

Weekly Market View

Second-wave jitters

The equity market rally has stalled amid worries about a second pandemic wave slowing an economic recovery and US-China tensions; we believe averaging-in remains a valid strategy

Equities: Hang Seng should get a boost from a likely decision to include dual-listed new-economy stocks

Bonds: While US Investment Grade bond yield premiums could compress further amid Fed purchases, the path is likely to be gradual and bumpy

FX: Any signs of a renewed COVID-19 wave or growing US-China tensions would be positive for the USD in the near-term

Second wave jitters

Also find out...

What is the likely impact of Fed bond ETF purchases on bond prices?

Will dual-listed stocks be allowed in the Hang Seng index?

What are the signposts for FX and gold markets?

Chart of the week: Jobs recovery key as US equity rally stalls

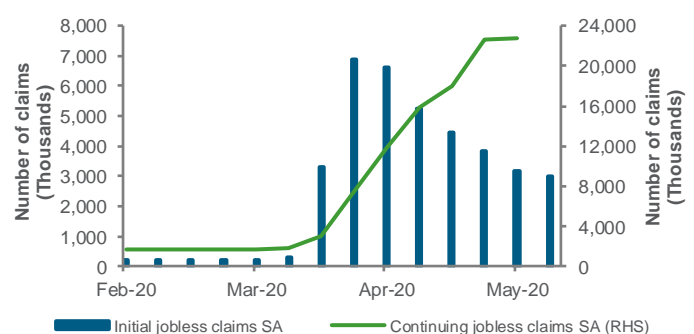
A stabilisation in jobless claims would be a key indicator that the worst is over – this could drive the next leg of the equity market rally

S&P 500 index



Source: Bloomberg, Standard Chartered

US initial and continuing jobless claims



Editorial

Second-wave jitters

After the rebound comes the hangover. Global equities have soared as much as 35% from their 23 March lows, retracing almost two-thirds of previous losses on the back of unprecedented stimulus and signs that the worst of the COVID-19 pandemic could be over. However, the equities reversal in the past two weeks likely reflects the 'hangover' phase as markets worry that early re-opening of economies could lead to a second-wave of infections, forcing renewed lockdowns. Comments from US health experts and Fed policymakers warning of downside risks and President Trump's rhetoric against China add to the uncertainty.

We assess the implications of re-opening of major economies through their high-frequency data. So far, this data reflects the gradual normalisation of economic activity in China, led by the manufacturing sector (see page 3). While we have seen new clusters of infections in China and South Korea, they have been limited in scope and contained by targeted quarantine measures. Germany's decision to re-open land borders from 15 June indicates its confidence that the worst of the pandemic is likely over. However, any new infections in these economies will likely be under the spotlight in the coming weeks.

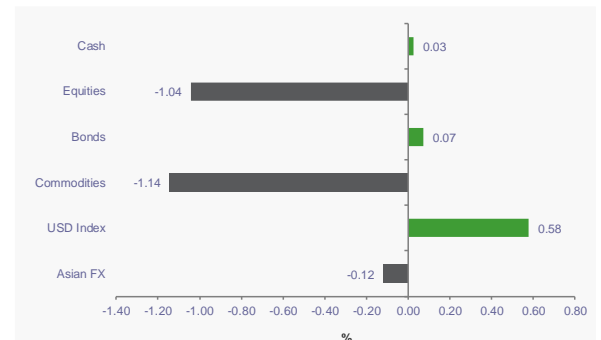
While economic growth data for March and April have been predictably weak (with signs of deflationary pressure, not least due to the slump in oil prices), a key indicator of where growth goes from here would be the pace of a job market recovery. US initial jobless claims have continued to decline for the sixth week in a row after its record surge in March.

We believe equities are undergoing a healthy correction after the April run-up. Technical charts show the S&P 500 index faces resistance near the 200-day moving average (c. 3,000). Support is just below 2,800 (see page 3). In the absence of a major resurgence of the pandemic, we believe March lows are unlikely to be tested again, especially with the Fed, ECB and PBoC reiterating their pledge to increase policy support if needed. There is also talk of more fiscal stimulus worldwide (see page 3 for India's latest). Given this, we would view drawdowns as an opportunity to average into our preferred assets – US and Asia ex-Japan equities and Emerging Market (EM) and Asia USD bonds.

