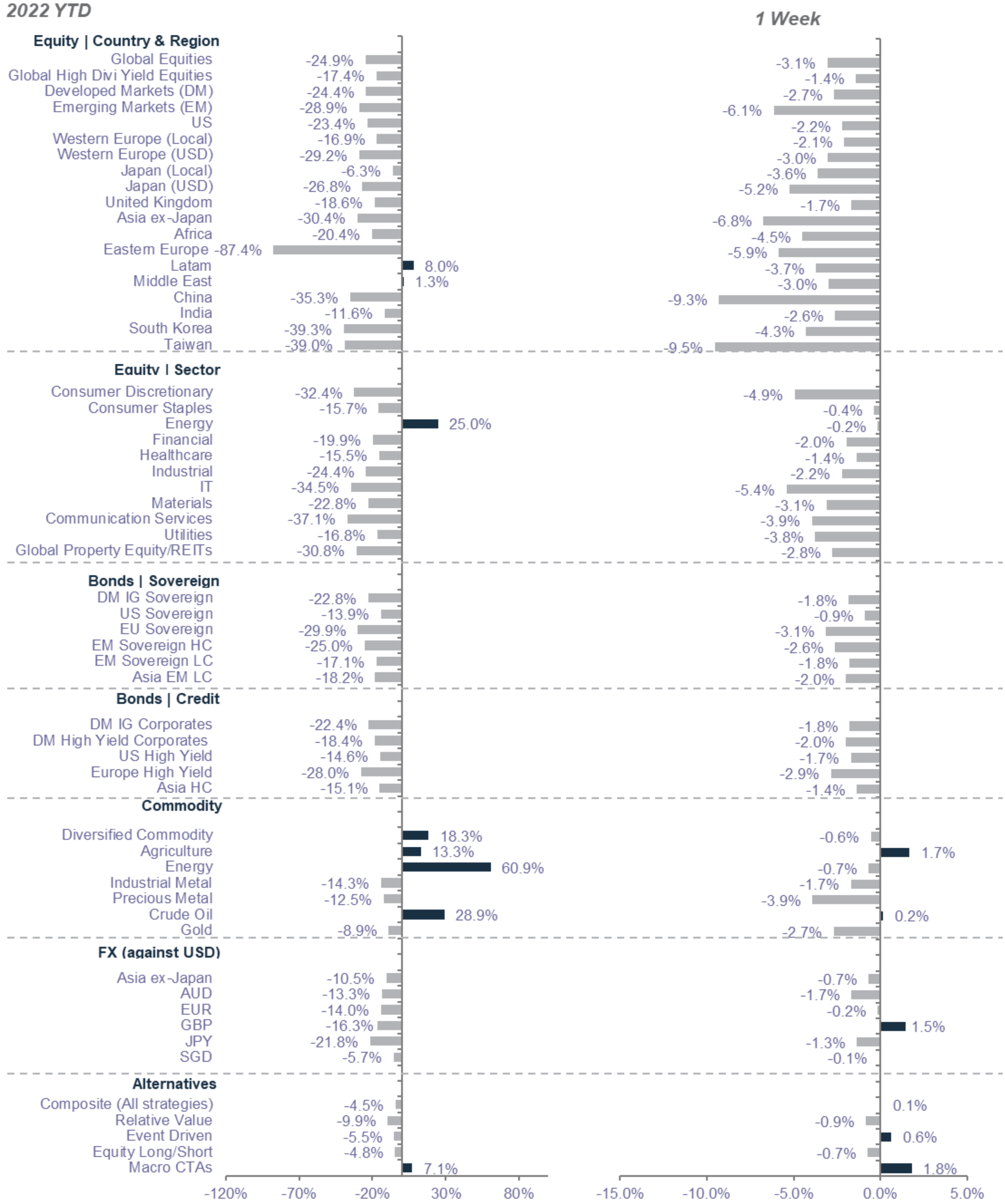
GBP/USD

Source: Bloomberg, Standard Chartered

Measures of GBP volatility remain elevated

GBP/USD 1m at the money implied vol

Market performance summary *



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

*Performance in USD terms unless otherwise stated, 2022 YTD performance from 31 December 2021 to 13 October 2022; 1-week period: 06 October 2022 to 13 October 2022

Our 12-month asset class views at a glance

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

Source: Standard Chartered Global Investment Committee

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

Economic and market calendar

	Event	Next week	Period	Expected	Prior
MON					
TUE	CH	Industrial Production y/y	Sep	4.9%	4.2%
	CH	GDP y/y	3Q	3.5%	0.4%
	CH	Retail Sales y/y	Sep	3.2%	5.4%
	GE	ZEW Survey Expectations	Oct	-	-61.9
	EC	ZEW Survey Expectations	Oct	-	-60.7
WED	UK	CPI y/y	Sep	-	9.9%
	EC	CPI y/y	Sep	-	9.1%
	US	Housing Starts	Sep	1485k	1575k
THU	US	Philadelphia Fed Business Outlook	Oct	-5	-9.9
	US	Initial Jobless Claims	15 Oct	-	-
FRI/SAT	EC	Consumer Confidence	Oct P	-	-28.8

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

Next support for S&P500 is at 3608

Technical indicators for key markets as on 13 October

Index	Spot	1st support	1st resistance
S&P 500	3,670	3,608	3,701
STOXX 50	3,362	3,337	3,381
FTSE 100	6,850	6,787	6,952
Nikkei 225	26,909	26,392	27,271
Shanghai Comp	3,016	2,985	3,037
Hang Seng	16,389	15,939	17,290
MSCI Asia ex-Japan	538	528	559
MSCI EM	855	840	883
Brent (ICE)	94.2	91.8	97.2
Gold	1,660	1,649	1,683
UST 10y Yield	3.93	3.89	3.96

Source: Bloomberg, Standard Chartered
Note: These short-term technical levels are based on models and may differ from a more qualitative analysis provided in other pages

Investor diversity remains reasonably high across assets

Our proprietary market diversity indicators as of 13 October

Level 1	Diversity	1-month trend	Fractal dimension
Global Bonds	◐	↓	1.34
Global Equities	◐	↓	1.50
Gold	●	↓	1.56
Equity			
MSCI US	●	→	1.57
MSCI Europe	◐	↓	1.42
MSCI AC AXJ	◐	↓	1.31
Fixed Income			
DM Corp Bond	◐	↓	1.37
DM High Yield	●	↓	1.76
EM USD	●	↓	1.66
EM Local	●	↓	1.58
Asia USD	●	↓	1.53
Commodities			
WTI Crude Oil	●	→	1.68

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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