We would also watch for any spike in FX volatility after the recent lull, especially in USD/CNY, from any renewed US-China tensions.

Global equities fell over the past week, while the USD rose amid concerns about downside risks to the economy from any second wave of the pandemic

Benchmark market performance w/w*



Source: MSCI, JP Morgan, DJ-UBS, Citigroup, Bloomberg, Standard Chartered

*Week of 07 May 2020 to 14 May 2020

Euro area equity market technicals have weakened, US remains neutral, while Asia remains positive

Technical indicators for key markets as on 14 May 2020

Index	Spot	1st support	1st resistance	Short-term trend
S&P	2,853	2,730	2,955	→
STOXX 50	2,760	2,550	2,947	↗
FTSE 100	5,742	5,597	6,070	↗
Nikkei 225	19,915	19,400	20,800	↗
Shanghai Comp	2,870	2,800	2,940	↗
Hang Seng	23,830	23,600	25,000	↑
MSCI Asia ex-Japan	603	577	615	↗
MSCI EM	909	864	930	↗
Brent (ICE)	31	23	36	↗
Gold	1,730	1,655	1,745	↑
UST 10Y Yield	0.63	0.30	0.92	↓

Source: Trading Central, Standard Chartered

Note: Arrows represent short-term trend opinions

Factors to watch

China high-frequency indicators point to gradual recovery

As economies re-open, the focus is likely to turn to how quickly economic activity returns to normal. Trends from China, the first major economy to relax lockdowns, indicate a robust recovery in the industrial sector, but persistent weakness in services and retail sectors. Among industries, cement and steel rod inventories and heavy truck and excavator sales are back to pre-lockdown levels, indicating a pick-up in construction activity as authorities jump-start infrastructure spending. Coal consumption at power plants is above 2019 levels for the first time since January. Among retail sales, although smartphone sales have rebounded to above pre-lockdown levels, sales of cars and properties are 20-30% below and hotel occupancy and domestic flights are 40-50% below January levels. Also, while intra-city traffic congestion has returned to 2019 levels, inter-city passenger traffic is almost 50% below last year's levels. All of this points to a gradual, two-tier recovery.

In the US and Euro area, which are likely 1-2 months behind China in the COVID-19 cycle, data appears to be stabilising after a sharp plunge in March. However, the recovery trajectory in US/Europe may differ somewhat from that of China given (i) the absence of significant infrastructure spending, and that (ii) most the stimulus measures were directed towards small businesses and to help keep workers in jobs.

What is the technical outlook for US equities?

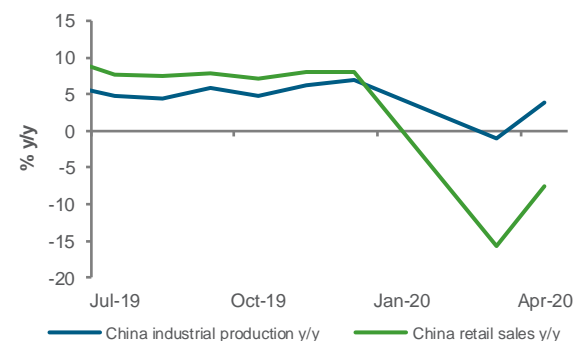
The S&P 500's rally has stalled at key resistance around the 200-day moving average (DMA; 3,000) and the 61.8% retracement of the February-March fall (at 2,935). This loss of momentum raises the chances of a setback following the 35% rally from the late-March low. The 4 May low of 2,798 is a crucial support – any break below this could trigger a correction following a minor double-top (April 29 and May 12 highs), potentially paving the way towards the 31 March high of 2,641 (7.4% below Thursday's close). In the event 2,798 holds, the probability of a break above the 200DMA increases, in our view, potentially opening the way towards February's record high of 3,394. If 2,798 breaks, but 2,641 holds, a retest of the 200DMA could still be possible, but with reduced odds of a move towards February's high. If 2,641 breaks, a broad range of 2,192-2,955 (March low and May high) could ensue.

India's stimulus exceeds that of Emerging Market peers

India's INR 20trn (~USD 265bn) economic support package, equalling about 10% of GDP, makes it the largest among EM peers. The fiscal impact is likely to be low, given most of the package thus far consists of credit guarantees to ease financial stress and boost the effectiveness of central bank measures to cut funding costs.

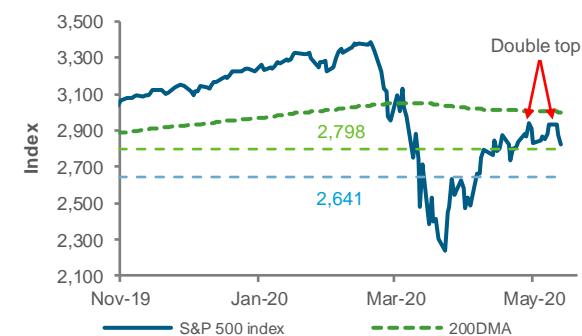
However, the near-term outlook is still uncertain given India is yet to see a peak in COVID-19 infection rates. Furthermore, the extension of the lockdown has raised the probability of a rare contraction in the economy. Although equity markets have partially recovered, the extended lockdowns raise the risk of sharp earnings downgrades, given consensus still expects 10% growth in Nifty index earnings for the year ending March 2021. This could challenge further equity market strength in the near term. Government bond yields have risen following the government's plan to raise its annual bond issuance by about 50% amid falling tax revenues. However, we believe the INR is likely to remain relatively resilient compared to EM peers given lower oil prices, positive balance of payment dynamics and ample FX reserves.

China data shows a two-tier recovery: the industrial sector is leading while retail sales, services are lagging
China's industrial production and retail sales growth



Source: Bloomberg; Standard Chartered

The S&P 500 index faces resistance around 3,000; the 4 May low of 2,798 is a crucial support, followed by 2,641
S&P 500 index, with key technical levels



Source: Bloomberg; Standard Chartered

India's record stimulus package should support the INR, although the risk of sharp earnings downgrades remains a near-term challenge for the equity market

MSCI India index, USD/INR



Source: Bloomberg, Standard Chartered

Top client questions

Q What is the likely impact of Fed bond ETF purchases on bond prices? Do you still see a risk of further volatility in US High Yield (HY) bonds?

While markets are quite optimistic about the Fed's announcement that it will start purchasing corporate bond ETFs, we view it as a glass half-full due to the following reasons:

- The total amount of US Investment Grade (IG) and HY bonds owned by ETFs amount to less than 5% of the market. Given that the Fed is likely to purchase up to 20% of an ETF, that would amount to the Fed buying less than 1% of the market.
- The positivity around ETF purchases masks the fact that the US bond issuances are rising, and future issuance plans appear onerous, in our view.
- The Fed's primary and secondary market bond purchases programmes do not intend to buy single-B or CCC-rated bonds that are the most stressed area within the bond market. Hence, we believe there is a high likelihood that default rates still rise to high single digits, similar to past recessions, which could put upward pressure on HY bond yield premiums.

Hence, given that the Fed has just started buying corporate bonds, the yield premiums over the past month have likely been largely driven by optimistic investor sentiment. While IG spreads have room to compress a bit more, the path may be gradual and bumpy.

Q Are 10-year US Treasury yields likely to rise due to higher supply?

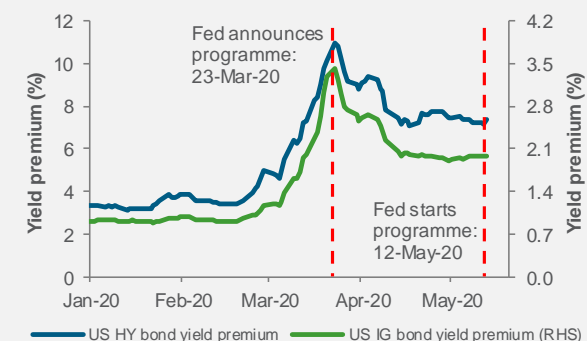
In the next 6-12 months, we believe the massive increase in the supply of US Treasuries is unlikely to lead to sharply higher yields. Our benign view on yields rests on the following four pillars:

- **Fed Funds rates** – While the Fed has indicated that it is reluctant to move interest rates to negative territory, markets are assigning a reasonably high probability of further rate cuts by the Fed.
- **Fed bond purchases** – They are likely to stay elevated for the rest of 2020, helping absorb additional supply coming to the market.
- **Inflation expectations** – The decline in oil prices has led to sharply lower long-term inflation expectations. This means inflation expectations are unlikely to rise sharply over the next 6-12 months, even if oil prices rebound modestly as we expect, providing an anchor to US Treasury yields.
- **Global growth uncertainty** – US Treasuries are usually treated as a safe haven asset. As we discuss at the start of this publication, any economic recovery is likely to be uneven and take time. Additionally, the risk of a second wave of COVID-19 exists. Hence, safe-haven demand for US Treasuries is likely to stay in place.

Thus, while it is possible that yields rise somewhat from current levels as economies start to reopen, they are unlikely to be sharply higher on a sustained basis, in our view.

Although US Investment Grade bond yield premiums have room to compress a bit more amid Fed purchases, the path may be gradual and bumpy

US Investment Grade and High Yield bond yield premium over Treasuries



Source: Bloomberg, Standard Chartered

US Treasury yields are likely to remain under pressure from the drop in long-term inflation expectations, while global growth uncertainty sustains safe-haven demand

US 10-year government bond yield; 10-year inflation expectations derived from inflation-protected bonds



Source: Bloomberg; Standard Chartered

Top client questions (cont'd)

Q Will dual-listed stocks be allowed in the Hang Seng index?

On 18 May, the Hang Seng Indexes Company will announce the result of its consultation on the eligibility of Weighted Voting Rights (WVR) companies and secondary-listed companies for inclusion in the Hang Seng Index and Hang Seng China Enterprises Index. Although there are currently only three WVRs listed in Hong Kong, they are new-economy stocks with high growth potential, accounting for about 31% of the Hang Seng Index's current market capitalisation. We expect results of the consultation to be supportive for inclusion; stocks could be added in steps to help investors transit. On secondary-listed companies, the review is only on Greater China companies. Given this means the only stock for consideration is a technology giant, we believe investors will support this proposal as the stock is too big to be excluded from the index. In addition, it is reported that more Chinese ADRs may choose the secondary listing form. Excluding these could undermine the representativeness of the Hang Seng index.

Should Hang Seng Index open its door to WVRs and secondary listings, we expect two heavyweight new economy stocks will qualify to join the index initially. This would be positive for the Hang Seng Index as it would broaden its exposure to China's growing tech sector and induce more institutional fund flows for benchmarking purposes. China equities remain our preferred market in Asia ex-Japan.

Q What are the signposts for FX and gold?

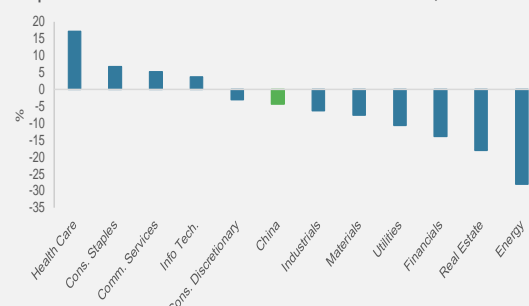
FX markets have recently drifted into a range-bound scenario. From here, our focus is on risk catalysts and technical range breakouts:

- A simple bellwether for market sentiment is likely to be the direction of US equities. Stability or a continuing rise would support a pro-risk stance and likely help the USD to weaken. A sharp decline would likely re-trigger the demand for USD.
- Behind the market sentiment driver, three underlying factors are likely to be key. Firstly, the coming weeks are critical for the economic reboot – any sign of a second COVID-19 wave would be USD-supportive. Secondly, a further rise in US-China tensions would likely drive support the USD and safe-haven currency strength. Finally, markets will likely be sensitive to EU unity following a recent German court ruling on ECB policy. Signs of a deterioration could weaken the EUR and lift the USD.
- From a technical perspective, we would focus on a breakout of the EUR/USD from either initial support at 1.0725 or resistance at 1.1025 to signal the next broad move for the USD. Any escalation of US-China tensions that put the trade deal at risk could push USD/CNH above the previous 7.1650 high. AUD/USD is showing signs of consolidating recent gains; a break below 0.6370 could open a decline to the 0.6000-0.6150 window.

Against this backdrop, we believe our "buy-on-dips" strategy for gold remains valid. On technical charts, gold has broken above the top of its triangle pattern – traditionally viewed as a consolidation pattern. A further break above immediate resistance at 1747 would likely pave the way for gains towards 1800. We would continue to add exposure to gold on pullbacks, with key supports at around 1720 and 1680.

New-economy sectors such as healthcare, technology have outperformed China equities YTD

YTD performance of MSCI China index sectors, USD-based



Source: MSCI, FactSet, Standard Chartered

Any signs of a second COVID-19 wave or rise in US-China tensions in the coming weeks would be USD supportive

EUR/USD



Source: Refinitiv; Standard Chartered

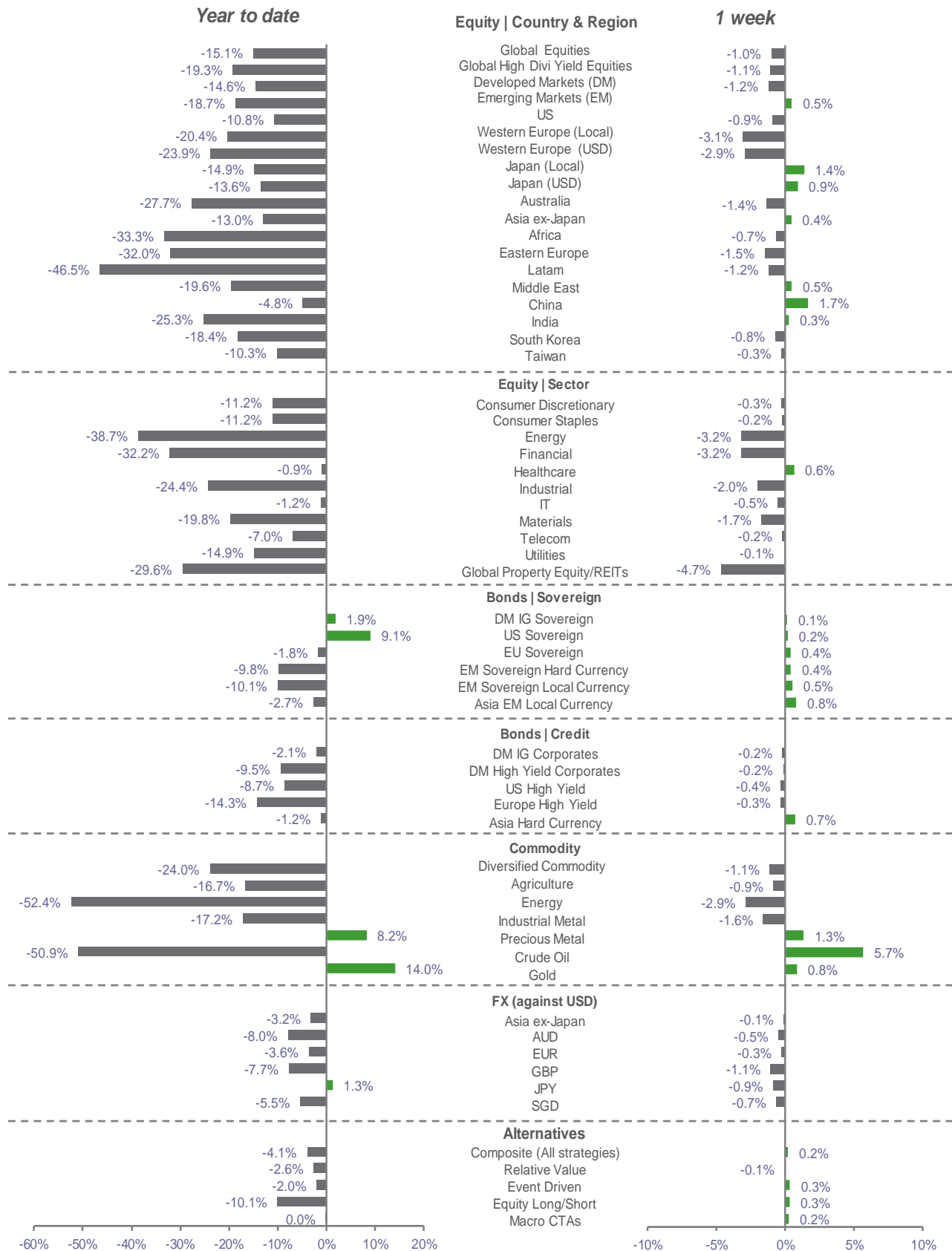
Gold has broken above the top of its triangle pattern; further break above resistance at 1747 would likely pave the way for gains towards 1800

Gold price, USD/oz



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, 2019 performance from 31 December 2019 to 14 May 2020, 1 week period: 07 May 2020 to 14 May 2020

Economic and market calendar

	Event	Next Week	Date	Period	Expected	Prior
MON	JN	GDP Annualized SA q/q	18-May-2020	1Q P	-4.5%	-7.1%
TUE	UK	Average Weekly Earnings 3m/y/y	19-May-2020	Mar	–	2.8%
	EC	ZEW Survey Expectations	19-May-2020	May	–	25.2
	US	Building Permits	19-May-2020	Apr	1000k	1350k
	US	Housing Starts	19-May-2020	Apr	950k	1216k
WED	EC	ECB Current Account SA	20-May-2020	Mar	–	40.2b
	UK	CPI Core y/y	20-May-2020	Apr	–	1.6%
	EC	Consumer Confidence	20-May-2020	May A	–	-22.7
THUR	US	Philadelphia Fed Business Outlook	21-May-2020	May	-40.0	-56.6
	US	Markit US Composite PMI	21-May-2020	May P	–	27
	US	Leading Index	21-May-2020	Apr	-5.7%	-6.7%
	US	Existing Home Sales	21-May-2020	Apr	4.38m	5.27m
FRI/SAT	FR	Markit France Composite PMI	22-May-2020	May P	–	11.1
	GE	Markit/BME Germany Composite PMI	22-May-2020	May P	–	17.4
	EC	Markit Eurozone Composite PMI	22-May-2020	May P	–	13.6

	Event	This Week	Date	Period	Actual	Prior
MON						
TUE	CH	PPI y/y	12-May-2020	Apr	-3.1%	-1.5%
	CH	CPI y/y	12-May-2020	Apr	3.3%	4.3%
	IN	Industrial Production y/y	12-May-2020	Mar	-16.7%	4.6%
	US	CPI Ex Food and Energy y/y	12-May-2020	Apr	1.4%	2.1%
WED	JN	BoP Current Account Adjusted	13-May-2020	Mar	¥942.3b	¥2352.5b
	UK	GDP y/y	13-May-2020	1Q P	-1.6%	1.1%
	US	PPI Ex Food and Energy y/y	13-May-2020	Apr	0.6%	1.4%
THUR	JN	Machine Tool Orders y/y	14-May-2020	Apr P	-48.3	-40.7%
FRI/SAT	CH	Industrial Production y/y	15-May-2020	Apr	3.9%	-1.1%
	CH	Retail Sales y/y	15-May-2020	Apr	-7.5%	-15.8%
	CH	Fixed Assets Ex Rural YTD y/y	15-May-2020	Apr	-10.3%	-16.1%
	US	Retail Sales Ex Auto and Gas	15-May-2020	Apr	–	-2.8%
	US	Industrial Production m/m	15-May-2020	Apr	–	-5.4%
	US	Capacity Utilization	15-May-2020	Apr	–	72.7%
	US	U. of Mich. Sentiment	15-May-2020	May P	–	71.8
	IN	Exports y/y	15-May-2020	Apr	–	-34.6%

Source: Bloomberg, Standard Chartered; key indicators highlighted in blue; *refers to Jan-Feb 2020 combined data

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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